NASSCOM

Mr. Achyuta Ghosh
Head Research, NASSCOM

NASSCOM, a trade association, is the apex body for the USD180b IT BPM industry in India, an industry that has made phenomenal contribution to India's GDP, exports, employment, infrastructure and global visibility. In India, the IT BPM industry provides the highest employment in the private sector.

IT industry to emerge stronger from COVID-19

Digital to see accelerated traction over medium term

In our first edition of Motilal Oswal Virtual Conference Series – Opportunities and Challenges in the COVID-19 Era, we hosted a call with Mr. Achyuta Ghosh, Head of Research at NASSCOM. Mr. Ghosh shed much light on the current IT industry and the need for changes in the future. Key insights highlighted below:

- **Government could become biggest technology spender:** Trade wars and new caveats are expected as the current supply chains have got disrupted. Mr. Ghosh expects the government to become the biggest technology spender as technology has played a vital role during the current COVID-19 pandemic. He further expects offices to adopt the work from home (WFH) model for a significant share of employees even after the pandemic ends.
- **Disruption in Tech spending:** While hardware and tech consulting services would be greatly affected, NASSCOM expects software and tech outsourcing to see relatively less impact. Among verticals, Travel, Retail and Hospitality are expected to be the worst hit while Industrial Manufacturing and Telecom should see medium impact. Mr. Ghosh expects Healthcare, Ecommerce and Technology to see low/positive impact due to the ongoing situation.
- **Learnings from 2009:** Historical data suggests that IT spending growth lagged GDP growth in FY09 and FY10 but picked up FY11 onwards. Further, Indian IT export growth reported a spike in FY11 (18.5% v/s 5.9% in FY10). Mr. Ghosh suggests that these trends can be expected in the current situation as well.
- Post the global financial crisis (GFC) the IT industry saw a rise in fixed price (FP) projects and local hirings, which led to an increase in onsite revenues. Utilizations across companies improved meaningfully (from 70% to 85%). While Telecom/Hi-tech slowed down, Retail and Healthcare picked up. Also, small and medium businesses (SMB) as a customer segment picked up. Thus, it may be interesting to see if any such structural shifts play out post the COVID-19 pandemic too, he concurs.
- **Imperatives for Indian IT:** Indian IT players have demonstrated immense speed and flexibility in enabling WFH for ~90% employees in 4 weeks time. But, it is imperative for Indian IT companies to manage pricing, stay in the game and remain close to clients by providing solutions and co-investing. Mr. Ghosh believes that the industry should get ready for the new normal, which involves uncertainty, agility, emergence of new technologies and increased governance.
- **NASSCOM's 5 point Government Stimulus agenda:**

1. 1-year extension of SEZ/SEIS schemes to maintain export competitiveness.
2. Salary support to employees and access to working capital for SMEs.
3. Measures for cost optimization via GST exemptions and PF/ESI opt-out options.
4. Extend WFH policy till Jul'20 with cross utilization of assets and locations.
5. Accelerate funding for start-ups as ~90% are undergoing revenue losses and ~70% have a runway of less than three months.

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Valuation and view

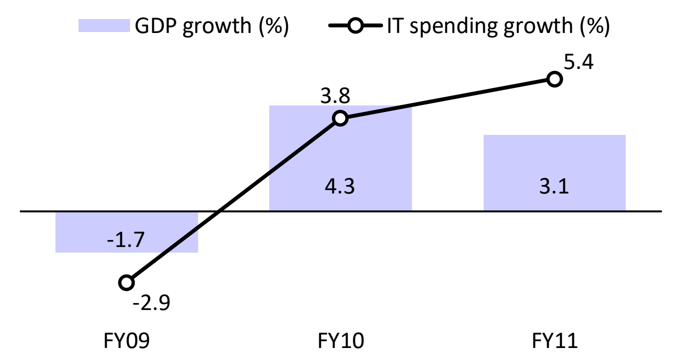
Despite the uncertainty in the environment, we continue to prefer TCS, Infosys and HCLT among the large-caps and Mindtree, LTI and Persistent among Tier-II companies. This is attributable to their historical track record of adapting to multiple business challenges/technology change cycles. Moreover, recent results/commentaries offer us some comfort on the new business wins, ramp-ups, cost optimization and margin management capabilities of these companies.

