FIRST LIGHT

28 January 2025

RESEARCH

CONSUMER STAPLES

Is it FY22 again? Impact of inflation on FY25 and FY26 earnings

CANARA BANK | TARGET: Rs 115 | +25% | BUY

Continued weak earnings, asset quality improves

JK CEMENT | TARGET: Rs 4,511 | -6% | HOLD

Healthy show in challenging times; valuations priced in

SUMMARY

CONSUMER STAPLES

- We expect input cost headwind on gross margins to be higher in the March 2025 quarter compared to the December 2024 quarter
- Palm oil, cocoa, coffee, wheat and tea are in high inflation and impacting gross margins of companies with respective exposure
- We downgrade Britannia (Hold from Buy) and Godrej Consumer (Sell from Hold) and retain ratings on Nestle (Hold) and Tata Consumer (Buy)

Click here **for the full report.**

CANARA BANK

- Weak operating performance, NIMs contracted sequentially. CBK guided for advances growth of 10% in FY25E
- Asset quality improved with stable slippage ratio, targets credit cost of below 110bps in FY25E
- We assume coverage on CBK with a BUY rating and TP of Rs 115, assigning 1x Dec'26 ABV

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JK CEMENT

- Grey cement volumes at 4.3mt (excluding clinker volumes) rose by ~4%/13% YoY/QoQ as demand revives in key operating regions
- Strong EBITDA reversal by ~80% QoQ to ~Rs 4.9bn (-20% YoY), EBITDA margin too reversed QoQ to 18% (-380bps YoY) on cost savings
- We trim FY25E EBITDA by 4% and tweak FY26E/FY27E, value JKCE at 14x 1Y forward EV/EBITDA and lower TP to Rs 4,511. Maintain HOLD

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27 January 2025

Is it FY22 again? Impact of inflation on FY25 and FY26 earnings

- **We expect input cost headwind on gross margins to be higher in the March 2025 quarter compared to the December 2024 quarter**
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Commodity headwinds to accelerate in 4QFY25: Advance purchase agreements and FX hedges have limited the full impact of commodity inflation in the December 2024 quarter. If current commodity prices sustain, we expect commodity pressure for the FMCG sector to accelerate in 4QFY25. Commodity headwinds are the highest for companies with large palm oil exposure and a relatively elastic portfolio. We estimate spot palm oil inflation with spot currency at 59% in 2HFY25. The weakness in INR is adding to the already high inflation. Market position is key to cost recovery and companies with leading positions are relatively okay, but still need to raise prices amidst a slowdown in urban consumer demand.

Which companies are most affected?: Nestle is most impacted due to high inflation in cocoa, coffee and palm oil. Britannia is also materially impacted from palm oil and wheat inflation. Commodity headwind for both companies between 3QFY25 and FY26 is in the range of ~700bps to 1,100bps.

What is the earnings outlook for 2HFY25 and FY26?: All analysed companies are increasing prices, reducing grammage and improving cost efficiencies to offset inflation. We expect it to be a cost to cost offset instead of a flat margin percentage restoration outcome. Some pullback in A&P is likely in inflationary products such as Tea, confectionary, soaps etc. Overall, we expect meaningful profit pressure for FMCG companies over the next 3-6 months. Compared with consensus, at an aggregate level for the analysed companies, our EBITDA forecast is 7% lower for FY25, 19% lower for FY26 and 7% lower for FY27.

Valuation: We move our valuation methodology from PE Rel to Absolute PE. We use 5Yr avg P/E on 12m to Dec-26 EPS across our coverage. Our new target prices are BRIT Rs5,131, GCPL Rs977, NEST Rs2,299 and TATACONS at Rs1,155.

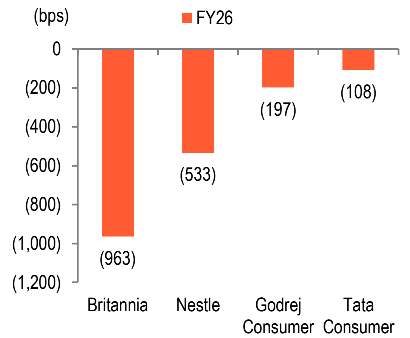
Our view: While the FMCG commodity headwind is transitory, we expect stock prices to be volatile with a downward bias over the next 3-6 months. We have a cautious sector view but closely monitor the rural and urban demand trajectory. Any recovery will favourably impact volume elasticity and FMCG pricing power.

