

IPC: Q1 FY22 – Time to rebuild equity portfolio

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Quarterly Investment Policy Committee (IPC) – turning overweight on equity



A. Macro

- 1. Global consensus: Equity allocation at pre-Covid high
- 2. Economic Recovery: ACAI shows more indicators turning green but pace uneven
- 3. Economy shows contrasting trends

B. Equity Markets – turning overweight

- 1. Equity markets have performed in FY21 but have become footloose too
- 2. The Reliance factor: Did it make a real difference to portfolios?
- 3. The market hasn't reacted much to Covid second wave yet
- 4. FIIs flow dip as India Risk Premium is down
- 5. The currency factor: INR depreciates while DXY has started gaining
- 6. Global equity: US protected its nontradeables sector
- 7. Valuations getting support of earnings: China still cheap
- 8. Valuation froth exists in various pockets

C. Fixed Income and Others

- 1. Supply overhang to keep yields rangebound
- 2. CAD, INR, commodities resulting in higher imported inflation
- 3. Inflation concern gives little headroom for RBI response to Covid second wave
- 4. Fixed income remains a play on yield curve
- 5. Gold: Negative outlook persists

E. Strategy

F. Model Portfolio

- 1. Construct and Stance
- 2. Model portfolio : Outperformance over longer period
- 3. Model Portfolios Maintaining outperformance so far

Summary & conclusion: Overweight on Equity and Hybrid; Under weight Fixed Income/Commodities



- 1. The global consensus trade continues to favour an equity risk-on strategy. In India near term risks have accumulated in the nature of a still mixed economic recovery, surging second wave, withdrawal of FIIs, weaknesses in currency and a footloose market where thematic chase proved elusive.
- 2. For the long-term investor, with an investment horizon of 3yr+ the near-term factors would need to be looked through. The infrastructure, cap good and the manufacturing sector has shown traction in recent times paving the way for medium term improved growth prospects. Corporate earnings remain strong in this backdrop and likely to survive the setback from second wave of Covid. In the meanwhile the somewhat soft market amidst somewhat corrected valuation provides opportunity to build portfolios for long term. We have thus **turned overweight on equity from neutral earlier**.
- 3. On the fixed income side heavy supply from all agencies with similar institutional appetite implies bond market condition would remain tight for the second year in succession. RBI needs to step up its OMO well beyond GSAP 1.0 while a hardening inflation outlook would limit headroom for RBI to turn policies any further accommodative than what it is already. We have therefore turned underweight on fixed income space from neutral earlier.
- 4. We stay overweight on the Hybrid space comprising REITs/InvITs and underweight on Gold as earlier.

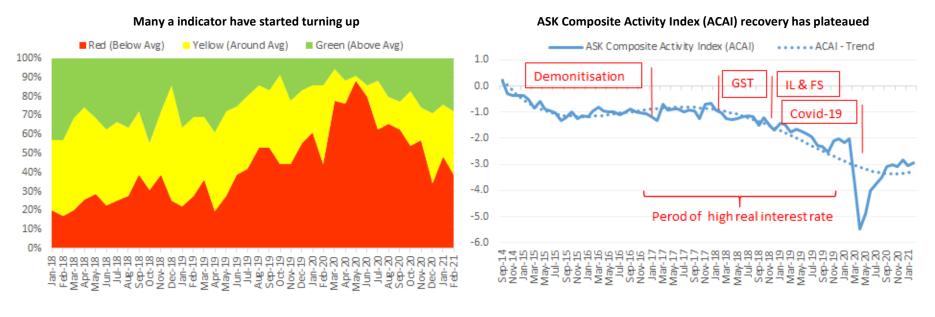
Global consensus: Equity allocation at pre-Covid high





Economic Recovery: ACAI shows more indicators turning green but pace of recovery plateaued at some level





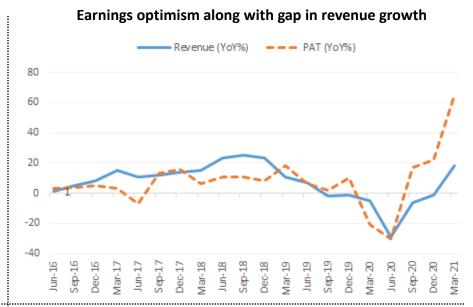
- ACAI shows indication of economy bottoming out in Apr-2020 and after relatively sharp recovery in May-20 and Jun-20 and continued recovery thereafter albeit it seemed to have plateaued at some level.
- New order book have shown huge traction and government expenditure has picked up in a significant way. In the transport sector railway freight remains buoyant while road traffic too has seen first signs of improvement. In the financial sector, money supply has remained steady while life insurance premium has seen a sudden spurt. On the external front imports have risen while foeign investment has remained high for successive months.
- However, fuel consumption has dipped again, air traffic is yet to normalize and other financial market indicators like bank credit, rating profile, primary capital market mobilization, etc. remain muted.

