India market outlook – March 2022

March 04, 2022

Equity market outlook:

Since the beginning of the crises in Ukraine (24th February 2022), MSCI India has declined 4%, underperforming MSCI Emerging markets index (-2.8%). All sectors barring energy and metals have posted negative returns in the past week. (Source: Morningstar; Currency: USD).

On YTD basis (01 Jan 2022 to 3 Mar 2022), MSCI has declined 7.1% versus MSCI EM decline of 4.7%. (Source: Morningstar; Currency: USD). Weak global cues - fears of a Fed rate hike and escalating geopolitical tension between Russia and Ukraine have been the primary reason for the market fall. The Russia-Ukraine event is likely to keep the equity markets volatile in the near term as India is an importer of oil, gas and other commodities. Higher commodity led inflation could impact consumer goods companies as these companies will be unable to completely pass on the higher input costs. Foreign Portfolio investors have pulled out USD 9.8bn from Indian equities, which is highest compared to most Asian peers except Taiwan.

We continue to believe that 2022 will be the year of elevated volatility for equity markets and hence an active management approach has to be adopted for alpha generation. With recent correction, market valuations have moderated, thereby providing stock picking opportunities in select sectors. We would accumulate companies with strong balance sheets, agile managements, low leverage and sustainable business models. We are positive on sectors which are closely linked to the economic recovery like real estate, financials, auto and telecom.

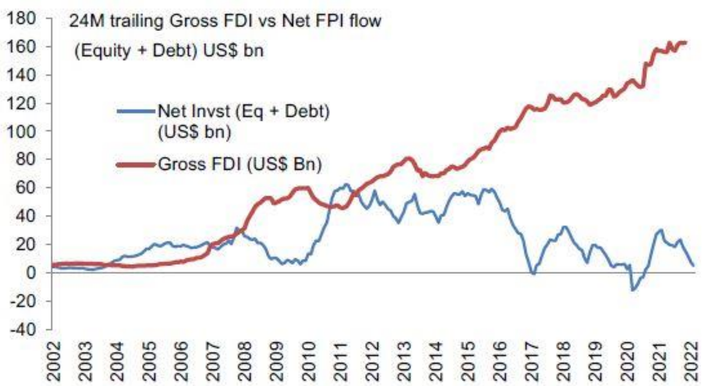
We remain constructive on Indian equities over the long term owing to a conducive domestic environment, supportive Government policies focused on capex led economic growth, favorable external indicators - high forex reserves, increased share of Foreign Direct Investment (FDI) flows and increasing participation of domestic investors in equity markets which is a more structural trend (refer charts below). On YTD basis, domestic institutional investors have been strong buyers of Indian equities with cumulative net flows of USD 8.5bn in CY2022, thereby providing support to equity markets. (Source: Bloomberg).

In terms of triggers, we would monitor US 10 Year treasury yield, Fed roadmap for withdrawal of stimulus, crude oil prices and Russia – Ukraine developments. Market performance ahead could also be determined by earnings growth as the recent run-up in commodity prices could lead to downgrades in the earnings estimates for some sectors.

Fixed Income Outlook:

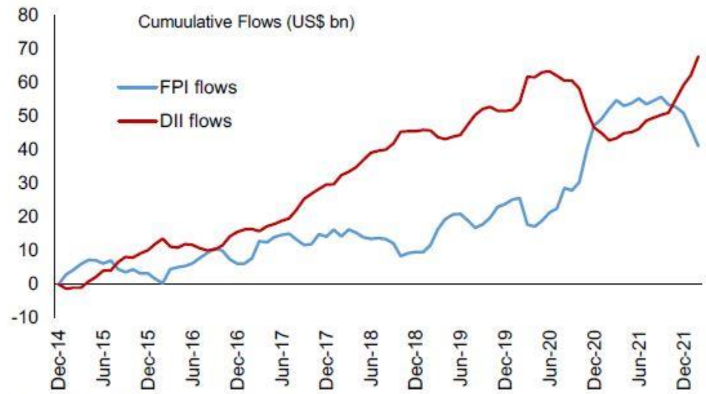
Bond markets have witnessed substantial volatility in February amid tightening global financial conditions, elevated crude oil prices, heavy bond supply for FY23 and lately the geopolitical tensions related to Russia-Ukraine. Brent crude prices have surged from USD 98/bbl levels on Feb 24, 2022 to presently ~USD 110/bbl. The sanctions imposed on Russia and their SWIFT payment system in the days post the invasion, also have a strong bearing on the global supply chain bottlenecks, which can impact commodity/energy prices contributing to an upsurge in inflation globally. For India specifically, since we are a big net importer of crude oil/energy, this impacts our current account meaningfully, and is also negative on inflation as crude prices affects food components of CPI basket indirectly. With a weakening current account, we expect the USD to continue to appreciate against the INR, in such a risk-off environment. Hence, from a fixed income perspective, at current elevated crude oil/higher inflation risk, we remain cautious on fixed income, and continue to be positioned in USD cash and other floating rate products from a defensive point of view.

