4 DECEMBER 2019

INDIA STRATEGY

JM FINANCIAL

The 20/20 view

JM Financial Institutional Securities Limited

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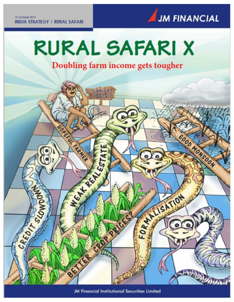
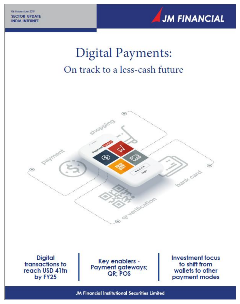
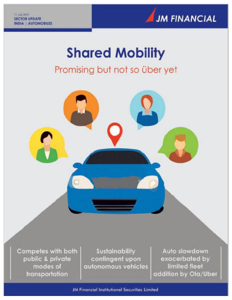


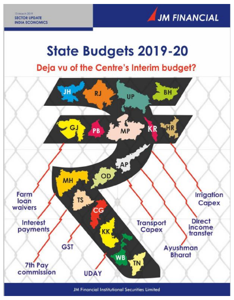
RURAL SAFARI X



DIGITAL PAYMENTS



SHARED MOBILITY



STATE BUDGETS

JM FINANCIAL

The 20/20 view

Market indices at all-time highs. Economy at its slowest pace. Enough has been debated about global flows and why the composition and earnings drivers of the main indices do not fully reflect the current slowdown. While the probability of a tail risk to economy and to the markets from a collapse of the financial system is lower owing to global and domestic backstops, macro remains mixed and a study of the earnings profile of companies under coverage is showing us that a recovery is necessary for stock price levels to give sustainable returns from here on, more so for the midcaps. We are building a recovery thesis, albeit more of a "worst is behind thesis" rather than a fully blown recovery, led by lower interest rates, fiscal measures aimed at demand side, and narrowing of corporate spreads.

A broad based recovery will continue to be stalled by i) limited fiscal space, ii) overcapacity in housing, power and iii) muted private sector capex. Based on this, the bottom-up earnings estimates yield us 11%/29%YoY growth for sales and PAT for Nifty in FY21E. For our broader coverage of 200+ stocks, similarly, we estimate 11%/26%YoY. The earnings growth leaders are the consumer discretionary, financials and materials and laggards IT, and industrials. Market multiples (NTM PE, earnings yield) are above neutral zone and while flows could take it higher, a macro recovery is essential to make it more sustainable. The move towards mid and small caps is a medium-term call, in our view, given that the contribution of the recovery factor is higher for them. Sector-wise, we recommend overweight private financials, select industrials for a recovery, tactical overweight in healthcare and maintain equal weight in IT.

1) Mixed macro now and gradual recovery next year

Sales growth has slid for last 3 quarters and estimated sales growth for 2HFY20/FY21 is 13%YoY and 11% YoY respectively for companies under coverage. Our view is for a gradual pick-up driven by lower rates, compression in spreads and demand side measures by the Govt., given low income growth (exhibit 26-28). We expect credit growth to pick up to 10-11% in FY21E from 8.1%YTD now. Inflation is likely to test nerves in 4QFY20/1QFY21 but expect it to ease towards 2H21. We expect government to use all tools including currency to try to revive growth. Our internal estimates for capex (exhibit 48) project modest capex growth over 19-22, with a resilient commercial RE.

2) How much of the earnings growth is recovery led?

We expect Nifty to post 14%YoY profit growth in FY20 and 29% in FY21 (exhibit 96). For our coverage universe, the numbers are 20% and 26%YoY respectively. Our analysis of stock-wise earnings indicates that a likely 30-50% of incremental earnings growth for Nifty and our coverage universe are dependent on a macro recovery (exhibit 98). This does not include the recovery in the pharma or the telecom sector as these are unrelated to a cyclical economic recovery. There could be some subjectivity in our analysis but looking at the sectors driving the growth next year viz., discretionary, materials and financials, the assumptions are self-evident. We believe the pharma sector, itself, is at an interesting point from a tactical perspective.

3) Pharma and healthcare – a new tactical buy

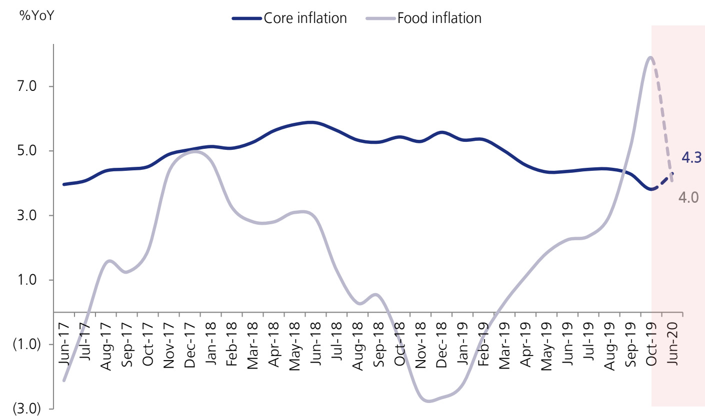
The top-down view on pharma is eye-catching with weight of the sector in Nifty down by 500bps over 5 years to ~2%, the trailing P/B (Exhibits 113-118) is at a decade low (along with drop in ROE), and under-ownership of companies with higher US businesses. At such low levels of Nifty weight, positioning vis-à-vis is meaningless and a more nuanced, bottom up approach works better. For now, we recommend a tactical overweight here and will evaluate as we see further traction. Our analyst likes Alembic, Torrent, Cipla, Natco and Sanofi (last mentioned a domestic play) but a broader "basket" approach similar to the CPSE basket might be better from a risk-reward perspective.

4) The top 5 large caps and top 10 mid/small cap picks

Among existing themes, we continue to back long-term themes of "formalisation," "financialisation," and "lower cost of capital." Overall valuations are above the neutral zone on a NTM basis (Exhibit 100) and this is not in a clear buy zone. Our recommended overweight sectors are private financials, select auto stocks, and healthcare. IT remains an equal weight. Our model portfolio and the key portfolio changes are in Exhibit 120 and 121 respectively. Our top 5 large cap picks are Avenue Supermarts, Axis Bank, Bajaj Finserv, Bandhan Bank, and Reliance Industries, and top mid/small cap picks Alembic Pharma, Ashok Leyland, Bharat Forge, CanFin Homes, Infoedge, Natco Pharma, Sundram Fasteners, Teamlease and VIP Industries.

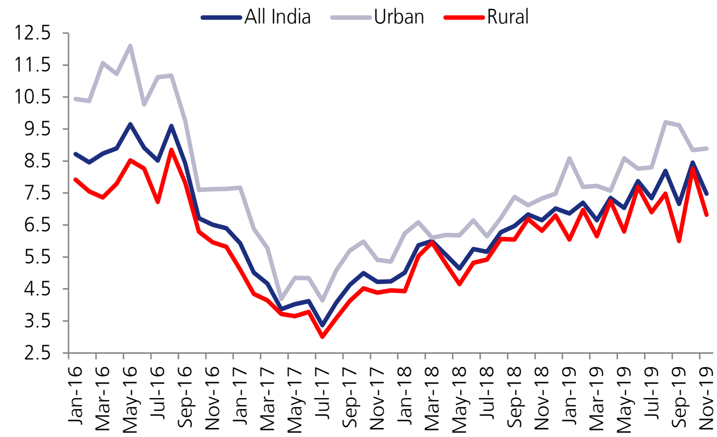
Focus Charts

Exhibit 1. Food inflation expected to cool to c.4% by Jun'20, while core inflation likely to rise to 4.3%YoY



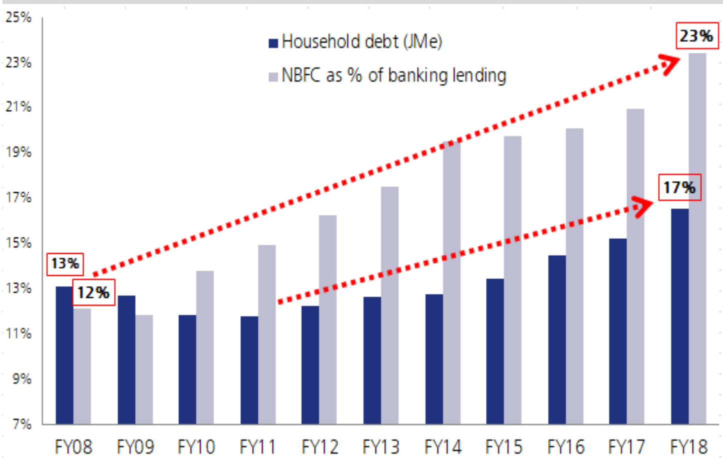
Source: CMIE, JM Financial

Exhibit 2. Unemployment rate (%) in India rising



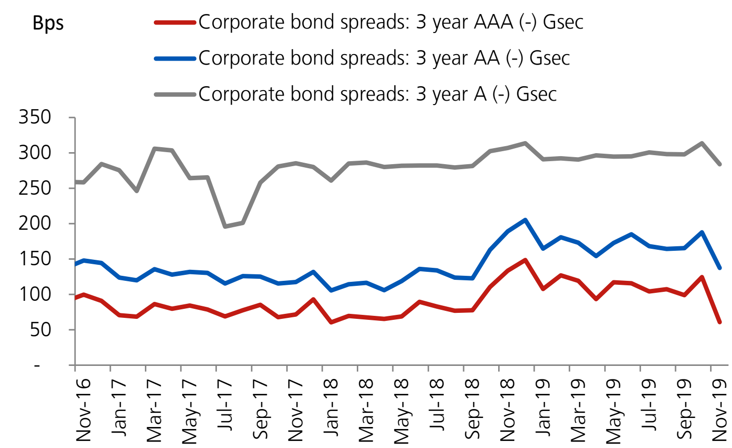
Source: CMIE, JM Financial

Exhibit 3. Household debt as % of GDP is estimated to have crossed crisis levels



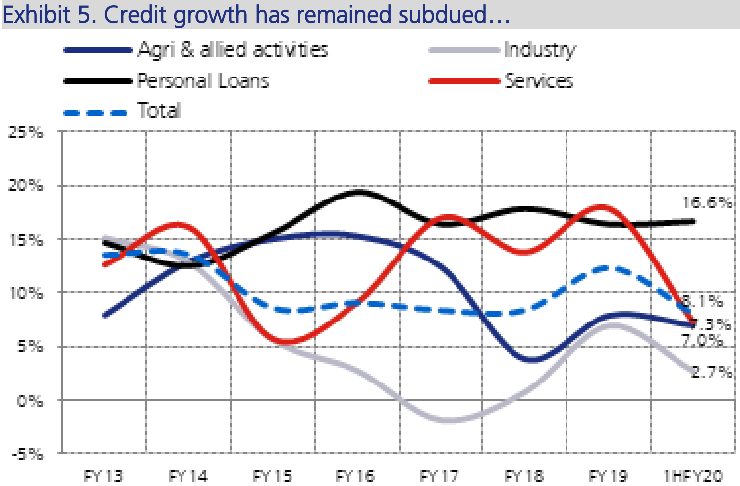
Source: RBI, JM Financial; Household debt includes i) personal loans (credit card outstanding, education, vehicles, consumer durables, housing), ii) Housing finance credit and iii) NBFC credit

Exhibit 4. Corporate bond spreads are narrowing across tenor and ratings



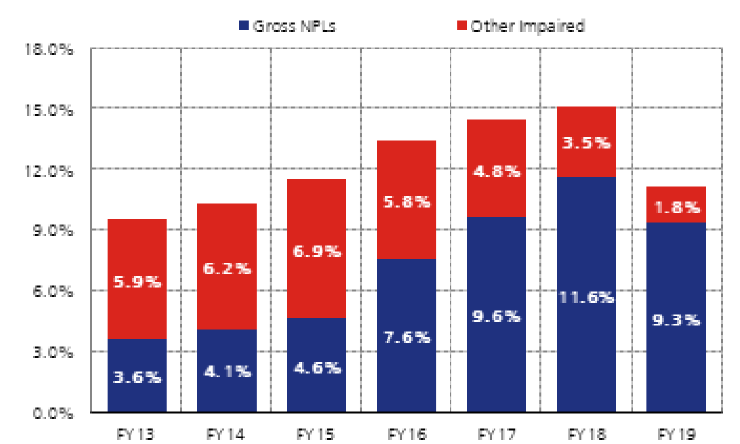
Source: Bloomberg, JM Financial

Exhibit 5. Credit growth has remained subdued…



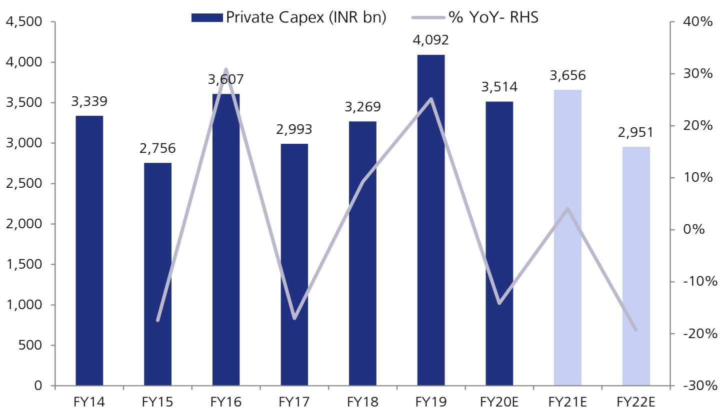
Source: RBI, JM Financial

Exhibit 6. But stress assets outlook far better



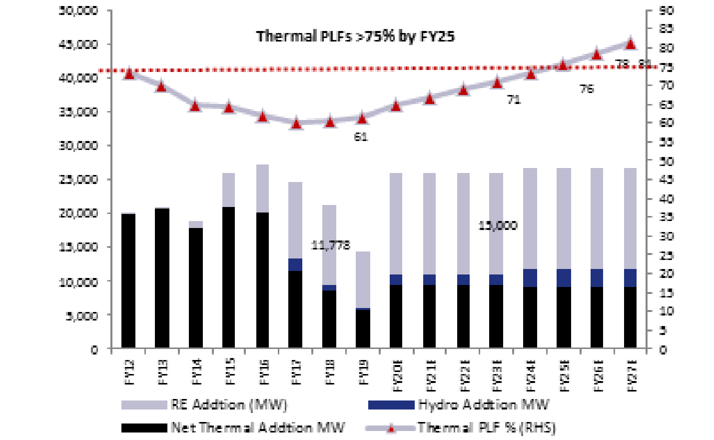
Source: RBI, JM Financial

Exhibit 7. Private sector capex to register modest growth in FY21



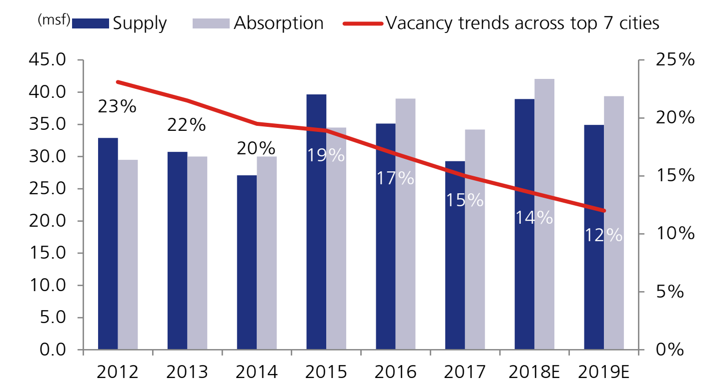
Source: Company, JM Financial; 130 companies under our coverage I

Exhibit 8. Power generation still largely renewables led



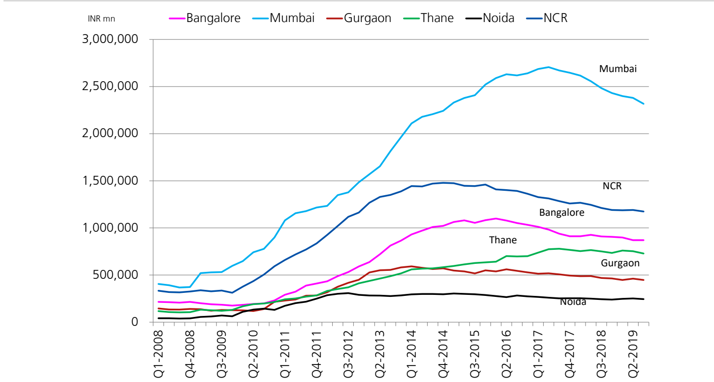
Source: JM Financial, CEA,MNRE

Exhibit 9. Increase in absorption coupled with drop in vacancy augur for well for office space capex to continue



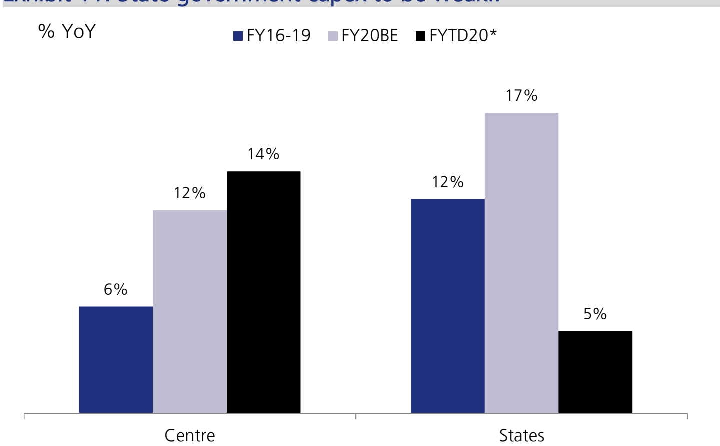
Source: Embassy REIT DRHP, CBRE, JM Financial

Exhibit 10. Off from peak inventory levels but long way to go in residential



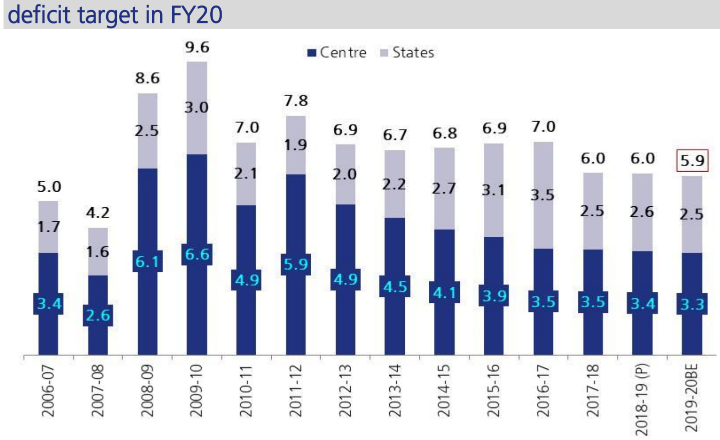
Source: Industry, JM Financial

Exhibit 11. State government capex to be weak..



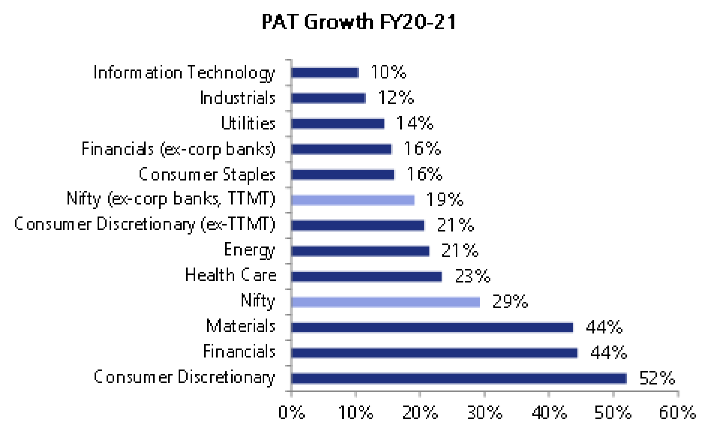
Source: Union Budget, State Budget, CGA, CAG, JM Financial

Exhibit 12. ..Given the pressures that states face to meet the fiscal deficit target in FY20



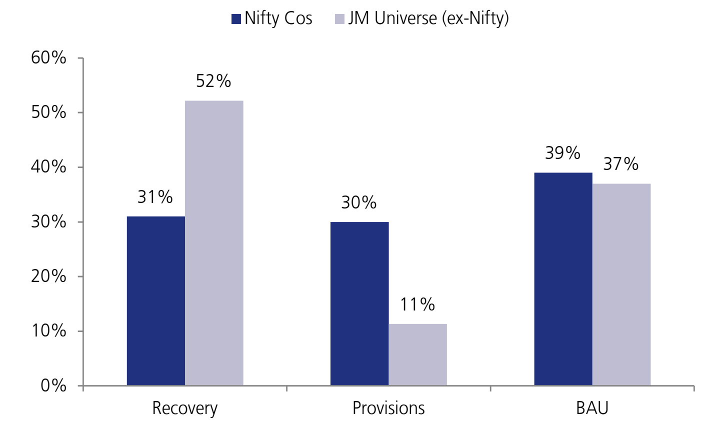
Source: CMIE, JM Financial

Exhibit 13. Estimated FY21 EPS growth for Nifty c.29%



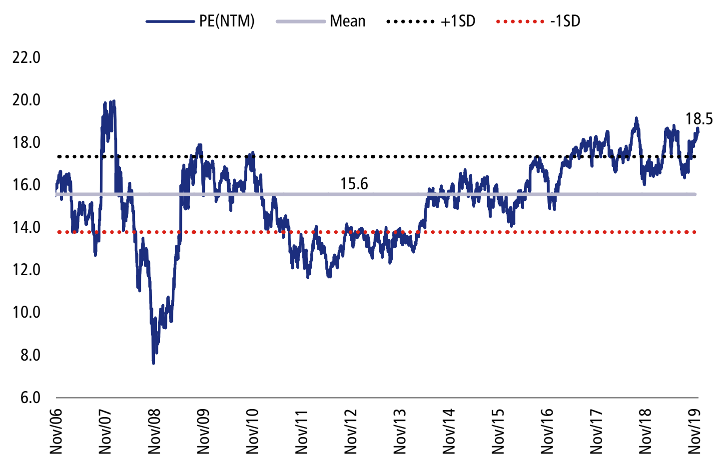
Source: JM Financial

Exhibit 14. Macro recovery crucial to deliver exp. earnings growth



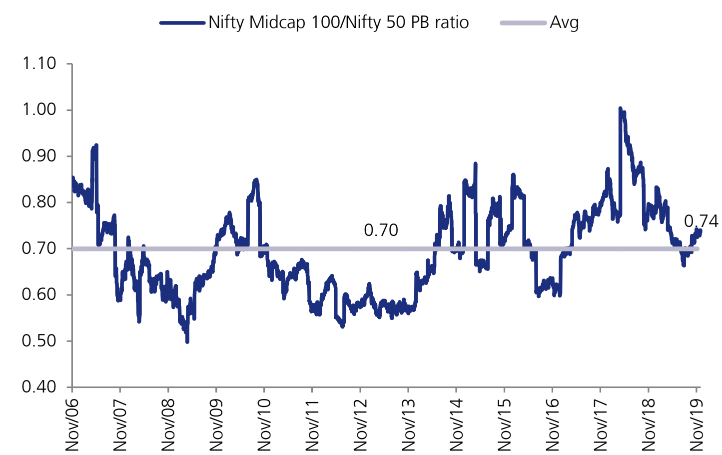
Source: JM Financial, BAU also includes inorganic growth opportunities

Exhibit 15. Nifty NTM PE at 18.5x



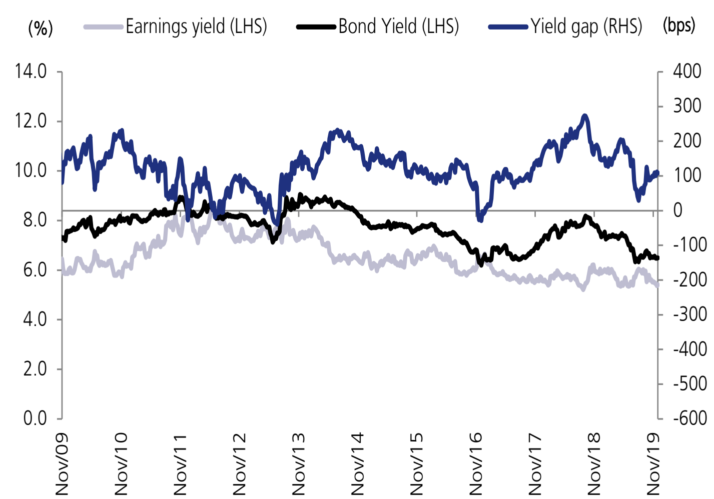
Source: Bloomberg, JM Financial

Exhibit 16. Nifty Midcap 100 to Nifty PB (TTM) at 0.74



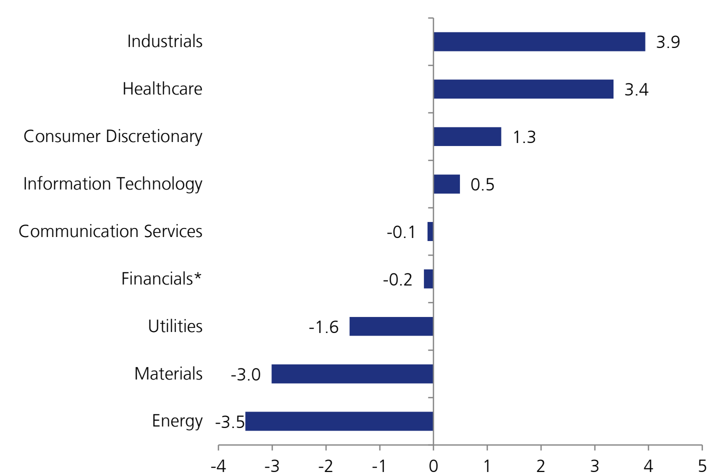
Source: Bloomberg, JM Financial

Exhibit 17. Yield gap (10yr bond yield-Earnings yield) ~110bps



Source: Bloomberg, JM Financial

Exhibit 18. JM portfolio weight over Nifty weight (OW on Industrials & Healthcare)



Source: JM Financial, *overweight on private financials

Calendar

Calendar 2019-20

Oct'19	Nov'19	Dec'19	Jan'20
• RBI Monetary Policy • Canadian General elections • ECB Monetary policy • FOMC meeting • Maharashtra and Haryana assembly elections • 2QFY20 result season • Deadline for the 15th Finance Commission to submit recommendations • Mario Draghi's term as ECB's Chairman ends	• Declaration of Rabi MSP for 2019-20 • Jharkhand assembly elections • 2QFY20 result season • IMF's meeting on Indian economy	• RBI Monetary Policy • ECB Monetary policy • FOMC meeting • Rabi sowing progress • Bank of Japan Monetary Policy Meet • OPEC meeting • Jharkhand assembly election results	• Economic Survey • 3QFY20 result season • Bank of Japan Monetary Policy Meet • FOMC meeting • ECB Monetary policy • Delhi assembly elections
Feb'20	**Mar'20**	**Apr'20**	**May'20**
• Union Budget • RBI Monetary Policy • 3QFY20 result season	• Bank of Japan Monetary Policy Meet • FOMC meeting • ECB Monetary policy	• 4QFY20 result season • RBI Monetary Policy • Bank of Japan Monetary Policy Meet • FOMC meeting • ECB Monetary policy • IMD initial forecast for monsoon	• 4QFY20 results season
Jun'20	**Jul'20**	**Aug'20**	**Sep'20**
• RBI Monetary Policy • Bank of Japan Monetary Policy Meet • FOMC meeting • ECB Monetary policy • IMD revised forecast for monsoon • MSP declaration for Kharif season	• ECB Monetary policy • FOMC meeting • 1QFY21 result season	• RBI Monetary Policy • Progress of monsoon and Kharif sowing • 1QFY21 result season	• FOMC meeting
Oct'20	**Nov'20**	**Dec'20**	
• RBI Monetary Policy • ECB Monetary policy • FOMC meeting • 2QFY21 result season • Bihar assembly elections	• Declaration of Rabi MSP for 2020-21 • 2QFY21 result season • US presidential elections	• RBI Monetary Policy • ECB Monetary policy • FOMC meeting	

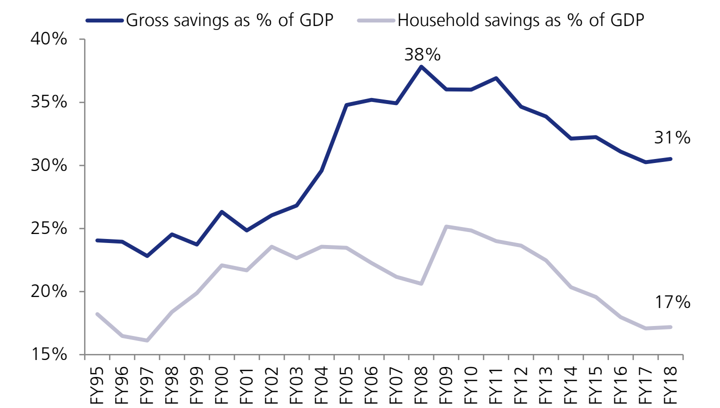
Growth Outlook- Hinges on the play out of its pillars

GDP= C+ I + G + NX

Consumption (C)

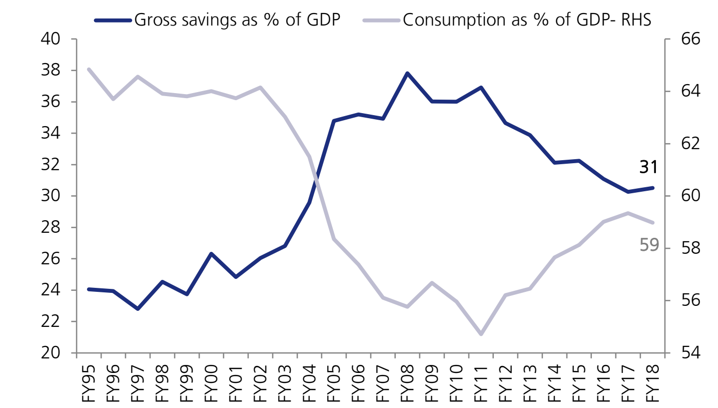
Over the years, India's gross savings-to-GDP ratio has declined from 37.8% in FY08 to 30.5% in FY18. This has been accompanied by an increase in private consumption as % of GDP from 56% in FY12 to 59% in FY18 (exhibit 19,20). Quarterly volume growth in various consumer companies reveals moderation in private consumption- exhibit 21.