Exhibit 1: Massive disruption in tech spending to create new tech opportunities

Current Priority Tech	Current Priority Tech Application Areas	Future Tech Areas
Cloud	Smart Cities	Quantum computing
Cyber security	Electric & Autonomous	6G
Analytics	E-commerce	Hyperloop
Artifical Intelligence	Virtual Gaming and eSports	Space tourism
Internet of Things	Connectivity	3D bioprinting
5G	Agritech	Floating farms
Data centers	Edutech	Nano technology
Immersive Media	Healthtech	Edge computing
Robotics & Automation	Data Platforms	Behavioural biometrics
Blockchain	Smart manufacturing	Natural language generation
	Security and Insurance	Robotics-as-a-Service

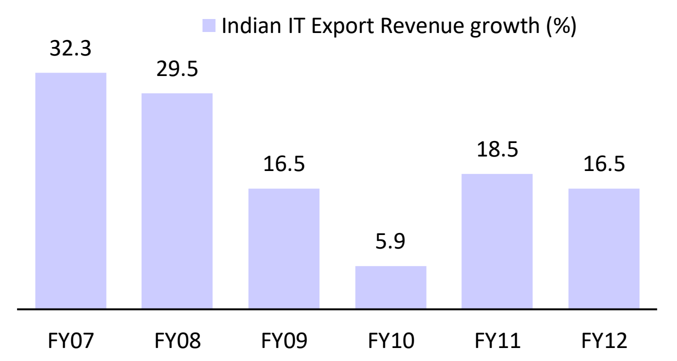
Source: NASSCOM, MOFSL

Exhibit 2: IT spending growth lagged but picked up in FY11…



Source: NASSCOM, MOFSL

Exhibit 3: …together with a spike in export revenue growth



Source: NASSCOM, MOFSL

Mr. Ashok Khanna
Former Group Head,
Vehicle Finance, HDFC Bank

Mr. Ashok Khanna is a veteran with over 40 years of direct/indirect experience in the auto industry. He has worked with auto OEMs such as Toyota and Kinetic Honda. Over the last 21 years, he has been associated with vehicle finance in the banking business.

Recovery to take at least 6-12 months

Dealers stressed; Delinquencies increasing for financiers

In our second edition of Motilal Oswal Virtual Conference Series – Opportunities and Challenges in the COVID-19 Era, we hosted a call with Mr. Ashok Khanna, former Group Head – Vehicle Loans, HDFC Bank. Mr. Khanna shared his views on the expected growth in various segments, delinquencies and impact of the proposed scrappage policy.

- **Recovery in 2Ws/PVs 6-12 months away; M&HCV recovery to be further prolonged:** Recovery in 2Ws could be delayed due to increased cost of ownership post BS6. In PVs, premium cars should see faster recovery (3-4 months) while used cars could see better demand. **Rural and semi-urban markets are expected to be relatively better placed.** M&HCV recovery could get further prolonged due to lower capacity utilization. Even before the Covid-19 outbreak, ~35% of trucks remained unutilized. Mr. Khanna expects t**ractor recovery to be the fastest on the back of rural economy revival, but the same would also depend on rainfall.**
- **Delinquencies to rise meaningfully; Credit underwriting to be tightened:** Due to lack of freight demand as well as acute driver shortage, fleet utilization in the CV segment has been minimal. **Cheque bounce rates in this segment could be as high as 45-50% (compared to 30-40% in PVs/2Ws).** More importantly, **losses given the default (LGD) could widen** as compared to historical run-rate levels, leading to higher eventual credit losses for financiers. Given this backdrop, financiers are likely to take a cautious stance on lending, resulting in **lower LTVs (75-80% going forward v/s 85-90% currently). Also, the space vacated by NBFCs would not necessarily be taken up by banks.** Captive financiers (who had 3-4% dealer pay-outs) are likely to face challenges; they would have to re-examine policies and tweak accordingly.
- **Auto dealers stressed:** Over the past three years, over 200 dealers (across spectrum) have shut shop in India. Dealers are facing several challenges that are affecting margins such as high product fatigue, inventory and discounts, thus impacting inventory clearance. Also, rapid expansion, renovation and reckless financing resulted in over-leveraging of dealers, which in turn, has affected dealer viability. For long-term sustainability, dealers need to cut cost and manage inventory better (possibly have just in-time inventory management at dealer's end).
- **Recovery to be divergent across customer profile/geography: The driver-cum-operator segment would be the fastest to recover while the Small Road Transport Operator (SRTO) segment would remain stressed.** Large fleet operators would have to incentivize drivers to return from villages. Given the lower impact of COVID-19 in rural and semi-urban areas, recovery for automobiles in these geographies is likely to be faster than that in urban areas.
- **Widening the scope of PSL assets could spur lending:** According to Mr. Khanna, lending to the auto sector could be given an impetus if more products are included in it. For example, if 2Ws and small-ticket cars (under INR0.6m) are included in the PSL basket, it would help improve credit flow to the sector. In

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addition, Mr. Khanna believes that GST on 2Ws should be reduced to 15% as 2W buyers have a different profile compared to car buyers. Also, road tax by the state governments should be uniform and brought down.

