25 November 2020

India Strategy

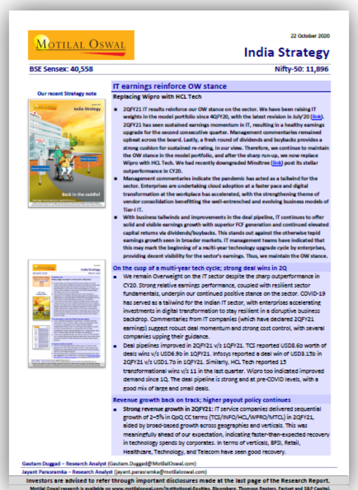
BSE Sensex: 44,523 | **S&P CNX: 13,055**

Refer to our Sep'20 Quarter Review


MOTILAL OSWAL
India Strategy
BSE Sensex: 43,443
Nifty-50: 12,720
2QFY21 Results Review: An all-round beat!
Earnings upgrade after years; Upgrades outweigh downgrades by 4x

Our recent Strategy notes


MOTILAL OSWAL
28 October 2020
India Strategy
BSE Sensex: 39,922
Nifty-50: 11,730
Divergence: The story of 2020 so far...
Earnings – the key driver of divergence


MOTILAL OSWAL
22 October 2020
India Strategy
BSE Sensex: 40,558
Nifty-50: 11,896
IT earnings reinforce OW stance
Replacing Wipro with HCL Tech

Corporate India doubles down on cost control!

Analyzing costs in greater detail; margin expansion to moderate in 2HFY21

- In the recently concluded 2QFY21 results, both Nifty and the MOSL Universe reported broad-based earnings beat, leading to healthy 9-10% earnings upgrades in FY21 estimates for both sets of aggregates. A detailed analysis of 2QFY21 earnings can be found here.
- One of the key and defining features of this performance was the better-than-expected focus on cost mitigation measures, apart from demand recovery and a healthy tailwind from gross margin expansion.
- In this note, we analyze the cost components in slightly greater detail and highlight various elements pertaining to these.

2QFY21 was an optimum combination of gross margin expansion and operating cost reduction

- In 2QFY21, for the MOFSL Coverage Universe, despite 7% YoY decline in revenues, EBITDA posted healthy 9% growth v/s the expectation of a flattish YoY performance. All key sectors, barring Capital Goods and Utilities, reported operating margin expansion. Ex-Financials, Nifty reported 310bps YoY EBITDA margin expansion to 19.8%; MOSL-ex-Financials reported 320bps YoY expansion to 19.4%.
- Thus, operating costs for our Universe declined 11% YoY. Within the operating cost bucket, other expenses declined 8% YoY, pointing toward continued cost control initiatives implemented by companies. Cement (-10%), Automobiles (-11%), Technology (-14%), and Oil & Gas (-21%) YoY have been the key sectors to report double-digit decline in other expenditure. Utilities (+18%), Retail (+4%), and Banks (+4%) YoY have seen an increase in other expenditure over the same period.
- RM tailwind and demand recovery, coupled with better pricing power owing to supply constraints and lower discounts, resulted in sharp gross margin expansion for our Universe. The gross margin for MOSL Universe (129 companies, ex-BFSI, IT, and Telecom) expanded 600bps YoY to 42%. Cyclical and commodities such as Metals and Oil & Gas saw a maximum of 850bps and 490bps gross margin expansion YoY, respectively. The Retail, Consumer, and Automobile sectors have seen 280bps, 100bps, and 50bps contraction, respectively, in gross margins YoY.

Other cost elements of P&L see a marginal rise

- While gross margin expansion and overhead cost reduction clearly propelled operating margin expansion, other elements of P&L costs saw a marginal rise. Staff costs expanded a modest 4% YoY for our MOFSL Universe companies. Sectors that have seen a staff cost increase include Consumer (+9%), Utilities (+9%), Banks (+9%), Healthcare (+8%), Oil and Gas (+8%) and IT (4%). Sectors

Gautam Duggad – Research analyst (Gautam.Duggad@MotilalOswal.com)
Research analyst: Deven Mistry (Deven@MotilalOswal.com) | **Jayant Parasramka** (jayant.parasramka@motilaloswal.com)

that saw YoY contraction in employee costs are Media (-21%), Retail (-20%), Cement (-6%), and Metals (-5%).

- As normalcy returned and new launch/re-launch activity gained momentum, advertising costs for the MOSL Consumer Universe rebounded to 9.3% of sales in 2QFY21 from 7.1% in 1QFY21, but were still down v/s 10.5% in 2QFY20.

