Sharekhan by BNP PARIBAS

Powered by the Sharekhan 3R Research Philosophy

Affle (India) Ltd

Robust Q1; connected all growth dots

Internet & new media	Sharekhan code: AFFLE	Result Update

3R MATRIX	+	=	-
Right Sector (RS)	✓		
Right Quality (RQ)	✓		
Right Valuation (RV)		✓	

\+ Positive = Neutral - Negative

What has changed in 3R MATRIX

	Old		New
RS		↔	
RQ		↔	
RV		↔	

Reco/View	Change
Reco: **Buy**	↔
CMP: **Rs. 4,166**	
Price Target: **Rs. 6,000**	↓

↑ Upgrade ↔ Maintain ↓ Downgrade

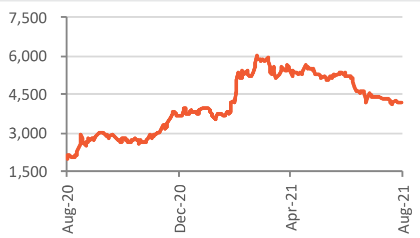
Company details

Market cap:	Rs. 11,103 cr
52-week high/low:	Rs. 6,287 / 1,810
NSE volume: (No of shares)	0.81 lakh
BSE code:	542752
NSE code:	AFFLE
Free float: (No of shares)	1.1 cr

Shareholding (%)

Promoters	60
FII	8
DII	18
Others	14

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	-5.5	-20.8	-1.0	105.6
Relative to Sensex	-9.3	-30.7	-7.0	63.2

Sharekhan Research, Bloomberg

Summary

- Q1FY2022 revenues were strong, led by a robust 85% y-o-y growth in converted users; EBITDA margin contracted by 204 bps y-o-y owing to higher employee costs. OCF to PAT ratio remained at 134%.
- Faster adoption of digital advertising in its top verticals, launch of products and shift of budgets towards mobile advertising are expected to strongly drive up revenues.
- Increasing direct customers' revenue contribution and partnerships with OEMs would help Affle to maintain its market position given higher access to first-party data; expect revenue/earnings to post a CAGR of 45%/32% over FY2021-FY2024E
- We maintain a Buy on Affle (India) Limited with a revised PT of Rs. 6,000, given greater adoption of its platforms, a unique CPCU business model and expansion into new geographies.

Affle (India) Limited (Affle India) delivered another quarter of strong revenue growth in Q1FY2022 despite the devastating impact of second wave of COVID-19 in India, aided by broad-based growth across markets. Revenues grew by 69.8% y-o-y to Rs. 152.5 crore, beating our estimates, led by strong growth in converted users and an increase in CPCU (Cost per Converted User) rate. The number of converted users grew by 85.3% y-o-y during Q1FY2022, while the average rate of CPCU grew by 2.4% y-o-y to Rs. 42 (average CPCU rate of Rs. 40.9 for the last eight quarters). EBITDA margin declined by 204 bps y-o-y to 23%, below our estimates, owing to higher employee expenses (impact of -150 bps y-o-y) and a rise in other expenses. Adjusted net profit came in at Rs. 29.5 crore (up 57.3% y-o-y and 11.4% q-o-q) and was 9% ahead of our estimates. Operating cash flow (OCF) grew 51% y-o-y during the quarter, implying OCF to net profit of 134% versus 92%/140% in Q4FY2021/Q1FY2021.Faster adoption of digital advertising by advertisers in top 10 high-growth verticals (that contributed 90% to Affle India's total revenue in Q1FY2022), expansion of markets through organic and inorganic medium (both emerging and developed markets), launching of new products in the connected devices space and shifting budgets towards mobile advertising by advertisers are expected to drive strong revenue growth going ahead. The consolidation of Jampp acquisition (largely present in LatAm and America in certain verticals) and higher on-ground presence in LatAm would shift the revenue mix towards international markets, which would help to boost its average CPCU rate. Higher revenue contribution from direct customers and partnerships with mobile OEMs and operators has enabled the company to get first-party data, which would help the company to maintain its market position among the publishers and advertisers. Given its leadership position in emerging markets, expansion into developed markets and accelerated transition of organisations to mobile advertising, we believe Affle is well-positioned to deliver a revenue CAGR of 45% over FY2021-FY2024E.

