

Investment Matters

June 2021



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EQUITY OUTLOOK

Cyclicals leading the market

The markets bounced back in May after two flat months, led primarily by the second Covid wave starting to recede and some acceleration in vaccination. Some of the laggard sectors over Feb-Mar '21 like banking, auto, energy and infrastructure led the market revival. The earnings season was mixed but the impact of the second wave does not seem to have been as severe as in 2020, which fuelled some optimism. We remain constructive on the markets and the three pillars of our approach remain unchanged: minimise cash, focus on market leaders with strong balance sheets and shift emphasis to cyclicals over defensives.

	May-21	Performance (%)			
		1m	3m	6m	1Y
Major Indian indices					
Sensex	51,937	6.5%	5.8%	17.6%	60.2%
Nifty	15,583	6.5%	7.3%	20.2%	62.7%
CNX-100	15,799	6.8%	7.7%	20.8%	61.9%
CNX-500	13,226	7.0%	8.6%	23.4%	69.1%
Mid-cap and Small-cap Indices					
BSE Mid-cap	21,758	7.1%	8.9%	28.6%	83.7%
BSE Small cap	23,596	8.9%	17.1%	39.8%	116.6%
CNX Mid cap	25,775	6.5%	10.8%	30.7%	94.2%
CNX Small cap	9,267	8.2%	15.1%	41.0%	131.5%

Source: Bloomberg

	May-21	Performance (%)			
		1m	3m	6m	1Y
NSE sector indices					
CNX Bank	35,527	8.4%	2.1%	20.0%	84.1%
CNX Auto	10,492	8.8%	3.2%	18.0%	68.7%
CNX Realty	336	8.6%	-3.9%	28.7%	86.6%
CNX Infrastructure	4,328	6.8%	5.3%	26.4%	52.1%
CNX Energy	19,909	10.4%	5.9%	22.5%	52.4%
CNX FMCG	35,243	4.8%	8.6%	11.1%	20.3%
CNX Pharma	14,052	4.3%	17.8%	18.7%	43.8%
CNX IT	27,115	5.7%	11.6%	24.6%	93.5%

Source: Bloomberg

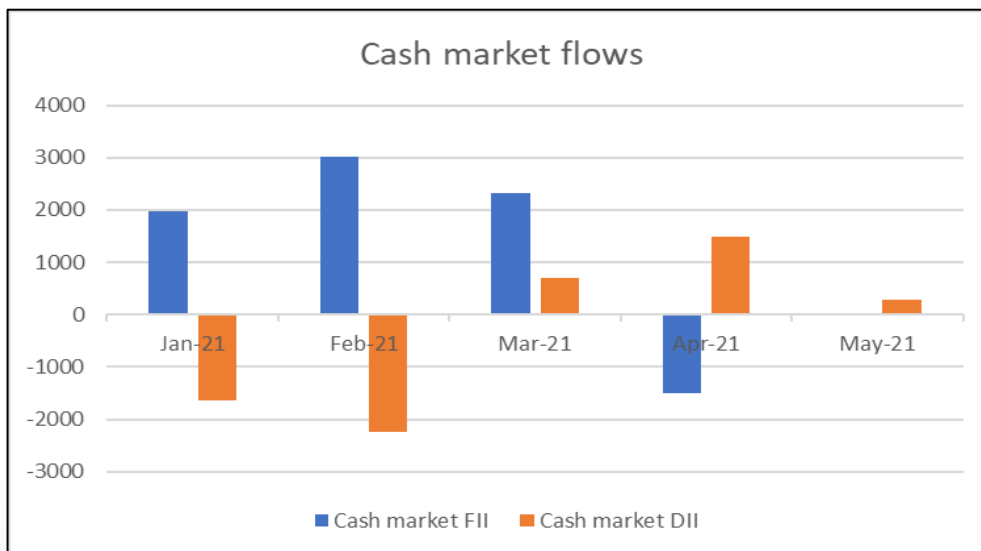
EQUITY OUTLOOK

Economy Recovering

The second Covid wave is steadily receding, leaving behind a distressing humanitarian crisis. In the short term, the “unlock” impact would be positive as businesses that are directly impacted by closures start to slowly recover. There are, however, lingering worries over the revival. The impact of Covid on personal wealth and income is still uncertain. Moreover, we expect state governments to be more circumspect in opening up after the experience of Mar-May 2021. We will have to wait to see if pent-up demand plays as quickly as it did in 2020. A full consumption recovery is likely once vaccination coverage has made headway by end CY21.

