BOBCAPS
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FIRST LIGHT

16 April 2020

RESEARCH

BOB Economics Research | Wholesale Inflation
WPI slips

BOB Economics Research | Trade
Trade contraction shows impact of lockdown

Wipro | Target: Rs 170 | –9% | SELL
Weak quarter; guidance and dividends suspended

Transport Corp of India | Target: Rs 255 | +47% | BUY
Fundamentals intact, valuations compelling

Petronet LNG | Target: Rs 330 | +57% | BUY
Resilient earnings from long-term contracts

Banking | Q4FY20 Preview
Limited lockdown impact in Q4

Building Materials | Q4FY20 Preview
Expect an insipid quarter

Automobiles
Yongda call takeaways: China luxury car demand on the rebound

SUMMARY

India Economics: Wholesale Inflation

WPI inflation moderated to a 4-month low of 1% in Mar'20 from 2.3% in Feb'20. This was led by lower food inflation which eased to 5.5% in Mar'20 from 7.3% in Feb'20 and Fuel & Power inflation. With decline seen in international oil prices this month, we expect WPI to ease further. Food prices may also decelerate once restrictions on movement of goods are lifted in a phased manner. We anticipate growth to fall to 1.5% in FY21 and CPI inflation at 3.8% which gives RBI room to lower rates by another 50bps.

Click here for the full report.

TOP PICKS

LARGE-CAP IDEAS

Company	Rating	Target
Bajaj Finance	Buy	3,000
Cipla	Buy	570
Eicher Motors	Buy	25,000
Petronet LNG	Buy	330
Reliance Industries	Buy	1,500

MID-CAP IDEAS

Company	Rating	Target
Alkem Labs	Buy	2,870
Greenply Industries	Buy	145
Laurus Labs	Buy	510
Transport Corp	Buy	255
Ashok Leyland	Sell	64

Source: BOBCAPS Research

DAILY MACRO INDICATORS

Indicator	Current	2D (%)	1M (%)	12M (%)
US 10Y yield (%)	0.75	(2bps)	(21bps)	(184bps)
India 10Y yield (%)	6.50	0bps	17bps	(90bps)
USD/INR	76.28	0	(3.2)	(9.6)
Brent Crude (US$/bbl)	29.60	(6.7)	(12.6)	(58.7)
Dow	23,950	2.4	3.3	(9.5)
Shanghai	2,827	1.6	(2.1)	(13.1)
Sensex	30,690	(1.5)	(10.0)	(21.9)
India FII (US$ mn)	**9 Apr**	**MTD**	**CYTD**	**FYTD**
FII-D	(183.1)	(751.8)	(10,511.3)	(751.8)
FII-E	246.8	358.0	(6,245.0)	358.0

Source: Bank of Baroda Economics Research

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Important disclosures, including any required research certifications, are provided at the end of this report.

India Economics: Trade

India's trade deficit remained steady at US$ 9.8bn in Mar'20 on a MoM basis. Both exports and imports came off sharply showing the impact of lockdowns. Notably, non-oil-non-gold imports fell steeply by 30.5%, posting the worst decline on record. Exports too fell across categories. Oil exports were lower due to sharp decline in prices. However, lower oil prices also imply that CAD as % of GDP will moderate further in FY21. This bodes well for INR.

Click here for the full report.

Wipro

Wipro (WPRO) reported a subpar Q4FY20 with a miss on both revenue and operating margins. The company suspended quarterly guidance citing Covid-19 uncertainties and decided not to recommend final dividend. The latter came as a negative surprise, highlighting potential vulnerability despite a healthy balance sheet. We cut FY21/FY22 EPS by 13%/14% and lower our target FY22E P/E multiple to 11x (from 13.5x) to factor in the volatile business climate – reiterate SELL with a revised Mar'21 TP of Rs 170 (vs. Rs 240 earlier).

Click here for the full report.

Transport Corp of India

Covid-19 has severely disrupted Transport Corp's (TRPC) operations across verticals. Freight and 3PL are the hardest hit while seaways is less affected. We expect a transitory spurt in demand once the lockdown is lifted, but full-fledged recovery could begin only in Q4FY21. However, TRPC's business fundamentals remain strong and we expect long-term industry trends to be favourable. We cut FY20-FY22 EPS estimates by 13-46% and lower our Mar'21 TP to Rs 255 (vs. Rs 355). Maintain BUY on attractive risk-reward post the recent correction.

