MOTILAL OSWAL

11 February 2021
3QFY21 Results Update | Sector: Financials

Piramal Enterprises

Bloomberg	PIEL IN
Equity Shares (m)	212
M.Cap.(INRb)/(USDb)	368.4 / 5
52-Week Range (INR)	1676 / 608
1, 6, 12 Rel. Per (%)	4/-23/-21
12M Avg Val (INR M)	2655

Financials & Valuations (INR b)

Y/E March	2020	2021E	2022E
Revenues	130.7	127.0	134.3
EBITDA	17.9	35.0	38.2
PAT	-5.5	27.0	30.2
EPS (INR)	-24.5	119.6	127.2
EPS Gr. (%)	NA	NA	6
BV/Sh. (INR)	1,274	1,507	1,589
Payout (%)	NA	35	35
Valuations			
P/E (x)	NA	13.7	12.8
P/BV (x)	1.3	1.1	1.0
Div. Yield (%)	0.8	2.6	2.7

Shareholding pattern (%)

As On	Dec-20	Sep-20	Dec-19
PromoterPromoter	46.1	46.1	46.1
DIIDII	10.5	10.2	9.9
FIIFII	29.3	29.7	29.9
OthersOthers	14.1	14.1	14.2

FII Includes depository receipts

CMP: INR1,633 TP: INR2,170 (+33%) Buy

Scaling down Wholesale Lending; Pharma segment stable

- Piramal Enterprises (PIEL)'s consol. PAT increased 19% YoY to INR8b. The Financial Services (FS) segment was characterized by a run-down in the Wholesale Lending book, the rollout of the Retail segment, and marginal asset quality deterioration.
- The Complex Hospital Generics (CHG) business was volatile due to COVID in 3QFY21. On the other hand, the Contract Dev. and Manufacturing Org. (CDMO; led by a strong order book) / India Consumer business (led by increased demand for Self-Care and Baby Care products) has been steady.
- As the Carlyle deal commenced in Oct'20, the consol. networth jumped from INR315b to INR355b QoQ. The equity infusion was used to primarily pare down debt – consol. net debt/equity ratio is at a multi-year low of 0.9x.
- After a lackluster 1HFY21, the Real Estate segment rebounded in 3QFY21 across most large cities. We expect the company to remain cautious in Wholesale Lending, with incremental disbursements to be largely driven by the Retail segment. **We forecast a 12% loan book CAGR over FY21–23E. The company has a provision buffer of 6.3% of loans, which is largely adequate.** While the Dewan Housing Finance (DHFL) deal is value-accretive, we await final regulatory approvals before incorporating it in our estimates. Maintain Buy, with TP of INR2,170 (FY23E SOTP-based).

FS – running down Wholesale Lending; INR343b DHFL deal

- After three quarters of stable loans, the loan book declined 10% QoQ to INR464b. **The GNPL ratio (proforma) increased 120bp QoQ due to the slippage of one corporate account. Total BS provisions increased 40bp QoQ to 6.3%. PIEL restructured 3.8% of loans in the quarter.**
- Cost of funds remains elevated at 10.8%, resulting in ~400bp spreads. We believe this could improve as a) leverage in the Financial Services business is down from 2.5x to 1.9x YoY and b) the asset quality picture is much clearer, and total stress due to the pandemic is likely to be much lower than initially feared.
- The DHFL acquisition is another step toward BS 'retailization'. **The total deal consideration is INR342.5b, of which the upfront cash component is INR147b (incl. cash on DHFL's BS) and the deferred component (NCDs) is INR195.5b.**
- PIEL launched its Retail Lending segment with six products in 3QFY21 – Mass Housing Finance, Affordable Housing Finance, LAP, Secured Business Financing, Digital Personal Loans, and Digital Purchase Finance (the last two are via partnerships). Overall yield in this segment is 11.5–12%.