Key positives

- Stronger-than-expected revenue growth; revenue grew by 69.8% y-o-y.
- Converted users grew by 85.3% y-o-y
- Cash conversion remained strong; OCF to net profit ratio stood at 134% in Q1FY2022.

Key negatives

- Higher employee expenses (up 125% y-o-y) impacted margins.
- International markets EBIT margin declined to 30.7% from 65.3% in Q4FY2021 due to higher investments.

Our Call

Valuation – Investing in the right areas: We have tweaked our earnings estimates for FY2022E/FY2023E/FY2024E, factoring in Q1FY2022 results and higher investments on sales team to strengthen its position in new geographies. Given its leadership position in both in-app and on-device ecosystems, end-to-end offerings in the CPCU business model, first-mover advantage in connected device segment especially in the emerging markets and improving share of mobile ad spends to overall ad spends, Affle India is well positioned to capture opportunities from favourable industry tailwinds in terms of higher smartphone penetration and faster adoption of digital advertising in the emerging markets. The acquisition of Jampp and investments in international markets are expected to impact on margins in coming quarters, but we believe it would provide high-growth opportunities in the coming years. We forecast Affle India's revenues and earnings to report a CAGR of 45% and 32%, respectively, over FY2021-FY2024E. Affle India's stock price has corrected by ~20% in the last three months, which offers a good investment opportunity for long term. At CMP, the stock trades at 52x/36x its FY2023E/FY2024E earnings. We continue to prefer Affle India, considering its strong balance sheet along with positive cash flow conversions, greater adoption of platform and a long runway for growth. Hence, we maintain a Buy rating on the stock with a revised PT of Rs. 6,000.

Key Risks

(1) Entry of a large technology player in this space; (2) Inability to generate relevant data for targeted advertisers; and (3) Government regulations related to management of consumer dataand respect for privacy.

Valuation Rs cr

Particulars	FY21	FY22E	FY23E	FY24E
Revenue	516.8	945.1	1,234.8	1,589.0
OPM (%)	25.2	18.8	21.0	23.0
Adjusted PAT	135.0	148.0	215.3	309.7
% YoY growth	*106.1*	*9.6*	*45.4*	*43.8*
Adjusted EPS (Rs.)	53.0	55.9	80.9	116.4
P/E (x)	82.2	75.0	51.6	35.8
P/B (x)	30.9	21.9	15.4	11.0
EV/EBITDA (x)	85.2	61.9	41.8	20.4
RoNW (%)	37.6	29.1	29.8	30.8
RoCE (%)	34.3	28.2	30.8	31.8

Source: Company; Sharekhan estimates

Strong revenue growth, OCF generation remained robust

Affle delivered strong revenue growthdespite devastating impact of the second wave of COVID-19 in India, aided by broad-based growth in both India and international markets. However, EBITDA margin continued to remain below our expectations and contracted by 204 bps y-o-y owing to a sharp increase in employee expenses. Revenues grew by 69.8% y-o-y to Rs. 152.5crore, led by strong growth in converted users and slight increase in CPCU (Cost per Converted User) rate. The number of converted users grew by 85.3% y-o-y during Q1FY2022, while CPCU grew by 2.4% y-o-y to Rs. 42. EBITDA margin declined by 204 bps y-o-y to 23%, below our estimates, owing to 125% y-o-y growth employee expenses (owing to workforce addition at international locations). Ratio of inventory and data costs to overall revenue increased 50 bps y-o-y to 58%in Q1FY2022. However, EBITDA grew 56% y-o-y to Rs. 35.1 crore, in-line with our expectations of Rs. 35.2 crore. Reported net profit came at Rs. 35.7 crore,led byhigher-than-expectedrevenue growth and higher other income. Excluding extraordinary items (gain on revaluation of financial instruments and tax outgo on gain on financial instruments), adjusted net profit came at Rs. 29.5 crore (up 57.3% y-o-y and 11.4% q-o-q) and was 9% aheadof our estimates of Rs. 27.1 crore.Operating cash flow (OCF) grew 51% y-o-y during the quarter, implying an OCF to net profit of 134% versus 92%/140% in Q4FY2021/Q1FY2021.

