

ALPHA STRATEGIST

“Goldilocks & Three Bears”



**WINNING PORTFOLIOS
POWERED BY KNOWLEDGE**

September 2024 | Issue No. 141

- With the stabilization seen in terms GDP growth, cooling down of twin deficits (Fiscal deficit & Current Account deficit) and inflation trending lower, we feel that Indian Economy has entered in a Goldilocks phase.
- Improving Forex reserves, stable currency and the declining 10 Yr yields also provide additional comfort on the macro front.
- However, there are certain risks in current scenario like Global events, Inflation and Valuations which can cause near to medium term volatility in the markets and impact the investors' return
- Basis this, our theme for this edition is **"Goldilocks & Three Bears"**, where along with describing the goldilocks phase, we have provided mitigants to these above risks.
- From a valuation perspective, large-cap stocks seem to be fairly valued, while mid- and small-cap stocks are currently trading at higher valuations. However, based on consensus estimates, the earnings growth for Mid Caps and Small Caps is high compared to Large Caps
- With the current scenario of rich valuations and heightened volatility sector rotation is expected to continue and be more prominent going forward.
- We still continue with our view to have a duration bias in the fixed income portfolio so as to capitalize on the likely softening of yields in the next 1-2 years





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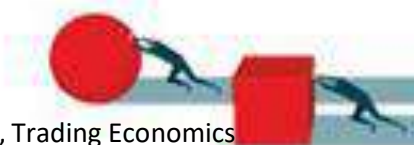
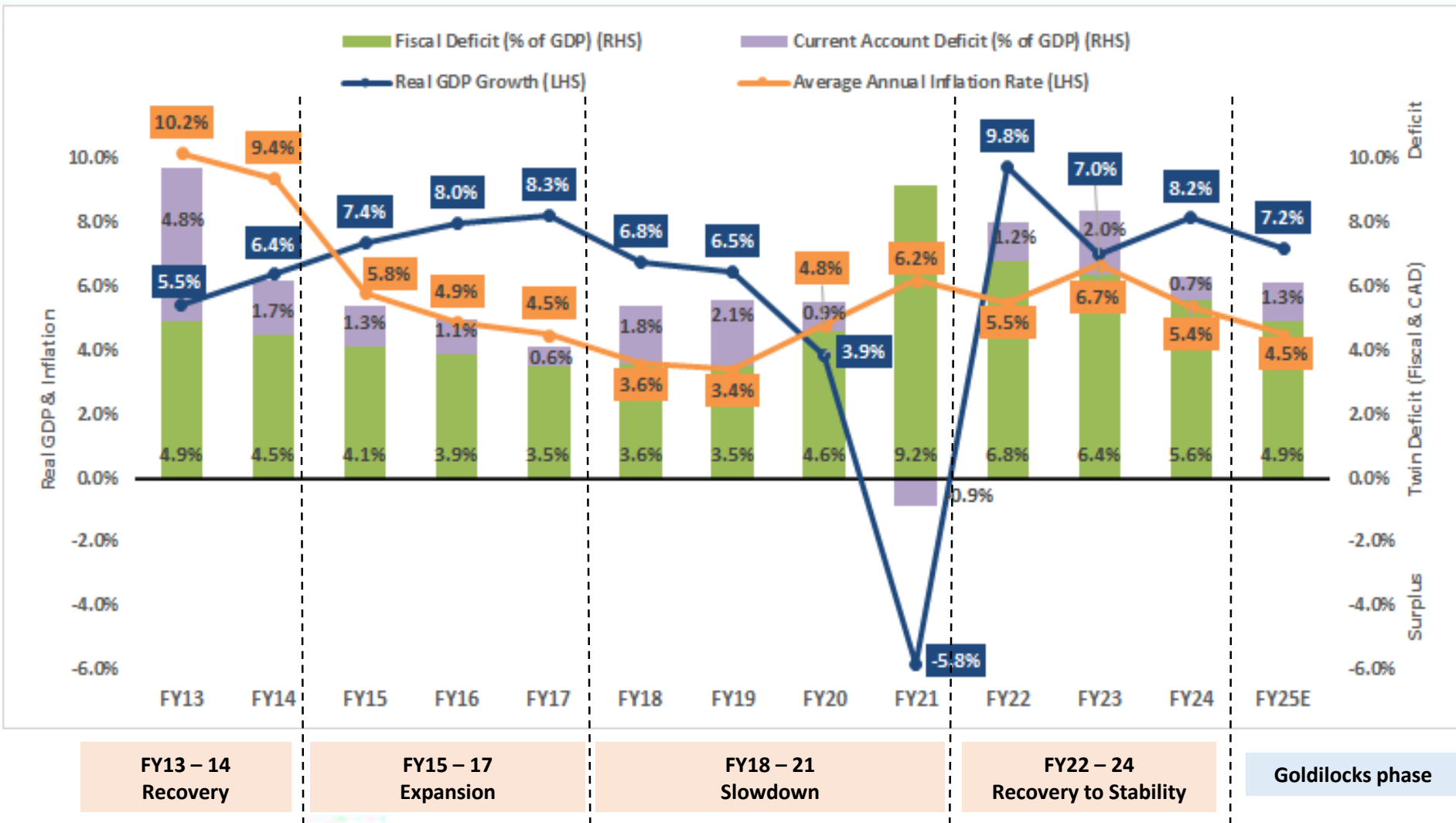
Asset Class Performance – CYTD24

2021	2022	2023	1st Jan'24 to 31st Aug'24 (Abs basis)
Equity-IND 30.2%	Gold 13.9%	NASDAQ 46.0%	Equity-IND 22.2%
Equity-US 29.1%	Liquid 5.1%	Equity-IND 25.8%	Equity-US 19.1%
NASDAQ 23.5%	Equity-IND 3.0%	Equity-US 25.7%	NASDAQ 18.4%
MSCI DM 22.2%	Real Estate 2.8%	MSCI DM 22.3%	MSCI DM 16.2%
Liquid 3.6%	Debt 2.5%	Gold 15.4%	Gold 13.9%
Debt 3.4%	MSCI DM -10.0%	MSCI EM 7.7%	Debt 9.6%
Real Estate 3.1%	Equity-US -10.7%	Debt 7.3%	MSCI EM 8.2%
MSCI EM -2.9%	MSCI EM -13.5%	Liquid 7.1%	Liquid 7.4%
Gold -4.2%	NASDAQ -26.1%	Real Estate 2.0%	Real Estate 4.6%

Note: Price Index values are being considered. Returns for Debt & Liquid are taken on Annualised basis, rest all are on absolute basis
 Equity IND - Nifty 50, Equity US - S&P 500 INR, MSCI DM – MSCI World Index (Developed) INR, MSCI EM -MSCI Emerging Index INR, Gold - Gold INR, Debt - CRISIL Composite Bond Index, Liquid - CRISIL Liquid Index, NASDAQ - NASDAQ Composite index INR, Real Estate - RBI House Price Index (3 month returns for CY24 since data for this index is available only till end Jun'24)



