Company: IndiaMART

Business Slotting: B2B > B2C Asset Light > Asset Heavy Intellectual Prop > Laborious Price Setter > Price Taker Monopoly / Duopoly > Oligopoly

Company Background:

IndiaMART is over 20 years old company (revenue Rs. 500+ Cr.), which operates in B2B e-commerce, commanding a market share of 60%. It has tried various models (like auction model), pivoted with learnings and finally emerged as India's leading B2B e-commerce marketplace with **market share of 60%**.

Buyers and suppliers meet on the platform to engage and trade their products. The IndiaMART service is free for buyers and suppliers are charged with subscription charges to appear higher in the search list.

Suppliers can list themselves for free, but can also take subscription packages like Silver Monthly, Silver Annual, Gold, Platinum to gain higher order traction.

Silver Package => Rs 30k / year =>
Supplier storefront + Unique webpage with personalized URL containing IndiaMART domain name + Access to online payment gateways + 7 RFQ credits per week + Product Listing Priority

Gold Package => Rs 30k to 60k / year =>
Silver Package benefits + TrustSEAL verification + 14 RFQ Credits per week [OR]
Silver Package benefits + Personalized URL without IndiaMART domain + 21 RFQ Credits per week

Platinum Package => Gold++
Gold Package benefits + Higher Priority Listing + More RFQ Credits

IndiaMART is also able to attract companies like JCB, Tata, Mahindra which is automatically drawing attention from other smaller businesses too.

The company receives the payments for full year / multi-year well in advance and typically has this deferred revenue as cash in its balance sheet. This leads to **negative working capital for the company** (no inventories too).
60% of deferred revenue is typically expired in the next 12 months and the remaining 40% is typically expired after the next 12 months.

There is no good alternative to buyers and suppliers currently to source their products through e-commerce and hence IndiaMART commands a huge market share of 60%+. There are 142k paying suppliers on IndiaMART as of Q3FY20, with average ARPU at 40k-45k per year.

Top 10% suppliers among these 142k are Platinum subscribers.

These Platinum subscribers drive around 40% of the company's revenues.
Competitors like Udaan, Walmart Wholesale, Amazon Business, Metro Cash N Carry are entering the B2B E-commerce segment. However, these are focussed on wholesale to distributor to retailer B2B e-commerce of finished goods in FMCG and Apparel category.

Further work => Why is the competition first focussed on wholesale / distributor / retailer B2B than SME B2B? Don't they find favourable economics / markets? Or is it due to IndiaMART already quite ahead on the curve? Ask them their comments on IndiaMART's business.

Value-additive features IndiaMART is next focussed on:

Product Videos => Illiterate people running MSMEs can't have access to technologies like IndiaMART as the buyers can't read the product description. So the company is adding features like Product videos where the suppliers can describe the features of the product in Hindi / local language through videos
Payments => Scaling up 'Pay With IndiaMART' profitably, while charging fees for the payments
Credit => Rope in an external NBFC and provide credit to MSMEs through IndiaMART to ensure stickiness of the customers, while charging fees for the same
SaaS => Create SaaS based features / products to MSMEs and integrate those through IndiaMART. IndiaMART invested in Vyapar, which is an accounting app built for MSMEs.
Differential Pricing => Introduce differential pricing based on industry / location / size of the company instead of charging every company at Rs 30k for Silver subscription.

Operational Metrics:

Registered Suppliers - 55 lakhs in FY19 from 23 lakhs in FY16
Paying Suppliers - 1.3 lakhs in FY19 from 0.72 lakhs in FY16
Paying Suppliers % - 2.3% in FY19 from 3.1% in FY16
ARPU from each supplier - 39k in FY19 from 34k in FY16 (In FY20, this will hit 45k due to one-time price hike of 5k Rs)
Total MSMEs in India about 6 crores and those connected to the Internet are 1 crore.

Churn rate of annual subscribers => 20% per year among annual subscribers
Churn rate of monthly subscribers => 5% per month among monthly subscribers

1688.com is a subsidiary of Alibaba, which dominates the domestic B2B e-commerce in China.
Paying Suppliers in Alibaba - 9.14 lakhs in CY19
Revenues of 1688.com are still growing at 25%-35% rate, however mostly driven by ARPU growth, suggesting scope for lots of incremental value addition possible.