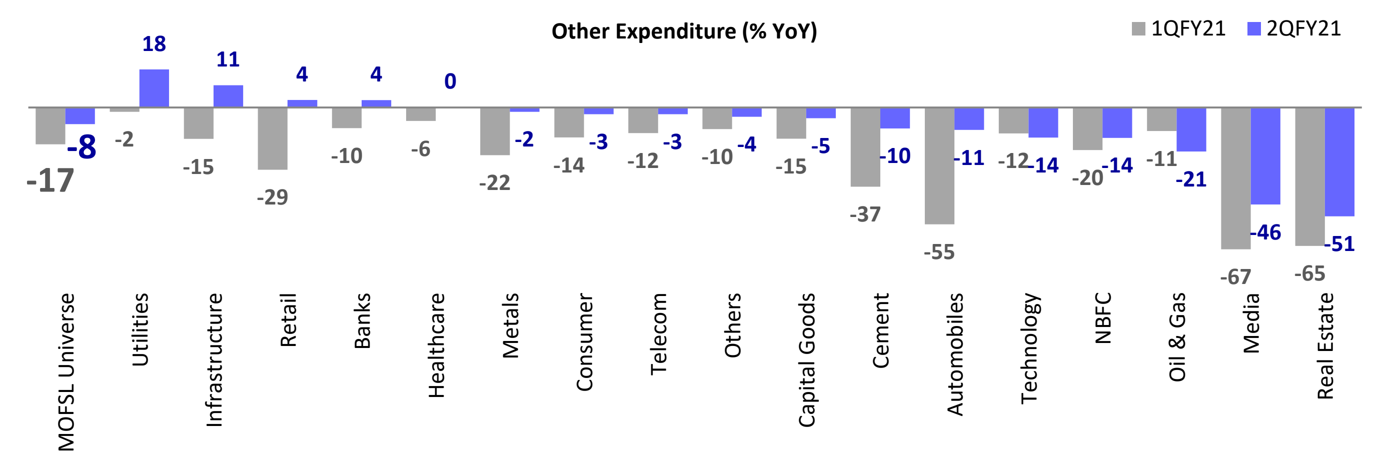
34 Nifty-50 companies have seen EBITDA margin expansion

- 34 out of 50 companies in the Nifty Universe have seen EBITDA margin expansion, while 16 companies have reported EBITDA margin contraction.
- JSW Steel, Divi's Lab, IOC, Ultratech Cement and Sun Pharma have seen expansion of 910bps, 790bps, 690bps, 610bps and 600bps YoY, respectively, in EBITDA margins.
- Coal India, ONGC, Titan, ITC and Eicher Motors, on the other hand, have posted a contraction of 480bps, 440bps, 430bps, 280bps and 240bps YoY, respectively, in EBITDA margins.

Pace of margin expansion to moderate in 2HFY21

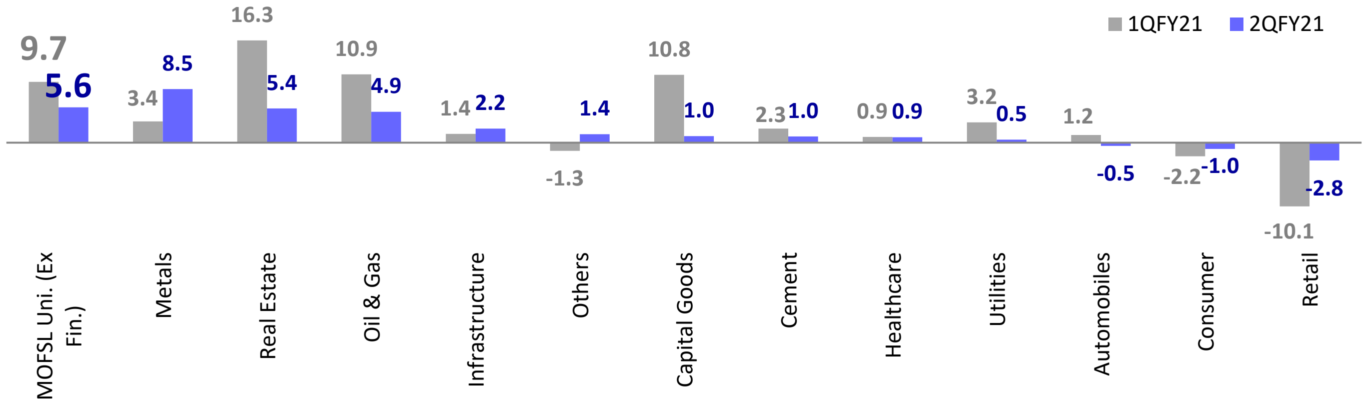
- After the sharp beat on costs and faster-than-expected demand recovery, FY21E earnings for the MOSL Universe and Nifty saw upgrades of 11% and 9%, respectively.
- Going forward, we expect some elements of P&L costs to make a comeback as the economy opens up more and travel cost and other overheads gradually return. Also, RM costs are going up sequentially for several sectors (Consumer, Auto, and Cement).
- Also, cost reduction has been factored in, and consequently, there is limited room for surprise now, in our view. We now build in 140bps and 110bps EBITDA margin expansion to 18.2% and 17.4% for Nifty-ex-Financials for 3QFY21E and 4QFY21E, respectively.
- For the MOSL Universe-ex-Financials, operating margin expansion is expected at 190bps and 220bps to 18.1% and 17.6% for 3QFY21E and 4QFY21E, respectively, v/s 19.4% in 2QFY21.

