Market snapshot

Equities - India	Close	Chg .%	CYTD.%
Sensex	80,425	0.0	11.3
Nifty-50	24,573	0.1	13.1
Nifty-M 100	57,761	0.2	25.1
Equities-Global	**Close**	**Chg .%**	**CYTD.%**
S&P 500	5,608	1.0	17.6
Nasdaq	17,877	1.4	19.1
FTSE 100	8,357	0.5	8.1
DAX	18,422	0.5	10.0
Hang Seng	6,226	1.0	7.9
Nikkei 225	37,389	-1.8	11.7
Commodities	**Close**	**Chg .%**	**CYTD.%**
Brent (US$/Bbl)	82	-0.6	5.3
Gold ($/OZ)	2,504	-0.1	21.4
Cu (US$/MT)	9,143	1.5	8.0
Almn (US$/MT)	2,414	4.1	2.9
Currency	**Close**	**Chg .%**	**CYTD.%**
USD/INR	83.9	-0.1	0.8
USD/EUR	1.1	0.5	0.4
USD/JPY	146.6	-0.7	3.9
YIELD (%)	**Close**	**1MChg**	**CYTD chg**
10 Yrs G-Sec	6.9	0.00	-0.3
10 Yrs AAA Corp	7.5	0.05	-0.3
Flows (USD b)	**19-Aug**	**MTD**	**CYTD**
FIIs	-0.3	-2.36	1.7
DIIs	0.21	4.49	35.6
Volumes (INRb)	**19-Aug**	**MTD***	**YTD***
Cash	1,166	1314	1295
F&O	2,87,900	3,62,762	3,77,755

Note: Flows, MTD includes provisional numbers.
*Average

Today's top research idea

EMS: PLI and Components: Crafting precision in every circuit

PLI and component manufacturing

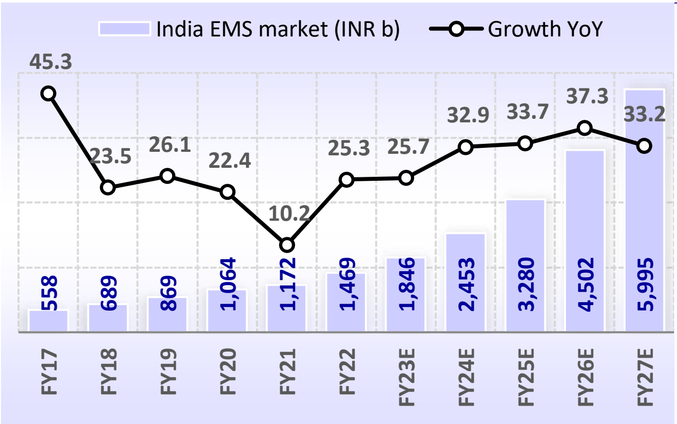
- India has successfully established a manufacturing presence in sectors like mobile phones and consumer electronics, and the next objective is to boost value addition. To further enhance localization and value addition in India, additional initiatives will be necessary to stimulate component manufacturing, an area where the government is already engaged in developing various schemes.
- Significant announcements are already being made in larger components such as semiconductor chips, display screens, battery chargers, and mechanical parts.
- This trend offers substantial growth opportunities for companies focusing on PLI and electronic manufacturing. We initiate coverage on Dixon Technologies (BUY) and Amber Enterprises (BUY) as these companies have already achieved market leadership in their key domains and are now concentrating on expanding their presence towards components.

Research covered

Cos/Sector	Key Highlights
EMS	PLI and Components: Crafting precision in every circuit
20th AGIC (Day 1)	CEO track
Consumer	Consumption tracker: Steady demand trend; pricing to further support growth
EcoScope	Are household finances in India a sign of distress or optimism?

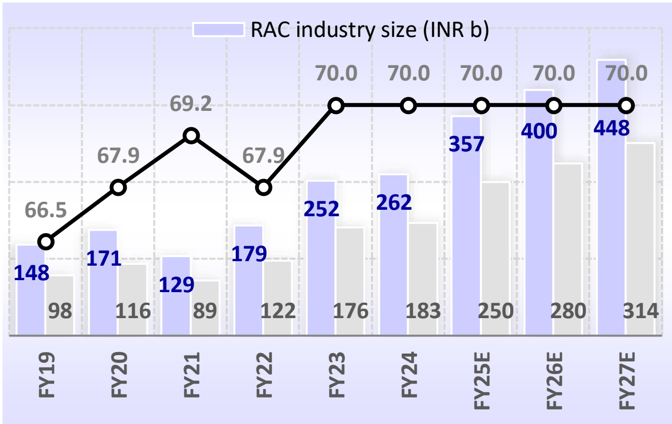
Chart of the Day: EMS (PLI and Components: Crafting precision in every circuit)

Domestic EMS market is expected to grow at a fast 32% CAGR over FY22-27



Source: MOFSL, Company

Share of RAC industry at OEM/ODM level stands around 70%



Source: MOFSL, Company

Research Team (Gautam.Duggad@MotilalOswal.com)

In the news today

Kindly click on textbox for the detailed news link

1

CPSEs capex still to recover, down 16% in April-July

Capital expenditure by the central public sector enterprises including departmental agencies (CPSEs) fell by 16% in aggregate in April-July, indicating that public capex is yet to recover from impact of general elections on project implementations.

2

Asean FTA review: India to seek more tariff cuts, tighter RoR

India is looking for further tariff cuts in key items of its export interest such as chemicals, metals and alloys, machinery, plastic and rubber, textiles, leather and gems and jewellery, as part of the "complete review" of the free trade agreement with ASEAN

3

July natural gas consumption up, output dips

India's natural gas consumption increased 5.8% YoY in July, while production fell 1.4%. Gas imports increased 14.8%, while NGC's natural gas production fell 3%. Private sector output remained flat.

4

Review of National Steel Policy begins

The NSP had set a target of 300 million tonnes (mt) of crude steel production by 2030. India's crude steel production stood at 143 mt in FY24, a rise of 12.6% from 127 mt in FY23. It has increased by around 42% since the launch of the NSP in 2017 when the country produced 101 mt of crude steel.

5

After a sober quarter, liquor companies hope for a Patiala high in second half

In India, the June quarter saw stable liquor demand with a decline in brandy and rum consumption. Despite a slight increase in whisky sales, the market faced supply chain disruptions due to elections and higher excise duties in Karnataka. Premium brands continued to show growth, boosted by younger consumers opting for higher-priced options.

6

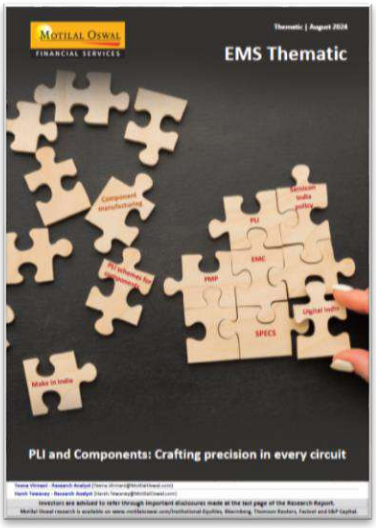
Mid-sized global restaurant chains find Indian market palatable

Recent months have seen several mid-sized global cafes and restaurant brands enter the Indian market or negotiate with local partners, despite declining sales for larger chains.

7

Diamond houses strive to win back choosy Chinese buyers, plan $8-10 mn campaign with DeBeers

Last week, a meeting of natural diamond houses was held in Mumbai to discuss the road ahead. They have overcome the sudden crunch during the financial meltdown of 2008-09, but are sensing a different challenge this time around.



PLI and Components: Crafting precision in every circuit

PLI and component manufacturing

India has successfully established a manufacturing presence in sectors like mobile phones and consumer electronics, and the next objective is to boost value addition. The government has already initiated various measures, such as the Production Linked Incentive (PLI) schemes and the Semicon India program, to promote electronic manufacturing in India. Additionally, the government has reopened the window for the PLI Scheme for White Goods to attract more investments. To further enhance localization and value addition in India, additional initiatives will be necessary to stimulate component manufacturing, an area where the government is already engaged in developing various schemes. Significant announcements are already being made in larger components such as semiconductor chips, display screens, battery chargers, and mechanical parts. This trend offers substantial growth opportunities for companies focusing on PLI and electronic manufacturing. We initiate coverage on Dixon Technologies (BUY) and Amber Enterprises (BUY) as these companies have already achieved market leadership in their key domains and are now concentrating on expanding their presence across different segments and backward integration.

Electronic industry is benefitting from government measures

The government has implemented several initiatives such as PLI, PMP, SPECS, EMC, and Semicon India to boost investments in the electronics and EMS industries. With these measures, electronics production moved up from $48b in FY17 to $101b in FY23. India's electronic manufacturing capacity is projected to reach $500b (finished goods $350b and components $150b) by FY2030 which would imply significant investments in enhancing the component ecosystem too. Currently, country has significant presence and capabilities of assemblers and OEMs in the electronics value chain such as Foxconn, Dixon, Amber, Pegatron, Apple, Samsung, BoAt, Atomberg, particularly in mobile and consumer electronics segments but is heavily reliant on imports for components and design capabilities across all sectors. A progress on component manufacturing is being initiated by few companies which will evolve more in the coming years.

Initiatives needed from government for developing entire eco-system

Component manufacturing has not shown the same growth as it requires an upfront initial capex and has lower asset turnover ratios with a gestation period of 1-2 years from investment to production. Hence, industry is seeking more initiatives from government to boost component manufacturing in India. Niti Ayog has recommended several measures to boost component manufacturing and India's positioning in the global electronics manufacturing and country's integration into Global Value Chains (GVC). These include 1) fiscal incentives for component manufacturing, 2) Incentives for investing in R&D, 3) tariff simplification, 4) soft infrastructure initiatives, 5) Tech transfer enablement and 6) setting up of industrial infra zones.

Electronic manufacturing is poised for a long-term growth

Backed by these measures, the domestic EMS industry is likely to grow to INR6.0t in FY27 from INR1.46t in FY22. This is expected to benefit the companies operating in this segment, such as Dixon Technologies, Amber Enterprises, et al. We believe that

Valuation metrics

Cos.	Mcap (INR b)	TP INR	Upside (%)
Dixon	8.8	15,000	21.0
Amber	1.7	5,000	21.0
Kaynes Tech	3.5	5000	-1.5
Syrma SGS Tech.	0.9	540	31.1
Cyient DLM	0.7	880	12.1
Avalon Tech	0.4	560	14.5

these companies have already attained a significant scale and market leadership and are now poised for backward integration through component manufacturing. To further boost localization and value addition in India, additional initiatives will be necessary to promote component manufacturing in the country, where the government is already working on various schemes.

Dixon Technologies: Pioneering the future of manufacturing and electronics

Dixon Technologies (DIXON) has emerged as a fast-growing diversified player in the electronics manufacturing services (EMS) industry. DIXON is a key beneficiary of several production-linked incentive (PLI) schemes for mobile phones, IT hardware, white goods, lighting, and AC components. It has consistently increased its market share in different segments through new technology tie-ups or new client additions. Its recent partnerships with: 1) HKC Corp for manufacturing of displays for mobile phones, TVs, and automotive, and 2) Longcheer Group for mobile phones, along with stake purchase of Ismartu, and sub-licensing arrangement with Google for TVs last year will help the company maintain its market leadership position. We expect DIXON to continue focusing on new segments, backward integration, ODM mix improvement, and operational efficiencies to boost its margins despite the rising revenue contribution from the low-margin mobile segment.

DIXON TECHNOLOGIES

Financials Snapshot (INR b)

Y/E March	FY25E	FY26E	FY27E
Sales	333.8	434.8	525.3
EBITDA	13.1	17.5	21.7
EBITDA Margin (%)	3.9	4.0	4.1
PAT	6.6	9.7	12.8
EPS (INR)	111.2	162.8	213.8
EPS Growth (%)	80.8	46.4	31.3
BV/Share (INR)	391.6	551.4	762.2
Ratios			
Net D/E	-0.3	-0.5	-0.6
RoE (%)	32.9	34.5	32.5
RoCE (%)	37.7	38.3	35.8
Payout (%)	2.7	1.8	1.4
Valuations			
P/E (x)	111.2	75.9	57.8
P/BV (x)	31.6	22.4	16.2
EV/EBITDA (x)	55.8	41.3	32.8
Div Yield (%)	0.0	0.0	0.0

Dixon Technologies: Financial outlook and view

We estimate a revenue/PAT CAGR of 44%/51% during FY24-27. We believe that an efficient working capital cycle, a focus on capital allocation, and higher asset turnover ratios should result in an RoE/ RoCE of 33%/36% by FY27E. We initiate coverage on the stock with a BUY rating and a DCF-based TP of INR15,000. Though valuations are on the higher side, strong industry growth drivers, presence in the fast-growing segments, possibility of adding more segments, and best-in-class RoIC will keep valuations higher.

