ICRA

Monthly Research Compendium

July 2023

Monthly Research Compendium

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Research Compendium is a compilation of some of ICRA's key research reports released in the previous month.

The ICRA Research compendium offers a summary of some of the most thought-provoking research reports published during the month

Each slide communicates key excerpts from the respective reports through charts and tables

Follow the link in the caption of each slide to access the detailed report on ICRA's website

Summary

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Auto Components: Industry benefits from operating leverage in Q4 FY2023; however, upside limited as export outlook remains weak

Banking: Bank bond issuances to decline below Rs. 900 billion in FY2024 after touching all-time high in FY2023

Chemicals – Agrochemicals: Demand pressures and inventory destocking to weigh on agrochemical industry performance

Cross Sectoral Trends and Outlook: Waiving of ISTS charges to cut LCOH by 15-20%, saving up to Rs 0.3 trillion pa

Economy: Merchandise trade deficit rose to five-month high in May 2023; CAD likely to widen to $10-12 billion in Q1 FY2024

Fashion Retail: Underperforming value segment to decelerate fashion retailers' revenue growth to 10% and affect profit margins by ~100 bps in FY2024

Ferrous Metals: Steep rally in carbon prices and CBAM compliance requirements could pull down the profits of Indian steel exports to EU

Gas Utilities: China's shift towards use of coal and Russian piped gas leads to easing of global LNG market

Hospital: ICRA's channel check indicates mid-teens revenue growth and stable margins for the industry in FY2024

NBFC: Guidelines on default loss guarantee further clear the air around digital lending

Summary

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Power Distribution: Rising costs and modest tariff hikes stifle discoms; multiple reforms in progress

Roads: Project awards may decline to 9,000-9,500 km in FY2024, ahead of the General Elections

Real estate – Retail Mall: Rental income to increase by 8-10% YoY in FY2024 for mall operators

Refining & Marketing: Significant improvement in marketing margins for OMCs

Securities Broking: Margin trading facility volume steady even as cash market turnover subsides

Auto Components: Industry benefits from operating leverage in Q4 FY2023; however, upside limited as exports outlook remains weak

Auto Components Outlook - Stable

Exhibit : Sample of companies which witnessed improvement in operating margins in Q4 FY2023, on QoQ basis

	Revenues	OPBDITA (%)	
Company Name	**Growth (%)**	**Q3 FY2023**	**Q4 FY2023**
JTEKT	↑↑	9.0%	9.5%↑
Samvardhana Motherson International	↑↑	7.8%	9.0%↑
Varroc	↓	7.5%	8.9%↑
Endurance	↑	11.4%	12.8%↑
Bosch	↑↑	11.0%	12.9%↑
Sundaram Fasteners	↑	14.0%	15.7%↑

Exhibit : Sample of companies which witnessed decline in operating margins in Q4 FY2023, on QoQ basis

	Revenues	OPBDITA (%)	
Company Name	**Growth (%)**	**Q3 FY2023**	**Q4 FY2023**
Exide Industries	↑	11.8%	10.4↓
Gabriel India	↑	7.2%	7.1%↑
Automotive Axles	↑	11.9%	11.2%↓
JBM Auto	↑	11.1%	10.6%↓
Lumax Industries	↑	9.6%	8.0%↓
LG Balakrishnan & Bros	↓↓	18.4%	17.1%↓

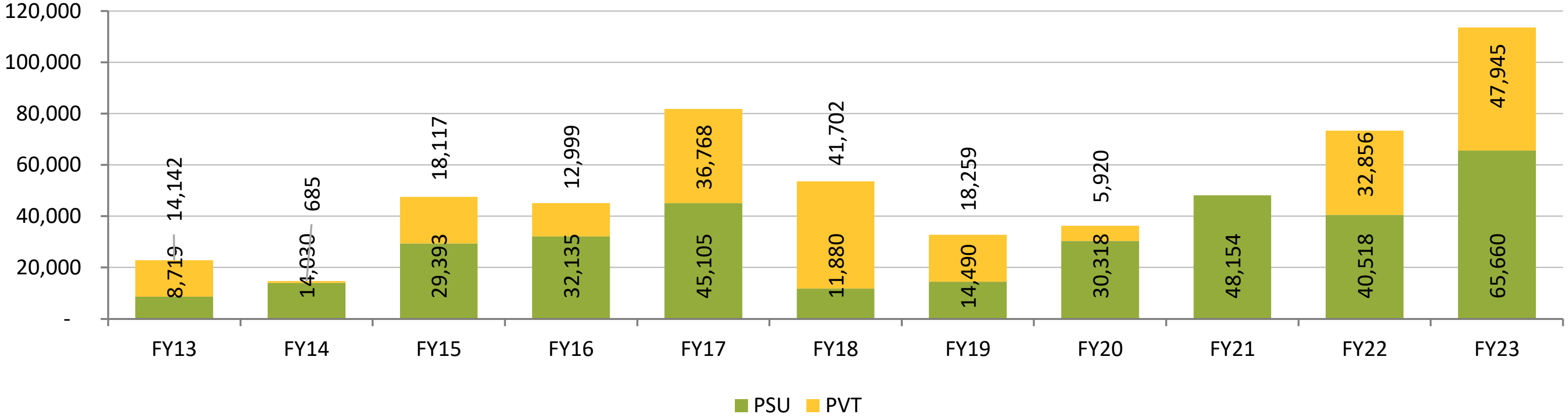
- While 66% of the entities have reported QoQ margin improvement, benefitting from the operating leverage, 33% have reported QoQ decline, impacted by specific challenge on product mix, inventory provisioning, air freighting etc.
- Despite increase in volumes and softening of cost inflationary pressures, margins for the sample remained range-bound at ~10.5-11% in Q3 and Q4 FY2023. The margins were impacted by unfavourable product mix and sub-optimal capacity utilisation as export demand weakened

