BOBCAPS
TRUST | INNOVATION | EXCELLENCE

FIRST LIGHT

12 August 2020

RESEARCH

[Initiation] VST Tillers Tractors | Target: Rs 1,800 | +20% | BUY

Power tillers to steer growth – initiate with BUY

BOB Economics Research | Monthly Chartbook

India to recover with a lag

BOB Economics Research | IIP

IIP showing signs of recovery

V-Mart Retail | Target: Rs 1,665 | –7% | SELL

Lockdown blues; near-term outlook remains murky

SUMMARY

VST Tillers Tractors

We believe VST Tillers Tractors (VSTT) is poised for strong growth given its market leadership in power tillers (~50% market share), ready capacity, focused growth in tractors and debt-free status. Import curbs on Chinese tillers (~30% market share) from Jul'20 are expected to fuel a 40% YoY spike in VSTT's tiller volumes for FY21 and propel segmental volumes well ahead of industry, at a 19% CAGR over FY20-FY23. This coupled with tractor launches should aid a 17%/59% revenue/earnings CAGR for the company. Initiate with BUY; Sep'21 TP Rs 1,800.

Click here for the full report.

TOP PICKS

LARGE-CAP IDEAS

Company	Rating	Target
Bajaj Finance	Buy	4,000
Cipla	Buy	850
GAIL	Buy	150
Petronet LNG	Buy	305
Tech Mahindra	Buy	780

MID-CAP IDEAS

Company	Rating	Target
Alkem Labs	Buy	3,600
Chola Investment	Buy	280
Laurus Labs	Buy	1,200
Transport Corp	Buy	240
Mahanagar Gas	Sell	750

Source: BOBCAPS Research

DAILY MACRO INDICATORS

Indicator	Current	2D (%)	1M (%)	12M (%)
US 10Y yield (%)	0.58	1bps	(7bps)	(107bps)
India 10Y yield (%)	5.89	0bps	13bps	(61bps)
USD/INR	74.90	0	0.4	(5.8)
Brent Crude (US$/bbl)	27,791	1.3	6.6	7.3
Dow	3,379	0.8	(0.1)	20.0
Shanghai	38,182	0.4	4.3	1.6
Sensex	44.99	1.3	4.0	(23.2)
India FII (US$ mn)	**7 Aug**	**MTD**	**CYTD**	**FYTD**
FII-D	119.2	3.5	(14,524.2)	(4,764.7)
FII-E	174.3	1,342.1	54.0	6,656.9

Source: Bank of Baroda Economics Research

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India Economics: Monthly Chartbook

While global economy is showing signs of expansion with manufacturing and services PMIs above 50, India's PMIs have decelerated owing to local lockdowns in Jul'20. Rural economy is the bright spot with higher tractor sales and kharif sowing. Agri exports are also increasing. On the other hand, state government capex is down by 44% which implies weak investment outlook. Even with a weak growth outlook, RBI could not cut policy rates as inflation is above its tolerance band of 6%. Seems the easing cycle is behind and government spending will have to continue to revive domestic economy. Thus we expect yields to remain in 5.5-6% range in near-term.

Click here for the full report.

India Economics: IIP

India's industrial output declined by 16.6% in Jun'20 as against a decline of 33.9% in May'20. After a span of six months, FMCG output reported a positive growth of 14%. Capital goods, consumer durables, construction and intermediate goods did report lower pace of contraction, which is encouraging. While PMI for Jul'20 has decelerated, a few other indicators are pointing to underlying recovery. Notably, we do expect a weak state government capex which implies muted investment spending in the near-term.

Click here for the full report.

V-Mart Retail

V-Mart Retail (VMART) reported a below-expected Q1FY21 – revenue plunged 83% YoY to Rs 781mn as SSSg dropped 85% in a lockdown-hit quarter. The company reported an operating loss of Rs 296mn (adj. for Ind-AS 116) stemming from negative operating leverage, which resulted in a pre-tax loss of Rs 384mn. Management is hopeful of recovery in Q3 led by the festival/ marriage season and onset of winter. We slash our FY21 PAT estimate by 56% and roll over to a revised Sep'21 TP of Rs 1,665 (vs. Rs 1,630). Maintain SELL.

