

EQUITY OUTLOOK

May 2024

Inflation poses a common challenge to the Global Economy

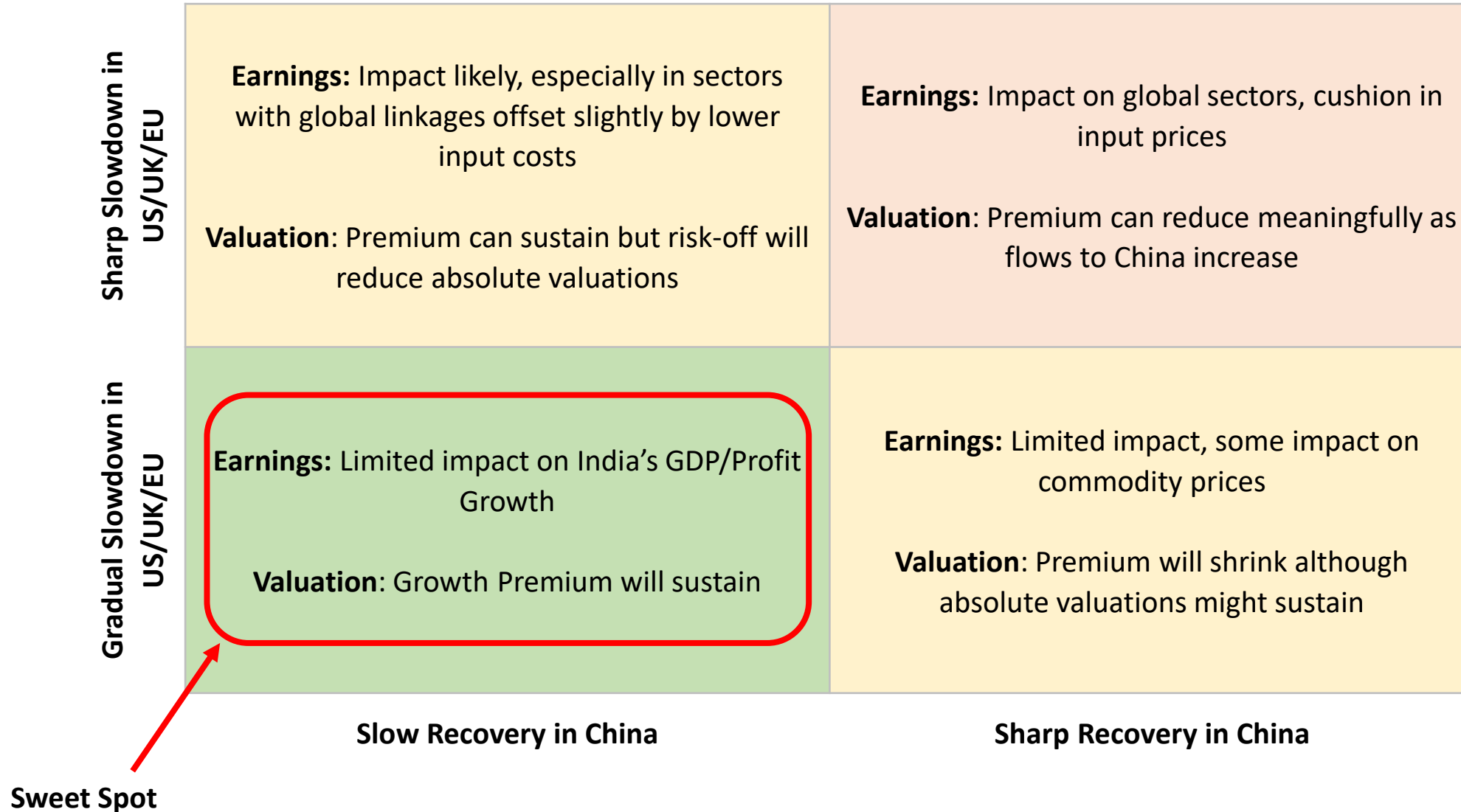
Bringing inflation down without causing too much collateral damage to economy and labour markets

Although inflation has moved down from its peak, its still way above the target

Monetary Policy to tackle inflation

The direction of monetary policy in advanced economies is increasingly unambiguous now:

- Bringing down inflation within target range
- Avoiding a wage-price spiral
- Bringing consistency in inflation expectations



Positive

Fundamentals

Banks, Capital goods,
Manufacturing

Pharma/Healthcare



India has outperformed given the expectation of strong earnings momentum this quarter.



Corporate earnings downgrade risk has reduced.

- Banks and Capital goods lead the positive earning upgrade cycle.
- Urban consumption after significant growth in 2022 is slowing due to impact of inflation and interest rates. In contrast, rural consumption is picking up, albeit gradually. Pharma recovery underway especially in US generics
- Sectors with topline risk (e.g. IT, FMCG) have stabilized; margins to be supported by lower input costs or easing attrition & wage pressure.



The biggest risk to the market of crude prices with the recent escalation in the Middle East. This could threaten India's valuation premium

