

Liquidity, Valuation and Events: July 2019 Darkest Before Dawn

Global Indices

Index Name	Country	29 Jun 2018	29 Mar 2019	28 Jun 2019	3 Month Return (%)	1 Year Return (%)
Developed Economies						
DAX	Germany	12,306	11,526	12,399	8%	1%
Swiss Market	Switzerland	8,609	9,478	9,898	4%	15%
Nasdaq	US	7,510	7,729	8,006	4%	7%
CAC 40	France	5,324	5,351	5,539	4%	4%
Straits Times	Singapore	3,269	3,213	3,322	3%	2%
NYSE	US	12,504	12,697	13,050	3%	4%
Dow Jones	US	24,271	25,929	26,600	3%	10%
FTSE 100	UK	7,637	7,279	7,426	2%	-3%
Nikkei 225	Japan	22,305	21,206	21,276	0%	-5%
Seoul Composite	South Korea	2,326	2,141	2,131	0%	-8%
BRICs						
RTS Index	Russia	1,154	1,198	1,381	15%	20%
Bovespa	Brazil	72,763	95,415	100,967	6%	39%
S&P BSE SENSEX	India	35,423	38,673	39,395	2%	11%
NIFTY 50	India	10,714	11,624	11,789	1%	10%
Hang Seng	Hong Kong	28,955	29,051	28,543	-2%	-1%
Shanghai Composite	China	2,847	3,091	2,979	-4%	5%
Other Emerging Economies						
MerVal	Argentina	26,037	33,466	41,796	25%	61%
KLSE Composite	Malaysia	1,692	1,644	1,672	2%	-1%
Taiwan Weighted	Taiwan	10,837	10,641	10,731	1%	-1%
Jakarta Composite	Indonesia	5,799	6,469	6,359	-2%	10%

Indices Performance

Index Name	29 Jun 2018	29 Mar 2019	28 Jun 2019	3 Month Return (%)	1 Year Return (%)
Nifty Financial Services	11,007	12,544	13,556	8%	23%
NIFTY Realty	272	269	285	6%	5%
NIFTY Infra	3,126	3,208	3,369	5%	8%
NIFTY Bank	26,364	30,427	31,105	2%	18%
NIFTY IT	13,990	15,628	15,936	2%	14%
NIFTY 50	10,714	11,624	11,789	1%	10%
NIFTY Private Bank	14,962	17,316	17,197	-1%	15%
NIFTY Consumption	5,031	4,855	4,756	-2%	-5%
NIFTY FMCG	28,966	30,321	29,546	-3%	2%
NIFTY Energy	13,333	16,484	16,047	-3%	20%
Nifty Midcap 100	18,181	18,259	17,654	-3%	-3%
NIFTY PSU Bank	2,792	3,339	3,206	-4%	15%
NIFTY Auto	10,709	8,335	7,928	-5%	-26%
Nifty Smallcap 100	7,178	6,673	6,200	-7%	-14%
NIFTY Pharma	9,173	9,347	8,065	-14%	-12%
NIFTY Media	3,026	2,497	2,040	-18%	-33%

LIQUIDITY – FII FLOWS

Equity

(in Rs. Crore)	Apr– 19	May – 19	June – 19	TOTAL
Gross Purchase	1,10,741	1,41,247	1,04,877	3,56,865
Gross Sale	89,547	1,33,328	1,02,282	3,25,157
Net Investment	21,193	7,920	2,596	31,709

Debt

(in Rs. Crore)	Apr– 19	May – 19	June – 19	TOTAL
Gross Purchase	24,268	28,622	44,313	97,203
Gross Sale	29,367	27,510	35,994	92,871
Net Investment	-5,099	1,111	8,319	4,331

Total Net FII Flows in April- June'19

Rs. 36,040 Crore

Source: ACE MF

LIQUIDITY – DII FLOWS

(in Rs. Crore)	Apr– 19	May – 19	June – 19	TOTAL
Gross Purchase	2,10,218	1,43,923	58,638	4,12,779
Gross Sale	2,05,478	1,34,963	54,995	3,95,436
Net Investment	4,740	8,960	3,643	17,343

Source: ACE MF

MF ACTIVITY

Equity

(in Rs. Crore)	Apr– 19	May – 19	June – 19	TOTAL
Gross Purchase	46,209	61,422	47,005	1,54,635
Gross Sale	51,128	56,259	40,773	1,48,159
Net Investment	(4,919)	5,163	6,232	6,476

