

Vakrangee: E-commerce and rural growth

In this report we flag 1) Takeaways post our recent meeting with Vakrangee's (VKI, Not Covered) CEO; 2) Details from its 2Q17 results announced on Nov 7 and 3) Its recent tie-up with Jio where the company would be selling Jio smartphones/SIMs in its outlets. Vakrangee is characterized by: 1) Its exposure to e-commerce space given its tie-up with Amazon and 2) Its strong exposure in rural areas through its 20K stores.

2Q17: Results & conference call takeaways

Vakrangee reported 22% yoy higher revenue, driven by increased outlet rollouts. Revenues from Vakrangee Kendra's increased to 63% (53% yoy growth), while e-governance decreased to 37% (12% yoy decline in revenues). EBITDA margins came in at 23.7% (40 bps lower qoq as the contribution of Vakrangee Kendra increased). On the call, management stated that they are on track to meet their rollout targets of 35k outlets by FY'17 and 75k by 2020. In terms of incremental tie ups, the company tied up with Aramex and Delhivery for logistics business and with Reliance General and Bajaj Alliance for insurance products. The company also said that they are currently registering Rs. 75k/month of revenues from rural and Rs. 120k/month from urban centers. Vakrangee expects the pace of ATM rollouts to improve in tandem with IOCL outlets rollout.

Takeaways post company meeting

1) Vakrangee said that even though Amazon is currently active in 1k outlets, they are confident of meeting their 20k year-end target. 2) Vakrangee has installed digital signage space on a pilot basis at select outlets, and going forward expects them to be an additional source of revenue. 3) Vakrangee is looking to open 5-6k outlets through IOCL by March'17. It expects IOCL rollouts to be faster as KYC formalities for petrol pump owners are already in hand. 4) Vakrangee has stepped up tie ups with insurance agents and is likely to add further insurance companies as its partner. 5) For this year Vakrangee has committed to pay 15-25% of PAT as dividends, but does not rule out increasing dividends from next year, as the debt levels come down.

Tie-up with Jio: To help Jio improve its non-urban reach

VKI in its 2Q17 results announced that it has tied-up with the new entrant telco Jio (subsidiary of Reliance Industries) to sell LYF smartphones and its 4G SIMs. Jio is currently conducting a pilot service in 17 outlets in 3 states (Maharashtra, Rajasthan & UP). From a telco sector perspective, we believe that such a move will help improve 1) 4G penetration in non-urban areas as VKI centers are usually located in such places and cater mainly to mid-to-low-end of the market; 2) Help faster acceleration of tail of smaller telcos which usually cater to this market and may find difficult competing with Jio's unlimited voice offering.

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Takeaways from company visit

Amazon rollout to accelerate: Amazon is currently active in 1k outlets, but the company is confident of meeting its 20k outlet schedule by end of March'17. The rollout of outlets has been slow, as Amazon has to set up the logistics supply chain, which they are doing customized on the basis of where Vakrangee's outlets are located, but Vakrangee believes the rollout will gather pace once the logistics chain is in place. In terms of financials, Vakrangee believes that integration of Amazon services leads to 15% incremental income for Vakrangee from an outlet - clocking 20 orders of Rs. 500 per day, generating Gross Merchandise Value (GMVs) of Rs. 10k per month or Rs. 300k per month.

Looking to tap incremental advertisement revenue as well: In order to further monetize outlets, Vakrangee has rolled out digital signage space on a pilot basis in select outlets. As per the initiative, digital monitors display merchant advertisements at the outlets. Given that it is a test service, it is currently being offered free of cost to the advertisers. However, management says that it is garnering significant interest from merchants, who are keen to rent out the space.

