Aug, 2022

MARKET IMPACT REPORT

GLOBAL MACROECONOMIC OUTLOOK

Uncertainty and Gloomy Outlook

A tentative recovery in 2021 has been followed by increasingly gloomy developments in 2022. The economic distress induced by the Ukraine crisis is causing widespread hardship and substantially slowing the global economic growth in 2022 and adding to the inflation – suggestive of the stagflation of the 1970s. Rapid increases in food and fuel prices, and significant tightening of monetary policy in advanced economies have hit developing nations the hardest. According to the International Monetary Fund projections, the global growth will decelerate from an estimated 6.1% in 2021 to 3.6% in 2022 and 2023. Inflation estimates for 2022 are 5.7% in developed economies and 8.7% in emerging market and developing economies as a result of commodity price hikes and a broadening of price pressures due to the war, which is prompting more central bank tightening. Also, China's economic slowdown has added to global supply chain disruptions.

Macroeconomic Indicators

Indicators	US	UK	China	India
GDP YoY (FY21-22)	5.7%	7.4%	8.1%	8.95%
Inflation Rate (June 2022)	9.1%	9.4%	2.5%	7.01%
10 Year G-Sec	2.79%	1.93%	2.78%	7.37%
Policy Rate	1.58%	1.25%	2.85%	4.9%

Source: Bloomberg

Monetary Policies

Central bank	Benchmark	Current Rate	Method	Policy Measures
Federal Reserve	Fed Fund Rates	1.58%	Contractionary Monetary Policy	The Fed raised the federal funds rate by 75 basis points.
Reserve Bank of India	Repo Rate	4.90%	Contractionary Monetary Policy	Increase the policy repo rate under the liquidity adjustment facility (LAF) by 50 basis points to 4.90 per cent
People's Bank of China	Loan Prime Rate (1 Year)	3.7%	Quantitative Easing	The People's Bank of China pledged to keep monetary policy support to aid the economy's recovery while signaling that stimulus would likely focus on boosting credit rather than lowering interest rates.
	Loan Prime Rate (5 Years)	4.45%		

Source: Bloomberg

GLOBAL MACROECONOMIC OUTLOOK

Fed leaves it open

The Federal Open Market Committee of the US Federal Reserve hiked the federal fund rate by 75bps to the range of 2.25% - 2.50%. Fed chairman Jerome Powell outrightly rejected the speculations that the US economy is in recession. The FOMC members are of the opinion that the strong labour market allows the US economy to tolerate rapid monetary tightening. Reiterating the commitment to achieve 2% inflation target, Fed chairman indicated that another unusually large increase could be appropriate at the next meeting. The US yield curve is now inverted the most in two decades, highlighting that markets strongly believe a recession is around the corner. The 2 year yields are now over 30bps lower than the benchmark 10yr yields clearly indicating that the market sees higher risk of recession than the Fed.

Exhibit 1: Yield Curve most Inverted in decades (Spread between 2-year and 10-year Treasury yields)

Source: Bloomberg

Fiscal Policy

India

As India has shown the best recovery among the emerging nations, the fiscal measures taken by the government have played a major role in reaching this level. The pandemic has cost India two years of economic growth, leading to increased income poverty. The government expenditure has increased substantially on rural employment and food subsidy. The Fiscal Deficit is expected to be 6.4% of the GDP for FY23. The Fiscal Strategy of India consists of 3 P's: Protectionism through increasing tariffs and incentives like PLI schemes to increase production and projects to create infrastructure.

USA

US Fiscal Deficit has been estimated that it will shrink to $1 trillion. Revenues are projected to reach their highest level as a share of GDP. Outlays are projected to decrease in the post covid era as spending on pandemic-related wanes will decrease. However, growing debt and interest rates will cause net outlays (Disbursement- Refunds) to increase. An increase in the expenditure related to healthcare and the ageing population will boost federal outlays, significantly relative to the GDP if current policies remain unchanged. The government expects to spend $6.011 trillion and 65% of this fiscal expenditure will be for social security, Medicare and Medicaid.

Republic of China

As China has a huge ability as compared to other emerging nations to spend, it has signalled a willingness to deploy further policy support to ensure stable economic performance. The fiscal deficit has been forecasted to widen by 5.8% in 2023. The government will continue to use tax cuts and tax rebates to support growth amounting to CNY 2.5 trillion. More focus will be on R&D development due to the threat that the nation is facing from China + 1 strategy in the post covid world. The government is also focussing on the property market which has been facing strains due to the Evergrande failure of debt repayment which had a ripple effect on the economy. Officials vowed to keep prices and market expectations stable and adopt city-specific measures to ensure the sector's sound development. Fitch believes this implies further easing of local administrative measures and may add impetus to social housing construction.

Europe

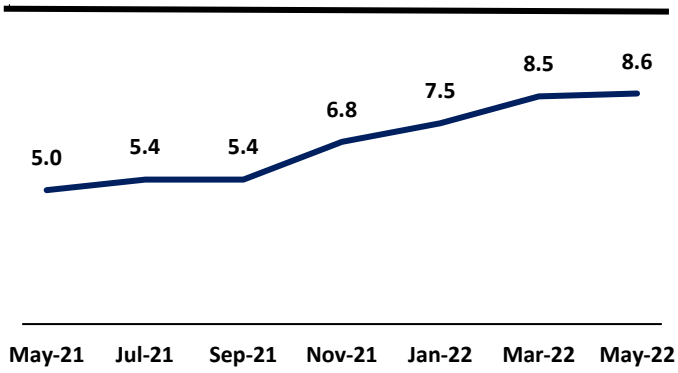
Europe, being on the frontline of Ukraine war, faces the biggest risk of stagflation, characterized by rising inflation, stagnating output and rising unemployment. The Euro area job market has been resilient so far, despite a surge in headline inflation, driven by soaring prices. The EU's fiscal rules will remain suspended until the end of FY23 to help countries fallout from the Ukraine war.

GLOBAL MACROECONOMIC OUTLOOK

Global Inflation Boiling Up

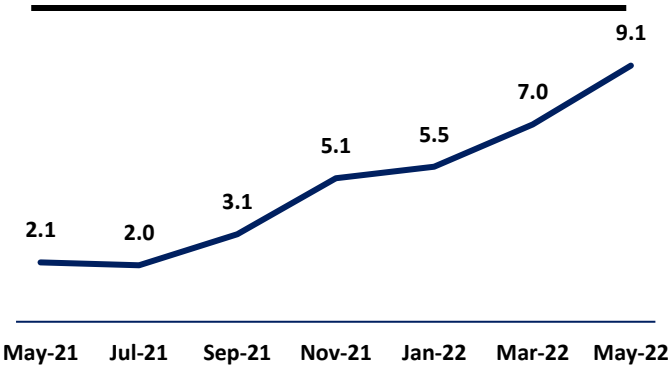
Against the backdrop of global economic slowing down on account of Covid-19 pandemic and the ongoing conflict between Russia and Ukraine, supply chain bottlenecks have ensued. The impact of same has been reflected with the surge in global inflation. There also has been an exacerbated risk of stagflation (sluggish growth and higher inflation) going further. Global inflation print has scaled to its highest level since the 1980s, with persistent surge in crude and food prices.

Exhibit 2: US inflation spiked in May 2022 (%)



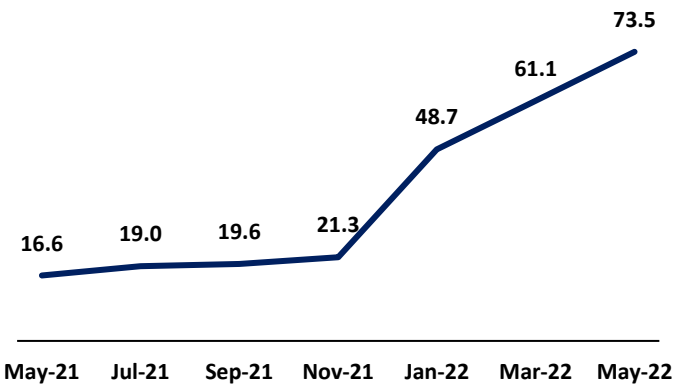
Source: Bloomberg

Exhibit 3:UK inflation surges to 40 year high (%)



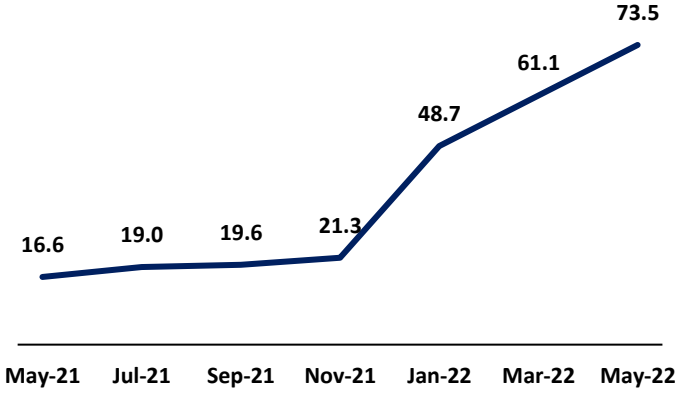
Source: Bloomberg

Exhibit 4:Turkey's inflation growing at a rapid pace (%)



