Q3 RESULTS PREVIEW

# SMEs may show weaker performance

## Analyses of samples indicate moderation in net sales, profit, beside operating margins

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Small and mid-cap companies (SMEs) are expected to show poorer results in the third quarter, based on an analysis of the results' preview by 14 brokerages. Net sales may increase by 19 per cent for the mid-cap and moderate to around 12 per cent for the small-cap. The mid-cap firms are expected to report a marginal drop in net profit; for small-caps, it could decline 28 per cent. The operating margins will remain under pressure, with a possible decline of at least 100 basis points for both categories.

The 44 SMEs that had announced their third quarter results till January 16 were in line with the projection of the 14 brokerages noted here. Despite aggregate net sales having risen 19 per cent, 44 SMEs have reported a 16 per cent decline in net profit in the quarter. The decline is much sharper, 66 per cent, if we exclude three banks — IndusInd, South India Bank and DCB — from the sample. However, the profit performance has also been skewed on account of four companies that reported a combined net loss of ₹174 crore in the quarter.

Among small-cap companies, SpiceJet, CCCL and Bharti Shipyard are expected to report net losses. Among mid-cap, Jet Airways, Tata Chemicals, MTNL and Suzlon would be reporting net losses. Ashok Leyland, which reported a significant downturn in net profit in the first and second quarters, is likely to be a star performer, with net profit growth of 100 per cent in the third quarter. The profit growth rate would be higher for Bharat Forge, Carborundum Universal, ING Vysya, Federal Bank, Alstom Projects, India Cement, Shree Cement, Britannia Industries and Marico.

The third quarter preview by 14 brokerages hints at 18 per cent growth in net sales for the corporate sector (sample of 352 companies), excluding oil marketing companies. The rate of growth of the sample companies would be much slower compared to the 23.6 per cent in the second quarter and 29 per cent achieved in the first quarter of this financial year. The net profit of the total sample is expected to be four to five per cent, marginally higher compared to the second quarter (down 1.4 per cent), but significantly weak compared to the first quarter (up 19.7 per cent).

Crisil Research expects year-on-year (y-o-y) revenue growth of 14-15 per cent in the quarter, as compared to a far healthier 22.5 per cent in the same quarter of 2010-11. Citigroup Research expects Q3 to finally signal a marked slowing in demand, with sales growth to moderate from 20-plus per cent to 12 per cent.

Ebitda (earnings before interest, taxes, depreciation and amortisation) margins should decline by 100-200 basis points, mainly on account of slower volume growth and high cost of inputs, coupled with limited pricing flexibility. Companies with substantial debt on their balance sheet will be further hurt by increased interest costs and mark-to-market losses (writing down securities to rflect current values) reported on foreign currency debt and derivatives due to the depreciation of the rupee.

The brokerages have analysed 355 companies, of which 147 are from the mid-cap and 86 from the small-cap universe. The growth rate has been calculated by taking the average for each company studied here and then aggregating these to arrive at the final figure.

### UNDER PRESSURE

**Slowdown in demand may hit stocks**

| | Growth rate in sales | | | Growth rate in net profit | | |
|---|---|---|---|---|---|---|
| | Q1 | Q2 | Q3E* | Q1 | Q2 | Q3E* |
| Small-cap (86) | 14.37 | 14.09 | 11.56 | 16.20 | -37.90 | -27.97 |
| Mid-cap (147) | 26.96 | 20.93 | 18.92 | 20.81 | -16.68 | -4.30 |
| Large-cap (119) | 29.18 | 23.12 | 17.21 | 19.56 | -7.84 | 5.08 |
| Total sample (352) | 28.98 | 23.58 | 18.10 | 19.69 | -1.38 | 4.41 |

In brackets: Sample size; * based on estimates of 14 brokerages, ex- three oil marketing companies