asset 360 ONE

panorama

June 2023

Key Insights:

Margin expansion lifts corporate sector performance

- Manufacturing sector was dragged down by metals, while Services was impacted by mediocre IT performance
- Steep fall in WPI inflation reflected in the moderation of raw material costs
- Continued correction in WPI inflation is expected to bolster margins in Q1FY24 as well
- Global commodity prices continue to correct on growth concerns
- Consumer-facing sectors witness decline in sales growth in April-May 2023

Strong growth in wages observed across rural and urban regions

- Higher wages leading to an increase in employee expenses for services sector firms
- Elevated unemployment rates can slow wage growth, but there may be variations across sectors
- Banking and Real Estate witness strong hiring activity while IT sector lags on weak growth prospects

Global rate hike cycle coming to an end, but risks persist

- Central Banks to maintain higher interest rates throughout 2023, prioritizing caution in terms of inflation
- Risk sentiments expected to improve with end of global rate hike cycle, boosting equity flows into EMs
- RBI likely to maintain repo rate at current levels in 2023, assuming inflation follows expected trajectory
- Underlying inflation momentum subsiding, leading to less generalized inflation

Corporate Performance & Outlook

Margin expansion lifts corporate sector performance

Manufacturing sector dragged down by metals, while services impacted by mediocre IT performance

Performance of Listed Non-Financial Companies (YoY%)

Improvement in operating profit despite moderation in sales growth indicates margin expansion

Metals, capital goods, textiles, and chemicals impede sales growth

Metals weighed down the overall performance of manufacturing sector with profits contracting 55% YoY in Q4

Due to stability concerns in the global BFSI sector, the performance of the IT sector was mediocre

Services sector also witnessed moderation in sales growth

Margin expansion observed across both manufacturing and services sectors

Consumer-facing sectors demonstrated improved sales growth

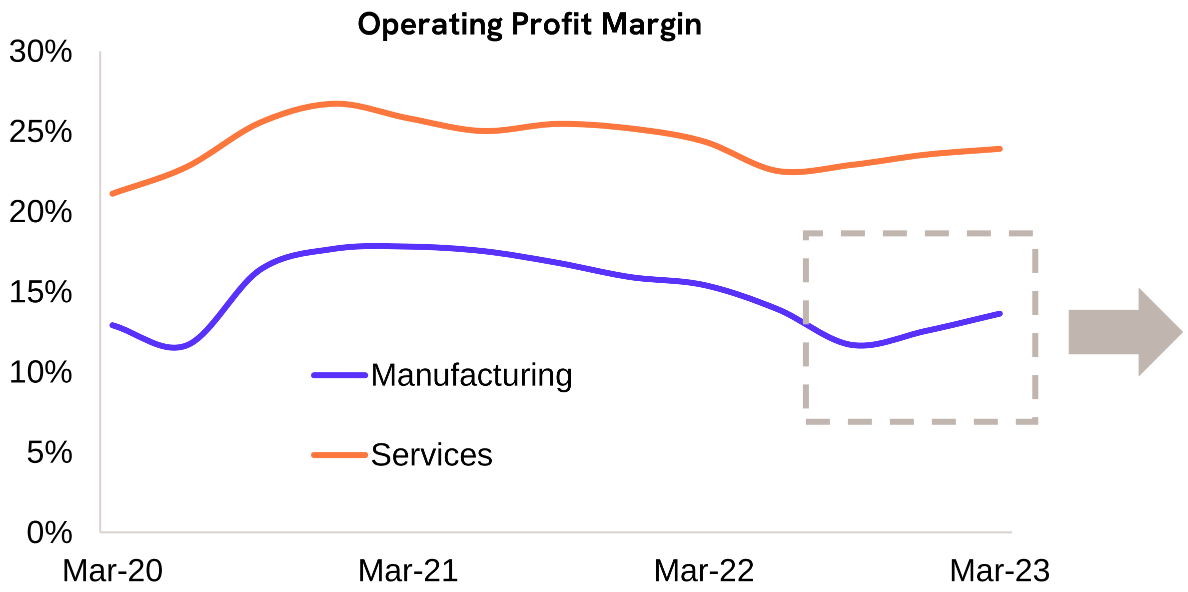
Note: Performance based on a set of 2154 listed non-financial companies

Source: ACE Equity, 360 ONE Asset Research

BFSI: Banking, Financial Services, and Insurance, Operating profit: EBITDA – other income

Steep fall in WPI inflation reflects in moderation of raw material costs

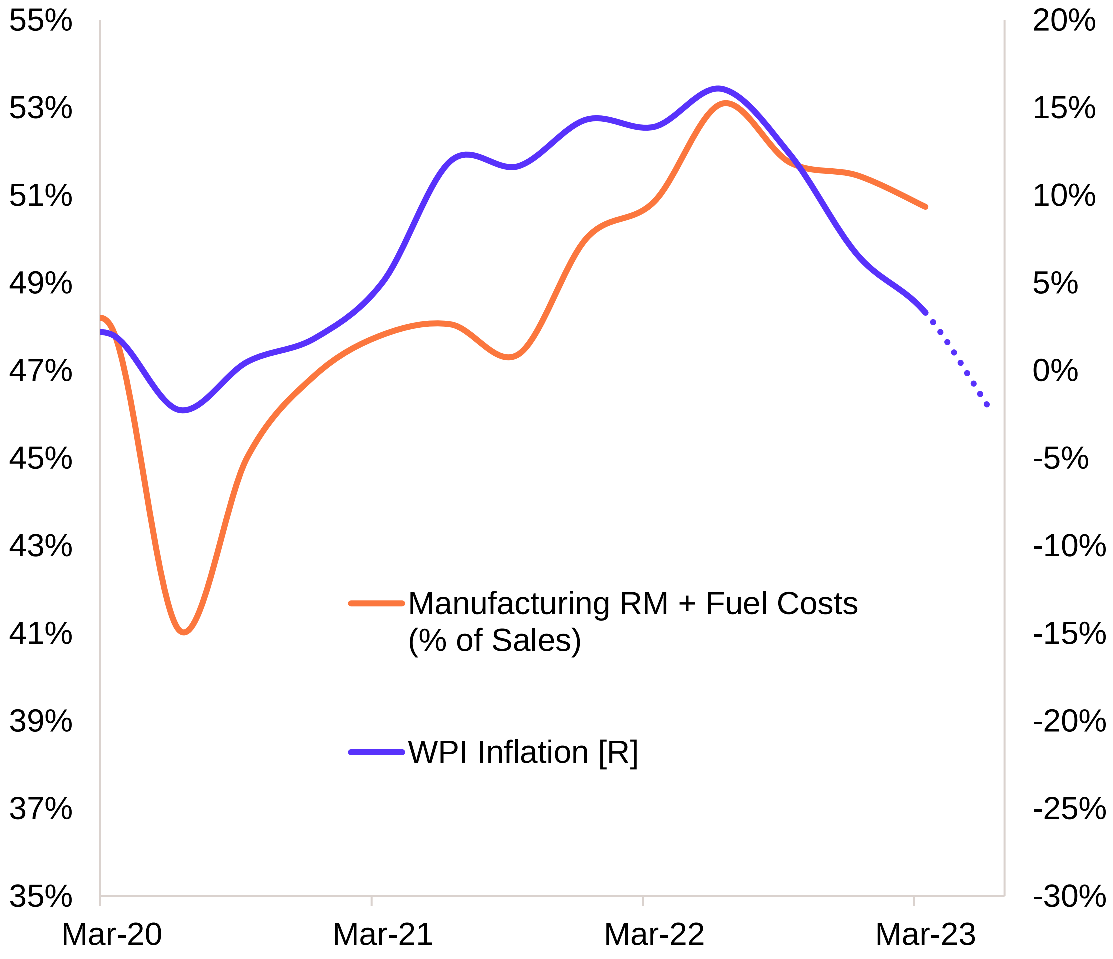
Ongoing correction in WPI inflation expected to bolster margins in Q1FY24 as well



