EQUITY MARKET REVIEW

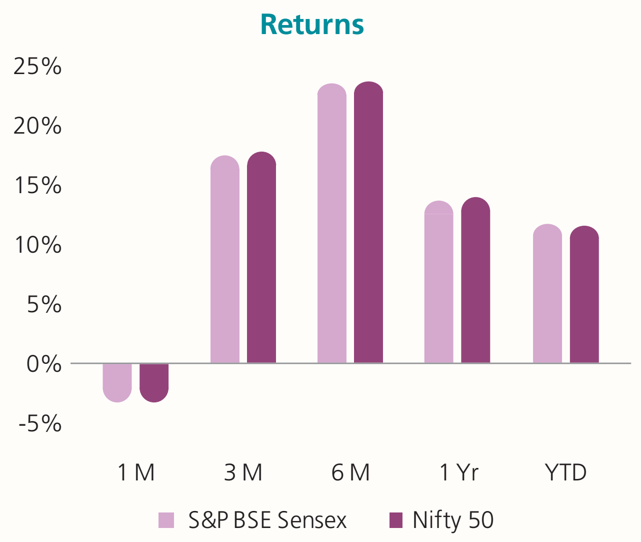
JANUARY, 2021

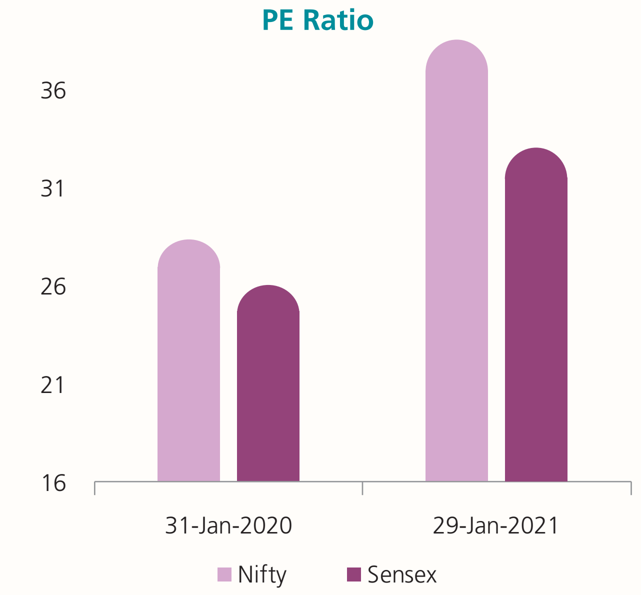
L&T Financial Services
Mutual Fund

Indian equities underperformed Emerging Markets (EMs) in January after outperformance in December. Domestically, the focus was on the December quarter earnings. Among the Nifty companies, earnings beats to consensus forecasts were seen for more than 70% of the companies reported in the month of January (~55% of the Nifty companies have reported December quarter earnings). India reached the peak of the COVID-19 pandemic in mid-September and has witnessed declines in daily cases and a number of deaths since then.

MSCI India (US$) declined 2.4% in January and significantly underperformed peers MSCI APxJ (+3.4%) and MSCI EM (+3.0%). Nifty50 and S&P BSE Sensex ended the month of January with (-2.5%) and (-3.1%) returns, respectively. Midcaps and Smallcaps outperformed the large caps by ~3% in January.

Among broader markets, the Midcap index outperformed the Largecap index by 390 bps while the Smallcap index outperformed large cap index by 250 bps. BSE Midcap and BSE Smallcap indices ended the month of January with 0.8% and -0.6% returns, respectively.





GLOBAL MARKETS

Global equities traded higher during the first 3 weeks of the month but saw a sharp decline in the last week with MSCI ACWI ending the month down 0.5% in January. This follows strong returns in the previous two months with December (+4.5%) and November (+12.2%).

European equities (SXXP -1.6%) underperformed relative to their US peers (SPX -1.1%) in January led by a weaker EUR (-0.7%). VIX index was up 45% (MoM) to end the month at 33.09 following an 11% gain in December. COVID-19 second/third waves broadened during the month. The global growth outlook remains for a modest Q1 slowdown to below trend due to the virus and lockdowns, but a sharp acceleration from Q2 as economies reopen and vaccines are deployed.

Worldwide, major indices saw mixed trends. Hang Seng was an outperformer with 3.9% returns, followed by Nikkei (+0.8%) and FTSE (-0.8%). Dow Jones and Euro Stoxx were the worst performers with -2% returns each.