Exhibit 19. Declining gross domestic savings as % of GDP driven by the fall in household savings that constitute c. 56% share



Source: CMIE, JM Financial

Exhibit 20. … which is partly explained by the rise in consumption as % of GDP



Source: CMIE, JM Financial

Exhibit 21. Growth in various indicator of some consumer companies has been in the red zone

% YoY	1QFY17	2QFY17	3QFY17	4QFY17	1QFY18	2QFY18	3QFY18	4QFY18	1QFY19	2QFY19	3QFY19	4QFY19	1QFY20	2QFY20
FMCG- Volume growth														
Asian Paints	12%	12%	3%	12%	1%	9%	6%	9%	13%	10%	19%	10%	17%	15%
Berger paints	12%	9%	7%	12%	6%	7%	9%	9%	15%	12%	19%	11%	15%	13%
HUL	4%	-1%	-4%	4%	0%	4%	11%	11%	12%	10%	10%	7%	5%	5%
Colgate	5%	4%	-12%	-3%	-5%	-1%	12%	4%	4%	7%	7%	3%	4%	4%
Dabur	4%	5%	-5%	2%	-4%	7%	13%	8%	21%	8%	12%	4%	10%	5%
Titan (Jewellery)	6%	-32%	4%	37%	49%	49%	6%	6%	-3%	24%	20%	15%	6%	-14%
Jubilant Foodworks	-3%	4%	-3%	-8%	7%	6%	18%	27%	26%	21%	15%	6%	4%	5%
Westlife	3%	7%	5%	1%	9%	8%	21%	25%	24%	26%	15%	6%	7%	7%
BUILDING MATERIALS- Volume growth														
Kajaria	6%	3%	1%	11%	3%	5%	10%	5%	9%	11%	16%	11%	10%	1%
Somany	3%	11%	1%	13%	-16%	4%	6%	2%	18%	-4%	8%	-3%	8%	5%
Century Ply	18%	-1%	1%	1%	12%	-2%	5%	8%	8%	13%	7%	-4%	1%	-1%
AUTO- domestic Sales														
4w (Only MSIL)	5%	18%	4%	15%	14%	19%	12%	11%	25%	-1%	1%	0%	-19%	-31%
Tractors- Only M&M	21%	37%	21%	14%	14%	34%	6%	44%	20%	-4%	13%	-15%	-15%	-7%
Hero Motorcorp	6%	16%	-13%	-6%	6%	11%	16%	23%	14%	5%	5%	-11%	-12%	-21%
2-wheeler sales	14%	21%	-5%	-2%	8%	12%	16%	25%	16%	5%	8%	-9%	-12%	-21%
4 -wheeler sales	0%	18%	0%	11%	4%	13%	6%	7%	20%	-4%	-1%	-2%	-18%	-29%
REAL ESTATE- Volume of inventory sold														
Prestige Estates	3%	-5%	-39%	-53%	-16%	-18%	41%	112%	61%	66%	55%	34%	4%	-11%
Sobha	-4%	1%	-24%	-18%	1%	1%	52%	40%	18%	20%	-3%	11%	11%	0%
Oberoi	83%	181%	-90%	-5%	-34%	-2%	43%	-3%	193%	38%	-3%	11%	-16%	-42%
Godrej	-55%	-41%	16%	-17%	204%	111%	20%	150%	-35%	-31%	95%	153%	15%	111%
HEALTHCARE- Patient volumes														
Dr. Lal		31%	7%	-3%	-5%	29%	19%	8%	5%	26%	10%	2%	2%	23%
TELECOM														
Mobile Broadband subscribers	55%	67%	82%	94%	95%	76%	58%	53%	52%	51%	47%	38%	34%	
Total mobile subscr..	6%	5%	12%	13%	15%	13%	4%	1%	-3%	-1%	1%	-2%	2%	
Data consumed	52%	115%	613%	685%	782%	629%	127%	133%	148%	131%	119%	96%	72%	

Source: Company, JM Financial

We believe that the key factors driving consumption are income growth and financing availability, which have been elaborated below:

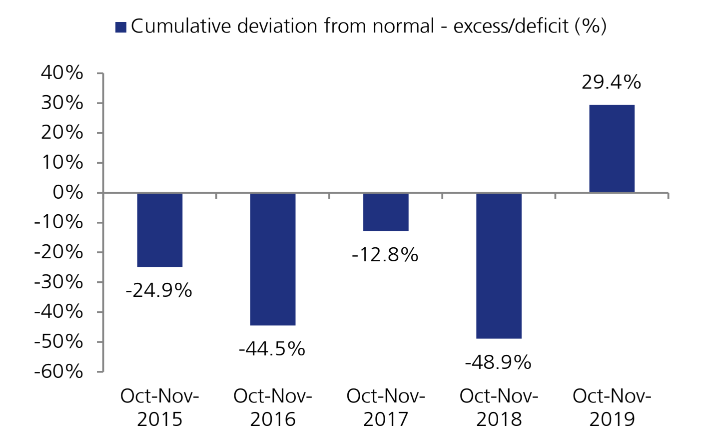
A.Income growth

This factor further relies primarily on i) rural income growth, ii) jobs creation, and iii) wealth effect.

i) Rural income: Rural households contribute around 50% to GDP, 40% of FMCG sales, 50% two-wheeler sales, 30% four wheeler sales and 45% telecom contribution (FICCI Oct'18). Rural had been faring better than urban till late 2018, however head-winds such as i) weak agri based pricing (Food deflation in late 2018 & early 2019), and ii) declining exports impacted farm income. On the other hand i) weak credit disbursement environment post NBFC-led crisis (post Sep'18) and ii) formalisation efforts weakened non-farm income, as discussed in Rural Safari X | Doubling farm income gets tougher.

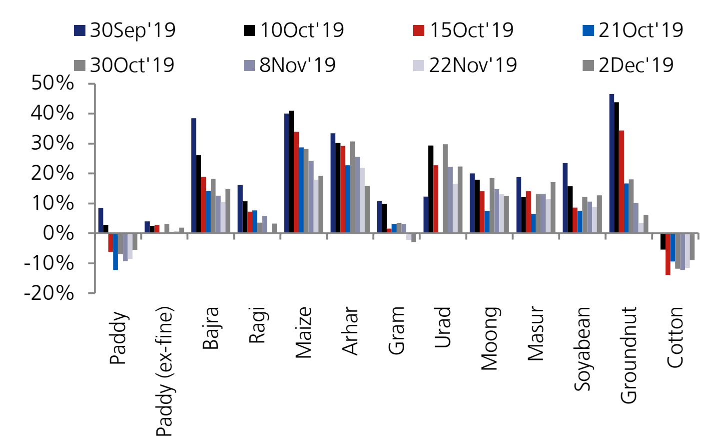
After a flat YoY sowing in Kharif season, we do expect, rabi sowing to be delayed, but better YoY in FY20 (FY19: -4% YoY), given higher than normal rainfall (10% ahead of LPA) in 2019. In terms of farm income, kharif output has seen impact on quantity & quality given, let rains, even in harvest period (Oct-Nov'19), and therefore agri-commodity prices are sustaining YoY higher levels (coarse cereals, Pulses, oilseeds & vegetables etc.). As a result, on an aggregate farm income can see a better YoY benefiting farm inputs in particular (tractor sales). **However, the sluggish trend in non-farm income growth (impacted by lower liquidity, weak exports, low rural wage growth) would constrain any material pick-up in rural consumption.**

Exhibit 22. Excess rains after end of Monsoon, adversely impacted kharif crop output quality in 2019



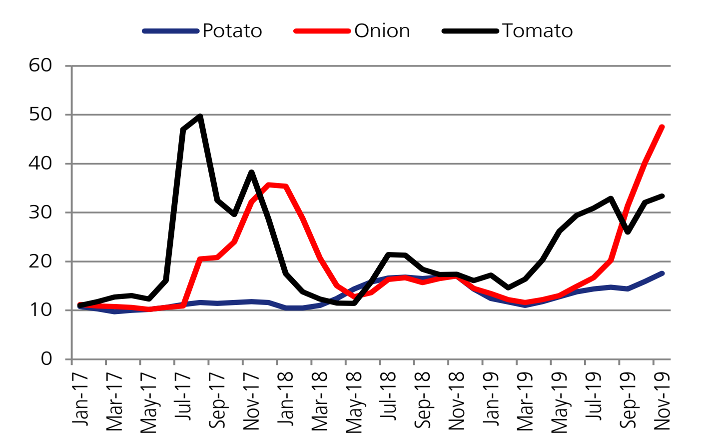
Source: CMIE, JM Financial

Exhibit 23. Supply side challenges have led to higher agri prices (YoY%, wholesale) than last year; sustainance is still uncertain



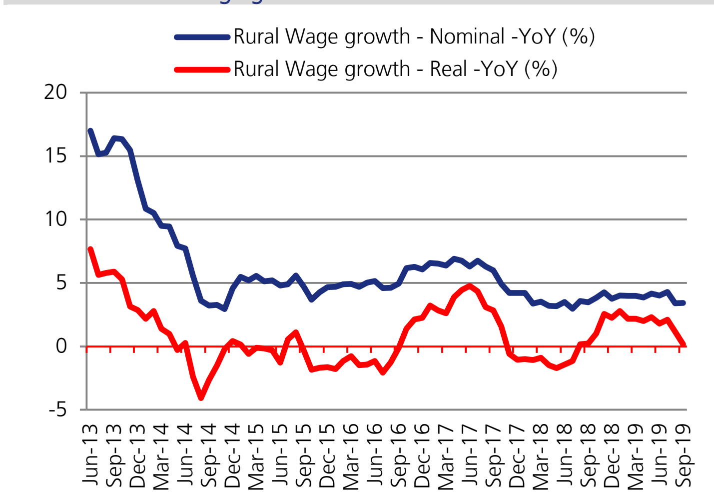
Source: agmarknet, JM Financial, Note: Average of modal prices of agri-mandis

Exhibit 24. Food inflation can see a spike in near-term; largely on account of vegetable price increases (wholesale, INR/kg)



Source: Ministry of Consumer Affairs, CMIE, JM Financial

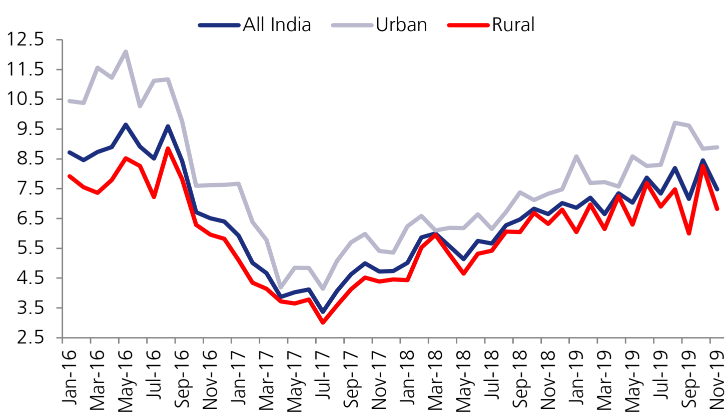
Exhibit 25. Rural wage growth remains subdued



Source: CMIE, JM Financial

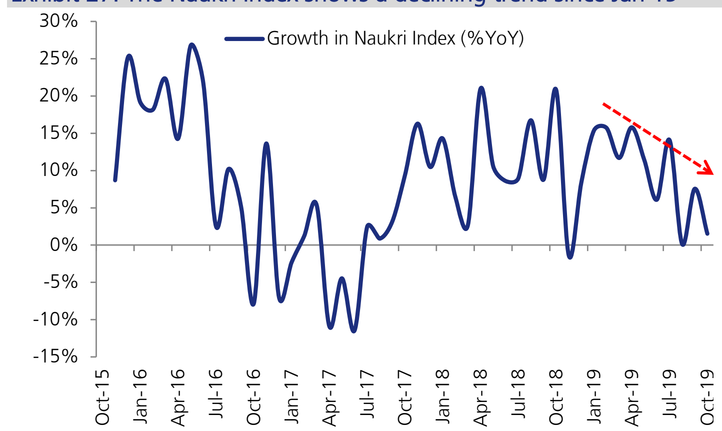
ii) **Job-creation in the economy:** The Government has been releasing payroll additions and increase in EPFO. According to the latest series, during the period Sep'17-Sep'19 -i) c.28.5mn new subscribers joined the EPF scheme, ii) 31mn new enrolments happened under ESI, and iii) 1.5mn new subscribers came under the national pension system (NPS). However, job prospects do not seem all that rosy. The unemployment rate as calculated by the CMIE is on the upward trajectory, while the Naukri Job Index growth has been moderating (exhibit 26,27). The number of students passing out with degrees has grown 4.7% (FY12-16), driving the demand-supply mismatch.

Exhibit 26. Unemployment rate (%) in India rising



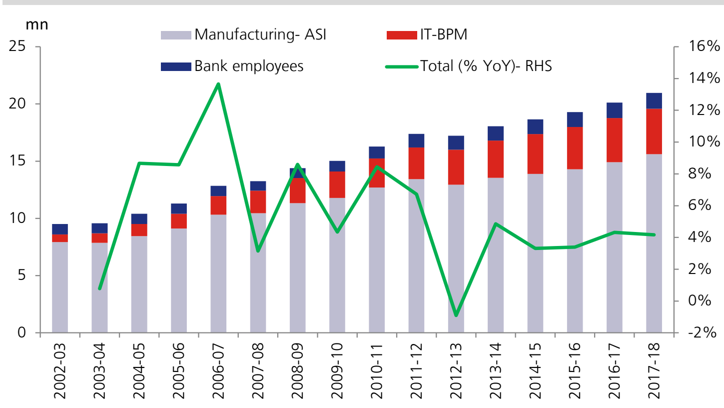
Source: CMIE, JM Financial

Exhibit 27. The Naukri Index shows a declining trend since Jan'19



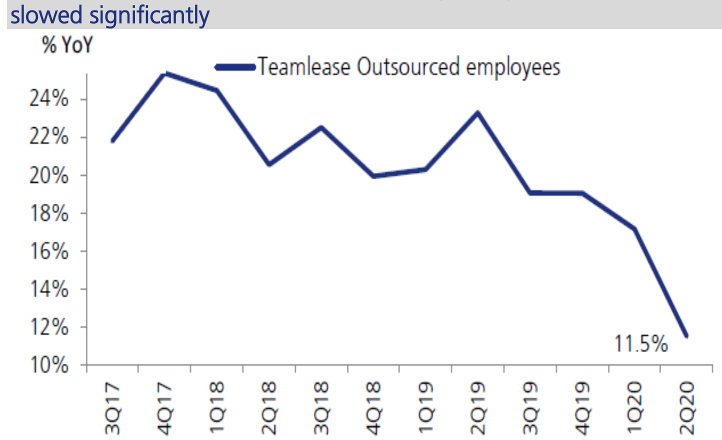
Source: CMIE, JM Financial

Exhibit 28. Moderation in employment growth in major organized sectors



Source: CMIE, RBI, MOSPI, NASSCOM, JM Financial

Exhibit 29. Growth in outsourced employees by Team lease too has slowed significantly



Source: Teamlease, JM Financial

Box 1 : Job losses at Middle management level in IT companies

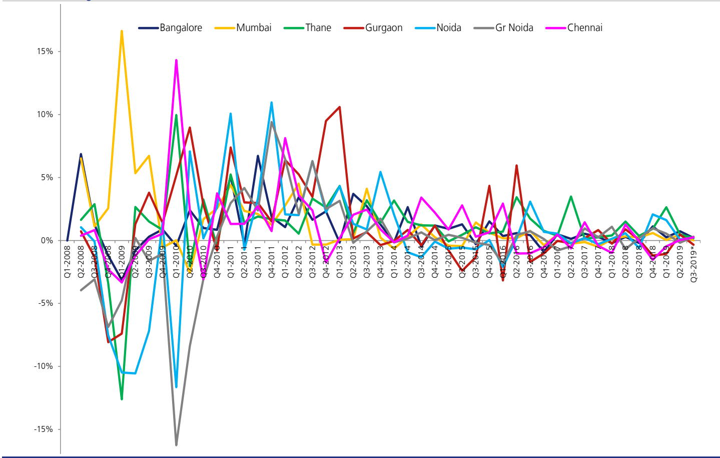
Barring Cognizant, no other company has publically announced a job cut. Cognizant has formally said it plans to remove 10,000 to 12,000 mid-to-senior level employees from their current roles, of which, it aims to re-skill and redeploy 5,000. This means net 5,000-7,000 people could get laid-off. This translates to 1.7-2.4% of their current headcount. Typically, involuntary attrition is ~1.5% for the Top5 companies (excluding CTSH). If each of those companies decides to do similar bench cuts like CTSH, this could imply a combined c.23,000 cut at mid-to-senior level, assuming 2% attrition. At current levels of 1.5%, the combined cut would be 17,000. We don't believe that mid-tier companies would see any major spikes as they normally do not carry a large experienced bench. Growth uptick in head count of certain IT firms in FY20 shown below:

% YoY	Q217	Q317	Q417	Q118	Q218	Q318	Q418	Q119	Q219	Q319	Q419	Q120	Q220
TCS	11%	10%	9%	7%	5%	3%	2%	4%	6%	7%	7%	9%	10%
Infosys	6%	3%	3%	1%	-1%	1%	2%	6%	10%	12%	12%	9%	9%
Wipro*	-5%	-4%	-4%	2%	0%	-3%	-3%	0%	8%	9%	7%	9%	6%
HCLT	4%	7%	11%	9%	8%	7%	4%	5%	7%	11%	15%	16%	15%
TechM	7%	9%	12%	8%	4%	-2%	-4%	-2%	1%	6%	7%	11%	11%
Cognizant	12%	17%	17%	12%	5%	0%	0%	0%	5%	7%	8%	9%	7%

Source: Company, JM Financial; * incl. subcontractors till FY16

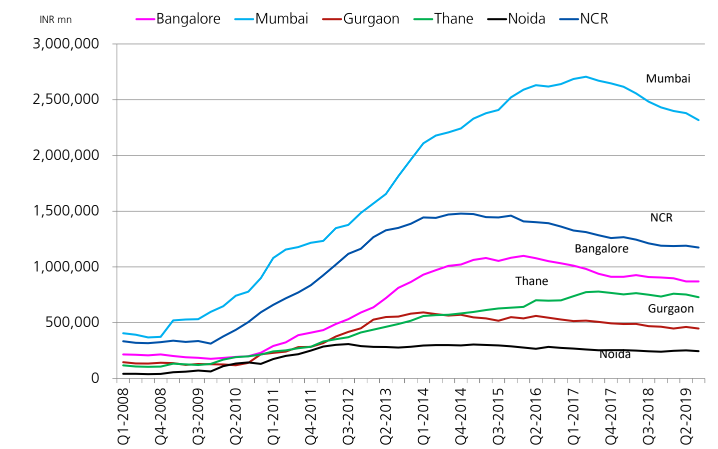
iii) **Land prices and wealth effect:** For rural India, overall, wealth effect continues to remain weak, impacting large ticket consumption. Our recent visits (Sep-Oct'19) indicate limited positive momentum in some regions such as Bihar (benefit from urbanisation), Telangana (on account of digitisation of land records), while the stopping of infrastructure projects at Amaravati (proposed capital of Andhra Pradesh) has dampened land prices in the region. Yet to encounter a sustained increase in rural land prices and barring regions adjacent to urban areas or where large infrastructure projects are coming up, we do not see much evidence of land transactions picking up as yet. For urban India, property prices in the top 5 cities have stagnated in the past 5 years (Exhibit 30)

Exhibit 30. Prices continue to remain subdued on the back of excess inventory



Source: Various, JM Financial

Exhibit 31. Off from peak inventory levels but long way to go in residential



Source: Industry, JM Financial

BOX 2: Personal Income tax on the way?

- As per various media reports, the Govt. is considering to adopt a personal income tax cut in the Union budget to stimulate the slowing economy. Reduction in income tax rates affect the behaviour of individuals through both income and substitution effects. Making leisure more expensive, the subsitution effect of lower tax rates encourages people to work more, while the income effect tends to reduce labour supply by prompting a sense of higher real income. Assessing the likely impact of the tax cut is an empirical question. The tax cut experience (both corporate and income tax) in the US shows that the contribution to the rise in GDP after one year of the tax cuts was highest due to consumption. However, it is not certain whether this came more from the rise in hourly wages post the corporate tax cuts, or due to the personal income tax cut.
- In our view, a personal income tax could induce higher precautionary savings if the economy is unable to revive sentiments and perceives the tax cut as temporary given that i) the govt. is fiscally inclined towards consolidation, and ii) tax cuts could be financed in future by raising taxes on other goods/services. According to our calculations, if income tax rates are cut as per media reported DTC suggestions (see below) , the Centre may have to bear the brunt of c. INR 1trn in FY21 which is c.50-60bps of the GDP. The multiplier effect of a personal income tax cut has been empirically found (by a study by NIPFP based on data for the period 1991-2012) to be -1.01 which implies that every 1 unit cut in taxes, increases GDP by 1.01 units. This in turn could translate into a monthly peak benefit of c.INR 2,000-2,500 on an average for some 50mn return filers. This gain could be lower depending upon the withdrawal of exemptions.

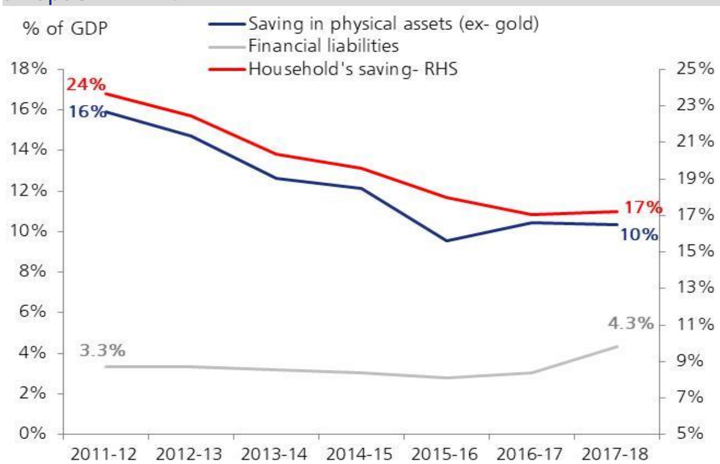
INCOME TAX BRACKETS			
CURRENT		DTC PROPOSAL	
Up to 2.5 lakhs	Nil	Up to 5 lakhs	Nil
2.5-5 lakhs	5%	5-10 lakhs	10%
5-10 lakhs	20%	10-20 lakhs	20%
Above 10 lakhs	30%	20 lakhs-2 crores	30%
		Above 2 crores	35%

Source:Media

B. Financing conditions better than a year before

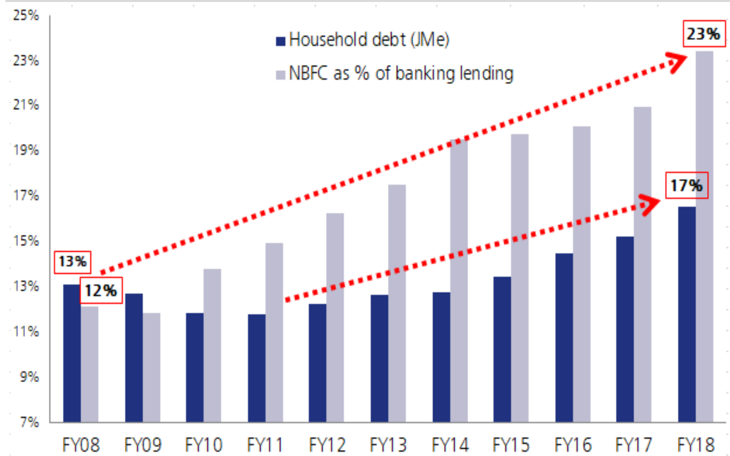
Availability of finance for consumption has driven household debt in the recent years. We calculate household debt as the sum of outstanding i) personal loans from SCBs (consumer durables, education, credit cards outstanding, vehicles), ii) NBFC credit, and iii) HFC credit. We find that the household debt-to-GDP ratio has grown from c.13% in FY08 to c.17% in FY18, i.e. higher than 2008 crisis levels (exhibit 33). Household financial liabilities at the same time have seen a sharp rise in FY18 to 4.3% vs. c.3% previously (exhibit 32). While higher debt-to-GDP ratio's are associated with higher economic growth in the short-run with reversal of effects in three to five years (IMF Oct'17), it should be noted that these numbers are significantly lower than other nations like China (53.6%) or the US (75%). Thus, outlook on consumption will continue to depend in the lending ability of the banks and NBFCs.