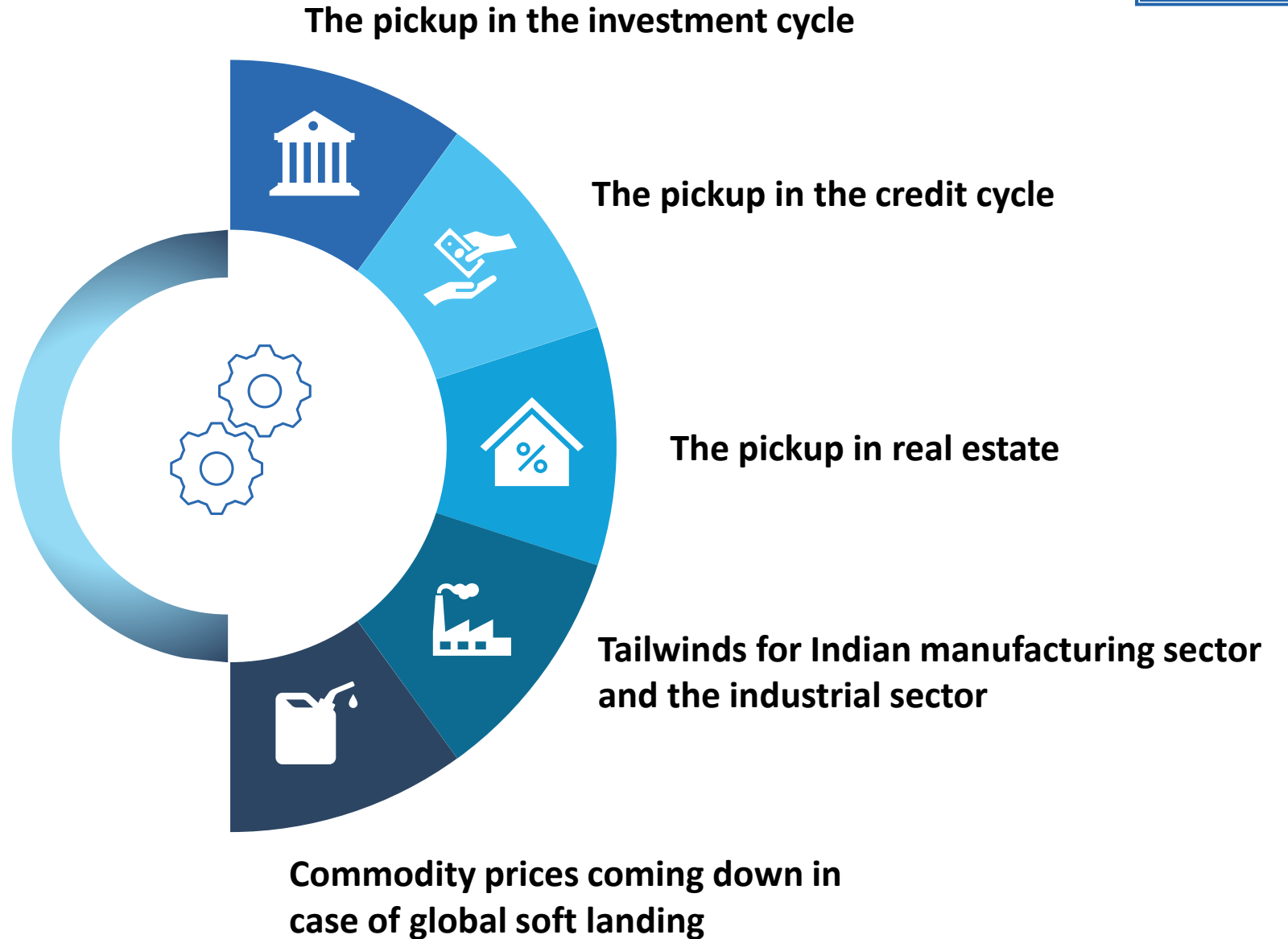
Neutral

IT, Rural
Consumption

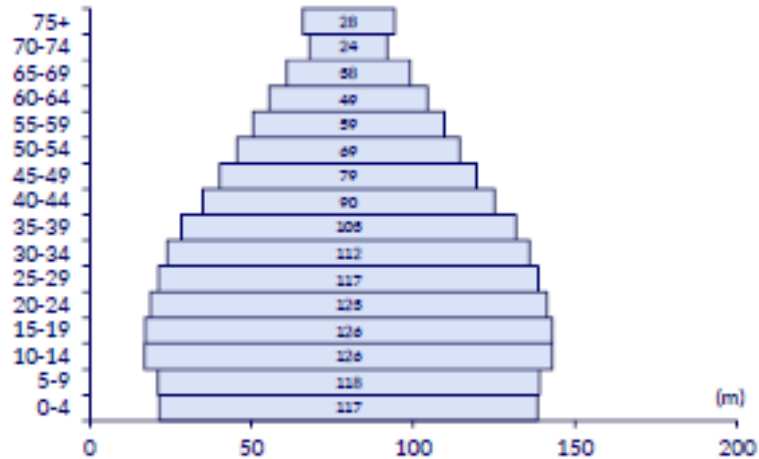
Urban consumption,
Commodities

Negative

The longer term drivers of earnings in India

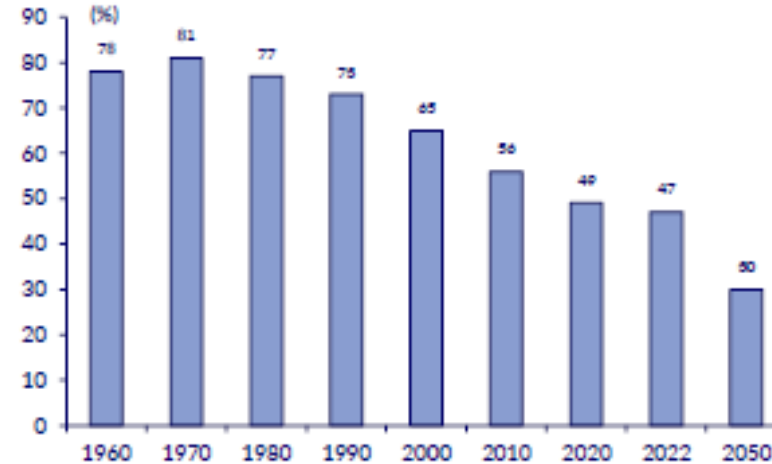


India population pyramid - 2020



Source: UNDP, CLSA

India's dependency ratio



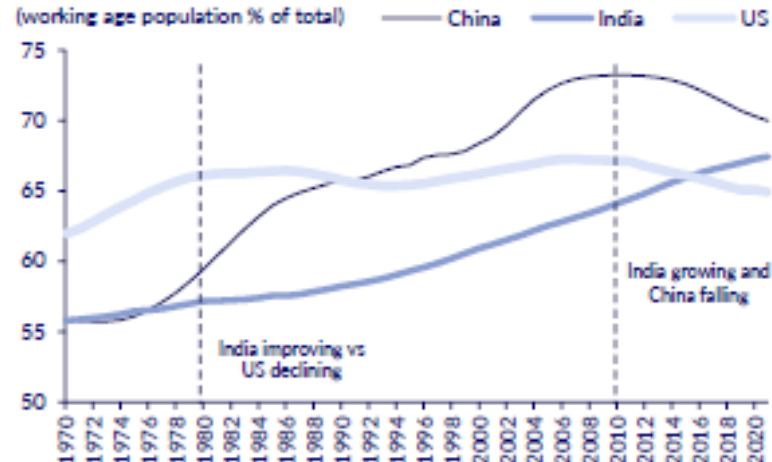
Source: World Bank, CLSA

Working age population projection for India



Source: UNDP, CLSA

India's working age population in comparison to China and the US



Source: UNDP, CLSA

- India's dependency ratio (children and elderly population / total population) has consistently fallen from 73% in 1990 to 47% in 2022. It is expected to further fall to 30% in 2050.
- India's working population has been on a steady increase while US and China are facing a decline.

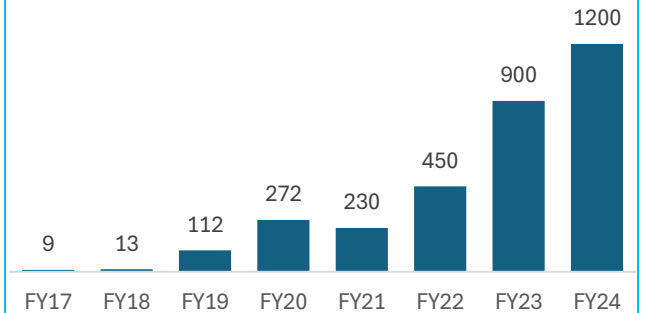
- PLI should attract total capex of ~Rs.4.4tn over next 4-5 years and could fast-track the capex plans of private sector by at least two years

Category	Overall PLI Incentive committed (Rs. Bn)	Committed/ Likely Investment/ Capex (Rs. Bn)	Asset Turnover (x)	Incremental Revenue over 5-year period (Rs. tn)	Employment (Direct + Indirect)	Duration
Mobiles/Electronics	410	110	~25x	10.5	5,00,000	FY22-FY27
Pharma	150	100				
Pharma – API/KSM	69.4	54	~3x	2.9	1,00,000	FY21-FY29
Pharma - Medical Devices	34.2	9				
White Goods & LED	62	79	3-4x	1.7	4,00,000	FY22-FY27
Solar PV	45	175	~4x	3.5	1,50,000	5 years
Telecom	122	30	~20x	2.4	40,000	FY22-FY27
Food	109	61	~4-5x	1.2	2,47,730	FY22-FY27
Automobile & Auto Components and drone	261	425	~4-5x	2.3	7,50,000	FY23-FY28
IT Hardware 2.0	243	48	~20x	3.3	2,25,000	FY21-FY25
Speciality Steel	63	400	~1x	2.0	5,25,000	FY23-FY28
Textile	107	190	~3x	3.0	7,50,000 (2,40,134 Direct Employment)	FY23-FY28*
EV Battery	181	450	~1x	~2.2	-	FY23-FY28
Semiconductor	760	2300	~0.4x	~4.6	1,35,000	FY23-FY27
Specified Electronic Components (Round -2)	21	-	-	-	-	-
Total	2,638	4,451		39.6	38,22,730	

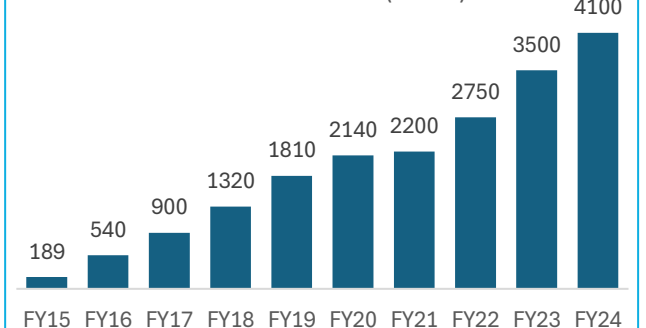
Foreign companies approved under PLI

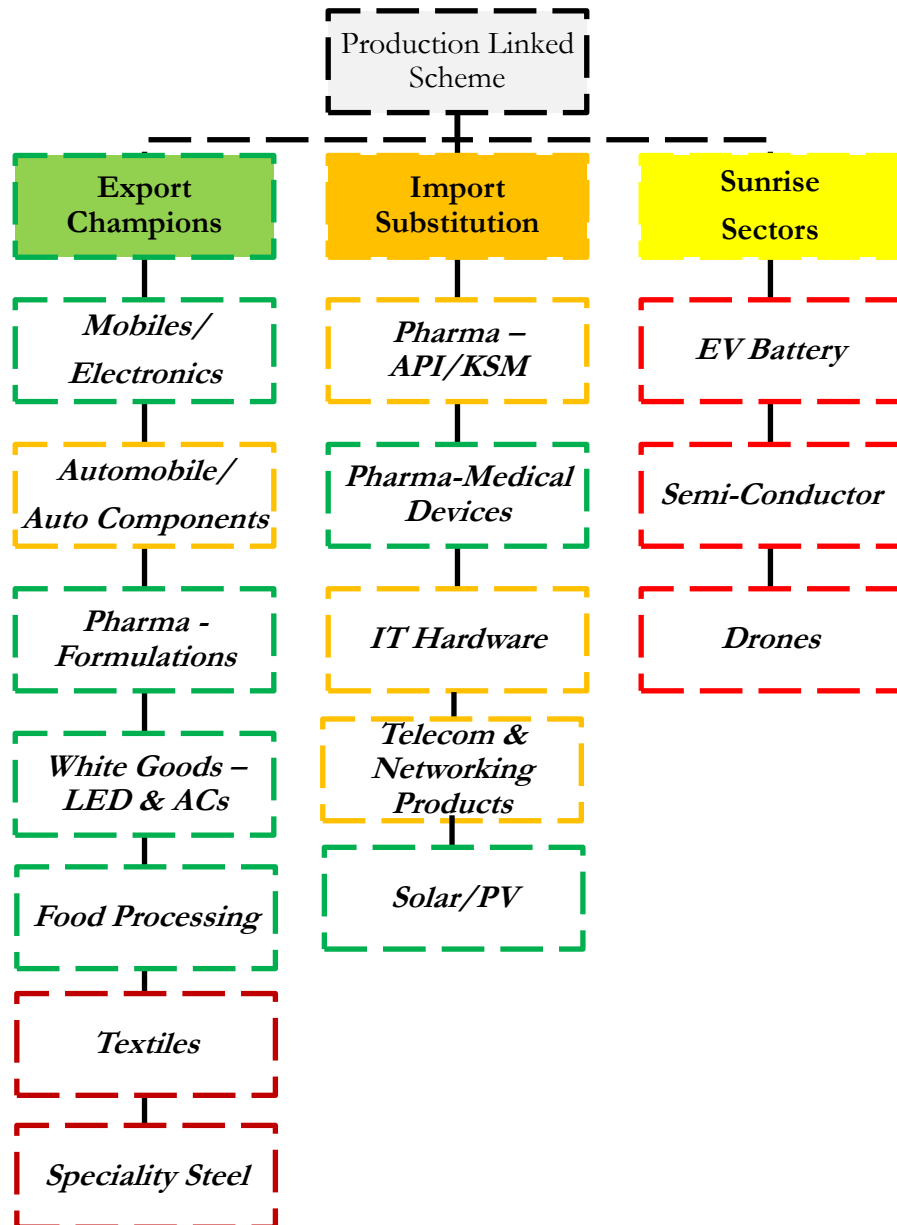
- Electronic and IT:** Wistron, Samsung, Foxconn, Hon Hai, Dell, Pegatron, Rising Star
- Pharma:** Mylan Laboratories Limited, Amneal Pharmaceuticals Private Limited
- Textiles:** Autoliv and Kimberly Clark, Avgol, Evertop Textile & Apparel Complex, Rane TRW Steering Systems, Toray International

Mobile Phone Exports from India (Rs. Bn)



Mobile Production (Rs. Bn)

