Market Update

April 2021

The markets ended the month of March 2021 with minor gains of 1.1%. However, the volatility during the month continued to be high. Concerns of "taper tantrum" and a 2nd wave of Covid-19 cases in India led to cautiousness and bouts of selloffs. However, economic indicators and economic recovery enthused investors, leading to investment interest at every reaction. Broader markets were also flattish with the BSE Mid-cap and BSE Small-cap 250 indices gaining 1% and 0.7% respectively.

The financial year 2021 turned out to be one of the most eventful year. Starting with Covid-19 related scare and one of the sharpest corrections in recent times, markets ended with a lot of hope, optimism and spectacular gains. Nifty 50 gained a superb 71% for FY21, with the broader markets doing much better.

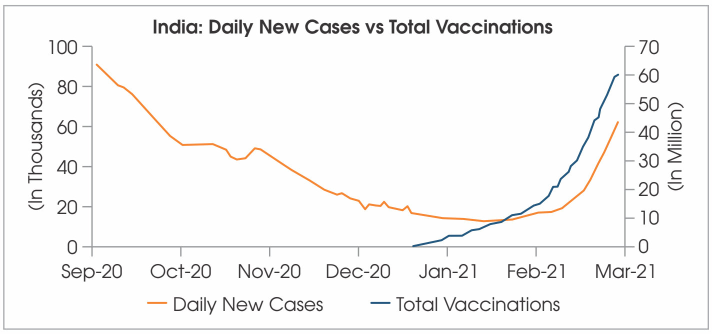
The month started on a positive note as after two quarters of contraction, 3QFY21 GDP grew at 0.4% and vaccination drive gained steam. However, the rapid spurt in Covid-19 cases, imposition of lockdowns, night curfews in some parts of India, elevated crude prices and jump in bond yields weighed on sentiments. On the macro front, World Bank raised India's FY2022 GDP forecast to 10.1% from 5.4% earlier. Some near-term macro challenges were visible with March CPI inflation rising to 5.52% compared to 5.03% in February on higher fuel prices.

Globally, the US Federal Reserve kept interest rates unchanged and mentioned that it does not currently expect to hike interest rates through 2023. Indian Central Bank, RBI too in its April 2021 monetary policy has maintained status quo.

FII buying slightly moderated to ~USD2.5bn in March 2021 (YTD +USD7.5bn) vs net inflows of ~USD3bn witnessed in February 2021, but it was encouraging to see DIIs turn net buyers for the first time in CY21 with net inflows of ~USD0.7bn (YTD -USD3.2bn). Mutual Funds saw a net subscription of ~USD1.05bn during March 2021, a first net inflow in nine months. (Source: NSDL, SEBI, AMFI)

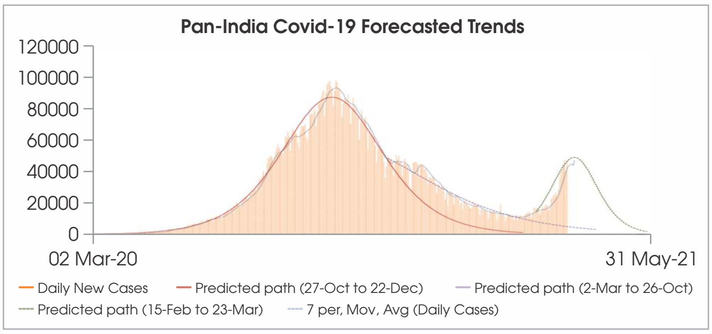
Vaccine Rollout

India is seeing its second wave of Covid-19 cases forcing authorities to act. The good thing this time is that everyone around is aware of the symptoms plus precautions that they must take. The State governments too have more localised lockdowns and curbs on mobility against a full lockdown. With cases largely localised and concentrated, and with momentum of vaccination likely to increase significantly, there are expectations that the second wave can be controlled soon. Expectations are of the 2nd wave peaking out somewhere in May 2021 and that should be heartening. India's vaccination roll-out phase has also been encouraging, though it needs to be rolled out much faster than at present to cover the vast population.