Exhibit 32. Financial liabilities of households as a % of GDP have seen an uptick in FY18



Source: RBI, JM Financial

Exhibit 33. Household debt as % of GDP is estimated to have crossed crisis levels



Source: RBI, JM Financial; Household debt includes i) personal loans (credit card outstanding, education, vehicles, consumer durables, housing), ii) Housing finance credit and iii) NBFC credit

Exhibit 34. Retail loan growth for banks and NBFCs has moderated

NBFCs														
AB Capital								128%	110%	48%	61%	41%	41%	33%
BAF	53%	58%	51%	141%	117%	109%	98%	22%	31%	35%	43%	47%	45%	43%
CIFC	18%	18%	16%	14%	15%	16%	21%	25%	30%	32%	30%	30%	27%	24%
HDFC	19%	18%	17%	16%	16%	15%	17%	19%	18%	19%	18%	-14%	-14%	-10%
Indostar									176%	203%	175%	343%	228%	145%
LICHF	15%	15%	14%	14%	14%	14%	15%	15%	13%	13%	14%	14%	15%	15%
LTFH	13%	15%	13%	11%	25%	33%	52%	68%	73%	67%	60%	47%	34%	22%
Magma	-3%	-3%	-3%	-9%	-10%	-10%	-11%	-4%	-3%	0%	-3%	1%	5%	1%
MMFS	3%	2%	6%	10%	13%	4%	-1%	6%	13%	24%	24%	25%	20%	18%
PNB Housing				43%	41%	49%	55%	46%	43%	33%	26%	28%	20%	12%
Repco	25%	24%	21%	16%	13%	10%	10%	10%	12%	11%	12%	12%	13%	11%
SCUF	14%	10%	15%	15%	19%	20%	15%	15%	14%	12%	-1%	-2%	-1%	-2%
SHTF	84%	57%	45%	-15%	-15%	5%	16%	35%	33%	34%	21%	7%	-27%	-3%
BANKS														
Yes Bank	71%	65%	26%	17%	48%	79%	101%	100%	105%	102%	83%	62%	44%	30%
IndusInd	29%	27%	25%	25%	22%	22%	24%	26%	28%	29%	28%	27%	24%	21%
Axis	26%	26%	23%	27%	29%	29%	32%	23%	21%	20%	20%	19%	22%	23%
ICICI	22%	21%	17%	18%	19%	19%	22%	21%	20%	21%	22%	22%	22%	22%
HDFC	29%	25%	18%	26%	25%	26%	34%	26%	25%	23%	23%	19%	16%	14%
Kotak	19%	20%	16%	20%	24%	26%	33%	34%	33%	31%	30%	29%	26%	20%
BOB	-2%	-2%	-1%	14%	6%	11%	33%	19%	34%	34%	18%	24%	56%	49%
PnB	20%	22%	12%	14%	16%	16%	22%	15%	10%	14%	15%	22%	22%	19%
SBI standalone	20%	20%	18%	21%	45%	44%	44%	38%	14%	14%	18%	19%	19%	19%
Federal	8%	22%	27%	26%	28%	17%	14%	18%	18%	20%	22%	24%	26%	25%

Source: Company, JM Financial

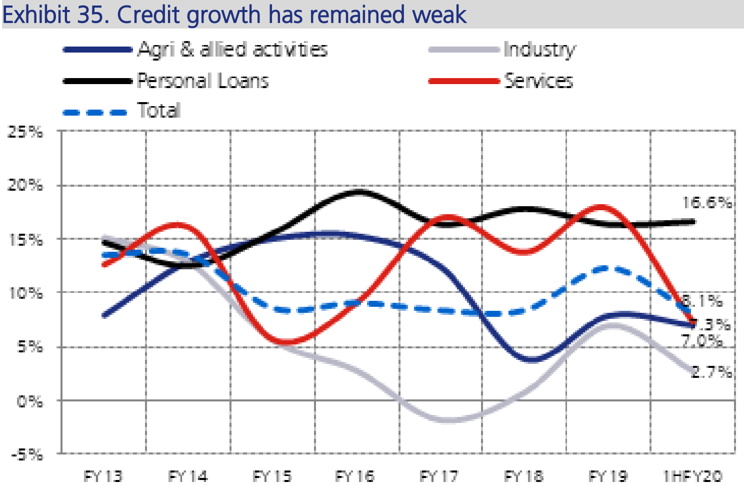
1. Banking sector

Loan growth expected to be c.10-11% over the next 18 months: Loan growth has moderated to 8.1% YoY as on Sep'19 and we expect the loan growth to remain muted at 10-11% over the next 18 months. The lower loan growth is largely driven by the muted outlook for corporate loan growth as private sector capex remains weak. Retail loan growth is also expected to moderate, largely due to weakness in vehicle finance and the SME space.

PSU banks consolidation - Bold step; however positives to flow only gradually: GoI announced consolidation of 10 PSU Banks into 4 PSU which will bring down overall count of PSU banks to 12. We see this move as positive over the longer term primarily ensuring easier governance/management, better transparency and potentially better efficiencies if executed well. In the near-term, however, as these banks go through the merger process, a significant proportion of management/employee bandwidth is likely to get consumed / diverted away from growth and resolutions and could be a drag on overall environment (these banks form c.23% of overall credit of the banking system). On the other hand, we expect the private banks to continue to gain market share supported by their comfortable capitalisation, better asset quality and healthy liability franchisee.

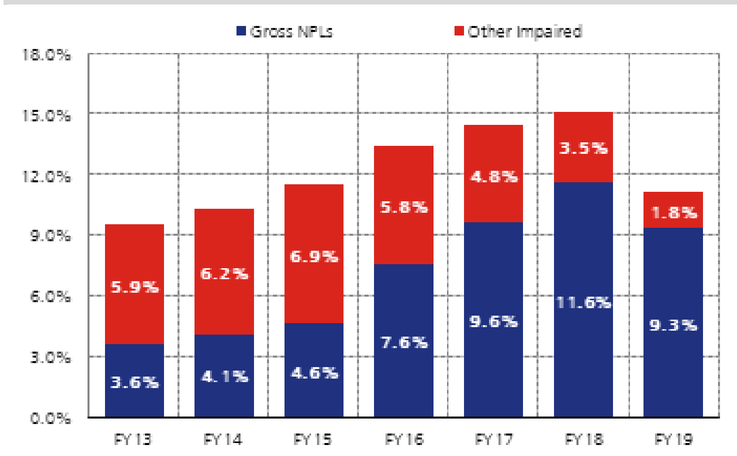
New stress formation has reduced; albeit credit cost moderation is dependent on resolution of newer stressed names: GNPLs for the banking system has reduced to 9.3% as of Mar'19 with resolutions in certain large ticket size exposures and also moderation in slippages. Further, stress recognition for the banking sector has improved, with impaired asset ratio (not classified as NPA) now at 1.8%. However, emergence of newer stressed names (as witnessed over the past few months) may delay the normalisation of credit costs which in turn may delay the expansion in return ratios for corporate banks.

Exhibit 35. Credit growth has remained weak



Source: RBI, JM Financial

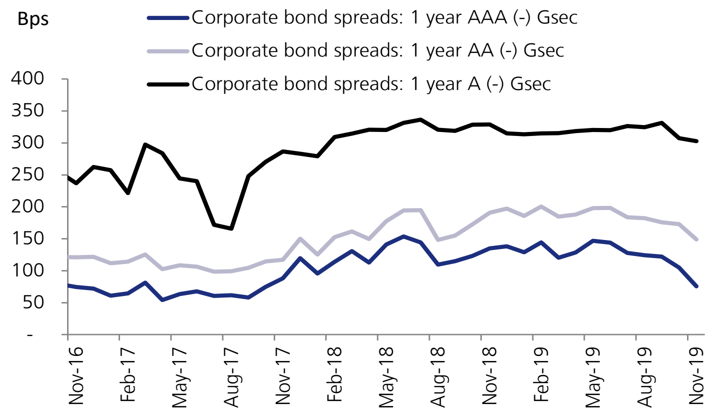
Exhibit 36. But stress assets outlook far better



Source: RBI, JM Financial

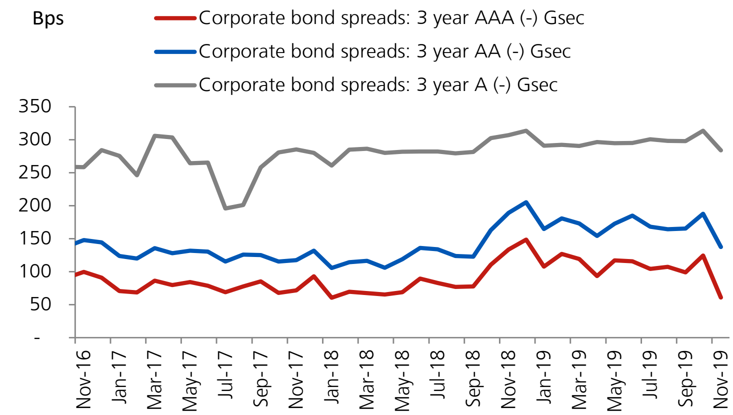
Liquidity has improved; rate transmission expected to improve further: System liquidity has been positive (at INR 2 trn as of Nov'19) since June'19 (after 9 months of tight liquidity) supported by INR 3 trn durable liquidity (OMO) infusion by RBI since Oct-18. Excess system liquidity (in conjunction with implementation of external benchmark linked retail loans) should aid in increased transmission of rates by banks. Further, risk perception in the system is also improving gradually with narrowing corporate spreads.

Exhibit 37. Corporate bond spreads are narrowing….



Source: Bloomberg, JM Financial

Exhibit 38. … across tenor and ratings

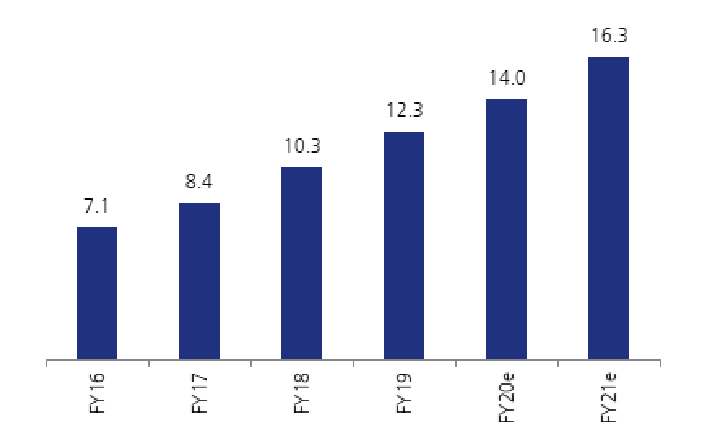


Source: Bloomberg, JM Financialt

2. NBFCs

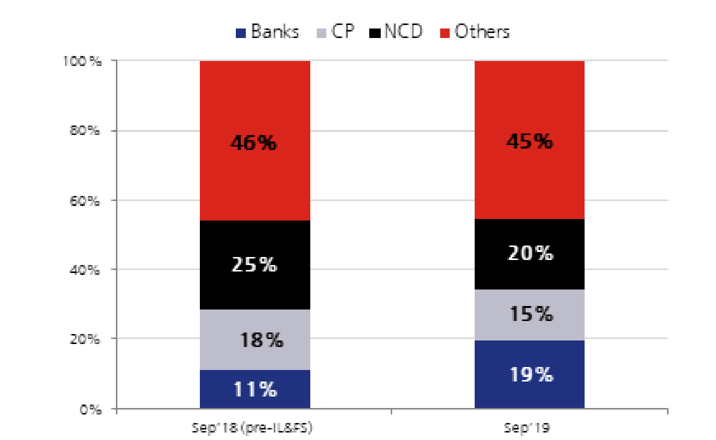
We expect a broader consumption slowdown including autos will weigh on growth in the near term. We are building in an 15% AUM CAGR over FY19-21E for our coverage vs. 20% AUM CAGR over FY16-19. On the liability side, credit flow from banks to NBFCs will be key as capital market participants are expected to remain on the side-lines – share of bank funding has gone up to 19% of Sep'19 borrowing mix vs. 11% pre IL&FS. NBFCs may witness softening rates especially the better rated NBFCs thus aiding spreads favourably. Coming to asset quality, it is expected to remain stable albeit with certain lumpy slippages in the real estate space. Key catalyst going forward is implementation of the INR250bn RE fund announced by the GOI for completion of stuck projects in affordable and mid-housing segment

Exhibit 39. Aggregate AUM for NBFCs (covered)- INR trn



Source: Company, JM Financial

Exhibit 40. Aggregate borrowing mix



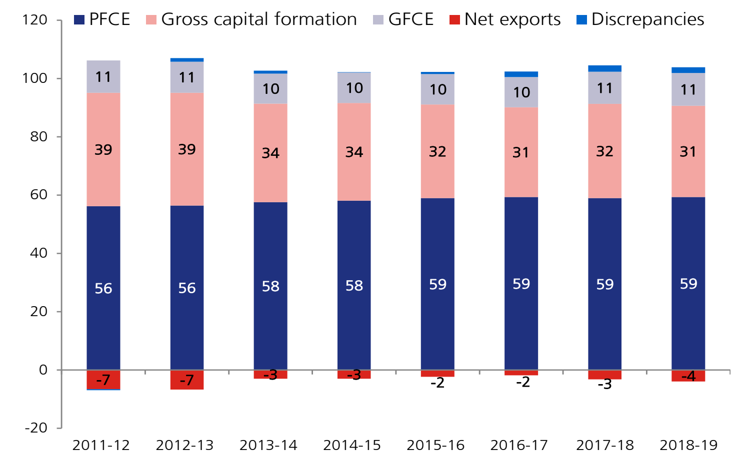
Source: Company, JM Financial

Investments (I)

Falling share of Capital formation in GDP

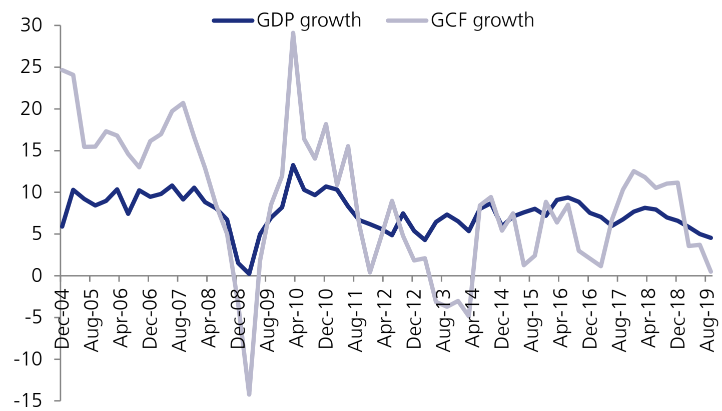
Sustainable growth demands longer-term investments. While India is a consumption-driven economy, the share of gross capital formation (GCF) in GDP has fallen from c.39% in FY12 to c.33% in FY19. There has been a sharp downturn in growth in capital formation too- from 11% YoY in 3QFY19 to 0.5% YoY in 2QFY20- exhibit 41,42

Exhibit 41. Declining share of GCF in GDP



Source: CMIE, JM Financial

Exhibit 42. Gross capital formation growth has fallen sharply since 3QFY19



Source: CMIE, JM Financial

By economic activity, the decline seems to have come mainly on account of moderation in the i) real estate+ sector (falling share from 25% in FY12 to 21% in FY18; 2% 6-year CAGR, done primarily by households), followed by ii) manufacturing (CAGR: 4%), iii) power (share falling from 7% to 6% and CAGR of 2%, and iv) construction (7% share in FY12 reduces to 6% share in FY18; 2% YoY)- exhibit 43

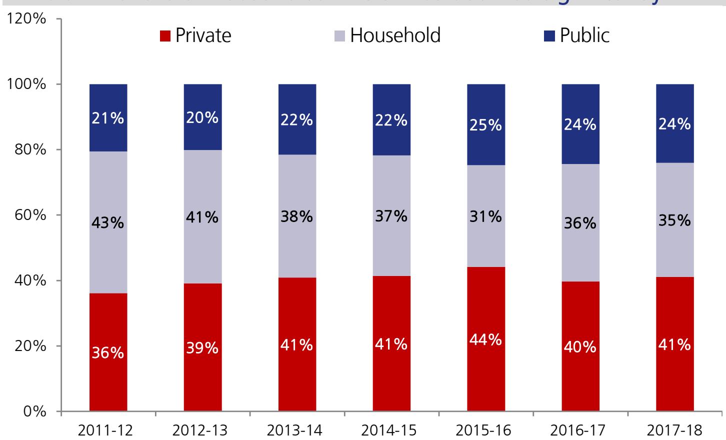
Exhibit 43. The sharpest fall in share in capital formation has been seen in Real estate+, followed by manufacturing, power and construction

	INR bn		%	SHARE (%)						
	FY12	FY18	CAGR	FY12	FY13	FY14	FY15	FY16	FY17	FY18
REAL GROSS CAPITAL FORMATION-by economic activity	32,057	42,870	5%							
Agriculture, forestry and fishing	2,739	2,738	0%	9%	8%	9%	8%	6%	7%	6%
Crops	2,344	2,222	-1%	7%	6%	7%	6%	5%	6%	5%
Others	395	516	5%							
Industry	12,229	14,217	3%	38%	37%	36%	34%	36%	34%	33%
Manufacturing	6,150	7,605	4%	19%	19%	18%	18%	19%	18%	18%
Electricity, gas, water supply and other utility services	3,084	3,428	2%	10%	9%	9%	9%	10%	8%	8%
Construction	2,325	2,572	2%	7%	8%	5%	6%	6%	6%	6%
Others	670.85	611.70	-2%							
Services	17,089	25,915	7%	53%	55%	56%	59%	58%	59%	60%
Real estate, ownership of dwelling and professional services	8,168	9,097	2%	25%	24%	26%	28%	22%	23%	21%
Public administration, defence and other services	3,986	7,393	11%	12%	12%	14%	14%	15%	17%	17%
Trade and repair services	1,599	3,950	16%	5%	10%	6%	9%	8%	9%	9%
Road transport	1,180	1,663	6%	4%	3%	2%	2%	2%	3%	4%
Communication and broadcasting services	544	1,354	16%	2%	2%	6%	2%	4%	3%	3%
Financial services	427	1,037	16%	1%	1%	1%	2%	2%	1%	2%
Others	1,185	1,422	3%							

Source: CMIE, JM Financial

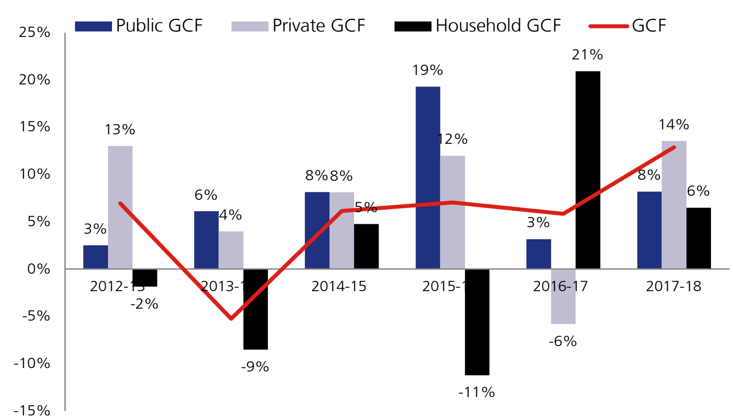
By sector, we observe that share of households in gross capital formation has declined from 43% in FY12 to 35% in FY18, while growing at a CAGR of merely 1%. Private GCF has instead grown at a CAGR of 7% over the same period, helping to smoothen fluctuations in household capex to stablilise overall GCF growth. Given this, we analyse private, public and household capex separately, to assess the capex restoration in India.

Exhibit 44. Share of households in GCF has declined significantly



Source: CMIE, JM Financial

Exhibit 45. Private and Govt. CGF are required to maintain stable GCF growth amid fluctuations in household GCF



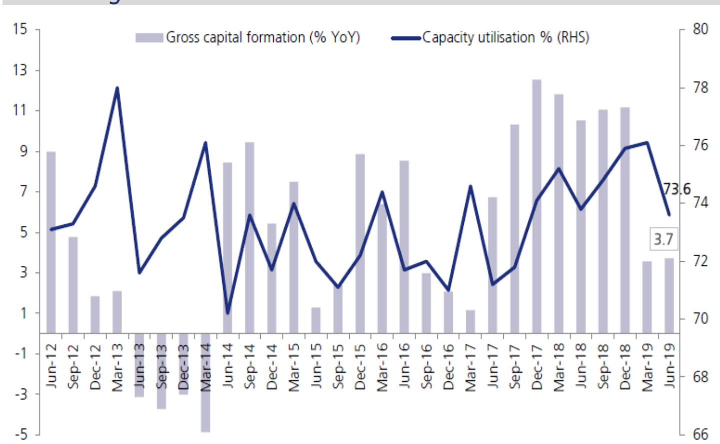
Source: CMIE, JM Financial

A. Private capex

The private sector accounts for ~40%+ of gross capital formation in India with manufacturing contributing roughly 35%, followed by real estate (20%), communication & broadcasting services (7%), power (7%) and trade.

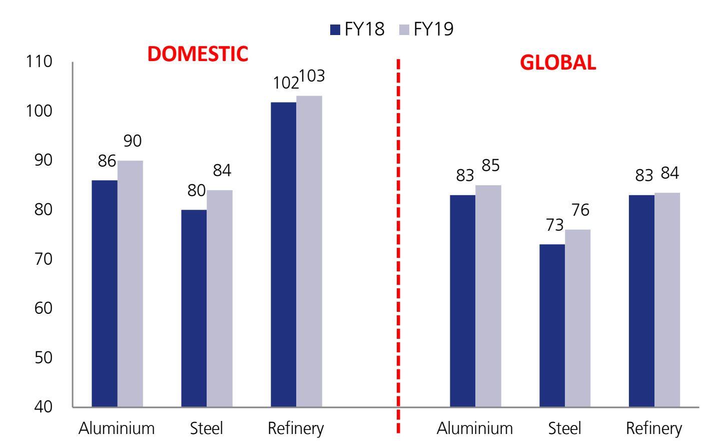
- Current & expected capacity utilisations: RBI's OBICUS (Order Books, Inventories and Capacity Utilisation Survey) reveals CU in 1QFY20 stood at 73.6%, in line with slowing growth in gross capital formation (Exhibit 46).

Exhibit 46. Capacity utilization moderated in 1QFY20 stood at 73.6%, moderating



Source: CMIE, JM Financial

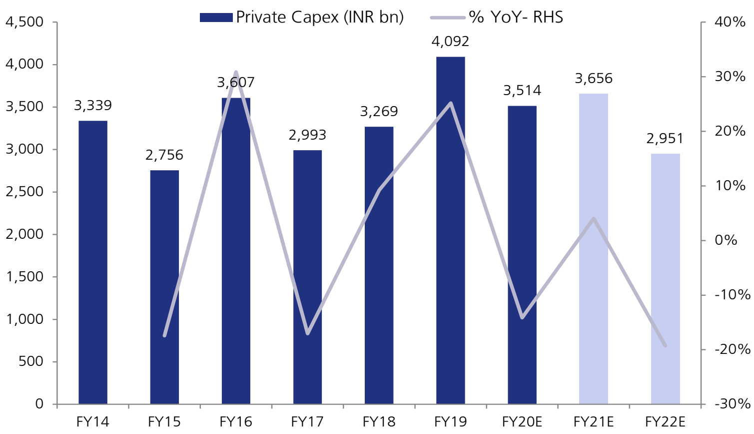
Exhibit 47. Global vs. domestic capacity utilisation in selected industries for FY19



Source: WSA, JPC, BP Global, MoPNG, Blooomberg JM Financial

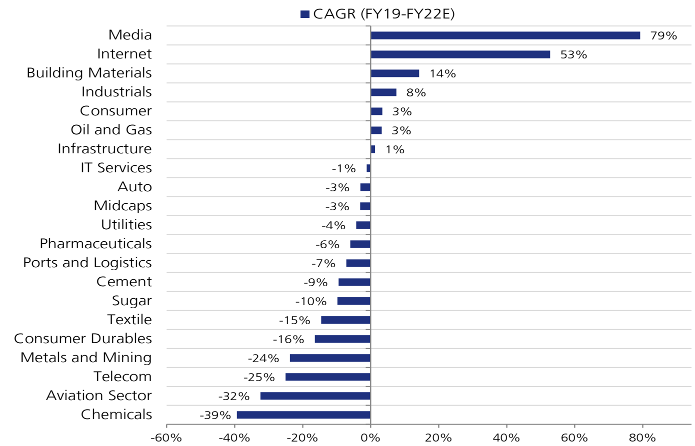
- **Estimates for private capex:** Our internal estimates for private capex shows significant de-growth in capex for a few capital intensive sectors such as i) Utilities (18% share; FY19-22 CAGR -4%), ii) metals & mining (12% share; CAGR -24%), and iii) telecom (16% share; CAGR -25%). Nevertheless, the largest capex sector- Oil & Gas (32% share) is projected to expand capex by 3% over FY19-22. Overall private capex is estimated to record a negative CAGR of 6% during FY19-22(ex-TTMT and ex-Telecom).

Exhibit 48. Private sector capex to register modest growth in FY21



Source: Company, JM Financial; 130 companies under our coverage

Exhibit 49. Sector-wise CAGR during FY19-22E



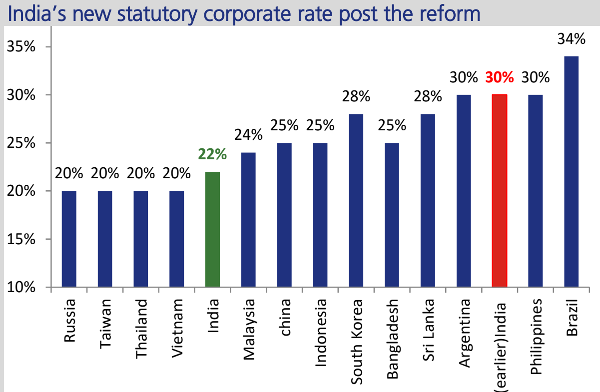
Source: Company, JM Financial; Auto excludes Tata Motors

Box 3- Corporate tax cuts and implications on private capex

The recent corporate tax cut in India questioned various aspects of the stimulus-i) the quantum of dent to the fiscal, ii) impact of the tax cut, and iii) optimal allocation of the resources foregone by the govt. It would not be new to state that the shortfall of the tax cut are overestimated, and that the short-term impact will be negative due to capex cuts with increased fiscal stress for states. In the medium to longer term however, the corporate tax is expected to lead to i) formalisation at a faster pace and ii) higher capital expenditure (domestic & FDIs). Higher corporate savings generated through lower tax rate are expected to benefit- i) private sector banks, ii) oil & gas, iii) consumer staples and iv) retail the most. These are likely to pass-through in the form of i) higher capex and hence job creation (industrials), ii) lower prices (FMCG and autos) and iii) higher dividends (oil & gas).

In the longer term we expect the benefits of corporate tax to materialise in the form of profit shifting into India. Globally, corporate tax rates have fallen and evidence suggests that non-OECD countries lose about 1.3% of GDP due to companies shifting profits to low-tax locations. Consequently, profit-shifting from other economies into India due to lower corporate tax structure, in conjuction with i) changing supply chains owing to trade wars, and ii) possibility of India's deal in RCEP and US-India could be a manifestation of the tax reform. The negative relationship between capex and unemployment rate assures job creation through these avenues.