Pharma – outlook on improving track

- Pharma sales grew moderately by 5.6% YoY for 3QFY21. CDMO / India Consumer products increased 16% YoY / 14% YoY, driving overall growth in the Pharma segment.
- This was partly offset by 13% YoY decline in the CHG segment.

Research Analyst: Alpesh Mehta (Alpesh.Mehta@MotilalOswal.com);+91 22 6129 1526 | **Piran Engineer** (Piran.Engineer@MotilalOswal.com); +91 22 6129 1539
Nitin Aggarwal (Nitin.Aggarwal@MotilalOswal.com); +91 22 6129 1542 | **Divya Maheshwari** (Divya.Maheshwari@motilaloswal.com); +91 22 6129 1540

- Slowdown in the CHG segment led to a 400bp YoY margin contraction in the Pharma segment. Notably, the EBITDA margin has expanded 1000bp from 1QFY21 to date and is expected to improve further going forward.
- Strong growth in the order book for the CDMO segment, the addition of new contracts / revival of surgeries in the CHG segment, and sustained momentum in the India Consumer product segment present better prospects for the overall Pharma segment going forward.

Highlights from management commentary

- It targets 50% share in Retail Lending (via inorganic expansion as well).
- It did a one-time restructuring of INR17.41b (3.8% of loans) in 3QFY21. This was done for four corporate accounts belonging to the Hospitality, Auto Components, Infra, and Real Estate sectors. Just 1% of retail loans were restructured.
- With the non-compete clause being over with regard to the Abbott deal, PIEL may look to re-enter the Domestic Formulation space, subject to a strategic mix and the valuation of inorganic opportunities.

Valuation and view

Over the past 1–2 years, PIEL has curtailed disbursements in Wholesale Lending and reduced exposure to its Top 10 clients by 25%+. In our view, this cautious stance is likely to continue over the next few quarters too, while the company looks to ramp up its Retail Lending business. While it is still early days, the initial asset quality outcome post moratorium has been positive. As the economic scenario gets better, asset quality is likely to improve – this would have a second-order impact on PIEL's availability and cost of debt capital as well. We raise our EV/EBITDA multiple for the Pharma business to 16x (from 14x earlier), factoring in a strong order book in the CDMO/CHG segment and improved profitability in the India Consumer product segment. Using SOTP, we arrive at TP of **INR2,170** (FY23E-based). Maintain **Buy**.

Quarterly Performance							INR m
Y/E March	FY20				FY21		
	1Q	2Q	3Q	4Q	1Q	2Q	3Q
Financial Services Business							
Revenues (INR m)	**20,144**	**19,540**	**19,626**	**17,184**	**18,995**	**18,608**	**17,950**
Change QoQ (%)	4.2	-3.0	0.4	-12.4	10.5	-2.0	-3.5
Change YoY (%)	29.2	12.8	6.6	-11.1	-5.7	-4.8	-8.5
PBT (INR m)	**7,344**	**7,355**	**5,904**	**-17,049**	**6,261**	**6,037**	**6,842**
Change QoQ (%)	39.0	0.1	-19.7	-388.8	-136.7	-3.6	13.3
Change YoY (%)	19.6	13.9	-10.9	-422.7	-14.7	-17.9	15.9
AUM (INR b)	**566**	**531**	**514**	**510**	**513**	**515**	**464**
Change QoQ (%)	0.0	-6.3	-3.1	-0.9	0.6	0.5	-10.0
Change YoY (%)	20.4	0.5	-6.9	-10.0	-9.4	-2.9	-9.8
ROAs (Cal %)	5.2	5.4	4.5	-13.3	4.9	4.7	0.0
Reported Leverage (D/E x)	3.7	2.8	2.5	2.3	2.2	2.1	1.9
ROEs (Cal %)	15.7	15.7	12.3	-35.1	12.6	11.6	0.0
NIMs (% Cum Rep)	5.7	5.4	5.5	5.2	6.5	6.3	6.2
Yield on loans (% Cum Rep)	14.0	14.0	14.3	14.3	15.2	14.8	14.6
Cost of funds (% Cum Rep)	10.3	11.0	11.1	11.2	10.8	10.8	10.8
GNPA %	0.9	0.9	1.8	2.4	2.5	2.5	3.7
ECL %	1.9	1.8	1.8	5.8	5.9	5.9	6.3
Borrowing Mix (%)							
Term Loans	63.0	67.0	65.0	65.0	62.0	48.0	50.0
NCDs	19.0	18.0	18.0	19.0	19.0	38.0	39.0
Securitisation	0.0	6.0	8.0	7.0	6.0	4.0	3.0
Others	18.0	9.0	9.0	9.0	13.0	10.0	8.0
Pharma Business							
Revenues (INR m)	11,724	13,165	13,074	16,226	10,379	14,411	13,741
Change QoQ (%)	-20.6	12.3	-0.7	24.1	-36.0	38.9	-4.6
Change YoY (%)	10.0	17.5	13.0	9.9	-11.5	9.5	5.1
EBITDA (INR m)	2,427	3,037	4,124	4,749	1,093	2,897	2,914
Change QoQ (%)	-30.9	25.1	35.8	15.2	-77.0	165.0	0.6
Change YoY (%)	53.8	38.7	63.1	35.2	-55.0	-4.6	-29.3
Revenue Mix							
Global	90.7	91.5	91.3	95.3	90.4	90.6	90.5
Domestic	9.3	8.5	8.7	4.7	9.6	9.4	9.5
Global EBITDA Margins	**22.0**	**24.0**	**23.0**	**26.0**	**11.0**	**0.0**	**0.0**