Debt

(in Rs. Crore)	Apr– 19	May – 19	June – 19	TOTAL
Gross Purchase	2,23,392	2,42,203	1,92,460	6,58,056
Gross Sale	1,72,939	2,10,863	1,491,76	5,32,979
Net Investment	50,453	31,340	43,284	1,25,077

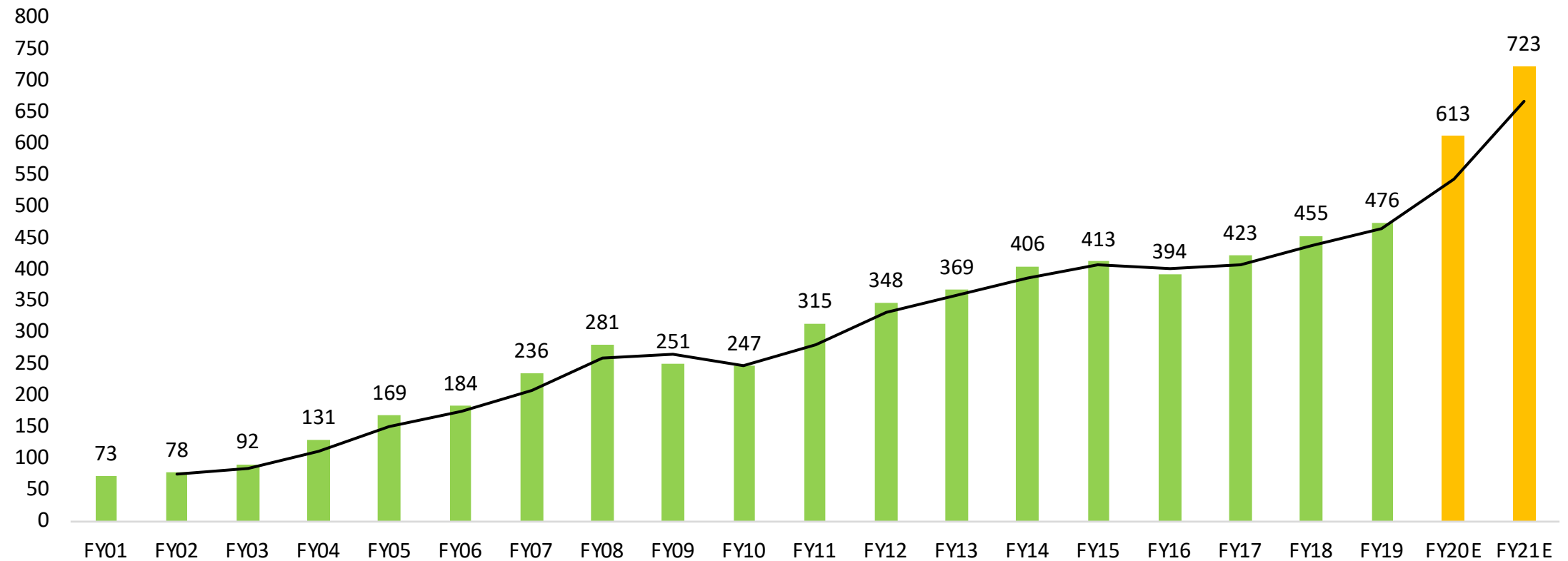
Total Net MF Activity in Jan-Mar'19

Rs: 1,31,553 Crores

Source: ACE MF

Earnings Check

Nifty EPS Trend – Market expects accelerating earnings growth in FY20/21



Source: Bloomberg,

Valuation of benchmark stocks above Long-term average

Nifty 12 month forward PE (vs. 10 year average)



