



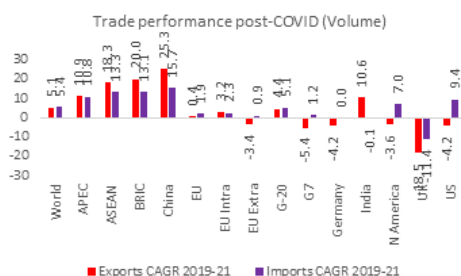
TM

India Economics and Strategy

30 September 2022

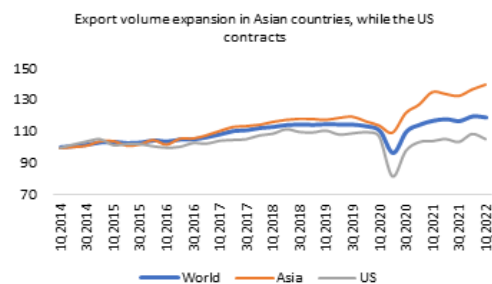
INDIA ECONOMICS

The global bounty



Source WTO, Systematix Research

Disproportionate gains to Asia from post-pandemic stimulus in AEs



Source WTO, Systematix Research

Please see our portfolio views and list on page 8 & 9

Receding global bounties to hurt India's consumption and cap goods

We examine the implications of global tightening and economic slowdown on India's consumption and employment revival, as also the capital goods sector that is highly dependent on exports of engineering goods.

Rising dependence on global impulses: External trade has risen to 50% of GDP (1QFY23), highlighting its significance in India's outlook amidst contracting exports, which is down 24% from Mar'22. Widening trade deficit, slowing global impulses and tightening financial conditions due to declining forex reserves, rising interest rates and weakening INR can blunt the revival in domestic consumption.

Pervasive global economic slowdown: Aug'22 PMIs indicate that the global economy is sliding into contraction, particularly in advanced economies (AEs). Chinese manufacturing is in contraction and India remains strong; we expect the slowdown to widen. Most institutions now project global growth at 2.5-3% in 2022 and to decelerate further to 2.0-2.5% in 2023. As a result, WTO's world trade volume growth projection can be scaled down significantly from 3% for 2022 and 3.4% for 2023 (Apr'22) to below our estimated structural trend of 1.7% and 5.2% CAGR during 2019-22, respectively. This could have a significant impact on India and China outlook. Thus, our FY23E real GDP projection of 5.0-5.5% is lesser than RBI's 7.2%.

Episodic gains to India, China from post-pandemic AEs stimulus are reversing: The colossal rise in stimulus-led demand in AEs resulted in export volumes contracting for G7 countries (-5.4%, 2019-21, UK -4.2% and US -18.5% CAGR over 2019-21). It also triggered a significant surge in global export volume growth (5.1%), particularly for China (25%) and India (11%). India's export-led sectors, particularly metals, textiles, readymade garments, chemicals, machinery, auto parts, gained from higher commodity prices, rising orderbook, booming cash flows and rise in market capitalisation. Thus, with AE on a tightening mode now, the bounties for these sectors are dissipating, as they face erosions in both volume and price realisation.

Indian cap goods exports gain in the US markets, will it sustain?: Indian capital goods sector gained from export demand in the US. But with the cyclical downturn imminent in major economies, orderbooks of export-oriented machine exporters could also face risk, which have been robust thus far. New orders for machinery in the US is now contracting in real terms (-7.5% in Jul'22). While the projects under implementation in India have risen since 2019 (up 9.5%), in real terms, it has contracted by 25%. Hence, as global commodity prices correct, the value of orderbook for capital goods companies, both exports and domestic led, could also contract. Thus, operating matrix and valuations of the machinery industry are extremely sensitive to the economic slowdown in AEs, correction in commodity prices and dollar strength.

Consumption is the mainstay for India, but risks are emerging: India's consumption revival has resulted from the impact of a) an unwinding pent-up demand, b) rebound in corporate sales, reflecting the surge in global commodity prices and exports translating into improved compensation, c) leverage on spending, d) drawdown in household savings, f) fiscal support and g) patchy employment recovery. For consumption momentum to sustain, corporate cash flow gains should translate into wider employment creation. But the global spill overs are turning adverse much before a full recovery, making policy choice for RBI and the government tricky; this could end up translating into a sub-par growth trajectory.

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Post pandemic bounce in exports waning

Declining external trade, fiscal support, and lackluster private capex intensifies dependence on India's consumption: The deceleration in India's exports to 1.6% YoY at USD 33.8bn (Aug'22) and 24% contraction from the Mar'22 peak marks the fading of the post pandemic positive global trade cycle (Exhibit 3).

Importantly, exports of engineering goods, including metals, machinery & other products, comprising 30% of non-oil exports, have declined by 25% at USD 7.8bn from its peak in 2022, across Asia (-29%), Europe (-34%) and the US (-23%); these cumulatively contribute 70% of total engineering goods exports (Exhibit 5).

This is a significant shift, as global trade rebound, fueled by large stimulus in advanced economies, was the most significant contributor for India's recovery to 8.7% real GDP growth in FY22 from the COVID shock. Global trade (imports + exports of goods and services) continues to be a major contributor to nominal GDP, rising to 50% of total in 1QFY23.

Dissipating fiscal support (real government consumption spending declining 10.4% QoQ SA in 1QFY23) has also increased the dependence of India's growth on domestic consumption (61% of GDP), as private capex remains feeble (imports/exports of machinery has declined to a 25-year low of 126% in FY23E). Decline in exports and continued expansion in imports (USD 62bn in Aug'22, 37% YoY and -9% from Jun'22 peak) has expanded the trade deficit to USD 29bn, reflecting the strength in domestic consumption demand.

Anecdotal evidence of Indian manufacturing facing lower export demand: Media reports show that key sectors such as textile, machinery, plastic, gems & jewelry are facing weakening of in export orders, resulting in scaling down of operations (see [here](#)), in response to falling economic activities, particularly in the US, Europe and China.

Export associations indicate a decline in the export orderbook to 1-1.5 months, from 6 months earlier. Due to delays in dispatches, new orders and weakening demand for apparels, textile companies are also asking banks to extend their credit limits under the ECLGS facility (see [here](#)). Indian readymade garment (RMG) exports have gained share due to the weak situation in Bangladesh's RMG industry, which recorded 14% CAGR during 2019-2021 to USD 52bn.

Export duty on steel and restriction on export of food grains have also impacted these sectors. Overall, anecdotal evidence suggests an impending drag on both manufacturing, particularly engineering goods (see [here](#)) and agri produce.

Indian manufacturing is now facing competition from cheaper Chinese goods across value-added products, including garments, handbags, furniture, household items, electronics and electrical products, etc (see [here](#)).

Pervasive global economic slowdown, India PMI still positive: S&P global PMI survey (Sep'22) points out that the global economy has slid into a contraction in Aug'22, first time since Jun'22. A broad-based deterioration in output and demand conditions is impacting global trade volumes (Exhibit 2, see [here](#)), persisting underlying factors being high inflation, demand destruction, rate hikes by central banks and risk aversion. UK & Europe are in a downturn, and US has recorded contraction. Emerging markets are mixed, with contraction in Chinese manufacturing being countered by better services; Brazil has seen modest gains and India remains strong.

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However, the fact that both China and India gained significantly from disproportionate rise in exports to the US and Europe amid post-COVID supply disruptions, it is only a matter of time when the impact of slowdown or contractions in AE would impact EMs as well. Global manufacturing PMIs indicate perceptible decline in new orders and work backlogs. China faces additional drag from the zero-COVID policy on top of headwinds from the housing market, non-bank and debt drag. The weakening demand conditions are now slowing the pricing power for manufacturing, which is also reflected in contracting commodity prices, especially non-oil.

India, China gained from stimulus-led rebound and supply shortages in AEs: The post-COVID demand-led stimulus and the prolonged supply chain problems in AE created significant opportunity for Asian countries, particularly India and China exports. They gained from both shortage-triggered spurts in global commodity prices and disproportionate volume growth. Global export (and import) volumes grew by 5.1% (5.4%) CAGR over 2019-21, more than twice the post GFC average (2008-2019) average of 2.3%, which was a considerable decline from 5.6% average during the 1998-2008 synchronous global growth and trade cycle (Exhibit 13-16).

This surge in export volume came as an opportunity created by contraction for G7 countries (-5.4%, 2019-21), particularly for UK (-4.2%) and the US (-18.5%), due to strong domestic demand and supply-chain constraints, thereby creating space for China and India, which experienced 25% and 11% CAGR in export volumes, respectively.

Disproportionate gains for Asia exports could be episodic: The disproportionate gain in market share in export volume may be significantly episodic (and partly cyclical), as the high inflation and tightening interest rates scenarios are resulting in global demand destruction, particularly for AEs. The post pandemic trend in global trade volume is estimated at 1.7% compared with the 2019-21 average of 5.1%, which implies that the decline in volume growth in 1Q2022 to 1.2% (3-year CAGR) may sustain with growth slowdown in the US, Europe, and China. Hence, the current growth projection of WTO at 3% for 2022 and 3.4% for 2023 could be subjected to sharp downscaling (Exhibit 9-11).

Corroborating our assessment that India's growth rebound from the pandemic shock was highly dependent on global rebound in trade (see [here](#)), we find that the 10-year elasticity of real GDP growth with respect to global export volume growth has risen to 1.73x (for every 1% rise in trade, 0.73x for China) from 1.13x in 2008 (Exhibit 12).

Hence, the downside risk to growth for China and India from slowing global trade is greater now than in 1992-2008 (high growth, and liberal trade regimes). It is thus no surprise that China continues to struggle in countering a sagging economy, despite a series of stimulus' since Feb'22; China is likely to slow to 2-2.5% in 2022 (OECD, Conference Board, Sep 2022), missing its official target of 5.5% (see our note [here](#)). For India too, we have scaled down our projection to 5.0-5.5% for FY23E, with structural trend at 4.0-4.5% (see [here](#)). These are lower than RBI's projections of 7.2% for FY23E and consensus at 6.5% for FY24E.

India's export share reversed after a long stagnation since 2013: After rising from 0.8% in 2002 to a peak of 1.8% in 2013, India's share in global goods exports fell to 1.6-1.7% before rebounding to 1.8% in 2021, on the back of post-pandemic upsurge. Within this, textiles and RMG saw the most rebound, reversing most of the decline, with a rise from 3.8% in 2020 to 4.6% currently. Likewise, the share of metals (2.7%), meat-fish, etc (2.7%), machinery (0.73%), agri produce (2.3%), too rose sharply (Exhibit 17-18).

The post-pandemic trend in global trade volume is estimated at 1.7% compared with the 2019-21 average of 5.1%, which implies that the decline in volume growth in 1Q2022 to 1.2% (3-year CAGR), may sustain, with growth slowdown in the US, Europe, and China. Hence, the current growth projection of WTO at 3% for 2022 and 3.4% for 2023 could be subjected to sharp downscaling

India's growth rebound from the pandemic shock was highly dependent on global rebound in trade (see [here](#)). We find that the 10-year elasticity of real GDP growth with respect to global export volume growth has risen to 1.73x (for every 1% rise in trade, 0.73x for China) from 1.13 in 2008

Broad sectors that could face export vulnerability are agricultural produce and food related, textiles, readymade garments, metals (including steel), machinery & equipment, auto parts, and chemicals, in our view. We have already seen textile and garment exporters, as well as steel manufacturers facing significant decline. Most of these sectors gained from higher commodity prices, rising orderbooks and surging market capitalisations of listed companies. We have precautionary views on such names, and recommend higher concentration on domestic consumption themes

Since FY20, the share of engineering goods export to the US has been rising (12.4% in Mar'19 to 18.4% in Aug'22), despite overall exports in the segment having fallen. Iron and Steel & Machine tools have been the major drivers. Historically, it has been seen that since early 1990s, when the US (and AEs) prospers, exports to EMs get diverted to AEs, to gain from the rise in prices, as price realisation is much higher in AEs than in EMs. Hence, the episodic rise since FY20 is susceptible to a decline, due to the slowdown or recession in AEs

Sectors that gained the most are likely to lose the most; domestic themes placed better: Lead indicators, and media reports indicate that sectors that benefited the most from the disproportionate rise in exports to AE during the post-pandemic demand burst too are adversely impacted, as they face declining volume and export price realisations due to correction in global commodity prices.

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Most of these sectors gained from higher commodity prices, rising orderbooks, disproportionate rise in operating cash flows and surging market capitalisations of listed companies. We have precautionary views on such names and recommend higher concentration on domestic consumption themes.

Rise in share of engineering goods export to the US is episodic:

Since FY20, the share of engineering goods export to the US has been rising (12.4% in Mar'19 to 18.4% in Aug'22), despite overall exports having fallen in the segment (in value and volume terms, Aug'22). Iron and Steel & Machine tools have been the major drivers. Historically, when the US (and AEs in general) prospers, exports to the EMs get diverted to AEs, to gain from the rise in prices, as the price realisation is much higher in AEs than in EMs. Though Asia remains a dominant market for India's engineering exports, its share in total exports of engineering goods have fallen since 2020. Also, when commodity prices rise, the share of exports to AEs ascends and vice versa (as seen during 2000-06, when the US was prospering with the rising share of Indian exports to the US). So, Indian exports of engineering goods mimic both, the commodity cycle as well as the growth cycle of AEs. Hence, with the global scenario worsening, and for AEs in particular, Indian exports are susceptible to a decline, as the current level of buoyancy is episodic in nature (Exhibit 8, 24-25).

