BOBCAPS
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FIRST LIGHT

15 July 2019

RESEARCH

BOB Economics Research | Inflation and IIP

Inflations inches up, IIP moderates

Infosys | Target: Rs 820 | +13% | ADD

Impressive deal wins; risks to operating margins ahead

IndusInd Bank | Target: Rs 1,850 | +23% | BUY

No major surprises

Pharmaceuticals | Q1FY20 Preview

Good Q1 for Sun, Alkem, Dr Reddy's; stabilising for Cipla, Lupin

SUMMARY

India Economics: Inflation and IIP

CPI inflation rose to 8-month high of 3.2% in Jun'19 led by food inflation, in particular pulses, meat and fish. Industrial activity, on the other hand, moderated to 3.1% in May'19. With drop in sown area this year, pulses prices and thus food inflation is expected to increase. However, core inflation is likely to moderate (4.1% in Jun'19). In FY20, CPI inflation will be within RBI's target of 4%. A slowing global and domestic economy along with fiscal consolidation implies room for 25 bps rate cut in Aug'19.

Click here **for the full report.**

Infosys

Infosys (INFO) reported a largely in-line Q1FY20 operating performance, with 2.8% QoQ CC revenue growth and 20.5% EBIT margins. At US$ 2.7bn, the company notched up its highest quarterly deal wins, which supported upbeat revenue guidance for FY20. Though strong deal wins and guidance lay the ground for healthy growth momentum, margin management could be a challenge given elevated attrition and tight staff cost control. We tweak FY20/FY21 EPS by –2%/–1%; on rollover to Jun'20, our TP remains at Rs 820.

Click here **for the full report.**

TOP PICKS

LARGE-CAP IDEAS

Company	Rating	Target
Cipla	Buy	630
GAIL*	Buy	245
ONGC	Buy	230
TCS	Add	2,360
HPCL	Sell	210

*GAIL target price is adjusted for the 1:1 bonus issue

MID-CAP IDEAS

Company	Rating	Target
Balkrishna Ind	Buy	1,290
Future Supply	Buy	780
Greenply Industries	Buy	245
Laurus Labs	Buy	495
PNC Infratech	Buy	235

Source: BOBCAPS Research

DAILY MACRO INDICATORS

Indicator	Current	2D (%)	1M (%)	12M (%)
US 10Y yield (%)	2.14	8bps	(1bps)	(71bps)
India 10Y yield (%)	6.49	(5bps)	(58bps)	(129bps)
USD/INR	68.44	0.2	1.7	0.2
Brent Crude (US$/bbl)	66.52	(0.7)	6.8	(10.7)
Dow	27,088	0.8	3.9	8.7
Shanghai	2,918	0.1	2.3	2.8
Sensex	38,823	0.7	(2.4)	6.2
India FII (US$ mn)	**10 Jul**	**MTD**	**CYTD**	**FYTD**
FII-D	(75.2)	877.5	2,305.8	1,761.2
FII-E	(67.1)	(611.0)	10,727.9	3,882.7

Source: Bank of Baroda Economics Research

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IndusInd Bank

IndusInd Bank (IIB) has reported consolidated numbers for Q1FY20 post-merger with Bharat Financial (BHAFIN). PAT at Rs 14bn (+38% YoY) beat estimates largely due to below-expected provisions. Exposure to potentially stressed groups declined to 1.67% of loans vs. 1.9% in Q4FY19, while SMA-2 loans halved to 0.17%. Loan growth at 28% YoY remained in line with Q4 despite the merger, as BHAFIN had tightened lending norms in a few states. The bank is opening 40-50k savings accounts of BHAFIN customers each day.

Click here for the full report.

Pharmaceuticals: Q1FY20 Preview

We expect a strong quarter for SUNP (boosted by one-time US generic supplies) and DRRD (full quarter of gSuboxone, ramp-up in new launches incl. gPropofol, Isotretinoin, and cost savings). Cipla/LPC should see stabilising quarter after a high US base from gSensipar/ gRanexa stocking. Alkem's EBITDA is forecast to grow 11-12% YoY, while ARBP (Ertapenem competition), DIVI and Laurus could see a lacklustre Q1. The avg USD/INR is Rs 69.5 (vs. 70.5 QoQ) while BRL & ZAR has depreciated ~5% vs. INR.

Click here for the full report.

INFLATION AND IIP

12 July 2019

Inflation inches up, IIP moderates

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CPI inflation rose to 8-month high of 3.2% in Jun'19 led by food inflation, in particular pulses, meat and fish. Industrial activity, on the other hand, moderated to 3.1% in May'19. With drop in sown area this year, pulses prices and thus food inflation is expected to increase. However, core inflation is likely to moderate (4.1% in Jun'19). In FY20, CPI inflation will be within RBI's target of 4%. A slowing global and domestic economy along with fiscal consolidation implies room for 25 bps rate cut in Aug'19.