Source: ICRA Research, Ace Equity. ↑: Increase in expense as % of OI or single-digit revenue growth; ↓: Decline in expense as % of OI or single-digit revenue decline; ↓↓: Double digit decline in revenues or >400 bps fall in margins, ↑↑ Double digit growth in revenues or >400 bps increase in margins

Banking: Bank bond issuances to decline below Rs. 900 billion in FY2024 after touching all-time high in FY2023

Banking Outlook - Positive

Exhibit: Total bond issuances by banks (Rs Crore)



Bond issuances likely to decline below Rs. 900 billion in FY2024

- Credit-deposit gap likely to persist in FY2024 as well, which banks will seek to bridge by issuing bonds.
- Refinance from SIDBI/NABARD and certificates of deposit to remain alternative sources of funding.
- Certificates of deposit outstanding increased to Rs. 3.0 trillion on May 19, 2023 from Rs. 1.9 trillion last year (May 20, 2022).
- Bank bond issuances to remain below Rs. 900 billion in FY2024 after hitting all-time high of Rs. 1.1 trillion in FY2023
- Lower issuances likely to be seen, mainly in Tier-I and Tier-II cities in FY2024.

Source: AIMIN, ICRA Research, SIDBI: Small Industries Development Bank of India, NABARD: National Bank for Agriculture and Rural Development

Chemicals – Agrochemicals: Demand pressures and inventory destocking to weigh on agrochemical industry performance

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Chemicals Outlook - Stable

Exhibit: Prices – Corn, soyabean and wheat (in $/MT)

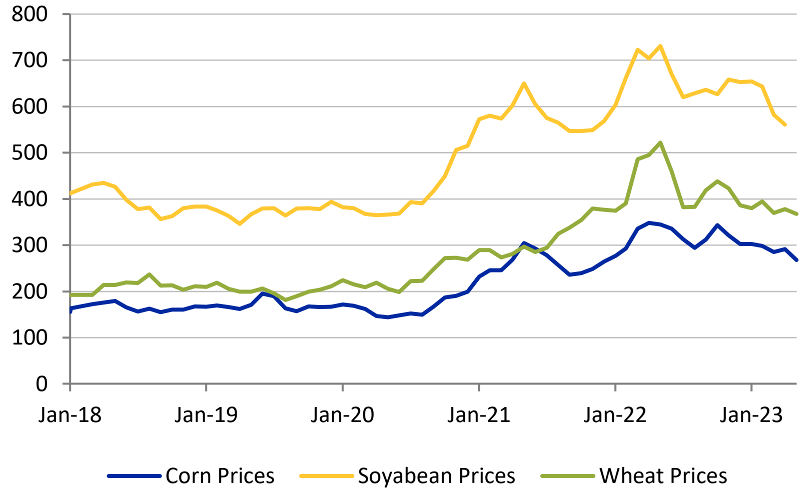
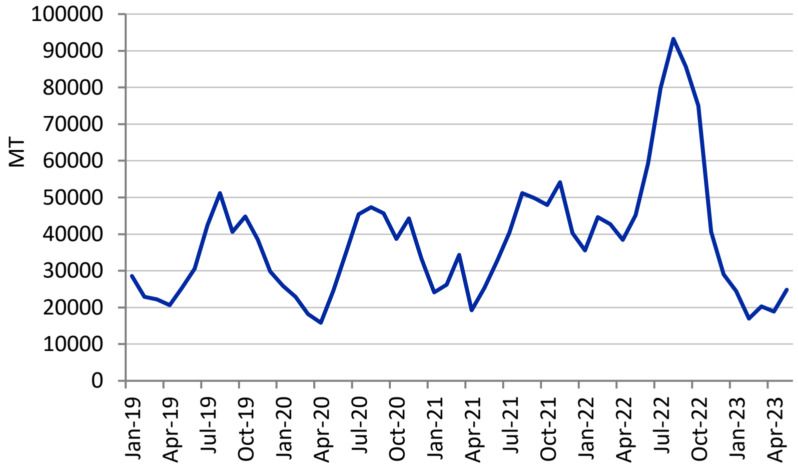


Exhibit: Pesticides import by Brazil (in MT)



- Multi-decade high crop prices had led to strong demand for agrochemicals in CY2022. It also led to a significant build-up of systemic inventory in key geographies like Brazil and the US. However, softening of crop prices and uncertain weather forecasts owing to El-Nino phenomenon led to a decline in agrochemical demand.
- Additionally, inventory destocking in key economies has led to a steep decline in demand, as was seen in Brazil. Profitability of agrochemical players to moderate with weakening demand, increasing supply from China and softening crop prices across the globe.

Source: IMF; World Bank, Govt of Brazil, Bloomberg; ICRA Research

Cross Sectoral Trends and Outlook: Waiving of ISTS charges to cut LCOH by 15-20%, saving up to Rs 0.3 trillion pa

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- In February 2023, the GoI extended the waiver of Inter-State Transmission System (ISTS) charges for renewable power to hydrogen-manufacturing plants. This initiative will help reduce the LCOH*.
- LCOH per kg of Green Hydrogen stands at $4-5 per kg currently through electrolysis method.

Exhibit: LCOH for per kg of Green Hydrogen

	~LCOH ($/kg)	~LCOH (Rs/kg)
Capex	0.6	45-50
Opex	0.2	15-20
Electricity & ISTS	2.5	200-205
Others	0.8	60-65
Total cost	**4-5**	**350-400**

Electricity and ISTS charges form 50-60% of LCOH

Electricity units needed per kg of Green Hydrogen	~60 kwh
ISTS charges	@ ~Rs 1
Savings with ISTS waiver	~Rs 60

- Waiver of ISTS charges is expected to cut the cost of Green Hydrogen by 15-20%.
- National Green Hydrogen Mission has a target of 5 MMT by 2030. The waiver can save up to Rs 0.3 trillion pa.

