MONTHLY NEWSLETTER

FEBRUARY 2022

WHAT'S INSIDE

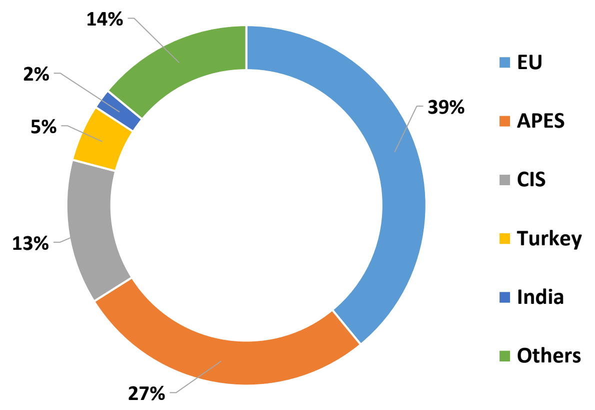
RUSSIA-UKRAINE CRISIS MAY PUSH BACK ECONOMIC RECOVERY

HOWEVER AGGREGATE EARNINGS IMPACT MINIMAL

Since the past two years, a sequence of unprecedented events transpired and disrupted the global economic balance considerably. The chaos caused by the pandemic in 2020 was followed by the Fed's decision to raise interest rates to fight inflation. While the world was coming to grips with these twin blows and as it was emerging from the latest wave of Omicron , the Russia-Ukraine crisis began and aggravated the macro backdrop and caused commotion in global equity. At the beginning of CY22, what looked like a post-pandemic, potential demand recovery-led inflation risk is now increasingly turning into a supply shock-led inflation risk.

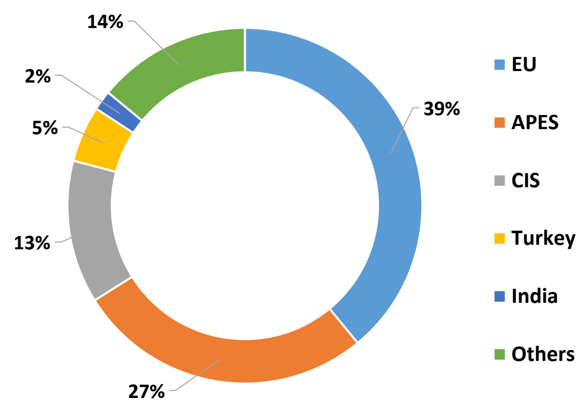
Central banks will now have to perform the crucial task of steering the economies. Thus, in the very near term, the tapering as well as interest rate hikes by the US Fed becomes a key monitorable. The Government of India and the RBI too will need to relook at the fiscal math presented in the Feb'22 Union Budget which has come under pressure in the ever-changing global macro backdrop. Let's witness how India has been impacted by this conflict.

