

FUNDAMENTAL MARKET UPDATE

August 2020



Top Picks

Company	CMP (₹)	TP (₹)
Auto		
Endurance Technologies	1,093	1,297
Swaraj Engines	1,634	1,891
Banking/NBFC		
Cholamandalam Inv	241	280
IDFC First Bank	32	36
Chemicals/Agro Chemicals		
PI Industries	1,982	2,416
FMCG		
Britannia Industries	3,827	4,220
IT		
Persistent Systems	1,050	1,276
Zensar Technologies	178	204
Pharma & Healthcare		
Alembic Pharma	1,002	1,400
Metropolis Healthcare	1,790	2,156
Telecom/ Others		
Chalet Hotels	165	200
Hawkins cooker	4,918	5,682
Inox Leisure	294	350
JK Lakshmi cement	280	328
Reliance Industries	2,112	2,366
VIP Industries	303	348

Source: Company, Angel Research

Note: Closing price as on 27th August, 2020

Economic recovery led rally expected to continue

Expectations of further improvement in economic activities along with the possibility of a vaccine sometimes by end of 2020 or early 2021 has led to the rally becoming more broad based recently. While we see continued momentum in sectors with strong revenue visibility like IT, Pharma and Telecom, beaten down sectors like aviation, hotels and retail have also started out performing the markets. We expect the recovery theme to play out over the next few quarters and are adding Chalet Hotels, Inox Leisure, Hawkins cooker and VIP industries to the portfolio. These companies belong to the worst impacted sector but are market leaders with strong business franchises and available at prices which are significantly below their pre Covid levels.

Sectors with revenue visibility will continue to outperform markets

Though the rural, essential and digital theme have played out along expected lines since the beginning of the crisis we believe that there are a clear case for further upsides in most sectors given revenue visibility and strong growth prospects. We expect rural focused sectors like Agrochemicals, two wheelers and tractors along with IT Pharma and Telecom will continue to do well given strong demand dynamics.

Current phase of global rally led by improvement in economic activities

Global markets have recovered sharply from the lows in March with the S&P 500 at all time highs and is currently trading ~8% higher than its Jan closing levels. While the initial phase of the rally from the March lows was led by fed induced liquidity the second phase of the rally from July was driven by improvement in the global economy.

While India too has witnessed improvement in economic activities from April lows we are still well behind most developed countries in terms of recovery to pre Covid levels. However pent up demand along with inventory buildup prior to the festive season and gradual opening up of the services sector should lead to further improvement in economic activities over the next couple of months.

Increase in recovery rate coupled with improved visibility on vaccine is positive

While there has been a surge in new cases in India post unlocking there has also been a sharp increase in recovery rates to over 75% along with drop in mortality rates. Moreover there has been positive development on the vaccine front with three promising vaccine which are at various stages of development and markets are building in the possibility that vaccination could start in the beginning of 2021.

Leading to rally in cyclical and beaten down sectors on recovery hopes

Market rally has become broader based due to positive news flow on vaccine and expectations of continued economic recovery due to pent up demand and further opening of the services sector. While we expect that cyclical and beaten down sectors will continue out performing markets for some more time we believe that one should take a stock specific approach and buy into the leaders in the sector which have strong business franchises.

Key risks which can derail the recovery rally are 1) Delay in vaccine production as compared to timelines expected by markets 2) Growth faltering significantly as compared to market expectations post festive season.

Sectors with revenue visibility have outperformed markets post Covid-19

Lockdown due to Covid-19 crisis had an adverse impact on most part of the economy

As expected sectors with strong revenue visibility have outperformed markets

The Covid -19 outbreak globally this year had an unprecedented impact on global economy and markets. As the rapid spread of the virus risked overwhelming healthcare in various countries given the infectious nature of the disease only option was to implement strict social distancing measures. However such measures brought the world to a virtual standstill and hurt the global economy substantially.

Given the lockdowns significant portion of the economy barring a few were adversely impacted. Therefore sector specific investment strategy was the key in such unprecedented times with a clear focus on sectors which were either

1. Rural Focused
2. Essential in nature
3. Benefitted from adoption of work from home (Digital)

Sectors like FMCG and Pharma which are essential in nature were amongst the least impacted sectors. While FMCG companies did face same headwinds due to distribution related issues, Pharma sector posted a good set of numbers for Q1FY21 led by surge in exports.

