CareEdge
RATINGS

FORESIGHTS

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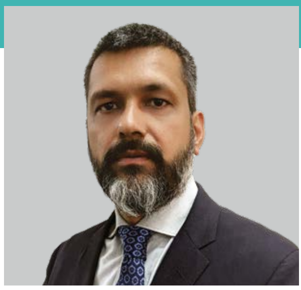
CORPORATE INDIA: STEADY SHIP IN TURBULENT WATERS

CareEdge Ratings has clocked an all-time high credit ratio (ratio of upgrades to downgrades) of 3.74 times in H1FY23, depicting a buoyant credit outlook. This is in the backdrop of the ongoing geopolitical tensions, financial market volatility and the possibility of a recession in major economies. Will this turbulence disturb corporate India's ship or will it sail steadily across the turbulent waters?

FOREWORD

SACHIN GUPTA

Chief Rating Officer
& Executive Director



It gives me immense pleasure to launch Foresights – CareEdge's power-packed monthly publication that would give you a thorough understanding of some macroeconomic and sector-specific developments shaping the country. And as analysts, economists and policymakers across the world try hard to make sense of the global economy, I believe there could not have been a better time to present this to you.

Today, we are facing high levels of inflation, rising interest rates and a looming fear of recession in most developed economies amid continued geopolitical tensions. This publication will attempt to bring clarity on the complex issues of – the global and domestic macro economy, the performance of the Indian corporate sector, and the outlook on various industries. Also included is a heatmap to provide a snapshot of the Indian economy and our projections for the key macroeconomic parameters.

The cover story of this month's edition is on the performance of the Indian corporate sector as measured by the credit ratio (the number of upgrades divided by the number of downgrades). And this tells us a very interesting story. While the Russia-Ukraine war started in February 2022, with all its consequent stress events, the credit ratio for April-September 2022 has been the highest ever at 3.74 times. This indicates the resilience of the Indian corporate sector despite global concerns, and I believe there are three key reasons for this.

The credit ratio, which helps measure the performance of the Indian corporate sector, was the highest ever at 3.74 times for April-September 2022. This indicates the resilience of the Indian corporate sector despite global concerns.

Firstly, the low leverage of the corporate balance sheets. Over the last 10 years, there has been a continuous decline in the leverage of the Indian corporate sector. The leverage of the top 1,000 corporates has come down to 0.3x in FY2022 from 0.65x in FY2013. This has allowed the corporates to withstand the multiple shocks of lockdowns, pandemic, commodity inflation and now global turmoil.

Secondly, domestic demand has continued to show improvement as reflected in healthy data on bellwether sectors such as auto. In fact, private consumption expenditure in Q1 FY23 GDP has grown by a healthy 9.9% compared with the pre-pandemic period of Q1 FY20.

Finally, the government's focus on driving investments is also giving a fillip to corporate performance.

While we were anyway seeing a strong push in the infrastructure sector, especially roads and renewables over the last few years, the more recent focus on the manufacturing sector through PLI schemes is giving good investment visibility in the near to medium term.

Overall, we must admit that we are living in rather uncertain times. The central banks across the globe are not yet showing any signs of slowing down the interest rate hikes, even amid slowing growth. The hope though is that the Indian corporate sector will be able to manage its forex, financing, and commodity price risks on the back of stable domestic demand.

I hope Foresights lends some clarity in understanding the larger developments and turns out to be a good read for you. Looking forward to your thoughts and suggestions on this.

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NOTE FROM

RAJANI SINHA

Chief Economist

The Indian economy has been recovering, albeit at a slower than expected pace. The GDP data for Q1 FY23 shows a modest growth of 3.8% when compared to the pre-pandemic period of Q1 FY20. While inflation has inched down from the peak touched in May 2022, CPI inflation remains high. Moreover, there are strong headwinds posed to India's economic recovery from the global slowdown.

Consumption and Investment in the economy are showing gradual signs of improvement. Private consumption and Investment expenditure in Q1 FY23 GDP grew by 9.9% and 6.7% respectively when compared with the pre-pandemic period of Q1 FY20. Some of the other high-frequency economic indicators like e-way bill collection, GST revenue, auto sales, and PMI continue to show expansion. A fall in global commodity prices should support the manufacturing sector going forward, while the services sector would benefit from the pent-up demand.

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The Central Government has been focusing on Investment to propel the economy on a higher growth trajectory. In Apr-Aug 2022, the Union Government recorded a capex growth of 46.8% (YoY) and has achieved 34% of the strong capital expenditure budgeted for FY23. With the Corporate Balance Sheet in good shape and with the capacity utilisation level improving, we could see a pickup in the private capex cycle. We are seeing healthy growth in bank credit, mainly led by the retail and services sector.

A big cause of concern currently is the vulnerability of India's external sector. India's exports have been slowing down as a fallout of the global economic slowdown. Net exports sharply pulled down the GDP in Q1 FY23. India's average monthly trade deficit has widened to US$ 28 billion in the last three months compared to the average monthly trade deficit of US$ 16 billion in FY22. With the sharp widening of the trade deficit, India's CAD could widen to more than 3.5% of GDP in FY23. In terms of capital inflows, while FDI inflows have remained healthy, there has been sharp volatility in FPI flows. Overall, India's Balance of Payment is estimated to record a deficit of more than USD 65 billion in FY23. The sharp weakening of the Indian rupee and the depletion of India's forex reserves, highlight the concerns on the external front.

Inflation at 7% in August 2022 remains a cause of concern. The main culprit was food inflation which shot up to 7.6% in August from 6.7% in July. On a sequential basis (MoM), there was a sharp increase in prices for items like Cereals, Vegetables, Milk and Pulses. Given the uneven distribution of rainfall and unfavourable climatic condition, we are seeing an increase in many of these food items. Moreover, the core inflation (excluding food and fuel) remained high at around 6% in August, highlighting the deep penetration of inflation in the economy.

With the persistence of inflation, RBI has hiked the policy repo rate by 190 bps in the last five months. RBI is likely to move towards a positive real rate of interest. Hence, if the sequential momentum in inflation accelerates, RBI could take the terminal repo rate higher to 6.25-6.5%.