Exhibit 1: Amazon category wise take rates

Category	Commission	Category	Commission
Consumer Electronics	2.26%	Home and Kitchen	5.65%
External HDD, Pen drives, Memory Cards	2.26%	Video Games	5.65%
Amazon.in Gift cards	2.83%	Luggage and Bags	5.65%
Beauty and Health	5.65%	Sports, Fitness and Outdoors	5.65%
Books and Media	5.65%	Personal Care Appliances	5.65%
Toys and Baby Products	5.65%	Pet Products	5.65%
Watches	5.65%	Clothing	8.48%
Fashion Jewelry	5.65%	Shoes	8.48%

Source: Company Report

Faster expansion with IOCL tie-up: Vakrangee is looking to open 5-6k outlets through IOCL by March'17 and up to 20k outlets in the next 24-30 months. Opening outlets through IOCL is preferable as owners have already undergone basic KYC checks (financial capability, police verification, credit verification, reference check etc.). However, the outlets are mainly spread out in urban and semi urban regions, in line with IOCL's presence. Vakrangee over the last 6 months has conducted dealer roadshows in order to generate interest from the outlets, and is currently in the process of selecting locations which would be most suited to roll out the initial network.

Insurance agents tying up to expand rural reach: Tie ups with Vakrangee enable insurance companies to target a new set of customers, and new insurance companies have looked to tie up with Vakrangee. As per IRDA's (Insurance Regulatory and Development Authority) new norms, corporate agents are allowed to tie up with up to nine insurers (three life, non-life and health each). Vakrangee's outlets are currently earning double digit commissions, through direct and indirect commission from insurers. Vakrangee is presently tied up with three life (HDFC Standard Life, Bajaj Allianz, LIC), two non-life (Tata AIG, Reliance General) and two health (Signa TTK, Religare) insurance agencies, and the company plans to tie up with additional non-life insurance companies to distribute insurance products through their outlets.

Considering dividend increase: For this year, Vakrangee has committed to paying between 15-25% of the net profit of the year as dividend. Additionally, Vakrangee looks to pay off Rs. 2.5bn of debt this year from the cash flows. Post the payment of debt, Vakrangee will become debt free, and the company said it may look at increasing the dividend payout to the shareholders from the next year as it is following up a capex light model.

2Q17 results

Exhibit 2: 2Q'17 results table

Vakrangee - consolidated financials						Management comments
Rs mn (except per share data)	2Q16A	1Q17A	2Q17A	YoY	QoQ	
Total Revenues	7,894	9,182	9,603	22%	5%	On track of VK rollouts. Expect to reach 75k centers by FY'2020.
Cost of materials consumed	(7,141)	(6,861)	(7,128)	0%	4%	Commissions to franchisees key driver. Expect proportion to increase over time
Change in inventories	1,421	49	(10)	NM	NM	
Employee Benefit expenses	(59)	(92)	(108)	82%	17%	
Other expenses	(54)	(63)	(86)	59%	36%	
Total operating expenses	(5,833)	(6,968)	(7,331)	26%	5%	
EBITDA	2,061	2,214	2,272	10%	3%	
EBITDA margin	26.1%	24.1%	23.7%	-2.4 pps	-0.5 pps	Expect EBITDA margins to trend lower as e-governance portion reduces
Dep & Amortisation	(423)	(212)	(199)	-53%	-6%	Should trend lower as historical capex is written off
EBIT	1,638	2,002	2,072	27%	4%	
Finance cost	(141)	(136)	(134)	-5%	-2%	Expect to trend lower as VK biz replaces e-governance biz
Profit before taxes	1,496	1,866	1,939	30%	4%	
Income tax es	(535)	(651)	(675)	26%	4%	
Effective tax rate (%)	35.7%	34.9%	34.8%	-0.9 pps	-0.1 pps	Full tax paying entity
Net Income	962	1,215	1,264	31%	4%	
Basic EPS	1.9	2.3	2.4	28%	4%	