Highlights from management commentary

Wholesale Lending

- It targets 50% share in Retail Lending in the near term.
- It has launched six retail lending products thus far and would launch one product every month.
- Do not foresee any equity capital raise for the next 3–5 years in the FS business.
- The Infra book is down from the peak of INR45b to INR23.75b currently.
- Exposure to Lodha is down from the peak of INR33b to INR26.71b currently. This could decline to INR25b by end-FY21. Also, the exposure would be bifurcated into INR10b of Lodha exposure and the balance to an SPV, comprising ready inventory.
- Omkar – there was exposure to counterparties in JDAs.
- Cost of funds should decline with a higher share of retail lending.

Retail Lending

- Personal and purchase loans are at an experimental stage right now. This experimentation is being carried out in urban markets with first-time jobbers with incomes of INR25–50k.

- It went live with a partnership with Zest Money in 3QFY21. Three more fintech partnerships are lined up in 4QFY21. PIEL keeps the float economics, while the partner provides the risk cover. In short, the partner manages the front-end and PIEL the back-end.
- Yield: Small business loans – 13%, LAP – 12%, Mass housing finance – 10.5%, Affordable housing finance – 11.5–12%
- There is INR53b worth of retail loans currently.

Asset quality

- It did a one-time restructuring of INR17.41b (3.8% of loans) in 3QFY21. This was done for four corporate accounts belonging to the Hospitality, Auto Components, Infra, and Real Estate sectors. Just 1% of retail loans were restructured.
- It is confident that balance sheet provisions are adequate to meet any future contingencies.
- The DCCO extension was done for 10–12% of the lending book in the first quarter of FY21.
- Stage 2 + Stage 3 loans are up 5% QoQ.
- Auto anc. exposure of INR4.36b slipped into NPL in 3Q. PIEL preferred to initiate recovery proceedings by liquidating company assets rather than restructuring it.

DHFL-related

- The management is examining the Wholesale book, but cannot comment on upside in the same.
- The Retail book stands at INR280–290b – do not expect any significant markdown on the same at the time of the merger. It would look to cross-sell other retail lending products from the DHFL branch network. For about half the branches, business could resume once the acquisition happens. There was meaningful attrition a year ago, but this has now reduced.
- It would issue 10-year NCDs to DHFL creditors at 6.95%.
- Expect RBI approval within 10 days, followed by NCLT filing. The process is expected to fully close in June.