Recommendation snapshot

Ticker	Price	Target	Rating
BRIT IN	5,176	5,131	HOLD
GCPL IN	1,127	977	SELL
NEST IN	2,175	2,299	HOLD
TATACONS IN	966	1,155	BUY

Price & Target in Rupees | Price as of 27 Jan 2025

Commodity headwind on FY26 margins (bps)



Sources: Company, Bloomberg, BOBCAPS Research

BUY
TP: Rs 115 | ⮝ 25%

CANARA BANK | Banking | 28 January 2025

Continued weak earnings, asset quality improves

- **Weak operating performance, NIMs contracted sequentially. CBK guided for advances growth of 10% in FY25E**
- **Asset quality improved with stable slippage ratio, targets credit cost of below 110bps in FY25E**
- **We assume coverage on CBK with a BUY rating and TP of Rs 115, assigning 1x Dec'26 ABV**

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Weak operating performance: CBK witnessed moderation in operating performance due to lower yield on loans and higher cost of funds, resulting in lower NII growth (down 3% YoY and 2% QoQ). However, advances growth was healthy at 11% YoY (4% QoQ). NII came in at Rs 91.5bn, down 3% YoY, 2% QoQ, vs. our estimate of Rs 98.6bn. NIMs contracted by 15bps QoQ to 2.7%. Yield on advances declined by 7bps QoQ while cost of funds increased by 10bps QoQ. Management foresees gross loan advances growth of 10% in Mar'25.

PPoP was bolstered by other income growth: PPoP was healthy supported by strong other income growth which grew 15% YoY and 2% QoQ. Further, operating expenses was moderate and was up 3% YoY (7% QoQ) which aided PPoP growth in Q3FY25. PAT came in at Rs 41bn, up 12% YoY and 2% QoQ vs. our estimate of Rs 42.1bn.

Advances saw healthy growth while deposits were moderate: Advances was healthy with growth of 11% YoY (4% QoQ). On a gross book basis retail, agri and MSME (RAM) grew 12% YoY (3% QoQ) and corporate book 8% YoY (4% QoQ). Retail book rose 36% YoY (7% QoQ) led by housing loan (up 12% YoY) and vehicle loan (up 17% YoY). Deposits moderated in Q3 and rose 8% YoY (up 2% QoQ). CASA deposits saw lower growth of 2% YoY, while term deposits saw higher growth of 11% YoY which aided overall deposits growth.

Performance mostly in line with the guidance for FY25: Management had guided for 13 parameters in FY24 for FY25. Most of these parameters have been achieved by the bank.

Assume coverage with a BUY on CBK: Considering the management guidance and its performance against it with stable assets quality, we believe the bank has levers to perform well going forward. We model a PAT CAGR of 11% over FY24-27E with ROA of 1.03-1.04% over FY24-27E. We value the bank at 1x Dec'26 ABV and assume coverage with a BUY rating and TP of Rs 115 (from Rs 140).

Key changes

Target	Rating
▼	◀ ▶

Ticker/Price	CBK IN/Rs 92
Market cap	US$ 9.7bn
Free float	42%
3M ADV	US$ 27.2mn
52wk high/low	Rs 129/Rs 89
Promoter/FPI/DII	63%/11%/11%

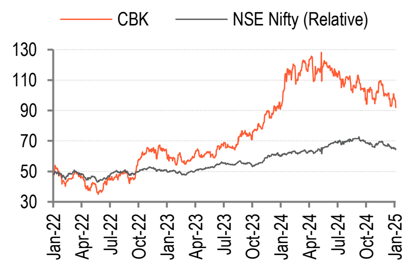
Source: NSE | Price as of 27 Jan 2025

Key financials

Y/E 31 Mar	FY24A	FY25E	FY26E
NII (Rs mn)	3,65,659	3,76,010	4,29,938
NII growth (%)	16.3	2.8	14.3
Adj. net profit (Rs mn)	1,45,543	1,63,285	1,80,547
EPS (Rs)	16.0	18.0	19.9
Consensus EPS (Rs)	16.0	18.0	19.6
P/E (x)	5.7	5.1	4.6
P/BV (x)	1.0	0.8	0.7
ROA (%)	1.0	1.0	1.0
ROE (%)	18.1	17.2	16.5

