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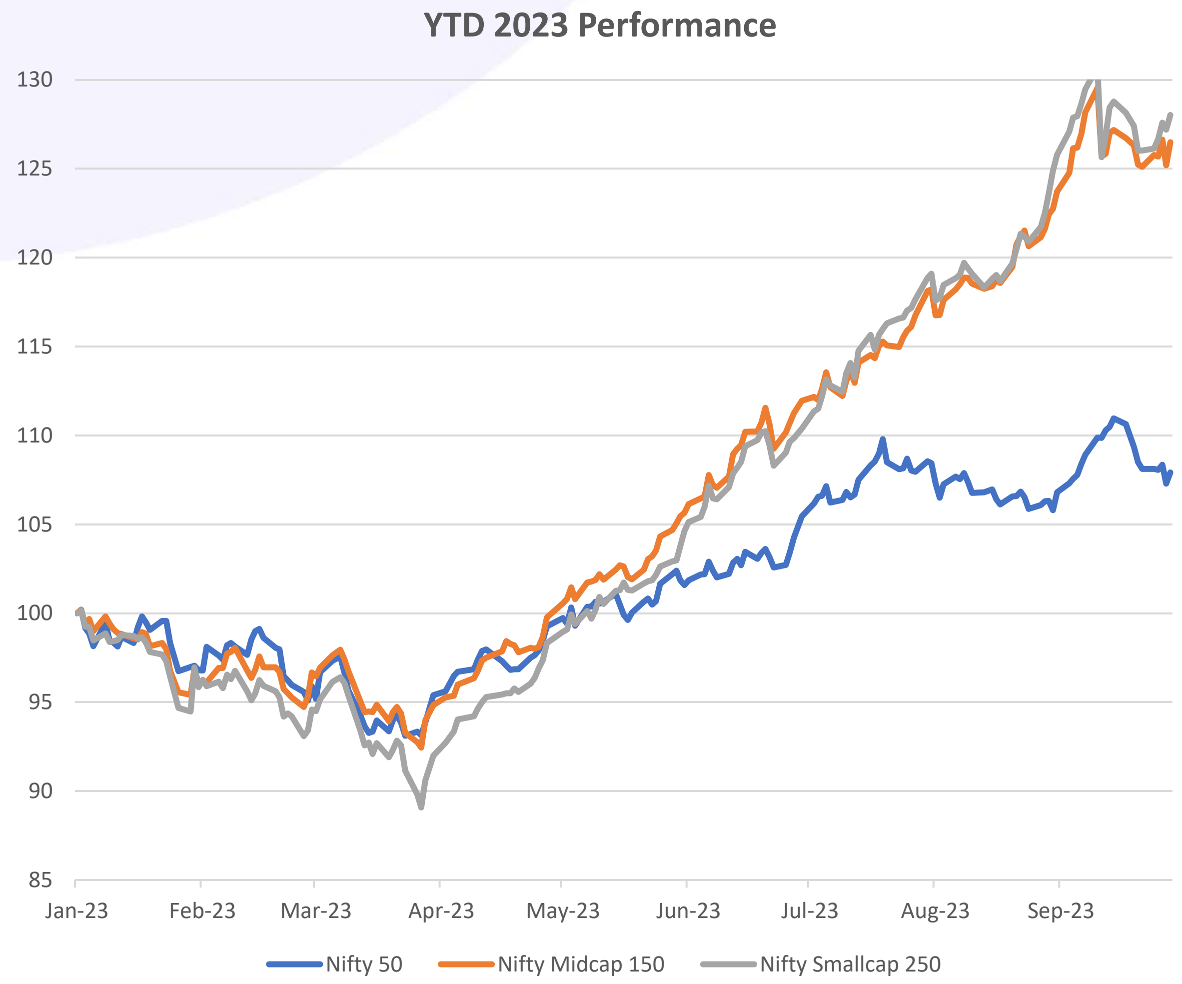
Market Insight - October 2023

Equity Outlook

Indian Equities: 2023 Snapshot



- Nifty 50 Index witnessed correction in August but bounced back in Sept and made all time highs crossing 20000 high mark (Nifty 50) and is now trading 3-4% below an all-time high as flows turned negative in September.

- However, there has been a one-way rally in the mid and small-cap space.

		Absolute		CAGR	
	1 Month	YTD	1 Year	3 Years	5 Years
Largecap	1.40	7.22	12.26	19.82	11.95
Midcap	3.32	27.39	29.92	32.72	19.84
Smallcap	3.58	29.00	32.96	34.77	18.95

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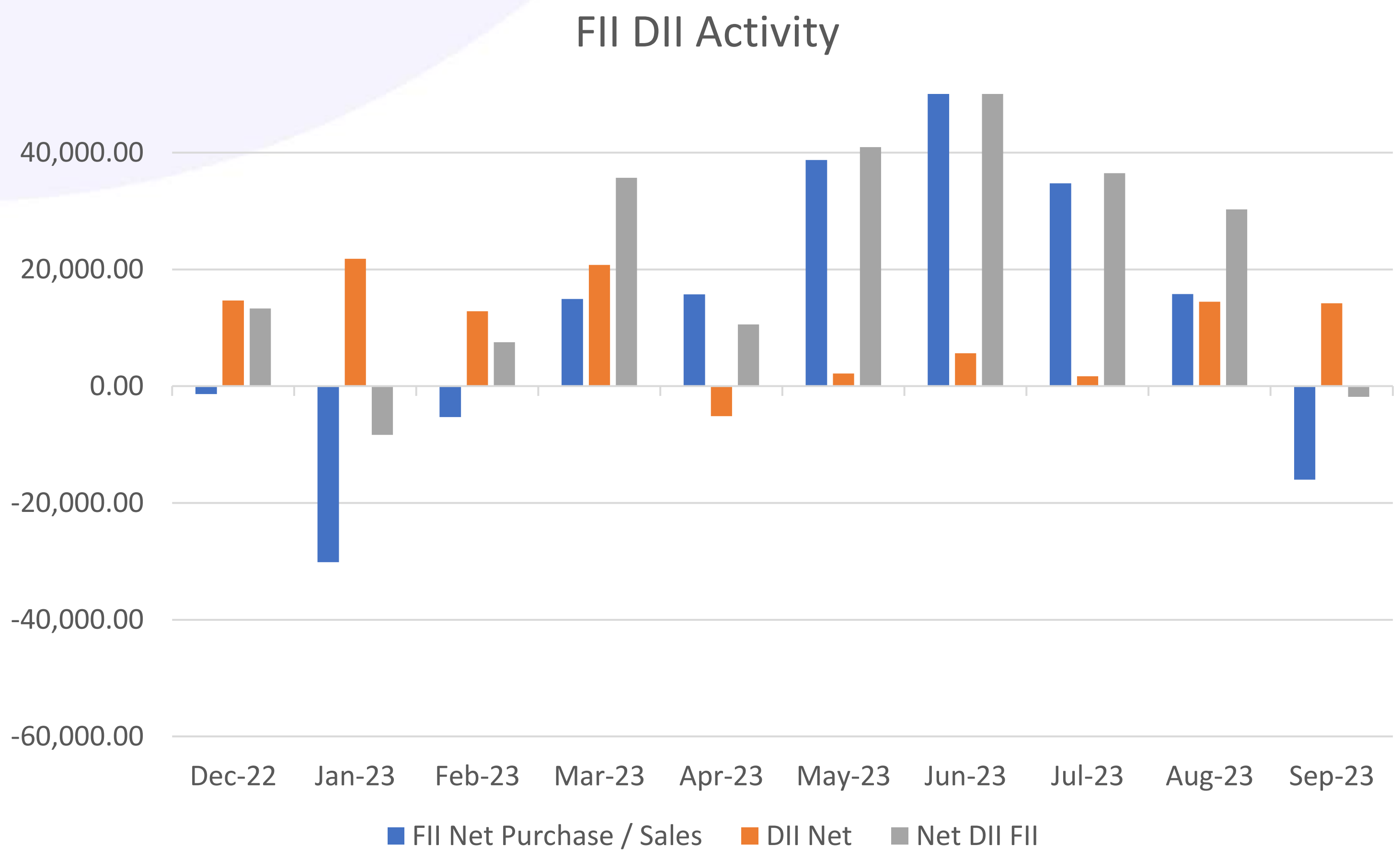
Data as on 30th Sep 2023
Source: https://www.niftyindices.com/reports/historical-data

FII net sellers in Sept after 6 consecutive months of buying



- FIIs were continuously buying in the Indian Equity Markets from March till August but turned net seller in September.
- June 2023 saw highest inflow from FII in last 12 months.
- So far, FIIs have bought nearly Rs. 1.19 lakh crore worth of Indian Equities in this CY.
- Mutual Fund Flows have been very strong (mainly in the last 2 months)
- Flows were highest predominantly in the Small and Midcap category.
- Smallcap Funds alone show inflows are more than 8000 crores in last few months.
- SIP Flows are also very strong as they crossed Rs. 15,000 cr mark for the second consecutive year.