Click here for the full report.

INITIATING COVERAGE

BUY
TP: Rs 1,800 | ⮝ 20%

V.S.T TILLERS TRACTORS | Automobiles | 11 August 2020

Power tillers to steer growth – initiate with BUY

We believe VST Tillers Tractors (VSTT) is poised for strong growth given its market leadership in power tillers (~50% market share), ready capacity, focused growth in tractors and debt-free status. Import curbs on Chinese tillers (~30% market share) from Jul'20 are expected to fuel a 40% YoY spike in VSTT's tiller volumes for FY21 and propel segmental volumes well ahead of industry, at a 19% CAGR over FY20-FY23. This coupled with tractor launches should aid a 17%/59% revenue/earnings CAGR for the company. Initiate with BUY; Sep'21 TP Rs 1,800.

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Import curbs to reinforce dominance in power tillers: VSTT leads the power tiller market in India with ~50% share. In Jul'20, the Indian government imposed import restrictions on Chinese tillers that currently command ~30% of the market and account for 50% of units imported annually. In the base case, we estimate that these curbs will give VSTT access to demand for >6,500 tillers in FY21, over and above the growth expected from a buoyant rural sector. We thus model for an 19% volume CAGR in the company's tiller segment for FY20-FY23 vs. 9% for industry. Tiller capacity stands at 60,000 units p.a. and FY20 utilisation was 32%.

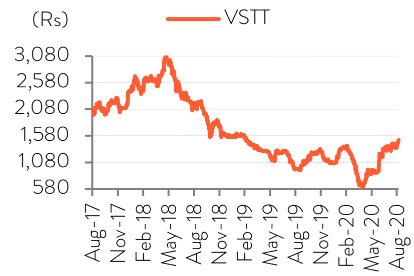
Going strong in tractors: VSTT's current capacity stands at 36,000 units p.a. and it sold ~7,150 tractors in FY20, implying capacity utilisation of ~20%. The company launched a 27hp tractor in Jan'20, extending its footprint across the compact segment. We expect an 8% volume CAGR in the tractor business over FY20-FY23 (vs. –2% for FY16-FY20), led by the new product launch and anticipated healthy rural income.

Initiate with BUY: We are positive on VSTT given its strong FCF, debt-free balance sheet, and demand impetus from power tiller import curbs. Revenue/ EBITDA/PAT are forecast to log a robust CAGR of 17%/72%/59% over FY20-FY23. We value the stock at 23x Sep'22E EPS to arrive at our TP of Rs 1,800.

Ticker/Price	VSTT IN/Rs 1,497
Market cap	US$ 174.5mn
Shares o/s	9mn
3M ADV	US$ 0.7mn
52wk high/low	Rs 1,550/Rs 588
Promoter/FPI/DII	55%/5%/15%

Source: NSE

STOCK PERFORMANCE



Source: NSE

KEY FINANCIALS

Y/E 31 Mar	FY19A	FY20A	FY21E	FY22E	FY23E
Total revenue (Rs mn)	6,148	5,437	6,997	7,821	8,671
EBITDA (Rs mn)	461	175	604	783	882
Adj. net profit (Rs mn)	461	180	504	642	721
Adj. EPS (Rs)	53.3	20.9	58.4	74.3	83.4
Adj. EPS growth (%)	(58.9)	(60.9)	179.9	27.3	12.2
Adj. ROAE (%)	7.8	3.1	8.1	9.6	10.0
Adj. P/E (x)	28.1	71.8	25.6	20.1	17.9
EV/EBITDA (x)	27.9	74.3	21.2	16.3	14.5

Source: Company, BOBCAPS Research

India to recover with a lag

While global economy is showing signs of expansion with manufacturing and services PMIs above 50, India's PMIs have decelerated owing to local lockdowns in Jul'20. Rural economy is the bright spot with higher tractor sales and kharif sowing. Agri exports are also increasing. On the other hand, state government capex is down by 44% which implies weak investment outlook.Even with a weak growth outlook, RBI could not cut policy rates as inflation is above its tolerance band of 6%. Seems the easing cycle is behind and government spending will have to continue to revive domestic economy. Thus we expect yields to remain in 5.5-6% range in near-term.

