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Q4 FY’19 EARNINGS UPDATE
Q4 FY 19 Earnings: Slowdown in Sales Momentum after 3 strong Quarters

Sales growth for the BSE200 was dragged by Commodities like Metals and Oil & Gas.

Weak auto sales are well known and this has raised concerns on a broad consumer slowdown. Auto companies all missed volume growth estimates across segments. They were also plagued with high channel inventory.

Staples companies had weak-to-in-line volume growth. Companies attributed the same partly to the low availability of financing at their channel partners following the NBFC issues, which have dragged on. On the demand side, staples companies said that conditions worsened from Jan-Feb to Mar-Apr, partly as rural consumers have seen a softening.

Consumer discretionary, more so linked with urban consumer, seems to be less impacted as yet. Part of this can be attributed to rising formalization in these sectors. Seasonal demand items like coolers and air-conditioners saw robust demand on account of hot summer.
Q4 FY 19 Earnings: EBITDA growth tepid dragged by Auto

- EBITDA Growth slowed after 6 strong quarters of double digit growth
- At the EBITDA level, BSE200 growth remained tepid at 10%; strong delivery by cement, industrials and metals; FMCG, pharma were muted; Auto contracted
- For Q3 FY19, headline EBITDA grew 3%, mainly dragged down by inventory losses in PSU Oil Marketing Companies. Ex of these companies, EBITDA growth was 13% YoY
Low base and lower provisions by Corporate Banks push up profitability

Reversal in Corporate Banks profitability resulted in 44% YoY growth in BSE200 PAT, boosted by a low base effect.

Ex Financials PAT grew only 5% - dragged by Auto & Pharma

Industrials and Metals continued their strong performance whereas Cement saw a sharp uptick in profits on account of price hikes.
Q4 FY 19 Earnings: Sectoral Trends

Positives

• Though corporate banks (viz, ICICI, Axis and SBI) earnings somewhat disappointed for 4Q, the miss was largely on account of improved coverage ratios. Slippages moderated and FY20 earnings were actually upgraded.
• Industrials, especially construction companies continued to report robust numbers and order books.
• Consumer discretionary, more so linked with urban consumer, seems to be less impacted as yet. Part of this can be attributed to rising formalization in these sectors.
• Cement companies finally started seeing some realization improvement, which has resulted in upgrades of 2-5% for reporting companies.

Negatives

• Weak auto sales are well known and this has raised concerns on a broad consumer slowdown. Auto companies had a weak quarter, as weak volumes and high inventory led to higher discount. Margins saw a 1-5ppt hit, driving downgrades across the board.
• Staples companies had weak-to-in-line volume growth. On the demand side, staples companies said that conditions worsened from Jan-Feb to Mar-Apr, partly as rural consumers have seen a softening.
• Three of the four large IT companies, viz, TCS, Infosys and HCLT, gave growth guidance/outlooks implying c.9-10% revenue growth in FY20. Margin outlook is weaker on account of INR appreciation, higher employee costs and supply pressures in the US.
Q4 FY 19 Stable Sectors: slowdown visible in topline led by Autos

**Stable Segment Sales Gr YoY, ex Financials**

**Stable Segment EBITDA Gr YoY, ex Financials**

**Stable Segment PAT Gr YoY, ex Financials**

**Stable Segment PAT Gr YoY, incl Financials**

**Stable Sectors:** Auto, Retail Banks, NBFC, Consumer Staples, Consumer Discretionary, IT Services, Healthcare / Pharma
Q4 FY 19 Cyclical Segment: Corporate Banks boost profitability

Cyclical Sectors: Cement/Building Material, Corp Banks, Industrials (including CVs), Utilities, Telecom, Commodities (Metals/Oil & Gas etc)
FY19 EARNINGS
FY 19 Earnings: Sales Growth Robust

• Notwithstanding the slowdown in Q4, FY 19 Sales growth was a robust 18% - highest in last 6 years.