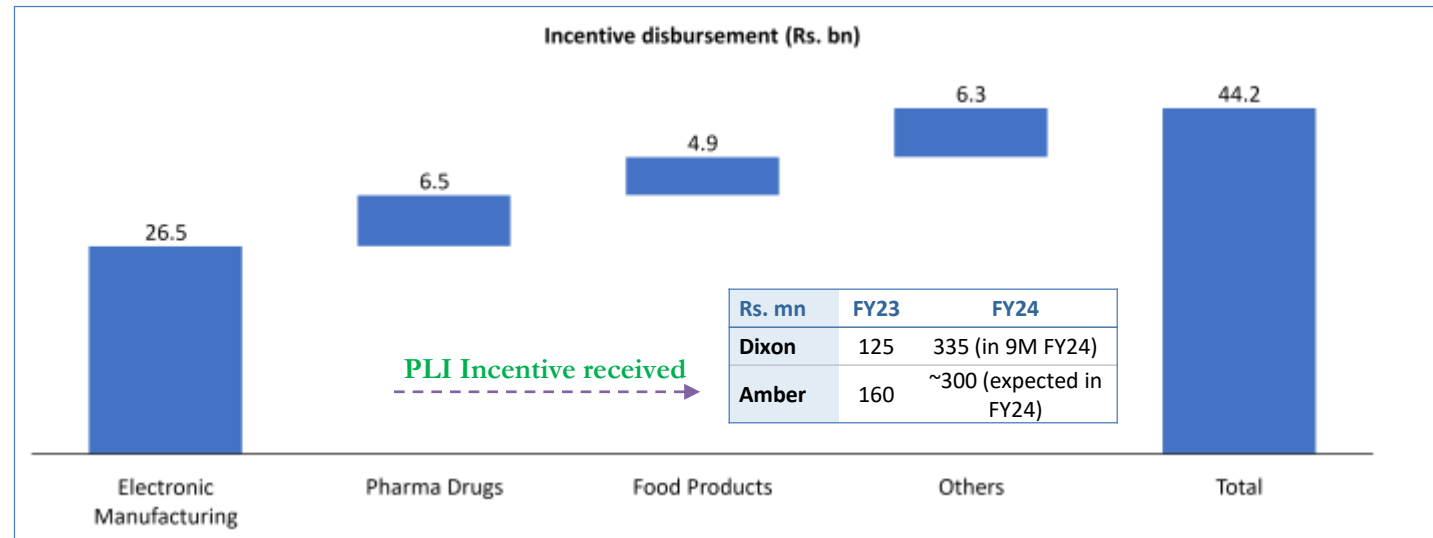




FDI inflows related to PLI sectors

FDI	Sectors (\$, mn)				Growth	
	FY18-FY20	FY21-FY23	9M FY23	9M FY24	FY21-FY23 vs. FY18-FY20	9M FY24
Automobile Industry	7,537	10,533	1275	913	40%	-28%
Drugs and Pharmaceuticals	1,794	4,963	1818	913	177%	-50%
Non-Conventional Energy	4,044	4,898	1662	2144	21%	29%
Chemicals, excl Fertilizers	4,346	3,663	1515	770	-16%	-49%
Electrical Equipments	2,037	3,005	1263	323	48%	-74%
Food Processing Industries	2,438	1,999	1221	3841	-18%	215%
Telecommunications	13,325	1,773	812	837	-87%	3%
Electronics	1,071	1,332	691	1583	24%	129%
Information and Broadcasting	2,714	932	741	1	-66%	-99.9%
Textiles Incl Dyed, Printed	976	701	571	1084	-28%	90%
Mining	459	681	696	271	48%	-61%
Medical and Surgical Appliances	516	674	712	488	31%	-32%

#2: Govt. has disbursed Rs. 44.2bn as incentives so far under the PLI Scheme, out of which Electronic received Rs. 26.5bn



	Phase 1 Downcycle	Phase 2 Cycle Bottom / Early Recovery	Phase 3 Midcycle	Phase 4 Late Cycle	Phase 5 Downcycle	Phase 6 Cycle Bottom / Early Recovery	Phase 7 Mid cycle / Late cycle
	1998-2002	2003 – 2005	2006 – 2008	2009 – 2012	2013 – 2020	2021 – 2023	2024 – 2027
	<ul style="list-style-type: none"> Lower commodity prices NPA cycle was bottoming out; Banking system had excess liquidity Real Estate slowdown; Uncertain global market outlook 	<ul style="list-style-type: none"> Early signs of commodity price increase Electricity Act- Opening-up of power sector Higher Govt. Spend 	<ul style="list-style-type: none"> Strong private participation in power, steel and cement Commodity prices on strong up-move globally, triggering capex Pickup in residential real estate 	<ul style="list-style-type: none"> Excess capacity starts building up post '08-'09 crisis Leveraged private players especially in power and steel sector Demand drops due to global slowdown and domestic policy paralysis 	<ul style="list-style-type: none"> Lower commodity prices Adverse real estate cycle with massive excess inventories Excess supply across sectors Balance sheet repair with gradual consolidation in market share with a few players 	<ul style="list-style-type: none"> Balance sheet strengthens across large companies Large assets under NCLT resolved Falling corporate NPA cycle Residential Realty, Govt spend and favorable global demand PLI incentives system might pre-empt/fast track potential capacity addition 	<ul style="list-style-type: none"> Govt. Capex to flatten out while Pvt. Capex to take the baton PLI incentives to fast-track potential capacity addition Balance sheet to get leveraged across Pvt and Households
Govt Capex CAGR (%)	4%	23%	8%	11%	12%	31.8%	The capex upcycle led by: <ul style="list-style-type: none"> Demand-led Inflation should drive utilization and capex More brownfield capex to follow Import substitution Market share gain led Pvt. Capex Frenzy to add capacity
GFCF CAGR (%)	9.0%	12.5%	21.5%	14.4%	8.5%	24%	
Metal prices CAGR (%)	0%	24%	21%	5%	-4%		
WPI Inflation (%)	4.6%	5.5%	5.5%	8.1%	1.6%	7.9%	
Cost of Debt (%)	10.5%	6.7%	9.3%	9.2%	8.1%	7.3%	
Leverage (D/E)	Deleveraging in 2002	Releveraging	Releveraging	Releveraging	Deleveraging in 2021		
Slippages (%)	6.7%	3.6%	1.8%	2.2%	6.0%		
Corporate Credit growth (%)	12%	23%	24%	22%	3%	5.2%	
Liquidity/Excess SLR (%)	7.8%	16.3%	4.9%	4.7%	7.2%		
Capacity Utilization (%)	~80%	~85%	>90%	~75%	~70%	~72%	
Private sector in Public Infra	Low	Low	High	Very High	Low		
Residential Real Estate	Slowdown ↓	Strong Growth ↑	Moderate Growth ↔	Strong Growth ↑	Slowdown/Consolidation ↓		
Global Outlook	Negative	Positive	Very Positive	Negative	Positive since Oct-20		

Note: Government Capex is the Central & State Government spend CAGR during the specific periods, GFCF – Gross fixed capital formation; Metal price is USD price of Copper and Steel; WPI – Average inflation during that period; Cost of debt is 10 yr AAA corporate bond yield; Capacity Utilization is average utilization of steel, cement and aluminum capacity; Source: RBI, Ministry of Commerce, Avendus Spark Research

Active exposure in Mid & Small Caps to capitalise on investment cycle led economic growth

Actively seeking GARP opportunities (Value with Triggers, Earning Upgrade Cycle) on bottom-up basis; valuation discipline key in high interest rate regime

BALANCED PORTFOLIO STRATEGY TO CAPTURE THE ECONOMIC CYCLE

- ❑ Balanced portfolio strategy to capitalise on the various pockets of strong earnings recovery and outlook
- ❑ Drivers of growth cutting across Investment Cycle, Power, Capital goods and Real estate
 - Recovery in investment cycle led by healthy cash flows in the corporate sector and government's counter-cyclical fiscal policy makes us incrementally positive on the industrial/capital goods sector leading us to progressively increase the exposure to this segment.
 - Recovery in power demand, capex in generation (renewable + thermal) and transmission implies over-weight stance on the associated sectors/stocks.
 - In Financials, after a period of margin expansion and lowering credit costs, growth has normalised. Mid/small caps re-rating has been significant in last 6-12 months, future upside likely to be more bottom-up based on execution as regulatory changes on unsecured lending reduces the growth differential vs. large banks. Large cap banks still reasonably priced despite margin headwinds. Any delay in rate cuts can provide positive surprise to the lowered expectations on net interest margins (NIMs)
 - With an increasing number of companies seeking digital solutions, IT spends have gone up structurally. Global uncertainty over next 6 months however has led us to be on the sidelines even though the sector underweight on IT has come down slightly in portfolios.

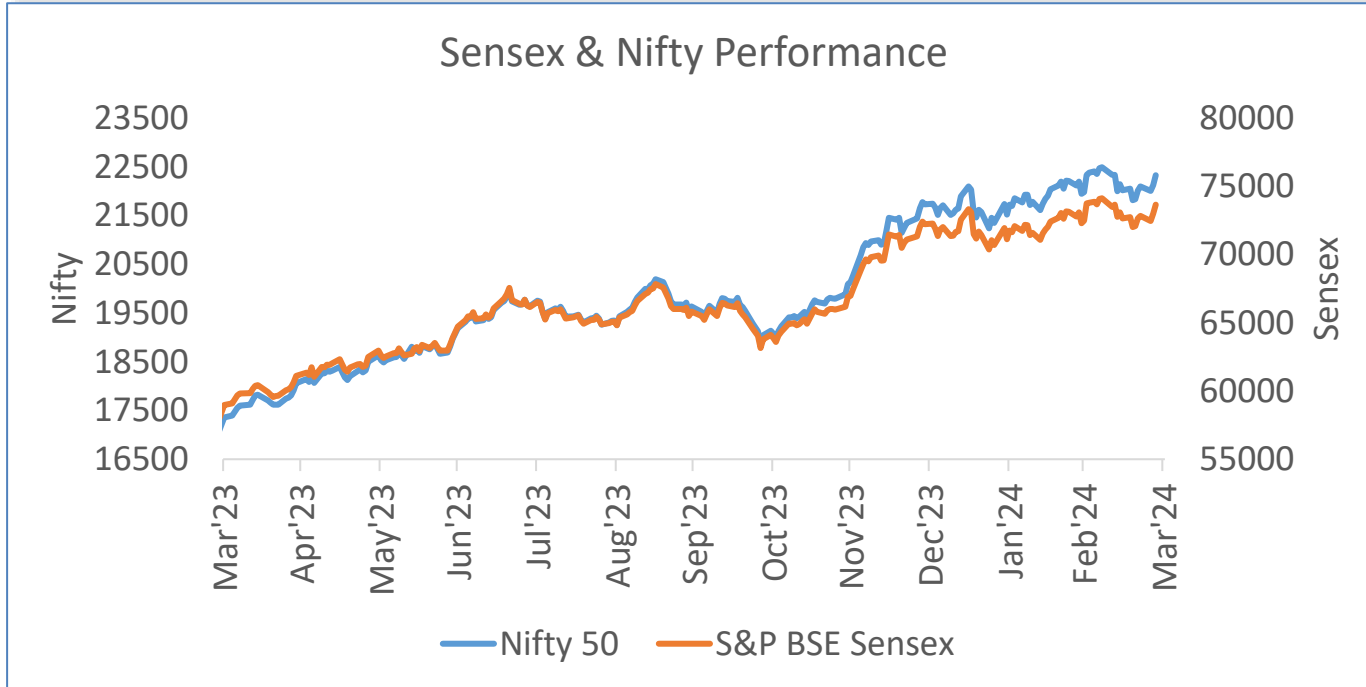
Fiscal Year end	FY 14	FY 15	FY 16	FY 17	FY 18	FY 19	FY 20	FY 21	FY 22	FY 23	Latest*
GDP Growth (%)	6.6	7.2	7.9	7.9	7.3	6.1	4.2	-7.4	4.5	7.2	8.4
CPI Inflation (%)	9.5	5.9	4.9	3.8	3.6	3.4	5.8	5.5	7	5.7	4.85
Current Account (% of GDP)	-1.7	-1.3	-1.1	-0.6	-1.9	-2.4	0.1	-0.2	-1.2	-2	1.2
Fiscal Deficit (% of GDP)	4.5	4.1	3.9	3.5	3.5	3.4	4.6	9.3	6.7	6.4	5.1
Crude Oil (USD/Barrel)	107	53	39	60	58	65	23	59	111	80	88
Currency (USD/INR)	60	63	66	65	65	70	75	73	76	82	83
Forex Reserves (USD bn)	304	342	356	370	424	413	490	579	606	579	638
GST collections (lakh Crs)							1222	1239	1421	1601	2.10

