Market Outlook - March 2023

ASK Investment Managers

Dear Investor,

Month of correction in Global Equities

We have witnessed correction in Global Equities in February 2023 and there are multiple factors at play:

A) Concern over global inflation continued to weigh heavy as January US inflation print came in at 6.4% YoY against the expected 6.2% YoY. Though inflation continued to come off for 7th month, it was the pace of easing that bothered markets leading to US 10Y going up by ~41 bp during the month,

B) On the other hand, economic data continues to be strong, with advance US retail sales growing by 3% MoM (against expect 2% MoM growth) – the largest gain since 2021, further fueling the hypothesis of higher for longer in terms of interest rates,

C) Further on geopolitical concerns resurfaced with China engaging in dialogue with Russia and President Biden's Ukraine visit, which weighed negatively on overall sentiment.

While MSCI EM has been down ~6.5% in February in USD terms, led by declines in Hong Kong, Korea, Malaysia, and Brazil, MSCI World index held up better with ~2.5% down move, primarily led by a decline in the US market. Indian equities, on the other hand, continued to hold up - outperforming their Emerging market counterparts, with ~3% fall in Nifty 50 in USD terms. India's outperformance could be attributed to the stronger earnings performance and overall stable economic data of the country.

The Indian equity market remained weak with Nifty 50 seeing a fall of 2% in local currency terms. The broader market underperformed, with BSE 500 seeing a 2.9%. PSU banks index saw a sharp decline of around 9% on profit booking and on concerns around Adani exposure, while metals and utilities were down by approximately 13% and 18%, respectively. On the other hand, IT sector saw up move of ~3% during the month on the back of decent quarterly performance and no negative surprise in the quarter gone by. FMCG and Capital goods also saw an uptick of around ~2% each benefitting from domestic demand momentum. Financials and Auto Indices were down ~3% and ~2%, respectively.

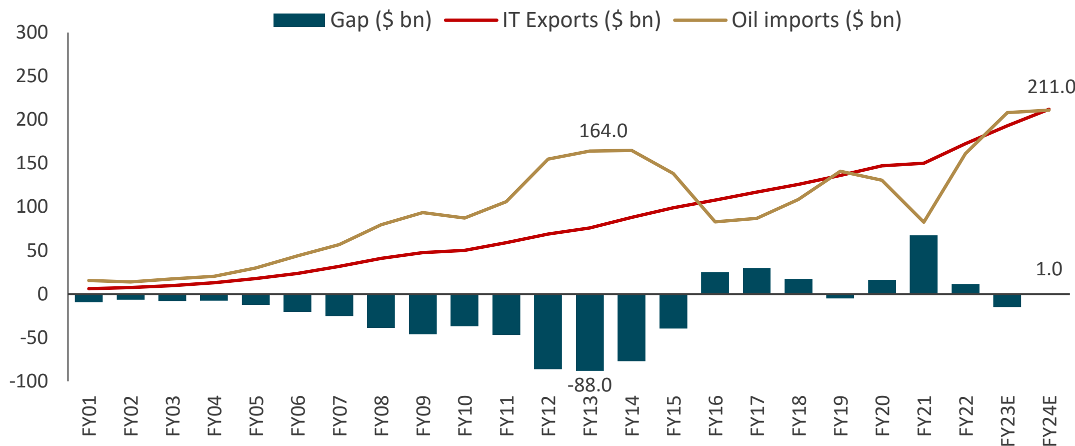
Crude and Balance of Payments (BOP)

Crude has been a one factor that has had impact on India's external balance. The consensus view currently is of balanced oil market in 2023. However, predicting oil supply and demand is very tricky, as apart from demand supply, geopolitics too play an important part. Following factors need to be watched very closely: a) Russian production; b) China demand; c) US Supply. Any surprise here can lead to imbalance.

While crude price remain as uncertain as ever, India should be relatively better able to manage the pressure, primarily on two counts:.

- The normalization of supply chains globally that bodes well for ensuring lower commodity prices pressures ex of crude oil. Reuters CRB Index has fallen 9.7% YoY so far this financial year.

- The current account dynamics in India are turning supportive amid relative resilience of software services earning (USD 63.3 bn net inflow in H1FY23 vs USD 51.91 bn in H1FY22). With the recession in West projected to be shallow, the risks to software earnings are far less pronounced than earlier feared. Over period with consistent rise in IT exports, the gap between IT exports and Oil imports have reduced considerably, that can be a big support As such FY24 may continue to witness stable inflows under invisible head including remittances (which will be steady due to elevated oil prices).



Source: Bloomberg, ASK IM Research

Amid resilient earnings under IT services exports and consistency in remittance income earnings, FY23E CAD is expected to fall below 3.0% from 3.4% of GDP estimated earlier. FY24E CAD is estimated at 2.9%-3% which is well within the sustainable zone.

With respect to inflation, the energy shock post Russia Ukraine war has shown us that government can well manage the inflation shock by not allowing the pump prices to rise in times of rising oil prices and to fall in times of falling oil prices. While this does put pressure on earnings of OMCs, it helps government to manage the inflationary pressures better. Amid El Nino risks and premature heat wave conditions in India, food inflation can be a much bigger worry than energy inflation. Moreover, the pressure that was emerging due to passthrough of higher natural gas prices is expected to provide some relief. Platts JKM slid below the $15/MMBtu mark recently -- the lowest level since August 2021.

Valuations and Flows

In January, there was an outflow of USD 3.7 bn, but in February, Foreign Institutional Investors (FII) flows remained more or less flat. This can be attributed to the strong earnings performance of Indian equities and geopolitical uncertainty. In the same month, Domestic Institutional Investors (DII) invested a net of USD 1.3 bn, primarily driven by robust retail participation as demonstrated by USD 1.7 bn worth of SIP inflows.

The Nifty's 12-month forward PE ratio has corrected by around 22%, declining from its peak of 22.9x to 17.9x. Valuations are off-peak and relatively more comfortable.

Indian markets outperformed global equities in February (after a weak January on a relative basis), continuing the trend from CY22. Indian market outperformance is led by strong earnings performance and policy stability in the country. Earning outlook for India remains robust partially led by easing raw material prices, and also low credit cost for banks which is expected to lead to strong earnings growth in the coming quarters.

Happy investing!

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