

Contents

Special Reports

Strategy

Strategy: Slow boil

Daily Alerts

Results

Sun Pharmaceuticals: Operationally in line

Grasim Industries: Strong quarter led by VSF and Chemicals

Tata Chemicals: Consumers hold the key

Godrej Agrovet: A mixed bag

Sunteck Realty: Gearing up

Vardhman Textiles: Weak results

Sadbhav Engineering: Deleveraging benefits

Ashoka Buildcon: Most factors in favor

India Cements: Volumes good, margins weak

Company alerts

ICICI Bank: Revitalizing the bank

Economy alerts

Economy: Input prices' inflation eases on base effect

EQUITY MARKETS

India	Change %			
	14-Aug	1-day	1-mo	3-mo
Sensex	37,852	0.6	3.6	6.5
Nifty	11,435	0.7	3.8	5.9
Global/Regional indices				
Dow Jones	25,162	(0.5)	0.4	1.6
Nasdaq Composite	7,774	(1.2)	(0.4)	5.1
FTSE	7,498	(1.5)	(1.3)	(3.1)
Nikkei	22,179	(0.1)	(1.9)	(2.4)
Hang Seng	27,221	(0.4)	(4.6)	(12.5)
KOSPI	2,240	(0.8)	(3.1)	(8.9)
Value traded – India				
Cash (NSE+BSE)	338		358	334
Derivatives (NSE)	7,495		5,581	4,044
Deri. open interest	4,110		3,743	3,957

Forex/money market

	Change, basis points			
	14-Aug	1-day	1-mo	3-mo
Rs/US\$	70.3	(4)	176	255
10yr govt bond, %	8.1	(1)	(1)	4

Net investment (US\$ mn)

	13-Aug	MTD	CYTD
FIs	(133)	274	(140)
MFs	2	22	11,140

Top movers

Best performers	Change, %			
	14-Aug	1-day	1-mo	3-mo
RCOM IN Equity	21	0.5	71.4	96.7
SUNP IN Equity	602	6.7	12.7	27.6
RIL IN Equity	1,211	1.9	12.5	26.6
DABUR IN Equity	453	2.7	23.3	22.8
SBIN IN Equity	295	0.3	17.2	21.3

Worst performers

JPA IN Equity	13	(0.4)	(7.5)	(26.3)
TTMT/A IN Equity	135	(0.4)	(5.1)	(26.3)
VEDL IN Equity	215	(0.6)	4.2	(22.8)
JSP IN Equity	200	(0.2)	1.8	(21.5)
TTMT IN Equity	249	0.0	(1.3)	(19.8)

August 16, 2018

BSE-30: 37,852

Slow boil. 1QFY19 net profits of the Nifty-50 Index grew 12.3%, 2% above our estimates while net profits of KIE coverage universe grew 12.5%, 14.4% above our expectations due to lower losses of certain PSU banks (ex-financials 0.6% above expectations). We model 20% growth in net profits of the Nifty-50 Index for FY2019 (down from 23% before 1QFY19 results season) and 24% for FY2020. However, valuations are heady and macro weak and faces growing risks from a large number of global issues.

Too many macro variables—hope for the best

We see increased volatility and macro risks over the next few weeks from (1) potential escalation in US-China trade issues, (2) possible ‘hard’ sanctions on Iran leading to sharp decline in Iran oil exports and higher crude oil prices and (3) possible EM contagion given Turkey’s fragile macroeconomic situation and weak macroeconomic positions of several EMs. India’s delicate macroeconomic position will be hurt by higher oil prices given oil’s large influence over CAD/BoP (currency), GFD (bond yields) and inflation (interest rates).

Cyclical recovery versus structural recovery; positive underlying trends in 1QFY19 results

1QFY19 results showed solid improvement in volumes across sectors although the growth figures are flattered by a low base (1QFY18 was pre-GST quarter). We note that 2-year growth numbers (CAGR) are quite mediocre, raising concerns about the strength and sustainability of the ongoing economic recovery, which is led by consumption demand. On the other hand, the Indian banking NPLs seem to be peaking and resolutions moving ahead, a good sign.

Convergence of multiples between ‘growth’ and ‘value’ stocks

We expect further re-rating of certain banks, gas and metal companies on positive sector- and company-specific developments, leading to some convergence between the valuations of the expensive ‘growth’ (‘quality’) stocks and inexpensive ‘value’ stocks. Further deterioration in the macro could delay the ‘convergence’ but also pose risks to rich valuations of ‘growth’ stocks. The market has so far ignored India’s weak macro and rewarded the IT sector with a massive re-rating given currency-led higher earnings. The Indian market has delivered 9% return in INR terms and (-)1% return in USD terms CYTD18, lest we celebrate.

Valuations are rich for the broad market and super-rich for ‘favored’ stocks

The Nifty-50 Index trades at 21.8X FY2019E ‘EPS’, supported by the super-rich valuations of private banks and NBFCs, consumer staple and discretionary stocks and even certain IT stocks. We expect 20% and 24% growth in net profits of the Nifty-50 Index for FY2019 and FY2020, largely driven by banks (rebound in net profits of ‘corporate’ banks), IT, metals & mining and oil & gas. Lower LLPs drive the profits of ‘corporate’ banks and weaker INR of the latter three.

INSIDE

1QFY19 net profits of Nifty-50 Index increased 12.3%, 2% above expectation...pg36

FY2019E net profits of Nifty-50 Index to grow 20%...pg21

Nifty-50 Index trading at 21.8X FY2019E ‘EPS’pg16

Sanjeev Prasad

Sunita Baldawa

Anindya Bhowmik

MARKET VIEW: UNCERTAIN MACRO WITH PLENTIFUL RISKS

The performance of the market for the rest of the year will depend on (1) strength of economic recovery (cyclical versus structural recovery), (2) level of crude oil prices, which will shape India's macro and (3) convergence or divergence of multiples between 'growth' and 'value' stocks. Politics will also become important by the end of the year. The Indian market trades at expensive multiples (19.8X 12-month forward P/E), pulled up by the very high multiples of 'growth' ('quality') stocks.

Weak macro and growing risks

The performance of the Indian market over the next few months would depend on (1) strength of ongoing economic recovery, (2) level of crude oil prices, which will shape India's macro through its influence on CAD, inflation and GFD, (3) global risk sentiment in the context of escalating global trade tensions and growing EM problems and (4) convergence of multiples between 'growth' and 'value' stocks, if any, or continued divergence of multiples between the two buckets of stocks as has been the case for the past several months.

We believe the current economic recovery is somewhat embellished by the low base of 1HCY18, crude prices may have a large influence on India's macro if the Iran-US situation were to deteriorate into 'hard' sanctions on exports of oil from Iran and EM challenges may act as headwinds for the broader market. Nonetheless, multiples between 'growth' and 'quality' stocks may converge on possible sector-specific and stock-specific developments that may give more confidence to the market about 'value' stocks in general.

- ▶ **Cyclical recovery may more accurately describe ongoing economic recovery.** We believe that part of the ongoing economic recovery simply reflects recovery of a low base in 1HCY17 as economic activity was affected by demonetization (announced on November 8, 2016) and GST (implemented from July 1, 2017). We note that the yoy growth for several consumer staple products (staples and discretionary items) has been quite impressive for the past three quarters (3QFY18, 4QFY18 and 1QFY19). In particular, we note that 1QFY18 quarter was the pre-GST quarter and volumes were particularly subdued due to pre-GST de-stocking by the entire manufacturing and distribution chain.

However, the growth is less impressive on a 2-year CAGR basis for the same quarters (see Exhibit 1), which may more accurately represent the real strength of the economic recovery. More importantly, we note that comparisons will become progressively tougher from 2QFY19. Volume growth figures could disappoint versus Street's lofty expectations unless the recovery is led by new job creation and investment and not simply a normalization of demand conditions post the twin 'blows' of demonetization and GST.

Exhibit 1: Volume growth for consumer products is generally unimpressive on a 2-year CAGR basis
Volume growth of automobile and consumer companies, 1QFY17-1QFY19 (%)

	1QFY17	2QFY17	3QFY17	4QFY17	1QFY18	2QFY18	3QFY18	4QFY18	1QFY19	2-y CAGR
Automobiles										
Ashok Leyland	16.8	(12.5)	7.4	9.9	(12.1)	20.3	40.8	24.2	49.9	14.8
Bajaj Auto- 2Ws	13.0	23.5	(3.3)	(11.8)	(22.3)	0.8	1.5	20.4	39.3	4.0
Hero Motocorp	6.6	17.2	(12.7)	(5.8)	6.1	11.3	16.4	22.9	13.7	9.9
Maruti Suzuki	5.4	18.5	3.9	14.8	14.3	19.4	12.4	11.6	25.9	20.0
Mahindra & Mahindra	13.4	16.4	(11.7)	(9.1)	(6.0)	16.9	1.5	10.0	9.0	1.2
Consumer staples										
Bajaj Corp. - Almond Drop Hair Oil	2.2	1.6	1.6	(7.1)	(6.6)	6.5	4.5	6.9	11.2	1.9
Britannia Industries - Domestic	8.0	8.0	2.0	2.0	2.0	6.0	13.0	12.5	12.0	6.9
Colgate - Overall	6.0	4.0	4.0	(3.0)	(5.0)	(1.0)	12.0	4.0	4.0	(0.6)
Colgate - Toothpaste	5.0	4.0	4.0	(3.0)	(5.0)	(1.0)	12.0	4.0	4.0	(0.6)
Dabur - Domestic	4.1	4.5	4.5	2.4	(4.4)	7.2	13.0	7.7	21.0	7.6
GSK Consumer	0.0	(3.0)	(17.0)	(0.7)	(3.0)	2.4	17.0	8.0	12.8	4.6
GCPL - Soaps	10.0	(5.0)	(5.0)	5.0	(8.0)	12.0	15.0	12.0	12.0	1.5
HUL (FMCG business)	4.0	(1.0)	(1.0)	4.0	—	4.0	11.0	11.0	12.0	5.8
Marico - Domestic	8.0	3.4	3.4	10.0	(4.0)	8.5	9.4	1.0	12.4	3.9
Marico - Parachute	7.0	(6.0)	(6.0)	15.0	(5.0)	8.0	15.0	(5.0)	9.0	1.8
Marico - Saffola	11.0	8.0	8.0	6.0	(3.0)	9.0	—	(1.0)	10.0	3.3
Marico - Value-added hair oils	9.0	11.0	11.0	10.0	(6.0)	8.0	8.0	11.0	15.0	4.0
Consumer discretionary										
Asian Paints	12.0	12.0	12.0	9.0	2.0	9.0	6.0	10.0	13.0	7.4
ITC - Cigarettes	3.0	4.0	4.0	—	2.0	(8.0)	(5.0)	(5.0)	1.0	1.5
Jubilant Foodworks - SSG	(3.2)	4.2	4.2	(7.5)	6.5	5.5	17.8	26.5	25.9	15.8
Pidilite - Domestic consumer business	9.0	7.8	7.8	6.0	—	15.0	23.0	13.0	20.0	9.5
Titan - Jewelry	6.0	(32.0)	(32.0)	37.0	49.0	49.0	6.0	6.0	(2.6)	20.5

Source: Companies, Kotak Institutional Equities

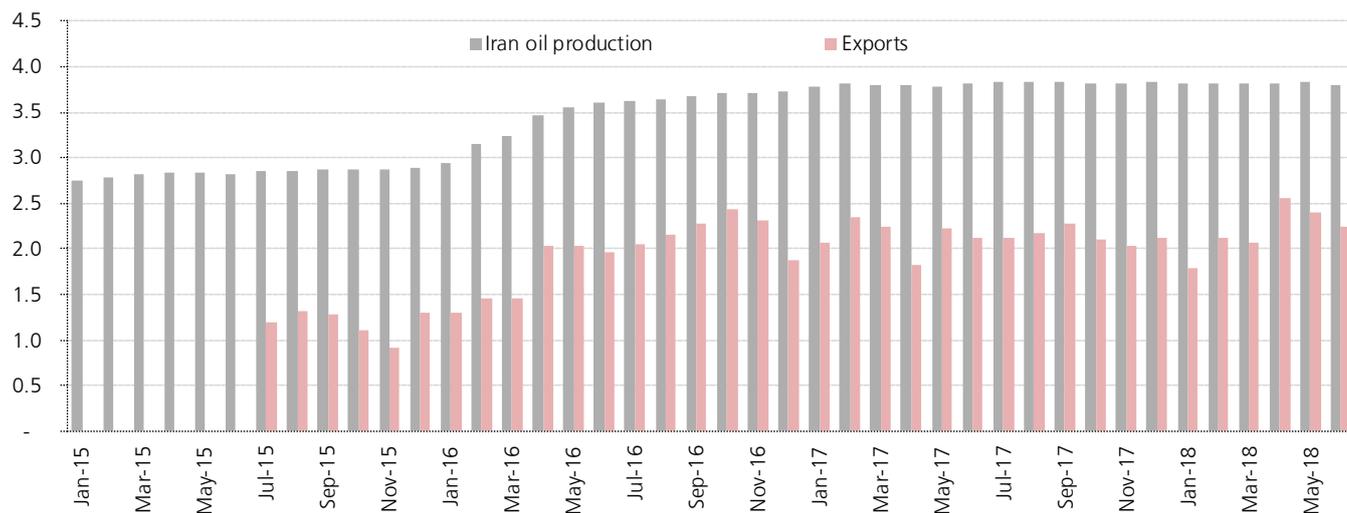
It would be interesting to see how the market reacts to weaker yoy growth numbers from 2QFY19 onwards. In our view, the expansion in the multiples of the 'growth' stocks may also represent a more expansive view of growth by the market, buoyed by the strong yoy growth in volumes for the past three quarters.

- ▶ **Crude prices may spike if the US was to impose 'hard' sanctions on Iran.** We note that any 'hard' sanctions by the US government on oil exports from Iran may result in a dramatic decline in Iran oil exports, which will upset global oil supply-demand balance. The next phase of US sanctions effective November 5, 2018 specifically target Iran's oil industry and among other things include sanctions against (1) purchase of oil from National Iranian Oil Company and other Iranian oil & gas companies and (2) transactions by foreign financial institutions with the Central Bank of Iran and designated Iranian financial institutions.

We note that Iran's oil exports of 2.2 mn b/d in 1HCY18 (see Exhibit 2 for Iran's production and exports of oil since January 2015) is quite large compared to available spare capacity of the OPEC (see Exhibit 3 for global oil supply-demand balance and OPEC spare capacity). Other oil producers may find it hard to offset any cut in Iran oil exports beyond 0.5 mn b/d. The continued decline in Venezuela oil production (see Exhibit 4) may further aggravate global oil supply.

Exhibit 2: Iran's oil exports are at 2.2 mn b/d in 1H CY18

Monthly production and exports from Iran, calendar year-ends, 2015-18 (mn b/d)



Source: OPEC, Kotak Institutional Equities

Exhibit 3: OPEC implied spare capacity could decline sharply with lower Iran oil production

Estimated global crude demand, supply and prices, calendar year-ends, 2012-22E

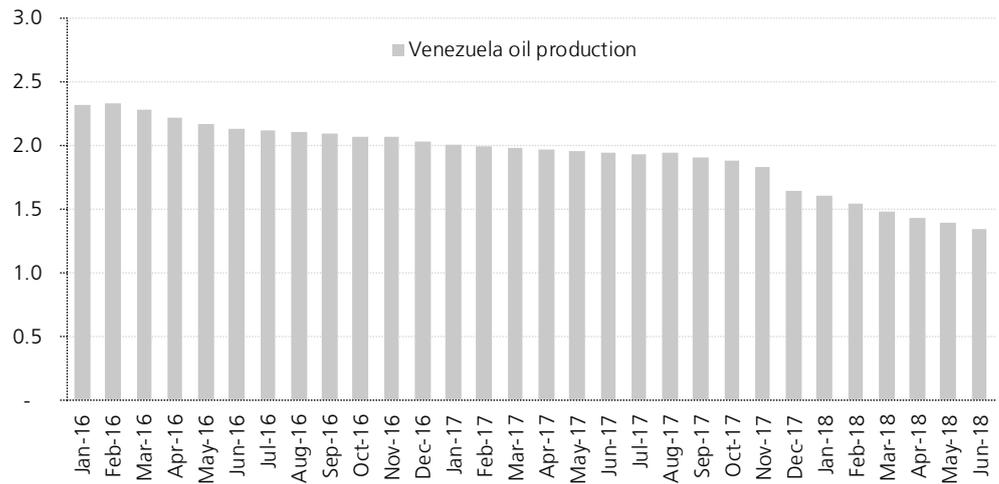
	2012	2013	2014	2015	2016	2017	2018E	2019E	2020E	2021E	2022E
Demand (mn b/d)											
Total demand	90.7	91.7	93.0	95.0	96.2	97.7	99.1	100.5	101.6	102.6	103.7
Yoy growth	1.2	1.1	1.2	2.0	1.2	1.5	1.4	1.4	1.2	1.0	1.1
Supply (mn b/d)											
Non-OPEC	52.5	54.5	57.0	58.1	57.4	58.2	60.2	62.0	62.4	62.8	63.2
Yoy growth	(0.4)	2.1	2.4	1.1	(0.7)	0.8	2.0	1.8	0.3	0.4	0.4
OPEC											
Crude	32.1	30.6	30.5	31.8	32.8	32.3	32.0	32.0	32.0	32.0	32.0
NGLs	6.4	6.2	6.3	6.6	6.8	6.9	6.9	7.0	7.1	7.2	7.3
Total OPEC	38.4	36.8	36.8	38.4	39.6	39.2	38.9	39.0	39.1	39.2	39.3
Total supply	90.9	91.3	93.7	96.5	97.0	97.4	99.1	101.1	101.5	102.0	102.5
Total stock change	0.2	(0.5)	0.7	1.5	0.8	(0.3)	0.0	0.6	(0.1)	(0.6)	(1.2)
OPEC crude capacity	35.8	35.2	35.2	35.2	35.9	35.6	35.1	34.9	35.9	36.0	36.2
Implied spare capacity	3.9	4.1	5.5	4.8	3.9	2.9	3.1	3.5	3.7	3.4	3.0
Demand growth (yoy, %)											
	1.3	1.2	1.4	2.2	1.2	1.6	1.4	1.4	1.1	1.0	1.1
Supply growth (yoy, %)											
Non-OPEC	(0.8)	3.9	4.5	1.9	(1.2)	1.5	3.4	3.1	0.5	0.7	0.7
OPEC	7.4	(4.4)	0.0	4.5	3.1	(1.0)	(0.7)	0.2	0.3	0.1	0.2
Total	2.5	0.4	2.7	2.9	0.5	0.5	1.8	1.9	0.4	0.5	0.5
Dated Brent (US\$/bbl)											
	112	109	99	52	44	54	57	73	68	65	65
World GDP growth (%)											
	3.4	3.3	3.6	3.4	3.2	3.7	3.9	3.9	3.7	3.8	3.8

Notes:

(a) OPEC production data includes Indonesia in 2012 and Gabon from 2013 onwards.

Source: IEA, Kotak Institutional Equities estimates

Exhibit 4: Sharp decline in oil production from Venezuela due to ongoing socioeconomic crisis
 Monthly production of crude oil in Venezuela, January 2016 onwards (mn b/d)



Source: OPEC, Kotak Institutional Equities

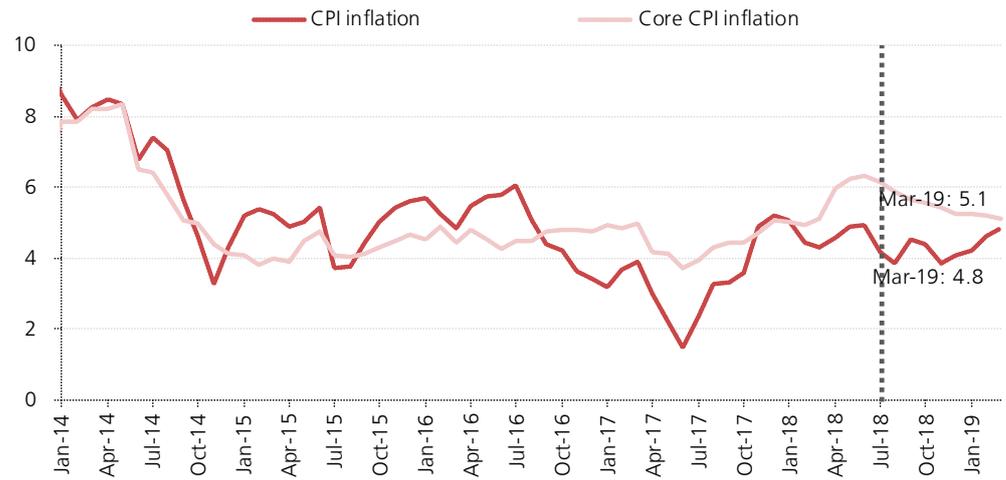
India's macro position would worsen if oil prices were to shoot above US\$80/bbl. We note that a US\$10/bbl change in crude oil prices results in (1) 50 bps impact on CAD/GDP; we model 2.8% CAD/GFD at US\$72.5/bbl Dated Brent crude price; see Exhibit 5, (2) 30 bps impact on inflation; we model 4.6% average CPI inflation for FY2019; see Exhibit 6 and (3) modest impact on GFD through higher subsidies on kerosene and LPG; we model gross under-recoveries at ₹460 bn versus the government's provision of ₹265 bn. GFD could rise further if the government was to reduce taxes on diesel and gasoline in order to mitigate the impact of higher oil prices.

Exhibit 5: India's external vulnerabilities will be higher at higher oil prices
India's balance of payments, March fiscal year-ends, 2014-19E (US\$ bn)

	2014	2015	2016	2017	2018	2019E		
						Oil@67.5/bbl	Oil@72.5/bbl	Oil@80/bbl
Current account	(32.4)	(26.8)	(22.2)	(15.3)	(48.7)	(70.8)	(78.2)	(89.5)
GDP	1,858	2,038	2,103	2,270	2,602	2,758	2,758	2,758
CAD/GDP (%)	(1.7)	(1.3)	(1.1)	(0.7)	(1.9)	(2.6)	(2.8)	(3.2)
Trade balance	(147.6)	(144.9)	(130.1)	(112.4)	(160.0)	(186.5)	(194.0)	(205.2)
Trade balance/GDP (%)	(7.9)	(7.1)	(6.2)	(4.9)	(6.2)	(6.8)	(7.0)	(7.4)
- Exports	319	317	266	280	309	331	334	337
- oil exports	63	57	31	32	39	41	43	47
- non-oil exports	255	260	236	249	270	290	290	290
- Imports	466	461	396	393	469	518	528	542
- oil imports	165	138	83	87	109	132	142	157
- non-oil imports	301	323	313	306	360	386	386	386
- gold imports	29	34	32	28	34	34	34	34
Invisibles (net)	115	118	108	97	111	116	116	116
- Services	73	77	70	67	78	80	80	80
- software	67	70	71	70	72	74	74	74
- non-software	6.0	6.2	(1.8)	(2.6)	5.4	5.5	5.5	5.5
- Transfers	65	66	63	56	62	66	66	66
- Income (net)	(23)	(24)	(24)	(26)	(29)	(30)	(30)	(30)
Capital account	48.8	89.3	41.1	36.5	91.4	42.0	42.0	42.0
Percentage of GDP	2.6	4.4	2.0	1.6	3.5	1.5	1.5	1.5
Foreign investment	26	73	32	43	52	20	20	20
- FDI	22	31	36	36	30	30	30	30
- FPI	5	42	(4)	8	22	(10)	(10)	(10)
- Equities	14	15	(4)	9	2	(2)	(2)	(2)
- Debt	(8)	26	(0)	(1)	21	(8)	(8)	(8)
Banking capital	25	12	11	(17)	16	12	12	12
- NRI deposits	39	14	16	(12)	10	9	9	9
Short-term credit	(5.0)	(0.1)	(1.6)	6.5	13.9	6.0	6.0	6.0
ECBs	11.8	1.6	(4.5)	(6.1)	(0.2)	2.0	2.0	2.0
External assistance	1.0	1.7	1.5	2.0	2.9	2.0	2.0	2.0
Other capital account items	(10.8)	1.1	3.3	7.6	6.2	—	—	—
E&O	(0.9)	(1.1)	(1.1)	0.4	0.9	—	—	—
Overall balance	15.6	61.4	17.9	21.6	43.6	(28.8)	(36.2)	(47.5)
Memo items								
Average USD/INR	60.5	61.2	65.4	67.2	64.5	67.6	67.6	67.6
Average Brent (US\$/bbl)	107.6	86.5	47.5	49.0	57.6	67.5	72.5	80.0

Source: RBI, Kotak Institutional Equities estimates

Exhibit 6: Upside risks to inflation from crude price, INR weakness and higher-than-usual MSP hikes
Headline and core CPI inflation (%)



Source: CEIC, Kotak Institutional Equities estimates

In our view, valuations of several stocks could see a de-rating in case (1) India's macroeconomic conditions were to deteriorate on the back of significantly higher crude oil prices (US\$15/bbl or more from current levels) and/or (2) earnings were to disappoint. The market perhaps believes that India's macroeconomic situation will improve over the next few months and/or earnings growth would be strong enough to offset any macro-related concerns including higher interest rates/cost of capital.

- ▶ **EM contagion (if any).** The market would also have to contend with (1) any contagion effect of the troubles in the Turkish economy with rapid deterioration in the macroeconomic position of the country and (2) weakness in global economy on escalation of global trade issues, which could result in a risk-off sentiment for EMs. As such, EMs have been very poor performers over the past year or so, lagging the strong performance in DMs and US markets (see Exhibit 7).

Exhibit 7: Emerging markets have massively underperformed developed markets in the past year
Performance (not annualized) of emerging and developed markets over period of time (%)

	% change in local currency							% change in USD						
	1-mo	3-mo	6-mo	YTD	1-yr	3-yr	5-yr	1-mo	3-mo	6-mo	YTD	1-yr	3-yr	5-yr
Developed markets														
Australia	0	3	8	4	10	18	22	(1)	0	(0)	(3)	2	16	(3)
France	(0)	(2)	6	2	6	9	33	(2)	(6)	(2)	(3)	2	12	14
Germany	(1)	(4)	2	(4)	2	13	48	(3)	(8)	(6)	(9)	(1)	16	27
Hong Kong	(3)	(11)	(7)	(7)	2	16	23	(3)	(11)	(7)	(8)	1	14	22
Japan	(1)	(2)	5	(2)	14	9	63	0	(3)	2	(0)	13	22	43
Singapore	(1)	(8)	(5)	(5)	(2)	4	1	(1)	(10)	(9)	(7)	(3)	6	(7)
UK	(0)	(1)	7	(1)	4	17	18	(3)	(6)	(2)	(6)	2	(5)	(3)
US (Dow Jones)	1	2	2	2	15	44	67	1	2	2	2	15	44	67
US (S&P500)	1	4	6	6	14	35	70	1	4	6	6	14	35	70
MSCI World								(0)	0	2	1	9	22	41
Emerging markets														
Brazil	1	(9)	(4)	1	13	63	52	(0)	(15)	(19)	(14)	(8)	44	(9)
MSCI China	(5)	(13)	(9)	(8)	4	25	37	(5)	(13)	(10)	(9)	3	24	36
India	4	6	8	9	17	34	99	2	3	(0)	(1)	7	25	74
Indonesia	(3)	(1)	(12)	(9)	(1)	26	23	(4)	(4)	(18)	(15)	(9)	19	(12)
Korea	(2)	(8)	(6)	(8)	(3)	14	17	(2)	(12)	(9)	(13)	(2)	19	16
Malaysia	4	(3)	(3)	(1)	1	12	(0)	2	(7)	(6)	(2)	6	11	(20)
Mexico	1	5	2	(1)	(5)	11	16	(1)	7	(2)	1	(12)	(5)	(23)
Philippines	2	(5)	(12)	(12)	(5)	2	14	2	(6)	(15)	(18)	(9)	(12)	(6)
Russia	(10)	(9)	(12)	(7)	4	29	(19)	(10)	(9)	(12)	(7)	4	29	(19)
Taiwan	(0)	(0)	4	2	6	30	37	(1)	(3)	(1)	(2)	4	36	34
Thailand	3	(4)	(6)	(3)	9	20	17	3	(7)	(11)	(5)	8	27	10
MSCI EM								(3)	(9)	(10)	(10)	(1)	21	9

Source: Bloomberg, Kotak Institutional Equities

A further strengthening of the US dollar relative to EM currencies on the back of continued strength in the US economy (see Exhibit 8) and subsequent rate hikes by the US Fed could further weigh on EMs. Many EMs face different challenges ranging from (1) threat of further US sanctions (Russia, Turkey) to vigorous US trade actions (China), (2) high overall and external debt relative to the size of the GDP (many EMs) and (3) high CAD and GFD (Argentina, Brazil, India, South Africa, Turkey).

Exhibit 8: Recent data shows steady growth in the US economy
Trend in key economic variables for the US economy

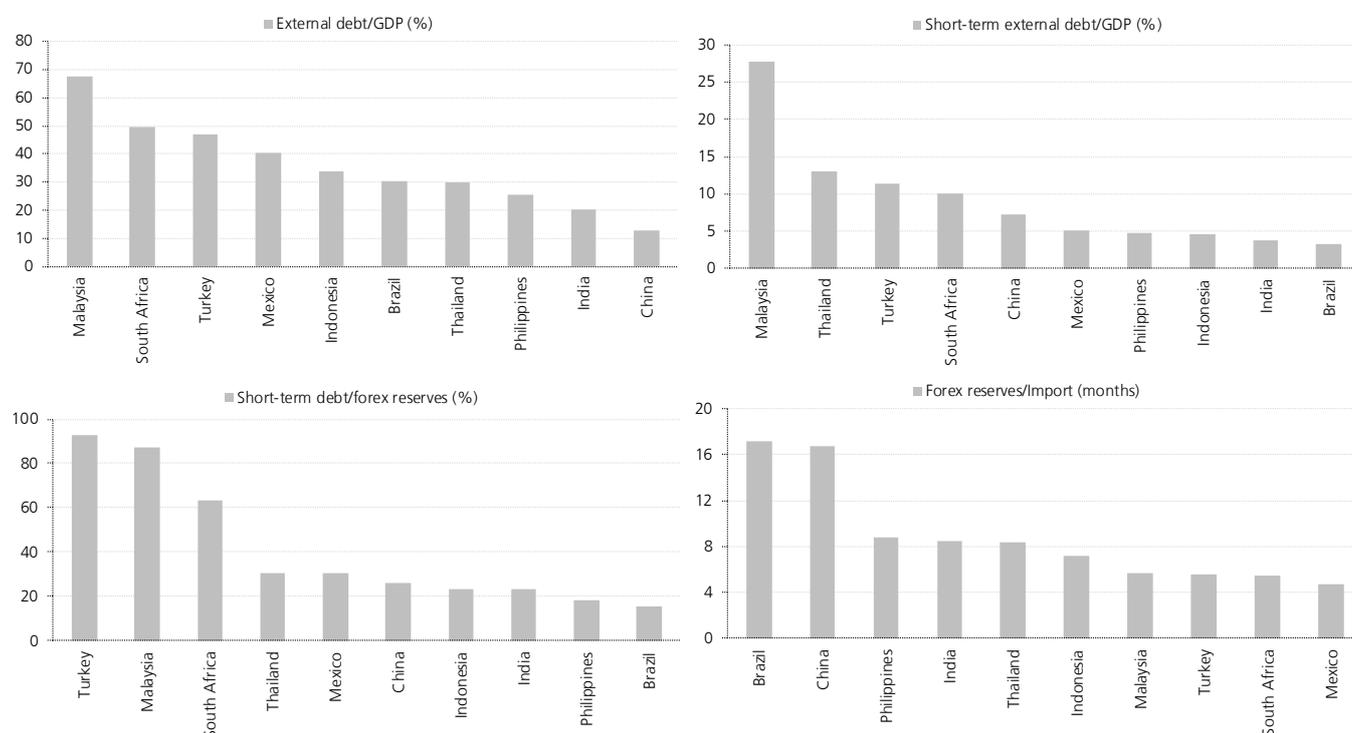
Monthly indicators	Jul-17	Aug-17	Sep-17	Oct-17	Nov-17	Dec-17	Jan-18	Feb-18	Mar-18	Apr-18	May-18	Jun-18	Jul-18
Average private earnings (yoy, %)	2.6	2.6	2.8	2.4	2.4	2.7	2.8	2.6	2.7	2.6	2.7	2.7	2.7
Conference Board consumer confidence (X)	120.0	120.4	120.6	126.2	128.6	123.1	125.4	130.8	127.7	125.6	128.0	126.4	127.4
Core PCE (yoy, %)	1.4	1.3	1.4	1.4	1.5	1.5	1.5	1.5	1.8	1.8	2.0	1.9	
CPI (yoy, %)	1.7	1.9	2.2	2.0	2.2	2.1	2.1	2.2	2.4	2.5	2.8	2.8	2.9
Core CPI (yoy, %)	1.7	1.7	1.7	1.8	1.7	1.8	1.8	1.8	2.1	2.1	2.2	2.3	2.3
Housing starts (SAAR, '000)	1,185	1,172	1,158	1,265	1,303	1,210	1,334	1,290	1,327	1,276	1,337	1,173	
Industrial production (yoy, %)	1.6	0.9	1.1	2.6	3.5	3.1	3.2	3.8	3.6	4.7	3.2	3.6	
ISM manufacturing (X)	56.3	58.8	60.8	58.7	58.2	59.3	59.1	60.8	59.3	57.3	58.7	60.2	58.1
ISM non-manufacturing (X)	53.9	55.3	59.8	60.1	57.4	55.9	59.9	59.5	58.8	56.8	58.6	59.1	55.7
Non-farm payrolls ('000)	190	221	14	271	216	175	176	324	155	175	268	248	157
Participation rate (%)	62.9	62.9	63.1	62.7	62.7	62.7	62.7	63	62.9	62.8	62.7	62.9	62.9
Personal savings rate (% of disposable income)	3.5	3.5	3.0	3.0	2.6	2.5	3.0	3.3	3.2	3.0	3.2		
Retail sales excl. automobiles (sa, yoy, %)	3.7	4.6	5.7	5.5	7.1	6.3	4.8	5.7	5.3	5.1	7.1	7.0	
S&P house price index (yoy, %)	5.8	5.8	6.2	6.4	6.4	6.3	6.4	6.7	6.7	6.7	6.5		
Unemployment rate (%)	4.3	4.4	4.2	4.1	4.1	4.1	4.1	4.1	4.1	3.9	3.8	4.0	3.9
Quarterly indicators	Mar-16	Jun-16	Sep-16	Dec-16	Mar-17	Jun-17	Sep-17	Dec-17	Mar-18	Jun-18			
CAD/GDP (%)	(2.4)	(2.4)	(2.4)	(2.4)	(2.3)	(2.4)	(2.3)	(2.4)	(2.3)				
GFD/GDP (%)	(2.5)	(2.8)	(3.1)	(3.1)	(3.4)	(3.7)	(3.4)	(3.4)	(3.7)	(3.7)			
Real GDP (SAAR, qoq, %)	0.6	2.2	2.8	1.8	1.2	3.1	2.8	2.3	2.2	4.1			

Source: Bloomberg, CEIC, Kotak Institutional Equities

On the external front, India is relatively better off with low external debt-to-GDP and short-term external debt-to-GDP ratios (see Exhibit 9 for a summary of India's external debt position relative to other EMs) versus other EMs although it does have a relatively high CAD (see Exhibit 10), which could worsen if crude oil prices were to rise substantially from current levels. India also has persistently high GFD although this is less of an issue in the current macro-environment with more external than internal challenges. Lastly, most of India's public debt is financed by internal borrowings.

Exhibit 9: India's external debt position superior to other EM countries

External debt/GDP, short-term debt/GDP, short-term debt/forex reserves and forex reserves/imports of various countries, calendar year-end, 2017 (%)



Notes:

(a) Short-term debt is on the basis of original maturity. In most cases, actual short-term debt repayment (within one year) based on residual maturity of debt will be higher.

Source: World Bank, RBI, Kotak Institutional Equities

Exhibit 10: India has a high CAD/GDP ratio compared to other economies

CAD/GDP ratio, calendar year-ends, 2009-19E (%)

	2009	2010	2011	2012	2013	2014	2015	2016	2017E	2018E	2019E
Argentina	2.2	(0.4)	(1.0)	(0.4)	(2.1)	(1.6)	(2.7)	(2.7)	(4.8)	(5.1)	(5.5)
Brazil	(1.6)	(3.4)	(2.9)	(3.0)	(3.0)	(4.2)	(3.3)	(1.3)	(0.5)	(1.6)	(1.8)
China	4.8	3.9	1.8	2.5	1.5	2.2	2.7	1.8	1.4	1.2	1.2
India	(2.8)	(2.8)	(4.3)	(4.8)	(1.7)	(1.3)	(1.1)	(0.7)	(2.0)	(2.3)	(2.1)
Indonesia	1.8	0.7	0.2	(2.7)	(3.2)	(3.1)	(2.0)	(1.8)	(1.7)	(1.9)	(1.9)
Korea	3.7	2.6	1.6	4.2	6.2	6.0	7.7	7.0	5.1	5.5	5.8
Malaysia	15.0	10.1	10.9	5.2	3.5	4.4	3.0	2.4	3.0	2.4	2.2
Mexico	(0.9)	(0.5)	(1.0)	(1.5)	(2.4)	(1.8)	(2.5)	(2.1)	(1.6)	(1.9)	(2.2)
Philippines	5.0	3.6	2.5	2.8	4.2	3.8	2.5	(0.3)	(0.4)	(0.5)	(0.6)
Russia	3.8	4.1	4.7	3.2	1.5	2.8	5.0	2.0	2.6	4.5	3.8
South Africa	(2.7)	(1.5)	(2.2)	(5.1)	(5.9)	(5.3)	(4.4)	(3.3)	(2.3)	(2.9)	(3.1)
Taiwan	10.4	8.3	7.8	8.9	10.0	11.7	14.3	13.6	13.8	13.6	13.5
Thailand	7.9	3.4	2.5	(0.4)	(1.2)	3.7	8.0	11.7	10.8	9.3	8.6
Turkey	(1.8)	(5.8)	(8.9)	(5.5)	(6.7)	(4.7)	(3.7)	(3.8)	(5.5)	(5.4)	(4.8)

Notes:

(a) Data for India as of March fiscal year-ends.

Source: IMF, Kotak Institutional Equities

- ▶ **Politics—market seems quite relaxed about it.** The market will increasingly focus on three state elections (Chhattisgarh, Madhya Pradesh and Rajasthan), which are due in December 2018/January 2019 where BJP is the incumbent ruling party. These states were also big contributors to the BJP's strong performance in the 2014 general elections.

A favorable outcome for the BJP in the state elections will assuage any residual concerns about the performance of the BJP in the next general elections (due in April/May 2019) and the electoral prospects of the BJP and the ruling-coalition (NDA) post its recent electoral losses in by-elections to the lower house of parliament and in the Karnataka state elections. However, the market could get jittery if the BJP were to lose two states while the loss of three states would be a catastrophic event for the market.

A weak performance of the BJP in the forthcoming state elections (although less likely) would intensify speculation about the electoral prospects of the BJP in the 2019 elections, especially if national and regional opposition political parties were to form opportunistic alliances against the BJP in the forthcoming general elections, drawing from the template of the Karnataka state election where the second- and third-largest parties (INC and JD(S)) combined to form a government at the expense of the BJP despite the BJP being the largest party with 104 seats in the 222-seat state assembly.

As of now, the market firmly believes that the same BJP-led coalition will form the next government too albeit with fewer seats for the BJP. We note that the BJP has a slender majority in the lower house of parliament currently (it lost a few seats in recent by-elections) and its utter dominance in several states makes it vulnerable to loss of a few seats in those states (see Exhibit 11).

Exhibit 11: BJP crosses half-way mark of 272 seats on its own
Current number of seats in Lok Sabha by states

Name of state	Members	INC	BJP
Andhra Pradesh	25	0	2
Arunachal Pradesh	2	1	1
Assam	14	3	7
Bihar	40	2	22
Chhattisgarh	11	1	10
Goa	2	0	2
Gujarat	26	0	26
Haryana	10	1	7
Himachal Pradesh	4	0	4
Jammu and Kashmir	6	0	3
Jharkhand	14	0	12
Karnataka	28	9	15
Kerala	20	8	0
Madhya Pradesh	29	3	26
Maharashtra	48	2	22
Manipur	2	2	0
Meghalaya	2	1	0
Mizoram	1	1	0
Nagaland	1	0	0
Odisha	21	0	1
Punjab	13	4	1
Rajasthan	25	2	23
Sikkim	1	0	0
Tamil Nadu	39	0	1
Telangana	17	0	1
Tripura	2	0	0
Uttar Pradesh	80	2	68
Uttarakhand	5	0	5
West Bengal	42	4	2
Name of UT			
Andaman and Nicobar Islands	1	0	1
Chandigarh	1	0	1
Dadra and Nagar Haveli	1	0	1
Daman and Diu	1	0	1
Delhi	7	0	7
Lakshadweep	1	1	0
Puducherry	1	1	0
Total	543	48	272
Chhattisgarh, Gujarat, MP, Rajasthan and UP	171	8	153

Source: Lok Sabha, Kotak Institutional Equities

Valuations are expensive for the market as a whole

We find the valuations of the Indian market to be rich (see Exhibit 12) and note the significant disconnect between high equity market valuations and weak macroeconomic outlook, as can be seen in the divergence between bond and equity yields (see Exhibit 13).

Exhibit 12: We expect earnings of the Nifty-50 Index to grow 19% in FY2019 and 24% in FY2020

Valuation summary of Nifty-50 sectors (full-float basis), March fiscal year-ends, 2018-20E (based on current constituents)

	Mcap.	Adj. mcap.	Earnings growth (%)			PER (X)			EV/EBITDA (X)			Price/BV (X)			Div. yield (%)			RoE (%)		
	(US\$ bn)	(US\$ bn)	2018	2019E	2020E	2018	2019E	2020E	2018	2019E	2020E	2018	2019E	2020E	2018	2019E	2020E	2018	2019E	2020E
Automobiles	99.3	54.6	(1.5)	15.0	26.8	24.3	21.2	16.7	10.3	9.0	7.4	3.4	3.1	2.7	1.0	1.0	1.2	14.1	14.5	16.2
Banking	330.4	245.9	(16.9)	44.8	72.9	43.3	29.9	17.3	—	—	—	3.3	2.9	2.5	0.6	0.6	0.9	7.6	9.6	14.6
Cement	26.2	9.9	(4.4)	23.8	30.9	33.1	26.7	20.4	16.2	10.3	9.0	2.2	2.0	1.9	0.3	0.3	0.3	6.6	7.7	9.2
Consumers	138.9	70.2	13.4	14.8	14.2	50.2	43.7	38.3	34.0	29.0	25.2	13.5	12.4	11.3	1.2	1.3	1.6	26.9	28.3	29.5
Energy	185.2	77.5	(0.2)	7.4	5.0	13.5	12.6	12.0	8.8	7.6	7.1	1.8	1.6	1.5	2.4	2.0	2.1	13.1	12.9	12.4
Industrials	25.1	22.1	22.4	21.7	10.9	24.2	19.9	18.0	20.3	16.1	15.5	3.5	3.2	2.9	1.3	1.8	2.0	14.5	16.0	16.0
Infrastructure	11.1	4.1	(2.1)	1.2	21.1	20.2	19.9	16.5	13.6	13.6	11.3	3.7	3.2	2.7	0.5	0.5	0.5	18.2	15.8	16.4
Media	7.1	4.0	7.8	11.3	17.0	34.2	30.7	26.3	22.2	19.1	16.1	6.5	5.8	5.1	0.5	0.9	1.1	19.1	18.8	19.3
Metals & Mining	53.1	22.2	24.5	56.8	10.9	13.3	8.5	7.6	7.4	5.6	5.1	1.8	1.6	1.5	3.9	4.7	5.7	13.9	19.4	19.9
Pharmaceuticals	38.9	21.0	(33.8)	11.9	38.3	35.0	31.3	22.6	19.4	16.4	12.2	3.4	3.1	2.8	0.6	0.6	0.8	9.8	10.0	12.4
Others	4.4	3.2	21.1	14.0	12.1	14.2	12.5	11.1	9.9	8.5	7.2	3.4	2.8	2.3	1.3	1.6	1.8	23.9	22.4	21.0
Technology	200.5	84.8	1.0	12.6	9.4	23.0	20.4	18.7	16.7	14.0	12.7	5.5	4.9	4.5	1.3	2.0	3.2	23.9	23.8	24.2
Telecom	28.5	10.1	(26.8)	(97.2)	373.6	44.9	1,626.1	343.4	8.1	9.3	8.1	2.3	2.4	2.5	2.4	1.2	0.7	5.1	0.1	0.7
Utilities	32.5	12.7	(0.3)	25.5	8.5	12.9	10.3	9.5	9.7	7.9	7.2	1.5	1.3	1.2	3.3	3.1	3.3	11.3	13.0	13.0
Nifty-50 Index	1,181	642	(2.1)	19.7	23.6	24.6	20.5	16.6	12.0	10.1	9.1	3.1	2.8	2.5	1.4	1.5	1.9	12.6	13.6	15.3
Nifty-50 Index (ex-energy)	996	565	(2.9)	24.6	29.9	29.0	23.3	17.9	13.6	11.3	10.0	3.6	3.2	2.9	1.2	1.4	1.8	12.5	13.9	16.3

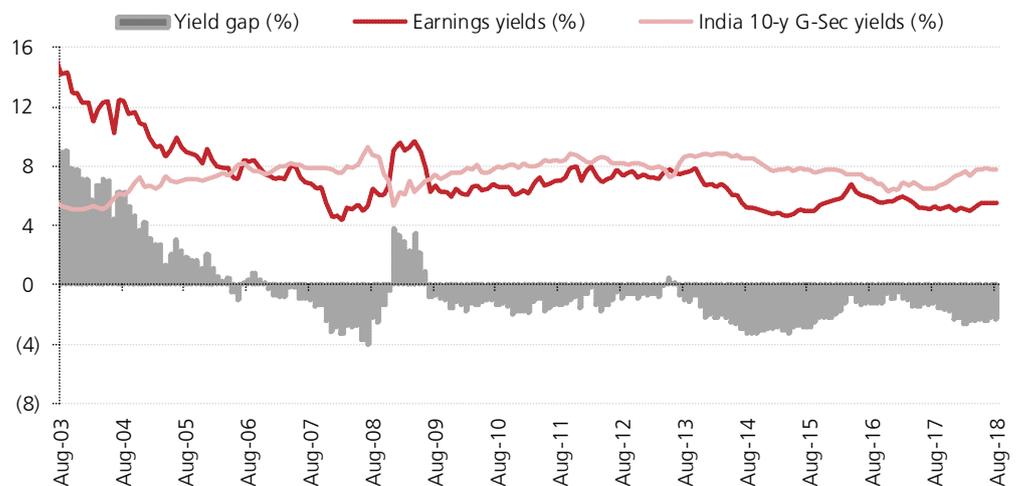
Notes:

(a) We used consensus numbers for Indiabulls Housing Finance and Kotak Mahindra Bank.

Source: Kotak Institutional Equities estimates

Exhibit 13: Earnings yields have been broadly stable over the past several months despite a sharp increase in bond yields

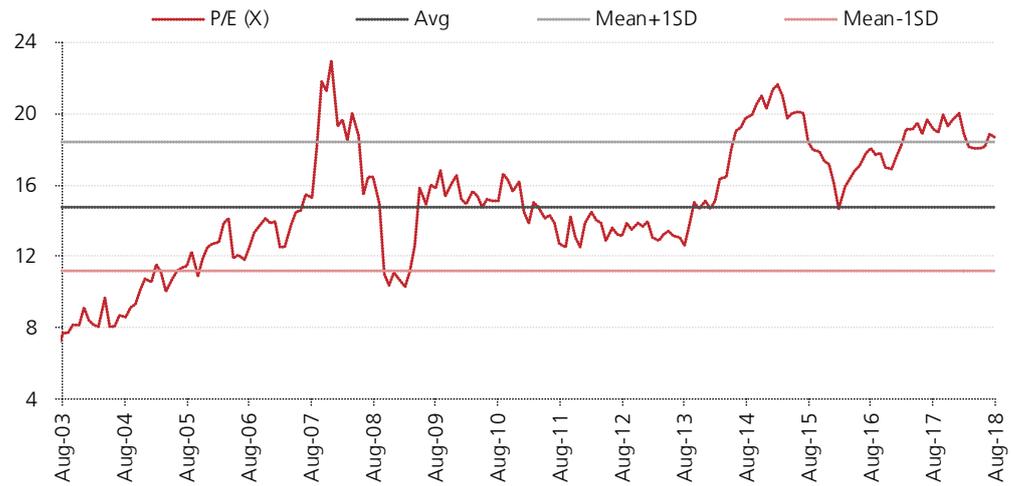
Nifty earnings yield and bond yield, March fiscal year-ends, 2004-19 (%)



Source: Bloomberg

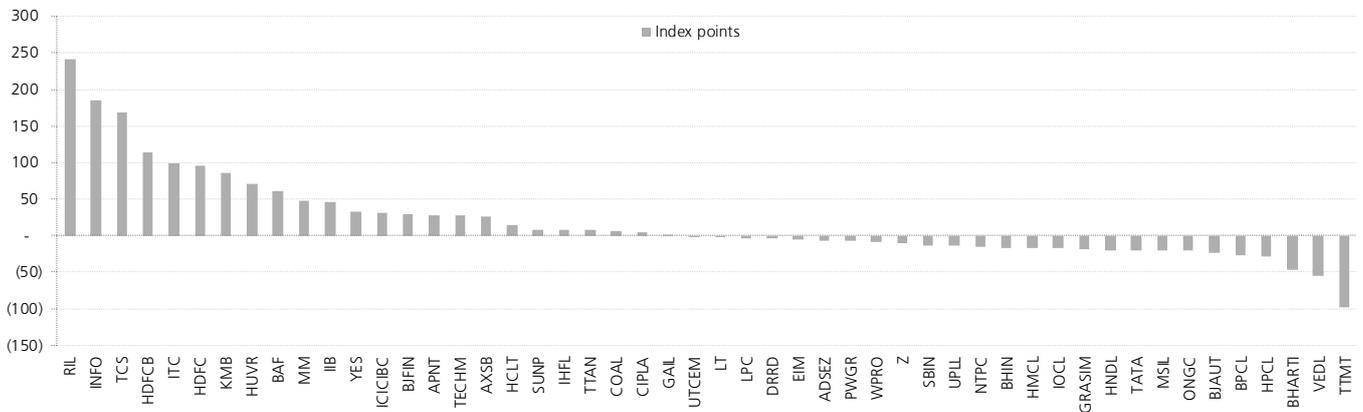
The Indian market has traded historically at much lower levels (see Exhibit 14 for the 12-month forward valuation parameters on full-float basis). We note that the market's (1) recent performance (see Exhibit 15 for contribution of various stocks to the Nifty-50 index's CYTD performance) has been driven by and (2) expensive valuations are supported by rich valuations of certain stocks in the private financials, consumer staples and discretionary sectors, RIL and IT stocks.

Exhibit 14: Valuation of the Indian market is well above historical levels
12-m rolling forward PE of Nifty-50 Index, March fiscal year-ends, 2004-19 (X)



Source: Bloomberg, Kotak Institutional Equities

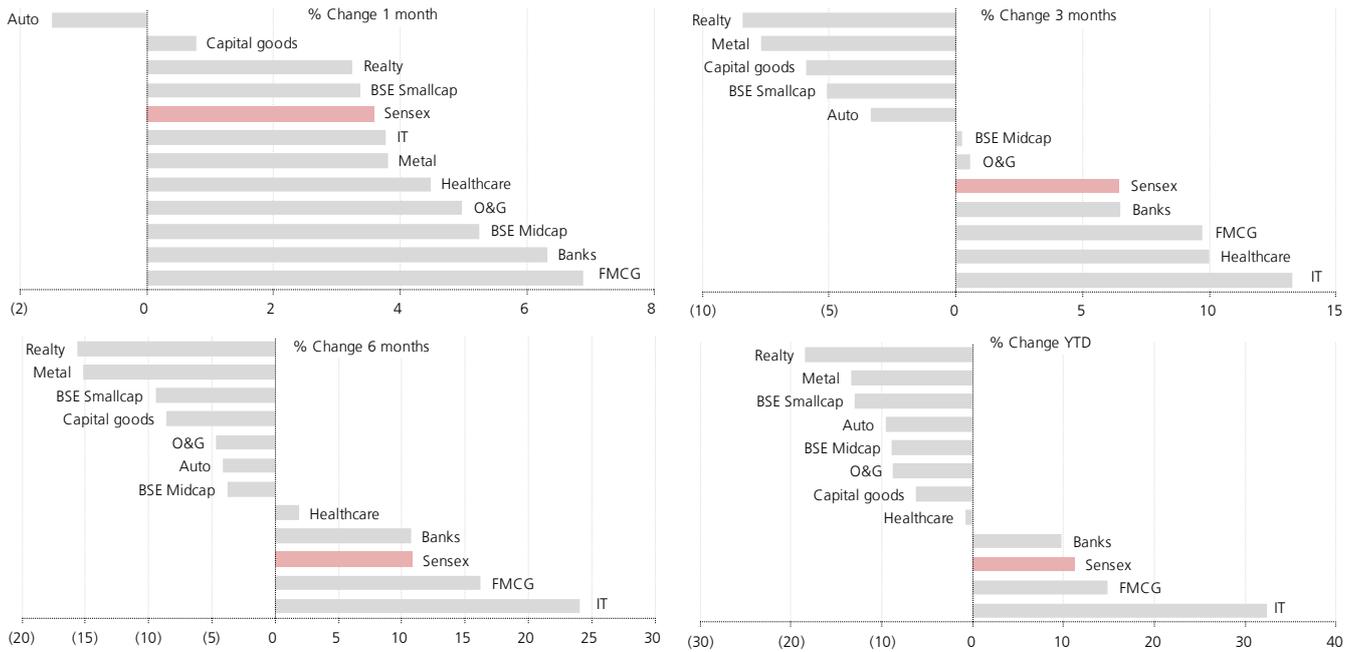
Exhibit 15: A handful of companies contributed to Nifty's CYTD18 returns
CYTD contribution of Nifty-50 Index



Source: Bloomberg, Kotak Institutional Equities

Despite the strong headline performance of the market with the Nifty-50 Index being up 9% CYTD, mid-cap. and small-cap. stocks have struggled in general as also have many large-cap. stocks (see Exhibit 16). In USD terms, the BSE mid-cap. index is down 17% CYTD and the BSE small-cap. index down 21%. Even with the Nifty-50 Index, a few stocks have performed extraordinarily well (up 30-60% CYTD) while a few in the downstream oil & gas and metals & mining sectors are down sharply (20-40%). Exhibit 17 shows the diverse performance of the constituents of the Nifty-50 Index CYTD and the stark gap in valuations.

Exhibit 16: Large-caps have outperformed mid/small-caps in the past few months
 Performance of various sectoral indices versus BSE-30



Source: Bloomberg, Kotak Institutional Equities

Exhibit 17: Most large-cap. stocks are already trading around or above our 12-month fair valuations
Valuation summary of Nifty-50 Index stocks, March fiscal year-ends, 2018-20E

	P/E (X)			EV/EBITDA (X)			Price (Rs)	Target price (Rs)	Upside (%)	Performance			
	2018	2019E	2020E	2018	2019E	2020E				1-mo	3-mo	1-Year	YTD
Ultratech Cement	48.8	34.2	26.5	24.0	17.8	14.7	4,299	2,950	(31)	8	5	9	(0)
Bajaj Finance	65.2	41.6	31.6	—	—	—	2,830	2,000	(29)	15	52	65	61
Reliance Industries	20.5	17.4	15.5	14.8	11.8	10.1	1,211	985	(19)	10	23	54	31
Eicher Motors	36.6	29.1	24.6	26.4	21.1	17.8	28,992	24,000	(17)	5	(5)	(5)	(4)
Sun Pharmaceuticals	39.7	35.4	24.9	23.6	19.4	14.3	602	500	(17)	8	27	28	5
Bajaj Finserv	40.5	29.0	23.2	—	—	—	7,113	6,100	(14)	12	32	36	36
Yes Bank	20.9	19.3	17.6	—	—	—	383	335	(12)	2	11	8	21
TCS	29.7	24.5	22.5	22.1	17.9	16.5	2,004	1,790	(11)	1	17	62	48
Hindustan Unilever	71.2	59.6	52.7	51.1	41.3	36.3	1,747	1,570	(10)	0	16	51	28
Titan Company	72.4	57.7	47.3	49.6	38.3	30.5	926	840	(9)	10	1	47	8
Hero Motocorp	17.6	17.8	16.0	10.9	10.6	9.3	3,263	3,000	(8)	(6)	(11)	(18)	(14)
IOCL	7.8	8.8	9.2	4.6	5.0	5.0	161	150	(7)	1	(5)	(23)	(17)
Dr Reddy's Laboratories	38.6	25.7	19.4	17.8	13.0	9.2	2,279	2,150	(6)	(2)	13	14	(6)
Bajaj Auto	18.9	17.9	16.4	12.7	12.2	10.9	2,646	2,500	(6)	(16)	(7)	(7)	(21)
Asian Paints	68.0	51.5	42.8	41.6	32.3	26.7	1,395	1,325	(5)	2	8	21	20
IndusInd Bank	33.3	28.3	22.9	—	—	—	1,998	1,900	(5)	4	4	23	21
Lupin	21.9	30.9	21.4	13.5	14.5	10.5	837	800	(4)	(3)	11	(13)	(5)
HDFC Bank	31.0	26.8	22.3	—	—	—	2,089	2,000	(4)	(4)	3	19	12
Axis Bank	575.6	34.3	15.4	—	—	—	618	600	(3)	18	12	26	10
Infosys	21.8	19.9	18.0	15.1	13.6	12.2	1,408	1,400	(1)	7	19	45	36
BPCL	9.4	10.0	9.7	7.6	7.3	6.9	377	375	(0)	(3)	(7)	(21)	(27)
Bharti Infratel	20.6	21.7	23.7	7.5	8.1	8.5	284	285	0	(6)	(10)	(25)	(25)
HCL Technologies	16.0	14.2	13.5	11.3	9.3	8.5	997	1,025	3	1	8	16	12
Wipro	16.8	15.0	13.1	10.7	9.4	8.2	284	295	4	1	4	(1)	(9)
HPCL	6.5	8.3	8.5	5.7	7.3	7.7	270	285	6	(0)	(16)	(38)	(35)
Cipla	36.7	27.3	20.8	19.0	15.4	12.2	643	680	6	3	11	13	6
HDFC	25.8	34.7	29.2	—	—	—	1,942	2,075	7	(2)	1	13	14
ITC	34.5	31.9	28.4	22.7	20.7	18.2	308	330	7	14	8	14	17
UPL	14.2	12.5	11.1	9.9	8.5	7.2	610	660	8	9	(16)	(29)	(20)
Kotak Mahindra Bank	39.7	32.3	25.6	—	—	—	1,293	1,400	8	(8)	2	32	28
Maruti Suzuki	35.7	28.3	23.2	20.0	16.3	12.9	9,133	10,000	9	(3)	5	20	(6)
Mahindra & Mahindra	25.1	21.2	18.5	16.5	13.8	11.9	952	1,085	14	5	12	40	27
Tata Steel	8.6	7.6	6.8	6.3	5.9	6.2	579	660	14	4	(5)	(2)	(16)
Coal India	25.0	10.5	10.2	18.8	6.7	6.4	283	326	15	6	5	19	7
GAIL (India)	18.6	14.5	13.2	11.6	9.1	8.3	380	440	16	6	10	36	1
Tech Mahindra	15.8	14.6	12.3	11.6	8.7	7.0	673	785	17	5	1	67	33
Zee Entertainment Enterprises	34.2	30.7	26.3	22.2	19.1	16.1	514	600	17	1	(11)	(1)	(12)
Indiabulls Housing Finance	14.3	12.4	10.0	—	—	—	1,291	1,550	20	15	6	10	8
ONGC	9.6	8.2	8.2	5.1	3.9	3.7	166	200	20	8	(11)	3	(15)
ICICI Bank	31.5	39.2	12.7	—	—	—	332	400	20	24	7	14	6
NTPC	13.8	10.5	10.1	11.1	8.6	8.0	157	190	21	3	(9)	(9)	(11)
Bharti Airtel	77.4	(63.7)	(89.6)	8.2	9.6	8.1	367	445	21	2	(4)	(10)	(31)
Adani Ports and SEZ	20.2	19.9	16.5	13.6	13.6	11.3	373	460	23	1	(9)	(6)	(8)
State Bank of India	NM	38.4	8.0	—	—	—	295	370	25	14	16	6	(5)
L&T	24.2	19.9	18.0	20.3	16.1	15.5	1,253	1,600	28	(3)	(9)	9	(0)
Grasim Industries	20.8	19.1	14.4	12.0	7.3	6.7	987	1,275	29	5	(10)	(11)	(15)
Power Grid	11.9	10.0	8.8	8.5	7.2	6.6	187	250	34	3	(10)	(16)	(7)
Hindalco Industries	10.1	8.1	7.1	6.4	5.4	4.7	221	305	38	1	(9)	(3)	(19)
Tata Motors	12.5	11.3	6.9	3.7	3.5	2.9	249	425	71	(6)	(23)	(34)	(42)
Vedanta	10.0	6.7	5.6	5.5	4.5	3.7	215	370	72	2	(24)	(26)	(35)
Nifty-50 Index	25.5	21.8	17.1	12.0	10.1	9.1	11,435	11,850	4	3.8	5.8	16.8	8.6

Source: Bloomberg, Kotak Institutional Equities estimates

The multiples of 'value' stocks have hardly seen any changes over the past few years (see Exhibit 18), which is probably fair in a few cases given the business models of certain companies while the multiples of 'growth' stocks have expanded significantly over the same period (see Exhibit 19). Many of the market's favorites in the large-cap. and mid-cap. space have seen further re-rating in the past 2-3 months despite their already-high multiples.