Click here for the full report.

Petronet LNG

Our recent interaction with the Petronet LNG (PLNG) management deepens confidence in our core investment thesis of (a) faster recovery in utilisation levels at Dahej post lifting of the economic shutdown – as most of its consumers fall under the essential category; and (b) improved demand outlook from H2FY21 led by CGD, fertilisers and power, triggered by sustained low LNG prices (see Feb gas consumption surges). In the current uncertain climate, PLNG's ~16mmtpa of long-term contracts limit earnings downside risks. Maintain BUY.

Click here for the full report.

Banking: Q4FY20 Preview

We expect a modest fourth quarter for our banking coverage followed by a sharp credit slowdown in Q1FY21 as the lockdown impact unravels. Q4 systemic loan growth has been tepid at 6% YoY but is expected to be higher for large private banks, while asset quality should perk up across the board. Management comments on unsecured retail/SME delinquencies and moratorium impact are keenly awaited. As noted in our sector report, the top 3 private banks offer a higher margin of safety led by sturdy liability franchises, growth capital and fortified balance sheets.

Click here for the full report.

Building Materials: Q4FY20 Preview

Building material companies under our coverage are likely to post a dull Q4FY20 as tough market conditions have been further accentuated by the lockdown in end-March, thus taking a toll on volumes. We expect low single-digit volume declines for tile and plywood players. Pipe companies are likely to post a muted performance marked by flat/negative revenue YoY, excepting ASTRA which could see a 10% uptick. Management commentary on business strategies post Covid-19 will be a key monitorable.

Click here for the full report.

Automobiles

We hosted a call with China Yongda Automobile Services (Yongda), one of the leading luxury car dealers in China with over 200 outlets catering to marquee brands such as BMW, Porsche, Mercedes Benz, Audi and JLR. Key takeaways: (1) luxury car demand bouncing back faster than mass market cars, (2) luxury carmakers maintain CY20 volume targets, (3) JLR's performance on an uptrend in China, (4) strong long-term outlook for luxury vehicles in China.

Click here for the full report.

WHOLESALE INFLATION

15 April 2020

WPI slips

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WPI inflation moderated to a 4-month low of 1% in Mar'20 from 2.3% in Feb'20. This was led by lower food inflation which eased to 5.5% in Mar'20 from 7.3% in Feb'20 and Fuel & Power inflation. With decline seen in international oil prices this month, we expect WPI to ease further. Food prices may also decelerate once restrictions on movement of goods are lifted in a phased manner. We anticipate growth to fall to 1.5% in FY21 and CPI inflation at 3.8% which gives RBI room to lower rates by another 50bps.

Food inflation eases: WPI slipped to a 4-month low of 1% in Mar'20 from 2.3% in Feb'20. Food inflation eased to 5.5% in Mar'20 from 7.3% in Feb'20. This was largely led by softening of vegetable prices which increased by 11.9% in Mar'20 from 30% in Feb'20. Onion prices explain the dip. Cereal inflation dropped to almost 2-year low of 2.7% in Mar'20 from 5.2% in Feb'20 as prices of both paddy (1.7% vs 3.7% in Feb'20) and wheat (4.8% vs 6.4% in Feb'20) edged lower. Fruit prices contracted by 0.4% in Mar'20. While milk (5.4% vs 4.5% in Feb'20) prices inched up, those of eggs declined by 14.1% in Mar'20, largest fall seen in this series.

Fuel inflation down: Fuel and power inflation contracted by 1.8% in Mar'20 from an increase of 3.4% in Feb'20, as mineral oil price index declined by 8.2% compared with an increase of 1.1% in Feb'20. Coal prices remained steady while electricity prices rose by 9.9% versus 9% in Feb'20. The dip in mineral oil index can be explained by 50% decline in Mar'20 on a YoY basis versus a 14% contraction in Feb'20. We expect headline fuel inflation to moderate in Apr'20 as international oil prices have declined further on a YoY basis (MTD) on the back of faltering global demand.

