JM FINANCIAL

Strategy

Taking pulse of the economy, stock market and flows

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India's economic challenges may have troughed, and trends in some key parameters suggest that the outlook is improving: (1) GDP grew by 6.2% in 3QFY25, picking up from the 5.6% low of 2QFY25; (2) Food inflation and Brent crude prices have come off sharply. We expect RBI to continue its policy easing measures with another 25bps cut in repo rates in its Apr'25 meet; (3) Central government capex growth picked up in Dec'25 and Jan'25, and the outlook for FY26E is decent; and (4) Above-average reservoir levels, increasing rural wages, lower tax rates and an improving job market are positives for the urban and rural economies. Interestingly, FIIs might have sensed this and have bought Indian equities worth USD 3.8bn since 20th Mar'25. We prefer large caps where 1-year forward P/E of 18.6x is not that far from the 25-year average of 17.2x. Midcaps and small caps are still not cheap, trading higher than +1SD. A key near-term worry is Trump's likely announcements on 2nd Apr'25, which, if too harsh on India, can cause another round of correction in the India market.

- **What drove the market correction?** The market correction was driven by the confluence of three factors: (1) Weak Indian economic data in 2QFY25, (2) Weak corporate earnings in 2Q and 3QFY25, and (3) FIIs finding more palatable valuations in China and attractive opportunities in the US. This drove FII outflows to the tune of USD 25.6bn over Oct'24 to Feb'25. DII inflows of USD 39.5bn counterbalanced these outflows, in the absence of which the market correction could have been sharper.

- **India's economic challenges have troughed and FIIs may have sensed this:** India's economic challenges might have troughed and trends in some key metrics indicate that the outlook is improving: (1) GDP grew at 6.2% in 3QFY25, picking up from the 5.6% lows of 2QFY25; (2) Food inflation has come off sharply over the last few months to 3.8% in Feb'25. Brent crude has also corrected from the peak of USD 91/bbl in Apr'24 to USD 73/bbl currently. RBI is likely to continue its policy easing measures with another 25bps cut in repo rates in its Apr'25 meet; (3) Central government capex growth also picked up in Dec'25 and Jan'25, and the outlook for FY26E is decent; (4) Above-average reservoir levels, increasing rural wages, lower tax rates and an improving job market are big positives for the urban and rural economies. Interestingly, FIIs may have sensed this and have bought Indian equities worth USD 3.8bn since 20th Mar'25.

- **Large cap valuations almost mean reverted; mid & small caps still not cheap:** Since Sep'24, the Nifty50 has corrected ~11% from its top and valuations have come off from the peak of 23.0x to 18.6x 1-year forward (closer to the 25-year mean of 17.2x). We believe that the mean reversion story has broadly panned out, leaving limited room for a downside hereon. Bank Nifty valuations appear extremely attractive at <15-year mean. The margin of safety in the mid and small caps is limited, given valuations are higher than +1SD with limited room for earnings disappointment.

Exhibit 1. JM Financial top picks

11 Large Caps		4 Mid-Caps	9 Small Caps	
RIL	Varun Beverages	JSPL	Metro Brands	Paradeep Phosphates
Hindalco	TCS	JSW Energy	Aster DM	HG Infra
Bharti Airtel	Shriram Finance	Dixon	Nuvama Wealth	
Sun Pharma	TVS	BHEL	Ahluwalia Contracts	
Axis Bank			JK Cement	
UltraTech			KPIT	
DLF			Lemon Tree	

Source: JM Financial

What drove the recent market correction?

The market correction, in our opinion, was driven by: (1) Weak Indian economic data in 2QFY25 (2) Weak corporate earnings in 2Q and 3QFY25, and (3) FIIs finding more palatable valuations in China and attractive opportunities in the US.

Exhibit 2. India market valuations and index movements

Key Index	Correction v/s 52 week high	53 week low v/s 52 week high	Move up from recent bottom	1-yr forward P/E (x)	Mean 1-yr forward P/E (x)	Current P/E vs. long term mean	+1SD 1-yr forward P/E (x)
Nifty50	-10.2%	-16.4%	7.4%	18.6	17.2	+8.1%	19.4
Nifty Midcap 100	-14.9%	-23.1%	10.6%	28.0	19.3	+45.4%	25.3
Nifty Smallcap 100	-18.2%	-27.5%	12.7%	20.7	14.9	+38.9%	19.1
Bank Nifty	-5.3%	-12.4%	8.1%	11.8	14.2	-16.9%	17.7
Nifty IT	-18.5%	-22.6%	5.3%	23.9	19.7	+21.3%	24.3
BSE Auto	-22.8%	-27.5%	6.5%	20.3	16.9	+20.1%	22.2
BSE Capital Goods	-17.6%	-28.5%	15.1%	32.2	23.1	+39.4%	29.5
Nifty FMCG	-19.8%	-24.4%	6.1%	36.2	31.0	+16.8%	35.6
Nifty Energy	-25.2%	-34.9%	14.9%	13.8	11.5	+20.0%	13.1
Nifty Pharma	-11.0%	-17.9%	8.4%	26.9	22.5	+19.6%	25.7

Source: Bloomberg, BSE, NSE, JM Financial

Weak economic data points

- YoY GDP growth moderated to 5.4% in 2QFY25, lower than market expectations of 6.5%. Inflationary pressures in the economy remained high (>5% vs. RBI's target of 4%) - mainly fuelled by vegetable prices. RBI continued to prioritise price stability over growth, and hence kept the policy rate at restrictive levels (6.5%).

Weak corporate earnings

- In 2QFY25, the analysis of 227 companies out of the 275-stock JMFL coverage universe suggested that 45% missed estimates. This trend continued in 3Q; out of the JMFL coverage universe, 41% companies missed estimates. Further splitting 3QFY25 performance in terms of market capitalisation, 50% of small-cap companies missed forecasts, while misses were lower in midcaps (34%) and large caps (28%).
- Management commentary suggested that there was a slowdown in urban demand across FMCG, retail, auto and mall operators. Besides this, chemicals, consumer durables and building materials also witnessed a moderation in demand. MFIs, select private sector banks and NBFCs witnessed stress in their unsecured book.

FIIs found better opportunities in China and US

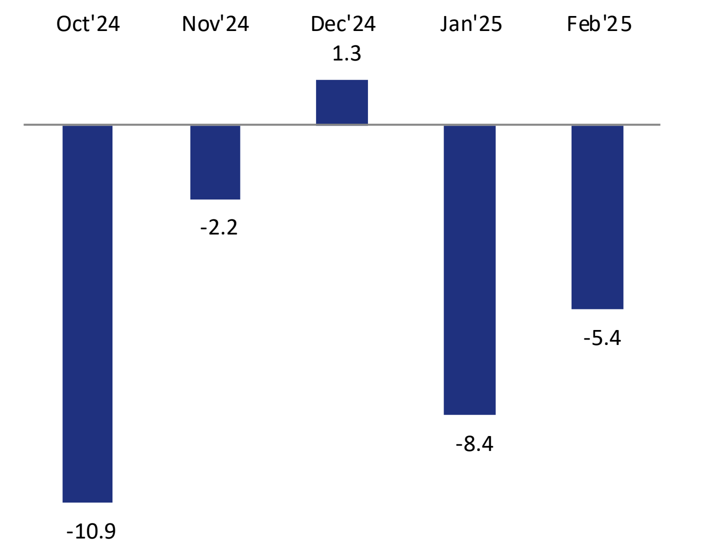
- It all started with the "Sell India, Buy China" trade post the Chinese government announcing stimulus measures for the economy in Sep'24. FIIs preferred moving to China, which was trading at less than half the valuations of India. India's 1-year forward P/E through Jul'24 to Sep'24 was > 1 standard deviation above mean. Consequently, China saw FII inflows of USD 96bn in Sep'24.
- In the 2024 US presidential elections, Trump and the Republicans gained control over all the three branches of the US government. Trump also won the popular vote, something he was unable to do in 2016. We believe Trump's plans for lower corporate taxes, higher import tariffs, and deportation of illegal immigrants will result in growth in the US economy, higher inflation, higher interest rates and a stronger US dollar. This tempted FIIs to take at least some portion of their money back to the US.

USD 25.6bn of net selling by FIIs over Oct'24 to Feb'25

- Our analysis suggests that significant FII outflows have historically led to sharp corrections in the Indian markets. In most instances wherein the Nifty 50 has declined > 5% in a month, FII flows have been negative. Over the period Oct'24-Feb'25 FIIs offloaded Indian equities to the tune of USD 25.6bn.

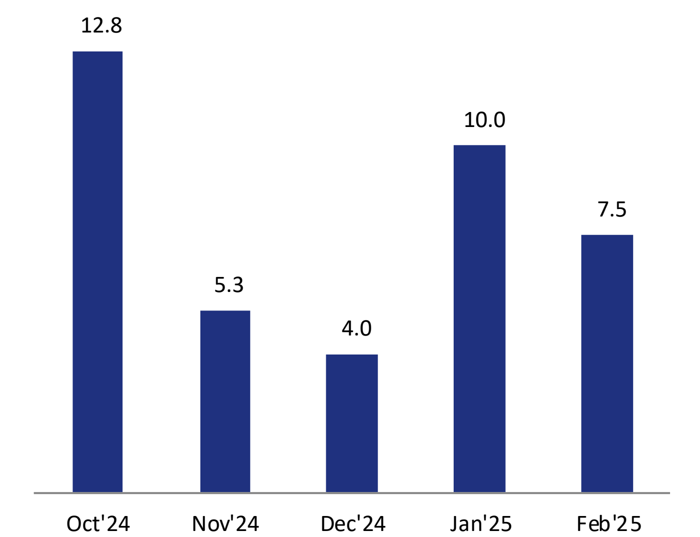
- While part of this was counterbalanced by DII inflows of USD 39.5bn, a correction in the Indian equity market was inevitable. We believe that, if not for increased DII participation, the quantum of correction could have been larger.
- Sectors that saw the highest FII outflows over this period include: (1) BFSI – USD 6.1bn, (2) Oil and Gas - USD 5.9bn, (3) Auto and auto components - USD 3.8 bn, and (4) FMCG – USD 3.3bn, while the sectors that witnessed inflows included (1) IT - USD 719mn, (2) Realty - USD 389mn, and (3) Chemicals - USD 234mn.