RUSSIA EXPORTS ONLY 1.8% TO INDIA

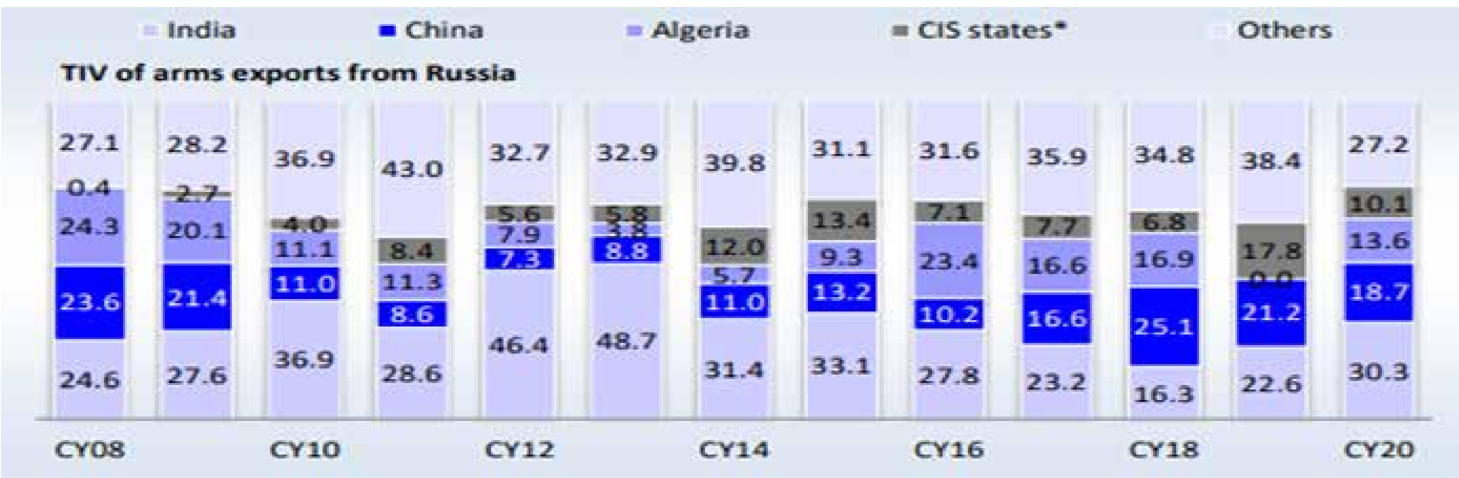


WHEREAS

RUSSIA IMPORTS JUST AROUND 1.5% FROM INDIA



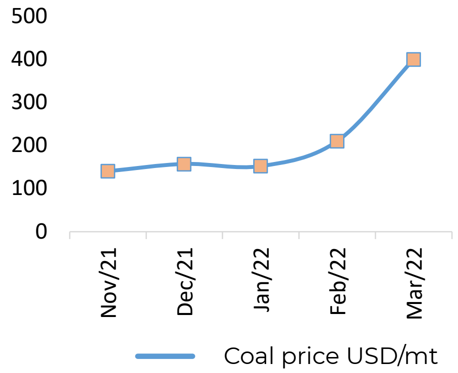
...but India is dependent on Russia for procuring arms and ammunitions which stands at 30% of India's defense import



Although there is a negligible direct merchandise trade between Russia and India, the latter is highly dependent on the former for its defense procurement. The dependency on Russia, however, is on a declining trend. Russia's share in India's imports declined to <40% over CY19-CY20, from 70% till recently. India is becoming self-reliant in terms of defense and the Russian-Ukraine conflict will further accelerate the same.

IMPACT ON COMMODITIES

COAL

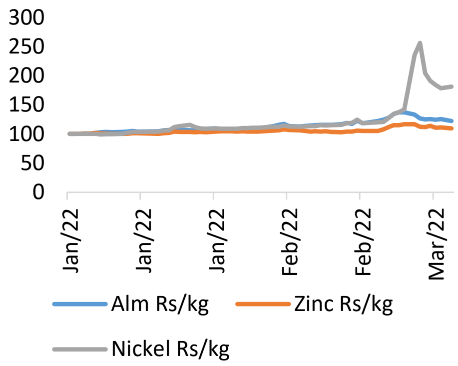


Russia contributes 18% of global thermal coal out of which 42% exported to Europe

High dependence on Russia in global trade of thermal coal is leading to huge volatility in thermal coal prices

This is likely to impact the operating cost for cement industry and steel industry due to their dependence on coal

METALS

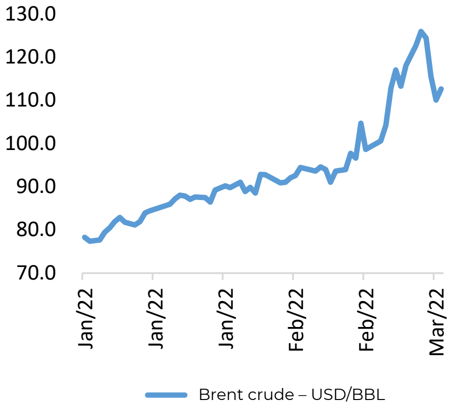


Russia accounts for 9-12% of world exports of several metals (Aluminium, nickel, steel etc)

Prices of aluminium, copper, nickel and steel expected to remain at elevated levels in the near to medium term

Commodity companies are the direct beneficiaries of rising metal prices

CRUDE OIL & GAS



Russia accounts for nearly 17% of global natural gas production and 10% of global crude oil production globally

India imports 85% of its crude oil requirement leading to short term repercussions due to high prices of global crude price

Higher crude oil prices will likely lead to higher current account deficit , higher inflation, wider-than otherwise fiscal deficit, squeeze on margins for OMCs

IMPACT ON MAJOR SECTORS

AUTOMOBILES

The gross margin for automobile companies is likely to get impacted due to rise in commodity prices such as aluminium, oil etc and shortage of semi-conductor production.

Rise in Crude Oil & Rubber prices will also have an impact on Gross profit margins of tyre manufacturers

OIL & GAS/CEMENT

E&P (Exploration and procurement of oil) companies expected to benefit with rise in crude oil realization

Within cement, significant cost escalations, owing to increase in key input variables (coal/pet coke/diesel) likely to impact margin

CONSUMERISM

High crude prices will lead to high inflationary impact.

In addition, high prices of grain, palm oil will also affect consumer companies, and alcobevs. High metal prices will also impact margin of consumer durables. Companies are likely to raise prices but ability to pass on without impacting demand is low

INFORMATION TECHNOLOGY

Near-term gains expected for IT services companies driven by INR depreciation.

There may be some indirect consequences from individual clients in continental Europe with exposure to commodity prices like Energy.

The impact though will not be very meaningful due to the industry's broad client base.

PHARMACEUTICALS

About 10-30% of API manufacturing cost is due to solvents. Further API forms 30-45% of formulation cost in case of generics.