Amber Enterprises: Moving beyond cyclicality

Amber Enterprises (Amber) is a leading player in ODM/OEM solutions for the Indian RAC industry. The company is one of the beneficiaries of PLI scheme with an early-mover advantage in PLI-led capex for RAC and AC components. With strategic diversification towards the high-growth electronics market (especially PCB manufacturing) and an increasing scope of work in the mobility segment, we expect Amber to benefit from margin improvement. We expect the company's transition from Amber 1.0 (AC-focused) to Amber 2.0 (electronics) and Amber 3.0 (mobility) to reduce business cyclicality and result in improved asset turnover and return ratios after the initial few years of capex.

AMBER ENTERPRISES

Financials Snapshot (INR b)

Y/E MARCH	FY25E	FY26E	FY27E
Sales	84.6	102.2	119.4
EBITDA	6.3	8.4	9.9
EBITDA Margin (%)	7.4	8.2	8.3
PAT	2.3	3.5	4.6
EPS (INR)	68.1	105.1	135.7
EPS Growth (%)	69.6	54.3	29.1
BV/Share (INR)	680.8	785.8	921.5
Ratios			
Net D/E	0.4	0.3	0.1
RoE (%)	10.5	14.3	15.9
RoCE (%)	9.8	12.1	13.4
Valuations			
P/E (x)	60.7	39.3	30.4
P/BV (x)	6.1	5.3	4.5
EV/EBITDA (x)	24.0	17.8	14.7

Amber Enterprises: Financial outlook and view

We estimate a revenue/EBITDA/PAT CAGR of 21%/26%/50% over FY24-27, which is likely to be driven by mid-teens CAGR in the consumer durable segment, high growth in the electronics and mobility segments, and a 100bp margin improvement over FY24-27. We initiate coverage on Amber with a BUY rating and a DCF-based TP of INR5,000, implying 42x P/E on two-year forward EPS (Sep'26E).

Key risks and concerns

The sector is poised for high growth in the coming years. Key risks to this growth could arise from slower-than-expected growth in electronic manufacturing, a slowdown in user industries such as consumer durables, mobile phones, and air conditioners, supply chain issues affecting the import of raw materials, changes in the government's priorities for the PLI scheme or semiconductor manufacturing, and a global slowdown that could detrimentally impact exports.

HDFC Bank

Mr. Sashidhar Jagdishan
CEO

Financials & Valuations (INR b)

Y/E March	FY24	FY25E	FY26E
NII	1,085	1,233	1,395
OP	944	1,017	1,167
NP	608	680	779
NIM (%)	3.4	3.5	3.5
EPS (INR)	80.0	89.6	102.5
EPS Gr. (%)	1.0	11.9	14.5
BV/Sh. (INR)	580	649	731
ABV/Sh. (INR)	555	622	699
Ratios			
RoE (%)	14.6	14.6	14.9
RoA (%)	1.8	1.8	1.9
Valuations			
P/E(X)	20.4	18.2	15.9
P/E(X)*	17.2	15.4	13.4
P/BV (X)	2.8	2.5	2.2
P/ABV (X)	2.5	2.2	2.0

* adjusted for subs

Building a sustainable franchise

Pursuing profitable growth; return ratios to expand gradually

We hosted Mr. Sashidhar Jagdishan, CEO of HDFC Bank, as a part of CEO Track at AGIC 2024. Here are our key insights from the session:

Transition phase underway; focusing on profitable growth

HDFC Bank is navigating through a significant transition after the merger with HDFC, with a focus on stabilizing and growing deposits. The bank has faced seasonal challenges related to the outflow in current accounts; however, the bank has sustained the momentum in deposits, with an emphasis on longer-term, more sticky retail deposits. The bank aims to address the imbalance between credit and deposit growth and is working to ensure that deposit growth matches or exceeds credit growth. Alongside, the bank aims for profitable growth rather than simply balance sheet expansion, and this strategy includes a deliberate reduction in LDR, faster than market expectations.

Focus on engagement over rate competition

HDFC Bank continues to prioritize customer engagement and service delivery over competition on deposit rates. This approach has allowed the bank to maintain disciplined pricing while winning customers through superior services. The bank's disciplined approach to deposit mobilization is reflected in its growing market share and the addition of 2.2m new relationships during the quarter. Monthly inflows across savings, salary, and current accounts have increased by 20% compared to last year, further solidifying its deposit base.

Borrowing mix to decline gradually

The bank has significantly reduced its borrowings, with a substantial decline of INR750b in 4QFY24 and INR600b in 1QFY25. This reduction includes a notable decrease in commercial papers as they matured. Moving forward, the bank plans to continue reducing its borrowings, with ~60% of the total borrowings scheduled to mature within the next three years. About INR600b of HDFC Ltd's high-cost borrowings will mature in FY25, of which ~INR250b were paid in the Jun'24 quarter. This strategic shift toward lower-cost deposits is expected to enhance liquidity and improve margins over time.

Pursuing profitable growth; cautious on unsecured retail before stress builds up

HDFC Bank's loan growth in 1QFY25 was not fully aligned with its strategic objectives. The bank focuses on maintaining resilience over the next three quarters, emphasizing the importance of strong customer relationships. In the home loan segment, the bank is working to increase the primary account relationships of its borrowers, with 85% of home loan borrowers already maintaining savings accounts with HDFC Bank. Growth in unsecured personal loans has been deliberately moderated, reflecting the bank’s strong understanding of market cycles, while aligning with the regulatory intent.

Investing for sustainable growth

HDFC Bank is making strategic investments with a focus on long-term growth, aiming to become an institution that stands the test of time. The bank envisions a legacy that spans over centuries, grounded in strong ethos and culture. With this vision, the bank is committed to investing for sustainable growth, acknowledging that it will take decades to reach its goals, much like the journey of public sector units (PSUs) that currently dominate the sector.

Near-term challenges, long-term opportunities

The recent merger has thrown some near-term challenges along with several long-term opportunities for the bank, which will enable it to continue to build shareholder value. The leadership team is focused on execution while remaining confident in the bank's ability to manage challenges effectively. The bank's model remains intact, with a proven ability to navigate through credit cycles, and a strong emphasis on maintaining profitability and strategic investments, particularly in technology, to drive growth across businesses. HDFC Bank is poised to sustain NIMs through a balanced product mix and growth strategy. Despite early indicators of rising stress in asset quality, the bank remains confident that it can manage risks effectively and continue its long-term growth trajectory.

Operational efficiency to aid long-term profitability

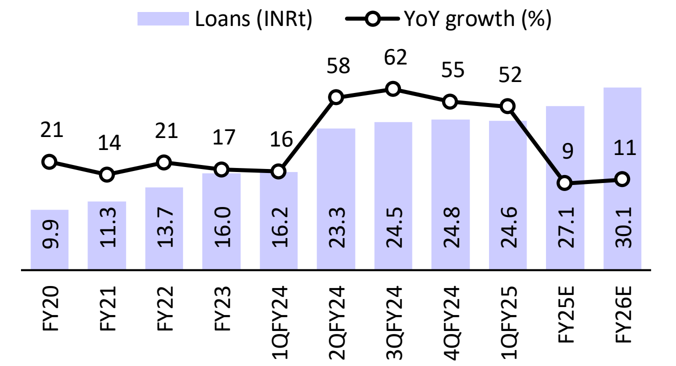
The bank is committed to stabilizing its cost-to-earnings ratio, with a focus on long-term targets rather than short-term pressures. Staff costs have increased due to recent additions to the workforce and ongoing compensation adjustments. Despite these pressures, the bank remains focused on maintaining operational efficiency and delivering consistent performance in a competitive environment.

Employee-First culture and Execution excellence

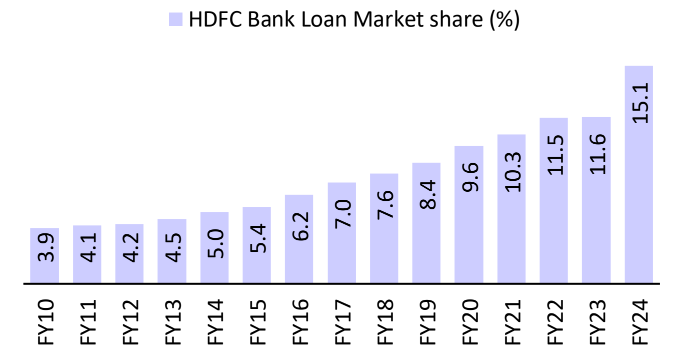
At the core of HDFC Bank's strategy is its commitment to an employee-first culture, ensuring that its workforce is well-prepared to manage complex situations. This ongoing process includes continuous training and a focus on the right attitude and ethos. The leadership's strategic thinking is deeply embedded in the bank's DNA, ensuring that the institution continues to thrive regardless of external challenges. This focus on execution is where the real opportunity lies, driving the bank's success.

Story in charts

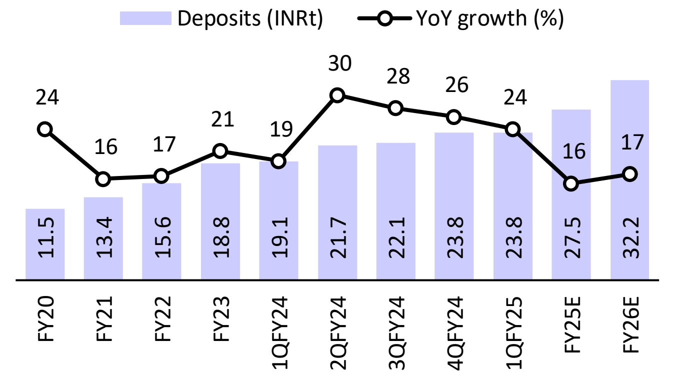
Estimate ~10% CAGR in loans over FY24-26E



Loan market share expands to 15.1%, post-merger

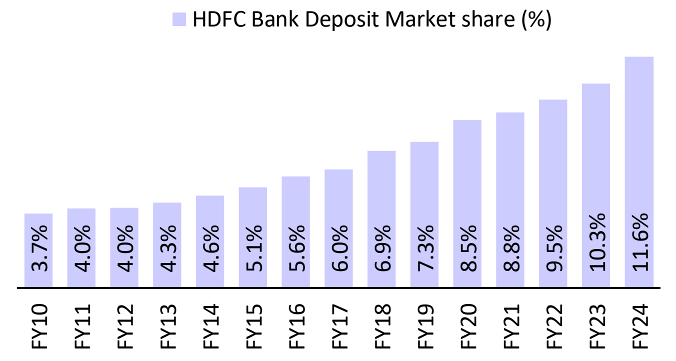


Est. 16% CAGR in deposits over FY24-26E



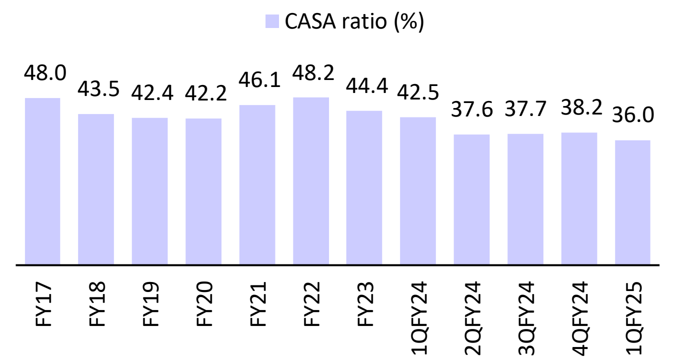
*2QFY24 and thereafter growth in on merged bais Source: MOFSL, Company