India's new statutory corporate rate post the reform



Source: IMF. JM Financial

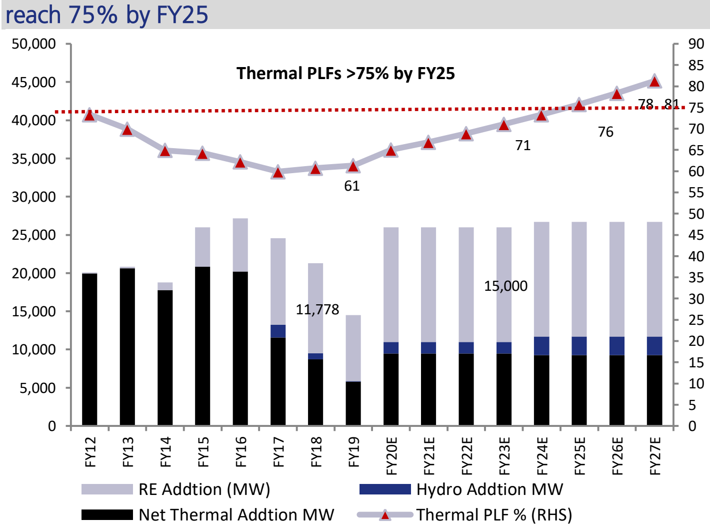
Focus sectors for private capex

i) Power

- **Next cycle of thermal capex depends on renewable energy capex and battery costs:** In the current scenario of a) power demand growing by 5-6% p.a., b) 7.5-15GW / year of estimated solar + wind capex and c) under-utilised thermal capacity (25GW without PPAs) + >38GW of under construction plants (excl. pvt sector capex), we find thermal PLFs reaching 74-75% by FY23-25, implying thermal capex ordering possibly by FY21-22. However, any improvement in battery storage technology in this period (FY20-23) will work against thermal capex. However, given the weak financial capability of banks which are already burdened with >25GW of stranded capacities we find it unlikely for thermal power capex to pick up for next 2-3 years even if RE power additions slowdown. (see our Dec'18 update on India power sector capex)

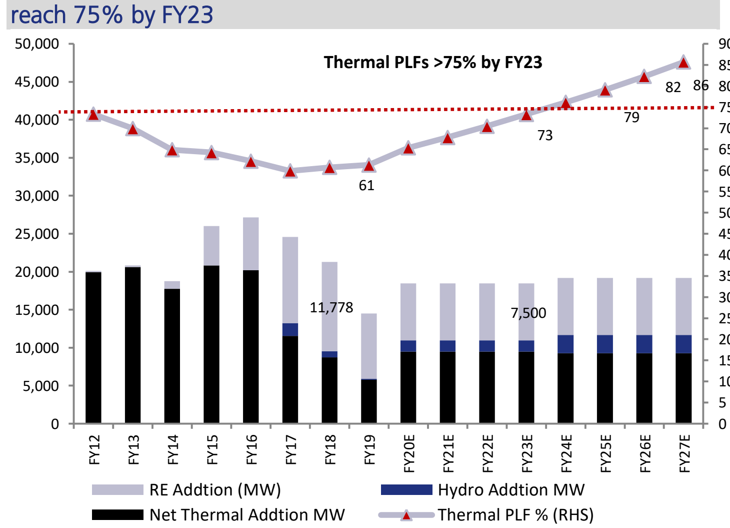
- **Power transmission more focused towards State capex:** As per the National Electricity Plan, incremental transmission capex in India will be more focused towards intra state transmission (in FY17-22). Intra-State transmission capex is estimated at INR 1.6trn in this period – however historically States have always lagged behind targets with a hit rate of only 30-40% of targets. Inter-state capex (by PGCIL) is expected to be stagnant at c. INR 1trn while renewables related green energy corridors adding INR 430bn to the overall basket with most of it being under competitive bidding (TBCB). This is well reflected in PGCIL FY20 capex falling to INR 150bn vs. historic average of INR 200-250bn.

Exhibit 50. 38GW Thermal + 15GW/yr RE addition - Thermal PLFs reach 75% by FY25



Source: JM Financial, CEA,MNRE

Exhibit 51. 38GW Thermal + 7.5GW/yr RE addition - Thermal PLFs reach 75% by FY23

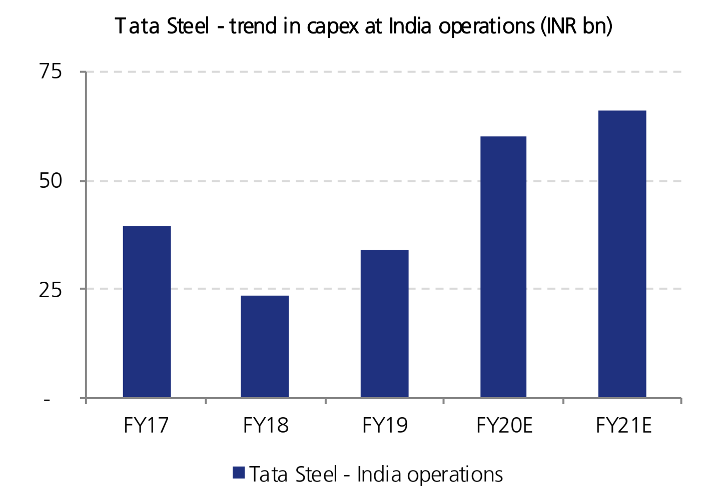


Source: JM Financial, CEA, MNRE

ii) Steel

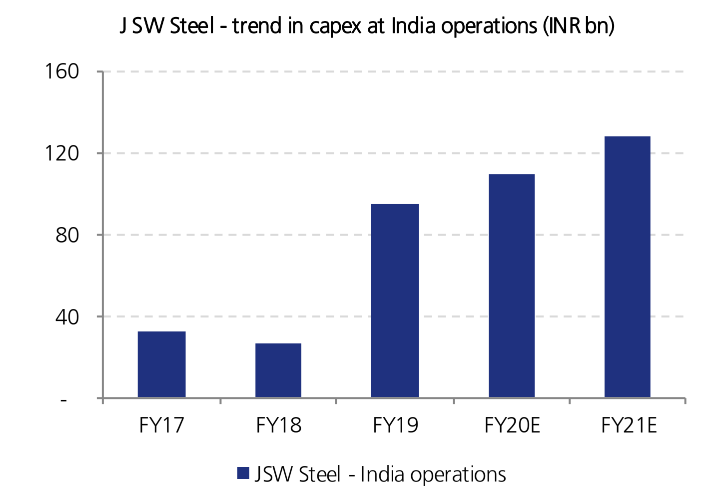
Steel majors postpone part capex due to weak market conditions: Tata Steel and JSW steel have reduced FY20 capex guidance by c.25% driven by weak 1HFY20 performance/market conditions. The companies had earlier announced aggressive organic expansions in FY19. Tata steel had planned capex of INR 235bn over FY19-22 to expand its capacity from 13mtpa to 18mtpa (expansion of 5mtpa capacity at Kalinganagar). JSW Steel had announced capex of INR 44.4bn to a) expand crude steel capacity from 18mtpa to 24.7mtpa, b) modernize/enhance downstream facilities and c) install cost saving initiatives. The capex spend going forward will be a function of revival of steel spreads. Other large ferrous companies such as JSP and SAIL are at the end of their expansion cycle and have lower near term planned capex. Hindalco's deleveraging focus and judicious capital allocation based on return ratios has led to lower capital expenditure over FY20-21E – more focussed towards high return downstream and alumina assets. We could see some revival of capex towards latter part of FY21.

Exhibit 52. Tata Steel capex to expand from 13mtpa to 18mtpa



Source: Company, JM Financial

Exhibit 53. JSW Steel capex to expand from 18mtpa to 24mtpa



Source: Company, JM Financial

Exhibit 54. Total capex incurred/planned for FY17-19/FY20E-21E (INR bn)

	FY17-FY19	FY20E-FY21E	Growth in planned capex vs. last 3 years capex (x)
Tata Steel	97	126	1.3
JSW Steel	155	239	1.5
Jindal Steel & Power	113	27	0.2
SAIL	148	60	0.4
Hindalco	35	36	1.0
Hindustan Zinc	91	43	0.5
NMDC	56	52	0.9
Total	**695**	**582**	**0.8**

Source: Company, JM Financial; Note: Represents capex of only Indian operations (excluding international capex), JSP capex is for steel business

Tata Steel/JSW steel have postponed part capex of FY20 led by weak 1HFY20 performance

Exhibit 55. India steel demand/supply

mn tons	FY15	FY16	FY17	FY18	FY19	FY20E	FY21E
Total crude steel capacity	110	117	123	123	123	124	127
Crude steel production	88	90	97	104	107	112	115
Finished Steel Production	75	75	85	92	96	101	103
Add: Imports	9.3	11.7	7.2	7.5	7.8	6.9	8.5
Less: Exports	6	4	8	10	6	4.1	4.1
Finished steel real consumption	77	82	84	91	98	103	110
Capacity utilization (%)	81	77	79	84	87	90	90

Source: JPC, JM Financial

iii) Refineries

(1) **OMCs:** Indian Oil & Gas sector, specifically the Oil Marketing Companies (OMC's) have completed major capital expenditure towards upgrading the refineries for BS-VI compliance and are in the process of commercially commissioning the upgraded units. This may result in slightly lower capacity utilisation in the near term. Also, OMC's had announced total five-year Capex of c. INR 3.5tr but weaker than expected GRMs coupled with completion of the BS-VI up-gradation have resulted into slight reduction of capex guidance from the previously announced capex.

(2) **Gas companies:** Under our coverage have seen increased volume uptake with Gujarat Gas benefitting from the NGT order to switch to NG. Also, PNGRB has issued authorisations for around 175 circles and we expect capex to gradually build-up. Overall, in the next few years, CGD capex could reflect strong growth.

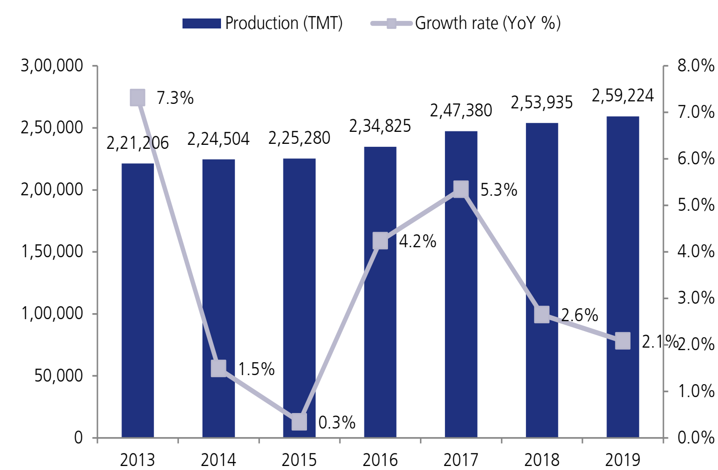
(3) **Exploration companies** like ONGC and Oil have seen a decline in production with focus being on maintaining production in-line with the last year. Also, ONGC post-acquisition of HPCL, had taken debt and is currently deleveraging. ONGC expects to increase production after 2022 with new fields coming in at KG. Indian refiners saw utilisation of 103.14% in FY19 with capacity of 251,385 TMT. Reliance has invested c. INR 4tr in telecom and oil & gas over the last 5 years. However, now RIL has completed majority of the capex and would now significantly scale down. Overall, while CGD capex could increase over the next few years, lower capex by RIL (incl. telecom capex) would result in lower total capex.

Exhibit 56. Estimated Capex of Companies under coverage

INR mn	Capex			
	2019	2020	2021	2022
BPCL	93,072	76,300	95,000	1,00,000
GAIL	75,350	68,510	96,010	77,330
GujGas	4,896	5,055	3,317	3,444
GSPL	1,967	2,066	2,190	2,321
HPCL	1,15,307	1,20,000	1,35,000	1,65,000
IGL	7,440	4,049	4,213	4,384
IOCL	2,38,125	2,44,125	2,50,250	2,50,250
OIL	20,277	22,204	41,669	43,227
ONGC	2,02,360	3,17,244	3,24,630	3,34,088
PLNG	1,746	8,401	11,901	11,328
PSU total	7,60,540	8,69,974	9,66,201	9,93,394
RIL	2,41,000	1,69,971	1,28,740	1,08,053
Total	10,01,540	10,39,945	10,94,941	11,01,447

Source: Company, JM Financial

Exhibit 57. Refinery production



Source: Company, JM Financial

Exhibit 58. Indian Refinery capacity

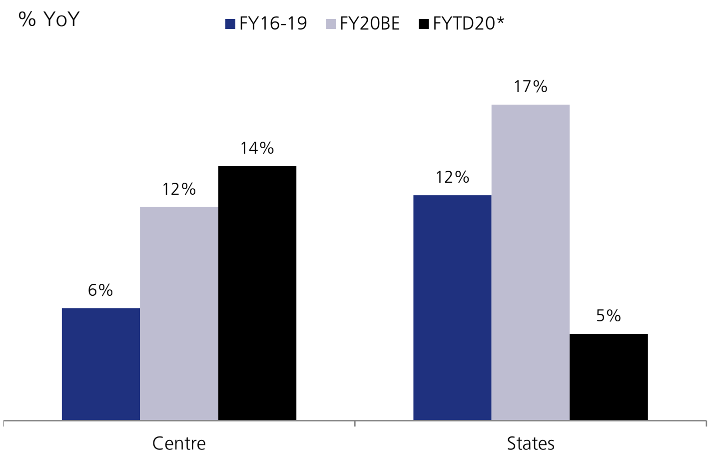
	Capacity (in TMT)				Utilization			
	2012	2015	2018	2019	2012	2015	2018	2019
IOCL	54,200	54,200	69,200	69,200	103%	99%	100%	104%
BPCL	21,500	21,500	27,500	27,500	106%	108%	102%	112%
HPCL	14,800	14,800	15,800	15,800	109%	109%	116%	117%
CPCL	11,500	11,500	11,500	11,500	92%	94%	94%	93%
NRL	3,000	3,000	3,000	3,000	94%	93%	94%	97%
MRPL	15,000	15,000	15,000	15,000	85%	98%	108%	108%
ONGC	66	66	66	66	105%	77%	121%	100%
RIL	60,000	60,000	68,200	68,200	113%	113%	103%	101%
NEL	18,000	20,000	20,000	20,000	75%	103%	104%	94%
BORL	6,000	6,000	6,000	7,800	34%	104%	112%	73%
HMEL	9,000	9,000	11,300	11,300	0%	81%	78%	110%
Total	2,13,066	2,15,066	2,47,566	2,51,385	96%	104%	102%	103%

Source: Industry, JM Financial

B. Government capex

Public sector contributes around c.24-25% to gross capital formation. While both States and Centre engage in capital spending, States capex-to-GDP ratio is almost 2x that of the Centre (3.0% vs. 1.6% for Centre) adjusting for transfers from the Centre. Moreover, the 3-year CAGR in capex for states stands at 17%, almost 3x of the Centre (6%). While the Centre's capex is mainly directed towards defence, railways, roads, urban development and police (accounting for 75-80% of budgeted capex), states focus on transport, irrigation, rural development and water supply, sanitation, housing & urban development. FYTD20, capex has only recently picked for states (since Aug'19; 32% of BE has been spent so far), while 59% of the capex has been spent for the Centre.

Exhibit 59. FYTD20 govt. finally seeing some traction post Jul'19



Source: Union Budget, State Budget, CGA, CAG, JM Financial

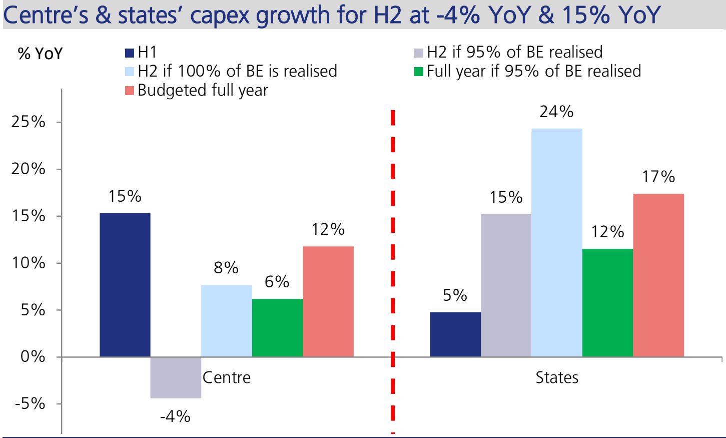
Exhibit 60. Around 59% of budgeted capex has been spent for the Centre (till Oct'19) vs. 32% for states (till H1FY20)

INR bn	FY17	FY18	FY19	FY20BE	FYTD20	% of BE	% YoY
CENTRE	2,846	2,631	3,029	3,386	2,013	59%	14%
Defence	915	954	985	1,082	741	68%	21%
Roads	412	508	686	721	453	63%	2%
Railways	452	434	531	658	376	57%	22%
Housing+	165	153	170	195	96	49%	16%
STATES*	3,386	3,534	4,070	4,777	1,515	32%	5%
Transport	802	754	972	730			
Irrigation	788	778	1004	932			
Rural dev.	145	178	268	336			
Water sanitation	181	216	249	338			

Source: Govt. budgets, CGA, CAG, JM Financial; For Centre till Oct'19; For states till Sep'19

Even as the general govt. fiscal is tight, the Centre is expected to meet the fiscal deficit target of 3.3% though off-budgeting techniques, RBI dividend, and PM KISAN savings- refer to Fiscal section in the report. States could however, fall short of the budgeted capex as their revenues are under pressures not only due to stagnant own tax revenues, but also de-growth in tax devolution from the Centre. Consequently, capex cuts are likely to materialise as has been seen historically in case of revenue shortfall. Assuming only 95% of the budgeted capex is realised, overall capex growth for states would settle at 12%YoY vs. 17% if entire budgeted capex was realised. This would still imply a 15% YoY growth in H2 by states. However, **we estimate that any realisation below 86% of budgeted capex would yield a negative capex growth for H2 for states**. The corresponding case for the Centre reveals that 95% capex realisation for FY20 would imply YoY contraction in capex for H2 for the Centre- refer to exhibit 61

Exhibit 61. If only 95% of budgeted capex is realised in FY20, Centre's & states' capex growth for H2 at -4% YoY & 15% YoY



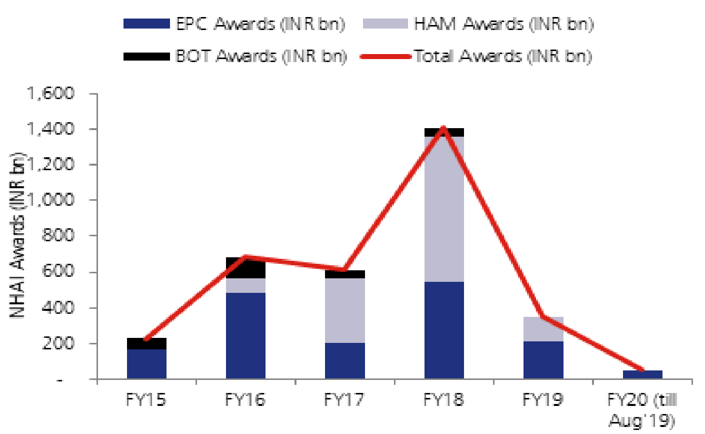
Source: CGA, CAG, JM Financial

Exhibit 62. Some capex projects in operation

Roads sector- Bharatamala	After the announcement of Bharatmala, ordering from the NHAI jumped 100% YoY in FY18, at c.INR 1.4trn for 7,394km (+70% YoY), with most awards in 4QFY18. However both ordering & execution have slowed down in FY19 – YTD FY20, on delays in land acquisition and financial closure for higher mix of hybrid annuity model (HAM) projects. We estimate c. INR 600-700bn of outstanding NHAI tenders which may be awarded in 4QFY20 – FY21 resulting in a pick-up. However as NHAI acquires land, developers achieve financial closure and start execution; we expect a pickup in execution from FY21
Metros	In Aug'17, the Union cabinet approved a **new metro rail policy** which increases private participation in metro development. The policy mandates PPP component mandatory for states to avail central assistance. It also mandates last mile connectivity to metro stations, Transit Oriented Development (TOD) to promote dense urban development along metro corridors. State govt/UTs can prepare Detailed Project Report (DPR) in line with the Metro rail policy and can submit for approval and funds. The govt. has provided budgetary support worth **c.INR 542bn** over FY16-FY19RE towards metro rail projects. C.657km of metro rail is operational with another 791km of metro rail under development across 27 cities, as reported by the ministry

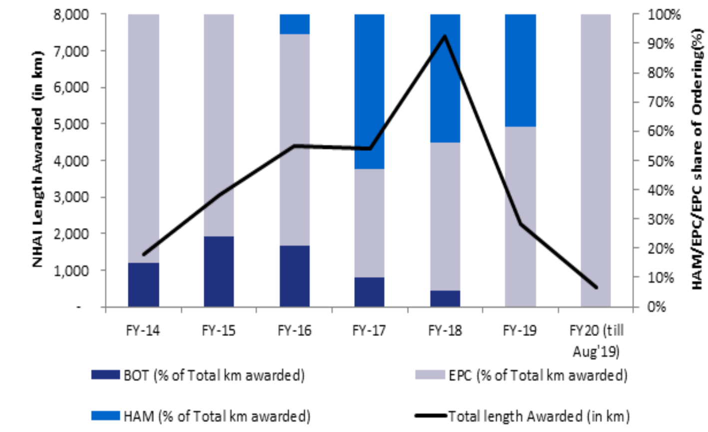
Source: Union budget, JM Financial

Exhibit 63. NHAI awards FYTD20 have been slow



Source: Industry, JM Financial

Exhibit 64. NHAI Ordering mix



Source: Industry, JM Financial

Box 4: The INR 100trn infrastructure target of the govt.

The govt. has announced a target of INR 100trn as part of its manifesto. Since then while there has been some progress in terms of setting up a task force to identify projects, there has much debate about financing the INR 100trn target. We recently invited Mr. Vinayak Chatterjee, Chairman and co-founder of Feedback Infrastructure to our India Conference held on 7-8Nov'19. According to him, both the USD 5trn economy and INR 100trn infra target go hand in hand. While nominal GDP needs to grow at c. 13% CAGR, he estimates that gross capital formation in infrastructure (GCFI) should increase from current levels to at least 8.5% of GDP by FY25 which is possible as most countries have reached c.14% levels at their peak. India can gradually progress and reach c.INR 100trn of the infra spend by FY25 as shown in the Exhibit below.

Gradual achivement of the INR 100 trn target (INR trn)	
2020-21	13
2021-22	15
2022-23	20
2023-24	23
2024-25	30
TOTAL	101

Considering the funding for FY23, that comes out to be around c. INR 20trn, INR 10trn/yr can be funded through a mix of i) central (c. INR 4.4trn in FY20) and state budgets, ii) borrowings from bilateral / multi-lateral agencies, and iii) borrowings at urban local bodies. However, the balance 10 trn/yr is likely to pose a challenge which may need DFI's and PPP mode projects.

Annual Target	Break-up	Sources	
INR 20 trn	10	?	8 DFI*
			2 PPP*
	4	Other Public Funds	
		[States + ULBs* + Bilateral / Multilateral + PSUs]	
	6	Budget	
	INR 20trn		

Structuring and funding the DFI: Given that corporate India is keen to limit itself to developemnt and construction risks (EPC) and with FII's keen on taking operational risks (brownfiled investment) only, the appetitie for PPP mode projects is limited currently. In this context, a DFI is needed to fund the projects through supply of low-cost funds for Long-term investment. The DFI could be funded by a) relaxing the fiscal deficit by 0.5% which can yeild c. INR 1trn and b) asset monetisation (c. INR 0.9trn target for FY20) which can form c. INR 2trn of equity fund base for the DFI which can be leverage further to create a c. INR 20 trn balance sheet for Infra funding.

Reviving PPP: Citing the Kelkar committee report on "Revisiting and Revitalising PPP model of Infrastructure development", Mr. Chhatterjee highlights the need for a) Independent sector regulators in road and rail, b) National facilitation commiitteee for resolution of conflicts as 63% of PPP projects come-up for renegotiation in first 5 years, c) Bespoke concession structuring for optimal risk-allocation and d) Making renegotiation an intrinsic part of long concession agreements among others while borrowing funds through Municipal bonds (Munis) for funding Urban Infra may be explored

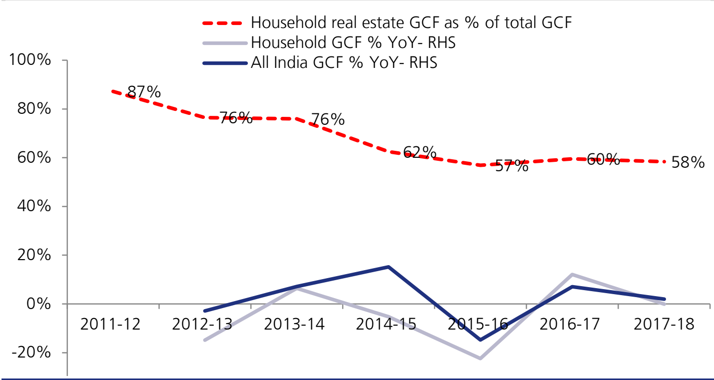
C. Household capex

Household's contribution to capital formation is around 30%. Of this, 36% accounts for real estate investment, followed by trade & repair services (17%) and crops (14%). In fact, around 60% of the capex in real estate happens through household, followed by private (40%). Household share in real estate capex has however fallen from 85%+ in FY12 to 58% in FY18- exhibit 65. Given this, we focus on the housing sector.

Special focus: Real estate - Commercial and resident showing divergent trends

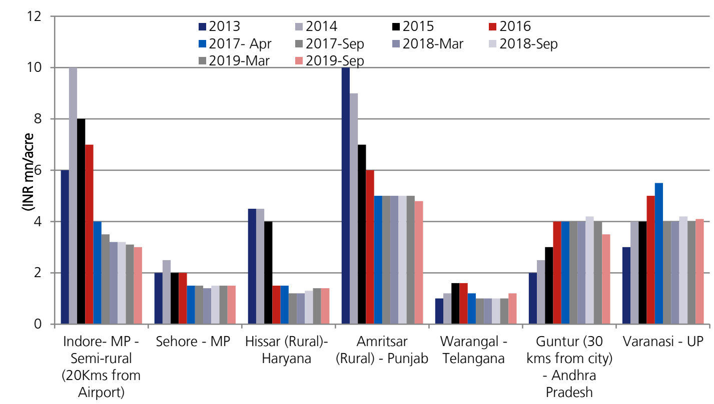
As highlighted earlier, the share of gross capital formation (GCF) in GDP has fallen from c.40% in FY13 to c.35% in FY18 mainly due to real estate+ sector which saw falling share from 25% in FY12 to 21% in FY18; 2% 6-year CAGR. Since the household sector is the top contributor to real estate capex (60%), followed by the private sector, the drag on overall capital formation can be revived by recovery in housing demand. Inventory by value peaked across the top 6 cities middle of last year but has stayed elevated (exhibit 31 above). As per our estimate, as launches slowdown, and there is a natural attrition and cuts to inventory, certain cities can begin to see revival in new launches.

Exhibit 65. Household real estate GCF key driver for overall moderating share of real estate in capital formation



Source: CMIE, JM Financial

Exhibit 66. Real estate prices have yet to record an uptick



Source: JM Financial

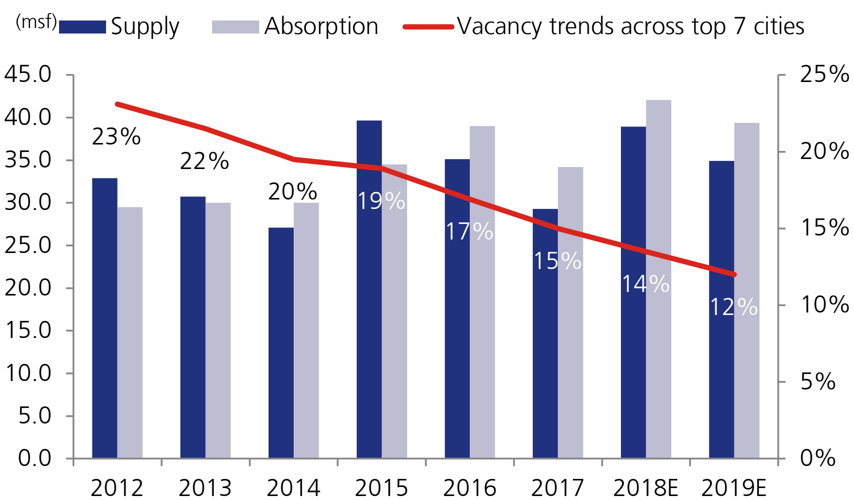
The Indian real estate markets have been showing divergent trends with commercial office spaces hitting new high in terms of absorptions (33mn sq ft in 9MCY19 compared to 28.7/33.2 in CY17 and CY18) along with very low vacancy levels (13.2%; 13.7% in 9MCY18). Residential on the other hand has been struggling with high inventory levels (33 months across top 7 cities; peak of 44 months in 3QFY17) and low absorption rates. Measures like demonetisation and GST have resulted in low demand coupled with the overhang of the already high inventory. The supply side has been further impacted with the ongoing liquidity crisis. Currently, the government is taking proactive measures (decreasing interest rates, creation of special situation fund, tax breaks for affordable housing schemes) to spur demand and also revive stalled projects. While we notice an improvement over past year but these are not yet helping clear the inventory implying further demand boost is required in the form of even lower prices or tax incentives. Recent government measures aimed at ensuring completion of projects and buyout of stressed portfolios are, meanwhile, steps aimed at gradually easing supply side pressures and ease stress on financial creditors. We believe that at some point in the cycle, a demand boost is a necessity. Affordable housing remains a ray of hope with the segment benefitting from continuous government support. Under PMAY-U, 2.86mn houses have been built (9.65mn sanctioned).