Cautious recovery: While electronic imports, passenger car sales, E-way bills and electricity demand are showing signs of improvement, manufacturing and serivces PMI, diesel consumption and state government revenues are still decelerating. Consumer demand is likely to remain weak as seen in RBI's consumer confidence index which plummeted to a record low of 53.8 in Jul'20 (63.7 in May'20). However, rural demand is likely to be better given the normal monsoon and accelerated sowing.

Central spending robust: In Q1FY21 centre's overall spending rose by 13.1% compared with 2% increase seen last year. The surge was driven by 40% jump in capex (-27.6% last year) and 10.5% increase in revenue spending (6.1% last year). Higher spending was seen by Ministries of Roads, Finance and Agriculture. This was achieved despite continued decline in centre's net receipts (-47.3%). States' spending in Apr-May'20 has also been higher (6.5%) compared with last year (-0.4%), but was supported only by revenue spending (9.5% versus 4.1%). State capex remains badly hit (-44% versus 0.4%). With market borrowings of states lower in Jul'20, we expect spending to cool off.

Higher inflation binds RBI: With inflation remaining above RBI's tolerance band of 6%, RBI maintained policy rates. The current available data suggests CPI is likely to be elevated in Jul'20 as well. This is on account of higher vegetable prices (especially potato and tomato) and higher retail prices of petrol and diesel owing to rise in local taxes. Thus, 10Y yield has also risen by 5bps since policy. Given the inflation outlook, we believe the rate cut cycle is behind us unless growth deteriorates from current estimated trajectory.

INR consolidates gains: INR rose by 0.9% in Jul'20 building on gain of 0.1% in Jun'20. This was on the back of FII inflows of US$ 1bn in the equity segment as well as a weaker dollar (DXY index fell by 4.2% in Jul'20 on MoM basis) even though oil prices inched up in the month. EM currencies too rose by 1.4%. INR is likely to see an appreciating bias led by several factors such as: 1) weaker dollar, 2) rangebound oil prices, 3) resumption in foreign inflows, and 4) lower trade deficit.

IIP

11 August 2020

IIP showing signs of recovery

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India's industrial output declined by 16.6% in Jun'20 as against a decline of 33.9% in May'20. After a span of six months, FMCG output reported a positive growth of 14%. Capital goods, consumer durables, construction and intermediate goods did report lower pace of contraction, which is encouraging. While PMI for Jul'20 has decelerated, a few other indicators are pointing to underlying recovery. Notably, we do expect a weak state government capex which implies muted investment spending in the near-term.

KEY HIGHLIGHTS

- IIP growth fell at a slower pace of 16.6% in Jun'20.
- Pace of decline moderated mainly in manufacturing.
- We expect slower pace of deceleration in the coming months, as domestic and global economy reopens.

IIP a tad better: Industrial output fell at a slower pace of 16.6% in Jun'20 versus a decline of 33.9% in May'20. While mining output continued to see a visible contraction of 19.8% in Jun'20 versus 20.5% in May'20, manufacturing output witnessed an improvement with pace of decline now at 17.1% versus 38.4% in May'20. Electricity output too reported a decline of 10% versus 14.9% in May'20. This translates into 35.9% drop in industrial activity in Q1FY21 compared with 3.8% decline in Q4FY20 and a 3% increase in Q1 last year. Q2FY21 might have started on a weaker footing. Manufacturing PMI has eased in Jul'20 to 46 from 47.2 in Jun'20. While we expect contraction to continue in the coming months, the pace of decline will be lower.

FMCG output expands: FMCG goods output rose sharply (after 6 consecutive months of decline) by 14% in Jun'20 from a decline of 11.1% in May'20. Consumer durables output declined at a slower pace of 35.5% against 69.4% in May'20. So was the case with capital goods which declined by 36.9% against 65.2% in May'20. Even construction goods saw a recovery with a decline of 21.3% from 40.7% in May'20. Intermediate goods production also fell at a slower pace of 25.1% against 40.6% in May'20.

