FIRST LIGHT

21 February 2023

RESEARCH

India Strategy | Q3FY23 Review

New quarter, old challenges

SAIL | Target: Rs 95 | +10% | HOLD

Higher production positive but legacy issues linger

TVS Motor | Target: Rs 1,252 | +13% | HOLD

Steady performance; healthy outlook

Pharmaceuticals

IPM growth slows down in January

Daily macro indicators

Indicator	16-Feb	17-Feb	Chg (%)
US 10Y yield (%)	3.86	3.81	(5bps)
India 10Y yield (%)	7.32	7.37	5bps
USD/INR	82.72	82.83	(0.1)
Brent Crude (US$/bbl)	85.1	83.0	(2.5)
Dow	33,697	33,827	0.4
Hang Seng	20,988	20,720	(1.3)
Sensex	61,320	61,003	(0.5)
India FII (US$ mn)	**15-Feb**	**16-Feb**	**Chg ($ mn)**
FII-D	(36.9)	9.1	46.0
FII-E	93.0	245.6	152.5

Source: Bank of Baroda Economics Research

SUMMARY

INDIA STRATEGY: Q3FY23 REVIEW

- Q3FY23 was a middling quarter with investment themes outperforming consumption sectors; export-oriented sectors did well
- Capital goods/BFSI outperformed and staples/discretionary underperformed; tier-I IT players saw a resurgence
- We retain our stock-specific approach with a largely defensive stance; prefer retail-focused lenders and consumption themes

Click here **for the full report.**

SAIL

- Q3 marks recovery in line with peers; production uptick helped SAIL partly bridge the gap with existing capacity
- Plugging of margin gap vis-à-vis peers requires resolution of bloated employee base and margin penalty on legacy blast furnaces
- We raise TP to Rs 95 (from Rs 90) on valuation rollover; maintain HOLD

Click here **for the full report.**

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TVS MOTOR

- Realisation-led performance aids ~70bps YoY rise in Q3FY23 EBITDA margin; judicious product mix behind better pricing
- Commodity price softening a welcome tailwind and should continue to bolster earnings
- Current valuations price in the positives; we maintain HOLD and roll over to a revised TP of Rs 1,252 (vs. Rs 1,068)

Click here for the full report.

PHARMACEUTICALS

- IPM MAT Jan'23 grew 5.2% YoY led by Gastro, Cardiac and pain therapies while anti-infectives, respiratory and VMN lagged
- Jan'23 grew meagrely at 3.5% YoY weighed down by anti-infectives and respiratory (high bases), despite strong growth in cardiac/neuro/derma
- CIPLA and ERIS remain our top picks in the sector

Click here for the full report.

Q3FY23 REVIEW

20 February 2023

New quarter, old challenges

- **Q3FY23 was a middling quarter with investment themes outperforming consumption sectors; export-oriented sectors did well**
- **Capital goods/BFSI outperformed and staples/discretionary underperformed; tier-I IT players saw a resurgence**
- **We retain our stock-specific approach with a largely defensive stance; prefer retail-focused lenders and consumption themes**

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Some wins, some losses in Q3: Q3FY23 was a tepid quarter which saw Nifty 50 earnings rise 11% YoY led by the BFSI sector. Investment-led sectors such as capital goods and cement posted a healthy topline while consumption-driven sectors such as FMCG and durables found their pricing abilities put to the test. BFSI had a good quarter with margin expansion and improved asset quality. Exports were steady in both services and manufacturing sectors led by tier-I IT and electronics manufacturing services (EMS) players, though the pharma sector saw continued generics price erosion in the US.

Capital goods and cement spring topline surprises: We note clear outperformance among investment-driven sectors, such as capital goods which posted strong numbers and robust order inflows. The recent **capex-heavy budget** lends a further fillip to these sectors. Cement saw 18% YoY topline growth but muted margins and profits.

Consumption sector slows: Staples and durables players had a dull quarter as inflationary pressures weighed on demand. Rural consumption remained sluggish though commentary points to some respite in Q4, a view echoed by auto majors.