Indian cap goods exports: Significant gains in the US markets: A significant portion of the buoyancy in the capital goods sector over the past two years appears to be driven by export demand, especially from the US. Indian companies have gained from demand created in the US after tax cuts there in 2017, and the post-pandemic shortages in a variety of components such as electrical equipment, electronics, AC compressors, auto components, metals, and other engineering goods. Indian exports of machinery to the US hence, increased from USD 2.2bn in 2016 to USD 5bn in 2019 and further to USD 6bn in 2021 (Exhibit 27). This implied a significant rise in India's exports of machinery to the US from 19% of total for the category to 28% in 2021.

It is untenable however, to contend that Indian machinery exports have started competing out Chinese, which had a total global export bill under machinery and equipment of USD 805bn (2021), of which, USD 115bn went to the US, at 10% CAGR over 2019, and 20x higher than Indian exports (Exhibit 28). Long-term trends indicate that factors behind India's export of machinery to the world (particularly to the US) are both structural and cyclical; it rises with improved liberal trade regime (1992-2008), gains from global cyclical upcycle and is accompanied by rising commodity prices.

Significant buoyancy in India's capital goods sector has been driven by export demand, especially from the US. Indian companies gained from demand created in the US (after its tax cuts in 2017) and post-pandemic shortages in a variety of components such as electrical equipment, electronics, AC compressors, auto components, metals, and other engineering goods. This implies a significant rise in India's exports of machinery to the US from 19% of total for the category to 28% in 2021. But China still dominates the US market in exports of capital goods, and is 20x higher than India

With US PMI falling, new orders for machinery have slowed and shrunk by 7.5% YoY (Jul'22) from a peak of 23% (Jun'21) in real terms. Hence, with the cyclical downturn imminent in major economies (US, Europe and China) and commodity price correction under way, export-oriented machine exporters could also face risk on their orderbooks

But new order for machines is contracting in real terms now: With US PMI falling, new orders for machinery have slowed, and shrunk by 7.5% YoY (Jul'22) from a peak of 23% (Jun'21, Exhibit 21) in real terms. Hence, with the cyclical downturn imminent in major economies (US, Europe and China), commodity price correction under way, export-oriented machine exporters could face risk on their orderbooks, which continue to swell thus far.

Based on our select sample of companies, we find that the expansion in order books of machine-producing companies has been driven by private companies (specially Siemens, followed by ABB, Thermax, Kirloskar Brothers, and TRIL), growing at 33% YoY in nominal term. While the order books of PSU companies (BHEL and BEL, 82% of total Rs 2trn in Jun'22) have been stagnant, defense-related orders from the government have however grown well (HAL). While a significant part of the overall order book surge is driven by the digitisation theme for Siemens, we also find a high correlation between private sector order book and the synchronous rise in global commodity prices since early 2020 (Exhibit 30-35).

Over a longer horizon, the operating matrix of all machinery industry would be extremely sensitive to the global economic and commodity price cycles. These include growth in sales, operating profit, margins and return ratios (Exhibits 38-43). These sensitivities also make the Machinery index (CMIE) or machinery stock valuations highly exposed to vulnerability arising from higher rates and decline in metals prices due to a stronger dollar (Exhibit 42-45).

At the broader level, while the projects under implementation of all sectors have risen by Rs 12trn since the end of 2019 (up 9.5%) in real terms, it has contracted by 25% after adjusting for manufacturing WPI (Exhibit 36-37).

Revival in India's consumption driven by lagged impact of trade buoyancy

The revival in India's consumption since the pandemic shock is driven by a) unwinding of pent-up demand, b) revival in sales growth in specific sectors, especially export-led, resulting in compensation improving, c) household (HH) leveraging, d) drawdown of gross financial savings of households to 10.8% of GDP after the sharp rise to 16% of GDP in FY21 post COVID, f) patchy gains in employment, and g) post-COVID fiscal support in rural areas under the Garib Kalyan Yojna (see [here](#)), extended free food distribution program till Dec'22 costing Rs 2.5trn in FY23E, and an enlarged MNREGA budget (declining from a high of Rs 1.11trn in FY21 to Rs 730bn in FY23BE).

However, the revival in consumption so far has been partial and less broad-based. We note the following trends in the leading indicators:

Revival in sales growth of Indian companies, translating into better compensation growth, incremental gains in employment and leveraged spending have helped revive India consumption. A large part of this revival is attributed to positive global spillover after the pandemic. But with global headwinds now getting pervasive and domestic employment gains still tentative, tightening in financial conditions as an impact of global tightening makes the policy choice challenging for RBI and the government. The trade-off could lead to a sub-par growth trajectory

- a) Sales growth of non-finance companies has rebounded to an 8-quarter average of 27% YoY (1QFY23) from the post lockdown low of -7.5%. This has resulted in compensation growth recovering to 10% from 3% (8-quarter average, Exhibit 46). While it remains only modestly above the retail inflation at 7%, it still signals some improvement in spending power in the organised sector.
- b) A large part of the rebound in corporate sales growth can be attributed to the surge in global commodity prices, rising share of trade in India's GDP (50% in 1QFY23) and IT services exports.
- c) Resulting from the gains in the organised sectors and low real interest rates on lending and deposits, retail lending growth of banks have risen further to 18%, implying leveraged consumption (Exhibit 47).
- d) Net financial savings rate (% of GDP) of households increased substantially to 16% (net of financial liabilities) in FY21, driven by the lockdown impact. But that has reversed in FY22, declining to 10.8% and providing a fillip to consumption (Exhibit 54-55).
- e) RBI and CMIE consumer confidence indices improved consistently, but still are 26% lower than the pre-pandemic levels. Likewise, surveys on employment conditions show decline in the level of pessimism (Exhibit 44-45).
- f) While CMIE employment data shows that of the 17.1mn individuals displaced due to the lockdown, only 6.9 mn (or 40%) have been absorbed (Exhibit 48). Reversal of labor from agri after the opening-up, to other sectors in search of work has been far greater than was initially absorbed due to the shock. The construction sector saw a part of the employment gains; manufacturing and services sectors absorbed only 40% and 60% of the people displaced, respectively (Exhibit 49). All put together, employment fell by 10mn, mostly in manufacturing (-7.6mn) and services (-5.1mn). (Exhibit 50)
- g) Overall, while the employment scenario has improved modestly, gains in manufacturing sectors like metals, machinery, chemicals, and a strong rebound in construction materials have been significant (Exhibit 53); majority of the other sectors are lagging. Similarly, in service sectors, maximum improvement is seen in wholesale and retail trades, BFSI and IT sectors (Exhibit 52). But the aggregate employment in the services sector has been lower, especially for less-skilled jobs. Recent data (Jul-Aug, Exhibit 51) shows that employment momentum slowed in 2QFY23, declining by 3.4mn after having risen by 0.67mn in 1QFY23. The decline is mainly contributed by the manufacturing sector (-0.9mn), and outflows in the agri sector continue (4.5mn).

Thus, the big picture is that gains in employment and consumption are largely driven by the formal and urban sectors. There is excess supply of labor, especially for the less skilled or in the unorganised sector, keeping the wage and income growth modest, unmatched for the high level of inflation at 7%.

For the consumption momentum to sustain, gains in corporate cash flows should translate into wide-spread gains in employment and wages. The concern is that the post-pandemic recovery in consumption is strongly linked to the lagged impact of positive global spill overs, which are now receding

For the consumption momentum to sustain, gains in corporate cash flows should translate into wide-spread gains in employment and wages. The concern is that post-pandemic recovery in consumption is strongly linked to the lagged impact of positive global spill overs, which are now receding. In addition, the fiscal support to rural areas is also declining from the post-COVID peak.

Thus, the tightening of domestic financial conditions, rising rates, high inflation, contraction in exports and rupee depreciation come at a time when India's employment and consumption recovery from the pandemic shock is still incomplete. This makes the policy choice for RBI and the government very tricky, which may end up translating into a sub-par trajectory.

Systematix portfolio view: Increased focus on domestic themes

- a) Continue to focus on domestic themes, with an OW on consumption.
- b) Rising rates and currency depreciation could have implications on growth and valuations, especially for the rate-sensitive and deep cyclical sectors.
- c) Consumption demand exposed to leveraged consumption, viz., housing and autos could also get impacted. We have reduced our OW on autos.
- d) Reduce exposures in global cyclicals and companies that gained from post pandemic rebound in the US and Europe, especially in consumer and industrial spaces.
- e) Banking sector stocks and other cyclicals such as industrial and base metals are likely to be more vulnerable. Maintain our UW on Banks and BFSI (see our latest note [here](#)). We have zero weight on metals.
- f) **Favorable impact of decline in global crude prices**
 - 1) **OMCs HPCL and BPCL top gainers:** Beneficiaries of sharp improvement in marketing margin, expected hike in retail auto fuel prices; adverse for upstream companies.
 - 2) **Consumption stocks: Asian Paints, Berger Paints and Pidilite** are expected to continue with their strong volume growth momentum on the back of festive season demand. Demand has been resilient, despite 25-30% price hike since Dec'21. The decline in crude-sensitive raw material prices is likely to translate into significant improvement in operating parameters. Premium multiples are likely to sustain due to dominant market position.

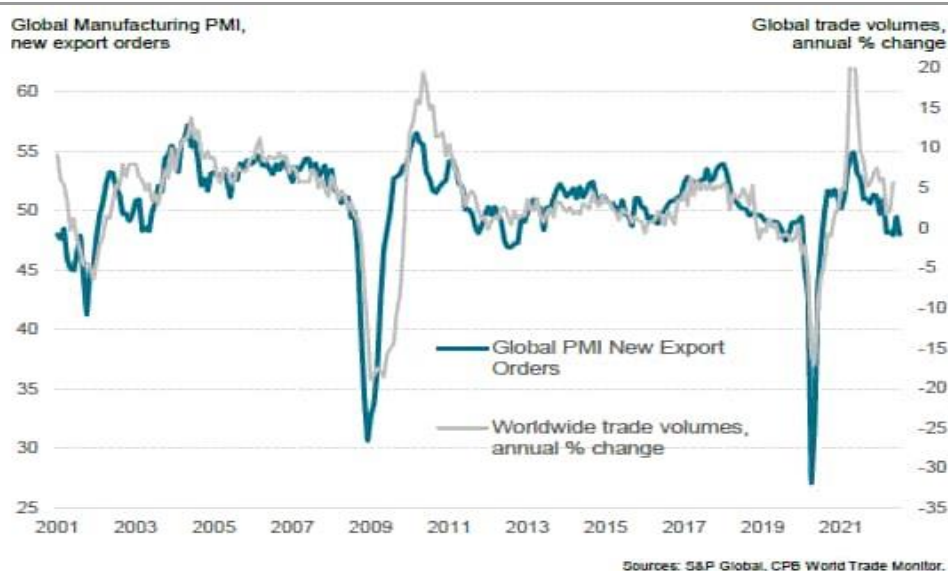
Our OW on pharma is backed by our latest note [Favorable risk reward](#): The Indian pharma sector is poised for mid-single to high-single-digit sales growth and margin expansion. Our positive outlook on the sector stems from 1) likely easing of inflationary pressures 2) expected easing of price erosion pressure in the US, 3) monetisation opportunities in complex generics, and 4) secular growth potential in branded formulations (India and EMs). Tailwinds from a potential cyclical upturn in the pricing of oral solids in developed markets and scale up in China market for select players is something we have not factored in our estimates and is a free call option. News flows on the NCE pipeline should improve the medium-to-long-term growth sentiment, and trickle into valuation multiples. Companies now are cash positive, and have strong FCFs, which they could leverage for opportunistic acquisitions. We recommend a **BUY on Sun Pharma, Cipla, Dr. Reddy's, Ajanta Pharma and Indoco Remedies, HOLD on Lupin and a SELL on DIVI's.**

Maruti Suzuki has been our non-consensus SELL idea.