Exhibit 3. FIIs net sellers for USD 25.6bn over Oct'24 to Feb'25



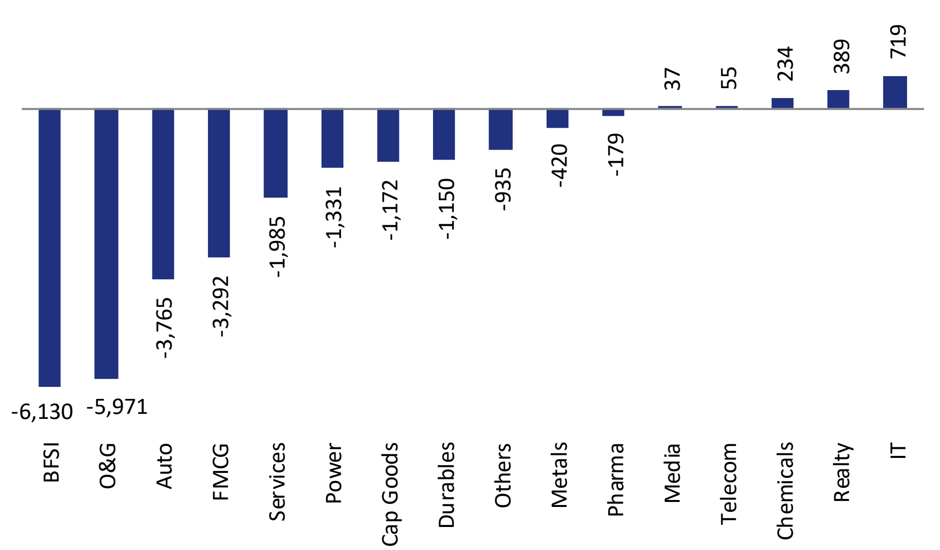
Source: NSDL, JM Financial

Exhibit 4. DIIs net buyers for USD 39.5bn over Oct'24 to Feb'25



Source: NSDL, JM Financial

Exhibit 5. India sectoral FII flows Oct'24 to Feb'25 (USD mn)



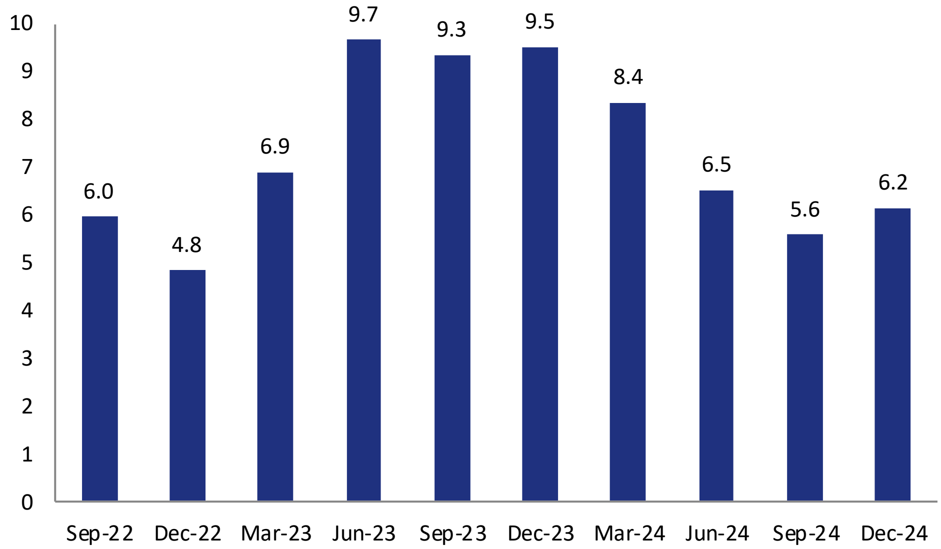
Source: NSDL, JM Financial

Why do we foresee a recovery in the Indian economy?

GDP growth picking up from the lows of 2QFY25

GDP grew by 6.2% in 3QFY25, bouncing back from the sluggish 5.6% in 2QFY25. Even if we assume a conservative 6.2-6.3% growth (vs. the RBI target of 6.5%) for FY25E, 4QFY25 GDP growth at 6.5% would be higher than that in 3QFY25. We also expect GDP growth at 6.5% in FY26E.

Exhibit 6. Real GDP growth (YoY, %)

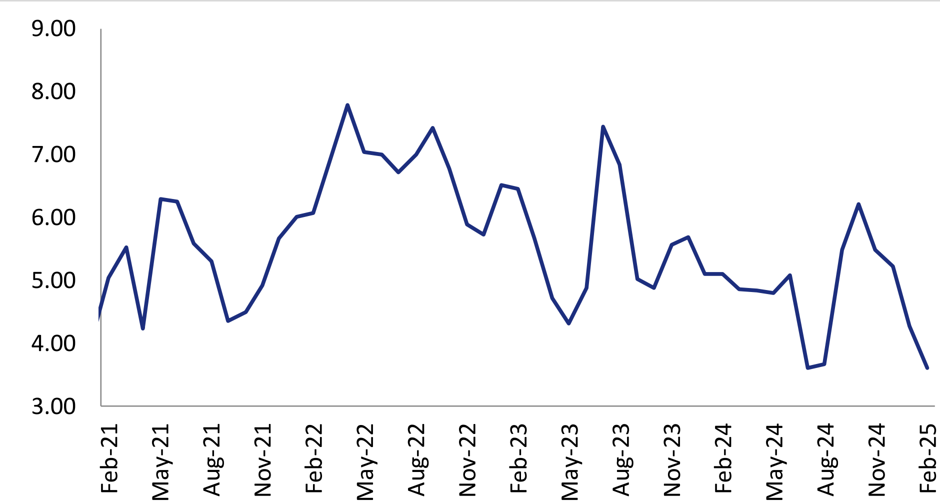


Source: MOSPL, JM Financial

Rate cut cycle has begun in India already

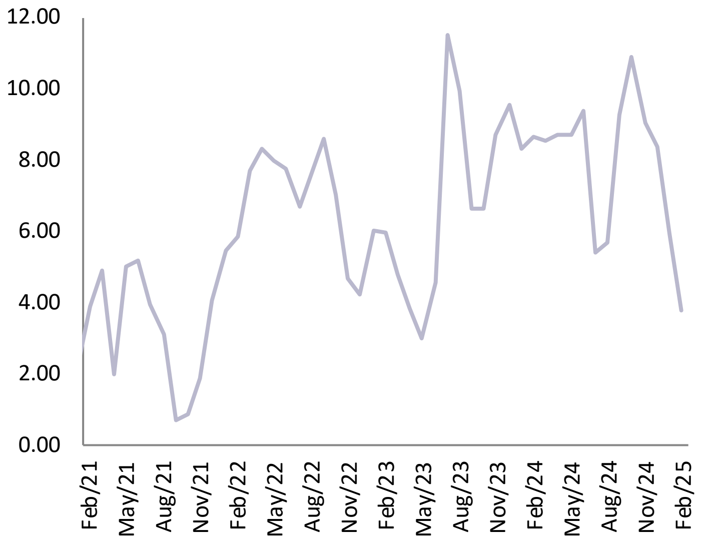
- RBI reduced the repo rate from 6.5% to 6.25% in Feb'25 for the first time in nearly 5 years. We believe the RBI will continue its policy easing measures with another 25bps cut in repo rates in the Apr'25 MPC meet.
- CPI inflation, as of Feb'24 moderated to <4% in Feb'25 and stood at 3.6% from 6.2% as of Oct'24. This decline was predominantly the result of a sharp fall in food inflation (~39% of the CPI basket), from the highs of 10.9% in Oct'24 to 3.8% in Feb'25.

Exhibit 7. India CPI inflation (%) (3.6% as of Feb'25)



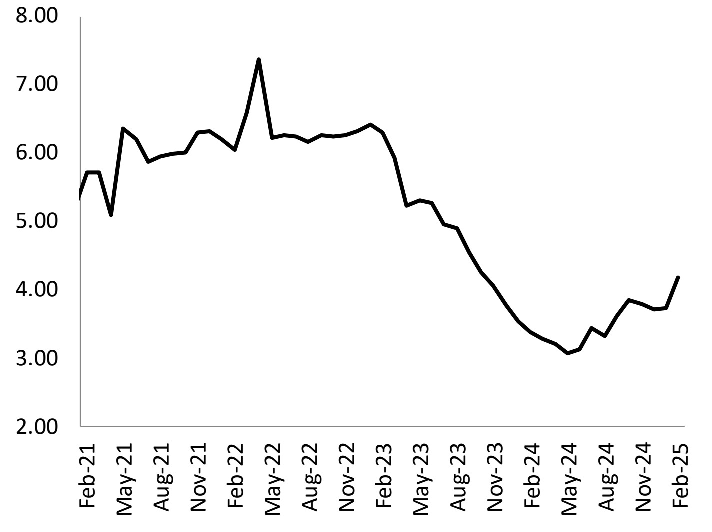
Source: CMIE, JM Financial

Exhibit 8. India food inflation (%) (3.8% in Feb'25)



Source: CMIE, JM Financial

Exhibit 9. India core inflation (%) (4.2% in Feb'25)