- **Scrappage policy to be a key positive:** Scrappage policy should be a relief to the auto sector as it would spur new vehicle demand. At the same time, it would reduce cost of production due to recycling of materials like steel and plastic.
- **Moratorium rates to vary across financiers:** According to Mr. Khanna, prudent financiers would witness 15-17% of their car finance customers avail moratorium, while for others, the number could be as high as 30-35%. He expects extension in the moratorium on EMIs to be extended further.

Mr Pradeep Singhal,
Chairman, AITWA

Mr Mahendra Arya,
National President, AITWA

Mr Abhishek Gupta,
Joint General Secretary, AITWA

All India Transporters Welfare Association (AITWA) represents nearly 65% of the organized road transport business in India.

Transportation industry limping back slowly

Freight and driver availability remain key to recovery

In our second edition of the Motilal Oswal Virtual Conference Series, *Opportunities and Challenges in the COVID-19 Era*, we hosted an interaction with Mr Pradeep Singhal, Chairman of the All India Transporter Welfare Association (AITWA), to shed light on the current supply chain situation, along with other factors such as transporters' viability, drivers' availability, and risk of default. Here are the key highlights:

- Of the total 8m commercial vehicles (CVs) in India, 130–140k trucks ply on the national highway. Currently, the country is reporting just 25–30% of normal freight movement.
- While the movement of goods is improving sequentially, it is still substantially weak. Based on e-way bills data, the average daily e-way bills in May (up to 4th May)/April/March stood at 261k/284k/1350k per day, against over 1700k e-way bills per day in the pre-COVID-19 era.
- **Driver shortage**: This is currently a concern; AITWA expects them to be back four to six weeks after the lockdown is lifted (assuming the pandemic is under control by then).
- **Revival only in essential goods industry**: The Pharma and FMCG supply chain has recovered as these industries were on the essential goods list; movement has also been witnessed in Agriculture. Metals and Capital Goods are also seeing some movement as unfulfilled orders are finally being transported.
- **Freight increased by 10–25%, but does not add to profit:** This is due to most trucks having to return with empty loads and the higher compensation being given to drivers. Freight rates are currently at optimal levels as freight moves in tandem with the demand and supply equation; however, both supply and demand are currently running low.
- **Truck operator viability is in bad shape:** 70% of truck operators are single-/small-fleet operators, and for most of them, their trucks are the only source of income. Over 50% of these operators are expected to default on their EMIs in the absence of any relief package.
- **Used CV market**: Used CV would not see any demand due to a high unutilized fleet capacity (35% in the pre-COVID-19 era), and freight demand is expected to fall ~30% in FY21.
- FTL (Full Truck Load) shipping is still managing to operate for essential goods, but LTL (Less than Truck Load) shipping is facing a challenge in terms of viability due to the lack of warehousing as warehouses are either closed, at full capacity, or short of man power.
- **Scrappage policy**: This policy would help modernize the fleet, but it would be viable only if the price is not raised. Currently, all trucks with a national permit are less than 15 years old.

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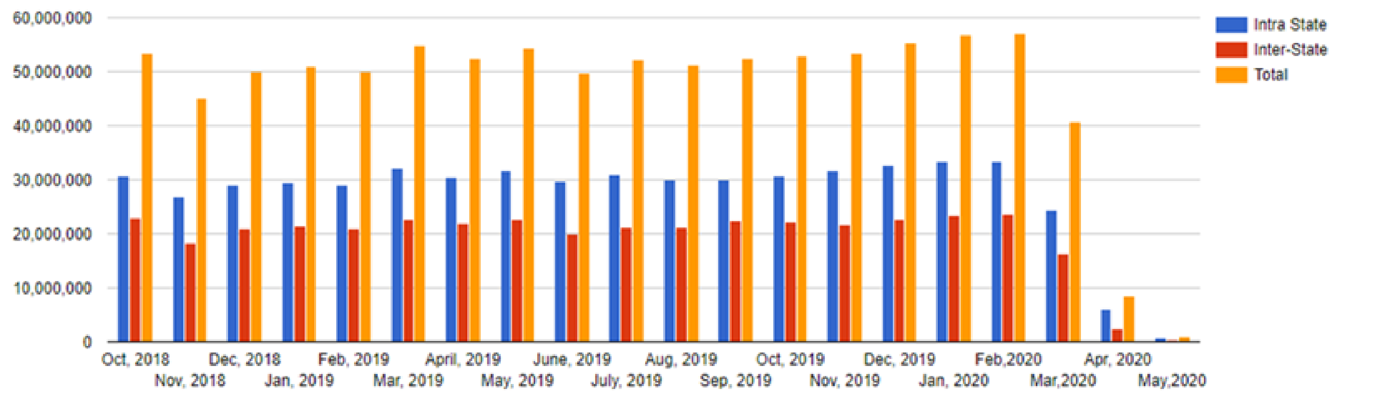
- **Competition from Indian Railways**: The new plan by the Indian Railways to move parcels could take away some of the business of road transporters; however, it is not likely to have a high impact as railways usually do not have much spare capacity after bulk bookings.
- **The Dedicated Freight Corridor**: This would impact the industry, mostly long-route trucks. For example, a 30k trailer that plies on the Western Corridor would be affected.