Exhibit 1: Systematix model portfolio

| | Sector weights | | | Systematix Financial portfolio | Stock weights |
|------------------------------|----------------|--------------|--------------|--------------------------------|---------------|
| | Systematix | Nifty Index | OW/UW | | |
| Agri Input & Chemicals | 1.0 | 0.5 | 0.47 | SRF | 1.0 |
| Auto & Auto Ancillaries | 7.0 | 6.0 | 1.02 | Eicher Motors | 2.0 |
| | | | | Ashok Leyland | 2.0 |
| | | | | TVS | 1.5 |
| | | | | Endurance | 1.5 |
| Building Materials | 0.5 | - | 0.50 | Stylam | 0.5 |
| Cement | 3.0 | 2.2 | 0.82 | Shree Cement | 1.0 |
| | | | | UltraTech Cement | 1.3 |
| | | | | Ramco Cement | 0.8 |
| Consumer Durables | 3.0 | - | 3.00 | KEI | 1.0 |
| | | | | Bajaj Electricals | 2.0 |
| Consumer Staples & Retail | 13.54 | 12.2 | 1.38 | GCPL | 4.5 |
| | | | | Britannia Industries | 1.4 |
| | | | | HUL | 3.0 |
| | | | | ITC | 2.3 |
| | | | | Aditya Birla Retail | 2.3 |
| Industrials | 2.0 | - | 2.00 | BEL | 1.0 |
| | | | | HAL | 1.0 |
| Infrastructure/Construction | 2.5 | 3.6 | -1.09 | Larsen & Toubro | 2.5 |
| IT Services | 12.0 | 15.3 | -3.31 | HCL Tech | 4.0 |
| | | | | Infosys | 6.0 |
| | | | | Persistent Systems | 2.0 |
| Metals & Mining | - | 2.8 | -2.76 | | |
| Oil & Gas | 11.6 | 12.6 | -1.00 | Reliance Industries | 6.8 |
| | | | | BPCL | 1.5 |
| | | | | IGL | 3.3 |
| Pharmaceuticals & Healthcare | 5.50 | 3.9 | 1.58 | Dr Reddy's | 2.0 |
| | | | | Cipla | 2.0 |
| | | | | Indoco Remedies | 1.5 |
| Telecom | 3.0 | 2.3 | 0.68 | Bharti Airtel | 3.0 |
| Utilities | 3.0 | 2.5 | 0.46 | NTPC | 3.0 |
| Financials | 32.4 | 36.2 | -3.76 | Financials | |
| Insurance | 1.0 | 1.4 | -0.40 | HDFC Life | 1.0 |
| NBFC | 8.0 | 9.3 | -1.33 | Bajaj Finance | 2.5 |
| | | | | Cholamandalam Finance | 1.5 |
| | | | | HDFC | 2.0 |
| | | | | Shriram Transport | 2.0 |
| Banks | 23.4 | 25.4 | -2.02 | AXIS Bank | 3.6 |
| | | | | HDFC Bank | 9.0 |
| | | | | ICICI Bank | 8.8 |
| | | | | State Bank of India | 2.0 |
| | 100.0 | 100.0 | | Total | 100.0 |

Benchmarked to Nifty 30, last updated on Sep 19, 2022

Exhibit 2: Global goods trade, steep fall in export orders akin to post GFC, 2019 trade wars and 2011 European crisis

Source: S&P Global

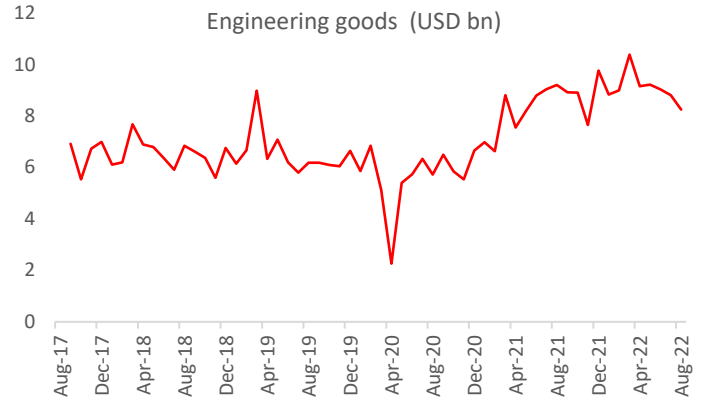
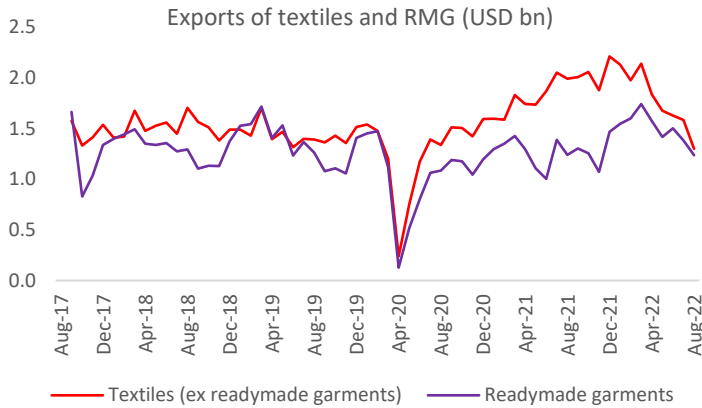
Exhibit 3: India's goods trade (USD bn), slowing exports and widening deficit

| Exports (USD bn) | Apr-Aug'22 | Apr-Aug'21 | % Share | % YoY | Aug'22 | Aug'21 | % Share | % YoY |
|---------------------------------|-------------------|-------------------|----------------|-------------|---------------|---------------|----------------|--------------|
| Engineering goods | 46.6 | 45.1 | 24.2 | 3.3 | 8.3 | 9.7 | 25.0 | (14.6) |
| Petroleum products | 40.3 | 23.4 | 20.9 | 72.3 | 4.9 | 4.7 | 14.9 | 5.4 |
| Gems and Jewellery | 16.8 | 16.1 | 8.7 | 4.6 | 3.3 | 3.4 | 10.0 | (4.1) |
| Organic & Inorganic chemicals | 13.3 | 11.5 | 6.9 | 15.7 | 2.5 | 2.2 | 7.7 | 13.4 |
| Drugs and Pharma | 10.5 | 9.9 | 5.5 | 5.8 | 2.1 | 2.0 | 6.5 | 6.6 |
| Electronic goods | 8.3 | 5.4 | 4.3 | 54.7 | 1.7 | 1.1 | 5.2 | 50.7 |
| Readymade garments | 7.1 | 6.0 | 3.7 | 17.8 | 1.2 | 1.2 | 3.7 | (0.4) |
| Rice | 4.7 | 3.8 | 2.4 | 21.8 | 1.0 | 0.7 | 3.1 | 42.3 |
| Textile (ex RMG) | 5.0 | 6.0 | 2.6 | (16.6) | 0.9 | 1.3 | 2.7 | (32.3) |
| Plastic etc. | 3.9 | 4.2 | 2.0 | (6.3) | 0.7 | 0.8 | 2.3 | (1.5) |
| Total of 10 | 156.5 | 131.4 | 81.3 | 19.1 | 26.7 | 27.2 | 81.1 | (1.5) |
| Rest | 36.1 | 33.0 | 18.7 | 9.2 | 6.3 | 6.2 | 19.0 | 0.5 |
| Total Exports | 192.6 | 164.4 | 100.0 | 17.1 | 33.0 | 33.4 | 100.0 | (1.2) |
| Imports (USD bn) | Apr-Aug'22 | Apr-Aug'21 | % Share | %YoY | Aug'22 | Aug'21 | % Share | %YoY |
| POL | 99.4 | 52.8 | 31.3 | 88.4 | 17.6 | 9.4 | 28.5 | 86.4 |
| Electronic goods | 32.7 | 25.1 | 10.3 | 29.9 | 7.3 | 5.9 | 11.8 | 22.9 |
| Coal, Coke etc. | 26.8 | 9.8 | 8.4 | 174.4 | 4.5 | 1.9 | 7.4 | 133.6 |
| Machinery | 18.2 | 15.0 | 5.7 | 21.7 | 3.9 | 2.9 | 6.3 | 33.3 |
| Gold | 16.4 | 18.8 | 5.2 | (12.8) | 3.5 | 6.7 | 5.7 | (47.5) |
| Organic & Inorg, Chemicals | 16.3 | 11.5 | 5.1 | 41.2 | 3.0 | 2.1 | 4.8 | 42.7 |
| Precious & Semi-precious stones | 13.9 | 12.2 | 4.4 | 14.7 | 2.4 | 2.2 | 3.9 | 7.5 |
| Artificial resins, plastic etc. | 10.6 | 7.6 | 3.3 | 39.2 | 2.0 | 1.4 | 3.3 | 47.0 |
| Vegetable Oil | 9.2 | 6.9 | 2.9 | 33.4 | 1.9 | 1.3 | 3.1 | 41.6 |
| Non-ferrous metals | 8.7 | 6.5 | 2.7 | 33.6 | 1.8 | 1.3 | 2.9 | 32.0 |
| Total of 10 | 252.0 | 166.0 | 79.3 | 51.8 | 47.9 | 35.3 | 77.6 | 35.6 |
| Rest | 65.8 | 52.2 | 20.7 | 26.1 | 13.8 | 9.8 | 22.4 | 40.9 |
| Total Imports | 317.8 | 218.2 | 100.0 | 45.6 | 61.7 | 45.1 | 100.0 | 36.8 |

Source: Gol press release

Exhibit 4: India's textile exports declined by 45% due to softening prices and slackening demand in AEs

Exhibit 5: India's engineering goods exports declined by 20% since 1QFY22, slowing manufacturing PMIs in AEs

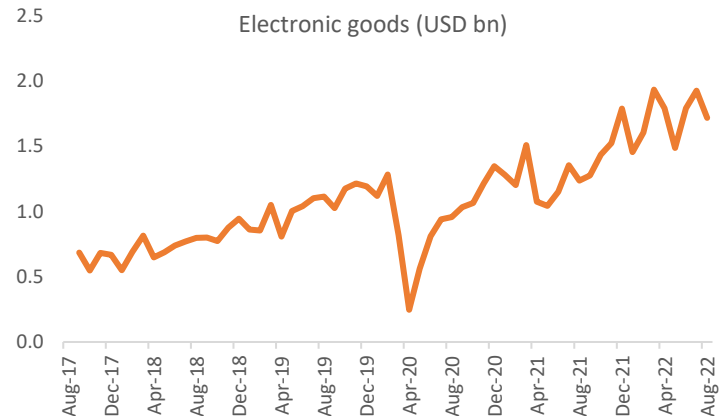
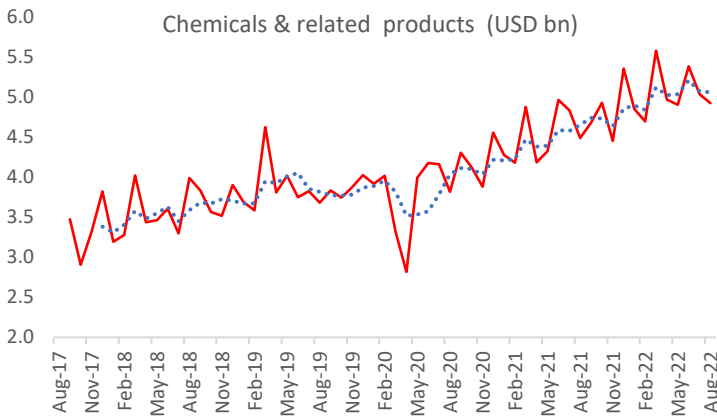


Source: WTO, Systematix Research

Source: WTO, Systematix Research

Exhibit 6: Chemicals exports have been resilient, but are losing momentum

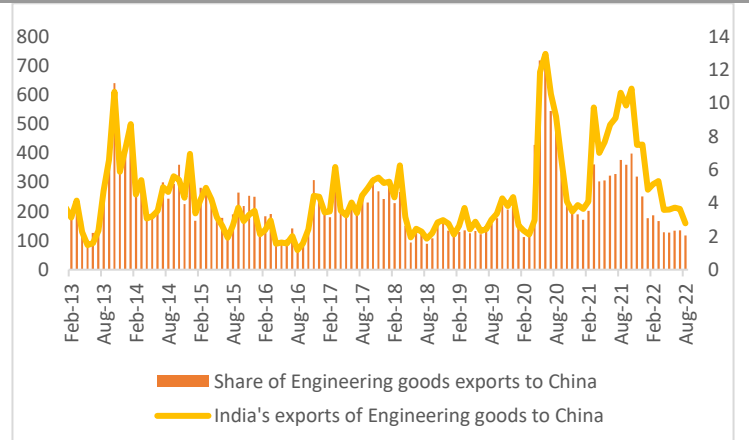
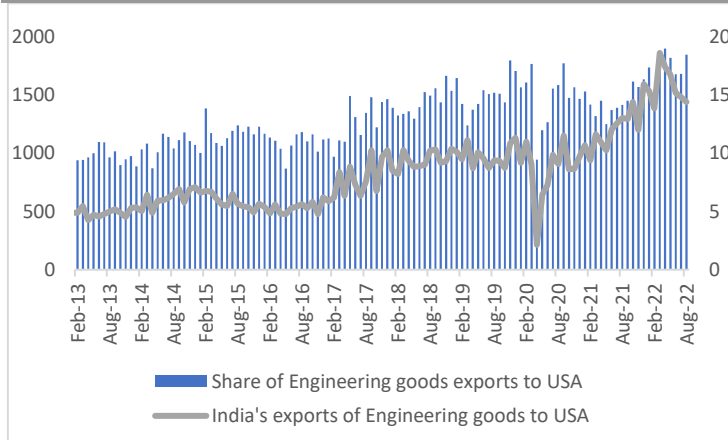
Exhibit 7: Electronic goods exports have been resilient, but are losing momentum



Source: WTO, Systematix Research

Source: WTO, Systematix Research

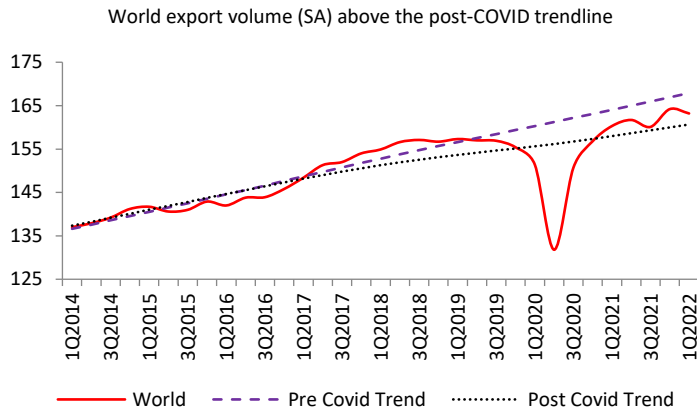
Exhibit 8: Share of engineering goods exports to the US rises but falls in China; in value terms, there is a decline in both countries