Exports shine: Tier-I IT companies posted 1-5% CC growth despite a seasonally weak quarter due to furloughs and also reversed their underperformance vis-à-vis tier-II players (seen over the past 4+ quarters). Further, Q3 saw robust TCV for the top tier (+10% YoY ex-TCS). In manufacturing, our EMS basket clocked strong topline growth YoY (ex-DIXON), while KKC also recorded robust exports.

Unrelenting macro challenges: Broader commentary across sectors highlights the same old challenges that have been plaguing India Inc for the past few quarters. While commodity prices have corrected from peaks, they remain elevated. Inflation is eating into demand and rural offtake remains modest. The chip shortage is another persistent problem, impacting sectors from auto to durables and capital goods.

Retain stock-specific approach: We retain our stock-specific approach with a largely defensive stance – our preference for retail-focused lenders and consumption themes continues.

RESULT REVIEW

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HOLD
TP: Rs 95 | ⮝ 10%

SAIL | Metals & Mining | 20 February 2023

Higher production positive but legacy issues linger

- **Q3 marks recovery in line with peers; production uptick helped SAIL partly bridge the gap with existing capacity**
- **Plugging of margin gap vis-à-vis peers requires resolution of bloated employee base and margin penalty on legacy blast furnaces**
- **We raise TP to Rs 95 (from Rs 90) on valuation rollover; maintain HOLD**

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Q3 marks recovery from lows: While SAIL's Q3FY23 EBITDA recovered from a bottom, in line with consensus, net income missed estimates on higher debt.

Production gap partly bridged: SAIL finally delivered a production pickup in Q3, achieving an annualised run-rate of 18.8mt. This is still short of its 21mt potential and further pickup is likely to be slow, contingent on utilisation improvement in structural mills at Durgapur and IISCO. We expect sales to pick up to 4.8mt in Q4 (+16% QoQ) and 17.6mt in FY24 (+12% YoY).

EBITDA constrained by legacy issues: While higher sales should help reduce per-unit fixed costs, legacy issues of a higher employee base and older blast furnaces continue to weigh on profitability. SAIL's employee cost could come in line with peers when the company implements its next wave of expansion (13mt) sans material addition to the employee base. Similarly, the US$ 80-90/t gap in EBITDA margin for legacy vs. newer blast furnaces can be closed upon modernisation of these units planned in the next wave. See **Plodding quest for growth** for details.

FY23 forecasts cut: Accounting for weaker 9MFY23 actuals and an increase in borrowings, we cut our FY23 EBITDA estimate by 23%. Factoring in slower steel margin stabilisation over FY24, we assume EBITDA margins of Rs 7.2k/t/Rs 8.0k/t for FY24/FY25 and tweak our EBITDA forecasts by -5%/-2%.

Likely to lag peers in next growth phase: SAIL plans to add 3mt of capacity via debottlenecking over the next 3-4 years and to start a 4.5mt brownfield expansion project over the next couple of years (of 13mt planned by FY31). This translates into a slower growth trajectory than peers who have put into motion capex over FY24-FY26.

Maintain HOLD: We raise our TP from Rs 90 to Rs 95 as we revise estimates and roll our valuation base forward to FY25E, continuing to value the stock at an unchanged target EV/EBITDA multiple of 4x. Retain HOLD given limited upside potential of 10%.

Key changes

Target	Rating
▲	◀ ▶

Ticker/Price	SAIL IN/Rs 86
Market cap	US$ 4.3bn
Free float	35%
3M ADV	US$ 19.5mn
52wk high/low	Rs 112/Rs 64
Promoter/FPI/DII	65%/4%/11%

