CGSCIMB InCred Equities

Sector Note

March 07, 2022

Financial Services - AMCs

Buoyant business model, few beneficiaries

- We initiate coverage on India AMC sector with an Overweight rating as growth and returns opportunities remain buoyant amid underpenetrated markets and rising reach of AMCs.
- With rising awareness towards mutual fund investments, AMCs are likely to become one of the core components of household savings in India.
- AMC business in India remains concentrated among a few large players with access to a large pool of free cash flow/superior RoE/higher dividend payout.

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India

Overweight *(Initiating coverage)*

Highlighted Companies

Aditya Birla Sunlife AMC
ADD, TP Rs650, Rs500 close
We remain comfortable with the valuation of **ABSL AMC** with best-in-class RoE and improved profitability.

Nippon Life India Asset Management Ltd
ADD, TP Rs380, Rs300 close
We like NAM India with best-in-class dividend payouts and improving profit matrices.

UTI Asset Management company
Add, TP Rs1,100, Rs847 Close
We remain confident of a turnaround candidate which is available at an attractive risk-reward ratio.

Summary Valuation Metrics

P/E (x)	Mar22-F	Mar23-F	Mar24-F
Aditya Birla Sunlife AMC	21.5	18.7	15.9
Nippon Life India Asset Management Ltd	18.3	16.6	14.5
UTI Asset Management company	18.29	16.64	14.53

Dividend Yield	Mar22-F	Mar23-F	Mar24-F
Aditya Birla Sunlife AMC	2.3	3.5	4.7
Nippon Life India Asset Management Ltd	2.7	3.3	4.1
UTI Asset Management company	2.73%	3.31%	4.13%

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Financial Services - Others

Buoyant business model, few beneficiaries

- With rising importance of financial savings among Indian households along with underpenetration of mutual funds, the future of Indian AMCs remains promising.
- As incremental flows are led by retail investors, AUMs of equity funds /ETFs are at the forefront – keeping the market share struggle among AMCs intact.
- AMC business in India remains concentrated among a few large players with access to a large pool of free cash flow/superior RoE/higher dividend payout.

India AMCs' AUM to top ~Rs50tr by FY24F on retail flows into equities

As per AMFI data, Indian asset management companies (AMCs) posted ~14.6% AUM CAGR over FY19-21 amid Covid-19 disruption, aided by rising retail participation, improved geographic penetration as well as mark-to-market (MTM) gains arising on investments. We expect the momentum to continue and factor in industry AUM topping Rs50tr by FY24F (~16% CAGR over FY21-24F). Equity funds may remain in favour (first choice of retail customers) followed by improving traction in passive funds or ETFs. As mutual fund business is highly concentrated among top 7-10 AMCs, compounded growth is for a few beneficiaries who will struggle over managing market leadership, especially in equity funds.

AMC business model - free cash flow/zero credit risk/superior RoE

One of the key arguments favoring investment in AMC stocks across the globe has been that unlike most financial players, AMCs do not attract credit risk which is the biggest safeguard for earnings stability. This, coupled with a relatively simplified business model and high operating leverage, results in superior RoEs. Finally, due to a linear capital structure and absence of additional capital requirement for growth, AMCs generate a decent free cash flow for investors, which in turn is eligible for distribution as dividend.

Lenders or non-lenders – which is a preferred play?

This is the common question as the investor is picking an investment between lenders (banks/NBFCs) and non-lenders (AMCs/insurers). For Indian markets, the common theme for both segments have been improving financialization among retail Indian population through increasing reach and digital infrastructure. Our preference for AMCs is triggered by profit and margin uncertainty for lenders amid a tightening monetary cycle and rising inflation though even AMCs will face volatility in flows due to such economic variables. Yet rising retail participation along with free cash flow and absence of credit risk resulting in higher dividend payouts do provide comfort. Recent diversity in product offerings is also likely to keep retail investor interest intact in AMCs.

Comparison of AMCs – chase over market share gain in equity funds

We have compared eight large AMCs in India on the basis of assets under management or AUM, having a market share of ~78% of industry AUM as at Dec 2021-end, to understand their uniqueness across parameters. Most AMCs have lost market share in equity funds during recent years due to various factors including underperformance of schemes, aggressive competition, superior digital reach, etc. Each AMC has expertise in a particular area and there is enough scope for growth and profitability improvement.

Initiate coverage on AMC sector with Overweight rating

We initiate coverage on Indian AMC sector with Overweight rating considering the huge growth opportunity and under-penetrated markets. We are comfortable with the valuation of **ABSL AMC (Add, TP Rs650)** with best-in-class RoE and improved profitability. We also are confident of a turnaround in **UTI AMC (Add, TP Rs1,100),** available at an attractive risk-reward ratio. We like **NAM India (Add, TP Rs380)** with best-in-class dividend payouts and improving profit matrices. We are also confident of **HDFC AMC (Hold, TP Rs2,300)** reviving its market share, but await a relatively attractive risk-reward ratio. Among unlisted players, we are positive on SBI AMC and ICICI Prudential AMC amid market leadership and best-in-class return ratios. Key downside risks: Cyclical business with fluctuations in inflows, regulatory risk impacting earnings, and a highly competitive market scenario, etc.

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Companies

Key investment arguments for India AMCs

Retail flows to dominate AUM profile

Rising retail participation is always an indicator of a further rise in equity AUM, as traditionally retail investors have preferred equity as a mode of investment through mutual funds. On the equity fund side, preference will also continue as the returns scorecard in recent years has been in its favour. While ETFs are still a small fraction of total AUM, the share of these passive investment vehicles will only grow in coming years, in our view.

Profitability set to improve despite pressure on yields

We believe the pressure on yields due to the rise in AUM as well as replacement of old funds with new ones will normalize over the next couple of quarters, but higher brokerage charges amid intensified competition among AMCs are likely to stay. We are factoring in muted revenue yields for all AMCs under our coverage in FY23F, whereas some improvement is likely in FY24F with normalization of TER. However, gradually with operating leverage coming into play, we do factor in sufficient improvement in profit yield in FY24F.

Regulations to ensure better transparency

The Securities and Exchange Board of India (SEBI), mutual fund regulator, has been very proactive with regulatory changes to ensure that loopholes are plugged. As AMC business is yet to mature in India along with a low literacy level of Indian population regarding investment in financial instruments, especially in semi-urban and rural areas, SEBI has been very active in keeping a close eye over the overall functioning of AMCs and regulations surrounding the same.

AMCs enjoys free cash flows with Superior RoEs

One of the key arguments favouring investment in AMC stocks across the globe has been that unlike most financial players, AMCs do not attract credit risk which is the biggest safeguard for earnings stability. This, coupled with a relatively simplified business model and high operating leverage, results in superior RoE. Finally, due to linear capital structure and absence of additional capital requirement for growth, AMCs generate a decent amount of free cash flow for investors, which in turn is eligible for distribution as dividend.

Right mix of Lenders and Non-lenders is preferred

India's banking and financial services sector, although cyclical, is a gradual long-term growth story backed by under-penetration, consistent push for financial inclusion and rising digitalization. The question is lenders or non-lenders - which one should investors prefer as they are picking an investment between lenders (banks/NBFCs) and non-lenders (AMCs/insurers). Lenders are restricted over capital dilution and credit risks but are available at relatively attractive valuations. Non-lenders with limited credit risk and superior RoEs are expensively valued. However, business models may remain cyclical. We strongly believe that selecting the right mix of the two is an ideal strategy.

Stock recommendations

Figure 1: Our AMC recommendations along with brief financial highlights

AMC	Reco	Cur Price	Tgt Price	UPSIDE	Macp(US$ Bn)	AUM CAGR % FY21-24F	Rev CAGR % FY21-24F	PAT CAGR % FY21-24F	RoE FY23F	RoE FY24F	PAT Yield FY23F	PAT Yield FY24F	P/E FY23F	P/E FY24F	% of AUM FY23F	% of AUM FY24F
ABSL	Add	500	650	30%	2	15%	17%	21%	34%	36%	0.22%	0.23%	24	21	5.1%	4.4%
NAM India	Add	299	380	27%	3	18%	14%	13%	25%	28%	0.27%	0.28%	28	24	7.8%	6.7%
UTI	Add	847	1,100	30%	1.5	16%	14%	14%	18%	19%	0.26%	0.27%	22	19	5.5%	4.9%
HDFC	Hold	2,082	2,300	11%	6	12%	13%	11%	27%	27%	0.35%	0.35%	30	27	9.8%	8.5%

SOURCES: INCRED RESEARCH, COMPANY REPORTS, PRICED AT 4TH MAR 2022

Aditya Birla Sunlife AMC (ABSLAMC) (Add, TP Rs650)

- ABSL AMC, in our view, is geared up for reshuffling in AUM with equity and alternative funds (incl. ETFs) registering a surge backed by retail participation.
- We are factoring in ~20.6% CAGR in PAT over FY21-24F backed by gradual improvement in yields coupled with operating efficiency supporting profits.
- Initiate coverage with Add rating and TP of Rs650 based on dividend discount model, corresponding to ~20.7x P/E at FY24F EPS & ~4.4% FY24F AUM.

Nippon Life India AMC (NAMIN) (Add, TP Rs380)

- NAM India has regained debt market share and we expect the same for equity soon due to their scheme outperformances, rising reach and digital initiatives.
- We are building AUM growth of ~18% CAGR from FY21-24F with rising share of equity and consistent dominance of ETFs
- Initiating coverage on NAM India with Add rating and a TP of Rs380 based on dividend discount model, at ~23.6x FY24F P/E and ~6.7% FY24F AUM.

UTI Asset Management (UTIAM) (Add, TP Rs1,100)

- UTI AMC is committed towards superior profitability backed by reshuffling in AUM coupled with decent scope for improvement in operating leverage.
- We are factoring in ~14.4% CAGR in PAT over FY21-24F amid healthy revenue yields and improved PAT yields backed by well managed operating expenses.
- Initiating coverage on UTI AMC with Add rating and a TP of Rs1,100 based on Dividend Discount model, at ~18.8x FY24F P/E and ~4.9% FY24F AUM.

HDFC AMC (HDFCAMC) (Hold, TP Rs2,300)

- HDFC AMC manages elevated individual flows, backed by strong brand recognition, leading to best-in-class returns but market share fall is a concern.
- We factor in a revenue CAGR of 14.9% backed by overall AUM CAGR of ~11.6% whereas PAT is expected to grow by ~11.3% over FY21-24F.
- Initiate coverage with Hold rating and a TP of Rs2,300 based on Dividend Discount model, corresponding to ~26.8x FY24F P/E and ~8.5% FY24F AUM.

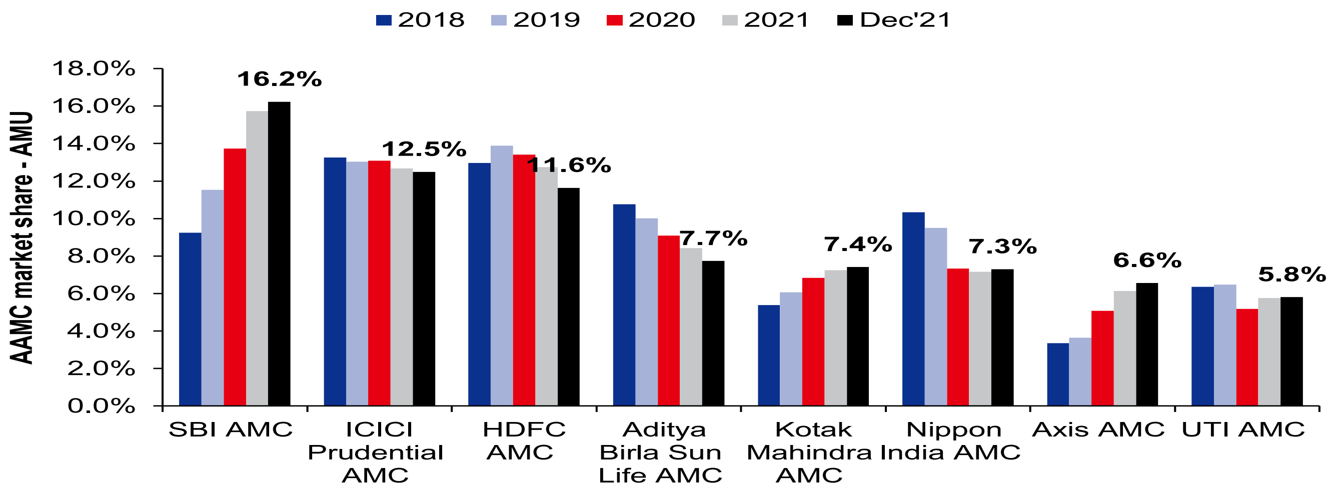
Indian AMCs
Comparable analysis

Comparable analysis of AMCs in India

Here, we present a comparison of large AMCs in India across various parameters to understand the strengths and weakness of each one of them. We have calculated these numbers based on data available on AMFI website and from individual AMC presentations.

Leadership (total AUM) – movement in market share

Figure 2: Movement in market leadership in total AUM



SOURCES: AMFI, INCRED RESEARCH, COMPANY REPORTS

Most AMCs lost market share, barring SBI, Axis, Kotak MFs

Considering the trend of past seven years, we observe that most AMCs have lost their market share despite absolute growth, mainly due to aggressive practices followed by a few players. Overall, industry AUM witnessed ~18.9% CAGR over FY16-21 at Rs32,172bn.

Market share gainers

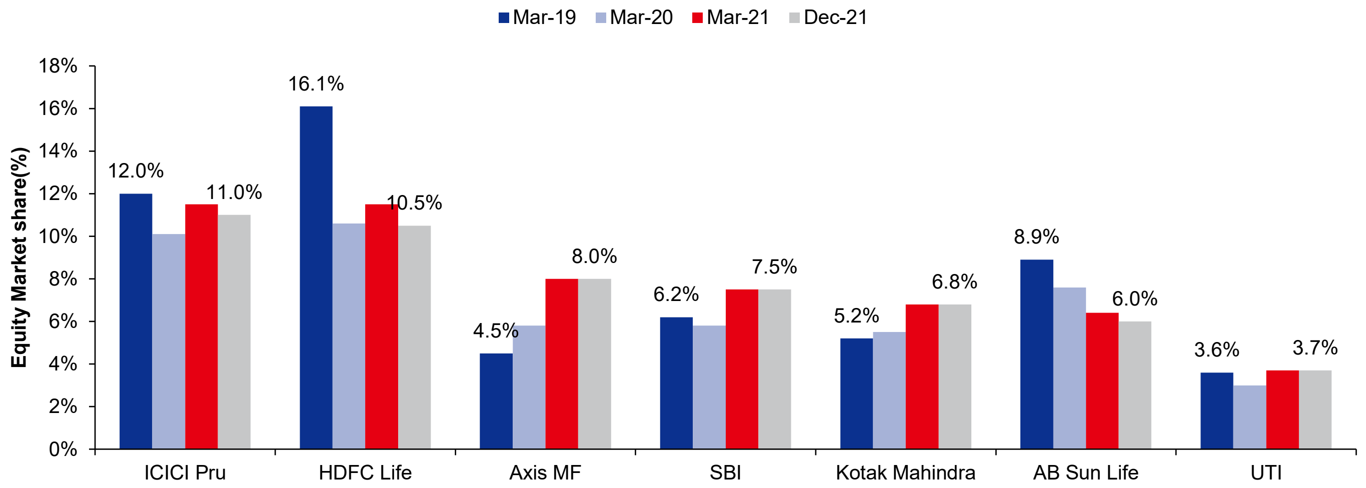
SBI AMC stands out with a rapid pace in AUM growth, allowing it to earn the largest AMC tag in India in Dec 2021. SBI AMC doubled its market share from ~8.1% in Mar 2016 to 16.2% in Dec 2021. Similarly, Axis AMC witnessed multi-fold growth in AUM with an improvement in market share to ~6.6% in Dec 2021 from ~2.9% in Mar 2016 whereas Kotak AMC improved its market share to ~7.4% in Dec 2021 from ~4.4% in Mar 2016.

Market share losers

On the losing front, Aditya Birla AMC and Nippon Life AMC witnessed a decline from their double-digit AUM share to mid-single digit number, but stability is expected from here on. ICICI Prudential AMC and HDFC AMC have been witnessing stiff competition, but their market shares have been stable over the past few years. However, HDFC AMC has been losing its leadership position in terms of AUM growth in recent years.

Leadership (equity fund AUM) – movement in market share

Figure 3: Movement in market leadership in equity fund AUM



SOURCES: AMFI, INCRED RESEARCH, COMPANY REPORTS

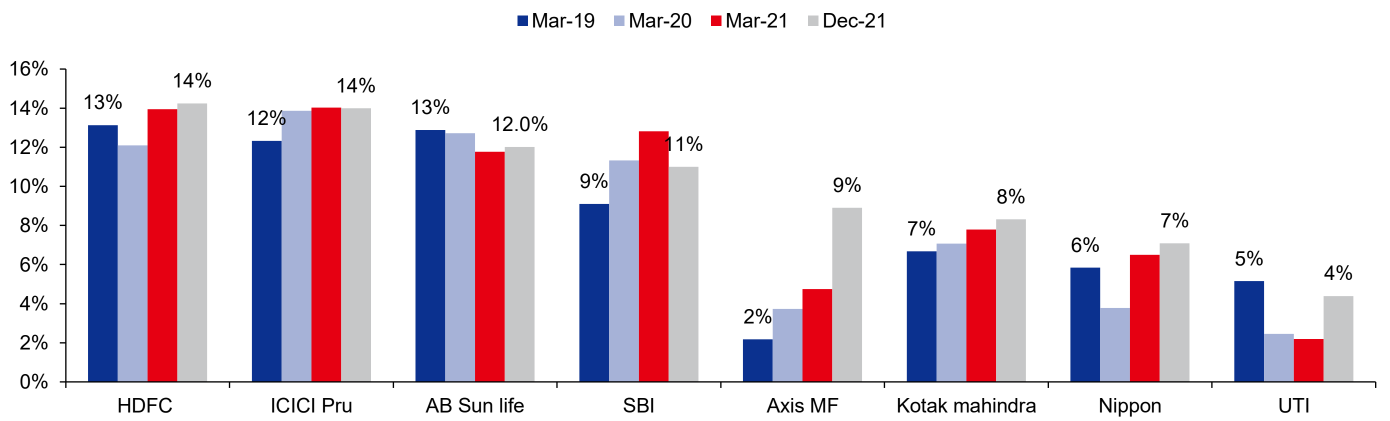
HDFC AMC lost major share against Axis AMC and SBI AMC

Considering the trend of past three-and-half years, we observe that HDFC AMC has lost major ground on equity fund AUM, from ~16% in FY19 to ~10.5% in Dec 2021 whereas ICICI Prudential AMC managed to retain its leadership position despite losing market share from ~12% in Mar 2019 to 11% in Dec 2021.

Axis AMC has been a major beneficiary in past few years with equity fund market share almost doubling from ~4.5% in Mar 2019 to ~8% in Dec 2021. Similarly, SBI AMC gained momentum with its equity fund market share improving from ~6.2% in Mar 2019 to ~7.5% in Dec 2021. Kotak Mahindra AMC is the only gainer apart from these two AMCs, as the rest have all have lost equity fund market share.

Leadership (debt fund AUM) – movement in market share

Figure 4: Movement in market leadership in debt fund AUM



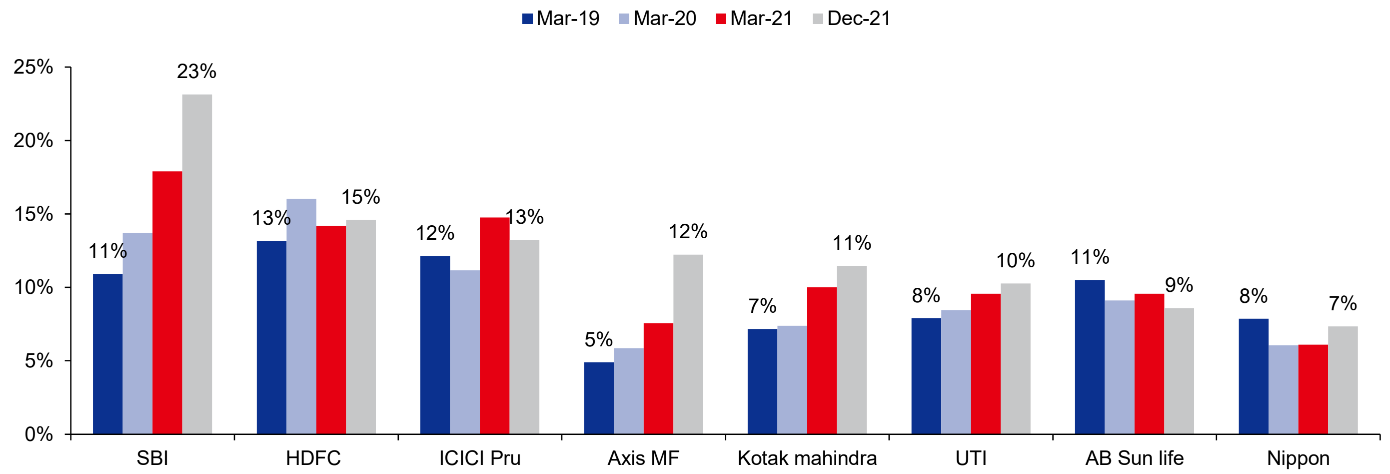
SOURCES: AMFI, INCRED RESEARCH, COMPANY REPORTS

HDFC/I PRU AMC manage leadership position, but Axis MF/ SBI AMC register gains

Considering the trend of past three-and-half years, we observe that HDFC AMC along with ICICI Prudential AMC manged market leadership position with ~14% share but AB Sunlife lost some share. Axis MF once again remained the main beneficiary with a 9% market share whereas SBI managed at ~11%.

Leadership (liquid AUM) – movement in market share

Figure 5: Movement in market leadership in liquid fund AUM



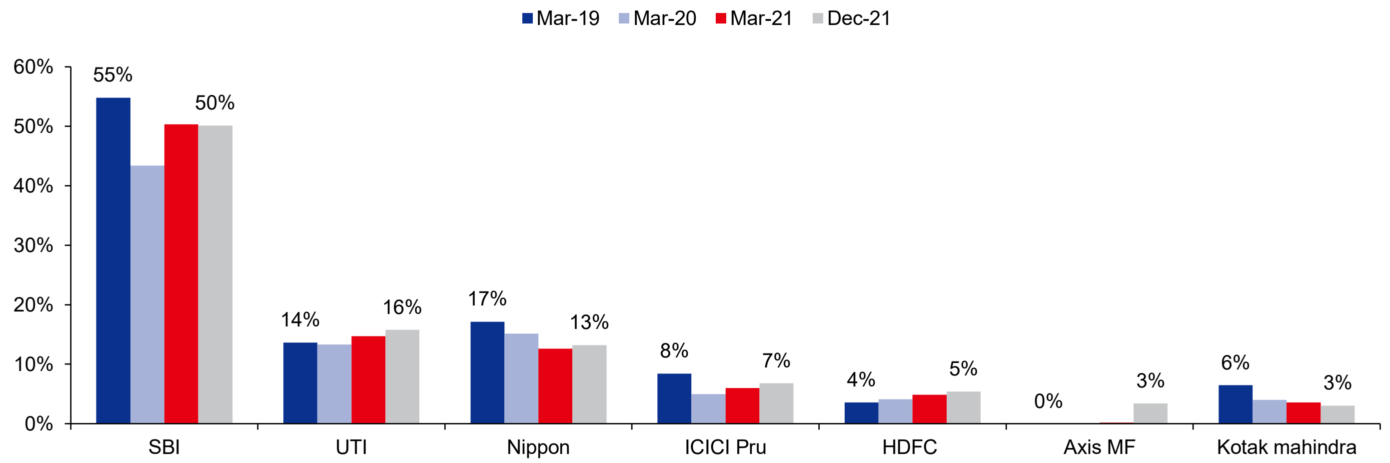
SOURCES: AMFI, INCRED RESEARCH, COMPANY REPORTS

SBI AMC gains leadership position led by PSU-affiliated flows

Considering the trend of past three-and-half years, we observe that SBI AMC has managed to double market share to ~23% in Dec 2021 from ~11% in Mar 2019, mainly led by PSU-affiliated flows. AB Sunlife AMC along with NAM India remain market losers in the segment.

Leadership (ETFs) – movement in market share

Figure 6: Movement in market leadership in ETF AUM



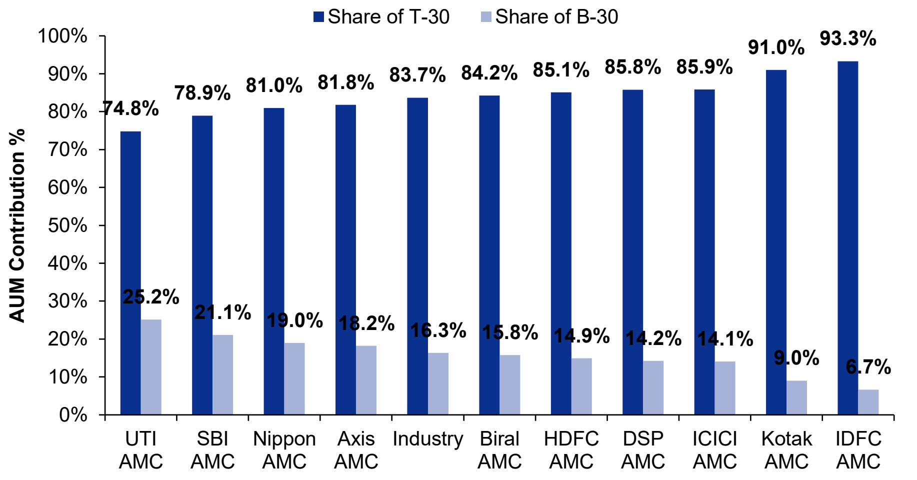
SOURCES: AMFI, INCRED RESEARCH, COMPANY REPORTS

SBI AMC dominates the market, NAM India holds its position

SBI AMC, again led by government and PSU-affiliated flows, dominates ETFs with ~50% market share. These flows also made it gain leadership position on overall AUM basis. It is followed by UTI AMC which also gained business through government affiliations. NAM India managed to hold a decent share with ~13% market share mainly led by its exclusive bouquet of products available in ETF segment.

Presence in B-30 cities – penetration remains low

Figure 7: Share of T-30 (Top-30 cities) and B-30 (beyond T-30 cities) AUM among top 10 AMCs in India (Jun 2021-end)



SOURCES: AMFI, CRISIL, INCRED RESEARCH

B-30 cities' share remains under-penetrated for most AMCs

Despite the breakout growth observed over last 10-15 years, Indian asset management industry continues to be significantly under-penetrated compared to other countries and other financial services in India. One of the key reasons for the same has been low geographic penetration in B-30 cities (beyond top-30 cities) where nearly 90% of Indian households are located.

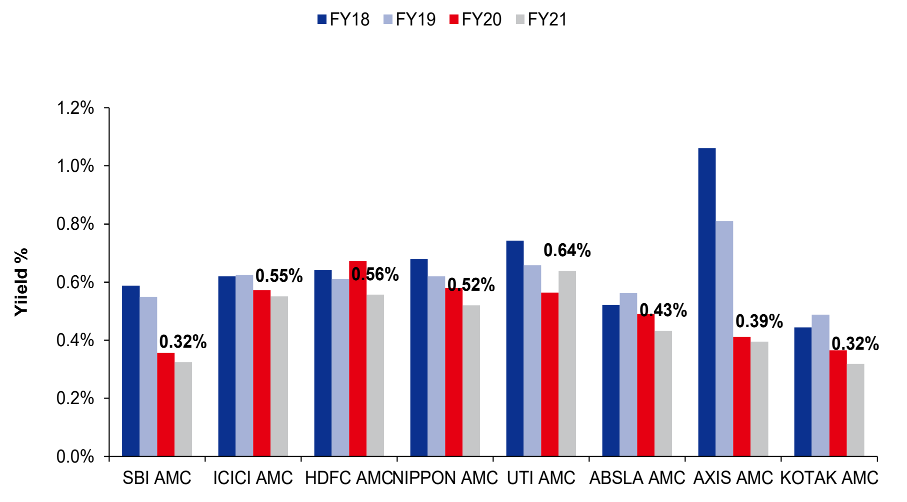
The share of B-30 cities in total industry AUM hovered around just 15-17% over last few years. Of the 97.9m folios as at Mar 2021-end, around 56.5m folios are from T-30 cities and 41.4m from B-30 cities. Our interactions with most AMC managements indicate that B-30 cities will continue to expand their customer base, although the ticket size will be small. While T-30 markets will be value-driven and volume-driven at the same time, B-30 will be volume-driven followed by value.

SBI AMC and UTI AMC remain better off versus other AMCs

UTI AMC and SBI AMC are the only two players having a share greater than 20% of AUM in B-30 cities (cities after Top-30 cities). Higher presence of AMCs in B-30 cities makes them well-placed to attract new customers at these locations. This is primarily due to their established position, infrastructure, and distribution capabilities for which they have already invested in. The ability to charge an additional 30bp in expense ratios for B-30 locations reduces the pressure on scheme margins.

Revenue yield – decline is in sync with SEBI regulations

Figure 8: Rationalization of revenue yields is in sync with SEBI regulations



SOURCES: INCRED RESEARCH, COMPANY REPORTS

Revenue yields witness a dip post change in SEBI norms

With consistent growth in AUM, as per SEBI regulations, larger fund schemes need to operate with a lower TER (total expense ratio). Subsequent to regulatory changes, as a result of the reduction in TER, the investment management fee in general is accordingly lower, particularly in open-ended equity funds and hybrid funds.

UTI AMC manages superior yields whereas SBI AMC is at the lower end

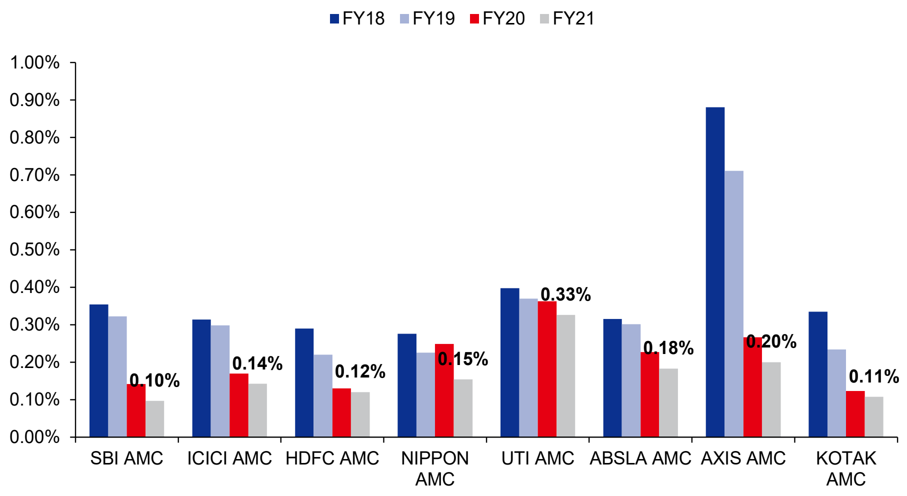
UTI AMC stands out with highest yields on AUM at ~64bp in FY21 whereas SBI AMC managed lowest yields, at ~32bp. Yields are generally a function of asset mix and with an elevated share of passive funds, SBI AMC witnessed a consistent dip in yields, which we expect will flatten soon.

ICICI AMC, Nippon AMC and Birla AMC witness stable yields

Post change in SEBI norms, ICICI Prudential AMC, NAM India AMC and Aditya Birla Sunlife AMC witnessed stable yields, a result of the balanced mix of AUM with rising traction in equity funds and ETFs. We expect revenue yields to remain under pressure over FY22-23F amid repricing of AUM as well as new TER norms after which we can expect a revised and improved margins profile from FY23F.

Operating expenses – rationalization across the board

Figure 9: Operating expenses witnessed a sizable improvement over the years



SOURCES: INCRED RESEARCH, COMPANY REPORTS

Operating leverage is a key feature of AMC model

All AMCs have witnessed a sharp improvement in cost-to-average assets ratio over the years with operating leverage kicking in for them. This is the benifit of the model whereby post initial investments, with a rise in AUM, increase in operating expenses is slower compared to the rise in revenue which in turn supports profitability.

SBI AMC manages lower cost of operations followed by HDFC AMC

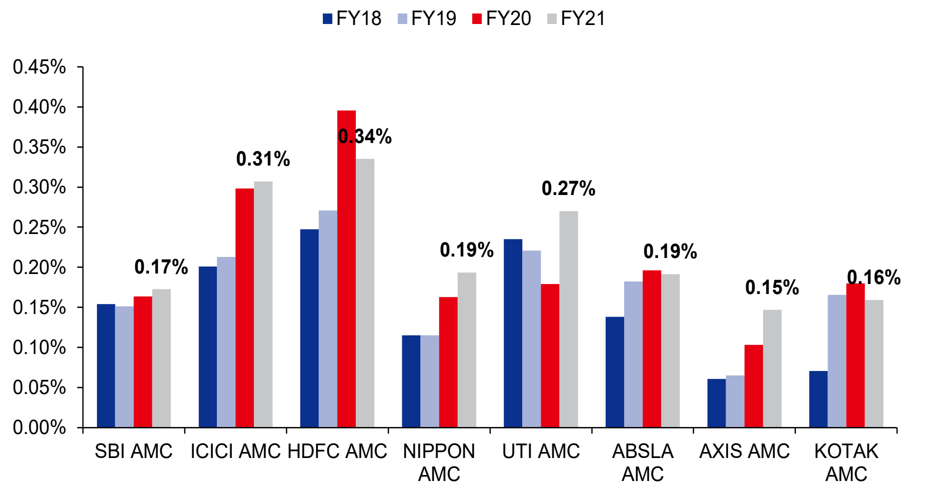
SBI AMC, despite being market leader, manages operations at the best utilisation level, resulting in lowest cost-to-average assets ratio followed by HDFC AMC which enjoys superior yields as well.

UTI AMC continues to struggle on cost front

UTI AMC, on the other hand, has a higher cost burden which in turn impacts the profitability of the company. Though the AMC has witnessed an improvement over the years, still there is enough scope for improvement in coming years. Axis AMC is also loaded with a relatively higher operating charge but the same has witnessed a substantial improvement over the years.

PAT yields – operating leverage plays its role

Figure 10: Contrary to the decline in revenue yields, PAT yields witness a surge



SOURCES: INCRED RESEARCH, COMPANY REPORTS

PAT yields improve on the back of better operating leverage

Interestingly, in contrast to the decline in revenue yields, AMCs have witnessed an improvement in PAT yields backed by strong operating leverage which has played a pivotal role in improving profits for AMCs.

HDFC AMC manages superior yields whereas Axis AMC is at the lower end

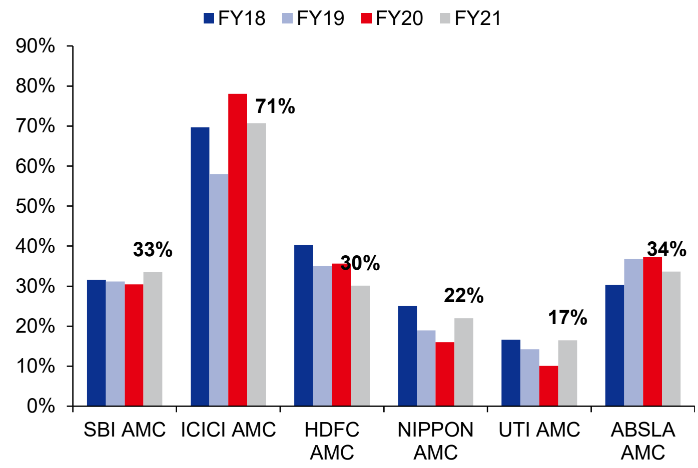
HDFC AMC manages to earn best-in-class profitability with superior AUM mix (elevated share of equity funds) as well as a well-managed cost structure. ICICI Prudential AMC is also on a similar path with relatively better profit yields.

Axis AMC and Kotak AMC on the lower end of the curve

Axis AMC and Kotak AMC are on lower end of profitability. Kotak AMC has relatively low revenue yields which in turn is transmitted to weak PAT yields as well. For Axis AMC, the same can be attributed to elevated employee expenses, which had been the case with Nippon AMC and Birla AMC as well earlier. However, gradually they managed to improve. We expect muted profitability trend in FY22F year amid pressure on revenue yields, but a surge in profitability is expected from FY23F.

