

SELL

TP: Rs 210 | ▼ 14%

**NIPPON LIFE INDIA
 ASSET MANAGEMENT**

Diversified Financials

15 May 2020

Levers for opex control have peaked

Nippon Life Asset Management (NAM) reported a Rs 360bn sequential AUM decline in Q4FY20, largely due to the mark-to-market effect. Strong opex control aided EBITDA growth of 14% YoY. In our view, the levers for opex control have largely played out. We cut FY21-FY22 EPS estimates by 10% each as the high-yielding equity business is likely to clock muted growth. Our Mar'21 TP stands revised down to Rs 210 (vs. Rs 280 earlier) – maintain SELL.

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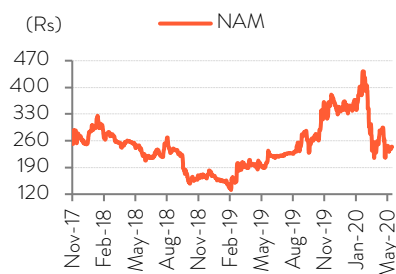
Gaining debt market share looks difficult: AUM (end of period) saw a rundown of ~Rs 360bn on a sequential basis in Q4 – primarily due to the MTM effect, and not redemptions. Though SIP flows were steady at Rs 8.1bn, we expect the high-yielding equity business to slow down in the wake of Covid-19. We also argue that gaining market share in debt looks difficult for NAM given FY19-FY20 debt write-offs.

Ticker/Price	NAM IN/Rs 244
Market cap	US\$ 2.0bn
Shares o/s	612mn
3M ADV	US\$ 10.4mn
52wk high/low	Rs 453/Rs 208
Promoter/FPI/DII	76%/5%/7%

Source: NSE

Levers for opex control largely played out: EBITDA grew 14% YoY to Rs 1.6bn as the company maintained a tight leash on expenses. We believe NAM has largely exhausted its levers in terms of limiting marketing and discretionary spends. EBITDA margin at 59% expanded ~1,800bps YoY due to cost control and looks to have peaked, in our view. Other income was negative due to a Rs 1.5bn MTM effect on investments in own schemes. Adjusted for this one-off, PAT grew 3% YoY in Q4 to Rs 1.6bn and 17% in FY20 to Rs 5.7bn.

STOCK PERFORMANCE



Source: NSE

Maintain SELL: Not only will gaining market share in debt prove challenging, but we believe NAM also faces a tough balancing act to add equity market share and maintain profitability. We retain our SELL rating with a revised Mar'21 TP of Rs 210 (earlier Rs 280) as we cut our FY21-FY22 earnings estimates by 10% each to bake in the pandemic impact.

KEY FINANCIALS

Y/E 31 Mar (Rs mn)	FY18A	FY19A	FY20P	FY21E	FY22E
Core PBT (Rs mn)	4,987	5,290	5,696	5,811	7,040
Core PBT (YoY)	10.1	6.1	7.7	2.0	21.2
Adj. net profit (Rs mn)	4,572	4,871	4,158	5,827	6,820
EPS (Rs)	7.5	8.0	6.8	9.5	11.1
P/E (x)	32.6	30.6	35.9	25.6	21.9
MCap/AAAUM (%)	6.3	6.3	7.2	6.3	5.5
RoAAAUM (in bp)	19.4	20.4	19.9	24.7	25.3
ROE (%)	21.0	19.7	16.1	22.1	24.9

Source: Company, BOBCAPS Research

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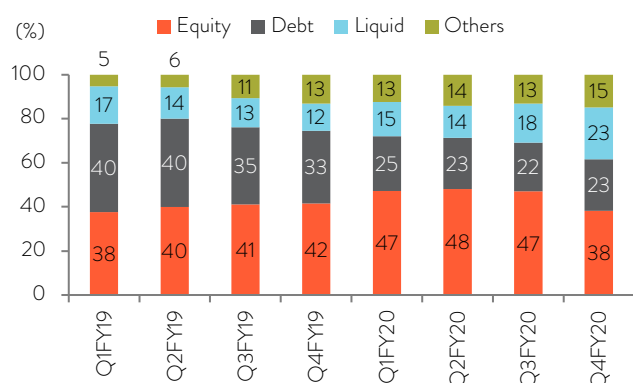