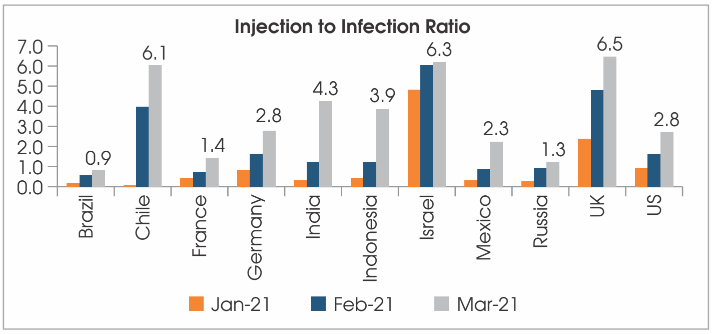


Source: Worldometer

Source*: NSDL, PTI, ANI, Bloomberg, BSE



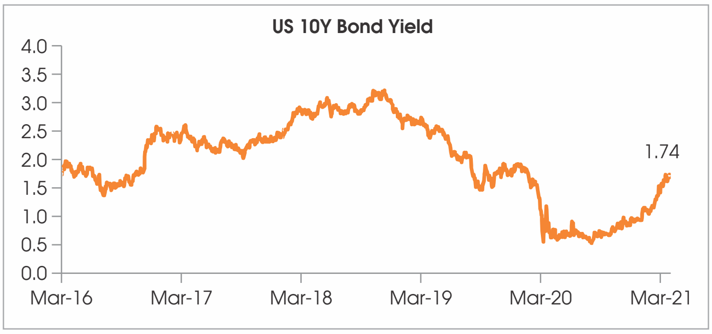
Source: SBI Report



Source: SBI Report

Yields

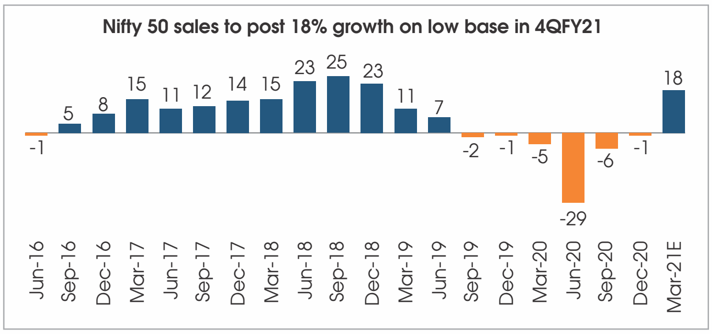
We have seen spike in yields across the globe. With economic recovery, all other indicators and asset classes back at pre-covid levels, yields have also come back to some extent at pre-covid levels. Risk of higher inflation hurting economic recovery underway is real as signalled by rising bond yields, but likely to be temporary given weakness in aggregate demand recovery. Inflation is largely cost-push inflation rather than demand-pull. Going forward, we do not expect materially sharp reactions as we continue to expect liquidity to be plenty.



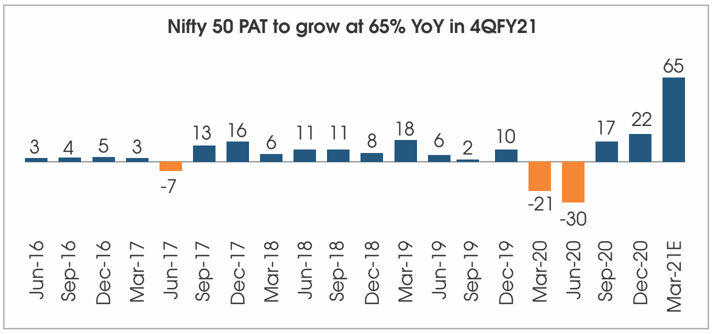
Source: Bloomberg

Earnings

The expectations for Nifty 50 earnings for FY21, post the onset of Covid-19 pandemic in March 20 were for a 25-30% drop. As time passed by, the recovery in economy & corporate profitability turned out much better than expected. In fact, after a long time, we are seeing many more upgrades than downgrades over the last three quarters. The earnings season for the December quarter was one of the best in the last 13 years and the March 21 quarter earnings are also expected to be quite good. Thus, from a scenario of a 25-30% drop in FY21 Nifty 50 earnings projected in April 20, it is now expected that there will be a healthy 13% earnings growth in FY21 Nifty 50 earnings, despite the challenges posed by the Covid-19 pandemic (Motilal Oswal Research estimates).



Source: Motilal Oswal Estimates



Source: Motilal Oswal Estimates

Constituents of markets and their movement

An interesting aspect of the markets, particularly over the last 6-8 months has been change in stocks and sectors that have been outperforming. Broader markets have significantly outperformed, with the midcap and smallcap indices doing much better. It has been a combination of massive underperformance from 2017 to 2020, faster growth and deep discount in valuations compared to their historic ratios as well as their large cap peers. Institutional apathy towards them, reflected by almost zero to very low holdings in these stocks, also has been a reason for the strong performance by this segment.

Another interesting trend has been the move away from "Quality at any Price" to "Growth at Reasonable Price". Here we would like to reproduce a table (refer Table A) that we had presented in our report titled, "Bubble in Quality" (To view the report click here). The table highlights that the market cap of HUL + Nestle as on October 24, 2019 was INR 6,07,331crs (~USD83bn) with a joint Net Profit of INR 7,666crs (~USD1.05bn). On the other hand, all metal, steel, cement, building material companies listed in India with a cumulative net profit of INR 73,816crs (~USD10bn) had a market cap of INR 6,01,254crs (~USD82bn). Thus, for 10x the profits, these so called "low quality" companies traded as exactly the same market value, highlighting the disconnect as also the opportunity that existed.

