FIRST LIGHT

28 October 2021

RESEARCH

Persistent Systems | Target: Rs 4,170 | +3% | HOLD

Growth outperformance continues

Cera Sanitaryware | Target: Rs 5,895 | +8% | HOLD

Healthy demand traction but priced in

Cipla | Target: Rs 1,160 | +28% | BUY

Results better than expected; EBITDA margin resilient

Daily macro indicators

Indicator	Current	2D (%)	1M (%)	12M (%)
US 10Y yield (%)	1.61	(2bps)	16bps	84bps
India 10Y yield (%)	6.36	1bps	18bps	52bps
USD/INR	74.96	0.2	(1.7)	(1.7)
Brent Crude (US$/bbl)	86.40	0.5	10.6	109.7
Dow	35,757	0.0	2.8	30.2
Shanghai	3,598	(0.3)	(0.4)	10.5
Sensex	61,350	0.6	2.2	51.4
India FII (US$ mn)	**25-Oct**	**MTD**	**CYTD**	**FYTD**
FII-D	47.7	(81.6)	(6.6)	2,020.7
FII-E	(253.1)	(667.2)	7,862.7	536.4

Source: Bloomberg

SUMMARY

Persistent Systems

- Stellar Q2 print with revenue growth of 9.3% QoQ USD (incl. Capiot) driven by BFSI and healthcare
- EBIT margin at 13.9% beat our/consensus estimates. TCV at a robust US$ 282.5mn (+15% QoQ)
- We raise FY22/FY23 EPS and hike our target P/E to 40x. Revise TP to Rs 4,170 (vs. Rs 3,560) but retain HOLD as upsides look capped

Click here **for the full report.**

Cera Sanitaryware

- Q2 consolidated revenue grew 24% YoY with the sanitaryware/faucet segments increasing 30%/63%
- With ~95% of the RM basket stable, operating margin expanded 260bps YoY to 15.3% and EBITDA grew 50%
- We raise our TP to Rs 5,895 (vs. Rs 4,375) on a higher multiple and rollover but retain HOLD as positives look priced in

Click here **for the full report.**

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Cipla

- Q2 revenue/EBITDA grew 10%/4% YoY to Rs 55bn/Rs 12bn, beating our estimates by 6%/4%
- Cost control and a better mix kept EBITDA margin healthy at 22.2% despite lower Covid product contribution and US price erosion
- Launch momentum to continue with a high-value pipeline for H2FY23. Reiterate BUY; TP unchanged at Rs 1,160

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RESULT REVIEW

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HOLD

TP: Rs 4,170 | ⮝ 3%

PERSISTENT SYSTEMS | Technology & Internet | 27 October 2021

Growth outperformance continues

- **Stellar Q2 print with revenue growth of 9.3% QoQ USD (incl. Capiot) driven by BFSI and healthcare**
- **EBIT margin at 13.9% beat our/consensus estimates. TCV at a robust US$ 282.5mn (+15% QoQ)**
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Revenue well ahead of estimates: PSYS reported revenue growth of 9.3% QoQ USD in Q2FY22 vs. our optimistic estimate of 7.4%. IP revenue grew 4.3% QoQ USD despite seasonality and services grew 10.1% QoQ. Growth was spread across three verticals, led by healthcare (+13% QoQ USD).

Robust margin: EBIT margin stood at 13.9% (+30bps QoQ) vs. 13.1% estimated. Offshoring continued to improve with 57.1% revenue share (+160bps QoQ). While offshore billing rates were up 0.5% QoQ, PSYS was able to reduce onsite billing by 2.7% due to lower cost in Mexico, aiding margins. Blended utilisation at 82.8% improved 270bps QoQ backed by talent deployment over the last couple of quarters.

Attrition accelerates: As the industry continues to reel under a talent crunch, PSYS reported its highest-ever attrition rate of 23.6% (+7ppt QoQ). To backfill this, PSYS inducted 975 employees QoQ. Management expects supply pressure to persist for the next few quarters. To contain attrition, PSYS has launched an ESOPs programme covering 80% of employees. Supply-side costs are expected to impact margins and hence PSYS is in talks with clients for better billing rates.

Strong deal wins: The pipeline is strong with TCV at US$ 282.5mn in Q2, up 15% QoQ. ACV at US$ 201.1mn was up 7% QoQ. The quarter saw key wins in the software, hi-tech, BFSI and healthcare verticals. The largest BFSI deal win was worth >US$ 50mn in TCV, spread over a period of five years. PSYS added eight new clients in the US$ 1mn-5mn revenue bucket and one in the >US$ 5mn bucket.

Maintain HOLD: In line with sector-wide commentary, management is confident of demand growth for the next 2-3 years and indicated that its steady TCV win rate is directly proportional to revenue growth. Based on the buoyant outlook and contribution from acquired entities (SCI and Shree Partners), we raise FY22/FY23/FY24 revenue estimates by 4%/6%/5%. EPS rises only 6%/1%/1% due to lower USDINR estimates and a conservative margin outlook. We also upgrade our target P/E to 40x (vs. 35x) on steady deal wins and upbeat growth, yielding a new Sep'22 TP of Rs 4,170 – retain HOLD as current valuations of 39.7x FY23E price in the strong outlook.