Higher revenue contribution from direct customers and geography expansion to bode well

Faster adoption of digital advertising by advertisers in itstop 10 high-growth verticals (contributed 90% to its total revenue in Q1FY2022), expansion of markets through organic and inorganic medium (both emerging and developed markets), launching of new products in connected devices space and shift of budgets towards mobile advertising by advertisers are expected to drive its revenue growth going ahead. Further, the management aims to reach over 10 billion connected devices (including personal wearables, connected TV, and smart household appliances) to enable unique and integrated omni-channel consumer journeys over the next 10 years.The management indicated that total mobile ad spend to total ad spends in emerging markets (including India) would shift from 20% to 50% (inline with developed markets) over next 3 years, given accelerated adoption of mobile and higher screen time on mobile by consumers. As a result, mobile ad spend in India is expected to grow at 32.4% CAGR over FY2020-2025. The consolidation of Jampp acquisition (largely present in LatAm and America in certain verticals) and higher on-ground presence in LATAM would shift the revenue mix towards international markets, which would help to boost its average CPCU rate. Contribution of direct customers increased to 71% of its total revenue in Q1FY2022 from 57% in FY2020, which has enabled the company to stay ahead of curve by fortifying its market position. Direct connections with mobile OEMs, operators and advertisers enable the company to get the first-party data, which bode well for Affle in terms of positioning with respect to first-party data both with the advertisers and publishers. Given its leadership position in emerging markets and expansion into developed markets, we believe Affle is well-positioned to deliver a revenue CAGR of 45% over FY2021-FY2024E.

Key result highlights from earnings call

- **Expect revenue mix to shift towards international markets from Q2FY2022:** Revenue growth was broad-based as contribution from both India and international markets remained at 50% each. The company's revenue growth was 69.8% y-o-y, led by 94% y-o-y and 53% y-o-y growth in India and international markets respectively. Management stated that the change in revenue contribution would shift towards international markets from Q2FY2022 on the back of the consolidation of Jampp acquisition (largely present in LatAm and America in certain verticals) and higher on-ground presence in LATAM. The management indicated that the company's ongoing efforts in enhancing sales force in international markets and building localized presence in major international markets would drive the company's next level revenue growth in the long term. Further, management stated that the higher revenue contribution from international markets would have a positive impact on its average CPCU rate.
- **Strengthened relationship with advertisers directly:** The management highlighted that it has strengthened its position with the investments in enhancing platform and product capabilities across the global and emerging markets. The company's strategy is primarily based on 2V (Vernacular and Verticalisation) approach which enables the company to offer higher conversion rate to advertisers by partnering with mobile OEMs and operators. As a results, the company's direct customer contribution increased to 71% to its total revenue in Q1FY2022 from 57% in FY2020. In last two years, the company's revenue contribution has substantially declined from agencies and the company has deepened its relationship with advertisers directly.