Manufacturing sector experienced a significant improvement in operating margins due to a decline in raw material costs, including fuel

Decline in costs is in line with steep correction in WPI inflation

The ongoing correction in WPI inflation, driven by falling commodity prices, is expected to support margins in Q1FY24 as well

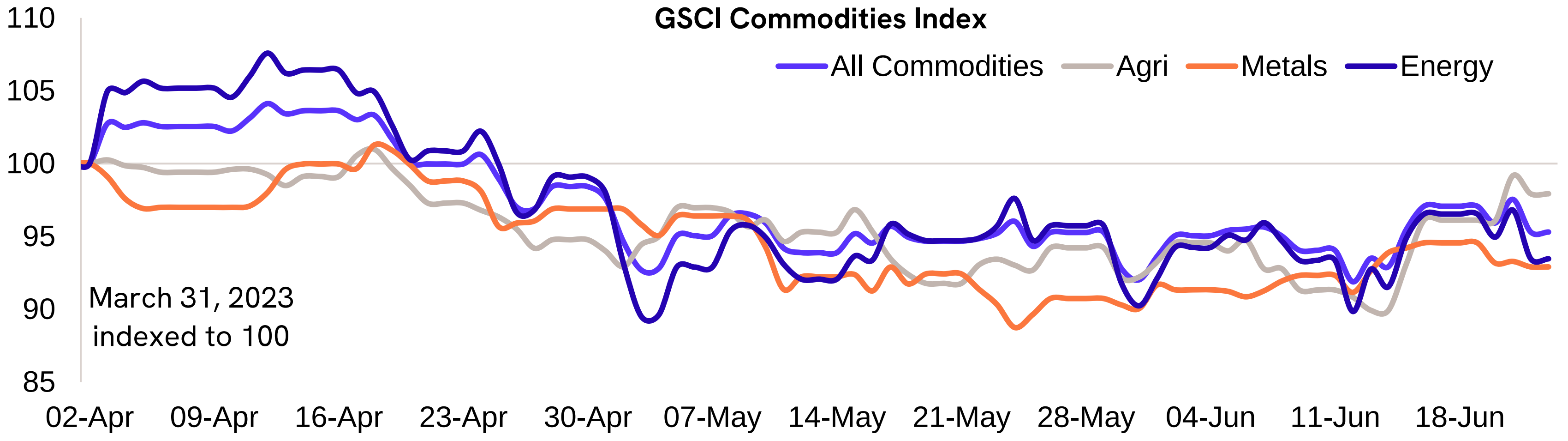


Source: ACE Equity, Office of Economic Advisor, 360 ONE Asset Research

Note – RM: Raw Material, WPI: Wholesale Price Index

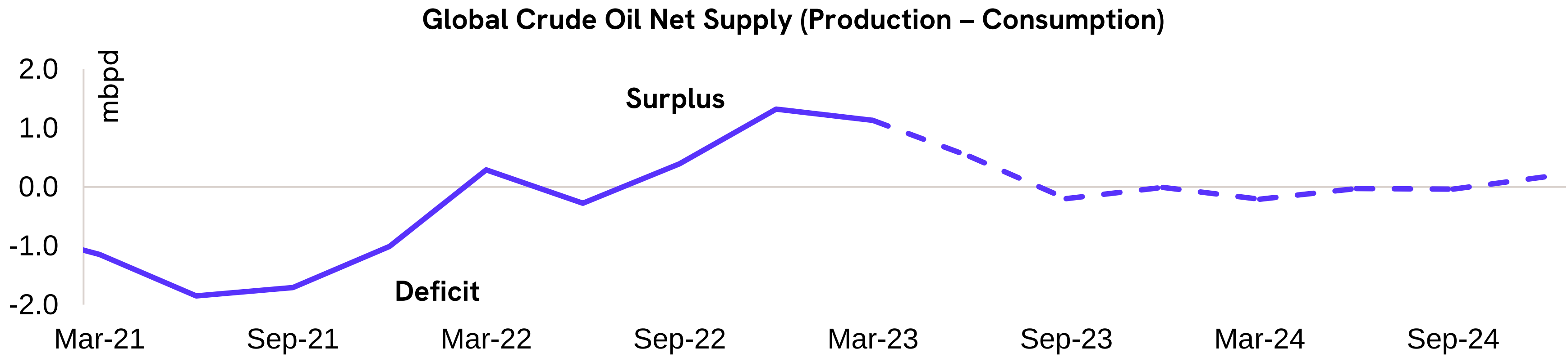
Global commodity prices continue to correct on growth concerns

Production cuts ineffective in bolstering the crude oil market, as demand and supply are anticipated to remain balanced



Commodity prices continue to decline in Q1FY24 due to global growth concerns and recession risks

Weak growth in China also leading to weakness in the commodity markets



Crude oil market has transitioned from deficit to surplus

EIA forecasts the market to maintain rough balance in the future

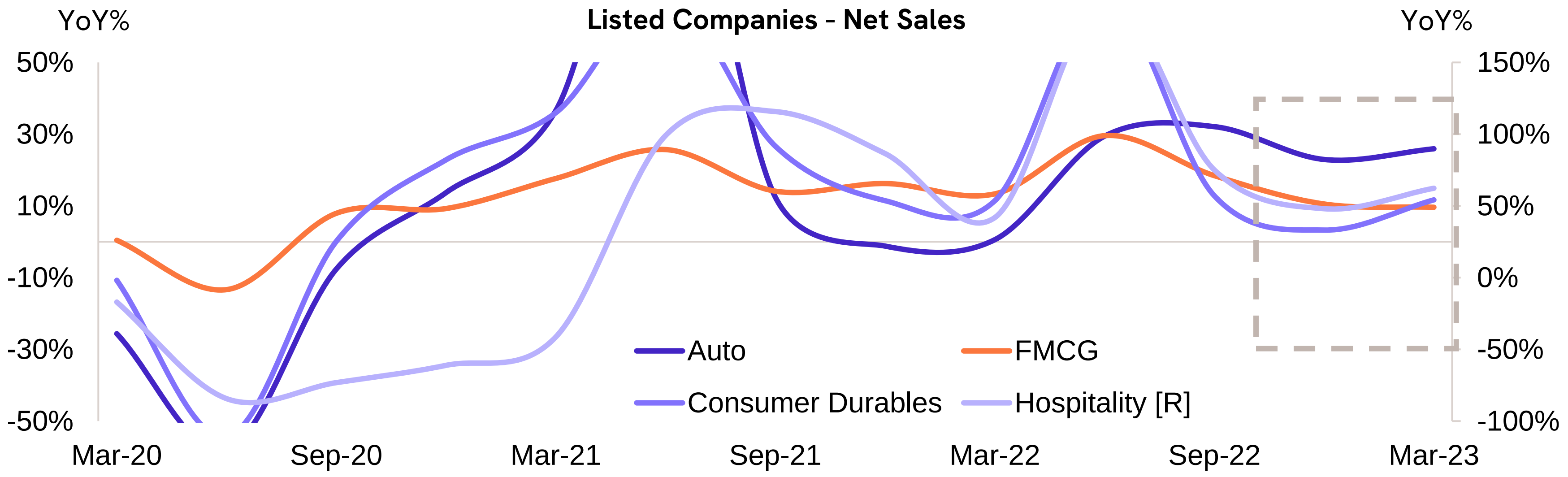
Production cuts by OPEC+ members have also proven ineffective in supporting crude prices