Elevated crude prices expected to impact gross margin of pharma companies

LOGISTICS

With a sharp rise in global crude oil price, domestic fuel price hike is imminent in the near term, putting pressure on the road logistics operators

Global trade restrictions could impact EXIM trade negatively resulting in a decline in volumes handled by the rail logistics operators.

BANKING

Banking sector could see marginal loan growth impact on demand softness and possibly higher interest rates.

Bond yields are likely to rise thus leading to some MTM losses. However, the overall impact is not likely to be very significant.

NIFTY 50 AND NIFTY 500 INDICES - INSULATED FROM OIL PRICE SHOCKS

Brent Crude Oil price has increased from $65/bbl since the start of Dec-21 to $100/bbl currently, after touching a high of $139/bbl and we expect the price to remain at an average $90-100/bbl for FY23. The increase in Oil prices is unlikely to cause any meaningful change in FY23 EPS estimates for both Nifty 50 and Nifty 500.

BRENT CRUDE OIL PRICE RISES ON GEOPOLITICAL TENSIONS

Nifty 50	Upside %	Weighted impact %
Oil & Gas	15%	3.3%
Metals & mining	11%	1.1%
IT Services	1%	0.2%
Telecom	0%	0.0%
Power	0%	0.0%
Banks	-3%	-0.7%
Financial Services	-3%	-0.2%
Pharma	-4%	-0.1%
Engg. & Cap Goods	-6%	-0.1%
Consumer Goods	-8%	-0.5%
Cement	-20%	-0.2%
Auto & Auto anc.	-31%	-1.9%
Others	-7%	-0.1%
TOTAL		**0.8%**

NIFTY 500	Upside %	Weighted impact %
Oil & Gas	15%	2.7%
Sugar	15%	0.0%
Metals & mining	11%	1.9%
IT Services	1%	0.1%
Power	0%	0.0%
Textiles	0%	0.0%
Entertainment	0%	0.0%
Telecom	0%	0.0%
Banks	-3%	-0.6%
Financial Services	-3%	-0.3%
Chemicals	-3%	-0.1%
Pharma	-4%	-0.2%
Engg. & Cap Goods	-6%	-0.3%
Consumer Goods	-8%	-0.3%
Hotels	-8%	0.0%
Cement	-20%	-0.4%
Airlines	-30%	-0.3%
Auto & Auto anc.	-31%	-1.0%
Others	-7%	-0.2%
TOTAL		**1.1%**

