Investment Snapshot

For the quarter ended in December - FY 22

INDIAN MARKETS, A LONG TERM OPPORTUNITY

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Quarter gone by for Macros

Global macros in CY2022 have been in a perfect storm of energy led inflation, which led to one of the fastest rate hike cycles initiated by central banks. Consequently, global economy has begun to show signs of impending slowdown in growth and moderating price pressures. The Impact of tightening financial conditions, elevated inflation and high prices/shortage of food and energy has started reflecting in moderating global PMI's and business confidence Indexes. Hence, the narrative for global macros in CY2023 has now transformed to that of global central banks slowing down on rate hikes, as inflation abates across economies and growth slowdown is getting more pronounced.

On the positive side, Inflation has now started receding with normalisation of supply chains and cooling of energy prices. The key silver lining is that despite an uncertain and volatile global environment, Indian economy has been largely resilient and has emerged as an oasis of hope, mainly led by strong domestic demand, robust festival season, waned Covid impact, and expectations of a prolonged capex cycle. High-frequency indicators such as strong credit growth, robust GST collections, expansionary PMI's, improving auto sales, electricity demand & strong toll collections along with receding Inflationary pressures and comfortable forex reserves are key positives.

Quarter gone by for Equity Markets

With respect to markets, Global equities witnessed great amount of volatility amidst aggressive rate hikes. Indian Equity Markets has had a modest CY2022 amidst heavy volatility with the benchmark Nifty Index delivering 4.3% returns. However, in the global context, it's CY22 performance was spectacular compared to global counterparts. During CY22, MSCI EM lost ~22%, and MSCI world lost ~20% of its value in USD terms, while Nifty 50 was down only ~6% in comparable terms. The performance is extremely enthusing given the fact that Foreign Investors (FII's) have been relentless sellers, which has been equally matched by domestic investors. The markets were led by domestic facing sectors like Banking & Financials, Autos, Cement, and Capital Goods & Infra while the export oriented sectors like IT & Pharma underperformed.

Q4CY22 was a volatile quarter with the market oscillating between fears of aggressive tightening and recessionary fears. The quarter saw a sharp recovery in global markets led by China's reopening and its decision to finally drop COVID zero policy, US inflation coming off, and consequent pace of rate hikes slowing down across central banks. For the quarter, India underperformed global peers in Q4CY22 in relative returns, even though absolute returns were positive. Stepping into CY2023, while Indian markets came under pressure on concerns around corporate governance in a renowned corporate group, but fundamentals remain intact.

In terms of FII flows, FII's went on to be net buyers in H2CY23, after sharp selling spree seen in H1CY23 as second half saw durable reversal in trend of FII selling led by strong earnings momentum in India, which aided it to outperform most global peers. In Q4CY23, FII's continued to be net buyers, investing net of US $ 5.5 bn in Indian equities while DII's remained strong participants, investing net of US $ 35.8 bn in Indian equities in CY22 (net buyers of US $ 3.3 bn in Q4CY23), finding support from strong retail participation. In CY2023, the tide has again turned negative with FII's turning net sellers, while DII's continuing to be net buyers.

Union Budget 2023-24 is indeed a progressive and growth oriented budget, continuing the path and vision laid down in the earlier budgets. Pro-Growth measures and Capex oriented focus was yet again the overarching theme of Budget 2023-24, thus exemplifying government's unflinching resolve to sustain the growth recovery amidst looming global growth slowdown. The government has dexterously delivered a fine balancing act, by sticking to the fiscal consolidation glide path, while continuing the pace of infra led – capex spend, along with credible revenue and nominal GDP growth assumptions.

Quarter gone by for Debt Markets

With respect to rates markets in CY22, global as well as domestic bond yields have risen sharply in response to aggressive tightening by global central banks, as inflation remained elevated. Consequently, we saw US Fed increase rates cumulatively by 450bps, while RBI increased rates by 250bps in this cycle. In Q4CY22 we saw US Fed increasing rates cumulatively by 125bps during the quarter as though US inflation began to show signs of easing, robust labour market conditions led to rise in US bond yields. The dollar however eased from highs while crude oil prices moderated. Inflation continued to fall both in US as well as in India. RBI also lowered the pace of hike from 50bps to 35bps and to 25bps in Feb 2023. Domestic bond yields softened from the previous quarter, while the INR depreciated despite easing of crude oil prices and FX reserves rebounding from lows. High frequency indicators continued to hold up, supported by a robust festive season. With governments' net borrowing via market loans for next fiscal being contained at ₹11.8 lakh cr despite heavy capex announcement, along with the government reiterating its fiscal consolidation glide path to less than 4.5% fiscal deficit by FY26 was indeed reassuring for bond markets.