Source : Bloomberg

*GDP data for Q3FY24, Current Account Deficit is as of 31 Dec 23, Fiscal Deficit data is FY24-25(Estimates),Crude oil, Currency, Forex Reserves and GST collections as on 30th April 2024

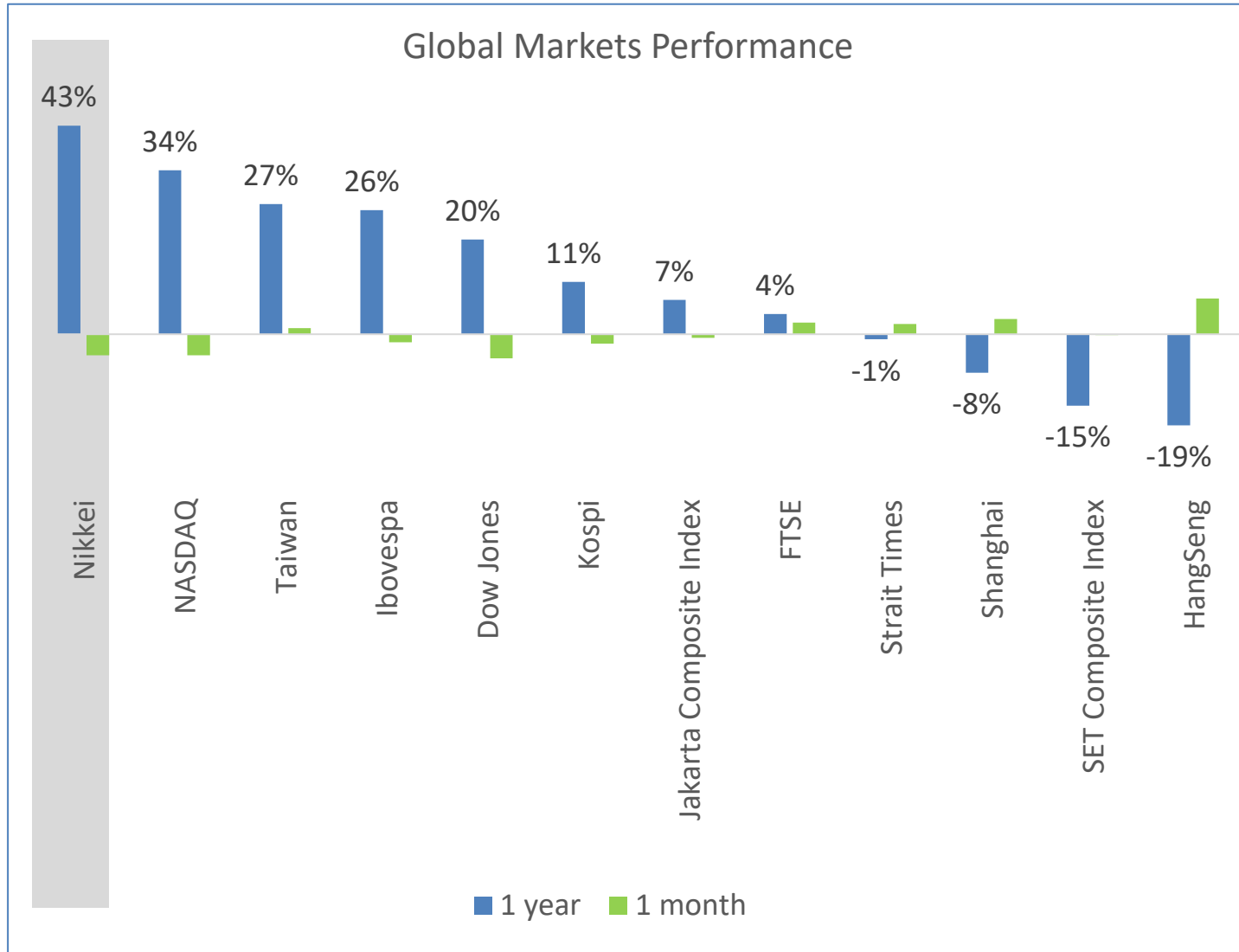
A background image of a financial market performance chart. It features a grid with multiple data series: a candlestick chart in red and blue, and several line graphs in blue, yellow, and red. The chart shows various trends and peaks over time.

MARKET PERFORMANCE

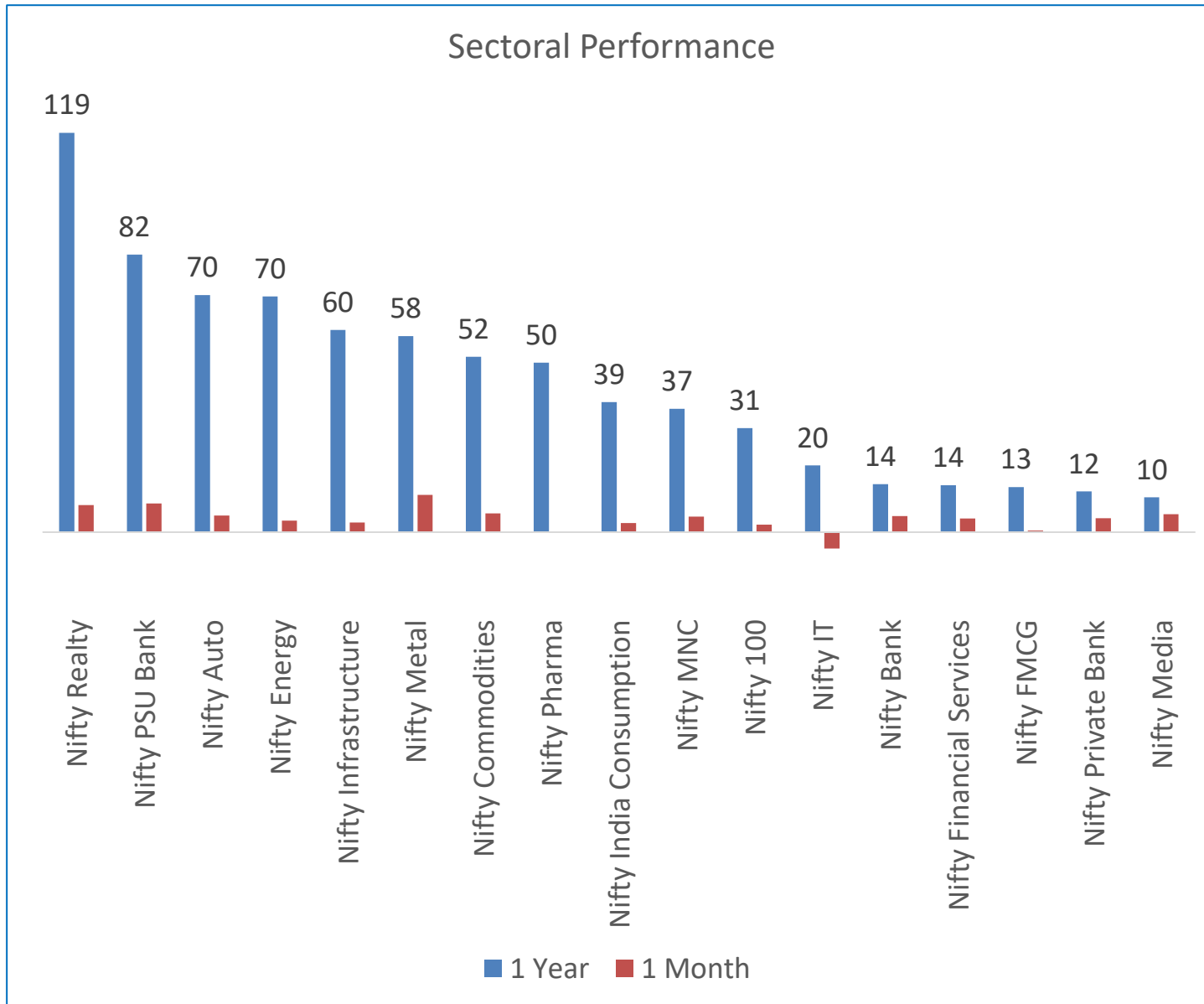


- ❑ NIFTY 50 ended the month 22,604.85 (+1.24%).
- ❑ The index has closed higher for the third straight month.
- ❑ Political continuity and new government agenda (manifesto) provides further support to existing themes