Exhibit 18: Most 'value' stocks in our universe have not seen much change in multiples over the past few years
 12-m forward PE multiple and earnings growth of 'value' stocks in KIE universe, March fiscal year-ends, 2011-20

Company	Sector	12-m forward PB/PE multiple (X)								
		31-Mar-11	31-Mar-12	31-Mar-13	31-Mar-14	31-Mar-15	31-Mar-16	31-Mar-17	31-Mar-18	Current
Axis Bank	Banks/NBFCs	2.6	1.8	1.7	1.6	2.6	1.8	2.1	2.1	2.5
Bank of Baroda	Banks/NBFCs	1.7	1.1	0.8	0.9	0.9	1.0	1.3	1.2	1.1
Canara Bank	Banks/NBFCs	1.3	0.9	0.7	0.5	0.6	0.5	0.9	1.1	1.3
Federal Bank	Banks/NBFCs	1.3	1.2	1.2	1.1	1.3	0.9	1.8	1.4	1.4
ICICI Bank	Banks/NBFCs	2.2	1.6	1.7	1.8	2.1	1.5	1.8	2.1	2.1
LIC Housing Finance	Banks/NBFCs	2.2	2.1	1.5	1.4	2.3	2.3	2.2	1.9	1.6
Shriram Transport	Banks/NBFCs	3.0	1.9	1.8	1.8	2.4	2.0	2.1	2.7	1.9
State Bank of India	Banks/NBFCs	1.9	1.7	1.4	1.3	1.6	1.2	1.4	2.1	1.7
BPCL	Energy	13	15	15	14	14	10	13	12	10
GAIL (India)	Energy	14	11	9	11	13	13	14	15	14
HPCL	Energy	9	8	9	10	10	8	13	9	8
IOCL	Energy	9	8	9	10	11	8	10	9	9
ONGC	Energy	9	9	9	8	9	10	10	9	8
Reliance Industries	Energy	14	11	11	11	10	11	13	15	17
Coal India	Metals & Mining	16	13	11	11	13	11	11	15	10
Hindalco Industries	Metals & Mining	10	8	6	11	8	13	14	10	8
Hindustan Zinc	Metals & Mining	10	9	7	7	8	11	12	14	12
JSW Steel	Metals & Mining	9	8	8	11	9	18	10	15	12
National Aluminium Co.	Metals & Mining	17	15	11	14	9	15	23	12	8
NMDC	Metals & Mining	13	8	8	8	9	12	14	10	9
Tata Steel	Metals & Mining	8	9	8	9	9	26	9	9	7
Vedanta	Metals & Mining	6	5	5	7	9	13	9	12	6
CESC	Utilities	8	7	6	10	11	9	11	11	8
JSW Energy	Utilities	8	14	8	10	13	8	10	18	12
NHPC	Utilities	16	10	9	9	9	9	9	10	8
NTPC	Utilities	16	13	10	10	13	11	11	14	10
Power Grid	Utilities	16	14	11	10	12	10	13	12	9
Tata Power	Utilities	15	13	17	14	16	13	12	12	11

Notes:

(a) For banks/NBFCs, we have used P/B and BPS.

Source: Companies, Kotak Institutional Equities estimates

Exhibit 19: Most 'growth' stocks in our universe got re-rated sharply over the past few years on lower DM yields
12-m forward PE multiple and earnings growth of 'growth' stocks in KIE universe, March fiscal year-ends, 2011-20

Company	Sector	12-m forward PB/PE multiple (X)								
		31-Mar-11	31-Mar-12	31-Mar-13	31-Mar-14	31-Mar-15	31-Mar-16	31-Mar-17	31-Mar-18	Current
Bharat Forge	Automobiles	18	16	15	19	31	24	29	35	25
Hero Motocorp	Automobiles	14	16	15	17	17	17	16	20	17
Eicher Motors	Automobiles	15	14	16	25	70	33	33	36	27
Maruti Suzuki	Automobiles	14	15	15	17	s	19	20	32	26
Bajaj Finance	Banks/NBFCs	1.6	1.4	1.5	1.9	3.5	4.2	5.6	6.5	7.7
Cholamandalam	Banks/NBFCs	1.6	1.6	1.8	1.6	2.6	2.8	3.2	4.8	3.5
HDFC Bank	Banks/NBFCs	3.8	3.5	3.5	3.5	3.6	3.2	3.8	4.0	3.7
Indusind Bank	Banks/NBFCs	2.8	2.8	2.5	2.6	3.8	2.9	3.7	4.6	4.0
Yes Bank	Banks/NBFCs	2.3	2.2	2.0	1.7	2.5	2.2	3.1	2.9	2.9
ACC	Cement	21	22	14	24	23	22	39	30	24
Ambuja Cements	Cement	19	20	13	21	27	26	33	31	24
Shree Cement	Cement	NA	29	14	21	52	39	32	37	34
UltraTech Cement	Cement	14	17	15	26	28	30	32	42	31
Asian Paints	Consumer Products	26	30	35	37	39	40	49	52	47
Colgate-Palmolive (India)	Consumer Products	23	29	28	33	40	34	38	43	39
Dabur India	Consumer Products	25	24	26	29	34	31	35	42	47
Glaxosmithkline Consumer	Consumer Products	30	31	35	29	37	31	30	38	32
Hindustan Unilever	Consumer Products	25	29	28	32	41	40	41	56	56
Jubilant Foodworks	Consumer Products	37	49	38	39	58	53	53	77	52
Marico	Consumer Products	25	26	28	24	33	35	42	49	49
Nestle India	Consumer Products	35	33	36	38	42	46	63	63	60
Page Industries	Consumer Products	24	26	26	35	61	45	47	75	73
United Breweries	Consumer Products	47	54	58	68	74	55	55	65	59
United Spirits	Consumer Products	22	14	29	56	58	68	46	79	54
ABB	Industrials	25	32	35	35	86	56	44	63	44
BHEL	Industrials	15	10	8	19	21	23	27	31	20
L&T	Industrials	20	18	17	22	31	23	20	23	19
Siemens	Industrials	35	30	22	41	69	53	47	41	32
Thermax	Industrials	17	14	17	23	33	31	31	41	32
Cipla	Pharmaceuticals	20	17	19	20	30	19	22	25	24
Dr Reddy's Laboratories	Pharmaceuticals	23	16	16	18	25	24	22	32	23
Lupin	Pharmaceuticals	19	19	21	21	32	22	20	24	26
Sun Pharmaceuticals	Pharmaceuticals	22	22	23	22	30	26	21	43	30

Source: Companies, Kotak Institutional Equities estimates

We expect some convergence of multiples between expensive 'growth' stocks and inexpensive 'value' stocks if oil prices were to remain at current levels or even rise moderately from current levels based on re-rating of multiples of 'value' stocks in financials (so-called corporate banks), metal & mining and oil & gas as we expect sector-specific and stock-specific positive developments in the aforementioned sectors. We discuss the specific catalysts in more detail on the section on earnings.

We note that dispersion in multiples across 'growth' and 'value' stocks across and between sectors has become quite stark (see Exhibit 20) with the market making a strong call on the future of certain companies and effectively segregating them into (1) long-term winners where no price or valuation is too high to own the stocks and (2) long-term losers where no price or valuation is too low to sell the stocks.

Exhibit 20: Significant increase in dispersion in valuation within and between sectors
 12-month rolling forward P/E and P/B valuation for Nifty-50 stocks, March fiscal year-ends, 2013-18 (X)

Company	Mar-13	Mar-14	Mar-15	Mar-16	Mar-17	Mar-18	Jul-18
Banking companies							
Axis Bank	1.7	1.6	2.6	1.8	2.0	1.9	2.1
Bajaj Finance	1.5	1.9	3.5	4.2	5.6	5.3	7.6
Bajaj Finserv	1.4	1.2	1.8	1.8	3.6	3.6	4.3
HDFC	4.8	4.4	5.9	4.5	5.7	4.7	5.1
HDFC Bank	3.5	3.5	3.6	3.2	3.8	3.8	4.0
ICICI Bank	1.7	1.8	2.1	1.5	1.8	1.7	1.9
Indiabulls Housing Finance	1.4	1.1	2.6	2.2	3.2	3.4	3.5
IndusInd Bank	2.5	2.6	3.8	2.9	3.7	4.0	4.1
Kotak Mahindra Bank	2.8	2.8	3.9	3.3	3.7	3.6	4.5
State Bank of India	1.4	1.3	1.6	1.2	1.6	1.2	1.3
Yes Bank	2.0	1.7	2.5	2.2	3.1	2.4	2.6
Non-banking companies							
Adani Ports and SEZ	15.2	17.8	22.8	18.0	19.5	17.6	19.1
Asian Paints	33.0	35.5	38.3	37.9	45.4	43.7	53.1
Bajaj Auto	13.8	15.5	15.4	16.5	18.1	16.7	16.9
Bharti Airtel	22.6	23.4	24.4	23.3	34.3	51.3	139.6
Bharti Infratel	26.3	22.7	30.5	26.3	20.1	22.3	20.5
BPCL	15.3	14.2	13.9	9.8	10.7	10.0	9.5
Cipla	18.5	18.8	30.5	19.9	24.0	20.4	25.4
Coal India	10.7	10.8	13.4	11.6	13.5	11.9	9.8
Dr Reddy's Laboratories	16.6	17.8	23.0	20.5	21.0	18.5	20.6
Eicher Motors	16.0	24.8	38.1	32.9	32.4	28.8	26.2
GAIL (India)	9.4	10.6	12.8	13.4	13.4	14.1	14.9
Grasim Industries	8.4	11.0	12.6	12.1	13.6	15.0	19.1
HCL Technologies	14.2	15.3	18.2	13.4	13.7	14.4	13.4
Hero Motocorp	13.5	16.5	16.1	17.2	16.9	17.5	16.4
Hindalco Industries	6.1	10.7	8.2	12.7	9.4	9.0	8.1
Hindustan Unilever	27.8	32.8	40.0	38.9	40.5	47.1	55.9
HPCL	9.1	10.4	10.3	7.8	10.5	8.2	6.8
Infosys	16.4	15.3	18.5	18.3	15.1	16.2	18.1
IOCL	8.8	10.3	10.6	7.6	10.6	8.4	7.9
ITC	27.7	27.4	23.6	23.3	28.4	24.7	27.9
L&T	15.2	22.0	28.0	21.5	22.9	22.9	20.6
Lupin	19.8	20.3	31.3	20.2	19.9	19.4	21.8
Mahindra & Mahindra	14.3	15.0	19.1	17.8	19.9	19.1	21.8
Maruti Suzuki	12.8	17.2	21.5	17.7	21.9	26.3	28.0
NTPC	10.5	9.8	12.5	10.2	12.3	11.4	10.4
ONGC	9.2	8.4	9.2	10.4	10.1	7.9	6.8
Power Grid	10.5	10.3	12.4	9.9	11.5	9.9	9.2
Reliance Industries	11.2	11.3	10.4	11.3	14.0	13.0	15.7
Sun Pharmaceuticals	22.6	20.4	29.0	24.2	21.1	24.8	28.7
Tata Motors	6.9	7.4	8.1	8.6	11.6	8.1	9.4
Tata Steel	8.3	9.0	9.0	29.1	10.8	8.1	7.8
TCS	19.7	18.7	20.4	18.5	16.8	19.1	23.3
Tech Mahindra	10.6	12.7	14.8	12.6	11.8	15.8	14.7
Titan Company	25.3	27.7	32.6	31.5	41.0	55.8	49.0
Ultratech Cement	15.8	24.0	23.5	27.7	34.7	31.2	33.3
UPL	6.3	7.5	13.6	13.3	16.6	15.4	13.1
Vedanta	5.1	7.0	9.4	12.8	9.1	7.6	6.7
Wipro	13.7	15.1	16.4	14.1	14.0	14.5	14.4
Zee Entertainment Enterprises	23.3	26.5	31.6	29.1	33.0	32.1	29.7

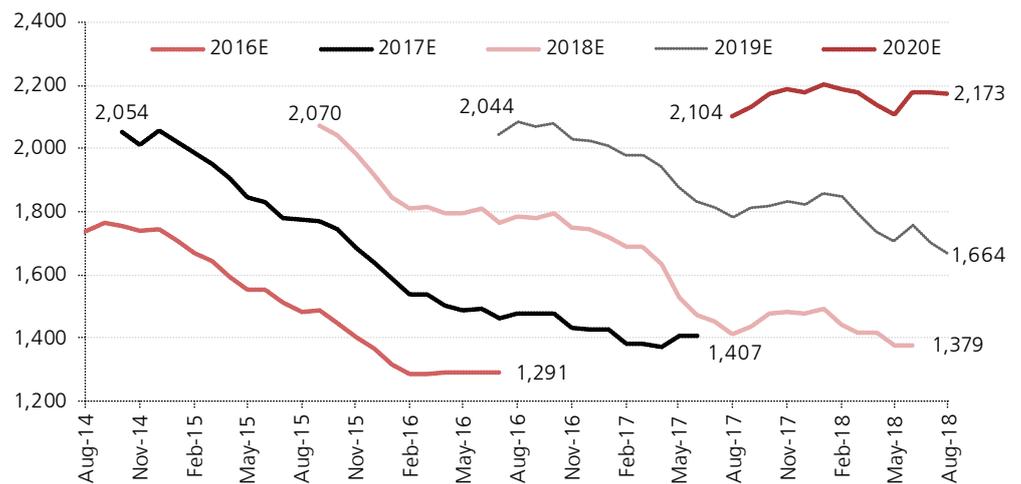
Source: FactSet, Kotak Institutional Equities

We have seen some convergence of multiples in the financial sector over the past few weeks with strong performance of the 'corporate' banks on the back of (1) decline in fresh slippages in 1QFY19, (2) peaking of NPLs and increase in PCR of banks, (3) favorable outcomes in resolutions of a few NCLT 1 cases and (4) speculation around new management of AXSB.

Earnings outlook looking better but risks exist

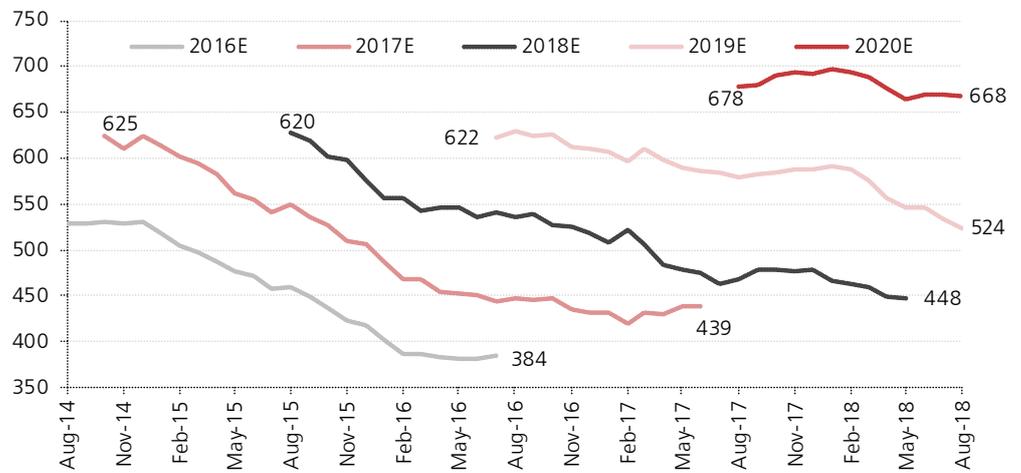
1QFY19 results saw further earnings downgrades for FY2019E and FY2020E (see Exhibits 21 and 22 for our 'EPS' estimates for the BSE-30 and Nifty-50 indices) even though results were generally in line with expectations. The sharp cut in earnings estimates for SBI on the back of weaker estimated treasury income in FY2019 and in VEDL due to lower metal price assumptions has resulted in moderate earnings reduction for the profits of the Nifty-50 Index in FY2019.

Exhibit 21: Our EPS estimates have seen sharp cuts in the past few months
BSE-30 Index EPS estimates trend, March fiscal year-ends, 2016-20E (Rs)



Source: Kotak Institutional Equities estimates

Exhibit 22: Our Nifty EPS estimates have seen sharp cuts in the past few months
Nifty-50 Index EPS estimates trend, March fiscal year-ends, 2016-20E (Rs)



Source: Kotak Institutional Equities estimates

We note that banks and metal companies were/are the biggest contributors to incremental profits for FY2019 and FY2020. Thus, the cut in net profits estimates for SBI and some of the metal companies has dented our earnings estimates for FY2019 although our net profit estimates for FY2020 are relatively impact.

We now expect 20% and 24% growth in net profits of Nifty-50 Index for FY2019 and FY2020 (see Exhibit 23 for the breakdown of net profits of the Nifty-50 Index by sectors). The recovery in net profits reflects our assumptions of (1) normalization of operating conditions in sectors such as banks with lower loan-loss provisions in FY2019-20, post peaking of NPLs in FY2018 and creation of sufficient provisions in FY2017-18, (2) higher global commodity prices from FY2018 levels and (3) moderate domestic economic recovery.

Exhibit 23: Banking, energy and metals & mining sectors to drive incremental profits of the Nifty-50 Index in FY2019-20E
Break-up of net profits of the Nifty-50 Index across sectors, March fiscal year-ends, 2015-20E (based on current constituents)

	Net profits (Rs bn)						Contribution (%)					Incremental profits			
	2015	2016	2017	2018	2019E	2020E	2016	2017	2018	2019E	2020E	2019E		2020E	
												(Rs bn)	(%)	(Rs bn)	(%)
Automobiles	278	311	292	287	330	419	11	8	9	8	8	43	7	89	9
Tata Motors	142	140	94	68	75	122	5	3	2	2	2	7	1	47	5
Banking	684	612	642	533	772	1,334	21	19	16	19	27	239	36	563	59
PSU banks	131	100	105	(65)	69	330	3	3	(2)	2	7	134	20	261	28
Private banks	553	512	537	599	703	1,005	18	16	18	17	20	105	16	302	32
Cement	35	49	58	55	69	90	2	2	2	2	2	13	2	21	2
Consumers	164	159	171	193	222	254	6	5	6	6	5	29	4	31	3
Energy	559	660	958	957	1,027	1,079	23	28	28	26	22	71	11	52	5
IOCL	42	103	259	194	173	166	4	8	6	4	3	(22)	(3)	(7)	(1)
ONGC	189	174	217	223	261	262	6	6	7	6	5	38	6	1	0
Reliance Industries	236	253	299	350	411	462	9	9	10	10	9	62	9	51	5
Industrials	33	41	59	72	88	98	1	2	2	2	2	16	2	10	1
Infrastructure	12	29	39	38	39	47	1	1	1	1	1	0	0	8	1
Media	10	10	13	14	16	19	0	0	0	0	0	2	0	3	0
Metals & Mining	209	155	225	280	439	487	5	7	8	11	10	159	24	48	5
Coal India	137	143	93	70	167	172	5	3	2	4	3	97	15	5	1
Tata Steel	0	(19)	40	81	91	102	(1)	1	2	2	2	10	2	11	1
Vedanta	51	28	73	80	120	143	1	2	2	3	3	39	6	24	2
Pharmaceuticals	107	113	117	78	87	120	4	3	2	2	2	9	1	33	4
Others	1	11	18	22	25	28	0	1	1	1	1	3	0	3	0
Technology	505	553	604	610	687	751	19	18	18	17	15	77	12	65	7
Telecom	80	63	61	44	1	6	2	2	1	0	0	(43)	(7)	5	0
Utilities	148	121	177	176	221	240	4	5	5	5	5	45	7	19	2
Nifty-50 Index	2,824	2,886	3,434	3,361	4,023	4,972	100	100	100	100	100	662	100	948	100
Nifty-50 change (%)	3.4	2.2	19.0	(2.1)	19.7	23.6									
Nifty-50 EPS (FF)	398	384	439	448	524	668									

Source: Kotak Institutional Equities estimate

We discuss our earnings projections by sectors and the key drivers for strong growth in earnings through FY2020E below. We also examine the key risk factors to earnings by sectors, which becomes relevant in the context of the rich valuations for several sectors.

- ▶ **Automobiles.** We note that the automobile sector accounts for 7% of the incremental profits of FY2019, which is lower than its contribution to the net profits of the Nifty-50 Index at 8% for FY2019. Our net profit estimates may be at risk from lower-than-expected gross margin due to (1) inability of the automobile companies to pass on the steep increase in input RM costs such as metals and crude oil (driver of plastic prices); we have modeled this partly and (2) stiff competition across segments as companies vie to regain lost market share (BJAUT in economy segment of motorcycles) or defend market shares. The competitive environment could deteriorate if volumes were to disappoint.

Exhibit 24 shows the gross and EBITDA margins of the automobile stocks under our coverage. We model FY2019-21E gross margin of most automobile companies to deteriorate from FY2018 levels and EBITDA margin to expand in a few cases (AL, MSIL, TTMT, TVS). We would note that the gross and EBITDA margins of the automobile companies have expanded significantly over the past three years following the decline in input prices from FY2015.

Exhibit 24: We expect some moderation in margins of auto companies over FY2019-21E

Gross and EBITDA margin of auto companies under KIE coverage, March fiscal year-ends, 2014-21E (%)

	Gross margin (%)								EBITDA margin (%)							
	2014	2015	2016	2017	2018	2019E	2020E	2021E	2014	2015	2016	2017	2018	2019E	2020E	2021E
Amara Raja Batteries	25.1	26.3	28.5	26.0	24.0	23.6	23.7	23.6	16.3	16.7	17.8	16.0	14.6	14.7	15.0	15.0
Apollo Tyres	41.8	45.4	49.7	47.7	43.4	43.1	42.7	43.5	14.0	15.1	16.9	14.0	11.1	13.1	13.9	14.6
Ashok Leyland	23.5	26.5	30.3	30.6	29.1	28.2	28.4	27.6	1.7	7.6	11.9	10.9	10.4	10.3	11.5	11.3
Bajaj Auto	30.6	29.2	31.3	31.0	29.3	27.0	27.1	26.8	21.8	19.0	21.2	20.3	19.0	17.1	17.2	17.0
Balkrishna Industries	50.5	51.3	59.8	58.3	54.1	54.7	55.3	55.1	24.2	23.9	31.5	32.0	28.9	29.9	30.8	30.5
Bharat Forge	49.0	47.3	46.5	46.9	44.7	46.5	46.8	47.6	15.3	18.9	20.7	19.6	20.6	22.2	22.4	22.0
CEAT	35.8	38.6	43.6	41.0	38.9	38.9	38.8	38.4	11.8	11.8	14.1	11.4	9.9	11.5	12.2	12.4
Eicher Motors	31.9	34.0	44.4	47.3	48.2	48.5	47.9	47.1	10.5	12.8	27.4	30.9	31.3	32.0	31.6	31.3
Escorts	28.3	28.5	30.6	31.8	32.8	32.5	33.0	33.0	6.1	3.3	5.2	7.9	11.2	12.4	13.0	12.9
Exide Industries	26.9	26.9	29.5	29.1	26.6	26.7	26.7	26.6	13.7	13.2	14.8	14.3	13.5	14.6	14.7	14.8
Hero Motocorp	26.4	26.9	30.7	32.1	31.1	29.3	29.3	29.1	10.7	12.2	15.4	16.3	16.4	15.2	15.4	15.3
Mahindra & Mahindra	30.6	30.4	31.9	32.3	33.5	33.0	33.0	32.5	13.5	12.5	13.5	13.1	14.8	15.2	15.2	14.5
Maruti Suzuki	25.8	27.3	30.1	29.3	29.1	29.3	29.5	29.3	11.9	13.4	15.4	15.2	15.1	15.4	16.1	16.2
Motherson Sumi Systems	37.0	38.3	39.8	39.2	39.0	36.4	35.7	35.6	8.7	9.1	9.5	9.8	9.1	9.7	10.0	10.0
Schaeffler India	36.0	38.9	42.6	39.6	42.8	40.3	41.6	41.7	13.1	14.8	17.7	16.5	19.1	17.7	19.5	19.8
SKF	36.7	37.9	37.6	38.2	41.6	41.5	41.6	41.9	11.5	11.7	12.1	12.8	15.8	15.7	16.2	16.7
Tata Motors	38.3	39.1	40.2	38.5	36.9	38.0	38.1	38.3	15.0	14.9	14.0	12.4	11.3	12.0	13.5	13.7
Timken	38.1	40.2	40.0	40.9	41.0	42.6	42.5	42.4	9.9	14.4	15.5	15.0	13.2	16.2	16.7	16.8
TVS Motor	28.8	27.3	28.1	27.0	26.4	25.5	25.5	25.5	6.1	6.0	7.3	7.1	7.5	8.0	8.5	8.9
WABCO India	42.9	41.2	40.0	40.1	37.6	37.1	37.2	36.2	15.0	15.1	15.6	15.8	15.3	15.4	16.4	15.0

Source: Companies, Kotak Institutional Equities estimates

- ▶ **Banks and NBFCs.** We expect loan-loss provisions (see Exhibit 25) to decline and RoEs to improve of several banks under our coverage over FY2019-21E after a very weak performance in FY2016-18, which drives a sharp recovery in the profits of private and public banks both under our coverage. We note that the banking sector will contribute about 36% and 59% of the incremental profits of the Nifty-50 Index in FY2019 and FY2020, respectively.

Exhibit 25: We expect loan-loss provisions of several banks under our coverage to normalize over FY2019-21E

LLP as a percentage of average loans and RoEs, March fiscal year-ends, 2014-21E (%)

	2014	2015	2016	2017	2018	2019E	2020E	2021E
Public banks								
Bank of Baroda	1.0	1.1	3.3	2.2	3.4	1.1	1.0	0.9
Canara Bank	1.0	1.3	3.1	2.1	3.9	2.2	1.0	0.6
Punjab National Bank	1.8	2.3	4.4	2.9	6.5	4.7	1.2	1.2
State Bank of India	1.4	1.6	2.2	2.3	3.8	2.0	1.3	1.1
Union Bank	1.2	1.2	1.5	2.4	4.4	2.1	1.3	1.0
Old private banks								
City Union Bank	1.1	0.9	1.1	1.1	1.2	1.0	1.0	0.9
DCB Bank	0.5	0.7	0.6	0.8	0.7	0.7	0.7	0.6
Federal Bank	0.4	0.4	1.1	0.9	0.9	0.8	0.6	0.7
J&K Bank	0.3	2.2	2.0	5.0	2.0	1.2	1.0	1.0
Karur Vysya Bank	0.7	1.6	0.8	1.6	2.8	2.8	1.0	0.9
New private banks								
Axis Bank	1.0	0.9	1.5	3.3	4.0	1.9	0.8	0.8
HDFC Bank	0.7	0.6	0.6	0.7	0.9	0.7	0.9	0.8
ICICI Bank	0.8	0.9	2.7	3.2	3.5	3.0	0.8	0.7
IndusInd Bank	0.8	0.7	0.8	1.1	0.8	0.8	0.9	0.9
RBL Bank	0.6	0.3	0.6	0.8	0.9	0.7	0.7	0.7
Yes Bank	0.5	0.6	0.6	0.6	0.7	0.8	0.8	0.8
Small finance banks								
Equitas Holdings	1.1	1.8	1.4	1.9	2.5	1.6	2.0	2.0
Ujjivan Financial Services	0.6	0.9	0.6	1.4	4.6	1.0	1.4	1.5

Source: Companies, Kotak Institutional Equities estimates

We expect banks to make further provision in 1HFY19 related to fresh NPLs from the non-NPL stress loan book and increase overall provision coverage ratio (PCR) to comfortable levels to absorb the eventual ECL/LGD arising from resolution of NPLs or liquidation of assets. We expect provisions to start declining from 2HFY19. Private and PSU banks have both increased provisions significantly over the past few quarters (see Exhibit 26) goaded by the RBI to do so. We also rule out meaningful increase in fresh NPLs as banks have been forced to recognize a greater part of their non-NPL stressed loan book as NPLs in 4QFY18 (see Exhibit 27) post the February 12, 2018 directive of the RBI. For our modeling purposes, we assume a large increase in the PCR for the banks under our coverage (see Exhibit 28) over FY2019-21E.

Exhibit 26: Significant increase in provisions over the past few quarters

Provisions, pre-provision operating profits and ratio of the two for banks in KIE coverage universe, 1QFY18-1QFY19

	Pre-provision operating profits (Rs bn)					Provisions (Rs bn)					Ratio (%)				
	1QFY18	2QFY18	3QFY18	4QFY18	1QFY19	1QFY18	2QFY18	3QFY18	4QFY18	1QFY19	1QFY18	2QFY18	3QFY18	4QFY18	1QFY19
Public banks															
Bank of Baroda	26	30	37	27	30	24	23	34	67	22	89	77	94	250	72
Canara Bank	25	25	28	18	29	22	22	27	91	26	89	87	94	514	88
Punjab National Bank	32	33	42	(4)	42	26	24	45	204	58	81	74	105	(4,549)	137
State Bank of India	119	200	118	159	120	89	191	189	281	192	75	96	161	177	161
Union Bank	21	18	10	8	21	17	36	33	57	22	81	200	341	737	108
Old private banks															
City Union Bank	3	3	3	3	3	1	1	1	1	1	39	40	29	29	26
DCB Bank	1	1	1	1	1	0	0	0	0	0	26	24	28	27	23
Federal Bank	6	6	6	6	6	2	2	2	4	2	42	30	29	63	33
Karur Vysya Bank	4	4	4	5	5	2	3	3	4	4	52	75	77	82	92
J&K Bank	4	4	4	3	3	5	2	3	3	3	140	67	65	94	73
New private banks															
Axis Bank	43	38	39	37	44	23	31	28	72	33	55	83	73	196	76
HDFC Bank	75	78	85	88	86	16	15	14	15	16	21	19	16	17	19
ICICI Bank	52	70	51	75	58	26	45	36	66	60	50	64	71	88	103
IndusInd Bank	16	16	17	18	18	3	3	2	3	4	20	18	14	19	19
Yes Bank	17	19	20	21	25	3	4	4	4	6	17	23	21	19	25

Source: Companies, Kotak Institutional Equities

Exhibit 27: Large portion of standard stressed assets recognized as NPA in FY2018, particularly in 4QFY18

Watch-list movement of corporate banks, March fiscal year-ends, 2017-18

	2017		2018		GNPA (%)		NNPA (%)		PCR (%)		Advances (Rs bn)	
	Standard stressed loan		Standard stressed loan		2017	2018	2017	2018	2017	2018	2017	2018
	Amount	% of stressed	Amount	% of stressed								
	Rs bn	book	Rs bn	book								
Axis bank	279	59.7	91	23.4	5.0	6.8	2.1	3.4	59.5	51.6	3,731	4,397
Bank of Baroda	172	30.0	100	16.0	10.5	12.3	4.7	5.5	57.7	58.4	3,833	4,274
Canara Bank	212	39.2	95	17.4	9.6	11.8	6.3	7.5	36.7	39.9	3,420	3,817
ICICI Bank	268	39.8	85	14.3	8.7	9.9	5.4	5.4	40.2	48.4	4,642	5,124
Punjab National Bank	301	36.4	125	13.6	12.5	18.4	7.8	11.2	40.9	43.8	4,195	4,337
State Bank of India	505	31.0	258	10.4	6.9	10.9	3.7	5.7	48.1	50.4	16,273	20,484
Union Bank	148	30.6	50	9.2	11.2	15.7	6.6	8.4	44.1	50.7	3,017	3,139
Yes Bank	9	31.5	3	11.5	1.5	1.3	0.8	0.6	46.9	50.0	1,323	2,035

Notes:

(a) Non-NPL stressed loan includes standard restructured loans, watch-list, SDR, S4A and 5/25.

(b) We have used SDR, S4A and 5/25 data of 1QFY18 for FY2017 for PNB.

Source: Companies, Kotak Institutional Equities

Exhibit 28: We model a meaningful increase in PCR for banks under our coverage over FY2019-21E
 Provision coverage ratio (excluding write-off), March fiscal year-ends, 2014-21E (%)

	2014	2015	2016	2017	2018	2019E	2020E	2021E
Public banks								
Bank of Baroda	49	50	52	58	58	59	61	62
Canara Bank	21	33	34	37	40	40	47	57
Punjab National Bank	47	40	37	41	44	49	56	70
State Bank of India	50	51	43	48	50	58	64	67
Union Bank	44	47	42	44	51	53	57	67
Old private banks								
City Union Bank	33	31	37	40	45	51	57	73
DCB Bank	47	43	51	51	60	50	52	56
Federal Bank	70	65	43	46	44	49	60	73
J&K Bank	87	55	50	59	54	54	47	51
Karur Vysya Bank	50	59	58	30	38	42	43	47
New private banks								
Axis Bank	66	67	57	58	50	55	64	74
HDFC Bank	73	74	70	69	70	62	60	63
ICICI Bank	69	59	51	40	49	65	77	84
IndusInd Bank	70	63	59	58	56	58	59	60
Yes Bank	85	72	62	47	50	49	60	68
Small finance banks								
Equitas Holdings	20	26	30	49	47	61	64	67
Ujjivan Financial Services	81	74	74	61	75	92	96	89

Source: Companies, Kotak Institutional Equities estimates

We believe GNPLs and slippages may have peaked and expect resolutions in the pending cases before the NCLT over the next few months. The NCLT1 cases have seen meaningful progress with resolutions in seven of the 12 cases (see Exhibit 29) and likely resolution in two steel assets over the next 2-3 months given the number of interested buyers that have bid aggressively for those assets.

Exhibit 29: Resolution process underway for bankruptcy cases

Status of major stressed companies in NCLT

Company	Date of admission	Admitted claims (Rs bn)	Bench	Filed by	Current status
ABG Shipyard	2-Aug-17	189	Ahmedabad	ICICI Bank	New resolution plan received from Liberty House after fresh bids were invited; previous bids were rejected by Committee of Creditors
Alok Industries	18-Jul-17	296	Ahmedabad	SBI	Committee of Creditors has accepted the Rs51 bn bid of Reliance-JM Financial ARC
Amtek Auto	25-Jul-17	126	Chandigarh	Corporation Bank	Committee of Creditors has accepted the bid of Liberty House; details of the bid is not out in public domain
Bhushan Power & Steel	26-Jul-17	372	New Delhi	PNB	JSW Steel is reported to have emerged as the highest bidder in the latest round of bidding by offering Rs197 bn; Liberty House and Tata Steel had previously offered Rs185 bn and Rs170 bn respectively
Bhushan Steel	26-Jul-17	560	New Delhi	SBI	Tata Steel has successfully acquired the company; it had offered Rs352 bn to financial creditors as per the terms of the resolution plan
Electrosteel Steel	21-Jul-17	132	Kolkata	SBI	Vedanta has successfully acquired the company; it had offered Rs53 bn to financial creditors as per the terms of the resolution plan
Era Infra Engineering	12-Apr-17	101	New Delhi	UBI	Insolvency process is ongoing; earlier litigation on insolvency proceedings overruled on Feb-18; no bids yet
Essar Steel	2-Aug-17	492	Ahmedabad	SBI	NCLAT, the appellate body, is hearing litigations to determine the winning bid, after both Arcelor Mittal and Numetal contested their bids being disqualified; NuMetal reportedly offered Rs 370 bn in the second round
Jaypee Infratech	9-Aug-17	96	Allahabad	IDBI	Committee of Creditors has accepted the bid of Lakshadweep Pvt. Ltd; Rs74 bn was offered to lenders
Jyoti Structures	4-Jul-17	76	Mumbai	SBI	Committee of Creditors has approved the resolution plan submitted by a group of HNIs led by Sharad Singhi; they had made an offer of Rs35 bn
Lanco Infratech	7-Aug-17	453	Hyderabad	IDBI	Committee of Creditors has rejected the revised resolution plan of Tamil Nadu-based Thriveni Earth Movers ; may go for liquidation
Monnet Ispat	18-Jul-17	102	Mumbai	SBI	Committee of Creditors has approved the resolution plan submitted by JSW Steel-AION Capital; Rs37 bn offered as part of the resolution
Total		2,996			

Source: NCLT, IBBI, Kotak Institutional Equities

We model (1) a modest decline in the NIMs of private retail banks under our coverage due to likely increased competition and (2) an increase in NIMs of other banks led by improved operating performance of the banks and normalization of NII after two years of large reversal of interest income booked earlier due to slippages in the corporate loan book. However, the biggest driver of the profits of the banks in the latter category is our assumption of lower LLPs and not, improvement in NIMs.

For the NBFCs, we see pressure on NIMs/RoEs in general due to (1) increase in borrowing costs and (2) increased competition in all the lending segments. We have already seen a squeeze on the NIMs of the HFCs due to increased competition in the housing finance segment. However, we expect the NIMs of the MFIs and rural finance companies to recover from the lows of FY2017. Exhibit 30 gives the NIM and RoE of the major banks and NBFCs under our coverage for FY2014-21E.

Exhibit 30: We see pressure on NIMs for private banks and NBFCs, improvement in RoEs for PSU and 'corporate' private banks
NIM and RoE of banks and NBFCs, March fiscal year-ends, 2014-21E (%)

	NIM (%)								RoE (%)							
	2014	2015	2016	2017	2018	2019E	2020E	2021E	2014	2015	2016	2017	2018	2019E	2020E	2021E
Banks																
Axis Bank	3.4	3.5	3.6	3.5	3.1	3.0	3.1	3.1	17.4	17.8	16.8	6.4	0.5	7.1	14.1	14.1
Bank of Baroda	2.0	2.0	1.9	2.1	2.3	2.7	2.6	2.6	13.8	9.2	(14.4)	3.4	(5.8)	12.7	14.0	13.7
Canara Bank	2.1	2.0	1.9	1.8	2.2	2.4	2.5	2.5	8.9	8.8	(8.9)	3.4	(12.2)	(1.0)	10.1	12.0
Federal Bank	3.2	3.2	3.1	3.2	3.0	2.9	2.9	2.8	12.6	13.7	6.0	9.8	8.2	8.8	11.4	12.8
HDFC Bank	4.4	4.4	4.4	4.4	4.4	4.1	4.1	4.0	21.3	19.4	18.3	17.9	17.9	16.7	16.2	17.0
ICICI Bank	3.2	3.4	3.5	3.4	3.2	3.1	3.2	3.2	14.0	14.7	11.4	10.9	6.6	5.1	14.5	15.5
IndusInd Bank	3.8	3.7	3.8	4.0	4.0	4.1	4.2	4.1	18.0	19.7	17.1	15.7	17.1	17.6	16.8	17.0
Punjab National Bank	3.2	3.0	2.5	2.3	2.1	2.3	2.4	2.8	10.2	8.5	(13.3)	3.6	(32.5)	(23.4)	10.7	13.8
State Bank of India	3.1	3.0	2.8	2.7	2.6	2.7	2.8	3.0	10.0	10.6	7.3	6.3	(3.2)	3.1	13.6	16.7
YES Bank	2.8	3.0	3.2	3.3	3.1	3.0	2.9	3.1	25.0	21.3	19.9	18.6	17.7	16.6	15.9	17.2
NBFCs																
Bharat Financial Inclusion	7.4	8.2	7.9	7.2	7.4	7.4	7.7	7.9	16.5	25.0	24.9	15.1	16.7	17.9	18.5	19.0
Cholamandalam	5.1	5.5	5.9	6.0	6.5	6.9	6.4	6.4	17.1	17.4	17.9	18.0	20.6	24.5	24.3	24.3
HDFC	3.7	3.8	4.1	3.8	4.9	3.3	3.3	3.3	20.6	21.2	22.3	20.4	23.9	13.8	14.5	16.0
L&T Finance Holdings	5.6	6.2	6.2	6.3	6.6	4.9	4.8	4.8	10.5	13.9	12.6	13.8	14.2	18.9	18.8	18.3
LIC Housing Finance	2.3	2.3	2.5	2.7	2.4	2.3	2.3	2.3	18.8	15.7	16.9	16.6	14.5	14.3	14.4	14.3
Mahindra & Mahindra Financial	7.8	7.4	7.2	6.6	7.2	7.4	7.4	7.5	18.6	15.5	11.4	6.4	11.3	14.3	15.8	16.7
Muthoot Finance	9.5	9.5	10.7	13.0	14.6	13.1	12.7	12.8	19.0	14.3	15.1	19.4	24.1	18.4	16.9	17.2
PNB Housing Finance	3.0	3.0	3.1	2.9	3.0	2.7	2.6	2.5	16.7	15.4	17.6	13.6	14.0	15.2	15.9	17.0
Shriram City Union Finance	12.1	13.7	13.5	13.6	13.5	12.7	12.4	12.1	20.2	15.8	12.1	11.6	12.5	15.8	16.9	17.6
Shriram Transport	7.3	7.3	7.7	7.3	7.7	7.7	7.3	7.2	16.3	14.1	12.2	11.7	13.1	18.3	17.5	17.1

Source: Companies, Kotak Institutional Equities estimates

- **Cement.** We have cut our profitability assumptions for FY2019-20E for the cement companies under our coverage repeatedly through FY2018 and in 1QFY19 too given disappointing results in practically every quarter. Nonetheless, we still see downside risks to our profitability assumptions for FY2019-21 given (1) subdued cement prices on weak supply-demand balance (see Exhibit 31; new cement capacity addition precludes improvement in capacity utilization through FY2021) and (2) sharp increase in input prices (petroleum coke for fuel and diesel for transportation). Exhibit 32 compares the historical profitability (₹/ton) with our estimates for FY2019-21E.

Exhibit 31: We expect capacity utilization to remain below 70% until FY2021
Cement demand-supply balance, March fiscal year-ends, 2015-21E (mn tons)

	2015	2016	2017	2018	2019E	2020E	2021E
All-India							
Closing installed capacity (mtpa)	417	441	461	467	487	506	537
Incremental installed capacity (mtpa)	43	24	19	7	20	19	30
Effective capacity (mtpa)	396	429	451	464	477	497	522
Incremental effective capacity (mtpa)	22	33	22	13	13	19	25
Capacity growth (%)	5.7	8.4	5.0	2.9	2.9	4.1	5.0
Cement consumption (mn tons)	266	279	275	293	315	341	369
Incremental consumption (mn tons)	14	13	(3)	18	22	26	28
Consumption growth (%)	5.7	4.8	(1.2)	6.5	7.6	8.1	8.1
Cement production (mn tons)	271	283	280	298	320	345	373
Incremental production (mn tons)	15	13	(3)	18	22	26	28
Growth (%)	5.9	4.6	(1.2)	6.3	7.5	8.0	8.0
Capacity utilization (%)	68	66	62	64	66	68	70

Source: CMA, Kotak Institutional Equities estimates

Exhibit 32: We model a sharp recovery in the profitability of cement companies under our coverage
Profitability (EBITDA/ton) of cement companies, March fiscal year-ends, 2014-21E (Rs/ton)

	2014	2015	2016	2017	2018	2019E	2020E	2021E	Growth (% yoy)						
									2015	2016	2017	2018E	2019E	2020E	2021E
ACC	565	508	489	544	593	670	709	753	(10)	(4)	11	9	13	6	6
Ambuja Cement	750	867	669	747	845	952	1,038	1,082	16	(23)	12	13	13	9	4
India Cement	536	749	894	780	620	621	716	742	40	19	(13)	(20)	0	15	4
JK Cement	586	619	625	881	809	730	886	901	6	1	41	(8)	(10)	21	2
JK Lakshmi Cement	536	589	370	460	479	567	742	785	10	(37)	24	4	18	31	6
Orient Cement	491	725	398	321	531	678	761	834	48	(45)	(19)	66	28	12	10
Shree Cement	885	705	773	1,125	1,077	1,100	1,214	1,262	(20)	10	46	(4)	2	10	4
Ultratech Cement	834	850	939	931	893	1,002	1,096	1,172	2	11	(1)	(4)	12	9	7

Source: Companies, Kotak Institutional Equities estimates

We would note that the sector has failed to meet with consensus estimates on profitability and earnings for the past 4-5 years. Cement companies' earnings have very high sensitivity to profitability assumptions. Exhibit 33 shows the FY2019-21E EPS of the cement companies under our coverage at various levels of profitability (₹100/ton higher and lower versus our base-case profitability estimates).

Exhibit 33: Earnings of cement companies are highly sensitive to cement profitability assumptions
EPS sensitivity of cement companies for change in EBITDA/ton, March fiscal year-ends, 2019E-21E

	(EBITDA: -Rs100/ton)			Base Case			(EBITDA: +Rs100/ton)		
	2019E	2020E	2021E	2019E	2020E	2021E	2019E	2020E	2021E
ACC									
Volumes (mn tons)	28.0	29.4	30.9	28.0	29.4	30.9	28.0	29.4	30.9
EBITDA/ton (Rs)	562	601	645	670	709	753	778	817	861
EBITDA (Rs bn)	15.8	17.7	19.9	18.8	20.9	23.3	21.8	24.0	26.6
PAT (Rs bn)	9.5	11.0	12.9	11.6	13.2	15.3	13.7	15.5	17.6
EPS (Rs)	51	59	69	62	70	81	73	82	94
Ambuja standalone									
Volumes (mn tons)	24.3	26.1	28.0	24.3	26.1	28.0	24.3	26.1	28.0
EBITDA/ton (Rs)	852	937	982	952	1,038	1,082	1,053	1,138	1,182
EBITDA (Rs bn)	20.7	24.5	27.5	23.1	27.1	30.3	25.6	29.7	33.2
PAT (Rs bn)	13.4	16.8	19.3	15.1	18.6	21.2	16.9	20.4	23.2
EPS (Rs)	7	8	10	8	9	11	8	10	12
Shree Cement									
Volumes (mn tons)	25.8	30.4	34.6	25.8	30.4	34.6	25.8	30.4	34.6
EBITDA/ton (Rs)	1,002	1,117	1,164	1,100	1,214	1,262	1,198	1,312	1,360
EBITDA (Rs bn)	27.4	35.7	41.9	29.9	38.6	45.3	32.5	41.6	48.7
PAT (Rs bn)	12.8	19.7	23.9	14.7	22.0	26.5	16.6	24.2	29.0
EPS (Rs)	367	566	687	421	630	760	475	694	833
Ultratech									
Volumes (mn tons)	69.7	74.3	79.3	69.7	74.3	79.3	69.7	74.3	79.3
EBITDA/ton (Rs)	906	999	1,075	1,002	1,096	1,172	1,099	1,192	1,268
EBITDA (Rs bn)	64.4	75.8	87.1	71.3	83.1	94.9	78.1	90.4	102.7
PAT (Rs bn)	29.9	39.5	49.9	34.5	44.5	55.2	39.2	49.5	60.5
EPS (Rs)	109	144	182	126	162	201	143	180	220

Source: Companies, Kotak Institutional Equities estimates

- ▶ **Consumer staples.** We expect the consumer staple companies to deliver steady revenue and earnings growth over FY2019-21E driven by (1) recovery in volumes led by the steady economic recovery, (2) likely increased government spending on the rural economy through an expansion of the MSP program, (3) implementation of 7CPC-related salary and pension increases for employees and ex-employees of various state governments that are yet to implement the same and (4) steady profitability.

However, we see some risk to our (1) growth assumptions in a few cases, particularly discretionary companies and (2) margin assumptions from the recent steep increase in commodity (particularly crude oil) prices and sharp depreciation in the currency. It is possible that the Street may have extrapolated the strong rebound in sales due to the low base in 2HFY17 (demonetization) and 1QFY18 (pre-GST destocking) to FY2019-20. A few consumer companies have already seen some compression of margins in FY2018 from high levels of FY2017 although we do believe that consumer staple companies do have a fair degree of pricing power and thus, can increase prices to offset any increase in input prices and they have also increased focus on other costs such as A&SP and employee costs over the past 2-3 quarters in order to control overall costs.

We assume some moderation in gross and EBITDA margins in a few cases but keep gross and EBITDA margins at FY2018 levels in most cases. Exhibit 34 shows that the gross and EBITDA margins of consumer staple companies under our coverage have expanded quite significantly over FY2014-17.

Exhibit 34: We assume gross and EBITDA margins of consumer companies to sustain at high levels post significant expansion over FY2014-18
Gross margin and EBITDA margin of consumer companies, March fiscal year-ends, 2014-21E (%)

	Gross margin (%)								EBITDA margin (%)							
	2014	2015	2016	2017	2018	2019E	2020E	2021E	2014	2015	2016	2017	2018	2019E	2020E	2021E
Asian Paints	42.3	43.8	43.6	44.7	42.4	42.9	43.1	43.4	15.7	15.8	19.4	19.8	19.0	20.8	21.1	21.5
Bajaj Corp.	60.0	61.7	62.7	66.2	67.5	66.4	66.5	66.6	27.7	29.0	34.2	33.1	30.6	29.2	30.2	31.0
Britannia Industries	39.7	40.3	40.3	38.3	38.4	39.2	40.0	40.4	9.1	11.0	14.5	14.1	15.1	16.5	17.4	17.9
Colgate-Palmolive (India)	60.8	63.1	61.8	62.9	64.4	65.5	65.1	65.3	18.6	20.6	24.3	23.7	26.6	28.0	28.3	28.8
Dabur India	52.1	52.5	51.1	50.1	50.4	50.8	50.8	50.9	16.3	16.8	19.3	19.6	20.9	21.7	22.0	22.3
GlaxoSmithKline Consumer	64.3	65.2	67.5	67.5	66.8	68.3	68.5	68.6	17.9	16.9	20.3	20.9	20.5	21.9	22.3	22.5
Godrej Consumer Products	53.2	53.6	54.1	55.4	56.6	56.9	56.9	57.0	15.1	16.5	19.4	20.5	21.0	22.0	22.4	22.7
Hindustan Unilever	48.8	49.2	50.7	50.8	53.0	54.2	54.3	54.4	16.0	16.6	18.3	19.0	21.1	23.0	23.4	23.7
ITC	60.4	59.8	63.2	60.1	61.1	61.3	61.4	61.5	37.0	36.9	37.5	36.4	38.3	39.6	40.4	41.2
Jubilant Foodworks	73.9	74.8	76.2	75.6	74.6	74.1	74.0	73.9	14.4	12.2	10.8	9.3	14.6	17.9	19.6	21.0
Jyothy Laboratories	47.5	48.5	47.5	46.9	49.9	47.9	48.1	48.3	11.9	12.4	15.0	15.3	15.5	15.6	15.9	16.2
Marico	48.8	45.6	49.0	52.2	47.0	45.6	47.5	48.2	16.0	15.2	17.5	19.6	18.0	17.2	18.3	18.8
Nestle India	54.5	53.9	57.3	57.2	56.5	58.6	58.9	59.0	21.9	20.9	19.6	21.7	21.7	24.8	25.5	25.8
Page Industries	53.1	53.7	61.8	59.5	57.4	57.7	57.9	58.1	21.5	20.7	20.9	19.4	21.2	23.3	23.6	23.8
Pidilite Industries	44.9	44.9	51.8	53.0	52.5	51.4	51.9	52.4	15.7	15.9	21.9	22.4	22.1	21.9	22.8	23.6
Tata Global Beverages	52.5	52.0	45.4	47.5	45.7	45.5	45.8	46.1	9.7	9.7	9.9	11.7	12.3	12.0	12.6	13.2
Titan Company	26.3	26.5	27.5	28.3	27.5	26.8	27.3	27.4	9.6	9.6	8.3	8.7	10.2	10.8	11.4	11.6
United Breweries	59.0	59.6	56.1	53.9	53.2	53.7	53.9	54.1	14.1	13.3	14.3	13.6	16.1	17.7	18.0	18.4
United Spirits	40.8	40.8	41.3	42.9	47.5	49.1	49.6	49.7	10.0	7.4	10.7	11.4	12.5	14.7	16.1	16.9

Source: Companies, Kotak Institutional Equities estimates

Nonetheless, we note that the earnings growth of these companies will largely follow top-line growth as there may be limited scope for EBITDA margins to expand meaningfully from current levels. We would expect low teens growth for revenues and earnings for most of the consumer staple companies in a reasonably good scenario with (1) volume growth in line with real GDP growth and (2) price/mix realization growth in line with or slightly above inflation.

- **Metals & mining.** The metals & mining sector is an important contributor to the growth in profits of the Nifty-50 Index in FY2019 and FY2020 accounting for 24% of the incremental profits of the Nifty-50 Index for FY2019. The profits of this sector can be quite volatile and we have seen earnings downgrades in 1QFY19 on weaker assumptions of non-ferrous metal prices. In particular, zinc prices have collapsed in the past few months; we had expected the same to occur in FY2019 on onset of new capacities. However, prices have already weakened on concerns on near-term growth and unwinding of speculative positions. Metal prices face further downside risk from a full-blown trade war between China and the US, which could dent global economic growth and demand for metals. Nonetheless, we have good visibility on a meaningful portion of the profits of the sector for a few reasons.

- In the case of Coal India, we have reasonable confidence about its FY2019 and FY2020 net profits as it (1) raised the price of raw coal by ₹100/ton in January 2018 and (2) implemented a ₹50/ton evacuation charge in December 2017. Coal India will account for 15% of incremental profits of the Nifty-50 Index and 61% of the metals and mining sector in FY2019.
- In the case of non-ferrous metal stocks, our assumed prices for FY2019-21E are broadly in line with the current spot prices and modestly higher than five-year average prices (see Exhibit 35). We base our assumptions on the improved global supply-demand balance in the case of non-ferrous metals (aluminum) reflecting (1) higher global consumption on the back of ongoing global economic recovery and (2) reduced supply from China following its decision to close certain aluminum capacities. Also, Vedanta, the other big contributor (other than Coal India) to the incremental profits of the metals & mining sector, would see a significant ramp-up in volumes through FY2020E (see Exhibit 36), which will drive its profits apart from higher aluminum profitability on the back of higher aluminum-alumina spreads.

Exhibit 35: Our price assumptions may be at risk

Price assumptions for metal companies, March fiscal year-ends, 2017-21E (US\$/ton)

	Price assumptions					Historical prices	
	2017	2018	2019E	2020E	2021E	Spot	5-year avg.
Non-ferrous							
Hindalco Industries							
Aluminum prices (all -in)	1,789	2,167	2,200	2,225	2,275	2,385	2,096
Hindustan Zinc							
Lead	2,000	2,372	2,450	2,350	2,400	2,420	2,176
Zinc	2,365	3,047	3,100	2,750	2,800	3,080	2,391
Nalco							
Aluminum prices (all -in)	1,789	2,167	2,200	2,225	2,275	2,385	2,095
Vedanta							
Aluminum prices (all -in)	1,789	2,167	2,200	2,225	2,275	2,385	2,096
Lead	2,000	2,372	2,450	2,350	2,400	2,420	2,176
Zinc	2,365	3,047	3,100	2,750	2,800	3,080	2,391
Ferrous							
JSW Steel							
HRC price	493	604	574	561	561	674	666
NMDC							
Iron ore fines (Rs/ton)	2,033	2,871	2,428	2,443	2,481	3,179	2,686
Iron ore lumps (Rs/ton)	2,778	3,443	2,828	2,843	2,881	3,585	3,868
Tata Steel							
HRC price	493	604	574	561	561	674	662

Source: Bloomberg, Company, Kotak Institutional Equities estimates

Exhibit 36: Volumes of certain metal companies to jump sharply over the next two years
Volume assumptions of metal companies, March fiscal year-ends, 2017-21E ('000 tons)

	Volume assumptions				
	2017	2018	2019E	2020E	2021E
Non-ferrous					
Hindalco Industries					
Aluminum	1,266	1,291	1,291	1,291	1,291
Copper	368	408	408	408	418
Hindustan Zinc					
Lead	138	169	179	215	215
Zinc	696	793	778	943	955
Nalco					
Aluminum	389	426	442	442	442
Vedanta					
Aluminum	1,071	1,597	2,000	2,062	2,062
Copper	401	402	—	—	—
Lead	138	169	179	215	215
Zinc	852	950	1,029	1,349	1,362
Iron ore sales ('000 dmt)	10,100	7,600	2,300	2,300	2,300
Oil—gross ('000 boe/d)	190	186	215	245	256
Ferrous					
Jindal Steel and Power					
Finished steel sales	3,347	3,760	5,794	6,505	6,615
JSW Steel					
Finished steel sales	14,774	15,620	16,055	16,565	20,714
NMDC					
Iron ore sales	35,620	36,100	38,000	40,000	42,000
Tata Steel					
Steel deliveries (Standalone)	10,973	12,150	12,500	12,800	13,100
Steel deliveries (Europe)	9,930	9,990	10,116	10,116	10,116

Source: Company data, Kotak Institutional Equities estimates

- For ferrous metal stocks, the government's decision to impose minimum import prices (MIP)/anti-dumping duties for steel imports in 2016 will continue to support high profitability for the sector. We have seen significant improvement in the profitability of the domestic steel industry in FY2017 and FY2018 from trough levels in FY2016 although global steel prices and profitability have also recovered.
- ▶ **Oil & gas.** The earnings of the oil & gas sector, particularly the government-owned companies, is somewhat uncertain given risks of possible government intervention in pricing of diesel and gasoline (1) at higher levels of crude oil prices and (2) before state and general elections in case oil prices were to stay at high levels or increase further. We note that government-owned downstream oil companies kept the prices of diesel and gasoline stable before the Gujarat elections in December 2017 and Karnataka elections in May 2018 although they did raise prices subsequently to market levels.

For the government-owned upstream oil & gas companies, we already assume that they will bear a certain portion of oil subsidies (see Exhibit 37), which will result in their net realized crude price being meaningfully lower versus global crude oil prices. We model US\$55/bbl net realized price for OIL and ONGC for FY2019-21, which is well below our assumed crude price (Dated Brent basis) of US\$72.5/bbl for FY2019 and US\$67.5/bbl for FY2020 versus US\$57.6/bbl in FY2018. The government has so far refrained from imposing subsidy burden on the government-owned companies.

Exhibit 37: Our base-case scenario assumes 100% windfall tax on upstream PSUs above US\$55/bbl

Share of under-recoveries for various participants, March fiscal year-ends, 2010-20E (Rs bn)

	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019E	2020E
Macro-assumptions											
Dated Brent crude oil price (US\$/bbl)	67.1	84.0	113.5	111.8	107.8	85.7	48.0	49.0	57.5	72.5	67.5
Exchange rate (Rs/US\$)	47.4	45.6	47.9	54.4	60.5	61.1	65.5	67.1	64.5	68.7	69.5
Subsidy burden											
Petrol	52	22	49	11	—	—	—	—	—	—	—
Diesel	93	344	812	921	628	109	—	—	—	—	—
LPG	143	220	300	396	503	406	161	121	210	382	354
Kerosene	174	196	274	294	306	248	115	76	47	68	42
Subsidy burden	461	782	1,434	1,621	1,437	763	276	197	256	450	396
Gross under-recoveries	491	814	1,465	1,651	1,468	793	276	197	256	450	396
Subsidy sharing											
Payment by government (direct budgetary support)	30	32	31	31	31	31	—	—	—	—	—
Payment by government (oil bonds/cash)	260	410	835	1,000	746	313	263	197	256	255	257
Receipt from upstream companies	144	303	550	600	670	428	13	—	—	196	139
Share of ONGC	116	249	445	494	564	363	11	—	—	169	121
Share of Oil India	15	33	74	79	87	55	2	—	—	26	18
Share of GAIL	13	21	32	27	19	10	—	—	—	—	—
Net under-recovery of OMCs	56	69	49	21	21	22	0	—	—	—	—

Source: Companies, PPAC, Kotak Institutional Equities estimates

Thus, we do not see meaningful risks to our earnings estimates of the upstream oil & gas companies. In fact, we could see positive surprise in the earnings of OIL and ONGC if they are able to realize global prices for their crude oil. Exhibit 38 shows the EPS of the upstream oil companies at various levels of global crude oil prices and net realized oil prices for FY2019 and FY2020.

Exhibit 38: Earnings of ONGC and OIL are highly sensitive to crude price and net price realization assumptions

Earnings sensitivity of ONGC and OIL to crude price, March fiscal year-ends, 2019E-21E

	2019E			2020E			2021E		
	Downside	Base-case	Upside	Downside	Base-case	Upside	Downside	Base-case	Upside
ONGC									
Net realization (US\$/bbl)	50.0	55.0	60.0	50.0	55.0	60.0	50.0	55.0	60.0
Net profits (Rs mn)	238,007	261,062	284,116	238,316	261,766	285,216	222,594	246,364	270,133
Earnings per share (Rs)	18.5	20.3	22.1	18.6	20.4	22.2	17.3	19.2	21.0
% upside/(downside)	(8.8)		8.8	(9.0)		9.0	(9.6)		9.6
Oil India									
Net realization (US\$/bbl)	50.0	55.0	60.0	65.0	55.0	60.0	65.0	55.0	60.0
Net profits (Rs mn)	22,635	26,163	29,692	23,438	27,042	30,646	22,689	26,354	30,020
Earnings per share (Rs)	19.9	23.1	26.2	20.7	23.8	27.0	20.0	23.2	26.5
% upside/(downside)	(13.5)		13.5	(13.3)		13.3	(13.9)		13.9

Source: Kotak Institutional Equities estimates

For the government-owned downstream oil companies (BPCL, HPCL and IOCL), we model a decline in their earnings led by our assumption of (1) weaker refining margins; refining margins have been weak over the past 2-3 months as global crack spreads have come down due to the sharp increase in crude oil prices relative to product prices and (2) lower gross auto fuel marketing margins at ₹1.6/liter versus ₹1.8/liter in FY2018.

We do see downside risks to the marketing margins on auto fuels and earnings of the downstream oil companies in FY2019 as India has a few state elections as also the general elections over the next nine months. The downstream oil companies' earnings have very high sensitivity to small changes in refining (see Exhibit 39) and marketing (see Exhibit 40) margins.

