

INDIA REWIND

India Rewind is a monthly update from DSP's Investment desk. It separates the alpha from the noise and aims to deliver key insights to readers, packed within a 2 minute reading time.

We were in the US and Canada this past month for investor meetings. Many of the questions were on India's growth potential, rising crude, earnings impact and inflation. On that last one, while we have been reading about it for the longest time, nothing hits home like personal experience. And so on our trip, "Sorry we don't do room service anymore" was a common thread across hotels, while many stores that displayed ads for employing workers (~15-18 USD/hour) were still struggling to fill positions. Is it the same in India? Not just yet we would think.

Inflation in India (CPI ~7.7%) remains elevated mainly driven by rising crude, food and commodity prices. While wages have increased in export-oriented sectors like IT services and also Startups (fueled by ~USD 38bn VC investments in CY21), we do not see evidence of labor shortage, at least for now. To tackle inflationary pressures for the common man, the Indian govt. i) reduced excise duty by ~INR 8/liter on petrol prices, which is expected to reduce CPI by ~30bps (assuming oil prices stay ~USD 110/bbl), ii) increased subsidy on cooking gas (~INR 200/cylinder) and iii) increased additional subsidy for fertilizers by ~USD 14bn. This does put some pressure on the fiscal, but the govt. has some buffer from robust tax collections given a strong economic reopening post Covid (GST collection last month at ~USD 19bn, +44% YoY). Despite various uncertainties, India's GDP grew by ~8.7% in FY22 (recovering from contraction of ~6.8% in FY21). India is still expected to grow ~7.5% in FY23E, the highest among large economies.

On the ground update: On the rural front, tractor and two-wheeler registrations sequentially improved up ~5% MoM. The govt.'s rural employment program is picking up (~+32% YoY). Agricultural exports continue to improve (up ~25% YoY) driven by higher exports of oil seeds, dairy and poultry products. On the urban front, e-way bills which are a forward-looking indicator for GST collections are up ~5% QoQ. On a monthly basis, ~75m e-way bills are generated now, which is higher than the pre-pandemic high of ~57m. Recovery in demand and business pickup led to an all-time high GST collection of ~USD 195bn in FY22 (vs USD ~154bn FY19, pre-Covid). Manufacturing and construction activities continue to remain strong.

Flows: In CYTD22, FIIs have been net sellers in Indian equities to the tune of ~USD 22bn while DIIs have played 'the balancer', buying ~USD 24bn. The monthly systematic inflows from retail investors into mutual funds have been strong at ~USD 1.5bn. Since Oct'21, FIIs have now sold ~USD 32bn (0.8% of market cap vs. 2% during GFC) and ~80% of selling was in banks and infotech (i.e. sectors heavily owned by FIIs). This has been the largest absolute selling in India's history, but almost surprisingly (and thanks to the domestic 'balancers'), markets have corrected just ~9% in this period.

Earnings: 4QFY22 results season in India is winding down. About 95% of MSCI India's market cap (97 out of 107 companies) have reported earnings so far. 4Q profits are up ~20% YoY/9% QoQ. Among these 97 companies, beats and misses are evenly split ~40% each, while ~20% reported in line with expectations. Metals, Utilities and Banks saw the largest positive surprises while Consumer Staples and Pharma saw misses. Some takeaways from management guidance: i) companies across sectors are facing margin headwinds from increased input cost despite calibrated price hikes, ii) auto companies are seeing strong enquiry and demand but continue to face supply constraints (waiting periods of 4-6 months for new cars are common), iii) managements remain hopeful of rural recovery given likely good harvest season, expectation of normal monsoon and higher agri prices.

Valuations: With the recent correction, Nifty 12MF PE is now at ~18X which is ~21% off the peak of ~22.9X, and 1SD above the long-term average. This PE multiple has come off from the peak on account of two factors: a) ~12% price correction and b) an upward revision in earnings over the last 6 months and earnings roll over. For the month of May'22/YTD, MSCI India USD Index returned ~-6%/-9.5%, MSCI India Smallcap Index returned ~-8.4%/-14.8%, while MSCI EM returned ~-0.1%/-12.5%. One of the questions on investors' minds is, "Is there further market downside from here?". Nobody knows the future of course, but here below is an interesting *Chart of the Month*, depicting how global and Indian equity markets performed across drawdown cycles earlier. On average, India has fallen ~37% from the peak in prior crises, while in the current one (inflation, rate-hike cycle), the market is down ~12%. Are we headed lower from here, or are investors pricing-in India as a structural opportunity?

