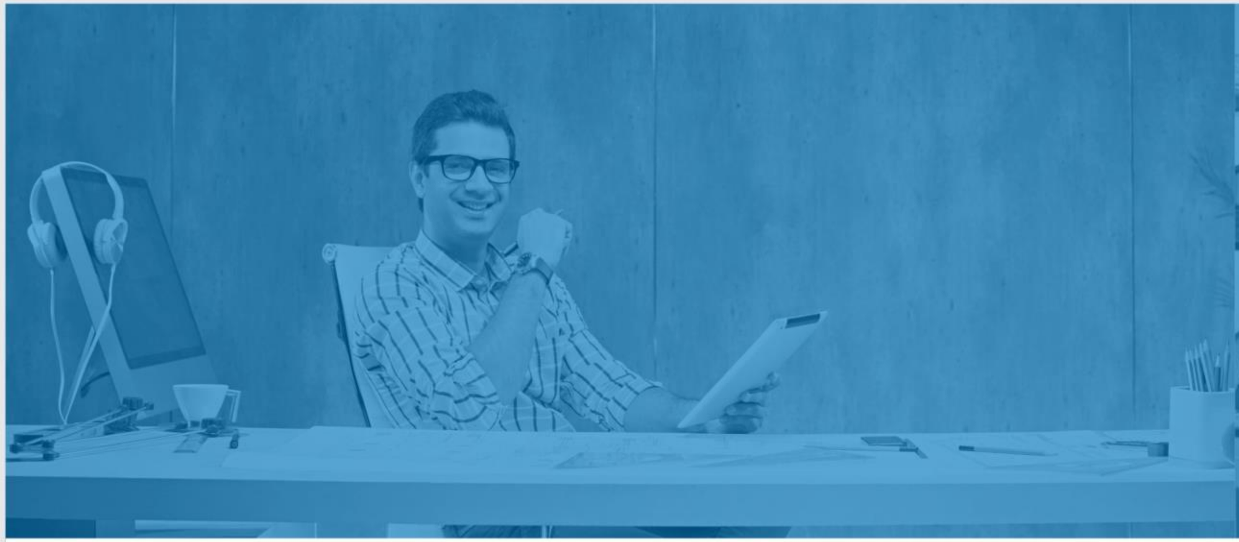

2020 Year-end Review & Outlook for 2021

January 2021

LIFE GOALS. **DONE.**

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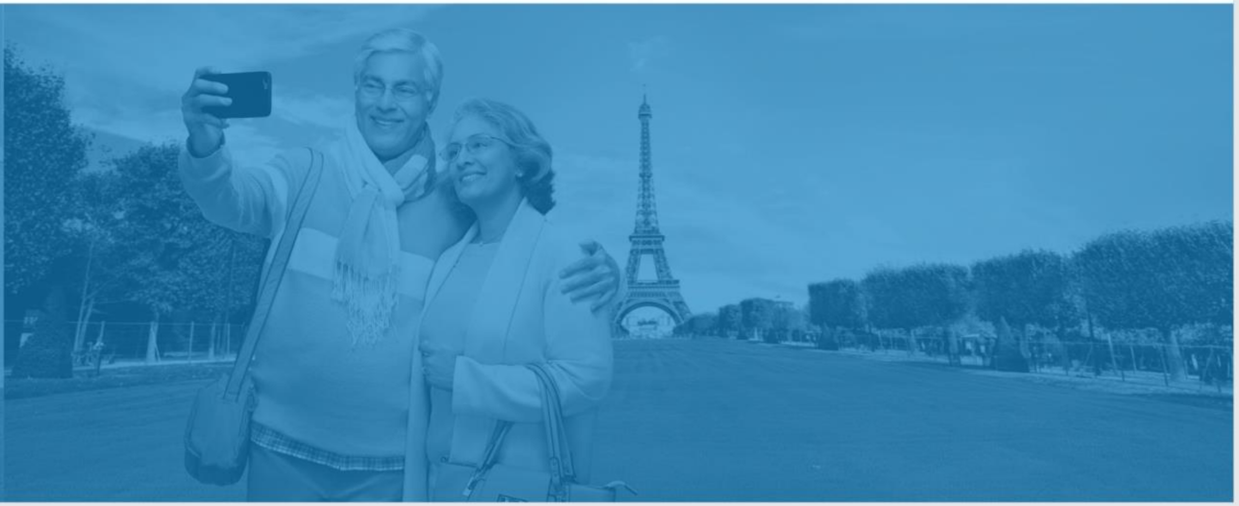


2020 – The Year That Was!

Covid-19 lockdown

- In March 2020, we witnessed the "Great Lockdown" across several countries. India saw one of the most stringent lock-downs globally.
- Economic activity plunged to record lows.
- Global markets (incl. India) saw a sharp fall in March.

Massive monetary & fiscal stimulus

- Global central banks & governments launch massive monetary & fiscal/economic stimulus to deal with Covid-19.
- Leads to a liquidity surge in global markets, helping them to start recovering.

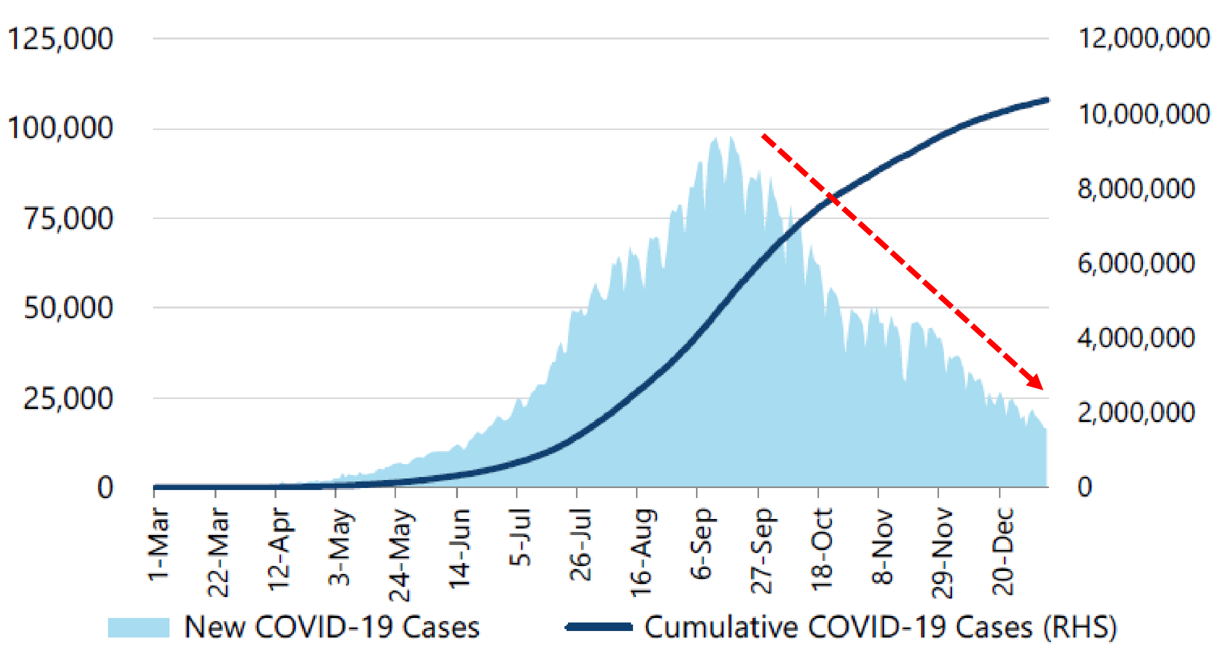
Economic & Market Recovery; Positive Vaccine News

- With opening-up of economies, we see a strong recovery in economic indicators.
- Global markets see sharp recovery and some cross pre-covid levels.
- Positive news on vaccine development & efficacy, although global cases continue to rise.
- Countries start launching and administering Covid-19 vaccines.

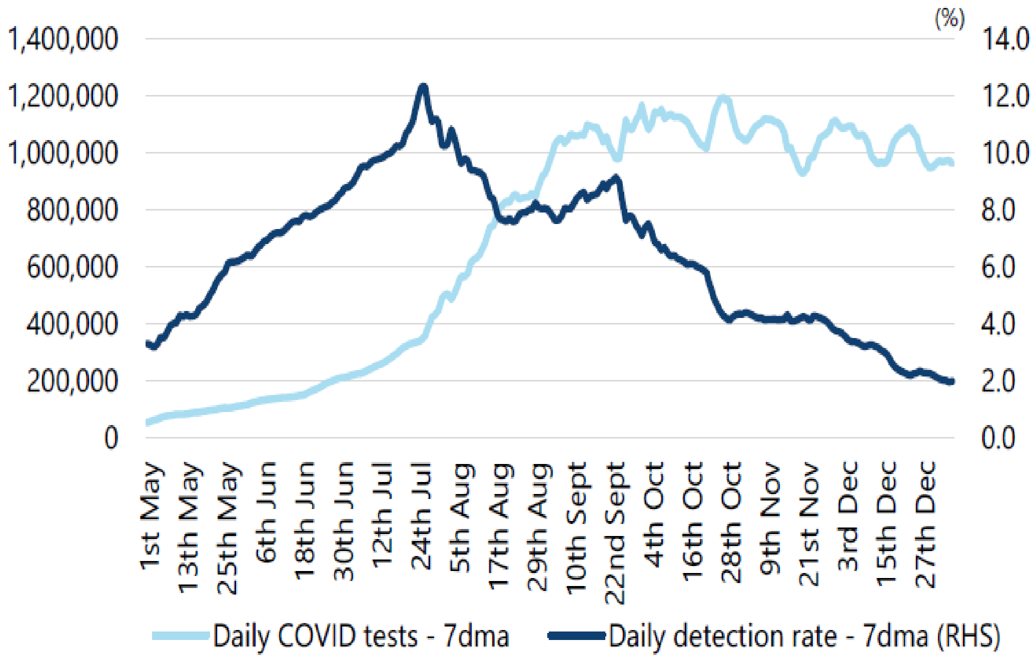
Greater digital adoption was a key theme due to the Covid lock-down, and we expect that to continue in coming years

Despite Covid-19 cases rising globally, India has seen a significant moderation

India- Covid-19 Cases Trend



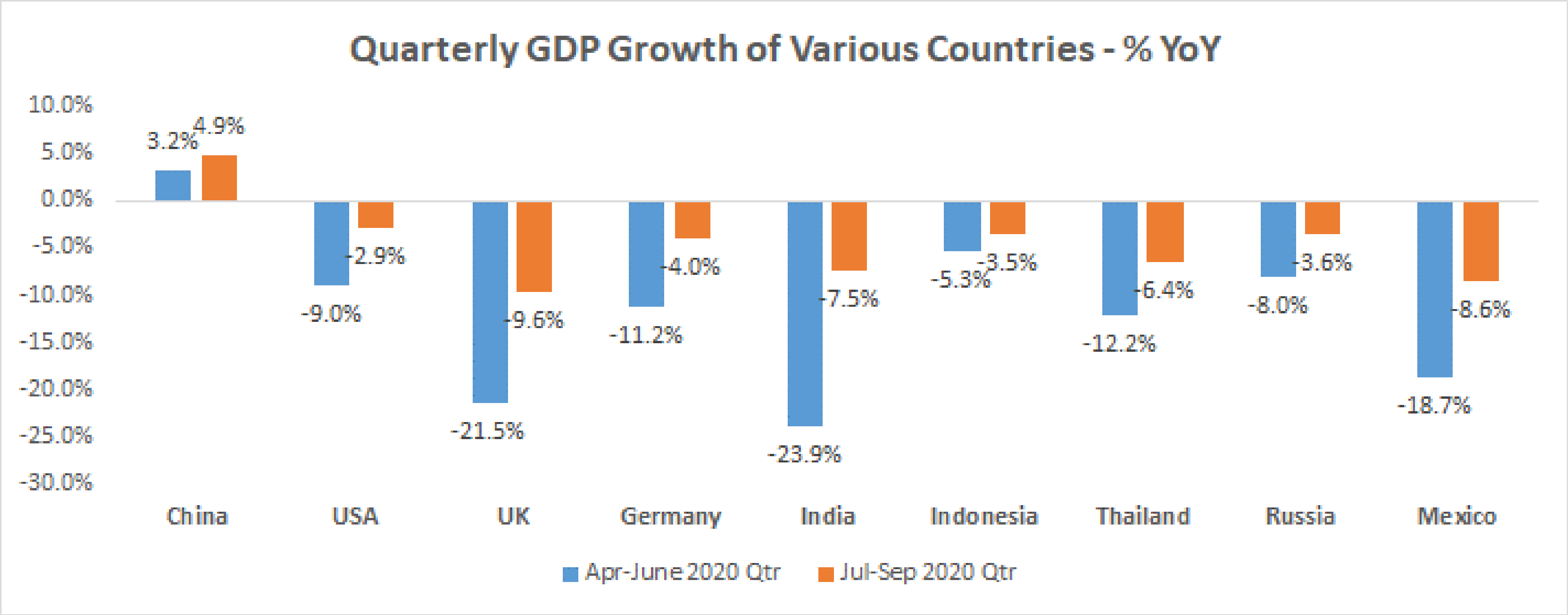
Covid detection rate in India has come down from 12% to 2%



- Globally, Covid-19 cases have been escalating (esp. in the US); Europe seeing some respite after a second wave
- In India, daily new cases have moderated significantly since the peak in Sep 2020, resulting in active cases coming down substantially and recovery rate rising to above 95%. Mortality rate has remained low in India (below 1.5%)

Source: Ministry of Health, ICMR, Jefferies

Global growth slowdown is not as sharp as feared; good recovery seen in Jul-Sep 20 Qtr