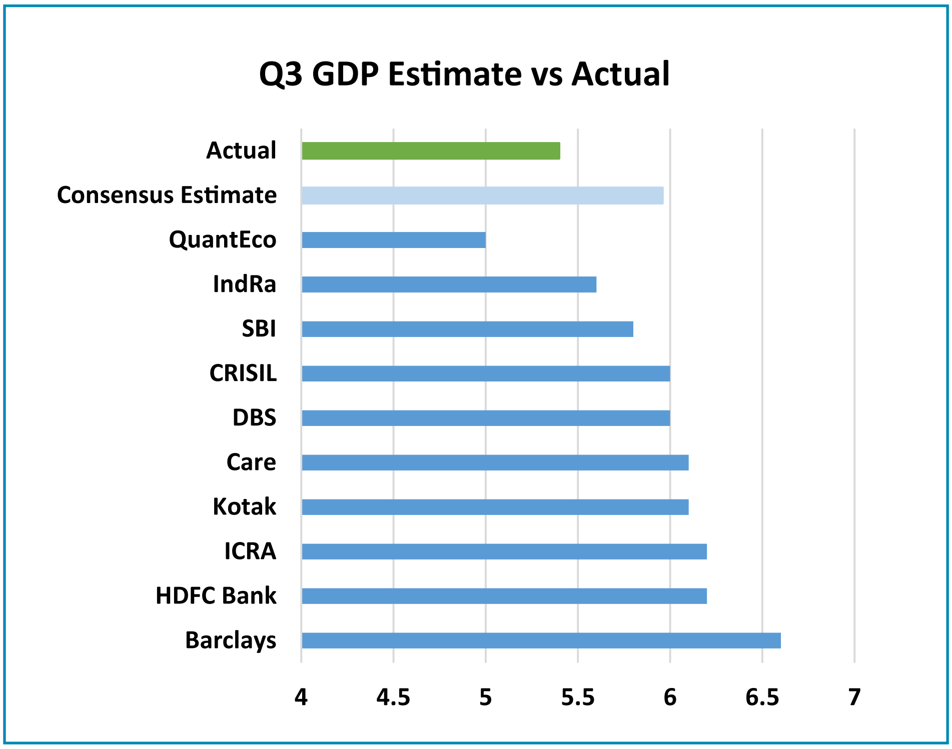
Conclusion

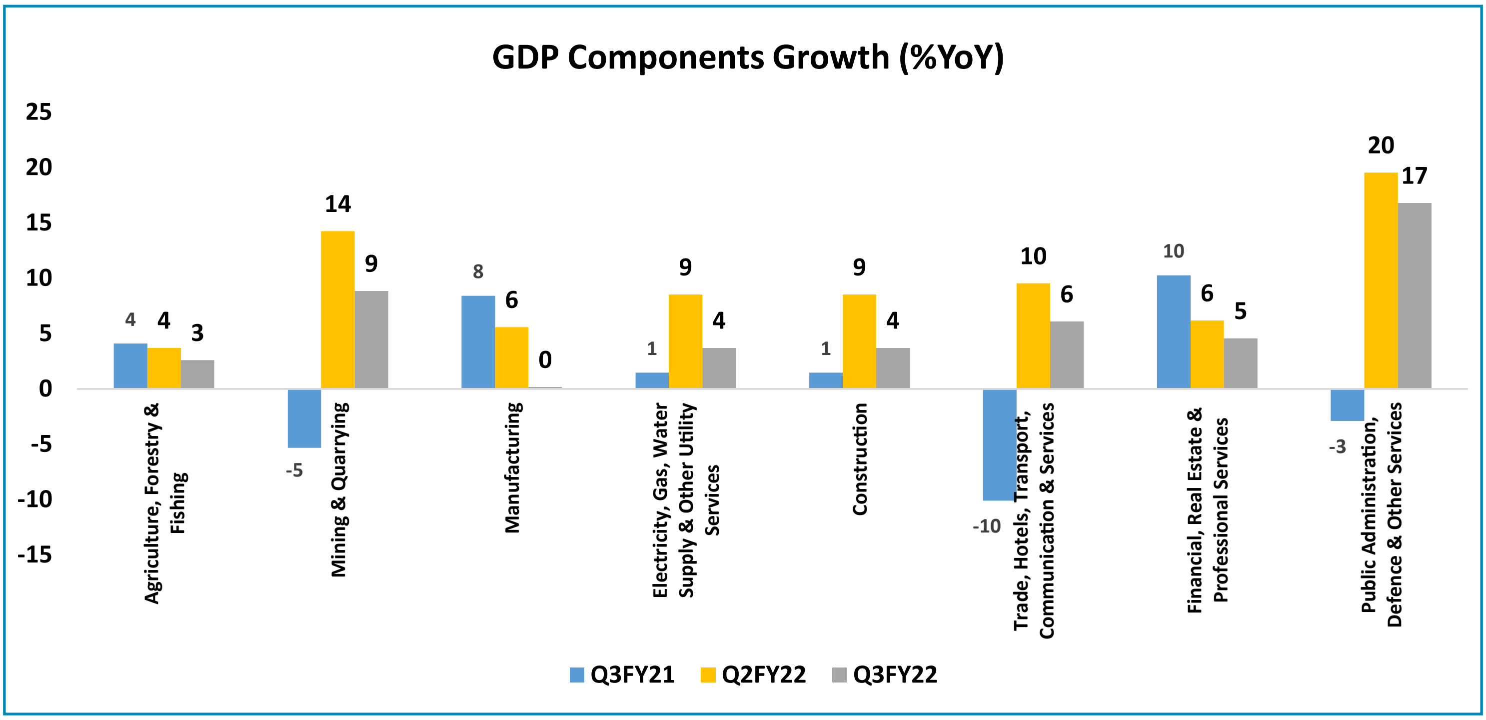
Commodity facing sectors are likely to benefit from the commodity inflation (10%+ EPS impact). Sugar sector will benefit as demand for ethanol, an alternative fuel, is set to rise (10%+ EPS impact). IT services sector will benefit marginally on rupee depreciation (1% EPS impact). Bulk of the other sectors are not significantly impacted (0-10% EPS impact). In terms of highly negative impacted sectors, Cement, Airlines and Auto & Auto anc. have a major negative EPS impact (20-30%), however, it's only the Auto sector which has a meaningful weighted impact on the indices. On an aggregate level, Nifty 50 (+0.8% EPS impact) and Nifty 500 (+1.1% EPS impact) indices are not seeing any meaningful change in FY23 estimates.