*Source: Niti Aayog, Press Information Bureau (PIB), Department for Business, Energy & Industrial strategy, UK Government Publications, Industry, ICRA Research Note: * The levelised cost of hydrogen (LCOH) is the discounted lifetime cost of building and operating a production asset, expressed as a cost per energy unit of hydrogen produced, covers all relevant costs, capital, operating, fuel and financing costs.*

Economy: Merchandise trade deficit rose to five-month high in May 2023; CAD likely to widen to $10-12 billion in Q1 FY2024

Exhibit: Trends in Merchandise Trade Balance- Aggregate

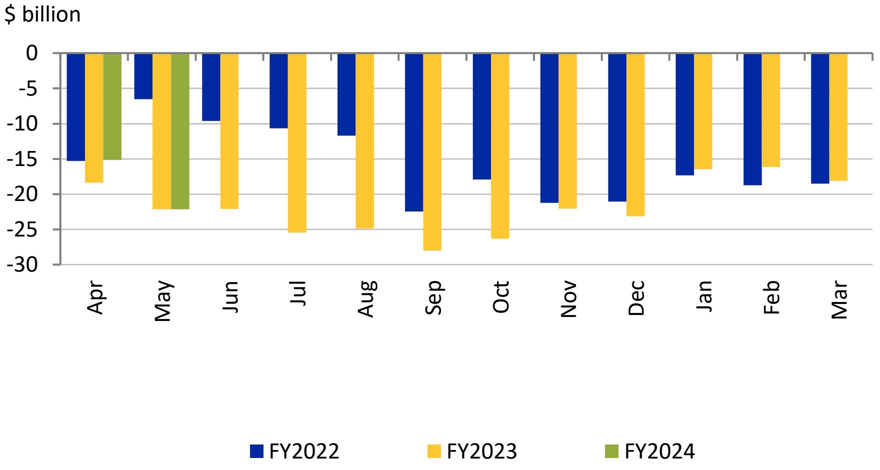
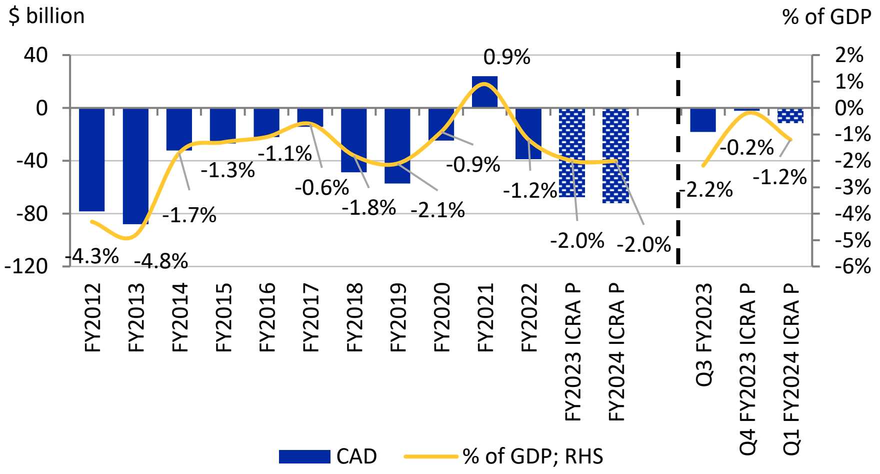


Exhibit: Trends in Current Account Deficit ($ billion; % of GDP)



- With a steeper sequential uptick in imports than exports, the merchandise trade deficit widened to a five-month high of $22.1 billion in May 2023 from $15.1 billion in April 2023, while remaining largely similar to the year-ago level.
- The available trade data for April-May 2023 suggest that the current account deficit (CAD) is likely to widen to ~$10-12 billion in Q1 FY2024 from ~$2 billion expected in Q4 FY2023, while remaining manageable at ~1.2% of the gross domestic product (GDP).

Source: Ministry of Commerce and Industry, GoI, RBI; CEIC; ICRA Research
**P: Projected; Data labels correspond to CAD as % of nominal GDP; ICRA's nominal GDP Proj. has been used for FY2023 and FY2024;*

Fashion Retail: Underperforming value segment to decelerate fashion retailers' revenue growth to 10% and affect profit margins by ~100 bps in FY2024

Exhibit: Movement in average sales per sq ft per month for value fashion segment

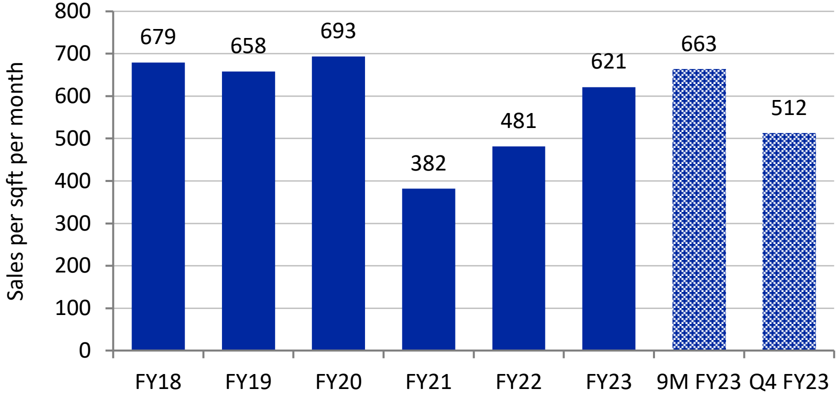
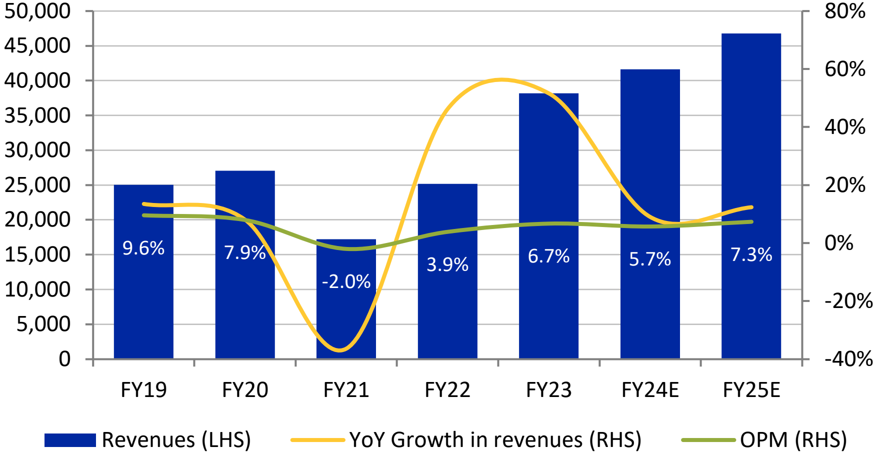