Source: CMIE, Share % on RHS, Exports (USD mn, monthly), Systematix Research

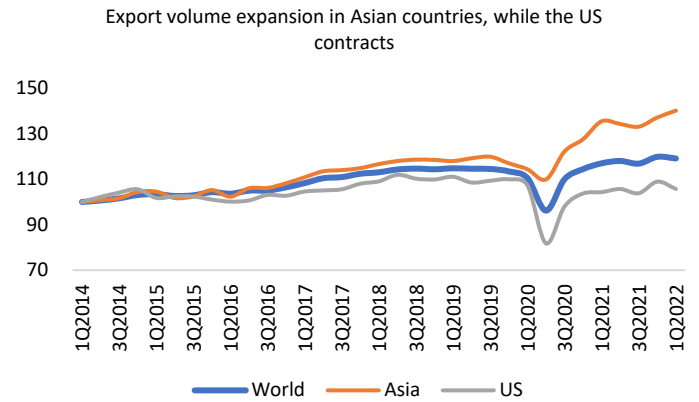
Source: CMIE, Systematix Research, Share % on RHS, Exports (USD mn, monthly)

Exhibit 9: Global merchandise export volumes rebounded higher than pre-COVID, but to a lower trendline; currently slowing



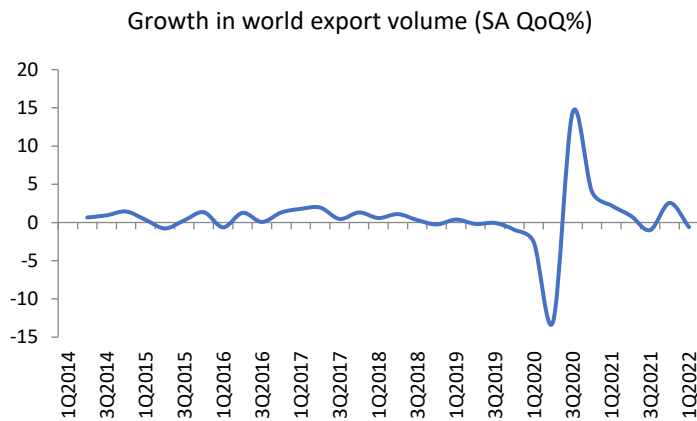
Source: WTO, Systematix Research

Exhibit 10: Asia gained disproportionately from the post-COVID rebound; trade rebound due to supply chain constrained AE



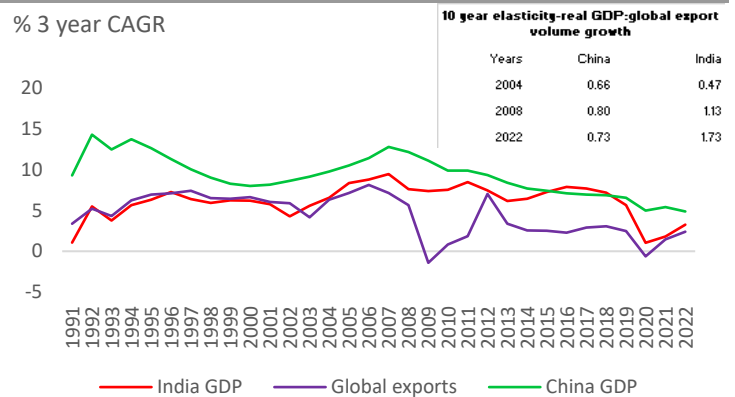
Source: WTO, Systematix Research

Exhibit 11: Global trade volume is slowing due to weakening



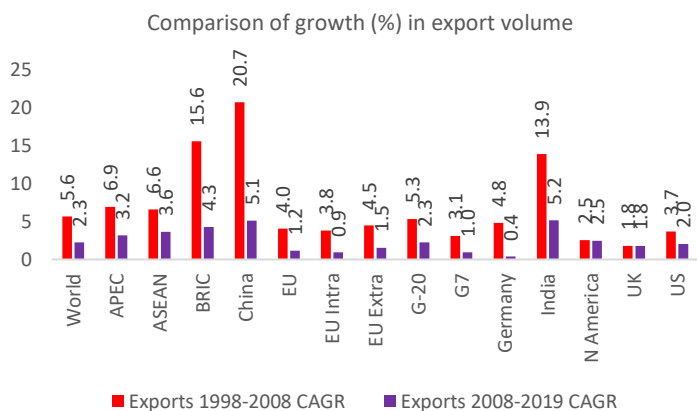
Source: WTO, Systematix Research

Exhibit 12: Both India and China have been highly sensitive to global trade volume growth, now higher for India



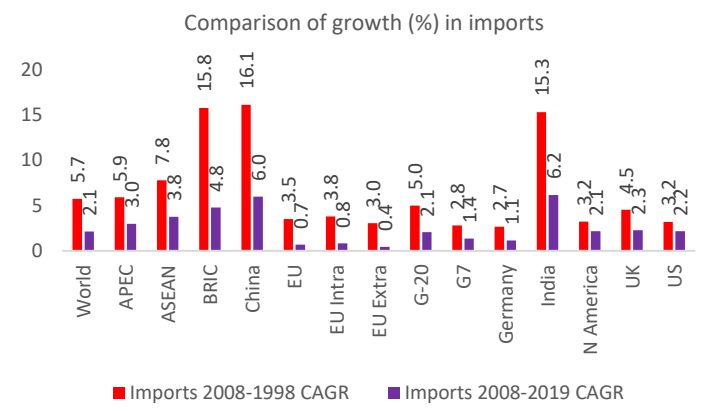
Source: WTO, Systematix Research

Exhibit 13: Performance of export growth post Asian crisis for China, India, & Asia was much stronger than after GFC 2008



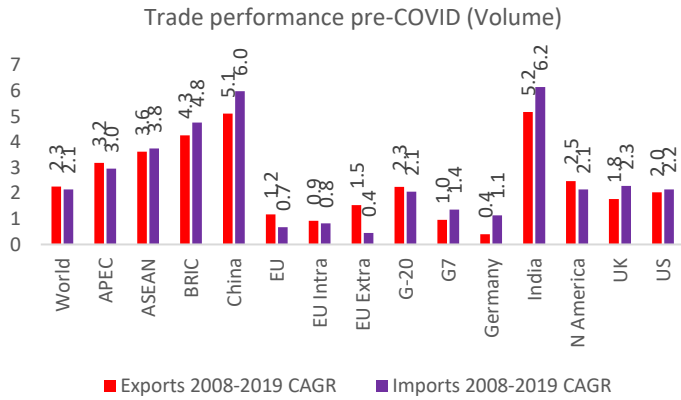
Source: WTO, Systematix Research

Exhibit 14: Strong domestic growth also seen in robust import growth post Asian crisis for China, India, and Asia vs post GFC 2008



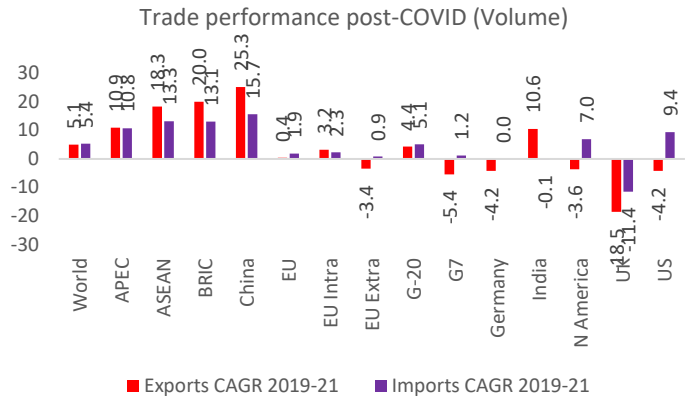
Source: WTO, Systematix Research

Exhibit 15: Unlike post-Asian crisis, post-GFC average export growth lagged imports for Asia; impact of de-globalisation



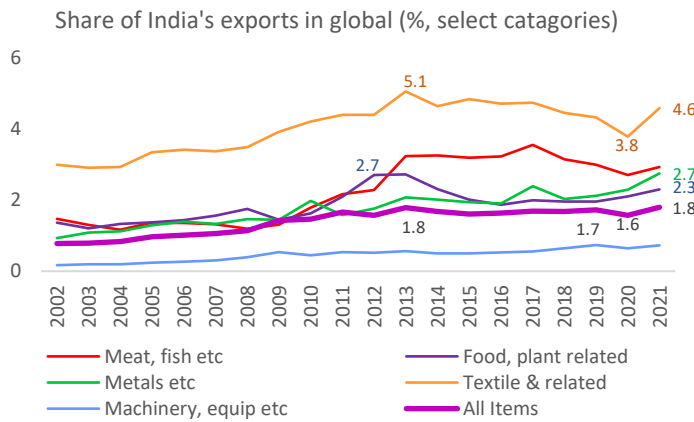
Source: WTO, Systematix Research

Exhibit 16: Average export growth during 2019-21 higher than the post-GFC average; Asia gained from supply shortages in AEs



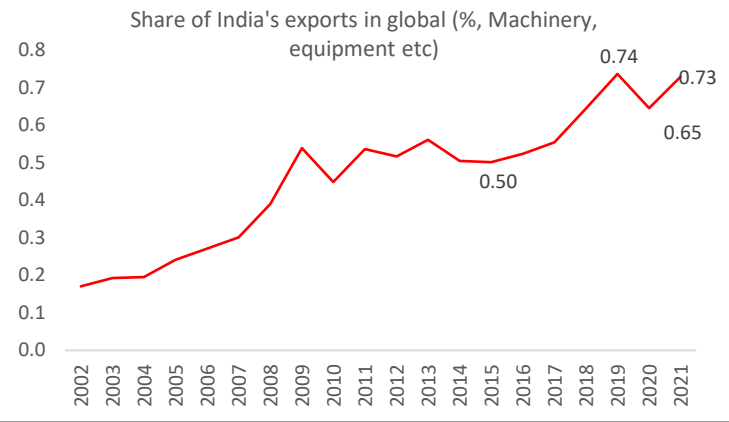
Source: WTO, Systematix Research

Exhibit 17: India's share in trade rebounds after being stagnant since 2013; led by commodity prices & supply chain-issues in AEs



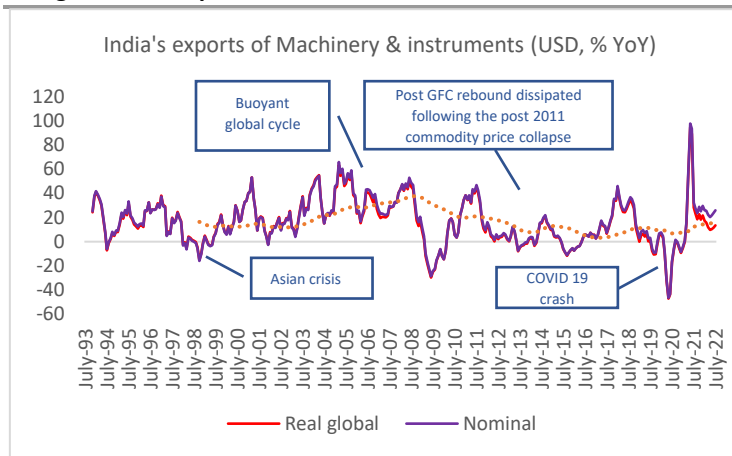
Source: CMIE, Systematix Research

Exhibit 18: Domestic capital goods sector gained from exports of machinery and equipment, mainly to the US



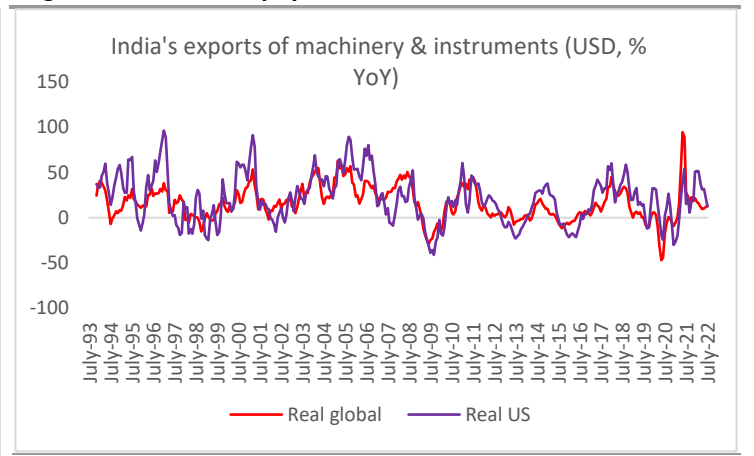
Source: CMIE, Systematix Research

Exhibit 19: Machinery exports high susceptible to global cycles and global metal prices



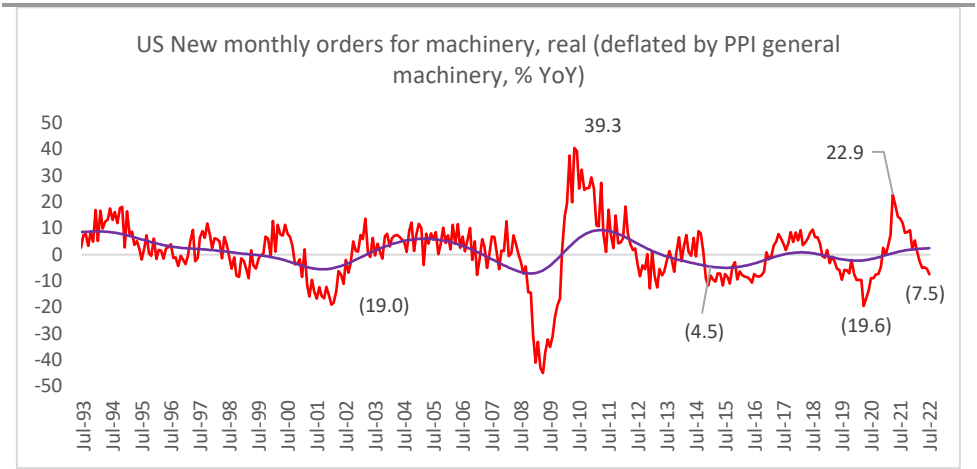
Source: CMIE, Systematix Research

Exhibit 20: Machinery exports to the US shows greater sensitivity to global or commodity cycles



