

**BUY**

TP: Rs 515 | ▲ 30%

**MAHINDRA LOGISTICS**

Logistics

02 August 2019

## Disappointing quarter on all fronts

**Subdued user industries exacted a heavy toll on Mahindra Logistics' (MLL) Q1FY20 performance. Consolidated revenue/EBITDA (adj. for Ind-AS 116) declined 3%/28% YoY and adj. PAT fell 19% YoY, translating into massive earnings miss. Though headwinds emanating from plunging auto sales pose near-term growth hurdles, long-term prospects remain intact, in our view. We crop FY20/FY21 earnings by 14%/10% and cut our target P/E multiple to 27x (from 30x). Rolling valuations over, our Jun'20 TP moves to Rs 515 (from Rs 600).**

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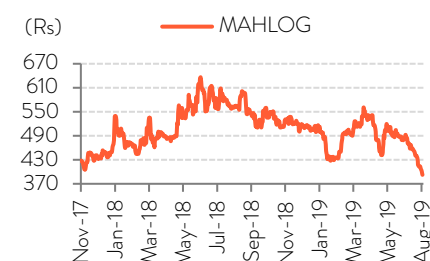
**Slowdown takes a toll:** Plummeting auto volumes triggered a 6% YoY dip in SCM anchor segment revenue. More surprisingly, non-Mahindra, non-auto revenues also dipped 0.4% YoY, as a large bulk player scaled down its business to MLL. Growth in pharma and consumer, the addition of marquee clients, and sustained momentum in the warehousing segment (+25% YoY) were the only positives. The topline is likely to be under pressure in FY20, with revival contingent upon recovery in auto and other user industries.

Ticker/Price	MAHLOG IN/Rs 396
Market cap	US\$ 407.1mn
Shares o/s	71mn
3M ADV	US\$ 0.4mn
52wk high/low	Rs 578/Rs 376
Promoter/FPI/DII	59%/10%/13%

Source: NSE

**Margin disappoints:** While MLL's gross margin was resilient (operating expenses down ~70bps YoY), higher employee cost (+23%/+175bps YoY) led to 110bps YoY EBITDA margin contraction to 3.3%. Interest earned on tax refund boosted other income (+140%), cushioning the fall in adj. PAT (-19% YoY). Given muted topline growth, we expect margins to remain subdued in FY20.

## STOCK PERFORMANCE



Source: NSE

**Structural potential intact:** While acknowledging the bleak short-term outlook, we remain constructive on MLL's long-term potential given 3PL industry growth prospects, robust positioning and clientele, and a strong balance sheet.

**Revise TP to Rs 515:** We cut FY20/FY21 earnings and reset to a lower target P/E of 27x to allow for a tough demand climate, leading to a TP of Rs 515.

## KEY FINANCIALS

Y/E 31 Mar	FY18A	FY19A	FY20E	FY21E	FY22E
Adj. net profit (Rs mn)	640	856	957	1,280	1,589
Adj. EPS (Rs)	9.0	12.0	13.4	17.9	22.2
Adj. EPS growth (%)	34.1	33.2	11.7	33.8	24.1
Adj. ROAE (%)	16.7	18.7	17.9	20.7	22.4
Adj. P/E (x)	44.0	33.1	29.6	22.1	17.8
EV/EBITDA (x)	23.0	18.2	17.1	12.4	10.0