FIG 1 – QUARTERLY PERFORMANCE

(Rs mn)	Q4FY20	Q4FY19	YoY (%)	Q3FY20	QoQ (%)	FY20	FY19	YoY (%)
Total income	1,496	3,975	(62.4)	3,606	(58.5)	11,932	16,499	(27.7)
Operating Expenses	1,129	2,018	(44.1)	1,560	(27.7)	5,945	9,396	(36.7)
EBITDA	1,617	1,415	14.3	1,471	9.9	6,085	5,391	12.9
Core PBT	1,523	1,578	(3.5)	1,361	11.9	5,696	5,290	7.7
Other income	(1,249)	543	(330.2)	575	(317.3)	(98)	1,713	(105.7)
PBT	274	2,121	(87.1)	1,936	(85.9)	5,598	7,002	(20.1)
Tax	232	604	(61.6)	443	(47.6)	1,441	2,132	(32.4)
Net Profit	41	1,517	(97.3)	1,493	(97.2)	4,158	4,871	(14.6)

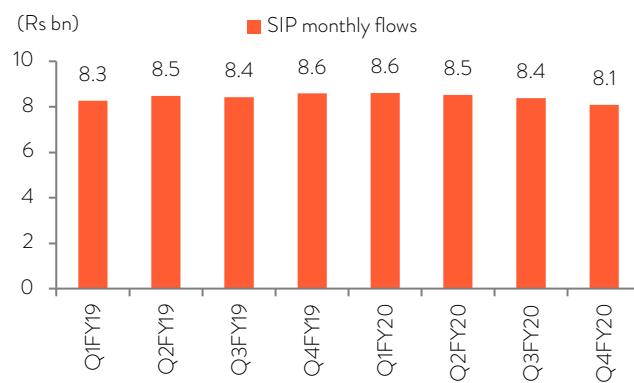
Source: Company, BOBCAPS Research

**FIG 2 – EQUITY AUM DECLINE DRIVEN LARGELY BY
BY MTM EFFECT**



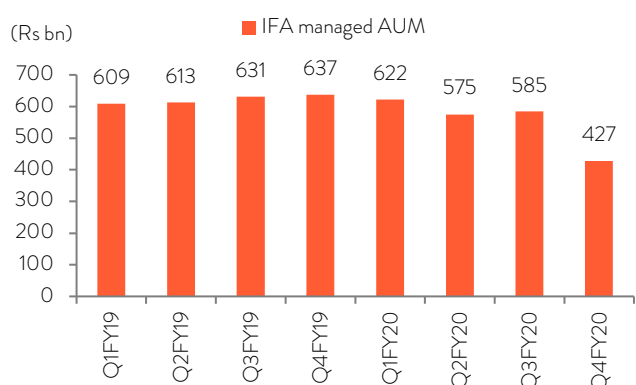
Source: Company, BOBCAPS Research

FIG 3 – SIP FLOW STEADY



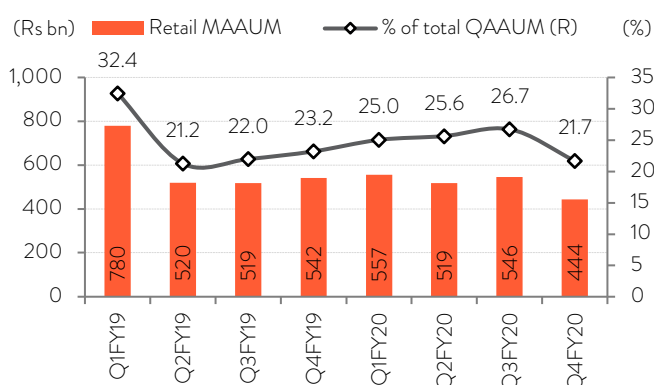
Source: Company, BOBCAPS Research

FIG 4 – MTM LOSSES ON IFA-MANAGED AUM...



Source: Company, BOBCAPS Research

FIG 5 – ...AND RETAIL AUM (LARGELY EQUITY)