Source: Bloomberg, STEO EIA , 360 ONE Asset Research

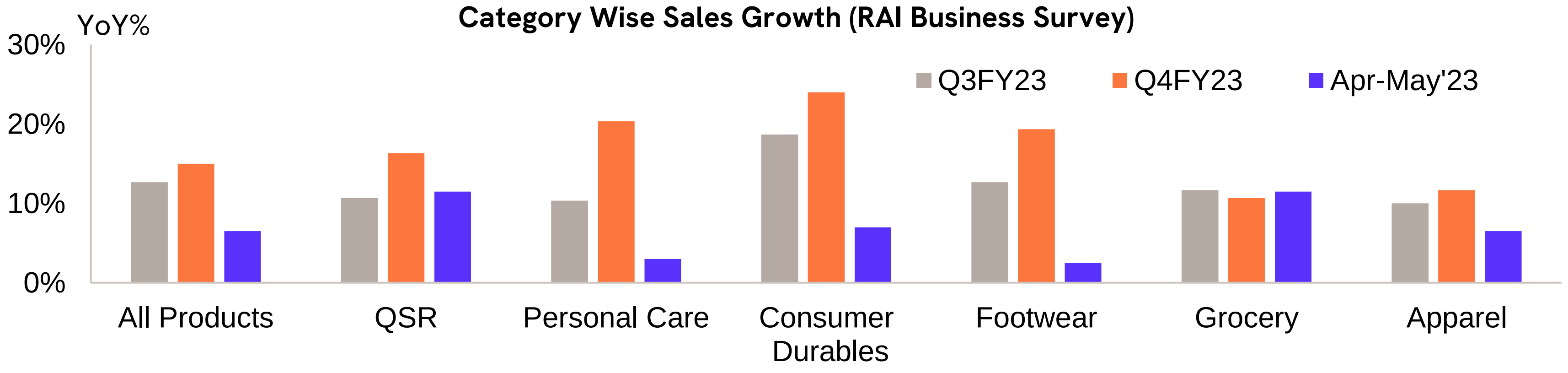
Note: mbpd: million barrels per day

Consumer-facing sectors witness decline in sales growth in Q1FY24

Improvement in sales in March quarter has not sustained in Apr-May 2023



Consumer-facing sectors (excluding FMCG) experienced an improvement in sales growth during Q4



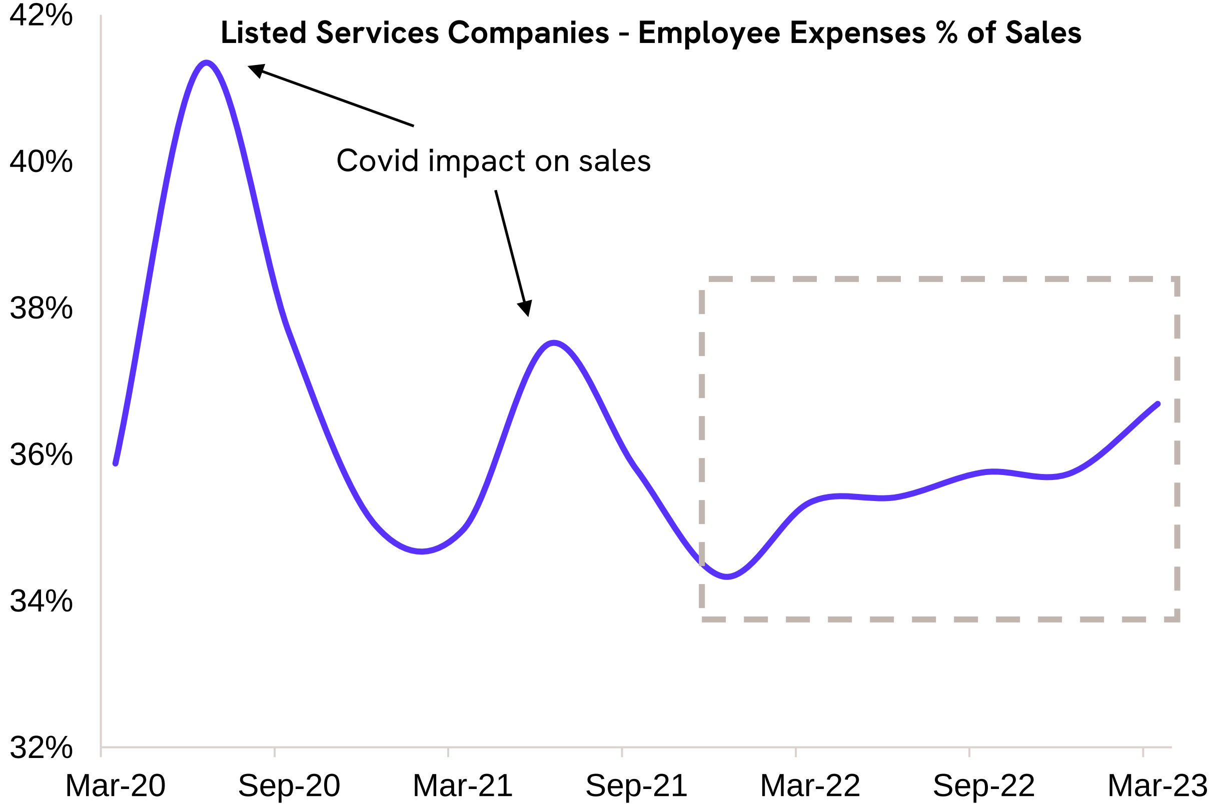
Sales growth, however, has been weaker in April-May 2023, as reported by the Retailers Association of India's Business Survey