Registered Buyers - 8.27 crores in FY19 from 2.71 crores in FY16
Visits / Buyers - 8.75 in FY19 from 9.66 in FY16
Enquiries / Buyers - 5.42 in FY19 from 4.24 in FY16

Buyer traffic is reasonably distributed across Metros, towns and rural villages.
Seller traffic is focused on Metros and Tier II towns.

Further work on 1688.com => Find out the % of paying suppliers; contribution of Top 10% customers to revenues and trend of ARPU in over past couple of years

Turnaround in FY16:

Three things lead to turnaround of the company in FY16:

1. Pricing of the product
2. Detailed product specification / Transition from classified listing website to product catalog website
3. Behavioural based algorithmic match-making where we started to use suppliers' RFQ consumption behaviour to assess his preferred location and product category over his stated location and stated product category

Examples of Product Catalog website for suppliers:
https://www.indiamart.com/hero-agrotraders/
https://www.indiamart.com/captivtrade-bengaluru/

Further work => Find out the pricing and supplier package methodology prior to FY16 and what were the learnings then?

Customer Industry Trend/Outlook -> ☑ Tailwinds ☐ Headwinds ☑ Secular

IndiaMART revenues depend on the trend of more and more SMEs getting onto the internet and those businesses getting used to run their business through the Internet.

With high internet penetration since FY17 due to the launch of Jio, lots of Indian population (especially the young) are introduced to the Internet. As this population starts to assume SME business responsibility (aka passing onto the next generation), the internet adoption tailwind is to continue for IndiaMART.

Elevator Pitch – *"Company is run by Software Professionals and is playing on SMEs internet adoption theme. About 10% of MSMEs are already registered with the company and 50% of internet-penetrated MSMEs are registered with IndiaMART, with almost no competition. New entrants like Udaan, Flipkar Wholesale are more focussed on distribution of finished products in the FMCG / Apparel category from manufacturers to dealers to retailers, while IndiaMART's focus is on all SMEs, primarily on the manufacturing side. There is lots of scope for increased value addition like providing Credit, building SaaS products to ensure stickiness of the customers. The business has high operating leverage and incremental increase in revenues will keep improving the margins as the company has turned profitable just in FY19, with EBITDA margins of ~10% while globally e-commerce companies operate at EBITDA margins of 40-50%."*

Background of promoter and business theme:

Software Engineer Promoters: Dinesh Agarwal started IndiaMART in the late 1990s and tried various experiments and pivoted the business couple of times before reaching the current stage. For example, some of his experiments include determining the price of the deal using an auction based model (during 1999), providing logistics support through Tolexo.com.

	FY 15-16	FY 16-17	FY 17-18	FY 18-19
Revenue (in Cr.)	251	332	430	548
PBT	-131	-64	-61	54

(Source: Annual Reports)

Further work => Get hold of IndiaMART's financials before FY16 too, to get record of 10 years instead of just 4 years.

Quality of product:

1. Random searches on the platform work very fine without any technical lapses. Enquiring about a product is convenient and receiving a call from various suppliers, if buyer is registered
2. Supplier store-fronts look neat with good description of each product (Product videos is an upcoming feature)
3. Well-known businesses in India are listing their products on the IndiaMART website, which will bring in traction.
   For example: JCB, Tata, Mahindra

Having penetrated 1.4 lakh suppliers as paying customers (1688.com has 9.14 lakh as paying suppliers in China), of which 10% are platinum users, which includes well known companies like JCB, Tata, Mahindra suggests the quality of the product and experience of the users.

Further work => Get on the ground feedback from SMEs on the product. If they are not using the product, find out why they are not using it and what is the product lacking.

BUSINESS ATTRACTIVENESS

1. **Strongly differentiated business model -> High**
   a. Strongest B2B E-commerce player in the country with highest market share
   b. Achieved reasonable scale with 1.4 lakh paying suppliers
   c. Bringing in large companies like Tata, JCB, Mahindra… could bring in higher impact of network effect
   d. Supplier storefronts integrated with e-commerce leads to easy product discoverability for buyers. Further working on product videos could bring in illiterate MSME players, as the videos can be made in Hindi / regional languages
   e. No other known player in MSME B2B focus as all competition like Udaan, Flipkart Wholesale is focussed on Wholesale - Retail B2B of finished FMCG / Apparel goods

f. Future work of the company on differential pricing could bring in more customers

2. **Competitive Position getting stronger/weaker -> Stronger**
    a. Competition seems to be more focussed on B2B e-commerce of finished FMCG / Apparel goods from distributor to retailer
    b. Most of the competitors just started this business and facing headwinds just during their initial stages due to COVID-19 crisis

3. **Next Level of business -> High**
    a. Should become the default / standard choice of B2B E-commerce for SMEs and due to high operating leverage, the profitability of the company should also increase a lot if revenues take off. Lots of scope to add further value to the customers.