Source: Bloomberg

Exhibit 5:Germany's inflation upward trend (%)

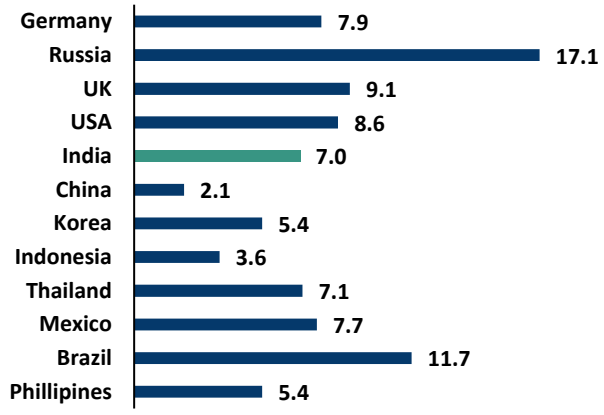


Source: Bloomberg

How does India fare?

Despite global inflation soaring, all the countries cannot be viewed similarly as no one glove fits all. Also, India ii doing relatively better than other countries on this account. Indian economy has been facing the brunt of "imported inflation" led by ,mounting pressure on energy, fertilizers and other inputs. However the aggravated impact of the same has been curtailed with proactive measures such as reduction in excise duty, duty free import of sunflower and soyabean. Yes the current inflation does continue to remain above RBI's mandate but as compared to other global countries, India is in a much better place to manage inflation.

Exhibit 6:Comparison of inflation May 2022 (%)



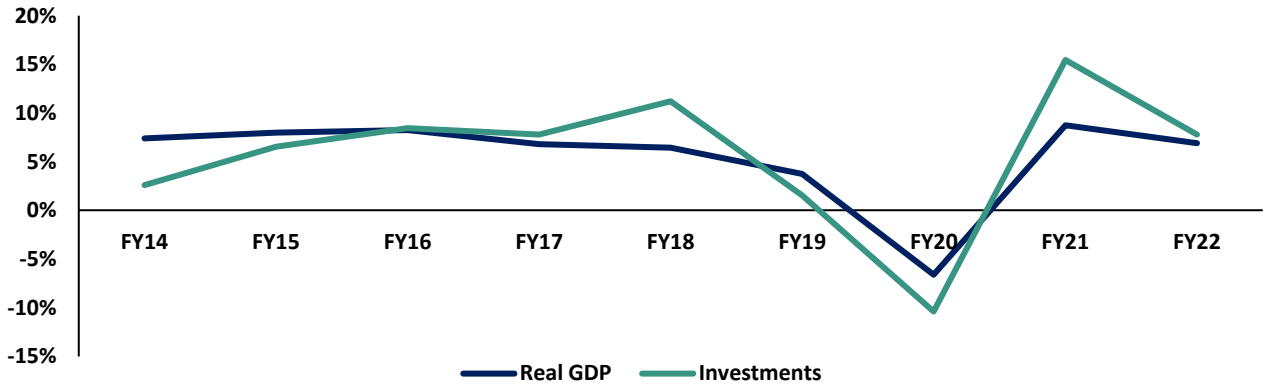
Source: Bloomberg

INDIAN MACROECONOMIC OUTLOOK

India's GDP growth for the Q4FY22 was recorded at 4.1% and the overall GDP for FY22 was at 8.7%. Both the numbers are lesser than expected indicating a flat growth rate considering the base effect as GDP contracted by 6.6% in FY21. Towards the end of FY21, there was excitement as India was prepared for a robust economic revival, with forecasters expecting more than 9% growth. The slow growth can be attributed to the omicron wave, hawkishness by the US Fed and the Russia-Ukraine conflict which led to a confluence of headwinds such as rising commodity prices, and disruption in the global supply chain and trade.

The GDP impact is currently not too significant as RBI Policy continues to be aggressive. Over the past two months, the policy rate has increased by 90 basis points to 4.9%. However, the effective rate increase is even higher when taking into account the introduction of the Standing Deposit Facility, which has increased the lower bound of the policy corridor from 3.35% to 4.65%, implying a total increase of 130 basis points. The central bank's principal goal is to promote growth, but doing so comes at the expense of excessive inflation, making life difficult for the average person.

Exhibit 7: Macroeconomic indicators like Real GDP and Investments trend over the years showing economic activities are recovering post pandemic



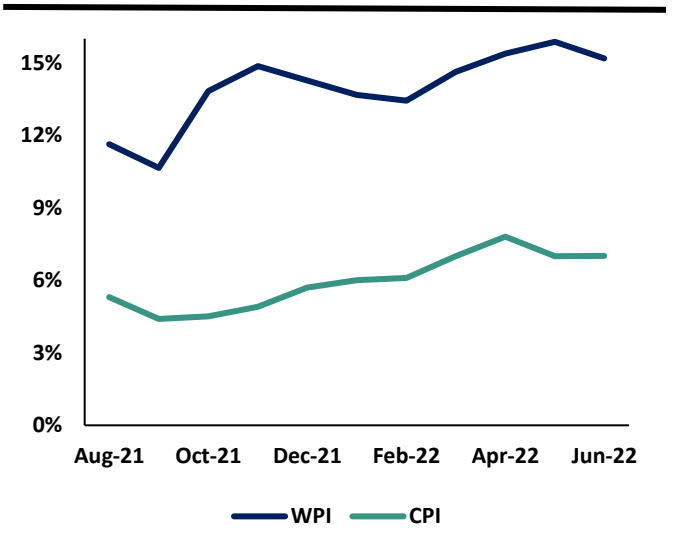
Source: OECD

Inflation

Common man problems continues due to high inflation rates:

The inflation rate stayed significantly over the RBI's objective of 4% and also above the tolerance band's upper range of 6%. The inflation rate for non-food items was even greater, exceeding 7%. Additionally, from 2021 to 2022, the Wholesale Price Index (WPI) inflation rate was double digits, and in April and May of 2022, it topped 15%. The present jump in inflation is brought by sharp price increases in crude oil (which rose to 83.56% in March from 55.17 % in February) and other commodities around the world.
High inflation results in price increases of essential goods like cooking oil, vegetables, transport and communication. Indonesia's ban on sunflower oil has caused a reduction in imports and a rise in oil prices. Soaring prices are leading to a fall in savings and in addition, increased interest rates have put a burden on the common man's pocket.

Exhibit 8: Wholesale and Consumer Price Inflation (%)



Source: Office of Economic Advisor, Bloomberg

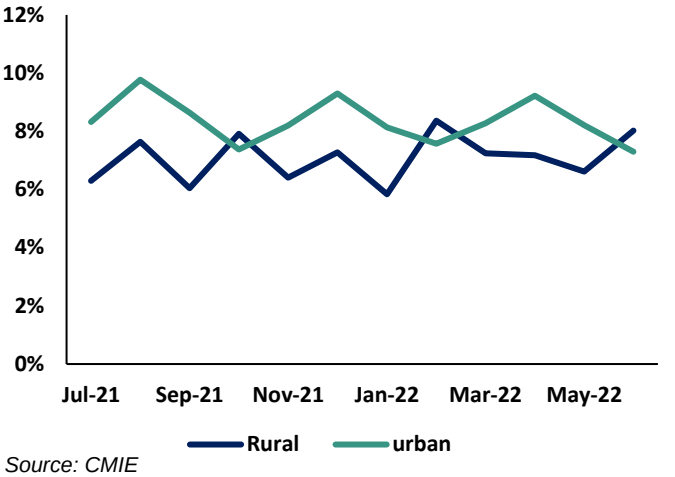
INDIAN MACROECONOMIC OUTLOOK

Unemployment Rates

India witnesses rising unemployment rates:

India's total unemployment rate grew by over 12% from last year in July and the rural unemployment rate grew by a staggering 26%. 8 million jobs were lost in rural India due to poor monsoons. However, the rate of unemployment was only modestly increased by the departure of small business owners and agricultural laborer's from the labor force. India's employment rate fell to 35.8% in June 2022, its lowest level in two years. According to CMIE, 2.5 million paid jobs were lost, demonstrating industry's escalating fragility. Among the Indian states, Rajasthan has witnessed the highest unemployment rate of 29.8%.