- **Strong industry tailwinds to drive its growth:** Affle India' management highlighted that the world is undergoing a paradigm shift with accelerated connected experiences, which has resulted in redefining the digital priorities of advertisers across the globe. The company has been investing on artificial intelligence and machine learning capabilities to drive conversion rate across the connected devices. The management remains optimistic on strong revenue growth in FY2022, led by shift of advertising budgets towards mobiles and programmatic advertising by advertisers. Total mobile advertising spends to total advertising spends remain at 20% in emerging markets including India, while this ratio remains at 50% in developed markets. The management expects that mobile ad spend to total ad spends in emerging markets would shift to 50% in next 3 years, given accelerated adoption of mobile and higher screen time on mobile by consumers. As a result, mobile advertising spends in India is expected to grow at 32.4% CAGR over FY2020-2025. Given a sharp increase in connected devices and higher adoption of smart devices, the advertising spend allocation towards mobiles is expected to accelerate going ahead. Further, adoption of its consumer platform in its key high-growth segments (90% of its total revenue) would continue to increase, which would help to drive the user conversions going ahead.
- **Affle India business is insulated from any change in cookies policy on browsers:** the management stated that most of consumers are currently using smartphone devices, in turn the advertisers are shifting their budget towards digital. The management believes that the recent decision regarding the launch of app tracking transparency measures by Apple would have a less negative impact on its business given its significant exposure to Android devices (only 5-10% exposure to iOS devices). Further, the company's OEM and operator strategy provides a shield as OEMs and operators have a lot of autonomy with respect to Android devices, especially in emerging markets. Further, Google announced that it will delay the phase out of the Chrome web browser technology that tracks users for ad purposes until 2023. However, Affle has a negligible dependence on browsers. The company's business is more dependent on the in-app and on-device ecosystem and emerging markets (here customers use Android as the platform of choice). Hence, the ban on cookies by Goggle would not have any impact on its business.
- **Focused on strategies to maintain its growth momentum:** The management highlighted that the company's tech enabled platform focused delivery which is a part of Affle 2.0 strategy, played out well during FY2021. The company has successfully integrated its platforms, themes and IP portfolio to unlock vernacular consumer experience and deeper verticalisation across key customer segments. The company also strengthened its mobile OEM and operator partnerships to power an open Internet connectivity ecosystem play. This further augmented its consumer platform enabled greater returns on investments (RoI) impact for its advertisers. The company has expanded its human resource capabilities with local presence in some of the international geographies, which has been contributing to the growth of the company.
- **Consistent growth in advertising spend across its top verticals:** Affle has divided its high-growth verticals in four categories (E, F, G, and H), which contributed over 90% to its total revenue in FY2021as against 74% in FY2020. Management witnessed strong traction for its offerings across category E (E-commerce, Entertainment, EdTech), category F (Fintech, Foodtech, and FMCG), category G (Gaming, Groceries, and Government),and category H (Healthtech). The management indicated that the company witnessed consistent growth across these verticals as advertisers in these industry verticals have been digital much faster than earlier.
- **Affle aims to reach over 10 billion connected devices:** The management indicated that consumer trends have been encouraging, given increasing mobile usage and higher screen time by customers, a significant increase in internet traffic, impressions and clicks and an increasing percentage of transactions on mobile. Management highlighted that it has been trying to expand opportunities beyond mobile to connected devices. Affle aims to reach over 10 billion connected devices (including personal wearables, connected TV, and smart household appliances) by 2030. The company has launched household IDs internally, which would help advertisers to target customers at a specific locations and/or households. The company would launch such products in developed markets such as LatAm and America and strengthen its presence in emerging markets as well. The company plans to make entry into China. The management remains confident on achieving target of 10 billion connected devices on the back of launching new products in developed markets, first-mover advantage in emerging markets and entering into new markets like China.

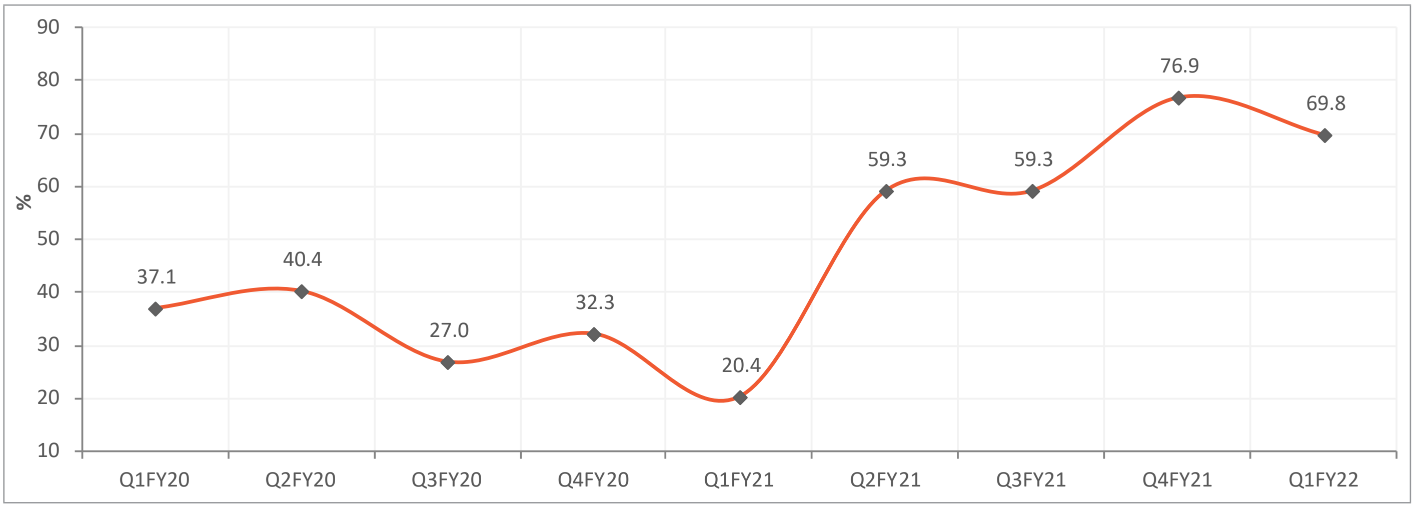
- **Focus on cash flow management:** The management highlighted that it continues to focus on working capital management and positive cash flow from operations. Cash flow from operations stood at Rs. 39.6 crore in Q1FY2022, implies a cash conversion to net profit ratio of 134%.
- Acquisition strategy: Affle has acquired stakes in eight companies over the last 2.5 years. The management indicated that it acquires those businesses where it sees business synergies with the company's core business and the acquired company's net profit margin can be expanded to Affle's level. The acquisition strategy has been around its core strategy such as vernacular and verticalisation strategy.
- **Focus on 2V strategy:** The management indicated that it would continue to invest 2V strategy along with emphasis on the vertical omni-channel integration to further strengthen its market position and expand the reach across the connected device. Management also highlighted that its strategies deeply focuses on strengthening its consumer platform business. The company takes different approaches, including proximity marketing, connected TV medium and partnership with OEMs to reach its customers through the 2V strategy.
- **Headcount:** The company has more than 425 employees on the full-time contracts. However, the company has certain functions where it has employees on contract or outsourced.