Pharma business

- With significant new contracts in place and the gradual revival of surgeries in key markets in the EU/US, the CHGS business outlook remains promising with the easing of the lockdown.
- PIEL launched 15+ new products and 35+ SKUs in 9MFY21 in India Consumer Products (ICP), driving overall growth in this segment.
- With the non-compete clause being over with regard to the Abbott deal, PIEL may look to re-enter the Domestic Formulation space, subject to a strategic mix and the valuation of inorganic opportunities.
- The CDMO business tends to be a little lumpy, due to which sales were moderately lower in 3QFY21. Health deliveries are scheduled for 4QFY21, resulting in higher growth.

Others

- Residential RE sales have now exceeded pre-COVID levels in most large cities.

Valuation and view

- Over the past two years, PIEL deleveraged its balance sheet through: a) infusing INR54b equity via preferential and rights issue, b) the sale of Decision Resources Group (DRG) for USD900m, and c) a 20% stake sale in the Pharma segment to Carlyle Group for EV of USD2.8b. **As a result, net debt to equity for the consolidated entity has declined from 2x to 0.9x over the past two years.**
- In the Real Estate segment, the company seeks to sell down loans, a prudent decision in this environment. Additionally, with real estate sales picking up in the industry, escrow collections are likely to improve going forward.
- **The total provision buffer of INR29b (6.3% of loans) on the balance sheet is comforting.** Given initial asset quality trends, we do not foresee any meaningful addition to the same.
- The Pharma business is seeing increased traction. The recent stake sale to Carlyle has set the benchmark for its valuation.
- We arrive at TP of **INR2,170** using SOTP (FY23E-based). **Buy**.

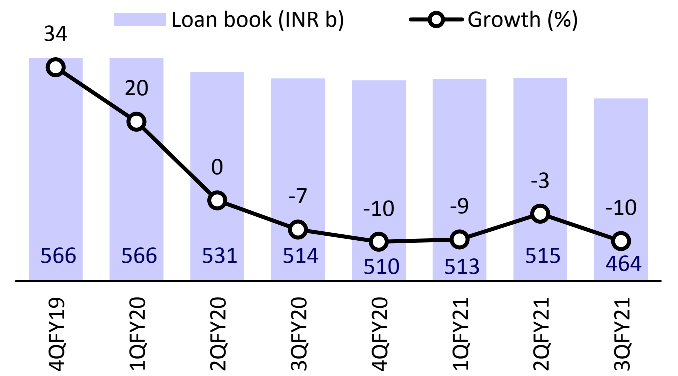
Exhibit 1: SOTP (FY23E-based)

	Value (INR B)	Value (USD B)	INR per share	% To Total	Rationale
Lending Business	211	2.8	890	41	1.0x PBV
Pharma Business	182	2.4	765	35	Pharma EV/EBITDA 16x; EV of INR288b; 80% Stake; 20% Holdco dis
Shriram Group	54	0.7	227	10	Based on our TP for SHTF and SCUF
Unallocated NW	68	0.9	288	13	1x PBV (Net of DTA, OCI and Shriram Group allocated NW)
Total Value	**515**	**6.9**	**2,170**	**100**	**Implied 1.3x Consolidated BV**
Current market cap.	387	5.2	1,633		
Upside (%)	***32.9***	***32.9***	***32.9***		

