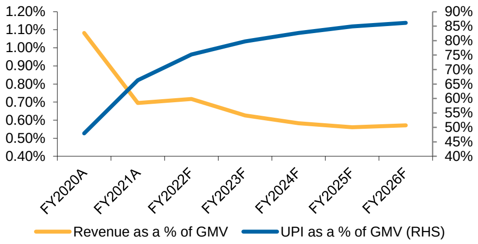
18 November 2021 | India

EQUITIES

ONE97 IN — Underperform

Price (at CLOSE#, 12 Nov 2021) — Rs2,150.00

PayTM – Blended take rates to fall as share of UPI picks up



Source: Company data, Macquarie Research, November 2021

Valuation - 1200	Rs	1,200.00
12-month target	Rs	1,200.00
Upside/Downside	%	-44.2
GICS sector Telecommunication Services		
Market cap	Rsbn	1,384
Number shares on issue	m	643.6

Investment fundamentals

Year end 31 Mar		2022E	2023E	2024E	2025E
Revenue	m	44,875	53,025	62,174	74,738
EBITDA	m	-15670	-16555	-17161	-18808
EBIT	m	-16957	-17855	-18772	-20232
EBIT growth	%	nmf	-5.3	-5.1	-7.8
Adjusted profit	m	-12758	-8676	-10035	-9292
EPS adj	Rs	-20.42	-13.48	-15.59	-14.44
EPS adj growth	%	nmf	34.0	-15.7	7.4
ROE	%	-9.4	-6.6	-8.2	-8.3
P/BV	x	10.2	10.9	11.8	12.9

Source: FactSet, Macquarie Research, November 2021
(All figures in INR unless noted)

One 97 Communications (ONE97 IN)
Too many fingers in too many pies

Key points

- We believe PayTM's business model lacks focus and direction. We initiate with an UP rating and TP of Rs1,200, implying 40%+ downside
- Achieving scale with profitability a big challenge; company is a cash guzzler
- Regulations and competition are added worries

Initiate with Underperform rating and TP of Rs1,200

Dabbling in multiple business lines inhibits PayTM from being a category leader in any business except wallets, which are becoming inconsequential with the meteoric rise in UPI payments. Competition and regulation will drive down unit economics and/or growth prospects in the medium term in our view. Unless PayTM lends, it can't make significant money by merely being a distributor. We therefore question its ability to achieve scale with profitability. We value the stock using a 0.5x PSg multiple on Dec-23 annualised sales to arrive at our TP of Rs1,200, implying 44% downside The key game changer could be an ability to monetise UPI, which could completely swing the investment case. A 10bp fee on UPI provides a fair value of Rs2,900-3,300 based on PSg/DCF (see pp 45-47).

Competition will drive down unit economics

Most things that PayTM does, every other large ecosystem player like Amazon, Flipkart, Google, etc, are doing. The competition is quite evident in the BNPL space and distribution of various financial products. Longer term, take rates in the distribution business will be driven southwards by competition and regulation.

Building scale with profitability a challenge; FCF +ve by FY30E

For large fintechs, unless they have a closed loop ecosystem and a captive customer base, building scale with profitability will remain a big challenge in our view, which we discussed in our recent India Fintech report. Consumer & merchant loan distribution at best, is only a ~$350m revenue opportunity for PayTM in our view, as shown in Fig 49. PayTM has to lend, i.e., use its own balance sheet to make loans and do that profitably for which it needs a banking license, credit underwriting experience and collection infrastructure, all of which are lacking at present in our view. Despite factoring in an aggressive ~50% CAGR increase over the next five years in non-payment business revenues led by distribution business, we expect PayTM to generate +ve FCF only by FY30E.

Regulations, bank license - the other elephants in the room

RBI most likely will introduce regulations in the Fintech space, particularly in the BNPL space in our view. We are also not enthused with the company's complicated organisation structure, related-party transactions, churn in top management and a thinly staffed board with 75% of members being based out of India. Macquarie's MGRS (governance and risk scoring) system places PayTM below median. Obtaining a small finance bank license could be difficult in our view given that Chinese controlled firms own more than a 30% stake in PayTM.

Valuations expensive especially when path to profitability is unclear

PayTM's valuation, at ~26x FY23E Price to Sales (P/S), is expensive especially when profitability remains elusive for a long time. Most fintech players globally trade around 0.3x-0.5x PSg (price to sales growth ratio) and we have assumed the upper end of this band. We are unwilling to give it a premium here as we are unsure about the path to profitability. Key risks include change in regulations which allow monetisation of UPI and receipt of a banking license.

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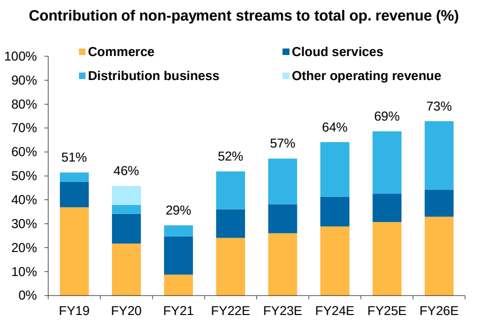
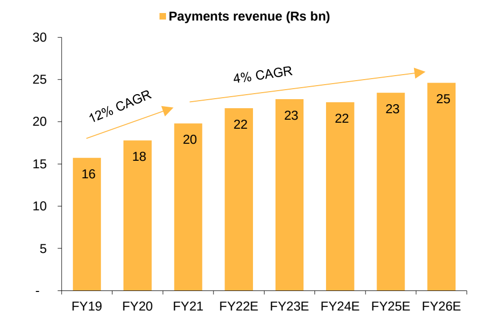
Inside

Our forecasts build sharp pick-up in non-payment-based revenues for PayTM…



Source: Company data, Macquarie Research, November 2021

But payments revenue to clock mere 4% CAGR over FY21-26, despite strong GMV growth



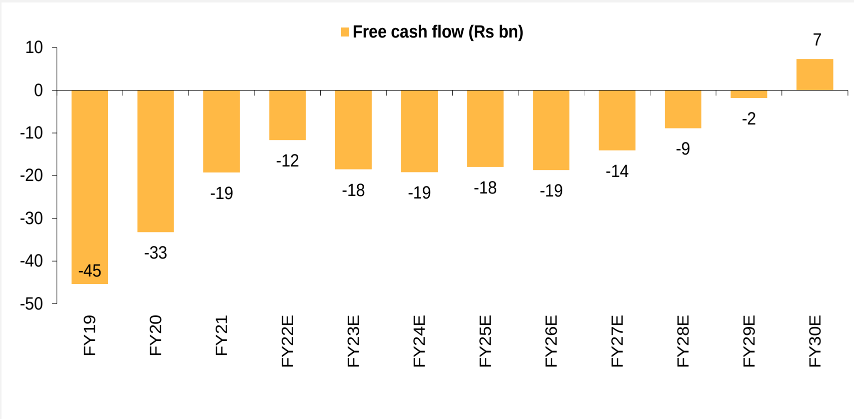
Source: Company data, Macquarie Research, November 2021

Investment overview

Company profile

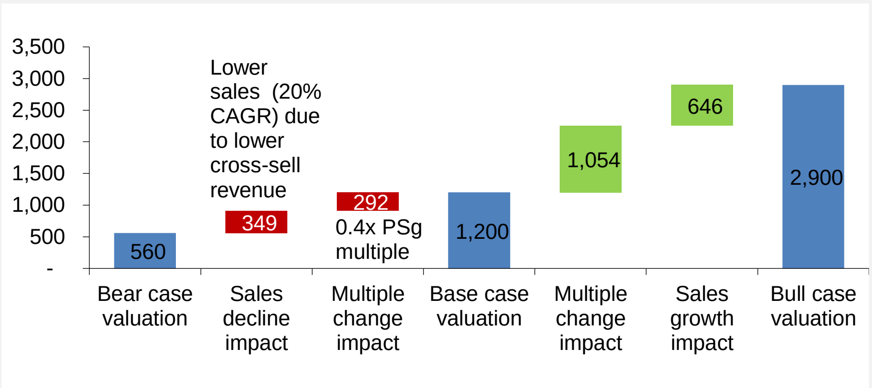
- One97 Communications (PayTM) is India's leading digital ecosystem for consumers and merchants. It offers payment, commerce, cloud and financial services to 330+ million consumers (Monthly Transacting Users of 50mn plus) and over 20+ million merchants, as of 31 March 2021.
- PayTM has a market share of 65-70% in the digital wallets business and about 40% in the consumer to merchant segment by transaction volume of mobile payment instruments.
- PayTM's founder Vijay Shekhar Sharma is expected to own 13% stake post the IPO, with the Chinese controlled firms Alibaba and Ant Financial owning a substantial 31% stake.

We don't see PayTM generating +ve FCF until FY30



Source: Company data, Macquarie Research, November 2021

PayTM – Bull and bear case valuation



Source: Macquarie Research, November 2021

Note: Throughout the report, One97 Communications and PayTM have been used interchangeably. One97 Communication is the parent company that is being listed which launched the popular PayTM product (pay through mobile) in 2009 which has now become synonymous with the parent company name.

Initiate coverage with UP rating and TP of Rs1,200.

Lacks leadership in most segments

Too many fingers in too many pies

We initiate coverage on PayTM with an UP rating and TP of Rs1,200, implying 44% downside from current levels. The biggest challenge for PayTM will be to achieve scale with profitability. As can be seen in Fig 1, PayTM has a history of spinning off several business verticals without achieving market leadership or profitability.

Fig 1 PayTM – Jack of all trades, master of none

Business line	Business launched	Scale achieved	Customer & merchant franchise	Key observations and comments
Payments	2014 (wallet), 2017 (payments bank)	- FY21 UPI txn mkt share: 8% by val & 12% by vol - FY21 P2M Wallet payments mkt share: 65-70% by vol - FY21 P2M payments mkt share: 40% by vol - No.1 UPI beneficiary bank with FY21 mkt share of 17% - GMV of Rs 4,033 bn (FY19-21 CAGR: 33%)	- 337mn consumers (50mn MTUs) - 155mn PayTM UPI handles - 65mn payments bank accounts - 22mn merchants on platform	- Payments **cannot be monetised as UPI with zero MDR** is convenient alternative. - **c.65%** of PayTM's GMV corresponds to payments made with UPI - Hence, PayTM's payments take rate has halved from **1.4% in FY19 to 0.7% in FY21** - PayTM is **mkt leader in wallets but that is now only 0.6%** of system retail payments - PayTM Payments Bank has **only $0.7bn of deposits**, despite 50m active customers - As a payments bank, **PayTM cannot lend & cannot accept deposits >Rs 0.2mn**
Payment gateway	2012	- Largest payment gateway in India based on txn vols - Most merchant QR codes for any company in India	- 22mn merchants on platform - 5mn merchants use 'PayTM for Business' app	- Payments acquiring is difficult to monetise, esp. since PayTM is **unable to lend**
Consumer lending	2018	- 6.9mn loans disbursed to date of which 4.3mn loans disbursed in 1HFY22	- 0.7mn merchants accept PayTM Postpaid - Partnered with 2 NBFCs	- Assuming Rs 10k avg ticket size, total loan disbursed is only **c.Rs 25bn** in FY21 - PayTM's take rate in this disbursement would be **c.3%**, we believe
Credit Card	2020	NA	- Co-branded credit cards with HDFCB, SBI	- Card partnership **helps banks to tap into PayTM's customer** base for distribution - PayTM acts largely as a customer acquisition platform/distributor for large banks here
Wealth	2018	Combined AUM of $0.9bn in MFs, gold & stock broking	- 1.5mn users for MFs - c.307k unique trading clients - 74mn using digital gold	- Sub-scale distribution business with **only $0.9bn AUM** - **Zero commissions** as PayTM Money is a platform for non-distributor MF plans - Fringe player with **<1% market share** in equity broking
Insurance distribution	2020	- 32mn cumulative attachment & insurance products sold	- 11.4mn unique customers - 47 insurance company tie-ups	- Online channels only account for **1% of total industry** premium sold (FY20) - Policybazaar is already mkt leader in online insurance distribution (50% mkt share) - Remaining 50% of market dominated by banks' own online distribution
Ticketing	2015	- 2nd largest movie booking platform (by vol of tickets) in FY20	- All domestic airlines, 2k bus operators for travel	- All these business lines (ticketing for travel and entertainment, gaming, food delivery, ride hailing, commerce and cloud services, mini apps etc) are included in 'Commerce GMV' (**Rs 42bn i.e., only 1% of overall GMV**) - Take rates (calculated) however are much higher here at **~6% of GMV** - **Why super-apps?** Smartphone itself is a super-app. Also, it is difficult for a payments player to 'close the loop' on their platform in India (due to free alternative, UPI)
Gaming	2018	NA	28 mn users	
Mini app platform	2020	455 mini apps on platform	8.7mn active monthly users	
Advertising	2019	364 advertisers have run campaigns on PayTM platform	NA	

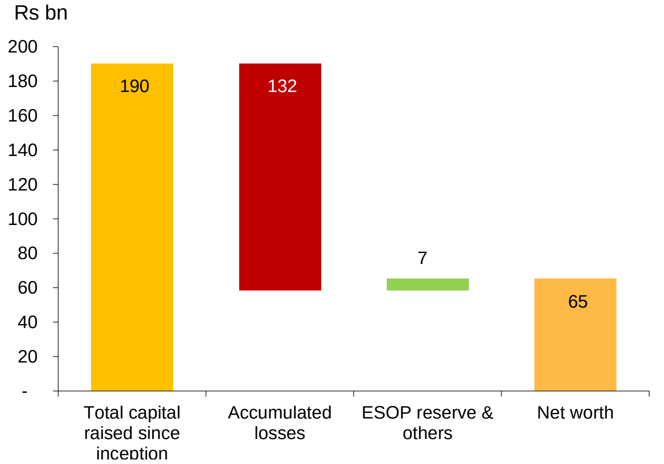
Source: Company, Macquarie Research, November 2021

PayTM - A cash burning machine

PayTM has been a cash burning machine, spinning off several business lines with no visibility on achieving profitability. As can be seen in the figures below, PayTM has drawn in equity capital of Rs190bn since inception, of which only c.70% (Rs132bn) has gone towards funding losses.

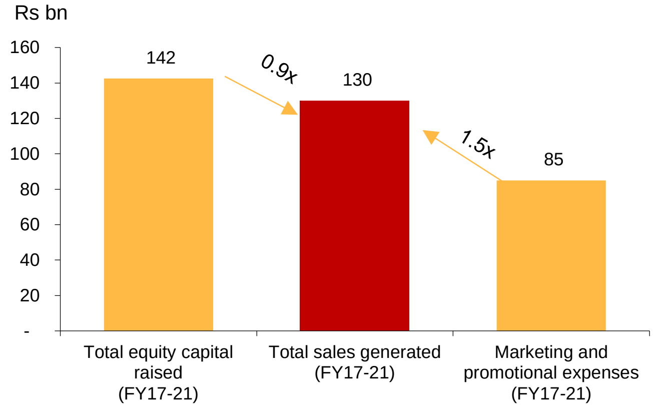
That PayTM has a problematic business model is exemplified in the figures below – the business generates very low revenues for every dollar invested or spent towards marketing. This is especially problematic for a low-margin consumer-facing business where competition across each vertical is only increasing.

Fig 2 PayTM has been a cash burning machine – 70% of capital raised since inception has funded losses



Source: Company data, Macquarie Research, November 2021

Fig 3 For a low gross margin business, PayTM generates low revenues per $ invested

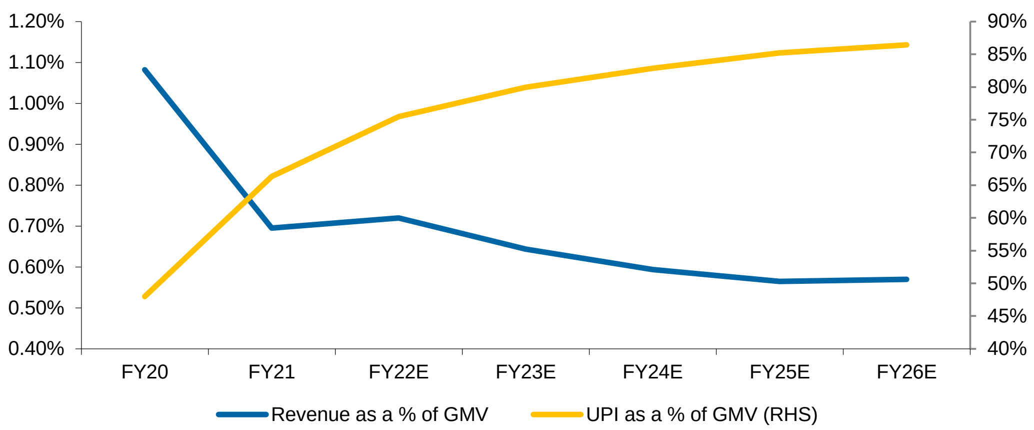


Source: Company data, Macquarie Research, November 2021

Payments business – a loss leader

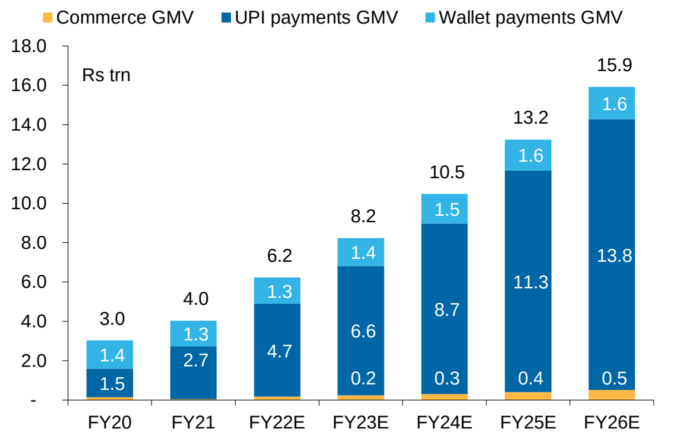
PayTM's payments-based business model has been disrupted by UPI – a real-time retail payment system developed by government-backed NPCI. In Dec-19, UPI was made available free of cost (zero MDR) by the Indian government, universally to consumers and merchants. UPI now accounts for ~65% of PayTM's GMV, which we expect to increase further to ~85% by FY26E. Hence PayTM's take-rates should continue to decline.

Fig 4 As UPI's share in PayTM's GMV goes up, payment take rates will come down



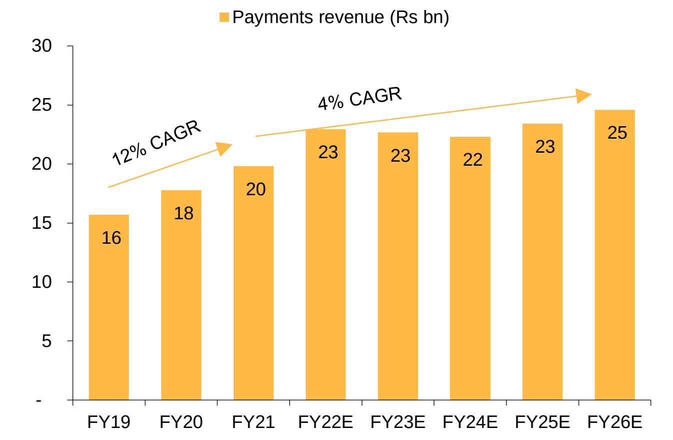
Source: Company data, NPCI, Macquarie Research, November 2021

Fig 5 We expect GMV to deliver a 32% CAGR over FY21-26, but led by zero-MDR UPI payments



Source: Company data, Macquarie Research, November 2021

Fig 6 Hence, we expect payments revenue to clock a mere 4% CAGR over FY21-26, despite strong GMV growth



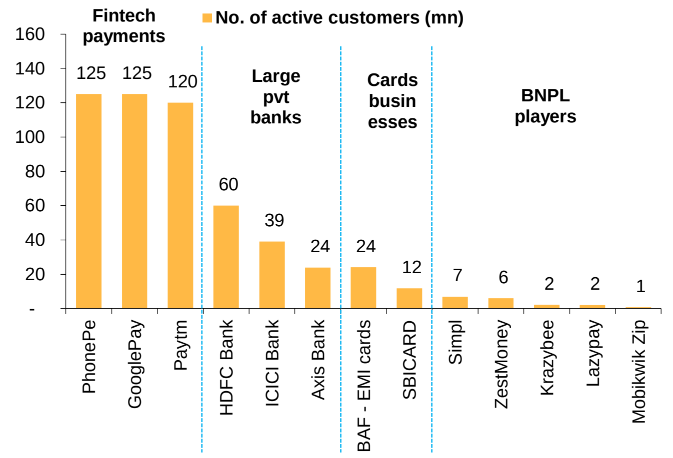
Source: Company data, Macquarie Research, November 2021

Financial product distribution – not scalable without a balance sheet

As a result of the large-scale disruption in retail payments, PayTM has been forced to pivot into several other businesses in search of profitability. It has amassed a 50mn+ strong active consumer base and 22mn merchant base, which it hopes to monetise by cross-sell/distribution of other products.

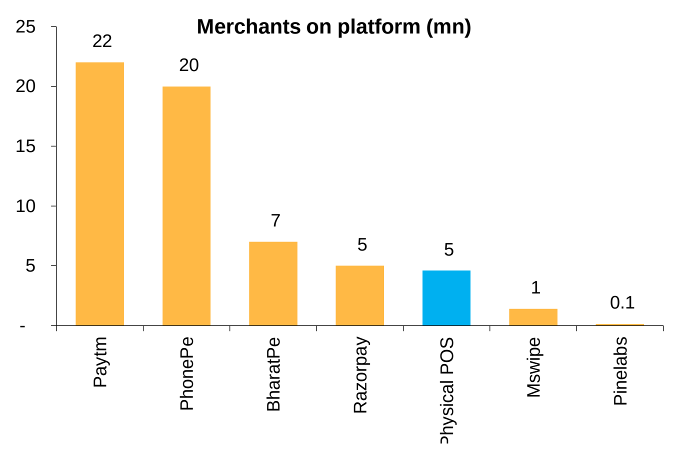
While the core payments business has been in operation since 2014, the company has spun off several verticals in the past 3 years including consumer lending (2020), co-branded credit cards (2020), insurance distribution (2020), wealth management (2018) and its mini-app platform (2020).

Fig 7 Positively, PayTM has built a strong customer base..



Source: Company data, Macquarie Research, November 2021

Fig 8 … and also on-boarded merchants at a large scale

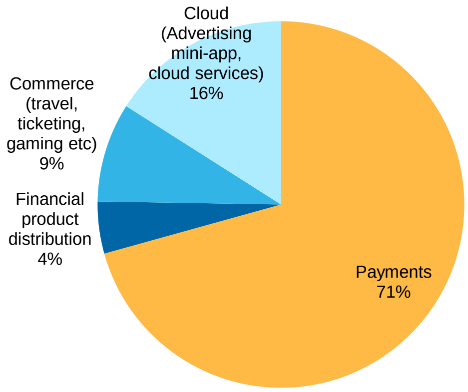


Source: Company data, RBI, Macquarie Research, November 2021

However, none of this has translated into significant revenues or profitability for PayTM. Furthermore, PayTM has not achieved any meaningful market leadership in any of its verticals outside payments.

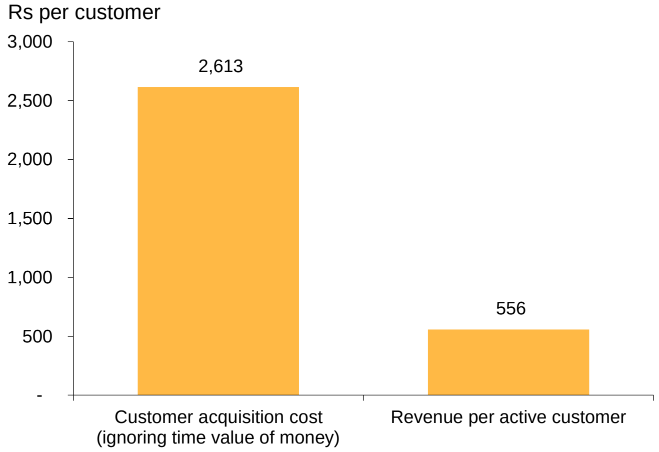
At best, we expect PayTM to generate US$ 350mn of revenues through distribution and we believe, that estimate is aggressive. Larger proportion of revenues can accrue ONLY if it starts lending which at present it can't do.

Fig 9 However, payments (low gross margin business) still account for 70% of revenues for PayTM (FY21)



Source: Company data, Macquarie Research, November 2021

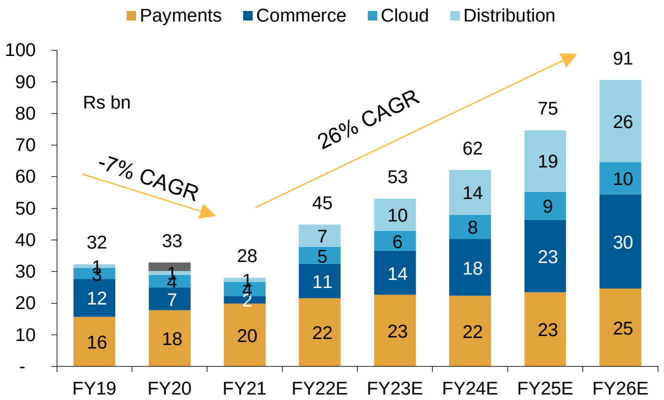
Fig 10 Revenue per active customer is still nowhere near recovering the cost of acquisition



Source: Company data, Macquarie Research, November 2021

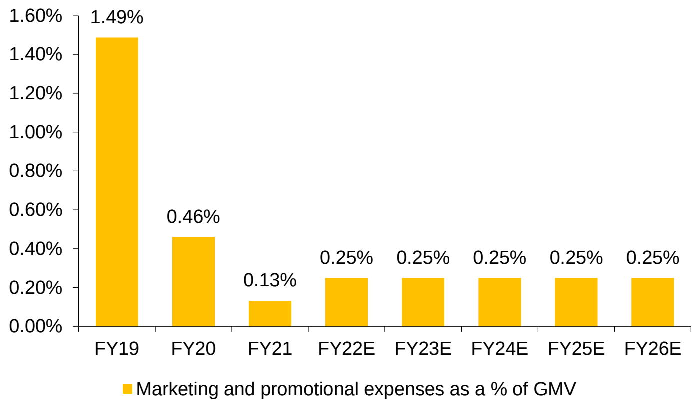
Having a payments bank in its group, PayTM cannot directly lend to its customer base, and hence it plans to act as a distributor of financial products (loans, MFs, insurance etc) to be able to monetise it. With competitive and regulatory pressures clamping down on disintermediation costs across financial services businesses, we are sceptical of how much profitably this business can be scaled up. Hence, despite assuming an aggressive 26% CAGR in overall operating revenues for PayTM over FY21-26, we fail to see EBITDA break-even by FY26. We expect it to be FCF positive only by FY30E in our model assumptions.