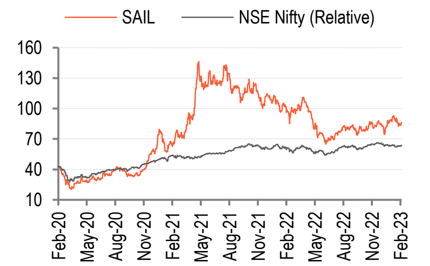
Source: NSE | Price as of 17 Feb 2023

Key financials

Y/E 31 Mar	FY22A	FY23E	FY24E
Total revenue (Rs mn)	1,035	1,042	1,061
EBITDA (Rs mn)	213	87	129
Adj. net profit (Rs mn)	122	26	58
Adj. EPS (Rs)	29.6	6.4	14.0
Consensus EPS (Rs)	29.6	5.1	11.2
Adj. ROAE (%)	24.6	4.8	10.0
Adj. P/E (x)	2.9	13.5	6.2
EV/EBITDA (x)	3.7	7.1	4.3
Adj. EPS growth (%)	195.2	(78.5)	119.9

Source: Company, Bloomberg, BOBCAPS Research

Stock performance



Source: NSE

HOLD
TP: Rs 1,252 | 13%

TVS MOTOR | Automobiles | 20 February 2023

Steady performance; healthy outlook

- **Realisation-led performance aids ~70bps YoY rise in Q3FY23 EBITDA margin; judicious product mix behind better pricing**
- **Commodity price softening a welcome tailwind and should continue to bolster earnings**
- **Current valuations price in the positives; we maintain HOLD and roll over to a revised TP of Rs 1,252 (vs. Rs 1,068)**

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Healthy topline driven by improved realisations: TVSL's Q3FY23 net sales rose 15% YoY (-9% QoQ) to Rs 65.5bn driven by improved realisations (+15% YoY, +8% QoQ). Volumes were flat YoY (-16% QoQ) as domestic two-wheeler sales offset challenges in the export market. Realisation gains came from an improved product mix as the semiconductor supply shortage eased.

Margins expand on lower costs and better mix: Raw material cost rose 14% YoY but fell 10% QoQ as commodity prices softened. Gross margin at 24.5% improved from 23.8% in Q3FY22 on account of price hikes and a better product mix. EBITDA grew 16% YoY (-11% QoQ) to Rs 6.6bn on a high base and adj. PAT rose 22% YoY (-13% QoQ) to Rs 3.5bn, translating to a PAT margin of 5.4% (5.1% in Q3FY22).

Healthy demand outlook: Management expects to grow ahead of industry, both in domestic and international markets, with a strong brand portfolio that includes Apache, Raider, Jupiter, NTORQ, HLX Series, Radeon, Ronin, TVS King, and EV TVS iQube. Given improved chip availability, management expects higher production of premier products. On the exports front, the company believes that external risks have peaked in Q3 and the macro situation should brighten in Q4.

Thrust on EVs: TVSL sold 29k electric scooters in the domestic market in Q3FY23 and expects to cross 100,000 units during FY23. About 10% of domestic scooter volumes are contributed by electric vehicles (EV), with TVS iQube available in ~200 touchpoints across India. The company plans to launch a series of new EV products from a complete portfolio spanning 5KW to 25KW over the next 12-18 months.

Limited upside potential; HOLD: We believe the focus on premiumisation would safeguard margins and any easing of raw material cost will offer added cushioning. In our view, TVSL will continue to beat industry growth as high-end EV/traditional segment launches will further rejuvenate the portfolio. However, positives look priced in at current valuations of 22x FY25E EPS and hence we retain our HOLD rating. On rollover of valuations to FY25E, we have a new TP of Rs 1,252 (vs. Rs 1,068), valuing the core business at 25x EPS and adding Rs 33/sh (consensus value) for TVS Credit.