Source: MOFSL, Company

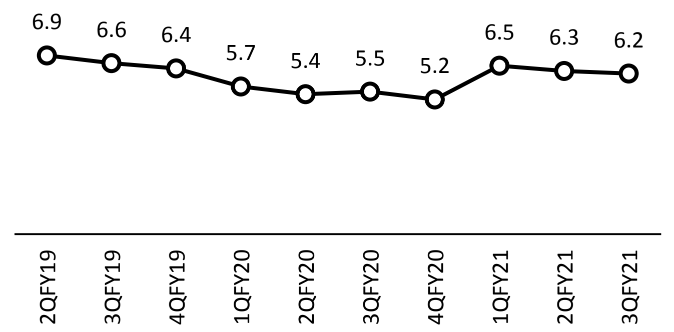
Key exhibits

Exhibit 2: Loan book runs down QoQ



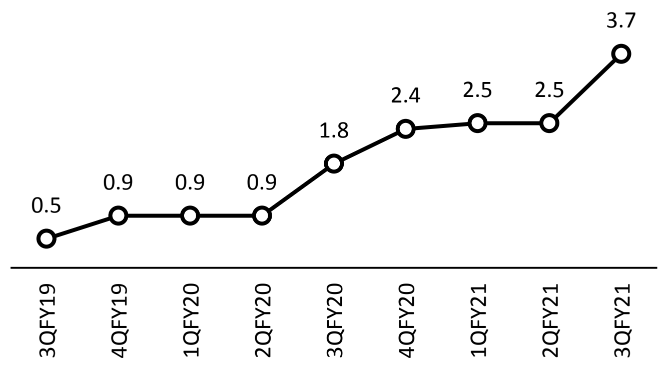
Source: MOFSL, Company

Exhibit 3: NIM largely stable (%)



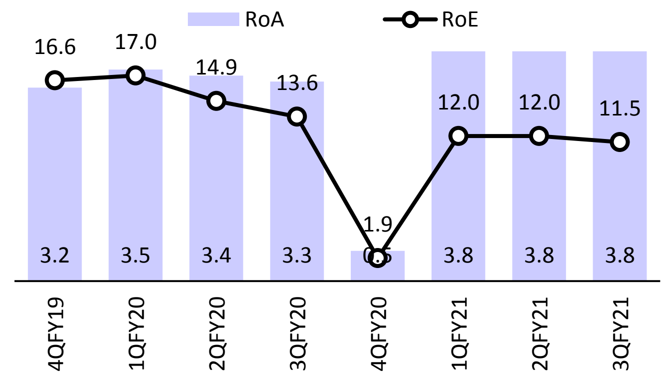
Source: MOFSL, Company

Exhibit 4: GNPL ratio up 120bp sequentially (%)



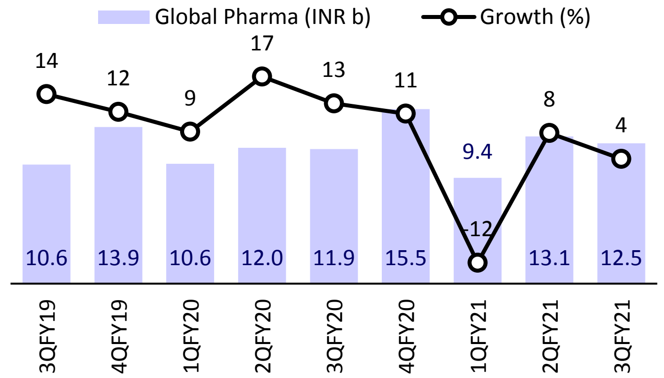
Source: MOFSL, Company

Exhibit 5: Return ratios stable (%)