Fig 11 We expect revenues to deliver a 26% CAGR by FY26E, led by distribution & commerce (cross-sell) revenues



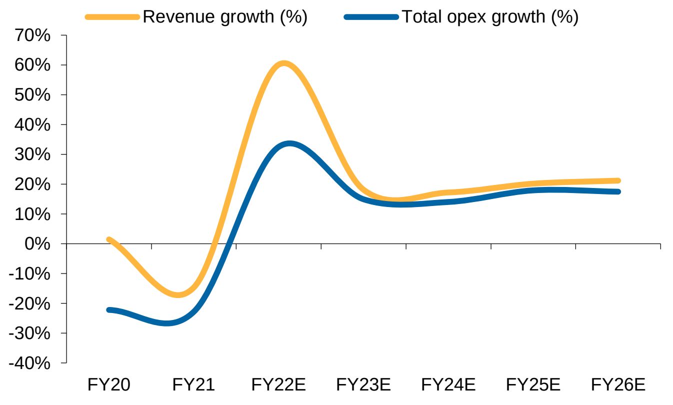
Source: Company data, Macquarie Research, November 2021

Fig 12 However, marketing and promotional expenses will also need to pick-up from current depressed levels



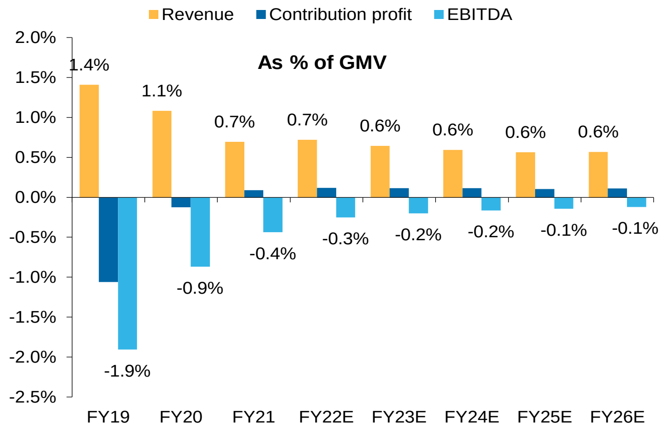
Source: Company data, Macquarie Research, November 2021

Fig 13 Opex growth will trail revenues but not nearly enough …



Source: Company data, Macquarie Research, November 2021

Fig 14 …Even in our aggressive revenue estimates we fail to see EBITDA break-even by FY26



Source: Company data, Macquarie Research, November 2021

As can be seen in Fig 15 below, the main driver for PayTM's operating costs over FY21-26, in our estimates, is the marketing & promotional expenses (50% CAGR over FY21-26E). We build a normalisation in this expense (25bps of GMV, as shown in Fig 12 above), as we believe the FY21 level is unsustainably low for PayTM's revenue growth to sustain. This is driving a 19% overall CAGR in operating expenses for PayTM. Unless marketing and promotional expenses pick up, a 26% revenue CAGR that we are forecasting is not possible in our view. We believe our revenue forecasts are reasonably aggressive.

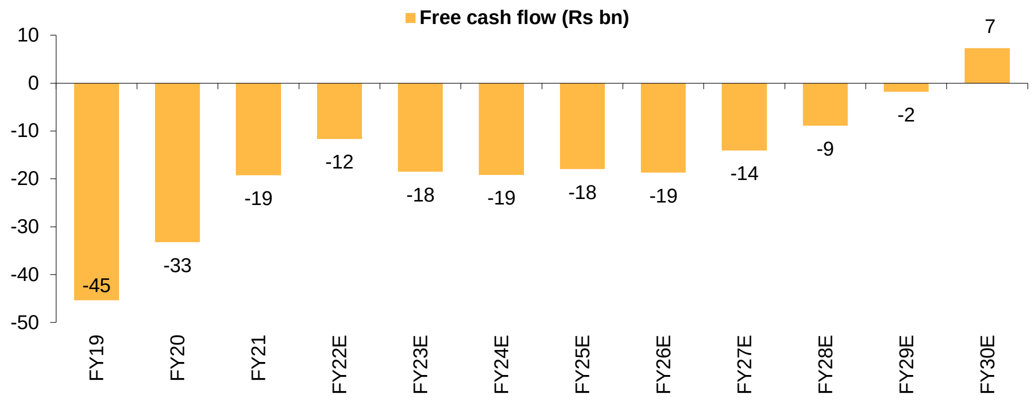
As a result, despite a strong 26% CAGR in operating revenues in our estimates, PayTM's EBITDA is flattish over FY21-26E.

Fig 15 We expect opex to deliver a 19% CAGR over FY21-26, largely led by normalisation of marketing expenses (50% CAGR). As a result PayTM's EBITDA is expected to remain flat over FY21-26

Rs bn	FY21	FY22E	FY23E	FY24E	FY25E	FY26E	CAGR (FY21-26)
Operating revenues	**28**	**45**	**53**	**62**	**75**	**91**	**26%**
Payment processing cost	19	22	23	24	28	33	12%
Marketing and promotional expenses	5	16	21	26	33	40	50%
Employee benefits expense	12	13	15	17	20	23	14%
Software, cloud and data centre expenses	3	4	4	4	4	4	5%
Other opex	6	6	7	8	9	9	10%
Total opex	**46**	**61**	**70**	**79**	**94**	**110**	**19%**

Source: Company, Macquarie Research, November 2021

Fig 16 We expect free cash flow to turn positive only by FY30E



Source: Company data, Macquarie Research, November 2021

Consumer loan distribution – credit cost experience is poor across fintechs

As highlighted, in our detailed India Fintech report, for long-term sustainable profits in consumer lending, fintechs like PayTM must resort to use of their own balance sheets. Otherwise, the unit economics in a distribution-led business with wholesale funding and elevated credit costs is not practical, in our view. In fact, the credit cost experience for Indian fintech lenders has been exceptionally poor with several fintechs reporting mid-teen credit costs. High credit costs, coupled with high funding costs and low-lending ticket sizes make fintechs' distribution only approach to consumer lending unviable in our view, and PayTM is no different.

Fig 17 Credit cost experience for Indian fintech lenders has been poor. 'Distribution-only' business models of fintech lenders is not scalable, in our view

Fintech	Business line	Asset quality
PayU finance	BNPL (Lazypay) and personal loans	FY21 GNPLs at **19%**. FY21 credit cost at **11%**
Mobikwik	BNPL	FY21 Credit cost at **20% of GMV**
KrazyBee	BNPL	9MFY21 credit cost at **10%**. As of Feb 21, restructured portfolio is at **19%**
CapitalFloat	BNPL (Amazon PayLater) + SME financing	1HFY21 credit cost at **11%**
Simpl	BNPL	FY20 credit cost at **150%** of revenues
LendingKart	Unsecured SME loans	FY21 credit cost at **7%**. Restructuring at **20%**

Source: Company data, Credit rating agencies, Macquarie Research, November 2021

We don't think PayTM is likely to get any banking license

PayTM is constrained from lending due to its payments bank license, which does not allow it to assume credit risk in any form. PayTM Payments Bank completes 5-years of commercial operations in May-2022 and would then become eligible to apply for a small finance bank license, which would enable it to lend to its customer base. It would also enable it to freely accept deposits, which are now constrained at a limit of Rs 0.2m per customer, under its payments bank license.

However, in our view, PayTM is not a practical contender for a universal / small finance bank license. The main reason in our view is that Chinese controlled firms, Alibaba and Ant group still own close to 31% stake in One97 Communications (PayTM parent entity) post the IPO. If we consider a pass through to the PayTM payments bank, then the Chinese controlled entities still own around ~15% stake in the payments bank. This may not be looked at favourably by the regulator, in our view.

RBI also in general has stayed away from granting any banking license to any corporate-backed entity. While this has been proposed by an internal working group of RBI, it remains highly unlikely that this will change in the near future, in our view.

Add to that PayTM's complicated organisation structure, inter-party/related party transactions could be a cause of concern for the regulator in our view. We have discussed some of the corporate governance aspects in the later part of the report.

Regulatory risk is real

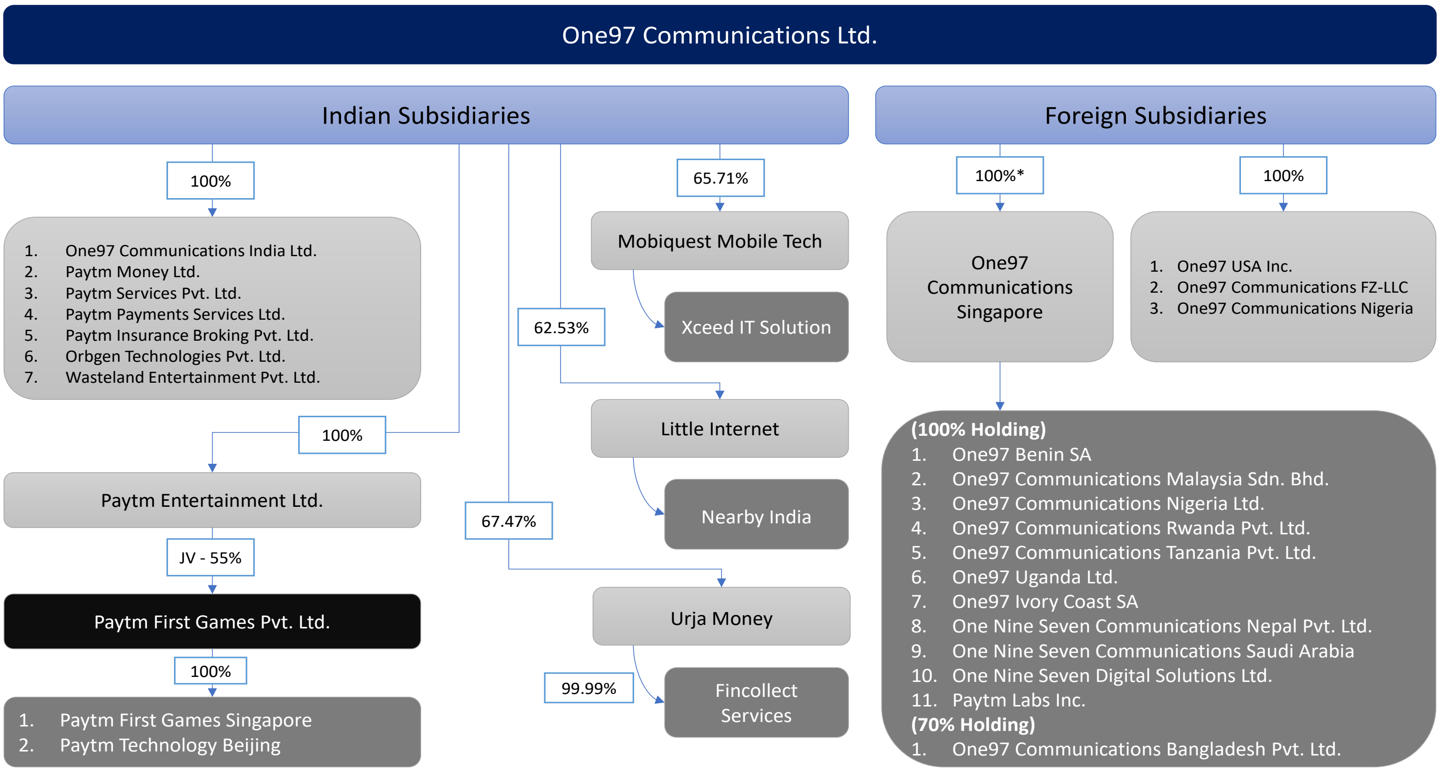
On the flip side there are several risks to PayTM's (and all fintechs) financial services distribution-led business model from a regulatory standpoint, in our view. There are several examples of regulators – SEBI, IRDA and RBI clamping down on financial services distributors to reduce frictional costs to the consumer and prevent mis-selling.

RBI could ask fintechs to maintain a certain fraction of loans originated on their own balance sheet (similar to securitisation norms). It could also prescribe capital requirements for loan originating fintechs, as applicable for NBFCs and banks in the system. In recent speeches, RBI has hinted at the same. Similar regulatory interventions in China over the past year have had serious repercussions on unit economics of fintech players like Ant Financial.

Corporate governance – scope for improvement exists

PayTM's group organisation structure is complex - One 97 has close to 15 domestic subsidiaries and 17 international subsidiaries. This opens up risks of related-party transactions and there have been inter-party/related party transactions (discussed in detail in sections below), in the past which have attracted regulatory attention.

Fig 18 PayTM has a complex organisation structure. Key subsidiaries are shown below



Source: Company data, Macquarie Research, November 2021

Furthermore, PayTM has a seen a host of senior executives resigning in the run up to its IPO. The board strength is 8 members and only 2 of these are based in India. PayTM ranks “below median” in our MGRS (governance and risk score) framework of corporate governance. Refer the section on governance for more details.

Our valuation for PayTM implies a ~40%+ downside

Considering PayTM’s heavily cash-burning business model, no clear path to profitability, large regulatory risks to the business and questionable corporate governance, we believe the company is overvalued at the upper end of price band of Rs2,150.

Despite our aggressive revenue growth assumptions (26% CAGR over FY21-26E vs minus 7% CAGR in FY19-21), we fail to see how the business can break-even at an EBITDA level by FY26 and a FCF level by FY30E, as shown in Fig 14 and 16 above.

We value PayTM using 0.5x PSg multiple on Dec-23 annualised sales to arrive at our TP of Rs1,200, implying 44% downside to the upper end of its IPO price band (Rs2,150).

Fig 19 PayTM valuation – based on price-to-sales growth (PSg) methodology implies a ~45% downside

PSg - based valuation	
CAGR sales growth (FY26-21)	26.4%
Dec-23 annualised sales (Rs m)	55,312
Target PSg multiple (x)	0.5x
Valuation based on PSg (Rs m)	772,453
No. of shares (m)	644
Target price (Rs)	**1,200**

Source: Macquarie Research, November 2021

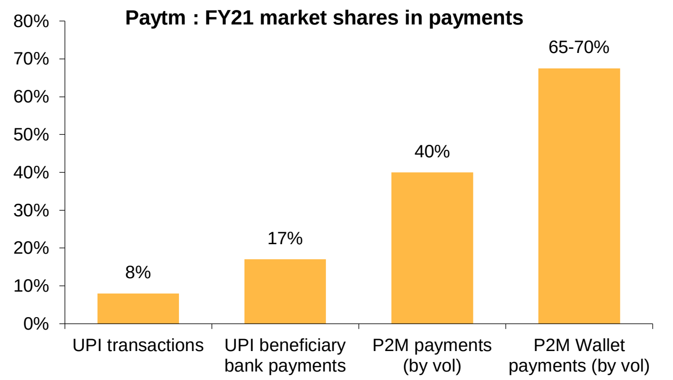
PayTM can't monetise payments, which has been disrupted by UPI

Wallets have become irrelevant

Payments business – A loss making proposition

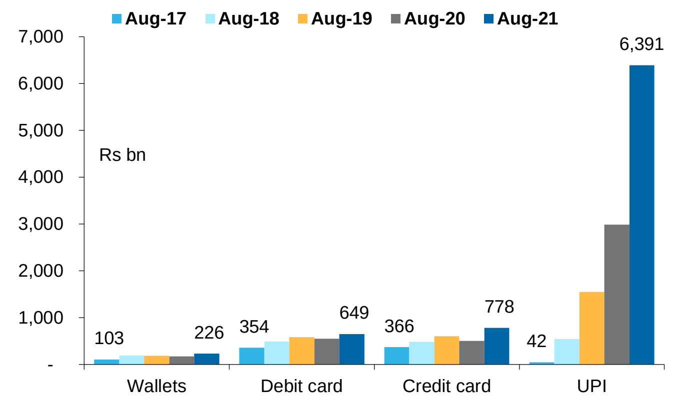
PayTM is the market leader in the mobile wallet space where it was one of the early movers. However, as seen in Fig 21 and 25, mobile wallets have become increasingly irrelevant (<1% of retail payments) since the advent of UPI.

Fig 20 PayTM is a market leader in mobile wallet payments – but this business is becoming increasingly irrelevant



Source: One97 IPO prospectus, Macquarie Research, November 2021

Fig 21 Wallets (PPIs) are now <1% of overall non-cash retail payments vs 15% for UPI

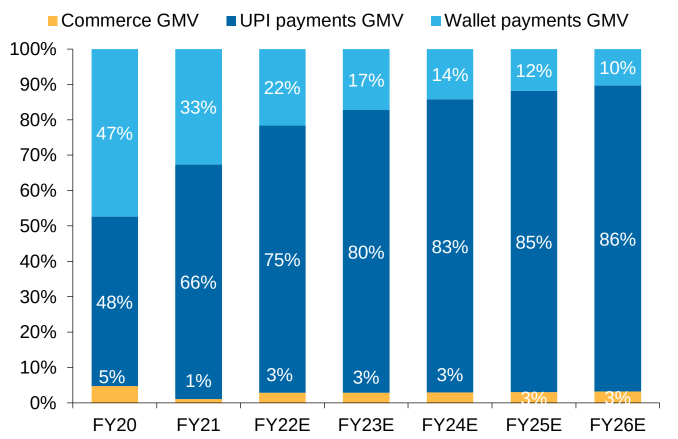


Source: RBI, Macquarie Research, November 2021

PayTM is also a leading player in P2M payments as per Redseer, with ~40% market share of payments by volume in FY21. However, as we've pointed out earlier, a significant part of this is through the UPI route, which cannot be monetised. In Dec-19, Govt of India mandated that merchant discount rates (MDR) for all UPI transactions, will be zero. UPI is hence completely free of cost to both the customer and the merchant.

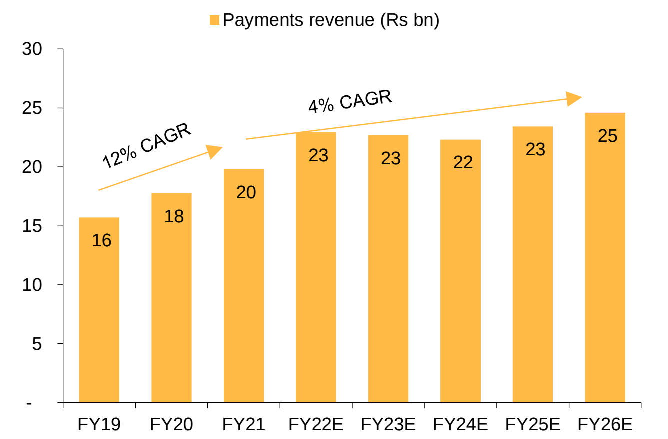
UPI payments account for c.65% of PayTM's FY21 GMV in our view, which will further scale up to ~85% by FY26. As a result, PayTM's payments revenues will only deliver a 4% CAGR over FY21-26E in our estimates, despite our aggressive assumption of 32% CAGR in GMV over the same period.

Fig 22 UPI payments will scale up to ~85% of PayTM's GMV by FY26, in our view



Source: Company data, Macquarie Research, November 2021

Fig 23 Hence, payments revenues should only clock 4% CAGR over FY21-26, despite 32% GMV CAGR in our estimate



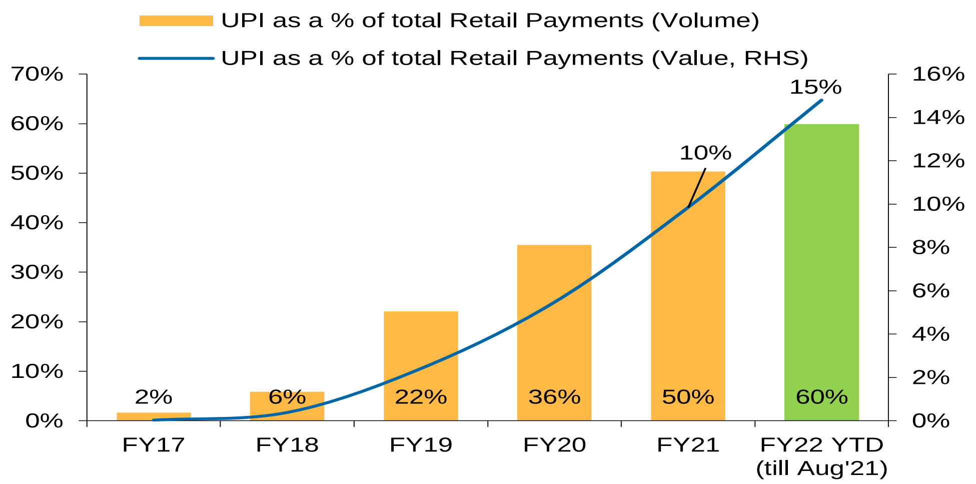
Source: Company data, Macquarie Research, November 2021

UPI has disrupted PayTM's payments revenues

Retail payments in India has been witness to a massive overhaul over the past 5 years. UPI – a real-time, bank-to-bank payment system launched by National Payments Corporation of India (Govt owned entity) in Apr-16, has now grown to 60% of system payments by volume. UPI is a ubiquitous offline as well as online mode of payment, that is now head and shoulders above all other form factors of retail payment (cards, mobile wallets etc).

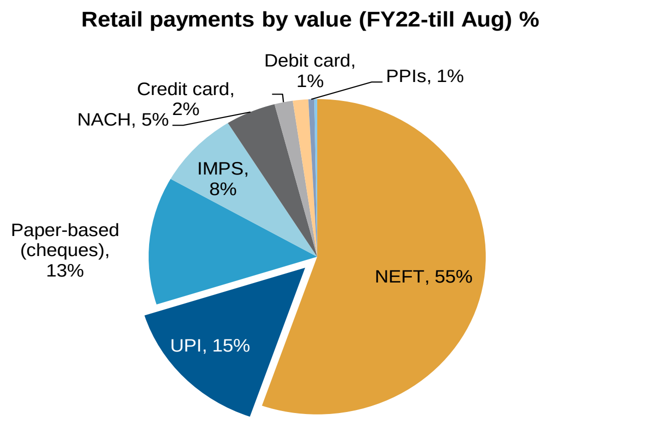
UPI has been made completely free of cost to both consumers and merchants (zero MDR), since Dec-19. This has enhanced UPI's payments value proposition even more – monthly transactions via UPI (in value terms) are now 3.5x since Dec-19.

Fig 24 UPI now accounts for 60% of system retail payments by volume (15% by value)



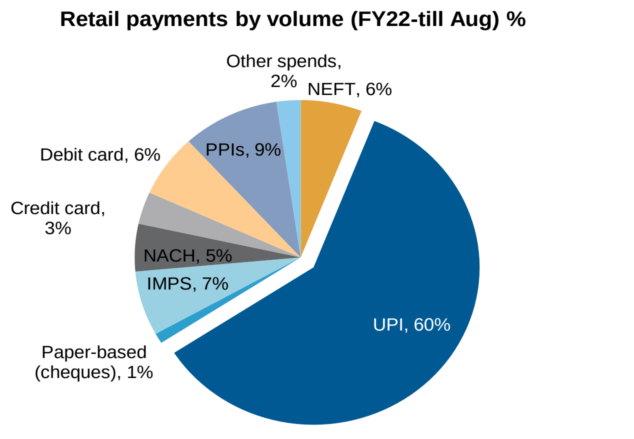
Source: RBI , Macquarie Research, November 2021

Fig 25 UPI is 2nd largest mode of retail payment (by value) in system



Source: RBI, Macquarie Research, November 2021

Fig 26 …and the largest in volume terms



Source: RBI, Macquarie Research, November 2021

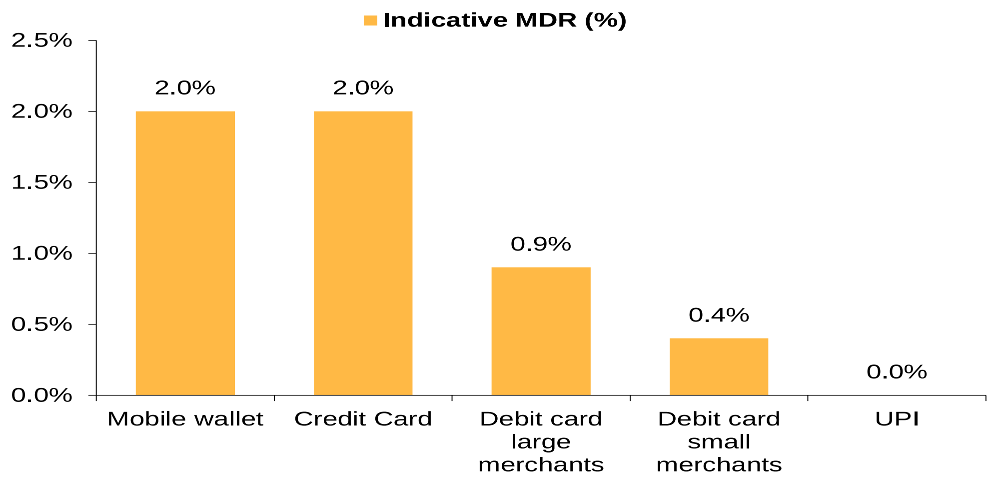
UPI has up-ended business economics for payments system providers. To the extent that we believe standalone payments as a business model cannot succeed in India. Payments is at most a loss-leading customer acquisition engine for fintechs.