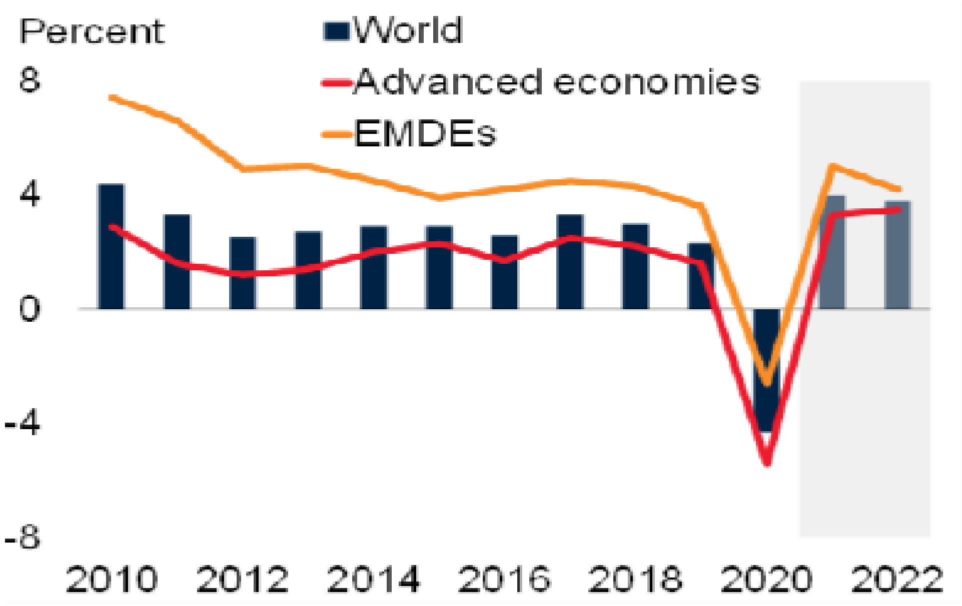


- Sharp recovery seen in Q2 FY21 (July –Sep 20) on account of opening up of economies, post lock-downs imposed earlier
- In India too, Q2 FY21 GDP contraction at -7.5% was better than RBI's projection of -9.8%, and a significant recovery from a record Q1 FY21 contraction of -23.9% (amidst one of the most stringent lock-downs globally)

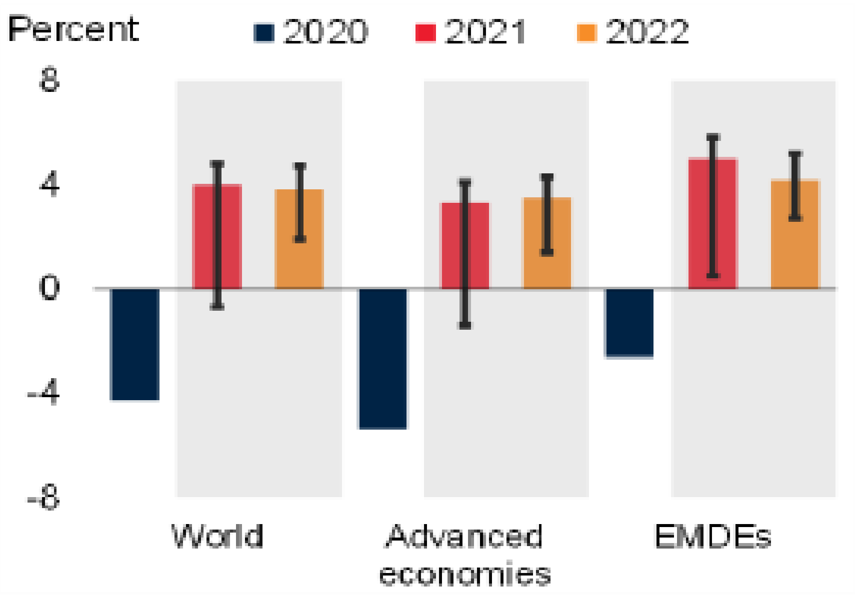
Source: Bloomberg

Global recession in 2020 may not be as deep as expected earlier; healthy recovery seen in 2021

Global GDP Growth Trend



Possible Scenarios of Global Growth

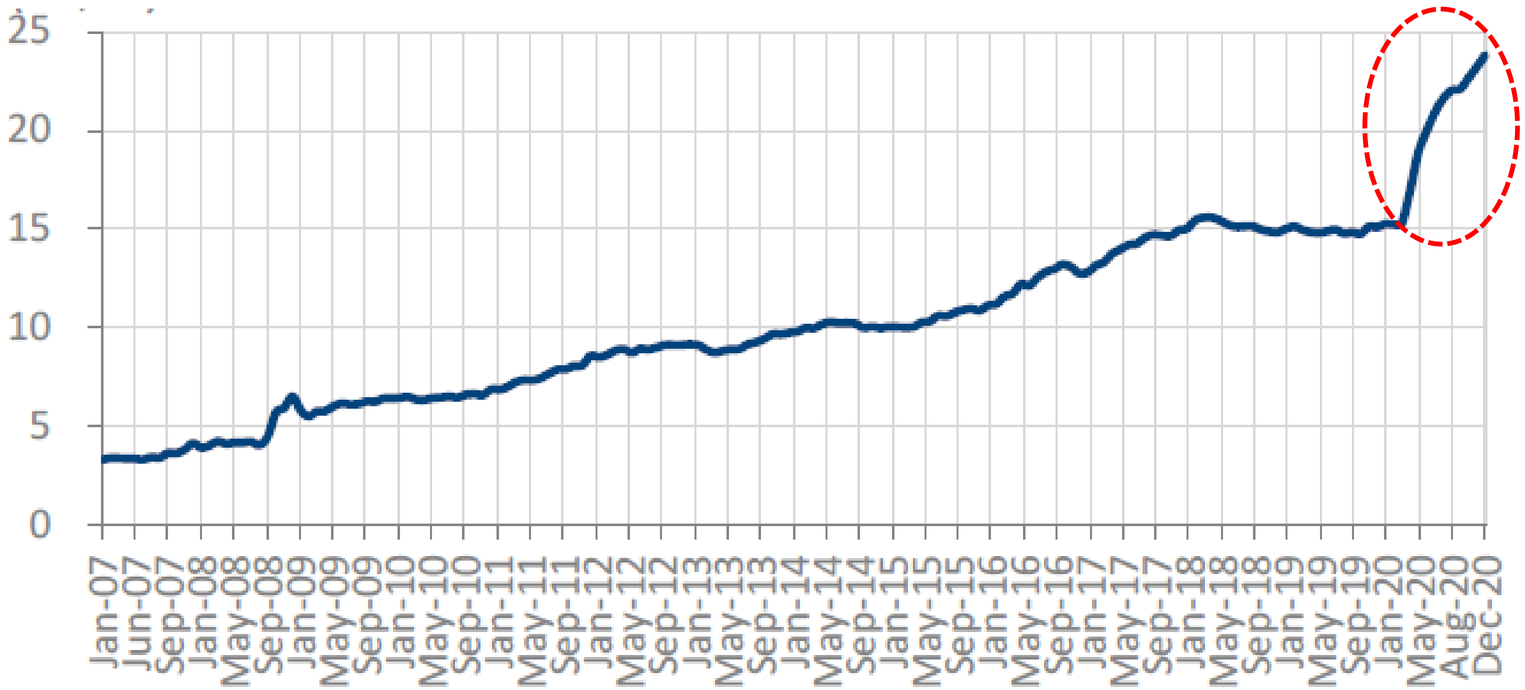


- World Bank projects global GDP to contract 4.3% in CY20 & grow by 4.0% in CY21. Global GDP expected to reach pre-pandemic level by end of 2021.
- Emerging markets GDP to contract by a lower 2.6% in CY20 (primarily helped by China) and grow by 5% in CY21.

Source: World Bank Global Economic Prospects, January 2021. EMDEs = Emerging Markets & Developing Economies

Major global central banks’ balance sheets have seen massive expansion in 2020

Central Bank Balance Sheet of G4* Countries - Combined (US$ in trillion)

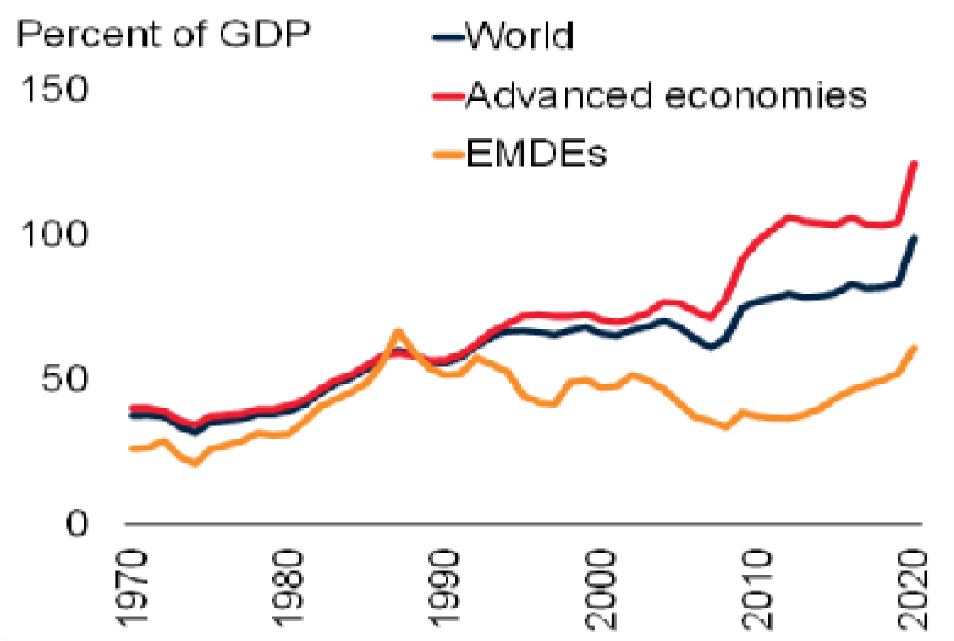


- Major central banks (esp. US Fed & ECB) have gone for massive monetary stimulus, leading to a global liquidity surge
- G4 central bank combined balance sheet has expanded by around $9 trillion in 2020, dwarfing the expansion seen during Global Financial Crisis (GFC) of 2008-09.

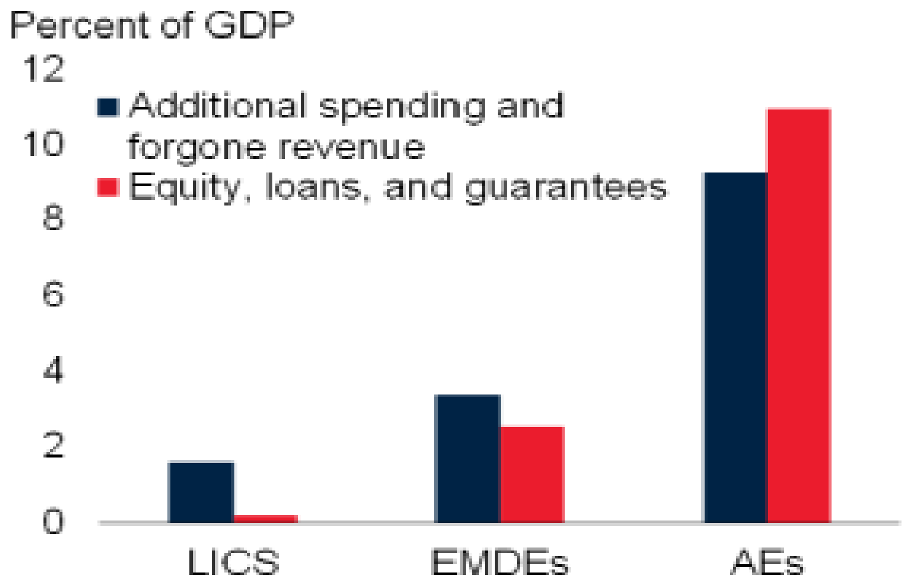
Source: Bloomberg, IIFL Research. *G4 includes US Fed, ECB, Bank of England and Bank of Japan

With massive Covid stimulus, government debt burden to expand

Government debt (as % of GDP)



Fiscal measures in response to Covid-19 pandemic (% of GDP)



- With large stimulus package to deal with Covid pandemic, global government debt burden (esp. of advanced economies) to further expand—which is a cause of concern.

Source: World Bank Global Economic Prospects, January 2021. AEs = Advanced Economies, EMDEs = Emerging Markets & Developing Economies. LICs = Low Income Countries

Most global markets have recovered and surpassed pre-covid levels

Performance of International Indices (ended Dec 2020, in %)					
Index Name	Country / Region	FYTD 21 9 mths	1 Yr	5 Yrs	10 Yrs
KOSPI	South Korea	63.8	30.8	7.9	3.4
BOVESPA	Brazil	63.0	2.9	22.4	5.6
IISL Nifty 50	**India**	**62.6**	**14.9**	**12.0**	**8.6**
MSCI EM PR USD	Emerging Mkts	52.2	15.8	10.2	1.2
TSEC TAIEX	Taiwan	51.8	22.8	12.1	5.1
MSCI Asia Ex Japan PR USD	Asia ex Japan	50.5	22.5	11.0	4.0
S&P 500	US	45.3	16.3	12.9	11.6
MSCI World PR USD	World	45.2	14.1	10.1	7.7
Nikkei 225	Japan	45.1	16.0	7.6	10.4
FSE DAX TR	Germany	38.1	3.5	5.0	7.1
RTS RTSI PR USD	Russia	36.8	-10.4	12.9	-2.4
JSX Composite	Indonesia	31.7	-5.1	5.4	4.9
S&P/ASX 200	Australia	29.7	-1.5	4.5	3.3
FTSE SET All Share	Thailand	27.0	-10.9	1.4	2.6
CAC 40	France	26.3	-7.1	3.7	3.9
Shanghai Composite	China	26.3	13.9	-0.4	2.1
FTSE Bursa Malaysia KLCI	Malaysia	20.5	2.4	-0.8	0.7
Hang Seng	Hong Kong	15.4	-3.4	4.4	1.7
FTSE/SGX STI	Singapore	14.6	-11.8	-0.3	-1.1
FTSE 100	UK	13.9	-14.3	0.7	0.9