Exhibit 1: Two consecutive quarters of overhead cost reduction across sector in MOSL Universe



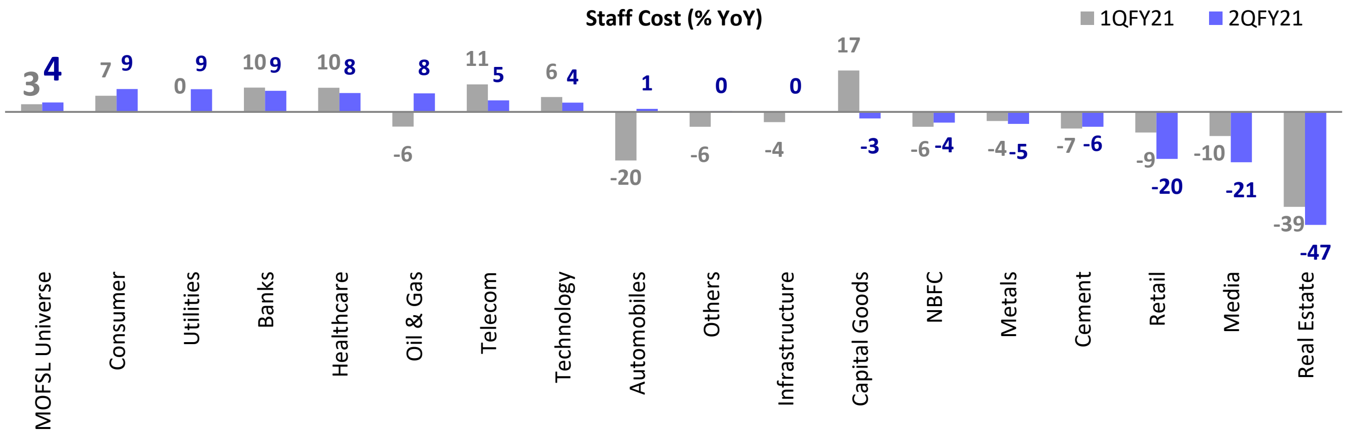
Source: MOFSL, Note: The Universe includes data for 179 companies

Exhibit 2: Gross margins expanded 600bps YoY; Metals and O&G see sharp GM expansion



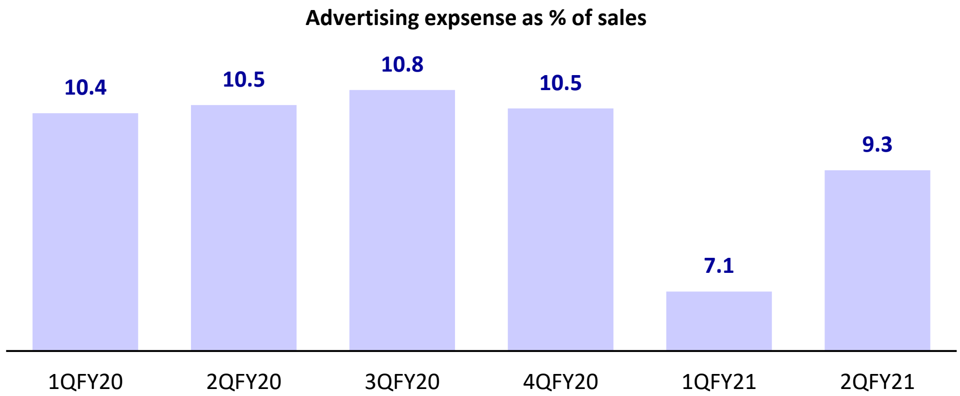
Source: MOFSL, Note: The Universe includes data for 129 companies

Exhibit 3: Staff cost was however up YoY for many sectors



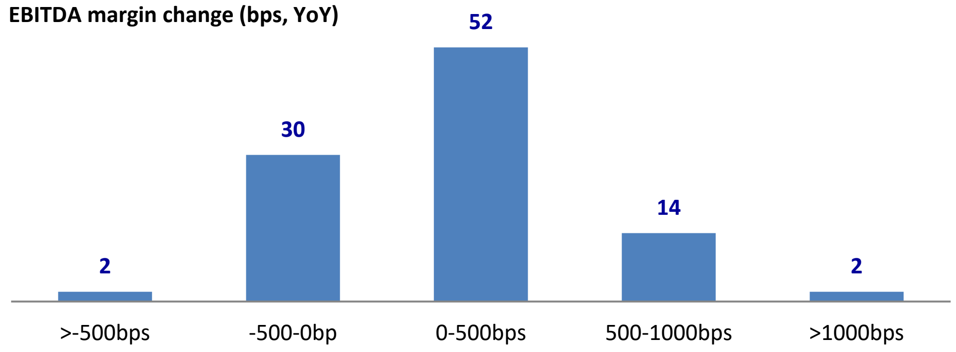
Source: MOFSL, Note: The Universe includes data for 179 companies

Exhibit 4: AD spends rebounded sequentially for Consumer companies but still down YoY



Source: MOFSL, Note: Universe consists of 10 consumer companies

Exhibit 5: 34 out of 50 Nifty companies reported EBITDA margin expansion; 8 reported expansion >=500bps



Source: MOFSL

Exhibit 6: Top 10 Non-BFSI Nifty companies that saw EBITDA margin expansion in 2QFY21

