Investment Matters

February 2022

FY23 BUDGET: STIMULATING DURABLE GROWTH

The FY23 Union Budget continued the government's renewed focus on growth recovery that began last year. The preference for government capex over consumption stimuli was reinforced as the government stayed with its belief that this creates structural growth. The other notable feature was the conservative numbers, which we believe has multiple benefits.

We remain constructive on Indian equities and are increasingly confident on the growth recovery driving a sustained mid-teen market earnings growth over 2-3 years. Our key sector preferences are consumers, cyclicals (ex-commodities) and exporters, underpinned by our broad views on key macro indicators. We continue to focus on strong companies with market leadership and significant competitive advantage. Outside the new-age sectors, we prefer investing in companies with strong balance sheets, cash flows and strong-to-improving return ratios.

		Performance (%)			
Major Indian indices	**Jan-22**	**1M**	**3M**	**6M**	**1Y**
Sensex	58,014	-0.4%	-2.2%	10.3%	25.3%
Nifty	17,340	-0.1%	-1.9%	10.0%	27.2%
CNX-100	17,547	-0.4%	-1.9%	9.4%	27.7%
CNX-500	14,921	-0.5%	-1.1%	9.2%	32.0%
Mid-cap and Small-cap Indices					
BSE Mid cap	24,613	-1.4%	-2.6%	6.6%	36.1%
BSE Small cap	29,227	-0.8%	4.4%	9.1%	62.5%
CNX Mid cap	30,274	-0.6%	-0.6%	8.8%	44.8%
CNX Small cap	11,116	-1.5%	3.2%	5.6%	54.9%

Source: NSE, BSE

		Performance (%)			
NSE sector indices	**Jan-22**	**1M**	**3M**	**6M**	**1Y**
CNX Bank	37,975	7.0%	-2.9%	9.8%	24.2%
CNX Auto	11,704	7.0%	3.6%	16.5%	19.3%
CNX Realty	480	-0.8%	-3.7%	20.5%	57.1%
CNX Infrastructure	5,057	2.2%	0.2%	14.1%	37.7%
CNX Energy	24,984	10.4%	7.5%	32.0%	54.6%
CNX FMCG	36,467	-3.0%	-4.6%	1.2%	10.1%
CNX Pharma	13,180	-7.3%	-5.0%	-8.6%	8.3%
CNX IT	34,825	-10.0%	1.2%	14.3%	41.3%

Source: NSE, BSE

Budget takeaways

Capex push

The government has accentuated its path of pushing public capex to stimulate the economy. Capital expenditure for FY23 is up 35.4% y/y (excluding Air India Recapitalisation in FY 22). Some of the components are one-off, but we are encouraged by the sharp increase in categories like road construction, which is achievable and has multiplier effects on growth. The capex push should kick off a virtuous cycle where we see a multi-year growth cycle for infrastructure and industrial companies, after a sustained period of struggle through the decade ending 2020

Growth in spend (y/y)	FY19	FY20	FY21	FY22RE	FY23BE
Overall capex	17%	9%	27%	42%	24%
Roads	36%	0%	31%	36%	55%
Railways	23%	28%	60%	7%	17%

Source: Union Budget Documents, Ambit Capital research.

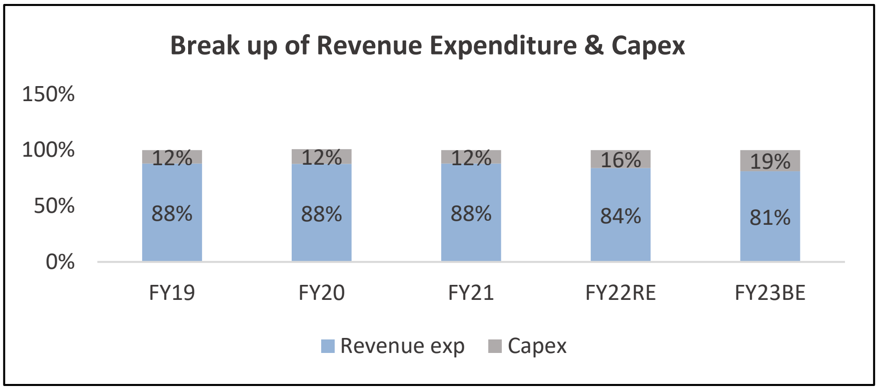
Note: Data refers to capex through budgetary support. If we include extra budgetary resources of public sector enterprises, total capex for FY23 is budgeted to rise by 13% YoY.