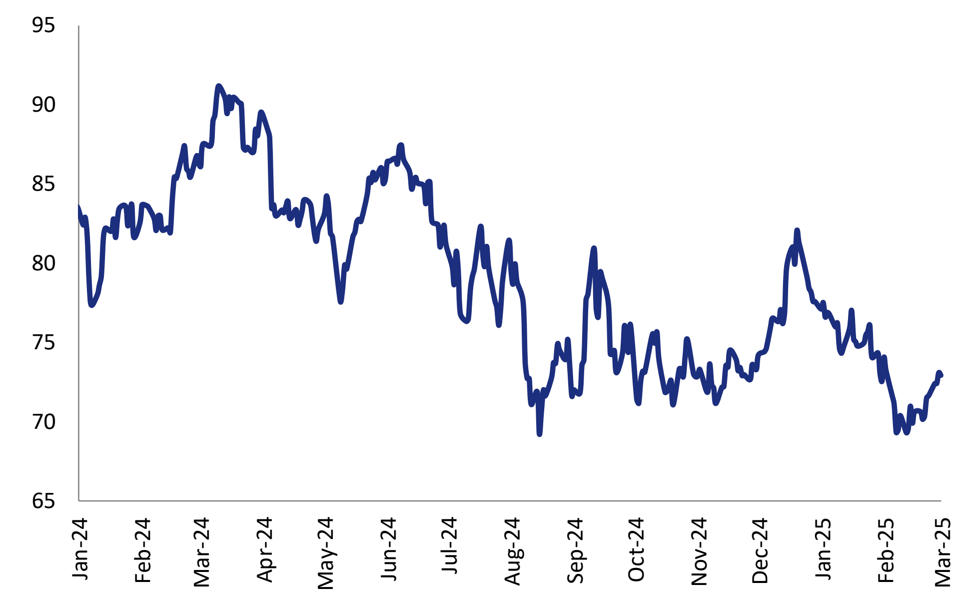


Source: CMIE, JM Financial

Brent crude correction is another significant positive

India, being a net importer of crude, benefits from a decline in prices. Since the peak of USD 91/bbl in Apr'24, Brent crude prices have corrected significantly to USD 73/bbl currently. This should appreciably ease inflationary pressure.

Exhibit 10. Movement in Brent crude since Jan'24 (USD/bbl)



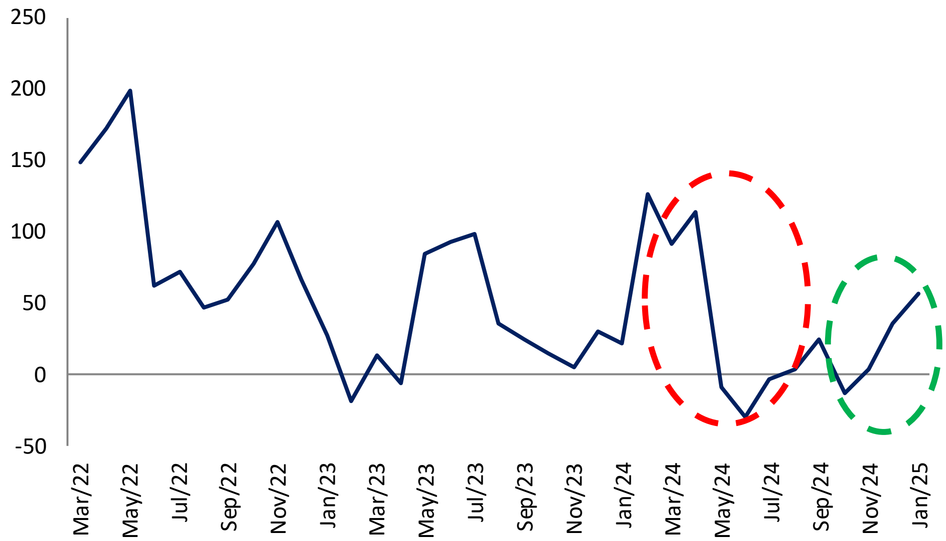
Source: Bloomberg, JM Financial

Government capex has already started picking up

- Central government capex growth in 1HFY25 was weak due to the general elections and a strong monsoon that disrupted supply chains in India (highlighted with a red circle in Exhibit 11). On the back of this, the government revised down its FY25 capex outlay to INR 10.2trln vs. initial expectations of INR 11.1trln.
- We observed green shoots in Nov'24, and this further picked up in Dec'25 and Jan'25 (highlighted with a green circle in Exhibit 11).

- Outlook for FY26E remains decent with an expected central government capex outlay of INR 11.2trln (+7.3% YoY).

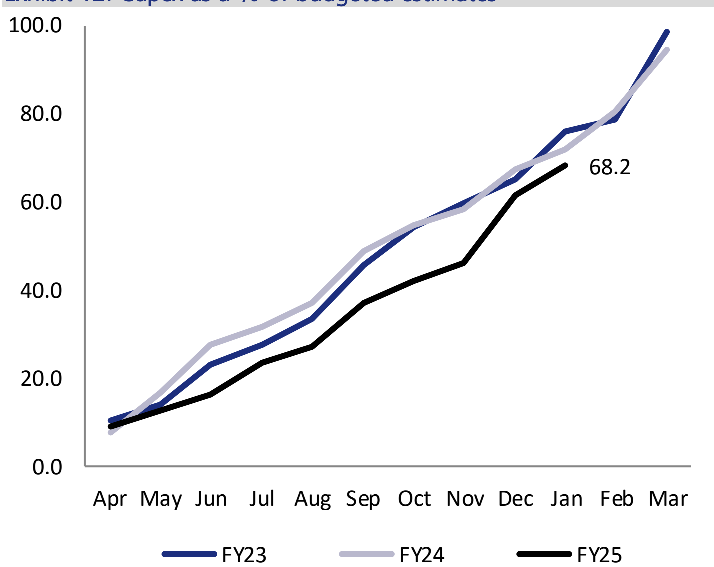
Exhibit 11. Growth in India's central government capex (3M rolling) (%)



Source: CGA, JM Financial

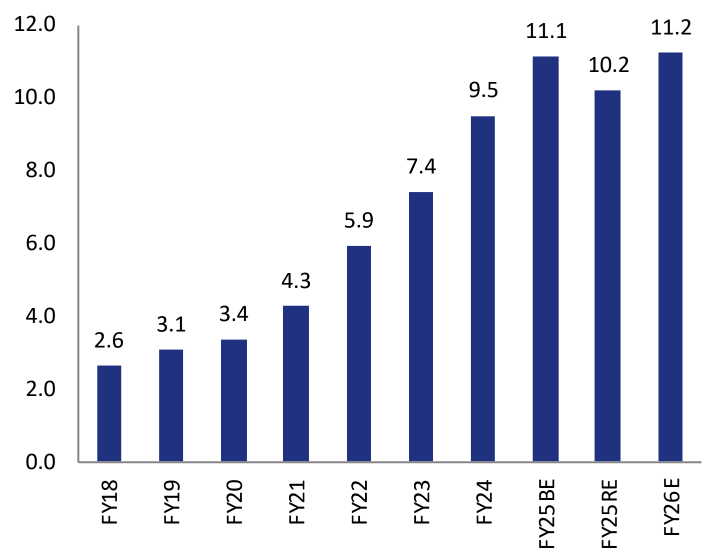
- In 1HFY25, capex incurred as a % of FY25BE stood at 37.3%, significantly lower than 49% on a YoY basis. However, through Oct'24-Jan'25, this seems to have significantly picked up. It is now at 68.2% vs. 72% observed in FY24.

Exhibit 12. Capex as a % of budgeted estimates



Source: CGA, JM Financial

Exhibit 13. Central government capex (INR trln)



Source: CGA, JM Financial

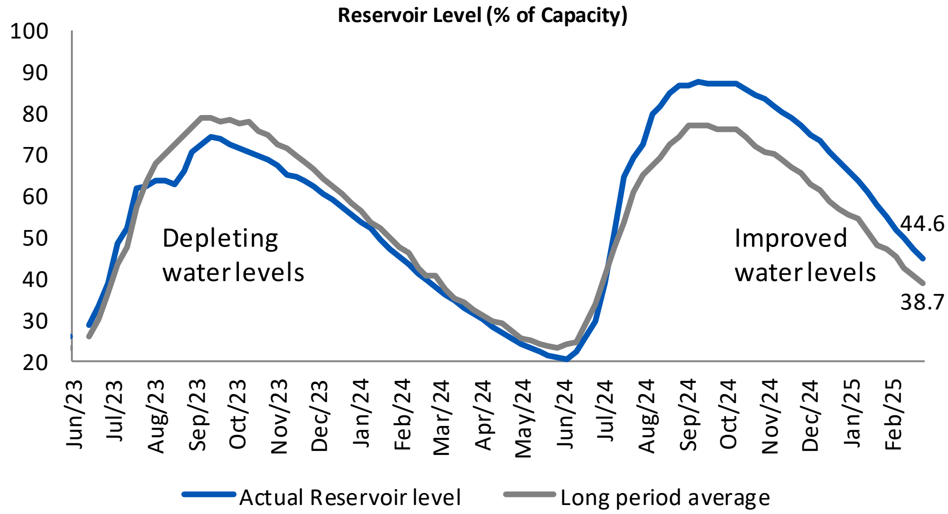
Outlook for urban and rural consumption improve

Reservoir levels and wage growth should drive up rural consumption in FY26…

- Unlike CY24, the rural economy should do better in CY25 on the back of good monsoons and comfortable reservoir levels. As highlighted in Exhibit 14, current reservoir levels are higher than long-term average levels. This has given confidence to the farmers and led to higher crop sowing, which should eventually reflect in higher income. The uptick in agricultural and non-agricultural wages should also drive higher disposable income.