Results (Consolidated) Rs cr

Particulars	Q1FY22	Q1FY21	Y-o-Y %	Q4FY21	Q-o-Q %
Net sales	**152.5**	**89.8**	**69.8**	**141.6**	**7.7**
Inventory and data costs	88.4	51.6	71.3	81.2	8.8
Employee expenses	18.8	8.3	124.7	16.4	14.5
Other expenses	10.2	7.3	39.3	9.4	8.6
EBITDA	**35.1**	**22.5**	**56.0**	**34.5**	**1.6**
Depreciation	5.2	4.3	20.7	5.2	0.4
EBIT	**29.9**	**18.2**	**64.3**	**29.3**	**1.8**
Other Income	12.7	2.5	416.4	35.9	-64.7
Finance cost	1.4	0.5	168.3	1.3	9.0
PBT	**41.2**	**20.1**	**104.7**	**64.0**	**-35.7**
Total tax	5.3	1.3	293.9	5.4	-1.9
Reported net profit	**35.7**	**18.8**	**90.3**	**58.5**	**-38.9**
Adjusted net profit	**29.5**	**18.8**	**57.3**	**26.5**	**11.4**
Adjusted EPS (Rs.)	13.7	7.4	85.9	10.4	31.3
Margin (%)			**BPS**		**BPS**
EBITDA	23.0	25.0	-204	24.4	-139
EBIT	19.6	20.2	-66	20.7	-114
Adjusted NPM	19.4	20.9	-155	18.7	64
Tax rate	12.8	6.6	614	8.4	440