Shifting balance of expenditure

The lack of a direct consumption stimulus is notable. The uneven recovery in FY22, skewed towards higher-income segments, had driven expectations that such a measure was forthcoming. We do not see this as an issue for multiple reasons:

- There is an indirect stimulus via the increased spending on roads and railways. These are labour-intensive sectors that create large employment opportunities for lower-income segments.
- The extension of the ECLGS* scheme should help SMEs get back on their feet in FY23. This should help in transmission of growth to a broader base than what we saw in FY22.
- Outside the budget, the real estate sector is recovering across the country. This, again, is an important sector for low-friction absorption of excess labour throughout the country.
- The recent wave of the Omicron variant of Covid-19 created minimal disruptions to normal life. If the pandemic does, indeed, peter out, the lack of lockdowns should also help in reducing the stress on lower-income segments. * *Emergency Credit-linked Guarantee Scheme*

We believe that the capex push is the optimum usage of the four-year window of higher fiscal deficit, as it creates more durable growth than direct consumption stimuli.



Source: Union Budget Documents

Conservative budgeting

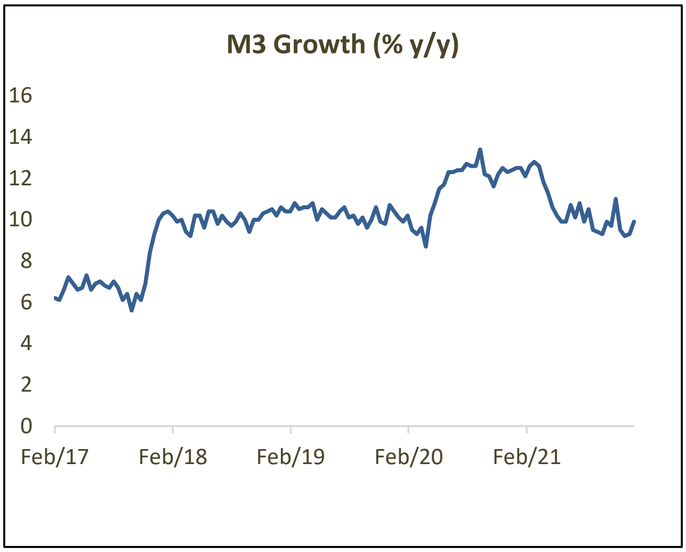
The government has stuck to its fiscal consolidation path of reducing the deficit by 50bp in FY23. More importantly, the numbers are conservative on multiple fronts – GDP growth assumptions, tax buoyancy and disinvestment assumptions. The obvious benefit of this is that it increases the credibility of the exercise, an area in which India has decades of spotty performance. The other positive is that it eases pressure on the government machinery – optimistic targets lead to second-order issues like overzealous tax collection efforts, aggressive push for disinvestments, and so on. It is likely that the final deficit will undershoot by 8 to10%, but that is a cushion that gives the government breathing space.