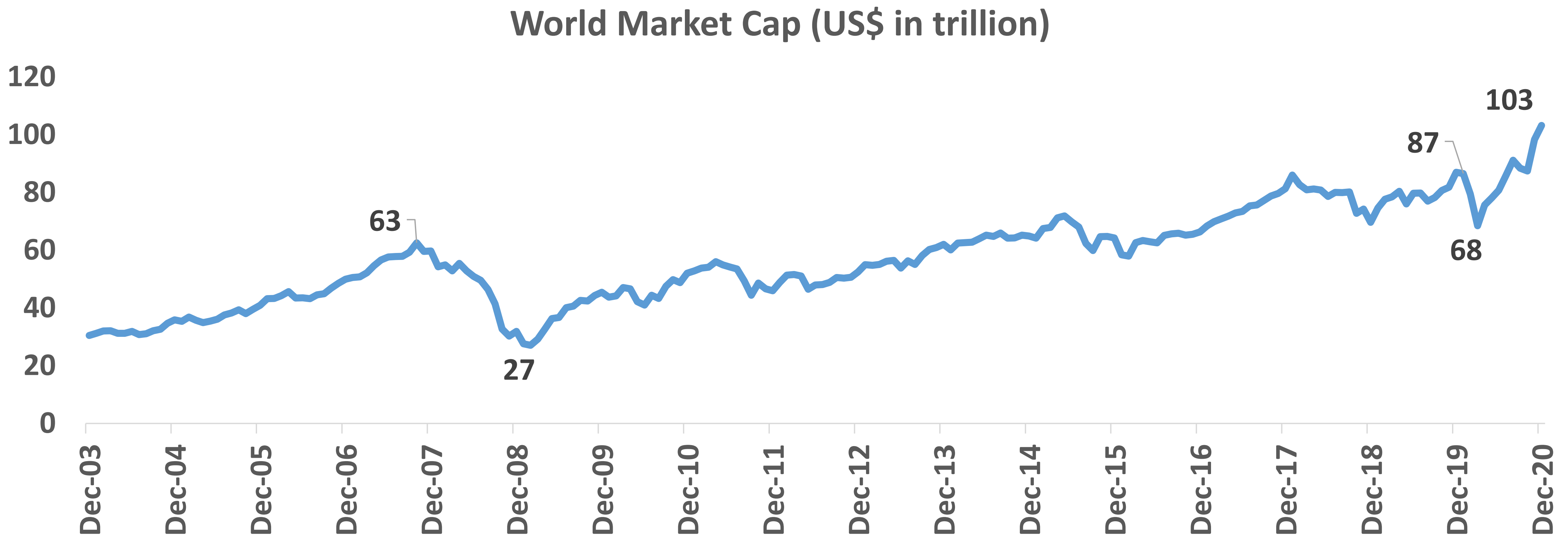
Source: Morningstar Direct. Returns are in local currency of index, and returns greater than 1 year are CAGR
Date sorted on the basis of FYTD 21 return in descending order

After a sharp correction in Feb-Mar 2020, a swift market recovery during FYTD 21 (April – Dec 2020)

- Indian markets among the top performers in FYTD21
- Massive liquidity infusion by major central banks
- Positive news on Covid vaccine & launches
- Strong economic recovery

- Over the long term (5 & 10 years) Indian market has outperformed most peer Emerging Markets

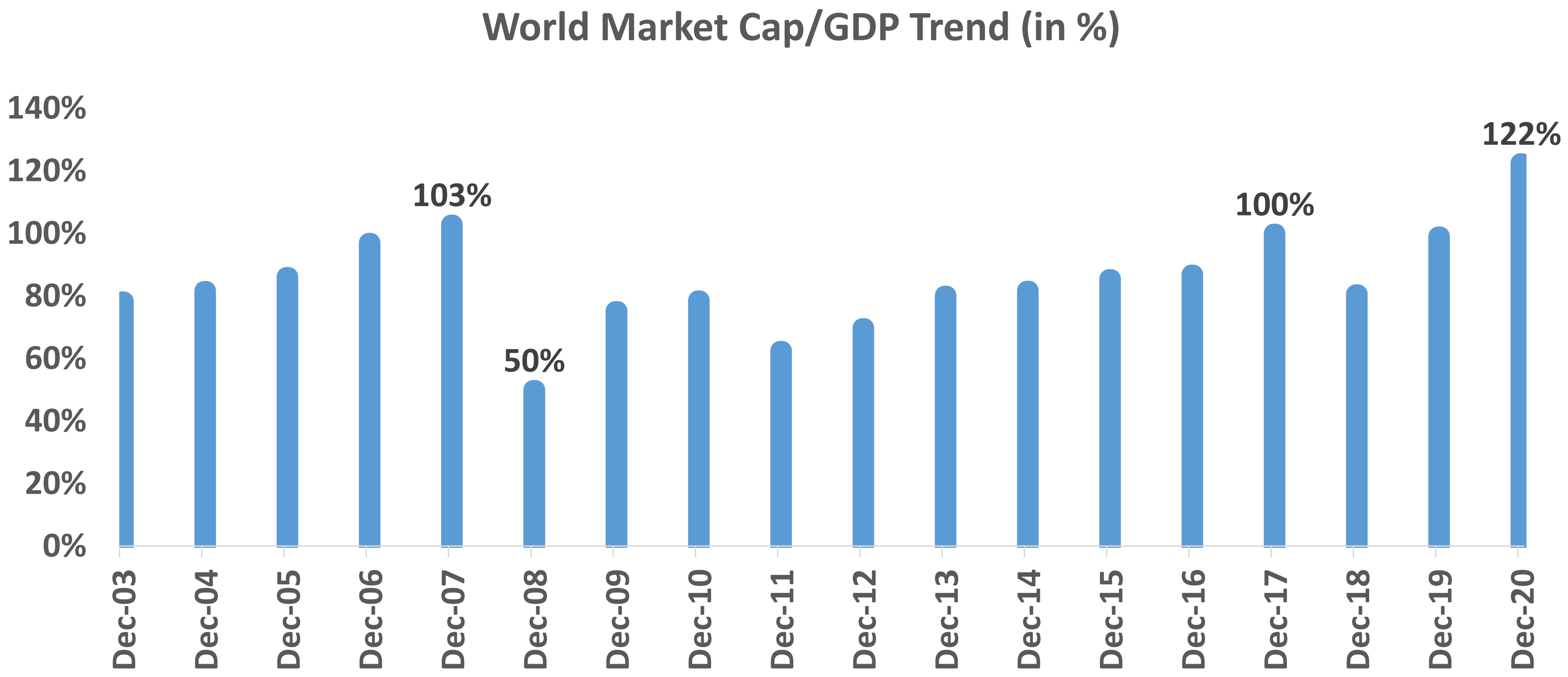
World market cap has crossed US$100 trn for the first time



- Market capitalization of all listed stocks in the world crossed the US$100tn mark for the first time in Dec’2020.
- This is a sharp recovery from Mar’2020 levels---world market cap fell 22% in March, followed by a 50% rise.

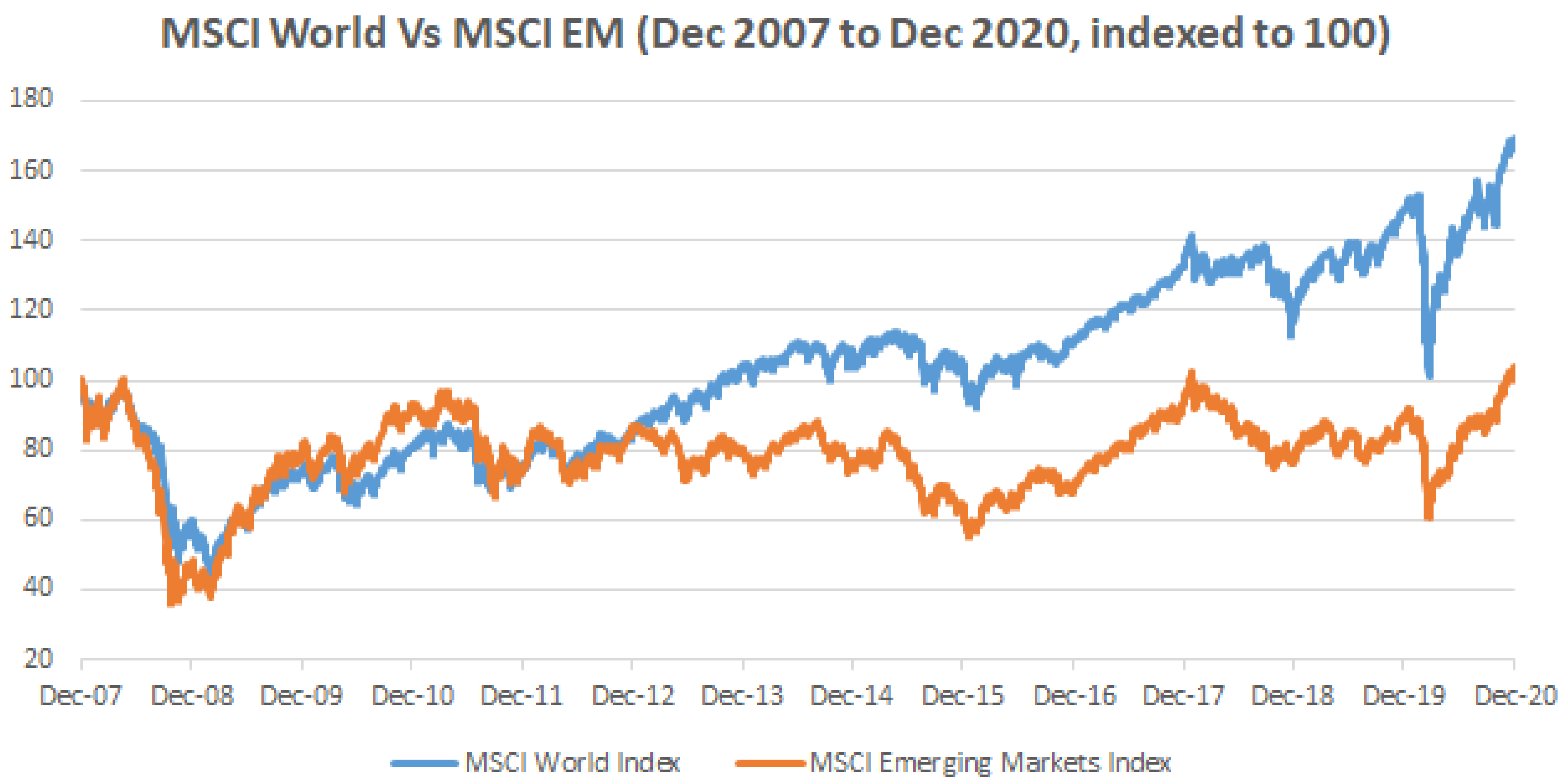
Source: Bloomberg

World market cap to GDP is at its highest level at ~120%, indicating that global market valuations are elevated



Source: Bloomberg
Market Cap is as of year end and GDP is nominal for the Calendar year

MSCI EM index now back to pre-GFC level; significantly underperformed MSCI World



- MSCI Emerging Market index has significantly underperformed MSCI World index (developed markets), primarily dragged down by China.
- Will the large divergence in performance correct to some extent in coming years? Dollar depreciation to help Emerging Markets?

Source: Bloomberg. GFC = Global Financial Crisis of 2008-09

Global crude prices have seen a strong recovery

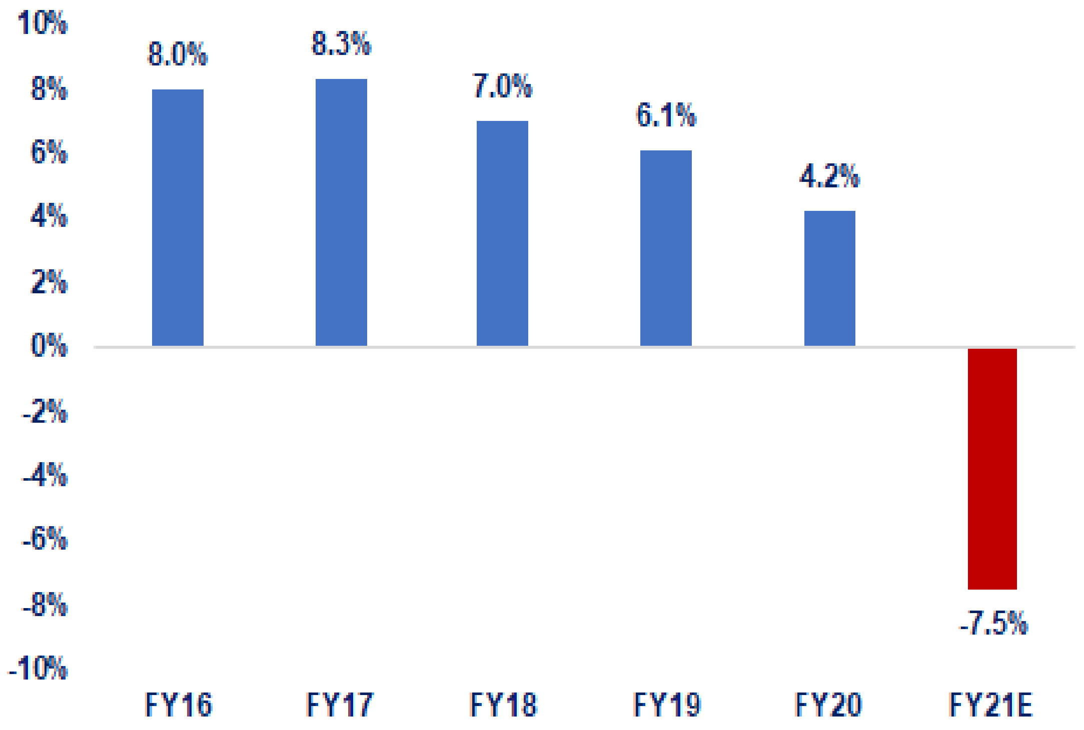
Brent Crude Price Trend in CY2020 (US$ / barrel)

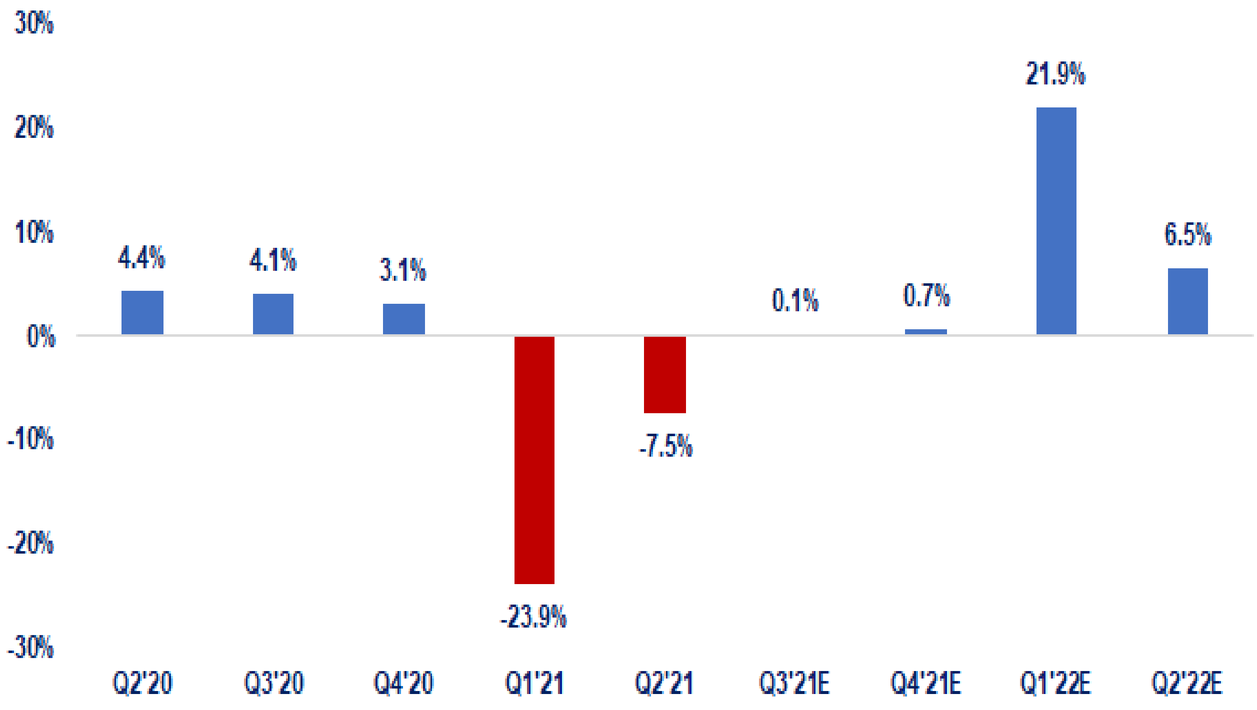
- Crude oil prices have recovered from their lows in April 2020, with economic activity picking up, global risk appetite improving, and on the back of OPEC production cuts