Exhibit 39: Earnings of OMCs are highly sensitive to refining margin assumptions

Earnings sensitivity of BPCL, HPCL and IOCL to refining margins, March fiscal year-ends, 2019E-21E (Rs mn)

	2019E			2020E			2021E		
	Downside	Base-case	Upside	Downside	Base-case	Upside	Downside	Base-case	Upside
BPCL									
Refining margins (US\$/bbl)	5.5	6.5	7.5	5.6	6.6	7.6	5.6	6.6	7.6
Net profits (Rs mn)	63,951	73,891	83,831	65,938	76,178	86,418	66,639	77,036	87,434
EPS (Rs)	32.5	37.6	42.6	33.5	38.7	43.9	33.9	39.2	44.5
% upside/(downside)	(13.5)		13.5	(13.4)		13.4	(13.5)		13.5
HPCL									
Refining margins (US\$/bbl)	5.2	6.2	7.2	5.1	6.1	7.1	5.1	6.1	7.1
Net profits (Rs mn)	43,345	49,398	55,451	42,172	48,293	54,414	42,347	48,511	54,676
EPS (Rs)	28.4	32.4	36.4	27.7	31.7	35.7	27.8	31.8	35.9
% upside/(downside)	(12.3)		12.3	(12.7)		12.7	(12.7)		12.7
IOCL									
Refining margins (US\$/bbl)	6.2	7.2	8.2	5.4	6.4	7.4	5.6	6.6	7.6
Net profits (Rs mn)	149,206	172,658	196,110	141,675	165,638	189,602	146,223	170,359	194,495
EPS (Rs)	15.7	18.2	20.7	14.9	17.5	20.0	15.4	18.0	20.5
% upside/(downside)	(13.6)		13.6	(14.5)		14.5	(14.2)		14.2

Source: Kotak Institutional Equities estimates

Exhibit 40: Earnings of OMCs are highly sensitive to marketing margin assumptions

Earnings sensitivity of BPCL, HPCL and IOCL to marketing margins, March fiscal year-ends, 2019E-21E (Rs mn)

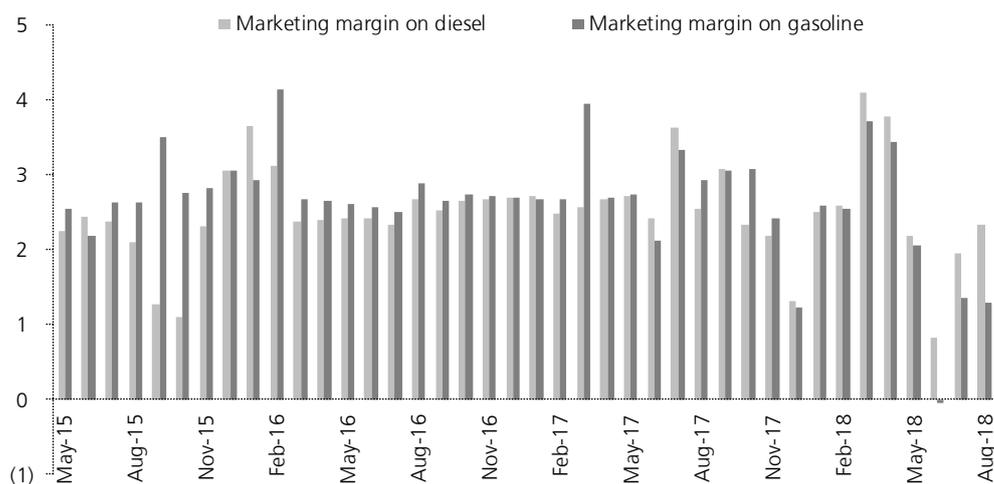
	2019E			2020E			2021E		
	Downside	Base-case	Upside	Downside	Base-case	Upside	Downside	Base-case	Upside
BPCL									
Auto fuels margins (Rs/liter)	1.1	1.6	2.1	1.3	1.8	2.3	1.3	1.8	2.3
Net profits (Rs mn)	62,308	73,891	85,474	64,097	76,178	88,259	64,430	77,036	89,642
EPS (Rs)	31.7	37.6	43.5	32.6	38.7	44.9	32.8	39.2	45.6
% upside/(downside)	(15.7)		15.7	(15.9)		15.9	(16.4)		16.4
HPCL									
Auto fuels margins (Rs/liter)	1.2	1.7	2.2	1.3	1.8	2.3	1.3	1.8	2.3
Net profits (Rs mn)	39,035	49,398	59,761	37,479	48,293	59,107	37,222	48,511	59,801
EPS (Rs)	25.6	32.4	39.2	24.6	31.7	38.8	24.4	31.8	39.2
% upside/(downside)	(21.0)		21.0	(22.4)		22.4	(23.3)		23.3
IOCL									
Auto fuels margins (Rs/liter)	1.1	1.6	2.2	1.2	1.8	2.3	1.3	1.8	2.3
Net profits (Rs mn)	152,671	172,658	192,645	144,819	165,638	186,458	148,664	170,359	192,054
EPS (Rs)	16.1	18.2	20.3	15.3	17.5	19.7	15.7	18.0	20.3
% upside/(downside)	(11.6)		11.6	(12.6)		12.6	(12.7)		12.7

Source: Kotak Institutional Equities estimates

We note that marketing margins on auto fuels are still below normal levels (see Exhibit 41 for monthly marketing margins on diesel and gasoline) as the oil companies have not raised prices of diesel and gasoline sufficiently to offset the increase in crude oil prices and depreciation in the INR fully.

Exhibit 41: Marketing margins on auto fuels have recovered recently

Gross marketing margin on diesel and gasoline, March fiscal year-ends, 2016-19 (Rs/liter)



Source: PPAC, Kotak Institutional Equities estimates

- ▶ **IT and pharmaceuticals.** We see moderate recovery in the profits of the IT and pharmaceuticals sectors from FY2019 although the recovery seems to be getting delayed for certain pharmaceutical companies (DRRD, LPC) with high exposure to the US generic market. 1QFY19 results of the pharmaceutical companies showed deeper-than-expected price erosion in the base US generic portfolio of the companies.

In the case of the IT sector, we expect FY2019 profits to recover from the low base of FY2018 as (1) the BFSI companies will likely increase their budgets after years of scrimping, (2) the likely depreciation in the currency will support EBIT margins, (3) mid-cap companies will see higher EBIT margins after addressing various company-specific issues (MT, TM) and (4) other income will increase from a low base in FY2018 due to lower cash balance on completion of buyback programs in FY2017-18.

In the case of the pharmaceuticals sector, we expect new launches to pick up from 2HFY19 driving US generic revenues and overall, revenues and profits. FY2018 profits were affected significantly by weak US generic revenues (see Exhibit 42) due to continued pricing pressure in the case of certain FTF products and delays in launches of new products. We have seen the trend continuing in 1QFY19.

Exhibit 42: We expect a strong pickup in US generic revenues of the pharmaceutical companies from FY2020

US revenues for pharmaceuticals companies, March fiscal year-ends, 2016-21E

	US revenues (US\$ mn)						Yoy growth (%)					
	2016	2017	2018	2019E	2020E	2021E	2016	2017	2018	2019E	2020E	2021E
Aurobindo	947	1,020	1,156	1,245	1,300	1,341	22	8	13	8	4	3
Cipla	324	392	401	497	564	742	119	21	2	24	13	32
Dr Reddy's	1,162	951	926	1,112	1,274	1,353	10	(18)	(3)	20	15	6
Lupin	915	1,207	898	774	938	1,079	(4)	32	(26)	(14)	21	15
Torrent	412	201	171	194	221	240	197	(51)	(15)	13	14	9
Sun Pharma	2,066	2,056	1,354	1,595	1,857	1,964	(8)	(1)	(34)	18	16	6
Taro	866	784	544	533	504	479	11	(9)	(31)	(2)	(5)	(5)
Ex-Taro Sun	1,200	1,271	810	1,063	1,353	1,485	(18)	6	(36)	31	27	10

Source: Companies, Kotak Institutional Equities estimates

Model Portfolio: No change

Exhibit 43 is our recommended large-cap. Model Portfolio. We have a judicious mix of (1) expensive 'growth' stocks that will likely correct less in the event of any market correction and where we expect growth in earnings/book to partly offset any correction in multiples and (2) inexpensive 'value' stocks that may correct further in the event of a market correction but where we expect a re-rating in multiples (P/E or P/B) led by positive company-specific issues (strong increase in earnings and improvement in financial returns).

Exhibit 44 is our recommended mid-cap. Model Portfolio.

Exhibit 43: 'Barbell' portfolio of 'growth' and 'value' stocks
KIE large-cap. Model Portfolio

Company	Price (Rs)		KIE weight	
	14-Aug-18		(%)	
Automobiles				
Mahindra & Mahindra	952		5.0	
Maruti Suzuki	9,133		3.1	
Tata Motors	249		2.1	
Automobiles			10.2	
Private Banks and NBFCs				
HDFC	1,942		8.1	
HDFC Bank	2,089		10.2	
ICICI Bank	332		8.5	
ICICI Prudential Life	399		1.9	
IndusInd Bank	1,998		2.3	
LIC Housing finance	547		1.9	
Private Banks and NBFCs			33.0	
PSU Banks				
Bank of Baroda	146		1.9	
State Bank of India	295		4.6	
PSU Banks			6.5	
Consumers				
Colgate-Palmolive (India)	1,134		2.1	
Dabur India	453		2.0	
Marico	364		2.2	
Consumers			6.3	
Energy				
GAIL (India)	380		3.0	
ONGC	166		1.9	
Energy				
Petronet LNG	222		1.8	
Reliance Industries	1,211		6.9	
Energy			13.7	
Industrials/Construction				
L&T	1,253		5.2	
Industrials/Construction			5.2	
Metals & Mining				
Hindalco Industries	221		2.6	
Vedanta	215		1.9	
Tata Steel	579		2.5	
Metals & Mining			7.1	
Others				
InterGlobe Aviation	1,051		1.6	
Others			1.6	
Pharmaceuticals				
Cipla	643		2.8	
Pharmaceuticals			2.8	
Technology				
Infosys	1,408		9.3	
Tech Mahindra	673		1.9	
Technology			11.2	
Utilities				
Power Grid	187		2.5	
Utilities			2.5	
BSE-30			37,852	100.0

Source: Kotak Institutional Equities estimates

Exhibit 44: We recommend mid-cap. stocks in automobile components, financials, industrials and power utilities
KIE mid-cap. Model Portfolio

Company	Sector	Rating	Target			Mkt cap. (Rs mn)	Mkt cap. (US\$ mn)	EPS (Rs)			PER (X)			PBR (X)			RoE (%)		
			Price (Rs)	price (Rs)	Upside (%)			2018	2019E	2020E	2018	2019E	2020E	2018	2019E	2020E	2018	2019E	2020E
CEESC	Utilities	BUY	909	1,180	29.7	120,547	1,725	87.1	114.8	128.1	10.4	7.9	7.1	0.8	0.8	0.7	7.9	10.0	10.4
Escorts	Automobiles	BUY	876	1,200	37.0	74,679	1,536	38.8	59.1	70.8	22.6	14.8	12.4	3.1	2.6	2.2	13.5	17.6	18.0
Federal Bank	Banks	BUY	89	130	46.4	175,839	2,516	4.4	5.7	7.9	20.3	15.7	11.3	1.6	1.4	1.3	8.2	8.8	11.4
Jyothy Laboratories	Consumer Products	ADD	223	240	7.7	81,007	1,159	4.4	5.6	6.6	50.6	39.6	34.0	7.1	6.1	5.3	14.4	16.6	16.8
Kalpitaru Power Transmission	Industrials	BUY	363	560	54.5	55,637	796	18.3	23.0	32.1	19.8	15.7	11.3	2.1	1.9	1.6	11.0	12.5	15.2
Laurus Labs	Pharmaceuticals	ADD	447	500	11.8	47,411	678	15.9	16.2	29.2	28.2	27.5	15.3	3.2	2.9	2.4	11.9	10.9	17.1
Max Financial Services	NBFCs	ADD	468	650	39.0	125,484	1,796	4.6	6.3	6.4	102.0	74.5	73.2	—	—	—	6.5	8.3	8.0
Prestige Estates Projects	Real Estate	ADD	254	315	24.1	95,156	1,362	12.5	9.5	10.3	20.2	26.7	24.6	2.0	1.9	1.8	10.3	7.3	7.5
Sadbhav Engineering	Infrastructure	BUY	271	440	62.5	46,470	665	12.9	17.8	18.2	21.1	15.2	14.9	2.5	2.2	1.9	12.5	15.2	13.7
Shriram City Union Finance	NBFCs	ADD	2,010	2,250	11.9	132,607	1,898	100.7	141.4	173.6	20.0	14.2	11.6	2.5	2.3	2.0	12.5	15.8	16.9

Source: Companies, Kotak Institutional Equities estimates

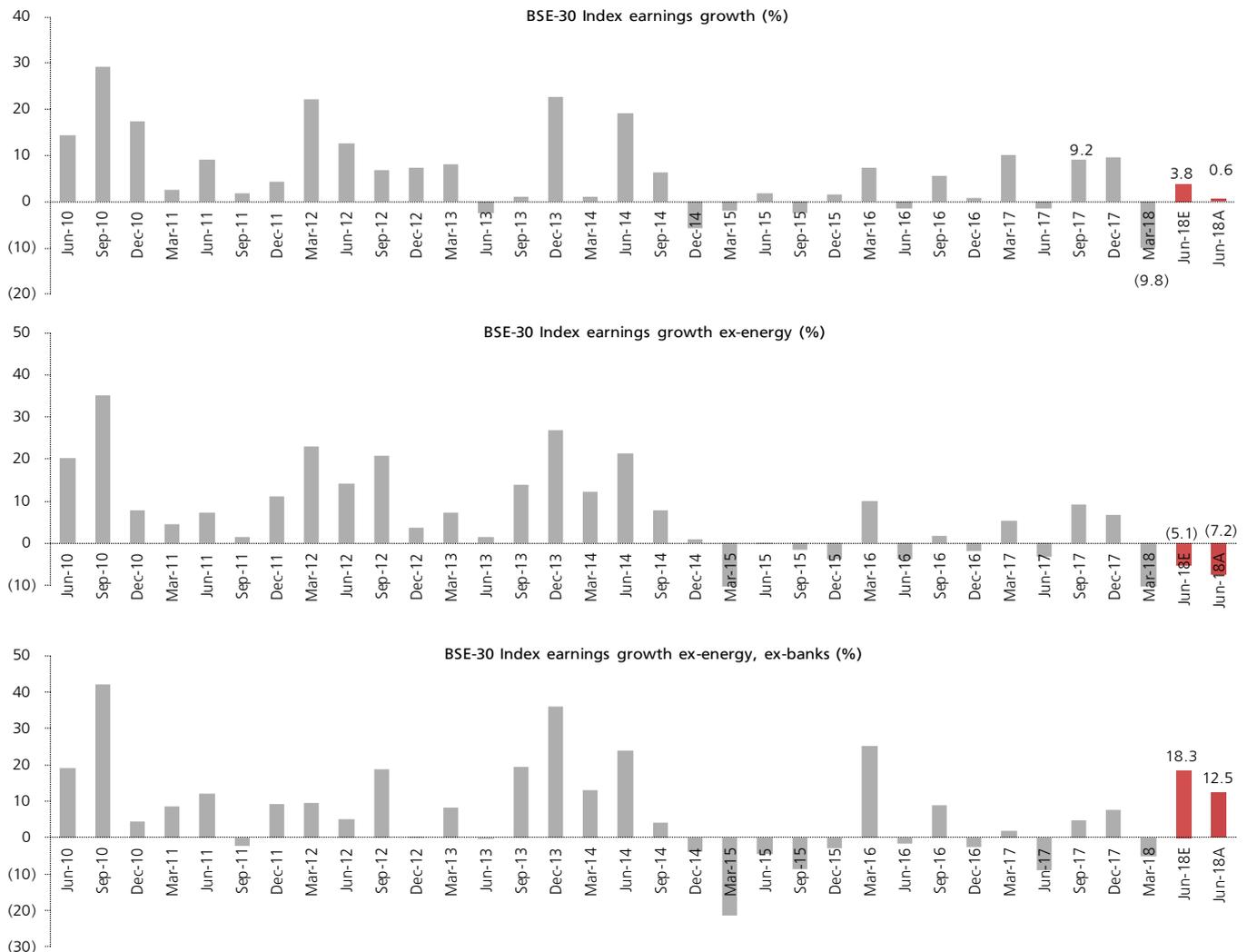
1QFY19 RESULTS ANALYSIS: BETTER THAN EXPECTATIONS

1QFY19 net profits of the KIE universe increased 12.5% yoy, led by double-digit growth in net income of almost every sector helped by the low base of 1QFY18. Net income of the KIE universe came in 14.4% ahead of our expectation, led by better-than-expected results of banks, especially of PSU banks, which reported lower-than-expected losses. Net profits of the BSE-30 Index and Nifty-50 Index grew 0.6% (3.1% below estimates) and 12.3% (2% ahead of estimates).

1QFY19 results: Net profits of the BSE-30 Index increased 0.6% yoy

Exhibit 45 presents the quarterly trend in earnings growth of the BSE-30 Index. Adjusted net profits of the BSE-30 Index increased 0.6% yoy versus our expectation of 3.8% yoy increase. Adjusted net profits of the Nifty-50 Index increased 12.3% yoy versus our expectation of 10.1% yoy increase. However, excluding banking stocks, net income of the BSE-30 Index and Nifty-50 Index increased 17.4% yoy and 27% yoy. High credit costs and provisions in case of Axis Bank, ICICI Bank and SBI dragged the yoy performance of BSE-30 Index and Nifty-50 Index.

Exhibit 45: 1QFY19 adjusted net profits of the BSE-30 Index increased 0.6% yoy versus our expectations of 3.8% increase
Adjusted net income growth of BSE-30 Index (%)



Source: Kotak Institutional Equities estimates

- Net profits versus expectations for BSE-30 Index and Nifty-50 Index. Exhibit 46 compares 1QFY19 adjusted net profits of the BSE-30 stocks with 1QFY18, 4QFY18 and 1QFY19E adjusted net profits while Exhibit 47 compares 1QFY19 adjusted net profits of the Nifty-50 Index with 1QFY18, 4QFY18 and 1QFY19E adjusted net profits.

Exhibit 46: 1QFY19 results of the BSE-30 Index were below expectations

Comparison of 1QFY19 net income of BSE-30 stocks, actual versus expected

Company	Sector	Adjusted net income (Rs bn)				Change (%) A versus E	Growth (%)		
		Jun-17	Mar-18	Jun-18A	Jun-18E		yoy	qoq	2y CAGR
Bajaj Auto	Automobiles	9.5	10.8	11.2	12.5	(10)	18	3	7
Hero Motocorp	Automobiles	9.1	9.7	9.1	10.1	(10)	(1)	(6)	1
Mahindra & Mahindra	Automobiles	7.5	11.2	12.6	11.4	11	67	12	25
Maruti Suzuki	Automobiles	15.6	18.8	19.8	24.0	(18)	27	5	15
Tata Motors	Automobiles	2.1	30.2	(12.0)	(5.1)	(134)	(681)	(140)	NM
Axis Bank	Banking	13.1	(21.9)	7.0	0.2	4,021	(46)	132	(33)
HDFC	Banking	14.2	28.5	21.9	22.5	(3)	54	(23)	8
HDFC Bank	Banking	38.9	48.0	46.0	46.9	(2)	18	(4)	19
ICICI Bank	Banking	20.5	10.2	(1.2)	0.4	(402)	(106)	(112)	NM
IndusInd Bank	Banking	8.4	9.5	10.4	10.0	4	24	9	25
Kotak Mahindra Bank	Banking	13.5	17.9	15.7	15.2	4	17	(12)	21
State Bank of India	Banking	20.1	(77.2)	(48.8)	(52.6)	7	(343)	37	NM
Yes Bank	Banking	9.7	11.8	12.6	12.0	5	31	7	31
Asian Paints	Consumers	4.2	4.8	5.6	5.4	3	31	16	2
Hindustan Unilever	Consumers	12.9	14.1	15.7	16.4	(4)	21	11	18
ITC	Consumers	25.6	29.3	28.2	27.3	3	10	(4)	9
ONGC	Energy	38.8	59.2	61.4	70.0	(12)	58	4	20
Reliance Industries	Energy	80.2	94.4	94.6	95.0	(0)	18	0	15
L&T	Industrials	8.9	31.7	12.1	11.4	6	36	(62)	41
Adani Ports and SEZ	Infrastructure	7.7	9.3	6.9	7.7	(10)	(10)	(25)	(8)
Coal India	Metals & Mining	23.5	12.9	37.8	30.2	25	61	192	11
Tata Steel	Metals & Mining	15.4	32.6	22.8	32.4	(30)	49	(30)	168
Vedanta	Metals & Mining	15.3	24.2	15.3	25.1	(39)	1	(37)	58
Sun Pharmaceuticals	Pharmaceuticals	5.3	10.5	9.8	8.9	11	87	(6)	(31)
Infosys	Technology	34.8	36.9	36.1	37.1	(3)	4	(2)	3
TCS	Technology	59.5	69.0	73.4	69.5	6	23	6	8
Wipro	Technology	20.8	18.0	21.2	20.0	6	2	18	2
Bharti Airtel	Telecom	4.1	4.1	(5.4)	(4.5)	(20)	(232)	(232)	NM
NTPC	Utilities	26.2	25.4	25.9	27.5	(6)	(1)	2	5
Power Grid	Utilities	19.8	18.5	22.4	20.5	9	13	21	12
BSE-30 Index		585	602	588	607	(3.1)	0.6	(2.3)	1.1
BSE-30 Index (ex-energy)		466	449	432	442	(2.3)	(7.2)	(3.7)	(3.2)
BSE-30 Index (ex-banks)		447	576	525	553	(5.1)	17.4	(8.9)	7.1
BSE-30 Index (ex-banks, energy)		328	422	369	388	(4.9)	12.5	(12.7)	3.5

Notes:

(a) Kotak Mahindra Bank is not under KIE coverage. We used consensus estimates.

Source: Bloomberg, Companies, Kotak Institutional Equities estimates

Exhibit 47: 1QFY19 results of the Nifty-50 Index were moderately above estimates led by the strong performance of the downstream oil stocks (large adventitious gains)

Comparison of 1QFY19 net income of Nifty-50 stocks, actual versus expected

Company	Sector	Adjusted net income (Rs bn)				Change (%) A versus E	Growth (%)		
		Jun-17	Mar-18	Jun-18A	Jun-18E		yoy	qoq	2y CAGR
Bajaj Auto	Automobiles	9.5	10.8	11.2	12.5	(10)	18	3	7
Eicher Motors	Automobiles	4.6	6.5	5.8	6.0	(3)	25	(11)	24
Hero Motocorp	Automobiles	9.1	9.7	9.1	10.1	(10)	(1)	(6)	1
Mahindra & Mahindra	Automobiles	7.5	11.2	12.6	11.4	11	67	12	25
Maruti Suzuki	Automobiles	15.6	18.8	19.8	24.0	(18)	27	5	15
Tata Motors	Automobiles	2.1	30.2	(12.0)	(5.1)	(134)	(681)	(140)	NM
Axis Bank	Banking	13.1	(21.9)	7.0	0.2	4,021	(46)	132	(33)
Bajaj Finance	Banking	6.0	7.2	10.2	8.2	25	69	41	55
Bajaj Finserv	Banking	5.8	6.9	8.3	7.7	7	41	20	24
HDFC	Banking	14.2	28.5	21.9	22.5	(3)	54	(23)	8
HDFC Bank	Banking	38.9	48.0	46.0	46.9	(2)	18	(4)	19
ICICI Bank	Banking	20.5	10.2	(1.2)	0.4	(402)	(106)	(112)	NM
Indiabulls Housing Finance	Banking	7.9	10.3	10.5	9.4	12	34	2	29
IndusInd Bank	Banking	8.4	9.5	10.4	10.0	4	24	9	25
Kotak Mahindra Bank	Banking	13.5	17.9	15.7	15.2	4	17	(12)	21
State Bank of India	Banking	20.1	(77.2)	(48.8)	(52.6)	7	(343)	37	NM
Yes Bank	Banking	9.7	11.8	12.6	12.0	5	31	7	31
Grasim Industries	Cement	3.5	5.9	6.4	5.1	25	85	9	42
Ultratech Cement	Cement	8.9	7.1	6.0	5.8	2	(33)	(16)	(12)
Asian Paints	Consumers	4.2	4.8	5.6	5.4	3	31	16	2
Hindustan Unilever	Consumers	12.9	14.1	15.7	16.4	(4)	21	11	18
ITC	Consumers	25.6	29.3	28.2	27.3	3	10	(4)	9
Titan Company	Consumers	2.8	3.4	3.5	3.7	(5)	26	4	36
BPCL	Energy	7.4	26.7	22.9	18.5	24	208	(14)	(6)
GAIL (India)	Energy	9.0	9.9	12.6	10.2	23	40	27	22
HPCL	Energy	9.2	17.5	17.2	13.7	25	86	(2)	(9)
IOCL	Energy	26.7	51.7	68.3	50.1	36	156	32	(9)
ONGC	Energy	38.8	59.2	61.4	70.0	(12)	58	4	20
Reliance Industries	Energy	80.2	94.4	94.6	95.0	(0)	18	0	15
L&T	Industrials	8.9	31.7	12.1	11.4	6	36	(62)	41
Adani Ports and SEZ	Infrastructure	7.7	9.3	6.9	7.7	(10)	(10)	(25)	(8)
Zee Entertainment Enterprises	Media	3.1	3.9	3.5	3.8	(8)	12	(12)	2
Coal India	Metals & Mining	23.5	12.9	37.8	30.2	25	61	192	11
Hindalco Industries	Metals & Mining	3.9	3.8	4.1	5.6	(27)	5	10	19
Tata Steel	Metals & Mining	15.4	32.6	22.8	32.4	(30)	49	(30)	168
Vedanta	Metals & Mining	15.3	24.2	15.3	25.1	(39)	1	(37)	58
UPL	Others	4.4	9.3	5.1	4.7	8	14	(45)	15
Cipla	Pharmaceuticals	4.1	1.5	4.5	3.2	38	9	191	14
Dr Reddy's Laboratories	Pharmaceuticals	0.6	3.0	4.6	3.1	48	672	51	90
Lupin	Pharmaceuticals	3.6	4.0	2.0	3.5	(42)	(44)	(50)	(52)
Sun Pharmaceuticals	Pharmaceuticals	5.3	10.5	9.8	8.9	11	87	(6)	(31)
HCL Technologies	Technology	21.7	22.3	24.0	22.3	8	11	8	8
Infosys	Technology	34.8	36.9	36.1	37.1	(3)	4	(2)	3
TCS	Technology	59.5	69.0	73.4	69.5	6	23	6	8
Tech Mahindra	Technology	8.0	12.2	9.0	8.7	4	13	(26)	10
Wipro	Technology	20.8	18.0	21.2	20.0	6	2	18	2
Bharti Airtel	Telecom	4.1	4.1	(5.4)	(4.5)	(20)	(232)	(232)	NM
Bharti Infratel	Telecom	6.6	6.6	6.4	6.2	3	(4)	(3)	(8)
NTPC	Utilities	26.2	25.4	25.9	27.5	(6)	(1)	2	5
Power Grid	Utilities	19.8	18.5	22.4	20.5	9	13	21	12
Nifty-50 Index		733	822	823	807	2.0	12.3	0.1	1.1
Nifty-50 Index (ex-energy)		561	563	546	549	(0.6)	(2.8)	(3.0)	(0.7)
Nifty-50 Index (ex-banks)		575	771	730	727	0.5	27.0	(5.3)	4.3
Nifty-50 Index (ex-banks, energy)		403	512	453	469	(3.4)	12.4	(11.4)	3.9

Notes:

(a) Indiabulls Housing Finance and Kotak Mahindra Bank in Nifty-50 Index are not under KIE coverage. We have used consensus estimates.

Source: Bloomberg, Companies, Kotak Institutional Equities estimates

Among Nifty-50 Index stocks that outperformed our estimates at the net income level were: (1) Axis Bank, (2) BPCL, HPCL and IOCL (large adventitious gains), (3) Cipla (higher other income), (4) DRRD (higher gross margin, lower-than-expected R&D, lower tax) and (5) M&M (lower-than-expected other expenses).

On the other hand, a few stocks underperformed our estimates: (1) Bharti Airtel, (2) ICICI Bank (high provisions), (3) Lupin (sharp decline in the US revenues due to competitive pressures, market changes and lack of specific market opportunities), (4) Maruti Suzuki (higher-than-expected increase in other expenses), (5) ONGC (decline in other income and a higher tax rate), (6) Tata Motors (weaker-than-expected performance of JLR led by one-time de-stocking in China and higher-than-expected hedge and forex losses) and (7) Vedanta (lower zinc volumes, forex losses)

- **EBITDA in line with our expectations.** Adjusted EBITDA of the BSE-30 Index increased 27.8% yoy versus our expectations of 26.8% yoy increase. The strong yoy growth reflects (1) low base in 1QFY18 in the case of several domestic consumption sectors and (2) higher commodity prices and profitability (oil & gas sector). Exhibit 48 compares 1QFY19 EBITDA of the BSE-30 Index with 1QFY18, 4QFY18 and 1QFY19E EBITDA. Out of the 22 non-finance companies in the BSE-30 Index, six companies beat our estimates by more than 5% but six companies missed our EBITDA estimates by more than 5%.

Exhibit 48: 1QFY19 EBITDA of the BSE-30 Index was in line with estimates

Comparison of 1QFY19 EBITDA of BSE-30 stocks, actual versus expected

Company	Sector	Adjusted EBITDA (Rs bn)				Change (%) A versus E	Growth (%)	
		Jun-17	Mar-18	Jun-18A	Jun-18E		yoy	qoq
Bajaj Auto	Automobiles	9.4	13.2	12.8	15.1	(15)	37	(3)
Hero Motocorp	Automobiles	13.0	13.7	13.8	14.3	(4)	6	0
Mahindra & Mahindra	Automobiles	14.3	19.9	21.1	20.3	4	47	6
Maruti Suzuki	Automobiles	23.3	30.2	33.5	35.8	(6)	44	11
Tata Motors	Automobiles	49.6	108.9	54.3	58.7	(7)	9	(50)
Asian Paints	Consumers	6.7	8.4	8.7	8.3	5	31	4
Hindustan Unilever	Consumers	18.7	20.5	22.5	23.5	(4)	21	10
ITC	Consumers	37.5	41.4	42.0	40.1	5	12	1
ONGC	Energy	98.8	113.8	147.3	155.7	(5)	49	29
Reliance Industries	Energy	125.5	184.7	206.6	187.7	10	65	12
L&T	Industrials	20.6	53.9	29.1	24.5	19	42	(46)
Adani Ports and SEZ	Infrastructure	15.7	19.3	15.9	14.1	13	1	(18)
Coal India	Metals & Mining	27.6	(16.0)	40.7	36.6	11	47	354
Tata Steel	Metals & Mining	49.7	65.0	64.7	73.6	(12)	30	(0)
Dr Reddy's Laboratories	Pharmaceuticals	3.1	5.5	7.6	6.9	9	148	37
Sun Pharmaceuticals	Pharmaceuticals	11.0	16.8	16.1	15.2	6	47	(5)
Infosys	Technology	45.6	49.3	49.7	49.9	(0)	9	1
TCS	Technology	74.1	86.5	90.7	89.1	2	22	5
Wipro	Technology	26.9	25.1	25.0	27.5	(9)	(7)	(0)
Bharti Airtel	Telecom	77.6	69.3	67.3	65.7	2	(13)	(3)
NTPC	Utilities	50.4	59.1	59.5	58.8	1	18	1
Power Grid	Utilities	62.0	65.2	71.4	70.5	1	15	9
BSE-30 Index		861	1,054	1,100	1,092	0.8	27.8	4.4
BSE-30 Index (ex-energy)		637	755	746	749	(0.3)	17.2	(1.2)

Source: Companies, Kotak Institutional Equities estimates

We do the same exercise for the Nifty-50 Index in Exhibit 49. For the Nifty-50 Index, adjusted EBITDA increased 35%, 3.7% ahead of expectation. Of the 39 non-finance companies in the Nifty-50 Index, 13 beat our estimates by more than 5%, while 10 missed our EBITDA estimates by more than 5%.

Exhibit 49: 1QFY19 EBITDA was ahead of estimates

Comparison of 1QFY19 EBITDA of Nifty-50 stocks, actual versus expected

Company	Sector	Adjusted EBITDA (Rs bn)				Change (%) A versus E	Growth (%)	
		Jun-17	Mar-18	Jun-18A	Jun-18E		yoy	qoq
Bajaj Auto	Automobiles	9.4	13.2	12.8	15.1	(15)	37	(3)
Eicher Motors	Automobiles	6.2	8.0	8.1	8.0	1	30	2
Hero Motocorp	Automobiles	13.0	13.7	13.8	14.3	(4)	6	0
Mahindra & Mahindra	Automobiles	14.3	19.9	21.1	20.3	4	47	6
Maruti Suzuki	Automobiles	23.3	30.2	33.5	35.8	(6)	44	11
Tata Motors	Automobiles	49.6	108.9	54.3	58.7	(7)	9	(50)
Grasim Industries	Cement	5.6	8.4	10.5	8.4	26	90	25
Ultratech Cement	Cement	15.6	17.0	16.2	15.5	5	4	(5)
Asian Paints	Consumers	6.7	8.4	8.7	8.3	5	31	4
Hindustan Unilever	Consumers	18.7	20.5	22.5	23.5	(4)	21	10
ITC	Consumers	37.5	41.4	42.0	40.1	5	12	1
Titan Company	Consumers	3.9	4.6	5.0	5.3	(6)	27	9
BPCL	Energy	12.3	37.2	38.8	29.6	31	216	4
GAIL (India)	Energy	17.0	17.0	22.4	18.6	21	32	32
HPCL	Energy	16.3	29.2	31.9	25.7	24	96	9
IOCL	Energy	51.9	106.5	125.8	94.4	33	142	18
ONGC	Energy	98.8	113.8	147.3	155.7	(5)	49	29
Reliance Industries	Energy	125.5	184.7	206.6	187.7	10	65	12
L&T	Industrials	20.6	53.9	29.1	24.5	19	42	(46)
Adani Ports and SEZ	Infrastructure	15.7	19.3	15.9	14.1	13	1	(18)
Zee Entertainment Enterprises	Media	4.8	5.1	5.7	5.8	(2)	17	12
Coal India	Metals & Mining	27.6	(16.0)	40.7	36.6	11	47	354
Hindalco Industries	Metals & Mining	11.5	12.6	13.3	15.5	(15)	15	5
Tata Steel	Metals & Mining	49.7	65.0	64.7	73.6	(12)	30	(0)
Vedanta	Metals & Mining	48.7	78.4	62.8	66.8	(6)	29	(20)
UPL	Others	7.5	12.2	8.5	8.3	1	13	(30)
Cipla	Pharmaceuticals	6.5	5.6	7.3	7.0	4	12	30
Dr Reddy's Laboratories	Pharmaceuticals	3.1	5.5	7.6	6.9	9	148	37
Lupin	Pharmaceuticals	7.7	7.1	5.3	8.0	(34)	(31)	(26)
Sun Pharmaceuticals	Pharmaceuticals	11.0	16.8	16.1	15.2	6	47	(5)
HCL Technologies	Technology	26.8	30.4	32.3	31.1	4	20	6
Infosys	Technology	45.6	49.3	49.7	49.9	(0)	9	1
TCS	Technology	74.1	86.5	90.7	89.1	2	22	5
Tech Mahindra	Technology	9.3	14.1	13.6	12.9	5	45	(4)
Wipro	Technology	26.9	25.1	25.0	27.5	(9)	(7)	(0)
Bharti Airtel	Telecom	77.6	69.3	67.3	65.7	2	(13)	(3)
Bharti Infratel	Telecom	15.8	15.9	15.2	15.5	(2)	(4)	(5)
NTPC	Utilities	50.4	59.1	59.5	58.8	1	18	1
Power Grid	Utilities	62.0	65.2	71.4	70.5	1	15	9
Nifty-50 Index		1,128	1,463	1,523	1,468	3.7	35.0	4.1
Nifty-50 Index (ex-energy)		807	975	950	957	(0.7)	17.8	(2.5)

Source: Companies, Kotak Institutional Equities estimates

Many of the companies in the Nifty-50 Index outperformed at the EBITDA level. Among the notable outperformers were (1) BPCL and HPCL (large adventitious gains versus large adventitious losses in 1QFY18), (2) DRRD (higher gross margin, lower R&D expenses), (3) RIL (sharp increase in petrochemical contribution) and (4) L&T (margin improvement).

Among the companies that missed were (1) Bajaj Auto (led by deterioration in the product mix and increase in discounts), (2) Hindalco (higher-than-expected alumina transfer price from Utkal Alumina resulted in lower EBITDA of standalone company), (3) Lupin (sharp decline in the US business) and (4) Tata Motors (lower-than-expected results at JLR).

► **Reported net income of the Nifty-50 Index increased 5.9% yoy and 6.1% qoq.**

Exhibit 50 shows the reported net income of the Nifty-50 Index for 1QFY18, 4QFY18 and 1QFY19. A few companies had large extraordinary items in 1QFY19. (1) Adani Ports booked forex MTM loss of ₹3.8 bn in 1QFY19 on US\$-denominated loans as per Ind-AS prescription, (2) Bharti Airtel had exceptional items of ₹6.4 bn for network re-farming and up-gradation program, levies and taxes pertaining to internal restructuring and litigation-related assessment and integration-related cost, (3) Tata Motors reported forex losses related to revaluation of current assets and liabilities (working capital) and (4) Tata Steel reported ₹3.7 bn of forex losses at its SE Asian operations.

Exhibit 50: Reported net income of the BSE-30 Index increased 5.9% yoy and declined 6.1% qoq
Comparison of 1QFY19 reported net income of Nifty-50 stocks

Company	Sector	Reported net income (Rs bn)			Growth (%)	
		Jun-17	Mar-18	Jun-18	yoy	qoq
Bajaj Auto	Automobiles	9.9	10.8	11.2	13	3
Eicher Motors	Automobiles	4.6	4.6	5.8	25	25
Hero Motocorp	Automobiles	9.1	9.7	9.1	(1)	(6)
Mahindra & Mahindra	Automobiles	7.5	11.5	12.6	67	9
Maruti Suzuki	Automobiles	15.6	18.8	19.8	27	5
Tata Motors	Automobiles	31.8	21.3	(19.0)	(160)	(190)
Axis Bank	Banking	13.1	(21.9)	7.0	NM	NM
Bajaj Finance	Banking	6.0	7.2	10.2	69	41
Bajaj Finserv	Banking	5.8	6.9	8.3	41	20
HDFC	Banking	14.2	28.5	21.9	54	(23)
HDFC Bank	Banking	38.9	48.0	46.0	18	(4)
ICICI Bank	Banking	20.5	10.2	(1.2)	(106)	(112)
Indiabulls Housing Finance	Banking	7.9	10.3	10.5	34	2
IndusInd Bank	Banking	8.4	9.5	10.4	24	9
Kotak Mahindra Bank	Banking	13.5	17.9	15.7	17	(12)
State Bank of India	Banking	20.1	(77.2)	(48.8)	NM	NM
Yes Bank	Banking	9.7	11.8	12.6	31	7
Grasim Industries	Cement	3.5	3.7	6.4	85	72
Ultratech Cement	Cement	8.9	4.9	6.0	(33)	23
Asian Paints	Consumers	4.3	4.8	5.6	31	16
Hindustan Unilever	Consumers	12.8	13.5	15.3	19	13
ITC	Consumers	25.6	29.3	28.2	10	(4)
Titan Company	Consumers	2.7	2.8	3.5	31	24
BPCL	Energy	7.4	26.7	22.9	208	(14)
GAIL (India)	Energy	9.0	10.2	12.6	40	23
HPCL	Energy	9.2	17.5	17.2	86	(2)
IOCL	Energy	45.5	52.2	68.3	50	31
ONGC	Energy	38.8	59.2	61.4	58	4
Reliance Industries	Energy	91.1	94.4	94.6	4	0
L&T	Industrials	8.9	31.7	12.1	36	(62)
Adani Ports and SEZ	Infrastructure	8.2	12.1	10.1	22	(17)
Zee Entertainment Enterprises	Media	2.5	2.3	3.3	30	41
Coal India	Metals & Mining	23.5	12.9	37.8	61	192
Hindalco Industries	Metals & Mining	2.9	3.8	4.1	43	10
Tata Steel	Metals & Mining	9.2	101.9	19.5	113	(81)
Vedanta	Metals & Mining	15.3	32.7	15.3	1	(53)
UPL	Others	4.7	7.4	5.1	8	(31)
Cipla	Pharmaceuticals	4.1	1.5	4.5	9	191
Dr Reddy's Laboratories	Pharmaceuticals	0.6	3.0	4.6	672	51
Lupin	Pharmaceuticals	3.6	(7.8)	2.0	(44)	126
Sun Pharmaceuticals	Pharmaceuticals	(4.2)	13.3	9.8	331	(26)
HCL Technologies	Technology	21.7	22.3	24.0	11	8
Infosys	Technology	34.8	36.9	36.1	4	(2)
TCS	Technology	59.5	69.0	73.4	23	6
Tech Mahindra	Technology	8.0	12.2	9.0	13	(26)
Wipro	Technology	20.8	18.0	21.2	2	18
Bharti Airtel	Telecom	3.7	0.8	1.0	(74)	17
Bharti Infratel	Telecom	6.6	6.1	6.4	(4)	5
NTPC	Utilities	26.2	29.3	25.9	(1)	(12)
Power Grid	Utilities	19.8	18.5	22.4	13	21
Nifty-50 Index		776	875	822	5.9	(6.1)

Source: Companies, Kotak Institutional Equities

Exhibit 51 compares reported net income of the Nifty-50 Index with adjusted net income. We remove extraordinary items, such as prior-period items, while computing adjusted EBITDA and net income (adjusted for tax impact) but do not remove additional branding costs, employee costs or foreign currency-related gains or losses. These represent normal costs of doing business. Finally, banks reported very high loan-loss provisions over the past few quarters pertaining to fresh impaired assets but we treat this as a normal P&L item and anyway, P&Ls of banks are less relevant compared to their balance sheets.

Exhibit 51: Few cases of one-off items in 1QFY19

Adjusted and reported net income of the Nifty-50 stocks, 1QFY19 (Rs mn)

Company	Sector	Net income		
		Adjusted	Reported	Difference
Bajaj Auto	Automobiles	11,152	11,152	—
Eicher Motors	Automobiles	5,762	5,762	—
Hero Motocorp	Automobiles	9,092	9,092	—
Mahindra & Mahindra	Automobiles	12,572	12,572	—
Maruti Suzuki	Automobiles	19,753	19,753	—
Tata Motors	Automobiles	(11,973)	(19,024)	(7,051)
Axis Bank	Banking	7,011	7,011	—
Bajaj Finance	Banking	10,180	10,180	—
Bajaj Finserv	Banking	8,258	8,258	—
HDFC	Banking	21,900	21,900	—
HDFC Bank	Banking	46,014	46,014	—
ICICI Bank	Banking	(1,196)	(1,196)	—
Indiabulls Housing Finance	Banking	10,547	10,547	—
IndusInd Bank	Banking	10,357	10,357	—
Kotak Mahindra Bank	Banking	15,745	15,745	—
State Bank of India	Banking	(48,759)	(48,759)	—
Yes Bank	Banking	12,604	12,604	—
Grasim Industries	Cement	6,426	6,426	—
Ultratech Cement	Cement	5,984	5,984	—
Asian Paints	Consumers	5,580	5,580	—
Hindustan Unilever	Consumers	15,670	15,290	(380)
ITC	Consumers	28,187	28,187	—
Titan Company	Consumers	3,492	3,492	—
BPCL	Energy	22,933	22,933	—
GAIL (India)	Energy	12,593	12,593	—
HPCL	Energy	17,192	17,192	—
IOCL	Energy	68,313	68,311	(2)
ONGC	Energy	61,439	61,439	—
Reliance Industries	Energy	94,590	94,590	—
L&T	Industrials	12,148	12,148	—
Adani Ports and SEZ	Infrastructure	6,907	10,065	3,158
Zee Entertainment Enterprises	Media	3,472	3,259	(213)
Coal India	Metals & Mining	37,843	37,843	—
Hindalco Industries	Metals & Mining	4,135	4,135	—
Tata Steel	Metals & Mining	22,803	19,540	(3,263)
Vedanta	Metals & Mining	15,330	15,330	—
UPL	Others	5,091	5,100	9
Cipla	Pharmaceuticals	4,456	4,456	—
Dr Reddy's Laboratories	Pharmaceuticals	4,561	4,561	—
Lupin	Pharmaceuticals	2,001	2,001	—
Sun Pharmaceuticals	Pharmaceuticals	9,825	9,825	—
HCL Technologies	Technology	24,031	24,031	—
Infosys	Technology	36,120	36,120	—
TCS	Technology	73,400	73,400	—
Tech Mahindra	Technology	8,994	8,994	—
Wipro	Technology	21,205	21,205	—
Bharti Airtel	Telecom	(5,363)	973	6,336
Bharti Infratel	Telecom	6,380	6,380	—
NTPC	Utilities	25,881	25,881	—
Power Grid	Utilities	22,405	22,405	—

Source: Companies, Kotak Institutional Equities estimates

KIE coverage universe: Net profits increase 12.5% yoy

1QFY19 net profits of the KIE coverage universe increased 12.5% yoy, 14.4% ahead of our expectations. In our coverage universe, 69 stocks beat our earnings forecast by more than 5%, 59 reported adjusted net income in the -5% and +5% range of our estimates and 68 missed our estimates by more than 5%.

Exhibit 52 compares 1QFY19 net profits of KIE coverage sectors with 1QFY18, 4QFY18 and 1QFY19E net profits. As can be seen, many sectors delivered double-digit growth in net income on a yoy basis, helped by a low base in certain sectors, large adventitious gains in 1QFY19 in the case of downstream oil companies and higher metal prices in the case of metal & mining companies.

Exhibit 52: 1QFY19 net income of KIE coverage increased 12.5% yoy
Comprehensive sector-wise PAT analysis of 1QFY19 earnings season (Rs bn)

	Jun-17	Mar-18	Jun-18A	Jun-18E	Change (%)			
					A/E	yoy	qoq	2y CAGR
Automobiles	66	119	73	88	(17)	11	(38)	(10)
Banks/Financial Institutions	200	(194)	119	(11)	1,187	(41)	161	(16)
Cement	27	26	26	21	20	(6)	(1)	2
Consumer products	71	82	86	88	(2)	21	5	11
Energy	186	281	296	278	6	59	6	5
Industrials	19	51	27	26	4	37	(48)	24
Infrastructure	15	19	15	16	(9)	(4)	(22)	3
Internet	1	0	1	1	(10)	(1)	303	10
Media	8	9	11	11	(2)	33	12	12
Metals & Mining	90	143	141	151	(7)	56	(1)	44
Others	26	23	25	24	4	(3)	10	5
Pharmaceuticals	22	29	29	29	1	30	(1)	(20)
Real Estate	4	6	7	4	99	70	15	10
Technology	152	167	173	166	4	14	4	6
Telecom	3	1	(17)	(15)	(15)	(704)	(1,323)	NM
Utilities	63	56	64	63	2	2	15	3
KIE universe	955	818	1,074	939	14.4	12.5	31.3	2.0
KIE universe (ex-energy)	768	537	778	660	17.8	1.3	44.8	0.7
KIE universe (ex-banks)	754	1,012	956	950	0.6	26.7	(5.5)	5.1
KIE universe (ex-banks, energy)	568	731	659	671	(1.8)	16.1	(9.8)	4.9

Source: Kotak Institutional Equities estimates

The banking sector reported a modest profit despite very high provisions for a few private banks and PSU banks under our coverage. Axis Bank, ICICI Bank and SBI reported sharp decline in net income on yoy basis. The downstream oil companies reported a sharp increase in net income on a yoy basis due to large adventitious gains in 1QFY19 versus adventitious losses in 1QFY18.

Subdued US revenues of most pharmaceutical companies resulted in a modest yoy increase in the net income of pharmaceutical companies. However, the telecom sector saw a sharp decline in net profits due to continued aggressive pricing strategy of R-Jio.

Exhibit 53 shows sectors that exceeded or fell short of our expectations on sales, EBITDA and net profits. Cement, industrials and metals & mining beat our estimates at the revenue level while automobiles, consumer products and energy missed our revenue expectations. Cement, energy and industrials beat EBITDA estimates but automobiles, metals & mining and pharmaceuticals disappointed. Finally, Banks/FIs, cement and energy beat our expectations at the net income level while automobiles, infrastructure and telecom disappointed.

Exhibit 53: 1QFY19 net profits of automobiles, banks and metals & mining underperformed expectations

Performance of sectors versus expectations (KIE universe) in 1QFY19/2QCY18 (Rs bn)

	Companies	Net sales (Rs bn)		Change
	(#)	Actual	Expected	(%)
Revenues: Sectors posting positive surprises				
Cement	10	297	285	4
Metals & Mining	9	1,341	1,291	4
Industrials	13	539	522	3
Banks/Financial Institutions	35	988	964	2
Utilities	7	418	408	2
Revenues: Sectors posting negative surprises				
Real Estate	7	56	61	(9)
Automobiles	22	1,708	1,732	(1)
Consumer products	23	564	571	(1)
Energy	12	4,580	4,612	(1)
Media	6	63	64	(1)

	Companies	EBITDA (Rs bn)		Change
	(#)	Actual	Expected	(%)
EBITDA: Sectors posting positive surprises				
Cement	10	54	48	14
Energy	12	609	548	11
Industrials	13	53	49	9
Infrastructure	9	33	32	6
Internet	2	1	1	5
EBITDA: Sectors posting negative surprises				
Automobiles	22	204	215	(5)
Pharmaceuticals	12	56	58	(4)
Metals & Mining	9	306	315	(3)
Consumer products	23	131	133	(1)
Telecom	4	95	95	(0)

	Companies	PAT (Rs bn)		Change
	(#)	Actual	Expected	(%)
PAT: Sectors posting positive surprises				
Banks/Financial Institutions	35	119	(11)	1,187
Cement	10	26	21	20
Energy	12	296	278	6
Technology	9	173	166	4
Others	16	25	24	4
PAT: Sectors posting negative surprises				
Automobiles	22	73	88	(17)
Telecom	4	(17)	(15)	(15)
Internet	2	1	1	(10)
Infrastructure	9	15	16	(9)
Metals & Mining	9	141	151	(7)

Source: Kotak Institutional Equities estimates

Exhibit 54 shows the movement in EBITDA margins across sectors over the past few quarters. We are reluctant to look at EBITDA margins for some sectors (cement, energy and metals & mining) and focus on absolute profitability (₹/ton or US\$/ton). Nonetheless, the exercise is useful to understand specific issues dogging some sectors. For example, EBITDA margin of the consumer products sector saw a 150 bps improvement in EBITDA margin reflecting (1) benefits of operating leverage and (2) benefits from GST in the form of savings on certain taxes on inputs that could not be offset against taxes on finished products in the previous regime.

Exhibit 54: Overall EBITDA margin expanded on a yoy basis
Comparison of EBITDA margin for KIE universe stocks (%)

	Jun-17	Sep-17	Dec-17	Mar-18	Jun-18A	Jun-18E
Automobiles	11.0	14.2	13.2	13.3	11.9	12.4
Cement	21.3	18.6	17.2	17.5	18.3	16.7
Consumer Products	21.8	22.5	22.4	22.9	23.3	23.2
Energy	10.2	13.7	14.5	12.5	13.3	11.2
Industrials	8.3	9.4	10.1	12.4	9.9	9.3
Infrastructure	32.0	34.0	33.2	32.3	32.9	31.0
Internet	24.9	30.6	29.6	23.8	30.1	28.8
Media	31.2	32.0	32.2	28.9	34.3	34.0
Metals & Mining	20.6	18.5	22.3	19.2	22.8	24.4
Others	15.3	14.7	14.3	11.9	12.8	12.9
Pharmaceuticals	17.3	20.3	20.0	18.5	18.6	19.5
Real Estate	30.8	32.8	30.0	14.6	26.0	16.6
Technology	22.4	23.4	23.4	23.5	23.1	23.0
Telecom	31.0	31.3	31.5	31.5	28.2	28.3
Utilities	41.0	43.7	40.9	38.4	41.3	41.2
KIE universe	16.3	18.0	18.3	16.8	17.4	16.7

Source: Kotak Institutional Equities estimates

1QFY19 RESULTS TAKEAWAYS: IMPROVING UNDERLYING TRENDS

Banks saw decent recovery in loan growth while corporate banks saw decline in slippages although provisioning remained high. Consumer staples reported strong volume growth off a low base. Passenger vehicles continued their steady growth trend, while commercial vehicles saw a sharp increase in volumes. Cement companies reported moderate volume growth but struggled to maintain profitability. Order booking for industrial companies was decent in a weak seasonal quarter suggesting moderate underlying demand.

Key takeaways from 1QFY19 results—some recovery and recipe for optimism

- ▶ Slippages decline for 'corporate' banks; business as usual for 'retail' banks. 'Corporate' banks reported a steep qoq decline in slippages in 1QFY19 as most of the standard stressed assets were classified as NPLs in 4QFY18 following the RBI's February 12, 2018 directive (see Exhibit 55). Also, banks had a few upgrades following resolution of two stressed accounts under NCLT-1 in 1QFY19; this also resulted in interest recognition on the resolved accounts and sequential improvement in NIMs. Most banks saw a modest decline in GNPLs this quarter. Banks such as AXSB, BOB, ICICIBC and SBI have largely recognized the bulk of their earlier standard stress loan book as GNPLs.

Exhibit 55: Large qoq decline in slippages for most banks under our coverage; modest decline in GNPLs
Trend in gross NPLs, net NPLs and slippages, 1QFY18-1QFY19

	Gross NPLs (%)					Net NPLs (%)					Slippages (%)				
	1QFY18	2QFY18	3QFY18	4QFY18	1QFY19	1QFY18	2QFY18	3QFY18	4QFY18	1QFY19	1QFY18	2QFY18	3QFY18	4QFY18	1QFY19
Public banks															
Bank of Baroda	11.4	11.2	11.3	12.3	12.5	5.2	5.1	5.0	5.5	5.4	5.4	3.7	5.8	12.6	4.0
Canara Bank	10.6	10.5	10.4	11.8	11.1	7.1	7.0	6.8	7.5	6.9	6.4	3.9	2.9	14.2	4.4
Punjab National Bank	13.7	13.3	12.1	18.4	18.3	8.7	8.4	7.6	11.2	10.6	6.3	3.5	3.1	27.4	6.8
State Bank of India	10.0	9.8	10.4	10.9	10.7	6.0	5.4	5.6	5.7	5.3	5.4	1.9	5.7	7.2	3.0
Union Bank	12.6	12.4	13.0	15.7	16.0	7.5	6.7	7.0	8.4	8.7	5.9	3.6	5.4	12.8	5.9
Old private banks															
City Union Bank	3.1	3.1	3.3	3.0	3.0	1.8	1.8	1.7	1.7	1.7	2.5	2.4	2.1	2.3	1.8
DCB Bank	1.7	1.8	1.9	1.8	1.9	0.9	0.9	0.9	0.7	0.7	2.2	1.9	2.4	1.8	1.7
Federal Bank	2.4	2.4	2.5	3.0	3.0	1.4	1.3	1.4	1.7	1.7	2.3	1.5	2.0	4.1	2.0
Karur Vysya Bank	4.3	4.8	5.9	6.6	7.4	2.9	3.2	3.9	4.2	4.5	3.8	4.0	6.4	5.6	6.8
J&K Bank	10.8	10.9	10.1	10.0	9.8	4.7	4.8	4.3	4.9	4.7	4.1	3.9	2.9	12.1	5.4
New private banks															
Axis Bank	5.0	5.9	5.3	6.8	6.5	2.3	3.1	2.6	3.4	3.1	3.8	9.3	4.3	15.7	3.9
HDFC Bank	1.2	1.3	1.3	1.3	1.3	0.4	0.4	0.4	0.4	0.4	—	—	—	—	—
ICICI Bank	8.0	7.9	7.8	8.8	8.8	4.9	4.4	4.2	4.8	4.2	4.3	4.0	3.6	12.5	3.2
IndusInd Bank	1.1	1.1	1.2	1.2	1.2	0.4	0.4	0.5	0.5	0.5	2.1	1.6	0.8	3.6	1.2
RBL Bank	1.5	1.4	1.6	1.4	1.4	0.8	0.8	1.0	0.8	0.8	2.1	1.2	2.5	1.2	1.5
Yes Bank	1.0	1.8	1.7	1.3	1.3	0.4	1.0	0.9	0.6	0.6	—	—	—	—	—
New private banks															
Equitas Holdings	4.9	5.8	5.0	2.7	2.8	2.4	2.8	1.6	1.4	1.5	—	—	—	—	—
Ujjivan Financial Services	6.2	5.0	4.2	3.6	2.7	2.3	1.4	1.0	0.7	0.3	—	—	—	—	—
Total	8.3	8.2	8.3	9.4	9.1	4.6	4.4	4.3	4.7	4.4					
Public banks	10.9	10.7	10.9	12.5	12.4	6.6	6.2	6.1	6.8	6.4					
Private banks	4.1	4.4	4.3	4.7	4.5	2.1	2.2	2.1	2.3	2.0					

Source: Companies, Kotak Institutional Equities

Exhibit 56 shows the provisions, pre-provision operating profits (PPOP) and the ratio of the two for the past five quarters for the banks under our coverage. Most banks reported healthy improvement in PPOP except ICICIBC and SBIN. At the same time, provisions remained at elevated levels for corporate banks; ICICIBC and SBIN reported losses as a result.

Exhibit 56: Significant increase in provisions over the past few quarters

Provisions, pre-provision operating profits and ratio of the two for banks in KIE coverage universe, 1QFY18-1QFY19

	Pre-provision operating profits (Rs bn)					Provisions (Rs bn)					Ratio (%)				
	1QFY18	2QFY18	3QFY18	4QFY18	1QFY19	1QFY18	2QFY18	3QFY18	4QFY18	1QFY19	1QFY18	2QFY18	3QFY18	4QFY18	1QFY19
Public banks															
Bank of Baroda	26	30	37	27	30	24	23	34	67	22	89	77	94	250	72
Canara Bank	25	25	28	18	29	22	22	27	91	26	89	87	94	514	88
Punjab National Bank	32	33	42	(4)	42	26	24	45	204	58	81	74	105	(4,549)	137
State Bank of India	119	200	118	159	120	89	191	189	281	192	75	96	161	177	161
Union Bank	21	18	10	8	21	17	36	33	57	22	81	200	341	737	108
Old private banks															
City Union Bank	3	3	3	3	3	1	1	1	1	1	39	40	29	29	26
DCB Bank	1	1	1	1	1	0	0	0	0	0	26	24	28	27	23
Federal Bank	6	6	6	6	6	2	2	2	4	2	42	30	29	63	33
Karur Vysya Bank	4	4	4	5	5	2	3	3	4	4	52	75	77	82	92
J&K Bank	4	4	4	3	3	5	2	3	3	3	140	67	65	94	73
New private banks															
Axis Bank	43	38	39	37	44	23	31	28	72	33	55	83	73	196	76
HDFC Bank	75	78	85	88	86	16	15	14	15	16	21	19	16	17	19
ICICI Bank	52	70	51	75	58	26	45	36	66	60	50	64	71	88	103
IndusInd Bank	16	16	17	18	18	3	3	2	3	4	20	18	14	19	19
Yes Bank	17	19	20	21	25	3	4	4	4	6	17	23	21	19	25

Source: Companies, Kotak Institutional Equities

Credit off-take continued to show signs of strong recovery, especially with private banks reporting very strong growth while PSU banks under our coverage saw decent recovery. Outstanding credit of banks as of June 30, 2018 to the industry sector is still flat on a yoy basis. However, strong loan growth in retail and trade financing has spurred the overall system growth (see Exhibit 57; we treat others as part of retail credit).

Exhibit 57: Modest revival in overall credit growth

Deployment of gross bank credit in major sectors (Rs bn)

	Jun-17	Jul-17	Aug-17	Sep-17	Oct-17	Nov-17	Dec-17	Jan-18	Feb-18	Mar-18	Apr-18	May-18	Jun-18	Proportion (%)	Growth yoy (%)
Food credit	511	456	482	398	412	356	238	473	347	338	326	527	624	1	22
Agriculture	9,719	9,743	9,777	9,971	9,810	9,882	9,981	10,068	10,168	10,302	10,269	10,279	10,355	13	7
Industry	26,185	26,280	26,112	26,404	25,991	26,041	26,341	26,151	26,272	26,993	26,511	26,446	26,417	34	1
- Textiles	1,927	1,933	1,932	1,954	1,935	1,949	2,007	2,047	2,054	2,099	2,051	2,038	2,033	3	5
- Chemical / Products	1,536	1,550	1,554	1,575	1,529	1,549	1,598	1,630	1,607	1,630	1,552	1,612	1,571	2	2
- Iron and Steel	3,213	3,241	3,246	3,225	3,223	3,223	3,223	3,207	3,210	3,262	3,222	3,093	3,005	4	(6)
- Engineering	1,463	1,474	1,460	1,508	1,507	1,503	1,514	1,505	1,511	1,553	1,512	1,514	1,526	2	4
- Gems & Jewelry	689	680	709	724	696	681	690	688	692	727	694	701	681	1	(1)
- Construction	849	816	811	834	839	855	862	871	857	901	897	902	911	1	7
- Infrastructure	8,915	8,884	8,859	8,949	8,839	8,796	8,898	8,767	8,816	8,909	8,878	8,839	8,912	12	(0)
- Power	5,203	5,247	5,217	5,262	5,161	5,121	5,200	5,153	5,172	5,196	5,188	5,142	5,140	7	(1)
- Telecom	827	830	820	871	846	844	854	798	821	846	864	864	883	1	7
- Roads	1,721	1,710	1,713	1,717	1,727	1,707	1,703	1,688	1,692	1,665	1,632	1,638	1,624	2	(6)
- Others	1,164	1,098	1,109	1,099	1,105	1,124	1,140	1,129	1,131	1,202	1,195	1,194	1,265	2	9
- Others	7,592	7,702	7,542	7,634	7,424	7,485	7,550	7,437	7,525	7,912	7,704	7,747	7,779	10	2
Trade	4,078	4,059	4,096	4,346	4,265	4,328	4,406	4,484	4,487	4,669	4,605	4,729	4,700	6	15
Retail loans	16,401	16,657	16,854	17,547	17,447	17,630	17,952	18,286	18,544	19,085	19,211	19,181	19,336	25	18
- Housing	8,619	8,636	8,906	9,086	9,035	9,221	9,362	9,466	9,556	9,746	9,855	9,919	9,983	13	16
- Vehicle loans	1,716	1,726	1,735	1,786	1,804	1,808	1,831	1,847	1,859	1,898	1,904	1,911	1,906	2	11
- Education loans	695	701	706	720	718	717	704	708	705	697	691	692	686	1	(1)
- Others	5,371	5,594	5,507	5,955	5,890	5,884	6,056	6,265	6,423	6,744	6,762	6,659	6,760	9	26
Others	12,315	12,258	12,278	13,402	13,071	13,265	13,713	13,547	13,919	15,835	15,207	15,203	15,518	20	26
- Transporters	1,102	1,107	1,103	1,126	1,123	1,145	1,152	1,172	1,189	1,213	1,214	1,218	1,223	2	11
- Professional/others	1,278	1,322	1,284	1,305	1,366	1,353	1,422	1,508	1,540	1,554	1,532	1,546	1,536	2	20
- Real Estate loans	1,771	1,774	1,761	1,863	1,829	1,819	1,825	1,841	1,802	1,858	1,849	1,840	1,863	2	5
- NBFCs	3,410	3,375	3,405	3,862	3,615	3,603	3,682	3,760	3,902	4,964	4,524	4,439	4,616	6	35
- Others	4,754	4,679	4,726	5,246	5,138	5,345	5,633	5,266	5,486	6,247	6,087	6,160	6,280	8	32
Total	69,209	69,452	69,599	72,068	70,996	71,501	72,631	73,009	73,737	77,223	76,130	76,365	76,949		11

Source: RBI, Kotak Institutional Equities

Exhibit 58 shows yoy credit growth for the banks under our coverage as well as total credit growth for the past few quarters. Most of the banks have reported high growth in disbursements with private banks reporting impressive growth this quarter backed by growth in retail advances.