INDIA Q3 FY22 GDP

SMALL ROADBLOCKS

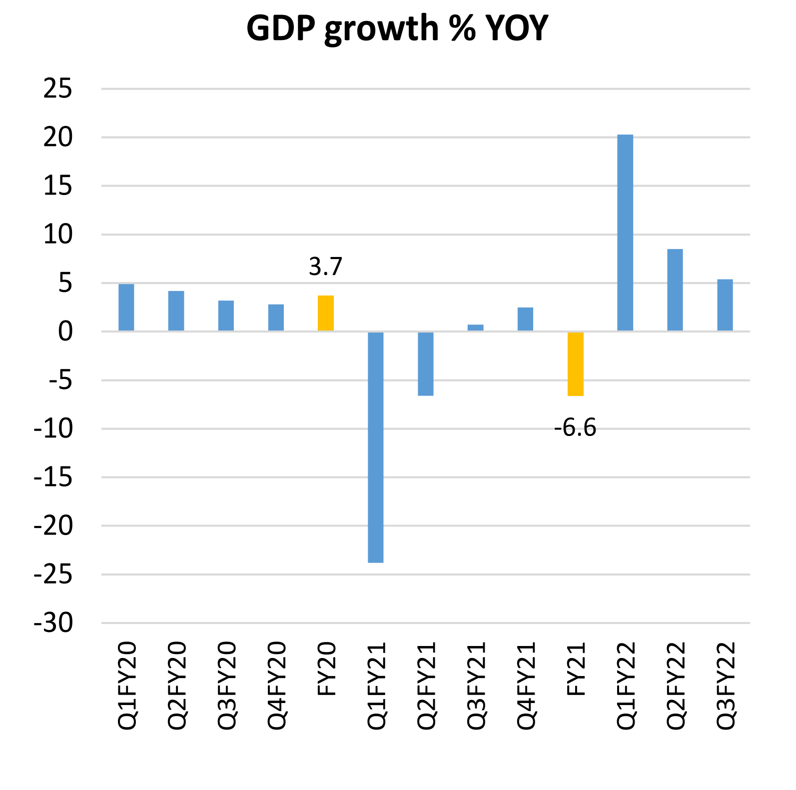
India's growth slowed at a sharper-than-expected rate to stand at 5.4% in Q3FY22 (Consensus: 6.0%), reflecting a combination of unfavorable base effects and consolidation of activity. The low growth was led by industrial sector slowdown. Growth plunged in manufacturing, electricity, and consumption, partly owing to supply-chain disruptions, driven by the auto sector and sequential easing in corporate profitability. The services and mining segment, public administration, and defence staged good growth, mainly due to low base effect. Agricultural growth weakened further to 2.6% due to uneven monsoons and weak rural demand.



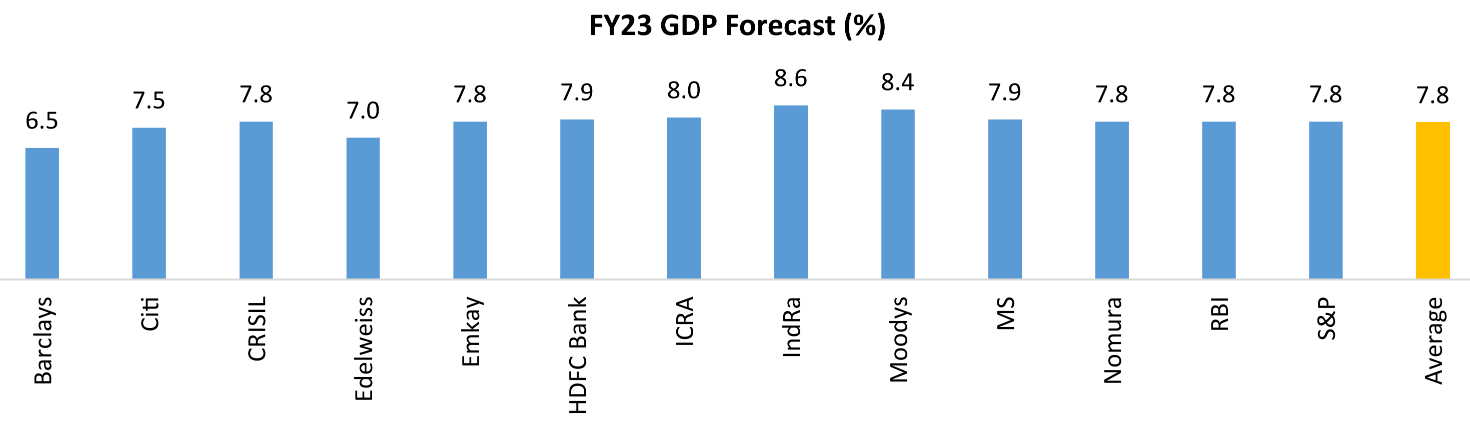


To make the situation more difficult, the current events unfolding may further slowdown the growth process. Omicron has already caused some softness in demand in the first half of Q4 FY22 and the geopolitical escalation may potentially disrupt global energy trade and prices weighing on near-term growth. While the evolution of geopolitical tensions and the magnitude of the energy supply shocks are uncertain, prolonged conflict of over 3-4 months can see sustained pressure on inflation. Fiscal and monetary support should continue to favour growth, especially as the recovery in domestic economic activity is yet to be broad-based. However, rising inflation can complicate matters and put policy makers in a tight spot. A moderation in output of contact intensive services, trade, etc. could be seen in Q4, along with those hit by supply-chain disruptions. But the impact of the pandemic is unlikely to last beyond Q4 though geopolitics and inflation would largely dominate headlines

