PhillipCapital

Macro and Strategy Outlook

Slowdown to aggravate; domestic and global

12 March 2020

INDIA | MACRO & STRATEGY I Annual Publication

Anjali Verma (+ 9122 6246 4115)
anverma@phillipcapital.in

Aditi Mohol (+ 9122 6667 9943)
amohol@phillipcapital.in

We expect India's FY20 GDP to close at 4.5%, Q4FY20 will be hit by Covid-19. While there is extreme uncertainty about the duration and extent of its impact on economic slowdown, we do anticipate that 2020 globally and FY21 in India will be a year of grinding economic and earnings growth. Assuming that Covid-19 is contained by Q1FY21, we place FY21 GDP growth at 4.5-5% and March 2021 Nifty target at 10700-11200. In case of its long-lasting impact, GDP growth can dip to 3.5-4% and Nifty to 8500-9200 (intermittently). A solid/concerted/global fiscal and monetary stimulus will be a positive for equities from the current levels. We have been highlighting the limitations of global monetary stimulus in case of an economic slowdown (yields already near bottom vs. at peak at the time of financial crisis). Over the last decade, global growth/equities were supportive for India, not the case anymore.

Additionally, we have the problem of Yes Bank collapse in India, whose financial response/impact is still unknown. With the peril of Yes Bank and weak economic activity, other weak players could fall prey to higher NPAs eating into capital and inability to raise capital – Our much anticipated consolidation theme is now playing out in the financial sector as well – which will be a growth grinding process (read benign credit growth).

All other Indian macro data (inflation, CAD, interest rates, liquidity) should remain supportive. Brent is a strong positive for India. We expect RBI to lower rates by 50-100bps from hereon, 10-year bond yield at 5.8%-6.5%, USD-INR range of 71-76. Current corporate earnings estimates are expected to be slashed; we assume 10-12% earnings growth in FY21-22.

2HFY21 should fare better, thus we suggest adding equities on the decline. The lasting impact of current slowdown will be in terms of limited gains/returns and flows. While on the basis of current earnings estimates, equities are looking attractive at current levels, but our base case scenario is of sharp earnings cut in FY21 and FY22.

Macro outlook – GDP on declining trend for varied factors: Our forecast for GDP growth is at 4.5-5% for FY21 and 5.0-5.5% for FY22. Growth trends have been disappointing in the last three years; a rise from here will be grinding due to limited triggers and higher base. We expect private consumption to fare better followed by government spending and private investments; trade will remain extremely weak for FY21-22. Manufacturing should remain weak; agriculture and services will maintain current trends.

EARNINGS – Will be SLASHED for FY21-22: While current estimates reflect decent growth, nothing exciting; we expect sharp cut in the estimates for FY21-22. Covid-19 will have adverse impact on consumption sectors which has been the key supporting segment over the last few years. Investment sector are expected to remain weak; lower tax revenue and disinvestment risk will weigh on public capex. Financials will also feel the stress of economic slowdown, possibility of higher NPAs and credit slowdown. Last when Indian markets corrected in August-September 2019 was on account of domestic slowdown, global economy was in a decent state which is not the case anymore.

We see the following scenarios playing out:

- **Base case (March'21 Nifty target of 10700-11200);** estimated 10%/12% earnings growth in FY21/22; 1-year fwd PE assumed at 17x. Our current estimates are at 12%/26%/16% for FY20/21/22 and EBITDA growth at 5%/14%/13%
- **Bear case: (long-lasting Covid-19 impact): (8500-9200):** estimated 8/10% earnings growth in FY21/22, 1-year fwd PE assumption of 15.5x.
- **Bull case: (Global stimulus, contained Covid-19 in India):** 11,700-12,200: estimated 15/17% earnings growth, 1-year fwd PE assumption of 18x.

While there is extreme uncertainty about direction that markets will take, we stick with 'only high quality thesis', we did not deter even when mid-caps were rising. Stocks we like are: HDFC, HDFC bank, ICICI bank, HUL, Asian paints, Havells, Orient electric, Trent, ABFRL, TCS, Infosys, Divi's, Ipca labs, Maruti, Escorts, Ultratech, JK cement, L&T, BEL, SRF, and Atul.

Index

GDP – Consistently hit for varied factors

Indian GDP has been in declining trend for the last three years, could have been for longer period, if the data wasn't revised/changed. Every time one expected economic activity to have bottomed/start improving, it was hit by a new dynamics. One common underlying reason has been structural change underway since the NDA government came to power in FY15, largely domestic-led reasons. This was also the time when global economies coped well and benefited from fiscal and monetary stimulus. In some economies, they even tried to reverse the stimulus confident of economic revival.

Come FY21, global economies are hit by Covid-19, its economic impact still unknown and contingent on its duration and cure. Consequently, bond yields have slumped to near zero expecting interest rate cuts, problem is, this tool has been fully exploited and no more scope is left. At the time of financial crisis, US/EU 10-year bond yield stood at 4-4.5%, implying there was scope to protect economy by lowering rates, which doesn't exist anymore, across the globe. Fiscal stimulus was also announced over the last decade. Commodity prices (barring Gold) have crashed on the fear of economic slowdown. <u>We fear, that global economy may remain tepid for a long period of time, implying lower returns across asset class. We don't envisage an economic recession yet and work with the assumption of containment of the virus in the next few months.</u>

Back in India, Covid-19 is contained so far, however, it has impacted movement, thus the business activity is expected to be hit for a couple of months. Sharp plunge in brent prices is a windfall boom for India. Collapse of Yes bank has shaken leftover confidence on the Indian economy. Reported GDP data for Q3FY20 indicated that quarter gone by was worse than 1H which was a surprise for us. Q4FY20 and Q1FY21 will be dented due to Covid impact. Thus, we expect economic momentum to remain weak, GDP growth around 5%. Long lasting impact of the virus will likely result in GDP trending to 3.5-4% range.

- **We estimate GDP growth at 4.5-5% in FY21 and 5.0-5.5% in FY22. Lower oil prices (if sustain) will be the key growth positive for India. FY20 GDP growth is expected at 4.5% due to Covid-led sharp slowdown in Q4.**
- We see private consumption and government spending to fare better, followed by net exports. Investments should remain weak.
- Services and agriculture output is expected to be stable in FY21.
- Industrial activity to remain weak.
- Agriculture production is assumed to grow at 3.5-4.0%. Robust rabi sowing is a strong positive.

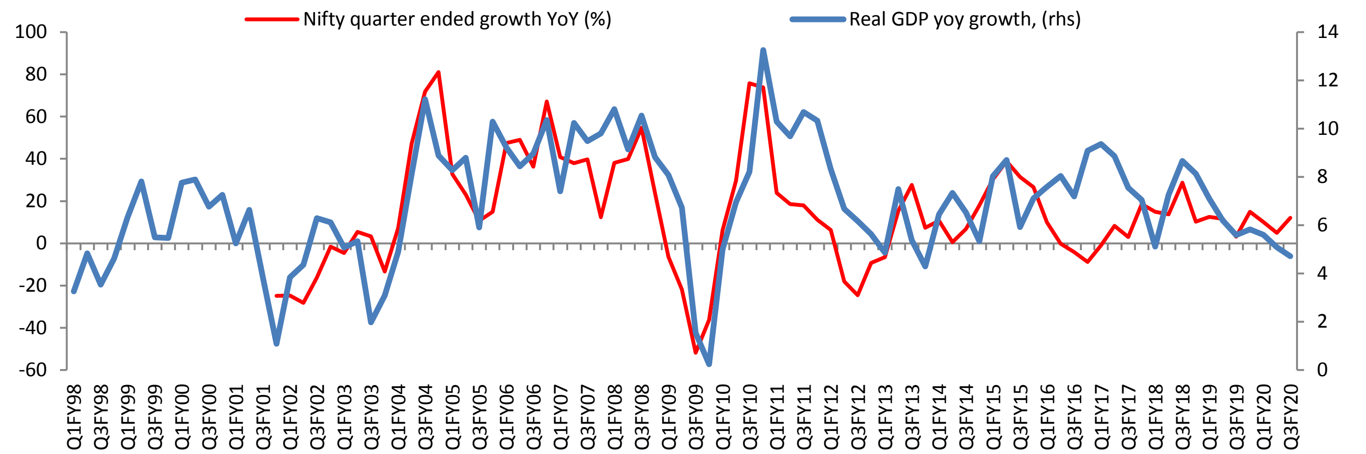
Trends and estimates of GVA (Gross value added), %

	FY15	FY16	FY17	FY18	FY19	FY20PCE	Oil = 55 Corona = H1 impact Yes bank = H1 impact FY21PCE	Oil = 50 Corona = Q1 impact Yes bank = Q1 impact FY21PCE	Oil = 45 Corona = No impact Yes bank = No impact FY21PCE	FY22PCE
Agriculture	**-0.2**	**0.6**	**6.8**	**5.9**	**2.4**	**3.7**	**3.0**	**3.5**	**4.0**	**3.5**
Industry	**8.1**	**11.9**	**8.4**	**6.8**	**4.5**	**0.5**	**-0.7**	**2.9**	**3.9**	**3.9**
Mining and Quarrying	9.7	10.1	9.8	4.9	-5.8	1.0	-1.0	1.5	3.0	3.0
Manufacturing	7.9	13.1	7.9	6.6	5.7	0.3	-1.0	3.0	4.0	4.0
Electricity, gas and water supply	7.2	4.7	10.0	11.2	8.2	1.5	2.5	4.0	5.0	5.0
Services	**9.0**	**8.6**	**8.1**	**6.7**	**7.5**	**6.3**	**5.8**	**6.2**	**7.0**	**6.8**
Construction	4.3	3.6	5.9	5.0	6.1	2.5	3.0	4.0	5.0	5.0
Trade, hotels, Transport, & Communication	9.4	10.2	7.7	7.6	7.7	5.6	5.0	5.5	6.0	6.0
Financing, Insurance, Real Estate& business services	11.0	10.7	8.6	4.7	6.8	6.6	5.5	6.0	6.7	6.7
Public administration, defence, & other services	8.3	6.1	9.3	9.9	9.4	9.0	9.0	9.0	10.0	9.0
GVA at Basic Price	**7.2**	**8.0**	**8.0**	**6.6**	**6.0**	**4.5**	**3.8**	**5.0**	**5.8**	**5.6**

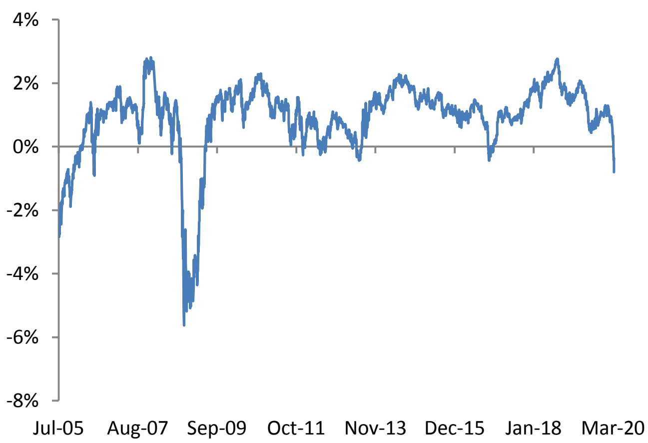
Source: RBI, CSO, PhillipCapital India Research

Key charts

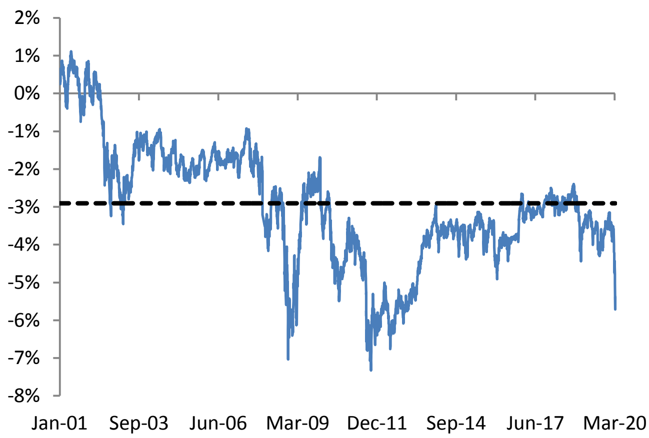
Highly correlated Nifty and GDP returns



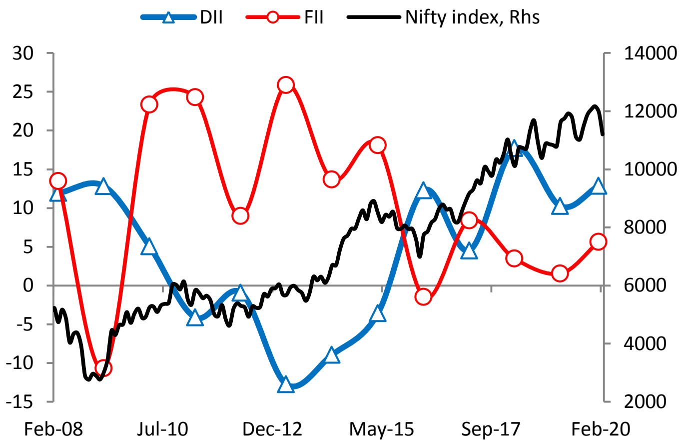
India 10 yr bond yield less Earnings yield



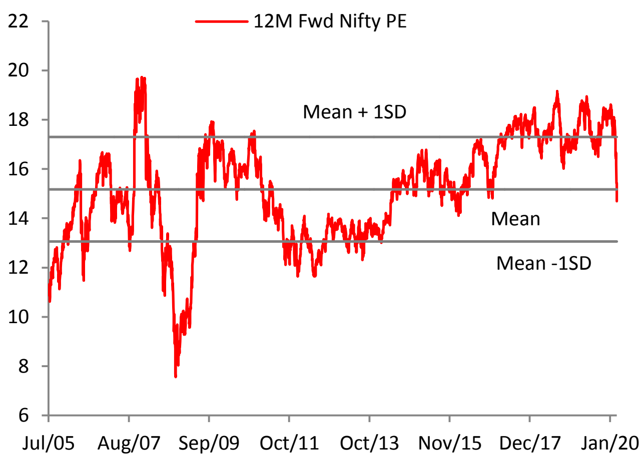
US 10 yr bond yield less Earnings yield



Financial year wise FII/DII flows in $bn

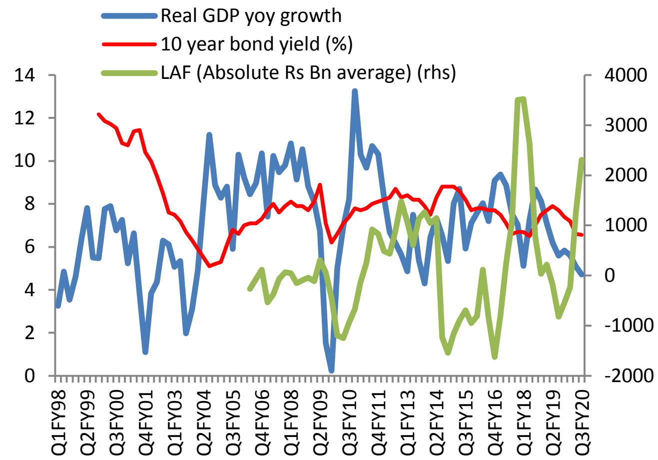


Nifty PE trends

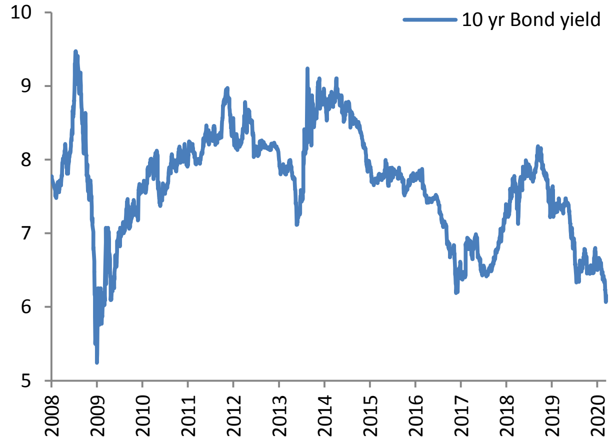


Source: Bloomberg, PhillipCapital India Research

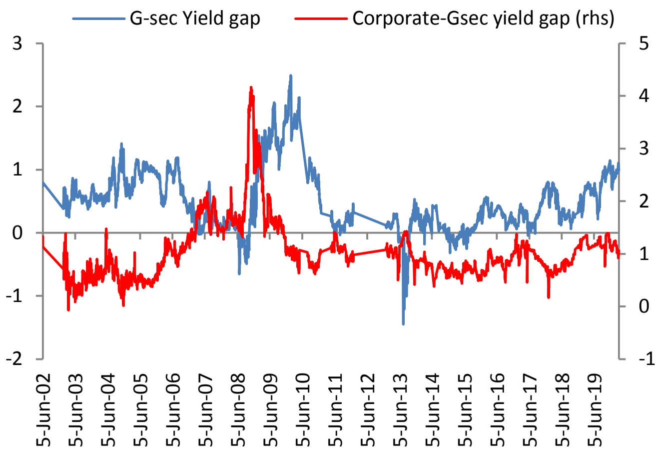
Real GDP growth, 10-yr bond yield (%) and LAF



India's bond yield curve (%)



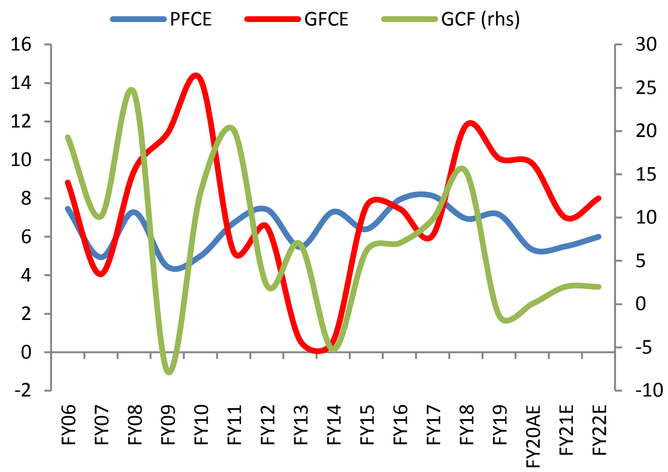
G-sec and Corporate-G-sec Yield gap (%)



G-sec bond yield curve (%)

Corporate bond yield curve (%)

Growth rates of GDP components (%)



Source: RBI, CSO, Bloomberg, PhillipCapital India Research

Macro outlook – Feeble!!

What drives an economy: C + I + G + X – M

Private consumption

Was responsible for FY20 slowdown, Stability expected in FY21

Private consumption (PFCE) growth dipped to a low of 5% in FY20 from the highs of 7-8% in FY16-19. We expect it to remain stable to marginally higher in FY21 owing to adverse impact of Covid-19 and economic weakness to keep incomes/demand muted; higer rabi sowing and cheap consumer credit is a positive; liquidity impact of the Yes bank crisis is still unknown (will be a risk factor). We see FY21/22 average growth at 5.5-6%. As on Q2FY20, PFCE/GDP share was at 56%; it can move higher to 57-58% in the medium-term, peak is at 60%.

Recovery in rural India – we are watchful: Slight uptick is being seen in terms of rural demand due to robust rabi sowing; decent government spending and a good monsoon can take it higher in the next few years. We have been highlighting the likelihood of a change in the government stance – towards relatively higher food inflation so that farmers earn higher income (theme of doubling farmers' incomes) – so far the trend is in line with our view, but we remain watchful.

A widespread domestic/global impact of Covid-19 is the key risk to further derail Indian consumption story. Chain of events that can damage Indian consumption outlook: Lower discretionary consumption due to its contagious impact ➔ higher inventory➔ higher discounts (low margin) ➔ lower production ➔ jobs/income loss ➔ lower credit demand ➔ impact on financial sector. **We opine that it will be contained/human fears normalised by Q1FY21. Its extension beyond that will have a serious adverse impact on Indian economic growth as private consumption is the largest (58%) GDP contributor. In that scenario, private consumption growth can fall to 3-4%.**

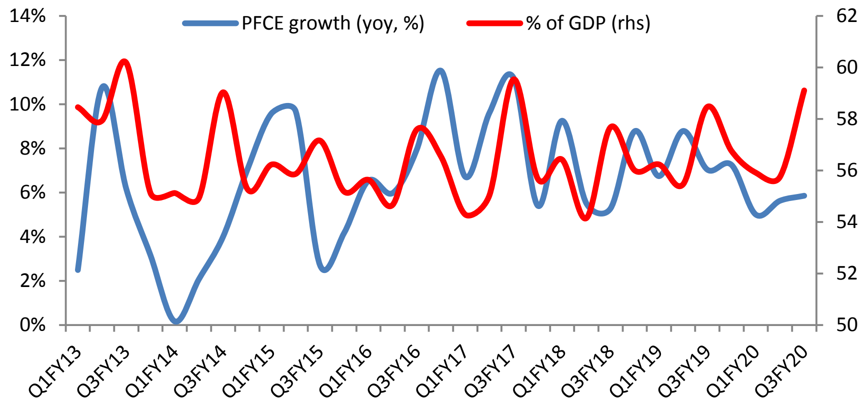
Sectors we like: Retail, consumer durables, health, clothing & footwear, education, hotels/restaurants.

Stocks we like: HUL, ABFRL, Trent, Bajaj Electricals, Orient Electric, Hitachi, Asian Paints, Maruti, Escorts.
More additions with 2-3-year horizon: Dabur, Titan, Nestle.

Long-term themes to play:

- Higher consumption, lower savings from income.
- Higher quality of consumption – premiumization to pick pace as standard of living improves and availability of more premium products
- Higher discretionary spend vs. staples.
- Herbal/organic/non-chemical segments to gain market share
- Credit-led buying.

Private consumption – Hit by Corona



Source: RBI, PhillipCapital Research

Break-up of PFCE components – consumption pattern shifting to non-basics

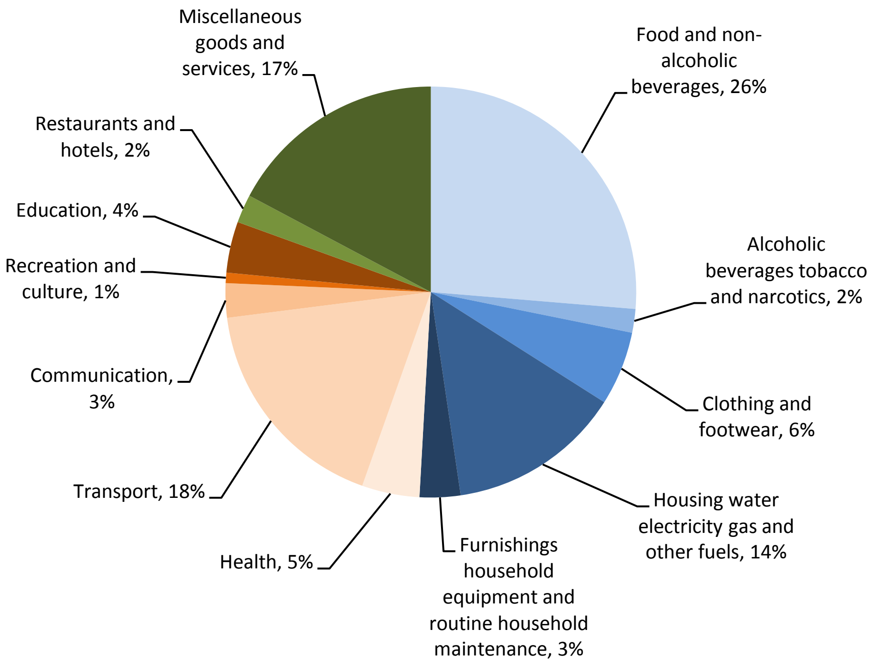
- While spending on food, fuel, water, and house (rent) remains dominant, its share in the consumption basket is consistently trending lower – currently at 40% vs. 47% in FY14.
- Rising: Transport (17.6%), miscellaneous goods & services (17.2%, comprises of personal care services (salons) & goods (jewellery/watches/leather products) and banking/legal/business services), health (4.5%), education (4%), and communication (2.7%).
- Stable: Restaurant/hotels (2.2%), furnishings (3.2%), clothing & footwear (5.8%) – we expect each of these shares to trend higher from current levels.
- Consumption of alcoholic beverages & tobacco is stable to lower – we expect this to go down.
- Share of services consistently rising (at 51.8% vs. 47% in FY14). Uptick also seen in share of consumer durables (at 3.6% vs. 3%); non-durable goods dipped to 37.5% from 41.6%.

