Market Outlook

March 2020

FM, RBI measures to provide interim breather…

Fear, anxiety and pandemonium sum up the current global scenario, which has been brought to an almost standstill situation in the wake of the Coronavirus issue. The coming few months are expected to be difficult to navigate as global trade has dwindled and all financial markets have witnessed a swift meltdown thereby discounting the anticipated damage that will be inflicted upon the global economy.

We believe that recent announcements by the Finance Minister (FM) and RBI are likely to be a much needed breather for the formal and informal segment of the economy.

Nevertheless, there exists three key questions in the minds of an investor

1. Till what time the current pandemic will subside
2. Quantum of demand destruction that is likely to happen
3. To what extent asset prices will get reset across financial markets

The straightforward answer is not known to any one, in our view. However, at the same time, history being a good judge, tells us that financial markets do discount such events at a very rapid pace, sometimes overshooting on the downside. Even on a historical basis, we believe broader markets have coincided with long term averages currently, which does not surely indicate a bottom. However, at the same time it has started throwing up opportunities in the large cap/midcap space.

In the current milieu, some of the large and best managed companies are available at attractive valuations on a historical basis. Hence, in our view, one should venture out and accumulate companies (depending on their risk appetite and time horizon), which have gone through such challenging cycles and have come out much stronger when such events subside.

Our Top Picks in the large cap space are HDFC Bank, Kotak Mahindra Bank, Titan, Dabur Bharti Airtel, Avenue Supermarts and SBI Life

Our Top Picks in midcap space are Bata, Tata Consumer Products (erstwhile Tata Global Beverages), Trent,

Foodgrain distribution – necessary measure to support masses

The Finance Minister in her press briefing yesterday announced measures to support the most vulnerable sections of the society amid the prevailing outbreak of Covid-19. The government intends to give 5 kg of cereal i.e. rice/wheat for three months to 80 crore eligible population for free. Moreover, they will also provide 1 kg of regional pulses for three months to those 80 crore people, again free of cost. **We envisage this as a necessary step to support the masses and will likely cost the exchequer around ₹ 50,000 crore. The government is holding stock to the tune of 38.1 MMT of rice (includes conversion of paddy at the rate of 65%) and wheat stock of 35.1 MMT. The government would distribute either 12 MMT of rice/wheat or combination of both items, which would deplete the inventories at FCI and reduce the storage cost.**

Particulars	Amount
Quantum of Cereal to be provided per month	5 kg
No of months of free assistance	3.0
No of intended Beneficial's	80 crore
Total Quantum of food-grains to be distributed	12 million tonne
Average Rice Costs / kg = Paddy MSP Price + Conversion from Paddy to Rice	₹ 30/kg
Total costs of Cereals distributed (₹ crore)	**36,000**
Quantum of Pulses to be provided per month	1 kg
No of months of free assistance	3.0
No of intended Beneficial's	80 crore
Total Quantum of cereals to be distributed	2.4 million tonne
Average price of Pulses	₹ 60/kg
Total costs of Pulses distributed (₹ crore)	**14,400**
Total cost of food support (₹ crore)	**50,400**

Source: Bloomberg, ICICI Direct Research

FM announcements – to address informal segment pain

- The government announced transfer of ₹ 500 per month for the three months to women Jan Dhan accounts. As per the estimates, around 20.4 crore Jan Dhan accounts are there. This would translate into ₹ 30,600 crore disbursement to the beneficiaries. **We expect this to translate to higher consumption of regular day to day items. Hence, it is positive for FMCG stocks.**

- A ₹ 2000 transfer to the 8.69 crore farmers under PM Kisan scheme amounts to ₹ 17380 crore. This will not be the additional outlay but the advance payment. Hence, we expect this money to help farmers buy certain farm inputs ahead of Kharif season. **Major beneficiaries would be seed, fertiliser companies**

- Poor senior citizen/widows/handicapped would receive ₹1000 in two instalment over three months. This would result into additional outlay of ₹ 3000 crore assuming 3 crore beneficiaries. **The amount could assist higher consumption of medical items along with FMCG items. Since the disbursal is not significant, hence we are not expecting any major benefits to the said sector stocks**

