kotak Securities

August 2020

Market Outlook

- Covid 19 situation
- Global growth concerns
- Vaccine progress
- Normal monsoon
- FPI / FII Investments into India
- Earnings growth

Amit Agarwal, CFA
agarwal.amit@kotak.com
+91 22 6218 6439

MARKET OUTLOOK FOR AUGUST 2020

The pandemic and containment measures have impacted global economy in a big way. An overwhelming policy response is helping to mitigate the damage. Also, this is not a business cycle slowdown and recovery. That is why investors are seeing beyond the unprecedented contraction and markets have recovered well before any signs of a rebound in economies. Interest rates are zero or lower at all the major central banks. There is a lot of economic spare capacity which could keep inflation low for some time. This would help central banks to keep rates low, which will keep bond yields low. Globalization was already in reverse before COVID-19 and the virus has only accelerated the anti-globalization trend. European Union leaders have agreed upon an exceptional stimulus package worth USD 860 billion to pull their economy out of the corona black hole. This infusion is in addition to trillions of dollars announced globally especially by US, Japan and EU.

Bourses across the world moved higher in July 2020 on hopes of early availability of a vaccine inspite of unstable economic growth. Another round of shutdowns in a few countries is frightening but hopes of a drug/vaccine are keeping markets upbeat. Gold surged to its lifetime highs crossing USD 1940 per ounce which indicates that the prices of gold is going to remain strong despite decent equity return. Negative real interest rates and global uncertainty is helping gold to move higher. Fresh tension between the US-China and ever increasing number of Covid19 cases is negative for markets.

In India, both Sensex and Nifty have gained in the month of July 2020 on the back of 1) firm global markets, 2) encouraging Q1FY21 earnings so far, 3) expectation of normal to excess rainfall in FY21 with higher Kharif sowing, 4) improvement of high frequency economic indicators from the lows of March and April, 5) surplus trade balance in June 2020, & 5) expectations of further fiscal and monetary policy support and strong flows (both domestic and FPI/FII).

We expect FY21 net profits of the Nifty-50 Index to decline 3.2% and FY22 net profits to grow 38%. We would clarify that FY21E estimates are not very relevant given the impact of Covid pandemic on domestic and global economy, which will result in a sharp decline in both volumes and profitably in many sectors. We would note that the modest decline in net profits in FY21 hides bigger decline in operating profits as FY20 profit was impacted negatively by large adventitious and inventory losses of the downstream oil companies and RIL.

We expect a steep recovery in the net profits of the Nifty-50 Index in FY22 from the low levels of FY21. In particular, we see sharp recovery in net profits of (1) banks due to our assumption of lower provisions in the banking sector in FY22 from high levels of provisions assumed in FY21 to factor in the impact of Covid on finances of households and companies, (2) the metals sectors led by our view of a sharp recovery in global metal prices from current depressed levels and (3) the telecom sector led by our assumption of further increase in ARPUs; current ARPUs are still quite low compared to costs and historical levels.

After the sharp run up Quality non-financial stocks are fully valued on FY22E EPS; Most of them are back to or above pre Covid price levels. Similarly, most growth stocks are also now trading at expensive valuations. The overall risk-reward balance has become unfavorable. Hence one needs to remain cautious on markets from hereon. The wider-than-usual dispersion in valuations between 'growth' and 'value' stocks and contribution of few stocks in market recovery has made it difficult to take a top-down approach. One needs to have a bottoms up approach while selecting stocks. Our updated EPS for Nifty-50 stands at Rs.450 for FY21E and Rs.627 for FY22E. On last week's closing the Nifty-50 is trading at 25x FY21E and 18x FY22E. The one year forward PE of Nifty at 22x looks very expensive.

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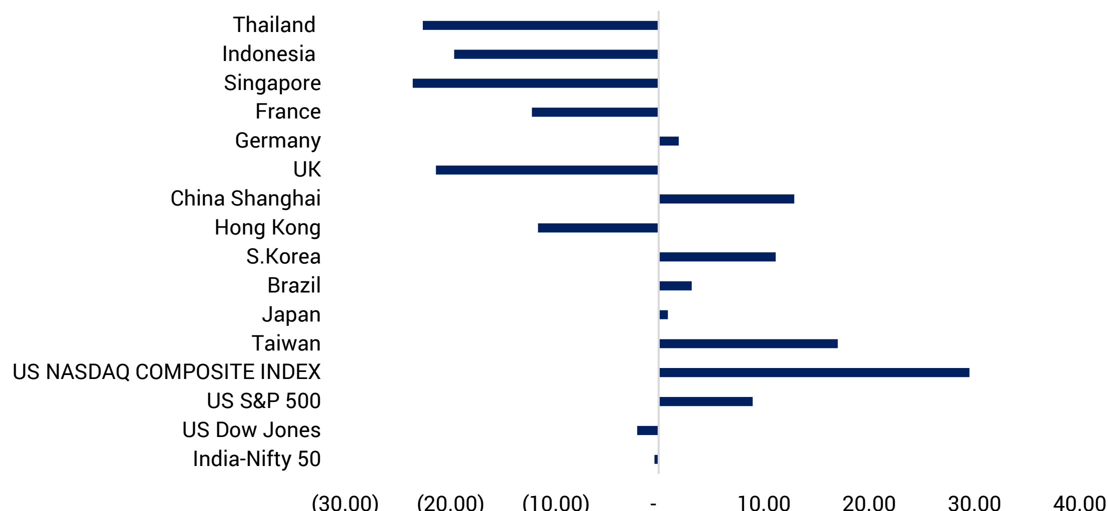
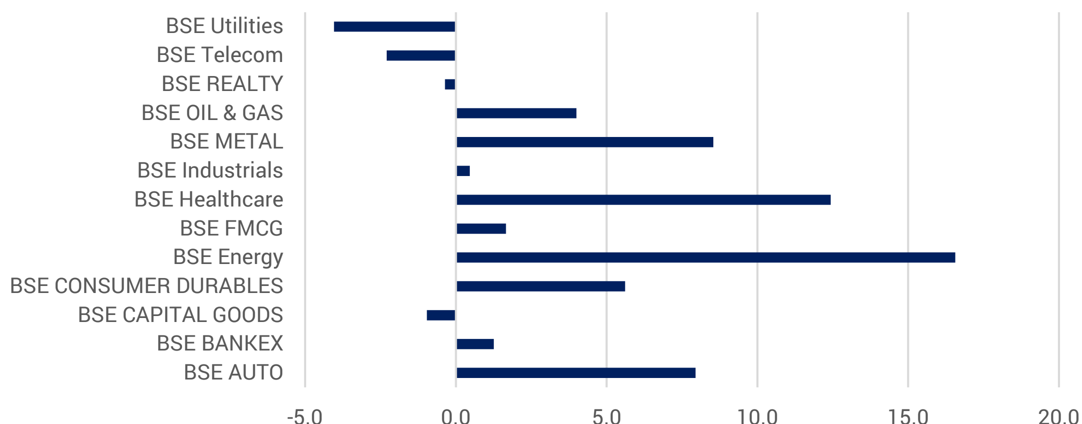
PRIVATE CLIENT GROUP

1-year performance of benchmark global indices



Source: Bloomberg

1-month BSE sectoral performance



Source: Bloomberg

TOP INVESTMENT IDEAS

Company	Rating	Price (Rs) 31 Jul 20	Fair Value (Rs)	Upside/ Downside (%)	Mkt cap. (Rs Cr)	EPS (Rs) FY21E	EPS (Rs) FY22E	EPS growth (%) FY21E	EPS growth (%) FY22E	P/E (x) FY21E	P/E (x) FY22E	P/B (x) FY21E	P/B (x) FY22E	RoE (%) FY21E	RoE (%) FY22E
Axis Bank Ltd	BUY	432	600	38.9	1,22,166	35.1	41.4	509	18	12.3	10.4	1.4	1.3	11.1	11.9
Hindalco Industries	BUY	163	225	38.0	36,839	10.5	20.0	-41	91	15.6	8.2	0.2	0.2	3.9	7.1
ITC Ltd	BUY	194	260	33.9	2,38,681	10.5	12.3	-9	18	18.5	15.7	1.6	1.6	18.9	22.0
Larsen & Toubro Ltd	BUY	913	1,210	32.5	1,28,361	35.3	66.8	-44	89	25.9	13.7	4.0	3.7	7.9	13.1
Mindtree Ltd	REDUCE	1,083	890	-17.9	17,889	54.9	62.5	43	14	19.7	17.3	12.2	10.2	26.2	25.1
Petronet LNG Ltd	BUY	248	300	21.0	37,140	18.7	22.2	6	19	13.2	11.2	1.8	1.7	24.9	27.9
PNC Infratech Ltd^	BUY	133	185	38.7	3,422	12.2	18.7	-12	53	10.9	7.1	1.2	1.0	11.6	15.5
Voltas Ltd	SELL	598	440	-26.5	19,729	10.3	17.8	-37	73	58.1	33.6	6.1	5.6	7.7	12.5

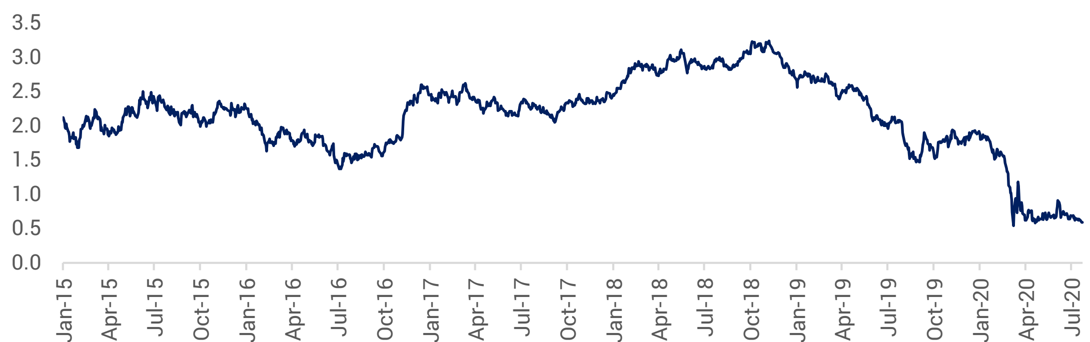
Source: Kotak Institutional Equitites Research, ^ Kotak Private Client Group, For details refer to KIE India Daily report dated 31 July 2020; Note: Earnings season has started and KIE would be changing their earnings estimates, price targets and ratings of above companies as and when their results are out in near future.

INTERNATIONAL MARKETS

Fall in treasury yields

The yield on the benchmark U.S. 10-year Treasury continue to remain at lower levels of ~0.6%, as investors shift their investments to safe sovereign treasuries due to volatile stock market and alternate investments from burgeoning coronavirus crisis. The country has reported the highest number of coronavirus cases in the world — over 4.5 million to date — and more than 150, 000 deaths, according to data compiled by Johns Hopkins University. This news is weighing on the risk sentiment, as more and more businesses are likely to close, as the virus spread continues. Lower interest rates will make it more attractive for businesses to borrow to invest and for households to borrow to spend. Given investment and consumption are the two main pillars of GDP, lower rates usually stimulate economic growth.

Quarterly YoY growth of real GDP in the United States



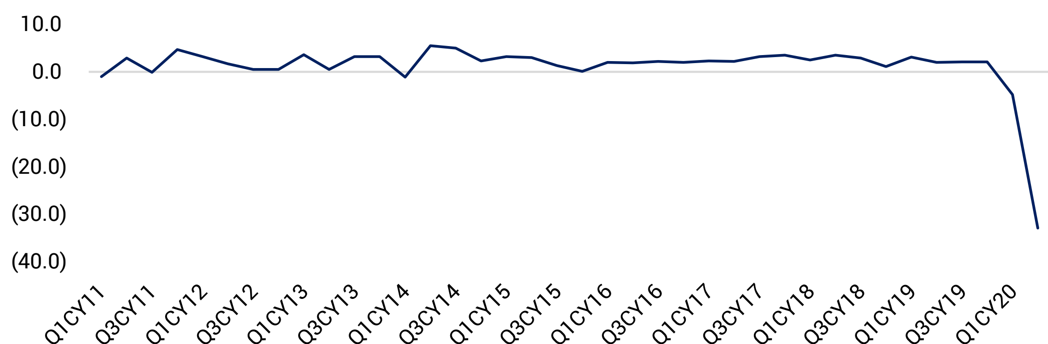
Source: US department of treasury

US GDP slumps 32.9% in Q2CY20

The US economy suffered its worst fall since the Great Depression in CY20 falling 32.9%. This slump more than tripled the previous record of 10% seen in the second quarter of 1958, with a 5% fall for Q2CY20. Most of the decline in activity came in April as the country closed down non-essential businesses and ordered people to stay home as much as possible. The job layoffs during this period drove the unemployment rate to a record 14.7% that month. As the states are no longer under lockdown, the worst economic collapse has likely passed in the US. But the recent surge in Coronavirus cases has complicated the growing recovery.