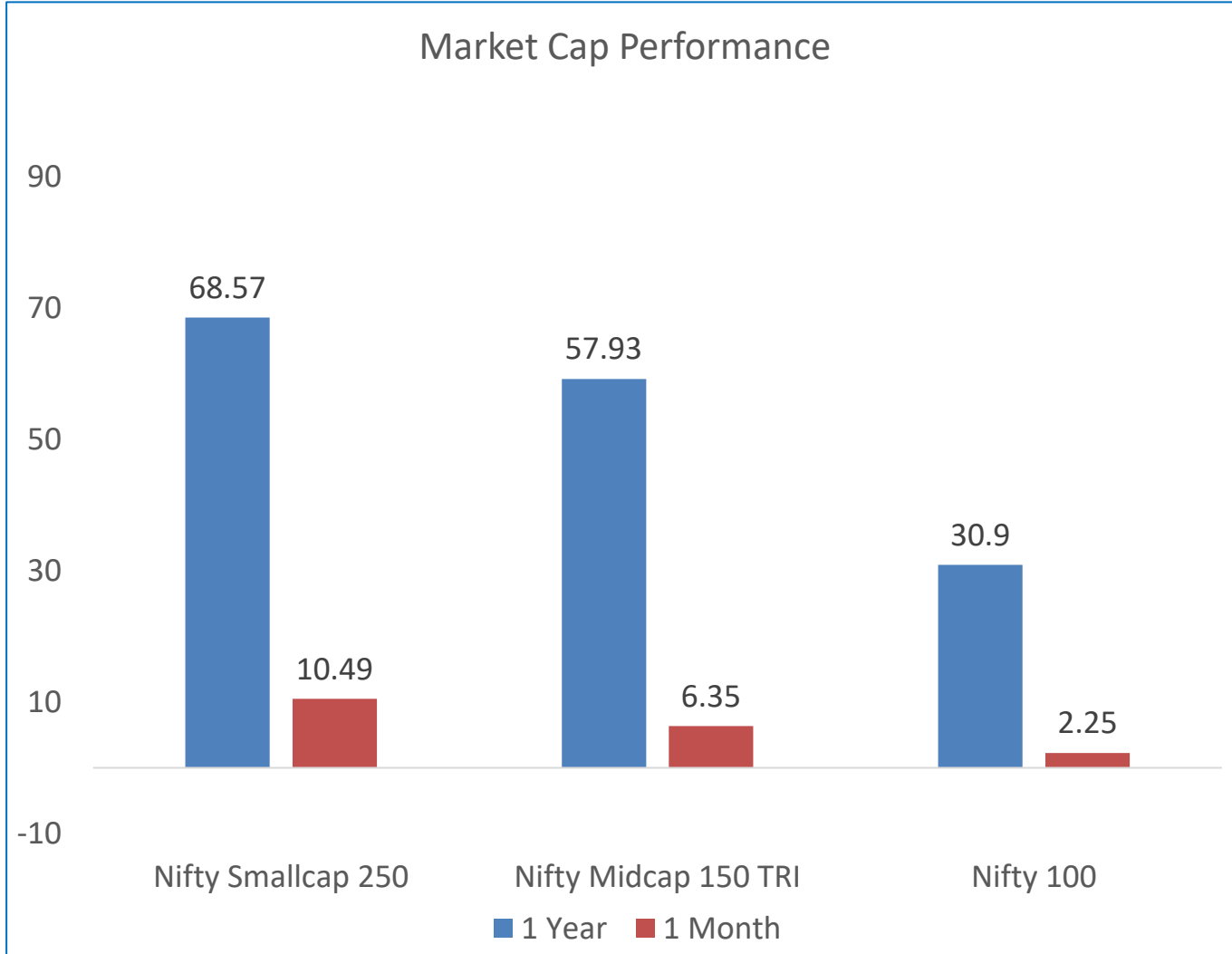
	Nifty 50	Sensex
FY24	28.80%	25.00%
CYTD	4.05%	3.81%
1 Month	1.24%	1.11%



- The market was largely a function of US inflation numbers and April marked the third-straight month of higher-than-expected core CPI inflation.
- Market optimism over a Fed rate cut in the first half of 2024 was dashed and the investor outlook turned decidedly hawkish
- The European market was almost unscathed in relation to its counterparts on this side of the Atlantic. Even though investors in the euro zone and the United Kingdom also had to adjust their expectations of rate cuts, the negative impact on the equity markets was less pronounced.



- On the sectoral front Media, Bank, IT, Financial Services and FMCG underperformed the benchmark index ie BSE Sensex, rest all sectors outperformed specially Auto, Real Estate & Energy.
- For the year ending April 24, Realty (119%) and PSU Bank (82%) made the highest gains while Media (10%) was the lowest performer.

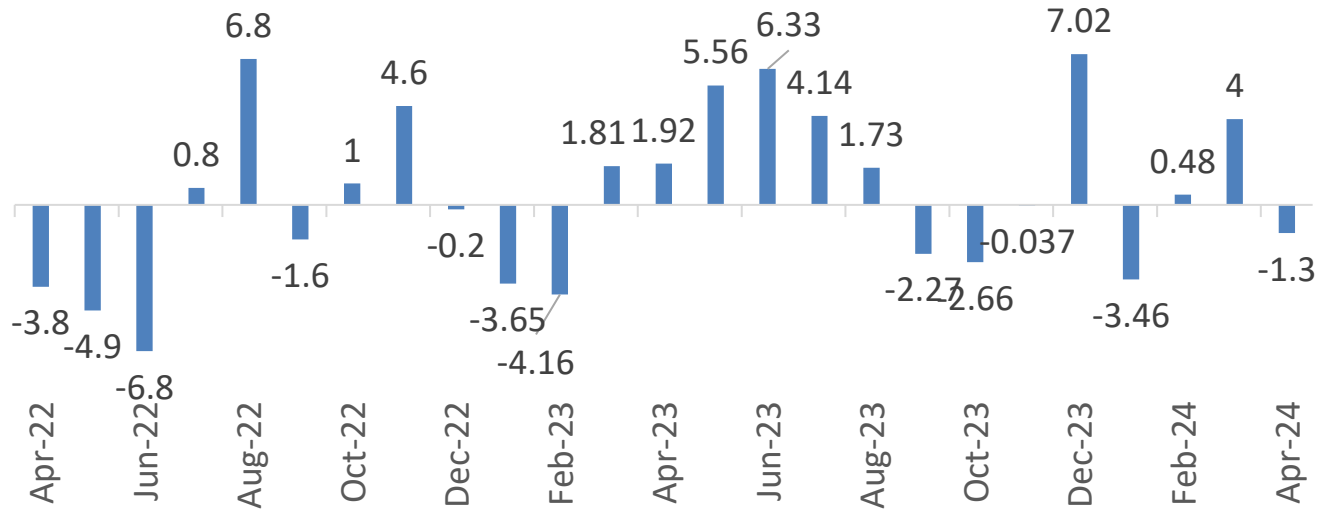


- Mid-cap and small cap index have outperformed the large cap index in both 1 month and in 1 year period.



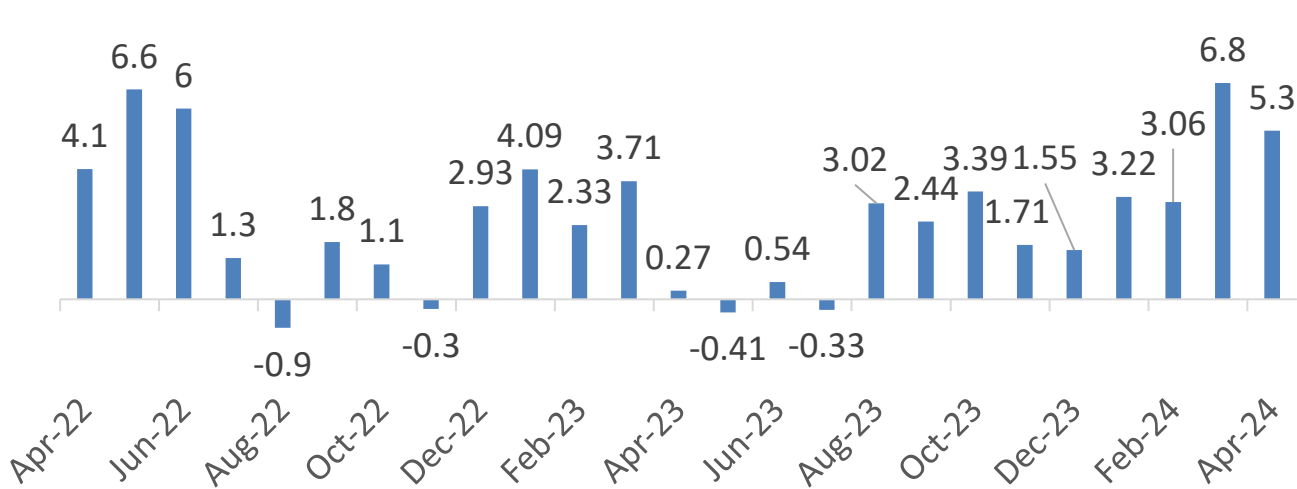
FLAWS

FII Net Equity Flows (\$Bn)



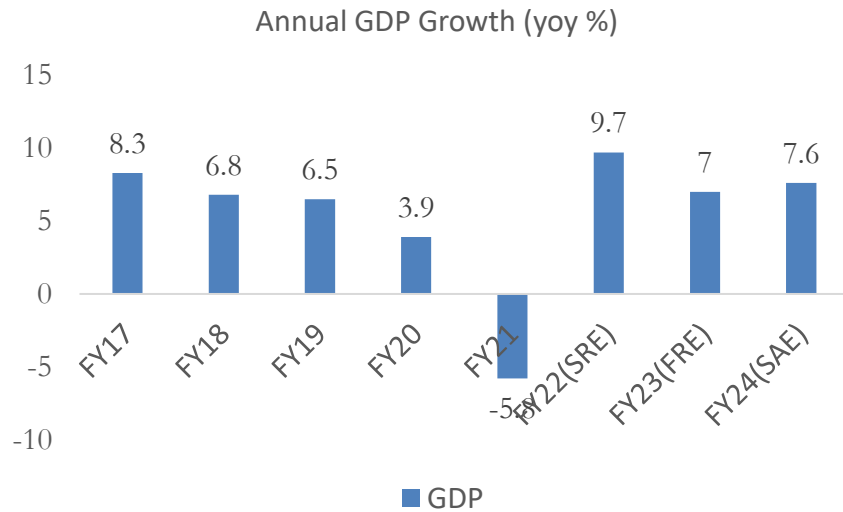
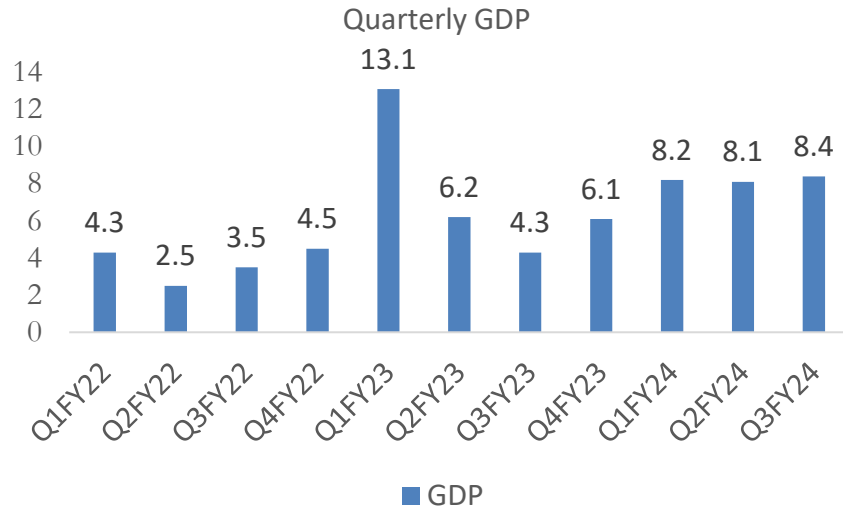
- DIIs continue to be strong buyers for the 9th consecutive month of inflows in April'24 at USD5.3b
- FIIs recorded outflows of USD1.3b in Apr'24

DII Net Equity Flows (\$Bn)