- Commercial office space hitting new highs; will drive capex: The demand for commercial real estate has been hitting new high in terms of absorptions (33mn sq ft in 9MCY19 compared to 28/33 in CY17 and CY18) along with very low vacancy levels (c.12%; 23% in FY12). This growth has been primarily led by IT/ ITeS (48% of overall leasing) and BFSI (11%) occupiers. The IT/ITeS markets of Hyderabad, Bangalore and Pune continue to lead leasing activity with high pre-lease commitments and rental escalations. We expect this trend to continue as lot of developers are focussing on building IT parks and commercial office spaces. The emergence of REITs as an alternative funding platform has further driven the capex cycle towards commercial real estate.

- Affordable housing - Government's effort to revive housing investment: PMAY (U): The Union Budget 2019-20 allocated INR 10bn (INR 19bn for FY18-19) for the CLSS scheme under PMAY(Urban) with INR 6bn earmarked under CLSS – I for economically weaker section (EWS) and lower income group (LIG) and INR 4bn under CLSS – II for middle income group (MIG).

  Progress under PMAY-U: The data shows that till Nov'19, 9.65mn houses were sanctioned under PMAY-U, of which 2.86mn have been built, i.e. c.29% of the number of sanctioned houses. This is against a completion percentage of 18% in Nov'18. Work for more than 5.6mn units is underway. The total investment done in projects under this scheme is around 5.7trn. INR 579bn have been released in the central assistance. Data shows that the scheme is in progress but it still has a long way to go. The rate at which houses have been built so far may not be enough to meet the housing needs of the country by 2022 but continues to maintain momentum in an otherwise sluggish real estate market

Exhibit 67. Increase in absorption coupled with drop in vacancy augur for well for office space capex to continue



Source: Embassy REIT DRHP, CBRE, JM Financial

Rural Housing – Step up in execution?

Rural Housing under Pradham Mantri Awas Yojana (PMAY –G) has a target to construct 29.5mn pucca houses for rural households over FY17-22. The first phase of the program (FY17-19) aimed to construct 10mn houses over FY18 & FY19. In terms of progress, against the target of 10mn houses in phase-1, at Apr'19, the completion was 77% and improved to 86% by Nov'19. Among states, Bihar, Tamil Nadu lagged in completion percentages as compared to national average.

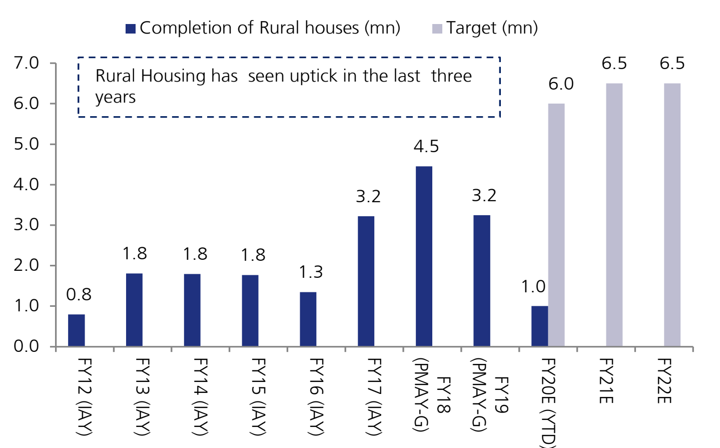
Exhibit 68. First phase of PMAYG (FY17-19): 86% completion, few states such as Bihar, Tamil Nadu dragged overall completion down

	Number of rural pucca houses (mn)						Progress of Pucca Rural houses as % of Target			
State	MoRD Target	Sanctions	1st	2nd	3rd	Completed	1st instalment	2nd instalment	3rd	Completed
Madhya Pradesh	1.4	1.4	1.4	1.4	1.4	1.3	99.8%	98%	97%	95%
West Bengal	1.4	1.4	1.4	1.4	1.4	1.3	99.5%	98%	97%	96%
Uttar Pradesh	1.3	1.3	1.3	1.3	1.3	1.3	99.8%	99%	98%	98%
Bihar	1.2	1.1	1.1	0.9	0.7	0.7	93%	75%	60%	61%
Odisha	1	1	1	0.9	0.9	0.9	99.9%	96%	91%	87%
Chhattisgarh	0.8	0.8	0.8	0.8	0.7	0.7	99.9%	97%	93%	92%
Rajasthan	0.7	0.7	0.7	0.7	0.7	0.7	99.7%	98%	95%	95%
Jharkhand	0.5	0.5	0.5	0.5	0.5	0.5	99.8%	97%	92%	90%
Maharashtra	0.4	0.4	0.4	0.4	0.4	0.4	94%	87%	83%	80%
Tamil Nadu	0.3	0.3	0.3	0.2	0.2	0.2	95%	75%	65%	61%
Assam	0.3	0.2	0.2	0.2	0.2	0.2	89%	86%	78%	75%
Gujarat	0.2	0.2	0.2	0.2	0.2	0.2	99%	93%	82%	91%
Karnataka	0.1	-	0.1	0.1	0.1	0.1	72%	64%	58%	55%
Andhra Pradesh	0.1	-	0.1	0	0	0	52%	39%	37%	38%
Others	0	0	0	0	0	0	74%	66%	59%	57%
All India	10	9.5	9.7	9.1	8.7	8.5	96.60%	91.50%	86.70%	85.50%

Source: iay, JM Financial, Note: Status as of 27Nov'19

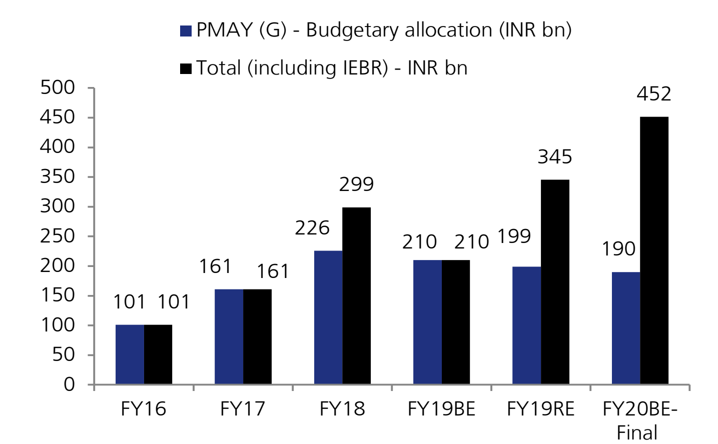
The target for phase-II of the PMAY (G) is much more ambitious with aim of construction of 19.5mn houses over FY20-22, and would need a run-rate of 6.5mn house completion per year, a significant acceleration from the 3.0-4.5mn run rate pace recorded over the past three years. In terms of spending, the budgetary allocation has been at INR190bn in FY20BE, but including IEBR, allocation for FY20BE is INR452bn, up by 31% YoY and almost double of FY16-18 spending run-rate.

Exhibit 69. Rural Housing – Completion and target of pucca rural houses over the years



Source: iay, JM Financial, Note: Status as of 27Nov'19

Exhibit 70. Allocation for Rural Housing – Step up in budgetary allocation for rural housing (including IEBR)



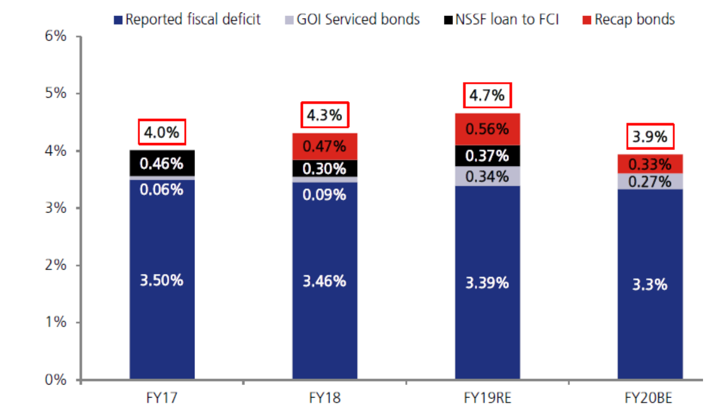
Source: Union budget, JM Financial

Government (G) - Slippage likely due to states

Exhibit 71. Centre + states GFD-to GDP target ratio at 5.9% for FY20

Source: CMIE, JM Financial; FY16, FY17 GFD for states includes UDAY costs

Exhibit 72. Alhtough, true fiscal deficit for the Centre is more than 3.9%



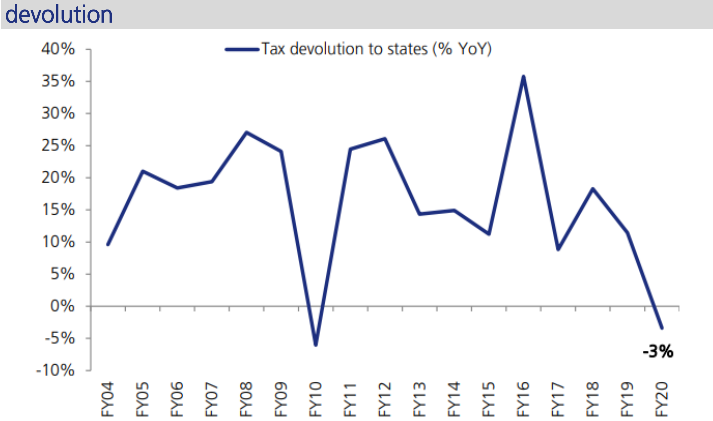
Source: CMIE, JM Financial

Exhibit 73. The Centre is estimated to meet the GFD-to GDP target of 3.3% through off-budget accounting of the food subsidy

INR bn	FY18	% YoY	FY19A (P)	% YoY	FY19RE	% YoY	FY20BE	% YoY	FY20e	% YoY	Shortfall
Gross Tax Revenue	19,190	12%	20,803	8%	22,482	17%	24,612	18%	21,876	5%	(2,736)
Taxes on Income	4,308	18%	4,617	7%	5,290	23%	5,690	23%	5,238	13%	(452)
Corporation Tax	5,712	18%	6,636	16%	6,710	17%	7,660	15%	6,660	0%	(1,000)
Customs	1,290	-43%	1,179	-9%	1,300	1%	1,559	32%	1,176	0%	(383)
Union Excise Duties	2,594	-32%	2,310	-11%	2,596	0%	3,000	30%	2,400	4%	(600)
Service Tax	812	-68%	69	-92%	93	-89%	-		-		-
GST	4,426		5,840	32%	6,439	45%	6,633	14%	6,333	8%	(300)
States and UTs' share	(6,730)	11%	(7,615)	13%	(7,615)	13%	(8,091)	6%	(7,214)	-5%	(877)
Central govt. net tax revenue	12,425	13%	13,170	6%	14,844	19%	16,496	25%	14,662	11%	(1,834)
Non-tax revenue	1,927	-29%	2,462	28%	2,453	27%	3,132	27%	3,658	49%	
Of which Surplus from RBI/National	1,049		na	na	1,313		1,772	na	2,298	na	526
Of which Telecom receipts	321	-54%	na	na	392	22%	505	na	505	na	
Central govt. revenue receipts	14,352	4%	15,632	9%	17,297	21%	19,628	26%	18,320	17%	
Non-debt Capital Receipts	1,157	77%	1,029	-11%	932	-19%	1,198	16%	1,198	16%	
Of which divestments	1,000	110%	850.5	-15%	850	-15%	1,050	23%	1,050	23%	
Total Receipts	15,509	8%	16,661	7%	18,228	18%	20,826	25%	19,518	17%	
Food subsidy	1,003	-9%	1,019	2%	1,713	71%	1,842	81%	800	-21%	1,042
Rural Spending	1,866	14%	1,970	6%	2,217	19%	2,913	48%	2,563	30%	
Of which PM KISAN					200		750	na	400	na	350
Total Expenditure	21,420	8.4%	23,113	8%	24,572	15%	27,863	21%	26,471	15%	
Revenue expenditure	18,788	11%	*20,085*	7%	21,406	14%	24,478	22%	23,086	15%	
Capital Expenditure	2,631	-8%	*3,029*	15%	3,166	20%	3,386	12%	3,386	12%	
Fiscal Deficit	5,911		6,453		6,344		7,038		6,953	8%	
Fiscal Deficit/GDP	3.46%		3.39%		3.37%		3.34%		3.36%		

Source: Union Budget, CMIE, CGA, JM Financial

Exhibit 74. But states' under pressure due to contracting tax devolution



Source: CMIE, JM Financial; *up to Oct''20

Exhibit 75. Hence, expenditure cuts are likely by states

	% YoY		% of BE	
	FYTD19	FYTD20	FYTD19	FYTD20
Revenue receipts*	16%	5%	41%	39%
Tax revenues	14%	2%	43%	40%
Grants from Centre	27%	21%	36%	40%
Non tax revenues	26%	-3%	34%	31%
Non-debt capital receipts	283%	56%	15%	30%
Total receipts	17%	5%	40%	39%
Revenue expenditure	11%	9%	41%	40%
Capital expenditure	24%	5%	31%	31%
Capital outlay	22%	3%	30%	30%
Loans and advances	49%	19%	44%	40%
Total expenditure	13%	9%	39%	39%
Fiscal deficit			32%	38%

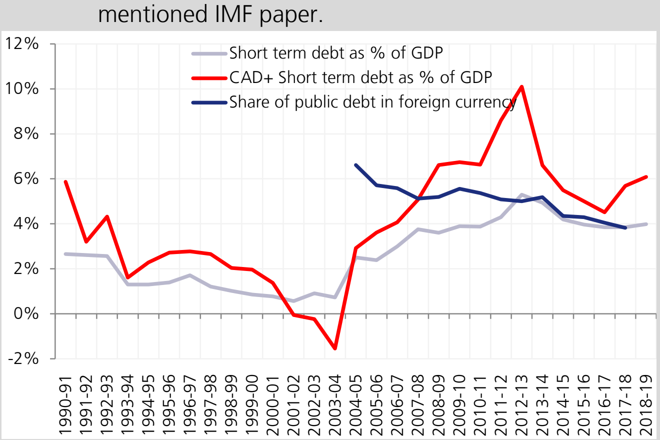
Source: CMIE, JM Financial; Up to H1FY20

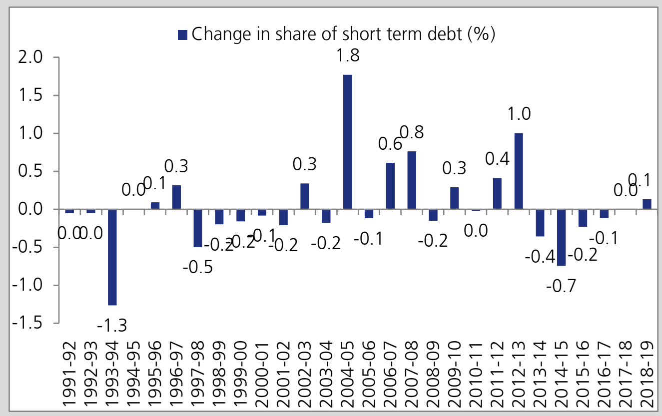
Box 5: Does India have fiscal space?

The IMF defines fiscal space on the basis of two key factors: i) Financial availability, and ii) sustainability.

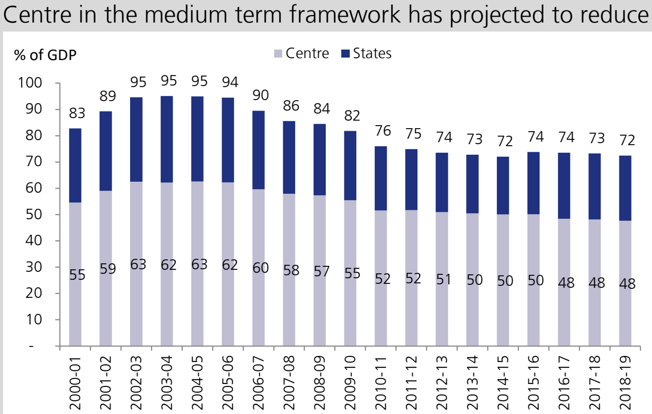
A. **Financial availability:** This is the extent to which the government can expect to have access to market funding at reasonable rates. Using indicators that the IMF uses in its report- Assessing Fiscal Space (2018) we note the following for India:

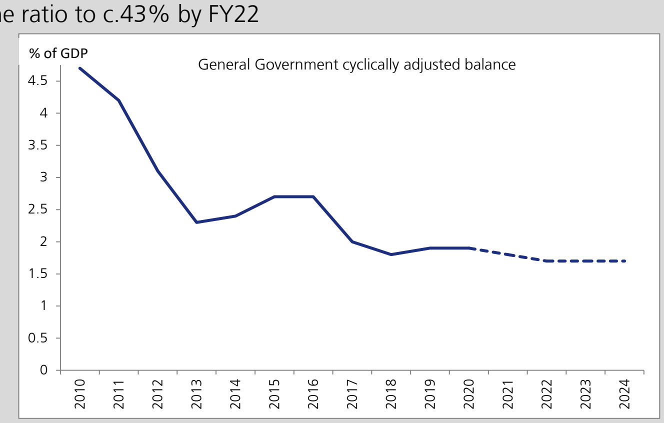
1. **Peak sovereign bond spreads** (calculated as per MAC DSA guidelines and using the stated thresholds) with respect to the year 2018. We note that India enters stands in the **high risk zone**. Even if we use i) latest data on yields, and ii) similar thresholds, India has peak spreads equivalent to i) 516bps, and ii) 616bps respectively. This places it in the medium risk zone.
2. **Debt profile indicators**
   - **Share of public debt in foreign currency:** Stands at c.4%; further, the s**hare of public debt held by non-residents** stood close to 5.4% of the total general govt. debt in 2018. Both these factors imply that India's debt profile has low risk vs. other EMs.
   - **Change in share of short term debt (%):** Short-term debt for India has been moderating since 2012-13. But has seen a moderate uptick in 2018-19 to 4%. Yet the change in this share has rarely exceeded 1ppt on a sequential annual basis unlike certain other EMs
   - **External financing requirements (% GDP)-** This is defined as current account deficit plus short-term total external debt. For India this number stands at 6.1%, an uptick being seen since FY17 onwards. However, this is lower than most EMs in the mentioned IMF paper.





B. **Sustainability**: Refers to the extent to which public debt and annual financing needs (composed of the budget deficit and repayment of debt coming due) of the government remain sustainable. We note that India's total govt. liabilities ratio has been non-increasing even as states have been seeing an increase in liabilities, keeping overall debt levels more or less constant. In the Union budget, the Centre in the medium term framework has projected to reduce the ratio to c.43% by FY22





The realism of assumed medium-term fiscal adjustment plans is captured by the cyclically-adjusted primary fiscal balance. We note that for India, the change in cyclically adjusted primary fiscal balance is actually negligible given the projected path of the CAPB by the IMF Fiscal monitor 2019. Further, for the longer term, the IMF paper also analyses the scale of longer term pressures on public finances using the relative size of the adjustment of the cyclically-adjusted primary balance after accounting for demographic trends and costs associated with population aging. In the context of India, the following put India in a comfortable position in the long run as well- i) Outlay on old people with rise in aging people, i.e. pensions as % of GDP is estimated flat during 2015-2030 (0.0ppt change) and ii) expenditure on health as % of GDP is likely to rise by merely +0.4% change during 2015-2030 (As per the IMF Fiscal monitor)

We conclude that based on the i) thresholds from the paper, and ii) data for the period 2017-18, India seems to have limited fiscal space. This is because the **financial availability** factors are limited given that it stood in high risk zone for peak sovereign spreads, even as debt indicators and sustainability seems reasonable. The **medium and longer term factors** too do not seem to place pressure on the public finances. However, since the above anaylsis does not take into account the **off-budget liabilities** of the govt, it is possible that even in the medium and long term public finances are in discomfort.

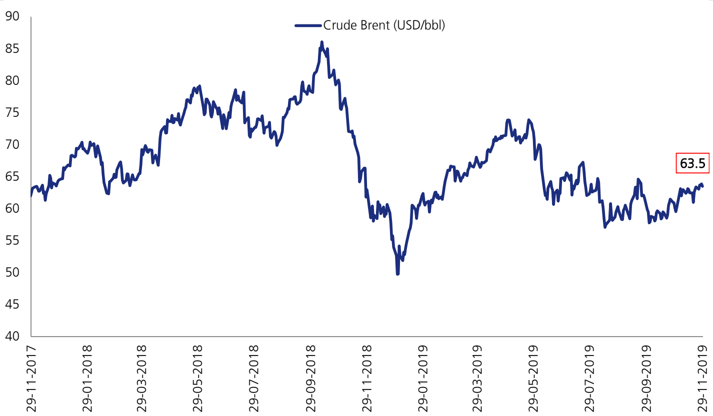
External Sector (NX)

Assessment of the external front of the Indian economy hinges on three key factors- i) oil prices, and ii) global monetary easing, and iii) global growth

i) Oil prices to remain subdued

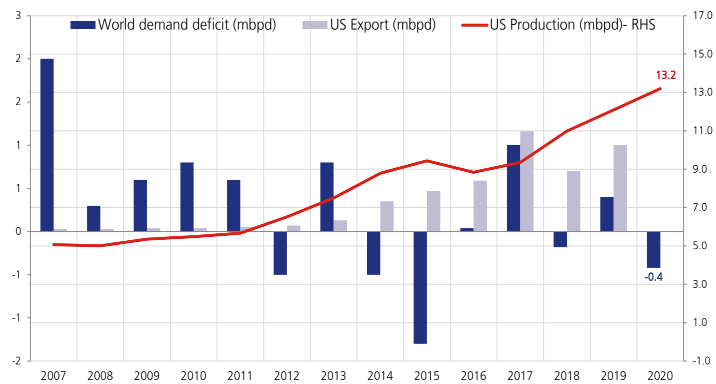
Oil prices for now are expected to remain low especially after the International Energy Agency (IEA) revised its oil demand growth forecast in Sep'19 for this year down to 1.1mbd vs. 1.4mbd in Feb'19. For 2020, the OPEC estimates a global oil demand surplus- exhibit 77

Exhibit 76. Oil prices have remained range bound in 2H2019



Source: Bloomberg, JM Financial

Exhibit 77. The OPEC expects an oversupply in the world oil market in 2020



Source: OPEC, JM Financial

ii) Global growth outlook more favourable in 2020

In Apr'19, the IMF projected global growth to rise to 3.3%YoY in 2019. However, by Oct'19, the growth forecast was revised down by 0.3ppts to 3.0% YoY, the slowest since the global financial crisis on account of i) slowdown in global activity (primarily manufacturing and global trade) particularly in emerging markets and euro area, even though ii) the fiscal stimulus in China and US helped counter the negative impact of tariffs. In 2020, global growth is expected to grow by 3.4%YoY on account of i) durable normalization in emerging market and developing economies (EMDE) and ii) continued healthy performance of relatively faster-growing EMDE- exhibit 78

Risks to growth: Uncertainty looms from trade barriers and heightened geopolitical tensions, including Brexit-related risks which are estimated to further disrupt supply chains and hamper confidence, investment, and growth. Such tensions, as well as other domestic policy uncertainties, have been estimated to negatively affect the projected growth pickup in EMEs and the euro area. Other risks involve the financial conditions for EMDEs as they adjust to i) progressive interest rate hikes by the Federal Reserve, and ii) impending end of asset purchases by the European Central Bank..

Exhibit 78. Global growth is expected to pick in 2020 on account

						Change of 2019 wrt			
Country	2017	2018	2019	2020	2024	2018	2019	2020	2024
World GDP growth	3.8	3.6	3.0	3.4	3.6	-0.2	-0.6	0.4	0.2
Brazil	1.1	1.1	0.9	2.0	2.4	0.1	-0.2	1.2	0.3
China	6.8	6.6	6.1	5.8	5.9	-0.2	-0.4	-0.3	0.1
India	7.2	6.8	6.1	7.0	7.4	-0.4	-0.7	0.9	0.4
United States	2.4	2.9	2.4	2.1	1.7	0.6	-0.6	-0.3	-0.3
Euro Area	2.5	1.9	1.2	1.4	1.3	-0.6	-0.7	0.2	-0.1

Source: IMF, JM Financial; w.r.t. implies with respect to

iii) Accommodative monetary policy by global central banks

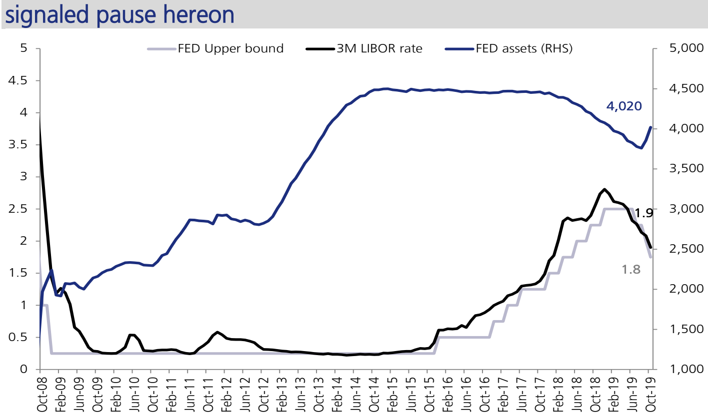
According to the IMF, in the absence of the current monetary stimulus globally, global growth would be lower by 0.5ppts in both 2019 and 2020. This stimulus has therefore helped offset the negative impact of US–China trade tensions, which is estimated to cumulatively reduce the level of global GDP in 2020 by 0.8%.

- FED cut interest rate after over a decade: The US central bank cut its key interest rate by 25 bps first time post financial crisis in July'19 signalling its readiness to provide more support as US growth slowed down. This was followed by two more 25bps cut to ensure US economy does not slip into a recession. However, it has signalled a pause in the rate cut cycle in the Oct'19 policy statement. Fed sees the current stance of monetary policy as likely to remain appropriate as long as incoming information about the economy remains broadly consistent with the outlook of moderate economic growth, a strong labour market, and inflation near the 2% objective.

- The European Central Bank too cut the interest rate on bank reserves, money banks deposit with it, for the first time since 2016, by 10bps to -0.5%. In the last governing council meeting ECB decided to maintain the interest rates until the inflation outlook would converge to a level close to, but below, 2% within its projection horizon. Net purchases by the bank under the asset purchase programme (APP) has restarted starting 1Nov'19 at a monthly pace of €20bn to reinforce the accommodative impact of its policy rates. This will end shortly before it starts raising the key ECB interest rates.

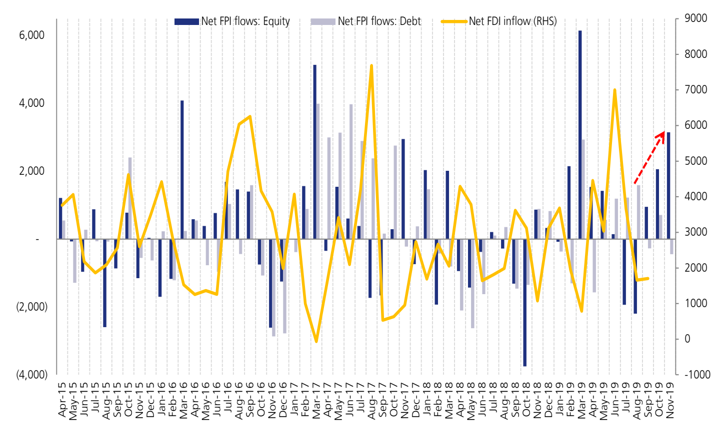
- The Bank of Japan: In its Oct'19 monetary policy, the bank maintained short and long term interest rates at their present level as long as it is necessary. They are paying close attention to the possibility that the momentum toward achieving the price stability target will be lost. The Bank will purchase Japanese government bonds (JGBs) so that 10-year JGB yields will remain at around 0%. With regard to the amount of JGBs to be purchased, the Bank will conduct purchases in a flexible manner so that their amount outstanding will increase at an annual pace of about 80 trillion yen.