On July 29th, Federal Reserve left the benchmark interest rate unchanged near zero and again vowed to use all their tools to support the U.S. economy amid a shaky recovery from the coronavirus pandemic.

US GDP contracts 32.9% in second quarter of CY20



Source: www.Statista.com

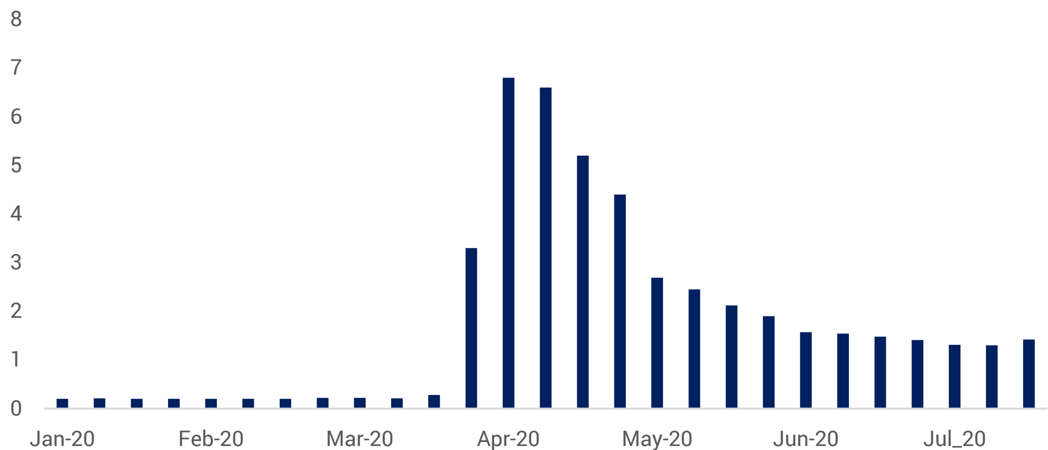
Retail Sales and Weekly Jobless Claims in US

It was 18th straight week in July 3rd week in which initial jobless claims totaled at least 1 million (July third week it was 1.42 million). Peak was in April first week of 6.8 mn jobless claims. Initial jobless claims have risen by more than 45 million since last week of March, 2020. The insured unemployment rate, a basic computation of those collecting benefits vs. the total workforce, fell to 11.2% (from 12.4% in previous week).

Covid19 and lockdown has also impacted retail sales with high increasing retail inventory/sales ratio in US. The total business inventories/sales ratio based on seasonally adjusted data at the end of May, 2020 remains high 1.51. The May 2019 ratio was 1.40 and in April 2020 it was 1.69.

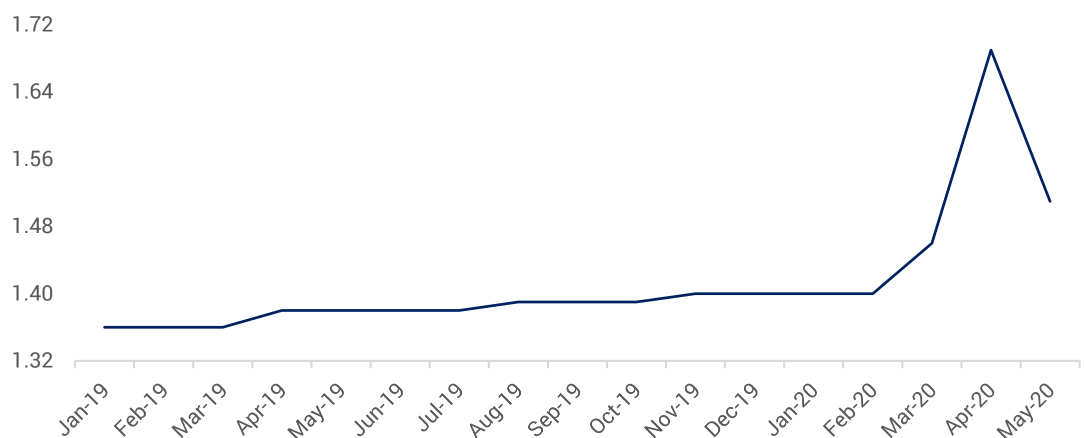
Persistently high jobless claims and weak consumer demand are troubling signs for both workers and the economy.

Weekly Jobless claims in US in 2020 in million



Source: U.S. Bureau of Labor Statistics

US Retail Inventories to Sales Ratio: General Merchandise Stores (x)



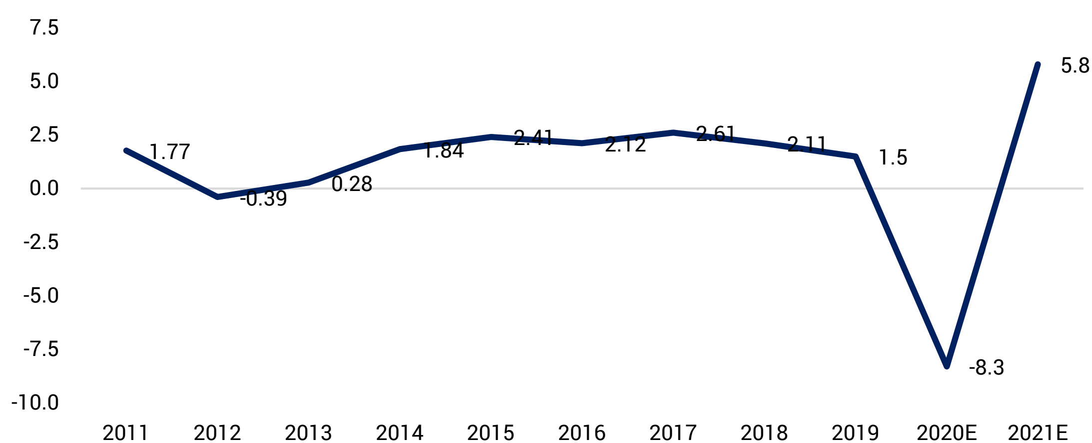
Source:US Census Bureau

European Commission Economic forecast

The EU economy will experience a deep recession in CY20 due to the coronavirus pandemic, despite the swift and comprehensive policy response at both EU and national levels. The European Commission has warned that longer than anticipated coronavirus lockdowns in many countries would cause a significantly deeper recession than previously predicted. The European commission's calculations had worsened as the lifting of containment measures had been more "gradual" than expected at the start of the pandemic with large economies such as Germany reintroducing lockdowns post recurrent outbreaks of Covid-19. European Commission now expects EU gross domestic product to shrink 8.3% this year, a steeper drop than the 7.4% it previously forecasted and the worst on record. However, the IMF has warned that the region could shrink as much as 10.2% in 2020. The commission also lowered its forecast for a potential economic rebound in 2021, estimating growth of 5.8%, down from a previous forecast of 6.1%.

The commissions economic forecasts has increased pressure on political leaders to agree on the recovery fund, which would be instrumental in "significantly boosting the prospects for a synchronized recovery.

European Commission growth forecast in %

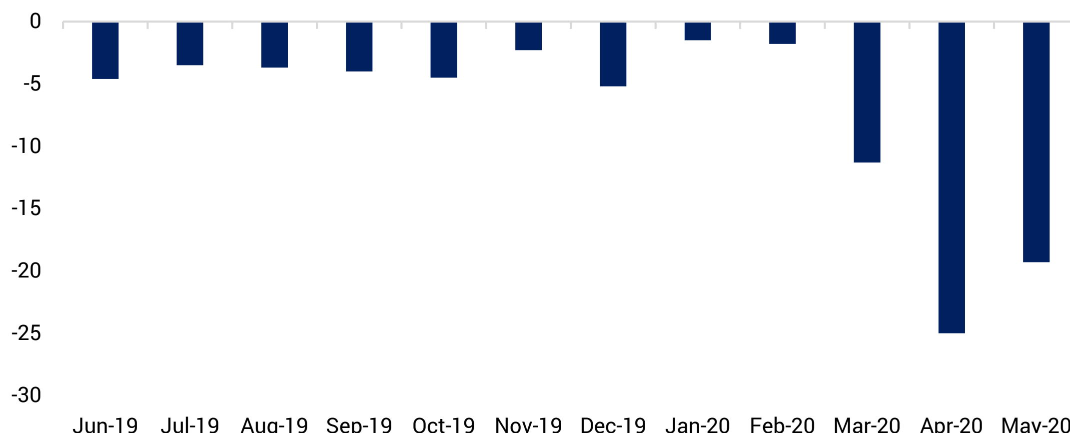


Source: European Commission

German Industrial Production

German industrial production increased sharply in May as restrictions to contain the spread of the coronavirus pandemic eased. Total industrial output–comprised of output in manufacturing, energy and construction rose 7.8% in May 2020 MoM (from April 2020 which reported degrowth of -25.3%) versus forecast of 10% increase. Also, compared with May 2019, total industrial output fell 19.3% in calendar-adjusted terms. The recent data shows that Europe's largest economy is past the worst of the deepest slump in decades, they also point to a long climb back to pre-crisis levels. With its export-oriented economy, Germany's growth is highly dependent on growth in other parts of Europe, Asia and US and also the gravity of dispute between China and US.

Industrial Production in Germany (YoY in %)



Source: Federal statistics office of Germany

Other major European Economies

France

French authorities have reported 400 to 500 active coronavirus outbreak clusters but there are no signs of an imminent “second wave”. France has made the wearing of face masks compulsory in all indoor public spaces, warning of fines for those refusing to comply. From July 20, self-employed worker can now claim up to €1,500 per month from France’s Covid-19 solidarity fund. Up until now, only businesses from certain sectors such as hospitality, restaurants, tourism, culture, events and sports were allowed to claim funds until December 2020. France's parliament has voted to implement a bill intended to protect victims of domestic violence. According to the John Hopkin University, France recorded over 180,000 confirmed cases of COVID-19 till 30th July 2020 and over 30,000 mortalities due to covid19. The fear regarding businesses and employment have rapidly increased since February in France.

United Kingdom (UK)

The UK government has signed deals for access to around 90 million doses of promising coronavirus vaccines under development by leading pharmaceutical and vaccine companies including BioNTech/Pfizer and Valneva. The coronavirus pandemic has had an unprecedented impact on British government borrowing, leading to an estimate of 127.9 billion pounds (US $1,621 billion) for Q2CY20 (more than double over Q2CY19). The UK has allowed quarantine-free international travel to nearly 60 "lower risk countries", excluding India and the US. British Prime Minister Boris Johnson announced 3 billion pounds ($3.8 billion) in funding to help the country's health service cope with a possible second wave of the coronavirus this winter. The Bank of England’s chief economist, Andy Haldane, has insisted that Britain is enjoying a V-shaped recovery (Source: Bank of England) and the economy had recovered about half of the massive fall in output that took place in March and April when the Covid-19 lockdown was most intense. According to the John Hopkin University, UK recorded over 300,000 confirmed cases of COVID-19 till 30th July 2020 and over 45,000 mortalities due to covid19.

ECB opts to wait and see, leaves rates and stimulus program unchanged

The European Central Bank (ECB) in its latest monetary policy meeting left the policy rate unchanged and expects them to remain at their present or lower levels until it has seen the inflation outlook robustly converge to a level close to, but below, 2%. The interest rate on its main refinancing operations stands at 0%, and the interest rates on its marginal lending facility and deposit facility remain at 0.25% and -0.50% respectively.

As per ECB press release and commentary, it will continue its purchases under the pandemic emergency purchase program (PEPP) EUR1.35 trillion. The council will conduct net asset purchases under the PEPP until at least the end of June 2021 and, in any case, until it judges that the coronavirus crisis phase is over. Net purchases under the asset purchase program (APP) will continue at a monthly pace of EUR20 bn, together with the purchases under the additional EUR120 bn temporary envelope.