Source: Bloomberg

India's Q3 & Q4 FY21 GDP growth is expected to be positive; strong recovery expected in FY22

India GDP – Trend and Projections (% YoY)





- RBI now project's India's GDP to contract by 7.5%YoY in FY21 vs earlier forecast of 9.5% contraction
- Economists expects GDP to grow by 8.0-9.5% in FY22

- RBI now estimates GDP growth to turn positive in Q3 FY21 vs Q4 FY21 earlier
- Q1 FY22 expected to register strong growth (helped by base effect)

Source: MOSPI, RBI

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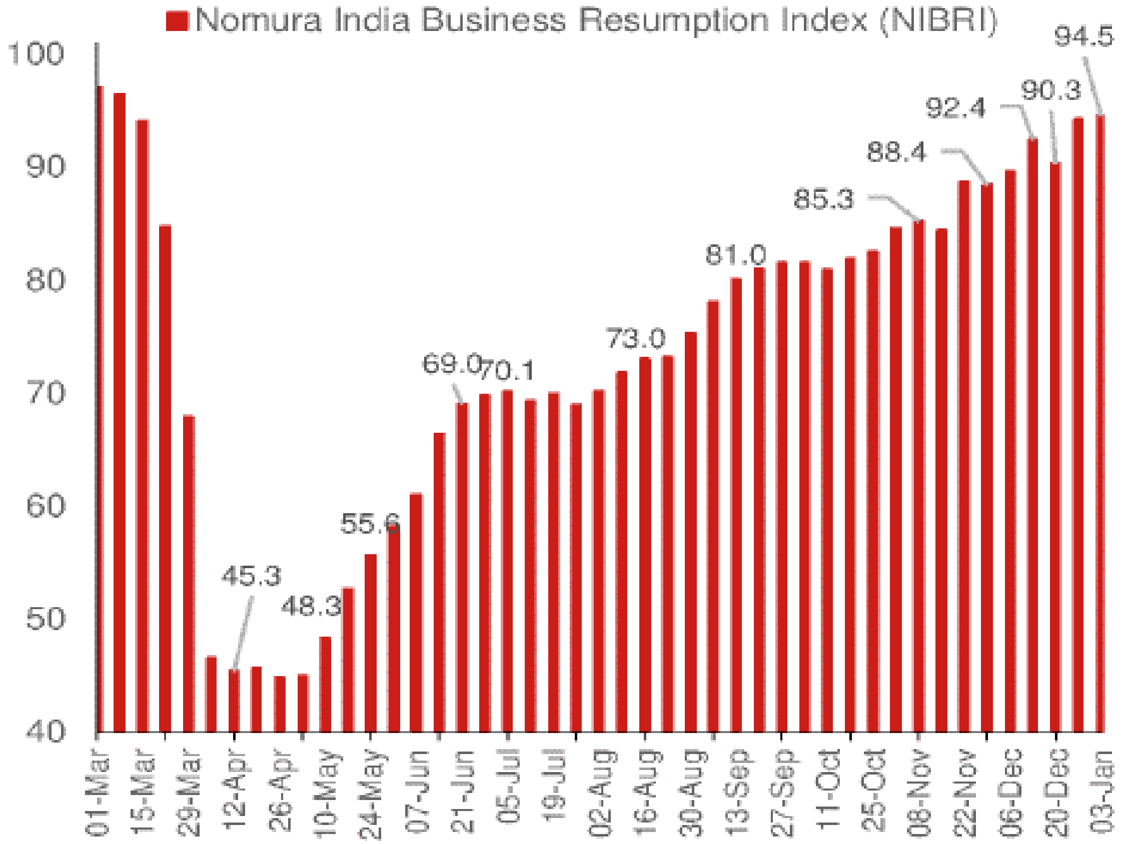
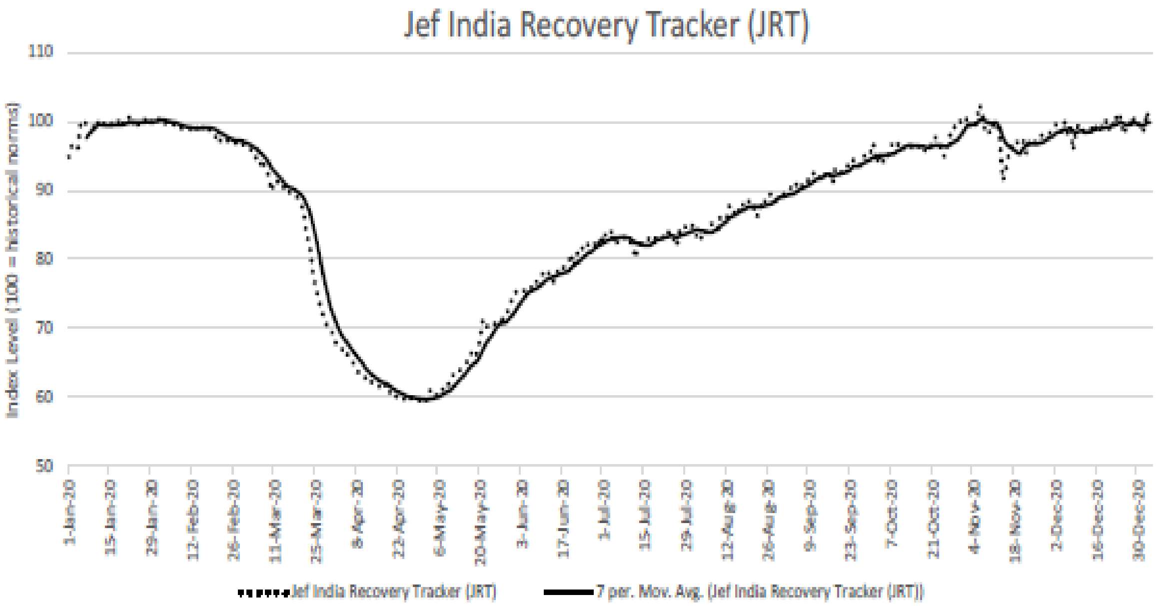
Economic / Business Activity in India back to ~95-100% of Pre-Covid levels

Nomura India Business Resumption Index indicates that economic activity is back to ~95% of Pre-Covid levels



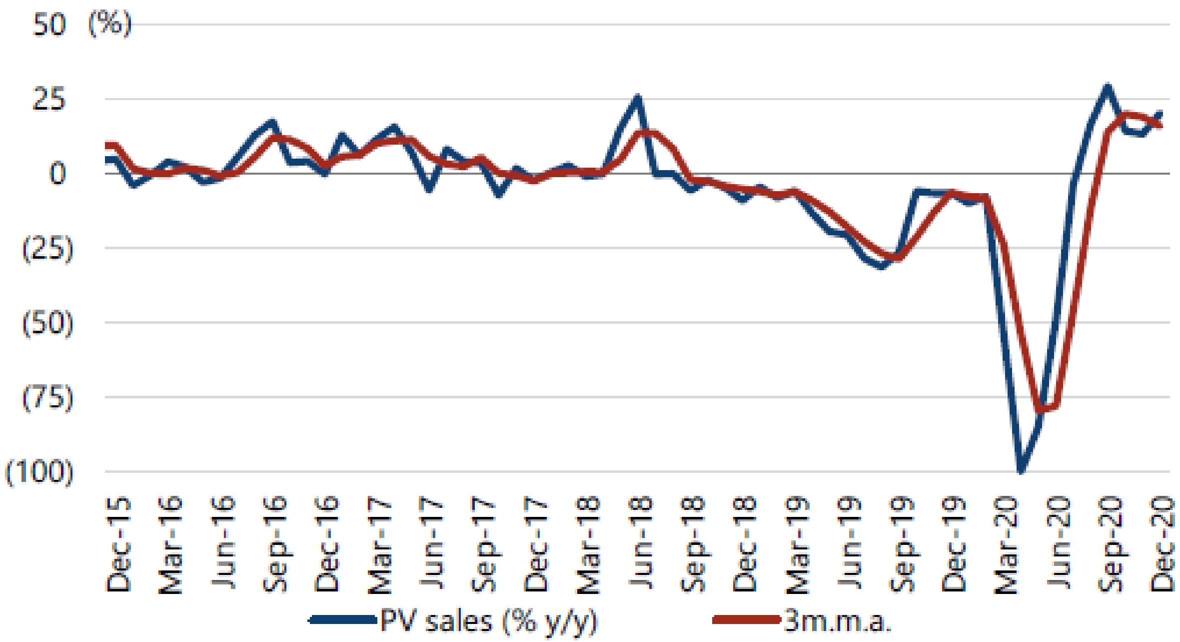
Jefferies India Economic Activity index indicates that overall activity is back to ~100% of Pre-Covid levels



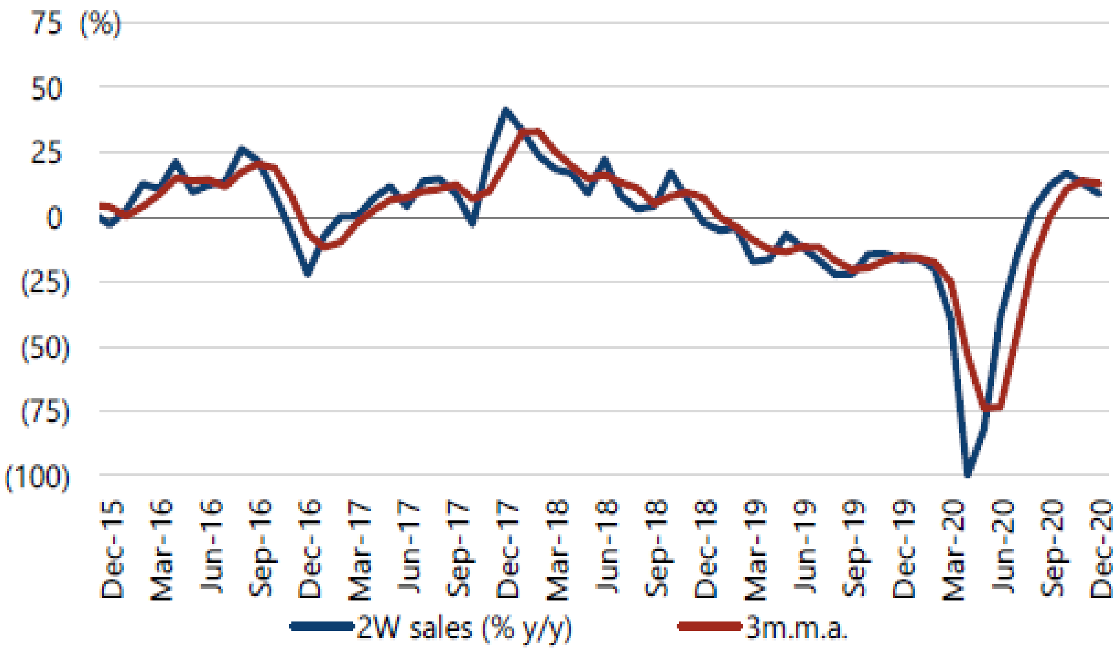
Source: Nomura, Jefferies

High Frequency Indicators like auto sales point to strong recovery – in positive growth territory

Passenger Vehicle Sales (% YoY)



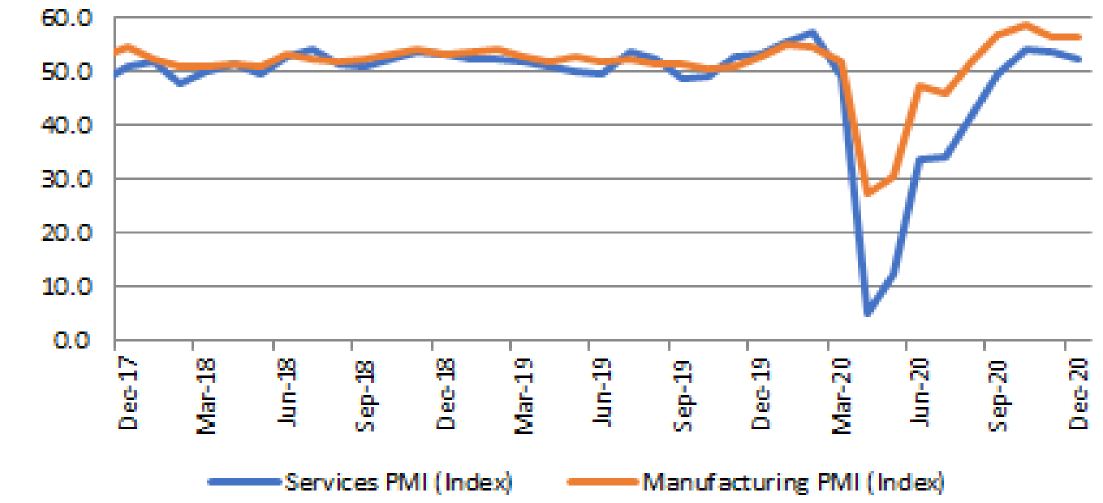
2-Wheeler Sales (% YoY)