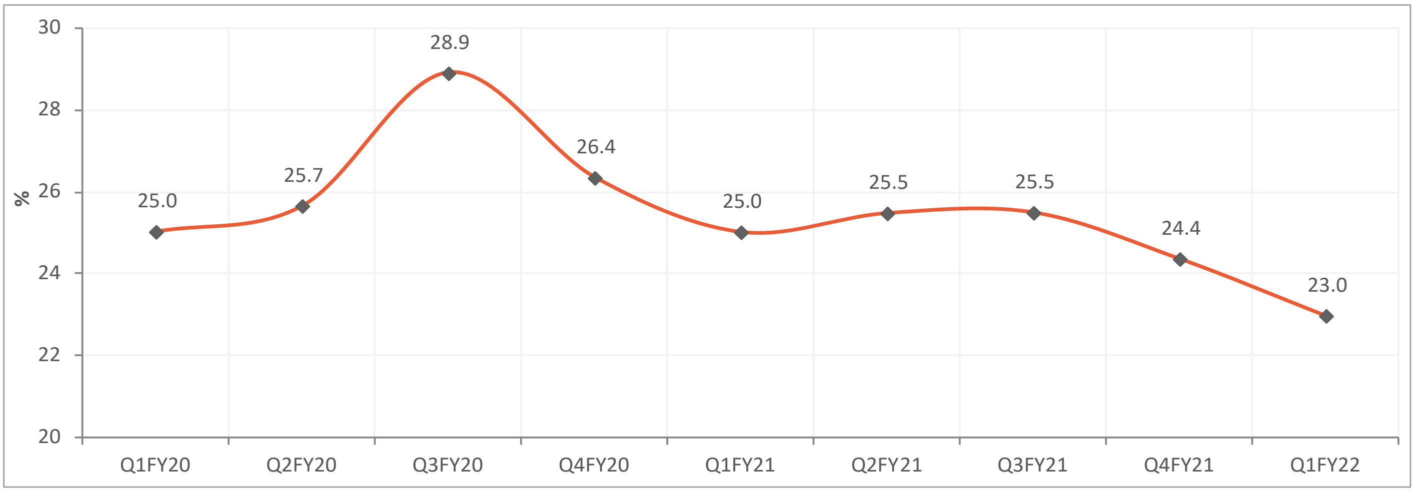
Source: Company; Sharekhan Research

USD revenue growth trend (y-o-y)



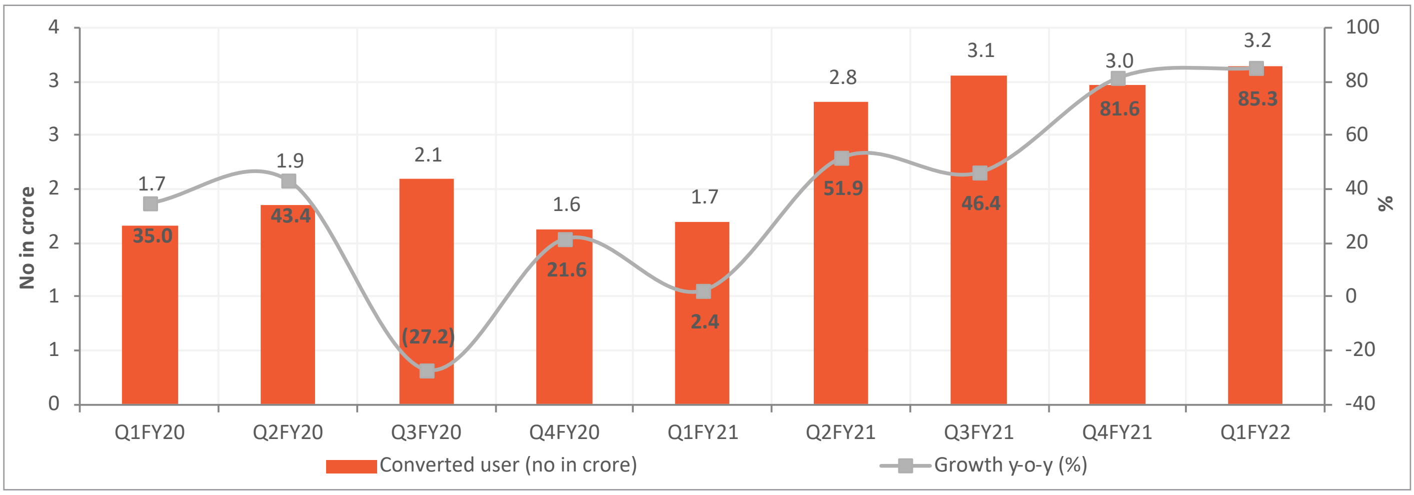
Source: Sharekhan Research

EBITDA margin (%) trend



Source: Sharekhan Research

Converted users (no in crore) and growth (% y-o-y)



Source: Sharekhan Research

Outlook and Valuation

■ Sector view – Expect strong growth in mobile ad revenue to continue

Digital advertising spends are expected to report a 32.5% and 18% CAGR, respectively, in India and Southeast Asia (SEA) in the next 5 years because of rising active internet users, rapid adoption of smartphones and connected devices, and a young population. Mobile advertisement spends are projected to reach a 50% of total advertising spends from 20% currently over next 3 years. The combined opportunities in mobile-app video, OTT and CTV programmatic advertising spends across the globe are expected to post a 17% CAGR over 2020-2025.

