FIRST LIGHT

05 October 2020

RESEARCH

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Exports gain traction

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Protracted bear market yet to run its course

Automobiles
Sep'20 Auto Sales: Upward trajectory continues

SUMMARY

India Economics: Trade

India's trade deficit fell to US$ 2.9bn in Sep'20 from US$ 6.8bn in Aug'20 as exports rose by 5.3%, first time in 6-months. Pharma exports increased the most at 24.4%. Imports too are recovering led by non-oil-non-gold imports which fell by 13.3% in Sep'20 compared with a fall of 29.6% in Aug'20. Imports will pick-up gradually, in sync with domestic demand because of which current account surplus is estimated at US$ 39bn (1.5% of GDP) in FY21. We continue to remain positive on INR.

Click here for the full report.

Market Strategy: Model Portfolio

The recent rally across mid- and small-caps is yet to bring about a reversal of the long-term bearish trends that began in Jan'18. Performance of these indices continues to diverge from that of large-cap indices, though we do note a common thread of outperformance among pharma, chemical and IT companies across market cap. The worsening economic fundamentals will continue to have a bearing on corporate financials. Both our model portfolios (large & midcap) have outpaced their benchmarks by ~1% and ~4% respectively.

Click here for the full report.

TOP PICKS

LARGE-CAP IDEAS

Company	Rating	Target
Bajaj Finance	Buy	4,000
Cipla	Buy	850
GAIL	Buy	155
Petronet LNG	Buy	310
Tech Mahindra	Buy	910

MID-CAP IDEAS

Company	Rating	Target
Alkem Labs	Buy	3,600
Chola Investment	Buy	280
Laurus Labs	Buy	1,200
Transport Corp	Buy	270
Mahanagar Gas	Sell	750

Source: BOBCAPS Research

DAILY MACRO INDICATORS

Indicator	Current	2D (%)	1M (%)	12M (%)
US 10Y yield (%)	0.68	3bps	(4bps)	(92bps)
India 10Y yield (%)	6.01	(3bps)	(13bps)	(69bps)
USD/INR	73.76	0.1	(0.5)	(4.1)
Brent Crude (US$/bbl)	40.95	(0.2)	(9.1)	(29.0)
Dow	27,782	1.2	(3.0)	6.5
Shanghai	3,218	(0.2)	(5.5)	10.8
Sensex	38,068	0.2	(3.5)	(1.6)
India FII (US$ mn)	**29 Sep**	**MTD**	**CYTD**	**FYTD**
FII-D	(14.7)	569.4	(14,520.6)	(4,761.1)
FII-E	(144.3)	(731.3)	4,076.0	10,679.0

Source: Bank of Baroda Economics Research

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Automobiles

Auto sales continued their upward trajectory, improving MoM in September. Easing of lockdowns, a gradual increase in production capacities and filling of channel inventory were key reasons for growth. MSIL's domestic PV sales surged 32% YoY while 2W players saw volumes rise supported by healthy exports. MHCV volumes continued to be the worst affected, declining 23%/26% YoY for AL/TTMT. Tractor sales remained resilient owing to healthy rural sentiment, growing at 17%/9% YoY for MM/ESC.

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TRADE

03 October 2020

Exports gain traction

India's trade deficit fell to US$ 2.9bn in Sep'20 from US$ 6.8bn in Aug'20 as exports rose by 5.3%, first time in 6-months. Pharma exports increased the most at 24.4%. Imports too are recovering led by non-oil-non-gold imports which fell by 13.3% in Sep'20 compared with a fall of 29.6% in Aug'20. Imports will pick-up gradually, in sync with domestic demand because of which current account surplus is estimated at US$ 39bn (1.5% of GDP) in FY21. We continue to remain positive on INR.