Deposit market share has improved to 11.6%



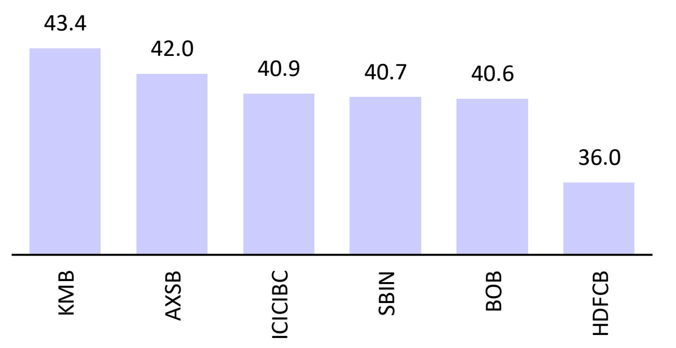
Source: MOFSL, Company

CASA ratio has moderated to 36% post-merger



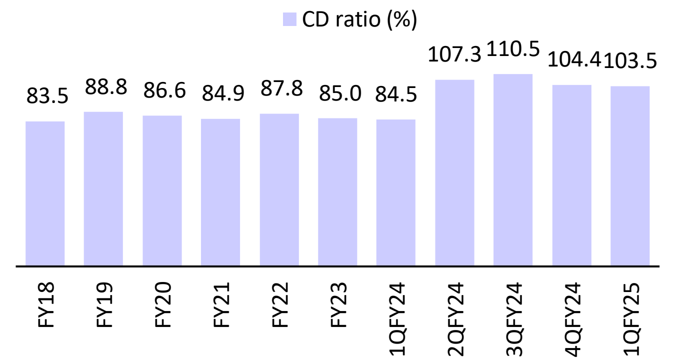
Source: MOFSL, Company

CASA ratio across peers – 1QFY25 (%)



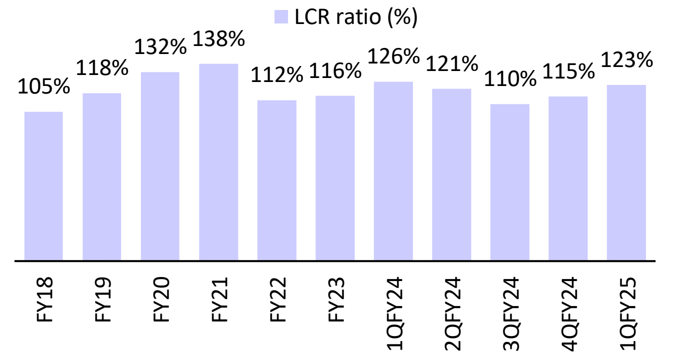
Source: MOFSL, Company

HDFCB aims to significantly improve its CD ratio by consciously maneuvering its business growth



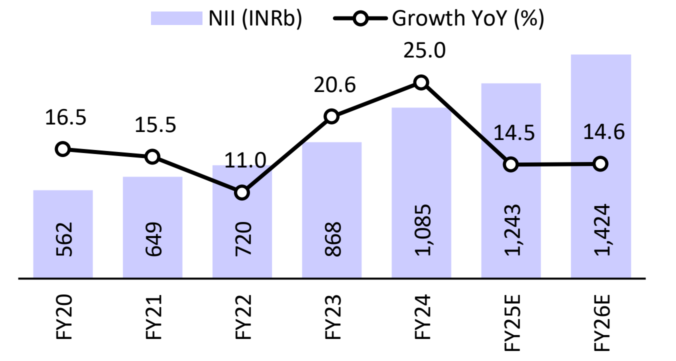
Source: MOFSL, Company

LCR ratio has improved to 123% in 1QFY25



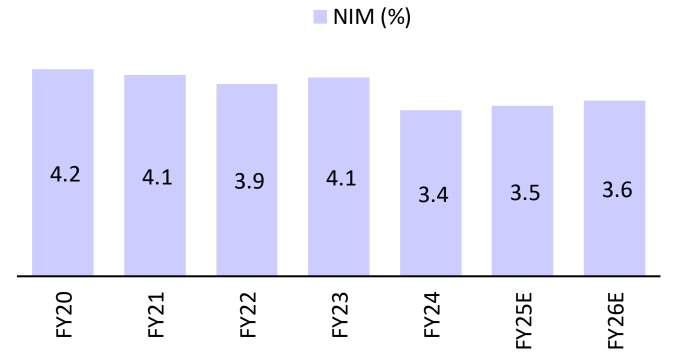
Source: MOFSL, Company

Estimate NII growth at ~15% in FY26



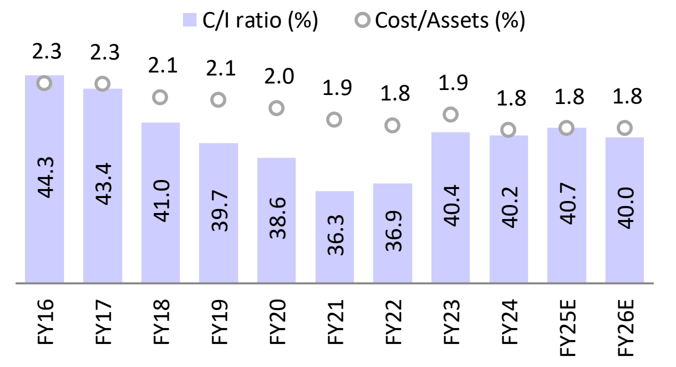
Source: MOFSL, Company

NIMs to remain range bound at 3.5-3.6%



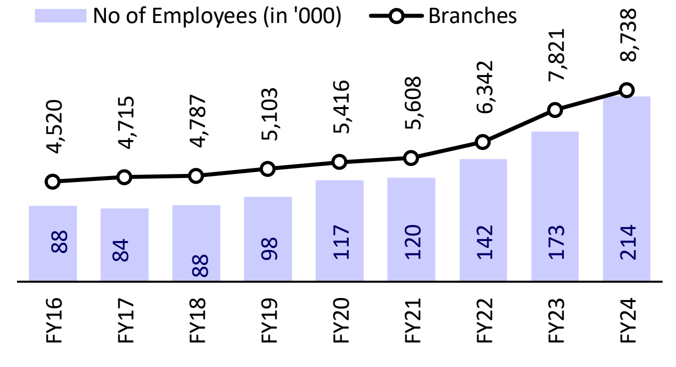
Source: MOFSL, Company

C/I ratio stands at 40.2% with cost/assets at 1.8% as on FY24



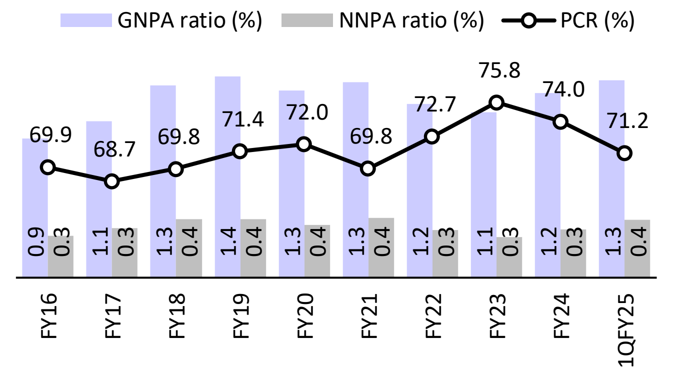
Source: Company, MOFSL

Bank added ~40k staff and ~917 branches in FY24



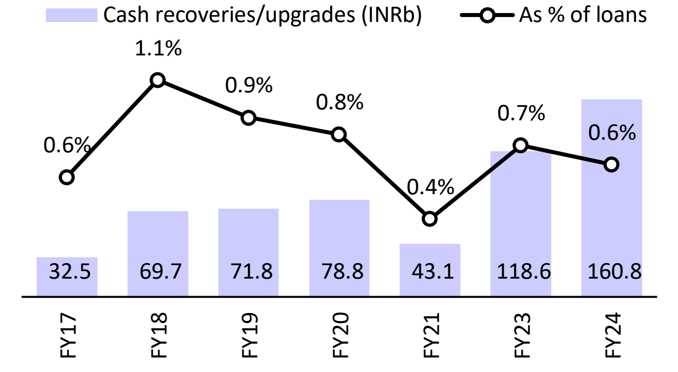
Source: Company, MOFSL

GNPA/NNPA ratios at 1.3%/0.4% in 1QFY25



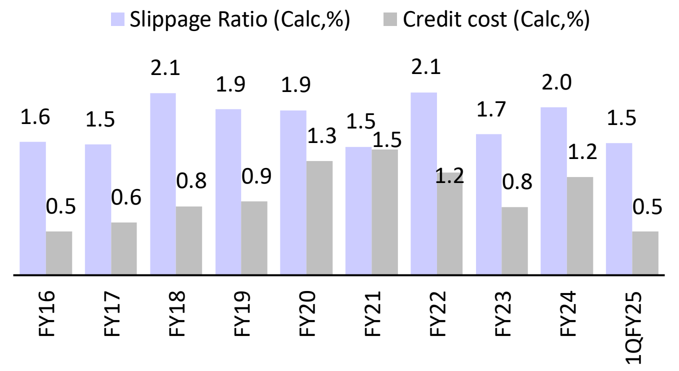
Source: Company, MOFSL

Cash recoveries/upgrade sstood at 0.6% of loans



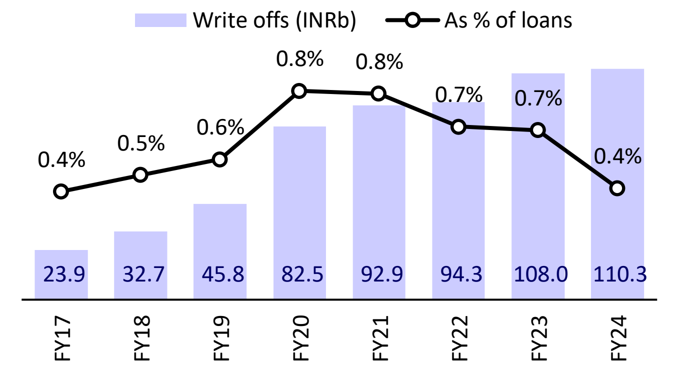
Source: Company, MOFSL

Slippage ratio, credit cost remainh under control



Source: Company, MOFSL

FY24 write-offs stood at INR110b (0.4% of loans)



Source: Company, MOFSL

Tata Steel

Mr. T V Narendran
CEO & MD - Tata Steel

Financials & Valuations (INR b)

Y/E MARCH	2024	2025E	2026E
Sales	2,292	2,387	2,601
EBITDA	223	338	403
Adj. PAT	34	123	171
EBITDA Margin (%)	9.7	14.2	15.5
Adj. EPS (INR)	2.7	9.9	13.7
EPS Gr. (%)	-61.8	263.9	39.4
BV/Sh. (INR)	69	74	81
Ratios			
Net D:E	0.9	0.8	0.8
RoE (%)	3.6	13.8	17.7
RoCE (%)	7.3	13.5	16.2
Payout (%)	133.0	50.8	51.0
Valuations			
P/E (x)	56.5	15.5	11.1
P/BV (x)	2.2	2.1	1.9
EV/EBITDA(x)	12.0	7.9	6.6
Div. Yield (%)	2.4	3.3	4.6
FCF Yield (%)	1.1	6.2	8.4

Tata Steel – Transforming for a sustainable tommorow

Tata Steel well placed to capitalize on strong domestic steel demand

We hosted Mr. T V Narendran, CEO & MD, Tata Steel, as a part of CEO Track at AGIC CY24. Here are our key insights from the session:

India steel demand to grow well aided by economic cycle

Steel demand in India has been robust, driven by strong consumption demand and government capex on infra projects in the last few years. As per industry estimates, steel demand is expected to rise from 136 MMT in FY24 to 200 MMT in FY30. This growth would be driven by a) increasing per-captive income, b) strong investments in infra development by the government, and c) increasing per-capita steel consumption, which is very low compared to other countries like China and USA.

Capacity expansion underway to capitalize on growth opportunity; value-added downstream products to remain key focus

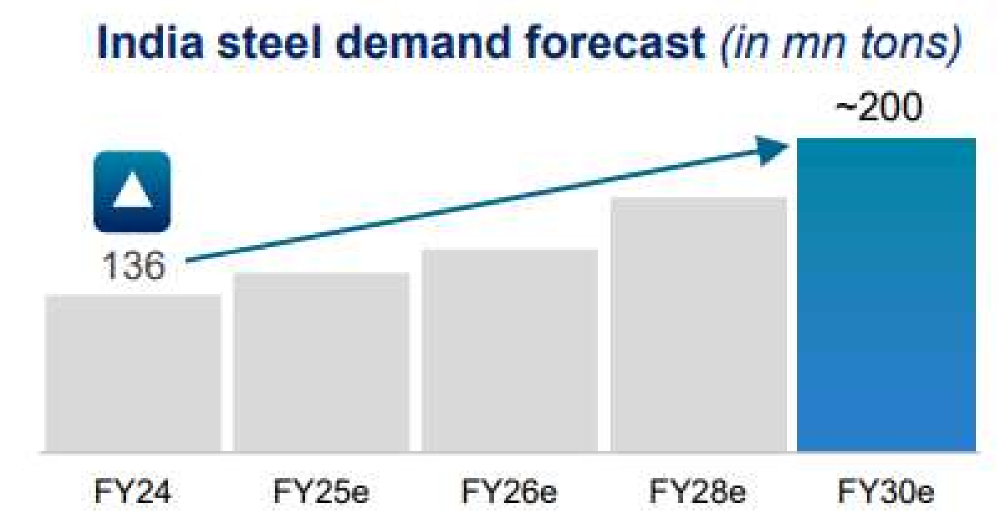
To capitalize on the upcoming opportunity, Tata Steel is expanding its India capacity by 2x to 40 MMT. It is expanding flat steel capacity from 16 MTPA to 27 MTPA and long steel Capacity from 5MTPA to 13 MTPA. Tata Steel would maintain its backward integration strength and enhance its Iron ore mining capacity from 38 MTPA to 60-65 MTPA to support the higher steel capacity. It is also adding 6 MTPA pellet capacity in Kalinganagar.