- Ujjwala scheme women will be given free cylinders for the next three months. Total relief will be to the tune of ~₹ 17500 crore for 8.3 crore families below poverty line. **We believe this move will increase OMC's working capital for three to six months. However, on account of lower oil prices, it will not have any material impact on them**

Source: Bloomberg, ICICI Direct Research

Key takeaways from RBI's announcements

Measures taken by RBI	Impact
Repo Rate reduced by 75 bps to 4.4%	Reduce borrowing costs structurally for the borrowers over the time
Reverse Repo reduced by 90 bps to 4%	This move is undertaken to encourage banks to induce lending rather than parking additional funds with RBI
CRR reduced by 100 bps to 3%, Daily CRR reduced from 90% to 80%	CRR cut to benefit all banks. This move will inject ₹ 1.37 lakh crore in the banking space and banks to earn ₹ 10960 crore as interest income at 8% assumed vs zero earlier.This will be a key offset for the needed provisions and lowering their cost of funds.
3 month moratorium period for payments of installments for term loans and interest on WC facilities to be deferred by 3 months. Also WC limits be re calculated. All this not to impact the credit score of the borrowers	As it includes all term loans, all retail, home, Micro Finance and corporate loans are covered except credit cards. Such moratorium will provide much needed respite for borrowers, especially MSME and unsecured retail loans without burdening lenders with increase in asset quality pressure. However, clarity is awaited on impact of NPV loss related to moratorium which may be needed in the P&L.
Conducting auctions of TLTRO upto 3 year tenor for a total amount of ₹1 lakh crore. Liquidity availed in this facility needs to be invested in corporate bonds, commercial papers and NCD of investment grade category and can be classified in HTM	RBI is regularly conducting to infuse liquidity at lower rate in to the system but the targetted investment in corporate Bond/ CP etc will ease the pressure in bond market. Classification into HTM category vs MTM done earlier in these papers is positive for corporate papers trading at high rates. Expect PSU banks to participate in the same.

Source: Bloomberg, ICICI Direct Research

RBI's announcement boosts investment opportunity in debt market

- RBI in its surprise preponed Monetary Policy Committee (MPC) meeting cut Repo rate by 75bps and Reverse Repo rate by 90bps to 4.4% and 4.0% respectively. Thereby the corridor stands wider at 40 bps from 25 bps earlier. The upper band as denoted by the Marginal Standing Facility (MSF) continues at 25 bps over the repo rate.

- RBI will conduct Targeted Long Term Repo Operations (TLTROs) for up to 3 years amounting to a total of ₹ 1 lakh crore at the policy rate. Liquidity availed under the scheme by banks has to be deployed in investment grade corporate bonds, commercial paper, and non-convertible debentures both in primary and secondary market and will not be marked to market. This measure will help reduce yield on corporate bond and commercial papers.

- RBI also announced several other measures like CRR cut of 100bps from 4.0% to 3.0%, raised MSF limit from 2% of SLR to 3% of SLR effective immediately till end June, various sorts of moratorium and dispensations on payment and recognitions have been provided without any impact required to be recognized on asset quality or the credit history of the beneficiary

- With system liquidity in surplus and RBI's further liquidity boosting measures, the system liquidity is likely to remain in surplus in the near to medium term. Effectively, the Reverse Repo should be the operating rate rather than the Repo rate. Accordingly, the G-Sec and Corporate bond spread over Reverse Repo rate should become the primary focus leading to higher scope for reduction in G-Sec and corporate bond yields.