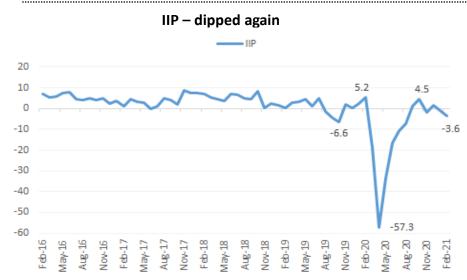
Note: The ASK Composite Activity Indicator (ACAI) is a comprehensive tracker of the economy with a data dashboard of 36 key indicators of the economy covering nearly all aspects of the non-agricultural economy including energy, manufacturing, investments, real estate, infrastructure, foreign trade & investments, transports, financial services, and measures of corporate and government financial health and household well being. The number of variables that are at (yellow), above (green) or below (red) their historical average for the period, provides a good guide to the state of the economy. The aggregate of the 36 indicators into a single index - ACAI incorporates the extent of variation in the variables apart from their direction of change. ACAI is meant to serve as a more recent (nowcasted) and alternative measure of economic activities to be available before the GDP data is released for the quarter

Economy shows contrasting trends

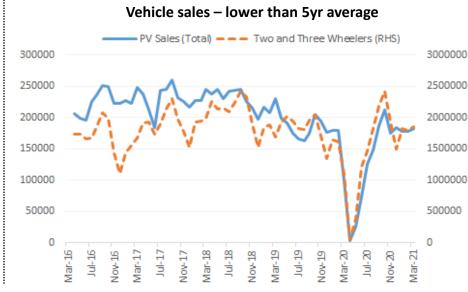








Sources - CMIE, Refinitiv, ASKWA Research







Equity markets have performed in FY21 but have become footloose too – High market correlation sectors



	Sensex	Cons Discre Goods & Serv	Finance	Industrials	Banks	Basic	Capital	BSE Metals	Power	PSUs	Cons Durables
Quarterly Return		Goods & Serv				Materials	Goods				Durables
Jun-17	4.4	0.1	8.1	2.5	7.6	5.8	2.0	-3.7	-2.2	ГС	5.0
	4.4	8.1		3.5			3.8			-5.6	
Sep-17	1.2	4.6	5.3	0.9	2.8	8.1	0.6	19.3	-0.9	2.6	9.6
Dec-17	8.9	16.6	4.5	14.8	6.8	13.3	11.4	10.1	8.0	10.2	29.3
Mar-18	-3.2	-8.7	-4.2	-9.3	-5.8	-11.6	-3.4	-10.8	-10.7	-14.3	-1.9
Jun-18	7.5	-1.2	5.8	-7.9	7.6	-5.3	-5.4	-1.9	-8.4	-7.2	-9.2
Sep-18	2.3	-8.6	-7.2	-7.7	-4.3	0.6	-2.2	1.6	-0.9	-1.7	-5.3
Dec-18	-0.4	2.1	8.5	5.0	8.5	-4.2	10.0	-10.8	3.6	0.9	8.2
Mar-19	7.2	-1.6	8.5	-0.8	12.4	1.1	-1.9	-4.1	1.8	5.6	15.3
Jun-19	1.9	-3.8	3.6	2.2	2.4	-0.6	7.5	-2.2	2.9	2.5	9.5
Sep-19	-1.9	-0.6	-6.0	-7.2	-6.0	-9.3	-5.8	-18.2	-7.6	-15.0	-1.0
Dec-19	6.7	4.6	11.8	-2.1	11.5	4.7	-9.4	14.8	-0.4	4.5	-3.3
Mar-20	-28.6	-30.9	-38.5	-36.1	-39.9	-32.3	-35.2	-45.2	-28.5	-35.9	-22.6
Jun-20	18.5	23.0	14.7	24.4	10.2	30.1	17.1	26.2	14.3	9.5	5.0
Sep-20	9.0	15.3	1.1	12.1	0.3	14.7	7.6	15.2	5.0	-7.0	19.4
Dec-20	25.4	22.9	41.5	32.3	47.4	24.8	35.5	39.7	24.8	27.4	25.2
Mar-21	3.7	2.9	4.1	21.3	4.6	25.5	12.5	23.7	20.0	16.0	8.0
Financial Year											
FY18	11.3	20.4	14.0	8.8	11.4	14.6	12.3	12.8	-6.5	-8.6	45.9
FY19	17.3	-9.3	15.5	-11.4	25.5	-7.8	0.0	-14.8	-4.3	-2.8	7.2
FY20	-23.8	-30.9	-33.2	-40.6	-35.4	-36.1	-40.6	-49.7	-32.3	-41.6	-18.8
FY21	68.0	79.3	70.8	123.5	70.3	133.5	92.1	151.2	79.6	50.3	69.5
Quarterly Average											
FY07 -FY14	3.0	2.6	4.9	3.5	5.3	2.7	3.8	3.1	1.1	1.3	4.6
FY15 -FY21	3.3	4.1	4.4	3.4	4.4	4.5	3.1	3.0	2.1	1.1	6.7
FY07 -FY21	3.2	3.3	4.7	3.4	4.9	3.5	3.5	3.1	1.5	1.2	5.6

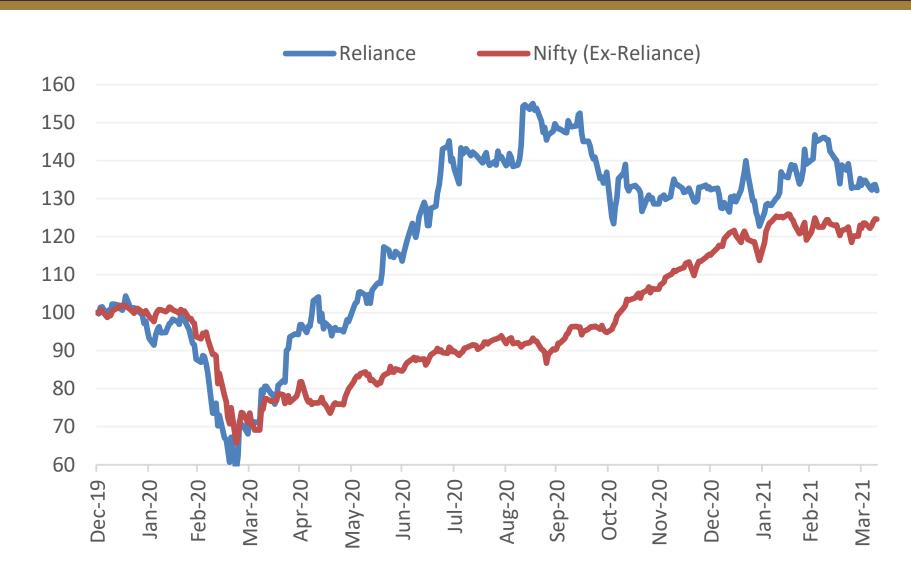
Equity markets have performed in FY21 but have become footloose too – Low market correlation sectors



