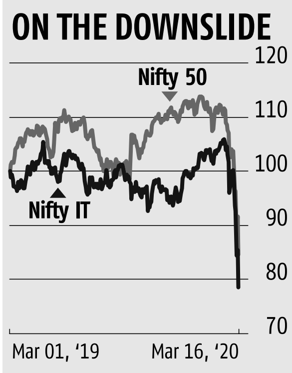
Analysts see 8-10% decline in FY21 earnings of IT firms

Lower spends by key customer segments may hurt revenues and margins, offsetting gains from a weak rupee

SHREEPAD S AUTE
Mumbai, 16 March



With the spread of coronavirus or COVID-19 remaining unabated, major global central banks have intervened to soften the pandemic's economic impact by reducing interest rates or by quantitative easing (infusing cheap funds). While the Reserve Bank of India (RBI) on Monday announced measures to ease liquidity in the domestic banking system, the US Federal Reserve on Sunday cut its interest rate near to zero.

While the jury is out on how much these efforts may help, the weakening demand environment has cast a shadow for major Indian information technology (IT) players, given their dependence on US financial services and the retail and energy sectors.

Top IT players — such as Tata Consultancy Services (TCS), Infosys, HCL Technologies, and Wipro — earn 21-32 per cent of their revenue from the BFSI (banking, financial services and insurance) sector and the US accounts for over 50 per cent of their top line.

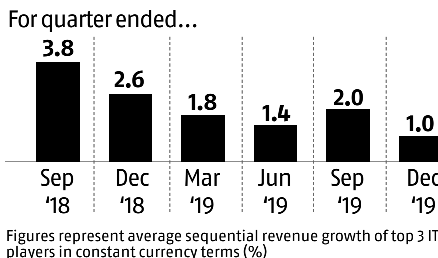
Toeing the broader market movement (the Nifty is down 24 per cent in the last one month), the Nifty IT index has also lost over 25 per cent, touching its 52-week low on last Friday, despite a weaker rupee being favourable for domestic IT players.

Amit Chandra, analyst at HDFC Securities, said: "Amid a likely negative impact of interest rate cuts by banks globally, including the US Fed, Indian IT players could see a flattish growth in the first half of FY21 (April-September 2020), in constant currency terms. This, in turn, would make achieving higher-single digit revenue growth in FY21 difficult for major IT players."

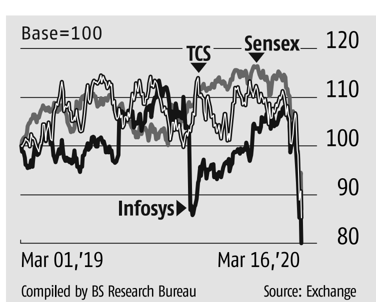
Other analysts, too, have similar views. Sanjeev Hota, head of research at Sharekhan, said: "With sharp rate cuts in the US, which would impact the spending of BFSI clients, and lower discretionary spending in certain verticals amid the coronavirus pandemic, it looks challenging for Indian IT companies to achieve higher-single digit growth in FY21."

DISMAL GROWTH FOR IT FIRMS

For quarter ended...



Figures represent average sequential revenue growth of top 3 IT players in constant currency terms (%)



Compiled by BS Research Bureau Source: Exchange

CORONAVIRUS PANDEMIC

Lower interest rates, along with the impact of coronavirus on corporate earnings, are likely to hurt IT spending in the BFSI sector, mainly banks. This could have a negative impact on Indian IT players in two ways -- the conversion of existing deals into revenue would get delayed and new deal size would come down. There could also be pressure on margins as clients seek more bang for the buck. In fact, coronavirus has only added to the woes for BFSI vertical, which was already seeing pain in the past few quarters. Many IT companies had reported negative growth in the BFSI verticle in the December 2019 quarter, on a sequential basis.

Not only from BFSI, but the growth pain would also stem from the retail segment, the second-largest business vertical (15-17 per cent of revenues) for some IT players. This is because, major the US- and Europe-based retail stores are closed to curtail the coronavirus spread.

Some analysts also see pressure on the energy segment because of the crash in crude oil prices as this will impact energy projects. Companies like Infosys and Wipro derive up to 13 per cent of revenue from the energy segment. Additionally, travel restrictions may also weigh on the overall performance of IT companies.

Muted demand or IT spending is also expected to impact margins despite the rupee's depreciation. Likely discounts by IT companies to get deals would curtail margin benefits from the rupee's depreciation to a great extent, says an analyst from a domestic broking house. Thus, even as one may expect some margin push in the March 2019 quarter from the rupee depreciation, how IT companies protect their margin in the next financial year would be the key.