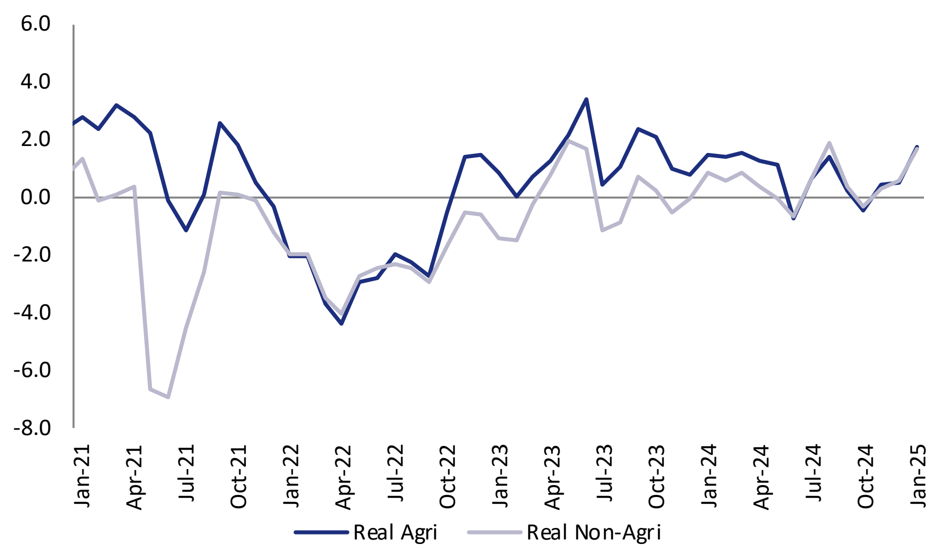
- India has also seen many major state elections recently where the winning party has promised cash dole-outs (primarily to women). This should also contribute to the buoyancy of the rural economy.

Exhibit 14. India reservoir levels are at comfortable levels currently (%)



Source: CEIC, JM Financial

Exhibit 15. Growth in rural wages is clearly visible (%)

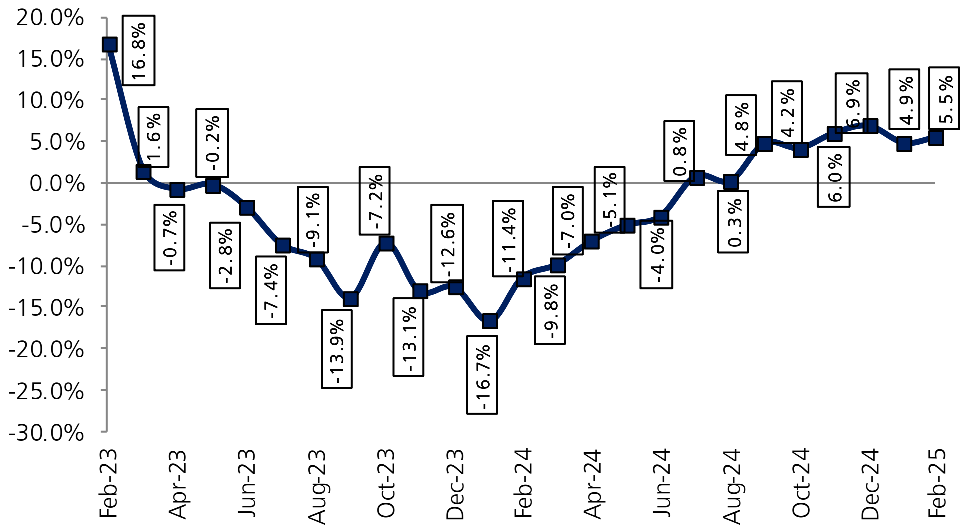


Source: CMIE, JM Financial

Urban consumption can benefit from tax cuts and an improving job market

- One school of thought is that the recent stock market correction could have a negative wealth effect (given higher participation from retail investors and retail household savings in the recent rally), which could impact consumer discretionary demand. Our channel checks with passenger vehicle dealers indicate a subdued environment; several dealers indicated a decline in customer walk-ins and deferment of purchases. At the same time, to incentivise customer decisions, discounts are also at elevated levels. On similar lines, demand for consumer durables also remains subdued (barring ACs, which is expected to benefit from a strong summer).
- However, we expect that the income tax cuts announced in the recent Budget, wherein the government has foregone revenue to the tune of INR 1trln should place money in the hands of the urban population and drive discretionary spends.
- Another data point that may act as a driver of urban consumption is that, as suggested by the Naukri job search index, job creation seems to be picking up.

Exhibit 16. Naukri job speak index (%, 3m rolling basis)

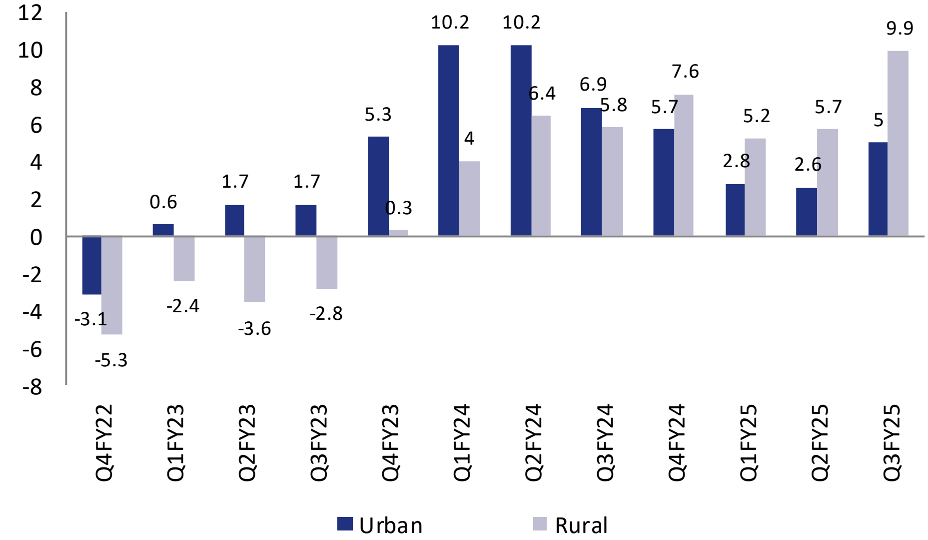


Source: Naukri, JM Financial

Rural seems to be doing better than urban recently

- Data from NielsenIQ also suggests that FMCG volume growth has been picking up, especially on the rural front, with YoY growth of 9.9% in Q3FY25. The rural economy has continued to be the main consumption driver over the last 3 quarters, with growth improving from 5.7% in the previous quarter.
- Similar trends are also being observed in urban volumes, although they lag rural growth. Urban FMCG volume has grown 5% YoY in 3QFY25 vs. 2.6% sequentially.
- As we highlighted earlier, the moderation of food inflation can be a driver for both the urban and rural economies, which, combined with savings from tax cuts and higher wages, should drive higher disposable income that, in turn, should drive up discretionary spend.

Exhibit 17. Rural demand grows significantly while urban consumption inches up

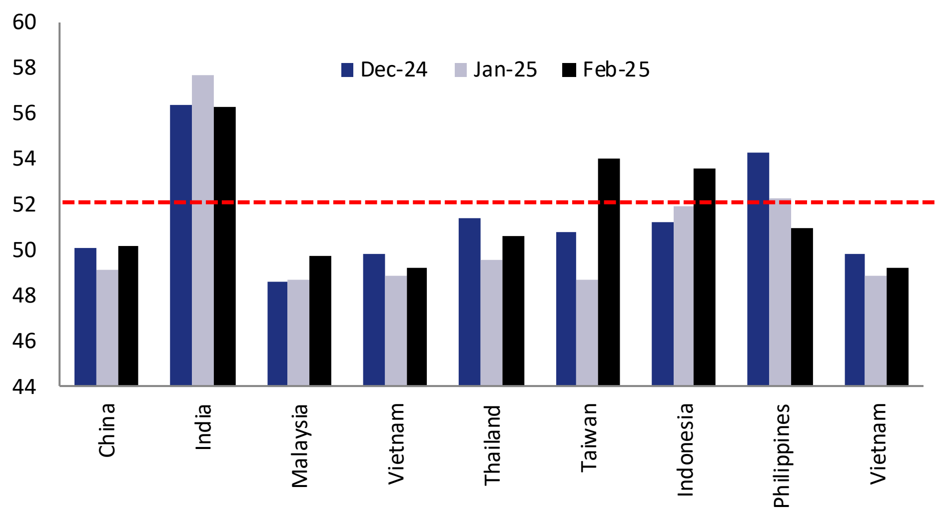


Source: NielsenIQ, JM Financial

Manufacturing activity is strong

India's manufacturing performance continues to be robust when compared to its Asian peers. This is evident from the latest PMI reading of 56.3, which is substantially higher despite the recent moderation. China's PMI reading (50.2) is barely in the expansion zone.