Source: Company, BOBCAPS Research

**BOB Capital Markets Ltd is a wholly owned subsidiary of Bank of Baroda**

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



**FIG 1 – QUARTERLY PERFORMANCE – CONSOLIDATED**

Y/E Mar (Rs mn)	Q1FY20	Q1FY19	YoY (%)	Q4FY19	QoQ (%)
<b>Total revenues</b>	<b>8,992</b>	<b>9,282</b>	<b>(3.1)</b>	<b>10,147</b>	<b>(11.4)</b>
Operating expenses*	7,781	8,096	(3.9)	8,852	(12.1)
% of sales	86.5	87.2	(69bps)	87.2	(71bps)
Employee expenses	745	607	22.8	714	4.4
% of sales	8.3	6.5	175bps	7.0	125bps
Other expenses	172	174	(0.9)	172	-
% of sales	1.9	1.9	4bps	1.7	22bps
Total expenditure	8,698	8,877	(2.0)	9,738	(10.7)
<b>EBITDA</b>	<b>293</b>	<b>405</b>	<b>(27.6)</b>	<b>409</b>	<b>(28.3)</b>
EBITDA margin (%)	3.3	4.4	(110bps)	4.0	(77bps)
Depreciation	54	51	6.9	61	(10.6)
<b>EBIT</b>	<b>239</b>	<b>355</b>	<b>(32.6)</b>	<b>348</b>	<b>(31.3)</b>
Interest expenses	9	8	19.5	10	(10.7)
Other income	70	29	142.0	19	264.9
Extraordinary income/(expense)	-	-	-	-	-
<b>PBT</b>	<b>300</b>	<b>376</b>	<b>(20.2)</b>	<b>357</b>	<b>(16.1)</b>
PBT margin (%)	3.3	4.0	(71bps)	3.5	(19bps)
Profit/(loss) from share of profit from JV and minority interest	(0)	(3)	NM	(4)	NM
<b>Adjusted PAT – before Ind-AS 116 adjustments</b>	<b>195</b>	<b>240</b>	<b>(18.8)</b>	<b>235</b>	<b>(17.2)</b>
Adjusted PAT margin	2.2	2.6	(42bps)	2.3	(15bps)
<b>IND-AS 116 impact</b>	<b>(9)</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>
<b>Reported PAT</b>	<b>186</b>	<b>240</b>	<b>(22.4)</b>	<b>235</b>	<b>(20.8)</b>
Reported PAT margin (%)	2.1	2.6	(51bps)	2.3	(25bps)

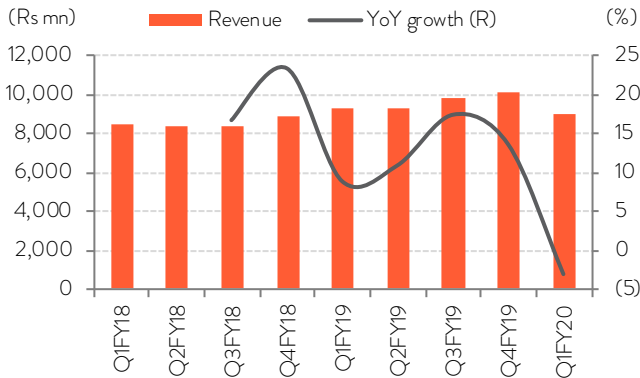
Source: Company, BOBCAPS Research | \*We have adjusted the Ind-AS 116 impact in operating expenses

**FIG 2 – SEGMENT-WISE CONSOLIDATED REVENUE BREAK-DOWN**

Y/E Mar (Rs mn)	Q1FY20	Q1FY19	YoY (%)	Q4FY19	QoQ (%)
<b>Supply Chain Management segment (A)</b>	<b>8,010</b>	<b>8,380</b>	<b>(4.4)</b>	<b>9,173</b>	<b>(12.7)</b>
Mahindra Group	4,890	5,210	(6.1)	5,430	(9.9)
Non-Mahindra clients	3,120	3,170	(1.6)	3,740	(16.6)
<b>Non-Mahindra SCM - Service-wise</b>					
Transportation	2,160	2,400	(10.0)	2,780	(22.3)
Warehousing	960	770	24.7	960	-
<b>Non-Mahindra SCM - Industry-wise</b>					
Auto	810	850	(4.7)	850	(4.7)
Non-auto	2,310	2,320	(0.4)	2,890	(20.1)
<b>People Transport Solution (PTS) segment (B)</b>	<b>981</b>	<b>900</b>	<b>9.0</b>	<b>974</b>	<b>0.7</b>
<b>Total consolidated revenue (A+B)</b>	<b>8,992</b>	<b>9,282</b>	<b>(3.1)</b>	<b>10,147</b>	<b>(11.4)</b>

