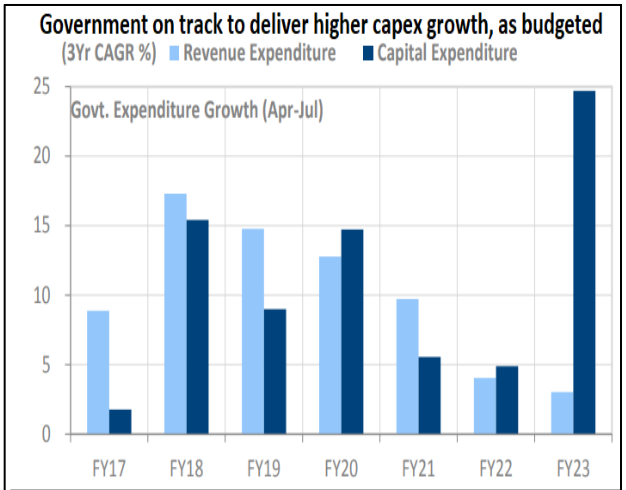
Market Commentary: India will outperform but cannot be an outlier

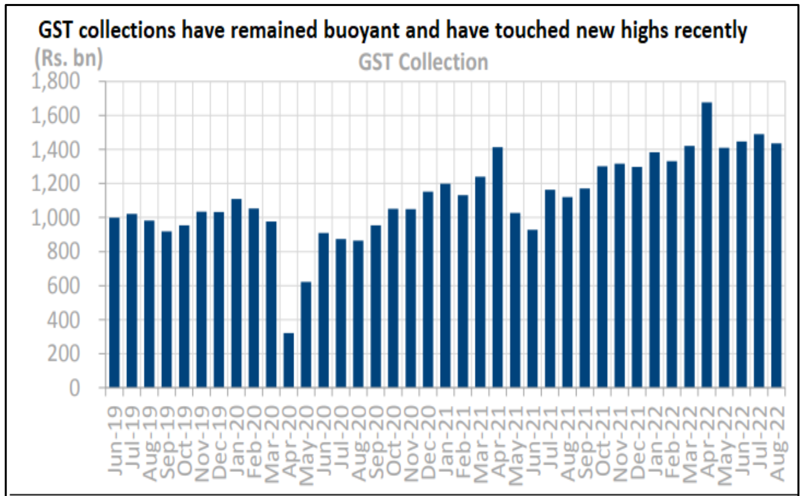
The markets have been trading with a bearish bias for the past few days post the FOMC meet in the US on Wednesday. The 0.75 basis point hike by the Fed was well anticipated by the market, however, the projection of further big rate hikes in the near future dampened the mood of the investors.

Moreover, all the major developed nations are facing severe economic challenges. The recession fears in the US and European countries, the Russia-Ukraine war and the political uncertainty in China has further casted a dark cloud of uncertainty in the global economy.

This led the US10 Year bond yields to rise to 3.82%, highest since 2010. The high frequency indicators of India, however, are printing a very promising picture. A standout data has been the decline in unemployment rate from 7.8% in June to 6.8% in July which was primarily due to higher employment in the rural areas as also seen in MNREGA job demand for Jul'22 falling to 25mn. Almost 65% of India's population lives in the rural areas and hence higher employment here definitely gives a boost to the consumer sentiment. The GST collections have been very robust, with it being above the 1 lakh crore mark for 15 consecutive months and above 1.4 lakh crore mark for the sixth straight month. Strength in the revenue collections for the govt. means that what looked like an ambitious target on Capex, might be pursued capably. If we look at the provisional cash market data, In the last few days, we have seen that FIIs are turning net sellers again after being net buyers for over two months. However, Analysis of passive funds, both FIIs and Domestic MFs, shows that Despite the big sell-off by FIIs during the last year, where active FII money has seen outflows of $14.4bn/ $24.5bn in CY21/CY22YTD in secondary markets, passive FII money has actually seen inflows to the tune of $7.3bn and $1.6bn in CY21/CY22YTD. But we have to understand that during times of panic, the correlations among all markets become 1. So, it would not be that the Indian market will keep outperforming while the Global markets fall. Due to globalization, a decline in major global economies will naturally have some impact on India, no matter how strong our economy is. Like all countries, we too will witness a fall in the short to medium term.