India : Goldilocks phase – GDP, Inflation & Twin Deficits



Source: MOWL, RBI, MOSPI, Trading Economics

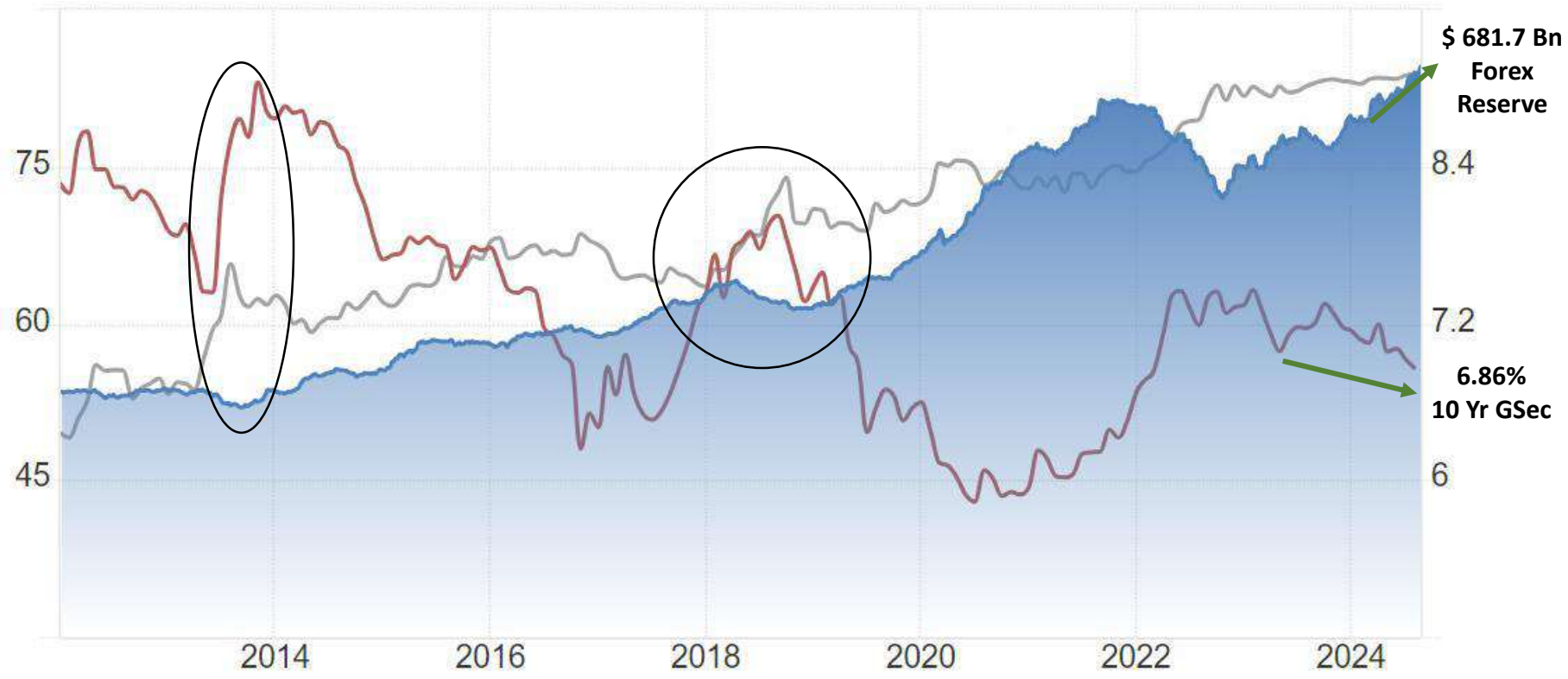
Disclaimer: The above graph is for informational purpose. Past performance may or may not be sustained in future.

India : Goldilocks phase – Forex Reserves, Exchange rate & 10 Year yield

Fragile Phase

Slowdown Phase

Goldilocks Phase



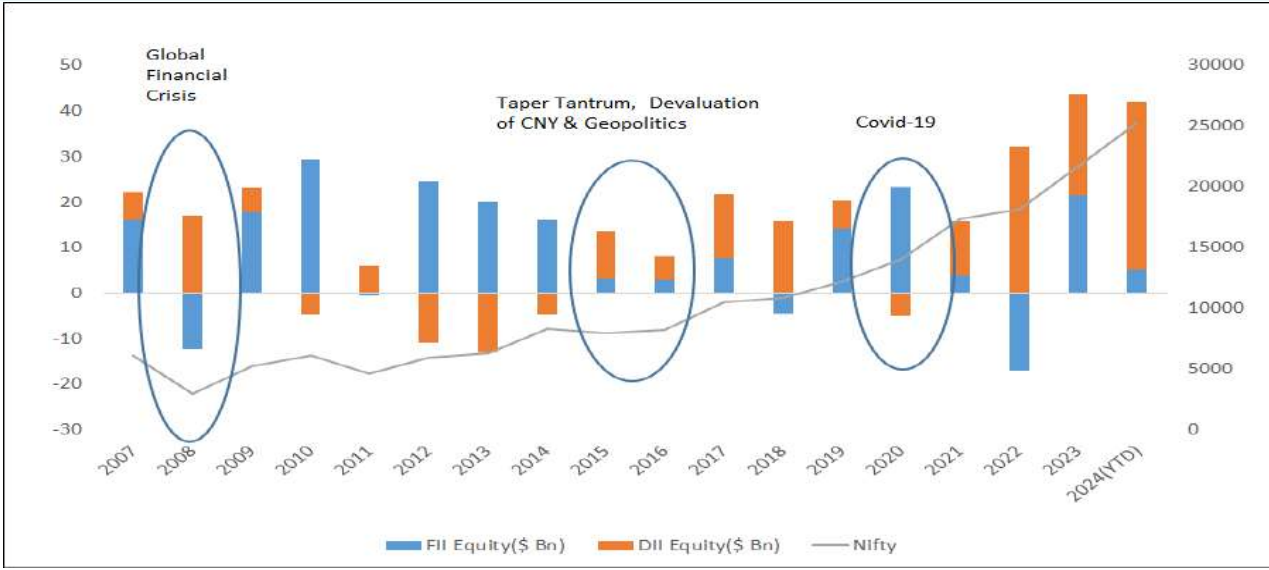
USDINR - US Dollar Indian Rupee
 India 10Y (%)
 India Foreign Exchange Reserves (USD Million)



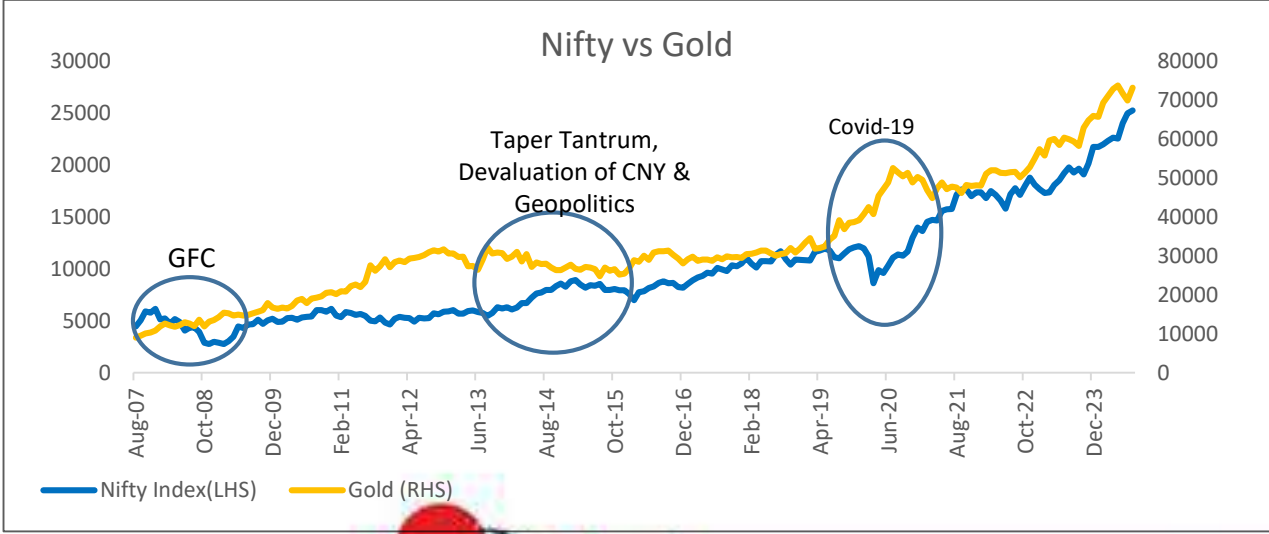
Source: MOWL, Trading Economics

Disclaimer: The above graph is for informational purpose. Past performance may or may not be sustained in future.