Standalone						Management comments
Segment Analysis	2Q16A	1Q17A	2Q17A	YoY	QoQ	
Total Revenue	7,839	9,116	9,435	20%	3%	
Vakrangee Kendra	3,885	5,506	5,958	53%	8%	New tie-ups announces in insurance, logistics and telecom segments
E-Governance	3,954	3,611	3,478	-12%	-4%	E-governance degrowing in line with managements outlook to reduce exposure
Total EBITDA	2,050	2,205	2,273	11%	3%	
Vakrangee Kendra	929	1,216	1,268	36%	4%	
E-Governance	1,121	989	1,005	-10%	2%	
EBITDA margin (%)	26%	24%	24%	-2.1 pps	-0.1 pps	
Vakrangee Kendra	24%	22%	21%	-2.6 pps	-0.8 pps	E-governance EBITDA margins higher, but lower net profit margins
E-Governance	28%	27%	29%	0.6 pps	1.5 pps	
Revenue split (%)						
Vakrangee Kendra	49.6%	60.4%	63.1%	13.6 pps	2.7 pps	VK business proportion will keep increasing, and reach 100% by 2020
E-Governance	50.4%	39.6%	36.9%	-13.6 pps	-2.7 pps	
EBITDA split (%)						
Vakrangee Kendra	45.3%	55.1%	55.8%	10.4 pps	0.6 pps	
E-Governance	54.7%	44.9%	44.2%	-10.4 pps	-0.6 pps	

Source: Company Report

Takeaways from Q2 conference call

On track to meet rollout targets: Vakrangee said it is on track to meet their rollout targets of opening up 35k outlets by FY'17, and 75k outlets by FY'2020. The Government's push towards cash subsidies is also helping the company to generate momentum.

Pilot with insurers: Vakrangee is in the pilot stages of rollout with insurance agents Reliance General and Bajaj Allianz, while it has recently rolled out services with Tata AIG across all its outlets.

Logistics tie ups with Aramex, Delhivery: Vakrangee has entered into logistics tie ups with Aramex and Delhivery, and is testing services on a pilot basis. They have currently rolled out services in 19 pin codes, and have delivered 68k parcels over the last three months.

Run rate of 75k/120k from rural/urban outlets: Vakrangee is registering a business run rate of Rs. 75k per month from the rural outlets, and Rs. 120k per month from urban outlets. Margins from both locations remain similar.

ATM rollout split to pick up post IOCL rollouts: Vakrangee expects ATM rollouts to pick up as IOCL centers gather pace, as the company believes that IOCL centers would be best suited as locations for ATMs.

Expect EBITDA margins to trend lower in future: Vakrangee expects EBITDA margins to decline in future as proportion of Vakrangee Kendra revenues grow (in contrast with e-governance). This is as e-governance has higher EBITDA margins. But on the net income level, Vakrangee expects net income margins to improve.

Capex breakeven for franchisees between 12-18 months: Vakrangee said that they expect their franchisees to recoup their capex investments within 12-18 months of opening the franchise. The breakeven period is 12 months for rural outlets (on account of lower investments), and 18 months for urban outlets.

Exhibit 3: Vakrangee divisional revenue breakup

Segment	FY16 Revenue	FY20E Revenue	Area of Business	Type of service	Revenue model	Vakrangee Kendra Revenue split	
						Current	FY'20E
Vakrangee Kendra	53%	> 90%	Banking	Bank account opening Deposits, Retail loans, Direct Benefit Transfer, etc	Rs 20/ Account opening 48 bps of transaction size	30 - 35%	30%
			Insurance	Life/Non Life Insurance, Government schemes, Tie-up with Tata AIG to distribute product	10 - 25% commission	5 - 10%	5 - 10%
			E-Governance services	Card Enrolments, Utility Bills, Taxes, and Levies, etc Land records, Rail Tickets, Exam fee payments, etc	Varied based on type of service	10 - 15%	10%
			E-commerce	Mobile/DTH Recharge & bill payment, Education Exclusive tie up with Amazon India Other tieups - Redbus, Ricoh, M&M group	Mobile/DTH: 2 - 5% of Recharge Amazon: 4 - 15% of GMV	35 - 40%	45 - 48%
E-Governance	47%	< 10%	Legacy E-Governance project implementation	National E-Governance Plan (NEGP) projects like Unique Identification Project (UID), PDS, etc	Varied based on terms of contract		

Source: Company report

Exhibit 4: Consolidated Income Statement (Rs mn)