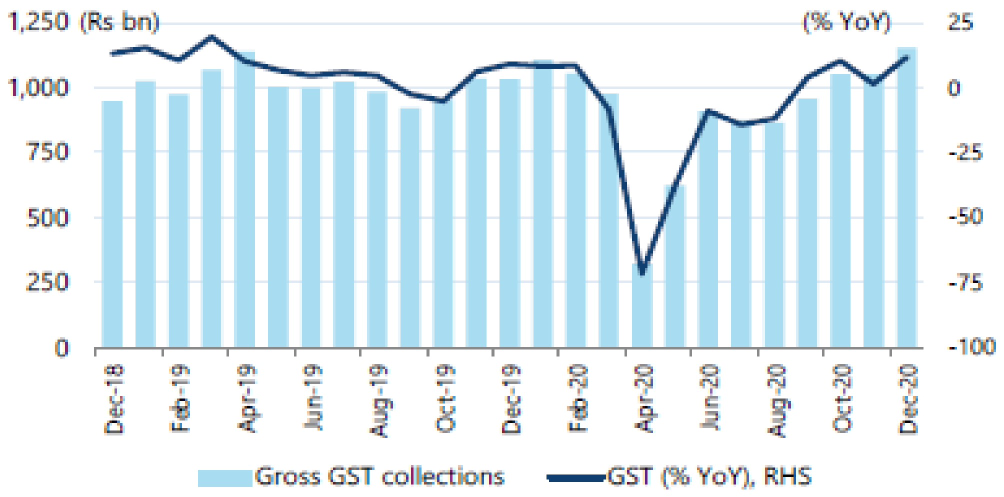
Source: SIAM, Jefferies

Other key indicators also pointing to strong recovery

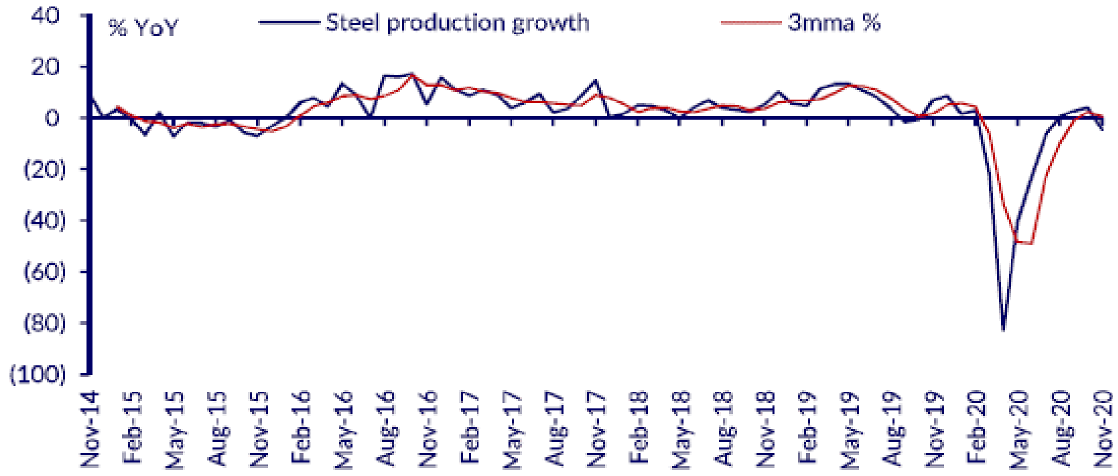
Manufacturing & Services PMI surges into expansion territory



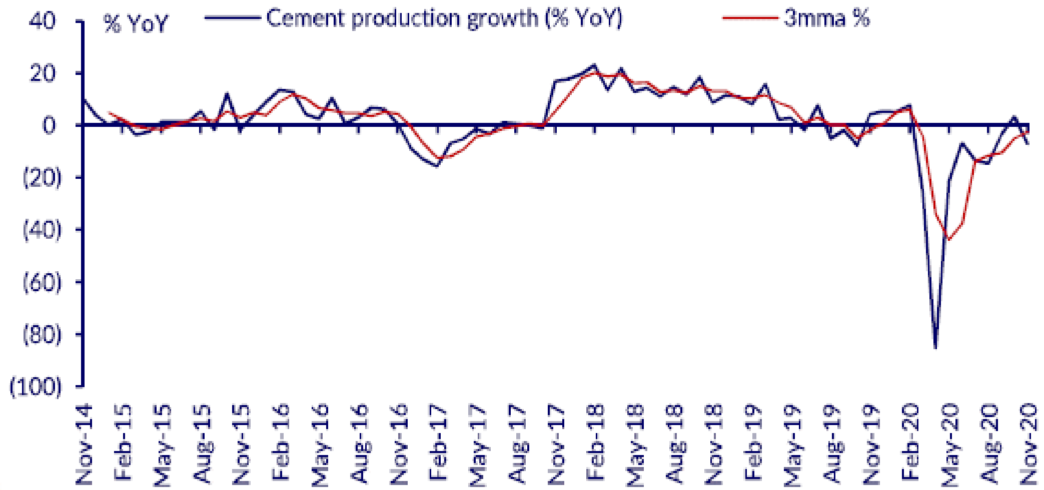
GST collections hit record high in Dec 2020



Steel production has seen healthy recovery



Cement production has also seen healthy recovery



Source: Jefferies, IHS Markit, CLSA

External sector remains strong

India Current Account & Balance of Payment Trend

US $ Billion	FY19	FY20	FY21E
Exports	337	320	277
Imports	518	478	373
Trade Balance	-181	-158	-96
Net invisibles	123	133	122
Current Account Balance	**-58**	**-25**	**26**
CAD % to GDP	-2.1%	-0.9%	1.0%
FDI	31	43	44
FII	-1	1	37
ECB	10	23	-6
NRI Deposits	10	9	10
Others	4	8	-7
Capital Account Balance	**54**	**84**	**78**
Balance of Payment	**-4**	**59**	**104**

Forex Reserves US$ Bln

- Current account expected to be surplus in FY21, if crude price doesn't rise much from current level.
- Balance of Payment (BoP) surplus has led to record annual accretion in forex reserves to all-time highs. BoP expected to be in strong surplus in FY21 helped by robust foreign capital flows.

FPI equity inflows have been robust in FYTD 21; DIIs register outflows

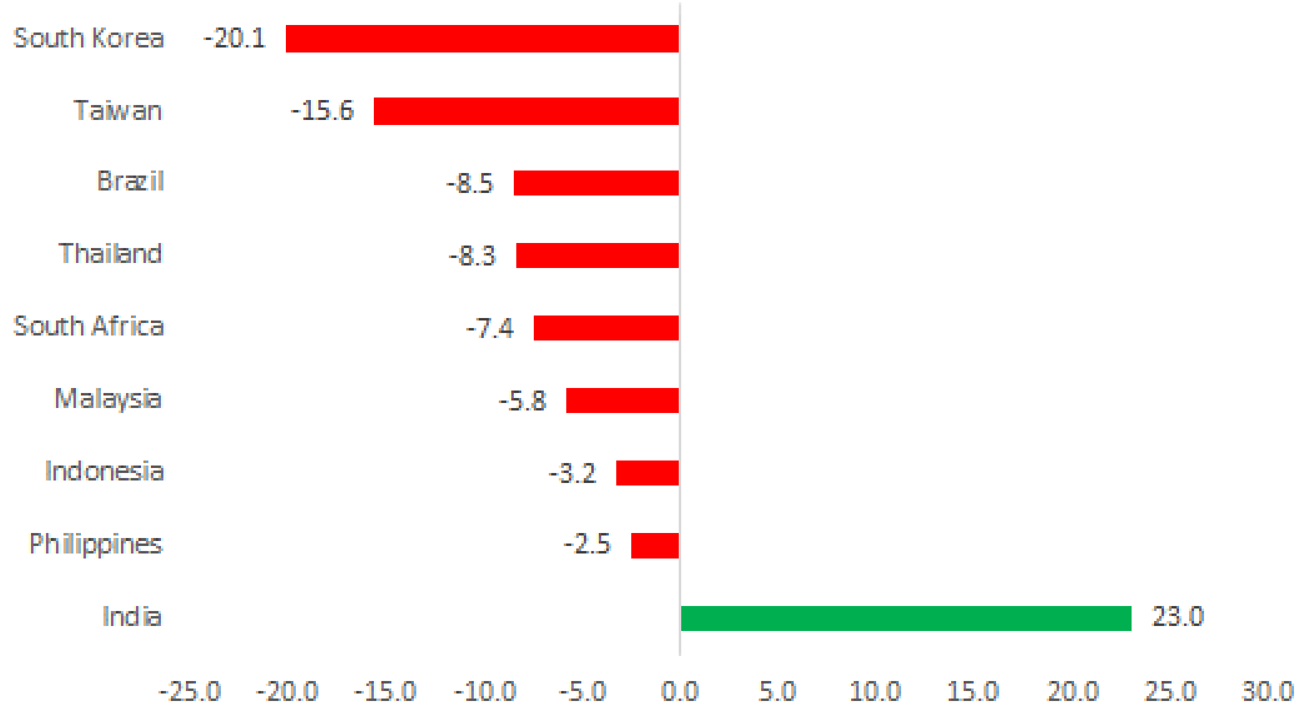
Source: NSDL, Axis Capital	Rs in Crore	
Month-end	**FPIs**	**DIIs**
30 November 2019	22,489	-7,971
31 December 2019	6,118	-741
31 January 2020	14,095	2,250
29 February 2020	-1,521	16,933
31 March 2020	-58,632	55,595
30 April 2020	-4,112	-826
31 May 2020	13,001	11,357
30 June 2020	18,684	2,434
31 July 2020	8,590	-10,008
31 August 2020	45,637	-11,047
30 September 2020	-5,690	110
31 October 2020	18,400	-17,318
30 November 2020	70,896	-48,339
31 December 2020	53,500	-37,294

Source: NSDL, Axis Capital	Rs in Crore	
Year	**FPIs**	**DIIs**
FY2008	52,572	47,794
FY2009	-48,250	60,040
FY2010	1,10,752	24,211
FY2011	1,10,121	-18,709
FY2012	43,738	-5,347
FY2013	1,40,032	-69,069
FY2014	79,709	-54,161
FY2015	1,11,445	-21,446
FY2016	-14,171	80,416
FY2017	60,196	30,787
FY2018	21,074	1,13,258
FY2019	-90	72,115
FY2020	6,151	1,29,301
FYTD2021 (upto December)	2,18,906	-1,10,931

- FPI equity flows surge on the back of strong global liquidity. Nov 2020 registered record high FPI flow & flow remained strong in Dec 2020.
- However, DIIs have seen outflows. Nov 2020 registered record high DII outflow & outflows continued in Dec 2020.

India was among the only emerging markets to register strong FPI equity inflows in CY20

Country-wise FPI equity flows in CY 2020 (US$ in billion)

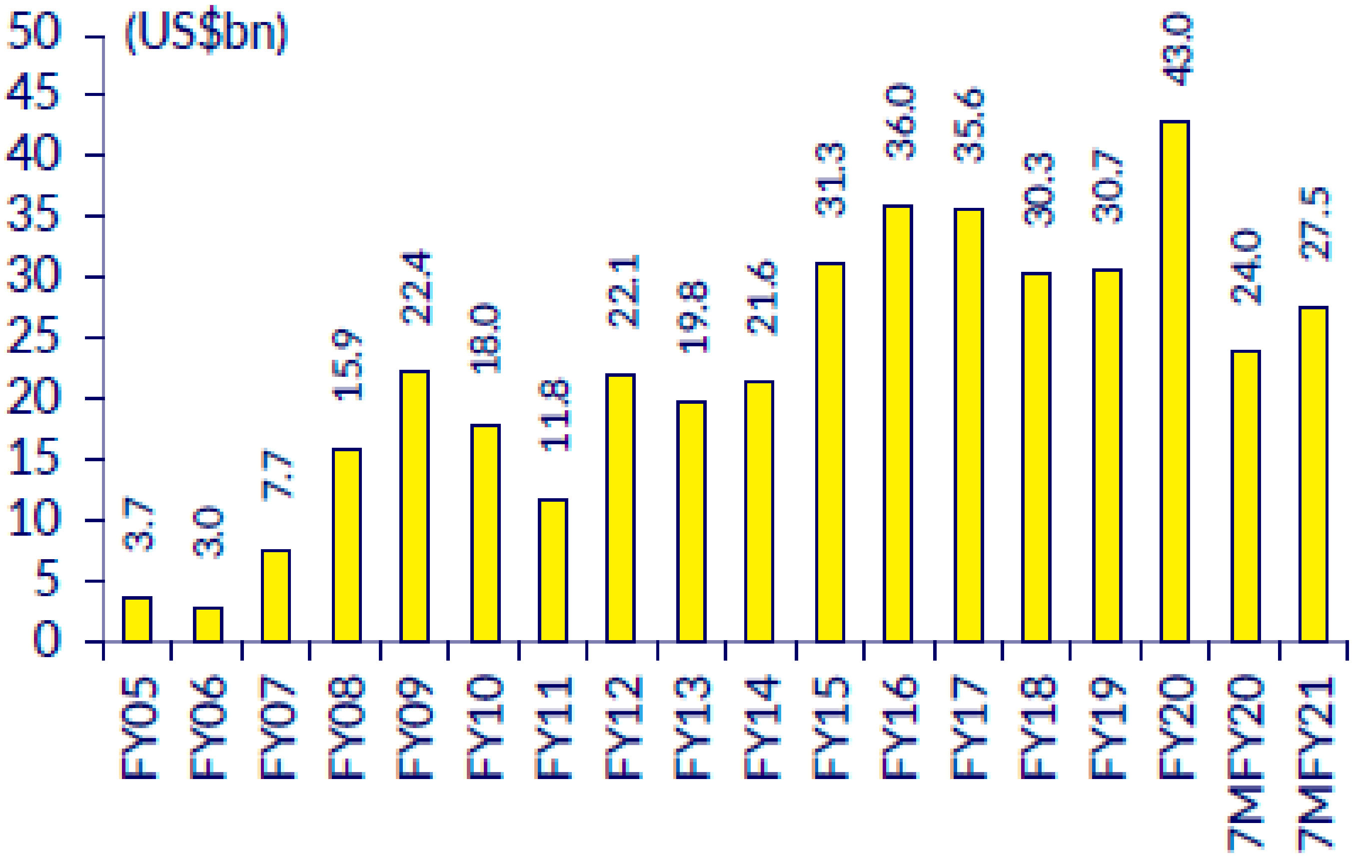


- India registered one of the strongest calendar-year wise FPI equity inflows in 2020 (CY10 saw highest FPI equity inflow of $29 billion)
- Most other peer emerging and Asian markets registered FPI equity outflow in CY20