		Sales (INR b)		EBIDTA (INR b)		EBIDTA Margin (%)		
Company	Sector	Sep-19 (actual)	Sep-20 (actual)	Sep-19 (actual)	Sep-20 (actual)	Sep-19 (actual)	Sep-20 (actual)	Chg pp
JSW Steel	Metals	171.1	190.4	22.7	42.5	13.2	22.3	9.1
Divis Labs	Healthcare	14.5	17.5	5.1	7.6	35.3	43.3	7.9
IOC	Oil & Gas	1116.9	856.1	47.1	94.3	4.2	11.0	6.8
Ultratech Cement	Cement	96.2	103.5	19.2	27.0	19.9	26.0	6.1
Sun Pharma	Healthcare	79.5	84.6	16.1	22.2	20.2	26.2	6.0
Tata Steel	Metals	345.8	371.5	38.2	61.1	11.0	16.4	5.4
Asian Paints	Consumer	50.5	53.5	9.5	12.7	18.9	23.6	4.7
Dr Reddy' s Labs	Healthcare	40.8	49.0	8.5	12.2	20.8	24.9	4.2
Infosys	Technology	226.3	245.7	56.4	70.8	24.9	28.8	3.9
Britannia	Consumer	30.5	34.2	4.9	6.8	16.1	19.8	3.6

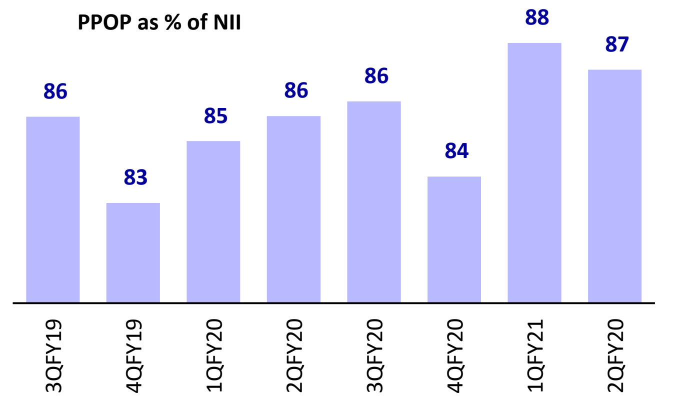
Source: MOFSL

Exhibit 7: Ten Non-BFSI Nifty companies which witnessed maximum EBITDA margin contraction in 2QFY21

		Sales (INR B)		EBIDTA (INR B)		EBIDTA Margin (%)		
Company	Sector	Sep-19 (actual)	Sep-20 (actual)	Sep-19 (actual)	Sep-20 (actual)	Sep-19 (actual)	Sep-20 (actual)	Chg pp
Tata Motors	Automobiles	654.3	535.3	71.6	56.7	10.9	10.6	-0.4
NTPC	Utilities	236.3	250.2	72.1	75.3	30.5	30.1	-0.4
Larsen & Toubro	Capital Goods	353.3	310.3	40.2	33.3	11.4	10.7	-0.6
Hero Motocorp	Automobiles	75.7	93.7	11.0	12.9	14.5	13.7	-0.8
Grasim Industries	Cement	48.0	34.4	6.6	4.0	13.7	11.6	-2.2
Eicher Motors	Automobiles	21.9	21.1	5.4	4.7	24.7	22.3	-2.4
ITC	Consumer	116.6	111.8	45.6	40.6	39.1	36.3	-2.8
Titan Company	Retail	46.6	45.5	5.2	3.1	11.2	6.9	-4.3
ONGC	Oil & Gas	244.9	169.2	132.9	84.4	54.3	49.9	-4.4
Coal India	Utilities	203.8	211.5	42.5	34.0	20.8	16.1	-4.8

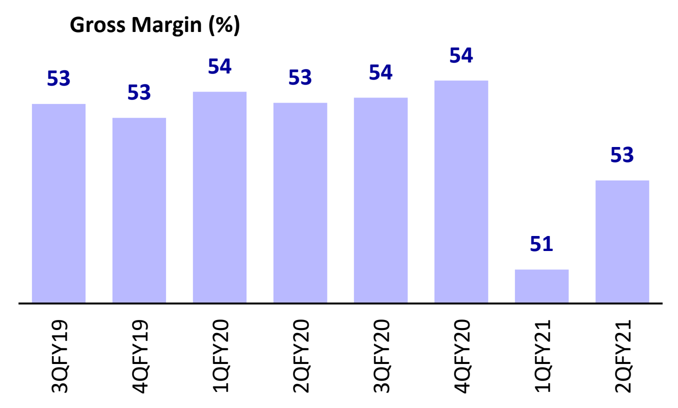
Source: MOFSL

Exhibit 8: For Private Banks, PPOP margins as % of NII remained stable



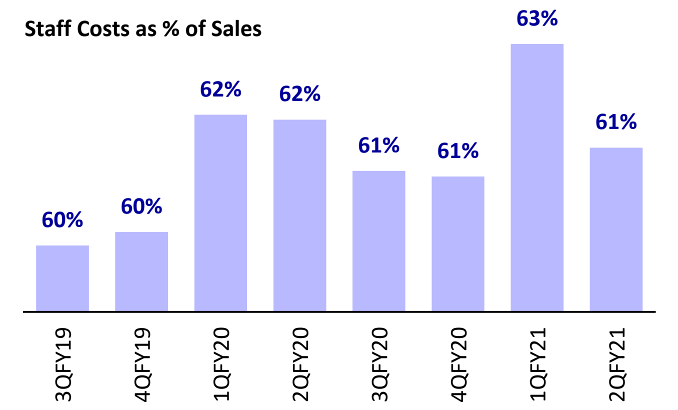
Source: MOFSL. Note: Universe consists of 10 private banks.

