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Indian Corporate Sector: Q1 FY2020 Performance Review and Outlook

September 2019

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Financial Performance of the Indian Corporate Sector in Q1 FY 2020

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Summary

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Macroeconomic headwinds impacted Revenue growth of India Inc. during Q1 FY2020

The Q1 FY2020 financial results of 642 companies in the Indian Corporate Sector showed continued weakening in the revenue growth to 5.7% from 9.3% in the sequential previous quarter and 22.4% in the year-ago period. The revenue growth slowdown has been primarily driven by the weak consumer sentiment, which was reflected in sequential contraction of 7.7% in revenues from consumer-oriented sectors. Automobiles sales reported sharp double-digit decline, which has continued into the current quarter as well, while FMCG companies reported a sequential slowdown in volume growth in both rural and urban markets. Among the various consumer-oriented sectors, companies in the Consumer Durables sector reported revenue growth during the quarter on the back of sales of cooling products. Overall, revenues from consumer-oriented companies in ICRA's sample were flat on a YoY basis but contracted by 7.7% sequentially.

The revenues of commodity-linked sectors in ICRA's sample grew by 6.2% on a YoY basis during Q1 FY2020, driven primarily by higher realisations for Oil and Gas entities (on a YoY basis), while sectors like Metals & Mining and Iron & Steel reported a contraction in revenues on account of tepid realisations. On a sequential basis, the softening of commodity prices led to contraction of 3.3% in revenues from commodity-linked sectors during Q1 FY2020. Among other sectors, the IT sector reported strong revenue growth of 10.0% in Q1 FY2020 (in INR terms) supported by rupee depreciation on a YoY basis and traction in digital offerings across verticals. Additionally, sectors like Power, Pharmaceuticals and Telecom supported revenue growth to an extent.

ICRA expects weakening demand, higher discounting, lower realization in select commodity sectors, especially metals, and impact of negative operating leverage to have had a negative impact on the profitability of India Inc. during Q1 FY2020, as reflected in YoY PBT margin contraction of 114 bps. However, this was not visible in the EBITDA margin trend, with aggregate EBITDA margin for ICRA's sample improving by 136 bps on sequential and was flat on YoY basis at 17.7%, possibly due to the impact of Ind AS 116 adjustment, wherein operating leases have been capitalized by companies, thereby reducing rental costs and increasing depreciation and interest outgo. Sectors like aviation and retail, which have significant reliance on operating leases, reported a sharp improvement in EBITDA margins due to this.

Summary

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Continued weak consumer sentiments likely to keep Q2 FY2020 financial performance also subdued

Given the weak macroeconomic environment and the continued subdued demand sentiment, partly contributed by the tight liquidity situation, the performance of the Indian Corporate sector is expected to remain muted in Q2 FY2020 as well. Consumer demand sentiment continues to remain weak, both in rural and urban sectors, with the liquidity situation yet to ease out. The late onset of the monsoons and the unfavorable spatial and temporal distribution of rains, which led to flooding in multiple states, is also likely to keep the rural demand sentiment subdued over the near term.

The continued muted demand situation was visible in the decline of 5% in retail two-wheeler sales, and 9% in retail passenger vehicle sales in August 2019, and YTD decline of 5% and 3% for two-wheelers and passenger vehicle retails till August 2019. While the Government has recently announced measures for easing the liquidity situation and supporting certain industries, including automobiles, the on-ground impact of these remain to be seen.

During Q1 FY2020, cement volume growth slowed down to 1.8% due to slowdown in project execution on account of general elections, economic slowdown impacting private sector capex, as well as liquidity issues and labour scarcity. Steel consumption on the other hand, grew by 7% during the quarter on a YoY basis. Along with revival in consumer demand sentiment, pickup in infrastructure projects and execution remains critical for the overall recovery in the Indian Corporate sector.

Although the muted consumer sentiments will have an adverse impact on the revenue growth, factors such as benign commodity prices (steel, sugar and some other non-ferrous metals) will support profitability indicators to some extent. However, the profitability indicators could come under pressure if the global oil prices continue upward trajectory.

Summary

Revenue growth continued to disappoint in Q1 FY2020

Revenue growth

5.7%

Revenue Growth

Weak start to the fiscal with the growth momentum significantly moderating from the double-digit levels reported in Q1 FY2019

Weak consumer demand

Prices for some commodities declined on a QoQ basis

7.7%

Decline in revenues from consumer sectors on a QoQ basis

The revenues from consumer-oriented sectors declined by 7.7% on a QoQ basis with the weak consumer sentiment, both in rural and urban regions

Change in margins*

26 bps

Improvement in PBT margins on QoQ basis

Soft commodity prices and fuel prices, and favourable movement of INR against the USD on sequential basis helped improvement in margins on QoQ basis

114 bps

Contraction in PBT margins on YoY basis

Weakening demand, lower realisation in select commodity sectors, heavy discounting and negative operating leverage impacted profitability on YoY basis

**PBT Margins strictly not comparable with previous quarters due to IndAS 116 adjustment*

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Thank You!