Exhibit: Movement in operating income and profits*



- Fashion retailers, especially with presence in the value fashion segment, have been witnessing a demand slowdown post the end of the festive season due to inflationary pressures. This pain is likely to be short-lived with the demand expected to revive from H2 FY2024 onwards, post the onset of the festive season.
- The OPM is expected to moderate by ~100 bps (after IndAS116 adjustments) in FY2024, given the moderation in revenue growth and continued high advertisement and promotions expenses. The same is expected to improve in FY2025 as benefits of operating leverage kicks in.

*Source: ICRA Research, *Numbers excluding the impact of Ind AS 116; aggregate of 11 listed platers in fashion industry*

Ferrous Metals: Steep rally in carbon prices and CBAM compliance requirements could pull down profits of Indian steel exports to EU

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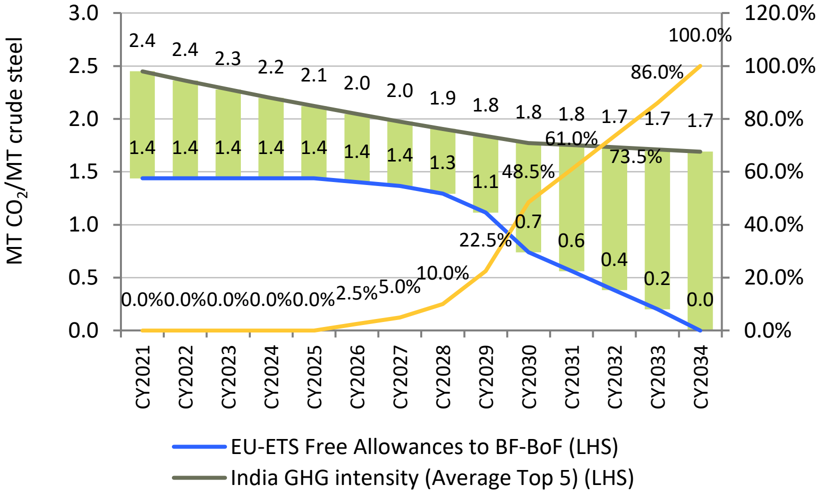
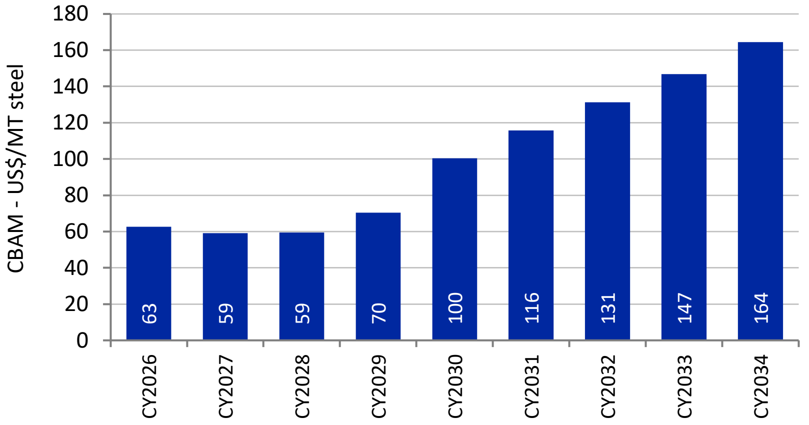
Ferrous Metals Outlook - Stable

Trend in EU-ETS free allowance for an EU steel mill vs. average GHG emission intensity (scope 1) of leading Indian players for the BF-BoF route of production