Consol. IS (Rs mn)	FY11	FY12	FY13	FY14	FY15	FY16	1Q15	2Q15	3Q15	4Q15	1Q16*	2Q16*	3Q16	4Q16*	1Q17*	2Q17*
Total Revenue	8,903	13,578	15,524	19,581	27,864	31,964	6,819	7,007	7,046	6,992	7,063	7,894	8,204	8,803	9,183	9,603
YoY Growth%		52.5%	14.3%	26.1%	42.3%	14.7%					3.6%	12.7%	16.4%	25.9%	30.0%	21.7%
QoQ Growth%								2.8%	0.6%	-0.8%	1.0%	11.8%	3.9%	7.3%	4.3%	4.6%
Operating expenses	(7,107)	(10,920)	(11,510)	(13,550)	(20,226)	(23,265)	(5,178)	(5,110)	(5,013)	(4,925)	(5,055)	(7,141)	(5,798)	(5,271)	(6,861)	(7,128)
Change In Inventory	35	51	292	(137)	46	56	12	20	24	(9)	(2)	1,421	(139)	(1,224)	49	(10)
Employee Benefit expenses	(265)	(125)	(285)	(314)	(196)	(254)	(39)	(45)	(50)	(61)	(55)	(61)	(64)	(71)	(92)	(108)
Other Expenses	(171)	(123)	(153)	(173)	(196)	(225)	(44)	(39)	(47)	(66)	(51)	(54)	(68)	(52)	(63)	(86)
Total Expenses	(7,509)	(11,117)	(11,657)	(14,173)	(20,573)	(23,687)	(5,250)	(5,174)	(5,087)	(5,062)	(5,163)	(5,835)	(6,069)	(6,617)	(6,968)	(7,331)
EBITDA	1,394	2,462	3,867	5,408	7,291	8,277	1,569	1,832	1,959	1,931	1,900	2,059	2,135	2,186	2,215	2,272
EBITDA margin%	15.7%	18.1%	24.9%	27.6%	26.2%	25.9%	23.0%	26.1%	27.8%	27.6%	26.9%	26.1%	26.0%	24.8%	24.1%	23.7%
YoY Growth%		76.6%	57.1%	39.8%	34.8%	13.5%					21.1%	12.4%	8.9%	13.2%	16.5%	10.3%
QoQ Growth%								16.8%	7.0%	-1.5%	-1.6%	8.3%	3.7%	2.4%	1.3%	2.6%
Depreciation and Amortization	(550)	(874)	(1,571)	(1,809)	(1,649)	(1,640)	(407)	(411)	(411)	(419)	(438)	(423)	(428)	(352)	(212)	(199)
Finance Costs	(176)	(558)	(860)	(779)	(749)	(560)	(205)	(204)	(197)	(144)	(144)	(140)	(139)	(138)	(136)	(134)
Profit before tax	668	1,029	1,437	2,820	4,893	6,076	957	1,217	1,352	1,368	1,319	1,496	1,567	1,696	1,866	1,939
Tax Expense	(187)	(320)	(394)	(1,070)	(1,675)	(2,128)	(195)	(416)	(458)	(605)	(451)	(534)	(539)	(587)	(651)	(675)
Minority Interest	0	(0)	0	1	0	0	0	0	0	0	0	0	0	0	0	0
Net Income	481	709	1,043	1,750	3,218	3,948	762	801	893	762	868	962	1,028	1,109	1,215	1,264
Net Income margin%	5.4%	5.2%	6.7%	8.9%	11.6%	12.3%	11.2%	11.4%	12.7%	10.9%	12.3%	12.2%	12.5%	12.6%	13.2%	13.2%
YoY Growth%		47.2%	47.2%	67.8%	83.9%	22.7%					13.9%	20.1%	15.1%	45.4%	40.0%	31.4%
QoQ Growth%								5.1%	11.6%	-14.7%	13.8%	10.8%	6.9%	7.8%	9.6%	4.0%
Basic EPS	1.07	1.42	2.08	3.48	6.39	7.59	1.51	1.59	1.77	1.51	1.72	1.86	1.95	2.10	2.29	2.38
YoY Growth%		32.7%	46.5%	67.3%	83.6%	18.8%					13.9%	17.0%	10.2%	39.1%	33.1%	28.0%
QoQ Growth%								5.3%	11.3%	-14.7%	13.9%	8.1%	4.8%	7.7%	9.0%	3.9%
Diluted EPS	0.97	1.40	2.04	3.44	6.06	7.44	1.48	1.58	1.68	1.44	1.63	1.81	1.93	2.10	2.29	2.38