Exhibit 58: Credit growth improved, especially in private banks as they continue to take market share from PSU banks
Yoy growth in loans for banks in KIE universe, 1QFY17-1QFY19 (%)

	1QFY17	2QFY17	3QFY17	4QFY17	1QFY18	2QFY18	3QFY18	4QFY18	1QFY19	2-y CAGR
Public banks										
Bank of Baroda	(11.2)	(14.6)	(8.9)	(0.1)	4.1	9.4	14.1	11.5	9.8	6.9
Canara Bank	(0.9)	1.3	(0.1)	5.3	6.7	9.5	12.5	11.6	12.7	9.6
Punjab National Bank	2.8	3.4	(1.8)	1.7	2.1	4.2	17.2	3.4	3.9	3.0
State Bank of India	10.7	7.2	4.1	7.3	0.5	0.9	1.1	(0.9)	10.3	15.1
Union Bank	5.1	9.6	5.5	8.6	9.9	11.3	13.5	4.0	7.9	8.9
Old private banks										
City Union Bank	18.5	16.0	12.5	12.1	13.4	15.6	19.7	16.9	17.3	15.3
DCB Bank	27.9	29.1	24.3	22.4	22.0	20.5	27.5	28.6	30.6	26.2
Federal Bank	19.3	27.2	32.0	26.2	29.1	24.7	22.0	25.4	23.6	26.3
Karur Vysya Bank	5.8	5.4	1.5	5.0	7.7	11.9	16.6	11.0	12.9	10.3
J&K Bank	12.9	4.0	(3.5)	(0.8)	(0.2)	8.0	28.5	14.2	22.8	10.7
New private banks										
Axis Bank	21.2	18.5	10.1	10.1	11.8	16.1	21.2	17.8	14.4	13.1
HDFC Bank	23.2	18.1	13.4	19.4	23.4	22.3	27.5	18.7	22.0	22.7
ICICI Bank	12.4	10.9	5.2	6.7	3.3	6.3	10.5	10.4	11.3	7.2
IndusInd Bank	29.7	26.4	25.1	27.9	24.3	24.5	25.1	28.2	29.4	26.8
Yes Bank	33.0	37.7	38.7	34.7	32.1	34.9	46.5	53.9	53.4	42.4
Public sector	4.2	2.8	1.1	5.4	2.5	4.0	6.8	2.7	9.5	
Private sector	19.6	17.3	12.3	14.6	15.1	17.0	22.3	19.6	20.5	
Total	9.5	7.9	5.1	8.7	6.8	8.5	12.2	8.6	13.6	

Notes:

(a) SBI numbers from 1QFY18 onwards are for the merged bank.

Source: Companies, Kotak Institutional Equities estimates

► **Consumer-facing businesses saw volume growth aided by weak base quarter.**

Most of the consumer staples and discretionary companies under our coverage reported healthy performance in 1QFY19 with strong volume growth across our coverage given the low base in 1QFY18 (de-stocking before GST introduction). However, the volume growth of most of the consumer companies, especially staples, is unimpressive when viewed on a 2-year CAGR basis, with most of them delivering low-single-digit CAGR in volumes.

Exhibit 59 shows the trends in volume growth for the major companies under our coverage over the past several quarters. Discretionary categories and stocks in certain discretionary segments showed strong momentum in 1QFY19 too. A few companies reported qoq contraction in gross margin owing to high RM cost; however, strict cost control and operating leverage helped most deliver margin expansion at EBITDA level in a few cases (see Exhibit 60). We note that yoy comparisons may not be strictly valid given that EBITDA margins were generally depressed in 1QFY18 due to negative operating leverage. Automobile volumes showed strong yoy growth across all segments in 1QFY19, accentuated by a weak base in case of 2-Ws. The PV segment continued its strong volume growth with MSIL reporting a 26% volume growth yoy and a two-year volume CAGR of 20% suggesting demand buoyancy in PVs. 2-W volumes optically delivered strong double-digit yoy growth in 1QFY19 but two-year volume CAGR is modest for HMCL (10%) and unimpressive for BJAUT (4%) suggesting the peaking effect of a low base in 1QFY18.

Exhibit 59: Consumer companies reported strong volume growth in 1QFY19 off a low base; 2-year CAGR is less impressive
Volume growth of consumer companies, 1QFY17-1QFY19 (%)

	1QFY17	2QFY17	3QFY17	4QFY17	1QFY18	2QFY18	3QFY18	4QFY18	1QFY19	2-y CAGR
Staples										
Bajaj Corp. - Almond Drop Hair Oil	2.2	1.6	1.6	(7.1)	(6.6)	6.5	4.5	6.9	11.2	1.9
Britannia Industries - Domestic	8.0	8.0	2.0	2.0	2.0	6.0	13.0	12.5	12.0	6.9
Colgate - Overall	6.0	4.0	4.0	(3.0)	(5.0)	(1.0)	12.0	4.0	4.0	(0.6)
Colgate - Toothpaste	5.0	4.0	4.0	(3.0)	(5.0)	(1.0)	12.0	4.0	4.0	(0.6)
Dabur - Domestic	4.1	4.5	4.5	2.4	(4.4)	7.2	13.0	7.7	21.0	7.6
GSK Consumer	0.0	(3.0)	(17.0)	(0.7)	(3.0)	2.4	17.0	8.0	12.8	4.6
GCPL - Soaps	10.0	(5.0)	(5.0)	5.0	(8.0)	12.0	15.0	12.0	12.0	1.5
HUL (FMCG business)	4.0	(1.0)	(1.0)	4.0	—	4.0	11.0	11.0	12.0	5.8
Marico - Domestic	8.0	3.4	3.4	10.0	(4.0)	8.5	9.4	1.0	12.4	3.9
Marico - Parachute	7.0	(6.0)	(6.0)	15.0	(5.0)	8.0	15.0	(5.0)	9.0	1.8
Marico - Saffola	11.0	8.0	8.0	6.0	(3.0)	9.0	—	(1.0)	10.0	3.3
Marico - Value-added hair oils	9.0	11.0	11.0	10.0	(6.0)	8.0	8.0	11.0	15.0	4.0
Discretionary										
Asian Paints	12.0	12.0	12.0	9.0	2.0	9.0	6.0	10.0	13.0	7.4
ITC - Cigarettes	3.0	4.0	4.0	—	2.0	(8.0)	(5.0)	(5.0)	1.0	1.5
Jubilant Foodworks - SSG	(3.2)	4.2	4.2	(7.5)	6.5	5.5	17.8	26.5	25.9	15.8
Pidilite - Domestic consumer business	9.0	7.8	7.8	6.0	—	15.0	23.0	13.0	20.0	9.5
Titan - Jewelry	6.0	(32.0)	(32.0)	37.0	49.0	49.0	6.0	6.0	(2.6)	20.5

Source: Companies, Kotak Institutional Equities

Exhibit 60: Gross and EBITDA margins expanded yoy for most consumer staple companies in 1QFY19
Gross and EBITDA margin of consumer companies under our coverage, 1QFY17-1QFY19

	Gross margin (%)									EBITDA margin (%)								
	1QFY17	2QFY17	3QFY17	4QFY17	1QFY18	2QFY18	3QFY18	4QFY18	1QFY19	1QFY17	2QFY17	3QFY17	4QFY17	1QFY18	2QFY18	3QFY18	4QFY18	1QFY19
Asian Paints	47.1	44.4	43.8	43.7	42.8	41.3	42.2	43.2	43.2	22.8	19.0	19.6	18.1	17.4	18.8	20.9	18.7	19.9
Bajaj Corp.	65.5	66.4	65.6	67.3	65.2	67.0	69.0	67.3	66.6	34.7	34.2	32.8	32.4	30.7	28.6	32.6	32.4	31.2
Britannia Industries	39.8	37.6	37.8	38.0	38.7	37.8	38.7	38.5	40.0	14.8	14.2	13.8	13.7	14.5	14.8	15.5	15.6	15.3
Colgate-Palmolive (India)	62.3	63.0	63.9	62.6	63.4	63.4	65.2	65.7	65.9	20.9	26.0	24.5	23.5	22.7	27.7	27.3	28.2	27.0
Dabur India	50.8	51.2	49.4	49.0	48.9	50.1	51.6	50.7	49.6	17.9	20.6	18.0	21.8	17.3	21.4	20.5	23.9	18.6
GlaxoSmithKline Consumer	70.7	66.0	67.8	65.9	65.2	64.7	69.0	68.3	69.6	21.6	22.7	19.5	19.8	16.9	23.4	20.0	21.2	20.8
Godrej Consumer Products	53.6	55.1	56.0	56.7	53.5	56.2	57.2	59.0	56.3	18.1	19.7	21.0	22.7	16.0	21.2	22.4	23.6	18.9
Hindustan Unilever	51.3	49.5	51.4	51.0	52.1	52.7	54.5	52.6	54.0	20.1	17.9	17.6	20.1	21.9	20.2	19.6	22.5	23.7
ITC	57.8	62.0	63.5	57.9	61.5	57.8	63.4	62.2	61.6	35.1	37.6	38.3	34.8	37.6	36.5	40.0	39.1	39.2
Jubilant Foodworks	76.8	74.8	74.9	76.9	76.4	74.1	74.5	74.3	74.5	9.5	9.7	9.7	9.9	11.7	14.1	17.2	16.4	16.6
Jyothy Laboratories	49.3	49.0	45.6	43.9	52.7	48.1	48.3	50.6	49.1	18.5	15.6	13.2	13.6	11.5	16.4	16.1	17.1	15.2
Marico	52.1	52.7	51.8	52.2	47.8	47.0	46.5	46.6	42.3	21.3	17.6	19.3	19.7	19.3	16.9	18.6	17.0	17.5
Nestle India	57.8	57.9	57.6	56.1	55.1	56.9	58.9	59.1	59.6	21.7	21.4	21.3	21.2	19.1	23.5	24.8	25.8	24.6
Page Industries	54.8	59.7	59.7	64.6	54.2	57.6	55.6	62.6	54.9	19.2	20.1	18.8	19.5	19.6	20.5	20.8	24.1	23.2
Pidilite Industries	52.3	53.5	53.2	53.1	51.5	53.0	53.4	52.1	50.5	25.1	22.7	21.5	19.9	21.1	24.6	24.0	18.4	20.8
Tata Global Beverages	45.2	48.1	46.4	50.4	46.6	45.5	46.4	44.3	45.6	13.7	11.7	10.6	10.7	14.3	12.6	13.6	8.6	13.8
Titan Company	28.6	31.1	23.1	26.7	25.4	27.0	25.8	29.0	26.9	10.4	10.4	9.6	7.8	9.7	13.1	10.5	11.6	11.5
United Breweries	54.9	54.2	53.8	51.3	52.5	54.1	52.4	52.7	54.1	18.6	11.7	12.5	9.1	19.0	17.4	12.7	14.1	21.5
United Spirits	43.4	42.0	42.0	44.2	46.0	47.6	47.4	48.8	49.1	10.5	10.0	12.0	12.9	9.6	16.3	12.0	12.6	11.3

Source: Companies, Kotak Institutional Equities

Exhibit 61 shows the quarterly volumes of various automobile segments. CV volumes saw strong growth in 1QFY19 with AL and TMT reporting 50% and 85% yoy volume growth and 15% 2-year volume CAGR each, indicating continued momentum in the underlying demand environment. Cement volumes showed decent increase based on the stocks under our coverage (see Exhibit 62), with most companies reporting moderate-to-strong growth. UTCEM reported 32% yoy growth in volumes and a two-year CAGR of 17%, which also reflects acquisition of JPA's capacities. We believe moderate recovery in housing demand, strong government support to affordable housing and pickup in infrastructure spending, especially roads, contributed to the strong underlying volume growth.

Exhibit 61: Impressive quarter for 4Ws and CVs on 2-year basis too
Domestic volumes of select companies in auto sector, 1QFY17-1QFY19

	1QFY17	2QFY17	3QFY17	4QFY17	1QFY18	2QFY18	3QFY18	4QFY18	1QFY19	2-y CAGR (%)
Domestic sales volumes (units)										
Ashok Leyland	28,939	30,096	29,770	44,459	25,435	36,216	41,930	55,230	38,119	
Bajaj Auto										
Two wheelers	548,880	579,545	459,427	413,539	426,562	583,997	466,531	497,875	594,234	
Three wheelers	75,204	74,383	53,602	49,958	52,347	84,938	110,123	122,229	94,431	
Eicher Motors										
Two wheelers	143,329	163,821	170,538	173,419	178,882	199,422	201,157	221,741	219,725	
Commercial vehicles	13,602	11,262	9,610	15,034	9,913	13,296	13,570	19,773	14,153	
Hero Motocorp	1,706,444	1,776,381	1,430,569	1,570,261	1,811,343	1,976,270	1,665,489	1,929,616	2,060,342	
Maruti Suzuki	322,340	383,030	356,503	382,668	368,431	457,401	400,586	427,082	463,840	
M&M (passenger vehicles)	59,360	56,139	54,652	66,053	55,785	65,614	55,476	72,630	60,779	
Tata Motors										
Commercial vehicles	73,254	70,529	72,192	89,645	60,446	90,258	102,742	123,010	111,642	
Passenger vehicles	36,659	46,687	43,387	45,771	39,713	52,388	53,235	64,864	52,937	
Yoy change (%)										
Ashok Leyland	16.8	(12.5)	7.4	9.9	(12.1)	20.3	40.8	24.2	49.9	15
Bajaj Auto										
Two wheelers	13.0	23.5	(3.3)	(11.8)	(22.3)	0.8	1.5	20.4	39.3	4
Three wheelers	48.3	10.8	(18.8)	(29.8)	(30.4)	14.2	105.4	144.7	80.4	12
Eicher Motors										
Two wheelers	37.4	30.8	37.0	19.8	24.8	21.7	18.0	27.9	22.8	24
Commercial vehicles	27.7	18.4	(8.3)	10.4	(27.1)	18.1	41.2	31.5	42.8	2
Hero Motocorp	6.6	17.2	(12.7)	(5.8)	6.1	11.3	16.4	22.9	13.7	10
Maruti Suzuki	5.4	18.5	3.9	14.8	14.3	19.4	12.4	11.6	25.9	20
Mahindra & Mahindra	13.4	16.4	(11.7)	(9.1)	(6.0)	16.9	1.5	10.0	9.0	1
Tata Motors										
Commercial vehicles	11.2	(2.6)	(2.3)	(2.8)	(17.5)	28.0	42.3	37.2	84.7	15
Passenger vehicles	(1.2)	19.7	20.8	22.4	8.3	12.2	22.7	41.7	33.3	32

Source: SIAM, Kotak Institutional Equities

Exhibit 62: Cement volumes increased substantially yoy; 2-year volume CAGR adjusted for UTCEM's acquisition of JPA is more moderate
Volume trends for cement companies under KIE coverage, 1QFY17-1QFY19

	1QFY17	2QFY17	3QFY17	4QFY17	1QFY18	2QFY18	3QFY18	4QFY18	1QFY19	2-y CAGR (%)
Yoy volume growth (%)										
ACC	(1)	(10)	(9)	4	10	18	27	8	7	8
Ambuja Cements	(2)	(7)	—	3	5	12	2	3	5	5
Dalmia Bharat	22	20	20	17	6	6	17	14	13	10
India Cements	10	11	40	18	15	13	1	6	16	15
JK Cement	1	4	(6)	(15)	15	12	22	29	23	19
JK Lakshmi Cement	27	(1)	4	6	8	10	15	2	1	4
Orient Cement	43	16	19	25	0	11	9	(3)	14	7
Shree Cement	19	9	5	11	14	7	8	9	19	16
UltraTech Cement	7	(1)	(2)	0	(1)	18	37	32	39	17
Total volume growth (%)	8.4	1.3	2.5	5.3	6.1	13.2	19.7	15.1	19.3	12.5
Volumes (mn tons)										
ACC	6.1	5.1	5.5	6.6	6.7	6.0	6.9	7.1	7.2	
Ambuja Cements	5.8	4.5	5.5	6.0	6.1	5.0	5.6	6.2	6.4	
Dalmia Bharat	3.8	3.4	3.5	4.6	4.0	3.6	4.2	5.2	4.5	
India Cements	2.3	2.4	2.7	2.9	2.7	2.7	2.7	3.1	3.1	
JK Cement	1.6	1.6	1.7	1.9	1.9	1.8	2.0	2.4	2.3	
JK Lakshmi Cement	2.1	1.7	1.8	2.3	2.3	1.9	2.1	2.3	2.3	
Orient Cement	1.4	1.2	1.3	1.7	1.4	1.3	1.4	1.7	1.6	
Shree Cement	5.2	4.6	4.9	5.9	5.9	4.9	5.3	6.4	7.0	
UltraTech Cement	12.7	10.6	11.0	13.4	12.6	12.4	15.1	17.6	17.5	
Total	41.0	35.1	37.8	45.2	43.5	39.7	45.3	52.1	51.9	

Notes:

(a) 2QFY18 and 3QFY18 yoy growth numbers are not comparable for ICEM and UTCEM as it include volumes of merged/acquired assets.

Source: Companies, Kotak Institutional Equities

However, the profitability of cement stocks under our coverage was quite erratic with ACC and ACEM reporting marked improvement in EBITDA/ton sequentially while SRCM, UTCM and the smaller cement companies reporting deterioration in the same metric. Exhibit 63 shows realizations and profitability of the cement stocks under our coverage for the past few quarters.

Exhibit 63: Profitability declined for most companies (except ACC and Ambuja)

Realizations, power & fuel costs and EBITDA for cement companies, 1QFY17-1QFY19 (Rs/ton)

	1QFY17	2QFY17	3QFY17	4QFY17	1QFY18	2QFY18	3QFY18	4QFY18	1QFY19
ACC									
Realization (Rs/ton)	4,341	4,462	4,477	4,348	4,597	4,733	4,569	4,626	4,836
Fuel & power cost (Rs/ton)	853	1,058	975	981	1,016	1,130	1,024	1,410	1,037
EBITDA (Rs/ton)	662	426	309	483	711	557	473	550	713
Ambuja									
Realization (Rs/ton)	4,412	4,454	4,393	4,208	4,667	4,621	4,565	4,602	4,736
Fuel & power cost (Rs/ton)	812	972	831	895	933	968	1,098	1,021	1,028
EBITDA (Rs/ton)	1,009	613	589	606	1,013	706	865	815	977
Dalmia Bharat									
Realization (Rs/ton)	4,695	4,921	4,845	4,513	5,160	5,038	5,037	5,093	5,250
Fuel & power cost (Rs/ton)	537	662	689	695	809	836	823	757	876
EBITDA (Rs/ton)	1,320	1,141	1,142	1,206	1,395	1,213	1,095	1,137	1,162
India Cement									
Realization (Rs/ton)	4,521	4,721	4,581	4,546	4,807	4,650	4,420	4,528	4,425
Fuel & power cost (Rs/ton)	875	864	1,007	1,105	1,076	1,101	1,124	1,131	1,302
EBITDA (Rs/ton)	857	894	739	707	696	664	595	514	508
JK Cement									
Realization (Rs/ton)	4,703	4,743	4,601	4,736	4,953	5,166	4,847	4,838	4,820
Fuel & power cost (Rs/ton)	736	790	802	837	858	960	948	1,041	2,465
EBITDA (Rs/ton)	879	761	768	843	940	966	733	669	658
JK Lakshmi Cement									
Realization (Rs/ton)	3,684	3,765	3,665	3,574	3,944	4,055	3,978	3,896	4,038
Fuel & power cost (Rs/ton)	622	669	825	745	840	937	974	953	940
EBITDA (Rs/ton)	557	538	452	317	527	498	448	440	410
Shree Cement									
Realization (Rs/ton)	3,906	3,969	3,697	3,771	4,146	4,170	4,120	4,157	4,107
Fuel & power cost (Rs/ton)	634	782	609	776	777	844	949	939	1,012
EBITDA (Rs/ton)	1,287	1,352	989	856	1,167	1,094	1,041	962	722
UltraTech									
Realization (Rs/ton)	4,864	5,117	5,032	4,940	5,263	5,295	5,032	5,103	4,946
Fuel & power cost (Rs/ton)	727	834	880	865	967	1,076	1,001	1,076	1,067
EBITDA (Rs/ton)	1,080	1,037	949	957	1,239	1,089	841	965	928

Source: Companies, Kotak Institutional Equities

- ▶ **Decent execution and order inflows print for industrials.** Domestic revenues of the industrial companies under our coverage increased 11% yoy in 1QFY19 (see Exhibit 64). At the same time, order inflows increased 24% yoy, mainly led by BHEL and L&T (see Exhibit 65). In particular, L&T reported a 27% growth and 19.3% CAGR on 2-year basis in order inflows in 1QFY19, which is a healthy sign regarding domestic investment, given L&T's wide presence across infrastructure segments. While ordering in L&T was mainly led by heavy engineering, hydrocarbon and infrastructure segments, the same for BHEL was driven by FGD, power and railways.

Exhibit 64: Moderately strong domestic revenues for industrial companies in 1QFY19

Domestic revenues of industrials companies under KIE coverage, 1QFY17-1QFY19

	Domestic revenues (Rs bn)									yoy growth (%)								
	1QFY17	2QFY17	3QFY17	4QFY17	1QFY18	2QFY18	3QFY18	4QFY18	1QFY19	1QFY17	2QFY17	3QFY17	4QFY17	1QFY18	2QFY18	3QFY18	4QFY18	1QFY19
ABB	18	17	21	18	18	16	24	21	23	(6)	1	(2)	7	2	(10)	13	12	28
BHEL	55	64	61	92	53	59	62	91	54	34	15	19	(3)	(3)	(7)	2	(1)	2
Cummins	8	8	9	8	9	7	9	8	9	4	11	17	18	10	(7)	3	(4)	(4)
Larsen & Toubro	107	127	133	218	122	132	148	246	139	(0)	2	(1)	10	14	4	11	13	13
Siemens	22	26	19	25	23	27	21	28	26	(6)	(15)	(8)	(3)	4	4	6	12	16
Thermax	6	7	6	10	5	6	7	9	6	(13)	(6)	(21)	25	(15)	(14)	19	(7)	12
Total	216	249	249	371	230	247	270	403	256	5	3	2	6	7	(1)	8	9	11

Notes:

(a) We have used historical share of exports to estimate domestic revenues of ABB, BHEL, Siemens and Thermax.

Source: Companies, Kotak Institutional Equities

Exhibit 65: Strong order inflows for industrial companies

Order inflows of key industrials and construction companies, 1QFY17-1QFY19 (Rs bn)

	Order inflows (Rs bn)									yoy growth (%)								
	1QFY17	2QFY17	3QFY17	4QFY17	1QFY18	2QFY18	3QFY18	4QFY18	1QFY19	1QFY17	2QFY17	3QFY17	4QFY17	1QFY18	2QFY18	3QFY18	4QFY18	1QFY19
ABB	20	30	56	23	23	19	29	26	25	8	29	173	28	13	(35)	(48)	10	8
BHEL	32	21	16	166	18	19	121	252	37	(84)	(12)	(74)	6	(45)	(10)	651	52	110
Larsen & Toubro	135	195	194	289	151	144	353	363	192	(9)	35	(14)	16	12	(26)	82	26	27
Siemens	32	25	32	47	28	27	33	29	28	44	10	(6)	61	(12)	10	1	(38)	(0)
Thermax	5	5	7	7	5	7	8	9	9	(41)	(32)	(20)	(28)	4	26	9	16	58
Voltas	11	4	7	10	12	7	6	12	4	81	139	4	(1)	15	75	(9)	29	(66)
Total	203	255	280	495	238	223	549	691	295	(46)	27	(14)	11	17	(13)	96	40	24

Notes:

(a) We have used domestic order inflows for L&T, for the rest of the companies, we have used total order inflows.

Source: Companies, Kotak Institutional Equities

However, the market has already priced in a strong recovery in revenues and profits as can be seen in the high valuations of certain industrial stocks (see Exhibit 66). While we model a sharp recovery in revenues and profits in FY2019 and FY2020 with estimated net profit growth of 22% and 20%, respectively, valuations are still quite stiff even if our estimates materialize. We do not rule out downside risks to our earnings estimates, especially if (1) public capex was to see a sudden slowdown given possible fiscal challenges and (2) private investment was to get deferred on higher macro and potential political uncertainty.

Exhibit 66: Valuation of industrial stocks are quite stiff even after factoring a significant recovery in their earnings

Valuation summary of industrials stocks under KIE coverage, March fiscal year-ends, 2018-20E

Company	EPS (Rs)			EPS growth (%)			P/E (X)			EV/EBITDA (X)			P/B (X)		
	2018	2019E	2020E	2018	2019E	2020E	2018	2019E	2020E	2018	2019E	2020E	2018	2019E	2020E
ABB	19.8	25.8	29.4	12	30	14	61	47	41	34	27	25	7.1	6.5	5.9
BHEL	2.2	2.6	5.0	63	16	95	33	28	14	8	7	4	0.8	0.8	0.8
Cummins India	24.2	27.8	32.7	(8)	15	18	28	24	21	24	20	17	4.7	4.4	4.1
Kalpitaru Power Transmission	18.3	23.0	32.1	51	26	39	20	16	11	8	7	5	2.1	1.9	1.6
KEC International	17.9	20.9	27.2	51	17	30	17	14	11	9	8	7	3.9	3.1	2.5
L&T	51.7	63.0	69.8	22	22	11	24	20	18	20	16	15	3.5	3.2	2.9
Siemens	23.9	29.1	35.4	21	21	22	42	35	28	24	20	16	4.4	4.1	3.9
Thermax	20.6	27.8	38.7	(4)	35	39	50	37	27	31	24	18	4.3	4.0	3.7
Voltas	17.3	17.4	20.6	11	0	19	35	35	30	30	26	22	5.2	4.7	4.2

Source: Companies, Kotak Institutional Equities estimates

- **Modest recovery in topline of pharmaceutical companies.** Most pharmaceutical companies barring LPC reported modest growth in US revenues on a yoy basis (flattish on 2-year CAGR basis). Revenues of the six pharmaceutical companies under our coverage with a large US presence saw 11% growth on a yoy basis (see Exhibit 67).

While US sales of DRRD were up 7% yoy (2% 2-year CAGR) and that of Cipla were up 4% yoy (1% 2-year CAGR), LPC reported a meltdown in its US business, reporting 23% yoy decline in sales. SUNP meanwhile reported a 13% yoy growth in its US sales, although it is still down 21% on a 2-year basis.

Exhibit 67: Pharmaceutical companies saw some stabilization in their US businesses
Trend of quarterly sales of Indian pharmaceuticals across geographies, 1QFY18-1QFY19 (Rs mn)

	Sales (Rs mn)								yoy growth (%)				2-y CAGR (%)		
	1QFY17	2QFY17	3QFY17	4QFY17	1QFY18	2QFY18	3QFY18	4QFY18	1QFY18	2QFY18	3QFY18	4QFY18		1QFY19	
Aurobindo															
Total sales	37,259	37,755	39,062	36,416	36,788	44,359	43,361	40,491	42,503	(1)	17	11	11	16	7
ARV	3,030	2,785	3,419	2,619	2,446	2,075	2,389	1,486	1,468	(19)	(25)	(30)	(43)	(40)	(30)
Europe	8,312	8,134	8,554	7,772	9,176	11,135	11,716	11,516	10,094	10	37	37	48	10	10
RoW	1,940	1,768	1,878	1,971	1,939	2,434	2,502	2,096	2,230	(0)	38	33	6	15	7
US	17,039	17,351	17,451	16,432	16,964	20,989	19,096	17,388	19,799	(0)	21	9	6	17	8
Others	6,938	7,717	7,760	7,622	6,263	7,726	7,658	8,005	8,912	(10)	0	(1)	5	42	13
Cipla															
Total sales	36,500	37,511	36,472	35,820	35,251	40,824	39,138	36,980	39,390	(3)	9	7	3	12	4
Europe	1,400	1,340	1,260	1,800	1,580	1,477	1,710	1,360	1,340	13	10	36	(24)	(15)	(2)
India	14,490	14,690	14,080	11,970	12,710	16,460	16,010	13,530	15,440	(12)	12	14	13	21	3
RoW	3,600	4,087	3,135	3,297	3,836	4,558	3,710	3,940	4,690	7	12	18	20	22	14
South Africa	4,030	4,623	4,950	4,680	4,880	5,265	5,200	5,330	5,750	21	14	5	14	18	19
US	6,570	6,633	6,620	6,460	6,460	6,180	6,500	6,750	6,700	(2)	(7)	(2)	4	4	1
Others	6,410	6,138	6,428	7,613	5,784	6,884	6,008	6,070	5,470	(10)	12	(7)	(20)	(5)	(8)
Dr Reddy's Laboratories															
Total sales	33,188	35,923	37,076	34,763	33,159	35,352	38,060	35,349	36,388	(0)	(2)	3	2	10	5
CIS	700	900	1,000	1,100	900	900	1,000	1,100	1,000	29	—	—	—	11	20
Europe	1,615	1,776	2,148	2,066	2,075	2,424	2,006	1,711	2,283	28	36	(7)	(17)	10	19
India	5,233	6,251	5,947	5,711	4,687	6,370	6,126	6,138	5,390	(10)	2	3	7	15	1
RoW	1,300	1,300	1,848	1,564	1,347	1,406	1,500	1,900	1,549	4	8	(19)	21	15	9
Russia	2,300	2,700	3,100	3,400	3,500	3,200	3,400	2,500	3,800	52	19	10	(26)	9	29
US	15,523	16,134	16,595	15,349	14,946	14,318	16,073	14,487	15,995	(4)	(11)	(3)	(6)	7	2
Others	24,355	6,862	6,438	5,573	5,704	6,734	7,955	7,513	6,371	(77)	(2)	24	35	12	(49)
Lupin															
Total sales	43,136	42,112	44,049	41,619	38,068	38,742	39,004	39,785	37,746	(12)	(8)	(11)	(4)	(1)	(6)
Europe	1,185	1,347	1,520	1,420	1,256	1,514	1,359	1,808	1,416	6	12	(11)	27	13	9
India	9,499	9,958	9,912	8,788	9,324	11,593	10,688	9,647	11,924	(2)	16	8	10	28	12
Japan	4,232	4,368	4,492	4,619	4,979	4,957	5,729	5,098	5,032	18	13	28	10	1	9
US	21,775	19,978	21,488	18,216	15,351	13,659	14,500	14,990	11,858	(30)	(32)	(33)	(18)	(23)	(26)
Others	6,444	6,461	6,637	8,577	7,158	7,018	6,727	8,242	7,516	11	9	1	(4)	5	8
Sun Pharma															
Total sales	82,450	82,651	79,222	71,370	62,088	66,503	66,532	69,771	72,242	(25)	(20)	(16)	(2)	16	(6)
EM	10,311	11,305	11,599	12,308	10,828	12,740	12,285	12,794	13,065	5	13	6	4	21	13
India	18,543	20,090	19,694	19,164	17,610	22,210	20,850	19,626	21,520	(5)	11	6	2	22	8
RoW	5,625	5,254	7,603	7,412	7,412	7,215	7,800	7,435	7,169	32	37	3	0	(3)	13
US	40,706	36,908	34,193	25,781	22,622	19,838	21,254	23,716	25,460	(44)	(46)	(38)	(8)	13	(21)
Others	7,265	9,095	6,135	6,705	3,617	4,501	4,343	6,200	5,028	(50)	(51)	(29)	(8)	39	(17)

Source: Companies, Kotak Institutional Equities

AUGUST 16, 2018

RESULT

Coverage view: **Neutral**

Price (₹): **602**

Target price (₹): **520**

BSE-30: **37,852**

Operationally in line. SUNP's 1QFY19 revenues were in line with estimates; even as EBITDA and PAT were higher than estimates, adjusting for lower R&D, both were in line with estimates, with R&D likely to scale up from 2QFY19. This will also be accompanied by spends to build out the specialty franchise within FY2019/20, though Ilumya's initial ramp-up could likely disappoint given the deteriorating competitive landscape and a weak efficacy profile. **REDUCE** with revised TP of ₹520/share.

Company data and valuation summary

Sun Pharmaceuticals

Stock data

52-week range (Rs) (high,low)	610-433
Market Cap. (Rs bn)	1,443.9

Shareholding pattern (%)

Promoters	54.4
FIs	16.3
MFs	8.1

Price performance (%)

	1M	3M	12M
Absolute	7.5	27.0	27.6
Rel. to BSE-30	3.8	19.3	6.0

Forecasts/Valuations

	2018	2019E	2020E
EPS (Rs)	15.2	16.8	24.0
EPS growth (%)	(47.5)	11.1	42.5
P/E (X)	39.7	35.7	25.1
Sales (Rs bn)	264.9	304.2	348.0
Net profits (Rs bn)	36.5	40.5	57.8
EBITDA (Rs bn)	56.1	66.5	87.7
EV/EBITDA (X)	23.6	19.4	14.2
ROE (%)	9.8	10.2	13.1
Div. Yield (%)	0.3	0.6	0.8

Operationally in-line quarter; lower R&D largely a timing issue

SUNP's 1QFY19 revenues were largely in line with our estimates (+1.8% vs KIE). Domestic formulations revenues grew by 22% yoy (+1% vs KIE), and US was US\$10 mn lower than our estimates with the miss largely driven by Taro (-US\$15 mn vs KIE), while ex-Taro business was largely in line, given the authorized generic launch of Welchol. RoW grew by 11% yoy, 2% ahead of estimates. However, API revenues grew by 28% yoy, 23% higher than our estimates. Gross margins at 70.8% were 70 bps lower than our estimate, presumably driven by higher sales of authorized generic version of Welchol (low-margin business), with some improvement in base business post Halol clearance, though the management guided to Halol approvals getting staggered through 1HFY20. SG&A and staff costs were largely in line with estimates, though R&D at ₹4.8 bn was 16% lower than estimates; the management reaffirmed its full-year R&D guidance of 8-9% of sales (vs 6.7% in 1QFY19). Given the lower R&D, EBITDA was higher by 5.7%, with EBITDA margins at 22.2% (+80 bps vs KIE). Depreciation was lower by ₹550 mn qoq, thereby resulting in PAT exceeding estimates by 11%, though adjusting for the lower R&D, PAT was in line with estimates.

A lot hinges on specialty rollout

Given the continued pressures in the US generics segment, SUNP's FY2019-21 growth is contingent on the success of specialty franchise, with the market having high hopes on the three specialty products (Odomzo, Ilumya and Cequa). Odomzo market share gains have already disappointed initial expectations. We believe Ilumya's initial ramp-up could also disappoint, as we remain unconvinced of the efficacy profile versus both IL-17's and IL-23's (to some extent even Humira, though it stacks strongly against TNF's on safety). We expect Ilumya to trail both guselkumab and risankizumab, which we believe will likely emerge as the IL-23 class leader by a margin. Given the intensifying competition and increasing reimbursement hurdles, there are now signs of heavy rebating by existing players. In such a scenario, SUNP will also need to rebate and promote Ilumya aggressively to gain a meaningful share.

Rewarding for optionality, though not adjusting for risk—REDUCE

We cut our FY2019-21 EPS by 2-3%. After factoring in a full ramp-up for the specialty products by FY2020/21, SUNP is now trading at 24.4X FY2020E EPS and 20X FY2021E EPS, with FY2022E likely to see a cliff year for several of its specialty products (Topicort spray, Absorica, Yonsa, BromSite). **REDUCE** with a target price of ₹520/share (from ₹500/share), as we roll over to June 2020E.

Chirag Talati, CFA

Kumar Gaurav

Exhibit 1: Sun Pharma – consolidated interim results
March fiscal year-ends (Rs mn)

	1QFY19	1QFY19E	1QFY18	4QFY18	(% chg.)			yoy		
					1QFY19E	1QFY18	4QFY18	FY2019E	FY2018	(% chg.)
Sales	72,242	70,963	62,088	69,771	1.8	16.4	3.5	304,152	264,895	14.8
Gross profit	51,173	51,448	45,314	52,070	(0.5)	12.9	(1.7)	218,294	190,648	14.5
Staff costs	(14,330)	(14,170)	(13,299)	(13,413)	1.1	7.8	6.8	(59,038)	(53,671)	10.0
R&D	(4,849)	(5,750)	(5,015)	(6,155)	(15.7)	(3.3)	(21.2)	(25,482)	(20,669)	23.3
SG&A	(15,927)	(16,321)	(16,045)	(15,668)	(2.4)	(0.7)	1.7	(67,235)	(60,227)	11.6
EBITDA	16,067	15,206	10,957	16,835	5.7	46.6	(4.6)	66,539	56,081	18.6
Depreciation	(4,016)	(4,600)	(3,466)	(4,552)	(12.7)	15.9	(11.8)	(16,822)	(14,998)	12.2
Interest expense	(1,309)	(1,500)	(1,094)	(1,554)	(12.7)	19.6	(15.8)	(5,363)	(5,176)	
Other income	1,998	2,500	1,520	3,028	(20.1)	31.4	(34.0)	8,412	8,388	
Exceptionals	0	0	(9,505)	0				0	0	
Pretax profits	12,739	11,606	(1,589)	13,523	9.8	(901.6)	(5.8)	52,766	34,535	52.8
Tax	(1,639)	(1,857)	(1,618)	1,767	(11.8)	1.3	(192.7)	(8,651)	(8,452)	2.4
Minority interest	(1,275)	(870)	(1,042)	(2,200)	46.6	22.4	(42.0)	(3,574)	(4,468)	
Net income	9,825	8,879	(4,249)	13,090	10.7	(331.2)	(24.9)	40,541	21,616	87.6
Net income (adjusted)	9,825	8,879	5,256	10,504	10.7	86.9	(6.5)	40,541	33,665	20.4
EPS (Rs)	4.1	3.7	(1.8)	5.4	10.7	(331.2)	(24.9)	16.8	9.0	87.6
EPS adjusted (Rs)	4.1	3.7	2.2	4.4	10.7	86.9	(6.5)	16.8	14.0	20.4
Tax rate (%)	12.9	16.0	(101.8)	(13.1)				16.4	24.5	
Divisional sales										
US (US \$ mn)	380	390	351	368	(2.6)	8.3	3.3	1,593	1,354	17.6
- Taro US	135	150	141	155	(10.3)	(4.7)	(13.3)	532	545	
- Ex-Taro US	245	240	210	213	2.2	17.0	15.3	1,061	809	
Domestic formulations (Rs. mn)	21,520	21,196	17,610	19,626	1.5	22.2	9.6	89,939	80,293	12.0
RoW (Rs mn)	20,240	19,841	18,239	20,231	2.0	11.0	0.0	87,094	78,132	11.5
API	3,940	3,200	3,089	3,324	23.1	27.5	18.5	13,714	13,993	(2.0)
% margin										
Gross margin	71	72	73	75				72	72	
R&D	6.7	8.1	8.1	8.8				8.4	7.8	
SG&A	41.9	43.0	47.3	41.7				41.5	43.0	
EBITDA	22.2	21.4	17.6	24.1				21.9	21.2	

Source: Company, Kotak Institutional Equities estimates

Exhibit 2: Taro – interim results
March fiscal year-ends (US\$ mn)

	1QFY19	1QFY19E	1QFY18	4QFY18	(% chg.)			yoy		
					1QFY19E	1QFY18	4QFY18	FY2019E	FY2018	(% chg.)
Sales	155	170	161	175	(9.0)	(4.2)	(11.8)	631	662	(4.7)
Total expenditure	(96)	(96)	(84)	(100)	0.0	14.7	(4.4)	(390)	(96)	306.6
Cost of sales	(55)	(56)	(45)	(56)	(2.8)	21.8	(3.1)	(218)	(198)	9.7
R&D	(13)	(18)	(15)	(20)	(25.9)	(9.0)	(34.3)	(80)	(70)	13.6
SG&A	(19)	(20)	(24)	(24)	(4.7)	(20.5)	(18.9)	(93)	(72)	29.2
Depreciation	(4)	(4)	(4)	(4)	13.9	13.9	(3.9)	(19)	(16)	17.4
EBITDA	67	76	81	79	(10.9)	(17.1)	(15.0)	260	321	(19.1)
Interest income	8	6	4	6				20	20	
Forex expense/(income)	10	0	(20)	16				0	(32)	
Other income	1	2	2	0				1	2	
Settlement expense	0	0	0	(0)				0	(2)	
Pretax profits	82	80	65	97	1.9	26.2	(16.1)	261	292	(10.6)
Tax	(14)	(12)	(10)	(11)				(52)	(82)	
Net income	67	68	55	87	(0.9)	23.5	(22.1)	209	210	(0.6)
EPS (US\$)	1.6	1.7	1.2	1.9	(0.9)	34.9	(14.9)	4.7	5.1	(9.0)
Tax rate (%)	(17.3)	(15.0)	(15.5)	(11.0)				(20.0)	(28.0)	
% margin										
Cost of sales	(35.3)	(33.0)	(27.8)	(32.1)				(34.5)	(30.0)	
R&D	(8.6)	(10.6)	(9.1)	(11.6)				(12.7)	(10.6)	
SG&A	(12.5)	(11.9)	(15.0)	(13.6)				(14.7)	(10.8)	
EBITDA	43.6	44.5	50.5	45.3				41.2	48.6	

Source: Company, Kotak Institutional Equities estimates

Exhibit 3: Changes in estimates

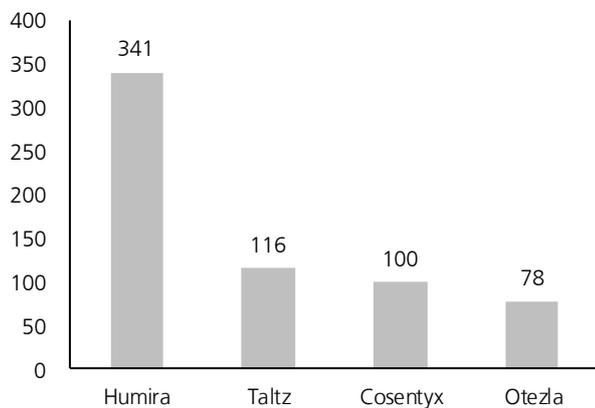
March fiscal year-ends (Rs mn)

	New estimates			Old estimates			Changes %		
	2019E	2020E	2021E	2019E	2020E	2021E	2019E	2020E	2021E
Sales	304,152	347,990	378,992	299,642	341,455	376,530	1.5	1.9	0.7
Gross profits	218,294	252,144	275,669	219,964	249,754	276,116	(0.8)	1.0	(0.2)
EBITDA	66,539	87,731	100,364	66,559	87,026	101,420	(0.0)	0.8	(1.0)
PBT	52,766	74,984	89,549	53,487	75,357	91,983	(1.3)	(0.5)	(2.6)
Tax	(8,651)	(13,840)	(17,157)	(8,808)	(13,909)	(17,628)	(1.8)	(0.5)	(2.7)
Adjusted PAT	40,541	57,790	69,653	40,898	58,073	71,440	(0.9)	(0.5)	(2.5)
Adjusted EPS (Rs)	16.8	24.0	28.9	17.1	24.3	29.8	(1.5)	(1.2)	(2.9)

Source: Kotak Institutional Equities estimates

Exhibit 4: Significant DTC spends required to penetrate the crowded psoriasis market

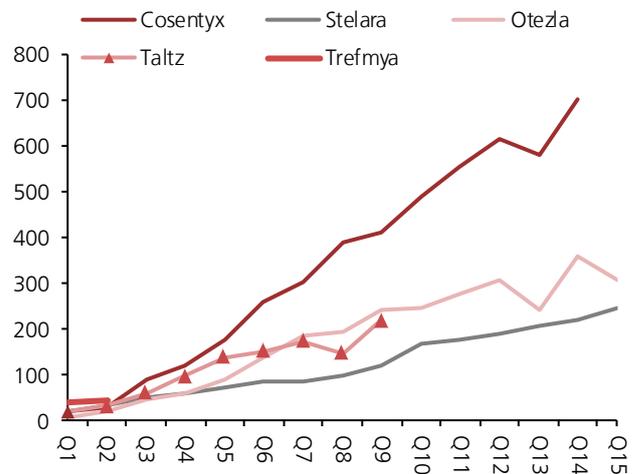
DTC spend, calendar year-end, 2017 (US\$ mn)



Source: Industry data, Kotak Institutional Equities estimates

Exhibit 5: Despite stronger label, Taltz has failed to replicate Cosentyx' launch success

Quarters after launch (US\$ mn)



Source: Industry data, Kotak Institutional Equities estimates

Exhibit 6: SUNP ANDA filing trend

1QFY16 – 1QFY19, March fiscal year-ends

	1QFY16	2QFY16	3QFY16	4QFY16	1QFY17	2QFY17	3QFY17	4QFY17	1QFY18	2QFY18	3QFY18	4QFY18	1QFY19
Approvals													
ANDA approvals - during the period	4	4	1	5	7	6	1	4	5	3	5	5	6
Cumulative ANDA approvals	442	445	435	440	417	423	424	428	433	422	418	422	428
Filings													
ANDA filed - during the period	6	6	5	11	1	3	8	14	8	4	4	19	3
Cumulative ANDA's filed	592	598	603	614	615	618	626	640	648	652	656	675	678
Pending													
ANDA -pending approval	154	154	156	159	150	144	149	157	151	136	126	139	135
- of which tentative approvals	12	12	10	13	15	13	14	16	16	16	14	14	15

Source: Company, Kotak Institutional Equities

Exhibit 7: Taro ANDA filing trend

1QFY16 – 1QFY19, March fiscal year-ends

	1QFY16	2QFY16	3QFY16	4QFY16	1QFY17	2QFY17	3QFY17	4QFY17	1QFY18	2QFY18	3QFY18	4QFY18	1QFY19
Approvals													
ANDA approvals - during the quarter	2	0	1	4	4	1	1	4	4	1	4	1	1
NDA approvals - during the quarter	0	1	0	0	0	0	0	0	0	0	0	0	0
Filings													
ANDA filings - during the quarter	0	2	2	6	2	3	1	3	2	0	2	3	3
NDA filings - during the quarter	0	0	0	0	0	0	0	0	0	0	0	0	0
Pending approval													
ANDA	32	34	35	36	34	36	36	35	33	32	30	32	32
NDA	1	0	0	0	0	0	0	0	0	0	0	0	0

Source: Company, Kotak Institutional Equities

Exhibit 8: Sun Pharma – segmental revenue build-up

March fiscal year-ends, 2013-21E (Rs mn)

	2013	2014	2015	2016	2017	2018	2019E	2020E	2021E
Domestic formulations	29,660	36,918	67,166	75,537	77,490	80,293	89,939	100,840	113,165
US (excluding Taro)	25,633	52,737	44,585	47,728	53,380	53,076	73,735	96,568	106,277
Taro (US)	31,956	40,468	47,506	56,634	52,487	35,234	36,958	36,774	34,623
RoW/EM	18,240	19,084	60,646	57,461	77,114	78,132	87,094	97,291	108,461
Total formulations	105,489	149,207	219,903	237,360	260,470	246,735	287,727	331,472	362,526
API	7,550	8,010	9,910	14,025	15,980	13,993	13,714	13,439	13,170
Others	73	138	792	752	715	679	645	613	582
Other income	610	740	1,469	5,256	13,142	4,235	2,067	2,466	2,713
Total	113,721	158,096	232,074	257,392	290,307	265,642	304,152	347,990	378,992
yoy growth, %									
Domestic formulations	2	24	82	12	3	4	12	12	12
US (excluding Taro)	104	106	(15)	7	12	(1)	39	31	10
Taro	44	27	17	19	(7)	(33)	5	(0)	(6)
RoW	64	5	218	(5)	34	1	11	12	11
Total formulations	41	41	47	8	10	(5)	17	15	9
API	23	6	24	42	14	(12)	(2)	(2)	(2)
Total	40	39	47	11	13	(8)	14	14	9
% of sales									
Domestic formulations	26	23	29	29	27	30	30	29	30
US (excluding Taro)	23	33	19	19	18	20	24	28	28
Taro	28	26	20	22	18	13	12	11	9
RoW	16	12	26	22	27	29	29	28	29
Total formulations	93	94	95	92	90	93	95	95	96
API	7	5	4	5	6	5	5	4	3

Source: Company, Kotak Institutional Equities estimates

Exhibit 9: Sun Pharma – consolidated profit and loss, balance sheet, cash model
 March fiscal year-ends, 2013-21E (Rs mn)

	2013	2014	2015	2016	2017	2018	2019E	2020E	2021E
Net revenues	112,999	160,784	275,390	287,953	315,784	264,895	304,152	347,990	378,992
Gross Profit	92,265	132,990	207,998	223,121	234,477	190,648	218,294	252,144	275,669
Staff costs	(15,345)	(20,744)	(45,026)	(47,971)	(49,023)	(53,671)	(59,038)	(63,761)	(68,861)
R&D expenses	(7,042)	(10,153)	(18,373)	(23,025)	(21,459)	(20,669)	(25,482)	(28,706)	(31,315)
Other expenses	(20,916)	(30,158)	(64,462)	(63,630)	(63,103)	(60,227)	(67,235)	(71,946)	(75,129)
EBITDA	48,963	71,936	80,136	88,494	100,893	56,081	66,539	87,731	100,364
Depreciation & amortisation	(3,362)	(4,094)	(11,947)	(10,135)	(12,648)	(14,998)	(16,822)	(17,677)	(18,389)
EBIT	49,482	72,923	68,189	78,359	88,245	41,083	49,718	70,054	81,974
Net Interest	(432)	(442)	(5,790)	(4,769)	(3,998)	(5,176)	(5,363)	(5,281)	(5,198)
Other income	3,881	5,081	4,008	914	6,232	8,388	8,412	10,210	12,773
Exceptional items	—	(25,174)	(2,378)	(6,852)	—	(9,505)	—	—	—
Profit before tax	49,050	72,481	63,904	74,486	90,578	44,062	52,766	74,984	89,549
Tax & Deferred Tax	(8,456)	(7,908)	(9,147)	(9,349)	(12,116)	(8,452)	(8,651)	(13,840)	(17,157)
Less: minority interest	(4,863)	(7,375)	(9,363)	(11,126)	(8,819)	(4,468)	(3,574)	(3,354)	(2,739)
Net Income (adjusted)	35,732	57,198	45,394	54,011	69,644	33,665	40,541	57,790	69,653
EPS adjusted (Rs)	17.2	27.6	18.9	22.4	28.9	14.0	16.8	24.0	28.9
Balance sheet									
Equity	166,248	204,461	293,582	354,901	404,305	419,847	459,429	512,369	573,569
Total borrowings	1,982	24,890	75,963	83,381	80,910	97,518	96,018	94,518	93,018
Deferred tax liability	2,054	2,757	985	616	3,148	2,190	2,190	2,190	2,190
Other liabilities	30,568	35,493	92,561	80,263	112,321	118,846	123,512	128,537	132,180
Total liabilities	208,812	293,708	490,279	542,196	614,102	643,028	685,776	742,240	805,583
Net fixed assets	50,771	58,242	110,201	133,606	149,403	157,111	172,671	164,994	156,604
Investments	11,064	7,876	5,989	5,933	4,605	53,996	53,996	53,996	53,996
Cash	53,639	95,886	131,155	147,045	153,717	140,200	170,175	212,882	269,075
Other current assets	84,882	121,192	215,576	225,287	287,360	286,061	303,155	324,589	340,129
Total assets	208,812	293,708	490,279	542,196	614,102	643,028	705,658	762,122	825,465
Cashflow statement									
Operating profit before working capi	44,812	45,410	71,765	84,923	95,485	42,382	69,588	92,661	107,938
Tax paid	(10,735)	(7,889)	(17,404)	(19,885)	(20,571)	(8,452)	(8,651)	(13,840)	(17,157)
Change in working capital	(448)	2,071	1,796	2,656	(4,092)	6,186	(12,429)	(16,410)	(11,897)
Capital expenditure	(8,455)	(9,060)	(23,419)	(33,825)	(36,929)	(20,000)	(12,500)	(10,000)	(10,000)
Free cash flow	25,174	30,532	32,739	33,869	33,894	20,115	36,009	52,411	68,885
Margins and ratios									
Gross profit margin (%)	81.7	82.7	75.5	77.5	74.3	72.0	71.8	72.5	72.7
EBITDA margin (%)	43.3	44.7	29.1	30.7	31.9	21.2	21.9	25.2	26.5
Tax rate (%)	17.2	10.9	14.3	12.6	13.4	19.2	16.4	18.5	19.2
RoAE (%)	26.3	19.1	20.2	16.3	20.5	5.8	10.2	13.1	14.0
RoACE (%)	40.0	52.9	33.4	29.8	31.3	16.3	18.6	25.9	30.1

Source: Company, Kotak Institutional Equities estimates

AUGUST 16, 2018

RESULT

Coverage view: **Cautious**

Price (₹): 987

Target price (₹): 1,170

BSE-30: 37,852

Strong quarter led by VSF and Chemicals. Grasim's standalone EBITDA increased 25% qoq to ₹10.5 bn led by higher earnings in both VSF (+46% qoq) and chemicals businesses (+20% qoq) on improved volumes and firm prices. The company is also gaining on market development efforts in India as domestic VSF volumes increased by 31% yoy. Grasim has undertaken ₹75 bn expansion in VSF, chemicals which will result in close to 40% growth in capacities over the next two years (over FY2018). We maintain our BUY rating and revise target price to ₹1,170 (from ₹1,275 earlier).

Company data and valuation summary

Grasim Industries

Stock data				Forecasts/Valuations				
				2018	2019E	2020E		
52-week range (Rs) (high,low)		1,300-914		EPS (Rs)	47.4	46.2	54.9	
Market Cap. (Rs bn)		648.8		EPS growth (%)	(30.1)	(2.5)	18.8	
Shareholding pattern (%)				P/E (X)	20.8	21.4	18.0	
Promoters		40.1		Sales (Rs bn)	562.0	756.9	843.7	
Flts		34.3		Net profits (Rs bn)	31.1	30.4	36.1	
MFs		5.2		EBITDA (Rs bn)	98.9	176.3	201.6	
Price performance (%)				EV/EBITDA (X)	11.8	7.3	7.0	
Absolute		1M	3M	12M	ROE (%)	7.0	5.2	5.9
Rel. to BSE-30		1.8	(15.8)	(26.1)	Div. Yield (%)	0.6	0.6	0.6

Strong standalone earnings led by both VSF and chemicals business

Grasim's standalone earnings were ahead of our estimate—the company reported revenues of ₹47.9 bn (+75% yoy, +4% qoq), EBITDA of ₹10.5 bn (+90% yoy, +25% qoq) and net-income of ₹6.4 bn (+85% yoy, +72% qoq), against our estimate of ₹45.9 bn, ₹8.4 bn and ₹5.1 bn, respectively. The earnings beat was led by improved volumes and margins in both VSF and chemicals operations.

- ▶ **VSF—EBITDA improves 68% yoy.** VSF revenues increased 35% yoy to ₹24.8 bn (+11% qoq), EBITDA increased 68% yoy to ₹5.9 bn (+46% qoq). Volumes increased by 9% yoy to 132,000 tons (+6% qoq) aided by 31% yoy growth in domestic sales to 109,000 tons—domestic volumes now account for 83% of sales versus 69% in 1QFY18. Realization improved 6% qoq on the back of firm global prices and higher domestic sales—this helped increase EBITDA/ton by 37% qoq to ₹44,400/ton.
- ▶ **Chemicals—EBITDA improves 103% yoy.** The chemical business reported its highest ever EBITDA at ₹5 bn (+103% yoy, +20% qoq) aided by (1) an 18% yoy increase in caustic soda volumes to 235,000 tons (+9% yoy), and (2) higher caustic soda realizations (+25% yoy, steady qoq). The company's capacity utilization was 92% in the chemicals business.

Grasim reported consolidated revenues of ₹168.6 bn (-3% qoq) and net income of ₹11.2 bn (+8% qoq)—the restructuring exercise makes year-on-year comparisons less relevant. We highlight 1QFY19 earnings report for other key segments in page 2.

We cut our target price to ₹1,170/ton and maintain BUY rating

We cut our target price to ₹1,170/ton (from ₹1,275 earlier) as we cut our standalone estimates on lower margin expectation. Our SOTP-based TP of ₹1,170/share comprises (1) ₹517/share value for 60% ownership in Ultratech valued at 30% holding company discount on our fair value of ₹2,950/share, (2) VSF (₹198/share) and chemicals (₹170/share), valued at 6X EBITDA on FY2020E earnings, (3) ₹182/share for Aditya Birla Capital valued at 30% holding company discount to CMP for Grasim's 56% ownership, and (4) ₹94/share for investments held in equity of group companies (at 30% discount to CMPs. We value other smaller operations at ₹38/share (these include textile, rayon, fertilizers, insulators, etc).

Abhishek Poddar

Murtuza Arsiwalla

Samrat Verma

Changes in our estimate

Exhibit 6 highlights changes in our estimates.

We cut our consolidated EBITDA estimate by 0-2% to ₹176 bn, ₹202 bn and ₹229 bn for FY2019E, FY2020E and FY2021E. Our EPS estimate is cut by 5-17% to ₹46.2, ₹54.9 and ₹70.3 for FY2019E, FY2020E and FY2021E. The hit on the EPS is higher due to expected higher losses from IDEA which results in a drag from losses from associates.

The key changes in our estimates across businesses include:

- ▶ **Cement operations—cut in estimates.** We incorporate lower EBITDA estimate for Ultratech—we had cut EBITDA by 0-3% to ₹71 bn, ₹83.1 bn and ₹94.9 bn for FY2019E, FY2020E and FY2021E. Our revised earnings estimates factor volume estimates of 66.8 mn tons, 71.4 mn tons and 76.4 mn tons for FY2019E, FY2020E and FY2021E. Earnings revision was driven by a cut in our realization assumption by 2-3% for FY2019-2021E and tweaking in cost estimates.
- ▶ **Standalone earnings—factor an improvement.** We cut our EBITDA estimate for standalone operations by 0-10% to ₹41.5 bn, ₹41.6 bn and ₹42 bn for FY2019E, FY2020E and FY2021E. This is largely as we assumed lower margins in VSF, chemicals business as against a sharp jump in earnings in last few quarters. The weakening of CNY/US\$ can take some sheen out of the sharp increase in prices seen in recent quarters.

We estimate Idea net losses at ₹73.2 bn, ₹74.9 bn and ₹66.4 bn for FY2019E, FY2020E and FY2021E, respectively. Correspondingly share of Grasim for its 28% equity holding will be ₹20.5 bn, ₹20.9 bn and ₹18.6 bn for each of the years.

Other segment earnings print—key businesses.

- ▶ **Ultratech—subdued due to weak realizations, rising costs.** Ultratech's earnings were broadly in line with estimates—the company reported revenues of ₹86.6 bn (+31% yoy, -4% qoq), EBITDA of ₹16.2 bn (+4% yoy, -5% qoq) and net-income of ₹6 bn (-33% yoy, -16% qoq), against our estimate of ₹84.9 bn, ₹15.5 bn and ₹5.9 bn, respectively. Domestic volumes increased by 33% yoy to 16.8 mn tons (-5% qoq; capacity utilization: 77%) led by ramp-up of acquired assets—note that last year's volumes exclude acquired assets as acquisition was completed only in June 2017; we estimate volume growth for extant operations (ex-acquisition) at close to 10% yoy for 1QFY19.

While realizations were weak at ₹4,950/ton (-1% yoy, +1% qoq), the increase in costs to ₹4,020/ton (+5% yoy, +1% qoq) resulted in EBITDA/ton falling to ₹928 (-21% yoy, +1% qoq). The cost increase is due to a combination of higher raw-material, freight and fuel costs as well as weaker INR/US\$ rate—these cost drivers which make 65% of total costs are under pressure.

- ▶ **IDEA—extraordinary income due to sale of towers to ATC.** Grasim reported profit from associate of ₹416 mn in the quarter compared to loss from associate of ₹1.4 bn in 4QFY18. This was largely due to one-off gains from the sale of standalone towers to ATC. The company recognized share of profit of ₹3.7 bn for the quarter due to this sale.

VSF—EBITDA improves 68% yoy on firm prices, higher volumes

VSF revenues increased 35% yoy to ₹24.8 bn (+11% qoq), EBITDA increased 68% yoy to ₹5.9 bn (+46% qoq). VSF volumes increased 9% yoy to 132,000 tons (6% qoq)—the company reported its highest ever domestic sales of 109,000 tons (+31% yoy) and domestic sales now account for 83% of total sales compared to 69% earlier. The 6% qoq increase in volumes was aided by debottlenecking of capacity.

Firm prices along with higher domestic sales pushed up blended realization by 24% yoy to ₹188,000 tons (+4% qoq) and aided in improvement in EBITDA/ton to ₹44,400/ton (+54% yoy, +37% qoq). The company also highlighted improved cost efficiencies led by improved consumption norms in steam, power, caustic soda and others.

Also, there was no water shortage this year aided by adequate water storage—last year Harihar operations were impacted due to water shortage.

Chemicals—EBITDA improves 103% yoy

The chemical business reported its highest ever EBITDA at ₹5 bn (+103% yoy, +20% qoq) aided by (1) an 18% yoy increase in caustic soda volumes to 235,000 tons (+9% yoy), and (2) higher caustic soda realizations (+25% yoy, steady qoq). The company's capacity utilization was 92% in the chemicals business. The blended EBITDA/ton increased to ₹21,000/ton (+74% yoy, +10% qoq) led by better realizations, cost efficiencies.

The management highlighted that caustic soda prices have moderated in the quarter due to some softening in global prices due to delayed ramp-up of alumina plants post winter cuts and increased imports from the Middle East into India. Earnings were aided by an increase in volumes of specialty products (chlorine-based value-added products).

Volume growth story in VSF and Chemicals businesses

Grasim will spend ₹75 bn in capacity expansion and sustenance projects over the next 2-3 years—this includes ₹43 bn towards brownfield expansion in VSF operations and ₹13 bn for expansion in chemicals operations.

- ▶ **Chemicals.** The company completed the commissioning of 146 ktpa caustic soda plant at Vilayat during the quarter which resulted in total capacity increasing to 1,140 ktpa. The board of Grasim has approved the ₹11 bn investment in expanding the capacity of caustic soda and specialty chemicals, which will increase Grasim's total capacity to 1,310 ktpa.
- ▶ **VSF.** The company's capacity in VSF is 546 ktpa and it is pursuing a 219 ktpa expansion at its Vilayat plant—the project work has already commenced with order placement for long lead equipment. The total VSF capacity upon completion of these projects will increase to 788 ktpa.