Estimated CBAM for Indian steel exports to the EU



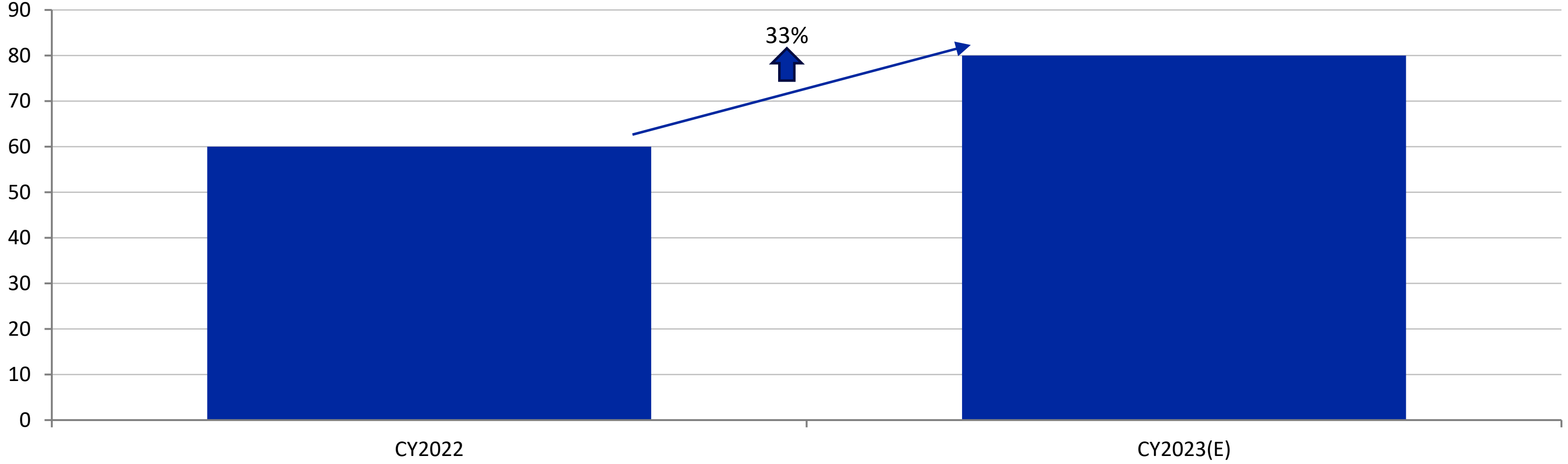
- After the end of the transition period ending December 31, 2025, the phasing-out of free allocation under the European Union's Emission Trading System (EU-ETS) will happen parallelly with the phasing-in of the Carbon Border Adjustment Mechanism (CBAM) over the subsequent eight years (CY2026-CY2034). The current EU-ETS free allocation benchmark for the BF-BoF route is significantly below the average scope 1 emission intensity of leading domestic BF-BoF based steelmakers.
- ICRA's analysis suggests that after relatively modest levels of CBAM incidence between CY2026 and CY2029, as the pace of phase-out of free allowances picks up thereafter, the incidence of CBAM is expected to significantly increase between CY2030 and CY2034.

Source: European Commission, Company announcements, ICRA Research; trajectory of reduction in GHG intensity for Indian mills estimated based on company guidance
**Indicates estimated impact on mill profits solely attributable to CBAM compliance, everything else remaining the same, price of carbon assumed constant at Euro 90/MT (US$ 97/MT)*

Gas Utilities: China's shift towards use of coal and Russian piped gas leads to easing of global LNG market

Gas Utilities Outlook - Stable

Exhibit: Imports of Russian piped gas into China via "The Power of Siberia" pipeline (in bcm)



- Domestic coal production in China has seen a growth of 4.2% as of May 2023, while coal imports increased by nearly 60% in Q1 CY2023, thereby increasing the share of coal in China's energy mix to 56.2% (first such increase in the last 10 years).
- Even the piped gas supply from Russia, via the 'Power of Siberia' pipeline, is expected to increase by nearly one-third in CY2023. This has led to a 6% decline in Chinese liquefied natural gas (LNG) imports, as of Q1 CY2023, and has aided in easing the global LNG demand-supply scenario.

Source: Industry; ICRA Research

Hospital: ICRA's channel check indicates mid-teens revenue growth and stable margins for the industry in FY2024

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Hospitals Outlook - Stable

Exhibit: Expected revenue growth in FY2024

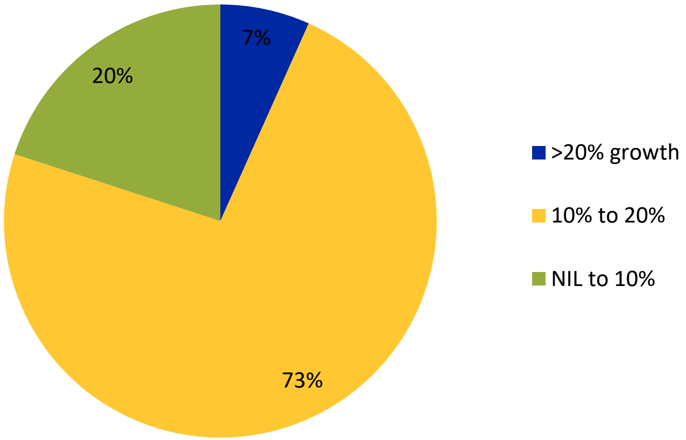
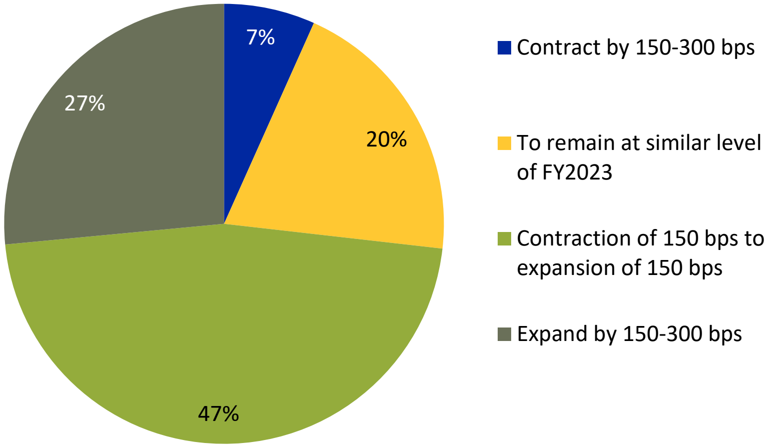


Exhibit: Expected OPM movement in FY2024 over FY2023



- Revenues of 73% of respondent hospitals grew more than 10% in FY2023, supported by strong occupancy and higher ARPOB levels. That said, 27% of the respondents reported revenue growth of less than 10%, given the high base, which included revenues from Covid treatment and vaccination drives in FY2022.
- Favourable specialty mix supporting ARPOB and continued benefit from cost optimisation measures aided 67% of the respondent hospital companies to report over 15% OPM in FY2023. Around 33% of the respondents reported less than 15% OPM, primarily due to moderate scale of operations.