Overall, India's economy is relatively better placed in midst of the global economic turmoil. However, we need to be cautious as the Indian economy cannot remain unscathed from the global turmoil. There are concerns not just about global demand slowing down, but also risks of further disruption in the global supply chain. The financial markets will remain volatile in midst of the global turbulence and tightening of financial conditions. Amidst growth and inflation concerns, India also needs to be wary of the widening of its twin deficit.

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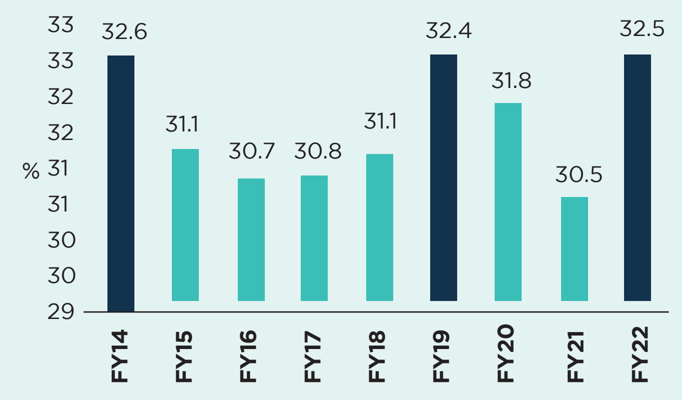
ECONOMY

INVESTMENT PUSH: NEED OF THE HOUR

India's economy is wading through various challenges and recording a gradual recovery from the pandemic. At this crucial juncture, investment push is the critical force that could push India to a higher and sustainable growth trajectory. The government has in the last few years announced various schemes like Production Linked Incentive, National Infrastructure Pipeline, National Monetisation Pipeline, PM Gati Shakti plan and corporate tax cuts to spur investment in the economy. While Investment to GDP ratio improved to 32.5 in FY22, it remained below the peak of 34 level achieved in FY12 and FY13. Given the strong multiplier effect that an investment push has on the economy, the Finance Minister had recently urged the private sector to spur up their capex plans.

Investment (GFCF) as % of GDP



Source: MOSPI

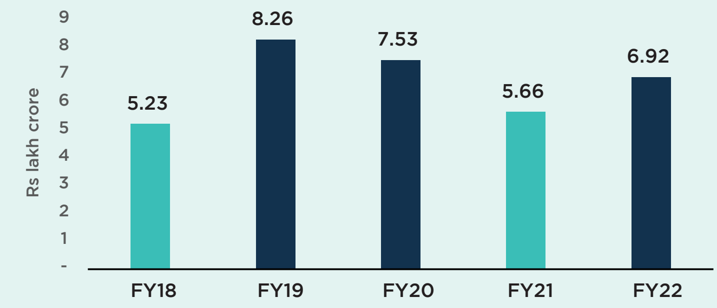
The Centre and State Governments along with the Corporate sector are critical pillars of investment in the economy. The Centre and State's capital expenditure have a strong multiplier effect of 2.45 and 2 respectively (RBI 2020). As per Niti Aayog, this multiplier is even larger during phases of economic contractions. Given the need of the hour, the Central Government has pushed up investment efforts. The Central Government has recorded capex growth of 46.8% (YoY) in Apr-Aug 2022 and has achieved 34% of the strong capital expenditure budgeted for FY23.

However, the states have so far been slow in their capex. A study of aggregate data for 21 states shows that their combined capex in the first four months is marginally lower than the corresponding period of the previous year. These 21 states have budgeted for a strong capex growth of 39% in FY23. However, capital spending by the states had a slow start in FY23 owing to the concerns of cessation of GST compensation and lower market borrowings by the states due to delays in the Centre's approval. In Apr-June 2022, the aggregate capex by these 21 states was lower by 9% compared to previous year. However, in July there has been a pickup in capex by the state governments. Going forward, the state governments' capex is likely to further improve with the disbursement of the Rs 1 lakh crore interest free loan by the Centre. The Centre is also front-loading the tax devolution to states, having released two instalments of tax devolution in August.

Coming to the corporate sector, we find that the players have been hesitant in midst of the domestic and global economic uncertainties. However, there has been recovery in capex from the pandemic lows. Our study of 659 listed non-finance companies shows that capex grew by 22% in FY22, though it still remains below the pre-pandemic period. Capex has been mainly in sectors like Telecom, Oil & Gas, Power, Retailing, Iron & Steel, Auto and Auto ancillaries. The top 10 players have contributed around 50% to the total capex for FY22.

Investment Projects announced has dropped in Q1 and Q2 of FY23 after touching a high in Q4 FY22. However, it is important to note that the share of private players in

Capex by India Inc.



Source: Ace Equity; CareEdge;
Note: Numbers based on data of 659 non-finance companies

Investment Projects announced has jumped to more than 90% in the last two quarters. Some other indicators that can be taken as a proxy of pick-up in investment, like production of capital goods and imports of capital goods have seen an improvement in the last few months. IIP for capital goods breached the pre-pandemic level in June 2022 and has recorded a healthy growth in July. Capital goods imports grew by an encouraging 21% (YoY) during the Apr-Aug period of FY23.

While there are some signs of capex revival by the private sector, the revival is skewed with few sectors and few big players contributing to the bulk of investment in the economy. The small and mid-sized players continue to remain hesitant in midst of all the global and domestic economic uncertainties.

Given the deleveraging in the last few years and with improving capacity utilisation levels (manufacturing sector CU level breached 75 level), we could see an improvement in capex by the corporate sector. The most critical aspect would be sustenance of the demand recovery that we are witnessing. The recent fall in global commodity prices and consequent easing of input prices are also supportive of investment upsurge. While interest cost is rising for corporates, that is unlikely to be a big deterrent for the capex cycle, as interest rates are unlikely to rise sharply from the current levels. However, we need to be cautious of the global slowdown and tightening of financial conditions globally as that would adversely impact India's economic revival.

