BOBCAPS
TRUST | INNOVATION | EXCELLENCE

FIRST LIGHT

08 August 2019

RESEARCH

HCL Technologies | Target: Rs 1,230 | +20% | BUY
Organic growth trending up; upgrade to BUY on cheap valuations

Pidilite Industries | Target: Rs 1,120 | –13% | SELL
In-line quarter; cut to SELL on rich valuations

BOB Economics Research | Monetary Policy Review
Unconventional rate cut

Mayur Uniquoters | Target: Rs 330 | +51% | BUY
Auto demand slump, margin contraction mar Q1

Cipla | Target: Rs 595 | +15% | BUY
Core EBITDA miss; recovery ahead

Hindustan Petroleum Corp | Target: Rs 200 | –18% | SELL
Near-term outlook remains bleak

SUMMARY

HCL Technologies

A strong revenue beat (+4.2% QoQ CC vs. +1.8% est.) but below-expected margins rounded off an in-line operating performance from HCL Tech (HCLT) for the Jun'19 quarter. Management's robust FY20 outlook is intact at 14-16% CC growth, albeit now baking in stronger organic revenues. In our view, valuations at 13.7x/12.1x FY20E/FY21E P/E are attractive, carrying 20% upside at our revised Jun'20 TP of Rs 1,230 (vs. Rs 1,260). Upgrade from ADD to BUY.

Click here for the full report.

TOP PICKS

LARGE-CAP IDEAS

Company	Rating	Target
Cipla	Buy	595
GAIL*	Buy	245
ONGC	Buy	230
TCS	Add	2,360
HPCL	Sell	200

*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	715
Greenply Industries	Buy	245
Laurus Labs	Buy	480
PNC Infratech	Buy	235

Source: BOBCAPS Research

DAILY MACRO INDICATORS

Indicator	Current	2D (%)	1M (%)	12M (%)
US 10Y yield (%)	1.70	(1bps)	(35bps)	(127bps)
India 10Y yield (%)	6.34	(5bps)	(23bps)	(145bps)
USD/INR	70.83	(0.1)	(3.2)	(3.1)
Brent Crude (US$/bbl)	58.94	(1.5)	(8.1)	(21.0)
Dow	26,030	1.2	(2.9)	1.6
Shanghai	2,778	(1.6)	(5.3)	(0.1)
Sensex	36,977	0.8	(4.5)	(1.8)
India FII (US$ mn)	**5 Aug**	**MTD**	**CYTD**	**FYTD**
FII-D	(15.0)	(29.5)	2,624.4	2,079.8
FII-E	(308.6)	(893.9)	8,510.7	1,665.5

Source: Bank of Baroda Economics Research

BOBCAPS Research
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Pidilite Industries

Pidilite Industries (PIDI) reported in-line consolidated Q1FY20 revenue growth of 10% YoY, aided by a 6% rise in consumer & bazaar (CBP) volumes. A 120bps increase in operating margins to 22% drove EBITDA/PAT growth of 16%/23% YoY. Management expects margins to remain favourable in light of benign RM prices, but indicated that demand conditions are challenging. We find valuations expensive at 48x FY21E P/E and thus downgrade the stock to SELL from REDUCE. Rolling forward, we have a new Jun'20 TP of Rs 1,120 (vs. Rs 1,080).

Click here **for the full report.**

India Economics: Monetary Policy Review

RBI surprised with a 35bps reduction in policy rates (4-2 vote) while maintaining an accommodative stance. Two MPC members voted for 25bps change. RBI has indicated room to further cut rates as it looks at closing the negative output gap. While RBI expects growth at 6.9% in FY20 (6.8% in FY19), recent indicators suggest growth will be lower. Thus RBI will be in a position to cut repo rate further by 40bps in the financial year to support growth as inflation outlook remains favourable.

Click here **for the full report.**

Mayur Uniquoters

Mayur Uniquoters' (MUNI) Q1FY20 standalone revenue decreased 9% YoY as a sharp slowdown in footwear and auto sector demand saw volumes drop 9%. Standalone operating margins plummeted 710bps YoY to 19.6% due to higher RM cost and other expenses, inducing EBITDA/PAT declines of 33%/38% YoY. We cut FY20/FY21 PAT estimates by 18%/14% and reset our target P/E from 20x to 15x to bake in the bleak near-term demand outlook. Rolling valuations forward, we have a Jun'20 TP of Rs 330 (Rs 490 earlier).

