

RESEARCH

India Strategy | Q3FY22 Review

Growth blunts cost inflation

BOB Economics Research | CPI

CPI touches 6%

Reliance Industries | Target: Rs 2,520 | +8% | HOLD

Derisking the O2C business

SUMMARY

India Strategy: Q3FY22 Review

- 84% of Nifty 200 stocks either beat or met Q3 consensus revenue estimates but less than 60% did so at the net income level
- BFSI, IT, industrials and metal sectors led the earnings beat while other sectors had an almost equal split between beats and misses
- We note visible improvement in business environment across the board though raw material inflation remains a headwind

[Click here for the full report.](#)

India Economics: CPI

CPI inflation rose to 6% in Jan'22 from 5.7% in Dec'21, led by food inflation (5.4% versus 4%). However, core inflation eased by 10bps to 6% due dip in prices under transport and communication, health and personal care items. Going forward, we expect core inflation to remain sticky due revival in domestic demand, and build of input price pressures as seen in WPI. We also expect inflation to overshoot RBI's estimates in FY22 and FY23. Despite this, we expect RBI to remain on hold for now, to support growth.

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Daily macro indicators

Indicator	10-Feb	11-Feb	Chg (%)
US 10Y yield (%)	2.03	1.94	(9)
India 10Y yield (%)	6.73	6.70	(3)
USD/INR	74.95	75.38	(0.6)
Brent Crude (US\$/bbl)	91.4	94.4	3.3
Dow	35,242	34,738	(1.4)
Hang Seng	24,924	24,907	(0.1)
Sensex	58,926	58,153	(1.3)
India FII (US\$ mn)	09-Feb	10-Feb	Chg (\$ mn)
FII-D	(94.9)	(4.7)	90.2
FII-E	(86.9)	(225.9)	(139.0)

Source: Bank of Baroda Economics Research

BOBCAPS Research

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Reliance Industries

- RIL plans to restructure a part of its O2C business to address climate risks and open up new opportunities for value addition
- Approach involves (i) conversion of carbon-intense feedstock into chemicals & clean energy and (ii) potential strategic partnerships
- We maintain our HOLD rating and TP of Rs 2,520

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Q3FY22 REVIEW

14 February 2022

Growth blunts cost inflation

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Beat on revenue but mixed result at net income level: To date, 97% of Nifty 200 stocks (by market cap) have reported Q3FY22 numbers. Our analysis of beats and misses against consensus estimates for these companies indicates that 41% of companies beat revenue estimates while 43% largely met expectations. Further, 43% of companies exceeded forecasts at the net income level while ~17% had inline earnings. Reported revenue during the quarter was 8% higher than consensus and net income was 6% higher.

BFSI, IT and energy sectors led the beat: The Q3FY22 revenue beat was driven by energy, financials and materials, while the earnings beat was led by IT, energy and financials. The banking sector saw visible improvement in both credit quality and overall profitability. Asset growth at ~11.2% YoY was robust. The IT sector performed well despite significant headwinds from salary hikes and attrition.

Robust growth: Our analysis of a wider set of Nifty 500 companies indicates that overall revenue increased 25% YoY and 10% QoQ in Q3FY22 while net income grew 32% YoY and just 3% QoQ. Revenue grew across the board, barring the financials, real estate and healthcare sectors. Net sales was 28% higher than the pre-pandemic quarter of Q3FY20 while net income was 113% higher.

Raw material cost inflation a clear headwind: Further analysis of Nifty 500 companies indicates that raw material costs posed a clear headwind, though companies were largely able to pass on the higher cost to end users.

Investment view: While we believe the private capex cycle is still ~1.5 years away (see our strategy note [Macro & Micro: India at takeoff point](#) of 11 Jan), we remain constructive on export-oriented sectors such as IT and chemicals. We also expect moderation in metals margin.