4. **Value Migration Curve -> High**
    a. Product Videos could bring in MSMEs run by illiterate people who don't have the capability to read the product description
    b. Differential Pricing could bring in MSMEs who find Rs 30k / year as an expensive proposition. Factoring in Industry / Size / Location and pricing the subscription could bring in more customers
    c. Providing credit access to MSMEs could bring in more customers, give ability to charge fees for the same and ensure stickiness of the customer
    d. Providing company-owned Payment interface to customers could create additional revenue stream
    e. Creating SaaS based products and integrating through IndiaMART could bring in additional revenue in-flows (Eg: Vyapar integrated through IndiaMART)

5. **Quality of earnings -> High**
    a. Bargaining power -> Lack of competition. Increase of Rs 5k across all subscription packages in 2019 was received reasonably well.
    b. Moving Average Sales -> Revenues accounted for the quarter actually moving averages of the collections as there is a lot of deferred revenue i.e. customers prepay the amount when they buy multi-year or multi-quarter packages
    c. Reasonable Pricing Power -> As the company moves ahead on the value migration curve, it should be able to charge the customers more and more. 1688.com's revenues in China sitll grow at 25%-35%
    d. When the company turned profitable, it jumped to EBITDA margins of 10%. With global comparable companies like Alibaba, Facebook, Naukri margins at 40% - 50%, it should be achievable for IndiaMART

6. **Key growth drivers**
    a. Internet Adoption by MSMEs -> Lots of internet adoption going on in the country after launch of Jio and more and more MSMEs are getting tech-enabled. This trend should bring in more MSMEs onto the platform ***-> Medium***
    b. Value additive migration -> Lots of scope for higher value-addition like Credit, Differential pricing, SaaS, Product Videos, Payments… ***-> Medium***

7. **Intellectual Property – High**

    Software design and development is high value add work. And in IndiaMART's situation, there is a lot of scope for incremental value addition, which will further increase the value of the IP owned by the company.

8. **Profitability Drivers**

    P&L Overview:

	Mar-16	Mar-17	Mar-18	Mar-19	CAGR %
Revenue from Operations	245.75	317.76	410.51	507.42	27%
Net gain on financial assets	3.72	11.91	16.16	37.32	116%
Other Income	1.54	2.26	2.86	3.65	33%
Total Revenue	251.01	331.94	429.53	548.39	30%
Employee benefits	181.92	209.67	194.86	229.98	8%
Employee benefits Margin %	26%	34%	53%	55%	
D&A	3.68	4.63	2.89	4.13	4%
Net loss on financial assets	7.09	19.28	122.86	65.26	110%
Other Expenses	189.43	162.5	169.02	195.09	1%
Tax	0.45	0.2	-115.22	33.88	-

PAT	-131.57	-64.35	54.76	20.04	-

(Source: Annual Report & IPO Prospectus)

a. **Employee Benefits**

Incremental requirement in employees is lower compared to incremental revenue generation capability for software platforms after they reach their initial mass of customers, thus providing scope for high operating leverage.

The company is already benefiting through this operating leverage as one can see it turned profitable in FY19 with PBT margins of 10%. In 9MFY20, the PBT margins have risen to 30%.

As per recent conference call, the company is giving hikes to all employees every June after it turned profitable. Important to retain the employees as this is a value-add business.

The Company started outsourcing the sales representatives as not many people from good educational background are interested in doing SME sales. So the company started outsourcing its sales staff from FY18. For every new 5000 customers, the company may have to hire extra 50-100 people as temporary sales staff.

c. **Operating Leverage - High**

	Mar-16	Mar-17	Mar-18	Mar-19
Sales	251.01	331.94	429.53	548.39
Revenue from Ops	245.75	317.76	410.51	507.42
PBT (without MTM on financial assets)	-124.01	-44.86	62.76	119.18
Operating Leverage				

With incremental operating revenues of 97 crores, the company was able to increase its PBT (without financial assets impact) by 57 crores, suggesting very high operating leverage.