Exhibit 1: Essential sectors have been the first to recover

Sector	Recovery in Q1FY21*	Current status**	Comment
FMCG	~95%	~100%	FMCG being an essential item had limited impact due to covid-19 though discretionary demand was impacted adversely.
Pharma	>100%	>100%	Pharma sector benefitted from Covid -19 due to Increase in demand for API along with strong growth in US/EU markets

Source: Company, Angel Research; *Revenues as a percentage of Q1FY20, ** Revenues in Jul/Aug as per management interaction

Rural focused sectors also continued to do well though two wheeler and tractor numbers were adversely impacted due to total lockdown in the month of April which had led to zero sales for the month. However as the lockdowns were relaxed we saw strong sequential improvement in sales in June and July. Agrochemicals did extremely well due to bumper Rabi crop and increased food grain procurement by the Government which has led to improvement in rural income.

Exhibit 2: Rural focussed sectors also delivered

Sector	Recovery in Q1FY21*	Current status**	Comment
Agrochemicals	>100%	>100%	Due to government support in the initial phase of lockdown and on the expectation of normal monsoon, demand is robust for this sector
2 wheelers	~38.0%	~88%	Strong demand from rural India, down trading, greater focus on personal mobility along with pent up demand to drive growth for the sector
Tractors	~78%	~100%	Strong demand momentum, aided by positive sentiments due to good Rabi crop, normal monsoon and higher spending by Government

Source: Company, Angel Research; * Revenues as a percentage of Q1FY20, ** Revenues in Jul/Aug as per management interaction

As expected Telecom sector was one of the biggest beneficiary due to the increased adoption of work from home which led to a data boom. Similarly IT companies too managed to seamlessly adapt to work from home while demand side impact was less than feared initially.

Exhibit 3: It and telecom also posted better than expected numbers for Q1

Sector	Recovery in Q1FY21*	Current status**	Comment
IT	>100%	>100%	Companies expected to post sequential growth from Q2 onwards driven by Strong demand due to greater adoption of digital technologies
Telecom	>100%	>100%	We expect sector will continue to do well on the back of increased data consumption. Jio and Airtel will continue to gain market share.

Source: Company, Angel Research; * Revenues as a percentage of Q1FY20, ** Revenues in Jul/Aug as per management interaction

We expect agrochemicals, two wheeler, IT, telecom and tractors will continue to do well

Sectors with revenue visibility will continue to do well

Though the rural, essential and digital theme have played out along expected lines since the beginning of the crisis we believe that there are a clear case for further upsides in most sectors given revenue visibility and strong growth prospects. Continues strength in the rural economy on the back of a good monsoon along with pent up demand bodes well for Agrochemicals, two wheelers and tractors. While FMCG should continue to witness good demand upsides would be limited for the sector given rich valuations.

Similarly we expect IT sector will continue to do well as demand environment continues to remain robust due to greater adoption of digital technologies. Telecom is also expected to continue doing well given increased demand for data and gradual increase in ARPUs due to consolidation in the industry.

Exhibit 4: List of recommended stocks with strong revenue visibility

Company	CMP (₹)	Target (₹)	Rationale
Alembic Pharma	1,002	1,400	We expect growth in demand for Indian API to continue along with recovery in domestic market and growth in US markets led by new launches.
Britannia	3,827	4,220	We expect healthy growth and profitability on the back of increase in market share, strong brand, wide distribution network and new product launches.
Endurance Technologies	1,093	1,297	Pent up demand along with consumer preference for personal transportation is expected to act as tailwinds for domestic 2W, which would benefit Endurance
Pi Industries	1,982	2,416	We remain positive on the company given strong demand for Agrochemicals and continued traction in the CSM business
Swaraj engine	1,634	1,891	Strong recovery in the tractor industry (due to robust Rabi crop production, hike in MSP & the forecast of a normal monsoon) will benefit players like Swaraj Engines.