PFCE components at constant and current prices (Rs bn)

	Constant price							Current price						
By purpose	**FY13**	**FY14**	**FY15**	**FY16**	**FY17**	**FY18**	**FY19**	**FY13**	**FY14**	**FY15**	**FY16**	**FY17**	**FY18**	**FY19**
Food and non-alcoholic beverages	15903	17059	17260	17571	19607	20249	20925	17509	20604	22482	23830	27906	29684	31240
Alcoholic beverages tobacco and narcotics	1282	1292	1415	1407	1416	1374	1480	1425	1576	1860	1999	2136	2191	2469
Clothing and footwear	3158	3766	3857	4211	4233	4274	4631	3539	4608	5050	5823	6140	6478	7315
Housing water electricity gas and other fuels	8530	9070	9523	9804	10113	10465	10871	9265	10480	11510	12182	13028	14309	15744
Furnishings household equipment and routine household maintenance	1693	1864	1988	2187	2259	2349	2552	1801	2076	2309	2490	2741	2921	3273
Health	1987	2167	2484	2745	3085	3305	3608	2143	2488	3003	3497	4109	4595	5370
Transport	7757	8009	8567	9736	10748	12804	13972	8249	9074	10045	12187	13788	16433	18805
Communication	1194	1252	1541	1609	1620	1885	2148	1267	1422	1799	1887	1954	2350	2831
Recreation and culture	520	544	576	568	580	612	651	545	604	686	710	748	809	900
Education	1937	2045	2181	2389	2625	2923	3197	2115	2405	2749	3200	3704	4308	5023
Restaurants and hotels	1206	1214	1286	1445	1561	1656	1775	1293	1386	1491	1639	1803	1983	2219
Miscellaneous goods and services	6966	7650	8749	10566	11602	12436	13703	7359	8438	9833	12287	13704	15459	17868
By durability														
Durable goods	1756	1734	1897	2064	2335	2531	2824	1768	1839	2133	2382	2720	2905	3265
Semi-durable goods	3920	4512	4792	5173	5207	5324	5754	4352	5429	6102	6936	7289	7733	8699
Non-durable goods	21899	23273	23861	24791	27080	28444	29784	24056	27890	30612	33580	38522	41456	44634
Services	24560	26413	28878	32211	34825	38033	41152	26336	30002	33970	38831	43230	49427	56462
Private Final Consumption Expenditure in domestic market	**52134**	**55932**	**59428**	**64239**	**69446**	**74331**	**79514**	**56512**	**65160**	**72817**	**81730**	**91761**	**101520**	**113059**
Final consumption expenditure of resident households in the rest of the world	602	635	821	882	989	1095	1264	643	714	935	968	1103	1258	1515
Final consumption expenditure of non-resident households in the economic territory	945	993	1123	1307	1433	1628	1698	1010	1118	1279	1433	1599	1870	2034
Private Final Consumption Expenditure	**51791**	**55573**	**59127**	**63814**	**69002**	**73798**	**79081**	**56145**	**64756**	**72473**	**81264**	**91265**	**100908**	**112540**

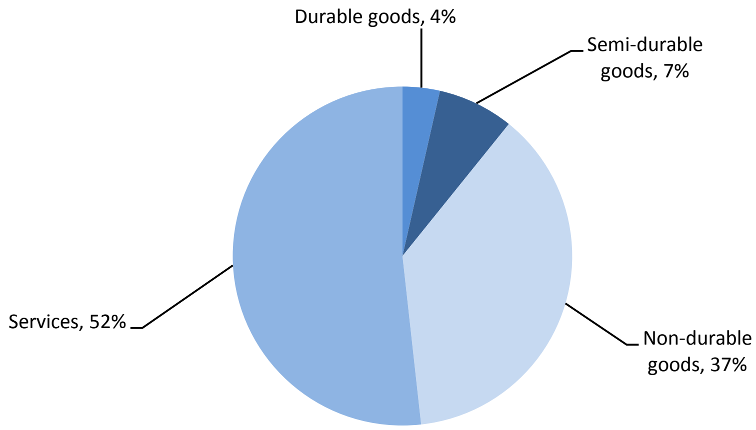
Source: RBI, PhillipCapital Research

PFCE components, by Purpose (% of total, FY19)



Source: CSO, RBI, PhillipCapital India Research

PFCE components, by durability (% of total, FY19)

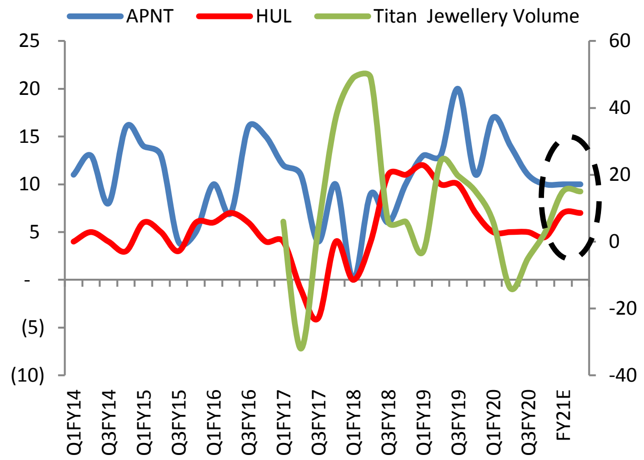


Source: CSO, RBI, PhillipCapital India Research

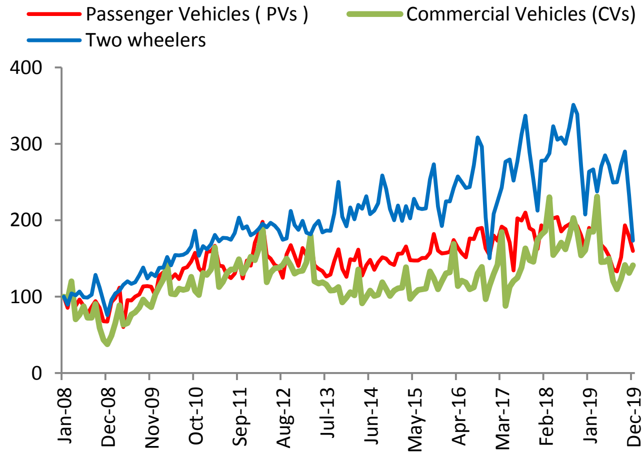
Sectoral growth trends – Staples to look better, Discretionary stable; Covid-19 – key risk

- HUL volume growth is expected to rise to 7% in the FY21-22, push to come from GSK merger. Growth was at 4.5% in FY20.
- Dabur to inch higher to 7% from 5% in FY20.
- Asian paints growth to remain stable at 10% in FY20-22.
- Jubilant to inch slightly higher to 6% from 5% in FY20.

Volume growth of key consumption companies – stable to higher



Auto segmental volume growth (Base: Jan-08 = 100)

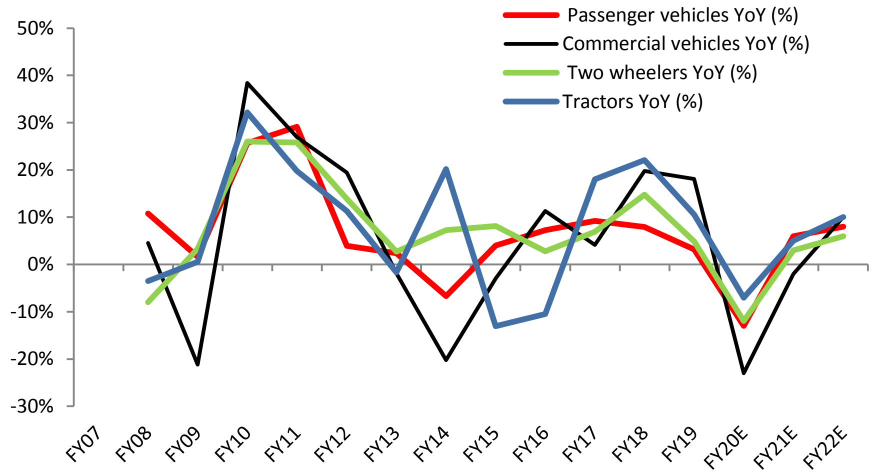


Source: ACE Equity, Companies, PhillipCapital India Research

For automobiles – PVs to fare decently; others tepid

- PVs to inch higher to 6% in FY21 from -13% in FY20.
- 2Ws to remain muted at 3% growth vs. -12% in FY20.
- CVs likely to contract in FY21 as well by 2% vs. 23% in FY20.

Auto segmental volume growth – to pick up from FY21E for PVs, tractors, and 2Ws; CVs will take longer



Source: Ace Equity, PhillipCapital Research

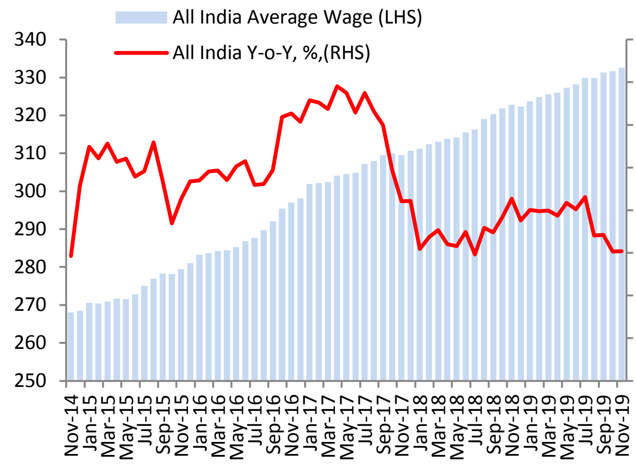
For Retail – SSSG growth trends are expected to be stable in FY21 across companies.

Retail companies SSSG growth (%) – stable growth trend in FY21

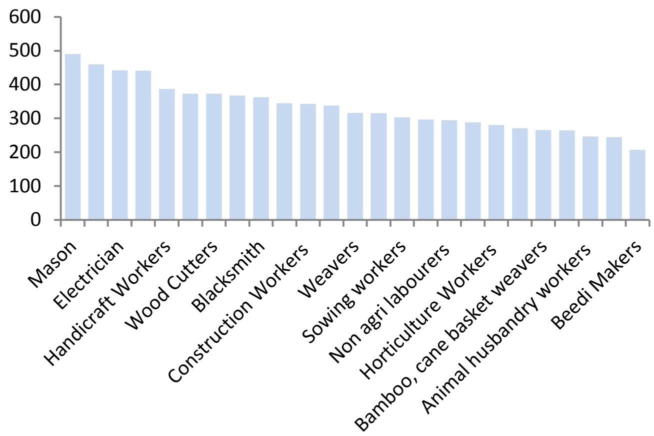
SSSG (%)	FY14	FY15	FY16	FY17	FY18	FY19	FY20E	FY21E	FY22E
ABFRL (Pantaloons)	-2%	5%	6%	5%	-2%	1%	6%	6%	5%
Brand Factory (FLFL)	8%	5%	8%	17%	16%	14%	0%	5%	8%
Central (FLFL)	12%	8%	7%	18%	10%	6%	6%	5%	7%
Big Bazaar (Future Retail)	6%	10%	12%	14%	13%	11%	6%	5%	NA
Shoppers stop	10%	5%	9%	3%	2%	4%	3%	5%	6%
Westside (Trent)	9%	11%	8%	9%	9%	9%	12%	10%	9%
V-Mart	12%	7%	-1%	15%	9%	4%	3%	6%	7%
D-Mart	26%	22%	22%	21%	14%	12%	12%	12%	12%
V2 Retail	13%	14%	6%	2%	-4%	5%	NA	NA	NA

Source: Companies, PhillipCapital Research

All-India wages – growth at its lowest level



All India wages by type of work as of Nov 2019

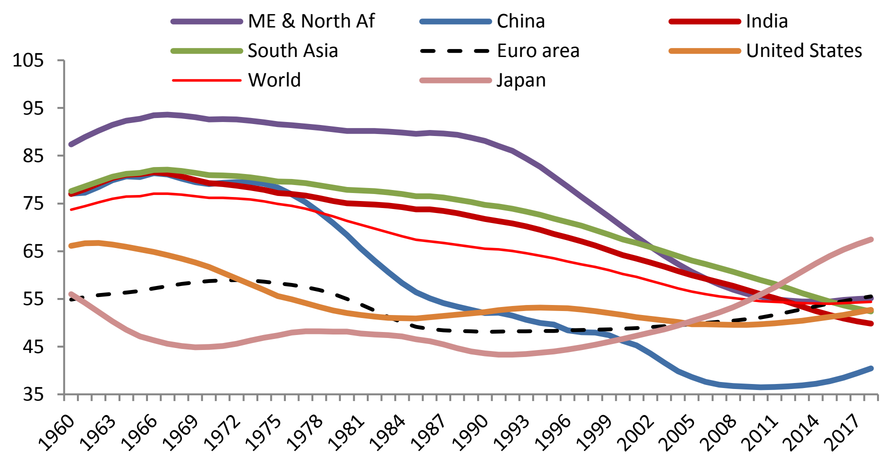


Source: RBI, PhillipCapital Research

Population size/demographic dividend bolsters growth in the face of headwinds

India's rising working age population/falling dependent population will continue to aid rapid growth and offer dividend to India's consumption story in the long-run. As can be seen from the chart below, India's dependency ratio is trending lower vs. rising trend of China and other developed countries.

Age dependency ratio – still declining for INDIA (% of working-age population)

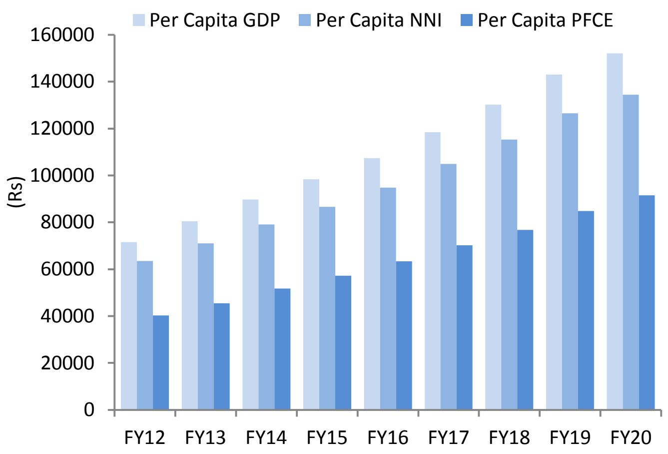


Source: UNDP, PhillipCapital Research

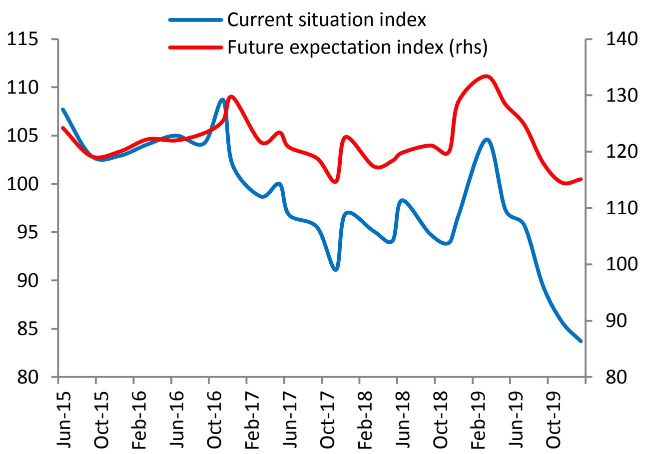
Per capita income/ Private final consumption expenditure (PFCE) – Expectedly dipped in FY20, should inch higher in FY21-22

- Average growth was subdued in FY20 for both constant and current prices – 5-9%. Per capita PFCE fared better, others were tepid.
- For FY20, India's per capita income stood at US$ 1,900 and consumption at US$ 1,300.
- India ranks third on GDP, based on PPP – it contributes 8% of the world GDP growth.
- However, consumer confidence has seen a SHARP drop in the last 8-months.

Per capita GDP, income, and consumption – trending higher

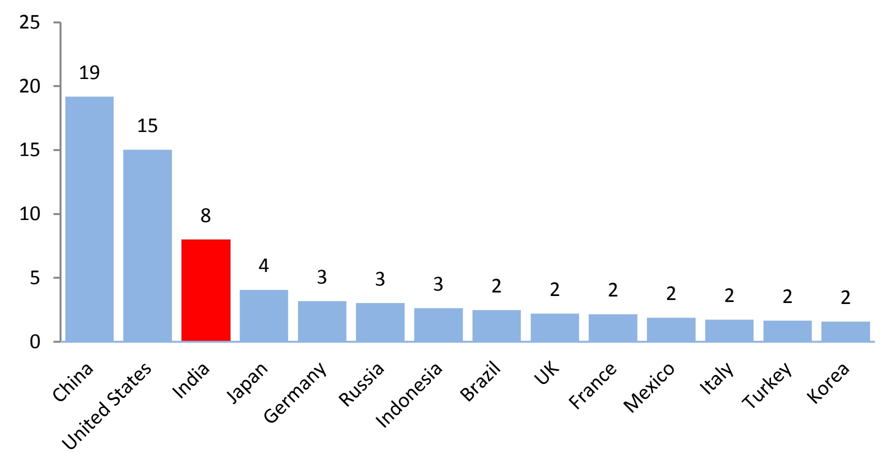


Consumer confidence index – trending lower since Q1FY20



Source: RBI, CSO, PhillipCapital India Research

% of world GDP (PPP basis) – India ranks third

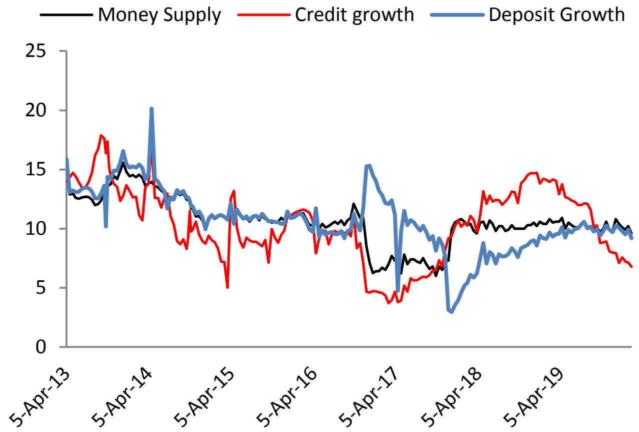


Source: IMF, PhillipCapital Research

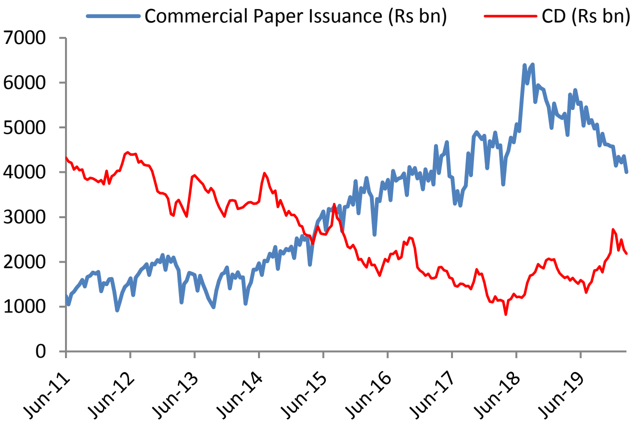
Credit to stay tepid in FY21 despite low cost of borrowing

- Credit and CIC growth remains significantly below usual trends. Deposit/M3 is marginally below trends. We do see second order adverse impact of the Yes bank collapse in terms of deposit and credit growth.
- Current prevalent credit/CIC/deposit/M3 yoy growth is at 7%/12%/9%/9.6%. For FY21-22, we expect growth to rise to 7-8%/12-13%/9-10%/9-10%.
- Retail and services credit will remain buoyant in FY21, while corporate credit should continue to be tepid amidst economic weakness.
- RBI has taken impressive measures to ensure better transmission of rates through banking channel as well as market rates. Lower borrowing cost is a positive to encourage lending, however, due to excess capacity/inventory and muted rise in incomes, we believe an uptick will be gradual.
- Liquidity will remain easy for productive credit channels.

M3, deposits - Stable; credit growth declined (YoY, %)

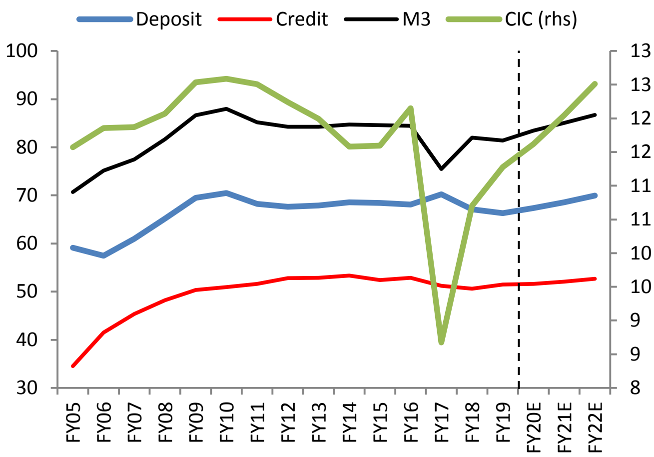


Slowdown in NBFCs led to drop in CP issuances, CDs faring well

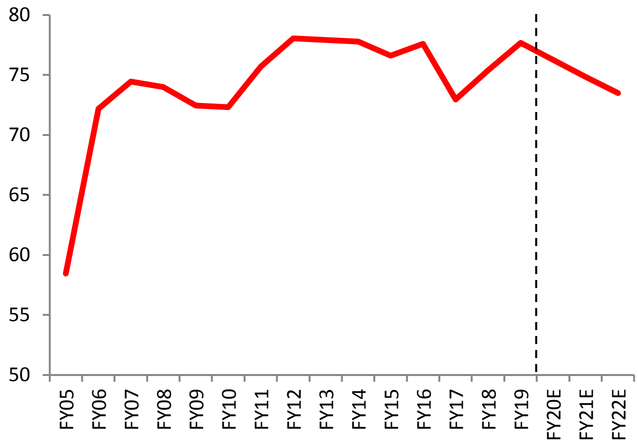


Source: RBI, Bloomberg, PhillipCapital Research

Banking parameters as % of nominal GDP – stable to marginally better trends



Credit/deposit ratio – likely to stay muted

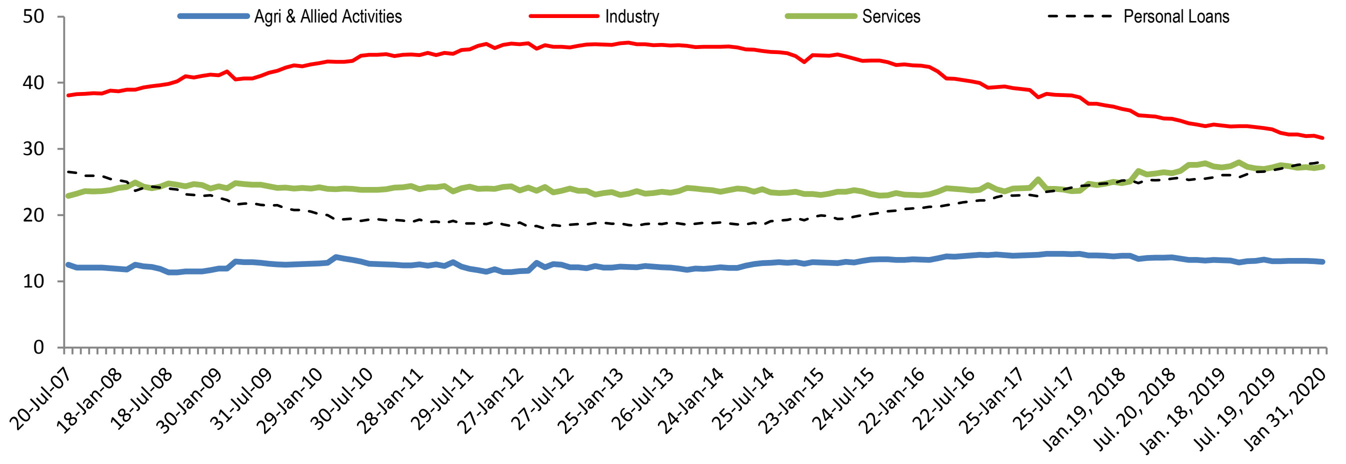


Source: RBI, Bloomberg, PhillipCapital Research

- **Agriculture sector credit:** Maintained trend growth rate due to priority sector norms, average growth of 7%.
- **Industrial credit:** Large industries fared relatively better than MSMEs, despite all the government and liquidity push. Overall credit remains tepid, FYTD growth at -2%. Share of industrial credit/total credit has shrunk to 32% from 45% in 2014. Share of micro/medium/large corporate credit share is at 4.2%/1.2%/26.3%.

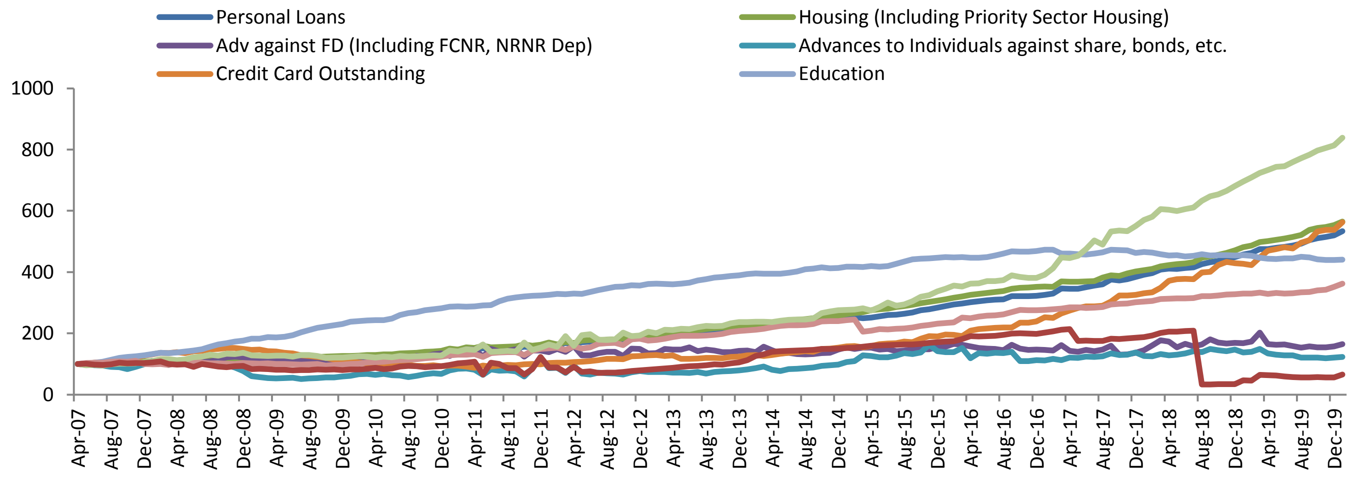
- Slowdown is evident across industries, FYTD credit has contracted for all the industries barring marginally higher outgo for construction, telecommunication, and rubber-plastic products. Highest contraction was seen in metals, engineering, textiles, gems & jewellery, food processing, and other infrastructure.
- **Services-sector credit:** Share of services credit was largely stable (27%); sharp rise was seen in the share of NBFC credit – at 8.3% vs. 7% a year ago. Credit offtake took place for commercial real estate as well.
- **Personal loans – the push factor:** Share at 28% vs. 26% a year ago, led by housing and other personal loans. 57% of the credit jump in personal loans came from housing (Rs 1,500bn); it was at Rs 887bn for personal loans. Slight increase in credit card share (at 1.2%, Rs 184bn FYTD addition) and vehicle loans (Rs 204bn FYTD addition). Housing lending picked up under the priority segment as well.