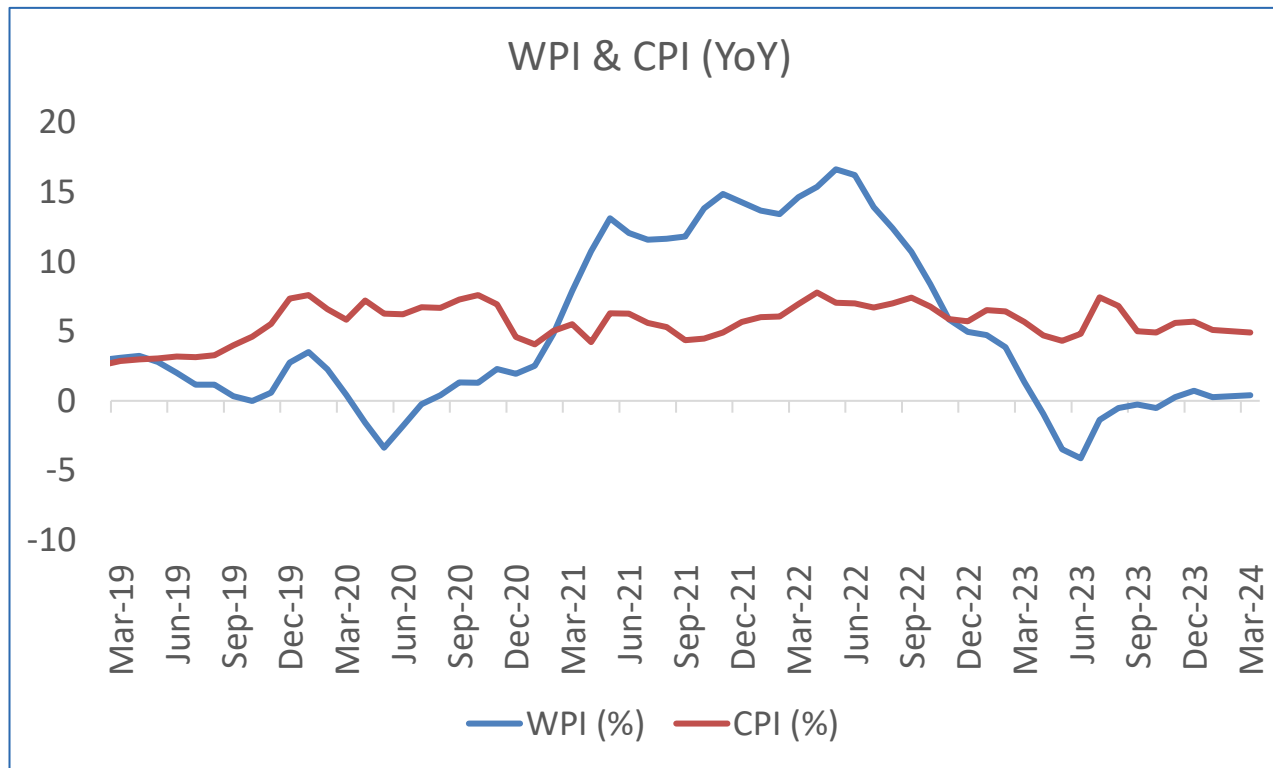




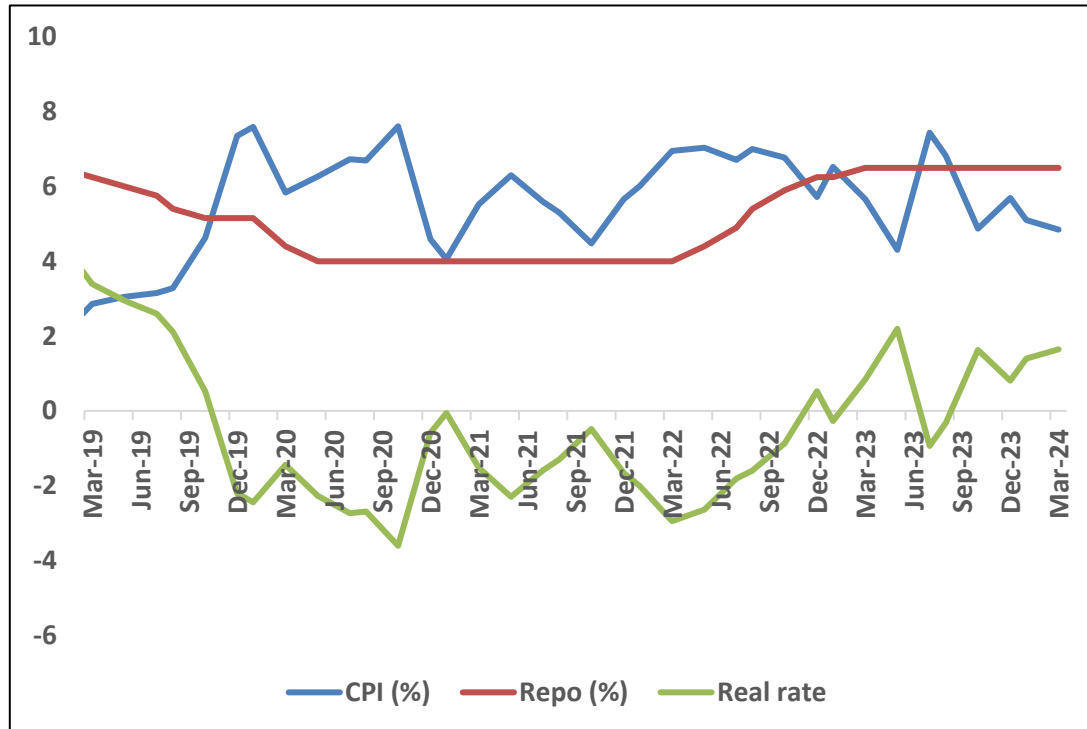
MACRO



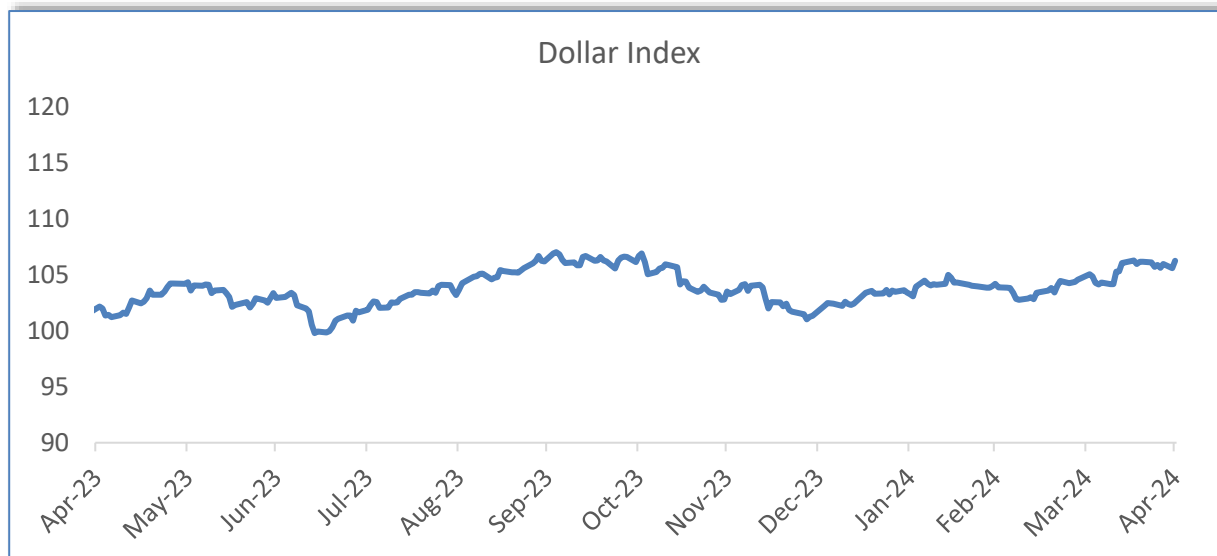
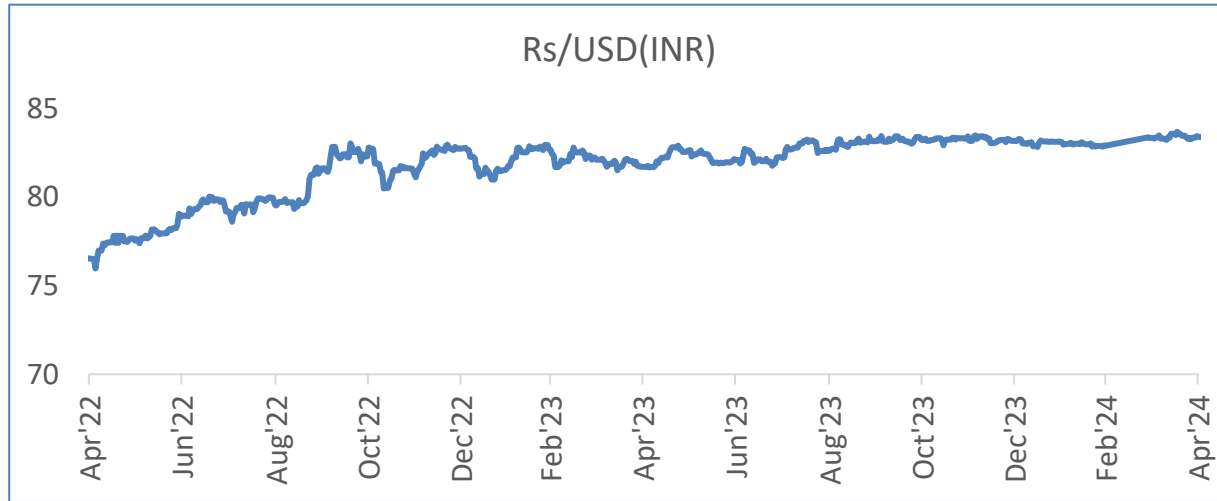
- ❑ The GDP figures, with third-quarter GDP growth at 8.4% and the second advanced estimate (SAE) projecting a full-year growth of 7.6%, have come as a positive surprise exceeding expectations.
- ❑ The stellar full year growth is led by the manufacturing sector and construction sector, while there has been some moderation in the services sector growth.
- ❑ In terms of quarterly growth, the GDP growth of 8.4% in Q3 FY24 marks the highest in six quarters. Although industrial growth experienced a sequential slowdown, it maintained a double-digit growth momentum, expanding by 10.4% YoY in Q3 FY24.