Source: Company, Bloomberg, BOBCAPS Research

Stock performance



Source: NSE

HOLD
TP: Rs 4,511 | ⩔ 6%

JK CEMENT | Cement | 27 January 2025

Healthy show in challenging times; valuations priced in

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- **Strong EBITDA reversal by ~80% QoQ to ~Rs 4.9bn (-20% YoY), EBITDA margin too reversed QoQ to 18% (-380bps YoY) on cost savings**
- **We trim FY25E EBITDA by 4% and tweak FY26E/FY27E, value JKCE at 14x 1Y forward EV/EBITDA and lower TP to Rs 4,511. Maintain HOLD**

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Healthy grey cement volume gains aid performance: JKCE reported a 5% YoY fall (+14% QoQ) in revenue to ~Rs 25.4bn in Q3FY25 largely aided by healthy grey cement volume though realisations stayed weak on fragile prices. Grey cement volumes at 4.3mt (excluding clinker volumes) improved by ~4%/13% YoY/QoQ owing to demand reversal in JKCE's key region of operations. Grey cement realisation fell by ~8% YoY to Rs 4,757/t (+1% QoQ) indicating weak demand.

Healthy cost savings push up margins: The overall cost fell 1%/6% YoY/QoQ to Rs 4,726/t, owing to lower energy cost and flat logistics cost. Logistics cost was flat YoY at Rs 1,299/t despite higher transportation to farther markets. Energy cost fell by 8%/4% YoY/QoQ to Rs 1,819/t due to reduction in fuel prices to Rs 1.5/kcal from Rs 1.82/kcal. The blended proportion was ~67% in Q3FY25. Other expenditure was high at 9% YoY to Rs 4.5bn in expenses spent on value-add products and branding.

EBITDA/margins reverse strongly QoQ, YoY still falls short: EBITDA fell 20% YoY but recovered sharply QoQ (+80%) to ~Rs 4.9bn, and EBITDA margin recovered sharply to 18% from 11% in Q2FY25 (fell by 380 bps YoY) due to cost reduction and steady realisations despite volume gains QoQ. The aggregate EBITDA/t recovered sharply by 60% QoQ to Rs 1,040/t (down 22% YoY).

Expansion plans on track: JKCE's board approved the acquisition of Saifco Cements (Saifco) situated in Jammu and Kashmir. Saifco has a clinker capacity of 0.26mt and grinding capacity of 0.42mt. JKCE's previously-announced 3.3mt grey clinker line-II at Panna and 3mt grinding unit in Bihar and 1mt each in Hamirpur, Prayagraj and Panna (3mt) are on track to be completed by Dec'25.

Retain valuations and HOLD rating: We trim our EBITDA estimates for FY25 EBITDA by 4% and tweak FY26/FY27 due to a weak 9MFY25 but expect a healthy recovery. EBITDA/PAT CAGR is now at 29%/25% over FY24-27E. JKCE's focus remains on long-term growth with timely capex. Improving earnings quality and reducing balance sheet stress are key. We continue to value JKCE at 14x 1Y forward EV/EBITDA to arrive at a TP of Rs 4,511 (from Rs 4,190). Maintain HOLD.

Key changes

Target	Rating
▲	◄ ►

Ticker/Price	JKCE IN/Rs 4,786
Market cap	US$ 4.3bn
Free float	54%
3M ADV	US$ 5.8mn
52wk high/low	Rs 4,916/Rs 3,642
Promoter/FPI/DII	46%/16%/22%

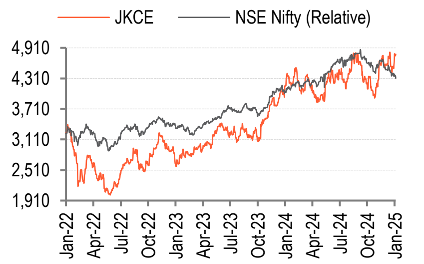
Source: NSE | Price as of 27 Jan 2025

Key financials

Y/E 31 Mar	FY24A	FY25E	FY26E
Total revenue (Rs mn)	1,05,632	1,16,412	1,37,737
EBITDA (Rs mn)	16,502	18,049	23,901
Adj. net profit (Rs mn)	8,361	7,700	11,033
Adj. EPS (Rs)	108.2	99.7	142.8
Consensus EPS (Rs)	108.2	101.4	140.5
Adj. ROAE (%)	17.2	13.8	17.2
Adj. P/E (x)	44.2	48.0	33.5
EV/EBITDA (x)	25.1	23.3	13.5
Adj. EPS growth (%)	48.6	(7.9)	43.3

Source: Company, Bloomberg, BOBCAPS Research

Stock performance



Source: NSE

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BUY – Expected return >+15%

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SELL – Expected return <-6%

Note: Recommendation structure changed with effect from 21 June 2021

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