Bank credit break-up (% of total credit) – industry lower, services and personal loans trending higher, agriculture stable



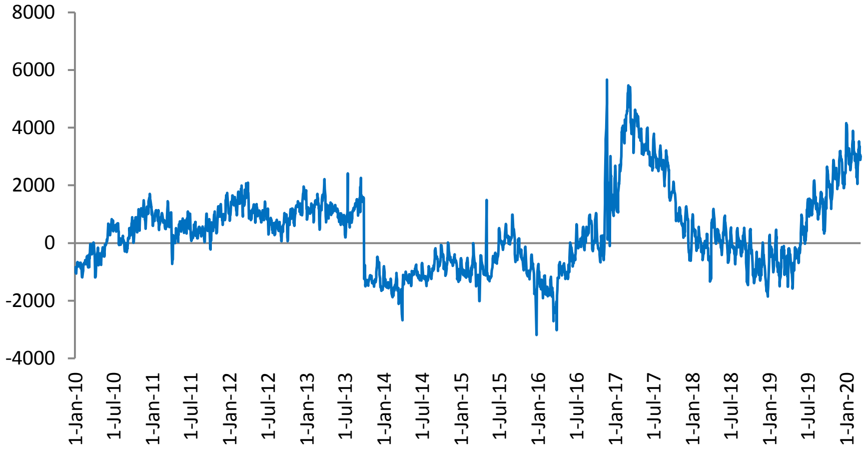
Source: RBI, PhillipCapital India Research

Retail credit growth trends (April 07 = 100)



Source: RBI, PhillipCapital India Research

LAF balances (Rs bn)

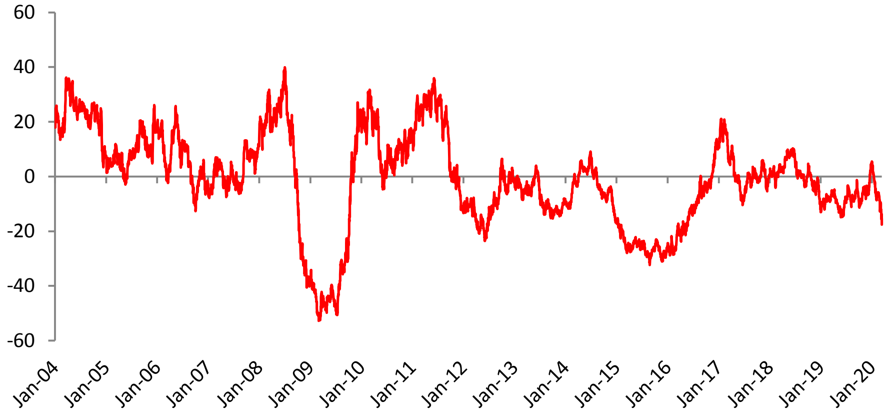


Source: RBI, PhillipCapital Research

Inflation/interest rates to soften in FY21-22

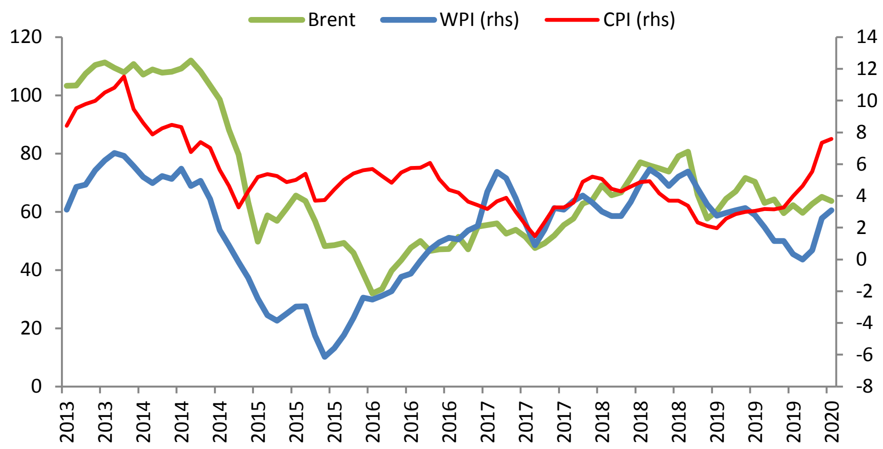
- Sharp, unanticipated crash in brent prices is a BIG positive for inflation. Even if government hikes excise duties, <u>reasonable benefits are likely in terms of lower inflation.</u> <u>Here we assume an average brent price of US$ 50 per barrel in FY21.</u>
- Inflation is expected to soften in FY21, 2H CPI trends will be supported by favourable base effect. We assume manageable food and non-food inflation – no spike across products.
  - After signs of settling down of US-China trade tensions, there was hope of better days ahead for the global economy. However, coronavirus has rattled this confidence. Because of this its uncertainty (extent and duration) we expect commodity prices to be muted at least in 1HFY21.
  - Domestically, food inflation unexpectedly surged in FY20, possibly supported by the government in order to help farmers' incomes. In case of a change in the government's policy on managing food inflation, upside risks exist.
  - Core inflation is likely to remain in check, under 3% owing to sharply lower fuel inflation.
  - Rising competition, muted demand, and excess capacity will support benign core inflation outlook.
- <u>**Average CPI inflation for FY21/22 should be 2.5-3.5% vs. 4.8% in FY20. Oil prices and food inflation are the key risk to our estimates.**</u>
- We believe that inflation has peaked out and will be trending lower. It will be higher until 1HFY21 and turn fairly benign in 2HFY21.
- <u>**Due to benign inflation expectation, sub-optimal economic growth, and financial market instability, we expect RBI to lower rates by 25-75bps anytime now and in FY21**</u>. RBI should continue to take measures to improve transmission and support growth.
- While fiscal pressures will worsen in FY21 due to weak economic conditions, bond yields are likely to remain benign. We see 10-year bond yield at 5.8-6.5% in FY21.

Bloomberg commodity index (yoy growth, %)



Source: CSO, Bloomberg, PhillipCapital Research

CPI, WPI, Brent (yoy growth, %)



Source: CSO, Bloomberg, PhillipCapital Research

Financial Sector

NBFCs caused breakdown; Banks gained/stabilize; Yes bank and Covid-19 to add to the problem

We have been of the view that the recent slowdown in the Indian economy was caused by liquidity tightness in the NBFC sector, the segment which was incrementally financing growth that banks wouldn't. Here, we look at the current health of the NBFC sector to gauge the scope of sectoral and economic financing recovery ahead.

- 3-year AAA-rated corporate bond yield has fallen to 6.8% from 9% in October 2018, 8% in Apr-May 2019.
- 3-year AA-rated corporate bond yield has fallen to 7.1% from 9.4% in Oct. 2018, 8.6-8.7% in Apr-May 2019.
- Bank credit to NBFCs has risen to Rs 7.3tn from Rs 5.5tn (in Oct. 2018).
- Banking liquidity has eased to Rs 2.5-3tn surplus from deficit of Rs 1tn in October 2018.
- For the NBFCs under our coverage, AUM growth is expected to remain healthy at 18% for FY21-22, similar to FY20. Excluding Bajaj Finance, it is estimated to grow by 12% vs. 9% in FY20.
- Disbursement growth for 5 NBFCs is expected at 9/12% in FY21/22 vs. 2%/7% in FY20/19. Incremental disbursement of Rs 133bn in FY21 and Rs 194bn in FY22 vs. Rs 23bn in FY20.
- **Disbursement break up:** Refinance/used vehicles forms the highest share at 40% (its share fell in Q3FY20), followed by CVs (at 23%), tractor/PVs/MSME (each at 7-7.5%), 2Ws at 6%, gold at 5%. In Q3FY20, a pick-up was seen in tractors, PVs, and 2Ws.
- **We like Shriram transport, Bajaj Finance (not rated), and HDFC ltd in this space.**

Banks: Weak macros a risk

- Credit growth expected to remain tepid in FY21.
- 'Loss of Confidence' due to the withdrawal limit imposed on Yes bank and PMC bank on banking deposits, is still unknown.
- The sore point that has been limiting the banks from lending, was rising NPAs eating into capital through higher provisioning. While our banking team expects NPAs to dip in FY21-22 (table below), however, due to likely adverse impact of Covid-19 as well as ripple effect of Yes bank collapse on economic activity, there are upside risks to these numbers.
- Capital adequacy ratio is sufficient (above the regulatory norm of 8%) across all private banks and most of public-sector banks.
- Lower lending rates is a positive for lending, however, may not push it higher due to lack of confidence of future growth prospects.

After the fallout of the Yes Bank, there will be consolidation in the private sector, in the lines of the public sector. This is expected to be grinding for banking activity. We expect ICICI bk, Axis bk, HDFC bk, Kotak bk, SBI, and HDFC to gain market share over the next few years, we remain positive on these names.

Bank-wise GNPA and NNPA trends and our expectations

	GNPA Ratio				NNPA Ratio			
	3Q20	FY20	FY21	FY22	3Q20	FY20	FY21	FY22
Axis	5.00%	4.70%	4.00%	3.30%	2.10%	1.90%	1.30%	1.10%
DCB	2.20%	2.20%	2.10%	2.00%	1.00%	1.00%	1.00%	0.90%
ICICI	6.00%	5.60%	4.40%	3.20%	1.50%	1.30%	1.10%	1.10%
IndusInd	2.20%	2.20%	1.90%	1.90%	1.10%	1.10%	1.00%	1.00%
HDFC	1.40%	1.60%	1.50%	1.40%	0.50%	0.40%	0.40%	0.50%
Kotak	2.50%	2.50%	2.40%	2.30%	0.90%	0.90%	0.80%	0.80%
BOB	10.40%	9.90%	8.20%	7.10%	4.10%	4.30%	3.90%	3.90%
Canara	8.30%	7.20%	5.40%		4.90%	4.30%	3.20%	
Indian	7.20%	6.70%	12.00%	11.10%	3.50%	3.10%	3.43%	3.10%
PNB	16.30%	14.20%	12.00%		7.20%	5.20%	3.90%	
SBI	6.90%	6.10%	5.10%	4.70%	2.70%	2.20%	1.70%	1.70%

Source: Companies, PhillipCapital India Research

Bank-wise capital availability trends

	CET 1(%)				Tier 1(%)				Total capital (%)			
	Mar-17	Mar-18	Mar-19	Q3FY20	Mar-17	Mar-18	Mar-19	Q3FY20	Mar-17	Mar-18	Mar-19	Q3FY20
Axis	11.1	11.7	11.3	14.3	11.9	13	12.5	15.5	15	16.6	15.5	18.7
ICICI	13.7	14.4	13.6	13.6	14.4	15.9	15.1	15	17.4	18.4	16.9	16.5
HDFC Bank	12.8	12.2	14.9	16.2	12.8	13.2	15.8	17.1	14.6	14.8	17.1	18.5
Kotak Bank	15.9	17.5	16.7	17.5	15.9	17.6	16.9	17.7	16.8	18.2	17.5	18.2
BOB	9	9.2	10.4	9.9	9.9	10.5	11.6	11.5	12.2	12.1	13.4	13.5
Canara	8.9	9.5	8.3	10.3	9.8	10.3	9	11.1	12.9	13.2	11.9	13.9
Indian Bank	11.8	11	11	12.8	12.2	11.3	11.3	13.1	13.6	12.6	13.2	15.0
PNB	7.9	6	6.2	10.6	8.9	7.1	7.5	11.9	11.7	9.2	9.7	14.0
SBI	9.8	9.4	9.6	10.2	10.4	10.1	10.7	11.6	13.1	12.9	12.7	13.7

Source: Companies, PhillipCapital India Research

Investments – Public capex, the saviour

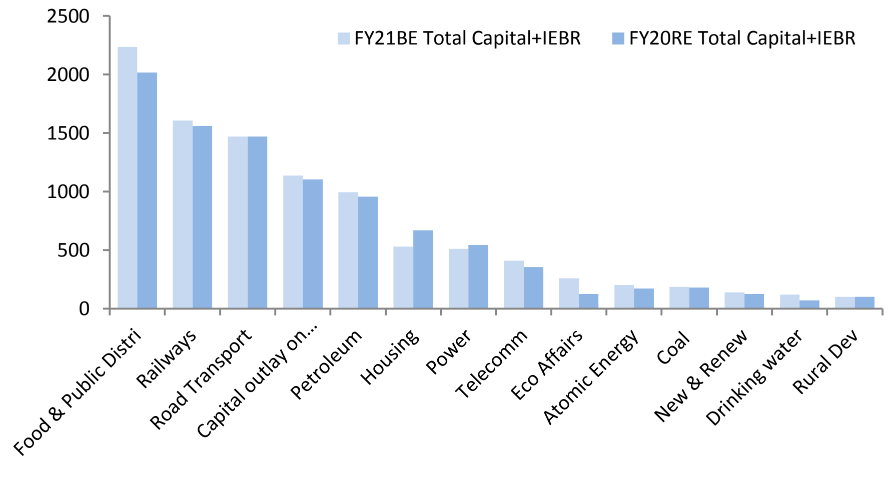
- GFCF saw its worse in FY20 due to weak demand, higher existing capacity, and high base last year. Slowdown became more prominent for the private sector, government capex fared well amidst fiscal stress.
- **As per RBI data, capacity utilization levels dropped to 69% in Q2FY21, lowest since data availability (Q3FY14). Q2GFCF growth was at 0.5% (lowest since FY15). This indicates excess available capacity in the system.**
- For FY21, we expect it to remain weak – slight improvement in private capex due to lower corporate tax rate for the new manufacturing units to be commissioned by March'23; public capex will remain buoyant assuming disinvestment plans are met and tax revenue fall is limited. We assume GCF to grow by 1-2% vs. -1.3%/0% in FY19/20.
- Currently, share of GCF/nominal GDP has fallen to 30%, lowest since FY05, peak rate was at 40% in FY11.
- Capital productivity declined – ICOR surged to 6 in FY20 from 4.8 in the last two years (also the aggregate historical levels).
- Considering the signs of economic weakness, we turn cautious on this sector. We recommend a combination of quality cement and capital goods companies trading at attractive valuations.
- **Our top picks are:** Ultratech, JK Cement, BEL, and L&T

Key capex indicators we looked at – uptick seen, may not sustain:

Government capex spend – The capex driver

Government keeping up with planned capex spend at a time of fiscal stress in the last few years reiterates its focus on infra development; we expect it to persist even going ahead. For FY21, the government capex is budgeted at Rs 4,121bn vs. Rs 3,489bn last year. **Adding IEBR, it amounts to Rs 10,847bn vs. Rs 10,595bn in FY20.**

Top ministry-wise capex + IEBR expenditure (Rs bn)



Source: Budget Document, PhillipCapital India Research

Companies' order book – Robust expectations for FY21-22, downside risk exists now

We analysed the order inflows and outstanding order books of infra and capital goods companies (8 + 16 = 24) to gauge the capex execution in coming years. Current analysis is based on the current analyst estimates, which we fear may be revised downward owing to economic weakness

- **Order inflows:** FY20 was an extremely weak year for infra ordering while the capital goods space trended higher (ahead of expectations). Total order inflows were largely stable at Rs 3.4tn in FY19-20. We expect it to rise to Rs 4.6tn in FY22 (average growth of 17% in the next two years).
- Infra companies recorded a sharp dip in FY20, which is expected to see an improvement in FY21-22. Dip was seen in roads segment, power, and water infra while building and metro construction remained stable; irrigation ticked higher.
- Order inflows are estimated to pick up for PNC Infra, IRB, Ashoka Buildcon, and Sadbhav Engineering.
- Roads order awarded by NHAI dipped to 2,222km in FY19.
- Within capital goods space, the defence sector is gaining momentum, infrastructure remains the largest sector followed by power; and railways is inching higher, but remains marginal.
- Order inflows are expected to see strong growth (30%+) for BHEL, BEL (base low for FY20), and KEC. L&T's order inflows growth is estimated at 7%/10% for FY21/22 vs. 10% average for the last three years.
- **Order book:** We expect order book for infra and capital goods companies to grow by 10-12% in FY21-22 vs. 7.4% in FY18-20. It is estimated to stand at Rs 8.6tn in FY22 vs. Rs 7tn in FY20.

Order inflows and order book for infra and capital-goods companies

Order Inflows (Rs Bn)	FY14	FY15	FY16	FY17	FY18	FY19	FY20E	FY21E	FY22E
Infra	215	204	243	300	493	514	174	460	525
Capital goods	2057	2392	2444	2445	2596	2916	3188	3562	4114
Total	**2272**	**2596**	**2687**	**2745**	**3089**	**3430**	**3362**	**4022**	**4639**
Growth rate (yoy, %)									
Infra		-4.9	19.2	23.2	64.6	4.2	-66.2	164.6	14.1
Capital goods		16.3	2.2	0.1	6.1	12.4	9.3	11.7	15.5
Total		**14.3**	**3.5**	**2.2**	**12.5**	**11.1**	**-2.0**	**19.6**	**15.3**

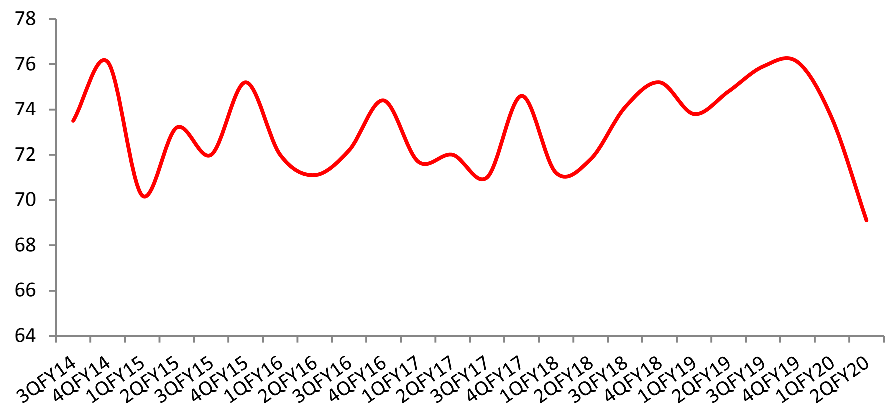
Order Book (Rs Bn)	FY14	FY15	FY16	FY17	FY18	FY19	FY20E	FY21E	FY22E
Infra	561	562	568	624	869	1112	886	969	1056
Capital goods	3914	4379	4725	4974	5058	5494	6035	6677	7511
Total	**4476**	**4940**	**5293**	**5598**	**5927**	**6606**	**6922**	**7646**	**8567**
Incremental		**465**	**353**	**305**	**329**	**679**	**316**	**724**	**921**
Growth rate (yoy, %)									
Infra		0.1	1.2	9.8	39.3	27.9	-20.3	9.4	8.9
Capital goods		11.9	7.9	5.3	1.7	8.6	9.9	10.6	12.5
Total		**10.4**	**7.1**	**5.8**	**5.9**	**11.5**	**4.8**	**10.5**	**12.0**

Source: Companies, PhillipCapital India Research

Capacity utilisation fairly low

- As on Q2FY20, capacity utilisation has declined to multi-year low of 69% vs. last 4-year average of 73%.
- In general, industries in India are sitting on excess capacity. With likelihood of only a gradual demand improvement, we don't expect a surge in capacity utilization levels in FY21 as well.

Capacity utilisation rates at its lowest level (%)



Source: RBI, PhillipCapital India Research

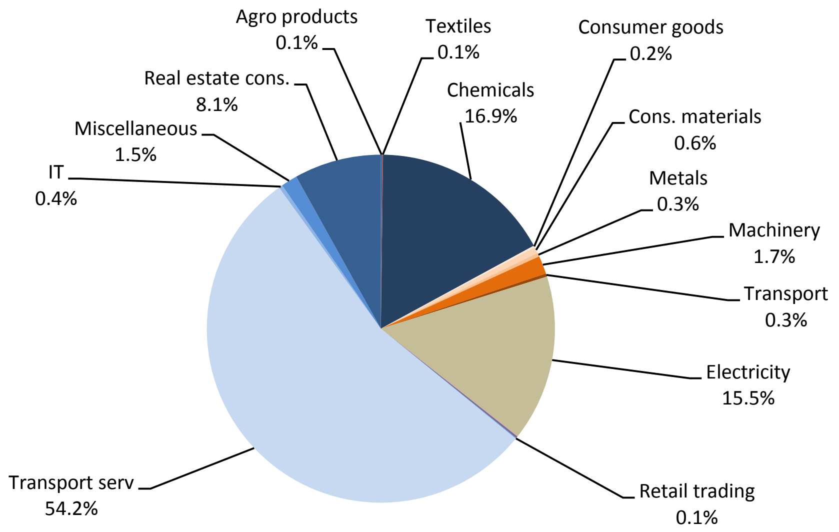
CMIE – Improvement in Dec. 2019 quarter, may fizzle out

- For Oct-Dec 2019, new (highest in 6 quarters) and completed (3-quarter high) projects paced higher.
- 'Completed projects' were primarily led by metals (JSPL), followed by construction and real-estate services (Aamby valley), and construction materials industry (Dalmia Bharat). Transport services remained strong for the last few quarters (NHAI).
- Projects under implementation have stayed strong for the second consecutive quarter. Projects outstanding have also seen improvement (at a 3-quarter high).
- Projects stalled and shelved remained elevated – highest in transport services (Uttarakhand Metro Rail, Mumbai Suburban Corridor Project) and electricity (NTPC's wind-power project).

Current sector trends (based on new projects):

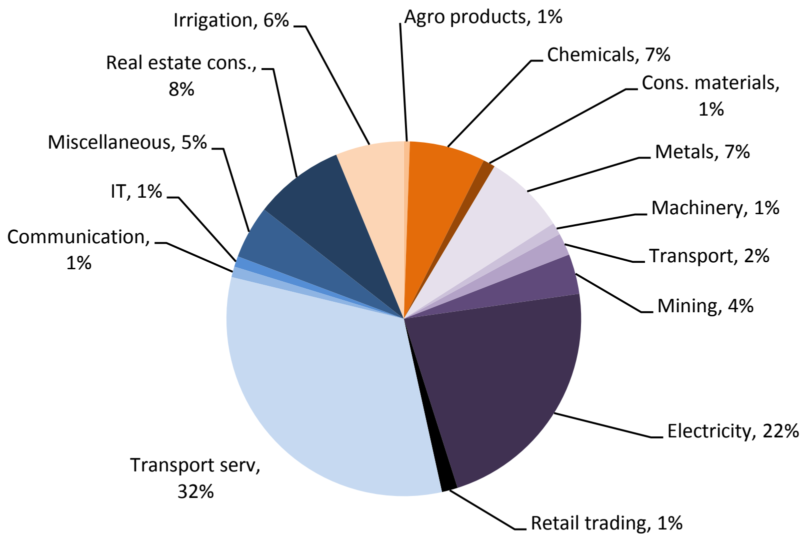
- **Strong:** Transport services (53% of total, led by InterGlobe Aviation), chemicals (17%, Reliance Industries' Jamnagar refinery), electricity (15%, solar power project of the Andhra Pradesh government), and construction & real estate (8%, commercial complex for defence at Lucknow).
- **Seeing improvement:** machinery (2%), construction materials (1%), and mining (1%).
- **Weaker ones:** Textiles, transport equipment, IT, and irrigation.

Break-up of New projects (Industry-wise)



Source: CMIE, PhillipCapital India Research

Break-up of Outstanding projects (Industry-wise)

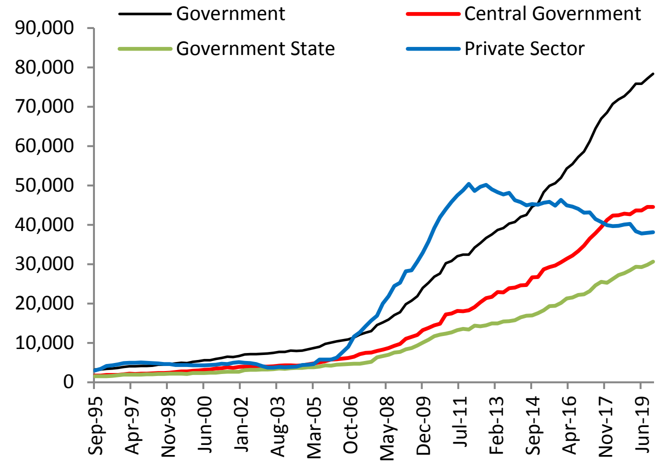


Source: CMIE, PhillipCapital India Research

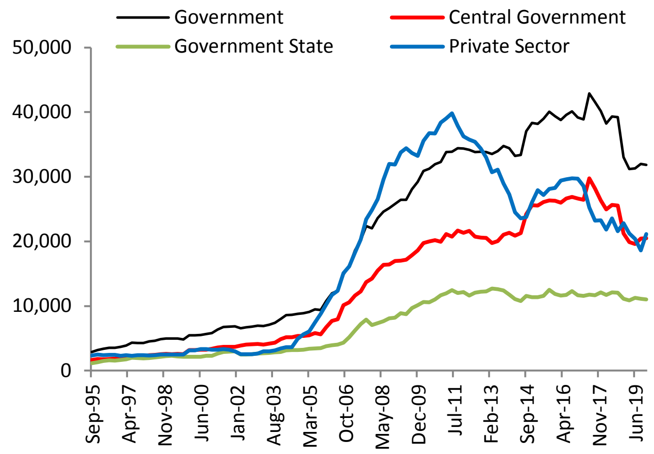
Private-sector remains weak, but gaining traction; central government incrementally weaker

- The private sector is seen pacing higher in terms of new projects, led by aviation, refinery, and solar power; rest of the segment participation remains weak.
- Government-sector projects are seen dipping across segments (except under-implementation and outstanding), notably in new projects, and after a pronounced pick-up in 'projects announced' a couple of quarters ago.
- State governments are seen faring better than the central government.