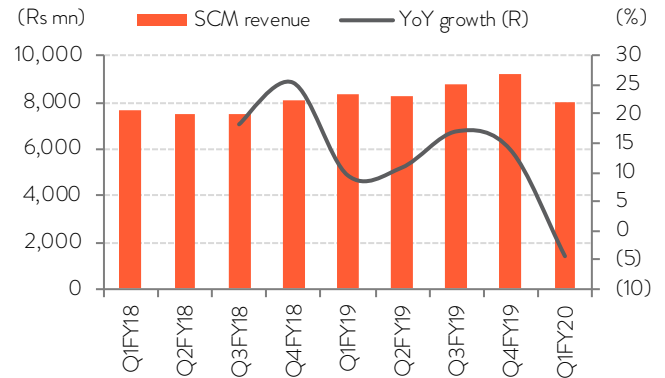
Source: Company, BOBCAPS Research

**FIG 3 – CONSOLIDATED REVENUE DECLINED 3.1% YOY TO RS 9BN**



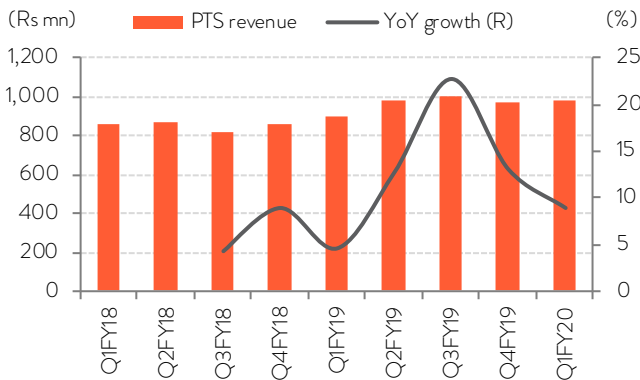
Source: Company, BOBCAPS Research

**FIG 4 – SCM SEGMENT DECLINED 4.4% YOY LED BY DROP IN ANCHOR AND NON-ANCHOR CUSTOMERS**



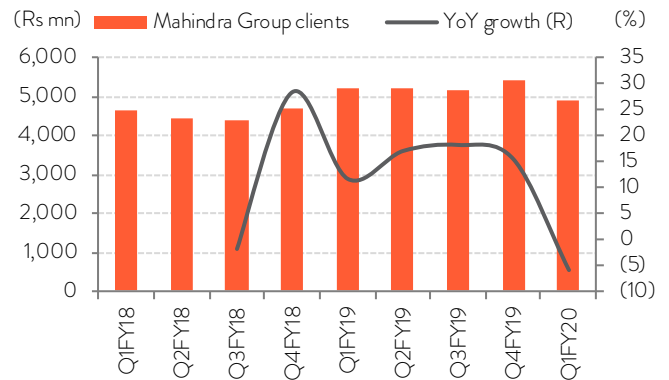
Source: Company, BOBCAPS Research

**FIG 5 – PTS SEGMENT GROWTH ALSO SLOWED DOWN TO 9% YOY**



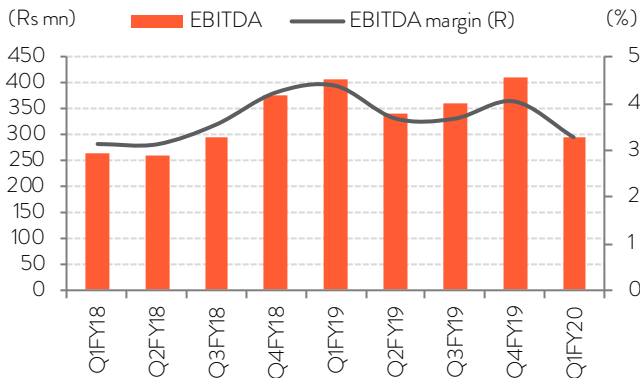
Source: Company, BOBCAPS Research

**FIG 6 – REVENUE FROM THE MAHINDRA CLIENT SEGMENT DECLINED 6% YOY**



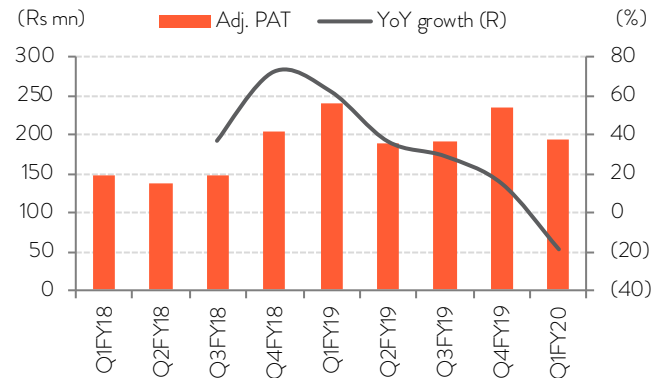
Source: Company, BOBCAPS Research

**FIG 7 – EBITDA DECLINED SHARPLY BY 28% YOY DUE TO HIGHER EMPLOYEE COSTS**



Source: Company, BOBCAPS Research

**FIG 8 – ADJ. PAT (AFTER MINORITY) FELL 19% YOY TO RS 195MN**



Source: Company, BOBCAPS Research

## Earnings call highlights

- **Subdued growth across user industries:** MLL is witnessing weak demand from all key user industries – auto, tractor, consumer, bulk. Expects growth in Q2FY20 to be incrementally better than Q1.
- **Business scaled down by a bulk client:** In Q1FY20, a large customer operating in the bulk industry scaled down its business to MLL, impacting growth of the non-Mahindra SCM segment. The company highlighted that competitive commercial terms offered by competitors at the time of contract renewal was the key reason for loss of business. Management does not foresee a similar outcome in any other client accounts.
