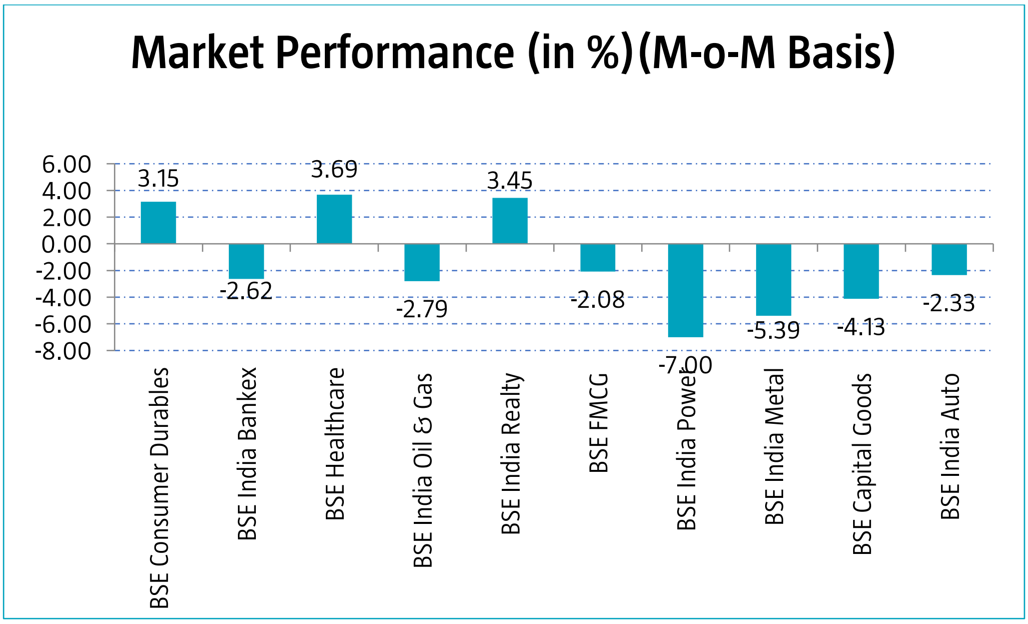
Equity Market Update

- In the month of Dec'24, Nifty 50 dropped sharply by -2.02% amid rupee's record fall against the U.S. dollar, U.S. Federal Reserve's hawkish tone on interest rate cuts in CY'25, softening second quarter earnings and uncertainty amid escalating tensions in the Middle East due to the conflict also added to fall.
- Foreign Institutional Investors (FIIs) were net buyers in Indian equities to the tune of ₹ 15,446.57 crore.
- Gross Goods and Services Tax (GST) collections in Dec'24 stood at Rs. 1.77 trillion, mostly driven by festive demand, representing an 7.3% rise on a yearly basis and this points towards the growing trajectory of the Indian economy.
- The combined Index of Eight Core Industries (Refinery Products Industry, Electricity, Industry, Steel Industry, Coal Industry, Crude Oil Industry, Natural Gas Industry, Cement Industry, Fertilizers Industry) increased by 4.3% YoY in Nov 2024 as compared to 7.9% growth in Nov 2023. The production of the Eight Core Industries remained mixed in Nov 2024 over the corresponding month of last year, with cement witnessed the highest rate of growth with 13.0% followed by coal with 7.5% growth, while crude oil fell the most by 2.1% followed by natural gas by 1.9%.
- However, during the month, sentiment was boosted after a positive turnaround from foreign institutional investors to domestic equity markets.
- Globally, U.S. Equities markets decreased after the U.S. Federal Reserve made its anticipated announcement regarding a reduction in interest rates by a quarter point on 18th Dec'24. European equity markets fell on concerns regarding political instability in several significant European nations. Continued worries about the Federal Reserve's interest rate trajectory caused Asian equity markets to plummet. In contrast to market expectations for a cut, the People's Bank of China decided to maintain its benchmark lending rates at their current level, which caused the Chinese market to plummet.



Note: The past performance may or may not be sustained in the future.

