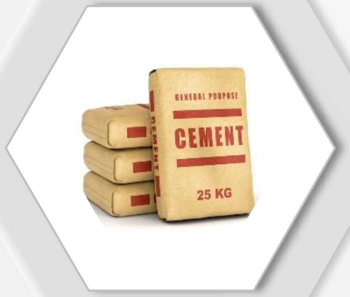
AXIS SECURITIES

February 2025

Top Conviction Ideas
Q3FY25
(Consolidated)



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Top Conviction Ideas: Q3FY25 (Consolidated)

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February 2025

Top Conviction Ideas: Cement

Uttam Kumar Srimal

Cement Sector: Q3FY25 Review

Q3FY25 Cement Review – Recovery in Sight; Q4FY25 Expected to be Better

✓ *Financial Performance*

- The companies under our coverage reported revenue growth of 3% YoY, while EBITDA/PAT de-grew by 12%/34%, against expectations of flattish revenue growth and 20%/50% de-growth in EBITDA/PAT. Volume growth during the quarter was higher by 200 bps at 9% compared to expectations of 7%.

- EBITDA margins declined by 300 bps YoY, driven by lower realisations, although partially offset by lower costs during the quarter. On a QoQ basis, EBITDA margins improved by 450 bps as realisation per tonne improved by 2% to Rs 5,462 for the coverage universe. EBITDA per tonne for the quarter stood at Rs 830, up 35% QoQ and down 26% YoY. The benefit of operating leverage also supported higher EBITDA/tonne during the quarter.

- Realization per tonne improved by 2% QoQ but declined by 7% YoY to Rs 5,462, as most regions experienced a rise in cement prices. The cost per tonne was Rs 4,630, showing a 2% decrease YoY/QoQ, as power and fuel costs softened by 12% to Rs 1,090 per tonne.

- Performance among the companies in our coverage was mixed. UltraTech, JK Cements, and Shree Cement reported better-than-expected results, while Ambuja Cement, ACC, Birla Corp, and Dalmia Bharat Ltd fell short of expectations. Ambuja Cement and ACC Ltd performed better on an absolute basis, driven by higher incentives and other income. JK Lakshmi and Star Cement’s margins were marginally above expectations.

- No new capacities were announced or commissioned within our coverage universe during the quarter. Previously announced capacities are progressing as planned and are expected to become operational according to the given timelines.

- Management indicated that cement prices have improved since Q3FY25 exit levels, with expectations for better demand revival in Q4FY25 as government infrastructure expenditure picks up.

Cement Sector: Outlook

Better Realization & Improved Demand Supported Overall Performance

In Q3FY25, the cement volume for our coverage universe grew by 7%, surpassing our expectations. Realisations improved by 2% as cement prices increased, while operating costs reduced by 2% YoY/QoQ. We anticipate better operating performance from cement companies in Q4FY25, supported by positive operating leverage benefits, improved pricing, and higher government spending on infrastructure projects.

Cement demand better than expectations:

- Cement demand improved during the quarter after a subdued H1FY25, which was impacted by extreme weather conditions, the general election, and a shortage of labour. Higher demand in Oct'24 and Dec'24, driven by a pick-up in housing and a revival in rural demand, offset the subdued performance in Nov'24, due to festivity and labour shortages. Infrastructure demand also improved in the later part of December 2024.
- Demand has picked up in Q4FY25 and is expected to remain buoyant, as Q4 traditionally remains a strong period for construction activity. Non-trade demand is anticipated to rise with the revival of government expenditure on infrastructure.

Cement prices

- Cement prices declined by 7% YoY but improved 2% QoQ and are currently higher than the average Q3FY25 prices by Rs 100/tonne. Some rollback in cement price hikes implemented in Dec'24 was observed, particularly in the South and East, while prices in the North, Central, and West regions remained firm.
- Market dynamics and the demand-supply scenario will dictate the pricing environment.

Cement Sector: Outlook

Input Cost

- The softening of power and fuel costs positively impacted the operational performance of cement companies in Q3FY25. During the quarter, power and fuel costs decreased by 12% YoY to Rs 1,075/tonne for our coverage universe.

- Going forward, power and fuel costs are expected to remain largely in line with Q3FY25 levels. Pet coke and coal prices have increased marginally following a recent correction, while diesel prices remain stable. Additionally, raw material costs are projected to remain steady, supporting cost efficiency in the coming quarters.

- **We remain positive as long-term demand drivers are intact and expect cement demand to grow at a CAGR of 7%-8% over FY24-27E. Sector consolidation is expected to benefit large players through economies of scale, supply chain efficiency, and better pricing in the long term. Despite ongoing capacity additions, we believe long-term cement demand will outpace supply.**

- **Cement prices and trends in fuel costs will be key monitorables.**

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Short and Medium-term Outlook

Short term

Decline in Cement Prices

Higher Competitive Intensity

Higher Capex outlay in budget for infrastructure

Better Housing, Infra, and Real Estate demand

Capacity expansion plan progressing well.

Medium Term

Key Monitorables – ***Higher Price Realizations; Input Cost, Demand pick up***

Top Conviction Ideas: Cement

Stock	Reco.	TP	Recommendation Rationale
UltraTech Cement Ltd	BUY	Rs 13,510*	✓ The company's capacity expansion plan is progressing well. Its total grinding capacity currently stands at 165.8 mtpa in India, following the acquisition of India Cement assets. ✓ The company plans to add a further 6.3 mtpa in FY25, 12 mtpa in FY26, and another 15 mtpa in FY27, bringing its total cement manufacturing capacity to 209.3 mtpa in India, including Kesoram's 10.8 mtpa. ✓ With the expanded capacity and increasing scale, we expect the company to consolidate its market leadership position further and increase its market share from the current 25% to 28%. We anticipate the company will grow its volume at an 11% CAGR over FY24-27E. ✓ The company expects a cost reduction of Rs 200-300 per tonne in the next 2-3 years. We project that the company's EBITDA margin will increase to 22% in FY27E, driven by higher volume, better realisations, and cost optimisation initiatives. ✓ Between 2013 and 2024, the market share of large players increased from 46% to 55%, and by FY27-28, it is expected to rise further to 65%-70%. With the growing pace of consolidation and capacity expansion by top players, its overall market share is set to increase further. This trend will positively influence cement pricing, economies of scale, and supply chain efficiency. The company, being the top player in the country, is well-positioned to benefit from this consolidation in the medium to long term.

Note: Target Price is based on our Q3FY25 Result Update Report

Top Conviction Ideas: Cement

Stock	Reco.	TP	Recommendation Rationale
JK Cements Ltd	BUY	Rs 5,380*	✓ The company's capacity expansion program, aiming to add 6 MTPA, is progressing well and will bring its total grey cement capacity to 30 MTPA from the current 24 MTPA, representing a 13% capacity CAGR over FY23- FY26. ✓ The ramp-up of recently commissioned capacity in Prayagraj (2 MTPA) and ongoing expansions are anticipated to support robust volume growth in the coming periods. Given these developments, the company is expected to achieve a volume CAGR of 12% over FY24- FY27E. ✓ The company delivered a strong operating performance during the quarter, driven by higher realisations and positive operating leverage, resulting in a 54% QoQ improvement in EBITDA per tonne, reaching Rs 1,000. This positive trend is expected to continue in Q4FY25, supported by robust cement demand and better realisations. ✓ Management projects cost savings of Rs 150-200 per tonne over the next two years. Consequently, we anticipate the company will achieve an EBITDA margin range of 19% -20 % in FY27E, driven by higher volumes, better realisations, and ongoing cost optimisation efforts. ✓ We project the company will grow its volume, revenue, EBITDA, and APAT at a CAGR of 12%, 10%, 25%, and 36%, respectively, over FY24- FY27E.

***** Note: Target Price is based on our Q3FY25 Result Update Report*

Top Conviction Ideas: Cement

Stock	Reco.	TP	Recommendation Rationale
 **Ambuja Cements Ltd**	**BUY**	**Rs 655***	✓ The company is expanding its capacity from the current 97 MTPA (including 8.5 MTPA of Orient Cement) to 118 MTPA, with the ongoing expansion set to be completed in phases over FY25-FY26. ✓ The company is exploring further growth opportunities to achieve a combined capacity of 140 MTPA by FY28. This expansion is expected to support the company's sustained growth momentum. Volume and revenue are projected to grow at CAGRs of 11% and 10%, respectively, over FY24-FY26E. ✓ Business initiatives are expected to further lower operating costs by reducing the clinker factor and logistics costs, improving the sale of blended cement, and expanding the EBITDA margin. We forecast the company's EBITDA margins to improve to 18%-19% in FY26E. ✓ Strong infrastructure demand and ongoing needs from the housing and commercial sectors are anticipated to boost cement demand in H2FY25. Strategic investments in roads, railways, and urban and commercial amenities are poised to drive robust growth. The company expects demand for the industry during FY25 to grow in the range of 4-5%.

***** Note: Target Price is based on our Q3FY25 Result Update Report***

AXIS SECURITIES

February 2025

Top Conviction Ideas: Metals & Mining

Aditya Welekar

Steel EBITDA Weakness Persists; Performance of Aluminum Names Remains Robust

Financial Performance

- **For Aluminium companies under coverage:**
  - ✓ **Hindalco's** Indian operations stood robust, offsetting Novelis's impacted profitability due to tighter scrap spreads and flooding at one of the European units. Consolidated EBITDA grew by 26% YoY but declined by 5% QoQ to Rs 7,601 Cr (3% beat vs. consensus), led by strong upstream Aluminium and Copper EBITDA.
  - ✓ **NALCO's** Revenue/EBITDA/PAT beat our and consensus estimates because of strong performance by both the Alumina and Aluminium divisions. Consolidated revenue at Rs 4,662 Cr (up 39%/17% YoY/QoQ) stood ahead of consensus estimate by ~6%. EBITDA at Rs 2,328 Cr (up 201%/50% YoY/QoQ) beat the consensus estimates by 30%, led by a higher topline, while RM and employee costs remained under control.
- **For Steel companies under our coverage:**
  - ✓ **Tata Steel's** consolidated revenue declined 3% YoY and stood flat QoQ (2% ahead of consensus) on account of lower realisations in India and Europe. Consolidated Adj. EBITDA (excluding one-off gain from earlier provisions of Rs 1,412 Cr) stood at Rs 5,742 Cr, flat YoY, up 4% QoQ. This was a 20% beat against ours and consensus due to higher-than-expected results from Indian operations and NINL, as well as lower EBITDA/t loss in Europe.

Metals & Mining: Q3FY25 Review (Cont'd)

Steel EBITDA Weakness Persists; Aluminum Names Performance Remains Strong

Financial Performance

- **Tata Steel's** Indian Adjusted EBITDA stood at Rs 6,110 Cr, down 26%/9% YoY/QoQ, 1% ahead of our estimates. Europe's EBITDA/t loss narrowed down to $41/t vs. our estimate of $53/t (EBITDA/t loss in Q2FY25 was at $75/t), mainly due to lower other expenses and RM costs in the UK.
- **SAIL** reported largely in-line numbers amidst weak steel prices and post-weak Q2FY25 results. Adj. Revenue (up 5%/6% YoY/QoQ) stood in line with our and consensus estimate. Adj EBITDA (adjusted for provisional rail price impact) stood at Rs 2,030 Cr (down 5% YoY but up 59% QoQ on impacted Q2FY25), a 5% beat vs. our estimate (a 2% miss against consensus) aided by lower employee costs and other expenses.
- **Coal India** adj. EBITDA (exl. stripping activities) stood at Rs 10,405 Cr (down 13% YoY/up 45% QoQ), a 9% miss vs. our estimate, led by higher contractual expenses partially offset by lower employee expenses. The e-auction premium stood better than our estimate at 76% (vs. our est. of 53%) and as compared to 69% in Q2FY25. E-auction volumes grew YoY/QoQ but stood below our estimate at 19 MT.
- **APL Apollo tubes** managed to pull back its EBITDA/t at Rs 4,173/t in Q3FY25 (vs. weak EBITDA/t in Q2FY25 at Rs 1,821/t), inline with the guidance range of Rs 4,000-4,500/t. EBITDA/t improved despite continued macro headwinds in Q3FY25.
- **JTL Industries** EBITDA/t at Rs 4,005/t (down 5% YoY but up 21% QoQ) stood slightly ahead of our estimate by 3%. EBITDA (down 17% YoY but up 18% QoQ on impacted base) stood ahead of our estimate by 3%, mainly due to lower RM costs.

Steel Sector: Outlook

- **Steel spreads are likely to improve slightly in Q4FY25:** SAIL's management stated that the Blended Coking coal costs are expected to decline by ~Rs 1,000/t QoQ in Q4FY25, led by declining imported coking coal prices. The average blended NSR in Jan'25 declined by ~Rs 1,000/t to Rs 48,500/t; however, prices are likely to increase in the coming months as market sentiments are now positive for flat steel. This may improve spreads slightly in Q4FY25 on a QoQ basis. For Tata Steel, Indian operations spreads could increase as NSR in India will be flat QoQ (if the safeguard duty announcement is in Q4FY25, it will pose an upside to NSRs). Coking Coal consumption cost is expected to be ~$10/t lower QoQ. However, spreads could come under pressure in Europe as NSRs will likely fall by ~£60/t in the UK and Netherlands. This is because the annual contract resets at the calendar year-end, where it signed more contracts for steel supplies to packaging than automotive (which fetches higher NSRs). Coking coal costs in the Netherlands will be $20/t lower QoQ, while iron ore consumption cost is expected to be about $3-4/t lower QoQ. (not applicable to the UK as it transitioned to steel substrate).

- **Steel prices remain weak:** Steel HRC prices (traders market ex-Mumbai) have declined by 15% YoY and 6% QoQ and averaged at Rs 48,734/t in Q3FY25. Spot prices have corrected to Rs 48,000/t, down 1.5% compared to the Q3FY25 average. Weak Chinese domestic demand and higher Chinese exports have led to a decline in steel prices in India. Chinese steel exports in CY24 stood at 111 MTPA, up 22% YoY. **China's Crude steel production** in CY'24 declined by 1.7% to 1,005 mtpa.

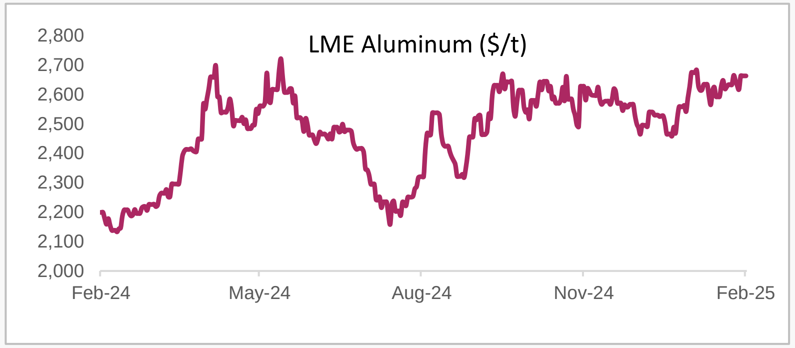
- **Steel raw materials soften:** A decline in steel production in China has softened the coking coal and iron ore prices recently, thereby providing some relief to the spot spreads. Spot coking coal prices are down to $190/t (Q3FY25 average at $218/t, down 30%/11% YoY/QoQ FOB Australia), while iron ore prices in Q3FY25 averaged at $102/t, CFR China, down 21% YoY, up 2% QoQ. Spot iron ore prices are currently trading higher at $107/t on account of disruption at Australian ports due to tropical cyclone Zelia.

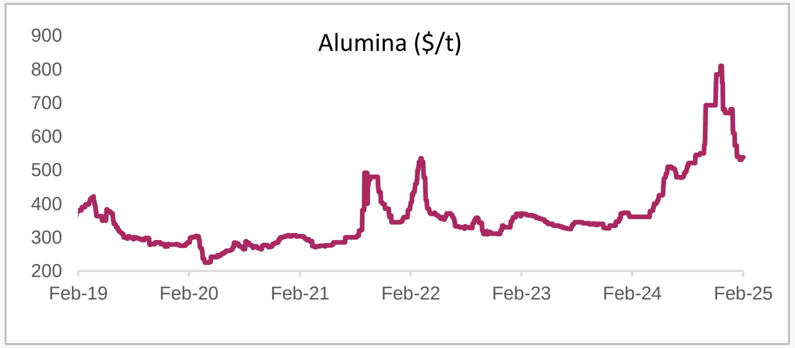
- **Key Monitorables:** Demand of 25% Safeguard duty outcome, more China stimulus measures, and the impact of 25% tariffs on steel imports in the US will be the key monitorables in future.

