BOBCAPS
TRUST | INNOVATION | EXCELLENCE

FIRST LIGHT

22 October 2019

RESEARCH

BOB Economics Research | October MPC Minutes

Growth concerns imply another 25bps cut

Reliance Industries | Target: Rs 1,670 | +18% | BUY

Cyclicals a mixed bag, RJio and Retail surge ahead

L&T Infotech | Target: Rs 2,010 | +25% | BUY

On course for a rebound

Ather Energy | NOT LISTED

Key call takeaways

Agriculture

Maharashtra's sugar production to nearly halve in 2019-20

SUMMARY

India Economics: October MPC Minutes

MPC minutes show four out of six members favour accommodative stance and further rate cuts as long as economy is firmly on the path to recovery. The remaining two are data dependent. Growth indicators such as IIP, non-food credit, exports and non-oil-non-gold imports have disappointed since the last policy. However, led by higher vegetable prices, headline inflation did touch 4%. We believe this will ebb as fresh crop arrives in the market in the next few weeks/ months. Thus another 25bps rate cut is on the cards.

Click here for the full report.

TOP PICKS

LARGE-CAP IDEAS

Company	Rating	Target
Cipla	Buy	555
GAIL	Buy	200
HPCL	Buy	400
ONGC	Buy	200
TCS	Add	2,230

MID-CAP IDEAS

Company	Rating	Target
Alkem Labs	Buy	2,230
Future Supply	Buy	730
Greenply Industries	Buy	200
Laurus Labs	Buy	480
PNC Infratech	Buy	250

Source: BOBCAPS Research

DAILY MACRO INDICATORS

Indicator	Current	2D (%)	1M (%)	12M (%)
US 10Y yield (%)	1.75	1bps	(9bps)	(143bps)
India 10Y yield (%)*	6.71	5bps	(1bps)	(120bps)
USD/INR	71.17	0.4	0.6	3.3
Brent Crude (US$/bbl)	59.91	0.8	(13.2)	(24.4)
Dow	27,026	0.1	(0.2)	6.5
Shanghai	2,977	0	(1.8)	19.7
Sensex	39,052	1.2	5.2	12.3
India FII (US$ mn)	**16 Oct**	**MTD**	**CYTD**	**FYTD**
FII-D	53.8	21.0	3,994.4	3,449.8
FII-E	125.4	560.1	8,720.8	1,875.6

Source: Bank of Baroda Economics Research | *7.26% GS 2029

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Reliance Industries

Reliance Industries' (RIL) Q2FY20 EBITDA marginally beat estimates at Rs 221bn (+5% YoY, +4% QoQ). Key Q2 highlights: (a) GRMs disappoint at US$ 9.4/bbl, (b) petchem EBITDA above estimates at Rs 89bn (–5.8% YoY) on lower operating costs and higher production, (c) retail EBITDA higher at Rs 23bn (+67% YoY), and (d) RJio EBITDA a miss at Rs 53bn (+8.5% QoQ). The earnings outlook from RIL's consumer-facing businesses remains buoyant, while GRMs could trigger an upgrade on IMO impact.

Click here for the full report.

L&T Infotech

L&T Infotech (LTI) did better than expected in Q2FY20, posting 2.4% QoQ CC revenue growth despite client-specific challenges. Management believes the worst is over and expects growth in the top account to resume from Q3, which brightens the near-term outlook. The company continues to bag large deals, adding three new clients with an aggregate TCV of US$ 100mn in Q2. Management has guided for double-digit revenue growth in FY20. We tweak estimates and reiterate BUY; on rollover to Sep'20 our TP remains at Rs 2,010.

Click here for the full report.

Ather Energy

We hosted a call with Karan Punjabi, Head of Finance at electric scooter manufacturer Ather Energy (Ather). Key takeaways: (1) sales ramp-up underway, (2) S340 model discontinued, (3) encouraging response to Chennai foray, (4) gross margin to improve, and (5) EV vs. ICE breakeven in two years.

Click here for the full report.

Agriculture

We met senior officials of the Maharashtra State Co-Operative Sugar Factories Federation (MSCSFF) which has 190 co-operative sugar mills as members. Key takeaways: (1) MSCSFF estimates that sugar production in the state will plummet to 5.5-6mn tonnes (mt) in the upcoming Oct'19-Sep'20 season vs. ~10.7mt last season (SS18-19), due to a ~30% drop in cane cropping area expected this year. (2) Output is projected to recover in SS20-21 to ~8.5mt provided monsoons are normal next year.