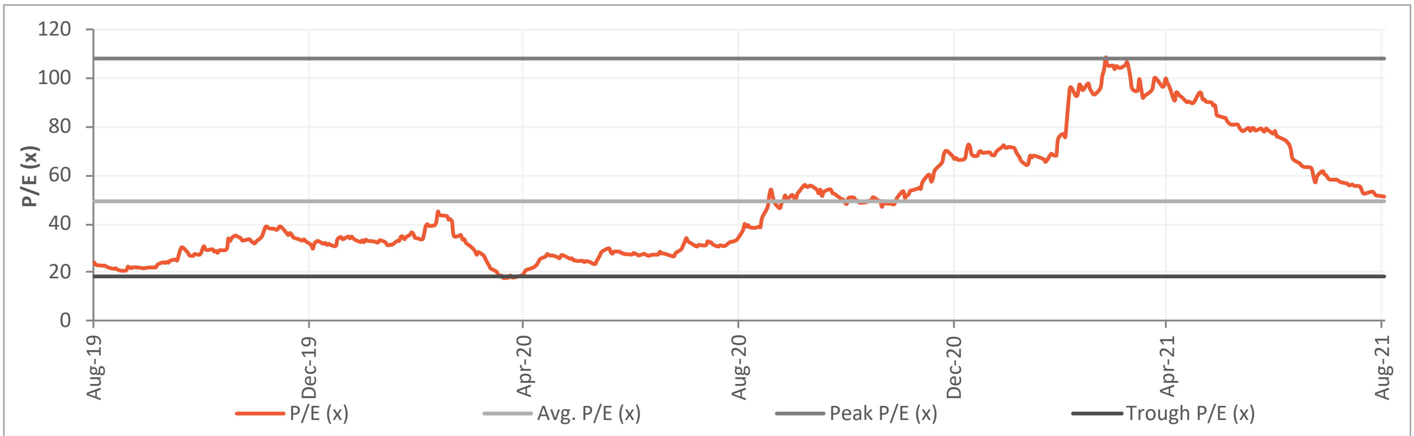
■ Company outlook – Long runway for growth

Affle's exposure in fast-growing markets such as India and South-East Asia and segments such as e-Commerce provide a platform for sustainable growth momentum in the longterm. With a scalable end-to-end offering across the ad-tech value chain and the CPCU model, we believe that Affle would continue to derive high ROI for advertisers. Management expects to deliver at least a 25-30% revenue CAGR in the next five years because of its CPCU model, focus on 2V (Vernacular and Verticalisation) strategies to strengthen market position, expand its reach to connected devices and entry into new geographies.

■ Valuation – Presence in the right spots

We have tweaked our earnings estimates for FY2022E/FY2023E/FY2024E, factoring in Q1FY2022 results and higher investments on sales team to strengthen its position in new geographies. Given its leadership position in both in-app and on-device ecosystems, end-to-end offerings in the CPCU business model, first-mover advantage in connected device segment especially in the emerging markets and improving share of mobile ad spends to overall ad spends, Affle India is well positioned to capture opportunities from favourable industry tailwinds in terms of higher smartphone penetration and faster adoption of digital advertising in the emerging markets. The acquisition of Jampp and investments in international markets are expected to impact on margins in coming quarters, but we believe it would provide high-growth opportunities in the coming years. We forecast Affle India's revenues and earnings to report a CAGR of 45% and 32%, respectively, over FY2021-FY2024E. Affle India's stock price has corrected by ~20% in the last three months, which offers a good investment opportunity for long term. At CMP, the stock trades at 52x/36x its FY2023E/FY2024E earnings. We continue to prefer Affle India, considering its strong balance sheet along with positive cash flow conversions, greater adoption of platform and a long runway for growth. Hence, we maintain a Buy rating on the stock with a revised PT of Rs. 6,000.