Source: MFI Explorer, ICRA Analytics Ltd. Data as on: 31st Dec'24

Equity Market Outlook

The global macro environment remains complex with the latest US unemployment and growth data being more resilient than estimated. Inflation and other data points indicate that inflation, while cooling on headline, the core Personal Consumption Expenditures (PCE) is not receding incrementally – pushing back aggressive rate cut hopes. This led to US 10-year rallying from 3.7% to 4.6% over last 3 months. The dollar index continued to strengthen because of Republican Party's victory, a negative for all Emerging Market (EM) capital flows in the near term. All EM's witnessed capital outflow during 3QFY25. Geopolitics in the middle east, Ukraine-Russia is clearly on an escalator path. However, the USA Republican Party's Presidential Candidate's return might mean de-escalation in wars over next few months – energy/growth positive. Expect USA Republican Party's Presidential Candidate's administration to be net positive for India on trade (China plus one) and defense (need for Asian partner against China) fronts. The US growth is stabilizing at lower levels (but resilient) as the fiscal and monetary impulse is receding, employment data moderating and inflation is moderating gradually – although not as much as was expected. The latest PCE in the US is running at 2.4% now (core PCE at 2.8%). This is leading to a possible goldilocks scenario where you might get lower inflation without hurting growth too much. We expect another 75-100bps in CY25. Europe is gradually stabilizing at lower levels, but manufacturing continues to suffer. China continues to have challenges on growth revival due to ageing population and leverage in households/Real estate, which are structural in our view. Commodities in general may remain muted for extended period, given >30-40% of every commodity is consumed by China and the recent stimulus doesn't change structural challenges of China in our assessment.

Geopolitical tensions are taking time to abate. Given these tensions, supply chains and global trade have become vulnerable to new dimensions now, missing till pre-covid. India remains one of the differentiated markets in terms of growth and earnings. In our worldview, 1) the Liquidity, 2) Growth and 3) Inflation surfaced post monetary and fiscal expansion in CY20-21 in that order and they will reverse in the same order during CY23-24. We have seen an initial downtick in inflation, which will accelerate in our view over the next few quarters. We expect 75-100bps of interest rate cuts over the next 12 months now.

Indian macro remains best among large markets except for growth part, where the last Gross Domestic Product (GDP) print came in at 5.4% - leading to downgrade in FY25 GDP growth to 6.6% by RBI. The Current Account Deficit has improved significantly and is expected to be ~1% for FY25. Most domestic macro and micro indicators remain steady. Given these aspects, the domestic equity market remains focused on earnings. Earnings growth remains relatively far better than most Emerging Markets/ Developed Markets. Having said this, FY25 earnings growth for nifty is likely to be single digit, a downgrade of >5% from the start of the financial year. Large Banks, Pharma, Auto, industrials, Telecom, Hospital and Real Estate are witnessing a healthy earnings cycle whereas Commodities, FMCG, chemicals continue to face headwinds. Indian equity market (Nifty) trades at 20FY26 earnings – in a fair valuation zone from medium term perspective – given longevity of earnings cycle in India. The broader market has moved up >30% in last 1 year -capturing near term earnings valuation positives for FY25/26E. Expect a rollover returns, as the earnings rollover to FY27E. Given the upfronting of returns in mid and small caps (aided by very strong flows also), valuations are at 20-30% premium to past; we are more constructive on large cap from FY25/26 perspective. Domestic cyclicals continue to have earnings edge over global cyclical and consumption. Select financials, select auto, Real Estate, Cement, Industrials, Power, Hotels/Hospitals/Aviation on domestic side continue to display healthy earnings. We believe that domestic consumption could turn out to be a dark horse in FY26 along with Cement.

Having said this on near term earnings challenges /market context, we believe that Indian economy is in a structural upcycle which will come to fore as global macroeconomic challenges recede over next few quarters. Our belief on domestic economic up-cycle stems from the fact that the enabling factor are in place viz. 1) Corporate and bank balance sheets are in best possible shape to drive capex and credit respectively, 2) Consumer spending remains resilient through cycles given our demographics, 3) Govt is focused on growth through direct investments in budget as well as through reforms like GST(increasing tax to GDP), lower corporate tax and ease of doing business (attracting private capex), Production Linked Incentives private capital through incentives for import substitution or export ecosystem creation) and 4) Accentuated benefits to India due to global supply chain re-alignments due to geopolitics. This makes us very constructive on India equities with 3-years view. We believe that India is in a business cycle / credit growth / earnings cycle through FY24-27E – indicating a healthy earnings cycle from medium term perspective.

Source: ICRA MFI Explorer

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