Click here **for the full report.**

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Cipla

Q1 was subdued and had multiple moving parts: (1) reduction in India GRx business by Rs 2bn, (2) Rs 1.6bn sales deferral in India Rx + EM market, (3) gSensipar sales worth US$40mn, and (4) weak ROW commentary. India business is likely to stabilise by Q3, and Rs 1.6bn of deferred sales should be recovered from Q2. Adj. EBITDA for Sensipar missed estimates by 12% but base margins improved QoQ following diffusion in the trade GRx business. We cut FY20/FY21 EPS by 7-8% and revise TP to Rs 595 (vs. Rs 630).

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Hindustan Petroleum Corp

HPCL's Q1FY20 earnings at Rs 8.1bn (–52% YoY) came in below estimates, marred by low GRMs (US$ 0.75/bbl, after US$ 2.6/bbl inventory loss). Marketing segment EBITDA at Rs 20.3bn (–27% YoY) was in line. We trim FY20 earnings by 3.7% on reduced GRM assumptions. A challenging macro environment for cyclicals exposes less efficient refiners to earnings shocks, offsetting gains from low oil prices. Our SOTP-based TP changes to Rs 200 (from Rs 210) as we roll forward to Sep'21 valuations. Maintain SELL.

Click here for the full report.

BUY
TP: Rs 1,230 | ^ 20%

HCL TECHNOLOGIES | IT Services | 08 August 2019

Organic growth trending up; upgrade to BUY on cheap valuations

A strong revenue beat (+4.2% QoQ CC vs. +1.8% est.) but below-expected margins rounded off an in-line operating performance from HCL Tech (HCLT) for the Jun'19 quarter. Management's robust FY20 outlook is intact at 14-16% CC growth, albeit now baking in stronger organic revenues. In our view, valuations at 13.7x/12.1x FY20E/FY21E P/E are attractive, carrying 20% upside at our revised Jun'20 TP of Rs 1,230 (vs. Rs 1,260). Upgrade from ADD to BUY.

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Strong revenue beat: HCLT's Q1FY20 revenues at US$ 2.4bn increased by 3.8% QoQ or 4.2% QoQ CC vs. our/consensus estimates of ~1.8% QoQ CC growth. We note that HCLT is the only name amongst tier-I IT services peers to report a revenue beat in Q1. EBIT margins at 17.1% contracted 190bps QoQ vs. our estimate of a 130bps QoQ decline, impacted by currency headwinds, visa costs, transition costs and lower profitability in the ERS (engineering and R&D services) business.

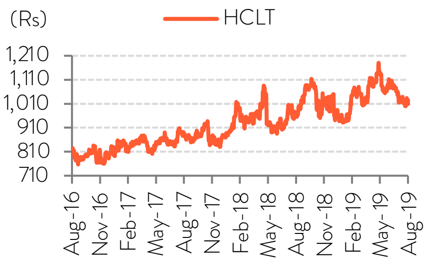
Organic growth trending higher: HCLT posted 3.8% QoQ CC (14% YoY CC) organic growth, ahead of our/consensus estimates of ~1.3% QoQ CC growth. The improved organic revenue traction will make up for loss of inorganic revenue in FY20 due to a one-month delay in IBM product deal consummation (negative impact of 60-80bps YoY). Thus, the unchanged FY20 revenue guidance of 14-16% CC growth now implies higher organic growth compared to the earlier guided 9-11% CC range.

Upgrade to BUY: We trim our FY20/FY21 EPS estimates by 5%/6% on account of higher tax rate assumptions and a lower currency reset. Rolling valuations forward, we move to a revised Jun'20 TP of Rs 1,230 (vs. Rs 1,260 earlier) and upgrade the stock to BUY on attractive valuations.