Global Events – DII leading flows, Gold can act as hedge



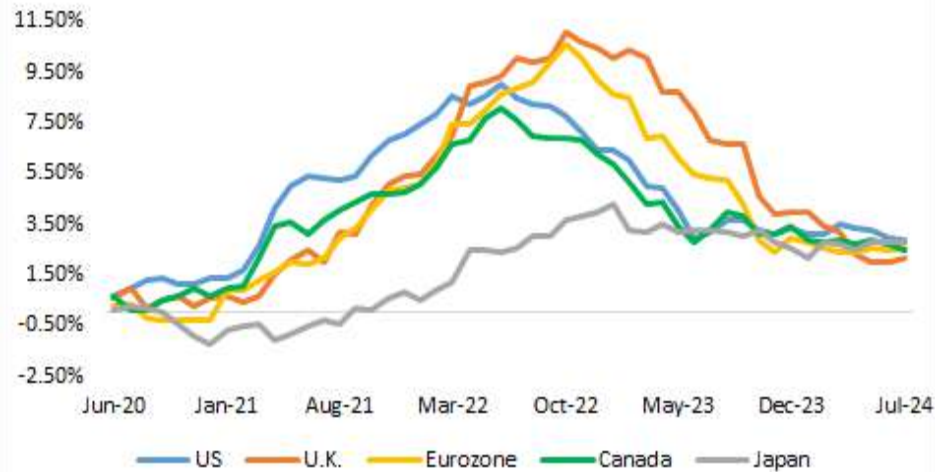
- In terms of flows coming into the equity market, DII have clearly dominated the FII post Covid.



- Gold can act as hedge to the overall portfolio during the times of heightened volatility

Inflation – Global & India CPI trending lower

CPI (YoY) Major Economies



CPI (YoY) India

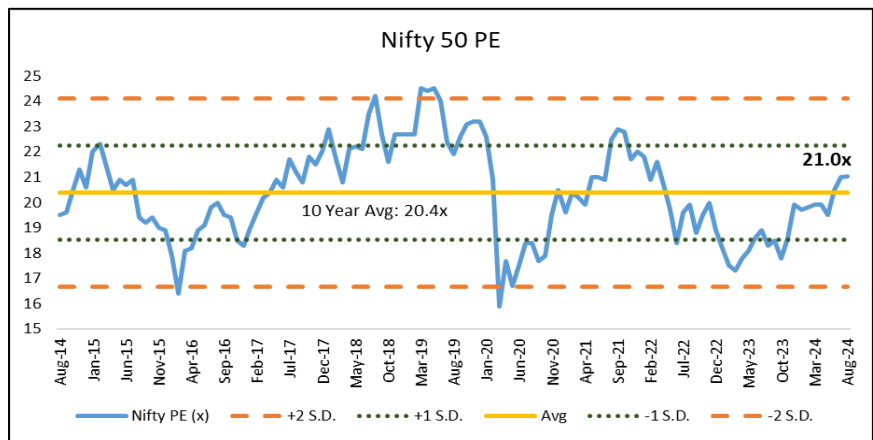


- The inflation in the major economies has been slowing down after the highs recorded in the mid of CY22
- Inflation in Japan has remained steady, prompting the BoJ to raise interest rates to record highs
- Inflation in India is at its lowest levels in the last 4 years mainly on the back of easing food inflation

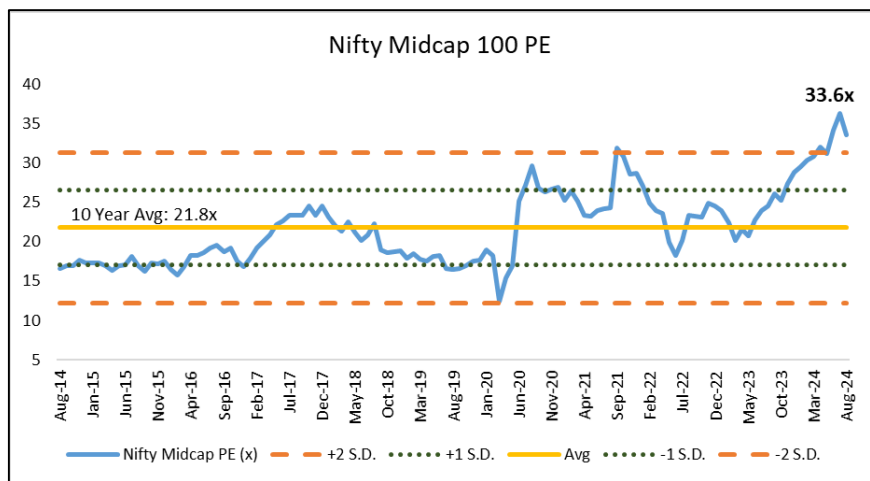


Valuations – Large Caps more attractive than Mid & Small Caps

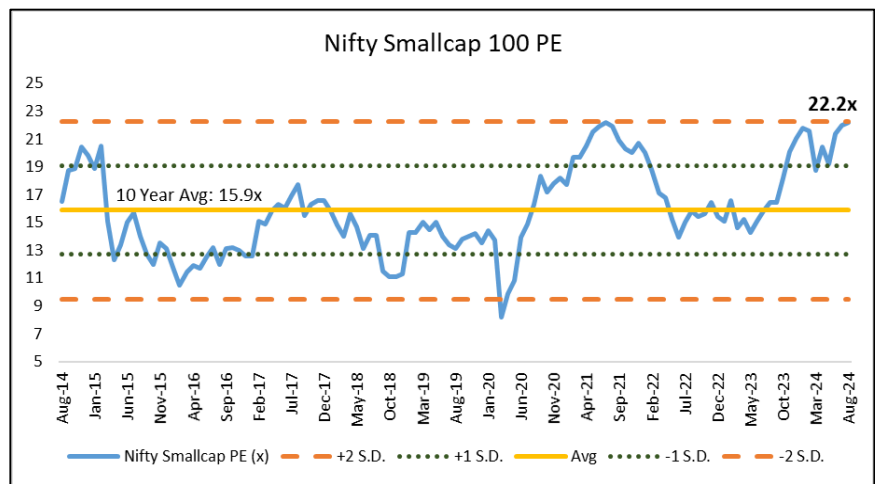
Nifty 50 PE 1 Year Forward - (10 Year Period)



Nifty Midcap 100 PE 1 Year Forward - (10 Year Period)



Nifty Smallcap 100 PE 1 Year Forward - (10 Year Period)



- Nifty Midcap forward PE & Nifty Smallcap forward PE are trading significantly higher & higher respectively compared to their respective long-term average.



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Mid & Small Caps expected to have higher earnings growth than Large Caps over next couple of years

Indices	Return on Equity			Estimated growth in EPS*	
	Aug'24	Aug'24 (Ex of BFSI and Oil & Petroleum)	Wt of BFSI and Oil & Petroleum	FY25E	FY26E
Large Cap	21.0%	24%	36.2%	7.7%	6.0%
Mid Cap	18.2%	18%	26.5%	23.2%	22.0%
Small Cap	16.4%	17%	16.3%	22.4%	7.4%

* Estimated earnings growth is taken from Bloomberg consensus estimates

Note 1: The stocks are bifurcated in terms of Large, Mid and Small basis average market capitalization available on AMFI website

Note 2: Motilal Oswal Nifty 500 Index Fund is considered as proxy to get the underlying constituents for Nifty 500

Note 3: Large Cap refers to top 100 companies, Mid Cap refers to 101 to 250th company and Small Cap refers to 251st to 500th company

Note 4: BFSI sector includes Banks, Finance and Capital markets

- The ROE profile seems to be decent across the market cap.
- Within Large Caps, the ROE profile improves after excluding BFSI and Oil & Petroleum sectors.