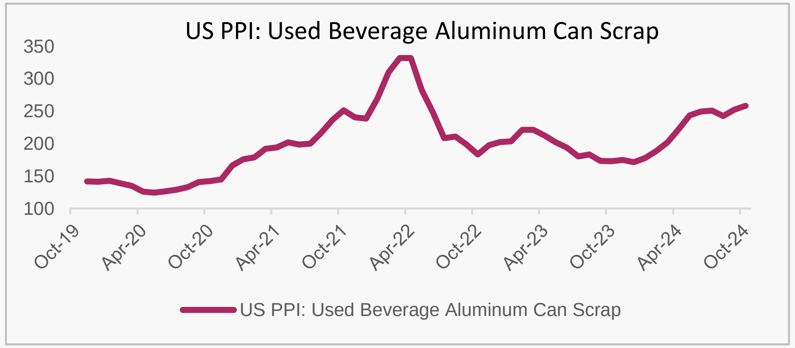
Aluminium Sector: Outlook

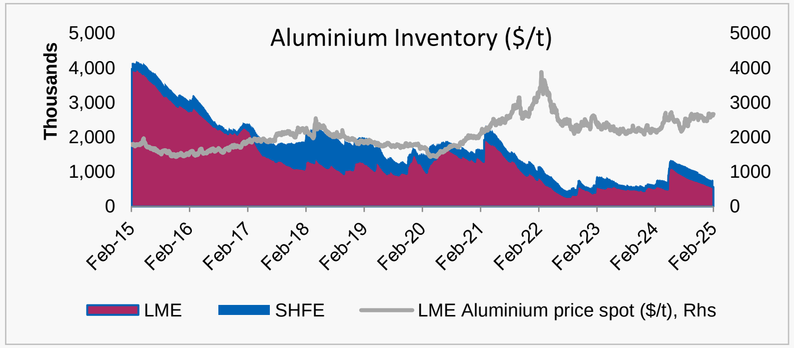
- **Aluminum Q3FY25:** LME Aluminum prices averaged at $2,577/t in Q3FY25, up 17%/8% YoY/QoQ. Aluminium prices found support from the firm Alumina prices, which provided cost support to Aluminum prices and the series of Chinese stimulus measures announced in Sep'24.
- **Alumina prices (FOB WA) averaged at $691/t in Q3FY25 (up 107%/36% YoY/QoQ)**, led by production curtailment at the Alcoa and Rio alumina refinery in Australia and Chinese refinery curtailments. The Chinese refinery curtailments have been due to domestic bauxite shortage and disruptions in Guinea, where China imports the majority of its bauxite requirements. (~72% of total Bauxite imports of China in 9MCY24 was from Guinea). Demand, on the other hand, is stable as smelters continue operations. The global Alumina market expects a deficit of 1.4MT in CY24 (as per Norsk Hydro Q4CY24 ppt); however, the market is expected to ease with a surplus of 0.1MT expected in CY25 and 0.2MT in CY26. The ramp-up of several new alumina refineries in Indonesia, India and China will rebalance the market in CY25. Alumina prices have corrected from the peak of $810/t in Dec'24, and the spot Alumina prices are trading at $520/t.
- **Aluminum Supply/Demand balance:** On the supply side, few restarts or new projects are on the horizon, and China is holding its capacity cap (45 mtpa). On the demand side, the demand for beverage cans and packaging remains good. On the other hand, automotive growth slows. Rate cuts support building & construction demand. For CY24, as per Norsk Hydro Q4CY24 ppt, the primary Aluminium global balance is expected to remain largely balanced, and in CY25, a deficit of 0.6MT is projected by CRU.
- **Impact of 25% tariffs on Aluminium.** On 10th Feb'25, President Trump announced a 25% tariff on Aluminium imports into the US from all countries. Canada is the major exporter of Aluminium to the US, forming almost 58% of US Aluminium imports in Jan-Nov'24, followed by UAE and China, which stand distinct second and third in the list of imports. The higher tariffs are reflected in the higher Midwest premium, which is the premium which US consumers pay over the LME benchmark.
- Tariff impact, Fed rate cuts, Chinese stimulus and other geopolitical events will reshape the Aluminium market going forward.

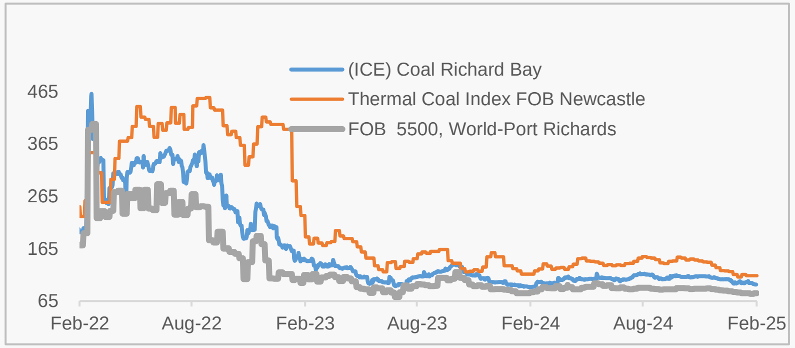
Metals & Mining Key Charts

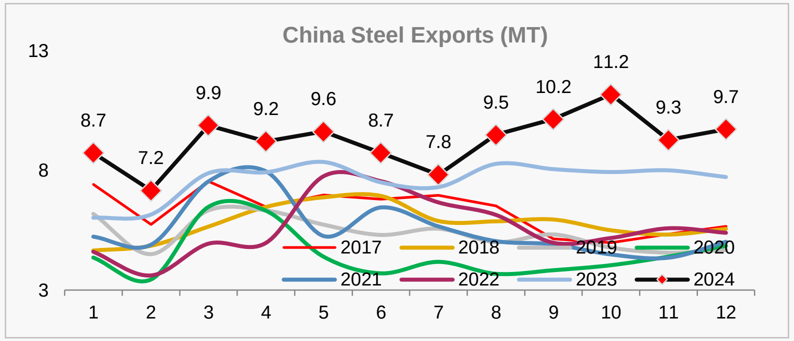


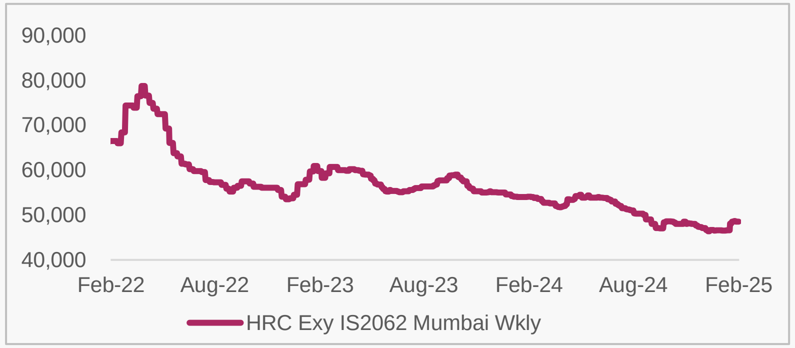


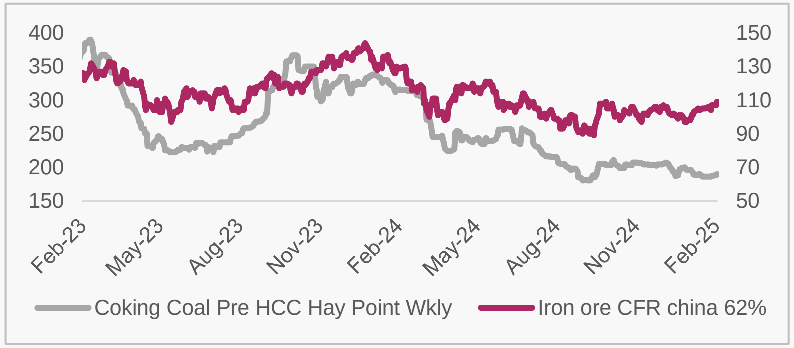












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Short, Medium and Long term outlook

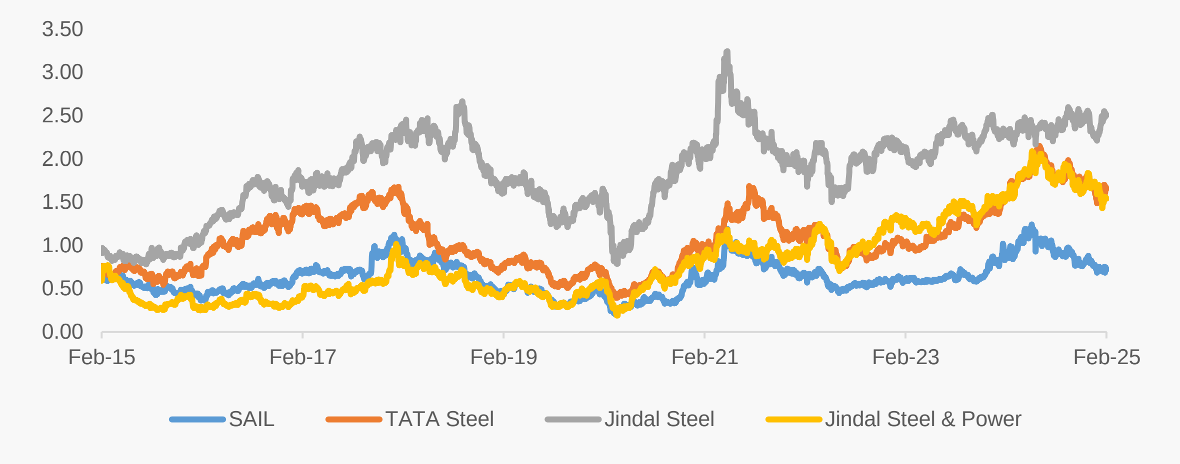
	Near-Mid term outlook	Long-term outlook	Current Valuation	Recommendation
Steel				
Tata Steel	FCF likely to be under pressure in FY26 on UK restructuring and EAF Capex. Deleveraging to take back seat.	Tata Steel's equity story will get a boost with the expansion of TSK phase II 5mtpa BF. Normalization of European operations to reduce drag on cash flow	Tata steel trades at 1.65x 12MF consensus P/B. The valuation is not cheap against the LT average of 1.09x P/B.	Rising Debt amidst weak steel prices, expansion and restructuring Capex at UK poses challenge. However. We have a **BUY** rating post correction in stock price which offers some valuation comfort.
SAIL	In FY25, steel production guidance is 18.5 MT and sales volume target is ~17.5 MT. Until the expansion Capex kicks in, SAIL's profitability will be guided by coking coal prices and NSRs.	SAIL's next phase of the Capex wave raises concerns as it completed its earlier hot metal expansion plan from 14.6 MT to 25 MT after much delay and Capex over-run.	SAIL is trading at 0.72x 12MF P/B against LT average of 0.63x. Valuations have slightly cooled off from the peak of 1.24x in May'24	We maintain our **HOLD** rating on SAIL as steel prices remains weak and risk of higher leverage is there as expansion Capex picks up.
Aluminium				
Hindalco	Aluminium prices are strong despite fading cost support from Alumina prices. Higher LME prices and lower coal costs augurs well for Hindalco	The downstream Capex benefit will be back ended and FCF is expected to increase post the completion of expansion projects. Augurs well in the long term	Hindalco trades at 5.6x 12MF EV/EBITDA which is below the LT average of 6.3x	We have a **BUY** rating as major downstream expansion Capex is almost complete.
Nalco	Aluminium prices are still holding strong, however, Alumina prices have corrected from the peak.	The Alumina refinery expansion will bring in additional revenue from incremental Alumina sales. Execution risk remains. Valuation are stretched.	NALCO is now trading at 5.35x 12MF EV/EBITDA against LT average of 4.8x which looks slightly stretched.	Valuations are not cheap, however, we maintain a **BUY** as contribution of refinery expansion from FY27 kicks in.
Others				
Coal India	Fall in e-auction premiums and Volumes leading to slower earnings growth	Higher production volume targets. Good dividend yield	CIL trades at 12MF EV/EBITDA of 3.87x against LT average of 5.1x which looks decent	We have a **BUY** rating on coal production ramp up potential
APL Apollo tubes	Demand was sluggish in 9MFY25, demand to pick up in going ahead – but its key monitorable. Jal Jeevan capex increased.	Raipur plant ramp up to drive higher EBITDA/t. Long term target of 10mtpa tube capacity		We have a **BUY** rating on account of capacity ramp up ahead.
JTL Industries	Demand was sluggish in 9MFY25, demand to pick up in going ahead	In the long term target is to increase capacity to 2mtpa. Mid term target is to achieve capacity of 1mtpa by FY25		We have a **BUY** rating on account of capacity ramp up ahead.

Key Monitorables – Impact of US Tariffs, Fed Rates Cut Trajectory, China Stimulus and other Geopolitical Events and Risks

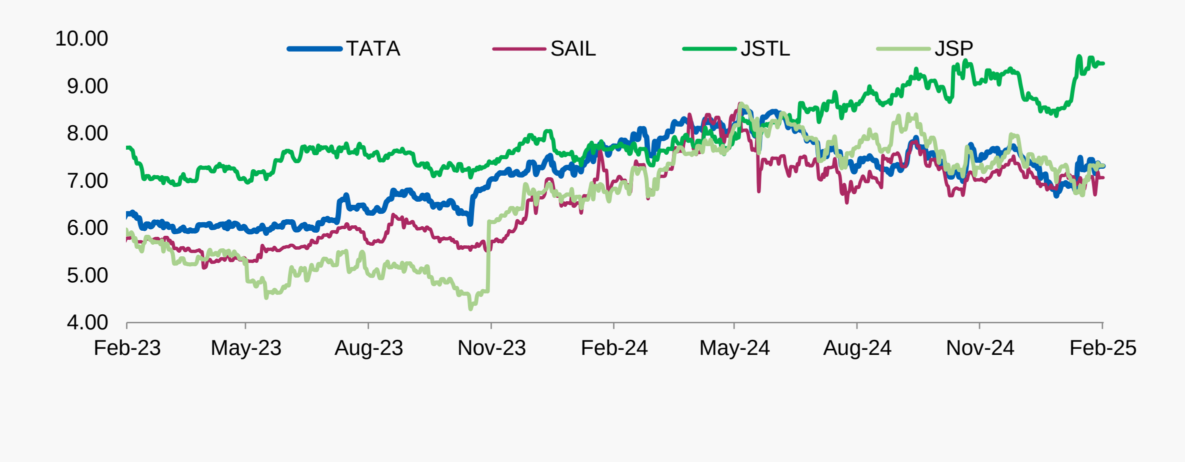
Valuations Retreated from Recent Highs

- SAIL is trading at P/B of 0.72x vs LT average of 0.63x
- Tata Steel is trading at P/B of 1.65x vs LT average of 1.09x
- JSPL is trading at P/B of 1.54x vs LT average of 0.81x
- JSW Steel is trading at P/B of 2.51x vs LT average of 1.85x

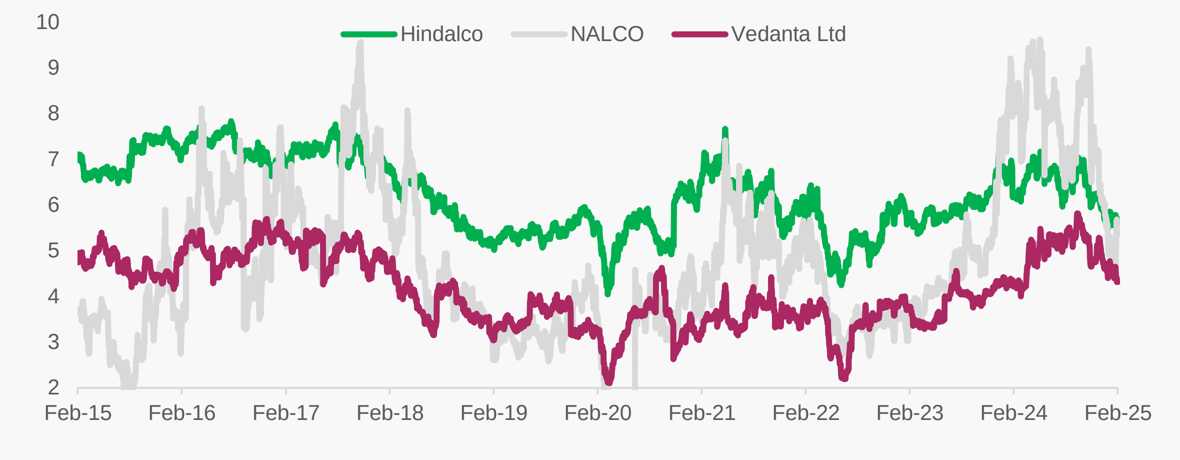
12MF P/B



12MF EV/EBITDA



12MF EV/EBITDA



Source: LSEG Workspace

Top Conviction Ideas: Metals & Mining

Stock	Reco.	TP	Recommendation Rationale
Hindalco	BUY	Rs 710*	✓ **The company's expansion projects,** such as the 600kt Bay Minette (by H2CY26), Copper Inner Grooved Tubes (in Q4FY25) and Aluminium downstream projects (end of FY25-26), will lead to an increase in the EBITDA/t from FY27 onwards as the projects get commissioned and start contributing fully from FY27. ✓ **Downstream projects Capex** (Silvassa 34 ktpa and FRP-2 170 ktpa) is almost complete, and the ramp-up will progress. Now, the focus will be on Indian upstream projects (Aluminium and Copper smelter and Alumina Refinery) with a total Capex of $4-5 Bn spread over the next 3-3.5 years. The company will use a combination of internal cash and will raise debt of $1-1.5 Bn for funding this Capex over the next 3-3.5 years. ✓ **Management envisages double-digit IRR** and plans to complete the upstream expansion projects with a Net Debt/EBITDA < 1.0-1.5x. In our view, Hindalco's capital allocations towards upstream assets look well placed, given its strong Indian balance sheet and robust domestic demand. ✓ **Novelis:** The management has withdrawn EBITDA/t guidance for the near term, citing pressure on scrap spreads. However, the long-term EBITDA/t towards $600/t is maintained. ✓ **The copper segment** is doing well, led by good electrification demand. The management has guided for a quarterly run-rate of Rs 650 Cr EBITDA on a sustainable basis for its copper business.