Source: ACE Equity, RAI Business Survey, 360 ONE Asset Research

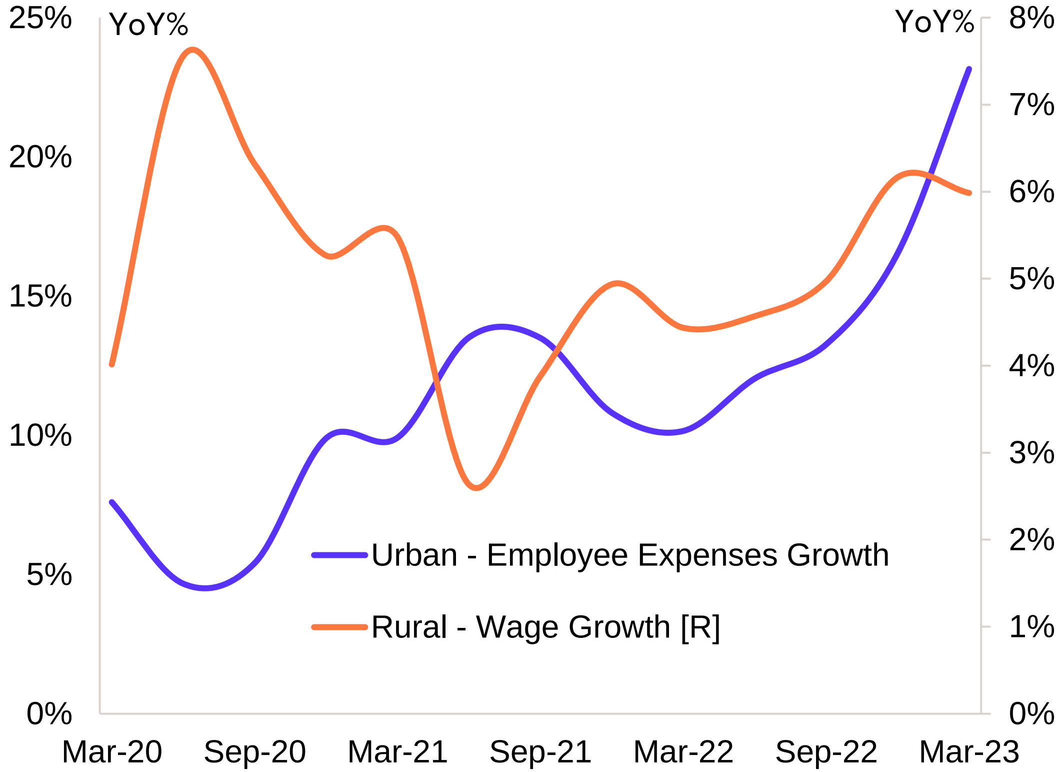
Wages & Employment

Strong growth in wages across rural and urban regions

Higher wages leading to increase in employee expenses for services sector firms



Employee expenses for services sector firms has increased to 37% of sales in March 2023 from 34% in December 2021



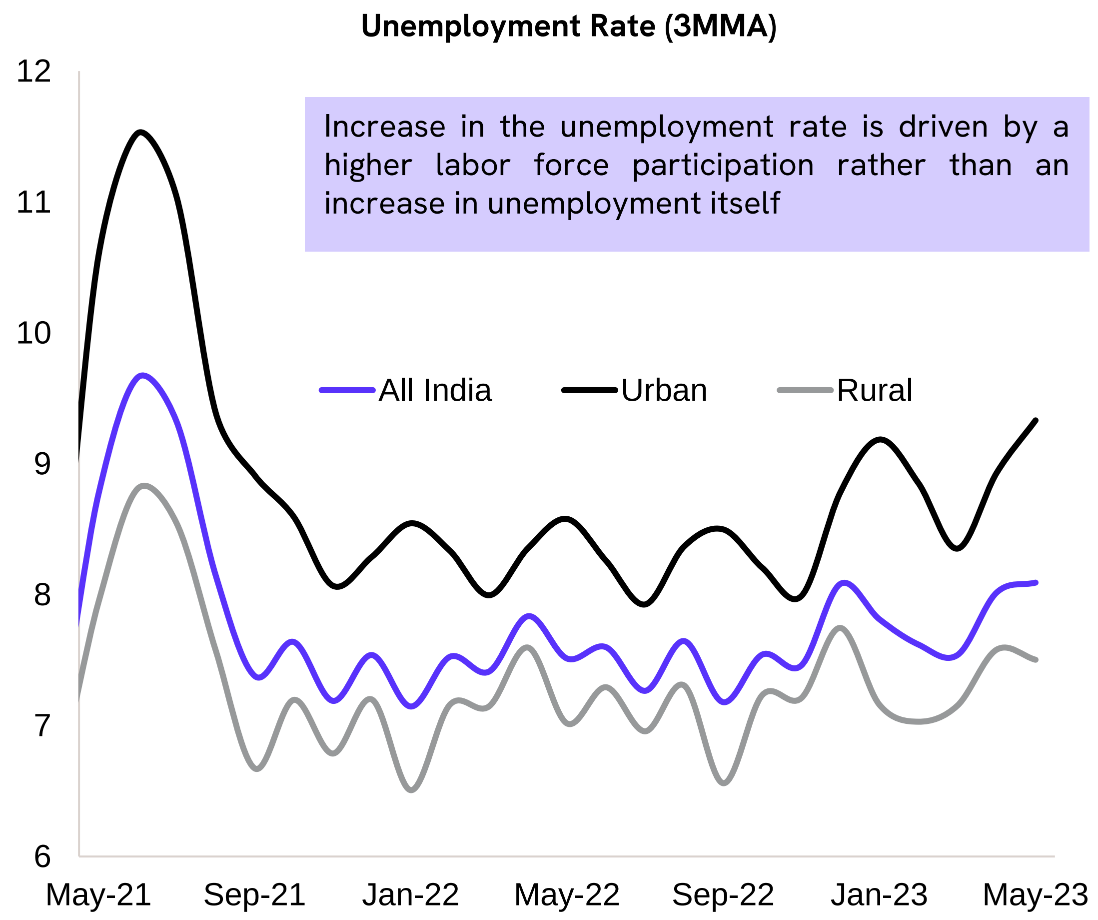
Both urban and rural regions are witnessing an increase in employee costs/wages, which bodes well for consumption

Source: ACE Equity, CMIE, 360 ONE Asset Research

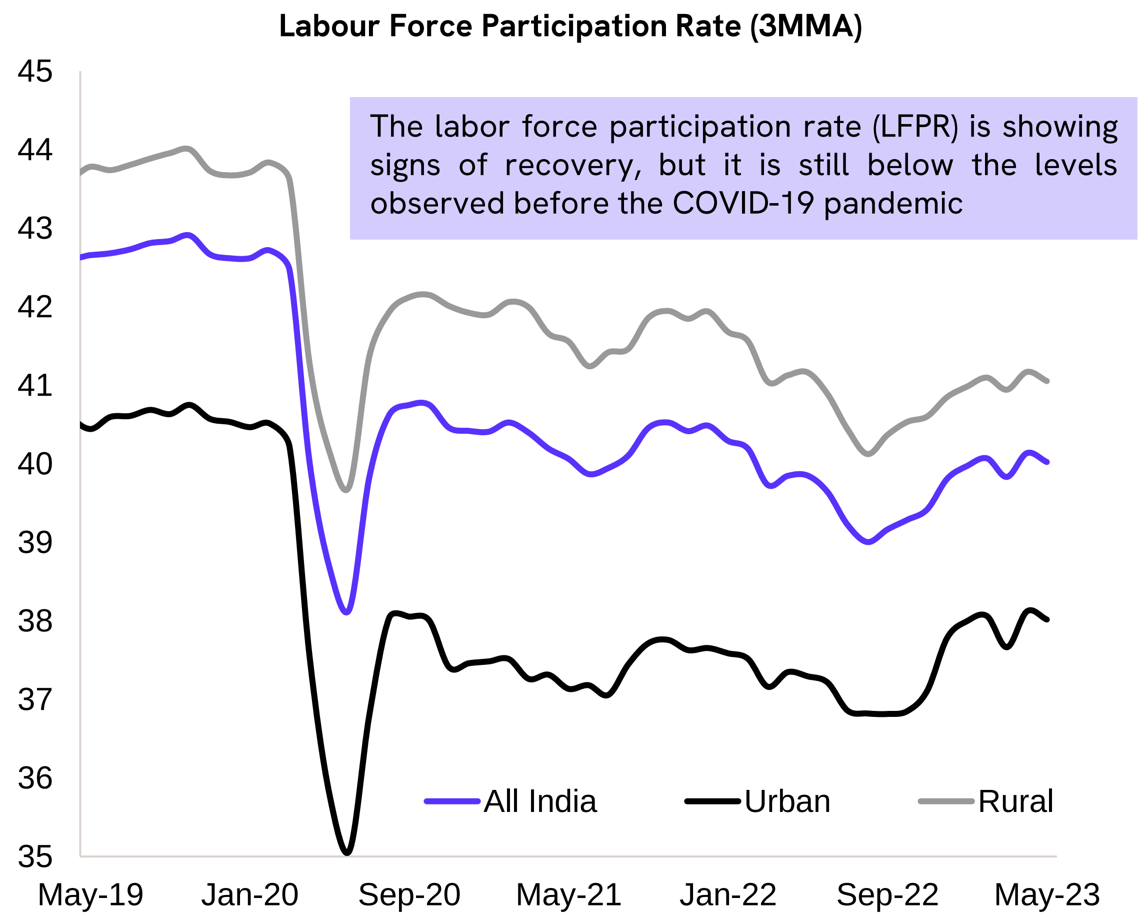
Note: Urban- Employee Expenses Growth corresponds to a set of listed companies including financials