Overseas flows stabilise

A remarkable feature of the May’21 rally was the weak institutional flows over the month. FII cash volumes stabilised after the sharp April’21 outflows, though there was some selling in derivatives. There was no offset from Domestic Institutional Investors (DII) buying to support the markets either. We think this is a combination of increased retail participation, enhanced confidence as the second wave receded and the broad-based earnings outlook (discussed in the next section). FII flows may not match the highs of 2HCY20 in the near term, but we see an overall positive outlook as the global economy revives against a background of abundant liquidity and an overall rebalancing towards emerging markets.



a) DII- Domestic Institutional Investors (Includes Bank, DFIs, Insurance, New Pension Scheme and MF)

b) FII data is till May 28, MF data is till May 24 and DII Data is till May 31

Source: Bloomberg, Kotak Institutional Equity

EQUITY OUTLOOK

Earnings season: Positive signs

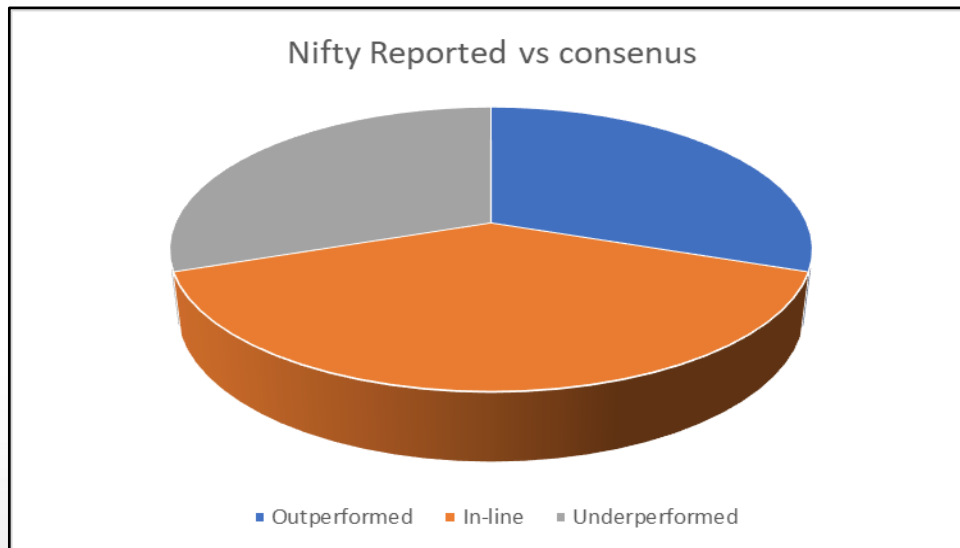
Nifty companies (ex-financials) showed a modest bounce-back in growth and profitability, despite a ~200bp drop in gross margins as the impact of commodity price inflation is starting to bite manufacturers. Financials, of course, showed a sharp growth in PAT due to the base effect of one-time COVID provisions that started in 4QFY21. Overall, there was an even distribution of surprises and disappointments in the 46 Nifty companies to have reported so far.

Non-Financials									
4QFY21	Revenue growth			EBITDA margin			PAT		
	Y/Y Chg	Q/Q Chg	2 Yr. CAGR	Reported	Y/Y Chg	Q/Q Chg	Y/Y Chg	Q/Q Chg	2 Yr. CAGR
Nifty	17%	14%	-5%	33%	7%	1%	266%	4%	8%

Source: Bloomberg, Spark Capital

Total Nifty									
4QFY21	Revenue growth			EBITDA growth			PAT		
	Y/Y Chg	Q/Q Chg	2 Yr. CAGR	Y/Y Chg	Q/Q Chg	2 Yr. CAGR	Y/Y Chg	Q/Q Chg	2 Yr. CAGR
Nifty	17%	14%	-4%	59%	19%	8%	245%	5%	9%

Source: Bloomberg, Spark Capital



Data as on 4 June 2021, Inline is +/- 3% vs consensus, source: Bloomberg.