As payments by itself cannot be monetised, fintech payments players must figure out a sustainable and profitable alternative. This could include a) financial product manufacturing i.e., lending or b) distribution or cross-sell of other products on the platform.

As a 49% holder in PayTM Payments Bank (which is not allowed to lend as per RBI license conditions), PayTM cannot directly lend to its customer base. Hence, distribution/cross-selling has been the way to go for PayTM.

Also, zero MDR on UPI payments poses another more significant problem for online platforms, in our view. Payments now cannot be the hook to 'close the loop' on an online platform – as payments providers cannot provide consumers platform benefits like cashbacks/incentives/rewards in an economically viable way. At the same time, UPI with its zero MDR proposition is also much more attractive to merchants, who are incentivised not to use other payment modes like wallets.

Fig 27 UPI is a very convenient mode of payment and is also zero-cost to the consumer & merchant



Source: Macquarie Research, November 2021

A snapshot of PayTM's charges at its payment gateway, for different modes of payments is shown below.

Fig 28 PayTM : Online MDR take rate at PayTM payment gateway)

Payment Instrument	Small Medium Business	Enterprise
	Merchant Discount Rate	Merchant Discount Rate
UPI - Standard	0%	We understand scale. Get in touch for a custom pricing plan designed for your business requirement.
UPI - Subscription	₹5- 65 per mandate for annual subscription plan	
Paytm Wallet	1.99%	
Credit Card*	1.99%	
Debit Card* - Rupay	0%	
Debit Card* - Mastercard & VISA	0.4% for Below ₹2,000 0.9% for more than ₹2,000	
Netbanking	1.99%	
International PG	2.9%	

Source: PayTM website, Macquarie Research, November 2021

Fig 29 PayTM: Offline (In-store) MDR take rates at PayTM QR POS

Payment Instrument	Merchant Discount Rate (MDR)	Monthly Acceptance Limit
Paytm Wallet	0%	Unlimited*
UPI Payment	0%	
Rupay Debit Card	0%	

Transaction limit: Unlimited *

Get Started

* Transaction limit depends on the number of required documents provided by merchants.

** Above pricing is applicable for SME merchants.

Source: PayTM website, Macquarie Research, November 2021

From the table of charges in the figures above we can infer that:

a) PayTM makes no revenue through UPI payments – as an issuer or acquirer

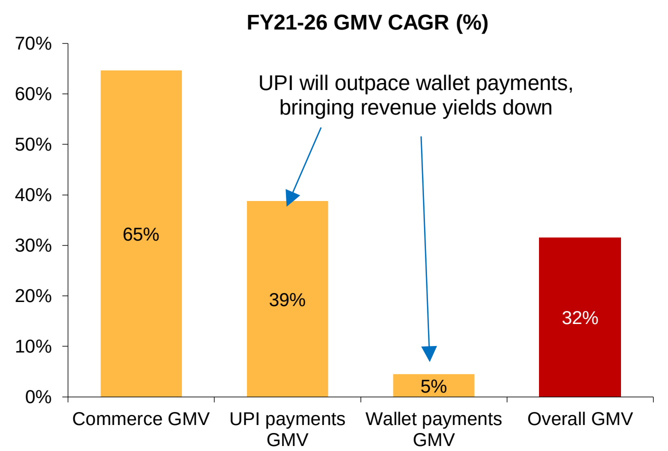
b) PayTM only makes revenues as an issuer on wallet transactions (where its gross take rate is ~2%)

c) As a payments acquirer, PayTM largely only recovers the cost of a credit card/debit card transaction from the merchant (to pay to the issuer).

Hence, wallet transactions are the only revenue generating piece in PayTM's payments business.

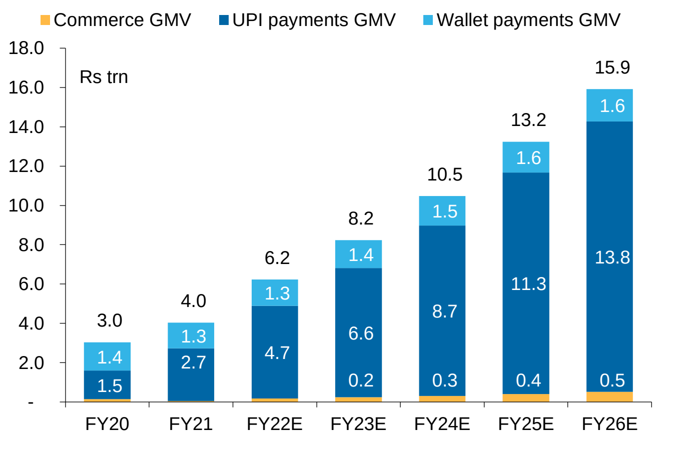
This reinforces our view that standalone payments cannot be a viable revenue/profit engine for PayTM. Further evidence lies in PayTM's own operational metrics.

Fig 30 We expect PayTM's overall GMV to deliver at 32% CAGR over FY21-26 led by UPI payments



Source: Company data, Macquarie Research, November 2021

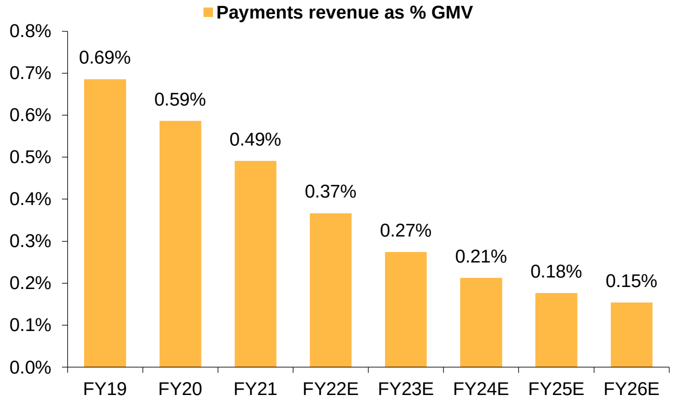
Fig 31 UPI payments will further inch up to ~85% of overall GMV by FY26 in our view (65% in FY21)



Source: Company, Macquarie Research, November 2021

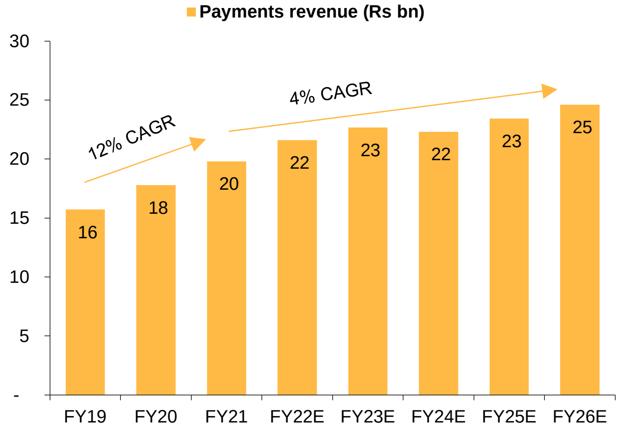
PayTM's take rates in payments have been continuously falling and will continue to do so as the share of UPI in the overall mix picks up. As a result, we expect overall payments revenues to drag – clocking only a 4% CAGR over FY21-26E vs 32% CAGR in GMV. The commerce GMV shows a very rapid growth but that is coming off a small base and overall commerce GMV is still a small proportion of overall GMV as shown in figure 31.

Fig 32 As a result, payments take rates will continue to fall, as UPI earns zero MDR



Source: Company, Macquarie Research, November 2021

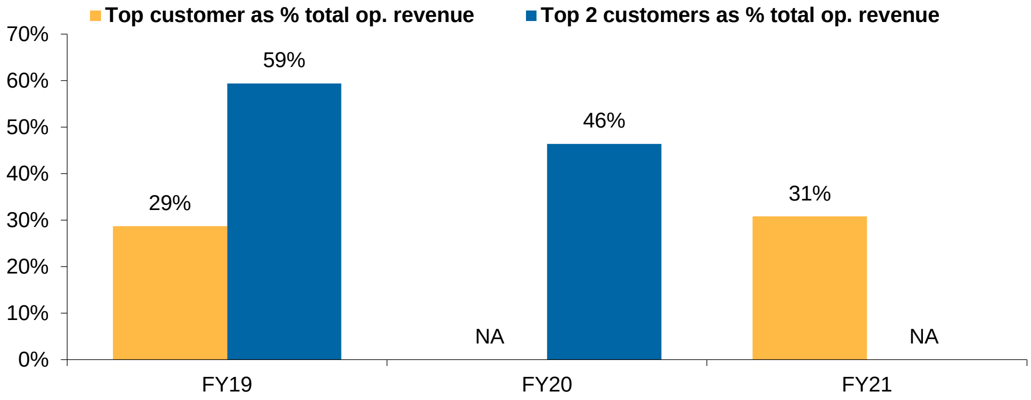
Fig 33 We expect payments revenue to clock a mere 4% CAGR over FY21-26, despite 32% CAGR in GMV



Source: Company, Macquarie Research, November 2021

Separately, we also believe there are significant concentration risks in PayTM's payments business. As can be shown in Fig 34 below, ~30% of PayTM's operating revenues are derived from a single large customer (FY21). This has been a trend that has been persistent for the past 3 years, with chunky revenues derived from top 2 customers, as shown below.

Fig 34 Concentration risks: ~30% of PayTM's revenues are derived from a single external customer

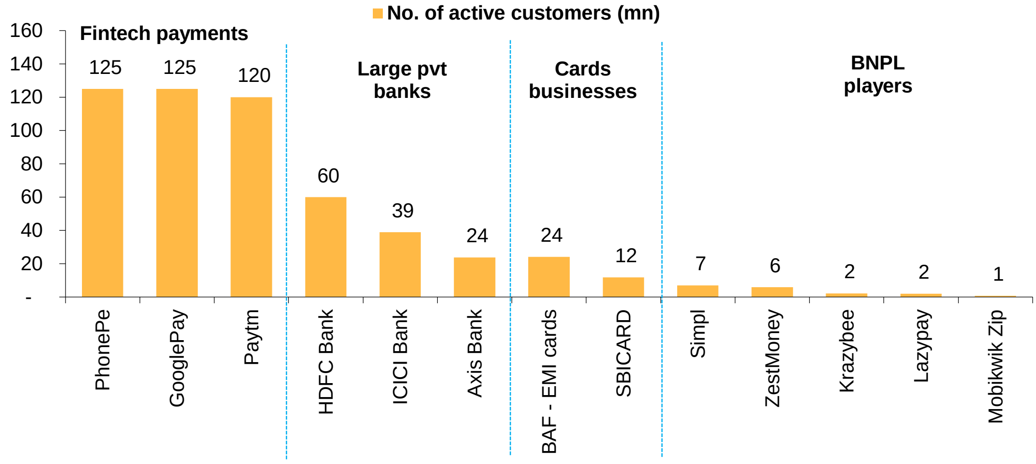


Source: Company data, Macquarie Research, November 2021

How has payments business fared as customer/merchant acquisition tool?

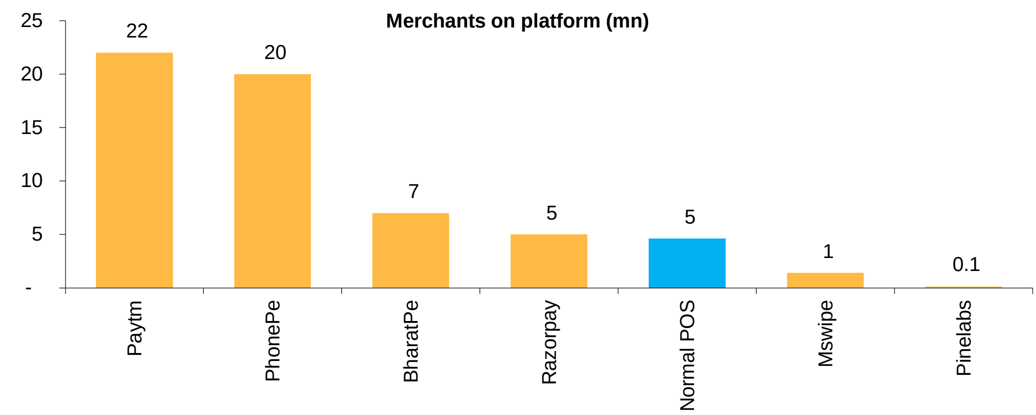
PayTM has amassed sizable consumer & merchant ecosystems as shown in the figure below. However, PayTM's inability to monetise any of this successfully has been a sore pain point in our view and is symbolic of the weak value proposition of its platform.

Fig 35 PayTM has amassed a sizable customer base



Source: Company data, Macquarie Research, November 2021

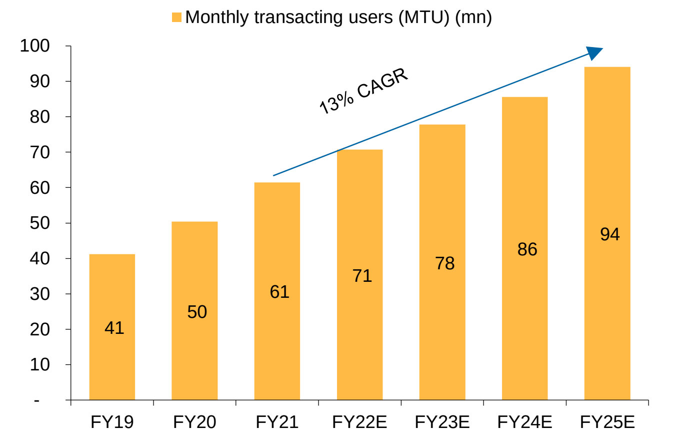
Fig 36 As well as a large merchant acquiring ecosystem



Source: Company data, RBI, Macquarie Research, November 2021

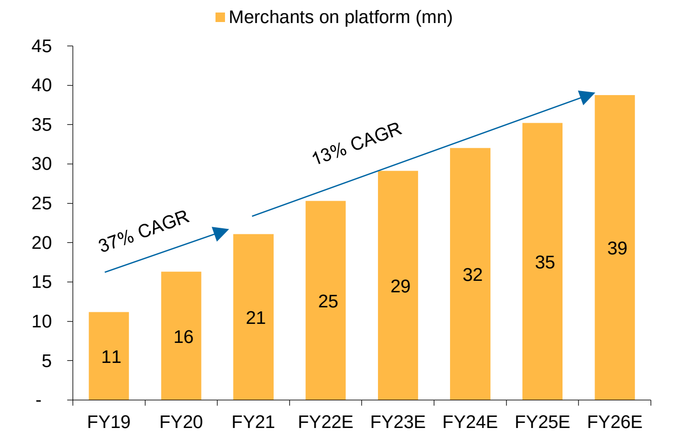
We expect PayTM to continue to scale up its consumer franchise at mid-teen CAGR over the next 5 years. However, the growth in the number of merchants on platform should slow down as penetration peaks out considering that there are around 60-70mn merchants in India and a large proportion of them are not bankable/credit worthy, in our view, as they are micro-SMEs. India only has c.65mn MSMEs at present and PayTM's penetration in merchant acquisition is already very high at c.30-35%.

Fig 37 We expect PayTM to scale up its monthly transacting users at a 13% CAGR



Source: Company, Macquarie Research, November 2021

Fig 38 Merchant acquisition rates is also expected to clock a 13% CAGR over FY21-26E



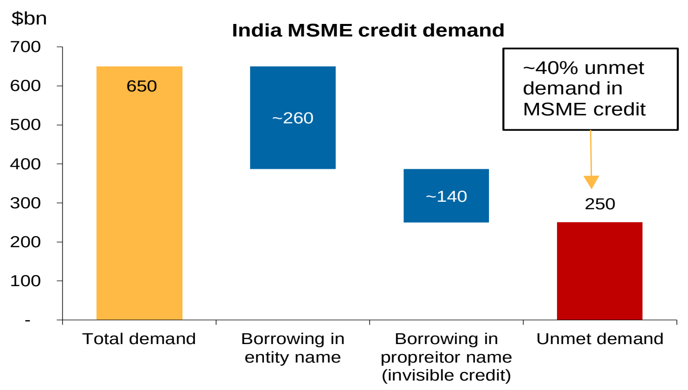
Source: Company, Macquarie Research, November 2021

The key monitorable for PayTM will be to see how PayTM manages to monetise its consumer-merchant ecosystem. Since payments clearly is not the answer, it will have to look elsewhere – as discussed in the sections that follow.

How scalable is the merchant franchise?

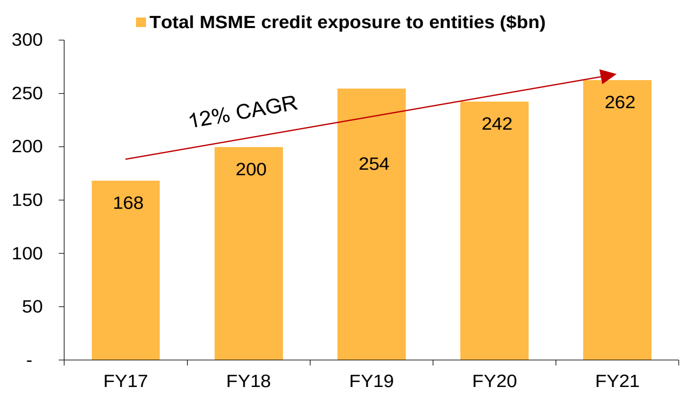
Credit to small merchants / MSMEs in India has always been an underpenetrated segment. In fact, some estimates (shown in Fig 39 below), suggest that there is a ~40% unmet demand for MSME credit in India – which translates to a $250bn credit opportunity. Yet despite this large opportunity, MSME credit has only hobbled along at a 12% CAGR over the past 5 years. Clearly, there is some disparity between the 'on-paper' demand for merchant loans, and the actual bankable demand, in our view.

Fig 39 India has $250bn shortfall in meeting MSME credit requirement



Source: BCG, TU CIBIL, World Bank, Macquarie Research, September 2021

Fig 40 Yet MSME credit has only grown at 12% CAGR since FY17

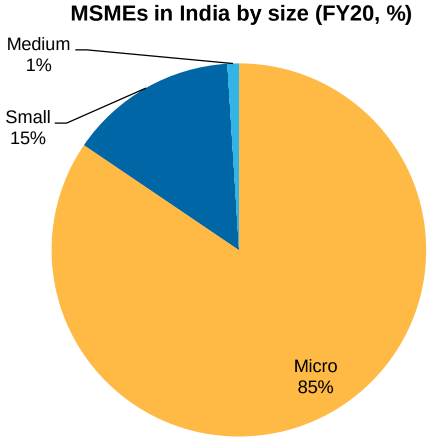


Source: TU CIBIL, Macquarie Research, November 2021

A significant majority of MSME credit is not bankable, in terms of creditworthiness, in our view. Banks and NBFCs have largely catered to the top layer of MSMEs in India. And yet, their NPLs in this segment have been woefully high at 12-13%, as shown in Fig 42 below.

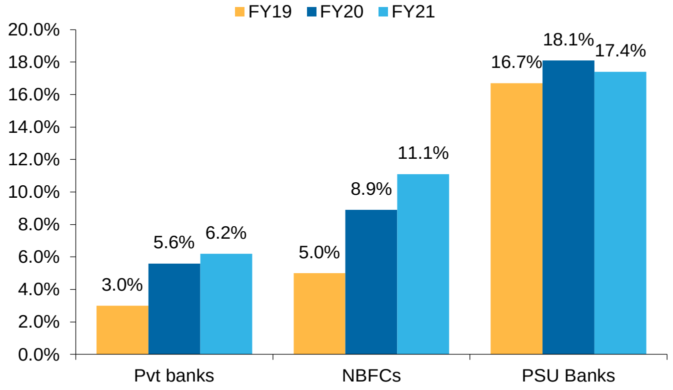
Furthermore, ministry of MSME data for FY20 suggests that **85% of India's c.65mn MSME units are only 'micro' enterprises (i.e., investment in plant & machinery < Rs 2.5mn).** Hence, while this does seem like a very large & underpenetrated segment in terms of volume, we believe that the size of the opportunity in value terms is not as large.

Fig 41 85% of India's ~65mn MSMEs are micro units



Source: Ministry of MSME report, Praxis, Macquarie, November 2021

Fig 42 Banks and NBFCs have largely lent to the top/creamy layer of MSMEs and still had high NPLs



Source: TU CIBIL, Macquarie Research, November 2021

In our estimates for factoring in merchant loan distribution revenues, we have factored the following assumptions:

- No. of merchants on PayTM's platform goes to 39m by FY26E (from 22mn currently)
- Average ticket size for merchant loan disbursements goes to Rs 79k by FY26E
- Loans as a percentage of merchants on the platform is ~8%. This is in line with our view that the bulk of the MSMEs in India (and on PayTM's platform) are not bankable – dues to sub-scale operations, lack of creditworthiness etc
- PayTM's take rates on merchant loan distribution is 3%, gradually paring down to 2.6% by FY26E.We believe online distribution take rates will go down with increasing competition
- Based on our assumptions, (calculations in figure below) – PayTM can generate distribution revenues of ~US$ 86m in FY26E through merchant loans

Fig 43 Merchant loan distribution – what are we building in our estimates?

Merchant loan distribution – Our Model Assumptions	**FY22E**	**FY26E**
No. of merchants on PayTM platform (mn)	25	39
No. of loans disbursed (mn) (A)	2.0	3.1
Loans as % of merchants on platform	8%	8%
Avg ticket size of merchant loans disbursed (Rs '000) (B)	45	79
Total loans disbursed by PayTM (Rs bn) (C = A x B)	90	241
Paytm's take rate on loans disbursed (%) (D)	3.0%	2.6%
Merchant loan Distribution revenue for Paytm (Rs bn) (E = C x D)	**2.7**	**6.4**
Merchant loan Distribution revenue for Paytm (US $ mn)	**36**	**86**

Source: Macquarie Research, November 2021

Hence, we see that the merchant lending opportunity for PayTM is not as large as is made out to be (<$100mn average revenue run-rate). In our estimates, we have not assumed any direct / on-balance-sheet lending revenues for PayTM, as it cannot assume credit risk. If PayTM is able to lend on its own balance sheet, there could upside risks to our estimates.

For a lending business to be profitable at scale, lending with own balance sheet is a must, in our view.

Overall distribution business at best a $350mn revenue opportunity for PayTM

Distribution segment – Building scale with profitability is an issue

Overall distribution business at best is a $350mn revenue opportunity for PayTM

As PayTM is constrained by its payments bank license, it cannot lend on its own balance sheet. Instead, PayTM plans to monetise its 50mn+ customer base by distributing financial products to it. This is an avenue that has always been open to PayTM but has only been explored by the company recently. Financial product distribution was only 5% of operating revenues in FY21. We expect this to go to ~30% of overall revenues or roughly cRs26bn (~US$350mn) by FY26E. Refer fig 49 for more details.

We believe PayTM can scale up its consumer/merchant loan distribution business, to an extent by selling down consumer loans/ BNPL loans/ merchant loans to its customer & merchant base. For this purpose, PayTM has tied up with NBFCs/bank partners (Clix Capital, Arthimpact, Suryoday SFB & AB Capital) for warehousing BNPL (PayTM Postpaid) and personal loans generated on its platform.

Fig 44 Financial product distribution business – Loan distribution could be a key revenue driver for PayTM going forward

Business line	Business launched	Scale achieved	Customer & merchant franchise	Our take
Consumer lending	2018	- 4.3mn loans disbursed by PayTM in 1HFY22	- 0.7mn merchants accept PayTM Postpaid - Partnered with 2 NBFCs to warehouse loans	- Assuming Rs 10k avg ticket size, total loan disbursed is only **c.Rs 25bn** in FY21 - PayTM's take rate in this disbursement would be **only c.3%**, we believe
Credit Card	2020	NA	- Co-branded credit cards with HDFCB, SBI	- Card partnership **helps banks to tap into PayTM's customer** base for distribution - PayTM acts largely as a customer acquisition platform/distributor for large banks here
Wealth	2018	Combined AUM of $0.9bn in MFs, gold & stock broking	- 1.5mn users for MFs - c.307k unique trading clients - 74mn users using digital gold service	- Sub-scale distribution business with **only $0.9bn AUM** - **Zero commissions** as PayTM Money is a platform for non-distributor MF plans - Fringe player with **<1% market share** in equity broking
Insurance distribution	2020	- 31mn cumulative attachment & insurance products sold	- 11.4mn unique customers - 47 insurance company tie-ups	- PayTM primarily sells small ticket movie & travel ticket cancellation insurance - Online channels only account for **1% of total industry** premium sold in India (FY20) - Policybazaar is already mkt leader in online insurance distribution (~50% mkt share) - Remaining 50% of market is dominated by banks' own online distribution

Source: Company data, Macquarie Research, November 2021

PayTM has also partnered with leading banks (HDFC Bank and SBI). Card partnership helps banks to tap into PayTM's customer base for distribution. PayTM acts largely as a customer acquisition platform/distributor for large banks here.

The other distribution businesses – wealth management, broking & insurance distribution are largely sub-scale at present, as can be seen in the table above

A 'distribution-only' model is not scalable, in our view. Balance sheet is a must

In our view, the 'distribution-only' approach in consumer lending, where PayTM piggy-backs on another lender's balance sheet is not sustainable or highly scalable. We have highlighted this earlier in our India Fintech Report, as a key problem affecting fintech scalability in India.

Fintechs involved in consumer lending in India face prohibitively high credit costs as well as high wholesale funding costs, which do not make the business economically viable. This is exacerbated even more because of the low-ticket size and unsecured nature of loans on these platforms.