Click here for the full report.

OCTOBER MPC MINUTES

18 October 2019

Growth concerns imply another 25bps cut

MPC minutes show four out of six members favour accommodative stance and further rate cuts as long as economy is firmly on the path to recovery. The remaining two are data dependent. Growth indicators such as IIP, non-food credit, exports and non-oil-non-gold imports have disappointed since the last policy. However, led by higher vegetable prices, headline inflation did touch 4%. We believe this will ebb as fresh crop arrives in the market in the next few weeks/ months. Thus another 25bps rate cut is on the cards.

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Growth faltering: MPC members noted that growth momentum has slowed further since the last policy meeting as seen in most high-frequency indicators and RBI's forward looking surveys. Q1 GVA growth slipped to 4.9% with manufacturing at 0.6%. GDP growth was at 5% with consumption at 3.6%. Thus output gap has widened further. This drove the decision to cut rates by 25bps. MPC members welcomed government's recent measures to boost growth and provide liquidity to NBFCs. Cut in corporate tax stands out. On balance, the MPC was of the view that government measures along with better transmission of rates (repo-linked) and a revival in rural demand will result in a cyclical recovery in growth in H2FY20.

Inflation outlook benign: MPC members opined that inflation is expected to be well anchored within MPC's target of 4%. The increase in headline inflation is driven by higher food prices. Core inflation has been trending down because of slowdown in the economy. Seasonal spike in food prices will ebb because above normal monsoon will result in adequate Rabi output. RBI had estimated Q2 CPI inflation at 3.4%. Actual is 3.5% as CPI inflation in Sep'19 increased to 4% led by accelerating food inflation which is mostly seasonal in nature rather than structural and thus should not change RBI's view.

More rate cuts on the card: Persistent negative output gap along with a benign inflation outlook warrant accommodative monetary stance and further cut in policy rate. Four out of six MPC members favour not only continuation of an accommodative stance, but also further reduction in policy rate to kickstart the economy. Two of them (Dr. Chetan Ghate and Dr. Pami Dua) are more inclined towards a data dependent approach. For them, Oct'19 inflation print and Q2FY20 GDP data to be released on 29 Nov'19 will set the framework for policy action. We believe another 25bps rate cut is due.

KEY HIGHLIGHTS

- Growth to remain weak in Q2 led by both domestic and global factors.
- Inflation expected to remain under RBI's target.
- RBI to cut rates further by 25bps to support growth.

BUY
TP: Rs 1,670 | ⮝ 18%

RELIANCE INDUSTRIES | Oil & Gas | 21 October 2019

Cyclicals a mixed bag, RJio and Retail surge ahead

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Reliance Industries' (RIL) Q2FY20 EBITDA marginally beat estimates at Rs 221bn (+5% YoY, +4% QoQ). Key Q2 highlights: (a) GRMs disappoint at US$ 9.4/bbl, (b) petchem EBITDA above estimates at Rs 89bn (–5.8% YoY) on lower operating costs and higher production, (c) retail EBITDA higher at Rs 23bn (+67% YoY), and (d) RJio EBITDA a miss at Rs 53bn (+8.5% QoQ). The earnings outlook from RIL's consumer-facing businesses remains buoyant, while GRMs could trigger an upgrade on IMO impact.

Cyclicals EBITDA contribution shrinks: In a mixed Q2, GRMs underperformed at US$ 9.4/bbl while petchem earnings outperformed. Management did not put out clear guidance on GRMs in the runup to IMO regulations, given declining global oil demand. Oil-to-chemicals (refining + petchem) EBITDA contribution shrank to ~65% vs. 72% YoY. Petchem production scaled up to 9.9mmt, a historical quarterly high; EBITDA margins beat estimates, likely led by lower operating costs as gross margins stayed soft on global demand concerns.

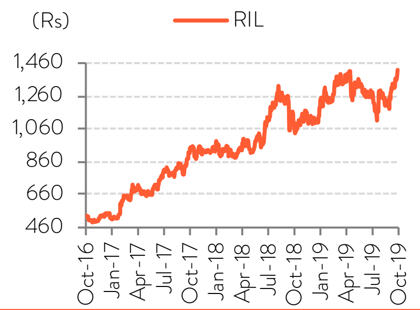
Consumer-facing businesses continue to uplift earnings: RJio subscriber additions sustained traction, touching 355mn, but ARPU was below estimates at Rs 120 – this led to below-expected EBITDA at Rs 53bn (+49% YoY). ARPU could improve from Q3FY20 (by ~Rs 15) following recently imposed billing rates for voice, with an intent to recover IUC charges. Retail EBITDA surged to Rs 23.2bn (+67% YoY) led by core margins of 8.9% (+130bps YoY).