Operating Leverage led by ☑ Asset Turns ☑ Product Mix ☑ Employee Costs

a. **Asset Turns**

	Mar-17	Mar-18	Mar-19
Fixed Asset Turns	33.67	50.14	62.74

Since this is a software product, there is no need for incremental PPE investment to create additional revenues. Focus is on on-boarding more customers onto the platform.

b. Product Mix

As Value Migration Curve was mentioned earlier, there is lots of scope for value-addition generating incremental revenues. Product Videos. Differential Pricing. Credit. Payments. SaaS.

c. Employee Cost

Incremental salary / bonus payout to employees is not the same as incremental revenue, as we are observing in the company's financials, described above.

KEY MONITORABLE

a. Growth => Company's ability to sustain growth rates needs to be monitored. The growth curve has fallen from 30+% to 20+% during the economic slowdown in 2019 and we should check how things pan-out during the COVID-19 crisis
b. MSME Financial Situation => MSMEs will be the most affected during the COVID-19 crisis and may keep a sharp eye on expenses to ensure survival of their businesses
c. Competition => With WalMart, Udaan, Amazon showing interest in this area, need to check their progress and if they will be able to take away IndiaMART's clients
d. Execution of new features to grow up ARPU => Company has been listing out various new value-additive features they'd be working on. Should monitor their progress on the same and check their execution capability
e. Deployment of cash building up in the Balance Sheet => With high operating leverage and deferred revenue, lots of cash is flowing into IndiaMART's balance sheet. Should check on how the company would invest this cash

MANAGEMENT QUALITY

1. **DNA of business**

The company has been growing by playing on the MSME internet adoption theme and has been to get some traction with about 1.42 lakh customers by Q3FY20. Management started this business during the late 90s and have pivoted their business model multiple times over the years to achieve current business performance.

a. **Cost Efficiency Focus – Can't say**

Not much history is available to have a strong view on this one.
IndiaMART did a lot of advertising until FY16 and once they picked up the growth curve post that, they stopped advertising. From FY16-19, raise in salaries of employees is limited too.
From FY20, there is an uptick in employee expenses. There were no advertising expenses post FY16 till date.

b. **Production Efficiency – High**

As a software platform business, the production efficiency / asset turnovers would be high and also there would be a lot of scope to increase it further.

c. **Capital Efficiency/Allocation – Low**

	Mar-17	Mar-18	Mar-19
Sales/Fixed Assets= Fixed Asset Turns	33.67	50.14	62.74
Sales/Total Assets= Asset Turns	1.59	1.12	0.8

From the above table it can be seen that while the company has very high fixed asset turns and increasing further while the total asset turns are very low. This is due to the cash piling up in the balance sheet while the company turns profitable. There is not much history on how the company will use this cash as it just turned profitable. It invested 33 crores in a startup called Vyapar which is an accounting software product for SMEs. We need to observe how the company spends further cash it will generate.

Following is the concise balance sheet of the company for the last four years.

	Mar-16	Mar-17	Mar-18	Mar-19
Liabilities				
Equity + R&S	-327.1	-390	-321.3	159.9
Borrowings	0	0	0	0
Other Liabilities	521.7	610.9	863.9	660.9

Assets				
Net Block + CWIP	9.8	7.5	7.3	8.5
Investments	128.6	136.3	311.1	607.4
Cash	18.7	17.7	46.7	40.2
Other Assets	64.3	66.9	184.9	173.2

Since FY18, the company has been generating lots of cash which is being driven into financial investments. The net worth of the company just turned positive in FY19. There is a surge in Other Assets since FY18 as the company started accounting deferred tax assets. No dividend history as the company just went public.

Further work => Find out what are those deferred tax assets? Why is there a sudden surge in FY18?

d. **Innovation – Low**

Though IndiaMART is a first mover in this area and present since the late 90s. The progress they have achieved is not extraordinary to be honest. The website has a product catalog page for each supplier and good search engine. Some stuff like Product Videos, Payments, Credit are not yet available and their progress in general seems to be slow.

e. **New Revenue Stream/ Geography – Low**

Most of the revenues for the company comes from Metros and Tier II cities. There is a limited contribution of suppliers from small towns and rural areas. Penetration into these areas should help the company scale up and build a stronger network effect. Company is working on features like Product Videos, Differential pricing to onboard MSMEs from small towns and rural areas.

