5th August 2020 CMP –₹300.9/- View –**POSITIVE**

Company Background and Business Model

Mahindra Logistics (MAHLOG) is one of India's largest third-party logistics (3PL) solutions providers with an asset-light model. It has two business segments – Supply Chain Management (SCM) and Enterprise Mobility (EM) – that contribute ~90% and ~10% respectively to its revenue. It has developed a scalable and flexible business model with a large network of business partners. With its technological expertise, client relationships, and the Mahindra Group's strategic support, MAHLOG should be a major beneficiary of a pick-up in India's 3PL market.

Important Statistics

M.Cap (₹bn)	₹215.4
52 Week H/L (₹)	458 /199
NSE Code	MAHLOG
BSE Code	540768

Investment Argument

- **Technology driven asset light business model –** Its business model is quite differentiated, with a focus on technology and supply-chain solutions rather than pure transportation. It outsources transportation requirements from business partners (~1,450 in SCM and ~350 in EM) and its warehousing space is leased. Such an asset-light business model allows flexibility and scalability in its operations and high capital efficiency. Its focus is on logistics solutions, managing customers' inbound, outbound, and in-factory logistics, and warehousing. MAHLOG has invested in developing a technology platform that reduces customers' idle time and optimizes vehicle planning and warehousing requirements. It has developed expertise in integrated end-to-end solutions for diverse customers through its 24 offices, 350 operating locations, and 35 network hubs, and pan-India business partners.
- **3PL likely to grow much faster in post COVID –** 3PL has gained wide acceptance in developed countries and is evolving in India post GST. The Indian logistics industry's CAGR is likely to be ~10% to touch ~₹28.1tn over FY21-25, post covid-19. The Indian 3PL market should grow to ₹1.05tn in FY25 from ₹580bn in FY20, a CAGR of 13%. Short-term growth will be lower due to COVID-19, after which the 3PL market should grow by 17-18% annually. Sectors such as pharma, e-commerce, consumer goods, organized retail, and engineering have high 3PL growth potential of 15-25%, while auto should recover from a low base. Indian logistics is seeing a structural change after GST, e-way bill, and infrastructure status to the industry. Supply-chain operations are shifting from small unorganised players to large pan-India players, who are integrating with the global supply chains for imports and exports.
- **Enterprise mobility impacted due to COVID-19; Customers acquisition remains strong –** MAHLOG provides technology-enabled people-transportation services under the brand "Alyte" to ~100+ domestic and MNC companies, operating mainly in IT, ITeS, business process outsourcing, financial services, and consulting segments. This business is also asset light, and focuses on small vehicles provided by c.350 business partners across 12 cities. The COVID-19 pandemic and social distancing norms, along with increased culture of work from home, is likely to impact the EM business in the short term. Being a B2B company, MAHLOG was significantly affected by the stoppage of work at the end customers during Apr'20, with a gradual recovery in May'20 and ramp up in Jun'20. Cross border logistics was affected initially but started gradually. However, the current uncertainty in trade relation is expected to affect international

Financials

(₹ mn)

Particulars	FY18	FY19	FY20
Revenue	34,161	38,513	34,711
EBITDA	1,256	1,502	1,597
EBITDA Margin (%)	*3.7*	*3.9*	*4.6*
Net Profit	653	856	551
EPS (₹)	8.8	12.0	7.7
RoNW (%)	16.2	18.7	10.6
RoCE (%)	25.5	18.0	12.2

freight forwarding in the near to medium term. There has been an improvement in driver and labour availability. Its warehousing services were back to 80% of the pre-COVID utilization levels. Customer acquisition was strong during the second half of the quarter. It invested in secured inbound transportation with a leading steel company. It also won the contract for inbound transportation for the country's largest manufacturer of decorative and automotive glass. It continued to expand both with existing and new customers in FMCG and personal care. It continues to expand in cross border solution base which is reflected in its freight forwarding business. It went live for one of India's largest engine manufacturer, large international elevator manufacturer, leading fuel system manufacturer Overall, the company has significantly improved from by the end of the quarter.

- **MoM improvement during Q1FY21 –** Consolidated net revenue declined 54% YoY to ₹4,105mn on account of 51.0% YoY decline in Supply Chain Management (SCM) revenue and a decline of 81.9% YoY in Enterprise Mobility (EM). The revenues were affected by the COVID-19 led lockdown during Apr'20. However,the company witnessed improvement in revenue run-rate MoM with Jun'20 exit at around 80% of normal revenue run-rate. It also witnessed improvement in driver and labourer availability. The company also continued acquisition of new customers and expansion of its services for both new and existing customers. The SCM revenue of Mahindra group declined by 65% YoY on account of continued weakness in the automobile sector along with a disruption caused by COVID-19 pandemic during the quarter. The revenue from non-Mahindra group SCM declined by 28.8% YoY which too was affected by dip in auto revenues (down 56.3% YoY) and COVID-19 led disruption. Despite, the steep decline in revenues, the company was able to maintain its gross margins YoY at 9.7% (although down 66 bps QoQ) due to a higher share of warehousing revenue. However, lower absorption of fixed costs due to dip in revenue led to operating loss of ₹22mn versus operating profit of ₹401mn in Q1FY20. Higher depreciation (up 23.9% YoY) and higher interest expense (up 28.2% YoY) led to a consolidated net loss of ₹158mn versus net profit of ₹186mn in Q1FY20 It had been able to shrink its working capital requirement by ₹1,000mn leading to net cash and cash equivalent of ₹1,880mn at the end of Q1FY21. The company expects the post COVID era to be favorable for 3PL industry with smarter supply chain demands from the customers along with formalization of the industry. Auto sector has been affected by COVID-19 also by supply and demand disruption both domestically and internationally. The farm sector has been performing well on account of better rural demand, good monsoon and long term government initiatives for the sector. The strong improvement in auto volumes during FY22 is further expected to aid in driving growth for the company Manufacturing and engineering were impacted during first half of the quarter but are returning to normal by June. E-commerce witnessed strong tailwind as online shopping and delivery increased which is also expected to result in better demand for warehousing, fulfillment, express logistics etc. FMCG, personal care and pharma has seen improvement operating through lockdown. FMCG and retail sectors were affected on volume terms and will have to redesign their supply chain. The company added 0.25msf warehousing space under management in Q1FY21 and expects to add another 1mn sq.ft during rest of 9MFY21.