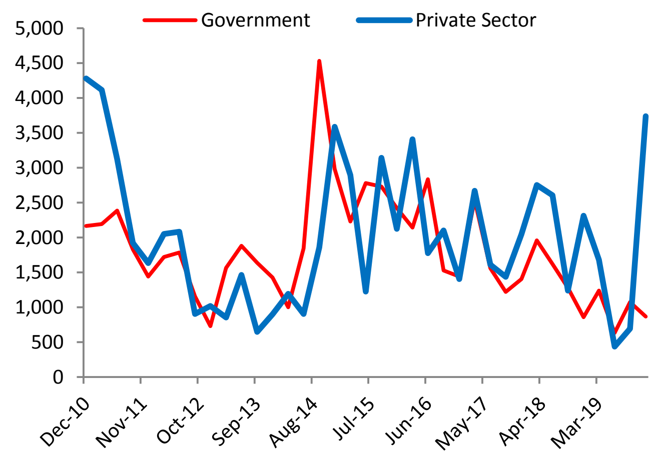
Government and private sector share (projects under implementation)



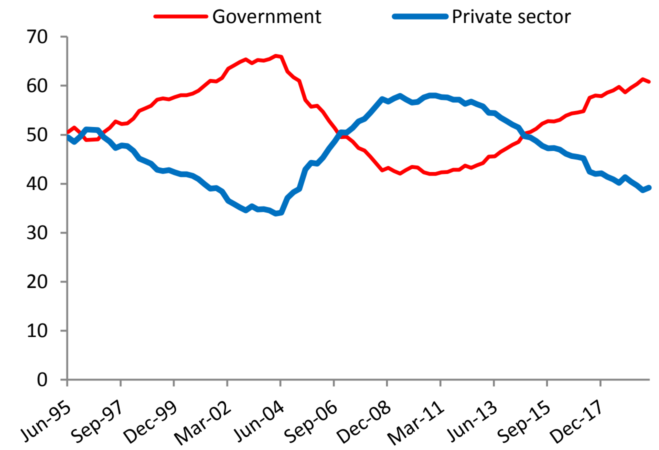
Government and private sector share (projects announced)



Private and government sector share (new projects)



Share of government and private sector (outstanding projects)



Source: CMIE, PhillipCapital India Research

New project announced: Sector-wise summary

(Rs bn)	FY16	FY17	FY18	FY19	9MFY20
Conventional power	1,577	551	482	429	506
Renewable power	1,487	1,123	2,194	1,624	906
Power gen	3,064	1,674	2,676	2,053	1,413
Power T&D	351	206	152	223	11
Power	**3,415**	**1,880**	**2,828**	**2,276**	**1,424**
Coal & lignite	**61**	**72**	**31**	**17**	**8**
Crude oil & natural gas	75	97	697	65	1
Petroleum products	1,787	887	471	1,526	709
Natural gas distribution	213	58	87	138	17
Oil & gas	**2,075**	**1,042**	**1,255**	**1,730**	**726**
Roads	2,726	3,320	2,127	1,160	148
Railways	2,625	1,881	1,011	321	313
Airport Infra	144	192	175	116	2
Ports	964	602	82	56	42
Water & irrigation	615	1,224	569	513	87
Infrastructure	**7,074**	**7,219**	**3,964**	**2,166**	**593**
Housing construction	835	762	675	658	210
Commercial complexes	207	348	273	257	372
Real estate	**1,042**	**1,110**	**949**	**915**	**582**
Hotels, hospitals, education etc	**1,291**	**516**	**518**	**468**	**203**
Metals	**633**	**1,363**	**491**	**708**	**182**
Cement	**155**	**316**	**195**	**279**	**123**
Electronics	**1,347**	**82**	**173**	**203**	**76**
Chemicals	**820**	**311**	**525**	**830**	**109**
Auto	309	204	250	165	17
F&B	**322**	**345**	**198**	**171**	**57**
Textiles	120	178	204	74	25
Pharma	62	60	125	52	23
Fertilisers	176	222	0	2	-
Telecom	38	582	44	2	10
IT	148	141	33	158	45
Others	1,418	577	1,187	557	258
Total ex-Air transport	**20,504**	**16,221**	**12,970**	**10,772**	**4,463**
Air transport services	577	1,249	345	1,528	2,343
Total	**21,082**	**17,470**	**13,314**	**12,300**	**6,806**

Source: CMIE, PhillipCapital India Research

RBI's industrial outlook at multi-year lows

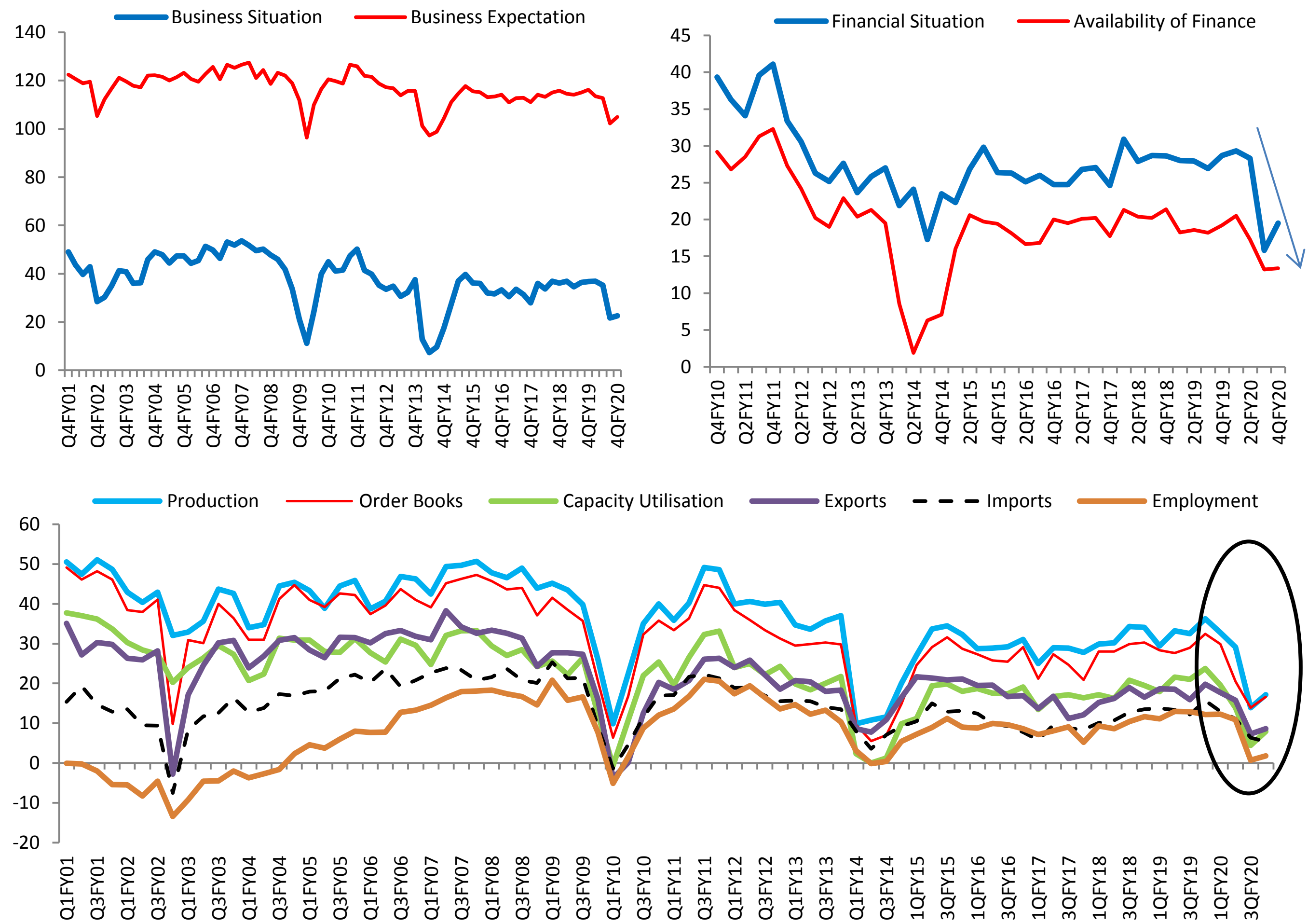
The RBI's Industrial Outlook Survey expects marginal improvement vs. Q3FY20 from participants across industrial variables in Q4FY20

RBI's industrial outlook survey: Responses for Q3FY20 (actual) and Q4FY20

	Q4FY20E	Q3FY20A
Production	Picked up, after Q3FY20 low	Turned positive vs. Q2FY20
Order books	Picked up, after Q3FY20 low	Turned positive vs. Q2FY20
Pending orders	Highest since FY14	Highest since FY10
Capacity utilisation	Slight improvement vs. Q3FY20	Negative since Q2FY20
Exports	Marginal uptick vs. Q3FY20	Turned negative
Imports	Lowest since FY14	Lowest since FY10
Employment	Weakest level since FY14	Lowest since FY10
Financial situation	Picked up after Q3FY20	Turned positive vs. Q2FY20, dismal vs. elevated levels of last 2 years.
Availability of finance	Dipped to 5 year low	Weakest since FY10
Business situation	Weakest since FY14	Turned positive vs. Q2FY20
Business expectations	Marginal uptick vs. Q3FY20	Weakest level since FY09

Source: RBI, PhillipCapital India Research

RBI's industrial outlook survey

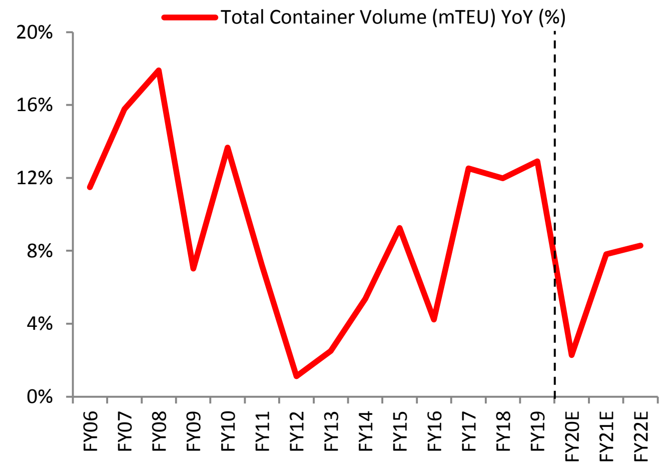


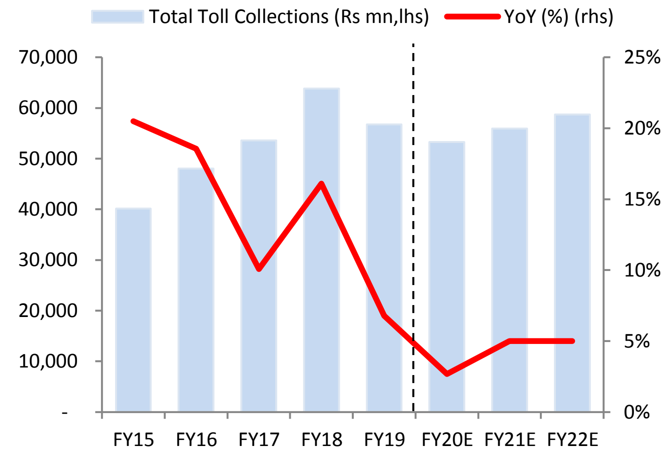
Source: RBI, PhillipCapital India Research

Ports and toll data – Marginal improvement seen ahead

- While we expected **container volume growth** to improve in FY20, it has remained tepid, growing 2% from the highs of 13% in FY19. Growth is expected to pick up from FY21-22 at 8%. Activity at the ports will be affected by Covid-19 at least till Q1FY21.
- FY17-21 average volume growth will advance to 10% vs. 4% in the earlier five years.
- Overall, **port volume (all commodities)** is expected to be tepid at 2% in FY20, to improve to 5% in FY21-22.
- **Railway volumes** will improve to 5% in FY21 vs. 0% in FY20.
- **Toll collections** are estimated to grow by 5% in FY21-22 vs. 3% in FY20.

Total container volumes and toll collection



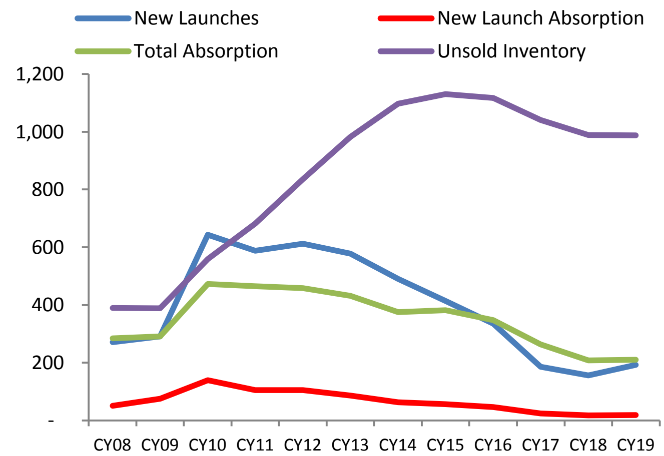


Source: Companies, PhillipCapital Research

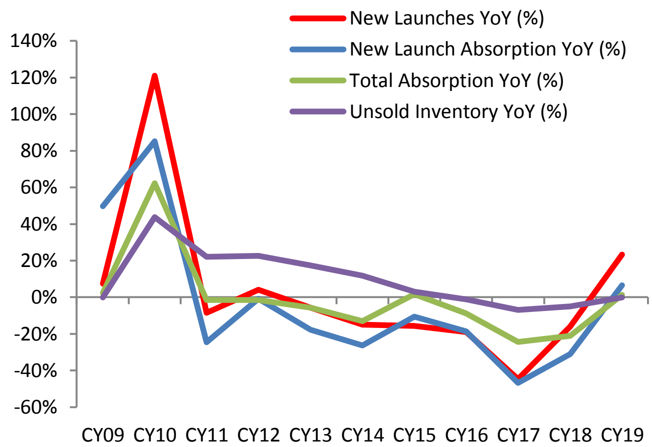
Real estate: Bottomed out, but Still not out of the woods

- For the industry as a whole, unsold inventory, while lower than the peak, still remains elevated as on 2019.
- New launches picked up in 2019.
- Within the sector, listed space is faring better. 2HFY20 sales are better than 1H, further improvisation expected in FY21-22.

Real estate unit-wise data (msf)



Real estate unit-wise data (yoy growth)



Source: Knight Frank, Liases Foras, PhillipCapital India Research

Real estate sales – FY20 will be similar to FY19

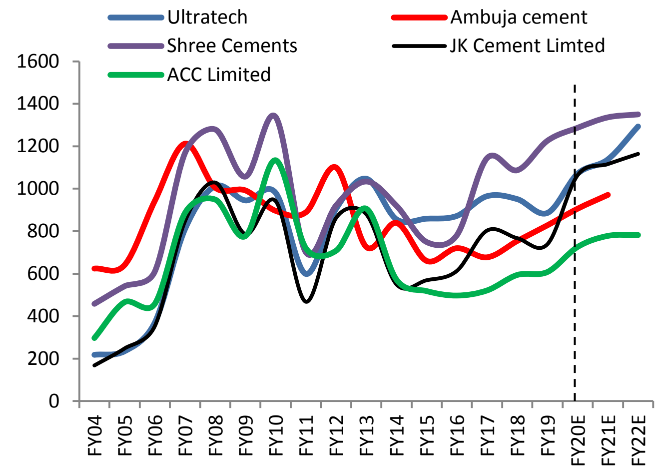
Sales in Sq. ft	FY14	FY15	FY16	FY17	FY18	FY19	FY20 FYTD
Sobha	3585185	3279004	3383723	3001829	3625390	4006585	3165993
GPL	2960000	3880000	4321000	3110000	6260000	8790000	5190000
Oberoi Realty	278964	1034392	1309262	566113	554069	732922	481829
Total	**6824149**	**8193396**	**9013985**	**6677942**	**10439459**	**13529507**	**8837822**
yoy growth (%)							
Sobha sales in sq. ft.		-9%	3%	-11%	21%	11%	
GPL in sq. ft.		31%	11%	-28%	101%	40%	
Oberoi Realty in sq. ft.		271%	27%	-57%	-2%	32%	
Total		**20%**	**10%**	**-26%**	**56%**	**30%**	

Source: Companies, PhillipCapital India Research

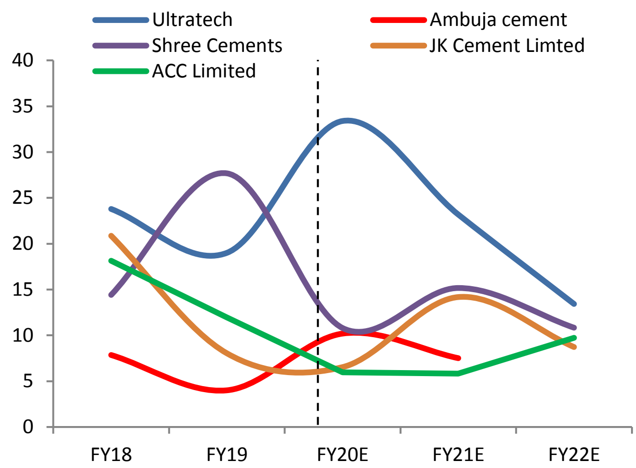
Cement: Relying on realizations

- Volume growth is expected to be muted in FY21-22, but we expect realizations to continue improving in the coming years (chart below). Lower crude prices (if they sustain) will be a positive for margins.
- We prefer to play infra investment through Cement; we like Ultratech and JK cement in this space.

Company-wise EBITDA/tonne (Rs)



Company-wise Net sales (YoY growth, %)



Source: Companies, PhillipCapital Research

Government spending – To remain buoyant; will stay a growth facilitator

Government spending will remain strong in coming years – a build-up on its rising pace over the last few years.

- We estimate FY20/21 GFCE growth at 8.5% vs. 6.5% in FY19.
- In FY20, revenue spending will rise more than budgeted while capex spend will be lower that the upwardly revised budgeted numbers.
- However, government capital expenditure should fare well in FY21.
- Focus will persist on agriculture, irrigation, rural development, housing, roads, railways, metros.
- Defence spending will take precedence in coming years.

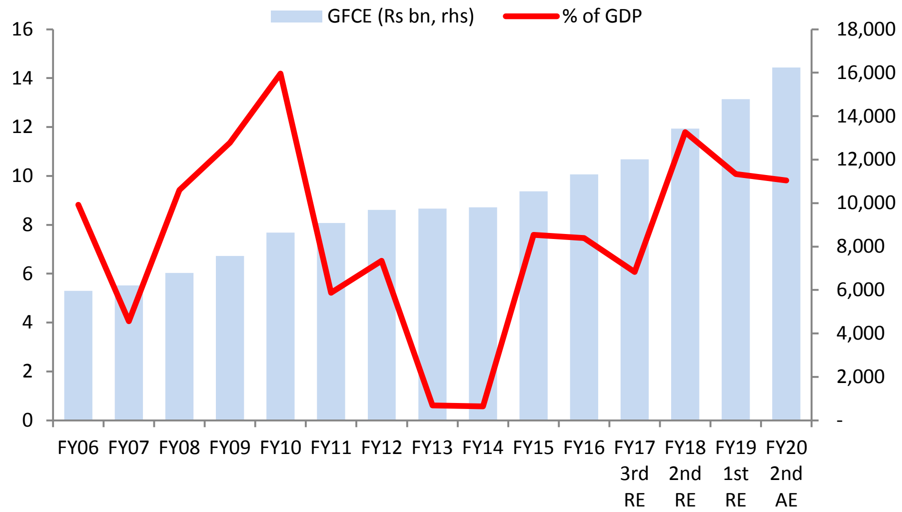
Additional government spending in FY21 is at Rs 3,437bn vs. Rs 3834bn in FY20, total at Rs 30,422bn. Its break-up: Interest (24%), transfer to states/IT & telecom (13% each), union territories (11%), agriculture (10%), pension (8%), finance/tax administration (5% each), transport (3%), urban development/food subsidy/defence/social welfare (2% each), education/health/petroleum subsidy/scientific departments (1% each), and rural development (0.4%).

Key ministry-wise total expenditure (including IEBR)

Rs Bn	FY19				FY20				FY21 BE				% of Total
Ministry/ Department	Revenue	Capital	IEBR	Total	Revenue	Capital	IEBR	Total	Revenue	Capital	IEBR	Total	FY21BE
Interest Payments	5826	0		5826	6251	0		6251	7082	0		7082	23.3
Defence Services (Revenue)	1956	0		1956	2059	0		2059	2093	0		2093	6.9
Transfers to States	1097	94		1191	1484	70		1554	1910	95		2004	6.6
Revenue	549	0	0	549	1220	0	0	1221	1365	1	0	1366	4.5
Agriculture, Cooperation and Farmers' Welfare	461	0		461	1019	0		1019	1343	1		1344	4.4
Defence Pensions	1018	0		1018	1178	0		1178	1338	0		1338	4.4
Food and Public Distribution	1062	9	1650	1071	1140	13	2005	1152	1210	12	2223	1222	4.0
Rural Development	1118	0	107	1118	1226	1	100	1226	1200	1	100	1201	3.9
Capital Outlay on Defence Services	0	952		952	0	1104		1104	0	1137		1137	3.7
Police	822	95		917	935	97		1032	954	98		1052	3.5
Road Transport and Highways	97	676	612	773	109	722	750	830	98	820	650	918	3.0
Railways	21	528	805	549	21	678	882	700	22	700	908	722	2.4
Fertilisers	706	0	7	706	800	0	29	800	713	0	5	713	2.3
Telecommunications	185	21	88	206	184	49	306	234	408	257	152	664	2.2
Health and Family Welfare	506	24	0	530	608	18	27	627	639	11	30	650	2.1
Pensions	447	0		447	506	0		506	612	0		612	2.0
School Education and Literacy	484	0		484	565	0		565	598	0		598	2.0
Housing and Urban Affairs	248	158	334	406	231	192	477	423	289	211	319	500	1.6
Petroleum and Natural Gas	305	19	1003	324	423	6	950	429	420	9	985	429	1.4
Higher Education	296	23	0	319	362	21	10	383	372	22	30	395	1.3
Jammu & Kashmir	0	0			0	0			308	0		308	1.0
Women and Child Development	230	0		230	262	0		262	300	0		300	1.0
Economic Affairs	22	62		84	33	126		160	33	260		293	1.0
Drinking Water and Sanitation	184	0	87	184	184	0	70	184	215	0	120	215	0.7
Atomic Energy	87	87	73	174	94	81	90	174	89	93	109	182	0.6
External Affairs	146	9		155	162	11		174	160	13		173	0.6
Power	135	20	740	156	141	18	524	159	148	11	499	159	0.5
Posts	140	8	0	148	117	7	0	124	144	11	0	155	0.5
Defence (Misc.)	63	46	6	109	97	50	6	147	97	48	6	145	0.5

Source: Budget document, PhillipCapital India Research

Government final consumption expenditure



Source: RBI, CSO, PhillipCapital India Research

Fiscal deficit: More linked to growth than yields

Weak economic activity will hamper tax collections and risk fiscal deficit for FY21. Recent capex spend is disappointing, particularly after government revised the targets higher for FY20 during the budget planning. Government will be required to spend Rs 810bn in Feb-Mar 2020 to achieve the budgeted capex targets. Other risks for FY21 – disinvestment targets, AGR payment schedule. Fiscal slippage will be managed by expenditure reduction; we see no risk of higher government borrowing, thus no impact on the bond yields. Lower spending by the government will be contra-growth for FY21 as it was in FY19-20. Lower brent prices will benefit government by way of higher revenues in case excise duties are raised.

Central government fiscal account

	Rs Bn				% of GDP				yoy growth (%)			
	FY19A	FY20BE	FY20RE	FY21BE	FY19A	FY20BE	FY20RE	FY21BE	FY19A	FY20BE	FY20RE	FY21BE
Nominal GDP	**189712**	**211006**	**204422**	**224894**					**11.0%**	**11.2%**	**7.8%**	**10.0%**
Revenue receipts	**15529**	**19628**	**18501**	**20209**	**8.2%**	**9.3%**	**9.1%**	**9.0%**	**8.2%**	**26.4%**	**19.1%**	**9.2%**
Tax (net)	13172	16496	15046	16359	6.9%	7.8%	7.4%	7.3%	6.0%	25.2%	14.2%	8.7%
Non – tax	2357	3132	3455	3850	1.2%	1.5%	1.7%	1.7%	22.3%	32.9%	46.6%	11.4%
Capital receipts	**7622**	**8236**	**8485**	**10213**	**4.0%**	**3.9%**	**4.2%**	**4.5%**	**7.8%**	**8.1%**	**11.3%**	**20.4%**
Recovery of loans	181	148	166	150	0.1%	0.1%	0.1%	0.1%	15.5%	-17.9%	-8.0%	-9.9%
Other reciepts (mainly PSU disinvestment)	947	1050	650	2100	0.5%	0.5%	0.3%	0.9%	-5.3%	10.8%	-31.4%	223.1%
Borrowings and other liabilities	6494	7038	7668	7963	3.4%	3.3%	3.8%	3.5%	9.9%	8.4%	18.1%	3.8%
Total receipts	**23151**	**27863**	**26986**	**30422**	**12.2%**	**13.2%**	**13.2%**	**13.5%**	**8.1%**	**20.4%**	**16.6%**	**12.7%**
Total revenue expenditure	**20074**	**24478**	**23496**	**26301**	**10.6%**	**11.6%**	**11.5%**	**11.7%**	**6.8%**	**21.9%**	**17.0%**	**11.9%**
Total capital expenditure	**3077**	**3386**	**3489**	**4121**	**1.6%**	**1.6%**	**1.7%**	**1.8%**	**16.9%**	**10.0%**	**13.4%**	**18.1%**
Total expenditure	**23151**	**27863**	**26986**	**30422**	**12.2%**	**13.2%**	**13.2%**	**13.5%**	**8.1%**	**20.4%**	**16.6%**	**12.7%**
Fiscal deficit	**6494**	**7038**	**7668**	**7963**	**3.4%**	**3.3%**	**3.8%**	**3.5%**	**9.9%**	**8.4%**	**18.1%**	**3.8%**
Revenue deficit	**4545**	**4850**	**4995**	**6092**	**2.4%**	**2.3%**	**2.4%**	**2.7%**	**2.5%**	**6.7%**	**9.9%**	**22.0%**
Effective Revenue deficit	2627	2777	3078	4027	1.4%	1.3%	1.5%	1.8%	4.0%	5.7%	17.2%	30.8%
Primary deficit	668	433	1417	881	0.4%	0.2%	0.7%	0.4%	7.5%	-35.2%	112.3%	-37.8%
Gross Market Borrowing	5710	7100	7100	7800	3.0%	3.4%	3.5%	3.5%	-2.9%	24.3%	24.3%	9.9%
Net Market Borrowing	4227	4731	4740	5449	2.2%	2.2%	2.3%	2.4%	-6.2%	11.9%	12.1%	15.0%

Source: Budget Document, PhillipCapital India Research

Non-tax, capital receipts, and subsidies break-up

Rs Bn	FY16	FY17	FY18	FY19A	FY20BE	FY20RE	FY21BE
Disinvestment	421	400	1000	947	1050	650	2100
Telecom	565	787	321	408	505	590	1330
Dividends	1121	1230	914	1134	1635	1999	1554
Public Enterprises	306	519	465	431	575	483	657
RBI	815	712	449	704	1060	1516	896
Subsidies	**2640**	**2348**	**2244**	**2229**	**3382**	**2636**	**2621**
Food	1394	1102	1003	1013	1842	1087	1156
Fertilisers	724	663	664	706	800	800	713
Petroleum	299	275	245	248	375	386	409
Interest subsidies			221	200	261	259	282
Others	222	308	111	62	103	104	61

Source: RBI, PhillipCapital India Research

Gross tax components

	Rs Bn				YoY Growth				% of GDP			
	FY19A	FY20BE	FY20RE	FY21BE	FY19A	FY20BE	FY20RE	FY21BE	FY19A	FY20BE	FY20RE	FY21BE
Gross Tax Revenue	**20805**	**24612**	**21634**	**24230**	**8.4%**	**18.3%**	**4.0%**	**12.0%**	**11.0%**	**11.7%**	**10.6%**	**10.8%**
Direct Tax	11366	13350	11700	13190	13.4%	17.5%	2.9%	12.7%	6.0%	6.3%	5.7%	5.9%
Personal Income Tax	4730	5690	5595	6380	9.8%	20.3%	18.3%	14.0%	2.5%	2.7%	2.7%	2.8%
Corporation Tax	6636	7660	6105	6810	16.2%	15.4%	-8.0%	11.5%	3.5%	3.6%	3.0%	3.0%
Indirect tax	**9439**	**11262**	**9934**	**11040**	**2.9%**	**19.3%**	**5.2%**	**11.1%**	**5.0%**	**5.3%**	**4.9%**	**4.9%**
GST	5816	6633	6123	6905	31.4%	14.0%	5.3%	12.8%	3.1%	3.1%	3.0%	3.1%
Excise Duty	2320	3000	2480	2670	-10.6%	29.3%	6.9%	7.7%	1.2%	1.4%	1.2%	1.2%
Customs Duty	1178	1559	1250	1380	-8.7%	32.3%	6.1%	10.4%	0.6%	0.7%	0.6%	0.6%
Service Tax	69	0	12	10	-91.5%	-100.0%	-82.6%	-15.0%	0.0%	0.0%	0.0%	0.0%

Source: RBI, PhillipCapital India Research

FY21 key fiscal parameters

- Revenue/capital expenditure growth at 12%/18% for FY21.
- Tax-GDP ratio is estimated to rise to 10.8% vs. 10.6% in FY20RE and 11.7% in FY20BE.
- Gross market borrowing at Rs 7,800bn vs. Rs 7,100bn in FY20RE.
- Net market borrowing to rise by Rs 700bn; at Rs 5,449bn vs. Rs 4,740 in FY20RE.
- States' share in tax is estimated to be higher at 32.4% vs. 30.3% in FY20RE; pay-out in FY20 was significantly (by Rs 1,531bn) lower than initially budgeted.