Exhibit 9: Gross margins for Consumer companies in MOSL coverage bounce back from the 1QFY21 lows



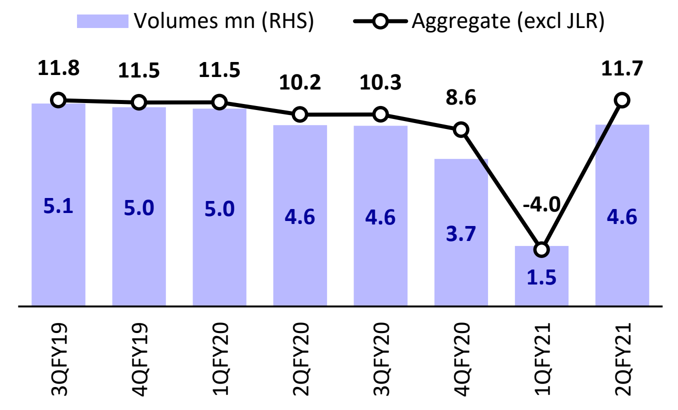
Source: MOFSL. Note: Universe consists of 17 companies.

Exhibit 10: Staff costs decline sequentially and YoY for IT companies



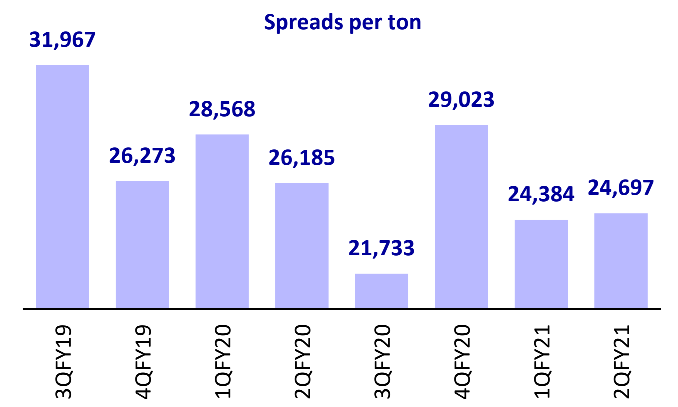
Source: MOFSL. Note: Universe consists of 12 IT companies

Exhibit 11: EBITDA Margins for Autos up YoY after posting operating loss in 1QFY21



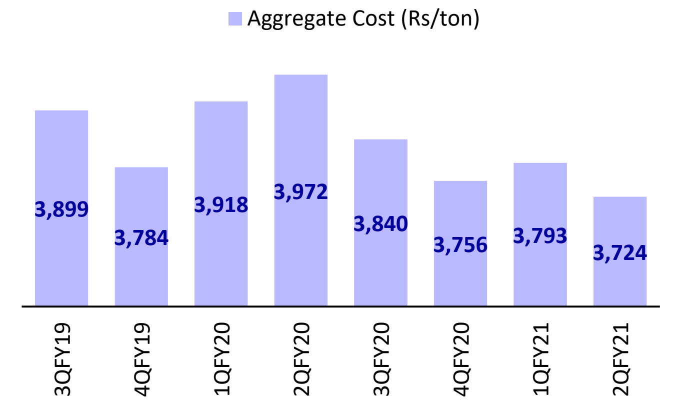
Source: MOFSL. MOFSL Auto Universe except JLR

Exhibit 12: Steel spreads per ton stable sequentially in 2QFY21



Source: MOFSL. Universe consists of 4 steel companies.

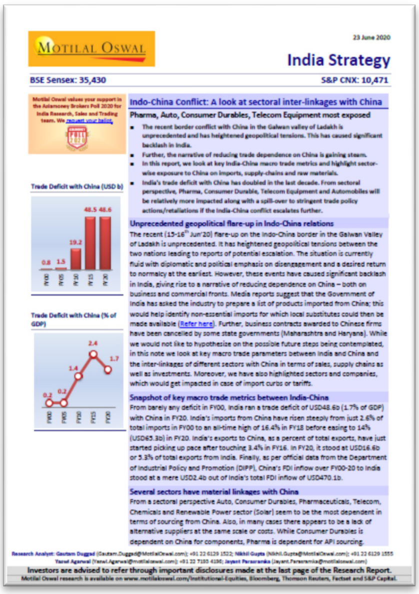
Exhibit 13: Cement universe posted a 6% YoY decline in operating costs in 2QFY21