Source: Company, Angel Research

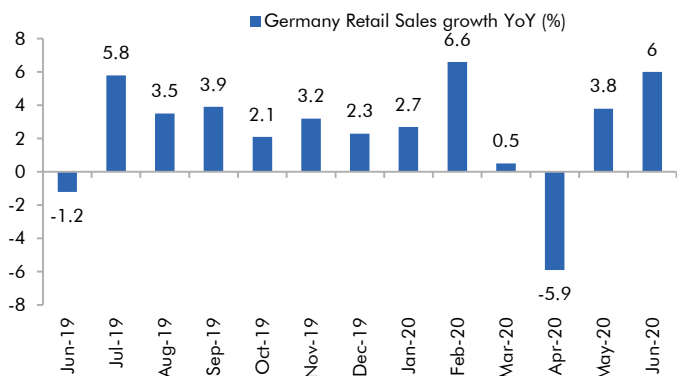
Second phase of global rally led by economic recovery

Global economy has improved significantly since bottoming out in April

Global markets have recovered sharply from the lows in March with the S&P 500 at all time highs and is currently trading ~8% higher than its Jan closing levels. While the initial phase of the rally from the March lows was led by fed induced liquidity the second phase of the rally from July was driven by recovery in the underlying economy which is reflected in high frequency data points like the PMI numbers, Retail sales and Industrial production data.

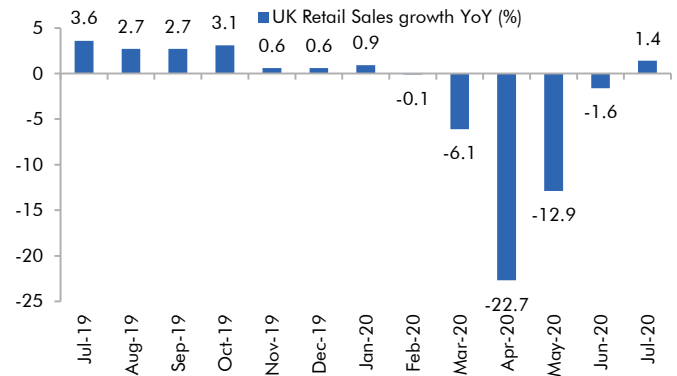
Europe has staged a bounce back as lockdowns were eased - Europe was amongst the first of the developed economies to witness a surge in infections in March after China. As a result many countries like France, Spain & Italy implemented nationwide lockdowns which led to a sharp fall in aggregate demand. However as social distancing norms were gradually eased from May there was a rebound in the economy led by pent up demand.