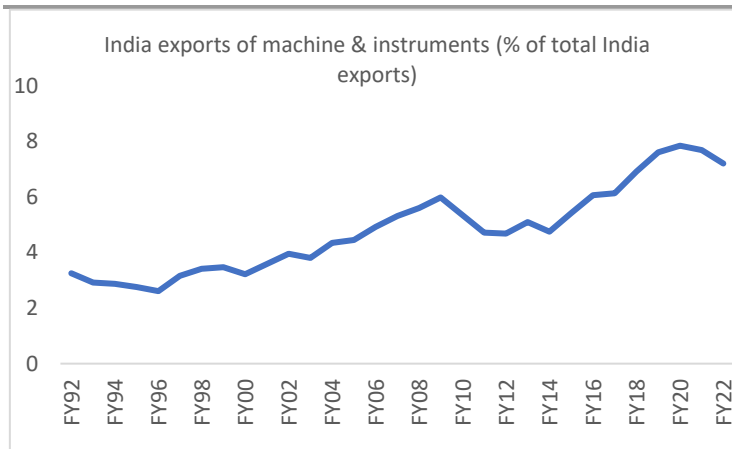
Source: CMIE, Systematix Research

Exhibit 21: New order of machinery in the US has started contracting (% YoY)



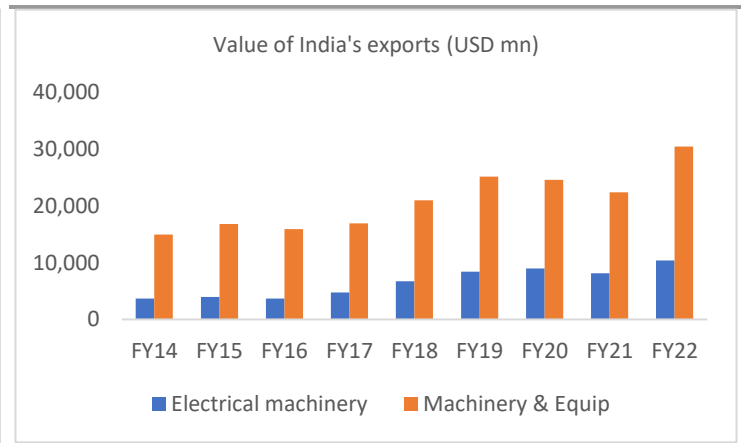
Source: CBO, Systematix Research

Exhibit 22: Machinery & equipment as share of India's exports rise to over 7% from 5% in FY14



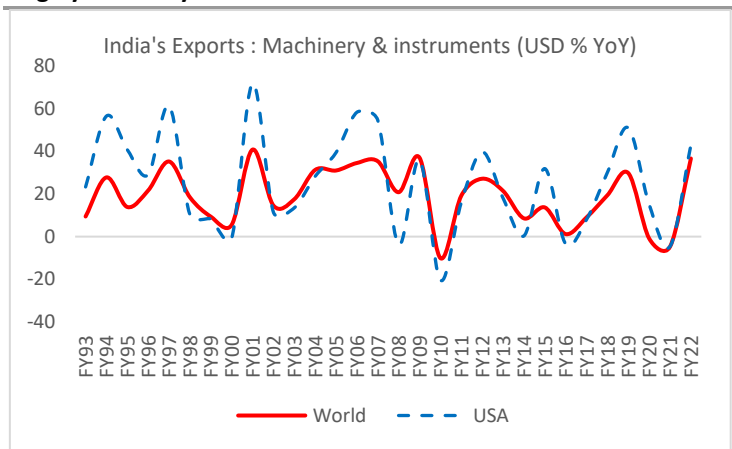
Source: CMIE, Systematix Research

Exhibit 23: Exports rose in absolute terms during 2018-19 and in FY22



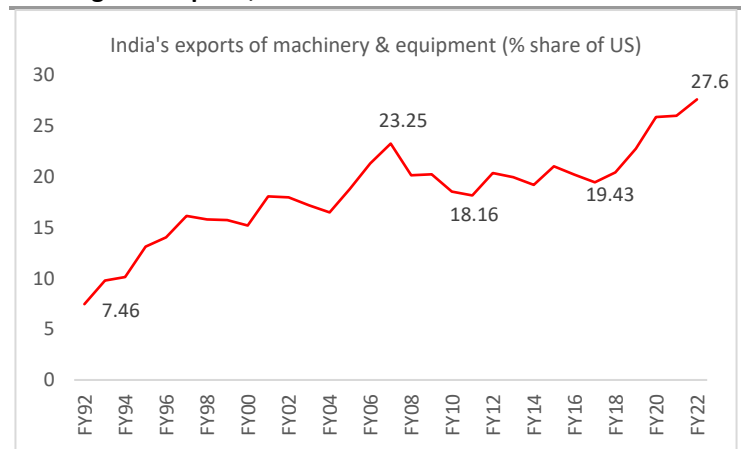
Source: CMIE, Systematix Research

Exhibit 24: Revival in India's capital goods exports to the world largely driven by the US market



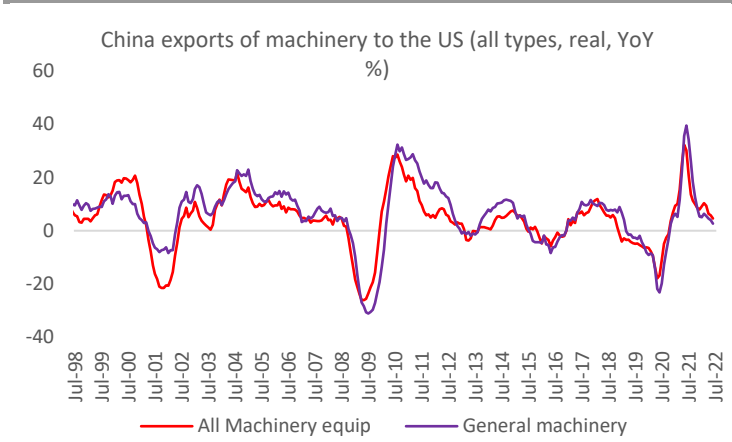
Source: CMIE, Systematix Research

Exhibit 25: Exports of machinery to the US has risen to 28% of India's global exports; a slowdown in the US is a risk to the sector



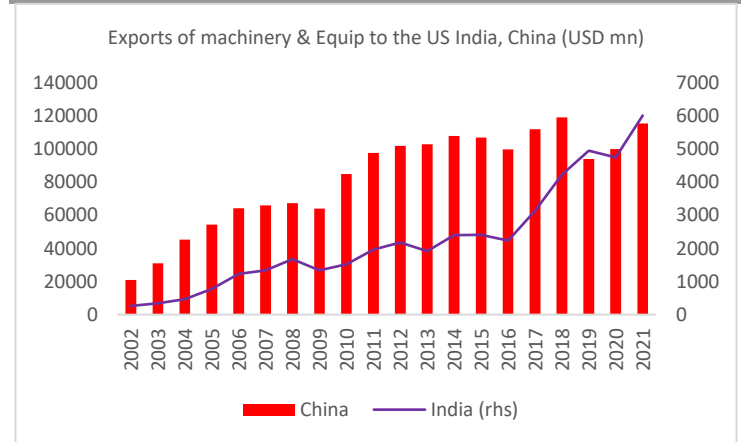
Source: CMIE, Systematix Research

Exhibit 26: Chinese export of capital goods to the US is also susceptible to cyclicity



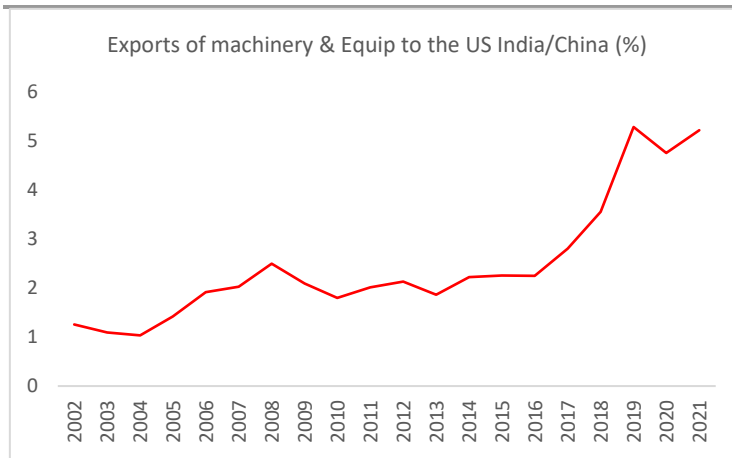
Source: CMIE, Systematix Research

Exhibit 27: There has been a rise in India's exports to the US since US tax cuts in 2017, but China is 20x higher



Source: CMIE, Systematix Research

Exhibit 28: India's share in the US machinery market has increased from 2.5% to 5% since 2017



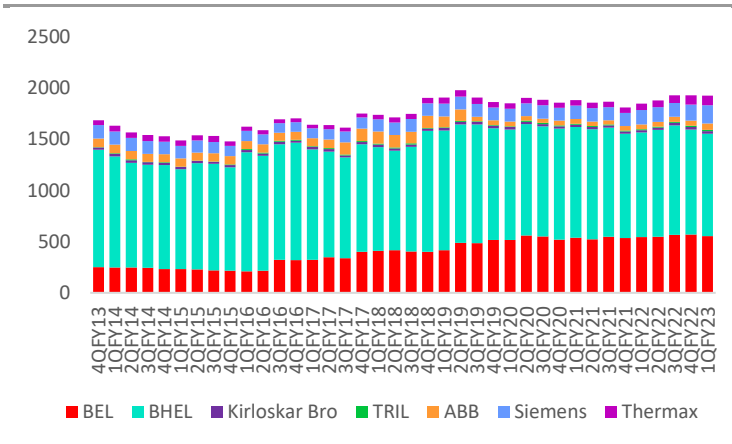
Source: CMIE, Systematix Research

Exhibit 29: India's share in exports remained stagnant in 2013-2019, the rise in 2021 compensates for the post-COVID decline



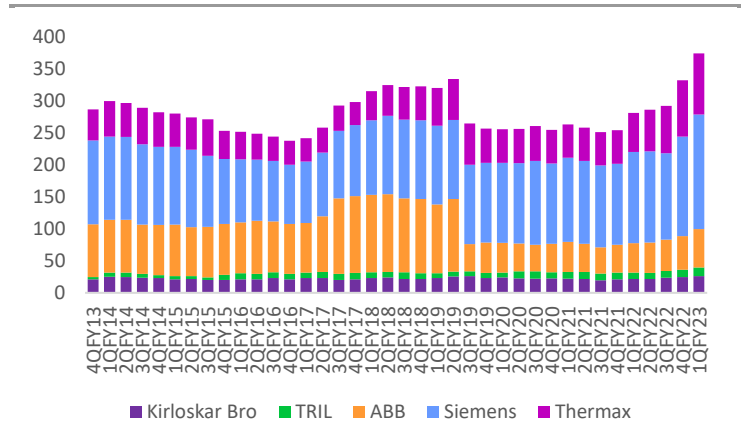
Source: CMIE, Systematix Research

Exhibit 30: Order book of machinery-producing companies (INR bn), recovery driven by private cos, PSU remain stagnant



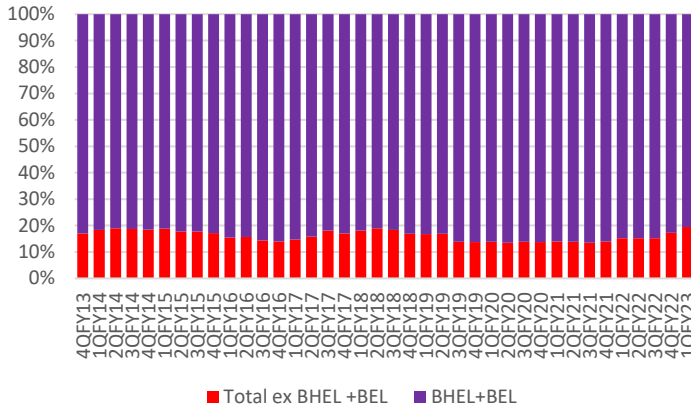
Source: CMIE, Defense companies like HAL has seen orderbook rising at 13% CAGR during FY19-FY22 at INR 850bn, 80% of which is manufacturing, little exports

Exhibit 31: Strong rebound in order book for ABB, Siemens and Thermax, significant exports contribution (INR bn)