Higher unemployment rates could moderate wage growth

Wage growth across sectors will vary depending on the demand for workers and availability of skills



Note: Unemployment Rate = Persons Unemployed / Labor Force



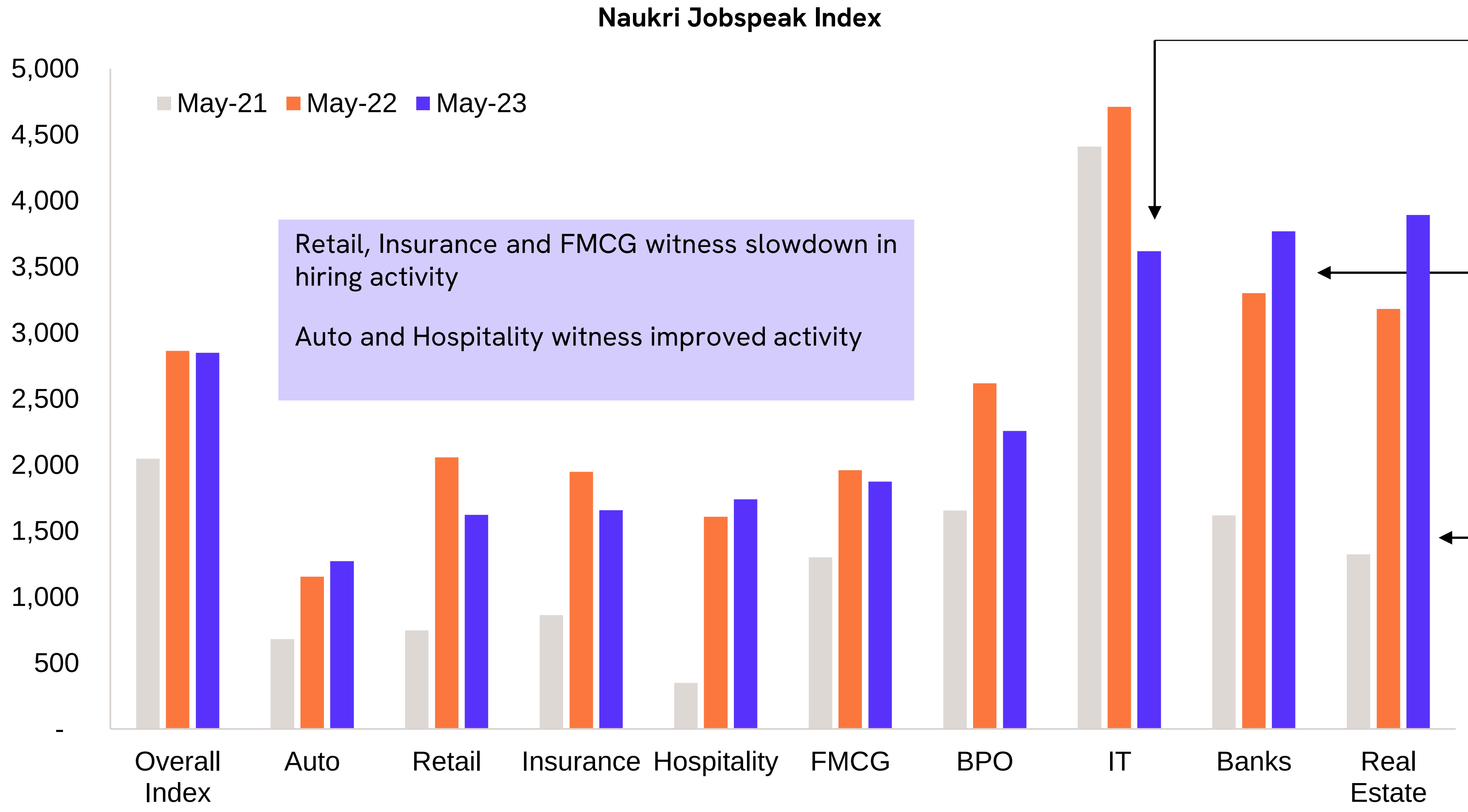
Note: Labor Force Participation Rate = Labor Force / Working Age Population

Source: CMIE, 360 ONE Asset Research

3MMA: 3 month moving average

Banking and Real Estate sectors witness strong hiring, IT sector lags

Overall hiring activity has remained flat, but there are significant sectoral variations



Retail, Insurance and FMCG witness slowdown in hiring activity

Auto and Hospitality witness improved activity

Hiring in the IT sector has been adversely affected due to weak growth prospects

Banks are observing significant hiring activity as they announce record profits, impressive credit growth, and reduced credit costs

The real estate sector is experiencing a surge in hiring, with many developers reporting their best-ever sales in the fourth quarter. Additionally, there is a steady flow of new property launches contributing to this trend

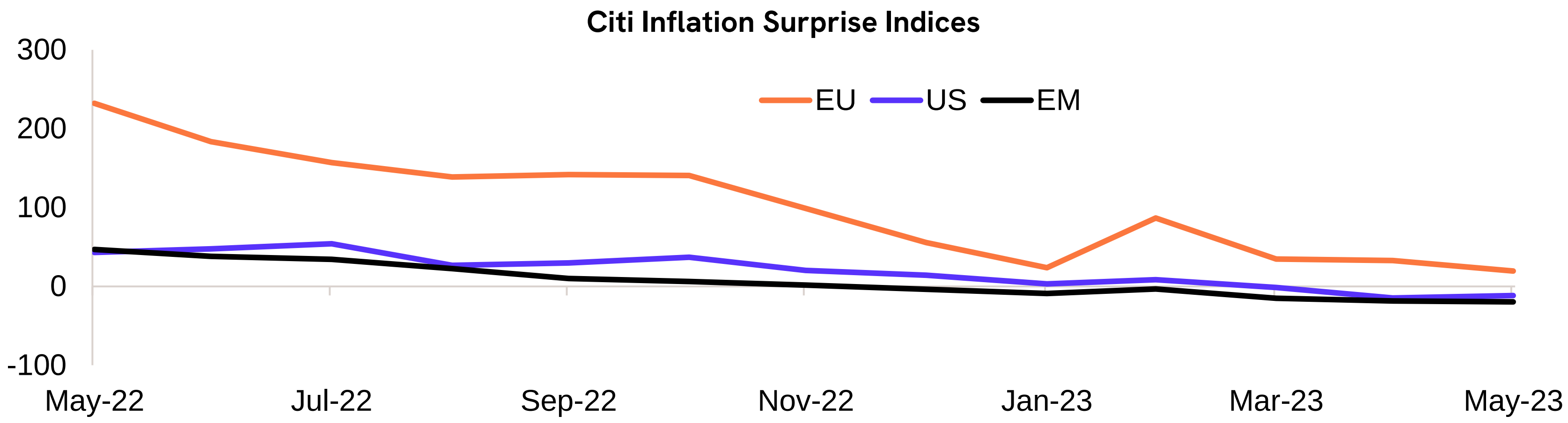
Source: CMIE, 360 ONE Asset Research

Note: Indices not comparable across sectors

Rates – ‘how high?’ to ‘how long?’