SECTOR PERFORMANCE

Indian equity markets underperformed the MSCI Emerging Market Index. Industrials, Discretionary, IT and Communication Services outperformed while Energy and Healthcare were notable laggards in January. Auto was the best performing sector with 6.3% returns outperforming Sensex by 9.4%. Capital goods 3.9%, IT 2.4%, Consumer Durables -1.0%, Oil & Gas -2%, Realty -2.4%, Power -2.8% outperformed Sensex. FMCG -3.1%, and Bank -3.4%, underperformed the Sensex. Healthcare and Metals were the worst performing sectors with -4.9% returns, respectively.

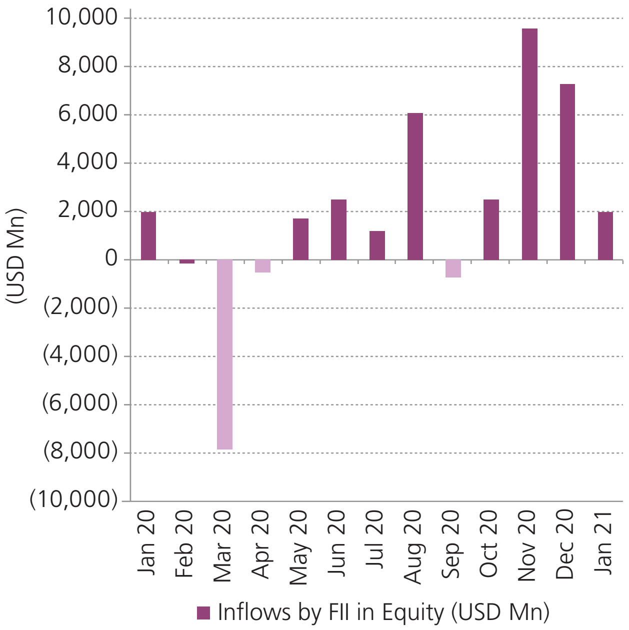
INSTITUTIONAL ACTIVITY

FIIs recorded monthly inflows of US$2.6 bn into Indian equities in the month of Jan vs. inflows of $7.3 bn in Dec'20 taking FY21 net inflows to $32.7 bn. This is 4th consecutive month of inflows.

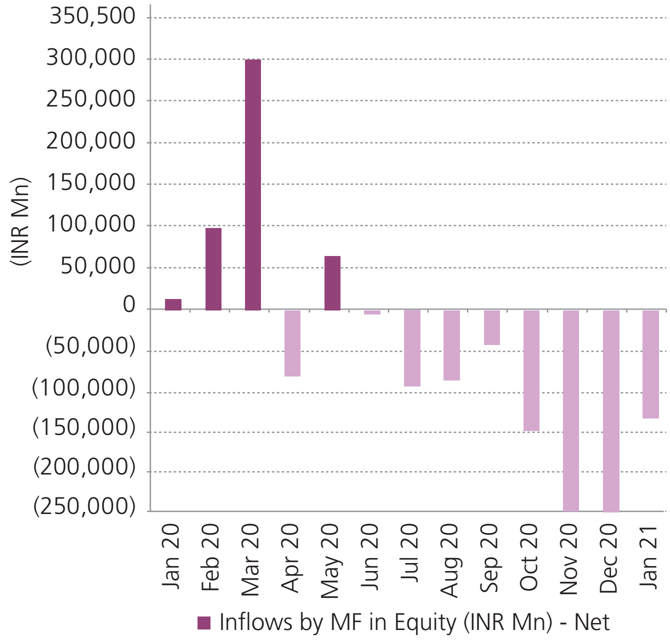
DIIs remained net equity sellers with outflows of US$1.6 bn in Jan vs. outflow of US$5.1 bn in Dec taking FY21 tally of outflows to $16.7 bn. Within DIIs, both Insurance funds and mutual funds were net sellers in Jan. Mutual funds were net equity sellers at $2.2 bn while insurance funds sold $58 mn of equities in Jan.

Mutual fund and insurance fund flow data is as of 25th Jan.

Inflows by FII in Equity (USD Mn) - Net



Inflows by MF in Equity (INR Mn) - Net



MACRO-ECONOMIC DEVELOPMENTS

Economic Survey published ahead of the Union Budget estimates FY21 GDP contraction at 7.7% and a growth of 11% in FY22. This implies real GDP growth of 2.4% over FY20. The economic survey estimates GDP growth to be aided by normalization of economic activity supported by the roll-out of COVID-19 vaccines, government reforms and pick-up in credit demand given adequate liquidity and low-interest rates.

The Union Budget FY21 surprised with a larger-than-expected headline forecast deficit, though a large part of this was on account of clearance of historical food subsidies. 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). An additional Rs 440 bn has been set aside as contingency Infra spends (should the need arise), and another Rs 200 bn will be used to seed a new Infrastructure Development Finance Institution.

