

Demonetisation impact: GST uncertainty bigger worry for consumer durables, say experts

With the shock of demonetisation and the uncertainty of GST implementation looming large, the moot question is how these factors would impact the consumer durable sector in 2017.

To discuss the fundamentals of various sectors, CNBC-TV18 spoke to three wise men B Thiagarajan, Joint MD, Blue Star for their industry perspective, Rabindra Nath Nayak, Senior Research Analyst-Power & Capital Goods, Dolat Capital Group Company and Prakash Diwan, Altamount Capital Management from market and stock performance perspective.

Thiagarajan is not at all worried about the demonetisation impact and believes the industry has the potential to grow by 15 percent in 2017, especially on back of lower penetration.

The penetration currently is below 4 percent, he adds. According to him, the impact of demonetisation on the industry should be around 2-2.5 percent.

However, he is a bit skeptical of GST and the uncertainty regarding its implementation time – whether April or July etc and the forex rate (rupee-dollar movement).

He is also of the belief that if rural class, agri class get some incentives from government then 2017 both optimistic and challenging. Meanwhile, Nayak believes the near-term impact of demonetisation could be on the secondary sales but long-term he is still positive on the sector.

He is upbeat on Blue Star and Whirlpool on back of new product launches and strong balance sheet respectively. Market expert Diwan says the sector is in a state of flux due to headwinds like demonetisation and uncertainty of its medium to long-term impact, and question mark on GST implementation. The only silver lining to the above two dark clouds could come in form of largesse announced for rural and semi-urban segment in the Budget.

It is time to be stock specific in this sector, says Diwan, adding that for long term investors it would be the ideal time to start looking at adding to their portfolios in January.

Existing customers too need not panic. Stock specific, besides Blue Star he is bullish on IFB Industries too. Below is the verbatim transcript of B Thiagarajan, Rabindra Nath Nayak and Prakash Diwan's interview to Latha Venkatesh and Sonia Shenoy on CNBC-TV18.

Latha: How has this quarter been, how much lower if at all compared to Q3 of last year and compared to Q2? Thiagarajan: This morning I saw you talking about the market should cool down and how the temperatures are and after a very fantastic festival season, we continue to be doing well.

There was a bit of a hiccup in the month of November and it continues in December with regards to the secondary movement. However, I do not anymore worry about the demonetisation as an issue at all. It is something that happened and the market is trying to cope with much more in tier III, IV and V markets than in tier I and II.

On the whole, we should end the year -- first I am talking about the market, the total air conditioners market should still show a growth of somewhere around 15 percent at the backdrop of good summer and we would have grown anywhere between 25-30 percent.

So, that is no longer the issue at all, demonetisation. On the other hand, I will be concerned about the goods and services tax (GST). The first uncertainty is whether it is going to be April 1 or July 1.

It more appears to be July 1. We are worried about the transition rules. We are now reconciled to the fact that the rate may as well be 28 percent and all of us including you are worried about some other cess will be there or not there. In any case, the price of the air conditioners should go up anywhere between 2.5 percent or so and contrary to the view that GST will boost the GDP by 2 percent, I don't think in the short term anything is going to happen.

Some sectors will benefit, some sectors the prices may be going up, so, I think the air conditioner prices, 2.5-3 percent price increase is very likely as and when the GST happens. If it is not going to happen during the summer season which means from April 1, it is quite likely the markets behave in such a manner that buy the air conditioners before GST comes into effect.

I have seen consumers and the dealers behaving that way and therefore the summer sales can be good. We will see some kind of hiccup during implementation because of the transition rules where some goods suffered the old CENVAT and some goods suffered the state VAT and how these all will be treated, the clarity is yet to emerge.

Therefore I see July to September period to be which I think we can cope with in order to prepare for a better festival season.

Latha: What was the number you said, third quarter you grew by 15 percent compared to what in Q2 and previous Q3? Thiagarajan: I have not yet stated anything about Q3 growth.

I only indicated year end the market should grow by around 15 percent. We should be growing anywhere between 25-30 percent. Latha: Year-on-year (YoY)?

Thiagarajan: Yes, that is right. Q3 numbers are yet to be in hand but in terms of primary sales, I am not seeing any major impact that is happening at this moment. There was a problem in November end but the markets are beginning to cope with demonetisation.