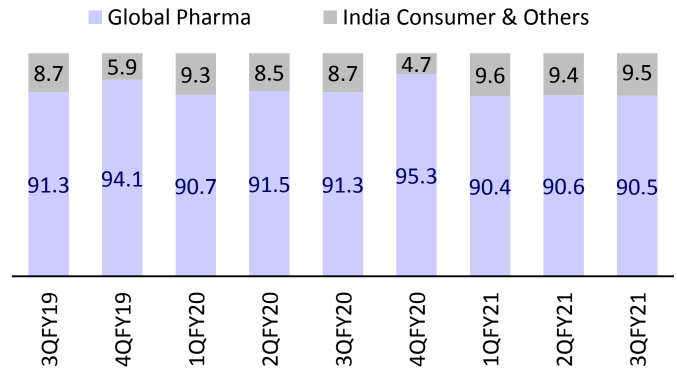
Source: MOFSL, Company

Exhibit 6: Global Pharma revenue up 4% YoY



Source: MOFSL, Company

Exhibit 7: Share of Indian Consumer business at ~10%



Source: MOFSL, Company

Financials and valuations

INCOME STATEMENT								INR m
	FY16	FY17	FY18	FY19	FY20	FY21E	FY22E	FY23E
Revenues	**63,815**	**85,468**	**1,06,394**	**1,32,153**	**1,30,683**	**1,27,022**	**1,34,314**	**1,52,900**
Change (%)	*24.6*	*33.9*	*24.5*	*24.2*	*-1.1*	*-2.8*	*5.7*	*13.8*
HealthCare	34,670	38,927	43,220	47,860	54,189	53,593	63,474	72,995
Financial Services	17,397	33,515	49,816	70,634	76,494	73,429	70,840	79,905
Info Mgmt	11,559	12,224	12,092	13,322				
Others	188	802	1,266	337				
EBITDA*	**13,726**	**21,007**	**29,611**	**36,582**	**17,889**	**35,041**	**38,248**	**46,935**
Change (%)	*57.8*	*53.0*	*41.0*	*23.5*	*-51.1*	*95.9*	*9.2*	*22.7*
HealthCare	3,266	6,028	8,001	9,809	14,336	10,719	13,647	16,424
Financial Services #	8,185	12,837	19,933	24,507	3,553	24,322	24,602	30,511
Info Mgmt	2,276	2,143	1,677	2,266				
EBIT*	**11,172**	**17,190**	**24,838**	**31,380**	**12,686**	**29,663**	**32,620**	**41,057**
Change (%)	*92.6*	*53.9*	*44.5*	*26.3*	*-59.6*	*133.8*	*10.0*	*25.9*
HealthCare	1,151	3,124	4,244	5,880	9,208	5,341	8,019	10,546
Financial Services #	8,159	12,813	19,897	24,431	3,478	24,322	24,602	30,511
Info Mgmt	1,862	1,254	697	1,069				
Unallocated Inc/(Exp)	**-4,028**	**-3,988**	**-5,200**	**-6,605**	**-3,510**	**490**	**488**	**488**
Core PBT	**7,144**	**13,202**	**19,638**	**24,775**	**9,176**	**30,153**	**33,108**	**41,544**
Change (%)	*110.6*	*84.8*	*48.7*	*26.2*	*-63.0*	*228.6*	*9.8*	*25.5*
Exceptional Items	457	-99	0	-4,656	0	0	0	0
Reported PBT	**7,600**	**13,103**	**19,638**	**20,119**	**9,176**	**30,153**	**33,108**	**41,544**
Taxes	**495**	**2,281**	**6,928**	**8,611**	**19,604**	**7,538**	**8,277**	**10,386**
Tax Rate (%)	*6.5*	*17.4*	*35.3*	*42.8*	*213.7*	*25.0*	*25.0*	*25.0*
PAT	**7,105**	**10,821**	**12,710**	**11,507**	**-10,429**	**22,614**	**24,831**	**31,158**
Change (%)	*-73.6*	*52.3*	*17.5*	*-9.5*	*-190.6*	*-316.8*	*9.8*	*25.5*
Minority Interest	0	-3	0	0	0	0	0	0
Share from Asso. Co	1,942	1,699	2,801	3,194	4,896	4,364	5,339	5,981
PAT Post MI	**9,047**	**12,523**	**15,511**	**14,701**	**-5,533**	**26,978**	**30,170**	**37,139**
Change (%)	*-68.3*	*38.4*	*23.9*	*-5.2*	*-137.6*	*-587.6*	*11.8*	*23.1*
Dividend (Including Tax)	**3,635**	**4,348**	**5,415**	**6,065**	**3,500**	**9,442**	**10,560**	**12,999**