Bond market stress

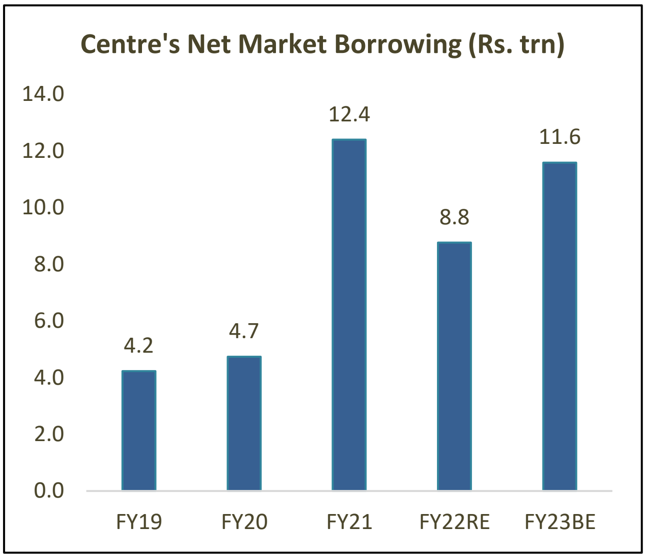
The bond market did not take the numbers well, with an ~20bp spike in bond yields since 31-Jan-22. We think the stress in the market should persist for some months as the market is squeezed from both ends.

- Supply is being constrained as M3 growth starts to normalise on the back of the RBI withdrawing stimulus and, possibly, challenges to foreign capital inflows on the back of the Fed tightening. Moreover, the RBI's ability to conduct open market operations will be constrained by the need to tighten policy.

- This is being met by a sharp spike in demand – the borrowing calendar for 1HFY23 will be based on the budgeted amount and not capture the possible upsides to government revenue.



Source: Bloomberg



Source: Union Budget Documents, RBI, Ambit Capital Research

Economic outlook

Growth: We see a multi-year period of growth, propelled by the virtuous cycle kicked off by the post-pandemic stimuli. The next 3-5 years should see multiple engines of growth firing simultaneously. Capex should get kicked off by the government's push starting FY22. Consumption is likely to accelerate as the growth becomes more broad-based from FY23. Exports are back after a long hiatus, helped by global growth, diversification of global supply chains and the government's fiscal support to select industries.

Fiscal deficit: We see steady fiscal consolidation from FY23 onwards. India's fiscal deficit is counter-cyclical with high growth as revenue buoyancy kicks in and spending is relatively inelastic. The government is likely to comfortably meet the FY26 target of 4.5% if growth remains elevated.

Interest rates: Stress on long-term bond yields should start to taper from late CY22 as growth kicks in and revenues overshoot budget estimates. On the other hand, short-term yields should continue their upward journey as the RBI moves towards a less accommodative monetary policy. We do not see higher interest rates as a challenge to growth – they will still be moderate compared to history and other demand drivers like capex and exports will continue to be in play.

Currency: The rupee should largely remain stable (against USD) through the next 2-3 years. The Fed tightening is a threat, but that should be offset by high growth, strong equity markets and some tightening from the RBI. Currency market collapses are often co-incidental with equity market stress in India – so this is a variable that we will continue to track closely.

Inflation: We have probably seen the worst of inflation. Global commodity inflation should cool off (even if prices go up) on a higher base and global monetary tightening. Supply-side challenges should also improve through the next 3-4 quarters as the impact of Covid-19 wanes throughout the world. We do not see a return to the 2019 levels of 2-3% but it should remain within the RBI's tolerance band of 4-6%.

Seshadri Sen
Head of Research
Alchemy Capital Management Pvt. Ltd

Source:
Alchemy Research

MARKET INSIGHTS

Alchemy view on Market trends, analysis, and way forward; with additional inputs from industry experts about the different aspects to superlative asset management.

1. Market Views : Market Views - Jan 2022 - YouTube

2. Blog : 2022: Strong Year For Equities Read More

3. Interviews :

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- Mr. Hiren Ved in an interaction with CNBC Awaaz: Watch the video
- Mr. Hiren Ved in an interaction with The Week: Read the article
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Q3 FY22 Performance of Portfolio Companies

The following table summarizes the performance of portfolio companies** for Q3 FY22 :