FY23 – MINOR CUTS, BUT STILL THE FASTEST GROWING LARGE ECONOMY



It is too early to say if the current geopolitical tensions can have a lasting impact in disrupting supply chains and commodities movement. However, some organisations have cut their FY23 estimates by 30-50bps to factor in rising external risks, lower global trade, higher commodity prices leading to higher inflation, widening current account deficit, higher interest rates, and possibly higher fiscal deficit / curtailment of government spending on CAPEX. On the brighter side, even if inflation inches higher in FY23, most estimates are pencilling the inflation to stay within the upper band of RBI's tolerance level, which implies the interest rates may not go out of hand for RBI. Consumption, specifically, private consumption has been the main highlight of India's growth story post GFC, but it has been languishing after 2018 and seen a secular hit since then. Government consumption and investment remain in the forefront, as they will need to fill the growth and jobs bridge until private investment and consumption recover.



Conclusion

India's Q3 FY22 GDP slowed much more than expected, and the economy faces near-term headwinds. India's GDP has hit a slightly rough patch, with the geopolitical tensions and the rising crude oil situation painting a grim picture. However, there is ammunition both on the fiscal and monetary side to tide over the current situation. The services sector is likely to provide the much needed support for growth next year. India is still pegged to be the fastest growing large economy in FY23, with average real GDP growth expectations of 7.8%, and our forex reserves are quite adequate to avert any currency crisis given the external shocks. The economy has had its set of challenges but has been able to navigate itself quite well.

DIIs NEUTRALIZING FII OUTFLOWS ON D-STREET

Investors have been quite a worried lot with FPIs selling Indian equities left, right and centre. In this section we try and understand the background of FPI buying and selling in the form of FAQs

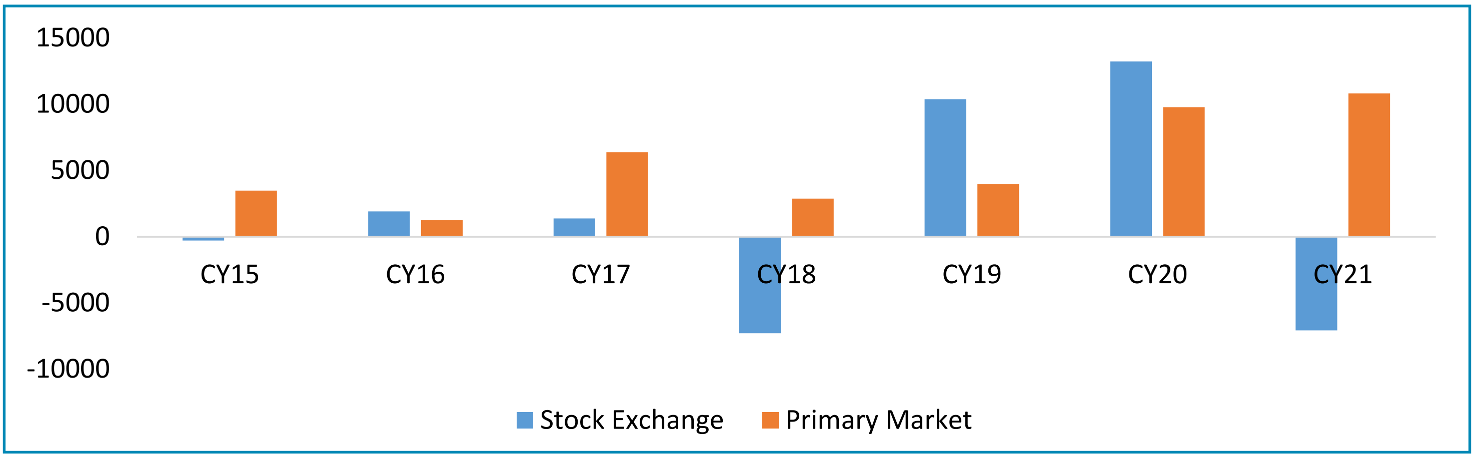
Are FPIs a uniform class of investors?

- No, FPIs involves diverse classes such as pension funds (long term), Hedge funds (short term) and also Emerging Market (EM) funds and ETFs. These investors also diverge in investment in terms of horizon, objectives and strategies. So there is no uniform selling across the market as if they do so, then they will be non-adhering to the mandate given to them.

Does the provisional data released every evening represent the actual net FPI flows into India?