Exhibit 79. The FED has already cut rates by 75bps this year, with a signaled pause hereon



Source: Federal reserve, Bloomberg, JM Financial

Exhibit 80. Flows have picked significantly post Sep'19

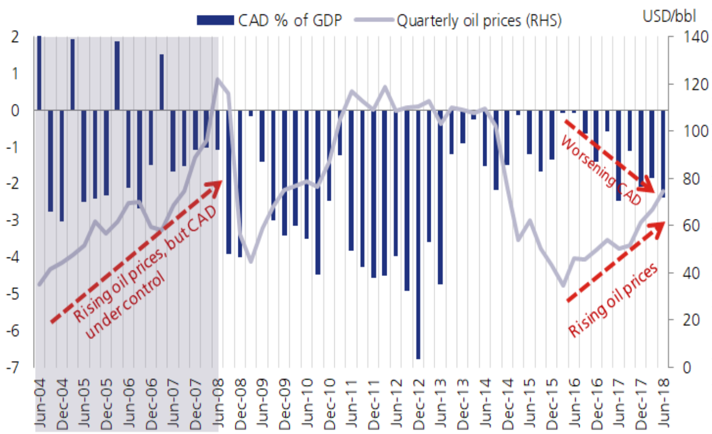


Source: CMIE, Bloomberg, JM Financial

Implications on CAD- Likely to be contained due to low oil prices

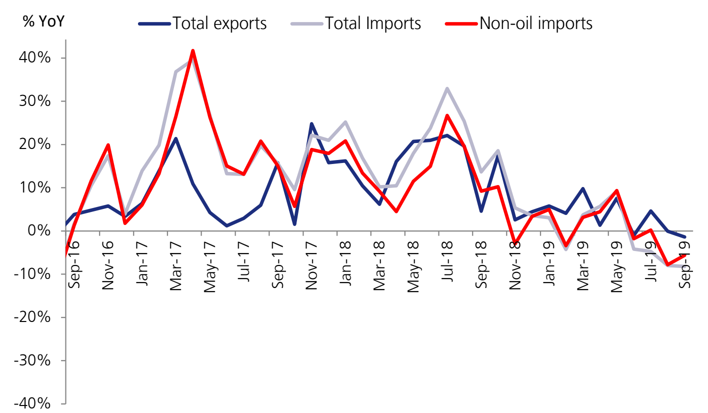
The current account deficit for 1QFY20 stood at USD 14.3bn (2.04% of GDP), vs. i) USD 4.6bn in 4QFY19 (0.7% of GDP), and ii) USD 15.8bn (2.3% of GDP) in 1QFY19. With slowdown in the global economy and moderation in oil prices, both exports and imports have seen a significant moderation- exhibit 82. Oil as highlighted above is expected to remain low, consequently given that oil and related imports hold around 25-28% share in our import bill, the CAD is expected to remain modest. It should be noted that India imports c.1.7bn barrels of oil, of which 20-25% is re-exported. This amounts to around 1.3bn barrels on adjusting for re-exports. Thus, a USD 10/bbl increase implies additional import bill c.40bps of GDP

Exhibit 81. Lower oil prices are expected to take care of CAD



Source: CMIE, JM Financial

Exhibit 82. The global slowdown has moderated our import and export growth

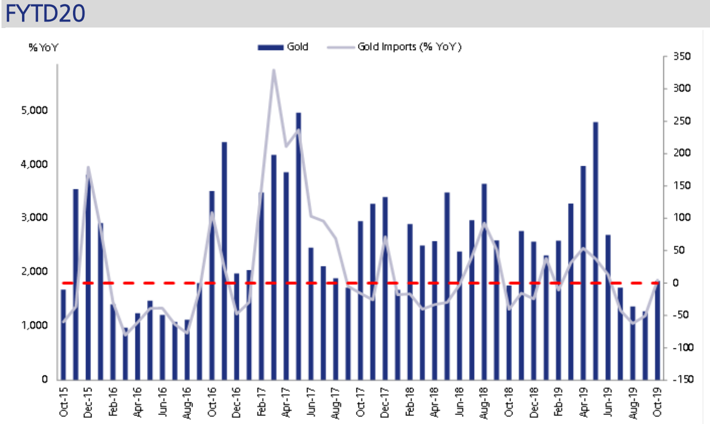


Source: CMIE, JM Financial

- The non-oil, non-gold deficit has been improving significantly: The Non-oil, non-gold trade deficit stood at USD 27bn vs. USD 38bn in FYTD19. This improvement in non-oil, non-gold deficit has been driven by interaction of these major goods balances (for period Apr-Oct)-
  - **Trade deficit moderated** for (1) Chemicals, (EX:IM share (% of total)::15:11) (2) electronic goods (EX:IM share:: 4:12)- sharp rise in telecom exports (3) ores & minerals: (EX-IM share: 2:5) (4) Ferrous & non-ferrous metals: (EX:IM:: 4:4)
  - **Higher trade surplus** for (1) Transport equipment (EX:IM share::9:4)
  - **Lower trade surplus** for (1) Agri. products (EX:IM share:: 11:5) driven by contraction in marine products, rice and buffalo meat (together c.45%+ of total agri. exports) despite decline in vegetables oil (edible) c. 40-52% share); (2) Textiles (Incl. readymade garments) (EX:IM share of 10:2), (3) Leather

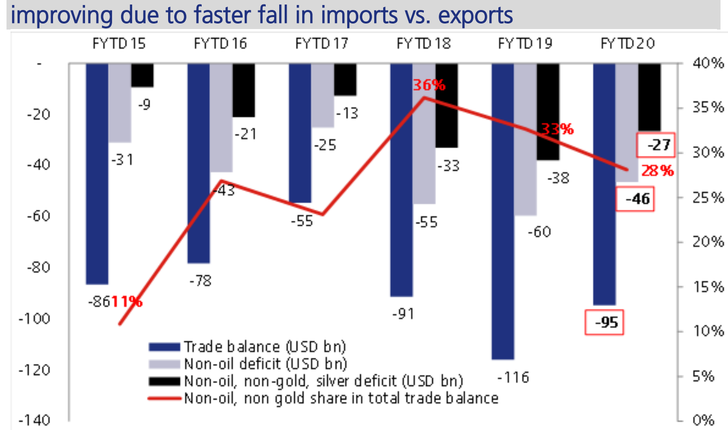
Even as gold prices remain significantly higher on a YoY basis, gold imports have witnessed a de-growth of 9%YoY FYTD20 (Apr-Oct'19) due to 21%YoY volume contraction.

Exhibit 83. Gold import growth in negative territory for most of FYTD20



Source: CMIE, JM Financial

Exhibit 84. The non-oil, non-gold merchandise deficit has been improving due to faster fall in imports vs. exports



Source: CMIE, JM Financial

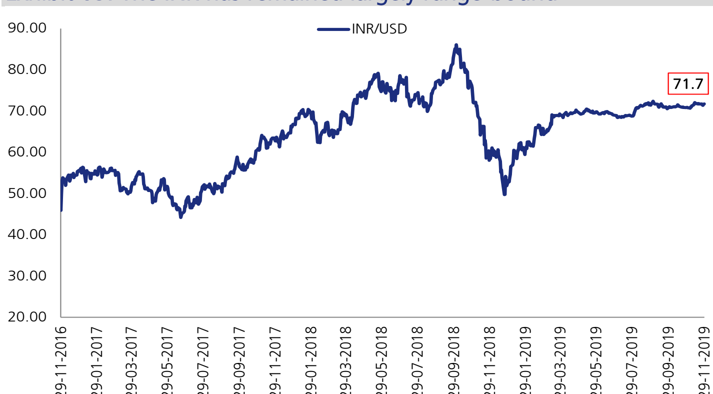
Outlook: The commencement of the US-China trade war, along with the new tax cut in the country have opened an opportunity for India. India has already had some short term benefits concerning agri exports- i) Shipping its first ever consignment of non-basmati rice to China in Sep'18, ii) approval to export raw sugar and soyabean to China, etc. The medium term consequences of a trade war will depend how the dynamics of the US-China trade truce, RCEP and global growth play out. The measures announced by the govt. would also boost exports in the medium run. These include-

- The phase out MEIS with RoDTEP effective 1Jan'20. This is positive for exporters as i) countries like the US have challenged India's export "subsidy" programmes, and ii) the outlay for RoDTEP is c.2x of MEIS (FY19 outlay c.INR270bn vs. RoDTEP outlay of INR 500bn annually). Going forward, clarity on the schemes' rates & relevant HS codes is awaited.
- The govt. also stated that Export Credit Guarantee Corporation (ECGC) will offer higher insurance cover to banks lending working capital for exports. Currently banks that lend to exporters ask them to obtain insurance cover from ECGC as protection against payment risk. ECGC arrives at the credit worthiness of buyers (importer) and limits the maximum amount that can be shipped at given point in time. The current announcement will raise the quantum of exports by allowing banks to take more risk as all risks from banks and exporters are borne by the govt. (estimated cost c. INR 170bn).
- The govt. announced the revised Priority Sector Lending norms for Export Credit, which releases additional INR 360bn to INR 680bn as export credit under priority sector. This will be a positive when coupled with the announcement on ECGC.
- In the longer term, the announcement of the set up FTA Utilisation Mission to work with Federation of Indian Export organisations and export houses to utilise concessional tariffs in each FTA is an essential steps taken by govt. as currently most exporters remain unaware about completely utilising FTA agreements.

Implications on the INR- Upward pressures likely

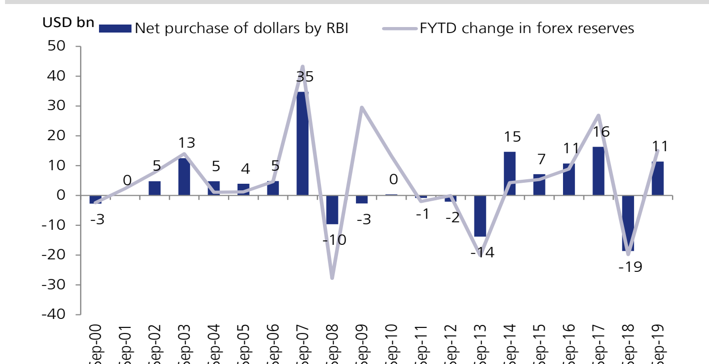
The EMBI bonds spreads, reflected by JP Morgan Index have fallen by 112bps since the local peak of 435bps in Dec'18. Despite the surge of flows driven by global monetary easing, the INR has largely remained range-bound since mid-2019 due RBI's active dollar purchase (exhibit 86). The INR currently stands at an FYTD20 average of 70.3 With certain assumptions on the expected movement in i) oil, ii) dollar index, iii) interest diffferential and iv) inflation differential, we expect the INR to remain in the range 70-72.5 until Jun-20.

Exhibit 85. The INR has remained largely range-bound



Source: Bloomberg, JM Financial

Exhibit 86. FYTD20 the RBI has bought dollars worth USD 11bn vs. net sale in FYTD19



Source: CMIE, JM Financial

Exhibit 87. The INR has underperformed major EMs since Oct'19

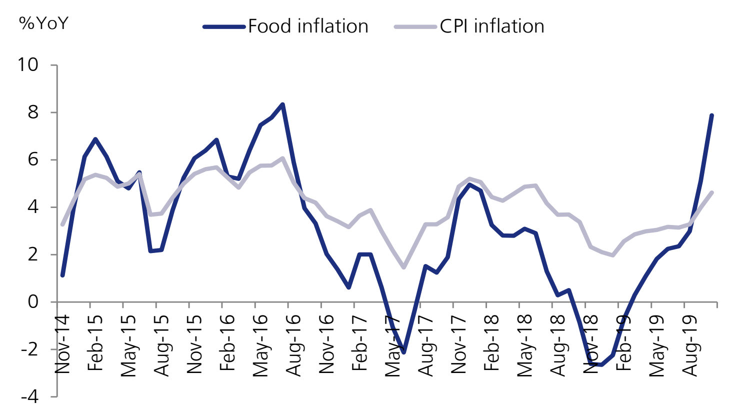
% change	YTD	FYTD	Since Jul'19	Post Oct'19
Brazil	9%	10%	10%	1%
Russia	-8%	-2%	1%	-2%
Indonesia	-2%	-1%	0%	-1%
South Africa	1%	3%	3%	-5%
India	3%	4%	5%	1%
China	2%	5%	2%	-2%
Taiwan	0%	-1%	-2%	-2%
Thailand	-7%	-5%	-2%	-1%

Source: Bloomberg, JM Financial

Inflation outlook and policy rates

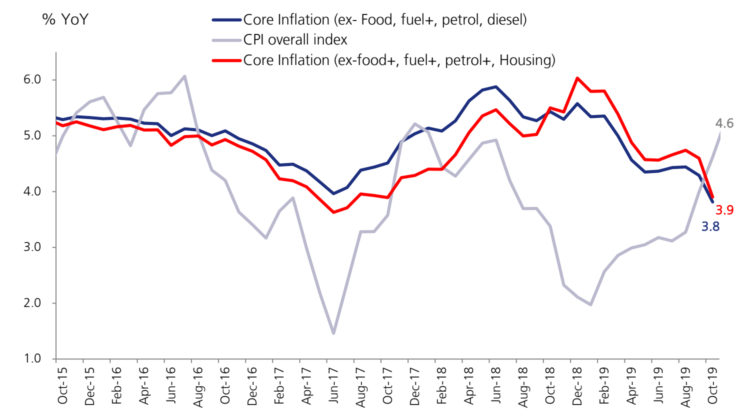
Inflation remained benign for most of the fiscal year which also led the RBI to slash the repo rate by almost 135bps since Feb'19. However, there has been a sudden uptick in inflation, primarily due to a more broad-based rise in food inflation (cereals, milk, pulses, sugar, vegetables, fruits). Core inflation on the other hand dipped to its lowest levels since the construction of the new series at 3.8% YoY in Oct'19; reflecting the economic slowdown- exhibit 89.

Exhibit 88. CPI inflation breached RBI's medium term target of 4.0% in Oct'19



Source: CMIE, JM Financial

Exhibit 89. Core inflation on the downward trend due to growth slowdown



Source: CMIE, JM Financial

Inflation outlook: The present food inflation uptick is largely supply driven. However, due to i) overall high food stock levels, ii) increase in crop productivity, and iii) subdued global Agri commodity prices; sustained high food inflation (high single digits) is unlikely in the medium term. Going forward, we expect food inflation to remain above 5%+ until Dec'19, post which it is expected to moderate. Our view on various heads in given below:

Exhibit 90. Food inflation expectations

	Weight	FYTD20 (%YoY)	Expectations	Inflation Outlook
Cereals	9.67%	1.45	Stable	Rice prices remain subdued on account of high production along with subdued global prices impacting retail prices. The adverse impact from high rainfall on production is largely limited for Paddy. Wheat is expected to see a strong Rabi sowing going ahead (because of high moisture level in ground) with a shift from pulses; and hence would have price increase in a limited range. Coarse cereals (maize, Jowar, etc.) would see significant rain related adverse impact and price rise, but their weightages in CPI food is low to impact it meaningfully.
Pulses	2.38%	5.80	Minor uptick	The production of pulses has remained in the range of 23-25mn tonnes in past three years, largely meeting the consumption demand. In addition, FY17 & FY18 had imports of 5-7mn tonnes, creating a scenario of glut. Pulses imports came down in FY19 to c.2mn tonnes and demand supply normalised by end of FY20. In FY20, kharif pulses production (c.40% of total production) is likely to be lower at least by 10-15%YoY, and initial sowing trends for Rabi is not encouraging. However, this year would also witness an expansion in Rabi sown area and net net Rabi pulses sowing should not end significantly below FY19. Pulses pricing therefore could remain volatile and with an upward bias till Jan-Feb'20; and then would normalise based on i) Rabi final sowing data (Rabi sowing is delayed this year as kharif was delayed), and ii) any effort made by Govt. to increase imports. Additionally, Government still has c.3.5mn tonnes of pulses in stock (majority gram) and a reversion of pulses inflation of 2014-15 time frame is not likely at this point.
Fruits	2.89%	-1.66	Stable	No material movement and would remain low
Sugar	1.36%	-1.08		There has been over global oversupply scenario in sugar which still persists. However, excess rainfall and crop destruction would lead to lower production from India and would support prices and arrest any more declines. Expected to see a minor uptick or a stable trend.
Milk	6.61%	1.26		Retail milk prices has seen some uptick in selected regions (Amul, Tamil Nadu), but a sustained price increase is still not visible and inflation could be largely stable.
Eggs, meat	4.04%	8.25	Stable	
Spices	2.50%	2.17	Stable	
Vegetables oils	3.56%	0.99		Global vegetable prices remain subdued and so any sharp uptick is not expected.
Vegetables	6.04%	9.32	Volatile, uptick in recent period	Vegetables prices would remain volatile and would be driving higher inflation in near term. Onions in particular would see prices at elevated levels for 1-2 months; till imports arrive and export slowdown reflects in the markets. However, once weather becomes normal, given a good rainfall, aggregate vegetable production should benefit and would limit price rise.

Source: JM Financial; FYTD: Arp-Oct'19

Core inflation is unlikely to show a reasonable uptick unless growth picks up. While gold price are expected to moderate hence containing the upwards pressure on core inflation, two key items mentioned below are likely to raise core inflation by c.50bps by 1QFY21. Overall we estimate core inflation c.4.3%YoY by Jun'20 vs. 3.8% currently.

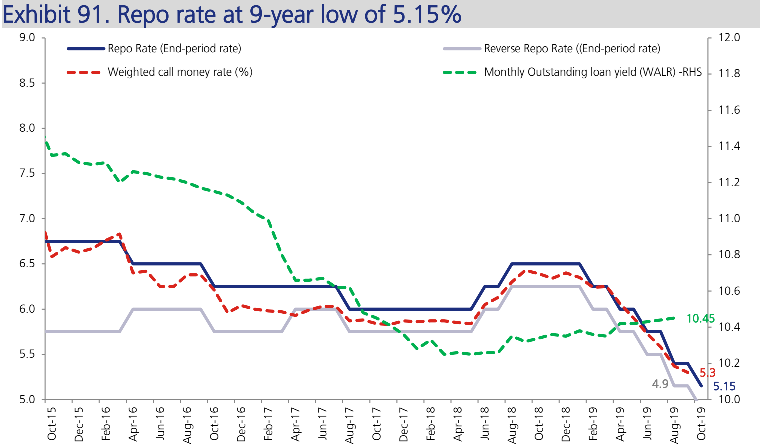
i) **Mobile tariffs (Wt: 1.84%):** The weighted average tariff increase from Oct-19 to Aug-20 is expected to be c.22% which is expected to translate to increase in CPI index of 41bps at the current weightage of 1.84%

ii) **Motor cars/ cycle (Wt: 1.3%):** On the basis of purely BS6 transition, cumulative car prices increase starting Dec'19 to 1Apr'20 is around- i) 5% for cars (wt: 0.48%) and ii) 12% for 2W (wt: 0.79%). Since these together hold c. 1.3% weight in the CPI Index, these price chages could bring an upside of c.6bps in CPI inflation.

RBI is expected to remain accommodative unless there are visible signs of growth

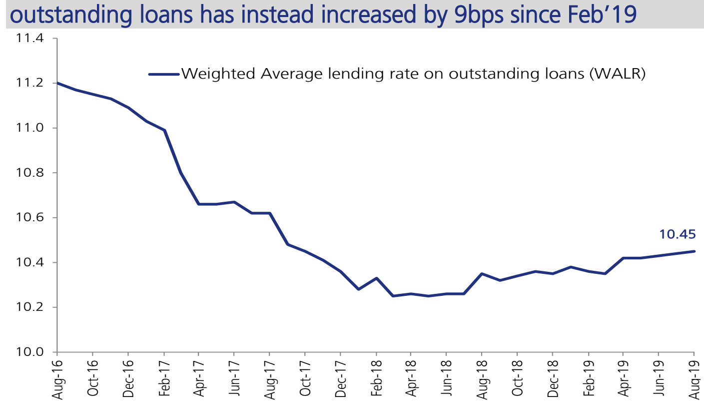
With our expectation that food inflation won't rise to double-digits, along with i) the RBI's priority to close the negative output gap, ii) scanty transmission of the cumulative rate cuts until Aug'19, and iii) limited fiscal space for additional growth stimulus are likely to keep the RBI engaged in rate cuts. However, the quantum of further rate cuts may be constrained by i) a possible terminal repo rate of the RBI given the 9-year low repo rate currently (5.15%); and ii) signaled pause by the FED.

Exhibit 91. Repo rate at 9-year low of 5.15%



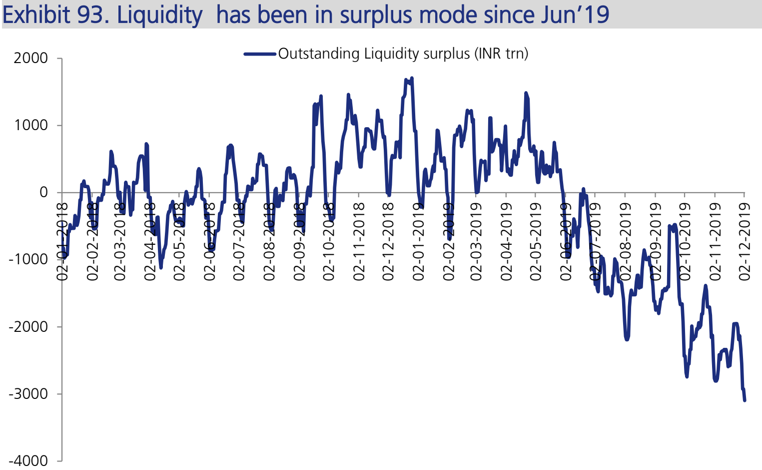
Source: RBI, JM Financial

Exhibit 92. Transmission so far has been scanty: WALR on outstanding loans has instead increased by 9bps since Feb'19



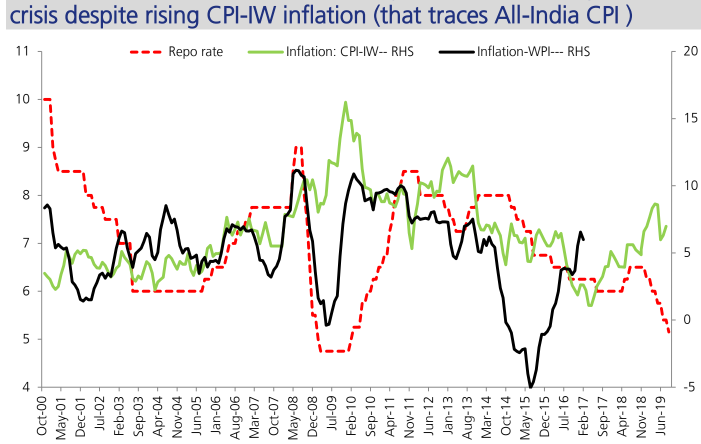
Source: RBI, CMIE, JM Financial

Exhibit 93. Liquidity has been in surplus mode since Jun'19



Source: Bloomberg, JM Financial

Exhibit 94. Repo rate was slashed by c. 425bps during the 2008 crisis despite rising CPI-IW inflation (that traces All-India CPI)



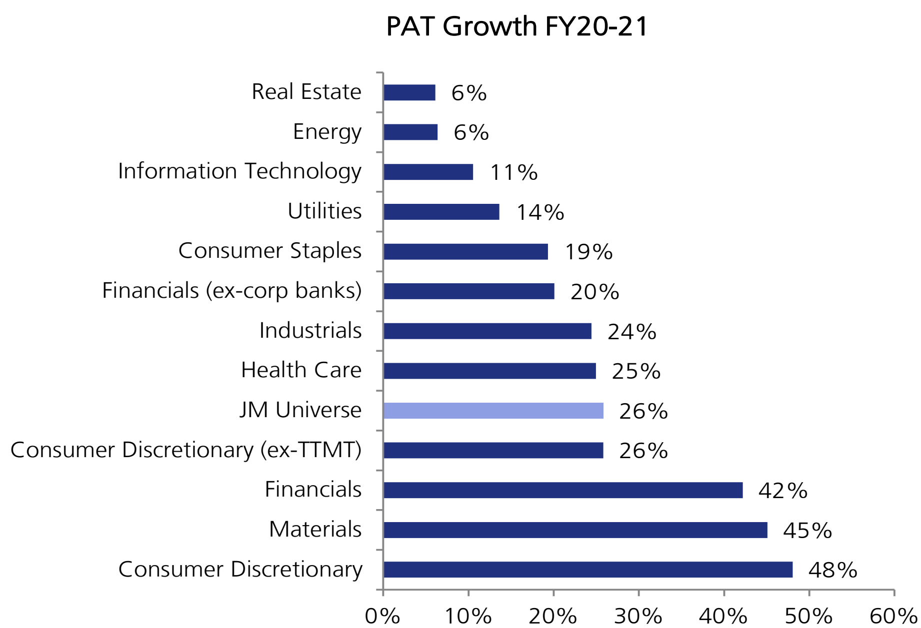
Source: CMIE, JM Financial

Earnings Growth

We estimate Nifty sales, EBITDA, and earnings growth of 5%/8%/14% YoY in FY20 and 11%/15%/29% YoY in FY21.

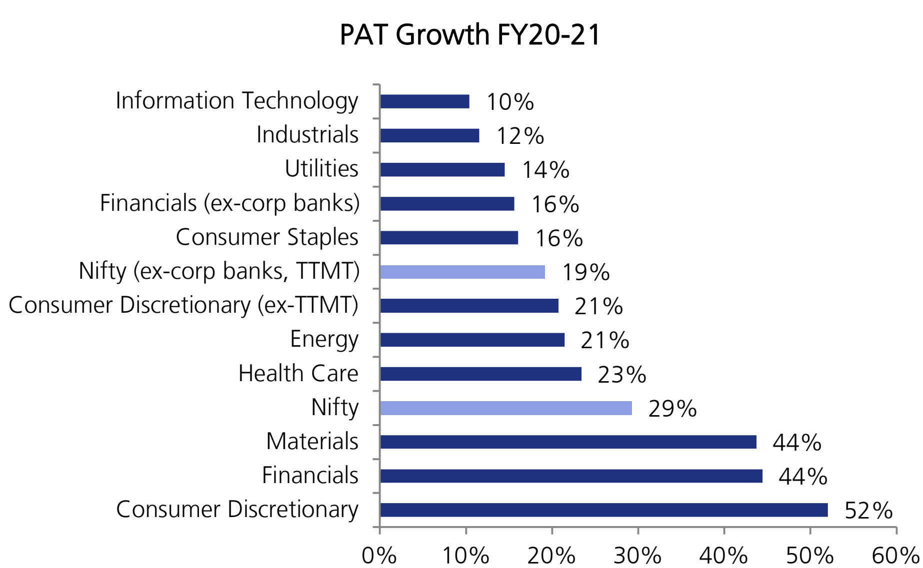
- Drivers of earnings growth: The earnings growth for FY21 for the JM Universe and Nifty is mainly driven by consumer discretionary, financials and materials. If we were to exclude the 4 large corporate banks (SBI, ICICI, Axis, and Yes) and Tata Motors, the Nifty FY21 earnings growth falls from 29%YoY to 19%YoY. Normalisation of credit costs, reduction in tax rate and cyclical recovery are the key drivers for the earnings growth for the next year. The lowest growth rates are expected from IT and industrials for Nifty, and energy and IT for the JM universe.

Exhibit 95. JM Universe (171 companies)



Source: JM Financial

Exhibit 96. Nifty and Nifty constituents



Source: JM Financial

- **Sector-wise contribution to earnings:** To analyse further we looked at the sector-wise contribution to Nifty EPS over the years. It can be clearly seen that share of profits of financials is estimated to increase further, as share of few sectors (consumer discretionary, IT, healthcare) are expected to decline. Another interesting observation is that financials, energy and IT account have accounted for over 60% of Nifty's EPS over the years, revealing its significant dependence on these 3 sectors.