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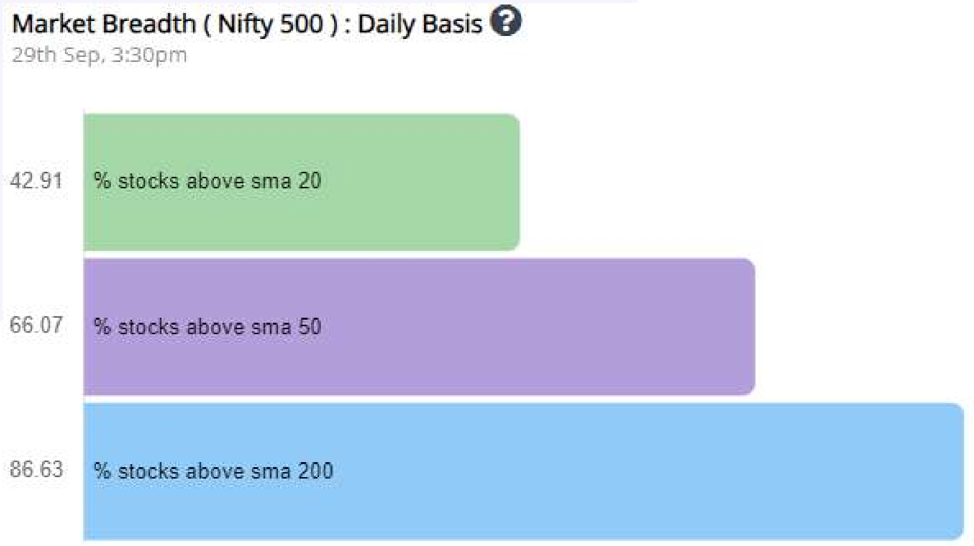
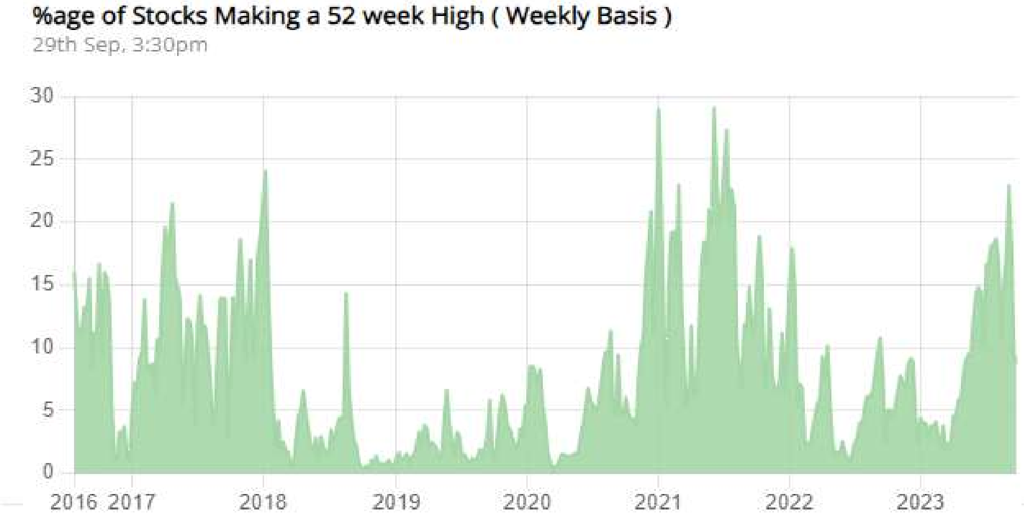
Source: moneycontrol.com

Technical Indicators look strong on Longer Timeframe





Source: Chartink.com

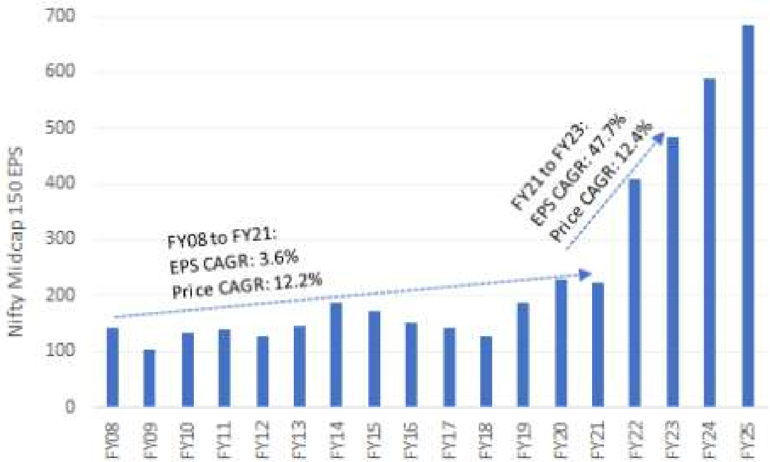
- The bull market that started in 2020 made a top in Oct 2021 near 18600 levels.
- Markets consolidated for nearly two years.
- Recently, in June 2023, Nifty50 index crossed Oct 2021 high. Trading above 50 and 200 DMA.
- Mid cap and Small cap indices have also broken out of their resistance (Oct 2021) levels.
- After crossing 20000 mark in September, Nifty 50 index is going through a small correction (3-4%). But is still technically strong (still above 50-200 DMA)
- Other technical factors such as: no. of stocks making 52-week highs, % of stocks above 50 and 200 DMA also indicate bullishness in the market.
- However, the no. of stocks above 20 DMA has gone down due to the recent correction in the market.

Bull Run Supported by earnings growth

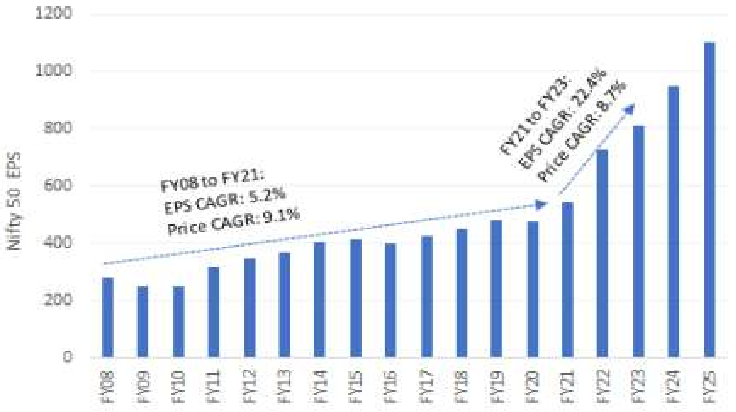
- After a decade of draught in earnings, earnings make a comeback in 2021 in Indian Markets.
- Nifty 50 earnings are almost 2.5x in last two years.
- Last time such earnings growth was seen from 2004-2008 where earnings went up 3-4X during that period.