Exhibit 9: Rural unemployment rate exceeded urban unemployment in May'22



Source: CMIE

Trade Deficit

Imports outpace the rise in exports:

India's total exports, including both goods and services, have increased by 23.5% y-o-y in June 2022, totaling to US $40.13 billion. The total imports for the same period have increased 55.7% , totaling to US $82.4 billion, leading to a trade deficit of US $26.18 billion, 173% up y-o-y. While the ongoing conflict between Russia and Ukraine increase commodity prices globally, the spill over consequences of runaway inflation are harming trade demand and prospects for global economy. Imports have been essentially fueled by energy sources like oil and coke, with the latter being fueled by a shortage of indigenous coal in India.

Exhibit 10: India's overall trade deficit widening because of higher growth in imports as compared to exports

		April – June 2021 (USD Billion)	April – June 2022 (USD Billion)	Growth vis-à-vis April – June 2021(%)
Merchandise	Exports	95.54	118.96	24.51
	Imports	126.96	189.76	49.47
	Trade Balance	-31.42	-70.8	-125.34
Services	Exports	56.22	70.97	26.25
	Imports	30.41	45.35	49.15
	Trade Balance	25.81	25.62	-0.74
Overall	Exports	151.75	189.93	25.16
	Imports	157.35	235.11	49.47
	Trade Balance	-5.62	-45.18	-125.34

Central Bank Outlook

Rate hikes and its impact:

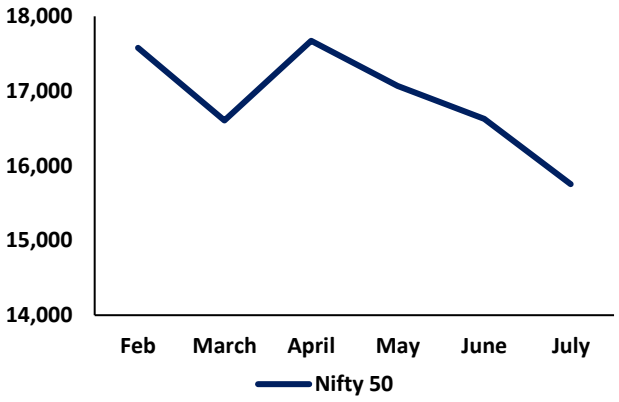
The current repo, bank and reverse repo rates are 4.90%, 5.15%, 3.35% respectively. RBI increased key policy rate by 50 basis points to control prices from 4.40%. It signaled continued monetary tightening to combat inflation, which is anticipated to remain above the legally permitted upper tolerance level for the fiscal year. The RBI promised that there would be adequate liquidity to support company loans. Despite expectations that it would be increased from its current level of 4.5%, the cash reserve ratio (CRR) was left unaltered. The central bank had received a request from Indian lenders not to raise CRR further.

INDIAN EQUITY MARKET

Performance of Stock Market

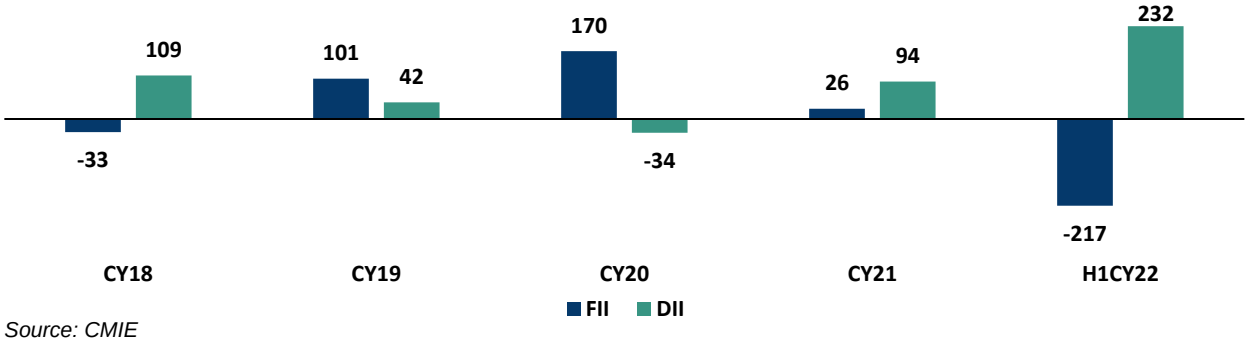
Indian stocks have shown a downward trajectory this year. In the first 6 months of this year, Sensex lost around 7% due to inflationary pressure and tremendous hike in interest rate by central banks around the world. India along with global markets crashed in March 2022 due to panic amidst the Russia-Ukraine war and spikes in crude oil prices. Market began recovery in May but the bloodbath continued from June and the stocks are hovering back to March 2022 levels. As shown in Exhibit , the rising flow of DII is acting as counterbalancing force against sharp FPI outflows. FPI outflow is more due to rebalancing global portfolios and it is barely indicative of any deviation in India's economic growth story.

Exhibit 11: Performance of Nifty 50 over last 6 months



Source: Google Finance

Exhibit 12: Domestic investors capitalizing on opportunity foregone by Foreign Investors amid risk-off institutional flows in (INR crore)

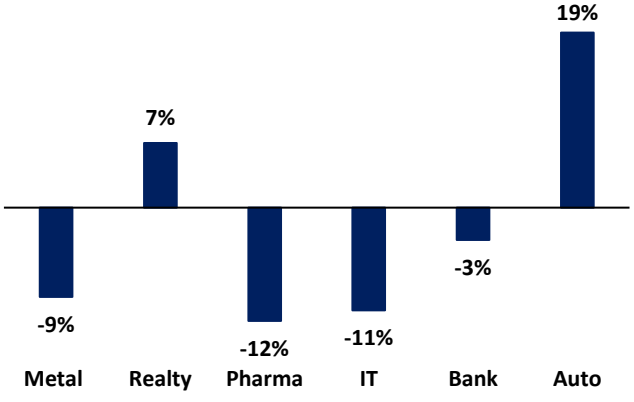


Source: CMIE

Sectoral Indices

Considering last year's performance, Auto and Realty sectors emerged as the top performers, attributing to recovery from covid and no rate hikes by RBI promoting an environment conducive to investment. Pharma & healthcare sectors, on the other hand had poor performance due to continuous new variants of covid creating a negative sentiment pertaining to the sectors. IT stocks continues to fall as fear of recession and rising inflation surround the global markets.

Exhibit 13: Performance of major sectors for last 1-year



Source: NSE

Exhibit 14: Top performers & underperformers (6months)

Sectors	Outperformers	Underperformers
Auto	Mahindra & Mahindra (33.06%)	Bharat Forge (-2.55%)
Bank	Bank of Baroda (11.16%)	IDFC First Bank (-1.33%)
IT	Tata Elxsi (27.70%)	HCL Tech (-2.2%)
Pharma	Cipla (4.83%)	Glenmark Pharma (-2.26%)
Metal	Coal India (17.39%)	JSPL (-4.3%)

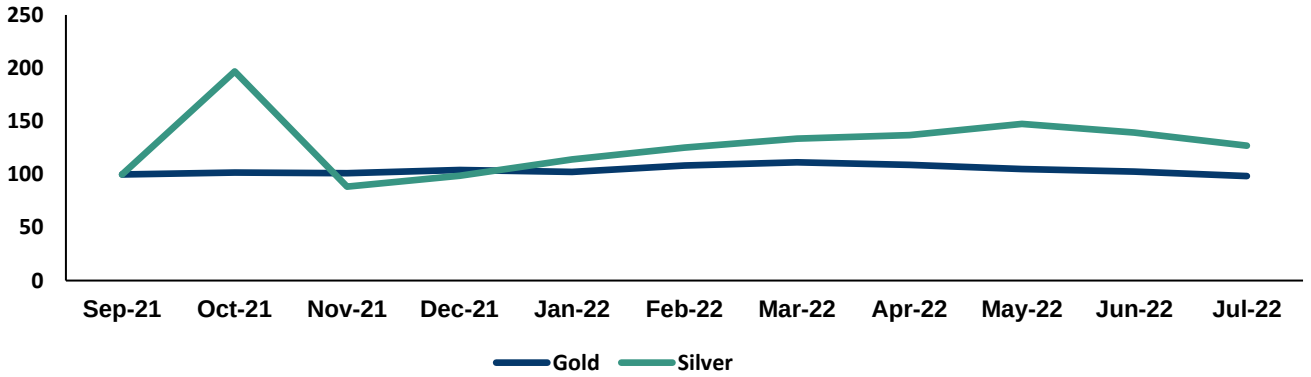
Source: NSE

COMMODITIES

The 'yellow metal' saw a price hike in India in the first 3 months of 2022. It stood at ₹ 51,243 in June as compared to Rs 48,243 in January, a 6.5% increase. This surge in gold prices took place in spite of the decline in Nifty 50 of around 12% in the same time period due to the uncertain global conditions, being used as an inflation hedge. The depreciation of Indian rupee with respect to the US Dollar, increase in the US Fed rate, the Ukraine-Russia war and historically high rates of inflation seem to be the reasons for such trends. The US central bank trimming on federal reserves may put a stop on this price hike. However, with RBI expected to hike rates, the volatility in the market is expected to persist.