Along with the upstream capacity expansion, the company is also expanding its downstream capacity with expansion across Tubes, Wires, Tinplate and DI pipes segment. The focus remains on value-added downstream products to enhance profitability and reduce the impact of volatile commodity prices.

Focus on sustainability – Targeting Net Zero emissions at Tata Steel Group level by 2045

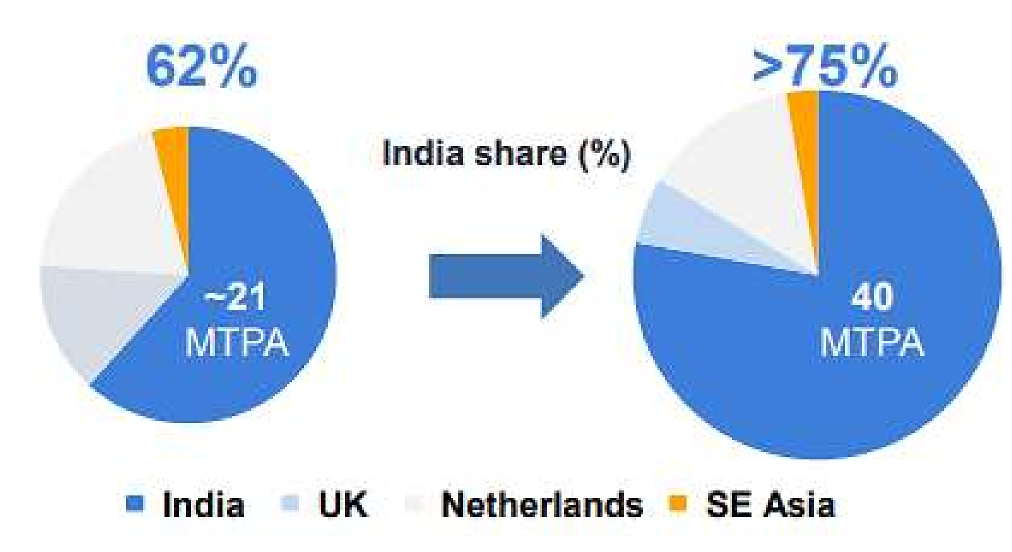
The company continues to focus on reducing its carbon footprint. It is taking multiple initiatives in this regard across India and other countries. At its UK facility, Tata Steel is transitioning to scrap-based EAF capacity and winding down the blast furnaces. The company is also focusing on green steel making in the Netherlands and is in discussions with the Netherlands Government. It aims to reduce carbon emissions by 30-40% by 2030. It is in discussion with the government and technology partners for the same.

India steel demand outlook



Source – Tata Steel Investor Presentation, Industry reports

Tata Steel's India capacity to double to 40 MTPA



Source - Tata Steel Investor Presentation

Godrej Consumer Products

Mr. Sudhir Sitapati
MD & CEO, Godrej Consumer Products

Financials & Valuations (INR b)			
Y/E March	2024	2025E	2026E
Sales	141.0	149.7	166.5
Sales Gr. (%)	5.9	6.2	11.2
EBITDA	30.7	33.9	37.9
EBITDA Margin. %	21.8	22.6	22.7
Adj. PAT	19.8	22.7	27.6
Adj. EPS (INR)	19.3	22.2	27.0
EPS Gr. (%)	13.2	15.1	21.3
BV/Sh.(INR)	123.3	128.5	136.5
Ratios			
RoE (%)	15.0	17.7	20.3
RoCE (%)	15.2	16.5	19.4
Payout (%)	77.6	76.5	70.5
Valuation			
P/E (x)	72.6	63.1	52.0
P/BV (x)	11.4	10.9	10.3
EV/EBITDA (x)	47.0	42.4	37.8

Focus on expanding TAM by innovation

We hosted Mr. Sudhir Sitapati, Managing Director and CEO, Godrej Consumer Products, as part of our CEO Track at AGIC 2024. Here are our key insights from the session:

Strategy for FY25

The company over the last 2-3 years has focused on simplifying the business process across its India and international businesses. It helped the company identify white spaces in India business (both at product and distribution level) and profitability improvement for international business. India business scalability is the top priority and hence, it is focusing on expanding the addressable market. The framework to enter into new categories includes category growth, operating margin and right to win for GCPL.

For FY25, GCPL has outlined a three-pronged strategy: 1) Premiumization, which involves launching premium innovations, entering new premium categories, and expanding premium channels; 2) Efficiency improvement, in which GCPL plans to enhance efficiency by investing in manufacturing capabilities and increasing media investments; and 3) Affordability in rural markets, in which the company aims to drive growth in rural areas by introducing access packs to cater to price-sensitive consumers.

Industry outlook

The demand trajectory is gradually improving. Rural markets have seen multiple challenges over the last two years as many headwinds affected overall consumption. Indian economic growth was 7-8% last year, but consumption growth was only 4%. Such growth divergence is higher than normal and there is high possibility of consumption growth recovery in the near term to medium term.

Strong focus on innovation will continue

GCPL has consistently introduced innovations across its categories. In FY24, the company launched Goodnight Agarbatti (Jan '24) using the RNF molecule, Godrej Fab Liquid Detergent priced at INR99, and Godrej Aer O car freshener. Each of these products is expected to generate over INR1b in revenue. New products together contribute ~4% additional volume growth in FY25. While the success of these innovations has varied, GCPL's strong pipeline for new products and effective go-to-market strategy provide an advantage in driving growth, especially in underpenetrated categories.

Positive momentum for RCCL business

Although RCCL revenue declined ~25% in FY24 due to its simplification initiatives, the underlying business momentum remains strong. The company is targeting to achieve INR6-6.5b in revenue in FY25. GCPL has gained significant market share in modern trade, e-commerce, and rural areas, but has lost some share in urban general trade (GT). Management is now returning to RCCL's previous strategy of focusing on GT channels, recognizing that cosmetic stores require more active selling than distribution. GCPL aims to achieve EBITDA of ~INR1.4-1.5b in FY25.

Foray into pet care to expand TAM in India

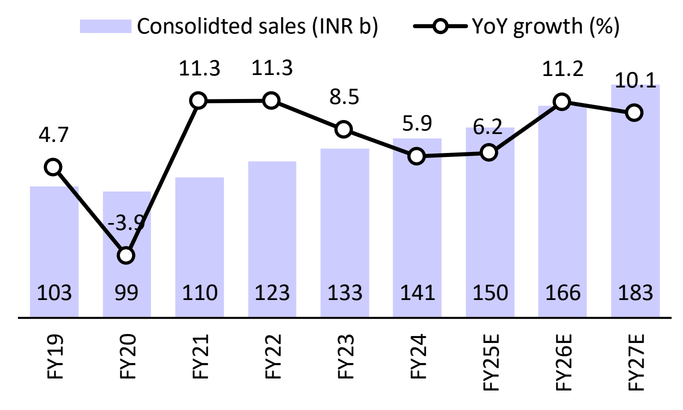
GCPL has launched Godrej Pet Care, entering the INR50b pet care market, which is a high-margin category globally (~40-50% gross margin, ~15-25% EBITDA margin). GCPL sees significant long-term growth potential in this space, expecting late-teens growth over the coming decades. The company believes its strong position in pet care is supported by Godrej Agrovet's market leadership in animal feeds, expertise in pet food, R&D capabilities, and supply chain advantages. The market is largely driven by top two brands, hence GCPL sees right to win in this category and looking to achieve high single digit market share. GCPL plans to invest INR5b in operating expenses over the next five years, aiming for the business to turn cash positive thereafter. Manufacturing is expected to start in 2HFY26E, given the long lead time for setting up capex. Mr. Nitin Jain has been appointed COO for the business.

Medium-term aspirations

The consolidated business will deliver high-single-digit volume growth with mid-teens EBITDA margin in FY25. Over the medium term, the company is looking to achieve high-single to low-double digit volume growth in India with healthy mix of pricing. EBITDA margin is expected to be in mid-high 20s. International business will continue to improve operating profitability by reducing overhead costs and closing down non-performing business.

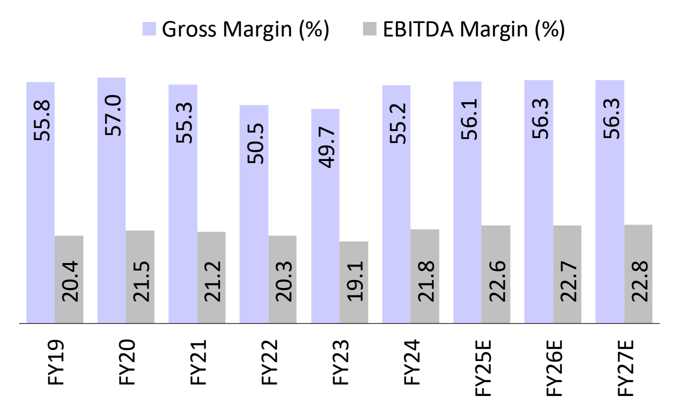
Story in charts

Revenue CAGR is expected at ~9% over FY24-27...



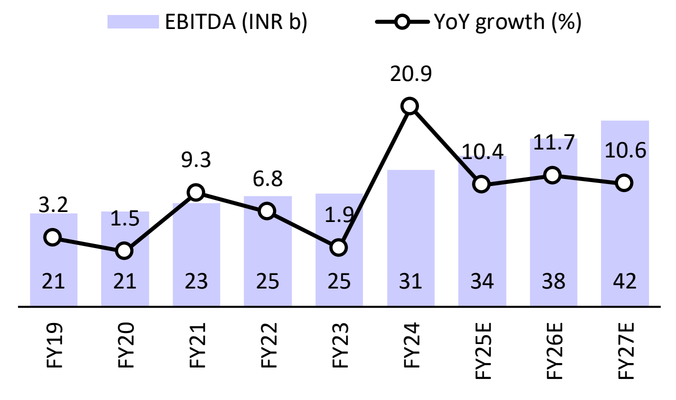
Source: Company, MOFSL

...with the stable margins



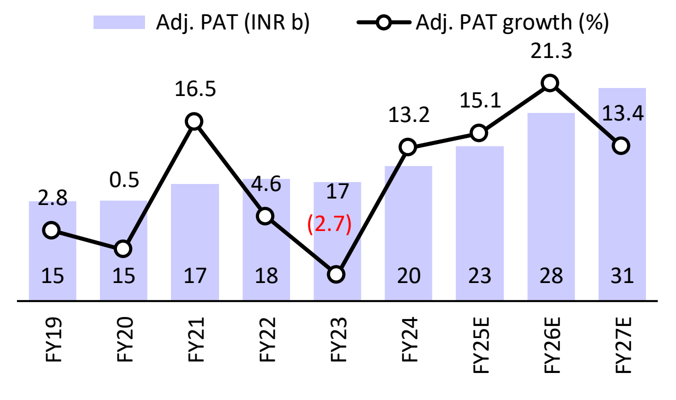
Source: Company, MOFSL

EBITDA expected to see ~11% CAGR over FY24-27E



Source: Company, MOFSL

PAT CAGR is expected at ~16% over FY24-27E



Source: Company, MOFSL

Hero MotoCorp

Mr. Niranjan Gupta
Managing Director & CEO,
Hero MotoCorp

Financials & Valuations (INR b)

Y/E March	2024	2025E	2026E
Sales	374.6	409.8	467.1
EBITDA	52.6	59.9	69.2
Adj. PAT	40.9	46.3	55.5
Adj. EPS (INR)	204.6	231.5	277.4
EPS Gr. (%)	40.5	13.2	19.8
BV/Sh. (INR)	900	960	1,037
Ratios			
RoE (%)	23.6	24.9	27.8
RoCE (%)	23.1	24.4	27.3
Payout (%)	73.3	73.4	72.1
Valuations			
P/E (x)	25.4	22.4	18.7
P/BV (x)	5.8	5.4	5.0
Div. Yield (%)	2.9	3.3	3.9
FCF Yield (%)	4.2	3.8	5.1

Premiumisation and EVs to remain key focus areas

New launch momentum to continue in FY25

We hosted Mr. Niranjan Gupta, MD & CEO, Hero MotoCorp, as a part of CEO Track at AGIC CY24. Here are our key insights from the session:

Indian 2Ws – huge growth potential ahead

India has the largest young population with a burgeoning middle class. Further, rising government capex is likely to drive higher income and hence higher discretionary consumption. This, in turn, is driving a noticeable shift in consumption patterns like EV transition and premiumisation. The premium segment has grown 20%+ in the last two years as today's youth have big aspirations. Even in 2Ws, India continues to have ample long-term growth potential as the penetration stands at 114 vehicles per 1,000 population, which is about 40% lower than its South Asian counterparts. The management believes that while EV penetration is likely to continue to pick up in scooters (expects around 50% EV penetration in scooters by 2030), the same in motorcycle is likely to take time as one would need a much bigger battery (2-3x) for the same performance.