Note: Target Price is based on our Q3FY25 Result Update Report

Top Conviction Ideas: Metals & Mining

Stock	Reco.	TP	Recommendation Rationale
APL Apollo tubes	BUY	Rs 1,750*	✓ **EBITDA/t rebounds QoQ after weak Q2FY25 show:** APL Apollo managed to pull back its EBITDA/t at Rs 4,173/t in Q3FY25, inline with the guidance range of Rs 4,000-4,500/t. EBITDA/t improved despite continued macro headwinds in Q3FY25. The company managed to grab the market share of its competitors, mainly from the secondary Patra market, as the spread between HRC and Patra narrowed. The general products segment, which competes with the Patra market, posted a marked improvement in the EBITDA/t at ~Rs 2,000/t vs. negative Rs 24/t in Q2FY25. ✓ **Guidance of upward EBITDA/t trajectory maintained:** In Q4FY25, the company targets to achieve EBITDA of ~Rs 400 Cr and EBITDA/t of Rs 4,500/t+. This will be driven by the rise in sales volume QoQ as the prevailing lower HRC prices aid in gaining the Patra market. For FY26, the EBITDA/t target is Rs 5,000/t. This could be achieved through i) incremental gain of Rs 400-500/t from operating leverage as capacity increases from 4.3MT to 5MT next year and ii) Another Rs 400-500/t increment in margin from a higher VAP mix through its Raipur and Dubai plants. In H2CY25, retail demand could pick up, and the current discounts would be put off. ✓ **Strategy to penetrate newer markets:** To cater to the East Indian market, two greenfield plants are coming in Siliguri and Gorakhpur and one plant in Bangalore for a lighter section. These three plants will provide an incremental market of ~1.5MTPA, which will be ramped up in the next 2-3 years. Furthermore, the company is also focusing on international markets with the commencement of the Dubai plant (operating at 58% utilisation), and it has also received orders from Saudi Arabia.

** Note: Target Price is based on our Q3FY25 Result Update Report*

Top Conviction Ideas: Metals & Mining

Stock	Reco.	TP	Recommendation Rationale
Tata Steel	BUY	Rs 155*	✓ **Indian operations stood resilient:** Indian Adj. EBITDA (excl. the one-time benefit of provision) stood at Rs 6,110 Cr (down 26%/9% YoY/QoQ), largely in line with our estimate. Sales volume grew 8% YoY to 5.29 MT. Neelachal EBITDA grew impressively by 67% QoQ, and it is currently operating at rated capacity. Cost at KPO-II will come as it ramps up fully by FY27 due to operating leverage with its expansion from 3 to 8 MTPA. ✓ **UK EBITDA to be neutral by Jun'25 (unchanged from previous call):** EBITDA/t loss at UK narrowed by £114/t to £121/t QoQ, aided by fixed cost take-out programs, yielding £146/t cost saving and offsetting the £31/t drop in the realisation. On an absolute basis, there has been an improvement in fixed costs by about £70 Mn QoQ, mainly in relation to maintenance costs, employment costs, and operating charges upon closure of heavy-end assets in the UK. ✓ **Netherlands:** TSN is operating at rated 7 mtpa hot metal production after BF shutdown due to relining. However, EBITDA/t de-grew by £15/t QoQ at TSN, led by lower steel spreads due to subdued steel demand in Europe. Spreads have dipped to multi-year lows, with spreads including energy and carbon costs currently in the region of about €170 per ton (last witnessed in 2016). The company is focusing on cost-reduction programs to offset the impact of lower spreads. ✓ With the recent correction in stock price, we see an opportunity for a fresh entry with our TP of Rs 155/share.

**** Note: Target Price is based on our Q3FY25 Result Update Report***

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February 2025

Top Conviction Ideas: Pharmaceutical & Hospitals

Ankush Mahajan
Aman Goyal

Pharma & Hospital Sector: Q3FY25 Review

Q3FY25 Pharma Review – Stability in Hospitals; Growth Momentum in Pharma

✓ ***Key Highlights & Financial Performance***

- The pharmaceutical universe under our coverage reported Q3FY25 growth of 10.2% YoY and 2.3% QoQ, driven by strong growth in the India business (11.2% YoY) and stability in the US business despite a decline in gRevlimid sales.
- In the domestic market, the Indian Pharmaceutical Market (IPM) recorded 8% YoY growth in Q3FY25. Chronic therapies grew by 9%, while acute therapies saw a modest 4% growth, primarily due to a weak season for acute segments.
- Gross margins improved to 65.7%, reflecting a 152 bps increase YoY but a decline of 18 bps QoQ. This improvement was supported by the launch of niche products, low single-digit price erosion, a higher proportion of Indian business in the product mix, and stable raw material prices.
- The healthcare sector delivered robust growth in Q3FY25, with top-line revenue increasing by 23% YoY and 2% QoQ. This growth was driven by improved occupancy rates, which rose by 215 bps YoY, while ARPOB grew by 5% YoY.

Pharma Sector: Outlook

Pharma Back on Growth Track

- The pharmaceutical universe under our coverage reported Q3FY25 growth of 10.2% YoY and 2.3% QoQ, driven by strong growth in the India business (9.8% YoY) and stability in the US business despite a decline in gRevlimid sales.
- Gross margins improved to 65.7%, reflecting a 152 bps increase YoY but a decline of 18 bps QoQ. This improvement was supported by the launch of niche products, low single-digit price erosion, a higher proportion of India business in the product mix, and stable raw material prices. EBITDA margins stood at 25.2%, up 71 bps YoY but stable QoQ, despite the impact of lower gRevlimid sales in the US.
- On a QoQ basis, the US business, at $2107 Mn, remained nearly flat due to lower gRevlimid contributions (Cipla, Dr. Reddy, Aurobindo). Additionally, competition in gSuprep and gDoxycycline (Lupin) and the expected 3%-5% price erosion in the base business also contributed. Aurobindo's injectable business was affected by the WL issued for its Eugia III facility.
- In the domestic market, our universe reported 11.2% growth, while the IPM recorded 8% YoY growth in Q3FY25. Chronic therapies grew by 9%, while acute therapies saw a modest 4% growth, primarily due to a weak season for acute segments.
- Overall, we anticipate a strong pipeline in segments such as biosimilars, GLP-1, and peptides for pharmaceutical companies over the next three years. Companies with a higher proportion of chronic portfolios are outperforming the IPM. Consequently, **we maintain a positive outlook on companies like Lupin and Abbott India.**

Hospital Sector: Outlook

Healthcare: Robust Momentum led by Higher Occupancies & Payor Mix

- In our coverage, the healthcare sector delivered strong growth in Q3FY25, with top-line revenue increasing by 23% YoY and 2% QoQ. This was driven by improved occupancy rates, which rose by 215 bps YoY, alongside a 5% YoY increase in ARPOB, averaging Rs 57,080 across the industry. Higher purchasing power and increased insurance penetration contributed to the rise in occupied beds, providing greater access to healthcare services and driving growth.

- Operating margins stood at 24.1%, down 50 bps YoY and 150 bps QoQ, indicating stability in operating profitability. Max reported an operating margin of 26.3%, an increase of 65 bps QoQ, with an ARPOB of Rs 75,900, up 1% YoY. Fortis, with a 19.5% margin, achieved an occupancy rate of 67%, an increase of 300 bps YoY, largely driven by its mature hospital unit in Gurgaon. Similarly, Medanta reported an operating margin of 25.6%, higher than the industry average.

- Insurance payers contributed 34% to total revenues this quarter, growing 30% YoY and 5% QoQ. However, insurance penetration remains relatively low, presenting significant growth potential as awareness of health coverage rises and purchasing power improves. Additionally, high-growth therapies such as cancer and cardiac care continue to drive double-digit growth, further boosting ARPOB and occupancy rates.

- We expect the healthcare sector to sustain its growth trajectory, with annual ARPOB growth of 6% and an improvement of 100 bps in occupancy rates. Key growth drivers include a favorable shift in the payer mix, higher surgical volumes, and increasing insurance penetration. **We remain positive on Max Healthcare Institute and Fortis Healthcare Ltd.**

Pharma Sector: Volatility Amid U.S. Tariff Uncertainty

- It is expected that the Indian Pharma Industry will need to wait for the tariff issue to be resolved. The products supplied by the Indian Pharma Industry to the U.S. fulfill a crucial role in helping the U.S. government control healthcare costs. There is a high possibility that certain high-value drugs, which are essential, could be exempted from tariffs. However, it is expected that generic pharma products will likely be spared, as the generic business has already experienced significant price erosion over the past few years.

- In the event that tariffs are imposed, it is expected that most of them will be passed on to consumers. Therefore, we do not foresee a significant negative impact on the industry. India's competitive advantage in this sector is long-term—it won't disappear overnight. Even if new pharma manufacturing is initiated elsewhere, it takes at least 5 to 7 years to establish a new facility, get products approved, and begin production. This is a long-term process. As a result, we do not expect any immediate short-term impact from tariffs on the pharma industry.

- The Indian Pharma Industry's manufactured products fulfill an important healthcare need in the U.S., so they are expected to be excluded from the scope of tariffs. Even if tariffs are imposed, most of them will likely be passed on to consumers. The exact impact on business is difficult to predict, but its essential role in the industry gives confidence that, if there is any negative effect, it will be minimal. **We look forward to more clarity in the coming months from the U.S. Trump Administration, as tariffs have not yet been announced. We believe generics could be spared from the implementation of tariffs. If tariffs are introduced, considering the important role of these products, the impact will be minimal.**

- **We believe there could be volatility in Indian Pharma stocks until there is more clarity on tariffs.**

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Short and Medium-term Outlook - Pharma

Short Term

Trend in price erosion after the normalisation of drug shortages supply in the US

India: Weak acute season and NLEM impacted growth

Medium Term

Better sales growth was led by gRevlimid and the launch of new products GLP-1 & Peptides

Field force expansion to drive growth in India

Better margins for full year due to normalized cost inflation and moderation in US Price Erosion

Key Monitorables – Price Erosion, Margins Expansion, and Launch of New Products

Short and Medium-term Outlook - Hospitals

Short Term

Intense competition among peer hospitals and oversupplying of beds in micro markets.

Delay in commissioning beds.

Medium Term

Higher Occupancies & improved ARPOB Across the industry.

Key therapies Like Cardio & Oncology growing by double digit.

Insurance payor, Purchasing Power, and Surgical mix pacing momentum are key drivers.

Key Monitorables – Improved Occupancies; Insurance penetration; New Hospital projects

Top Conviction Ideas: Max Healthcare

Stock	Reco.	TP	Recommendation Rationale
Max Healthcare	BUY	Rs 1,315*	• Max Healthcare reported a revenue of Rs 2,281 Cr, surpassing expectations, driven by a marginal decline in occupancies and steady ARPOB, aided by new hospitals. ARPOB stood at Rs 75,900, flat YoY, while occupancy improved to 75%, up 200 bps YoY on a like-to-like basis, supported by an 8% YoY increase in occupied bed days. The top line grew 34% YoY, with strong contributions from both mature and developing hospitals. EBITDA margins stood at 26.3%, down 136 bps YoY but improving sequentially by 65 bps. Adjusted PAT was Rs 390 Cr, reflecting 15% YoY growth, driven by operational efficiencies and cost control. • Developing hospitals showed a steady ramp-up, with revenue growth of 22% YoY. Occupancies improved by 800/400 bps QoQ/YoY, leading to a 14.5% rise in occupied bed days, although ARPOB remained subdued due to a shift in the payer mix. Max Dwarka achieved EBITDA breakeven within six months, reporting Q3 revenue of Rs 59 Cr, while Max Lucknow and Max Nagpur delivered EBITDA growth of 58% and 50% YoY, respectively. • Mature hospitals continued strong performance, delivering 16% YoY revenue growth, with occupancies rising by 200/400 bps QoQ/YoY and ARPOB improving by 7% YoY. Growth was supported by higher realisations from existing hospitals and an improved therapy mix. EBITDA margins for mature hospitals expanded by 70 bps YoY to 28.6%, benefiting from scale efficiencies. • **Outlook:** Max Healthcare's revenue mix remains well-balanced, with continued growth in institutional and international patient segments. The recent increase in institutional business share is expected to stabilise as higher-value payer segments expand. The short-term margin impact from new hospital ramp-ups should gradually ease as these facilities scale operations. Lucknow and Nagpur are expected to witness further profitability expansion, driven by higher occupancy rates and the introduction of new clinical programs.

Note: Target Price is based on our Q3FY25 Result Update Report

Top Conviction Ideas: Lupin

Stock	Reco.	TP	Recommendation Rationale
Lupin Ltd	BUY	Rs 2,500*	• **Lupin reported strong results, exceeding expectations**, with revenue growing 11% YoY. Growth was led by the India and US businesses, which expanded by 11.9% and 12.3% YoY, respectively, while the EMEA business recorded a robust 20.9% YoY growth. However, the Emerging Markets segment declined by 4.7% YoY, while the API business gradually recovered with a 4% YoY increase. • **Gross margins improved by 330 bps YoY** and remained flat QoQ, supported by a favourable product mix, lower input costs, a reduced share of in-licensed products, and enhanced cost efficiencies. EBITDA margins improved by 350 bps YoY, remaining stable QoQ. Reported PAT grew 40.1% YoY, surpassing expectations. • **North America Business**: Lupin's US sales stood at $235 Mn, reflecting a 10.8% YoY growth in constant currency. Overall, the segment reported a revenue of Rs 2,121 Cr, up 12.3% YoY. Growth was driven by volume expansion in inline products and new product contributions, although pricing pressure and competition in gSuprep and gAlbuterol impacted performance. • **Outlook:** Lupin has a strong pipeline of niche products that could drive double-digit growth in the US market. Injectable products such as Glucagon and Dalbavancin, with a combined market opportunity of $500 Mn, are expected to launch within six months. Additionally, Liraglutide and Risperidone could contribute to revenue in FY27E. Lupin is also exploring opportunities in biosimilars, including Ranibizumab and Aflibercept, while Tolvaptan is expected to enhance its generic portfolio.