NIFTY 50 EPS

Sharp growth in Midcap earnings during post-covid phase



Large Cap earnings growth too have returned but at a lower pace than midcap



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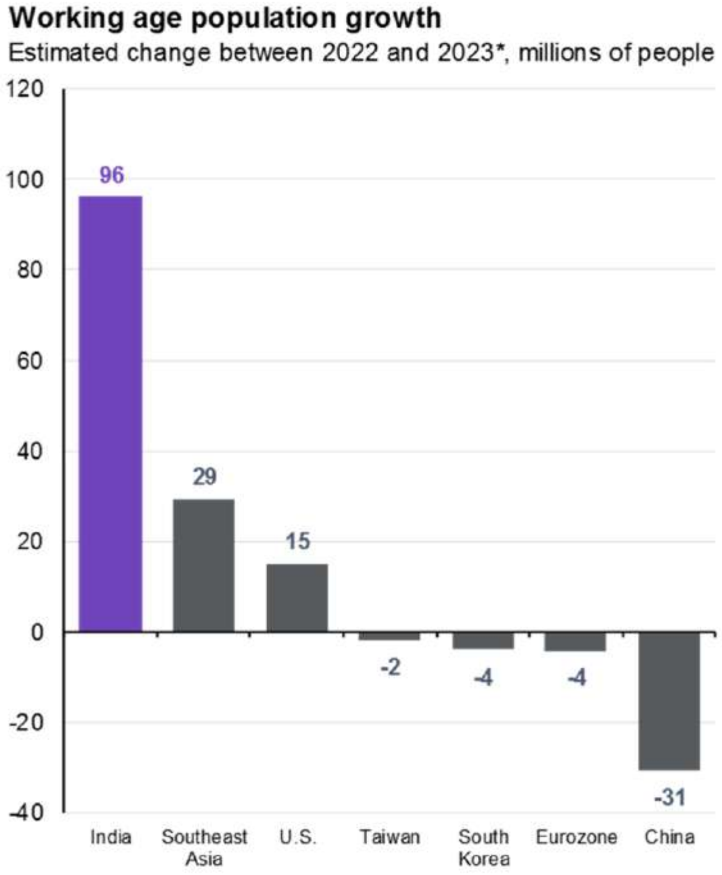
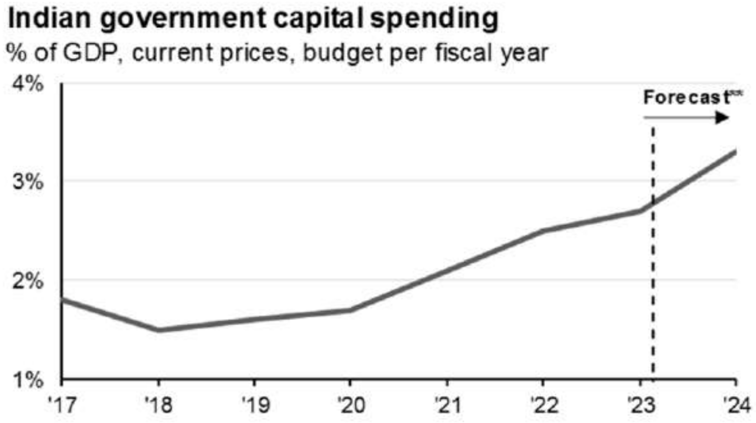
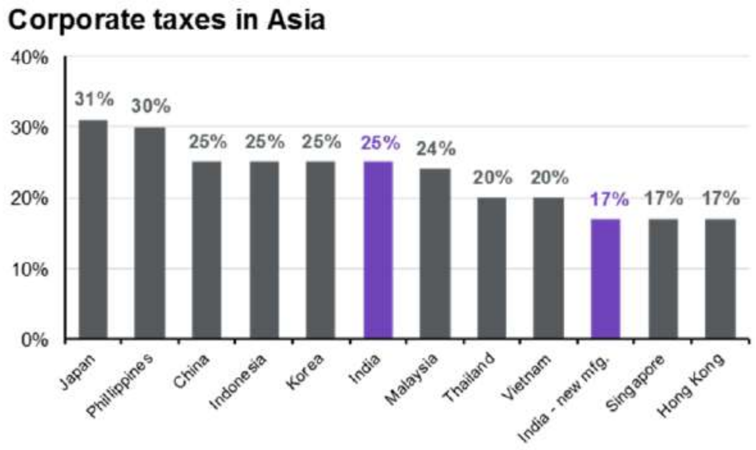
Source: Trendylene

Further, Macros are supporting

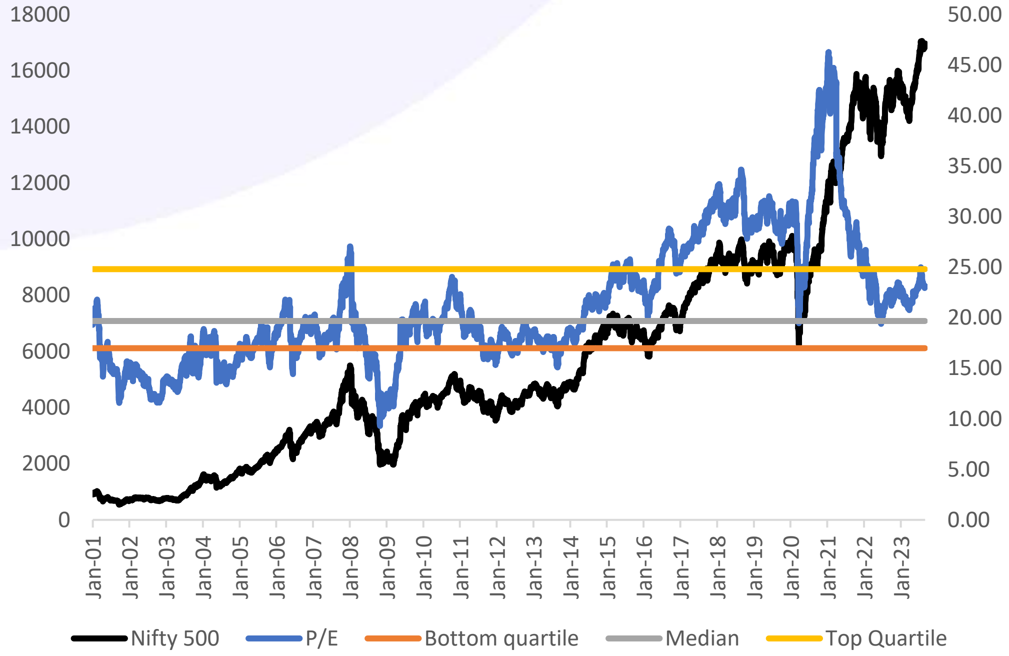
- Working age demographics are very favorable in India relative to other countries and regions.
- Government is investing more in projects that will help the country grow over the long-term.
- India has lowered wages for new manufacturing firms in a move to become more business friendly and encourage firms to relocate there.

