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INDIAN CORPORATE SECTOR

Mixed quarter for the Indian Corporate sector as margins decline on back of rising cost headwinds

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Quarterly Update

The Indian Corporate Sector showed strong revenue growth in Q2 FY2019 driven by stable demand from consumer-oriented sectors and robust growth in commodity prices

Q2 FY 2019 results released so far indicate healthy revenue growth but compression in profit margins

The Q2 financial results released by 176 companies in the Indian Corporate Sector shows revenue growth of 23.9% on a YoY basis driven by robust growth in commodity linked sectors on back of rising commodity prices, and stable consumer demand. Commodity linked sectors posted 61% revenue growth on a YoY basis, supported by higher oil and steel prices, and healthy demand for cement. Excluding commodities, revenue growth for rest of the sample was 13.7% YoY, which too is relatively higher vis-a-vis previous quarters. In the consumer-oriented sectors, the trends were mixed-bag. For instance, the Passenger Vehicle segment registered a de-growth of 3.6% in Q2 FY2019 on a YoY basis because of delayed festive season, high base and rising ownership cost (Fuel, EMIs and Insurance). The 2W segment also registered tepid growth of 4.9% in Q2 driven by steep price hike after the change in insurance guidelines for third party cover and delayed festive season. Except for the automobile sector, other consumer linked sectors saw stable consumer demand, as reflected in the healthy volume growth in FMCG and Consumer Durables. Among other sectors, IT sector reported healthy revenue growth of 9.2% (in USD terms) supported by digital offerings and pickup in demand from BFSI clients.

However, EBIDTA margins declined by 220 bps on a YoY basis because of rise in raw material and energy cost and adverse impact of rupee depreciation

While revenues grew at a healthy pace in Q2, the aggregate EBITDA margins declined by 220 bps on a YoY basis and 70 bps on QoQ basis to 18.1% because of rise in energy costs and increase in input costs. While sectors such as Airlines, Cement and Building Materials (Tiles & Glass) reported a decline in EBITDA margins because of sharp increase in fuel prices, sectors such as Paints, Auto OEMs, News Print and Consumer Durables also saw margin contraction because of rising input costs. The increase in input costs is attributed to rise in commodity prices, such as steel, and higher import costs because of INR depreciation. While several companies across sectors reported an increase in realizations, the extent of pass through doesn't appear adequate to mitigate the adverse impact from higher fuel and input costs.

Rupee depreciation and higher fuel costs to keep profit margins suppressed in FY 2019

The adverse impact of sharp rupee depreciation and high fuel prices is expected to sustain in the current fiscal

The adverse impact of INR depreciation and higher fuel prices is likely to continue in the current fiscal. The INR depreciated 5.8% between June 30, 2018 and Sep 30, 2018 against the US Dollar. As a result, companies in sectors like Auto OEMs, Airlines, Consumer Durables and Paints that have sizeable imports witnessed contraction in EBITDA margins during Q2. Besides INR depreciation, sharp increase in fuel costs have also put pressure on energy intensive sectors such as Cement, Airlines and Tiles & Ceramics. Several companies reported an increase in logistics costs Q2 FY 2019 because of the rise in fuel prices. While sectors like consumer durables, Auto OEM, Ceramic Tiles and Paints took price hikes in Q2 FY 2019, the Airlines sector continued to witness pricing pressure (as reflected by subdued trend in in ticketing yields) because of intense competition within the sector.

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