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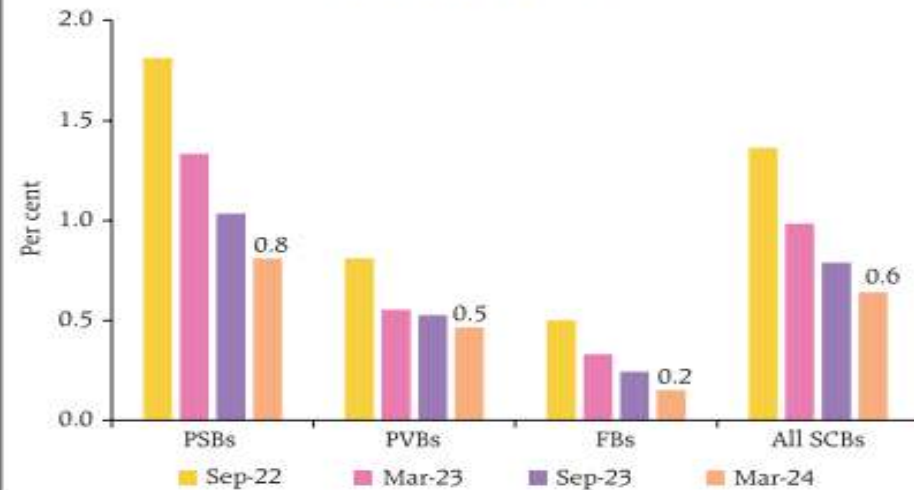
India Inc – Fundamental Strength

Gross Debt/Equity

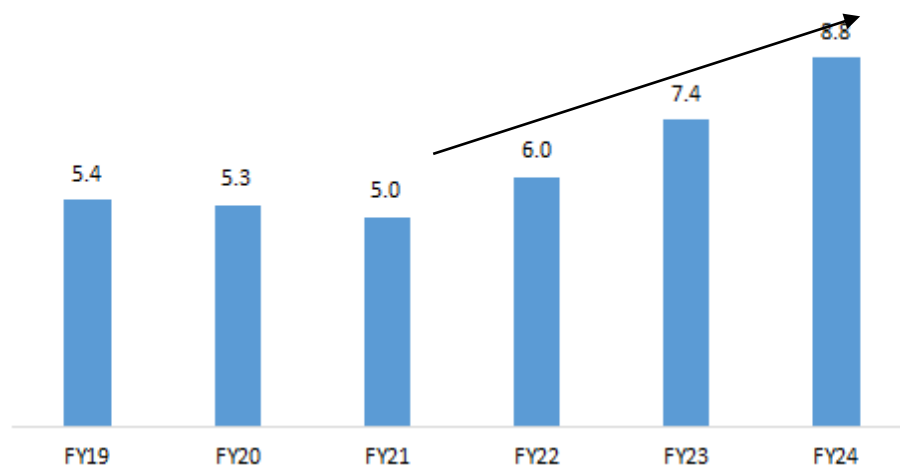


Source: Capitaline, I-Sec Research

b. SCBs' NNPA Ratio



Total Capex by Nifty 500 Companies (INR Tn)



Capital Expenditure – Trend and Capital Outlay going forward

MAJOR INDUSTRIES AND THEIR CAPEX PLANS

Huge Capex happening across different sectors in India



- Sectors like Power and Defence have a bulk of capex allocation going forward and basis that the stocks in these sectors have also been rewarded
- New age sectors like Semiconductors, Data centers and Electric Vehicles (covered under Auto industry and Auto Anc's) have sizeable capex plans.

Sector Rotation

2021	2022	2023	CYTD (Aug'24)
Metal 73.4%	PSU Bank 74.7%	Realty 82.0%	Oil & Gas 42.6%
IT 62.3%	Metal 25.3%	Auto 48.8%	Auto 41.6%
Realty 54.7%	FMCG 20.1%	Infra 40.1%	Pharma 38.8%
Cons Durables 46.7%	Oil & Gas 16.9%	Pharma 34.8%	Realty 34.9%
PSU Bank 44.8%	Auto 16.6%	PSU Bank 33.3%	Cons Durables 33.2%
Infra 37.8%	Fin Svcs 10.5%	FMCG 30.8%	Infra 29.9%
Oil & Gas 37.2%	Infra 7.5%	Nifty 500 26.9%	PSU Bank 23.2%
Nifty 500 31.6%	Nifty 500 4.2%	IT 26.3%	Nifty 500 23.1%
Auto 20.3%	Realty -10.5%	Cons Durables 23.7%	IT 22.2%
Fin Svcs 14.6%	Pharma -10.7%	Metal 19.1%	Metal 18.3%
FMCG 12.4%	Cons Durables -12.7%	Fin Svcs 14.3%	FMCG 12.4%
Pharma 10.9%	IT -24.5%	Oil & Gas 13.1%	Fin Svcs 11.1%

- Considering the last 4 years (including CYTD'24), the sector rotation has been visible, different sectors being the top performers across different years.
- With the current scenario of rich valuations and heightened volatility sector rotation is expected to continue and be more prominent going forward.

Note: Total Return Index values considered. Fin Svcs: Financial Services, Cons Durables: Consumer Durables



