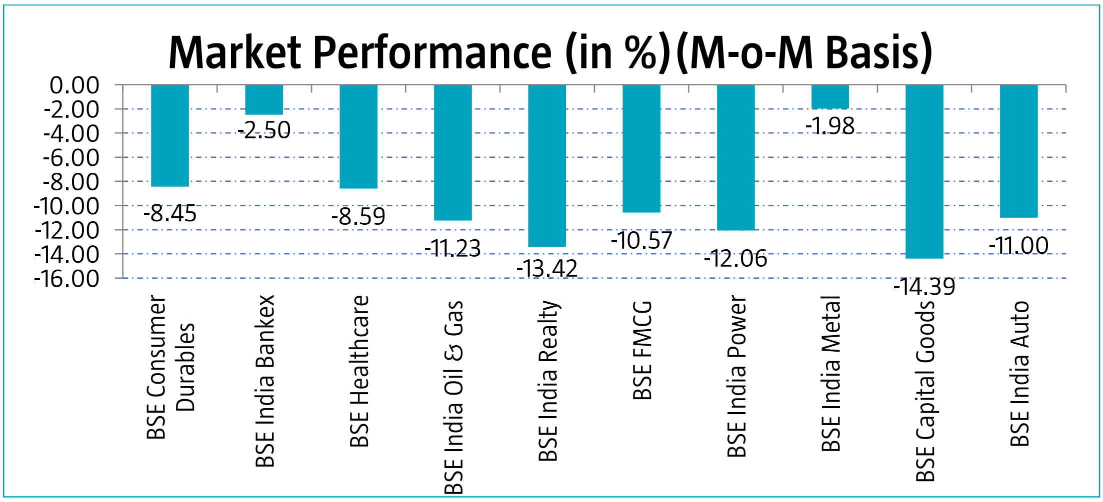
Equity Market Update

- In the month of Feb'25, Nifty 50 dropped sharply by 5.89% amid rupee's record fall against the U.S. dollar, broad-based sell-off across the sectors on concerns over weak corporate earnings in Q3 FY'25 and continued foreign fund outflows. There were concerns surrounding potential U.S. tariffs which could potentially drive-up consumer prices, potentially delaying the reduction of interest rates even further which affected the market sentiments.
- Foreign Institutional Investors (FIIs) were net sellers in Indian equities to the tune of ₹35,694.26 crore.
- Gross Goods and Services Tax (GST) collections in Feb'25 stood at Rs. 1.84 trillion, representing a 9.1% 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 4.6% YoY in Jan 2025 as compared to 4.2% growth in Jan 2024. All the components of the Eight Core Industries witnessed growth in Jan 2025 over the corresponding month of last year except crude oil & natural gas, with cement production which witnessed the highest rate of growth with 14.5% followed by refinery products with 8.3%, while electricity rose the least by 1.3% followed by fertilizers by 3.0%.
- Globally, U.S. equity markets decreased following ongoing tariff concerns and indications that the U.S. Federal Reserve is likely to keep interest rates on hold for some time. European equity markets rose after robust earning numbers. However, concerns regarding the U.S. President's tariff threats and policies weighed on market sentiment. The closing of the Asian equity markets was uneventful as U.S. President announced that the implementation of tariffs on imports from Mexico and Canada will proceed as scheduled. Japanese market plunged amid the release of mixed industrial production and retail sales data for Jan'25



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

Source: MFI Explorer, ICRA Analytics Ltd. Data as on:28th Feb'25

Equity Market Outlook

The global macro environment remains complex with, 1) US growth inflation dynamics indicating possibility of stagflation, 2) Tariff news flow keeps the uncertainty and inflation resilience going in an environment where the incremental data points continue to indicate consumer slowdown. US might be in for a negative growth surprise in an environment of headline inflation leaving limited room to cut beyond current expectations of 50-75bps in CY25. Trump policies up to now are indicating their inward focus with a multi-polar world and lack of respect for global trade and defense agreements of previous US establishments. We worry that this might lead to negative global growth impulse with limited ability to cut US interest rates. It is almost impossible to change the supply chains and value chains that have been developed and nurtured over the last 3 decades. Expect uncertainty to prevail both on global growth and capital flows for Emerging markets including India. Only silver lining of this environment is that it can quickly lead to US recession potentially easing monetary policy, Fed providing liquidity and faster interest rate cuts. US dollar would depreciate under such circumstances – a positive for Emerging markets.

Emerging markets witnessed strong capital outflows over last 3 months. After strengthening for 3 months, the dollar index has started depreciating – a good sign – indicating possible flows moving towards Emerging markets and Europe, based on domestic factors in each market. Europe and China growth rates remain subdued at best. Euro area might be eventual beneficiary of this environment since it forces it to enable policies which make it better as economic and geopolitical zone. European leaders have been forced to make serious choices for the first time in last several decades. They will start looking East more and India could be beneficiary of that along with China and others. Geopolitics in the middle east, Ukraine-Russia is clearly on a de-escalation path, positive for growth and negative for energy prices. 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. Only positive for China is its cheapness and good quality tech listed entities.

Geopolitical tensions are only getting complex. Given these tensions, supply chains and global trade have become vulnerable to new dimensions now, missing till pre-covid. 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 CY24-25. India remains one of the differentiated markets (Exports just 15% of GDP) in terms of structural growth and earnings, notwithstanding cyclical slowdown that we are witnessing right now.

Indian macro remains best among large markets except for growth part. The last Gross Domestic Product (GDP) print came in at 5.4% and 6.2% respectively for 2Q/3QFY25 - leading to downgrade in FY25 GDP growth to ~6.5% by consensus. Current Account Deficit has improved significantly and is expected to be 1-1.5% for FY25E/FY26E. Most domestic macro and micro indicators remain steady. Given these aspects, the domestic equity market remains focused on earnings. While the structural earning growth has been healthy at >15% CAGR for FY20-24, FY25E has moderated to mid-high single digit, a cause of concern. We believe that this cyclical slowdown is driven by, 1) Reduced Govt spend during 1HFY25 (which is catching up now), 2) Significantly above average monsoon in southern part of country and 3) Stringent liquidity and administrative actions by RBI on retail credit (which is also reversing now). Consumption and revenue expenditure at State /Central level has started moving up.. Financials, Pharma, industrials, Telecom, Hospital, Hotels, Aviation and Real Estate are witnessing a healthy earnings cycle whereas FMCG, Commodities and IT continues to face headwind. Indian equity market trades at 19xFY26/17xFY27 consensus Nifty earnings – in an attractive valuation zone from medium term perspective – given longevity of earnings growth potential in India. Large caps seem to have become quite attractive based on these valuations. The broader market has moved up >50% in last 2 year capturing near term earnings positives. While the latest correction has taken out the froth in mid-caps and small caps, they continue to trade at 10-15% premium to their own historical valuations – indicating that the strong earnings revival is must for this part of the market. FY26/27 is expected to be a stock pickers market as against broad themes as experienced in FY24/25.

Having said this on near term earnings /market context, we believe that Indian economy is in a structural upcycle which will come to fore as global macroeconomic challenges/flow 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 cycle 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 constructive on India equities with 3-5 years view. We believe that India is in a business cycle / credit growth / earnings cycle through FY23-27E – indicating a healthy earnings cycle from medium term perspective.

Source: ICRA MFI Explorer

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