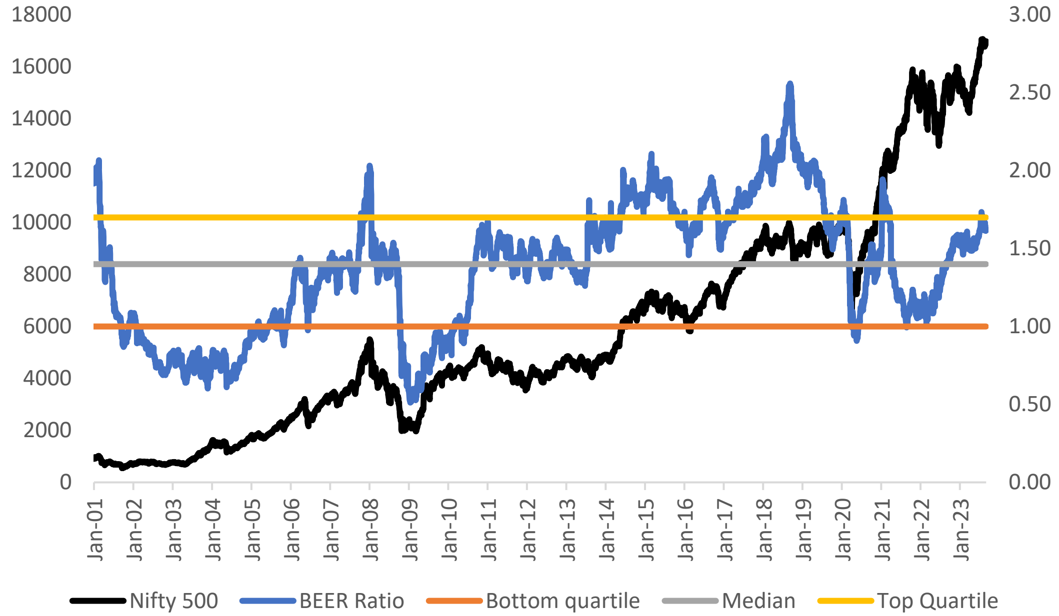






However, Valuations are on a higher side



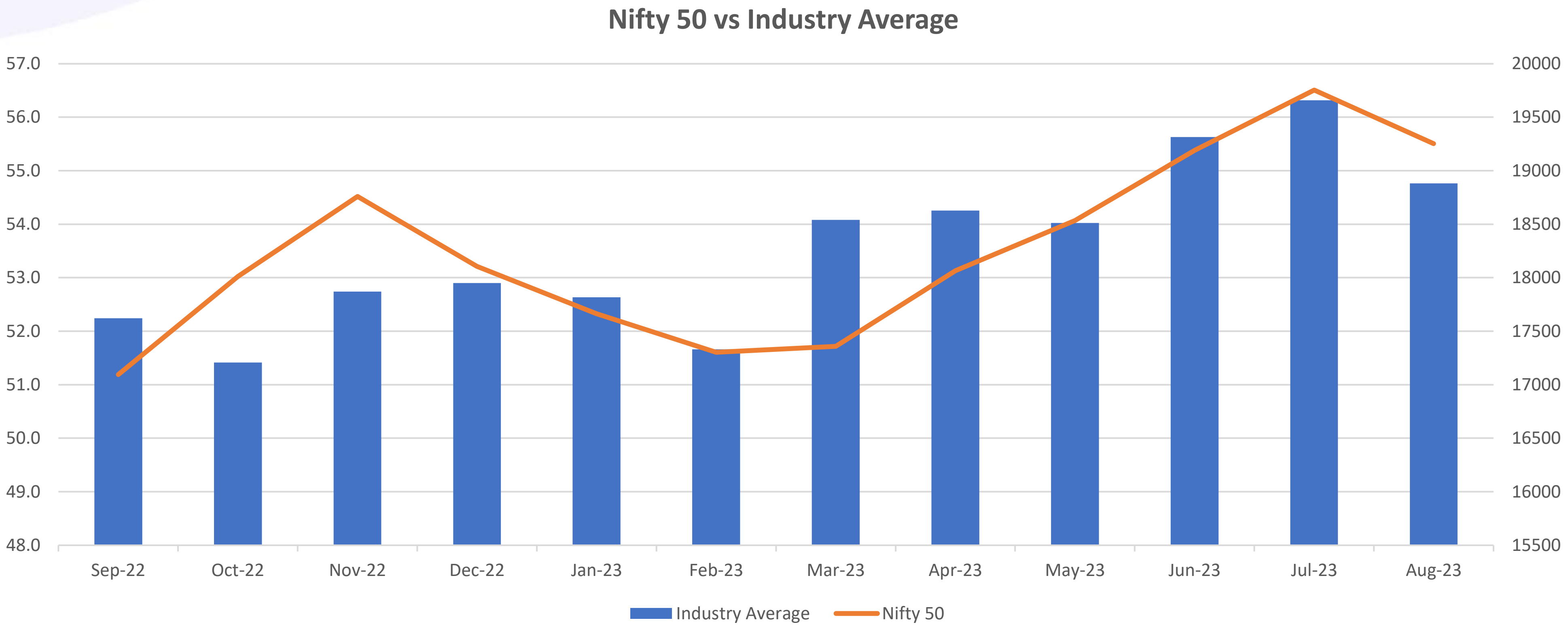


- Based on PE and BEER Ratio (which is Bond Equity Earnings Yields Ratio is a metric used to evaluate the relationship between bond yields and earnings yield in the stock market), the market looks slightly expensive

Note: PB methodology has been changed by NSE and hence has fell significantly (taking consolidated book value vs standalone earlier). However, historical data is basis earlier methodology and hence we have ignored PB based model for now

MFs Industry look Neutral on Equities

- The average Net Equity Level (in BAF) stands just above 50% indicating the industry participation is not aggressive on Equities
- Majority of AMCs which follow valuation driven approach including HDFC and ICCI Pru have Lower equity allocation.



Industry Positioning : Bullish on small cap

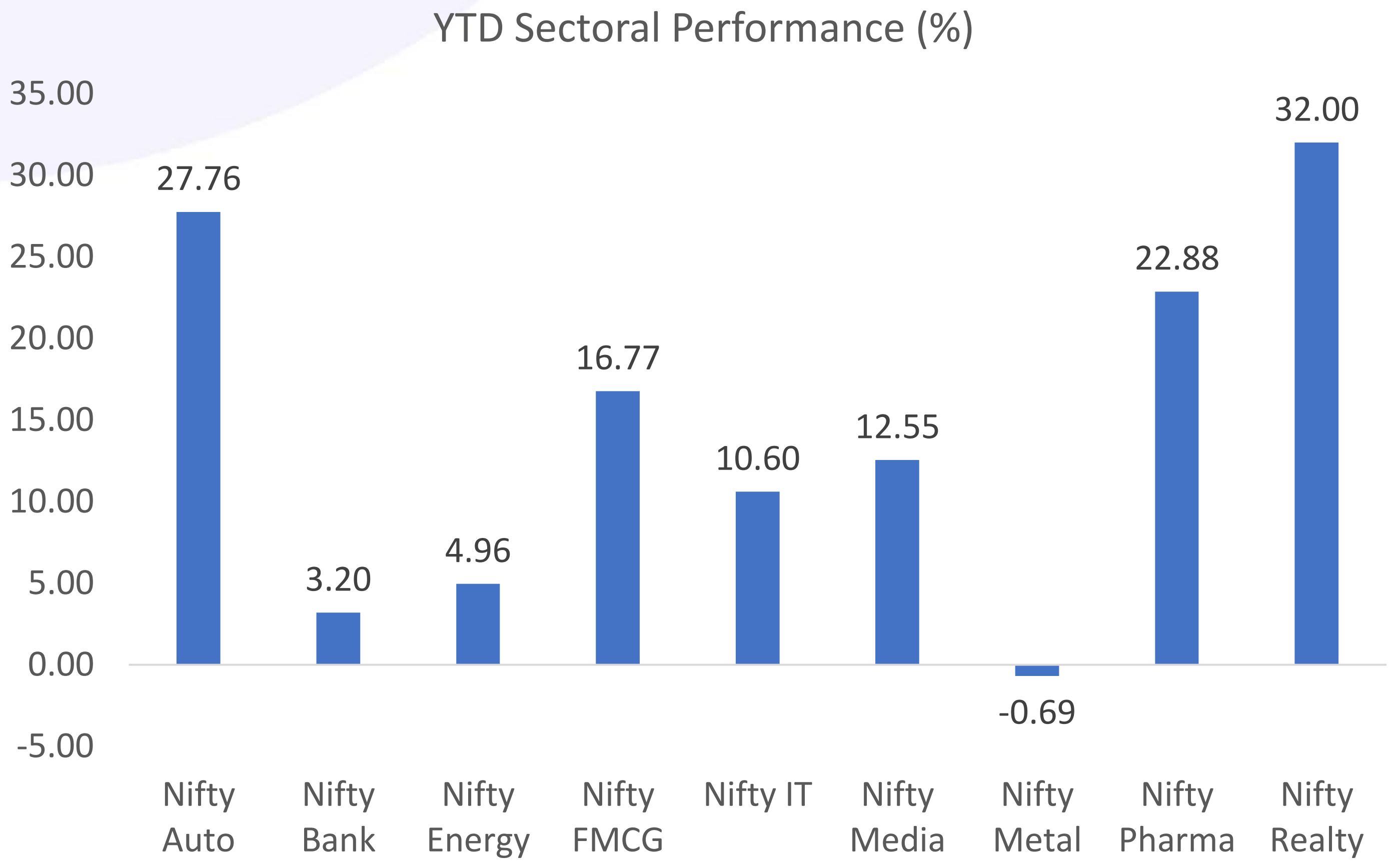
MCap		Current	NSE 500	Industry last 12M Avg	12M Min	12M MAX
Large	**UW**	59.93	73.75	64.11	59.93	66.30
Mid	**Marginally OW**	18.44	16.64	17.90	17.33	18.49
Small	**OW**	14.21	8.80	11.68	10.09	14.21

- MF industry too is bullish on smallcaps over large caps as seen in the allocation of flexi cap category.
- Also, industry is bullish on small caps as the allocation is highest in last 12 months. Well above the industry average and Index fund allocation.

Fund NAme	Large Cap	Mid Cap	Small Cap
MF Industry Average	59.93	18.44	14.21
Motilal Oswal Nse 500 ETF	73.75	16.64	8.80
HDFC Flexi Cap Fund	80.38	6.47	3.17
SBI Flexicap Fund	62.09	20.98	8.48
Kotak Flexicap Fund	72.48	24.22	2.00
Axis Flexi Cap Fund	74.55	7.83	13.53
ICICI Pru Flexicap Fund	74.53	10.04	10.78
Mirae Asset Flexi Cap Fund	68.32	19.75	9.77