Key ECB interest rates (%)

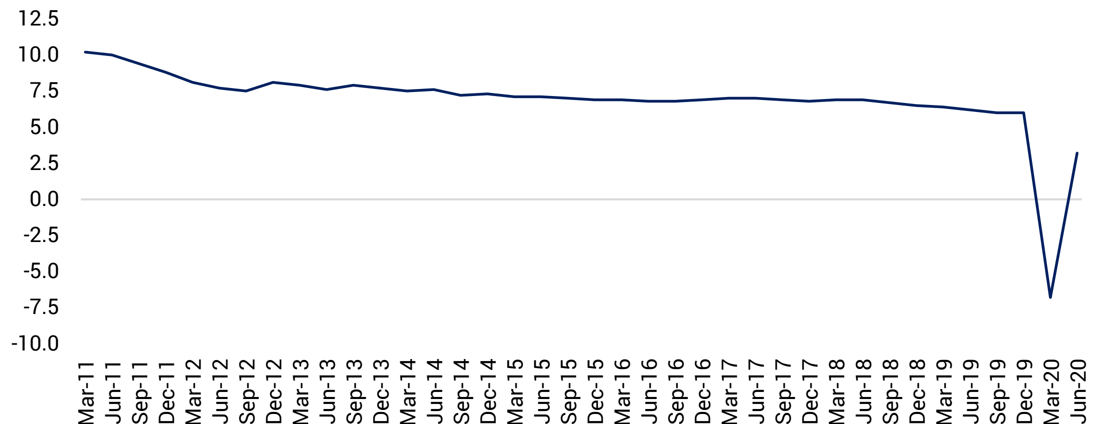
With effect from		Deposit	Main refinancing operations		Marginal
Year	Day	facility	Fixed rate	Variable rate	Lending facility
2019	18 Sep.	−0.50	0.00	-	0.25
2016	16 Mar.	−0.40	0.00	-	0.25
2015	9 Dec.	−0.30	0.05	-	0.30
2014	10 Sep.	−0.20	0.05	-	0.30
	11 Jun.	−0.10	0.15	-	0.40
2013	13 Nov.	0.00	0.25	-	0.75
	8 May.	0.00	0.50	-	1.00
2012	11 Jul.	0.00	0.75	-	1.50
2011	14 Dec.	0.25	1.00	-	1.75
	9 Nov.	0.50	1.25	-	2.00
	13 Jul.	0.75	1.50	-	2.25
	13 Apr.	0.50	1.25	-	2.00
2009	13-May	0.25	1.00	-	1.75
	8 Apr.	0.25	1.25	-	2.25
	11 Mar.	0.50	1.50	-	2.50
	21 Jan.	1.00	2.00	-	3.00

Source: European Central Bank

Chinese GDP grows 3.2% in Q2CY20

China's GDP figures showed growth of 3.2% in the second quarter of CY20, a strong rebound from the first three months of the year (from -6.8%) when the country reported its first contraction since the end of the Cultural Revolution in the mid-1970s. That puts the overall decline for the first half of the year at just 1.6%, an enviable performance compared with most big economies still struggling with the pandemic. The figure of 3.2% GDP growth is higher than experts were predicting and points towards a V-shaped recovery - that is, a sharp fall followed by a quick recovery. It also means China avoids going into a technical recession - signified as two consecutive quarters of negative growth. The Chinese government has been rolling out a raft of measures to help boost the economy, including tax breaks. The numbers are being closely watched around the world with lot of hopes, as all the other countries experience weakness in domestic economy.

Chinese quarterly YoY GDP growth (%)



Source: National Bureau of Statistics of China

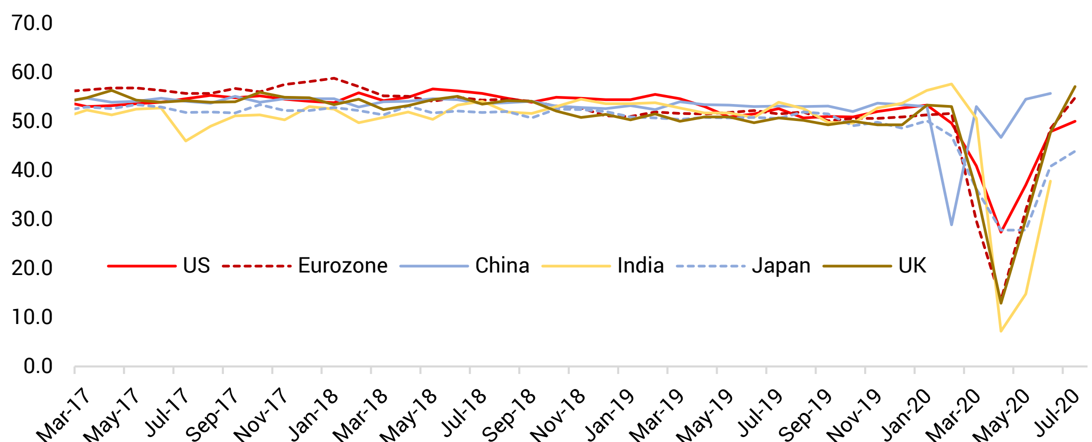
Global June Flash PMIs: Don't get carried away by recovery signs yet

The flash IHS Markit Eurozone Composite PMI rose further in July 2020 from the all-time low of 13.6 seen back in April 2020, climbing from 48.5 in June 2020 to 54.8. Both manufacturing and services returned to growth. Similarly, U.S. Composite PMI Output Index posted 50.0 in July, up from 47.9 in June, signaling a stabilisation in private sector output. However, while the survey's output measures hint at an initial v-shaped recovery, other indicators such as backlogs of work, falling sales, reduction in orders, negative business expectation and employment warn of downside risks to the outlook.

Also, July flash composite PMI data for Japan and UK and final June composite PMI for China and India indicated a marked improvement in business conditions across the private sector economy following the easing of lockdown measures to contain the spread of the coronavirus disease 2019 (COVID-19).

Even with the July rebound there's a long way to go before the output lost to the pandemic is regained and, while businesses grew more optimistic about the year ahead, a V-shaped recovery is by no means assured.

Composite PMI for major economies rebounding

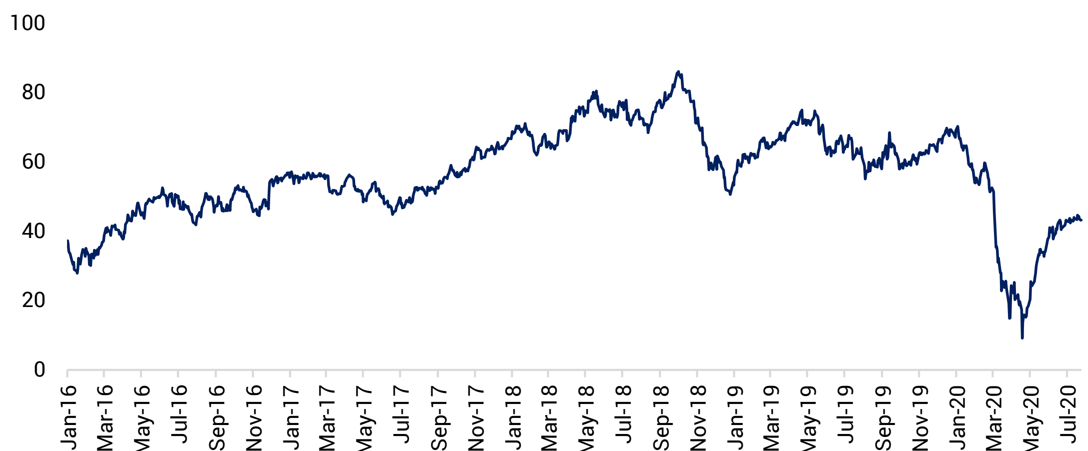


Source: IHSMarkit

Short term energy outlook

International Energy Agency (IEA) raised its demand forecast to 92.1 million barrels per day (bpd) for CY20 by 400,000 bpd in July 2020 from its June outlook. Accelerating number of COVID-19 cases worldwide (especially US), re-start of Libyan exports (adding to the vulnerability of the OPEC+ production restrain), bloated inventories due to the evaporation of demand and mounting tension between the United States and China posed a risk to the outlook of IEA. On the other hand, weaker US dollar, stimulus package of Euro 750 billion in Europe and estimated second stimulus package in US are supportive of the IEA forecast. We are estimating a base case of USD 40/barrel for Brent crude in FY21.

Brent Crude in US$/barrel



Source: Macrotrend.com

Potential coronavirus vaccine lifting market sentiments globally

Vaccine progress

Preclinical testing	142
Stage 1	17
Stage 2	13
Stage 3	5
Approval	0

Source: WHO

Researchers around the world are racing to develop a vaccine against Covid-19, with more than 150 candidate vaccines now tracked by the World Health Organization (WHO). However, there is no data from any human trials showing whether any protective antibody immune response would be strong- and long-lasting enough. One of the reasons for this is “TIME”, as the high-speed development and testing of potential coronavirus vaccines has been underway for barely six months - not long enough to show longevity of any protection they offer. Vaccines normally require years of testing and additional time to produce at scale, but scientists are hoping to develop a coronavirus vaccine within 12 to 18 months.

News from across the globe on potential vaccine progress is lifting broader market sentiment. Currently markets are desperate to latch onto any positive developments in the vaccine field. However, till date we do have any really surprising or significant news on the vaccine. The global race of companies across the globe to develop a vaccine for COVID-19 continues which has claimed over 700,000 lives globally.

How far we are from Covid Vaccine

Country	Firm	Preclinical testing	Stage 1	Stage 2	Stage 3	Approval
India	Zydus Cadila	Done	On			
India	Bharat Biotech	Done	On			
UK	Imperial college London	Done	Done	On		
UK	Astrazeneca & Oxford Univesity	Done	Done	Done	On	
US	Moderna	Done	Done	On		
US	Novavax	Done	On			
Germany	BioNTech,Pfizer & Phosun Pharma	Done	Done	On		
Russia	Sechenov First Moscow & State Medical University	Done	Done	Done	On	
Australia	University of Melbourne & Murdoch Children's Research Institute	Done	Done	Done	On	
Australia	Vaxine Pty Ltd & Meditox	Done	On			
China	Wuhan Institute & Sinopharm	Done	Done	Done	On	
China	Sinovac	Done	Done	Done	On	
China	Cansino Biological & Beijing Institute	Done	Done	On		

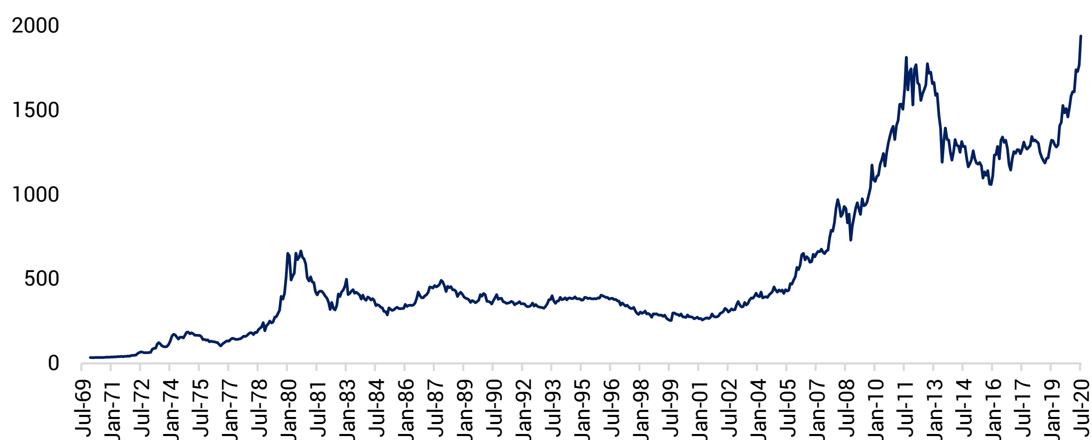
Source: WHO regulatory focus

Gold versus other asset classes

Concerns over the continuous rise in COVID-19 cases, falling 10 year US real yields and weak demand for USD supported gold prices in the month of July. Gold had a remarkable performance in the first seven months of 2020, increasing by ~25% in US-dollar terms. Though equity markets around the world rebounded sharply from their Q1CY20 lows, the high level of uncertainty surrounding the COVID-19 pandemic, ultra-low interest rate environment and investors' need to reduce risk, with the recognition of gold as a hedge further benefited gold underscored by the record inflows seen in gold-backed ETFs.

Investors have embraced gold in 2020 as a key portfolio hedging strategy. Looking ahead, expectations for a faster recovery (V-shaped) from COVID-19 are shifting towards slower recovery (U-shaped), or potential setbacks from additional waves of infections (W-shaped). Regardless of the recovery type, the pandemic will likely have a lasting effect on asset allocation. It will also continue to reinforce the role of gold as a strategic asset.

