FIRST LIGHT

21 October 2022

RESEARCH

BOB Economics Research | State Finances

Cash imbalances of states

Havells India | Target: Rs 1,500 | +24% | BUY

Margins hit trough; expect recovery in H2

Dixon Technologies | Target: Rs 5,200 | +21% | BUY

Buoyant numbers, bright prospects

IIFL Wealth | Target: Rs 2,206 | +22% | BUY

Guidance maintained despite slower flows

Metals & Mining

Aluminium market in need of supply rebalancing

Daily macro indicators

Indicator	18-Oct	19-Oct	Chg (%)
US 10Y yield (%)	4.01	4.13	13bps
India 10Y yield (%)	7.43	7.45	2bps
USD/INR	82.36	82.99	(0.8)
Brent Crude (US$/bbl)	90.0	92.4	2.6
Dow	30,524	30,424	(0.3)
Hang Seng	16,915	16,511	(2.4)
Sensex	58,961	59,107	0.2
India FII (US$ mn)	**17-Oct**	**18-Oct**	**Chg ($ mn)**
FII-D	81.8	37.6	(44.2)
FII-E	(22.3)	104.4	126.7

Source: Bank of Baroda Economics Research

SUMMARY

India Economics: State Finances

In the current fiscal year, we have noticed that there are a number of states which have been consistently using RBI's cash flow management facilities in order to meet their fiscal commitments. While these facilities are provided with an objective of meeting temporary mismatches, some states are using them on a regular basis which signals possible liquidity stress. In this note, we briefly look at states which using these facilities more extensively and their receipts and expenditure patterns.

Click here for the full report.

Havells India

- Muted margins in Q2 owing to poor profitability in both ECD and cables along with wider losses at Lloyd
- Expect margin recovery in H2 given full absorption of high-cost inventory and easing of commodity prices
- FY23/FY24 EPS cut 9%/6%; on rollover, our TP remains unchanged at Rs 1,500 – retain BUY

Click here for the full report.

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Dixon Technologies

- Strong Q2 beat with topline up 38% YoY to Rs 39bn and PAT 15% ahead of our estimates at Rs 777mn
- EBITDA margin up 25bps QoQ to 3.8% on higher contribution from ODM verticals of lighting and home appliances
- Well placed to capture growing opportunities; we raise FY23/FY24 EPS 2%/5% and roll to a revised TP of Rs 5,200 (vs. Rs 4,500) – retain BUY

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IIFL Wealth

- Q2 AUM grew 5% YoY to Rs 2.7tn with flows muted at Rs 61bn; however, earlier profit guidance remains intact
- Focused on expanding trail-based ARR model; recurring revenue formed 68% share in Q2 and recurring AUM 58%
- FY23/FY24/FY25 net flow estimates pared 8%/2%/2% and TP revised to Rs 2,206 (vs. Rs 2,277); retain BUY

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Metals & Mining

- We summarise the read-across from Alcoa's Q3 results and our global channel checks
- With demand decelerating, the global market needs additional supply curtailments – on top of the 1.6mt of cuts so far – to rebalance
- Potential sanctions on Russian metal could impact the global trade balance provided the restrictions rein in global traders

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STATE FINANCES

20 October 2022

Cash imbalances of states

In the current fiscal year, we have noticed that there are a number of states which have been consistently using RBI's cash flow management facilities in order to meet their fiscal commitments. While these facilities are provided with an objective of meeting temporary mismatches, some states are using them on a regular basis which signals possible liquidity stress. In this note, we briefly look at states which using these facilities more extensively and their receipts and expenditure patterns.

Sonal Badhan
Economist

RBI's cash management facilities

RBI has made provisions for 3 kinds of facilities namely, Special Drawing Facility (SDF), WMA (Ways and Means Advances) and OD (Over Draft), for "State Governments to tide over temporary mismatches in the cash flows of their receipts and payments". These have been explained in detail in the appendix.