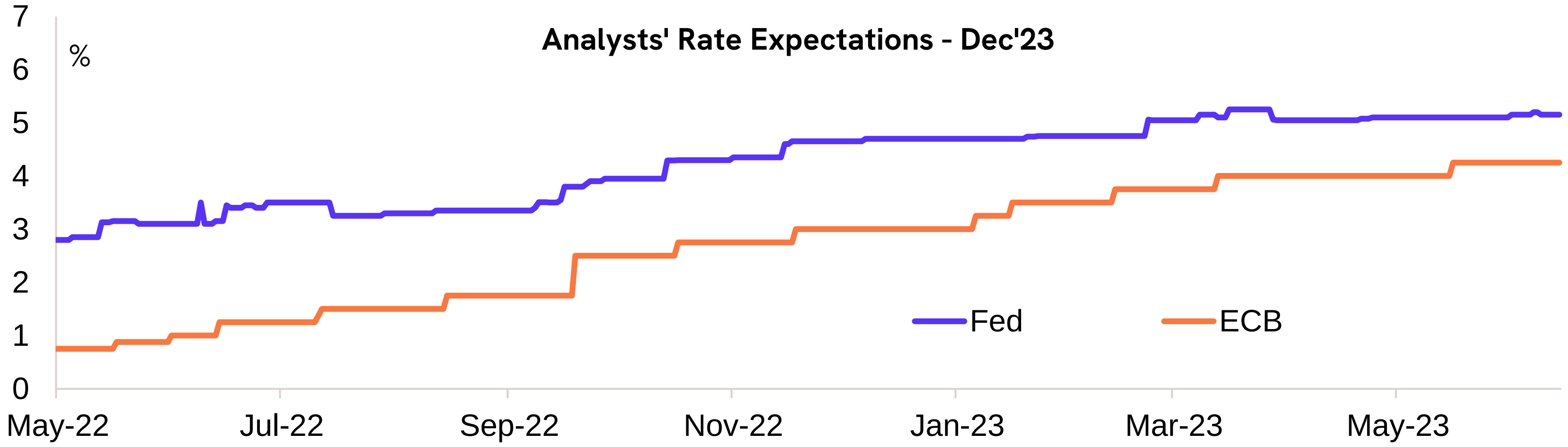
Global rate hike cycle is reaching its conclusion, but risks persist

Central Banks are anticipated to maintain higher interest rates throughout 2023, prioritizing caution regarding inflation



Surprise indices measure degree of deviation between economic data releases and market expectations

Inflation surprises fading and are now negative in US and Emerging Markets



Global central banks are nearing the end of the rate hike cycle, as inflation is now progressing in line with expectations

However, the Reserve Bank of Australia and the Bank of Canada decided to raise rates, despite pausing in earlier meetings

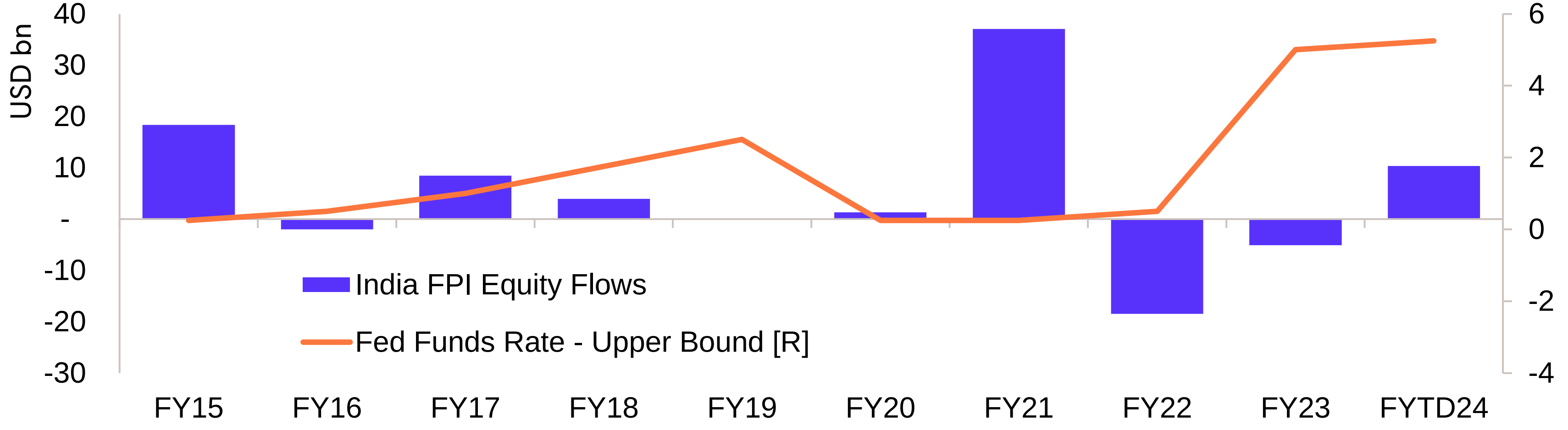
FOMC pauses in June 2023, but indicates 2 more hikes going ahead

Source: Bloomberg, 360 ONE Asset Research

Note: ECB – Main Refinancing Operations Fixed Rate, FOMC: Federal Open Market Committee

Fed's pause could potentially trigger equity flows into India

Improved risk sentiment expected as global rate hike cycle ends, boosting equity flows into emerging markets