Gold prices since 1969 in $/ounce



Source: World Gold Council

As per World Gold Council, Gold-backed ETFs (gold ETFs) recorded their seventh consecutive month of positive flows, adding 104 tonnes in June – equivalent to US$5.6bn or 2.7% of assets under management (AUM) – taking global holdings to new all-time highs of 3,621 tonnes. This brings H1CY20 global net inflows to 734 tonnes (US$39.5bn), significantly above the highest level of annual inflows, both in tonnage terms (646 tonnes in 2009) and US-dollar value (US$23bn in 2016).

YTD Gold-Backed ETFs flows data for H1CY20

Region	Total AUM (bn)	Holdings (tonnes)	Change tonnes	Flows (US$bn)	Flows (% Aum)
Asia	5.8	102.2	22.9	1.2	20.69%
Europe	88.7	1560.6	238.5	12.5	14.09%
North America	107.9	1898.4	458.0	24.9	23.08%
Other	3.4	59.6	14.6	0.9	26.47%
Total	**205.8**	**3620.8**	**734.0**	**39.5**	**19.19%**

Source; World Gold Council

DOMESTIC MARKETS

We estimate FY21E GDP growth at -5.8%

The Ministry of Statistics and Programme Implementation in July released quick estimates of the Index of Industrial Production (IIP) which showed the index value at 88.4 in May, 2020 against 53.6 in April, 2020 (and at 135.4 in May, 2019). The NSO continued to point out that the recent IIP readings should not be compared with the pre-pandemic data owing to the disruptions in production caused by the nationwide lockdown. Among the sectors, manufacturing production contracted 39.3%, mining by 21% and electricity production by 15.4%.

IIP prints for May indicate that economic activity started to normalize since the easing of lockdown though June will be a better indicator of the level of reversal in activity. We retain our FY21E GDP growth estimate of -5.8%. The RBI MPC should be comforted by the easing of supply-chain disruptions, which will be favorable for inflation. We reiterate our call of further 25-35 bps of repo rate cuts along with focus on regulatory/liquidity measures.

Sectoral Classification of IIP

	Mining (%)			Manufacturing (%)			Electricity (%)			General (%)		
	2019	2020	2021	2019	2020	2021	2019	2020	2021	2019	2020	2021
April	3.8	5.1	(27.0)	4.9	4.0	(67.1)	2.1	6.0	(23.0)	4.5	4.3	(57.6)
May	5.8	3.2	(21.0)	3.6	2.5	(39.3)	4.2	7.4	(15.4)	3.8	3.1	(34.7)
June	6.5	1.5		6.9	0.2		8.5	8.2		7.0	1.2	
July	3.4	4.9		7.0	4.2		6.6	4.8		6.5	4.3	
August	(0.6)	0.0		5.2	(1.7)		7.6	(0.9)		4.8	(1.4)	
September	0.1	(8.6)		4.8	(4.0)		8.2	(2.6)		4.1	(4.3)	
October	7.3	(8.0)		8.2	(2.3)		10.8	(12.2)		1.8	(4.0)	
November	2.7	1.9		(0.7)	2.7		5.1	(5.0)		8.5	1.8	
December	(1.0)	5.7		2.9	(0.7)		4.5	(0.1)		7.3	0.1	
January	3.8	4.4		1.3	1,8		0.9	3.1		7.5	2.2	
February	2.2	9.6		(0.3)	3.8		1.3	11.5		6.9	5.2	
March	0.8	(1.4)		0.1	(22.4)		2.2	(8.2)		5.3	(18.3)	
Average	2.9	1.5		3.9	(1.1)		5.2	1.1		3.9	(0.6)	

Source: CEIC, Kotak Institutional Equities

We estimate FY21E GDP growth at -5.8%

Components	FY14	FY15	FY16	FY17	FY18	FY19	FY20	FY21E
Real GVA	6.1	7.2	8.0	7.9	6.9	6.6	3.9	(5.8)
Agriculture and allied	5.6	(0.2)	0.6	6.3	5.0	2.9	4.0	2.8
Industry	3.8	7.0	9.6	7.7	5.9	6.9	0.9	(14.5)
Mining	0.2	9.7	10.1	9.5	5.1	1.3	3.1	(4.1)
Manufacturing	5.0	7.9	13.1	7.9	5.9	6.9	0.0	(18.4)
Electricity	4.2	7.2	4.7	10.0	8.6	7.0	4.1	(1.4)
Construction	2.7	4.3	3.6	6.1	5.6	8.7	1.3	(13.1)
Services	7.7	9.8	9.4	8.4	8.1	7.5	5.5	(3.3)
Trade, hotel, transport, communication	6.5	9.4	10.2	7.7	7.8	6.9	3.6	(9.0)
Financial, real estate, professional services	11.2	11.0	10.7	8.7	6.2	7.4	4.6	(10.2)
Real GDP	**6.4**	**7.4**	**8.0**	**8.2**	**7.2**	**6.8**	**4.2**	**(5.8)**

Source: CEIC, Kotak Economics Research estimate

CPI inflation moderates to a three-month low

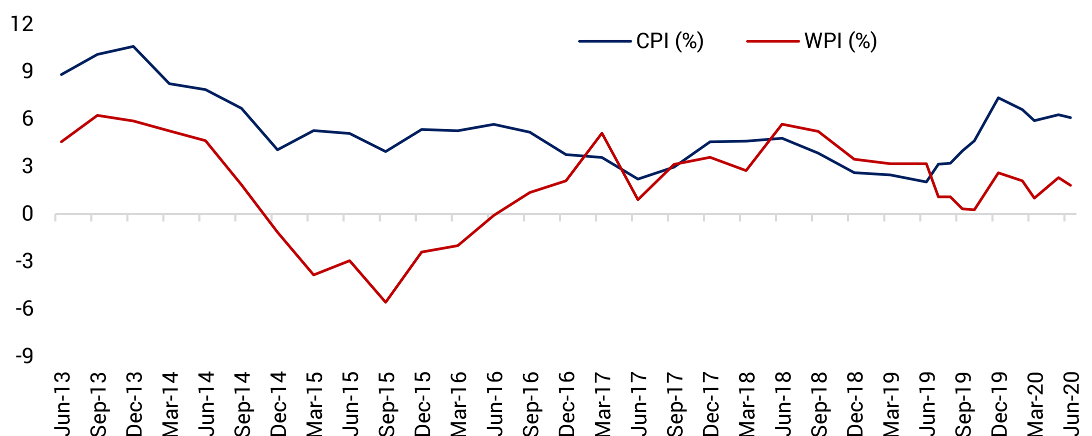
June 2020 CPI inflation moderated to 6.09% as against 6.27% in May amid favorable base effects despite increasing momentum. The softening was led by lower food inflation of 7.9% (9.2% in May) owing to moderation observed across vegetables (1.9% from 5.5% in May), fruits (-0.7% from 2% in May), and sugar and confectionary (4.4% from 6% in May). Though economic activity remains weak, core CPI inflation rose to 5.2% (4.8% in May) owing to higher inflation in the personal care segment (12.4%) and in the transport and communication segment (7.1%). Higher gold prices along with the pass-through of the excise duty hikes on petrol and diesel were the major contributors to core inflation.

On the other hand, June WPI inflation fell by 1.8% as against a fall of 3.2% in May. Food WPI went up by 2% (1.1% in May) led by higher prices of pulses, spices, eggs, meat and fish, and milk. Fuel and power inflation fell by 13.6%.

RBI to continue focusing on unconventional measures

The recent inflation data suggests that CPI inflation has remained above the RBI's upper limit of 6% for the past three months. The trajectory has however been moderating and much of the recent rise in inflation can be attributed to higher fuel and gold prices. We note that the oil prices are now broadly stable and the excise duty hikes have been passed through. Meanwhile, food inflation should continue to normalize as supply restrictions ease. We expect the headline CPI inflation to move back into the RBI's target zone from July and average 4.8% in FY2021 (6% in 1HFY21 and 3.6% in 2HFY21). On the policy front, we believe that the RBI MPC would continue to provide the policy response required to address the demand shock. We expect another 25-35 of repo rate cuts along with liquidity and regulatory measures to address any financial sector dislocations. However, given that the MPC has frontloaded the repo rate cuts in anticipation of benign inflation trajectory in 2HFY21, we believe that scope for further aggressive rate cuts may be limited and would depend on the evolution of growth and inflation.

We expect CPI inflation to average 4.8% in FY21



Source: CEIC, Kotak Economic Research

Covid impact reflects in GST collections

Based on the monthly PIB release, total GST collection was at Rs909 bn for June 2020, Rs620 bn for May and Rs323 bn for April. Gross GST collections in 1QFY21 were at Rs1.85 TN—a contraction of 41% over 1QFY20. June GST collections are a combination of past three months collections and as such should not be read as a normalization of GST revenue trend. (As per the release of 1st August 2020 of the Ministry of finance, the gross GST revenue collected in the month of July, 2020 is Rs.874 bn)

Expect FY21E GFD/GDP at 7.2%

GST collections in June point towards some improvement in economic activity after partial easing of lockdowns. Increase in the number of e-way bills generated also suggests that GST collections could fare better going ahead, but will be well short of the budgeted estimates. The trend in direct and other indirect taxes has so far been disappointing. 3MFY21 fiscal deficit was at 83.2% of FY21BE (Budgetary Estimate). Gross tax collections for 3MFY21 fell by 33% with direct taxes and indirect taxes witnessing a contraction of 30% and 34%. Meanwhile, the government's incremental measures remain within our additional spending expectations. We, therefore, continue to factor in a shortfall of Rs 5 trn in FY21E in overall receipts, Covid-related expenditure of Rs 4 trn (Rs2.7-3.2 trn proposed till now), and expenditure savings of Rs2.7 tn. We retain FY21E GFD/GDP estimate at 7.2% with downside risk depending on the extent of fiscal costs being shifted outside budget and upside risks in case of minimal expenditure cuts

Monthly GST collection (Rs bn)

Month	CGST	SGST	IGST	Cess	Total	Filings (mn)
18-Jun	160	220	495	81	956	6.5
18-Jul	159	223	500	84	965	6.6
18-Aug	153	212	499	76	940	6.7
18-Sep	153	211	501	80	944	6.7
18-Oct	165	228	534	80	1,007	6.7
18-Nov	168	231	497	80	976	7.0
18-Dec	164	225	479	79	947	7.2
19-Jan	178	248	512	87	1,025	7.3
19-Feb	176	242	470	85	972	7.3
19-Mar	204	275	504	83	1,066	7.6
19-Apr	212	288	547	92	1,139	7.2
19-May	178	245	499	81	1,003	7.2
19-Jun	184	253	478	85	999	7.4
19-Jul	179	250	596	86	1,021	7.6
19-Aug	177	242	490	73	982	7.6
19-Sep	166	226	451	76	919	7.6
19-Oct	176	237	465	76	954	7.4
19-Nov	196	271	490	77	1,035	7.8
19-Dec	200	268	481	83	1,032	8.1
20-Jan	209	282	530	86	1,108	8.3
20-Feb	206	273	485	89	1,054	8.4
20-Mar	192	256	445	83	976	7.7
20-Apr	NA	NA	NA	NA	323	NA
20-May	NA	NA	NA	NA	620	NA
20-Jun	190	240	403	77	909	NA

Source: Ministry of Finance, Kotak Institutional Equities

Monthly tax receipts of the Indian government, March fiscal year-ends (Rs bn)