HMCL is changing gears as well – in line with market trends

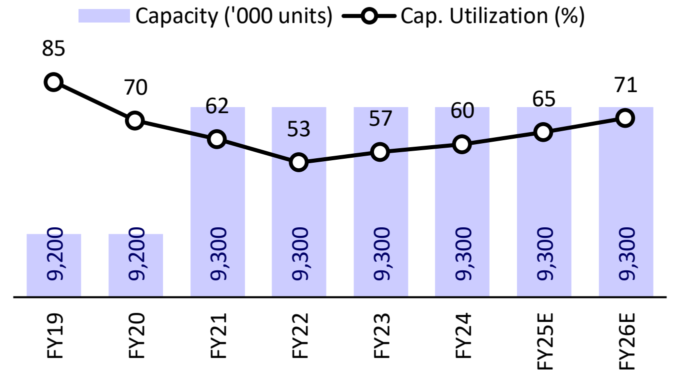
Over the last couple of years, HMCL has now shifted its focus in a bid to gain its presence in the 125cc + segment, in line with market trends. FY24 saw the highest number of new launches in the history of HMCL. More launches are expected to follow in FY25 (5 to 7 new products) as well, including in scooters and EVs (affordable). One critical aspect in new launches is to have at least one first-in-class feature and one best-in-class feature. HMCL targets to grow with collaborations like Harley Davidson (discussions are on to expand this further), Ather (partnership for charging points) and Zero (build and market Zero motorcycle EVs in India). Apart from the domestic focus, the company plans to ramp up its presence in exports as well. It would start Brazil operations in Q4FY25 and has already started dispatches to the Philippines in Mar'24.

Investing to build a premium brand

Apart from new product launches, HMCL is also focusing on enhancing its brand presence. It is now in the process of upgrading its existing dealerships to Hero 2.0 (target for 800 outlets to move to Hero 2.0 from 500 outlets currently from 20 in FY23). The company also plans to set up Premia Stores, which will house only premium vehicles (targets to set up 150 outlets in FY25 from current 42). HMCL is also investing in digital initiatives like DigiFin, which will make financing accessible and affordable to customers.

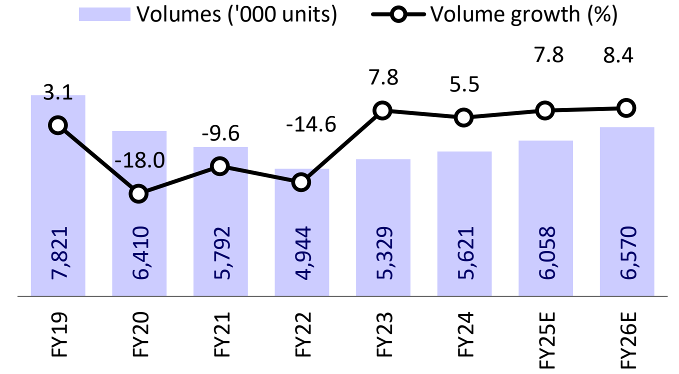
Story in charts

Adding capacity ahead of growth



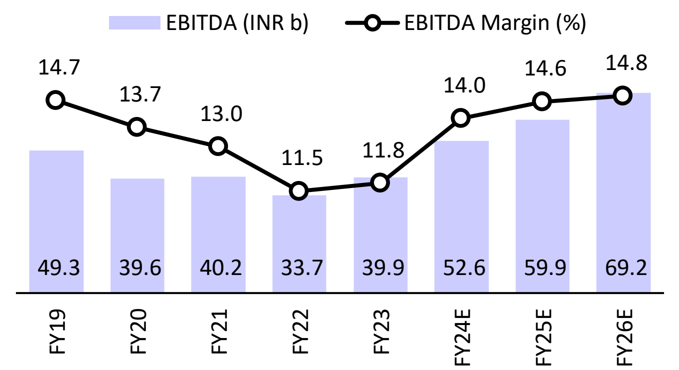
Source: Company, MOFSL

Volume sustainability led by rural recovery



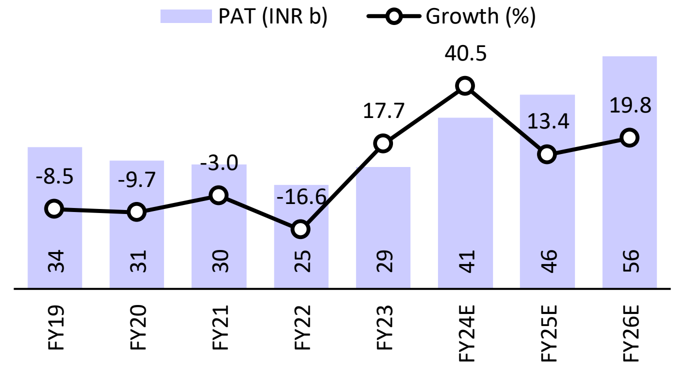
Source: Company, MOFSL

EBITDA margin trajectory



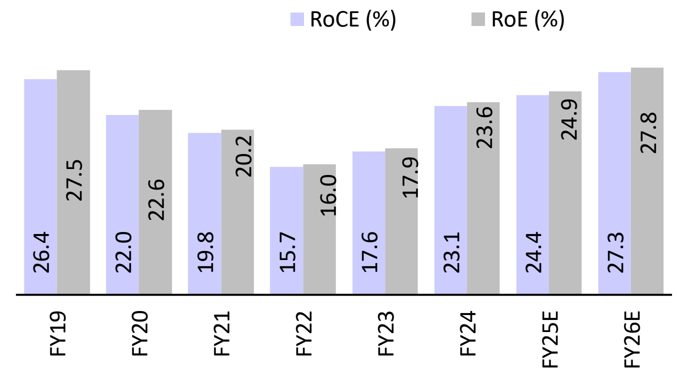
Source: Company, MOFSL

PAT growth to be steady



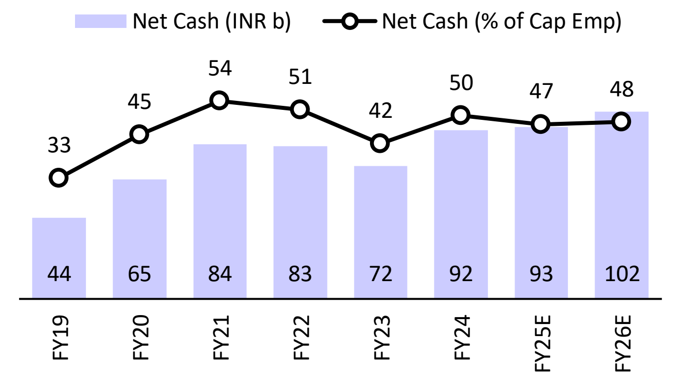
Source: Company, MOFSL

Trend in return ratios



Source: Company, MOFSL

Trend in cash levels



Source: Company, MOFSL

Bosch

Mr. Guruprasad Mudlapur
Managing Director, Bosch, and President, Bosch Group, India

Financials & Valuations (INR b)

Y/E March	FY24	FY25E	FY26E
Sales	167.3	178.4	203.4
EBITDA	20.9	23.4	28.0
Adj. PAT	18.3	21.7	25.7
EPS (INR)	620.5	736.5	872.0
EPS Gr. (%)	28.5	18.7	18.4
BV/Sh. (INR)	4,091	4,467	4,919
Ratios			
RoE (%)	15.9	17.2	18.6
RoCE (%)	20.6	21.8	23.6
Payout (%)	44.4	48.9	48.2
Valuations			
P/E (x)	52.2	44.0	37.2
P/BV (x)	7.9	7.3	6.6
Div. Yield (%)	1.2	1.1	1.3
FCF Yield (%)	1.0	1.1	1.4

India's evolving auto market: Shaping the road to 2030

Moving toward cleaner and sustainable options

We hosted Mr. Guruprasad Mudlapur, MD of Bosch and President of Bosch Group, India, as a part of CEO Track at AGIC CY24. Here are our key insights from the session:

Clean mobility, advanced tech, and global megatrends shaping 2030

The world is moving toward cleaner fuel, emphasizing the importance of clean, efficient, and safe mobility. Today's vehicles are significantly more advanced, incorporating cutting-edge technologies and features. China is leading the way in autonomous technology, setting a benchmark for others.

Several global megatrends are shaping the future, including the aim to achieve 50% renewable energy by 2030, backed by strong policy support. Additionally, the middle class is expected to see its per capita income double by 2030, and the population will increasingly consist of Gen Z and Millennials, who are heavily reliant on technology. Urban populations are projected to double by 2030, further influencing these trends.

Steady growth and electrification trend in India

The Indian auto market is poised for steady growth. Passenger vehicles (PVs) are expected to clock a 3.3% volume CAGR by 2030, with 21% of this market transitioning to EVs, driven by factors like total cost of ownership, premiumization, and a growing charging ecosystem. Light commercial vehicles (LCVs) are expected to post a 5.4% CAGR, with 20% EV penetration by 2030.

Heavy commercial vehicles (HCVs) are projected to see a 2% volume CAGR by 2030, returning to 2018 levels. The slower growth expectation for this segment is due to a change in mix toward higher-tonnage vehicles, improvements in general turnaround time for fleet operators, phased implementation of DFC and increased load-carrying capacity. Further, EV penetration in this segment is expected to reach 6%.

Strategic investments powering tech advancements in India

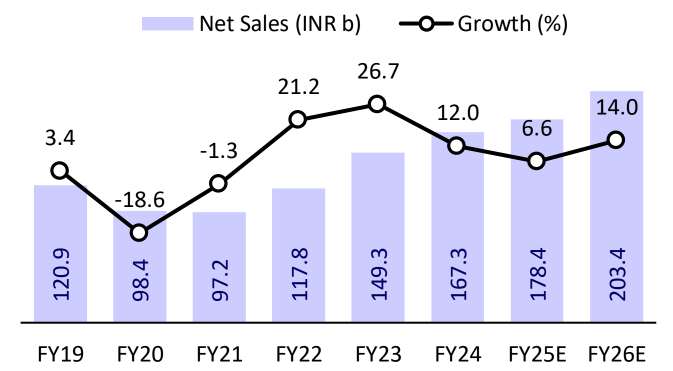
Significant investments are driving the global transformation toward a more sustainable and technologically advanced future in India. The renewable energy sector is set to receive USD70b, while USD58b is allocated to green hydrogen development. The EV transition will be supported by USD24b, and USD23b is earmarked for the semiconductor industry. These investments are crucial for achieving India's ambitious goals set for 2030 and beyond.