COVER STORY

CORPORATE INDIA: STEADY SHIP IN TURBULENT WATERS

Credit Quality Assessment for H1 FY23

CareEdge Ratings has clocked an all-time high Credit Ratio at 3.74 times in H1FY23, which points towards a buoyant credit outlook, despite the prevailing geopolitical tensions and recessionary conditions in developed nations. The Credit Ratio (ratio of upgrades to downgrades) has been on an uptick from 2.64 times in H2FY22 to 3.74 times in H1FY23. CareEdge Ratings upgraded the ratings of 318 entities and downgraded the ratings of 85 entities during this period. The credit ratio for both, the Investment Grade (IG) and Below Investment Grade (BIG) portfolio in H1 FY23 was at the highest in the last decade at 3.90 times and 3.54 times, respectively.

These numbers are reassuring and indicate that despite turbulent times, with global economies like China witnessing slow growth, high inflation and rising interest rates and fear of developed economies like the US and EU slipping into recession, the Indian economy is relatively better placed with the highest GDP growth. With high-frequency economic indicators looking healthy and consumption and investment demand picking up amid the easing of commodity prices, CareEdge Ratings believes corporate India has remained stable and will continue to grow at a gradual pace.

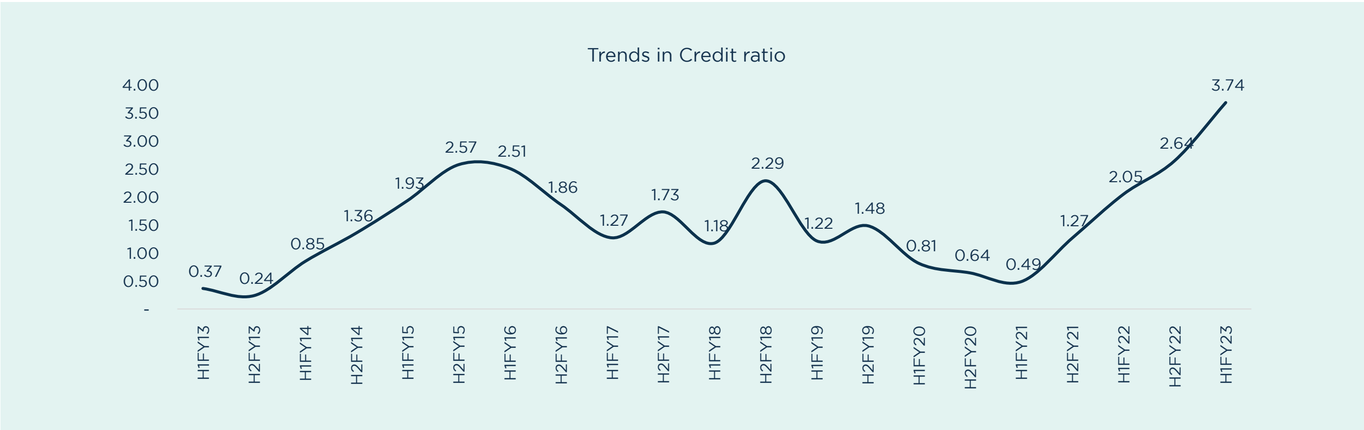
CareEdge Ratings' upgrades in H1FY23 were mainly driven by a post-pandemic broad-based recovery across sectors with the manufacturing sector's credit ratio at 4.59, leading the overall improvement in the credit ratio. The sectors that saw high upgrades in this half were textiles, healthcare, steel, chemicals, auto, pharmaceuticals and real estate in the manufacturing/ services sector. The upgrades in the manufacturing/services sector were on the back of significant deleveraging of corporate balance sheets and domestic demand recovery, supported by government initiatives helping revival of the capex cycle.

The credit ratio for infrastructure continues to be upbeat at 2.24 in H1FY23, though with a slight moderation from the high of 3.17 in H2FY22 with roads and renewables being the front-runners, followed by EPC /Construction. Enhanced pace of execution along with strong order inflows, commissioning of projects, operational projects recording robust revenues, refinancing of projects at better financing terms and structured financing avenues like InvITs drove upgrades in the infrastructure sector.

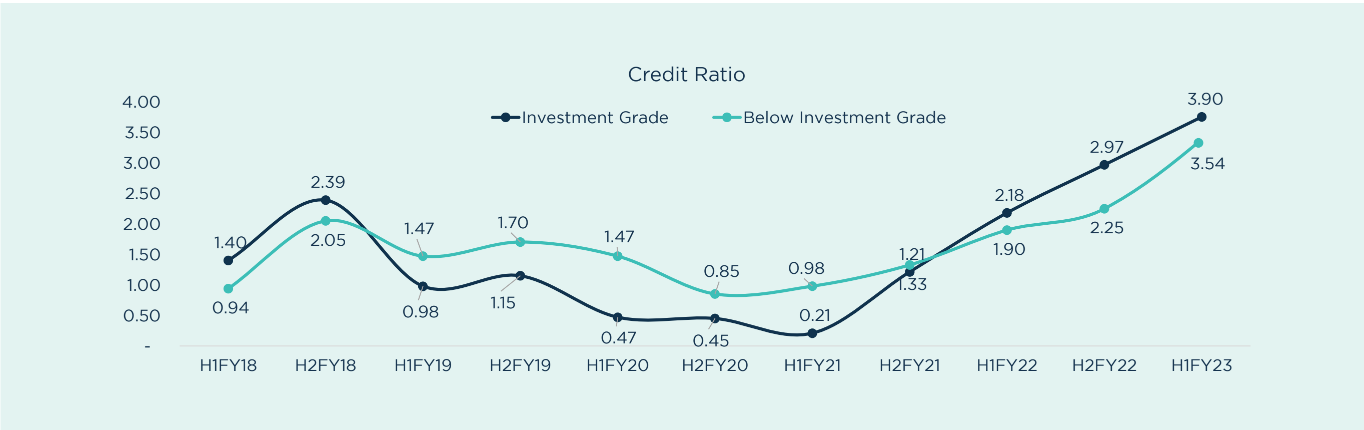
The Banking & Financial Services (BFSI) sector credit ratio witnessed the sharpest improvement in credit ratio moving up from 1.24 in H2FY22 to 4.0 times in H1FY23, driven by upgrades in NBFCs. Significant equity infusions and scaling up of operations amid waning of the pandemic-related concerns in collections, drove the majority of the upgrades.