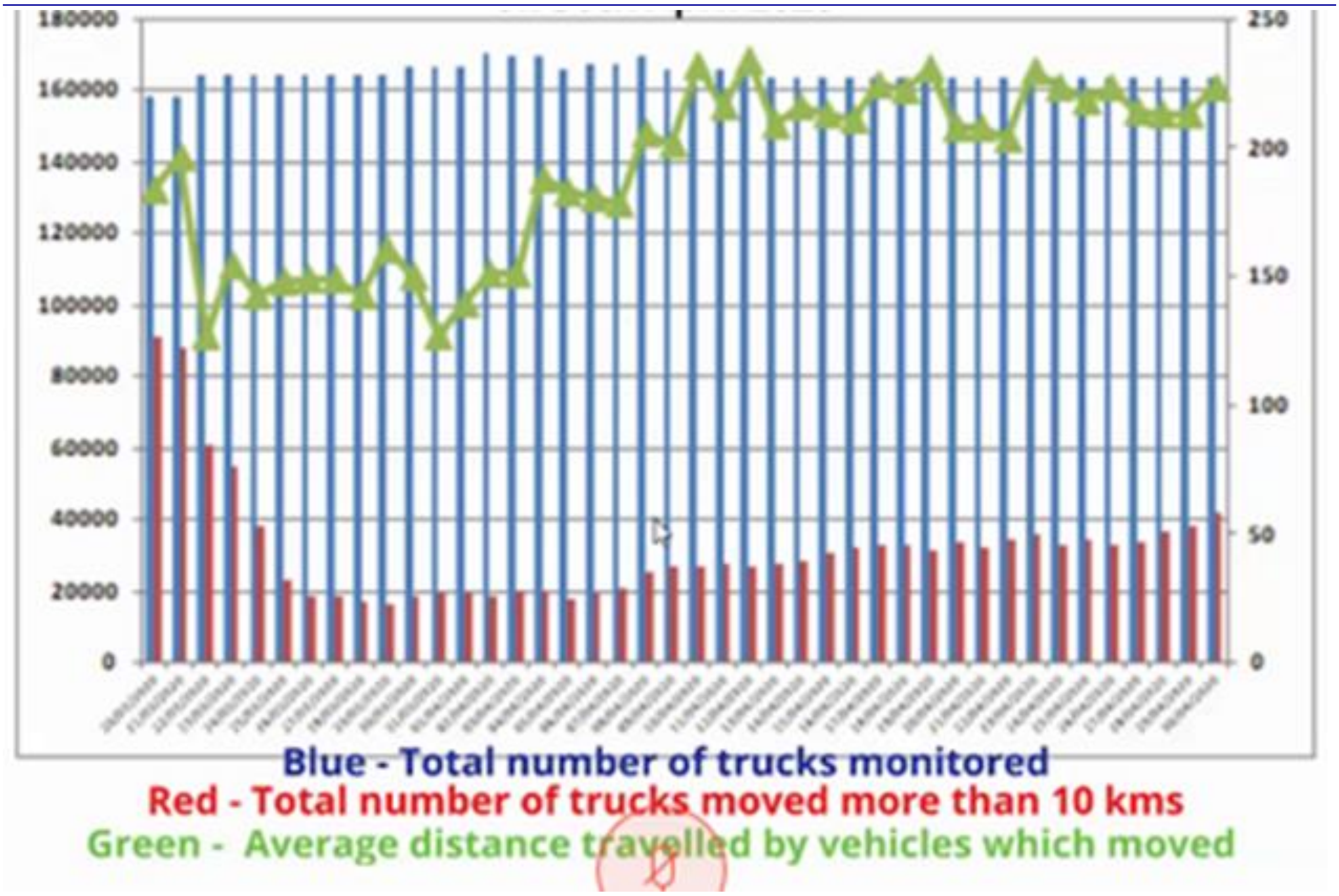
Story in charts

Exhibit 4: Number of e-way bills generated



Source: Company, MOFSL

Exhibit 5: Truck movement analysis through multiple sets of data sourced as of 30th April 2020



Source: Company, MOFSL

NOTES

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BUY	>=15%
SELL	< - 10%
NEUTRAL	> - 10 % to 15%
UNDER REVIEW	Rating may undergo a change
NOT RATED	We have forward looking estimates for the stock but we refrain from assigning recommendation

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