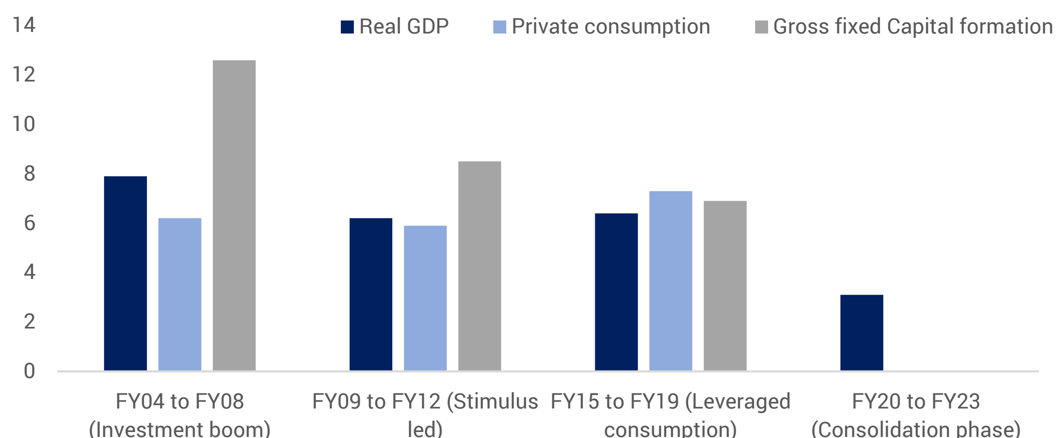
Breakup	Jun-20	Jun-19	May-20	YoY	MoM	Q1FY21	Q1FY20	YoY
Gross tax revenues	**1,436**	**1,858**	**586**	**-23**	**145**	**2,697**	**4,004**	**-33**
Direct taxes	**650**	**1,072**	**74**	**-39**	**780**	**1,193**	**1,707**	**-30**
Corporation tax	372	695	-25	-46	-1,570	542	706	-23
Income tax	264	364	87	-27	202	621	969	-36
Other taxes	13	13	12	0	15	29	32	-7
Indirect taxes	**785**	**784**	**511**	**0**	**54**	**1,501**	**2,292**	**-34**
Customs duty	58	113	56	-48	4	154	395	-61
Excise duty	244	196	109	24	124	353	370	-4
Service tax	9	1	-1	764	-1,523	8	6	16
GST	473	475	346	0	37	986	1,521	-35
CGST	302	354	190	-15	59	550	1,168	-53
IGST	97	40	96	139	0	291	107	172
Compensation cess	75	80	60	-7	24	145	246	-41
Net tax revenues	**1,010**	**1,361**	**124**	**-26**	**712**	**1,348**	**2,514**	**-46**
Non-tax revenues	**44**	**51**	**50**	**-14**	**-13**	**152**	**335**	**-55**
Non-debt capital receipts	27	17	5	62	488	36	48	-25

Source: Ministry of Finance

Consolidation phase-FY20 to FY23E

India's real GDP growth over the next 3-4 years may be a sharp contrast to the growth profile seen over the past 10-15 years. After the periods of investment boom, stimulus-led growth, and leveraged consumption, India will see growth settling down to a more modest pace. Going into the Covid crisis, the economy was already facing headwinds with slowing growth, shrinking fiscal space, NBFCs in crises along with weak corporate and bank balance sheets (though they have been improving gradually). The four broad balance sheets of the economy (financial sector, corporates, government, and households) were already under some stress and the Covid crisis has increased the uncertainty and well as risks of further slippages.

GDP growth is likely to consolidate over FY20 to FY23E (%)



Source: CEIC, Kotak Economics Research estimates

Key sectors to generate the recovery

The government task force had provided a detailed road-map on spending Rs111 trillion over FY20-25 before the pandemic. The table below details the proposed annual spending in each year for various infrastructure sectors. Key sectors such as energy, railways, roads and urban infrastructure account for 72% of the proposed spending.

Energy, railways, roads and urban infrastructure comprise bulk of spending under NIP

Rs bn	FY20	FY21	FY22	FY23	FY24	FY25	FY20 to FY25
Agriculture & food processing	36	39	36	19	12	6	1,687
Airports	187	217	248	213	254	51	1,434
Digital communication	784	618	545	387	381	381	3,097
Energy	2,236	4,415	4,424	4,681	4,978	4,668	26,800
Industrial infrastructure	191	431	448	351	230	105	3,150
Irrigation	1,145	2,006	1,757	1,374	1,153	705	8,945
Ports	134	181	206	159	77	100	1,212
Railways	1,334	2,625	3,088	2,738	2,212	1,679	13,676
Roads	3,326	3,833	3,570	2,528	2,408	3,327	20,338
Rural infrastructure	1,403	1,768	2,108	1,119	1,071	271	7,739
Social Infrastructure	566	783	850	553	461	259	3,934
Urban infrastructure	2,982	4,622	4,041	2,349	2,172	1,599	19,193
Total	**14,321**	**21,538**	**21,323**	**16,471**	**15,408**	**13,151**	**1,11,204**

Source: National Infrastructure Pipeline Report, Kotak Economics Research

India Posts first Trade Surplus in 18 Years

June exports fell by 12.4% to US$21.9 bn (May: US$19.1 bn), but registered a sequential growth of 15% MoM owing to further improvement in economic activity after the lifting of global lockdowns. While June imports contracted 47.6% (4.9% MoM) to US$21.1 bn, reflecting the slump in domestic economic activity. Oil imports fell 55% to US$4.9 bn. Meanwhile, non-oil imports fell by 45% (14% MoM).

FY21E BoP to remain hugely in surplus; USD-INR likely within 74-77.5 in the year ahead

June trade balance registered a surplus as imports continue to contract at a much sharper pace compared to exports, even as lockdown-related restrictions were further eased. This continues to point towards the severe dent to domestic demand. With oil prices likely to remain stable in the current range (average crude oil price of US$40/bbl), we expect FY21 current account to register a surplus of 0.6% of GDP. Meanwhile, the capital account balance may moderate in FY21 owing to the volatile FPI flows. Factoring this, we expect FY21E BoP to stay hugely in surplus at US$59.4 bn. Despite a huge surplus, we expect the RBI to intervene aggressively to avoid a sharp INR appreciation. The INR outlook will also be shaped by extent of global liquidity, US-China trade disputes, India's border issues and the spread of Covid. We continue to expect USD-INR to trade in the range of 74 -77.5 (more likely closer to the lower bound) in the rest of FY21.

Foreign trade for India in US $ bn

Date	Jun-20	Jun-19	May-20	Chg (%) YoY	Chg (%) MoM	Q1FY21	Q1FY20	Chg (%) YoY
Exports	21.9	25.0	19.1	(12.4)	15.0	51.0	81.0	(36.6)
Oil exports	1.9	2.7	1.6	(31.6)	15.0	5.0	12.0	(59.1)
Non - Oil exports	20.0	22.3	17.4	(10.0)	15.0	47.0	69.0	(32.8)
Imports	21.1	40.3	22.2	(47.6)	(4.9)	60.0	129.0	(53.3)
Oil imports	4.9	11.0	3.5	(55.3)	41.4	13.0	35.0	(62.8)
Non - Oil imports	16.2	29.3	18.7	(44.7)	(13.5)	47.0	94.0	(49.7)
Gold imports	0.6	2.7	0.1	(77.4)	698.0	1.0	11.0	(94.0)
Trade Balance	**0.8**	**(15.3)**	**(3.1)**			**(9.0)**	**(48.0)**	

Source: Bloomberg, Kotak Institutional Equities

FY21 Monsoon: moving towards normal rainfall

Till July 28th, cumulative rainfall was 0.5% above long-term average (LTA) with the weekly rainfall 53% below LTA. On a cumulative basis, spatial distribution of monsoon has been normal though over the last few weeks rainfall has weakened in most parts of India, especially north-west India and central India. Out of the 36 sub-divisions across India, till date, seven have received deficient rainfall, 19 have received normal rainfall, and 9 have received excess rainfall.

Seasonal Rainfall Scenario in mm (1st June to 28th July, 2020)

Region	Actual	Normal	% Deviation from LPA
All India	**426**	**424**	**0.5**
East & Northeast India	825	741	11.3
Northwest India	210	265	-20.8
Central India	451	459	-1.7
South Peninsula	396	356	11.2

Source: IMD

Sowing status: much higher than last year's level

As of July 24, the total Kharif acreage was 18% higher than the same period last year. Sowing was late last year due to extremely weak start to monsoon. There is an expectation that farmers will continue to have a bumper crop this year and would drive rural growth.

Sowing much higher than last year's levels, Acreage for major crops, December calendar year-ends (mn hectares)

As on July 24, 2020	2020	2019	Change (%)
Rice	22.2	18.8	18.5
Pulses	10	7.9	25.7
Coarse cereals	13.7	12	14
Oilseeds	16.6	13.4	24.6
Sugarcane	5.2	5.1	1
Jute & Mesta	0.7	0.7	1.5
Cotton	11.8	9.6	22.5
Total	80	67.5	18.4

Source: Ministry of Agriculture, Kotak Institutional Equities

FPIs remain net buyers in Indian equity markets in July, 2020

According to depository's data, FPIs invested Rs 6,141 crore into equities and withdrew Rs1,772 crore from the debt segment on a net basis in July. Globally the scenario is evolving and there are multiple factors which are dictating the direction of foreign flows. On the domestic front, the challenges with respect to rising COVID cases and recovery of economic growth remains and that will continue to be a deterrent for foreign investors. As the earnings season proceeds we could witness more volatility and higher turnover in Indian markets. This coupled with peak valuations could lead to some kind of profit booking by FPIs. The recent appreciation in rupee could also work in favour of FPIs when they are taking out money from India.

Monthly FPI/FII Net Investments in CY20 (up till July 30th)

Month	Equity	Debt	Debt-VRR	Hybrid	Total
January	12,123	-11,648	529	-46	957
February	1,820	2,097	2,637	2,416	8,970
March	-61,973	-60,376	4,165	-19	-1,18,203
April	-6,884	-12,552	4,033	544	-14,859
May	14,569	-22,935	1,000	11	-7,356
June	21,832	-1,545	3,766	1,957	26,009
July	6,141	-1,772	-1,727	0	2,642
YTD	**-12,372**	**-1,08,731**	**14,402**	**4,863**	**-1,01,838**

Source: NSDL

SIP inflows remain strong

Systematic investment plans (SIP) of mutual funds remains stable ~Rs 80 bn mark in the month of June 2020 despite Covid19, uncertainty, slowdown in economic activity and market volatility. In Q1FY21, Central Depository Services Limited (CDSL) added 19.6 lakh investor accounts at an average of ~6.5 lakh accounts per month (versus 3 lakh per month in Q1FY20). We feel strong SIP inflow figures and increased retail participation are a positive indication that investors continue to put faith in the long term prospects of Indian Markets.

Investor Accounts of CDSL (in crore)

Month	Number
Jan-20	2.01
Feb-20	2.06
Mar-20	2.12
Apr-20	2.18
May-20	2.23
Jun-20	2.31

Source: CDSL

Monthly SIP contribution

Rs bn	FY21	FY20	FY19	FY18	FY17
Total		**1,001**	**927**	**672**	**439**
March		86.4	80.6	71.2	43.4
February		85.1	81.0	64.3	40.5
January		85.3	80.6	66.4	41.0
December		85.2	80.2	62.2	39.7
November		82.7	79.9	58.9	38.8
October		82.5	79.9	56.2	34.3
September		82.6	77.3	55.2	37.0
August		82.3	76.6	52.1	35.0
July		83.2	75.5	49.5	33.3
Jun	79.2	81.2	75.5	47.4	33.1
May	81.2	81.8	73.0	45.8	31.9
April	83.7	82.4	66.9	42.7	31.2

Source: AMFI

Not much to read into 1QFY21 results or top-down market valuations

The wide variation in performance of stocks over the past few months, the wider-than-usual dispersion in valuations between 'growth' and 'value' stocks and contribution of a few stocks (largely RIL and INFO) to the market recovery renders any top-down view of the market pointless. We expect earnings of the Nifty-50 Index to decline 1.8% in FY21 and grow 38% in FY22. We estimate Banks, consumer staples, electric utilities and telecom sectors to drive incremental profits of the Nifty-50 Index in FY20-22E.