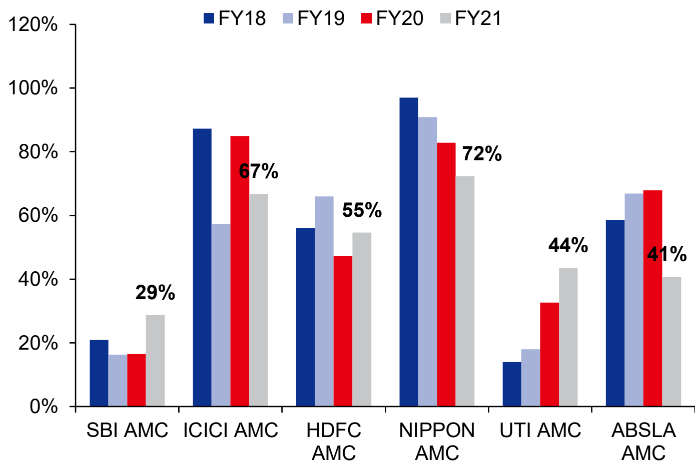
Return ratios and dividend payout – higher the better

Figure 11: Better profitability results in superior RoE



SOURCES: INCRED RESEARCH, COMPANY REPORTS

Figure 12: Low capital requirement allows high dividend payout



SOURCES: INCRED RESEARCH, COMPANY REPORTS

ICICI Prudential AMC tops RoE list followed by Birla AMC

ICICI Prudential AMC tops the list with best-in-class RoE which is a result of better revenue yields and profitability. Birla AMC, despite lower PAT yields, manages better RoE which is the result of optimum utilisation of capital. UTI AMC is at the lowest end of RoE due to heavy operating expense structure which needs to be modified.

Nippon AMC tops dividend payout list followed by ICICI Prudential AMC

Nippon AMC manages highest dividend payout among AMCs as the company has been distributing ~72% of profits as dividend, but this trend has been declining over the years. It is followed by ICICI Prudential AMC with ~67% payout. Linear capital model and absence of any capital requirement allows AMCs to distribute a major portion of their profits as dividend. SBI AMC has been distributing lowest profits to its unit holders, but the same can see an improvement post-listing.

Scheme performance of AMCs in India

As market share in equity fund AUM remains most challenging in recent times for AMCs across India, we have analysed scheme performance of equity products of listed AMCs in India. We have measured returns based on timeframe as well as market cap of stocks that the scheme handles.

Following is the key outcome of our exercise:

Figure 13: Ranking of a scheme (up to top 10) from each AMC across market cap stocks for different time frame

	Equity Large-Cap			Equity Multi-Cap			Equity Mid-Cap			Equity Small-Cap		
	Based on 1-year return	Based on 3-year return	Based on 5-year return	Based on 1-year return	Based on 3-year return	Based on 5-year return	Based on 1-year return	Based on 3-year return	Based on 5-year return	Based on 1-year return	Based on 3-year return	Based on 5-year return
NAM India	3	-	-	3	8	6	5	-	-	4	7	3
UTI AMC	6	5	8	-	-	-	8	8	7	-	-	-
ABSL AMC	8	-	-	-	-	-	-	10	-	-	-	-
HDFC AMC	-	-	-	-	-	-	-	-	-	-	-	6

SOURCES: AMFI, INCRED RESEARCH, COMPANY REPORTS

NAM India AMC has been a relatively better performer followed by UTI AMC

The schemes of NAM India AMC have been performing well as schemes for each market cap (large/multi/mid/small) has one NAM India scheme in top 10 position across timeframes. Management has been highlighting about its scheme outperformance since a while now and remains confident of a revival in equity fund market share in coming quarters.

UTI AMC is also performing well in certain buckets

Equity fund schemes of UTI AMC have also been doing better, at least in large-cap and mid-cap stocks whereas multi-cap and small-cap are still struggling. The investment team of UTI AMC has been revamped already and is well prepared to regain lost momentum for the AMC.

ABSL AMC and HDFC AMC have still been struggling

There was limited outperformance visible from schemes run by ABSL AMC as well as HDFC AMC. However, we remain optimistic about a gradual recovery in the performance of schemes run by both these AMCs.

Scheme outperformance is a must to attract equity fund inflows

Although the conclusion that scheme outperformance is a must for equity fund inflows has been arrived at from limited data available and needs to be relooked based on more detailed data points, the bottom line to understand is that considering the access to information that retail customers have along with a competitive environment in AMC markets, scheme outperformance is a must to attract equity fund inflows.

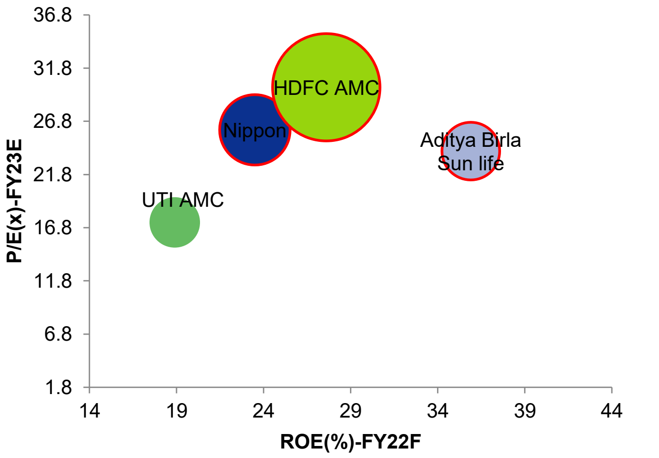
Indian AMCs
Valuation comparison

Valuation parameters

We have plotted all listed AMCs, based on their forward RoEs, on a valuation table. We have considered one-year and two-year forward multiples to assess valuation premium or else discounting of all listed players.

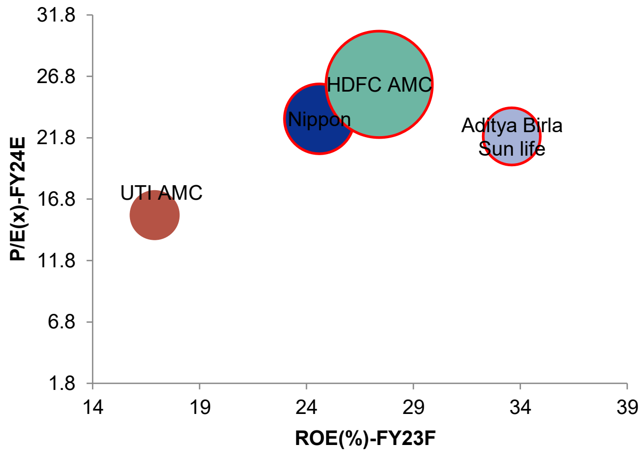
Comparison based on P/E to RoE basis

Figure 14: RoE in FY22F compared to FY24F P/E



SOURCES: BLOOMBERG, INCRED RESEARCH ESTIMATES

Figure 15: RoE in FY23F compared to FY24F P/E



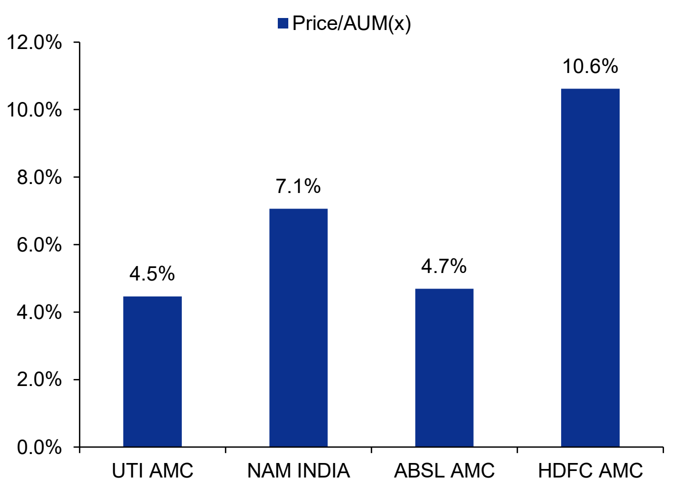
SOURCES: BLOOMBERG, INCRED RESEARCH ESTIMATES

ABSL and UTI AMC trade below the trendline

On comparing listed AMCs, based on P/E and RoE multiple, we observe that Aditya Birla Sunlife AMC (ABSL) and UTI AMC (UTI) are better placed compared to Nippon Life Asset Management (NAM India) and HDFC AMC (HDFCA). We see a probable expansion in multiple for ABSL and UTI AMC in comparison to NAM India and HDFCA.

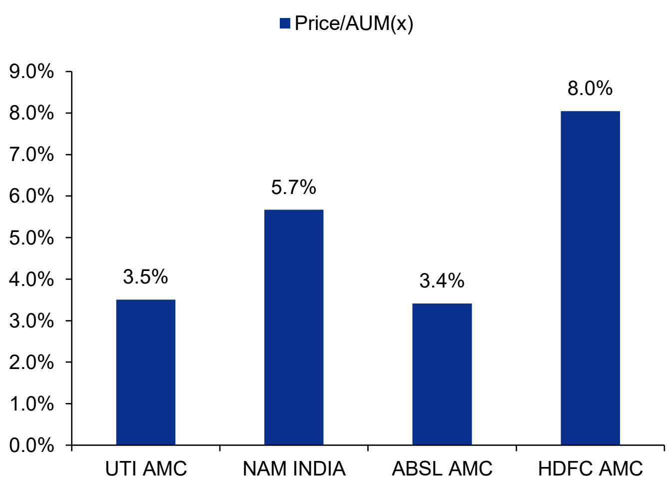
Market capitalization as a % of AUM

Figure 16: Current market cap to 3QFY22 AUM (%)



SOURCES: INCRED RESEARCH, BLOOMBERG

Figure 17: Current market cap to FY24F AUM (%)



SOURCES: INCRED RESEARCH ESTIMATES, BLOOMBERG

ABSL and UTI AMC trade cheap on AUM basis as well

On comparing listed AMCs, based on % of AUM, we observe that Aditya Birla Sunlife AMC (ABSL) and UTI AMC (UTI) are trading at a attractive valuation compared to Nippon Life Asset Management (NAM India) and HDFC AMC (HDFCA). We see a probable expansion in % of multiple for ABSL and UTI AMC compared to NAM India and HDFCA.

Indian AMCs
Investment arguments

India AMC AUM to top Rs50tr by FY24F

India AMCs witnessed consistent demand for mutual funds (mainly equity funds and ETFs) during the past several years and even the Covid-19 pandemic could not derail the momentum. As per AMFI data, India AMCs witnessed AUM CAGR of ~19.8% over FY14-FY21.

The key contributors to this surge are given below:

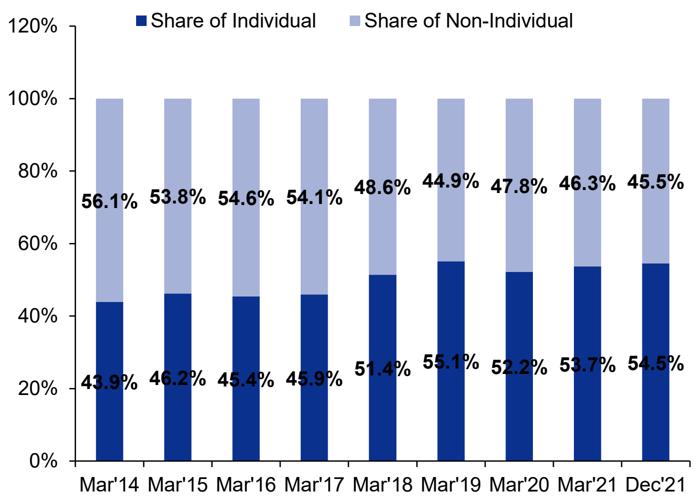
- Rising traction among Indian retail households (Including SIPs).
- Rising geographical penetration.
- Diversified product mix.
- Dynamic distribution reach.

These factors ensured a sustained AUM growth momentum for the industry.

Rising retail participation to aid AUM growth

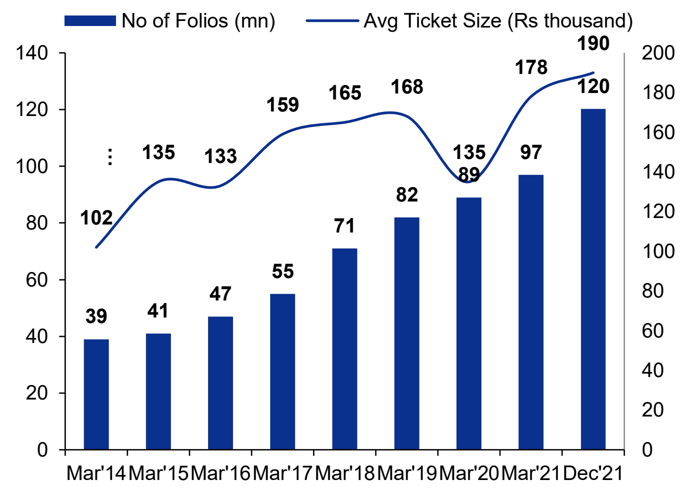
Backed by financialization of savings along with rising awareness about mutual funds led to rising retail participation in AMCs. The trend is improving but is still way below developed nations, thereby creating enough scope for growth.

Figure 18: Share of individuals in industry AUM is improving



SOURCES: AMFI, INCRED RESEARCH, COMPANY REPORTS

Figure 19: Individual folios and average ticket size witness a rise

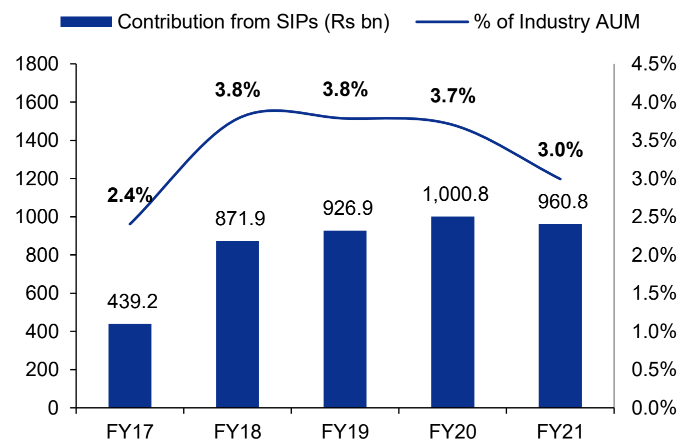


SOURCES: AMFI, INCRED RESEARCH, COMPANY REPORTS

SIPs have been a key contributor to retail participation

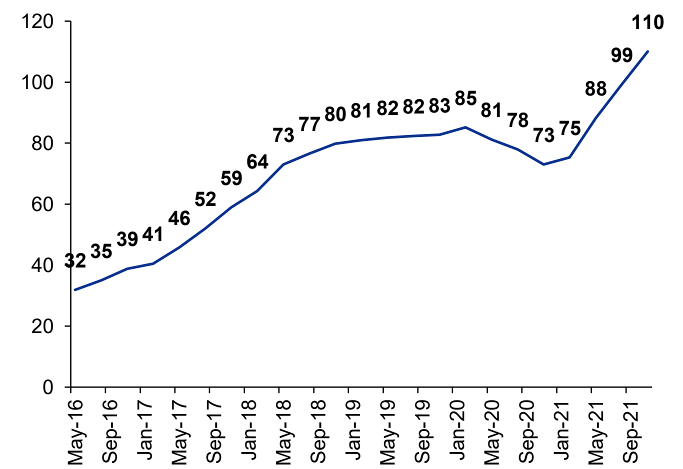
As per AMFI data, mutual fund industry collected approximately Rs0.96tr through SIPs in FY21 as against Rs1tr in FY21. However, we expect this number to be surpassed in FY22F.

Figure 20: Contribution of SIP flows remains healthy



SOURCES: AMFI, INCRED RESEARCH, COMPANY REPORTS

Figure 21: SIP folios are on the rise since past few years

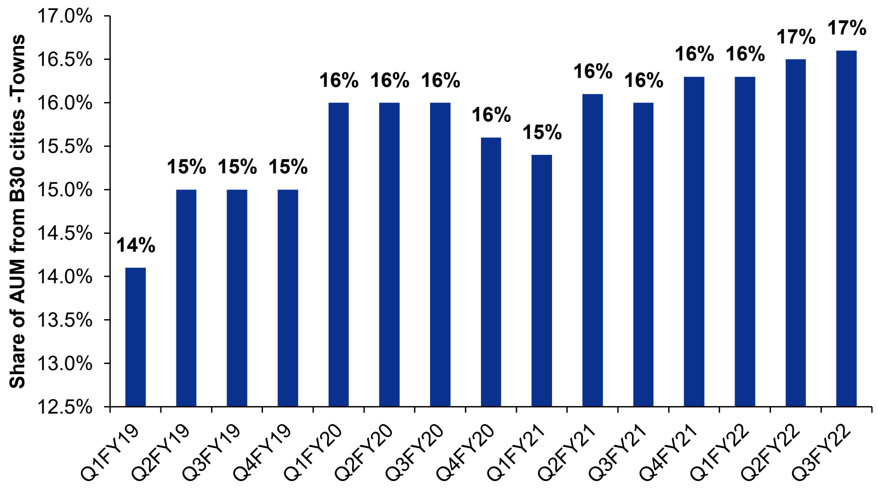


SOURCES: AMFI, INCRED RESEARCH, COMPANY REPORTS

Increasing traction in B-30 cities

Mutual funds have been witnessing low geographic penetration in B-30 cities (beyond Top-30 cities) where nearly 90% of Indian households are located. Our interactions with most AMC managements indicate that B-30 cities will continue to see expansion in customer base, although the ticket size will be small. While Top-30 cities (T-30) will be value-driven and volume-driven at the same time, B-30 will be volume-driven followed by value.

Figure 22: Share of B-30 (cities after Top-30 cities) in AMC AUM



SOURCES: AMFI, INCRED RESEARCH, COMPANY REPORTS

The share of B-30 cities (cities after Top-30 cities) in total industry AUM hovered around just 15-17% over last few years. As per AMFI data, of the 97.9m folios as at end-Mar 2021, around 56.5m folios are from T-30 cities and 41.4m from B-30 cities.

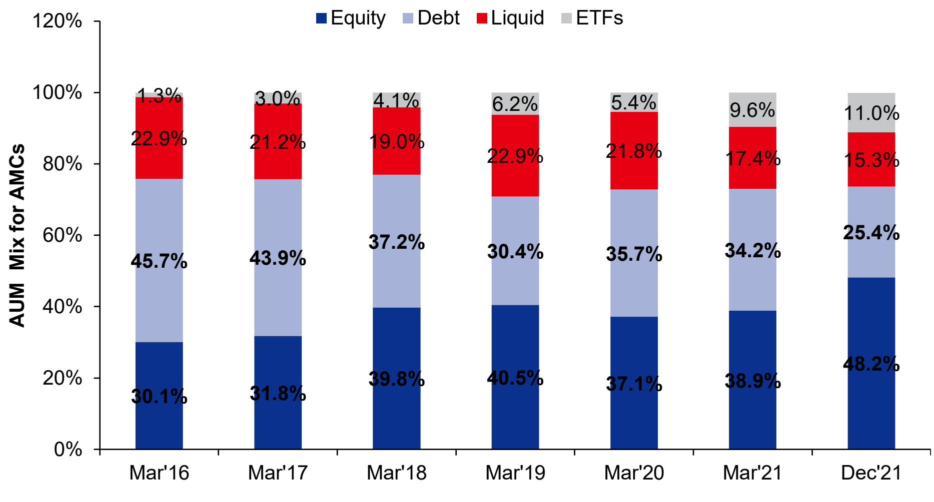
Passive funds in India gain momentum

Indian AMCs have not only increased their reach across different geographies but have also diversified into different investments (including passive investments). This has resulted in a rise in investor interest as well as momentum in overall AUM.

The rise of ETFs in India

ETF (exchange traded fund) as a mode of investment is gaining popularity among investors for several reasons, but primarily active mutual funds are finding it increasingly difficult to sustain higher returns and several of them have been lagging benchmarks. Also, ETFs are now being built on indices with strategies, sector opportunities that are distinct from plain vanilla mainstream mutual funds or MFs.

Figure 23: The rise in ETF share is clearly visible



SOURCES: AMFI, INCRED RESEARCH, COMPANY REPORTS

Even though India still has a long way to go in ETFs' market maturity, when compared to other countries, the numbers look promising.

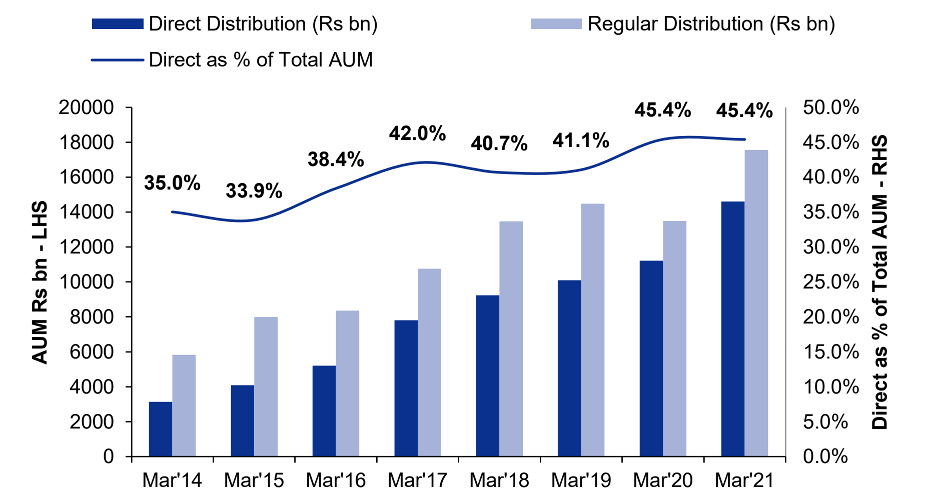
Moving towards differentiated distribution channels

Traditionally, mutual funds are being distributed through three alternative channels: independent financial advisors (IFAs), banks and national distributors. However, gradually the mode of distribution is witnessing a dynamic change.

Rising focus on direct channels for distribution

In Sep 2012, SEBI mandated mutual fund houses to start offering products through the direct route alongside distributors. A direct plan is what you buy directly from the mutual fund company (usually from its own website) whereas a regular plan is what you buy through an advisor, broker, or distributor (intermediary). The expense ratio is higher under a regular plan.

Figure 24: Rising dominance of the direct channel of distribution is visible



SOURCES: AMFI, INCRED RESEARCH, COMPANY REPORTS

Direct plans offers the benefit of a lower expense ratio to investors compared with regular plans. They also allow AMCs to directly connect with investors without depending on intermediaries. Gradually, we may see rising investor awareness and integration of user interfaces through digital channels to promote growth in direct plan AUM.

Fintech entity as a distributor is a value-add proposition for all

The emergence of fintech platforms could lead to a substantially different market landscape for the asset management industry. On the consumer side, it breaks down the market segmentation created by numerous distribution channels organized by fund families, banks, and brokers, just like Amazon did for books and retail goods. Moreover, platforms distribute funds via easy-to-use mobile apps, which allow individuals to make quick investment decisions. On the production side, fund managers, no matter how small or invisible, have the potential to reach the entire user base of these platforms.

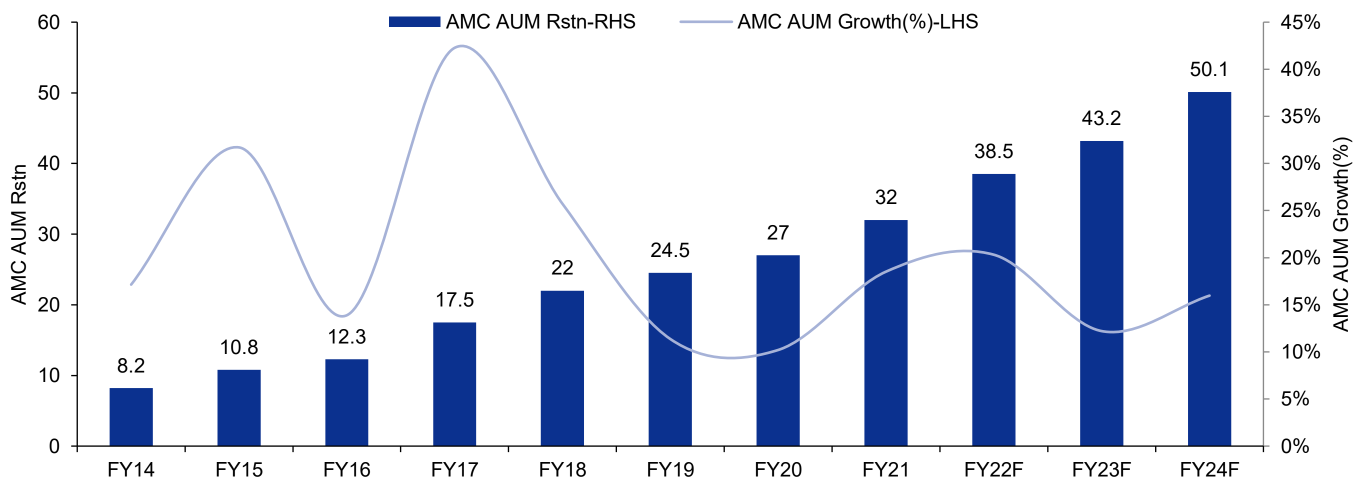
Traditional players holding ground; fintech provides the challenge

As stated earlier, fintech companies are gaining ground in MF distribution business but traditional players (brokers and national distributors) are still far ahead. As at Mar 2021-end, individual and national distributors (NDs) had ~37% share in total industry AUM compared to ~5% in case of fintech firms. As at Mar 2021-end, assets under advisory of distributors and NDs amounted to Rs12tr out of total Rs32tr industry assets. Fintech firms have an average AUM of Rs.1.6tr. In case of new sales in FY21, the share of traditional players (includes individual distributors and NDs) was 28%.

India AMC AUM to surpass Rs50tr by FY24F

Backed by rising retail participation, improved penetration, diversified product mix and a scalable distribution mix, we expect India AMCs to deliver ~16% CAGR over FY21-24F and surpass AUM of Rs50tr by FY24F.

Figure 25: AMC AUM to top Rs50tr by FY24F, in our view



SOURCES: AMFI, INCRED RESEARCH ESTIMATES, COMPANY REPORTS

AUM market share remains highly concentrated in top 7-10 AMCs in India. So, the compounding growth story is applicable to limited beneficiaries. We expect large AMCs to grow even bigger while smaller ones might see further consolidation. Although consistent regulatory intervention remains the biggest challenge in the near term, it also brings transparency in overall business which should be taken on a positive note.

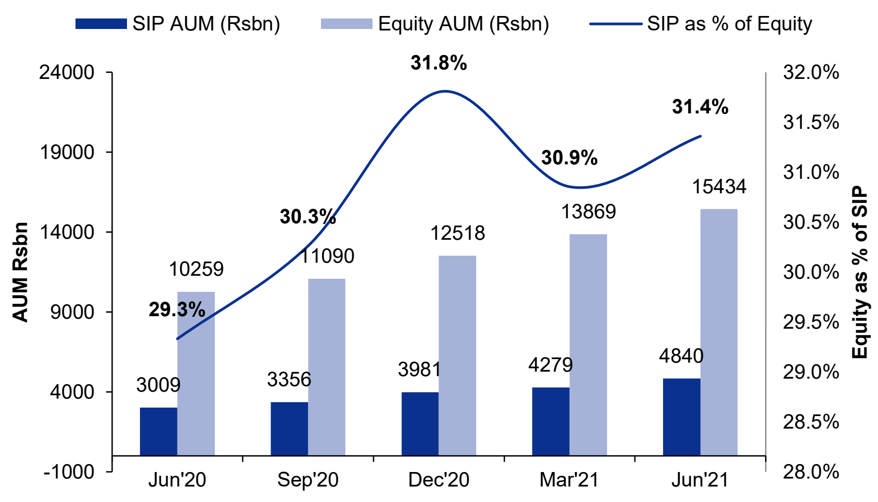
Equity funds/ETFs dominate AUM profile

Our projection of industry AUM topping Rs50tr by FY24F is primarily based on rising retail participation (including through systematic investment plans or SIPs) and across geographies including smaller towns and cities in India.

Equity fund is the preferred mode of retail participation

Rising retail participation is always an indicator of a further rise in equity fund AUM as traditionally, retail investors have preferred equity as a mode of investment through mutual funds. On the equity fund side, preference will also continue as the returns scorecard in recent years has been in its favor.

Figure 26: SIP flow has a direct correlation with equity AUM



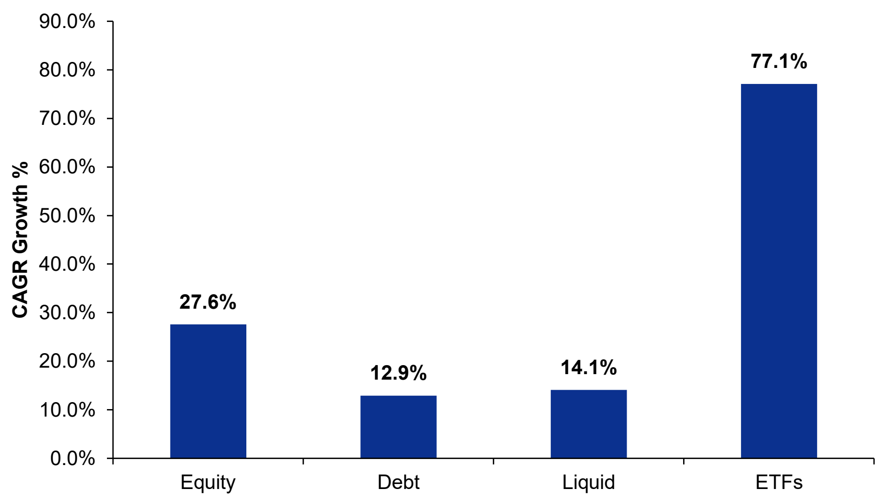
SOURCES: AMFI, INCRED RESEARCH, COMPANY REPORTS

Equity AUM has a direct correlation with SIP flow and with a gradual improvement in SIP flow, we expect traction in equity AUM to remain stronger on a relative basis.

ETFs (passive funds) continue to maintain traction

While ETFs are still a small fraction of total AUM, the share of these passive investment vehicles will only grow in the years ahead, in our view.

Figure 27: AUM CAGR % of top 10 AMCs in India by asset class from Mar 2016 to Jun 2021



SOURCES: AMFI, INCRED RESEARCH, COMPANY REPORTS

For top 10 players, as per AMFI data, ETFs grew at a CAGR of approximately 77% between Mar 2016 and Jun 2021, outpacing other segments. Going ahead as well, we expect traction in ETFs to continue to remain robust amid diversity in returns as well as rising customer confidence in the product.

Fixed-income flows to depend on monetary policy

Indian AMCs have witnessed a relatively muted growth in debt/liquid fund AUMs over past several years amid interest rate softening supporting equity investment over fixed income, but we believe that we are already at the bottom of the interest rate cycle and the only way policy rates can move is northwards.

Liquid funds/shorter maturity products preferred

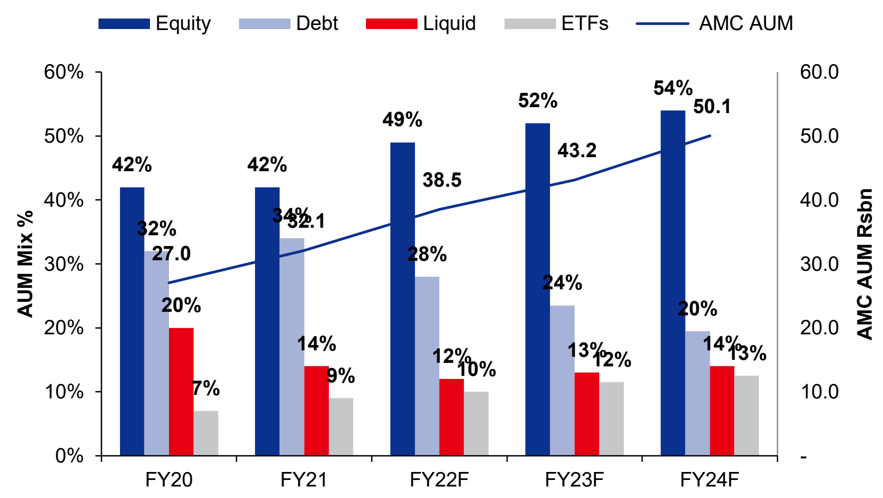
When inflation is soaring in the economy, investors cannot ignore real interest rates. Fixed deposits at 5% interest per annum are already giving negative returns. Though interest rates may be a bit higher for long-tenure bonds, it makes no sense to lock-in, as rates are expected to rise, and investors are bound to experience volatility in case rates move up gradually.

Considering probable tightening of the monetary cycle, liquid funds will witness better traction over debt funds as shorter-tenure assets will generate better returns compared to longer-tenure debt funds. While the investment in short-to-medium duration funds earn a higher yield, the liquid fund exposure reduces the overall impact of interest rate movement on the fixed-income portfolio.

Mix of equity funds/ETFs to drive AUM growth

Based on the matter stated above, we expect India AMCs to deliver ~16% CAGR over FY21-24F and surpass AUM of Rs50tr by FY24F. Equity funds and ETFs will remain major contributors to AUM growth and increase their share in total AUM whereas liquid funds will see some traction and debt funds may witness a decline amid a rising rate scenario.

Figure 28: AUM mix over FY21-24F



SOURCES: AMFI, INCRED RESEARCH ESTIMATES

We are confident of improved profitability

As we remain confident on AUM growth for AMCs, being a concentrated industry, large players will gain a major advantage out of the same. However, such consistent AUM growth needs to be translated into healthy profit growth as well which remains questionable, mainly amid shrinking revenue yields for AMCs due to various factors.

Pressure on revenue yields likely in the near term

- Most listed AMCs have reported pressure on revenue yields in past couple of quarters which can be attributed to various reasons, but we are broadly categorizing the same into following broad parts:
- With consistent growth in AUMs, as per SEBI regulations, larger fund schemes need to operate with lower TER (total expense ratio). The investment management fee is, in general, the residual amount of TER after charging the scheme with other expenses like commission/brokerage and scheme operating expenses. Subsequent to regulatory changes, as a result of the reduction in TER, the investment management fee in general is accordingly lower, particularly in open-ended equity funds and hybrid funds.
- Secondly, although upfront distribution commission is no longer there, considering competitive intensity, brokers and distributors have started commanding higher commission. Hence, incremental new fund offers (NFOs) are witnessing lower yields.
- As better-yield old assets are getting replaced by lower-yield new assets, overall yields come under pressure. This is rather transitionary and would normalise over a period.
- As passive funds (ETFs) witness superior growth compared to other asset classes, yields are expected to remain under pressure as passive funds command lower management fees. However, most AMC managements are planning to develop smart beta products on the passive front (higher yields in passive) to cushion blended yields.

Muted revenue yields in FY23F, improvement likely in FY24F

As we understand after our interactions with various AMC managements, the pressure on yields due to the rise in AUM as well as replacement of old funds with new ones will normalize over the next couple of quarters, but higher brokerage charges amid intensified competition among AMCs may stay. We are factoring in muted revenue yields for all AMCs under our coverage in FY23F whereas some improvement is likely in FY24F with normalization of TER.

Other operating income for AMCs to remain volatile

We have been witnessing volatility in other income for most AMCs during recent years. Such volatility affects overall profitability of AMCs in either way but consistency of the same always remains a questionable thing.

Fluctuations in other income due to investment book fragility

Most AMCs invest a portion of their investment book in their own equity schemes and other related schemes. In case of large volatility in markets (equity as well as fixed income), AMCs need to mark-to-market profits/losses arising from such investments which keeps other operating income fragile. We do not expect any major change in this regard.

Yield pressure to be compensated by rationalising costs

As stated earlier, revenue yields are expected to remain under pressure, at least in the near term, but to manage profitability most AMC managements are likely to rationalise overall operating expenses.

Employee charges rationalisation, passive funds have better leverage

A major portion of operating expenses (~40-50%) for AMCs is routed through employee charge which already has seen rationalization since past several quarters in case of most AMCs, but AMCs being operating leverage play, we do expect that with a surge in AUM there is a scope for further rationalisation.

Additionally, the rise in passive funds has an advantage of being managed by a small team of employees and with a rise in volume, incremental opex related to ETFs is expected to be negligible. This in turn would support profitability further.

Focus on digitalisation – direct channels preferred to cut costs

Most AMC managements are intending to leverage investments made in technology to drive retail customer growth, reduce marketing and operational cost, and improve profitability. Investment in technology is expected to increase online sale of schemes, online payment, digital onboarding as well as customer interaction on digital channels.

AMCs are trying to make their services accessible on mobile platforms and online portals by improving and maintaining easy-to-use applications for investors and distributors. In addition, they are actively exploring potential strategic relationship opportunities with both conventional and non-conventional large digital businesses operating in the space of e-commerce, over-the-top (OTT) channels and aggregators to capture AUM growth driven by the rising importance of digital distribution.