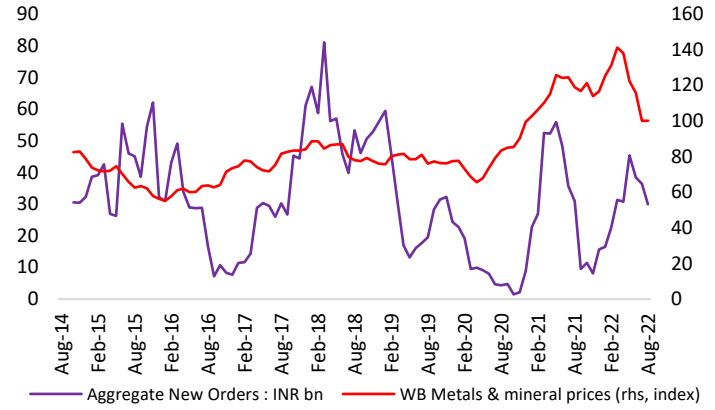
Source: CMIE, Systematix Research

Exhibit 32: A large portion of the machinery-producing companies has not grown



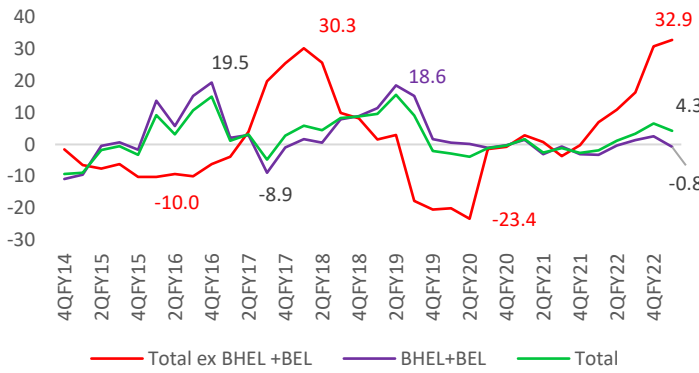
Source: CMIE, Systematix Research

Exhibit 33: New orders for machinery & equip. highly correlated to global metals prices, downside risk from global cycle (% YoY)



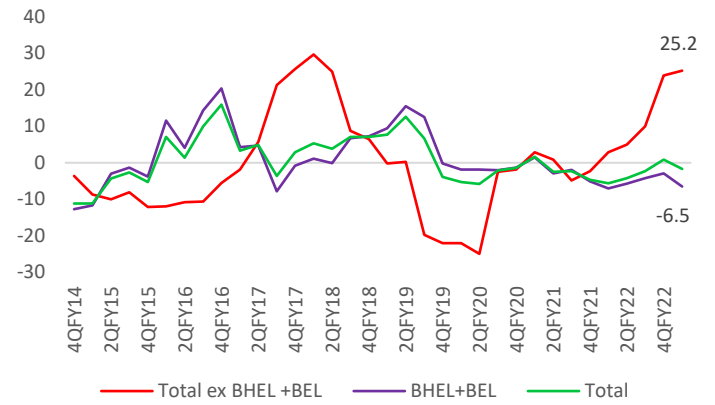
Source: CMIE, all companies, 6 month moving average

Exhibit 34: Nominal order book of machinery-producing companies (% YoY), PSU typically seen counterbalancing private companies



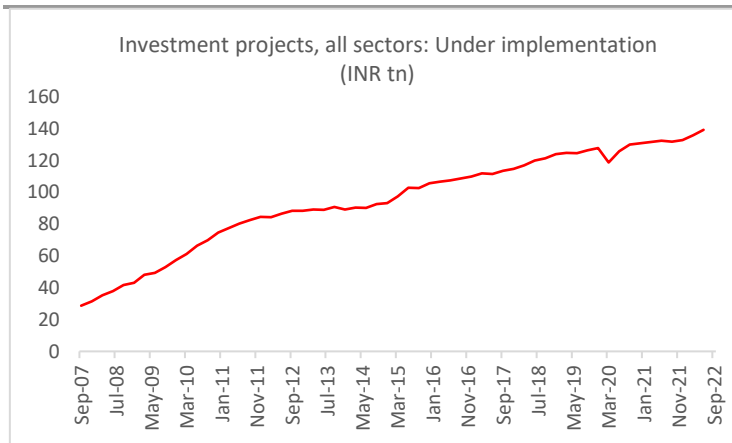
Source: CMIE, Systematix Research

Exhibit 35: Real order book of machinery-producing companies (% YoY), PSUs typically seen counterbalancing private companies



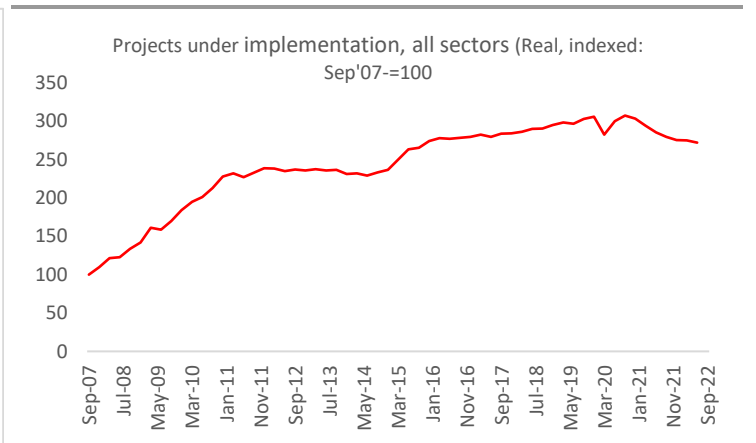
Source: CMIE, Systematix Research

Exhibit 36: Recent uptick in projects under implementation and new projects announced significantly driven by high inflation



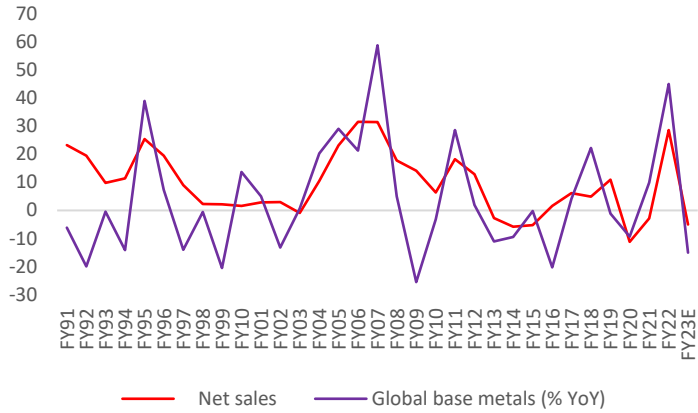
Source: CMIE, Systematix Research

Exhibit 37: In real terms, projects under implementation have declined below pre-COVID levels



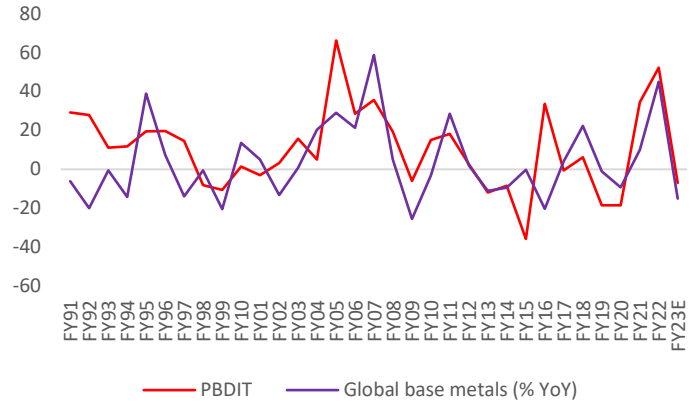
Source: CMIE, Systematix Research, Deflated by WPI manufacturing

Exhibit 38: Machinery industry sales vs global metal prices



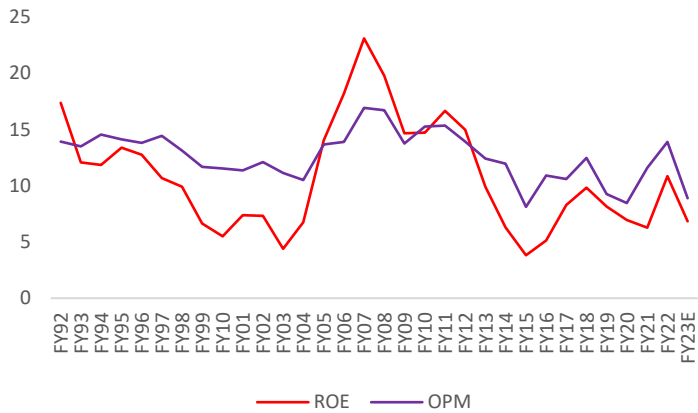
Source: CMIE, Systematix Research

Exhibit 39: Machinery industry sales vs global metal prices



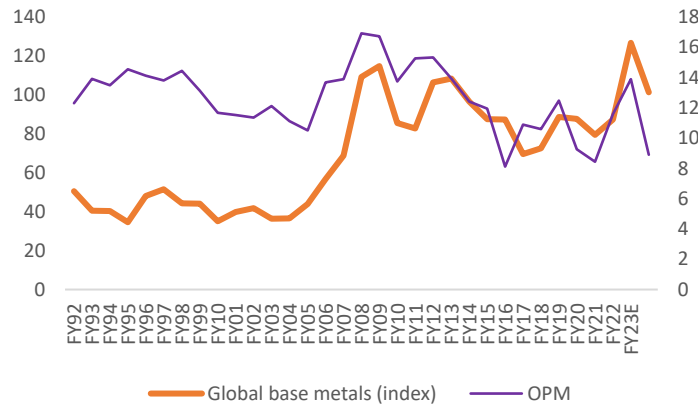
Source: CMIE, Systematix Research

Exhibit 40: Machinery industry, ROE vs OPM



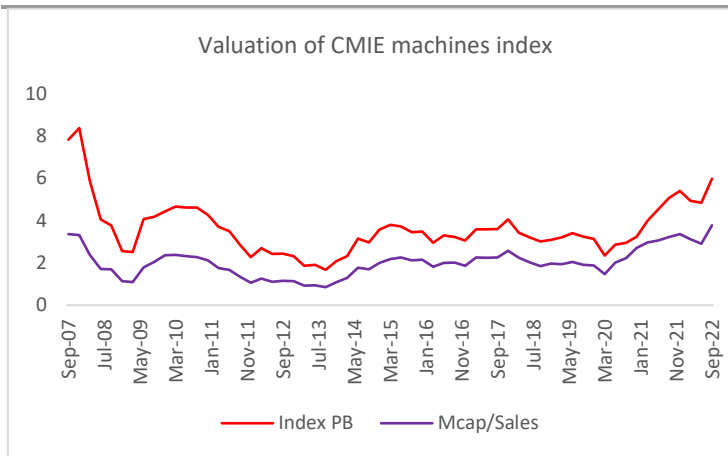
Source: CMIE, Systematix Research

Exhibit 41: Machinery industry, OPM vs global metal prices



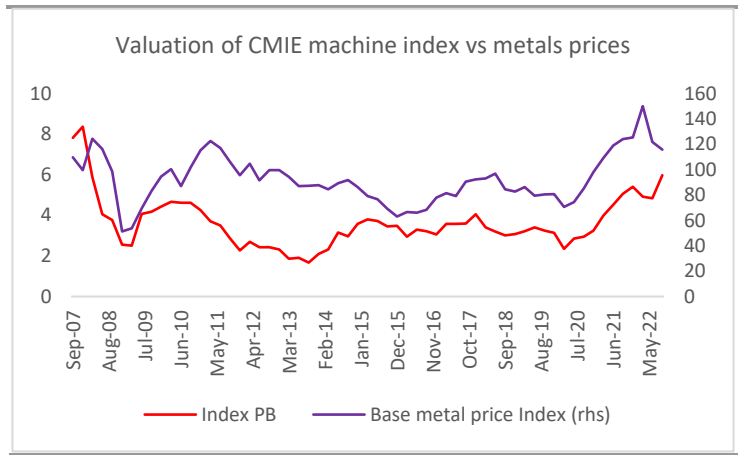
Source: CMIE, Systematix Research

Exhibit 42: Valuations in the machinery sector at the 2007-08 bubble levels



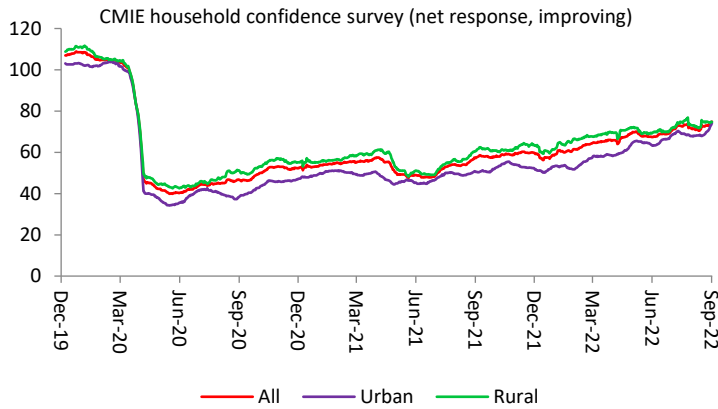
Source: CMIE, Systematix Research

Exhibit 43: Valuations in machine sector driven by disproportionate commodity price surge, which is not correcting