Deflation in core continues: Core deflation remained unchanged from Feb'20 at 0.8% in Mar'20. Manufactured inflation eased marginally to 0.3% in Mar'20 from 0.4% in Feb'20. Of the 22 items in core index, 13 saw decrease in prices, with sharpest decrease seen in other leather items (-2.2% vs -1.4%), basic metals (-4.1% vs -3.6%) and fabricated metal products (-1.8% vs -1.3%). This is in line with global trend as international commodity prices have declined sharply in Mar'20 on a YoY basis by 13% compared with a decrease of 4.2% in Feb'20. In Apr'20, commodity prices have contracted at an even faster pace of 14.8%.

TRADE

15 April 2020

Trade contraction shows impact of lockdown

India's trade deficit remained steady at US$ 9.8bn in Mar'20 on a MoM basis. Both exports and imports came off sharply showing the impact of lockdowns. Notably, non-oil-non-gold imports fell steeply by 30.5%, posting the worst decline on record. Exports too fell across categories. Oil exports were lower due to sharp decline in prices. However, lower oil prices also imply that CAD as % of GDP will moderate further in FY21. This bodes well for INR.

Sameer Narang
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Exports nosedive: Exports fell steeply in Mar'20 by 34.6% versus an increase of 2.9% in Feb'20. During FY20 exports have contracted by 4.8% from an increase of 8.7% in FY20. In Mar'20, apart from domestic lockdown, sharp reduction in global demand also contributed to the decline. The sharpest decline was seen in engineering goods at 42.3% followed by gems & jewellery at 41% and chemicals falling by 32.9%. Oil exports too fell by 31.1% versus an increase of 10.1% in Feb'20. With countries across the world, including India, imposing lockdowns, we expect exports to remain muted in the near term due to both demand and supply conditions.

Imports fall steeply as well: Imports too plunged by 28.7% in Mar'20 versus an increase of 2.5% in Feb'20. Oil imports led the fall at 15% compared with an increase of 14.3% in Feb'20 as oil prices crashed by 49.7% in Mar'20 on a YoY basis. After showing a pickup in Jan-Feb'20, non-oil-non-gold imports fell by 30.5% registering the biggest decline on record as the COVID-19 restrictions kicked-in. Within this, imports of pearls and precious stones fell the most at 53.5%, followed by iron and steel at 45.8% and electronics at 29.1%. Capital goods imports too fell by 20% versus an increase of 7.6% in Feb'20.

Trade deficit to remain contained: India's trade deficit remained stable at US$ 9.8bn in Mar'20 (US$ 9.9bn in Feb'20) as both exports and imports fell by US$ 6bn MoM. For FY20, trade deficit narrowed to US$ 160bn from US$ 184bn in FY19 led by a drop in both oil deficit (US$ 4bn) and non-oil deficit (US$ 20bn). Exports are expected to remain tepid as global growth is likely to fall by 3% (IMF). Lockdowns in India's major export partners such as EU and US will also impinge on exports. However, range-bound oil prices and weak demand will keep imports in check. Hence, we expect trade deficit to be even lower in FY21. This should ease some pressure on INR.

KEY HIGHLIGHTS

- Exports contract by (-) 34.6% in Mar'20 compared with an increase of 2.9% in Feb'20.
- Import growth also slips to (-) 28.7% in Mar'20 versus an increase of 2.5% in Feb'20.
- Trade deficit remained stable at US$ 9.8bn versus US$ 9.9bn in Feb'20.

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SELL
TP: Rs 170 | ⮟ 9%

WIPRO | IT Services | 16 April 2020

Weak quarter; guidance and dividends suspended

Wipro (WPRO) reported a subpar Q4FY20 with a miss on both revenue and operating margins. The company suspended quarterly guidance citing Covid-19 uncertainties and decided not to recommend final dividend. The latter came as a negative surprise, highlighting potential vulnerability despite a healthy balance sheet. We cut FY21/FY22 EPS by 13%/14% and lower our target FY22E P/E multiple to 11x (from 13.5x) to factor in the volatile business climate – reiterate SELL with a revised Mar'21 TP of Rs 170 (vs. Rs 240 earlier).