Note: Target Price is based on our Q3FY25 Result Update Report

Top Conviction Ideas: Fortis Healthcare Ltd

Stock	Reco.	TP	Recommendation Rationale
Fortis Healthcare Ltd	**BUY**	**Rs 860***	• Fortis Healthcare reported a revenue of Rs 1,928 Cr, in line with expectations, driven by higher ARPOB and improved occupancy levels. ARPOB stood at Rs 67,123, up 9.9% YoY, while occupancy improved to 67% (up 300 bps YoY), supported by a 4.3% YoY increase in occupied bed days. Hospital segment EBITDA margins stood at 20%, up 200 bps YoY. The rebranded Agilus Diagnostics reported muted growth of 5.2% YoY, with EBITDA of Rs 49 Cr, reflecting a 16.1% margin, up 450 bps YoY. • The company's topline grew by 14.8% YoY, while overall EBITDA margins stood at 19.5%, down 241 bps QoQ but showing an annual improvement of 255 bps. The reported PAT was Rs 254 Cr, including an exceptional gain of Rs 24 Cr from the divestment of Richmond Road Hospital, Bangalore. Adjusted PAT grew 71.6% YoY, supported by operational efficiencies and cost control. • The 9.9% rise in ARPOB was largely driven by an improved payer and case mix. The international patient segment generated a revenue of Rs 132 Cr during the quarter, up 17% YoY, contributing 8% to total revenue. Key specialties performed strongly, accounting for 62% of total hospital revenue (up from 61% YoY). Oncology grew 30% YoY, led by a 44% increase in haematology and bone marrow transplants, while neurosciences saw 18% growth. Robotic surgeries surged 77%, underscoring the company's focus on advanced procedures. Other key specialties, including cardiac sciences, gastroenterology, orthopaedics, and renal sciences, also exhibited robust expansion. • **Outlook:** Fortis Healthcare remains focused on profitable growth through brownfield expansions, operational efficiencies, and portfolio optimisation. The company targets 14-15% revenue growth in the hospital business, with ARPOB expected to grow at 5-6% YoY. Hospital EBITDA margins are projected at 20.5% for FY25, with a long-term goal of reaching 25% through higher occupancy and an improved specialty mix..

**** Note: Target Price is based on our Q3FY25 Result Update Report***

AXIS SECURITIES

February 2025

Top Conviction Ideas

Banking, Financial Services & Insurance (BFSI)

Dnyanada Vaidya
Pranav Nawale

Banks – Q3FY25 Performance Review

Earnings Growth Weak; Asset Quality Pain in Unsecured Segments Persists

- **Banks** (incl. SFBs) under our coverage reported an in-line performance, delivering a credit growth at ~12% YoY, mirroring systemic growth. This was owing to the continuous and conscious slowdown visible in the unsecured segments, particularly microfinance, credit cards and personal loans, as asset quality concerns continued to haunt. Credit growth was primarily driven by **Retail** and **SME portfolios**, while banks continued to remain aloof in pursuing corporate growth given pricing pressures. With macro headwinds and asset quality uncertainties, most managements have refrained from giving credit growth guidance for FY26E.
- **Deposit growth** during the quarter **was soft**, with competitive intensity remaining high. Deposit growth was mainly driven by TDs, while CASA deposits de-grew QoQ, weighing on CASA ratios for majority banks. During the quarter, banks started to shift their focus towards mobilising CASA Deposits and have refrained from indulging in irrational TD pricing to maintain CoF, anticipating a rate cut.
- **NIMs for most banks moved with a slight negative bias** during the quarter, primarily driven by (i) the continued repricing of deposits driving CoF higher, (ii) regulatory-mandated reclassification of penal interest as penal charges, (iii) elevated slippages from the unsecured pool (specifically for lenders with higher exposure to the stressed segments), resulting in higher interest reversals, and (iv) Shift in the portfolio mix towards lower-yielding segments or slower growth in better-yielding segments. Thus, NII growth for our under-coverage banks was marginally below our expectations at 7/1% YoY/QoQ.
- **Fee income** growth was in line with business growth. Treasury income for most banks was weak, weighing on operational profitability. Opex growth was modest, with conscious efforts to keep Opex ratios under check, especially amidst slower business growth. Collectively, these factors weighed on PPOP, which grew by 12% YoY and de-grew by 8% QoQ (lower vs. our estimates by ~5%).
- **The stress in the personal loans, credit card and microfinance portfolios continued to keep slippages elevated**. Asset quality for most banks remained stable QoQ, barring a select few, with support from healthy recoveries. Credit costs continued to remain elevated for banks (**mainly SFBs**) with higher exposure to unsecured segments, primarily microfinance. Earnings growth decelerated, de-growing at 4% QoQ in Q3FY25.

NBFCs – Q3FY25 Performance Review

Asset Quality Concerns in Certain Segments Persist; Growth Momentum Calibrated

- During the quarter, disbursement momentum improved for vehicle financiers and diversified financiers, while microfinanciers continued to grow in a calibrated manner. Owing to political factors, disbursement growth momentum was hampered for housing financiers under our coverage. Our under-coverage **NBFCs (across financiers)** reported a healthy AUM growth of 23/5% YoY/QoQ, largely in line with our estimates. Within our coverage universe, Vehicle Financiers/Housing Financiers/Diversified Financiers/Microfinanciers/Gold Financiers reported 23/12/28/6/14% YoY AUM growth.
- **Margins trends remained divergent, with diversified financiers and vehicle financiers reporting largely steady or slight improvement in NIM trends (ex-Shriram Finance owing to excess liquidity)** led by stable CoF. On the other hand, **housing financiers, microfinanciers** and **gold financiers** reported a **sharp deterioration in NIMs**, driven by yield pressures (slower growth and higher slippages) and an inch-up in CoF. Thus, despite in-line AUM growth, NBFCs under our coverage reported NII growth of ~19/4% YoY/QoQ in Q3FY25, marginally lower than our estimates, owing to sharper-than-expected NIM contraction for certain financiers.
- **Collection Efficiency (CE) ex-MFI** has been broadly stable with a positive bias QoQ; however, it continues to remain slightly below normalised levels. CE in the CV segment improved marginally. However, the pace of improvement has been lower compared to a strong improvement generally visible in Q3 historically. The concerns around the asset quality of **Microfinanciers** continued to remain elevated, with collections remaining below par, though slightly better or at par vs Q2FY25. Most microfinanciers have indicated that fresh PAR accretion has peaked out, with trends expected to reverse from Q1/Q2FY26 onwards. Continued asset quality concerns kept credit costs elevated, dampening the pace of earnings. Credit costs for our coverage NBFCs increased significantly by 65/18% YoY/QoQ, resulting in a miss on our earnings estimates. Earnings (ex-one off gains in Shriram Finance) for our coverage NBFCs (across financiers) de-grew by ~1/4% YoY/QoQ.

Diversified Financials – Q3FY25 Performance Review

Mixed Quarter; Credit Card Players Remain Underperformers

- For ***Credit Card Issuers (SBICARD),*** the collection efficiency trends have improved in Q3FY25. ***The company has witnessed a reduction in the flows into delinquencies and the delinquency trends in the new customer acquisitions.*** This can be credited to the several steps taken to strengthen new customer acquisition and the underwriting and portfolio management framework to tackle the rising stress in the credit card portfolio. SBIC has also seen green shoots on recoveries from written-off accounts, which have improved in Q3FY25 vs Q2FY25. Thus, with positive trends continuing on asset quality metrics, SBIC expects credit costs to moderate, driving earnings growth. The impact of the festive season was visible on operational performance.
- ***Life Insurer (SBILIFE)*** reported a ***good quarter,*** reporting strong APE growth of 13/30% YoY/QoQ during the quarter. In Q3FY25, VNB margins (calc.) stood at 26.9% despite a higher share of ULIPs. The full impact of margins re-pricing of certain non-PAR products visible in Q3FY25 and the launch of protection products helped SBILIFE partially offset the impact of higher ULIPs in the product mix. While the Banca channel will continue to dominate the distribution mix, the agency channel will continue its strong growth trajectory. Since there has been no clarity from the regulator on the restrictions on the Banca business being limited to 50%, the company's focus on the agency channel could take care of any such contingency.
- ***Asset Management Company (NAM)*** reported a healthy MF QAAUM growth of 51/4% YoY/QoQ while continued market share gains across segments. The net flows in Jan'25 haven't shown any signs of distortion and stay on par with Dec'24 trends. While SIP closures were higher in Dec'24, NAM performed better than the industry, with lower SIP discontinuations. This can be credited to the retail-focused, fragmented customer, ensuring better customer retention. During the quarter, NAM launched two new products in the index fund category to further augment the company's passive offerings.

Q3FY25 PERFORMERS – WINNERS AND LOSERS

	HITS	MISSES
Banks	ICICI BANK	IDFC FIRST BANK
	HDFC BANK	KARNATAKA BANK
	KOTAK MAHINDRA BANK	EQUITAS SFB
	DCB BANK	BANDHAN BANK
	CITY UNION BANK	IDFC FIRST BANK
NBFCs and Diversified Financials	BAJAJ FINANCE	SBI CARDS
	CHOLAMANDALAM INV & FIN	CREDITACCESS GRAMEEN (▼ Rating Downgrade)
	MAS FINANCIAL	CANFIN HOMES
	SBI LIFE	MANAPPURAM FINANCE

** Based on Q3FY25 Performance

The Way Forward for

Banks

- ✓ With the competitive intensity amongst banks continuing to remain high, we expect an **enhanced focus on deposit mobilisation** to continue by banks. Managements have highlighted that banks will avoid irrational deposit pricing while anticipating the rate-cut cycle to begin. With the interest rate cycle reversing after a 24-month pause on rates, we do not expect an immediate downward repricing of deposits, especially given the tight liquidity conditions.
- ✓ Amidst stress persisting in the unsecured segments – **credit card, microfinance** and **personal loans** and demand weakening in certain pockets, we believe banks would continue to exercise caution and thus expect banks to **exit FY25 with credit growth ranging between ~11-12%**. A clear focus area remains to maintain a balanced LDR; hence, deposit growth will also mirror credit growth. We expect our under-coverage banks (including SFBs) to deliver a steady credit growth of ~14% CAGR over FY25-27E against a deposit growth of ~14% CAGR over the same period, thereby maintaining a steady incremental LDR.
- ✓ With the RBI reversing the interest rate cycle in Feb'25, **the impact on Q4FY25 NIMs will be limited, and the impact in its entirety will be visible from Q1FY26 onwards.** The RBI's action in its Apr'25 MPC meeting will be keenly eyed. **Pvt. Banks are likely to face higher margin pressures,** with a bulk of their book being EBLR-linked. On the other hand, **PSU Banks** remain fairly insulated, given a higher share of MCLR-linked loans (as repricing happens with a lag). Similarly, **SFBs** are expected to benefit in the rate cut cycle given a higher share of fixed-rate loans. **Most banks continue to prioritise margins over growth.**
- ✓ **Asset quality concerns will continue to trouble** lenders with **higher exposure to troubled unsecured segments** for the next couple of quarters. However, the asset quality metrics in the secured portfolio continue to hold up well. We expect credit costs for MFI-dominant banks to remain elevated in the near term.
- ✓ At this juncture, we would prefer banks with promising growth prospects, healthy deposit franchises, stable asset quality metrics and strong and steady management teams.

The Way Forward for

NBFCs

- ✓ Stress in the microfinance sector is likely to have peaked out and should recede over the next 2 quarters. Microfinanciers appear fairly confident of growth normalisation from H2FY26 onwards. However, with the new MFIN guardrails applicable from Apr'25, we would watch out for any additional stress that might spill over. With capacity utilisation showing a gradual improvement trend, we expect vehicle financiers to resume their growth momentum, though with caution. Additionally, the **recent budgetary announcements with rate cut tweaks are likely to support retail demand. We pencil in healthy AUM growth of ~22% CAGR over FY25-27E.**
- ✓ Backed by expectations of growth in the unsecured (better yielding) segments gradually picking up along with rate cut, we could expect positive movement on NIMs for **credit card issuers, diversified financiers, gold financiers and vehicle financiers** under our coverage (given a higher share of fixed-rate loans). **We expect NBFCs (across financiers) under our coverage to deliver NII growth of ~22% CAGR over FY25-27E**.
- ✓ Despite a brake on delinquencies, microfinanciers/credit card issuers will continue to see elevated slippages in Q4FY25/Q1FY26. Thus, credit costs will continue to remain elevated for microfinanciers for the coming couple of quarters. For other financiers, we could expect better recoveries going into Q4FY25, supporting asset quality improvement. Expecting recovery in both microfinance and credit cards from early FY26, we expect gradual normalisation in credit costs, thereby supporting earnings. Near-term pressures on earnings will persist. Navigating the headwinds effectively, we expect **NBFCs under our coverage to deliver an earnings growth of ~25% CAGR over FY25-27E.**

Medium Term Outlook

(a) Deceleration in deposit growth could weigh on Credit growth

(b) Continued concerns around pressure on collections and rising in the unsecured segments could keep credit costs elevated for Bank/NBFCs

(a) Continued demand visibility in the Retail/MSME segment, with gradual pick-up in corporate lending

(b) Steady Asset Quality Metrics with no major signs of stress visible in secured retail and corporate segments, thereby keeping credit costs under control

(c) CRR cut and boost to liquidity by RBI key positives

(d) Deferment of implementation of LCR and ECL norms positive

Key Monitorables

(1) Deposit Growth – a key decisive factor to ensure credit growth sustenance
(2) Asset Quality headwinds in the unsecured lending space
(3) NIM movement for banks with the rate cycle reversing

Top Conviction Ideas: Tier I Banks

Stock	Reco.	TP	Recommendation Rationale
ICICI Bank Ltd.	BUY	Rs 1,500*	✓ **Consistent Outperformer**: The bank reported yet another strong quarter, demonstrating strong credit growth, healthy margins, and robust asset quality, thereby keeping credit costs largely steady. ***ICICI Bank remains our most preferred pick amongst the banks.*** ✓ **2%+ RoA delivery**: We expect the bank to continue delivering a strong performance over the medium term enabling a consistent RoA/RoE delivery of 2.2-2.3%/17-18% supported by (1) strong business growth while maintaining a steady C-D Ratio, (2) focus on strengthening fee income, (3) range-bound Opex ratios with no aggressive investments in sight, (4) pristine asset quality metrics and (5) adequate capitalisation. We factor in strong business growth and expect the pace of earnings growth to remain healthy. We factor in Advances/NII/Earnings growth of 16/11/12% CAGR over FY25-27E. ✓ **Asset quality remains pristine:** Gauging the headwinds in the unsecured lending space, ICICIB gradually decelerated its pace of growth in the unsecured segment (~14% portfolio mix). In line with industry performance, the bank has also seen an inch-up in delinquencies in the Credit Card and Personal Loan portfolio. However, trends are expected to stabilise in the coming quarters. The credit costs in the retail and corporate portfolios continue to remain stable. Business banking credit costs are lower than credit costs in the retail portfolio. The bank does not expect any significant asset quality challenges, with performance remaining stable across segments and expects credit costs to be capped at ~50bps on a steady state basis.