* Financials as per Ind AS reporting

Source: Company report

Exhibit 5: Vakrangee Standalone Segment-wise split

Standalone Segments (Rs mn)	FY14	FY15	FY16	1Q15	2Q15	3Q15	4Q15	1Q16	2Q16	3Q16	4Q16	1Q17*	2Q17*
Total Revenue	19,654	27,754	31,686	6,809	6,979	7,011	6,956	7,010	7,839	8,110	8,728	9,116	9,435
Vakrangee Kendra	7,612	11,884	16,868	2,762	2,965	3,211	2,945	3,493	3,885	4,377	5,114	5,506	5,958
E-Governance	12,042	15,870	14,818	4,046	4,014	3,800	4,011	3,517	3,954	3,733	3,615	3,611	3,478
Total EBITDA	5,642	7,274	8,238	1,569	1,828	1,956	1,921	1,891	2,050	2,116	2,182	2,205	2,273
Vakrangee Kendra	2,371	3,593	4,037	858	907	1,043	785	882	929	1,052	1,175	1,216	1,268
E-Governance	3,270	3,681	4,201	711	921	913	1,136	1,010	1,121	1,064	1,007	989	1,005
EBITDA margin (%)	28.7%	26.2%	26.0%	23.0%	26.2%	27.9%	27.6%	27.0%	26.2%	26.1%	25.0%	24.2%	24.1%
Vakrangee Kendra	31.2%	30.2%	23.9%	31.1%	30.6%	32.5%	26.6%	25.2%	23.9%	24.0%	23.0%	22.1%	21.3%
E-Governance	27.2%	23.2%	28.4%	17.6%	22.9%	24.0%	28.3%	28.7%	28.3%	28.5%	27.9%	27.4%	28.9%
Revenue split (%)													
Vakrangee Kendra	38.7%	42.8%	53.2%	40.6%	42.5%	45.8%	42.3%	49.8%	49.6%	54.0%	58.6%	60.4%	63.1%
E-Governance	61.3%	57.2%	46.8%	59.4%	57.5%	54.2%	57.7%	50.2%	50.4%	46.0%	41.4%	39.6%	36.9%
EBITDA split (%)													
Vakrangee Kendra	42.0%	49.4%	49.0%	54.7%	49.6%	53.3%	40.8%	46.6%	45.3%	49.7%	53.8%	55.1%	55.8%
E-Governance	58.0%	50.6%	51.0%	45.3%	50.4%	46.7%	59.2%	53.4%	54.7%	50.3%	46.2%	44.9%	44.2%

* Financials as per Ind AS reporting

Source: Company report

Exhibit 6: Consolidated Balance sheet

Consol. Balance Sheet (Rs mn)	FY11	FY12	FY13	FY14	FY15	FY16	2Q17*
Fixed Assets	2,724	5,516	4,371	4,845	2,829	1,322	1,253
Other Non-Current Assets	352	392	364	668	120	306	683
Inventories	177	244	538	1,625	1,694	5,071	5,040
Trade Receivables	2,745	4,455	6,527	7,683	11,993	8,579	8,565
Cash & Equivalents	176	284	319	293	382	1,673	1,937
Other Current Assets	719	270	1,707	2,131	3,354	4,150	4,951
Total Assets	6,894	11,162	13,826	17,246	20,372	21,101	22,428
Long-Term Borrowings	0	1,560	1,457	862	374	125	246
Other Non-Current Liabilities	522	802	907	745	441	150	116
Short-Term Borrowings	1,634	2,156	2,852	3,216	3,156	2,828	2,698
Trade Payables	868	1,218	1,755	2,524	2,131	1,144	784
Other Current Liabilities	312	1,229	1,688	2,104	2,197	1,644	955
Total Liabilities	3,337	6,964	8,659	9,451	8,299	5,890	4,799
Share Capital	237	250	502	503	503	529	529
Reserves & Surplus	3,234	3,919	4,636	6,270	9,070	14,682	17,099
Total Equity	3,556	4,169	5,138	7,795	12,073	15,211	17,628
Minority Interest and others	1	29	29	0	0	0	1
Total Equity & Liabilities	6,894	11,162	13,826	17,246	20,372	21,101	22,428