Overall, the credit outlook remains stable but with some hiccups. Healthy capital expenditure by the government and the likely improvement in private sector capex amid rising capacity utilisation levels should boost investment in the economy. Going forward, CareEdge expects the credit outlook to be stable with deleveraging of balance sheets and growth in domestic demand, supported by Government initiatives.

However, the impact of the Russia–Ukraine crisis, volatility in commodity prices, inflationary pressures, rising interest rates and weak GDP growth in China, along with recessionary fears in the US and the EU, are the key monitorables on credit risk.

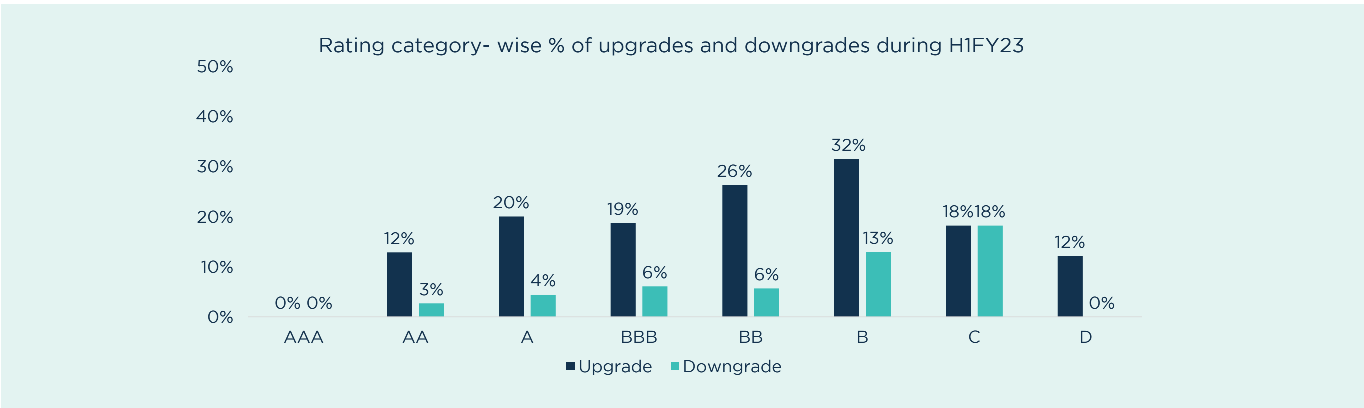


Source: CareEdge Ratings



Source: CareEdge Ratings

• The credit ratio of both, Investment grade (IG) and Below investment grade (BIG) entities for H1FY23 is at its highest.



Source: CareEdge Ratings

INDUSTRY RESEARCH

GROWTH MOMENTUM FOR AFFORDABLE HOUSING TO CONTINUE IN FY23

Key Highlights

Driven by housing and loan against property (LAP), the housing finance segment grew 20% y-o-y in FY22 after a muted show in FY21.

The share of LAP in the overall loan book increased in FY22. Going forward, CareEdge expects affordable housing finance companies (HFC) to continue to outpace the industry with an expected growth rate of around 18% in FY23.

As affordable HFCs were relatively slow in passing on the interest rate benefit to the customers, profitability for HFCs improved with relatively higher net interest margins (NIMs) and controlled credit costs.

The asset quality improved on the back of rising recoveries.

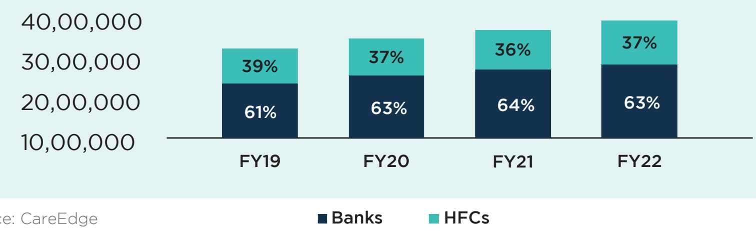
CareEdge expects affordable HFCs to continue to report healthy profitability metrics with RoTA of around 3%.

With HFCs operating at a relatively low gear due to the lower risk appetite of lenders and a cautious market, the capital structure remained modest. Bank loans continued to dominate the funding profile of the affordable segment, with National Housing Bank forming a major share.

Banks Continue to Dominate; HFCs Regain Some Lost Share

Although the banks continued to dominate and accounted for 63% of the housing finance portfolio, HFCs outshined in FY22. After a modest growth for two straight years, HFCs reported a double-digit growth rate in FY22 at 11% y-o-y, surpassing the 7% posted by the banks. Consequently, the share of HFCs, which has been contracting for the past two years, improved in FY22 from 36% to 37%. Improvement in the macroeconomic environment, low-interest rate regime, and initial signs of recovery witnessed in the real estate sector were the key catalysts for growth.

HFCs Outpace Banks in Growth



Source: CareEdge

LAP Leads Growth for Affordable HFCs

The affordable HFCs, which had been growing at significantly higher rates than the industry in the past, witnessed a moderation in growth in FY21 following the Covid-19 pandemic-induced challenges. However, growth picked up in FY22, with the affordable segment growing at 20% y-o-y. Relatively smaller base, the ability to penetrate the unorganised segments and strong appraisal skills to underwrite below-prime customers remained the key strengths for the affordable HFCs.

In terms of loan products, growth in affordable HFCs was mainly driven by the relatively higher-yielding LAP segment. Accordingly, the share of the LAP segment increased from 19% to 25% in the overall loan portfolio of affordable HFCs. With respect to yields, most of the affordable HFCs were slow in passing on the interest rate benefit to borrowers, which along with the rising share of LAP in the portfolio, resulted in yields remaining largely in line with the pre-Covid levels.

Going forward, the segment may face some headwinds from the rising interest rates, increasing construction costs and decline in disposable income amidst high inflation. However, CareEdge expects affordable HFCs to continue to outpace the industry growth with an expected growth rate of around 18% projected for FY23.