Looking at the current trends (Apr'22-Aug'22) in utilization of SDF/WMA/OD facilities by states, some of the major states which seem to be having problems in fiscal management include:

- Andhra Pradesh, Telangana, Punjab and Rajasthan.
- Majority of the North Eastern states have also been using RBI's cash flow management facility consistently.
- Maharashtra, Assam and Karnataka have taken recourse to SDF while Kerala has used WMA too. However, the number of days for which they have availed this facility is low unlike the top four.

On an average, Andhra Pradesh and Telangana have availed Rs 712 and Rs 735 crore respectively under SDF facility alone this fiscal year. Out of the 153 days (Apr-Aug), these states availed SDF for 133 and 152 days respectively. Amount accessed via WMA was even higher, averaging Rs 1,773 crore for Andhra Pradesh and Rs 1,206 crore for Telangana, and that too on a regular basis. Even OD facility was availed, which is provided at rates higher than repo rate (see appendix for details). Amongst the North-Eastern states, Manipur, Mizoram and Nagaland are the ones which have availed all three facilities.

Other worrisome trend emerges from Rajasthan and Punjab, which too availed funds under SDF facility for 110 and 90 respectively, out of a total of 153 days. Average funds availed by them were higher than those accessed by Andhra Pradesh and Telangana.

RESULT REVIEW

BOBCAPS
TRUST | INNOVATION | EXCELLENCE

BUY
TP: Rs 1,500 | ⮝ 24%

HAVELLS INDIA | Consumer Durables | 20 October 2022

Margins hit trough; expect recovery in H2

- **Muted margins in Q2 owing to poor profitability in both ECD and cables along with wider losses at Lloyd**
- **Expect margin recovery in H2 given full absorption of high-cost inventory and easing of commodity prices**
- **FY23/FY24 EPS cut 9%/6%; on rollover, our TP remains unchanged at Rs 1,500 – retain BUY**

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Margins drag down Q2: HAVL's Q2FY23 revenue grew 14% YoY to Rs 36.8bn (3Y CAGR: 18%), with volumes contributing ~80% of the growth. However, EBITDA margin deteriorated 600bps YoY to 7.8% (3Y avg: 12.2%) due to larger losses at Lloyd and poor margins in the electronic consumer durables (ECD) and cables & wires (C&W) segments.

Lloyd's losses widen but market share rises: Management reiterated its strategy of chasing market share and has seen visible results, in that Lloyd now commands 12-13% share in the air conditioner segment. However, this strategy caused the subsidiary's EBITDA losses to rise to Rs 840mn in Q2 vs. Rs 563mn in Q1FY23. The company expects to hike prices from Q4FY23 in response to scheduled changes in energy efficiency norms. Management is guiding for lower losses at Lloyd in coming quarters and expects double-digit contribution margins by Q4.

ECD to improve in H2: The ECD business, which witnessed strong traction over the past year, remained muted in Q2 (+6% YoY vs. 3Y CAGR of 12%) on account of lower volumes in fans. Sluggish B2C demand and channel destocking curtailed sales. We expect the slowdown to continue in Q3, but a relatively favourable season for water heaters should compensate for the pullback.

Margins bottoming out: The full absorption of high-cost inventory in Q2 amidst softer raw material prices and lower realisations weighed on margins, with C&W reporting a muted EBIT margin of 6.3%. Extended EBITDA losses at Llyod was a further dampener. We expect easing commodity costs along with a winding down of high inventory to enable EBITDA margins to return to normal.

Growth and margin pullback transient; maintain BUY: We believe the margin deterioration and subdued growth in key verticals is transient in nature and will normalise in H2FY23. Additionally, HAVL's balance sheet (Rs 2.1bn in cash equivalents) is robust. We remain positive on the company's branding, wide presence, superior execution and inherent growth story. Factoring in the Q2 print, we trim our FY23/ FY24 EPS estimates by 9%/ 6%. On rolling valuations forward to Sep'24E, our TP stays at Rs 1,500 based on an unchanged 53x P/E (10% premium to 5Y avg). BUY.

