

# Relationship between the Base Interest Rate and Share Prices of FMCG Companies in India

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## ABSTRACT

This is a study on "RELATIONSHIP BETWEEN THE BASE INTEREST RATE AND SHARE PRICES OF FMCG COMPANIES IN INDIA" which aims to check if there exists any relationship between the share prices of fast moving consumer goods (FMCG) and the base interest rate in India, by the using paired t test. For this study we have considered top 8 listed FMCG companies in India. The top 8 companies have been chosen based on their turnover at the latest reporting date. The period of this study is 5 years. The FMCG companies chosen for this study are Hindustan Unilever Limited (HUL), Colgate – Palmolive, ITC Limited, Nestle, Britannia Industries Limited, Marico Limited, Procter and Gamble, and Godrej Group.

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## 1. Introduction

### Denotation of FMCG

Fast Moving Consumer Goods are consumer goods of chronic nature that are purchased by customers on a recurrent basis. Goods that come under the bracket of FMCG are all consumables except pulses, fruits and legumes. The term FMCG is domestic term that is used only in the Indian Economy. Though this sector is present globally, this sector is denoted overseas as 'consumer packaged goods'.

### An Understanding of FMCG Industry in India

As per November 2018, India Brand Equity Foundation Report (India Brand Equity Foundation, 2018), the FMCG is considered one of the prodigious sectors of the Indian Economy and is the fourth largest sector of the economy. This sector contains three major segments which are namely; food and beverages, healthcare and household and personal care. Among these three segments in the FMCG sector, household and personal care segment is the largest which accounts to 50% of the sector followed by personal care which accounts to 31% and the lowest being food and beverages at 19%.

The FMCG industry in India is growing swiftly in India. This sector has grown from US \$ 31.6 Billion in 2011 to US \$ 52.75 Billion in 2017 – 2018, moreover, this sector is expected to grow by 27.86% CARG. The reason for this swift upward movement in growth is due to a number of factors such as shift to more organized markets, increase in penetration, easy availability of products due to increase in distribution channels and finally an increase in consumption by the rural population. Apart from higher expected growth of FMCG Industry, another dazzling feature of this industry in India is that it attracts a lot of perks, such as support from the government in terms of policies and growing demands thereby making this sector inordinately attractive.

### Understanding Base Rate

The base rate concept was brought forward on 1<sup>st</sup> of July 2011, in the slightest degree across banks India. The BPLR (Benchmark Prime Lending Rate) was utilised before the concept of base rate system was introduced. Credit pricing had been of great clarity with the introduction and implementation of the base rate. The base rate is that the minimum ROI (rate of interest) that's set by RBI to grant a loan. This rate is typically taken because the normal rate by all the banks functioning therein country. Once the base rate is declared by the RBI, no bank is permissible to grant any of loan to its customers at a rate that's not up to base rate that has been introduced on that date by the RBI. The base rate was introduced by the RBI as the credit market didn't have much transparency

## 2. Review of Literature

**A)** In India, Fast Moving Consumer Goods (FMCG) constitutes the fourth largest sector of the economy. Over the last couple of years, the FMCG sector has witnessed tremendous growth and is continuing to grow briskly. As per CARE Rating Report (Sabnavis, Kansara, & Mishra, 2018), in the year 2019, this sector will behold a growth of around 14% to 16%, despite the fact that in 2018, this sector witnessed a sedated growth of 2.4% that is lower by 400 basis points in contrast to the precursory years.

**B)** The lowering down of growth of the FMCG Sector in the year 2018 is constituted by the introduction of Goods and Service Tax (GST) during the year. The post implementation effect of GST was strongly felt on the FMCG Sector. The enforcement of GST led to 3% to 8% fall in prices of goods produced by the FMCG Sector at various retail stores across the country. This fall in price of goods led to a ramped decrease in net profits of about 60%. However, the net sales had seen a growth of around 1.5% during the year in comparison to sales in the year 2017. In spite of the growth in net sales, the impact of the fall in prices of consumer goods led to a decline of net profit margin of around 4.4%. The reports of HDFC Securities (HDFC Securities, 2017) indicate that

financial year 2017 and 2018 was arduous year for the FMCG Sector due

**C)** In accordance with the reports of Livemint (Mishra, 2015), the Indian Economy falls among the top 10 attractive countries for Foreign Direct Investments (FDI). During the year 2017 – 2018, the FDI Investments in India stood at USD 69.96 Billion as mentioned by the DIPP Secretary, Ramesh Abhishek, out of which USD 13.07 Billion belongs to the FMCG Sector.

**D)** The study conducted by Dharia Dilasha and Kakadia Sachita (Dilasha & Sachita, 2015) depicts that there are many factors that affect the share price of FMCG Companies. Some of which has been talked about in their study are revenues, operating profit, net profit, operating profit margin, netprofit margin, reserves, debt, P/E and EPS.

**E)** An article penned down by Viveat Susan Pinto (Pinto, 2018) states that the trend of premiumisation has been a rugged theme for the FMCG Sector in the past but the picture today is quite divergent. On having a closer look at the turnover of FMCG Companies turnover, one can elucidate that 75% of the sales of the FMCG firms are led by volume led growth while only 25% is price led growth. This situation is antithetical to that of financial years 2014 to 2016 where the price led growth was at 50% to 60%. This indicates that for FMCG firms today, sales volume is the pretext for its growth.