EQUITY OUTLOOK

Preference for cyclicals

Some defensive sectors like consumer durables are showing some momentum, but we believe that cyclicals will continue to outperform. The macro tailwind is in their favour, as we think government and capital spending is more likely to drive the revival than consumption. The consumption names, no doubt, have a better history of steady growth and stronger balance sheets. The cyclical sectors are showing incremental improvement on three counts a) faster EPS growth over FY20-23, b) improved CFO/EBITDA conversion and c) improving balance sheets through deleveraging (see table below). This revival of earnings is likely to be the catalyst to a closing of the valuation gap after a multi-year outperformance from defensives.

	Defensives	Cyclicals
EPS upgrade (FY22)	3.5%	11.7%
Change in EPSg (forward over historic)	0.8%	22.1%
Change in CFO/EBITDA (FY22 over FY19)	-1.9%	14.0%
Change in DER (FY22 over FY19)	0.02	-0.33

	Defensives		Cyclicals	
	FY17-20	FY20-23 E	FY17-20	FY20-23 E
EPS CAGR	12.9%	13.7%	5.5%	27.6%
ROE	25.2%	25.5%	13.4%	13.5%
	FY19	FY22 E	FY19	FY22 E
CFO/EBITDA	72%	70%	58%	72%
Net debt/Equity	-0.19	-0.17	0.28	-0.06
PE (FY22)		39.0		22.2

Methodology

Universe: Combined coverage universe of Kotak and spark capital

Estimates: Spark (primary) and Kotak where spark did not cover

Aggregate data weighted by market capitalisation.

Sectoral classification of defensives and cyclicals is defined on next page

EPS upgrade is from 1-Oct 2020 to 4 June 2021

PE as of 24 May 2021

Source: Spark Capital, Kotak Institutional Equities, Bloomberg

EQUITY OUTLOOK

Cyclicals	Defensives
<i>Basic materials</i>	<i>FMCG</i>
<i>Chemicals</i>	<i>Consumer discretionary</i>
<i>Auto and auto ancillaries</i>	<i>Communications</i>
<i>Energy</i>	<i>Pharma</i>
<i>High NPA banks/NBFCs</i>	<i>Low-NPA banks/NBFCs</i>
<i>Realty</i>	<i>Insurance and specialty finance</i>
<i>Industrials</i>	<i>Technology</i>
<i>Utilities</i>	

Sector positioning

We remain constructive on markets and are gradually shifting towards cyclicals. Our exposure within defensives remains primarily with low-NPA lenders, pharma, and IT – the latter two gives us exposure to the global growth revival and helps diversify our risks. Our exposure in cyclicals is spread across chemicals, turnaround lenders, metals, auto ancillaries and industrials. We endeavour to mitigate the higher risk in the cyclical sectors with conservative stock selection – focusing on companies with relatively strong (or improving) balance sheets and managements with a stellar track record. We continue to minimise our cash positions and aim to fully invest as soon as possible.

Seshadri Sen
Head of Research
Alchemy Capital Management Pvt. Ltd

Source:
Alchemy Research
Bloomberg

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. Blogs – May 2021

- Battling through the Covid stress

[Read More](#)

2. Interviews – May 2021*

- 4 sectors with strong earnings momentum

[Mr. Seshadri Sen to Economic Times](#)

3. Podcast – May 2021*

- Will second wave delay earnings recovery in FY22?

[Mr. Hiren Ved to HT Smartcast](#)

*Hyperlinks to other websites made available here are to be accessed at the sole risk of the user; the content, accuracy, opinions expressed, and other links provided by these resources are not investigated, verified, monitored, or endorsed by Alchemy.

Q4 FY21 Performance of Portfolio Companies

The following table summarizes the performance of portfolio companies** for Q4 FY 21