India's evolving auto market segments

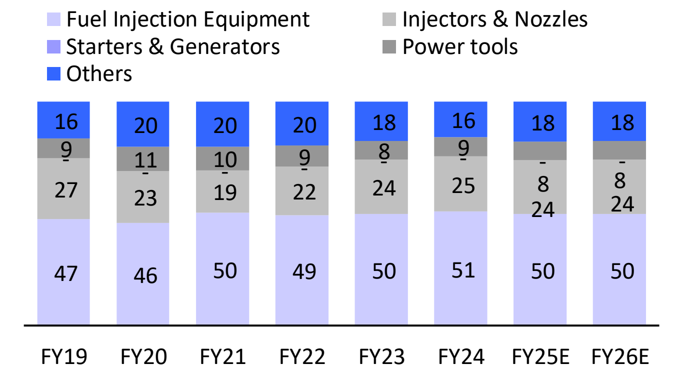
India's consumer landscape is evolving, with growing aspirations shaping the future design of vehicles. The average ticket size for cars varies across different segments, which can be broadly divided as below: 1) India 1 is the consuming class which represents 9% of the population and have USD15k per capita income. The avg cost of vehicles they buy is: i) between USD 30k-45k – 2% of PV industry, ii) USD 45k and above – 1% of PV industry; 2) India 2 is the aspirant class and consists of 21% of population with avg per capita income of USD3k. These aspirants buy vehicles divided into 3 sub-segments: i) priced between USD9k-15k – 42% of volumes, ii) priced between USD20-30k – 25% of PV industry, and iii) priced up to USD9k – 30% of volumes. It is this category that is driving most of the premiumisation trends in India with significant personalization, particularly in areas of safety and comfort.

Story in charts

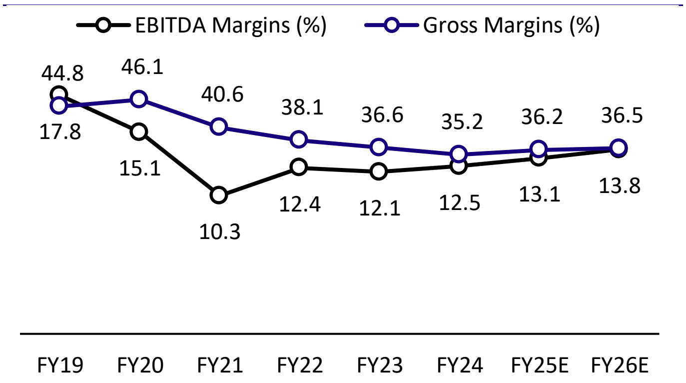
Trend in sales



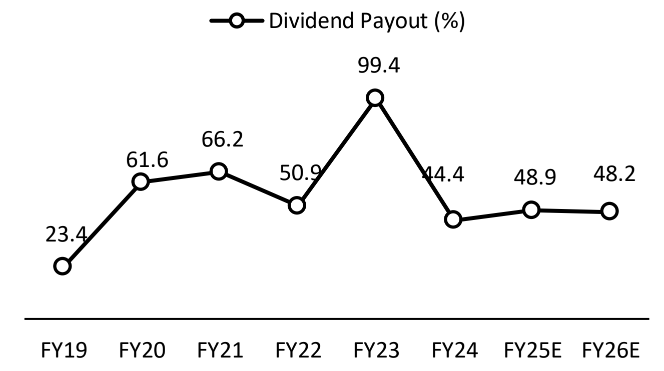
Segment mix



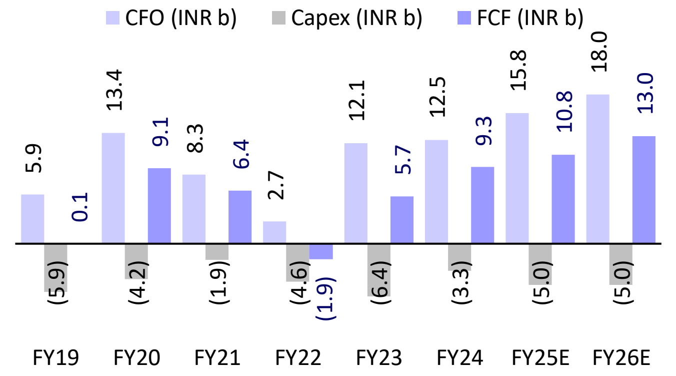
Gross margin vs. EBITDA margin



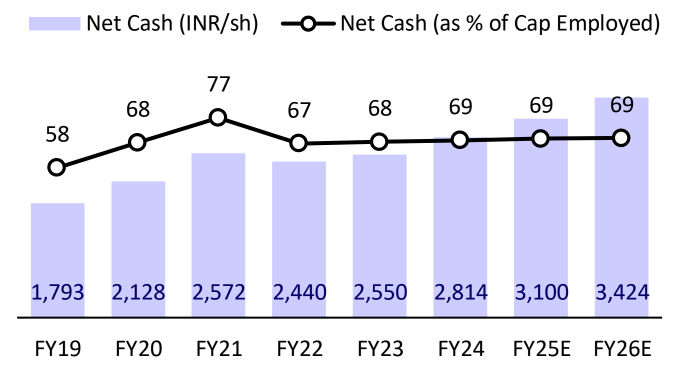
Trend in dividend payout



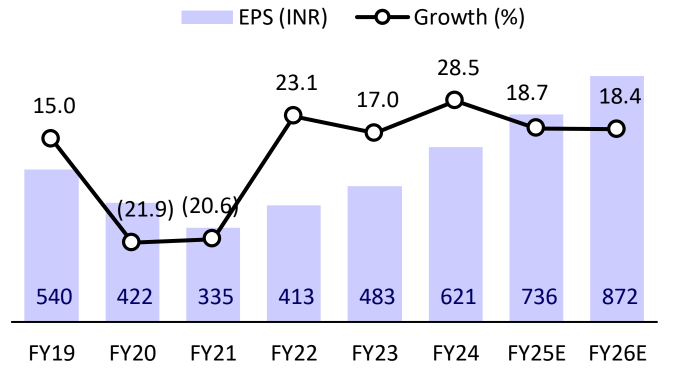
FCF and net cash



Cash, as % of capital employed, stands at ~69%

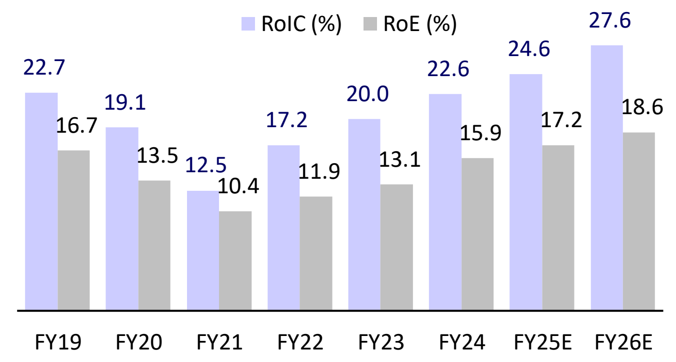


EPS and EPS growth trends



Source: Company, MOFSL

Trend in return profile



Source: Company, MOFSL

BSE

Mr. Sundararaman Ramamurthy
MD & CEO

Financials & Valuations (INR b)

Y/E Mar	FY24	FY25E	FY26E
Net Sales	13.9	27.3	31.8
EBITDA	4.0	13.0	15.0
PAT	7.7	11.6	13.2
Adj PAT	3.7	11.6	13.2
EPS (INR)	27.0	85.6	97.3
EPS Gr (%)	77.6	217.4	13.7
BV / Sh (INR)	244	270	299
Ratios (%)			
RoE	23.4	31.7	32.6
Payout ratio	26.3	70.0	70.0
Valuations			
P/E (x)	99.2	31.3	27.5
P / BV (x)	11.0	9.9	9.0

Creating a vibrant exchange

Huge growth opportunities lies ahead

We hosted Mr. Sundararaman Ramamurthy, MD & CEO of BSE Ltd, as a part of CEO Track at AGIC 2024. Here are our key insights from the session:

India has seen a massive transformation in the environment for exchanges

In 2002 Indian exchanges were processing 1.1m trades per day, which has surged to 60m orders per day in 2024. Execution time for orders has reduced from 1.08 seconds to micro/nano seconds today. This growth has been possible on the back of investments in technology and a solid regulatory environment, which has constantly evolved.

Multi-fold growth possible in India by 2047

It is envisaged that by 2047, India will be a developed economy and its GDP will grow 8x to USD40t. Considering the market cap-to-GDP ratio of more 1.2-1.5x in developed economies currently, India's market cap can surge more than 8x. With such growth, the number of listed corporates (currently at 5,000+) will grow exponentially and so will the unique investor base, which stands at 100m currently. Demographic dividend will further accentuate this growth. Unique MF investor base (45m) and the distributor (0.2m vs 2.7m for Life Insurers) count are also likely to surge during this period. Product innovation will play a meaningful role in this growth and India has to move from being price takers to price setters in products such as gold and crude oil.

Growth is likely to come with challenges

Technological development to meet the scaling up of volumes and customer need for faster implementation of trades will be key. Cybersecurity is a critical area where consistent investments would be needed. Concentration in equities and commodities within exchanges has to ease over the longer term. Resultantly, exchanges and brokers will have to develop their infrastructure.

Cyclicality of revenues for BSE not an issue

With a high share of transaction revenues, cyclicality is presumably high for exchanges, including BSE. However, if the exchanges are able to diversify their product mix between various asset classes, the cyclicality of transaction revenues will reduce. Furthermore, listing fees, treasury income, data services and index business will lend stability to revenues.

Changes in regulation can aid improvement in cash market share

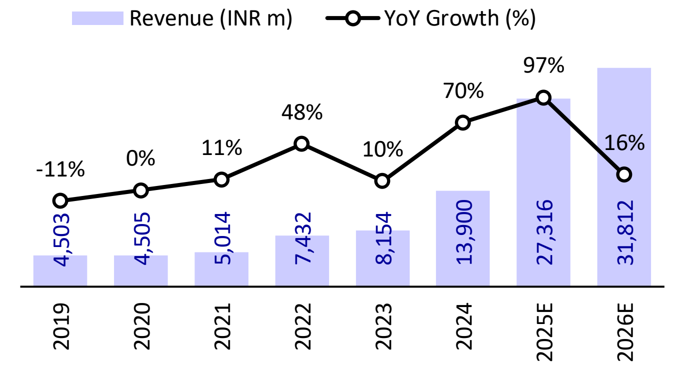
BSE has seen a sharp improvement in the market share in the derivatives segment as it was able to address a product gap in the segment. In the cash segment no such white spaces are prevalent. For institutional trades in the segment, investors needed one contract note for trades on multiple exchanges. With the same being implemented from Oct'24, BSE expects a significant increase in volumes from the institutions in the cash segment.

MF segment will continue to thrive

Star MF platform has seen phenomenal growth in the past couple of years and has maintained its leadership position. In Jul'24 the platform had 52.5m trades, of which 32.5m trades were done via SIPs. This momentum is likely to sustain over the medium term. To further strengthen its position, BSE has invested INR210m to develop Star MF 2.0, which will be launched soon.

Story in charts

Exhibit 1: Strong revenue growth to sustain



Source: MOFSL, Company

Exhibit 2: BSE gaining market share in F&O notional turnover

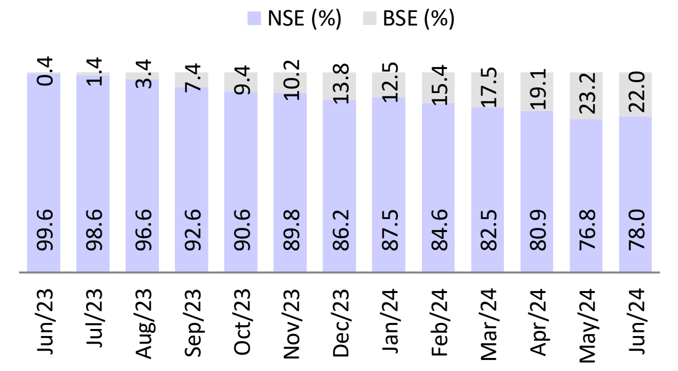
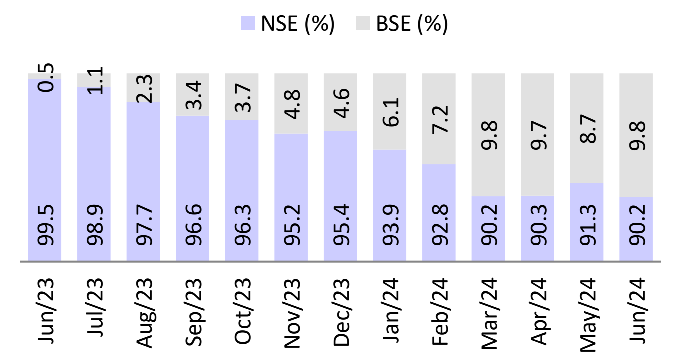
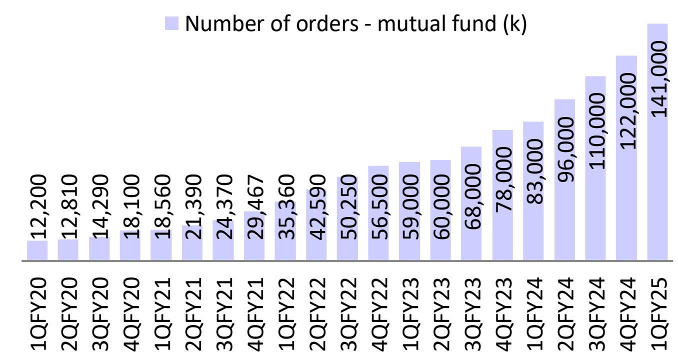