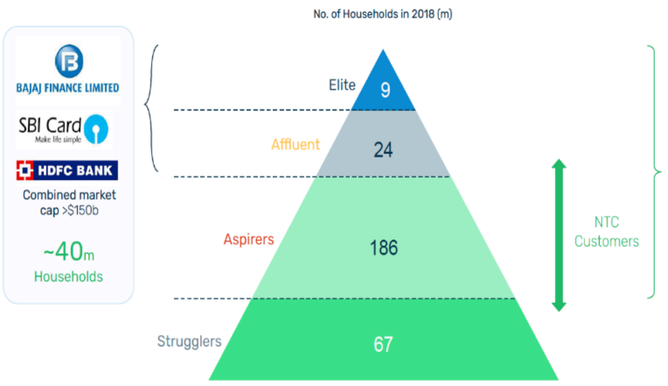
We continue to believe consumer lending can be scaled profitably only as a 'balance sheet' and not a 'distribution-only' business in India.

The total addressable market (TAM) from consumer loan distribution will only be $1.5-2bn of revenue pool by FY26E, in our view

The addressable opportunity for fintechs largely lies in the unbanked/under-banked segments not catered to by mainstream banks and NBFCs. As per Zestmoney, the opportunity in consumer loans is towards the ~200mn 'aspiring' households which are not catered to by banks with credit card / personal loan / consumer durable loan offerings. In other words, the low hanging fuit for fintechs like PayTM lies in sub-prime segments.

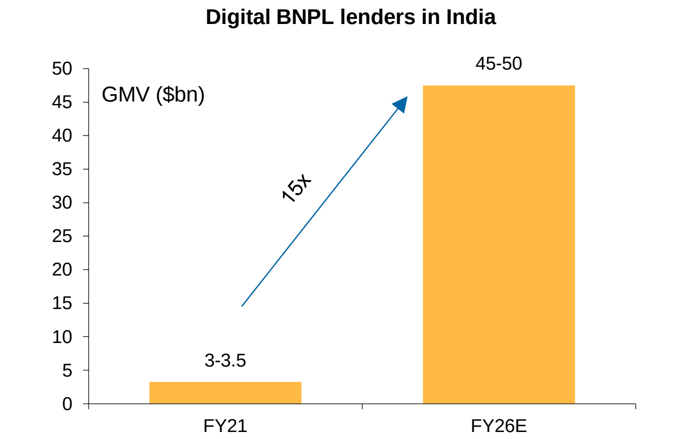
As per Redseer, digital BNPL players' GMV could scale up 15x to $45-50bnby FY26E. We believe this is where the opportunity for PayTM in consumer lending lies. However, since PayTM will largely be engaged in selling down these loans to partner banks/NBFCs balance sheets, the addressable fee pool is much lower.

Fig 45 Fintech consumer lending opportunity is in the untapped ~200mn 'aspiring' households in India



Source: Zestmoney, Macquarie Research, November 2021

Fig 46 Digital BNPL spends in India will grow 15x to $45-50bn by FY26E, as per Redseer



Source: Redseer, Macquarie Research, November 2021

If we assume a 3% take rate for the industry, the total addressable fee pool works out to just ~$2bn for the fintech BNPL industry as shown in Fig 47 below.

Hence, our estimates for PayTM work out to US$250mn revenues by FY26E, which represents ~12% market share in consumer loan distribution / BNPL (Fig 47 below) . We believe this is a reasonable assumption to work with. These estimates reinforce our view that the bigger profit pool lies in lending using own balance sheet, rather than a distribution-only approach.

Fig 47 By our estimates, consumer loan distribution fees could be a ~$2bn addressable market by FY26E, of which PayTM will garner ~12% market share

Fintech consumer lending fee pool - how big can it get?	**US$ bn**
Digital BNPL GMV (FY26E, Redseer est)	45
Other fintech consumer lending (FY26E, Macq est)	25
Total fintech-led consumer lending	**70**
Average distribution take rate (Macq est)	3%
Total addressable fee pool (FY26E)	**2.1**
Our FY26E consumer loan distribution revenue est. for PayTM (Rs 18bn in FY26E)	0.25
Implied consumer loan distribution market share for PayTM in our estimates	**12%**

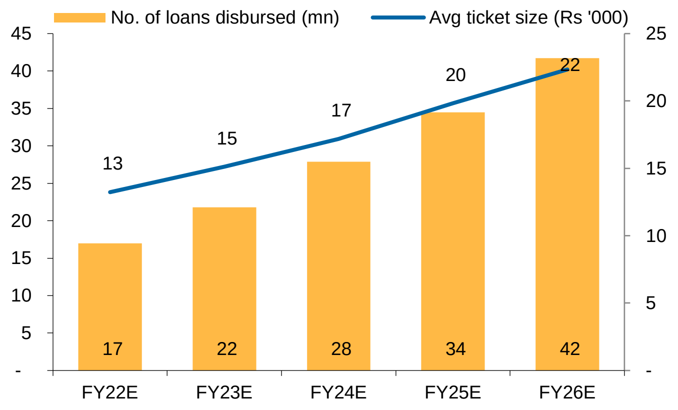
Source: Redseer, Macquarie Research, November 2021

For the merchant loan distribution business, we have already estimated revenues of c.US $85mn in FY26E, in Fig 43 above. Hence, the combined loan distribution franchise will generate revenues of c.US$ 330mn (Rs 24bn), in our view.

What do our estimates build for the distribution business?

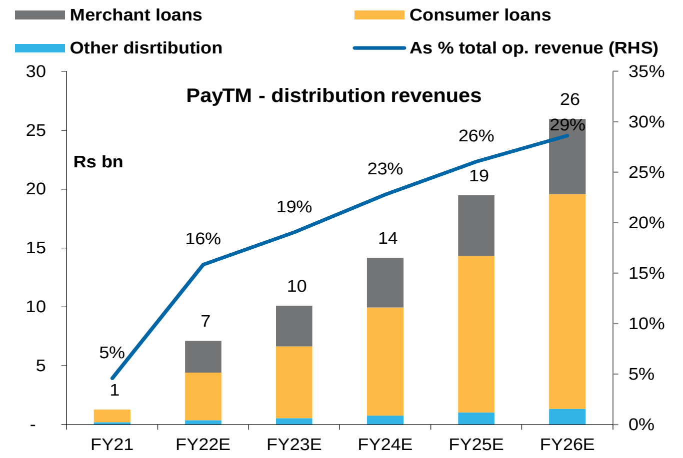
- Our forecasts are largely centred around loan product distribution, which should be the key driver of revenue. Insurance and wealth/MF distribution are still sub-scale businesses and will not move the needle on our revenue forecasts
- PayTM sold down 4.3mn loans in 1HFY22. We expect PayTM to source 17mn loans in FY22 and thereafter scale up this business at 25% volume CAGR.
- Avg ticket sizes (blended for consumer and merchant loans) is expected at c. Rs 13k – gradually scaling up to Rs 22k by FY26.
- We assume a take rate of 3% for PayTM in loans distributed which will come down over the years a bit driven by competition
- By our estimates, PayTM can generate distribution revenue of Rs 26bn by FY26 (Rs 1.3bn in FY21).
- This segment should aid PayTM's margins incrementally in our view, as it largely involves cross-sell. However, as discussed earlier, we remain doubtful of the scalability of this model in which PayTM acts as a pure distributor

Fig 48 We expect PayTM to source 40mn+ loans per annum by FY26



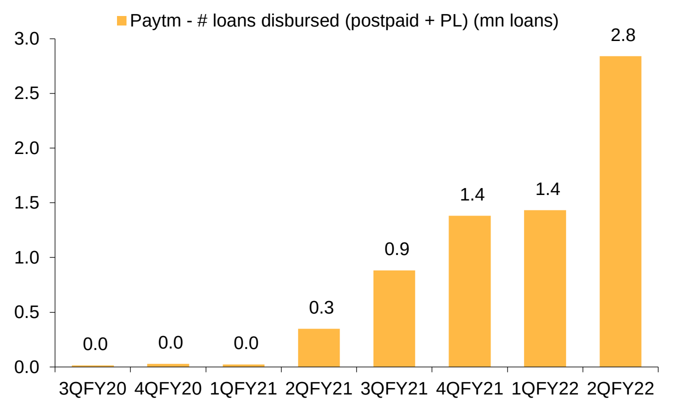
Source: Company, Macquarie Research, November 2021

Fig 49 This will help it generate overall distribution revenues of c.Rs 26bn by FY26



Source: Company, Macquarie Research, November 2021

Fig 50 PayTM started scaling up its BNPL and personal loan distribution business only in 2HFY21



Source: Company, Macquarie Research, November 2021

Fig 51 PayTM Postpaid lags other BNPL players in no. of loans disbursed – though they have a head start

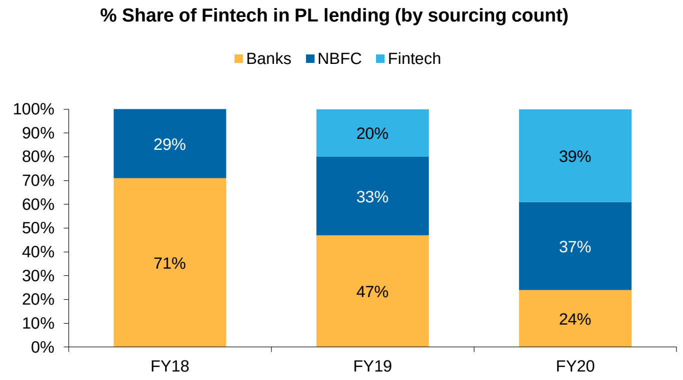
Total consumer txns processed since inception	Period	mn transactions
BAF	**FY16-FY21**	**56**
Simpl	2015-present	49
Flipkart Pay later	2017-Jul'21	42
Amazon Pay Later	Apr'20-Jun'21	10
LazyPay	2017-present	10
BAF (e-comm only)	**FY16-FY21**	**7**
Paytm Postpaid	Dec'20 - Sep'21	6
Mobikwik BNPL	May'19-Mar'21	5

Source: Company, Macquarie Research, November 2021

Fintech consumer lending experience has been poor in India

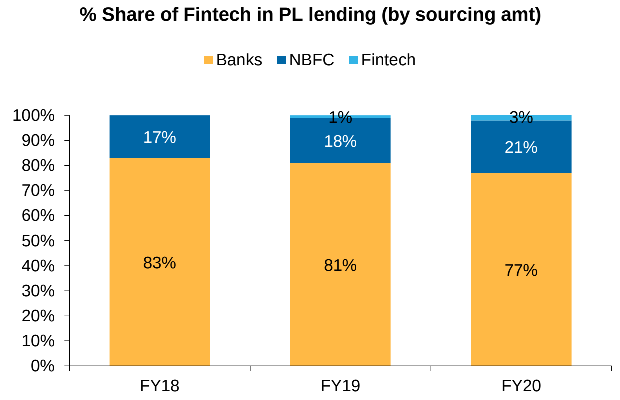
The asset quality experience of loans originated by new-age fintechs has been poor, as can be seen from the figures below. While fintechs accounted for ~40% of loans originated by volume in FY20, in value terms this only amounts to ~3%. Lending ticket sizes for fintech personal loans at Rs 9k is much lower than that of banks (~Rs 388k), as shown in Fig 54. Fintechs have a much higher exposure to millennial and new-to-credit customers.

Fig 52 Fintechs have made big impact on personal loan sourcing vols



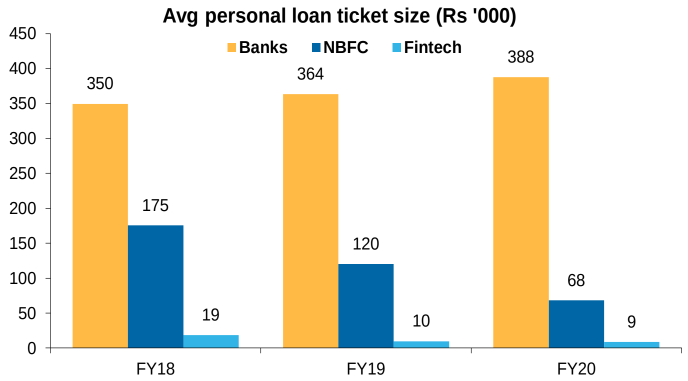
Source: Experian credit bureau, Macquarie Research, November 2021

Fig 53 …but are still fringe players in value terms in personal loans



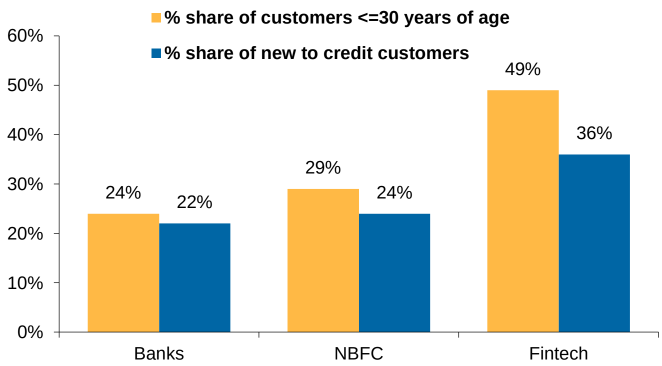
Source: Experian credit bureau, Macquarie Research, November 2021

Fig 54 PL lending ticket sizes of fintechs much lower than banks/NBFCs



Source: Experian credit bureau, Macquarie Research, November 2021

Fig 55 Fintechs have higher share of millennial/NTC customers



Source: Experian credit bureau, Macquarie Research, November 2021

While lower ticket lending ticket sizes as done by fintechs place them at a natural disadvantage in terms of unit economics, this is further exacerbated by the poor credit quality experience suffered by a majority of fintechs. This is summarised in the Fig 56 below. The charts above and the table below show that the quality of credit generated by fintechs is largely sub-prime in nature and we remain sceptical of the scalability of these businesses and customer franchises as 'pure-distribution' businesses.

Fig 56 Credit cost experience for Indian BNPLs/digital lenders has been poor

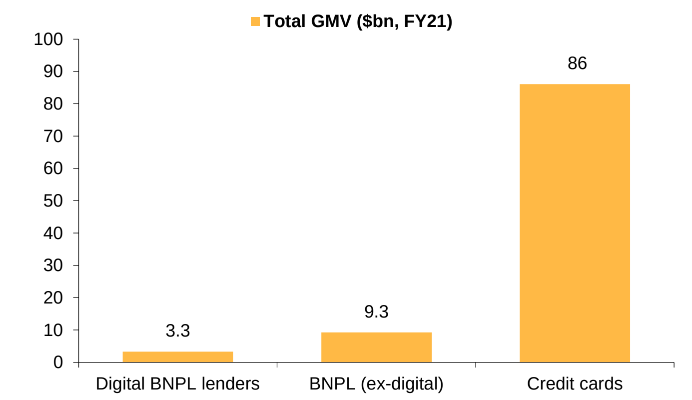
Fintech	Business line	Asset quality
PayU finance	BNPL (Lazypay) and personal loans	FY21 GNPLs at **19%**. FY21 credit cost at **11%**
Mobikwik	BNPL	FY21 Credit cost at **20% of GMV**
KrazyBee	BNPL	9MFY21 credit cost at **10%**. As of Feb 21, restructured portfolio is at **19%**
CapitalFloat	BNPL (Amazon PayLater) + SME financing	1HFY21 credit cost at **11%**
Simpl	BNPL	FY20 credit cost at **150%** of revenues
LendingKart	Unsecured SME loans	FY21 credit cost at **7%**. Restructuring at **20%**

Source: Company data, Credit rating agencies, Macquarie Research, November 2021

Further, BNPL is a business with questionable economics in India

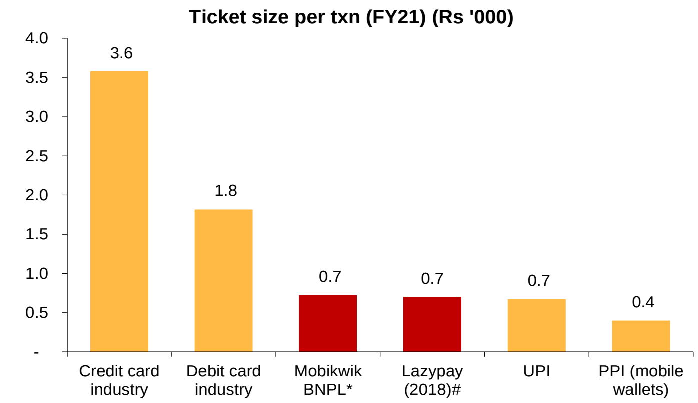
BNPL is a nascent market in India (US$3-3.5bn) that could grow 15x over next 5 years to $45-50bn, as per Redseer. Currently however, digital BNPL GMV is small at <4% of overall credit card spends in India (FY21). BNPLs/ fintechs still operate in fringe customer segments (low-ticket lending to new-to-credit customers). Importantly, BNPL players still operate via co-lending models using the balance sheet of larger banks/ NBFCs.

Fig 57 BNPL spends are still <4% of credit card spends (FY21



Source: Mobikwik DRHP, RBI, Macquarie Research, November 2021

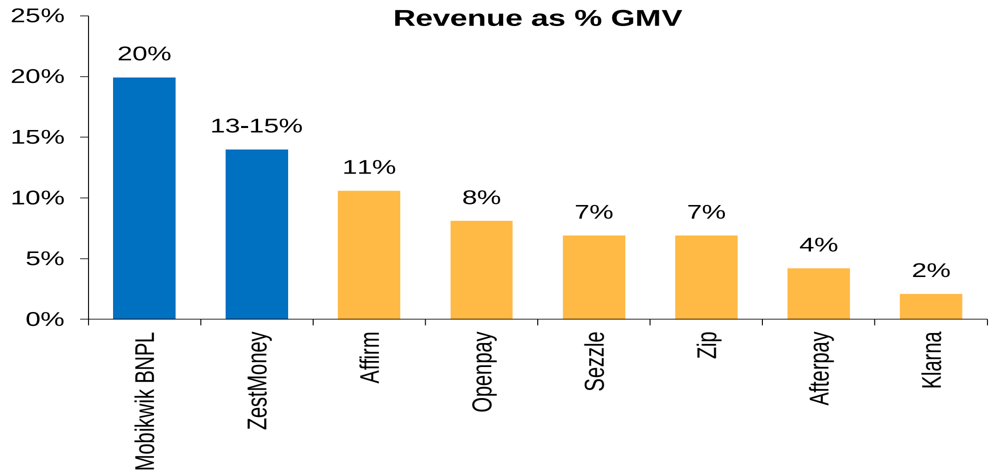
Fig 58 BNPL ticket sizes are generally lower than credit card spends



Source: Mobikwik DRHP, RBI, Macquarie Research; *BNPL spend / no. of transactions, # from media report

Further, BNPLs in India tend to operate very much like personal loan providers (i.e., lenders) instead of payments/ convenience-based form factors. For BNPLs in India, revenue at 15-20% of GMV for BNPLs in India is much higher than global BNPL peers.

Fig 59 Indian BNPLs have higher topline as % GMV vs global peers due to higher share of interest income + late fees



Source: Company data, Macquarie Research, November 2021

Fig 60 BNPL players' interest rates/ late fee charges are steep – this could perhaps indicate that late fees and interest are significant drivers of revenue

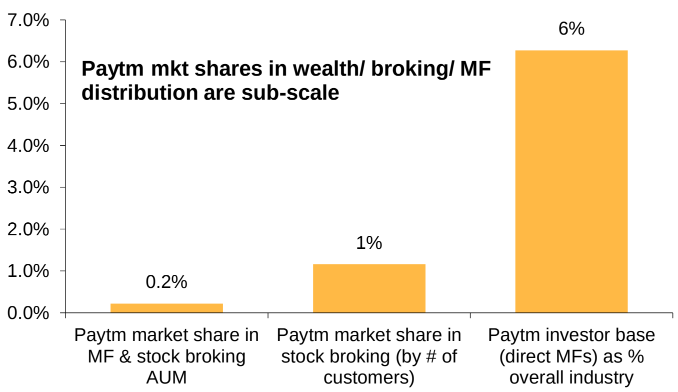
Company	Interest rate: Pay by EMI / POS financing	Interest rate: Revolving credit/ personal loan	Late fees
ZestMoney	0%	32%	Rs 250+ 1% per day on late repayments
Simpl	0%	NA	Rs 250 per cycle default
Epaylater	NA	36%	Rs 100 per cycle default
KrazyBee (E-voucher loans)	0-24%	0-30%	Rs 500+ 0.2% penalty charge per day
Paytm Postpaid	NA	43%	Rs 10-500 per cycle default
AmazonPay Later	24%	NA	Rs 100-500 per cycle default
Mobikwik Zip			Rs 20-200 per cycle default. Plus 1% late fee after 3rd cycle
Flipkart PayLater			Rs 60-600 per cycle default
LazyPay (PayU Finance)	15-32%	20%	Rs 50-500 per cycle default

Source: Company data, Macquarie Research, November 2021

Other distribution segments (ex-loan distribution) are still sub-scale for PayTM

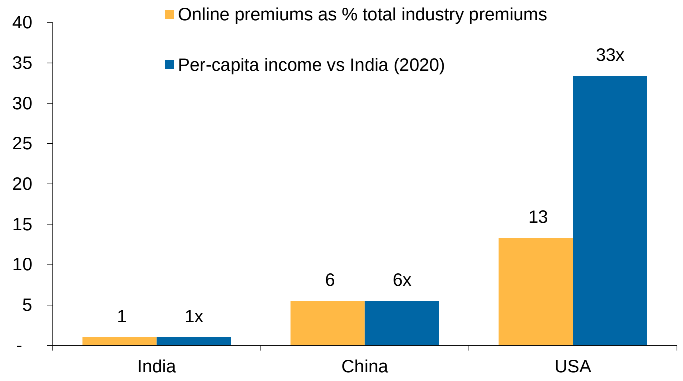
- **Insurance & attachment products:** For PayTM, this segment primarily comprises a) small ticket movie and travel ticket cancellation protections on its platform, as well as b) more traditional insurance products (auto, health, life etc) through its subsidiary (PayTM Insurance Broking Ltd), which started in 2020. In India, the online insurance market is only 1% of total premium sold (FY20) as per Frost & Sullivan, as compared to 13% in USA and 5.5% in China in 2020. Moreover, PolicyBazaar is already the market leader in online insurance distribution in India with ~50% market share of online insurance market, while the remaining 50% is dominated by banks' own distribution, in our view. PayTM has no market leadership in this space, and we expect this segment to remain sub-scale
- **Wealth (incl. mutual funds, equity trading & gold):** While this is an exciting segment from an overall industry perspective, PayTM has not been able to create much of an impact in these segments. PayTM has been active in this business since 2019, when it formed PayTM Money. This is largely a sub-scale distribution business with only $0.9bn AUM for PayTM. Moreover, PayTM Money acts a platform for non-distributor Mutual fund plans and so does not earn commissions. On the broking front, PayTM Money is only a fringe player with <1% market share

Fig 61 Wealth, broking & MF distribution – PayTM has subscale market share across these businesses



Source: Company, Macquarie Research, November 2021

Fig 62 Insurance distribution – We believe online insurance distribution is a saturated market in India. It is in-line with per-capita income



Source: Redseer, Macquarie Research, November 2021

PayTM Mall was a failed experiment and super-app approach may go the same way.

PayTM cannot 'close the loop' with payments

Cloud & Commerce – Platform strength will be tested

PayTM offers a host of platform services through its app, which include travel ticketing, movie ticketing, PayTM First Subscription as well as mini-app services provided to gaming, including PayTM First Games, and commerce merchants (including PayTM E-commerce Pvt Limited). While PayTM has tasted some success in ticketing, we remain sceptical of the scalability of a super-app/ app aggregator approach in India. This segment will be a test of platform strength for PayTM, and as highlighted earlier we are unsure how a payments platform can 'close the loop' for offerings on its platforms.

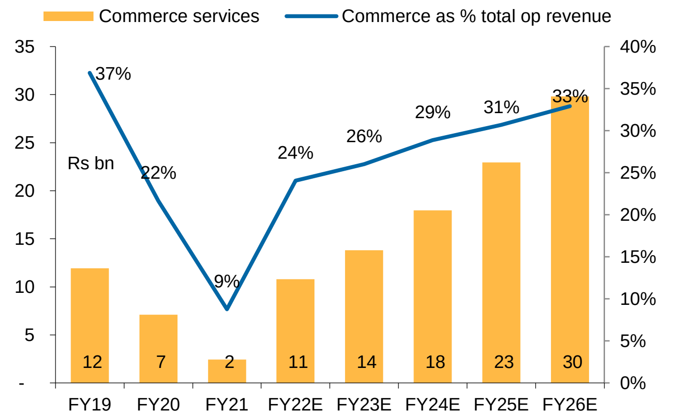
Fig 63 Cloud & commerce – Several disparate revenue streams but the platform value proposition is weak, in our view

Offerings on the PayTM App	Scale achieved	Services Offered by	Revenue Model
Travel ticketing	- 2k bus operators for travel	OCL through its own merchant network	**Consumer:** Convenience fees in certain select cases **Merchant:** Payments processing fee, marketing fee and advertising fee (including for Mini-apps) and other fees
Entertainment ticketing	- second-largest movie booking platform (by vol of tickets) in FY20 - 5.7k screen partners for movies	- OCL through its own merchant network - Wasteland Entertainment Pvt Ltd (PayTM Insider), 100% subsidiary of OCL	
Mini-apps Store	- 480 mini apps on platform - 5.7mn active monthly users	- Developer partners (on-boarded by OCL) - PayTM E-commerce Pvt Ltd mini-app for online shopping (OCL has no stake in PEPL)	
Games	23mn users	- PayTM First Games Pvt Ltd (step-down sub) - These revenues not consolidated in OCL	**Consumer**: Platform fee **Merchant:** Hosting commission
PayTM First Subscription	NA	OCL, in collaboration with partners	**Consumer:** Recurring subscription **Merchant**: Distribution fee (select)

Source: Company data, Macquarie Research, November 2021; OCL = One 97 Communications Limited (PayTM parent company)

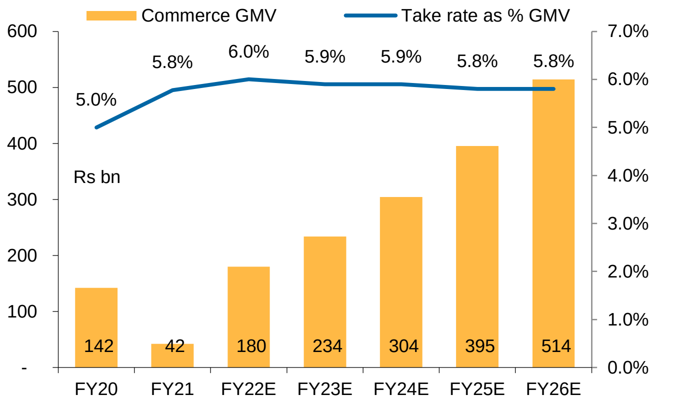
Since payments are difficult to monetise, it is difficult to provide strong incentives to consumers to transact on the platform in an economically viable way. At the same time, merchants also do not have significant incentive to transact on a platform with low value proposition to end-consumers and low customer stickiness. However, in our estimates, we still do factor in an optimistic pick-up in commerce revenues to Rs34bn by FY26.