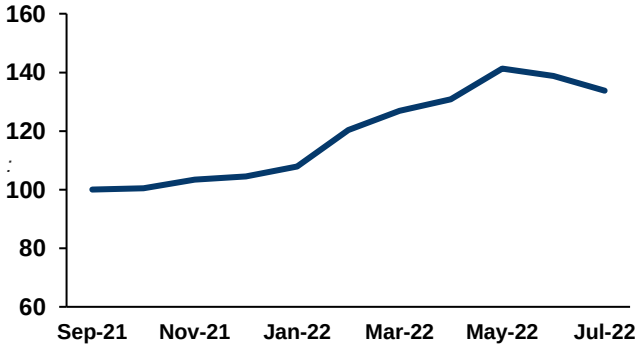
Silver prices stood at $18.89/t oz in July as compared to $23.16/t oz in January 2022. This was due to the surge in cases of Covid-19 in China and the efforts by government to bring high-level inflation under control. Silver prices in India have also been affected by international prices, foreign exchange rate and policies by the Fed. Silver is expected to trade at $18.93/t oz by the end of this quarter and $17.87 in 12 months. The trend is expected to remain negative as the currency has managed to maintain pressure over it and Fed is expected to take further measures to control the rising inflation.

Exhibit 15: Gold prices and silver prices for the past year (price based to 100)



Source: investing.com, MCX

Exhibit 16: Crude Oil for the past year (price based to 100)



Source: investing.com, MCX

In May, brent crude oil future rose reaching $124 a barrel-mark, the highest since 2008. This happened due to the increase in Russia-Ukraine conflict leading to fears of lower supply of oil. The effort to reduce prices by reducing the crude reserves also failed to bring speculations down. In July, the prices have come down to under $96 a barrel, due to introduction of a new variant of Covid-19 in China(top crude oil importer),fears of lockdown, increase in dollar and fear of a global economic slowdown as central banks increase rates to combat inflation. According to OPEC, global oil demand will rise in 2023 but at a pace lesser than 2022.

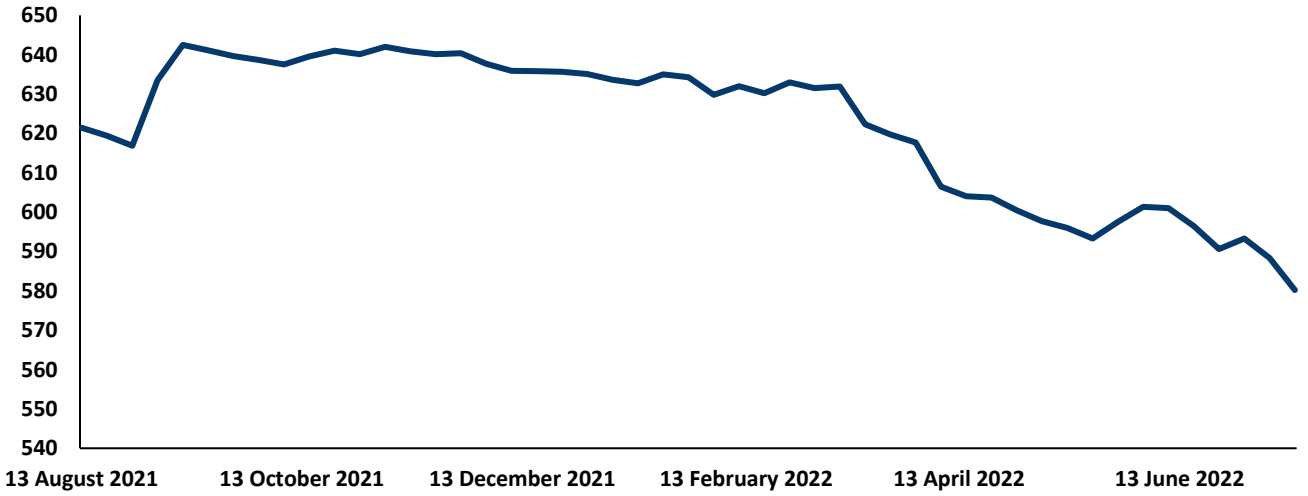
India meets 80% of its crude oil demand through imports. The rising crude oil prices have led the government to promote the production of usage of a bio-fuel Ethanol. In India, the ethanol market stood at $2805.38 million dollars in 2021 at is expected to grow at a CAGR of 12.68%. Currently, ethanol blending with petrol is 8.5% from 2.07% in 2016-17. The government aims to increase it to 10% by 2022 and 20% by 2025. The demand expansion of India has been due to government policies and its usage in making sanitisers, According to ISMA, India has the capacity to make 722 crore litres of ethanol and it will increase to 1,500 crore litres by end of 2025.

FOREX

Foreign Exchange Reserve

India's foreign exchange reserves were down to INR 572.71 bn. It was because of a dip in foreign currency assets (FCAs). RBI has stepped up intervention in the foreign exchange market. RBI has been selling dollars to restrain extreme volatility in the exchange rate and to contain runaway depreciation in the rupee. In addition, foreign exchange reserves may face challenges as 43% of the short term debt will mature this FY as per RBI's latest data on India's external debt as of March 2022 as it comprises of 44% of total forex reserves.

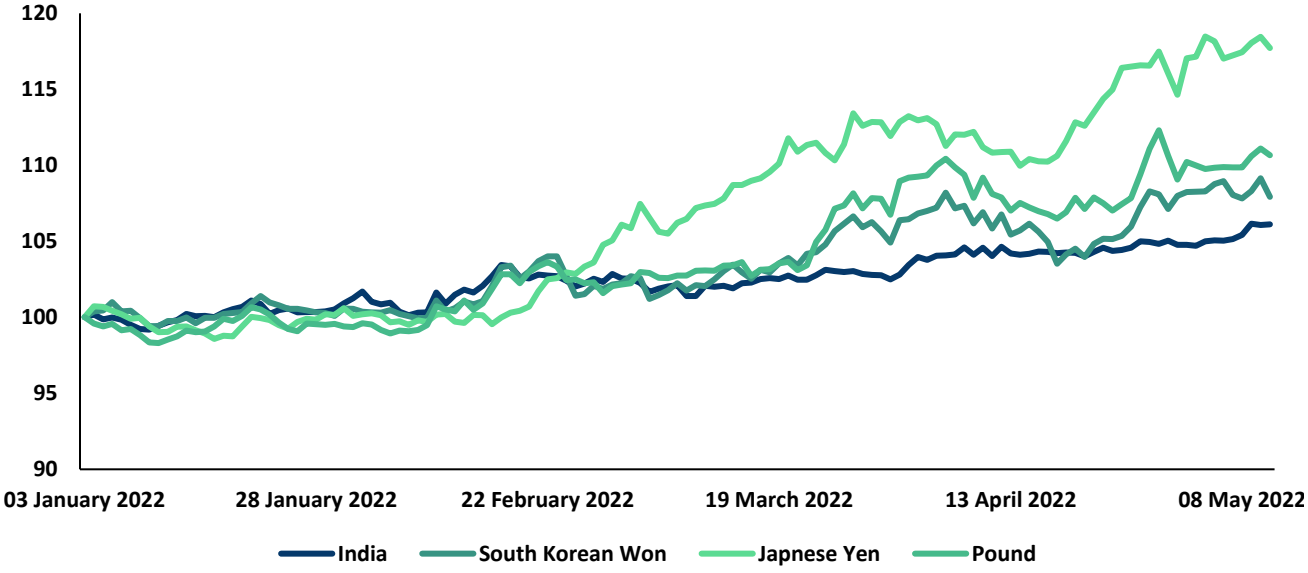
Exhibit 17: RBI shifted its stance from accumulator to a spender, forex reserves reduced marginally



Source: Reserve Bank of India

Indian rupee has depreciated least against dollar in comparison to other currencies from developed and developing nations like UK, South Korea, Japan and other emerging economies. The better performance of Indian currency reflects India's prudent management of the challenges of inflation, supply chain disruption and covid-19 pandemic. RBI liberalized norms to boost its foreign inflows to address the weakening of rupee.