Key changes

Target	Rating
▲	◀ ▶

Ticker/Price	PSYS IN/Rs 4,038
Market cap	US$ 4.3bn
Free float	70%
3M ADV	US$ 14.3mn
52wk high/low	Rs 4,390/Rs 1,103
Promoter/FPI/DII	30%/26%/44%

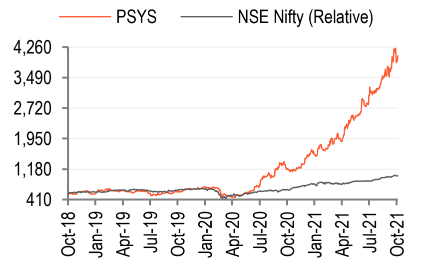
Source: NSE | Price as of 27 Oct 2021

Key financials

Y/E 31 Mar	FY21A	FY22E	FY23E
Total revenue (Rs mn)	41,879	56,441	68,837
EBITDA (Rs mn)	6,830	9,034	11,193
Adj. net profit (Rs mn)	4,507	6,260	7,374
Adj. EPS (Rs)	56.5	78.5	92.4
Consensus EPS (Rs)	56.5	83.7	101.7
Adj. ROAE (%)	17.1	21.0	21.5
Adj. P/E (x)	71.5	51.5	43.7
EV/EBITDA (x)	47.1	35.5	28.6
Adj. EPS growth (%)	32.4	38.9	17.8

Source: Company, Bloomberg, BOBCAPS Research

Stock performance



Source: NSE

HOLD

TP: Rs 5,895 | ⮝ 8%

CERA SANITARYWARE | Construction Materials | 27 October 2021

Healthy demand traction but priced in

- **Q2 consolidated revenue grew 24% YoY with the sanitaryware/faucet segments increasing 30%/63%**
- **With ~95% of the RM basket stable, operating margin expanded 260bps YoY to 15.3% and EBITDA grew 50%**
- **We raise our TP to Rs 5,895 (vs. Rs 4,375) on a higher multiple and rollover but retain HOLD as positives look priced in**

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Healthy revenue growth led by strong demand traction: CRS reported 24% YoY growth in Q2FY22 consolidated revenue to Rs 4bn as (a) it filled the space vacated by peers who depend on imports from China which declined due to high shipping costs, and (b) it saw a revival in real estate demand and increasing retail consumption.

Operating margin expands: During the quarter, ~95% of RM cost was largely stable. Gross margin thus expanded 410bps YoY to 53.4% which coupled with a better product mix and benefits from price hikes spurred EBITDA margin gains of 260bps YoY (+615bps QoQ) to 15.3%.

Demand outlook healthy: Demand has been robust and the sanitaryware/faucet segments ran at optimal capacity utilisation of 97%/90%. CRS expects to see strong demand traction in coming quarters led by (a) a bounce back of real estate demand, (b) pent-up demand for home improvement post pandemic, (c) low interest rates, and (d) lower competition from peers who were dependent on sourcing from China and are now facing supply issues due to high freight cost. Management believes these positives can continue for the next two years.

Maintain positive view…: We expect CRS to witness healthy traction in ensuing years on the back of strong underlying demand and market share gains in sanitaryware (as peers face severe supply issues). The company will focus on replenishing channel inventory and ensuring product availability, leading to an increase in inventory days in FY22 (rise in debtor days also possible).

…but value priced in: We trim EBITDA margin assumptions to incorporate the H1 results, increasing contribution of outsourcing and management commentary. Though we lower FY22/FY23 EPS estimates by 5%/2% on reduced margins, we raise our target one-year forward P/E multiple from 30x to 40x (10% premium to the stock's five-year median of 36.4x) to factor in CRS's market share gains, extensive reach, healthy balance sheet and management pedigree. Positives, however, appear priced in at current valuations of 39x FY23E EPS – we retain HOLD, rolling over to a new Sep'22 TP of Rs 5,895 (vs. Rs 4,375).

Key changes

Target	Rating
▲	◄ ►

Ticker/Price	CRS IN/Rs 5,472
Market cap	US$ 948.3mn
Free float	46%
3M ADV	US$ 2.0mn
52wk high/low	Rs 6,450/Rs 2,625
Promoter/FPI/DII	54%/18%/28%