Exhibit 18. India's manufacturing PMI is superior to its Asian peers



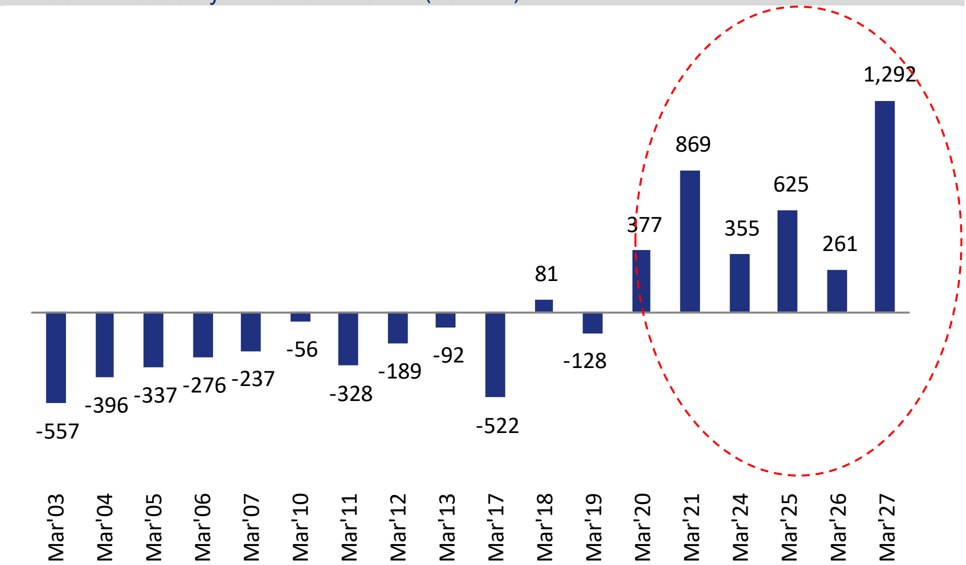
Source: Bloomberg, JM Financial

Have the FIIs already sensed that the economy is improving?

Are the FIIs back?

FIIs remained net sellers in the first half of Mar’25, offloading equities to the tune of USD 3bn; but they turned net buyers in the second half. Since 20th Mar’25, they have consistently been net buyers in Indian equities, purchasing stock worth USD 3.8bn.

Exhibit 19. India daily FII flows in Mar’25 (USD mn)

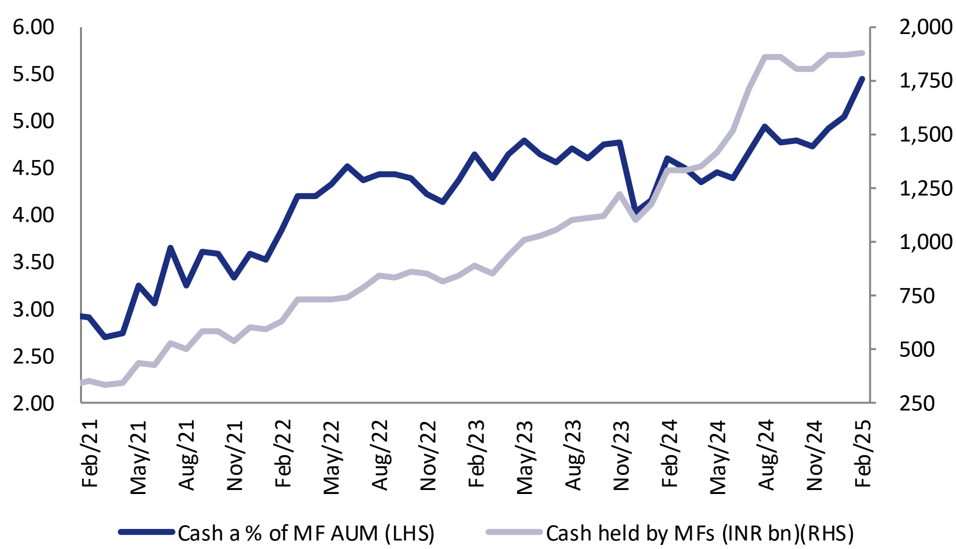


Source: NSDL, JM Financial

DII cash levels of INR 1.9trln seem encouraging

Data as of end-Feb’25 suggests that DIIs are sitting on a fairly large pile of cash, which is ~5.4% of equity AUM.

Exhibit 20. Cash levels with Indian MFs



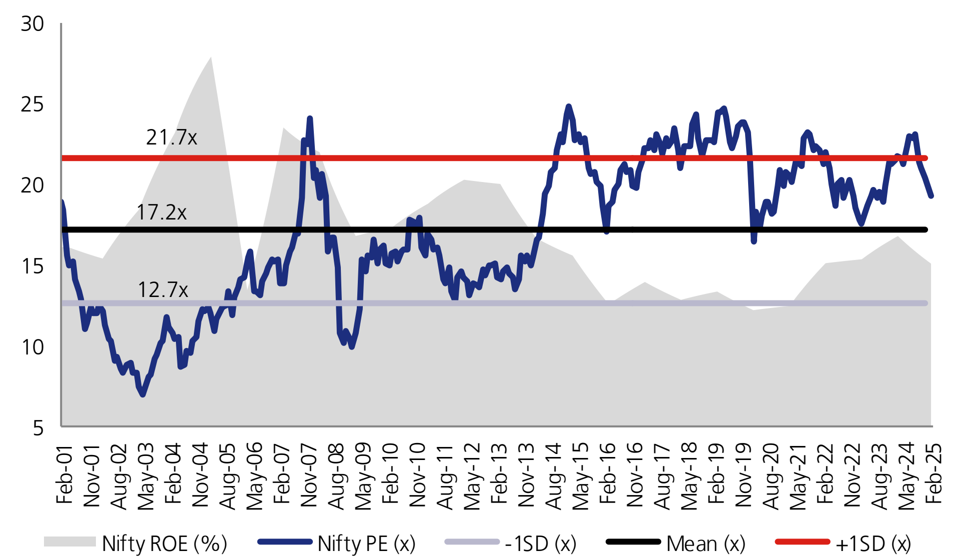
Source: Company, Bloomberg, JM Financial

Large cap valuations have become more reasonable

Nifty50 valuations have almost mean reverted

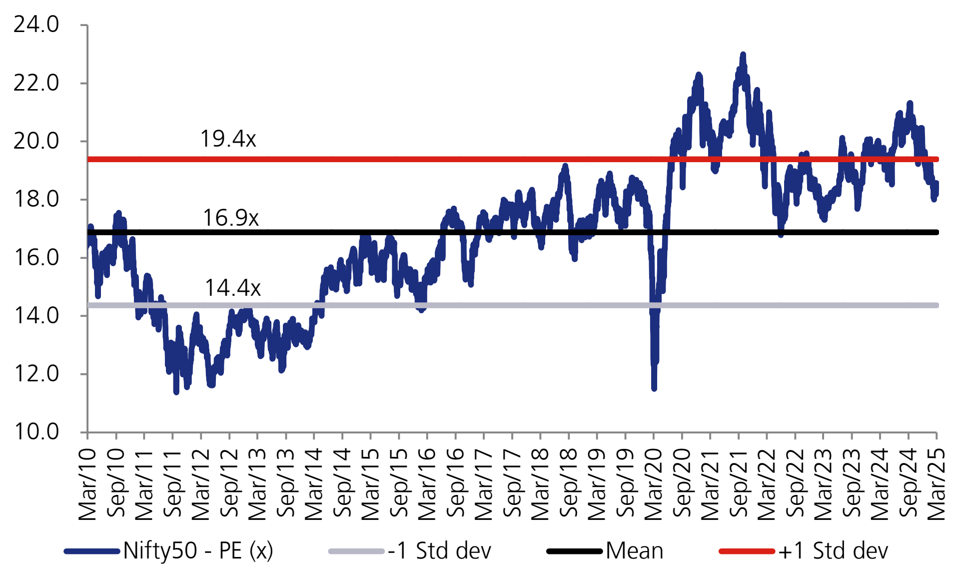
Since Sep'24, the Nifty50 has corrected ~11% from the top of 26,277. Valuations, on similar lines, have come off from the peak of 23.0x to 18.6x 1-year forward P/E, closer to the long-term average of 17.2x. We believe that the mean reversion story has broadly panned out, leaving room for limited downside. However, this depends on decent corporate earnings in 4QFY25 and FY26.

Exhibit 21. Nifty – 1-yr forward P/E chart (since 2000)



Source: Bloomberg, JM Financial

Exhibit 22. Nifty – 1-yr forward P/E chart (since 2010)