	Sensex	Auto	IPO	Utilities	Realty	Oil & Gas	Energy	Healthcare	Telecom	BSE IT	FMCG
							- 07				
Quarterly Return											
Jun-17	4.4	6.3	14.6	-0.8	27.7	-2.7	-1.7	-7.3	5.2	-5.1	12.5
Sep-17	1.2	3.3	1.6	5.4	1.1	12.4	11.9	-5.0	4.5	1.2	-6.3
Dec-17	8.9	10.6	4.6	10.8	26.3	9.7	11.7	9.7	22.8	13.4	9.4
Mar-18	-3.2	-10.1	2.1	-11.5	-14.5	-10.3	-6.4	-11.1	-21.1	7.3	-3.8
Jun-18	7.5	-0.9	-3.5	-6.5	-7.0	-6.5	0.2	6.4	-10.3	15.0	9.0
Sep-18	2.3	-9.9	-12.8	0.4	-17.9	8.8	18.3	7.3	-13.8	12.3	2.6
Dec-18	-0.4	-3.0	4.6	2.5	5.6	-7.5	-9.8	-7.3	-3.3	-9.9	2.8
Mar-19	7.2	-9.6	1.1	0.6	15.5	11.1	16.9	3.5	3.9	8.5	-0.7
Jun-19	1.9	-4.9	11.2	-1.3	6.0	-3.1	-5.3	-10.5	-3.7	2.5	-3.2
Sep-19	-1.9	-6.4	10.3	-7.5	-10.2	-1.1	1.8	-3.1	-2.1	0.1	3.6
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Mar-20	-28.6	-41.9	-27.9	-27.0	-40.6	-32.0	-29.3	-9.5	-12.9	-17.0	-10.1
Jun-20	18.5	42.2	11.4	19.3	16.8	26.4	43.4	33.9	34.4	15.9	9.8
Sep-20	9.0	17.0	35.6	-6.9	5.7	-3.4	21.7	21.7	-20.7	34.2	-1.8
Dec-20	25.4	16.4	17.0	22.9	48.3	15.1	-5.4	9.5	22.5	21.4	14.1
Mar-21	3.7	6.9	4.9	19.6	7.8	5.2	3.9	-1.6	2.2	9.5	2.1
Financial Year											
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FY19	17.3	-21.7	-11.0	-3.2	-6.9	4.5	25.0	9.5	-22.3	26.3	14.1
FY20	-23.8	-42.9	1.3	-32.8	-34.8	-34.4	-25.9	-15.7	-5.4	-15.9	-12.7
FY21	68.0	107.1	85.6	63.2	97.3	47.9	71.6	75.6	33.4	106.7	25.5
Quarterly Average											
FY07 -FY14	3.0	4.2	2.2	1.8	3.3	3.1	3.1		1.3	3.5	3.5
FY15 -FY21	3.3	2.9	6.6	2.4	4.1	2.3	4.3	3.3	1.1	4.5	2.5
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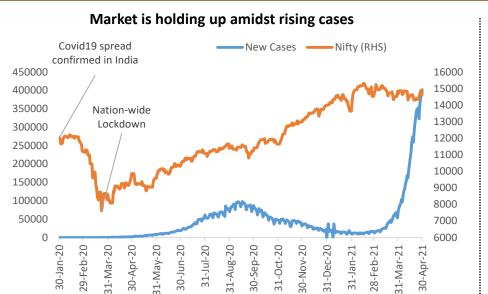
The Reliance factor: Did it make a real difference to portfolios?

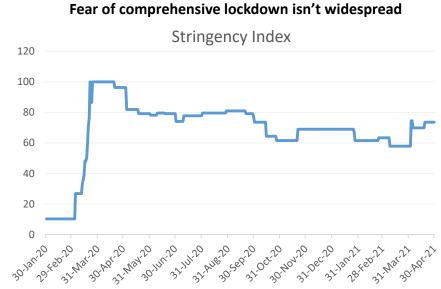




The market hasn't reacted much to Covid second wave yet

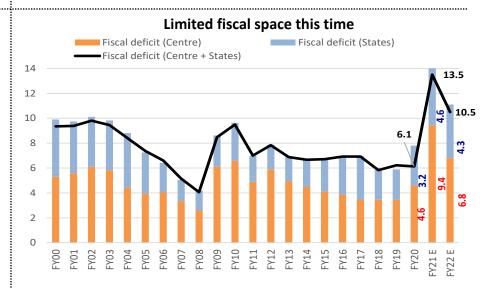






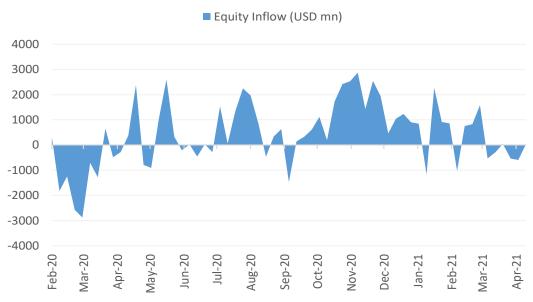
Vaccination of major population to take whole of FY22 People fully vaccinated (%) People vaccinated (%) 100 90 60 50 40 30 20 10 Apr-21 May-21 Jun-21 Jul-21 Jul-21 Sep-21 Nov-21 Nov-21 Jan-22