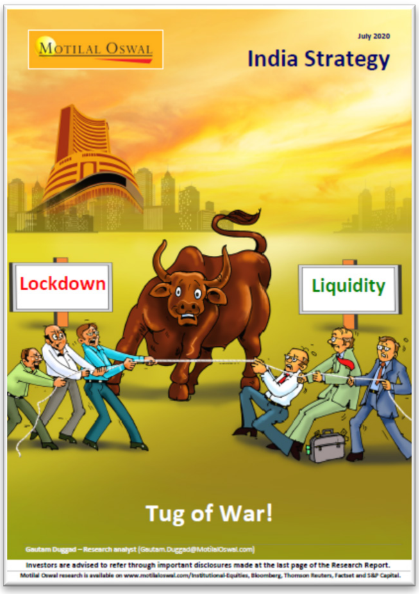


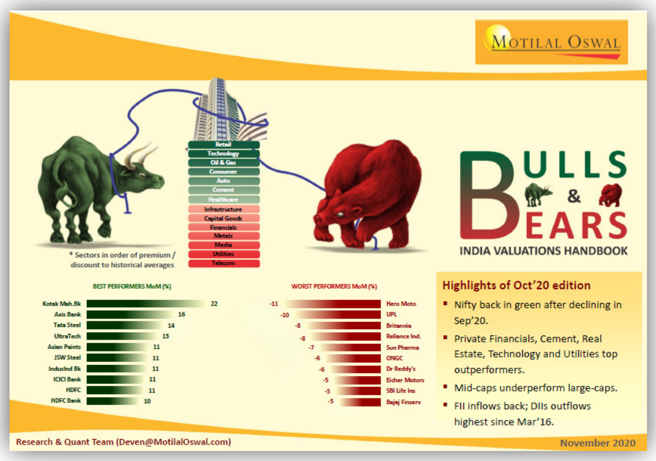
Source: MOFSL. Universe consists of 10 cement companies.

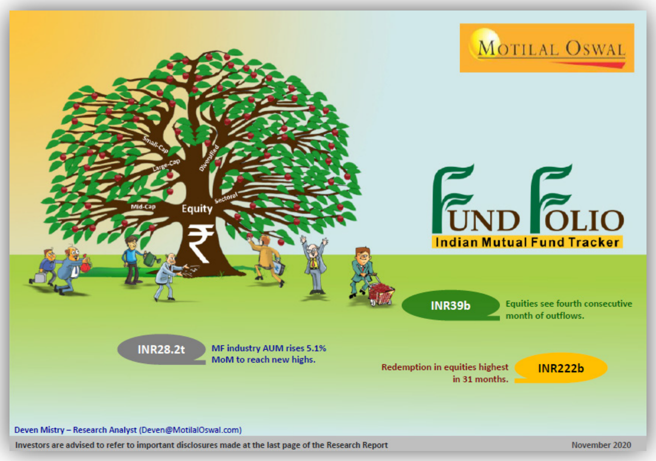
NOTES

India Strategy, Thematic and Quant Research Gallery









Investment Rating	Expected return (over 12-month)
BUY	>=15%
SELL	< - 10%
NEUTRAL	> - 10 % to 15%
UNDER REVIEW	Rating may undergo a change
NOT RATED	We have forward looking estimates for the stock but we refrain from assigning recommendation

*In case the recommendation given by the Research Analyst is inconsistent with the investment rating legend for a continuous period of 30 days, the Research Analyst shall within following 30 days take appropriate measures to make the recommendation consistent with the investment rating legend.

Disclosures:

The following Disclosures are being made in compliance with the SEBI Research Analyst Regulations 2014 (herein after referred to as the Regulations).

Motilal Oswal Financial Services Ltd. (MOFSL) is a SEBI Registered Research Analyst having registration no. INH000000412. MOFSL, the Research Entity (RE) as defined in the Regulations, is engaged in the business of providing Stock broking services, Investment Advisory Services, Depository participant services & distribution of various financial products. MOFSL is a subsidiary company of Passionate Investment Management Pvt. Ltd.. (PIMPL). MOFSL is a listed public company, the details in respect of which are available on www.motilaloswal.com. MOFSL (erstwhile Motilal Oswal Securities Limited - MOFSL) is registered with the Securities & Exchange Board of India (SEBI) and is a registered Trading Member with National Stock Exchange of India Ltd. (NSE) and Bombay Stock Exchange Limited (BSE), Multi Commodity Exchange of India Limited (MCX) and National Commodity & Derivatives Exchange Limited (NCDEX) for its stock broking activities & is Depository participant with Central Depository Services Limited (CDSL) National Securities Depository Limited (NSDL),NERL, COMRIS and CCRL and is member of Association of Mutual Funds of India (AMFI) for distribution of financial products and Insurance Regulatory & Development Authority of India (IRDA) as Corporate Agent for insurance products. Details of associate entities of Motilal Oswal Financial Services Limited are available on the website at http://onlinereports.motilaloswal.com/Dormant/documents/Associate%20Details.pdf

Details of pending Enquiry Proceedings of Motilal Oswal Financial Services Limited are available on the website at https://galaxy.motilaloswal.com/ResearchAnalyst/PublishViewLitigation.aspx

