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INDIA REWIND

DSP INVESTMENT MANAGERS

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.

September and October are the festive months in India which include the celebrations of Navaratri and Diwali. The festive season sale is a key indicator of domestic economic activity. The estimated festive bonanza sale for Indian companies is USD ~12bn during the period, up ~28% YoY mainly driven by the retail segment including fashion, consumer discretionary and autos. We did an interesting pan-India channel check to gauge demand trends across sectors and companies. The growth is mainly driven by i) strong demand ii) good discounts (in durables) iii) and mainly the first festive season without Covid disruption. An interesting trend which emerges from the dealer/distributor checks is that the demand for premium products remains robust compared to the mass or entry-level products. The strong festive sale is also depicted in the goods and service tax (GST) collection for Oct-22, ~USD 20bn, 2nd highest collection ever, up ~18% YoY. The consumption uptrend is notable at a time the world is staring at a possible recessionary phase (not yet visible in India probably due to the strong domestic market while exports may feel the heat).
Market Performance: In Oct 22/YTD MSCI India USD Index was ~2.5%/-8.1% and MSCI India Small cap Index was ~-0.6%/-12.8%, while MSCI EM's performance was ~-3.2%/-31.2% and MSCI DM ~7.1%/-21.2%. MSCI India USD has outperformed MSCI EM by ~23% and DM by ~13% in YTD22.

MSCI India's valuation remains stretched more on a relative basis than in absolute terms. MSCI India now trades at 1.6SD above its long-term average and a premium of ~3 SD above World and EM, hence warranting caution. MSCI India's 12-month forward PE is now at ~21.6x while on a relative basis P/E premium vs. MSCI Asia Ex-Japan expanded to fresh highs of 92%. The majority of MSCI India stocks (65%) are still trading above pre-covid multiples, although fewer stocks are at peak valuation vs. a year ago.

What's driving India's relative valuation premium? We believe this is a mix of superior GDP growth, strong corporate earnings and domestic portfolio flows. The widening gap in relative valuation is mainly driven by the wide performance divergence seen in CYTD22 with the MSCI EM index USD down ~31%, MSCI DM down ~21% while MSCI India's correction is relatively smaller at ~8%. Additionally, the relative valuations are also driven by the strength in earnings growth for MSCI India (~15% in CY23E) much stronger than MSCI EM (~2% in CY23E). The estimated earnings for CY23E post the recent downward revision of ~4% for MSCI India while MSCI EM witnessed a massive ~24% downgrade for CY23E., MSCI India earnings are expected to grow ~15% in CY23E while MSCI EM expected at ~2% in CY23E. India also remains one of the fastest-growing economies (~7% in FY23E) with GDP growth of ~400-500bps higher than EM and the World.
Over the last 5 years (FY17-22), the profit pool growth for MSCI India has been mainly derived from the EPS expansion (~12.6% CAGR FY17-22), and not "PE re-rating" (TTM PE ~22x in FY17 vs. ~25x in FY22) (*please see chart of the month*), indicating improving fundamentals. However, we believe that the further upside in equities will be driven by earnings growth as PE is already elevated.

Flows: FII outflows CYTD is now ~USD 23bn while domestic inflows (mutual funds and insurance) have remained extremely strong at ~USD 33bn. The monthly systematic flows into mutual funds have remained on an average of ~USD 1.5bn.
Can the domestic flows remain resilient? Indian domestic economy has remained resilient so far with strong economic activity across the country. The continuing up trend in financialization of household savings (52% in FY21 vs 31% in FY12) and the emergence of Equities (including mutual funds) as the preferred instrument of savings (10.2% of total household savings flows in CY21 vs 1.2% in previous 3 years) among domestic investors gives additional comfort of future inflows into the equity markets. This is also one of the stronger reasons for the market resilience and hence remains a key monitorable risk if the flow slows down.

Earnings: We are halfway into the 2QFY23 (quarter ending Sept 22) earnings season, 55% of the MSCI India cap (42 out of 109 stocks) have reported earnings so far. Out of the 42 companies, 31% beat estimates, 33% reported in line with street estimates and 36% missed consensus. The MSCI India's 2QFY23 consensus estimate profit growth of 3% YoY, dragged down by commodities (energy and metal). Ex-commodities, earnings are expected to grow by ~25% YoY, led by financials and autos.