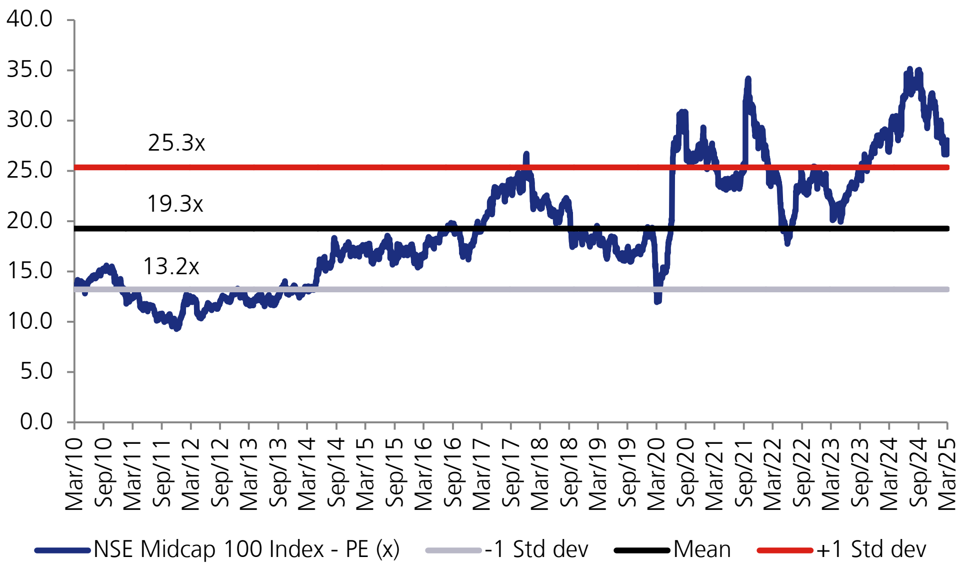


Source: Bloomberg, JM Financial

Nifty Midcap 100 and Nifty Small Cap 100 valuations remain above +1SD

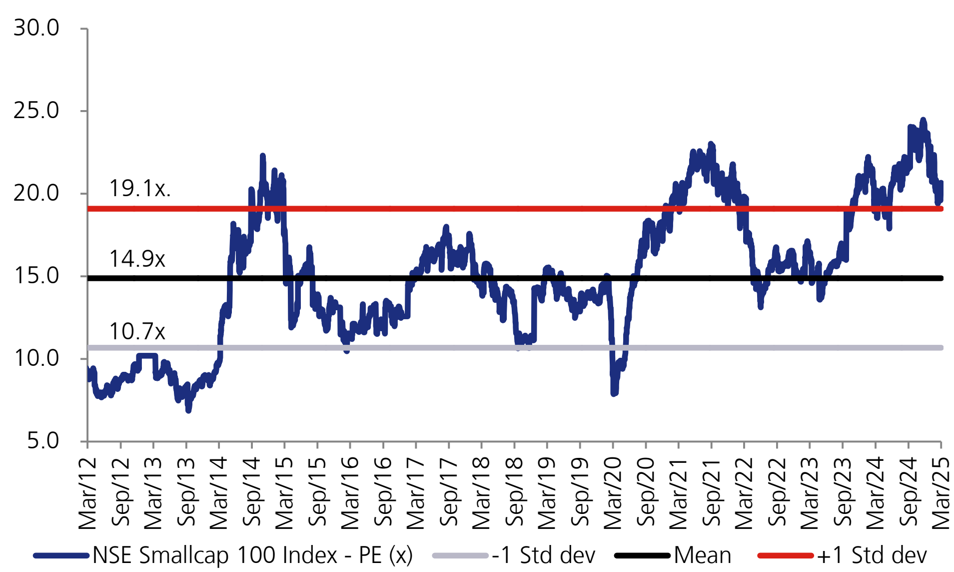
However, Nifty Midcap 100 and Nifty Small Cap 100 1-year forward P/E still trade higher than +1SD despite the 15% and 18% correction respectively. Hence higher earnings growth delivery is more pertinent in mid and small caps to prevent a further correction.

Exhibit 23. Nifty Midcap 100 – 1-yr forward P/E chart (since 2010)



Source: Bloomberg, JM Financial

Exhibit 24. Nifty Small Cap 100 – 1-yr forward P/E chart (since 2012)

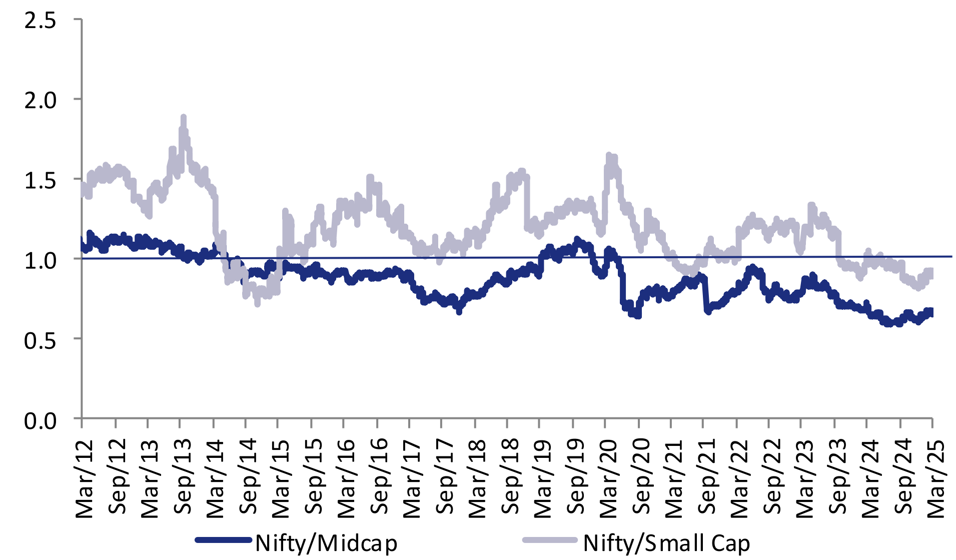


Source: Bloomberg, JM Financial

Nifty50 trades at a discount to mid and small cap indices

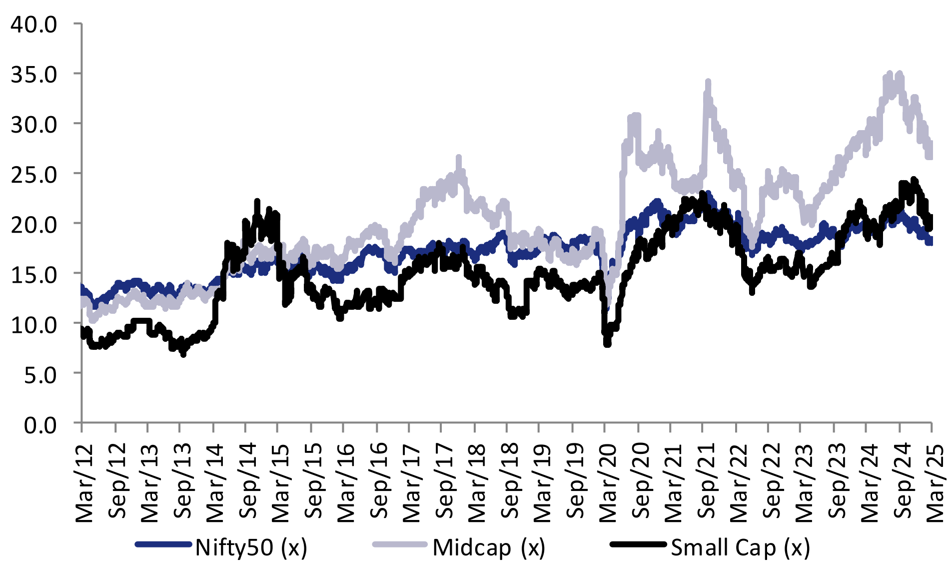
Interestingly, Nifty50 valuations are now at a discount to the midcap and small cap indices. As can be observed from the below exhibit, the Nifty premium reversed for both the midcap and small cap indices around 2HCY14. While this trend continued for the midcap index, it reversed for the small cap index, reverting only for a brief period in 2019, and again in 2HCY23.

Exhibit 25. Comparing Nifty forward valuation premium to Midcap 100 and Small cap 100



Source: Bloomberg, JM Financial. Note: The horizontal line marks 1, above which it is a Nifty premium and below which it is a Nifty discount

Exhibit 26. Comparing 1-yr forward mean valuations (x)



Source: Bloomberg, JM Financial

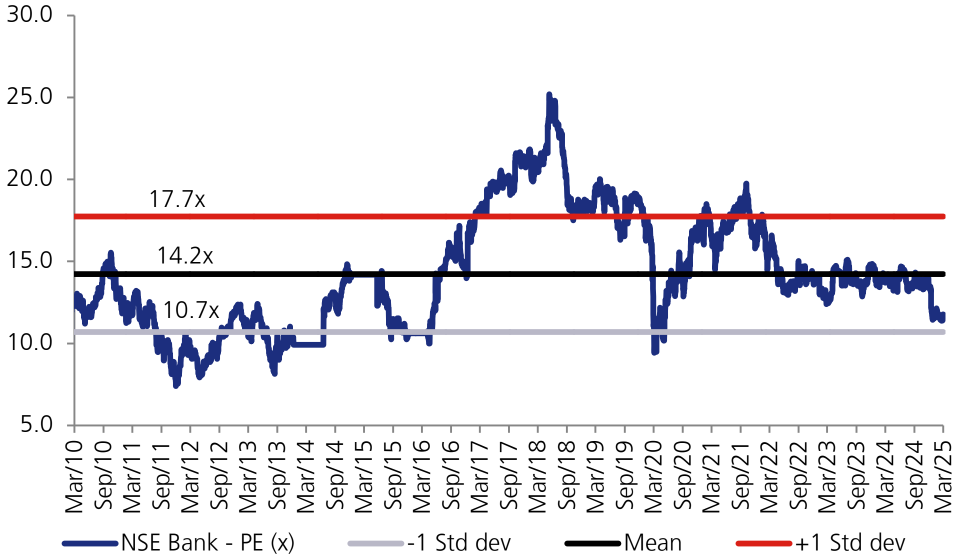
Nifty Bank valuations appear to be attractive

Compared to the Nifty50, Bank Nifty valuations appear significantly attractive trading below their 15-year mean and closer to -1SD. This indicates either of two possibilities:

- **The Bank Nifty has not really performed well.** This does not seem to be the case. When we analyse the performance of the Nifty50 and the Bank Nifty since Covid-19, we conclude that while the Bank Nifty has underperformed the Nifty, the underperformance is not that meaningful. To put this into perspective, over the last 5 years, i.e., from Covid-19 lows, the Nifty has given an absolute return of 170%, compared to the Bank Nifty's 155%.