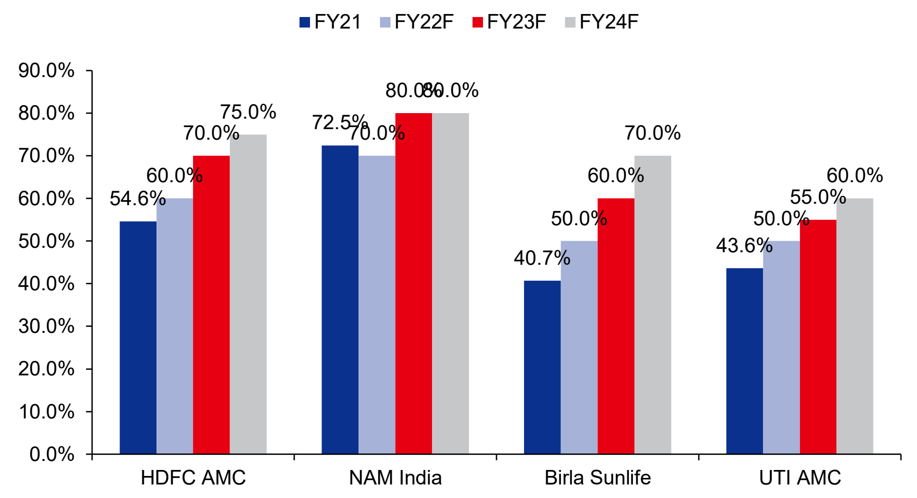
Muted PAT yields, but absolute profit growth to continue

As we expect muted revenue yield in FY23F, optimisation of digital initiatives will take at least a few quarters which will ensure muted growth in profitability in coming fiscal. However, gradually with operating leverage coming into play, we do factor in sufficient improvement in profit yield in FY24F.

Superior RoE, higher dividend payout

One of the key arguments favouring investment in AMC stocks across the globe has been that unlike most financial players, AMCs do not attract credit risk which is the biggest safeguard for earnings stability. This, coupled with a relatively simplified business model and high operating leverage, results in superior RoE. Finally, due to linear capital structure and absence of additional capital requirement for growth, AMCs generate a decent amount of free cash flow for investors, which in turn is eligible for distribution as dividend.

Figure 29: Dividend payout by AMCs remains elevated

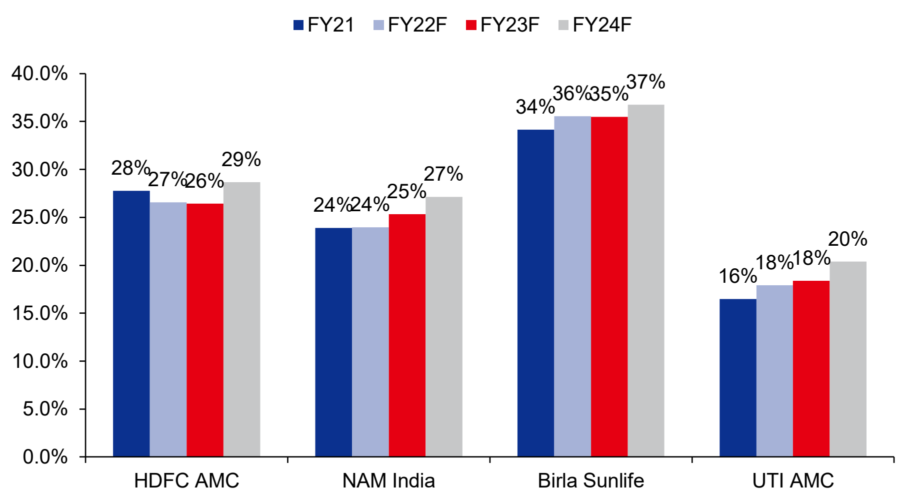


SOURCES: AMFI, INCRED RESEARCH, COMPANY REPORTS

Superior RoE is key outcome of AMC business

AMC business in general requires a gestation period and may have to fund losses till the assets under management (AUM) reach a critical size. However, once the fund house breaks even, there is huge operating leverage as fixed costs - a prime component of which is salary and wages - do not rise in the same proportion as the corpus or AUM. There is a huge non-linearity in this business without or with very little consumption of capital. Return on Equity (RoE) will be high. All this makes sense for a perfect investment decision.

Figure 30: RoE profile for AMCs remains superior



SOURCES: AMFI, INCRED RESEARCH, COMPANY REPORTS

Superior RoE will command better valuation

AMCs across the globe have been valued using differentiated methodologies. Under the income approach, one of the methodologies used to value an AMC is discounted cash flow (DCF) or price-earnings capitalisation methodology (PECV). As Indian AMCs can generate superior RoE, they are ideally able to command a better multiple. Even under the market approach, valuation multiples like value as a % of AUM remains the most relevant. AMCs with better profit margins and higher return ratios typically attract higher AUM multiples in the marketplace.

Terminal growth rate for AMCs remains high

Apart from free cash flow distributable to investors, there’s one more benefit. Most businesses offer a terminal growth rate of 5%. For AMC business, this growth rate is much higher because the assets grow not just on the back of fresh inflow but also on the back of underlying and existing corpus growing in debt as well as in equity markets based on returns of the asset class itself.

Lenders or non-lenders – what is the preferred option?

India's banking and financial services sector (BFSI), although cyclical, is a gradual long- term growth story backed by under-penetration, a consistent push for financial inclusion and rising digitalization. So, inclusion of BFSI stocks in an investor's portfolio is not only index-led requirement but also a necessity to play mid to long-term India growth story.

Diversity available in financial space for investments

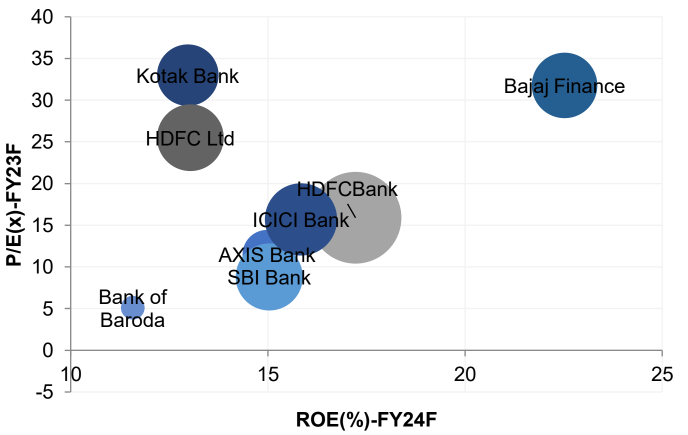
India has a diversified financial sector undergoing rapid expansion, both in terms of strong growth of existing financial services firms and new entities entering the market. The sector comprises commercial banks, insurance companies, non-banking financial companies, co-operatives, pension funds, mutual funds, and other smaller financial entities. In past few years, diversity is available for investors within the financial space, from banks and NBFCs (lender) to insurance and asset managers (non-lenders). The banking regulator has allowed new entities such as payment banks to be created recently, thereby adding to the type of entities operating in the sector.

Lenders or non-lenders – what is the preferred option?

This is the most common question as the investor is picking an investment between lenders (banks/NBFCs) and non-lenders (AMCs/insurers). Lenders are restricted over capital dilution and credit risks but are available at relatively attractive valuations. Non-lenders with limited credit risk and superior RoEs are expensively valued. However, business models may remain cyclical.

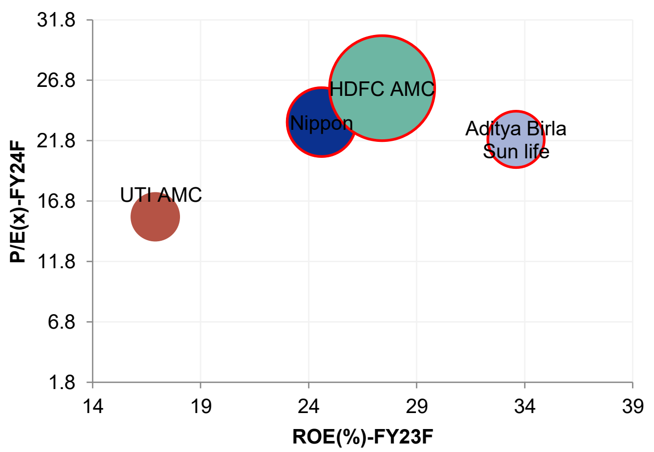
The financial sector in India is predominantly banking-dominated with commercial banks accounting for more than 64% of total assets held by the financial system. However, non-lending financial institutions have slowly and gradually grown in size and confidence in the market and are finally setting their entry into Indian capital markets. Non-lenders provide an opportunity to investors to participate in the growth arising out of changing face of Indian finance industry, sans worrying about side effects of non-performing assets or NPAs, liquidity, asset liability management or ALM and asset quality of lending players.

Figure 31: Lenders with low RoE command low P/E



SOURCES: INCRED RESEARCH, BLOOMBERG ESTIMATES, BUBBLE SIZE IS MARKET CAPITALISATION

Figure 32: Lenders with high RoE command better P/E



SOURCES: INCRED RESEARCH, BLOOMBERG ESTIMATES, BUBBLE CHART IS MARKET CAPITALISATION

Mix of the two is an ideal option with preference for better returns

Both are ideal plays for India retailisation story and an ideal mix of both is a better strategy to generate superior returns.

- Our preference for AMCs is triggered by uncertainty over profitability of lenders amid rising interest rates as global monetary tightening is a must amid elevated level of inflation.
- AMCs will also face an issue as volatility in banking stocks will ensure equity markets also getting impacted and so also to the fund flows. However, consistent awareness and educational campaigns run by AMFI as well as other regulators have made mutual funds as one of preferred mode of investment option for Indian retail customers.
- With increasing financial penetration across India, demand for mutual funds (from retail investors) is likely to grow on a steady note, despite volatility in markets and flows.
- Lastly, as regards AMCs, we prefer staying with big and better brands with diversified product portfolios and skilled investment teams which will ensure safeguarding of investor interest even during volatility.

Regulations to ensure better transparency

The Securities and Exchange Board of India (SEBI), mutual fund regulator, has been very proactive with regulatory changes to ensure the loopholes are plugged. As AMC business is yet to mature in India along with a low literacy level of Indian population regarding investment in financial instruments, especially in semi-urban and rural areas, SEBI has been very active in keeping a close eye over the overall functioning of AMCs and regulations surrounding the same.

Approval from major unit holders mandated for scheme closure

In Feb 2022, to further safeguard the interest of mutual fund investors, SEBI made it mandatory for trustees of mutual funds to obtain the consent of unit holders when most of the trustees decide to wind up a scheme. The decision to amend the regulations came after the Supreme Court's decision in a case pertaining to winding-up of Franklin Templeton Mutual Fund's six debt schemes. The move will safeguard minority holders' interest in the schemes and bring in transparency.

Mark-to-market for investments and implementation of IND-AS

SEBI has mandated mutual funds to mark all investments to market and carry investments in the balance sheet at market value. Any profit or loss arising from such transaction will be passed through revenue account, but such unrealized gains cannot be utilized for distribution. Our interactions indicate that most AMCs already follow this practice as this brings more clarity over current situation of the investment book. In addition, mutual funds have to follow Indian Accounting Standards (Ind-AS) from 2023-24 financial year onwards.

Slashing of total expense ratio for AMC schemes

In Sep 2020, SEBI announced the slashing of total expense ratio (TER) of mutual funds. This decision is attributed to bring transparency in the appropriation of expenses, curb mis-selling and churning. The decision has been taken after considering the economies of scale. The recommendations include doing away with the practice of upfront commission, introduction of reducing AUM-based trail commission, levelling commission across top-15 cities (T-15) and beyond 15-top cities (B-15) distributors and disclosing trail commission to investors at the time of sale of units.

The difference between the expenses ratio of direct and regular funds is only to the tune of distributor commission only. Such moves will keep exerting pressure on AMC managements and their investment teams to keep expenses in check and to utilise the sources available in a best possible manner.

Ban on upfront commission to distributors

In Oct 2018, SEBI banned the payment of upfront commission to distributors. Also, SEBI notified that all commissions and expenses are to be expensed from the MF scheme P&L alone and not through any other route. As per earlier practice, AMCs paid upfront commission through their own P&L, while trail commission was paid through respective schemes. The banning of upfront commission and the adoption of a full-trail model resulted in a decline in topline yields of AMCs, but they have also been accompanied by a commensurate decrease in opex.

Cap over total expense ratio (TER) for AMCs

Similarlly, SEBI announced a reduction in the maximum total expense ratio (TER) that can be charged to mutual fund schemes. This largely had a negative impact on AMCs, which operate large MF schemes (given higher TER cut for higher AuM slabs). However, most of this TER cut has been transferred to distributors. As per our interactions with HDFC AMC and NAM managements, 85-90% of TER cut has been transferred to distributors.

Key risk for AMC business

It's a cyclical business

A significant portion of AMC revenue comes from management fees charged on the assets they manage. Any decrease in AUM will cause a decline in fees and, therefore, revenue from operations and, consequently, net profit. The AUM may decline or fluctuate for various reasons, many of which are outside anyone's control. Further, in our view, these factors may inhibit AMC's ability to grow AUM which will adversely affect revenue from operations and net profit.

Revenue yield may remain under pressure

Risks to the business are a drop in expense ratio (fee that funds collect from investors), as nudged by the capital market regulator. This, coupled with the rise in brokerage commission and competition intensity among AMCs, has impacted sales and revenue yields of AMC business in recent times and this may continue in the coming period as well, in our view.

Regulatory risk

India's financial sector regulators are more customer-centric than those of other countries, and we expect regulatory intervention to prevent any loopholes in the business cycle of AMCs. SEBI, being the regulator, has imposed various restrictions on AMCs including a cap on TER, etc. In the future as well, such regulatory changes can create hurdles for AMC business. The Reserve Bank of India or RBI also plays an important role in regulating AMCs, and mutual funds need its approval if they are launching guaranteed schemes. Finally, the Ministry of Finance works as the overall authority for all these regulators.

Contribution from other income to remain volatile

More recently, as per a SEBI circular, an AMC will have to invest -- either from its net worth or from funds garnered from their sponsors – at least 0.13% of the assets under management (AUM) in a scheme with very high risk. Any profit or loss from such investment generally gets routed through other income for the P/L of AMC. Hence, we expect other income trend for AMCs to remain volatile.

Demand disruption due to Covid-related lockdowns

Retail investor remains a key participant in case of AMCs and any disruption created by the Covid-19 pandemic-induced lockdowns would be a risk to growth of new customers and profitability due to higher claims, in our view.

Competition from other financial instruments remains consistent

Investors have been gradually shifting from physical assets to financial assets. Additionally, they have also been reallocating their savings to mutual funds in recent years. However, as noted earlier, overall mutual fund penetration in India remains low. In addition, insurance products such as unit-linked investment products, which provide dual benefits of protection and long-term savings, are competing for market share.

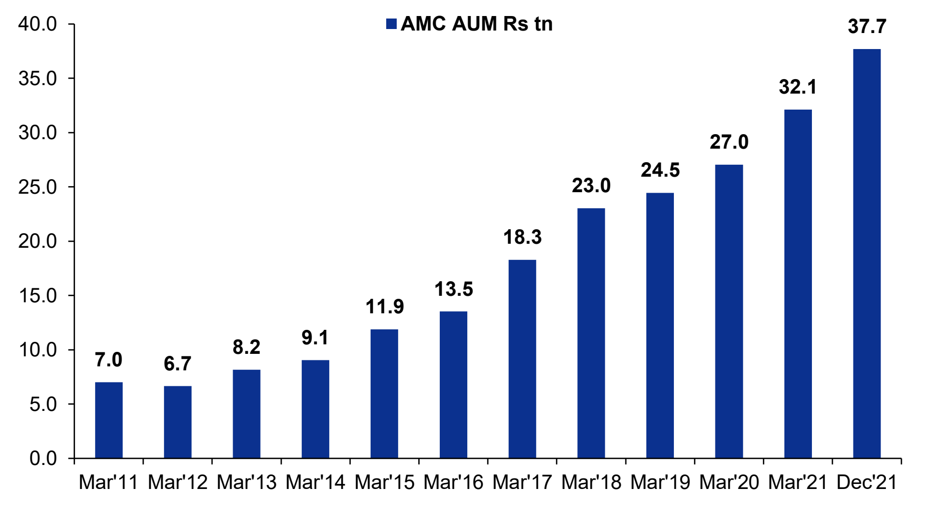
Indian AMCs
Industry profile

AMCs in India – a sustainable growth story

Indian AMCs have been witnessing gradual growth since more than two decades, post announcement of mutual fund regulations by SEBI in 1996. The industry's AUM topped the milestone of Rs10tr for the first time in May 2014 and in a short span of about three years, the AUM size increased more than two-fold and crossed Rs20tr for the first time in Aug 2017.

Industry AUM stood at Rs37.73tr as at end-Dec 2021. The total number of accounts (or folios as per mutual fund parlance) as at end-Dec 2021 stood at 12.02 crore (120.2m), while the number of folios under equity and hybrid schemes, with maximum investment from retail segment is at about 9.74 crore (97.4m).

Figure 33: AMC AUM in India (Rs tr)

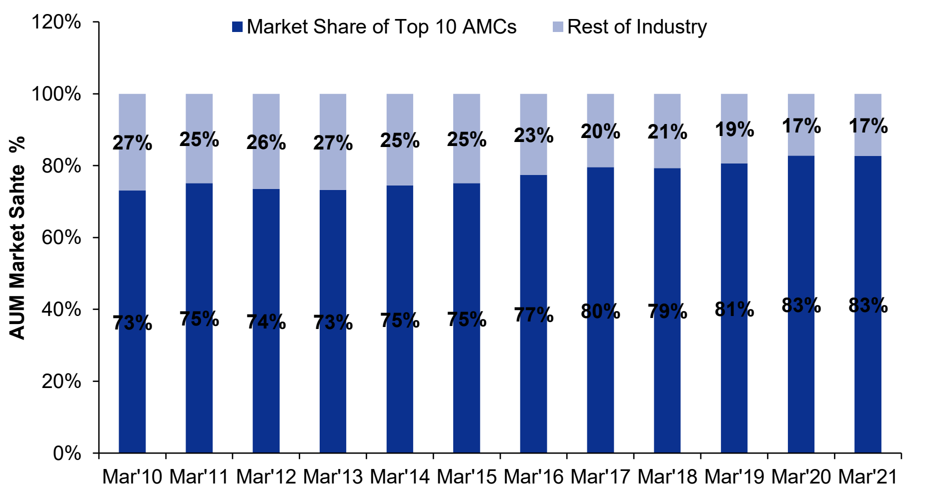


SOURCES: AMFI, INCRED RESEARCH, COMPANY REPORTS

Concentrated market with consistent consolidation

Indian AMC industry continues to be dominated by domestic players of which many are associated with banks along with some domestic business houses having strong brands built in other fields of business The mutual fund industry continues to be concentrated. The top 10 AMCs collectively command more than four-fifths of mutual fund industry's assets.

Figure 34: Top 10 AMCs accounted for ~83% of total industry AUM as at end-Mar 2021

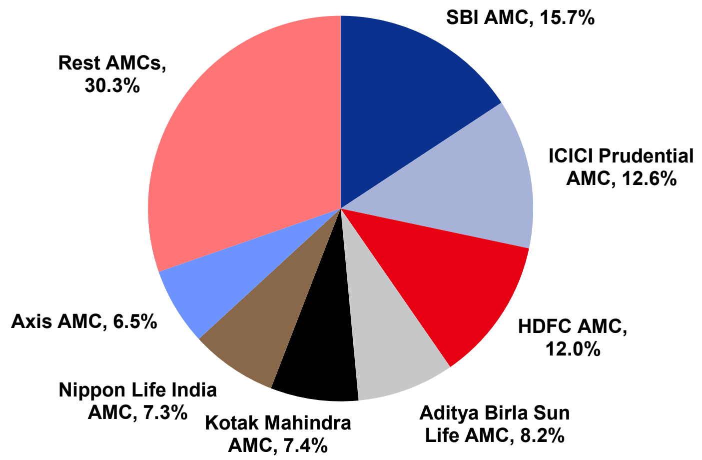


SOURCES: AMFI, INCRED RESEARCH, COMPANY REPORTS

Large seven AMCs account for ~70% of industry AUM as at Dec 2021-end

As at Dec 2021-end, the number of active AMCs stood at 45, while AUM share of top-7 AMCs was ~70% of average AUM.

Figure 35: AMC market share as at end-Dec 2021



SOURCES: AMFI, INCRED RESEARCH, COMPANY REPORTS

Exit of foreign players led to a rise in domestic AMCs' dominance

While the industry has seen an increase in the number of mutual fund players, it has also undergone consolidation. With profits skewed towards large fund houses, many M&As were witnessed over the past decade. Most of the deals have been by way of acquisition due to consistent exit by foreign players, whose stakes were bought out by domestic companies.

Figure 36: Consolidation of fund houses in recent years

	Year	Fund house exited	Merged with	% of Industry AUM (on year of exit)
1	2012	FIL Fund Management	L&T Investment Management	1.31%
2	2013	Daiwa Asset Management	SBI AMC	0.03%
3	2014	ING Investment Management	Aditya Birla Sun Life AMC	0.06%
4	2014	Pine Bridge Mutual Fund	Kotak Mahindra AMC	0.07%
5	2014	Morgan Stanley Investment Management	HDFC AMC	0.28%
6	2015	Goldman Sachs Asset Management	Nippon India AMC	0.68%
7	2015	Deutsche Bank Asset Management	DHFL Pramerica Asset Managers	1.89%
8	2016	JP Morgan Asset Management	Edelweiss Asset Management	0.47%
9	2019	DHFL Pramerica Asset Managers	PGIM India Asset Management	0.31%
10	2021	BNP Paribas Asset Management	Baroda Asset Management	0.24%

SOURCES: AMFI, INCRED RESEARCH, COMPANY REPORTS

Similarly, new entrants will aid expansion of overall market

There are many new entrants coming into the MF space such as Zerodha, NJ, Samco, White Oak, etc. New players coming into the industry help the industry grow and go to the next level. Expansion will happen with more players coming in as MFs are still heavily underpenetrated.

The major reasons behind the rise of new MFs are their potential to raise generous returns, relatively lower fees, innovative products, and the adoption of technology for easier facilitation. These new mutual funds' only aim is to acquire market share and put together great value for their investors However, like in previous years, the consolidation phase is expected to continue whereby some players will exit and some will consolidate and merge with larger players.

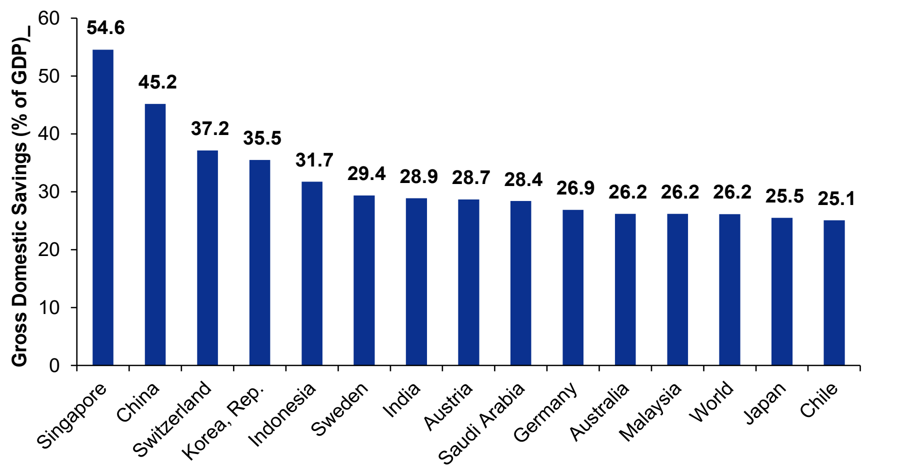
Financialization of savings aids growth

Indian AMCs have witnessed ~21% CAGR in AUM over last five years (FY16-21), highest globally, as per AMFI mainly aided by rising preference for financial assets within household savings, greater access to information, and increasing reach to smaller cities and towns.

India remains in top bucket in domestic savings

Among global economies, India's has one of the highest savings rates (gross savings-to-GDP), at ~28.4% (as at FY20-end). With the rise in India's GDP over time, Indian household savings also witnessed a surge. As India lacks government support in respect of education, health and unemployment/retirement benefits, Indian households tend to save more to meet uncertainties.

Figure 37: India's domestic savings as a % of GDP remained high in FY20

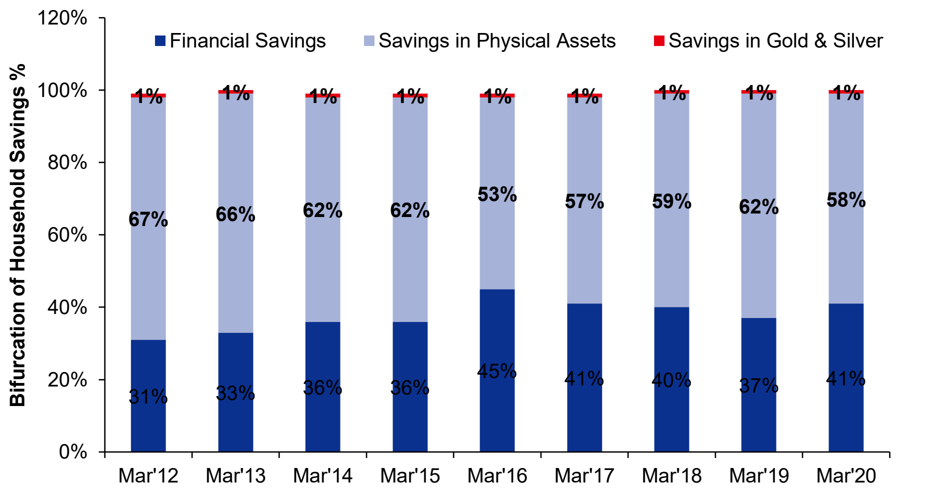


SOURCES: RBI, INCRED RESEARCH,

A clear switch from physical assets to financial assets is visible

Capital markets are expected to remain an attractive part of financial savings. While household savings in physical assets declined to 58% in FY20 from 67% in FY12, financial savings grew to 41% in FY20 from 31% in FY12, as per RBI. Along with an increase in financial literacy, and relative outperformance of financial assets in recent years, the share of financial assets as a proportion of net household savings is set to increase over the years. The rise in financial assets is expected to further boost investments in mutual funds.

Figure 38: Bifurcation of household savings

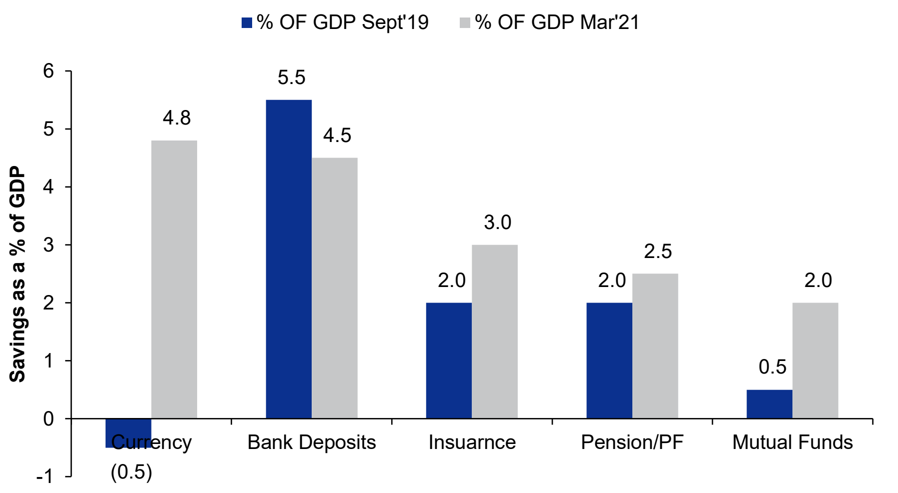


SOURCES: RBI, INCRED RESEARCH

Rise in MF investments is evident in supporting AMCs' AUM

The increase in household financial assets was led by a significant increase in households' holdings of mutual funds, insurance products and currency. Households' investments in mutual funds increased to 1.7% of gross domestic product or GDP in 1QFY21 from 0.2% in 1QFY20 whereas in insurance products they are estimated to have increased to 3.3% in 1QFY21 from 2.3% in 1QFY20, as per IRDAI (Insurance Regulatory and Development Authority of India).

Figure 39: Movement in savings as a % of GDP



SOURCES: RBI, INCRED RESEARCH

The increased flows to mutual funds seem to have been driven by low returns on bank deposits and the rise in stock market returns. Additionally, investor awareness programmes as well as product innovations from AMCs such as systematic investment plans (SIPs) supported growth in AMC flows.

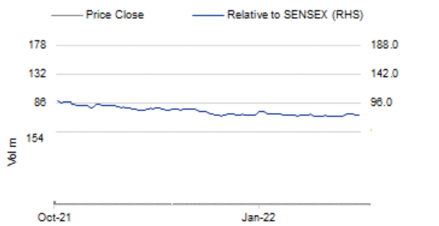
India

ADD *(Initiating coverage)*

Consensus ratings*:	Buy 7	Hold 0	Sell 0

Current price:	Rs500
Target price:	Rs650
Previous target:	NA
Up/downside:	30.0%
EIP Research / Consensus:	-14.9%
Reuters:	
Bloomberg:	ABSLAMC IN
Market cap:	US$1,889m
	Rs143,870m
Average daily turnover:	US$0.0m
	Rs0.0m
Current shares o/s:	288.0m
Free float:	46.0%

**Source: Bloomberg*



Source: Bloomberg

Price performance	1M	3M	12M
Absolute (%)	(5.4)	(14.1)	0.0
Relative (%)	0.3	(8.9)	0.0

Major shareholders	% held
Aditya Birla Capital	50.0
Snl life	37.0
Public	13.0

Aditya Birla Sunlife AMC

Focus on Equity Flows, AUM to see diversity

- ABSL AMC, in our view, is geared up for reshuffling in AUM with equity and alternative funds (incl. ETFs) registering a surge backed by retail participation.
- We are factoring in ~20.6% CAGR in PAT over FY21-24F backed by gradual improvement in yields coupled with operating efficiency supporting profits.
- Initiate coverage with Add rating and TP of Rs650 based on dividend discount model, corresponding to ~20.7x P/E at FY24F EPS & ~4.4% FY24F AUM.

Gearing up for equity/ETF flows, dominance in debt schemes in place

Aditya Birla Sunlife (ABSL) AMC, the fourth-largest AMC in India, (~7.7% market share based on QAAUM as at end Dec 21) enjoys a dominant position in fixed-income segment backed by its diversified product offerings, superior track record and strong corporate relationships. However, like most peers, ABSL has been losing market share in equity schemes. More recently, ABSL AMC's management has introduced a couple of schemes in equity and ETFs and the focus has been rising over sticky retail inflows through low-ticket SIPs. The company is investing in digital infrastructure to smoothen the on-boarding process and deepen penetration in B-30 cities (beyond Top-30 cities). We remain confident of the measures and expect a surge in equity AUM (including ETFs) in coming years.

Alternative products to regain momentum and aid further profitability

In addition to MF business, ABSL AMC offers variety of alternative products like PMS, AIF, offshore and real estate products to HNIs and institutional investors. The AMC has witnessed a drawdown in these funds in past years however with diversity attracting the investors (amid uniform returns in MF schemes), the management is now prepared to grab the opportunity and expand these segments. The AMC already has Rs20bn under PMS with improving traction.

Steady profitability: dividend payouts to improve

ABSL AMC has reported ~19.8% CAGR growth in profits over FY16-21 backed by better operating efficiency and surge in treasury income as revenue yields, like peers, have witnessed a dip. Going ahead, we are factoring in gradual recovery in revenue yields amid regulatory pressures, yet superior operating leverage to support profitability with ~20.6% CAGR growth over FY21-24F.

Initiate coverage with Add rating and TP of Rs650

On comparing listed AMCs, based on price/earnings to RoE multiple, we observe that Aditya Birla Sunlife AMC (ABSL) is attractively placed compared to peers. We initiate coverage on ABSL with Add rating and a TP of Rs650, based on the dividend discount model, corresponding to ~20.7x P/E at FY24F EPS and ~4.4% of FY24F AUM. Our target price is based on the assumptions of cost of equity at 11.7% and a terminal growth rate of 5%. Key downside risks: Low traction in new funds, branding risk and industry-related risks.