Where will money be spent in FY21? Additional government spending in FY21 is at Rs 3,437bn. Its break-up: Interest (24%), transfer to states/IT and telecom (13%), union territories (11%), agriculture (10%), pension (8%), finance/tax administration (5%), transport (3%), urban development/food subsidy/defence/social welfare (2%), education/health/petroleum subsidy/scientific departments (1%), rural development (0.4%).

Where is the FY21 money coming from? Additional tax/non-tax revenue in FY21 is estimated at Rs 3,437bn. Its break-up: core income tax (40%), CGST (39%), core corporate tax (36%), dividend from PSUs (10%), GST compensation cess (7%), income & corporate surcharge (4%), corporate health & education cess (2%), cess on crude oil and social welfare surcharge (1%).

Are the estimates realistic? Tax revenue could slip, disinvestment targets are optimistic, slight fiscal slippage is more likely.

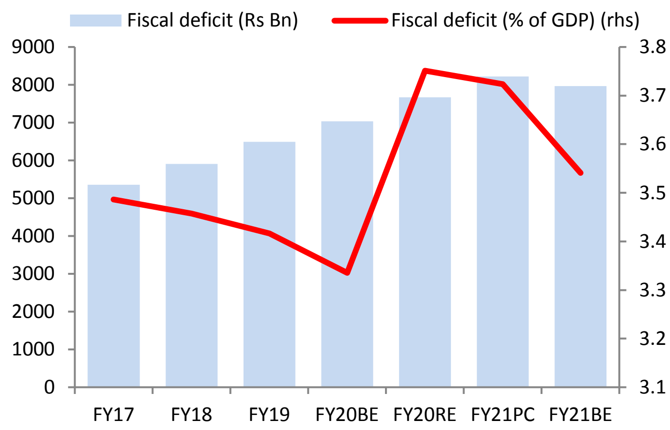
Major government schemes

Up: PMGSY (Rs 54bn), construction of new lines (Rs 41bn), AMRUT (Rs 39bn), development services (Rs 36bn), Green Revolution (Rs 34bn), interest subsidy for credit to farmers (Rs 33bn), Pradhan Mantri Krishi Sinchai Yojana (Rs 32bn), Swachh Bharat Mission (Rs 27bn), PMAY (Rs 22bn), Crop Insurance Scheme (Rs 21bn), National Rural Drinking Water Mission / National Education Mission (Rs 15bn), Mid-day Meal (Rs 11bn), National Ganga Plan / Gram Jyoti Yojna (Rs 4bn), National Livelihood Mission – Ajeevika / Price Stabilization Fund (Rs 2bn).

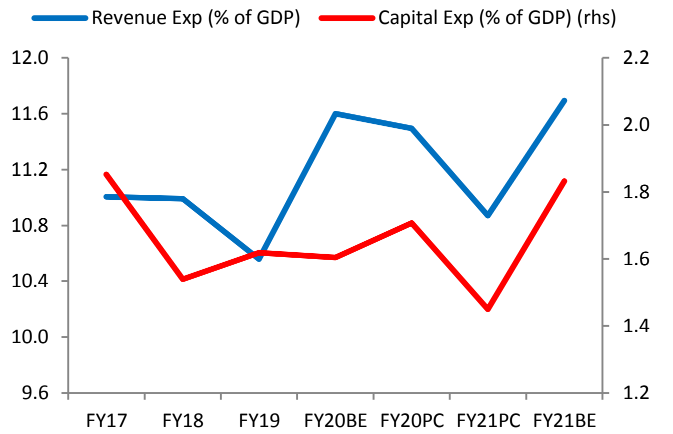
Down: MNREGA (Rs 95bn), LPG to poor households (Rs 26bn), modernization of police forces (Rs 10bn), Interest Equalization Scheme (Rs 6bn), Credit Support Program (Rs 5bn), jobs and skill development / Integrated Power Development Scheme (Rs 4bn), police infrastructure (Rs 3bn), and National Health Mission (Rs 2bn),

Unchanged: PMEGP, interest subsidy for guarantee funds, and National Social Assistance Program.

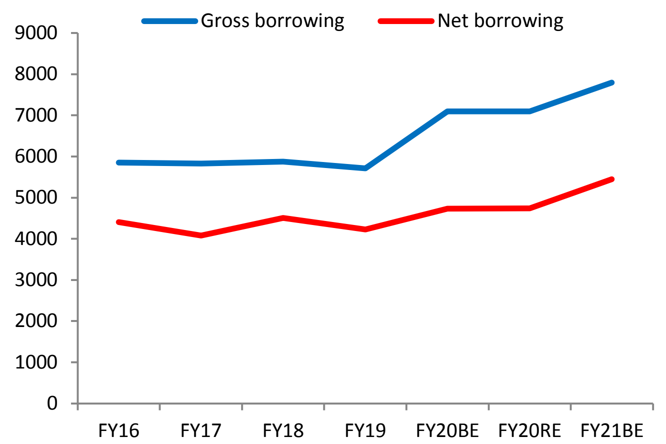
Central government fiscal deficit



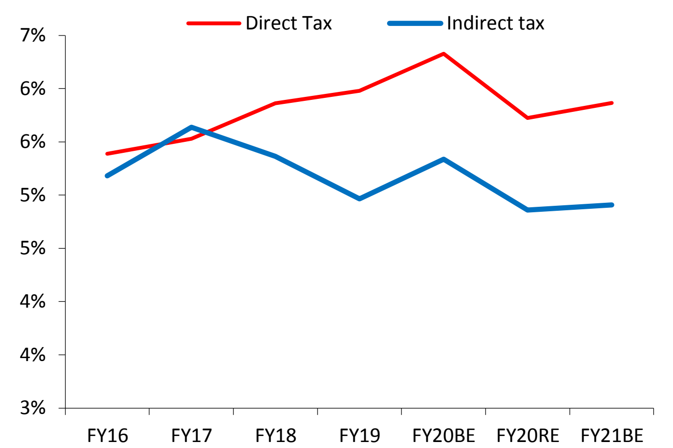
Revenue and capital expenditure (% of GDP)



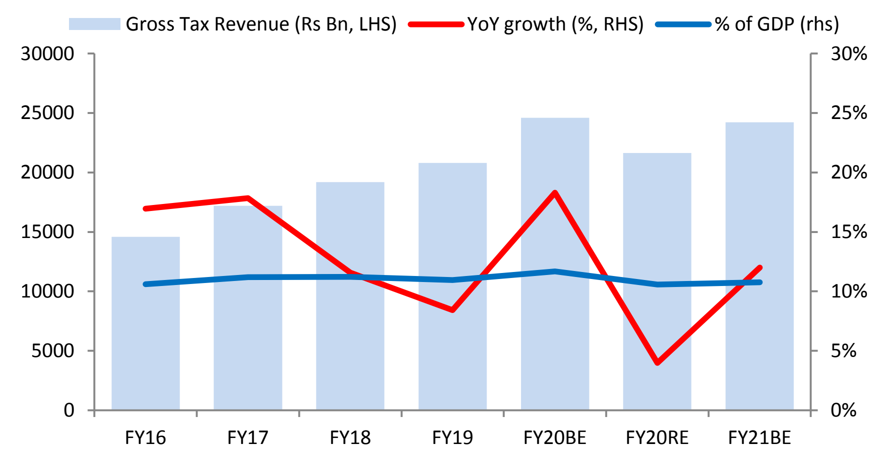
Gross and net market borrowing (Rs bn)



Direct and indirect tax (% of GDP)



Gross tax revenue



Source: Budget Document, PhillipCapital India Research

Outlay on major schemes

(Rs bn)	FY19A	FY20BE	FY20RE	FY21BE
National Social Assistance prog	84	92	92	92
MNREGA	618	600	710	615
Green Revolution	118	126	100	133
Pradhan Mantri Krishi Sinchai Yojana	81	97	79	111
Pradhan Mantri Gram Sadak Yojna	154	190	141	195
Pradhan Mantri Awas Yojna	254	259	253	275
National Rural Drinking Water Mission	55	100	100	115
Swachh Bharat Mission (SBM)	154	126	96	123
National Health Mission (NHM)	315	337	343	341
National Education Mission	308	385	377	392
National Programme of Mid-day meal	95	110	99	110
Development Services	216	276	250	286
National Livelihood Mission-Ajeevika	63	98	98	100
Jobs and Skill Development	61	73	57	54
Urban Rejuvenation Mission: AMRUT	121	138	98	138
Modernisation of Police Forces	33	35	42	32
Interest subsidy for credit to farmers	115	180	179	212
Namami Gange-National Ganga Plan	7	8	4	8
LPG connection to poor households	32	27	37	11
Crop Insurance Scheme	119	140	136	157
Interest Equalisation Scheme	26	29	29	23
Price Stabilisation Fund	15	20	18	20
Police Infrastructure	51	48	45	41
Interest Subsidy for guarantee funds	16	19	19	19
Credit Support Programme	7	6	6	1
Prime Minister Employment Gen Prog (PMEGP)	21	23	25	25
Gram Jyoti Yojna	38	41	41	45
Integrated Power Dev Scheme	39	53	57	53
Construction of New Lines	56	73	79	120

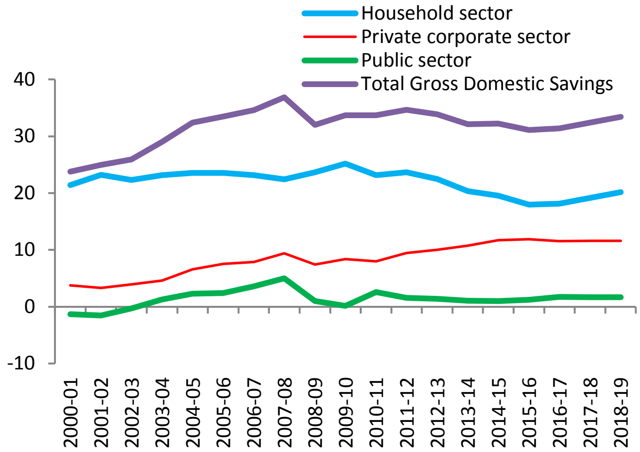
Source: Budget Document, PhillipCapital India Research

Savings – inched higher, led by real estate

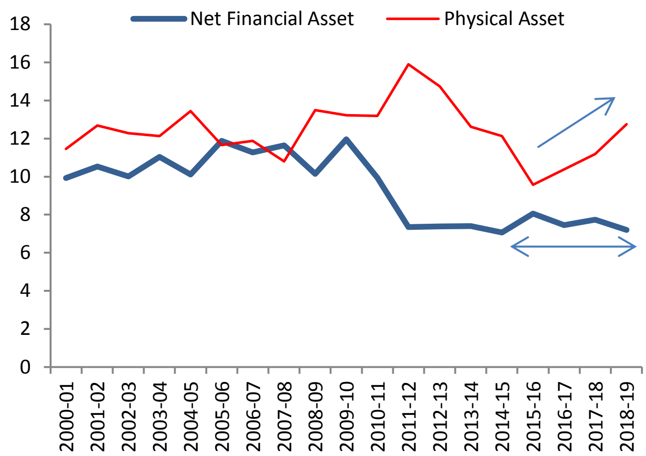
- Savings rate for FY19 rose to 33.4% of GDP vs. 32.4% in FY18 and 31.4% in FY17.
- Gross savings have been dipping since FY16 due to lower household savings. Reversal also comes from the same segment; it is at 12.8% of GDP vs. 9.6% in FY16 and 16% in FY12; an addition of Rs 8,632bn since FY16.
- While we expected physical HH savings to rise in FY18-19, we were also optimistic about financial savings, which weakened in FY19, after rising in FY18. It currently stands at 7.2% of GDP vs. 8.1% in FY16 – an addition of Rs 1,193bn.
- Overall HH savings stood at 20.2% vs. 19.2%/18.1% in FY18/17.
- Private and public sector savings rate remained as stagnant as it was in the last three years at 11.6%/1.7%.

We expect physical HH savings rate to trend higher for the next few years; private sector savings should gradually inch higher. Overall, we expect gross savings rate to inch higher at a marginal pace from current levels.

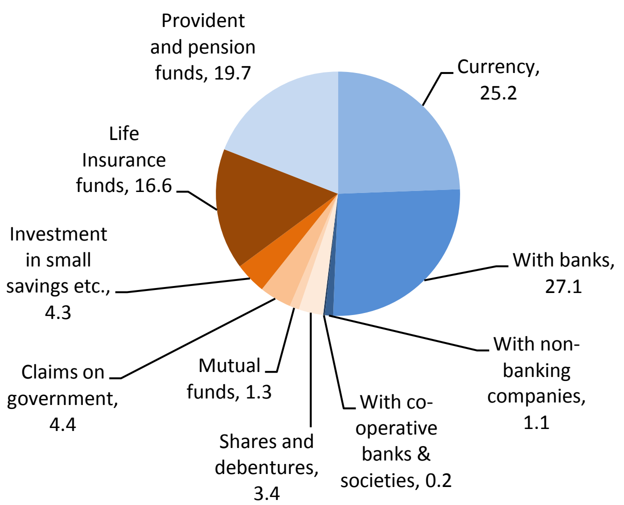
Savings and its break-up (as % of GDP) – HH savings up, others stable



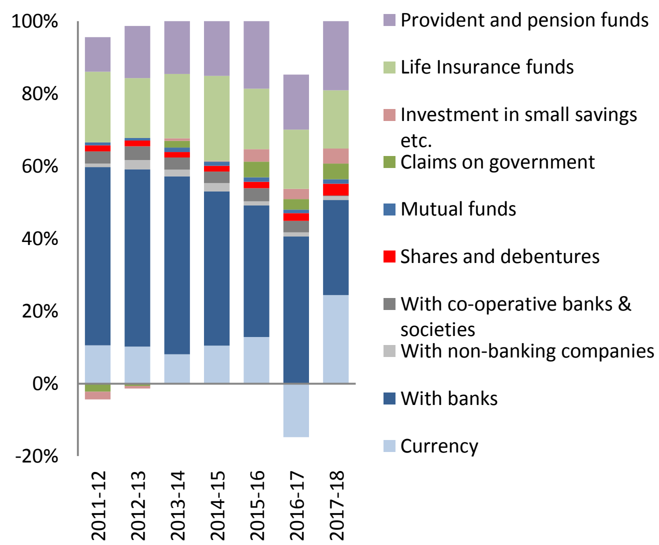
Physical and financial savings (% of GDP) – physical assets inched higher



Components of financial savings (FY18)



Trends of important components of financial savings



Source: , RBI, CSO, PhillipCapital India Research

External Sector – CAD near negligible; prolonged Covid19 will be growth negative, oil a boom

We expect foreign trade to contract in FY21, slight growth in FY22. Trade activity is expected to dip due to sharply lower brent prices as well as our expectation of benign global and domestic economic health.

- Lower oil prices will dent growth of the oil dependent economies; Middle-East is crucial for remittances transferred to India, which saw a decent growth in FY18-20, expected to dip in FY21. We assume that brent prices will remain fairly benign, at US$ 50/barrel for FY21 and US$ 55/barrel for FY22.
- Software services exports will be impacted due to restricted activity owing to Covid-19.
- Capital flows will also be impacted, at the current juncture, we expect the flows to be slightly lower than FY20.

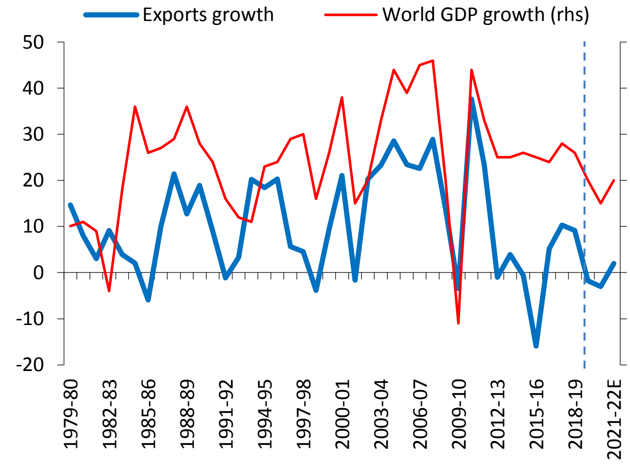
Exports and imports growth estimates are at -3.0%/-4.5% in FY21 and 2%/2% in FY22. Invisibles should soften in FY21 after a robust run in FY18-20; we see growth at -2.5%/5.4% in FY21/22. Remittances and software services exports will weaken amidst economic slowdown. CAD estimate for FY21-22 is at 0%-0.5% of GDP.

Capital flows, primarily in the form of FDI, will remain the key contributor of foreign reserves in India for many years to come. In the long-term, we see higher FDI and exports, as the main fallout of the corporate tax cut. Lower yet robust capital flows are estimated for FY21-22, at US$ 60-70bn per year. Other segments such as FII, ECB, and NRI deposits will also decline in FY21 vs. FY20.

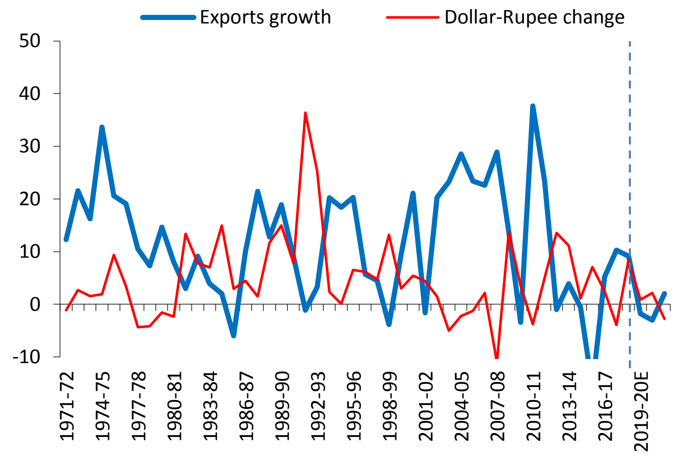
While trade fundamentals are supportive in favour of Rupee stability, it is the dollar sell-off and growth slowdown fears that have led to Rupee depreciating to 74. We expect the rupee to range between 70-75 in FY21. (FY21 average: 72; FY22: 70). We assume that global economic growth will be weak but not in recession. Recessionary scenario will further widen the scope of Rupee weakness.

Sector outlook: While IT services are likely to be impacted due to Covid-19 by way of new deals as well as restricted movement/activity, Weak Rupee will be a positive. We like TCS and Infosys in this space.

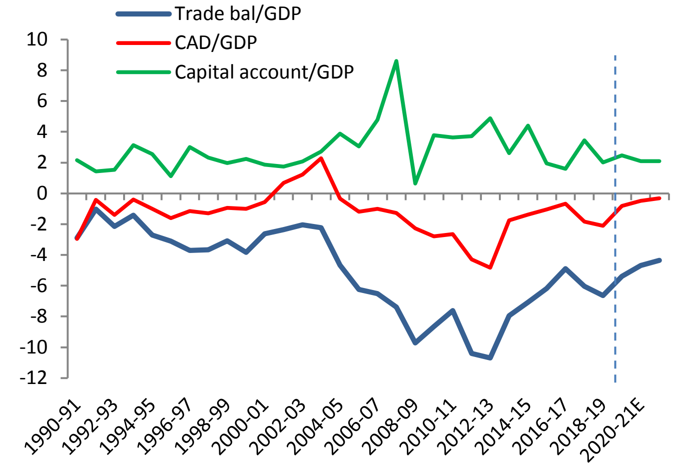
Exports and world GDP growth



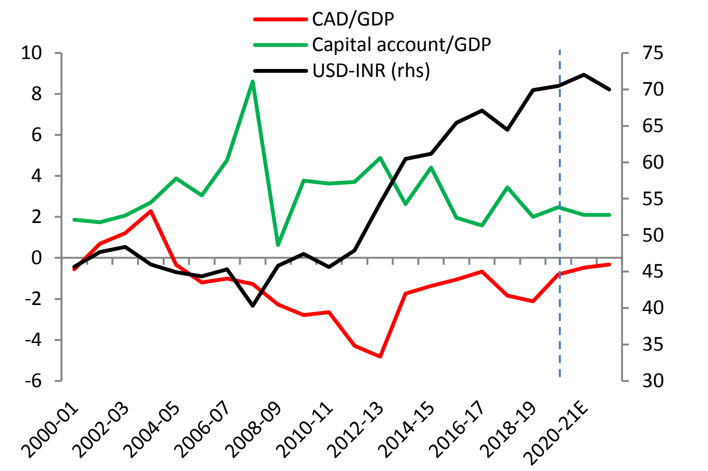
Exports and dollar-rupee change



External sector indicators (% of GDP)



Currency response to external sector indicators



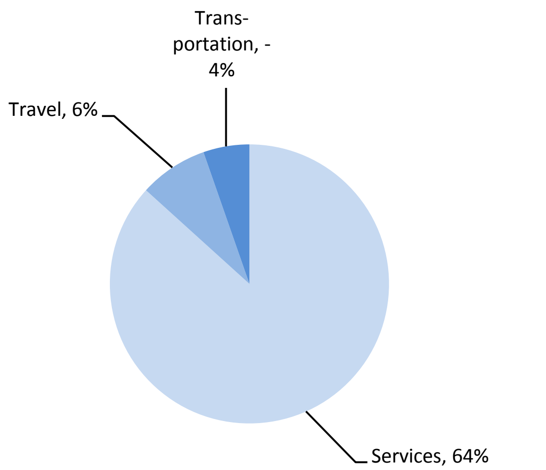
Source: Ministry of Commerce, RBI, PhillipCapital Research

External sector account and estimates

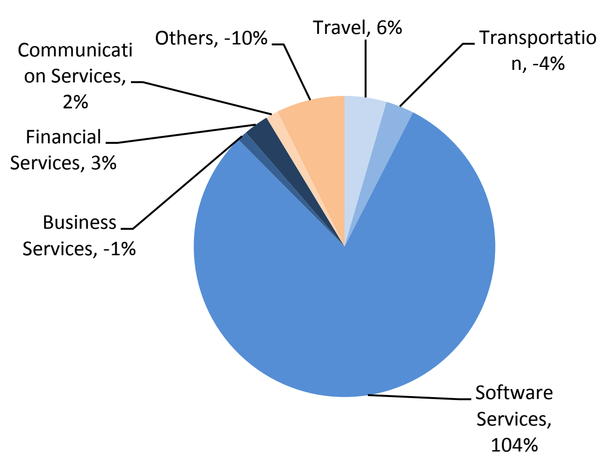
	USD Bn				YoY growth			% of GDP			
	FY19	FY20E	FY21E	FY22E	FY20E	FY21E	FY22E	FY19	FY20E	FY21E	FY22E
Exports	**337.2**	**331.2**	**321.2**	**327.7**	**-1.8**	**-3.0**	**2.0**	**12.4**	**11.5**	**10.5**	**9.8**
Imports	**517.5**	**486.5**	**464.6**	**473.9**	**-6.0**	**-4.5**	**2.0**	**19.1**	**16.9**	**15.2**	**14.1**
Oil Imports	140.6	128.6	100.0	110.0	-8.5	-22.2	10.0	5.2	4.5	3.3	3.3
Non-oil imports	376.9	357.9	364.6	363.9	-5.1	1.9	-0.2	13.9	12.4	11.9	10.8
Trade deficit	**-180.3**	**-155.3**	-143.3	-146.2	**-13.9**	**-7.7**	**2.0**	**-6.6**	**-5.4**	**-4.7**	**-4.4**
Net Invisibles	**123.0**	**132.0**	**128.7**	**135.6**	**7.3**	**-2.5**	**5.4**	**4.5**	**4.6**	**4.2**	**4.0**
Software services	77.7	83.9	87.2	91.6	8.0	4.0	5.0	2.9	2.9	2.8	2.7
Remittances	69.9	74.1	70.4	72.5	6.0	-5.0	3.0	2.6	2.6	2.3	2.2
Investment income	-28.9	-29.0	-30.0	-30.0	0.5	3.4	0.0	-1.1	-1.0	-1.0	-0.9
Current Account Deficit	**-57.3**	**-23.3**	**-14.7**	**-10.6**	**-59.3**	**-36.9**	**-28.0**	**-2.1**	**-0.8**	**-0.5**	**-0.3**
Foreign investment	30.1	47.0	47.0	50.0	56.2	0.0	6.4	1.1	1.6	1.5	1.5
FDI	30.7	37.0	37.0	40.0	20.5	0.0	8.1	1.1	1.3	1.2	1.2
FII	-0.6	10.0	10.0	10.0	-	0.0	0.0	0.0	0.3	0.3	0.3
External borrowing	15.9	19.5	11.0	14.0	23.0	-43.6	27.3	0.6	0.7	0.4	0.4
ECB	10.4	15.0	8.0	9.0	44.0	-46.7	12.5	0.4	0.5	0.3	0.3
Short-term trade credit	2.0	2.0	1.0	2.0	-1.0	-50.0	100.0	0.1	0.1	0.0	0.1
Banking Capital	7.4	4.0	5.0	5.0	-46.2	25.0	0.0	0.3	0.1	0.2	0.1
NRI deposits	10.4	7.0	8.0	9.0	-32.6	14.3	12.5	0.4	0.2	0.3	0.3
Capital Account	**54.4**	**71.5**	**64.5**	**70.5**	**31.4**	**-9.8**	**9.3**	**2.0**	**2.5**	**2.1**	**2.1**