- **In the last few week, yields across corporate bonds have moved up sharply by more than 150-200bps. Yield on AAA oriented corporate bond fund have moved up from around 6.8% in February to currently around 8.2%, a rise of 140bps. In current extremely conducive global debt market environment, this presents as excellent investment opportunity for lump sum investment. Investors may also capitalize on higher indexation benefit in long term capital gains by investing before 31st March**

Source: Bloomberg, ICICI Direct Research

HDFC Bank

HDFC Bank has efficiently focused on retail business and has garnered strong liability franchise to yield superior profitability over the years. Seasoned portfolio and management experience led to higher than industry advances growth at ~24% CAGR in FY08-19. Advances were at ₹ 9.3 lakh crore as of December 2019, with major traction towards the retail book. Enriched customer experience, strong network of 5345 branches and focus on digitisation has enabled to build a strong liability franchise with CASA comprising ~40% of deposits. Such high CASA limits cost of funds and thereby enable to report superior NIM above 4% consistently. Prudent asset quality has been core to the bank. The same has safeguarded the bank from NPA issues faced by the industry in recent fiscals. RoA at ~1.5% and RoE at 15-18% remain consistent for the bank with valuations expected to remain at a premium.

Kotak Mahindra Bank

Kotak Mahindra Bank (KMB), promoted by Uday Kotak, reported a loan book of ₹ 216774 crore as on December 2019. It has built a branch network of 1539 branches. Increased focus towards retailisation of loans has enabled KMB to earn the best NIM in industry at 4.7%. The savings rate was hiked by KMB to 6% in 2011, boosting savings deposits growth to ₹ 239354 crore by December 2019. CASA ratio improved from 50.7% in December 2018 to 53.7% in December 19, which is the best in industry. Overall asset quality remained resilient with GNPA ratio at 2.46% in Q3FY20. The bank has no major exposure to IL&FS & other stressed assets. Going ahead, healthy business growth coupled with stable margins are expected to augur well for the bank.

Titan

Titan Company is the market leader in the Indian jewellery market through its flagship brand Tanishq. The company also has a presence in other consumer segments of watches and eyewear. The company has also entered the online jewellery market through acquisition of caratlane.com. Volatility in gold prices, impact of Covid-19 (closure of retail outlets owing to national lockdown) and reduced demand in discretionary spends are expected to impair consumer demand in the near term. However, the company is likely to recoup lost sales owing to pent up demand from H2FY21. Tanishq's sustained efforts towards enhancing the share of wedding jewellery is paying dividends with the wedding jewellery portfolio growing at a faster pace than non bridal jewellery. The company has consistently exhibited its ability to gain market share on a sustained basis amid a tough industry scenario. Robust balance sheet (30%+ RoCE and virtually debt free status) and asset light distribution model have enabled it to outpace peers in terms of store addition (added 34 Tanishq stores for 9M ended December 2019, which is equivalent to FY19 store addition) Over the longer term, we expect Titan to be a key beneficiary as India's gold market continues to strive towards regulation and standardisation.

Bharti Airtel

Bharti Airtel is the key beneficiary of the consolidation in the telecom sector. Airtel continues to report a relatively stronger retention of its revenue market share with stable KPI across, and also enjoys a comfortable leverage vis-à-vis peers post the fund raise. Notwithstanding AGR issue, Airtel's survival is assured post fund raising and tariff hike. Recent development such as full AGR dues demand will not be an issue as it has the requisite funds at disposal. Moreover, a possibility of government relief (either in terms of reduction in levy, or spectrum cost reduction or floor pricing) is likely to boost the overall telecom industry return ratio metric. With a strong footing in challenging times, Airtel is one of the better placed telecom players.

SBI Life

Continued focus on business growth and improvement in the product mix has remained the core strength. In terms of business growth, SBI Life has reported highest NBP growth among top private insurers above 30% CAGR in the last four years, thereby increasing its market share to ~20%. Proportion of high margin protection business has been on an uptrend from 5% in FY18 to ~11% in Q3FY20, which remains accretive for VNB margins expected at ~18% ahead. Improving persistency and excellent operating efficiency remain strong levers for earnings. Strong distribution with ~24000 branches of SBI and more than 1 lakh agents, remain key catalyst. With annual gross premium of ₹40000 crore and AUM of ₹ 164000 crore in FY20, we expect operating RoEV to improve to ~18% in FY22E translating into EV growth at 15-16% CAGR in EV in FY20-22E to ₹ 35000 crore. Therefore, we remain positive on SBI Life, being a play on growth led by distribution, brand reach and adequate product mix.