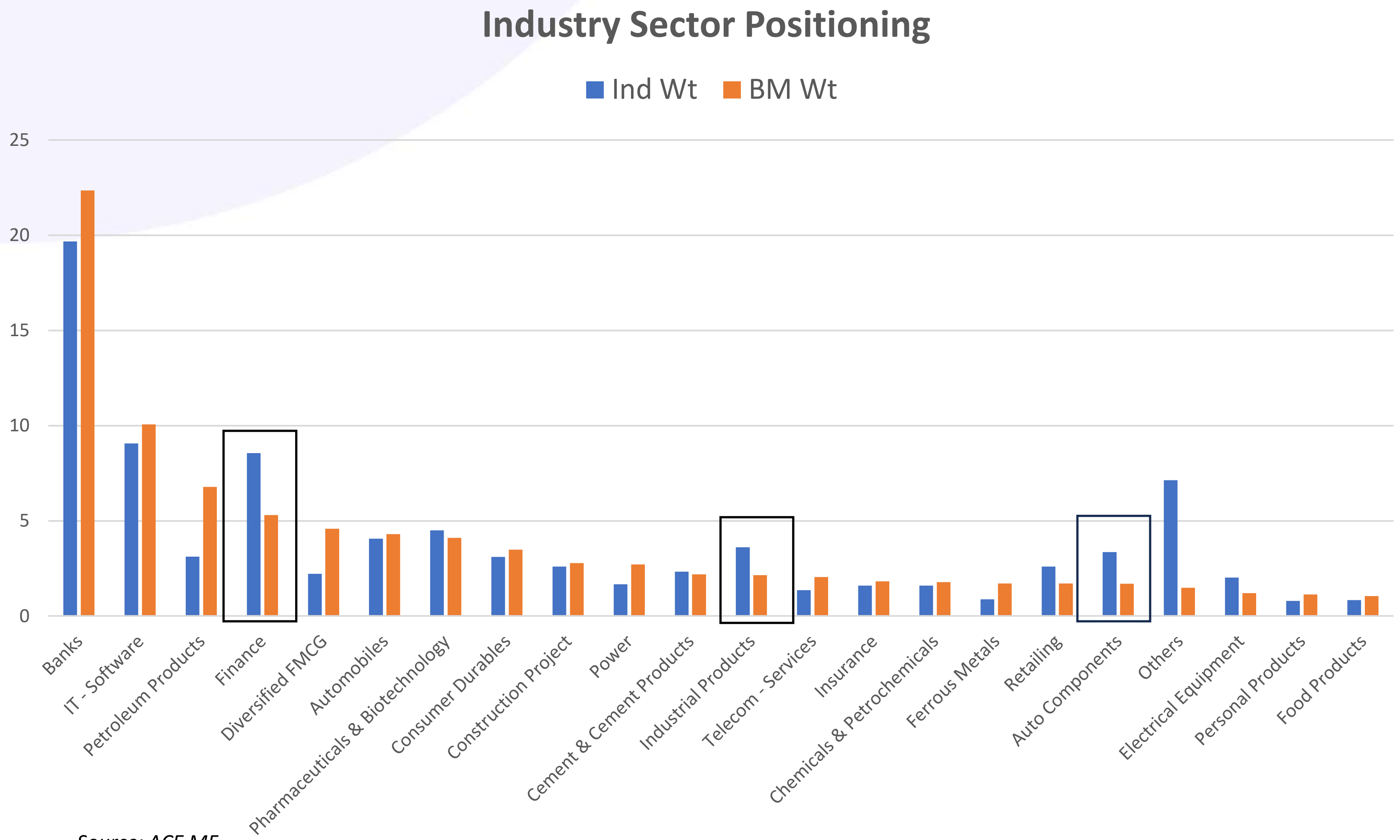
Source: ACE MF

Sectorally - Realty Auto led the recent rally



- Almost all sectors gave Positive returns in 2023, except metals.
- Realty has been the best performing sector YTD followed by Auto and Pharma.
- Banks and IT have been flat for last 2-3 months.
- Recently media has started to outperform and has been best performing sector in Aug.

Industry placing bets on Finance, Auto components and Industrials



Source: ACE MF

- MF Industry exhibits notable overweight positions in Industrial Products, Finance.
- Mainly underweight positions in banks, Petroleum Products, Diversified FMCG.
- The industry is also bullish on retailing as well as Auto components.
- Whereas there is under ownership in IT stocks.

Sector in Focus: Media

Media & Entertainment provides a large long term structural opportunity in India and the consolidation in the sector is a great inflexion point for the business.

Indian M&E sector grew 16.4% in 2021 to reach INR1.61 trillion

	2019	2020	2021	2022E	2024E	CAGR 2021-2024
Television	787	685	720	759	826	5%
Digital media	221	235	303	385	537	21%
Print	296	190	227	241	251	3%
Online gaming	65	79	101	120	153	15%
Filmed entertainment	191	72	93	150	212	32%
Animation and VFX	95	53	83	120	180	29%
Live events	83	27	32	49	74	32%
Out of Home media	39	16	20	26	38	25%
Music	15	15	19	21	28	15%
Radio	31	14	16	18	21	9%
Total	**1,822**	**1,386**	**1,614**	**1,889**	**2,320**	**13%**

All figures are gross of taxes (INR in billion) for calendar years | EY estimates

Sub-sectors		Key drivers
Television	Subscription	+ Strong performance by regional channels; Cost advantage vs. OTT - Second / Third pay TV connections getting curtailed on the back of OTT and Free dish
	Advertisement	+ Continued mass & wide reach with high penetration for building & sustaining brands + Ad revenue as share of GDP lags other countries, expected to increase
OTT	SVOD	+ Improved internet & smartphone access, and payment mechanisms + Investment in content, pricing innovations & bundling creating targeted niche properties
	AVOD	+ Significant increase in online content consumption + Ad technology and format innovations
Gaming		+ Mobile first gaming population with rising internet & smartphone access + Local games targeted specifically at local audience
Print		+ Focus on exclusive content with emphasis on credibility; reputed brands to gain - Shift to digital (esp. ads), reduced metro/English press subscriptions
Search & Social		+ Rise in online shoppers, social media users + Low ticket size makes it suitable for India's large SME segment
Audio		+ Growth in audio streaming, international & regional music + Wide reach with high penetration; Ad volumes shifting to Tier2++
Cinema		+ Expectation of growth due to a strong content pipeline and rebound demand - Shift to Digital/OTT release during the pandemic
Animation, VFX & Post-production		+ Increasing importance on content and better technology adoption + Availability of low cost and high skilled talent in India
OOH & Others		+ Upcoming infra projects, evolving digital OOH (DOOH)

Why Media Looks interesting now?

- **Consolidation in the Industry**: 1.4 billion Indians, distributed over 280 million households, need to be entertained and after the near to-complete industry consolidation phase, there will only be 3 large Indian players and a couple of international players that will be able to meaningfully cater to this need.

- **Consolidation leading to Pricing prower**: Consolidation in the industry will give pricing power to players and greater ability to negotiate with talent (very important factor in entertainment business)

- **High Growth expected:** Media and Entertainment Industry in India is about USD 27 billion with 1.4 billion consumers. This is expected to grow at 10-12% over the next decade to reach USD 55-70 billion in size offering a very large opportunity to leading players.

- **Attractive Valuations**: Media companies are available at very attractive valuations at the bottom of their earnings cycle. The earnings cycle for these companies, today, factors in very little growth in advertisement, no increase in subscription revenues for almost 4 years and peak losses on OTT platforms.

- **Tailwinds:** TRAI has finally implemented the New Tariff Order 2.0, now called NTO 3.0, starting April 1, 2023 and with this, broadcasters would now be able to now raise prices increasing their Average Revenue Per User (ARPU). Advertisement revenues are expected to bounce back from 2nd Half of financial year 2024 and losses on OTT platforms should also start coming down after peaking in financial year 2023.

MF Industry positioning on stocks

Large cap

Overweight	Active Weight
ICICI Bank Ltd.	1.04
Sun Pharmaceutical Industries Ltd.	0.77
NTPC Ltd.	0.67
Ultratech Cement Ltd.	0.59
Tata Motors Ltd. - DVR Ordinary	0.53

Underweight	Active Weight
HDFC Bank Ltd.	-2.58
Reliance Industries Ltd.	-2.52
Tata Consultancy Services Ltd.	-1.47
Asian Paints Ltd.	-1.08
Kotak Mahindra Bank Ltd.	-1.07

Mid Cap

Overweight	active Weight
Cholamandalam Investment and Finance Company Ltd.	1.27
Bharat Electronics Ltd.	1.05
PI Industries Ltd.	0.88
Clearing Corporation Of India Ltd.	0.85
ICICI Bank Ltd.	0.65

Underweight	active Weight
Shriram Finance Ltd.	-1.49
Yes Bank Ltd.	-1.34
Adani Power Ltd.	-1.12
Tata Elxsi Ltd.	-1.10
AU Small Finance Bank Ltd.	-1.09

Small Cap

Overweight	Active Weight
Clearing Corporation Of India Ltd.	1.05
Navin Fluorine International Ltd.	0.61
Timken India Ltd.	0.59
DCB Bank Ltd.	0.55
Rolex Rings Ltd	0.55

Underweight	Active Weight
Suzlon Energy Ltd.	-1.79
Jindal Stainless Ltd.	-1.02
KPIT Technologies Ltd.	-1.01
RBL Bank Ltd.	-1.01
BSE Ltd.	-0.99

Stock Trends in Smallcap MFs

Overweight	Fresh Entry (No of Small MF schemes)
Emami Ltd	3
Jyothy Labs Ltd	3
PCBL Ltd	3
ICICI Securities Ltd	3
BSE Ltd	3
Global Health Ltd	2
IDFC Ltd	2
Ideaforge Technology Ltd	2
Suzlon Energy Ltd	2
Divgi Torqtransfer Systems Ltd	2

	Complete Exit (No of Small MF schemes)
PVR Inox Ltd	3
Home First Finance Company India Ltd	3
Zee Entertainment Enterprises Ltd	3
Greenply Industries Ltd	2
Computer Age Management Services Ltd	2
LTIMindtree Ltd	2
Carborundum Universal Ltd	1
Balrampur Chini Mills Ltd	1
Timken India Ltd	1
Radico Khaitan Ltd	1

Equity Outlook – Neutral on Equities, Bullish on Small cap, Media

- Markets have been running up since March lows. The good news is this rally has been accompanied by a strong economy, robust corporate profit outlook and improving macros.

- From valuation perspective, markets are not cheap but are not very expensive either. Earnings growth is favourable as well. But, there has been a one-way rally in the mid and small-cap space since March lows. Hence a correction may occur. However, it may be swift and give a chance to add on more. At this juncture, FOMO is high and we would advise not to jump the gun.