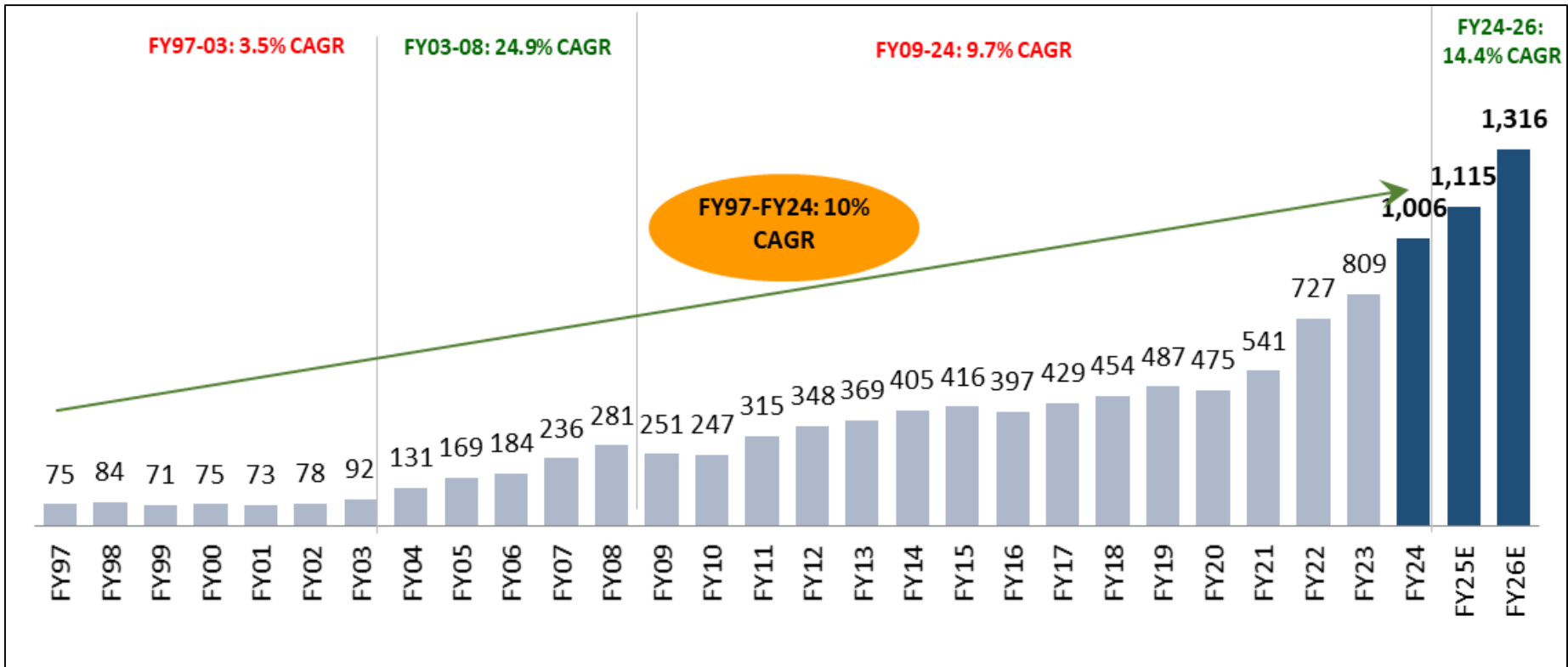
Nifty 50 – Sectorwise Earnings Growth

Sector	PAT (INR b)						Growth YoY (%)					
	FY21	FY22	FY23	FY24	FY25E	FY26E	FY21	FY22	FY23	FY24	FY25E	FY26E
Automobiles	179	76	289	624	678	793	74	-57	278	116	9	17
BFSI	1,044	1,433	2,026	2,541	2,894	3,381	25	37	41	25	14	17
Capital Goods	68	84	104	130	145	187	-23	24	24	25	12	29
Cement	100	130	115	134	135	168	0	31	-11	16	1	24
Consumer	292	319	386	438	460	511	1	9	21	13	5	11
Healthcare	129	172	181	220	259	301	38	33	6	21	18	16
Logistics	45	59	77	89	111	132	-10	30	30	16	24	19
Metals	344	926	540	599	777	923	45	169	-42	11	30	19
Oil & Gas	776	1,107	1,089	1,550	1,497	1,804	20	43	-2	42	-3	21
Retail	10	23	33	35	41	51	-35	138	40	7	17	24
Technology	836	958	1,022	1,055	1,165	1,316	7	15	7	3	10	13
Telecom	-7	35	82	113	181	309	Loss	Loss	LP	39	60	71
Utilities	271	303	310	369	381	419	21	12	3	19	3	10
Others	11	8	27	35	43	43	15	-29	249	29	22	0
Nifty	4,098	5,634	6,281	7,931	8,768	10,340	19	38	11	26	11	18

- BFSI and Metals to drive FY25E earnings for the Nifty 50



Nifty 50 - Earnings Growth Outlook

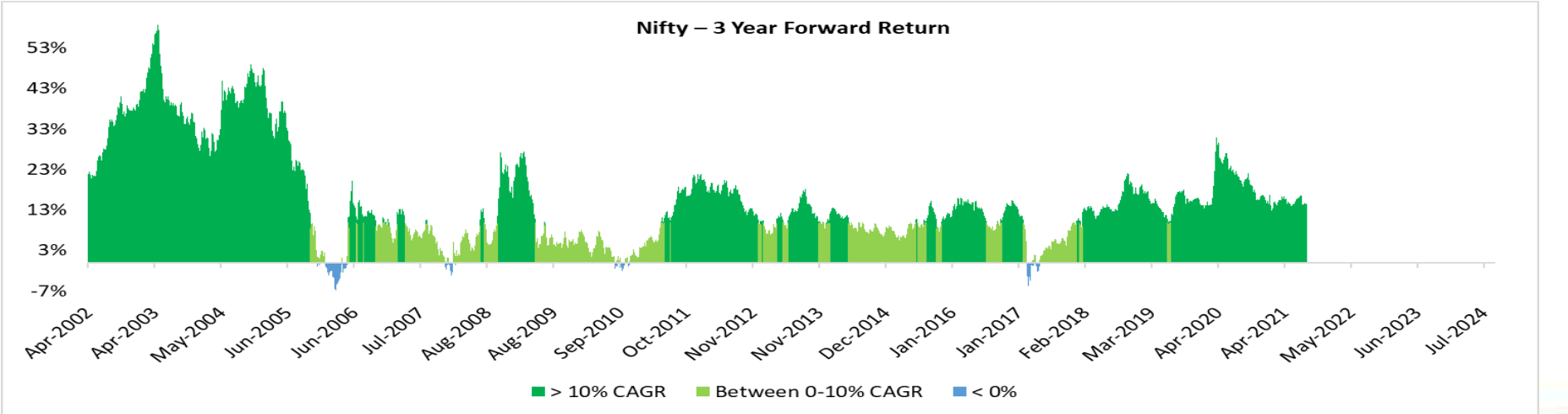


- Nifty EPS is estimated at INR 1,115/INR 1,316. Nifty EPS is expected to grow 11% and 18% in FY25 and FY26, respectively



Temperature Gauge Index

- Temperature Gauge Index is an equally weighted index of EY-BY and MOVI Index
- It incorporates PE Ratio, PB Ratio, Div. Yield and G-sec Yield, and hence is a useful valuation metric.



Data as on 3rd September'24

Source: Capital Line, Bloomberg Internal Research

Disclaimer: The above graph is for informational purpose. Past performance may or may not be sustained in future.

Temperature Gauge Index – Sensitivity Analysis

Temperature Gauge Index - Sensitivity Analysis					
Nifty50/10 Yr Gsec	6.58%	6.78%	6.98%	7.18%	7.38%
24000	113	114	115	116	117
24250	114	115	116	117	118
24500	114	115	116	117	118
24750	114	116	117	118	119
25000	115	116	117	118	119
25250	115	116	117	118	119
25500	116	117	118	119	120
25750	116	117	118	119	120
26000	116	117	118	119	120
26250	117	118	119	120	121
26500	117	118	119	120	121
26750	117	118	119	121	122
27000	118	119	120	121	122

Pink cell Indicates Current Level of Nifty 50 and 10 yr G-sec levels. Data as on 3rd September'24