Source: Bloomberg, CLSA

India FDI inflows were strong – helped by big stake sales by Reliance Industries

India FDI flow trend – Fiscal Year-wise (US$ in billion)



Source: Ministry of Commerce, CLSA

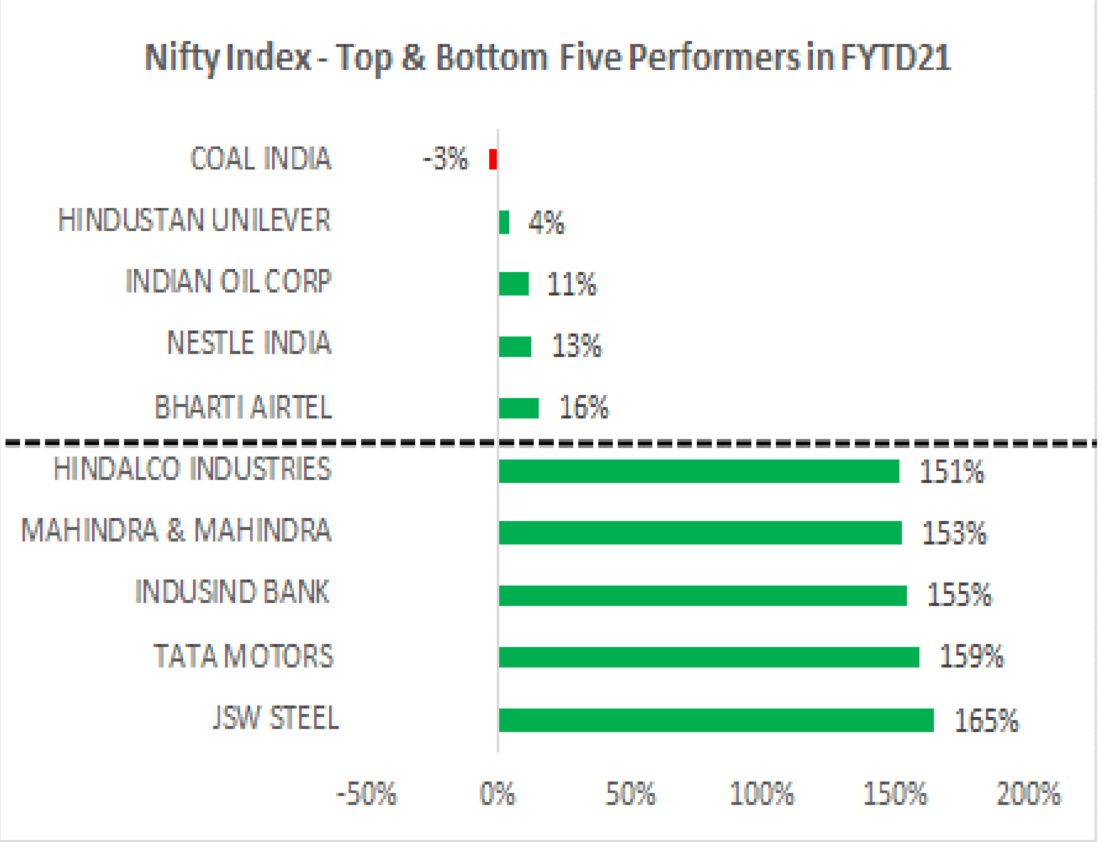
Market rally has become broad-based

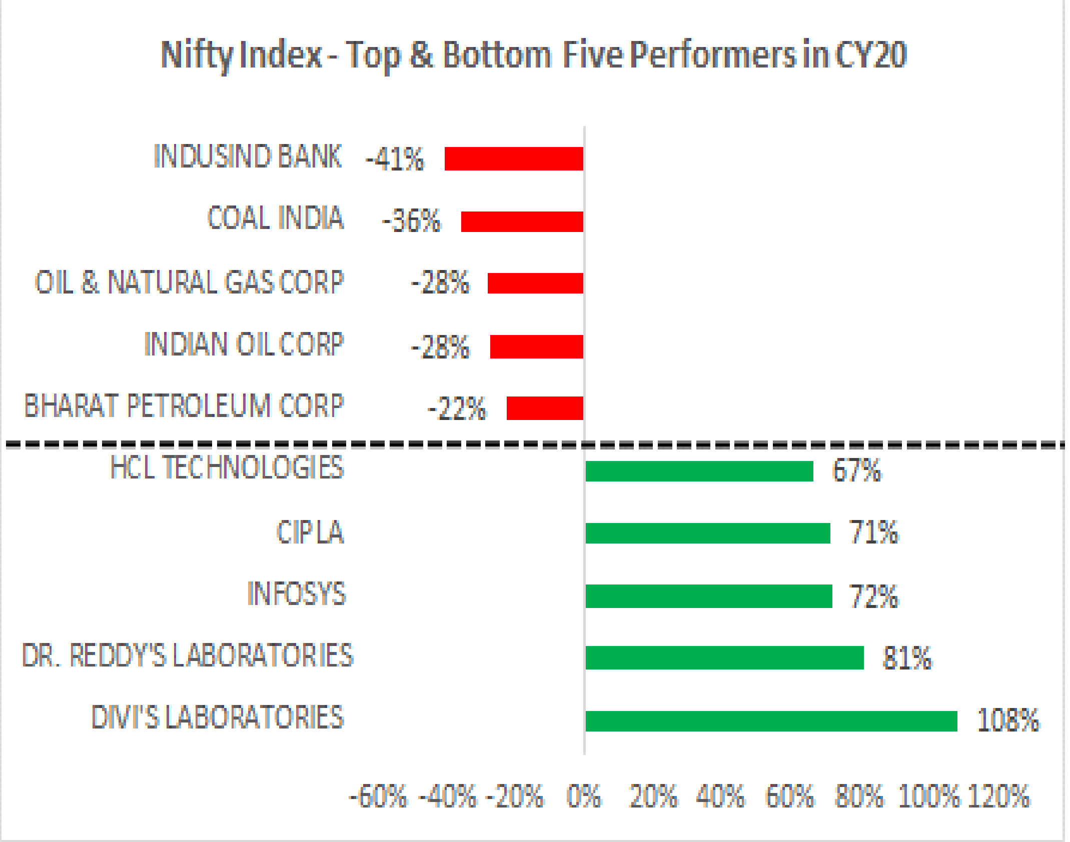
Performance of Domestic Indices as of Dec 2020 (in %)		
Index Name	FYTD 21	1 year
S&P BSE Metal	103.0	11.2
IISL NIFTY Smallcap 100	97.2	21.5
S&P BSE Auto	93.7	12.6
S&P BSE IT	88.8	56.7
IISL Nifty Midcap 50	84.6	24.9
S&P BSE Realty	83.1	8.7
S&P BSE Healthcare	78.5	61.4
S&P BSE Capital Goods	70.7	10.6
IISL Nifty 500	64.6	16.7
S&P BSE BANKEX	62.8	-2.1
IISL Nifty 50	62.6	14.9
S&P BSE Consumer Durables	57.0	21.5
S&P BSE Power	49.7	7.1
S&P BSE Oil and Gas	40.6	-4.4
S&P BSE PSU	29.6	-16.9
S&P BSE FMCG	23.0	10.5

Source: Morningstar Direct. Data sorted in descending order on the basis of FYTD 21 return

- **Equity markets rallied strongly during FYTD21 (April – Dec 2020)**
  - ➢ Due to strong FII inflows, positive vaccine news, healthy corporate earnings and strong recovery in economic activity
  - ➢ Mid/Small-caps outperformed, making the rally more broad-based
  - ➢ Sectors like metals, IT auto, realty and healthcare outperformed
  - ➢ Sectors like PSU, FMCG, oil & gas underperformed
  - ➢ Cyclical sectors trying to play catch-up
- **For CY20 too, equity markets closed with healthy gains. IT, pharma & broader markets (small/mid-caps) outperformed**

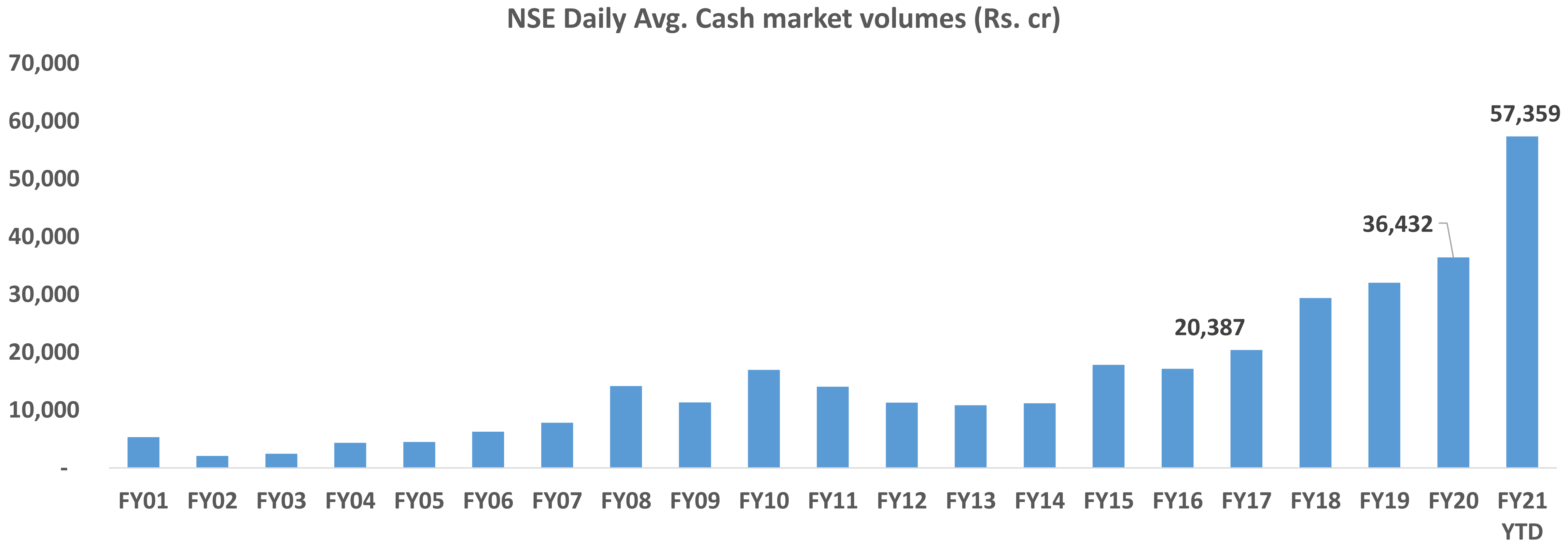
Top & Bottom Five Performers of Nifty index in CY 2020 & FYTD 21





Source: Bloomberg. FYTD-21 = April 2020 to Dec 2020. Past performance is not an indicator of future performance.

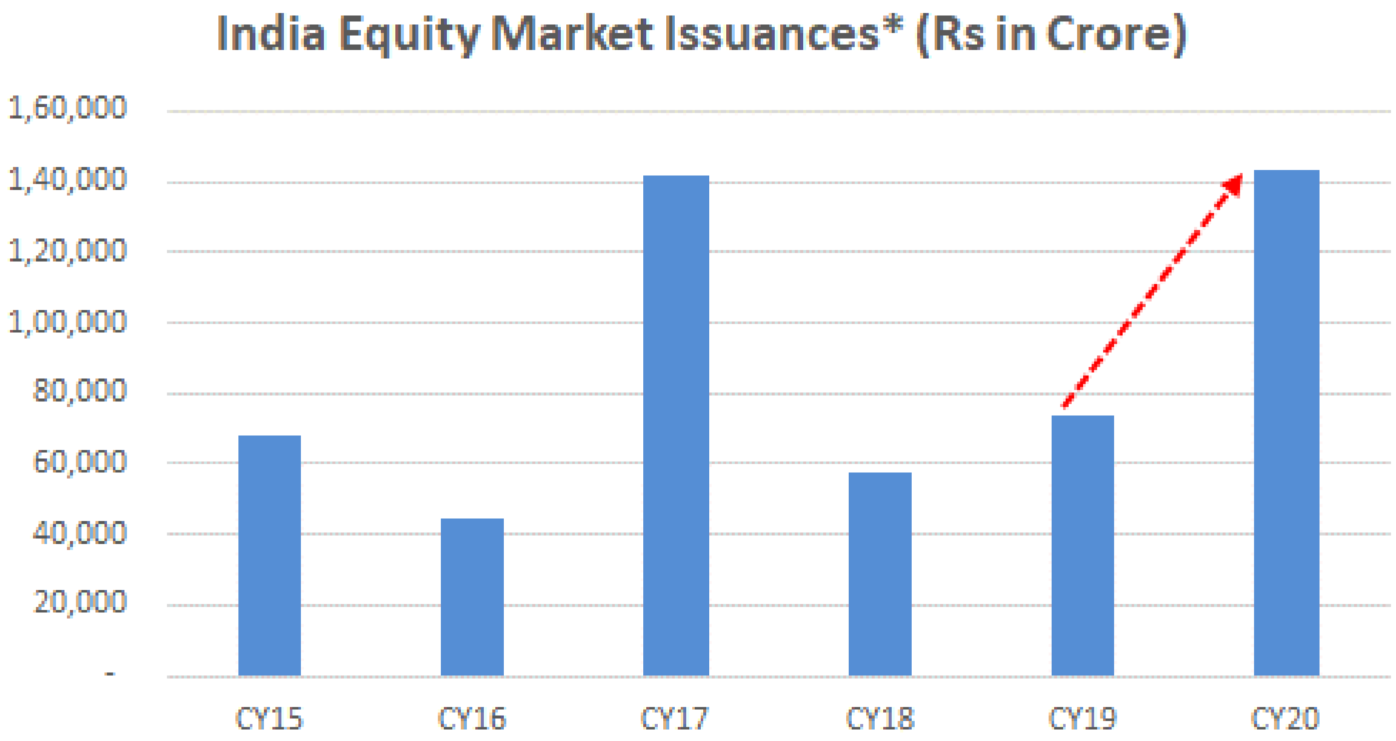
Equity market activity has been buoyant – Cash volumes up significantly



- Equity market activity has been buoyant with NSE's FY21 daily volume averaging ~57,000cr v/s ~36,000cr in FY20 (up 57%).
- Retail participation in equity markets has moved up to ~65% levels in FY21 v/s ~42% two years ago. Sharp addition of 8 mln demat accounts in FYTD21 (upto Nov)– around 50% YoY growth.