Source: Ministry of Commerce, RBI, PhillipCapital Research

Net Invisibles break-up (FYTD'20 September, % of total)

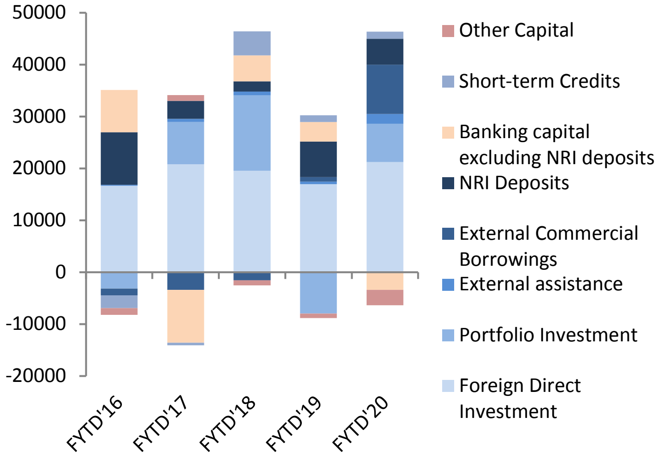


Break-up of Services trade (under invisibles), FYTD 20

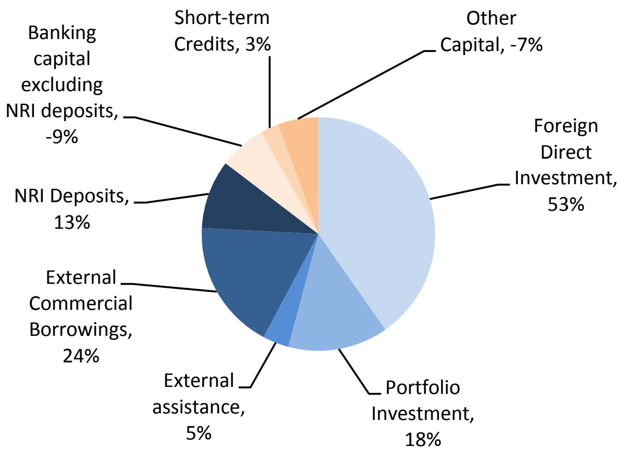


Source: RBI, PhillipCapital India Research

BoP capital flows for Apr-Dec for the respective financial year



Capital flows (FYTD'20 September, % of total)



Source: RBI, PhillipCapital India Research

Top commodities by exports (April-January)

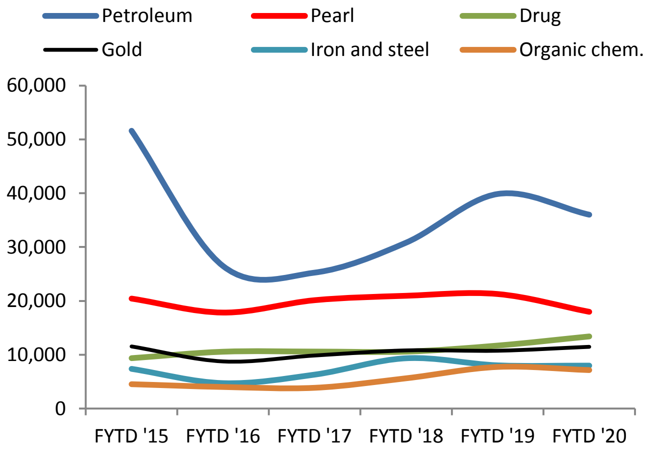
Exports (top-4 commodities): Petroleum products entail the highest share, followed by pearls & precious stones, pharmaceuticals, and gold & precious metal jewellery.

Rising trend: Drugs & pharmaceuticals increased at a faster pace in (FY19-20) after remaining stable for FY16-18, gold was marginally higher, and electric machinery/equipment.

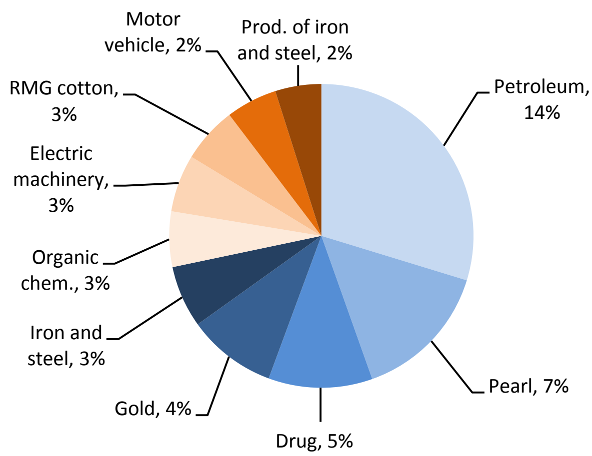
Stable: Iron & steel, cotton.

Falling: Pearls and precious stones (after rising in FY17-19, share fell to 7% in FYTD20 from 9% in FY17), petroleum products, and organic chemicals (vs. double-digit growth in FY18-19).

Top commodities by exports (YTD FY20, USD mn)



Top-10 exports commodities (YTD FY20, %)



Source: Ministry of Commerce, PhillipCapital India Research

Top countries by export (FYTD, April to January)

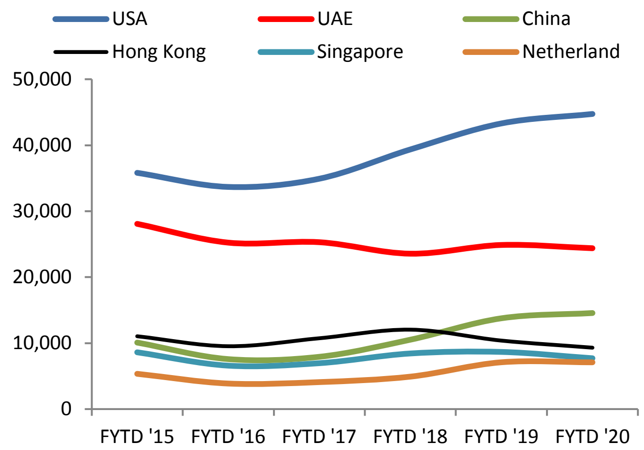
Exports: India exported the greatest number of products to USA (17% vs. 14% in FY15), UAE (fallen to 9% in FY17 from 11% in FY20), and China; exports with other key countries have fallen in FY20.

Rising trend: While trending higher, growth has been subdued in FY20. China recorded growth of 6% (vs. >30% in FY18-19), USA at 3% (vs. >10% in FY18-19).

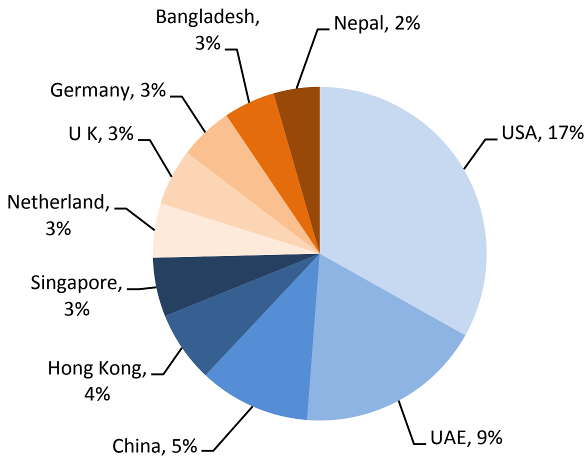
Stable: Netherland (due to a high base).

Falling: Majority of the countries have registered contraction with the steepest fall observed for Bangladesh/Singapore (had seen +ve growth in FY17-19), and Hong Kong.

Top countries by export (YTD FY20, USD mn)



Top-10 exports countries (YTD FY20, %)



Source: Ministry of Commerce, PhillipCapital India Research

Top commodities by imports (FYTD, April to January)

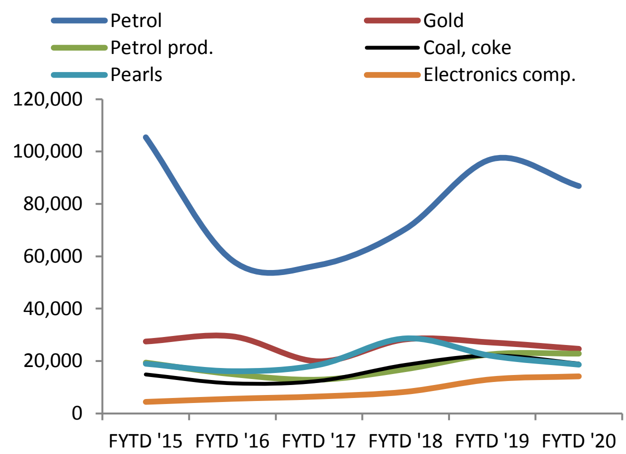
Imports: Petroleum crude holds the highest share in % of goods imported (fallen to 21% from 27% in FY15), followed by gold, petroleum products, coal, pearls & precious stones, and electronic components.

Rising trend: Electronic components was the sole top imported product, which grew at a robust rate of 8% (although growth has moderated from >15% in FY15-19).

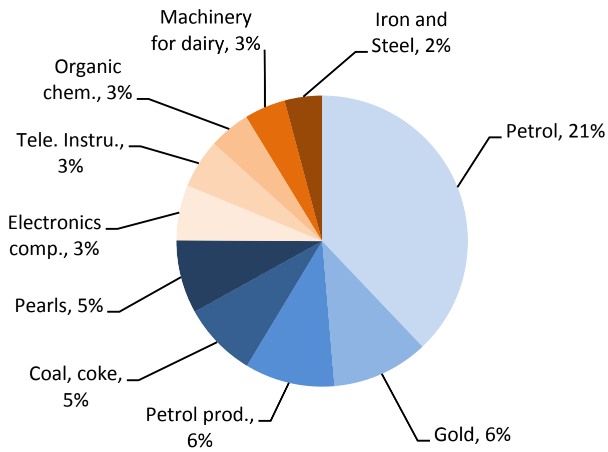
Stable: Petroleum products (from double-digit growth in FY18-19).

Falling: Telecom instruments/pearls & semi-precious stones (consecutive decline), coal/organic chemicals/petroleum crude (vs. rising trend in FY18-19).

Top commodities by import (YTD FY20, USD mn)



Top-10 import commodities (YTD FY20, %)



Source: Ministry of Commerce, PhillipCapital Research

Top countries by import (FYTD, April to January)

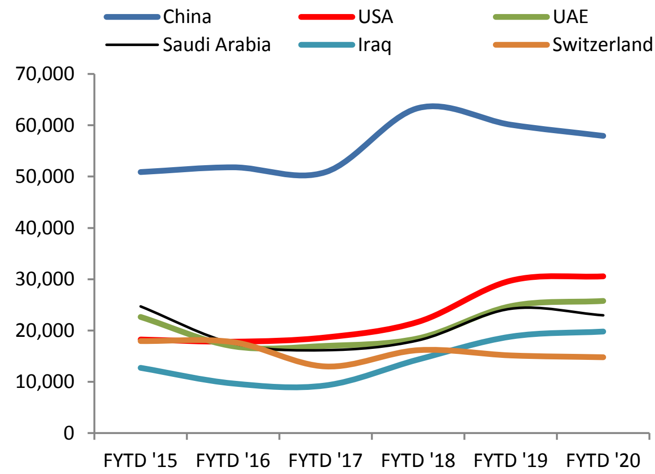
Imports: India imported most from China, USA (share increased to 8% from 5% in FY15), and UAE.

Rising trend: Subdued with imports from Iraq growing by 5%, followed by UAE and USA (vs. robust growth in FY18-19).

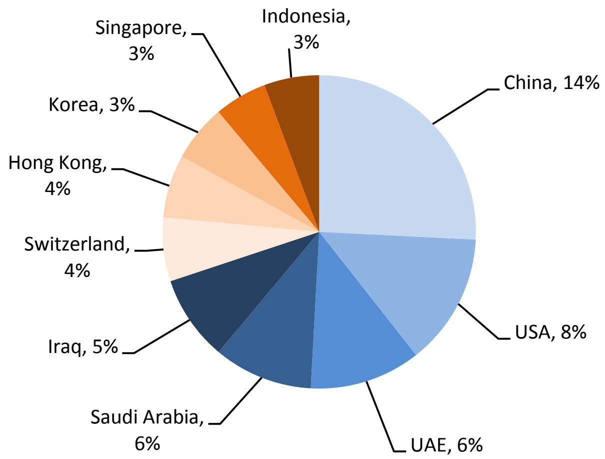
Stable: Singapore and Hong Kong.

Falling: China (contracted for second consecutive year), Korea, Saudi Arabia, Hong Kong, and Switzerland.

Top countries by imports (YTD FY20, USD mn)



Top-10 import countries (YTD FY20, %)

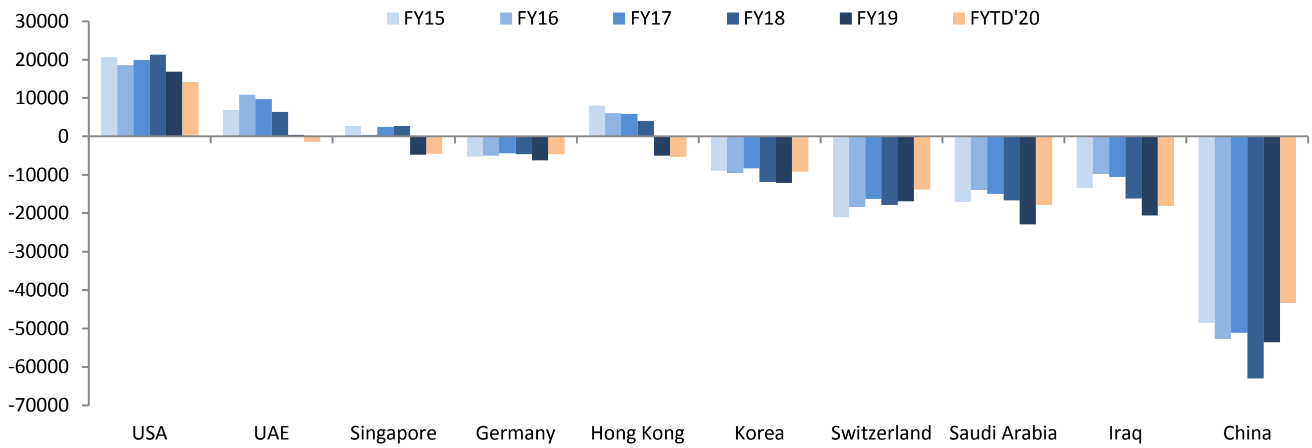


Source: Ministry of Commerce, PhillipCapital India Research

India's top trading partners: Barring USA, India's trade position in deficit

- Surplus with USA has dipped to US$ 14bn from US$ 21bn in FY18.
- With the rest of our larger trading partners, India has a trade deficit position, highest being China at US$ 43bn (vs. US$ 63bn in FY18), followed by Iraq/Saudi Arabia (oil led), and Switzerland (US$ 14bn), Korea (US$ 9bn).

Country-wise trade deficit

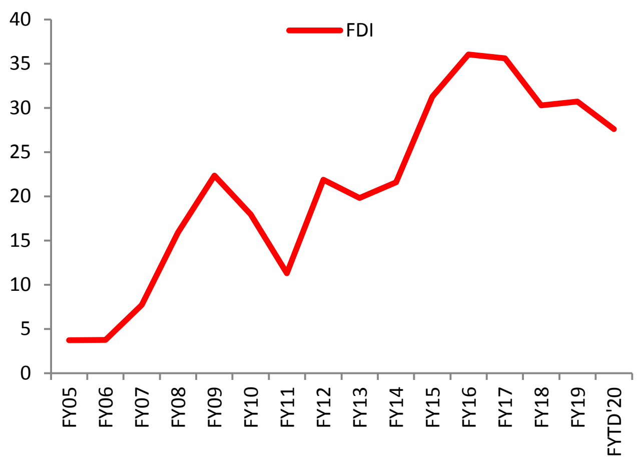


Source: Ministry of Commerce, PhillipCapital India Research

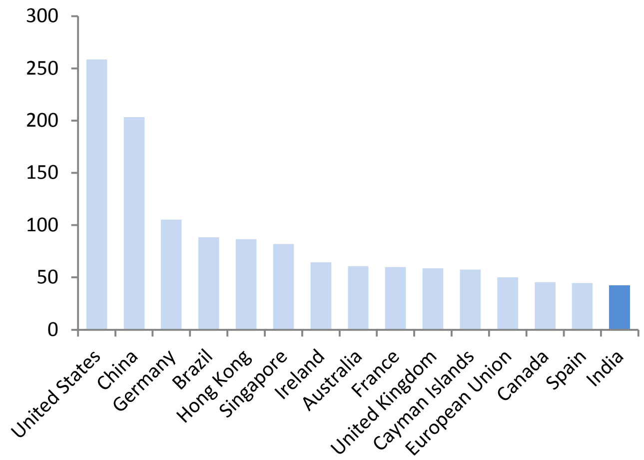
FDI – Key driver for capex flows to India

- There has been a sharp rise in FDI flows to India in the last 6 years, cumulatively India has received US$ 190bn since FY15. We believe that FDI will continue to rise in coming years led by 'Make/Assemble in India'' push by the government and recent reduction in corporate tax rates for the new manufacturing units. In the next few years, we expect India's exports to see a reasonable jump and possibility of further curbing of trade deficit.
- According to UNCTAD (2019), India was among the top FDI recipients in South Asia, and majority of the inflows went into the services industry, including IT.

Foreign direct investment, net inflows (USD bn)



Country-wise FDI, net inflows (USD bn, 2018)

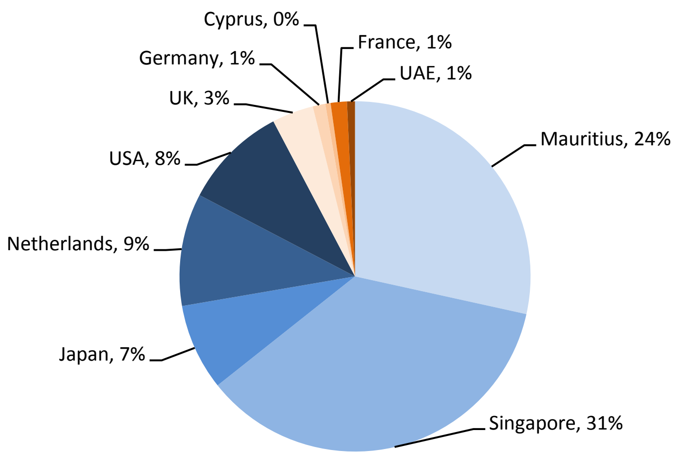


Source: RBI, WTO, PhillipCapital India Research

Country-wise FDI trends

- Singapore has replaced Mauritius as the top source of investment.
- Mauritius' value declined due to the revamped tax treaty, but its share increased to 24% FYTD from 18% in FY19; the peak was 36% in FY17.
- USA's/Netherlands' share in FDI to India increased to 9%/8% from 6%/5% in FY18.
- Japan and UK were sharply higher in Q2FY20 while they were weak yoy.
- Declining share (% of total): Germany, UAE, Cyprus, France – weak FYTD flows.

FDI break-up as per countries (FYTD'20 September, % of total)



Source: DPIIT, PhillipCapital Research

Country-wise FDI flows to India

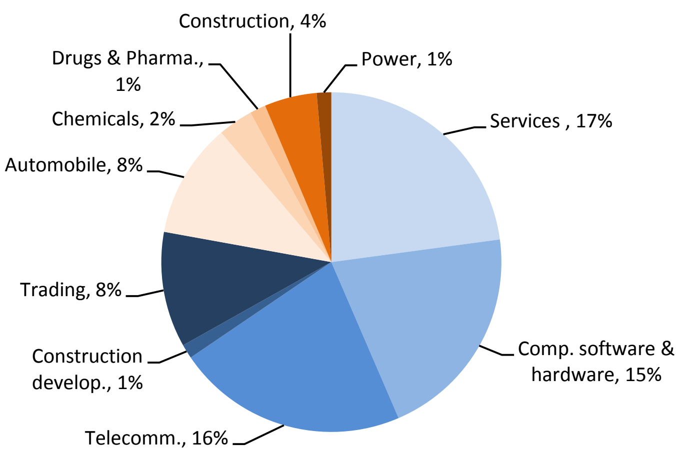
FDI	FY18	FY19	FYTD'20	FY18	FY19	FYTD'20
	USD Bn			% of total		
Singapore	12	16	8	27	37	31
Mauritius	16	8	6	36	18	24
Netherlands	3	4	2	6	9	9
USA	2	3	2	5	7	8
Japan	2	3	2	4	7	7
UK	1	1	1	2	3	3
France	1	0	0	1	1	1
Germany	1	1	0	3	2	1
UAE	1	1	0	2	2	1
Cyprus	0	0	0	1	1	0
Total	**45**	**44**	**26**	**100**	**100**	**100**

Source: DPIIT, PhillipCapital Research

Commodity-wise FDI trends

- Computer software, hardware, telecom, and services sector have received highest FDI in India over the years.
- Followed by trading and automobile.
- In FY20, FDI surged in the telecom sector, others lost momentum. Automobiles maintained a resilient pace of FDI.
- Sharp fall was seen in services, computer software/hardware, chemicals, trading, power, and construction activity.

Top sectors receiving foreign direct investment (FYTD'20 September, % of total)



Source: DPIIT, PhillipCapital Research

Top sectors receiving foreign direct investment

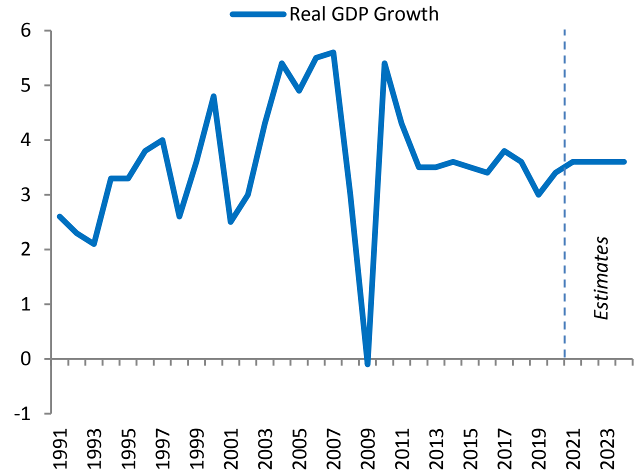
FDI ($ Bn)	FY18	FY19	FYTD'20	FY18	FY19	FYTD'20
	USD Bn			% of total		
Services sector	7	9	4	15	21	17
Telecom	6	3	4	14	6	16
Computer software & hardware	6	6	4	14	14	15
Trading	4	4	2	10	10	8
Automobile industry	2	3	2	5	6	8
Construction Infrastructure activities	3	2	1	6	5	4
Chemicals (other than fertilizers)	1	2	1	3	4	2
Drugs & Pharma	1	0	0	2	1	1
Power	2	1	0	4	2	1
Total	**45**	**44**	**26**	**100**	**100**	**100**

Source: DPIIT, PhillipCapital Research

Global Macros – struck by Covid-19

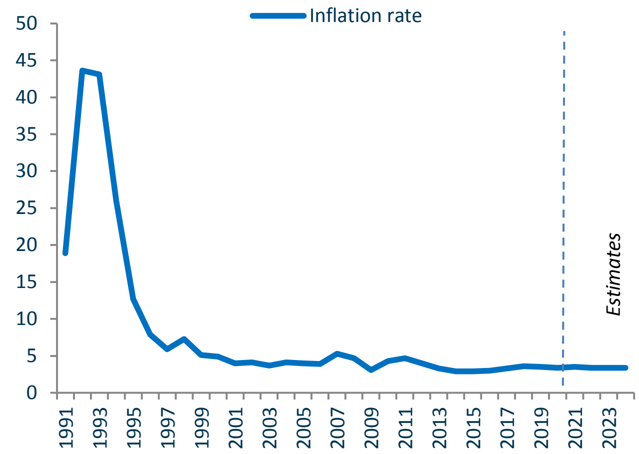
While global economic growth is at risk due to Covid-19 India's lower growth will still outperform. Global GDP growth could fall to as low at 2.0-2.5% in 1H2020. China's GDP growth will likely be 2-3% vs. 6% last year. Covid-19 disruption will take the form of demand and supply impact, lower trade activity, and fiscal and monetary push, which will affect the entire economic curve and equation. While a higher impact would be felt in 1H2019, there is likely to be permanent damage to output. 2H 2019 should fare better, assuming Covid-19 does not become a pandemic (already an epidemic).

World GDP, yoy growth (%)



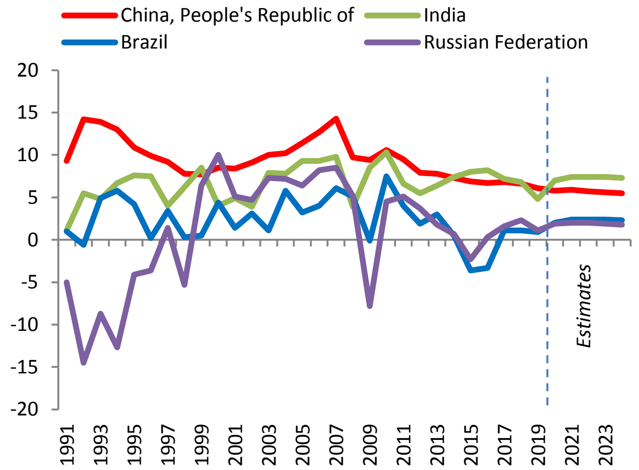
At 3% in 2019, world GDP registered the slowest growth rate since 2010. It is expected to grow at a moderate pace over the coming years (3.4-3.6%). However, there is a definitive downside risk to these estimates, post Covid-19, we believe. Thus, 2020 will likely be weaker than 2019.