Exhibit 6: FDI > FPI: More Stability in Flows



Source: CEIC, SEBI, Bloomberg, Morgan Stanley Research

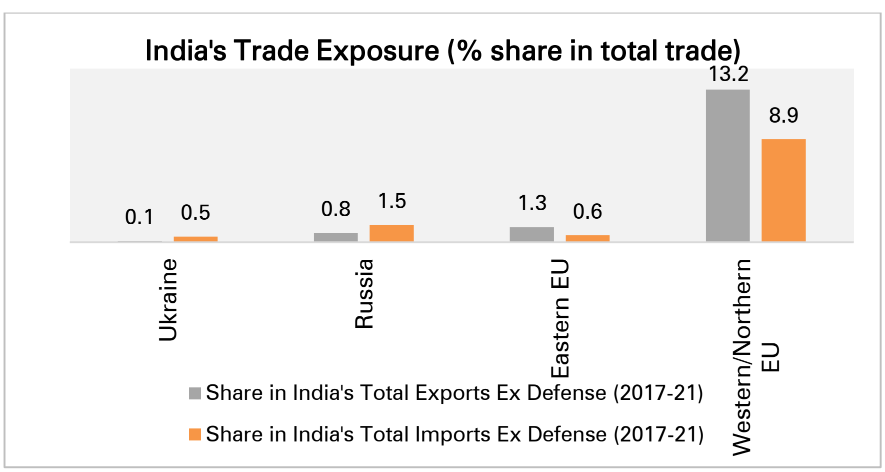
Exhibit 7: Strong Domestic Bid



Source: CDSL, SEBI, Morgan Stanley Research.

<u>**Some key facts about India's trade relations with Russia/Ukraine/Europe**</u>

- India's import exposure to Russia (ex-defense) is limited and accounts for only ~1.5% of total Imports. Other major imports include precious metals ~5% and petroleum products ~1.7%.
- Defense import dependence though large, has declined from ~62% share in 2010 to ~51% between 2016 and 2020. Indian exports exposure to Russia is merely ~0.8% of total exports, majorly being tea which is ~13 of total tea exports of India over last 5 years.
- Ukraine's share in total India imports is merely ~0.5%.
- Eastern Europe economies account for just 1.3% of India's export & 0.6% of its imports.
- We thus don't expect the ongoing crisis to impact Indian markets significantly as trade exposure is limited. However, need to be watchful of the impact of crisis on Western Europe where India has good trade exposure (imports and exports).



Source: Citi Research

Disclosures:

This article is for information purposes only and is not an offer to sell or a solicitation to buy any security or a recommendation or advise. The information that is used here is believed to be from reliable sources and is publicly available, including information developed in-house. These views alone are not sufficient and shouldn't be used for the development or implementation of an investment strategy. It should not be construed as investment advice to any party. All opinions and estimates included constitute our view as of this date and are subject to change without notice. While utmost care has been exercised while preparing the article, the sender does not warrant the completeness or accuracy of the information and disclaims all liabilities, losses and damages arising out of the use of this information. The recipient of this article should rely on their investigations and take their own professional advice.

In the preparation of the material contained in this document, the AMC has used information that is publicly available, including information developed in-house. Some of the material used in the document may have been obtained from members/persons other than the Fund and/or its affiliates and which may have been made available to the Fund and/or to its affiliates. Information gathered and material used in this document is believed to be from reliable sources. The Fund however does not warrant the accuracy, reasonableness and/or completeness of any information. For data reference to any third party in this material no such party will assume any liability for the same. All recipients of this material should before dealing and or transacting in any of the products referred to in this material make their own investigation, seek appropriate professional advice and carefully read the offer document. We have included statements/opinions/recommendations in this document, which contain words, or phrases such as "will", "expect", "should", "believe" and similar expressions or variations of such expressions that are "forward looking statements". Actual results may differ materially from those suggested by the forward looking statements due to risk or uncertainties associated with our expectations with respect to, but not limited to, exposure to market risks, general economic and political conditions in India and other countries globally, which have an impact on our services and / or investments, the monitory and interest policies of India, inflation, deflation, unanticipated turbulence in interest rates, foreign exchange rates, equity prices or other rates or prices, the performance of the financial markets in India and globally, changes in domestic and foreign laws, regulations and taxes and changes in competition in the industry.

The AMC (including its affiliates), the Fund and any of its officers, directors, personnel and employees, shall not be liable for any loss, damage of any nature, including but not limited to direct, indirect, punitive, special, exemplary, consequential, as also any loss of profit in any way arising from the use of this material in any manner.