Source: NSE, MOFSL

Equity market issuances have picked up significantly in 2020; comparable to 2017

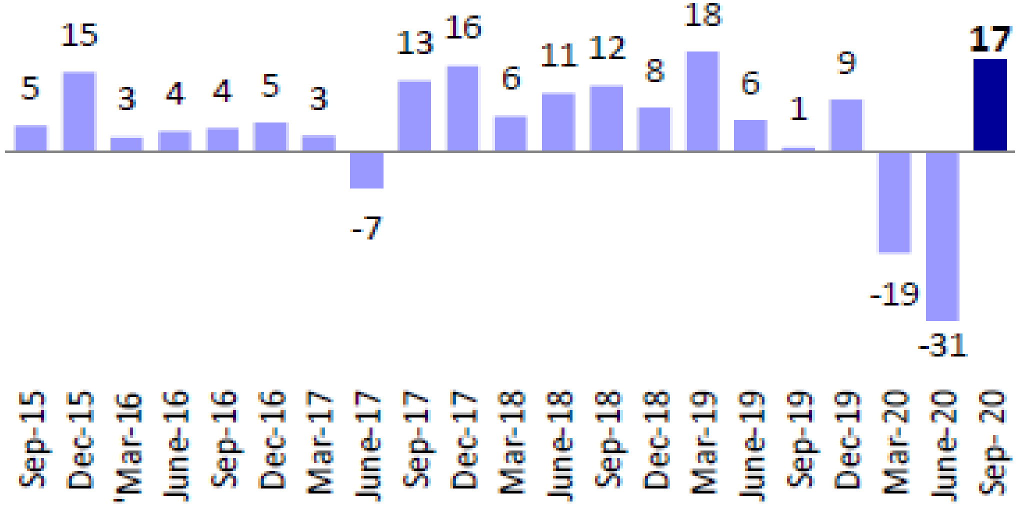


- With buoyancy in equity markets, equity market issuances have picked up, and the trend could continue (if market conditions remain favourable)
- Some of the recent IPOs have seen massive over-subscription and a robust listing gain, indicating that appetite remains strong

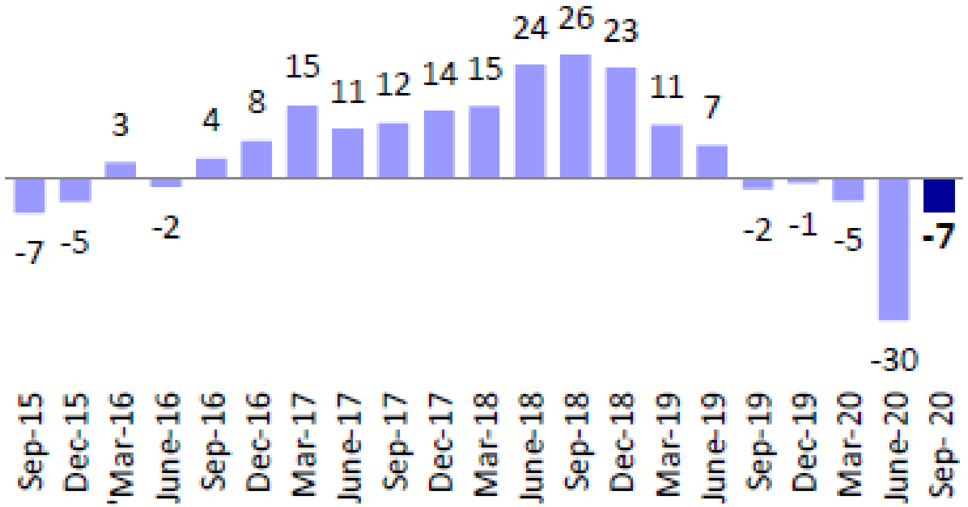
Source: Prime Database, Kotak Institutional Equities. * Equity Market issuances includes IPO, FPO, QIP & OFS

Q2 FY21 earnings have come in better than expected, helped by cost control

Nifty Q2 FY21 PAT growth (%YoY) strong vs expectation of decline



Nifty Q2 FY21 Sales decline (%YoY), in-line

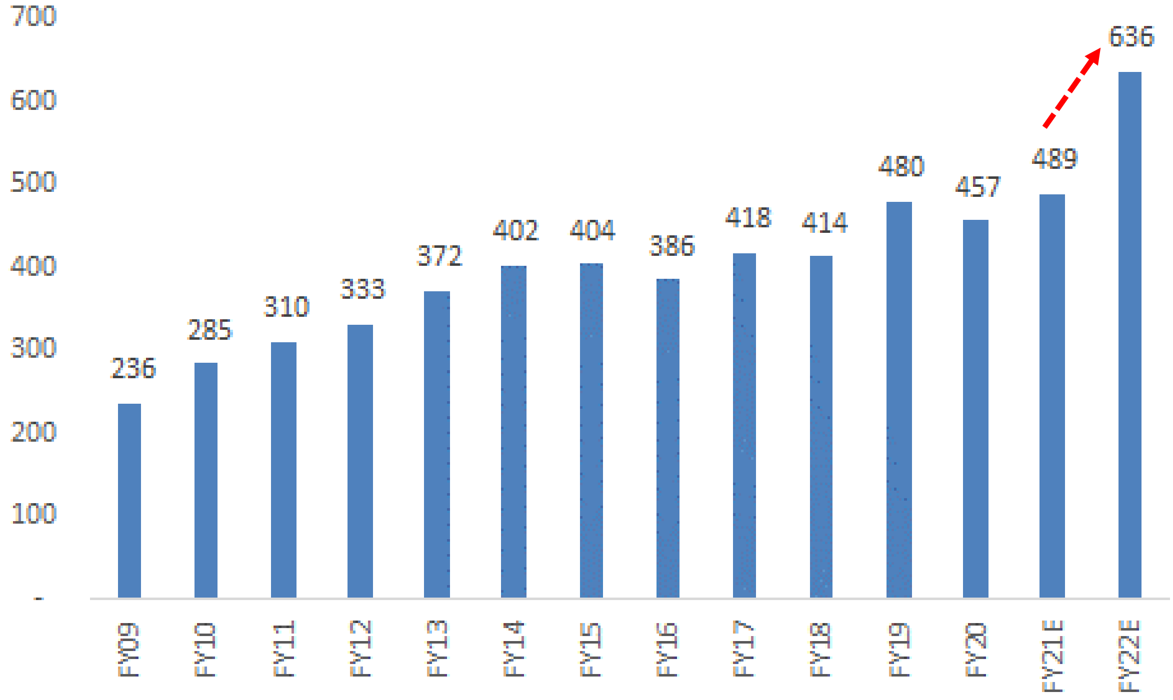


- Nifty Q2 FY21 earnings were quite strong, helped by cost control. As a result we have seen earnings getting upgraded.
- Earnings expected to continue to recover through FY21 (~7% growth during the year), and pick up strongly by ~30% in FY22.

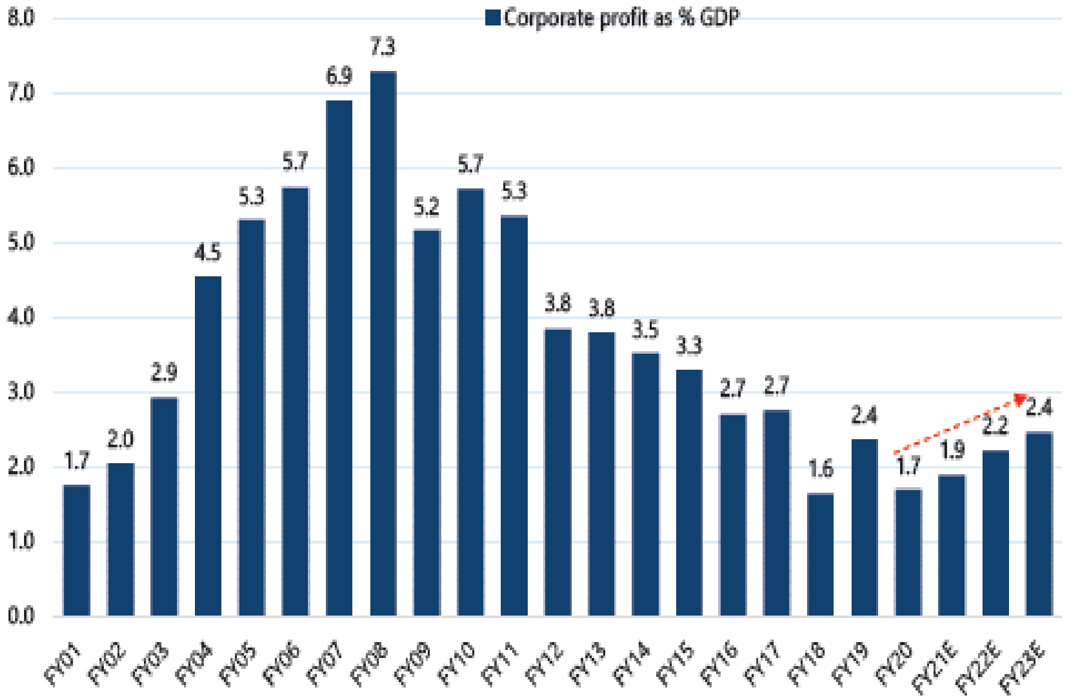
Source: Motilal Oswal

Earnings expected to recover in FY22; Corporate profit to GDP may have bottomed out

Nifty EPS Trend



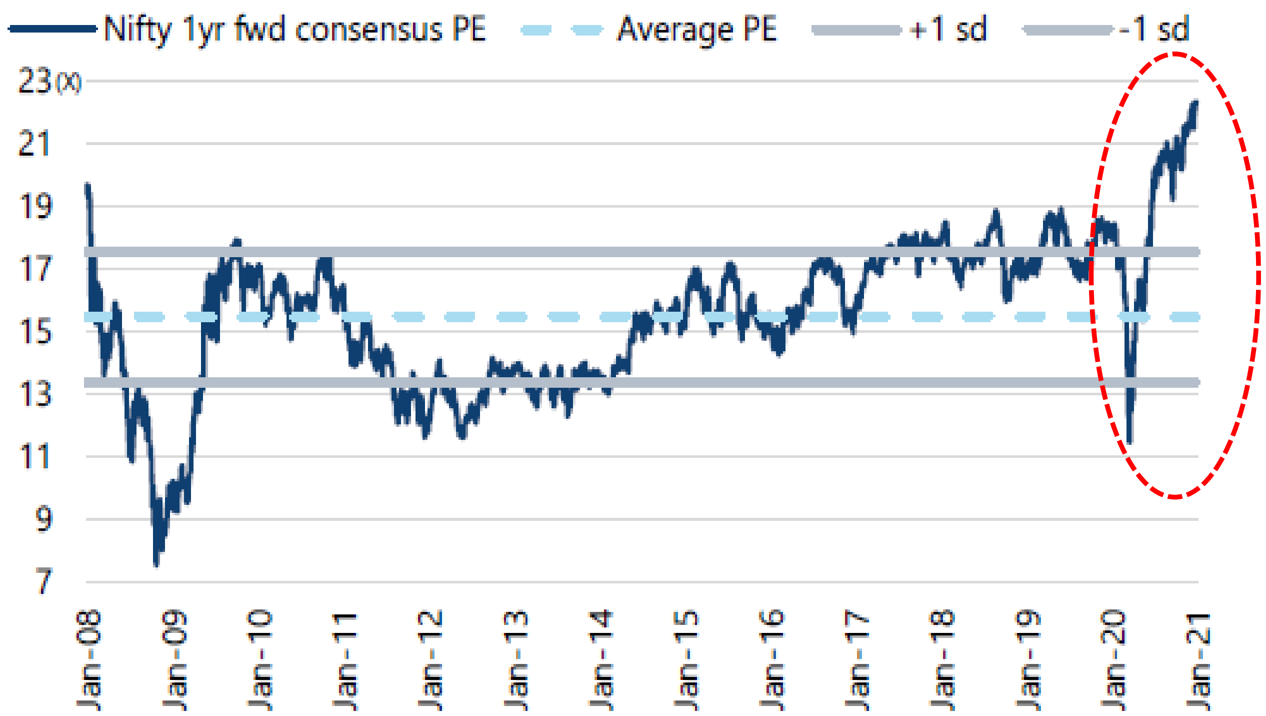
Corporate Profit to GDP expected to recover in coming years



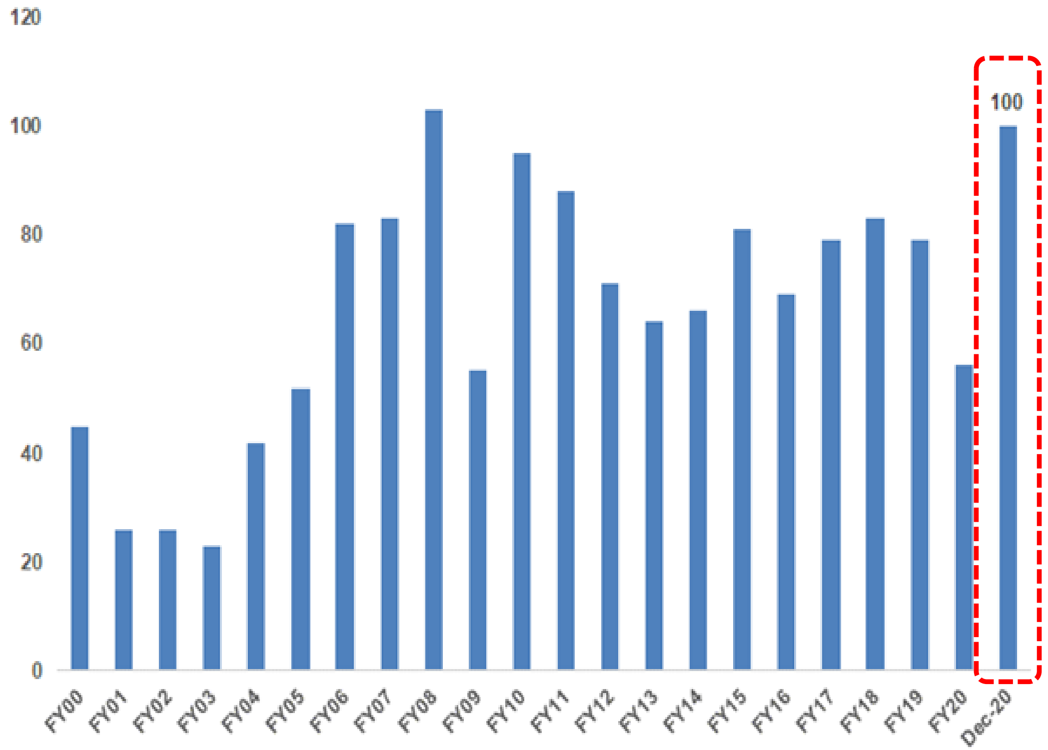
Source: Bloomberg, Jefferies, IIFL Research