Profitability Indicators Remain below pre-Covid Levels

Affordable HFCs were relatively selective in passing on the interest rate benefit to their borrowers. Despite the declining interest rate environment, yields remained largely in line with the pre-Covid levels (yields in FY21 were higher due to the cautious stance taken by most of the HFCs). Funding costs for affordable HFCs, however, benefitted from the rising share of low-cost National Housing Bank funding along with the low-interest rate regime. Consequently, NIMs improved to 7.4%. With the rise in disbursements, the operating expenses to the average total assets (ATA) ratio increased; however, they remain lower than the pre-Covid level at 3.3%. Overall, higher NIMs along with controlled credit costs boosted the profitability profile of affordable HFCs, which reported a RoTA at 3.1%, which is higher than the pre-Covid level.

As the interest rate scenario changes, the lending spreads may come under pressure. Affordable HFCs have also started to pass on the hikes to customers at a relatively slower rate. Any impact of the repricing will be visible in FY24 as a lot of resets may happen in the current year. However, the spreads charged by lenders on these companies over benchmarks are getting compressed with improvement in the balance sheets of the companies. We expect affordable HFCs to continue to report healthy profitability metrics with RoTA of around 3%. The impact of a decline in NIMs is expected to get largely offset by improved operating efficiency and controlled credit costs.

Improving Economy Helps

Affordable HFCs reported improvement in their asset quality metrics with the gross NPA ratio declining from 4.1% to 3.4% in FY22. The segment reported strong recovery performance in the second half of FY22 as the economic activity picked up and the unorganised sector flourished.

Headline asset quality metrics also got impacted by the implementation of IRAC norms. It was relatively higher in the affordable segment as compared to prime due to its target borrower profile. Affordable HFC borrowers generally have limited financial flexibility and are highly susceptible to the impact of an economic downturn. This makes it difficult for them to clear the entire due amount resulting in relatively sticky GNPAs. In terms of provision coverage, affordable HFCs provided lesser as compared to prime HFCs with a provision coverage ratio of around 25% provisioning in the affordable segment, mainly since affordable HFCs do not have builder loans in their portfolio.

For affordable HFCs entities, bank and NHB borrowings were the main source of funding. The share of low-cost NHB borrowings improved from 17% to 23% of the borrowing mix, which further supported the fall in the cost of funds.

Capital structure continues to be comfortable with gearing remaining lower than pre-Covid times for affordable HFCs. HFCs have been maintaining healthy on-balance sheet liquidity for the last few quarters given the challenging operating environment. The gearing for the affordable HFCs stood at around 2.4x. The low-risk appetite of the lenders along with a cautious market stance led to a further decline in the gearing of the affordable HFCs segment.

INDUSTRY RESEARCH

PHARMA PLAYERS' FY23 PROFITABILITY MARGINS MAY SEE 200-250 BPS DIP

Key Highlights

With a market size of around USD 47-49 billion in FY22 (April 1 to March 31), the Indian pharmaceutical industry ranks third in terms of volume and thirteenth in terms of value globally.

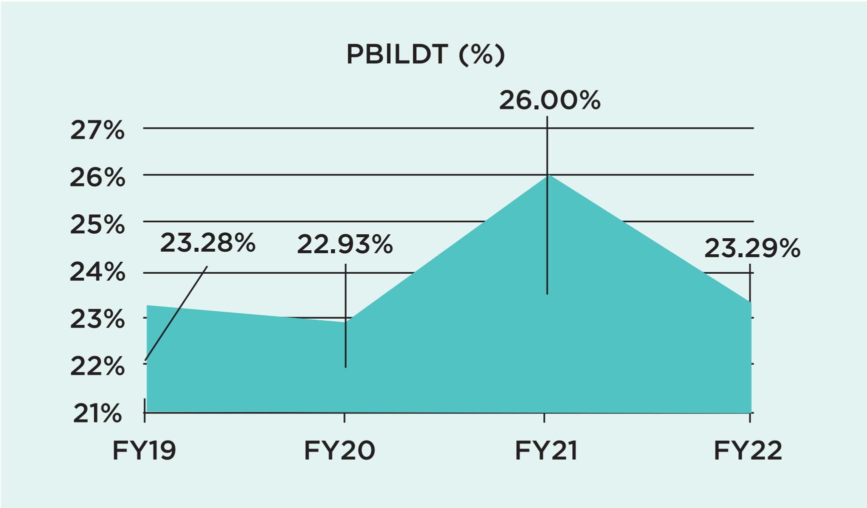
The industry has exhibited CAGR of 8-9% during FY17 to FY22 while posting a y-o-y growth of 5-7% in FY22, largely driven by higher domestic consumption, even as the exports value was stable at USD 24.60 billion in FY22.

The US continued to be the prime export destination, constituting nearly 34% of total exports during FY22, which registered a growth of 2% in USD terms while export to the Rest of the World (ROW) witnessed a decline of 7%.

Based on industry aggregates that represent over 85% of the overall pharma market, the operating profitability has remained stable at about 23% during the last 4 years (FY21 being the exception). However, with various factors affecting the Indian pharma entities, CareEdge expects operating profitability to taper by 200-250 bps in FY23.

The Rise and Fall of PBILDT Margin from FY20 to FY22

Pharma sector had witnessed a significant jump in its operating profitability (PBILDT) margin in FY21 over FY20 on account of sharp reduction in marketing, travelling and conveyance expenses in the backdrop of Covid-19 pandemic restrictions. .The profitability was also supported by Covid-led sales opportunities. However, with the normalisation of above-mentioned expenses along with waning sales opportunity of Covid-related drugs, the industry suffered a decline in its PBILDT margin during FY22 over FY21. This apart, US generic market saw a steep rise in competition and consequent price erosion, which also impacted the profitability of Indian Pharma Industry during FY22. The US generic market saw a steep rise in competition and subsequent price subsequent price erosion (10-12%) which has also impacted the profitability of the Indian pharma sector during FY22. However, the negative impact of price erosion on profitability was partly offset by the depreciation of INR against USD.



Source: Ace Equity; Industry aggregates of over 165 Indian pharma companies compiled by CareEdge Ratings. These companies represent more than 85% of the overall pharma market.