- ❑ The CPI-based inflation for the month of March eased to a five-month low of 4.85 per cent from 5.09 per cent in February
- ❑ Core inflation remained subdued and moderated marginally to 3.3% in March from 3.4% in February, consistently staying below the 4% threshold for four consecutive months.
- ❑ Among non-food and non-fuel categories items such as clothing and footwear, household goods/services, housing, healthcare, education transport and communications witnessed a moderation in inflation which helped in bringing core inflation down
- ❑ The WPI inflation softened marginally to 0.53% in March 2024 from 0.2% in February 2024 bringing the FY24 headline inflation to (-) 0.7% from 9.6% in FY23

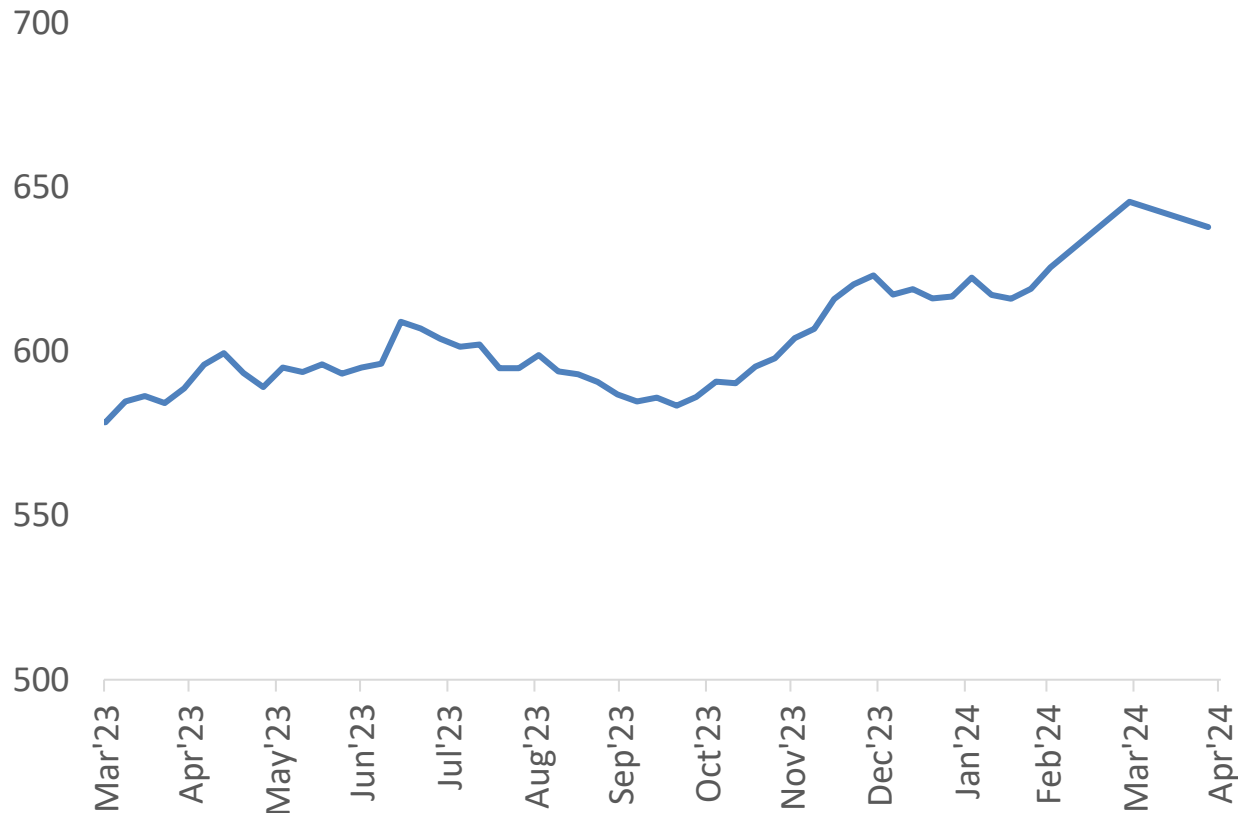


- ❑ In the April MPC RBI maintained a status quo on the repo rate keeping it unchanged at 6.5%. MPC decided with a 5 1 majority to maintain stance as withdrawal of accommodation
- ❑ Inflation is treading down, supported by favorable base effects though stubborn services prices are keeping it elevated relative to targets
- ❑ In its first bi-monthly committee meeting for FY24–25, the Reserve Bank of India (RBI) maintained the real GDP growth forecast for the current fiscal year at 7%
- ❑ CPI inflation for current year is expected to be at 4.5 %



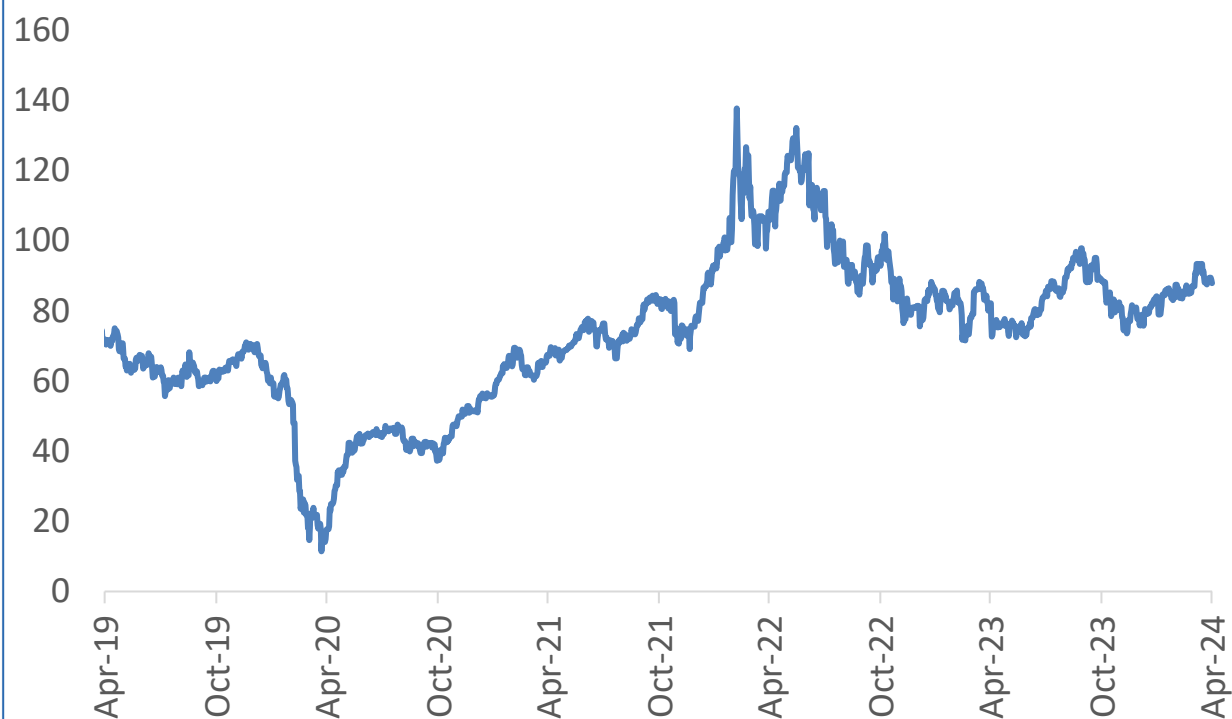
- Most global currencies were under pressure as dollar strength resurfaced led by diminished possibility of a Fed rate cut in Jun'24.
- Even so, the performance of INR was much better relative to other peers, given that India's macro fundamentals remain fairly robust.
- The USD-INR exchange rate fluctuated between 83.23 and 83.68 with an average of 83.41 in April 2024.
- Indian currency the best performing currency due to strong macro economic indicators and RBI two-way intervention in currency markets

Foreign Exchange Reserves (USD Billions)



- Foreign exchange reserves declined to USD 637.9 in April 24 from USD 645 bn in March 24.
- The central bank intervenes in the spot and forwards markets to prevent runaway moves in the rupee.
- Apart from the central bank's intervention, changes in foreign currency assets, expressed in dollar terms, include the effects of appreciation or depreciation of other currencies held in the RBI's reserves.

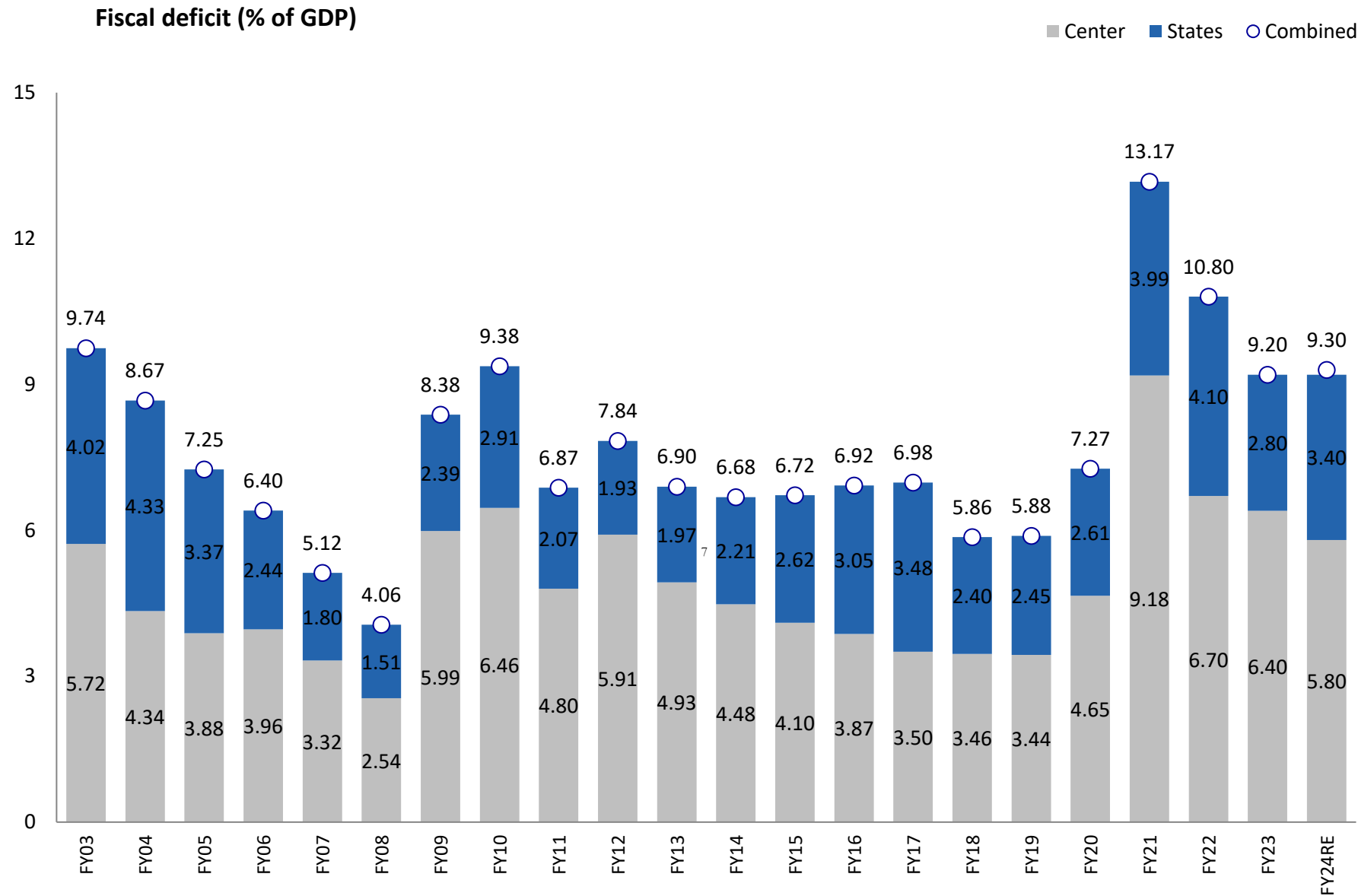
Brent Spot (US\$/barrel)



- ❑ Crude Oil prices ended in red over eased geopolitical tensions and lower demand forecasts.
- ❑ EIA in its short-term energy outlook, cut 2024 world oil demand forecasts, while made room for higher US production.
- ❑ EIA cut forecasts for 2024 world oil demand growth by 480,000 bpd and now sees 0.95 bpd YoY increase. Natural gas prices ended higher on relief rally despite of enough storage.