KEY HIGHLIGHTS

- CPI inflation rose by 3.2% in Jun'19 vs 3% in May'19.
- Core inflation cools off to 4.1% in Jun'19 vs 4.2% in May'19.
- IIP growth eases to 3.1% in May'19 from 4.3% in Apr'19.

IIP growth moderates: Industrial growth for May'19 moderated to 3.1% from 4.3% in Apr'19 on the back of deceleration in mining to 3.2% (5.1% in Apr'19) and manufacturing to 2.5% (4% in Apr'19). Within manufacturing, capital goods reported an increase of only 0.8% (1.2% in Apr'19) and consumer durables contracted by (-) 0.1%. On the other hand, FMCG production accelerated to 7.7% from 5.9% in Apr'19. Positive base effect had a role to play. Infra sector rose by 5.5% compared with 7.2% in Apr'19. Electricity production improved to a 7-month high of 7.4% in May'19 (6% in Apr'19).

Food inflation drove CPI higher: CPI inflation rose to 8-month high of 3.2% in Jun'19 from 3% in May'19 led by 30bps jump in food inflation (2.2% in Jun'19 from 1.8% in May'19). Higher food inflation was seen in meat and fish at 9% in Jun'19 (8.1% in May'19) and pulses at 5.7% in Jun'19 (2.1% in May'19). Veggie prices rose by 4.7% in Jun'19 compared to 5.5% in May'19. Given the large drop seen in sowing in pulses and oilseeds, we believe food inflation will accelerate further in the year. However, excess supply in cereals (food stocks) will ensure that food inflation remains anchored at less than 4% in FY20.

Core edged lower: Core inflation fell by 10bps to 4.1% in Jun'19 compared to 4.2% in May'19. Deceleration was visible in household goods and services at 4.3% in Jun'19 (4.6% in May'19), transport and communication at 0.7% in Jun'19 (1.6% in May'19) and recreation and amusement at 5.2% in Jun'19 (5.6% in May'19). Lower oil price (10% in Jun'19) have had a positive impact. Health and education prices continued to gain traction. Higher gold prices led to personal care inflation also inching up. Budget will also impart an inflationary impulse in the form of higher taxes on motor spirit and customs duties. However, an appreciating currency and muted demand will neutralise the impact. For the year, CPI inflation is likely to remain below RBI's target of 4%.

ADD
TP: Rs 820 | ⮝ 13%

INFOSYS | IT Services | 13 July 2019

Impressive deal wins; risks to operating margins ahead

Infosys (INFO) reported a largely in-line Q1FY20 operating performance, with 2.8% QoQ CC revenue growth and 20.5% EBIT margins. At US$ 2.7bn, the company notched up its highest quarterly deal wins, which supported upbeat revenue guidance for FY20. Though strong deal wins and guidance lay the ground for healthy growth momentum, margin management could be a challenge given elevated attrition and tight staff cost control. We tweak FY20/ FY21 EPS by –2%/–1%; on rollover to Jun'20, our TP remains at Rs 820.

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In-line operating performance: INFO reported revenues of US$ 3.1bn (+2.3% QoQ or +2.8% QoQ CC incl. 60bps tailwinds from the Stater acquisition) – slightly softer than our estimate of 3.1% QoQ CC growth but in line with consensus. EBIT margins at 20.5% (–100bps QoQ) met expectations. BFSI performance excluding the ABN AMRO deal was weak (–0.3% QoQ in dollar terms). Among verticals, communications/energy & utility led with 4.6%/4.7% QoQ dollar revenue growth. Among geographies, North America stood out with 3% QoQ dollar growth.

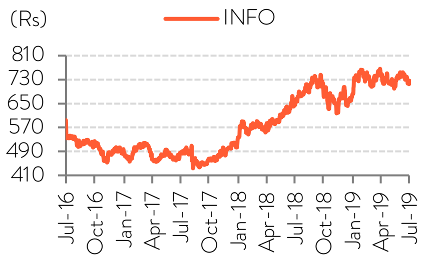
Deal wins impressive, revenue guidance revised up: Aided by the ABN AMRO contract (whose size management is yet to disclose), INFO posted its highest quarterly deal-win TCV of US$ 2.7bn. The company raised its FY20 revenue growth guidance to 8.5-10% from 7.5-9.5% earlier (in CC terms), implying a CQGR of 1.6%/1.9% at the lower/top end of the band for the rest of FY20. EBIT margin guidance was unchanged at 21-23%.