Chart of the Month: Markets performance across drawdown cycles (MSCI Indices)

Price correction (peak to trough for each market)									
Region	Asian Financial Crisis	Tech Bubble	Global Financial Crisis	European Crisis	Shanghai Bust	US-China Trade War	COVID	Average	Current Crisis
India	-43%	-61%	-69%	-38%	-27%	-20%	-23%	-37%	-12%
China	-79%	-72%	-66%	-29%	-39%	-30%	-22%	-48%	-43%
EU	-16%	-45%	-61%	-29%	-16%	-19%	-26%	-28%	-13%
Hong Kong	-60%	-46%	-57%	-24%	-24%	-20%	-29%	-35%	-21%
Indonesia	-93%	-76%	-68%	-21%	-36%	-24%	-52%	-47%	-6%
Singapore	-68%	-55%	-61%	-24%	-30%	-21%	-39%	-40%	-20%
Taiwan	-55%	-67%	-60%	-28%	-25%	-17%	-30%	-37%	-15%
Thailand	-92%	-63%	-59%	-25%	-28%	-17%	-45%	-43%	-13%
UK	-14%	-46%	-61%	-20%	-27%	-20%	-30%	-28%	-3%
US	-16%	-46%	-53%	-17%	-9%	-14%	-20%	-23%	-13%

Sources: Bernstein Research (chart) Internal, Bloomberg, Elara, UBS, FII - Foreign Institutional Investor, DII - Domestic Institutional Investor, FY - Financial Year, CY - Calendar Year, YoY is Year over Year, YTD - Year to date, QoQ - Quarter on quarter EM- Emerging Markets, GST- Goods and service tax, VC- Venture capital, CPI- Consumer price index, GST- Goods and service tax, SD- Standard Deviation, 12MF- 12 month Forward PE



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India at a Glance

	FY17	FY18	FY19	FY20	FY21	FY22	FY23E	FY24E
Economic Activity and Employment								
GDP, USD bn	2295	2651	2701	2871	2668	3174	3553	3903
GDP per capita, USD	1767	2018	2036	2141	1969	2318	2568	2792
Real GDP growth, %	8.3	6.8	6.5	4.0	-6.6	8.7	7.5	6.6
Prices, interest rates and money								
CPI inflation, % y/y (average)	4.5	3.6	3.4	4.8	6.2	5.5	6.6	5.0
Repo rate, % (year-end)	6.25	6.0	6.25	4.4	4.0	4.0	5.5	6.0
10 year bond yield, % (year-end)	6.7	7.4	7.4	6.1	6.2	6.8	8.0	7.5
USDINR (year-end)	64.8	65.0	69.2	75.4	73.5	75.8	78.0	78.0
Fiscal accounts								
General government budget balance, % GDP	-7.0	-5.9	-5.9	-7.8	-13.9	-10.7	-10.2	-9.5
Balance of payments								
Trade balance, USD bn	-112	-160	-180	-158	-102	-192	-244	-237
Exports, USD bn	280	309	337	320	296	422	444	459
Imports, USD bn	393	469	518	478	398	615	688	695
Current account balance, USD bn	-14	-49	-57	-25	24	-50	-98	-88
Foreign direct investment (net), USD bn	35.6	30.3	30.7	43.0	44.0	39.9	45.0	48
Total FX reserves, USD bn	370	425	413	478	577	607	582	578
Total external debt, % GDP	20.5	20.0	20.1	19.5	21.4	20.8	20.5	20.4
Credit ratings								
Moody's	Baa3	Baa2	Baa2	Baa2	Baa3	Baa3	Baa3	Baa3
S&P	BBB-	BBB-	BBB-	BBB-	BBB-	BBB-	BBB-	BBB-
Fitch	BBB-	BBB-	BBB-	BBB-	BBB-	BBB-	BBB-	BBB-

Source: CEIC, Haver, UBS estimates; Note: Data is for FY ending March, E - Estimates

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