FIRST LIGHT

18 August 2022

RESEARCH

India Strategy: Q1FY23 Review

Cost pressures behind us

SUMMARY

India Strategy: Q1FY23 Review

- Nifty 200 earnings were moderately below consensus, with only 40% of companies delivering a beat in Q1FY23
- India's market outlook is robust but could be swayed by global headwinds given heightened slowdown risks in China, EU and the US
- We maintain our conservative investment approach and remain positive on retail-focused lenders, staples and IT in the near term

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Daily macro indicators

Indicator	15-Aug	16-Aug	Chg (%)
US 10Y yield (%)	2.79	2.8	2bps
India 10Y yield (%)	7.27	7.29	2bps
USD/INR	79.64	79.66	0.0
Brent Crude (US$/bbl)	95.1	92.3	(2.9)
Dow	33,912	34,152	0.7
Hang Seng	20,041	19,831	(1.0)
Sensex	59,463	59,842	0.6
India FII (US$ mn)	**10-Aug**	**11-Aug**	**Chg ($ mn)**
FII-D	89.5	19.9	(69.7)
FII-E	308.8	282.9	(25.9)

Source: Bank of Baroda Economics Research

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Q1FY23 REVIEW

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Nifty 200 income still impacted by cost pressures: Nifty 200 companies were able to beat consensus revenue expectations by 4.2%, but their net income missed estimates by 3.1% in Q1FY23. In all, 42% of the companies reported revenue above consensus expectations (31% in Q4FY22). At the PAT level, 40% were ahead of consensus (38% in Q4) whereas 42% fell short (38% in Q4).

Robust growth in NSE universe earnings: Overall earnings for the NSE listed universe grew 39% YoY and 4% QoQ. Growth was led by the energy (74% YoY), utilities (60%) and consumer discretionary (43%) sectors, while healthcare (5%) and financials (12%) lagged. At the net profit level, real estate (152%) and consumer discretionary led (111%) outperformed. Cost pressures remained high with surging prices of raw materials, finished goods, power and fuel, but we believe input costs as a percentage of revenue likely peaked in Q1FY23. Wage expense appears to have stabilised and freight cost declined sharply.

Sector summary: The **life insurance** sector saw robust growth in premium with higher VNB (value of new business) margins. **Consumer durables** faced both demand and margin headwinds. High-cost inventory clouds the near-term outlook, but the festive season and good monsoons could provide a silver lining. Our **pharma** coverage reported muted growth on a high base. In **building materials,** demand varied across home decor segments, but margin pressure was visible across the board due to higher gas and timber costs. **Energy** and **commodity** companies had mixed results, while **banks** finally began focusing on growth as asset quality concerns abated. **FMCG** had a modest volume uptick and **IT** posted steady growth.

Investment view: We believe India is better placed than most peers amid the global volatility, though a meaningful capex cycle is still a few quarters away. Given that the Nifty 50 valuation has gradually inched back to +1SD from its 5Y mean, the upside from current levels looks limited. In our view, a conservative approach will serve investors better through CY22. We remain constructive on retail-focused lenders, consumption and IT sectors – the latter due to good earnings visibility and moderate valuations. We are cautious on energy and utilities, and largely neutral on other sectors.

Reporting season trends

India Q1FY23	QoQ (%)	YoY (%)
Net Sales	3.8	38.6
Raw materials	12.8	68.3
Salaries & wages	3.7	13.4
Interest expenses	4.7	7.5
PAT	(14.6)	20.5
Q1FY23 Surprise	**Revenue (%)**	**Income (%)**
Weighted	4.2	(3.1)
Average	5.7	0.5

Source: Bloomberg, BOBCAPS Research

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Recommendation scale: Recommendations and Absolute returns (%) over 12 months

BUY – Expected return >+15%

HOLD – Expected return from -6% to +15%

SELL – Expected return <-6%

Note: Recommendation structure changed with effect from 21 June 2021

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