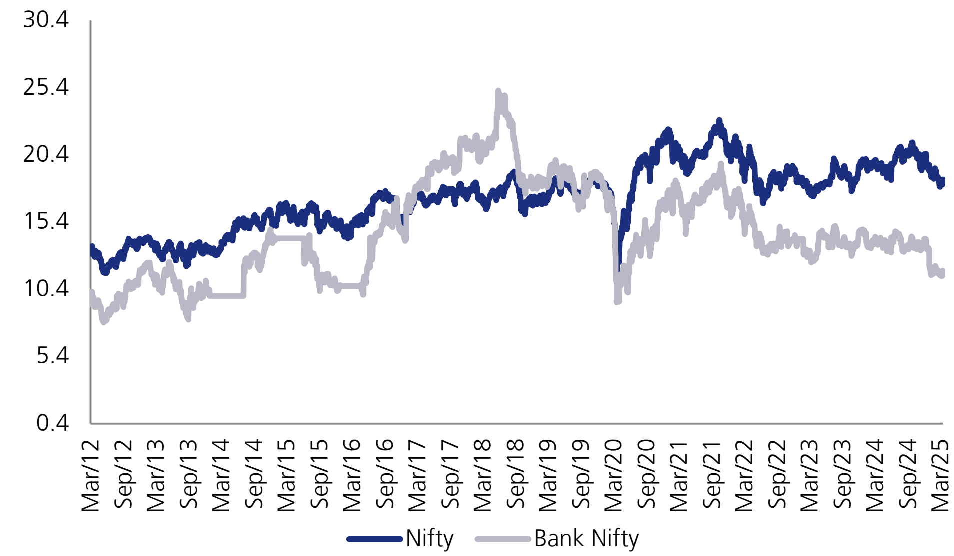
- **The Street remains wary of according a higher multiple to banks.** This appears to be the reason given uncertainty over several moving parts, which include delinquencies in the unsecured book of banks, rate cuts, and the economy being unable to pickup to expected levels, amongst others.

Exhibit 27. Nifty Bank – 1-yr forward P/E chart (since 2010)



Source: Bloomberg, JM Financial

Exhibit 28. Nifty Bank and Nifty50 1-yr forward mean P/E (x)



Source: Industry, Bloomberg, JM Financial

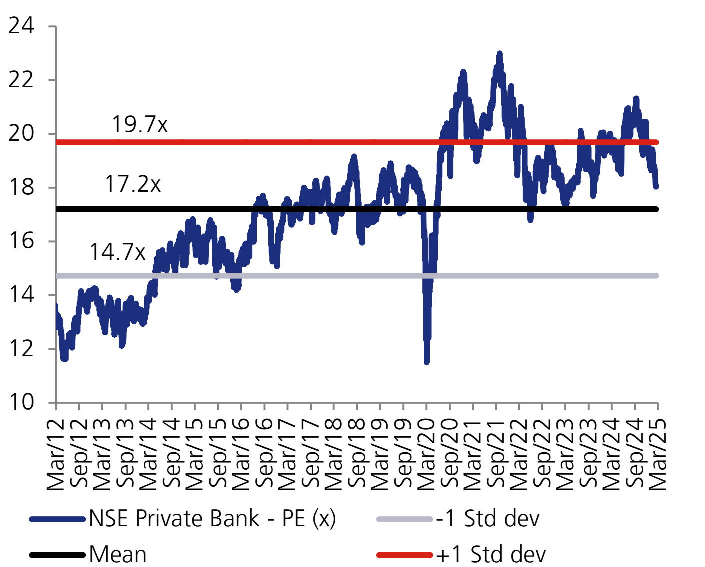
The Bank Nifty's attractive valuations vis-à-vis the Nifty50 can further be explained by the below exhibit, which plots the Nifty50 valuation premium over the Bank Nifty, currently at 1.6x vs. the mean of 1.2x since 2012. This leaves room for a potential catch-up in valuations for the Bank Nifty or, on the flip side, a slide in valuations of the Nifty.

Exhibit 29. Nifty50 valuation premium over Bank Nifty

Source: Industry, Bloomberg, JM Financial

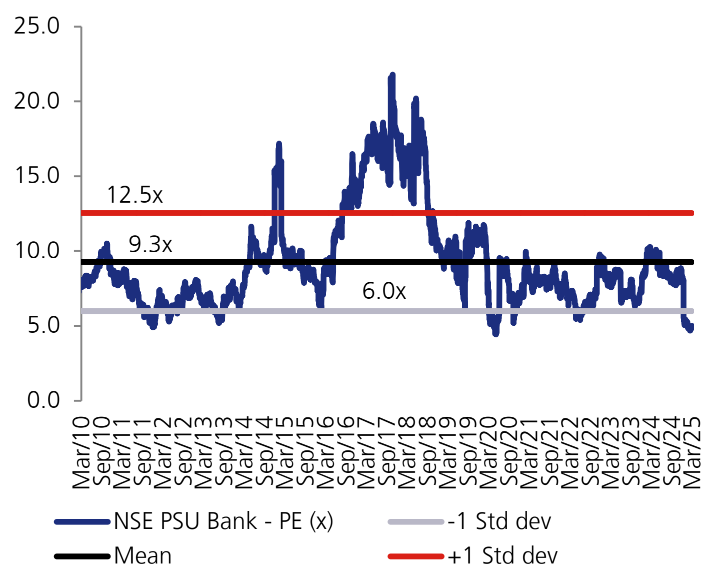
Further slicing the data, we conclude that, solely on the basis of valuations, PSU Banks appear to be attractively valued on both absolute and relative basis. As can be seen in Exhibit 30 and 31, while Private Banks are trading slightly above their historical mean valuations, PSU Banks are trading below the -1SD valuations. Further, on a relative basis as well (Exhibit 33), the premium of private bank valuations over PSU bank valuations is at an all-time high; similar levels have been witnessed only during Covid-19, when the worry was that PSU Banks were highly susceptible to regulatory interference.

Exhibit 30. Nifty Private Bank – 1-yr forward P/E chart



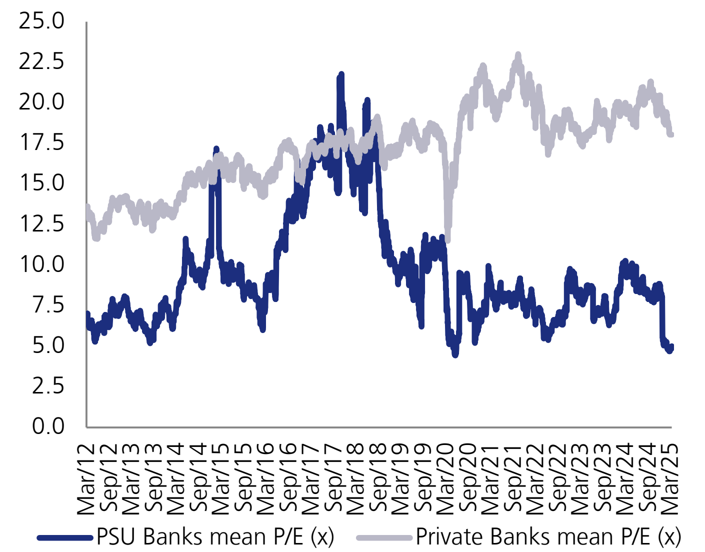
Source: Bloomberg, JM Financial

Exhibit 31. Nifty PSU Bank – 1-yr forward P/E chart



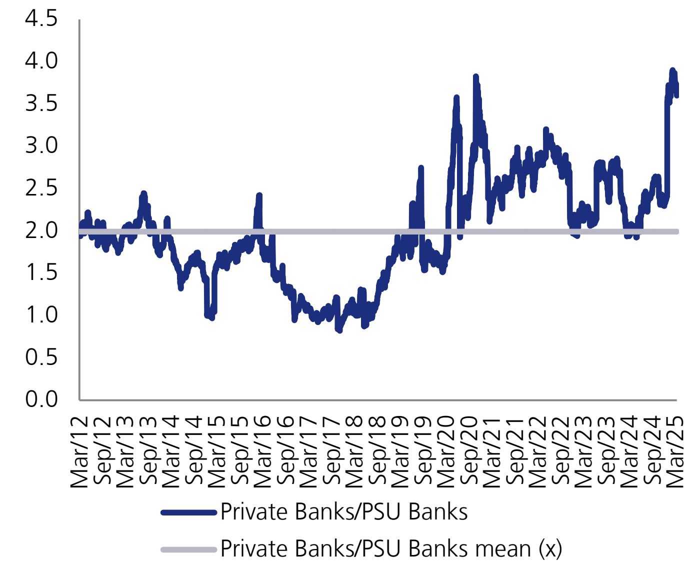
Source: Bloomberg, JM Financial

Exhibit 32. Comparing Private and PSU bank valuations



Source: Bloomberg, JM Financial

Exhibit 33. Premium of private bank valuations over PSU banks



Source: Bloomberg, JM Financial

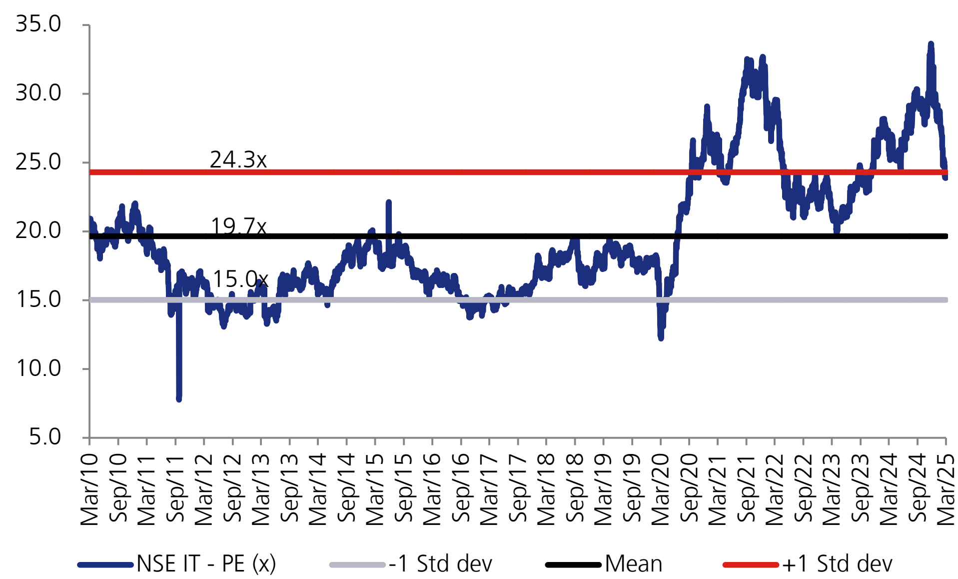
But beyond valuations, how are they placed?