- No. This includes only the net flows into secondary market. But the real picture can be gauged only after including the flows into primary market. We hold the view that FPIs have been sellers in 2021. However, they have actually been net buyers in 2021 if we consider both primary and secondary markets as they have invested heavily in IPOs and Pre-IPOs. Hence FPIs have been net sellers just once in 2018 in both the markets

Breakup of FPI inflows into primary and secondary markets (US $mn)

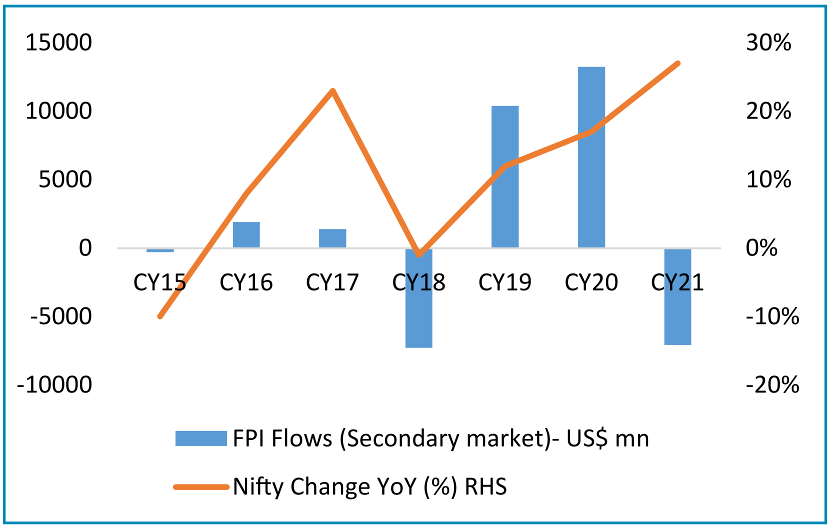


What are the considerations in FPI's investing strategies?

- Many FPIs run an arbitrage or Long/short book. They take self-cancelling positions in equities of various regions, categories whether emerging vs developed, countries and segments whether cash vs derivative. Currency is another important consideration in many FPIs' investing strategies. Their positioning is usually not reflective of their fundamental view on a country, region, or category.

Does the FPI flows materially influence the market?

- As seen in the adjacent chart, there is no material influence of FPI flows in direction of market beyond 5-6 months. The sensitivity of FPI outflows on benchmark index over the years has considerably reduced.



- Till quite recently, a phenomenon that used to wreak havoc in Indian equity markets was a large-scale departure of foreign funds. Not anymore. Today, the country's stock market does not seem to be held ransom to the fluctuations of FII flows. Heavy buying by domestic institutional investors (DII) including mutual funds and life insurance companies have capped the downside.

FII likely to return to Indian market as the size, consistency is unmatchable

EQUITY PERFORMANCE OF MAJOR EMERGING MARKETS

CAGR	1 YEAR	3 YEARS	5 YEARS
Russia	-47.4%	-14.5%	-7.5%
China	0.0%	7.2%	2.8%
Brazil	10.0%	-5.3%	0.2%
Turkey	-33.5%	-12.4%	-11.3%
India	9.2%	12.1%	10.0%
Thailand	2.4%	-1.1%	2.6%
Indonesia	8.6%	1.2%	3.2%
Malaysia	-3.9%	-3.8%	-0.4%
South Africa	9.3%	6.2%	4.1%
Mexico	16.5%	3.7%	1.2%

CAGR in USD

Analysts are of the view that FII selling should abate and subsequently reverse after a while since there aren't too many major economies that offer stable businesses and decent return prospects as shown in the adjacent chart. India offers one of the largest consumer markets and a well-diversified economy, across sectors like IT, pharma, consumption, which are structural in nature and hence will always generate interest from investors both domestic and FIIs. Flows will be driven by macros as well as corporate profitability where India should do well vis-à-vis other emerging markets

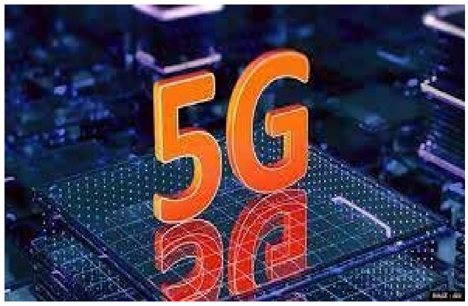
WHAT CAUGHT OUR ATTENTION THIS MONTH?

Retail inflation hits 8-month high in February

Retail inflation scaled an eight-month peak of 6.07% in February, hitting the upper band of the RBI's medium-term target of 4.5%

Inflationary pressure is only going to exacerbate in March, as oil marketing companies are set to soon pass on the spike in global crude oil prices to consumers

Govt plans to launch 5G services by August-22, eyes spectrum sale by May-22



Telecom minister Ashwini Vaishnaw is confident that 5G will be launched in India by August-22

The minister also added that a complete ecosystem for 5G right from 5G core network, radio network, telecom equipment and 5G handset is being developed in India

DoT has asked TRAI to expedite consultations with stakeholders and finalise recommendations on holding spectrum auction for 5G services

Retail business grows 10% MoM in Feb as economy opens up

According to Retailers Association of India (RAI), the rise witnessed in Feb 22 marks a growth of 6% compared to Feb 2020.

