EQUITY MARKET REVIEW

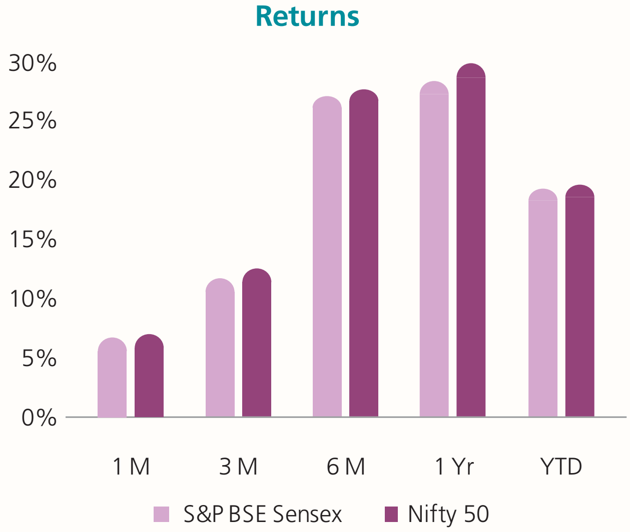
FEBRUARY, 2021

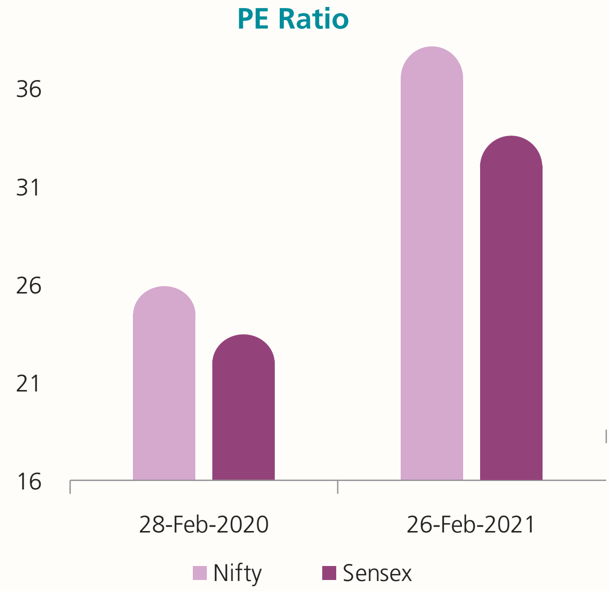
L&T Financial Services
Mutual Fund

After lagging behind in January, Indian equities significantly outperformed Emerging Markets (EMs) on post-budget euphoria. The Union Budget which was presented on February 1, 2021 stressed upon higher public capital expenditure. The FY21 fiscal deficit outturn came in much higher than expectations at 9.5% of GDP. 4Q20 GDP growth disappointed at 0.4% (YoY), underpinned by weak service sector growth. The focus over the month was on December-quarter earnings. Adjusted PAT for the BSE All Cap grew at 33% (YoY) in 3QFY21. Close to 70% of this was on account of Materials/Energy – benefitting from ongoing commodity inflation.

MSCI India (US$) rose 5.1% in February and significantly outperformed the peers MSCI APxJ (+3.8%) and MSCI EM (+4.4%). Nifty50 and S&P BSE Sensex ended the month of February with 6.6% and 6.1% returns, respectively outperforming emerging markets. Midcaps and Smallcaps outperformed the largecaps by 4.4% and 6%, respectively in February.

Among broader markets, the Midcap index outperformed the Largecap index by 440 bps while the Smallcap index outperformed the Largecap index by 600 bps. BSE Midcap and BSE Smallcap indices ended the month of February with 10.5% and 12.0% returns, respectively.





Past performance may or may not be sustained in the future.

GLOBAL MARKETS

Global equities continued to trade higher and exhibited unusually broad momentum, delivering 12-month highs on several equities benchmarks up until the middle of the month. The last two weeks, however, saw broad deleveraging across equities and global asset classes. Equities saw a global sell-off in risky assets amidst a sharp rise in bond yields. Investors struggled with little improvement in the US labor market and weighed a rise in bond yields on worries about potential inflation (with oil prices at a 12-month high and copper price near a decade-high).

The VIX index was down 16% (MoM) to end the month at 28 following a 45% gain in January. The IMF, World Bank and our JPM economists have all recently revised global growth higher. Economic output is expected to grow at 5-6% this year, making it the fastest pace since the mid-80s.