3 Yr Forward Returns Of Nifty At Different Levels Of Temperature Gauge Index

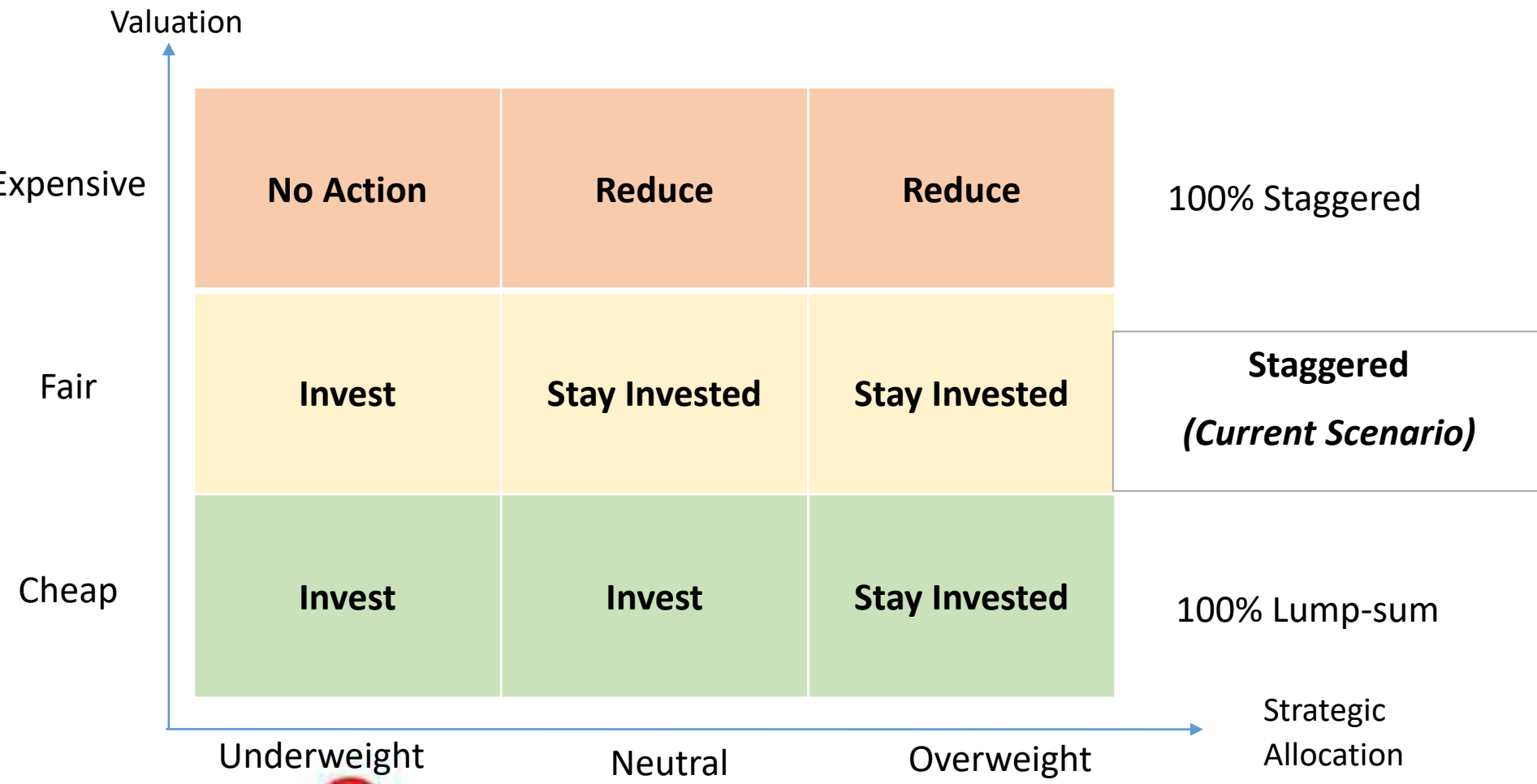
Nifty 50		No. of Observations	% of Observations	3 Yr Return CAGR			% Times in CAGR range		
Index in Range	Index in Range			Min	Max	Average	% Times Positive	6% to 10%	>=10%
65	70	60	1%	24%	57%	43%	100.0%	0%	100%
70	75	202	2%	15%	51%	32%	100.0%	0%	100%
75	80	285	3%	14%	45%	37%	100.0%	0%	100%
80	85	168	2%	15%	43%	34%	100.0%	0%	100%
85	90	207	3%	12%	49%	33%	100.0%	0%	100%
90	95	539	7%	2%	47%	27%	100.0%	2%	97%
95	100	832	10%	1%	44%	18%	100.0%	8%	91%
100	105	714	9%	-2%	30%	13%	98.7%	20%	71%
105	110	810	10%	-4%	22%	10%	83.1%	15%	56%
110	115	1797	22%	-7%	22%	9%	64.5%	28%	22%
115	120	1579	19%	-4%	21%	8%	74.1%	21%	23%
120	125	804	10%	-2%	18%	9%	83.2%	7%	55%
125	130	135	2%	0%	16%	12%	88.1%	4%	69%
130	135	84	1%	-2%	15%	6%	91.7%	0%	36%
135	140	28	0%	-3%	0%	-1%	10.7%	0%	0%

Data as on 3rd September'24



Equity Allocation & Deployment Grid

➤ Below grid is based on Temperature Gauge Index



- The equity outlook remains positive given robust economic growth, strong flows and capex spending. The expected rate-cut cycle will also add further impetus to the economy. The ongoing global events and the approaching U.S. elections may heighten the volatility in the short term.
- From a valuation perspective, large-cap stocks seem to be fairly valued, while mid- and small-cap stocks are currently trading at higher valuations. However, the expected earnings growth over the next two years remains robust for mid- and small-cap segments.
- If Equity allocation is lower than desired levels, investors can increase allocation by implementing a staggered investment strategy **over 3 to 6 months for large & multi cap strategies** and **6 to 12 months for select mid & small-cap strategies** with accelerated deployment in the event of a meaningful correction.





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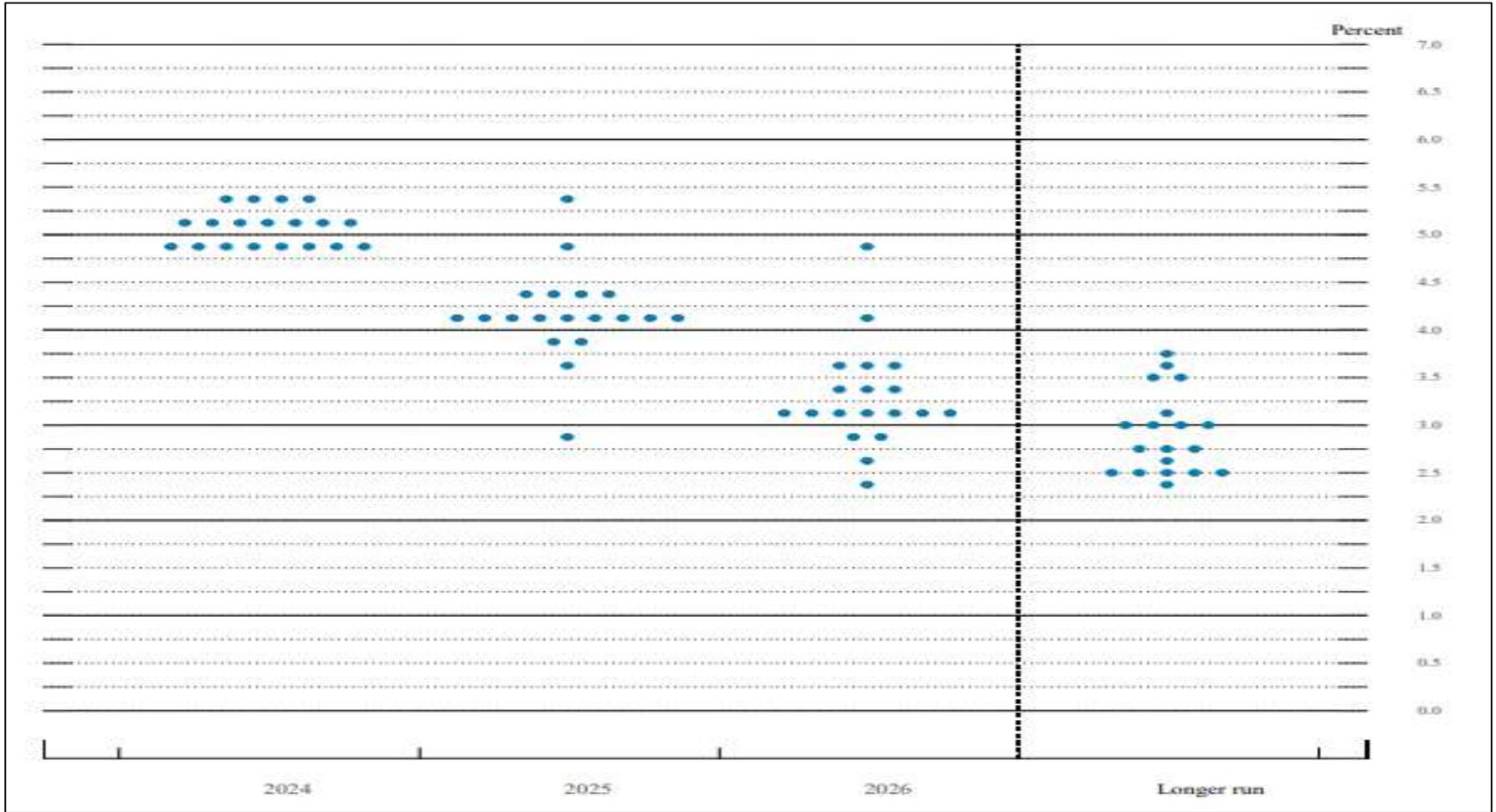
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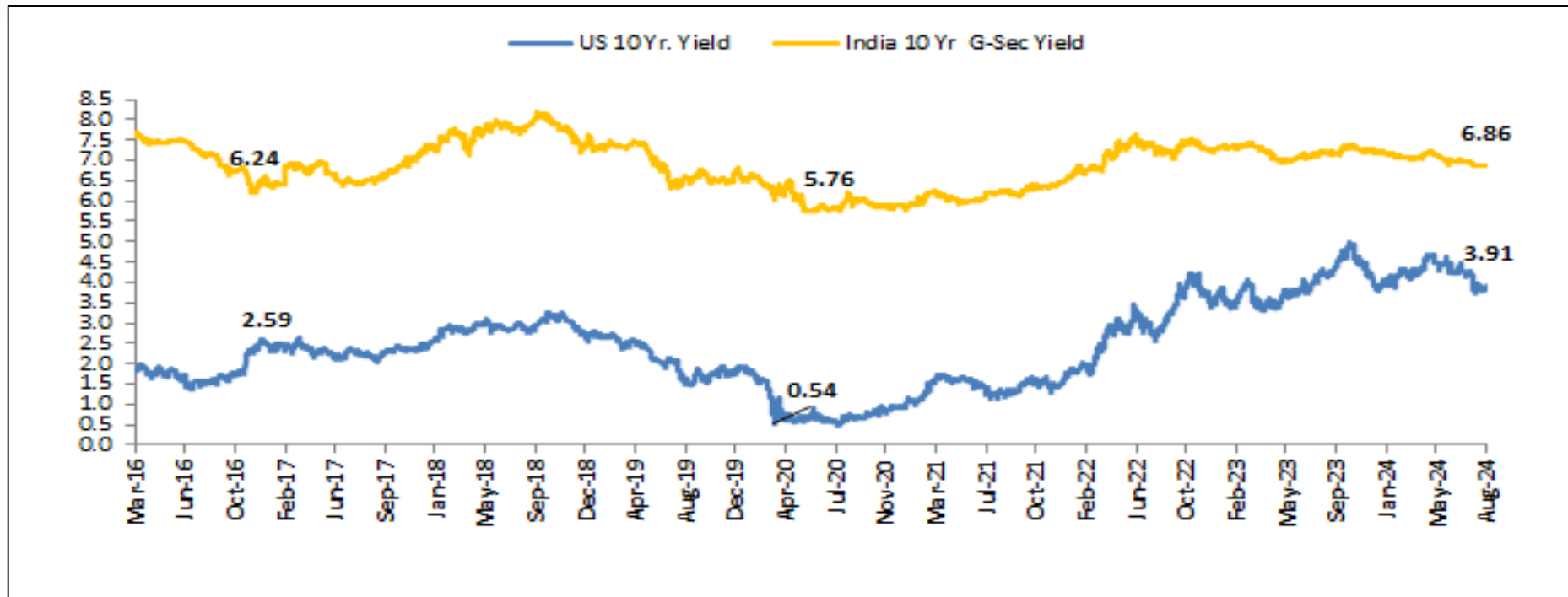
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US Fed projections for Interest Rates