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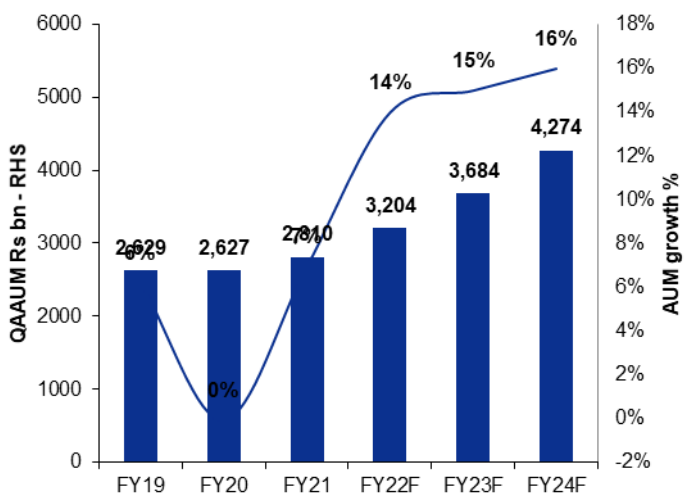
Financial Summary	Mar-20A	Mar-21A	Mar-22F	Mar-23F	Mar-24F
Total Non-Interest Income (Rsm)	12,147	11,779	14,002	15,979	18,646
Operating Revenue (Rsm)	12,147	11,779	14,002	15,979	18,646
Net Profit (Rsm)	4,859	5,157	6,678	7,709	9,038
Core EPS (Rs)	16.87	17.91	23.19	26.77	31.38
Core EPS Growth	(93%)	6%	29%	15%	17%
FD Core P/E (x)	29.61	27.90	21.54	18.66	15.92
DPS (Rs)	183.33	77.78	11.59	17.40	23.54
Dividend Yield	36.70%	15.57%	2.32%	3.48%	4.71%
BVPS (Rs)	45.7	59.2	75.2	84.5	92.4
P/BV (x)	10.93	8.44	6.65	5.91	5.41
ROE	38.3%	34.1%	34.5%	33.5%	35.5%
% Change In Core EPS Estimates					
InCred Research/Consensus EPS (x)			1.08	1.13	1.19

SOURCES: INCRED RESEARCH, COMPANY REPORTS

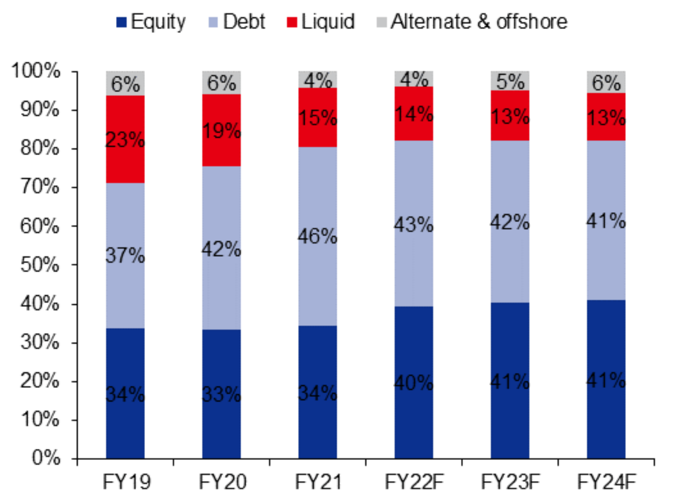
ABSL AMC- key charts

Figure 40: Retail-driven AUM momentum to continue



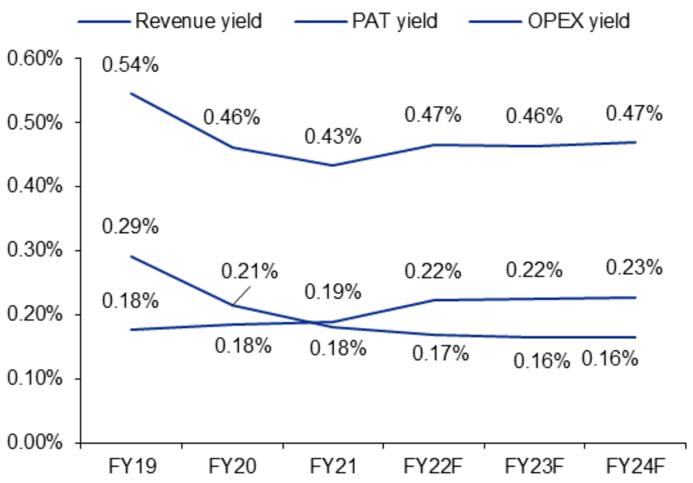
SOURCES: INCRED RESEARCH ESTIMATES, COMPANY REPORTS

Figure 41: Diversified AUM mix with a rising share of equity funds



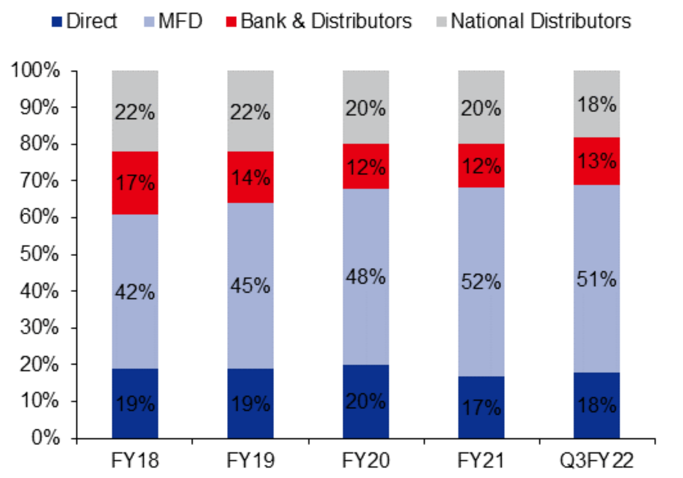
SOURCES: INCRED RESEARCH ESTIMATES, COMPANY REPORTS

Figure 42: Steady PAT led by healthy operating efficiency



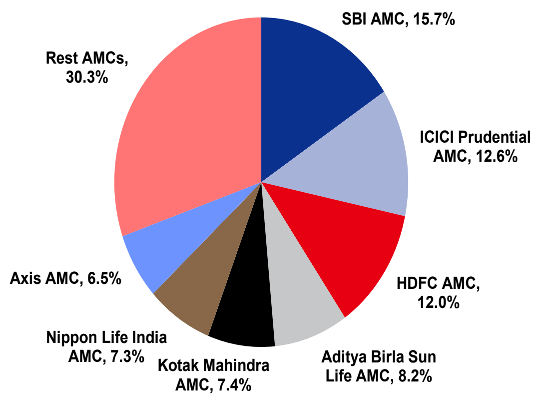
SOURCES: INCRED RESEARCH ESTIMATES, COMPANY REPORTS

Figure 43: MFD remains a key contributor to distribution



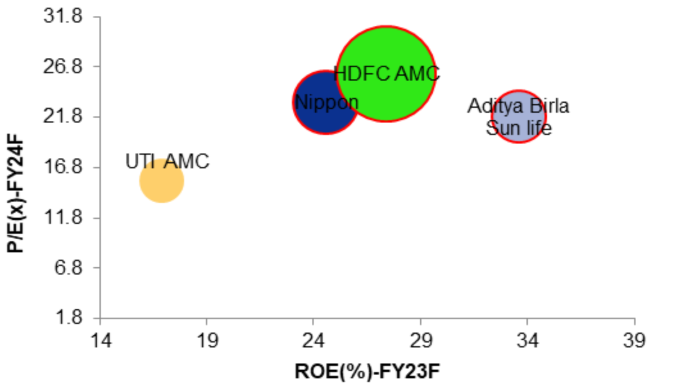
OURCES: INCRED RESEARCH, COMPANY REPORTS

Figure 44: ABSL AMC is fourth-largest AMC in India (on AUM basis) as at end-Dec 2021



SOURCES: AMFI, INCRED RESEARCH

Figure 45: ABSL AMC is favorably placed compared to peers



SOURCES: INCRED RESEARCH, COMPANY REPORTS, BLOOMBERG ESTIMATES

Largest non-bank AMC, dominance in debt

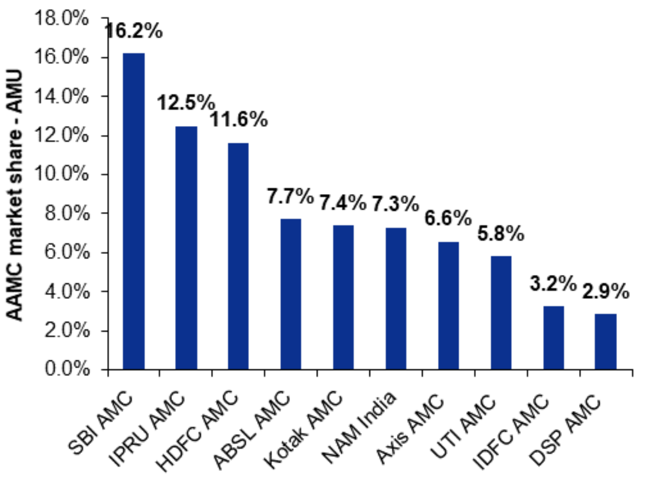
ABSL AMC is the fourth-largest AMC in India, and largest non-bank affiliated AMC in the country, with ~7.7% market share as at end-Dec 21 based on average AUM (QAAUM), as per AMFI. In mutual fund or MF business, the company has built a highly dominant position in fixed-income assets due to its strong corporate relationships, but more recently, we have witnessed a surge in equity funds in overall AUM. The company also managed an alternate asset business, which includes PMS, AIFs, real-estate funds, offshore funds, etc. Currently, the contribution from this segment is not meaningful, but we expect a steady revival over FY21-24F

The company has a large pan-India network of empanelled distributors with a presence in 280+ locations, 69,000+ KYD-compliant mutual fund distributors (MFDs), 240+ national distributors and 100+ bank partners. The company also has strategic tie-ups with more than 70 fintech firms for distribution of its products.

Debt-driven AUM growth; pandemic hits growth

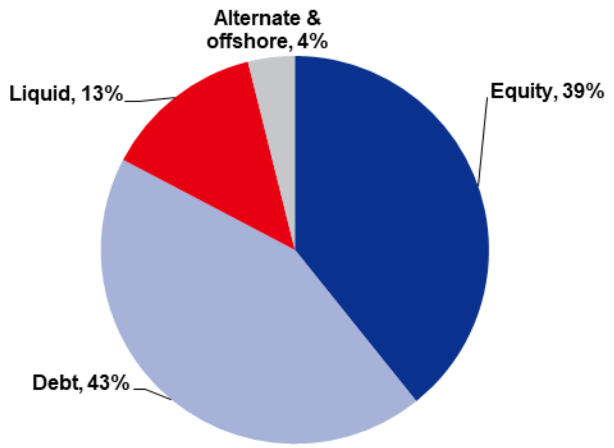
The company's AUM grew at a ~3.4% CAGR over FY19-21 with the proportion of debt AUM growing at ~14.8% CAGR, at ~46% of overall AUM, indicating debt fund dominance for the company. However, we have witnessed a sharp surge in equity fund AUM during 9MFY22, backed by MTM gains in equity portfolio as well as rising retail participation (including through SIPs), primarily towards equity fund AUM. This has resulted in a surge in equity fund AUM to ~39% as at Dec 2021-end.

Figure 46: ABSL AMC is the fourth-largest AMC in India, as per AMFI



SOURCES: AMFI, INCRED RESEARCH, COMPANY REPORTS

Figure 47: AUM bifurcation as at end-Dec 2021



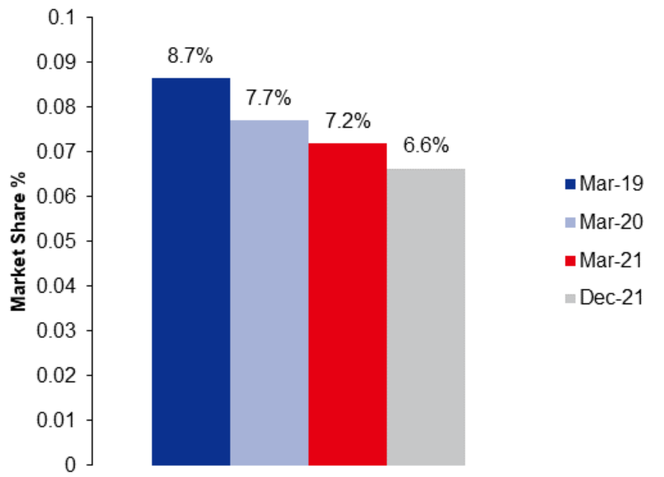
SOURCES: AMFI, INCRED RESEARCH, COMPANY REPORTS

Regaining market share in debt funds, but struggle in equity funds continues

Unlike certain businesses in the financial services space, asset management by its nature tends to be much more volatile, especially in the short term as it is highly correlated with equity markets. The recent pandemic (Covid-19) has initially impacted overall flows for AMCs across India along with MTM losses in equity due to a sharp correction in markets, but gradually AMCs managed to regain the lost momentum.

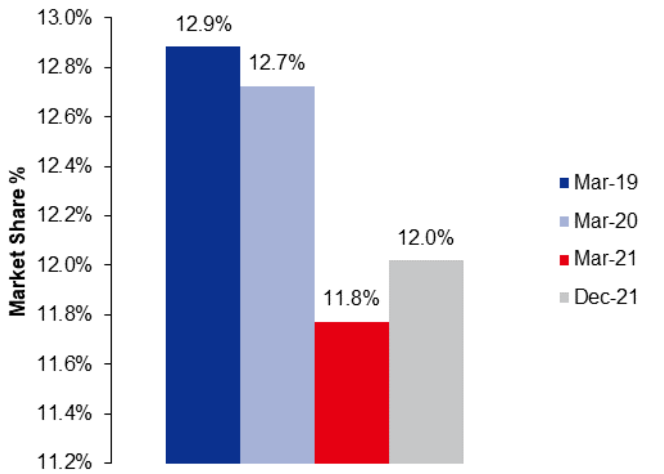
All AMCs did see a contraction in their equity fund AUM in Mar 2020 due to the steep fall in equity markets, triggered by the suddenness of the pandemic and the resultant nation-wide lockdown. However, with the pandemic reinforcing the importance of financial savings among Indian households and given the under-penetration of mutual funds, the outlook remains promising.

Figure 48: Market share loss in equity funds continues



SOURCES: AMFI, INCRED RESEARCH, COMPANY REPORTS

Figure 49: Market share in debt funds stabilizes



SOURCES: AMFI, INCRED RESEARCH, COMPANY REPORTS

ABSL AMC has gradually regained market share in debt funds with a share of ~12% as at end-Dec 21 against ~12.9% as at end Dec-19. Unique product basket along with a deep relationship with corporate segment has always been a key feature of ABSL AMC's fixed-income division.

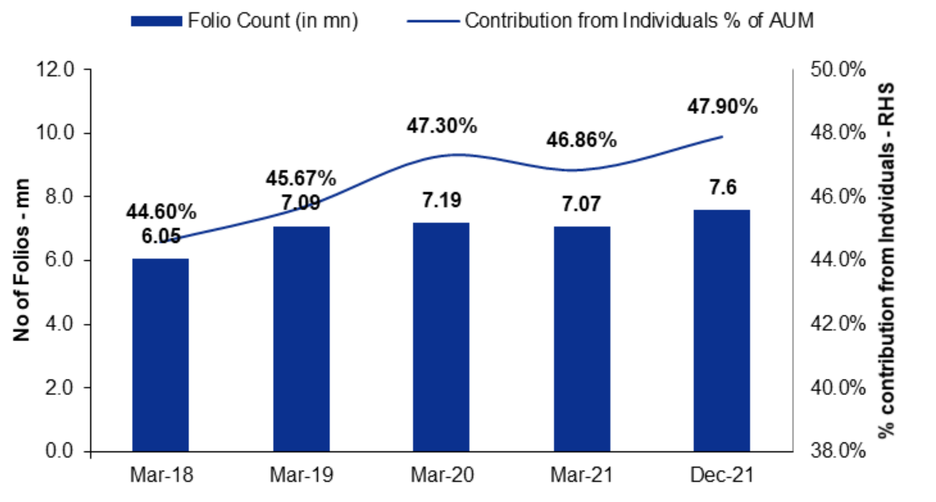
On equity fund flows front, despite the rise in overall equity AUM, ABSL AMC has been losing market share with its overall market share at ~6.6% in Dec 2021 as against ~8.7% in Mar 2019. Equity flows were impacted due to several reason including underperformance of large equity fund schemes as well as an extremely competitive landscape which has tilted overall equity flows towards its rivals.

Management is committed to improve equity fund market share by increasing equity fund inflows, especially from retail investors. The investment team has been focusing on improving the performance of individual schemes to attract incremental flows.

Retail to drive growth, targeting sticky AUM

The aftermath of the past one year has geared up ABSL management's focus towards the need for investments to aid long-term life savings. Management has re-built its diversified solution suite with active and passive strategies across equity and fixed income, considering market cycles and investors of all kinds. Retail customers, being primarily under focus, various fund launches in muti-cap and mid-cap segments have also been done to attract retail inflows.

Figure 50: Growing retail folios with a rising share of individuals in overall AUM



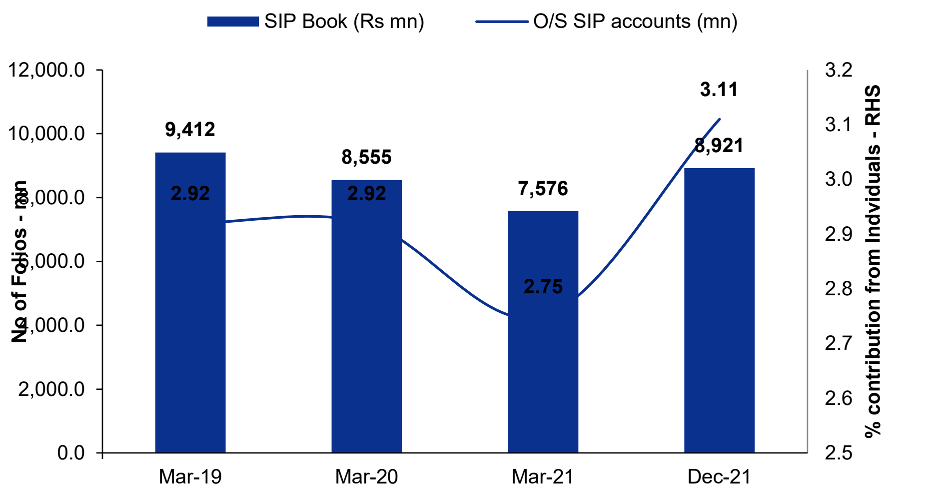
SOURCES: INCRED RESEARCH, COMPANY REPORTS

SIP improvement holds the key for retail momentum

ABSL AMC is focusing on strengthening its retail franchise by increasing its market share in B-30 cities (beyond Top-30 cities) by increasing its presence, building SIP book and addition of new folios.

Systematic investment plan (SIP) AUM for ABSL AMC has increased from Rs252.5bn as at end-Mar 2020 to Rs418.4bn as at end-Mar 2021 to Rs501bn as at end-Dec 2021. Despite the pandemic, the company was still able to register 0.63m SIPs in FY21, which is around 85% of the previous financial year's number.

Figure 51: SIP contribution is on the rise

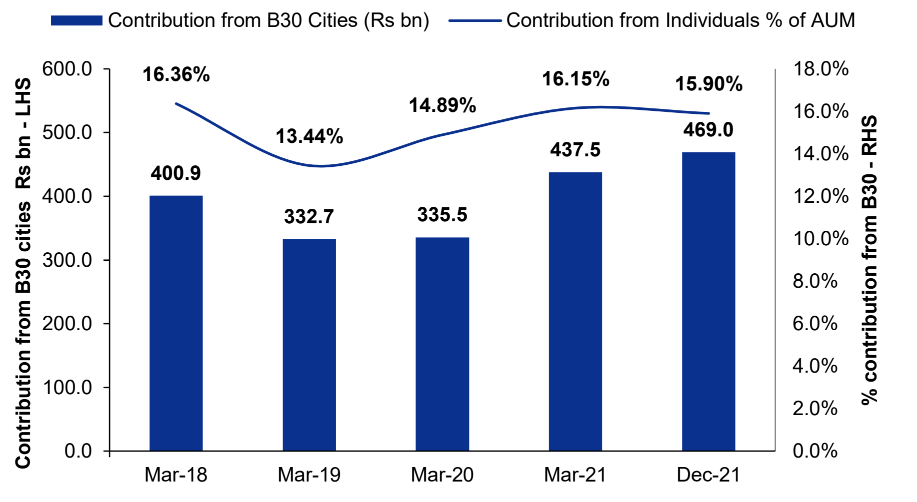


SOURCES: INCRED RESEARCH, COMPANY REPORTS

B-30 cities' contribution is on the rise

Like most peers, ABSL has also witnessed the traction normalising from B-30 cities (beyond Top-30 cities). Interestingly, overall AUM is growing at a slower pace compared to the rise in folios counts, which is an indicator of lower average ticket size for SIPs. This trend will ensure more stickiness of the flows, even in case of a volatile market trend.

Figure 52: SIP flow and count have witnessed an improvement during FY21 & 9MFY22



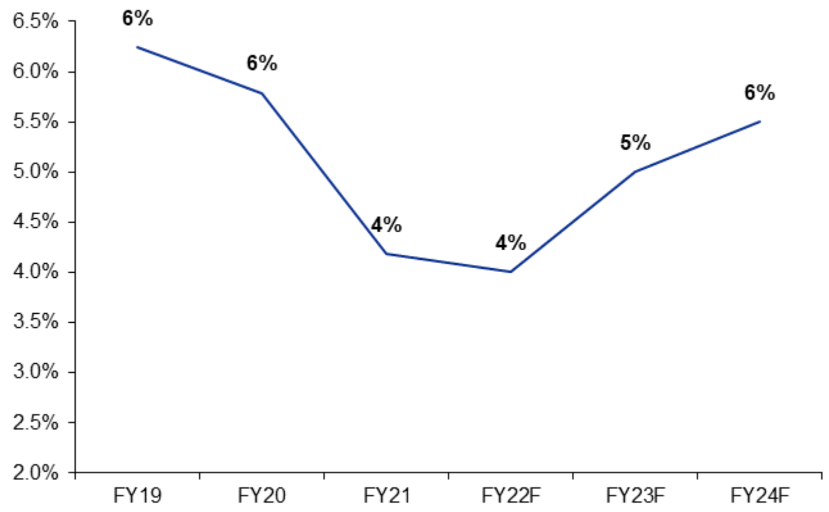
SOURCES: INCRED RESEARCH, COMPANY REPORTS

Post Covid-19 pandemic, ABSL AMC is witnessing improved traction in sticky retail flows through low-ticket SIPs. Going ahead, management intends to launch schemes catering to the needs of a diversified retail customer base, investing in digital infrastructure to smoothen overall customer on-boarding process and deepening penetration in B-30 cities. We remain confident of a resurgence in equity fund dominance for the company in coming years.

Alternative products to regain momentum

In addition to MF business, ABSL AMC offers alternate products to HNIs and institutional investors. The company offers PMS, AIF, offshore and real estate products to its customers. This was a quite successful mode of AUM for the AMC till a few years ago, but due to underperformance of a few schemes as well as an adverse interest rate cycle there was a sharp decline in alternative AUM.

Figure 53: The share of alternative products is expected to rise



SOURCES: INCRED RESEARCH ESTIMATES, COMPANY REPORTS

PMS/offshore/real estate in focus under alternative products

ABSL AMC has categorically identified a few areas of growth under alternative products including, but not restricted to PMS/offshore funds and passive funds.

- The company already has a corpus of Rs20bn under PMS, which we expect to double in next 3-4 of years.
- On offshore funds, the company aims to grow its offshore equity AUM by expanding into new geographies such as the United States, the United Kingdom and Europe, and it is also developing new real-estate scheme launches.
- Like peers, ABSL AMC intends to focus on gaining market share in passive investment products such as ETFs, index funds etc. Towards achieving this goal, it has already launched seven index funds with 16 products already in the pipeline.
- More recently, the AMC launched India's first silver ETF + FOF combo in Jan 2022.
- The company will target HNIs, pension trusts and insurance companies through registered investment advisors, brokers, digital distribution platforms and direct channels.

PMS/offshore/real estate in focus under alternative products

ABSL AMC, through these efforts, in our view, is likely to witness a surge in equity fund and alternative fund flows whereas fixed-income products will register a muted growth momentum over FY21-24F.

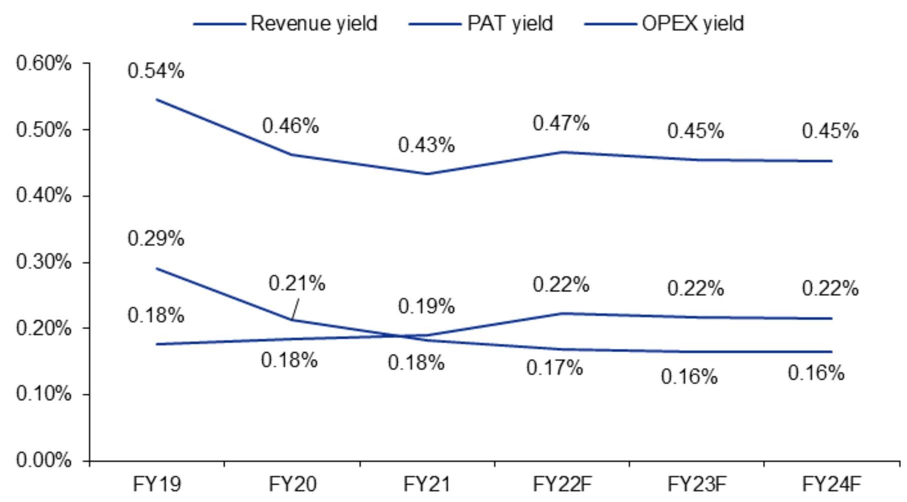
Steady profitability: div payouts to improve

ABSL AMC has reported ~19.8% CAGR in profits over FY16-21 backed by better operating efficiency and support from treasury income as revenue yields, like peers, have witnessed a dip. Going ahead, we are factoring in muted revenue yields amid pressure on equity yields, but consistent operating leverage will support profitability which is likely to rise by ~17% CAGR over FY21-24F.

Limited scope for further improvement in profit yields

ABSL AMC, backed by superior operating leverage, has managed to witness an improvement in profitability. Going ahead, we do not expect any major change in operating expenses as most of the lever has already been utilised. We forecast flat PAT yields in coming years.

Figure 54: Trend in profitability

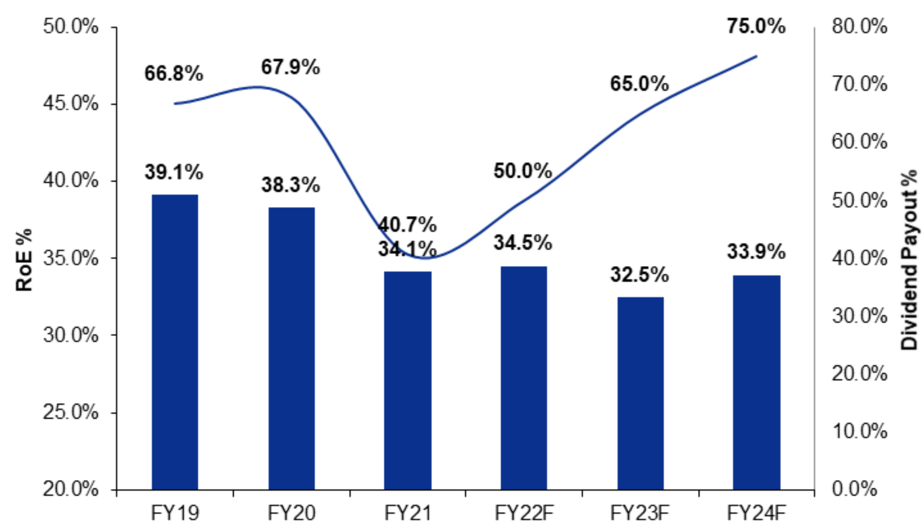


SOURCES: INCRED RESEARCH ESTIMATES, COMPANY REPORTS

However, linear capital structure allows better dividend payouts

As per the AMC's model, which requires minimum additional capital, we expect ABSL AMC's management to maintain superior RoE due to the low-cost structure and improved dividend payouts in coming years.

Figure 55: Rise in RoE to support elevated payouts



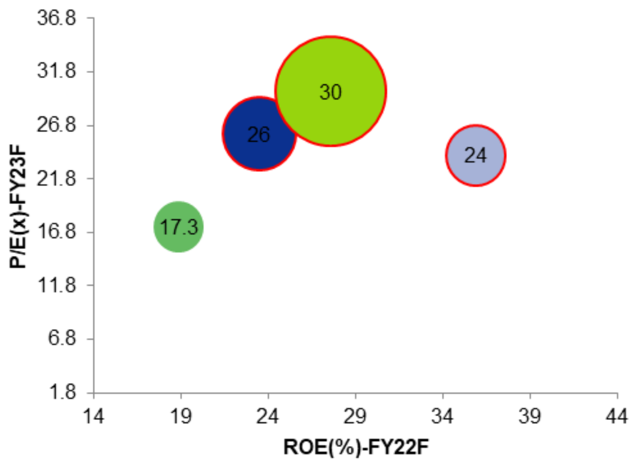
SOURCES: INCRED RESEARCH ESTIMATES, COMPANY REPORTS

Outlook & valuations

We have plotted all listed AMCs, based on their forward ROEs, on a valuation table. We are considering one-year and two-year forward multiples to assess valuation premium or else discounting of all listed players.

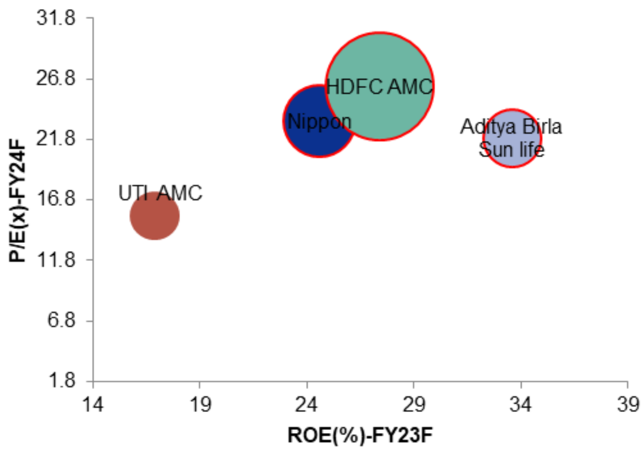
Comparison based on P/E to RoE basis

Figure 56: RoE in FY22F compared to FY23F P/E



SOURCES: BLOOMBERG, INCRED RESEARCH ESTIMATES

Figure 57: RoE in FY23F compared to FY24F P/E



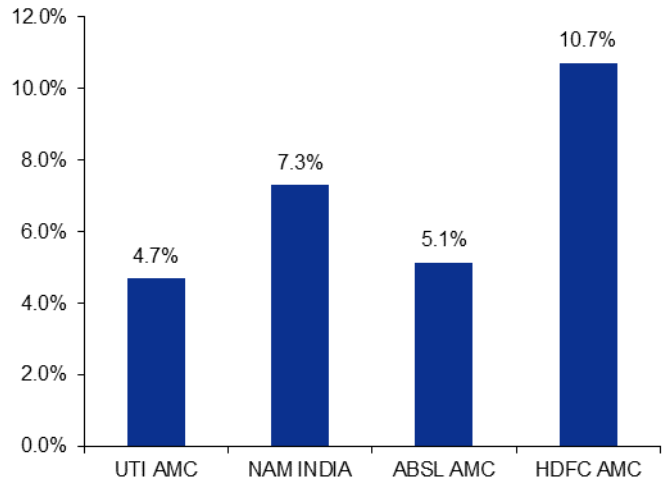
SOURCES: BLOOMBERG, INCRED RESEARCH

Trades below the trend line, risk-reward favourable

On comparing listed AMCs, based on price/earnings and RoE multiple, we observe that Aditya Birla Sunlife AMC (ABSL) is better placed compared to peers. We see a probable expansion in multiple for ABSL AMC.

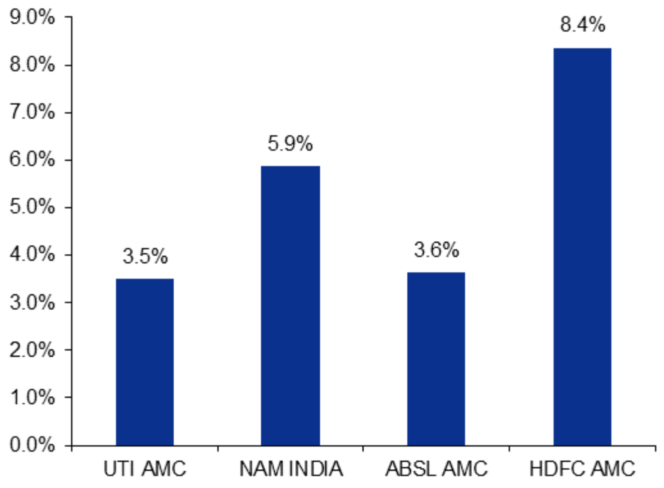
Market capitalisation as a % of AUM

Figure 58: Current market cap to 3QFY22 AUM (%)



SOURCES: INCRED RESEARCH, COMPANY REPORTS

Figure 59: Current market cap to FY24F AUM (%)



SOURCES: INCRED RESEARCH, COMPANY REPORTS

We initiate coverage on ABSL with Add rating and a TP of Rs650, based on the dividend discount model, corresponding to ~20.7x P/E at FY24F EPS and ~4.4% of FY24F AUM. We have assumed cost of equity at ~11.7% and terminal growth of ~5%.

Our assumption of cost of equity at 11.7% is based on a risk-free rate of 6%, risk premium of 6% and beta of 0.9. We have taken terminal growth as 5%, which is the expected perpetual growth rate of India's GDP.

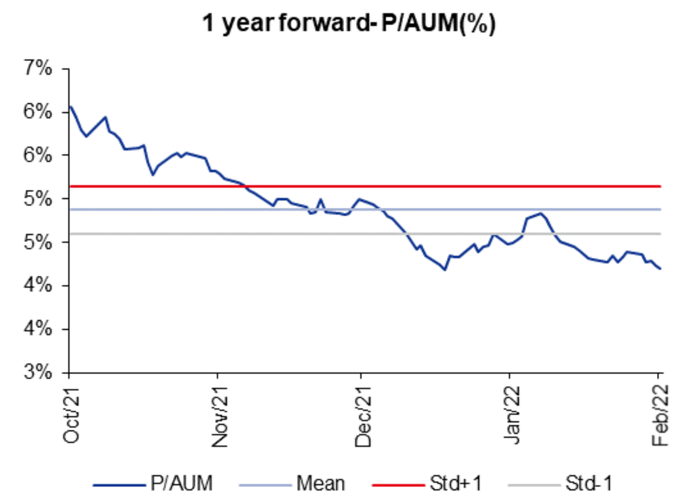
Figure 60: Valuation of ABSL AMC

Valuation	
Cost of Equity(%)	11.7
Dividend Payout ratio(%)	85%
Terminal Growth(%)	5%
Present value of Free cash flow(Rsmn)	1,86,800
Outstanding shares(mn)	288
Target Price Per share(Rs)	649
EPS(Rs)	30
P/E(x)	22

SOURCES: INCRED RESEARCH ESTIMATES, COMPANY REPORTS

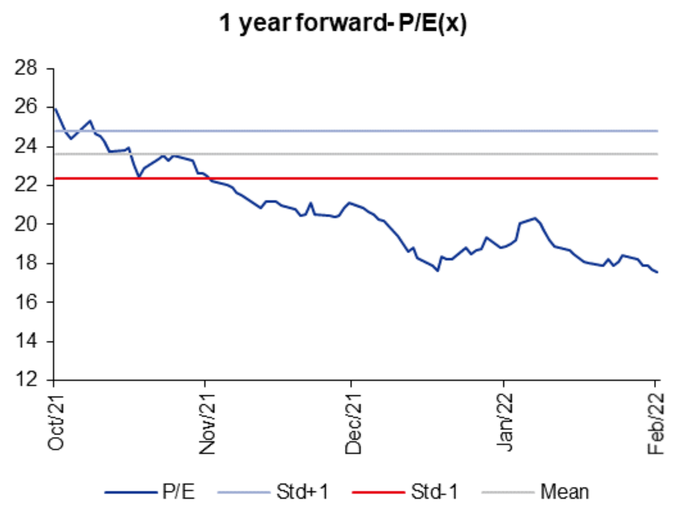
Historical valuation of ABSL AMC

Figure 61: One-year forward P/AUM with standard deviation



SOURCES: INCRED RESEARCH, COMPANY REPORTS

Figure 62: One-year forward P/E with standard deviation



SOURCES: INCRED RESEARCH, COMPANY REPORTS

Peer comparison

Figure 63: Peer comparison

Indian Peers	BBG ticker	Rating	Closing Price (LC)	Target Price	Mcap (US$ bn) Current	AUM(US$bn) FY22F	AUM(US$bn) FY23F	PAT (US$m) FY22F	PAT (US$m) FY23F	P/E FY22F	P/E FY23F
Nippon Life	RNAM	Add	300	380	2.7	38	38	103	115	27	24
HDFC AMC	HDFCAMC	Hold	2,082	2,300	6.3	60	60	189	203	33	31
AB AMC	ABSLAMC	Add	500	650	2.0	42	47	92	111	21	18
UTI AMC	UTIAM	Add	847	1,100	1.5	31	35	78	88	19	17

SOURCES:INCRED RESEARCH ESTIMATES, BLOMBERG, PRICES AS ON 4TH MAR 22:

Risks to our investment thesis

Low traction in new equity funds and ETF funds

ABSL AMC is going to launch various new products related to equity funds and ETFs to complete is product basket. However, in our view, due to a volatile market these new funds may see lower customer traction, leading to lower growth.

Dent to brand image

ABSL AMC, despite being a non-banking AMC, is able to gain significant market share due to the strong brand of Aditya Birla Group. Any adverse news on other companies of the group can led to lower fund flows, in our view.

Higher marketing and customer acquisition cost can dent profitability

ABSL AMC doesn't have the parentage of a bank, like other bank-led AMCs, as a result of which it may need to spend more on customer acquisition which could led to a deterioration in its profitability.

Underperformance in equity funds may lead to market share loss

ABSL AMC has not witnessed market share loss so far due to underperformance of its funds, but any underperformance of its funds from now on can result in a steep market share loss, in our view.

Industry-related risk

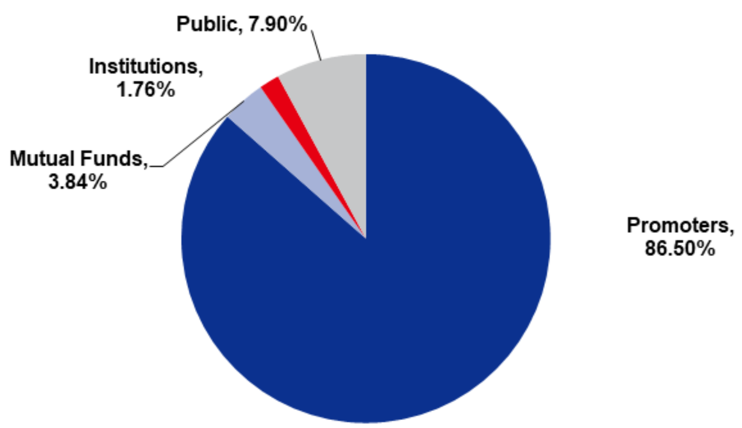
Like other AMCs, ABSL AMC is exposed to the risk of lower inflows due to any downcycle, pressure on yields because of a drop in its expense ratio, and the risk of regulatory intervention.