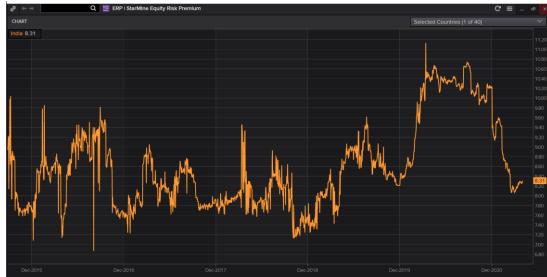
Sources - CMIE, Refinitiv, ASKWA Research



FIIs flow dip as India Equity Risk Premium (ERP) goes down

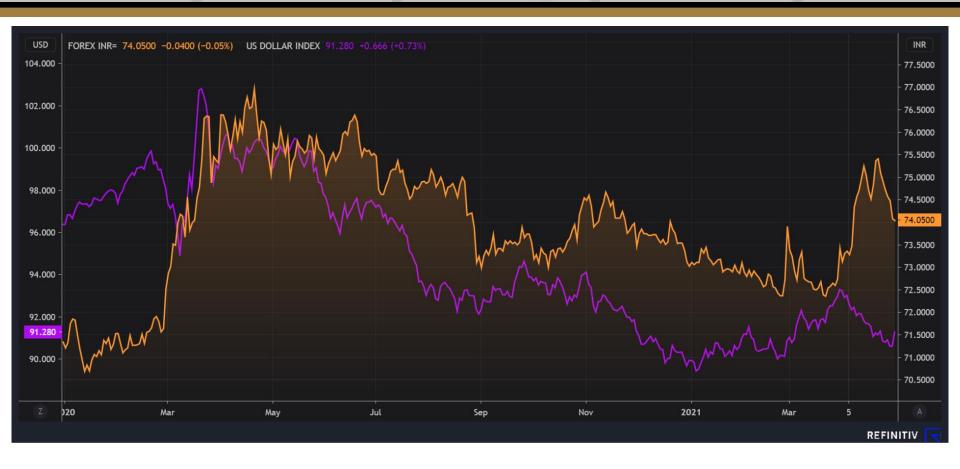






The currency factor: INR depreciates while DXY has started gaining

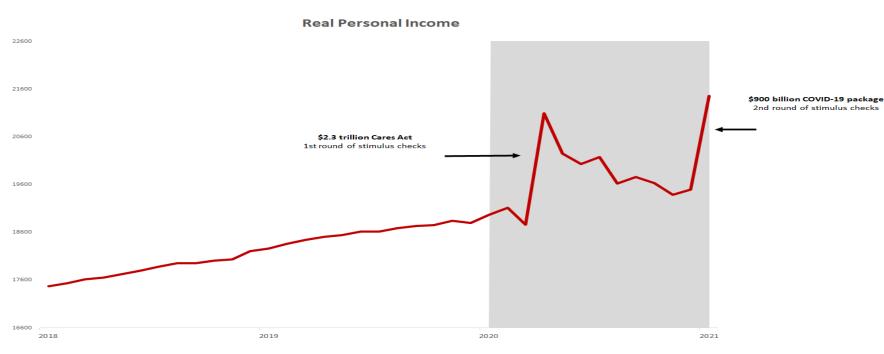




Global equity: US protected its non-tradeables sector

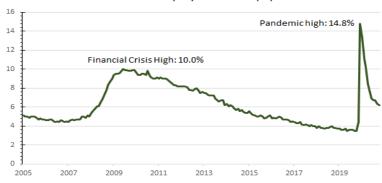


Personal income received a booster through budgetary programme



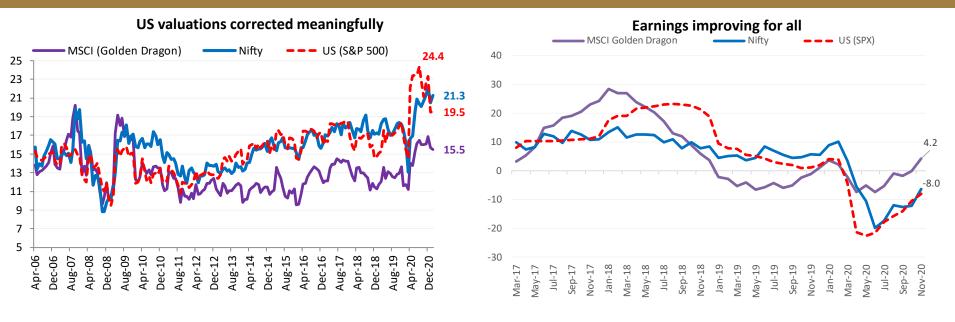
US Labour market is healing

U.S. Unemployment Rate (%)