Exhibit 5: German retail sales above pre Covid levels



Source: Company, Angel Research, Bloomberg

Exhibit 6: UK retail sales also above pre Covid levels

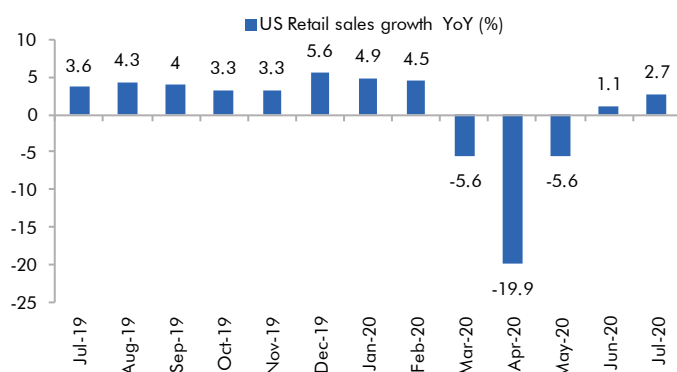


Source: Company, Angel Research, Bloomberg

US economy improved in July contrary to expectations

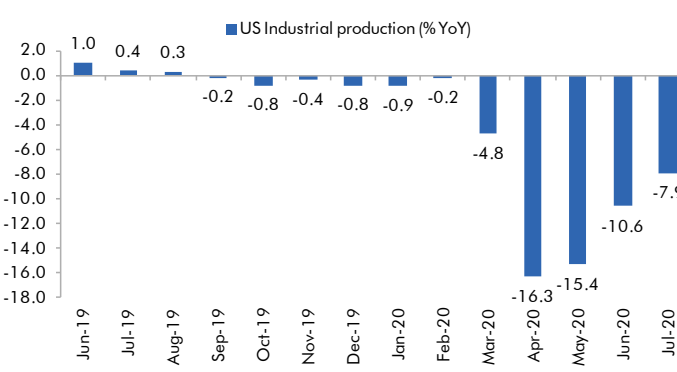
US economy also improving despite a surge in infections in July – The US too continued reporting improvement in the underlying economy despite resurgence of new Covid-19 cases in the US. Despite many states deferring or rolling back their reopening plans the US economy continued to improve contrary to expectations which were reflected in better industrial production and retail sales numbers. The US economy is expected to continue improving over the next few months as reopening plan gets back on track due to drop in new cases.

Exhibit 7: US Retail sales remained strong in July



Source: Company, Angel Research, Bloomberg

Exhibit 8: Manufacturing too recovering with a lag



Source: Company, Angel Research, Bloomberg

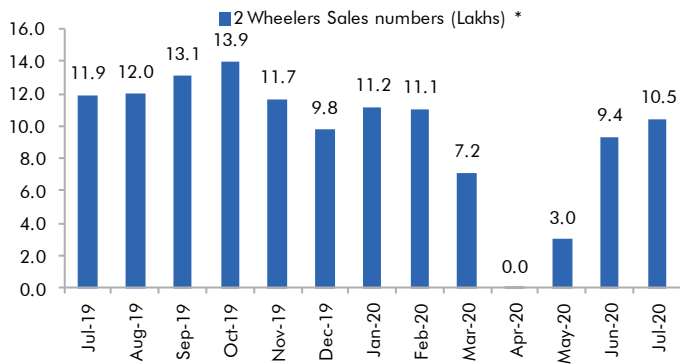
India too has recovered since bottom in April though full blown recovery yet to happen

India - Full blown recovery yet to happen

India which had implemented one of the strictest lockdowns globally was amongst the last to be impacted and therefore amongst the last to recover. As the unlock process was started the economy started gaining traction from the second half of June as supply chain issues were sorted out. The India economy continued to improve through July which was reflected in high frequency data points like PMI numbers, auto sales numbers and cement & steel production

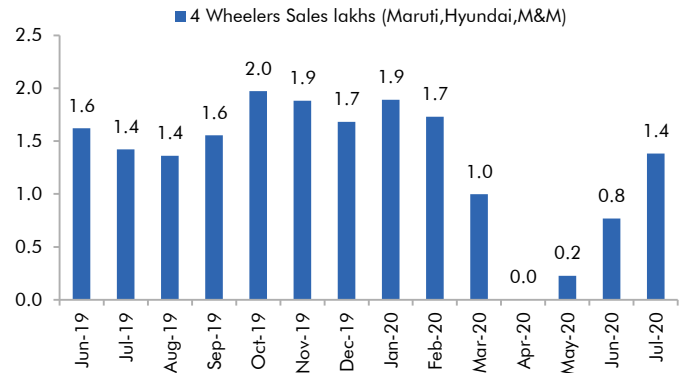
Auto companies reported another month of strong sequential growth with Maruti Suzuki reporting a 1.1% yoy increase in July domestic sales as compared to a 53.7% degrowth in June. Similarly Hero Motocorp also reported a 14% sequential growth in motorcycle sales.

Exhibit 9: 2 wheeler sales almost at pre Covid levels



Source: Company, Angel Research, SIAM * Hero, Bajaj & Eicher motors

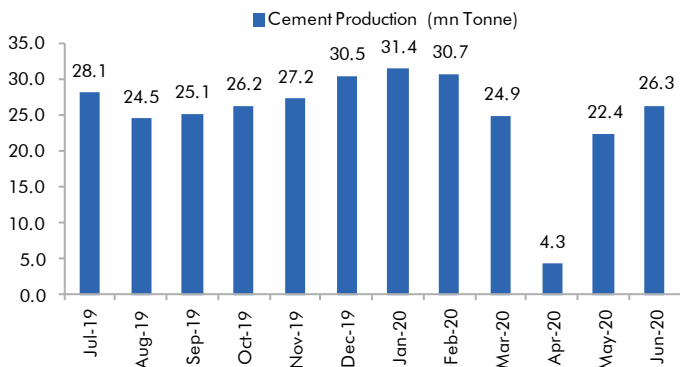
Exhibit 10: PV sales posted strong sequential growth