Ticker/Price	HCLT IN/Rs 1,023
Market cap	US$ 19.6bn
Shares o/s	1,357mn
3M ADV	US$ 25.3mn
52wk high/low	Rs 1,188/Rs 920
Promoter/FPI/DII	60%/27%/13%

Source: NSE

STOCK PERFORMANCE



Source: NSE

KEY FINANCIALS

Y/E 31 Mar	FY18A	FY19A	FY20E	FY21E	FY22E
Adj. net profit (Rs mn)	87,820	1,01,450	1,01,348	1,14,864	1,30,038
Adj. EPS (Rs)	63.0	74.6	74.7	84.7	95.8
Adj. EPS growth (%)	5.4	18.3	0.2	13.3	13.2
Adj. ROAE (%)	25.0	25.8	22.8	23.0	23.1
Adj. P/E (x)	16.2	13.7	13.7	12.1	10.7
EV/EBITDA (x)	12.1	9.8	8.2	6.8	5.9

Source: Company, BOBCAPS Research

RESULT REVIEW

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SELL
TP: Rs 1,120 | ⋎ 13%

PIDILITE INDUSTRIES | Construction Materials | 07 August 2019

In-line quarter; cut to SELL on rich valuations

Pidilite Industries (PIDI) reported in-line consolidated Q1FY20 revenue growth of 10% YoY, aided by a 6% rise in consumer & bazaar (CBP) volumes. A 120bps increase in operating margins to 22% drove EBITDA/PAT growth of 16%/23% YoY. Management expects margins to remain favourable in light of benign RM prices, but indicated that demand conditions are challenging. We find valuations expensive at 48x FY21E P/E and thus downgrade the stock to SELL from REDUCE. Rolling forward, we have a new Jun'20 TP of Rs 1,120 (vs. Rs 1,080).

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Modest revenue growth: PIDI's consolidated Q1 revenues grew 10% YoY to Rs 20.2bn, with 11.3% constant currency growth in overseas subsidiaries. Standalone revenues increased 10.6% YoY to Rs 17.8bn, backed by volume growth of 11% (6% in the CBP segment and 12% in industrial segment). Management has indicated that demand conditions remain challenging, but the company is countering this by expanding its product portfolio and extending its direct distribution reach to small towns.

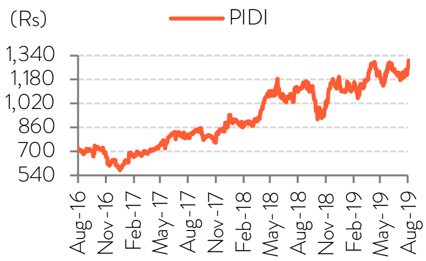
Margin trends favourable: Consolidated operating margins swelled 120bps YoY to 22% as higher gross margins (+86bps) and lower other expenses (–110bps) mitigated the impact of increased employee expenses (+80bps). EBITDA/PAT for the quarter grew 16%/23% YoY. Gross margins expanded as raw material prices softened. Management expects the favourable margin trends to hold as RM prices remain benign in Q2.

Downgrade to SELL on expensive valuations: While we like PIDI for its strong franchise and broad portfolio, valuations at 48x FY21E P/E look rich, especially against the backdrop of weakening demand. Downgrade to SELL from REDUCE with a revised Jun'20 TP of Rs 1,120 (earlier Rs 1,080), set at 40x one-year forward P/E.

Ticker/Price	PIDI IN/Rs 1,290
Market cap	US$ 9.3bn
Shares o/s	508mn
3M ADV	US$ 10.7mn
52wk high/low	Rs 1,324/Rs 895
Promoter/FPI/DII	70%/11%/19%

Source: NSE

STOCK PERFORMANCE



Source: NSE

KEY FINANCIALS

Y/E 31 Mar	FY18A	FY19A	FY20E	FY21E	FY22E
Adj. net profit (Rs mn)	9,159	8,901	11,669	13,648	15,830
Adj. EPS (Rs)	18.0	17.5	23.0	26.9	31.2
Adj. EPS growth (%)	7.5	(2.9)	31.1	17.0	16.0
Adj. ROAE (%)	26.0	23.1	26.1	26.4	26.5
Adj. P/E (x)	71.5	73.6	56.1	48.0	41.4
EV/EBITDA (x)	48.9	47.9	36.6	31.5	27.5

Source: Company, BOBCAPS Research

MONETARY POLICY REVIEW

07 August 2019

Unconventional rate cut

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RBI surprised with a 35bps reduction in policy rates (4-2 vote) while maintaining an accommodative stance. Two MPC members voted for 25bps change. RBI has indicated room to further cut rates as it looks at closing the negative output gap. While RBI expects growth at 6.9% in FY20 (6.8% in FY19), recent indicators suggest growth will be lower. Thus RBI will be in a position to cut repo rate further by 40bps in the financial year to support growth as inflation outlook remains favourable.