Source: ICRA Research; survey responses from 15 hospital entities

NBFC: Guidelines on default loss guarantee further clear the air around digital lending

Guidelines are a positive from a risk-sharing perspective between REs and their LSPs in a digital lending transaction

LSPs, including non-REs, can extend DLGs. This is likely to boost fintech partnerships further

Clarity on cap, tenor, form and invocation of DLGs is a positive from operational perspective

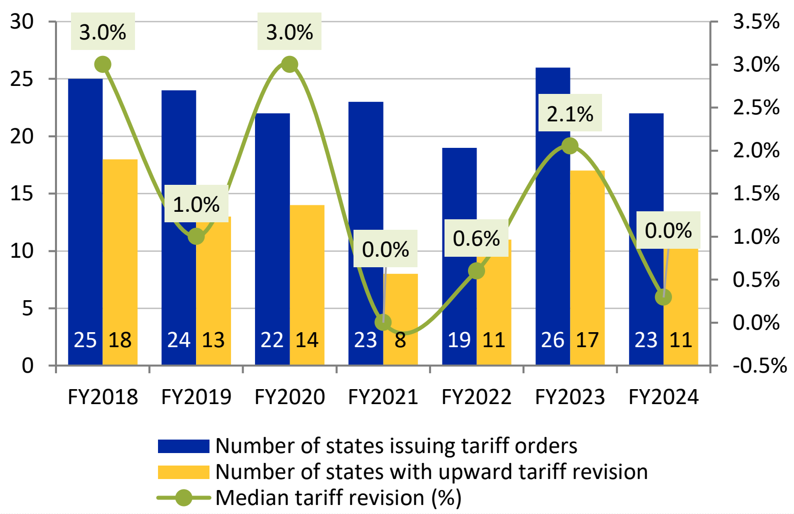
Increased due diligence and disclosure of DLG arrangements

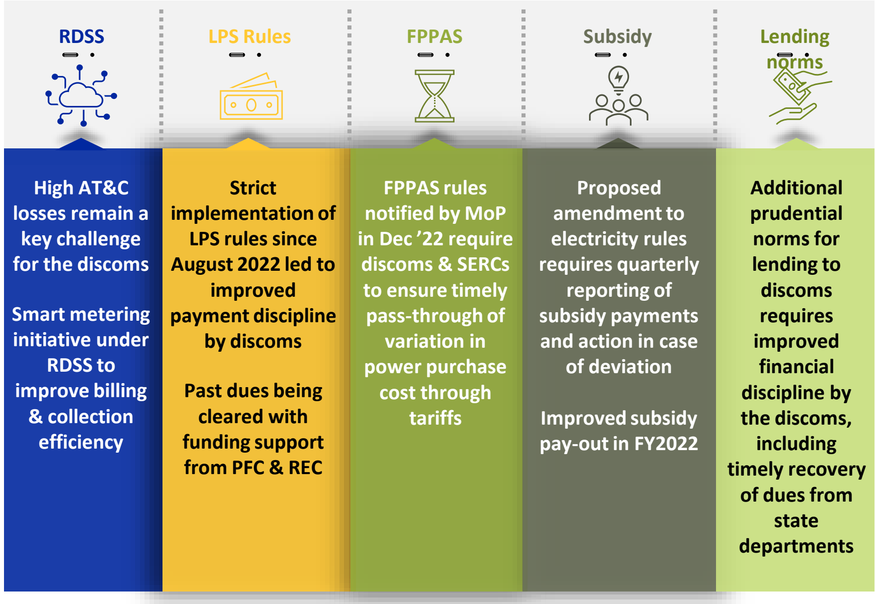
Source: ICRA Research

Power Distribution: Rising costs and modest tariff hikes stifle discoms; multiple reforms in progress

Power Distribution Outlook - Negative

Exhibit: Trends in tariff hikes approved for FY2024





- Progress in issuance of tariff orders for FY24 remains reasonable for state discoms with 23 of the 28 states issuing tariff orders thus far; however, the extent of the tariff hikes remains muted in relation to the rise in the cost of supply.
- Timely implementation of reform measures like FPPAS and smart metering remains key for a turnaround in discom performance.

Source: Tariff orders; ICRA Research

Roads: Project awards may decline to 9,000-9,500 km in FY2024, ahead of the General Elections

Roads Outlook - Stable

Exhibit: MoRTH yearly awards

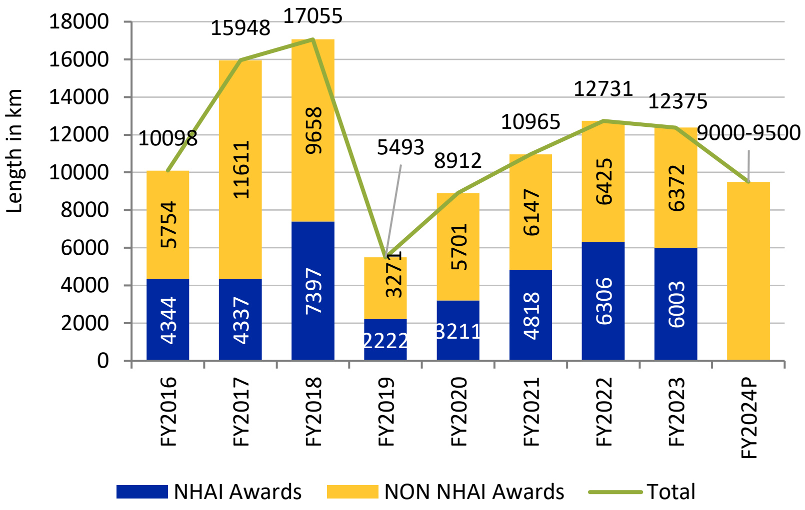
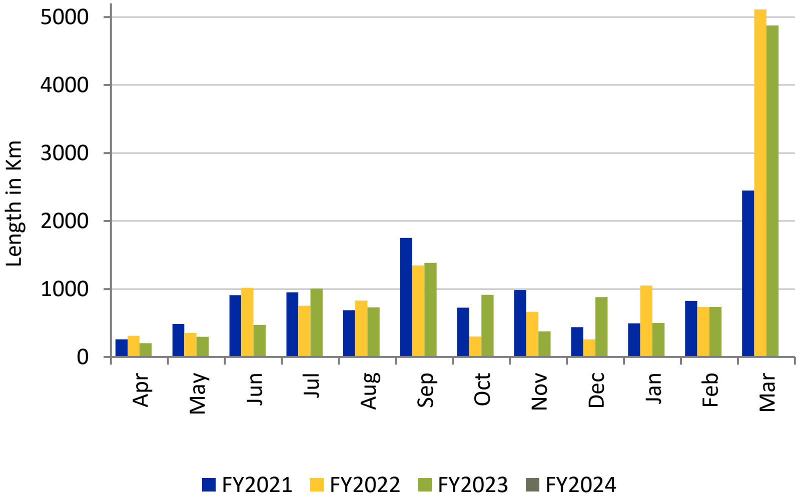