While INR has depreciated by ~11% against USD in CY22, much of this depreciation can be attributed to the strengthening of USD, as aggressive rate hikes by Fed this year has led to a sharper interest rate differential, which led to sharp strengthening of USD. Elevated trade deficits and the RBI recouping some of its depleted reserves kept the INR under pressure, leading to a depreciation of ~1.7% in Q4CY22, despite moderation in crude oil prices. However, the worst of pressures on the CAD seem likely behind with the easing of crude oil prices.

Macro- Economic and Fixed Income Outlook

Despite the global challenges, we remain constructive on the Indian economy. We believe the global macro environment may remain challenging as long as global monetary policy tightening continues, but very likely with pronounced slowdown in global growth and lowering inflation, central banks will gradually change their stance and end monetary tightening in the ensuing quarters. From domestic macros perspective, we believe in the current global landscape, India's positioning is quite favourable from domestic standpoint. On the domestic growth front, high frequency indicators continue to indicate resilience although export growth may face some headwinds from slowing global growth. Inflationary pressures have started abating, although core inflation is yet sticky. Rural growth has been under pressure amid inflationary headwinds and erratic monsoons, but strong Rabi sowing trends and easing inflation may aid the rural growth recovery going forward. Besides, Union Budget has indeed touched upon the key chords of growth in terms of capex thrust via infrastructure spend and support for MSME's in the form of credit guarantee schemes, aiding employment generation and consumption. Most importantly, it has provided tax reliefs at individual taxation front, which will help spur consumption in the lower- and middle-income strata, which augurs well for the economy. The Budget has also reintroduced P note mechanism for capital market, which should help revive FII's interest in India. Improving utilisation levels, lower corporate debt levels, higher profitability should augur well for a gradual uptick in investment demand. We reckon the Indian economy remains firmly entrenched on the path of recovery with broader long term fundamentals of the economy remaining intact. With respect to external account and INR, with the moderation in crude oil prices and peak of Fed's hawkishness being behind us, we reckon the worst of the pressures on CAD and INR depreciation are likely over and FX reserves are also off from lows.

From debt markets standpoint, Over last one year, Global and Domestic bond yields have been rising sharply due to aggressive stance on policy tightening by global central banks given the persisting high Inflation led by global supply chain disruptions and elevated commodity prices due to geopolitical disturbances. Amidst the global backdrop, RBI in sync with other global central banks has hiked rates by 250 bps cumulatively vs 450 bps by US Fed. RBI has embarked on frontloading of rate hikes given the backdrop of synchronized aggressive global policy tightening stance, concerns emanating on external account & rupee and volatility witnessed in global forex and rates market. Going forward, with imminent global growth slowdown and Inflation trajectory treaded lower, the bar for aggressive rate hikes in the ensuing policies is much higher and hence we believe we are close to the fag end of rate hiking cycle in India and globally. We don't expect a major uptick in yields from here-on, unless new challenges emerge. As we see inflation has peaked globally and has started treading downward now, thanks to hardening of interest rates globally & impact of steps taken by Government & monetary authorities. We expect Indian yields to remain range bound in response to the recent rate hikes and fear of persistent core inflation.

We believe interest rates would eventually start treading lower, as central banks gradually change their stance and get more dovish in response to pronounced growth slowdown and lower inflation trajectory. We expect Indian yields to remain range bound with a downward bias over the next few months.

Equity Outlook

We believe that the FII selling is tactical in nature and flows would eventually come back to India owing to strong long term structural growth potential which would bode well for future returns. We reckon the global markets backdrop would eventually stabilise, as stated above that the worst is behind and with base catching up and cumulative impact of central banks rate hikes start playing out. With respect to domestic equity markets, while the global headwinds are clouding the Indian markets and imparting bouts of volatility, we reckon structurally Indian markets are in a relatively good stead with strong economic and earnings recovery at sight coupled with multi-year investment cycle, which will continue to provide tailwinds and cheer the markets. Besides Union Budget continues to provide the requisite support via capex thrust, which would have a great multiplier impact on economic growth and employment generation in the country. High frequency indicators such as PMI's, GST, Electricity demand, Tax collections etc. continue to remain significantly into expansionary zone, despite the global data points cooling off/moving into contraction significantly. We believe Indian markets are at the cusp of a virtuous new earnings growth cycle. The current macro backdrop this time around is quite conducive with resilient domestic GDP growth, better Inflation management, deleveraged corporate balance sheets and fortified financial system balance sheets with lower NPA's and strong credit offtake, thus adding credence to our belief that strong momentum in India's corporate earnings growth cycle is imminent.