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Subpar quarter: WPRO underperformed our estimates on both revenue and operating margins. IT services revenue declined 1% QoQ in US dollar terms (+0.4% QoQ CC) vs. consensus estimates of sequentially flat dollar revenues. Adjusted for US$ 14mn-16mn of Covid-led headwinds (0.7-0.8% of revenue), IT services revenue was nearer the midpoint of the company's guided range of 0-2% QoQ CC growth. Segmental EBIT margins slipped 80bps QoQ to 17.6% vs. consensus estimates of 20bps contraction.

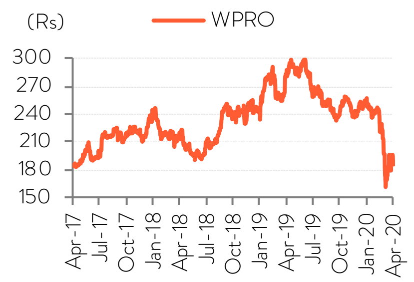
Quarterly guidance suspended: Unsurprisingly, management suspended quarterly guidance citing Covid-led uncertainties. We expect other Indian IT services peers to follow suit. US-listed peers such as Cognizant (CTSH), EPAM and Virtusa have already withdrawn their respective guidance. Management expects QoQ revenue contraction for Q1FY21 but refrained from commenting on margins, merely affirming that WPRO remains focused on cost optimisation.

No final dividend: The board did not recommend final dividend, which was a negative surprise given cash & liquid investments worth Rs 334bn or US$ 4.3bn and a debt-free balance sheet. We highlight the contrast with CTSH which paused its share repurchase scheme (and credit drawdown) in the US primarily due to a geographical mismatch in cash balance (parked in India) and requirement.

Ticker/Price	WPRO IN/Rs 187
Market cap	US$ 13.9bn
Shares o/s	5,715mn
3M ADV	US$ 11.9mn
52wk high/low	Rs 302/Rs 159
Promoter/FPI/DII	74%/9%/17%

Source: NSE

STOCK PERFORMANCE



Source: NSE

KEY FINANCIALS

Y/E 31 Mar	FY18A	FY19A	FY20A	FY21E	FY22E
Total revenue (Rs mn)	5,46,359	5,89,060	6,13,401	6,15,956	6,45,651
EBITDA (Rs mn)	1,05,418	1,21,661	1,24,867	1,15,903	1,27,293
Adj. net profit (Rs mn)	80,046	90,074	95,295	85,396	92,160
Adj. EPS (Rs)	13.3	14.9	16.7	14.4	15.5
Adj. EPS growth (%)	4.0	12.3	11.6	(13.9)	7.9
Adj. ROAE (%)	15.9	17.1	16.9	14.3	13.6
Adj. P/E (x)	14.0	12.5	11.2	13.0	12.0
EV/EBITDA (x)	10.7	9.5	8.7	8.7	7.8

Source: Company, BOBCAPS Research

BUY
TP: Rs 255 | ⮝ 47%

TRANSPORT CORP OF INDIA | Logistics | 15 April 2020

Fundamentals intact, valuations compelling

Covid-19 has severely disrupted Transport Corp's (TRPC) operations across verticals. Freight and 3PL are the hardest hit while seaways is less affected. We expect a transitory spurt in demand once the lockdown is lifted, but full-fledged recovery could begin only in Q4FY21. However, TRPC's business fundamentals remain strong and we expect long-term industry trends to be favourable. We cut FY20-FY22 EPS estimates by 13-46% and lower our Mar'21 TP to Rs 255 (vs. Rs 355). Maintain BUY on attractive risk-reward post the recent correction.

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Freight, 3PL hit hard: TRPC's freight vertical is facing a demand slowdown due to reduced consumption spending, as well as supply disruptions due to shortage of manpower (drivers, porters) and obstruction of truck movement by local law enforcement authorities. Consequently, a meagre 10-15% of its trucks are currently running. In 3PL, most warehouses are operational, while some transport activity is taking place for e-commerce/FMCG clients. The seaways business is operating relatively smoothly, especially along the eastern coast.

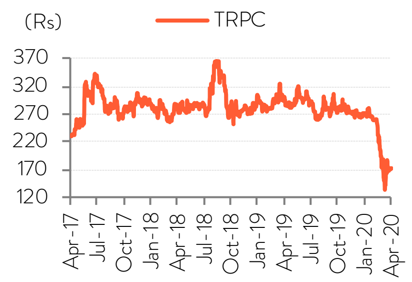
Protracted recovery: The announced relaxation in goods movement post 20 April should provide some respite, but it will take 2-3 weeks more for long haul transport to function seamlessly. Once the lockdown is lifted, we expect a spurt in demand as supply chain gaps are filled, but the Covid-19-led economic slowdown is likely to mar FY21 performance. Recovery could begin in Q4FY21.