Reporting season trends

Nifty 500: Q3FY22	QoQ (%)	YoY (%)
Net sales	9.6	24.5
Raw materials	16.8	43.7
Salaries and wages	3.2	11.9
Interest expenses	1.7	-1.0
Net Profit	3.1	32.4

Nifty 200: Q3FY22	Revenue (%)	Income (%)
Beat	8.0	6.1

Source: Bloomberg, BOBCAPS Research



CPI

14 February 2022

CPI touches 6%

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Sonal Badhan

CPI hardens: CPI inflation accelerated further to 6% in Jan'22 from 5.7% in Dec'21 led by a pickup in food inflation (5.4% in Jan'22 versus 4% in Dec'21). This was mainly led by rebound in prices of vegetables (5.2% versus -3%). Vegetable prices also rose on wholesale basis with vegetable inflation (WPI) at 38.5% in Jan'22 versus 31.6% in Dec'21. Apart from this, in the CPI basket, prices of meat and fish (5.5% versus 4.6%), cereals (3.4% versus 2.6%), eggs (2.2% versus 1.5%), milk (4.1% versus 3.8%) and spices (4.7% versus 4%) also increased. Amongst these, similar trend was also seen in wholesale prices for cereals, pulses, eggs, meat and fish and milk. On the other hand, in line with the trend seen in WPI, prices of fruits moderated in the CPI basket as well (2.3% versus 3.5%). Prices of oils and fats too eased (18.7% versus 24.3%).

Core inflation eases: CPI excluding food and fuel, edged down by 10bps to 6% in Jan'22 (6.1% in Dec'21). This was led by 37bps drop in transport and communication index to 9.4% (from 9.7% in Dec'21), followed by health (24bps drop to 6.9% versus 7.1%) and recreation and amusement index (31bps drop to 7% from 7.4%). Even personal care and effect index (21bps drop to 3.5% from 3.7%) and housing (9bps drop to 3.5% versus 3.6%) moderated. Other components of core such as, clothing and footwear (+54bps to 8.8% versus 8.3%) and household goods and services (7.1% versus 6.8%) showed considerable inflationary pressure. Even in the WPI basket, wearing apparel is seeing upward pressure (3.7% increase in Jan'22 versus 3.4% in Dec'21). However, contrary dip in prices of health in CPI, prices of pharma products are seeing upward movement in the wholesale basket (4.3% versus 4.1%). Going forward, with revival in demand taking shape, we expect core to remain sticky till Mar'22.

Fuel inflation a respite: Fuel and light index eased to 9.3% in Jan'22 from 11% in Dec'21. On the wholesale level, fuel and power inflation has remained unchanged from last month at 32.3% in Jan'22. In the CPI basket, moderation was led by dip in prices of Kerosene (by PDS) to (-) 5.9% in Jan'22 from (-) 1.8% in Dec'21. Coal prices (-0.1% versus 1.3%) and other fuel items (-0.4% versus 0.8%) also fell. Coal prices have remained unchanged on the wholesale level (3.1% in Jan'22), while Kerosene prices have seen a similar easing (63% in Jan'22 versus 100% in Dec'21). On the other hand, at the retail level, electricity prices (0.1% versus 0%) and diesel excluding conveyance (1.1% versus -1.6%) picked up. In the WPI basket too, electricity prices have seen sharp pick up (15.7% in Jan'22 versus -0.2% in Dec'21).

Inflation to overshoot RBI estimates: RBI in its latest monetary policy statement kept the inflation estimate for FY22 unchanged at 5.3%, with Q4FY22 print estimated at 5.7%, despite significant changes witnessed in the international oil market. While during the Dec'21 policy crude was trading at US\$ 70/bbl, it is currently hovering around US\$ 95/bbl. Geo-political tension and revival in global demand, both have contributed to the upward movement of prices. We believe, the full pass through of input cost inflation is yet to be seen. We also expect transport and communication inflation to increase post State elections. Thus we estimate CPI to come in at 5.5% in FY22. Even in FY23, we expect CPI to range between 5-5.5%, higher than RBI's estimate of 4.5%.