Avenue Supermarts

Over the years, D-Mart, through its proven business model, has been able to maintain consistent profitability and remains an exceptional performer in its peer group. Given the robust store operating metrics (breakeven in first year of its operations and industry best revenue/sq ft: ₹ 36000), D-Mart has progressively enhanced its return ratios despite being capex intensive. We expect the impact of virus to be limited owing to non-discretionary nature of the business. In a bid to reduce promoter stake to 75%, the company had successfully concluded qualified institutional placement (QIP) placement worth ₹ 4100 crore (2.0 crore shares at ₹ 2049/share). Incremental cashflow infusion in the company is expected to significantly shore up store addition pace (as per our calculations ~45 incremental stores can be opened) with foray into newer geographies. DMart has a capital efficient business model generating superior RoCE of 23% and fixed asset turnover ratio of 4.1x. The infusion of funds into the business would provide Avenue Supermarts the ammunition to enhance its store expansion pace resulting in higher revenue and profitability.

Dabur

Dabur India with a turnover of more than ₹ 8500 crore and earnings of more than ₹ 1400 crore has a strong portfolio of brands (Dabur Chyawanprash, Real, Hajmola, Vatika, Amla, Fem, Honey, Meswak, Dabur Red) with focus largely on ayurvedic & healthcare offerings. With a wave of demand for the ayurvedic & natural products in addition to Coronavirus outbreak globally, staples segment including Dabur has been gaining significance specially its healthcare and home care categories such as Chyawanprash, honey, glucose, toothpaste, shampoos and hair oil. Dabur's broad product portfolio provides a good play on Indian consumer goods spend by its strong presence in less penetrated and high growth categories. Rural segment contributes around 45% of its overall sales. Therefore, it is well placed to take advantage of the rural recovery. On the back of improved product mix & robust volume growth, there has been a significant improvement in operating margins from erstwhile 16% margins in FY14 & FY15 to ~20%+ margins levels in FY18 and FY19, respectively.

Bata

In the short-term, revenue growth is expected to be impacted owing to the disruption caused by Covid-19. However, we expect the company to tide over the uncertainty owing to its strong brand image and robust balance sheet. Bata has constantly taken enhanced efforts to transform its image from a mass brand to a premium brand through launch of new trendy collections, increasing spend on marketing and redesigning existing store models to appeal to the younger generation. The share of premium products is currently at ~ 50% while the focus is on continuously premiumising the product portfolio further over the medium to long term. The company's efforts of premiumisation have yielded better profitability as the RoCE has increased substantially from 16% in FY17 to 23.7% in FY19. It has a robust balance sheet with healthy cash and bank balance worth ₹ 839 crore with a negative working capital cycle. On the store expansion front, the company is planning to open 500 franchisee stores over the next five years. The asset light expansion is expected to further boost the return ratios over the medium to longer term.

Tata Consumer Products (erstwhile Tata Global Beverages)

Tata Consumer Products (TCPL), earlier known as Tata Global Beverages, commands 20% market share in the Indian tea segment. It expects to continue to grow above industry led by new launches and focus on premium tea varieties. The branded tea business has delivered robust volume growth of 8% in 9MFY20 driven by market share gains, inorganic growth, product innovation and focus on premiumisation. Tata Chemicals' consumer business has been growing at a strong ~20% over the last two years backed by robust growth in volumes across salt, pulses and spices. It has been maintaining its operating margins around 16%, much higher than TGBL's ~13% (as on 9MFY20). Though pulses and spices segments are smaller in size, we believe these underpenetrated and high growth categories would aid TGBL's growth. We believe investment behind new categories (Tata Dx detergent powder and Tata Nx sugar-free natural sweetener) including other newer segments, would be the key to growth, going ahead. On the back of strengthening its core business, expanding its geographical presence and shift to lower tax regime in India business, we expect adjusted PAT CAGR of 15.6% in FY19-21E. TGBL's India business revenue contribution has increased from the previous 47% in FY19 to ~52% in 9MFY20 with impressive EBITDA margins of 13%. The company has been exiting non-core international markets (exit from loss making China, Russia and Czech Republic subsidiaries and stake divested in its Sri Lankan plantations), which has been a drag on sales growth. This would further improve the overall profitability.