World inflation rate, yoy growth (%)



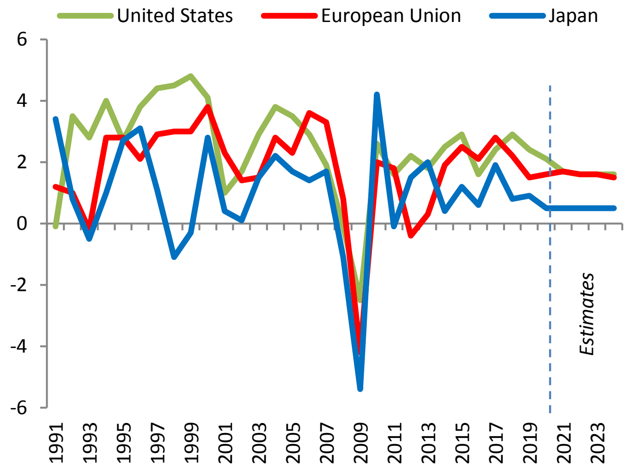
Inflation was stable in 2019 at 3.5%, and it is projected to be constant going ahead (3.4%-3.5%). Lower oil prices will be an added positive.

Emerging economies GDP, yoy growth (%) – India to outperform



All countries growth was tepid in 2019. Brazil and Russia's economy is expected to pick up in contrast to China's. China will be severely impacted due to the virus. Thus, India will be outperforming these economies.

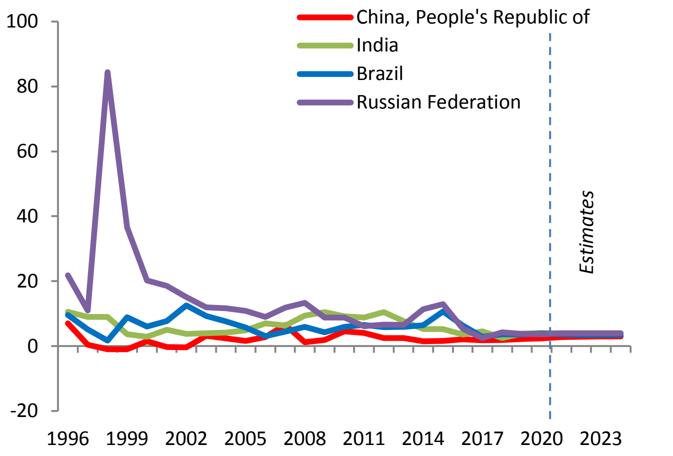
Developed Economies GDP, yoy growth (%)



Growth remained subdued in major developed economies in 2019. Going ahead, GDP is projected to be moderate in EU, US and Japan.

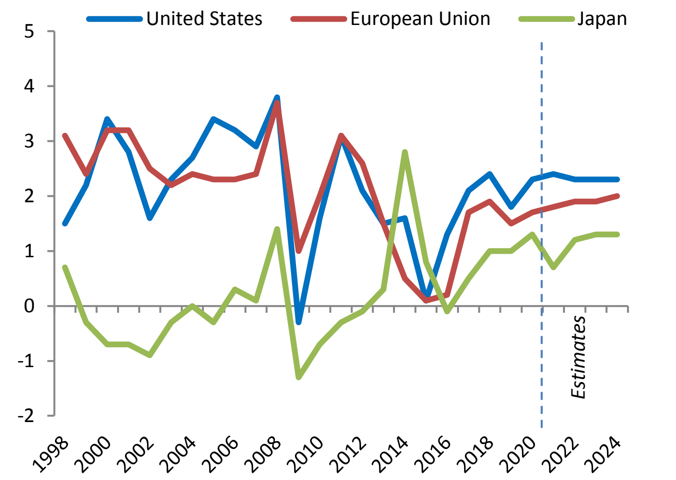
Source: IMF, PhillipCapital India Research

Inflation rate, yoy growth (%)



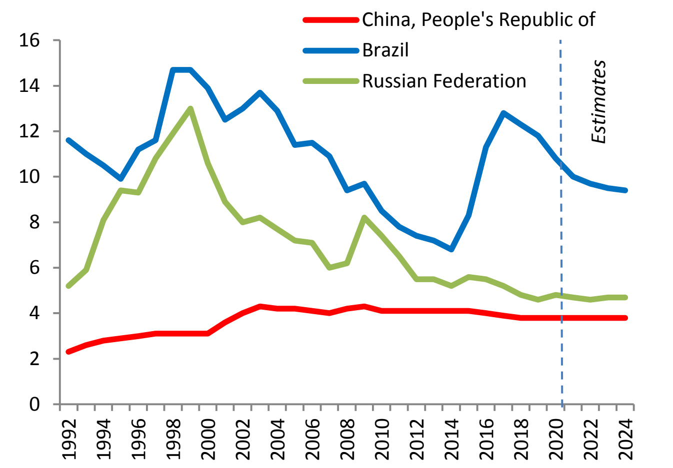
Inflation grew in China in 2019, while declining in Russia, and staying stable in Brazil. CPI is estimated to trend higher marginally in developing countries, especially in China.

Inflation rate, yoy growth (%)



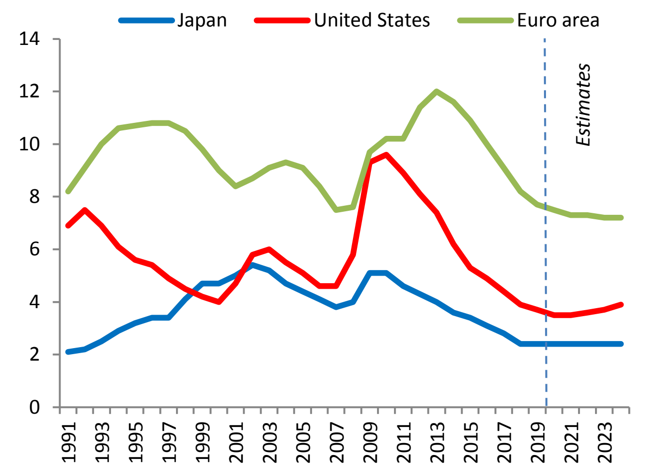
Inflation declined in US and EU in 2019, compared to 2017-18; while it is projected to rise at a moderate pace going ahead.

Unemployment rate, yoy growth (%)



While China and Russia's unemployment rate was stable in 2019, Brazil's jumped to double digits. Going ahead, it is projected to decline in Brazil and remain stable for other countries.

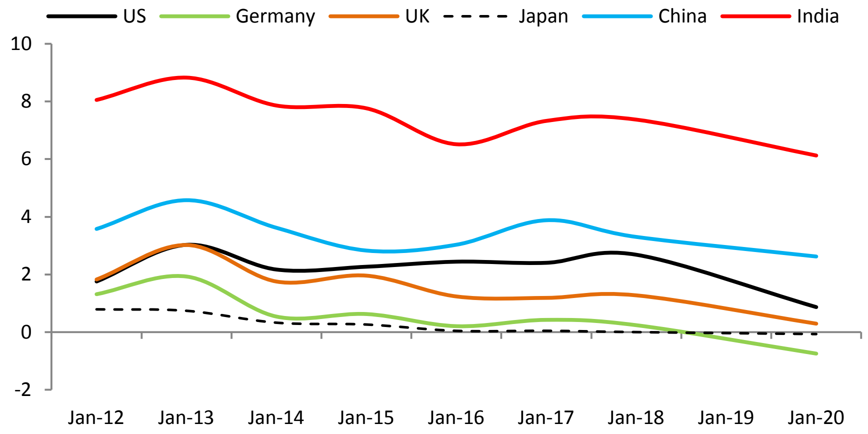
Unemployment rate, yoy growth (%)



Unemployment rate declined to multi-year lows in all three economies in 2019. Estimated to trend in the same range going ahead.

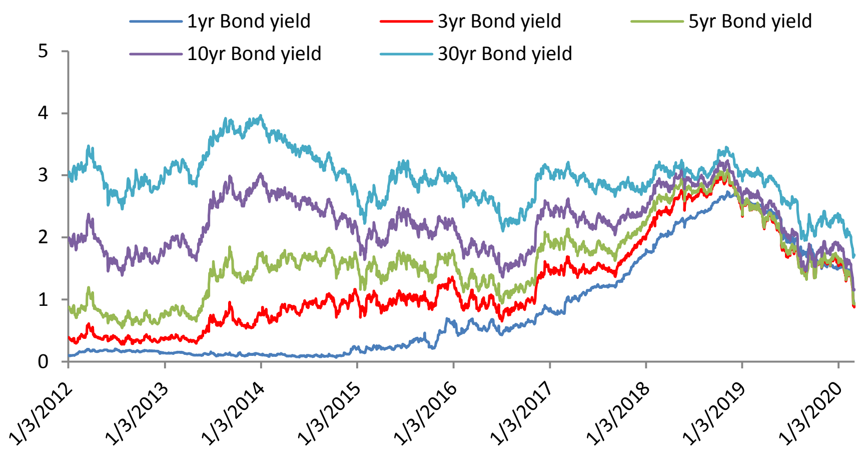
Source: IMF, PhillipCapital India Research

10-year yield trends for key economies



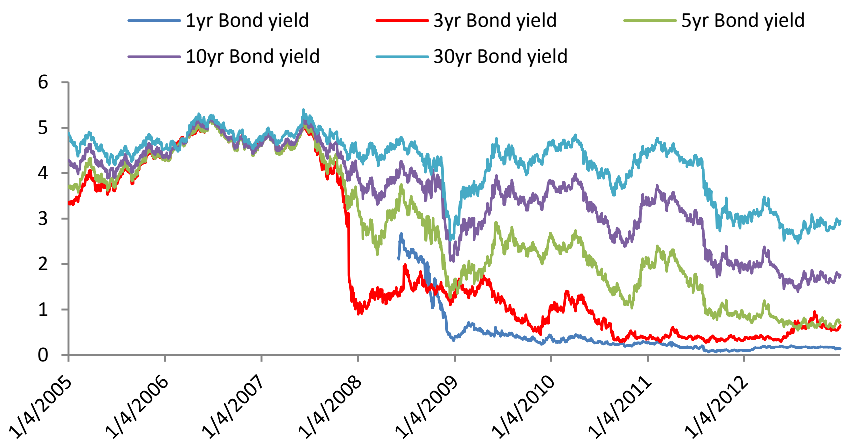
Source: Companies, PhillipCapital Research

US G-sec yield curve (1-3 year yields at same level) (2013-latest)



Source: Companies, PhillipCapital Research

US G-sec yield curve (2005-2012)



Source: Companies, PhillipCapital Research

EARNINGS – Will be SLASHED for FY21-22

Anjali Verma (+ 9122 6246 4115)
anverma@phillipcapital.in

Neeraj Chadwar
(Data Assistance)

While current estimates reflect decent growth, nothing exciting; we expect sharp cut in the estimates for FY21-22. Covid-19 will have adverse impact on consumption which has been key supporting segment over the last few years. Investments are expected to remain weak, as highlighted above. Financials will also feel the stress of economic slowdown, possibility of higher NPAs and credit slowdown. Last when Indian markets corrected in August-September 2019 was on account of domestic slowdown, global economy was in a decent state which is not the case anymore. A huge/concerted/global fiscal and monetary stimulus can reverse the falling trend of all the asset classes. The manner in which equities/yields have crashed is indicative of fears of global economic slowdown.

We see the following scenarios playing out:

- **Base case (March'21 Nifty target of 10700-11200);** estimated 10%/12% earnings growth in FY21/22; 1-year fwd PE assumed at 17x. Our current estimates are at 12%/26%/16% for FY20/21/22 and EBITDA growth at 5%/14%/13%
- **Bear case: (long-lasting Covid-19 impact): (8500-9200):** estimated 8/10% earnings growth in FY21/22, 1-year fwd PE assumption of 15.5x.
- **Bull case: (Global stimulus, contained Covid-19 in India):** 11,700-12,200: estimated 15/17% earnings growth, 1-year fwd PE assumption of 18x.

While there is extreme uncertainty about direction that markets will take, we stick with 'only high quality thesis', we did not deter even when mid-caps were rising. Stocks we like are: HDFC, HDFC bank, ICICI bank, HUL, Asian paints, Havells, Orient electric, Trent, ABFRL, TCS, Infosys, Divi's, Ipca labs, Maruti, Escorts, Shriram Transport, Ultratech, JK cement, L&T, and BEL.

Sector-wise NIFTY EPS additions

	EPS			EPS addition		EPS contribution
	FY20	FY21E	FY22E	FY21E	FY22E	FY21E
Automobile	32	39	49	7	10	5%
Cement	4	5	6	1	1	1%
Financial	150	223	269	72	46	51%
FMCG	40	45	48	5	3	4%
Industrial	32	34	38	2	4	1%
IT	81	88	96	6	9	4%
Metals	38	41	46	3	5	2%
Oil & Gas	90	115	133	25	18	18%
Pharma	15	18	22	3	3	2%
Power	31	35	38	3	3	2%
Telecom	(2)	11	16	13	5	9%
	511	**652**	**760**	140	108	

Source: Companies, PhillipCapital India Research

PC-Universe: PBT trends and estimates

SECTORS	FY19	FY20	FY21	FY22	FY20	FY21	FY22
Discretionary	8,78,713	8,56,593	9,78,497	11,42,205	-2.5%	14.2%	16.7%
Automobiles	3,53,937	2,88,238	3,29,073	3,91,833	-18.6%	14.2%	19.1%
FMCG	3,96,389	4,30,579	4,80,034	5,38,120	8.6%	11.5%	12.1%
Retail	32,960	34,237	45,190	56,019	3.9%	32.0%	24.0%
Paints/Tiles	37,476	41,922	50,156	60,302	11.9%	19.6%	20.2%
Con Electricals/Durable	55,386	58,858	71,008	84,912	6.3%	20.6%	19.6%
Consumer- Others	2,564	2,759	3,037	11,020	7.6%	10.1%	262.9%
Banks	6,10,440	10,45,084	13,71,383	16,71,846	71.2%	31.2%	21.9%
NBFC	3,14,982	2,89,064	3,83,646	4,30,043	-8.2%	32.7%	12.1%
Metals	7,12,122	3,80,420	5,28,879	6,11,600	-46.6%	39.0%	15.6%
Cap Goods	3,07,001	2,93,279	3,37,461	3,90,453	-4.5%	15.1%	15.7%
Cement	97,266	1,41,346	1,63,379	1,97,384	45.3%	15.6%	20.8%
IT Services	9,76,248	10,25,272	11,24,892	12,47,662	5.0%	9.7%	10.9%
Pharma	1,98,477	2,19,780	2,54,249	2,89,379	10.7%	15.7%	13.8%
Infrastructure	91,107	90,464	1,00,219	1,19,364	-0.7%	10.8%	19.1%
Logistics	23,148	18,912	23,449	27,556	-18.3%	24.0%	17.5%
Real Estate	54,913	63,288	75,173	78,175	15.3%	18.8%	4.0%
Agri Input	41,471	58,596	79,069	95,722	41.3%	34.9%	21.1%
Sp Chemicals	25,662	31,095	38,250	44,926	21.2%	23.0%	17.5%
Total	**4331549**	**4513193**	**5458546**	**6346314**	**4.2%**	**20.9%**	**16.3%**
% growth	**20.3%**	**4.2%**	**20.9%**	**16.3%**			

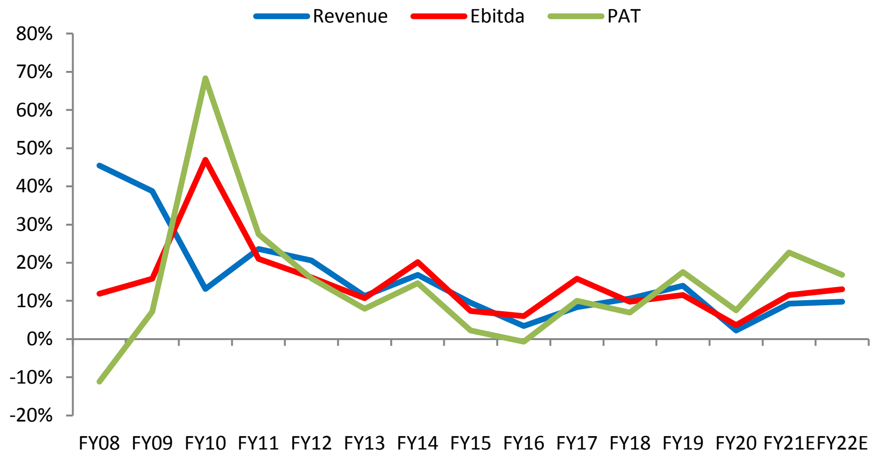
Source: Companies, PhillipCapital Research

PC-Universe: EBITDA trends and estimates

SECTORS	FY19	FY20	FY21	FY22	FY20	FY21	FY22
Discretionary	12,15,788	12,05,251	13,78,382	16,22,737	-0.9%	14.4%	17.7%
Automobiles	6,88,188	6,10,389	7,05,043	8,50,778	-11.3%	15.5%	20.7%
FMCG	3,92,844	4,25,430	4,72,573	5,27,558	8.3%	11.1%	11.6%
Retail	44,428	70,674	86,185	1,01,814	59.1%	21.9%	18.1%
Paints/Tiles	43,750	48,965	56,697	66,493	11.9%	15.8%	17.3%
Con Electricals/Durable	43,332	46,009	53,843	64,252	6.2%	17.0%	19.3%
Consumer- Others	3,247	3,784	4,041	11,842	16.6%	6.8%	193.0%
Banks	16,41,743	19,07,542	20,11,036	22,95,450	16.2%	5.4%	14.1%
NBFC	3,49,042	3,90,750	4,37,303	4,91,668	11.9%	11.9%	12.4%
Metals	12,57,757	9,61,039	11,33,383	12,36,795	-23.6%	17.9%	9.1%
Cap Goods	3,35,738	3,49,376	3,97,844	4,47,873	4.1%	13.9%	12.6%
Cement	1,80,487	2,28,086	2,58,088	2,88,072	26.4%	13.2%	11.6%
IT Services	9,77,913	10,56,881	11,76,459	13,03,886	8.1%	11.3%	10.8%
Pharma	2,64,172	2,94,627	3,28,309	3,71,097	11.5%	11.4%	13.0%
Infrastructure	1,37,965	1,47,784	1,68,721	1,88,880	7.1%	14.2%	11.9%
Logistics	23,354	28,740	32,861	37,555	23.1%	14.3%	14.3%
Real Estate	57,686	68,338	81,562	88,681	18.5%	19.3%	8.7%
Agri Input	75,067	1,13,430	1,25,099	1,39,685	51.1%	10.3%	11.7%
Sp Chemicals	36,282	40,790	49,687	57,423	12.4%	21.8%	15.6%
Total	**6552993**	**6792633**	**7578733**	**8569802**	**3.7%**	**11.6%**	**13.1%**
% growth	**11.5%**	**3.7%**	**11.6%**	**13.1%**			

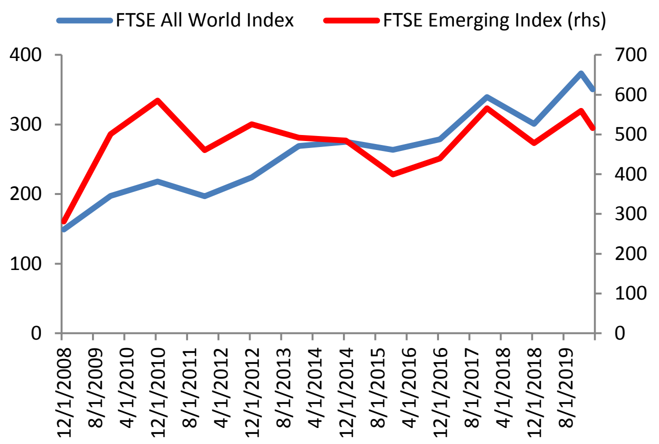
Source: Companies, PhillipCapital Research

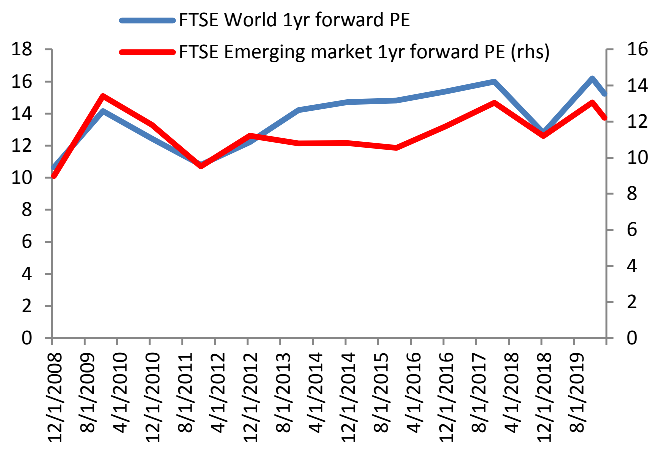
PC-Universe: Growth trends



Source: Companies, PhillipCapital Research

FTSE world and emerging index and forward PE

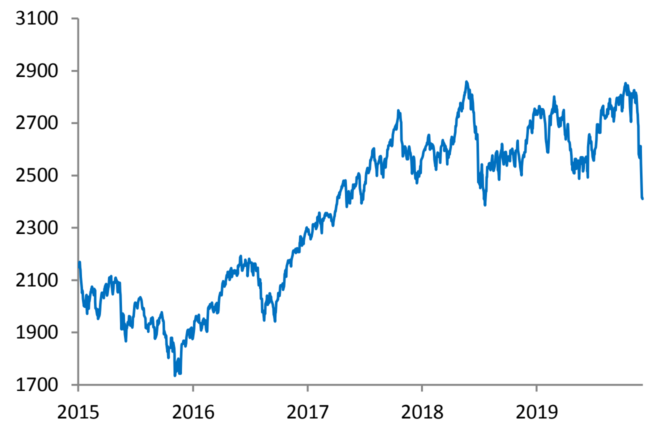




Source: Bloomberg, PhillipCapital Research

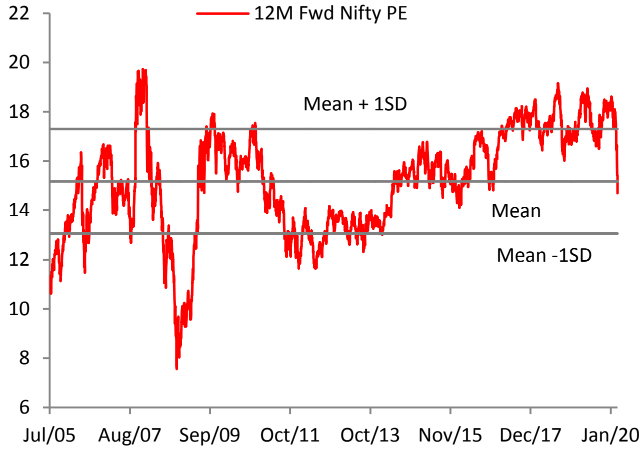
S&P 500 Index

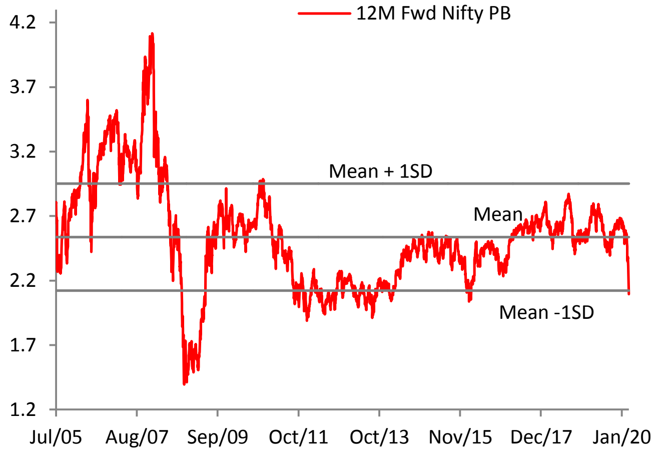
FTSE India Index

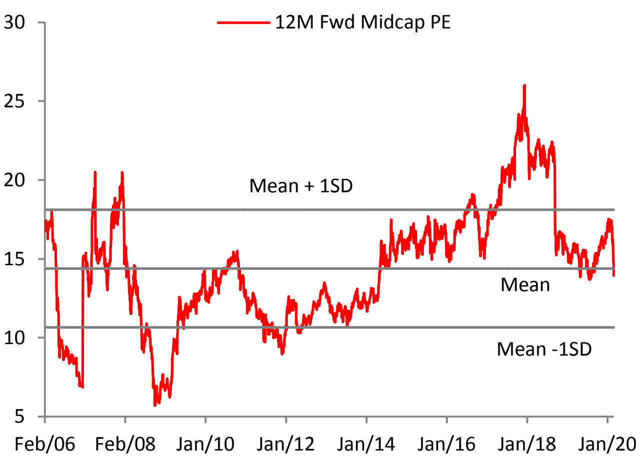


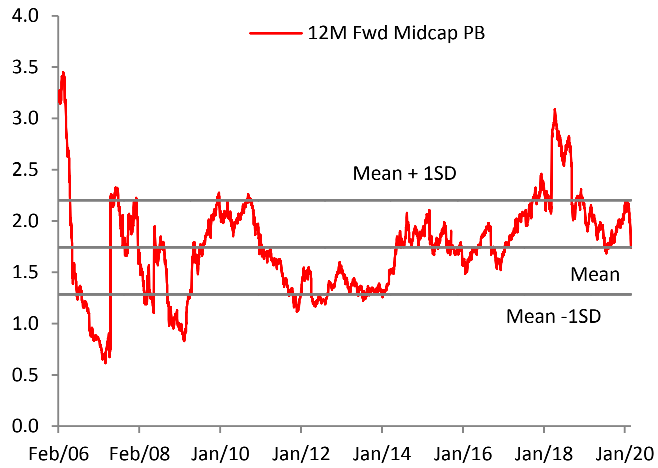
Source: Bloomberg, PhillipCapital Research