Figure 64: Key management profile as at end-Dec 2021

Name	Designation	Background
Kumar Mangalam Birla	Non-Executive Chairman	Mr. Kumar Mangalam Birla is Non-Executive Chairman of the company. He is also Chairman of the US$41bn multinational Aditya Birla Group and Chairman on the boards of all major group companies in India and globally, such as, Hindalco Industries Limited, Grasim Industries Limited, Vodafone Idea Limited, Aditya Birla Capital Limited, and Century Textiles Limited.
A. Balasubramanium	MD & CEO	Mr. A. Balasubramanian is Managing Director and Chief Executive Officer and has been associated as an employee of the company since 1994. He has completed advanced management programmes from IIM, Bengaluru and Harvard Business School. In 2016-18, he was appointed as Chairman of the AMFI board.
Mahesh Patil	CIO	He is an engineer and CFA, having more than 18 years of experience in equities
Bhavdeep Bhatt	Head-Retail sales	He has 21 years of experience in the finance domain and has served leading AMCs in India before joining ABSL AMC in 2009

SOURCES: INCRED RESEARCH, COMPANY REPORTS

Figure 65: Shareholding pattern as at end-Dec 2021



SOURCES: INCRED RESEARCH, COMPANY REPORTS

BY THE NUMBERS

Profit & Loss

(Rsm)	Mar-20A	Mar-21A	Mar-22F	Mar-23F	Mar-24F
Net Interest Income					
Total Non-Interest Income	**12,147**	**11,779**	**14,002**	**15,979**	**18,646**
Operating Revenue	12,147	11,779	14,002	15,979	18,646
Total Non-Interest Expenses	**(5,265)**	**(4,562)**	**(4,717)**	**(5,310)**	**(6,182)**
Pre-provision Operating Profit	6,522	6,853	8,940	10,306	12,083
Total Provision Charges					
Operating Profit After Provisions	6,522	6,853	8,940	10,306	12,083
Pretax Income/(Loss) from Assoc.					
Operating EBIT (incl Associates)	6,522	6,853	8,940	10,306	12,083
Non-Operating Income/(Expense)					
Profit Before Tax (pre-EI)	6,522	6,853	8,940	10,306	12,083
Exceptional Items					
Pre-tax Profit	6,522	6,853	8,940	10,306	12,083
Taxation	(1,663)	(1,696)	(2,262)	(2,597)	(3,045)
Consolidation Adjustments & Others					
Exceptional Income - post-tax					
Profit After Tax	4,859	5,157	6,678	7,709	9,038
Minority Interests					
Pref. & Special Div					
FX And Other Adj.					
Net Profit	4,859	5,157	6,678	7,709	9,038
Recurring Net Profit					

Balance Sheet

(Rsm)	Mar-20A	Mar-21A	Mar-22F	Mar-23F	Mar-24F
Total Gross Loans					
Liquid Assets & Invst. (Current)					
Other Int. Earning Assets					
Total Gross Int. Earning Assets					
Total Provisions/Loan Loss Reserve					
Total Net Interest Earning Assets					
Intangible Assets					
Other Non-Interest Earning Assets	**15,254**	**19,280**	**23,646**	**26,906**	**29,392**
Total Non-Interest Earning Assets	**15,254**	**19,280**	**23,646**	**26,906**	**29,392**
Cash And Marketable Securities	466	565	938	612	703
Long-term Investments					
Total Assets	15,720	19,846	24,585	27,518	30,095
Customer Interest-Bearing Liabilities					
Bank Deposits					
Interest Bearing Liabilities: Others	1,564	1,433	1,505	1,625	1,788
Total Interest-Bearing Liabilities	1,564	1,433	1,505	1,625	1,788
Banks Liabilities Under Acceptances					
Total Non-Interest Bearing Liabilities	987	1,366	1,435	1,549	1,704
Total Liabilities	2,551	2,799	2,939	3,175	3,492
Shareholders Equity	13,169	17,046	21,645	24,343	26,603
Minority Interests					
Total Equity	13,169	17,046	21,645	24,343	26,603

Key Ratios

	Mar-20A	Mar-21A	Mar-22F	Mar-23F	Mar-24F
Total Income Growth					
Operating Profit Growth	4.1%	4.9%	28.7%	14.9%	16.8%
Pretax Profit Growth	1%	5%	30%	15%	17%
Effective Tax Rate	25.5%	24.7%	25.3%	25.2%	25.2%

Nippon Life India Asset Management Ltd

Expensive, but still attractive

- NAM India has regained debt market share and we expect the same for equity soon due to their scheme outperformances, rising reach and digital initiatives.
- We are building AUM growth of ~18% CAGR from FY21-24F with rising share of equity and consistent dominance of ETFs
- Initiating coverage on NAM India with Add rating and a TP of Rs380 based on dividend discount model, at ~23.6x FY24F P/E and ~6.7% FY24F AUM.

India

ADD *(Initiating coverage)*

Consensus ratings*:	Buy 14 Hold 4 Sell 0
Current price:	Rs299
Target price:	Rs380
Previous target:	NA
Up/downside:	26.7%
EIP Research / Consensus:	-11.5%
Reuters:	NIPF.NS
Bloomberg:	NAM IN
Market cap:	US$2,446m
	Rs186,291m
Average daily turnover:	US$5.0m
	Rs382.7m
Current shares o/s:	0.0m
Free float:	46.0%

**Source: Bloomberg*

Source: Bloomberg

Price performance	1M	3M	12M
Absolute (%)	(13.5)	(18.2)	(17.1)
Relative (%)	(8.3)	(13.3)	(23.1)

Major shareholders	% held
Nippon Life Insurance	30.0
LIC	5.5
Baron	2.3

Regained market share in Debt funds; gain in equity funds awaited

NAM India managed to regain its lost share in debt funds with market share of ~7.1% as at end-Dec 2021 vs. 3.8% as at end-Mar 2020, which is equally attributable to management's consistent efforts towards outperformance as well as superior brand equity of the promoters. On Equity flows, NAM India continues to lose market share however, considering the gradual schemes outperformances along with a rising distribution reach and management's focus over various digital initiatives, we are confident of the AMC's ability to regain lost market share in equities as well.

First-mover advantage in ETFs; Focused on product differentiation

NAM India had been one of the first AMCs to start focusing on ETF as an investment class which has provided it with a first-mover advantage with ~72% share of exchange volume, as per company filings. The company has introduced various passive investment products with low-cost options that cater to different risk appetites. Generally, ETFs are low-yield products, but NAM India management claims superior yields due to product differentiation.

Limited yield improvement as operating leverage already optimized

Despite rise in equities, we are not factoring in any improvement in revenue yields due to regulatory pressure on yields to continue. We are factoring in ~13.2% CAGR in profits over FY21-24F which is in-line with revenues rise as we believe that NAM India has already benefited from improving operating leverage in past few years. Going ahead, we don't a case for any further operating leverage kicking in for NAM India.

Initiate coverage with Add rating and TP of Rs380

On comparing listed AMCs, based on P/E and RoE multiple, we observe that NAM India trades at a premium to peers like ABSL and UTI AMC, but we still expect a revival in valuation multiple backed by superior yield profile and highest dividend payout. We initiate coverage on NAM India AMC with Add rating and a TP of Rs380, based on dividend discount model, corresponding to ~23.6x FY24F P/E and ~6.7% FY24F AUM with Our target price is based on the assumptions of cost of equity at 11.7% and a terminal growth rate of 5%. Downside risks: Lower growth in fund inflows and underperformance of funds.

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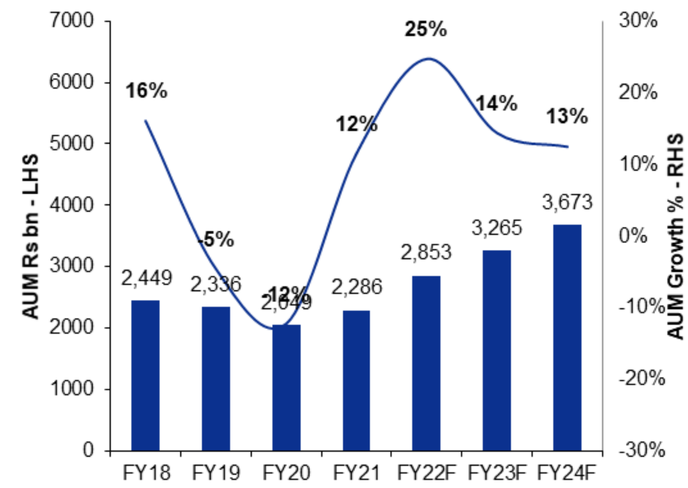
Financial Summary	Mar-20A	Mar-21A	Mar-22F	Mar-23F	Mar-24F
Operating Revenue (Rsm)	11,933	14,192	15,606	17,965	20,140
Net Profit (Rsm)	4,154	6,803	7,512	8,331	9,414
Core EPS (Rs)	6.79	11.03	12.19	13.51	15.27
Core EPS Growth	(15%)	63%	10%	11%	13%
FD Core P/E (x)	44.12	27.14	24.58	22.16	19.61
DPS (Rs)	0.00	0.00	0.00	0.00	0.00
Dividend Yield	0.00%	0.00%	0.00%	0.00%	0.00%
BVPS (Rs)	42.4	50.3	52.7	55.4	58.5
P/BV (x)	7.07	5.96	5.68	5.40	5.12
ROE	16.1%	23.9%	23.7%	25.0%	26.8%
% Change In Core EPS Estimates					
InCred Research/Consensus EPS (x)			1.04	1.05	1.05

SOURCES: INCRED RESEARCH, COMPANY REPORT

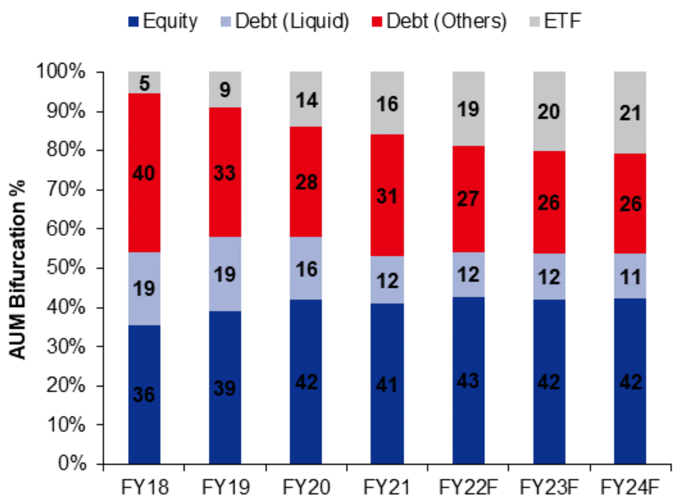
NAM India- key charts

Figure 66: Regains lost momentum post- transmission



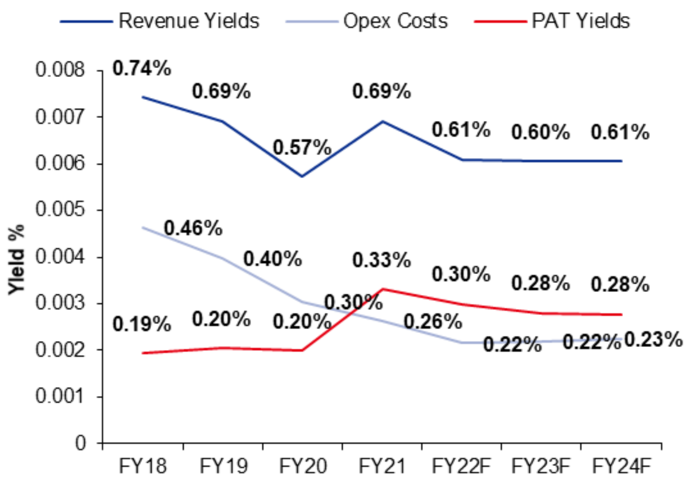
SOURCES: INCRED RESEARCH ESTIMATES, COMPANY REPORTS

Figure 67: Diversified AUM mix with a rising share of equity funds



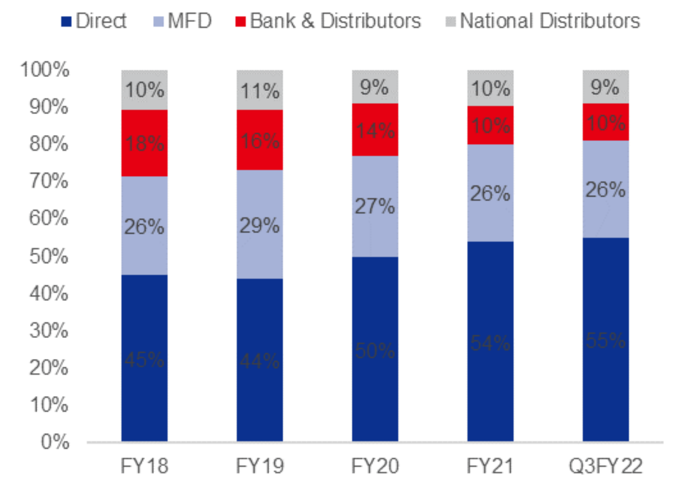
SOURCES: INCRED RESEARCH ESTIMATES, COMPANY REPORTS

Figure 68: Steady PAT led by healthy operating efficiency



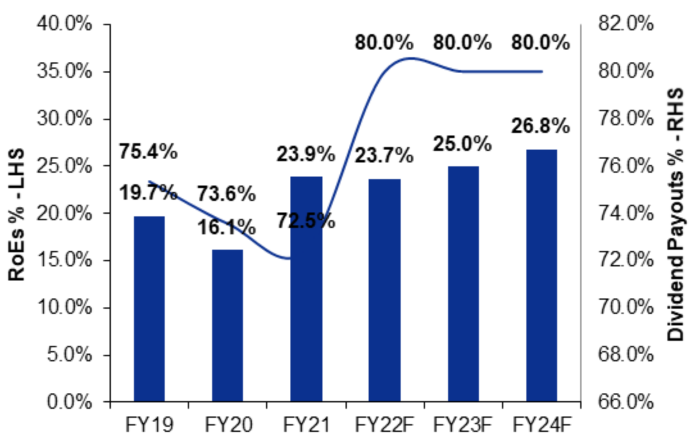
SOURCES: INCRED RESEARCH ESTIMATES, COMPANY REPORTS

Figure 69: MFD remains key contributor to MF distribution



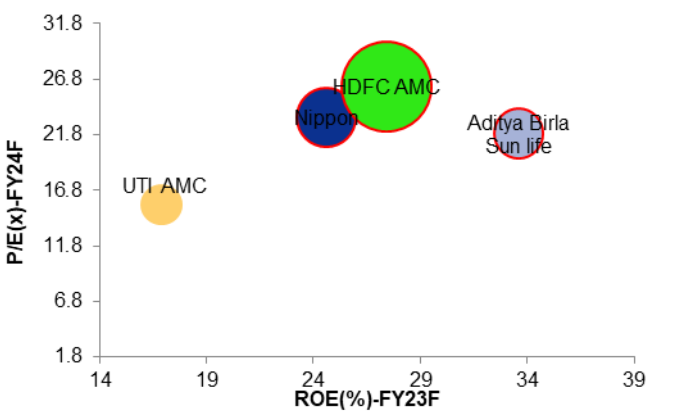
SOURCES: INCRED RESEARCH ESTIMATES, COMPANY REPORTS

Figure 70: NAM India manages the highest dividend payout compared to peers



SOURCES: INCRED RESEARCH ESTIMATES, AMFI

Figure 71: NAM India trades above the trendline of AMC valuation



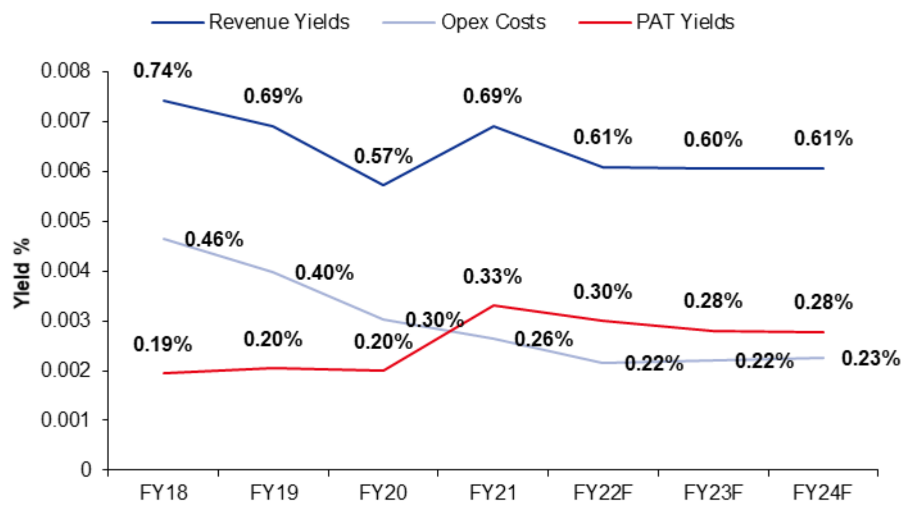
SOURCES: INCRED RESEARCH, COMPANY REPORTS ESTIMATES, BLOOMBERG ESTIMATES

Transformation success – gains awaited

Nippon Life India Asset Management Limited (NAM India) is the asset manager of Nippon India Mutual Fund (NIMF), promoted by Nippon Life Insurance (Japan) with ~73.9% shareholding. The AMC has witnessed volatile times earlier with heavy AUM outflows (on equity as well as debt front) and was loaded with heavy operating model impacting earnings.

However, in past couple of years, management has made tremendous efforts to turn around the company across various matrices, ranging from stability in investment team to rationalisation of business model and bringing stability in overall flows to the AMC. NAM India has successfully achieved the status of being one of the highest dividend-paying companies, with PAT yields improving by almost ~40% over past two years.

Figure 72: Rise in profitability with elevated dividend payout

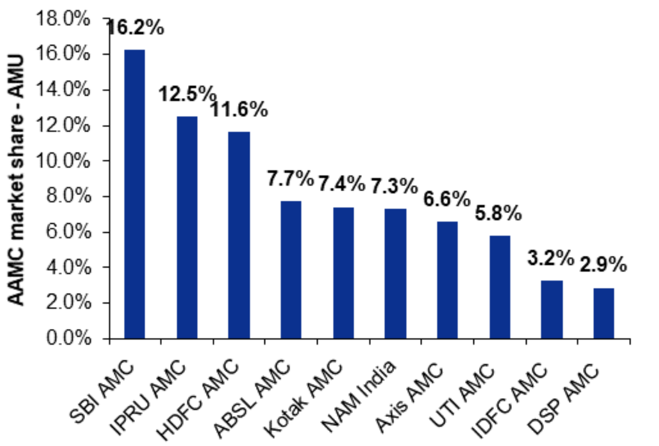


SOURCES: INCRED RESEARCH ESTIMATES, COMPANY REPORTS

Sixth-largest AMC in India; equity/ETF key contributor to AUM

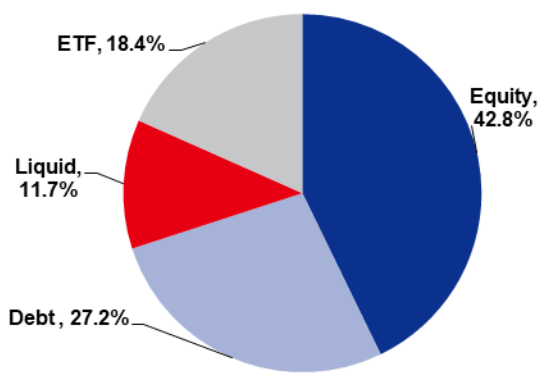
NAM India is India's sixth-largest asset management company in terms of assets under management as at end-Dec 2021 with an overall market share of ~7.3% of industry AUM. The company has witnessed significant improvement in overall equity fund inflows in recent years with rising traction in ETFs as well. As per company reports, NAM India AMC manages overall AUM of Rs3.45tr, but NAM India Mutual Fund manages funds worth Rs2.8tr.

Figure 73: NAM India holds sixth-largest AUM as at end-Dec 2021



SOURCES: AMFI, INCRED RESEARCH

Figure 74: NAM India MF holds mainly equity funds/ETFs as at end-Dec 2021



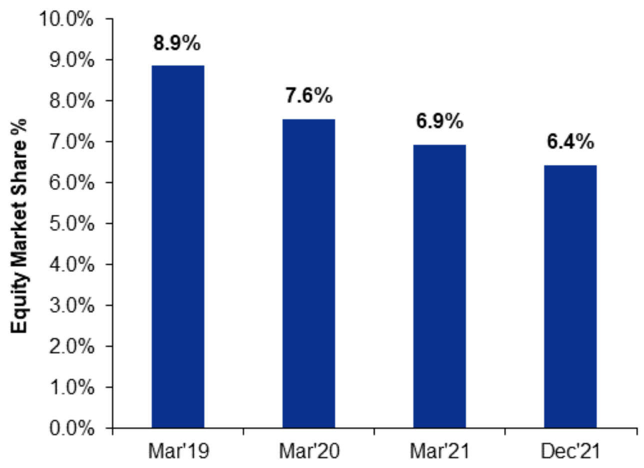
SOURCES: INCRED RESEARCH, COMPANY REPORTS

Debt flows improved, market share loss in equity continues

NAM India, post transformation, has managed to regain its lost share in debt funds which is equally attributable to management's efforts as well as promoter's track record. In May 2020, NAM India's board decided that all NIMF schemes will make new investments in only AA and above-rated issuers. Such moves have gained confidence among investors.

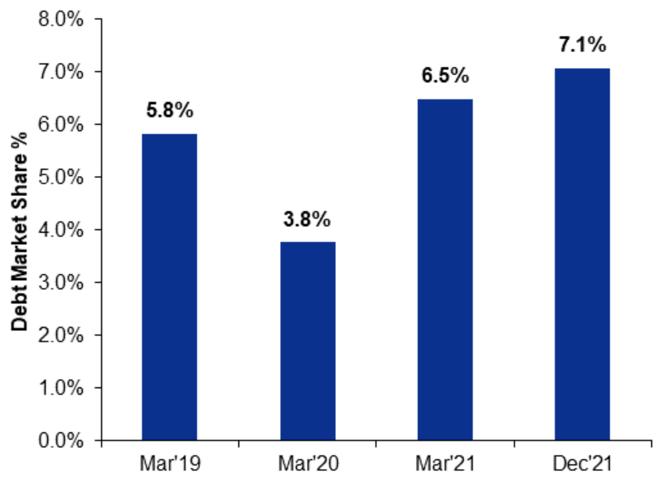
However, the company continues to lose market share in equity funds which needs to be a key monitorable in near future. Considering recent outperformance of schemes (like NAM India multi-cap fund, etc.) of NAM India equities team along with a rising distribution reach, aggressive marketing approach and differentiated digital initiatives, we remain confident of the AMC's ability to regain lost market share gradually.

Figure 75: Market share loss in equity funds continues



SOURCES: AMFI, INCRED RESEARCH

Figure 76: Regains lost share in debt fund segment

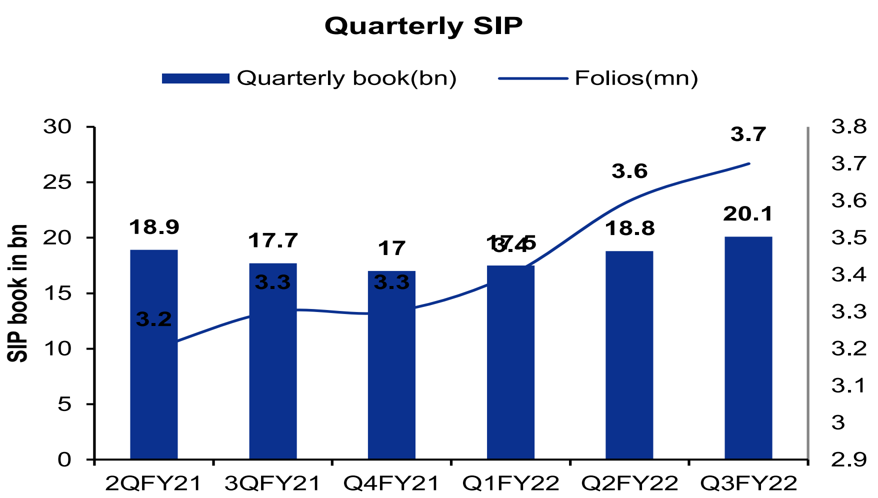


SOURCES: AMFI, INCRED RESEARCH

SIP – volatile growth but deepening reach

Due to highly volatile markets and impact of the global Covid-19 pandemic, Systematic Investment Plan (SIP) inflows reduced in the initial months of the pandemic but began normalising post-Covid. NAM India has witnessed SIP inflows with a consistent rise in folios. Despite the rise in folios, overall SIP book remains volatile as with retailization of overall SIP book, average SIP amount has been declining.

Figure 77: Growing quarterly SIP book

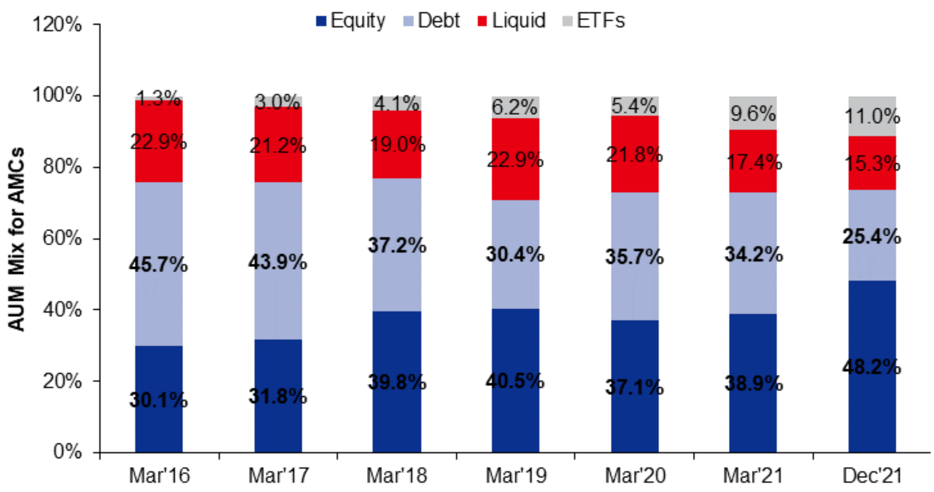


SOURCES: INCRED RESEARCH, COMPANY REPORTS

Leadership in ETFs – first-mover advantage

Indian markets have been witnessing a surge in demand for passive funds since last few years. ETF (exchange traded fund) as a mode of investment is gaining popularity among investors for several reasons, but primarily active mutual funds are finding it increasingly difficult to sustain higher returns and several of them have been lagging benchmarks. Also, ETFs are now being built on indices with strategies and sector opportunities that are distinct from plain vanilla mainstream mutual funds or MFs.

Figure 78: Rise in ETFs' share in Indian AMCs is clearly visible

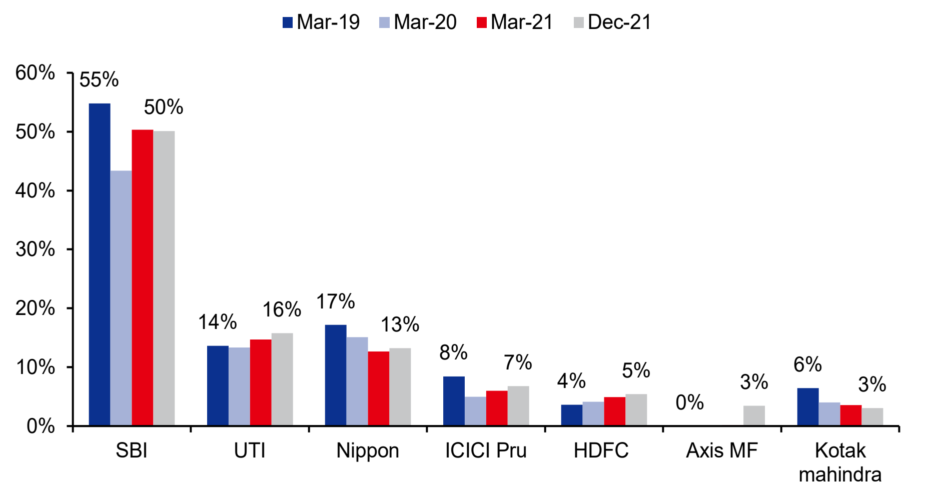


SOURCES: AMFI, INCRED RESEARCH

NAM India enjoys the first-mover advantage in the segment

NAM India was one of the first AMCs to start focusing on ETFs as an investment class which has provided it the first-mover advantage with a decent market share. The AMC spotted passive investing as a trend well ahead, enabling it to become one of the largest players in the ETF space in India with a 72% share of exchange volume, as per company filings.

Figure 79: NAM India remains a dominant player in ETF market in India



SOURCES: AMFI, INCRED RESEARCH

The company has introduced various passive investment products with low-cost investment options that cater to different risk appetites. Nippon India Mutual Fund has gained 1.4m new ETF folios in 2021 with ~42% market share of total industry ETF folios. The company has built an industry-best suite of fixed-income and equity products in this space and garnered an AUM of over Rs370bn, as per company filings.

Steady profitability, healthy dividend payouts

NAM India witnessed a sharp rise in profitability in FY21 but the same is attributable to a surge in treasury income amid mark-to-market or MTM gains on equity as well as debt investments of the AMC during the previous year.

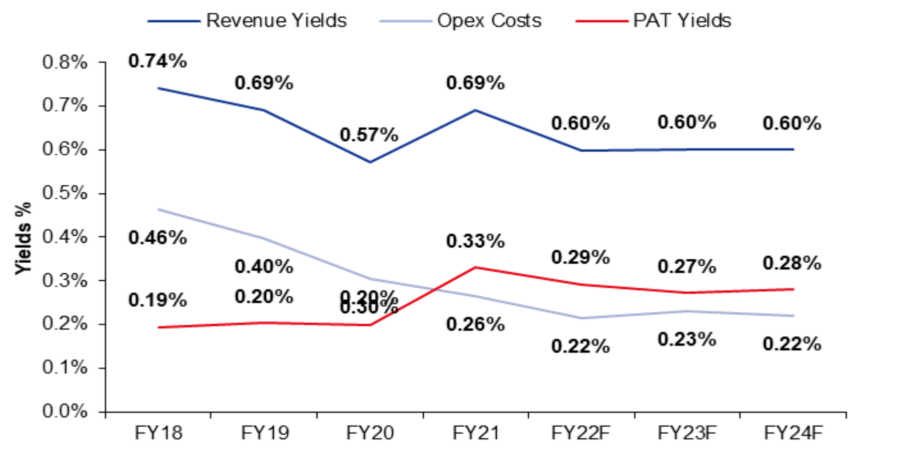
We are factoring in revenue yields remaining steady

Going ahead, we are factoring in a steady phase in revenue yields as most transitionary factors will settle down in coming quarters, in our view. We are not factoring in an improvement, despite the probable rise in equity flows, as we believe regulatory pressure on yields will continue to remain for AMCs in India.

Limited scope for further improvement in profit yields

NAM India has already benefited from operating leverage improving in the past. Going ahead, we do not expect any major change in operating expenses as most of the lever has already been utilised. We forecast flat PAT yields in coming years.

Figure 80: Profitability trend

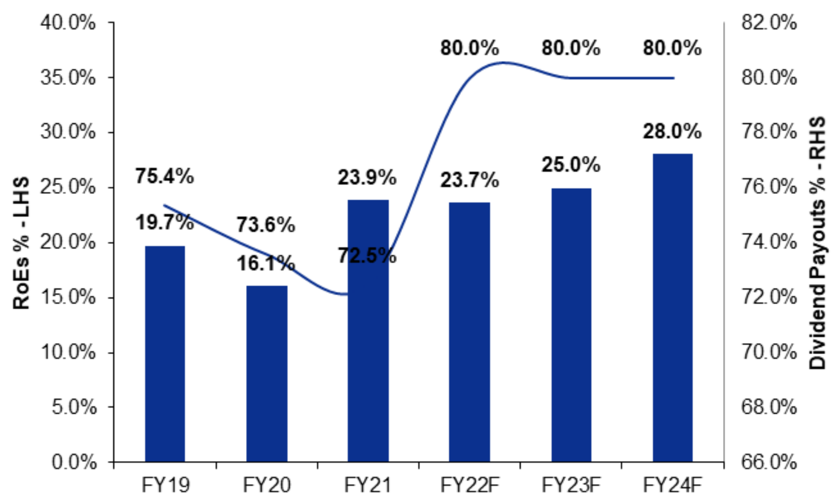


SOURCES: INCRED RESEARCH ESTIMATES, COMPANY REPORTS

However, linear capital structure to sustain dividend payouts

Factoring in the minimum requirement of additional capital, we expect NAM India to maintain elevated dividend payouts.

Figure 81: Rise in RoE to support elevated dividend payouts



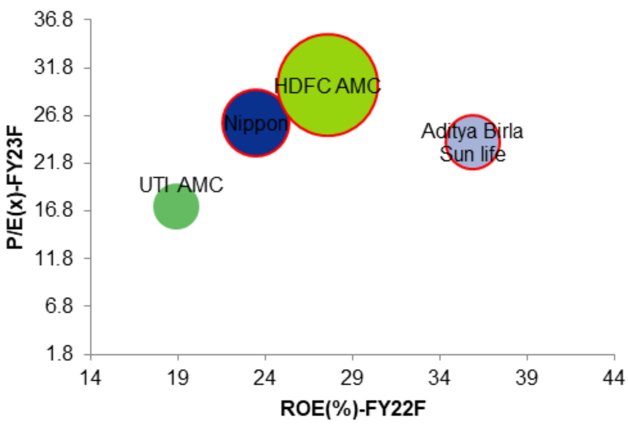
SOURCES: INCRED RESEARCH ESTIMATES, COMPANY REPORTS

Outlook & valuation

We have plotted all listed AMCs, based on their forward RoEs, on a valuation table. We are considering one-year and two-year forward multiples to assess valuation premium or else discounting of all listed players.

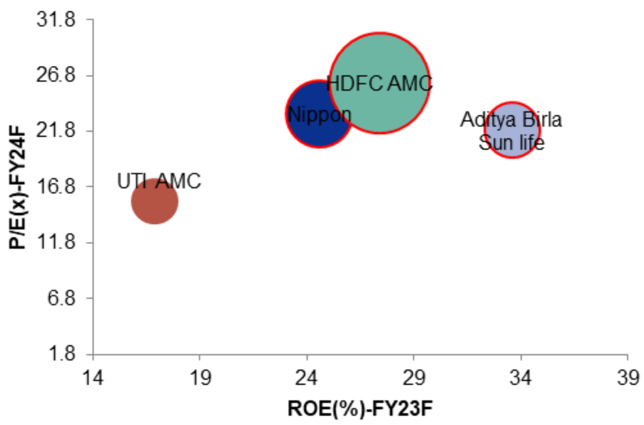
Comparison based on P/E to RoE basis

Figure 82: RoE in FY22F compared to FY23F P/E



SOURCES: BLOOMBERG, INCRED RESEARCH ESTIMATES

Figure 83: RoE in FY23F compared to FY24F P/E



SOURCES: BLOOMBERG, INCRED RESEARCH ESTIMATES

NAM India trades above the trend line, but still deserves expansion

On comparing listed AMCs, based on P/E and RoE multiple, we observe that NAM India is trading above the trendline, but we still expect a revival in valuation multiple backed by:

- Superior yield profile compared to peers with optimum operating leverage.
- ETFs to witness improved traction in Indian markets and NAM India, being a pioneer, will remain one of the key beneficiaries.
- NAM India is a step ahead in technology advancement compared to peers, which will give it an edge over competitors in coming years, in our view.
- NAM manages highest dividend payout among peers.

Initiating coverage on NAM India with Add rating

We initiate coverage on NAM India AMC with Add rating and a TP of Rs380, corresponds to ~ 23.6x at FY24F P/E and ~6.7% FY24F AUM. Our valuation of NAM is based on dividend discounting methodology, valuing the business on the basis cost of equity of 11% and terminal growth of 5%.

Our assumptions of the cost of equity at 11% is based on a risk-free rate of 6%, risk premium of 6% and beta of 0.9. We have taken terminal growth as 5%, which is the expected perpetual growth rate of India's GDP.