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Export growth picks up: As per preliminary data, India's exports rose for the first time in 6-months by 5.3% in Sep'20 compared with a 12.7% decline in Aug'20. Drugs and pharmaceutical exports rose by 24.4% (17.3% in Aug'20). Exports of engineering goods also picked up to 3.7% (decline of 7.7% in Aug'20). In Q2, exports are down by 5.7% compared with 36.2% decline seen in Q1FY21. We expect exports to show a steady improvement led by a recovery in global demand.

Imports also improve: Imports too showed a steady improvement and contracted by only 19.6% in Sep'20 compared with a decline of 26% in Aug'20. The improvement was led by non-oil-non-gold imports which contracted at a slower pace of 13.3% in Sep'20 versus a dip of 29.6% in Aug'20. Within this, imports of electronic items picked up to 3.5% (decline of 11.7% in Aug'20). Contraction in oil imports also eased to 35.9% versus 41.6% decline in Aug'20. Gold imports rose at a slower pace of 110.9% versus 171.3% in Aug'20. Gold prices were lower by 2.4% on a MoM basis.

Favorable outlook: India's trade deficit narrowed to US$ 2.9bn in Sep'20 from US$ 6.8bn in Aug'20. While the trade deficit in Q2FY21 at US$ 14.5bn is higher than in Q1 (US$ 9bn), it is considerably lower compared with Q2FY20 at US$ 39.7bn. Overall pickup in economic activity is visible with high frequency indicators such as manufacturing PMI (highest since Jan'12 at 56.8 in Sep'20 from 52 in Aug'20), improvement in electricity demand (2.5% in Sep'20 from a decline of 4.2% in Aug'20), e-way bills (contraction of 3.5% in Aug'20 against 7.3% in Jul'20) and GST collections of Rs 955bn (3.9% higher over last year). As a result, domestic demand is also expected to improve because of which trade deficit is estimated at US$ 75bn in FY21 as against US$ 24bn in H1FY21.

KEY HIGHLIGHTS

- Exports rose by 5.3% in Sep'20 versus a decline of 12.7% in Aug'20.
- Imports contract by 19.6% versus 26% decline in Aug'20.
- Trade deficit narrows to US$ 2.9bn from US$ 6.8bn in Aug'20.

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MODEL PORTFOLIO

01 October 2020

Protracted bear market yet to run its course

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The recent rally across mid- and small-caps is yet to bring about a reversal of the long-term bearish trends that began in Jan'18. Performance of these indices continues to diverge from that of large-cap indices, though we do note a common thread of outperformance among pharma, chemical and IT companies across market cap. The worsening economic fundamentals will continue to have a bearing on corporate financials. Both our model portfolios (large & midcap) have outpaced their benchmarks by ~1% and ~4% respectively.

Bearish undertone continues despite recent respite: As India's GDP growth outlook falters, earnings visibility remains murky across sectors. The financial sector has been the biggest laggard and expectedly so, as GDP contraction aggravates NPA risk. That said, pharma, chemicals and IT have rerated swiftly, with average earnings multiples improving by 50-100% since Apr'20. Auto (especially OEMs) has also rerated, driven by robust Aug'20 PV sales and sustained traction in tractor sales.

Downside risk to FY22 earnings: The Nifty is currently trading at ~17x FY22E EPS (after rerating from ~14x in May'20), while the Midcap 50 (M50) is at ~15x FY22E EPS. We expect earnings growth to resume from FY22 (after declines of 10%/17% for Nifty/M50 in FY21E), but see downside risk to consensus estimates as economic indicators worsen.

Deleveraged companies shine: As envisaged, pandemic uncertainty has lent **cash-rich companies a clear advantage**, visible in outperformance of the pharma, chemical and IT sectors (supported by earnings upgrades after Q1FY21). Energy and telecom are yet to catch up as macro concerns over regulations and economic recovery weigh heavy. Financials, consumer and industrials face emerging earnings downgrade risks stemming from pandemic unknowns.