*Financials as per Ind AS reporting

Source: Company report

Exhibit 8: Key Ratios

Key ratios	FY12	FY13	FY14	FY15	FY16	2Q17
Return On Invested capital	10.8%	12.0%	16.4%	23.4%	23.4%	23.3%
Return on Assets	7.9%	8.4%	11.3%	17.1%	19.0%	21.3%
Return On Equity	18.3%	22.4%	27.1%	32.4%	28.9%	27.5%
Days of Inventory	5.7	9.2	20.2	21.7	38.6	51.6
Days of Receivables	96.8	129.1	132.4	128.9	117.5	87.4
Days of Payables	34.3	46.5	55.1	41.3	25.2	15.5
Asset Turnover ratio	1.50	1.24	1.26	1.48	1.54	1.65
Current Ratio	1.14	1.44	1.50	2.33	3.47	4.62
Net Debt	3,431	3,990	3,785	3,148	1,279	1,007
Net Debt/EBITDA	1.39	1.03	0.70	0.43	0.15	0.11
Interest coverage ratio	2.8	2.7	4.6	7.5	11.8	15.5
Total Debt/Equity	0.9	0.8	0.5	0.3	0.2	0.2
Net Debt/Equity	0.8	0.8	0.5	0.3	0.1	0.1

Source: Company report

Exhibit 7: Consolidated Cashflow statement

Consol. Cash Flow (Rs mn)	FY11	FY12	FY13	FY14	FY15	FY16	2Q17*
Profit before Tax	668	1,029	1,437	2,820	4,893	6,076	3,801
Depreciation & Amortization	550	874	1,571	1,809	1,649	1,640	669
Change in Working Capital	(1,735)	(5)	(2,802)	(2,099)	(5,770)	(2,603)	(2,062)
Other Adjustments, Net	65	265	531	(256)	(783)	(2,440)	(1,423)
Cash Flow from Operations	(452)	2,164	736	2,275	(11)	2,673	985
Capital Expenditure	(605)	(3,745)	(930)	(2,284)	(44)	(134)	
(Acquisition) / Disposal of Investments	191	94	(3)	(2)	28	20	
Other Cash Inflow / (Outflow)	5	34	534	24	13	5	
Cash Flow from Investing	(409)	(3,617)	(398)	(2,261)	(2)	(109)	(307)
Shares Issue / (Repurchase)	85	122	11	7	0	1	
Proceeds from borrowings	1,074	2,081	594	(231)	(549)	(577)	
Dividends Paid	(34)	(50)	(100)	(101)	(126)	(132)	
Interest paid	(176)	(498)	(792)	(718)	(677)	(544)	
Other Cash Inflow / (Outflow)	39	(94)	(16)	1,003	1,453	(20)	
Cash Flow from Financing	988	1,561	(303)	(39)	102	(1,273)	(415)

*Financials as per Ind AS reporting

Source: Company report

Exhibit 9: Vakrangee expansion plan and progress

Expansion plan	FY17	FY18	FY19	FY20
Rural Kendras	25,000	35,000	45,000	50,000
Urban Kendras	10,000	15,000	20,000	25,000
Total	35,000	50,000	65,000	75,000
Additions				
Rural Kendras	9,329	10,000	10,000	5,000
Urban Kendras	4,994	5,000	5,000	5,000
Total adds	14,323	15,000	15,000	10,000
Quarterly progress	3Q16	4Q16	1Q17	2Q17
Rural Kendras	15,670	15,671	16,104	19,339
Urban Kendras	2,397	5,006	5,716	6,849
Total	18,067	20,677	21,820	26,188
Additions				
Rural Kendras	1,381	1	433	3,235
Urban Kendras	180	2,609	710	1,133
Total adds	1,561	2,610	1,143	4,368

Source: Company report

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I, Sachin Salgaonkar, hereby certify that the views expressed in this note accurately reflect my personal views about the subject securities and issuers. I also certify that no part of my compensation was, is, or will be directly or indirectly related to the view expressed in this note.

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