Source: Company, BOBCAPS Research

FIG 6 – DETAILED QUARTERLY PERFORMANCE

	FY19				FY20				Change (%)	
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	QoQ	YoY
Profit and Loss (Rs mn)										
Total income	4,100	4,240	4,040	3,975	3,604	3,226	3,606	1,496	(58.5)	(62.4)
Operating Expenses	2,430	2,533	2,317	2,018	1,705	1,551	1,560	1,129	(27.7)	(44.1)
EBITDA	1,350	1,378	1,182	1,415	1,546	1,451	1,471	1,617	9.9	14.3
Depreciation	80	87	90	(164)	76	76	91	89	(2.5)	(154.4)
Finance Costs	0	0	0	0	17	16	19	5	NM	NM
Core PBT	1,270	1,292	1,092	1,578	1,452	1,359	1,361	1,523	11.9	(3.5)
Other income	320	329	541	543	353	224	575	(1,249)	(317.3)	(330.2)
PBT	1,590	1,620	1,633	2,121	1,805	1,583	1,936	274	(85.9)	(87.1)
Tax	500	490	536	604	549	216	443	232	(47.6)	(61.6)
Net Profit	1,090	1,131	1,097	1,517	1,256	1,367	1,493	41	(97.2)	(97.3)
Ratios (Calc, %)										
Cost to core income ratio	64.3	64.8	66.2	58.8	52.5	51.7	51.5	41.1	(1,035bps)	(1,767bps)
EBITDA Margin	35.7	35.2	33.8	41.2	47.5	48.3	48.5	58.9	1,035bps	1,767bps
Core PBT Margin	33.6	33.0	31.2	46.0	44.7	45.3	44.9	55.5	1,057bps	950bps
RoAAUM	0.18	0.19	0.19	0.22	0.23	0.27	0.30	0.02	(28bps)	(20bps)
AUM (EOP)										
Total AUM	2,318	2,238	2,272	2,278	2,025	1,886	1,997	1,635	(18.1)	(28.2)
Equity	871	894	933	945	954	907	939	625	(33.4)	(33.9)
Debt	930	896	797	752	505	438	442	383	(13.4)	(49.1)
Liquid	392	317	298	280	312	273	352	384	9.2	37.3
Others	125	131	244	301	254	268	265	244	(8.0)	(19.0)
Other details										
No of Branches	298	298	299	300	294	290	290	290	0	(10)
Empanelled distributors	68,187	70,827	72,203	73,000	74,100	75,400	75,600	76,200	600	3,200
SIP Monthly flows (Rs bn)	8.3	8.5	8.4	8.6	8.6	8.5	8.4	8.1	(3.6)	(5.9)
SIP transactions (mn)	2.8	2.9	2.9	3.1	3.2	3.2	3.3	3.2	(3.0)	3.2

Source: Company, BOBCAPS Research

Earnings call highlights

- 17% of assets sourced from B30 cities
- Unrealised loss of Rs 1.5bn in Q4 due to MTM loss on investments in own schemes (Rs 1.3bn in equity schemes and Rs 200mn in debt schemes). Other income totaled Rs 270mn
- Other assets in investments represent investment into own AIF and trade receivables
- Employee expense ~33% variable. Long-term incentives frozen; hence the fall in employee expenses. Employee expenses not linked to NAV, but to company performance
- Other expenses declined in Q4 as marketing and discretionary spends reduced
- Opex guided at Rs 1.5bn per quarter in FY21 and FY22
- Consolidated fee commissions higher in Q4 because of fund raising in AIF
- No exposure of Reliance group companies in MF schemes
- Decision taken to invest in AA-and-above rated papers in debt schemes
- Debt mix changing towards liquid and overnight funds
- No direct exposure to NCDs
- 1 SIP transaction every 20 seconds due to digital capability
- Phantom stock options to close by FY22
- Asset management rights of Rs 2.4bn on balance sheet. No write-offs in FY20

Valuation methodology

NAM is trading at 25.6x/21.8x FY21E/FY22E EPS for an estimated ROE of 22.1%/24.9%. We believe the company is a play on the financialisation of savings in India. However, due to legacy brand issues and multiple debt write-downs during FY19-FY20, we think debt AAUM is unlikely to retrace to market share levels seen pre-IL&FS.

Further, given NAM's increasing reliance on independent financial advisors (IFA) to source equity flows, we expect revenue realisations to be lower than the average of the top-10 AMCs (at ~63bps). A high opex structure due to increased costs towards rebranding, marketing and ESOPs would dampen ~50% of revenue realisations. Core PBT yields could thus remain range-bound at 33-34bps, with PAT yields at 25bps over FY21-FY22 propped up by a benign tax rate. In our view, the company faces a tough balancing act between profitability and market share gains, with one coming at the expense of the other.