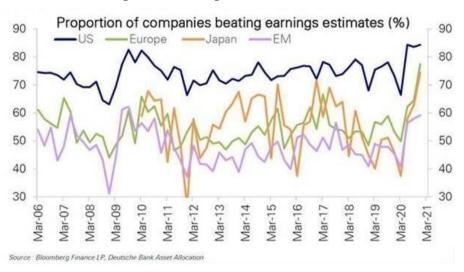


Valuations getting support of earnings: China still cheap





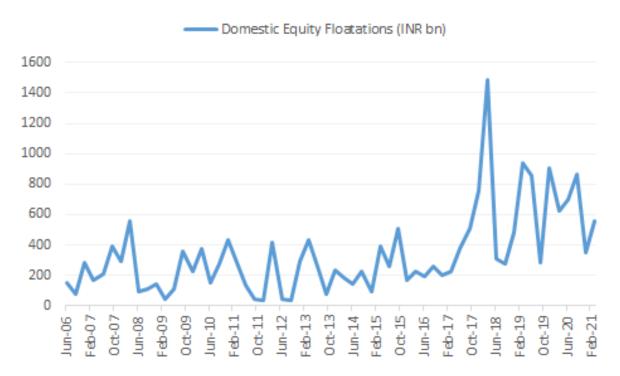
Earnings beat still highest in US



However, valuation froth exists in various pockets

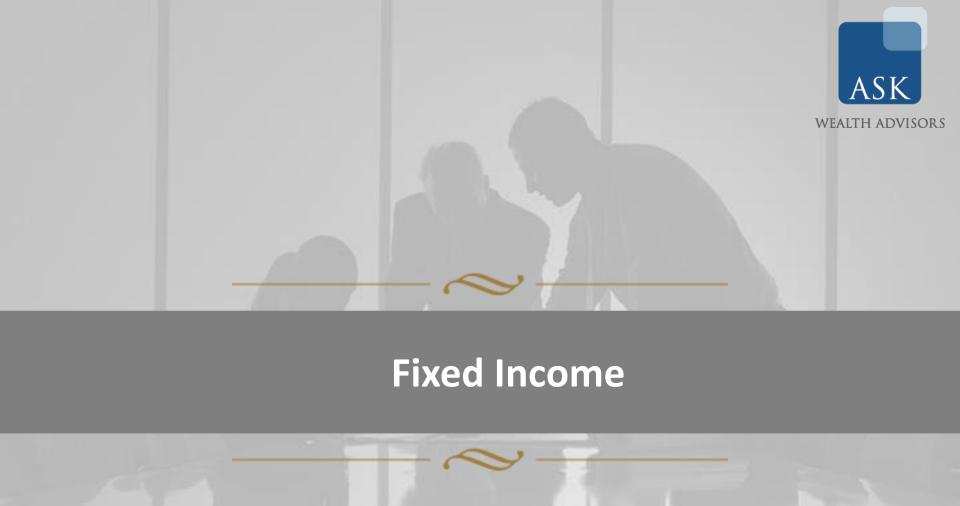


A boom in the floatation of new equity issues



However, many underperformed

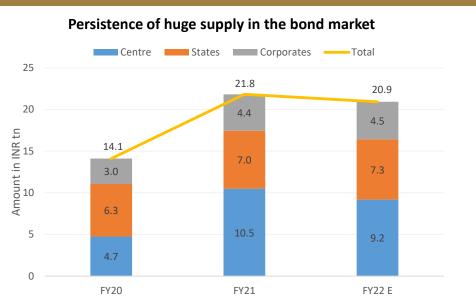
No. of IPOs	47
No. where listing price below offer	16
No. where current price below offer	17
No. where current price below listing	24

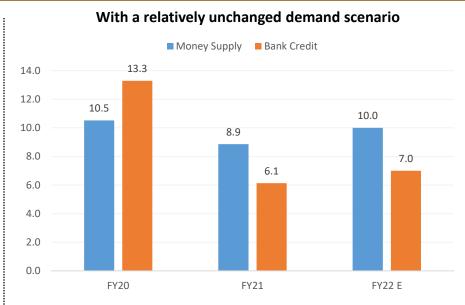


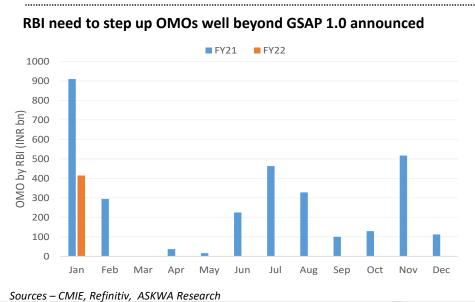


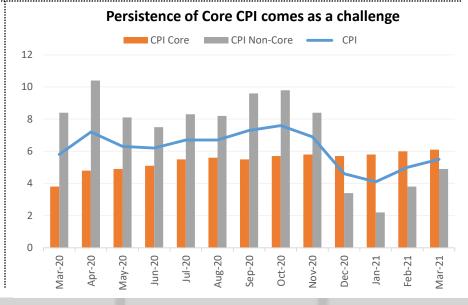
Supply overhang to keep yields rangebound