**F)** This study focuses on two aspects one being the share price of FMCG Companies and the other factor is Base Rate. In simple words base rate is minimum rate at which commercial banks can lend loans and is determined by the central bank of a country. The article by Rajrishi Singhal (Singhal, 2010) gives an in depth understanding of what base rate means and implies in the Indian context and why this new terminology was adopted by the Reserve Bank of India and what perks and drawbacks it carries along with itself.

### 3. Research Design

#### Statement of Problem

Base rate in the India Economy is a relatively unexplored topic. This is predominately because it was introduced by the RBI on 1<sup>st</sup> July 2011 that is about 8 years ago. On understanding base rate it can be observed that it has an effect on the loan borrowers. Since FMCG Sector is a loan driven sector, the changes of base rate could impact the FMCG Companies share price. This research paper helps in the understanding the relationship between base rate and share

price of FMCG companies thereby aiding investors make a sound investment decision.

#### Sources of Data

Secondary data has been taken for the purpose of this research paper.

The historical base rate and share prices has been collected from the following websites –

- <https://dbie.rbi.org.in/DBIE/>
- <https://www.nseindia.com/>

#### Hypothesis

Null (H0): There exists no relationship between the base rate and share price of FMCG Companies.

Alternative (H1): There exists a relationship between the base rate and share price of FMCG Companies.

#### Limitations

1. This study focuses on only two variables that is base rate and share price of FMCG companies, but it is important to note that there are other factors that affect the share price of FMCG companies, which has not been considered as they are extraneous variables and fall outside the scope of the study.
2. The reliability of the data depends upon the reliability of secondary sources such as RBI and NSE.
3. Only top 8 listed companies based on their turnover is selected thereby limiting the accuracy of the study.
4. The time frame of historical data is only 5 years therefore, it may not give a complete picture on the relationship between share price of FMCG companies and base rate.

### 4. Data Analysis and Interpretation

In order to find out if there exists any relationship between the Base Rate and Share Price of FMCG Companies, secondary data was first extracted from RBI and NSE websites. A sample of 8 FMCG companies is selected for the purpose of this study. The selection is made on the basis of turnover wherein listed companies with highest turnover is chosen. Following the extraction of data, the base rates of announced by RBI was matched against the adjusted close price of the shares of the FMCG companies. To check whether or not any possible relationship prevails Paired Sample T Test. The results of the test is provided below:

#### Paired Samples Test

		Paired Differences				t	df	Sig. (2-tailed)	
		Mean	Std. Deviation	Std. Error Mean	95% Confidence Interval of the Difference				
					Lower				Upper
Pair 1	BaseRate - HUL	-865.9059024	341.8267402	20.39167372	-906.0463514	-825.7654535	-42.464	280	.000
Pair 2	BaseRate - Colgate	-853.1345804	183.3366725	10.93694894	-874.6636637	-831.6054972	-78.005	280	.000
Pair 3	BaseRate - ITC	-218.7585981	37.28844564	2.224442173	-223.1373514	-214.3798449	-98.343	280	.000
Pair 4	BaseRate - Nestle	-6267.587112	1564.542627	93.33278824	-6451.310139	-6083.864085	-67.153	280	.000
Pair 5	BaseRate - Brit	-2703.160553	1681.936962	100.3359472	-2900.669106	-2505.652001	-26.941	280	.000
Pair 6	BaseRate - Marico	-202.3460213	87.95184758	5.246767346	-212.6741385	-192.0179041	-38.566	280	.000
Pair 7	BaseRate - PampG	-6097.756626	2355.446626	140.5141652	-6374.354896	-5821.158356	-43.396	280	.000
Pair 8	BaseRate - Godrej	-433.0613727	184.2671165	10.99245458	-454.6997172	-411.4230281	-39.396	280	.000

The above table shows that at a confidence level of 95%, the significance level is 0.000 for all the cases. Since the significance level is less than 0.05, the null hypothesis is rejected and the alternative hypothesis is accepted. Thereby validating the study.

### 5. Findings

This research paper elucidates that there is a strong relationship between the Base Rate and the Share Price of FMCG Companies in India.

### 6. Conclusion

We can make a primary conclusion that the equity share price of the various companies does move with the movements in Base Rate set by RBI. Base Rate was introduced by RBI as a minimum ROI (rate of interest) to grant a loan. It was introduced by the RBI as the credit market didn't have much

clarity; as some segment were unseen. The importance of base rate can be seen to provide great transparency and clear info on how much rate of interest a bank can really charge for a loan. Hence, the base rate brings about a well uniform and accepted rate to the nation's banks.

FMCG companies are loan-driven. Therefore, borrowing from private banks as capital is a commonality. Banks tend to charge lower rates of interest when they are permitted to do so; because base rate defines this it is of importance to equity shareholders.

This could provide investors or securities analysts a method to predict the variation for share prices of FMCG companies in India.

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