Fig 64 However, we still model an optimistic pick-up in commerce revenues



Source: Company data, Macquarie Research, November 2021

Fig 65 We expect GMV to bounce back above pre-covid levels in FY22E, and thereafter grow at 30% CAGR



Source: Company data, Macquarie Research, November 2021

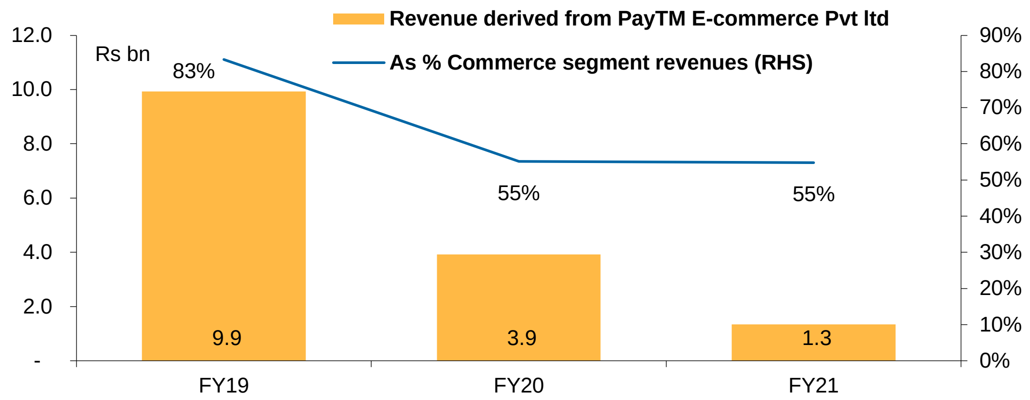
Large contribution from PayTM Mall, whose revenues have declined sharply

PayTM's weak platform strength becomes evident from the chart below. 55% of its revenues in the Commerce segment are derived from PayTM E-commerce Pvt Ltd (PayTM Mall). This is an entity that is owned separately by the promoters of PayTM, while the parent company itself (One97 Communications) has no direct ownership.

From the chart below, it is clear that the sharp fall in PayTM's commerce segment revenues over FY19-21 is directly attributable to the sharp decline in PayTM Mall's revenues. E-commerce is a segment where PayTM has had to compete head-on with deep pocket players (Amazon and Walmart-owned Flipkart). These players also have strong two-way customer-merchant ecosystems with strong consumer value propositions.

PayTM's foray into e-commerce has been a damp squib and we believe the super-app foray could go the same way.

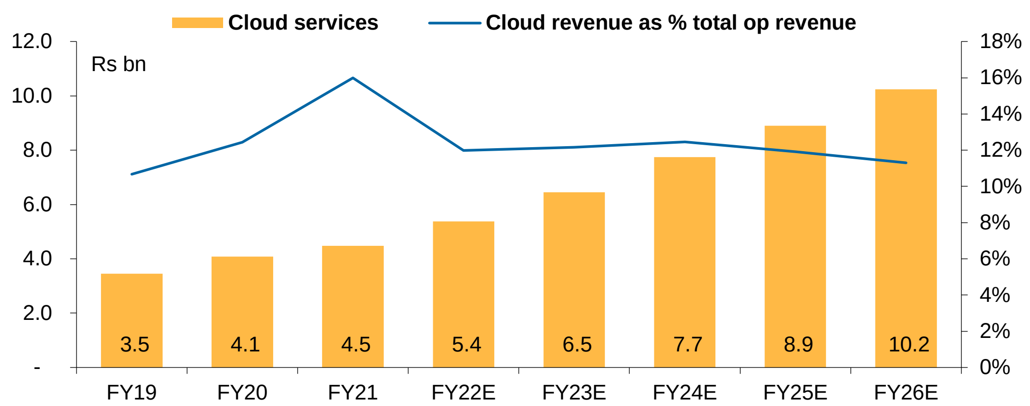
Fig 66 ~55% of PayTM's commerce segment revenues are derived from PayTM Mall (promoter-owned entity). This business' revenues have collapsed over past two years



Source: Company data, Macquarie Research, November 2021

PayTM also generates revenues from cloud services which includes revenue from advertising, and cloud solutions for SMEs and enterprise solutions. Cloud service fees are also charged for PayTM's Mini-app platform for developers. We expect cloud services to grow at 18% CAGR over FY21-26, as shown in Fig 67 below.

Fig 67 We expect cloud services to grow at 18% CAGR over FY21-26



Source: Company data, Macquarie Research, November 2021

PayTM competes with deep-pocketed players with stronger platform value propositions

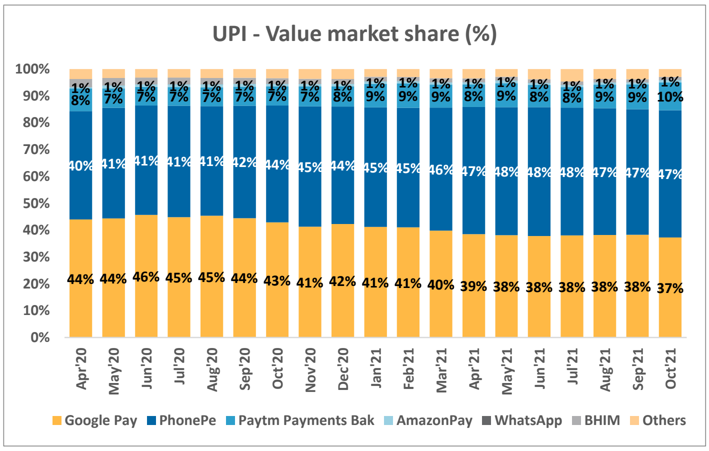
Competition to exert pressure on unit economics

PhonePe, Google Pay, Amazon are formidable competitors

PayTM trails behind GooglePay and PhonePe in overall UPI payments. These two players together account for 84% of UPI payments by value and 80% in volume terms. These platforms also have formidable 100mn+ active consumer franchises. PayTM is a distant third in overall UPI transactions, with 10% market share in value terms (Oct'21). It is also interesting to note that average UPI ticket sizes for PayTM are ~40% lower than those for GooglePay/PhonePe.

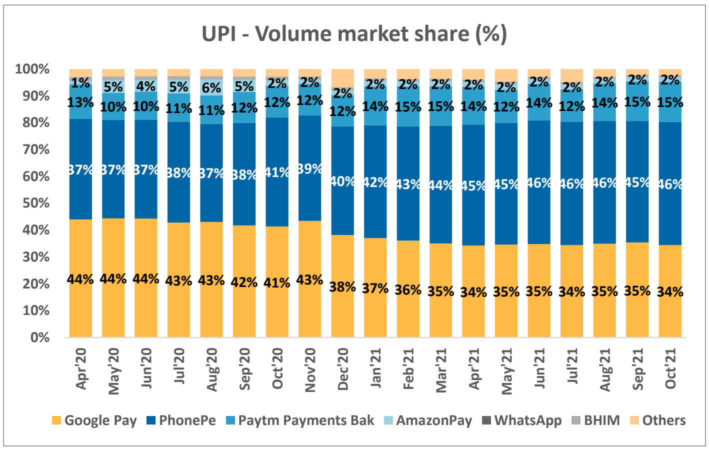
However, as per NPCI guidelines, GooglePay and Phonepe will have to bring down their market share to < 30% each by Jan'23. This could be an opportunity for other payment players, including PayTM.

Fig 68 Google Pay and PhonePe account for 84% of UPI transactions by value…



Source: RBI, Macquarie Research, November 2021

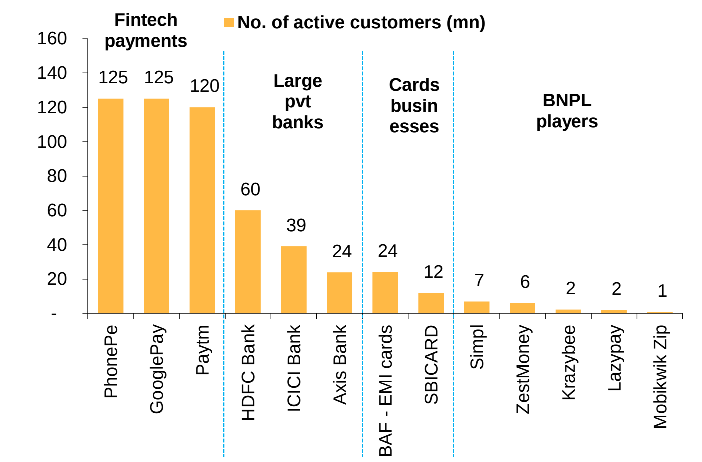
Fig 69 …and 80% by volume



Source: RBI, Macquarie Research, November 2021

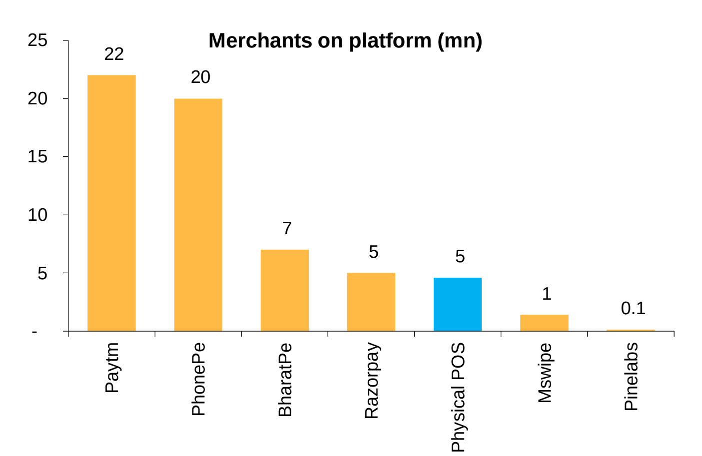
We believe PayTM will continue to face stiff competition from such deep-pocketed platform players as Google (GooglePay platform), Amazon (Amazon Pay platform), and PhonePe (owned by Walmart-owned Flipkart) etc. In fact, global tech giants like Amazon have consciously tweaked their offering for the Indian diaspora – for example, nowhere else in the world does Amazon sell insurance, train, flight and movie tickets.

Fig 70 GPay, PhonePe also have 100m+ customer franchises



Source: Company data, Macquarie Research, November 2021

Fig 71 PhonePe has onboarded merchants at scale, like PayTM. BharatPe also plans to double merchant network



Source: Company, Macquarie Research, November 2021

Furthermore, a number of large Indian conglomerates/other platform players have also forayed into super-apps to monetise their customer bases – these include the Tata Group, ITC, Reliance Jio and now Bajaj Finance. Clearly, the competition in this space is only headed north.

The point here is that PayTM's app is not unique in any way and competitors are offering similar products and accessibility to customers in terms of payments for various products. For a large player like Amazon, the main focus of its financial services offering is to increase the AOV (average order value) of its e-commerce business; hence we believe Amazon will use the financial services offering as an enabler to increase its AOV. Eventually the large players like Google, Facebook (partnered with lender for SME financing), Flipkart, and Amazon etc will drive down unit economics and take rates of distribution business.

Fig 72 Increasing competition - Several players are looking to monetise their large merchant platforms by distributing loans

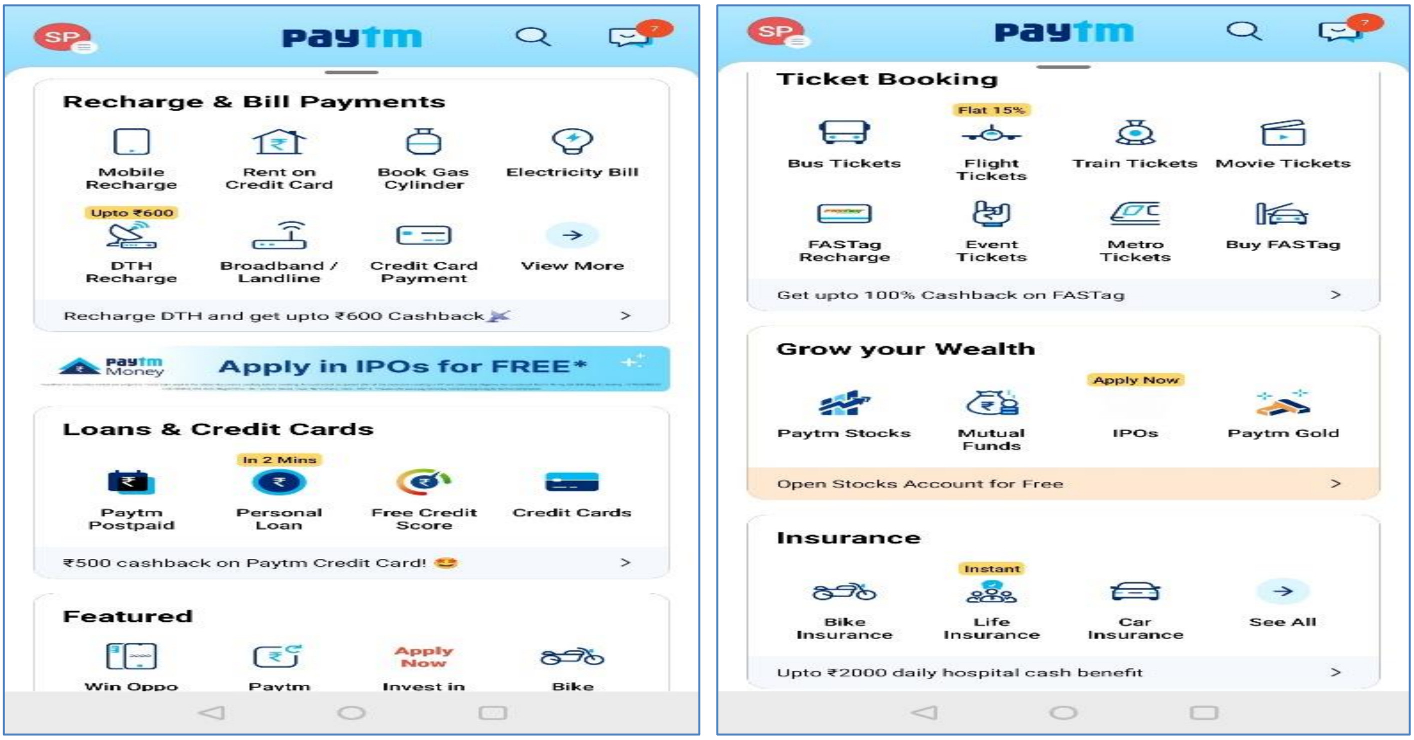
Platform	Merchants on platform	Lending partner	Lending business model
Facebook	~15 mn	Indifi	Loans to businesses selling on Facebook, Instagram and Whatsapp for Business.
Khatabook	10 mn		Lending to retailers/distributors using Khatabook's app for book-keeping
BharatPe	7.5 mn	Own SFB with Centrum	Working capital loans to merchants on BharatPe's payments platform. BharatPe wants to scale to 20mn merchants in 2 yrs
Razorpay	5 mn	Partner banks	Working capital loans to SMEs accepting payments on Razorpay's platforms at 1.5% per month
Tally	2 mn	Applied for own SFB license	Lending to SMEs that use Tally's ERP/accounting softwares
Flipkart Wholesale	1.5 mn	IDFC First Bank	Loans to help kiranas manage their working capital requirements and grow their business.
Udaan	200 k		Short term credit (15-21 days) to help SMEs procure on Udaan's B2B wholesale purchasing platform
Zomato	148 k	Incred	Working Capital loans to restaurants on Zomato's food delivery platform
Ofbusiness	5 k	40 lending partners	Unsecured credit upto Rs 20mn to help SMEs procure raw material on OfBusiness' platform

Source: Company press releases, various media sources, Macquarie Research, November 2021

On the merchant front, several large platforms in India are looking to monetise their sizable merchant bases by distributing financial services to them. Here too, PayTM faces competition from deep-pocketed global/VC-backed players. We believe increasing competition should have negative implications for PayTM's distribution take rates going forward.

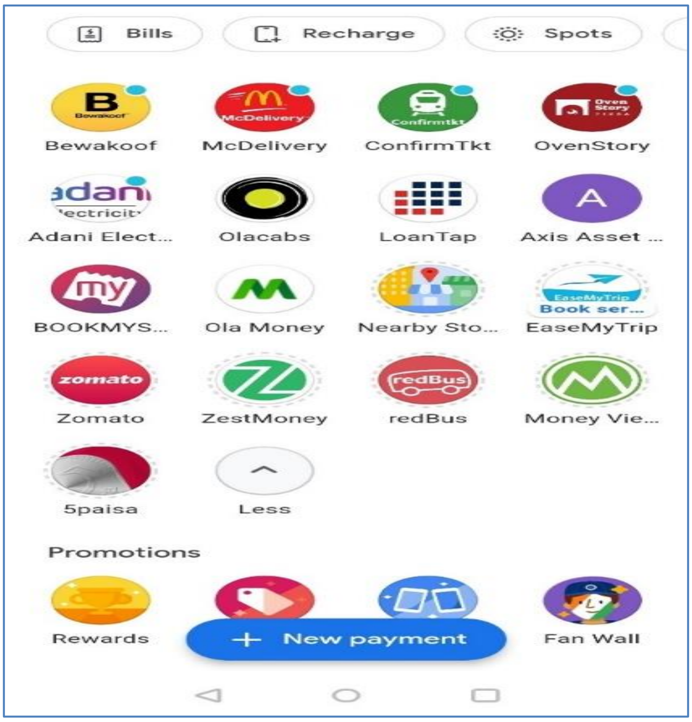
The winners here, in our view, will be decided by the strength of these platform offerings. This is a function of the two-sided consumer merchant network effects that these platforms can generate. Merchant-lending need not be a winner-take-all space, and will be a highly fragmented market going forward, in our view.

Fig 73 PayTM – Will the super-app approach work in the face of an increasing competitive environment?



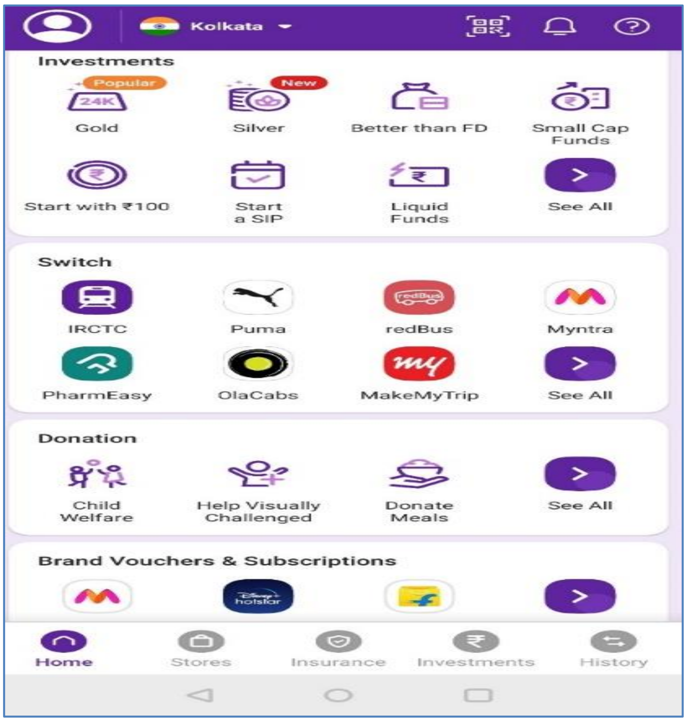
Source: PayTM app, Macquarie Research, November 2021

Fig 74 GooglePay with 100mn+ active customers has also forayed into a super-app / one-stop shop format



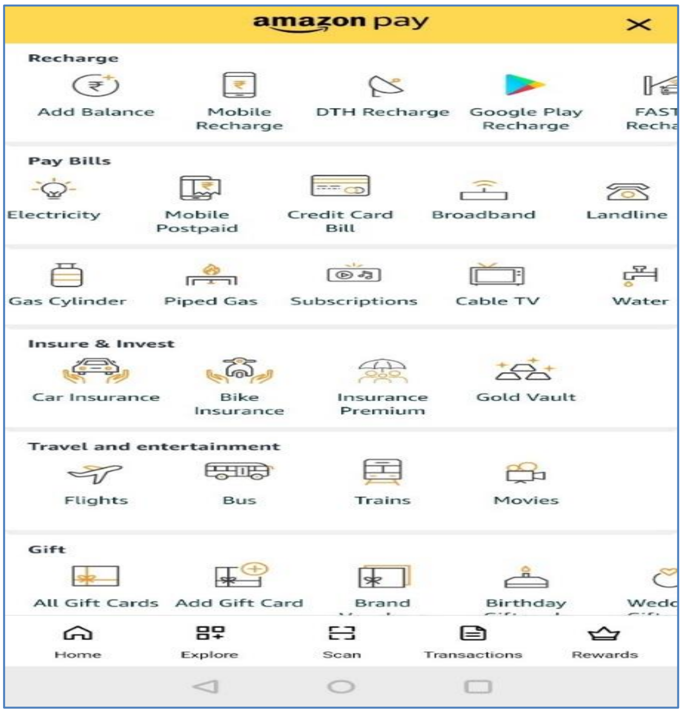
Source: Google Pay app, November 2021

Fig 75 Phonepe with 125mn active customers is also going down the same path



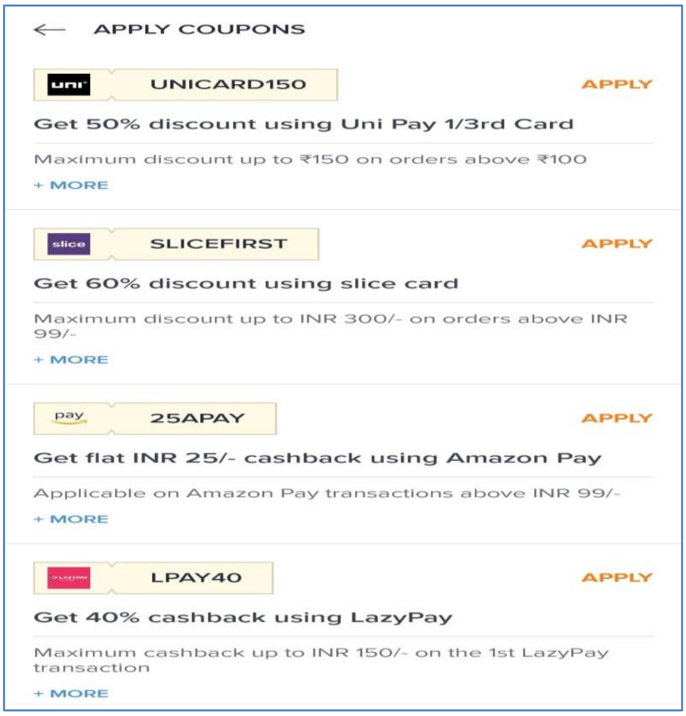
Source: PhonePe app, November 2021

Fig 76 AmazonPay has also has a super-app approach in India. Globally, nowhere else does Amazon sell train, flight or movie tickets.



Source: AmazonPay appNovember 2021

Fig 77 Even BNPLs have become a highly crowded space with players providing cashbacks/ incentives even for spends <$5!



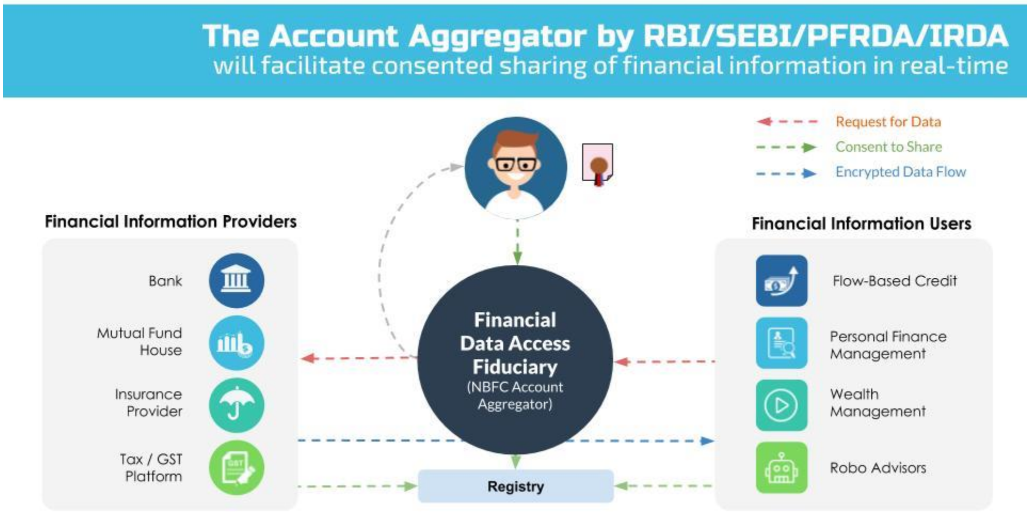
Source: Swiggy app, November 2021

Further, as can be seen in the screenshots in the adjacent figures, the super-app offerings on PayTM, Amazon, GooglePay, PhonePe etc look very similar at first sight. We believe platforms with strong two-way, closed-loop, consumer-merchant network effects will be the winners in this highly heated space. PayTM lags peers in this regard, as we believe it is difficult to close the loop with payments in India; furthermore, the platform incentives for consumers/merchants on PayTM are poor. In any case, we remain of the view that distribution/disintermediation costs are only going to go down in India across product lines. This is a key risk to the scalability of PayTM's business model.