Key changes

Target	Rating
◀ ▶	◀ ▶

Ticker/Price	HAVL IN/Rs 1,210
Market cap	US$ 9.2bn
Free float	41%
3M ADV	US$ 12.3mn
52wk high/low	Rs 1,429/Rs 1,037
Promoter/FPI/DII	60%/23%/9%

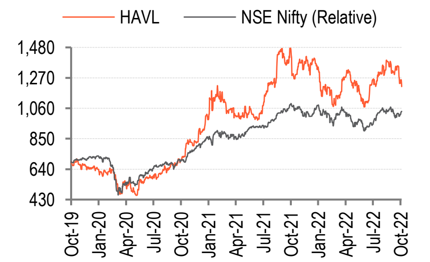
Source: NSE | Price as of 20 Oct 2022

Key financials

Y/E 31 Mar	FY22A	FY23E	FY24E
Total revenue (Rs mn)	1,39,385	1,58,658	1,78,918
EBITDA (Rs mn)	17,604	19,292	23,817
Adj. net profit (Rs mn)	11,965	13,277	16,403
Adj. EPS (Rs)	19.1	21.2	26.2
Consensus EPS (Rs)	19.1	23.1	27.7
Adj. ROAE (%)	21.4	20.7	22.2
Adj. P/E (x)	63.3	57.1	46.2
EV/EBITDA (x)	43.1	39.3	31.8
Adj. EPS growth (%)	14.6	11.0	23.5

Source: Company, Bloomberg, BOBCAPS Research

Stock performance



Source: NSE

BOBCAPS
TRUST | INNOVATION | EXCELLENCE

BUY
TP: Rs 5,200 | ⮝ 21%

DIXON TECHNOLOGIES | Consumer Durables | 21 October 2022

Buoyant numbers, bright prospects

- **Strong Q2 beat with topline up 38% YoY to Rs 39bn and PAT 15% ahead of our estimates at Rs 777mn**
- **EBITDA margin up 25bps QoQ to 3.8% on higher contribution from ODM verticals of lighting and home appliances**
- **Well placed to capture growing opportunities; we raise FY23/FY24 EPS 2%/5% and roll to a revised TP of Rs 5,200 (vs. Rs 4,500) – retain BUY**

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Strong Q2: Dixon posted an above-expected Q2FY23 performance as revenue grew 38% YoY to Rs 39bn (8% ahead of our estimates), led by broad-based growth across verticals (except security systems). EBITDA margin improved sequentially by 25bps to 3.8% (-17bps YoY), marginally above our 3.7% forecast. Adj. PAT came in at Rs 777mn, up 24% YoY and 15% ahead of our estimate.

Margin aided by ODM-led verticals: The lighting & home appliance verticals generate higher margins on account of their original design manufacturing (ODM) characteristics, and performed relatively well in Q2. EBIT margin stood at 8.2% in lighting (+100bps QoQ, +20bps YoY) and 9% in home appliances (+90bps YoY, +50bps QoQ). Amongst other verticals, consumer electronics posted improvement of 20bps QoQ (+50bps YoY) to 2.9% while the mobile segment recorded a modest 2.7% margin.

Guidance maintained: Management retained its FY23 revenue guidance of Rs 150bn but remains optimistic about securing newer, larger client deals in the near future, thus offering scope for guidance revision.

Expanding ODM capabilities: Dixon is focused on expanding its ODM capabilities as it looks to capture a considerable share of India's electronic manufacturing services (EMS) industry. The joint design manufacturing (JDM) business with an anchor client has yielded desired results and the company is in active talks with other customers for additional business. It has already entered into an agreement with Google for ODM sublicensing rights relating to Android. Additionally, Dixon is setting up an injection moulding plant by Q4FY23 to deepen its network and establish backward integration.

Bright prospects; maintain BUY: Over the years, Dixon has scaled up and fortified its leadership in the EMS business. Rapid yet judicious capacity expansion on the back of strong demand, backward integration, steady client acquisition, and favourable PLI schemes are fueling a high growth trajectory. Additionally, entry into newer verticals/products and incremental ODM contribution auger well for the company. We raise FY23/FY24 EPS estimates 2%/5% and roll over to Sep'24E valuations, yielding a revised TP of Rs 5,200 (vs. Rs 4,500), set at 55x P/E, a 20% premium to the 4Y avg.