• Energy, Industrials, Cement and Consumer Discretionary reported highest sales growth

• Auto, Staples and Telecom recorded single digit sales growth
FY 19 Earnings: EBITDA Growth in line with Sales Growth

- All sectors except Auto, Telecom and Utilities reported EBITDA growth in the ‘teens’
- EBITDA Growth highest in least 5 years
- 7 of 11 sectors witnessed stable to rising margins
FY 19 Earnings: Corporate Banks drive PAT growth

- Lower provisioning in Corp Banks as compared to FY18 drove PAT growth for BSE200
- Industrials, Commodities and Cement were the other key outperformers
FY 19 Earnings: Stable Segments record stable low double digit growth

Stable Segment Sales Gr YoY, ex Financials

- Mar-14: 26%
- Mar-15: 11%
- Mar-16: 18%
- Mar-17: 9%
- Mar-18: 4%
- Mar-19: 14%

Stable Segment EBITDA Gr YoY, ex Financials

- Mar-14: 26%
- Mar-15: 11%
- Mar-16: 18%
- Mar-17: 9%
- Mar-18: 4%
- Mar-19: 14%

Stable Segment PAT Gr YoY, ex Financials

- Mar-14: 26%
- Mar-15: 11%
- Mar-16: 18%
- Mar-17: 9%
- Mar-18: 10%

Stable Segment PAT Gr YoY, incl Financials

- Mar-14: 25%
- Mar-15: 12%
- Mar-16: 19%
- Mar-17: 15%
- Mar-18: 11%
- Mar-19: 11%
FY 19 Earnings: Cyclical segment saw sharp rebound

Cyclical Segment Sales Gr YoY, ex Financials

Cyclical Segment EBITDA Gr YoY, ex Financials

Cyclical Segment PAT Gr YoY, ex Financials

Cyclical Segment PAT Gr YoY, incl Financials
Corporate banks – Key Earnings growth driver for FY 20-21

Corporate Bank profitability has fallen from 13-14% of BSE200 PAT to -5%, a 18% swing. Recovery in these is the key to any forward estimates.

Consensus estimates expect normalization of Corp Bank profits in FY 20 and 21.

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- Even for PSU Corporate Banks, the trend in slippages has improved, though a few banks like PNB reported elevated slippages.
- However, healthy recoveries and write-offs enabled a decline in GNPA/NNPA ratios.
Infra and Capital Goods - key earnings growth driver for FY 20-21

- Industrials which includes both Capital Goods and Infra saw a robust Sales, EBITDA and PAT growth of 13%, 18% and 25% respectively.
- FY 19 Sales, EBITDA and PAT for this segment grew 18%, 20% and 35% respectively.
- Most players performed well with timely execution of projects, especially on the domestic front.
- But order inflows declined impacted by weakness witnessed in domestic ordering due to the general elections.
- Management commentary suggests small and medium-sized orders are flowing in; however, large ticket orders are on hold and should see finalization post elections.
Q4 FY 19 Earnings: Key Takeaways

- Fears of consumer slowdown and more misses than hits notwithstanding, the earnings cuts have been benign.

- There are some signs of consumer slowdown, but these are uneven in severity.

- Most of the bad news seems to be concentrated in Autos and staples results, with rural demand and liquidity issues taking most of the blame.

- Urban discretionary hasn’t slowed as much, though is trending weaker.

- Industrials and corporate banks seem to be well set on the earnings recovery path and the latter remain critical to the 20%+ Nifty earnings growth forecast for FY20.
• In FY 19, despite outperforming Stable segment in terms of Sales & PAT growth, Cyclical sectors saw a significant de-rating and underperformance in terms of stock performance.

• Even for FY 19-21, as per consensus estimate, Cyclical segment is expected to lead the earnings growth, driven by Corporate Banks.

• Despite the recent run up in Small Caps, Small Caps (-16.4% YoY) and Mid Caps (-5% YoY) have significantly underperformed the NIFTY (+11.1% YoY) in the last year and are trading at cheaper valuations relative to NIFTY.

• This is in marked contrast to the position in Jan-18 when the NIFTY was trading significantly cheaper to the mid and small cap indices.

• Of the various factors needed for Cyclical and Mid and small Cap outperformance, quite a few are in favour namely – favourable valuations, crude prices closer to $60, yields below 7% and last but not the least a stable government at the center.

• Improvement in domestic and global growth outlook can be a key trigger for the broader markets going forward though the NIFTY may not see a significant uptick.
Why Mid & Small cap?

**Positive PE Ratio**

- Dec-17:
  - NIFTY Index: 22.0
  - NSE Mid: 28.1
  - NSE Small: 20.4

- 31-May-19:
  - NIFTY Index: 23.8
  - NSE Mid: 17.4
  - NSE Small: 17.5

**1Yr Fwd PE Ratio**

- Dec-17:
  - NIFTY Index: 17.8
  - NSE Mid: 23.1
  - NSE Small: 17.3

- 31-May-19:
  - NIFTY Index: 18.3
  - NSE Mid: 15.3
  - NSE Small: 14.4

**Returns from Jan’18**

- NIFTY Index: 14.3%
- NSE Mid: -14.9%
- NSE Small: -28.7%
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