Fintech infra rails like Account Aggregators and OCEN will further democratise access to data across system

New innovations in NPCI's India Stack ecosystem, including account aggregators and open credit enablement network (OCEN) will only democratise access to financial data across the system and further reduce transactional costs. Account aggregators (AAs) are specialised NBFCs that facilitate the flow of information between financial companies. In effect, the AA ecosystem will work like a credit bureau for the asset side of a customer's finances. We believe that with increasing penetration of AA/OCEN, transaction costs for the banking system will come down and visibility of data across the system will only improve. Further proliferation of such services pose a serious risk to PayTM's distribution-led business model. The point here is there will eventually be no edge in having volume of data and using that as your core competency. All these open architecture frameworks will result in democratisation of data, and eventually frictional costs will come down.

Fig 78 Account aggregators enable transfer of financial information (with customer consent) between financial companies



Source: Sahamati, November 2021

Complex organisation structure

Related party transaction risks

High senior mgmt. attrition

"Below Median" MGRS rating

Governance & Risk

Board structure: 6/8 members overseas

Small board with substantial proportion of members based out of India

A board that consists of only eight members with six of them being based out of India is not necessarily an ideal desirable board structure in our view. Our MGRS (Macquarie Governance Risk Score) gives larger weightage to 8/11-member board team in our proprietary scoring model. Plus, for a company which is banking on the opportunities that exist in India, we would appreciate a board which is fairly represented with experts within India and especially people who come from a domestic financial services background, which we believe is lacking here.

Fig 79 PayTM's board has just 2 out 8 members based out of India

No	Board of Directors	Designation	Based out of	Additional Comments
1	Vijay Shekhar Sharma	Chairman, MD & CEO	India	Founder
2	Douglas Feagin	Non-Exec Director	USA	Ant Fin Nominee
3	Munish Varma	Non-Exec Director	UK	SVF Nominee
4	Ravi Chandra Adusumalli	Non-Exec Director	USA	SAIF and Elevation Capital Nominee
5	Mark Schwartz	Independent Director	USA	Goldman Sachs
6	Pallavi Shardul Shroff	Independent Director	India	Lawyer, Shardul Amarchand Mangaldas & Co
7	Ashit Lilani	Independent Director	USA	Saama Capital
8	Neeraj Arora	Independent Director	USA	Ex Google and Whatsapp

Source: Company data, Macquarie Research, November 2021

No split between the Chairman and MD/CEO

The founder Vijay Shekhar Sharma is the chairman as well as MD and CEO of the Company. Macquarie's MGRS system ideally prefers a split between the Chairman and MD/CEO posts as that will bring in more objectivity to the board.

Scope for better disclosures

PayTM's RHP (Red Herring Prospectus) filed on October 26, 2021, doesn't mention Ajay Shekhar Sharma, brother of Vijay Shekhar Sharma as a key management personnel but does list him as a relative who owns interest in the voting power of the group that gives them control or significant influence. He was appointed as the Chief Business Officer in August 2021, as per his linkedin profile as well as media reports.

Inter-party transactions; some under regulatory scrutiny

The problem with a complex multi-layer organisation with several subsidiaries and step-down subsidiaries is that there could be a web of inter-party transactions and that indeed is the case with PayTM.

In FY21, One97 Communication's (PayTM's) 100% subsidiary, PayTM Entertainment Limited, entered into a transaction of providing a one-time short-term loan to PayTM First Games where PayTM entertainment holds 55%. Due to this, PayTM Entertainment met the principal business test for determination of identification as a non-banking financial company. While the said loan has been repaid by PayTM First Games to PayTM Entertainment and further, PayTM Entertainment has no loans outstanding to any entity, this particular transaction is under RBI scrutiny. One97 communications had given loans worth Rs809mn to PayTM First Games.

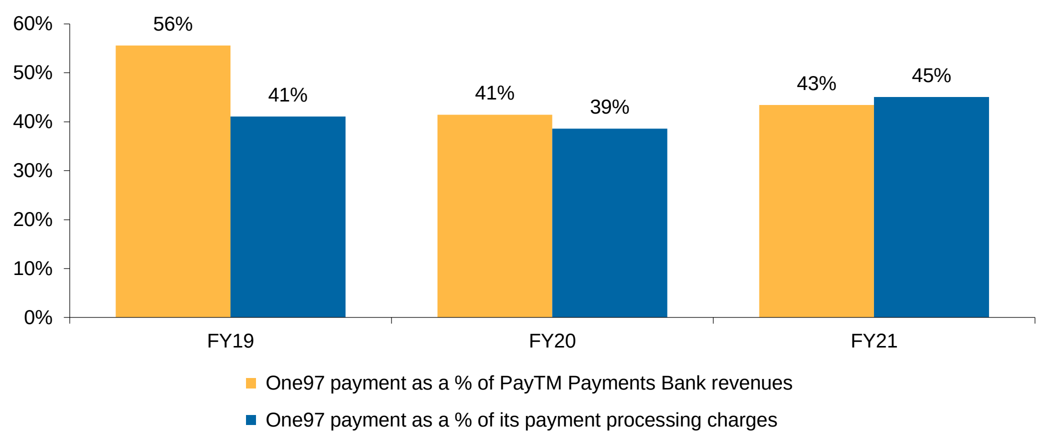
Another prominent example of inter-party transaction is that One97 communication pays almost 40-45% of the revenues that PayTM Payments Bank earns, where Vijay Shekhar Sharma (MD/ CEO of One97 Communications) owns a 51% stake.

Fig 80 Payment bank revenues vs. One97 (PayTM) payments for rendering the services

INR Mn	FY19	FY20	FY21
PayTM Payments Bank Sales	16,681	21,106	19,874
One97 (PayTM) for rendering of services	9,277	8,752	8,634

Source: Company data, Macquarie Research, November 2021

Fig 81 Close to 40-45% of Payments Bank revenues where Vijay Shekar Sharma owns 51% comes from One97 Communications (PayTM parent entity which is getting listed)



Source: Company data, Macquarie Research, November 2021

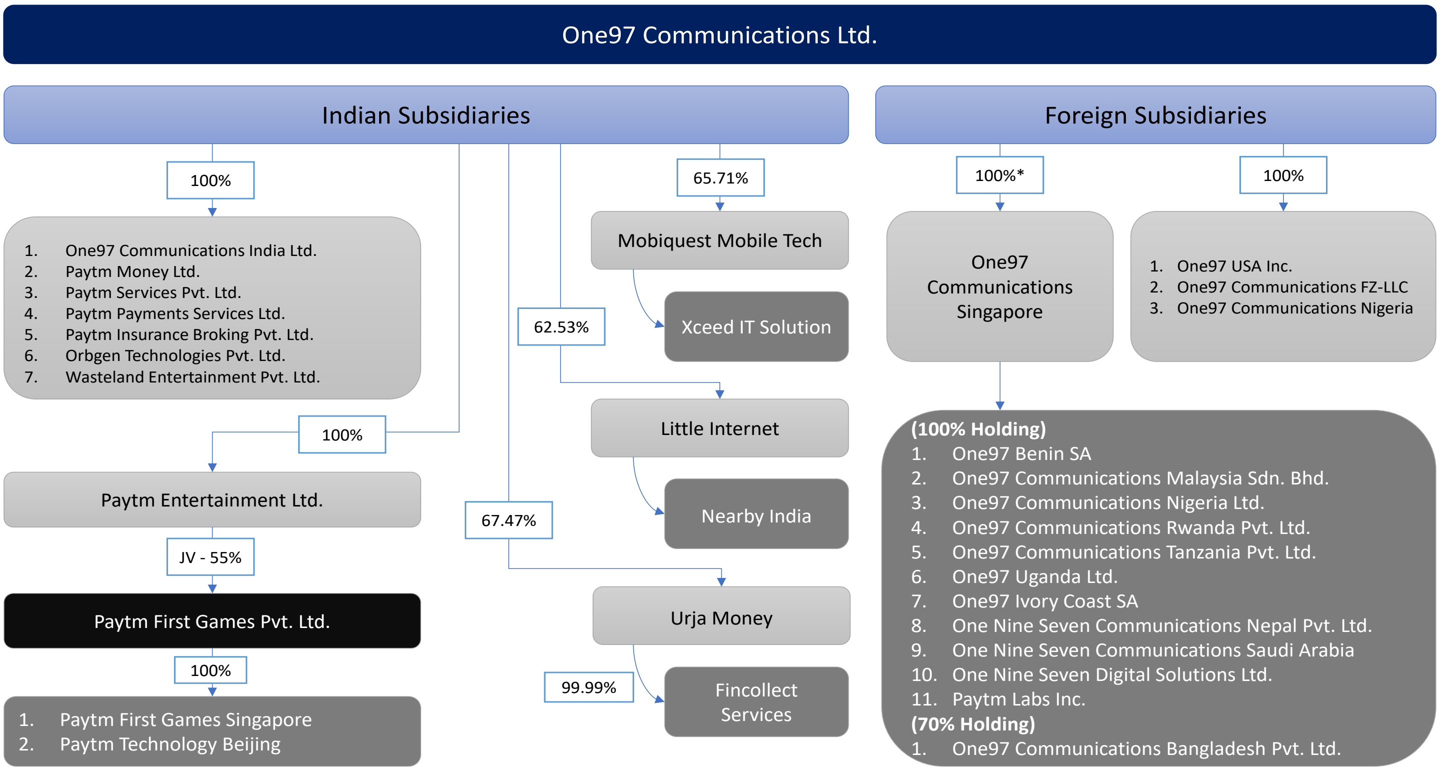
Senior management attrition – another red flag

A start-up firm is bound to have some flux in management. Most often the middle and lower management exits happen at a rapid pace. What is intriguing is that five senior executives of Vijay Shekhar Sharma-led PayTM quit ahead of its DRHP filing in July 2021. Amit Nayyar, PayTM president; Rohit Thakur, chief HR officer, and three other vice-presidents resigned from their posts in July 2021. Nayyar, who is a former Goldman Sachs executive, had joined the PayTM board in 2019. He was instrumental in building PayTM's financial subsidiary and insurance and lending verticals. Hence such flux worries us with respect to stability of the organisation.

Complex organisation structure

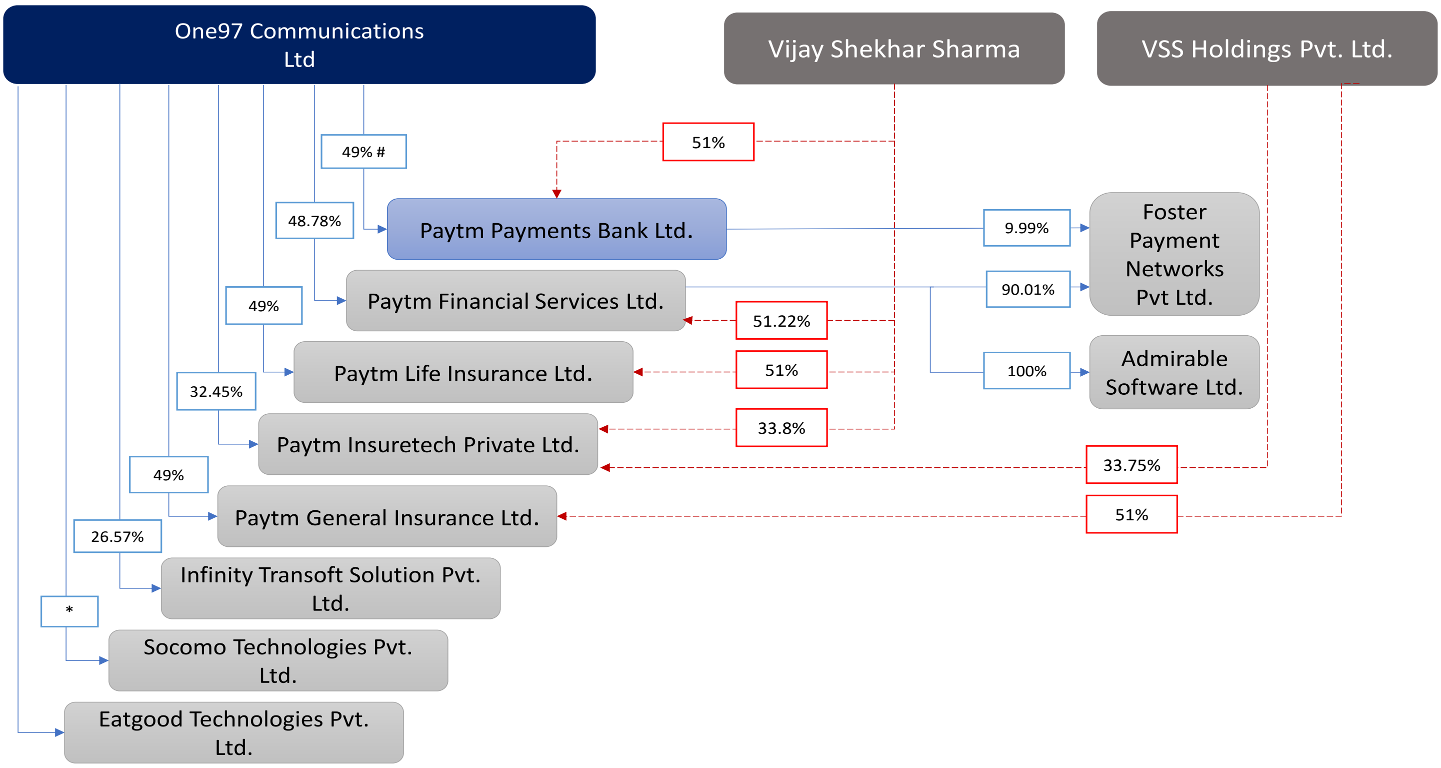
As shown below One97 communications organisation structure is quite complex with multiple subsidiaries. One 97 has close to 15 domestic subsidiaries and 17 international subsidiaries. Such multi-layer architecture can be a conduit for doing inter-party transactions, as explained in the previous section.

Fig 82 PayTM – Organisation structure



Source: Company data, Macquarie Research, November 2021

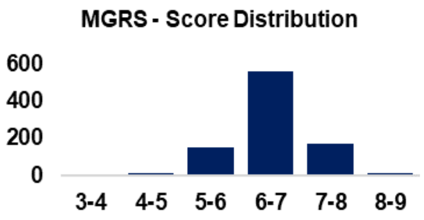
Fig 83 PayTM – Organisation structure: Key associate companies



Source: Company data, Macquarie Research, November 2021

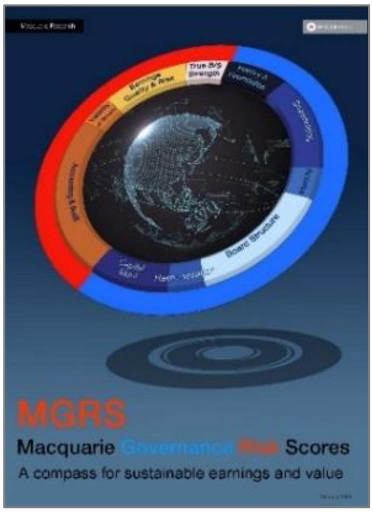
“Below Median” in our MGRS scoring

Finally, Macquarie’s proprietary MGRS scoring model places PayTM in” Below Median” level. This is because there are several important inputs (which the MGRS model uses) where PayTM doesn’t score well. For example, important red flags or inputs that have negative repercussions on the overall score are split between the chair and CEO, independence of the chair, senior management attrition, having a profitability and ROE target, interparty transactions, tenure of board members, CFO being on the board etc where PayTM doesn’t score well thereby pulling down the overall scores.



Source: Macquarie Research, November 2021

In 2015, we launched the Macquarie Governance and Risk Score (MGRS) to assess corporate governance ('CG') and inherent risk ('Risk') to published accounts. This series of reports marks an expansion of MGRS to our entire Asian coverage as well as an update of our proprietary set of questions. In MGRS, each covering analyst uses their on-the-ground knowledge to answer 120-130 questions (c.65% objective) spread across six CG and four risk categories, the results of which generate a score. In these sheets, the analysts highlight key points within assessments and identify areas in which form might not match substance. Click the link below for the detailed methodology.



ESG Research

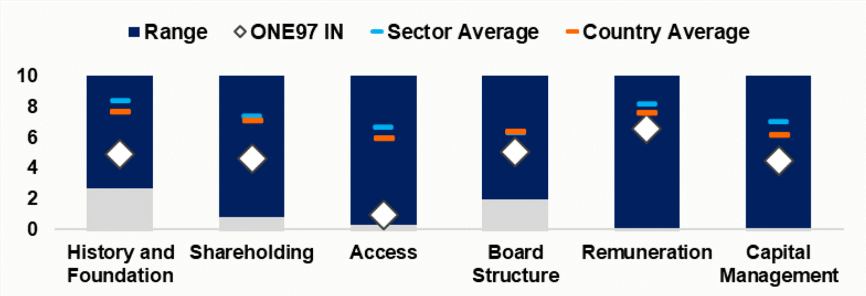
Macquarie Governance and Risk Score

Summary

One97 communications (PayTM) is India's largest Fintech company with 300mn plus customers and 20mn plus merchants. The company predominantly started as a payments (digital wallet) company and has now diversified into other streams like distribution of financial services, ecommerce and cloud.

Corporate Governance

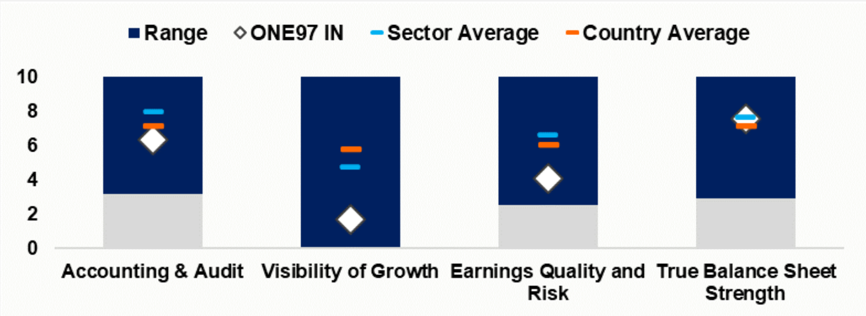
- There is no split of the Chairman and CEO position
- The CEO is a part of risk management committee, which is less desirable
- Frequent senior management attrition has been a cause of concern
- Inter-party transactions are another source of concern
- The group has a complex organisation structure with multiple subsidiaries.



Source: Bloomberg, FactSet, Macquarie Research, November 2021

Risk

- Grant of banking license from RBI could be a stamp of approval from the regulator, but RBI has raised some issues regarding related- party transactions.



Source: Bloomberg, FactSet, Macquarie Research, November 2021

Very unlikely to get bank license due to complex group structure, Chinese ownership

Regulations – Will it get a bank license?

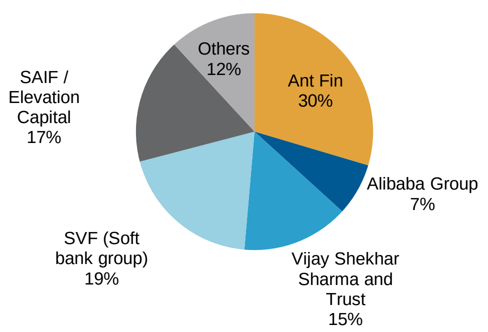
The probability of PayTM getting a bank license is low in our view

PayTM is constrained from lending due to its payments bank license, which does not allow it to assume credit risk in any form. PayTM Payments Bank completes five years of commercial operations in May 2022 and would then become eligible to apply for a small finance bank license, which would enable it to lend to its customer base. It would also enable it to freely accept deposits, which are now constrained at a limit of Rs0.2mn per customer, under its payments bank license.

However, in our view, PayTM is not a practical contender for a universal / small finance bank license. The main reason in our view is that Chinese controlled firms, Alibaba and Ant group, together still own close to a 31% stake in One97 Communications (PayTM parent entity) post the IPO. If we consider a pass through to the PayTM payments bank, then the Chinese controlled entities still own around a ~15% stake in the payments bank.

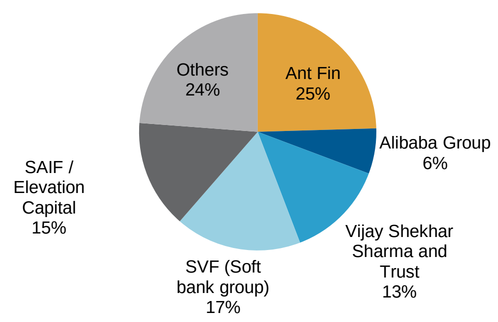
Due to the geopolitical tensions between India and China, the Indian government has been pretty cautious in clearing investment proposals from China. Both RBI and the government, in our view, will be careful in clearing proposals where Chinese firms own a majority stake, especially in more scrutinised sectors like banking. Also, RBI caps investments by any single individual/entity in banks at 5%. A promoter-led entity can be allowed to own 30% (as is the case with Kotak Bank) or 40% as is the case with small finance banks. However, PayTM doesn't have a promoter. There are however exceptions to the rule as in some cases the RBI has allowed individual entities to own larger stakes. But in many of those cases, the regulatory relaxation has been given to bail out beleaguered entities.

Fig 84 Pre-offer shareholding pattern – Ant and Alibaba own 37% stake



Source: Company data, Macquarie Research, November 2021

Fig 85 Post-offer shareholding pattern – Ant and Alibaba would still own 31% stake



Source: Company data, Macquarie Research, November 2021

Add to that, most small finance banks in India are microfinance companies barring few exceptions. Historically, the motive of the RBI has been to drive financial inclusion and help institutions that are helping weaker sections of the society, and hence the RBI gave given small finance bank licenses largely to MFI institutions in the past. If PayTM is going to do BNPL or consumer durable loans, we aren't sure whether it falls in the same bracket as MFIs from an ideology perspective for RBI to grant them a small finance bank license. Having said that, the RBI did issue a small finance bank license to a fintech company, Bharat Pe, recently. However, that in our view was a quid pro quo deal as Bharat Pe agreed to bail out a beleaguered cooperative bank, PMC bank.

Fig 86 List of small finance banks in India – most of them are microfinance companies

No	Bank	Main type of business
1	Ujjivan small finance bank	Microfinance
2	ESAF small finance bank	Microfinance
3	RGVN small finance bank	Microfinance
4	Janalakshmi small finance bank	Microfinance
5	Equitas small finance bank	Microfinance
6	Capital small finance bank	Microfinance
7	Suryoday small finance bank	Microfinance
8	Utkarsh small finance bank	Microfinance
9	Fincare small finance bank	Microfinance
10	AU small finance bank	Vehicle, business, housing loans

Source: RBI, Macquarie Research, November 2021

RBI also in general has stayed away from granting any banking license to any corporate-backed entity. While this has been proposed by an internal working group of the RBI, it remains highly unlikely that this will change in the near future, in our view.

Add to that PayTM's complicated organisation structure, inter-party/related party transactions could be a cause of concern for the regulator in our view. We have discussed some of the corporate governance issues in our earlier report.

Digital banking license unlikely to be issued in India – so that option is also ruled out for PayTM

Some of the markets in the ASEAN region have granted digital banking licenses as shown below. Currently the RBI hasn't given any indication to issue such licenses. The last paper on licensing of banks in India was the paper of IWG (Internal Working Group Committee) in Dec 2020, which talked about considering corporates for banking licenses and converting some of the large NBFCs to banks. It remained silent on the concept of digital banking licenses.

Considering that India already has a lot of open architecture platforms like UPI, Account Aggregators, e-KYC through Aadhar, etc. which can be used by all players in the system, we are unsure as to why a separate digital banking license needs to be issued.

Plus, the recent deal of Google Pay with Equitas to source Fixed Deposits has had issues with the RBI and shows the reservations that the RBI has with Fintechs to be involved in dealing with public deposits even though Google Pay is acting only as a sourcing agent. Therefore, we remain sceptical about Fintechs in general getting banking licenses in any form from the RBI.

So, we remain sceptical about Fintechs in general getting banking license in any form from RBI.