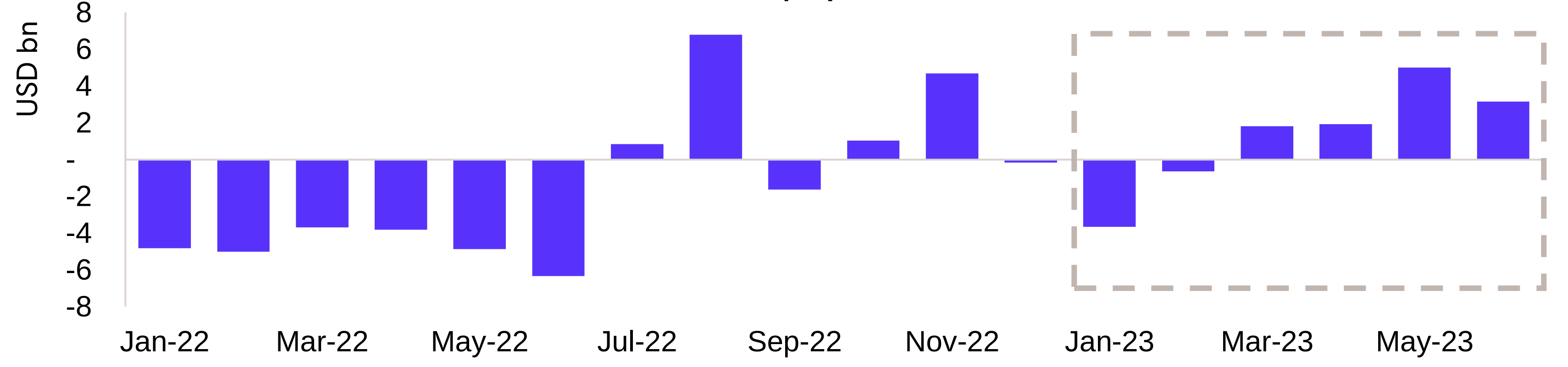


End of rate hike cycle positive for FPI equity flows into India

The pause by the Federal Reserve is expected to reduce financial volatility and risk aversion, thereby boosting equity flows into emerging markets

However, the reduction of the Fed's balance sheet may act as a counterbalance

India FPI Equity Flows



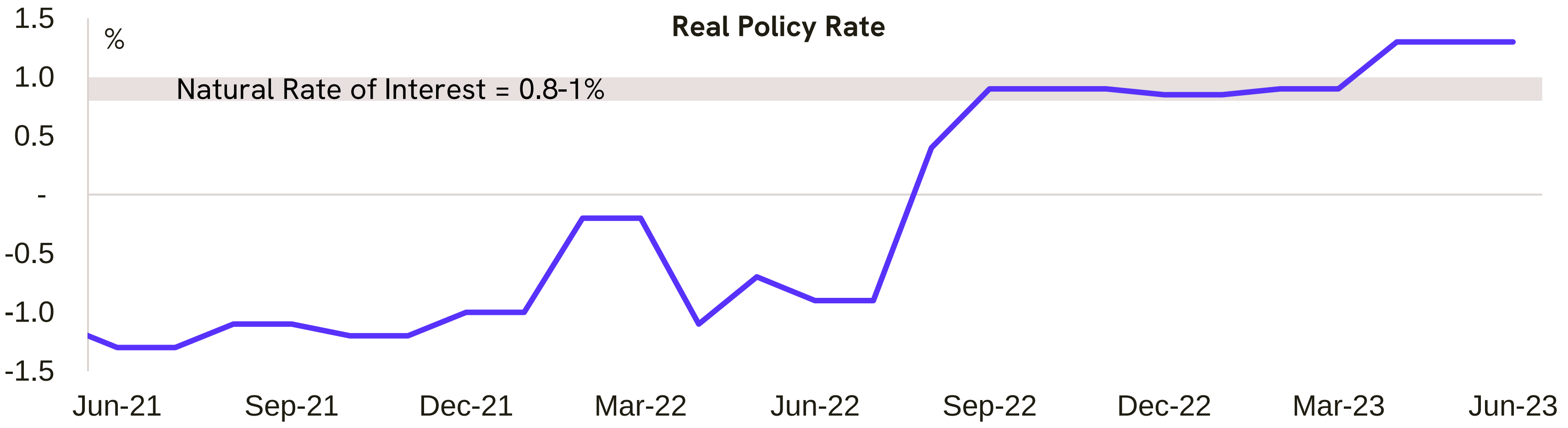
India has experienced a recovery in FPI equity flows in recent months, coinciding with the anticipated pause in the Federal Reserve's rate hike cycle

Source: Bloomberg, 360 ONE Asset Research

Note: data till 21 June 2023

Inflation has progressed as anticipated, but monsoon risks remain

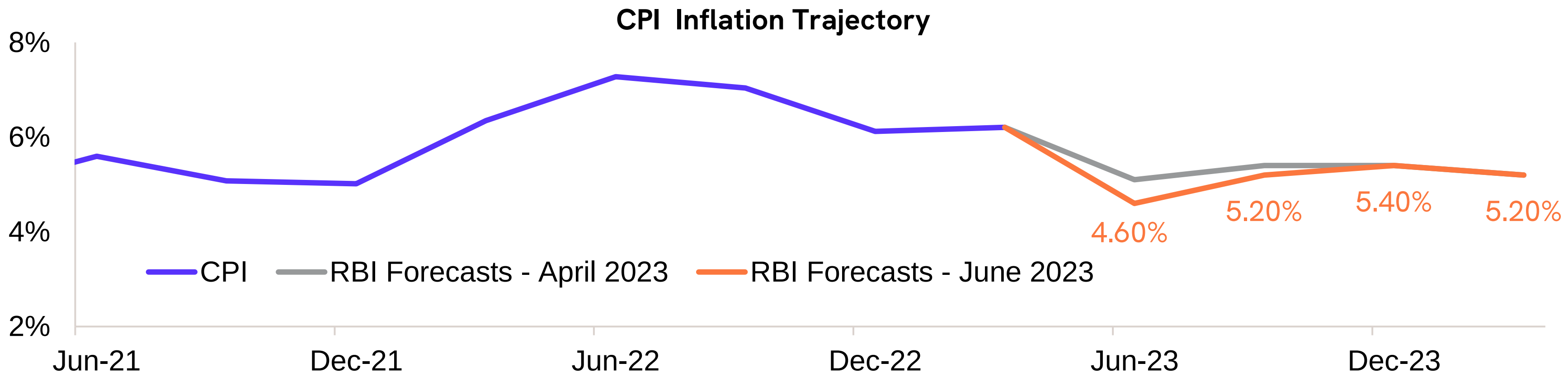
RBI likely to maintain the repo rate at current levels throughout 2023, assuming inflation evolves along expected lines



India's real policy rates are currently in restrictive territory

Unless there is a weak monsoon leading to an upward push in food inflation, there is limited room for further rate hikes

RBI is expected to adopt a 'wait and watch' approach throughout 2023



RBI revised inflation forecasts downward in June 2023 policy

Inflation trajectory assumes normal monsoon, in line with IMD forecasts of 96% of the Long Period Average (LPA)

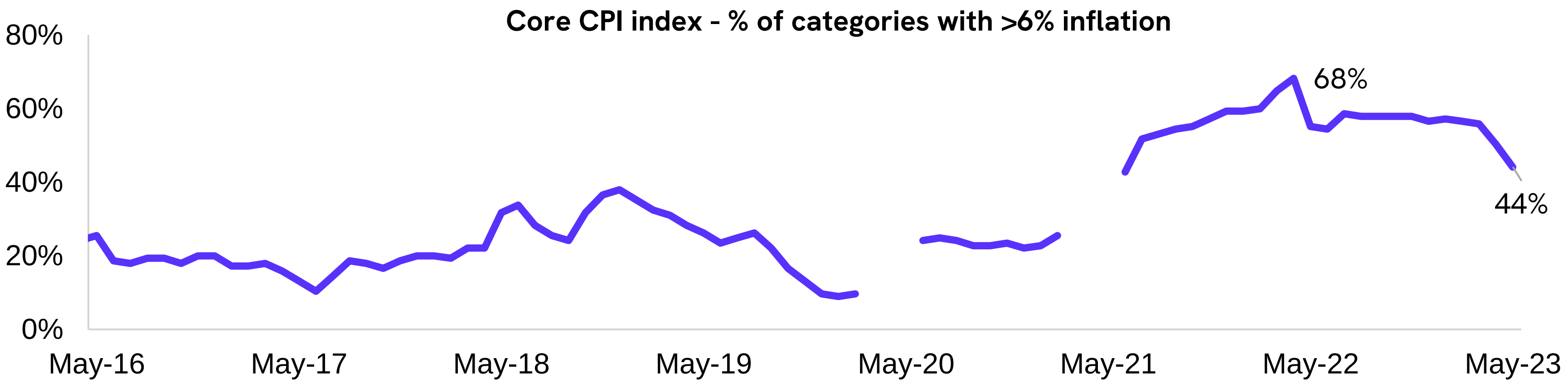
A weak monsoon has the potential to push the inflation trajectory upwards