Source: Company, Angel Research, SIAM

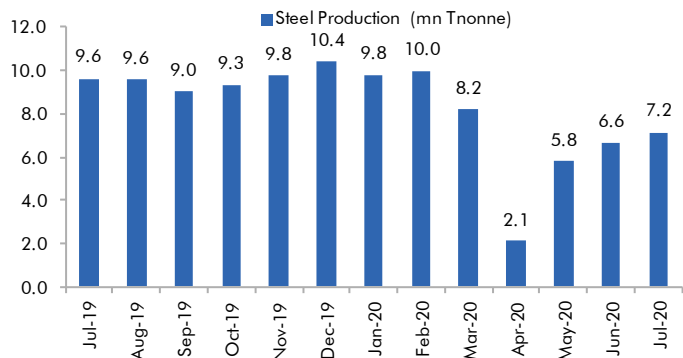
Cement and steel production data also point to continued improvement sequentially. Cement demand has rebounded strongly led by pent up demand and was down by just 7% YoY in Jun'20. Steel production has also been improving though at a slower pace and is down 26% YoY in July.

Exhibit 11: Cement production has improved sharply



Source: Company, Angel Research, SIAM, MOSPI

Exhibit 12: Steel production also improving gradually



Source: Company, Angel Research, World steel organization

Pent up demand and further opening of economy will provide further impetus to economy

Despite the slowdown in the last few days of July we expect that the economy will continue to improve from here on given pent up demand which along with inventory buildup prior to the festive season and gradual opening up of the services sector should lead to further improvement in economic activities over the next couple of months.

Low mortality rates despite surge in new cases is positive
Increase in recovery rate coupled with improved visibility on vaccine is providing confidence to markets

With the Government easing restrictions in a phased manner since Unlock 1.0 in June there has been a surge in new Covid-19 cases in India. However the surge in cases may be partially attributable to increased testing which is leading to more of asymptomatic cases also being recognized which were probably not being counted before.

Promising news flow on vaccine development is encouraging

This is reflected in higher recovery rates and lower death rates in India despite the surge in new Covid-19 cases. Recovery rate in India has improved to over 75% and is expected to improve further. Moreover there has been positive development on the vaccine front as there are three promising vaccine which are at advanced stages of development and there is a very high possibility that vaccination could start in the beginning of 2021.

Exhibit 13: Promising vaccines in advanced stages of development

Sno	Country	Company / Institute	Name of Vaccine	Current Status	Expected Timelines
1	USA	Moderna	mRNA-1273	Phase 3 Human trials	Result of Phase 3 in October 2020
2	UK	University of Oxford	Adenovirus vaccine vector	Phase 3 Human trials	Production as soon as October 2020
3	Russia	Gamaleya Research Inst.	Gam-Covid-Vac Lyo	Phase 3 Human trials	Start of Production by end of year

Source: Angel Research, nytimes.com

Leading to rally in cyclical and beaten downs sectors on recovery hopes

The Government had already been easing restrictions in a phased manner since Unlock 1.0 in June. While growth remained strong through most of July there was some tapering off towards the last 10 days as various states imposed localized lockdowns due to sharp surge in Covid-19 cases.

However most of the localized lockdowns in large metros have been withdrawn as the Covid-19 situation seems to be improving in India. Due to lockdowns in April and May there is pent up demand which along with inventory buildup prior to the festive season and gradual opening up of the services sector should lead to further improvement in economic activities over the next couple of months.

Rally to be more broad based due to expectations of continued economic recovery

Expectations of improvement in economic activities due to easing of restrictions along with the possibility of a vaccine sometimes by the end of 2020 or early 2021 has led to the rally becoming more broad based recently. We are seeing continued participation from cyclical sectors like Auto, construction and consumer durables while beaten down sectors like aviation, hotels, retail and real estate have also recently started out performing the markets.