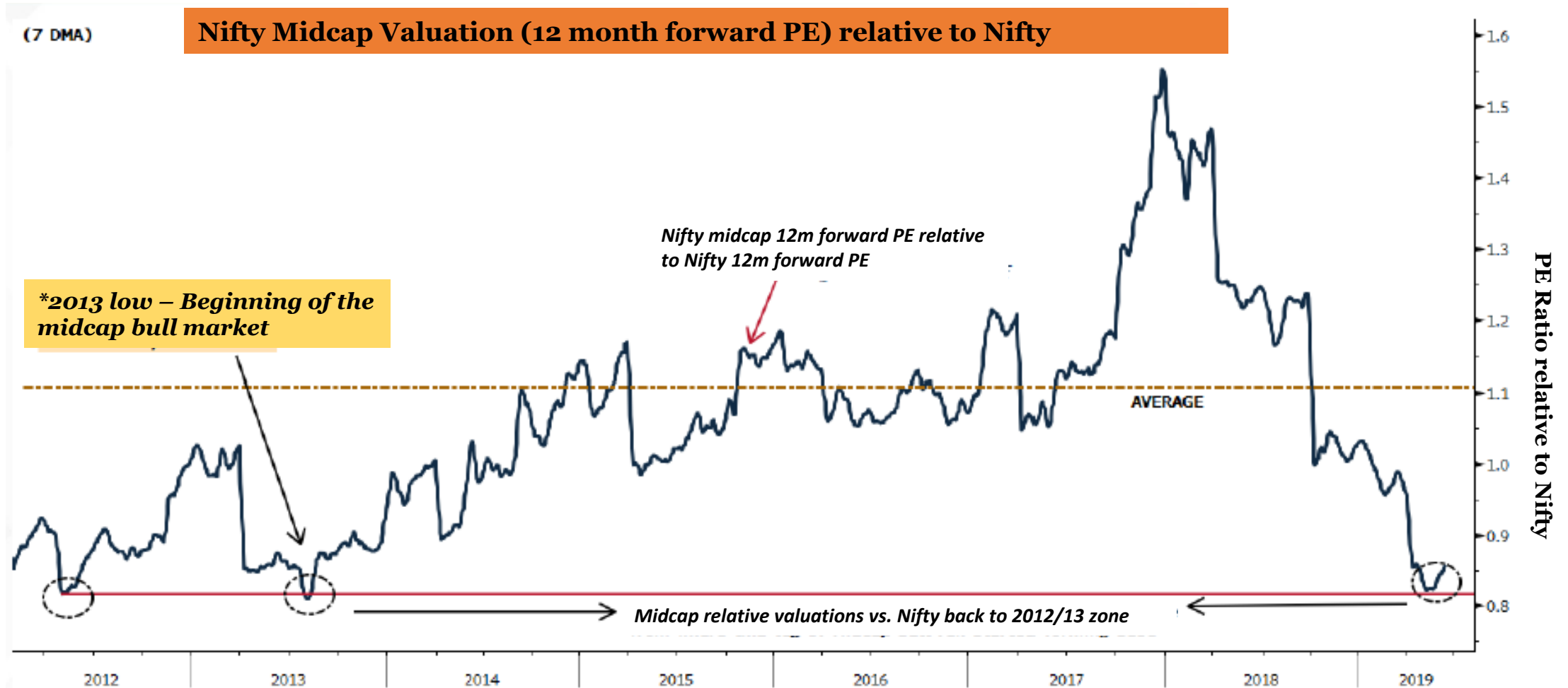
Nifty 12 month forward P/BV (vs. 10 year average)



- Re-rating of benchmark indices hinges on earnings growth in FY20E/21E
- Nifty takes a breather in June post strong run-up in May

Source: Motilal Oswal Research (as of June 2019)

... But Midcaps attractive vis-à-vis benchmark index



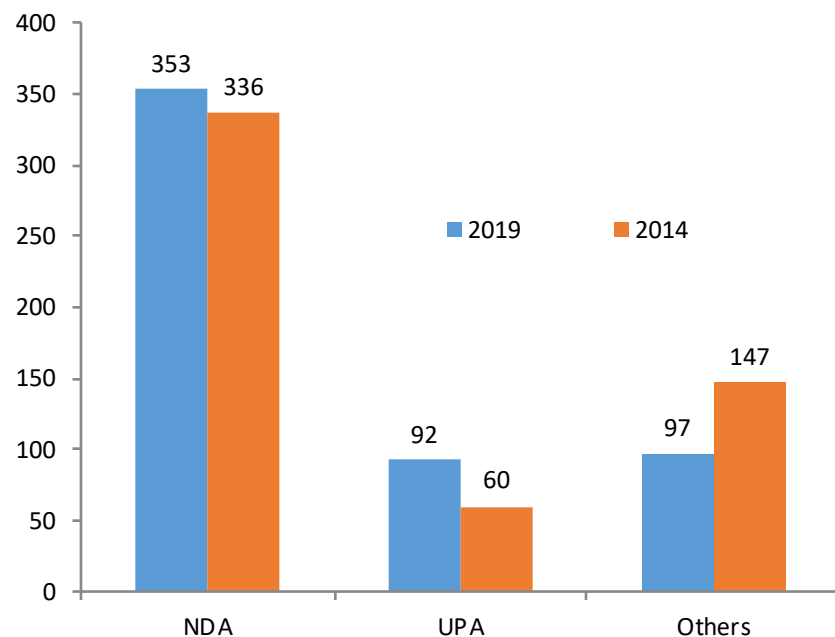
Source: Elara Securities, Kotak MF (June 2019)