Break-up of net profits of the Nifty-50 Index across sectors

Sector	Net Profits (Rs bn)			
	FY19	FY20	FY21E	FY22E
Automobiles & Components	211	110	-14	211
Tata Motors	-18	-75	-177	-18
Banks	**405**	**633**	**850**	**1,028**
ICICI Bank	34	79	159	189
State Bank of India	9	145	220	269
Capital Goods	86	89	49	94
Commodity Chemicals	22	26	18	35
Construction Materials	80	89	75	130
Consumer Staples	**213**	**243**	**257**	**306**
Diversified Financials	169	274	197	271
Electric Utilities	**210**	**218**	**246**	**286**
Fertilizers & Agricultural Chemicals	14	18	23	27
Gas Utilities	63	59	43	52
IT Services	706	737	728	819
Media	16	17	13	16
Metals & Mining	292	128	19	200
Tata Steel	104	40	-24	74
Oil, Gas & Consumable Fuels	1,103	716	728	992
Coal India	175	167	126	122
ONGC	296	169	48	91
Reliance Industries	391	396	414	593
Pharmaceuticals	71	77	94	115
Retailing	15	15	9	19
Telecommunication Services	**-1**	**-6**	**61**	**112**
Transportation	41	55	38	44
Nifty-50 Index	**3,715**	**3,499**	**3,435**	**4,755**
Nifty-50 change (%)	**12.8**	**(5.8)**	**(1.8)**	**38.4**
Nifty-50 EPS (FF)	**480.0**	**463.0**	**450.0**	**627.0**

Source: Kotak Institutional Equities estimates

Growth has collapsed- Key growth indicators (YoY, %)

Industry	Jun-19	Jul-19	Aug-19	Sep-19	Oct-19	Nov-19	Dec-19	Jan-20	Feb-20	Mar-20	Apr-20	May-20	Jun-20
Cement production	(1.7)	7.9	(4.9)	(2.1)	(7.7)	4.1	5.5	5.1	7.8	(25.1)	(85.3)	(21.4)	(6.9)
Commerical vehicle sale	(12.3)	(25.7)	(38.7)	(39.1)	(23.3)	(15.0)	(12.3)	(14.0)	(32.9)	(88.1)			
IIP Manufacturing	0.3	4.5	(1.7)	(4.0)	(2.3)	2.7	(0.3)	1.8	3.8	(22.4)	(67.1)	(39.3)	
Rail freight traffic	0.0	(1.3)	(8.7)	(11.2)	(11.1)	(2.8)	(0.2)	(2.7)	3.7	(18.9)	(40.1)	(28.1)	(11.6)
Steel production	5.6	3.4	3.5	2.5	1.0	0.5	0.6	0.2	1.9	0.3	(83.4)	(66.0)	(52.1)
Airport passenger traffic	6.2	1.8	3.9	1.1	4.0	11.2	2.6	2.2	8.9	(33.3)		(97.7)	(83.5)
Passenger Vehicle sales	(17.5)	(31.0)	(31.6)	(23.7)	0.3	(0.8)	(1.2)	(6.2)	(7.6)	(51.0)		(85.2)	(49.6)
Two wheeler sales	(11.7)	(16.8)	(22.2)	(22.1)	(14.4)	(14.3)	(16.6)	(16.1)	(19.8)	(39.8)		(83.8)	(38.6)

Source: CEIC, Kotak Institutional Equities

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PRIVATE CLIENT GROUP

Covid19 Update in India as on 30th July, 2020, improving but long way to go

The Covid-19 situation did not see much change over the past fortnight with (1) recovery rates continuing to improve; (2) fatality rates remaining low and (3) 'active' cases continuing to rise steadily. A few states have regressed with a sharp increase in cases although there is improvement in a few major cities. However, the number of active cases is yet to plateau. Thus, India will have to live through the Covid-19 pandemic with a great deal of uncertainty for longer.

Corona Virus Update in India as on July 30th, 2020

Indicator	Direction	Comments
No of cases in India	Upwards	Number of cases continue to increase, however the growth has come down to 5.2 % from 5.9% in June (doubling rate of 14 days). Total number of active cases as on 30th July has suprassed five lakhs with recovery rate of over 64%.
State wise	Mixed	Some of the states are more heavily affected compared to other states. The mortality rate of Covid-19 varies significantly in different states. Maharashtra most impacted.
Traffic data	Downwards	Road traffic remains lower than 2019 levels. While road traffic is up from the extreme lows of April 2020, the week-on-week change in congestion level was divergent across cities.
Civil Aviation	Weak	The number of departures and the number of people flying remain depressed
Payment data.	Strong	Daily average UPI and IMPS transaction values have recorded an all-time high in July.
Electricity consumption	Low	Covid-19 forced a prolonged lockdown and temporary shutting down of factories. This, in turn, led to lower electricity consumption.Electricity consumption in India, over the seven day period ending July 15, was 7% lower than electricity consumption in the similar period in 2019.
Real Estate and Vehicle Purchase	Weak	The daily average of property registrations in Maharashtra in July 2020 is lower than FY20 and is ~73% of FY19 daily average. Cars and two-wheeler registrations in June were both around 55% of the FY20 average.
Railway/Ports data.	Weak	After increasing in May and June, the daily average freight railway load declined in July. For all major ports, except Kandla, the yoy decline in June was lower than the yoy decline in April and May.
Number of job postings	Improved	Covid-19 has led to hiring freezes as well as involuntary attrition in certain industries. Most industries saw an increase in the number of new job postings in June, when compared to May led by Education, chemicals and FMCG.
Movement of people	Lesser	After plateauing for a while, we saw evidence of risk-averse behavior (people spending more time at home and less time at workplace/grocery shops).
Import duty collection.	Higher	July MTD import duty collections have been strong, compared to May and June collections.
Petroleum product consumption	Improved	The consumption of high-speed diesel in June was above the March consumption level. However, the consumption of petro-products is still well below normal levels (FY20 average).

Source: Kotak Institutional Equities, Ministry of Health and Family Welfare

Loss and Stimulus Option

The Indian economy is expected to have lost around Rs20-28 tn (11-16% of FY20 GDP) due to a 45-60 day lockdown. This is more of a 'production' value while the economic value (including livelihoods lost permanently and population moving into poverty) may be much higher. In the tradeoff between lives and livelihoods, the government imposed long lockdowns to protect the former. However, as economic activity starts returning back to normal, the demands for stimulus will increase. We prefer infrastructure-focused spending to a consumption stimulus, fully acknowledging that economic recovery would be slower but more durable.

SECTORAL SNIPPETS

Automobiles

We believe tractor industry demand should be at the forefront of recovery given record Rabi output supported by higher crop prices and adequate water reservoir levels once the supply chain normalizes. For domestic two-wheeler segment, we expect volume recovery in 2HFY21 led by (1) consumer preference for personal mobility (two-wheeler segment will be the top pick given low per capita income of Indian consumers) and (2) some pick-up in pent-up demand. We believe the domestic CV cycle is likely to bottom out by end of FY21 and revive going into FY22E.

Banks

The extension of moratorium on loan repayment implies that the headline earnings print does not reflect the current status of the business-at-hand. Hence, we are less inclined to give importance to the reported earnings of banks for 1HFY21. Further, we expect several public banks under our coverage (PNB, Canara and Union Bank) to report merged financials which implies volatility is likely to be high for several one-off reasons mostly pertaining to normalizing of account recognition practices, capital position, as we are not aware of the adjustments (mostly pertaining to retirement related expenses) made to net worth to closing balance sheets. With that framework in mind, we expect banks (under coverage) to show steady earnings though we are unsure if banks would step up provisions once more as slippages are likely to be on the lower side. Core performance to be weak as loan growth has slowed to ~6% yoy, which would put pressure on revenue growth, and we expect the decelerating trends to be more visible in retail-oriented loan books.

Cement

With the resumption in activities post the pan-India lockdown in April, demand recovery has been impressive. Demand recovery has been driven by pent-up demand, critical pre-monsoon work and strong rural demand. Strong prices should help offset fixed costs under-recovery in 1QFY21E and keep margins intact. Historically, cement prices correct by in July-September due to seasonality. Variable costs declined partially in June 2020 and were range-bound in July 2020.

Consumer sector

The overall consumption trend continued to be weak. With the Covid-19 outbreak and subsequent lockdown, all segments faced the brunt albeit with varying magnitudes. Discretionary was hit harder with sales coming to a grinding halt for a few names. Even as consumer off-take increased for select staples, disruption in supply chain would have prevented companies from channel up-stocking. However, margin prognosis is positive with benign crude and other RM prices (except dairy). Furthermore, low media intensity, strict control of overhead costs and Ind-AS 116 impact should help reported EBITDA margins, even as operating leverage will be a drag for most names.

Capital Goods

With the country emerging from the lockdown amid a slight recovery in economic activity, it is likely that capex plans will recover from the current lows in the coming months. But unless the pandemic is brought under control, investor sentiment is likely to remain weak. Many firms are struggling to meet current expenses, and have little appetite for fresh investments. Others are likely to conserve cash rather than make new investments till they see signs of a sustained revival in demand. Execution is also likely to be sluggish as labours situation has not eased completely. In the near term, we believe revenue and order intake will remain weak due to 1) restrictions on economic activity and 2) focus of the government and corporates on containing the spread of the Covid-19 virus. Working Capital may go up further, we believe.

Consumer Durables

We expect Consumer Durables demand to recover from its lows in June ending quarter aided by 1) removal of lockdown restrictions 2) pent-up demand and 3) festive season sales. Despite this, demand is likely to remain lower on a y-o-y basis as rising covid-19 cases is delaying normalisation of consumer demand and retail foot-falls. Corporates are likely to cut down on Ad-spends to preserve margins as volumes are likely to remain subdued. Working capital may also get stretched as brands would look to support vendors and channel partners with finance support and timely payments.

Construction sector

The execution of construction projects across India have got impacted due to migration of labour and raw material supply chain issues during Covid-19 led lockdown. The situation is improving on month on month basis but still construction companies are yet to see labour strength at pre-Covid levels. L&T has witnessed improved labour availability in July, but is still lower than its peak during January. Strong monsoon season is also expected to slow down the pace of construction work. KNR is operating at 50-65% labour across its sites and expects normalcy in execution rate post monsoon. Stimulus under Self Reliant India program including project extension up to six months without costs is positive for the construction companies. The imposition of Covid-19 resulted in a delay in awarding of projects, which is expected to pick up in the coming quarters. L&T expects projects pipeline from water, heavy civil, power T&D, building & factories and transportation infra (Source: L&T). We like L&T, KNR Constructions and PNC Infratech in the space.

Building Products

Demand for tiles and plywood is expected to witness gradual improvement going ahead. Segments and / or companies having high exposure to real estate sector could witness sluggish demand in the near term. Given loss of production in 1QFY21 and gradual ramp-up in capacity and gradual recovery demand, we expect the tiles and plywood segment to witness decline in FY21. However, in FY22E, we expect the tiles and plywood industry to witness healthy demand growth.

Gas Utilities

Lower gas prices and all-round development of infrastructure in gas value chain create a conducive environment for the government to undertake much desired reforms in the sector. Deregulation of domestic gas, unified pipeline tariffs, open-access to infrastructure and inclusion in GST can all go a long way in propelling gas consumption in the country. GAIL's dominant presence in the gas value chain makes it our preferred pick to play the theme, while ONGC and OIL can benefit from higher gas realizations, a risk to our negative stance on both. City Gas Distribution (CGD) companies operating as unregulated monopolies may be impacted from the onset of competition.

Pharmaceutical

We expect the domestic formulations segment to show -3% to +5% yoy growth on an underlying portfolio basis, though, the reported numbers will be obscure to some extent by inventory movements, as well as delayed recognition, given the spill-overs from 4QFY20. Also on the US front, we expect revenues to decline for the all the companies given some element of stocking in 4QFY20. We expect RoW businesses to suffer across the board, given the currency headwinds in South Africa and Brazil. We feel management commentary on raw material situation from China and update on Covid 19 challenges will be key factors to monitor.

Life Insurance

Life insurers (HDFC Life, ICICI Prudential Life and SBI Life) reported 29-43% yoy declines in value of new business (VNB) in 1QFY21 on the back of lower Annual Premium Equivalent (APE). Shifting the product mix to non-par/protection expanded margins for ICICI Life and SBI Life while a high non-par base compressed margin for HDFC Life. Other highlights are strong expense management (a combination of pullback in fixed and variable expenses) and lower persistency likely due to a reprieve granted by IRDA.

Information Technology Services

In July'20, Nifty IT Index gave a return of around 22%. Rupee has appreciated by around 0.89% as against USD in July'20. However, we expect rupee to depreciate against USD to 75.5/76/77 in FY21E, FY22E and FY23E, respectively. This will be positive for IT sector. Notably, revenues for all IT companies (except Infosys) saw a swing of 6-7% on a sequential basis in Q1FY21 on the back of supply side impact, cut in discretionary spending and aggressive spending pullback by clients in directly impacted verticals. Infosys bucked the sector trend with a sequential revenue decline of just 2% in c/c basis and reported growth of 1.5% yoy. Infosys is reaping the benefits of investments over the past two years. These investments have helped in driving strong revenue performance in FY20 which shall continue into FY21 and beyond— (1) augmentation of digital capabilities through additional investments and acquisitions aiding process of wallet share gain, (2) large deal wins through greater flexibility in profitability terms, engagement with additional channels and focused central teams, and (3) refined account management processes and additional resources have led to better account mining and growth in large deals and (4) localization which has enabled the company to win deals from companies in the vicinity of development centers.