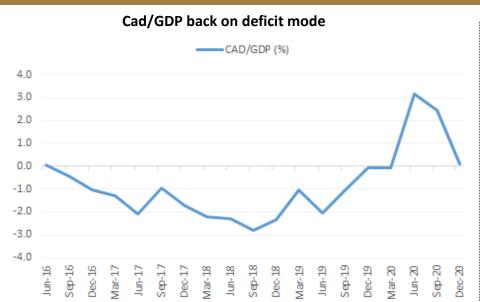


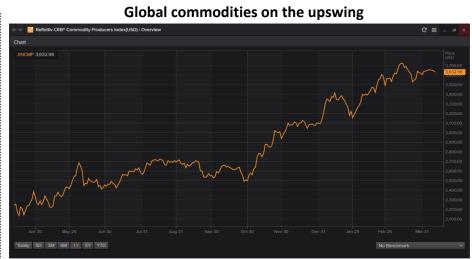


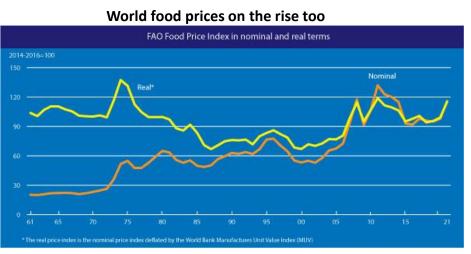


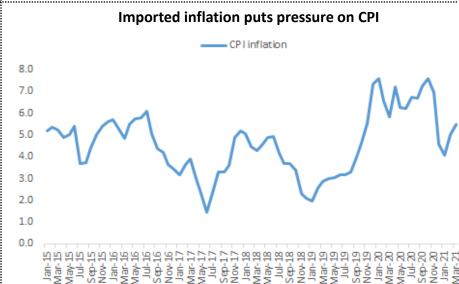
CAD, INR, commodities resulting in higher imported inflation





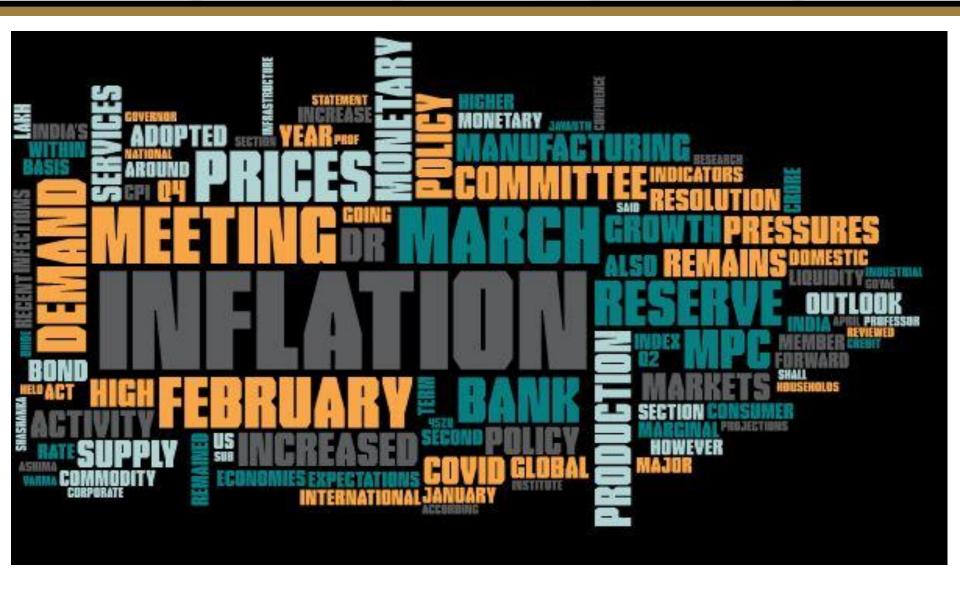






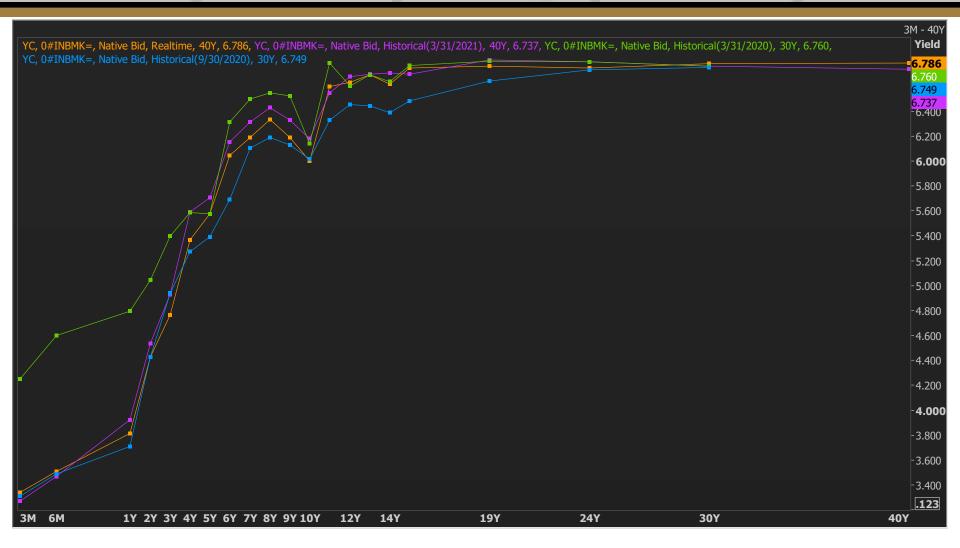
Inflation concern gives little headroom for RBI's response to Covid second wave