Valuations are quite elevated; Market cap to GDP near its peak

Nifty Forward P/E Ratio at peak levels

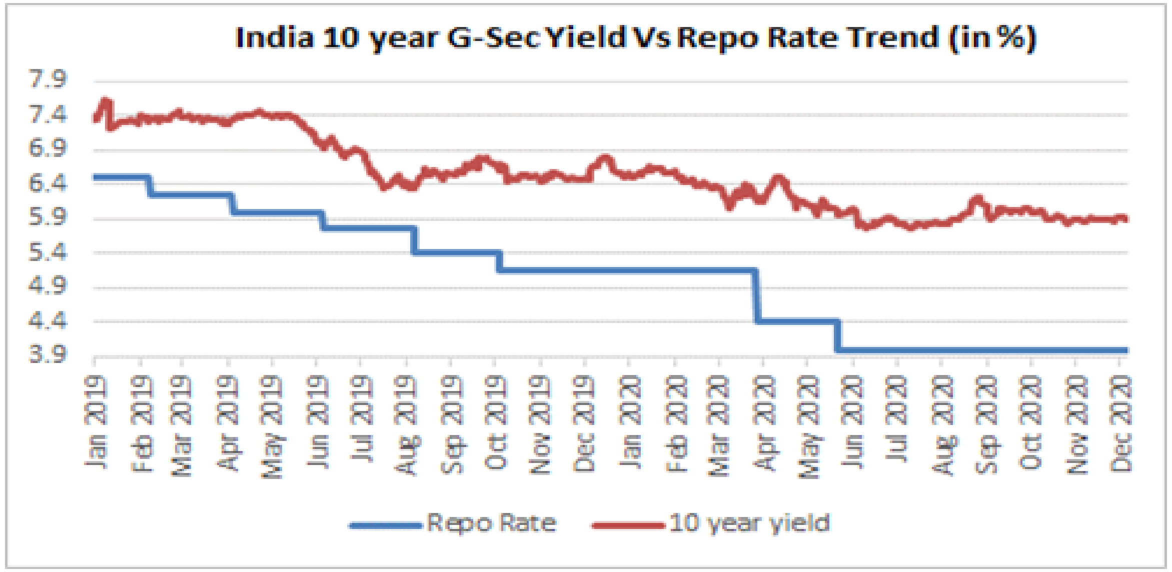


India Market Cap to GDP Trend (in %)

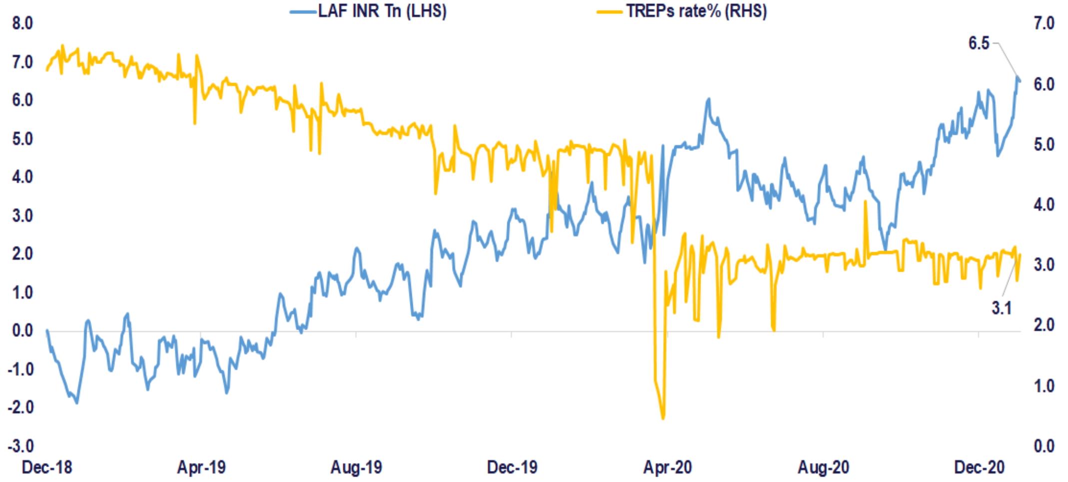


Source: Bloomberg, Jefferies, Motilal Oswal

Domestic liquidity is ample - RBI's focus has been on growth



Net Liquidity in the system (Rs trillion)

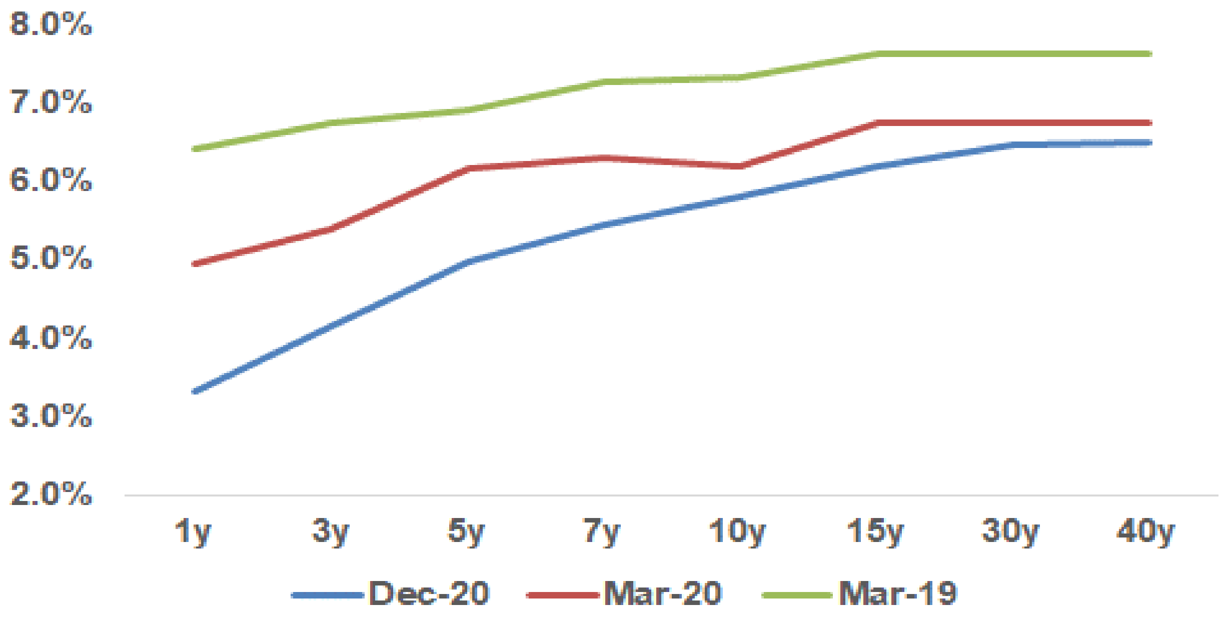


- RBI had cut policy rates earlier by 115 bps responding to the pandemic, but has left rates unchanged post May 2020.
    - Dovish undertone continues in Dec 2020 policy
    - Accommodative stance till next fiscal year
    - Growth over inflation
- CPI inflation has been elevated and above RBI's 6% upper limit for a while, primarily due to supply disruptions
    - Oct'20 at 7.6% and Nov'20 at 6.9%
    - RBI expects inflation to moderate to 4.6% by Sep 2021.
- Liquidity remains high at Rs 5-6 trn
- With inflation being elevated, minimal space for more rate cuts, and further monetary action will be dependent on inflation trajectory.
- We prefer medium term part of yield curve

Source: Bloomberg

India Yield Curve and Spread

India G-Sec Yield Curve

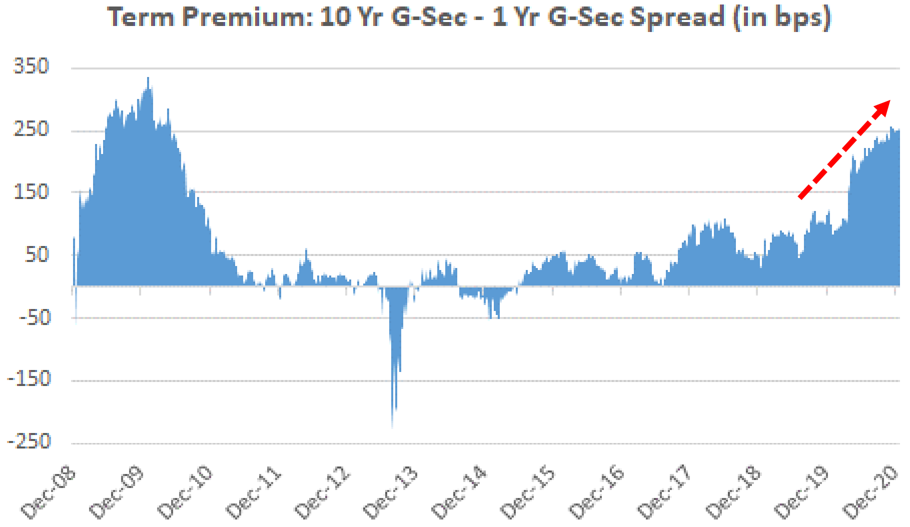


- Shorter end of yield curve (short term yields) has come down much more than the rest of the yield curve (esp. long term yields)
- Corporate bond spreads have come down, indicating reduction in risk aversion

AAA Spread (over G-Sec) %

AAA Spreads	5yr	10yr
Dec-20	0.3%	0.7%
Mar-20	0.4%	0.9%
Mar-19	0.8%	0.8%
Oct-18	1.0%	0.7%

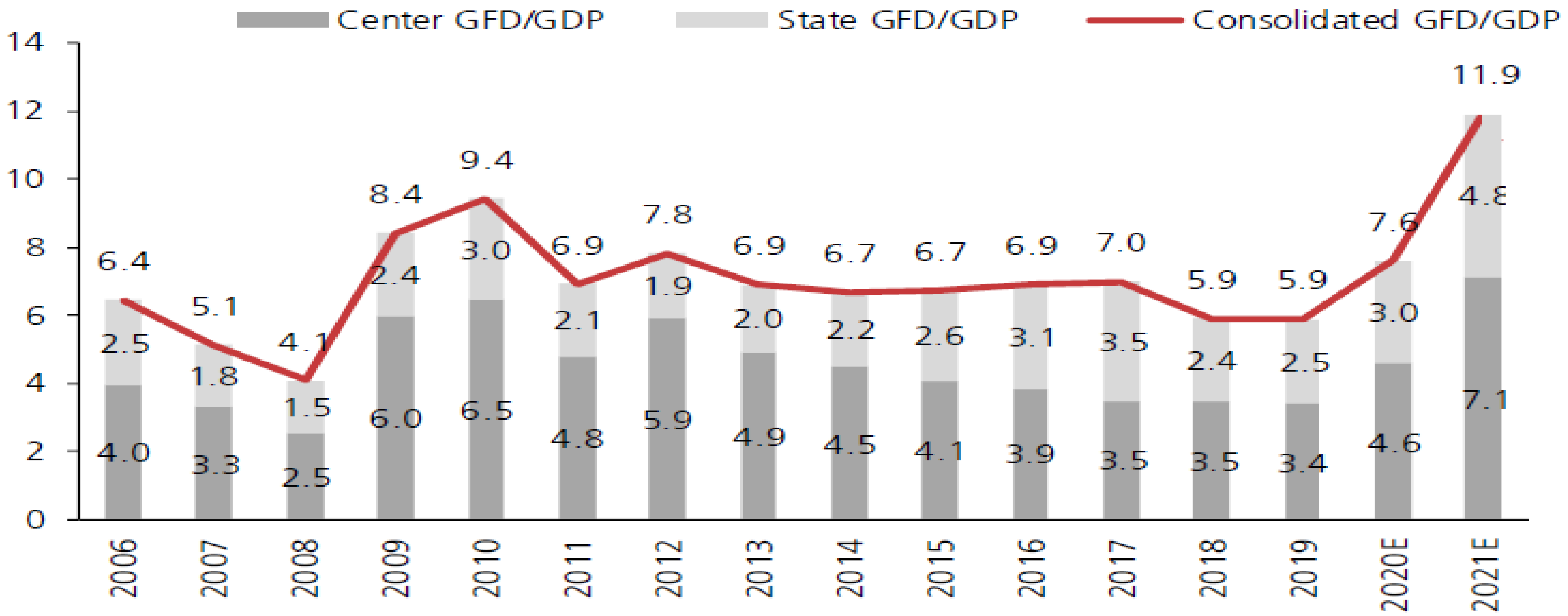
Term Premium has increased significantly



Source: FBIL, Bloomberg

While fiscal remains a worry, it can wait due to growth concerns

Fiscal deficit to balloon in FY21



- Center’s gross borrowing up from Rs 7.8 trln to Rs 13.1 trln for FY21. Borrowing calendar for H2 FY21 revised to Rs 5.4 trln
- State’s allowed to increase their fiscal deficit from 3% to 5% of GDP subject to conditions.
- Consolidated fiscal deficit (both centre & states) could rise to 11-12% of GDP in FY21

Source: Kotak Institutional Equities

Market Outlook for 2021

With launch of Covid vaccines, the worst is behind us; Economies to normalize & pick-up	• Even though global Covid cases are escalating (esp. in US), with the launch of Covid vaccines—the worst seems to be behind us. The big theme in 2021 will be vaccine administration drive. • 2021 will be the year of economic normalization & healthy recovery in economic growth.
Global liquidity surge helps to boosts markets	• The global liquidity surge helps markets to recover strongly—with some touching all-time highs. • The easy global liquidity scenario/monetary policy stance expected to continue for a while—to help in economic recovery
Market valuations are elevated; Corporate Earnings expected to recover strongly in FY22	• Market valuations are elevated, with Nifty index trading at ~22X FY22 EPS. • Corporate earnings to see strong recovery, with Nifty EPS growth expected to grow ~30% in FY22
Investment Strategy	• At this juncture, investors should systematically invest in equities, or use an asset allocation approach (based on their risk profile).
Debt Markets & Strategy	• Limited space available for further rate cuts, and dependent on future inflation trajectory • We prefer medium term part of the G-Sec yield curve.
Factors to watch out for	• Global monetary policy stance, upcoming India Union Budget (Feb 2021), movement of Dollar index (as it can impact EM flows), geo-political tensions, clarity on policy changes under new US govt, and progress of administration & efficacy of Covid vaccine

THANK YOU

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