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Takeaways from BOBCAPS Digital Conference

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- **Connected people and enterprises are shaping India's digital economy; structural drivers in place for robust, multiyear growth**
- **Foodtech, online gaming, data/cloud services and digital marketing are new frontiers of the digital economy**
- **AFFLE (BUY, TP Rs 1,390) a play on high-growth digital marketing and ECLX (BUY, TP Rs 2,880) on traditional enterprise digital transformation**

Our Digital Conference 2021 had C-suite dignitaries from Affle India (AFFLE), eClerx (ECLX), ESDS, Games 24*7, Big Basket and Mindtree (MTCL) who threw light on the evolving digital landscape. Key insights:

Large internet economy opportunity: India's internet economy is booming, which has buoyed the gaming and foodtech segments in particular. Key drivers behind the growing demand for internet-based companies are: (1) low penetration (e-grocery at 0.5%, e-commerce at 7%), (2) increased consumerism leading to more product categories, (3) the highest millennial and Gen Z population in the world, (4) rising demand for anytime-anywhere services, and (5) growing smartphone usage.

India emerging as new gaming frontier: India's gaming market is currently at the level that China's was in 2012. The high attachment rate of users, network effect and large young population are spurring growth. While the Indian audience likes classic games, e-sports are on the rise as well. Games 24*7 has carved a niche for itself as the No. 1 card gaming platform in the country with full-stack offerings that differentiate it from competition.

Foodtech growth aided by attractive value proposition: Price, convenience and assortment are key growth drivers in foodtech. Indian consumers are currently at the convenience stage. Product bundling and complimentary services are vital to achieving profitability in the delivery business. E-grocery is the only segment which provides access to a loyal older demographic.

Data centre business on the uptrend: ESDS, the oldest data centre company in India, emphasize relationship and pricing or deal commercials as key criteria to win business in India. It expects financial capital Mumbai to be the prime data centre location in India as most cable networks land in the city. ESDS largely caters to Indian clients, who are typically price sensitive, and has seen a vast increase in network density in recent months due to demand for cloud services. The boom in core banking digitisation, which was not even 10% of banking pre-Covid, has opened up various avenues for growth.

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Key conference takeaways

Affle India – BUY, TP Rs 1,390

We hosted AFFLE CFO Kapil Bhutani at our Digital Conference.

- The company delivered a landmark performance in Q2FY22 and management expects an industry-leading 25-30% revenue CAGR in the next 3-5 years.
- Digital marketing market size in developed markets are expected to grow at 8-10% YoY and developing markets at 25-30% CAGR for the next 3-5 years.
- AFFLE will focus on emerging markets and on the entertainment and edtech verticals.
- About 80% of the company's revenue comes from Android-dominated markets. In the Apple ecosystem, even if a consumer has given the requisite permissions to just a single app, it is enough for AFFLE to send targeted digital marketing advertisements.
- Q2FY22 saw integration of the JAMPP acquisition for the first time. JAMPP operates on IoS and has the US as part of its geography mix. Hence, revenue from iOS is also growing.
- Management plans to acquire companies that are struggling with profitability if their turnaround looks feasible.

eClerx – BUY, TP Rs 2,880

We hosted ECLX CFO Rohitash Gupta. Rohitash has been with ECLX as CFO since 2011.

- ECLX is a BPM firm that offers support in two areas: (1) customer experience and (2) domain-intensive services that provide efficiencies (specially to banking clients). The company primarily has three verticals: (1) digital, (2) customer experience, and (3) financial markets. Going ahead, revenue from automation and AI is expected to improve across verticals.
- The top-10 clients currently contribute 60% of revenue, which is the company's lowest concentration ever. Most clients are US-based and come from the banking and online retail space. The last five years have been choppy for the company, marked by flat revenue and contracting margins. However, growth has picked up during the last four quarters and ECLX is also seeing a much lower churn rate. Growth in top-10 clients has worked well by selling concentric/adjacent services in accounts that were already doing well.
- In the financial markets category, the company is heavily focused on capital markets – mostly mid-to-back-office work. It brings automation, AI and robotics domain knowledge to fintech clients. In financial markets, it transforms CMI, documentation, billing and brokerage work. Five years ago, most tasks were efficiency-related but now the focus is on regulation compliance.

- ECLX has been conducting consumer behaviour analytics and marketing support over the last five years. Marketing operations relate to backend activities and chat support for ecommerce websites. The company has opened onshore delivery centres as well.
- The consulting business is 5-6 years old and entails digital consulting and financial market consultancy for regulation compliance. This business was affected during Covid-19 but is now regaining traction.
- ECLX has a 60-90-day no-rolloff contract with clients which reduces some risk. While rolloffs are sometimes unavoidable, management believes its consulting focus, onshoring, automation and managed services will help combat the risk.
- Historically, Q1 and Q2 are peak attrition quarters. However, the Q2FY22 print was lower than that in 2018-19. ECLX has two categories of people: (1) those who plan, design, run, automate and metricize processes (20%) and (2) execution staff (80%). For the 20% staff, performance bonuses work well as a retention measure. Attrition remains high for the balance 80% but the cycle of fulfilling vacancies has reduced. BPO staff is easily hirable and not much planning is required.
- CLX is a creative studio which has seen stable growth over several years.
- Offshore work is done at the Mumbai centre.
- Margins should be stable. Mass return to office may bring in some additional cost.