Overall, investors are recommended to wait until more clarity on the top-line and margin fronts emerge. In view of these developments, some analysts said that they have cut their FY21 top-line and earnings estimates for domestic IT companies by 6-7 per cent and up to 8-10 per cent, respectively.

EMKAY STUDY

Passive global funds, algos might have magnified stock crash

ASHLEY COUTINHO
Mumbai, 16 March

The sell-off from passive global funds and algorithm-driven strategies might have exacerbated the stock market crash.

Nearly two-third of the $4.6 billion (₹34,000 crore) of net selling in Indian equities by foreign portfolio investors (FPIs) from February 19 till now has come from passive funds, estimates a report by Emkay Global Financial Services.

This is based on a study of about 200 exchange-traded funds (ETFs), with combined assets under management of $1.5 trillion that have an average India allocation of nine per cent. In this period, these ETFs saw outflow of $25 billion, the brokerage said.

ETFs make up roughly $38 bn (₹2.8 trillion) of the passive money coming into India. Of this, India-dedicated ETFs managed assets of a little over $10 bn (₹74,000 crore) as of end-December 2019.

A passive portfolio management aims to mimic the investment holdings of a particular index. Index funds, for instance, are a type of mutual fund with a portfolio constructed to match or track the components of an index, such as the Nifty 50. They purchase stocks in the same proportion as the weight of these in the index. This means these funds are supposed to perform in line with their benchmarks, except for a small difference known as the tracking error.

ETFs are similar to index funds, except that these may be bought and sold on the exchanges. They're preferred by institutional investors.

Both index funds and ETFs have seen significant inflow in developed markets over the past few years. The recent selloff, therefore, has also been led by these. Global funds such as BlackRock, Templeton and Fidelity could have 10-30 per cent of their investment routed through passive strategies, reckon experts.

"The selling can be exacerbated, as ETFs simply execute sell orders of the underlying investors. They cannot take a call on repurchasing shares at lower levels when valuations are attractive or sell stock X to buy Y or hold/deploy cash as is the case with active funds," explains U R Bhat, director at Dalton Capital Advisors. "The stampede to make an exit, with no regard to price or valuation, and the lack of buyers, can push prices down further."

Selling by hedge funds with algo-based stop-losses (orders to sell when the price drops to a prespecified level) could have got triggered in this market as well, he added. "These funds can go on a selling spree when stop-losses are triggered."

Algorithmic trading, where a computer automatically executes trades based on pre-programmed instructions, was introduced in India in 2009. It now contributes to about two-fifth of exchange volumes. This figure is over 80 per cent of volumes in developed markets such as America.

No-cost EMI option could be beneficial

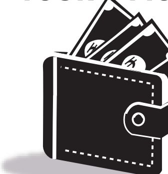
You may go for it, if you don't have to break an investment giving good returns

BINDISHA SARANG

Among the people working from their homes because of the Coronavirus pandemic, there is a marked tendency to go online and shop. Says Amber Ram, a Mumbai-based private sector employee: "I do sometimes tend to shop online just to ward off boredom." Shopping festivals like the Flipkart.com Big Shopping Day sale from March 19-22 add to the allure of online shopping. Even if you belong to the judicious bunch who genuinely needs to buy a big-ticket item, there are quite a few ways you can pay. You could go for the no-cost EMI option, break an investment, take a personal loan, or save for a few months and then buy. How should you go about making a choice?

How does a no-cost EMI work? If the price of a laptop is ₹1 lakh, you get to pay instalments of ₹10,000 for the next ten months. No interest cost is charged from you. Says Gaurav Aggarwal, director and head of unsecured loans, Paisabazaar.com: "Under the zero-cost EMI offer, the buyer repays the selling price in equal instalments over the tenure. The seller receives the discounted price while the bank receives the balance amount—the discount—as its interest. The only additional cost borne by the buyer is the GST levied on the interest component." In short, the discount that you would have enjoyed if you had paid lump sum goes to the bank as interest payment.

YOUR MONEY



Other loan options also exist. Says Adhil Shetty, CEO, BankBazaar: "Traditionally, credit cards have enabled users to opt for purchasing products on EMIs at no extra cost or documentation through an EMI on-call or EMI options offered by specific merchants. Today, you have the option of an EMI card as well. The EMI card is a pre-approved loan where the EMI starts only after you have used the card to buy a product."

