FIRST LIGHT

13 July 2020

RESEARCH

Reliance Industries | Target: Rs 1,820 | –3% | REDUCE

Earnings yet to justify rerating - cut to REDUCE

BOB Economics Research | IIP

First signs of recovery

SUMMARY

Reliance Industries

Reliance Industries' (RIL) diversification edge has shone during the pandemic as it grapples with a difficult environment for its cyclical and retail businesses, while enhancing RJio's earnings outlook (across verticals). Commendably, RIL has been able to garner US$ 17bn through stake sales in Jio Platforms and the rights issue. The focus will now be on earnings. As the company positions itself as an Oil-to-Tech behemoth, valuations have run well ahead at 15.5x FY23E EPS. Cut to REDUCE (from ADD) with a new Mar'21 TP of Rs 1,820 (vs. Rs 1,515).

Click here for the full report.

India Economics: IIP

India's industrial output declined by 34.7% in May'20 as against a decline of 57.6% in Apr'20. While recovery in FMCG goods is encouraging, capital and durable goods continue to show steep declines. Discretionary and investment demand will recover with a lag. However, broader economic activity is improving as seen in higher manufacturing PMI, electricity demand and E-Way bill generation in Jun'20. We see further improvement in activity in coming months, though rising COVID cases imply risks of local shutdowns.

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TOP PICKS

LARGE-CAP IDEAS

Company	Rating	Target
Bajaj Finance	Buy	3,000
Cipla	Buy	690
GAIL	Buy	150
Petronet LNG	Buy	305
Tech Mahindra	Buy	690

MID-CAP IDEAS

Company	Rating	Target
Alkem Labs	Buy	2,950
Chola Investment	Buy	200
Laurus Labs	Buy	630
Transport Corp	Buy	240
Mahanagar Gas	Sell	710

Source: BOBCAPS Research

DAILY MACRO INDICATORS

Indicator	Current	2D (%)	1M (%)	12M (%)
US 10Y yield (%)	0.61	(5bps)	(26bps)	(152bps)
India 10Y yield (%)	5.77	(1bps)	(4bps)	(72bps)
USD/INR	75.00	0	0.7	(9.6)
Brent Crude (US$/bbl)	42.35	(2.2)	3.8	(36.3)
Dow	25,706	(1.4)	(6.8)	(5.1)
Shanghai	3,451	1.4	17.5	18.3
Sensex	36,738	1.1	6.9	(5.4)
India FII (US$ mn)	**08 Jul**	**MTD**	**CYTD**	**FYTD**
FII-D	34.2	149.0	(14,133.0)	(4,373.5)
FII-E	(141.2)	(483.8)	(2,925.3)	3,677.7

Source: Bank of Baroda Economics Research

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BOBCAPS
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REDUCE
TP: Rs 1,820 | ∀ 3%

RELIANCE INDUSTRIES | Oil & Gas | 10 July 2020

Earnings yet to justify rerating – cut to REDUCE

Reliance Industries' (RIL) diversification edge has shone during the pandemic as it grapples with a difficult environment for its cyclical and retail businesses, while enhancing RJio's earnings outlook (across verticals). Commendably, RIL has been able to garner US$ 17bn through stake sales in Jio Platforms and the rights issue. The focus will now be on earnings. As the company positions itself as an Oil-to-Tech behemoth, valuations have run well ahead at 15.5x FY23E EPS. Cut to REDUCE (from ADD) with a new Mar'21 TP of Rs 1,820 (vs. Rs 1,515).

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RJio leading earnings and valuation upsurge: Our sanguine outlook on RJIO is based on ARPU expansion to Rs 170 by FY23 (from the current Rs 130) even as subscriber accretion slows. We see multiple levers for ARPU expansion – higher data usage coupled with staggered data tariff hikes, rising FTTH subscribers, and monetisation of lateral offerings (such as JioTV and JioCinema).

Retail momentum to sustain: We expect retail revenues to surge to Rs 3.4tn by FY23. Economies of scale would aid an estimated 3.6x surge in EBITDA to Rs 348bn by FY23 (from Rs 96bn in FY20).

