FIRST LIGHT

01 December 2022

RESEARCH

INDIA STRATEGY | MONTHLY WRAP

Market at all-time high but outlook mixed

BOB ECONOMICS RESEARCH | GDP

GDP growth slows to 6.3% in Q2FY23

Daily macro indicators

Indicator	28-Nov	29-Nov	Chg (%)
US 10Y yield (%)	3.68	3.74	6bps
India 10Y yield (%)	7.27	7.28	1bps
USD/INR	81.67	81.73	(0.1)
Brent Crude (US$/bbl)	83.2	83.0	(0.2)
Dow	33,849	33,853	0.0
Hang Seng	17,298	18,205	5.2
Sensex	62,505	62,682	0.3
India FII (US$ mn)	**25-Nov**	**28-Nov**	**Chg ($ mn)**
FII-D	45.0	28.2	(16.8)
FII-E	87.6	319.9	232.3

Source: Bank of Baroda Economics Research

SUMMARY

INDIA STRATEGY | MONTHLY WRAP

- Nifty 50 outperformed US and Japan benchmark indices in November while underperforming the EU
- India remains the priciest market with Nifty 12M forward P/E approaching 1SD above its 5Y mean
- Market faces upside risk to valuation multiple if US rate hike trajectory eases but downside risk to earnings from slowdowns in China and EU

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INDIA ECONOMICS: GDP

On the back of base effect, India's GDP growth moderated to 6.3% in Q2FY23 (13.5% in Q1). Government consumption contracted, while exports and investment disappointed. Manufacturing growth contracted sharply signaling concerns. Services sector also registered a dip. However, H2FY23 holds key for revival. Even as global economy is under evident threat of slow down owing to ongoing geo-political conflict, aggressive monetary tightening by global central banks and stubbornly high inflation. India's economy is growing at a steady pace on the back of strong fundamentals and as reflected by high frequency indicators. With this, we retain our forecast of Indian economy growing by 6.8% in FY23 with a downward bias with ever evolving landscape.

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BOBCAPS Research
research@bobcaps.in

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MONTHLY WRAP | Volume #10 | 30 November 2022

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- **Nifty 50 outperformed US and Japan benchmark indices in November while underperforming the EU**
- **India remains the priciest market with Nifty 12M forward P/E approaching 1SD above its 5Y mean**
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Kumar Manish | Aseem Madan
research@bobcaps.in

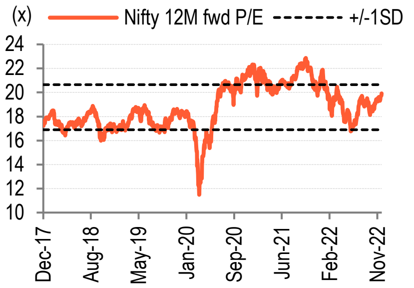
Nifty up 4.1% in November: The Nifty 50 index underperformed European stocks but outperformed the US and Japan benchmarks in November. Sector-wise, PSU banks (15.6%) continued to rally. The metal index climbed 11.3% and IT index 5.8%. Nifty Commodities was up 5.1% and Services 3.9%.

Raw material cost softens in Q2 but other opex still high: According to the Centre for Monitoring Indian Economy (CMIE), 4,000+ companies have reported earnings for the September-ending quarter. Aggregate income grew 25% YoY while profit dipped 2.9%. Amongst Nifty 200 companies, 41% beat consensus at the PAT level (40% in Q1) and 44% missed estimates (42% in Q1). Operating cost pressures declined this quarter as cost of raw materials, finished goods and freight all moderated. Interest expense rose but was modest by historical standards. Salary, wage and power costs stayed elevated. For details, see our Q2FY23 Review: Raw material costs cool off.

Outlook mixed: On the domestic front, we see a robust demand climate but a delayed capex cycle. Globally, we anticipate a slower rate of Fed hikes coupled with downturns in Europe and China, which will have a mixed impact on Indian markets over the next 1-2 years. We expect only a gradual pickup in India's capex given limited near-term triggers. Even so, we remain highly positive on sustained growth momentum over the longer term as the necessary building blocks spanning education, demographics, health, infrastructure, digitisation and financial inclusion are all in place (see our note of Jan'22: India at take-off point).

Investment view: While slower Fed hikes pose an upside risk to valuation multiples and could spur a brief rally in cyclicals, weakness in China and Europe represent downside risks to earnings for Indian equities and do not augur well for a sustained rally. Therefore, while cyclicals will likely outperform near term, we continue to advocate a conservative investment approach until the capex cycle gathers pace.

Nifty valuations now reapproaching +1SD above 5Y avg.



Source: Bloomberg, BOBCAPS Research

GDP

30 November 2022

GDP growth slows to 6.3% in Q2FY23

Jahnavi Prabhakar
Economist

On the back of base effect, India's GDP growth moderated to 6.3% in Q2FY23 (13.5% in Q1). Government consumption contracted, while exports and investment disappointed. Manufacturing growth contracted sharply signaling concerns. Services sector also registered a dip. However, H2FY23 holds key for revival. Even as global economy is under evident threat of slow down owing to ongoing geo-political conflict, aggressive monetary tightening by global central banks and stubbornly high inflation. India's economy is growing at a steady pace on the back of strong fundamentals and as reflected by high frequency indicators. With this, we retain our forecast of Indian economy growing by 6.8% in FY23 with a downward bias with ever evolving landscape.

Q2FY23 GDP

GDP growth moderated by 6.3% in Q2FY23 against an increase of 13.5% in Q1 on a YoY basis. This was marginally lower than our expectation of 6.5%. The moderation was largely owing to base effect. The dip was visible in private consumption which dropped down by 9.7% in Q2 (after clocking double digit growth of 25.9% in Q1). Growth in investment demand also eased by 10.4% in Q2 after increasing by 20.1% in Q1FY23. Exports too joined the bandwagon with growth slipping by 11.5% in Q2 against an increase of 14.7% in Q1FY23. Adding to the pain, government consumption declined sharply by (-) 4.4% after increasing by 1.3% in Q1.

GVA dragged down lower

GVA growth was back in single digits at 5.6% for Q2FY23 compared with double digit growth clocked of 12.7% registered in Q1FY23. Growth in manufacturing sector disappointed the most as it contracted by (-) 4.3% against an increase of 4.8% in Q1FY23, the same has been reflected by industrial production. Electricity and construction sector also registered much slower growth of 5.6% and 6.6% respectively in Q2FY23. Within the services sector, growth in trade, hotel (14.7% versus 25.7% in Q1FY23) and financial services (7.2% versus 9.2% in Q1FY23) slowed down in Q2FY23. Growth for public admin and defence also moderated sharply by 6.5% in Q2 (against 26.3% in Q1FY23). However, the only source of light was reflected by agriculture with growth improving by 4.6% from 4.5% in Q1FY23. Though same needs to be seen with caution as pace of rabi sowing needs to monitored.

Outlook for FY23

Against the backdrop of geopolitical conflict in the beginning of H1FY23, higher commodity prices, accelerating inflation and global rate tightening cycle, India's GDP has grown by 9.7% in the first half of H1FY23. The economy is expected to do much better in H2FY23 as inflation is expected to moderate and other high frequency indicators (buoyant GST collection, soaring credit growth, PMI, etc) signal recovery in the latter half. We expect the economy to grow by 6.8% for FY23 with a downward bias even as the global economy slows down.

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BUY – Expected return >+15%

HOLD – Expected return from -6% to +15%

SELL – Expected return <-6%

Note: Recommendation structure changed with effect from 21 June 2021

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