- **Robust client addition:** MLL continues to add marquee names to its non-anchor clientele, including Vedanta (transportation), Volkswagen (aftermarket warehousing), Alstom (store and line feed), Pfizer (control tower), Gulf Oil (transportation), Kalyani Maxion Wheels (transportation), and Federal Mogul.
- **Focus on consumer and pharma segments:** The company will maintain its focus on growing the consumer and pharma verticals within the non-Mahindra SCM segment to offset the auto industry slowdown. During Q1, the consumer, pharma and e-commerce segments grew at ~20% YoY. To compensate for loss of the bulk client's business, MLL is also focusing on adding more customers in this segment.
- **Exploring opportunities in other Mahindra group businesses:** Traction from the non-M&M Mahindra group businesses remains healthy. The company has recently won business from Mahindra CIE and has also bid for logistics services in the solar and steel businesses. However, the current share here remains small at ~10% of the total anchor customer segment.
- **Income tax refund:** During Q1FY20, MLL received an income tax refund of Rs 360mn, out of a pending sum of ~Rs 770mn. Interest from this tax refund boosted other income.
- **Strong cash position:** As of Q1, net cash stood at Rs 1.7bn.
- **Warehouse space addition:** MLL has added 0.4mn sq ft of warehousing area in Q1, taking the total area to 15.7mn sq ft.

## Valuation methodology

We remain positive on MLL’s long-term prospects considering (1) its entrenched competitive positioning in India’s burgeoning 3PL industry, (2) robust clientele and increasing presence in the key auto, consumer and pharma verticals within the 3PL industry, (3) impressive return ratios (ROIC of ~35% in FY19), and (4) strong, net-cash balance sheet.