Exhibit: MoRTH monthly awards



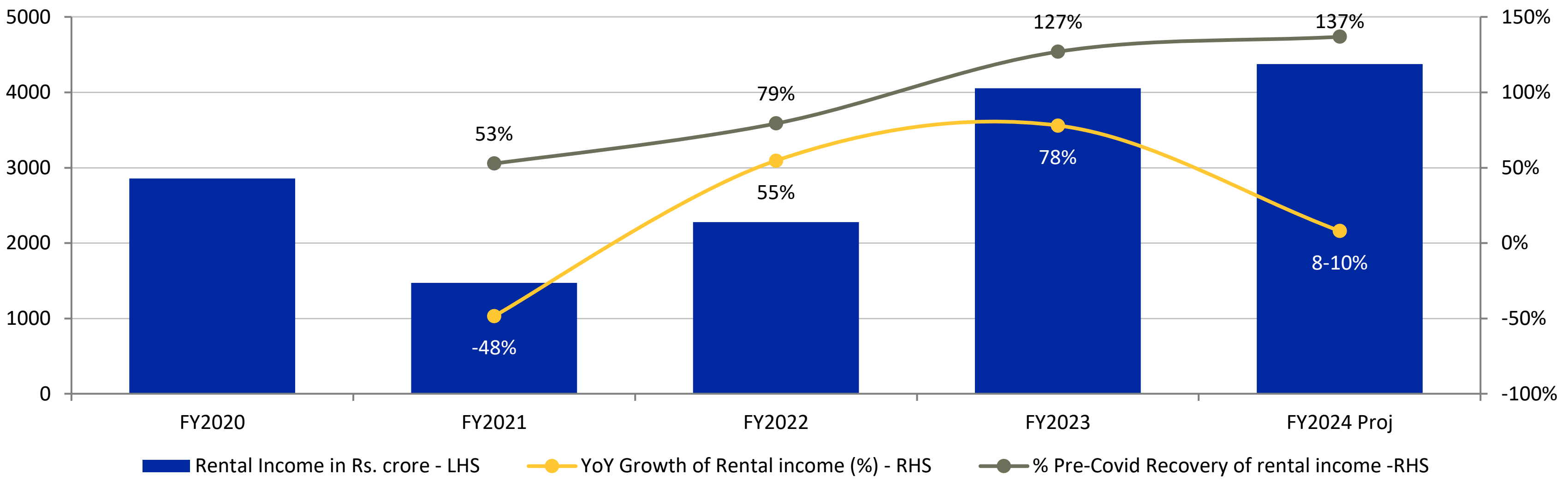
- The overall awards are expected to decline, owing to bidding activity slowing down before the General Elections, which are due around May 2024. Project awards are sizeable in the last quarter historically (49.4% and 54.2% of total projects for the year were awarded in Q4 FY2023 and Q4 FY2022, respectively).
- The overall awards of MoRTH declined marginally by 2.8% compared to FY2022, but remained healthy at 12,375 km during FY2023 against the backdrop of the Government's strong impetus to the road sector last year.

Source: ICRA Research, MoRTH, NHAI

Real estate – Retail Mall: Rental income to increase by 8-10% YoY in FY2024 for mall operators