I do not want to discuss what the exact number will be for Q3, all that I can tell is that it is not a very major impact I am seeing due to demonetisation. Sonia: Stocks like Blue Star and Whirlpool have done pretty well relatively this year. If you look at Blue Star's performance, it is still up almost 15 percent for the year; Whirlpool is up almost about 35 percent in 2016. Do you get a sense that this degree of outperformance could continue in the next calendar year as well and what are your thoughts on how long term investors should approach it? Nayak: We are positive on the sector per se. The demonetisation will have a near term impact on the sales particularly on the secondary sales.

However, if you see, in the quarter the demonetisation, it has come in, it is normally weakest quarter for the durables. So, we remain positive on the sector from the long term perspective. Latha: Is it a weak quarter for consumer durables per se and what are your thoughts of how 2016 would have ended? Diwan: More importantly we need to look at what do existing shareholders do and what do potentially new investors do. So, I am glad you chose this as the first sector to discuss the impact for next year because this is the sector along with automobile that is in the maximum state of flux.

Look at the headwinds, you have demonetisation and its medium to long term impact which is unknown. You have the Goods and Services Tax (GST) implementation and its impact which is still a question mark and the third thing is there is possibility of silver lining to these two dark clouds in the form of a budgetary largesse being announced for the rural or probably the semi-urban segment as well. Now what does happen to capital goods when let us there is more money in the pocket of potential buyers or consumers. That means that the lower end consumer white goods would start seeing a lot of traction.

So, it is not necessarily air conditioners but it is companies selling washing machines, microwaves, those are the ones that will start seeing an uptick post the Budget if the Budget is liberal enough for people to be left with so much money. But my sense is the run up that we have seen in some of these companies has been more because of the low liquidity profile most of these players have on the stock market and that could see a little bit of easing out. So, for long-term investors January would ideal time to start looking and adding into the portfolio. But existing investors don't need to panic is my way

of looking at this whole thing is. Especially you will have to be very stock specific now. The sector as a whole you can't paint it with one single brush.

There are different players, different business models, different margin profiles. So, what Mr Thiagarajan said they are agnostic to demonetisation and its potential impact because everybody believes that it is a short-term blip but you could have air conditioners making a comeback only post the second quarter. So, those things will have to be kept in mind as we go along.

Sonia: You did mention that for FY17 the air conditioner industry will grow by about 15 percent but can you look at little bit far out. What about calendar year 2017 or even FY18 for that matter? What kind of growth do you see for the industry and for your company? Thiagarajan: I have always maintained that room air conditioners is like playing T20 cricket. It is that 60 day window, rain happens, hailstorm happens, things get bad. On the whole the market will grow by 15 percent basically because of the penetration levels.

So, we are still below four percent or so. It is a very small market size compared to many other markets. The car owners not possessing air conditioners itself is very large. So, therefore I would still believe that the market has a potential to grow by 15 percent in calendar year 2017 and just not it was mentioned that the rural agricultural middle class if they are going to be looked after by the policy measures of the government given the fact that already 60 percent of the sale is happening in the entire 3-5 markets it will do well. I would term 2017 as an optimistic year but it is going to be very challenging as well because every morning you wake up with some sudden announcement that capital gains tax one day, GST one day and we are bit burdened with day to day reactions to many things that are happening unfolding.

But still the market should grow. Latha: Before demonetisation when we had spoken to you, you said the industry will grow 15 percent. Now will you trim a little for FY17 and will FY18 be less than or better than the pace of growth for FY17? Thiagarajan: I am again repeating this. The FY17 demonetisation effect for the whole industry should be some 2-2.5 percent, that is about all. It is the GST which will determine the way forward according to me and the Forex rate how rupee and dollar are going to move.

These two things I will watch. And China if it is going to be finding US market difficult whether they will end up slashing the prices and in which case China as a manufacturing destination may become attractive again. So, these are the factors I would worry about, no longer about demonetisation.

Latha: Which stock would you buy? Nayak: We are positive on these two stocks Whirlpool and Blue Star. Blue Star for its new product launches and Whirlpool for the strong balance sheet going ahead. We remain positive on these two stocks.

Diwan: I would add IFB to my buying list given the kind of softness that we have seen in the stock. Of course Blue Star continues to be category leader of sorts but I would avoid a lot of those stocks which we have been talking really positively like Lloyd and all and Whirlpool notwithstanding the brave phase that we have seen in terms of the 2020 sales target and all. But IFB and Blue Star probably stand out and at dips to be bought.

http://www.moneycontrol.com/news/business/demonetisation-impact-gst-uncertainty-bigger-worry-for-consumer-durables-say-experts_8162361.html