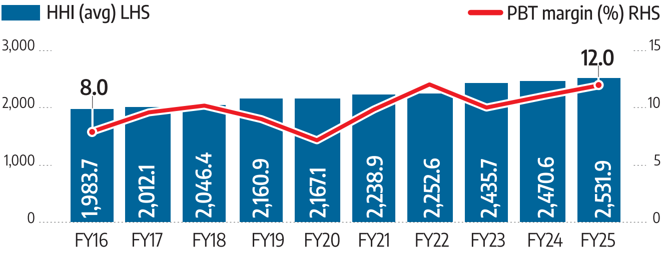
Corporate profits, margins soar as mkt concentration rises

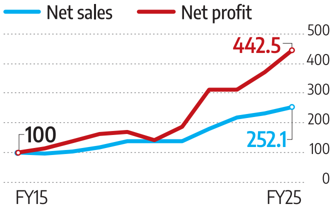
On the upswing

Market concentration vs profit margins



Sales not keeping pace

Earnings growth outpaces revenue growth (Base=100)



Note: Net sales, profits and margins of a common sample of BSE 500, BSE Midcap, and BSE Smallcap companies, excluding BFSI, oil & gas, and IT services firms
Average HHI (Herfindahl-Hirschman Index) for 8 Sectors: Aviation, cement, paints, passenger vehicles, steel, telecom, two wheelers, and tyres. HHI calculation includes the revenue of unlisted companies in the respective sector wherever possible
Sources: Capitaline, credit rating agencies, companies annual reports Business Standard calculation; Compiled by BS Research Bureau

KRISHNA KANT
Mumbai, 16 July

Corporate India has exhibited strong pricing power in recent years, resulting in a steady rise in profit margins across many sectors despite fluctuations in raw material and energy prices, and a persistent slowdown in revenue growth. The margin expansion has been most pronounced in the post-pandemic period.

This improvement in corporate margins has coincided with a steady rise in market concentration in key domestic sectors, as larger players have captured greater market share, either through mergers and acquisitions or through organic growth.

Market concentration, as measured by the Herfindahl-Hirschman Index (HHI), was higher in six of eight sectors in FY25 compared to levels seen in FY15 and FY20. Only two sectors, paints and two-wheelers, have seen a moderation in concentration over the past decade. In all other sectors — aviation, cement, passenger vehicles (or cars), steel, telecom, and tyres — the HHI is now close to all-time highs. Annual HHI scores for these sectors are available beginning FY06.

The average HHI score across these sectors increased to 2,532 in FY25, from 2,167 in FY20 and 1,980 in FY15. According to the US Department of Justice's HHI scale, these levels indicate an extremely high degree of market concentration in key industries.

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India-US trade deal: Trump signals tariffs above 10%

India must negotiate transparently, guard against one-sided outcomes, and not succumb to pressure for quick, symbolic agreements that compromise its long-term economic interests, Srivastava said.

"India must insist on a jointly issued, written statement before acknowledging any agreement. Verbal assurances or informal understandings --especially those announced on social media -- are no substitute for formal, verified commitments," he added.

A team of officials from New Delhi is currently in Washington to negotiate an interim trade agreement ahead of the August 1 deadline. India has been pressing for an exemption from Washington's proposed 26 per cent reciprocal tariff and the existing additional 10 per cent duty.

In a post on Truth Social, Trump said that as part of the deal, Indonesia has committed to buying $15 billion in US energy, $4.5 billion in American agricultural products, and 50 Boeing jets, including several 777s. "For the first time ever, our ranchers, farmers, and fishermen will have complete and total market access to the Indonesian market of over 280 million people," Trump wrote. "If there is any transhipment from a higher tariff country, then that tariff will be added on to the tariff that Indonesia is paying," he added.

Corporate profits and margins surge

Changes in sectoral mkt concentration

Sector	HHI FY15	HHI FY20	HHI FY25
Aviation	2,678.0	2,819.9	4,508.6
Cement	1,060.5	1,267.0	1,713.6
Paints	3,587.3	3,510.7	3,504.7
Passenger vehicels	1,426.6	1,523.7	1,589.0
Steel	1,554.9	1,930.2	2,117.9
Telecom	1,669.9	2,636.0	3,173.5
Two wheelers	2,376.1	2,189.6	2,079.4
Tyres	1,490.3	1,459.5	1,568.7

Note: Net sales, profits and margins of a common sample of BSE 500, BSE Midcap, and BSE Smallcap companies, excluding BFSI, oil & gas, and IT services firms; Average HHI (Herfindahl-Hirschman Index) for 8 Sectors: Aviation, cement, paints, passenger vehicles, steel, telecom, two wheelers, and tyres. HHI calculation includes the revenue of unlisted companies in the respective sector wherever possible
Compiled by BS Research Bureau; Source: Capitaline, credit rating agencies, companies annual reports BS calculation

Historical data shows a positive correlation between HHI scores and corporate margins. For instance, the average profit before tax (PBT) margin of listed companies, excluding those involved in banking, financial services, insurance, oil and gas, and IT services, have risen nearly 300 basis points over the past 10 years. Similar gains are observed in Ebitda (earnings before interest, taxes, depreciation and amortisation) margins since FY2014–15. These companies' PBT margin increased from 7.8 per cent of total revenue in FY15 to 12 per cent in FY25. Over the same period, net profit or profit after tax margin (PATM) expanded from 5 per cent to 8.8 per cent.