Worldwide, major indices saw positive trends. Nikkei was the outperformer with 4.7% returns, followed by Euro Stoxx (+4.5%) and Dow Jones (+3.2%). Hang Seng and FTSE were the worst performers with 2.5% and 1.2% returns, respectively.

SECTOR PERFORMANCE

Indian equity markets outperformed the MSCI Emerging Market Index. Utilities, Energy and Industrials outperformed while Staples and IT were the notable laggards in February. Metal was the best performing sector with 24.4% returns outperforming Sensex by 18.3%. Power (20.7%), Realty (15.2%), Oil & Gas (12.5%), Bank (12.5%), Capital Goods (10.5%), Consumer Durables (5.5%) outperformed Sensex. Auto (3.7%), Healthcare (1.1%), and IT (-1.6%) underperformed the Sensex. FMCG was the worst-performing sector, dipping by 2.1%.

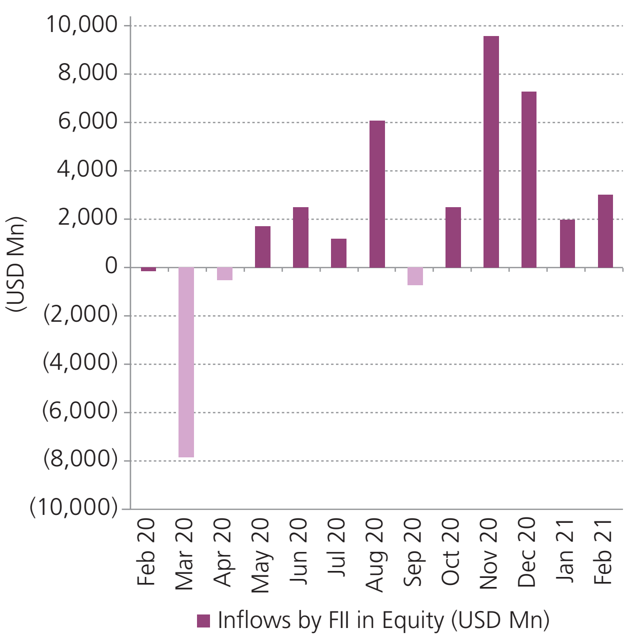
INSTITUTIONAL ACTIVITY

FIIs recorded monthly inflows of US$4.1bn into Indian equities in the month of Feb vs. outflows of $2.0 bn in Jan'21 taking FY21 net inflows to $36.2 bn. This is the 5th consecutive month of inflows. DIIs remained net equity sellers in Feb with outflows of US$2.2 bn in Feb vs. outflow of US$1.6 bn in Jan taking FY21 tally of outflows to $18.9 bn.

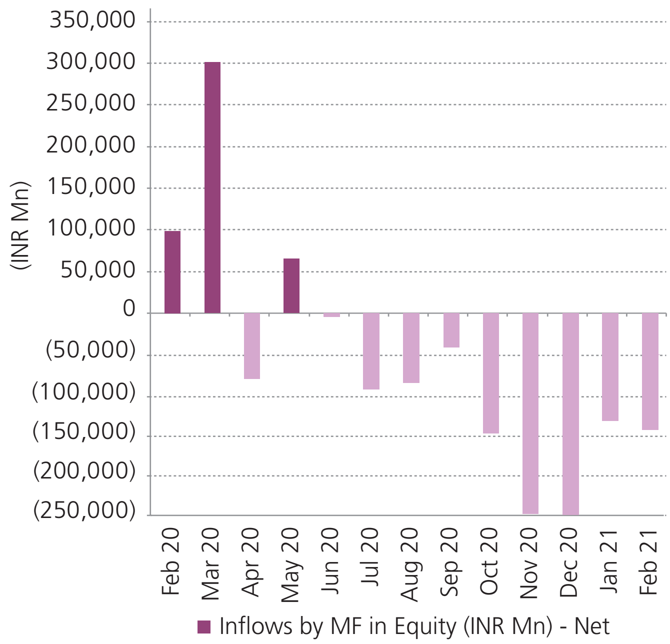
Within DIIs, Mutual Funds were net sellers, while insurance funds were small buyers in Feb. Mutual funds were net equity sellers at $2.0 bn while insurance funds bought $206 mn of equities in Feb.

Mutual fund and insurance fund flow data is as of February 16, 2021.