Trent

Trent, a leading retailer with presence across various consumer categories is gearing up for rapid growth driven by aggressive store addition. Trent's flagship store format 'Westside' generates one of the highest gross margins in the industry (~56%). Westside continues to be one of the most successful established franchises, deriving 97% share of revenues from private labels. Westside has continuously sustained same store sales growth of over 7%, outperforming peers in the industry. Over the last few quarters, the company's 'Zudio' value format stores are also being ramped up at a fast pace while Zudio revenues have outpaced the revenue growth of Westside (albeit on a low base). Over the last three quarters, the company has recorded 30%+ revenue growth on the back of aggressive store addition pace, coupled with healthy SSSG. The revenue trajectory is expected to be lower in Q4FY20, Q1FY21 owing to temporary store closures due to Covid-19. However, we expect a gradual pick-up in H2FY21. Over the last two years, Trent had aggressively shored up its store addition pace with capital infusion by the promoters (₹ 950 crore). Higher promoter commitment signifies positive momentum in core business performance metrics.

Top Mutual Funds Picks: Debt

HDFC Corporate Bond Fund

- HDFC Corporate Bond Fund is one of the most consistent and stable performing debt fund.
- The fund house adopts a relatively higher average maturity of around 4 years to gain from higher accrual. Established track record and consistency makes it an ideal debt fund for long term. The current YTM of the fund is around 8.2%

ICICI Prudential Corporate Bond Fund

- ICICI Prudential Corporate Bond Fund is stable performing AAA oriented debt fund.
- The fund manager adopts a relatively conservative approach in terms of Average maturity. Current Average maturity is around 2.5 years. 8.7. The current YTM of the fund is around 8.5%

L&T Triple Ace Bond Fund

- L&T Triple Ace Bond Fund is a uniquely positioned fund with long duration papers of PSUs and highly rated corporates
- The average maturity of the fund is ~8.5 years and is there best placed to capitalise on capital gains if yields going forward. The YTM of the fund is around 7.5%.

Source: ICICI Direct Research

Top Mutual Funds Picks: Equity

We suggest to invest in the following funds as a basket in a staggered manner over the next few months:

Axis Midcap Fund (Midcap)

- Axis midcap fund is one of the best performing fund in the midcap category. Good quality portfolio with high growth potential makes it one of the better funds in the midcap space especially in current market environment where many quality stocks have also corrected. The same provides good entry point as a portfolio.
- The fund manger has managed the volatility in the midcap space well by actively managing the cash holding. Axis as a fund house as focussed on quality growth oriented stocks and the same has worked exceptionally well for them.

ICICI Pru Bluechip Fund (Largecap)

- ICICI Pru Bluechip fund is one of the most consistent performing fund in the largecap category.
- The fund is an ideal mix of quality and value stocks and provides stability in performance
- The portfolio stocks are well positioned to ride on consistent growth opportunity while giving allocation to value stocks as well. This balanced portfolio in the largecap space is ideal for allocation in current market environment

SBI Large and Midcap Fund (Multicap)

- SBI as a fund house has emerged as a consistent and stable performing fund house. In general, it has a tilt towards quality stocks. Accordingly, it participated in the recent market cycle of growth stocks outperforming. The fund house is now balancing it by adding value oriented stocks to ensure a balanced investment style i.e. it is not sticking to growth at any price
- The fund is a multicap fund with good balance of growth stocks and stocks well placed to ride the macro play

Kotak Emerging Equity Fund (Midcap)

- This midcap fund offers an optimal mix of good quality growth oriented stocks and value stocks. The portfolio positioning should help the fund maintain a stable performance compared to the cyclical performance
- Fund manager Pankaj Tibrewal has been associated with the fund for almost 10 years. He has been a midcap/small cap specialist for long (Principal AMC funds used to do well when he was associated with it prior to joining Kotak)

Source: ICICI Direct Research

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