Brace for risk-off trade: Though valuations for cyclicals (especially in energy) look undemanding given expectations of a V-shaped demand recovery, the uncertainty surrounding Covid-19 continues to dampen projections. Factoring in upcoming presidential elections in the US and stretched global balance sheets, we maintain our overweight stance on sectors that offer strong earnings visibility – pharma, agrochemicals and IT. Financials and auto (mostly OEMs) remain our primary underweights.

BMP: TOP IDEAS

TOP 5 Overweight	TOP 5 Underweight
HCL Tech	Reliance Industries
Petronet LNG	Bajaj Auto
ICICI Bank	SBI
Maruti	Wipro
Tech Mahindra	Sun Pharma

Source: BOBCAPS Research

BMP-M50: TOP IDEAS

TOP 5 Overweight	TOP 5 Underweight
PI Industries	Ashok Leyland
L&T Infotech	TVS Motor
Gujarat State Petronet	Mahanagar Gas
Alembic Pharma	Escorts
Laurus Labs	RBL

Source: BOBCAPS Research

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AUTOMOBILES

01 October 2020

Sep'20 Auto Sales: Upward trajectory continues

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Auto sales continued their upward trajectory, improving MoM in September. Easing of lockdowns, a gradual increase in production capacities and filling of channel inventory were key reasons for growth. MSIL's domestic PV sales surged 32% YoY while 2W players saw volumes rise supported by healthy exports. MHCV volumes continued to be the worst affected, declining 23%/26% YoY for AL/TTMT. Tractor sales remained resilient owing to healthy rural sentiment, growing at 17%/9% YoY for MM/ESC.

PV sales rise: Domestic sales for Maruti (MSIL) increased 32% YoY to 152.6k units in Sep'20 while exports rose 9% YoY, albeit on a soft base. The company's mini/compact segments outperformed other categories, rising 36%/48% YoY. For H1FY21, MSIL posted a drop of 37% YoY. PV sales for M&M (MM) and Hyundai Motors were up 4% YoY each, while Tata Motors (TTMT) reported a 160% jump for Sep'20. We believe the latter could be attributed to channel filling ahead of the festive season and expanding OEM production capacities.

2W sales healthy: Hero's (HMCL) wholesale volumes rose 17% YoY to 715k in Sep'20, with motorcycle sales clocking a 18% growth while scooter sales increased by 2% YoY. 2W sales for Bajaj Auto (BJAUT) rose 20% YoY to 404.9k, while TVS Motor (TVSL) saw a 4% YoY increase to 313k units wherein mopeds (+20% YoY) outperformed other segments. 3W sales for TVSL and BJAUT remained weak, falling 4% and 44% YoY respectively. Royal Enfield reported total 2W sales of 60k units (+1 YoY) and its core <350cc segment grew at 4% YoY.

CV slump continues: Ashok Leyland's (AL) CV sales fell 5% YoY to 8.3k units. MHCVs were the worst hit, slumping 23% YoY while LCVs were up 17%. In H1FY21, AL's sale volumes have plunged 66% YoY, led by a steep 80% drop in MHCVs. CV sales for TTMT were down 11% YoY, MHCVs were down 26% while LCVs grew by 5% YoY. Sales for VECV dropped 7% to 3.5k units.

Tractors resilient: MM sold 43.4k tractors (+17% YoY) in Sep'20 while competitor Escorts (ESC) sold 11.9k units (+9% YoY). For H1FY21, tractor sales for MM/ESC were up 1%/4% YoY. Positive rural sentiment led by timely and widespread monsoons, higher kharif crop sowing and adequate retail finance are a few factors that bode well for the agriculture sector and should aid tractor demand in the coming festive months.

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BUY – Expected return >+15%

ADD – Expected return from >+5% to +15%

REDUCE – Expected return from -5% to +5%

SELL – Expected return <-5%

Note: Recommendation structure changed with effect from 1 January 2018 (Hold rating discontinued and replaced by Add / Reduce)

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