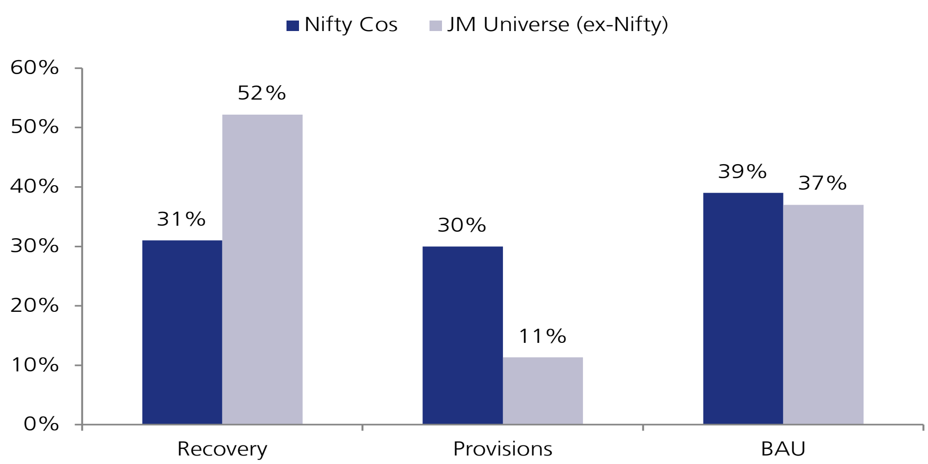
Exhibit 97. Sector-wise contribution to Nifty EPS

In INR	Absolute EPS (sector-wise)							% contribution to Nifty EPS						
Sector	FY15	FY16	FY17	FY18	FY19	FY20E	FY21E	FY15	FY16	FY17	FY18	FY19	FY20E	FY21E
Materials	25	15	23	30	53	40	57	6%	4%	6%	7%	11%	7%	8%
Industrials	14	13	22	23	26	33	37	3%	3%	6%	5%	5%	6%	5%
Health Care	15	15	18	12	10	11	13	4%	4%	5%	3%	2%	2%	2%
Financials	122	104	94	107	111	170	245	30%	27%	24%	23%	23%	31%	35%
Telecommunication Services	6	8	5	4	0	0	3	1%	2%	1%	1%	0%	0%	0%
Consumer Discretionary	49	46	45	41	32	27	42	12%	12%	11%	9%	7%	5%	6%
Energy	73	72	69	115	112	115	140	18%	19%	17%	25%	23%	21%	20%
Utilities	15	17	22	24	29	30	34	4%	4%	6%	5%	6%	5%	5%
Information Technology	64	64	70	72	74	77	85	16%	17%	18%	16%	15%	14%	12%
Consumer Staples	30	29	30	31	35	45	52	7%	8%	8%	7%	7%	8%	7%
Nifty EPS (in INR)	413	384	400	459	483	548	709	100%	100%	100%	100%	100%	100%	100%
Growth (% YoY)		-7%	4%	15%	5%	14%	29%							

Source: JM Financial

- **Macro recovery pivotal for delivering earnings growth:** For analysing the expected earnings growth in FY20-21, we categorised incremental earnings growth for each stock to be driven by (a) macro recovery, (b) provisions (in case of banks and NBFCs) or (c) business as usual (BAU). While this is a partly subjective exercise, we find that midcaps have a much higher recovery component (c.50%) built into the estimates vs. c.30% for Nifty; and for Nifty almost 1/3rd of the growth is contributed by lower provisioning by the larger banks. The companies (ex-financials) where we expect >20% YoY growth in earnings for FY21 are Maruti, Asian Paints, Pharma (Cipla, Sun Pharma, Dr Reddy's), Metals (Tata Steel, Hindalco, JSW Steel) and Ultratech.

Exhibit 98. Macro recovery crucial to deliver expected earnings growth



Source: JM Financial, BAU also includes inorganic growth opportunities

- **Expected growth of the key parameters of the Nifty constituents:** Our stock-wise expectations for the Nifty stocks are given below. We see risks to earnings in consumer discretionary (rural demand, economic recovery, fuel prices), metals (further decline in steel prices, slowdown in demand) and financials (increase in slippages and provisioning).

Exhibit 99. Forecasted growth for the Nifty constituents

	%YoY (FY19-20E)					%YoY (FY20E-21E)				
Nifty Stocks	Revenue	EBITDA	PAT	Change in EBITDA Margin	Change in PAT Margin	Revenue	EBITDA	PAT	Change in EBITDA Margin	Change in PAT Margin
ADANI PORTS	13%	11%	13%	-1%	0%	13%	14%	16%	1%	1%
ASIAN PAINTS	12%	17%	31%	1%	2%	16%	18%	21%	0%	1%
AXIS BANK	19%	25%	43%	3%	3%	17%	19%	125%	1%	15%
BAJAJ Finance	37%	42%	55%	2%	4%	27%	27%	30%	0%	1%
BHARTI AIRTEL	10%	15%	NA	1%	NA	3%	23%	NA	6%	NA
BHARTI INFRATEL	-1%	0%	-2%	0%	0%	2%	1%	3%	0%	0%
BAJAJ AUTO	4%	2%	10%	0%	1%	11%	17%	14%	1%	0%
BAJAJ FINSERV	96%	94%	67%	0%	-2%	21%	32%	19%	3%	0%
BPCL	-3%	0%	-5%	0%	0%	7%	18%	19%	0%	0%
BRITANNIA	8%	10%	22%	0%	1%	12%	16%	16%	1%	0%
CIPLA	2%	13%	7%	2%	0%	8%	14%	21%	1%	1%
COAL INDIA	-7%	-7%	4%	0%	2%	9%	22%	16%	3%	1%
DR. REDDY'S	8%	4%	3%	-1%	-1%	8%	19%	20%	2%	1%
EICHER MOTORS	3%	-11%	6%	-4%	1%	14%	18%	10%	1%	-1%
GAIL INDIA	-9%	-6%	-7%	1%	0%	3%	12%	8%	1%	0%
GRASIM	18%	-2%	181%	-4%	3%	3%	11%	6%	1%	0%
HCL TECHNOLOGIES	16%	16%	3%	0%	-2%	14%	16%	15%	1%	0%
HDFC	42%	46%	41%	2%	-1%	-10%	-12%	-12%	-2%	-1%
HDFC BANK	19%	22%	31%	1%	3%	19%	22%	26%	1%	2%
HERO MOTOCORP	-2%	-4%	1%	0%	0%	11%	13%	14%	0%	0%
HINDALCO	-4%	-10%	-25%	-1%	-1%	23%	23%	26%	0%	0%
HUL	7%	14%	20%	1%	2%	25%	31%	37%	1%	2%
ICICI BANK	18%	21%	180%	1%	11%	17%	19%	93%	1%	13%
INDUSIND BANK	24%	22%	57%	-1%	7%	23%	22%	32%	0%	2%
INFOSYS	10%	9%	7%	0%	-1%	12%	12%	9%	0%	0%
INDIAN OIL CORP	-3%	-9%	-23%	0%	-1%	12%	33%	40%	1%	1%
ITC	8%	9%	23%	1%	4%	10%	12%	13%	1%	1%
JSW STEEL	-12%	-27%	-47%	-4%	-4%	14%	19%	22%	1%	0%
KOTAK MAHINDRA BANK	21%	27%	41%	3%	5%	19%	23%	23%	2%	1%
LARSEN & TOUBRO	13%	24%	33%	1%	1%	11%	10%	11%	0%	0%
MAHINDRA & MAHINDRA	-5%	-3%	-13%	0%	-1%	10%	11%	12%	0%	0%
MARUTI SUZUKI	-6%	-24%	-23%	-3%	-2%	21%	43%	47%	2%	2%
NESTLE	11%	6%	17%	-1%	1%	13%	17%	19%	1%	1%
NTPC	11%	11%	9%	0%	0%	14%	18%	21%	1%	1%
OIL & NATURAL GAS CORP	9%	23%	47%	6%	8%	1%	-1%	-5%	-1%	-2%
POWER GRID CORP OF INDIA	24%	28%	11%	2%	-3%	8%	8%	11%	0%	1%
RELIANCE INDUSTRIES	5%	-1%	6%	-1%	0%	4%	-3%	0%	-1%	0%
STATE BANK OF INDIA	10%	13%	2078%	1%	13%	13%	19%	88%	3%	9%
SUN PHARMA	12%	14%	18%	0%	1%	12%	19%	27%	1%	2%
TATA STEEL	0%	-32%	-73%	-6%	-5%	5%	27%	154%	3%	3%
TCS	7%	7%	5%	0%	0%	10%	9%	10%	0%	0%
TECH MAHINDRA	8%	-5%	-1%	-2%	-1%	12%	19%	15%	1%	0%
Titan	11%	12%	14%	0%	0%	15%	19%	20%	0%	0%
TATA MOTORS	3%	-17%	-390%	-2%	-1%	14%	32%	NA	1%	NA
UPL	46%	76%	19%	3%	-1%	20%	35%	115%	2%	4%
ULTRATECH CEMENT	19%	40%	79%	3%	3%	19%	14%	26%	-1%	1%
VEDANTA	-2%	-7%	6%	-1%	1%	9%	14%	27%	1%	1%
WIPRO	4%	8%	12%	1%	1%	7%	7%	7%	0%	0%
YES BANK	9%	6%	-76%	-2%	-9%	11%	10%	496%	0%	11%
ZEE ENTERTAINMENT	13%	16%	36%	1%	4%	14%	18%	17%	1%	1%

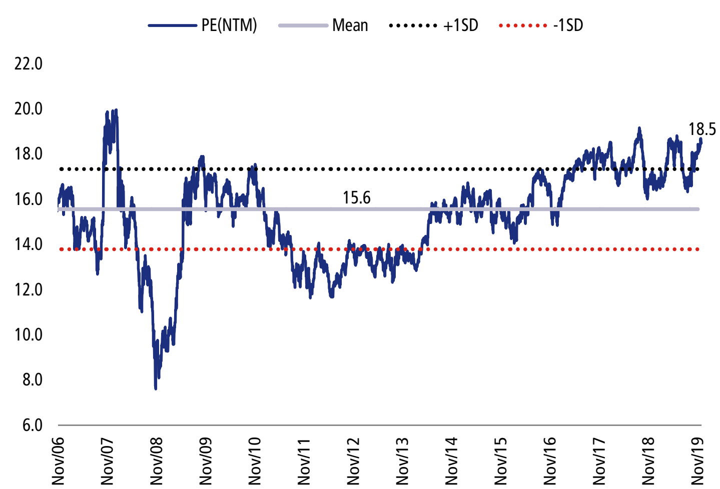
Source: Company, JM Financial

Valuations

We look at multiple valuation metrics to identify stocks for mispricing. We start with the market valuations. At an overall level, the broader market is trading at 18.5x, a premium of 18% to its long-term average. The yield differential between the risk-free and the market's earnings yield has been in a tight range of 90-110 bps in the month of November, given the drop in bond yields. While the yield gap at the start of FY20 was c.200bps, this drop in the yield gap looks similar to the period between April and September in 2016, when global yields came off and subsequently drove global growth. In our view, this round of drop in yields can also possibly lead to a short term burst of growth and feeds into our recovery thesis.

The Nifty Midcap/ Nifty PB ratio is trading just above its LTA of 0.7x. It can be seen that the market multiples are above neutral zone and while flows could take it higher, a macro recovery is essential to make it more sustainable.

Exhibit 100. Nifty NTM P/E at 18.5x

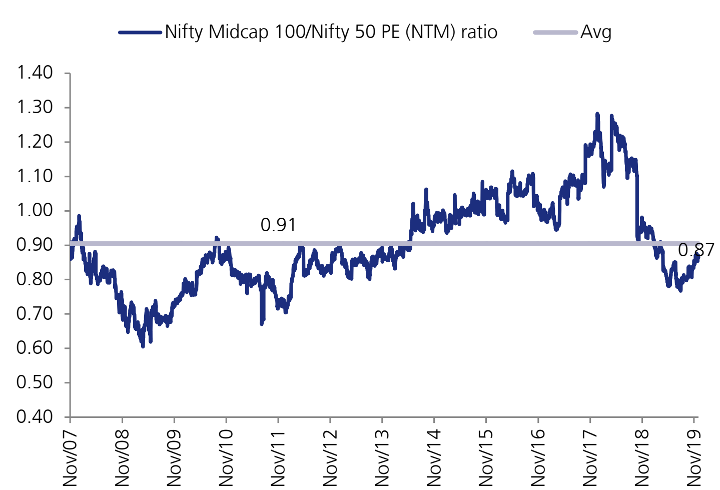


Source: Bloomberg, JM Financial

Exhibit 101. Nifty Trailing P/B at 2.9x

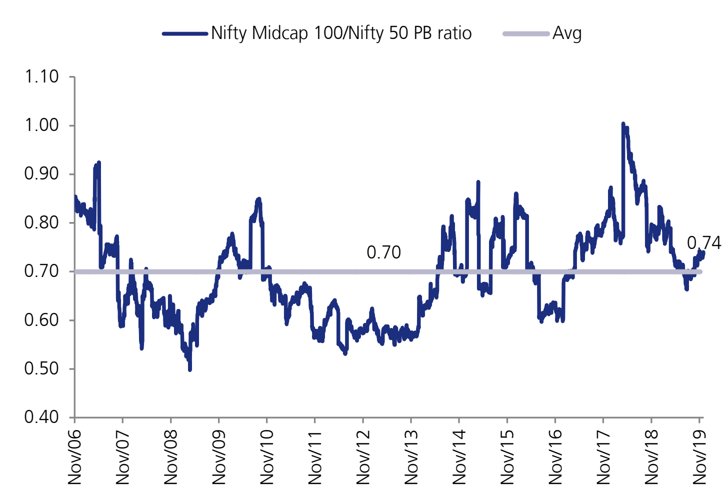
Source: Bloomberg, JM Financial

Exhibit 102. Nifty Midcap 100 to Nifty 50 PE (NTM) at 0.87



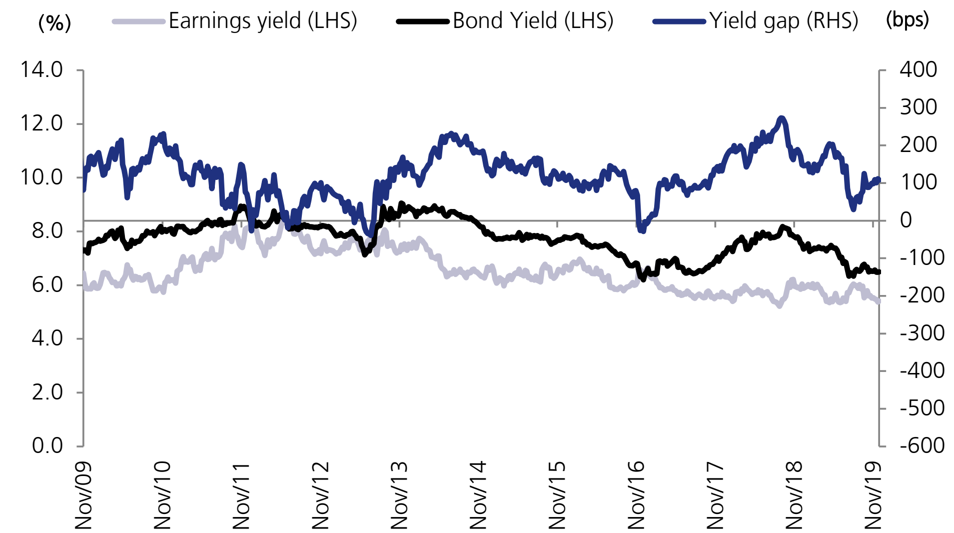
Source: Bloomberg, JM Financial

Exhibit 103. Nifty Midcap 100 to Nifty PB (TTM) at 0.74



Source: Bloomberg, JM Financial

Exhibit 104. Yield gap (10yr bond yield-Earnings yield) ~110bps



Source: JM Financial, Bloomberg

Exhibit 105. Global valuation – India has growth expectations at a premium to LTA

Country	Now				LTA				Premium/Discount			
	NTM EPS Growth	NTM PE	NTM PB	NTM RoE	NTM EPS Growth	NTM PE	NTM PB	NTM RoE	NTM EPS Growth	NTM PE	NTM PB	NTM RoE
India	26.9	19.7	2.8	14.2	16.7	16.0	2.6	16.1	60.5	23.2	8.3	(12.2)
US	9.0	17.9	3.3	18.4	11.6	15.0	2.5	16.5	(22.3)	19.3	32.8	11.3
Brazil	17.9	12.9	2.0	15.1	20.7	11.4	1.4	12.0	(13.7)	13.6	43.0	25.8
South Africa	16.2	11.4	1.6	14.5	15.8	12.9	2.0	15.4	2.5	(12.0)	(17.1)	(5.7)
Russia	2.6	6.5	0.9	13.4	3.6	5.7	0.7	11.5	(26.0)	13.2	32.3	16.9
China	25.0	16.0	2.3	14.6	26.9	19.7	2.6	13.3	(6.9)	(18.7)	(10.5)	10.1
Indonesia	10.6	14.9	2.1	14.3	15.6	14.9	2.5	17.0	(31.8)	0.1	(15.7)	(15.8)
Mexico	11.2	14.4	2.0	13.8	17.6	16.7	2.5	15.2	(36.2)	(14.3)	(21.7)	(8.7)
Taiwan	10.6	16.0	1.8	11.3	14.0	13.7	1.7	12.2	(24.4)	16.4	8.1	(7.1)
Thailand	9.9	15.6	1.7	11.0	41.7	13.2	1.8	13.3	(76.4)	18.1	(2.7)	(17.6)

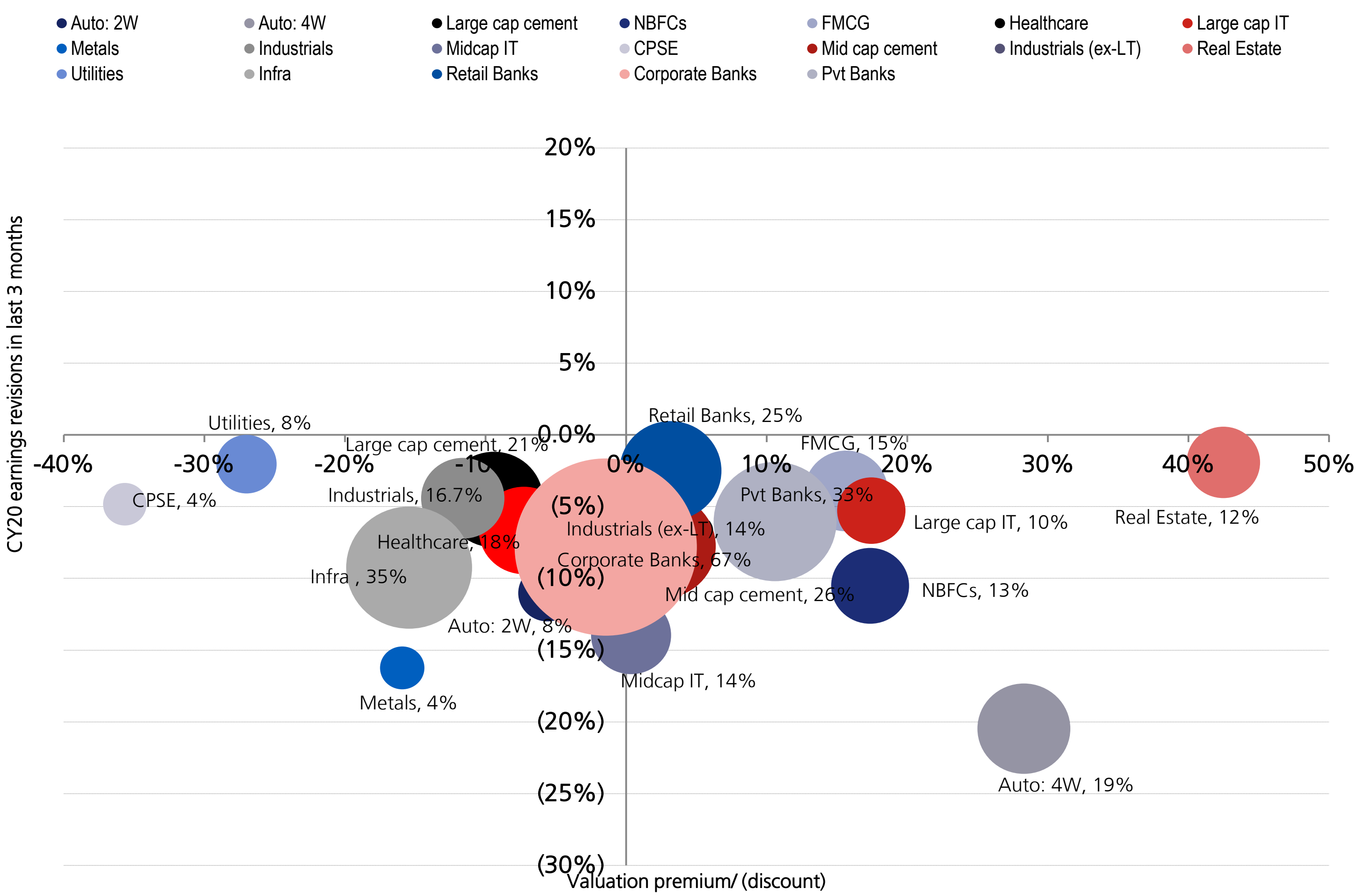
Source: Factset, JM Financial

We then look at sector valuations to identify sectors for mispricing

Sector Valuation

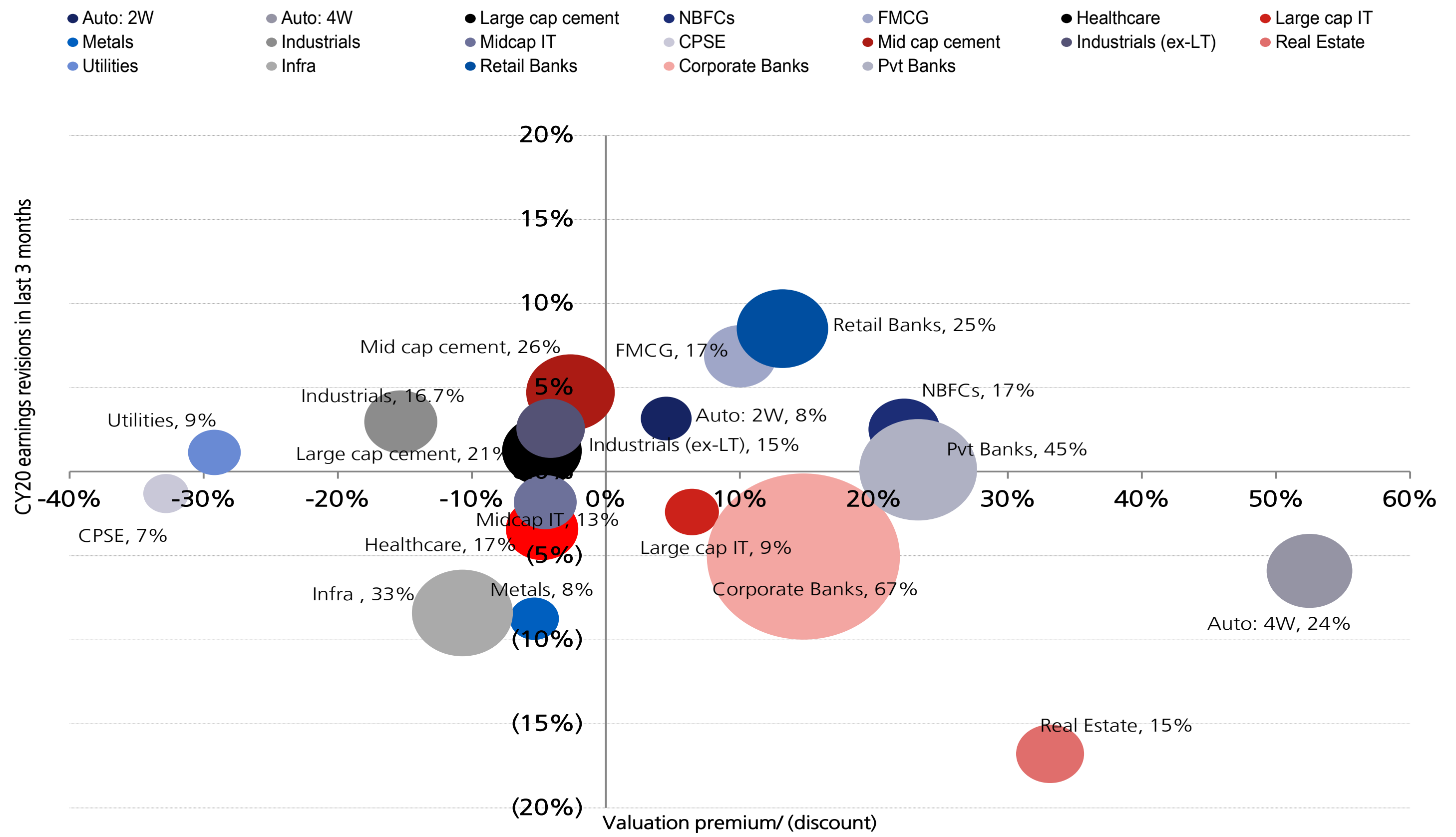
In the Exhibit below, we plot the earnings revisions for FY20 made YTD (Y-axis) with the premium/(discount) the sectors are trading at versus their long term trading history (X-Axis). The sectors that have seen earnings upgrade are retail banks, FMCG, cement and auto (2w). We see value in the following sectors : a) CPSE, b) Utilities, c) select healthcare stocks. Last year, we recommended a tactical trade in the CPSEs and this time we recommend Pharma as a tactical buy.

Exhibit 106. Sectoral positions (3 months back)



Source: Factset, JM Financial

Exhibit 107. Current sectoral positions- Retail Banks, FMCG, Cement and Auto (2W) see earnings upgrade



Source: Factset, JM Financial

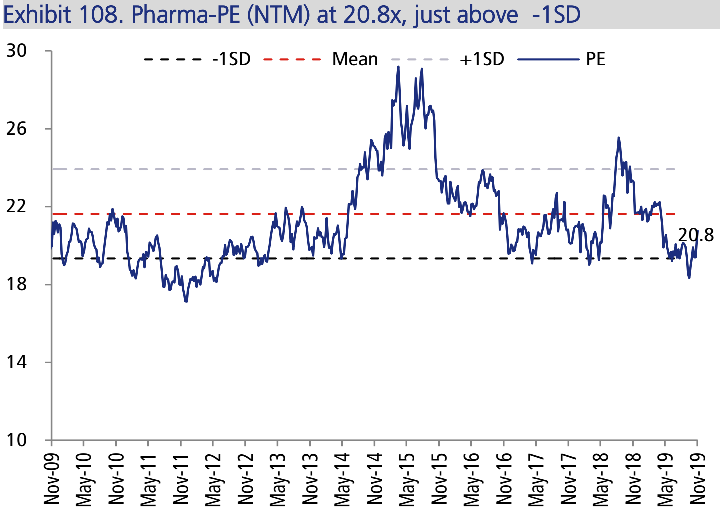
Pharma and healthcare- a tactical buy

We recommend pharma and healthcare as a tactical buy at this juncture. Valuations look attractive, PE (NTM) multiple stands at 21x (around 7 year low), even the PB (TTM) multiples for majority of the pharma stocks show that they are trading at a significant discount (30-60%) to LTA. The ROE has also fallen concurrently.

The weightage of pharma in Nifty has fallen by 500bps in last 5 years, and is around 10 year low. Mutual funds are overweight on Pharma, compared to BSE 500 index,but the weight itself is very low to make an assessment of overweight or underweight.

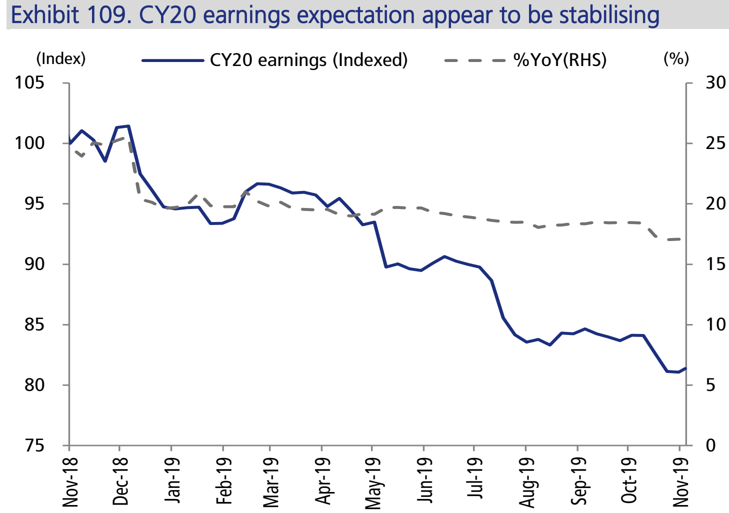
We prefer the following names Alembic, Torrent, Cipla, Natco and Sanofi.