Exhibit 1: Grasim's standalone earnings improved led by strong growth in volumes, margins of VSF and Chemicals business
Quarterly results for Grasim Industries (Standalone), March fiscal year-ends (Rs mn)

	1QFY19	1QFY19E	1QFY18	4QFY18	Change (%)			FY2019E	FY2018	(% chg.)
					KIE	yoy	qoq			
Net sales	47,892	45,883	27,403	46,056	4	75	4	192,346	157,885	22
Total expenditure	(37,350)	(37,526)	(21,850)	(37,609)				(150,796)	(127,083)	
EBITDA	10,542	8,358	5,553	8,447	26	90	25	41,550	30,802	35
EBITDA (%)	22.0	18.2	20.3	18.3				21.6	19.5	
Other income	1,217	1,030	658	1,020				5,169	4,614	
Interest	(588)	(490)	(73)	(486)				(1,661)	(1,281)	
Depreciation	(1,827)	(1,871)	(1,103)	(1,853)				(8,753)	(6,277)	
Pre-tax profits	9,343	7,026	5,036	7,128				36,306	27,858	
Tax	(2,344)	(1,897)	(1,564)	(1,210)				(10,892)	(7,445)	
Net income	6,426	5,129	3,472	5,918	25	85	9	25,414	20,413	25
Extraordinaries	—	—	—	(2,187)				—	—	
Reported net profits	6,426	5,129	3,472	3,731				25,414	20,413	
EPS (Rs)	9.8	7.8	5.3	5.7	25	85	72	38.7	31.1	25
Segment details										
Revenues										
VSF	24,800	23,098	18,360	22,320	7	35	11	96,242	83,760	15
Chemicals	15,790	15,089	10,840	14,390	5	46	10	59,376	50,040	19
Others	7,302	8,726	(1,957)	9,346	—	—	—	34,601	22,892	51
Total	47,892	46,913	27,244	46,056	2	76	4	190,219	156,692	21
EBITDA										
VSF	5,860	4,447	3,490	4,010	32	68	46	22,351	16,800	33
Chemicals	4,950	3,911	2,440	4,120	27	103	20	17,441	13,000	34
Others	480	933	—	1,050	—	—	—	3,751	2,656	41
Total	11,290	9,291	5,930	9,180	22	90	23	43,542	32,456	34
Operational details										
VSF										
Volumes (tons)	132,000	127,050	121,000	124,000	4	9	6	545,514	508,000	7
Realization (Rs/ton)	187,879	181,800	151,736	180,000	3	24	4	176,424	164,882	7
EBITDA (Rs/ton)	44,394	35,000	28,843	32,339	27	54	37	39,342	31,320	26
Chemicals										
Volumes (tons)	235,000	230,050	201,000	215,000	2	17	9	991,800	886,000	12
Realization (Rs/ton)	67,191	65,592	53,930	66,930	2	25	0	59,867	56,479	6
EBITDA (Rs/ton)	21,064	17,000	12,139	19,163	24	74	10	17,585	14,673	20

Source: Company, Kotak Institutional Equities estimates

Exhibit 2: Grasim's consolidated earnings improved on the back of higher standalone earnings
Quarterly results for Grasim Industries (Consolidated), March fiscal year-ends (Rs mn)

	1QFY19	1QFY18	4QFY18	Change (%)		FY2019	FY2018	(% chg.)
				yoy	qoq			
Net sales	168,567	98,459	174,380	71	(3)	756,918	561,980	35
Total expenditure	(129,880)	(76,631)	(139,180)			(580,592)	(463,072)	
EBITDA	38,687	21,828	35,200	77	10	176,327	98,909	78
EBITDA (%)	23.0	22.2	20.2			23.3	17.6	
Other income	2,330	2,361	2,539			11,669	9,902	
Interest	(12,964)	(1,495)	(12,046)			(54,328)	(13,591)	
Depreciation	(7,671)	(4,432)	(7,707)			(31,983)	(27,244)	
Pre-tax profits	20,382	18,262	17,985	12	13	101,685	67,976	
Tax	(6,803)	(5,456)	(4,879)			(32,877)	(19,471)	
Minority interest	(2,834)	(3,577)	(1,335)			(19,164)	(10,090)	
Profit from associates	416	(10)	(1,432)			(19,291)	(7,274)	
Net income	11,161	9,219	10,338	21	8	30,353	31,140	(3)
Extraordinaries	—	(315)	(3,137)			—	(4,356)	
Reported net profits	11,161	8,904	7,201	25	55	30,353	26,784	13
EPS (Rs)	17.0	19.1	11.0	(11)	55	46.2	47.4	(3)

Source: Company, Kotak Institutional Equities estimates

Exhibit 3: VSF, Chemical EBITDA increased in 1QFY19; inclusion of financial services, other businesses distorts yoy comparison
Division-wise breakup of Grasim's interim results (Consolidated), March fiscal year-ends (Rs mn)

	1QFY19	1QFY18	4QFY18	Change (%)		Proportion (%)			FY2019E	FY2018
				y-o-y	q-o-q	1QFY19	1QFY18	4QFY18		
Revenue										
VSF and Pulp wood	24,804	18,360	22,320	35	11	15	19	13	96,242	83,760
Cement	85,046	66,265	90,025	28	(6)	50	67	52	358,128	297,901
Chemicals	15,785	10,840	14,390	46	10	9	11	8	59,376	50,040
Financial services	30,502	—	42,030	—	—	18	—	24	189,058	108,913
Others	12,429	2,995	5,615	315	121	7	3	3	54,114	21,367
Total	168,567	98,459	174,380	71	(3)				756,918	561,980
Other income	2,330	2,361	2,539	(1)	(8)				11,669	9,902
EBITDA (includes other income)										
VSF and Pulp wood	5,860	3,490	4,010	68	46	24	19	18	22,351	16,800
Cement	18,026	15,601	17,028	16	6	21	24	19	71,251	58,833
Chemicals	4,950	2,440	4,120	103	20	31	23	29	17,441	13,000
Others	12,181	2,658	12,580	358	(3)				76,952	20,178
Total	41,017	24,189	37,738	70	9	24	25	22	187,996	108,811

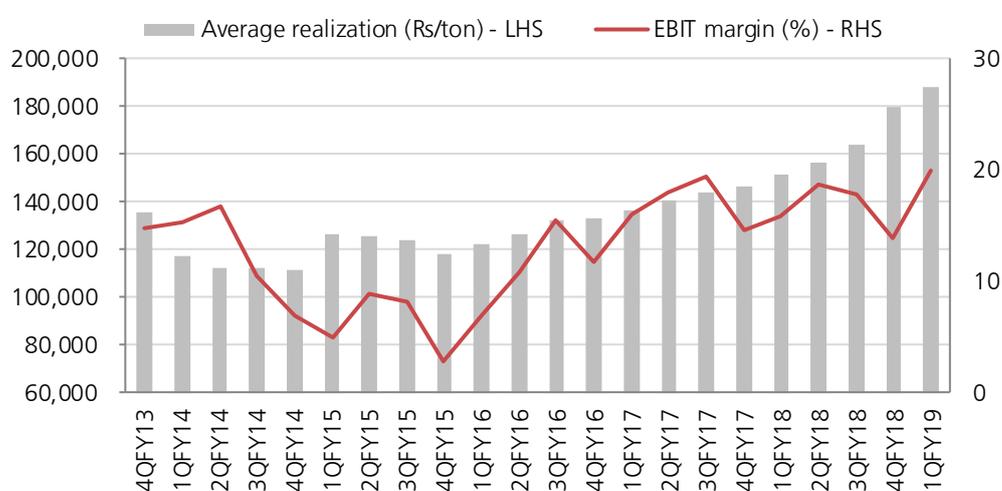
Source: Company, Kotak Institutional Equities estimates

Exhibit 4: Ultratech's volumes increased 33% yoy led by ramp-up of acquired cement assets
Key performance metrics of Ultratech cement for 1QFY19

	1QFY19	1QFY19E	1QFY18	4QFY18	Change (%)		
					KIE	yoy	qoq
Revenues (Rs mn)	85,046	84,857	66,265	90,025	0	28	(6)
EBITDA (Rs mn)	18,026	15,455	15,601	17,028	17	16	6
PAT (Rs mn)	10,265	5,850	8,906	7,142	75	15	44
Volumes (mn tons)	16.2	17.1	12.6	18.5	(5)	29	(12)
Realizations (Rs/ton)	4,946	4,953	5,263	4,877	(0)	(6)	1
EBITDA/ton (Rs/ton)	928	902	1,182	922	3	(21)	1

Source: Company, Kotak Institutional Equities estimates

Exhibit 5: VSF margins improved aided by improved realizations, higher domestic sales
VSF business - realizations and margins



Source: Company, Kotak Institutional Equities estimates

Exhibit 6: Grasim Industries, changes in estimates, March fiscal year ends, FY2019-2021E

	Revised estimate			Previous estimate			Change (%)		
	2019E	2020E	2021E	2019E	2020E	2021E	2019E	2020E	2021E
Consolidated									
Revenues	756,918	843,730	936,142	743,107	831,749	922,352	2	1	1
EBITDA	176,327	201,598	229,082	176,290	204,729	233,834	0	(2)	(2)
PAT	30,353	36,073	46,164	33,978	45,138	57,839	(11)	(20)	(20)
EPS	46.2	54.9	70.3	51.7	68.7	88.0	(11)	(20)	(20)
Standalone									
Revenues	192,346	202,002	210,289	178,535	190,022	196,499	8	6	7
EBITDA	41,550	41,638	41,969	41,514	44,769	46,721	0	(7)	(10)
PAT	25,414	24,202	23,483	26,623	29,217	30,503	(5)	(17)	(23)
EPS	38.7	36.8	35.7	40.5	44.5	46.4	(5)	(17)	(23)

Source: Kotak Institutional Equities estimates

Exhibit 7: Grasim Industries, valuation details, March 2020E financials (Rs/share)

	Basis	Multiple	EBITDA	Ownership	Value	
		(X)	(Rs bn)	(%)	(Rs bn)	(Rs/share)
Value of standalone entity						
VSF / VFY	EV/EBITDA	6	21	100	130	198
Chemicals	EV/EBITDA	6	18	100	112	170
Textiles (Jaya Shree Textiles)	EV/EBITDA	6	1	100	7	11
Agri business (Indo Gulf Fertilizers)	EV/EBITDA	6	2	100	14	21
Insulators (Aditya Birla Insulators)	EV/EBITDA	6	1	100	4	6
Standalone net cash				100	(19)	(29)
Value of standalone business					248	377
Value of investments						
Ultratech	TP (30% discount)	2,950		60	339	517
Aditya Birla Capital Ltd	CMP (30% discount)	141		56	119	182
Idea Cellular	CMP (30% discount)	52		28	37	56
Aditya Birla Fashions	CMP (30% discount)	192		11	12	18
Hindalco Industries	CMP (30% discount)	221		3	8	13
Larsen & Toubro	CMP (30% discount)	1,254		1	5	8
Value of investments					521	793
Total					768	1,170

Source: Kotak Institutional Equities estimates

Exhibit 8: Grasim's valuation has high sensitivity to UTCM's valuation, holding company discount
Valuation sensitivity of Grasim to UTCM's share prices, holding company discount (Rs/share)

		Hold co. discount (%)				
		-	20	30	40	50
Ultratech share price (Rs/share)	2,950	1,509	1,283	1,170	1,056	943
	3,500	1,647	1,393	1,266	1,139	1,012
	2,650	1,434	1,223	1,117	1,011	906
	2,950	1,509	1,283	1,170	1,056	943
	3,250	1,584	1,343	1,222	1,101	981
	4,150	1,810	1,523	1,380	1,236	1,093

Source: Kotak Institutional Equities estimates

Exhibit 9: Idea Cellular continues to be a drag on consolidated earnings
Attributable profits for Grasim Industries, March fiscal year-ends, 2017-21 (Rs mn)

	Ownership (%)	Attributable PAT				
		2017	2018	2019E	2020E	2021E
Grasim (Standalone)	100	15,600	20,413	25,414	24,202	23,483
Ultratech	60	15,766	13,388	19,620	25,281	31,627
ABCL	56		4,616	5,976	7,729	9,807
Idea Cellular	28		(11,671)	(20,491)	(20,973)	(18,586)
Others		307	4,395	(166)	(166)	(166)
Grasim (Consolidated)		31,673	31,140	30,353	36,073	46,164
Grasim (Consolidated ex-telecom)		31,673	42,811	50,844	57,046	64,750
Grasim (Consolidated EPS)		68	47	46	55	70
Grasim (Consolidated EPS ex-telecom)		68	65	77	87	99

Source: Company, Kotak Institutional Equities estimates

Exhibit 10: Grasim Industries, Profit model, balance sheet and cash flow model (consolidated), March fiscal year-ends, 2016-2021E (Rs mn)

	2016	2017	2018	2019E	2020E	2021E
Profit model (Rs mn)						
Net sales	362,177	360,684	561,980	756,918	843,730	936,142
EBITDA	62,700	73,851	98,909	176,327	201,598	229,082
Other income	7,555	9,478	9,902	11,669	11,984	16,182
Interest	(7,513)	(7,024)	(13,591)	(54,328)	(61,149)	(70,210)
Depreciation	(19,110)	(18,076)	(27,244)	(31,983)	(33,460)	(35,524)
Profit before tax	43,632	58,229	67,976	101,685	118,973	139,530
Current tax	(5,107)	(13,460)	(17,338)	(27,588)	(31,425)	(36,148)
Deferred tax	(5,236)	(3,607)	(2,133)	(5,290)	(6,816)	(8,527)
Net profit before minority	33,289	41,162	48,505	68,807	80,731	94,854
Share of profit of associates	1,455	1,294	(7,274)	(19,291)	(19,773)	(17,386)
Minority Interest	(9,105)	(10,783)	(10,090)	(19,164)	(24,885)	(31,305)
Adjusted PAT	25,639	31,673	31,140	30,353	36,073	46,164
Earnings per share (Rs)	54.9	67.8	47.4	46.2	54.9	70.3
Balance sheet (Rs mn)						
Equity	274,293	313,868	573,619	600,284	632,669	675,145
Borrowings	125,040	92,130	613,134	750,237	867,107	986,528
Minority Interest	87,288	97,019	263,369	282,532	307,417	338,722
Policy holders liability	—	—	363,734	402,551	464,576	538,942
Deferred tax liability	30,440	35,388	55,963	61,253	68,069	76,596
Current liabilities	78,894	89,271	208,640	177,802	203,248	245,348
Total liabilities	595,955	627,676	2,078,458	2,274,660	2,543,086	2,861,280
Fixed assets	330,436	330,893	553,554	566,896	602,516	611,396
Investments	40,064	50,694	199,521	180,230	160,457	143,071
Current investments	65,949	91,310	83,149	69,260	73,847	79,286
Investment of insurance business	—	—	130,192	157,152	197,840	245,065
Assets held to cover linked liabilities	—	—	247,089	265,626	289,199	318,963
Cash	23,072	23,070	13,149	36,774	39,730	69,795
Other current assets	106,280	101,765	689,887	836,803	1,017,579	1,231,785
Goodwill	30,155	29,944	161,918	161,918	161,918	161,918
Total assets	595,955	627,676	2,078,458	2,274,660	2,543,086	2,861,280
Ratios						
Book value (Rs/share)	588	672	873	914	963	1,028
RoAE (%)	10.1	10.8	7.0	5.2	5.9	7.1
RoACE (%)	9.9	11.5	7.3	8.3	8.6	9.0

Source: Company, Kotak Institutional Equities estimates

AUGUST 16, 2018

RESULT

Coverage view:

Price (₹): **673**

Target price (₹): **760**

BSE-30: **37,852**

Consumers hold the key. Tata Chemicals' results were marked by strong growth in India operations albeit from a low base, partly offset by weaker performance of overseas subsidiaries due to shutdowns. The incremental disclosures on relevant segment break-up is a welcome change, especially as the new initiatives in consumer and specialty products portfolios are expected to drive long-term earnings growth. We find the reward-risk favorable and retain ADD with an unchanged TP of ₹760.

Company data and valuation summary

Tata Chemicals

Stock data

52-week range (Rs) (high,low) 775-559

Market Cap. (Rs bn) 171.5

Shareholding pattern (%)

Promoters 30.8

FIs 11.1

MFs 24.8

Price performance (%)

	1M	3M	12M
Absolute	(3.2)	(11.9)	15.5
Rel. to BSE-30	(6.5)	(17.3)	(4.0)

Forecasts/Valuations

	2018	2019E	2020E
EPS (Rs)	52.1	44.1	50.5
EPS growth (%)	7.9	(15.3)	14.6
P/E (X)	12.9	15.3	13.3
Sales (Rs bn)	103.5	115.6	127.4
Net profits (Rs bn)	13.3	11.2	12.9
EBITDA (Rs bn)	22.7	23.8	27.0
EV/EBITDA (X)	7.2	6.3	5.2
ROE (%)	14.0	9.7	10.3
Div. Yield (%)	3.3	2.2	2.5

Strong domestic performance offset by overseas shutdown and higher tax rate

Reported consolidated revenues increased 13% yoy to ₹27.7 bn. EBITDA increased 8% yoy to ₹5.2 bn, reflecting moderation of margins for the domestic soda ash business and shutdown in overseas plants. Net income grew 24% yoy to ₹2.14 bn (EPS of ₹8.4), led by a sharp increase in other income, which was partly offset by a higher tax rate at 34%. Consolidated net debt reduced to ₹15 bn from ₹19 bn a quarter ago, with subsidy receivables declining to ₹5.1 bn from ₹8.6 bn. The company completed the acquisition of Allied Silica for ₹1.23 bn in June 2018.

Robust growth in consumer and specialty off a low base; weak basic chemicals performance

- ▶ **Basic chemistry—strong domestic offset by weak overseas.** The domestic soda ash business reported 9% yoy increase in revenues to ₹7.4 bn and 17% yoy increase in EBIT to ₹2 bn led by 16% growth in volumes to 201 ktons. North America revenues declined 7% qoq to ₹7.65 bn led by 5% reduction in volumes due to a planned shutdown in June and 5% decline in US\$-realizations; EBITDA declined 6% qoq to ₹1.3 bn saved by lower costs. Europe operations were relatively steady, while the African operations were impacted by heavy rains. The company indicated that the global soda ash market is expected to be tight given strong growth in demand, which is adequately absorbing incremental supplies from Turkey.
- ▶ **Consumer business—robust growth albeit from a low base.** The consumer segment, which constitutes salt, pulses, spices and other products, reported 33% yoy growth in revenues to ₹4.4 bn and 46% yoy jump in EBIT to ₹823 mn, led by (1) strong 28% yoy growth in salt volumes to 288 ktons from a low pre-GST base and (2) higher EBIT margins at 18.8% versus 15.8% in 1QFY18 and 15.5% in FY2018. The company confirmed that salt is being transferred from the basic chemistry segment, at an arms-length transfer pricing and hence, margins pertaining to its manufacturing facilities are accounted in basic chemistry.
- ▶ **Specialty products.** The specialty portfolio, including Rallis, Metahelix, nutritional solutions and advance materials, witnessed 25% yoy growth in revenues to ₹5.8 bn and a tad slower 19% yoy increase in EBIT to ₹671 mn, reflecting modestly lower margins.

Fine tune estimates; retain ADD with unchanged TP of ₹760

We cut FY2019-21E EPS by 2-3%, factoring in (1) improved outlook of global soda ash business, (2) lower estimates for Rallis, (3) FY2018 AR and 1QFY19 disclosures and (3) other minor changes. Our SoTP-based TP remains unchanged at ₹760 based on FY2020 estimates. We find the reward-risk favorable post the recent under-performance and expect incremental growth on consumers segment and new initiatives.

Tarun Lakhotia

Akshay Bhor

Exhibit 1: Interim results of Tata Chemicals, consolidated, March fiscal year-ends (Rs mn)

	1QFY19	1QFY19E	1QFY18	4QFY18	(% chg.)			FY2019E	FY2018	(% chg.)
					1QFY19E	1QFY18	4QFY18			
Net sales	27,691	26,573	24,517	25,551	4	13	8	115,626	102,697	13
Operating costs	(22,535)	(21,174)	(19,740)	(20,426)	6	14	10	(91,841)	(80,790)	14
EBITDA	5,157	5,399	4,778	5,124	(4)	8	1	23,785	21,907	9
Other income	817	600	187	738	36	336	11	3,143	1,595	97
Interest cost	(887)	(842)	(755)	(855)	5	17	4	(2,417)	(3,256)	(26)
Depreciation	(1,351)	(1,350)	(1,263)	(1,339)	0	7	1	(5,284)	(5,180)	2
PBT	3,735	3,806	2,947	3,668	(2)	27	2	19,227	15,066	28
Tax	(1,258)	(914)	(759)	(351)	38	66	258	(5,191)	(601)	
Exceptionals	—	—	—	12,715				3,750	12,783	
PAT before MI	2,477	2,893	2,187	16,031	(14)	13	(85)	17,785	27,248	(35)
MI	338	200	461	221	69	(27)	53	2,794	2,202	27
PAT	2,140	2,693	1,726	15,810	(21)	24	(86)	14,991	25,046	(40)
Adjusted PAT	2,140	2,693	1,726	6,910	(21)	24	(69)	11,241	12,263	(8)
Adjusted EPS (Rs)	8.4	10.6	6.8	27.1	(21)	24	(69)	44.1	48.1	(8)
EBITDA margins (%)	18.6	20.3	19.5	20.1				20.6	21.3	
Tax rate (%)	33.7	24.0	25.8	9.6				27.0	4.0	
Segment sales										
Basic chemistry products	19,415		18,785	19,509		3	(0)	81,381	76,729	6
Consumer products	4,383		3,297	4,028		33	9	19,888	15,122	32
Specialty products	5,844		4,675	3,827		25	53	21,661	18,434	18
Unallocated	57		44	43				209	190	
Less: inter-segment	2,007		1,527	1,857		31	8	7,514	7,022	7
Total sales	27,691		25,274	25,551		10	8	115,626	103,454	12
Segment profits										
Basic chemistry products	2,753		2,828	3,567		(3)	(23)	15,590	14,611	7
Consumer products	823		520	565		58	46	3,630	2,347	55
Specialty products	671		564	207		19	225	2,424	2,039	19
Unallocated	375		(209)	232				—	(32)	
Total EBIT	4,622		3,702	4,571		25	1	21,644	18,965	14
Segment margins (%)										
Basic chemistry products	14.2		15.1	18.3				19.2	19.0	
Consumer products	18.8		15.8	14.0				18.3	15.5	
Specialty products	11.5		12.1	5.4				11.2	11.1	
EBIT margin (%)	16.7		14.6	17.9				18.7	18.3	
Segment assets										
Basic chemistry products	147,485		138,994	142,132					142,132	
Consumer products	1,674		1,382	1,405					1,405	
Specialty products	23,378		18,488	19,839					19,839	
Unallocated	88,336		51,132	84,553					84,553	
Total assets	260,873		209,997	247,930					247,930	
Segment liabilities										
Basic chemistry products	27,669		29,325	28,804					28,804	
Consumer products	1,581		1,155	1,373					1,373	
Specialty products	10,127		7,966	7,561					7,561	
Unallocated	81,570		84,094	77,360					77,360	
Total liabilities	120,947		122,539	115,098					115,098	

Source: Company, Kotak Institutional Equities estimates

Exhibit 2: Strong growth in standalone results from a low pre-GST base for salt business

Quarterly details of standalone business, 1QFY17 onwards (Rs mn)

	1QFY17	2QFY17	3QFY17	4QFY17	1QFY18	2QFY18	3QFY18	4QFY18	1QFY19	Change (%)	
										Yoy	Qoq
Volumes ('000 tons)											
Soda ash	181	168	164	195	174	162	182	175	201	16	15
Salt	252	245	272	255	225	254	267	270	288	28	7
Financials (Rs mn)											
Net sales	15,970	16,150	9,310	9,390	8,680	8,260	9,120	9,180	9,960	15	8
Basic chemistry products					6,780				7,400	9	
Consumer products					3,300				4,380	33	
Specialty products					70				110	57	
Unallocated					40				40	0	
Inter-segment					(1,520)				(1,980)	30	
EBITDA	2,920	1,850	2,400	1,620	2,090	2,272	2,280	2,570	2,620	25	2
PBT	2,740	1,190	2,050	1,530	2,210	2,240	1,870	2,710	3,680	67	36
Basic chemistry products					1,730				2,030	17	
Consumer products					520				820	58	
Specialty products					(40)				(50)	25	
PAT	1,950	870	1,440	1,060	1,550	1,680	1,530	1,750	2,640	70	51

Source: Company, Kotak Institutional Equities

Exhibit 3: Africa volumes declined due to heavy rains and shutdown, while Europe volumes remained low

Quarterly details of Europe/Africa business, 1QFY17 onwards (Rs mn)

	1QFY17	2QFY17	3QFY17	4QFY17	1QFY18	2QFY18	3QFY18	4QFY18	1QFY19	Change (%)	
										Yoy	Qoq
Volumes ('000 tons)											
Europe-soda ash	127	128	123	113	106	107	104	78	76	(28)	(3)
Magadi-soda ash	72	61	68	76	86	86	78	85	73	(15)	(14)
Financials (Rs mn)											
Net sales	5,580	5,400	5,450	5,150	4,520	5,220	5,500	5,040	4,520	-	(10)
Europe	4,130	3,950	3,990	4,090	3,390	3,560	3,740	3,680	3,570	5	(3)
Magadi	1,450	1,450	1,460	1,060	1,130	1,660	1,760	1,360	950	(16)	(30)
EBITDA	520	630	670	980	420	810	900	990	330	(21)	(67)
Europe	410	570	550	840	220	550	630	780	450	105	(42)
Magadi	110	60	120	140	200	260	270	210	(120)	NA	NA
EBITDA per ton - Europe (US\$)	48	66	66	111	32	80	92	155	88	175	(43)
EBITDA per ton - Africa (US\$)	23	15	26	28	36	47	53	38	(25)	NA	NA
PBT	20	340	410	600	(30)	350	360	390	(200)	NA	NA
PAT	10	350	390	600	(30)	340	350	390	(200)	NA	NA

Source: Company, Kotak Institutional Equities

Exhibit 4: US volumes declined due to plant shutdown; lower costs mitigated lower realizations

Quarterly details of the US business, 1QFY17 onwards (Rs mn)

	1QFY17	2QFY17	3QFY17	4QFY17	1QFY18	2QFY18	3QFY18	4QFY18	1QFY19	Change (%)	
										Yoy	Qoq
Volumes ('000 tons)											
	569	572	556	543	569	630	562	589	558	(2)	(5)
Financials (Rs mn)											
Net sales	8,220	8,260	8,090	7,850	7,950	8,570	7,870	8,190	7,650	(4)	(7)
Net sales per ton (US\$)	216	215	215	216	217	212	213	216	205	(6)	(5)
EBITDA	1,610	1,890	1,700	1,170	1,490	2,180	1,800	1,410	1,320	(11)	(6)
EBITDA per ton (US\$)	42	49	45	32	41	54	49	37	35	(13)	(5)
PBT	850	1,180	920	520	700	1,410	1,600	680	520	(26)	(24)
PAT	420	520	400	130	270	690	3,270	1,040	210	(22)	(80)

Source: Company, Kotak Institutional Equities

Exhibit 5: We value TTCH at ₹760/share
SoTP valuation for TTCH, March 2020E basis

Business	Methodology	FY2020E	Multiple	Valuation	
		(Rs bn)	(X)	(Rs bn)	(Rs/share)
Basic chemistry products	EV/EBITDA	18.6	6.0	111.7	438
Consumer products	EV/EBITDA	4.6	15.0	68.7	270
Specialty products (ex-Rallis)	EV/Sales	1.8	2.0	3.6	14
Rallis	Fair value	21.7	0.8	17.4	68
Quoted investments	Fair value	16.3	0.8	13.1	51
Total assets				214.5	842
Less: Net debt				(6.7)	(26)
Less: Pension liability				(14.0)	(55)
Equity valuation				193.9	761

Source: Kotak Institutional Equities estimates

Exhibit 6: We expect gradual improvement in contribution from consumer and specialty portfolio
Segment-wise financials, March fiscal year-ends, 2018-21E (Rs mn)

	2018	2019E	2020E	2021E
Consolidated segment revenues				
Basic chemistry products	76,729	81,381	86,085	89,499
Consumer products	15,122	19,888	23,868	28,475
Specialty products	18,434	21,661	25,372	28,821
Unallocated	190	209	230	253
Inter-segment	(7,022)	(7,514)	(8,124)	(8,784)
Revenues	103,454	115,626	127,430	138,264
Consolidated segment EBIT				
Basic chemistry products	14,611	15,590	16,629	16,935
Consumer products	2,347	3,630	4,535	5,624
Specialty products	2,039	2,424	3,077	3,681
Unallocated	(32)	—	—	—
EBIT	18,965	21,644	24,241	26,239
EBIT margin (%)				
Basic chemistry products	19.0	19.2	19.3	18.9
Consumer products	15.5	18.3	19.0	19.8
Specialty products	11.1	11.2	12.1	12.8
EBIT margin	18.3	18.7	19.0	19.0

Source: Company, Kotak Institutional Equities estimates

Exhibit 7: Consolidated profit model, balance sheet and cash flow statement for Tata chemicals, March fiscal year-ends, 2014-21E (Rs mn)

	2014	2015	2016	2017	2018	2019E	2020E	2021E
Profit model (Rs mn)								
Sales	158,954	172,029	148,729	129,418	102,697	115,626	127,430	138,264
EBITDA	18,094	21,574	20,917	22,236	21,907	23,785	26,954	29,386
Other income	1,424	1,180	1,253	1,661	1,595	3,143	2,886	2,767
Interest	(5,793)	(4,540)	(5,255)	(4,112)	(3,256)	(2,417)	(1,924)	(1,584)
Depreciation	(4,712)	(4,631)	(5,261)	(5,347)	(5,180)	(5,284)	(5,599)	(5,914)
Extraordinary items	(14,202)	(1,997)	742	1,348	12,068	3,750	—	—
Profit before tax	(5,189)	11,585	12,397	15,787	27,134	22,977	22,317	24,656
Tax expense	(2,888)	(3,511)	(2,484)	(3,573)	(601)	(5,191)	(6,249)	(6,904)
Minority interest	(2,243)	(2,109)	(2,356)	(2,410)	(2,694)	(3,019)	(3,433)	(3,658)
Income from associates	—	—	149	128	492	225	242	260
PAT	(10,320)	5,965	7,706	9,931	24,331	14,991	12,877	14,354
Adjusted PAT	3,882	7,962	7,112	8,888	12,263	11,241	12,877	14,354
Adjusted EPS (Rs)	15.2	31.3	27.9	34.9	48.1	44.1	50.5	56.3
Balance sheet (Rs mn)								
Equity	55,655	55,517	68,543	79,082	111,017	121,306	128,853	137,878
Total borrowings	83,696	83,787	90,699	70,483	64,180	43,100	31,953	20,421
Deferred tax liability/minority interest	9,321	9,007	38,423	38,620	40,397	43,192	46,383	49,780
Current liabilities and provisions	53,431	59,746	45,888	47,866	43,192	42,567	44,993	47,219
Total liabilities	202,104	208,056	243,552	236,051	258,786	250,165	252,181	255,298
Net fixed assets	47,520	45,913	120,196	112,654	114,358	116,574	118,475	120,062
Goodwill/Intangible assets	67,226	69,570	17,619	16,984	17,319	17,319	17,319	17,319
Investments	4,409	4,374	21,879	27,907	28,683	28,683	28,683	28,683
Cash and equivalents	17,530	14,698	12,654	16,654	44,830	36,440	33,791	32,785
Other current assets and miscellaneous	65,420	73,502	71,205	61,852	53,596	51,149	53,913	56,449
Total assets	202,104	208,056	243,552	236,051	258,786	250,165	252,181	255,298
Free cash flow (Rs mn)								
Operating cash flow	9,177	19,483	17,769	18,751	21,149	16,176	18,781	20,899
Working capital changes	8,406	(11,177)	(652)	12,103	(5,691)	1,822	(338)	(310)
Capital expenditure (net)	(5,938)	(5,649)	(6,896)	(6,453)	(7,306)	(7,500)	(7,500)	(7,500)
Free cash flow	11,645	2,657	10,221	24,401	8,152	10,499	10,943	13,089
Ratios								
EBITDA margin (%)	11.4	12.5	14.1	17.2	21.3	20.6	21.2	21.3
Net debt/equity (X)	1.19	1.24	1.14	0.68	0.17	0.05	(0.01)	(0.09)
Book value (Rs/share)	218	218	269	310	436	476	506	541
RoAE (%)	6.2	13.0	10.4	10.9	11.1	8.7	9.2	9.8
RoACE (%)	11.0	13.6	10.7	12.7	12.8	14.5	16.8	18.7

Source: Company, Kotak Institutional Equities estimates

AUGUST 16, 2018
RESULT

Coverage view:

 Price (₹): **606**

 Target price (₹): **640**

 BSE-30: **37,852**

A mixed bag. GAVL's 1QFY19 results were marked by (1) strong performance of oil palm, (2) robust recovery in animal feed volumes and (3) sharp expansion in crop-protection margins. However, (1) contraction in animal feed margins, (2) deferment of Astec's exports order and (3) a weak dairy performance took some sheen away. We retain ADD with a TP of ₹640 (₹650 earlier), although we will look for better entry points in the stock to play the medium-term narrative of diversified agri/rural growth.

Company data and valuation summary

Godrej Agrovet

Stock data			Forecasts/Valuations				
52-week range (Rs) (high,low)	738-522		EPS (Rs)	2018	2019E	2020E	
Market Cap. (Rs bn)	116.4		EPS growth (%)	11.5	14.8	19.1	
Shareholding pattern (%)			P/E (X)	(6.9)	28.9	28.8	
Promoters	68.8		Sales (Rs bn)	52.6	40.8	31.7	
FIs	3.2		Sales (Rs bn)	51.9	59.0	67.1	
MFs	3.9		Net profits (Rs bn)	2.2	2.9	3.7	
Price performance (%)			EBITDA (Rs bn)	4.4	5.4	6.8	
Absolute	1M	3M	12M	EV/EBITDA (X)	27.1	22.1	17.3
Rel. to BSE-30	(0.7)	(10.5)	0.0	ROE (%)	14.7	15.7	17.4
	(4.1)	(15.9)	0.0	Div. Yield (%)	0.3	0.4	0.5

Strong volumes growth and in-line revenues marred by moderation in margins

GAVL's revenues increased 10% yoy to ₹14.8 bn, in line with our estimate, as robust 16% growth in animal feed and 29% growth in vegetable oil, were offset by a slower 2% growth in dairy revenues and unexpected 8% decline in crop protection revenues amid deferment of Astec's exports order. Gross and EBITDA margins remained steady yoy at 23.9% and 9.4%, respectively. EBITDA and EBIT increased 11-12% yoy to ₹1.39 bn and ₹1.17 bn, respectively, both a tad below our estimates. Adjusted net profit increased 6% yoy to ₹802 mn (EPS of ₹4.2), in line with our estimate, as lower other income was offset by higher associates' contribution.

Robust growth in crop protection and oil palm; signs of recovery in animal feed

- ▶ **Robust recovery in animal feed volumes offset by weak margins.** Animal feed volumes grew by 19% yoy to 304 ktons in 1QFY19 led by strong growth in cattle, boiler and layer feeds. Revenue grew 16% yoy reflecting modestly lower realizations. However, EBIT declined sharply by 9% yoy to ₹361 mn, reflecting 140 bps moderation in margins to 4.9%. GAVL attributed lower profitability to (1) sharply higher input prices for aqua feed as compared to 1QFY18 and (2) adverse pricing in cattle feed business due to lower milk prices.
- ▶ **Strong contribution from oil palm business.** Oil palm revenues jumped 29% yoy led by recent increase in domestic crude palm oil prices, benefiting from higher import duties. EBIT increased 68% yoy to ₹358 mn, led by sharp ~500 bps expansion in margins to 21.3%. Palm oil plantation area under coverage increased to 64,125 hectares from 61,700 hectares a year ago. GAVL's new palm oil mill in Andhra Pradesh is on track to commission during 2QFY19.
- ▶ **Delay in Astec's exports offset by sharp expansion in domestic margins.** Crop protection revenues declined 8% yoy led by deferment of export orders for Astec, which is expected to be included in 2QFY19. Domestic business (excluding Astec) was also subdued with net revenues growing by a modest 6% yoy. Nevertheless, overall crop-protection EBIT increased 7% yoy to ₹762 mn, reflecting sharp ~420 bps expansion in margins to 29.7% entirely contributed by the domestic portfolio. De-bottlenecking of Astec's capacities and new intermediate/backward integration plants are on track to commission later this year.
- ▶ **Weak performance of dairy segment.** Dairy business revenues grew by a modest 2% yoy presumably led by moderation in prices. EBIT margin was negligible at 0.1% due to higher provisioning costs pertaining to lower butter prices amid oversupply.

4-7% cut in EPS estimates

We cut FY2019-21 EPS estimates by 4-7%, factoring in (1) weakness in animal feed margins and dairy business, (2) higher capitalization/depreciation and (3) higher contribution from crop protection and oil palm segments. Our SoTP-based TP reduces to ₹640 from ₹650 earlier.

Tarun Lakhotia

Akshay Bhor

Exhibit 1: Quarterly results, March fiscal year-ends (Rs mn)

	1QFY19	1QFY19E	1QFY18	4QFY18	(% chg.)			FY2019E	FY2018	(% chg.)
					1QFY19E	1QFY18	4QFY18			
Net sales	14,844	14,928	13,441	11,947	(1)	10	24	58,954	51,853	14
Raw materials	(11,297)	(11,345)	(10,238)	(9,178)	(0)	10	23	(44,506)	(39,534)	13
Employee costs	(779)	(772)	(689)	(674)	1	13	16	(3,142)	(2,764)	14
Other costs	(1,375)	(1,375)	(1,256)	(1,354)	(0)	9	2	(5,899)	(5,125)	15
EBITDA	1,393	1,436	1,258	742	(3)	11	88	5,407	4,430	22
Depreciation	(224)	(220)	(216)	(217)	2	3	3	(996)	(859)	16
EBIT	1,169	1,216	1,042	524	(4)	12	123	4,410	3,571	24
Other income	39	70	67	108	(45)	(42)	(64)	237	318	(25)
Interest	(81)	(75)	(118)	(78)	9	(31)	5	(306)	(453)	(33)
Pretax profits	1,126	1,211	991	554	(7)	14	103	4,342	3,436	26
Extraordinary income	—	—	—	—	—	—	—	—	121	—
Current tax	(334)	(374)	(308)	(229)	—	—	—	(1,395)	(1,108)	—
Deferred tax	(59)	(45)	(35)	35	—	—	—	(125)	(100)	—
Income from associates	77	30	112	(40)	—	—	—	225	161	—
Non-controlling interest	(7)	(24)	(22)	(70)	—	—	—	(196)	(218)	—
Net profit attributable to shareholders	802	798	738	251	1	9	220	2,851	2,292	24
Adjusted net profits	802	798	738	251	1	9	220	2,851	2,171	31
Adjusted EPS (Rs)	4.2	4.2	4.0	1.3	1	5	220	14.8	11.5	29
Key ratios (%)										
Gross margins	23.9	24.0	23.8	23.2	(11)bps	6 bps	71 bps	24.5	23.8	75 bps
EBITDA margins	9.4	9.6	9.4	6.2	(24)bps	2 bps	318 bps	9.2	8.5	63 bps
Effective tax rate	34.9	34.6	34.6	35.0	—	—	—	35.0	35.1	—
Segment sales										
Animal feeds	7,373	6,916	6,345	6,827	7	16	8	29,624	25,760	15
Vegetable oil	1,683	1,566	1,309	517	7	29	225	6,908	5,854	18
Crop protection	2,567	2,974	2,795	1,872	(14)	(8)	37	9,986	8,818	13
Dairy	3,129	3,346	3,082	2,742	(6)	2	14	12,387	11,577	7
Others	153	181	165	21	—	—	—	272	248	—
Excise duty/elimination	(60)	(55)	(254)	(31)	—	—	—	(223)	(197)	—
Net sales	14,844	14,928	13,441	11,947	(1)	10	24	58,954	52,059	13
Segment EBIT										
Animal feeds	361	441	398	488	(18)	(9)	(26)	1,707	1,559	9
Vegetable oil	358	289	214	40	24	68	797	1,489	1,123	33
Crop protection	762	732	713	351	4	7	117	2,457	2,070	19
Dairy	2	64	12	(17)	(97)	(84)	(112)	131	130	1
Others	11	4	9	(23)	—	—	—	(36)	(33)	—
Unallocated	(290)	(244)	(244)	(225)	—	—	—	(1,085)	(996)	—
EBIT	1,204	1,286	1,103	614	(6)	9	96	4,663	3,854	21
Segment margins (%)										
Animal feeds	4.9	6.4	6.3	7.1	(148)bps	(138)bps	(225)bps	5.8	6.1	(29)bps
Vegetable oil	21.3	18.5	16.3	7.7	282 bps	495 bps	1,356 bps	21.6	19.2	238 bps
Crop protection	29.7	24.6	25.5	18.7	506 bps	416 bps	1,093 bps	24.6	23.5	112 bps
Dairy	0.1	1.9	0.4	(0.6)	(184)bps	(34)bps	67 bps	1.1	1.1	(6)bps
EBIT margin	8.1	8.6	8.2	5.1	(50)bps	(10)bps	297 bps	7.9	7.4	51 bps

Source: Company, Kotak Institutional Equities estimates

Exhibit 2: Strong performance in vegetable oil business; animal feeds margins soft
Segment-wise performance, 1QFY17 onwards (Rs mn)

	1QFY17	2QFY17	3QFY17	4QFY17	1QFY18	2QFY18	3QFY18	4QFY18	1QFY19
Segment sales									
Animal feeds	6,985	6,859	6,311	6,053	6,345	6,119	6,470	6,827	7,373
Vegetable oil	1,193	2,197	1,115	561	1,309	2,672	1,356	517	1,683
Crop protection	2,448	2,574	1,497	1,129	2,795	2,593	1,559	1,872	2,567
Dairy	2,513	2,572	2,437	2,576	3,082	2,928	2,825	2,742	3,129
Others	245	67	50	48	165	34	28	21	153
Excise duty/elimination	(100)	(113)	(15)	(27)	(254)	(87)	(30)	(31)	(60)
Net sales	13,285	14,156	11,395	10,340	13,441	14,258	12,207	11,947	14,844
Segment EBIT									
Animal feeds	462	360	395	447	398	284	389	488	361
Vegetable oil	223	491	248	64	214	616	253	40	358
Crop protection	565	672	270	200	713	647	359	351	762
Dairy	165	122	62	17	12	45	90	(17)	2
Others	2	(37)	(16)	(60)	9	9	(28)	(23)	11
Unallocated	(244)	(216)	(161)	(165)	(244)	(266)	(260)	(225)	(290)
EBIT	1,173	1,393	799	427	1,103	1,334	803	614	1,204
Segment EBIT margin									
Animal feeds	6.6	5.3	6.3	7.3	6.3	4.6	6.0	7.1	4.9
Vegetable oil	18.7	22.4	22.3	11.3	16.3	23.0	18.7	7.7	21.3
Crop protection	23.1	26.1	18.1	17.3	25.5	25.0	23.0	18.7	29.7
Dairy	6.6	4.8	2.6	1.0	0.4	1.5	3.2	(0.6)	0.1
Overall	8.8	9.8	7.0	4.2	8.2	9.4	6.6	5.1	8.1

Source: Company, Kotak Institutional Equities

Exhibit 3: Segment break-up, March fiscal year-ends, 2013-21E (Rs mn)

	2013	2014	2015	2016	2017	2018	2019E	2020E	2021E
Segment sales									
Animal feeds	22,389	24,232	25,430	25,442	26,208	25,760	29,624	33,179	36,496
Vegetable oil	2,752	3,574	3,938	4,042	5,066	5,854	6,908	7,944	9,056
Crop protection	2,213	3,040	3,352	4,959	7,647	8,818	9,986	11,696	13,577
Dairy	—	—	—	2,729	10,093	11,577	12,387	14,245	16,382
Others	255	178	398	377	243	248	272	300	330
Excise duty	(4)	—	—	(48)	(153)	(197)	(223)	(254)	(286)
Net sales	27,605	31,025	33,118	37,502	49,105	52,059	58,954	67,109	75,555
EBITDA									
Animal feeds	1,502	1,876	2,314	2,077	1,926	1,856	2,016	2,391	2,721
Vegetable oil	616	732	747	734	1,157	1,270	1,706	1,922	2,200
Crop protection	503	659	859	1,012	1,825	2,216	2,622	3,109	3,497
Dairy	NA	NA	NA	39	532	291	373	785	1,067
Others	6	(2)	(15)	(64)	(45)	24	27	29	32
Unallocated	(681)	(849)	(845)	(831)	(1,016)	(1,227)	(1,338)	(1,445)	(1,560)
EBITDA	1,946	2,415	3,060	2,967	4,380	4,430	5,407	6,791	7,957
EBITDA margins (%)									
Animal feeds	6.7	7.7	9.1	8.2	7.4	7.2	6.8	7.2	7.5
Vegetable oil	22.4	20.5	19.0	18.2	22.8	21.7	24.7	24.2	24.3
Crop protection	22.7	21.7	25.6	20.4	23.9	25.1	26.3	26.6	25.8
Dairy	NA	NA	NA	1.4	5.3	2.5	3.0	5.5	6.5
Others	2.2	(1.3)	NM	(16.9)	(18.4)	9.8	9.8	9.8	9.8
Unallocated	NA	NA	NA	(2.2)	(2.1)	(2.4)	(2.3)	(2.2)	(2.1)
EBITDA margin (%)	7.0	7.8	9.2	7.9	8.9	8.5	9.2	10.1	10.5

Source: Company, Kotak Institutional Equities estimates

Exhibit 4: GAVL commands a premium multiple compared to crop-protection companies
Crop protection peer valuations, March fiscal year-ends, 2018-20E

	Price	Market cap.	P/E (X)			EV/EBITDA (X)		
	(LC)	(US\$ mn)	2018	2019E	2020E	2018	2019E	2020E
Global companies								
BASF SE	79	82,905	12.1	12.1	11.2	6.9	7.2	6.7
Bayer AG	84	89,010	13.1	13.3	10.6	9.0	10.1	8.3
Dow DuPont	67	153,648	20.4	15.8	13.8	11.2	9.5	8.2
FMC Corp.	86	11,555	32.3	14.1	12.6	23.1	10.8	9.6
Nufarm Ltd	7	1,609	15.1	22.5	13.4	7.8	10.1	6.8
Indian companies								
Bayer CropScience	4,202	2,371	48.0	39.8	32.4	39.5	29.2	23.8
Dhanuka Agritech	545	382	21.2	20.4	17.7	15.5	14.9	12.2
PI Industries	788	1,552	29.4	25.0	19.7	21.7	17.8	13.9
Rallis India	195	541	22.4	19.1	16.0	13.9	12.6	10.6
UPL	610	4,442	14.2	12.5	11.1	9.9	8.5	7.2
Godrej Agrovet	605	1,661	52.6	40.8	31.6	26.7	21.8	17.1

Source: Bloomberg, Kotak Institutional Equities estimates

Exhibits 5: We value GAVL at Rs640/share on SoTP of diversified business segments
SoTP valuation of GAVL, March 2020E (Rs mn)

	March 2020E	EV/EBITDA (X)	Stake (%)	EV	Net debt	Equity value
Animal feed	2,391	16	100	38,250		
Oil palm	1,922	18	100	34,599	1,813	108,847
Crop protection (ex-Astec)	2,101	18	100	37,810		
Crop protection (Astec)	1,008	18	57	10,311	597	9,715
Creamline Dairy	785	20	52	8,153	163	7,989
ACI Godrej JV	964	16	50	7,710	178	7,532
Godrej Tyson Foods JV	549	20	50	5,477	(89)	5,566
Unallocated	(1,415)	12	100	(16,985)	0	(16,985)
Target market capitalization						122,664
Target price (Rs/share)						639
Implied March 2020E P/E multiple (X)						33

Source: Kotak Institutional Equities estimates

Exhibits 6: Consolidated financial summary of GAVL, March fiscal year-ends, 2013-21E (Rs mn)

	2013	2014	2015	2016	2017	2018	2019E	2020E	2021E
Profit model (Rs mn)									
Net sales	27,605	31,025	33,118	37,502	49,111	51,853	58,954	67,109	75,555
EBITDA	1,946	2,415	3,060	2,967	4,380	4,430	5,407	6,791	7,957
Depreciation	(193)	(276)	(370)	(524)	(747)	(859)	(996)	(1,205)	(1,334)
EBIT	1,753	2,139	2,691	2,443	3,633	3,571	4,410	5,586	6,624
Other income	110	149	137	627	590	318	237	264	308
Interest	(485)	(403)	(655)	(977)	(863)	(453)	(306)	(220)	(78)
Pretax profits	1,377	1,886	2,173	2,093	3,360	3,436	4,342	5,630	6,854
Extraordinary items	—	—	364	946	200	121	—	—	—
Current tax	(274)	(431)	(551)	(485)	(761)	(1,108)	(1,395)	(1,821)	(2,224)
Deferred tax	(128)	(75)	(55)	(270)	(256)	(100)	(125)	(150)	(175)
Share of income from associates	(7)	186	170	327	186	161	225	259	298
Reported net profits	967	1,566	2,101	2,611	2,729	2,510	3,047	3,918	4,753
Non-controlling interest	—	—	—	29	(241)	(218)	(196)	(246)	(307)
Reported net profit to shareholders	967	1,566	2,101	2,640	2,488	2,292	2,851	3,673	4,446
Adjusted net profit to shareholders	967	1,566	1,737	1,694	2,288	2,171	2,851	3,673	4,446
Adjusted EPS (Rs)	5.6	8.5	9.4	9.2	12.4	11.5	14.8	19.1	23.2
Balance sheet (Rs mn)									
Total equity	4,137	5,187	6,404	10,155	12,641	16,807	19,426	22,793	26,879
Deferred taxation liability	259	435	565	1,458	1,670	1,730	1,730	1,730	1,730
Borrowings	4,791	6,205	6,848	13,757	6,640	4,098	3,548	1,948	—
Current liabilities	2,957	3,934	3,711	5,862	11,197	12,890	14,655	16,682	18,782
Total liabilities and equity	12,143	15,761	17,529	31,232	32,149	35,525	39,360	43,154	47,392
Cash	219	1,145	175	420	623	318	370	488	1,183
Current assets	6,806	7,788	9,323	17,092	18,398	20,548	22,895	25,540	28,179
Total fixed assets	4,119	5,887	6,605	11,607	12,723	14,374	15,778	16,772	17,639
Investments	3	0	366	593	—	—	—	—	—
Loans	997	940	1,060	1,520	405	285	317	354	390
Total assets	12,143	15,761	17,529	31,232	32,149	35,525	39,360	43,154	47,392
Cash flow statement									
Operating cash flow, excl. working cap	1,251	2,014	1,709	1,758	3,019	3,555	3,806	4,860	5,778
Working capital	(1,308)	(1,576)	(31)	(1,046)	5,093	(471)	(614)	(655)	(576)
Capital expenditure	(1,594)	(1,113)	(1,858)	(1,302)	(2,049)	(2,461)	(2,400)	(2,200)	(2,200)
Free cash flow	(1,652)	(676)	(181)	(590)	6,063	622	792	2,005	3,002
Investments	(7)	(131)	(68)	581	610	(131)	—	—	—
Other income	(77)	(82)	(23)	(622)	471	51	237	264	308
Ratios (%)									
EBITDA margin	7.0	7.8	9.2	7.9	8.9	8.5	9.2	10.1	10.5
EBIT margin	6.3	6.9	8.1	6.5	7.4	6.9	7.5	8.3	8.8
Debt/equity	115.8	119.6	106.9	135.5	52.5	24.4	18.3	8.5	—
Net debt/equity	110.5	97.6	104.2	131.3	47.6	22.5	16.4	6.4	(4.4)
Book value (Rs/share)	25	30	38	63	77	98	110	128	149
RoAE	28.9	31.3	33.4	28.4	19.2	14.0	14.4	16.1	16.7
RoACE	16.8	15.9	15.9	10.0	12.7	11.6	12.8	14.9	16.4
RoACE (adjusted for goodwill)	16.2	15.9	16.2	8.8	12.4	12.0	13.4	15.6	17.4

Source: Company, Kotak Institutional Equities estimates

AUGUST 16, 2018
RESULT

Coverage view: **Neutral**

Price (₹): **463**

Target price (₹): **360**

BSE-30: **37,852**

Gearing up. Sunteck Realty continues to improve on sales at its Goregaon ODC project with sales aggregating ₹922 mn during the quarter, even as unit sales at BKC continue to supplement sales and the company prepares to launch its aspirational housing project at Naigaon during the quarter. Successful launch at Naigaon could propel sales momentum, though the same is sufficiently factored in CMP. Maintain REDUCE rating and revise target price to ₹360/share (from ₹330/share).

Company data and valuation summary

Sunteck Realty

Stock data				Forecasts/Valuations				
				2018	2019E	2020E		
52-week range (Rs) (high,low)		471-242		EPS (Rs)	15.3	18.7	19.0	
Market Cap. (Rs bn)		67.7		EPS growth (%)	4.8	22.4	1.6	
Shareholding pattern (%)				P/E (X)	30.3	24.8	24.4	
Promoters		66.8		Sales (Rs bn)	8.9	9.2	9.2	
Fls		22.3		Net profits (Rs bn)	2.1	2.6	2.7	
MFs		3.7		EBITDA (Rs bn)	3.7	3.8	4.0	
Price performance (%)				EV/EBITDA (X)	19.3	20.7	20.0	
Absolute		1M	3M	12M	ROE (%)	9.7	9.5	8.9
Rel. to BSE-30		14.2	0.1	54.1	Div. Yield (%)	0.3	0.2	0.2

Strong sales momentum at Goregaon, BKC supplements sales with additional units

Sunteck recorded sales of ₹1.8 bn selling an area of 89K sq. ft in 1QFY19. Collections were at ₹1.6 bn. Gross cash flows were positive at ₹1.1 bn as construction expenditure for the quarter was at ₹630 mn. Management highlighted that 46 units were sold in Sunteck City Phase 1 & 2 at sales value of ₹922 mn. Phase 3 of the project is expected to be launched in FY2020. During the quarter the company sold units in BKC (sales value of ₹660 mn), leaving an inventory of 49 that will likely be exhausted over the next 3-4 years.

Sunteck launched Gilbert Hill in Andheri (E) in 1QFY19 and sold 11 units with an average realization of ₹17,000/ sq. ft. Apart from this, the company also launched Gateway 51 during the quarter, commencement certificate for the same is expected by end 2QFY19.

Revenue recognition at ₹2.1 for the quarter was broadly in line with our estimates. We highlight Sunteck has continued with recognition of revenues on project completion basis post adoption of Ind-AS 115. EBITDA margins remained healthy at 53% compared to 41% in FY2018.

Naigaon—gearing up for a launch in 2QFY19 with targeted sales of ₹3 bn

Naigaon project is a mid-income housing project and will have gross sales area of nearly 10 mn sq. ft.; expected to be launched in 4-5 phases. As per management, the first phase (to be launched in 2QFY19) involves 1.5 mn sq. ft with ~2500 units in 7 towers with sales values of ₹8 bn. Sunteck would initially launch ~1500 units in 4-5 towers and expects sales of ₹3bn in 2QFY19. We highlight Naigaon is a JDA with revenue-sharing agreement with the land owner (26%). As it is the first JDA Sunteck will be developing post Ind-AS, we await clarity on the accounting to be followed for the project and also on the tax benefits, as part of the project was already launched and completed by the land owner.

Maintain REDUCE, revise target price to ₹360/share

Improving sales momentum at Goregaon is encouraging, as is the targeted launch of the Naigaon project. However, the slow pace of asset monetization at BKC remains a drag. Maintain REDUCE and revise TP to ₹360/share (from ₹330/share).

Murtuza Arsiwalla

Samrat Verma

Exhibit 1: Recognition from BKC and incremental recognition from Goregaon at higher prices beat reported margins
Sunteck: 3QFY18 and 9MFY18 results snapshot, March fiscal year-ends (Rs mn)

	1QFY19	1QFY19E	1QFY18	4QFY18	% change			FY2019E	FY2018	% chg
					1QFY19E	1QFY18	4QFY18			
Financials snapshot										
Net sales	2,111	2,268	1,334	2,067	(7)	58	2	9,166	8,883	3
Operating costs	(995)	(1,125)	(626)	(993)	(12)	59	0	(5,389)	(5,218)	3
EBITDA	1,116	1,143	707	1,074	(2)	58	4	3,777	3,664	3
Other income	139	50	21	50	178	569	178	128	148	(14)
Interest costs	(103)	(103)	(103)	(98)	(0)	0	5	(333)	(421)	(21)
Depreciation	(4)	(5)	(4)	(4)	(24)	0	(16)	(19)	(17)	14
PBT	1,148	1,085	622	1,021	6	85	12	3,554	3,375	5
Taxes	(397)	(325)	(223)	(400)	22	78	(1)	(1,090)	(1,079)	1
PAT	751	759	398	621	(1)	89	21	2,464	2,297	7
Net comprehensive income	589	722	352	560				2,305	2,132	
EPS (Rs/share)	4.2	5.1	2.5	4.0				16.4	15.2	
Key ratios										
EBITDA margin (%)	52.9	50.4	53.0	52.0				41.2	41.3	
PAT margin (%)	35.6	33.5	29.9	30.1				26.9	25.9	
Effective tax rate (%)	34.6	30.0	35.9	39.1				30.7	32.0	

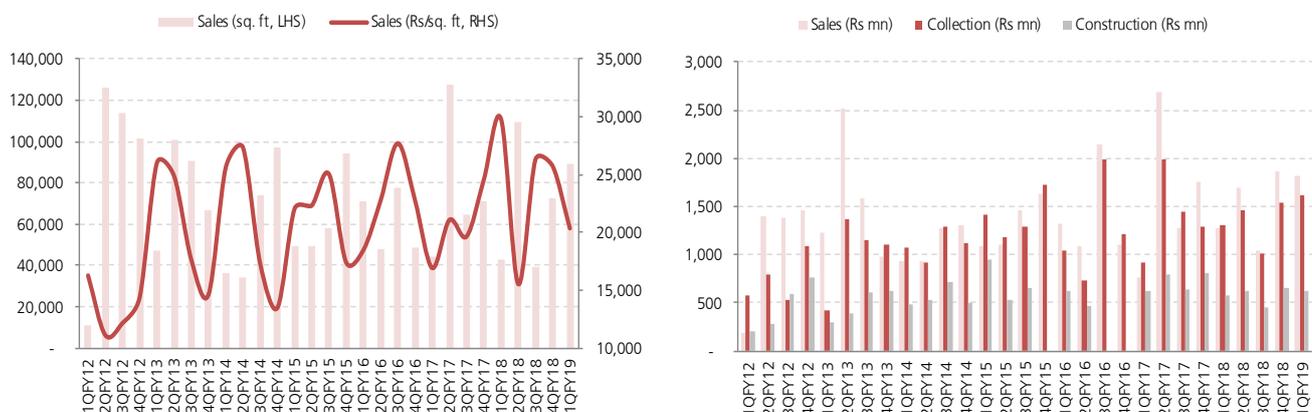
Source: Company, Kotak Institutional Equities estimates

Exhibit 2: Cash collection remained healthy at Rs1.6 bn with construction expense of Rs630 mn
Sunteck's operational performance, 1QFY18-1QFY19

	1QFY18	2QFY18	3QFY18	4QFY18	1QFY19
Sales (sq. ft)	42,880	109,330	39,523	72,289	89,247
Sales (Rs mn)	1,278	1,698	1,040	1,860	1,816
Sales (Rs/sq. ft)	29,813	15,531	26,306	25,727	20,350
Collection (Rs mn)	1,305	1,455	1,006	1,542	1,611
Construction (Rs mn)	570	617	448	652	630

Source: Company, Kotak Institutional Equities estimates

Exhibit 3: Quarterly volatility in blended realizations reflective of contribution of projects outside BKC
Sunteck's operational performance, 1QFY12-1QFY19



Source: Company, Kotak Institutional Equities

Exhibit 4: Our estimates do not factor revenue recognition at Naigaon that will likely accrue beyond FY2021E

Sunteck: Profit model, balance sheet, cash flow model, March fiscal year-ends, 2016-21E (Rs mn)

	2016	2017	2018E	2019E	2020E	2021E
Profit model						
Net sales	2,434	9,522	8,883	9,166	9,240	17,090
EBITDA	239	3,481	3,720	3,777	3,984	7,989
Other income	179	82	93	128	119	58
Interest	(169)	(455)	(421)	(333)	(483)	(213)
Depreciation	(19)	(19)	(17)	(19)	(19)	(20)
Pre-tax profits	231	3,088	3,375	3,554	3,600	7,815
Tax	(815)	(864)	(1,003)	(1,090)	(1,106)	(2,496)
Deferred taxation	878	(8)	(76)	—	—	—
Net income	294	2,216	2,297	2,464	2,495	5,318
Adjusted net income	233	2,043	2,142	2,622	2,665	5,506
Earnings per share (Rs)	1.7	14.6	16.7	16.4	16.6	36.6
Balance sheet						
Total equity	15,985	17,953	26,303	28,762	31,262	36,604
Non-controlling interests	584	706	775	775	775	775
Gross debt	12,340	9,440	5,181	11,445	13,995	964
Non-current liabilities	44	24	29	29	29	29
Current liabilities	12,781	8,647	4,275	3,448	5,246	7,442
Total liabilities and equity	41,734	36,771	36,563	44,458	51,307	45,814
Fixed assets	740	721	705	4,300	8,542	13,543
Non-current financial assets	2,697	2,680	1,709	1,679	1,684	1,691
Other non-current assets	318	298	219	219	219	219
Current assets	37,979	33,072	33,930	38,259	40,862	29,929
Total assets	41,734	36,771	36,563	44,458	51,307	45,382
Free cash flow						
Operating cash flow, excl. working capital	(693)	2,111	2,229	2,642	2,684	5,526
Working capital changes	109	563	(4,191)	(5,052)	56	9,501
Capital expenditure	2	(0)	(0)	(3,615)	(4,261)	(5,021)
Free cash flow	(583)	2,674	(1,962)	(6,025)	(1,520)	10,005
Ratios (%)						
Debt/equity	77.2	52.6	19.7	39.8	44.8	2.6
Net debt/equity	73.1	49.3	17.8	37.8	40.2	8.6
RoE (%)	1.4	12.0	10.6	8.4	7.7	15.1
RoCE (%)	1.8	9.6	9.5	6.9	6.4	15.7
Book value per share (Rs/share)	114	128	187	205	223	261
Adjusted book value per share (Rs /share)	54	68	127	145	163	201

Source: Company, Kotak Institutional Equities estimates

AUGUST 16, 2018

RESULT

Coverage view:

Price (₹): **1,148**

Target price (₹): **1,300**

BSE-30: **37,852**

Weak results. Vardhman's 1QFY19 EBITDA was 6% below our estimate reflecting lower-than-expected spreads amid sharply higher domestic cotton prices; net income was further impacted by lower other income and higher tax rate. Lower domestic cotton acreage, higher cotton prices and reduction in imports from China may keep the yarn spreads in check in the medium term. We cut FY2019-21 EPS estimates by 3-9% and TP to ₹1,300 (₹1,400 previously). ADD stays given undemanding valuation.