Election outcome – “Phir Ek Baar Modi Sarkar”

- Thumping majority win for the ruling NDA dispensation with 350+ seats – this the largest mandate for an incumbent government since 1984.
- **What does this mean?**
 - Political risks reduced and market expectations of Government’s continuity have been addressed.
 - Renewed expectations for a more reforms oriented policy agenda in divestment, labor reforms, ease of doing business and land acquisition.
- **Key action areas for the NDA government to steer the market are:**
 - Address the disquieting rural distress
 - Stem the drag on discretionary and staple consumption
 - Resolve bank balance sheet issues and recapitalize PSU banks to spur private capital expenditure
 - Initiate measures to infuse liquidity in the NBFC sector, which has a cascading effect on consumption & growth
 - Sustain Public Infrastructure spending and plug the fiscal deficit

Election outcome – Cont.

Election Outcome - 2019 vs. 2014



Source: ECI

NDA Performance across key states

States	Total Seats	2014 (Seats Won)	2019 (Seats Won)
UP	80	71	62
Maharashtra	48	23	23
West Bengal	42	2	18
Bihar	40	22	17
MP	29	27	28
Karnataka	28	17	25
Gujarat	26	26	26
Rajasthan	25	25	24
Orrisa	21	1	8

Source: ECI

Global Events (April-June Quarter)

- The IMF lowered its growth forecast for 2019 to 3.3 percent from the previous level of 3.5 percent in its latest World Economic Outlook (WEO).
- US GDP growth for 1CQ came in at 3.1% (vs. 2.2% in December Quarter)
- Trade war between US and China continued to Intensify – with both sides intending to raise tariffs
- In its FOMC meet in June 2019, the US Fed kept its policy rate unchanged in the range of 2.25 - 2.50% while hinting at rate cuts in future.
- Tensions between Iran and Western Nations intensified as two Saudi Arabian tankers were attacked in Strait of Hormuz, allegedly by Iran

Major events to be aware of:

Domestic

Event	Timeline/comments
Q1FY20 Earnings	August
Monsoon updates	IMD forecasts monsoons to return to normalcy in August/Sep after deficiency in June and July
Institutional Flows	Post Budget
RBI actions on liquidity	Post MPC
Auto Sales	Monthly Sales data for August & September

Global

Event	Timeline/comments
Brexit Update	31 October
Earnings Trend in US	August
US/Europe GDP forecasts	Economic growth in the key economies (US, Germany and other leading European nations) needs to be closely watched

Update August 2019

Budget Highlights – Didn't live Up to Expectations

- **Strong Infra Push** : Budget gave impetus to housing, water solutions, transportation, power transmission, etc. were highlighted in budget but funding requirement were inexplicit.
- **Disinvestment Target**: FY20 Disinvestment target at Rs. 1,050bn and Government willing to reduce stake to <51% but not willing to give up control
- **Buyback Tax**: Introduced tax on buyback at 20% (in-line with Dividend Distribution Tax)
- **Unintended FPI surcharge**: Surcharge on individual income tax categories at 3% on income of Rs2-5 crs and 7% on > Rs. 5 crs; For FPIs registered as trust with > Rs.5 crore of taxable income, effective tax increased from 35.8% to 42.7%
- **Recapitalizing PSU Banks**: Earmarked Rs. 70,000 crs to capitalise PSBs aimed at boosting credit growth.
- **Liquidity easing**: Banks encouraged to purchase high rated pooled assets of NBFCs worth Rs. 1 lakh crs, on which government proposes one time six month credit guarantee of first loss of 10% loss.
- **Fiscal Deficit target** revised from 3.4% to 3.3%.
- Proposed change in **Maximum Promoter Shareholding** limit to be brought down from 75% to 65%

Budget aimed for all-round Infrastructure development and stick to fiscal discipline but did not solve any imminent concerns like liquidity, slowing consumption, rural distress and subdued private sector capex.