**Federal Policy Rate Median Projection:
5.1% by 2024; 4.1% by 2025, 3.1% by 2026**



US & India 10 Yr G-Sec Curve

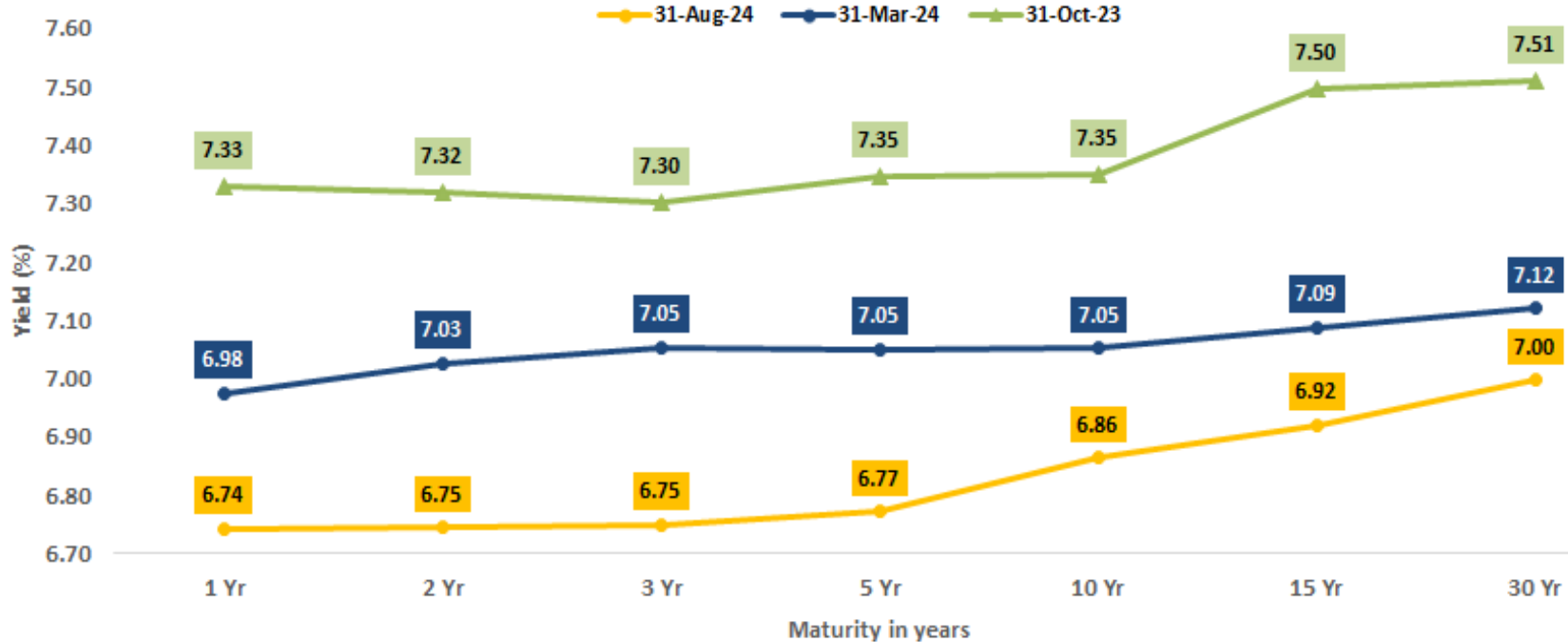


- U.S. 10-Year yield softened to around 3.91% after FED indicated reducing interest rates in Sep'2024.
- Healthy U.S. retail sales data, smaller-than-expected rise in weekly unemployment claims and an easing inflation print provided solace.
- India bond yields continue to be guided by liquidity conditions, moves in global benchmarks, with strong domestic demand supply conditions.



