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INDIAN CORPORATE SECTOR

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

Contacts:

Subrata Ray
+91 22 6169 3385
subrata@icraindia.com

Shamsher Dewan
+91 124 4545 328
shamsherd@icraindia.com

Sreejan Dutta
+91 124 4545 396
sreejan.dutta@icraindia.com

Jay Sheth
+91 22 6114 3419
jay.sheth@icraindia.com

Quarterly Update

The Indian Corporate Sector showed strong revenue growth in Q3 FY2019 driven by stable demand from consumer-oriented sectors and robust growth in commodity prices

However, EBIDTA margins declined by 75 bps on a YoY basis because of rise in raw material and energy cost and adverse impact of rupee depreciation

The adverse impact of sharp rupee depreciation and high fuel prices is expected to moderate in Q4 FY2019

Q3 FY 2019 results indicate healthy revenue growth but compression in profit margins

The Q3 FY2019 financial results released by 648 companies in the Indian Corporate Sector shows revenue growth of 17.3% on a YoY basis driven by robust growth in commodity-linked sectors on back of rising commodity prices, strong revenue growth in the IT sector and stable consumer demand. Commodity linked sectors such as **Oil & Gas, Iron & Steel and Cement** posted 27% revenue growth on a YoY basis, supported by higher oil and steel prices as well as healthy demand for cement. Excluding commodities, revenue growth for rest of the sample was 13.3% YoY, which is similar to the growth in Q2 FY2019. The IT sector reported a strong growth of 18.2% in rupee terms supported by scale-up in digital offerings, appreciation of US Dollar vis-a-vis INR and pickup in demand from BFSI clients. In US Dollar terms, the revenue growth for IT companies stood at 8.3% on a YoY basis. In the consumer-oriented sectors, the trends were a mixed-bag. For instance, the whole sale dispatch of Passenger Vehicle declined by 0.8% in Q3 FY2019 on a YoY basis because of high base and weak customer sentiments, partly contributed by rising ownership costs (Fuel, EMIs and Insurance). The 2W segment sales registered a growth of 8.4% in Q3 driven healthy motorcycle sales growth of 11.2%. Except for the automobile sector, other consumer linked sectors saw stable consumer demand, as reflected in the healthy volume growth in both FMCG and Consumer Durables segments.

While revenues grew at a healthy pace in Q3, the aggregate EBITDA margins declined by 75 bps on a YoY basis and 20 bps on QoQ basis to 16.4% because of rise in energy costs and increase in input costs. While sectors such as Airlines, Cement and Building Materials (Tiles & Glass) continued to report 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

Although the INR strengthened in Q3 FY2019 on a sequential basis, the average USD to INR exchange rate was Rs. 72.09 as compared to Rs. 70.03 in Q2 FY2019 and Rs. 64.74 in Q3 FY2018. As a result, companies in sectors like Auto OEMs, Airlines, Consumer Durables and Paints that have sizeable imports witnessed contraction in EBITDA margins during Q3. Besides INR depreciation, heightened fuel costs in October and November also put pressure on energy intensive sectors such as Cement, Airlines and Tiles & Ceramics. However, some positive trends emerged in latter half of Q3 FY2019 such as decline in global crude oil prices, significant jump in airline ticketing yield and price hikes in sectors such as cement and consumer durables, which led to a sequential improvement in the EBITDA margins of some sectors such as airlines, tiles & ceramics and cement.

CORPORATE OFFICE
Building No. 8, 2nd Floor, Tower A; DLF Cyber City, Phase II; Gurgaon 122 002
Tel: +91 124 4545300; Fax: +91 124 4545350
Email: info@icraindia.com, Website: www.icra.in

REGISTERED OFFICE
1105, Kailash Building, 11th Floor; 26 Kasturba Gandhi Marg; New Delhi 110001
Tel: +91 11 23357940-50; Fax: +91 11 23357014

Branches: **Mumbai**: Tel.: + (91 22) 24331046/53/62/74/86/87, Fax: + (91 22) 2433 1390 **Chennai**: Tel + (91 44) 2434 0043/9659/8080, 2433 0724/ 3293/3294, Fax + (91 44) 2434 3663 **Kolkata**: Tel + (91 33) 2287 8839 /2287 6617/ 2283 1411/ 2280 0008, Fax + (91 33) 2287 0728 **Bangalore**: Tel + (91 80) 2559 7401/4049 Fax + (91 80) 559 4065 **Ahmedabad**: Tel + (91 79) 2658 4924/5049/2008, Fax + (91 79) 2658 4924 **Hyderabad**: Tel +(91 40) 2373 5061/7251, Fax + (91 40) 2373 5152 **Pune**: Tel + (91 20) 2552 0194/95/96, Fax + (91 20) 553 9231