Chart of the Month: MSCI India Index growth mainly driven by EPS expansion during FY17-22

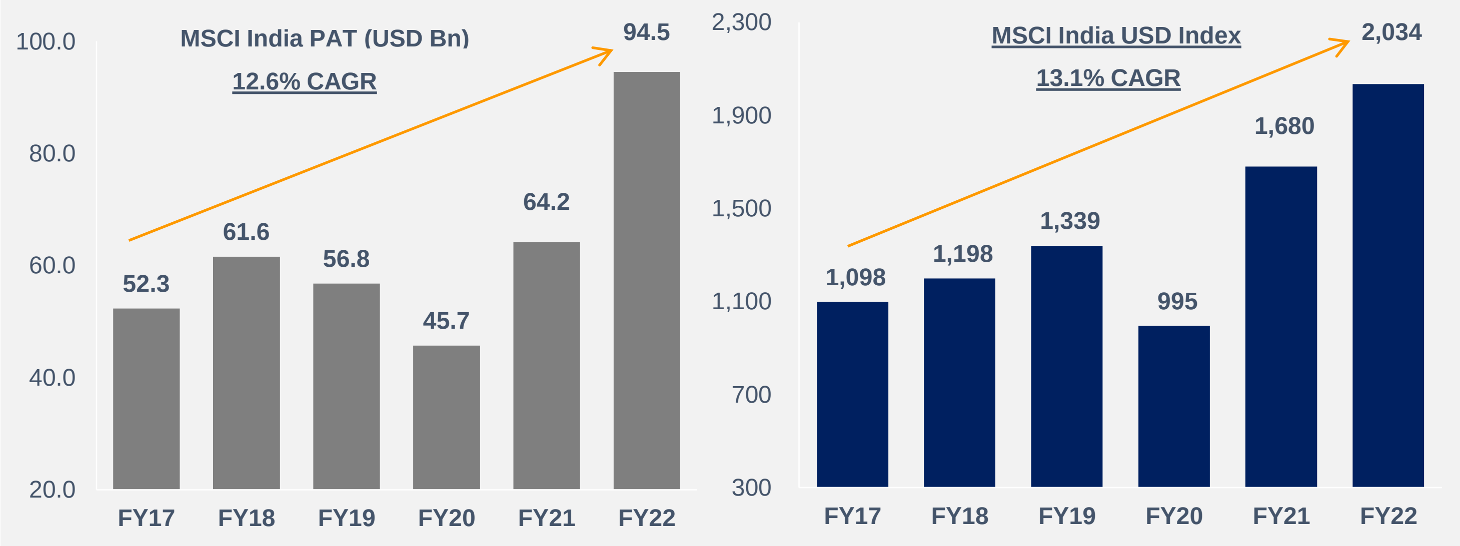

Chart Source: Motilal Oswal Research, Sources: Internal, Bloomberg, UBS Research, Goldman Sachs, FII - Foreign Institutional Investor, DII- Domestic Institutional Investor, FY - Financial Year, CY – Calendar Year; YoY is Year over Year, YTD- Year to date, EM- Emerging Markets, DM- Developed Markets, EPS- Earnings per share,

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For past Issues, please see below:
India Rewind October 2022
India Rewind September 2022
India Rewind August 2022
Older Issues

We hope you found this note interesting and welcome your feedback on InvestmentStrategists@dspim.com

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INVESTMENT MANAGERS

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	3405	3679
GDP per capita, USD	1767	2018	2036	2141	1969	2318	2463	2635
Real GDP growth, %	8.3	6.8	6.5	4.0	-6.6	8.7	7.0	5.7
Prices, interest rates and money								
CPI inflation, % y/y (average)	4.5	3.6	3.4	4.8	6.2	5.5	7.0	5.0
Repo rate, % (year-end)	6.25	6.0	6.25	4.4	4.0	4.0	6.25	6.25
10 year bond yield, % (year-end)	6.7	7.4	7.4	6.1	6.2	6.8	7.7	7.5
USDINR (year-end)	64.8	65.0	69.2	75.4	73.5	75.8	84.0	84.0
Fiscal accounts								
General government budget balance, % GDP	-7.0	-5.9	-5.9	-7.8	-13.9	-10.7	-9.4	-9.0
Balance of payments								
Trade balance, USD bn	-112	-160	-180	-158	-102	-192	-280	-232
Exports, USD bn	280	309	337	320	296	422	450	438
Imports, USD bn	393	469	518	478	398	615	731	670
Current account balance, USD bn	-14	-49	-57	-25	24	-39	-111	-67
Foreign direct investment (net), USD bn	35.6	30.3	30.7	43.0	44.0	39.9	35.6	38.1
Total FX reserves, USD bn	370	425	413	478	577	607	510	515
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