Over the past year, equity markets have weathered numerous adverse events like Russia-Ukraine conflict, surging energy costs (Crude oil & Natural gas), unprecedented inflation in developed world and consequent aggressive global monetary tightening etc. The markets have remained reasonably resilient especially amid the onslaught of relentless FII selling of more than ₹3 lakh crores over the past 12 months. We believe that the FII selling is tactical in nature and flows would eventually come back to India owing to strong long term structural growth potential, which would bode well for future returns. On the valuations front, even though the markets are barely 5% away from their all-time highs, they have had a reasonable time correction of over 18 months now. The earnings during these 18 months have caught up, which have ensured valuations revert to more reasonable levels providing a lot of comfort. Going forward, we remain constructive on Indian equity markets from the medium to long term perspective. BFSI and Consumption facing sectors such as FMCG, Auto and infra push beneficiaries – Capital goods would be the key themes in the ensuing year. Thus, Indian Equity markets present attractive opportunities given the compelling macro growth prospects in sight and we expect Indian equities to continue to command better valuation premium compared to EM peers. Given this construct, we remain constructive on equities as an asset class and history has exemplified that we should be believers in the ability of Equities to compound wealth over long period of time. We advise investors to partake in long-term potential of India and stay on course to leverage any dips, as an opportunity to buy.

Indicators	Q2FY20	Q3FY20	Q4FY20	Q1FY21	Q2FY21	Q3FY21	Q4FY21	Q1FY22	Q2FY22	Q3FY22	Q4FY22	Q1FY23	Q2FY23
Real GDP % YoY	4.4	4.1	3.1	-24.4	-7.4	0.5	1.6	20.1	8.4	5.4	4.1	13.51	6.3
Real GVA % YoY	4.3	3.5	3	-22.4	-7.3	1	3.7	18.8	8.5	4.7	3.9	12.8	5.6
Agriculture	3.5	3.6	5.9	3.5	3	4.5	3.1	4.5	4.5	2.6	4.1	4.5	4.6
Industry	0.5	-0.4	0.0	-31.0	-1.6	1.6	5.5	40.4	9.3	2.5	1.0	8.6	-3.1
Services	6.5	4.9	3.5	-24.9	-11	-0.2	3.2	16.1	11.1	9.2	5	17.7	9.3
Export Growth %	-4.1	-2.2	-12.4	-36.8	-5.5	-4.9	19.3	86.3	39.4	41.1	29.3	26.1	7.2
Import Growth %	-11.5	-12.5	-9	-51.7	-23.5	-3.5	19.2	105.7	66.49	50.9	29.7	45.0	31.0
Trade balance $ bn	-38.1	-34.6	-35.0	-10.8	-14.8	-34.5	-41.7	-30.7	-44.8	-59.7	-54.5	-63.0	-83.5
Current account balance $ bn	-6.3	-1.4	0.6	19.2	15.5	-1.7	-8.2	6.5	-10.0	-22.2	-13.4	-18.4	-36.4
Balance of payments $ bn	5.1	21.6	18.8	19.8	31.6	32.5	3.4	31.4	30.8	1.3	-16.1	4.4	-30.4
CAD as % of GDP	-0.9	-0.2	0.1	3.8	2.4	-0.1	-1.0	0.9	-1.3	-2.6	-1.5	-2.2	-4.4