Maintain BUY: We raise our Sep'20 TP to Rs 1,670 (from Rs 1,500) on higher EBITDA assumptions for RJio and Retail. We also factor in benefits from deleveraging over FY21/FY22 (~Rs 130/sh). RIL's management has clarified that its deleveraging targets are not contingent on the Saudi Aramco deal.

Ticker/Price	RIL IN/Rs 1,416
Market cap	US$ 126.2bn
Shares o/s	6,339mn
3M ADV	US$ 176.5mn
52wk high/low	Rs 1,428/Rs 1,016
Promoter/FPI/DII	47%/24%/28%

Source: NSE

STOCK PERFORMANCE



Source: NSE

KEY FINANCIALS

Y/E 31 Mar	FY18A	FY19A	FY20E	FY21E	FY22E
Total revenue (Rs mn)	4,082,650	5,810,200	5,425,940	6,074,031	5,997,696
EBITDA (Rs mn)	641,760	839,180	954,653	1,275,572	1,620,862
Adj. net profit (Rs mn)	352,869	398,370	446,560	648,349	899,527
Adj. EPS (Rs)	59.6	67.2	70.4	102.3	141.9
Adj. EPS growth (%)	17.4	12.8	4.8	45.2	38.7
Adj. ROAE (%)	12.7	11.7	11.0	14.1	16.9
Adj. P/E (x)	23.8	21.1	20.1	13.8	10.0
EV/EBITDA (x)	17.1	12.8	12.2	9.4	6.7

Source: Company, BOBCAPS Research

RESULT REVIEW

BUY TP: Rs 2,010 | ⮝ 25%	L&T INFOTECH	IT Services	18 October 2019

On course for a rebound

L&T Infotech (LTI) did better than expected in Q2FY20, posting 2.4% QoQ CC revenue growth despite client-specific challenges. Management believes the worst is over and expects growth in the top account to resume from Q3, which brightens the near-term outlook. The company continues to bag large deals, adding three new clients with an aggregate TCV of US$ 100mn in Q2. Management has guided for double-digit revenue growth in FY20. We tweak estimates and reiterate BUY; on rollover to Sep'20 our TP remains at Rs 2,010.

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Above-expected Q2: LTI reported a beat on revenues, growing at 2.4% QoQ CC vs. 1.4% estimated in Q2FY20. EBIT margins were largely in line at 15.5%, down 40bps QoQ.

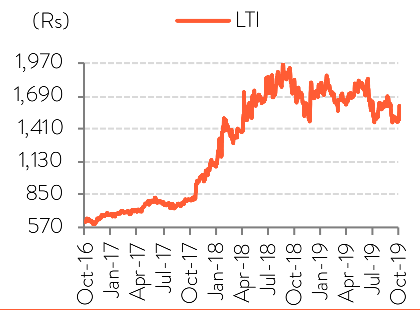
Client-specific challenges abating: After two quarters of decline, revenue from the top 5 clients returned to positive territory (+3.4% QoQ in dollar terms). Management indicated that the top client account (a drag on growth for the last two quarters) should witness a growth recovery from Q3FY20. Similarly, the hi-tech vertical is also guided to resume its growth trajectory from Q3, after headwinds from the loss of an account in Q2. Non-top 20 client revenue (+5% QoQ in dollar terms) continued to grow ahead of companywide growth.

Stellar deal signings: LTI maintained its streak of large deal wins, adding three new logos with an aggregate TCV of US$ 100mn during the quarter. H1FY20 net new deal TCV increased by 37% YoY to US$ 144mn, lending visibility for growth in H2. Management has guided for double-digit revenue growth in FY20 and retained the net margin guidance at 14-15%.