** Ex Exceptional, # Post interest expenses; FY16-18 nos based on IND AS; FY18 Excluding one off DTA of INR35.6b*

BALANCE SHEET								INR m
Y/E MARCH	**FY16**	**FY17**	**FY18**	**FY19E**	**FY20E**	**FY21E**	**FY22E**	**FY23E**
Equity Share Capital	345	345	424	424	451	451	474	474
Reserves (Ex OCI)	1,21,102	1,33,609	2,43,287	2,53,732	2,86,835	3,39,371	3,76,458	4,00,599
Networth	**1,21,447**	**1,33,954**	**2,43,711**	**2,54,156**	**2,87,286**	**3,39,822**	**3,76,933**	**4,01,073**
OCI	8,037	14,872	21,977	18,430	18,430	18,430	18,430	18,430
Networth	**1,29,484**	**1,48,826**	**2,65,688**	**2,72,586**	**3,05,716**	**3,58,252**	**3,95,362**	**4,19,502**
Change (%)	*-3.6*	*14.9*	*78.5*	*2.6*	*12.2*	*17.2*	*10.4*	*6.1*
Borrowings	**1,62,788**	**3,04,510**	**4,41,608**	**5,59,867**	**4,19,562**	**4,13,571**	**4,58,407**	**5,27,168**
Change (%)	*126.5*	*87.1*	*45.0*	*26.8*	*-25.1*	*-1.4*	*10.8*	*15.0*
Other liabilities	**17,526**	**29,058**	**20,708**	**23,808**	**23,808**	**27,197**	**32,013**	**37,437**
Change (%)	*26.0*	*65.8*	*-28.7*	*15.0*	*0.0*	*14.2*	*17.7*	*16.9*
Total Liabilities	**3,09,798**	**4,82,394**	**7,28,004**	**8,56,261**	**7,49,086**	**7,99,020**	**8,85,783**	**9,84,108**
Loans+Investments	**1,98,500**	**3,25,163**	**5,14,984**	**6,45,325**	**5,48,231**	**4,97,268**	**5,43,134**	**6,18,814**
Change (%)	*57.9*	*63.8*	*58.4*	*25.3*	*-15.0*	*-9.3*	*9.2*	*13.9*
Goodwill	54,854	54,272	56,326	59,395	11,391	11,391	11,391	11,391
Fixed Assets	23,949	54,251	57,402	57,510	57,935	63,729	70,739	78,520
Other assets	**32,495**	**48,707**	**99,293**	**94,032**	**1,31,529**	**2,26,633**	**2,60,519**	**2,75,383**
Change (%)	*22.2*	*49.9*	*103.9*	*-5.3*	*39.9*	*72.3*	*15.0*	*5.7*
Total Assets	**3,09,798**	**4,82,394**	**7,28,004**	**8,56,261**	**7,49,086**	**7,99,020**	**8,85,783**	**9,84,108**

Financials and valuations

Profitability Ratios (%)	FY16	FY17	FY18	FY19E	FY20E	FY21E	FY22E	FY23E
EBITDA Margin - IT	19.7	17.5	13.9	17.0				
EBITDA Margin - Pharma	9.4	15.5	18.5	20.5	26.5	20.0	21.5	22.5
Core ROE	5.5	9.8	8.2	5.9	-2.0	8.6	8.4	9.5
ROE	7.5	9.8	8.2	5.9	-2.0	8.6	8.4	9.5
Valuations								
Book Value (INR)	**704**	**776**	**1,148**	**1,198**	**1,274**	**1,507**	**1,589**	**1,691**
BV Growth (%)	1.0	10.3	47.9	4.3	6.4	18.3	5.5	6.4
Price-BV (x)					1.3	1.1	1.0	1.0
EPS (INR)	**52**	**73**	**73**	**69**	**-25**	**120**	**127**	**157**
EPS Growth (%)	-68.3	38.4	0.7	-5.2	-135.4	-587.6	6.4	23.1
Price-Earnings (x)					-66.6	13.7	12.8	10.4
DPS (INR)	**18**	**21**	**25**	**28**	**13**	**42**	**45**	**55**
Dividend Yield (%)					0.8	2.6	2.7	3.4

E: MOFSL Estimates

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