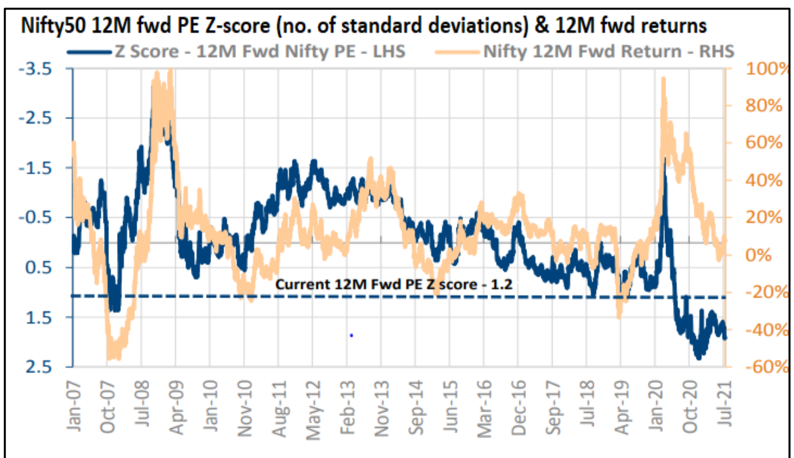


Source: CEIC, IIFL Research

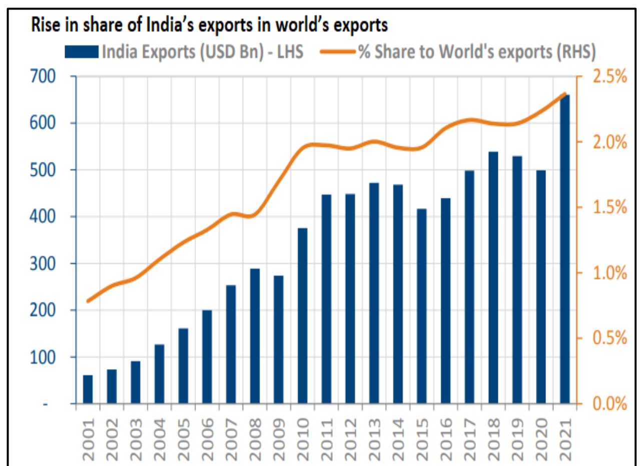


Source: CEIC, IIFL Research

A slowdown/recession would have an impact on our country's exports as demand for goods and services would begin to dry up. Hence we should expect higher volatility in IT stocks in the near term. However, India's emergence as one of the key global manufacturing hubs (Recent announcements by Google and Apple to manufacture in India resonates the same) coupled with China+1 theme shall aid export growth in the medium term.



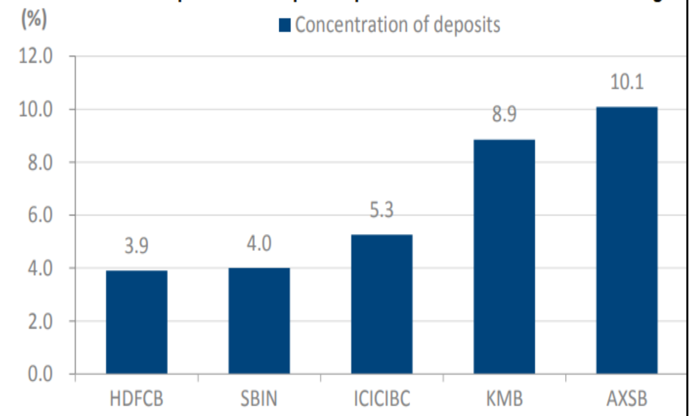
Source: Bloomberg, IIFL Research



Source: World Bank, IIFL Research

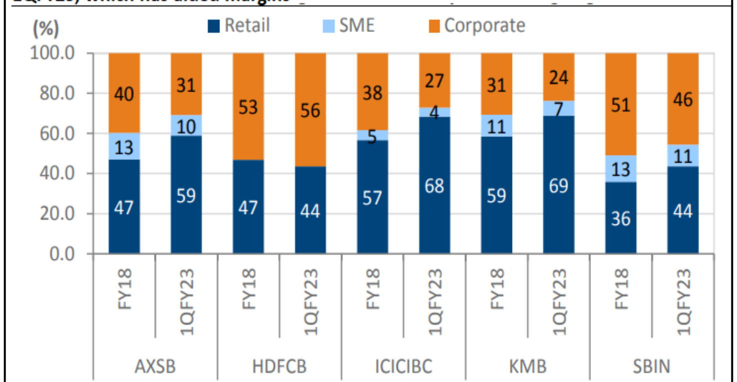
Currently Nifty trades at 1.2 Std-Dev. above 15-yr avg, both for PE and PB, but India's emerging rarity value means that Nifty can eke out modest returns. Earnings growth estimates in mid-caps, and especially small caps, are much in excess of historicals. Markets are expected to trade in a broad range for the medium term, and every correction would provide an opportunity to accumulate quality stocks for the long term. Technically, Nifty is likely to find short term support at the 200-day EMA situated at ~16850 levels while resistance is likely to at 17700. Breakdown of the 200-day EMA is likely to put further pressure on the Index. We would emphasize large caps over mid-caps and being overweight on Banks.

Concentration of deposits from top-20 depositors as of FY22 is also well managed



Source: Company, IIFL Research

Loan mix – Increase in the share of retail and SME loans has increased over FY18 - 1QFY23, which has aided margins



Source: Company, IIFL Research; Note: For HDFCB the mix is given as retail/corporate only due to a change in reporting

Banks are very well placed with supportive monetary stance, healthy capitalisation, improved liability profile, diversified asset mix and healthy asset quality along with strong coverage ratios. Tighter liquidity conditions, in an environment of rising loan demand, should in general benefit banks on margins. Technically, the Nifty bank index finds support at 38000 levels while resistance is likely to be at 39800 levels. HDFC Bank, ICICI Bank and SBI Remain our top picks.

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Recommendation Parameters for Fundamental/Technical Reports:

Buy – Absolute return of over +10%
Accumulate – Absolute return between 0% to +10%
Reduce – Absolute return between 0% to -10%
Sell – Absolute return below -10%

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