Categories such as consumer durables and electronics, food and groceries and QSR have indicated rapid YoY growth of 28%, 19% and 16%, respectively

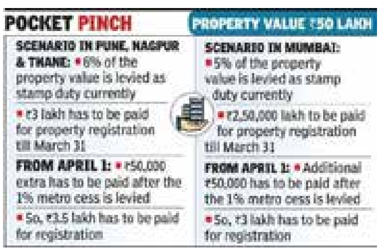
RAI, however, added that inflation and the war situation in Ukraine will have some impact on business positivity

India likely to delay mega LIC IPO to mid-April

The government had planned to launch it by March 31, 2022 but delayed the issue after Russia's invasion of Ukraine made financial markets highly volatile

The IPO's delay is one of the biggest fallouts in Asia's capital markets from the Ukraine crisis as it was slated to be one of the biggest insurance IPOs globally this year

The government would also wait to see the impact of expected monetary tightening by the U.S. Federal Reserve which could adversely affect Indian stock markets, pushing away foreign investors.



POCKET PINCH | **PROPERTY VALUE ₹50 LAKH**

SCENARIO IN PUNE, NAGPUR & THANE:	SCENARIO IN MUMBAI:
6% of the property value is levied as stamp duty currently	5% of the property value is levied as stamp duty currently
₹3 lakh has to be paid for property registration till March 31	₹2,50,000 lakh to be paid for property registration till March 31
FROM APRIL 1: ₹50,000 extra has to be paid after the 1% metro cess is levied	FROM APRIL 1: Additional ₹50,000 has to be paid after the 1% metro cess is levied
So, ₹3.5 lakh has to be paid for registration	So, ₹3 lakh has to be paid for registration

1% metro cess on property buys from next month

1% metro cess would be levied on property purchases from April 1 in Pune, Mumbai and Nagpur

The 1% metro cess would be a transport surcharge. It is intended to be used for building transport infrastructure projects like Metro, bridges and flyovers

Builders are urging the Maharashtra government to defer the levy of additional 1% metro cess on property transactions in the state by at least 2 years

RESEARCH & RANKING™

Maharashtra Budget proposes cutting VAT on CNG to 3% from 13.5%

The Maharashtra Deputy Chief Minister Ajit Pawar has reduced the VAT on natural gas to 3% from 13.5%

This move will make the domestic piped and compressed natural gas cheaper bringing much-needed relief to the households and vehicle owners.

This is also aimed at promoting the use of environmentally friendly natural gas

Services sector expands modestly in Feb-22 as pandemic retreats

Services sector activities in India picked up marginally in February on the back of better demand conditions and the retreat of the coronavirus pandemic

India Services Business Activity Index rose to 51.8 in February from 51.5 in January

The composite PMI output index rose to 53.5 in February from 53 in January as manufacturing firms recorded a notably stronger increase in business activity

International flights to operate with 100% capacity from March 27

The government had banned all international scheduled flights since March 23, 2020. Special international flights have been operating under airbubble

The move is expected to boost international tourism and will help soften airfares which has been soaring due to increase in covid oil prices

The number of weekly average daily fliers stood at 324k in the week ended (W.E) 05th Mar'22 vs 315k in the W.E. 26th Feb'22.

India signs free trade agreement with UAE

India has signed a trade pact with UAE that will reduce import duties on the majority of Indian exports to the country

In addition, government expects it to especially boost the export of gems and jewellery, and apparels to the UAE and raise total trade up to $100 billion in the next 5-years.

The UAE is India's 3rd-largest trade partner globally after United States and China.

With $3.2 trillion MCap, Indian stock market beats its British peer, becomes fifth largest in the world

India has outgrown the UK in terms of market capitalisation for the first time to become the fifth biggest stock market amidst the Russia Ukraine war

India's market cap stood at $3.2trillion as against $3.1 trillion for the UK, according to Bloomberg data.

Currently, the US is the world's biggest market valued at $47.32 trillion followed by China ($11.52 trillion), Japan ($6 trillion) and Hong Kong ($5.6 trillion).

GLOBAL NEWS THIS MONTH

Covid-19 lockdown in China's tech hub Shenzen

Amid a rapid resurgence of Covid 19 cases, two of the country's biggest cities, Shenzen and Shanghai have imposed strict virus measures

A lockdown in China's tech and manufacturing hub Shenzhen will likely disrupt global supply chains and ship availability causing a spike in freight rates and potentially affecting India's steel companies, electronics assemblers and carmakers.

Russia temporarily limits sugar, grain exports

Russia's PM signed a decree banning export of sugar until August 31 and banning rye, wheat, barley and maize exports to ex-Soveit countries until June 30

Deputy Prime Minister Viktoria Abramchenko, however, said the export of grain within the quota under individual licences would continue to be allowed.

The measures were adopted to protect the domestic food market in the face of external constraints

Nepal to become the first country to adopt India's UPI system for their digital transformation

NPCI International Payments Ltd (NIPL), the international arm of NPCI, has joined hands with Gateway Payments Service (GPS) and Manam Infotech to provide the services in Nepal.

THANK YOU

We would love to hear from you...

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