Key changes

Target	Rating
▲	◄ ►

Ticker/Price	DIXON IN/Rs 4,296
Market cap	US$ 3.1bn
Free float	66%
3M ADV	US$ 15.4mn
52wk high/low	Rs 5,859/Rs 3,181
Promoter/FPI/DII	34%/15%/8%

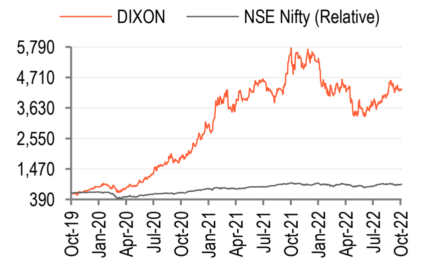
Source: NSE | Price as of 20 Oct 2022

Key financials

Y/E 31 Mar	FY22A	FY23E	FY24E
Total revenue (Rs mn)	106,971	171,280	220,502
EBITDA (Rs mn)	3,791	6,625	8,841
Adj. net profit (Rs mn)	1,903	3,556	5,044
Adj. EPS (Rs)	32.1	59.9	85.0
Consensus EPS (Rs)	32.1	62.7	92.0
Adj. ROAE (%)	22.0	30.4	31.8
Adj. P/E (x)	133.9	71.7	50.5
EV/EBITDA (x)	67.2	38.5	28.8
Adj. EPS growth (%)	19.1	86.8	41.9

Source: Company, Bloomberg, BOBCAPS Research

Stock performance



Source: NSE

BOBCAPS
TRUST | INNOVATION | EXCELLENCE

BUY
TP: Rs 2,206 | ▲ 22%

IIFL WEALTH | Diversified Financials | 20 October 2022

Guidance maintained despite slower flows

- **Q2 AUM grew 5% YoY to Rs 2.7tn with flows muted at Rs 61bn; however, earlier profit guidance remains intact**
- **Focused on expanding trail-based ARR model; recurring revenue formed 68% share in Q2 and recurring AUM 58%**
- **FY23/FY24/FY25 net flow estimates pared 8%/2%/2% and TP revised to Rs 2,206 (vs. Rs 2,277); retain BUY**

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Net flows low; official guidance maintained: IIFL Wealth's AUM grew 5% YoY and 6% QoQ to Rs 2.7tn in Q2FY23, 9% below our estimates. The company garnered net flows of only ~Rs 61bn during the quarter but put out upbeat H2 guidance of at least Rs 200bn in recurring net flows on the back of (i) a sum of Rs 40bn-45bn unlocked from the maturity of existing assets (not earning any trail fees), and (ii) better marketing efforts. We pare our FY23/FY24/FY25 net flow (net new money) estimates by 8%/2%/2% to Rs 314bn/Rs 398bn/Rs 444bn, and lower AUM estimates by ~2% across these years to Rs 4.4tn by FY25 from Rs 4.5tn earlier.

Yields steady: IIFL Wealth clocked yields of 59bps on a blended basis with recurring (ARR) yield at 70bps. The company earned Rs 142mn as carry income in Q2 (Rs 356mn in H1FY23), which is calculated on the non-ARR yields. Over FY23-FY25, we expect ARR yield to sustain at >65bps and overall yield at >50bps.

Return ratios expand: ROAE stood at 22.9% in Q2, expanding ~350bps YoY and 150bps QoQ. Net profit rose 23% YoY and 8% QoQ to Rs 1.7bn (missing estimates by 3%). The cost-to-income (C/I) ratio declined to 44.3% vs. 48.0% in Q2FY22 and 45.4% in Q1FY23. Our C/I estimate remains unchanged at 45% vs. official guidance of 44% for FY23. We forecast a net profit CAGR of 17% over FY22-FY25 to Rs 9.4bn, down 2.5-3% from our previous projection. We expect ~28% ROAE and ~7% ROAA by FY25.

Mid-market segment to be operational start FY24: The mid-market segment (Rs 50mn-250mn) that the company has been espousing over the last few quarters is expected to take shape by end-FY23 with client acquisition likely in early-FY24 in the UHNI and HNI segment, not retail.