PBILDT Margins to Taper in FY23

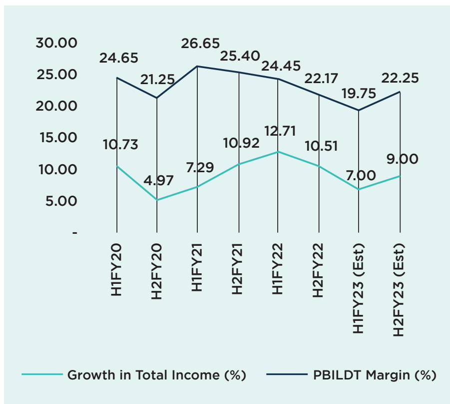
Presently, the industry is witnessing multiple challenges such as rising prices of active pharmaceutical ingredients (APIs) and key starting materials (KSM), the surge in solvent prices, a rise in freight and energy cost and continued pricing pressure in the US generic market. Due to supply chain disruptions and prevailing lockdown in China, the prices of some APIs/ KSM have increased between 25% to 120% while prices of excipients have risen between 15%-200% during the last 12-18 months. Apart from the cost of raw material, the cost of packing material also saw an upward movement of 25-100% during the past 12-18 months. The cost of power, fuel and coal witnessed a rise of more than 50% during the last one year while the cost of freight saw a jump of more than 2 times.

With the easing of travel restrictions, the US Food and Drug Administration (USFDA) has ramped up its regulatory inspection rates of pharmaceutical manufacturing facilities. During the past six months (January to June 2022), it has been observed that many Indian pharma companies have received Form 483 observations on their manufacturing facilities. Rising instances of audit observation by USFDA impacts the compliance cost and in turn hurts the profitability of the pharma sector. Any adverse observations from the regulatory authorities can also lead to a delay in the launching of new products or may even impact the current revenue stream, thus denting its prospects at least for the medium term. The ability of the Indian pharma companies to successfully sail through the inspections carried out by the regulatory authorities would be critical in determining their future growth plans and profitability margins.

Recently, India's drug pricing authority allowed a price hike of 10.7% for scheduled drugs which are under price control, considering the rise in the cost of production. This is the highest price hike allowed by it during the past many years which is expected to support the profitability of the pharma sector to an extent. Further, the pace of price erosion in the US market is likely to reduce to the mid-single digit in FY23. Furthermore, the recent sharp depreciation of INR against USD is also expected to support the profitability of the sector considering it is a net exporter.

Margins to Suffer

CareEdge expects the PBILDT margin of the sector to decline both on y-o-y and q-o-q basis to 19-20% in H1FY23 due to an increase in the cost of APIs and KSMs apart from increase in the cost of packing material, freight and compliance cost. It is likely that the PBILDT margin could rebound in H2FY23. CareEdge expects rupee depreciation to have a positive impact of nearly 100-150 bps on the PBILDT margin during FY23. On a full year basis, the PBILDT margin could shrink by 200-250 bps during FY23 over FY22 after considering the positive impact of rupee depreciation. Despite expected moderation in operating profitability in near to medium term, the credit profile of pharmaceutical companies is expected to remain strong due to their low reliance on external debt.



Y-o-Y Growth in Total Income (%) and PBILDT Margin (%)

INDUSTRY RESEARCH

5G AUCTION: TARIFF HIKES LIKELY AS TELCOS' DEBT NEARS Rs 6.2 TRILLION

Key Highlights

After 40 rounds and 7 straight days of bidding, the 5G spectrum auction concluded on August 1, fetching over Rs 1.50 trillion, higher than the government's expectations.

Though most bands were sold at the reserve price, the telecom service providers, aided by path-breaking reforms announced by Union Cabinet in September 2021, actively participated in auctions.

With an annual instalment outgo of Rs 13,400 crore towards the spectrum purchase and an investment outlay estimated at Rs 3 trillion in the next three years (FY23-25), the aggregate debt levels of the industry could surge by nearly 30% to Rs 6.20 trillion (including financial lease obligations) by end of FY23.

CareEdge expects successive tariff hikes by operators in the next 9-12 months, along with a levy of premium charges for 5G subscribers. This could cumulatively increase the average revenue per user (ARPU) by ~ 25% by H1FY24.

Bidding Touches All-time High

India's leading telecom operators Reliance Jio Infocomm Limited (Jio) and Bharti Airtel Limited (Airtel) emerged as the front runners in the spectrum auction, which saw 51.23 GHz, nearly 71% of the total 72.09 GHz, being sold. Contributing around 87% to the government's all-time high revenues for the total airwaves sold on a provisional basis, the two operators are now expected to possess a pan-India 5G network. The auction saw Jio acquire 220 MHz in the high-priced 700 MHz band at Rs 39,270 crore for efficient service coverage. Airtel and Vodafone Idea Limited (VIL) too acquired spectrum in the low-band airwaves.

The 3.3 GHz and 26 GHz (mmWave) bands witnessed maximum sales in the auction by the three TSPs and a modest bid by a new entrant, Adani Data Networks Limited (ADNL). As the 26 GHz band is primarily used for non-public networks and fixed wireless access, ADNL is expected to utilise the spectrum to deploy captive non-public networks across six circles of Andhra Pradesh, Gujarat, Karnataka, Mumbai, Rajasthan and Tamil Nadu. Meanwhile, Jio was the sole purchaser in the 700 MHz band, which is considered a premium band below 1 GHz, as it would help the operator cut

Bidder-wise Spectrum Quantity and Amount Payable

Particulars	Amount (in Rs. Cr)	Spectrum Won (In MHz)	% of Total Spectrum Sold
Jio	88,078	24,740.00	48.29
Airtel	43,084	19,867.80	38.78
Vi	18,799	6,228.40	12.16
Adani	212	400.00	0.78
Total	**1,50,173**	**51,236.20**	**100.00**

costs and provide better network coverage. The same was assisted by the decrease in the reserve price of the band by around 40% from the base price of 2021.