Should one break an existing fixed deposit or units of mutual funds? Says certified financial planner Nirreen Mamaji: "Redeeming an investment could be a bad strategy since the mutual fund units may have been purchased at lower NAVs. By not staying invested you might lose out on further gains." Long-term returns from equity mutual funds can be above 10 per cent. Similarly, breaking an FD that pays 8 per cent to get a discount worth 5 per cent may not be worthwhile. On the other hand, if you withdraw money from a savings account, which pays 3 per cent, to earn a lumpsum discount of 5 per cent, that could be a good decision.

In some cases, it makes sense to go for a no-cost EMI if that means you don't have to break an investment, even if you have to forgo the small discount available on lumpsum payment. Thus, a cost-benefit analysis needs to be done before choosing an option.

Experts have two suggestions regarding taking a loan to make a purchase. One, when you take a loan, there are always costs attached, though they may be hidden. Says Bengaluru-based financial expert Mrin Agrawal: "It is always better to save and buy a product instead of taking a loan. There is always an interest component in a loan though it maybe camouflaged." And two, experts are currently advising against all forms of debt. Says M. Barve, a Mumbai-based financial advisor: "In a time like this, when the markets are tanking, the economy is slowing down and jobs are at risk, taking on additional debt should be avoided."

DISCOUNT EARNED SHOULD EXCEED INTEREST EARNED

Assuming you buy a laptop for ₹1 lakh

Type	Savings account	Fixed deposit	Lump sum discount
Interest	4%	8%	10%
Gain from paying lump sum	6%	2%	10%
Gain (₹)	6,000	2,000	10,000

Source: MB Wealth Solutions

COMMODITIES

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PRICE CARD

As on Mar 16	International Price	International %Chg#	Domestic Price	Domestic %Chg#
METALS ($/tonne)				
Aluminium	1,677.0	-4.9	1,885.0	-0.8
Copper	5,530.5	-10.2	5,937.8	-7.5
Zinc	1,986.5	-12.5	2,100.4	-18.9
Gold ($/ounce)	1,460.3*	-1.1	1,668.2	0.5
Silver ($/ounce)	12.3*	-27.9	15.3	-20.7
ENERGY				
Crude Oil ($/bbl)	28.9*	-56.9	33.5	-49.1
Natural Gas ($/mmBtu)	1.8*	-23.1	1.8	-21.8
AGRI COMMODITIES ($/tonne)				
Wheat	180.8	-5.3	269.3	-10.5
Maize	181.0*	-2.5	219.3	-23.3
Sugar	343.4*	-2.4	464.8	-4.3
Palm oil	577.5	-19.8	942.5	-16.3
Rubber	1,466.1*	-8.4	1,750.4	-6.2
Cotton	1,284.9	-13.0	1,416.1	-11.2

* As on Mar 16, 20 1800 hrs IST, # Change Over 3 Months
Conversion rate 1 USD = 74.3& 1 Ounce = 31.1032316 grams.

Notes
1) International metals, Indian basket crude, Malaysia Palm oil, Wheat LIFFE and Coffee Karnataka robusta pertains to previous days price.
2) International metal are LME Spot prices and domestic metal are Mumbai local spot prices except for Steel.
3) International Crude oil is Brent crude and Domestic Crude oil is Indian basket.
4) International Natural gas is Nymex near month future & domestic natural gas is MCX near month futures.
5) International Wheat, White sugar & Coffee Robusta are LIFF E future prices of near month contract.
6) International Maize is MATIF near month future, Rubber is Tokyo-TOCOM near month future and Palm oil is Malaysia FOB spot price.
7) Domestic Wheat & Maize are NCDEX future prices of near month contract, Palm oil & Rubber are NCDEX spot prices.
8) Domestic Coffee is Karnataka robusta and Sugar is M30 Mumbai local spot price.
9) International cotton is Cotton no.2-NYBOT near month future & domestic cotton is MCX Future prices near month futures.

Source: Bloomberg Compiled by BS Research Bureau

Sebi backs China model: One commodity, one exchange

Notes the adoption of such a model helped the nation influence prices globally

RAJESH BHAYANI
Mumbai, 16 March

To deepen and grow commodity markets here, with an intention to make the country a price setter than a price taker in the segment, the Securities and Exchange Board of India (Sebi) has proposed a 'one commodity, one exchange' model.

At present, multiple exchanges are allowed to launch contracts in the same commodity, to enable competition and choice for investors. The Multi Commodity Exchange (MCX) is a major player in metals, precious metals and energy contracts. The National Commodity and Derivatives Exchange (NCDEX) is one in the agricultural segment; Indian Commodity Exchange (ICEX) in diamonds, paddy and steel.