KEY HIGHLIGHTS

- RBI cuts repo rate by 35bps, stance remains accommodative.
- Inflation projection retained at 3.3% for FY20.
- GDP forecast revised lower at 6.9% for FY20 from 7.0% earlier.

Unconventional rate cut of 35bps: With a 4-2 vote, RBI reduced policy rate by 35bps instead of its convention of changing the same in multiples of 25bps. Two members voted to reduce rate by 25bps. Stance continues to remain accommodative in-line with surplus liquidity conditions with the banks.

FY20 growth forecast at 6.9% from 7%: RBI reduced its GDP forecast for FY20 to 6.9% (5.8-6.6% in H1FY20, 7.3-7.5% in H2FY20) with risks tilted to the downside as global economic activity is expected to weaken further. Hence, exports are likely to be muted. Even domestic consumption and investment activity has decelerated. Rural spending is muted as sowing is behind normal levels. Credit availability has impacted consumption and investment demand which in turn has led to lower production. Surplus liquidity conditions are favourable for credit availability with a lag.

Inflation to remain below 4%: While food inflation is likely to increase led by vegetables and pulses, higher food grain stocks give comfort. Crude oil prices are unlikely to move up as global growth is decelerating. Core inflation is expected to remain muted as firms will have limited pricing power when demand is low. Hence, RBI expects CPI inflation at 3.1% and 3.5-3.7% in Q2FY20 and H2FY20 respectively. In Q1FY21 inflation is expected at 3.6%. Our CPI forecast remains at 3.5% and 3.7% for FY20 and FY21.

Rate cuts to continue: Given the domestic and global growth dynamics, we believe GDP growth will be lower at 6.5%. This implies a widening output gap. In RBI's view, the benign inflation outlook provides headroom for policy action to close the negative output gap. Hence, we continue to expect repo rate to move to 5% in the financial year which is in-line with global narrative of central banks taking over the mantle to support growth.

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BUY
TP: Rs 330 | ⮝ 51%

MAYUR UNIQUOTERS | Textiles | 07 August 2019

Auto demand slump, margin contraction mar Q1

Mayur Uniquoters' (MUNI) Q1FY20 standalone revenue decreased 9% YoY as a sharp slowdown in footwear and auto sector demand saw volumes drop 9%. Standalone operating margins plummeted 710bps YoY to 19.6% due to higher RM cost and other expenses, inducing EBITDA/PAT declines of 33%/38% YoY. We cut FY20/FY21 PAT estimates by 18%/14% and reset our target P/E from 20x to 15x to bake in the bleak near-term demand outlook. Rolling valuations forward, we have a Jun'20 TP of Rs 330 (Rs 490 earlier).

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Slowdown in user industries dents revenue: MUNI reported a 9.2% YoY decline in standalone revenue to Rs 1.3bn for Q1FY20, with volumes slipping 9%. Revenues contracted across verticals, falling 10% YoY in the domestic automotive OEM segment, 25% in automotive replacement and 13% in footwear. Management stated that the near-term demand outlook was bleak and hinges on recovery in auto sales. The new PU plant will start trial production in October and commercial production from December this year.

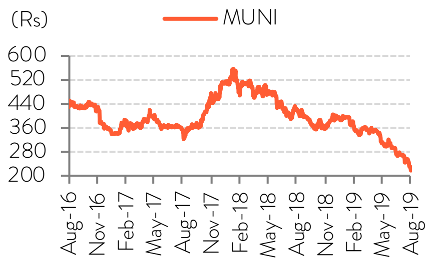
Operating margins slip: MUNI reported a 710bps drop in consolidated operating margins to 19.6%, mainly due to higher raw material cost (+408bps), employee cost (+89bps) and other expenditure (+212bps) – this dragged EBITDA/PAT down 33%/38% YoY. As per management, raw material (PVC resin) cost has spiraled 20% over the last six months and cannot be passed on in a weak market, thus hurting profitability.