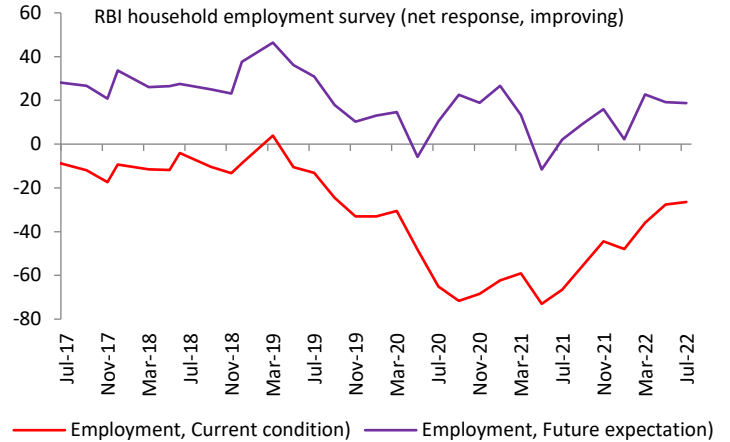
Source: CMIE, Systematix Research

Exhibit 44: India consumer confidence still in improvement mode



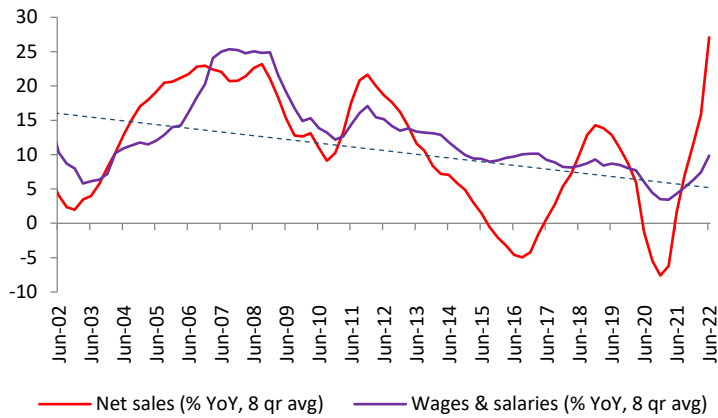
Source: CMIE, Systematix Research

Exhibit 45: Buoyed by improvement in employment condition



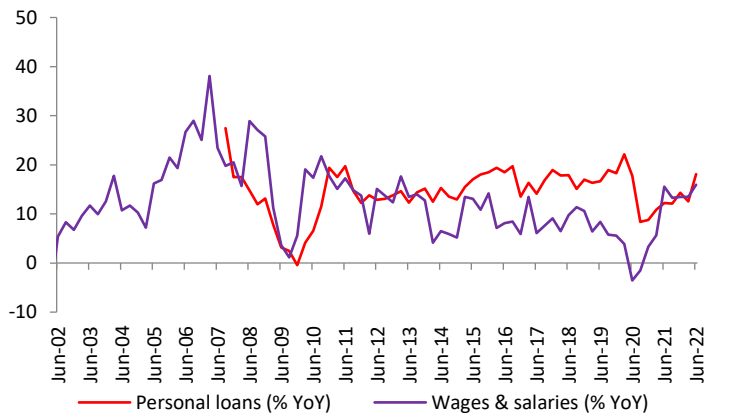
Source: CMIE, Systematix Research

Exhibit 46: Rebound in companies' sales growth leading to faster compensation growth in organised sectors...



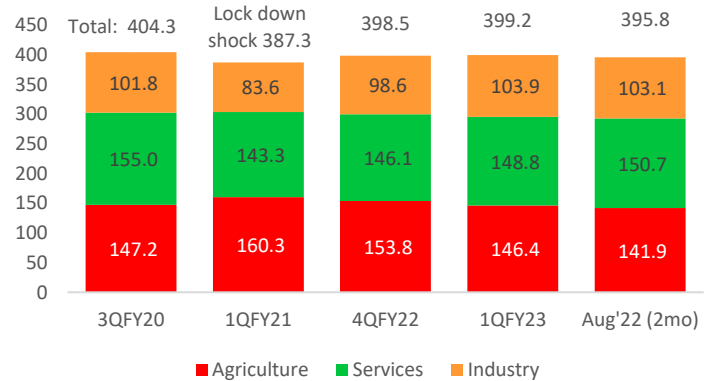
Source: CMIE, Systematix Research

Exhibit 47: ...also stimulating leveraged spending by urban households



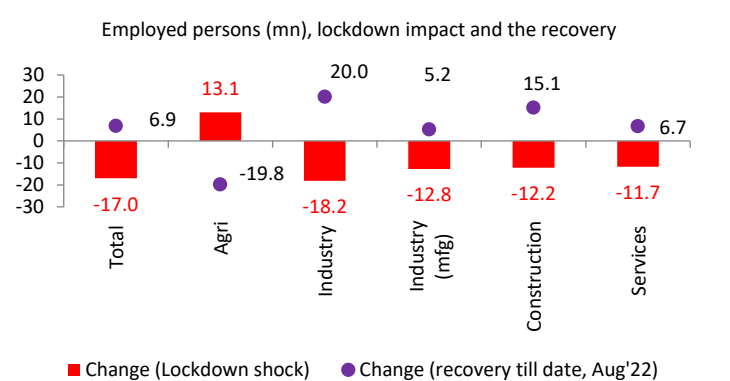
Source: CMIE, Systematix Research

Exhibit 48: Employed persons (mn), recovery from lockdown shock largely in industry, as workers move out of agri



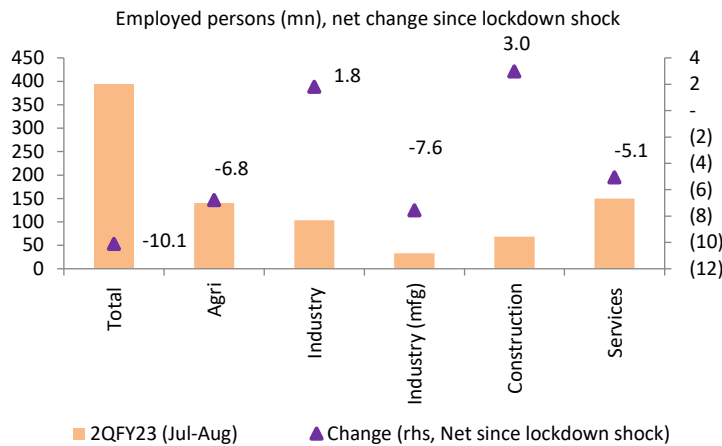
Source: CMIE, Systematix Research; Industry includes manufacturing, construction, mining & utilities

Exhibit 49: Since the lockdown displacements, only 40% of workers got absorbed, larger reversal from agri



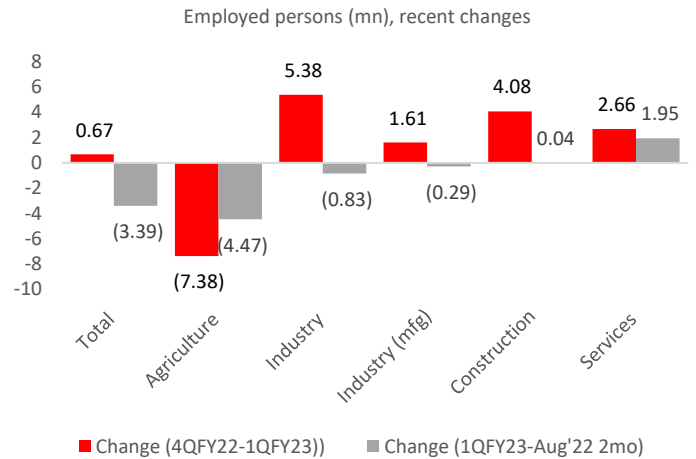
Source: CMIE, Systematix Research; Industry includes manufacturing, construction, mining & utilities

Exhibit 50: Net reversal from agri and displacement from manufacturing & services larger than absorption in construction



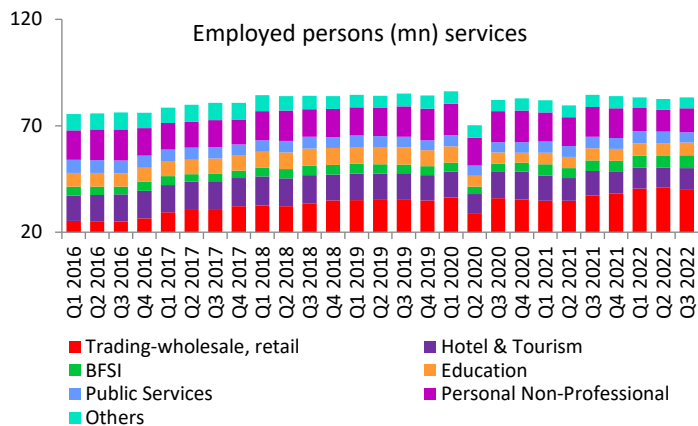
Source: CMIE, Systematix Research; Industry includes manufacturing, construction, mining & utilities

Exhibit 51: Momentum of recovery softened a bit in 2QFY22



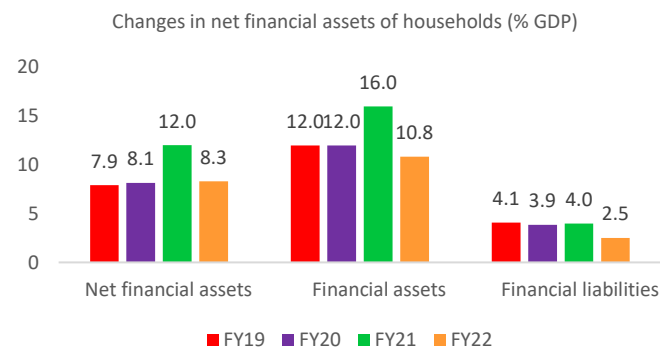
Source: CMIE, Systematix Research; Industry includes manufacturing, construction, mining & utilities

Exhibit 52: Retail & wholesale trade and BFSI recover; personal non-professional and hotels not much



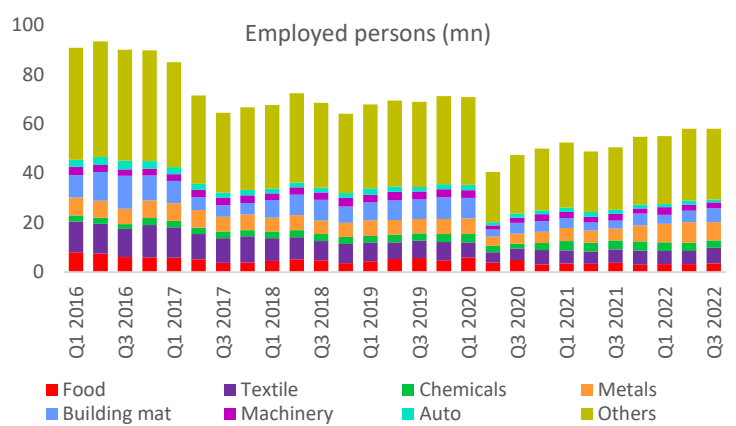
Source: CMIE, Systematix Research, others include health care, media & entertainment, communications, ITES, defense, professional personal services

Exhibit 54: Post pandemic rise in financial assets of HH was episodic, reflecting precautionary savings



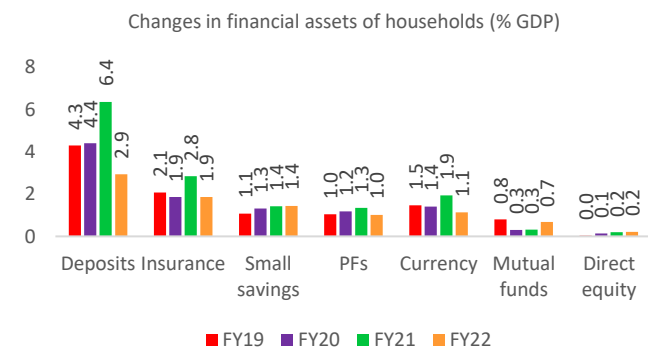
Source: RBI, Systematix Research

Exhibit 53: Manufacturing sector has seen consistent decline in employment



Source: CMIE, Systematix Research, Others includes foot ware & leather, pharma, gems and jewelry, FMCG, and handicrafts

Exhibit 55: Most savings have contracted significantly in FY22, low interest rates also dissuaded deposits

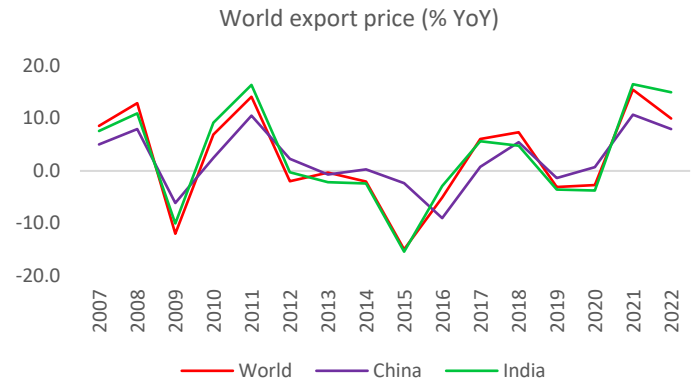


Source: RBI, Systematix Research

Additional Charts and Data

Exhibit 56: Rebound in global exports; volumes rebound after COVID shock, benefitting India and China; likely to slow

Exhibit 57: Bounce in exports despite rise in prices compounded export realisations for EM, India and China

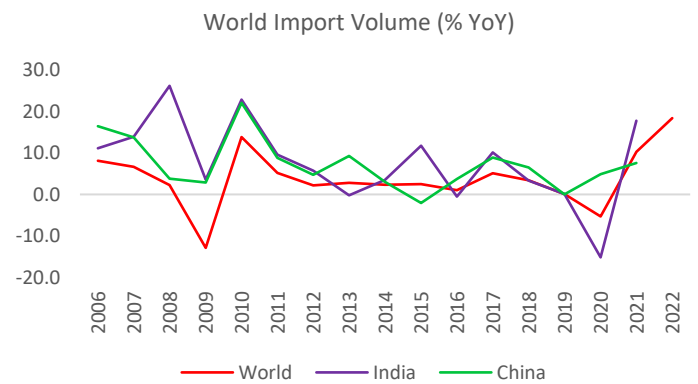
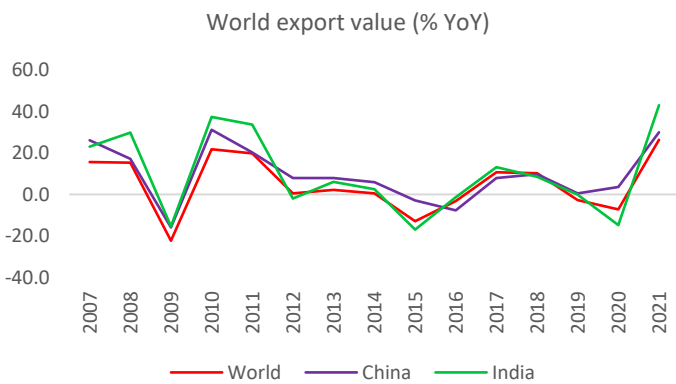