The bidding was led by Jio purchasing 48.29% of the total spectrum sold, followed by Airtel at 38.78% and VIL at 12.26%, in its 17 priority circles. Purchase of spectrum in the low-frequency bands (600 MHz, 700 MHz, 800 MHz, 900 MHz, 1800 MHz, 2100 MHz, 2300 MHz, 2500 MHz) will enable the telcos to increase coverage and reduce network congestion in 4G network, while purchasing in the mid- and high-frequency bands (3.3 and 26 GHz) will enable the operators to offer 5G services, which is envisaged to be sufficient to deploy 5G services across all circles by the government.

The hammer price in all spectrum bands remained at the reserve price, except for the 1800 MHz band, which garnered intense bidding for the UP (East) circle that accounts for over 100 Mn subscribers. The same resulted in an increase in the per unit price of the band by nearly 80% from the base price of Rs 91 crore to Rs 163 crore. The average unit price (i.e. per MHz spectrum) payable by TSPs to the government has gone down abysmally low at Rs 2.93 crore in the concluded auction as against Rs 90.95 crore in March 2021 auction.

Rollout of 5G Networks and Allied Investment – High Leverage Imminent

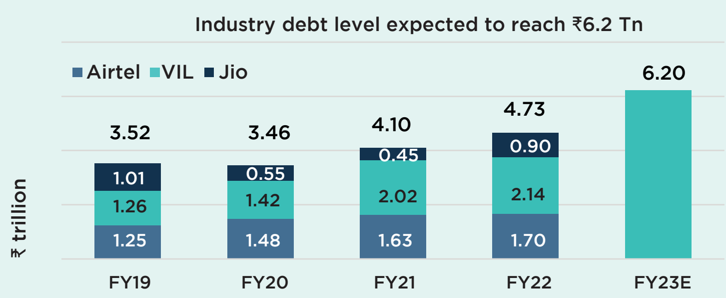
The rollout of 5G services would begin from October 2022. While the purchased spectrum is sufficient for coverage across the country, the achievement of complete coverage is expected to take a couple of years. This will necessitate an incremental investment outlay pegged at around Rs 3 trillion. Considering the TSPs shall opt for payments spread across the life of the spectrum i.e. 20 years, the aggregate annual instalment towards the spectrum purchase is estimated at an additional Rs 13,400 crore.

Considering the large quantum of investments required in the next two-three years, the TSPs are likely to witness an increase in leverage levels. CareEdge estimates the aggregate debt levels for the major TSPs to touch Rs 6.20 trillion by March 2023, an increase of about 30% from debt levels of ~Rs.4.73 trillion as on March 31, 2022.

While telcos are likely to charge a premium on 5G rollouts, CareEdge expects steep tariff hikes to be announced in their existing 4G plans as well, to recover their large investments made through bidding.

Given the demonstrated support of the government and the sector's rising appetite for growth capex, CareEdge outlook for the telecom sector continues to be 'Stable' with a positive bias. The TSPs are expected to witness an increase in their leverage levels with a significant capex outlay. For now, the sector is started making the right waves, but the real litmus test will be their ability to raise tariffs in the medium-term and retain market shares to support their credit profiles.

Debt Levels of Major TSPs



Sources: Company annual reports, CareEdge

INDUSTRY RESEARCH

TWO-WHEELERS' FY23 SALES TO RISE, MARGINS TO STAY UNDER PRESSURE

Key Highlights

After three years of consecutive decline, two-wheeler manufacturers are likely to see a sales volume growth of 6-6.5% in FY23 as rural and personal mobility demand grows.
The recovery in demand could have been higher, but supply-chain disruptions and high inflation (wholesale price increase of over 20%) hurt consumer sentiment.

Higher commodity costs and transition to BS-VI norms led to slow demand in the past three fiscals.
The PBIDLT margins could remain under pressure in FY23 unless a reversal in the input cost with the softening of commodity prices along with price hikes offers some cushion. CareEdge believes overall margins are expected to decline by 50-70 bps.

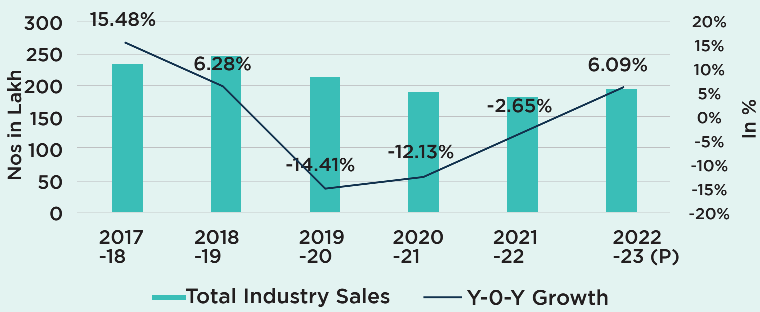
Bumpy Road Ahead amid Improving Macros

Two-wheelers sales fell by a compounded annual growth rate (CAGR) of 10% from FY19 to FY22 as lower rural demand amid Covid-19 induced economic slowdown, restricted mobility, and higher vehicle and fuel costs hurt. The transition to BS-VI in FY21, which led to a consequent price hike, also dampened demand sentiment.

Though the Covid-led restrictions eased in FY22, two-wheeler sales fell 2.65% y-o-y to 179 lakh units on account of extended work-from-home trend and slower ramp-up in the rural economy. The month-on-month volume moved in tandem with Covid cycles as reflected in April 2020 (Covid 1.0) and Q1FY22 (Covid 2.0). There was some respite in Q2FY22 and Q3FY22 as the pandemic waned and the festive season brought some cheer but from December 2021, commodity inflation again slowed demand.

In Q1FY23, the improving rural demand supported m-o-m volumes and led to a 37% jump, with the top four players, who hold over 85% market share, registering an average growth of 39% against Q1FY22.