Conducive long-term trends: Notwithstanding near-term challenges, TRPC will continue to benefit from favourable long-term industry trends – (1) the growing need for multi-modal services (TRPC among the few to have such capabilities), (2) growing logistics outsourcing to 3PL companies (it is among the leading 3PL players), and (3) consolidation in the trucking industry, which is likely to be hastened by the pandemic (among the largest FTL and LTL players).

Ticker/Price	TRPC IN/Rs 174
Market cap	US$ 173.8mn
Shares o/s	77mn
3M ADV	US$ 0.1mn
52wk high/low	Rs 327/Rs 122
Promoter/FPI/DII	67%/2%/10%

Source: NSE

STOCK PERFORMANCE



Source: NSE

KEY FINANCIALS

Y/E 31 Mar	FY18A	FY19A	FY20E	FY21E	FY22E
Total revenue (Rs mn)	23,499	27,536	27,296	26,227	30,672
EBITDA (Rs mn)	2,165	2,495	2,362	2,197	2,873
Adj. net profit (Rs mn)	1,238	1,460	1,387	1,005	1,493
Adj. EPS (Rs)	16.2	19.0	18.1	13.1	19.5
Adj. EPS growth (%)	52.4	17.7	(4.9)	(27.5)	48.5
Adj. ROAE (%)	17.6	17.7	14.5	9.5	12.7
Adj. P/E (x)	10.7	9.1	9.6	13.2	8.9
EV/EBITDA (x)	7.7	6.9	7.5	8.0	6.1

Source: Company, BOBCAPS Research

BUY
TP: Rs 330 | ⮝ 57%

PETRONET LNG | Oil & Gas | 15 April 2020

Resilient earnings from long-term contracts

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Our recent interaction with the Petronet LNG (PLNG) management deepens confidence in our core investment thesis of (a) faster recovery in utilisation levels at Dahej post lifting of the economic shutdown – as most of its consumers fall under the essential category; and (b) improved demand outlook from H2FY21 led by CGD, fertilisers and power, triggered by sustained low LNG prices (see Feb gas consumption surges). In the current uncertain climate, PLNG's ~16mmtpa of long-term contracts limit earnings downside risks. Maintain BUY.

Low LNG prices buoy volume outlook: The recent crash in oil prices will ensure that all LNG prices align to ~US$ 3/mmbtu levels by 20 May. If this price shift were to also align with lifting of the Covid-19 lockdown in India (staggered easing of restrictions announced from 20 April), we could see a strong V-shaped recovery in RLNG offtake from PLNG's Dahej terminal from Q2FY21.

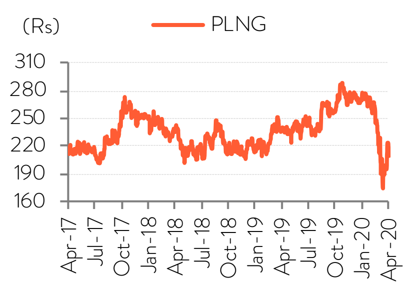
Contracts limit downside risk to earnings: Even if economic disruptions were to continue beyond Q1FY21, PLNG's ~16mmtpa of long-term regasification contracts limit the downside risks to its earnings. The company's plans to unlock another 2mmtpa of capacity at Dahej remain on track – this would be done in phases from 2021, through rollout of two storage tanks by FY23 (~Rs 6bn capex) and a third jetty by FY24. Beyond the existing ~16mmtpa of long-term contracts, PLNG has short-term contracts with OPAL (~0.5mmtpa) and Essar (~0.3mmtpa), yielding ~18mmtpa of volume visibility at Dahej. Kochi ramp-up to 1.5-2.2mmtpa is likely in H2FY21 post Kochi-Mangalore pipeline commissioning.

Maintain BUY: PLNG's fundamentals remain sound with structural improvement in EBITDA/mmbtu and 25%+ ROE expected over FY20-FY22. Existing volume contracts alleviate risks from competition.