Maintain BUY: We reduce FY20/FY21 PAT estimates by 18%/14% to factor in the disappointing Q1 and also cut our target one-year forward P/E multiple from 20x to 15x (25% discount to five-year average) considering near-term growth headwinds in user industries (auto, footwear). On rollover, we have a new Jun'20 TP of Rs 330 (earlier Rs 490).

Ticker/Price	MUNI IN/Rs 218
Market cap	US$ 139.5mn
Shares o/s	45mn
3M ADV	US$ 0.1mn
52wk high/low	Rs 428/Rs 211
Promoter/FPI/DII	61%/15%/24%

Source: NSE

STOCK PERFORMANCE



Source: NSE

KEY FINANCIALS

Y/E 31 Mar	FY18A	FY19P	FY20E	FY21E	FY22E
Adj. net profit (Rs mn)	905	903	751	943	1,111
Adj. EPS (Rs)	20.0	19.9	16.6	20.8	24.5
Adj. EPS growth (%)	21.9	(0.2)	(16.8)	25.5	17.8
Adj. ROAE (%)	21.7	18.7	13.8	15.6	16.5
Adj. P/E (x)	10.9	10.9	13.1	10.5	8.9
EV/EBITDA (x)	5.7	6.3	6.6	5.2	4.2

Source: Company, BOBCAPS Research

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BUY
TP: Rs 595 | ⮝ 15%

CIPLA | Pharmaceuticals | 07 August 2019

Core EBITDA miss; recovery ahead

Q1 was subdued and had multiple moving parts: (1) reduction in India GRx business by Rs 2bn, (2) Rs 1.6bn sales deferral in India Rx + EM market, (3) gSensipar sales worth US$40mn, and (4) weak ROW commentary. India business is likely to stabilise by Q3, and Rs 1.6bn of deferred sales should be recovered from Q2. Adj. EBITDA for Sensipar missed estimates by 12% but base margins improved QoQ following diffusion in the trade GRx business. We cut FY20/FY21 EPS by 7-8% and revise TP to Rs 595 (vs. Rs 630).

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Weak India, ROW and CGA sales were key negatives leading to EPS cut: India sales declined 12% YoY due to dispatch deferral of Rs 600mn in Rx and GRx destocking of Rs 2bn following a destabilisation risk at old distributors. Recovery is expected from Q3 as ramp-up from new distributors could take time. Cipla's receivable profile has improved QoQ but the lost business cannot be recouped. Deferred sales in ROW plus business challenges in the Middle East & CGA sales are other key negatives. Although part of these sales should be recovered, the annualised impact of subdued sales has led to ~7% earnings cut for FY20/ FY21 and could send the stock into time correction mode for the near term.

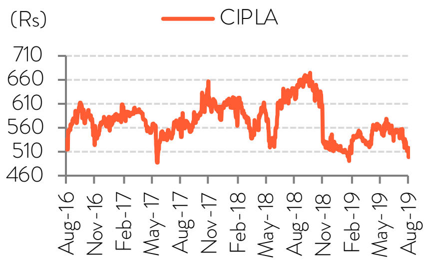
Margins improve sequentially ex-gSensipar: US sales were strong at US$ 160mn, mainly from gSensipar (US$ 40mn in our view). US base business should stabilise from Q2 following multiple generic entrants. Ex-Sensipar, we believe base business EBITDA margins/gross margins have improved ~140bps/ ~400bps QoQ following a drop in low-margin India GRx business.

Call takes: (1) Contribution from trade GRx at 16% in Q1 (23% in FY19); (2) Advair filing on track for FY20-end; (3) expect meaningful launches in US from Q3, (4) South Africa private market growth to normalise from Q2, and (5) China to be meaningful in next 3-5 years with focus on respiratory and oncology.

