BOBCAPS
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FIRST LIGHT

20 August 2020

RESEARCH

Muthoot Finance | Target: Rs 1,320 | +5% | ADD

Opex levers played out, valuations hit peak - cut to ADD

Pharmaceuticals

Expensive e-pharmacy deals; Neutral impact for pharma majors

SUMMARY

Muthoot Finance

Muthoot Finance's (MUTH) Q1FY21 gold AUM increased 15% YoY to Rs 413bn due to higher productivity. Stoppage of low-yield products and reset of liabilities kept spreads buoyant at ~14%. PBT surged 38% YoY to Rs 11.3bn aided by benign credit cost. We keep FY21 earnings unchanged and increase FY22 estimates by 4% to bake in a peaking of opex control despite strong demand. On rollover, our Jun'21 TP stands revised to Rs 1,320 (vs. Rs 1,250). Expensive valuations at 3x FY22E P/B lead us to downgrade the stock to ADD (from BUY).

Click here for the full report.

Pharmaceuticals

Media articles suggest growing consolidation in the e-pharmacy chain, i.e. Reliance-Netmeds and PharmEasy-Medlife. Though e-channels remain a leading disruptive trend within the pharma supply chain, we see multiple grey areas that could limit rapid penetration and margin synergies on the acquired assets. This trend is neutral-to-slight positive for manufacturers in long run.

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TOP PICKS

LARGE-CAP IDEAS

Company	Rating	Target
Bajaj Finance	Buy	4,000
Cipla	Buy	850
GAIL	Buy	155
Petronet LNG	Buy	310
Tech Mahindra	Buy	780

MID-CAP IDEAS

Company	Rating	Target
Alkem Labs	Buy	3,600
Chola Investment	Buy	280
Laurus Labs	Buy	1,200
Transport Corp	Buy	270
Mahanagar Gas	Sell	750

Source: BOBCAPS Research

DAILY MACRO INDICATORS

Indicator	Current	2D (%)	1M (%)	12M (%)
US 10Y yield (%)	0.67	(2)	4	(89)
India 10Y yield (%)	5.95	1	15	(64)
USD/INR	74.76	0.2	0.3	(4.3)
Brent Crude (US$/bbl)	45.46	0.2	5.4	(24.3)
Dow	27,778	(0.2)	4.1	7.0
Shanghai	3,451	0.4	7.4	19.8
Sensex	38,528	1.3	4.1	3.2
India FII (US$ mn)	**17 Aug**	**MTD**	**CYTD**	**FYTD**
FII-D	(38.8)	(85.3)	(14,612.9)	(4,853.4)
FII-E	1,645.2	5,233.6	3,945.4	10,548.3

Source: Bank of Baroda Economics Research

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RESULT REVIEW

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ADD
TP: Rs 1,320 | 5%

MUTHOOT FINANCE | NBFC | 19 August 2020

Opex levers played out, valuations hit peak – cut to ADD

Muthoot Finance's (MUTH) Q1FY21 gold AUM increased 15% YoY to Rs 413bn due to higher productivity. Stoppage of low-yield products and reset of liabilities kept spreads buoyant at ~14%. PBT surged 38% YoY to Rs 11.3bn aided by benign credit cost. We keep FY21 earnings unchanged and increase FY22 estimates by 4% to bake in a peaking of opex control despite strong demand. On rollover, our Jun'21 TP stands revised to Rs 1,320 (vs. Rs 1,250). Expensive valuations at 3x FY22E P/B lead us to downgrade the stock to ADD (from BUY).

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Gold AUM up 15% despite decline in gold tonnage: Gold loan AUM increased 15% YoY to Rs 413bn in Q1 due to a rise in productivity to Rs 88.6mn per branch (+13% YoY). Gold tonnage declined 6% QoQ to 165t as customers pledged lower amounts of collateral due to higher gold prices. Aided by the stoppage of low-yield products, yields (calc.) spiked ~180bps YoY to 23%. We note a 7% YoY decrease in loan accounts as customers made repayments at lower contracted rates per gram of gold and renewed loans at higher rates per gram of gold. MUTH has ~1.5 loans per customer.

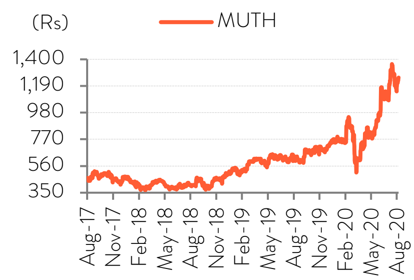
Diversified borrowing mix aids healthy spreads: MUTH reduced liability raising from NCDs and instead focused on banks and CPs. Calculated spreads rose ~200bps YoY to 14%. We believe better treasury management and repricing of CPs and NCDs will lower the cost of funds, thus keeping spreads stable. Excess cash on balance sheet caused a 50-60bps drag on NIM (14.6%).