Fig 87 Standalone digital banking licenses have picked up in other geographies

Market	Status	Standalone digital banks	Digital only offerings	Major bank apps
Singapore	Digital bank licences granted, to start operations in 2022	Sea	Standard Chartered[1]	DBS digibank
		Grab-Singtel		UOB Mighty
		Ant		OCBC Digital
		Greenland-Linklogis		
Indonesia	Smaller banks being repurposed as digital banks	Jago	Jenius (Btpn)	BCA Mobile
		BCA Digital	digibank (DBS)	BRI mo
		BRI Agro	TMRW (UOB)	Mandiri Livin'
				CIMB Octo
Philippines	First of 5 digital bank licences issued and operating already	Tonik	ING	BPI Mobile
			CIMB	
			Eon (UnionBank)	
			Diskartech (Rizal Commercial)	
			Komo (East West Bank)	
Thailand	No standalone digital banks likely	-	LINE BK (KBank)	K PLUS
			TMRW (UOB)	SCB Easy
Malaysia	5 Digital bank licences expected earliest end-2021	-	Mae[2]	Maybank2U
				CIMB Clicks
				HLB Connect

1 Based on its status as a 'significantly rooted foreign bank' (SRFB) in Singapore, Standard Chartered has the option of setting up a digital bank under its existing licence and has expressed an intention to do so. In Hong Kong, Standard Chartered has such a venture under the 'Mox' brand

2 Mae operates under a digital wallet licence and is wholly owned by Maybank

Source: Macquarie Research, November

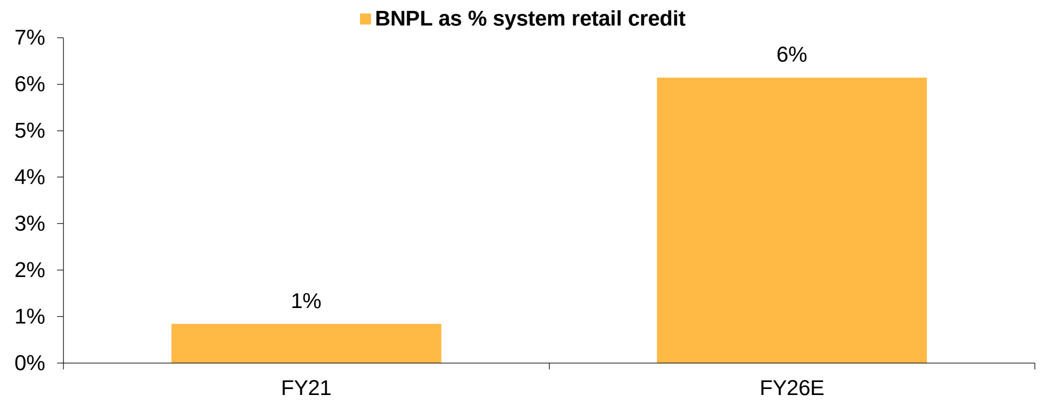
Could there instead be regulatory risks in PayTM's loan distribution model?

On the flip side, there are several risks to PayTM's (and all fintechs) financial services distribution-led business model from a regulatory standpoint, in our view. There are several examples of India's regulators – SEBI, IRDA and RBI – clamping down on financial services distributors to reduce frictional costs to the consumer and prevent mis-selling.

- Currently fintechs act as sourcing agents for other 'lending partners' with the loans sitting on the lending partner's balance sheet.
- However, fintechs also provide substantial default guarantees as well as security deposits to lending partners.
- Hence, credit risks these fintechs are exposed to are high – with little to no capital/licensing requirements.
- We believe it is likely that RBI might come up with restrictions on co-lending (similar to securitisation guidelines) in the near future.
- Current securitisation guidelines stipulate a minimum holding period of 6 monthly instalments before loans can be securitised by an NBFC. It also requires the NBFC to maintain minimum 5-10% of the loan on its own balance sheet.

In fact, in recent speeches RBI has highlighted the need to regulate fintechs, in a manner similar to NBFCs and banks. We believe this will be inevitable as loan originating fintechs become systemically more important. Any securitisation / minimum capital requirement could upend unit economics for fintechs, in our view.

Fig 88 BNPL could scale to ~6% of system retail credit by FY26E. We believe that fintech regulations on down-selling consumer loans are inevitable as this segment gathers scale



Source: Redseer, Macquarie Research, November 2021

Regulatory intervention in China :

Similar regulatory interventions in China over the past year have had serious repercussions on unit economics of fintech players like Ant Financial. Chinese regulators have intervened over the past year with several regulatory changes that have impacted fintechs' unit economics.

- For co-lending loans in China, online microlenders must now take up at least 30% of the total loan amount to a borrower.
- Payment companies are banned from extending loans. Players like Ant are required to break up the payment & lending businesses.
- Payment companies are now not allowed to collect any information which is irrelevant to payment transactions.
- Breaking data monopolies: Loan facilitators (like Ant) now cannot provide data and credit assessment on customers directly to funding providers. They must go through 1 of 3 licensed credit rating companies to provide any credit-related data to the banking system.
- The retail online microloan balance is now capped at Rmb300K (~US$45k) per person or 1/3 of annual income.
- Online micro-lending companies: Minimum capital requirement of Rmb1 billion (~US$150mn)

We think own balance-sheet lending is a must to grow a fintech lending business successfully in India

Such drastic regulatory changes could completely shake up fintech business models and unit economics in India as well. We believe it is quite probable that regulators could look to plug the regulatory arbitrage between fintechs and the financial lenders (banks / NBFCs etc) by imposing a) minimum capital requirements or b) requiring minimum holding requirements similar to securitisation norms.

This is a clear risk to a 'distribution-only' approach to lending in India. This is also in-line with our view that for fitnechs to be able to scale up their businesses sustainably in India they must resort to lending with their own balance sheets and a pure distribution approach may just not work.

However, what works for PayTM in this regard is that it does not plan to take any credit risk on its own balance sheet – and hence will act very similar to a traditional loan originating DSA (direct selling agent).

Fig 89 Indian fintechs currently use co-lending business models with loans carried on balance sheet of larger banks/NBFCs

Name	Lending partner
ZestMoney	22 lending partners
Simpl	ICICI Bank
Epaylater	Fullerton India, Arthashastra (own NBFC)
KrazyBee (E-voucher loans)	Own NBFC, AU SFB, HSBC, Fullerton, and IIFL
OlaMoney Postpaid	AB Capital, IDFC First
Paytm Postpaid	Clix Capital, Arthimpact, AB Capital
AmazonPay Later	Capital Float, Karur Vysya Bank, IDFC First Bank
Mobikwik Zip	IDFC First, DMI Finance, Faircent, Fullerton, InCred
Flipkart PayLater	IDFC First Bank
LazyPay	PayU Finance (Own NBFC)

Source: Company data, Macquarie Research, November 2021

Hence, we believe PayTM's financial distribution business is comparatively better off from a regulatory viewpoint, especially compared to other fintechs that provide default guarantees to lending partners and hence take an indirect credit risk.

Nevertheless, still as a BNPL player, not offering FLDGs (first loss default guarantees), PayTM could be subjected to some level of capital or minimum retention requirements albeit at lower levels compared to other BNPL players that are offering FLDGs.

Disintermediation costs have only been coming down across financial services business in India – and will continue to do so

Disintermediation costs across the financial services business are coming down in India led by both a) regulatory and b) competitive pressures.

There are several examples of regulators – SEBI, IRDA and RBI – clamping down on financial services distributors to reduce frictional costs to the consumer and prevent mis-selling. Some of these are enumerated below:

- Mutual funds: In 2018, SEBI banned asset management companies from giving upfront commissions to distributors to curb mis-selling. It also introduced AUM-wise caps on the total expense ratio that could be charged to consumers.
- Insurance: In 2010, IRDA introduced caps on commission paid to agents for sourcing ULIPs, after cases of rampant mis-selling.
- Payments: In Dec-2019, the Govt of India mandated that MDR for all UPI transactions shall be zero. In Dec-2017, RBI capped debit card MDRs at 0.4% for small merchants and 0.9% for large merchants.

At the same time, competitive forces and a maturing financial services market have also brought down retail fee rates across business lines. We believe this poses a key risk to PayTM's distribution-led business model pivot.

As proportion of UPI in overall GMV goes up, we expect blended take rates will reduce. Current levels of marketing and promotional expenses are also unsustainable.

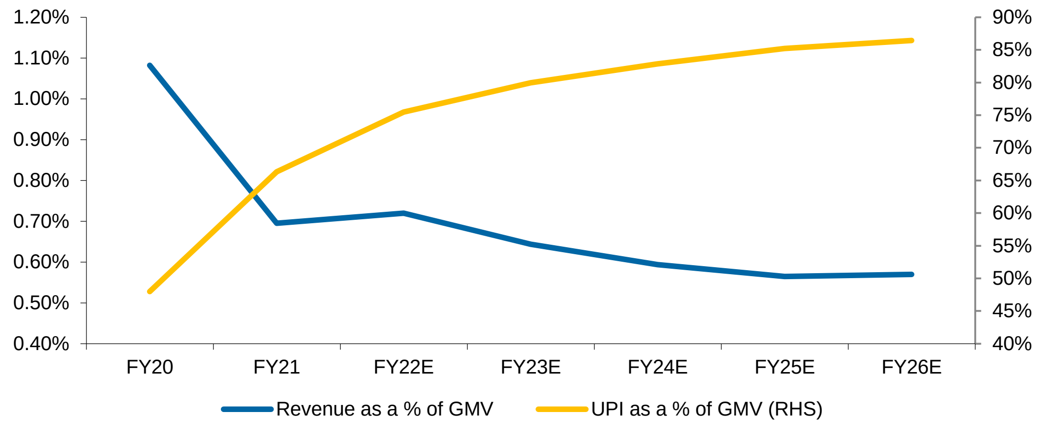
We expect PayTM to turn FCF positive only by FY30.

Profitability – A distant dream

UPI proportion to go up, keeping take rates subdued

We estimate that PayTM's share through the UPI platform in its overall GMV will increase from ~65%+ to 85% over the next five years. Since take rates on UPI GMV are nil, we expect the overall take rate to come down over the years. Note that we are building in sufficient revenues.

Fig 90 As UPI's share in PayTM's GMV goes up, overall take rates to come down

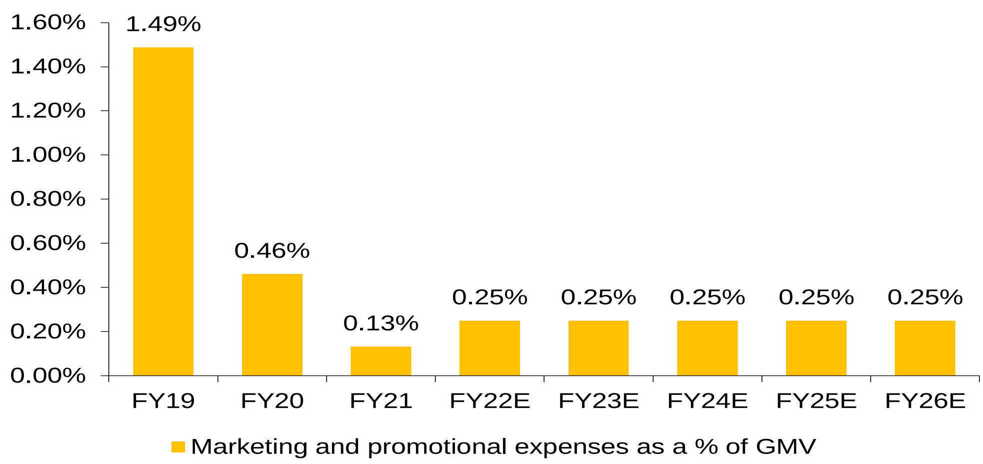


Source: Company data, Macquarie Research, November 2021

Marketing and promotion costs have to go up to sustain revenue growth

One of the main reasons for PayTM's reduced losses in FY21 and higher contribution profit was a sharp reduction in marketing and promotion (M&P) costs. The company has cut down on cash backs and other incentive mechanisms sharply. We don't believe it is sustainable. M&P costs as a % of GMV have reduced sharply from 150bps in FY19 to 13bps for FY21 due to which losses halved despite a 15% decline in revenues. We however expect this to increase to 25bps and most likely sustain around those levels. To sustain a 25%+ revenue CAGR, PayTM in our view can cut M&P costs substantially below 25ps.

Fig 91 Marketing and promotion costs have to go up in our view



Source: Company data, Macquarie Research, November 2021

We are assuming FCF positive only by FY30

We have assumed a strong 26% CAGR over FY21-26E despite falling take rates owing to strong growth in the distribution business (driven mainly by the distribution of loan products).

Fig 92 PayTM – key projections on the topline and its components

		FY2019A	FY2020A	FY2021A	FY2022F	FY2023F	FY2024F	FY2025F	FY2026F
GMV	Rs. Mn	2,292,000	3,032,000	4,033,000	6,232,540	8,235,299	10,469,278	13,238,160	15,911,152
% YoY growth	%	*NA*	*32.3%*	*33.0%*	*54.5%*	*32.1%*	*27.1%*	*26.4%*	*20.2%*
Revenue as a % of GMV	%	*1.41%*	*1.08%*	*0.69%*	*0.72%*	*0.64%*	*0.59%*	*0.56%*	*0.57%*
Total Revenue	Rs. Mn	**32,320**	**32,808**	**28,024**	**44,875**	**53,025**	**62,174**	**74,738**	**90,598**
% YoY growth	%	*NA*	*1.5%*	*-14.6%*	*60.1%*	*18.2%*	*17.3%*	*20.2%*	*21.2%*
Payment and financial services	Rs. Mn	15,711	17,778	19,808	21,589	22,668	22,314	23,430	24,601
% YoY growth	%	*NA*	*13.2%*	*11.4%*	*9.0%*	*5.0%*	*-1.6%*	*5.0%*	*5.0%*
Commerce and cloud services	Rs. Mn	15,365	11,188	6,932	16,176	20,257	25,689	31,839	40,056
% YoY growth	%	*NA*	*-27.2%*	*-38.0%*	*133.4%*	*25.2%*	*26.8%*	*23.9%*	*25.8%*
Distribution business revenue	Rs. Mn	1,244	1,290	1,284	7,110	10,099	14,171	19,469	25,941
% YoY growth	%	*NA*	*3.7%*	*-0.5%*	*453.7%*	*42.0%*	*40.3%*	*37.4%*	*33.2%*
Other operating revenue	Rs. Mn	0	2,552	0	0	0	0	0	0
% YoY growth	%	*NA*	*NA*	*-100.0%*	*NA*	*NA*	*NA*	*NA*	*NA*

Source: Company data, Macquarie Research, November 2021

However, owing to higher marketing and promotion expenses as outlined earlier as well as a higher employee expense driven by strong demand for tech talent, at the EBIDTA level we expect losses to continue for a substantial part of this decade. At best, we expect PayTM to be FCF positive only by FY30E.

Fig 93 PayTM: Free cash flows projections – we project FCF at best to turn positive from FY30E onwards

	FY19A	FY20A	FY21A	FY22E	FY23E	FY24E	FY25E	FY26E	FY27E	FY28E	FY29E	FY30E
Net sales	32,320	32,808	28,024	44,875	53,025	62,174	74,738	90,598	107,790	125,825	144,055	161,693
Net sales y-o-y growth (%)	*NA*	*1.5%*	*-14.6%*	*60.1%*	*18.2%*	*17.3%*	*20.2%*	*21.2%*	*19.0%*	*16.7%*	*14.5%*	*12.2%*
Earnings Before Interest and Taxes (EBIT)	-44,777	-28,089	-19,458	-16,957	-17,855	-18,772	-20,232	-20,463	-16,801	-10,804	-2,285	8,753
EBIT margin (%)	*-138.5%*	*-85.6%*	*-69.4%*	*-37.8%*	*-33.7%*	*-30.2%*	*-27.1%*	*-22.6%*	*-15.6%*	*-8.6%*	*-1.6%*	*5.4%*
Depreciation & amortization	1,116	1,745	1,785	1,287	1,300	1,612	1,425	1,176	1,399	1,633	1,869	2,098
as a % of sales (%)	*3.5%*	*5.3%*	*6.4%*	*2.9%*	*2.5%*	*2.6%*	*1.9%*	*1.3%*	*1.3%*	*1.3%*	*1.3%*	*1.3%*
Tax paid on EBIT	65	158	-27	0	0	0	3,106	3,284	4,200	2,701	571	-2,188
Tax rate (%)	*0.2%*	*0.5%*	*-0.2%*	*0.0%*	*0.0%*	*0.0%*	*25.0%*	*25.0%*	*25.0%*	*25.0%*	*25.0%*	*25.0%*
Gross cash flow	**-43,596**	**-26,186**	**-17,700**	**-15,670**	**-16,555**	**-17,161**	**-15,701**	**-16,003**	**-11,202**	**-6,470**	**155**	**8,663**
Working capital / capex changes	-1,749	-7,030	-1,512	3,995	-1,944	-2,024	-2,268	-2,691	-2,868	-2,397	-1,962	-1,335
Free cash flows	**-45,345**	**-33,216**	**-19,212**	**-11,675**	**-18,499**	**-19,185**	**-17,969**	**-18,693**	**-14,070**	**-8,867**	**-1,806**	**7,328**

Source: Company data, Macquarie Research, November 2021

Our critical assumption here is that UPI will form a very substantial part of the GMV and take rates on UPI transactions will continue to remain nil. While take rates in other businesses like wallets and ecommerce could also be under pressure due to competition and/or regulations, for the time being we have taken a flat take rate in these businesses in our financial projections for PayTM.

We value PayTM at Rs1,200/sh offering ~40%+ downside from IPO price of Rs2,150

Alternate DCF approach leads to Rs1,370/sh valuation

Valuation – A simple PSg based approach

Globally, payments is a mature, profitable business – these companies trade at 20-22x CY22F EV/EBITDA for mid-teen growth rates, as seen in Fig 94 below.

- Even within payments companies – new age payments businesses that are scaling up faster (Square/Adyen) are valued at 50-65x CY22E EV/EBITDA.
- BNPLs are largely yet to demonstrate profitability – we look to value these companies by using a PSg (Price/ Sales to Sales growth) ratio methodology.
- Growth rates for BNPL companies are much higher – 40-50% on average over CY22-23E.
- BNPLs trade at an average multiple of ~0.3x CY22E PSg. Payments companies trade at ~0.5x CY22E PSg on average

Fig 94 Valuations – where do global comps trade at?

	Market cap		Sales growth (%)			EV / Sales (x)			EV / EBITDA (x)			PSg multiple	
Company	**($mn)**	**EV ($mn)**	**2021**	**2022**	**2023**	**2021**	**2022**	**2023**	**2021**	**2022**	**2023**	**2022**	**2023**
BNPL													
Afterpay	33,143	33,317	81%	63%	54%	35	22	14	329	290	107	0.3	0.3
Affirm	37,083	36,128	64%	47%	44%	43	29	20	NM	NM	1,822	0.6	0.5
Zip	3,252	4,586	148%	71%	40%	12	7	5	NM	NM	108	0.1	0.1
Sezzle	917	631	106%	58%	38%	5	3	2	NM	NM	NM	0.1	0.1
Humm	404	2,664	-4%	7%	18%	6	5	5	23	26	23	0.1	0.0
BNPL average	**14,960**	**15,465**	**79%**	**49%**	**39%**	**28**	**19**	**13**				**0.4**	**0.3**
Global Payments													
Visa	471,297	472,877	10%	18%	14%	20	17	15	28	24	21	1.0	1.0
Mastercard	351,697	358,741	23%	20%	16%	19	16	14	33	26	22	0.8	0.9
Paypal	240,438	235,846	19%	20%	21%	9	8	6	32	27	22	0.4	0.3
American Express	140,497	149,317	9%	13%	10%	4	3	3	15	14	13	0.2	0.3
Square	104,806	104,657	88%	9%	22%	6	5	4	103	89	57	0.6	0.2
Adyen	78,602	75,345	-73%	38%	36%	76	55	40	122	86	63	1.5	1.2
Fidelity National	72,092	90,670	11%	8%	8%	7	6	6	15	13	12	0.6	0.6
Fiserv	66,188	87,232	4%	7%	8%	6	5	5	14	12	11	0.5	0.5
Discover Financial	34,419	41,289	-7%	1%	6%	3	3	3	6	8	9	2.0	0.4
Payments average	**173,337**	**179,553**	**9%**	**15%**	**16%**	**9**	**8**	**7**	**24**	**22**	**19**	**0.5**	**0.5**

Source: Bloomberg, Macquarie Research, November 2021

How are we valuing PayTM?

As seen above, globally the Fintech companies are trading at 0.3x-0.5x PSg. We are valuing at the upper end of that range at 0.5x for PayTM. We are unwilling to give premium multiples here for PayTM as we are unsure about the path to profitability especially in the context of UPI, regulations and competitive pressures that exist.

Fig 95 PayTM valuation – based on price-to-sales growth (PSg) methodology implies ~44% downside

PSg - based valuation	
Sales CAGR (FY21-26E)	26.4%
Dec-23E annualised sales (Rs m)	55,312
Target PSg multiple (x)	0.5x
Valuation based on PSg (Rs m)	772,453
No. of shares (m)	644
Target price (Rs) Rounded off	**1,200**

Source: Company data, Macquarie Research, November 2021

Alternative valuation methodology – DCF-based valuation of Rs1,370

We also tried valuing PayTM using a DCF-based methodology, which suggests a fair value of Rs1,370/share, also indicating downside of 36%. As can be seen in the figure below, the entire value for PayTM is captured in the terminal value as per our projections. This is because in our model assumption, PayTM turns FCF positive only from FY30 onwards.

Fig 96 Alternative valuation methodology – A DCF approach for valuing PayTM results in a valuation of Rs1,370/sh

Equity Valuation - DCF MACQUARIE

WACC Assumptions	
Risk free rate	6.3%
Beta	1.2
Market risk premium	4.6%
Marginal tax rate	25.0%
Pre-tax cost of debt	10.0%
Cost of equity	**11.8%**
Target debt/value ratio	20.0%
Target equity/value ratio	80.0%
WACC	**10.9%**
Growth Rate assumption	
Sustainable long term growth rate	10.0%

Enterprise Valuation	
Share Price (INR - trading currency)	2,150.0
Exchange rate	1.00
Share Count Adjustment Factor	1.00
No. of shares used to calculate mkt cap (m)	643.6
Total Market Cap (INRm)	**1,383,750**
Plus: Net Debt	-18,272
Plus: Minority Interests	-186
Less: Investments	131,691
Less: Associates	2,317
Plus: Pension Liabilities	0
Plus: Other Obligations	0
Enterprise value (INRm)	**1,231,284**

Asset valuation		
Present value of forecast cash flows (2022 - 2031)	-65,902	-9.0%
Present value of forecast cash flows (2032 - perpetuity)	795,737	109.0%
less weighted average net debt	-18,272	
less unfunded pension liabilities	0	
add net investments / associates	134,008	
less minority interests	-186	
Total Valuation	**882,302**	
NPV / share (as at 11 Nov 2021)	**1,371**	
Current share price	2,150.0	
Upside/(downside) to NPV / share	**(36.2%)**	

Free cash flows	FY2019A A	FY2020A A	FY2021A A	FY2022F F	FY2023F F	FY2024F F	FY2025F F	FY2026F F	FY2027F F	FY2028F F	FY2029F F	FY2030F F	FY2031F F
Net sales	32,320	32,808	28,024	44,875	53,025	62,174	74,738	90,598	107,790	125,825	144,055	161,693	177,863
Net sales y-o-y growth (%)	*na*	*1.5%*	*-14.6%*	*60.1%*	*18.2%*	*17.3%*	*20.2%*	*21.2%*	*19.0%*	*16.7%*	*14.5%*	*12.2%*	*10.0%*
Earnings Before Interest and Taxes (EBIT)	-44,777	-28,089	-19,458	-16,957	-17,855	-18,772	-20,232	-20,463	-16,801	-10,804	-2,285	8,753	22,079
EBIT margin (%)	*-138.5%*	*-85.6%*	*-69.4%*	*-37.8%*	*-33.7%*	*-30.2%*	*-27.1%*	*-22.6%*	*-15.6%*	*-8.6%*	*-1.6%*	*5.4%*	*12.4%*
Depreciation & amortization	1,116	1,745	1,785	1,287	1,300	1,612	1,425	1,176	1,399	1,633	1,869	2,098	2,308
as a % of sales (%)	*3.5%*	*5.3%*	*6.4%*	*2.9%*	*2.5%*	*2.6%*	*1.9%*	*1.3%*	*1.3%*	*1.3%*	*1.3%*	*1.3%*	*1.3%*
Tax paid on EBIT	65	158	-27	0	0	0	3,106	3,284	4,200	2,701	571	-2,188	-5,520
Tax rate (%)	*0.2%*	*0.5%*	*-0.2%*	*0.0%*	*0.0%*	*0.0%*	*25.0%*	*25.0%*	*25.0%*	*25.0%*	*25.0%*	*25.0%*	*25.0%*
Gross cash flow	**-43,596**	**-26,186**	**-17,700**	**-15,670**	**-16,555**	**-17,161**	**-15,701**	**-16,003**	**-11,202**	**-6,470**	**155**	**8,663**	**18,867**
Working capital/ Capex Changes	-1,749	-7,030	-1,512	3,995	-1,944	-2,024	-2,268	-2,691	-2,868	-2,397	-1,962	-1,335	-529
Free cash flows	**-45,345**	**-33,216**	**-19,212**	**-11,675**	**-18,499**	**-19,185**	**-17,969**	**-18,693**	**-14,070**	**-8,867**	**-1,806**	**7,328**	**18,338**

Source: Company data, Macquarie Research, November 2021

Note that the DCF-based methodology gives us a fair value which is roughly ~14% higher than our PSg methodology. Even in our **bull case sensitivity analysis**, the DCF-based methodology gives a fair value of Rs3,300 vs. PSg methodology fair value of Rs2,900.

Sensitivity analysis – Bull & bear scenarios

We also look at what could be the fair value of PayTM under different bull and bear case assumptions.

a) **Bull Case scenario:** In the bull-case, we estimate the impact on fair value if UPI transactions can be monetised. This is the key upside risk to our model assumptions as we believe our topline assumptions otherwise assumed fairly optimistic business growth. Hence, in our bull case we assume PayTM has a 10bps take rate on all UPI **transactions.** In this case, PayTM's sales FY21-26E CAGR picks up to 30% (from 26% in our model assumption), and there is a corresponding improvement in profitability as well. We use a target PSg multiple of 1.0x to account for this and our bull case valuation comes to Rs2,900/sh. Note that the reason why we are giving a higher multiple is because a substantial proportion of GMV, which consists of UPI, becomes monetizable. If you look at the risk section in the report, you will see that a mere 10bps take rate on UPI can significantly swing cashflow in a positive direction. The DCF-based methodology gives a fair value of Rs3,300 offering 50%+ upside in the stock from IPO price of Rs2,150.