Real estate Outlook - Stable

Exhibit: Trends in year-wise rentals for ICRA's sample



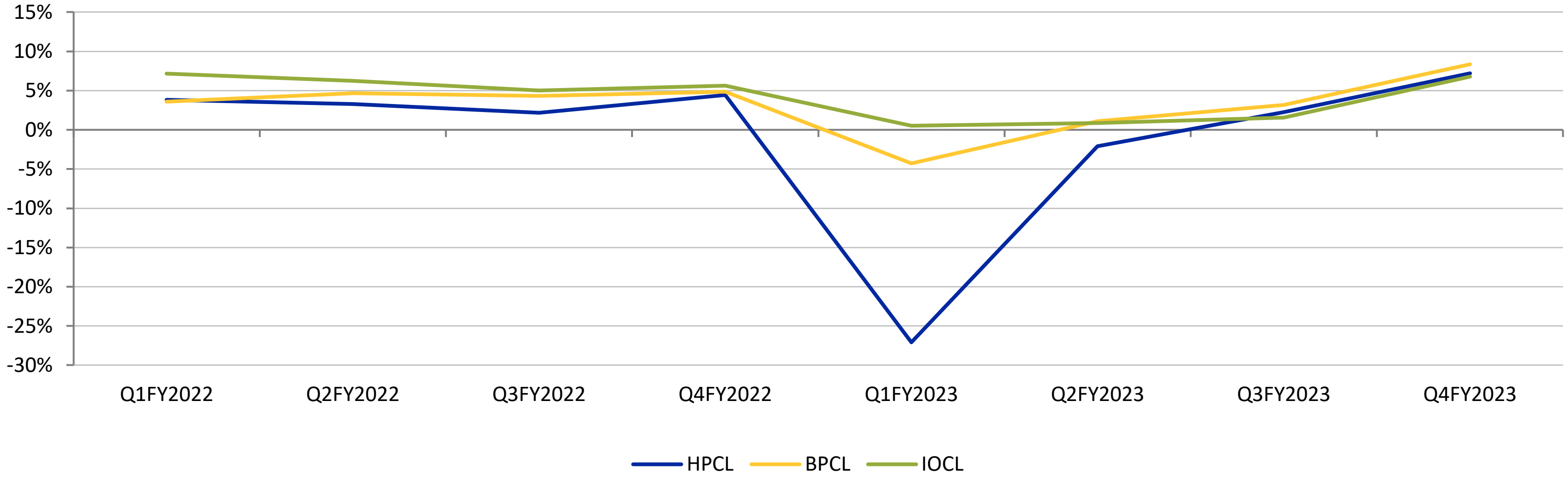
- In FY2024, the growth in rental income is expected to remain around 8-10% YoY, driven by contracted rental escalation and healthy retail sales, which is likely to improve the revenue share income.
- ICRA expects the credit profile of mall operators to remain stable, driven by healthy NOI, moderate leverage and healthy debt coverage metrics.

Source: ICRA Research, rental income including revenue share Pre-Covid Recovery of Rental income is on same base of FY2020 which includes 25 malls (Phoenix mills, Nexus malls and Lulu Kochi) totalling 16.6 msf across ten states. Rental income and Rental growth includes 38 malls totalling 25.4 million sft across twelve states. Cities include Delhi-NCR excluding Gurugram, Mumbai MMR, Bangalore, Hyderabad, Chennai and Pune

Refining & Marketing: Significant improvement in marketing margins for OMCs

Refining & Marketing Outlook - Stable

Exhibit : Quarterly operating margins trend



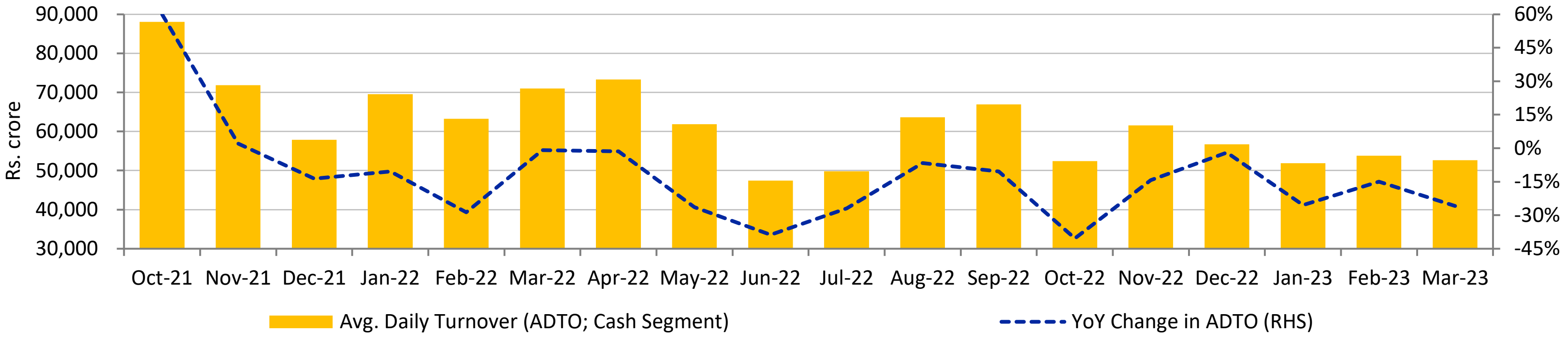
- The oil marketing company's (OMC) realisations were higher by Rs.13/litre for petrol and Rs.12/litre for diesel vis-à-vis international prices in May 2023. The retail selling prices have been on a freeze since May 2022. The improved marketing margins would help the OMCs recover the losses incurred in H1 FY2023.
- There is adequate headroom for downward fuel prices revision if the crude prices remain stable.

Source: Annual reports, ICRA Research, HPCL – Hindustan Petroleum Corporation Limited, BPCL – Bharat Petroleum Private Limited, IOCL – Indian Oil Corporation Limited

Securities Broking: Margin trading facility volume steady even as cash market turnover subsides

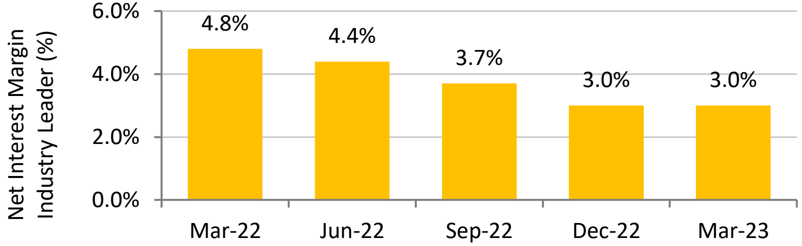
Securities Broking Outlook - Stable

Exhibit: Recent trend in ADTO in equity market's cash segment



- It has been empirically observed that cash volumes have a correlation with secondary market movements, with cash volumes increasing during a bull run.
- With rising systemic interest rates, money market borrowings became dearer for brokers. This, coupled with limited ability to pass on the hikes to customers due to high competition, brought the net interest margins under pressure in FY2023.

Exhibit: Net interest margin trajectory reported by industry leader



Source: SEBI.gov.in, bseindia.com, nseindia.com, www.ccilindia.com, ICICI Securities, ICRA Research

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Thank You!