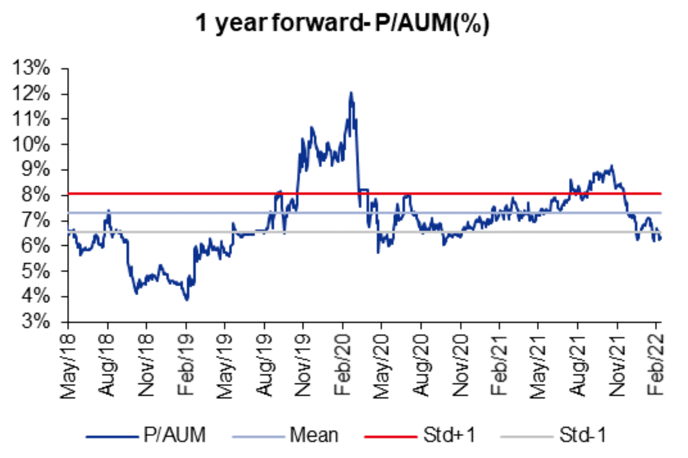
Figure 84: NAM India valuation

Valuation	
Cost of equity (%)	12
Dividend payout ratio (%)	85%
Terminal growth (%)	5%
Present value of free cash flow (Rsm)	2,32,019
Outstanding shares (m)	617
Target price per share (Rs)	380
EPS(Rs)	15
P/E(x)	25

SOURCES: COMPANY REPORTS ESTIMATES, INCRED RESEARCH

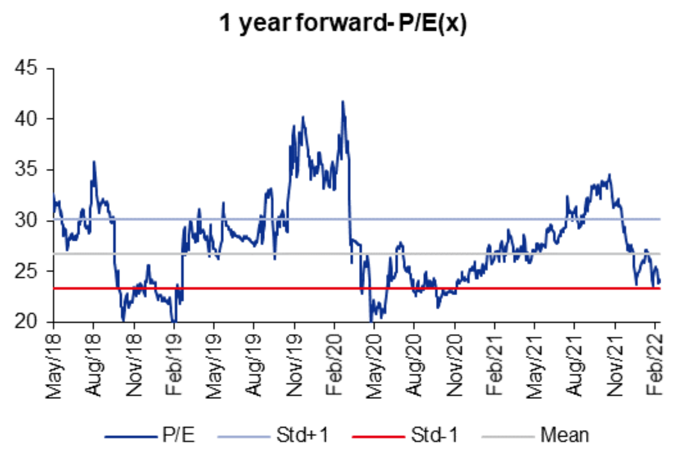
Historical valuation band of NAM India

Figure 85: One-year forward P/AUM with standard deviation



SOURCES: INCRED RESEARCH, COMPANY REPORTS

Figure 86: One-year forward P/E with standard deviation



SOURCES: INCRED RESEARCH, COMPANY REPORTS

Peer comparison

Figure 87: Peer comparison

Indian Peers	BBG ticker	Rating	Closing Price (LC)	Target Price	Mcap (US$ bn) Current	AUM(US$bn) FY22F	AUM(US$bn) FY23F	PAT (US$m) FY22F	PAT (US$m) FY23F	P/E FY22F	P/E FY23F
Nippon Life	RNAM	Add	300	380	2.7	38	38	103	115	27	24
HDFC AMC	HDFCAMC	Hold	2,082	2,300	6.3	60	60	189	203	33	31
AB AMC	ABSLAMC	Add	500	650	2.0	42	47	92	111	21	18
UTI AMC	UTIAM	Add	847	1,100	1.5	31	35	78	88	19	17

SOURCES: INCRED RESEARCH ESTIMATES,BLOOMBERG, PRICED AT 4TH MAR 22

Risks to our investment thesis

ETF growth may slow down leading to market share loss

NAM India had the first-mover advantage in exchange-traded funds (ETFs) leading to a market share of 13% in ETFs. New players can offer very low fees to customers to gain market share, which could lead to lower AUM growth for NAM India.

Instability in investment management team can led to a sharp de-rating

NAM India, after a high churn, has stabilized its investment management team which led to higher investor confidence. However, if again its investment managers move out, then it could again lead to loss of investor confidence which would be difficult to regain.

Underperformance can lead to lower growth in equity funds

NAM India has lost its market share in equity funds but regain of lost market share is likely due to the current outperformance of its equity funds. However, underperformance can lead to a lower growth in equity funds.

Dent to brand image

NAM India, despite being a non-banking AMC, is able to gain significant market share due to the strong brand of Nippon. Any negative news on other companies of the group can impact fund inflows.

Change in ownership can lead to instability

Nippon Life owns a 73% stake in NAM India. If Nippon Life decides to exit the business by selling its stake in NAM India, it can lead to instability.

Industry-related risk

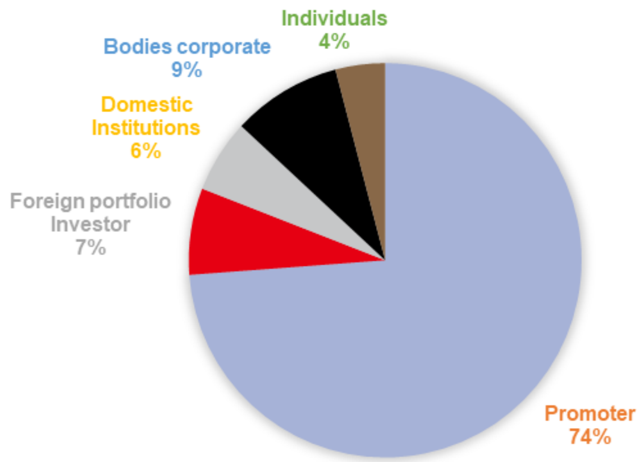
Like other AMCs, NAM India is exposed to the risk of lower flows due to any down cycle, pressure on yields due to the drop in expense ratio, and the risk of regulatory intervention.

Figure 88: Key management profile as at end-Dec 2021

Name	Designation	Background
Sundeep Sikka	ED & CEO	Mr. Sikka joined NAM India in 2003, holding various leadership positions before being elevated in 2009, when he became one of the youngest CEOs in India.
Minouru Kimura	Chairman	Mr Kimura joined Nippon in 1990 and heads Nippon Life Insurance in America, Europe and Asia.
Manish gunwani	CIO-Equity	Manish graduated from IIT Chennai with a B.Tech degree and has a Post Graduate Diploma in Management from IIM Bengaluru. Manish has over 21 years of work experience, primarily in equities, spanning roles in equity research and fund management.
Saugata Chatterjee	Co-Chief Business officer	Saugata has also successfully built SME and HNI segments. Under his different roles and leadership responsibilities over the last five years, the distribution team has come a long way with increased focus on opportunities, strategic approach and sharper execution.
Aashwin Dugal	Co-Chief Business Officer	Aashwin is a finance and marketing professional who brings with him 19 years of rich experience in banking and the mutual fund industry. He possesses deep understanding of institutional as well as retail markets. He has been with Nippon Life India Asset Management Limited (formerly Reliance Nippon Life Asset Management Limited) for about eight years.

SOURCES: INCRED RESEARCH, COMPANY REPORTS

Figure 89: Shareholding pattern as at end-Dec 2021



SOURCES: INCRED RESEARCH, COMPANY REPORTS

BY THE NUMBERS

Profit & Loss

(Rsm)	Mar-20A	Mar-21A	Mar-22F	Mar-23F	Mar-24F
Net Interest Income					
Total Non-Interest Income	**11,933**	**14,192**			
Operating Revenue	11,933	14,192	15,606	17,965	20,140
Total Non-Interest Expenses	**(6,001)**	**(5,090)**	**(5,603)**	**(6,870)**	**(7,602)**
Pre-provision Operating Profit	5,600	8,769	10,003	11,095	12,538
Total Provision Charges					
Operating Profit After Provisions	5,600	8,769	10,003	11,095	12,538
Pretax Income/(Loss) from Assoc.					
Operating EBIT (incl Associates)	5,600	8,769	10,003	11,095	12,538
Non-Operating Income/(Expense)					
Profit Before Tax (pre-EI)	5,600	8,769	10,003	11,095	12,538
Exceptional Items					
Pre-tax Profit	5,600	8,769	10,003	11,095	12,538
Taxation	(1,441)	(1,976)	(2,501)	(2,774)	(3,135)
Consolidation Adjustments & Others					
Exceptional Income - post-tax					
Profit After Tax	4,159	6,793	7,502	8,321	9,404
Minority Interests	(5)	9	10	10	10
Pref. & Special Div					
FX And Other Adj.					
Net Profit	4,154	6,803	7,512	8,331	9,414
Recurring Net Profit					

Balance Sheet

(Rsm)	Mar-20A	Mar-21A	Mar-22F	Mar-23F	Mar-24F
Total Gross Loans					
Liquid Assets & Invst. (Current)	18,846	25,500	28,559	31,987	35,825
Other Int. Earning Assets					
Total Gross Int. Earning Assets	18,846	25,500	28,559	31,987	35,825
Total Provisions/Loan Loss Reserve					
Total Net Interest Earning Assets	18,846	25,500	28,559	31,987	35,825
Intangible Assets					
Other Non-Interest Earning Assets	**1,881**	**1,444**	**782**	**764**	**1,842**
Total Non-Interest Earning Assets	**5,329**	**4,816**	**4,105**	**4,419**	**5,862**
Cash And Marketable Securities	4,633	3,606	3,786	3,976	4,175
Long-term Investments					
Total Assets	28,808	33,921	36,451	40,381	45,862
Customer Interest-Bearing Liabilities					
Bank Deposits					
Interest Bearing Liabilities: Others					
Total Interest-Bearing Liabilities					
Banks Liabilities Under Acceptances					
Total Non-Interest Bearing Liabilities	2,878	2,919	3,947	6,213	9,813
Total Liabilities	2,878	2,919	3,947	6,213	9,813
Shareholders Equity	25,929	31,003	32,504	34,168	36,049
Minority Interests					
Total Equity	25,929	31,003	32,504	34,168	36,049

Key Ratios

	Mar-20A	Mar-21A	Mar-22F	Mar-23F	Mar-24F
Operating Profit Growth	(16.5%)	53.4%	9.9%	10.9%	13.0%
Pretax Profit Growth	(20%)	57%	14%	11%	13%
Effective Tax Rate	25.7%	22.5%	25.0%	25.0%	25.0%
Net Dividend Payout Ratio					
Return On Average Assets	14.69%	21.69%	21.35%	21.69%	21.83%

SOURCES: INCRED RESEARCH, COMPANY REPORTS

India

ADD *(Initiating coverage)*

Consensus ratings*:	Buy 8	Hold 2	Sell 0

Current price:	Rs847
Target price:	Rs1,100
Previous target:	NA
Up/downside:	29.9%
EIP Research / Consensus:	-13.7%
Reuters:	UTIA.NS
Bloomberg:	UTIAM IN
Market cap:	US$1,411m
	Rs107,494m
Average daily turnover:	US$3.1m
	Rs239.3m
Current shares o/s:	0.0m
Free float:	46.0%

Source: Bloomberg

Source: Bloomberg

Price performance	1M	3M	12M
Absolute (%)	0.6	(19.4)	40.2
Relative (%)	6.6	(14.5)	30.1

Major shareholders	% held
T ROWE PRICE	23.0
PNB	15.0
SBI	10.0

UTI AMC

Enough steam for profitable improvement

- UTI AMC is committed towards superior profitability backed by reshuffling in AUM coupled with decent scope for improvement in operating leverage.
- We are factoring in ~14.4% CAGR in PAT over FY21-24F amid healthy revenue yields and improved PAT yields backed by well managed operating expenses.
- Initiating coverage on UTI AMC with Add rating and a TP of Rs1,100 based on Dividend Discount model, at ~18.8x FY24F P/E and ~4.9% FY24F AUM.

Equity flows improving, building case for Market share gains

UTI AMC posted market share loss over FY15-20 due to its lower focus on banca channel, and debt exposure to troubled entities like ILFS, DHFL, etc. It lost overall market share (primarily debt funds), from ~5.2% in FY17 to ~4.2% in Dec 21, as per AMFI. However, recently, equity flows have witnessed an improvement, backed by scheme outperformance as well as rising retail participation. UTI AMC already has built an improved distribution network (including banks) along with a stringent risk management framework and a clear focus on growth and profitability. Thus, we are factoring in UTI AMC to grow faster than peers and gain market share for next few years.

Decent room for operating leverage to drive profitability

UTI AMC has a higher cost burden due to excess employees charge which is expected to ease with consistent improvement in employee productivity as well as management's increasing focus towards digitalization. With operating leverage kicking in amid rise in revenues and decline in costs, UTI AMC, in our view, to witness a surge in profit yields.

Privatization on cards – probability of stake acquisition from PSUs

Post-IPO, T Rowe Price International (a global investment management firm) is the largest shareholder with ~23% stake in the AMC. T Rowe Price also owns a major stake in UTI Trustee Company. With the rising importance of financial savings among Indian households along with under-penetration and concentrated business model of mutual funds, the outlook for AMCs in India remains buoyant. Considering improving efficiencies of UTI AMC, T Rowe Price (already being an investment manager) can opt to buy out majority stake from PSU banks (the easiest route) and can become promoter of the AMC.

Initiate coverage with Add rating and TP of Rs1,100

On comparing listed AMCs based on price/earnings and RoE multiple, we observed that UTI AMC is trading at a steep discount to peers. With improvement in profitability, we see a probable expansion in the multiple for UTI AMC. We initiate coverage on UTI AMC with Add rating and a TP of Rs1,100, based on dividend discounting model, corresponding to ~18.9x at FY24F P/E and ~4.9% FY24F AUM. Our TP is based on assumptions of the cost of equity at 11.7% and a terminal growth rate of 5%. Key downside risks: Lower growth from B-30 cities and new channels, and industry-related risks.

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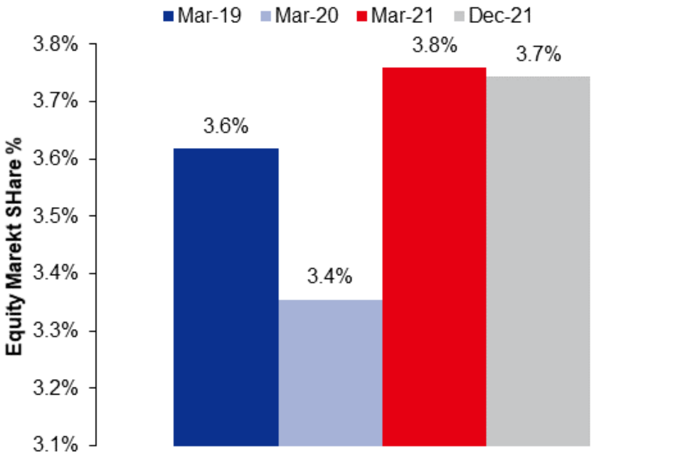
Financial Summary	Mar-20A	Mar-21A	Mar-22F	Mar-23F	Mar-24F
Total Non-Interest Income (Rsm)	8,900	11,986	13,698	15,849	17,600
Operating Revenue (Rsm)	8,900	11,986	13,758	15,922	17,709
Net Profit (Rsm)	2,715	4,941	5,871	6,453	7,390
Core EPS (Rs)	21.41	38.97	46.30	50.90	58.29
Core EPS Growth	(23%)	82%	19%	10%	15%
FD Core P/E (x)	39.55	21.73	18.29	16.64	14.53
DPS (Rs)	7.00	17.00	23.15	27.99	34.97
Dividend Yield	0.83%	2.01%	2.73%	3.31%	4.13%
BVPS (Rs)	218.7	254.4	277.6	300.5	323.8
P/BV (x)	3.87	3.33	3.05	2.82	2.62
ROE	10.1%	16.5%	17.4%	17.6%	18.7%
% Change In Core EPS Estimates					
InCred Research/Consensus EPS (x)			1.04	1.07	1.09

SOURCES: INCRED RESEARCH ESTIMATES, COMPANY REPORTS

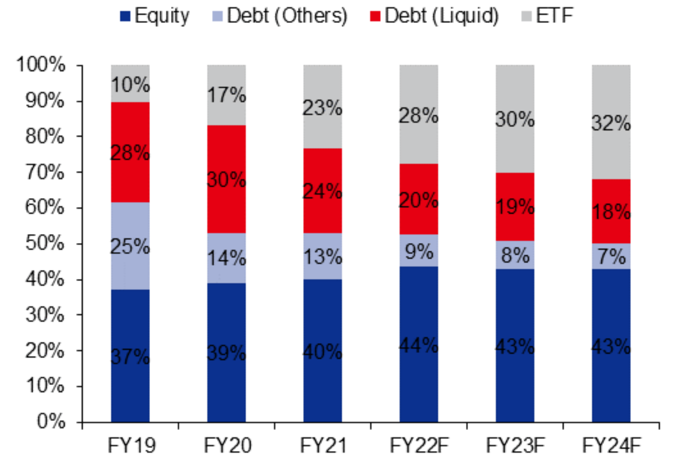
UTI AMC- key charts

Figure 90: UTI AMC is regaining market share in equity fund AUM



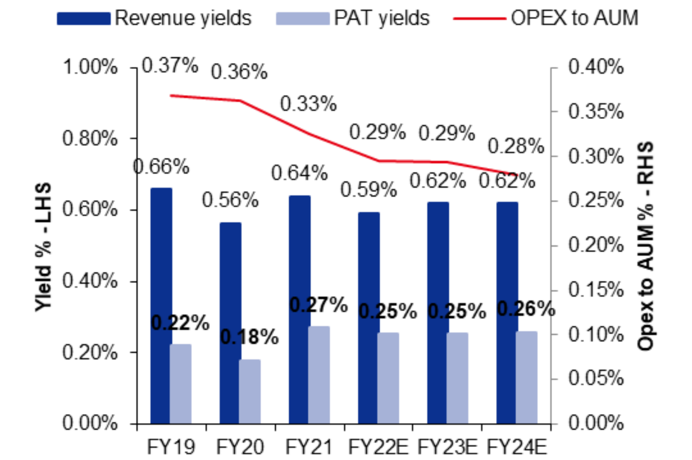
SOURCES: INCRED RESEARCH ESTIMATES, COMPANY REPORTS

Figure 91: Diversified AUM mix with a rising share of equity funds/ETFs



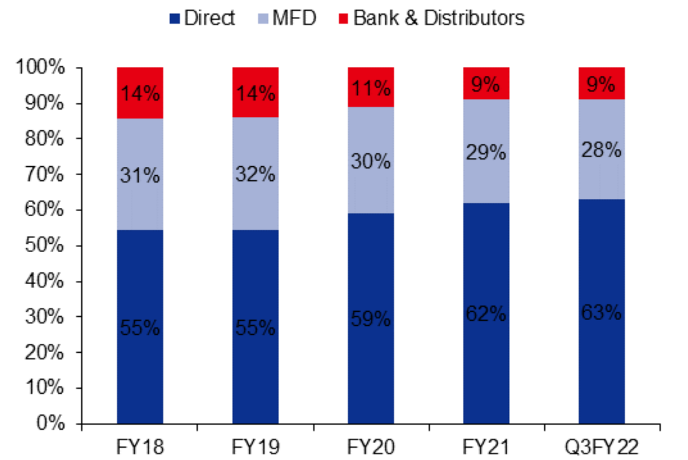
SOURCES: INCRED RESEARCH ESTIMATES, COMPANY REPORTS

Figure 92: Improved profitability led by operating efficiency



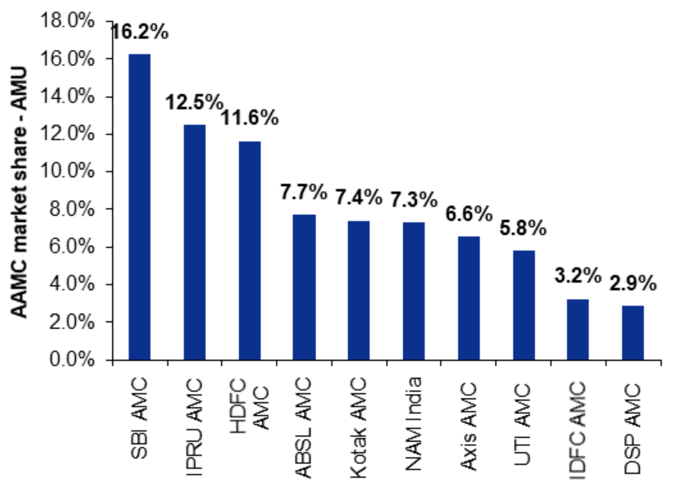
SOURCES: INCRED RESEARCH ESTIMATES, COMPANY REPORTS

Figure 93: Direct channels remain key for MF distribution



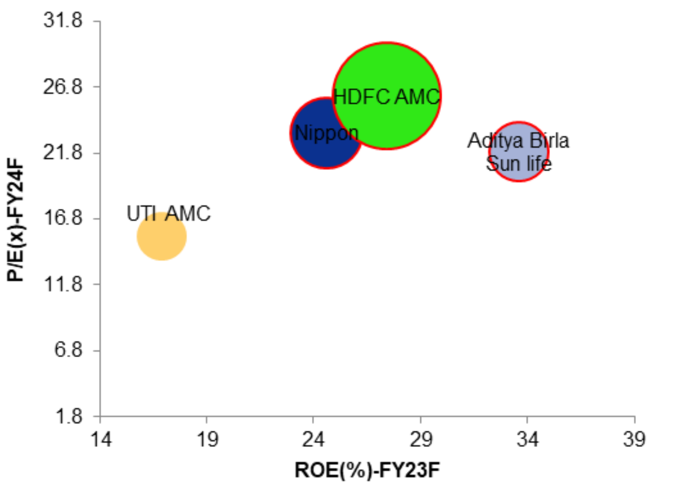
OURCES: INCRED RESEARCH ESTIMATES, COMPANY REPORTS

Figure 94: UTI AMC is eighth-largest AMC in India (AUM basis)



SOURCES: INCRED RESEARCH ESTIMATES, AMFI

Figure 95: ABSL AMC is favourably placed compared to peers



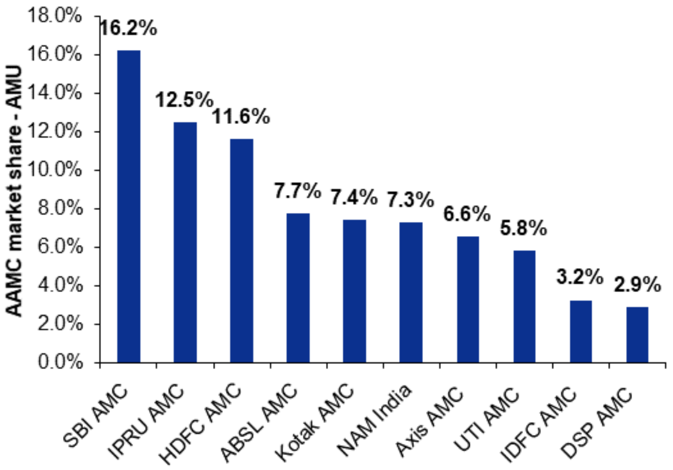
SOURCES: INCRED RESEARCH ESTIMATES, COMPANY REPORTS, BLOOMBERG ESTIMATES

AUM growth on track; equity flows in focus

UTI AMC is the second-largest asset management company in India in terms of total AUM and the eighth-largest asset management company in India in terms of domestic mutual fund QAAUM as at end-Dec 21 with an overall market share of ~5.8% of industry AUM. UTI AMC manages overall AUM of Rs13.1tr, but UTI Mutual Fund manages assets worth Rs2.2tr (Source: UTI Annual report).

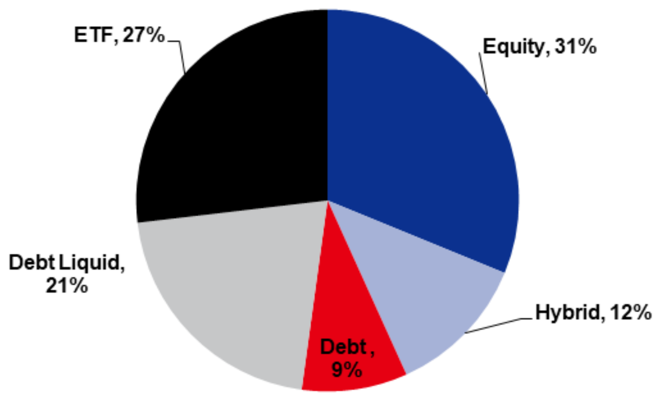
The AMC has the highest concentration in B-30 cities with roughly ~25.2% of its overall AUM contributed by B-30 geographies. A higher presence of AMCs in B-30 cities should allow AMCs to leverage their established position and the potential infrastructural capabilities in which they have already invested. The company has witnessed significant improvement in overall equity inflow in recent years with rising traction in ETFs as well.

Figure 96: AMCs based on AUM market share as at end Dec-21



SOURCES: AMFI, INCRED RESEARCH

Figure 97: MF AUM bifurcation as at end-Dec-21

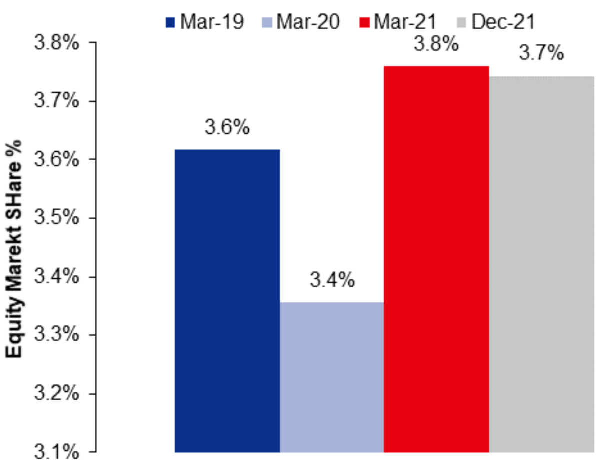


SOURCES: COMPANY REPORTS, INCRED RESEARCH

Market share loss eases, improvement seen across segments

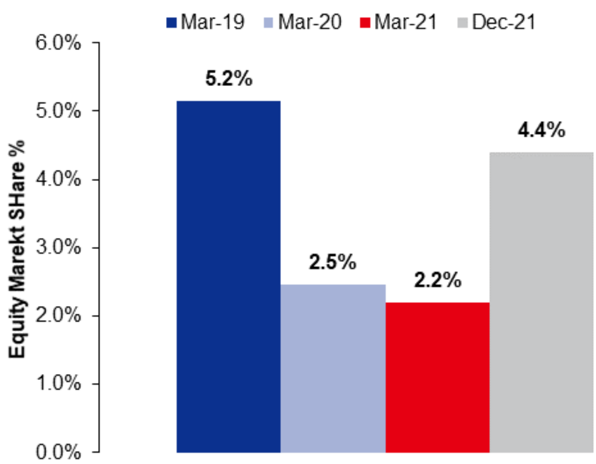
UTI AMC witnessed market share loss over FY15-20 due to its lower focus on Banca channel, and exposure to troubled entities like ILFS (Infrastructure Leasing and Financial Services Limited), DHFL (Dewan Housing Finance Limited), etc. UTI AMC lost market share mostly in debt funds, from ~5.2% in FY17 to ~4.2% in Dec 2021. However, equity fund inflow has already started witnessing an improvement, backed by outperformance of its investment team as well as rising retail participation.

Figure 98: Trend in equity fund market share for UTI MF



SOURCES: AMFI, INCRED RESEARCH

Figure 99: Trend in debt fund market share for UTI MF



SOURCES: AMFI, INCRED RESEARCH

Group companies also witnessed significant improvement

Group AUM of the company posted a growth of ~19% yoy to Rs13.1tr as at end-Dec 2021 compared to Rs11tr as at end-Dec 2020.

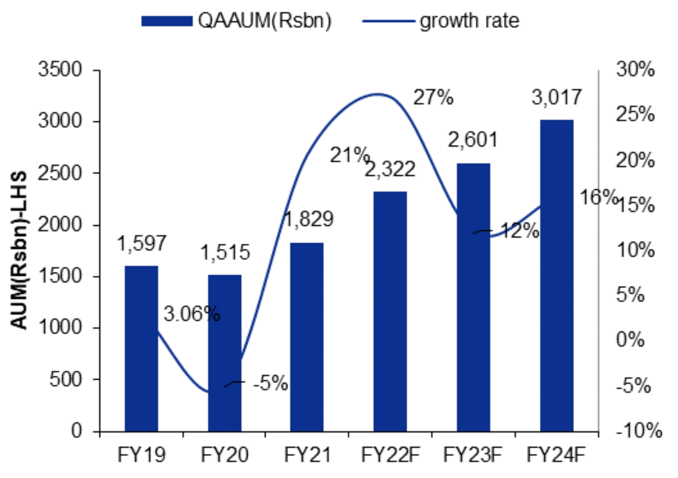
- The growth was led by UTI International (14% yoy), which looks after the offshore business of UTI AMC. UTI International, with its offices in Singapore, London and Dubai, has investors spread across 35 countries and is mainly focussed on investors in Asia, Europe and the Middle East.
- UTI RSL manages pension assets under the NPS of PFRDA (Pension Fund Regulatory and Development Authority). It has a market share of 28.75% in NPS.
- UTI Capital Private Ltd. focuses on growing the private capital investment management business of UTI AMC.
- Alternative Investment Fund (AIF) business in India is still in the growth phase and we feel that with its strong capability in AIF, it will be able to substantially grow this business.

We are factoring in a rise in market share for equity funds/AIF

Going ahead, UTI AMC already has improved distribution network (including banks) along with a stringent risk management framework for fixed-income products and a clear focus on growth and profitability. Thus, we believe UTI AMC will now grow faster than the industry and gain market share in next few years.

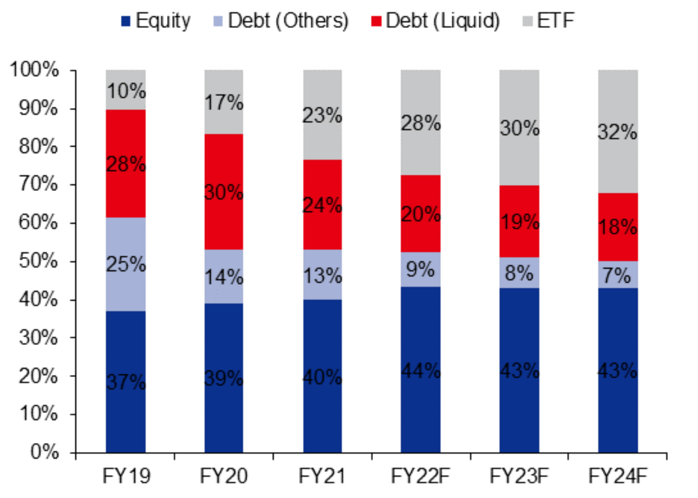
With its growth engine getting restarted, UTI AMC is focusing on equity fund inflows, and we believe most of its AUM growth will be driven by equity fund inflows leading to market share gain in equity funds. Higher equity fund and ETF growth will lead to a rise in market share for these funds, in line with the industry.

Figure 100: AUM growth to remain in teens



SOURCES: INCRED RESEARCH ESTIMATES, COMPANY REPORTS

Figure 101: Equity funds and ETFs to witness improved traction



SOURCES: INCRED RESEARCH ESTIMATES, COMPANY REPORTS

Leadership in B-30 cities is unique feature

Mutual funds have been witnessing low geographic penetration in B-30 (beyond top 30) cities where nearly 90% of Indian households are located. Our interactions with most AMC managements indicate that B-30 cities will continue to see expansion in customer base, although the ticket size will be small. While top-30 cities (Top 30 cities with the highest population) will be value-driven and volume-driven at the same time, B-30 will be volume-driven followed by value.

B-30 cities' share remains underpenetrated for most AMCs

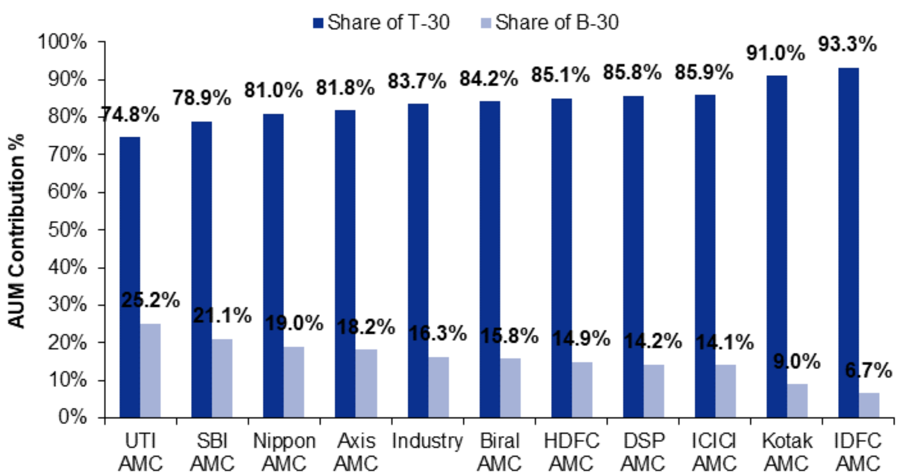
Despite the breakout growth observed over last 10-15 years, Indian asset management industry continues to be significantly underpenetrated compared to other countries and other financial services in India. One of the key reasons for the same has been low geographic penetration in B-30 cities where nearly 90% of Indian households are located.

The share of B-30 cities in total industry AUM hovered around just 15-17% over last few years. Of the 97.9m folios as at Mar 2021-end, around 56.5m folios are from T-30 cities and 41.4m from B-30 cities. Our interactions with most AMC managements indicate that B-30 cities will continue to expand their customer base, although the ticket size will be small. While T-30 markets will be value-driven and volume-driven at the same time, B-30 will be volume-driven followed by value.

UTI AMC and SBI AMC remain better off versus other AMCs

UTI AMC and SBI AMC are the only two players having a share greater than 20% in B-30 cities. Higher presence of AMCs in B-30 cities makes them well-placed to attract new customers at these locations. This is primarily due to their established position, infrastructure, and distribution capabilities, for which they have already invested in. The ability to charge an additional 30bp in expense ratios in B-30 locations reduces pressure on scheme margins.

Figure 102: Share of T-30 and B-30 AUM among top 10 AMCs in India (as at end-Jun 2021)



SOURCES: AMFI, CRISIL, INCRED RESEARCH

Operating leverage to drive profitability

UTI AMC has witnessed consistent improvement in equity fund AUM, the movement in yields had been insignificant considering that the rise was mainly because of passive funds or managed accounts. However more recently, UTI AMC witnessed a decline in yields due to market regulator SEBI's cap on total expense ratio, transition to newer funds at lower yields, lower share of equity funds and a rising share of lower-yield ETF funds. However, despite the pressure on yields for the industry in general, we are of the opinion that revenue yields for UTI AMC will remain stable due to the expected rise in the share of equity funds

Enough room left for improvement in employee expenses

Despite healthy revenue yields, profitability for the company remains moderate due to an elevated cost structure. The company witnesses highest operating costs compared to peers, which in turn impacts profitability.

As per management commentary at various public forums, UTI AMC is overstaffed with ~983 managerial staff (officers) and 403 non-managerial staff. Non-officer employees are unionised and negotiate pay hikes once in five years. Management highlighted that it expects ~250 employees to retire over FY21-25F. This, as per management, is expected to save ~Rs840m by FY25F.

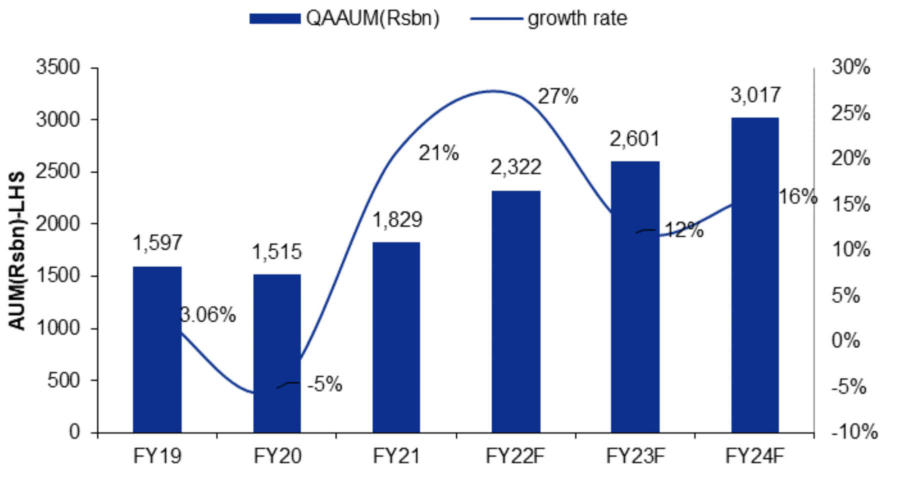
Management also stated that employee replacement costs will not be very high as the retirees are employees who have been with the company over a long time and are now highly paid. Additionally, employee strength will reduce as not all employees need to be replaced. Management expects that it can manage a scale of Rs3tr in AUM with ~900-1,000 employees.

Focus on digitalisation; moving towards rationalisation of costs

UTI AMC is already in a rapid transition mode as the AMC has implemented a comprehensive digital transformation programme to build efficacy, capacity, resilience and cost-effectiveness. UTI AMC took multiple initiatives with respect to application modernisation, hybrid cloud architecture adoption, business process digitalisation, enterprise data platform adoption and cybersecurity enhancement. The AMC now has a board-level Digital Transformation Committee.

Improved operating leverage to drive profitability

Figure 103: Operating leverage to drive profitability



SOURCES: INCRED RESEARCH ESTIMATES, COMPANY REPORTS

With such an improvement in operating leverage, driven by reduction in staff expenses as well as digitalisation of overall processes, UTI AMC is likely to witness a healthy trend in profitability in coming years.