Source: WTO, Systematix Research

Source: WTO, Systematix Research

Exhibit 58: Disproportionate surge in India and China's post-COVID export realisation, following years of subdued growth

Exhibit 59: China averaged higher on imports than India, due to sharp lockdown contraction in India

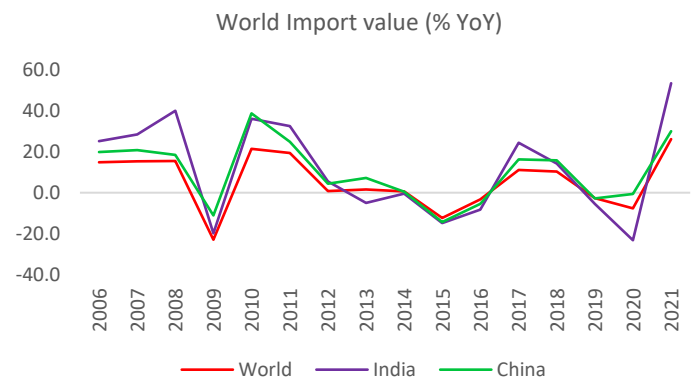
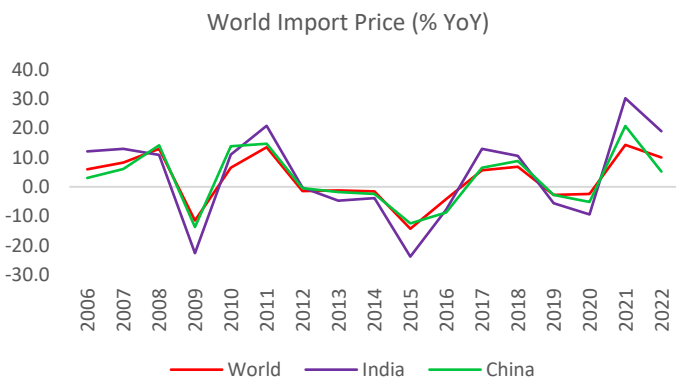


Source: WTO, Systematix Research

Source: WTO, Systematix Research

Exhibit 60: India has seen higher import price impact than China (crude price rise impact)

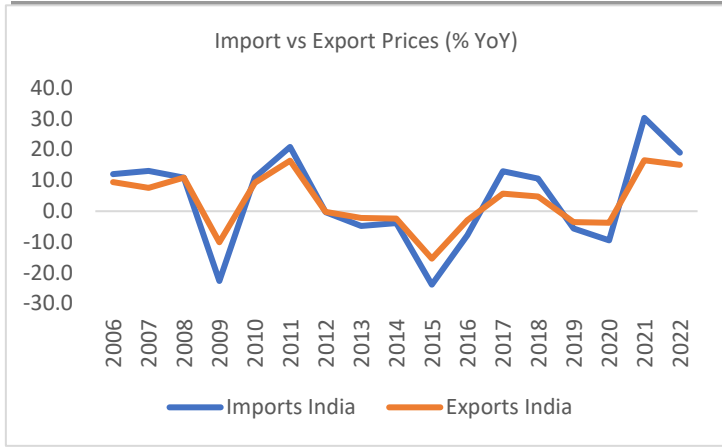
Exhibit 61: Resulting in significant upsurge in India imports, resulting in quick dip in trade deficit



Source: WTO, Systematix Research

Source: WTO, Systematix Research

Exhibit 62: India's import prices rose faster than exports



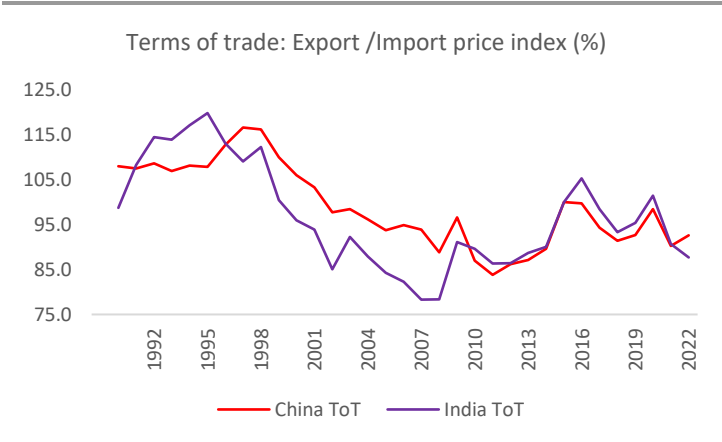
Source: WTO, Systematix Research

Exhibit 63: China's import prices rise relatively less than for India



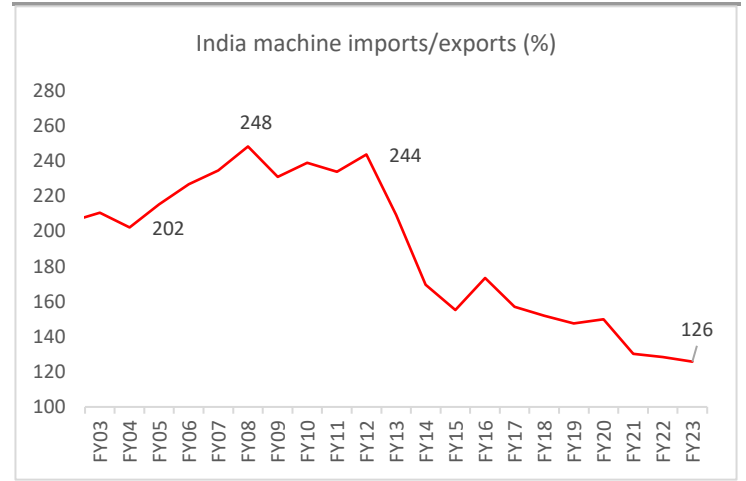
Source: WTO, Systematix Research

Exhibit 64: India's (China's) terms of trade weakened during the high growth phase (1992-2012), but rose in 2015-16 and in 2018, due to the fall in crude prices; this was accompanied by lower growth



Source: WTO, Systematix Research

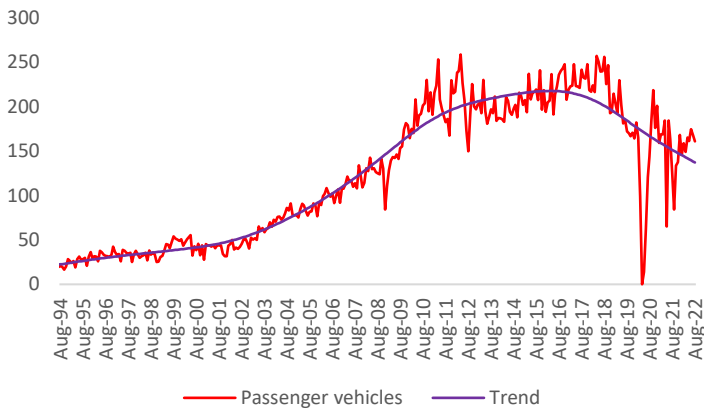
Exhibit 65: Weak domestic private capex has increased dependence of machine-producing Indian companies on exports



Source: WTO, Systematix Research

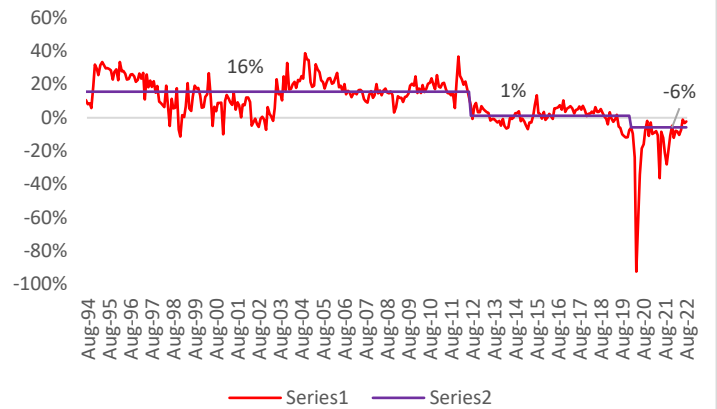
How strong is India's auto sector rebound?

Exhibit 66: Passenger cars (monthly production, SA, '000)



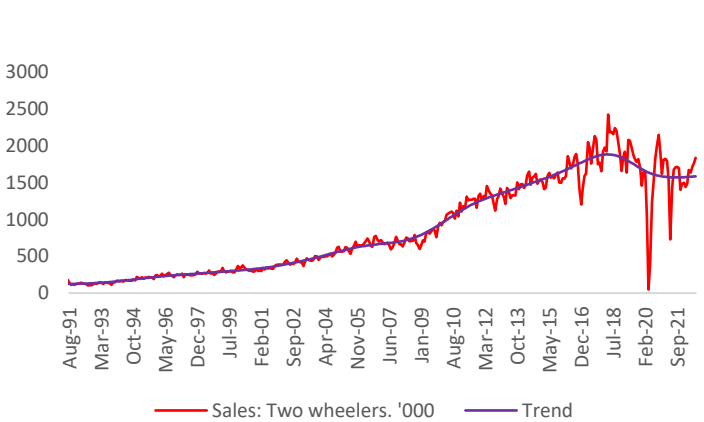
Source: CMIE, Systematix Research

Exhibit 67: Passenger cars (% growth, 3-year CAGR)



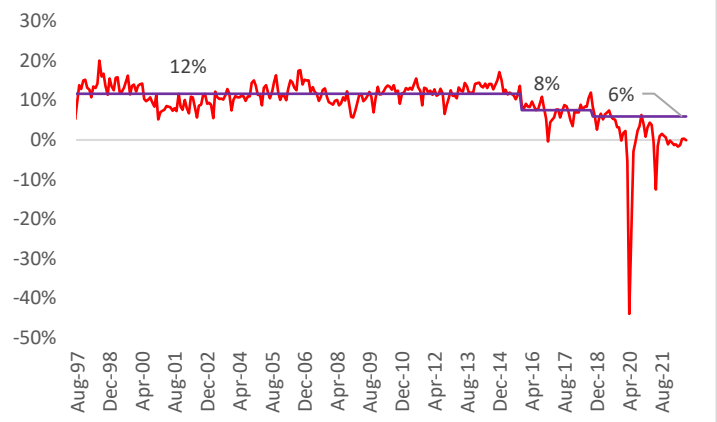
Source: CMIE, Systematix Research

Exhibit 68: Two-wheeler sales (monthly '000, SA)



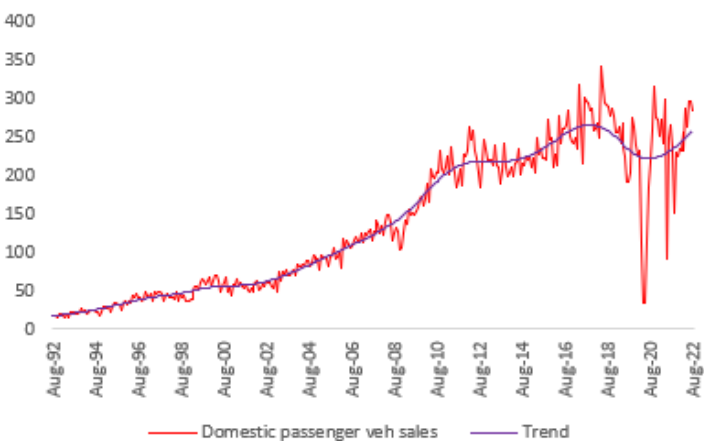
Source: CMIE, Systematix

Exhibit 69: Two-wheeler sales (6 year CAGR)



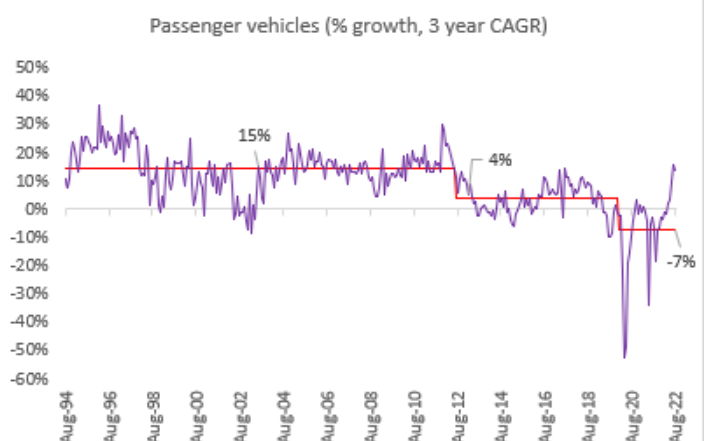
Source: CMIE, Systematix

Exhibit 70: Passenger vehicles (monthly sales, SA, '000)



Source: CMIE, Systematix Research

Exhibit 71: Passenger vehicles sales (% growth, 3-year CAGR)



Source: CMIE, Systematix Research

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