Real Estate

With the spread of the pandemic, the real estate companies are optimistic of consolidation in the industry. The companies are investing heavily to increase their outreach to customers via digital means and offer attractive schemes. Oberoi management stated that spread of Covid-19 has increased consumer awareness of the need for quality housing, leading to increase walk-ins at its projects as lockdown restrictions lifted in various centres. On the ground, construction labour has begun reporting to sites. As per Oberoi Realty, the company has 60% of its construction workforce available at sites. In commercial real estate, despite the lock-down in 1QFY21, Commercial real estate still holding very low vacancies. Landlords have seen some traction on lease agreements as cost conscious global clients saw an increased pace of office migration to low cost destinations such as India. Embassy REIT was able to see a contracted rental increase of 14% on 1.8 mn sq. ft. of office space across 22 leases in 1QFY21.

Metals and Mining

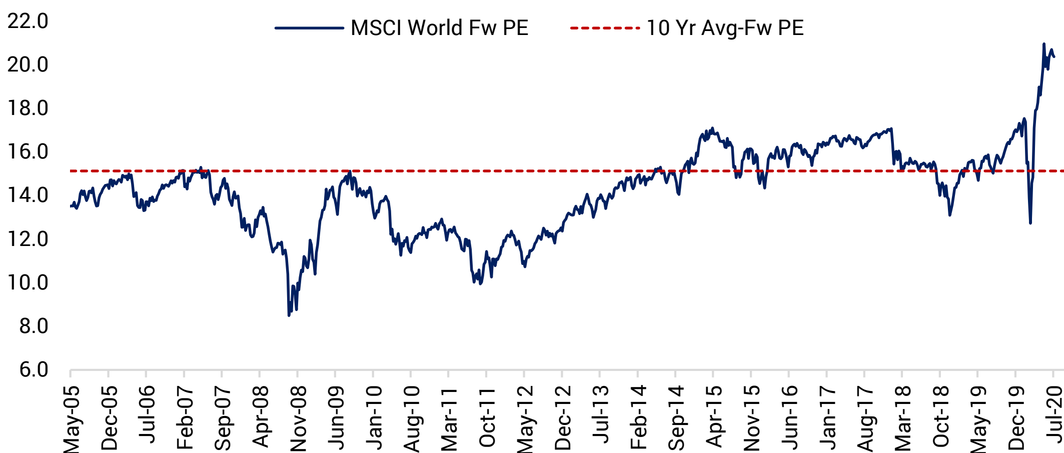
Domestic steel demand tanked in 1QFY21; however, exports helped primary producers to partly offset the impact on volume. Due to higher exports, blended EBITDA/ton declined. We expect steel prices to increase in 2QFY21 led by (1) increase in domestic steel prices – Rs500/ton hike in July 2020 and expect Rs1,000-1,500/ton hike in August 2020, (2) US$15-20/ton higher export prices, (3) higher domestic sales and lower exports. In addition, lower coking coal cost from 2QFY21E should support operating performance.

Telecommunication

Even as telecom services have been relatively more resilient than other parts of the economy, lower recharge activity amongst the low-end subs base and slower LTE net adds on account of the lockdown would mean a bit of a pause in the wireless sector's sequential revenue momentum in 1QFY21.

Based on Bloomberg consensus estimates the Fw PE of MSCI World Index has moved up to 20.4x. Even on CY21E the Fw PE works to 18.3x which is slightly above its previous peaks of last 15 years.

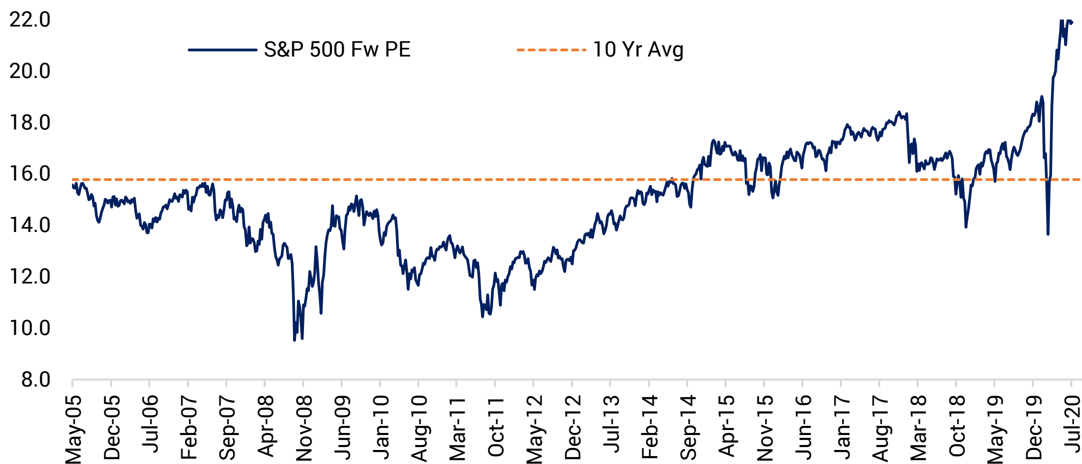
MSCI World Index: Fw PE chart



Source: Bloomberg & Kotak Securities – Private Client Group

Based on Bloomberg consensus estimates the S&P 500 Index is trading at 21.9x on 1 Yr Fw basis. At 19.8x CY21E, it is still higher than its previous peak of last 15 years which works to ~18x

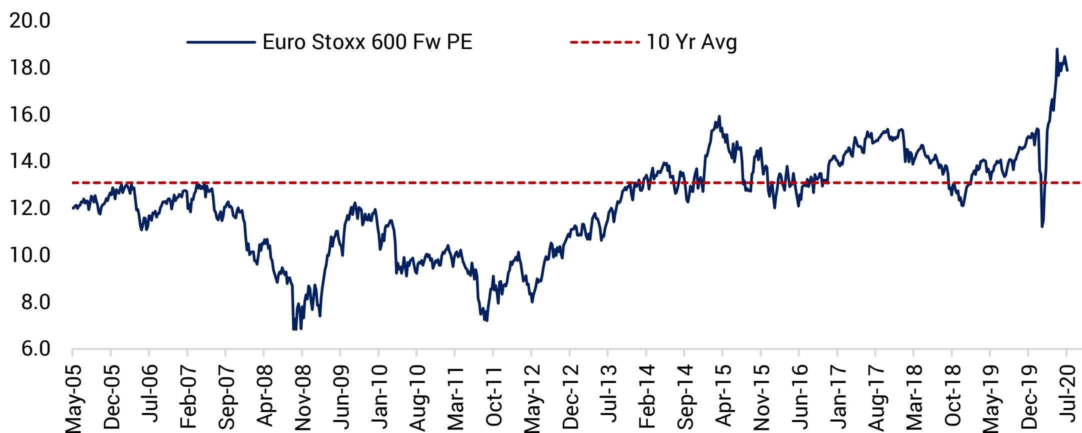
S&P 500 Index: Fw PE chart



Source: Bloomberg & Kotak Securities – Private Client Group

The Euro Stoxx 600 Index, based on Bloomberg estimates trades at 17.9x on 1 Yr Fw basis. On CY21E it trades at 15.9x, which is at par with its 15 year peak of ~16x. The 10 year average of Fw PE works to 13.1x.

Euro Stoxx 600 Index: Fw PE chart



Source: Bloomberg & Kotak Securities – Private Client Group

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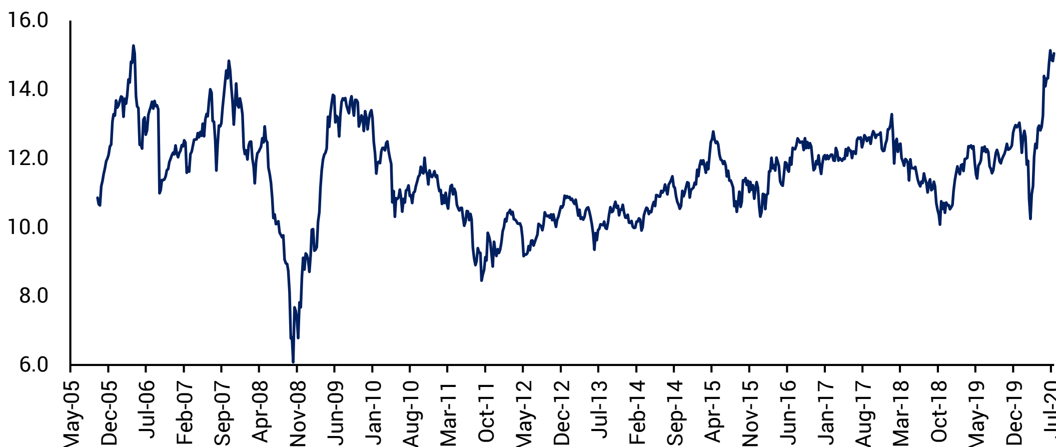
Based on Bloomberg estimates the MSCI EM Fw PE has now touched its 15 year peak of ~15x. In the last 5 years the Fw PE had peaked out at ~13x.

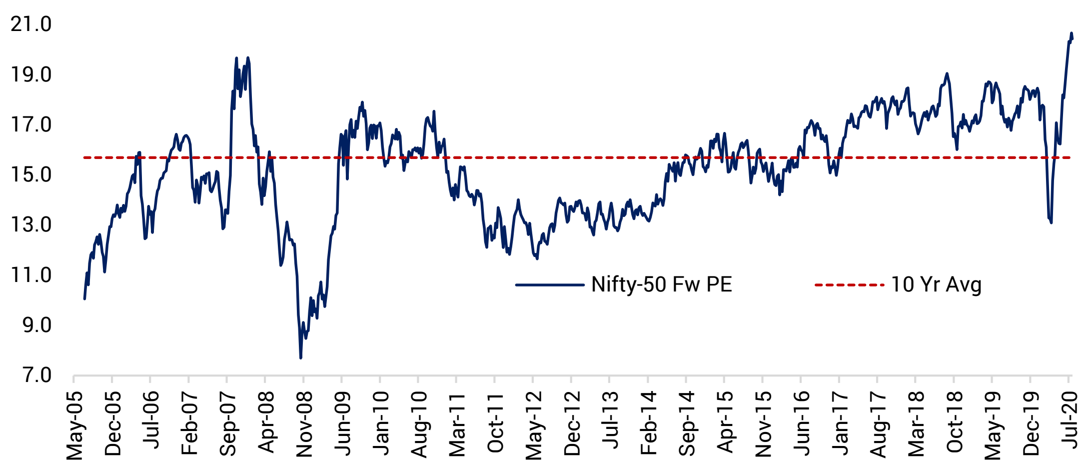
MSCI Emerging Markets: Fw PE chart (on 1 Yr Fw PE basis)



Source: Bloomberg & Kotak Securities – Private Client Group

Based on Bloomberg estimates the Nifty-50 trades at 20.4x on 1 Yr Fw basis. It has even surpassed the 2008 peak of 19.4x on Fw basis. The Nifty-50 Fw PE looks fairly valued on FY22E.

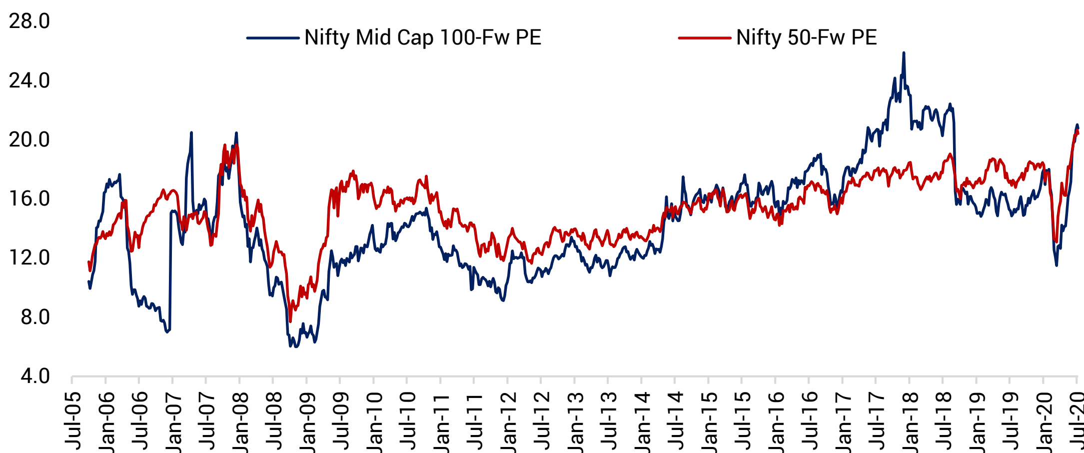
Nifty-50 Index: Fw PE chart



Source: Bloomberg & Kotak Securities – Private Client Group

There is no valuation gap between the Nifty-50 and the Nifty Mid Cap 100 Index. Based on Bloomberg estimates the 1 Yr Fw PE of Nifty-50 works to 20.4x whereas that of Nifty Mid Cap 100 Index works to 20.8x.