Table A

Company Name	Sector	Latest Market Cap (INR Cr)	FY19 Revenue (INR Cr)	FY19 PAT (INR Cr)	Peak Revenue (INR Cr)	Peak PAT (INR Cr)
Ultratech Cement Ltd.	Construction Materials	1,23,974	37,379	2,431	37,379	2,713
Shree Cement Ltd.	Construction Materials	65,010	12,555	1,015	12,555	1,384
Vedanta Ltd.	Non-Ferrous Metals	55,795	92,048	9,698	92,048	13,692
JSW Steel Ltd.	Iron & Steel	53,940	84,757	7,554	84,757	7,554
Tata Steel Ltd.	Iron & Steel	43,336	1,67,302	8,876	1,67,302	17,547
Hindalco Industries Ltd.	Non-Ferrous Metals	42,090	1,30,542	5,495	1,30,542	6,208
Ambuja Cements Ltd.	Construction Materials	41,232	26,041	2,960	26,041	2,960
ACC Ltd.	Construction Materials	29,165	14,802	1,510	14,802	1,561
The Ramco Cements Ltd.	Construction Materials	17,772	5,162	507	5,162	654
Dalmia Bharat Ltd.	Construction Materials	15,735	9,484	349	9,484	349
Steel Authority Of India Ltd.	Iron & Steel	14,953	66,974	2,126	66,974	6,851
Jindal Steel & Power Ltd.	Iron & Steel	10,980	39,372	2,412	39,372	4,002
Others Above 1000cr Mkt Cap		**87,271**	**1,05,323**	**6,071**	**1,06,259**	**8,340**
Total		**6,01,254**	**7,91,741**	**46,181**	**7,92,676**	**73,816**
HUL	FMCG	4,63,270	39,311	6,060	39,311	6,060
Nestle India Ltd.	FMCG	1,44,061	11,292	1,606	11,292	1,606
HUL + Nestle India		**6,07,331**	**50,603**	**7,666**	**50,603**	**7,666**

*Source: Ace Equity, Abakkus
**Sector classification as per Ace Equity
***Peak Profit = Highest Profit during FY10-19
****Market Capitalisation as of 24 Oct, 2019

Source*: NSDL, PTI, ANI, Bloomberg, BSE

In just 17 months since that report, this is what has happened (refer Table B). The market cap of HUL + Nestle has grown by 21% to INR 7,36,681crs (~USD100bn), underperforming even the Nifty 50 that has risen by 27% from 11,583 on October 24, 2019 to 14,691 on March 31, 2021. While the other group has seen a whopping 73% rise in their market cap to INR 10,39,918crs (~USD142bn).

Table B

		Market Cap (INR Crs)		
Company	**Sector**	**2021**	**2019**	**%Chg**
Ultratech Cement Ltd.	Construction Materials	1,94,493	123,974	57%
Shree Cement Ltd.	Construction Materials	1,06,313	65,010	64%
Vedanta Ltd.	Non - Ferrous Metals	85,031	55,795	52%
JSW Steel Ltd.	Iron & Steel	1,13,235	53,940	110%
Tata Steel Ltd.	Iron & Steel	97,756	43,336	126%
Hindalco Industries Ltd.	Non - Ferrous Metals	73,433	42,090	74%
Ambuja Cements Ltd.	Construction Materials	61,327	41,232	49%
ACC Ltd.	Construction Materials	35,741	29,165	23%
The Ramco Cements Ltd.	Construction Materials	23,649	17,772	33%
Dalmia Bharat Ltd.	Construction Materials	29,733	15,735	89%
Steel Authority Of India Ltd.	Iron & Steel	32,549	14,953	118%
Jindal Steel & Power Ltd.	Iron & Steel	35,048	10,980	219%
Others		**1,51,611**	**87,271**	**74%**
Total		**10,39,918**	**6,01,254**	**73%**
HUL	FMCG	5,71,133	4,63,270	23%
Nestle India Ltd.	FMCG	1,65,548	1,44,061	15%
HUL + Nestle India		**7,36,681**	**6,07,331**	**21%**
Nifty 50 Index Value		**14,691**	**11,583**	**27%**

Source: Ace Equity, data as of Oct 24th 2019 and Mar 31st 2021

The point we want to reiterate is that quality is always a key factor while investing, but "Buy at any Price" will not work eventually. Also, quality exists even in sectors that maybe cyclical but over a period even they report decent return ratios and are opportunities to invest in.

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