Stock	Sales (Rs Mn)			EBITDA (Rs Mn)			PAT (Rs Mn)		
	Q3FY22	Q3FY21	% chg	Q3FY22	Q3FY21	% chg	Q3FY22	Q3FY21	% chg
ANGEL ONE	4,448	2,221	100%	2,257	1,095	106%	1,647	784	110%
AVENUE SUPERMARTS	92,178	75,420	22%	8,665	6,891	26%	5,525	4,470	24%
BAJAJ AUTO	90,217	89,099	1%	13,721	17,296	-21%	12,142	15,563	-22%
BAJAJ FINANCE	60,005	42,958	40%	39,192	29,062	35%	21,253	11,460	85%
BLUE DART EXPRESS	15,062	11,239	34%	906	816	11%	476	367	30%
DEEPAK NITRITE	17,223	12,347	39%	3,519	3,350	5%	2,425	2,166	12%
DIXON TECHNOLOGIES (INDIA)	30,732	21,828	41%	1,030	1,005	2%	463	616	-25%
GLAND PHARMA	10,633	8,594	24%	3,489	2,642	32%	2,730	2,041	34%
ICICI BANK #	1,22,360	99,125	23%	1,01,483	88,198	15%	81,410	60,780	34%
INDIAMART INTERMESH	1,881	1,736	8%	788	878	-10%	702	802	-12%
INDIAN HOTELS COMPANY	11,112	5,599	98%	3,218	-167	NA	1,236	-1,399	NA
INFO EDGE (INDIA)	4,033	2,723	48%	1,121	682	64%	3,291	699	371%
L&T TECHNOLOGY SERVICES	16,875	14,007	20%	3,675	2,756	33%	2,488	1,861	34%
LARSEN & TOUBRO INFOTECH	41,376	31,528	31%	8,311	7,320	14%	6,125	5,192	18%
P I INDUSTRIES	13,563	11,621	17%	2,965	2,755	8%	2,223	1,954	14%
PIDILITE INDUSTRIES	28,507	22,990	24%	5,490	6,408	-14%	3,555	4,449	-20%
PRAJ INDUSTRIES	5,324	2,602	105%	462	160	189%	334	113	196%
RELIANCE INDUSTRIES	18,50,270	11,78,600	57%	2,97,060	2,15,660	38%	1,62,428	1,32,213	23%
SYNGENE INTERNATIONAL	6,414	5,845	10%	2,034	1,762	15%	1,040	1,022	2%
TATA CONSULTANCY SERVICES	4,88,850	4,20,150	16%	1,33,006	1,22,080	9%	98,060	87,270	12%
TATA CONSUMER PRODUCTS	32,084	30,696	5%	4,617	3,613	28%	2,748	2,231	23%
TATA ELXSI	6,350	4,770	33%	1,970	1,330	48%	1,510	1,050	44%
TATA MOTORS	7,22,293	7,56,538	-5%	67,642	1,15,096	-41%	-15,161	29,065	NA
TATA STEEL	6,07,831	3,95,941	54%	1,58,938	94,636	68%	95,727	37,001	159%
TITAN COMPANY	93,250	73,240	27%	13,990	8,580	63%	9,870	4,190	136%
UNITED SPIRITS	28,847	24,887	16%	4,907	3,838	28%	2,911	2,299	27%
VARUN BEVERAGES *	17,343	13,309	30%	2,076	1,722	21%	165	-197	NA
V-MART RETAIL	3,380	1,755	93%	206	-3	NA	-141	-190	NA
HDFC LIFE INSURANCE COMPANY @	25,970	21,570	20%	6,940	5,700	22%	2,759	2,670	3%
VIP INDUSTRIES	3,973	2,325	71%	572	92	522%	335	-70	NA
MPHASIS	31,237	24,743	26%	5,530	4,654	19%	3,575	3,255	10%
KDDL	2,581	1,782	45%	382	266	44%	137	78	76%
BAJAJ FINSERV	1,76,196	1,59,607	10%	1,75,867	1,59,585	10%	12,558	12,900	-3%

* indicates CY end - So Q3 FY22 = Q4 CY21
\# indicates Net Interest Income + Other income, Pre-Provision Operating Profit and PAT for banks
@ Indicates Annual Premium Equivalent (APE) and Value of New Business (VNB) for life insurance companies
** For Alchemy High Growth, Alchemy High Growth Select Stock & Alchemy Leaders Portfolios

Source-Alchemy Research

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