f. **Value Chain Migration – High**

As discussed already, there is a lot of scope for incremental value addition like Credit support, SaaS products, Product Videos, Differential Pricing, Payments….

g. **Strategic Thinking – Low / Can't say**

The company has been in existence for over 20 years operating as a soft monopoly, however it hasn't been able to scale up the business so much. While post 2016 the business has started to perform, the following remains a question why these things were not targeted by the company:

1. Limited features in 20 years - There are so many software companies which build an array of complete products in those 20 years while IndiaMART's main achievement has been the dedicated product catalog website + search / rank algorithm. Is the company moving a bit too slow? (Though they have done quite good in number of suppliers)

2. No Differential Pricing – Differential Pricing is something the management should have thought of very much since the beginning. Blanket pricing of packages could leave out lots of MSMEs from subscribing to IndiaMART.
3. Need to keep an eye on the number of Platinum customers - There is not much data on how the number of Platinum customers moved across the years as these are the ones who bring in a lot of revenue for the company.
4. Payments - The company has been working since a while on “Pay with IndiaMART” and admitted they are unable to scale. In another conf call, they mentioned that the payments market is confused citing that there are lots of payment methods like UPI, Wallet, Credit card…

Further work => Find out how platinum customers moved across the years. Is it increasing in line with the paying customers or its share of paying customers is rising / falling?

h. **Ability to manage downturns – Can’t say**

Not much information is available on the internet on how the management went through their hardships as a private company. They should have had their fair share of hardships as they just turned profitable and were in red until FY18.

Further work => Find out more about management’s story, focussing on how they behaved during tough times? What were the decisions taken and what drove them? Maybe the COVID-19 crisis is an opportunity to understand the management?

i. **Walking the Talk – Can’t say**

The company has been given some guidance in conference calls of FY20 but it is just three quarters since the company went public and difficult to assess in such short periods if they walk the talk or not. Should keep an eye on management’s words during the upcoming quarters and check if they are following it over time.

2. **Execution Skills**

a. **Workforce Handling – Can’t Say**

Management Salary is ~20 crores in FY19, listed below.

Dinesh Gulati - COO - 5.66 crores
Madhup Agrawal - National Head - 4.63 crores
Dinesh Chandra Agarwal - MD - 4.1 crores
Brijesh Kumar Agarwal - Whole Time Director - 2.98 crores
Prateek Chandra - CFO - 2.27 crores
Vikas Aggarwal - National Head - 1.62 crores
Amarinder Singh Dhaliwal - CPO - 1.23 crores
Abhishek Bhartia - SVP - 98.5 lakhs
Sudhir Gupta - SVP - 95.9 lakhs
Amit Jain - SVP - 77.2 lakhs

Interestingly, no median salary is provided in the annual report.

Also, COO and National Head are compensated more than the CEO.
FYI, PAT in FY19 was 54 crores (82 crores excluding impact of financial assets)

b. **Customer Trust/Win – High**

Customer trust is good as they have a decent amount of penetration and were also able to increase customers during the economic slowdown in 2019. The company has iconic business groups like Tata, Mahindra, JCB as customers.

c. **Deeper/Broader customer penetration – Medium**

Though the number of customers are reasonably good, there is still a lot of scope for penetration. 50% of customers are from Metros and 25% from Tier-II cities. Penetration in smaller towns and rural villages is very low and the company can work on that front.

Some initiatives taken by the company in that direction are differential pricing and product videos and needs to be seen on how they will execute it.

Good thing is there is no competition which has already taken out those supplier customers in small towns and rural villages.

d. **Successful Project – Medium**

Though the company has achieved good milestones on an overall basis, it is already established 20+ years ago. The fact that it took 20 years to achieve current state of business is not very impressive

3. Reputation

    a. **Family Business – Low**

    Though Brijesh Kumar Agarwal and Dinesh Agarwal are cousins, the other members on the senior management team are not of the same family.

    Building Software Platforms is high-value add work and one may not find so many high-skilled Tech executives in a single family and there is not much history of successful family-run Software businesses.

    b. **Minority Shareholder Treatment - Can't Say**

    The Company just went public in FY19 and it is very difficult to comment on how they would treat minority shareholders. FY20 is the first operational year after going public.

    Management mentioned in Q1FY20 that they were adopting a dividend policy to distribute to shareholders and paid out Rs 10 per share in March 2020.

