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When profitability is under strain

Tania Kishore Jaleel / Mumbai September 1, 2011, 0:18 IST

EPS of a company can fall due to pressure on profitability or rise in the number of shares. The latter shouldn't worry you too much.

With the March-June earnings growth under pressure due to high interest rates and input costs, a large number of companies were badly hurt, especially on the earnings per share (EPS) front.

The Nifty-50 saw 15 scrips report a fall in EPS, with Reliance Communications reporting the highest decline (61.7 per cent) on a year-on-year basis. For an investor in the company, this is surely bad news.

EPS is the portion of a company's profit which is allocated to each outstanding share of common stock. Higher the EPS, the higher each share should be worth. It serves as an indicator of a company's profitability. A positive EPS trend indicates the company is constantly looking to increase its earnings.

Alex Mathew, head (research), Geojit BNP Paribas Financial Services, says EPS could fall when the current market price of a stock falls. "If the market conditions are bad, EPS is bound to fall. It is indicative of the company's performance."

Some companies that have seen a dip in EPS include Maruti Suzuki, DLF, Cipla, Ambuja Cements, State Bank of India, Bharti Airtel and Reliance Communications. If you are invested in scrips whose EPS has dipped during the quarter, the current scenario clearly indicates an uncertain short-term outlook.

HOW THEY STACK UP

TOP 5 LOSERS IN NIFTY			
	■ EPS June 2011 (₹)	■ EPS June 2010 (₹)	% chg
Reliance Capital	10.04	15.55	-31.57
Bharti Airtel	14.69	21.55	-31.81
Ranbaxy Labs	17.99	33.30	-54.24
JP Associates	3.56	8.15	-56.31
Reliance Comm	6.06	15.84	-61.72
TOP 5 GAINERS IN NIFTY			
Dr Reddy's Labs	4.22	68.29	1518.00
Cain India	6.77	46.15	582.13
Tata Steel	21.11	130.36	517.57
Tata Motors	77.03	135.24	89.92
Bajaj Auto	69.01	119.60	73.31

Jagannadham Thunuguntla, head (equity), SMC Capitals, says companies which cannot handle the pressure of rising inflation, input costs and interest rates have seen a dip in earnings and EPS. "If investing now, one should choose with caution. Sectors such as real estate and infrastructure will be under pressure. If inflation and interest rates continue to be high, it will weigh on earnings growth", he says.

Another reason why EPS can decline is an increase in free float, or the number of a company's shares in the market.

However, in such circumstances, investors should not be too worried. Abhinav Angirish, managing director at Abchlor Investment Advisors, says investors should not get unnerved.

"The second quarter earnings have been slow due to rise in interest rates. Those invested in stocks whose EPS has fallen should not be in a hurry to exit. The overall earnings are down, so a quarter or two of falling EPS should not be reason enough for one to exit immediately," he adds.

So, when deciding on whether to stay invested or not in a stock which has witnessed a fall in EPS, you should identify the reason behind the decline.

“With interest rates likely to peak soon, we might see them drop soon. Companies facing the burden of high interest costs right now will get a breather in the near future. So, firms which have seen a dip in EPS due to high interest costs could be held on to. However, those with high input costs due to high commodity prices, could be looked at with caution”, advises Mathew.

Some companies that saw a rise in EPS are Dr Reddy's, Cairn India, ONGC, Infosys, Tata Steel, ICICI Bank and Reliance Industries.

Tags : EPS | profitability | earnings growth | Nifty-50 | Reliance Communications | Alex Mathew | Geojit BNP Paribas Financial Services | Jagannadham Thunuguntla | Abhinav Angirish |