Note: The natural rate of interest—the real interest rate that neither stimulates nor contracts the economy
Revisiting India's Natural Rate of Interest (RBI Bulletin Jun'22) estimated natural rate for the post-pandemic period in the range of 0.8 to 1% for Q3FY22

Source: MOPSI, RBI, 360 ONE Asset Research

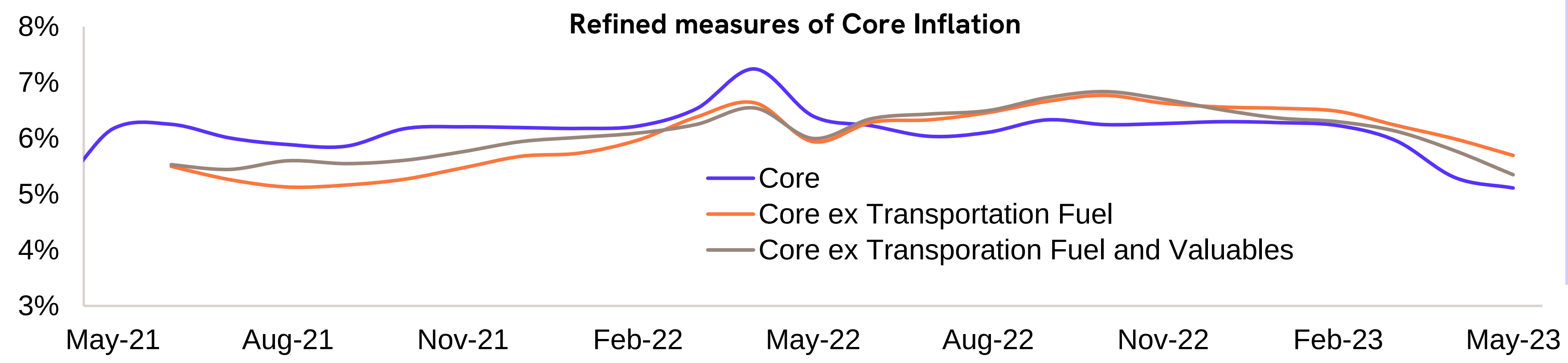
Underlying inflation momentum subsiding

We expect inflation to average around 5% in FY24, with the emergence of El Niño presenting potential upside risks



Inflation is no longer as generalized as it previously was

The proportion of items in the core basket experiencing inflation above 6% (the upper limit of RBI's inflation target) has decreased to 44% from its peak of 68% in April 2022



Refined measures of core inflation (excludes transportation fuels and valuables) also show continued easing of inflationary pressures.

The decline across all measures from peak in Q4 FY23 signifies that underlying inflation momentum is subsiding

Source: MOSPI, 360 ONE Asset Research

Note: Core inflation excludes volatile food and fuel components

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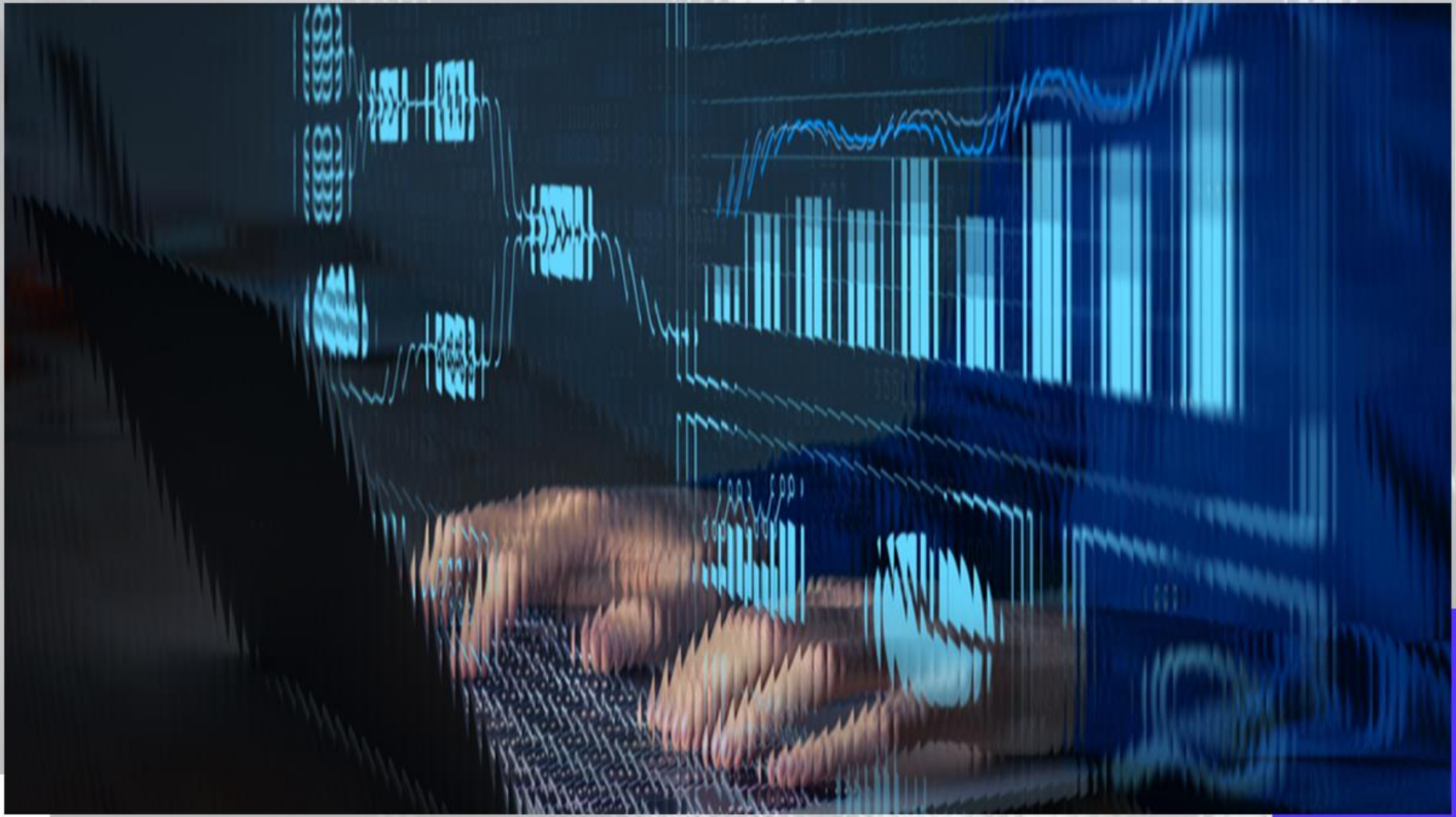

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