Fig 97 Bull case PayTM valuation leads to fair value of Rs 2,900/sh

PayTM bull case : PSg - based valuation	
Sales CAGR (FY21-26E)	30.1%
Dec-23E annualised sales (Rs m)	62,420
Target PSg multiple (x)	1.0x
Valuation based on PSg (Rs m)	1,314,125
No. of shares (m)	644
Valuation (Rs) Rounded off	**2,900**
CMP based on IPO price	2,150
Upside	**35%**

Source: Macquarie Research, November 2021

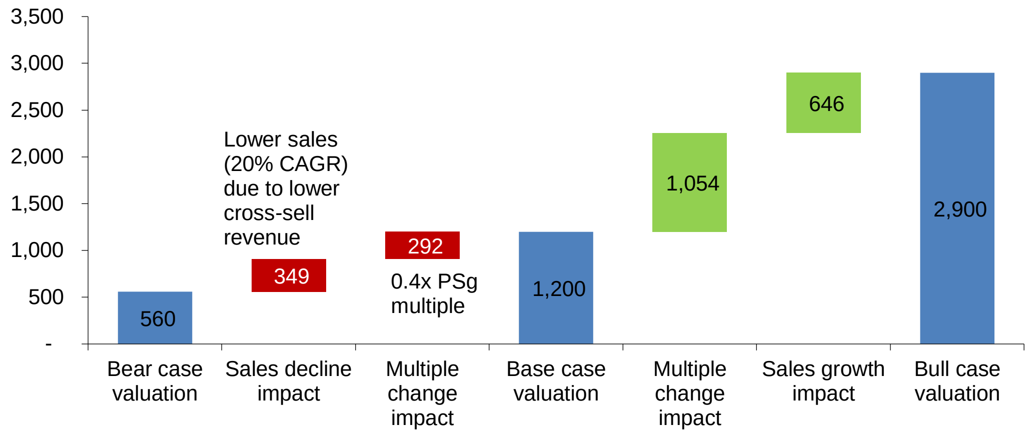
b) **Bear case scenario:** In our bear case, we assume lower cross-sell revenues in the commerce vertical (FY21-26E CAGR of 8% vs 24% in our model assumption). We also assume a 50bps lower take rate in the financial services distribution business. In this case, PayTM's sales CAGR falls to 20% (from 26% in our model assumption), and there is a corresponding decline in profitability as well. We use a target PSg multiple of 0.4x and our bear case fair value comes to Rs560/sh.

Fig 98 Bear case PayTM valuation leads to fair value of Rs560/sh

PayTM bear case : PSg - based valuation	
Sales CAGR (FY26-21E)	19.9%
Dec-23E annualised sales (Rs m)	45,232
Target PSg multiple (x)	0.4x
Valuation based on PSg (Rs m)	359,595
No. of shares (m)	644
Valuation (Rs) Rounded off	**560**
CMP based on IPO price	2,150
Downside	**-74%**

Source: Macquarie Research, November 2021

Fig 99 PayTM – bull and bear case valuation scenarios



Source: Macquarie Research, November 2021

If UPI can be monetised PayTM's FCF profile can improve

Receipt of bank license another key upside risk

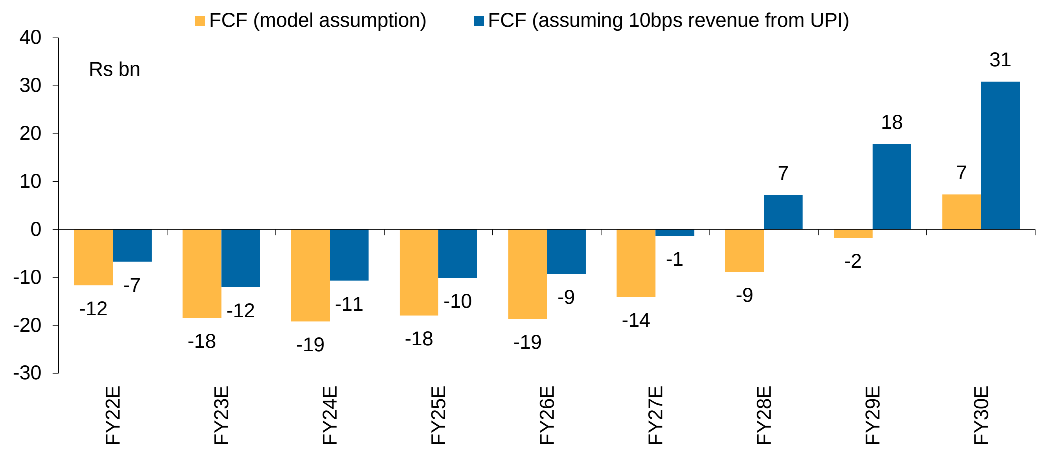
Risks – Monetisation of UPI and receipt of bank license

As mentioned previously, the key risk to our negative stance on PayTM would be if it is able to monetise UPI transactions on its platform in any way. This is something that we believe is highly unlikely to happen as transactional costs have only gone down across financial services businesses in India . However, this remains a key risk to our model assumptions.

If UPI can be monetised in any way going forward, it could be an enabler to 'close the loop' on the platform rewards and incentives to consumers, that are actually economically viable. However, even in such a scenario, we think charges on UPI will only be nominal (few basis points)

If we assume PayTM is able to make 10bps revenue on UPI transactions on its platform, then its cash flow profile starts turning positive from FY28 onwards (instead of FY30 in our original model assumption), as shown below.

Fig 100 If we assume 10bps revenue from UPI transactions, PayTM's FCF starts turning positive from FY28



Source: Macquarie Research, November 2021

Separately, another upside risk to our thesis is if PayTM is the ability to receive any sort of banking license (say small finance bank license or even a special digital bank license), which enables it to lend to customers on its own balance sheet.

Appendix: Financials, Management background, Shareholding pattern

Fig 101 One97 Communications Limited - Management profile

Key Managerial Personnel	Background	Equity Shares & ESOPs	Compensation FY21
Mr. Vijay Shekhar Sharma MD & CEO (Founder)	He also serves as Chairman of the Board. He holds a Btech degree in electronics & communications from Delhi College of Engineering. Mr. Sharma has received multiple industry honours and featured in Time Magazine.	60mn equity shares and 21mn ESOPs	Rs 40mn
Mr. Madhur Deora President and Group CFO (Joined - Oct'16)	He joined in 2016 as CFO & SVP. Prior to joining PayTM he worked with Citigroup Global Markets for 17 years. Mr. Deora holds a B.Sc Economics degree from Wharton School of the University of Pennsylvania..	640k equity shares and 670k ESOPs	Rs 22mn
Mr. Harinderpal Singh Takhar CEO, Paytm Labs (Joined - Jun'13)	He served as CEO of PayTM from 2011 to 2014. In the past, he has worked with PayPay Corporation, Research in Motion and Nokia. Mr. Takhar holds a Btech degree in Computer Engineering. from University of Delhi and an MBA degree from INSEAD.	1.2mn equity shares and 23k ESOPs	Rs 16mn
Mr. Vikas Garg CFO (Joined - May'14)	Before his current tenure at PayTM, he was associated with the company previously from 2008 to 2012. In the past he has worked with ICICI Bank and Ibibo. He holds a B.Comm degree from MDU, Rohtak and is certified as a CA by ICAI, India.	470k equity shares and 220k ESOPs	Rs 11mn
Ms. Renu Satti COO, Offline Payments (Joined - Oct'06)	She served as CEO of Paytm Payments Bank from 2017 to 2018 before her current role. Ms. Satti holds a B.Comm degree from University of Delhi.	280k equity shares and 110k ESOPs	Rs 12mn
Mr. Sudhanshu Gupta COO, Paytm First Games Pvt. Ltd. (Joined - Jun'18)	He has been associated with Paytm since 2013 and started his current role in 2018. He has worked with Flipkart, Diageo and PepsiCo in the past. Mr. Gupta holds a B.Sc degree from University of Delhi and a PGDBM from MDI Gurugram.	160k equity shares and 110k ESOPs	Rs 14mn
Mr. Bhavesh Gupta CEO, Lending Business (Joined - Aug'20)	He has more than 24 years of banking experience and has worked for Clix Capital, IDFC Bank and ICICI Bank in the past. He holds an MBA degree from Institute of Management Studies, Devi Ahilya Vishwavidyalaya, Indore.	380k ESOPs	Rs 22mn
Mr. Praveen Kumar Sharma MD & CEO, Paytm Payments Services (Joined - Sep'19)	He has worked with Google as a Regional Director and Head of Youtube and Display sales in the past. Mr. Sharma holds a BTech degree in Mechanical Engineering. from MDU, Rohtak and a PG diploma in Communications from Mudra Institute of Communications.	14k equity shares and 200k ESOPs	Rs 24mn
Mr. Manmeet Singh Dhody CTO, Payments (Joined - Apr'20)	He has worked with Amazon Development Centre India and Microsoft India (R&D) in the past. Mr. Dhody holds a B.Tech degree in Computer Engineering from University of Delhi and an MBA from Punjab University.	8k equity shares and 140k ESOPs	Rs 31mn
Mr. Deepankar Sanwalka President, Compliance and Operations (Joined - May'21)	Mr. Sanwalka has worked with PwC and KPMG in the past. He holds a B.Comm degree from University of Delhi and is certified as a CA by ICAI, India	150k ESOPs	N.A
Mr. Amit Khera Company Secretary and Compliance Officer (Joined - Apr'21)	He has worked with Publicis Groupe, Bharti Airtel and FieldFresh Food in the past. Mr. Khera holds a B.Comm degree from University of Delhi and a Business law degree from National Law School of India University, Bangalore.	16k ESOPs	N.A

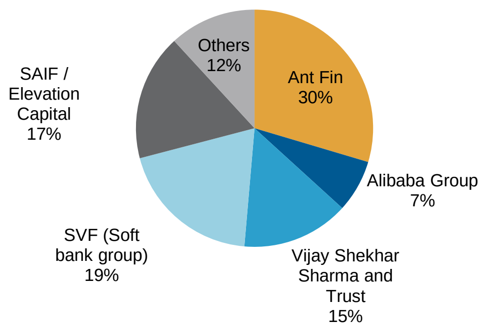
Source: Company Data, Macquarie Research, November 2021

Fig 102 One 97 Communication Limited – Key financials

Financial Summary	**FY21**	**FY22E**	**FY23E**	**FY24E**	**FY25E**	**FY26E**
GMV (Rs bn)	**4,033**	**6,233**	**8,235**	**10,469**	**13,238**	**15,911**
P&L (Rs mn)	**FY21**	**FY22E**	**FY23E**	**FY24E**	**FY25E**	**FY26E**
Payment and financial services	19,808	21,589	22,668	22,314	23,430	24,601
Commerce and cloud services	6,932	16,176	20,257	25,689	31,839	40,056
Distribution business revenue	1,284	7,110	10,099	14,171	19,469	25,941
Other operating revenue	0	0	0	0	0	0
Total operating revenue	**28,024**	**44,875**	**53,025**	**62,174**	**74,738**	**90,598**
Op. revenue as % GMV	*0.7%*	*0.7%*	*0.6%*	*0.6%*	*0.6%*	*0.6%*
Payment processing charges	19,168	21,814	23,059	24,079	27,800	33,413
Payment proc cost as % GMV	0.5%	0.4%	0.3%	0.2%	0.2%	0.2%
Marketing expenses	5,325	15,581	20,588	26,173	33,095	39,778
Marketing as % GMV	0.1%	0.3%	0.3%	0.3%	0.3%	0.3%
Contribution profit	**3,531**	**7,480**	**9,378**	**11,922**	**13,843**	**17,406**
Contribution profit as % GMV	*0.1%*	*0.1%*	*0.1%*	*0.1%*	*0.1%*	*0.1%*
Employee expense	11,849	13,034	14,989	17,237	19,823	22,796
Other opex	9,355	10,116	10,944	11,845	12,827	13,897
EBITDA	**-17,673**	**-15,670**	**-16,555**	**-17,161**	**-18,808**	**-19,287**
EBITDA as % GMV	*-0.4%*	*-0.3%*	*-0.2%*	*-0.2%*	*-0.1%*	*-0.1%*
Depreciation	-1,785	-1,287	-1,300	-1,612	-1,425	-1,176
EBIT	**-19,458**	**-16,957**	**-17,855**	**-18,772**	**-20,232**	**-20,463**
Other income	3,496	4,162	9,154	8,708	7,807	7,325
Extraordinaries	-1,021	0	0	0	0	0
PBT	-16,983	-12,795	-8,701	-10,064	-12,426	-13,138
PAT	**-16,961**	**-12,758**	**-8,676**	**-10,035**	**-9,292**	**-9,825**
PAT as % GMV	*-0.4%*	*-0.2%*	*-0.1%*	*-0.1%*	*-0.1%*	*-0.1%*
Balance sheet (Rs mn)	**FY21**	**FY22E**	**FY23E**	**FY24E**	**FY25E**	**FY26E**
Share Capital	605	644	644	644	644	644
Reserves & surplus	64,743	134,946	126,271	116,236	106,943	97,118
Minority interest	-186	-223	-248	-277	-304	-332
Net worth	**65,162**	**135,367**	**126,666**	**116,602**	**107,283**	**97,430**
Current liabilities	21,552	30,824	35,389	34,295	40,075	42,841
Long term liabilities	4,799	5,039	5,291	5,555	5,833	6,125
Total equity & liabilities	**91,513**	**171,231**	**167,346**	**156,453**	**153,191**	**146,396**
Cash & investments	56,553	131,691	121,984	111,131	100,578	88,803
Other current assets	17,445	20,086	23,733	21,611	25,978	26,961
Total current assets	73,998	151,777	145,717	132,742	126,556	115,764
Net tangible fixed assets	5,149	6,498	8,059	9,500	11,756	15,054
Other non-current assets	12,366	12,955	13,570	14,211	14,880	15,577
Total non-current assets	17,515	19,454	21,629	23,711	26,635	30,631
Total assets	**91,513**	**171,231**	**167,346**	**156,453**	**153,191**	**146,396**
Cash flow (Rs mn)	**FY21**	**FY22E**	**FY23E**	**FY24E**	**FY25E**	**FY26E**
Operating profit (EBIT)	-19,458	-16,957	-17,855	-18,772	-20,232	-20,463
Other operating cash flow adjustments	-1,367	6,990	1,261	1,660	4,935	5,206
Operating cash flow	**-20,825**	**-9,967**	**-16,593**	**-17,113**	**-15,297**	**-15,257**
Investing cash flow	**19,298**	**-3,692**	**-43,387**	**10,164**	**8,426**	**6,953**
Fresh equity issuance	107	83,000	0	0	0	0
Other financial cash flow	-2,328	240	252	265	278	292
Financial cash flow	**-2,221**	**83,240**	**252**	**265**	**278**	**292**
Total cash flows	**-3,708**	**69,580**	**-59,728**	**-6,684**	**-6,593**	**-8,012**
Important metrics	**FY21**	**FY22E**	**FY23E**	**FY24E**	**FY25E**	**FY26E**
Revenue growth	-15%	60%	18%	17%	20%	21%
EPS	-28.0	-20.4	-13.5	-15.6	-14.4	-15.3
BVPS	108	211	197	182	167	152
EBITDA margin	-63%	-35%	-31%	-28%	-25%	-21%
RoE (%)	-23%	-13%	-7%	-8%	-8%	-10%
EV / sales	43.9	27.4	23.2	19.8	16.5	13.6
P/ BV	19.9	10.2	10.9	11.8	12.9	14.2

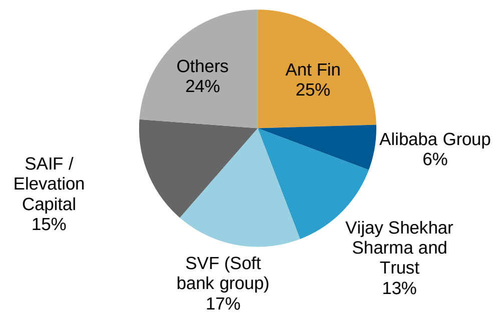
Source: Company, Macquarie Research, November 2021

Fig 103 Pre-offer shareholding pattern – Ant and Alibaba own 37% stake



Source: Company data, Macquarie Research, November 2021

Fig 104 Post-offer shareholding pattern – Ant and Alibaba will still own 31% stake on date of listing



Source: Company data, Macquarie Research, November 2021

Covered companies mentioned

- HDFC Bank (HDFCB IN, OP, CMP Rs 1548, TP Rs 2005)
- State Bank of India (SBIN IN, OP, CMP Rs 495, TP Rs 580)
- ICICI Bank (ICICIBC IN, OP, CMP Rs 764, TP Rs 835)
- Axis Bank (AXSB IN, N, CMP Rs 726, TP Rs 815)
- SBI Cards & Payments Services Ltd (SBICARD IN, OP, CMP Rs 1081, TP Rs 1110)

One 97 Communications (ONE97 IN)

Quarterly Results		3Q/22E	4Q/22E	1Q/23E	2Q/23E
Revenue	m	11,219	11,219	13,256	13,256
Gross Profit	m	5,765	5,765	7,491	7,491
Cost of Goods Sold	m	5,453	5,453	5,765	5,765
EBITDA	m	-3,917	-3,917	-4,139	-4,139
Depreciation	m	322	322	325	325
Amortisation of Goodwill	m	0	0	0	0
Other Amortisation	m	0	0	0	0
EBIT	m	-4,239	-4,239	-4,464	-4,464
Net Interest Income	m	1,041	1,041	2,288	2,288
Associates	m	0	0	0	0
Exceptionals	m	0	0	0	0
Forex Gains / Losses	m	0	0	0	0
Other Pre-Tax Income	m	0	0	0	0
Pre-Tax Profit	m	-3,199	-3,199	-2,175	-2,175
Tax Expense	m	0	0	0	0
Net Profit	m	-3,199	-3,199	-2,175	-2,175
Minority Interests	m	9	9	6	6
Reported Earnings	m	-3,189	-3,189	-2,169	-2,169
Adjusted Earnings	m	-3,189	-3,189	-2,169	-2,169
EPS (rep)		-5.11	-5.11	-3.37	-3.37
EPS (adj)		-5.11	-5.11	-3.37	-3.37
EPS Growth yoy (adj)	%	nmf	nmf	34.0	34.0
EBITDA Margin	%	-34.9	-34.9	-31.2	-31.2
EBIT Margin	%	-37.8	-37.8	-33.7	-33.7
Earnings Split	%	25.0	25.0	25.0	25.0
Revenue Growth	%	nmf	nmf	18.2	18.2
EBIT Growth	%	nmf	nmf	-5.3	-5.3

Profit & Loss		2022E	2023E	2024E	2025E
Revenue	m	44,875	53,025	62,174	74,738
Gross Profit	m	23,061	29,966	38,095	46,938
Cost of Goods Sold	m	21,814	23,059	24,079	27,800
EBITDA	m	-15,670	-16,555	-17,161	-18,808
Depreciation	m	1,287	1,300	1,612	1,425
Amortisation of Goodwill	m	0	0	0	0
Other Amortisation	m	0	0	0	0
EBIT	m	-16,957	-17,855	-18,772	-20,232
Net Interest Income	m	4,162	9,154	8,708	7,807
Associates	m	0	0	0	0
Exceptionals	m	0	0	0	0
Forex Gains / Losses	m	0	0	0	0
Other Pre-Tax Income	m	0	0	0	0
Pre-Tax Profit	m	-12,795	-8,701	-10,064	-12,426
Tax Expense	m	0	0	0	3,106
Net Profit	m	-12,795	-8,701	-10,064	-9,319
Minority Interests	m	37	25	29	27
Reported Earnings	m	-12,758	-8,676	-10,035	-9,292
Adjusted Earnings	m	-12,758	-8,676	-10,035	-9,292
EPS (rep)		-20.42	-13.48	-15.59	-14.44
EPS (adj)		-20.42	-13.48	-15.59	-14.44
EPS Growth (adj)	%	nmf	34.0	-15.7	7.4
PE (rep)	x	nmf	nmf	nmf	nmf
PE (adj)	x	nmf	nmf	nmf	nmf
Total DPS		0.00	0.00	0.00	0.00
Total Div Yield	%	0.0	0.0	0.0	0.0
Basic Shares Outstanding	m	644	644	644	644
Diluted Shares Outstanding	m	625	644	644	644

Profit and Loss Ratios		2022E	2023E	2024E	2025E
Revenue Growth	%	nmf	18.2	17.3	20.2
EBITDA Growth	%	nmf	-5.6	-3.7	-9.6
EBIT Growth	%	nmf	-5.3	-5.1	-7.8
Gross Profit Margin	%	51.4	56.5	61.3	62.8
EBITDA Margin	%	-34.9	-31.2	-27.6	-25.2
EBIT Margin	%	-37.8	-33.7	-30.2	-27.1
Net Profit Margin	%	-28.4	-16.4	-16.1	-12.4
Payout Ratio	%	nmf	nmf	nmf	nmf
EV/EBITDA	x	-82.4	-78.0	-75.2	-68.6
EV/EBIT	x	-76.1	-72.3	-68.8	-63.8
Balance Sheet Ratios					
ROE	%	-9.4	-6.6	-8.2	-8.3
ROA	%	-9.9	-10.5	-11.6	-13.1
ROIC	%	nmf	-41.8	-20.0	-16.8
Net Debt/Equity	%	-68.4	-26.0	-22.5	-18.3
Interest Cover	x	nmf	nmf	nmf	nmf
Price/Book	x	10.2	10.9	11.8	12.9
Book Value per Share		210.7	197.2	181.6	167.2

Cashflow Analysis		2022E	2023E	2024E	2025E
EBITDA	m	-15,670	-16,555	-17,161	-18,808
Tax Paid	m	0	0	0	-3,106
Chgs in Working Cap	m	-6,632	-916	-1,029	-1,413
Net Interest Paid	m	-4,162	-9,154	-8,708	-7,807
Other	m	16,497	10,032	9,785	15,836
Operating Cashflow	m	-9,967	-16,593	-17,113	-15,297
Acquisitions	m	-87	-87	-87	-87
Capex	m	-2,692	-2,916	-3,109	-3,737
Asset Sales	m	56	56	56	56
Other	m	-968	-40,439	13,304	12,194
Investing Cashflow	m	-3,692	-43,387	10,164	8,426
Dividend (Ordinary)	m	0	0	0	0
Equity Raised	m	83,000	0	0	0
Debt Movements	m	0	0	0	0
Other	m	240	252	265	278
Financing Cashflow	m	83,240	252	265	278
Net Chg in Cash/Debt	m	69,580	-59,728	-6,684	-6,593
Free Cashflow	m	-12,660	-19,510	-20,222	-19,034

Balance Sheet		2022E	2023E	2024E	2025E
Cash	m	98,344	38,617	31,932	25,339
Receivables	m	4,379	5,175	6,068	7,294
Inventories	m	0	0	0	0
Investments	m	33,347	83,367	79,199	75,239
Fixed Assets	m	6,498	8,059	9,500	11,756
Intangibles	m	0	0	0	0
Other Assets	m	28,662	32,129	29,755	33,564
Total Assets	m	171,231	167,346	156,453	153,191
Payables	m	9,425	11,137	13,059	15,697
Short Term Debt	m	5,693	5,693	5,693	5,693
Long Term Debt	m	0	0	0	0
Provisions	m	3,141	3,712	3,109	3,737
Other Liabilities	m	17,604	20,138	17,990	20,781
Total Liabilities	m	35,863	40,679	39,851	45,908
Shareholders' Funds	m	135,590	126,914	116,879	107,587
Minority Interests	m	-223	-248	-277	-304
Other	m	0	0	0	0
Total S/H Equity	m	135,367	126,666	116,602	107,283
Total Liab & S/H Funds	m	171,231	167,346	156,453	153,191

All figures in INR unless noted.
Source: Company data, Macquarie Research, November 2021

Important disclosures:

Recommendation definitions

Macquarie – Asia and USA
Outperform – expected return >10%
Neutral – expected return from -10% to +10%
Underperform – expected return <-10%

Macquarie – Australia/New Zealand
Outperform – expected return >10%
Neutral – expected return from 0% to 10%
Underperform – expected return <0%

Note: expected return is reflective of a Medium Volatility stock and should be assumed to adjust proportionately with volatility risk

Volatility index definition*

This is calculated from the volatility of historical price movements.

Very high–highest risk – Stock should be expected to move up or down 60–100% in a year – investors should be aware this stock is highly speculative.

High – stock should be expected to move up or down at least 40–60% in a year – investors should be aware this stock could be speculative.

Medium – stock should be expected to move up or down at least 30–40% in a year.

Low–medium – stock should be expected to move up or down at least 25–30% in a year.

Low – stock should be expected to move up or down at least 15–25% in a year.
* Applicable to select stocks in Asia/Australia/NZ

Recommendations – 12 months
Note: Quant recommendations may differ from Fundamental Analyst recommendations

Financial definitions

All "Adjusted" data items have had the following adjustments made:
Added back: goodwill amortisation, provision for catastrophe reserves, IFRS derivatives & hedging, IFRS impairments & IFRS interest expense
Excluded: non recurring items, asset revals, property revals, appraisal value uplift, preference dividends & minority interests

EPS = adjusted net profit / efpowa*
ROA = adjusted ebit / average total assets
ROA Banks/Insurance = adjusted net profit /average total assets
ROE = adjusted net profit / average shareholders funds
Gross cashflow = adjusted net profit + depreciation
*equivalent fully paid ordinary weighted average number of shares

All Reported numbers for Australian/NZ listed stocks are modelled under IFRS (International Financial Reporting Standards).

Recommendation proportions – For quarter ending 30 Sept 2021

	AU/NZ	Asia	USA	
Outperform	62.76%	67.53%	74.19%	(for global coverage by Macquarie, 4.72% of stocks followed are investment banking clients)
Neutral	31.03%	21.83%	24.73%	(for global coverage by Macquarie, 3.23% of stocks followed are investment banking clients)
Underperform	6.21%	10.64%	1.08%	(for global coverage by Macquarie, 0.00% of stocks followed are investment banking clients)

12-month target price methodology

ONE97 IN: Rs1,200.00 based on a DCF methodology

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