Note: Target Price is based on our Q3FY25 Result Update Report

Top Conviction Ideas: Tier I Banks

Stock	Reco.	TP	Recommendation Rationale
HDFC BANK We understand your world HDFC Bank Ltd.	BUY	Rs 2,000*	✓ **Progressing well on LDR improvement; Growth momentum to resume from FY26:** In line with HDFCB's stance of improving LDR aggressively to pre-merger levels of mid-80%, the bank has been progressing well, with deposit growth outpacing credit growth. We expect the bank's efforts to materialise with LDR dropping to ~87% by FY27E. HDFCB continues to calibrate growth, considering concerns about both credit quality and pricing (mainly in corporate lending). The bank is reorienting itself amidst a challenging environment, preparing to resume its growth journey and gaining market share as macros change. ✓ **Best-in-class Asset Quality**: HDFCB has maintained pristine asset quality across cycles, which can be credited to its strong underwriting practices and risk-calibrated lending. The management also emphasised that asset quality metrics across segments remain best-in-class, and the bank is confident that these trends are sustaining. ✓ **RoA to improve**: HDFCB remains an outlier among banks because of its strong asset quality performance, given the rising stress, especially in the unsecured segment. Thus, supported (i) Adequate levers to improve NIMs, (ii) Controlled Opex growth and improving productivity ensuring cost ratio moderation, and (iii) Pristine asset quality ensuring controlled credit costs should enable HDFCB to deliver an improving trend on return ratios. RoA/RoE is expected to range between 1.8-1.9%/14-15% over FY25-27E. **Faster improvements in LDR and NIM expansion remain key re-rating levers for the bank.**

Note: Target Price is based on our Q3FY25 Result Update Report

Top Conviction Ideas: Tier I Banks

Stock	Reco.	TP	Recommendation Rationale
State Bank of India	BUY	Rs 1,025*	✓ **Growth visibility is healthy; momentum remains buoyant:** SBI has reaffirmed its credit growth guidance of 14-16% in FY25, supported by healthy demand visibility in the retail portfolio and a strong corporate pipeline. The corporate loan pipeline currently stands at Rs 4.8 Tn (largely capex driven), of which Rs 2.2 Lk Cr have been sanctioned. The bank also expects growth in the Xpress Credit portfolio to pick up gradually (expecting double-digit growth), supported by the budgetary boost to consumption. We expect SBI to deliver a healthy advances growth of 13% CAGR over FY25-27E. ✓ **Asset Quality trends to remain healthy:** In Q3FY25, the SMA2 book inched-up sharply QoQ. However, it includes a long-term government sector customer of the Bank, with a fund-based outstanding of Rs 58 Bn. The account has been pulled back subsequently. Going ahead, the management does not expect any major negative surprises on asset quality across segments. Thus, as credit costs continue to normalise with the book ageing, SBI remains confident of capping credit costs at 50bps across cycles. ✓ **Cruising along to deliver RoA of 1%+**: SBI remains well-poised to sustain its growth momentum supported by its comfortable LDR, providing it levers to accelerate credit growth (especially in retail and SME), offering scope to support NIMs. We believe SBI could continue to deliver a sustainable RoA of 1% over the medium term backed by (1) Healthy growth visibility across segments, (2) Strengthening deposit franchise with focus on CASA deposits, (3) Ramping-up the fee income profile, (4) Controlled Opex and Provisions.

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Top Conviction Ideas: Tier I Banks

Stock	Reco.	TP	Recommendation Rationale
City Union Bank	BUY	Rs 215*	✓ **Growth momentum resumes, visibility healthy:** CUB will continue to focus on its core segments – MSME and Gold loans to drive growth hereon. Growth visibility has improved with the implementation of new digital initiatives. The bank does not intend to pursue growth in the unsecured segments. CUB has launched retail products - LAP, Home Loans and Affordable Housing - which are currently in the pilot stage and have been received well. Their contribution to the portfolio is expected to improve further to 8-9% over the next 3-4 years. We pencil in ~14% CAGR growth over FY25-27E, expecting the retail franchise to contribute healthily to incremental growth. ✓ **Asset Quality on an improving trend:** The management expects the slippages to trend downwards as it expects to cap its FY25 slippages at Rs 800 Cr and further improve going into FY26, with slippages maintained at Rs 700 Cr. Meanwhile, recoveries from live NPA and written-off accounts are expected to remain healthy and over and above the slippages for the next couple of quarters, thereby aiding asset quality improvement. CUB's negligible presence in the unsecured segment has insulated it from asset quality challenges visible across other players. ✓ **NIMs remain steady at 3.6% (+/-10bps):** The management remains confident of maintaining margins at 3.6% (+/-10bps) even in a rate cut cycle. The bank has successfully transitioned the gold loan book from a floating rate (primarily EBLR-linked) to a fixed rate, which should bode well from a margin perspective.

Note: Target Price is based on our Q3FY25 Result Update Report

Top Conviction Ideas: NBFCs and Diversified Financials

Stock	Reco.	TP	Recommendation Rationale
Bajaj Finance Ltd.	BUY	Rs 9,050*	✓ **Credit costs to moderate gradually:** BAF is continuing to take proactive risk actions by cutting segments and pruning exposures in stressed segments. The company has also brought down the share of customers having 3+ live unsecured loans significantly, and as it exits FY25, the share will be at par with pre-COVID levels. BAF has seen an improvement in collection efficiency (CE) across most segments in Dec'24-Jan'25 vs Oct-Nov'24 and expects the trend to continue. Thus, the management expects credit costs to settle at 2-2.05% in Q4FY25 and the downward trajectory to <2% to continue in FY26, provided Q4FY25 credit costs are within the guided range. BAF's management remains confident of maintaining GNPA/NNPA in a steady range of 1.2-1.4%/0.4-0.5% on a steady-state basis. **BAF will continue to prioritise asset quality over growth**. ✓ **Growth momentum to remain healthy; Airtel partnership to contribute to growth:** BAF's AUM growth was broad-based, except for slower growth in the auto finance portfolio. Going forward, the AUM mix is expected to remain largely unchanged. The management has guided for ~25% AUM growth to continue over FY26. Additionally, the recently announced partnership between BAF and Bharti Airtel (Airtel) offers the company the opportunity to tap into Airtel's customer base. Currently, 9 of BAF's products will go live by Mar'25, and the company will look to expand its product offerings through FY26. The company has identified a customer base of 200 Mn Airtel customers that does not overlap with BAF. We expect BAF to deliver a healthy ~26% CAGR growth over FY25-27E. ✓ **NIMs to remain stable:** The management has indicated that CoF is expected to remain stable hereon. Going into FY26, the management expects a 4- 5bps respite on CoF, with or without a rate cut. On the asset side, the management remains confident in protecting yields despite the fact that pricing pressure is visible in certain segments. However, the company will continue to balance margins and growth while prioritising margins. We expect margins to remain steady, ranging between 9.7% and 9.8% over FY25-27E.

Note: Target Price is based on our Q3FY25 Result Update Report

Top Conviction Ideas: NBFCs

Stock	Reco.	TP	Recommendation Rationale
Cholamandalam Investment & Finance Company Ltd.	BUY	Rs 1,650*	✓ **Asset Quality improvement from Q4FY25 onward:** The management expects asset quality to improve going into Q4FY25 and beyond. A majority of the stress in the CSEL portfolio is from the portfolio sourced through its partners, which the company is gradually phasing out over the next year, which should help in reducing NPAs in this segment. Additionally, the credit costs in the Home Loan (HL) and LAP book are gradually normalising as the book continues to season. CIFC's focus remains on improving collection, with the company adding 55% of the incremental hiring towards strengthening collections. Currently, the strength of the collections team is ~31K employees. The management expects credit costs to trend downwards from Q4FY25, with FY25 credit costs at ~1.4%. ✓ **VF portfolio asset quality to witness improvement:** The stress build-up in the SCV and LCV portfolio has been owing to slowing consumption and rural demand impacting the capacity utilisation of vehicles. However, on the brighter side, the management has indicated that the capacity utilisation of SCV/LCVs has improved meaningfully to 70-80% in Q3FY25 vs a bottom of ~50% over Q1-Q2FY25. Within the VF portfolio, the asset quality of 2-wheelers used CVs and used cars continues to hold up well. In the HCV portfolio, the recovery is slower. However, given CIFC's lower exposure, the impact is expected to be limited. Thus, VF portfolio credit costs are expected to gradually trend downwards over FY26. ✓ **Confident of delivering 25% growth:** The management has reiterated its guidance of delivering AUM growth of 25% over the medium term. CIFC will aim to maintain a disbursement growth of 15% in HL over the medium term, which should translate into an AUM growth of 25-30%. Similarly, in the LAP portfolio, the company is eyeing to clock a healthy disbursement growth of 25% over the medium term, driving strong AUM growth of 35-40%. We expect CIFC to deliver a broad-based AUM growth of ~26% CAGR over FY25-27E, with growth driven by HL and LAP segments.

*** Note: Target Price is based on our Q3FY25 Result Update Report***

Top Conviction Ideas: NBFCs

Stock	Reco.	TP	Recommendation Rationale
Shriram Finance Ltd.	BUY	Rs 705*	✓ **Optimism around growth momentum sustaining:** The management highlighted that rural demand remains robust and is expected to drive healthy AUM growth for SFL. Growth in the CV segment has been slower, primarily led by an increase in ATS (prices up ~30% over the past three years) rather than volume growth. Volume growth in the CV segment has been constrained due to limited capacity additions, with existing capacity witnessing improved utilisation rates. In PV financing, growth has been driven by both value and volume. SFL's market share in PV financing remains low, and the management foresees a significant growth runway ahead. Limited investment in public transport, except in select metro and Tier I cities, coupled with the graduation of 2W customers to used PVs, is expected to sustain buoyant growth in the segment. In the 2W segment, SFL aims to maintain 2x industry growth. ✓ **No concerning trends on asset quality visible:** SFL's asset quality deteriorated marginally in contrast to general H2 trends, wherein asset quality witnesses gradual improvement. However, the management sounded confident in maintaining stable asset quality, with no structural challenges visible. SFL expects asset quality improvement driven by healthy rural cashflows, with improvement visible in Q4FY25. **Credit costs are expected to remain under control at <2%.** ✓ **NIMs to rebound:** During Q3FY25, NIMs contracted by ~26bps, mainly due to excess liquidity due to a large ECB transaction. This had an impact of ~20bps on margins. The management has stated that the excess liquidity will be moderated over the next couple of quarters and will return to the company's earlier policy of maintaining 3 months liquidity buffer. Thus, margins are expected to improve going into Q4FY25. The incremental CoF stabilised and improved by 2bps during the quarter. This is expected to support NIMs going forward. **The rate cut would benefit the company's margins. We expect NIMs to remain steady at 8.7% (+/-5bps) over FY25-27E.**

****Note: Target Price is based on our Q3FY25 Result Update Report***

AXIS SECURITIES

February 2025

Top Sector Ideas: Infra-Road & Others

Uttam Kumar Srimal
Shikha Doshi

Infra-Road & Others Sector: Q3FY25 Review

Mixed Performance; Better Awarding and Execution Expected in FY26

- **Financial Performance:** During the quarter, road infrastructure companies under our coverage posted Revenue/EBITDA/PAT growth of -9%/-5%/-2% YoY, compared to our expectation of -3%/-4%/-11% YoY. The deviation in performance was primarily due to sluggish execution and delays in receiving AD. Profit deviation was attributed to KNR Constructions receiving an arbitration claim.
- **EBITDA Margins:** In Q3FY25, road infrastructure companies reported EBITDA Margins of 15.3% against our estimate of 14.2%. The improvement was largely driven by lower raw material costs and a reduction in employee expenses at HG Infra, GR Infraprojects, and J Kumar Infraprojects.
- **Road Sector Company-Wise Performance:** H.G. Infra and J Kumar Infraprojects recorded YoY revenue growth driven by strong execution, while GR Infra underperformed due to sluggish execution. PNC Infratech and KNR Constructions fell short of expectations due to a lower executable order book. However, in the case of PNC Infratech, NHAI lifted its ban on the company from bidding for NHAI projects.
- **Non-road Sector Company-Wise Performance:** KEC delivered a strong performance driven by the execution of high-margin T&D projects. Kalpataru Projects met expectations on the revenue front but fell short on PAT due to higher interest costs. RITES and PSP Projects reported lower revenue as project execution faced delays. Ahluwalia Contracts lagged behind expectations due to the NGT ban imposed in Delhi.

Short Term Outlook

- **Improvement in Project Awarding:** Awarding activity picked up during the quarter for most covered companies, except KNR Constructions. NHAI awarded ~970 km in 9MFY25, a sharp increase from just 227 km in H1FY25, as project awards were subdued in Q1FY25 due to the general elections. However, the awarding remains significantly below the FY25 target of 5,000 km and the 2,500 km awarded in FY24. The pace of NHAI project awards in FY25 is expected to be notably slower than in previous years, impacted by election cycles and a shift in focus toward upgrading existing highways rather than developing new ones. That said, awarding activity is expected to gain momentum in FY26, backed by a strong NHAI bidding pipeline and the Ministry's plan to award projects worth Rs 3,00,000 Cr in FY25 and beyond.

- **Pace of Road Construction Slowed Down:** The pace of national highway construction in India is projected to decline by around 7-10% in FY25, with construction slowing from 12,350 km in FY24 to an estimated 11,100-11,500 km in FY25, translating to a rate of approximately 31 km/day. The slowdown is primarily due to execution challenges, rising competition, and significant delays in receiving appointed dates after project awards. Additionally, construction progress remains weak, with ~3,190 km completed as of FY25YTD, compared to 6,644 km in FY24. This subdued awarding activity has negatively impacted order inflows for road construction companies.

- **Focus on Diversification:** Beyond road projects, companies have expanded into Railways, Metros, Solar, Power Transmission, Water Projects, and Tunneling to reduce dependence on road projects and enhance margins. Most companies anticipate these diversified segments to contribute 25-30% of their revenue.

Long Term Outlook

- **Pace of Road Construction to Gain Momentum:** The National Infrastructure Pipeline, aimed at overall infrastructure development, will continue to support road construction in the coming years. Despite challenges in FY25 and FY26, the Indian government remains committed to strengthening road infrastructure. The focus is shifting toward high-speed connectivity, with plans to complete 3,300 km of access-controlled highways in FY26, nearly doubling from 2,474 km as of December 2024.

- **Government Support Through Higher Capex:** In the Union Budget 2025-26, Capex for FY25 has been revised to Rs 10.2 Cr, while for FY26, it has been increased to Rs 11.2 Cr. An outlay of Rs 1.5 Lc Cr has been proposed for 50-year interest-free loans to states for infrastructure projects, with each infrastructure ministry required to develop a three-year pipeline of PPP projects. The government will launch a National Geospatial Mission to modernise land records and develop spatial data, improving land governance and planning. Additionally, a new Digital Network platform will streamline export-related documentation and trade processes.

- **Road Construction Companies to be Major Beneficiaries of Infra-spending:** Since most of these projects are expected to be awarded under the EPC and HAM models, road construction companies are positioned as key beneficiaries of the government’s infrastructure spending. With a strong order book, a healthy bidding pipeline, and a diversified portfolio, the sector's long-term outlook remains positive. **However, in the short term, there is cautious optimism, with a focus on new order inflows and the timely receipt of AD for awarded projects.**

- **We remain positive about the sector from a medium- to long-term perspective.**

AXIS SECURITIES

Short and Medium-term Outlook

Short Term

Order Inflow: Slow awarding activity to decrease revenue visibility

Delay in Appointed Dates: Delays in appointed date to affect revenue growth

Medium to Long Term

Better Order Inflow: Awarding expected to increase in FY25

Govt. Support: Increase in Capex through various initiatives to support growth in the sector

Key Monitorables- Direction of RM; Appointed date; Order Inflow; and Execution

Top Conviction Ideas: Road Infra

Stock	Reco.	TP*	Recommendation Rationale
HG Infra Engineering Ltd	BUY	Rs. 1720*	✓ **Healthy Order Book:** As of December 31, 2024, the company's total order book stood at Rs 15,080 Cr, equivalent to 3x FY24 revenue. A significant portion, 94%, of these projects is attributed to the Government of India, with the remaining 6% from the private sector, ensuring strong revenue visibility for the next 2-3 years. The company is anticipated to achieve a 15% CAGR revenue growth over FY24-26E. ✓ **Diversified Revenue Streams:** Traditionally focused on Roads and Highways, the company has successfully expanded into the Railways and Solar sectors, securing multiple orders in these segments. These now contribute 25% of the total order book, reducing dependence on a single sector. Management is also exploring opportunities in the transmission sector, particularly in Tariff-Based Competitive Bidding (TBCB) projects, which share similarities with EPC projects. This diversification and an expanding sectoral presence are expected to support 15% CAGR revenue growth over FY24-26E. ✓ **Order Inflow & Segment Diversification:** The company anticipates an order inflow of Rs 11,000-12,000 Cr in FY25, with projects worth around Rs 8,200 Cr already secured in 9MFY25. Management expects 35-40% of the order book to come from non-road projects over the next 2-3 years. Additionally, the company aims to secure Rs 10,000-12,000 Cr in new orders in FY26.