At the end of FY19 (before going public), non-promoter senior management professionals do hold shares of IndiaMART and can see some members of ‘Agarwal’ family among Top 10 shareholders. So promoters are not very incentivised to hurt minority shareholders

c. **Corp. Governance – Can’t Say**

Further Work => Find out how seriously Corporate Governance was taken before the company went public?

GROWTH/SCALABILITY

1. **Linear Growth - High**

a. Industry – Growth is linked to internet adoption by SME which is going to grow over the years
b. Market Share – Market share already high at 60%. The only company with lots of cash on the balance sheet. Competitors are startups which are burning a lot of cash. If COVID-19 crisis starts killing B2B e-commerce businesses, IndiaMART may be the last one to declare bankruptcy
c. Margin – Medium but there is high scope for increasing margins
d. Price Increase – High pricing power due to limited alternative options to customers

2. **Expansionary Growth - High**

a. Value Migration – Lots of new value-additive features can be introduced in the product. Product Videos, Credit support, SaaS, Payments….
b. New Geography – Most of the customers are from Metros and Tier-II cities. Lots of scope to increase penetration with supplier customers in small towns and rural villages. Product Videos and Differential Pricing are the right initiatives in that direction
c. New Revenue Stream – Providing additional services like Credit Support, Payments, SaaS could bring in new revenue streams for the company

Business Vulnerability / Strength

1. **Vulnerability:**

a. Nature of business – Long-term slowdown in SME businesses in India could affect the business. The company would still stay cash rich during this period due to deferred revenue arrangement.
b. Due to the company’s nature of developing features slowly, competition funded by VCs may be able to catch up with IndiaMART.

Further work => Spend time on JustDial and understand why it got disrupted. Check if relevant factors are applicable here.

2. **Strengths/opportunities:**

   a. Product usage has been established and the company has a reasonable low churn rate at 20% per annum. Also brought in well established large business groups like Tata / Mahindra as customers
   b. Opportunities exist on the value migration curve. As mentioned, Credit Interface / SaaS / Payments….

VALUATION

Undervaluation : Fairly Valued to Overvalued

Source: Screener

Current TTM P/E (of Q3FY20) is at 50 which is high on an absolute basis.
However, if one factors in strong topline growth of ~25% + huge operating leverage leading to lots of margin expansion + deferred revenue leading to negative working capital and lots of cash on the balance sheet, it is not very expensive.

There may not be much upside on re-rating the P/E parameter.
However, topline growth + further margin expansion should take care of disproportionate returns.

Valuations to be led by:

1. **Earnings Trajectory**

a. Management was guiding revenue growth of ~25%, coupled with operating leverage. Long-term aspiration for EBITDA margins are 40%-50%. Management quoted examples like Facebook. Earnings growth is important for the P/E multiple to sustain. Any put-off by earnings could potentially lead to de-rating

b. Revenue Growth / Degrowth aka movement is generally as it is looked at as Moving Average of 20-21 months of collections. This is due to the concept of deferred revenue where customers can buy the subscription for multiple months / years at one-go while buying IndiaMART subscription packages

2. **Value Migration**

a. There is a possibility for higher multiple to the company if the company is swift in adding more features to hook the customers

3. **Re-rating**

a. Unlikely, unless the company works on lots of value-additive features to hook the customer to the product at multiple levels. Or if the company uses the cash wisely which is building up in the balance sheet.

Valuation Overhang: Promoter Trust. High Salaries.

1. Promoter Trust: It is less than a year since the company went public. Needs to be seen on how the promoter treats the minority shareholder. Not much history is available on the promoter's

execution / discipline / stance / culture / ethics on the internet. Might need us to attend AGM and ask tough questions to the management team to get an idea

Further work => Attend AGM to talk to management / other senior executives to understand their discipline / culture / ethics and history of the company

2. High Salaries:
    a. High salaries are being paid to the management. Senior management put together made about ~20 crores in FY20 while PAT was 82 crores (54 crores including impact of financial assets)

Valuation Support:
Dividend. Capital Allocation

- **Dividend:** Company has just went public in Q1FY20 and started paying dividend in Q4FY20 at 0.5% yield. This could be a support as 0.5% yield for a high growth company is good.
- **Capital Allocation**: Company has about 800 crores of cash (tied with contract obligations / liabilities due to deferred revenue) on balance sheet while valuation is at 6000 crores. This cash can act as a support for valuation of the company