Snapshot of Macro Indicators

Source: Bloomberg, Reuters & FG Research

Indicators	Yearly Data												
	FY10	FY11	FY12	FY13	FY14	FY15	FY16	FY17	FY18	FY19	FY20	FY21	FY22
GDP Growth %	7.9	8.5	5.2	5.5	6.4	7.4	8	8.3	6.8	6.5	4	-7.3	8.7
GVA growth %	6.9	8	5.2	5.4	6.1	7.2	8	8	6.2	5.9	4.1	-6.2	8.1
CPI Inflation Avg	12.3	10.5	8.6	9.9	9.4	5.9	4.9	4.5	3.6	3.4	4.8	6.3	5.5
Exports (US $ bn)	182	256	310	307	319	317	266	280	309	337	320	296	422
Imports (US $ bn)	301	383	500	502	466	461	396	393	469	518	478	399	612
Trade Deficit (US $ bn)	-118	-127	-190	-196	-148	-144	-130	-112	-160	-180	-158	-102	-190
Trade Deficit (%of GDP)	-8.8	-7.6	-10.4	-10.7	-7.9	-7.1	-6.2	-4.9	-6	-6.7	-5.5	-3.8	-6.1
Brent Crude oil prices Y/E	81.3	117.3	123.8	109.3	107	53.3	38.7	52.7	69.1	70.3	21.5	62.4	106.6
Oil Import USD Bn	86.8	105.8	155	163.8	164.9	137.8	82.6	86.9	108.7	141.1	130.5	82.4	160.1
CAD $ Bn	-38.2	-48.1	-78.2	-88.2	-32.4	-27.9	-22.2	-15.3	-48.7	-57.3	-24.6	24	-13
CAD (% of GDP)	-2.8	-2.9	-4.3	-4.8	-1.7	-1.4	-1.1	-0.7	-1.8	-2.1	-0.9	0.9	-1.2
Capital account balance (US $ bn)	51.6	62	67.8	89.3	48.8	90	41.1	36.5	91.4	54.4	79.1	63.7	86
FDI (US $ bn)	18	9.4	22.1	19.8	21.6	32.6	36	35.6	30.3	30.7	43	44	39
FII (US $ bn)	32.4	30.3	17.2	26.9	4.8	40.9	-4.1	7.6	22.1	-0.6	1.4	36.1	-16.8
Total BoP (US $ bn)	13.4	10.9	-12.8	3.8	15.5	61.4	17.9	21.6	43.6	-3.3	59.4	87.3	47.5
Fiscal Deficit %	-6.6	-4.9	-5.9	-4.9	-4.5	-4.1	-3.9	-3.5	-3.5	-3.4	-4.6	-9.2	-6.7
Foreign Reserves (US $ bn)	279	305	294	292	304	342	360	370	425	413	478	579	607
Rupee (INR/$) Average	47.4	45.6	48.1	54.5	60.9	61.2	65.7	67.1	64.5	69.9	71	74.2	74.4
Repo Rate year ending	5	6.8	8.5	7.5	8	7.5	6.8	6.3	6	6.3	4.4	4.4	4.0
US-10 year end	3.8	3.5	2.2	1.8	2.7	1.9	1.8	2.4	2.7	2.4	0.7	1.7	2.3
GIND-10 year end	7.83	8.02	8.56	8.01	8.88	7.8	7.4	7.06	7.42	7.35	6.14	6.17	6.84

Source: Bloomberg, Reuters & FG Research

Market performance

Performance of Indian Equities across Market Caps and Debt benchmarks as on Sep' 30th, 2022

Sector	7 year CAGR	5 year CAGR	3 year CAGR	1 year	6 months	3 months
Nifty	12.5%	11.4%	14.2%	4.3%	14.9%	5.9%
Sensex	12.8%	12.3%	13.8%	4.4%	15.0%	5.9%
Nifty Midcap Index	13.0%	8.3%	22.6%	3.5%	18.5%	2.7%
Nifty Smallcap Index	8.1%	1.4%	18.6%	-13.8%	14.8%	3.1%
NIFTY Composite Debt Index	7.1%	6.7%	5.4%	1.9%	4.3%	2.2%

Source: Bloomberg, Reuters & FG Research

Global Indices Performance (%)

	7 year CAGR	5 year CAGR	3 year CAGR	1 year	6 months	3 months
Dow Jones Index (USA)	9.6%	6.0%	5.1%	-8.8%	6.6%	15.4%
S&P 500 (USA)	9.4%	7.5%	5.9%	-19.4%	0.4%	7.1%
NASDAQ Composite (USA)	11.1%	8.7%	5.3%	-33.1%	-5.9%	-1.0%
Nikkei 225 (Japan)	4.6%	2.8%	3.3%	-9.4%	0.6%	0.6%
Hang Seng (Hong Kong)	-1.5%	-7.9%	-11.1%	-15.5%	-9.5%	14.9%
FTSE 100 (UK)	2.6%	-0.6%	-0.4%	0.9%	3.9%	8.1%
Shanghai Composite Index (China)	-1.9%	-1.4%	0.4%	-15.1%	-8.8%	2.1%
DAX (Germany)	3.8%	1.5%	1.7%	-12.3%	8.7%	14.9%
iBovespa (Brazil)	14.2%	7.5%	-1.7%	4.7%	10.9%	-0.3%
MICEX (Russia)	2.9%	0.4%	-10.9%	-43.1%	-2.4%	10.1%

Source: Bloomberg, Reuters & FG Research

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