Exhibit 14: Worst impacted sectors are also reporting improvement in activity levels

Sector	Recovery in Q1FY21*	Current status**	Comment
Consumer durables	~51%	90%+	Seen decent sales recovery in July and August 20 due to pent-up demand. However there could be slowdown post festive season
Aviation/Hotels	9%/17%	15%/35%	Aviation demand expected to remain muted in the near future. However hotel sector is witnessing increase in occupancy in June and July
PV	~23%	~97%	Pent up demand and inventory push prior to festive season should lead to improvement in demand over next few months
Cement	~68%	~90%	Sector expected to reach pre Covid levels demand from Q3FY21. Despite lower volumes, companies able to maintain EBIDTA/tonne
Consumer discretionary (Retailing /Footwear /Liquor /Luggage/)	48% /41% /38% /8%	60% /80% /85% /20%	Expect slow recovery in Consumer discretionary segment due to slowdown in economy. However, we expect quick recovery low-ticket size items and liquor segment
Multiplex	0%	0%	It will take months for the industry to come back at pre covid level although stocks are trading attractive valuation.
Infrastructure	~65%	~80%	Strong order book and robust balance sheet will be crucial for the companies during covid-19 times. We expect private capex to be muted at least for next few months.
Realty	~42%	~60%	Expected muted demand for residential sector though commercial continues to do comparatively better with over 95% collection efficiency

Source: Company, Angel Research * Revenues as a percentage of Q1FY20, ** Revenues in Jul/Aug as per management interaction

As we expect that the recovery theme is expected to play out over the next few quarters we are taking exposure to market leaders from few of the worst impacted sectors which have very strong business franchises and are available at prices which are significantly below their pre Covid levels. While few of the companies are most likely to incur losses for a few more quarters we expect business to normalize for them by the second half of FY2022.

Exhibit 15: Recommended stocks in recovery theme

Company	CMP (₹)	Target (₹)	Rationale
Chaet Hotel	165	200	Company has posted strong sequential Revpar growth in July and future improvement is expected over next few months led by increased occupancy
Inox Leisure	294	350	Share prices have corrected more than 40% as all theatres are closed down due to covid-19 issue. Although, long term fundamentals are intact. Covid-19 can lead to further consolidation in the industry.
Hawkins Cookers	4,912	5,682	Gaining market share with peer, strong demand post Covid-19 and increase in penetration of cooking gas to drive higher growth
JK Lakshmi Cement	280	328	It is trading at a significant discount compared to other north based cement company such as JK Cement as well as historical valuation.
VIP Industries	303	348	Market leader (~50%+ share) with strong brand and wide distribution network. Recent correction provides investment opportunity in high quality stock from long term perspective

Source: Company, Angel Research

Exhibit 16: Top Picks

Company	CMP (₹)	TP (₹)	Rationale
Auto			
Endurance Technologies	1,093	1,297	Pent up demand and consumer preference for personal transportation is positive for domestic 2W companies, which would benefit Endurance.
Swaraj Engines	1,634	1,891	Strong recovery in the tractor industry (due to robust Rabi crop, hike in MSP & a normal monsoon) will benefit players like Swaraj Engines.
BFSI			
Cholamandalam Inv.	241	280	Diversified product mix will help capture growth in LCV, tractor and 2W segment. Adequate capital adequacy (20%+) and declined trend in Cost of fund and strong parentage provide comfort.
IDFC First Bank	32	36	We believe efforts to built retail liability franchise, fresh capital infusion and provision taken on the wholesale book will help to tide over this difficult time.
Chemicals/Agro Chemicals			
PI Industries	1,982	2,416	We remain positive on the company given strong demand for Agrochemicals and continued traction in the CSM business.
FMCG			
Britannia Ind	3,827	4,220	We expect healthy growth and profitability on the back of increase in market share, wide distribution network and new product launches.
IT			
Persistent Systems	1,050	1,276	Company has won deals worth USD 150mn in Q1Y21 and management has highlighted strong deal pipeline which will drive growth in H2FY21.
Zensar Technologies	178	204	We expect strong sequential growth in Q2FY21 driven by ramp up of existing projects and limited exposure to sectors like retail and Oil & gas.
Pharma & Healthcare			
Alembic Pharma	1,002	1,400	We expect growth in demand for Indian API to continue along with recovery in domestic market and growth in US markets led by new launches.
Metropolis Healthcare	1,790	2,156	We are positive on the company given expected long term growth rates of ~15% CAGR, stable margins profile and moderating competitive intensity.
Telecom/ Others			
Chalet Hotels	165	200	Company has posted strong sequential revpar growth in July and future improvement is expected over next few months led by increased occupancy.
Hawkins cooker	4,918	5,682	Gaining market share with peer, strong demand post Covid-19 and increase in penetration of cooking gas to drive higher growth.
Inox Leisure	294	350	Share prices have corrected more than 40% as all theatres are closed down due to covid-19 issue. Although, long term fundamentals are intact. Covid-19 can lead to further consolidation in the industry.
JK Lakshmi Cement	280	328	It is trading at a significant discount compared to other north based cement company such as JK Cement as well as historical valuation.
Reliance Industries	2,112	2,366	Digital and retail business to be key growth driver for the company. Spin off and investment by strategic investor in O2C business is key monitorable.
VIP Industries	303	348	Market leader (~50%+ share) with strong brand and wide distribution network. Recent correction provides investment opportunity in high quality stock from long term perspective