ESDS – Not Rated

We hosted Piyush Somani – MD and Chairman of ESDS Software Solution.

- Data centres in India are usually in Mumbai with Bengaluru being the second-most preferred location. Mumbai is important because it is the country's financial capital and a majority of network cables land in the city. The fibre network laid in Mumbai is also very robust with large bandwidth. In addition, the city has multiple utility companies providing electricity which ensures steady power supply.
- Data centres are classified into tier-I, II, III and IV categories. A tier-I centre has no redundancy. Tier-III has n+1 levels while tier-IV has the most redundancy (n+n). The higher the redundancy, the lower the chances of failure. In India, very few customers opt for tier-IV centres given their high pricing.
- A tier-III data centre requires Rs 0.6-1mn of investment per rack (physical steel and electronic framework designed to house servers, networking devices, cables and other computing equipment) and Rs 1.3mn toward non-IT infrastructure. ESDS puts up racks of very high intensity. Hence, 10 racks cost it ~Rs 250mn. Over a period of five years, a customer earns 4x ROI from cloud infrastructure.
- Currently most data centres in India are run by American or international companies. ESDS's Indian location and its ownership of the end-to-end customer journey is its USP. Managed services is a competitive space for the company.
- ESDS plans to grow organically in future.

Games 24*7 – Not Rated

We hosted Rahul Tewari who has been CFO at Games 24*7 for roughly two years now.

- India's gaming industry is currently where China's was in 2012 and is expected to follow a non-linear growth path in coming years. There are currently over 400mn registered gamers in the country (largest addressable market across world) and monetisation levels are likely to increase. Gaming content is highly personalised which also drives its non-linear growth.
- India recorded 7.3bn gaming downloads in 9MCY20, which is higher than even the US, making it a key emerging market.
- Games 24*7 is a full-stack gaming platform that is seeing 20-25% YoY growth. Its key competitors are MPL, Nazara Technologies, Dream11 ,123 and Octro. Unlike Games 24*7, none of them provide all segments of gaming, i.e. online rummy, fantasy sports, casual gaming and casual RMG (real money games). Games 24*7's intuitive user experience consists of an integrated app and common wallet which limits downtime and increases liquidity.
- The company's Rummy Circle has good ARPU and retention. Its USP is liquidity (faster availability of table).
- Growth potential is the highest in casual games which are monetised through low-cost in-app purchases. Advertisement revenue is fairly low.
- ARPU acceleration is a good indication of how cohorts are behaving on the platform.
- Viral adoption on Games 24*7 has been aided by its A-list brand ambassadors.
- The company owns Ultimate Games which is the second largest casual gaming studio in India. Rummy and Teen Patti are a part of this studio.

Expert foodtech panel

The expert foodtech panel at our Digital Conference comprised (1) a senior executive from one of India's leading e-Grocery companies, (2) Santanu Mitra, MD of Digital Economy Group at DBS Bank, and (3) Sachin Mittal, Senior VP at DBS Bank.

- E-commerce is preferred to physical stores because of pricing, convenience and assortment. India has moved up from the pricing stage of evolution to the convenience stage. The next phase will be assortment – for instance, a typical apparel store can have only 800 SKUs while ecommerce websites can provide 5,000-6,000 SKUs in every size.
- Boundaries between the food and grocery delivery businesses are getting blurred. E-grocery is a much less economical business as the wait time is longer. E-commerce players have less incentive to get into grocery delivery whereas food delivery players have more incentive to get into groceries as they operate within a squeezed timeline at peak hours in any case.

- By CY25, the Indian e-groceries market is expected to reach US$ 40bn-50bn. Video recipes are increasing sales for e-groceries. Consumers watching upstream content can be targeted for sales.
- A unique feature of the food delivery business is that it is a high-frequency service. It also penetrates the older demographic which is more loyal. Food delivery plus e-wallets makes for a unique, attractive proposition that translates to everyday app usage. This helps in garnering advertisement revenue as advertisers get access to customers on a daily basis. Take rate - e-commerce parlance is the commission fee charged by a marketplace for a transaction it facilitates on its platform – are also healthy in India.
- Southeast Asia has a 7% take rate. In India, food delivery has a reasonable ~20%+ take rate. India is a very low ASP market. Hence, profitability depends on increasing basket size and using margin levers efficiently. Tie-ups with fintech, advertisements and offering peripheral services are key to achieving profitability.
- The instant (super-quick) delivery model is questionable as logistics remains a problem. In super-quick mode, a delivery partner is catering to just one person at a time. Hence, upselling and raising basket size are important to attain profitability.
- Consolidation will occur in the Indian e-grocery industry but prolonged competition is likely to continue for the next 4-5 years. Players with the best execution and best customer experience will survive.
- Fintechs are using customer data for targeted advertisements.

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BUY – Expected return >+15%

HOLD – Expected return from -6% to +15%

SELL – Expected return <-6%

Note: Recommendation structure changed with effect from 21 June 2021

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