Movement in India's G-Sec Yield Curve

Movement in G - Sec Yields Across Maturities

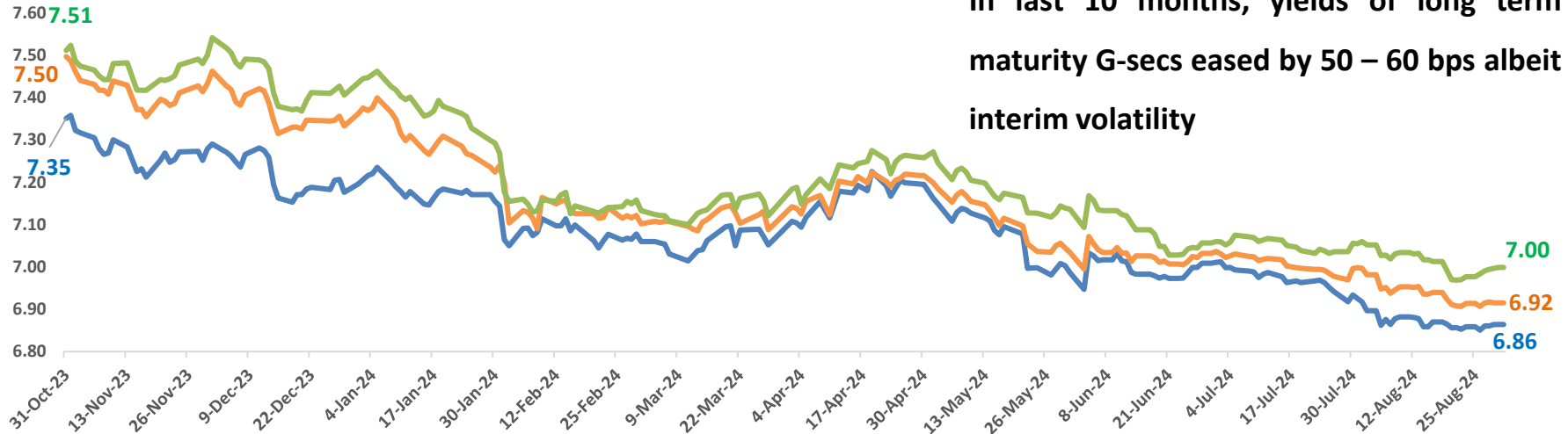


- ✓ Yields curve has shifted downwards and is gradually moving from a flat to a bull steepening on back of favourable demand supply dynamics and well-contained inflation
- ✓ **The short term yields are softening more than long term yields leading to increase in term spreads**



Movement in Long Maturity G Secs

— 10 Yr Gsec — 15 Yr Gsec — 30 Yr Gsec



Positive Factors :

- ✓ Stable Domestic Macros
- ✓ Inclusion of Bonds in Global Indices
- ✓ Change in India's Sovereign Outlook
- ✓ Lower Gross Borrowings
- ✓ Path to Fiscal Consolidation

Downside Risks :

- ✓ Mixed Global macro signals
- ✓ Divergent Global Central Bank Policies
- ✓ Rising Geopolitical tension

Reiteration of our View :

- ✓ Duration bias in the fixed income portfolio so as to capitalize on the likely softening of yields in the next 1-2 years

Scenario Analysis for Investment in G –Sec MF

								Post Tax Absolute		
								39%	25%	17%
Net YTM	Yield movement over next 1-3 Yrs (A)	Probability	Avg Maturity (Yrs)	Modified Duration (Yrs) (B)	Capital Gain/Loss (A*B)	Accrual (Z)	Total pre tax return Z+(A*B)	Total post tax return (Individuals @39%)	Total post tax return (Corporates @25%)	Total post tax return (MAT Corporates @17%)
6.86%	0.50%	Low	10.00	6.77	-3.4%	6.86%	3.48%	2.12%	2.61%	2.88%
6.86%	0.00%		10.00	6.77	0.0%	6.86%	6.86%	4.18%	5.15%	5.69%
6.86%	-0.50%	Reasonable	10.00	6.77	3.4%	6.86%	10.25%	6.25%	7.68%	8.50%
6.86%	-0.75%		10.00	6.77	5.1%	6.86%	11.94%	7.28%	8.95%	9.91%



We reiterate our view to have a duration bias in the fixed income portfolio so as to capitalize on the likely softening of yields in the next 1-2 years

- **30% of the portfolio may be invested in**
 - Actively managed duration funds to capitalize on evolving fixed income scenario
 - For passive duration allocation, one may invest in long term maturity G-sec papers to benefit from accrual income and potential MTM gains
- **30% - 35% of the portfolio shall be allocated to Multi Asset Allocation funds & Equity Savings Funds**
 - These funds aim to generate enhanced returns than traditional fixed income with moderate volatility through a combination of Domestic Equity, Arbitrage, Fixed income, International Equity, Gold & other Commodities
- **To improve the overall portfolio yield, 30% – 35% of the overall fixed income portfolio** can be allocated to Private Credit strategies, REITs/InvITs & select high yield NCDs
- **For liquidity management**, investments can be made in Floating Rate (9 to 12 months) & Arbitrage Funds (3 to 6 months)





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Gold and Silver takes breather after sharp rally this year



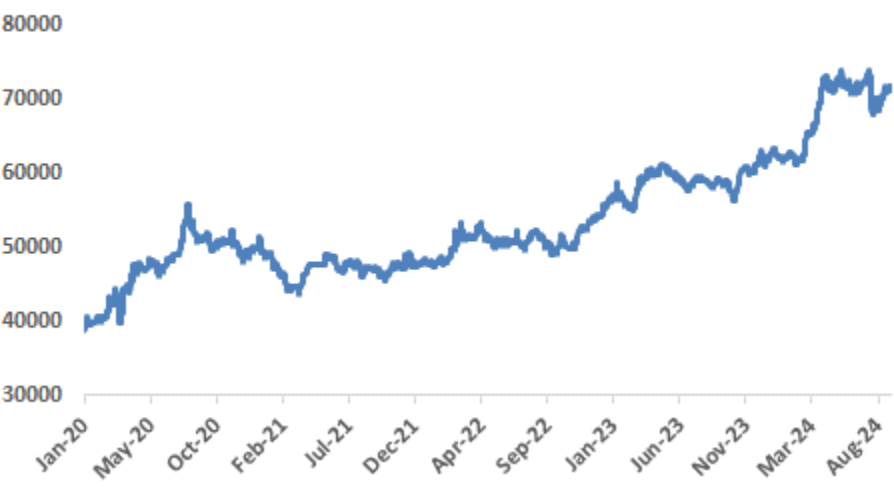
Source : Reuters

- In August, Gold rose over 2%, while Silver traded volatile in a broad range
- Major factors triggering volatility last month : Fed Rate cut expectations, Escalating geopolitical tensions and economic data points
- Domestic Gold prices did see some recovery post 9% duty cut, momentum is still lacking.

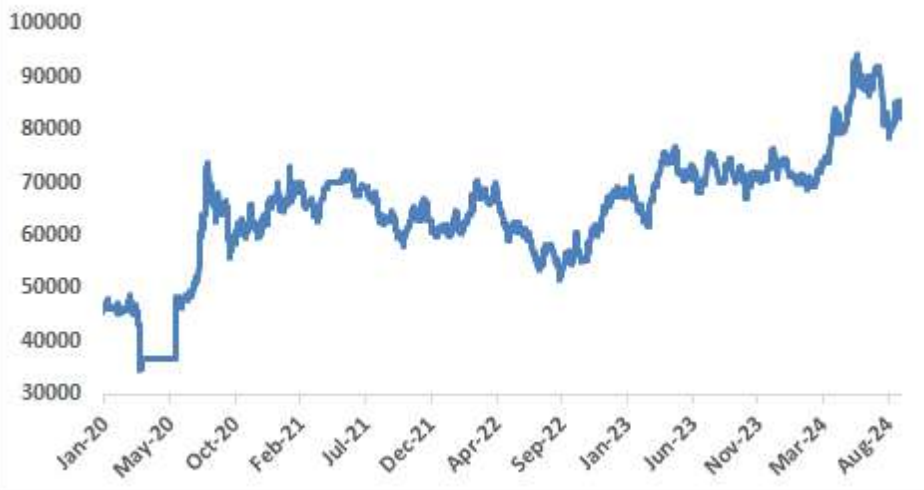


Gold & Silver – Historical Performance

MCX Gold Spot (INR/10 gm)



MCX Silver Spot (INR/Kg)



Particulars	Absolute Returns (%)				CAGR (%)	
	1 month	3 months	6 months	1 year	3 year	5 year
MCX Gold Spot (Rs)	1.5%	-0.5%	13.9%	20.1%	14.8%	12.8%
MCX Silver Spot (Rs)	-1.6%	-8.9%	17.5%	9.9%	9.1%	11.3%

Data as on 3rd September '24

Source: Bloomberg; Internal Research

Disclaimer: The above graph/data is for informational purpose. Past performance may or may not be sustained in future.



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