Source: Company, Angel Research

Exhibit 17: Top Picks Valuation Table

	Market Cap (₹ Cr)	CMP (₹)	Sales (₹)		PAT (₹)		ROE (%)		P/E (x)	
			FY21	FY22	FY21	FY22	FY21	FY22	FY21	FY22
Auto										
Endurance Technologies	15,367	1,093	5,884	7,465	281	608	8.7	16.2	54.7	25.3
Swaraj Engines	1,983	1,634	711	899	64	86	16.2	17.1	31.0	23.1
Chemicals/Agro Chemicals										
PI Industries	30,079	1,982	4,411	5,514	661	833	20.3	20.9	45.5	36.1
FMCG										
Britannia Ind	91,125	3,827	13,269	14,624	1,712	1,753	30.5	29.8	53.2	52.0
IT										
Persistent Systems	8,024	1,050	4,159	4,756	415	488	15.4	15.9	19.3	16.4
Zensar Technologies	4,001	178	4,059	4,558	319	384	12.5	14.3	12.5	10.4
Pharma & Healthcare										
Alembic Pharma	19,689	1,002	5,595	6,188	980	981	24.4	21.0	20.1	20.1
Metropolis Healthcare	9,072	1,790	920	1,156	144	217	23.0	27.4	63.1	41.8
Telecom/Others										
Chalet Hotels	3,377	165	484	995	(73)	83	(4.6)	4.9	NA	40.9
Hawkins cooker	2,600	4,918	575	728	51	77	32.5	42.4	51.0	33.8
Inox Leisure	3,024	294	628	2,153	(146)	162	NA	14.5	NA	18.7
JK Lakshmi Cement	3,288	280	3,793	4,306	223	278	14.5	12.3	14.7	11.8
Reliance Industries*	13,387	2,112	3,342	4,241	264	420	5.7	8.7	50.8	31.8
VIP Industries	4,288	303	808	1,650	(136)	108	NA	19.6	NA	39.7

Source: Company, Angel Research * RIL standalone numbers (market cap, revenues & PAT in '00' crore)

Exhibit 18: Top Picks Valuation Table – Banking/NBFC

Particular	Market Cap (₹ Cr)	CMP (₹)	NII (₹ Cr)		PAT (₹ Cr)		EPS (₹)		ROE (%)		P/BV (x)	
			FY21	FY22	FY21	FY22	FY21	FY22	FY21	FY22	FY21	FY22
IDFC First Bank	18,095	32	6,939	8,121	90	1530	0.2	2.7	0.5	8.0	1.1	1.0
Cholamand. Inv. & Fin	19,732	241	3,783	3,962	987	1346	12.0	17.0	11.5	14.1	2.2	2.0

Source: Company, Angel Research

Note: CMP is Closing price as of 27th Aug, 2020

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*Accumulate (5% to 15%)
Reduce (-5% to -15%)*

*Neutral (-5 to 5%)
Sell (< -15)*



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