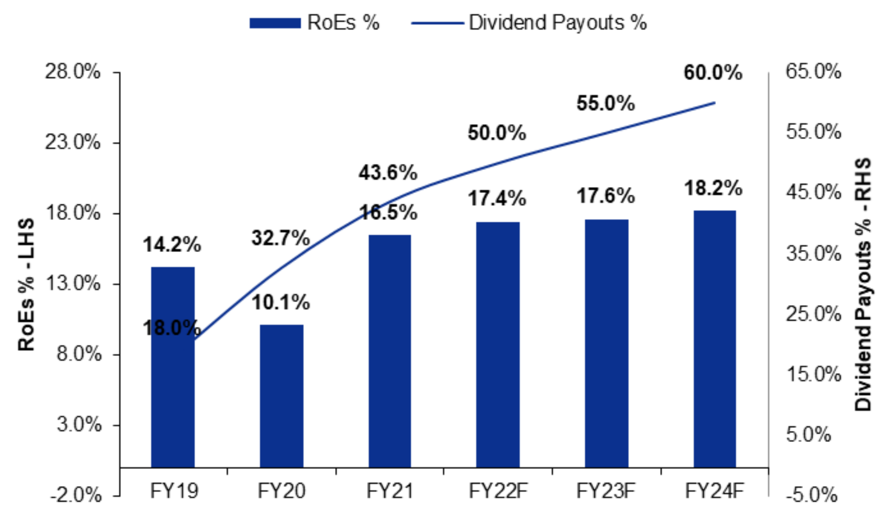
Improving Return ratios, dividend payouts

With a healthy trend in profits along with linearity of capital structure of the company, we believe overall RoE for the AMC is likely to improve from ~16.5% in FY21 to ~18.8% by FY24F. Though this is lower compared to peers, considering the current valuation discount, the same is far superior and will likely drive valuation expansion for the company in coming years.

Buiding a case for a rise in overall dividend distribution

As highlighted, with improvement in operating leverage driven by reduction in staff expenses as well as digitalisation of overall processes, UTI AMC is likely to witness a healthy trend in profitability in coming years. With improved profitability and return ratios, UTI AMC, in our view, will increase its dividend payout ratio to make it parallel with peers. We expect dividend payout ratio to improve to 60% by FY24F.

Figure 104: Improved profitability to drive superior RoE and higher dividend payout



SOURCES: INCRED RESEARCH ESTIMATES, COMPANY REPORTS

Is UTI AMC a privatization candidate?

UTI AMC, before its IPO, was owned by few large public sector banks and Life Insurance Corporation of India or LIC along with T Rowe Price. The public sector banks include State Bank of India or SBI, Punjab National Bank and Bank of Baroda. Most of these banks sold a huge chunk of their stake in the IPO while a small portion was also sold by T Rowe Price.

Figure 105: UTI AMC IPO details

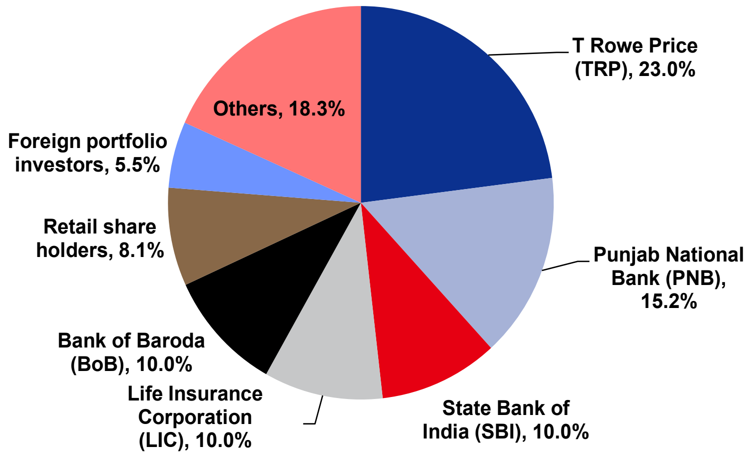
The offer details	Size (m shares)	Size (Rs m)
Offer for sale	38.99	21,598.80
State Bank of India (SBI)	10.46	5,794.80
Life Insurance Corporation (LIC)	10.46	5,794.80
Bank of Baroda (BoB)	10.46	5,794.80
Punjab National Bank (PNB)	3.8	2,107.20
T Rowe Price (TRP)	3.8	2,107.20
Reservations for	0.2	110.8
UTI AMC employees	0.2	
Net issue	**38.79**	**21,488**

SOURCES: INCRED RESEARCH, COMPANY REPORTS

Post-IPO, we have witnessed an improvement across areas

Post-IPO, T Rowe Price has been the largest shareholder with a 23% stake in the AMC. The AMC has witnessed sharp improvement in overall operating efficiency along with scheme-level performance, especially in equity fund AUM, which led to a surge in inflows for the AMC.

Figure 106: Shareholding patten of UTI AMC as at end-Dec 2021

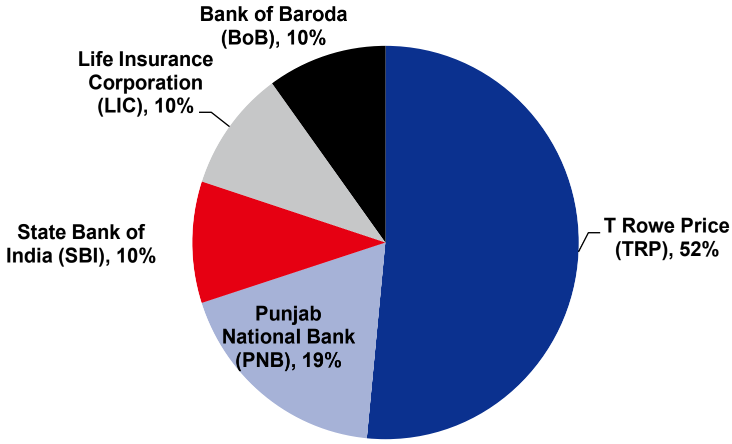


SOURCES: INCRED RESEARCH, COMPANY REPORTS

T Rowe Price bought a majority stake in UTI Trustee Company

Post-IPO, T Rowe Price also acquired a majority stake in UTI Trustee Company, a custodian of UTI AMC, from public sector banks and LIC. Under the deal, SBI, Bank of Baroda and LIC sold ~8.6% stake each in UTI Trustee Company to T Rowe Price, who now owns ~51.5% stake in the custodian company.

Figure 107: Shareholding pattern of UTI Trustee Company as at end-Dec 2021



SOURCES: INCRED RESEARCH, COMPANY REPORTS

Can UTI move the NAM India way?

Nippon Life India Asset Management (NAM India) was originally a joint venture between Reliance Capital (ADAG Group) and Nippon Life Asset management but after the former's financial problems impacted the AMC business, Nippon Life bought the entire stake (~75% as on date) from ADAG Group and restructured the entire organisation successfully

AMCs in India have huge scope for growth

In India, with the Covid-19 pandemic reinforcing the importance of financial savings among Indian households and given the under-penetration of mutual funds, the outlook remains buoyant. AMC remains a heavily concentrated industry with a few large players enjoying a major portion of market share.

UTI AMC, being the eighth-largest AMC in India with a significant access to government float, has decent scope for growth in coming years. Considering improving efficiency of UTI AMC, including fund performance, T Rowe Price (already an investment manager) can opt to buy out majority stake from public sector banks (which is the easiest route) and can privatise UTI AMC, similar to NAM India.

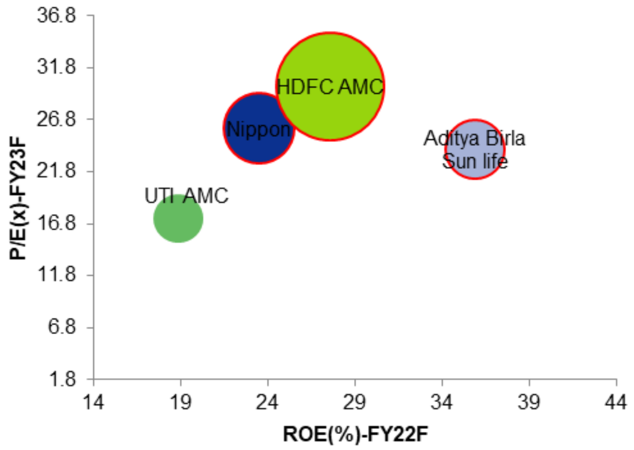
Although we do not give certain probability to the prospect and neither accommodate this aspect into our financial numbers and assumptions, we remain assertive to any such action in future.

Outlook and valuation

We have plotted all listed AMCs, based on their forward RoEs, on a valuation table. We are considering one-year and two-year forward multiples to assess valuation premium or else discounting of all listed players.

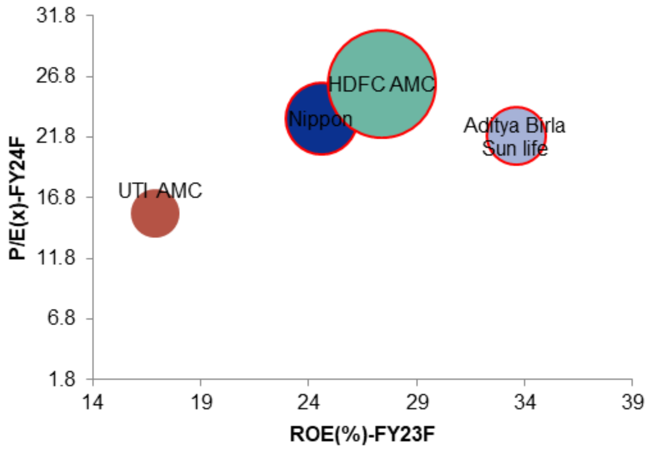
Comparison based on P/E to RoE basis

Figure 108: RoE in FY22F compared to FY23F P/E



SOURCES: BLOOMBERG, INCRED RESEARCH ESTIMATES

Figure 109: RoE in FY23F compared to FY24F P/E



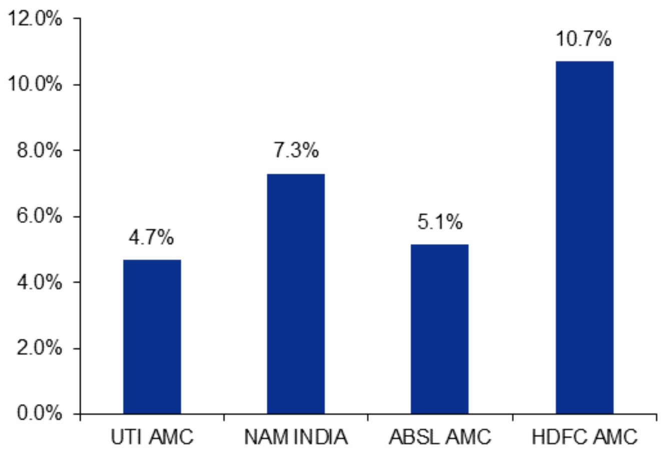
SOURCES: BLOOMBERG, INCRED RESEARCH ESTIMATES

UTI AMC trades below the trendline; multiple expansion likely

On comparing listed AMCs based on price/earnings and RoE multiple, we observe that UTI AMC is trading at a steep discount to peers. With overall improvement in business momentum led by market share gain for UTI AMC on the equity fund AUM front coupled with a rise in PAT yield led by operating leverage, we do see a probable expansion in multiple for UTI AMC

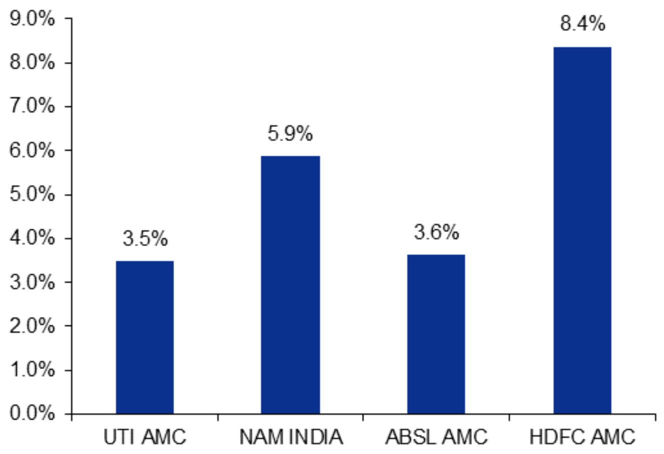
Market capitalisation as a % of AUM

Figure 110: Current market cap to 3QFY22 AUM (%)



SOURCES: INCRED RESEARCH, COMPANY REPORTS

Figure 111: Current market cap to FY24F AUM (%)



SOURCES: INCRED RESEARCH, COMPANY REPORTS

We are confident of UTI AMC's ability to turn around and leverage better to improve overall returns. We initiate coverage on UTI AMC with Add rating and a TP of Rs1,100, based on dividend discounting methodology, corresponds to ~18.9x P/E at FY24F EPS and ~4.9% FY24F AUM.

Our assumption of the cost of equity at 11% is based on a risk-free rate of 6%, risk premium of 6% and beta of 0.8. We have taken terminal growth as 5%, which is the expected perpetual growth rate of India's GDP.

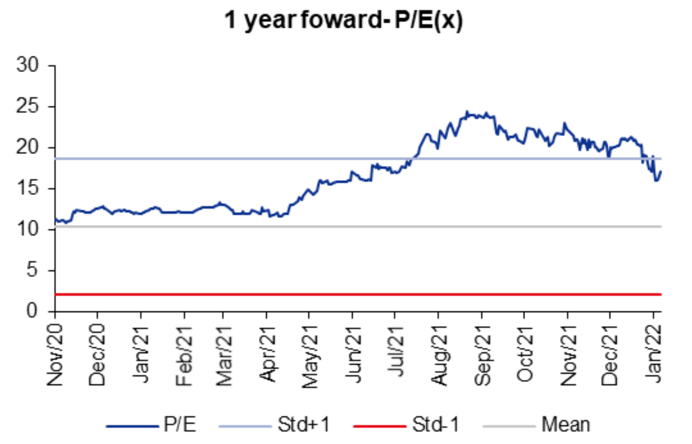
Figure 112: UTI AMC valuation

Valuation	
Cost of equity (%)	11
Dividend payout ratio (%)	60%
Terminal growth (%)	5%
Present value of free cash flow (Rsm)	1,34,162
Outstanding shares(m)	127
Target price per share (Rs)	1,100
EPS(Rs)	57
P/E(x)	19

SOURCES: INCRED RESEARCH, ESTIMATES COMPANY REPORTS

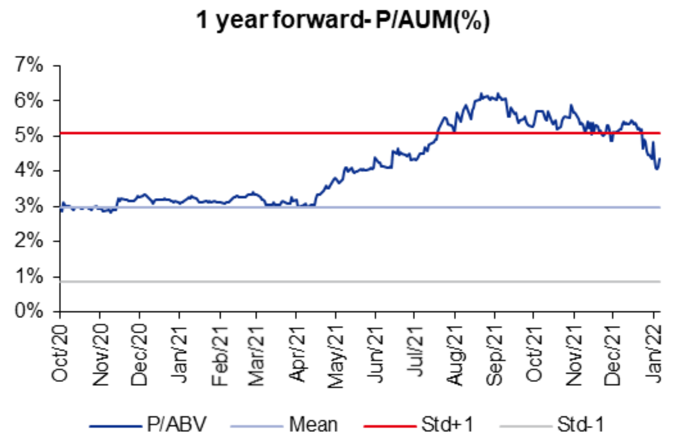
Historical valuation band for UTI AMC

Figure 113: One-year forward P/E (x) band with standard deviation



SOURCES: INCRED RESEARCH, BLOOMBERG

Figure 114: One-year forward P/AUM (%) band with standard deviation



SOURCES: INCRED RESEARCH, BLOOMBERG

Peer comparison

Figure 115: Peer comparison

Indian Peers	BBG ticker	Rating	Closing Price (LC)	Target Price	Mcap (US$ bn) Current	AUM(US$bn) FY22F	AUM(US$bn) FY23F	PAT (US$m) FY22F	PAT (US$m) FY23F	P/E FY22F	P/E FY23F
Nippon Life	RNAM	Add	300	380	2.7	38	38	103	115	27	24
HDFC AMC	HDFCAMC	Hold	2,082	2,300	6.3	60	60	189	203	33	31
AB AMC	ABSLAMC	Add	500	650	2.0	42	47	92	111	21	18
UTI AMC	UTIAM	Add	847	1,100	1.5	31	35	78	88	19	17

SOURCES: INCRED RESEARCH ESTIMATES, BLOOMBERG, PRICED AT 4RD MAR 2022

Risks to our investment thesis

New distribution channel may not materialize

UTI AMC has now increased partnership with banks for distribution of mutual fund schemes. However, with a lot of new players doing the same, UTI AMC may not have business from these banks, which could slow down its growth.

Cost rationalization unlikely

Due to intense competition and digitalization, UTI AMC may need to spend more on customer acquisition which can delay the benefits of operating leverage, leading to lower profitability.

Lower growth in B-30 cities can lead to lower margins

UTI AMC charges 30bp of fees higher from B-30 cities (beyond Top-30 cities) due to lower growth in B-30 cities, which can lead to lower profitability.

Higher marketing and customer acquisition cost can dent profitability

UTI AMC doesn't have the parentage of a bank, like other bank-led AMCs, as a result of which it may need to spend more on customer acquisition which could led to a deterioration in profitability.

Industry-related risk

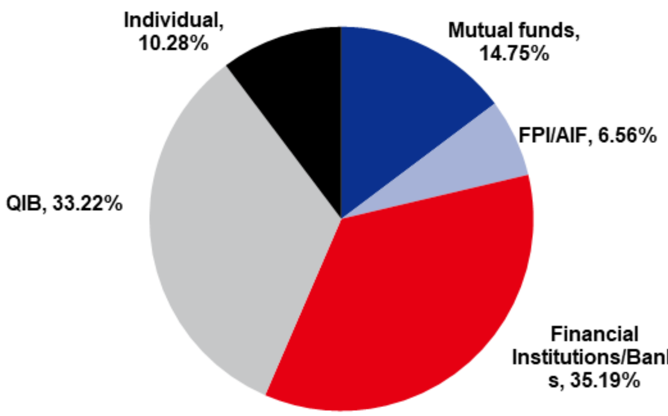
Like other AMCs, UTI AMC is exposed to the risk of lower inflows due to any downcycle, pressure on yields due to a drop in expense ratio, and the risk of regulatory intervention.

Figure 116: Key management profile as at end-Dec 2021

Name	Designation	Background
Dinesh Kumar Mehrotra	Chairman	Mr. Dinesh Kumar Mehrotra previously served as chairman and managing director of LIC. He holds a B.Sc. (Honours) degree from the University of Patna.
Imtaiyazur Rahman	CEO/Wholetime Director	Mr. Imtaiyazur Rahman is chief executive officer and whole-time director of the company. He has more than 30 years of experience. He is a science graduate, fellow member of Institute of Cost Accountants of India and Institute of Company Secretaries of India, and Certified Public Accountant (USA)
Vetri Subramaniam	CIO	He holds a B. Com degree from University of Madras and a Post Graduate Diploma in Management from Indian Institute of Management, Bengaluru. He joined the company with effect from 23 Jan 2017. Prior to this, he was associated with Invesco Asset Management Private Limited, Motilal Oswal Securities Limited, Kotak Mahindra Asset Management Company Limited, SSKI Investor Service Private Limited and Kotak Mahindra Finance Limited.
Peshotan Dastoor	Group President & Head – Sales	He holds double post-graduation qualification - Master of Commerce degree from University of Mumbai and Master's in Business Administration degree from Xavier's Institute of Management. He also holds the Calritas Investment Certificate from CFA Institute, USA. Mr. Dastoor joined UTI AMC on 6 May 2021, and has over 27 years of valuable experience

SOURCES: INCRED RESEARCH, COMPANY REPORTS

Figure 117: Shareholding pattern as at end-Dec 2021



SOURCES: INCRED RESEARCH, COMPANY REPORTS

BY THE NUMBERS

Profit & Loss

(Rsm)	Mar-20A	Mar-21A	Mar-22F	Mar-23F	Mar-24F
Net Interest Income					
Total Non-Interest Income	**8,900**	**11,986**	**13,698**	**15,849**	**17,600**
Operating Revenue	8,900	11,986	13,758	15,922	17,709
Total Non-Interest Expenses	**(5,151)**	**(5,598)**			
Pre-provision Operating Profit	3,413	6,030	6,909	8,607	9,856
Total Provision Charges					
Operating Profit After Provisions	3,413	6,030	6,909	8,607	9,856
Pretax Income/(Loss) from Assoc.					
Operating EBIT (incl Associates)	3,413	6,030	6,909	8,607	9,856
Non-Operating Income/(Expense)					
Profit Before Tax (pre-EI)	3,413	6,030	6,909	8,607	9,856
Exceptional Items					
Pre-tax Profit	3,413	6,030	6,909	8,607	9,856
Taxation	(664)	(1,087)	(1,036)	(2,152)	(2,464)
Consolidation Adjustments & Others					
Exceptional Income - post-tax					
Profit After Tax	2,749	4,943	5,873	6,455	7,392
Minority Interests	(35)	(2)	(2)	(2)	(2)
Pref. & Special Div					
FX And Other Adj.					
Net Profit	2,715	4,941	5,871	6,453	7,390
Recurring Net Profit					

Balance Sheet

(Rsm)	Mar-20A	Mar-21A	Mar-22F	Mar-23F	Mar-24F
Total Gross Loans					
Liquid Assets & Invst. (Current)					
Other Int. Earning Assets					
Total Gross Int. Earning Assets					
Total Provisions/Loan Loss Reserve					
Total Net Interest Earning Assets					
Intangible Assets	126	117			
Other Non-Interest Earning Assets	**3,166**	**3,473**	**3,667**	**3,763**	**3,862**
Total Non-Interest Earning Assets	**6,903**	**7,120**	**7,119**	**7,283**	**7,453**
Cash And Marketable Securities	1,193	2,060	3,781	5,245	6,692
Long-term Investments	**23,558**	**27,469**	**28,842**	**30,284**	**31,799**
Total Assets	31,653	36,649	39,742	42,813	45,944
Customer Interest-Bearing Liabilities					
Bank Deposits					
Interest Bearing Liabilities: Others					
Total Interest-Bearing Liabilities					
Banks Liabilities Under Acceptances					
Total Non-Interest Bearing Liabilities	3,822	4,280	4,435	4,600	4,773
Total Liabilities	3,822	4,280	4,435	4,600	4,773
Shareholders Equity	27,723	32,259	35,196	38,102	41,060
Minority Interests	**108**	**111**	**111**	**111**	**111**
Total Equity	27,831	32,370	35,307	38,213	41,171

Key Ratios

	Mar-20A	Mar-21A	Mar-22F	Mar-23F	Mar-24F
Total Income Growth					
Operating Profit Growth	(28.0%)	70.4%	115.4%	15.7%	11.2%
Pretax Profit Growth	(31%)	77%	15%	25%	15%
Effective Tax Rate	19.4%	18.0%	15.0%	25.0%	25.0%
Net Dividend Payout Ratio	32.7%	43.6%	50.0%	55.0%	60.0%
Return On Average Assets	8.79%	14.47%	15.37%	15.63%	16.65%

SOURCES: INCRED RESEARCH, COMPANY REPORTS

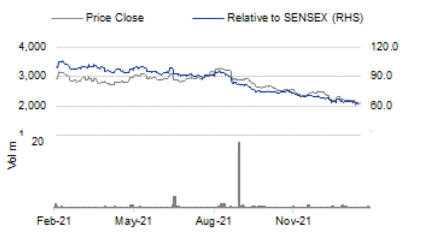
India

HOLD *(Initiating coverage)*

Consensus ratings*:	Buy 15	Hold 7	Sell 2

Current price:	Rs2,082
Target price:	Rs2,300
Previous target:	NA
Up/downside:	10.5%
EIP Research / Consensus:	-15.1%
Reuters:	
Bloomberg:	HDFCAMC IN
``Market cap:	US$5,828m
	Rs443,901m
Average daily turnover:	US$18.7m
	Rs1427.2m
Current shares o/s:	212.8m
Free float:	46.0%

**Source: Bloomberg*



Source: Bloomberg

Price performance	1M	3M	12M
Absolute (%)	(9.5)	(19.3)	(34.0)
Relative (%)	(4.0)	(14.4)	(38.8)

Major shareholders	% held
HDFC	52.0
ABRDN INVESTMENT	16.0
LIC	6.0

HDFC AMC

Outperformance to drive market share gains

- HDFC AMC manages elevated individual flows, backed by strong brand recognition, leading to best-in-class returns but market share fall is a concern.
- We factor in a revenue CAGR of 14.9% backed by overall AUM CAGR of ~11.6% whereas PAT is expected to grow by ~11.3% over FY21-24F.
- Initiate coverage with Hold rating and a TP of Rs2,300 based on Dividend Discount model, corresponding to ~26.8x FY24F P/E and ~8.5% FY24F AUM.

Preferred among retail investors due to strong brand recognition

HDFC AMC manages the third-largest AUM in the industry with ~11.6% market share as at end-Dec 2021, as per AMFI. The AMC's AUM grew at ~12.5% CAGR over FY18-21 with equity AUM at ~41% of total AUM due to higher retail traction which remains dominant at ~59.4% as against industry average of ~55%, as per company filing. The share of equity fund AUM remains heavy at ~45.7% of total AUM as at Dec 2021-end.

Loses market leadership in equity flows, AMC already in action mode

Although HDFC AMC has historically heavily relied on equity flows (mainly led by individual investors), the loss of market leadership position remains a concern. The same is partially attributable to new entrants gaining traction whereas a part of it is also due to underperformance of various schemes launched by the AMC. To tackle this loss, management has already been in action mode - from launching new investment schemes to broadening the product profile (including for passive funds). However, we believe the AMC needs to resolve its underperformance problem to regain lost traction in equity funds.

Healthy profitability despite the pressure on yields

In line with most peers, HDFC AMC witnessed a decline in yields due to various reasons including SEBI's cap on total expense ratio (TER) and a decreased share of equity funds in total AUM, etc. Going ahead, we are factoring in muted revenue yields, despite rising traction in equity flows, due to consistent regulatory pressure. However, we believe the benefit of lower opex to AUM will continue and lead to steady profitability for the AMC.

Initiate coverage with Hold rating and TP of Rs2,300

We initiate coverage on HDFC AMC with Hold rating and a TP of Rs2,300, based on dividend discounting, corresponding to ~26.8x FY24F P/E and ~8.5% FY24F AUM. Our target price is based on the assumptions of the cost of equity at 11.7% and a terminal growth rate of 5%. To sustain premium valuation and gain a further re-rating, HDFC AMC needs to start regaining its lost market share. As there are peers offering similar returns with relatively attractive valuations, HDFC AMC is expected to remain under pressure, at least till we see a decent regain of lost market share. Key upside risk: Steep outperformance of equity funds. Key downside risks: Top management churn, merger and acquisition or M&A and industry-related risks.

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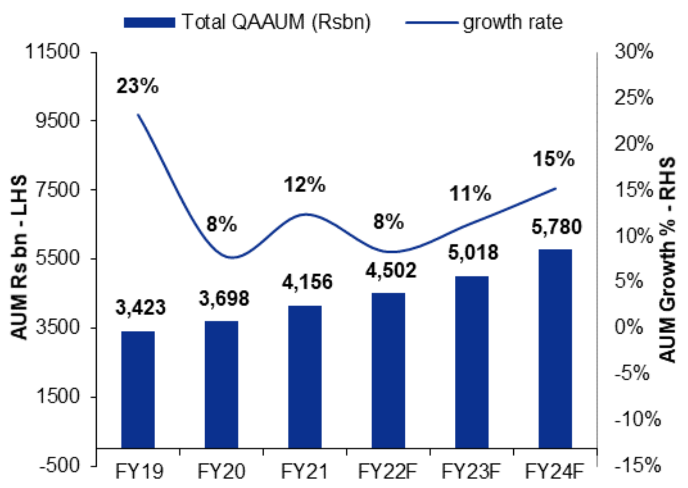
Financial Summary	Mar-20A	Mar-21A	Mar-22F	Mar-23F	Mar-24F
Total Non-Interest Income (Rsm)	21,435	22,017	25,103	28,037	31,522
Operating Revenue (Rsm)	21,435	22,017	25,103	28,037	31,522
Net Profit (Rsm)	12,625	13,258	14,235	16,207	18,300
Core EPS (Rs)	59.33	62.30	66.89	76.16	86.00
Core EPS Growth	36%	5%	7%	14%	13%
FD Core P/E (x)	35.09	33.41	31.12	27.33	24.20
DPS (Rs)	28.00	34.00	40.11	45.66	51.56
Dividend Yield	1.35%	1.63%	1.93%	2.19%	2.48%
BVPS (Rs)	189.3	224.4	251.2	281.7	316.1
P/BV (x)	10.99	9.27	8.29	7.39	6.59
ROE	35.6%	30.1%	28.1%	28.6%	28.8%
% Change In Core EPS Estimates					
InCred Research/Consensus EPS (x)			1.01	1.02	1.00

SOURCES: INCRED RESEARCH ESTIMATES, COMPANY REPORTS

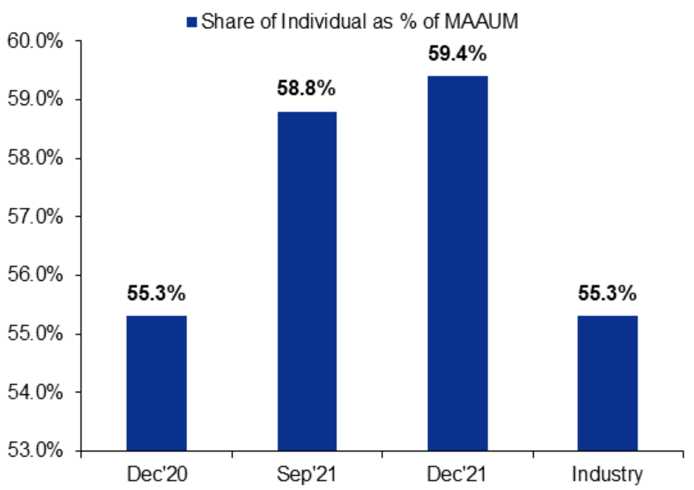
HDFC AMC- key charts

Figure 118: Retail-driven AUM momentum to continue



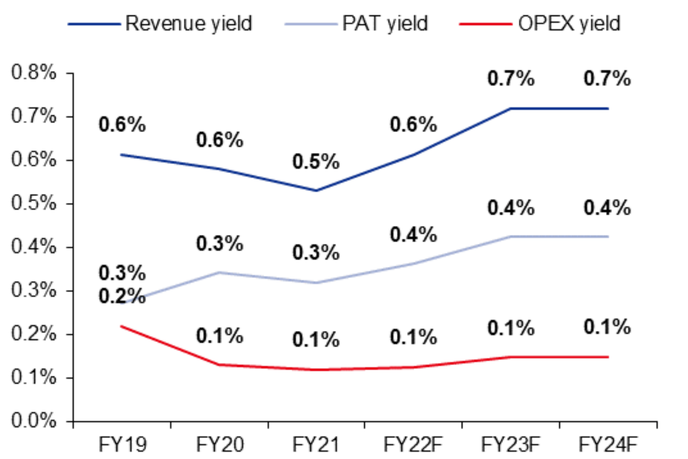
SOURCES: INCRED RESEARCH ESTIMATES, COMPANY REPORTS

Figure 119: Diversified AUM mix with a rising share of equity funds



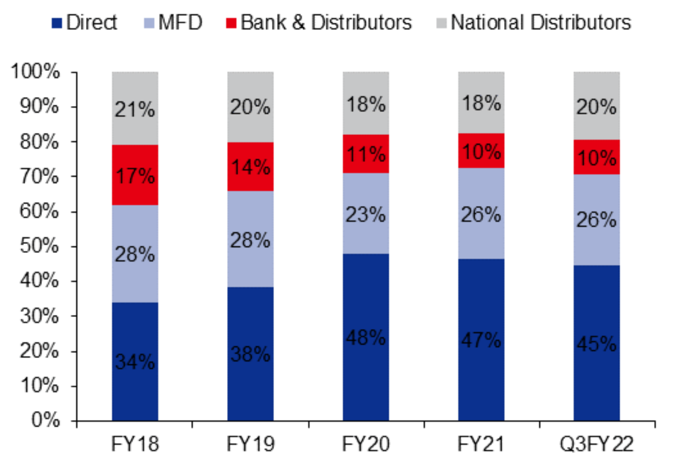
SOURCES: INCRED RESEARCH, COMPANY REPORTS

Figure 120: Steady PAT led by healthy operating efficiency



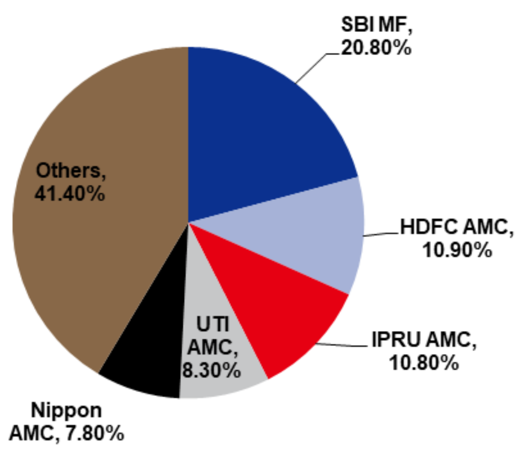
SOURCES: INCRED RESEARCH ESTIMATES, COMPANY REPORTS

Figure 121: Mutual fund distributors (MFDs) remain key contributors to distribution strength



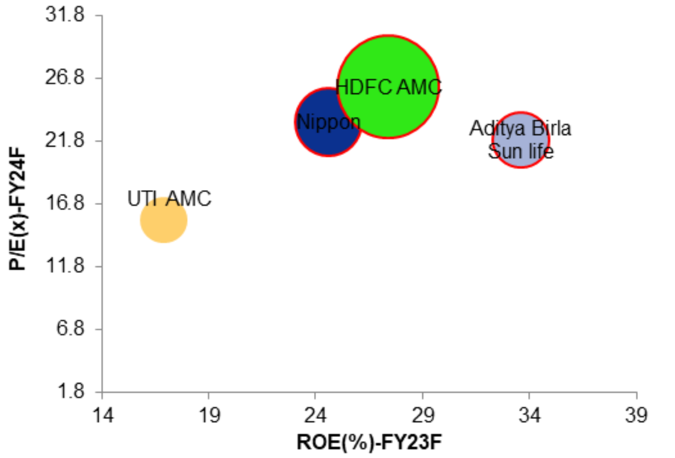
OURCES: INCRED RESEARCH, COMPANY REPORTS

Figure 122: HDFC AMC remains the second-largest AMC in B-30 cities, as per AMFI



SOURCES: INCRED RESEARCH, AMFI

Figure 123: HDFC AMC trades at expensive valuation compared to peers



SOURCES: INCRED RESEARCH, COMPANY REPORTS, BLOOMBERG ESTIMATES

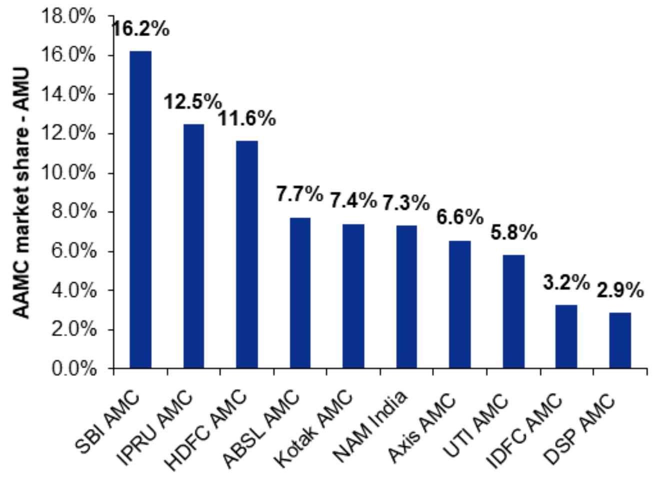
Pioneer among AMCs; strong retail base

HDFC AMC has been the pioneer among asset management companies in India in the private segment, dominating in AUM of debt as well as equity funds. Started in 1999, HDFC AMC was set up as a joint venture between Housing Development Finance Corporation Limited (HDFC Limited) and ABRDN Investment Management Limited (erstwhile known as Standard Life Investments Limited). It was the first AMC to come out an initial public offer (IPO) and became a public-listed entity in Aug 2018.