Ticker/Price	LTI IN/Rs 1,611
Market cap	US$ 4.0bn
Shares o/s	175mn
3M ADV	US$ 2.6mn
52wk high/low	Rs 1,897/Rs 1,436
Promoter/FPI/DII	75%/8%/10%

Source: NSE

STOCK PERFORMANCE



Source: NSE

KEY FINANCIALS

Y/E 31 Mar	FY18A	FY19A	FY20E	FY21E	FY22E
Total revenue (Rs mn)	73,064	94,458	1,03,286	1,14,878	1,28,327
EBITDA (Rs mn)	11,875	18,835	19,232	22,606	25,252
Adj. net profit (Rs mn)	11,124	15,157	15,082	17,613	19,002
Adj. EPS (Rs)	63.5	86.5	85.9	100.3	108.3
Adj. EPS growth (%)	(8.2)	36.1	(0.6)	16.8	7.9
Adj. ROAE (%)	31.8	34.6	28.3	28.1	25.9
Adj. P/E (x)	25.4	18.6	18.7	16.1	14.9
EV/EBITDA (x)	23.4	14.8	14.4	12.0	10.4

Source: Company, BOBCAPS Research

NOT LISTED

ATHER ENERGY | Automobiles | 18 October 2019

Key call takeaways

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We hosted a call with Karan Punjabi, Head of Finance at electric scooter manufacturer Ather Energy (Ather). Following are the key call takeaways:

Sales ramp-up underway: Ather currently sells 250-300 electric scooters per month (peak of ~400 units), lower than the company's initial expectations given supply-side constraints. Management expects to ramp this run-rate up to 400-500 units in the next few months. The company has sold a total of 2,000 units to date. Current plant utilisation stands at ~20%.

S340 model discontinued: Ather recently discontinued one of its scooter variants, the S340, as the order booking trend showed that close to 95% of customers opted for the premium S450 model. In addition, with the reduction in GST rates, pricing of the S450 has reduced to Rs 113k, closely matching that of the S340.

Encouraging response to Chennai foray: The company entered into Chennai in Jul'19, its second market after Bengaluru. Management stated that the response was encouraging (1,000+ bookings) and comparable to its Bengaluru launch.

Gross margin to improve: Ather currently operates at a negative gross margin but expects this to improve over the next 3-4 months with scale and engineering-related upgrades.

EV vs. ICE breakeven in two years: According to management, the running cost for its scooters is 30-40p/km as against Rs 2.2-2.5/km for a conventional (ICE) scooter. Based on an average run of 20km/day, breakeven on cost of ownership can typically be achieved at 15,000km (~2 years).

Battery cost continues to fall: The battery cost of electric two-wheelers continues to fall as industry volumes scale up. The long-term view that battery cost should come down below US$ 100/KwH stands, but timelines for the same remain unsure.

Financing of vehicles still low: In Ather's experience, ~20% of vehicles are bought on finance/lease. Insurance cover is provided by new-age companies such as Godigit. As volumes scale up, management expects the larger incumbents to also enter the space.

AGRICULTURE

18 October 2019

Maharashtra's sugar production to nearly halve in 2019-20

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We met senior officials of the Maharashtra State Co-Operative Sugar Factories Federation (MSCSFF) which has 190 co-operative sugar mills operating in the state as members. Key takeaways:

- MSCSFF estimates that sugar production in Maharashtra for the upcoming Oct'19-Sep'20 season will plummet to 5.5-6mn tonnes (mt) vs. ~10.7mt in the last marketing season (SS18-19).
- The lower production forecast for Maharashtra is primarily due to a ~30% drop in cane cropping area expected this year, at 770,000-780,000ha, owing to the below normal monsoons last year.
- Sugar output is projected to recover in SS20-21 to ~8.5mt provided the monsoons are normal during Jun-Oct'20. High reservoir water availability in the current year should bolster cane sowing.
- Sugar recovery in Maharashtra stood at 11.26% of cane crushed during SS18-19 and is expected to be at 11.1-11.2% in the upcoming season.
- Crushing operations in the state are expected to begin with a delay, in mid-November vs. the third week of Oct'18, due to lower sugarcane availability.
- Prices of the sweetener in Maharashtra are currently at Rs 31-31.5/kg (S-grade) and have stayed around these levels for the last few months.
- India can export ~4.5mt in SS19-20 (vs ~3.8mt in SS18-19) which will enable it to reduce excess inventory.
- Maharashtra's export quota for the upcoming season is ~1.8mt (vs. 1.55mt in SS18-19) and should be fully met, as was the case last season.
- Sugarcane is one of the most profitable crops for farmers that has assured offtake and payment cycles; hence, it will continue to be a preferred crop.
- Cane arrears due from millers to farmers in the state total ~Rs 3.3bn.
- Capex toward ethanol capacity addition looks difficult in the near term due to the stretched balance sheets of co-operatives in Maharashtra.
- Maharashtra has requested the Central government to increase the MSP (minimum selling price) of sugar from the current Rs 31/kg so that the profitability of companies can improve.

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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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