Exhibit 18: Indian Rupee has depreciated the least against US dollar in 2022 among other currencies of developing and developed nations



Source: www.investing.com

FOREX

USD INR

USD has appreciated by 7.05% YTD against INR. The first half of 2022 was all about equity markets readjusting to higher inflation and interest rate environment across the globe. In the month of June, commodities prices started cooling off. If this trend continues, it will reduce pressure on central banks to increase rates. Since the start of 2022, there have been a net negative figure for FPI investments. While In January 2022, FPI withdrew ₹28,526 crores, it surged up to 75.5% to ₹50,068 crores in March 2022. This constant outflow of FPI's funds from the Indian markets has been one of the key reasons for both the plunging of equity markets and a depreciation of the rupee against the US dollar. The strengthening of the US dollar index has also led to fall in rupee. The dollar index has been on a run and is currently trading around the highest level since December 2002. Although, the RBI has been relentlessly trying to curb the fall which is evident from the falling forex reserves.

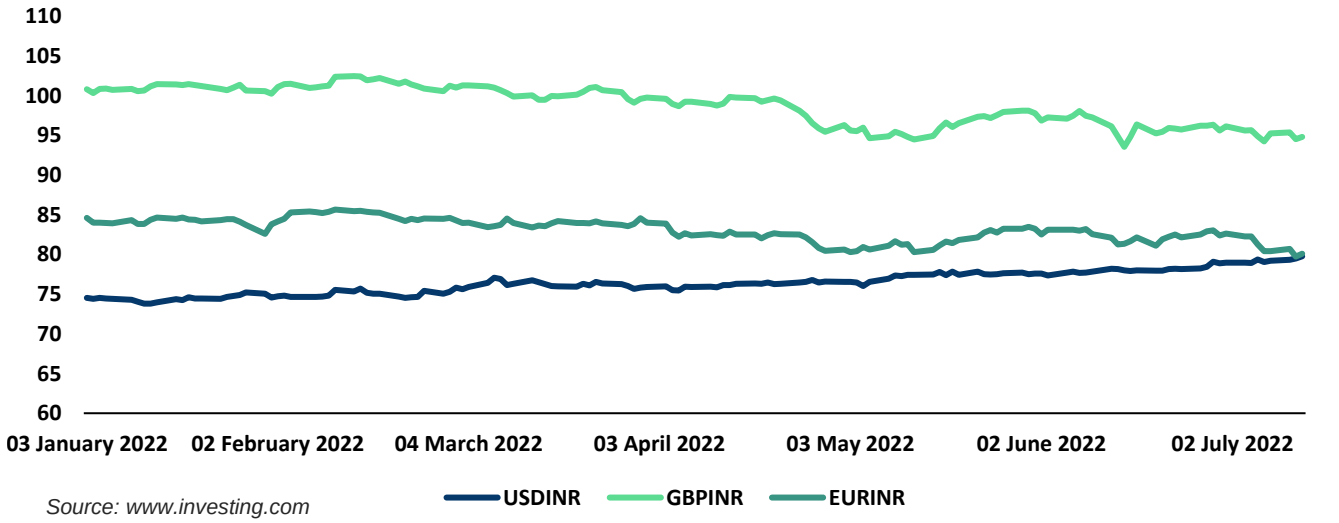
EUR INR

Euro has depreciated by 5.35% YTD against INR. Rate differentials and recession fears have been a massive drag on Euro of late, as the divergence in policy paths grows more apparent by the day. The conflict in Ukraine continues to impede any progress on reducing inflation, as food and energy costs continue to soar. To make matters worse, the Nord Stream 1 pipeline has been shut off for maintenance, and fears have grown over whether flows will even resume when work on the pipeline completes. As Europe broadly considers energy rationing amid this unique and historic situation, unrest continues to grow.

GBP INR

GBP has depreciated by 5.96% YTD against INR. UK's economy expanded by 0.5% on a monthly basis in May. This print followed April's contraction of 0.3% and surpassed the market expectation of 0%. Additionally, Industrial Production and Manufacturing Production grew by 0.9% and 1.4%, respectively, with both of those prints coming in stronger than analysts' estimates. Nevertheless, the positive impact of these data on the British pound remained short-lived. There were signs that demand has slowed. As a result, fears of a recession are once again under the spotlight. An economic setback seems inevitable in the US, and most major economies are still battling to recover from the early stages of the pandemic. The combination of slow growth, debt and high inflation would be a very tricky situation for the central bank to manage in the coming months.

Exhibit 19: USD/INR, GBP/INR and EUR/INR price movements



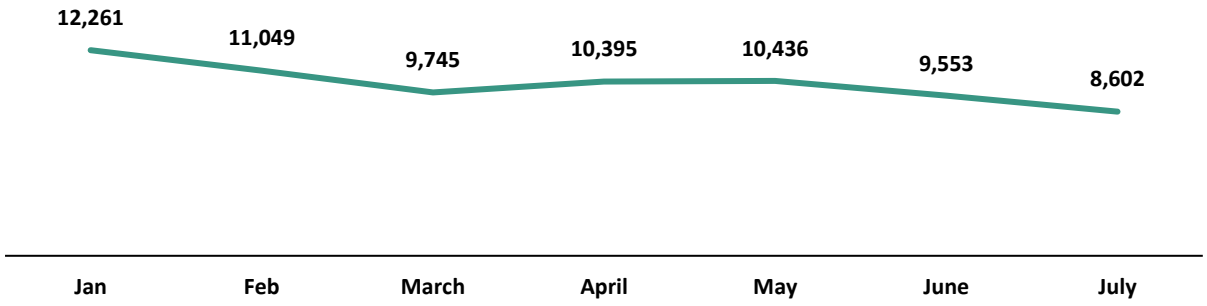
Source: www.investing.com

INITIAL PUBLIC OFFERINGS (IPO)

The excellent IPO activity from March to July 2022 attests for the immense growth potential of India. In the period aforementioned, 34 firms went public, compared to 19 in the same period in FY21. The IPOs had a total issue size of 33,590 crores. This increased total is the outcome of LIC's largest IPO in India in the month of May 2022, with a total issue size of 21,000 crore. If the amount of LIC's first public offering (IPO) is subtracted from the total issue size, then the overall issue size has plummeted. The reasons cited for this were rising geopolitical tensions, stock market volatility, market price corrections of overpriced equities in recent IPOs, the impact of inflation and rising interest rate rises, and the continued threat of the Covid-19 epidemic.

Many stocks that went public this year have seen their values fall. LIC experienced a significant drop in the issue price. As of July 27th, 2022, the price had dropped by 29% compared to the issue price at the IPO. Firms have been more cautious in introducing their IPO values after the massive drop observed in companies such as Paytm-parent One 97 Communications, PolicyBazaar, and Zomato in 2021, but they remain optimistic about the possibilities of raising capital from the market. They have also been mindful of how they time their IPOs, which is why several of them are in the process of launching their IPOs.

Exhibit 20: The declining performance of S&P BSE IPO Index (CY22)



Source: BSE

Exhibit 21: Major IPOs of FY22 and their performance

Company Name	Date of Listing	Issue Price (Rs)	Listed Price (Rs)	Price as on 30-06-22	Gain/Loss
Aether Industries Ltd	03-06-22	642 .00	701.00	780.05	21.50%
eMundhra Ltd	01-06-22	256.00	271.00	252.10	-1.52%
Delhivery Ltd	24-05-22	487.00	493.00	506.95	4.10%
Prudent Corp Advisory Services Ltd	20-05-22	630.00	660.00	498.45	-20.88%
LIC	17-05-22	949.00	867.00	673.60	-29.02%
Campus Activewear Ltd	09-05-22	292.00	355.00	325.15	11.34%

Source: Moneycontrol

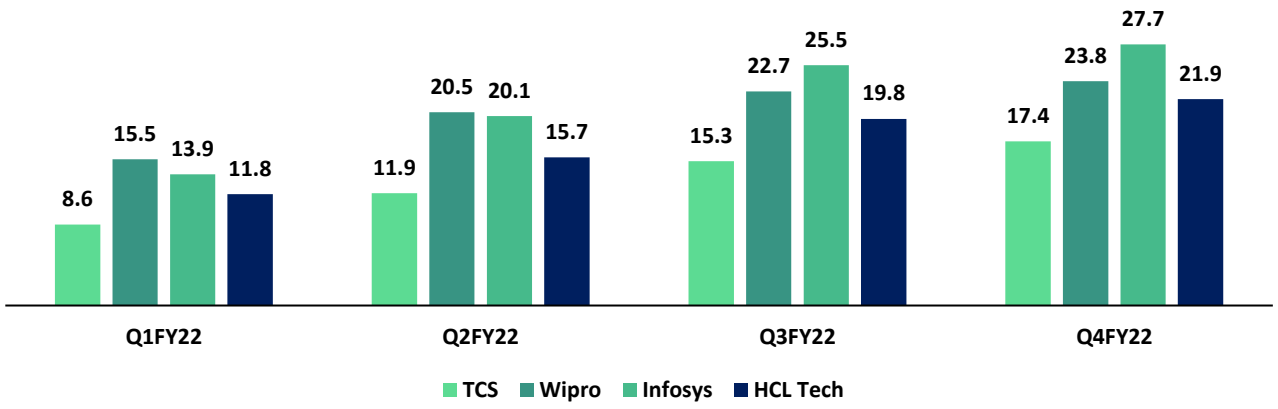
INDUSTRY OUTLOOK

IT Industry

The IT services company has achieved total revenue of $227 Bn for FY22 and yet has seen a drastic slump in market value since the start of 2022. The NIFTY IT index is down by nearly 30% YTD despite a 19% revenue growth for the IT services industry in FY22. In fact, a further slump in revenue growth to 12 ~ 13% is being anticipated for FY23. This could be attributed to the inflationary headwinds in the regions of the United States and the European Union which could tighten the IT expenditure of companies in these regions (These regions contribute 85% of the sector's revenue). Ever-increasing attrition rates and giants like TCS, and Infosys missing to match the earnings estimate of analysts has reduced the confidence of retail investors in the sector due to which the P/E ratio of NIFTY IT has fallen by 36% YTD.