Company data and valuation summary

Vardhman Textiles

Stock data		Forecasts/Valuations			
		2018	2019E	2020E	
52-week range (Rs) (high,low)	1,560-1,138	EPS (Rs)	103.0	118.3	129.8
Market Cap. (Rs bn)	65.9	EPS growth (%)	(8.0)	14.8	9.7
Shareholding pattern (%)		P/E (X)	11.1	9.7	8.8
Promoters	62.2	Sales (Rs bn)	62.5	67.4	72.6
FIs	10.6	Net profits (Rs bn)	5.8	6.7	7.3
MFs	14.2	EBITDA (Rs bn)	9.0	11.7	12.8
Price performance (%)	1M 3M 12M	EV/EBITDA (X)	9.5	7.2	6.6
Absolute	(4.8) (8.0) (1.2)	ROE (%)	12.7	13.1	13.0
Rel. to BSE-30	(8.1) (13.6) (17.9)	Div. Yield (%)	1.3	1.7	2.6

Moderation in gross margins takes the sheen away from strong revenue growth

Vardhman's revenues increased 8% yoy to ₹17 bn, 4% above our estimate, led by robust off-take of yarn and fabric in the domestic market. However, gross margins surprised negatively contracting 230 bps qoq to 46.7% reflecting (1) higher procurement price of cotton during later part of the harvesting season and (2) lower fabric margins amid a weak demand environment. EBITDA was 6% below our estimate at ₹2.9 bn, with margins remaining flat qoq at 17.2%, as lower gross margins was mitigated by operating leverage from higher volumes. Reported net income was 17% below our estimate at ₹1.6 bn (EPS of ₹28.2), impacted by sharp decline in other income and higher tax rate.

- ▶ **5% yoy growth in yarn and processed fabric sales volumes.** Yarn sales increased 4.6% yoy to 53.4 ktons, as compared to 1% increase in yarn production. Grey fabric sales declined 1% yoy to 43.3 mn meters, despite 1% increase in production volumes. Processed fabric sales grew 5.4% yoy to 31.1 mn meters, despite flat volumes. The company indicated that the utilization levels are near-100% on yarn facility and ~85% on fabric capacity.
- ▶ **Domestic cotton prices to stay elevated.** We expect the domestic cotton prices to stay elevated underpinned by (1) reduction in cotton acreages by 4% yoy in ongoing Kharif season, (2) early pest attacks in certain parts of Maharashtra, which may have a bearing on yields and (3) possible impact of higher MSPs, if the government decides to procure directly from the market. Domestic cotton prices have increased sharply since the previous harvesting season and are expected to stay elevated unless the yields surprise positively. The management also indicated that imports from China have slowed down amid elevated trade war concerns and relative depreciation of Chinese currency leading to costly imports.
- ▶ **Capacity expansion to drive next leg of growth.** The management indicated that capacity expansions largely remain on track and are expected to be fully commissioned by 4QFY18. Yarn capacity is expected to be fully utilized in a few months post commissioning, while fabric capacity may take time to ramp up depending on end-market demand.

Reduce FY2019-21 EPS estimates by 3-9%; retain ADD with a revised TP of ₹1,300

We reduce FY2019-21E EPS estimates to ₹118 (-9%), ₹130 (-7%) and ₹142 (-3%), respectively, factoring in (1) lower yarn-cotton spreads, (2) higher tax rate and (3) other minor changes. We retain ADD with a revised target price of ₹1,300 (₹1,400 earlier), based on 10X FY2020E EPS.

Tarun Lakhotia

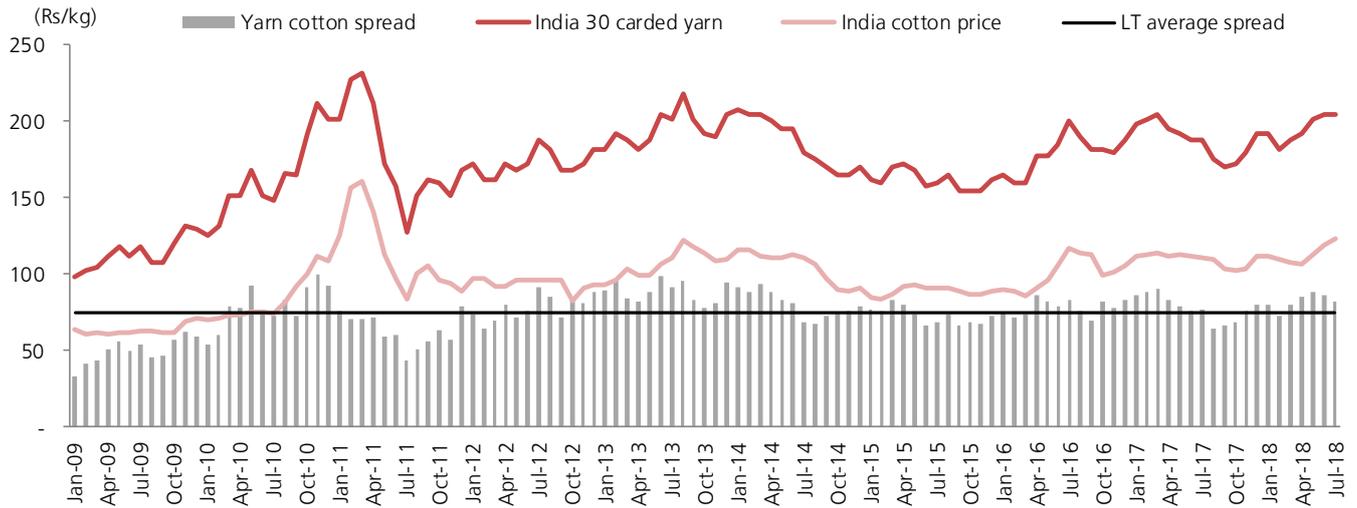
Akshay Bhor

Exhibit 1: Interim results of Vardhman, March fiscal year-ends (Rs mn)

	1QFY19	1QFY19E	1QFY18	4QFY18	(% chg.)			FY2019E	FY2018	(% chg.)
					1QFY19E	1QFY18	4QFY18			
Net sales	17,000	16,401	15,676	15,096	3.7	8.4	12.6	67,419	62,483	7.9
Cost of goods sold	(9,063)	(8,193)	(8,500)	(7,694)	10.6	6.6	17.8	(34,438)	(34,046)	1.2
Power and fuel	(1,639)	(1,631)	(1,553)	(1,531)	0.5	5.5	7.1	(7,081)	(6,271)	12.9
Employee expenses	(1,323)	(1,267)	(1,207)	(1,238)	4.4	9.6	6.9	(5,489)	(5,063)	8.4
Other expenses	(2,053)	(2,197)	(2,210)	(2,041)	(6.6)	(7.1)	0.6	(8,728)	(8,074)	8.1
EBITDA	2,922	3,112	2,205	2,592	(6.1)	32.5	12.7	11,683	9,030	29.4
Other income	273	500	474	613	(45.5)	(42.4)	(55.5)	1,385	1,974	(29.8)
Finance costs	(337)	(350)	(272)	(352)	(3.7)	24.0	(4.3)	(1,256)	(1,182)	6.3
Depreciation and amortization	(619)	(630)	(597)	(627)	(1.7)	3.8	(1.2)	(2,528)	(2,400)	5.3
Pretax profits	2,238	2,632	1,810	2,226	(15.0)	23.7	0.6	9,284	7,421	25.1
Extra-ordinaries	—	—	—	—				—	—	
Tax expense	(661)	(737)	(320)	(618)				(2,694)	(1,672)	
Net income before minority/associates	1,577	1,895	1,490	1,608	(16.8)	5.8	(1.9)	6,589	5,749	14.6
Income/(loss) from associates	50	50	26	49				175	175	
Minority interest	(36)	(20)	(28)	(21)				(91)	(113)	
Net income	1,591	1,925	1,488	1,637	(17.3)	6.9	(2.8)	6,673	5,812	14.8
Adjusted net income	1,591	1,925	1,488	1,637	(17.3)	6.9	(2.8)	6,673	5,812	14.8
Adjusted EPS (Rs)	28.2	34.1	27.1	29.0	(17.3)	4.0	(2.8)	118.3	106.6	11.0
Effective tax rate (%)	29.5	28.0	17.7	27.8				29.0	22.5	
Margins (%)										
Gross margins	46.7	50.0	45.8	49.0	(335)bps	91 bps	(234)bps	48.9	45.5	341 bps
EBITDA margins	17.2	19.0	14.1	17.2	(179)bps	312 bps	2 bps	17.3	14.5	288 bps
Production volumes										
Yarn ('000 tons)	51.2		50.7	50.9		1.0	0.8			
Grey fabric (mn meters)	45.0		44.6	43.4		0.9	3.7			
Processed fabric (mn meters)	30.1		30.0	31.0		0.3	(2.9)			
Sales including internal transfers										
Yarn ('000 tons)	53.4		51.1	50.1		4.6	6.6	212.7	206.5	3.0
Grey fabric (mn meters)	43.3		43.8	42.0		(1.1)	3.1	180.5	172.4	4.7
Processed fabric (mn meters)	31.1		29.5	31.0		5.4	0.3	127.5	120.6	5.7
Segment revenues										
Textiles	16,250		15,201	14,484		6.9	12.2			
Acrylic fibre	995		675	811		47.2	22.6			
Unallocated	—		—	—						
Less; inter-segment	(245)		(200)	(199)						
Total	17,000		15,676	15,096		8.4	12.6			
Segment EBIT										
Textiles	2,465		1,898	2,228		29.9	10.6			
Acrylic fibre	145		68	38		113.8	285.1			
Unallocated	(302)		(156)	(40)		93.9	659.5			
Total	2,308		1,810	2,226		27.5	3.7			

Source: Company, Kotak Institutional Equities estimates

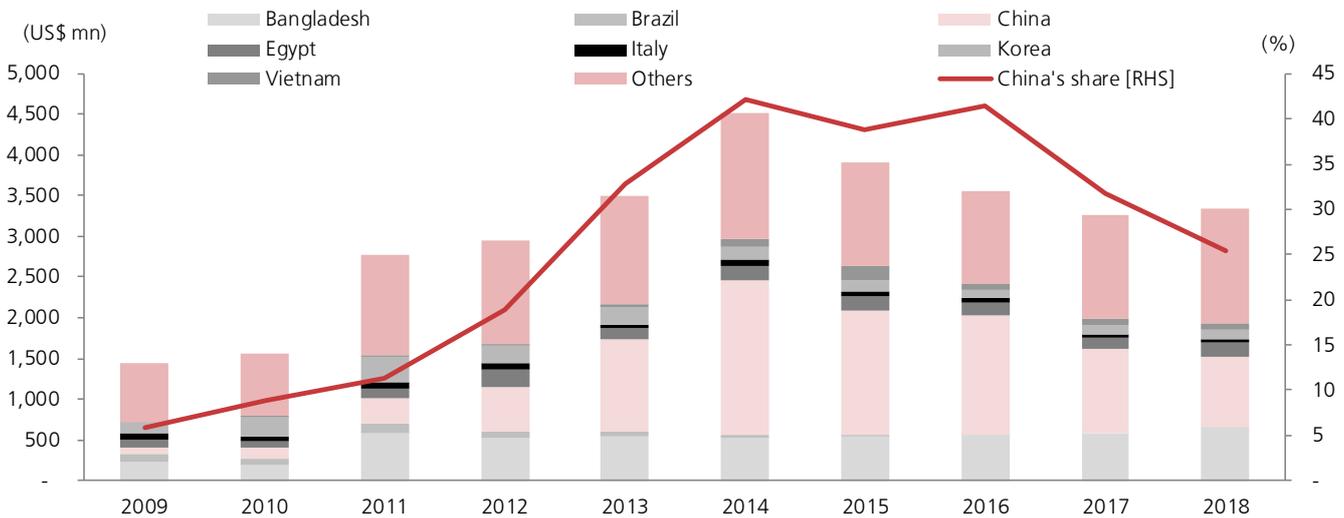
Exhibit 2: India yarn cotton spread, January 2009 onwards (Rs/kg)



Source: Ministry of Textiles, Kotak Institutional Equities

Exhibit 3: India's exports to China have declined over the past two years

Breakdown of yarn exports by destination and China's share, March fiscal year-ends, 2009-18 (US\$ mn, %)



Source: Ministry of Commerce, Kotak Institutional Equities

Exhibit 4: Cotton acreages have declined 4% yoy in the current season
State-wise area under cotton crop in the kharif season (mn hectares)

Crop	Kharif 2017	Kharif 2018	Yoy (%)
Andhra Pradesh	4.1	3.7	(7.7)
Gujarat	26.4	25.5	(3.1)
Haryana	6.6	6.7	1.4
Karnataka	4.1	3.6	(13.0)
Madhya Pradesh	5.8	5.2	(9.0)
Maharashtra	39.4	38.7	(1.8)
Odisha	1.4	1.5	4.9
Punjab	3.9	2.8	(26.2)
Rajasthan	5.0	5.0	(1.4)
Tamilnadu	0.1	0.0	(24.0)
Telangana	17.5	16.9	(3.5)
Others	0.3	0.2	(39.3)
All India	114.3	109.8	(4.0)

Source: Ministry of agriculture, Kotak Institutional Equities

Exhibit 5: Key assumptions, March fiscal year-ends, 2014-21E

	2014	2015	2016	2017	2018	2019E	2020E	2021E
Sales volumes								
Yarn ('000 tons) (a)	164.0	196.9	204.1	203.1	206.5	212.7	224.5	234.7
Grey fabric (mn meters) (a)	151.4	170.1	175.0	177.7	172.4	180.5	200.0	215.2
Processed fabric (mn meters)	106.5	111.4	111.9	118.1	120.6	127.5	139.6	153.6
Growth/margins (%)								
Revenue growth	24.0	10.0	(13.7)	2.9	3.6	7.9	7.7	6.4
EBITDA margins	23.7	16.5	20.1	19.9	14.5	17.3	17.7	18.1

Notes:

(a) Including internal transfers.

Source: Company, Kotak Institutional Equities estimates

Exhibit 6: Consolidated profit model, balance sheet, and cash model, March fiscal year-ends, 2014-21E (Rs mn)

	2014	2015	2016	2017	2018	2019E	2020E	2021E
Profit model (Rs mn)								
Net sales	61,664	67,860	58,596	60,300	62,483	67,419	72,611	77,272
EBITDA	14,633	11,178	11,763	11,993	9,030	11,683	12,848	13,989
Other income	960	1,963	1,583	2,832	2,149	1,560	1,699	1,828
Interest	(1,762)	(1,597)	(889)	(1,287)	(1,182)	(1,256)	(1,300)	(1,319)
Depreciation	(3,355)	(5,322)	(3,742)	(3,434)	(2,400)	(2,528)	(2,730)	(2,954)
Pretax profits	10,476	6,222	8,715	10,104	7,596	9,459	10,517	11,544
Extraordinary items	—	—	—	3,075	—	—	—	—
Current tax	(2,449)	(2,324)	(2,390)	(3,026)	(1,650)	(2,645)	(3,012)	(3,281)
Deferred tax	(372)	559	(84)	(210)	(22)	(49)	(88)	(127)
Adjusted net income	7,183	4,002	6,146	6,739	5,812	6,673	7,323	8,040
Adjusted EPS (Rs)	114.9	64.0	100.9	111.9	105.5	118.3	129.8	142.5
Balance sheet (Rs mn)								
Total equity	35,284	38,163	41,029	43,854	49,537	54,943	60,322	66,420
Deferred tax liability	2,924	2,232	2,377	2,712	2,666	2,715	2,803	2,930
Borrowings and long-term liabilities	33,930	26,642	26,573	22,696	20,622	21,622	20,372	19,122
Current liabilities	6,509	6,746	5,153	5,904	9,606	9,861	9,918	10,118
Total liabilities and equity	78,648	73,784	75,133	75,165	82,431	89,141	93,415	98,589
Cash	807	2,028	2,789	447	738	2,795	1,426	3,018
Loans and advances	6,395	4,782	3,490	3,284	3,285	3,287	3,288	3,290
Current assets	30,825	27,463	27,693	25,572	31,254	32,259	34,455	36,316
Net fixed assets	32,482	29,586	27,130	26,396	27,366	30,838	34,108	35,654
Investments	8,138	9,927	14,031	19,467	19,788	19,963	20,138	20,313
Total assets	78,648	73,784	75,133	75,165	82,431	89,141	93,415	98,589
Free cash flow (Rs mn)								
Operating cash flow, excl. working capital	12,334	9,854	9,534	9,475	8,407	9,338	10,236	11,208
Working capital	(3,995)	4,269	(383)	3,450	(1,981)	(751)	(2,142)	(1,662)
Capital expenditure	(6,582)	(3,128)	(3,888)	(3,099)	(2,803)	(6,000)	(6,000)	(4,500)
Free cash flow	1,757	10,995	5,263	9,826	3,623	2,587	2,095	5,046
Ratios/margins								
Debt/equity	1.0	0.7	0.6	0.5	0.4	0.4	0.3	0.3
Net debt/equity	0.9	0.6	0.6	0.5	0.4	0.3	0.3	0.2
EBITDA margins (%)	23.7	16.5	20.1	19.9	14.5	17.3	17.7	18.1
RoAE (%)	24.0	12.1	15.8	19.2	12.7	12.9	12.9	12.8
RoIC (%)	13.0	7.9	10.3	10.8	10.0	11.7	11.7	11.8

Source: Company, Kotak Institutional Equities estimates

AUGUST 16, 2018

RESULT

Coverage view: **Attractive**

Price (₹): **271**

Target price (₹): **435**

BSE-30: **37,852**

Deleveraging benefits. SEL is well-placed to benefit from deleveraging in FY2019 given (1) SIPL's coming-of-age ability to repay parent SEL (2) normalizing of its working capital situation (receivables, advances). This would support business growth arising from SEL's strong backlog despite some constraints regarding land acquisition. SEL would also indirectly benefit from its stake in SIPL as it churns cash flows from operations and additional monetization proceeds into HAM projects. We only tweak operational estimates and SoTP given an in-line 1QFY19, with a modest cut in revenue guidance. BUY.

Company data and valuation summary

Sadbhav Engineering

Stock data

52-week range (Rs) (high,low) 440-260

Market Cap. (Rs bn) 46.5

Shareholding pattern (%)

Promoters 46.5

FIs 15.5

MFs 22.2

Price performance (%)

Absolute (4.5) (29.2) (1.2)

Rel. to BSE-30 (7.9) (33.5) (17.9)

Forecasts/Valuations

	2018	2019E	2020E
EPS (Rs)	12.9	17.0	22.2
EPS growth (%)	17.4	31.7	31.0
P/E (X)	21.1	16.0	12.2
Sales (Rs bn)	35.1	41.9	53.8
Net profits (Rs bn)	2.2	2.9	3.8
EBITDA (Rs bn)	4.2	5.0	6.4
EV/EBITDA (X)	14.7	11.6	9.1
ROE (%)	12.5	14.5	16.5
Div. Yield (%)	0.0	0.0	0.0

Good progress made on financial closures; 25% of order backlog yet to receive the same

Seven of the 12 HAM projects won are contributing to execution and accounted for a majority of EPC revenues, a welcome shift for both working capital and margin. Such concentration of HAM projects in business would likely continue, given the state of the order backlog and of the Rs600 bn of near-term ordering prospects. Sadbhav continues to get preferential treatment from lenders for financial closures, even while it faces more demanding terms from non-PCA banks which make land assignment a pre-condition for lending/closure. Sadbhav is well placed among peers with just ~25% of its backlog of HAM projects awaiting financial closure. Key irritants from an execution perspective are projects in Una Kodinar and Rampur Kathgodam package II, where SEL is facing land acquisition concerns; the company would like to de-link land acquisition from financial closure by invoking a de-linking clause in the concession agreement, a proposal the NHAI is yet to accept.

Deleveraging benefit to continue through FY2019

SEL was able to reduce debt by Rs0.5 bn to Rs14.3 bn by end-1QFY19. Since then, it has received Rs1.1 bn from SIPL based on proceeds received from the MBCPNL project. More such repayments may be impending given the interest SIPL has received from the perspective of monetizing its road assets. SIPL is now self-sustaining in terms of funding its pending equity commitments even in the absence of monetization. In addition to such support given and not required by SIPL, SEL would also be able to deleverage more based on correction in working capital. This would be driven by the receipt of Rs1 bn of pending GST receivables and receipt of mobilization advances.

We broadly retain estimates given in-line 1QFY19 and modest cut in revenue guidance

Sadbhav Engineering reported a tepid and in-line 1QFY19 with a flattish yoy EBITDA and 26/14% yoy growth in PBT/PAT. The company has marginally lowered its revenue guidance to Rs41 bn based on delays in execution and the start of select projects. Traffic growth was also healthy at ~5.5-6% for its roads portfolio. We marginally revise our estimates and bring down our SoTP to Rs435, from Rs440 earlier.

Aditya Mongia

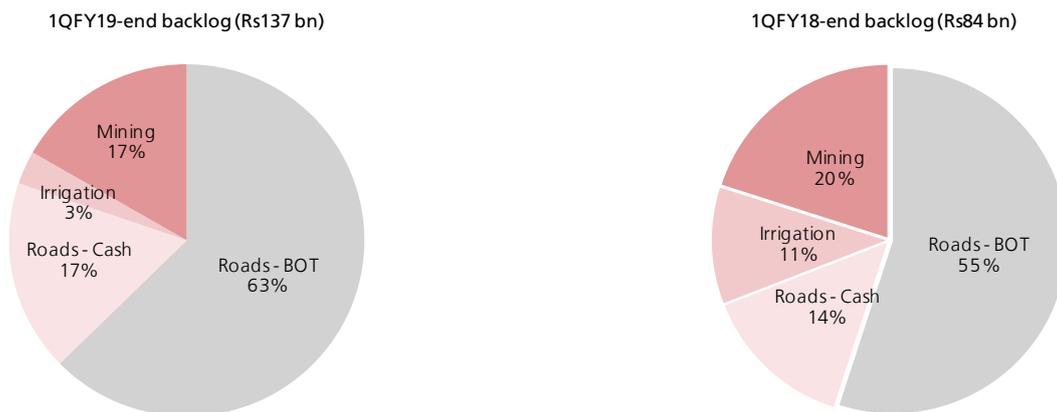
Ajinkya Bhat

Exhibit 1: SEL reported broadly in-line results; deleveraging drove modest beat in PBT
Sadbhav Engineering 1QFY19 results (standalone), March fiscal year-ends (Rs mn)

	1QFY19	1QFY19E	1QFY18	4QFY18	% change			FY2018	FY2017	% change	FY2019E	FY2018	% change
					vs est.	yoy	qoq						
Operational income	9,114	8,932	9,443	11,045	2	(3)	(17)	35,051	33,203	6	41,928	35,051	20
Total expenditure	(8,044)	(7,907)	(8,376)	(9,804)	2	(4)	(18)	(30,899)	(29,646)	4	(36,949)	(30,899)	20
Construction expenses	(7,434)	—	(7,436)	(8,934)		(0)	(17)	(28,134)	(26,551)			(28,134)	
Employee expenses	(424)	—	(309)	(552)		37	(23)	(1,553)	(1,366)			(1,553)	
Other expenses	(186)	—	(631)	(318)		(70)	(41)	(1,211)	(1,729)			(1,211)	
EBITDA	1,070	1,025	1,067	1,240	4	0	(14)	4,152	3,556	17	4,979	4,152	20
Other income	108	200	39	39		176	177	157	333	(53)	739	157	370
Depreciation	(241)	(257)	(245)	(236)		(2)	2	(979)	(1,000)	(2)	(1,102)	(979)	13
Net Interest	(257)	(328)	(322)	(345)		(20)	(25)	(1,167)	(992)	18	(1,556)	(1,167)	33
PBT	681	640	540	698	6	26	(3)	2,163	1,897	14	3,060	2,163	41
Taxes	(46)	—	15	—				44	(18)	(341)	(153)	44	(449)
Net PAT	634	640	555	698	(1)	14	(9)	2,207	1,879	17	2,907	2,207	32
Extraordinary / prior period items	—	—	—	—				—	—		—	—	
Reported PAT	634	640	555	698	(1)	14	(9)	2,207	1,879		2,907	2,207	32
Key ratios (%)													
Construction exp./ sales	81.6	—	78.7	80.9				80.3	80.0			80.3	
Staff cost/ sales	4.7	—	3.3	5.0				4.4	4.1			4.4	
Other exp./ sales	2.0	—	6.7	2.9				3.5	5.2			3.5	
EBITDA margin	11.7	11.5	11.3	11.2				11.8	10.7		11.9	11.8	
PBT margin	7.5	7.2	5.7	6.3				6.2	5.7		7.3	6.2	
Effective tax rate	6.8	—	(2.8)	—				(2.0)	1.0		5.0	(2.0)	
PAT margin	7.0	7.2	5.9	6.3				6.3	5.7		6.9	6.3	
EPS (Rs)	3.7	3.7	3.2	4.1				12.9	11.0		16.9	12.9	

Source: Company, Kotak Institutional Equities estimates

Exhibit 2: As of 1QFY19, HAM projects have taken a dominant role contributing 63% of the order backlog
Mix of order backlog of SEL, March fiscal year-ends, 1QFY18-1QFY19



Source: Company, Kotak Institutional Equities

Exhibit 3: Since 2QFY18, traffic growth has been healthy across the roads portfolio
Trajectory of toll collections for Sadbhav Engineering, March fiscal year-ends, 1QFY16-1QFY19

Revenues (Rs mn)	1QFY16	2QFY16	3QFY16	4QFY16	1QFY17	2QFY17	3QFY17	4QFY17	1QFY18	2QFY18	3QFY18	4QFY18	1QFY19	Yoy growth (%)
Quarterly collections														
Ahemdabad ring road	222	213	231	247	237	227	241	240	219	227	250	262	239	9.2
Aurangabad Jalna	92	69	63	88	78	88	96	91	93	86	96	102	102	10.2
Bijapur-Hungud	284	282	280	302	304	286	265	293	296	297	300	319	316	6.8
Hyderabad Yadgiri	134	119	142	153	149	125	141	153	171	159	185	179	202	17.9
Maharashtra border check-post	335	367	416	432	415	406	409	448	451	432	493	494	582	29.1
Rohtak Panipat	219	199	220	181	205	193	205	225	247	250	284	290	303	22.4
Dhule Palasner	358	368	384	391	418	399	418	449	426	441	475	475	457	7.3
Gomati Ka Chauraha Udaipur				229	252	243	273	250	263	265	273	262	282	7.5
BRTPL						94	104	105	116	110	108	104	115	(0.9)
RHTPL						83	133	130	132	136	153	150	151	14.1
Total (for yoy comparable projects)	1,217	1,180	1,257	1,274	1,311	2,144	2,285	2,383	2,414	2,402	2,602	2,622	2,732	13.2
Yoy growth (%)	9.6	8.7	10.7	6.5	7.8	4.2	1.8	6.7	4.8	12.0	13.9	10.0	13.2	
Tariff growth (%)	3.0	3.0	3.0	3.0	2.0	2.0	2.0	2.0	2.0	3.0	3.5	3.5	7.4	
Implied traffic growth (%)	6.4	5.6	7.4	3.4	5.7	2.2	(0.2)	4.6	2.8	8.8	10.0	6.3	5.4	
Daily collections (Rs mn / day)														
Ahemdabad ring road	2.4	2.3	2.5	2.7	2.6	2.5	2.6	2.7	2.4	2.5	2.7	2.8	2.6	
Aurangabad Jalna	1.0	0.7	0.7	1.0	0.8	1.0	1.0	1.0	1.0	0.9	1.0	1.1	1.1	
Bijapur-Hungud	3.1	3.1	3.0	3.3	3.3	3.1	2.9	3.3	3.3	3.2	3.3	3.4	3.5	
Hyderabad Yadgiri	1.5	1.3	1.5	1.7	1.6	1.4	1.5	1.7	1.9	1.7	2.0	1.9	2.2	
Maharashtra border check-post	3.7	4.0	4.5	4.7	4.5	4.4	4.5	5.0	5.0	4.7	5.4	5.3	6.4	
Rohtak Panipat	2.4	2.2	2.4	2.0	2.2	2.1	2.2	2.5	2.7	2.7	3.1	3.1	3.3	
Dhule Palasner	3.9	4.0	4.2	4.3	4.5	4.3	4.5	5.0	4.7	4.8	5.2	5.1	5.0	
Gomati Ka Chauraha Udaipur	—	—	—	2.5	2.7	2.6	3.0	2.8	2.9	2.9	3.0	2.8	3.1	
BRTPL	—	—	—	—	—	1.0	1.1	1.2	1.3	1.2	1.2	1.1	1.3	
RHTPL	—	—	—	—	—	1.4	2.3	2.3	2.3	2.3	2.6	2.5	1.7	
Total	13.4	12.8	13.7	14.0	14.3	23.3	24.8	26.5	26.5	26.1	28.3	28.2	30.0	

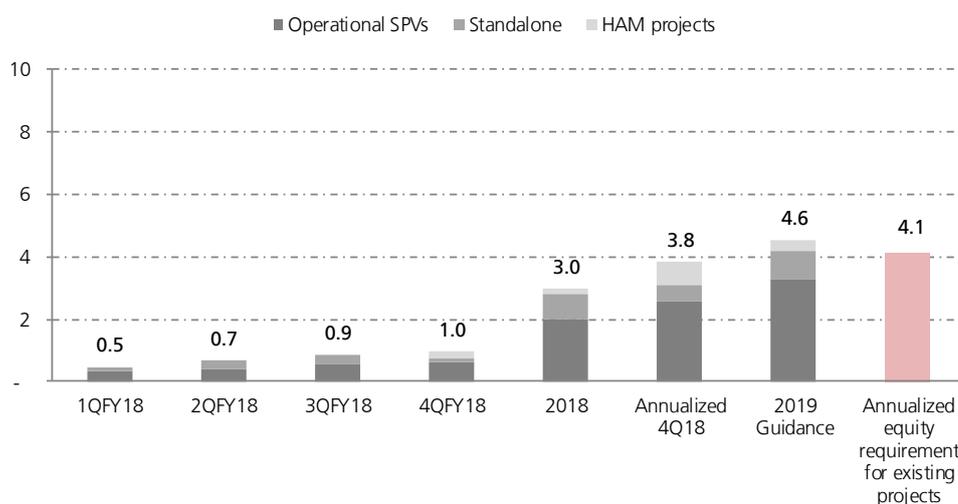
Source: Company, Kotak Institutional Equities estimates

1QFY19 earnings call takeaways

- ▶ **Good ordering pipeline in sight.** The company mentioned that NHA tendering had slowed down since Apr-2018 but is expected to recover by Sep-2018. The current bidding pipeline includes projects worth more than Rs600 bn that are due for bidding by Sep-2018, including:
 - 29 EPC projects with a total length of 1,075 km worth Rs198 bn
 - 38 HAM projects with a total length of 1,777 km worth Rs366 bn (opportunity for SIPL), likely to get delayed by another month as per the management
 - 4 overburden removal projects in mining segment worth Rs14.1 bn
 - One large irrigation project in Gujarat worth Rs24 bn
- ▶ **Guidance for FY2019.** The company targets Rs80 bn of order inflows in FY2019, largely driven by the roads segment. Based on the current order backlog and the new HAM projects expected to start in 2HFY19, the management expects a topline of Rs41 bn in FY2019 and Rs54-55 bn in FY2020 with stable EBITDA margin in the range of ~12%, modestly higher than FY2018 due to the improving mix of HAM projects in execution. Standalone debt currently stands at Rs14.3 bn, which is expected to go down by Rs2-2.5 bn by end-FY2019.

- ▶ **Deleveraging back on track.** In 4QFY18, Sadbhav Engineering had faced a hurdle in furthering its deleveraging agenda due to delays in the release of retention money for SIPL, which led to lower L&A repayments by SIPL and a delay in receipt of the mobilization advance by SEL. The deleveraging effort is back on track in YTD FY2019. SIPL has repaid Rs1 bn of L&A to SEL in the past 1-1.5 months. Outstanding L&A given to SIPL now stands at Rs4.3 bn, and is expected to repay another Rs1 bn in the near term. SIPL is due to receive over Rs7 bn on mobilization advance, which will help L&A repayment to SEL.
- ▶ **Update on HAM project backlog.** The company currently has 12 HAM projects in its backlog, of which seven have received appointed dates and have begun execution. These seven projects contributed Rs5.5 bn of revenues in 1QFY19. Of the recently won five HAM projects, one has completed financial closure and remaining four projects are expected to complete it by Sep-2018. These projects will contribute to execution in 2HFY19. Financial closure terms set out by banks strictly mandate 80% land acquisition before the appointed date. While the environment is not quite conducive for easy project financing, the company is confident of achieving its required funding by leveraging its good track record.
- ▶ **Other highlights.**
 - Two HAM projects of SIPL namely Una-Kodinar and Rampur-Kathgodam have faced trouble in acquiring land in some stretches amounting to proportionate order portion of Rs700 mn-Rs1 bn. SIP is keen to avoid a reduction in project size due to de-scoping and corresponding reduction in annuities. To this end, the company has proposed to NHAI that it defer construction for corresponding sections to a time when the land acquisition is completed. In the meanwhile, construction of the rest of the project can progress and annuities as per the original project cost can be started with provisional completion certificate. NHAI is yet to concur with this proposal.
 - Gross equity requirement to be funded by SIPL for HAM projects stands at ~Rs10 bn, equally split over the next three years i.e. over FY2019-21.
 - Recent news reports suggest a proposal before MoRTH to reduce mandatory land acquisition requirement for highway project construction commencement to 50% (from the 80% mandated currently). However, the company believes that for HAM projects, lenders will still insist on 80% land acquisition. Further, in order to implement such a proposal, contract terms will need to be changed by the government to allow partial completion in case of persistent hurdles in completing land acquisition.

Exhibit 4: Internal accruals are more than enough to fund equity requirement of existing projects
Comparison of cash profits and equity requirement of SIPL, March fiscal year-ends (Rs bn)



Source: Company, Kotak Institutional Equities estimates

Exhibit 5: Change in estimates primarily on account of a change in guidance on tax rate as SEL now uses 35 AD instead of 80IA benefits
Change in estimates for Sadbhav Engineering, March fiscal year-ends, 2018-21E

	2018	New estimates			Old estimates			% revision		
		2019E	2020E	2021E	2019E	2020E	2021E	2019E	2020E	2021E
Profit model										
Order inflows	93,662	76,980	84,678	94,693	76,980	84,678	94,693	—	—	—
Total income	35,051	41,928	53,803	63,191	42,533	55,620	64,854	(1)	(3)	(3)
EBITDA	4,152	4,979	6,381	7,485	5,052	6,596	7,682	(1)	(3)	(3)
Net interest expense	(1,010)	(817)	(554)	(562)	(841)	(778)	(820)			
PBT	2,163	3,060	4,645	5,653	3,053	4,511	5,405	0	3	5
Tax	44	(153)	(836)	(1,743)	—	(1,391)	(1,684)			
PAT	2,207	2,907	3,809	3,909	3,053	3,120	3,721	(5)	22	5
EPS (Rs)	12.9	17.0	22.2	22.8	17.8	18.2	21.7			
Ratios										
Revenue growth (%)	5.6	19.6	28.3	17.4	21.3	30.8	16.6			
EBITDA margin (%)	11.8	11.9	11.9	11.8	11.9	11.9	11.8			
PAT margin (%)	6.3	6.9	7.1	6.2	7.2	5.6	5.7			
Tax rate (%)	(2.0)	5.0	18.0	30.8	28.9	30.8	31.2			
Net debt/equity (X)	0.8	0.5	0.5	0.4	0.6	0.6	0.5			
RoAE (%)	17.8	19.3	20.6	17.7	20.1	17.3	17.4			
RoACE (%)	12.7	14.2	15.7	14.3	14.9	13.7	14.2			

Source: Company, Kotak Institutional Equities estimates

Exhibit 6: Sum-of-the-parts valuation of Sadbhav Engineering

Business	Value (Rs mn)	Proportionate value (Rs mn)	Shareholding (%)	Per share (Rs)	Comments
EPC business	41,017	41,017	100	239	8X EV/EBITDA on two-year forward basis
Sadbhav Infrastructure Projects				231	FCFE valuation of projects
Operational projects	50,475	47,276	69	190	
Ahmedabad Ring Road	3,575	3,575			100% stake
Aurangabad-Jalna	4,548	4,548			100% stake
Nagpur-Seoni	(297)	(297)			100% stake
Dhule	3,602	3,602			100% stake
MBCPNL	17,701	15,911			89.7% stake
Rohtak-Panipat	2,047	2,047			100% stake
Hyderabad-Yadgiri	5,021	5,021			100% stake
Bijapur-Hungund	6,118	4,711			77% stake
Gomti ka Chauraha-Udaipur	5,850	5,850			100% stake
Rajsamand-Bhilwara	3,648	3,648			100% stake
Rohtak Hissar	(1,339)	(1,339)			100% stake
Under construction projects		1,195	69	5	
Karnataka State Highway project	1,615	1,195			74% stake
SIPL standalone operations+HAM operations	9,167	9,167	69	37	4X Mar-2020 EV/EBITDA
15% holding company discount for SIPL				(35)	
Total				436	

Source: Company, Kotak Institutional Equities estimates

Exhibit 7: Segmental numbers for Sadbhav Engg (standalone), March fiscal year-ends, 2012-21E (Rs mn)

	2012	2013	2014	2015	2016	2017	2018	2019E	2020E	2021E
Total standalone										
Order inflows	32,607	46,518	23,298	22,211	25,040	35,035	93,662	76,980	84,678	94,693
Yoy growth (%)	35.6	42.7	(49.9)	(4.7)	12.7	39.9	167.3	(17.8)	10.0	11.8
Revenues	26,706	18,039	23,523	29,621	31,816	33,134	35,493	41,928	53,803	63,191
Yoy growth (%)	20.9	(32.5)	30.4	25.9	7.4	4.1	7.1	18.1	28.3	17.4
Order backlog	75,541	104,020	89,410	82,000	74,873	76,834	132,493	167,545	198,420	229,922
Roads (BOT)										
Order inflows	20,042	20,545	125	1,834	1,264	33,033	62,096	37,257	40,983	45,081
Revenues	19,790	7,127	6,435	14,239	17,034	3,330	12,753	25,950	30,499	33,877
Yoy growth (%)	61.1	(64.0)	(9.7)	121.3	19.6	(80.5)	283.0	103.5	17.5	11.1
Order backlog	33,402	46,820	30,510	18,105	2,335	32,038	81,381	92,688	103,172	114,377
Roads (others)										
Order inflows	5,133	7,048	7,163	10,799	23,777	1,615	25,569	28,126	30,939	35,580
Yoy growth (%)	(66.5)	37.3	1.6	50.8	50.0	(93.2)	—	10.0	10.0	15.0
Revenues	2,616	5,655	10,663	6,064	5,229	22,056	17,130	11,645	17,380	22,112
Yoy growth (%)	(54.7)	116.2	88.6	(43.1)	(13.8)	321.8	(22.3)	(32.0)	49.2	27.2
Order backlog	20,587	21,980	15,089	19,824	38,372	17,931	26,370	42,852	56,411	69,879
Irrigation										
Order inflows	2,474	7,898	8,620	4,537	—	—	—	5,000	5,500	6,050
Yoy growth (%)	(43.7)	219.2	9.1	(47.4)	(50.0)	—	—	—	10.0	10.0
Revenues	2,106	2,856	2,861	4,060	5,359	4,580	2,851	1,584	2,409	3,166
Yoy growth (%)	68.0	35.6	0.2	41.9	32.0	(14.5)	(37.8)	(44.5)	52.1	31.4
Order backlog	9,958	15,000	19,670	20,146	14,419	9,899	4,539	7,955	11,046	13,930
Mining										
Order inflows	4,958	11,027	7,390	5,042	—	386	5,997	6,596	7,256	7,981
Yoy growth (%)	106.5	122.4	(33.0)	(31.8)	(60.0)	—	2,500.0	10.0	10.0	10.0
Revenues	2,194	2,401	3,565	5,258	4,194	3,168	2,759	2,750	3,515	4,036
Yoy growth (%)	(21.0)	9.4	48.5	47.5	(20.2)	(24.5)	(12.9)	(0.3)	27.8	14.8
Order backlog	11,594	20,220	24,141	23,925	19,748	16,966	20,204	24,050	27,791	31,736

Source: Company, Kotak Institutional Equities estimates

Exhibit 8: Financials of Sadbhav Engg (standalone), March fiscal year-ends, 2012-21E (Rs mn)

	2012	2013	2014	2015	2016	2017	2018	2019E	2020E	2021E
Profit model										
Total income	26,755	18,110	23,581	29,698	31,863	33,203	35,051	41,928	53,803	63,191
Expenses	(23,853)	(16,552)	(21,092)	(26,696)	(28,608)	(29,646)	(30,899)	(36,949)	(47,421)	(55,706)
EBITDA	2,903	1,558	2,489	3,002	3,254	3,556	4,152	4,979	6,381	7,485
Interest (expense)/income	(651)	(844)	(1,181)	(1,382)	(1,515)	(1,534)	(1,772)	(1,556)	(1,447)	(1,500)
Depreciation	(274)	(318)	(474)	(817)	(849)	(1,000)	(979)	(1,102)	(1,182)	(1,270)
Other income	108	103	369	655	905	875	762	739	893	938
Pretax profits	2,086	499	1,203	1,458	1,795	1,897	2,163	3,060	4,645	5,653
Tax	(681)	(166)	55	(346)	(405)	(18)	44	(153)	(836)	(1,743)
Adjusted net income	1,404	741	874	1,112	1,342	1,879	2,207	2,907	3,809	3,909
EPS (Rs)	9.3	4.9	5.8	7.1	7.8	11.0	12.9	17.0	22.2	22.8
Balance sheet										
Total equity	7,623	8,325	9,572	13,521	14,715	16,609	18,668	21,303	24,756	28,300
Deferred taxation liability	235	317	357	244	232	(477)	(994)	(994)	(994)	(994)
Total borrowings	4,488	7,630	10,257	10,963	12,166	15,183	14,840	13,340	13,840	14,340
Total liabilities and equity	12,346	16,272	20,186	24,728	27,112	31,316	32,514	33,649	37,602	41,645
Net fixed assets	2,881	3,303	4,982	5,357	5,550	5,229	5,028	4,704	4,378	4,049
Investments	3,323	5,385	5,210	5,313	5,278	5,694	5,775	5,278	5,278	5,278
Net current assets (excl. cash)	5,015	7,150	8,471	13,356	15,552	19,934	21,458	19,104	22,978	25,166
Cash	563	218	762	351	366	230	127	2,282	2,484	3,576
Total assets	12,346	16,272	20,186	24,728	27,113	31,316	32,514	33,649	37,602	41,645
Free cash flow										
Cash flow from operations	722	(293)	1,047	(1,163)	1,543	169	3,536	5,765	2,361	3,399
Cash flow from investing	(778)	(2,802)	(1,914)	(1,351)	(841)	(1,095)	(858)	(282)	(856)	(941)
Free cash flow	(56)	(3,095)	(866)	(2,514)	702	(927)	2,678	5,483	1,505	2,458
Ratios										
EBITDA margin (%)	10.8	8.6	10.6	10.1	10.2	10.7	11.8	11.9	11.9	11.8
PAT margin (%)	5.2	4.1	3.7	3.7	4.2	5.7	6.3	6.9	7.1	6.2
Net debt/equity (X)	0.5	0.9	1.0	0.8	0.8	0.9	0.8	0.5	0.5	0.4
RoAE (%)	30.5	22.5	18.5	13.2	13.9	17.3	17.8	19.3	20.6	17.7
RoACE (%)	22.7	13.0	12.8	11.8	11.4	12.1	12.7	14.2	15.7	14.3

Source: Company, Kotak Institutional Equities estimates

AUGUST 16, 2018

RESULT

Coverage view: **Attractive**

Price (₹): **138**

Target price (₹): **235**

BSE-30: **37,852**

Most factors in favor. (1) A large order backlog, (2) a relatively debt-free standalone balance sheet, (3) projects with land largely in hand and (4) a scalable business model with limited share of outsourcing, all are in favor of ASBL. We build in the benefits of recent project wins in financials now that financial terms of most have been finalized. The same drives a higher ₹235 target price (₹210 earlier). 1QFY19 was steady on EPC and toll revenues and weak on EPC margin largely due to a weak revenue mix. We expect margin to normalize as revenues scale up meaningfully in 2HFY19. Retain BUY.

Company data and valuation summary

Ashoka Buildcon

Stock data		Forecasts/Valuations			
		2018	2019E	2020E	
52-week range (Rs) (high,low)	197-117	EPS (Rs)	8.4	8.8	10.3
Market Cap. (Rs bn)	38.7	EPS growth (%)	34.6	4.1	17.8
Shareholding pattern (%)		P/E (X)	16.4	15.8	13.4
Promoters	54.0	Sales (Rs bn)	24.5	33.2	44.7
FIs	4.9	Net profits (Rs bn)	2.4	2.5	2.9
MFs	30.5	EBITDA (Rs bn)	2.9	3.9	5.1
Price performance (%)	1M 3M 12M	EV/EBITDA (X)	13.2	10.3	8.6
Absolute	(13.8) (22.8) 9.9	ROE (%)	13.0	11.8	12.3
Rel. to BSE-30	(16.7) (27.5) (8.7)	Div. Yield (%)	0.8	1.2	0.9

Stage set for a sharp scale-up in execution from 2HFY19

Of the five projects pending financial closure, four have seen finalization of terms at 80:20 debt to equity and 9.45% interest cost. While these projects coupled with other commitments would entail about ₹7 bn of equity requirements, the same would largely get funded by internal accruals of a growing EPC business with a debt-free standalone balance sheet. Such funding requirements may be front-ended given the nature of the agreement with lenders. Lenders too should be comfortable lending to these projects, with most projects already ahead or close to the 80% land acquisition requirement. ASBL sees limited issues to scaling up execution based on its bandwidth to handle projects and ability to scale up the same, evident in good revenue growth reported in FY2018 without increasing share of outsourcing.

Ordering backlog and bidding pipeline suggest good growth phase to last for long

Order backlog of ASBL at ₹108 bn provides a visibility of three years on one-year forward revenues, which builds in 35%+ yoy growth. In addition, ASBL expects to grow such backlog by another 20-30% in FY2019 as it targets ₹50-70 bn of new orders. The focus of improving prospects is concentrated in the roads space while other opportunities include CGD, railway electrification and state-level transmission orders. ASBL does not see meaningful opportunities for power distribution and real estate orders in the near term.

Factor in scale-up in revenues and recovery in margin from 2HFY19

Adjusted for the one-time gain on settlement of a claim, ASBL's EBITDA at ₹701 mn was marginally below our estimate. Higher-than-expected other income still led to an outperformance at PAT level. All key line items of revenue/EBITDA/PAT declined yoy on high base; we note high level of execution in 1QFY18 prior to advent of GST. Management expects standalone revenues to report a feeble 2QFY19 as well and then scale-up in revenues from 3QFY19 with start of recently won HAM projects and ToT order (>50% share of current backlog). Yoy comparable toll revenues at ₹2.4 bn grew ~11% yoy with largely broad-based growth across its roads portfolio. We build in the financial impact of recently won HAM projects and increase our SoTP to ₹235 from ₹210 previously. Retain BUY.

Aditya Mongia

Ajinkya Bhat

Exhibit 1: Adjusted for Rs115 mn of one-off income from claim settlement, EBITDA was in line with estimates; higher-than expected other income led to PAT outperformance

Ashoka Buildcon 1QFY19 results (standalone), March fiscal year-ends (Rs mn)

	1QFY19	1QFY19E	1QFY18	4QFY18	% change			FY2018	FY2017	% change	FY2019E	FY2018	% change
					vs est.	yoy	qoq						
Total sales	6,837	6,156	7,064	7,023	11	(3)	(3)	24,463	20,065	22	33,225	24,463	36
Expenses	(6,025)	(5,417)	(6,138)	(6,216)	11	(2)	(3)	(21,528)	(17,638)	22	(29,284)	(21,528)	36
RM / operating expenses	(5,473)		(5,612)	(5,731)		(2)		(19,524)	(15,992)	22	(26,562)	(19,524)	36
Employee benefit expenses	(308)		(269)	(279)		15		(1,067)	(745)	43	(1,449)	(1,067)	36
Other expenses	(244)		(258)	(206)		(5)		(938)	(901)	4	(1,273)	(938)	36
EBITDA	813	739	925	808	10	(12)	1	2,934	2,427	21	3,940	2,934	34
Other income	366	205	92	612	78	297	(40)	978	719	36	820	978	(16)
Interest	(171)	(131)	(129)	(113)	31	32	52	(485)	(474)	2	(720)	(485)	48
Depreciation	(136)	(156)	(113)	(144)	(13)	20	(6)	(532)	(507)	5	(707)	(532)	33
PBT	871	656	775	1,163	33	12	(25)	2,895	2,164	34	3,334	2,895	15
Tax	(232)	(144)	(205)	(108)	61	13	114	(524)	(403)	30	(867)	(524)	65
Net profit	639	512	570	1,054	25	12	(39)	2,370	1,761	35	2,467	2,370	4
Key ratios (%)													
Construction exp./ sales	80.0		79.4	81.6				79.8	79.7		79.9	79.8	
Staff cost/ sales	4.5		3.8	4.0				4.4	3.7		4.4	4.4	
Other exp./ sales	3.6		3.6	2.9				3.8	4.5		3.8	3.8	
EBITDA margin	11.9	12.0	13.1	11.5				12.0	12.1		11.9	12.0	
PBT margin	12.7	10.7	11.0	16.6				11.8	10.8		10.0	11.8	
Effective tax rate	26.7	22.0	26.5	9.3				18.1	18.6		26.0	18.1	
PAT margin	9.3	8.3	8.1	15.0				9.7	8.8		7.4	9.7	
EPS (Rs)	2.3	1.8	2.0	3.7				8.4	6.2		8.8	8.4	

Source: Company, Kotak Institutional Equities estimates

Exhibit 2: Traffic growth was steady at 7% for 1QFY19

Trajectory of toll collections for key BOT projects

Revenues (Rs mn)	1QFY17	2QFY17	Adj.	4QFY17	1QFY18	2QFY18	3QFY18	4QFY18	1QFY19
			3QFY17						
Quarterly collections									
Bhandara	155	146	148	153	156	150	168	174	167
Durg	189	179	184	193	190	185	202	207	195
Jaora-Nayagaon	407	425	452	467	474	503	530	523	516
Indore Edlabad (ABL)	351	303	293	164	-	-	-	-	-
Belgaum Dharwad	186	178	188	192	214	208	231	224	230
Pimpalgaon – Nasik – Gonde	-	-	-	-	-	-	-	-	-
Sambalpur Baragarh	117	123	129	141	145	141	166	180	180
Dhankuni- Kharagpur	659	651	638	735	786	757	783	849	893
Total	2,064	2,004	2,032	2,044	1,966	1,944	2,080	2,158	2,181
Revenue growth (%)									
Bhandara	9.1	8.7	(3.7)	(5.7)	0.9	3.0	13.2	13.9	6.8
Durg	5.7	6.2	(2.5)	(2.1)	0.5	3.3	9.8	7.2	2.5
Jaora-Nayagaon	6.9	3.4	2.8	14.9	16.3	18.2	17.2	12.1	9.1
Indore Edlabad	8.0	0.9	(3.1)	NA	NA	NA	NA	NA	NA
Belgaum Dharwad	4.3	6.7	10.0	7.3	15.2	16.9	22.6	16.6	7.2
Pimpalgaon – Nasik – Gonde	NA								
Sambalpur Baragarh	15.7	27.3	19.3	12.6	23.7	15.1	28.7	28.2	23.9
Dhankuni- Kharagpur	12.6	15.8	6.8	9.8	19.3	16.3	22.8	15.6	13.6
Tariff hike (%)									
Bhandara	2.0	2.0	(2.5)	(2.5)	(2.5)	(2.5)	(2.5)	(2.5)	(2.5)
Durg	2.0	2.0	(2.5)	(2.5)	(2.5)	(2.5)	(2.5)	(2.5)	(2.5)
Jaora-Nayagaon	7.0	7.0	7.0	7.0	7.0	7.0	7.0	7.0	7.0
Indore Edlabad	7.0	7.0	7.0	7.0	7.0	7.0	7.0	7.0	7.0
Belgaum Dharwad	1.9	1.9	1.9	1.9	4.3	4.3	4.3	4.3	4.3
Pimpalgaon – Nasik – Gonde	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5
Sambalpur Baragarh	1.9	1.9	1.9	1.9	4.3	4.3	4.3	4.3	4.3
Dhankuni- Kharagpur	1.9	1.9	1.9	1.9	4.3	4.3	4.3	4.3	4.3
Total									
Traffic growth (%)									
Bhandara	7.0	6.5	(1.2)	(3.3)	3.4	5.6	16.1	16.8	9.5
Durg	3.6	4.1	(0.1)	0.4	3.1	5.9	12.6	10.0	5.1
Jaora-Nayagaon	(0.1)	(3.4)	(3.9)	7.4	8.7	10.5	9.5	4.8	1.9
Indore Edlabad	0.9	(5.7)	(9.5)	NA	NA	NA	NA	NA	NA
Belgaum Dharwad	2.4	4.7	8.0	5.3	10.5	12.1	17.5	11.8	2.8
Pimpalgaon – Nasik – Gonde	NA								
Sambalpur Baragarh	13.6	24.9	17.1	10.5	18.6	10.4	23.4	22.9	18.8
Dhankuni- Kharagpur	10.6	13.6	4.9	7.8	14.4	11.5	17.8	10.9	8.9
Total	6.3	7.7	2.8	6.0	10.9	10.3	15.5	10.9	7.1

Source: Company, Kotak Institutional Equities

Exhibit 3: Segmental break-up of standalone financials of Ashoka Buildcon, March fiscal year-ends, 2016-21E (Rs mn)

	2016	2017	2018	2019E	2020E	2021E
Total						
Order inflows	28,250	39,255	11,534	90,000	50,000	60,000
Order backlog	41,110	70,047	58,488	117,221	124,372	137,370
Revenues	19,541	20,065	24,463	33,225	44,748	49,067
Yoy growth (%)	(1)	3	22	36	35	10
EBITDA	2,494	3,046	2,695	3,940	5,059	5,519
Yoy growth (%)	(0)	22	(12)	46	28	9
EBITDA margin (%)	12.8	15.2	11.0	11.9	11.3	11.2
Roads						
Order inflows	28,250	23,358	9,702	70,000	30,000	36,000
Order backlog	32,910	51,949	42,558	91,663	93,037	99,369
Revenues	8,955	11,142	19,093	20,895	28,626	29,668
EBITDA	1,164	1,248	2,138	2,340	3,206	3,323
EBITDA margin (%)	13.0	11.2	11.2	11.2	11.2	11.2
Power T&D						
Order inflows	0	15,897	1,832	20,000	20,000	24,000
Order backlog	8,200	18,098	15,930	25,558	31,335	38,001
Revenues	9,230	5,999	4,000	10,372	14,223	17,334
EBITDA	1,015	660	420	1,089	1,493	1,820
EBITDA margin (%)	11.0	11.0	10.5	10.5	10.5	10.5
Sales						
Revenues	1,100	1,715	1,370	1,507	1,658	1,823
EBITDA	110	172	137	151	166	182
EBITDA margin (%)	10.0	10.0	10.0	10.0	10.0	10.0
BOT						
Revenues	256	1,209	-	450	242	242
EBITDA	205	967	-	360	194	194
EBITDA margin (%)	80.0	80.0	-	80.0	80.0	80.0

Source: Company, Kotak Institutional Equities

Exhibit 4: The large change in estimates is driven by large EPC orders won recently and related financial impact of funding; the same is not reflective of change in SoTP

Revision in estimates for Ashoka Buildcon standalone, March fiscal year-ends, 2018-21E (Rs mn)

	New estimates				Old estimates			% revision		
	2018	2019E	2020E	2021E	2019E	2020E	2021E	2019E	2020E	2021E
Income statement										
New orders	11,534	90,000	50,000	60,000	39,865	47,238	56,086	126	6	7
Yoy growth (%)	(70.6)	680.3	(44.4)	20.0	27.1	18.5	18.7			
Net revenue	24,463	33,225	44,748	49,067	31,389	37,044	41,639	6	21	18
Yoy growth (%)	21.9	35.8	34.7	9.7	25.9	18.0	12.4			
EBITDA	2,934	3,940	5,059	5,519	3,760	4,228	4,753	5	20	16
EBITDA margin (%)	12.0	11.9	11.3	11.2	12.0	11.4	11.4	-12 bps	-11 bps	-17 bps
Interest & finance charges	(485)	(720)	(895)	(981)	(173)	2	324			
Depreciation	(532)	(707)	(839)	(983)	(632)	(695)	(758)			
PBT	2,895	3,334	4,153	4,389	3,749	4,533	5,317	(11)	(8)	(17)
Tax	(524)	(867)	(1,246)	(1,519)	(937)	(1,360)	(1,595)			
PAT	2,370	2,467	2,907	2,870	2,812	3,173	3,722	(12)	(8)	(23)
EPS (Rs)	8.4	8.8	10.3	10.2	10.0	11.3	13.2	(12)	(8)	(23)

Source: Company, Kotak Institutional Equities estimates

Exhibit 5: SoTP break-up of Ashoka Buildcon

	Value (Rs mn)	Stake (%)	Proportional value (Rs mn)	Per share value (Rs)	Methodology
Ashoka Concession Limited (ACL)		76	28,447	101	
Bhandara	476	51	148	1	Mar-19 FCFE valuation
Durg	1,693	51	527	2	Mar-19 FCFE valuation
Jaora - Nayagaon	19,379	38	4,457	16	Mar-19 FCFE valuation
Belgaum Dharwad	5,469	100	3,336	12	Mar-19 FCFE valuation
Pimpalgaon-Nasik-Gonde	1,288	26	204	1	Average of FCFE valuation and claim on NHAI
Sambalpur Baragarh	3,217	100	1,962	7	Mar-19 FCFE valuation
Dhankuni- Kharagpur	11,546	100	7,043	25	Mar-19 FCFE valuation
Projects with no equity contribution from Macquarie					
Chennai ORR	4,909	50	2,455	9	Mar-19 FCFE valuation
KSHIP-II	729	100	380	1	Mar-19 FCFE valuation
Bagewadi Saundatti	215	100	215	1	Mar-19 FCFE valuation less investment
Hungund Talikot	134	100	134	0	Mar-19 FCFE valuation less investment
Kharar Ludhiana	2,065	100	2,065	7	Mar-19 FCFE valuation less investment
Ranastalam to Anandpuram	850	100	850	3	Mar-19 FCFE valuation less investment
Khairatunda - Barwa Adda	778	100	778	3	Mar-19 FCFE valuation less investment
Belgaum-Khanapur	859	100	859	3	Mar-19 FCFE valuation less investment
Tumkur-Shivamoga package I	376	100	380	1	Mar-19 FCFE valuation less investment
Tumkur-Shivamoga package II	685	100	699	2	Mar-19 FCFE valuation less investment
Vadodara Kim expressway Phase 1A pac	1,899	100	1,956	7	Mar-19 FCFE valuation less investment
Less value to make good 12% IRR ⁽¹⁾			(3,237)	(11)	Mar-19E valuation
Core construction business	29,785	100	29,785	106	6X Mar-20E EBITDA less debt
Value of ABL projects			8,171	29	
ABL asset portfolio	2,347	100	2,347	8	NPV of remaining year EBITDA less debt
Jaora - Nayagaon	19,379	36	5,824	21	Mar-19 FCFE valuation
Other investments	2,848	100	3,198	11	
Land investments	2,251	100	2,601	9	1X investments
Other investments	597	100	597	2	1X investments
Total			66,363	236	

Source: Company, Kotak Institutional Equities estimates

Exhibit 6: Standalone financial snapshot of Ashoka Buildcon, March fiscal year-ends, 2012-21E (Rs mn)

	2012	2013	2014	2015	2016	2017	2018	2019E	2020E	2021E
Profit model										
Total sales	13,380	16,376	15,566	19,667	19,378	20,065	24,463	33,225	44,748	49,067
Expenditure	(11,445)	(14,354)	(13,582)	(17,169)	(16,881)	(17,638)	(21,528)	(29,284)	(39,690)	(43,548)
Operating expenses	(10,797)	(13,489)	(12,726)	(16,075)	(15,580)	(15,992)	(19,524)	(26,562)	(36,023)	(39,528)
Employee cost	(372)	(431)	(492)	(614)	(730)	(745)	(1,067)	(1,449)	(1,951)	(2,140)
Other expenses	(276)	(434)	(365)	(481)	(571)	(901)	(938)	(1,273)	(1,715)	(1,880)
EBITDA	1,935	2,022	1,984	2,498	2,498	2,427	2,934	3,940	5,059	5,519
PBT	1,369	1,711	1,690	1,939	2,125	2,164	2,895	3,334	4,153	4,389
Tax	(325)	(533)	(499)	(517)	(644)	(403)	(524)	(867)	(1,246)	(1,519)
PAT	1,045	1,178	1,191	1,422	1,481	1,761	2,370	2,467	2,907	2,870
Weighted diluted number of shares	282	282	282	282	282	282	282	282	282	282
EPS based on diluted shares (Rs)	3.7	4.2	4.2	5.0	5.3	6.2	8.4	8.8	10.3	10.2
Balance sheet										
Shareholders funds	7,817	8,539	9,328	10,543	16,958	17,228	19,263	22,454	24,928	27,371
Share capital	552	527	790	793	936	936	936	936	936	936
Reserves & surplus	7,264	8,013	8,538	9,750	16,022	16,292	18,327	21,518	23,993	26,435
Loan funds	3,122	2,733	2,240	4,447	2,631	1,768	1,251	3,049	5,915	6,385
Deferred tax liabilities (net)	10	(7)	(20)	(99)	(199)	(304)	(350)	(350)	(350)	(350)
Total sources of funds	10,949	11,265	11,547	14,891	19,390	18,692	20,164	25,153	30,494	33,406
Net fixed assets	2,728	2,416	2,267	1,871	1,548	1,847	2,324	3,815	4,627	5,458
Investments	4,424	7,454	9,757	10,904	12,300	13,065	13,182	15,569	18,986	20,650
Cash & bank balances	386	338	305	256	274	638	1,235	1,235	1,235	1,235
Net current assets (excl. cash)	3,412	1,057	(782)	1,861	5,268	3,142	3,424	4,535	5,647	6,064
Total application of funds	10,949	11,265	11,547	14,891	19,390	18,692	20,165	25,153	30,494	33,406
Cash flow statement										
Cash flow from operating activities										
Operating profit before working capital changes	2,161	2,332	2,055	2,772	2,939	2,941	3,707	4,555	5,682	6,148
Adjustments for working capital changes	912	2,345	1,803	(3,030)	(5,787)	2,125	(282)	(1,111)	(1,112)	(417)
Income tax paid	(310)	(453)	(478)	(489)	(696)	(508)	(570)	(867)	(1,246)	(1,519)
Net cash flow from operating activities	2,763	4,271	3,380	(747)	(3,544)	4,558	2,855	2,578	3,324	4,213
Purchase of fixed assets	(430)	(517)	(367)	(199)	(314)	(700)	(1,700)	(1,500)	(1,650)	(1,815)
Purchase of non-current investments	(1,522)	(2,789)	(2,306)	(1,014)	(360)	(765)	(117)	(2,387)	(3,417)	(1,664)
Net cash flow from investing activities	(1,871)	(3,243)	(2,337)	(913)	(167)	(1,260)	(1,612)	(3,681)	(4,862)	(3,274)
FCF	890	1,026	1,039	(1,660)	(3,740)	3,298	1,243	(1,103)	(1,539)	939
Growth (%)										
Revenue growth	11.9	22.4	(4.9)	26.3	(1.5)	3.5	21.9	35.8	34.7	9.7
EBITDA growth	18.6	4.5	(1.9)	25.9	0.0	(2.8)	20.9	34.3	28.4	9.1
Recurring PAT growth	23.3	12.8	1.1	19.4	4.1	18.9	34.6	4.1	17.8	(1.3)
Key ratios										
EBITDA margin (%)	14.5	12.3	12.7	12.7	12.9	12.1	12.0	11.9	11.3	11.2
PAT margin (%)	7.8	7.2	7.7	7.2	7.6	8.8	9.7	7.4	6.5	5.8
Net debt to equity (X)	0.4	0.3	0.2	0.4	0.1	0.1	0.0	0.1	0.2	0.2
ROE (%)	14.1	14.4	13.3	14.3	10.8	10.3	13.0	11.8	12.3	11.0
ROCE (%)	14.7	13.7	13.6	14.7	10.7	10.1	12.4	14.3	15.2	14.2

Source: Company, Kotak Institutional Equities estimates

AUGUST 16, 2018

RESULT

Coverage view: **Cautious**

Price (₹): **111**

Target price (₹): **118**

BSE-30: **37,852**

Volumes good, margins weak. EBITDA of Rs1.6 bn (-16% yoy) was higher than our estimate led by volume growth of 16% yoy aided by improved demand in the South even though EBITDA/ton declined 27% yoy on weak realization. The company's debt over last 2-3 years remains largely unchanged despite lower capex spends. The capex spends, however, may rise as company will likely pursue expansion projects given plant utilization of ~80%. We revise our TP to Rs118 (Rs135 earlier) and maintain REDUCE.