Slowdown Evident

- Rural wages suppressed over the last 2 years
- Liquidity concerns, difficult credit environment and subdued rural demand resulting in slowdown in consumer demand
- Monthly Auto Production numbers continue to see de-growth; in addition, production cuts seen across Automobile companies

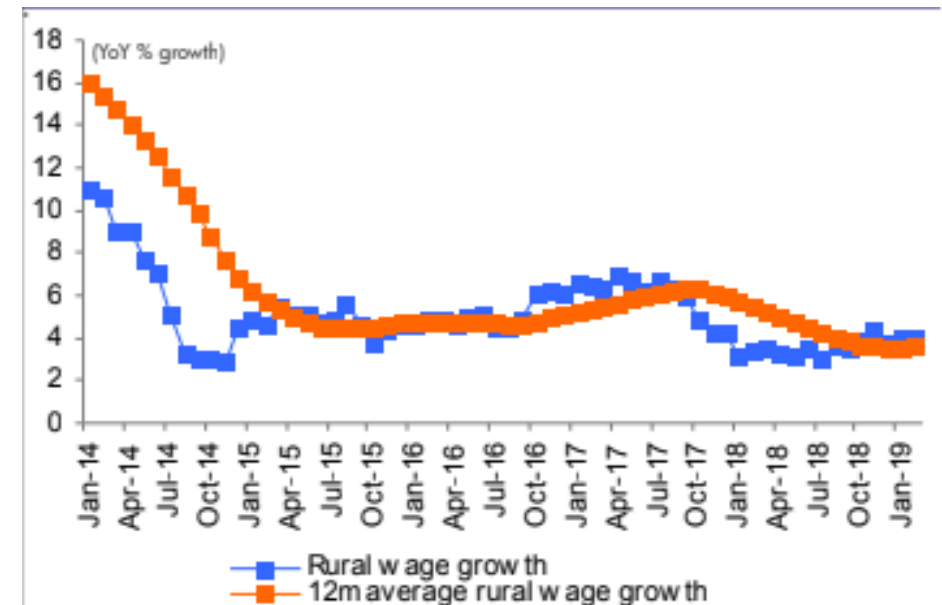
Monthly Auto Sales- Key companies

Company	July 2019	July 2018	YoY	July 2016	3 year CAGR	YTD Performance*
2W						
Hero	535,810	679,862	-21%	532,113	0%	-15%
Bajaj	170,978	201,433	-15%	174,324	-1%	-2%
TVS	208,489	247,382	-16%	206,605	0%	-6%
PVs						
Maruti	96,478	152,427	-37%	125,764	-8%	-25%
Hyundai	39,010	43,481	-10%	41,201	-2%	-8%
M&M	16,831	19,781	-15%	17,356	-1%	-5%
Tata Motors	10,485	17,079	-39%	13,547	-8%	-32%

Source: SIAM, Company data, Jefferies

* YTD Performance is for FY20, i.e. April-July 2019 vs. April-July 2018

Rural wage growth trend



Source: Antique Research

Monetary Policy – Priority to fuel growth

- RBI cut Repo rate by 50bps cumulatively in the June Quarter and followed it up with 35bps cut in the August Policy meeting.
- Stance changed from 'Neutral' to 'Accommodative' in the June MPC meeting
- GDP growth forecasts have been revised down due to weakness in domestic and external demand conditions

	Feb 2019	April 2019	June 2019	August 2019
Repo Rate	6.25%	6.0%	5.75%	5.4%
GDP forecast (FY20)	7.4%	7.2%	7.0%	6.9%
CPI forecast (H1 FY20)	3.2-3.4%	2.9 - 3.0%	3.0 - 3.1%	3.1%**
CPI forecast (H2 FY20)		3.5 - 3.8%	3.4 - 3.7%	3.5-3.7%
Stance	Neutral*	Neutral	Accommodative	Accommodative