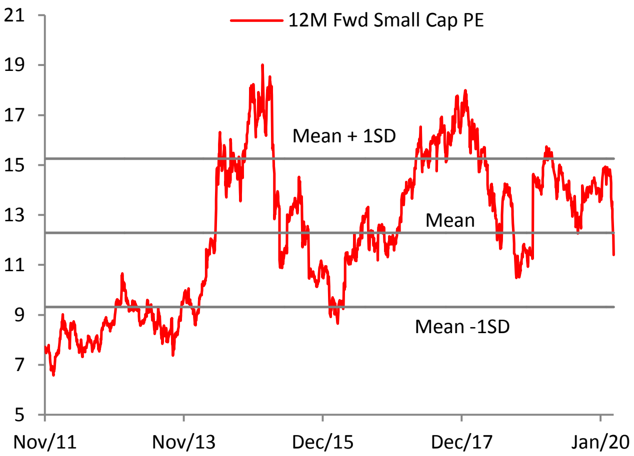
Nifty Valuation charts

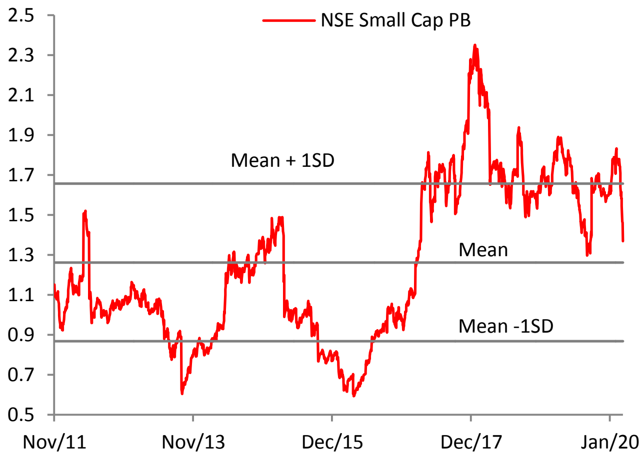






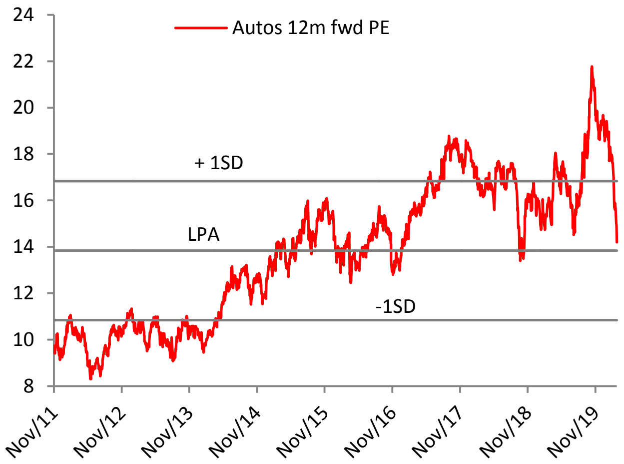


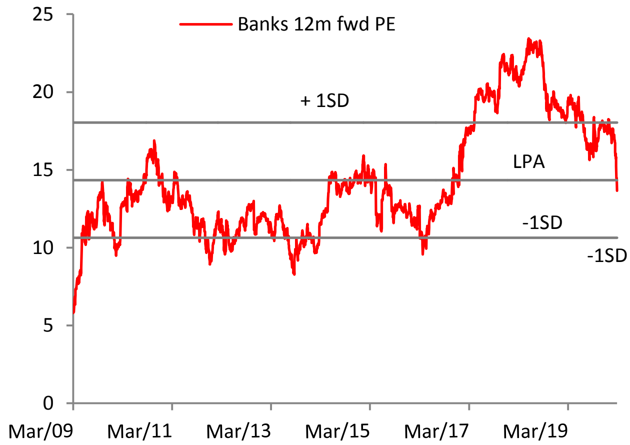


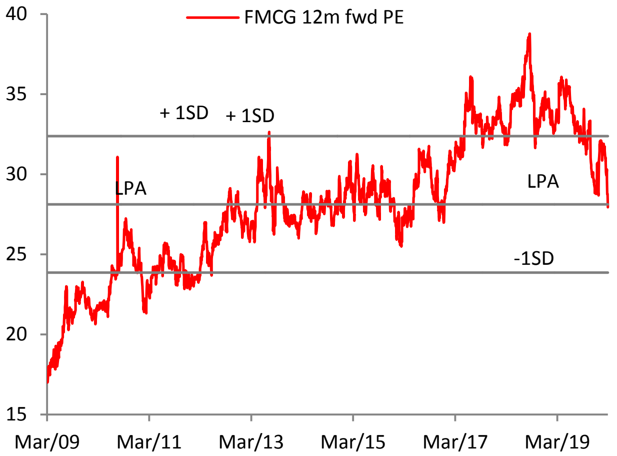


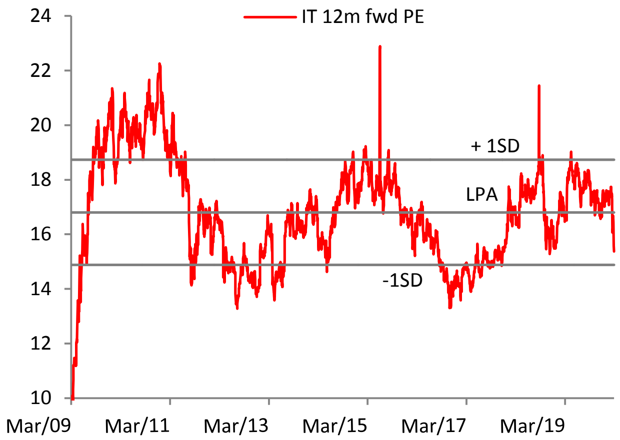
Source: Bloomberg, PhillipCapital India Research,

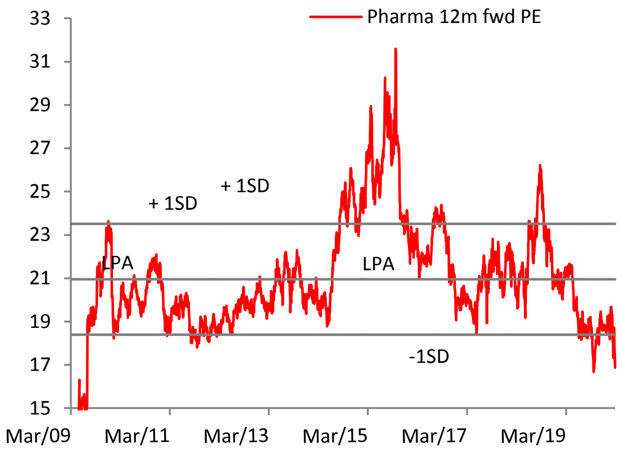
Sector Valuation charts

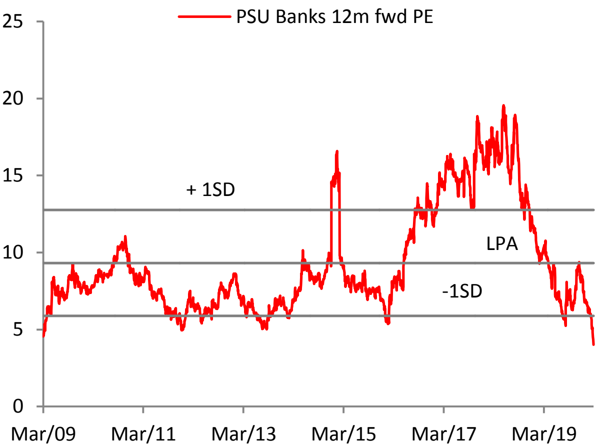






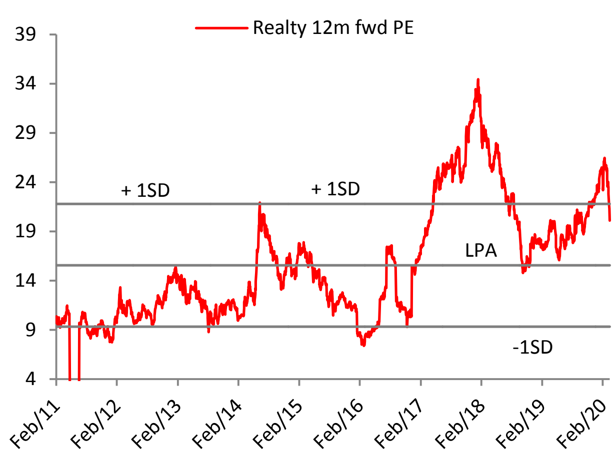


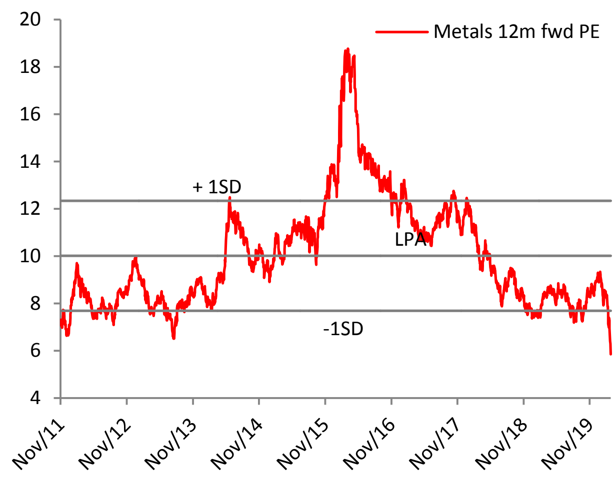


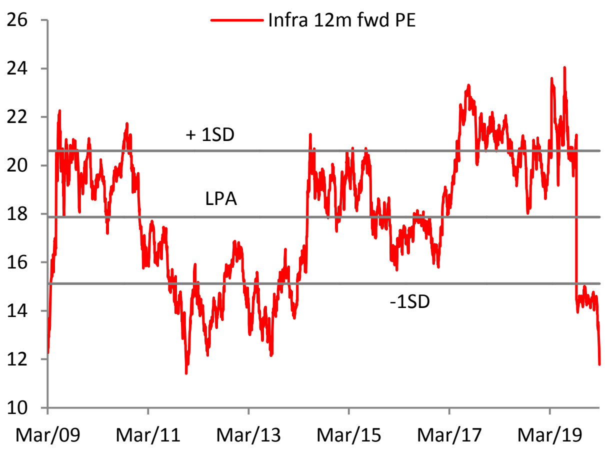


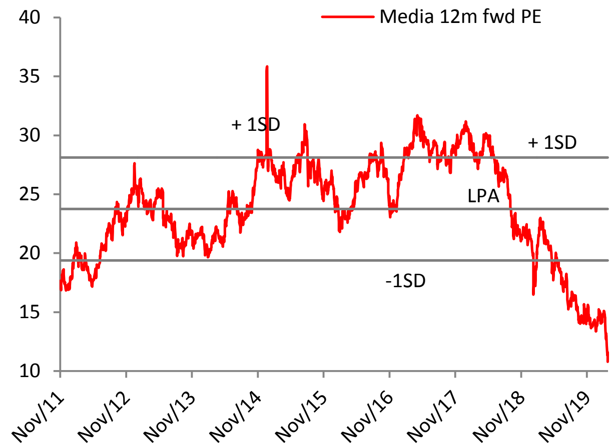
Source: Bloomberg, PhillipCapital India Research,

Sector Valuation charts









Source: Bloomberg, PhillipCapital India Research,

Risks to our outlook

- Prolonged/less impact of Covid19
- Hefty global Monetary/fiscal stimulus
- Sharp volatility in commodity prices
- Sharp global slowdown/recession
- Deficient monsoon
- Geo-political risks

IMF global macro indicators

Subject Descriptor	Units	2013	2014	2015	2016	2017	2018	2019	2020	2021E	2022E	2023E	2024E
Gross domestic product, constant prices	% Chg	3.5	3.6	3.5	3.4	3.8	3.6	3.0	3.4	3.6	3.6	3.6	3.6
Gross domestic product, current prices	US $ Bn	76842	78944	74779	75824	80262	84930	86599	90520	95353	100409	105786	111569
Investment	% of GDP	25.5	25.8	26.0	25.4	26.0	26.3	26.2	26.3	26.4	26.5	26.6	26.7
Gross national savings	% of GDP	26.2	26.7	26.5	26.0	26.5	26.7	26.5	26.5	26.5	26.6	26.6	26.6
Inflation, average consumer prices	% change	3.7	3.2	2.8	2.8	3.2	3.6	3.4	3.6	3.5	3.5	3.4	3.4
Trade volume of goods and services	% Chg	3.6	3.9	2.8	2.3	5.7	3.6	1.1	3.2	3.8	3.8	3.8	3.8
Volume of imports of goods and services	% Chg	3.5	4.0	2.8	2.3	5.7	3.8	1.0	3.3	3.9	3.9	3.9	3.8
Volume of exports of goods and services	% Chg	3.7	3.7	2.9	2.2	5.6	3.4	1.3	3.1	3.6	3.7	3.8	3.7
Commodity Price Index includes both Fuel and Non-Fuel Price Indices	Index, 2005=100	169.2	159.6	108.7	100.0	113.6	128.4	118.5	117.8	117.1	117.3	117.7	118.3
Crude Oil (petroleum), simple average of three spot prices; Dated Brent, West Texas Intermediate, and the Dubai Fateh, US$ per barrel	US $	104.1	96.2	50.8	42.8	52.8	68.3	61.8	57.9	55.3	54.6	54.7	55.3
Commodity Food and Beverage Price Index includes Food and Beverage Price Indices	Index, 2005=100	119.6	119.5	100.3	100.0	103.2	102.1	98.5	101.4	103.1	103.8	103.9	103.9
Commodity Metals Price Index includes Copper, Aluminium, Iron Ore, Tin, Nickel, Zinc, Lead, and Uranium Price Indices	Index, 2005=100	165.4	145.3	105.6	100.0	122.2	130.3	135.9	127.5	128.5	129.6	130.7	131.6

Source: IMF, PhillipCapital India Research,

Disclosures and Disclaimers

PhillipCapital (India) Pvt. Ltd. has three independent equity research groups: Institutional Equities, Institutional Equity Derivatives, and Private Client Group. This report has been prepared by Institutional Equities Group. The views and opinions expressed in this document may, may not match, or may be contrary at times with the views, estimates, rating, and target price of the other equity research groups of PhillipCapital (India) Pvt. Ltd.

This report is issued by PhillipCapital (India) Pvt. Ltd., which is regulated by the SEBI. PhillipCapital (India) Pvt. Ltd. is a subsidiary of Phillip (Mauritius) Pvt. Ltd. References to "PCIPL" in this report shall mean PhillipCapital (India) Pvt. Ltd unless otherwise stated. This report is prepared and distributed by PCIPL for information purposes only, and neither the information contained herein, nor any opinion expressed should be construed or deemed to be construed as solicitation or as offering advice for the purposes of the purchase or sale of any security, investment, or derivatives. The information and opinions contained in the report were considered by PCIPL to be valid when published. The report also contains information provided to PCIPL by third parties. The source of such information will usually be disclosed in the report. Whilst PCIPL has taken all reasonable steps to ensure that this information is correct, PCIPL does not offer any warranty as to the accuracy or completeness of such information. Any person placing reliance on the report to undertake trading does so entirely at his or her own risk and PCIPL does not accept any liability as a result. Securities and Derivatives markets may be subject to rapid and unexpected price movements and past performance is not necessarily an indication of future performance.

This report does not regard the specific investment objectives, financial situation, and the particular needs of any specific person who may receive this report. Investors must undertake independent analysis with their own legal, tax, and financial advisors and reach their own conclusions regarding the appropriateness of investing in any securities or investment strategies discussed or recommended in this report and should understand that statements regarding future prospects may not be realised. Under no circumstances can it be used or considered as an offer to sell or as a solicitation of any offer to buy or sell the securities mentioned within it. The information contained in the research reports may have been taken from trade and statistical services and other sources, which PCIL believe is reliable. PhillipCapital (India) Pvt. Ltd. or any of its group/associate/affiliate companies do not guarantee that such information is accurate or complete and it should not be relied upon as such. Any opinions expressed reflect judgments at this date and are subject to change without notice.

Important: These disclosures and disclaimers must be read in conjunction with the research report of which it forms part. Receipt and use of the research report is subject to all aspects of these disclosures and disclaimers. Additional information about the issuers and securities discussed in this research report is available on request.

Certifications: The research analyst(s) who prepared this research report hereby certifies that the views expressed in this research report accurately reflect the research analyst's personal views about all of the subject issuers and/or securities, that the analyst(s) have no known conflict of interest and no part of the research analyst's compensation was, is, or will be, directly or indirectly, related to the specific views or recommendations contained in this research report.

Additional Disclosures of Interest:
Unless specifically mentioned in Point No. 9 below:

1. The Research Analyst(s), PCIL, or its associates or relatives of the Research Analyst does not have any financial interest in the company(ies) covered in this report.
2. The Research Analyst, PCIL or its associates or relatives of the Research Analyst affiliates collectively do not hold more than 1% of the securities of the company (ies)covered in this report as of the end of the month immediately preceding the distribution of the research report.
3. The Research Analyst, his/her associate, his/her relative, and PCIL, do not have any other material conflict of interest at the time of publication of this research report.
4. The Research Analyst, PCIL, and its associates have not received compensation for investment banking or merchant banking or brokerage services or for any other products or services from the company(ies) covered in this report, in the past twelve months.
5. The Research Analyst, PCIL or its associates have not managed or co-managed in the previous twelve months, a private or public offering of securities for the company (ies) covered in this report.
6. PCIL or its associates have not received compensation or other benefits from the company(ies) covered in this report or from any third party, in connection with the research report.
7. The Research Analyst has not served as an Officer, Director, or employee of the company (ies) covered in the Research report.
8. The Research Analyst and PCIL has not been engaged in market making activity for the company(ies) covered in the Research report.
9. Details of PCIL, Research Analyst and its associates pertaining to the companies covered in the Research report:

Sr. no.	Particulars	Yes/No
1	**Whether compensation has been received from the company(ies) covered in the Research report in the past 12 months for investment banking transaction by PCIL**	No
2	**Whether Research Analyst, PCIL or its associates or relatives of the Research Analyst affiliates collectively hold more than 1% of the company(ies) covered in the Research report**	No
3	Whether compensation has been received by PCIL or its associates from the company(ies) covered in the Research report	No
4	PCIL or its affiliates have managed or co-managed in the previous twelve months a private or public offering of securities for the company(ies) covered in the Research report	No
5	Research Analyst, his associate, PCIL or its associates have received compensation for investment banking or merchant banking or brokerage services or for any other products or services from the company(ies) covered in the Research report, in the last twelve months	No

Independence: PhillipCapital (India) Pvt. Ltd. has not had an investment banking relationship with, and has not received any compensation for investment banking services from, the subject issuers in the past twelve (12) months, and PhillipCapital (India) Pvt. Ltd does not anticipate receiving or intend to seek compensation for investment banking services from the subject issuers in the next three (3) months. PhillipCapital (India) Pvt. Ltd is not a market maker in the securities mentioned in this research report, although it, or its affiliates/employees, may have positions in, purchase or sell, or be materially interested in any of the securities covered in the report.

Suitability and Risks: This research report is for informational purposes only and is not tailored to the specific investment objectives, financial situation or particular requirements of any individual recipient hereof. Certain securities may give rise to substantial risks and may not be suitable for certain investors. Each investor must make its own determination as to the appropriateness of any securities referred to in this research report based upon the legal, tax and accounting considerations applicable to such investor and its own investment objectives or strategy, its financial situation and its investing experience. The value of any security may be positively or adversely affected by changes in foreign exchange or interest rates, as well as by other financial, economic, or political factors. Past performance is not necessarily indicative of future performance or results.

Sources, Completeness and Accuracy: The material herein is based upon information obtained from sources that PCIPL and the research analyst believe to be reliable, but neither PCIPL nor the research analyst represents or guarantees that the information contained herein is accurate or complete and it should not be relied upon as such. Opinions expressed herein are current opinions as of the date appearing on this material, and are subject to change without notice. Furthermore, PCIPL is under no obligation to update or keep the information current. Without limiting any of the foregoing, in no event shall PCIL, any of its affiliates/employees or any third party involved in, or related to computing or compiling the information have any liability for any damages of any kind including but not limited to any direct or consequential loss or damage, however arising, from the use of this document.

Caution: Risk of loss in trading/investment can be substantial and even more than the amount / margin given by you. Investment in securities market are subject to market risks, you are requested to read all the related documents carefully before investing. You should carefully consider whether trading/investment is appropriate for you in light of your experience, objectives, financial resources and other relevant circumstances. PhillipCapital and any of its employees, directors, associates, group entities, or affiliates shall not be liable for losses, if any, incurred by you. You are further cautioned that trading/investments in financial markets are subject to market risks and are advised to seek independent third party trading/investment advice outside PhillipCapital/group/associates/affiliates/directors/employees before and during your trading/investment. There is no guarantee/assurance as to returns or profits or capital protection or appreciation. PhillipCapital and any of its employees, directors, associates, and/or employees, directors, associates of PhillipCapital's group entities or affiliates is not inducing you for trading/investing in the financial market(s). Trading/Investment decision is your sole responsibility. You must also read the Risk Disclosure Document and Do's and Don'ts before investing.

Kindly note that past performance is not necessarily a guide to future performance.

For Detailed Disclaimer: Please visit our website www.phillipcapital.in

IMPORTANT DISCLOSURES FOR U.S. PERSONS

This research report is a product of PhillipCapital (India) Pvt. Ltd. which is the employer of the research analyst(s) who has prepared the research report. PhillipCapital (India) Pvt Ltd. is authorized to engage in securities activities in India. PHILLIPCAP is not a registered broker-dealer in the United States and, therefore, is not subject to U.S. rules regarding the preparation of research reports and the independence of research analysts. This research report is provided for distribution to "major U.S. institutional investors" in reliance on the exemption from registration provided by Rule 15a-6 of the U.S. Securities Exchange Act of 1934, as amended (the "Exchange Act"). If the recipient of this report is not a Major Institutional Investor as specified above, then it should not act upon this report and return the same to the sender. Further, this report may not be copied, duplicated and/or transmitted onward to any U.S. person, which is not a Major Institutional Investor.

Any U.S. recipient of this research report wishing to effect any transaction to buy or sell securities or related financial instruments based on the information provided in this research report should do so only through Rosenblatt Securities Inc, 40 Wall Street 59th Floor, New York NY 10005, a registered broker dealer in the United States. Under no circumstances should any recipient of this research report effect any transaction to buy or sell securities or related financial instruments through PHILLIPCAP. Rosenblatt Securities Inc. accepts responsibility for the contents of this research report, subject to the terms set out below, to the extent that it is delivered to a U.S. person other than a major U.S. institutional investor.

The analyst whose name appears in this research report is not registered or qualified as a research analyst with the Financial Industry Regulatory Authority ("FINRA") and may not be an associated person of Rosenblatt Securities Inc. and, therefore, may not be subject to applicable restrictions under FINRA Rules on communications with a subject company, public appearances and trading securities held by a research analyst account.

Ownership and Material Conflicts of Interest

Rosenblatt Securities Inc. or its affiliates does not 'beneficially own,' as determined in accordance with Section 13(d) of the Exchange Act, 1% or more of any of the equity securities mentioned in the report. Rosenblatt Securities Inc, its affiliates and/or their respective officers, directors or employees may have interests, or long or short positions, and may at any time make purchases or sales as a principal or agent of the securities referred to herein. Rosenblatt Securities Inc. is not aware of any material conflict of interest as of the date of this publication

Compensation and Investment Banking Activities

Rosenblatt Securities Inc. or any affiliate has not managed or co-managed a public offering of securities for the subject company in the past 12 months, nor received compensation for investment banking services from the subject company in the past 12 months, neither does it or any affiliate expect to receive, or intends to seek compensation for investment banking services from the subject company in the next 3 months.

Additional Disclosures

This research report is for distribution only under such circumstances as may be permitted by applicable law. This research report has no regard to the specific investment objectives, financial situation or particular needs of any specific recipient, even if sent only to a single recipient. This research report is not guaranteed to be a complete statement or summary of any securities, markets, reports or developments referred to in this research report. Neither PHILLIPCAP nor any of its directors, officers, employees or agents shall have any liability, however arising, for any error, inaccuracy or incompleteness of fact or opinion in this research report or lack of care in this research report's preparation or publication, or any losses or damages which may arise from the use of this research report.

PHILLIPCAP may rely on information barriers, such as "Chinese Walls" to control the flow of information within the areas, units, divisions, groups, or affiliates of PHILLIPCAP.

Investing in any non-U.S. securities or related financial instruments (including ADRs) discussed in this research report may present certain risks. The securities of non-U.S. issuers may not be registered with, or be subject to the regulations of, the U.S. Securities and Exchange Commission. Information on such non-U.S. securities or related financial instruments may be limited. Foreign companies may not be subject to audit and reporting standards and regulatory requirements comparable to those in effect within the United States.

The value of any investment or income from any securities or related financial instruments discussed in this research report denominated in a currency other than U.S. dollars is subject to exchange rate fluctuations that may have a positive or adverse effect on the value of or income from such securities or related financial instruments.

Past performance is not necessarily a guide to future performance and no representation or warranty, express or implied, is made by PHILLIPCAP with respect to future performance. Income from investments may fluctuate. The price or value of the investments to which this research report relates, either directly or indirectly, may fall or rise against the interest of investors. Any recommendation or opinion contained in this research report may become outdated as a consequence of changes in the environment in which the issuer of the securities under analysis operates, in addition to changes in the estimates and forecasts, assumptions and valuation methodology used herein.

No part of the content of this research report may be copied, forwarded or duplicated in any form or by any means without the prior written consent of PHILLIPCAP and PHILLIPCAP accepts no liability whatsoever for the actions of third parties in this respect.

PhillipCapital (India) Pvt. Ltd.
Registered office: 18th floor, Urmi Estate, Ganpatrao Kadam Marg, Lower Parel (West), Mumbai – 400013, India.

ANJALI VERMA

Digitally signed by ANJALI VERMA
DN: c=IN, o=PHILLIPCAPITAL INDIA PVT LTD, postalCode=400706, st=Maharashtra,
2.5.4.20=e230711ee78105e7ed8bd9bf49614bf9035b911ed27d83312cf3ef4b50dfca2a, serialNumber=49b70d7e56947d49deb2c457c5e4c0f2bf09684212e31e49e5a40a6eb3ea7767, cn=ANJALI VERMA
Date: 2020.03.12 14:11:49 +05'30'