Key changes

Target	Rating
▲	◀ ▶

Ticker/Price	TVSL IN/Rs 1,104
Market cap	US$ 6.3bn
Free float	48%
3M ADV	US$ 25.4mn
52wk high/low	Rs 1,177/Rs 513
Promoter/FPI/DII	52%/13%/25%

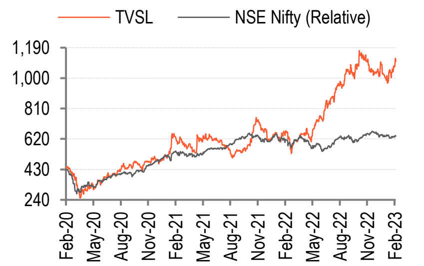
Source: NSE | Price as of 17 Feb 2023

Key financials

Y/E 31 Mar	FY22A	FY23E	FY24E
Total revenue (Rs mn)	207,905	257,636	302,735
EBITDA (Rs mn)	19,617	26,630	33,972
Adj. net profit (Rs mn)	9,237	14,522	19,676
Adj. EPS (Rs)	18.8	30.6	41.4
Consensus EPS (Rs)	18.8	31.8	42.0
Adj. ROAE (%)	19.2	24.9	26.9
Adj. P/E (x)	58.7	36.1	26.7
EV/EBITDA (x)	26.3	19.5	15.4
Adj. EPS growth (%)	46.0	62.5	35.5

Source: Company, Bloomberg, BOBCAPS Research

Stock performance



Source: NSE

PHARMACEUTICALS

20 February 2023

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IPM Jan'23 MAT growth at 5.2%: After double-digit growth in Nov'22 (+14.7%) and Dec'22 (+12.9%), the Indian pharma market (IPM) growth slowed down to 3.5% YoY in Jan'23, per IQVIA sales data. On MAT basis, IPM grew 5.2% (vs +19.4% last year) primarily on the back of price-led growth (+5.2%) and new introductions (+2.2%) while volumes declined 2.2% on a high base (MAT Jan'22 volume growth of 10.3%). Growth in chronic/acute therapies was +9.2%/3.0% on MAT basis and +10.6%/-1% for Jan'23.

Growth momentum in cardiac, neuro and gynaecology continue: IPM Jan'23 showed continued growth momentum in cardiac (+10%), neuro (+12%) and gynaecology (+11%) therapies, in-line with last two month's trend of double-digit growth. Anti-infectives (-3%), respiratory (-7%) and pain (flat) therapies saw steep decline vs strong growth in Dec'22. Among other therapies in top 10, derma grew 10% while gastro/antidiabetic grew 6%/7%, respectively.

On MAT Jan'23 basis, gynaecology (+15% vs. +19% last year), pain (+10% vs. +22%) and gastrointestinal (+10% vs. 19%) reported robust growth even on high bases of last years. Anti-infectives (flat vs. +34% last year), respiratory (+2% vs. 37%) and VMN (+2% vs. +18%) were laggards. Gastrointestinal and pain therapies continued to post double-digit growth despite high bases.

AJP, ALKEM and CIPLA lead growth on 3M basis: For 3M (Nov-Jan'23), the IPM grew 10% YoY driven by the gynaecology (+15%), neuro (+13%) and cardiac (+12%) segments. Barring respiratory (+9%), antidiabetic (+8%), and VMN (+8%), all other therapies beat IPM growth of 10% on 3M basis. From our coverage universe, IQVIA data indicates double-digit growth over Nov'22 to Jan'23 (3M) sales growth for AJP (+19%), ALKEM (+16%), CIPLA (+12%), and SUNP (+11%), but a muted showing for DRRD (+3%) while LPC (+9%), ALPM (+9%), and ERIS (+8%) grew in single digit.

Top picks: CIPLA (BUY, TP Rs 1,250) and ERIS (BUY, Rs 810) remain our top picks in the pharma sector.

Recommendation snapshot

Ticker	Price	Target	Rating
AJP IN	1,193	1,470	HOLD
ALKEM IN	3,262	3,000	SELL
ALPM IN	505	615	HOLD
CIPLA IN	1,026	1,250	BUY
DRRD IN	4,510	4,700	HOLD
ERIS IN	646	810	BUY
LPC IN	670	700	HOLD
SUNP IN	985	1,100	HOLD

Price & Target in Rupees | Price as of 17 Feb 2023

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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

Our recommendation scale does not factor in short-term stock price volatility related to market fluctuations. Thus, our recommendations may not always be strictly in line with the recommendation scale as shown above.

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