One-year forward P/E (x) band



Source: Sharekhan Research

Peer valuation

Particulars	CMP (Rs / Share)	O/S Shares (Cr)	MCAP (Rs Cr)	P/E (x)		EV/EBIDTA (x)		P/BV (x)		RoE (%)	
				FY22E	FY23E	FY22E	FY23E	FY22E	FY23E	FY22E	FY23E
Just Dial	4,166	3	11,103	75.0	51.6	61.9	41.8	21.9	15.4	29.1	29.8
Info Edge*	5,330	13	68,637	146.7	105.8	129.6	91.7	13.9	12.6	9.5	12.0
Affle India	971	6	6,059	32.3	22.3	38.0	25.1	4.1	4.0	12.7	14.3

*Source: Sharekhan Research, Bloomberg; *Standalone*

About company

Affle is a global technology company with a leading market position in India. The company has two business segments, i.e. (1) consumer platform and (2) enterprise platform. The consumer intelligence platform delivers consumer engagement, acquisitions, and transactions for leading brands and B2C companies through relevant mobile advertising. Affle aims to enhance returns on marketing spend through delivering contextual mobile ads and reducing digital ad fraud, while proactively addressing consumer privacy expectations. The enterprise platform helps offline companies to go online through platform-based app development, enabling of O2O (online to offline) commerce, and data analytics.

Investment theme

Affle, a leading adtech company in India, provides end-to-end offerings to advertisers through mobileadvertising using its proprietary mobile audience as a service (MAAS) platform for customers. Given its deep learning algorithm capabilities and ability to deliver more targeted and personalised advertisements, more advertisers have been using the consumer platform for running their digital ad campaigns on its platform. With increased share of digital ad spends and shifting of advertisers towards programmatic advertising, ad-tech vendors such as Affle are well placed to deliver higher growth going ahead.

Key Risks

(1) High client concentration; (2)entry of large tech player in this space; and (3) inability to generate actionable outcomes for targeted advertisers.

Additional Data

Key management personnel

Anuj Khanna Sohum	Founder, Chairman & CEO
Anuj Kumar	Co-founder, Chief revenue & operating office
Kapil Bhutani	Chief financial & operations officer
Charles Yong	Chief architect and technology officer
Vipul Kedia	Chief data and Platforms officer

Source: Company Website

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	MALABAR INDIA FUND LTD	4.48
2	Standard Life Aberdeen PLC	4.34
3	Nomura India Investment	1.79
4	Nippon Life India Asset Management	1.74
5	ABERDEEN STD ASIA FO PLC	1.63
6	Aditya Birla Sun Life Asset Management	1.40
7	Vanguard Group Inc	1.16
8	William Blair & CO LLC	0.98
9	Royal Bank of Canada	0.94
10	L&T Mutual Fund Trustee Ltd/India	0.93

Source: Bloomberg

Understanding the Sharekhan 3R Matrix

Right Sector	
Positive	Strong industry fundamentals (favorable demand-supply scenario, consistent industry growth), increasing investments, higher entry barrier, and favorable government policies
Neutral	Stagnancy in the industry growth due to macro factors and lower incremental investments by Government/private companies
Negative	Unable to recover from low in the stable economic environment, adverse government policies affecting the business fundamentals and global challenges (currency headwinds and unfavorable policies implemented by global industrial institutions) and any significant increase in commodity prices affecting profitability.
Right Quality	
Positive	Sector leader, Strong management bandwidth, Strong financial track-record, Healthy Balance sheet/cash flows, differentiated product/service portfolio and Good corporate governance.
Neutral	Macro slowdown affecting near term growth profile, Untoward events such as natural calamities resulting in near term uncertainty, Company specific events such as factory shutdown, lack of positive triggers/events in near term, raw material price movement turning unfavourable
Negative	Weakening growth trend led by led by external/internal factors, reshuffling of key management personal, questionable corporate governance, high commodity prices/weak realisation environment resulting in margin pressure and detoriating balance sheet
Right Valuation	
Positive	Strong earnings growth expectation and improving return ratios but valuations are trading at discount to industry leaders/historical average multiples, Expansion in valuation multiple due to expected outperformance amongst its peers and Industry up-cycle with conducive business environment.
Neutral	Trading at par to historical valuations and having limited scope of expansion in valuation multiples.
Negative	Trading at premium valuations but earnings outlook are weak; Emergence of roadblocks such as corporate governance issue, adverse government policies and bleak global macro environment etc warranting for lower than historical valuation multiple.

Source: Sharekhan Research

Sharekhan

by BNP PARIBAS

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