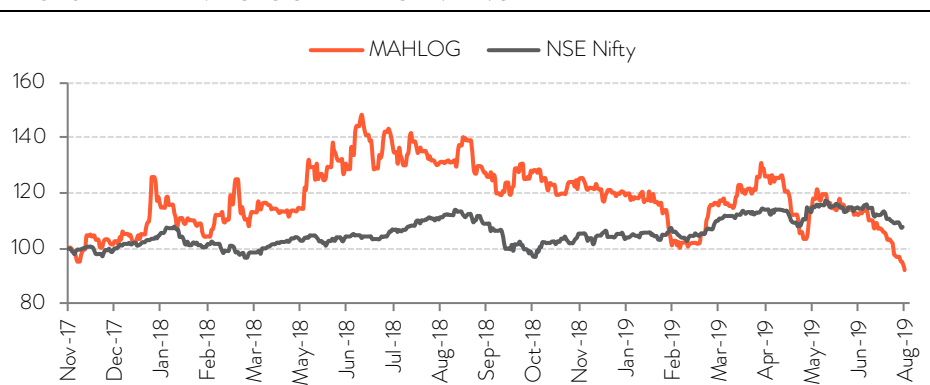
However, the economic slowdown and industry concentration have given rise to key near-term challenges by way of a slump in the automobile industry, a key client segment for MLL, and below-estimated traction in the non-Mahindra client segment. Accordingly, we scale back our revenue and earnings estimates for FY20/ FY21 by 6%/5% and 14%/10% respectively. We also pare our target P/E multiple to 27x from 30x given the challenging demand climate. Rolling valuations over, we have a revised Jun’20 target price of Rs 515 (Rs 600 earlier). Maintain BUY.

**FIG 9 – REVISED ESTIMATES**

(Rs mn)	FY20E			FY21E			FY22E
	Old	New	Change (%)	Old	New	Change (%)	Introduced
Revenues	42,866	40,269	(6.1)	48,618	46,256	(4.9)	53,536
EBITDA	1,889	1,593	(15.7)	2,383	2,135	(10.4)	2,650
EBITDA margin (%)	4.4	4.0	(45bps)	4.9	4.6	(29bps)	4.9
PAT	1,113	957	(14.0)	1,423	1,280	(10.0)	1,589
PAT margin (%)	2.6	2.4	(22 bps)	2.9	2.8	(16 bps)	3.0

Source: Company, BOBCAPS Research

**FIG 10 – RELATIVE STOCK PERFORMANCE**



Source: NSE

## Key risks

Key downside risks to our estimates are:

- lower-than-estimated traction in the non-Mahindra client segment,
- high churn in the non-anchor client segment, and
- delayed recovery in auto demand.

## FINANCIALS

### Income Statement

Y/E 31 Mar (Rs mn)	FY18A	FY19A	FY20E*	FY21E*	FY22E*
<b>Total revenue</b>	<b>34,161</b>	<b>38,513</b>	<b>40,269</b>	<b>46,256</b>	<b>53,536</b>
EBITDA	1,197	1,512	1,593	2,135	2,650
EBIT	1,000	1,293	1,362	1,858	2,320
Net interest income/(expenses)	(38)	(35)	(31)	(18)	(8)
Other income/(expenses)	59	76	133	120	123
Exceptional items	0	0	0	0	0
EBT	1,021	1,334	1,464	1,960	2,435
Income taxes	(368)	(468)	(498)	(666)	(828)
Extraordinary items	0	0	0	0	0
Min. int./Inc. from associates	(13)	(10)	(9)	(13)	(18)
<b>Reported net profit</b>	<b>640</b>	<b>856</b>	<b>957</b>	<b>1,280</b>	<b>1,589</b>
Adjustments	0	0	0	0	0
<b>Adjusted net profit</b>	<b>640</b>	<b>856</b>	<b>957</b>	<b>1,280</b>	<b>1,589</b>