** Note: Target Price is based on our Q3FY25 Result Update Report*

Top Conviction Ideas: Non Road

Stock	Reco.	TP*	Recommendation Rationale
Kalpataru Projects International Ltd	BUY	Rs 1350*	✓ **Robust order book:** As of 31st Dec'24, the company's order book stands at Rs 61,429 Cr, with YTD order inflows at Rs 20,181 Cr. Additionally, the company holds an L1 position in projects worth Rs 2,500 Cr. With a strong execution track record and growing opportunities across all segments, the company is well-positioned for steady revenue growth, projecting a 16% CAGR from FY24 to FY27. ✓ **EBITDA margins to improve:** This assessment highlights the temporary margin pressures faced by the company due to external factors, but the strong order book composition and efficiency-driven initiatives should support margin recovery. The projected 19%/31% CAGR in EBITDA/PAT over FY24-27E underscores the company's growth trajectory. ✓ **Reduction of stress in the water segment**: The sluggish performance in the water business has weighed on overall growth, with Rs 1,000 Cr infused into the segment during 9MFY25. Slow collections from JJM projects have been a key challenge, but the recent realisation of over Rs 240 Cr from January 2025 onward, along with an anticipated Rs 500-700 Cr collection in Q4FY25 or Q1FY26, signals improving cash flow. Furthermore, the Union Budget's commitment to 100% tap water coverage and increased funding for FY25-26 should drive faster collections and execution, supporting overall business momentum.

** Note: Target Price is based on our Q3FY25 Result Update Report*

Top Conviction Ideas: Road Infra

Stock	Reco.	TP*	Recommendation Rationale
J Kumar Infraprojects Ltd	BUY	Rs. 940*	✓ **Robust order book to drive revenue growth:** As of 31st Dec'24, the company's order book stood at Rs 20,529 Cr (5x FY24 revenue). The company is L1 in projects worth Rs 5,000 Cr, including two projects for the Maharashtra Expressway and one coastal road project for CIDCO in Mumbai. A healthy and robust order book provides revenue visibility for the next 3-4 years. We expect the company to report a revenue CAGR of 17% over FY24-FY26E. ✓ **Strong bidding pipeline:** The company has a strong bidding pipeline of Rs 40,000-47,000 Cr. This includes building projects worth Rs 8,000-9,000 Cr, metro and railway projects around Rs 7,000-8,000 Cr, and elevated corridors of approximately Rs 30,000 Cr. The company aims to win projects worth Rs 6,000-8,000 Cr in FY25. ✓ **Improvement in EBITDA margin:** The company anticipates that EBITDA margins will improve in FY26 and exceed 15%, driven by more efficient project execution and the acquisition of additional orders.

*** Note: Target Price is based on our Q3FY25 Result Update Report***

AXIS SECURITIES

February 2025

Top Conviction Ideas: Chemicals & Midcaps

SANI VISHE
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Chemicals Sector: Q3FY25 Review

✓ Pricing Pressure Persists with Some Hopes of Bottoming Out

- **Rising Volumes Signal Robust Demand, But at Lower Prices:** In Q3FY25, most chemical companies under our coverage reported volume growth and expressed confidence in meeting or coming close to their targeted volumes. However, subdued prices for key products resulted in weaker revenue growth and/or lower profitability. Management commentary suggested that inventory levels are normalising, and an uptick could be expected, though the timing of a clear revival remains uncertain. Logistical challenges stemming from Red Sea disruptions, which have impacted deliveries and freight costs, appeared to be easing to some extent. On the domestic front, the agrochemical industry demonstrated resilience despite unfavourable weather conditions and expects improved performance in the coming quarter with better weather conditions.

- **New Products Drive Revenue and Margins:** A few players, such as NFIL and Camlin, saw an uptick in prices for some end products, while most others continued to face pricing pressure. With external conditions remaining challenging, companies have intensified their focus on innovation, cost optimisation, and product diversification. Agrochemical players like Dhanuka and PI Industries reported strong growth in new products and plan to expand their product portfolios further. Aarti Industries, which has faced challenges in its energy business, is now looking to diversify its exposure to mitigate risks arising from fluctuations in gasoline prices.

- **Currency Fluctuations:** During the quarter, the rupee depreciated significantly against the dollar, while exchange rates against other currencies remained volatile. This adversely impacted companies with foreign currency debt or hedging contracts for their export exposure. However, most companies under our coverage have strong export exposure and could benefit from currency movements going forward as the impact reflects on the revenue side.

- **Outlook and Guidance:** While some companies in our coverage revised their guidance downward, most remain hopeful that prices have bottomed out. The demand outlook remains positive, though pricing will depend on multiple factors, including the ability of foreign players to continue dumping products, the potential imposition of new tariffs in the US, and fluctuations in raw material prices. The financial performance of chemical players in the coming quarter is expected to be driven by product differentiation and cost optimisation efforts.

AXIS SECURITIES

Chemicals Sector: Q3FY25 Review

✓ Financial Performance: Chemicals

Chemical companies in our portfolio delivered a mixed performance in Q3FY25. Those who achieved revenue growth through new product launches or innovation were able to sustain better margins, while others had to compromise on profitability due to their reliance on volume-driven growth at the expense of pricing. Additionally, most companies with foreign currency exposure, whether through debt or revenue, were impacted by currency fluctuations.

- **Dhanuka Agritech** posted a revenue of Rs 445 Cr, up 10% YoY and down 32% QoQ, largely in line with our estimate of Rs 458 Cr. The EBITDA came in at Rs 76 Cr, achieving a margin of 17%. The company experienced margin expansion on a YoY basis, primarily driven by a favourable product mix and new product introductions.

- **PI Industries'** revenues stood at Rs 1,901 Cr, up 0.2% YoY and down 14% QoQ, missing our estimate of Rs 1,992 Cr. The company reported an EBITDA of Rs 512 Cr, as its EBITDA margin declined to 26.9%, compared to 29.2% in Q3FY24 and 28.3% in Q2FY25, as it continued to face headwinds in the CSM Business.

- **Navin Fluorine International Ltd (NFIL)** reported strong all-around growth during the quarter and a significant margin recovery. It recorded a revenue of Rs 606 Cr, broadly in line with our estimate of Rs 594 Cr. EBITDA stood at Rs 147 Cr, exceeding our estimate of Rs 122 Cr, as EBITDA margins improved to 24.3% compared to 15.1% in the same quarter last year. PAT came in at Rs 84 Cr, up 7% YoY and 42% QoQ, beating our estimate of Rs 71 Cr.

- **Aarti Industries Ltd.'s** revenue came in at Rs 1,840 Cr, up 6% YoY and 13% QoQ, beating estimates by 5%. EBITDA was up 18% QoQ to Rs 232 Cr, driven by volume growth, operating leverage, and product mix improvements. The EBITDA margin stood at 12.6%, compared to 15% in Q3FY24 and 12% in Q2FY25. The company's PAT was Rs 46 Cr, down 63% YoY and 12% QoQ, primarily impacted by a mark-to-market loss of Rs 23 Cr on its long-term ECB loan due to rupee depreciation.

- **Apcotex Industries** reported a revenue of Rs 355 Cr, a notable 38% increase YoY, largely aligning with estimates. However, gross margins declined to 22.8%, down by 148 bps QoQ. EBITDA stood at Rs 27 Cr, with EBITDA margins declining 230 bps YoY and 21 bps QoQ to 7.6%. PAT came in at Rs 12 Cr, marking an increase of 4% YoY.

- **Archean Chemical Industries** reported a revenue of Rs 242 Cr, down 41% YoY and flat QoQ, missing our estimate by 15% due to subdued volumes of Bromine and Industrial Salt. EBITDA was Rs 80 Cr, down 45% YoY and up 7% QoQ, falling short of our estimates by 10%. The EBITDA margin stood at 33%, down 225 bps YoY.

- **Camlin Fine Sciences'** Q3FY25 performance beat our estimates on all fronts as revenue grew 12% YoY and 2% QoQ to Rs 433 Cr, and EBITDA came in at Rs 49 Cr. The EBITDA margin improved by 521 bps YoY to 11.3%. However, the company reported a net loss of Rs 7 Cr, primarily due to higher interest expenses.

- **NOCIL's** performance reflected continued pricing pressure and lower volumes as it reported a revenue of Rs 318 Cr, down 7% YoY and 12% QoQ, missing our estimate by 14%. EBITDA stood at Rs 24 Cr, down 51% YoY and 36% QoQ, while the EBITDA margin declined to 7.6% from 14.5% in Q3FY24.

Chemicals Sector: Outlook

✓ Focus on Cost Measures and New Growth Avenues

The first nine months of FY25 remained challenging for the chemical sector, impacted by subdued demand, an economic slowdown in key global markets, inventory destocking, oversupply in China, and concerns over further weakening global demand. Despite these challenges, the sector's structural growth story remains intact, supported by a strategic shift towards expanding export market share and resilient domestic demand.

- **Chemicals:** During this period, most companies were compelled to focus on operational efficiencies and innovation amid a challenging environment marked by subdued demand, oversupply, geopolitical tensions, and inflationary pressures. With market capacity exceeding demand, the industry is relying on price competitiveness to improve utilisation levels. Most players have been balancing pricing and volumes to safeguard EBITDA. While management commentary suggests early signs of recovery from FY26, uncertainties may persist over the next couple of quarters. The sector’s structural growth story remains intact, and companies using this phase to implement cost discipline and enhance capabilities will be well-positioned when a clear recovery emerges. Given the recent broader market correction, we see a meaningful upside in select coverage stocks that are poised for growth from FY26 onwards.
- **Agrochemicals:** We expect inventory levels at customers to normalise over the next two quarters, which may provide some support on the pricing front for agrochemical players. Domestically, with a strong reservoir position and a favourable groundwater situation, domestic revenues are expected to grow YoY in Q4. Over the medium term, we remain positive about the sector's growth potential despite the ongoing global industry challenges and uncertainties. Companies focusing on innovation, new product launches, and long-term partnerships are likely to experience a stronger recovery and margin improvement in the medium term.

Chemicals - Short and Medium-term Drivers

Negatives

Margins to remain under pressure

Aggressive dumping from China impacting sales realization

Few Product-specific Chemicals will take a few more quarters to normalize.

Higher freight cost and longer transit time

Higher competitive Intensity

Positives

Introduction of new products with further integration in product lines

Strategic Capex into new Chemistries

Efficient Inventory Management, and Cost Rationalization

Easing out of Freight Costs

Global recovery post-completion of the destocking cycle

Key Monitorables- Chinese dumping leading to over-supply and price erosion; Capex Plans; Demand trends across key end-user Industries; Update on the ramp-up of new projects, Freight costs and logistical Challenges, Imposition of new Tariffs in the USA

Midcap Opportunities: Review

✓ Financial Performance

Within midcap stocks under our coverage, the performance of Praj Industries, Pitti Engineering and Welspun Living was below our expectations with weaker-than-anticipated growth in revenues, which in turn impacted the profitability. **Mold-Tek** met our expectations on the revenue front but missed profitability estimates. The performance of Kirloskar Brothers, Va Tech Wabag and Gravita was broadly in line with our expectations or surpassed those in some cases.

- **Praj Industries Ltd.** reported a revenue of Rs 853 Cr, up 3% YoY and 5% QoQ, missing our estimate by 5%. EBITDA was down 39% YoY and 38% QoQ at Rs 59 Cr, as the EBITDA margin declined to 6.9% vs 11.6% in Q3FY24. Order intake during the quarter was Rs 1,053 Cr, compared to Rs 921 Cr in the previous quarter.
- **Mold-tek Packaging Ltd.'s** volumes increased by 7.5%, with overall revenue growth of 15.25%, indicating an improvement in average realisations. EBITDA per kg declined to Rs 36.72 per kg from Rs 39.64 per kg in Q2FY25. PAT stood at Rs 14 Cr, down 4% YoY and 2% QoQ, primarily due to significantly higher depreciation and finance costs associated with investments exceeding Rs 250 Cr made over the past two years.
- **Welspun Living Ltd.** Missed our estimates on all fronts during the quarter as growth in key growth areas slowed down due to weaker-than-expected demand and freight-related challenges. The company reported a revenue of Rs 2,490 Cr, up 3% YoY but down 13% QoQ, missing our estimate of Rs 2,820 Cr by 12%. EBITDA stood at Rs 280 Cr, declining 17% YoY and 22% QoQ, falling short of our estimate of Rs 367 Cr.
- **Kirloskar Brothers Ltd.** Reported a revenue of Rs 1,144 Cr for Q3FY25, up 19% YoY and 10% QoQ, largely in line with our estimate by 3%. The EBITDA stood at Rs 166 Cr, up 34% YoY and 17% QoQ, in line with our estimate of Rs 161 Cr as EBITDA margins improved to 14.5%, expanding by 169 bps YoY and 78 bps QoQ. PAT stood at Rs 114 Cr, up 37% YoY and 19% QoQ, aligning with our estimate of Rs 115 Cr.
- **Pitti Engineering Ltd.'s** Q3 performance was impacted by volatility in the key end market as the revenue marked a 37% YoY increase but a 3% QoQ decline at Rs 415 Cr. EBITDA stood at Rs 67 Cr, up 30% YoY and 1% QoQ, missing our estimate of Rs 75 Cr. PAT came in at Rs 29 Cr, reflecting an 83% YoY growth but a 24% QoQ decline. Notably, the Q3FY25 results included contributions from recently acquired and merged businesses, making direct YoY comparisons less relevant.
- **Va Tech Wabag Ltd.** reported a revenue of Rs 811 Cr, reflecting a substantial 15% YoY growth and a 16% QoQ increase, surpassing our estimate of Rs 760 Cr. EBITDA margin came in at 12.38%, below our estimate of 13.97%. EBITDA stood at Rs 100 Cr, up 2% YoY and 7% QoQ, below our estimate of Rs 106 Cr. This performance resulted in a PAT of Rs 70 Cr, marking a 12% YoY growth, missing our estimate of Rs 74 Cr by 6%. The order intake for the period stood at Rs 2,781 Cr, with the order book at over Rs 14,200 Cr, including framework contracts.
- **Gravita India Ltd.'s** revenue stood at Rs 997 Cr, up 31% YoY and 7% QoQ, primarily in line with our expectations of Rs 967 Cr. Adjusted EBITDA also came largely in line with our estimates, reaching Rs 102 Cr, up 14% YoY and 1% QoQ. The EBITDA margin stood at 10.3%, compared to our estimate of 10.9%, declining by 68 bps QoQ and 157 bps YoY. The company's PAT stood at Rs 78 Cr, up 28% YoY and 9% QoQ, beating our estimate by 15%.

Midcap Opportunities: Outlook

✓ Growth After Short-term Challenges

Most of the companies in our Midcaps coverage primarily cater to industrial customers and are influenced by demand trends in the industries they serve. Q3FY25 performance and management commentary indicate that demand is picking up in certain segments, while the broader outlook remains uncertain. Key factors to monitor going forward include shifts in private capex, domestic infrastructure spending, geopolitical developments affecting trade and logistics, and the imposition of Anti-Dumping Duties/Tariffs in the USA and other key markets.

- **Margins May Remain Under Pressure in the Near-Term**: Pitti Engineering maintained its volume guidance for FY25 and the medium term but acknowledged that its earlier revenue targets may not be met due to price fluctuations in the market. Mold-Tek Packaging also lowered its expectations for improvement in EBITDA/Kg. Similarly, while Welspun Living upheld its revenue growth guidance of 10-12% for FY25, it revised its EBITDA margin guidance downward. Overall, market commentary suggests that pricing pressures may persist in the near term, with margin improvements likely to be more visible from FY26 onward.

- **Long-Term Growth Prospects Intact:** Although some companies lowered their guidance for FY25, most remain confident in achieving their medium to long-term revenue and EBITDA targets. As highlighted earlier, the stocks in our coverage cater to both domestic and international industrial customers and stand to benefit from rising industrial activity. With increased infrastructure allocations and a strong push for domestic manufacturing, we expect midcap stocks in our coverage to perform well over the long term. Additionally, near-term export-related challenges are anticipated to subside over the next few quarters, leading to improved profitability and revenue growth for export-oriented companies.