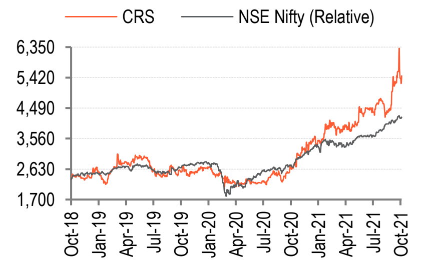
Source: NSE | Price as of 27 Oct 2021

Key financials

Y/E 31 Mar	FY21A	FY22E	FY23E
Total revenue (Rs mn)	12,243	14,436	16,780
EBITDA (Rs mn)	1,581	2,080	2,482
Adj. net profit (Rs mn)	1,008	1,427	1,754
Adj. EPS (Rs)	77.5	109.8	134.9
Consensus EPS (Rs)	77.5	106.1	144.6
Adj. ROAE (%)	12.3	15.4	16.9
Adj. P/E (x)	70.6	49.9	40.6
EV/EBITDA (x)	44.5	33.9	28.5
Adj. EPS growth (%)	(0.6)	41.6	22.9

Source: Company, Bloomberg, BOBCAPS Research

Stock performance



Source: NSE

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BUY
TP: Rs 1,160 | ⮝ 28%

CIPLA | Pharmaceuticals | 27 October 2021

Results better than expected; EBITDA margin resilient

- **Q2 revenue/EBITDA grew 10%/4% YoY to Rs 55bn/Rs 12bn, beating our estimates by 6%/4%**
- **Cost control and a better mix kept EBITDA margin healthy at 22.2% despite lower Covid product contribution and US price erosion**
- **Launch momentum to continue with a high-value pipeline for H2FY23. Reiterate BUY; TP unchanged at Rs 1,160**

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Highest quarterly revenue: Cipla reported its highest-ever quarterly revenue of Rs 55.2bn (+10% YoY) in Q2FY22 on the back of 11% growth in formulations while API revenue declined 9% YoY. India business grew 16% YoY (-11% QoQ) on a high base led by sustained volume traction across core therapies, even though Covid portfolio contribution moderated.

Branded formulations perform well: International revenue grew 14% YoY, supported by resumption of Middle Eastern supplies, strong performance in direct-to-market (DTM) businesses, and contribution from Covid products. The company continued to grow ahead of the market in South Africa private business (+40% YoY USD), while SAGA growth was muted at 7% YoY USD as SSA-CGA declined 21% due to order confirmation delays by some clients and an 8% decline in SA tender business.

US launch momentum to continue: US business was steady at US$ 142mn (+1% YoY/QoQ) due to continued momentum in core products (Diclofenac, Citalopram, Omeprazole), offsetting price erosion in the rest of the portfolio. Cipla reported generic prescription market share of 18%/39% for Albuterol/ Arformoterol for the week ended 8 October. It continues to focus on limited-competition, complex launches and has products such as Revlimid, Abraxane and Advair in the pipeline.

Prudent cost control; targeting FY22 margin of 22%: Gross margin contracted 100bps QoQ in Q2 due to lower Covid portfolio contribution and non-recurring inventory provisions. Higher R&D spend at 5% of revenue (vs. 4.5% same period last year) and resumption of offline promotional activities resulted in EBITDA margin falling 115bps YoY to 22.2% (-225bps QoQ). Margin stress was partly offset by prudent cost controls, but input cost escalation from China could strain margins near term.

Reiterate BUY: We like Cipla for its strong India franchise, rich US pipeline and low risk of price erosion in the US market. We thus retain BUY and keep our Sep'22 TP at Rs 1,160, based on an unchanged 17x forward EV/EBITDA multiple (implied P/E of 28x). Our target multiple is at the midpoint of the stock's 10-year historical band (12-22x) and 8% lower than that for Sun Pharma.

Key changes

Target	Rating
◀ ▶	◀ ▶

Ticker/Price	CIPLA IN/Rs 908
Market cap	US$ 9.8bn
Free float	63%
3M ADV	US$ 33.1mn
52wk high/low	Rs 1,005/Rs 707
Promoter/FPI/DII	36%/25%/21%

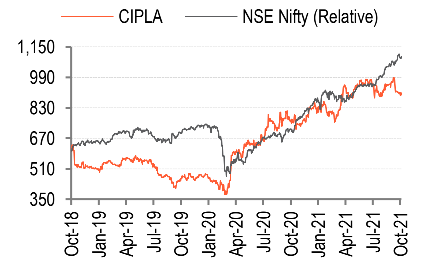
Source: NSE | Price as of 26 Oct 2021

Key financials

Y/E 31 Mar	FY21A	FY22E	FY23E
Total revenue (Rs mn)	1,91,595	2,16,263	2,35,667
EBITDA (Rs mn)	42,524	47,567	50,362
Adj. net profit (Rs mn)	24,048	27,604	29,733
Adj. EPS (Rs)	29.8	34.3	36.9
Consensus EPS (Rs)	29.8	35.1	41.7
Adj. ROAE (%)	14.1	14.2	13.5
Adj. P/E (x)	30.4	26.5	24.6
EV/EBITDA (x)	17.5	15.2	14.0
Adj. EPS growth (%)	55.6	14.8	7.7

Source: Company, Bloomberg, BOBCAPS Research

Stock performance



Source: NSE

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Recommendation scale: Recommendations and Absolute returns (%) over 12 months

BUY – Expected return >+15%

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

SELL – Expected return <-6%

Note: Recommendation structure changed with effect from 21 June 2021

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