Country	Rate	Central Bank Rate	CPI YoY	Real Rates
US	Fed funds	5.38%	3.5%	1.9%
UK	Bank Rate	5.25%	3.2%	2.1%
Canada	Overnight	5.00%	2.9%	2.1%
Switzerland	Target Rate	1.50%	1.0%	0.5%
Eurozone	Deposit rate	4.00%	2.4%	1.6%
Japan	Policy rate	0.05%	2.7%	-2.7%
Australia	Cash rate	4.35%	3.5%	0.8%
South Korea	Repo rate	3.50%	3.1%	0.4%
Taiwan	Discount rate	2.00%	2.1%	-0.1%
China	Loan Prime rate	3.45%	0.1%	3.4%
India	Repo rate	6.50%	4.9%	1.7%
Russia	Key Policy rate	16.00%	7.7%	8.3%

- ❑ The Fed in its May 01 2024 Federal Open Market Committee (FOMC) meeting, agreed to keep the target range of its Fed Funds Target Rate (FFTR) unchanged at 5.25%-5.50%.
- ❑ This was the sixth consecutive pause after having raised rates for ten meetings in a row before taking a first pause in June followed by another 25-bps hike in July 2023.
- ❑ The European Central Bank and Bank of England also kept their deposit rates unchanged.
- ❑ Rate cuts not expected in India during calendar year. However, the increased demand may drive up the rates.

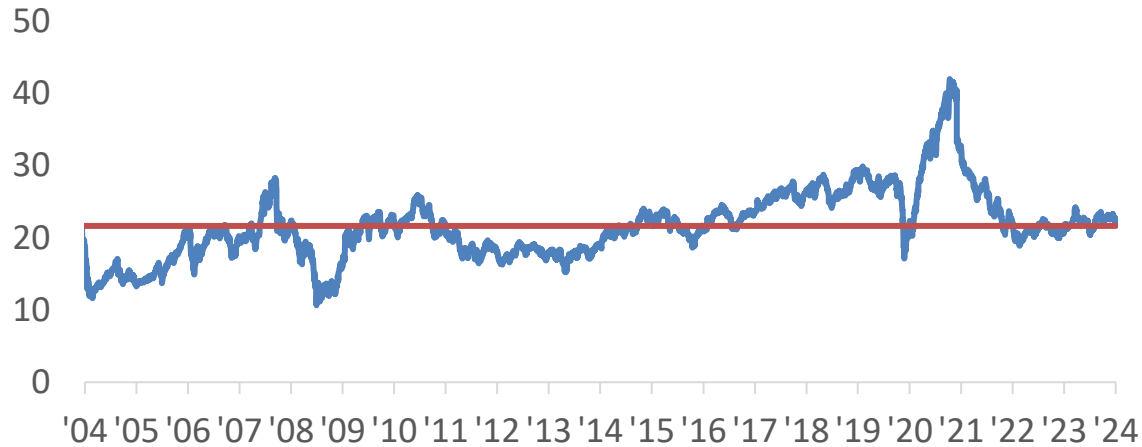


- ❑ The revised estimate or the budget deficit for FY23 was at 5.8% of GDP adjusted downwards from a budgeted estimate of 5.9% .
- ❑ The government reiterated its stated objective of bringing down the Fiscal Deficit to 4.5% of GDP by FY26.
- ❑ This budget takes a step in that direction with the proposed reduction of 70bps down to 5.1% of GDP for FY25.

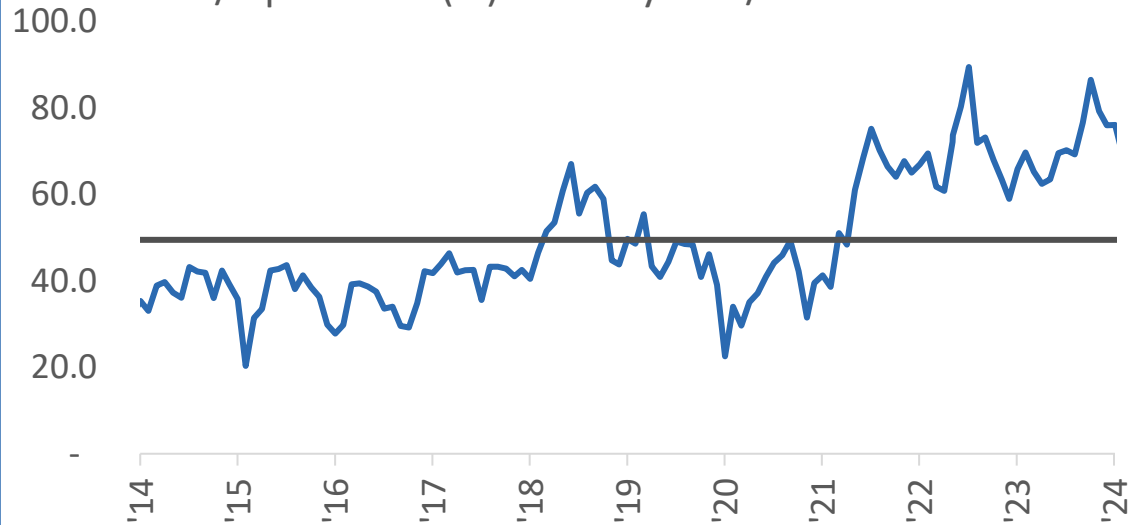
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VALUATION

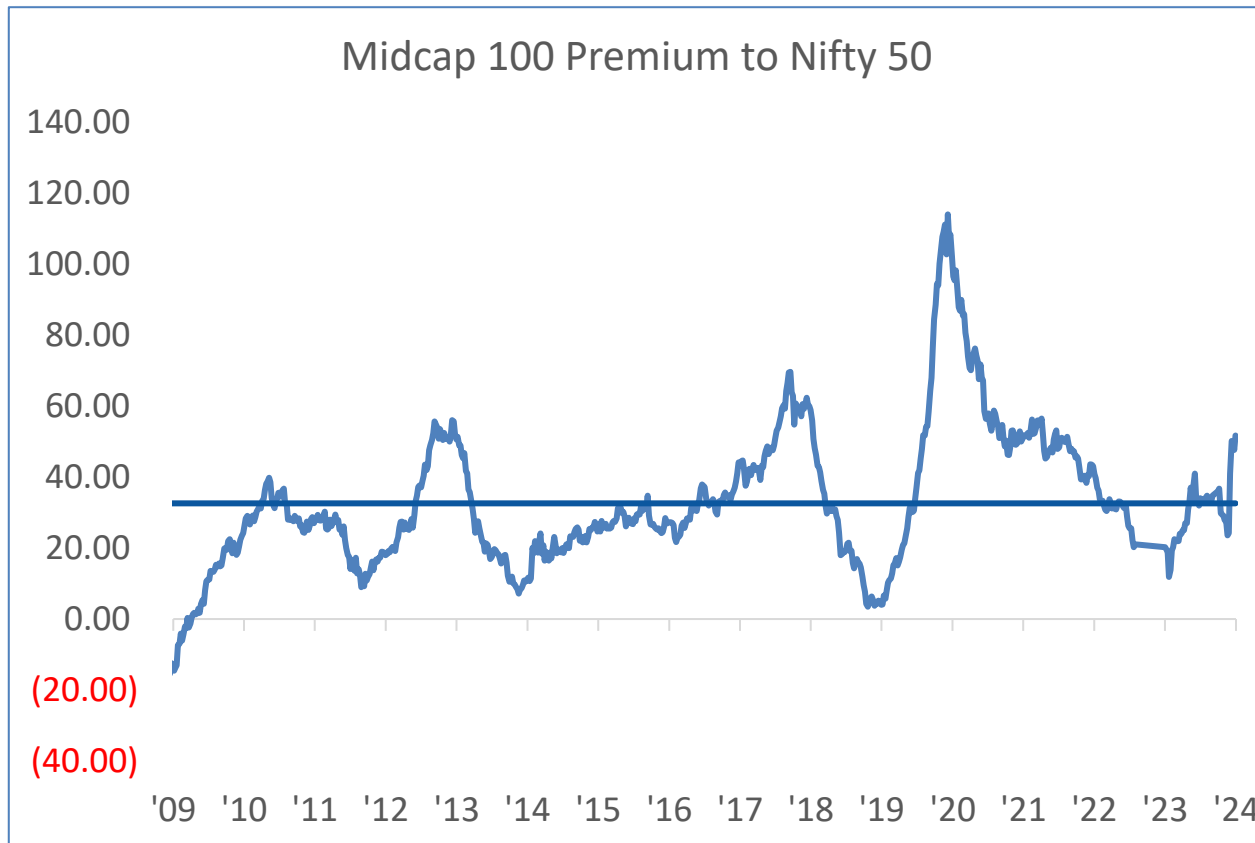
Nifty Trailing PE



P/E premium (%) for Nifty 50 v/s MSCI EM



- ❑ 1-year forward PE stands at 20x, higher than the historical average.
- ❑ Expected earnings growth for FY25 is at 16%
- ❑ In P/E terms, the Nifty 50 is trading at ~70% premium to the MSCIEM index, above its historical average of ~49%.
- ❑ Stable macros, broad based earnings growth and robust banking/corporate sector health driving the premium. Risk from the ongoing general elections appear relatively low
- ❑ Crude price remains a key risk especially post the recent escalation in the Middle East conflict



- ❑ The headline valuations for Nifty Midcap 100 has increased to ~52% premium.
- ❑ Risk reward in large caps is more favorable now
- ❑ Broad-based economic recovery (investment cycle revival) would imply more investment opportunities in mid and small caps in the long term.

THANK YOU

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