Top Conviction Ideas: Chemicals

Stock	Reco.	TP*	Recommendation Rationale
Navin Fluorine International Ltd	BUY	Rs. 4,300*	• **Volume and Realizations Lead HPP Growth:** The company's HPP segment recorded another strong quarter with 22% YoY revenue growth, driven by volume growth in HFO, R22, R32, and inorganic salts, along with improved price realisation. The additional R32 capacity of 4,500 metric tons is expected to be commissioned by Feb'25, while the AHF project remains on track for commissioning by early FY26. The demand outlook for R32 remains strong. • **Improving Utilization in Specialty Chemicals:** The specialty chemicals business showed signs of recovery during the quarter, which is in line with the management's commentary from the previous earnings call. The Dahej plant, with a capex outlay of Rs 540 Cr, commenced commercial production in Nov'24, and the first dispatch from Surat is expected in Q4FY25. NFIL remains focused on increasing capacity utilisation and sees strong order visibility in Q4FY25 and beyond. • **Strong visibility in CDMO:** The CDMO business posted 8% YoY revenue growth, with an order book providing clear revenue visibility going forward. The company continues to make progress in the European CDMO business and has received a scale-up order from a major U.S.-based customer. The first phase of the cGMP4 project remains on track for commissioning by Q3FY26. • **Valuation & Recommendation:** NFIL improved revenue visibility during the quarter, with the specialty chemicals segment showing signs of revival while other segments continued to perform well. Well-planned capex and operational discipline are expected to drive future growth and further improve margins. The margin improvement in the current quarter reinforces confidence in achieving or surpassing its EBITDA margin target of around 25%. With ongoing expansion, new molecule launches, and anticipated tie-ups in the CDMO space, the company is well-positioned to deliver strong performance in FY26 and FY27. We value the stock at 30x FY27E EPS, translating into a TP of Rs 4,300/share and recommend a BUY on the stock.

** Note: Target Price is based on our Q3FY25 Result Update Report*

Top Conviction Ideas: Chemicals

Stock	Reco.	TP*	Recommendation Rationale
Dhanuka Agritech Ltd	BUY	Rs. 1,780*	• **New products continue to drive growth:** During the quarter, the company experienced margin expansion on a YoY basis, primarily driven by a favourable product mix and new product introductions, strong sales, and liquidation of key products such as LaNevo and MYCORe Super. Both these products, launched this year, have been well received by farmers across India. Additionally, the company introduced a new 9(4) product, "Roxa" – Pyroxasulfone 85% WG, aimed at controlling weeds in wheat crops, which has garnered a positive market response. Looking ahead, in the next FY, Dhanuka plans to launch two 9(3) products—one for rice herbicides and another new fungicide for grapes and horticultural crops—along with several additional 9(4) products. • **Acquisition of Global rights for 2 Fungicides from Bayer:** The company has secured global rights to the active ingredients Iprovalicarb and Triadimenol (invented by Bayer AG). This acquisition positions Dhanuka to extend its presence in over 20 countries, marking a significant step in its global market expansion strategy. As part of this, Dhanuka plans to shift the manufacturing of at least one of the products to India, leveraging the capabilities of its manufacturing unit at Dahej, Gujarat. The overall market potential for these two molecules has a revenue potential of Rs 250 Cr. By FY27, the contribution from these two products to the top line is projected to be in the range of Rs 175-200 Cr, with a 10-15% CAGR growth thereafter. • **Valuation & Recommendation:** We expect that reduced inventory levels at customers will likely lead to improved pricing and demand for Dhanuka Agritech and other agrochemical players. Additionally, the company's Dahej plant, which currently has a negative EBITDA, is expected to support revenue and margin growth as utilization improves over the next two years. The company's strategy of focusing on introducing new, innovative, high-margin products, supported by its robust on-ground distribution network, has been crucial to its resilient performance. With prices possibly bottoming out, Dhanuka appears well-positioned to deliver a stronger performance. We value the stock at 18x FY27E with a BUY rating and target price of Rs 1,780/share.

****Note: Target Price is based on our Q3FY25 Result Update Report***

Top Conviction Ideas: Midcap Opportunities

Stock	Reco.	TP*	Recommendation Rationale
Kirloskar Brothers Ltd	BUY	Rs 2,100*	• **Robust Revenue Growth and Order Intake:** KBL posted a 19% YoY revenue growth during the quarter, with a 23% increase in the overseas business. Growth in the overseas segment was driven by strong performance in SPP UK and Dutch subsidiaries, while the company has observed traction in SPP US post-elections. KBL also maintains a strong order book of Rs 3,094 Cr (vs Rs 3,057 Cr in Q2FY25), indicating robust revenue visibility in the future. • **Strategic Steps Paying Off:** KBL has been strategically focusing on increasing the share of value-added products while significantly reducing its exposure to low-margin and lumpy EPC orders. Additionally, it has been investing in technological upgrades to enhance operational efficiencies and increase the value of its offerings. These efforts are evidently translating into the company's strong performance, as it has managed to expand margins significantly over the last two quarters. The management expressed confidence in sustaining the margin improvement going forward. • **Valuation & Recommendation:** With sustained demand from key end markets and a robust order book, KBL remains on track to achieve double-digit revenue growth in FY25. The current order book provides strong revenue visibility, and order intake is expected to remain strong going forward. Additionally, the focus on cost optimisation and an improved product mix should support continued margin expansion. We value the stock at 25x FY27E EPS with a target price of Rs 2,100/share and have a BUY rating on the stock.

**** Note: Target Price is based on our Q3FY25 Result Update Report***

Top Conviction Ideas: Midcap Opportunities

Stock	Reco.	TP*	Recommendation Rationale
VA Tech Wabag Ltd	BUY	Rs 1,970*	• **Order Pipeline Strengthening:** The company has secured new orders totalling over Rs 2,781 Cr this quarter, increasing its total order book to around Rs 14,200 Cr (including framework contracts). It also recently won a consortium order worth Rs 3,251 Cr ($371 Mn) for the Al Haer Independent Sewage Treatment Plant in Riyadh, Saudi Arabia. With this, the company is now likely to surpass the order book target of over Rs 16,000 Cr by the end of this fiscal year. • **Margins to improve with revenue growth acceleration:** The recent orders are expected to accelerate revenue growth starting in FY26. Management has guided a 15-20% revenue CAGR over the next three to five years. The sustained revenue growth and improving product mix are • also expected to drive profit margins higher in the medium term. • **Improving Cash Cycle:** The company has now been net cash positive for the eighth consecutive quarter, with a net cash position of Rs 263 Cr as of Q3FY25. It continues to focus on reducing working capital requirements and expects further improvement in the coming quarter. • **Valuation & Recommendation:** VA Tech Wabag Ltd. (VTW) has consistently grown its order book while strategically enhancing its revenue quality and predictability, which aligns with this focus. The company is looking to increase its share of more profitable international, industrial, and O&M contracts. With its current order book providing clear revenue visibility for the next 3-4 years, especially in terms of international orders, these strategic efforts are expected to help the company achieve its targeted margins, further strengthening its financial position and business sustainability. We have a BUY Rating on the stock with a target price of Rs 1,970/share, valuing it at 21x FY27E EPS.

Note: Target Price is based on our Q3FY25 Result Update Report

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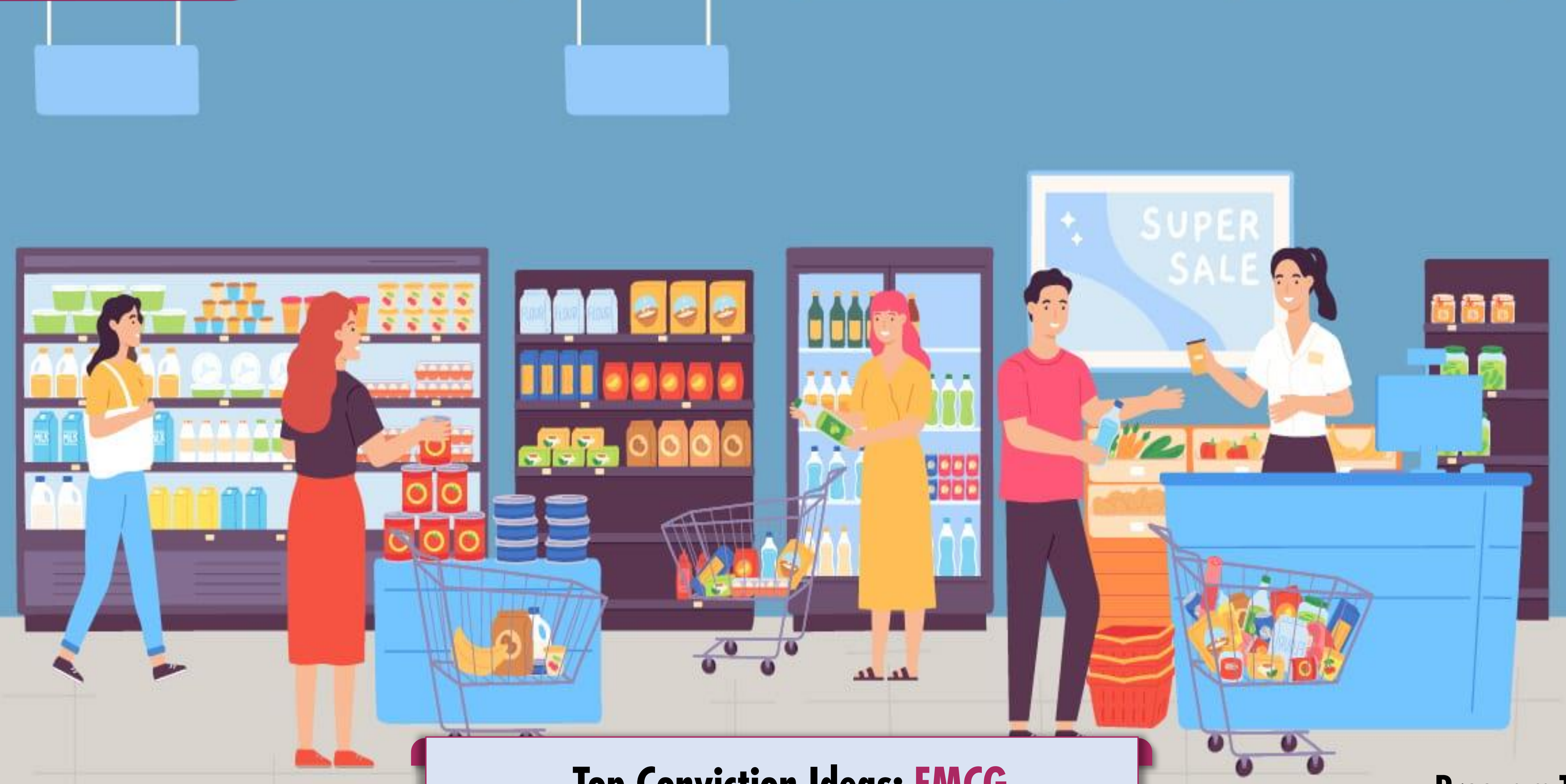

Top Conviction Ideas: FMCG

Preeyam Tolia
Suhanee Shome

FMCG Sector: Q3FY25 Review

Volume Growth Muted as Urban Reels Under Pressure

- **Topline growth remains muted:** Staple companies reported muted topline growth, with low single-digit volume growth, primarily due to weak urban consumer demand. However, rural demand continues to outpace urban demand and remains resilient. Based on management guidance, a meaningful recovery is expected only from Q1FY26.
- **Slowdown in Urban segment:** Urban, which accounts for 50-60% of FMCG sales, came under pressure as highlighted by most consumer companies due to 1) a slowdown in discretionary spending, 2) muted wage growth, 3) higher interest rates coupled with rising rentals and EMIs, and 4) increased competitive intensity from other D2C brands, as Q-commerce penetration has risen recently, leading to overall weakness in urban consumption.
- **Rural demand recovery sustains:** Easing rural inflation (with minimal impact from food inflation), higher government spending, better harvests, and higher MSP are expected to drive rural demand in the coming quarters as well.
- **Gross margin under pressure; EBITDA Margins in ‘Wait & Watch’:** Gross margins across staple companies have been under pressure due to a surge in key raw material prices (such as palm oil and other agri commodities) and higher packaging costs, which have impacted overall margin performance. With subdued volume growth and elevated raw material prices, EBITDA margin expansion is likely to remain constrained in the near term

FMCG Sector: Outlook

How Have Companies Performed In Q3FY25?

- **Demand recovery is likely to be delayed: FMCG companies have reported muted performance due to weakness in the urban market, which is owing to increased competitive intensity and a** subdued demand environment. However, rural recovery continues to grow faster owing to easing inflation, increased government spending, and higher MSP.
- Companies have highlighted that **volume growth (especially in staples) is likely to remain under pressure for the next 1-2 quarters and pick-up expected only from Q1FY26.**
- On the **Gross Margins front**, most companies reported subdued performance due to higher key raw material prices, such as agri commodities.

FMCG Sector: Outlook

What Makes the FMCG Sector a Good Bet?

- **Structural Growth Trajectory:** Indian FMCG companies are on a structural growth path, with several categories like shampoos and premium detergents still under-penetrated and underserved. Increasing rural penetration further strengthens the sector's growth potential.

- **Premiumisation Agenda Driving Overall Growth:** With rising purchasing power, Indian consumers are increasingly opting for premium and branded products. This premiumisation trend is expected to be a key growth driver for the FMCG sector.

- **Best-in-Class Return Ratios (ROCE, ROE):** In a volatile, uncertain, complex, and ambiguous (VUCA) environment, the FMCG sector stands out for delivering best-in-class return ratios such as ROCE, ROE, and dividend yield, ensuring long-term capital protection.

Short & Medium-term Outlook

Short term

Delayed Volume Recovery

Urban slowdown is likely to play spoilsport

Delayed Margin Recovery

Gross and EBITDA margins are likely to remain under pressure owing to subdued top line and increase in RM

Domestic Consumption Play

Better returns in this volatile environment

Rural Demand to Pick Up

Increase in government spending;
Consumer price inflation remains stable

Medium Term

Key Monitorables – Urban Recovery; Margins Trajectory; Competitive Intensity

Top Conviction Ideas

Stock	Reco.	TP*	Recommendation Rationale
Varun Beverages	BUY	Rs 710*	✓ VBL has consistently outperformed its peers in recent quarters despite a volatile environment. ✓ The company is expected to sustain its strong growth momentum, driven by key factors: 1) The strategic acquisition of BevCo, strengthening its presence in South Africa and DRC; 2) Expansion of its snacks portfolio beyond India, particularly in Zimbabwe and Zambia; 3) A continued push to increase distribution reach, especially in rural markets; 4) Commissioning of multiple greenfield and brownfield facilities, enhancing manufacturing capacity, expanding market reach, and optimizing transportation costs; and 5) Scaling up the high-margin Sting energy drink while expanding its value-added dairy, sports drinks (Gatorade), and juice segments. These strategic initiatives are set to drive long-term growth and profitability.

Note: The Target price is based on our Q3FY25 Result Update. We remain positive on the stock's long-term prospects and recommend 'BUY on Dips'.

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Top Conviction Ideas

Stock	Reco.	TP*	Recommendation Rationale
DOMS Industries	BUY	Rs 3080*	**The company has been executing strategic initiatives over the past few years, which are expected to drive growth in the coming years. Key initiatives include:** ✓ 1) Managing end-to-end operations to enhance efficiency while maintaining high-quality standards. The new 44-acre greenfield facility will further accelerate growth. ✓ 2) Expanding beyond the small pencil segment into the larger pens category, broadening the product portfolio. Additionally, entering fast-growing segments such as bags, toys, and diapers will provide an incremental growth boost. ✓ 3) Significant potential for distribution expansion, with DOMS currently reaching 1.35 Lc outlets. The company has the scope to scale up to ~3-3.5 Lc outlets, particularly in the underpenetrated east and south markets and smaller towns in India. ✓ 4) The strategic partnership with FILA will enable DOMS to expand its global footprint while leveraging FILA's R&D capabilities, offering a long-term competitive edge.

Note: The Target price is based on our Q3FY25 Result Update. We remain positive on the stock's long-term prospects and recommend 'BUY on Dips

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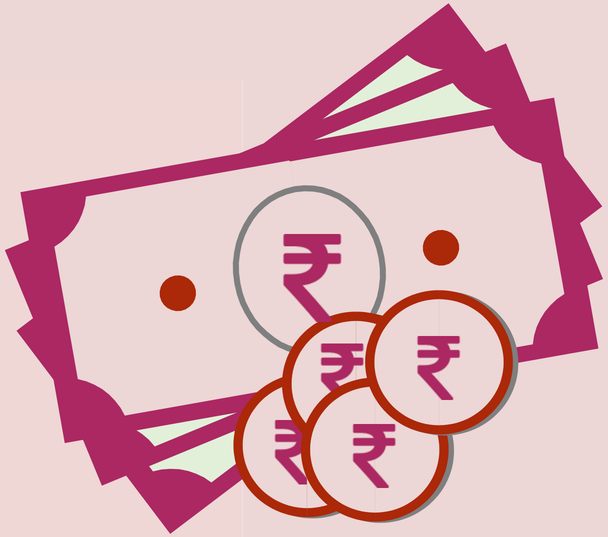

Top Conviction Ideas: Retail

PREEYAM TOLIA
SUHANEE SHOME

Discretionary Under Pressure as Consumer Sentiment Remains Muted

✓ *Financial Performance*

- **Consumer demand remains tepid:** Discretionary demand remains subdued, with a more pronounced impact on QSR and footwear. However, value retailer V-Mart performed relatively better and remains optimistic about future growth.