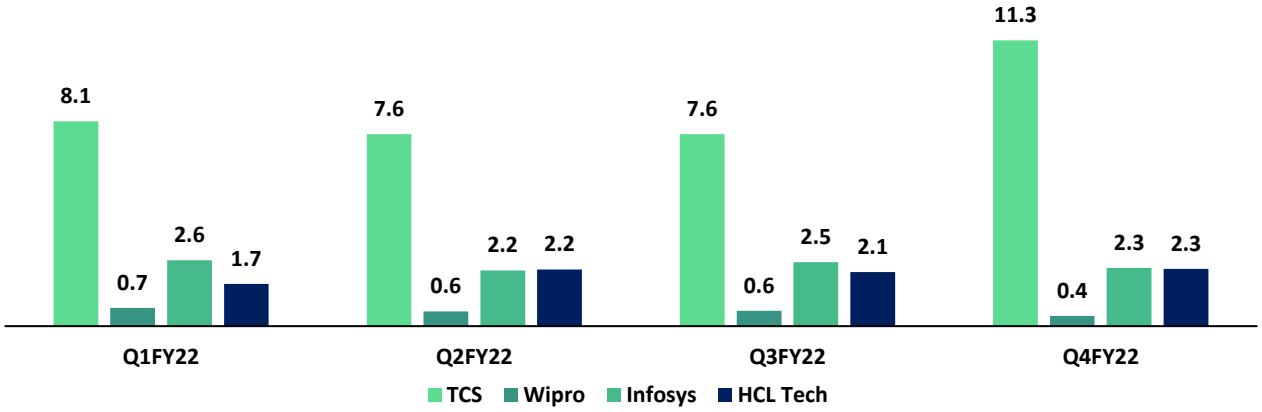
The drastic 7.3% fall of Indian Rupee against the dollar since the beginning of 2022 should have been a good news for the Indian IT companies, but this has been offset by the increasing strength of dollar against currencies like euro and pounds, as roughly 30% ~ 40% of the Indian IT industry revenue comes from European countries where these currencies are dominant. This leads to a negative impact on the overall dollar revenue of the companies.

Exhibit 22: IT companies continue to see an increase in attrition with TCS having the least rate in the industry (Attrition in %)



Source: Samriddhi Research, Company Data

Exhibit 23: IT companies witnessed somewhat volatile moment in TCV during FY22, TCS achieved its highest ever book value of $ 11.3B in Q4 FY22 (TCV in Billion USD)



Source: Samriddhi Research, Company Data

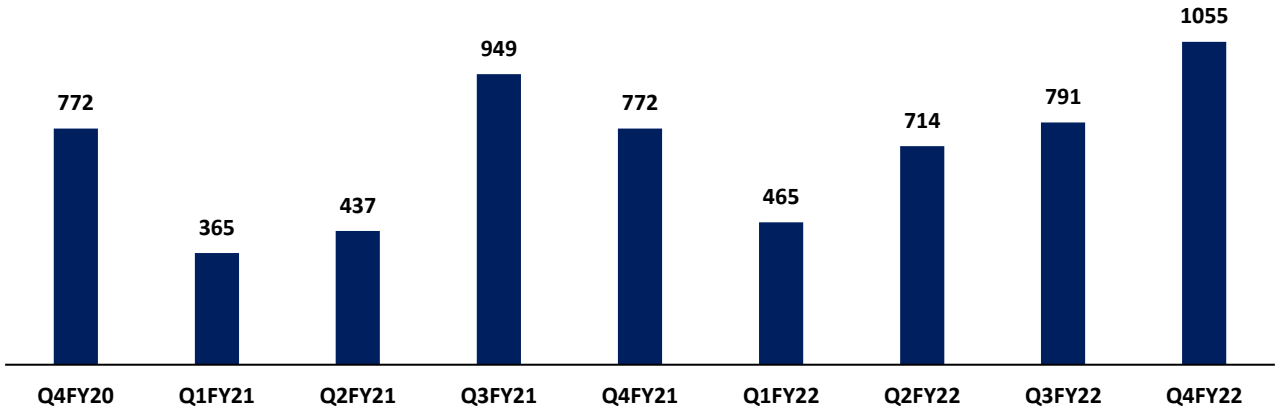
INDUSTRY OUTLOOK

Capital Goods Industry

About 12% of the entire manufacturing activity happening in India is contributed by the Capital Goods industry which is roughly about 2% of the India's GDP. In the period of last 5 years, S&P BSE – Capital Goods Index had shown nominal growth till FY21 but since the beginning of FY22, the index has given a run up of 32.5% till date. This can be attributed to the consensus of investors on long-term vision of several initiatives such as "PM Gati Shakti National Master Plan" and others taken by the government to boost the infrastructure of the country.

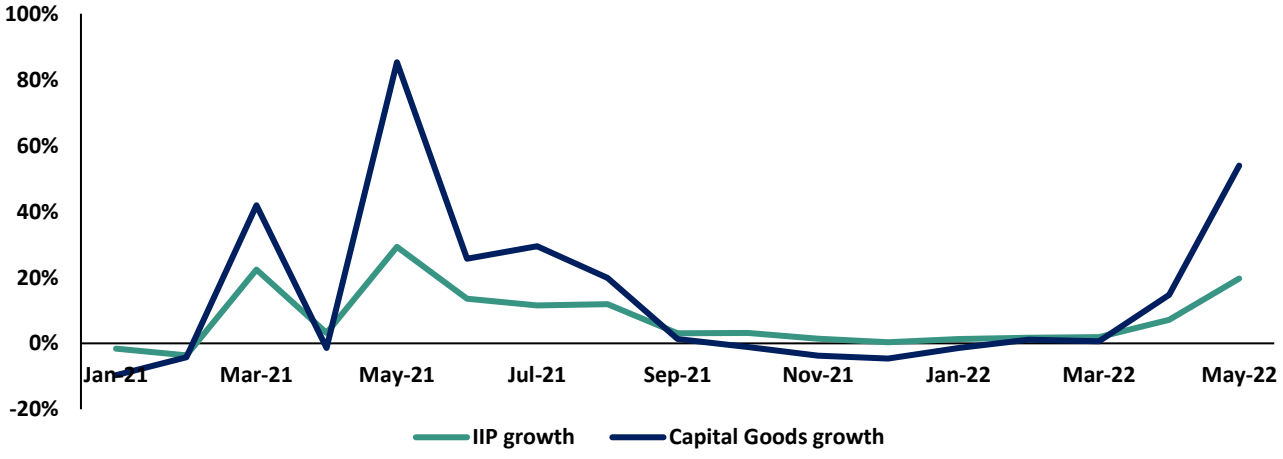
On the contrary, the index has contracted by 2.41% YTD due to some short-term problems like the margins being impacted by high commodity prices, high crude oil prices, high freight costs, supply chain disruption etc. Due to which companies could have sustained margin pressure. Also inflation is likely to effect companies profitability, though partially contained by price hikes, price-escalation clauses in variable price contracts and cost savings measures. Heavy power outages in April – May has affected the revenues of electrical equipment manufacturing companies, but as soon as this problem stops to persist the existing demand should more than make up for the supply. However, the government's capex cycle continues to be robust and private capex cycle is expected to pick up soon further supporting sector's growth.