Sebi feels if an exchange focuses on one or two commodities, it could be developed meaningfully. In the current system, it thinks, the exchanges' focus is on meeting the competition, rather than developing a market in their own commodities. And, liquidity gets fragmented.

An industry official who agrees said on condition of anonymity: "There is need for an approach similar to product patents for commodity contracts. When one exchange does a proper research and launched a contract, it is easier for another to duplicate that. Sebi's proposal is good in that way — when one exchange brings some uniqueness, it would then get time and enough incentives to develop and create liquidity in that contract."

So far India has been a major consumer or producer in wheat, rice, pulses, spices, cotton, tea, rubber, iron ore, steel, gold, silver and diamonds. In diamonds, rice, rubber, sugar and iron ore, among others, it is a major global importer or exporter.

CHINA LEADS THE PACK

DALIAN COMMODITY EXCHANGE: Soybean, iron ore and egg

ZHENGZHOU COMMODITY EXCHANGE: PTA, apple and cotton

SHANGHAI FUTURES EXCHANGE: Rubber

SHANGHAI GOLD EXCHANGE: Gold

SHANGHAI INTERNATIONAL: Gold, silver and platinum

ELSEWHERE IN THE WORLD

TOCOM: Rubber

LME: Non-ferrous metals

BURSA MALAYSIA: Crude palm oil

However, India is not yet in a position to meaningfully influence the global price. Sebi refers to this in a concept paper it issued late last week on the subject, on "global examples of some exchanges playing a significant role when they develop only one or two commodities".

China, for example, was a major producer or consumer in several commodities but began significantly influencing global prices only after it launched exchanges focused on certain commodities. British, Malaysian and US exchanges also provide examples of how exchanges focused on one or two commodities or one segment have been able to assume a leadership role.

Sebi wants to develop a similar model in India. One where exchanges will have to select a commodity in which only that bourse can dealin -- it would then have to develop the market for that commodity in three to five years, after which other exchanges may be allowed in.

Sebi notes that when this comes about, a particular bourse "should not misuse a monopolistic position and ensure market integrity is not compromised".

Sebi has also proposed that an exchange select two or three goods from a notified list of 91 commodities on which no derivative products have been launched by any other. The exchange could offer liquidity enhancement benefits and Sebi would relax the rules on daily and position limits, and daily price limits, in such cases.

Narinder Wadhwa, president, Commodity Participants Association of India, says he is not in favour. "A single exchange, single commodity approach is not advisable; it can make exchanges unviable," he feels. "For the development of commodities markets, the regulator should consider a proposal that when any exchange wants to introduce a contract which may be traded on another exchange, the latter come out with some uniqueness in that rather than duplicating the existing contract."

Coronavirus to take heavy toll on garment exports

T E NARASIMHAN
Chennai, 16 March

Readymade garment exports dropped by around 4.51 per cent to $1.437 billion in February 2019 compared to last year.

Exporters said the coronavirus (COVID-19) outbreak will impact exports for the next few months. This is because nearly 80 per cent of retail shops in western countries have shut due to the virus.

According to official data, while from December 2018 exports have been growing till May 2019 on a month-on-month basis, they have been falling since December 2019.

Exporters have attributed the drop mainly due to COVID-19, which impacted sentiment in the European market — the largest for Indian exporters.

Raja M Shanmugam, president of Tirupur Exporters' Association, which represent traders who export garments worth around ₹25,000 crore every year, says, "With the outbreak started in China, initially, it was looking like an opportunity for Indian exporters. This was because European customers, who were traditionally sourcing from China, started discussions with Indian exporters for new orders. But ever since the virus started spreading to Europe, in the last one or two weeks, things have turned upside down."

For orders placed, delivery is taking much more time than usual. This it the primary reason for the fall in exports.

T Thirukumaran, managing director, Estee Exports, one of the leading garment exporters, agrees.

Sales have dropped by almost 80% in the last two weeks

He said that as most countries are under lockdown, stores are shut due to restrictions by their governments and people don't go out and stay at home. The drop is mainly due to weak buying and many customers' going bankrupt or witnessing lower sales.

"The outlook for the future is very bleak due to coronavirus as many stores have shut all over Europe. Sales have dropped by almost 80 per cent in the last two weeks and this is going to continue until the virus is tamed," he said.

In Italy and France, where COVID-19 cases have been rising rapidly, all non-essential retail stores have been ordered to shut down. This forced Abercrombie & Fitch, New Jersey, Buck Mason, Everlane and Walmart to reduce working hours.