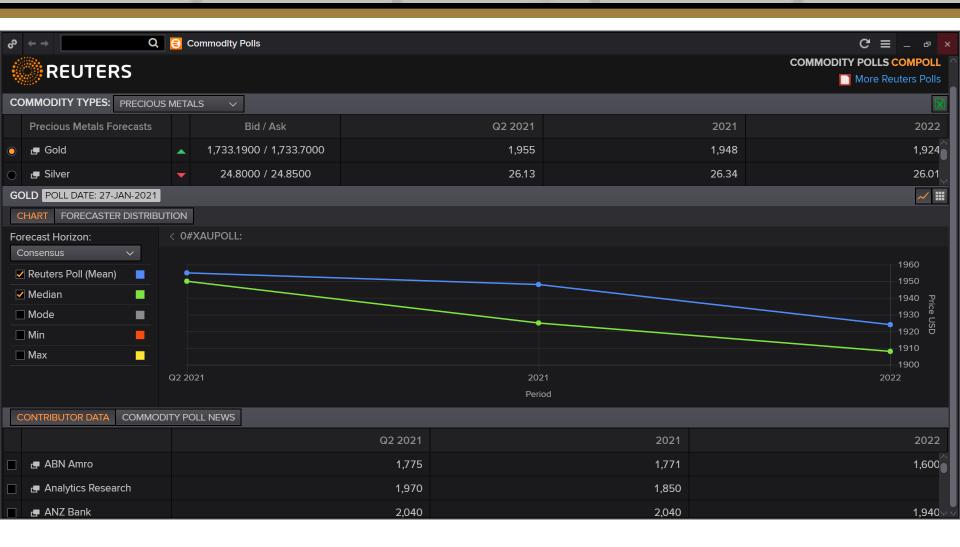
Fixed income: A play on yield curve





Gold: Negative outlook persists





Strategy: Overweight Equity; Domestic/ mid-cap/financial overweight too



Equity: Time to build portfolios taking advantage of near-term softness

- 1) Global consensus trade favours equity with its weight ruling at pre-Covid highs.
- 2) The macro scenario continue to underline the recovery that was getting slowly broadbased while the second wave of Covid is likely to cause some near-term setback. However, the traction on order book, robust tax collection and corporate profit point to the new catalysts that would help catch up on the growth curve once the Covid-related uncertainties subside.
- 3) Domestic equity markets performed well to return nearly 70% gain in FY21 after the dip of -24% last year while almost all sectors outdid the benchmark large cap index. However, FIIs flows have turned into outflow in Apr-21 in the backdrop of Covid second wave, a decline in equity risk premium of India and an altered INR expectations. Amidst all these and a flare up of Covid crisis, equity market has held up relatively well.
- 4) The underlying resilience of the market is palpable as earnings recovery have kept valuations under check even though pockets of overvaluation surely exists.
- 5) Prospects of US and China markets stays well based on the fiscal/monetary measures of the latter.
- 6) Long-term investors should look through the near-term uncertainties due to Covid and use the somewhat soft market to rebuild portfolio with higher tilt for domestic equities and within that higher allocation for mid/small cap and thematics.

We have turned overweight on equities with overweight on mid/small cap and financials.

Strategy: Underweight Fixed Income



Fixed Income market:

- There is a heavy borrowing programme lined up in FY22 including that from the Central, State governments and the private sector. This creates a supply overhang for the second year in succession.
- 2) Institutional demand would be shaped by an expected pick up of credit growth on moderate revival hope of the economy particularly the manufacturing sector.
- 3) Meanwhile inflationary pressure stays high both on account of imported inflation due to rising metals/commodity prices and depreciating outlook of INR. The persistence of core inflation also likely to keep the overall inflation high.
- 4) RBI clearly need to step up its OMO programme well beyond GSAP 1.0 announced and would also need sufficient liquidity buffer to keep the yield curve in shape.
- 5) The mid-duration play remains the favoured strategy to play the current shape of yield curve which offers little spread at the longer duration and low carry at the shorter end.
- 6) We have also turned over/under weight short/medium term to take benefit of a faster repricing in a rising interest rate scenario and to avoid greater MTM loss in case of longer maturity.

We see limited headroom for RBI to reverse the process of gradual withdrawal of accommodative stance and gear it towards a second round of easing for Covid response. The Gsec yields are likely to move within a narrow range therefore with limited upside.

We have thus turned underweight on fixed income.

Strategy: Overweight Hybrid (REITs/InvITs) and Underweight Commodities (Gold)



REITs/InvITs:

- 1) REITs/InvITs are at a nascent stage of development and is poised to be a major source of funding for India's growing housing and infrastructure sector.
- 2) There are incipient signs that the real estate sector is emerging out of the Covid-19 related crisis reflected in absorption of properties as well as in a reduction in inventories. There is also an increased demand and price pressure on the steel and cement sector.
- 3) Government support in the form of tax benefits as well as acceleration of urban and transport infrastructure is facilitating rapid growth of the two avenues.

We have therefore stayed **overweight on REITs/InvITs** in view of the improved economic and financial prospects of these two emerging channels.

Gold:

- Gold has fallen 15% from its peak in Aug-20 when equity and other asset classes started rallying on the back of a recovering economy.
- 2) The rising outlook of US bond yield has come as a major dampener for further meaningful rally of gold. Emerging alternative like cryptocurrency is another major drag.

In view of weakening of the relationship between gold and other financial variables and relative higher valuation we **stay underweight on gold.**