Exhibit 24: Ordering activity inflows for companies continues to see momentum (In INR Bn)



Source: Samriddhi Research, Company Data

Exhibit 25: Any significant uptick in IIP growth results in huge capital goods growth and the similar trend follows during downtick in IIP growth (IIP growth & Capital goods growth in %)



Source: Samriddhi Research, MOSPI

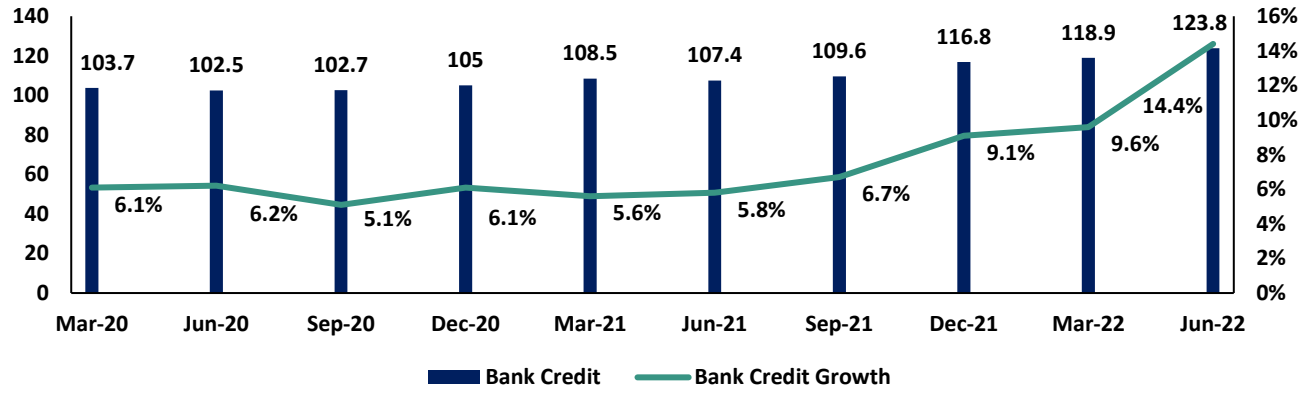
INDUSTRY OUTLOOK

BFSI Industry

The BFSI sector in India has experienced tremendous expansion and transition as a result of the country's increasing economy and technological advancements. The expansion of this industry has been fuelled by rising per capita income, the introduction of new financial avenues and products, and increased awareness of investment needs and financial products. The advent of UPI by NPCI was the most significant breakthrough in the industry. According to NPCI data, UPI processed 504 crore transactions worth Rs. 888169 crore up to March 29, 2022 the transaction value clearly demonstrates the industry's digital transformation. Banks have reported healthy Q1FY23 performance with improvement in loan growth, stable to improving margins and continued improvement in asset quality resulting in lower core credit cost.

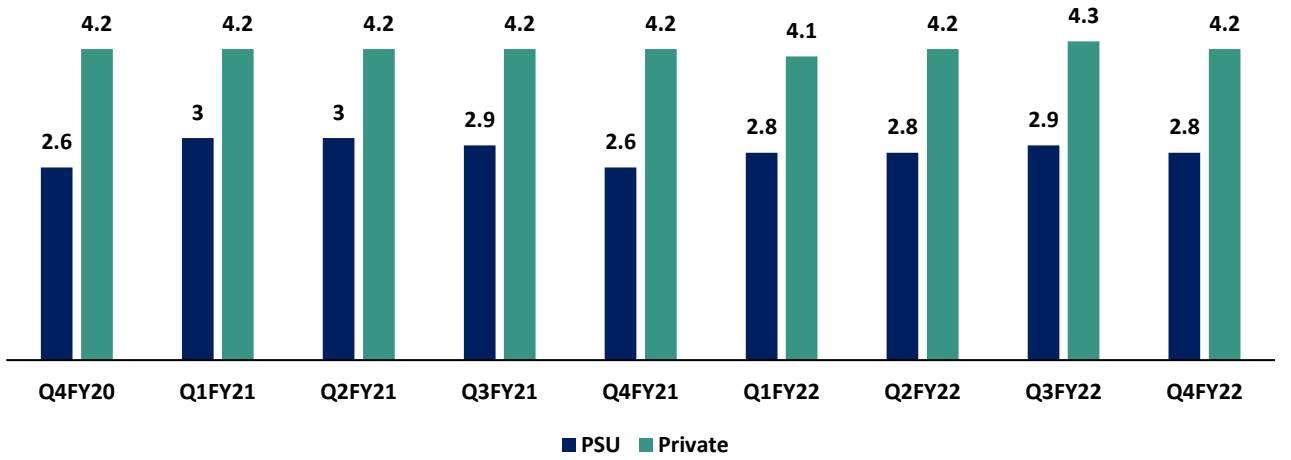
- **Digital lending -** The evolution in the lending space continues in India with Fintech companies being aggressively growth oriented in the underpenetrated market. The major factor contributing to increase in digital lending is the increasing usage of mobile phones in the country which has increased from 34 million to 844.84 million. The other factors due to which the growth is expected is the increasing internet penetration, credit flexibility due to increasing convenience provided by increasing competitors.

Exhibit 26: Bank credit growth remains on strong footing (y-o-y % growth, Bank Credit in Rs. Lakh crore)



Source: Samriddhi Research, Company Data

Exhibit 27: Net Interest Margins to exhibit a positive bias, supported by raising interest rates and healthy prick up in business growth (Margins in %)



Source: Samriddhi Research, Company Data

INDUSTRY OUTLOOK

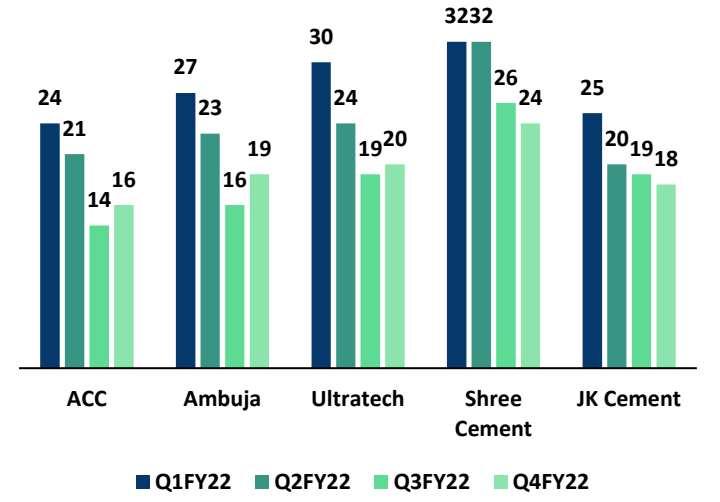
Cement Industry

India is the 2nd largest cement producer in the world and accounts for over 7% of the global installed capacity. The global economic revival post Covid caused an increase in the demand of commodities. The price rise was further accentuated by the Russia-Ukraine war. The biggest components of cement companies' expenditure account, power and transportation costs saw a sharp spike due to increase in the prices of pet coke, international coal and diesel. Cement companies took multiple price hikes during FY22 but the hikes were not in proportion to the rising costs. As a result, all the major cement companies in India posted weak EBITDA margins.

- **Peaking out of raw material prices** – In coming quarters the cement industry is expected to cope-up with the challenges it faced. There is an improvement in demand in June 2022 due to the pre-monsoon push and pet coke prices fell 10% MoM in June 2022 after peaking in Q4FY22. With global tightening in liquidity, the prices of coal and diesel are expected to fall soon.

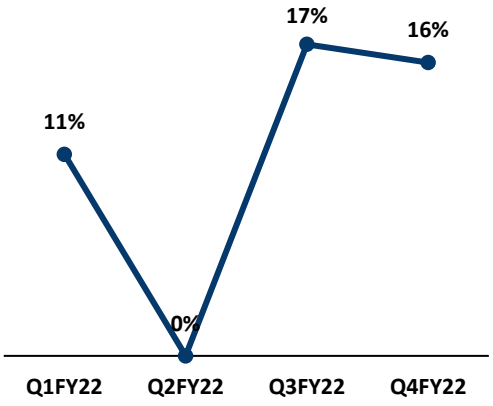
- **Price hikes -** The current average all-India cement prices are up by roughly 7% QoQ, which will translate into an increase from INR 15 per 50 kg bag. The current average all-India price of INR 350 per 50 kg bag would largely mitigate the cost pressures.

Exhibit 28: EBITDA Margins (%) of top 5 companies in terms of capacity



Source: Company data

Exhibit 29: Rise in power and transportation costs of top 5 companies by capacity



Source: Company data

- **Robust housing demand -** Although the reversal in the interest rate cycle has affected affordability, residential property prices are witnessing appreciation in India supported by robust uptake in sales. Housing prices have increased YoY during first half of 2022 across all markets for the first time since 2015. The residential segment saw strong growth in sales volumes/value in FY22 with top eight listed developers reporting ~50% growth in sales value at INR 45,766 crore. The overall momentum in real estate will boost earnings of cement companies.