- **Premium vs. value segment:** While the premium, luxury, and value segments remain strong, urban consumption, footwear, and QSR continue to face pressure.

- **Store expansion continues:** Despite the muted environment, most companies in our coverage have maintained or even increased their store opening guidance as they expand into smaller towns, supported by strong long-term growth levers.

- **EBITDA margins have experienced pressure** due to negative operating leverage resulting from subdued topline performance.

Retail Sector: Outlook

What Makes the Retail Sector a Good Bet?

- **Rapid formalisation undergoing –** The Indian retail market remains largely unorganised, presenting significant opportunities in smaller cities and towns. With rising disposable income, consumers are increasingly shifting towards branded products.

- **Smaller cities provide huge headroom –** Smaller cities and towns are witnessing faster growth than metros across categories such as apparel, QSR, and footwear. This trend is driven by rising aspirations for branded products and increasing disposable income, further supporting overall growth.

- **Structural Story to Continue**
  - ✓ **Higher disposable Income –** India's average per-capita income stands at $2,200, and any increase in income is likely to translate into higher discretionary spending, as per-capita expenditure on essential goods remains largely constant.
  - ✓ **Increased participation of women in the workforce** – Higher disposable income is driving increased sales in the women's wear segment.

Short and Medium-term Outlook

Short term

Demand:

Slowdown in discretionary spends

Margins:

Recovery in margins will be gradual

Medium Term

Domestic Consumption Play:

Likely to deliver better returns in this volatile environment

Rural Demand to Pick Up:

Increase in government spending and urban remittances

Consumer price inflation to start receding eventually

RM prices remain stable

Key Monitorables – Demand recovery; Margins Guidance; Inflation Trajectory; Competitive Intensity

Top Conviction Ideas: Retail

Stock	Reco.	TP	Recommendation Rationale
Trent	BUY	Rs 7,100*	✓ We expect strong sales growth to continue in the coming quarters, supported by Trent's aggressive store expansion and ongoing assortment renewal, which should drive higher footfall. Additionally, improved earnings across all formats, reduced losses at Star Bazaar, and increasing traction at the Inditex JV are positive indicators for the company. ✓ In recent years, Trent has implemented its playbook for the Star business, focusing on private labels, which is proving beneficial and is expected to be a key growth driver. Further, its expansion into the UAE, the launch of Zudio Beauty, and its recent entry into the fast-growing LGD jewellery segment are likely to contribute to long-term growth. ✓ Given these factors, we remain positive on Trent from a mid- to long-term perspective.

Note: The Target price is based on our Q3FY25 Result Update. We remain positive on the stock's long-term prospects and recommend 'BUY on Dips.'

Top Conviction Ideas: Retail

Stock	Reco.	TP	Recommendation Rationale
Ethos	BUY	Rs 3,070*	✓ Ethos's strong and consistent performance over the past several quarters underscores its promising future. Key growth drivers include: 1) Sustained demand in the premium and luxury watch segment, 2) Expansion into the fast-growing CPO segment, 3) Rising contribution from high-margin exclusive brands, 4) Diversification into the luxury luggage and jewellery segments, and 5) Significant potential for margin and ROCE expansion. ✓ With these factors in play, the company is expected to achieve a robust revenue CAGR of 33% and PAT growth of 38% over FY24-27E. At the current CMP, Ethos is trading at 44x/32x its FY26/27E EPS. Given its improving earnings visibility and enhanced return profile, the stock presents an attractive opportunity within the Smallcap space.

Note: The Target price is based on our Q3FY25 Result Update. We remain positive on the stock's long-term prospects and recommend 'BUY on Dips.'

AXIS SECURITIES

February 2025

Top Conviction Ideas: Automobile Industry

Shridhar Kallani
Auto Analyst

Auto Sector: Q3FY25 Review

Q3FY25 Auto OEM Review – Growth in 2W/Tractor OEMs Led by Rural Demand

✓ ***Financial Performance***

- The companies under our coverage reported Revenue/EBITDA/PAT growth of 11% YoY each; revenue was slightly below our estimate of 13% YoY, while EBITDA marginally outperformed our estimate of 10% YoY, and PAT was in line with our estimate of 10.5% YoY. This mixed performance was driven by (1) Revenue growth in 2W OEMs like TVS and Eicher, while Hero and Bajaj recorded flattish revenues; (2) Strong SUV sales growth for Maruti; (3) Commercial vehicles (Ashok Leyland), despite lower volumes, managed to grow revenues due to pricing discipline and higher exports; and (4) Tractors (Escorts), which performed in line with estimates.
- Margin pressures stemmed mainly from operational inefficiencies, higher discounting, and lower domestic wholesale sales volumes. On a QoQ basis, aggregate Revenue/EBITDA/PAT grew by 3%/3%/6%, compared to expectations of ~7%/10%/9% growth. EBITDA margins remained largely flat YoY/QoQ, as the positive impact of product premiumisation and cost control efforts was offset by higher discounting and negative operating leverage.

Q3FY25 Auto Ancillaries Review – Mixed Performance

✓ ***Financial Performance***

- The companies under our coverage reported Revenue/EBITDA/PAT growth of 8.4%/10.5%/12.5% YoY, exceeding expectations of 7%/8.5%/10.5%, respectively. This growth was driven by the premiumisation trend in 2Ws and PVs, stable raw material prices, and cost-control measures across auto ancillaries.
- Sansera Engineering, Endurance Technologies, UNO Minda, and Minda Corp delivered strong YoY EBITDA growth, while Automotive Axles and SSWL remained flat. CIE Automotive saw an 8.6% YoY decline due to lower volumes in its EU business.

Auto Sector: Outlook

Optimistic on 2W Demand Scenario: In 9MFY25, domestic sales volumes for 2Ws and tractors grew 12% and 5% YoY, respectively, while PVs remained flat, and CVs declined by 2% YoY. For FY25E, 2W demand is expected to grow in the early double digits, tractors in the mid-single digits, while PVs and CVs are likely to see flat to low single-digit volume growth.

- **PV:** The domestic PV industry reported flat YoY volumes in Q3FY25, impacted by a high base and subdued demand in select segments. However, the sales mix continues to shift towards SUVs, reflecting strong consumer preference. Over the long term, EV penetration within the PV segment remains a key growth driver, supported by evolving consumer trends and policy incentives.

- **2W:** The 2W segment grew 3% YoY in Q3FY25, driven by a recovery in rural demand and continued premiumization trends. During the quarter, the 125-150 cc motorcycle and scooter segments posted robust growth of 22% and 14% YoY, respectively.

- **CV:** The domestic MHCV segment recorded a 1% YoY decline in Q3FY25, while LCV volumes grew 3%. The medium-term growth outlook remains positive, supported by anticipated infrastructure spending in the Union Budget for FY26 and government initiatives to boost the rural economy. Additionally, replacement demand and the vehicle scrappage policy are expected to aid the segment further.

- **Tractors:** The tractor industry showed early signs of recovery, with improved rural demand supported by expectations of a favourable MSP. The segment is expected to benefit from increased government spending in the rural economy from FY26 onward.

- **3W:** Three-wheeler volumes remained flat YoY in Q3FY25 due to a high base, with demand driven by urban market recovery and expanding last-mile delivery applications, supported by a rising preference for electric variants.

- **EV (as per Vahaan):** EV two-wheeler volumes surged 76% YoY in Q3FY25 but remained flat QoQ, driven by growing consumer preference for sustainability, supportive government policies, and expanding EV infrastructure. EV penetration across other segments, including PVs and LCVs, continues to gain traction.

Outlook – Cautiously Positive

Stable Margin Outlook

- We expect EBITDA margins to remain broadly stable in the near term, supported by a richer product mix. However, raw material headwinds and negative operating leverage, driven by the high base, could exert slight pressure. The price benefits realised in previous quarters for some companies may limit further margin expansion.

Because of near-term growth challenges, we maintain a cautiously positive outlook on the domestic industry, with a gradual recovery in exports. Against this backdrop, we recommend a “Buy on Dips” strategy for quality stocks.

- We expect 2W sales volumes to sustain high single-digit growth in FY26E, supported by new premium segment launches, an extended replacement cycle, and a potential recovery in exports. A favorable monsoon and increased rural spending are likely to drive demand for entry-level motorcycles further.
- PV sales will be led by strong UV launches; however, overall growth is expected to remain in the low single digits in FY26E due to the high base of FY25E.
- In 9MFY25, domestic CV volumes declined YoY, but pent-up demand is expected in the near term. OEMs remain optimistic about long-term structural growth drivers, including India’s vast road network, policy measures aimed at reducing supply chain costs, the Vehicle Scrappage policy, and continued infrastructure Capex outlined in the Union Budget.
- Tractor volumes are expected to grow in the mid-single digits in FY26E, supported by a favorable monsoon and increased government allocations towards the farming sector.
- We remain selective in our approach. Among OEMs under our coverage, our Top Conviction Idea in 2Ws is **Hero Motocorp,** in CVs is **Ashok Leyland**, and in the PV/tractor segment, we favor **Mahindra & Mahindra** (non-coverage), given its strong SUV product portfolio and leadership position in the domestic tractor industry.

Auto Ancillaries

- In the long run, product premiumisation, strong order books, growing exports, and the shift toward EVs are expected to drive higher content per vehicle, boosting profitability. Our top conviction picks in the ancillary space remain **Uno Minda and Sansera Engineering Ltd. We also suggest a "Buy on Dips" approach for CIE Automotive, Endurance Technologies, and Minda Corporation for long-term gains.**

Short & Medium-Term Outlook

Short to Medium term

Gradual recovery in CV/Tractor expected

2W Demand – Shift towards e-2Ws, Premium scooters and Rural recovery

Premiumisation across segments to drive ASPs higher

Export-focused companies to benefit

Increasing share of EV/Hybrids/CNG in the fuel mix

Entry-level PV may see flattish volume on a YoY basis

Increased competition in the SUV space in PV

Entry of Global Players in The EV may broaden Industry growth but increase competition for OEMs

Long-Term

Key monitorables – *Rural Recovery; Pick-up in Exports*

Top Conviction Ideas: Auto

Stock	Reco.	TP	Recommendation Rationale
Hero Motocorp Ltd	BUY	Rs 5,285*	✓ **Long-term Growth Strategy:** Hero MotoCorp's 2030 strategy revolves around four key growth pillars: strengthening its core business, excelling in the premium segment, leading in EVs, and diversifying revenue streams. Guided by the 4S mantra—speed, scale, synergy, and simplification—the strategy also emphasises building a future-ready organisation and advancing ESG initiatives. As part of its portfolio reshaping, the company launched four new models at Bharat Mobility, reinforcing its position for long-term growth. ✓ **New Product Launches:** Product launches in premium scooters and EVs will drive growth, with new models set for Q4FY25 and FY26. The company is expanding its sub-Rs 1 Lc EV lineup with the Vida V2 platform, strengthening its presence in the mass-market scooter segment. New premium motorcycles like the Xpulse 210 and Xtreme 250R have received strong market feedback, while upcoming models, including the Xoom 125, Xoom 160, and Destini 125, will further enhance Hero's scooter portfolio. ✓ **EBITDA Margins:** Hero achieved EBITDA of over Rs 10,000 per vehicle, driven by a richer product mix and strategic pricing. The ICE segment's EBITDA margin stood at 16%, down 50 bps QoQ, mainly due to higher marketing and advertising expenses during the festive season. The company aims to sustain overall EBITDA margins in the 14-16% range in the medium term, supported by a stronger product mix—EVs and higher cc motorcycles, ongoing product premiumisation, lower material costs, and improved operational efficiencies, particularly in the EV segment.

*** Note: Target Price is based on our Q3FY25 Result Update Report***

Top Conviction Ideas: Auto Ancillaries

Stock	Reco.	TP	Recommendation Rationale
Ashok Leyland	BUY	Rs 245*	✓ **Company Growth Outlook:** Ashok Leyland is progressing toward its medium-term goals, including mid-teen EBITDA margins, 35% MHCV market share, expansion in non-MHCV segments, leadership in alternate fuels, and value unlocking from subsidiaries. The company is witnessing growth in tippers and multi-axle products, backed by a strong order book for electric vehicles under Switch. Non-CV businesses, including engines and spare parts, have grown 3.5% and 14% YoY, respectively. ✓ **Export Outlook:** Exports continue to be a key growth driver, with Q3FY25 export volumes rising 33% YoY. FY25 export volumes are expected to reach 15,000 units, up from 11,800 in FY24, keeping the company on track to achieve its medium-term target of 25,000 units. The long-term goal is set at 50,000 units annually, driven by localisation efforts and improving market conditions in GCC, SAARC, and Africa. Investments in assembly facilities and local operations have further strengthened its presence in these key regions. ✓ **Healthy EBITDA Margins:** Q3FY25 EBITDA came in at Rs 1,211 Cr, with margins improving to 12.8% (up 77 bps YoY). The expansion was driven by cost-reduction initiatives (~Rs 650 Cr annually), a stronger product mix with a higher share of tippers and multi-axle trucks, and relatively stable commodity prices. Going forward, continued premiumisation, operational efficiencies, and growth in high-margin non-CV businesses should further support EBITDA margins, keeping the company on track toward its mid-teen margin target.

Note: Target Price is based on our Q3FY25 Result Update Report

Top Conviction Ideas: Auto Ancillaries

Stock	Reco.	TP	Recommendation Rationale
Uno Minda	BUY	Rs 1,140*	✓ **Operational Highlights in Q3FY25:** (1) Uno Minda began commercial production at an advanced manufacturing facility at Khed city for 4W Lighting commissioned in Q3FY25. (2) NCLT approves the merger of Minda Kosei, Kosei Minda, and Kosei Minda Mould into Uno Minda Ltd. (3) The company's board approved Capex for expansion of the Casting facility at Hosur from 11kMT per annum to 15kMT per annum. ✓ **Robust Growth Across All Verticals:** UnoMinda's outperformance across all segments can be witnessed, led predominantly by the Lightning, Switches, Casting, and Other divisions (sensors, motors-controllers), which grew 15%/13%/12%/60% YoY, respectively, in Q3FY25. ✓ **EV Capabilities:** Sales of 2W EVs rose to Rs 238 Cr in Q3FY25, compared to Rs 164 Cr in Q3FY24, driven mainly by higher volumes of sensors and controllers. The potential EV kit value is estimated at Rs 35k, with Rs 27k currently in commercial production.

*** Note: Target Price is based on our Q3FY25 Result Update Report***

Top Conviction Ideas: Auto

Stock	Reco.	TP	Recommendation Rationale
Sansera Engineering	BUY	Rs 1,430*	✓ **Robust Order Book:** Sansera has a strong order book with annual peak revenues of Rs 2,201 Cr, 55% of which come from the Non-Auto, Auto Tech Agnostic, and EV segments. Its non-automotive business is seeing robust growth, with a total order book of Rs 600 Cr across semiconductors, EMS, aerospace, and defence. The company expects to execute 50% of its non-automotive order book by FY26, supported by increased activity in semiconductor and defence projects. ✓ **Strong Financials to Support Growth:** In Q3FY25, Sansera raised Rs 1,200 Cr through a QIP to support its strong order book and expansion plans. Of this, Rs 700 Cr was used to retire debt, bringing the gross debt down to Rs 350 Cr as of December 2024. The company allocated Rs 200 Cr for capex, Rs 100 Cr for land acquisition, and Rs 100 Cr for advanced manufacturing equipment. The remaining Rs 300 Cr includes Rs 25 Cr for QIP-related expenses, while the allocation of Rs 275 Cr will be finalised in the coming weeks, focusing on growth capex and other developmental initiatives. ✓ **EBITDA Margins:** The company is expected to achieve margins of 17-18% in FY25/26/27E, with EBITDA and PAT projected to grow at approximately 15% and 22% CAGR over FY24-27E. This growth will be driven by a shift in the sales mix toward non-Auto ICE components, higher capacity utilisation, expansion in exports, volume growth, and a recovery in Swedish operations.

*** Note: Target Price is based on our Q3FY25 Result Update Report***

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