Modest recovery may be visible: We see a modest recovery playing out in coming months as visible in improvement in electricity demand (8% contraction in Jul'20 against 13.6% decline in Jun'20), E-way bills (48.4mn in Jul'20 against 43.4mn in Jun'20) and auto sales (18.6% decline against 43% in Jun'20). However, further improvement may require unlocking of remaining parts of the economy such as travel, hospitality and entertainment. This is likely to normalise with a lag. In addition, given the sharp decline in capex by states, we believe investment demand will remain weak in the near-term.

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SELL
TP: Rs 1,665 | ⮟ 7%

V-MART RETAIL | Retail | 11 August 2020

Lockdown blues; near-term outlook remains murky

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V-Mart Retail (VMART) reported a below-expected Q1FY21 – revenue plunged 83% YoY to Rs 781mn as SSSg dropped 85% in a lockdown-hit quarter. The company reported an operating loss of Rs 296mn (adj. for Ind-AS 116) stemming from negative operating leverage, which resulted in a pre-tax loss of Rs 384mn. Management is hopeful of recovery in Q3 led by the festival/ marriage season and onset of winter. We slash our FY21 PAT estimate by 56% and roll over to a revised Sep'21 TP of Rs 1,665 (vs. Rs 1,630). Maintain SELL.

Lockdown dents revenue growth: VMART's revenue declined 83% YoY as same-store sales growth (SSSg) slumped 85% (volume SSSg down 84%). Per management, stores were open only for ~34% of days during the quarter which affected sales. The company continues to face operational challenges, with just ~75% of stores currently running due to localised lockdowns in many areas. Management expects demand to improve from Q3FY21 as the festival, marriage and winter seasons set in.

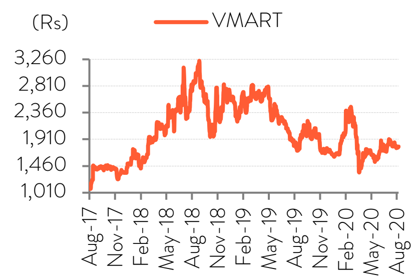
Steep operating loss: VMART reported an operating loss of Rs 296mn (adjusted for Ind-AS 116) due to negative operating leverage as sales plummeted, resulting in a pre-tax loss of Rs 384mn. The company has undertaken various cost control measures to cushion margins, such as rental renegotiation and employee cost rationalisation which should result in potential savings of ~Rs 180mn and ~Rs 300mn respectively in FY21.

Maintain SELL: We slash our FY21 earnings estimate by 56% (and pare FY22/FY23 forecasts by 3% each) due to continued Covid-19 headwinds, particularly in markets where VMART operates. On rollover, our TP stands revised to Rs 1,665 (from Rs 1,630) – we continue to value the stock at a 30x one-year forward P/E multiple and retain our SELL rating.

Ticker/Price	VMART IN/Rs 1,786
Market cap	US$ 434.4mn
Shares o/s	18mn
3M ADV	US$ 0.5mn
52wk high/low	Rs 2,545/Rs 1,200
Promoter/FPI/DII	51%/23%/26%

Source: NSE

STOCK PERFORMANCE



Source: NSE

KEY FINANCIALS

Y/E 31 Mar	FY19A	FY20P	FY21E	FY22E	FY23E
Total revenue (Rs mn)	14,337	16,620	13,336	21,158	25,772
EBITDA (Rs mn)	1,336	2,138	1,719	2,946	3,618
Adj. net profit (Rs mn)	724	493	151	901	1,120
Adj. EPS (Rs)	39.9	27.2	8.3	49.6	61.7
Adj. EPS growth (%)	(5.8)	(31.8)	(69.5)	497.9	24.3
Adj. ROAE (%)	19.1	11.4	3.2	17.5	18.3
Adj. P/E (x)	44.8	65.7	215.1	36.0	28.9
EV/EBITDA (x)	23.9	14.9	18.7	10.7	8.5

Source: Company, BOBCAPS Research

Disclaimer

Recommendations and Absolute returns (%) over 12 months

BUY – Expected return >+15%

ADD – Expected return from >+5% to +15%

REDUCE – Expected return from -5% to +5%

SELL – Expected return <-5%

Note: Recommendation structure changed with effect from 1 January 2018 (Hold rating discontinued and replaced by Add / Reduce)

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