Opex levers largely played out: The expense ratio decreased 90bps YoY to 3.6% driven by lower rent outgo. Credit cost was at ~15bps, leading to 38% YoY growth in PBT to Rs 11.3bn and PAT growth of 59% YoY to Rs 8.4bn.

Ticker/Price	MUTH IN/Rs 1,256
Market cap	US$ 6.7bn
Shares o/s	401mn
3M ADV	US$ 53.8mn
52wk high/low	Rs 1,406/Rs 477
Promoter/FPI/DII	73%/15%/7%

Source: NSE

STOCK PERFORMANCE



Source: NSE

KEY FINANCIALS

Y/E 31 Mar	FY19A	FY20A	FY21E	FY22E	FY23E
Net interest income	45,202	57,735	65,655	74,746	85,958
NII growth (%)	5.8	27.7	13.7	13.8	15.0
Adj. net profit (Rs mn)	19,721	30,183	34,660	39,825	46,447
EPS (Rs)	49.2	75.3	86.4	99.3	115.8
P/E (x)	25.5	16.7	14.5	12.6	10.8
P/BV (x)	5.1	4.4	3.6	3.0	2.5
ROA (%)	5.7	6.8	6.2	6.2	6.5
ROE (%)	22.4	28.3	27.1	25.9	25.2

Source: Company, BOBCAPS Research

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PHARMACEUTICALS

19 August 2020

Expensive e-pharmacy deals; Neutral impact for pharma majors

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Media articles suggest growing consolidation in the e-pharmacy chain, i.e. Reliance-Netmeds and PharmEasy-Medlife. Though e-channels remain a leading disruptive trend within the pharma supply chain, we see multiple grey areas that could limit rapid penetration and margin synergies on the acquired assets. This trend is neutral-to-slight positive for manufacturers in long run.

Deal valuation at 5-7.5x EV/Sales: As per media reports, Reliance Industries' retail subsidiary is acquiring over 60% stake in Vitalic Health including Netmeds for US$ 83mn (FY20 revenue: US$ 29mn), implying a trailing EV/Sales valuation of 5x. Secondly, Medlife and PharmEasy are reportedly in talks for a merger, wherein Medlife will own 19.6% of the combined entity valued at US$ 1-1.2bn (Medlife+PharmEasy FY20 revenue: ~US$ 170mn), implying trailing EV/Sales of 7-7.5x. Sales for both Medlife and PharmEasy grew 2.5x in FY20 over FY19. Most of these companies have huge PAT losses ranging from 1-1.4x per million of sales. Amazon has also launched its e-pharmacy business last week in Bengaluru with plans to foray into other metros.

Implications – neutral to manufacturer P&L: Online pharmacies account for ~5% of the US$ 19bn India pharma market (vs. ~2% in 2016) and are expected to have 15-16% share in the next 10 years, per Frost & Sullivan. While this is an important disruptive trend, grey areas could limit scalability, viz. concentration of brand building power with doctors and MRs, ill-defined laws on e-pharmacy, risk of spurious drugs, and deficient quality benchmarks vs. developed markets.

Thus, pharma companies may selectively choose to diversify channels besides the offline mode. Cost saving on field force is unlikely to be material, but two key positives would be: (1) improved drug access – volume push, especially in OTC and nutraceuticals, though the prescription space will be difficult, and (2) data analytics for better competitive outcomes for manufacturers.

Takeaways from interaction with pharma majors: (1) Margin benefits from a shift toward e-pharmacy will be low given that doctors/MRs remain key to new prescription generation. (2) Madras High Court has already lifted the stay on sale of drugs by e-pharmacies (suit filed by AIOCD in Oct'18), implying a positive government stance. (3) Ambiguity in health data sharing under the Draft PDP (Personal Data Protection Bill) poses a risk to privacy. (4) With rising M&A and a conducive demand climate, the government may be compelled to create an enabling regulatory environment in the near term.

RECOMMENDATION SNAPSHOT

Ticker	Rating
AJP IN	BUY
ALPM IN	BUY
ALKEM IN	BUY
ARBP IN	BUY
CIPLA IN	BUY
DIVI IN	REDUCE
DRRD IN	ADD
LAURUS IN	BUY
LPC IN	ADD
SUNP IN	REDUCE

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)

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