Retain ADD: With impressive deal wins and higher guidance, INFO could well close the revenue gap with TCS in FY20, especially after a soft Q1 at TCS. But in the absence of currency tailwinds, margin management could prove thorny for INFO due to its stubbornly high attrition (vs. best-in-industry levels for TCS).

Ticker/Price	INFO IN/Rs 727
Market cap	US$ 46.1bn
Shares o/s	4,349mn
3M ADV	US$ 84.9mn
52wk high/low	Rs 773/Rs 600
Promoter/FPI/DII	13%/35%/52%

Source: NSE

STOCK PERFORMANCE



Source: NSE

KEY FINANCIALS

Y/E 31 Mar	FY18A	FY19A	FY20E	FY21E	FY22E
Adj. net profit (Rs mn)	1,60,280	1,54,170	1,58,157	1,82,163	2,05,010
Adj. EPS (Rs)	36.9	35.4	36.3	41.8	47.1
Adj. EPS growth (%)	17.3	(4.0)	2.6	15.2	12.5
Adj. ROAE (%)	23.9	24.5	24.8	25.8	26.2
Adj. P/E (x)	19.7	20.5	20.0	17.4	15.4
EV/EBITDA (x)	15.4	14.2	13.9	11.6	10.3

Source: Company, BOBCAPS Research

BUY
TP: Rs 1,850 | ⮝ 23%

INDUSIND BANK | Banking | 12 July 2019

No major surprises

IndusInd Bank (IIB) has reported consolidated numbers for Q1FY20 post-merger with Bharat Financial (BHAFIN). PAT at Rs 14bn (+38% YoY) beat estimates largely due to below-expected provisions. Exposure to potentially stressed groups declined to 1.67% of loans vs. 1.9% in Q4FY19, while SMA-2 loans halved to 0.17%. Loan growth at 28% YoY remained in line with Q4 despite the merger, as BHAFIN had tightened lending norms in a few states. The bank is opening 40-50k savings accounts of BHAFIN customers each day.

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Asset quality remains manageable: GNPA increased 5bps QoQ to 2.15% in Q1, while the coverage ratio remained low at 43%. Exposure to stressed groups declined to 1.67% of loans in part due to repayments. The SMA-1 & 2 book nearly halved to 0.35%. Management asserted that SPVs of IL&FS are adequately provided for and even believes a write-back of some of these provisions is possible. FY20 credit cost guidance has been maintained at 65bps.

Loan growth in line with Q4: IIB's vehicle finance book grew ~24% YoY backed by secular growth across CVs, two-wheelers, three-wheelers and tractors. The non-vehicle finance/corporate book grew >20%/15-20%. Management continues to guide for mid-twenties growth overall in FY20.

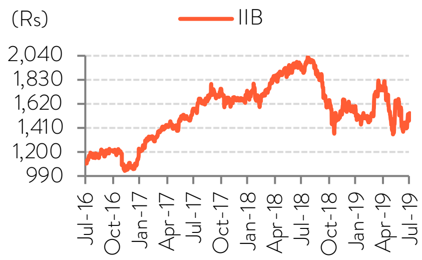
BHAFIN update: AUM at Rs 175bn grew 26% YoY in Q1 but was flat QoQ. Management has guided for 35% growth in FY20 supported by a 22-25% increase in borrowers and 10-15% rise in ticket size. In terms of liability accretion, IIB is opening 40-50k savings accounts of BHAFIN customers a day.

Maintain BUY with TP of Rs 1,850: We introduce estimates for FY22 and for post-merger financials. We continue to value the stock at 3x FY21E P/BV as merger synergies are expected to raise ROE to ~19% by FY21E.

Ticker/Price	IIB IN/Rs 1,510
Market cap	US$ 13.3bn
Shares o/s	603mn
3M ADV	US$ 98.0mn
52wk high/low	Rs 2,038/Rs 1,333
Promoter/FPI/DII	17%/52%/31%

Source: NSE

STOCK PERFORMANCE



Source: NSE

KEY FINANCIALS

Y/E 31 Mar	FY18A	FY19P	FY20E	FY21E	FY22E
Adj. net profit (Rs mn)	36,060	33,011	55,180	75,410	98,007
EPS (Rs)	60.2	54.9	84.2	106.5	138.4
P/E (x)	25.1	27.5	17.9	14.2	10.9
P/BV (x)	3.9	3.5	3.0	2.4	2.0
ROA (%)	1.8	1.3	1.7	1.8	1.9
ROE (%)	16.2	13.1	17.5	18.6	20.0