Exhibit 108. Pharma-PE (NTM) at 20.8x, just above -1SD



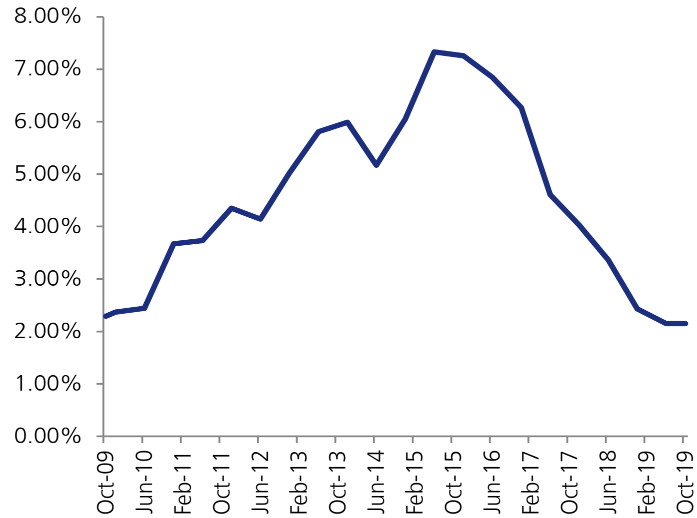
Source: Factset, JM Financial

Exhibit 109. CY20 earnings expectation appear to be stabilising



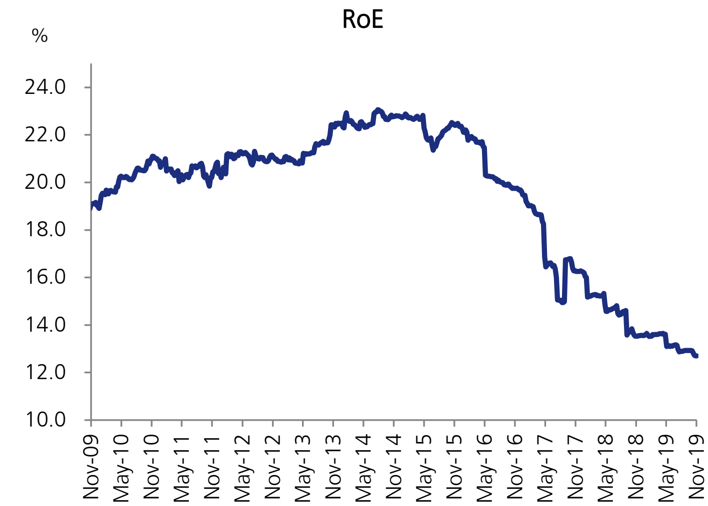
Source: Factset, JM Financial

Exhibit 110. Weightage of Pharma in Nifty ~10 year lows



Source: NSE JM Financial

Exhibit 111. ROE has fallen significantly

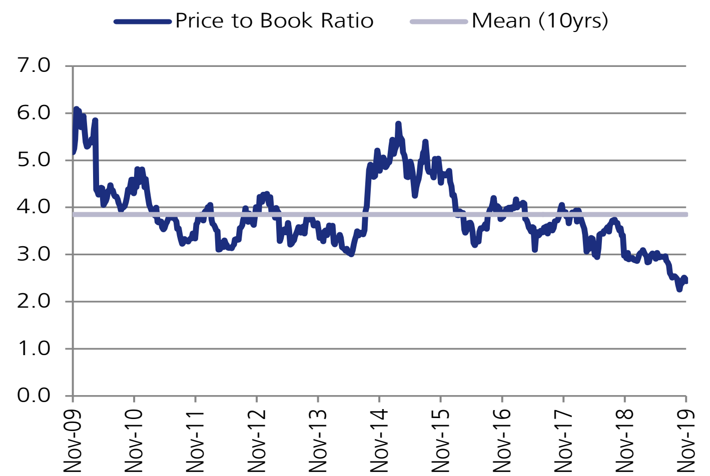


Source: Factset, JM Financial

Exhibit 112. Pharma stocks (Earnings revision vs valuation premium chart)

Source: Factset, JM Financial

Exhibit 113. Cipla- PB at 2.4x (35% discount to LTA)



Source: Bloomberg, JM Financial

Exhibit 114. Lupin- PB at 2.4x (60% discount to LTA)

Source: Bloomberg, JM Financial

Exhibit 115. Dr Reddy- PB at 3.2x (30% discount to LTA)

Source: Bloomberg, JM Financial

Exhibit 116. Sun Pharma- PB at 2.4x (55% discount to LTA)

Source: Bloomberg, JM Financial

Exhibit 117. Natco Pharma- PB at 2.9x (40% discount to LTA)

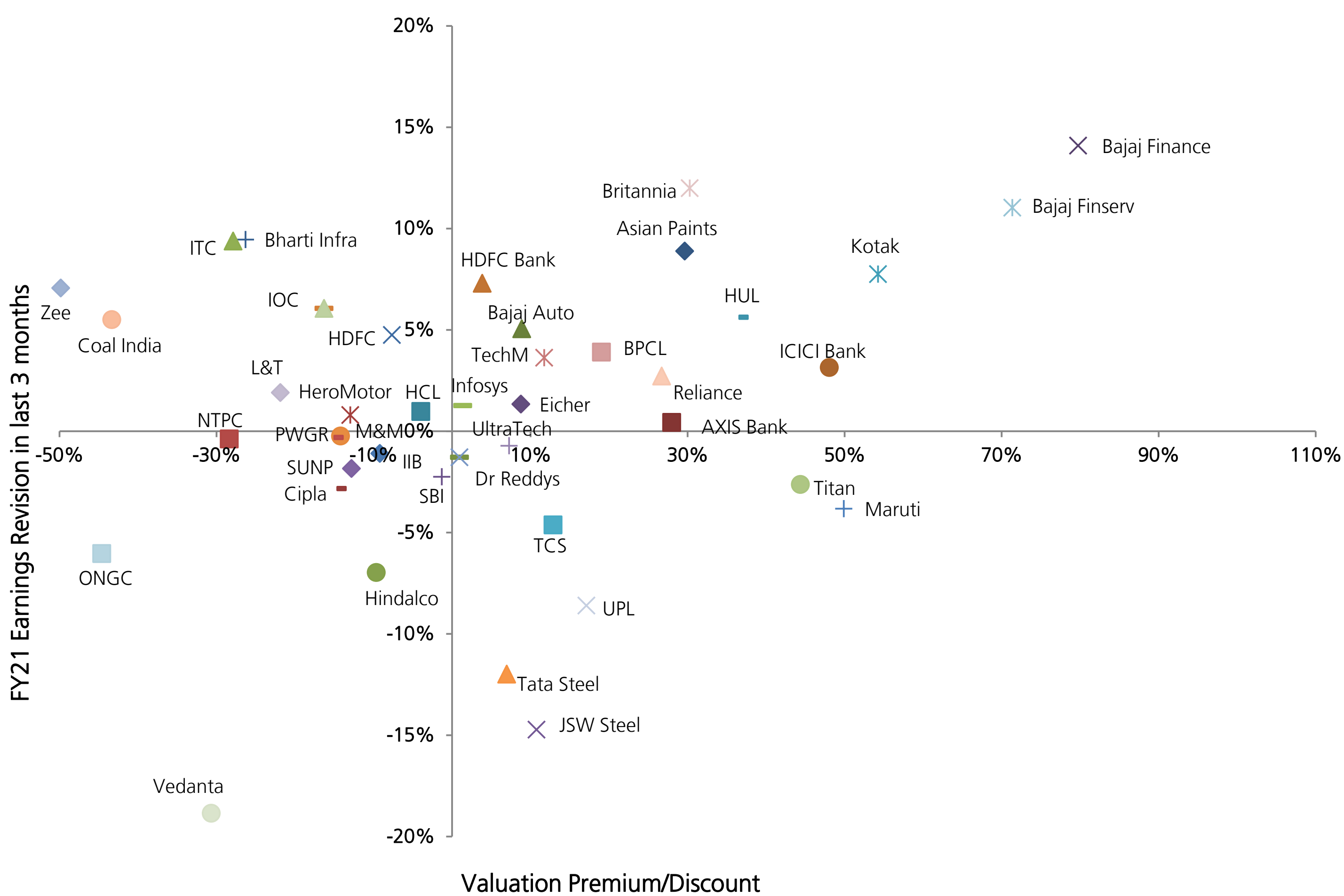
Source: JM Financial, Bloomberg

Exhibit 118. Torrent Pharma- PB at 6.3x (10% premium to LTA)

Source: JM Financial, Bloomberg

Moving from sectors to stocks, we try to pick out stocks where we see element of mispricing. We plot earnings revisions to premium/discount to valuations for the Nifty stocks (see Exhibit 119) and in our opinion, financial sector stocks stand out for their positive earnings revisions, while PSU stocks stand out for their valuation discounts.

Exhibit 119. Nifty Stocks (Earnings Revision vs Valuation Premium Chart)



Source:Factset, JM Financial

Model Portfolio

The recommended changes to the model portfolio, are listed in Exhibit 121. Post these changes, we are overweight healthcare, private financials, industrials and consumer discretionary.

Exhibit 120. JM Portfolio

Sector/Stock	Nifty Wt (%)	Portfolio Wt (%)	Stance	Mkt Cap (INR bn)	CMP INR/sh	YTD (%)
Consumer Discretionary	**7.2**	**8.5**	**OW**			
Britannia		0.8		733	3,048	(2)
Chalet Hotels		1.0		73	354	-
Dmart		1.0		1,147	1,833	14
Maruti Suzuki	2.1	2.7		2,156	7,139	(4)
Ashok Leyland		1.0		228	78	(24)
Sundram Fasteners		0.5		99	470	(12)
VIP Industries		0.5		61	429	(17)
Bharat Forge		1.0		209	448	(12)
Consumer Staples	**9.6**	**3.2**	**UW**			
Hindustan Unilever	3.2	3.2		4,391	2,028	11
Energy	**13.5**	**10.0**	**UW**			
Reliance Industries	10.2	10.0		10,009	1,579	41
Financials	**39.5**	**39.3**	**MW**			
HDFC Bank	10.9	10.0		6,874	1,255	19
ICICI Bank	6.1	6.6		3,293	509	41
IndusInd Bank	1.6	2.0		1,071	1,545	(3)
Bajaj Finance	2.0	3.0		2,385	3,965	50
Axis Bank	3.4	4.3		2,068	733	18
Bajaj Finserv	1.0	3.4		1,447	9,090	40
HDFC Ltd	7.5	7.5		4,009	2,320	18
Can Fin Homes		1.0		52	388	34
Bandhan Bank		1.5		931	578	5
Healthcare	**2.2**	**5.5**	**OW**			
Torrent Pharma		1.5		327	1,934	9
Cipla	0.5	1.0		366	454	(13)
Natco Pharma		1.0		106	582	(14)
Alembic Pharma	-	1.0		106	560	(7)
Sanofi India		1.0		162	7,040	11
Industrials	**4.4**	**8.3**	**OW**			
TeamLease Services		0.5		41	2,400	(16)
Voltas		1.0		228	690	25
Larsen & Toubro Ltd.	3.7	4.4		1,843	1,313	(9)
V Guard		1.4		98	230	1
Timken	-	1.0		68	899	55
Information Technology	**13.0**	**13.5**	**MW**			
Tech Mahindra	0.9	1.7		720	746	3
Infosys	5.1	5.1		2,974	698	7
TCS	4.9	4.9		7,696	2,051	11
HCL Technologies	1.3	1.3		1,526	1,125	17
Mindtree	-	0.5		118	717	(15)
Materials	**6.0**	**3.0**	**UW**			
Asian Paints	1.7	2.0		1,666	1,736	26
Ambuja Cement		1.0		401	202	(10)
Communication Services	**2.1**	**2.0**	**MW**			
Info Edge	-	1.0		312	2,553	77
Bharti Infratel	0.3	1.0		460	248	(4)
Utilities	**2.6**	**1.0**	**UW**			
GAIL	0.5	1.0		557	124	(31)
Cash		5.7				
Total	**100.0**	**100.0**				

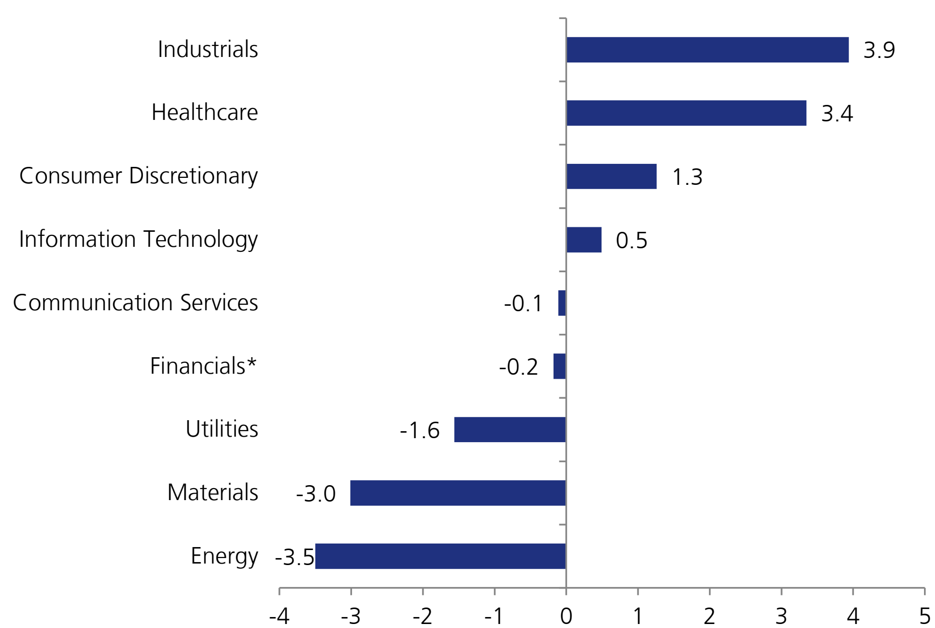
Source: JM Financial

Exhibit 121. Changes to the model portfolio

Action	Rationale
Add Can Fin Homes	Well-articulated strategy of new CEO, continuation of steady 16-18% loan growth with an upward bias, resilient margins aided by pricing power in tier 2/3 focused small ticket sized loans, best in class loan book mix (90% pure retail housing loans) with limited asset quality risks and 19-20% ROE forecast make us bullish on this HFC. At CMP, stock trades at 2x FY21E BV and 11x FY21E EPS for a PAT CAGR of 27% during FY19-FY21. Key Risk- Uncertainty of Canara Bank stake sale
Add Bharti Infratel	BHIN's Mar'21 DCF is INR 355, basis a 3-player mobile market sustaining. That would be upside of 35-40%. (at CMP). Stock is at FY21E EV/EBITDA of 7.5x and FCFF Yield of 7.5%. Stock has traded at 10x EV/EBITDA in the past prior to merger of Vodafone and Idea. Catalysts for BHIN stock- a) Jio matching new tariff of Bharti Airtel and Vodafone idea, b) Tenancy churn from VIL coming to end by 4QFY20, c)Govt. providing relief to telcos on AGR dues (part waiver, moratorium, staggered collection over 5-10 years, license fee reduction etc.), and d) VIL shareholders agreeing to put in INR 150-160bn of fresh equity
Add Sundram Fasteners	SFL, in our view, would continue to command premium multiples because of its strong management and promoter pedigree, constant focus to improve ROCE, high FCF generation of INR 10bn over FY20E-22E, continuous efforts to diversify revenue mix towards non-auto businesses and ability to improve margins. SFL in our view is set for consistent compounding on the back of an increase in its top line from demand revival, increase in capacity utilisations and higher non-auto contribution. We forecast a revenue/PAT CAGR 11%/21% during FY20-FY22E
Add VIP Industries	We continue to be bullish on VIP Industries' future growth prospect expecting its earnings to grow at CAGR 18% FY19-FY22E (considering lower corporate tax benefit). In our view, VIP's high-growth earnings phase from FY19-21E is yet to be factored in the price. Improvement in operational performance along with ROE (26%) as well as positive FCF generation in FY21E provides comfort. We recommend a BUY rating; valuing VIP Industries at 30x FY22E.
Add Alembic Pharma	Alembic continues to benefit from the churn in the US sartan market. With strong beats in US revenues and overall margins in the last 5 quarters being attributed to opportunities in US which might be non-recurring in nature, the stock is yet to price in the earnings impact of Alembic's ability to consistently exploit such opportunities. Even with modest assumptions of growth in the base US and domestic businesses, at 15x FY21E EPS, the stock is now trading at c.25% discount to its 5-year average trading range. Valuations are now compelling with the domestic formulations business now about to turn the corner.

Source: JM Financial

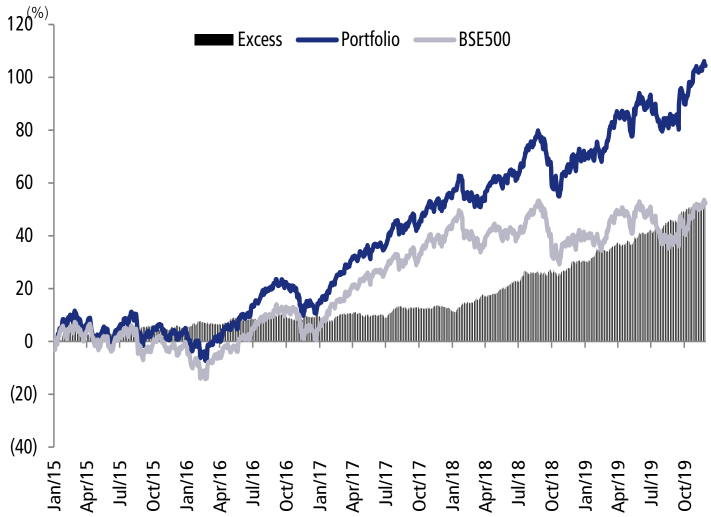
Exhibit 122. JM Portfolio weight over Nifty weight (OW on Industrials and Healthcare)



Source: JM Financial, *overweight on private financials

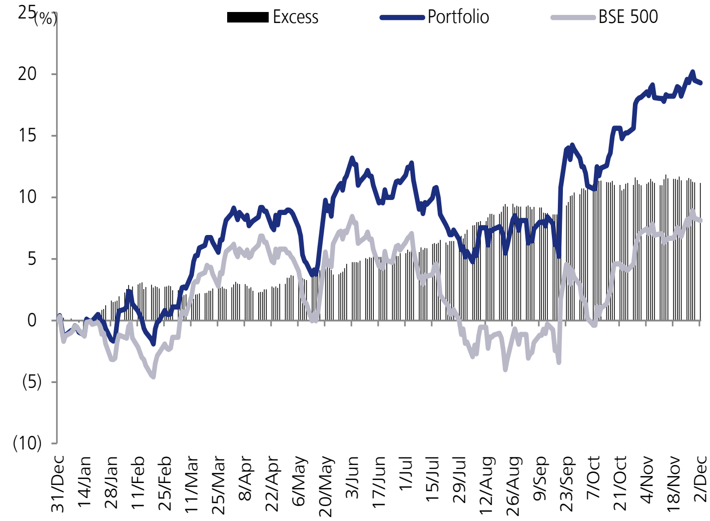
JM model portfolio performance : The model portfolio has outperformed the BSE500 benchmark by 52% since its inception in Jan '15 (vs. BSE500 return of 52.5%, excl. execution costs). YTD, the model portfolio's return of 19% has been better than BSE500's 8% YTD.

Exhibit 123. JM model portfolio vs. Nifty (excl. execution costs)



Source: Bloomberg, JM Financial, as on 2nd December, 2019, inception on 5th Jan '15

Exhibit 124. YTD, JM model portfolio vs. nifty (excl. execution costs)



Source: Bloomberg, JM Financial, as on 2nd December, 2019

Exhibit 125. High Frequency Indicators

Variable	Unit	FYTD20	Oct-19	Sep-19	Aug-19	Jul-19	Jun-19	May-19	Apr-19	FY19	Mar-19	Feb-19	Jan-19	Dec-18	Nov-18
Monetary															
Currency with public (M0)'	INR trn	21.6	21.6	21.9	21.8	20.9	21.2	21.2	20.9	20.6	20.6	20.3	19.9	19.5	19.2
10 year G-sec**	%	6.79	6.52	6.66	6.51	6.52	6.93	7.30	7.39	7.68	7.35	7.37	7.37	7.40	7.75
Outstanding liquidity ((+) implies deficit)***	INR trn	(2.3)	(2.5)	(1.9)	(1.6)	(1.6)	(1.4)	(0.3)	0.7	0.8	0.8	0.6	0.2	0.9	0.3
CPI inflation	%	3.5	4.6	4.0	3.2	3.2	3.2	3.1	3.0	3.4	2.9	2.6	2.0	2.1	2.3
Non-food credit growth	% YoY	(0.2)		8.1	9.8	11.4	(0.9)	11.4	11.9	12.3	12.3	13.2	13.1	12.8	13.8
Fiscal															
Total Receipts (Centre)	%YoY	15.6	(1.1)	(6.2)	70.5	55.3	(5.5)	(12.2)	36.6	7.4	22.9	(11.2)	17.3	10.7	(10.9)
Total Expenditure (Centre)	%YoY	13.6	9.1	34.3	25.9	23.9	(11.1)	3.5	14.0	7.9	(14.6)	17.6	20.3	(0.6)	(15.9)
Capital Expenditure (Centre)	%YoY	13.6	(5.1)	68.9	36.8	83.2	(34.1)	0.2	(34.5)	14.9	$	33.1	(35.0)	(61.1)	(32.8)
Revenue Expenditure (Centre)	%YoY	13.6	10.6	29.1	24.5	14.7	(8.5)	3.8	26.8	6.9	(47.3)	13.6	33.7	18.4	(13.7)
Centre's GFD (% of BE)	%	102.4	9.8	13.9	0.9	16.4	9.4	29.7	22.3	103.4	(33.0)	12.9	11.1	(2.4)	10.9
Central net market borrowings: FYTD ^^	INR bn	4,370	3,890	3,240	2,560	1,770	1,518	1,360	510	4,227	4,227	3,507	3,408	3,028	2,668
	%YoY	71.5	66.6	71.9	51.9	63.0	150.7	453.7	$	(5.7)	(5.7)	(21.8)	(20.1)	(23.5)	(24.0)
States net market borrowings: FYTD Cumulative^^	INR bn	4,783	1,945	1,564	1,278	850	589	374	249	3,496	3,496	3,168	2,685	2,406	2,074
	%YoY	17.3	14.5	13.7	10.0	(7.9)	(13.8)	(26.3)	(14.4)	2.5	2.5	6.0	0.5	(1.4)	(2.8)
Industrial															
Manufacturing PMI	Index	51.8	50.6	51.4	51.4	52.5	52.1	52.7	51.8	52.8	52.6	54.3	53.9	53.2	54.0
IIP	%YoY	1.3		(4.3)	(1.1)	4.3	1.2	4.5	4.3	3.6	(0.1)	0.1	1.7	2.6	0.3
Eight Core Industries	%YoY	0.25	(5.8)	(5.2)	(0.5)	2.7	0.7	5.1	6.3	4.3	4.8	2.2	1.5	2.6	3.6
Total CV sales	%YoY	(23.0)	(23.3)	(39.1)	(38.7)	(25.7)	(12.3)	(10.0)	(5.9)	17.6	0.3	(0.4)	2.2	(7.8)	5.7
Railway Freight (NTKm)	%YoY	(3.1)		(11.2)	(8.7)	(1.3)	0.0	0.7	1.9	6.6	7.2	4.4	5.5	2.7	5.6
Cargo handled at ports	%YoY	0.5	(5.1)	(0.3)	1.2	3.3	(0.5)	4.7	5.7	2.9	4.0	(0.5)	(2.3)	(4.0)	1.6
Truck Freight Rentals (Delhi to Mumbai) per 15 tonnes	INR '000	43.6	43.5	43.5	43.5	43.5	43.5	44.2	44.2	44.3	44.2	44.2	44.8	44.8	44.8
Consumption															
Domestic PV sales	%YoY	(20.2)	0.3	(23.7)	(31.6)	(31.0)	(17.5)	(20.5)	(17.1)	2.7	(3.0)	(1.1)	(1.9)	(0.4)	(3.4)
Domestic 2W sales	%YoY	(15.9)	(14.4)	(22.1)	(22.2)	(16.8)	(11.7)	(6.7)	(16.4)	4.9	(17.3)	(4.2)	(5.2)	(2.2)	7.1
Airline Revenue Passenger Km (domestic + international)	bn	105.0		17.1	17.8	17.5	17.8	17.9	16.8	225.2	18.6	18.4	20.9	20.8	19.2
JM Consumer RM Inflation#	%YoY	(8.6)	(13.2)	(10.2)	(9.2)	(11.5)	(10.1)	(6.7)	(2.0)	9.4	0.2	0.1	(2.4)	(2.6)	5.8
Fuel Consumption (Petrol+diesel)	% YoY	2.3	(2.9)	(0.7)	1.8	4.7	3.9	5.1	3.5	4.3	2.9	4.3	8.1	5.2	(1.5)
Digital															
Smartphone shipments	mn	36.9					36.9			144.5	32			36	
Online transactions volume (mobile + NEFT+IMPS)	mn	8,008.4		1,528.5	1,437.2	1,319.9	1,219.1	1,282.2	1,221.5	10,230	1,306.0	1,106.9	1,087.3	1,032.8	920.0
External															
Exchange Rate	INR/USD	70.3	71.1	71.3	71.2	68.8	69.4	69.8	69.4	69.9	69.5	71.2	70.7	70.7	71.8
Forex Reserves*	USD bn	448.6	442.6	433.6	428.6	429.6	427.7	421.9	418.5	411.9	411.9	399.2	398.2	393.4	393.7
Trade Balance	USD bn	94.6	11.0	10.9	13.5	13.4	15.3	15.4	15.3	(183.7)	(10.8)	(9.6)	(14.7)	(13.1)	(16.7)
Services Surplus	USD bn	38.3		6.2	6.2	6.3	6.8	6.2	6.7	78.4	6.6	6.8	6.7	6.6	6.6
CAD (% of GDP-Quarterly)	%	2.0					2.0			2.1	0.7			2.7	
Oil Prices##	USD/bbl	64.2	59.4	61.0	59.2	64.4	63.3	70.7	71.2	70.2	66.4	64.1	59.3	56.5	65.2
Flows (Net)															
FII inflows- Equity	USD bn	5.3~	2.1	0.9	(2.2)	(1.9)	0.15	1.4	1.5	1.76	6.1	2.4	(0.8)	0.3	0.9
FII inflow –Debt	USD bn	2.9~	0.7	(0.3)	1.6	1.2	1.2	0.5	(1.6)	(5.7)	2.9	(1.3)	(0.4)	0.8	0.9
Mutual fund inflows-Equity	INR bn	482.6	72.8	42	88.2	99.7	85.6	66.3	27.9	1,148	45.8	35.6	41.3	44.9	110.1
FDI Inflows	USD bn	20.9		1.7	1.7	3.8	7.0	2.1	4.4	34.6	3.7	2.4	3.7	3.2	1.1

Source: MoSPI, CGA, RBI, Bloomberg, CMIE, JM Financial;' as on 25Oct'19 ** average as on 29Nov'19, *** last day of month; as of 29Nov'19; ^^ As on 22Nov'19, #JM Proprietary Raw Material Index; ~ as on 28Nov'19, ## average till 29Nov'19, $ negative value in base year, * As on 22Nov'19

APPENDIX I

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(formerly known as JM Financial Securities Limited)

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Hold	Price expected to move in the range of 10% downside to 15% upside from the current market price.
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