Stock	Q4FY21	Q4FY20	% chg	Q4FY21	Q4FY20	% chg	Q4FY21	Q4FY20	% chg
3M India Ltd	8,272	6,732	23%	1,024	763	34%	705	601	17%
ABB INDIA LTD*	16,292	15,222	7%	1,323	145	812%	1,500	660	127%
Avenue Supermarts Ltd	73,031	61,935	18%	6,166	4,177	48%	4,349	2,869	52%
Bajaj Auto Ltd	85,961	68,159	26%	15,241	12,528	22%	13,321	13,103	2%
Bajaj Electricals Ltd	12,545	12,996	-3%	716	334	114%	560	0	-
Bajaj Finance Ltd	46,594	46,834	-1%	30,534	32,320	-6%	13,466	9,481	42%
Bajaj Finserv Ltd	1,53,869	1,32,943	16%	45,054	50,446	-11%	9,789	11,255	-13%
Bayer Cropscience Ltd	7,337	4,587	60%	827	582	42%	570	541	5%
Blue Dart Express Ltd	9,662	7,241	33%	1,739	157	1008%	891	-238	-
Deepak Nitrite Ltd	14,632	10,555	39%	4,547	2,621	73%	2,901	1,723	68%
Delta Corp Ltd	2,176	1,289	69%	855	580	47%	578	290	99%
Divi'S Laboratories Ltd	17,882	13,897	29%	7,163	4,445	61%	5,020	3,882	29%
Dixon Technologies Ltd	21,097	8,574	146%	798	559	43%	443	276	61%
Dr Reddy'S Laboratories Ltd	47,284	44,318	7%	10,171	9,406	8%	5,535	7,642	-28%
Eicher Motors Ltd	29,224	21,795	34%	6,685	5,033	33%	4,931	3,962	24%
Garware Technical Fibres Ltd	3,354	2,526	33%	709	552	28%	532	357	49%
Gland Pharma Ltd	8,871	6,352	40%	3,277	2,399	37%	2,604	1,948	34%
HCL Ltd	1,96,420	1,85,900	6%	50,970	47,200	8%	23,870	31,530	-24%
HDFC Bank Ltd #	2,47,141	2,12,366	16%	1,55,328	1,29,588	20%	81,865	69,277	18%
HDFC Life Insurance Company Ltd @	28,799	21,110	36%	-	-	-	7,920	5,100	55%
HDFC Ltd #	5,14,000	4,32,000	19%	46,400	39,700	17%	31,800	22,300	43%
Hindalco Industries Ltd	1,44,710	1,00,140	45%	18,790	14,450	30%	6,530	3,790	72%
ICICI Bank Ltd #	1,45,425	1,31,819	10%	85,398	73,901	15.6%	44,028	12,214	260%
L&T Infotech Ltd	32,694	30,119	9%	7,155	5,781	24%	5,457	4,274	28%
L&T Technology Services Ltd	14,405	14,466	0%	2,931	2,683	9%	1,945	2,048	-5%
Max Healthcare Ltd	10,890	10,084	8%	2,630	1,563	68%	1,090	463	135%
Multi Commodity Exchange Of India Ltd	970	1,122	-14%	442	476	-7%	384	655	-41%
Nestle India Ltd *	36,108	33,058	9%	8,805	7,426	19%	6,023	5,060	19%
Pidilite Industries Ltd	22,355	15,447	45%	4,608	3,009	53%	3,111	1,895	64%
Praj Industries Ltd	5,671	2,963	91%	749	320	134%	520	249	109%
Reliance Industries Ltd	14,95,750	13,64,920	10%	2,33,510	2,20,340	6%	1,83,670	99,140	85%
State Bank Of India	4,32,923	3,88,444	11%	1,97,001	1,84,651	7%	64,507	35,808	80%
Sundram Fasteners Ltd	10,793	7,196	50%	2,101	1,178	78%	1,302	591	120%
Syngene International Ltd	6,586	6,073	8%	2,154	2,041	6%	1,378	1,202	15%
Tata Consultancy Services Ltd^	4,37,050	3,99,460	9%	1,17,340	1,00,250	17%	92,460	80,490	15%
Tata Consumer Products Ltd	30,372	24,050	26%	3,002	3,083	-3%	539	-765	-
Tata Elxsi Ltd	5,184	4,389	18%	1,680	1,086	55%	1,152	821	40%
Tata Motor Ltd	8,86,279	6,24,930	42%	1,27,448	23,722	437%	49,998	-50,224	-
Tata Steel Ltd	4,99,774	3,37,700	48%	1,42,905	46,687	206%	86,708	21,043	312%
Titan Company Ltd	71,690	44,688	60%	7,950	6,037	32%	5,290	3,568	48%
Trent Ltd	7,737	7,228	7%	1,366	929	47%	505	26	1842%
United Spirits Ltd	22,190	19,806	12%	4,118	2,714	52%	1,673	239	600%
Varun Beverages Ltd *	22,409	16,764	34%	3,816	2,711	41%	1,368	561	144%
V-Mart Retail Ltd	3,519	3,327	6%	336	278	21%	-15	-84	-

* indicates CY end - So Q4 FY21 = Q1 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

§ Indicates Net Written Premium and PAT for general insurance companies

^ Sales EBIT and PAT

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