MOFSL, it's associates, Research Analyst or their relative may have any financial interest in the subject company. MOFSL and/or its associates and/or Research Analyst may have actual/beneficial ownership of 1% or more securities in the subject company in the past 12 months. MOFSL and its associate company(ies), their directors and Research Analyst and their relatives may; (a) from time to time, have a long or short position in, act as principal in, and buy or sell the securities or derivatives thereof of companies mentioned herein. (b) be engaged in any other transaction involving such securities and earn brokerage or other compensation or act as a market maker in the financial instruments of the company(ies) discussed herein or act as an advisor or lender/borrower to such company(ies) or may have any other potential conflict of interests with respect to any recommendation and other related information and opinions.; however the same shall have no bearing whatsoever on the specific recommendations made by the analyst(s), as the recommendations made by the analyst(s) are completely independent of the views of the associates of MOFSL even though there might exist an inherent conflict of interest in some of the stocks mentioned in the research report. Research Analyst may have served as director/officer, etc. in the subject company in the past 12 months. MOFSL and/or its associates may have received any compensation from the subject company in the past 12 months.

In the past 12 months , MOFSL or any of its associates may have:

a) managed or co-managed public offering of securities from subject company of this research report,
b) received compensation for investment banking or merchant banking or brokerage services from subject company of this research report,
c) received compensation for products or services other than investment banking or merchant banking or brokerage services from the subject company of this research report.
d) Subject Company may have been a client of MOFSL or its associates in the past 12 months.

MOFSL and it's associates have not received any compensation or other benefits from the subject company or third party in connection with the research report. To enhance transparency, MOFSL has incorporated a Disclosure of Interest Statement in this document. This should, however, not be treated as endorsement of the views expressed in the report. MOFSL and / or its affiliates do and seek to do business including investment banking with companies covered in its research reports. As a result, the recipients of this report should be aware that MOFSL may have a potential conflict of interest that may affect the objectivity of this report. Compensation of Research Analysts is not based on any specific merchant banking, investment banking or brokerage service transactions. Above disclosures include beneficial holdings lying in demat account of MOFSL which are opened for proprietary investments only. While calculating beneficial holdings, It does not consider demat accounts which are opened in name of MOFSL for other purposes (i.e holding client securities, collaterals, error trades etc.). MOFSL also earns DP income from clients which are not considered in above disclosures. Above disclosures include beneficial holdings lying in demat account of MOFSL which are opened for proprietary investments only. While calculating beneficial holdings, It does not consider demat accounts which are opened in name of MOFSL for other purposes (i.e holding client securities, collaterals, error trades etc.). MOFSL also earns DP income from clients which are not considered in above disclosures.

Terms & Conditions:

This report has been prepared by MOFSL and is meant for sole use by the recipient and not for circulation. The report and information contained herein is strictly confidential and may not be altered in any way, transmitted to, copied or distributed, in part or in whole, to any other person or to the media or reproduced in any form, without prior written consent of MOFSL. The report is based on the facts, figures and information that are considered true, correct, reliable and accurate. The intent of this report is not recommendatory in nature. The information is obtained from publicly available media or other sources believed to be reliable. Such information has not been independently verified and no guaranty, representation of warranty, express or implied, is made as to its accuracy, completeness or correctness. All such information and opinions are subject to change without notice. The report is prepared solely for informational purpose and does not constitute an offer document or solicitation of offer to buy or sell or subscribe for securities or other financial instruments for the clients. Though disseminated to all the customers simultaneously, not all customers may receive this report at the same time. MOFSL will not treat recipients as customers by virtue of their receiving this report.

Analyst Certification

The views expressed in this research report accurately reflect the personal views of the analyst(s) about the subject securities or issues, and no part of the compensation of the research analyst(s) was, is, or will be directly or indirectly related to the specific recommendations and views expressed by research analyst(s) in this report.

Disclosure of Interest Statement	Companies where there is interest
Analyst ownership of the stock	No

A graph of daily closing prices of securities is available at www.nseindia.com, www.bseindia.com. Research Analyst views on Subject Company may vary based on Fundamental research and Technical Research. Proprietary trading desk of MOFSL or its associates maintains arm's length distance with Research Team as all the activities are segregated from MOFSL research activity and therefore it can have an independent view with regards to subject company for which Research Team have expressed their views.

Regional Disclosures (outside India)

This report is not directed or intended for distribution to or use by any person or entity resident in a state, country or any jurisdiction, where such distribution, publication, availability or use would be contrary to law, regulation or which would subject MOFSL & its group companies to registration or licensing requirements within such jurisdictions.

For Hong Kong:

This report is distributed in Hong Kong by Motilal Oswal capital Markets (Hong Kong) Private Limited, a licensed corporation (CE AYY-301) licensed and regulated by the Hong Kong Securities and Futures Commission (SFC) pursuant to the Securities and Futures Ordinance (Chapter 571 of the Laws of Hong Kong) "SFO". As per SEBI (Research Analyst Regulations) 2014 Motilal Oswal Financial Services Limited(SEBI Reg No. INH000000412) has an agreement with Motilal Oswal capital Markets (Hong Kong) Private Limited for distribution of research report in Hong Kong. This report is intended for distribution only to "Professional Investors" as defined in Part I of Schedule 1 to SFO. Any investment or investment activity to which this document relates is only available to professional investor and will be engaged only with professional investors." Nothing here is an offer or solicitation of these securities, products and services in any jurisdiction where their offer or sale is not qualified or exempt from registration. The Indian Analyst(s) who compile this report is/are not located in Hong Kong & are not conducting Research Analysis in Hong Kong.