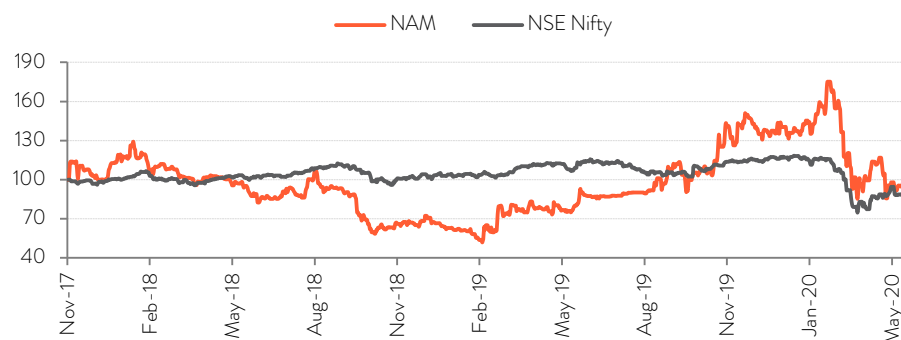
We maintain SELL and revise our Mar'21 target price down to Rs 210 (from Rs 280) as we cut FY21/FY22 earnings estimates by 10% each given the negative impact of Covid-19 on the high-yielding equity business. We have arrived at our target price using a three-stage dividend discount model (DDM). Our key assumptions are cost of equity of 14.0% (risk-free rate of 7.75% and beta of 1.2x), with average growth of ~15% in the five-year explicit period and terminal growth of 10%.

FIG 7 – REVISED ESTIMATES

(Rs bn)	Old		New		Change (%)	
	FY21	FY22	FY21	FY22	FY21	FY22
Total income	16	18	14	16	(8.1)	(8.1)
Operating Expenses	7	8	6	7	(7.1)	(7.1)
EBITDA	7	8	6	7	(14.0)	(13.3)
Core PBT	7	8	6	7	(15.1)	(14.2)
Other income	2	2	2	2	11.3	11.3
PBT	9	10	8	9	(9.6)	(9.5)
Tax	2	2	2	2	(7.0)	(6.9)
Net Profit	7	8	6	7	(10.5)	(10.3)
AAUM	2,475	2,827	2,357	2,699	(4.8)	(4.5)
RoAAUM (bp)	26	27	25	25	(157bps)	(162bps)

Source: Bloomberg

FIG 8 – RELATIVE STOCK PERFORMANCE



Source: NSE

Key risks

- Any further regulation on trail commissions could hamper equity flows from IFAs.
- Additional risky debt exposure could lead to loss of trust in the new brand too.
- Fund alpha underperformance could fuel redemptions, especially in T30 cities and among HNIs.

FINANCIALS

Income Statement

Y/E 31 Mar (Rs mn)	FY18A	FY19A	FY20P	FY21E	FY22E
Investment management fees	15,918	14,787	12,030	12,521	14,324
YoY (%)	21.7	(7.1)	(18.6)	4.1	14.4
Operating expenses	10,823	9,396	5,945	6,464	7,029
Core operating profits	5,094	5,391	6,085	6,057	7,295
Core operating profits growth (%)	9.2	5.8	12.9	(0.5)	20.4
Depreciation and Interest	107	101	389	246	254
Core PBT	4,987	5,290	5,696	5,811	7,040
Core PBT growth (%)	10.1	6.1	7.7	2.0	21.2
Other income	1,569	1,713	(98)	1,979	2,078
PBT	6,556	7,002	5,598	7,790	9,118
PBT growth (%)	12.8	6.8	(20.1)	39.2	17.1
Tax	1,984	2,132	1,441	1,963	2,298
Tax rate (%)	30.3	30.4	25.7	25.2	25.2
Reported PAT	4,572	4,871	4,158	5,827	6,820

Balance Sheet

Y/E 31 Mar (Rs mn)	FY18A	FY19A	FY20P	FY21E	FY22E
Equity capital	6,120	6,120	6,121	6,121	6,121
Reserves & surplus	17,533	19,580	19,809	20,725	21,798
Net worth	23,653	25,700	25,931	26,846	27,919
Borrowings	0	0	0	0	0
Other liabilities & provisions	2,918	2,058	2,878	2,950	3,023
Total liabilities and equities	27,225	27,758	28,808	29,796	30,942
Cash & bank balance	16,024	18,328	23,479	24,252	25,174
Fixed & Other assets	2,603	2,568	3,256	3,419	3,590
Total assets	27,225	27,758	28,808	29,796	30,942

Per Share

Y/E 31 Mar (Rs)	FY18A	FY19A	FY20P	FY21E	FY22E
EPS	7.5	8.0	6.8	9.5	11.1
Dividend per share	6.0	6.0	4.7	6.7	7.8
Book value per share	38.6	42.0	42.4	43.9	45.6

Source: Company, BOBCAPS Research

Valuations Ratios

Y/E 31 Mar (x)	FY18A	FY19A	FY20P	FY21E	FY22E
P/E	32.6	30.6	35.9	25.6	21.9
P/BV	6.3	5.8	5.8	5.6	5.3
Dividend yield (%)	2.5	2.5	1.9	2.7	3.2

