

Good growth, average margins

Barring banks, India Inc's showing in Q4 is encouraging

The bad news from the 720 companies that have declared their March 2018 quarterly results so far is that net profit has dropped 34 per cent, which is the worst quarterly performance in at least three years. But the good news is that if financials and energy are removed, net profit growth is 15 per cent — the best since the September 2016 quarter. This should not come as a surprise because several public sector banks (PSBs) have posted record losses thanks to higher provisioning for non-performing assets (NPAs). With the revenue growth of the 720 companies at 13.9 per cent, it is the second-best quarter in at least three years as the pressures of demonetisation and the goods and services tax (GST) have eased. Companies focused on the domestic market have seen their revenue grow 10 per cent. For this set of companies, which are less affected by global prices of products and services, combined net profit growth is an impressive 18.4 per cent year-on-year (YoY). There is some benefit of a low base effect as earnings were down 4.6 per cent during the corresponding quarter in the last fiscal year after the note ban.

The story on the margins front is, however, less impressive. Operating profit margins are the worst in 12 quarters after the March 2017 quarter as companies have not been able to pass on higher metal and energy prices to consumers. For domestic companies, the core operating margin is down 300 basis points to 16.6 per cent from the highs in June 2016. Revenues of every ₹100 cost raw materials of ₹35 in Q4, the highest in the last four years. The blow from higher input cost, however, has been cushioned by a steady fall in labour cost, which has accounted for just 6.8 per cent of net sales during the fourth quarter, the lowest in the last eight quarters.

For banks (State Bank of India is yet to announce its results), it has been the worst quarter with 23 banks in the sample reporting a combined loss of ₹262 billion during the fourth quarter. This is largely due to 11 of the 13 PSBs reporting losses in the quarter. Banks' interest income is up 5.3 per cent YoY, growing at the slowest pace in the last five quarters, mirroring poor growth in industrial credit. Retail banks and non-banking financial services companies have, however, reported solid performance. The information technology sector continues to face headwinds with the industry's net profit growing 0.2 per cent during the quarter, down from 6.5 per cent during the third quarter and 8.8 per cent a year ago, though sales growth at 5.5 per cent is the fastest in the last four quarters.

While the current sample of companies is not complete, it is a good representation of most sectors and provides a reasonably good picture of how India Inc has performed. However, the sustainability of higher profit growth remains a concern unless companies are able to improve margins by passing on higher raw material prices. With the recent rise in crude oil prices and a slowdown in industrial production after a good start in the current calendar year, it's not going to be easy.