Company data and valuation summary

India Cements

Stock data

52-week range (Rs) (high,low)	206-97
Market Cap. (Rs bn)	34.3

Shareholding pattern (%)

Promoters	28.2
FIs	18.7
MFs	22.4

Price performance (%)	1M	3M	12M
Absolute	3.7	(18.5)	(39.9)
Rel. to BSE-30	0.2	(23.4)	(50.1)

Forecasts/Valuations

	2018	2019E	2020E
EPS (Rs)	3.3	4.2	8.5
EPS growth (%)	(42.5)	28.0	102.6
P/E (X)	33.9	26.5	13.1
Sales (Rs bn)	53.4	57.4	63.7
Net profits (Rs bn)	1.0	1.3	2.6
EBITDA (Rs bn)	6.9	7.6	9.4
EV/EBITDA (X)	9.5	8.6	6.7
ROE (%)	2.0	2.5	4.8
Div. Yield (%)	0.9	0.9	0.9

1QFY19 earnings—strong volume growth at 16% yoy, but operating margins subdued

ICEM earnings were higher than our estimate—the company reported revenues of Rs13.6 bn (+5% yoy, -3% qoq), EBITDA of Rs1.6 bn (-16% yoy, -2% qoq) and net-income of Rs210 mn (-20% yoy, -40% qoq), against our estimate of Rs13.2 bn, Rs1.4 bn and Rs54 mn, respectively. The earnings beat was led by better-than-expected volume growth of 16% yoy to 3.1 mn tons during the quarter. The company attributes higher volumes to improved demand in the Southern states mainly from infrastructure activity pick-up.

EBITDA/ton declined 27% yoy to Rs508/ton (-2% qoq) due to the decline in realizations by 9% yoy to Rs4,425/ton (-2% qoq)—as per company, the impact of lower realization was close to Rs1 bn in profitability. The variable cost rose by 5% yoy during the quarter and profitability could have been weaker but for rationalization in fixed costs—total costs declined by 6% yoy to Rs3,920/ton led by a decline in fixed costs, especially for manpower, selling & overheads.

Company: demand was up 20% yoy in South during the quarter

ICEM management highlighted the rise in cement demand by 20% yoy during the quarter in the Southern region aided by the infrastructure push in Andhra-Pradesh/Telangana and a lifting of the sand mining ban in Tamil Nadu. The management believes plant utilization can be close to maximum capacity by 4QFY19 if demand pull from infrastructure remains strong, and is hopeful that cement prices in South would improve thereon. As incremental volumes have been easier to place, ICEM is restricting its volumes above certain prices.

We note that all-India cement demand increased by 14% yoy in 1QFY19, as per DIPP data. However, we note that this growth is off a low base as demand declined by 3% yoy in 1QFY18—the two year CAGR for 1Q works out to 5% for all-India demand. Most cement companies in the quarter have reported a pick-up in cement offtake from the infrastructure sector though there does not appear to similar pick-up from the housing sector yet.

We maintain a REDUCE rating with a revised target price of Rs118 (Rs135 earlier)

Cement prices in the South have been weak compared to last year despite improved demand even as cost pressures rise (Exhibit 4). We cut our EBITDA estimate for ICEM by 4-5% for FY2019-2020E on realization assumption. Our estimates still factor EBITDA/ton improving to Rs716 in FY2020E from Rs508/ton in 1QFY19. We maintain REDUCE with a revised TP of Rs118 (Rs135 earlier).

Abhishek Poddar

Murtuza Arsiwalla

Samrat Verma

Exhibit 1: India Cements reported 16% yoy volume aided by improved demand in Southern states; EBITDA/ton remains muted
Interim results for India Cements (standalone), March fiscal year-ends, 2017-2019E (Rs mn)

	1QFY19	1QFY19E	1QFY18	4QFY18	(% Chg.)			FY2019E	FY2018 (% chg.)	
					KIE	yoy	qoq			
Net sales	13,607	13,189	12,901	13,978	3	5	(3)	57,427	53,407	8
Raw materials	(2,335)	(2,366)	(2,269)	(2,470)				(10,348)	(9,416)	
Employee costs	(938)	(1,023)	(1,147)	(996)				(4,017)	(3,971)	
Power & fuel costs	(4,004)	(3,345)	(2,858)	(3,492)				(14,173)	(12,389)	
Freight costs	(3,217)	(3,127)	(2,847)	(3,315)				(13,778)	(11,940)	
Other costs	(1,552)	(1,904)	(1,923)	(2,119)				(7,464)	(8,764)	
Expenditure	(12,046)	(11,765)	(11,045)	(12,393)	2	9	(3)	(49,779)	(46,479)	
EBITDA	1,561	1,424	1,856	1,585	10	(16)	(2)	7,648	6,928	10
EBITDA (%)	11	11	14	11				13	13	
Other income	55	53	52	39				194	194	
Interest	(733)	(725)	(874)	(718)				(3,402)	(3,402)	
Depreciation	(616)	(671)	(630)	(664)				(2,601)	(2,559)	
Pre-tax profits	267	81	404	242				1,840	1,161	
Tax	(57)	(27)	(140)	110				(552)	(155)	
Net income	210	54	264	353	286	(20)	(40)	1,288	1,006	28
Extraordinaries	—	—	—	—				—	—	
Reported net income	210	54	264	353	286	(20)	(40)	1,288	1,006	28
Tax rate (%)	21	33	35	(46)				30	13	
EPS (Rs)	0.7	0.2	0.9	1.1				4.2	3.3	
Key operating parameters										
Despatch ('000 tons)	3,075	2,868	2,656	3,087	7	16	(0)	12,320	11,170	10
Realization (Rs/ton)	4,425	4,598	4,857	4,528	(4)	(9)	(2)	4,661	4,781	(3)
Profitability (Rs/ton)	508	497	699	514	2	(27)	(1)	621	620	0

Source: Company, Kotak Institutional Equities estimates

Changes in our estimates

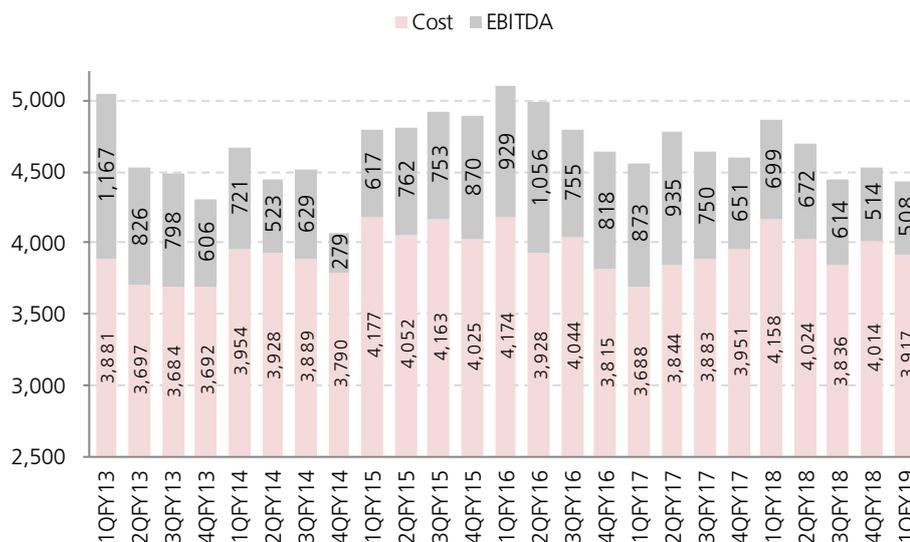
Exhibit 3 highlights key changes in our estimates.

We raise our volume assumption by 2% to 12.3 mn tons, 13.2 mn tons and 14.2 mn tons for FY2019E, FY2020E and FY2021E. We also tweak our realization & cost assumptions, resulting in a 6-7% cut in our EBITDA/ton estimates to Rs621, Rs716 and Rs742 for FY2019E, FY2020E and FY2021E. Our EBITDA estimate is cut by 4-5% to Rs7.6 bn, Rs9.4 bn and Rs10.5 bn for FY2019E, FY2020E and FY2021E. We estimate EPS of Rs4.2, Rs8.5 and Rs12 for FY2019E, FY2020E and FY2021E.

Key highlights of results

- ▶ **Costs declined due to lower fixed expenses in 1QFY19.** ICEM's costs declined by 2% qoq to Rs3,917/ton. The cost decline was on the back of a 20% qoq decline in fixed costs (employees, other expenses), which the management attributed to (1) lower repairs cost, (2) lower advertising spends, and (3) lower travel costs, etc.
- ▶ **Capex guidance of Rs1.5-2 bn for FY2019.** The company's capital expenditure for FY2019E will be close to Rs1.5-2 bn and will largely be on sustenance projects. The management highlighted that it will decide on plans to pursue new capacity additions in next few quarter based how demand pans out.
- ▶ **Debt increases due to higher working capital.** ICEM's gross debt increased by Rs1.6 bn from March 2018 to Rs32.9 bn due to the increase in working capital---they expect working capital increases to be reversed this year. The company will repay Rs1.9 bn during the year.
- ▶ **Trade and non-trade sales.** The company had trade sales of 60% while PPC sales accounted for 60% during the quarter.

Exhibit 2: ICEM's profitability under pressure due to subdued realizations and cost pressure
EBITDA/ton and Cost/ton for India Cements, 2013-2018 (Rs/ton)



Source: Industry, Kotak Institutional Equities estimates

Exhibit 3: Change in estimates for India Cements, March fiscal year-ends (Rs mn)

	Revised estimate			Previous estimate			Change (%)		
	2019E	2020E	2021E	2019E	2020E	2021E	2019E	2020E	2021E
Volume and realizations (mn tons, Rs/ton)									
Cement sales (mn tons)	12.3	13.2	14.2	12.0	12.9	13.8	2	2	2
EBITDA (Rs/ton)	621	716	742	669	765	792	(7)	(6)	(6)
Earnings estimates (Rs mn)									
Revenues	57,427	63,688	69,882	59,012	65,333	71,617	(3)	(3)	(2)
EBITDA	7,648	9,441	10,513	8,054	9,855	10,972	(5)	(4)	(4)
PAT	1,288	2,609	3,687	1,572	2,898	4,008	(18)	(10)	(8)
EPS	4.2	8.5	12.0	5.1	9.4	13.0	(18)	(10)	(8)

Source: Kotak Institutional Equities estimates

Exhibit 4: Cement prices in the South has been weak compared to last year

Region wise monthly average cement prices (Rs per 50kg bag)

(Rs/bag)	Jun-17	Jul-17	Aug-17	Sep-17	Oct-17	Nov-17	Dec-17	Jan-18	Feb-18	Mar-18	Apr-18	May-18	Jun-18	Jul-18	Aug-18
Andhra Pradesh	330	345	318	333	310	298	298	320	303	285	316	335	310	313	315
Karnataka	400	385	370	370	370	360	360	360	370	350	370	360	340	340	340
Kerala	398	390	398	368	373	353	363	385	345	363	373	355	355	388	364
Tamil Nadu	375	390	405	385	360	340	340	365	390	365	350	375	380	366	366
South	368	375	370	363	348	332	333	352	353	337	346	357	347	347	345
Change mom (Rs/bag)															
Andhra Pradesh	(25)	15	(28)	15	(23)	(13)	—	23	(18)	(18)	31	19	(25)	3	3
Karnataka	—	(15)	(15)	—	—	(10)	—	—	10	(20)	20	(10)	(20)	—	—
Kerala	(15)	(8)	8	(30)	5	(20)	10	23	(40)	18	10	(18)	—	33	(24)
Tamil Nadu	(5)	15	15	(20)	(25)	(20)	—	25	25	(25)	(15)	25	5	(14)	—
South	(12)	6	(5)	(6)	(16)	(16)	1	19	1	(17)	9	11	(10)	(0)	(2)

Source: Industry, Kotak Institutional Equities estimates

Exhibit 5: Our estimates factor a buoyant recovery in volumes led by strong demand from AP/Telangana region
Key standalone financial metrics and operating assumptions, March fiscal year-ends, 2016-21E (Rs mn)

	2016	2017	2018	2019E	2020E	2021E	Growth (%)			
							2018	2019E	2020E	2021E
Key Standalone financials (Rs mn)										
Revenue	42,268	50,795	53,407	57,427	63,688	69,882	5	8	11	10
EBITDA	7,754	8,610	6,928	7,648	9,441	10,513	(20)	10	23	11
PAT	1,495	1,749	1,006	1,288	2,609	3,687	(42)	28	103	41
Key operating metrics										
Volumes (mn tons)	8.7	11.0	11.2	12.3	13.2	14.2	1	10	7	8
Realization (Rs/ton)	4,871	4,601	4,781	4,661	4,831	4,931	4	(3)	4	2
Operating cost (Rs/ton)	3,977	3,821	4,161	4,041	4,115	4,189	9	(3)	2	2
Profitability (Rs/ton)	894	780	620	621	716	742	(20)	0	15	4

Source: Company, Kotak Institutional Equities estimates

Exhibit 6: We cut our TP of India Cements to Rs118/share (Rs135 earlier)
Valuation of India Cements based on March 2020E financials

Valuation	(Rs mn)	Multiple	EV	(Rs/share)
		(X)	(Rs mn)	
EBITDA (Rs mn)	9,441	7	65,805	214
Net-debt (Rs mn)			(29,321)	(95)
Equity value (Rs mn)			36,484	118
TP (Rs/share)				118

Source: Kotak Institutional Equities estimates

Exhibit 7: Profit model, balance sheet, cash model of India Cements, March fiscal year-ends, 2016-21E (Rs mn)

	2016	2017	2018	2019E	2020E	2021E
Profit model (Rs mn)						
Net sales	42,268	50,795	53,407	57,427	63,688	69,882
EBITDA	7,754	8,610	6,928	7,648	9,441	10,513
Other income	222	165	194	194	194	194
Interest	(3,661)	(3,589)	(3,402)	(3,402)	(3,241)	(2,705)
Depreciation	(2,195)	(2,571)	(2,559)	(2,601)	(2,668)	(2,735)
Extraordinary item	(196)	(16)	—	—	—	—
Profit before tax	1,924	2,600	1,161	1,840	3,727	5,267
Current tax	(333)	-	(179)	(460)	(932)	(1,317)
Deferred tax	(292)	(867)	24	(92)	(186)	(263)
Reported net income	1,299	1,734	1,006	1,288	2,609	3,687
Adjusted PAT	1,495	1,749	1,006	1,288	2,609	3,687
Earnings per share (Rs)	4.9	5.7	3.3	4.2	8.5	12.0
Balance sheet (Rs mn)						
Equity	49,809	51,099	52,003	52,920	55,158	58,474
Deferred tax liability	5,719	6,556	6,532	6,624	6,811	7,074
Borrowings	31,549	29,213	31,728	31,728	30,228	25,228
Current liabilities	16,544	19,584	16,994	17,216	19,040	20,845
Total liabilities	103,622	106,453	107,258	108,489	111,237	111,622
Fixed assets	72,750	71,007	69,675	69,075	68,407	67,672
Investments	5,507	6,190	5,884	5,884	5,884	5,884
Cash	67	68	84	412	908	416
Other current assets	25,298	29,188	31,615	33,119	36,039	37,650
Total assets	103,622	106,453	107,258	108,489	111,237	111,622
Free cash flow (Rs mn)						
Operating cash flow excl. working capital	3,541	3,835	4,118	3,980	5,463	6,685
Working capital changes	766	114	(5,018)	(1,281)	(1,096)	194
Capital expenditure	(1,632)	(969)	(1,228)	(2,000)	(2,000)	(2,000)
Free cash flow	2,675	2,979	(2,128)	699	2,367	4,879
Ratios						
Book value (Rs/share)	162	166	169	172	179	190
RoAE (%)	3.5	3.5	2.0	2.5	4.8	6.5
RoACE (%)	5.0	5.0	4.6	4.2	5.6	6.4

Source: Company, Kotak Institutional Equities estimates

AUGUST 16, 2018
UPDATE

Coverage view: **Attractive**

Price (₹): **332**

Target price (₹): **400**

BSE-30: **37,852**

Revitalizing the bank. Our key takeaways from a meeting with Mr. Sandeep Bakshi, COO of ICICI Bank: (1) growth in operating profits to be a key focus area while declining provisions would aid RoE improvement, (2) granularity of loan book continues, (3) lumpy loan impairment looks unlikely, (4) no rationale to make serious intervention on human resources. Our hypothesis that ICICI Bank would be a key re-rating bank remains unchanged. Maintain BUY (TP unchanged).

Company data and valuation summary

ICICI Bank

Stock data		Forecasts/Valuations			
		2018	2019E	2020E	
52-week range (Rs) (high,low)	366-255	EPS (Rs)	10.5	8.5	26.2
Market Cap. (Rs bn)	2,138.6	EPS growth (%)	(31.1)	(19.6)	209.1
Shareholding pattern (%)		P/E (X)	31.5	39.2	12.7
Promoters	0.0	NII (Rs bn)	230.3	252.9	290.6
FIs	60.6	Net profits (Rs bn)	67.8	54.5	168.4
MFs	17.2	BVPS	130.1	147.6	176.0
Price performance (%)		P/B (X)	2.6	2.3	1.9
Absolute	1M 24.2 3M 7.2 12M 13.9	ROE (%)	6.6	5.1	14.5
Rel. to BSE-30	19.9 0.7 (5.3)	Div. Yield (%)	0.5	0.5	1.6

Acknowledging the challenges is a battle that is half won

In a wide ranging discussion we came back with a lot of positives from our meeting with the COO which includes: (1) most of the challenges are known, recognized in the past two years and provisions are being increased, a process that would mostly end by FY2019, (2) focus has now shifted to growth, better underwriting with granularity, (3) looking to energize the bank as it has a superior liability franchise and a strong manpower to rebuild the organization to a position of strength. The COO felt that the organization can change for the better with minimalistic intervention as changes required are mostly around removing the pro-cyclicality of the business model, which the bank has faced in the past decade. We believe that the steps taken by the COO are positive and would improve the RoEs in the long term. The COO was quite keen to address the long-term underperformance of the bank as compared to peers.

Focus on operating profit and decline in provisions

A key recurring point in our discussion was the focus on (1) operating profits which would be led by loan growth that would be granular and reasonably well balanced between retail and corporate and (2) decline in provisions in the medium term. There was less attention given to market share or funding to greenfield projects. The bank was a lot more comfortable in refinancing post completion. Greater attention is being given to its retail/SME business and focus would be to increase customer penetration with higher cross sell. Provisions, on the other hand would decline in the next few quarters as ageing provisions would improve coverage while resolutions and transition to Ind-AS should see this exercise being completed by 4QFY19.

ICICI Bank remains the best re-rating candidate in our portfolio

We have long argued that the asset quality concern is getting addressed and the street has under estimated the strength of the liability franchise. The approach taken by the COO is more driven by identifying a framework to operate the business with the belief that it would take the firm on the path to better long-term value creation. Rather than taking a very disruptive approach towards changes, the COO has taken a softer approach of backing a majority of his existing team and showing his confidence to achieve the desired outcomes. The steps taken by the firm seems to be commonsensical at this point. We maintain our BUY rating on the bank (TP unchanged), our top pick in the sector.

M B Mahesh CFA

Nischint Chawathe

Dipanjan Ghosh

Key takeaways from the discussion

- ▶ **Asset quality.** The bank has substantially improved its disclosure in the current quarter by giving the rating profile of its loan portfolio. The objective of giving the granularity of the “BB and below” book was to address the possible slippages from this portfolio and the granularity outside the earlier drill down list. The management highlighted that is not too material and any sharp negative surprises look unlikely.

The internal rating profile of companies is a lot more stringent and a notch or two lower as compared to external credit ratings and hence they may not be strictly comparable across other banks or rating agencies. There would be lower downward movement from “BBB” and possibility of some “BB and below” to be upgraded as well in the coming few quarters. The management indicated trends over the next few quarters would help give comfort. Slippages are likely to be driven mostly from the “drill down list” that the management has already disclosed. Small ticket slippages are under control and there is no serious risk emanating from this book at this point.

While the bank has a broad outlook on credit costs, the bank is still not giving a firm direction on the trajectory of these provisions over the next few quarters. Suffice to say that the bulk of the provisioning would be completed in FY2019 and any final adjustments would be done to net worth when the Ind-AS implementation begins in 1QFY20. Provisions are harder to give a clear outlook for the next few quarters as a lot of it is being driven by ageing related provisions where there is a substantial jump in provisions as these assets move towards harder buckets like “doubtful 2 and 3”.

- ▶ **Focus on operating profits.** There is a clear communication to the team to focus on operating profits. This would be a function of loan growth, better pricing and opportunities to cross-sell.
 - **Not much of a change in loan portfolio.** Broadly looking to keep the loan mix closer to current levels and any changes would be a big deviation from current levels. Retail mix is likely to move in a band of 55-65% of the overall loans. Business focus would need to see greater balance between consumer interests and the bank. This would ensure lower friction and better value. Within retail, the bank is focused on increasing geographical penetration and greater cross sell of products. On the corporate side, there is no focus on greenfield projects and any opportunity in project financing would be to refinance completed projects. The bank’s cost of funds allows them to be extremely competitive as compared to the best of their peers. Working capital loans would continue to remain a mainstay source of growth. Credit information bureaus and data analytics has significantly improved the credit origination process in retail and CLIRIC/IBC is likely to see something similar happening to the corporate loan segment.
 - **Loan pricing and threshold returns.** The bank believes that the recent underwriting of loans is meeting their internal threshold on returns, including returns on risk adjusted capital. There is greater emphasis today to work as a complete team between the retail, corporate and SME verticals.
- ▶ **Human resources.** One of the key takeaways was that the COO was not comfortable in taking any disruptive action at the HR level. He felt that the talent in ICICI Bank was extremely strong and there is only a need to energize the team. Having come back to the bank after many years, he felt that the team has become much stronger, especially in the retail business and their performance (CASA, retail loans, NPLs etc) is a testimony of the same. There has been constant communication with the team on all the key developments that are happening and serious attempts are being made to ensure that the focus is on business and ensure that there is limited distraction from all the events that are happening outside.

- ▶ **Investigation outcomes.** The management did not specify any timelines but indicated they should be done in a reasonably short time period. They have been in constant discussion with all regulators and authorities. Our understanding based on the discussion suggests that this could be done in FY2019.
- ▶ **Reasonably aware of the underperformance.** One of the discussions where we thought that the management spent some time was the underperformance of the stock. The COO was aware the poor performance and the frequency with which ICICI Bank has been impacted at the end of every cycle. He said that the operating profits that are generated today would see greater translation to PAT in the coming few years which would ensure that the RoEs moves back to normalized levels. This would give greater comfort to investors and address the underperformance of the stock.

Exhibit 1: Strong growth continues in the retail segment while the bank is gradually lowering its exposure in its stressed sectors

Break-up of loan portfolio, March fiscal year-ends, 2008-18 (%)

	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Retail loans	57.1	48.7	43.7	38.8	39.3	37.7	40.8	43.5	47.3	50.6	54.7
Home loans	28.9	25.8	25.3	24.1	18.7	19.4	20.4	22.4	24.4	26.6	28.0
Auto loans	7.6	5.9	4.5	3.8	3.6	3.9	4.5	4.8	5.0	5.3	5.5
Commercial business/SME	8.9	7.4	7.3	6.8	6.9	5.1	3.6	2.7	2.8	3.1	3.2
Two wheeler loans	1.3	0.8	0.2	0.1	-	-	-	-	-	-	-
Personal loans	6.3	4.9	3.1	1.8	1.1	1.1	1.4	1.8	2.3	3.0	3.9
Credit cards	4.2	4.0	3.2	2.2	1.8	1.2	1.0	1.0	1.2	1.6	1.8
Others					7.2	7.0	10.0	10.8	11.6	11.0	12.2
Loans against FCNR dep	-	-	-	-	-	-	1.9	1.7	1.5	1.4	1.3
Non retail loans	42.9	51.3	56.3	61.2	60.7	62.3	59.2	56.5	52.7	49.4	45.3
Power	2.5	2.4	3.0	4.4	5.4	6.2	6.4	6.2	6.1	6.3	5.1
Infrastructure ex power	2.2	4.2	5.5	5.8	6.9	7.3	7.3	6.1	6.0	4.7	3.8
Services - Non finance	6.3	7.5	7.2	7.7	7.4	6.8	6.3	5.8	5.1	3.7	3.2
Iron and steel	4.1	4.4	4.6	4.2	4.7	5.4	5.4	5.5	5.7	4.9	3.8
Services - Finance	2.9	3.5	3.4	7.2	6.0	5.3	3.5	3.2	3.2	5.7	6.4
Wholesale/retail trade	1.1	1.2	2.4	2.3	1.9	1.9	1.9	2.9	2.8	2.4	2.3
Crude/refining	2.5	6.4	7.1	6.3	2.7	3.0	3.0	2.9	1.7	1.4	2.5
Construction	1.3	1.1	1.0	1.6	2.2	2.4	2.4	2.5	2.3	2.0	2.2
Mining	-	-	0.2	1.8	3.2	2.7	1.8	1.8	1.6	2.2	2.0
Electronics and engineering	0.9	1.6	1.7	2.0	2.2	2.2	2.3	1.7	1.5	1.5	1.5
Food and beverages	2.8	2.4	3.3	3.1	2.6	2.3	2.1	1.5	1.5	1.5	1.1
Cement	-	-	-	-	-	-	-	-	1.9	1.6	1.2
Other industries	13.6	13.5	13.4	12.4	14.2	15.5	16.8	16.1	13.3	11.5	10.3

Source: Company, Kotak Institutional Equities

Exhibit 2: ICICI Bank SOTP (FY2020) valuation

	ICICI share (%)	FY2020 (Rs)	Valuation methodology
Value of ICICI standalone	100.0	281	Based on residual growth model
Subsidiaries			
ICICI Financial Services		91	
ICICI Prudential Life	54.9	54	3X Embedded Value and 18X EVOP
General insurance	56.8	22	4.4X FY2020 PBR
Mutual funds	51.0	14	5.5% of AUMs
Other subsidiaries/associates			
ICICI Securities	74.0	9	15X FY2020 PER
ICICI Securities Primary Dealer	100.0	2	1X FY2020 PBR
ICICI Homes	100.0	4	1.5X FY2020 PBR
ICICI Bank UK	100.0	3	0.6X FY2020 PBR
ICICI Bank Canada	100.0	3	0.6X FY2020 PBR
Venture capital/MF	100.0	2	10% of AUM of US\$2 bn
Value of subsidiaries		114	
Value of company		395	

Source: Company, Kotak Institutional Equities estimates

Exhibit 3: ICICI Bank, growth rates, key ratios and Du Pont analysis

March fiscal year-ends, 2016-2021E (%)

	2016	2017	2018	2019E	2020E	2021E
Growth rates (%)						
Net loan growth	12.3	6.7	10.4	11.5	13.5	13.2
Customer assets growth	10.7	6.5	12.4	10.7	12.8	12.6
Corporate loans	3.9	(0.9)	(0.8)	8.7	11.3	11.8
Total retail loans	22.7	14.5	20.5	13.6	15.0	14.2
Deposits growth	16.6	16.3	14.5	13.1	15.5	15.0
Borrowings growth	(2.6)	(26.5)	(23.9)	13.5	(3.0)	1.5
Net interest income	11.5	2.4	5.9	10.8	16.4	14.9
Loan loss provisions	226.1	29.1	1.2	12.0	(71.9)	5.8
Non-interest income	25.8	27.3	(10.7)	(13.0)	14.6	12.7
Net fee income	6.9	7.7	9.4	16.0	14.0	14.1
Net capital gains	145.1	127.2	(26.9)	(73.0)	17.6	-
Total income	17.1	12.8	(1.9)	0.5	15.8	14.1
Operating expenses	10.3	16.3	6.4	9.8	10.8	10.5
Employee expenses	5.3	14.6	3.1	9.7	10.4	9.8
DMA	18.0	18.6	17.7	14.1	19.7	19.7
Asset management measures (%)						
Yield on average earning assets	8.7	8.4	7.7	7.5	7.6	7.8
Interest on advances	9.5	8.8	8.4	8.4	8.5	8.7
Interest on investments	7.2	7.6	6.8	6.6	6.7	6.8
Average cost of funds	5.6	5.4	5.0	5.1	5.0	5.1
Interest on deposits	5.5	5.0	4.5	4.6	4.9	5.0
Other interest	5.7	6.4	7.6	7.8	5.3	5.4
Difference	3.2	3.0	2.7	2.4	2.6	2.7
Net interest income/earning assets	3.5	3.4	3.2	3.1	3.3	3.3
New provisions/average net loans	2.7	3.2	3.0	3.0	0.8	0.7
Loans-to-deposit ratio	73.3	75.2	77.9	76.8	77.3	77.2
Share of deposits						
Current	14.0	15.3	15.9	15.1	14.6	14.2
Fixed	54.2	49.6	48.3	50.0	51.6	52.9
Savings	31.9	35.1	35.8	34.8	33.9	32.9
Tax rate	20.2	13.1	8.8	29.0	29.0	29.0
Dividend payout ratio	29.9	29.7	21.5	20.0	20.0	20.0
Asset quality metrics (%)						
Gross NPL	5.7	8.5	9.5	7.8	5.9	4.6
Net NPL	3.0	5.4	5.4	3.1	1.5	0.8
Slippages	4.3	7.7	6.2	2.4	1.3	1.2
Provision coverage (ex write-off)	47.6	35.8	42.6	60.5	73.8	81.6
RoA composition - % of average assets						
Net interest income	3.1	3.0	3.0	3.1	3.2	3.3
Loan loss provisions	1.6	2.0	1.9	2.0	0.5	0.5
Net other income	2.3	2.7	2.3	1.8	1.9	1.9
Operating expenses	1.9	2.1	2.2	2.1	2.1	2.0
(1- tax rate)	79.8	86.9	91.2	71.0	71.0	71.0
RoA	1.4	1.4	1.1	0.6	1.8	1.9
Average assets/average equity	8.0	7.7	7.5	7.8	8.0	8.1
RoE	11.4	10.9	8.3	4.7	14.4	15.2

Source: Company, Kotak Institutional Equities estimates

Exhibit 4: ICICI Bank income statement and balance sheet

March fiscal year-ends, 2016-2021E (₹ mn)

	2016	2017	2018	2019E	2020E	2021E
Total interest income	527,394	541,563	549,659	610,900	692,394	794,667
Interest on advances	389,432	396,034	408,662	455,242	518,991	601,736
Interest on investments	106,253	113,771	115,682	134,809	150,478	168,046
Total interest expense	315,154	324,190	319,400	355,875	395,433	453,464
Deposits from customers	215,488	228,717	234,288	275,044	338,435	395,673
Net interest income	212,240	217,373	230,258	255,025	296,961	341,203
Loan loss provisions	111,127	143,470	145,216	162,595	45,758	48,403
Net interest income (after prov.)	101,114	73,903	85,042	92,430	251,203	292,800
Other income	153,231	195,045	174,196	151,546	173,728	195,738
Net fee income	74,617	80,349	87,894	101,941	116,248	132,596
Net capital gains	37,954	86,232	63,059	17,000	20,000	20,000
Miscellaneous income	2,592	721	834	1,042	1,302	1,628
Operating expenses	126,836	147,551	157,039	172,430	190,989	210,978
Employee expense	50,023	57,337	59,140	64,904	71,656	78,645
DMA	9,340	11,078	13,036	14,872	17,795	21,295
Pre-tax income	121,959	112,787	74,346	71,547	233,942	277,560
Tax provisions	24,694	14,775	6,570	20,748	67,843	80,492
Net profit	97,264	98,012	67,776	50,798	166,098	197,067
% growth	(13.9)	0.8	(30.8)	(25.0)	227.0	18.6
PBT+provision-treasury gains	200,681	172,545	165,583	217,142	259,700	305,962
% growth	10.4	(14.0)	(4.0)	31.1	19.6	17.8
Balance sheet (Rs mn)						
Cash and bank balance	530,266	469,000	625,036	720,060	808,308	907,837
Cash	65,797	71,939	80,448	91,000	105,102	120,879
Balance with RBI	205,263	245,085	250,576	331,672	376,078	427,118
Balance with banks	2,446	3,801	4,849	5,334	5,867	6,454
Outside India	256,759	148,175	289,163	292,054	321,260	353,386
Net value of investments	1,604,118	1,615,065	2,029,942	2,266,147	2,443,214	2,723,024
Investments in India	1,522,607	1,541,700	1,962,100	2,198,912	2,376,704	2,657,223
Govt. and other securities	1,106,493	1,104,084	1,391,853	1,618,966	1,774,306	2,030,670
Shares	19,874	27,419	23,781	23,781	23,781	23,781
Subsidiaries	64,218	62,405	61,489	61,489	61,489	61,489
Debentures and bonds	92,742	100,750	153,889	156,967	172,664	189,930
Net loans and advances	4,352,639	4,642,321	5,123,953	5,715,719	6,486,483	7,342,879
Corporate loans	2,221,939	2,201,941	2,184,003	2,374,498	2,643,159	2,955,039
Total retail loans	2,130,700	2,440,380	2,939,950	3,341,221	3,843,324	4,387,840
Fixed assets	75,770	78,052	79,035	72,540	66,288	59,125
Net leased assets	2,415	2,415	2,415	1,035	880	748
Net owned assets	73,355	75,637	76,620	71,505	65,407	58,377
Other assets	575,737	625,345	-	-	-	-
Total assets	7,138,531	7,429,784	7,857,965	8,774,467	9,804,292	11,032,864
Deposits	4,214,257	4,900,391	5,609,752	6,345,572	7,328,947	8,429,051
Borrowings and bills payable	1,726,711	1,269,105	966,385	1,096,642	1,064,208	1,080,399
Preference capital	3,500	3,500	3,500	3,500	3,500	3,500
Other liabilities	300,207	260,778	230,239	241,751	193,401	154,721
Total liabilities	6,241,175	6,430,274	6,806,376	7,683,965	8,586,556	9,664,170
Paid-up capital	11,699	11,651	12,858	12,858	12,858	12,858
Reserves & surplus	885,657	987,860	1,038,731	1,077,644	1,204,878	1,355,836
Total shareholders' equity	897,356	999,511	1,051,589	1,090,502	1,217,736	1,368,694

Source: Company, Kotak Institutional Equities estimates

AUGUST 16, 2018

UPDATE

BSE-30: 37,852

Input prices' inflation eases on base effect. WPI inflation started to ease gradually with the unfavorable base effect starting to wane and will likely glide down to 4.2% by March 2019. However, the key risks will be from imported inflation (specifically, global commodity prices and currency depreciation) reflected in core inflation continuing to inch up. CPI inflation will continue to be RBI's focus. Moderation in inflation reaffirms our view that the RBI is likely to remain on hold through the rest of FY2019. We remain cautious on INR depreciation and persistence of global risk-off phase, which may warrant unconventional measures by the RBI apart from possibility of further rate hikes.

Headline WPI inflation eases as favorable base sets in

WPI inflation eased to 5.1% in July (Kotak: 5.4%, Consensus: 5.2%) from 5.8% in June, partly as the base effects waned. The trend was similar to CPI inflation, which also eased partly on the back of favorable base effects (Exhibits 1 and 2). Primary food inflation momentum in July increased to 2.1% mom (increases in almost all items) but due to base effect yoy print was at (-)2.2% yoy after 1.8% in June (Exhibit 3). Within food, vegetables increased sharply by 18.4% mom while fruit prices contracted 7.1% mom. Eggs, meat and fish continued to increase sequentially (0.8% in July). Pulses prices increased sequentially for the first time in nine months. Energy inflation was at 18.1% after 16.2% in June, with increase in LPG prices (7.9% mom), and fall in petrol (0.7%), and diesel (0.5%). Headline inflation continued to be propped up by energy and manufactured products segment (Exhibit 4). We estimate WPI inflation to ease to 4.2% in March 2019 and average at 4.5% in FY2019 against 2.9% in FY2018 (Exhibit 5).

Core WPI inflation inches up

Core WPI inflation (manufactured products excluding food products) increased marginally to 4.9% from 4.8% in June, even as sequential growth was flat (from 0.3% in June). Heavyweights (and global prices driven segments) such as 'basic metals' ((-)0.8% mom) and 'chemicals and chemical products' (0.1% mom) saw some sequential moderation but will likely increase given the recent INR depreciation. We estimate core inflation is close to its peak and ease to 3.9% by March 2019. We estimate average core inflation at 4.4% in FY2019 against 2.9% in FY2018.

RBI likely to pause; caution to prevail amid global volatility

Moderation in inflation reaffirms our view that the RBI may remain on hold through rest of FY2019. Easing growth momentum in 2HFY19 on the back of tighter financial conditions and adverse global growth is expected to begin dragging core inflation lower. Additionally, stable crude oil prices and partial pass-through of MSP into CPI inflation (25-30 bps) seem less of a concern in FY2019. The weekly improvement in sowing pattern and reservoir levels should further keep a lid on food prices. While the growth-inflation dynamics and the assessment of monetary policy transmission may keep the MPC on hold through the rest of FY2019, we remain cautious on INR depreciation on the back of ongoing meltdown in EM financial assets. Persistence of global risk-off and a consequent steep depreciation in the INR may warrant unconventional measures by the RBI apart from possibility of further rate hikes.

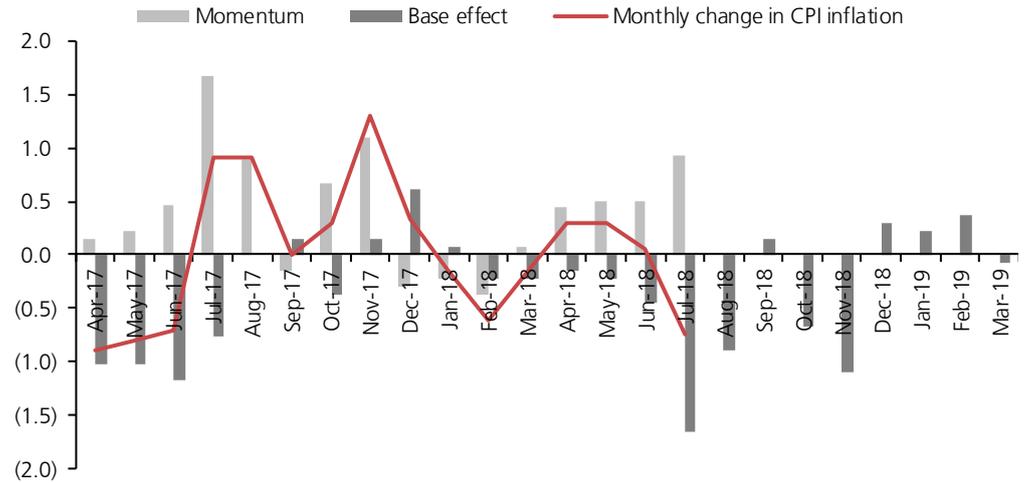
QUICK NUMBERS

- **Headline WPI inflation at 5.1% in July**
- **Core WPI inflation at 4.9% in July**
- **Expect FY2019 average WPI inflation at 4.5%; core WPI inflation at 4.4%**

Suvodeep Rakshit

Upasna Bhardwaj

Exhibit 1: Favorable base effects supported moderation in CPI inflation in July
Trend in momentum, base effect, and monthly change in CPI inflation (%)

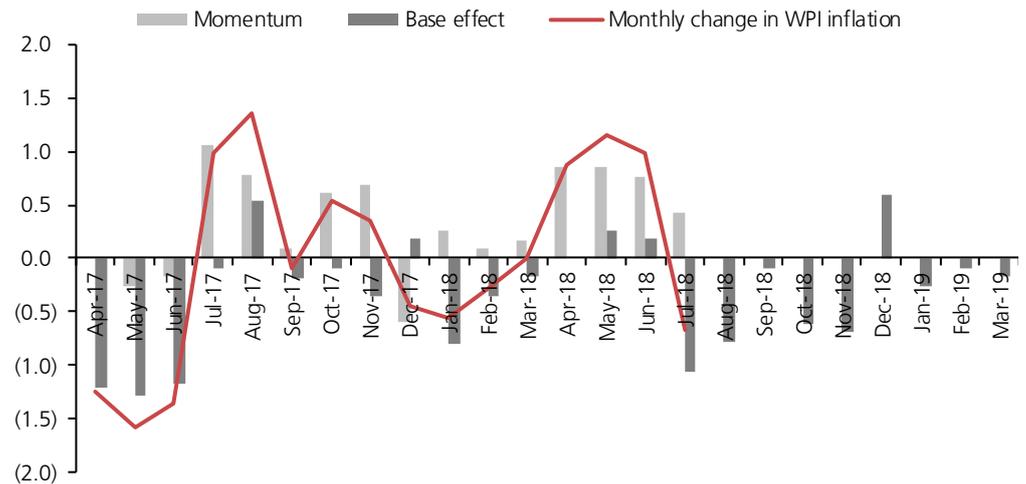


Notes:

(a) Momentum is mom growth while base effect is 12-m prior mom change with signs reversed.

Source: CEIC, Kotak Economics Research

Exhibit 2: Favorable base effects supported moderation in WPI inflation in July
Trend in momentum, base effect, and monthly change in WPI inflation (%)

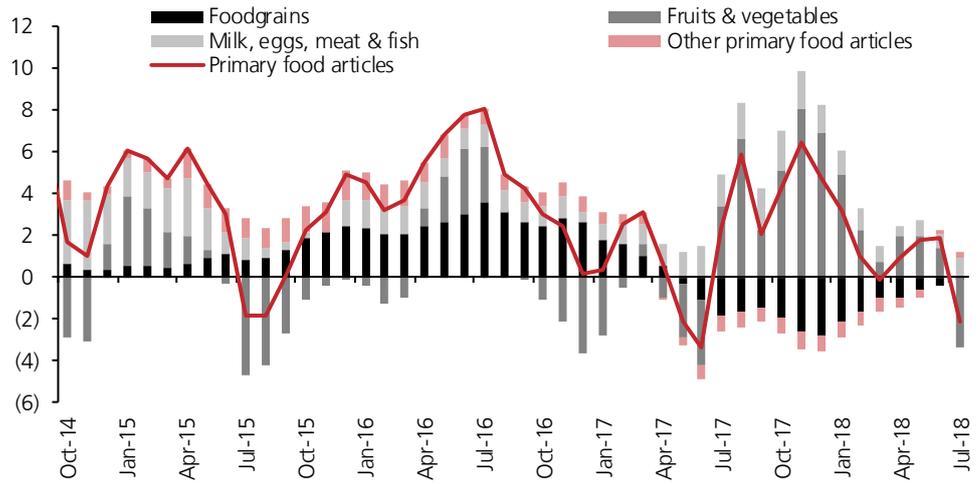


Notes:

(a) Momentum is mom growth while base effect is 12-m prior mom change with signs reversed.

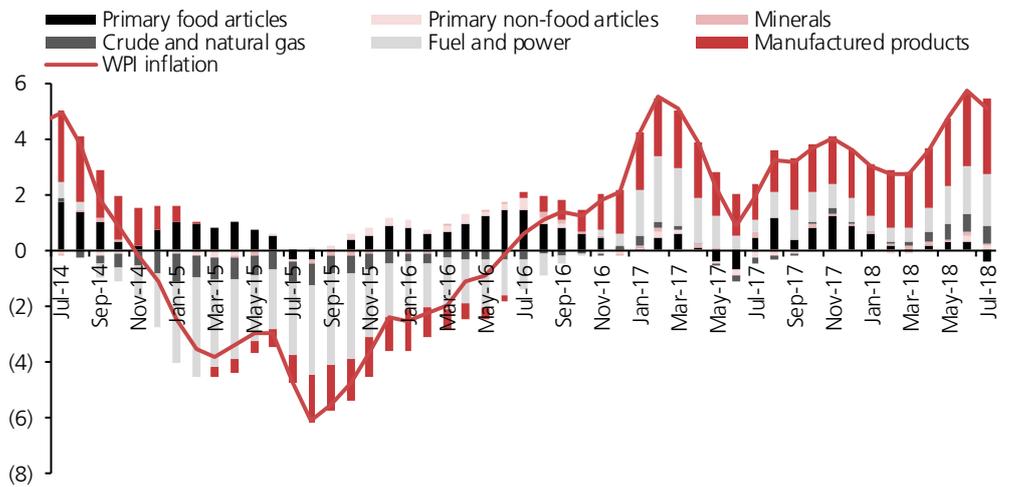
Source: CEIC, Kotak Economics Research

Exhibit 3: Vegetables and food grains inflation pushes down food inflation on favorable base
 Contribution of key food items to primary food inflation (%)



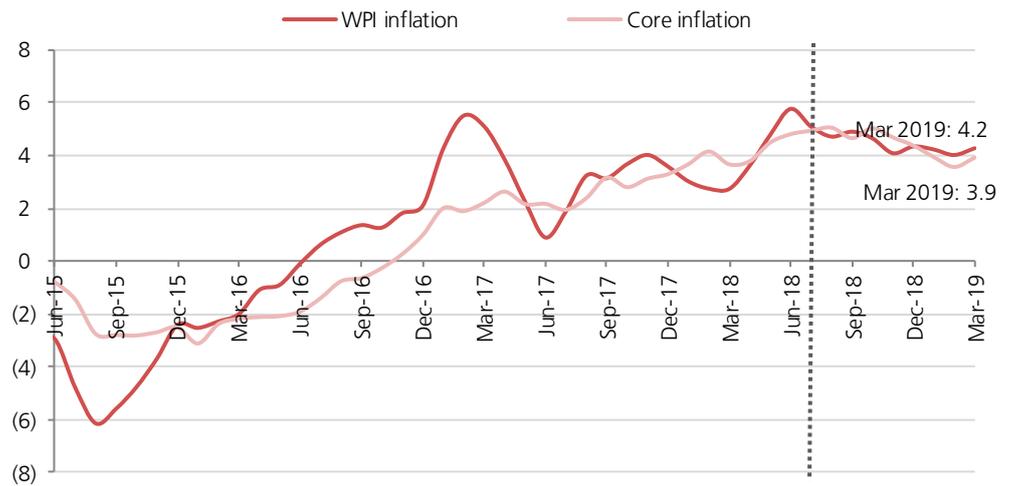
Source: CEIC, Kotak Economics Research

Exhibit 4: Energy and crude inflation propping up WPI inflation along with manufactured products
 Contribution of key items to WPI inflation (%)



Source: CEIC, Kotak Economics Research

Exhibit 5: WPI inflation will likely ease off gradually over next few months
Trend in headline and core WPI inflation (%)



Source: CEIC, Kotak Economics Research estimates

Kotak Institutional Equities: Valuation summary of KIE Universe stocks

Company	Rating	Price (Rs)		Upside (%)	Mkt cap.		O/S shares (mn)	EPS (Rs)			EPS growth (%)			P/E (X)			EV/EBITDA (X)			P/B (X)			RoE (%)			Dividend yield (%)			ADVT 3mo (US\$ mn)
		14-Aug-18	Target price (Rs)		(Rs bn)	(US\$ bn)		2018	2019E	2020E	2018	2019E	2020E	2018	2019E	2020E	2018	2019E	2020E	2018	2019E	2020E	2018	2019E	2020E	2018	2019E	2020E	
Automobiles																													
Amara Raja Batteries	REDUCE	847	780	(7.9)	145	2.1	171	28	32	37	(1.6)	17.1	15.9	30.7	26.2	22.6	16.3	14.0	12.0	4.9	4.3	3.7	17.0	17.4	17.5	0.5	0.6	0.7	5.3
Apollo Tyres	BUY	267	340	27.4	153	2.2	541	13	20	25	(38.0)	46.9	25.7	19.9	13.6	10.8	11.2	8.2	6.9	1.5	1.4	1.3	8.5	11.0	12.5	1.1	1.1	1.1	11.0
Ashok Leyland	BUY	126	160	27.0	370	5.3	2,926	5.4	6.2	8.9	8.0	15.3	43.2	23.4	20.3	14.2	13.5	10.4	7.5	5.1	4.4	3.7	23.7	23.4	28.4	1.9	1.5	2.1	49.5
Bajaj Auto	SELL	2,646	2,500	(5.5)	766	11.0	289	140	148	161	6.0	5.4	9.0	18.9	17.9	16.4	12.7	12.2	10.9	4.0	3.6	3.2	22.9	21.2	20.7	2.3	2.2	2.4	31.9
Balkrishna Industries	REDUCE	1,335	1,300	(2.6)	258	3.7	193	37	50	63	4.8	34.5	24.7	35.7	26.5	21.3	19.0	14.5	11.7	6.3	5.2	4.3	19.0	21.6	22.2	0.4	0.4	0.5	8.2
Bharat Forge	SELL	619	600	(3.1)	288	4.1	466	16	23	27	10.1	44.4	14.6	38.2	26.5	23.1	18.4	15.0	13.1	6.2	5.3	4.5	17.2	21.5	21.0	0.7	0.8	0.9	11.4
CEAT	ADD	1,437	1,500	4.4	58	0.8	40	65	99	108	(29.5)	53.7	8.3	22.2	14.5	13.3	10.7	9.1	7.8	2.2	2.0	1.7	10.4	14.4	13.8	0.8	0.7	0.7	13.4
Eicher Motors	SELL	28,992	24,000	(17.2)	791	11.3	27	792	997	1,180	29.3	25.8	18.4	36.6	29.1	24.6	26.4	21.1	17.8	14.7	10.6	8.0	46.4	42.4	37.1	0.1	0.1	0.1	19.4
Escorts	BUY	876	1,200	37.0	75	1.5	89	39	59	71	71.3	52.3	19.9	22.6	14.8	12.4	12.9	8.9	7.3	3.1	2.6	2.2	13.5	17.6	18.0	0.5	1.0	1.2	16.7
Exide Industries	SELL	292	235	(19.5)	248	3.6	850	8	10	11	0.6	25.3	11.0	35.6	28.4	25.6	19.9	16.2	14.4	4.6	4.2	3.8	13.5	15.4	15.5	0.8	1.0	1.2	7.9
Hero Motocorp	SELL	3,263	3,000	(8.1)	652	9.3	200	185	183	204	9.5	(0.9)	11.4	17.6	17.8	16.0	10.9	10.6	9.3	5.5	4.9	4.4	33.8	29.3	29.1	2.6	2.8	3.1	21.7
Mahindra CIE Automotive	ADD	255	290	13.7	97	1.4	378	10	14	16	107.0	45.0	12.7	26.6	18.3	16.3	13.0	9.2	8.1	2.6	2.3	2.0	10.4	13.2	13.1	—	—	—	2.9
Mahindra & Mahindra	BUY	952	1,085	14.0	1,184	16.9	1,138	38	45	51	22.0	18.5	14.4	25.1	21.2	18.5	16.5	13.8	11.9	3.6	3.2	2.8	15.1	15.8	16.0	0.8	0.9	1.1	33.6
Maruti Suzuki	ADD	9,133	10,000	9.5	2,759	39.5	302	256	323	393	5.1	26.4	21.8	35.7	28.3	23.2	20.0	16.3	12.9	6.6	5.7	4.8	19.8	21.6	22.5	0.9	0.9	1.1	64.8
Motherson Sumi Systems	SELL	298	280	(6.0)	627	9.0	2,105	8	12	14	6.1	41.9	21.4	36.4	25.7	21.2	13.7	10.4	8.6	6.3	5.4	4.6	19.0	22.7	23.4	0.8	1.0	1.1	15.2
MRF	REDUCE	73,820	69,000	(6.5)	313	4.5	4	2,669	3,425	3,932	(23.9)	28.3	14.8	27.7	21.6	18.8	12.5	10.2	8.8	3.2	2.8	2.4	12.3	13.9	13.9	0.1	0.1	0.1	6.6
Schaeffler India	BUY	5,350	6,000	12.1	89	1.3	17	143	156	199	22.0	9.0	27.3	37.4	34.3	26.9	22.0	20.9	15.9	5.2	4.7	4.2	15.0	14.5	16.4	0.3	0.6	0.7	0.6
SKF	ADD	1,713	1,800	5.1	88	1.3	51	58	69	82	24.6	19.7	18.5	29.7	24.8	20.9	18.4	15.8	13.1	4.8	4.1	3.6	16.1	16.7	17.1	0.6	0.7	0.8	0.4
Tata Motors	BUY	249	425	70.8	845	11.3	3,396	20	22	36	(28.0)	10.7	62.7	12.5	11.3	6.9	3.7	3.5	2.9	0.9	0.8	0.7	8.8	7.6	11.2	—	—	—	58.8
Timken	SELL	708	660	(6.8)	48	0.7	68	14	19	25	(5.3)	42.3	27.5	52.3	36.8	28.8	29.1	20.3	16.2	6.9	5.8	4.9	13.9	17.1	18.5	0.1	0.1	0.1	0.4
TVS Motor	SELL	519	405	(22.0)	247	3.5	475	14	16	20	18.7	13.9	23.0	37.2	32.7	26.6	22.8	18.1	14.9	8.6	7.3	6.2	25.1	24.2	25.4	0.6	0.9	1.1	14.1
WABCO India	SELL	6,750	6,350	(5.9)	128	1.8	19	144	169	222	27.8	17.8	31.3	46.9	39.8	30.3	30.4	25.9	19.6	8.4	7.0	5.8	19.5	19.2	20.9	0.1	0.2	0.2	0.5
Automobiles	Neutral				10,226	146					(0.9)	19.4	25.5	26.2	21.9	17.5	11.6	9.8	8.1	3.7	3.3	2.9	14.2	15.1	16.5	0.9	0.9	1.1	394.3
Banks																													
Axis Bank	ADD	618	600	(3.0)	1,588	22.7	2,567	1	18	40	(92.6)	1,577.6	122.3	575.6	34.3	15.4	—	—	—	3.0	2.7	2.2	0.5	7.1	14.1	0.8	0.4	1.0	58.1
Bank of Baroda	NR	146	—	—	387	5.5	2,652	(9)	21	26	(253.2)	323.7	26.4	(16.0)	7.1	5.6	—	—	—	1.6	1.3	1.0	(5.8)	12.7	14.0	—	—	—	34.7
Canara Bank	ADD	271	300	10.8	198	2.8	733	(58)	(5)	51	(406.6)	91.6	1,147.0	(4.7)	(55.9)	5.3	—	—	—	1.7	1.6	1.0	(12.2)	(1.0)	10.1	—	—	—	28.8
City Union Bank	ADD	185	190	2.6	136	1.9	665	18	19	21	6.5	5.8	13.3	10.4	9.8	8.7	—	—	—	1.6	1.5	1.3	30.6	31.1	31.1	0.3	1.8	2.0	1.8
DCB Bank	ADD	165	205	24.0	51	0.7	308	8	10	12	13.8	28.2	21.0	20.8	16.2	13.4	—	—	—	2.1	1.9	1.7	10.9	11.7	12.7	—	0.6	0.7	4.3
Equitas Holdings	BUY	142	190	33.6	48	0.7	340	0.9	4.4	8.4	(80.3)	378.4	89.9	153.2	32.0	16.9	—	—	—	2.2	2.1	1.9	1.4	6.4	11.2	—	—	—	4.3
Federal Bank	BUY	89	130	46.4	176	2.5	1,972	4.4	5.7	7.9	(9.3)	29.5	39.5	20.3	15.7	11.3	—	—	—	1.6	1.4	1.3	8.2	8.8	11.4	1.1	1.5	2.0	16.6
HDFC Bank	REDUCE	2,089	2,000	(4.3)	5,580	79.9	2,595	67	78	94	18.7	15.7	20.0	31.0	26.8	22.3	—	—	—	5.2	3.9	3.5	17.9	16.7	16.2	0.6	0.7	0.9	86.6
ICICI Bank	BUY	332	400	20.3	2,139	30.6	6,429	11	8	26	(31.1)	(19.6)	209.1	31.5	39.2	12.7	—	—	—	2.6	2.3	1.9	6.6	5.1	14.5	0.5	0.5	1.6	93.5
IDFC Bank	NR	45	—	—	152	2.2	3,404	2.5	1.2	2.9	(16.0)	(52.7)	146.7	17.6	37.3	15.1	—	—	—	1.0	1.0	0.9	5.7	2.6	6.3	1.1	0.5	1.3	9.5
IndusInd Bank	REDUCE	1,998	1,900	(4.9)	1,200	17.2	600	60	71	87	25.3	17.5	23.6	33.3	28.3	22.9	—	—	—	5.2	4.2	3.7	17.1	17.6	16.8	—	0.4	0.5	29.3
J&K Bank	BUY	59	100	70.6	33	0.5	557	4	7	11	111.6	82.4	63.8	16.1	8.8	5.4	—	—	—	0.8	0.7	0.7	3.4	5.9	9.1	—	2.3	3.7	0.4
Karur Vysya Bank	ADD	100	110	9.9	80	1.2	727	5	3	13	(52.2)	(32.3)	306.7	21.0	31.1	7.6	—	—	—	1.4	1.4	1.2	6.1	3.7	14.1	0.6	0.8	3.3	1.8
Punjab National Bank	ADD	80	90	12.6	221	3.2	2,761	(44)	(27)	12	(814.7)	40.4	145.3	(1.8)	(3.0)	6.7	—	—	—	5.1	4.0	1.3	(32.5)	(23.4)	10.7	—	-	-	39.9
RBL Bank	SELL	564	475	(15.8)	238	3.4	420	15	22	29	27.3	48.1	31.5	37.3	25.2	19.1	—	—	—	3.7	3.3	2.9	11.5	13.3	15.5	0.4	0.6	0.8	12.4
State Bank of India	BUY	295	370	25.5	2,632	37.7	8,925	(7)	8	37	(155.8)	204.8	380.5	(40.2)	38.4	8.0	—	—	—	2.3	1.9	1.4	(3.2)	3.1	13.6	—	0.1	0.1	96.0
Ujivan Financial Services	REDUCE	345	420	21.7	42	0.6	121	1	19	28	(96.6)	3,033.9	47.3	578.3	18.5	12.5	—	—	—	2.4	2.1	1.9	0.4	12.1	15.8	0.1	0.5	0.8	5.9
Union Bank	ADD	85	120	40.6	100	1.4	1,169	(45)	8	33	(656.0)	117.1	330.8	(1.9)	11.1	2.6	—	—	—	1.4	1.2	0.7	(23.7)	3.9	15.2	—	1.3	5.8	9.7
YES Bank	SELL	383	335	(12.4)	882	12.6	2,303	18	20	22	25.7	8.1																	