For U.S:

Motilal Oswal Financial Services Limited (MOFSL) is not a registered broker - dealer under the U.S. Securities Exchange Act of 1934, as amended (the"1934 act") and under applicable state laws in the United States. In addition MOFSL is not a registered investment adviser under the U.S. Investment Advisers Act of 1940, as amended (the "Advisers Act" and together with the 1934 Act, the "Acts), and under applicable state laws in the United States. Accordingly, in the absence of specific exemption under the Acts, any brokerage and investment services provided by MOFSL, including the products and services described herein are not available to or intended for U.S. persons. This report is intended for distribution only to "Major Institutional Investors" as defined by Rule 15a-6(b)(4) of the Exchange Act and interpretations thereof by SEC (henceforth referred to as "major institutional investors"). This document must not be acted on or relied on by persons who are not major institutional investors. Any investment or investment activity to which this document relates is only available to major institutional investors and will be engaged in only with major institutional investors. In reliance on the exemption from registration provided by Rule 15a-6 of the U.S. Securities Exchange Act of 1934, as amended (the "Exchange Act") and interpretations thereof by the U.S. Securities and Exchange Commission ("SEC") in order to conduct business with Institutional Investors based in the U.S., MOFSL has entered into a chaperoning agreement with a U.S. registered broker-dealer, Motilal Oswal Securities International Private Limited. ("MOSIPL"). Any business interaction pursuant to this report will have to be executed within the provisions of this chaperoning agreement.

The Research Analysts contributing to the report may not be registered /qualified as research analyst with FINRA. Such research analyst may not be associated persons of the U.S. registered broker-dealer, MOSIPL, and therefore, may not be subject to NASD rule 2711 and NYSE Rule 472 restrictions on communication with a subject company, public appearances and trading securities held by a research analyst account.

For Singapore:

In Singapore, this report is being distributed by Motilal Oswal Capital Markets Singapore Pte Ltd ("MOCMSPL") (Co.Reg. NO. 201129401Z) which is a holder of a capital markets services license and an exempt financial adviser in Singapore,
as per the approved agreement under Paragraph 9 of Third Schedule of Securities and Futures Act (CAP 289) and Paragraph 11 of First Schedule of Financial Advisors Act (CAP 110) provided to MOCMSPL by Monetary Authority of Singapore. Persons in Singapore should contact MOCMSPL in respect of any matter arising from, or in connection with this report/publication/communication. This report is distributed solely to persons who qualify as "Institutional Investors", of which some of whom may consist of "accredited" institutional investors as defined in section 4A(1) of the Securities and Futures Act, Chapter 289 of Singapore ("the SFA"). Accordingly, if a Singapore person is not or ceases to be such an institutional investor, such Singapore Person must immediately discontinue any use of this Report and inform MOCMSPL.

Registered Office Address: Motilal Oswal Tower, Rahimtullah Sayani Road, Opposite Parel ST Depot, Prabhadevi, Mumbai-400025; Tel No.: 022 71934200/ 022-71934263; Website www.motilaloswal.com.
CIN No.: L67190MH2005PLC153397.Correspondence Office Address: Palm Spring Centre, 2nd Floor, Palm Court Complex, New Link Road, Malad(West), Mumbai- 400 064. Tel No: 022 7188 1000.
Registration Nos.: Motilal Oswal Financial Services Limited (MOFSL)*: INZ000158836(BSE/NSE/MCX/NCDEX); CDSL and NSDL: IN-DP-16-2015; Research Analyst: INH000000412. AMFI: ARN - 146822; Investment Adviser: INA000007100; Insurance Corporate Agent: CA0579 ;PMS:INP000006712. Motilal Oswal Asset Management Company Ltd. (MOAMC): PMS (Registration No.: INP000000670); PMS and Mutual Funds are offered through MOAMC which is group company of MOFSL. Motilal Oswal Wealth Management Ltd. (MOWML): PMS (Registration No.: INP000004409) is offered through MOWML, which is a group company of MOFSL. Motilal Oswal Financial Services Limited is a distributor of Mutual Funds, PMS, Fixed Deposit, Bond, NCDs,Insurance Products and IPOs.Real Estate is offered through Motilal Oswal Real Estate Investment Advisors II Pvt. Ltd. which is a group company of MOFSL. Private Equity is offered through Motilal Oswal Private Equity Investment Advisors Pvt. Ltd which is a group company of MOFSL. Research & Advisory services is backed by proper research. Please read the Risk Disclosure Document prescribed by the Stock Exchanges carefully before investing. There is no assurance or guarantee of the returns. Investment in securities market is subject to market risk, read all the related documents carefully before investing. Details of Compliance Officer: Name: Neeraj Agarwal, Email ID: na@motilaloswal.com, Contact No.:022-71881085.

* MOFSL has been amalgamated with Motilal Oswal Financial Services Limited (MOFSL) w.e.f August 21, 2018 pursuant to order dated July 30, 2018 issued by Hon'ble National Company Law Tribunal, Mumbai Bench