Source: Company, BOBCAPS Research

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PHARMACEUTICALS | Q1FY20 Preview | 12 July 2019

Good Q1 for Sun, Alkem, Dr Reddy's; stabilising for Cipla, Lupin

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We expect a strong quarter for SUNP (boosted by one-time US generic supplies) and DRRD (full quarter of gSuboxone, ramp-up in new launches incl. gPropofol, Isotretinoin, and cost savings). Cipla/LPC should see stabilising quarter after a high US base from gSensipar/ gRanexa stocking. Alkem's EBITDA is forecast to grow 11-12% YoY, while ARBP (Ertapenem competition), DIVI and Laurus could see a lacklustre Q1. The avg USD/INR is Rs 69.5 (vs. 70.5 QoQ) while BRL & ZAR has depreciated ~5% vs. INR.

Key to watch: (1) Alkem Labs: Onset of domestic season in Q2, trade generics, FDA update on Baddi unit. **(2) Aurobindo (ARBP):** Progress on Sandoz deal, injectable bag line and gSensipar litigation; FDA inspection update for Units 3/7. **(3) Cipla:** Updates on channel de-stocking in trade generics and softness in South African tenders. **(4) Dr Reddy's (DRRD):** Proprietary business strategy hereon, gNuvaring/Copaxone launch timelines, Srikakulam reinspection dates. **(5) Divi's (DIVI):** Uptick in gross margin QoQ, capex progress. **(6) Lupin (LPC):** Solosec ramp-up, remediation progress (Goa, Indore-2, Somerset, Mandideep units). **(7) Laurus:** Formulation offtake, gross margin QoQ. **(8) Sun Pharma (SUNP):** Ilumya ramp-up & R&D spends for new indication; Halol EIR update.

KEY RECOMMENDATIONS

Ticker	Rating
ALKEM IN	BUY
ARBP IN	BUY
CIPLA IN	BUY
DIVI IN	REDUCE
DRRD IN	REDUCE
LAURUS IN	BUY
LPC IN	ADD
SUNP IN	REDUCE

FIG 1 – Q1FY20: US REVENUE EXPECTATIONS

(US$ mn)	Q4FY18	Q1FY19	Q2FY19	Q3FY19	Q4FY19	Q1FY20E	QoQ (%)	YoY (%)
ALKEM	63	63	69	74	69	72	4.5	13.9
ARBP	272	283	318	338	352	348	(1.2)	23.0
CIPLA	104	101	108	118	162	130	(19.8)	28.2
DRRD	223	237	210	209	212	237	11.8	0.0
LPC	233	177	178	197	247	200	(19.1)	13.0
SUNP (ex-Taro)	200	225	183	186	264	270	2.5	20.0
TARO	175	155	159	176	180	171	(4.8)	10.5

Source: Company, BOBCAPS Research

FIG 2 – Q1FY20 PREVIEW: GOOD FOR SUNP, ALKEM, DRRD; STABILISING FOR CIPLA, LPC; OTHERS LACKLUSTRE

Companies	Sales (Rs mn)			EBITDA (Rs mn)			PAT (Rs mn)			EBITDA Margin (%)		
	Q1FY20E	YoY (%)	QoQ (%)	Q1FY20E	YoY (%)	QoQ (%)	Q1FY20E	YoY (%)	QoQ (%)	Q1FY20E	Q1FY19	Q4FY19
ALKEM	18,619	11.5	0.4	2,379	11.0	1.2	1,463	7.4	(12.7)	12.8	12.8	12.7
ARBP	50,379	18.5	(4.8)	10,401	33.5	(1.9)	6,384	22.0	2.2	20.6	18.3	20.0
CIPLA	42,122	6.9	(4.4)	7,969	9.5	(17.1)	3,701	0.7	0.7	18.9	18.5	21.8
DRRD	40,385	8.5	0.5	8,817	16.4	7.6	4,614	1.2	6.2	21.8	20.4	20.4
LPC	43,032	11.6	(2.3)	7,415	40.7	(15.0)	3,232	59.4	12.5	17.2	13.7	19.8
SUNP	81,827	14.6	16.2	17,875	17.5	99.2	13,047	33.0	104.3	21.8	21.3	12.7
DIVI	11,633	16.9	(7.4)	4,047	15.0	(3.2)	2,802	16.9	(5.4)	34.8	35.4	33.3
LAURUS	5,386	(0.1)	(15.2)	810	0.5	(27.6)	120	(27.5)	(72.1)	15.0	15.0	17.6
Sector Agg.	**293,383**	**12.4**	**1.5**	**59,713**	**20.4**	**11.1**	**35,364**	**21.0**	**23.7**	**20.4**	**19.0**	**18.6**

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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