Equity-driven AUM growth; low prominence in ETFs

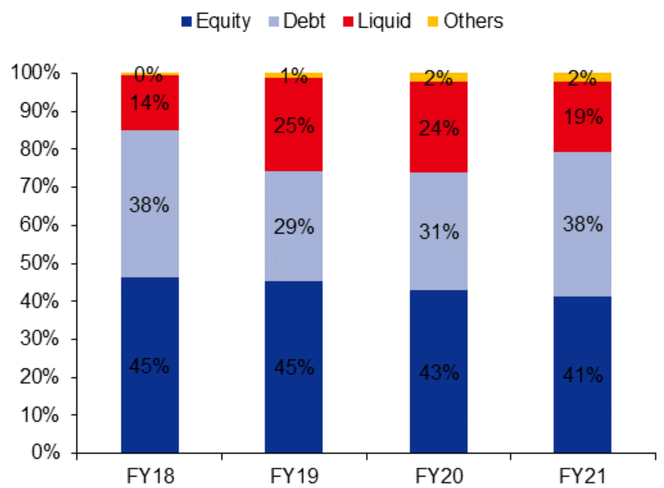
The company's AUM grew at ~12.5% CAGR over FY18-21 with the proportion of equity AUM at ~41% due to higher traction in retail individual investors, which remains dominant. Further, AMC's overall market share stood at ~11.6% as at Dec 2021-end, making it the third-largest equity fund manager in India.

Figure 124: Market share as at end-Dec 2021



SOURCES: INCRED RESEARCH, COMPANY REPORTS

Figure 125: AUM break-up for HDFC AMC

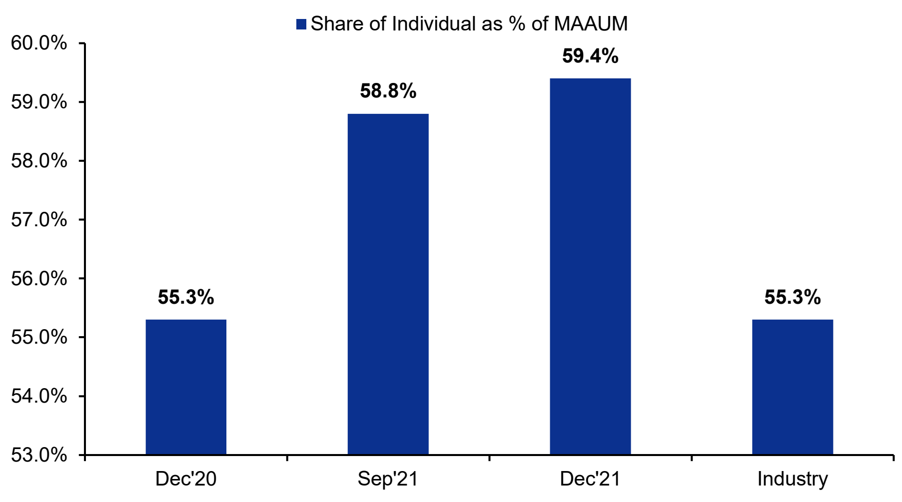


SOURCES: INCRED RESEARCH, COMPANY REPORTS

Preferred choice among retail invetsors

The business mix for HDFC AMC is granular with a higher reliance on retail/ individual investors (~59.4%) as against industry average of ~55%. These investors are normally sticky in nature, protecting against market fluctuations and have a higher level of persistency.

Figure 126: HDFC AMC has managed a better share of retail investor participation

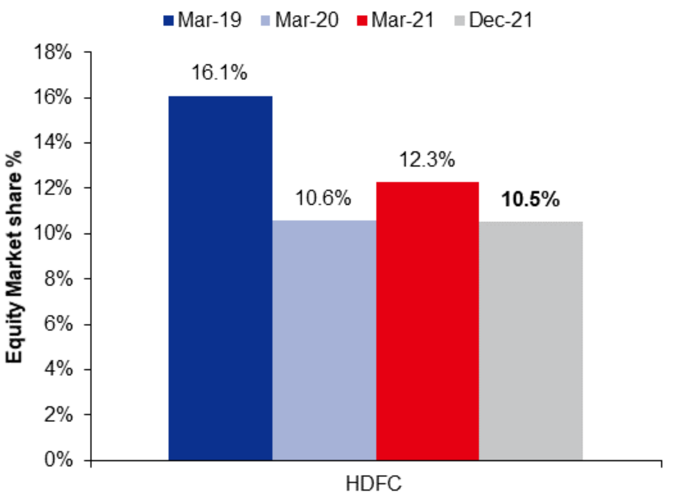


SOURCES: COMPANY REPORTS, INCRED RESEARCH

Market share loss in equity funds is a concern

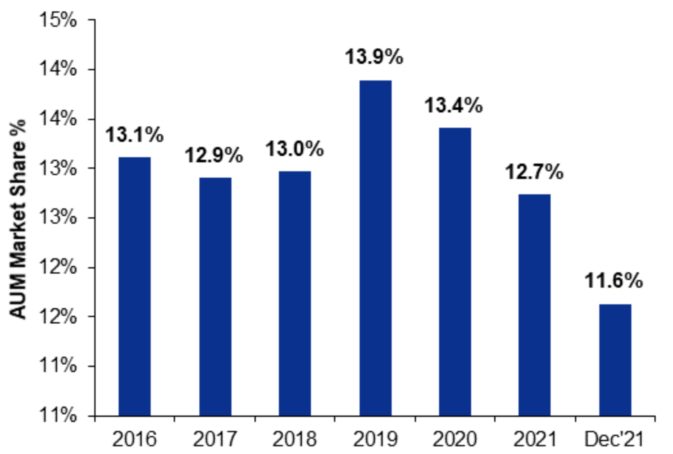
Although HDFC AMC has historically heavily relied on equity fund inflow (mainly led by individual investors), the AMC has lost its market leadership position. This is partly attributable to new entrants, resulting in extreme competition and rising penetration whereas a part of it is also due to underperformance of various schemes introduced by the AMC. Market share loss in equity funds has also impacted overall AUM share of the AMC.

Figure 127: Movement in equity fund market share of HDFC AMC



SOURCES: AMFI, INCRED RESEARCH

Figure 128: Movement in HDFC AMC's market share over the years



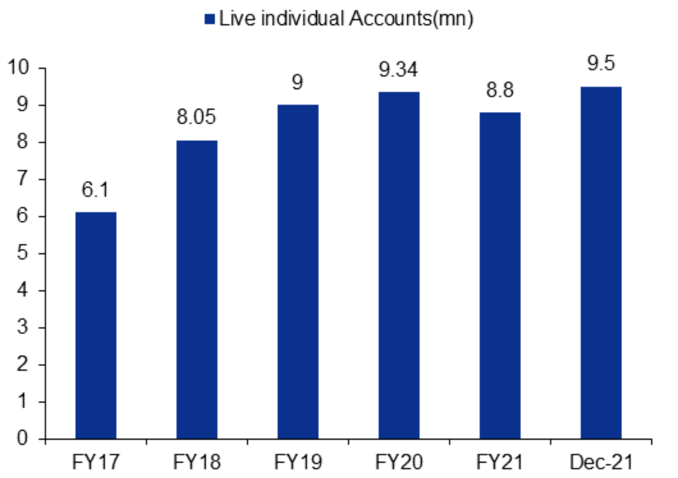
SOURCES: AMFI, INCRED RESEARCH

Management in action mode to regain lost share

The AMC's management has been highlighting its efforts on regaining lost market share for quite some time, which ranged from launching various new investment schemes to broadening its product profile in passive funds (HDFC AMC prefers direct equity over passive investments).

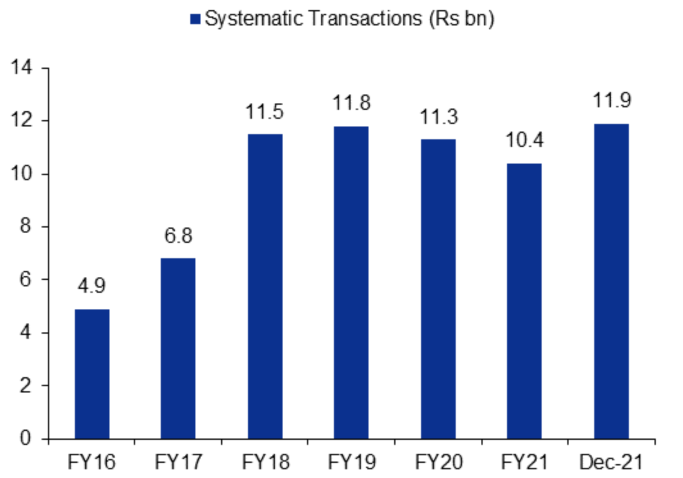
Its approach towards retail investors has also been improving, focusing on B-30 cities (beyond Top-30 cities) and improving SIP inflow. However, we are of the opinion that the AMC needs to resolve its underperformance to regain lost traction in equity funds.

Figure 129: Regains traction in live individual accounts post Covid-19 pandemic



SOURCES: INCRED RESEARCH, COMPANY REPORTS

Figure 130: Systematic inflows also are at pre-Covid level now, after declining in FY21

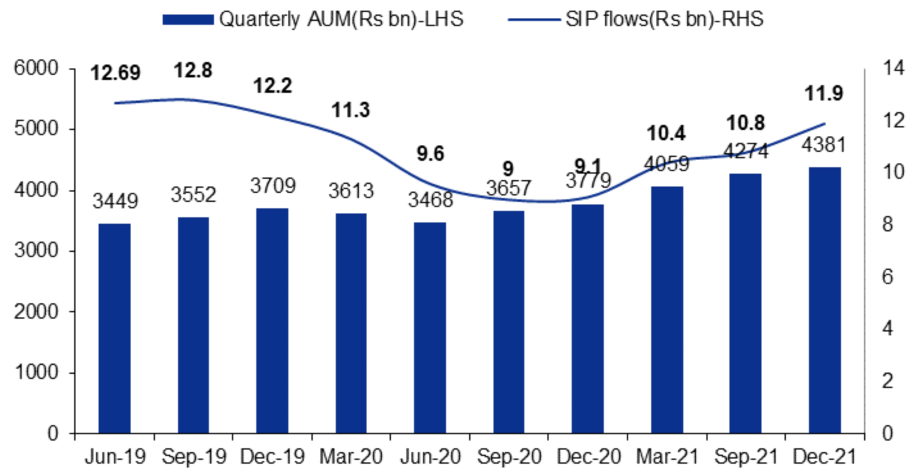


SOURCES: INCRED RESEARCH, COMPANY REPORTS

SIP flow regains traction gradually

HDFC AMC is witnessing a gradual revival in SIP flows, after losing traction during the pandemic. Systematic investment plan (SIP) AUM for HDFC AMC has increased from Rs4,059bn as at end-Mar 2020 to Rs4,381bn as at end-Dec 2021. SIPs are generally done in equity or hybrid funds and rising traction in them will further support equity AUM of the AMC.

Figure 131: SIP folios regain traction in recent quarters



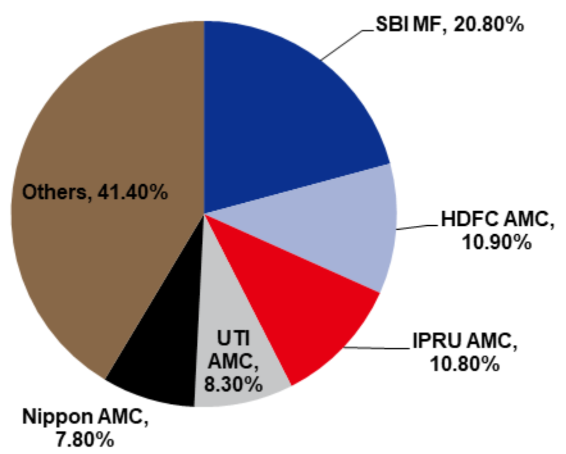
SOURCES: INCRED RESEARCH, COMPANY REPORTS

Although the pandemic has adversely affected several businesses, large or small, SIP flows in the last fiscal year were relatively stable. This validates the effectiveness of the financial literacy campaign by MF industry and the Association of Mutual Funds in India (AMFI). The campaign focused on making people aware of the importance of proactivity over reactivity while avoiding impulsive decisions based on temporary events.

HDFC AMC remains the second-largest AMC in B-30 cities

HDFC AMC remains second-largest player in B-30 cities (beyond Top-30 cities) based on mutual fund AUM with a presence across `98% postal pin codes in India with 149 branches in B-30 cites against 227 total branches. This trend will ensure more stickiness of the flows, even in case of a volatile market trend.

Figure 132: HDFC AMC has the second-largest presence in B-30 cities in India



SOURCES: INCRED RESEARCH, COMPANY REPORTS

Post Covid-19 pandemic, HDFC AMC is witnessing improved traction in sticky retail flows through low-ticket SIPs. We remain confident of a resurgence in equity fund dominance for the company in coming years.

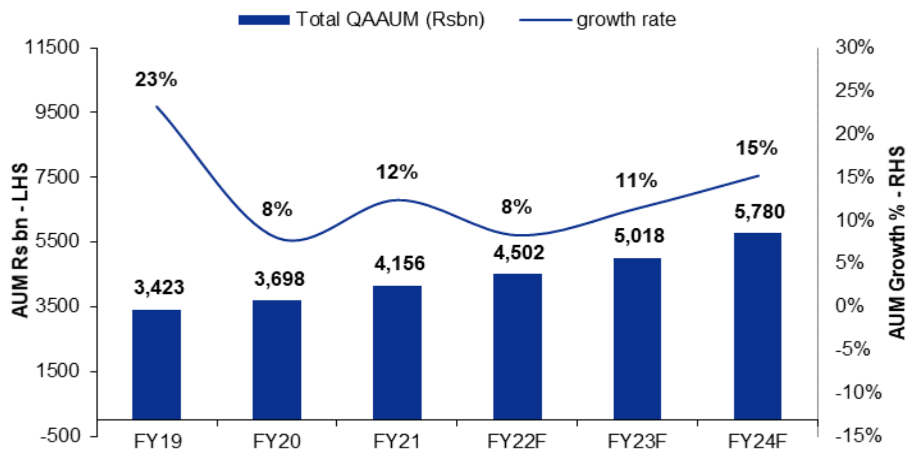
Healthy profitability despite yield pressures

In line with most peers, HDFC AMC witnessed a decline in yields due to SEBI's cap on total expense ratio (TER) and a decreased share of equity funds in total AUM. Consistent outflow of funds from old regime funds and replacing the same with new regime funds also resulted in consistent pressure on overall yields.

Revenue growth to remain in sync with AUM growth

Going ahead, we are factoring in a muted improvement in revenue yields of HDFC AMC, despite rising traction in equity fund inflow, backed by consistent pressure on equity flow along with rising traction in low-yield passive funds. We are factoring in a revenue CAGR of 13.5% over FY21-24F backed by overall AUM CAGR of ~10.5% and steady yields going ahead. We are factoring in equity AUM to rise to ~46% of overall AUM as against ~41% in FY21.

Figure 133: Trend in AUM growth over FY21-24F

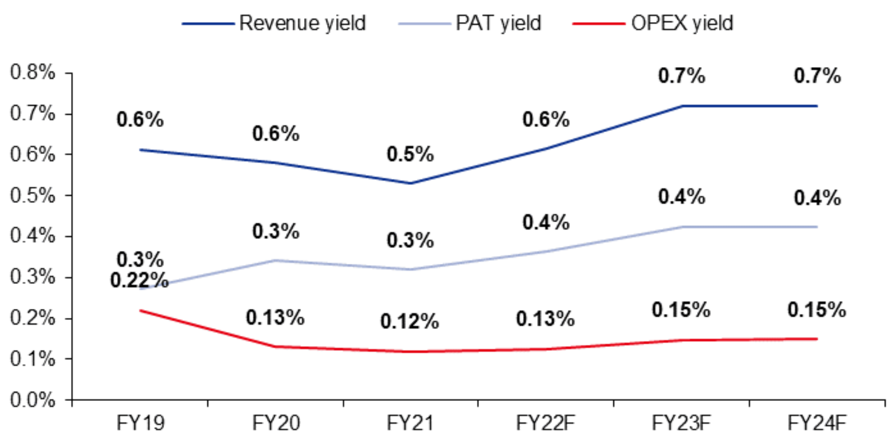


SOURCES: INCRED RESEARCH ESTIMATES, COMPANY REPORTS

Healthy profits amid tight operating expenses to continue

HDFC AMC has focused on cost rationalization since inception, and opex to AUM has decreased from 20bp in FY20 to 15bp in FY21. These cost benefits also accrued due to the benefits of operating leverage on the back of digitalization. We believe the benefits of lower opex to AUM will continue going ahead.

Figure 134: Operating leverage to offset pressure of revenue yield on profitability



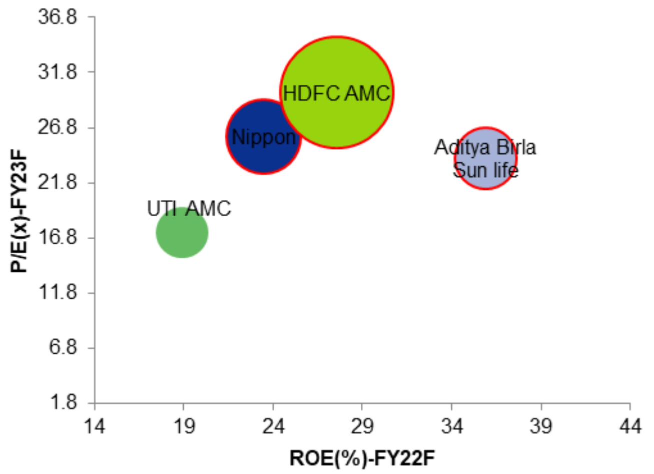
SOURCES: INCRED RESEARCH ESTIMATES, COMPANY REPORTS

Outlook & valuation

We have plotted all listed AMCs, based on their forward ROEs, on a valuation table. We are considering one-year and two-year forward multiples to assess valuation premium or else discounting of all listed players.

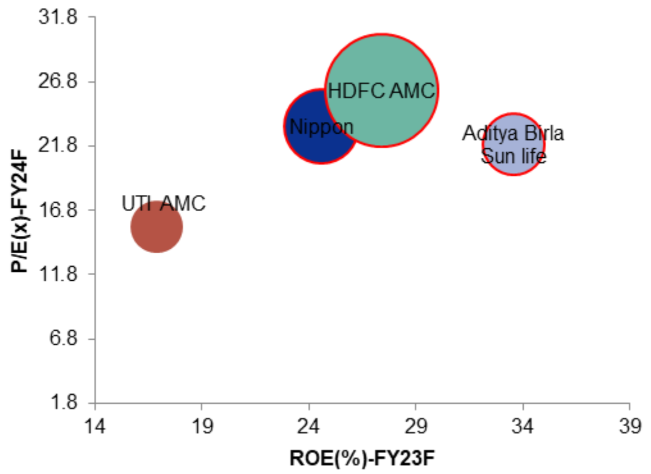
Comparison based on P/E to RoE basis

Figure 135: RoE in FY22F compared to FY23F P/E



SOURCES: BLOOMBERG, INCRED RESEARCH ESTIMATES

Figure 136: RoE in FY23F compared to FY24F P/E



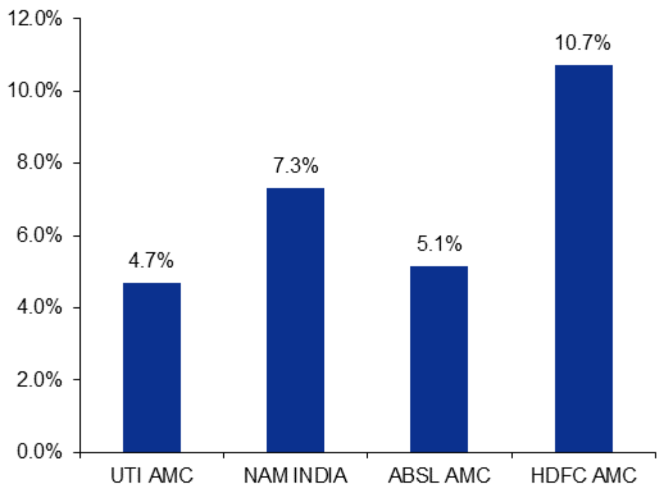
SOURCES: BLOOMBERG, INCRED RESEARCH ESTIMATES

HDFC AMC trades far above the trendline

On comparing listed AMCs, based on price/earnings and RoE multiple, we observe that HDFC AMC remains expensive compared to peers, already trading above the trendline. The stock has witnessed a sharp correction in last couple of quarters amid consistent loss in market share, which again remains a cause of concern when comparing the valuation.

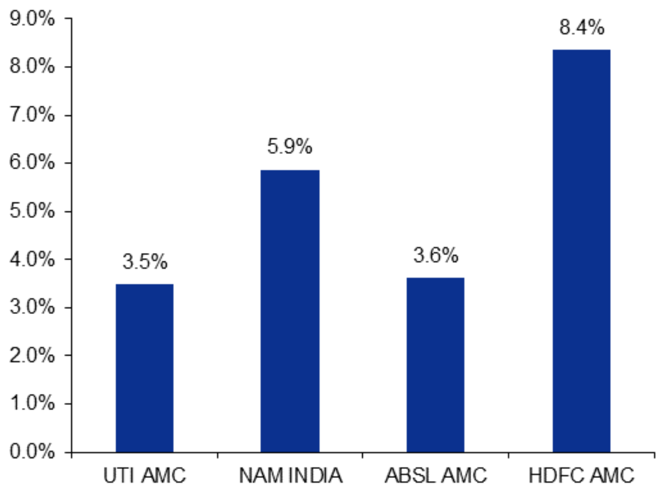
Market capitalisation as a % of AUM

Figure 137: Current market cap to 3QFY22 AUM (%)



SOURCES: INCRED RESEARCH, COMPANY REPORTS

Figure 138: Current market cap to FY24F AUM (%)



SOURCES: INCRED RESEARCH, COMPANY REPORTS

Even on price-to-AUM basis, HDFC AMC is available at ~8.4% of FY24F AUM which is the highest compared to peers. HDFC AMC needs to accelerate the AUM growth momentum (again by regaining lost share) to command a further premium from here on.

Initiating coverage on HDFC AMC with Hold rating

We initiate coverage on HDFC AMC with Hold rating and a TP of Rs2,300 based on dividend discounting model assuming cost of equity at ~11.7% and terminal growth of ~5%, corresponding to ~26.8x at FY24F P/E and ~8.5% FY24F AUM.

Our assumption of the cost of equity at 11.7% is based on a risk-free rate of 6%, risk premium of 6% and beta of 0.9. We have taken terminal growth as 5%, which is the expected perpetual growth rate of India's GDP.

Figure 139: Valuation of HDFC AMC

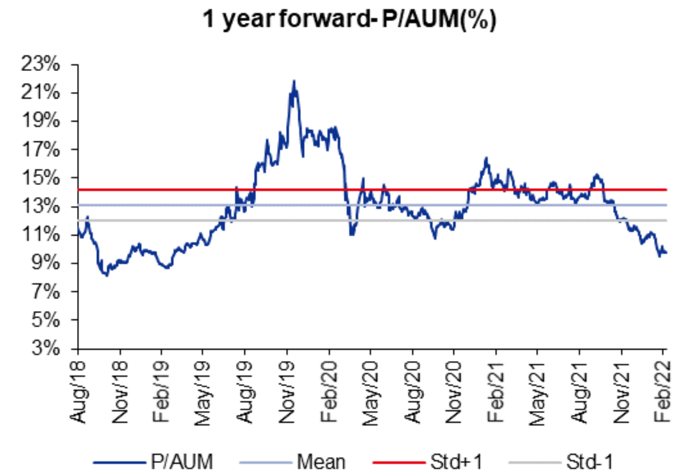
Valuation	
Cost of equity (%)	11
Dividend payout ratio (%)	80%
Terminal growth (%)	5%
Present value of free cash flow (Rsm)	5,14,553
Outstanding per share(m)	213
Target price per share (Rs)	2,300
EPS(Rs)	86
P/E(x)	28

SOURCES: INCRED RESEARCH ESTIMATES, COMPANY REPORTS

To sustain premium valuation and gain a further re-rating, HDFC AMC needs to start regaining its lost market share. As there are peers offering similar returns with relatively attractive valuations, HDFC AMC is expected to remain under pressure, at least till we see a decent regain in lost market share.

Historical valuation band of HDFC AMC

Figure 140: One-year forward P/AUM with standard deviation



SOURCES: INCRED RESEARCH, COMPANY REPORTS

Figure 141: One-year forward P/E with standard deviation

SOURCES: INCRED RESEARCH, COMPANY REPORTS

Peer comparison

Figure 142: Peer comparison as on Feb-22 end

Indian Peers	BBG ticker	Rating	Closing Price (LC)	Target Price	Mcap (US$ bn) Current	AUM(US$bn) FY22F	AUM(US$bn) FY23F	PAT (US$m) FY22F	PAT (US$m) FY23F	P/E FY22F	P/E FY23F
Nippon Life	RNAM	Add	300	380	2.7	38	38	103	115	27	24
HDFC AMC	HDFCAMC	Hold	2,082	2,300	6.3	60	60	189	203	33	31
AB AMC	ABSLAMC	Add	500	650	2.0	42	47	92	111	21	18
UTI AMC	UTIAM	Add	847	1,100	1.5	31	35	78	88	19	17

SOURCES:INCRED RESEARCH ESTIMATES BLOOMBERG: PRICED AT 4RD MAR 2022

Risks to our investment thesis

Key downside risks

Churn in key management

HDFC AMC has a stable team of investment managers. Any significant churn can lead to loss of investor confidence in the AMC.

Inappropriate merger and acquisition activity

HDFC AMC generates a lot of cash and thus there are merger and acquisition or M&A possibilities. However, M&A done at a higher valuation can be negative to HDFC AMC's valuation.

Continued underperformance can lead to further market share loss

HDFC AMC has lost market share due to underperformance of equity funds. If the underperformance continues, then it could result in further market share loss.

Demand disruption due to Covid-related lockdowns

Retail investor remains a key participant in case of AMCs and any disruption created by Covid-19 pandemic-induced lockdowns would be a risk to new customer growth and profitability due to higher claims, in our view.

Industry-related risk

Like other AMCs, HDFC AMC is exposed to the risk of lower inflows due to any downcycle, pressure on yields due to a drop in expense ratio, and the risk of regulatory intervention.

Key upside risks

Steep outperformance of equity funds

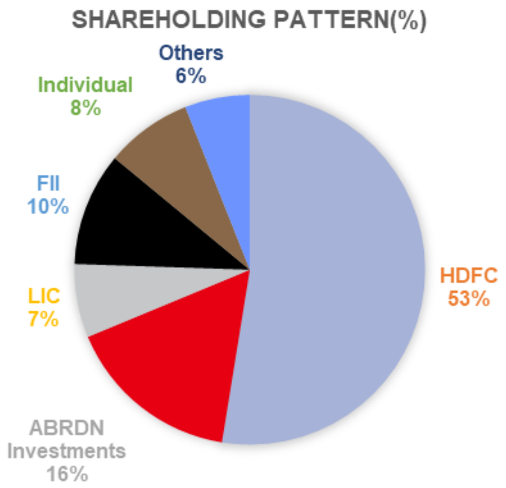
HDFC AMC has witnessed market share loss due to underperformance of its equity funds. If its equity funds outperform, then it can register market share gains and good fund inflows.

Figure 143: Key management profile as at end-Dec 2021

Name	Designation	Background
Navneet Munot	MD & CEO	Mr. Munot has 27 years of experience in financial services. He has worked with SBI Funds, Morgan Stanely and Adiya Birla before joining HDFC AMC in Feb 2021.
Naozad Sirwalla	CFO	Mr. Sirwalla has over 26 years of experience and comes to HDFC AMC from Lupa Systems Investment Advisors. He has worked with KKR India for over six years. Prior to that, he worked with Kotak Group, including Kotak Investment Advisors, for over 13 years.
Prashant Jain	CIO	He holds a bachelor's degree in technology from Indian Institute of Technology, Kanpur and holds a post-graduate diploma in Management from Indian Institute of Management, Bengaluru. He is also a designated Chartered Financial Analyst from Chartered Financial Analyst Institute, USA.
Naveen Gogia	Co-Head - Sales	Naveen is a pass-out from Nottingham Trent University. He has 25 years of experience.
Rajiv Maniar	Co-Head – Sales	He is an engineer having an experience of 25 years in AMCs.

SOURCES: INCRED RESEARCH, COMPANY REPORTS

Figure 144: Shareholding pattern as at end-Dec 2021



SOURCES: INCRED RESEARCH

BY THE NUMBERS

Profit & Loss

(Rsm)	Mar-20A	Mar-21A	Mar-22F	Mar-23F	Mar-24F
Net Interest Income					
Total Non-Interest Income	**21,435**	**22,017**	**25,103**	**28,037**	**31,522**
Operating Revenue	21,435	22,017	25,103	28,037	31,522
Total Non-Interest Expenses	**(4,400)**	**(3,974)**	**(5,944)**	**(6,427)**	**(7,122)**
Pre-provision Operating Profit	16,531	17,490	19,159	21,610	24,400
Total Provision Charges					
Operating Profit After Provisions	16,531	17,490	19,159	21,610	24,400
Pretax Income/(Loss) from Assoc.					
Operating EBIT (incl Associates)	16,531	17,490	19,159	21,610	24,400
Non-Operating Income/(Expense)					
Profit Before Tax (pre-EI)	16,531	17,490	19,159	21,610	24,400
Exceptional Items					
Pre-tax Profit	16,531	17,490	19,159	21,610	24,400
Taxation	(3,906)	(4,232)	(4,924)	(5,402)	(6,100)
Consolidation Adjustments & Others					
Exceptional Income - post-tax					
Profit After Tax	12,625	13,258	14,235	16,207	18,300
Minority Interests					
Pref. & Special Div					
FX And Other Adj.					
Net Profit	12,625	13,258	14,235	16,207	18,300
Recurring Net Profit					

Balance Sheet

(Rsm)	Mar-20A	Mar-21A	Mar-22F	Mar-23F	Mar-24F
Total Gross Loans					
Liquid Assets & Invst. (Current)					
Other Int. Earning Assets					
Total Gross Int. Earning Assets					
Total Provisions/Loan Loss Reserve					
Total Net Interest Earning Assets					
Intangible Assets					
Other Non-Interest Earning Assets	**1,540**	**1,847**	**1,897**	**1,950**	**2,006**
Total Non-Interest Earning Assets	**3,370**	**3,391**	**3,198**	**3,186**	**3,180**
Cash And Marketable Securities	271	24	671	2,398	6,100
Long-term Investments	**39,445**	**47,533**	**53,236**	**58,560**	**63,245**
Total Assets	43,086	50,947	57,105	64,144	72,524
Customer Interest-Bearing Liabilities					
Bank Deposits					
Interest Bearing Liabilities: Others					
Total Interest-Bearing Liabilities					
Banks Liabilities Under Acceptances					
Total Non-Interest Bearing Liabilities	2,793	3,186	3,650	4,206	5,266
Total Liabilities	2,793	3,186	3,650	4,206	5,266
Shareholders Equity	40,293	47,761	53,455	59,938	67,258
Minority Interests					
Total Equity	40,293	47,761	53,455	59,938	67,258

Key Ratios

	Mar-20A	Mar-21A	Mar-22F	Mar-23F	Mar-24F
Total Income Growth					
Operating Profit Growth	22.8%	5.9%	6.2%	12.8%	12.9%
Pretax Profit Growth	20%	6%	10%	13%	13%
Effective Tax Rate	23.6%	24.2%	25.7%	25.0%	25.0%
Net Dividend Payout Ratio					
Return On Average Assets	33.52%	28.20%	26.35%	26.73%	26.78%

SOURCES: INCRED RESEARCH, COMPANY REPORTS

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Description:	Excellent	Very Good	Good	N/A	N/A

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ADVANC – Excellent, Certified, **AMATA** – Excellent, Certified, **ANAN** – Excellent, n/a, **AOT** – Excellent, n/a, **AP** – Excellent, Certified, **ASP** – Excellent, n/a, **AWC** – Excellent, Declared, **AU** – Good, n/a, **BAM** – Very Good, Certified, **BAY** – Excellent, Certified, **BBL** – Excellent, Certified, **BCH** – Very Good, Certified, **BCP** - Excellent, Certified, **BCPG** – Excellent, Certified, **BDMS** – Excellent, n/a, **BEAUTY** – Good, n/a, **BEM** – Excellent, n/a **BH** - Good, n/a, **BJC** – Very Good, n/a, **BLA** – Very Good, Certified, **BTS** - Excellent, Certified, **CBG** – Very Good, n/a, **CCET** – n/a, n/a, **CENTEL** – Excellent, Certified, **CHAYO** – Very Good, n/a, **CHG** – Very Good, n/a, **CK** – Excellent, n/a, **COM7** – Excellent, Certified, **CPALL** – Excellent, Certified, **CPF** – Excellent, Certified, **CPN** - Excellent, Certified, **CPNREIT** – n/a, n/a, **CRC** – Excellent, Declared, **DELTA** - Excellent, Certified, **DDD** – Excellent, n/a, **DIF** – n/a, n/a, **DOHOME** – Very Good, Declared, **DREIT** – n/a, n/a, **DTAC** – Excellent, Certified, **ECL** – Excellent, Certified, **EGCO** - Excellent, Certified, **EPG** – Excellent, Certified, **ERW** – Very Good, Certified, **GFPT** - Excellent, Certified, **GGC** – Excellent, Certified, **GLOBAL** – Excellent, n/a, **HANA** - Excellent, Certified, **HMPRO** - Excellent, Certified, **HUMAN** – Good, n/a, **ICHI** – Excellent, Certified, **III** – Excellent, Declared, **INTUCH** - Excellent, Certified, **IRPC** – Excellent, Certified, **ITD** – Very Good, n/a, **IVL** - Excellent, Certified, **JASIF** – n/a, n/a, **JKN** – n/a, Certified, **JMT** – Very Good, n/a, **KBANK** - Excellent, Certified, **KCE** - Excellent, Certified, **KEX** – Very Good, Declared, **KKP** – Excellent, Certified, **KSL** – Excellent, Certified, **KTB** - Excellent, Certified, **KTC** – Excellent, Certified, **LH** - Excellent, n/a, **LPN** – Excellent, Certified, **M** – Very Good, Certified, **MAKRO** – Excellent, Certified, **MC** – Excellent, Certified, **MEGA** – Very Good, n/a, **MINT** - Excellent, Certified, **MTC** – Excellent, Certified, **NETBAY** – Very Good, n/a, **NRF** – Very Good, Declared, **OR** – Excellent, n/a, **ORI** – Excellent, Certified, **OSP** – Excellent, n/a, **PLANB** – Excellent, Certified, **PRINC** – Very Good, Certified, **PR9** – Excellent, Declared, **PSH** – Excellent, Certified, **PTT** - Excellent, Certified, **PTTEP** - Excellent, n/a, **PTTGC** - Excellent, Certified, **QH** – Excellent, Certified, **RAM** – n/a, n/a, **RBF** – Very Good, n/a, **RS** – Excellent, Declared, **RSP** – Good, n/a, **S** – Excellent, n/a, **SAK** – Very Good, Declared, **SAPPE** – Very Good, Certified, **SAWAD** – Very Good, n/a, **SCB** - Excellent, Certified, **SCC** – Excellent, Certified, **SCGP** – Excellent, Declared, **SECURE** – n/a, n/a, **SHR** – Excellent, n/a, **SIRI** – Excellent, Certified, **SPA** – Very Good, n/a, **SPALI** - Excellent, Certified, **SPRC** – Excellent, Certified, **SSP** - Good, Certified, **STEC** – Excellent, n/a, **SVI** – Excellent, Certified, **SYNEX** – Very Good, Certified, **TCAP** – Excellent, Certified, **THANI** – Excellent, Certified, **TIDLOR** – n/a, Certified **TISCO** - Excellent, Certified, **TKN** – Very Good, n/a, **TOP** - Excellent, Certified, **TRUE** – Excellent, Certified, **TTB** - Excellent, Certified, **TU** – Excellent, Certified, **TVO** – Excellent, Certified, **VGI** – Excellent, Certified, **WHA** – Excellent, Certified, **WHART** – n/a, n/a, **WICE** – Excellent, Certified, **WORK** – Good, n/a.

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Add	The stock's total return is expected to exceed 10% over the next 12 months.
Hold	The stock's total return is expected to be between 0% and positive 10% over the next 12 months.
Reduce	The stock's total return is expected to fall below 0% or more over the next 12 months.

The total expected return of a stock is defined as the sum of the: (i) percentage difference between the target price and the current price and (ii) the forward net dividend yields of the stock. Stock price targets have an investment horizon of 12 months.

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Neutral	A Neutral rating means stocks in the sector have, on a market cap-weighted basis, a neutral absolute recommendation.
Underweight	An Underweight rating means stocks in the sector have, on a market cap-weighted basis, a negative absolute recommendation.

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Neutral	A Neutral rating means investors should be positioned with a neutral weight in this country relative to benchmark.
Underweight	An Underweight rating means investors should be positioned with a below-market weight in this country relative to benchmark.