Exhibit 3: BSE's premium turnover market share improving



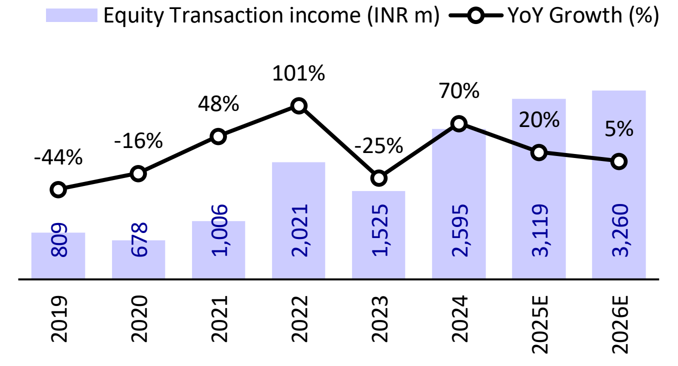
Source: MOFSL, Company

Exhibit 4: MF volumes continue to surge



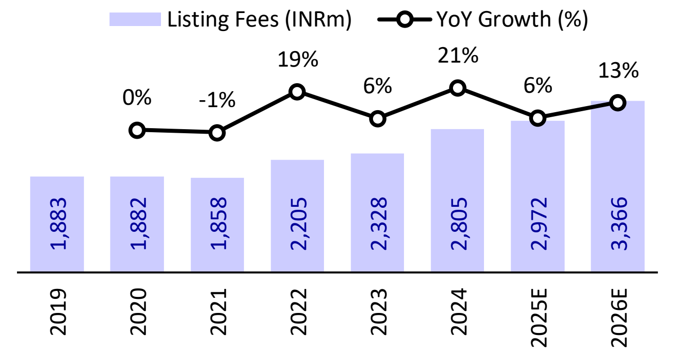
Source: MOFSL, Company

Exhibit 5: Trend in equity transaction income



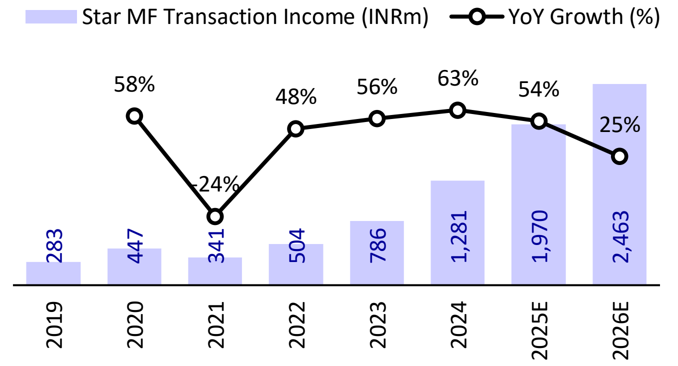
Source: MOFSL, Company

Exhibit 6: Trend in listing fees



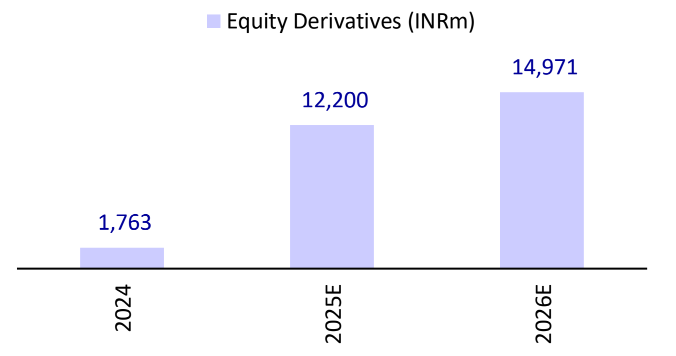
Source: MOFSL, Company

Exhibit 7: Trend in Star MF revenues



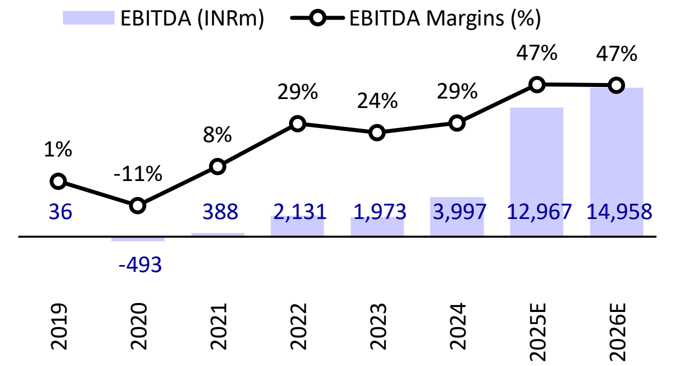
Source: MOFSL, Company

Exhibit 8: Trend in equity derivatives revenues



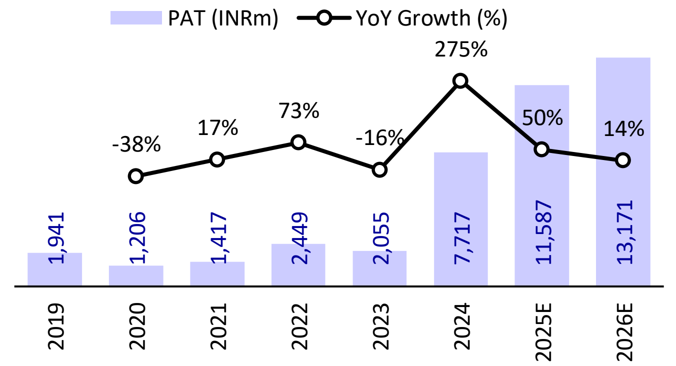
Source: MOFSL, Company

Exhibit 9: Improving profitability



Source: MOFSL, Company

Exhibit 10: PAT growth for BSE



Source: MOFSL, Company

Consumer

Valuation Summary

Company	Reco	CMP (INR)	TP (INR)
Consumer			
Hind. Unilever	Buy	2,744	3,250
ITC	Buy	501	575
Asian Paints	Neutral	3,076	3,150
Nestle India	Neutral	2,504	2,500
Pidilite Inds.	Neutral	3,055	2,950
Dabur India	Buy	621	750
Britannia Inds.	Neutral	5,732	5,850
Godrej Consumer	Buy	1,404	1,700
Marico	Buy	669	750
United Spirits	Neutral	1,404	1,400
Page Industries	Neutral	41,162	38,000
P & G Hygiene	Neutral	16,969	17,000
Colgate-Palm.	Neutral	3,549	3,150
United Breweries	Sell	1,990	1,800
Emami	Buy	803	950
Indigo Paints	Buy	1,448	1,700
Jyothy Labs	Neutral	556	565
Retail			
Titan Company	Buy	3,464	4,000
Kalyan Jewellers	Buy	549	650
Senco Gold	Buy	1,123	1,350
Jubilant Food.	Neutral	634	550
Devyani intl.	Buy	170	210
Westlife Foodworld	Neutral	807	775
Sapphire Foods	Buy	1,560	1,850
Restaurant Brands	Buy	106	140
Barbeque Nation	Neutral	633	625

Consumption tracker: Steady demand trend; pricing to further support growth

Our vibrant consumer universe, with a revenue pool of INR4,000b and a market cap pool of INR32,000b, recorded an aggregate revenue growth of +6%/+9% in 1QFY25/FY24. The coverage includes six sub-buckets, all of which posted growth in 1QFY25/FY24 (i.e., staples +5%/+6%, paints -1%/+4%, liquor +9%/5%, Innerwear +4%/-3%, QSR +6%/+12%%, and jewelry +15%/+28% YoY). Most sub-categories maintained a similar trend in 1QFY25. The staples universe continued to experience steady volume improvement, while margin delivery was better than expected. Paints witnessed a slowdown in growth due to industry factors, with weak margins. Liquor companies sustained healthy growth in the premium segment, with improved operating margin in 1QFY25. QSR faced growth challenges, particularly in the dine-in format and reported sluggish margins. Jewelry recorded a moderation in growth due to heat waves, gold inflation, et al., but its margin performance was surprising. Though management commentary for 2HFY25 remains optimistic, backed by pricing, it appears more achievable for staple companies at present. The following summarizes the performance of all sub-categories and key areas to monitor:

- **Staples:** The consumer staples companies struggled to maintain volume growth momentum during the last two years, largely due to external challenges such as erratic monsoons and high inflation, which severely dampened consumption in the mass segment. A modest upswing in volume growth is now visible after two years of subdued demand. In 1QFY25, harsh summer conditions and election-related restrictions have affected out-of-home consumption and categories such as HI, beverages, alcoholic beverages, and paints, while boosting demand for cooling products. We expect that the volume improvement trajectory will continue in the upcoming quarter of FY25, aided by stable retail inflation, a healthy progress of the monsoon season, and the government's budgetary allocation towards boosting the rural economy.
- **Paints:** The industry has been experiencing a moderation in growth during the last 3-4 quarters, marred by price cuts. Additionally, there has been a consistent entry of new players such as Grasim Industries, Pidilite, and JSW Group, altering the competitive landscape. These companies are investing heavily in capex (INR200-220b over the next 3-4 years) to enhance capacity by 20%. Though the new entrants are helping the category shift from unbranded to branded, they are also intensifying the competitive pressure. Weak discretionary demand and the changing competitive landscape are adversely affecting growth. In 1QFY25, demand was hit by price cuts (~3.5% in 4QFY24), an unfavorable product mix, general elections, and heat waves. To combat rising raw material prices, the paint companies have taken a 1-2% price hike in Jul'24 and may further increase prices in the upcoming quarters.
- **Innerwear:** PAGE continues to experience weakness in growth amid subdued demand in the apparel industry, resulting in excess inventory at channel partners. Management is implementing several initiatives to optimize channel

inventory, leading to a 10-day reduction in inventory days at channel partners in 1QFY25. Margins of innerwear companies were affected by increased discounts and volatile raw material prices. We are still awaiting more clarity on the near-term demand recovery and full inventory normalization at trade partners.

- **Liquor:** The P&A segment has consistently outperformed over the past three years, with pricing in key states playing a crucial role in driving revenue growth over the last 12 months. ENA continues to face inflationary pressures, while other key commodities like glass have remained stable, contributing to margin volatility for UNSP. Although barley costs, which affected margins, are now declining sharply, UBBL's margins remain hurt by the increased use of new bottles in its product mix. In 1QFY25, demand faced challenges despite the seasonality, primarily due to election-related restrictions and a lack of approvals for interstate transfers, while premium products performed well. Moving forward, a strategic focus on overcoming regulatory hurdles and capitalizing on the premiumization trends could further bolster growth.
- **QSR:** The quick-service restaurant (QSR) industry continues to face demand challenges, grappling with weak unit economics and intense market competition. There has been improvement in the delivery channel, as consumer traffic was positive, driven by consumer offers and the impact of heat waves. Dine-in demand remained weak, with most brands experiencing a double-digit decline. Both restaurant margin and EBITDA margin contracted for most of the brands over the last four to five quarters. We expect QSR companies to sustain a weak growth trajectory in the near term, although ADS appears to have bottomed out. The pace of recovery is expected to be slow, which will likely keep operating margins under pressure. Following a sharp dip in margins, any further contraction will be closely monitored. We are watchful for any signs of recovery (particularly for dine-in) in 2HFY25 and the pace of store additions in FY25.
- **Jewelry:** Despite the consumption slowdown across various categories, jewelry companies have delivered healthy growth fueled by an increase in footfalls, store additions, and healthy same-store sales growth (SSSG). However, in the first quarter, revenue growth was hit by a rise in gold prices (15% YoY), extreme heat waves, general elections, and fewer wedding days. We, however, remain optimistic about the jewelry sector and anticipate a continued rapid transition in consumer buying habits from informal/local to formalized channels. Factors such as rising ticket prices, improved shopping experiences, a wider product range, and others are driving this significant trend. The recent reduction in custom duties will further accelerate the shift from unorganized to organized retail channels.