- On a concerning note, monsoons have been uneven with 36% deficit in august and 13% surplus in sept leading to limiting rice and onion exports. Higher crude prices also need to be watched (near 100$ mark as of September End). With general elections less than a year away, we may see high volatility in the markets. Hence, we are currently neutral on the equity markets.

- Market cap – From market cap allocation perspective, we favor mid and small caps over largecaps. The earnings growth has been significantly higher in Mid and small caps in post covid phase. Valuation wise midcaps are well below their historical all time highs. We also analyzed the MF Market cap positioning of flexicap funds and largecaps are near the 12 months low allocation, so MF industry is also overweight on mid and small-caps. Further, the mid and small indices are exhibiting strong momentum.

- Sector – Media & Entertainment provides a large long term structural opportunity in India and the consolidation in the sector is a great inflexion point for the business. MF industry has been bullish on Auto components and Industrials for a while.

Fixed Income Outlook

- **Inflation**
  - Retail price inflation in India eased to 6.83% in August 2023 from 7.44% in July which was the highest since April 2022, and below market forecasts of 7%.
  - Despite the slowdown in August, inflation stayed above the central bank target of 2-6% impacting agricultural production and prompting a spike in food prices, specially vegetables.
  - But the government then subsidised vegetable prices and ban exports of some cereals including sugar and rice to control inflation

- **Growth (GDP)**
  - India's economy expanded by 7.8% in the April-June quarter, the most in a year and slightly surpassing market expectations of a 7.7% expansion.
  - The robust performance of the service sector was the main driver of GDP growth, accompanied by strong consumer demand and increased government capital expenditure. Private consumption, which accounts for nearly 60% of the economy, grew about 6% (vs 2.8% in Jan-Mar), while capital formation growth eased to about 8% (vs 8.9%).
  - According to forecasts released by the Reserve Bank of India, Asia's third-largest economy is projected to expand by 6.5% in this fiscal year.

Fixed Income Outlook

- The RBI has paused on rate hike in the policy reviews on 6 April, 8 June and 10 August 2023. Though the RBI stance remains as that of "withdrawal of accommodation", practically, rate hikes look extremely unlikely
- One can take exposure to longer maturity bonds as well. However, the yield curve is flat and you would not be compensated in terms of higher yield. From this perspective, it is better to match your investment horizon with the maturity of the bond.
- Further, For AAA and AA rated bonds, currently available yield levels are marginally higher than 10-year average. For A rated bonds, currently available levels are palpably higher.
- For AAA and AA rated bonds, current spreads over benchmark Gsec is lower than 10-year average. For A rated bonds, current spread is higher than 10-year average.
- The cumulative default rates of rating agencies are better than earlier, indicating that corporate health is better now.
- The rating stability / transition rates of rating agencies are reasonable - it is relevant because default rates are computed at current ratings.
- Historical data from Crisil shows risk-adjusted returns, computed as quoted level vis-à-vis the required yield for that rating category, has been positive for AA and A rated categories.
- Net-net, you can take credit exposure as long you are comfortable with the business model, track record and promoter quality of the issuer, and you are getting compensated in terms of yield

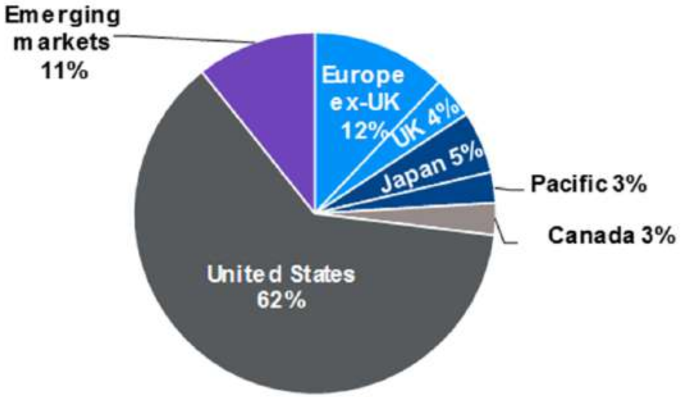
Global Outlook

Global Equity Market Performance

Returns	2023		2022		15-years	
	Local	USD	Local	USD	Ann.	Beta
Regions						
U.S. (S&P 500)	-	13.1	-	-18.1	11.3	0.9
AC World ex-U.S.	8.7	5.8	-9.2	-15.6	4.8	1.0
EAFE	11.2	7.6	-6.5	-14.0	5.2	1.0
Europe ex-UK	10.0	9.2	-12.2	-17.3	5.5	1.2
Emerging markets	4.4	2.2	-15.2	-19.7	4.1	1.1
Selected Countries						
Japan	26.2	11.6	-4.1	-16.3	4.9	0.7
United Kingdom	5.2	6.8	7.2	-4.8	4.3	1.0
France	11.7	10.8	-6.9	-12.7	5.8	1.2
Canada	4.2	4.5	-5.8	-12.2	4.7	1.1
Germany	10.6	9.7	-16.5	-21.6	4.1	1.3
China	-6.1	-7.1	-20.6	-21.8	4.2	1.0
Taiwan	17.4	11.8	-21.3	-29.1	10.9	1.0
India	8.7	8.3	3.0	-7.5	7.7	1.1
Brazil	7.1	13.0	8.6	14.6	1.1	1.4

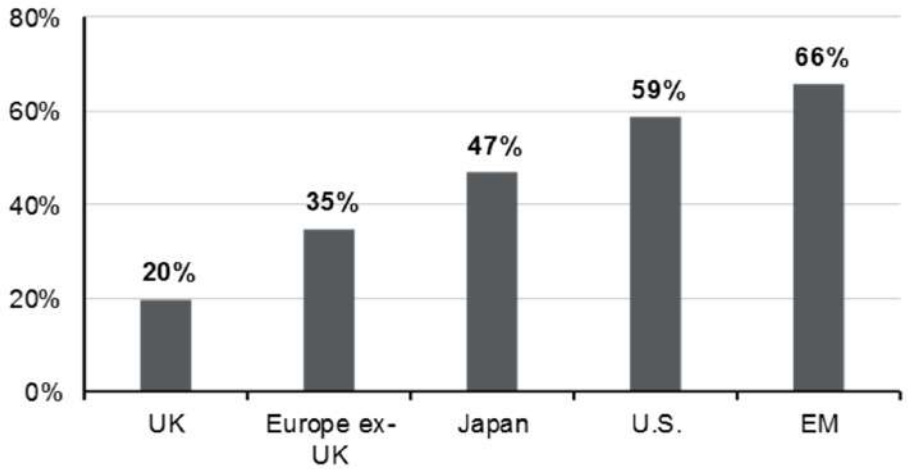
Weights in MSCI All Country World Index

% global market capitalization, float adjusted



Revenue exposure vs. country of listing

% of total revenue from home countries



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Rates in Global Economies

The advanced economies, given their historical interest rates, are not in a position to absorb high interest rates for a long time, without impacting their growth.

	Yield		2023 Return			
Aggregates	9/30/2023	12/31/2022	Local	USD	Duration	Correlation to U.S. 10yr
U.S.	5.39%	4.68%	-1.21%	-1.21%	6.2 years	0.91
Gbl. ex-U.S.	3.47%	3.13%	-	-2.84%	6.8	0.59
Japan	0.89%	0.75%	0.19%	-11.41%	9.2	0.63
Germany	3.58%	3.22%	0.23%	-0.57%	6.0	0.51
UK	4.99%	4.29%	-2.96%	-1.53%	7.8	0.50
Italy	4.41%	4.10%	1.91%	1.10%	5.9	0.38
China	2.80%	2.94%	3.45%	-1.54%	5.9	0.54
Sector						
Euro Corp.	4.52%	4.32%	2.53%	1.71%	4.3 years	0.42
Euro HY	8.43%	8.32%	6.76%	5.91%	3.0	0.01
EMD (USD)	9.03%	8.55%	-	1.76%	5.8	-0.02
EMD (LCL)	6.76%	6.86%	5.02%	4.28%	4.9	-0.09
EM Corp.	7.75%	7.28%	-	3.38%	4.8	-0.04