Ticker/Price	PLNG IN/Rs 210
Market cap	US$ 4.1bn
Shares o/s	1,500mn
3M ADV	US$ 10.2mn
52wk high/low	Rs 299/Rs 170
Promoter/FPI/DII	50%/27%/23%

Source: NSE

STOCK PERFORMANCE



Source: NSE

KEY FINANCIALS

Y/E 31 Mar	FY18A	FY19A	FY20E	FY21E	FY22E
Total revenue (Rs mn)	305,986	383,954	369,032	282,380	285,793
EBITDA (Rs mn)	33,124	32,935	45,578	52,216	54,078
Adj. net profit (Rs mn)	20,779	21,554	32,693	36,040	38,205
Adj. EPS (Rs)	13.9	14.4	21.8	24.0	25.5
Adj. EPS growth (%)	21.8	3.7	51.7	10.2	6.0
Adj. ROAE (%)	23.3	21.6	30.0	29.2	27.1
Adj. P/E (x)	15.2	14.6	9.6	8.7	8.2
EV/EBITDA (x)	9.9	9.9	6.8	5.6	5.1

Source: Company, BOBCAPS Research

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BANKING | Q4FY20 Preview | 15 April 2020

Limited lockdown impact in Q4

We expect a modest fourth quarter for our banking coverage followed by a sharp credit slowdown in Q1FY21 as the lockdown impact unravels. Q4 systemic loan growth has been tepid at 6% YoY but is expected to be higher for large private banks, while asset quality should perk up across the board. Management comments on unsecured retail/SME delinquencies and moratorium impact are keenly awaited. As noted in our sector report, the top 3 private banks offer a higher margin of safety led by sturdy liability franchises, growth capital and fortified balance sheets.

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Asset quality of unsecured loans on the radar: Banks are likely to showcase marginally better asset quality trends in Q4 as there were no lumpy slippages and this is a seasonally strong quarter in terms of recoveries and one-time settlements. Stress in the unsecured retail and MSME portfolios will be closely watched. We also await commentary on the share of loans under moratorium and measures initiated by banks to limit slippages from such accounts. A few banks may build contingent provisions to strengthen their balance sheets amid Covid-19.

Loan growth to come off across banks: Systemic credit growth has steadily moderated to ~6% YoY in Q4FY20 vs. ~15% a year ago due to weak corporate credit and a slowdown in unsecured retail loans. Loan growth is expected to slow for banks under our coverage in Q4, though large private players should fare relatively better. Proforma business updates suggest a sharp deceleration for Kotak Mahindra Bank (KMB: ~7% YoY) and IndusInd Bank (IIB: ~13%). Credit growth is likely to slump further given the lockdown, though the impact is difficult to quantify at this time.

NIMs to remain largely stable in Q4: Most banks have cut their MCLR by up to 80bps since Mar'19 even as growth in unsecured retail loans has moderated, which is likely to put pressure on yields. We expect this pressure to be offset by a reduction in term deposit rates over the last few months, lower interest reversals and one-off interest recognition on NPA recoveries, thereby keeping margins intact in Q4. Management outlook on NIMs will be keenly watched as the lockdown brings both growth and asset quality of unsecured retail loans into question.

RECOMMENDATION SNAPSHOT

Ticker	Rating
AXSB IN	BUY
DCBB IN	ADD
FB IN	BUY
HDFCB IN	BUY
ICICIBC IN	BUY
IDFCFB IN	ADD
IIB IN	BUY
KMB IN	BUY
RBK IN	ADD
SBIN IN	BUY

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BUILDING MATERIALS | Q4FY20 Preview | 15 April 2020

Expect an insipid quarter

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Building material companies under our coverage are likely to post a dull Q4FY20 as tough market conditions have been further accentuated by the lockdown in end-March, thus taking a toll on volumes. We expect low single-digit volume declines for tile and plywood players. Pipe companies are likely to post a muted performance marked by flat/negative revenue YoY, excepting ASTRA which could see a 10% uptick. Management commentary on business strategies post Covid-19 will be a key monitorable.