Maintain BUY: IIFL Wealth is trading at 21x FY24E EPS and appears undervalued, in our view. Following our estimate revisions, we have a new TP of Rs 2,206 (22% upside) vs. Rs 2,277 earlier, set at an unchanged 25x FY24E EPS – a 10% premium to the 3Y average given a robust model and strong fundamentals. BUY.

Key changes

Target	Rating
▼	◄ ►

Ticker/Price	IIFLWAM IN/Rs 1,809
Market cap	US$ 2.0bn
Free float	77%
3M ADV	US$ 0.8mn
52wk high/low	Rs 1,945/Rs 1,236
Promoter/FPI/DII	23%/23%/3%

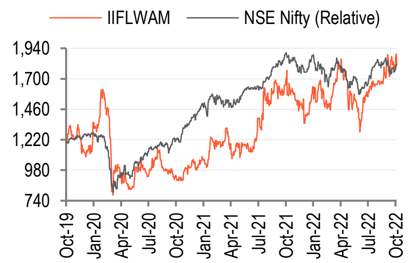
Source: NSE | Price as of 20 Oct 2022

Key financials

Y/E 31 Mar (Rs mn)	FY22A	FY23E	FY24E
PBT (Rs mn)	7,513	9,014	10,664
PBT growth (%)	54.9	20.0	18.3
Adj. net profit (Rs mn)	5,818	6,761	7,998
EPS (Rs)	64.1	74.6	88.2
Consensus EPS (Rs)	64.1	78.0	91.1
P/E (x)	28.2	24.2	20.5
MCap/AUM (%)	6.3	5.4	4.4
ROE (%)	20.0	22.1	24.9

Source: Company, Bloomberg, BOBCAPS Research

Stock performance



Source: NSE

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METALS & MINING

20 October 2022

Aluminium market in need of supply rebalancing

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- **With demand decelerating, the global market needs additional supply curtailments – on top of the 1.6mt of cuts so far – to rebalance**
- **Potential sanctions on Russian metal could impact the global trade balance provided the restrictions rein in global traders**

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Alcoa reports weak Q3: Alcoa (AA, Not Rated) reported adj. EBITDA of US$ 210mn in Q3CY22, down 77% QoQ and as much as 17% below consensus expectations despite a prior profit warning from the company. The decline was driven by a sharp drop in EBITDA/t to US$ 245/t (-75% QoQ) for aluminium and US$ 21/t (-79% QoQ) for alumina. The sequential fall-offs stemmed from lower realisations (72% of the decline), increased raw material and energy costs (18%), and other factors. Alcoa expects the weakness to continue into Q4.

Indian aluminium players to also report a weak Q3: We expect Indian players to report a significant QoQ decline in profitability as realisations have plummetted. Indian players may face a deeper impact from coal inflation due to significant exposure to imported coal.

Aluminium prices to be under pressure near term: Per our channel checks, near-term challenges from a global slowdown along with sticky, high raw material and energy costs (carbon, caustic soda, coal, natural gas) are likely to keep aluminium prices range-bound at US$ 2,100-2,400/t till the market rebalances. Easing of energy inflation, if any, could add further downward pressure.

Supply adjustments essential to rebalance global markets: With the demand slowdown, the global aluminium market is likely to turn into surplus in Q4CY22 from a deficit of 0.4mt in 9MCY22. In response to weakening fundamentals, Europe has already shuttered 1mt of capacity, taking the total closures this year to 1.6mt globally, but this is still not enough to rebalance the global market. At current prices, 20-30% of Chinese supply and 45-55% of ex-China supply is cash-negative, per Alcoa.

Russian metal sanctions: impact depends upon restriction of global traders: Sanctions on trade by global traders such as Glencore could materially disrupt global aluminium trade rebalancing by restricting diversion to China and other Asian countries, potentially tightening the market near term. However, sanctions on usage by developed countries alone may not have a material impact as our checks indicate that China could absorb close to 1mt of the Russian metal against the current 0.3-0.4mt.

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HOLD – Expected return from -6% to +15%

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Note: Recommendation structure changed with effect from 21 June 2021

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