* Stance in Feb 2019 was changed from calibrated tightening to Neutral

** 3.1% is Inflation forecast in August 2019 policy for Q2FY20

Source: RBI

Earnings Review Q1FY20

Industry	No of companies	Sales growth	PAT growth
Private Banks**	8	23%	37%
NBFCs (excludes HFCs)**	5	20%	5%
Housing Finance**	3	15%	-1%
PSU Banks**	3	14%	Turns positive
Consumer Durables	3	13%	-7%
IT - Software	5	11%	7%
Infra*	5	10%	-12%
Oil & Gas	4	9%	-20%
Pharma	4	9%	33%
FMCG *	8	6%	12%
Cement & Construction Materials	2	5%	26%
Telecom	2	4%	-369%
Autos - 2W /3W	4	-1%	6%
Metals	2	-4%	-39%
Autos - Passenger Vehicles	2	-6%	-38%
Autos - LCV	2	-8%	-137%
Others	11	28%	5%

Source: Company data, Ace Equity.

Q1FY20 earnings for BSE-100 companies reported so far(73 out of 100)

** For Banks and NBFCs, Sales is total Interest Income

Q1FY20 Earnings Trend

- Of the 74 companies that reported Q1 earnings, total sales grew by 9% and PAT by 5% yoy
- **Private Banks** saw strong earnings growth on the back of strong operating performance and improvement in asset quality
- **PSU Banks** cumulatively turned profitable, primarily on the back of improvement in asset quality and losses the previous year; management commentary and results pointed to bottoming out of NPAs.
- **NBFCs** saw slowdown in loan growth and pressure on NIMs. However, Bajaj Finance defied all odds and continued its growth momentum
- **Autos:** Weakness in Auto Sales was evident in earnings; 2W industry did relatively well.
- **IT :** Earnings for IT industry was led by Infosys and TCS; Companies saw margin pressures and tapering of growth (ex- Infosys)
- **Cement:** Companies saw strong earnings growth due to higher realisation. Due to elections volume growth was tepid
- **Consumer Durables:** Demand consumer durables remained strong aided by strong summer.
- **FMCG :** Industry saw stable volume growth
- **Infra:** Execution and order intake were sluggish due to election

Source: Company data, Ace Equity.

Q1FY20 earnings for BSE-100 companies reported so far (73 out of 100)

Sectoral Outlook

Sector	Comments
Banks	See strong credit growth and continued improvement in asset quality
Infrastructure & Capital Goods	Demand driven by robust government spending across Housing, public infrastructure, irrigation and transportation.
IT	Supported by weak rupee, increasing market share and better business models of Indian IT services vendors
Autos	Near-term demand muted due to BS-VI transition and increasing costs. However, long-term story remains intact
Insurance	Significant under-penetration currently and increasing financial inclusion to drive growth
FMCG	Near term demand subdued due to slowing rural economy
Metals	Global slowdown and trade tension to continue to lead to demand headwinds
Telecom	Increasing competitive intensity and mounting debt to put pressure on financials
NBFCs	Government's thrust on improving liquidity and improving regulatory oversight to lead to resumption of credit growth and stable asset quality

Global Indices in July

Index Name	Country	31 July 2018	28 Jun 2019	31 July 2019	1 Month Return (%)	1 Year Return (%)
Developed Economies						
FTSE 100	UK	7,749	7,426	7,587	2%	-2%
Nasdaq	US	7,672	8,006	8,175	2%	7%
Nikkei 225	Japan	22,554	21,276	21,522	1%	-5%
Dow Jones	US	25,415	26,600	26,864	1%	6%
Swiss Market	Switzerland	9,174	9,898	9,919	0%	8%
NYSE	US	12,963	13,050	13,067	0%	1%
CAC 40	France	5,511	5,539	5,519	0%	0%
Straits Times	Singapore	3,320	3,322	3,301	-1%	-1%
DAX	Germany	12,806	12,399	12,189	-2%	-5%
Seoul Composite	South Korea	2,295	2,131	2,025	-5%	-12%
BRICS						
Bovespa	Brazil	79,220	100,967	101,812	1%	29%
RTS Index	Russia	1,173	1,381	1,360	-1%	16%
Shanghai Composite	China	2,876	2,979	2,933	-2%	2%
Hang Seng	Hong Kong	28,583	28,543	27,778	-3%	-3%
S&P BSE SENSEX	India	37,607	39,395	37,481	-5%	0%
NIFTY 50	India	11,357	11,789	11,118	-6%	-2%
Other Emerging Economies						
Taiwan Weighted	Taiwan	11,058	10,731	10,824	1%	-2%
MerVal	Argentina	29,287	41,796	42,058	1%	44%
Jakarta Composite	Indonesia	5,936	6,359	6,391	1%	8%
KLSE Composite	Malaysia	1,784	1,672	1,635	-2%	-8%