- **Merger of titans -** The cement industry also witnessed its biggest consolidation. The Adani Group and Holcim signed a binding agreement for the sale of Holcim's India business. Holcim held 63% stake in Ambuja Cements. Ambuja Cements holds 50% stake in ACC while Holcim has a direct stake of 4.5% The total deal size is around $10.5 billion.

INDUSTRY OUTLOOK

Chemical Industry

A consistent value creator, the Indian chemical industry is an attractive hub of opportunities and worldwide trends could create new avenues for Indian companies. The input costs started to weigh on the chemical industry in FY22. Although the expected sales and profit for major chemical companies in Q1FY23 are expected to grow YoY, the QoQ demand has weakened slightly, especially in discretionary end-user industries like paint due to extreme inflation witnessed over the last quarters. The major reasons for such pressures are rising prices of crude oil and oleochemicals feedstock. Oleochemical feedstock prices were up by around 5-20% QoQ in Q1 FY23 due to Indonesia's ban on palm oil exports.

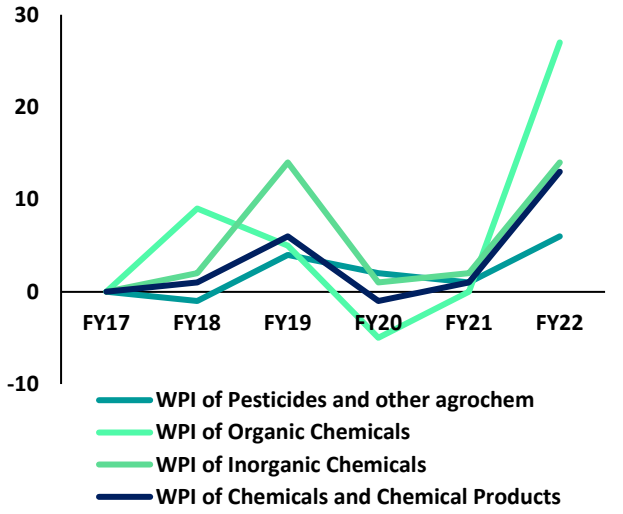
- **Opportunity to increase exports –** The China+1 story has worked for the Indian chemicals industry in the past 5 years. It can gain further momentum as China remains committed to containing the growth of chemical factories due to environmental concerns and MNC's are looking to diversify away from China. China constitutes around 45% of the global chemical industry. Countries want to have two to three suppliers now and many countries are looking at India as a potential player because of India's cost-competitive manufacturing and technological knowledge.

- **Capex cycle by chemical companies to continue** – Chemical companies in India are expected to spend INR 15,000 crore in FY23. A good part of this capex will be for backward integration, import substitution, and capacity expansion to meet the growing demand. Since companies have healthy cash flows, there will be low reliance on incremental debt.

- **Long-term view intact -** Although chemical companies took price hikes, they were not in proportion to the rise in input costs. As a result, the companies had to take a hit on their margins. But this prevented their revenues and volumes from slowing down. The cost pressure is expected to continue in the FY23 but the strong domestic and global demand for chemicals manufactured in India along with the planned capex will ensure that margins are restored back to pre-Covid levels.

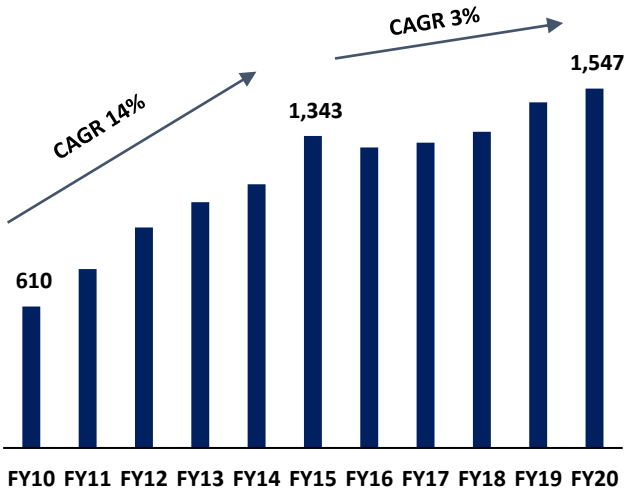
- **Robust demand for Specialty Chemicals -** Companies are expanding capacity to cater to rising demand of speciality chemicals from domestic and overseas. Specialty revenue has grown ~4x in the last 3 years and with the continuous capex, this segment's revenue is expected grow >2x from the current level. As global companies are trying to de-risk their supply chain from China, India has immense growth prospects in this industry.

Exhibit 30: Sharp spike observed in FY22 in WPI of different chemical groups



Source: Statista

Exhibit 31: Stagnation of chemical sales in China (in billion Euros)



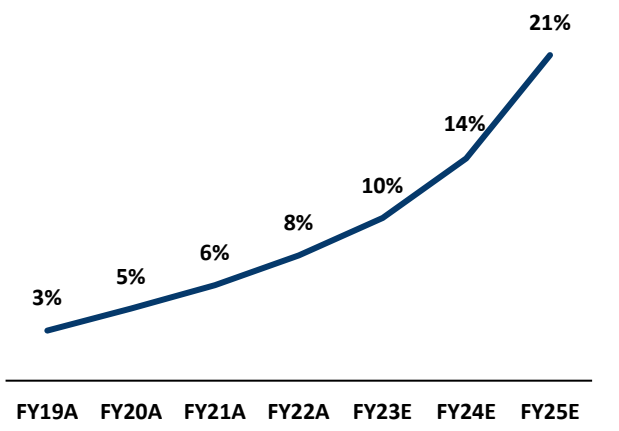
Source: Statista

INDUSTRY OUTLOOK

FMCG Industry

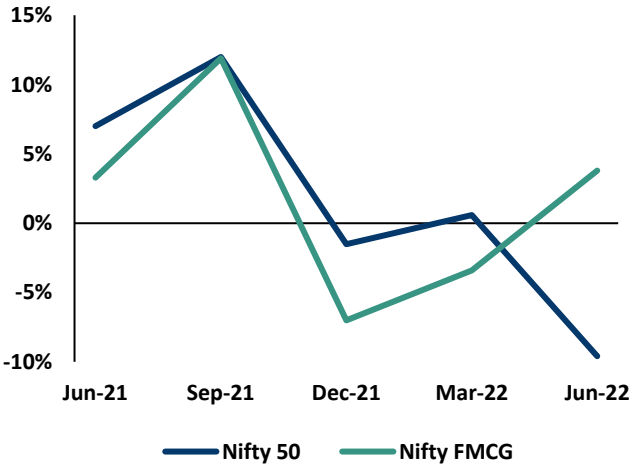
The FMCG market in India is projected to grow at a CAGR of 14.9% to US$ 220b by 2025, from US$ 110b in 2020. The primary growth factors for the consumer market are a rise in rural consumption, a rise in awareness, better access, online sales channels and lifestyle changes. In continuation from the previous year, macroeconomic indices continue to influence the consumption habits of Indian consumers, who are feeling the effects of the price increase in the food and essential segments.

Exhibit 32: Robust growth in Online FMCG market size in D2C sector



Source: Statista

Exhibit 33: Nifty FMCG vs Nifty 50 Quarterly Returns performance



Source: NSE

- **Declining demand in rural region:** The demand for fast-moving consumer goods in rural areas slowed down for the third consecutive quarter, with the volume slipping to 5.3 percent in the January-March period. The decline was the steepest in the last three quarters even as the FMCG industry saw a 6 percent year-on-year growth in the country during Q1 entirely as a result of aggressive price increases. Companies in the sector anticipate a revival in demand by July i.e. the second quarter of FY23.

- **Price hikes:** Due to geopolitical concerns, the domestic FMCG business was once again severely impacted by inflation in Q1FY23, which resulted in subsequent price hikes which eventually impacted volumes. The current quarter would continue to see gross margin contraction, the fall in commodity prices at the fag end of the quarter would release pressure on FMCG companies to take further price hikes, going forward.

- **Rise in commodity prices:** Most commodity prices seem to have peaked out in June 2022 and started cooling off considerably. Palm oil prices have dropped ~30% from the peak but average palm oil prices in Q1FY23 were up 54% against the average of Q1FY22. Similarly, crude oil prices have started cooling off from the peak but still remain above US$100/barrel.

- **Government restrictions:** The government has proactively restricted exports of wheat and sugar, which has cooled down Agri commodity prices as well. However, the whole FMCG sector and also the consumer durable sector offers a good medium-term investment opportunity because overall commodity price correction has occurred in Agri commodities.

- **Positive outlook:** India's FMCG sector is expected to witness double-digit growth (10-12%) in FY23. HUL becomes 1st FMCG company to hit Rs 50,000 crore business for the full year, Q4 net up 9%.

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