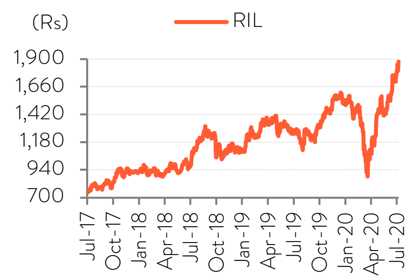
Cyclicals expected to struggle: Unrelenting oil demand concerns stemming from the pandemic continue to drive benchmark GRMs lower. Similarly, Petrochemical margins could struggle, as global economic takes a toll on demand for products. We see more downside risk to cyclical earnings.

Deleveraging priced in, upsides capped; cut to REDUCE: We need to see earnings traction from RIL, especially in RJio. We raise FY21/FY22 earnings estimates by 15%/5% to factor in better RJio earnings and lower debt, yielding a revised Mar'21 TP of Rs 1,820 (from Rs 1,515). Pressure in the cyclical (with downside risk to earnings) and retail segments caps valuation upsides.

Ticker/Price	RIL IN/Rs 1,878
Market cap	US$ 168.8bn
Shares o/s	6,762mn
3M ADV	US$ 432.3mn
52wk high/low	Rs 1,885/Rs 876
Promoter/FPI/DII	50%/24%/26%

Source: NSE

STOCK PERFORMANCE



Source: NSE

KEY FINANCIALS

Y/E 31 Mar	FY19A	FY20A	FY21E	FY22E	FY23E
Total revenue (Rs mn)	5,830,940	6,116,450	3,785,945	4,775,147	4,584,413
EBITDA (Rs mn)	841,670	882,170	938,561	1,393,498	1,709,815
Adj. net profit (Rs mn)	400,860	443,240	484,596	795,924	1,072,479
Adj. EPS (Rs)	59.3	65.6	71.7	117.7	158.6
Adj. EPS growth (%)	13.6	10.6	9.3	64.2	34.7
Adj. ROAE (%)	11.7	11.1	10.5	14.2	16.5
Adj. P/E (x)	31.7	28.6	26.2	16.0	11.8
EV/EBITDA (x)	17.3	16.9	16.4	10.9	8.7

Source: Company, BOBCAPS Research

IIP

10 July 2020

First signs of recovery

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India's industrial output declined by 34.7% in May'20 as against a decline of 57.6% in Apr'20. While recovery in FMCG goods is encouraging, capital and durable goods continue to show steep declines. Discretionary and investment demand will recover with a lag. However, broader economic activity is improving as seen in higher manufacturing PMI, electricity demand and E-Way bill generation in Jun'20. We see further improvement in activity in coming months, though rising COVID cases imply risks of local shutdowns.

KEY HIGHLIGHTS

- IIP growth declined at a slower pace of 34.7% in May'20.
- Pace of decline moderated across the board.
- With gradual removal of restrictions, industrial activity will gain momentum.

IIP contracts: Industrial output declined at a slower pace of 34.7% in May'20 from 57.6% in Apr'20. This was led by contraction in manufacturing which dropped by 39.3% from 67.1% in Apr'20, followed by mining at 21% from 27% in Apr'20. Electricity output too declined at a much slower pace of 15.4% in May'20 from 23% in Apr'20. Early signs of recovery can be seen across other indicators too with gradual improvement in manufacturing PMI to 47.2 in Jun'20 indicating a pickup in economic activity. Even export growth rebounded and improved to 36.5% in May'20 from 60.3% in Apr'20. In Q1FY21 so far (Apr-May'20), industrial growth has declined by 46.2% owing to lockdown imposed due to COVID-19 pandemic versus a decrease of 3.6% in Q4FY20.

Capital and durables goods continue to see steep decline: While capital goods output declined at a slower pace of 64.3% in May'20 as against 92.6%, it was still a steep decline. So is the case with durable goods which contracted by 68.5% in May'20 from a decline of 96% in Apr'20. On the other hand, FMCG goods reported a decline of 11.7% in May'20 as against 48.7% in Apr'20. Even construction goods saw a recovery with a decline of 42% from 84.7% in Apr'20. Intermediate goods production also fell at a slower pace of 44% in May'20 from 65.4% in Apr'20.

Industrial output to recover gradually: With the gradual removal of restrictions, improvement in mobility indices and re-opening up of businesses, industrial production is likely to improve further. Overall pickup in economic activity is further visible with slower pace of decline in both electricity demand (13.6% in Jun'20 from 21.4% in May'20) and E-way bills (12.7% decline in Jun'20 from 53% in May'20). However, uncertainty over COVID-19 vaccine and a possible surge in cases leading to local lockdowns remains a downside risk to this recovery.

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

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

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