Indices Performance in July

Index Name	31-Jul-18	28-Jun-19	31-Jul-19	1 Month Return (%)	1 Year Return (%)
NIFTY Pharma	9,179	8,065	7,988	-1%	-13%
NIFTY FMCG	31,007	29,546	29,066	-2%	-6%
NIFTY IT	14,588	15,936	15,620	-2%	7%
NIFTY Media	2,833	2,040	1,958	-4%	-31%
NIFTY Consumption	5,248	4,756	4,488	-6%	-14%
NIFTY 50	11,357	11,789	11,118	-6%	-2%
NIFTY Realty	273	285	267	-6%	-2%
Nifty Financial Services	11,663	13,556	12,707	-6%	9%
NIFTY Bank	27,764	31,105	28,876	-7%	4%
NIFTY Private Bank	15,613	17,197	15,917	-7%	2%
NIFTY Infra	3,158	3,369	3,087	-8%	-2%
NIFTY Energy	15,150	16,047	14,559	-9%	-4%
Nifty Midcap 100	18,877	17,654	15,921	-10%	-16%
Nifty Smallcap 100	7,466	6,200	5,522	-11%	-26%
NIFTY Auto	10,974	7,928	6,852	-14%	-38%
NIFTY PSU Bank	3,186	3,206	2,756	-14%	-13%

July & August sees FII selling and Domestic Buying

(in Rs. Crore)	July-2019	Week ending August 8th
FII Activity		
Gross Purchase	92,247	20,557
Gross Sale	109,117	25,503
Net Investment	(16,870)	(4,946)
DII Activity		
Gross Purchase	92,650	18,616
Gross Sale	72,256	13,633
Net Investment	20,394	4,983

- Post surcharge on FPI Trusts, market witnessed sharp fall due to FPI selling
- Global uncertainties ,stronger dollar and mixed domestic macros resulted in further selling
- Price decline in mid and small caps was steeper

Events that have rocked the markets in July - Aug

- **Tariff war escalation** – US Government announced that it would levy additional 10% tariff on \$300bn worth of Chinese goods
- **Yuan devaluation/depreciation** - China devalued its currency by 2% in 3 days to the lowest point in 2008; US officially declares China as “Currency Manipulator”
- **Iran issue** – Issues between Iran and Western Nations intensified in July & August
- **Fed Policy and outlook** – US Central Bank cuts Fed Rate by 25bps in August policy
- **Section 370** – Indian government scraps Article 370 and bifurcates the J&K state into 2 union territories, integrating it with mainstream India.
- **Japan-South Korea trade tensions:** Japan restricts exports of critical material used in South Korea’s High-Tech Industry.
- **Brexit update:** Theresa May replaced by Boris Johnson as Prime Minister; Uncertainty regarding hard Brexit continues
- **Monsoon Update:** Early deficiency of monsoon recovers but rainfall concentration in parts created havoc

Outlook for Asset Classes

Asset Classes	Performance in Q1FY20	Start to End Value In Q1FY20	Outlook for Q2FY20	Remarks
Debt	10-Year Gilt: down 47 bps 3-M T Bill: down 28 bps 6-M T Bill: down 19 bps 3-M CP: down 120 bps 1-Yr CP: down 110 bps 10-Yr AAA Corp: down 30 bps Call Rate: down 44 bps	7.35-6.88 6.31 - 6.03 6.35 – 6.16 8.3 – 7.1 9.1– 8.0 8.43– 8.13 6.02– 5.58	Gilt yields moderated sharply post the announcement of issue of Sovereign Bonds overseas. Further decline will wait for cues. Short term rates are likely to moderate post RBI rate cuts	This view will be negated once the Govt goes ahead with the first tranche of Bond issues overseas. Inflation is likely to moderate further. An uptrend will also cause yields to climb higher
Equity	Sensex: Up 1.8% Nifty: Up 1.4%	38,673– 39,395 11,624– 11,789	Post the sharp correction in July, resumption of FII flows, Q1FY20 results largely on expected lines and normal monsoon will cause an uptrend in the markets to resume	FPI Flows and Global events will have the most profound impact on markets this quarter.

Thank you