Model portfolio: Construct and Stance



IDC Classes	A (Cult A Cl	Unconstrained Model Portfolio (UMP)									
IPC Stance	Asset/Sub-Asset Class	AGGRESSIVE		ASSERT	ASSERTIVE		ICED	CAUTIC	ous	CONSERV	/ATIVE
		SAA	TAA	SAA	TAA	SAA	TAA	SAA	TAA	SAA	TAA
ow	Equity Allocation	80.0	85.0	63.8	68.8	47.5	52.5	31.3	36.3	15.0	20.0
UW	Offshore Funds	12.0	8.5	9.6	6.9	7.1	5.3	4.7	3.6	2.3	2.0
N	US ETFs, FOFs	8.0	5.7	6.4	4.6	4.8	3.5	3.1	2.4	1.5	1.3
N	China FOF	4.0	2.8	3.2	2.3	2.4	1.8	1.6	1.2	0.8	0.7
ow	Domestic Funds	68.0	76.5	54.2	61.9	40.4	47.3	26.6	32.6	12.8	18.0
UW	Large Cap Funds	30.6	30.6	24.4	24.8	18.2	18.9	12.0	13.1	5.7	7.2
UW	Multicap / Focussed Funds	23.8	23.0	19.0	18.6	14.1	14.2	9.3	9.8	4.5	5.4
ow	Midcap Funds	10.2	15.3	8.1	12.4	6.1	9.5	4.0	6.5	1.9	3.6
ow	Thematic/Sectoral/Special Situation	3.4	7.7	2.7	6.2	2.0	4.7	1.3	3.3	0.6	1.8
UW	Fixed Income / Debt Allocation	15.0	10.0	31.3	26.3	47.5	42.5	63.8	58.8	80.0	75.0
ow	Mutual Funds / ETF	10.4	6.4	23.4	19.4	36.4	32.4	49.4	45.4	62.4	58.4
ow	Short / Medium Term High Grade	4.2	2.9	9.4	8.7	14.6	14.6	19.8	20.4	25.0	26.3
UW	Long Term High Grade	6.2	3.5	14.0	10.7	21.8	17.8	29.6	25.0	37.4	32.1
uw	Secondary Market Bonds / MLD's / Tax Frees	2.6	1.6	5.9	4.9	9.1	8.1	12.4	11.4	15.6	14.6
N	Cash	2.0	2.0	2.0	2.0	2.0	2.0	2.0	2.0	2.0	2.0
ow	Hybrid	2.0	4.0	2.0	4.0	2.0	4.0	2.0	4.0	2.0	4.0
uw	Commodities	3.0	1.0	3.0	1.0	3.0	1.0	3.0	1.0	3.0	1.0
1	Total	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0

Model portfolio: Outperformance over longer period



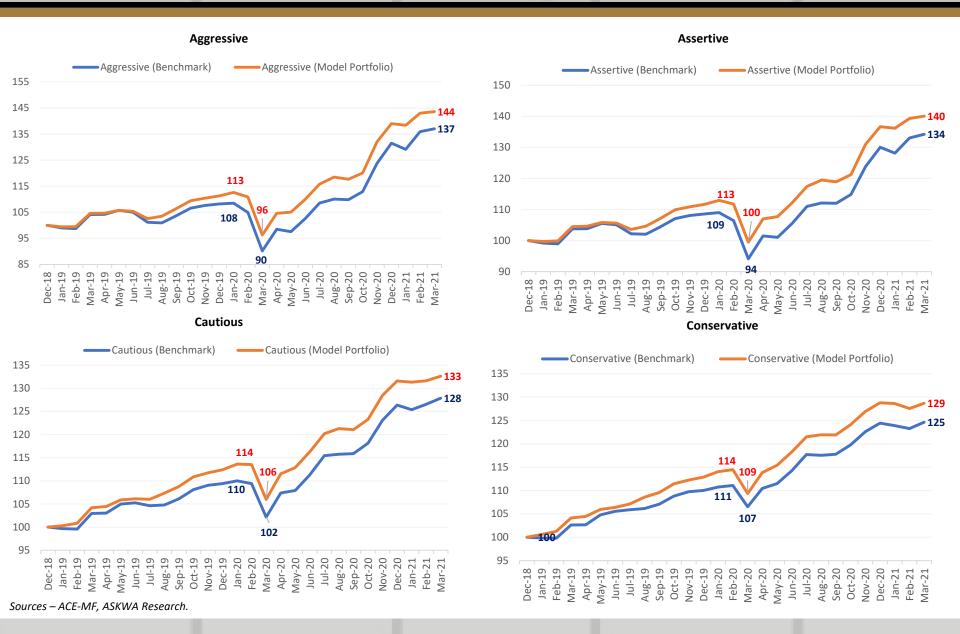
		1m	3m	6m	1у	2y	2y	Зу	Зу	Since Inception	Since Inception
		(Mar-				(CAGR)	(PoP)	(CAGR)	(PoP)	(Jul-17) (CAGR)	(Jul-17) (PoP)
		21)									
Aggressive	BM	0.8	4.2	24.8	52.0	14.7	31.6	12.5	42.2	10.7	45.2
	MP	0.4	3.3	22.0	49.2	17.2	37.3	12.8	43.6	10.8	45.7
Assertive	BM	0.9	3.2	19.8	42.6	13.7	29.3	11.8	39.6	10.1	42.5
	MP	0.5	2.5	17.8	40.8	15.8	34.0	12.2	41.3	10.4	43.7
Balanced	BM	1.0	2.2	15.0	33.7	12.7	27.0	11.0	36.9	9.5	39.6
	MP	0.6	1.6	13.6	32.9	14.4	30.9	11.7	39.3	10.1	42.2
Cautious	BM	1.0	1.2	10.4	25.2	11.4	24.2	10.1	33.5	8.8	36.1
	MP	0.8	0.8	9.5	25.1	12.8	27.3	10.9	36.6	9.6	40.0
Conservative	BM	1.1	0.2	5.8	17.0	10.2	21.4	9.2	30.4	8.0	32.7
	MP	0.9	-0.1	5.6	17.7	11.2	23.6	10.1	33.6	9.0	37.2
Nifty 50	BM	1.1	5.1	30.6	70.9	12.4	26.4	13.3	45.3	10.8	45.8

Note: BM - Benchmark, MP - Model Portfolio

Return for various period (1M, 3M, 6M, 1Y, 2Y and since inception have been computed with Mar-21 as the most recent period.

Model Portfolios – Maintaining outperformance so far





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