Ticker/Price	CIPLA IN/Rs 518
Market cap	US$ 5.9bn
Shares o/s	806mn
3M ADV	US$ 14.6mn
52wk high/low	Rs 678/Rs 484
Promoter/FPI/DII	37%/26%/13%

Source: NSE

STOCK PERFORMANCE



Source: NSE

KEY FINANCIALS

Y/E 31 Mar	FY18A	FY19A	FY20E	FY21E	FY22E
Adj. net profit (Rs mn)	12,340	13,409	15,074	16,904	19,646
Adj. EPS (Rs)	15.3	16.6	18.7	21.0	24.4
Adj. EPS growth (%)	(0.2)	8.7	12.4	12.1	16.2
Adj. ROAE (%)	8.9	9.0	9.5	9.8	10.4
Adj. P/E (x)	33.8	31.1	27.7	24.7	21.3
EV/EBITDA (x)	15.7	14.1	13.6	11.9	10.2

Source: Company, BOBCAPS Research

SELL
TP: Rs 200 | ⮟ 18%

HINDUSTAN PETROLEUM CORP | Oil & Gas | 08 August 2019

Near-term outlook remains bleak

HPCL's Q1FY20 earnings at Rs 8.1bn (–52% YoY) came in below estimates, marred by low GRMs (US$ 0.75/bbl, after US$ 2.6/bbl inventory loss). Marketing segment EBITDA at Rs 20.3bn (–27% YoY) was in line. We trim FY20 earnings by 3.7% on reduced GRM assumptions. A challenging macro environment for cyclicals exposes less efficient refiners to earnings shocks, offsetting gains from low oil prices. Our SOTP-based TP changes to Rs 200 (from Rs 210) as we roll forward to Sep'21 valuations. Maintain SELL.

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GRMs underperform on surprise inventory loss: HPCL's reported GRMs at US$ 0.75/bbl were well below estimates due to an inventory loss of US$ 2.6/bbl. While Singapore GRMs have recovered to ~US$ 6/bbl in Jul'19, negative light-heavy crude spreads limit HPCL's capability to improve its margins. We cut FY20E GRMs to US$ 5/bbl but remain constructive on the outlook over FY21-FY22 (maintaining our estimates at US$ 6/bbl), anticipating benefits from IMO regulations starting in CY20.

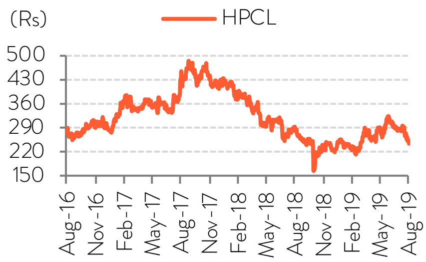
Marketing business earnings normalise: Earnings from the marketing business matched estimates at Rs 20.3bn. Though down 61% QoQ, this was to be expected as margins normalised. HPCL's dependence on marketing business EBITDA surged to >60% in Q1FY20, raising the risk profile of earnings as this business is sensitive to political intervention (IOCL being the least sensitive among OMCs).

Maintain SELL: At 5x FY21E EPS, HPCL's valuations may seem undemanding, but high reliance on marketing segment earnings remains a major concern in a politically sensitive climate and could negate gains from the recent decline in oil prices. GRM underperformance amid the global slowdown also remains a key risk to earnings.

Ticker/Price	HPCL IN/Rs 244
Market cap	US$ 5.3bn
Shares o/s	1,524mn
3M ADV	US$ 23.0mn
52wk high/low	Rs 334/Rs 163
Promoter/FPI/DII	51%/19%/30%

Source: NSE

STOCK PERFORMANCE



Source: NSE

KEY FINANCIALS

Y/E 31 Mar	FY18A	FY19A	FY20E	FY21E	FY22E
Adj. net profit (Rs mn)	72,183	66,900	59,176	61,882	74,128
Adj. EPS (Rs)	47.4	43.9	38.8	40.6	48.6
Adj. EPS growth (%)	(12.4)	(7.3)	(11.5)	4.6	19.8
Adj. ROAE (%)	31.0	23.9	18.5	17.6	19.1
Adj. P/E (x)	5.2	5.6	6.3	6.0	5.0
EV/EBITDA (x)	6.0	5.6	8.4	9.1	8.1

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)

Rating distribution

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