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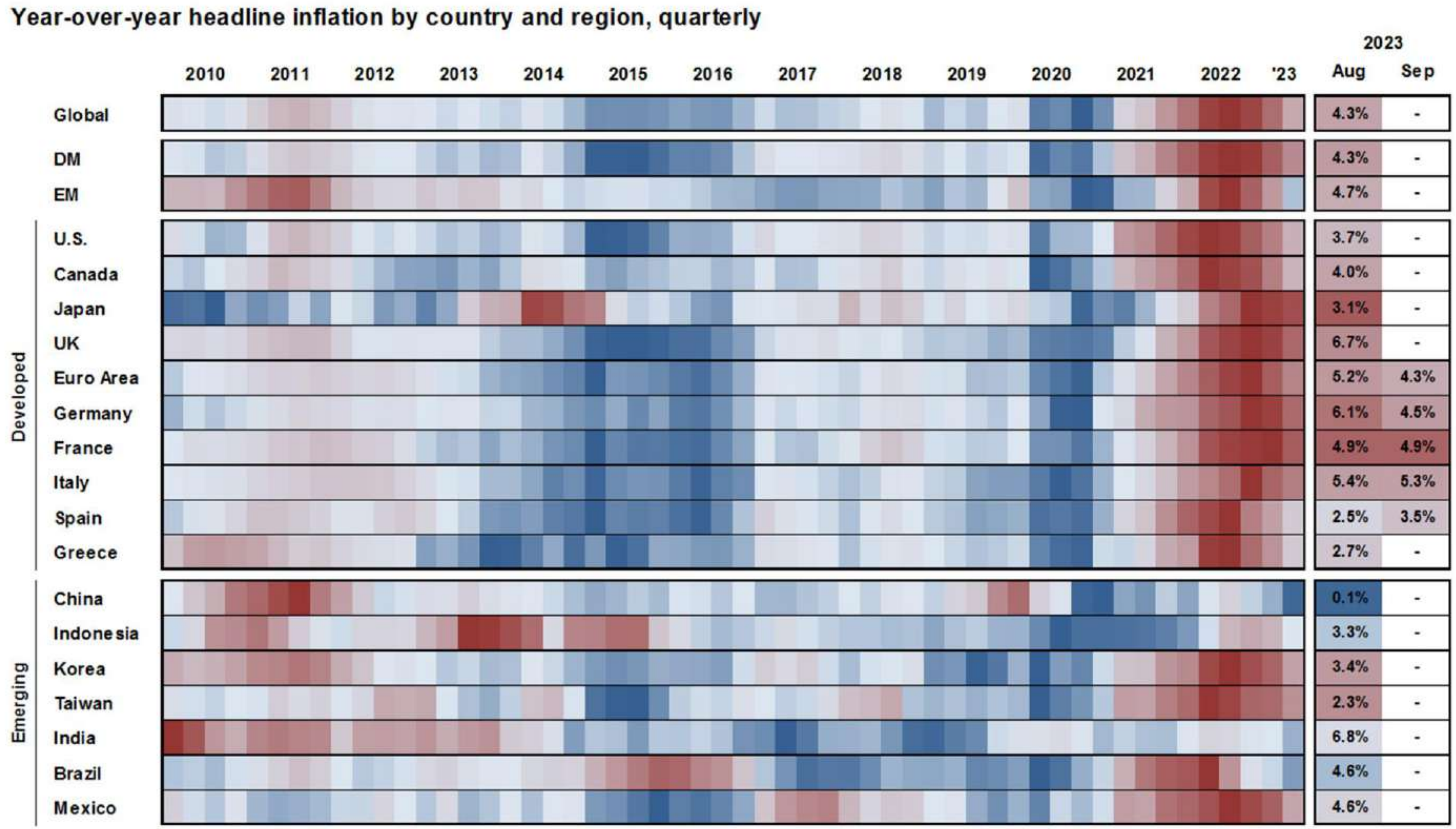
And the Inflation still remains the concern

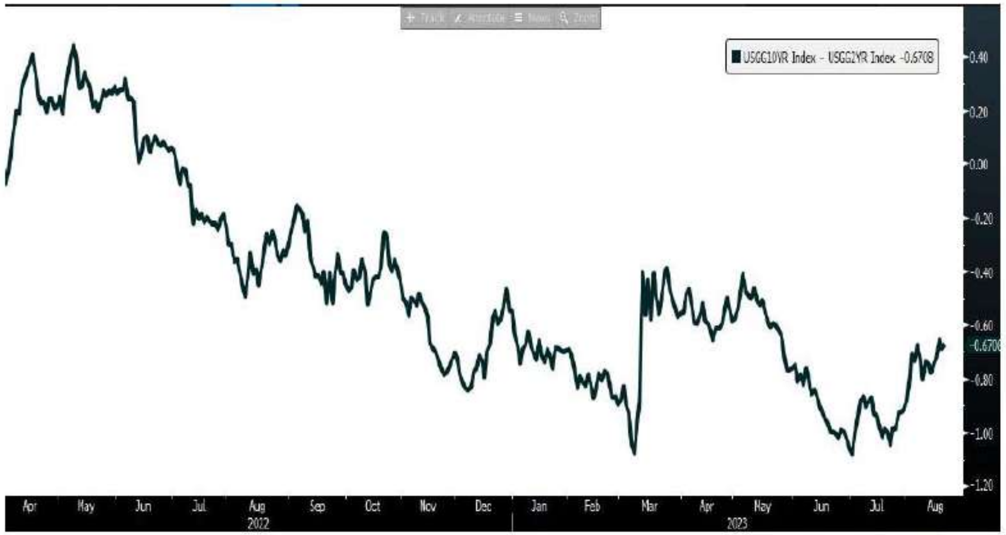


US not out of Cautious Zone

The graph below shows US Treasury 10-year yield minus 2-year yield. The term spread has been in negative zone since middle of 2022. May be not a recession, but negative 2-10 spread indicates at least muted expectation of rate action going forward.

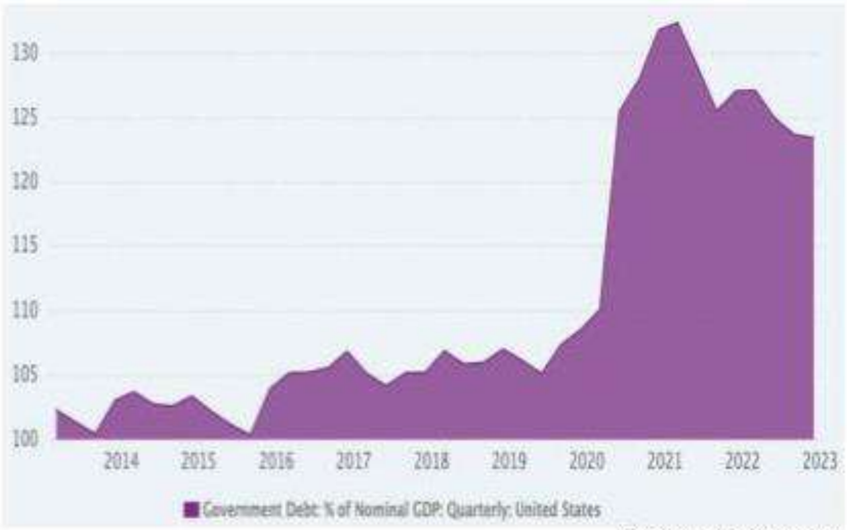
With outstanding debt of around USD 32 trillion and debt servicing cost of USD 1 trillion per year, it will be increasingly difficult to manage and service.

Us Curve Inversion still pronounced



(Source: Bloomberg)

US Government Debt to GDP – 120%



(Source: ceicdata.com)

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Even Valuation are not Looking Attractive

S&P 500 Index: Forward P/E ratio

Valuation measure	Description	Latest	25-year avg.*	Std. dev. Over-/under-Valued
P/E	Forward P/E	17.83x	16.76x	0.32
CAPE	Shiller's P/E	29.53x	27.73x	0.29
Div. Yield	Dividend yield	1.69%	1.98%	0.85
P/B	Price to book	3.61x	3.10x	0.63
P/CF	Price to cash flow	13.54x	11.27x	1.03
EY Spread	EY minus Baa yield	-0.78%	0.33%	0.58

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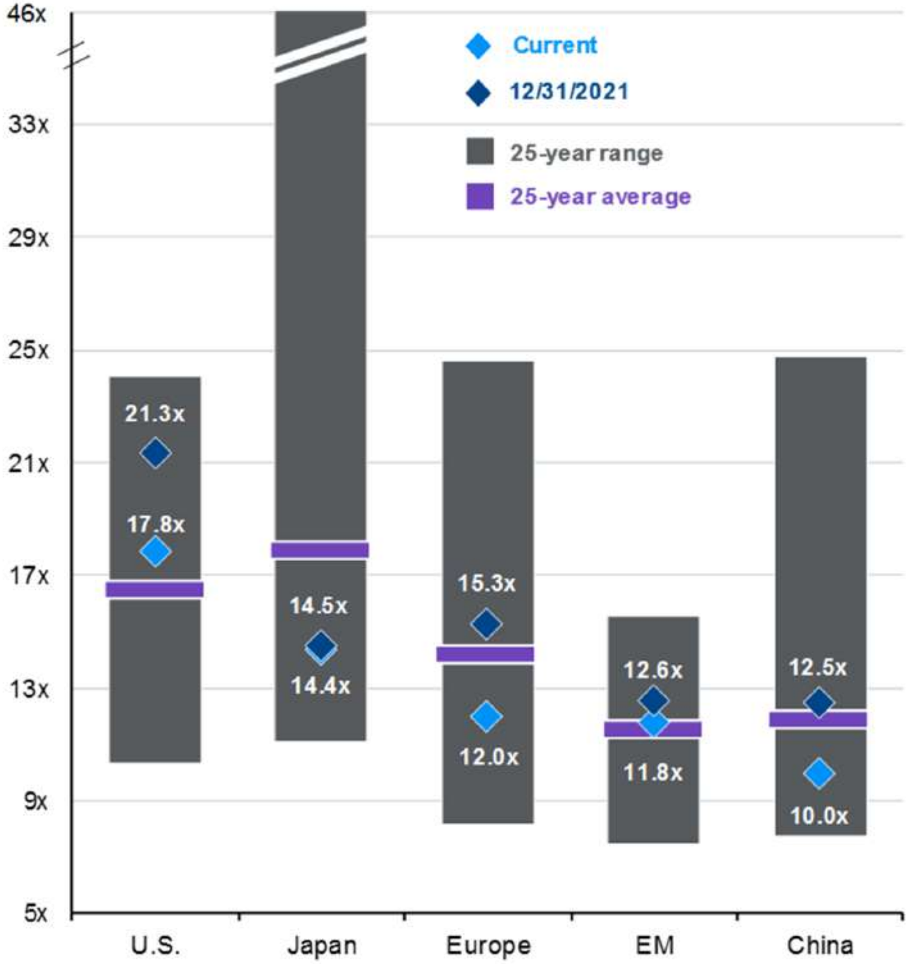
If not US, then where?