Tiles & Sanitaryware – dull quarter all round: Amid weak demand and the lockdown, we expect volume growth to decline in the low single digits for coverage tile companies, viz. Kajaria Ceramics (KJC) and Somany Ceramics (SOMC). Operating margins are forecast to contract 120bps and 100bps YoY respectively due to lower volume sales. In sanitaryware, Cera Sanitaryware (CRS) will likely report a subdued quarter as core category volumes remain tepid. We expect the company to post an ~85bps YoY margin decline due to weak sales.

Plywood & MDF – margin expansion in MDF: Greenply Industries (GIL) and Century Plyboards (CPBI) could see a dip in plywood volume growth. We forecast a 125bps YoY drop in operating margin for GIL due to reduced sales in India and Gabon. In the MDF segment, we expect Greenpanel Industries (GREENP) to report ~40% YoY volume growth partly aided by exports, whereas CPBI could grow at a slower ~10% due to near-peak utilisation of capacity. Both CPBI and GREENP will benefit from better profitability in MDF, aiding estimated margin expansion of 120bps and 300bps YoY respectively.

Pipes & Adhesives – ASTRA stands out: In the pipes segment, we estimate ~10% YoY revenue growth for Astral Poly Technik (ASTRA) aided by price hikes in CPVC, as compared to flat/negative growth for Supreme Industries (SI) and Finolex Industries (FNXP). Both ASTRA (better CPVC profitability) and FNXP (better PVC-EDC delta) are likely to post stronger EBITDA margins, up 40bps and 120bps YoY respectively. SI could see 65bps YoY margin contraction due to slower sales. In adhesives, PIDI is expected to have a modest quarter with volumes in the core CBP segment estimated to decline 1-2% YoY. Operating margins are forecast to rise 135bps due to lower raw material cost.

Watch for: Management commentary on strategies to deal with the fallout of Covid-19 in FY21 will be a key feature to watch this earnings season.

RECOMMENDATION SNAPSHOT

Ticker	Rating
KJC IN	BUY
SOMC IN	BUY
CRS IN	BUY
PIDI IN	SELL
MTLM IN	BUY
CPBI IN	BUY
ASTRA IN	REDUCE
FNXP IN	BUY
SI IN	BUY
GREENP IN	BUY

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AUTOMOBILES

15 April 2020

Yongda call takeaways: China luxury car demand on the rebound

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We hosted a call with China Yongda Automobile Services (Yongda), one of the leading luxury car dealers in China with over 200 outlets catering to marquee brands such as BMW, Porsche, Mercedes Benz, Audi and JLR. Key takeaways from the call are outlined below.

Luxury car demand bouncing back faster than mass market cars: After a weak Jan-Feb'20 largely due to Covid-19, demand for luxury cars in China has recovered swiftly in March as the lockdown in the country was lifted. The mass market segment remains sluggish. Yongda's inventory at March-end stood at comfortable levels of ~30 days. Notwithstanding the negative impact of a potential second wave of Covid-19 infections or US-China trade war concerns, demand should steadily recover.

Luxury carmakers maintain CY20 volume targets: Per management, full-year volume growth targets for China set by all OEMs in Jan'20 remain unchanged despite a weak Q1CY20 (BMW target +12%, Mercedes +5%, Porsche +7-8% and JLR +20%). OEMs are supporting dealers by extending interest-free credit periods (from 30 days to 60-90 days), releasing pending payments and offering special bonuses/gratuities to sales staff.

JLR's performance on an uptrend in China: Gross profit (GP) margin netted by Yongda from the JLR brand improved from –1% in 2018 to +1.3% in 2019 and is likely to further improve in 2020. Given JLR's average ASP in the range of RMB 600-700k, its GP margins can rise to 4-5% in the medium term. However, Yongda's management flagged off the need to raise quality standards of vehicles manufactured at the CJLR facility. Recent launches of the 'New Evoque' and 'XEL' in China and the 'New Defender' planned for H2CY20 are expected to support JLR's 20% volume growth target for the year.

Strong long-term outlook for luxury vehicles in China: China's luxury vehicle penetration has risen from 10% in 2015 to ~15% in 2019. While overall market growth for passenger vehicles may come off after several years of strong sales, Yongda expects a steady increase in luxury vehicle penetration.

EV market yet to gain traction: The Chinese government is extending subsidies for EV vehicles but luxury car buyers are holding back purchases due to a lack of options from established luxury carmakers and the fact that supporting infrastructure still appears inadequate.

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

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

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