### Balance Sheet

Y/E 31 Mar (Rs mn)	FY18A	FY19A	FY20E*	FY21E*	FY22E*
Accounts payables	4,863	6,001	6,620	7,604	8,800
Other current liabilities	205	419	331	380	440
Provisions	180	215	225	258	299
Debt funds	346	377	235	115	40
Other liabilities	0	0	0	0	0
Equity capital	711	715	715	715	715
Reserves & surplus	3,554	4,325	5,043	6,003	6,797
Shareholders' fund	4,266	5,039	5,757	6,717	7,512
<b>Total liabilities and equities</b>	<b>9,860</b>	<b>12,051</b>	<b>13,168</b>	<b>15,075</b>	<b>17,092</b>
Cash and cash eq.	1,161	1,475	1,994	2,043	2,253
Accounts receivables	5,200	6,317	7,171	8,237	9,534
Inventories	0	0	0	0	0
Other current assets	1,480	2,046	2,139	2,457	2,844
Investments	0	38	38	38	38
Net fixed assets	605	660	705	727	748
CWIP	6	26	0	0	0
Intangible assets	54	53	53	53	53
Deferred tax assets, net	141	187	187	187	187
Other assets	1,213	1,250	881	1,333	1,436
<b>Total assets</b>	<b>9,860</b>	<b>12,051</b>	<b>13,168</b>	<b>15,075</b>	<b>17,092</b>

Source: Company, BOBCAPS Research | \*Without factoring in Ind-AS 116 impact

### Cash Flows

Y/E 31 Mar (Rs mn)	FY18A	FY19A	FY20E*	FY21E*	FY22E*
Net income + Depreciation	837	1,076	1,188	1,558	1,918
Interest expenses	38	35	31	18	8
Non-cash adjustments	(9)	(46)	0	0	0
Changes in working capital	(614)	(332)	(38)	(769)	(489)
Other operating cash flows	0	0	0	0	0
<b>Cash flow from operations</b>	<b>252</b>	<b>732</b>	<b>1,181</b>	<b>806</b>	<b>1,438</b>
Capital expenditures	(240)	(294)	(250)	(300)	(350)
Change in investments	0	(38)	0	0	0
Other investing cash flows	0	0	0	0	0
<b>Cash flow from investing</b>	<b>(240)</b>	<b>(332)</b>	<b>(250)</b>	<b>(300)</b>	<b>(350)</b>
Equities issued/Others	31	3	0	0	0
Debt raised/repaid	3	31	(142)	(120)	(75)
Interest expenses	(38)	(35)	(31)	(18)	(8)
Dividends paid	(129)	(155)	(239)	(320)	(794)
Other financing cash flows	197	72	0	0	0
<b>Cash flow from financing</b>	<b>66</b>	<b>(84)</b>	<b>(412)</b>	<b>(458)</b>	<b>(877)</b>
<b>Changes in cash and cash eq.</b>	<b>78</b>	<b>316</b>	<b>520</b>	<b>48</b>	<b>210</b>
<b>Closing cash and cash eq.</b>	<b>1,161</b>	<b>1,475</b>	<b>1,994</b>	<b>2,043</b>	<b>2,253</b>

### Per Share

Y/E 31 Mar (Rs)	FY18A	FY19A	FY20E*	FY21E*	FY22E*
Reported EPS	9.0	12.0	13.4	17.9	22.2
Adjusted EPS	9.0	12.0	13.4	17.9	22.2
Dividend per share	1.5	1.8	3.3	4.5	11.1
Book value per share	59.0	69.7	79.9	93.5	104.9

### Valuations Ratios

Y/E 31 Mar (x)	FY18A	FY19A	FY20E*	FY21E*	FY22E*
EV/Sales	0.8	0.7	0.7	0.6	0.5
EV/EBITDA	23.0	18.2	17.1	12.4	10.0
Adjusted P/E	44.0	33.1	29.6	22.1	17.8
P/BV	6.7	5.7	5.0	4.2	3.8

### DuPont Analysis

Y/E 31 Mar (%)	FY18A	FY19A	FY20E*	FY21E*	FY22E*
Tax burden (Net profit/PBT)	62.7	64.2	65.4	65.3	65.3
Interest burden (PBT/EBIT)	102.1	103.2	107.5	105.5	104.9
EBIT margin (EBIT/Revenue)	2.9	3.4	3.4	4.0	4.3
Asset turnover (Revenue/Avg TA)	7.8	7.4	6.9	7.0	7.2
Leverage (Avg TA/Avg Equity)	1.1	1.1	1.1	1.1	1.0
Adjusted ROAE	16.7	18.7	17.9	20.7	22.4