Headline CPI for Dec at 4.6% was below than the market expectations largely led by food inflation (3.4% in Dec vs. 9.5% in Nov). The core-core inflation (core inflation ex gasoline and diesel) declined to 5.3% in Dec vs. 5.5% YoY in Nov. With inflation still expected to remain above the 4% average over the next two quarters.

Composite PMI declined by 1.4 pt MoM to 54.9 in Dec, following a 1.7 pt MoM decline in Nov. The decline in December was led by services which declined 1.4pt MoM to 52.3 while the Manufacturing PMI rose marginally by 0.1 pt MoM to 56.4. The forward-looking demand indicators remained constructive with composite new orders remaining strong at 54.9, though easing 0.9 pt MoM. However, the composite new export orders readings have remained below 50 throughout the recovery, printing at 46.2 in December (-1.3 pt MoM). This weakness is due to services, where the sub-index remained lackluster (37.1) compared to manufacturing (51.8), where export orders have largely recovered.

Nov IP declined by -1.9% YoY vs. 3.6% gain in Oct and came below cons forecast. Sep and Oct production benefited from both a) the pent-up demand as the economy was unlocking and b) inventory accumulation ahead of the festive season in November. Production for both consumer durables (98%) and non-durables (99%) are just below pre-pandemic levels. This contrasts with capital goods where production is at 93% of pre-pandemic levels.

India's monthly merchandise trade balance at US$15.44bn in Dec widened from US$9,87bn in Nov. Merchandise exports were up 0.1% YoY in Dec (vs. 8.7% decline in Nov) and imports were up 7.6% YoY in Dec (vs 13.3% decline in Nov). Imports ex Oil and Gold up 8% YoY, the first month with positive YoY print after 22 consecutive months of YoY declines. India's FX reserves are close to their all-time peak at $585.3 bn as of 22nd Jan. FX reserves have increased by US$4.5bn in the last 4 weeks. INR gained 0.2% and ended the month at 72.95/$ in Jan.

Benchmark 10-year treasury yields averaged at 5.9% in Jan (2 bps higher vs. Dec avg.). US 10Y yields are at 1.07% (-15 bps MoM, -44 bps YoY). Brent oil price gained 7.2% MoM in Jan to end the month at US$54.9/bbl following an 8.5% MoM gain in Dec. For CY20, oil prices declined 23% YoY on year-end values.

GST collections in January came at Rs1.19tn (+8.1% YoY), the highest monthly collection since GST was implemented in Jul-17. This was the 4th consecutive month with collections of more than Rs1tn.

The fiscal deficit for Apr-Nov came at INR 11.6tn or 145% of the budgeted FY21 deficit (INR 8.0tn). This compares to 122% reached during the same time frame in FY20.

OUTLOOK

MSCI India underperformed EM by 5.4% and ranked 16 performance-wise among EM vs. 9th in December. The BSE Sensex continued to underperform the Broader Market in January, while the MSCI India The growth index underperformed the Value indices for the 2nd month in a row. Sector rotation breadth and depth declined (MoM). India's underperformance is expected to decline given the gradual reopening of the economy. COVID-19 cases in India continue to decline from their peak in mid-September. The economy is responding positively to the sustainability of the recovery is seen post reopening.

High-frequency data suggest that economic activity continues to improve, even though it remains uneven across sectors. Urban indicators such as travel & hospitality, traffic and realty are improving. Electricity consumption continues to remain higher than year-ago levels. Railway freight volume, Petro products consumption continued to increase (MoM). India's mobility levels recovery has improved compared to a group of select countries on account of lockdowns in Europe and the US. Broader indicators are broadly flat (MoM). Pick-up in government revenues /spending, declining COVID cases and rising vaccinations are positive.

Improvement in economic activity is reflected in GST collections as Jan witnessed the highest ever monthly collection since GST implemented in July-17. This was 4th consecutive month with collections of more than Rs 1 tn. The sustained GST collection and several other data points show the economy moving close to normal across most segments.

With several economies executing fiscal expansion, an expansion in India is less likely to be punished. Budget 2021 surprised with a larger-than-expected headline forecast deficit. There is an increased focus on spending on infrastructure. Transportation Infra spend has seen a significant increase of 26%. This will kick-start the investment cycle leading to focus back on growth. Key beneficiaries will be the segments linked to infra and consumption. Further, govt. had already initiated its efforts towards making India a strong manufacturing destination under the broader theme of *Atmanirbhar Bharat and Make in India.* This is supported by improved technical capabilities of domestic firms, ease of doing business and Production Linked Incentive Schemes. The Indian economy has recovered strongly from COVID-19 and the multiple initiatives/reforms taken by the government will continue to keep it on a firm footing.

Source: Bloomberg, MSCI