Two-wheeler Sales Trend



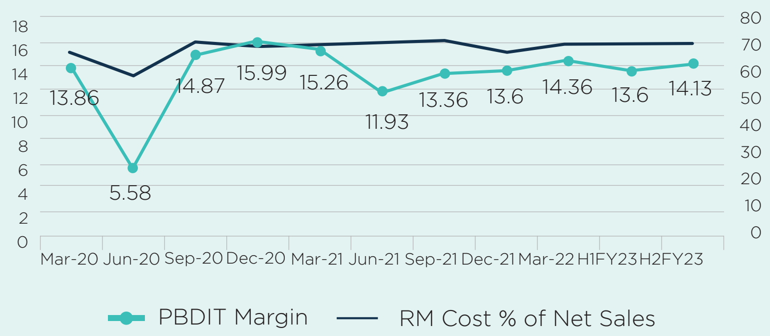
Electric Vehicle Traction to Drive Overall Volumes

Although the electric vehicle (EV) two-wheeler sales recorded a sharp growth of 61% in FY22, they accounted for only 1.3% of the total two-wheeler sales during the period. The recent surge in the demand for electric two-wheelers will support the overall sales of two-wheelers in FY23. The cost of an entry-level commuter Internal Combustion Engine (ICE) two-wheeler ranges between ₹50,000 and ₹65,000, while a high-speed EV two-wheeler costs anywhere between ₹90,000 and ₹100,000, restraining a large-scale shift towards EVs. However, in the short run, low fuel and ownership costs, low maintenance, along with the improving charging infrastructure, are likely to ensure a speedy transition towards EVs, along with extended subsidies maintaining the price band.

PBILDT Margin to Remain Under Pressure

The input prices for manufacturing two-wheelers have risen sharply since the start of the Russia-Ukraine war in Q4FY22. Raw materials like steel and aluminium were around 20.61% and 52% higher, respectively, in March 2022, on a y-o-y basis. Besides, the prices of other commodities used in the manufacturing of two-wheelers, such as rubber, paint, and plastic have also increased resulting in higher raw material costs for two-wheeler manufacturers. Also, despite the price hike taken by OEMs, the margins were impacted in Q4FY22, which reported a y-o-y decline by 90 bps.

Margin vs RM Cost



Source: CMIE, CareEdge, includes three-wheelers

Volumes to Rise, but Margins May Come Under Pressure

CareEdge expects the volume growth for the two-wheeler industry to be in the range of 6%-6.5%, with an increase of 1.12 lakh units in FY23, including exports, driven by improved mobility, pent-up demand, and improving consumer sentiments. The improvement in the rural demand, supported by a normal monsoon and the softening in input costs, is likely to drive healthy volume growth for domestic two-wheeler companies in FY23, as visible from Q1FY23. Despite volume growth, the margins are expected to remain under cost pressure due to the high commodity prices. CareEdge expects the PBIDLT margin to decline in H1FY23 by 76 bps on account of the higher raw material costs. The H2FY23 margins are expected to revive moderately by 53 bps as compared with H1FY23 with the expectation of the continued softening of input costs and the expected price hikes by the original equipment manufacturers.

ECONOMY DASH BOARD

HEAT MAP AND PROJECTION TABLE

		Jan-22	Feb-22	Mar-22	Apr-22	May-22	Jun-22	Jul-22	Aug-22	Sep-22
PMI-M	Unit	54.0	54.9	54.0	54.7	54.6	53.9	56.4	56.2	55.1
PMI-S	Unit	51.5	51.8	53.6	57.9	58.9	59.2	55.5	57.2	54.3
GST Collections	Rs lakh crore	1.4	1.3	1.4	1.7	1.4	1.4	1.5	1.4	1.5
E-Way Bill	Crore	6.9	6.9	7.8	7.5	7.4	7.4	7.6	7.8	
Air Passenger Traffic	Crore	1.5	1.8	2.4	2.4	2.7	2.5	2.4	2.5	
Railways Passenger Traffic	Crore	34.5	41.4	48.4	45.6	50.1	50.1	51.6	54.0	54.8
PV Sales	Lakh	3.0	3.1	3.4	3.0	3.1	3.3	3.5	3.4	
2-3 Wheeler Sales	Lakh	15.7	14.8	16.1	16.1	16.6	17.4	17.8	19.1	
Tractor Sales	Lakh	0.6	0.6	0.8	1.0	0.9	1.1	0.7	0.6	1.3
IIP	y-o-y%	2.0	1.2	2.2	6.7	19.6	12.7	2.4		
Core Sector	y-o-y%	4.0	5.8	4.8	9.6	19.3	13.2	4.5	3.3	
Power Consumption	y-o-y%	1.1	4.5	5.9	11.5	23.2	16.2	2.3	0.6	11.3
Petroleum Consumption	y-o-y%	2.3	5.4	6.5	9.6	23.7	17.9	6.1	16.3	8.1
Outstanding Bank Credit - Total	y-o-y%	8.2	7.9	8.6	11.1	12.1	13.2	14.5	14.3	
Capital Goods Import	y-o-y%	24.6	14.5	18.8	17.1	17.2	18.6	27.4	26.5	
Merchandise Exports	y-o-y%	27.9	34.5	26.4	29.2	21.0	30.4	2.1	1.6	-3.5

Note: Data for some indicators are high in April-June quarter due to base-effect

Indicator	FY18	FY19	FY20	FY21	FY22	FY23 Forecast
Gross Domestic Product (y-o-y%)	6.8	6.5	3.7	-6.6	8.7	6.9
CPI Inflation (y-o-y%)	3.6	3.4	4.8	6.2	5.5	6.5
Fiscal Deficit (as % of GDP)	3.5	3.4	4.7	9.2	6.7	6.5
Current Account Balance (as % of GDP)*	-1.8	-2.1	-0.9	0.9	-1.2	-3.6
Rupee (USD/ INR) (year-end)	65.0	69.2	75.4	73.5	75.8	81-83
10-Year G-Sec Yield (%) (year-end)	7.3	7.5	6.1	6.3	6.8	7.5-7.75

*** Note: (-) Deficit / (+) Surplus**

ABOUT US

CareEdge is a knowledge-based analytical group that aims to provide superior insights based on technology, data analytics and detailed research. CARE Ratings Ltd, the parent company in the group, is one of the leading credit rating agencies in India. Established in 1993, it has a credible track record of rating companies across multiple sectors and has played a pivotal role in developing the corporate debt market in India. The wholly-owned subsidiaries of CARE Ratings are (I) CARE Advisory, Research & Training Ltd, which offers customised advisory services, credible business research and analytical services (II) CARE Risk Solutions Private Ltd, which provides risk management solutions.

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