Kotak Institutional Equities: Valuation summary of KIE Universe stocks

Company	Rating	Price (Rs)		Upside (%)	Mkt cap.		O/S shares (mn)	EPS (Rs)			EPS growth (%)			P/E (X)			EV/EBITDA (X)			P/B (X)			RoE (%)			Dividend yield (%)			ADVT 3mo (US\$ mn)
		14-Aug-18	Target price (Rs)		(Rs bn)	(US\$ bn)		2018	2019E	2020E	2018	2019E	2020E	2018	2019E	2020E	2018	2019E	2020E	2018	2019E	2020E	2018	2019E	2020E	2018	2019E	2020E	
NBFCs																													
Bajaj Finance	SELL	2,830	2,000	(29.3)	1,636	23.4	575	43	68	90	29.2	56.6	31.9	65.2	41.6	31.6	—	—	—	10.3	8.5	6.9	19.7	22.4	24.0	0.1	0.2	0.3	58.7
Bajaj Finserv	REDUCE	7,113	6,100	(14.2)	1,132	16.2	159	176	245	307	10.3	39.7	25.2	40.5	29.0	23.2	—	—	—	5.7	4.6	3.9	15.6	17.5	18.1	0.2	0.2	0.2	19.3
Bharat Financial Inclusion	NA	1,218	—	—	170	2.4	139	33	43	54	55.5	31.1	27.2	37.3	28.4	22.4	—	—	—	5.7	4.6	3.8	16.7	17.9	18.5	—	—	—	10.1
Cholamandalam	REDUCE	1,472	1,500	1.9	230	3.3	156	62	90	110	35.5	44.8	22.1	23.6	16.3	13.4	—	—	—	4.7	3.8	3.1	20.6	24.5	24.3	0.4	0.7	0.9	7.3
HDFC	ADD	1,942	2,075	6.9	3,282	47.0	1,676	75	56	67	52.1	(25.8)	19.0	25.8	34.7	29.2	—	—	—	5.1	4.4	4.0	23.9	13.8	14.5	1.0	1.1	1.3	69.8
HDFC Standard Life Insurance	SELL	468	405	(13.5)	942	13.5	2,007	6	6	7	24.4	14.8	10.9	84.6	73.7	66.5	—	—	—	21.9	19.5	17.5	27.3	28.0	27.7	0.3	0.3	0.4	11.3
ICICI Lombard	SELL	781	620	(20.6)	354	5.1	454	19	26	32	22.0	37.1	21.5	41.1	30.0	24.7	—	—	—	7.8	6.6	5.5	20.8	23.8	24.2	0.5	0.8	0.9	2.2
ICICI Prudential Life	BUY	399	500	25.2	573	8.2	1,436	11	12	13	(3.7)	10.1	7.0	35.4	32.1	30.1	—	—	—	8.7	7.2	6.0	25.0	24.5	21.8	1.4	0.5	0.6	9.1
IIFL Holdings	SELL	742	625	(15.8)	237	3.4	319	29	38	45	32.4	31.5	18.6	26.0	19.8	16.7	—	—	—	4.7	3.5	3.0	19.0	20.5	20.0	0.8	1.1	1.3	1.5
L&T Finance Holdings	ADD	179	190	6.1	358	5.1	1,996	7	13	14	23.7	70.9	12.3	24.4	14.3	12.7	—	—	—	2.8	2.6	2.2	14.2	18.9	18.8	1.0	1.1	1.4	12.3
LIC Housing Finance	BUY	547	610	11.5	276	4.0	505	44	50	58	3.2	13.8	17.5	12.5	11.0	9.4	—	—	—	2.1	1.7	1.5	14.5	14.3	14.4	1.2	1.4	1.7	12.5
Magma Fincorp	BUY	140	200	43.1	38	0.5	237	10	12	15	1,014.5	24.6	25.8	14.4	11.5	9.2	—	—	—	1.4	1.4	1.2	10.2	12.9	14.1	0.6	1.3	1.6	1.1
Mahindra & Mahindra Financial	REDUCE	487	500	2.6	301	4.3	614	15	23	28	105.0	58.4	23.2	33.6	21.2	17.2	—	—	—	3.5	3.1	2.8	11.3	14.3	15.8	0.8	1.3	1.6	10.5
Max Financial Services	ADD	468	650	39.0	125	1.8	268	5	6	6	(20.4)	36.9	1.8	102.0	74.5	73.2	—	—	—	—	—	—	6.5	8.3	8.0	—	0.5	0.5	4.6
Muthoot Finance	ADD	411	480	16.9	164	2.4	400	43	38	40	45.6	(10.8)	4.0	9.5	10.7	10.3	—	—	—	2.1	1.8	1.6	24.1	18.4	16.9	2.4	2.1	2.2	4.7
PNB Housing Finance	REDUCE	1,273	1,325	4.1	213	3.0	167	50	62	75	57.7	25.3	20.9	25.6	20.4	16.9	—	—	—	3.4	3.0	2.6	14.0	15.2	15.9	0.7	0.3	0.3	4.9
SBI Life Insurance	ADD	659	785	19.1	659	9.4	1,000	12	15	18	20.8	26.0	22.9	57.1	45.3	36.9	—	—	—	10.2	8.6	7.2	19.4	20.6	21.3	0.3	0.4	0.4	3.5
Shriram City Union Finance	ADD	2,010	2,250	11.9	133	1.9	66	101	141	174	19.6	40.4	22.7	20.0	14.2	11.6	—	—	—	2.5	2.3	2.0	12.5	15.8	16.9	0.9	0.9	1.1	1.3
Shriram Transport	ADD	1,320	1,550	17.4	300	4.3	227	69	114	130	24.7	64.4	14.3	19.1	11.6	10.2	—	—	—	2.5	2.1	1.8	13.1	18.3	17.5	0.8	1.2	1.4	30.2
NBFCs	Neutral				11,123		159				36.9	14.8	19.4	32.5	28.3	23.7				5.5	4.6	4.0	16.8	16.1	16.8	0.6	0.7	0.8	590.6
Cement																													
ACC	SELL	1,564	1,270	(18.8)	294	4.2	188	49	62	70	32.7	27.0	13.8	32.1	25.3	22.2	17.2	14.0	12.0	3.1	2.9	2.7	10.1	11.9	12.5	1.1	1.1	1.1	15.7
Ambuja Cements	REDUCE	226	210	(7.2)	449	6.4	1,986	8	9	11	29.7	14.5	23.2	30.1	26.3	21.3	10.0	8.9	7.3	2.2	2.1	2.0	7.4	8.1	9.5	1.6	1.6	1.6	11.3
Dalmia Bharat	ADD	2,594	2,830	9.1	231	3.3	89	60	94	122	55.4	55.8	29.3	43.0	27.6	21.3	13.3	10.5	8.6	3.8	3.3	2.9	9.7	12.9	14.6	0.1	0.1	0.1	4.7
Grasim Industries	BUY	987	1,170	18.6	649	9.3	657	47	46	55	(30.1)	(2.5)	18.8	20.8	21.4	18.0	11.8	7.3	7.0	1.1	1.1	1.0	7.0	5.2	5.9	0.6	0.6	0.6	13.8
India Cements	REDUCE	111	118	6.5	34	0.5	308	3	4	8	(42.5)	28.0	102.6	33.9	26.5	13.1	9.5	8.6	6.7	0.7	0.6	0.6	2.0	2.5	4.8	0.9	0.9	0.9	8.1
J K Cement	ADD	779	890	14.2	54	0.8	70	43	45	79	59.3	3.7	75.4	18.0	17.4	9.9	9.9	10.2	8.4	2.8	2.5	2.0	16.2	15.0	22.3	1.0	1.0	1.0	0.5
JK Lakshmi Cement	ADD	325	370	14.0	38	0.5	118	4	11	28	(35.7)	153.5	147.9	72.6	28.7	11.6	13.5	10.0	6.5	2.6	2.5	2.1	3.7	8.9	19.5	0.6	0.6	0.6	0.4
Orient Cement	ADD	115	145	25.6	24	0.3	205	2	7	11	237.8	212.9	58.7	53.4	17.1	10.8	11.8	7.9	6.1	2.3	2.1	1.8	4.4	12.9	18.2	0.6	1.3	1.7	0.2
Shree Cement	SELL	17,267	12,500	(27.6)	602	8.6	35	397	421	630	3.4	6.0	49.7	43.5	41.0	27.4	23.4	19.1	14.3	6.8	5.9	5.0	16.7	15.4	19.7	0.3	0.3	0.3	5.3
UltraTech Cement	SELL	4,299	2,950	(31.4)	1,181	16.9	275	88	126	162	(7.8)	42.7	28.9	48.8	34.2	26.5	24.0	17.8	14.7	4.6	4.1	3.6	9.7	12.6	14.3	0.2	0.2	0.2	19.7
Cement	Cautious				3,556		51				6.5	19.5	30.3	34.3	28.7	22.1	15.3	11.0	9.4	2.6	2.4	2.2	7.5	8.4	10.0	0.6	0.6	0.6	79.7

Source: Company, Bloomberg, Kotak Institutional Equities estimates

Kotak Institutional Equities: Valuation summary of KIE Universe stocks

Company	Rating	Price (Rs)		Upside (%)	Mkt cap.		O/S shares (mn)	EPS (Rs)			EPS growth (%)			P/E (X)			EVEBITDA (X)			P/B (X)			RoE (%)			Dividend yield (%)			ADVT 3mo (US\$ mn)
		14-Aug-18	Target price (Rs)		(Rs bn)	(US\$ bn)		2018	2019E	2020E	2018	2019E	2020E	2018	2019E	2020E	2018	2019E	2020E	2018	2019E	2020E	2018	2019E	2020E	2018	2019E	2020E	
Consumer products																													
Asian Paints	REDUCE	1,395	1,325	(5.0)	1,338	19.1	959	21	27	33	2.9	32.1	20.3	68.0	51.5	42.8	41.6	32.3	26.7	15.9	13.9	12.1	24.6	28.8	30.3	0.6	0.9	1.1	20.8
Bajaj Corp.	ADD	420	470	11.9	62	0.9	148	14	15	17	(9.4)	7.8	10.3	29.4	27.2	24.7	23.2	21.8	18.6	12.6	12.7	12.6	42.8	46.3	51.2	2.9	3.1	3.3	0.4
Britannia Industries	ADD	6,460	6,700	3.7	776	11.1	120	84	104	127	13.5	24.5	22.2	77.2	62.0	50.7	51.1	40.7	33.3	22.8	18.1	14.6	32.9	32.5	31.8	0.4	0.5	0.7	11.9
Coffee Day Enterprises	REDUCE	247	290	17.2	52	0.7	211	3	8	10	49.1	129.9	30.0	74.0	32.2	24.8	12.8	11—	10—	2.2	2.1	1.9	3.1	6.6	8.0	—	—	—	0.8
Colgate-Palmolive (India)	ADD	1,134	1,250	10.2	308	4.4	272	24	27	32	15.2	14.7	15.6	47.7	41.6	36.0	27.3	23.9	20.8	20.2	20.4	17.4	46.2	48.8	52.2	2.1	1.4	1.7	8.1
Dabur India	REDUCE	453	390	(13.9)	800	11.4	1,762	8	9	10	7.2	17.3	12.9	58.3	49.7	44.0	49.4	41.6	35.9	14.0	14.0	12.2	25.9	28.1	29.6	1.7	0.8	1.0	14.3
GlaxoSmithKline Consumer	ADD	6,743	7,300	8.3	284	4.1	42	166	199	223	6.6	19.5	12.1	40.5	33.9	30.2	28.0	23.5	20.2	8.1	7.3	6.6	21.2	22.8	23.0	1.1	1.3	1.6	2.2
Godrej Consumer Products	SELL	1,295	1,100	(15.0)	882	12.6	681	21	25	29	11.5	18.8	13.7	60.6	51.0	44.9	43.0	36.2	31.5	14.1	12.0	10.4	25.2	25.4	24.8	0.5	0.7	0.7	9.4
Hindustan Unilever	REDUCE	1,747	1,570	(10.1)	3,782	54.1	2,160	25	29	33	25.0	19.5	13.2	71.2	59.6	52.7	51.1	41.3	36.3	53.3	46.6	39.6	78.1	83.5	81.4	1.1	1.2	1.4	35.6
ITC	ADD	308	330	7.2	3,763	53.9	12,275	9	10	11	7.8	8.2	12.3	34.5	31.9	28.4	22.7	20.7	18.2	7.4	6.9	6.5	19.4	20.4	22.2	1.7	1.9	2.2	49.6
Jubilant Foodworks	BUY	1,507	1,650	9.5	199	2.8	132	15	25	35	191.7	73.6	37.5	103.6	59.6	43.4	44.3	29.9	22.6	20.6	14.8	11.3	21.7	28.9	29.5	0.1	0.1	0.2	36.1
Jyothy Laboratories	ADD	223	240	7.7	81	1.2	364	4	6	7	(26.4)	27.6	16.7	50.6	39.6	34.0	31.0	26.4	22.5	7.1	6.1	5.3	14.4	16.6	16.8	0.2	0.4	0.7	1.6
Marico	ADD	364	375	2.9	470	6.7	1,291	6	7	8	7.4	8.9	20.0	58.1	53.4	44.5	41.0	37.1	30.6	18.5	17.5	16.3	33.2	33.7	37.9	1.1	1.3	1.5	9.5
Nestle India	ADD	10,885	11,000	1.1	1,049	15.0	96	127	171	197	21.1	34.2	15.7	85.7	63.8	55.1	47.2	36.6	31.6	30.7	28.2	25.9	36.6	46.1	49.0	0.8	1.1	1.2	8.5
Page Industries	SELL	33,232	25,000	(24.8)	371	5.3	11	311	418	508	32.5	34.3	21.6	106.8	79.5	65.4	68.1	51.4	42.4	43.7	33.6	26.6	45.9	47.8	45.5	0.4	0.5	0.7	9.0
Pidlite Industries	REDUCE	1,123	1,080	(3.8)	570	8.2	508	18	21	26	7.5	16.8	21.8	62.2	53.3	43.8	41.6	35.4	29.2	16.0	13.5	11.4	26.0	27.4	28.2	0.5	0.6	0.7	13.5
S H Kelkar and Company	BUY	205	290	41.6	30	0.4	145	7	7	10	2.1	(6.2)	41.9	27.7	29.5	20.8	19.3	19.1	13.7	3.5	3.2	2.9	12.8	11.3	14.5	0.9	0.9	1.0	0.4
Tata Global Beverages	REDUCE	238	250	5.2	150	2.1	631	7	8	9	20.7	7.7	17.0	32.3	30.0	25.6	17.0	16.5	14.4	2.1	2.1	2.0	7.0	7.0	7.9	1.1	1.3	1.5	13.4
Titan Company	SELL	926	840	(9.2)	822	11.8	888	13	16	20	43.3	25.6	21.8	72.4	57.7	47.3	49.6	38.3	30.5	16.2	13.6	11.4	24.3	25.6	26.3	0.4	0.5	0.6	36.6
United Breweries	SELL	1,336	1,100	(17.7)	353	5.1	264	15	21	25	71.6	38.9	22.3	89.5	64.5	52.7	39.4	31.6	27.3	13.2	11.1	9.5	15.7	18.7	19.4	0.1	0.2	0.3	12.1
United Spirits	REDUCE	625	590	(5.6)	454	6.5	727	8	10	13	39.1	34.7	30.9	82.2	61.0	46.6	47.2	35.4	28.7	18.1	12.5	9.2	24.9	24.2	22.7	—	—	0.3	17.6
Varun Beverages	ADD	783	800	2.1	143	2.0	183	12	15	20	377.8	29.8	34.5	68.0	52.4	39.0	20.5	17.3	14.7	8.1	7.2	6.2	12.1	14.6	17.1	—	—	0.1	1.6
Consumer products	Cautious				16,740	240					14.5	17.7	15.9	55.5	47.1	40.6	36.2	30.5	26.2	13.7	12.3	11.0	24.6	26.2	27.1	1.0	1.1	1.3	313.0
Energy																													
BPCL	REDUCE	377	375	(0.4)	817	11.7	1,967	40	38	39	(1.5)	(6.7)	3.1	9.4	10.0	9.7	7.6	7.3	6.9	2.2	2.0	1.8	24.8	20.5	19.1	5.6	4.0	4.1	30.6
Castrol India	SELL	155	155	0.0	153	2.2	989	7	7	8	3.3	2.9	10.1	22.5	21.9	19.9	14.1	13.7	12.3	15.0	14.4	14.0	67.9	67.1	71.5	3.1	3.5	4.0	4.0
GAIL (India)	BUY	380	440	15.9	856	12.3	2,255	20	26	29	21.8	27.8	10.0	18.6	14.5	13.2	11.6	9.1	8.3	2.1	2.0	1.8	11.7	14.0	14.1	1.9	2.2	2.5	23.1
GSPL	SELL	201	175	(12.8)	113	1.6	564	12	11	11	34.5	(6.5)	(0.5)	16.9	18.1	18.2	8.7	6.9	6.9	2.2	2.0	1.9	14.0	11.7	10.7	0.9	0.8	0.8	1.5
HPCL	REDUCE	270	285	5.5	412	5.9	1,524	42	32	32	(3.2)	(22.3)	(2.2)	6.5	8.3	8.5	5.7	7.3	7.7	1.7	1.6	1.4	28.7	19.6	17.4	6.3	4.9	4.8	27.8
Indraprastha Gas	SELL	285	240	(15.8)	200	2.9	700	10	12	13	19.0	16.4	12.3	27.6	23.8	21.2	17.4	15.1	13.3	5.7	4.9	4.3	22.4	22.1	21.5	0.7	0.9	1.1	11.5
IOCL	REDUCE	161	150	(6.6)	1,560	22.3	9,479	21	18	17	(24.8)	(11.2)	(4.1)	7.8	8.8	9.2	4.6	5.0	5.0	1.4	1.3	1.2	18.5	15.1	13.4	7.2	4.5	4.4	24.0
Mahanagar Gas	ADD	942	965	2.4	93	1.3	99	48	56	60	21.5	16.0	7.6	19.5	16.8	15.6	11.8	9.8	8.9	4.4	3.9	3.5	24.3	24.8	23.5	2.0	2.3	2.6	5.0
ONGC	ADD	166	200	20.2	2,135	30.5	12,833	17	20	20	3.1	16.8	0.3	9.6	8.2	8.2	5.1	3.9	3.7	0.9	0.9	0.8	9.9	11.2	10.6	4.0	4.1	4.2	18.4
Oil India	SELL	208	200	(3.8)	236	3.4	1,135	25	23	24	18.6	(6.7)	3.4	8.4	9.0	8.7	6.5	5.9	5.7	0.8	0.8	0.8	9.8	9.2	9.0	5.0	5.0	4.4	4.6
Petronet LNG	BUY	222	280	26.1	333	4.8	1,500	14	16	18	22.1	16.7	13.1	16.0	13.7	12.1	10.6	9.2	7.7	3.4	3.0	2.7	23.3	23.3	23.2	2.0	2.6	3.3	12.3
Reliance Industries	SELL	1,211	985	(18.6)	7,164	102.5	5,922	59	69	78	16.9	17.6	12.4	20.5	17.4	15.5	14.8	11.8	10.1	2.4	2.2	1.9	11.6	12.2	12.1	0.5	0.5	0.6	122.2
Energy	Attractive				14,072	201					0.9	7.2	5.2	13.6	12.7	12.1	8.8	7.7	7.1	1.8	1.7	1.5	13.3	13.0	12.5	2.4	2.1	2.1	283.2

Source: Company, Bloomberg, Kotak Institutional Equities estimates

Kotak Institutional Equities: Valuation summary of KIE Universe stocks

Company	Rating	Price (Rs)		Upside (%)	Mkt cap.		O/S shares (mn)	EPS (Rs)			EPS growth (%)			P/E (X)		EV/EBITDA (X)			P/B (X)			RoE (%)			Dividend yield (%)			ADVT 3mo (US\$ mn)	
		14-Aug-18	Target price (Rs)		(Rs bn)	(US\$ bn)		2018	2019E	2020E	2018	2019E	2020E	2018	2019E	2020E	2018	2019E	2020E	2018	2019E	2020E	2018	2019E	2020E	2018	2019E		2020E
Industrials																													
ABB	SELL	1,207	1,020	(15.5)	256	3.7	212	20	26	29	12.1	30.1	14.2	60.9	46.8	41.0	33.5	27.4	24.6	7.1	6.5	5.9	12.2	14.5	15.1	0.3	0.7	0.7	1.1
BHEL	REDUCE	72	78	8.0	265	3.8	3,671	2.2	2.6	5.0	62.7	16.5	95.3	32.9	28.2	14.5	7.9	7.4	3.9	0.8	0.8	0.8	2.5	2.9	5.6	2.5	2.9	5.7	10.0
Carborundum Universal	SELL	351	322	(8.3)	66	0.9	189	11	14	17	22.8	25.0	21.4	30.8	24.6	20.3	16.6	13.5	11.0	4.2	3.8	3.4	14.6	16.3	17.8	0.5	1.2	1.5	0.4
CG Power and Industrial	BUY	60	72	19.6	38	0.5	627	0.8	2.9	4.3	(72.2)	255.2	48.7	73.7	20.7	13.9	10.9	8.2	6.5	1.4	1.4	1.3	1.5	6.7	9.8	—	—	—	7.9
Crompton Greaves Consumer	SELL	263	215	(18.4)	165	2.4	627	5.2	6.2	7.5	13.3	19.5	20.7	51.0	42.6	35.3	31.3	26.6	22.5	20.9	14.5	11.2	49.5	40.4	35.8	0.6	0.8	0.9	2.8
Cummins India	REDUCE	673	710	5.6	186	2.7	277	24	28	33	(8.0)	15.2	17.5	27.8	24.2	20.6	24.5	20.2	17.3	4.7	4.4	4.1	17.3	18.7	20.6	2.1	2.2	2.6	4.1
Havells India	SELL	686	485	(29.3)	429	6.1	625	11	14	17	16.6	26.6	20.5	61.9	48.9	40.6	39.7	31.4	25.6	11.5	10.1	8.8	19.8	22.0	23.2	0.5	0.7	0.9	12.8
Kalpataru Power Transmission	BUY	363	560	54.5	56	0.8	153	18	23	32	50.6	26.0	39.1	19.8	15.7	11.3	8.4	6.9	5.5	2.1	1.9	1.6	11.0	12.5	15.2	0.5	0.5	0.5	0.7
KEC International	BUY	301	410	36.2	77	1.1	257	18	21	27	51.1	16.9	29.7	16.8	14.4	11.1	9.2	8.1	6.6	3.9	3.1	2.5	25.7	24.1	25.2	0.6	0.7	1.0	3.1
L&T	BUY	1,253	1,600	27.7	1,757	25.1	1,401	52	63	70	22.4	21.7	10.9	24.2	19.9	18.0	20.3	16.1	15.5	3.5	3.2	2.9	15.0	16.8	16.8	1.3	1.8	2.0	43.0
Siemens	SELL	1,007	1,000	(0.7)	359	5.1	356	24	29	35	21.2	21.4	21.7	42.0	34.6	28.5	24.2	19.6	15.8	4.4	4.1	3.9	10.8	12.3	14.0	1.0	1.2	1.4	3.1
Thermax	REDUCE	1,035	1,010	(2.4)	123	1.8	113	21	28	39	(3.6)	34.7	39.2	50.2	37.3	26.8	30.6	23.6	17.5	4.3	4.0	3.7	8.8	11.1	14.3	0.6	0.9	1.1	0.7
Voltas	SELL	614	530	(13.6)	203	2.9	331	17	17	21	10.7	0.4	18.8	35.5	35.4	29.8	30.4	26.5	21.6	5.2	4.7	4.2	15.9	13.9	14.8	0.6	0.6	0.7	14.8
Industrials	Neutral				3,980	57					19.8	21.7	20.7	31.0	25.5	21.1	20.4	16.5	14.4	3.4	3.1	2.9	10.8	12.3	13.7	1.1	1.5	1.8	104.5
Infrastructure																													
Adani Ports and SEZ	BUY	373	460	23.3	773	11.1	2,071	18	19	23	(2.1)	1.2	21.1	20.2	19.9	16.5	13.6	13.6	11.3	3.7	3.2	2.7	19.8	17.0	17.7	0.5	0.5	0.5	24.2
Ashoka Buildcon	BUY	138	235	70.3	39	0.6	282	8	9	10	34.6	4.1	17.8	16.4	15.8	13.4	13.2	10.3	8.6	2.0	1.7	1.6	13.0	11.8	12.3	0.8	1.2	0.9	0.6
Container Corp.	SELL	643	635	(1.2)	313	4.5	487	18	21	25	7.1	17.4	20.9	36.4	31.0	25.7	24.1	19.1	15.1	3.3	3.1	2.8	9.4	10.3	11.6	2.7	1.4	1.6	7.0
Dilip Buildcon	BUY	844	1,220	44.5	115	1.7	137	46	54	69	76.5	16.1	28.0	18.2	15.7	12.2	10.1	7.3	6.1	4.7	3.6	2.8	29.5	25.9	25.4	—	—	—	8.8
Gateway Distriparks	BUY	186	250	34.7	20	0.3	109	8	7	8	11.2	(5.8)	15.2	24.4	25.9	22.5	23.2	11.5	9.5	2.0	3.5	3.0	8.2	9.8	14.5	3.8	—	1.6	0.7
Gujarat Pipavav Port	BUY	110	150	35.9	53	0.8	483	4.1	5.3	6.5	(20.6)	29.7	22.9	26.8	20.7	16.8	13.1	11.0	9.0	2.6	2.6	2.5	9.8	12.7	15.3	3.1	4.0	4.9	0.8
IRB Infrastructure	BUY	191	320	67.6	67	1.0	351	23	31	33	10.8	36.8	7.1	8.5	6.2	5.8	6.9	6.5	7.0	1.2	1.0	0.9	14.5	17.6	16.3	1.2	1.6	2.1	6.0
Mahindra Logistics	REDUCE	558	565	1.3	40	0.6	71	10	15	21	16.2	50.7	39.3	56.9	37.7	27.1	32.8	21.0	15.2	9.5	7.8	6.3	18.2	22.7	25.8	—	—	—	0.7
Sadbhav Engineering	BUY	271	435	60.6	46	0.7	172	13	17	22	17.4	31.7	31.0	21.1	16.0	12.2	14.7	11.6	9.1	2.5	2.2	1.9	12.5	14.5	16.5	—	—	—	0.8
Infrastructure	Attractive				1,467	21					5.9	10.9	20.3	21.2	19.1	15.9	13.1	11.8	10.0	3.2	2.8	2.5	15.1	14.8	15.4	1.1	0.8	1.0	49.8
Internet																													
Info Edge	ADD	1,468	1,425	(2.9)	179	2.6	122	23	26	33	33.3	14.9	27.5	65.2	56.8	44.5	54.9	43.0	32.5	8.5	6.7	6.1	13.4	13.2	14.3	0.4	0.6	0.6	2.6
Just Dial	ADD	574	610	6.3	39	0.6	67	21	26	30	21.7	23.0	15.0	27.0	22.0	19.1	16.1	12.5	10.1	3.9	3.4	2.9	15.2	16.7	16.6	—	0.5	0.5	47.0
Internet	Cautious				218	3					28.0	17.6	23.0	52.2	44.4	36.1	41.1	32.5	25.5	7.0	5.7	5.1	13.5	12.9	14.2	0.3	0.5	0.6	49.5
Media																													
DB Corp.	REDUCE	246	270	9.6	45	0.6	184	18	20	23	(14.1)	14.9	12.3	14.0	12.2	10.8	7.4	6.6	5.8	2.7	2.5	2.4	19.9	20.7	22.3	5.3	6.8	8.5	0.6
DishTV	ADD	67	90	33.6	124	1.8	1,925	(0.4)	1.8	3.4	(143.0)	514.6	88.2	NM	36.8	19.6	11.1	5.8	4.6	1.9	1.8	1.7	(2.3)	5.1	8.9	—	—	—	7.7
Jagran Prakashan	REDUCE	115	131	13.8	34	0.5	311	10	11	12	(9.3)	10.0	13.6	11.9	10.9	9.6	4.8	4.7	4.0	1.7	1.8	1.7	14.3	15.9	18.2	2.6	4.3	6.5	0.5
PVR	BUY	1,314	1,430	8.9	61	0.9	47	27	38	50	25.5	41.2	32.3	48.9	34.7	26.2	16.5	13.3	11.3	5.7	5.0	4.3	12.3	15.3	17.6	0.2	0.3	0.4	10.5
Sun TV Network	REDUCE	779	925	18.7	307	4.4	394	29	35	39	10.2	20.7	10.9	27.0	22.4	20.2	18.1	15.2	13.2	6.7	6.0	5.4	26.3	28.1	27.9	1.3	2.2	2.6	22.6
Zee Entertainment Enterprises	ADD	514	600	16.7	494	7.1	960	15	17	20	7.8	11.3	17.0	34.2	30.7	26.3	22.2	19.1	16.1	6.5	5.8	5.1	20.3	19.9	20.6	0.5	0.9	1.1	17.5
Media	Attractive				1,065	15					(1.8)	28.7	21.0	32.9	25.5	21.1	15.8	12.1	10.4	4.5	4.1	3.7	13.7	16.3	17.7	0.9	1.5	1.8	59.4

Source: Company, Bloomberg, Kotak Institutional Equities estimates

Kotak Institutional Equities: Valuation summary of KIE Universe stocks

Company	Rating	Price (Rs)			Mkt cap.		O/S shares (mn)	EPS (Rs)			EPS growth (%)			P/E (X)			EV/EBITDA (X)			P/B (X)			RoE (%)			Dividend yield (%)			ADVT 3mo (US\$ mn)
		14-Aug-18	Target price (Rs)	Upside (%)	(Rs bn)	(US\$ bn)		2018	2019E	2020E	2018	2019E	2020E	2018	2019E	2020E	2018	2019E	2020E	2018	2019E	2020E	2018	2019E	2020E	2018	2019E	2020E	
Metals & Mining																													
Coal India	ADD	283	326	15.3	1,755	25.1	6,207	11	27	28	(24.2)	138.2	3.0	25.0	10.5	10.2	18.8	6.7	6.4	7.2	6.6	6.9	26.7	66.1	66.4	5.8	7.1	8.8	14.8
Hindalco Industries	BUY	221	305	37.8	497	7.1	2,229	22	27	31	155.4	25.1	13.6	10.1	8.1	7.1	6.4	5.4	4.7	0.9	0.8	0.7	9.7	10.6	10.8	0.5	0.5	0.5	35.7
Hindustan Zinc	ADD	285	290	1.7	1,205	17.2	4,225	22	22	26	9.3	3.7	14.7	13.3	12.8	11.1	8.2	7.4	6.1	3.4	2.9	2.5	27.2	24.4	24.2	2.8	2.8	2.8	7.7
Jindal Steel and Power	REDUCE	200	215	7.7	193	2.8	968	(8)	8	14	59.3	195.9	68.5	(23.5)	24.5	14.6	9.5	6.8	6.2	0.6	0.6	0.6	(2.7)	2.7	4.3	—	—	—	28.7
JSW Steel	ADD	341	350	2.6	825	11.8	2,417	27	30	27	83.9	10.2	(8.7)	12.7	11.5	12.6	8.1	7.1	7.8	2.9	2.4	2.0	24.8	22.4	17.3	1.0	1.0	1.0	20.5
National Aluminium Co.	ADD	70	80	13.9	136	1.9	1,933	4	9	7	12.7	125.8	(21.1)	17.0	7.5	9.5	7.3	3.4	4.4	1.3	1.2	1.2	7.7	16.8	13.0	8.1	8.5	8.5	9.5
NMDC	REDUCE	102	120	17.6	323	4.6	3,164	12	12	10	43.3	4.2	(14.3)	8.7	8.4	9.7	4.7	5.1	5.9	1.3	1.2	1.2	15.8	15.3	12.4	5.4	5.4	5.4	4.6
Tata Steel	ADD	579	660	14.0	663	9.5	1,205	67	76	85	62.6	12.8	12.1	8.6	8	6.8	6.3	5.9	6.2	1.2	1.0	0.9	17.2	14.3	14.3	1.6	1.7	1.7	71.1
Vedanta	BUY	215	370	72.0	800	11.4	3,717	22	32	39	9.6	49.1	19.7	10.0	6.7	5.6	5.5	4.5	3.7	1.3	1.1	1.0	12.9	18.0	19.4	3.7	4.5	5.4	51.2
Metals & Mining	Attractive				6,396	92					32.3	41.7	7.7	13.5	9.5	8.9	7.6	5.9	5.6	1.9	1.7	1.6	14.3	18.0	17.8	3.4	3.8	4.4	243.9
Pharmaceutical																													
Apollo Hospitals	ADD	1,131	1,090	(3.6)	157	2.3	139	8	20	27	(46.9)	133.5	36.7	134.0	57.4	42.0	23.8	20.0	16.9	4.8	4.6	4.2	3.4	8.2	10.5	0.2	0.4	0.6	8.8
Aster DM Healthcare	BUY	172	240	39.5	87	1.2	505	3	5	7	163.1	64.2	59.2	62.4	38.0	23.9	17.3	12.8	10.3	3.1	2.9	2.6	5.9	7.8	11.4	-	-	-	0.2
Aurobindo Pharma	ADD	631	640	1.4	370	5.3	584	42	40	48	6.0	(4.5)	20.1	15.1	15.8	13.2	10.5	10.7	8.9	3.2	2.7	2.3	23.2	18.4	17.3	0.7	0.8	1.0	21.1
Biocon	SELL	589	330	(44.0)	354	5.1	601	6	8	15	(39.2)	35.9	75.7	95.1	70.0	39.8	42.7	30.5	20.4	6.3	5.9	5.3	6.9	8.7	13.9	0.2	0.5	0.9	22.3
Cipla	BUY	643	680	5.8	518	7.4	805	18	24	31	40.2	34.5	31.0	36.7	27.3	20.8	19.0	15.4	12.2	3.6	3.2	2.9	10.2	12.4	14.6	0.5	0.8	1.0	26.7
Dr Lal Pathlabs	REDUCE	966	900	(6.8)	80	1.2	83	20	24	29	7.0	19.0	17.9	47.2	39.7	33.7	28.8	24.3	20.4	10.2	8.5	7.1	24.6	23.4	23.1	0.5	0.5	0.6	1.6
Dr Reddy's Laboratories	REDUCE	2,279	2,150	(5.7)	378	5.4	166	59	89	118	(18.5)	50.2	32.8	38.6	25.7	19.4	17.8	13.0	9.2	3.0	2.7	2.4	7.8	11.1	12.6	1.1	0.6	0.8	36.1
HCG	REDUCE	246	290	18.1	22	0.3	85	2	2	4	(40.0)	39.8	80.3	157.0	112.3	62.3	21.1	18.1	15.0	4.1	3.9	3.7	2.8	3.5	6.1	—	—	—	0.2
Laurus Labs	ADD	447	500	11.8	47	0.7	106	16	16	29	(11.9)	2.4	79.9	28.2	27.5	15.3	13.8	12.7	8.8	3.2	2.9	2.4	11.9	10.9	17.1	—	—	—	0.6
Lupin	REDUCE	837	800	(4.4)	378	5.4	450	38	27	39	(32.9)	(28.9)	44.0	21.9	30.9	21.4	13.5	14.5	10.5	2.8	2.6	2.3	12.6	8.6	11.4	1.1	0.5	0.7	41.3
Narayana Hrudayalaya	ADD	246	265	7.8	50	0.7	204	3	3	6	(38.1)	23.0	103.2	97.7	79.5	39.1	27.0	22.6	15.8	4.8	4.6	4.1	5.1	5.9	11.0	—	—	—	0.3
Sun Pharmaceuticals	REDUCE	602	520	(13.6)	1,444	20.7	2,406	15	17	24	(47.5)	11.1	42.5	39.7	35.7	25.1	23.6	19.4	14.2	3.8	3.5	3.1	9.8	10.2	13.1	0.3	0.6	0.8	51.8
Torrent Pharmaceuticals	NR	1,711	—	—	290	4.1	169	40	47	61	(27.4)	18.0	29.6	42.7	36.2	27.9	23.5	15.8	13.5	6.3	5.5	4.8	15.1	15.3	17.2	0.9	0.6	0.8	6.7
Pharmaceuticals	Neutral				4,175	60					(25.8)	11.2	37.1	35.1	31.5	23.0	19.2	16.3	12.4	3.8	3.4	3.0	10.7	10.9	13.2	0.5	0.6	0.8	217.8
Real Estate																													
Brigade Enterprises	BUY	194	340	75.0	26	0.4	136	11	9	9	(17.7)	(15.1)	(1.6)	17.5	20.7	21.0	10.9	11.1	10.9	1.2	1.1	1.1	7.6	5.5	5.2	1.3	1.3	1.3	0.3
DLF	RS	203	—	—	362	5.2	1,784	20.5	5.3	23.9	427.2	(74.4)	354.6	9.9	38.6	8.5	30.3	53.9	9.5	1.0	1.0	0.9	12.2	2.6	11.3	1.0	1.0	1.0	16.6
Godrej Properties	SELL	718	400	(44.3)	165	2.4	216	10.9	13.3	15.8	13.5	22.1	19.1	66.1	54.2	45.5	(4,405.1)	318.5	165.8	6.9	4.6	4.2	11.1	10.5	9.7	—	—	—	2.0
Oberoi Realty	BUY	480	560	16.8	174	2.5	340	13	62	44	14.0	385.4	(28.0)	37.7	7.8	10.8	28.2	10.7	13.4	2.7	1.8	1.5	7.3	27.4	15.2	0.4	0.4	0.4	2.3
Prestige Estates Projects	ADD	254	315	24.1	95	1.4	375	13	10	10	24.3	(24.2)	8.4	20.2	26.7	24.6	14.3	14.9	15.0	2.0	1.9	1.8	10.3	7.3	7.5	0.6	0.6	0.6	1.1
Sobha	REDUCE	494	510	3.2	47	0.7	95	23	23	36	37.5	2.4	51.7	21.5	21.0	13.9	13.2	12.4	9.7	1.7	2.2	1.9	8.0	9.0	14.8	1.4	1.4	1.4	1.7
Sunteck Realty	REDUCE	463	360	(22.2)	68	1.0	140	15	19	19	4.8	22.4	1.6	30.3	24.8	24.4	19.3	20.7	20.0	2.5	2.3	2.1	9.7	9.5	8.9	0.3	0.2	0.2	2.0
Real Estate	Neutral				937	13					147.2	(19.7)	68.0	17.4	21.7	12.9	25.5	23.4	12.9	1.7	1.5	1.4	9.6	7.1	10.7	0.6	0.6	0.6	25.9

Source: Company, Bloomberg, Kotak Institutional Equities estimates

Kotak Institutional Equities: Valuation summary of KIE Universe stocks

Company	Rating	Price (Rs)	Target price	Upside (%)	Mkt cap.		O/S shares (mn)	EPS (Rs)			EPS growth (%)			P/E (X)			EV/EBITDA (X)			P/B (X)			RoE (%)			Dividend yield (%)			ADVT 3mo (US\$ mn)
		14-Aug-18	(Rs)		(Rs bn)	(US\$ bn)		2018	2019E	2020E	2018	2019E	2020E	2018	2019E	2020E	2018	2019E	2020E	2018	2019E	2020E	2018	2019E	2020E	2018	2019E	2020E	
Technology																													
HCL Technologies	REDUCE	997	1,025	2.9	1,388	19.9	1,409	62	70	74	5.3	12.8	5.0	16.0	14.2	13.5	11.3	9.3	8.5	3.9	3.2	2.8	24.8	24.2	21.8	0.8	0.8	3.1	30.6
Hexaware Technologies	SELL	483	435	(9.9)	143	2.1	302	17	20	23	20.2	18.4	18.0	29.2	24.6	20.9	21.0	18.4	14.6	7.3	6.3	5.4	26.6	27.4	27.8	0.8	1.7	1.7	12.9
Infosys	ADD	1,408	1,400	(0.6)	3,076	44.0	2,175	65	71	78	3.0	9.7	10.4	21.8	19.9	18.0	15.1	13.6	12.2	4.7	4.4	4.0	21.8	23.0	23.5	2.0	3.1	2.8	80.8
L&T Infotech	ADD	1,785	2,000	12.1	309	4.4	175	64	83	94	13.9	30.5	13.0	28.1	21.5	19.0	24.7	16.5	13.9	8.1	6.5	5.3	31.8	33.5	30.7	0.9	1.3	1.5	4.3
Mindtree	ADD	1,010	1,115	10.4	166	2.4	165	35	43	53	37.8	24.9	23.6	29.2	23.4	18.9	21.3	14.7	11.8	6.1	5.2	4.4	21.4	23.9	25.2	1.1	1.3	1.6	22.8
Mphasis	SELL	1,163	825	(29.1)	225	3.2	193	44	53	57	14.4	20.5	7.1	26.5	22.0	20.6	19.2	16.2	14.4	4.1	4.3	3.9	14.6	18.7	19.9	1.7	1.7	2.1	10.8
TCS	REDUCE	2,004	1,790	(10.7)	7,671	109.8	3,829	67	82	89	1.1	21.2	8.8	29.7	24.5	22.5	22.1	17.9	16.5	8.8	7.7	7.6	29.4	33.4	33.8	1.2	2.0	3.6	95.4
Tech Mahindra	ADD	673	785	16.7	594	8.5	891	43	46	55	33.1	8.3	18.2	15.8	14.6	12.3	11.6	8.7	7.0	3.2	2.7	2.3	21.5	20.2	20.5	2.1	1.4	1.5	36.0
Wipro	REDUCE	284	295	3.7	1,287	18.4	4,507	17	19	22	(3.1)	11.8	14.6	16.8	15.0	13.1	10.7	9.4	8.2	2.7	2.3	2.1	16.0	16.4	16.8	0.4	0.5	3.5	12.4
Technology	Cautious				14,858	213					1.6	13.1	9.7	23.2	20.5	18.7	16.9	14.1	12.7	5.5	4.9	4.5	23.7	23.8	24.2	1.3	1.9	3.1	306.1
Telecom																													
Bharti Airtel	ADD	367	445	21.4	1,465	21.0	3,997	5	(6)	(4)	(42.9)	(221.5)	28.8	77.4	(63.7)	(89.6)	8.2	9.6	8.1	2.1	2.2	2.3	2.8	(3.4)	(2.5)	1.5	0.3	(0.2)	28.1
Bharti Infratel	REDUCE	284	285	0.4	525	7.5	1,850	14	13	12	(7.4)	(4.8)	(8.5)	20.6	21.7	23.7	7.5	8.1	8.5	3.1	3.2	3.2	15.7	14.6	13.7	5.1	3.7	3.4	11.4
IDEA	REDUCE	52	45	(13.5)	227	3.2	4,359	(10)	(17)	(17)	(656.8)	(75.6)	(2.4)	(5.4)	(3.1)	(3.0)	12.1	34.7	29.3	0.8	1.0	1.6	(16.0)	(29.7)	(41.1)	—	—	—	15.7
Tata Communications	ADD	566	660	16.7	161	2.3	285	2	0	3	(84.3)	(77.5)	694.2	344	1,526.6	192.2	10.3	11.1	9.7	32.3	(70.2)	(95.4)	4.5	7.8	(42.1)	1.1	1.1	1.3	3.8
Telecom	Cautious				2,378	34					(94.7)	(2,384.5)	5.0	756.1	(33.1)	(34.8)	8.7	10.9	9.6	2.1	2.3	2.5	0.3	(6.9)	(7.2)	2.1	1.1	0.6	59.1
Utilities																													
CESC	BUY	909	1,180	29.7	121	1.7	133	87	115	128	67.1	31.7	11.6	10.4	7.9	7.1	7.6	5.7	5.0	0.8	0.8	0.7	7.9	10.0	10.4	1.4	1.4	1.4	5.6
JSW Energy	REDUCE	69	70	1.5	113	1.6	1,640	3.1	5.1	6.5	(19.2)	65.9	26.8	22.5	13.6	10.7	7.0	5.8	4.8	1.0	0.9	0.9	4.7	7.2	8.5	-	-	-	1.5
NHPC	ADD	25	30	20.0	256	3.7	10,260	2.4	3.1	3.2	(17.3)	26.9	1.8	10.2	8.1	7.9	9.4	7.4	7.2	0.9	0.8	0.8	8.5	10.4	10.2	5.6	7.0	7.0	2.0
NTPC	BUY	157	190	21.1	1,294	18.5	8,245	11	15	16	(7.6)	30.9	4.4	13.8	10.5	10.1	11.1	8.6	8.0	1.3	1.2	1.1	9.5	11.6	11.3	3.6	2.8	3.0	13.0
Power Grid	BUY	187	250	33.5	979	14.0	5,232	16	19	21	9.6	19.3	13.6	11.9	10.0	8.8	8.5	7.2	6.6	1.8	1.6	1.5	15.8	17.1	17.5	2.8	3.3	3.8	28.9
Tata Power	BUY	69	90	30.9	186	2.7	2,705	10.7	6.0	7.0	80.7	(43.7)	15.6	6.4	11.4	9.9	8.5	10.5	10.0	0.6	1.1	1.0	21.4	10.1	10.6	—	—	—	4.5
Utilities	Attractive				2,949	42					4.5	18.6	8.8	11.9	10.1	9.3	9.2	7.8	7.2	1.2	1.2	1.1	10.2	11.9	12.0	3.1	3.0	3.2	55.5

Source: Company, Bloomberg, Kotak Institutional Equities estimates

Kotak Institutional Equities: Valuation summary of KIE Universe stocks

Company	Rating	Price (Rs)	Target price	Upside (%)	Mkt cap.		O/S shares (mn)	EPS (Rs)			EPS growth (%)			P/E (X)			EV/EBITDA (X)			P/B (X)			RoE (%)			Dividend yield (%)			ADVT 3mo (US\$ mn)																																							
		14-Aug-18	(Rs)		(Rs bn)	(US\$ bn)		2018	2019E	2020E	2018	2019E	2020E	2018	2019E	2020E	2018	2019E	2020E	2018	2019E	2020E	2018	2019E	2020E	2018	2019E	2020E																																								
Others																																																																				
Astral Poly Technik	SELL	1,145	640	(44.1)	137	2.0	120	15	19	25	20.8	30.2	28.8	78.1	60.0	46.6	43.8	32.2	25.6	13.5	10.6	8.7	18.8	19.8	20.5	0.1	0.1	0.1	1.1																																							
Avenue Supermarts	SELL	1,576	860	(45.4)	983	14.1	624	13	16	20	47.9	28.6	26.4	125.3	97.5	77.1	73.4	56.2	44.1	21.2	17.4	14.2	18.5	19.6	20.3	—	—	—	—																																							
Bayer Cropscience	REDUCE	4,202	4,100	(2.4)	166	2.4	34	88	106	130	6.4	20.5	23.1	48.0	39.8	32.4	39.5	29.2	23.8	8.1	7.0	6.0	15.7	18.9	20.0	0.4	0.5	0.6	0.5																																							
Dhanuka Agritech	ADD	545	650	19.3	27	0.4	49	26	27	31	7.7	3.9	15.4	21.2	20.4	17.7	15.5	14.9	12.2	4.2	3.7	3.2	21.9	19.2	19.2	1.0	1.0	1.2	0.2																																							
Godrej Agrovet	ADD	606	640	5.6	116	1.7	189	12	15	19	(6.9)	28.9	28.8	52.6	40.8	31.7	27.1	22.1	17.3	6.8	6.0	5.1	14.7	15.7	17.4	0.3	0.4	0.5	1.3																																							
Godrej Industries	RS	604	—	—	203	2.9	336	15	16	20	6.8	8.9	24.2	41.4	38.0	30.6	36.9	31.2	34.0	5.6	5.0	4.3	14.4	13.9	15.1	0.3	0.3	0.3	4.7																																							
InterGlobe Aviation	BUY	1,051	1,220	16.1	404	5.8	383	61	50	83	32.1	(17.9)	65.3	17.3	21.0	12.7	9.9	11.9	6.8	5.7	4.6	3.5	42.9	24.1	31.1	0.6	0.5	0.8	21.8																																							
Kaveri Seed	SELL	622	515	(17.2)	41	0.6	66	32	34	34	18.4	7.3	0.1	19.4	18.1	18.1	16.6	15.2	14.5	5.3	4.4	3.8	23.6	26.4	22.4	1.0	1.3	1.6	5.7																																							
PI Industries	BUY	782	875	11.8	108	1.5	138	27	31	40	(20.0)	17.9	26.8	29.4	25.0	19.7	21.7	17.8	13.9	5.6	4.7	3.9	20.7	20.5	21.7	0.4	0.5	0.6	1.7																																							
Rallis India	ADD	193	220	13.8	38	0.5	195	9	10	12	(1.5)	17.2	19.4	22.4	19.1	16.0	13.9	12.6	10.6	3.2	2.9	2.6	14.6	15.8	17.1	1.7	1.9	2.1	0.8																																							
SIS	REDUCE	1,101	1,130	2.6	81	1.2	73	22	33	40	43.3	48.5	21.1	49.1	33.0	27.3	26.4	20.7	17.3	7.8	6.6	5.4	20.1	21.8	21.7	0.2	0.3	0.3	0.7																																							
SRF	BUY	1,932	2,200	13.8	111	1.6	57	80	100	132	(10.4)	23.8	32.2	24.0	19.4	14.7	15.5	11.3	9.0	3.1	2.7	2.4	13.7	15.0	17.3	0.6	0.7	0.8	12.4																																							
Tata Chemicals	ADD	673	760	12.9	172	2.5	255	52	44	51	7.9	(15.3)	14.6	12.9	15.3	13.3	7.2	6.3	5.2	1.5	1.4	1.3	14.0	9.7	10.3	3.3	2.2	2.5	6.8																																							
TeamLease Services	SELL	2,555	1,785	(30.1)	44	0.6	17	43	58	75	28.0	34.2	29.0	59.3	44.1	34.2	61.5	44.7	33.9	9.9	8.1	6.5	18.2	20.1	21.1	—	—	—	1.3																																							
UPL	ADD	610	660	8.1	311	4.4	507	43	49	55	20.9	14.0	12.1	14.2	12.5	11.1	9.9	8.5	7.2	3.4	2.8	2.3	26.4	24.6	22.9	1.3	1.6	1.8	22.3																																							
Vardhman Textiles	ADD	1,148	1,300	13.2	66	0.9	56	103	118	130	(8.0)	14.8	9.7	11.1	9.7	8.8	9.5	7.2	6.6	1.3	1.2	1.1	12.7	13.1	13.0	1.3	1.7	2.6	1.0																																							
Whirlpool	SELL	1,755	1,350	(23.1)	223	3.2	127	28	37	46	13.0	33.9	24.7	63.5	47.4	38.0	37.8	29.1	23.1	12.4	10.3	8.5	21.4	23.7	24.5	0.2	0.4	0.5	1.1																																							
Others					3,229		46					15.9			6.6			26.9			31.3			29.4			23.1			20.4			17.9			14.2			5.7			4.9			4.2			18.3			16.7			18.1			0.5			0.5			0.7			83.3		
KIE universe					113,251		1,620					(4.8)			25.1			27.0			27.6			22.1			17.4			12.9			11.0			9.8			3.1			2.8			2.6			11.3			12.8			14.8			1.3			1.4			1.7					
KIE universe (ex-energy)					99,180		1,419					(6.5)			31.0			33.0			32.3			24.6			18.5			14.4			12.2			10.7			3.5			3.2			2.8			10.7			12.8			15.4			1.1			1.3			1.6					

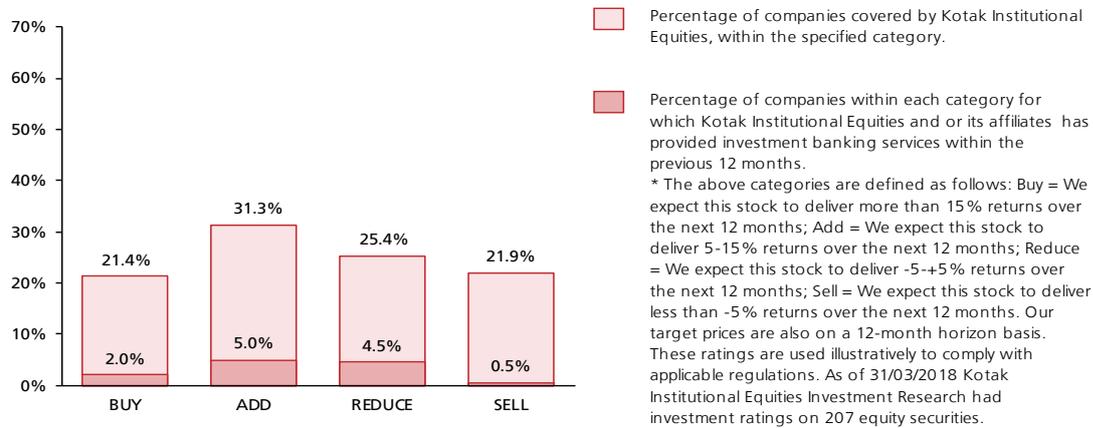
Notes:

- (a) We have used adjusted book values for banking companies.
 (b) 2018 means calendar year 2017, similarly for 2019 and 2020 for these particular companies.
 (c) Exchange rate (Rs/US\$)= 69.88

Source: Company, Bloomberg, Kotak Institutional Equities estimates

Kotak Institutional Equities Research coverage universe

Distribution of ratings/investment banking relationships



Source: Kotak Institutional Equities

As of June 30, 2018

Ratings and other definitions/identifiers

Definitions of ratings

BUY. We expect this stock to deliver more than 15% returns over the next 12 months.

ADD. We expect this stock to deliver 5-15% returns over the next 12 months.

REDUCE. We expect this stock to deliver -5+5% returns over the next 12 months.

SELL. We expect this stock to deliver <-5% returns over the next 12 months.

Our target prices are also on a 12-month horizon basis.

Other definitions

Coverage view. The coverage view represents each analyst's overall fundamental outlook on the Sector. The coverage view will consist of one of the following designations: Attractive, Neutral, Cautious.

Other ratings/identifiers

NR = Not Rated. The investment rating and target price, if any, have been suspended temporarily. Such suspension is in compliance with applicable regulation(s) and/or Kotak Securities policies in circumstances when Kotak Securities or its affiliates is acting in an advisory capacity in a merger or strategic transaction involving this company and in certain other circumstances.

CS = Coverage Suspended. Kotak Securities has suspended coverage of this company.

NC = Not Covered. Kotak Securities does not cover this company.

RS = Rating Suspended. Kotak Securities Research has suspended the investment rating and price target, if any, for this stock, because there is not a sufficient fundamental basis for determining an investment rating or target. The previous investment rating and price target, if any, are no longer in effect for this stock and should not be relied upon.

NA = Not Available or Not Applicable. The information is not available for display or is not applicable.

NM = Not Meaningful. The information is not meaningful and is therefore excluded.

Corporate Office

Kotak Securities Ltd.
27 BKC, Plot No. C-27, "G Block"
Bandra Kurla Complex, Bandra (E)
Mumbai 400 051, India
Tel: +91-22-43360000

Kotak Mahindra (UK) Ltd
8th Floor, Portoken House
155-157 Minories
London EC3N 1LS
Tel: +44-20-7977-6900

Overseas Affiliates

Kotak Mahindra Inc
369 Lexington Avenue
28th Floor, New York
NY 10017, USA
Tel: +1 212 600 8856

Copyright 2018 Kotak Institutional Equities (Kotak Securities Limited). All rights reserved.

- Note that the research analysts contributing to this report may not be registered/qualified as research analysts with FINRA; and
- Such research analysts may not be associated persons of Kotak Mahindra Inc and therefore, may not be subject to NASD Rule 2711 restrictions on communications with a subject company, public appearances and trading securities held by a research analyst account.
- Any U.S. recipients of the research who wish to effect transactions in any security covered by the report should do so with or through Kotak Mahindra Inc and (ii) any transactions in the securities covered by the research by U.S. recipients must be effected only through Kotak Mahindra Inc at vinay.goenka@kotak.com.

This report is distributed in Singapore by Kotak Mahindra (UK) Limited (Singapore Branch) to institutional investors, accredited investors or expert investors only as defined under the Securities and Futures Act. Recipients of this analysis / report are to contact Kotak Mahindra (UK) Limited (Singapore Branch) (16 Raffles Quay, #35-02/03, Hong Leong Building, Singapore 048581) in respect of any matters arising from, or in connection with, this analysis / report. Kotak Mahindra (UK) Limited (Singapore Branch) is regulated by the Monetary Authority of Singapore.

Kotak Securities Limited and its affiliates are a full-service, integrated investment banking, investment management, brokerage and financing group. We along with our affiliates are leading underwriter of securities and participants in virtually all securities trading markets in India. We and our affiliates have investment banking and other business relationships with a significant percentage of the companies covered by our Investment Research Department. Our research professionals provide important input into our investment banking and other business selection processes. Investors should assume that Kotak Securities Limited and/or its affiliates are seeking or will seek investment banking or other business from the company or companies that are the subject of this material and that the research professionals who were involved in preparing this material may participate in the solicitation of such business. Our research professionals are paid in part based on the profitability of Kotak Securities Limited, which include earnings from investment banking and other business. Kotak Securities Limited generally prohibits its analysts, persons reporting to analysts, and members of their households from maintaining a financial interest in the securities or derivatives of any companies that the analysts cover. Additionally, Kotak Securities Limited generally prohibits its analysts and persons reporting to analysts from serving as an officer, director, or advisory board member of any companies that the analysts cover. Our salespeople, traders, and other professionals may provide oral or written market commentary or trading strategies to our clients that reflect opinions that are contrary to the opinions expressed herein, and our proprietary trading and investing businesses may make investment decisions that are inconsistent with the recommendations expressed herein. Kotak Securities Limited has two independent equity research groups: Institutional Equities and Private Client Group. This report has been prepared by the Institutional Equities Research Group of Kotak Securities Limited. The views and opinions expressed in this document may or may not match or may be contrary with the views, estimates, rating, target price of the Private Client Group.

In reviewing these materials, you should be aware that any or all of the foregoing, among other things, may give rise to real or potential conflicts of interest. Additionally, other important information regarding our relationships with the company or companies that are the subject of this material is provided herein.

This material should not be construed as an offer to sell or the solicitation of an offer to buy any security in any jurisdiction where such an offer or solicitation would be illegal. We are not soliciting any action based on this material. It is for the general information of clients of Kotak Securities Limited. It does not constitute a personal recommendation or take into account the particular investment objectives, financial situations, or needs of individual clients. Before acting on any advice or recommendation in this material, clients should consider whether it is suitable for their particular circumstances and, if necessary, seek professional advice. The price and value of the investments referred to in this material and the income from them may go down as well as up, and investors may realize losses on any investments. Past performance is not a guide for future performance, future returns are not guaranteed and a loss of original capital may occur. Kotak Securities Limited does not provide tax advice to its clients, and all investors are strongly advised to consult with their tax advisers regarding any potential investment. Certain transactions - including those involving futures, options, and other derivatives as well as non-investment-grade securities - give rise to substantial risk and are not suitable for all investors. The material is based on information that we consider reliable, but we do not represent that it is accurate or complete, and it should not be relied on as such. Opinions expressed are our current opinions as of the date appearing on this material only. We endeavor to update on a reasonable basis the information discussed in this material, but regulatory, compliance, or other reasons may prevent us from doing so. We and our affiliates, officers, directors, and employees, including persons involved in the preparation or issuance of this material, may from time to time have "long" or "short" positions in, act as principal in, and buy or sell the securities or derivatives thereof of companies mentioned herein. Kotak Securities Limited and its non US affiliates may, to the extent permissible under applicable laws, have acted on or used this research to the extent that it relates to non US issuers, prior to or immediately following its publication. Foreign currency denominated securities are subject to fluctuations in exchange rates that could have an adverse effect on the value or price of or income derived from the investment. In addition, investors in securities such as ADRs, the value of which are influenced by foreign currencies affectively assume currency risk. In addition options involve risks and are not suitable for all investors. Please ensure that you have read and understood the current derivatives risk disclosure document before entering into any derivative transactions.

Kotak Securities Limited established in 1994, is a subsidiary of Kotak Mahindra Bank Limited. Kotak Securities is one of India's largest brokerage and distribution house. Kotak Securities Limited is a corporate trading and clearing member of BSE Limited (BSE), National Stock Exchange of India Limited (NSE), MSEI a. Our businesses include stock broking, services rendered in connection with distribution of primary market issues and financial products like mutual funds and fixed deposits, depository services and Portfolio Management. Kotak Securities Limited is also a depository participant with National Securities Depository Limited (NSDL) and Central Depository Services (India) Limited (CDSL). Kotak Securities Limited is also registered with Insurance Regulatory and Development Authority as Corporate Agent for Kotak Mahindra Old Mutual Life Insurance Limited and is also a Mutual Fund Advisor registered with Association of Mutual Funds in India (AMFI). Kotak Securities Limited is registered as a Research Analyst under SEBI (Research Analyst) Regulations, 2014.

We hereby declare that our activities were neither suspended nor we have defaulted with any stock exchange authority with whom we are registered in last five years. However SEBI, Exchanges and Depositories have conducted the routine inspection and based on their observations have issued advise letters or levied minor penalty on KSL for certain operational deviations. We have not been debarred from doing business by any Stock Exchange / SEBI or any other authorities; nor has our certificate of registration been cancelled by SEBI at any point of time.

We offer our research services to primarily institutional investors and their employees, directors, fund managers, advisors who are registered with us

Details of Associates are available on our website i.e. www.kotak.com

Research Analyst has served as an officer, director or employee of subject company(ies): No

We or our associates may have received compensation from the subject company(ies) in the past 12 months.

We or our associates have managed or co-managed public offering of securities for the subject company(ies) in the past 12 months. YES

We or our associates may have received compensation for investment banking or merchant banking or brokerage services from the subject company(ies) in the past 12 months. We or our associates may have received any compensation for products or services other than investment banking or merchant banking or brokerage services from the subject company(ies) in the past 12 months. We or our associates may have received compensation or other benefits from the subject company(ies) or third party in connection with the research report.

Our associates may have financial interest in the subject company(ies).

Research Analyst or his/her relative's financial interest in the subject company(ies): No

Kotak Securities Limited has financial interest in the subject company(ies) at the end of the month immediately preceding the date of publication of Research Report: YES

Our associates may have actual/beneficial ownership of 1% or more securities of the subject company(ies) at the end of the month immediately preceding the date of publication of Research Report.

Research Analyst or his/her relatives has actual/beneficial ownership of 1% or more securities of the subject company(ies) at the end of the month immediately preceding the date of publication of Research Report: No

Kotak Securities Limited has actual/beneficial ownership of 1% or more securities of the subject company(ies) at the end of the month immediately preceding the date of publication of Research Report: No

Subject company(ies) may have been client during twelve months preceding the date of distribution of the research report.

A graph of daily closing prices of securities is available at www.nseindia.com and <http://economictimes.indiatimes.com/markets/stocks/stock-quotes>. (Choose a company from the list on the browser and select the "three years" icon in the price chart).

Kotak Securities Limited. Registered Office: 27 BKC, C 27, G Block, Bandra Kurla Complex, Bandra (E), Mumbai 400051. CIN: U99999MH1994PLC134051, Telephone No.: +22 43360000, Fax No.: +22 67132430. Website: www.kotak.com / www.kotaksecurities.com. Correspondence Address: Infinity IT Park, Bldg. No 21, Opp. Film City Road, A K Vaidya Marg, Malad (East), Mumbai 400097. Telephone No: 42856825. SEBI Registration No: NSE INB/INF/INE 230808130, BSE INB 010808153/INF 011133230, MSE INE 260808130/INB 260808135/INF 260808135, AMFI ARN 0164, PMS INP000000258 and Research Analyst INH000000586. NSDL/CDSL: IN-DP-NSDL-23-97. Compliance Officer Details: Mr. Manoj Agarwal. Call: 022 - 4285 8484, or Email: ks.compliance@kotak.com. Investments in securities market are subject to market risks, read all the related documents carefully before investing.

In case you require any clarification or have any concern, kindly write to us at below email ids:

Level 1: For Trading related queries, contact our customer service at 'service.securities@kotak.com' and for demat account related queries contact us at ks.demat@kotak.com or call us on: Toll free numbers 18002099191 / 1800222299 and 18002099292

Level 2: If you do not receive a satisfactory response at Level 1 within 3 working days, you may write to us at ks.escalation@kotak.com or call us on 022-42858445 and if you feel you are still unheard, write to our customer service HOD at ks.servicehead@kotak.com or call us on 022-42858208.

Level 3: If you still have not received a satisfactory response at Level 2 within 3 working days, you may contact our Compliance Officer (Name: Mr. Manoj Agarwal) at ks.compliance@kotak.com or call on 91-(022) 4285 8484.

Level 4: If you have not received a satisfactory response at Level 3 within 7 working days, you may also approach CEO (Mr. Kamlesh Rao) at ceo.ks@kotak.com or call on 91-(022) 4285 8301.

First Cut notes published on this site are for information purposes only. They represent early notations and responses by analysts to recent events. Data in the notes may not have been verified by us and investors should not act upon any data or views in these notes. Most First Cut notes, but not necessarily all, will be followed by final research reports on the subject. There could be variance between the First cut note and the final research note on any subject, in which case the contents of the final research note would prevail. We accept no liability for the contents of the First Cut Notes.

For further disclosure please view <https://kie.kotak.com/kinsite/index.php>