- FY26 is expected to be a difficult year for PSU banks with a flat to decline in earnings vs. FY25 on account of multiple headwinds – (1) Decline in recoveries from earlier written-off loans and (2) New treasury regulations putting pressure on treasury income, which could have a negative impact on the fee income profile.
- The weakening liability franchise with market share loss in deposits and potential policy rate cuts should have a negative pressure on NIMs. Credit cost may normalise in FY26 from ultra-low levels seen in FY24/25 on account of increased stress in a few segments.
- Overall, we should see earnings YoY growth only in FY27. On the positive side, valuations are benign with most names trading below book. However, we will watch out for earnings momentum in the next few quarters before becoming more constructive.
- We prefer large private banks over PSUs at this point of time. If we further bifurcate private banks into large private banks and small private banks, we see that for most large banks, the issue of unsecured loans is well under control either due to controlled exposure to this category or the book consisting of premium customers, a category which is not under pressure currently.
- Further, while valuations of Private Banks may not be as attractive as that of PSU Banks, they are hovering around the mean, hence they do not fall under the overvalued category and might provide exposure to a more predictable set of numbers.

IT valuations have corrected meaningfully, but are still not attractive

The IT sector has seen valuation coming off from the peak of Sep'24 but is still at +1SD. This sector, arguably, is also the most susceptible to geopolitical risks, which can keep volatility elevated.

Exhibit 34. Nifty IT – 1-yr forward P/E chart (since 2010)

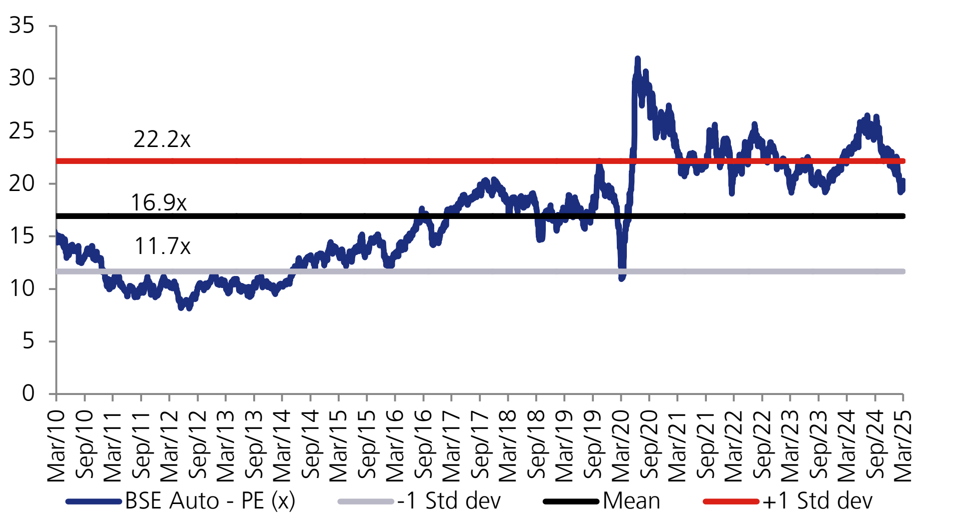


Source: Bloomberg, JM Financial

Other key indices

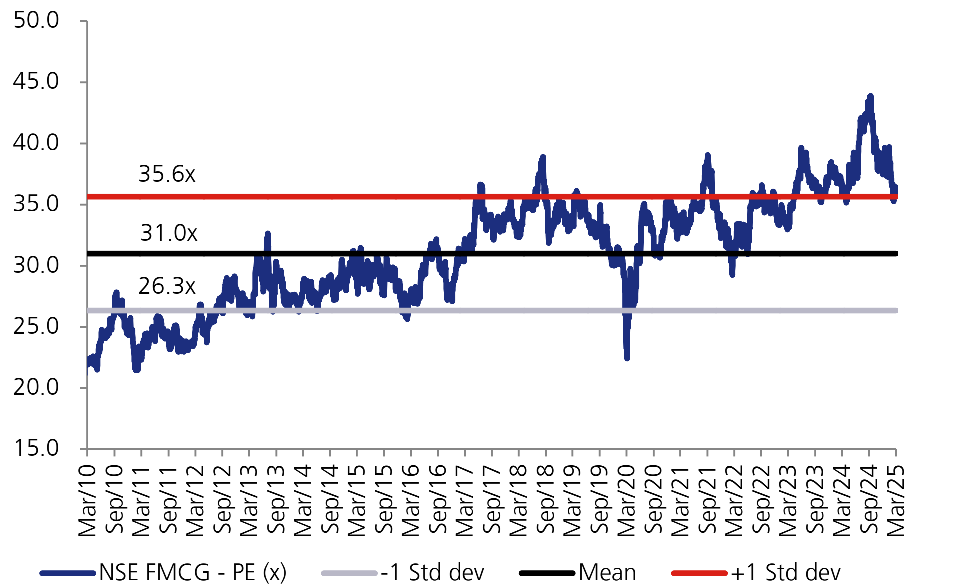
Below, we analyse how other indices besides Banking and IT are placed. We categorise a sector trading below its +1SD valuation as reasonably valued. Sectors that fall under this bucket include Autos. Besides this, FMCG, Capital Goods, Energy, and Pharma are hovering around +1SD, hence they appear relatively expensive.

Exhibit 35. BSE Auto – 1-yr forward P/E chart (since 2010)



Source: Bloomberg, JM Financial

Exhibit 36. Nifty FMCG – 1-yr forward P/E chart (since 2010)

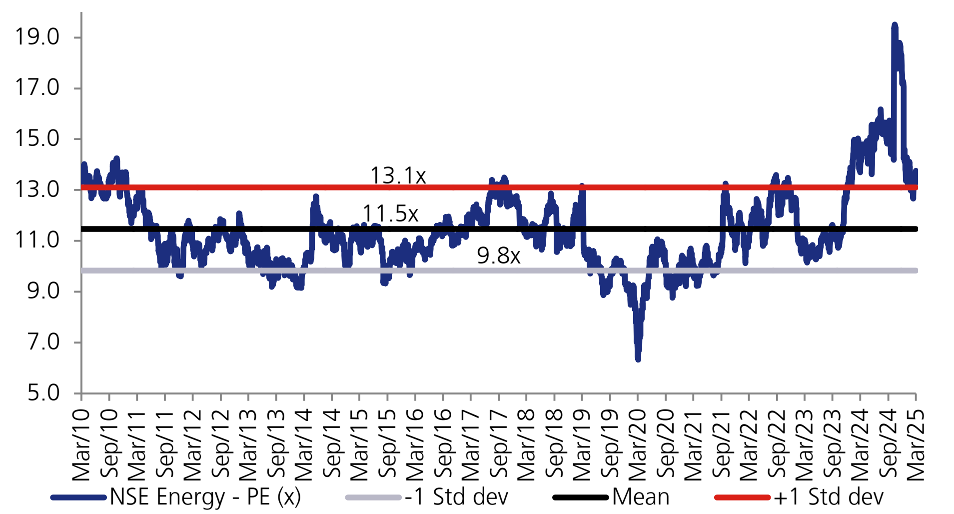


Source: Bloomberg, JM Financial

Exhibit 37. BSE Capital Goods – 1-yr forward P/E chart (since 2010)

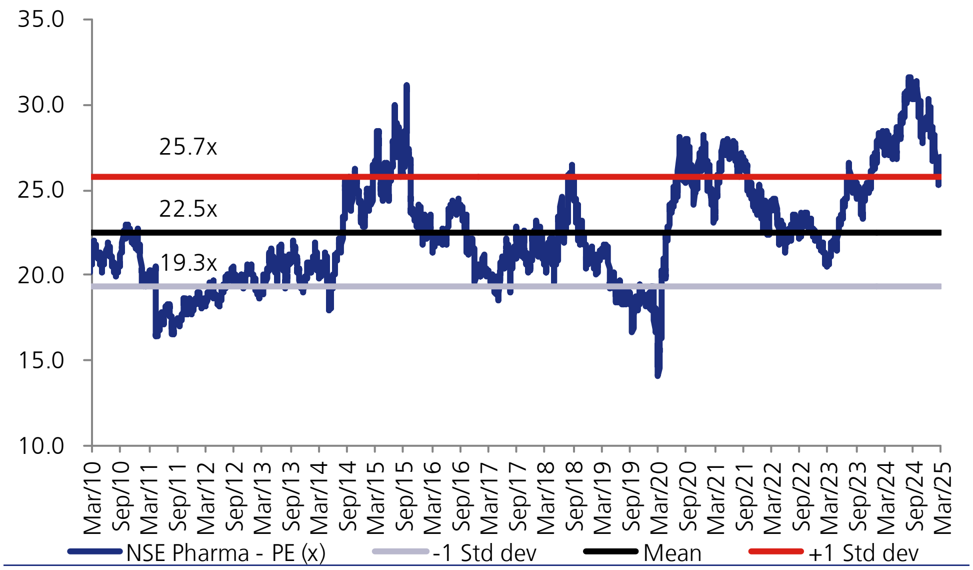
Source: Bloomberg, JM Financial

Exhibit 38. Nifty Energy – 1-yr forward P/E chart (since 2010)



Source: Bloomberg, JM Financial

Exhibit 39. Nifty Pharma – 1-yr forward P/E chart (since 2010)



Source: Bloomberg, JM Financial

APPENDIX I

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Rating	Meaning
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Hold	Price expected to move in the range of 10% downside to 10% upside from the current market price for stocks with market capitalisation in excess of INR 200 billion and REITs* and in the range of 10% downside to 15% upside from the current market price for all other stocks, over the next twelve months.
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