Valuation and View: Maintain preference for staples over discretionary

In our last consumer sector thematic report published in Apr'24, we emphasized our overweight stance on staple companies owing to favorable risk-reward dynamics and anticipated volume recovery in FY25 and FY26. We noted that the earnings cut cycle had been largely reflected in stock prices, leading to 15-20% corrections in valuation multiples of staple companies compared to their own five-year averages. Consequently, an improvement in volume print is expected to reduce these valuation differentials. Over the past two quarters, we have observed steady improvement in volume growth, along with optimistic management commentary regarding further acceleration in growth in the upcoming quarters. Our preference for staple companies remains strong, as we anticipate a sustained upward trajectory in earnings that largely justifies their premium valuations.

We maintain our cautious stance on discretionary stocks; however, we hold a positive view on jewelry companies. Various external and internal factors are contributing to robust earnings growth in the jewelry sector. We are monitoring QSRs, liquor, paint, and innerwear companies for indications of improved growth.
Top picks: We reiterate our overweight stance on the staple sector and continue to prefer HUL, GCPL, and Dabur as our top picks. In the discretionary space, we like jewelry companies, with Kalyan Jewelers and Titan being our top picks.

Are household finances in India a sign of distress or optimism?

Recent trends are certainly not favorable

- A few months ago, we published a detailed note discussing the financial position of India's household (HH) sector. Our analysis threw up four key conclusions:
  - Personal disposable income (PDI) has grown at a slower pace than the nation's gross domestic product (GDP) in the last few years.
  - For the first time in the post-independence period, private final consumption expenditure (PFCE) grew at a faster pace than PDI in the 2010s decade, which has continued in the 2020s[1] as well.
  - Household total savings stood at a six-year low in FY23, with net financial savings (NFS) at a four-decade low. It is expected to have picked up in FY24E but still remains at a low level.
  - Household debt has increased sharply in the past many quarters, majorly led by non-housing (or consumption-led) personal loans.

- With these facts, there has been an unsettled debate on whether a combination of weak income growth, lower household savings, faltering consumption growth and rising borrowings represents a distress situation or optimism (high confidence) among consumers. In the light of limited official data available on household finances and even slimmer details, it is not surprising that there are a variety of views and arguments regarding the same. In this note, we share our views and contribute to this debate. We also thought it best to address likely counter-arguments to our views. Overall, we believe that the recent trends in household finances are certainly not favorable and the longer they persist, the more worrisome they will be.
- A look at data reveals that the share of PFCE increased almost every year from its all-time low of 68.5% of PDI[2] in FY12 to a 27-year high of 77.0% of PDI in FY23 *(Exhibit 1)*, which has likely fallen marginally in FY24E. This is so because for the first time in any decade since independence, PFCE growth outpaced that of the PDI growth in the 2010s decade, which continued in the first four years of 2020s decade as well *(Exhibit 2)*.
- Further, household total savings stood at 23.3% of PDI (18.4% of GDP) in FY23, very close to the two-decade lowest level of 23% of PDI (18.0% of GDP) in FY16 *(Exhibit 3)*. Within savings, net financial savings (NFS) were at a four-decade low of 6.6% of PDI (5.3% of GDP) in FY23 (compared to ~10% of PDI in the pre-Covid years) and physical savings stood at a decade high of 16.6% of PDI *(Exhibit 4)*.
- At the same time, HH debt rose from 38% of PDI a decade ago to 48% of GDP in FY23 *(Exhibit 5)*. Within HH debt, non-housing borrowings grew faster than housing loans *(Exhibit 6)* in the past few years. The sharp surge in HH debt is reflected in a rise in annual borrowings (i.e., financial liabilities), which were 7.3% of PDI in FY23, the second highest since the 1970s (the peak was 8.5% of PDI in FY07).
- Although the official data on PDI, household savings and debt is not yet available for FY24, it is likely that PDI growth lagged GDP growth once again in FY24, as corporate profits and government receipts grew strongly. If so, since (nominal) PFCE growth was modest at 8.5% YoY in FY24, it suggests pick-up in household total savings to 24% of PDI, led by NFS (estimated at 7.2% of PDI). Household debt is estimated to have risen to 52% of PDI (40% of GDP) in FY24E.
- With these facts/estimates, we propose a theory to answer the question. The basic tenet of our views is based on a recent development. In the post-pandemic period, the income distribution in India (like many other economies) has very likely become more unequal, with the rich (including the high- and upper-middle income) population witnessing higher income growth since they majorly constitute the regular wage/salaried workers and also own a substantial portion of asset classes such as equity[3] and real estate. This recent development/trend plays an extremely important role in highlighting the potential worrying signs in household finances.

Let us say there is a consumer pyramid arranged by income, so that the richest people are at the top and the lowest-income earners make the bottom of the pyramid. One could argue about the steepness and slope of the pyramid and the share of the high-income or poverty-stricken segments, but they are distractions for our discussion here. Now, let's consider the four facts and combine them with our view of rising income inequality *(Exhibit 7)*.

<u>Fact#1:</u> Nominal PDI in India has grown at an average of 9.4% in the past five years (FY20-FY24E), compared to an average growth of 10.7% during FY15-FY19 period (and 12% during the 2010s decade).
Our belief of higher income inequality in the recent past comes from our analysis that suggests that income growth for the top of the consumer pyramid has been much higher. Since average growth in PDI has moderated over a period of time, it suggests that the rest of the consumer pyramid (including middle- and low-middle income and low-income sections) must have witnessed a slower-than-national growth in their income in the post-pandemic years.

<u>Fact#2:</u> Nominal/real PFCE in India has grown at an average of 9.9%/4.5% in the past five years (FY20-FY24E), compared to an average growth of 11.6%/7.2% during FY15-FY19 period (and 13.7%/7.4% during the 2010s decade).
It is safe to assume that the consumption growth or pattern of the rich consumers would not have undergone a substantial change in the past few years. If anything, their consumption would have grown at a slightly faster pace than earlier. If so, then the slowdown in consumption growth in the post-pandemic period (which has been more prominent in the past 6-7 quarters) in nominal/real PFCE must have come from the lower middle-to-lowest income consumer class, whose income growth, as we discussed above, has also likely slowed down.

<u>Fact#3:</u> Household total savings stood at a six-year low of 23.3% of PDI (18.4% of GDP) in FY23, which was close to the 20-year low of 23.0% of PDI (18.0% in FY16). It is expected to have picked up to 24% of PDI (19.0%) in FY24E.
It is well established that the saving propensity of the rich people is more than that of the middle- or low-income consumers. With higher income growth, it is then conceivable that total savings of the rich consumers – be it in financial and/or physical assets – would have increased in the post-pandemic years. However, since aggregate savings of the household sector were close to a 25-yeal low, it means that savings of the middle- to low-income consumers have fallen to such low levels that it entirely offset rising savings of the rich consumers (top of the pyramid).

<u>Fact#4:</u> Household debt stood at 48% of PDI (38% of GDP) in FY23, up from 38% (30%) a decade ago. It is likely to have risen further to 52% of PDI (41%) in FY24E. Details suggest that consumption-led (non-housing) consumer borrowings have risen at the fastest pace.
Household debt has risen in the past few years, with much sharper growth in the last 8-10 quarters. Our estimates suggest that it has risen to ~52% of PDI (415 of GDP) in FY24E, compared to 38% (30%) a decade ago. Details suggest that non-housing personal loans, i.e., consumption-led borrowings, have grown at a faster pace (~20%) than housing loans (~15%). Consequently, the share of non-housing personal loans has increased the most in the past few years. Once again, it is widely acknowledged that the bulk of consumption-led loans are owed to the lower middle- to low-income consumer classes, since the high-income individuals (including upper middle-income) do not borrow for consumption purposes.

Now, let's combine these arguments. Income growth of the middle- to low-income consumer class has been lower than national growth; their consumption weakness is likely to have been the primary cause of faltering national PFCE growth in the past few quarters; the fall in their savings have presumably offset higher savings of the rich-to-upper middle income class pulling down household total savings for the country; and their consumption-led borrowings have surged massively in recent years. Lower income growth, slower consumption growth, falling savings and rising consumption-led debt – these facts do not auger well for any section of society, let alone a very large and widespread middle- to low-income consumer section. This is where the feeling of uneasiness starts creeping into India's growth story and this is where the potential for destabilization lies.

Why is it important?
In his recent monetary policy statement, RBI Governor Mr. Shaktikanta Das answered this question for us. He said, *"…Even in such stable financial sector conditions, the emphasis cannot shift away from proactive identification of potential risks and challenges, if any…"* We have always been very careful to highlight that the recent trends in household finances in India may not imply immediate concerns. However, they certainly hold the potential for destabilizing the nation's financial stability, if they

continue for long. The combination of weak income growth and lower household savings has continued for about a decade now, while weak consumption growth and a sharp surge in household debt have occurred in the past 8-10 quarters. It is very likely that these trends will continue in the current year as well. Despite such facts, some participants argue that with non-performing loans (NPAs) at such low levels, there is nothing to worry about. Nevertheless, we are of the firm view that the longer these unfavorable trends in household finances continue, the closer we will be to the potential instability and more worrisome we will become. Unfortunately, it is very difficult to ascertain the timing of such events.

What could be the possible counter arguments to our cautious view?

- **What if new-to-credit (NTC) borrowers lead higher loan growth?** If so, this could lead to a higher debt service ratio but need not be concerning. In fact, RBI data confirms that strong growth in recent years is largely driven by the number of loan accounts rather than the amount of loans per account *(Exhibit 8)*. However, one must not confuse the number of accounts with the number of borrowers, as many borrowers would have multiple loans (and thus, loan accounts).

- Instead, we would like to highlight some insights about consumer credit from the RBI data that it shared in its bi-annual Financial Stability Report (FSR). In its **Jun'24 FSR** (Page 50, para 1.101), the RBI stated *"…little more than a half of the borrowers in this segment have three live loans at the time of origination and more than one-third of the borrowers have availed more than three loans in the last six months…"*. These ratios have increased in the past six months, as the corresponding numbers were 42.7% and 30.4% as per the **Dec'23 FSR** (page 59, para 1.137).

- **What if higher loan growth is led by middle of the pyramid, who would be more credit worthy than the population at the bottom?** While this counter-argument would give some comfort, it would also suggest that the income growth at this section is not enough to meet their consumption growth, leading to higher growth in consumption-led borrowings. If so, it would not be very strange to assume that income growth at the bottom of the pyramid would be even weaker, supporting their prominent role in driving weak consumption growth and lower savings.

- **What if income inequality has not risen and our assumption, to start with, is wrong?** This, to our mind, is the least likely counter-argument. It seems really far-fetched, especially considering the consumption patterns of high-ticket items such as cars or housing, wherein the premium segment has witnessed higher sales than the affordable segment. But since there is no official data on the same, one cannot be sure about any one scenario. Further, one could argue that aggressive redistribution policies of the government could have led to better income growth at the bottom of the pyramid and not-so-good income growth at the top. If so, then since rich people do not adjust their consumption habits easily, slower income growth would have led to lower savings by this class, driving lower household savings in the economy. Even then, this scenario fails to explain the rising growth in consumption-led loans and the weakening in overall consumption growth in recent quarters. These two trends must be driven by activities of the consumers closer to the broad base of the pyramid. Even if one assumes that higher borrowings are concentrated in the middle of the consumer pyramid (as explained in the counter-argument #2 above), it would suggest that the weakness in consumption growth at the bottom of the pyramid is very severe.

Overall, recent trends in household finances are certainly unfavorable and the longer they continue, the more dangerous they would be for the financial stability of the country. To our mind, they hold the potential to break the current calmness, and thus, extreme caution must be exercised on this front by the policy makers.

[1] 2020s in this note refers to the first four years of the decade – FY21-FY24E. Official data on PDI, household savings and household debt is not yet available for FY24, and thus, we have used our estimates of all these variables.

[2] Normally, all ratios are derived using GDP as the denominator. However, when we speak of household finances, it is always better to analyze the ratios with PDI as the denominator, wherever possible.

[3] In the US, official data confirm that 87% of corporate equities and mutual fund shares are held by top 10% of wealthiest people in the country or the 20% highest income-earners. In a recent post-Budget interview, India's Finance Secretary, Dr. T V Somanathan, stated that *"…88% of the value of capital gains earned in India, according to our study, comes from people whose returned income is more than 15 lakh rupees and 62% comes from those who are above 1 crore of returned income..."*.

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