Inflows by FII in Equity (USD Mn) - Net



Inflows by MF in Equity (INR Mn) - Net



MACRO-ECONOMIC DEVELOPMENTS

India's much-anticipated post-COVID budget struck the right chords by increasing transparency (bringing some off-balance sheet liabilities back on the books), doubling down on budgetary capex spend, seeking to jumpstart asset sales, and signaling an intention to commence some financial sector reforms. There is increased focus/spending on infrastructure by increasing capex by 26%. The Central Government will exceed budgeted spends on roads/railways during COVID-19 (FY21), and forecasts further 18% growth on Roads in FY22 (to Rs 1.08 tn).

4QCY20 GDP growth disappointed at 0.4% YoY, underpinned by weak service sector growth. Despite the downside surprise, sequential growth was strong at 25% QoQ, taking GDP to 96% of its 1QCY20 pre-pandemic level.

Headline CPI for Dec at 4.1% was slightly below expectations largely led by food prices dropping 1% MoM. The core-core inflation (core inflation ex gasoline and diesel) increased 0.5% MoM in Jan after a 0.3% rise in Dec likely reflecting a combination of pent-up demand and input cost pressures.

Composite PMI increased by 0.9 pt MoM to 55.8 in Jan, following a 1.4 pt MoM decline in Dec. Helped by stronger demand conditions, Services PMI rose to 52.8 in January from 52.3 in December, while Manufacturing PMI inched up to 57.7 in January from 56.4 in December. The forward-looking demand indicators remained constructive with composite new orders remaining strong at 55.9, increasing 1.0 pt MoM. The composite new export orders reading remained below 50, pulled down by the services sector. But it printed at 47.9 in January, a 1.7 pt MoM increase. The rise was contributed by both the manufacturing and the services sector. But the sub-index remained lackluster for services (38.5) compared to manufacturing (53.9), where the export orders have largely recovered.

Nov IP increased by 1.0% YoY in Dec and came above cons forecast. In level terms, industrial production was at 95% of its pre-pandemic level. Production for both consumer durables (98%) and non-durables (98%) is just below pre-pandemic levels. This contrasts with capital goods where production is at 89% of pre-pandemic levels.

The trade deficit remained elevated at US$14.5 bn in January, inching down from US$15.4 last month. The widening of the deficit has been underpinned by a jump in imports as activity continued to normalize, and a rise in crude oil prices, even as exports were strong as well. India's FX reserves are close to their all-time peak at $584 bn as of 19th Feb. FX reserves have decreased by US$1.5 bn in the last 4 weeks. INR lost 0.7% and ended the month at 73.47/$ in Feb.

Benchmark 10-year treasury yields averaged at 6.09% in Feb (19 bps higher vs. Jan avg.). US 10Y yields are at 1.4% (34 bps MoM, +26 bps YoY). Brent oil price gained 17.5% MoM in Feb to end the month at US$64.4/bbl.

Fiscal deficit for Apr-Jan came at INR 12.3 tn or 67% of the budgeted FY21 deficit (INR 18.5 tn). This compares to 106% reached during the same time frame in FY20.

OUTLOOK

MSCI India outperformed MSCI EM by 5.4 percentage points and ranked 6 performance-wise in the EM cohort. On an absolute basis, the index retraced significantly from its mid-February high, underpinning a volatile month for equities. India's performance rank in EM stood at 6th (among 27 EMs) vs. 16th in January. The BSE S&P Sensex continued to underperform the Broader Market in February, while the MSCI India Growth index underperformed the Standard and Value indices for the 3rd month in a row.

High-frequency data points for February continue to reflect sustained positive growth in YoY terms, indicating a favorable growth outlook in the near term. E-way bills for February continue to record double-digit growth at 15.6% YoY. The synchronous uptick in PV sales to 22% YoY in February, 10-month high credit growth in February, lower unemployment rate and composite PMI at a 4-month high indicate sustained recovery. Growth momentum is expected to gain further strength in the near term. The economy is at an inflection point, led by a supportive policy mix with strengthening demand, which should revive the private capex.

Improvement in economic activity is reflected in GST collections as February witnessed another month with GST revenue remained above the INR 1 trillion mark. This was 5th consecutive month with collections of more than Rs 1 trillion. The sustained GST collection and several other data points show the economy moving close to normal across most segments.

Positive growth momentum is likely to strengthen further, helped by normalization of economic activity and rollout of the vaccination program. With Budget 2021 and announced PLI schemes, the government has targeted both the public and private capex. Overall, supportive monetary and fiscal policy along with strengthening domestic and external demand which will subsequently facilitate an uptick in private capex, augurs well for a virtuous growth cycle ahead.

Source: Bloomberg, MSCI