	20-yr. avg. P/E ratio	Current P/E ratio
S&P 500	15.6x	17.8x
ACWI ex-U.S.	13.1x	12.4x



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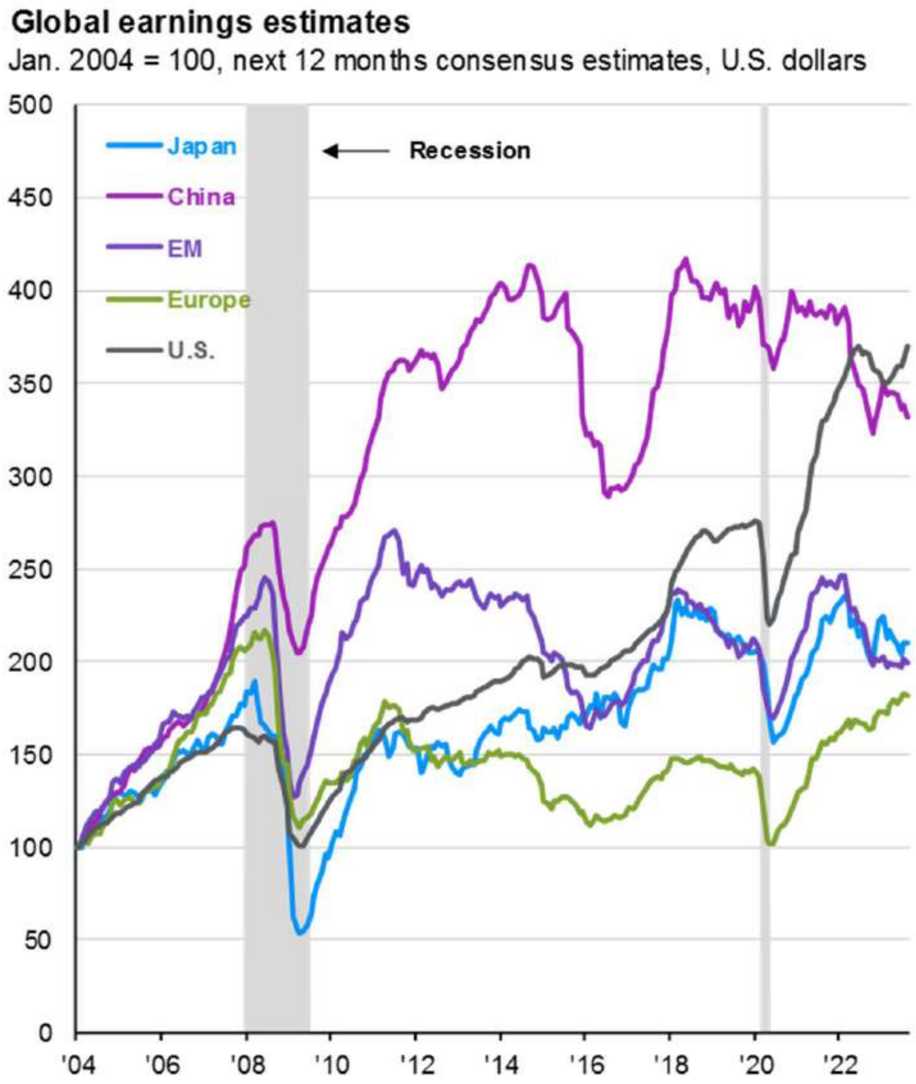
Where in International Markets?

- Earning growth in international markets combined with discounted valuations, help make the case for investing in non US Equities.

- However, Relatively Japan Looks most promising compared to Europe, China, or other EMs



Preference stays on Japan

- **Reforms are front-and-center again:** Current the reforms are being led by Tokyo Stock Exchange where it has urged all companies trading below their book value to devise a plan to improve capital efficiency and support their stock price. The scope for improvement is high as 50% of the stocks listed on TOPIX and 26% of stocks in MSCI Japan are currently trading at PB<1. We believe this could be a potential catalyst for structural re-rating of Japanese equities, an issue which has long haunted investors and would add to the tailwinds from ongoing accommodative policy stance.

- **Expect renewed interest from both foreign and domestic investors:** Japanese equities have been seeing renewed interest from foreign investors who have poured in 50.6$bn of money this year, which is the highest foreign institutional flow seen in Japan since 2013. Retail investor ownership has fallen from 40% in 1970s to ~17% now– we expect retail investor participation to also increase as households break-out of ‘saving’ mindset to ‘investing’ mindset led by inflation, wage growth and high savings.

- **Breaking the deflation spiral**- Japan is seeing inflation, which is at 3.3% after hitting a four decade high of 4.3% in Jan 2023. Return of inflation, reasonable growth and low unemployment rate is expected to bring change in consumption and investment patterns in Japan, and we are already seeing early signs of a shift with healthy wage growth, increasing capex and falling savings with steady consumption activity

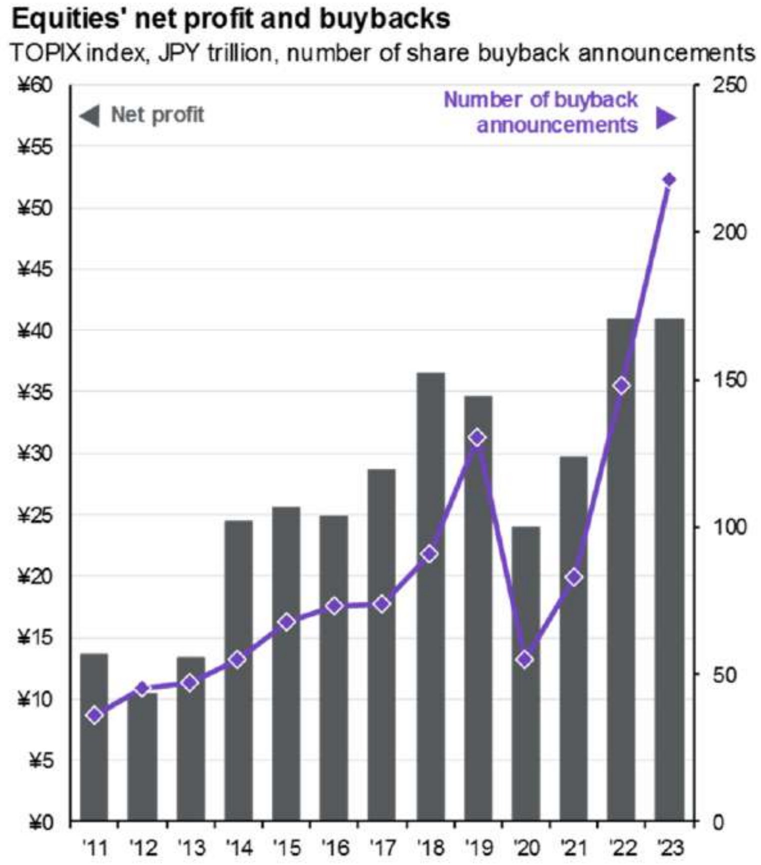
- **Attractive valuations and robust earnings support -**Even though Japan market has delivered strong returns YTD, up 22% in local currency terms, the market still looks attractive on valuations. MSCI Japan is trading at 15.0 x fwd PE vs. US market at 20.6 x PE.

Japan: Economy and markets

Historically, Japan has had weak, even negative, wage growth and deflation as a result of slow GDP growth.

More recently, both core inflation and wage growth have been picking up, which suggests more momentum in the economy.

The right hand side shows that share buybacks in Japan have increased, meaning companies are more confident about their future earnings and growth.



Thank You!

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