DuPont Analysis (Bps of AAAUM)

Y/E 31 Mar (bps of AAAUM)	FY18A	FY19A	FY20P	FY21E	FY22E
Operating income	67.5	61.9	57.7	53.1	53.1
Operating expenses	45.9	39.3	28.5	27.4	26.0
EBITDA	21.6	22.6	29.2	25.7	27.0
Depreciation and Others	0.5	0.4	1.9	1.0	0.9
Core PBT	21.2	22.2	27.3	24.7	26.1
Other income	6.7	7.2	(0.5)	8.4	7.7
PBT	27.8	29.3	26.9	33.1	33.8
Tax	8.4	8.9	6.9	8.3	8.5
ROAAAUM	19.4	20.4	19.9	24.7	25.3

Ratio Analysis

Y/E 31 Mar	FY18A	FY19A	FY20P	FY21E	FY22E
YoY growth (%)					
Investment management fees	21.7	(7.1)	(18.6)	4.1	14.4
Core operating profit	9.2	5.8	12.9	(0.5)	20.4
EPS	7.1	6.5	(14.7)	40.2	17.1
Profitability & Return ratios (%)					
Operating income to total income	91.0	89.6	100.8	86.4	87.3
Cost to Core income ratio	68.0	63.5	49.4	51.6	49.1
EBITDA margin	32.0	36.5	50.6	48.4	50.9
Core PBT margin	31.3	35.8	47.3	46.4	49.2
PBT margin (on total income)	37.5	42.4	46.9	53.7	55.6
ROE	21.0	19.7	16.1	22.1	24.9
Dividend payout ratio	96.7	90.9	82.7	84.3	84.3

Annual Average AUM

Y/E 31 Mar (Rs bn)	FY18A	FY19A	FY20P	FY21E	FY22E
AAAUM (Rs Bn)	2,357	2,388	2,084	2,357	2,699
YoY Growth (%)	24.6	1.3	(12.7)	13.1	14.5
% of AAAUM					
Equity	32.4	37.9	43.6	44.8	45.5
Debt	43.6	37.1	22.6	22.4	22.1
Liquid	17.7	17.9	20.0	19.9	19.6
Others	6.3	7.1	13.8	12.8	12.9

Source: Company, BOBCAPS Research

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Recommendations and Absolute returns (%) over 12 months

BUY – Expected return >+15%

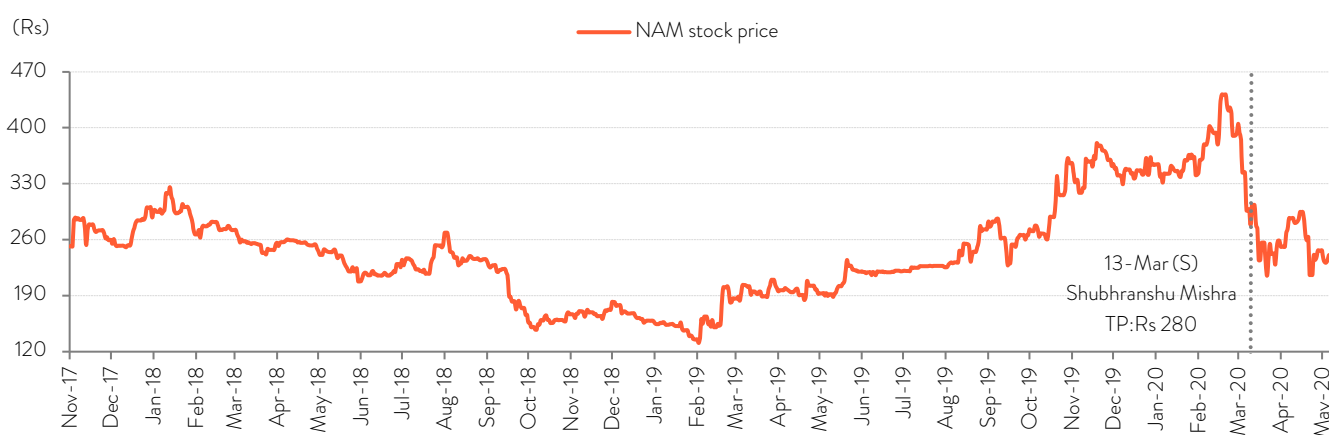
ADD – Expected return from >+5% to +15%

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: NIPPON LIFE INDIA ASSET MANAGEMENT (NAM IN)



B – Buy, A – Add, R – Reduce, S – Sell

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