As a result, corporate profits have outpaced the underlying growth in revenues or net sales. The divergence between earnings and revenue growth has been especially sharp during the post-pandemic years.

Over the past 10 years, corporate net sales have grown at a compound annual growth rate (CAGR) of 9.7 per cent. During the same period, these companies' combined profit before tax grew at a CAGR of 14.6 per cent, while profit after tax expanded even faster at a CAGR of 16 per cent.

The divergence has been even more pronounced since FY20. In the past five years, corporate net sales grew at a CAGR of 12.7 per cent, while PBT and PAT registered CAGRs of 25 per cent and 25.7 per cent respectively. Even as net sales growth slowed to 7.6 per cent on average in FY24 and FY25, net profits continued to rise, growing at an average rate of 19 per cent in the same period.

Some analysts point to a direct link between rising market concentration and higher corporate margins. "Our data suggests that profit margins in most industries are at their peak levels in the past 25 years. This can be directly attributed to the companies' immense pricing power, which comes from their market dominance," said Dhananjay Sinha, co-head of research and equity strategy at Systematix Institutional Equity.

According to Sinha, regulatory changes and macroeconomic shocks such as demonetisation, the introduction of the Goods and Services Tax (GST), the Insolvency and Bankruptcy Code (IBC), and the Covid-19 lockdown have largely benefited larger companies, enabling them to consolidate their dominance.

This is reflected in changes in sector-specific HHI scores. According to the US Department of Justice's HHI scale, five of the eight sectors in Business Standard's study — aviation, telecom, paints, steel, and two-wheelers — are classified as highly concentrated, with HHI scores of 1,800 or above. The remaining three sectors, cement, tyres, and passenger vehicles, are moderately concentrated, with scores above 1,000 but below 1,800. The HHI ranges from 0, indicating near-perfect competition, to 10,000, where a single firm controls the entire market. The HHI increases as the number of firms declines and as disparities in firm size widen. According to the 2023 US Department of Justice and Federal Trade Commission Merger Guidelines, any transaction that raises the HHI by more than 100 points in an already highly concentrated market is presumed likely to enhance market power.

HHI figures are based on the revenue share of all firms operating within each sector. Business Standard's calculations use reported annual revenues of listed companies, along with key unlisted firms for which data was available. For globally diversified firms such as Tata Steel and Bharti Airtel, only India revenues have been considered.

With little expectation of a near-term decline in market concentration, analysts anticipate corporate earnings will continue to outpace revenue growth. "Our coverage universe of companies is likely to deliver sales/Ebitda/PAT growth of 5 per cent/12 per cent/14 per cent year-on-year respectively in FY26," analysts at Motilal Oswal Financial Services wrote in their latest equity strategy report. This suggests that profit margins could expand further in FY26, even as the financial year marks a third consecutive year of low single-digit revenue growth. Ebitda and PBT margins in FY25 were the highest in the past three years and just below record levels set in FY22.

Some firms hit eject on Cloud-first

Walmart, the world's largest retailer, also decided to adopt a hybrid approach a few years ago.

The company invested in 10,000 edge nodes — in-house devices and servers that can handle data processing locally — to reduce reliance on public Cloud service providers.

Ashutosh Sharma, vice-president and research director at Forrester, says that earlier, enterprises were gung-ho about using public Clouds such as AWS, Microsoft Azure, and Google Cloud Platform for everything, but many have now tempered their exuberance.

"If you look at Europe, there is a huge desire to repatriate. Repatriate in the sense that they are not just content having it in their own data centres. They also have concerns about putting their workloads into global Cloud service providers that originate from the US. So they are thinking of working with local Cloud providers or putting certain workloads onto platforms that the government and local regulations have some control over," he added.

AWS told the UK's Competition and Markets Authority last year that its Cloud business faces competition from on-prem information technology. It also said that building a data centre requires considerable effort, so the fact that customers are doing it highlights both their level of flexibility and the attractiveness of moving back to on-prem.

"AWS said that customers may switch back to on-prem for a number of reasons, including to reallocate their own internal finances, adjust their access to tech, and increase the ownership of their resources, data, and security. AWS said that perceived benefits of on-prem may include closer control of assets and proximity," according to the report.

However, that doesn't mean Cloud is facing an imminent existential threat, especially at a time when the three Cloud giants are pouring billions into it.

James Blake, vice-president, cyber resiliency strategy at cybersecurity firm Cohesity, said that repatriation is happening mainly among firms that never fully embraced Cloud.

"They literally lifted and shifted what they were doing on-prem to Cloud. They just took their physical servers, created virtual images of them, and launched those virtual images in Cloud. From a return on investment perspective, I think you're missing a trick in some of the more advanced automations and feedback loops that you can create if you're using something like CloudFormation or Terraform — if you go to the extreme of infrastructure as code," Blake explained.

Deepak Mittal, chief executive of CloudKeeper, which provides Cloud cost optimisation solutions, said that there are other benefits to being on Cloud.

"Clients are not locked in, and there is no capital expenditure. They can change their mind. There's this whole scale-up and scale-down thing that you'll never get with a data centre. However, if your business is fixed, you know that these are your computing needs and those will not change over a five-year period, then you can move that part of the operation to your own data centre," he said.