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- **Business Risks –**
  - MAHLOG takes the services from its business partners and passes on its cost to the customers. There could be short term impact on financial performance due to mismatch of timing of contract renewal or negotiation with business partners and customers.
  - Revenue is still focused on the auto segment with ~65% share in SCM; medium-term growth will largely depend on this segment.
  - Outsourcing model means there is limited control on quality of service.
  - Spot hiring to manage seasonal demand could result in higher costs. In certain circumstances, hiring vehicles on an ad-hoc basis would be necessary, and such third-party vehicles could significantly increase operational cost, which could adversely affect margins.
  - In addition, availability of third-party vehicles may be uncertain during periods of high demand. MAHLOG does not have control over the servicing and maintenance of these vehicles.
  - MAHLOG operates in a highly competitive industry, dominated by a large number of unorganized players. The transportation segment is commoditized, and has low barriers to entry or exit, leading to a market with a very high degree of fragmentation.
  - Technological disruptions with many digital platforms for transportation can dilute MAHLOG's value proposition.
  - MAHLOG is focusing on aggressive growth in freight forwarding, which could lead to higher growth in revenue. However, the business is asset light with lower margins of 1.2-2.0%.

Outlook

MHALOG has seen strong improvement since May'20 and has been able to secure its gross margins. FY20 revenue was hurt by weakness in the auto sector (~65% of SCM revenue) with transition to BS-VI norms and COVID-19. In the post COVID era, we expect it to benefit from an increasing reliance of customers on smart supply chain providers like itself. **The auto sector is gradually improving and is likely to see a strong bounce in FY22. The company is aggressively expanding its non-Mahindra clients in SCM; this segment saw 40% revenue CAGR to ₹13.6bn over FY15-19, contributing 40% of total SCM revenue. Also, other sectors like Pharma, FMCG, E-commerce are likely to see growth post COVID also. It is on the right path of improving its earnings growth trajectory going ahead. Hence we view it as a value *BUY* with target range ₹ 340-350 at P/E of 38.8x FY20.**

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Key Performance Parameters

(₹mn)

Particulars	Q1FY21	Q1FY20	% Change	Q4FY20	% Change
Net revenues	4,105	8,990	(54.3)	8,118	(49.4)
Gross margin	398	873	(54.4)	841	(52.7)
Gross Margin (%)	9.7	9.7		10.4	
EBITDA	6.0	471	(98.7)	411	(98.5)
EBITDA Margin (%)	0.2	5.2		5.1	
Net profit	-166	186	(189.2)	104	(259.6)
Diluted EPS (₹)	-2.2	2.6		1.4	

Source: Company Filing

Mahindra SCM Revenue breakup

(₹ mn)

SCM Revenue breakup	Q1FY21	Q1FY20	YoY (%)
Mahindra	1,721	4,912	(65.0)
Non-Mahindra	2,205	3,098	(28.8)
Total	**3,926**	**8,010**	**(51.0)**

(₹ mn)

SCM Revenue by Service breakup	Q1FY21	Q1FY20	YoY (%)
Transportation	2,722	6,610	(58.8)
Warehousing & VAS	1,204	1,400	(14.0)
Total	**3,926**	**8,010**	**(51.0)**

(₹ mn)

SCM Revenue by Industry breakup	Q1FY21	Q1FY20	YoY (%)
Auto	2,075	5,650	(63.3)
Non-Auto	1,851	2,360	(21.6)
Total	**3,926**	**8,010**	**(51.0)**

Non-Mahindra SCM Revenue breakup

SCM Non-Mahindra Service Wise Break-up (%)	Q1FY21	Q1FY20
Warehousing	39	31
Transportation	61	69

SCM Non-Mahindra Industry Wise Break-up (%)	Q1FY21	Q1FY20
Non-Auto	84	74
Auto	16	26

(₹ mn)

SCM Non-Mahindra by Service breakup	Q1FY21	Q1FY20	YoY (%)
Transportation	1,355	2,138	(36.6)
Warehousing & VAS	850	960	(11.5)
Total	**2,205**	**3,098**	**(28.8)**

(₹ mn)

SCM Non-Mahindra by Industry breakup	Q1FY21	Q1FY20	YoY (%)
Auto	355	812	(56.3)
Non-Auto	1,850	2,286	(19.1)
Total	**2,205**	**3,098**	**(28.8)**

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Disclosure of Interest Statement Mahindra Logistics Ltd. as on August 5th, 2020

Name of the Security	Mahindra Logistics Ltd.
Name of the analyst	Jayakanth Kasthuri
Analysts' ownership of any stock related to the information contained Financial Interest Analyst : Analyst's Relative : Yes / No Analyst's Associate/Firm : Yes/No	NIL No Yes No
Conflict of Interest	No
Receipt of Compensation	No
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