Source: Company, BOBCAPS Research | Note: TA = Total Assets | \*Without factoring in Ind-AS 116 impact

**Ratio Analysis**

Y/E 31 Mar	FY18A	FY19A	FY20E*	FY21E*	FY22E*
<b>YoY growth (%)</b>					
Revenue	28.1	12.7	4.6	14.9	15.7
EBITDA	57.0	26.3	5.3	34.0	24.1
Adjusted EPS	34.1	33.2	11.7	33.8	24.1
<b>Profitability &amp; Return ratios (%)</b>					
EBITDA margin	3.5	3.9	4.0	4.6	4.9
EBIT margin	2.9	3.4	3.4	4.0	4.3
Adjusted profit margin	1.9	2.2	2.4	2.8	3.0
Adjusted ROAE	16.7	18.7	17.9	20.7	22.4
ROCE	23.6	25.8	23.9	29.0	32.3
<b>Working capital days (days)</b>					
Receivables	56	60	65	65	65
Inventory	0	0	0	0	0
Payables	54	59	62	63	63
<b>Ratios (x)</b>					
Gross asset turnover	33.3	32.4	27.8	26.7	26.0
Current ratio	1.5	1.5	1.6	1.6	1.6
Net interest coverage ratio	26.5	37.2	44.5	106.0	298.6
Adjusted debt/equity	(0.2)	(0.2)	(0.3)	(0.3)	(0.3)

Source: Company, BOBCAPS Research | \*Without factoring in Ind-AS 116 impact



## Disclaimer

### Recommendations and Absolute returns (%) over 12 months

**BUY** – Expected return >+15%

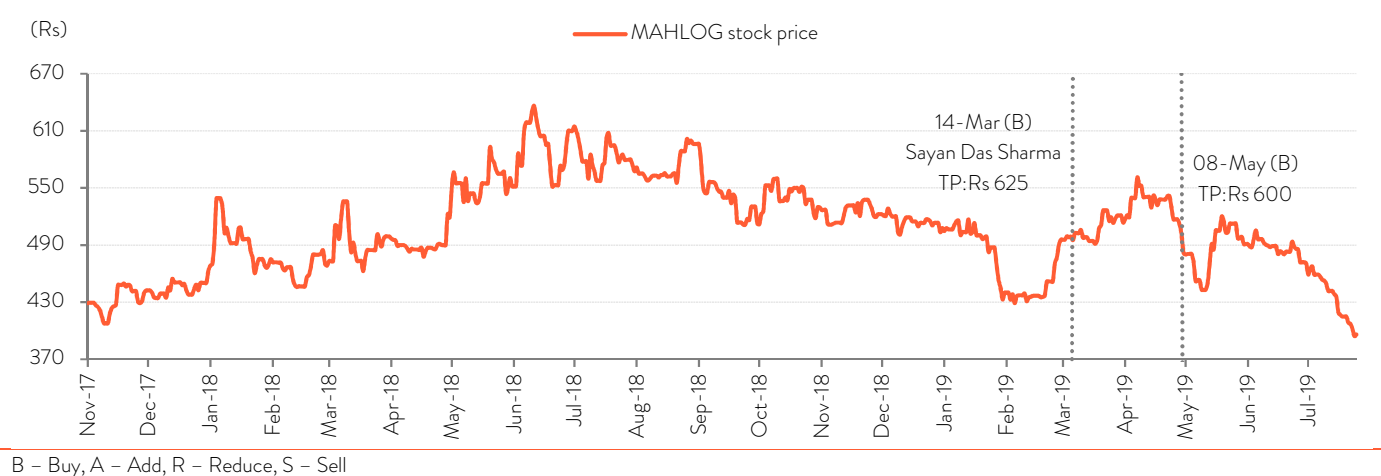
**ADD** – Expected return from >+5% to +15%

**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)

### HISTORICAL RATINGS AND TARGET PRICE: MAHINDRA LOGISTICS (MAHLOG IN)



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