HOLD
 TP: Rs 2,520 | ▲ 8%

RELIANCE INDUSTRIES | Oil & Gas

14 February 2022

Derisking the O2C business

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Announces blueprint for embracing new energy in O2C: With the development of a renewable energy portfolio (solar, use of biomass and hydrogen), RIL plans to repurpose syngas for the production of blue hydrogen and also aims to capture and monetise carbon in phase-1. As the company evolves its electrolyser ecosystem with cost-effective green hydrogen, it aims to once again repurpose syngas as a feedstock for chemicals.

Syngas subsidiary to involve strategic partners and investors: RIL is carving out a gasification business with a net asset value of US\$ 9.6bn as a separate subsidiary. It aims to structure the arm as a job work contractor to produce syngas, hydrogen and carbon for RIL and also to provide a minimum offtake guarantee. Management has guided for an initial valuation of US\$ 4bn for this subsidiary.

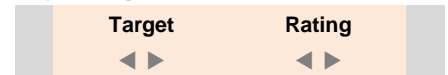
Upside from use of H2 as fuel: In the first stage, RIL expects the subsidiary to see valuation upsides from better utilisation of the syngas plant via production of blue hydrogen and carbon capture. RIL too will derive upsides from the shift away from fossil fuel as well as from monetising hydrogen and carbon.

Upside from use of syngas as feedstock: As green hydrogen becomes competitive and RIL's electrolyser ecosystem develops, the subsidiary will derive higher prices for syngas as a feedstock as against fuel use. Management plans to add value by expanding into the specialty chemicals chain, involving strategic partners and technology licensors.

Front-loading of value unlocking: RIL aims to tie up with strategic partners and investors to derisk the use of new technologies. The approach also helps unlock value at an early stage, as seen in the company's telecom and retail businesses.

Maintain HOLD: We retain our SOTP-based TP of Rs 2,520 which values RIL's refining business at 7.5x FY24E EV/EBITDA, petrochemicals at 8.5x, telecom (Jio Infocomm) at 10x and retail at 32x. Our TP includes Rs 111 for the value of its venture into digital services and Rs 47 for the new energy division.

Key changes



Ticker/Price	RIL IN/Rs 2,339
Market cap	US\$ 209.4bn
Free float	49%
3M ADV	US\$ 205.8mn
52wk high/low	Rs 2,751/Rs 1,877
Promoter/FPI/DII	50%/25%/14%

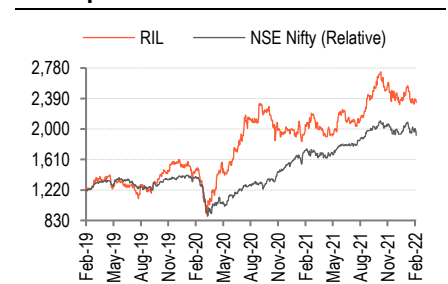
Source: NSE | Price as of 14 Feb 2022

Key financials

Y/E 31 Mar	FY21A	FY22E	FY23E
Total revenue (Rs mn)	46,69,240	68,85,377	79,00,553
EBITDA (Rs mn)	8,07,370	11,38,765	13,75,862
Adj. net profit (Rs mn)	4,36,628	5,82,093	7,18,765
Adj. EPS (Rs)	67.7	90.3	106.2
Consensus EPS (Rs)	67.7	87.7	112.3
Adj. ROAE (%)	7.6	8.0	9.1
Adj. P/E (x)	34.5	25.9	22.0
EV/EBITDA (x)	23.0	16.1	13.3
Adj. EPS growth (%)	(0.3)	33.3	17.6

Source: Company, Bloomberg, BOBCAPS Research

Stock performance



Source: NSE



Disclaimer

Recommendation scale: Recommendations and Absolute returns (%) over 12 months

BUY – Expected return >+15%

HOLD – Expected return from -6% to +15%

SELL – Expected return <-6%

Note: Recommendation structure changed with effect from 21 June 2021

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