Risk and Mitigations

1. **Business Risks**

a. **Supply and/or demand disruption - Low**

The Company's revenues are fairly diversified across industries. No single industry contributes more than 10% to the company's revenues. Important parameter to watch out for company's product demand is Indian SMEs financial condition

b. **Single Point of Failure - Medium**

Revenues are diversified. Only single point of failure is single corporate office located only at Delhi

c. **Environmental – No**

Not involved in chemicals production or environmental negative discharge activities

d. **Regulatory – No**

E-commerce regulations are more likely to come on foreign players than Indian players.

e. **Buyer Power - Low**

Due to lack of alternate products with such extensive network, buyers are likely to stick. Price increase of Rs 5000 in annual base packages from Rs 25000 to Rs 30000 in 2019 went reasonably smooth.

f. **Competition - Low**

New Players like Walmart Wholesale, Udaan are trying to enter the market slowly but are a couple of years (5-10 years) behind looking at their current progress. Their progress needs to be monitored however.

g. **Sustainability - High**

No such product is present in the market with high network effect + product catalog pages. Goal of the company should be to add hooks at multiple levels in the product to make the business more sticky. Company is making good efforts in that direction with plans of introducing Credit Interface / Product Videos….

Lots of SMEs don't have the ability to create their own webpages. IndiaMART is a good product for them to list their products. Also finding a supplier for a manufacturer is not easy through other internet services.

2. **Valuation Risks**

Risk covered in the valuation multiples:
Risks not covered. 30% Downside Possible in multiple. Not much upside in valuation multiple.

Risks are not covered in current multiples of ~50.
Though, stock price is currently placed at 2-3x upside in 2-3 years, fall in growth structurally could lead to de-rating causing capital loss. Also 2-3x upside in the stock price would be purely driven by earnings than any further re-rating.

Hence, Risks leading to fall in growth are not captured at current valuations.
Revenue growth did fall from 30-35% to 25% during the economic slowdown. Any further fall in growth due to the COVID-19 crisis could lead to valuation derating.

Liquidity Stress Test: Can sit tight for 1-2 years despite:
Execution Delay. Business Temporary Issues

Investors can hold on to IndiaMART stock during business issues like current COVID-19 lockdowns as the company has a lot of deferred revenue and that sits as cash on the balance sheet.

Exit criteria during such stress situations should be based on cash on books. Cash on books can only reduce if there are renewal subscriptions of the service.

MEDIUM TERM VISIBILITY – MEDIUM

1. Earnings - Deferred Revenue. Mgmt Guidance
    a. There is no capex as such for IndiaMART. Also none of the proposed value-additive features are close to completion.
    b. Deferred revenue growth has been about 25% (however fallen from 35%) implying security in revenue of upcoming quarters

c. Management aspires to grow at 25%+ YoY (guidance given pre-COVID-19 crisis)

2. Margins – Pricing. Employee Costs
    a. Pricing: IndiaMART has strong pricing power and as it migrates over the value curve, it can keep increasing its price for the extra services it is adding
    b. Employee Costs: Increase in revenue is being realized with lower increase in employee expenses, any increase in revenues is going to provide the operating leverage benefits to the company with respect to slower ramp of employee costs.

3. Efficiency – Investments
    a. Not much visibility on how efficiently the company will deploy the cash present in its balance sheets. They will most likely used to deploy as investments into startups / small tech companies

INVESTMENT RATIONALE
Strategic. 2-3x in 2-3 years. 10x in 10 years

The investment could be strategic as the story which is driving IndiaMART's ride is Internet Adoption by SMEs, which is a long term one. China, which is generally considered 1-2 decades ahead of India, has 1688.com (owned by Alibaba) thriving, as its revenue still grows at ~25%.

Assuming the company can grow at 20-25% for the next 3 years, slowing down to 15% for the next four years and 10% for the last three years, the company can grow its revenues by 5x in the next 10 years. Operating leverage could help the company increase its earnings by 10x too.

As long as the company keeps adding hooks to the product through value addition and competition is in check, 10x in 10 years is achievable. Visibility for the next 2-3 years is higher compared to the 10 year story as it is quite visible that SME internet penetration is quite low.

Sources referred:

1. IndiaMART Annual Reports
2. IndiaMART IPO Prospectus
3. IndiaMART Conference Calls
4. Alibaba Annual Reports
5. VP Thread on IndiaMART and Industry reports attached on the thread