One Yr Fw PE chart: Nifty-50 Vs Mid Cap 100 Index



Source: Bloomberg & Kotak Securities – Private Client Group

AXIS BANK

CMP: Rs.432 **Fair Value: Rs.600** **Reco: BUY** **Mkt Cap: Rs.122,166 Cr**

- Axis Bank's Loan growth slowed to 13% yoy in 1QFY21 compared to 16-18% growth over the past few quarters. Share of retail loans in loan books has been on the rise from the past few years. We expect 6.6%, 13.6% & 13.3% loan growth in FY21E, FY22E & FY23E respectively.
- Overall deposits growth was robust at 19% yoy with Saving account (SA) deposits growth of 15% yoy, Current account (CA) deposits growth of 8% yoy in 1QFY21. Current account & Saving account (CASA) ratio is at 40.9% in 1QFY21.
- Revenue growth decline of 1% yoy was driven by 33% decline in non-interest income. Net interest income (NII) grew by 20% and overall Net interest margin (NIM) (reported) declined 15bps qoq to 3.4% in 1QFY21. We expect NII to grow at 11.3%, 14.2% & 9.5% in FY21E, FY22E & FY23E respectively and NIM to remain stable at ~3% by FY22E.
- Gross non-performing loans (GNPL) ratio was marginally lower qoq at 4.7% while net non-performing loans (NNPL) ratio down ~40 bps qoq at a 4 year low of 1.2%. Around 10% of the loans (Previously 25%) are in moratorium book. We expect GNPL to decline to 4.5%, 4.2% & 3.9% in FY21E, FY22E & FY23E respectively and NNPL to rise 1.1%-1.3% throughout FY21E-FY23E.
- While near-term outlook is hazy for all banks, we believe a healthy asset mix, superior customer profile, liability strength and capital comfort will allow Axis Bank to ride this challenging period.
- Currently Axis Bank is trading at 1.25x FY22E book & at a discount to its peers. We maintain our BUY rating with a FV of Rs. 600 (unchanged) valuing the bank at 1.9x book and ~15x March 2022E EPS for RoEs of ~12%.

Note: The above is brief note on the company, based on the research report and update available (dated: 22nd July 2020) on our website at:

https://www.kotaksecurities.com/research_report/recommendation/indiadaily.html

HINDALCO INDUSTRIES LTD

CMP: Rs.163 **Fair Value: Rs.225** **Reco: BUY** **Mkt Cap: Rs.36,839 Cr**

- India EBITDA (including Utkal) of Rs1,260 cr(-9% yoy, +1% qoq) was 9% higher than KIE estimate of led by lower costs in aluminum division and recovery in Copper margins.
- Copper EBITDA increased to Rs300 cr (-18% yoy, 20% qoq), adjusted for Rs100 cr gain from derivative accounting, led by higher value added sales. CC rod sales increased to 73k tons, +4% yoy, with ramp-up of its new plant.
- Aluminum EBITDA (including Utkal) at Rs960 cr or EBITDA/ton of US$421/ton (-5% yoy, -2% qoq) was impacted by 11% yoy lower realization largely offset by 12% yoy lower costs/ton.
- Management expects cost to further decline by 4-5% sequentially in 1QFY21E led by coal, caustic and carbon costs.
- Novelis reported 4QFY20 adjusted EBITDA of US$361 mn (+1% yoy, +5% qoq) led by strong scrap spreads, tight beverage can market and recovery of contractual customer obligations.
- The company completed the acquisition of Aleris for US$2.8 bn in April 2020 and is now working to divest the two assets in FY2021E. KIE estimate FCF of US$176/381 mn in FY2021/22E versus US$384 mn in FY2020.
- Despite the growth capex, HNDL would deleverage in FY2021/22E led by strong FCF generation at Novelis. Net debt/EBITDA peaks at 4.4X in FY2021E and falls to 3.1X/2.7X in FY2022/23E. Maintain BUY given attractive valuation of 4.6X EV/EBITDA (Enterprise Value/Earnings Before Interest, Depreciation and Tax) FY2022E.

Note: The above is brief note on the company, based on the research report and update available (dated: 13th June 2020) on our website at:

https://www.kotaksecurities.com/research_report/recommendation/indiadaily.html

ITC LTD

CMP: Rs.194 **Fair Value: Rs.260** **Reco: BUY** **Mkt Cap: Rs.238,681 Cr**

- Overall 1QFY21 revenues came in at Rs8910 crores, down 21% yoy and 6% above our estimate. EBITDA was reported at Rs2650 crores, down 42% yoy but 10% above our estimate.
- Cigarette revenues declined 29% yoy to Rs3850 crores with a volume decline of around 38% as per our maths. Implied gross realizations improved around ~9% as the impact of price hikes was partly offset by down-trading.
- FMCG revenues grew 10% (12.2% excluding lifestyle retaining) with EBIT growing 61% yoy (EBIT margin of 3.7%). Hotels had a washout quarter while agri and paperboards were weak too.
- The cigarette business getting back to close to normal volume levels in June has dismissed concerns of behavioral changes in tobacco consumption due to extended lockdowns.
- Strong traction in the food and hygiene portfolio should help improve growth in FMCG. The hotels business is likely to have a slow recovery.
- The stock continues to offer a good combination of (1) inexpensive valuations, (2) healthy dividend yield, (3) promise of solid LT growth in FMCG and (4) emerging agri-business. Reiterate BUY with a SoTP-based FV of Rs 260 (from Rs 255).

Note: The above is brief note on the company, based on the research report and update available (dated: 26th July 2020) on our website at:

https://www.kotaksecurities.com/research_report/recommendation/indiadaily.html

LARSEN & TOUBRO LTD

CMP: Rs.913 **Fair Value: Rs.1210** **Reco: BUY** **Mkt Cap: Rs.128,361 Cr**

- Revenue during the Q1FY21 quarter was impacted to an extent of Rs 12000 cr by nationwide lockdowns, labor unavailability and supply-chain disruptions. pipeline remains strong.
- Core Engineering & Construction (E&C) Earnings before Interest Depreciation and Amortisation (EBITDA) for the quarter stood at Rs 760 cr, down 63% yoy and was impacted by negative operating leverage. E&C EBITDA margin of 6.7% was ahead of our estimates on better-than-expected infrastructure segment margins.
- PAT was impacted by sharp decline in EBITDA on lower execution and higher interest cost on incremental borrowings availed during the quarter to enhance liquidity position and take care of near-term repayments.
- Net working capital as percentage of sales has moved up during the quarter on execution slowdown. However, the company has witnessed improved collections from the government, which resulted in improving operational cash flows during the quarter.
- Order book at Rs 3.05 lakh crores was largely maintained at similar levels qoq on fresh inflow of Rs 23600 cr during the quarter from infrastructure, hydrocarbon and heavy engineering. A large part of domestic order book of Rs2.3 lakh crores comes from center and states (50%) and PSUs (32%) indicating comfort on collections.
- Management indicated a strong prospect pipeline of Rs6.3 tn spread across domestic (Rs5.1 tn) and international (Rs1.24 tn), which should start materializing albeit at a slow pace.
- Existing backlog can drive a 25% yoy growth in execution in absence of supply-chain bottlenecks.
- We marginally lower our core E&C estimates by ~4% on account of higher corporate expenses and slightly lower order inflows. This coupled with changes in KIE Fair Value for the listed subsidiaries and roll-forward yields a broadly unchanged SoTP-based Fair Value of Rs1,210 (from Rs1,200 earlier).

Note: The above is brief note on the company, based on the research report and update available (dated: 23RD July 2020) on our website at:

https://www.kotaksecurities.com/research_report/recommendation/indiadaily.html

MINDTREE LTD

CMP: Rs.1083 **Fair Value: Rs.890** **Reco: REDUCE** **Mkt Cap: Rs.17889 Cr**

- Mindtree reported sequential revenue decline of 9.1% to US$25.3 Cr, worse than estimate of 7.4% decline.
- All verticals except communications, media and technology (CMT) declined sequentially with travel & hospitality (T&H) leading the way at 54.6% qoq. Revenues ex-top client declined 15.5% qoq and 16.2% yoy to US$17.7 Cr.
- The top client was the bright spot and grew at 10.5% qoq and 43.7% yoy to US$7.6 cr. However, this has resulted in significant increase in top client concentration to 30% of revenues from 24.8% in 4QFY20 and 20.1% in 1QFY20.
- EBIT margin at 18.2% increased 110 bps qoq despite absorbing additional cost of 30 bps from visas and 60 bps contribution to State Funds for fight against Covid. Two key factors for EBITDA margin increase were—(1) 80 bps from rupee depreciation and (2) 30.2% qoq and 28.6% yoy absolute decline in other expenses with decline in travel, subcontracting costs and other miscellaneous expenses leading the way. Net profit at Rs 213 Cr grew 3.3% qoq and 129.3% yoy.
- Despite sharp rationalization, Mindtree is confident of sustaining margins around 18% in FY2021. The company has guided for sequential margin improvement in 2QFY20.
- Senior management team augmented with new additions. Organizational restructuring in process to enable faster scaling up.
- Strong deal wins TCV on the back of large deal win. Mindtree reported TCV of US$39.1 cr in Q1FY20, a yoy increase of 20.6%. The increase was entirely due to higher renewals.
- High client concentration, risks of business model in transition and high exposure to challenged verticals keep us cautious. We maintain REDUCE with an unchanged FV of Rs890.

Note: The above is brief note on the company, based on the research report and update available (dated: 15th July 2020) on our website at:

https://www.kotaksecurities.com/research_report/recommendation/indiadaily.html

PETRONET LNG

CMP: Rs.248 **Fair Value: Rs.300** **Reco: BUY** **Mkt Cap: Rs.37,140 Cr**

- We are positive on PLNG on account of rising dividend payout, efficient capital allocation, lower volumes/tariffs concern and attractive valuations. We expect PLNG to deliver a healthy 12% CAGR (compound annual growth rate) in earnings over the next 3-4 years driven by higher volumes and tariffs.
- In FY20, PLNG's PBT increased 20% to Rs40.4 bn (excluding Ind-AS 116 impact) led by 10% higher volumes at 1.81 Cr tons and 10% rise in gross margins despite including provisional ~20% cut in Kochi tariffs to Rs79/mn BTU.
- Dividend payout increased to Rs.12.5 (71%) in FY20 from Rs10 in FY19. The management allayed concerns on tariffs (1) proposed tariffs at Kochi will yield threshold IRR and (2) no material risks to tariffs or volumes at Dahej given its contractual terms. We expect gradual ramp-up in volumes driven by increase in utilization of Kochi post commissioning of pipeline.
- PLNG has laid out a medium-term roadmap to facilitate setting up of LNG retail outlets (ROs) along the major highways.
- We maintain BUY rating on PLNG with DCF-based FV of Rs. 300 noting strong earnings growth, reasonable valuation and high FCF/dividend yield of 6-8% pending final decisions on large investment proposals.

Note: The above is brief note on the company, based on the research report and update available (dated: 1st July 2020) on our website at:

https://www.kotaksecurities.com/research_report/recommendation/indiadaily.html

PNC INFRATECH LTD

CMP: Rs.133 **Fair Value: Rs.185** **Reco: BUY** **Mkt Cap: Rs.3422 Cr**

- PNC Infratech Ltd (PNC) is present in the business of construction and infrastructure development with expertise in highways, bridges, flyovers, airport runways, development of industrial areas, etc. The company has a long history in the Indian road sector and secured a contract from the first 10 tenders of NHDP in 1999.
- PNC has strong order book of ~ Rs 15000 cr which is 3.1 times FY20 revenue. The current order book gives strong revenue visibility for the next two to three years. In addition, the company targets to add ~Rs 7000 cr of order inflows in FY21.
- PNC is focusing on construction projects in the roads sector. As per management, the new projects are expected in second half of FY21 based on schedule of tenders.
- PNC has strong balance sheet with net cash of Rs 420 cr at standalone level at the end of FY20 and has asset monetization plans which will help in meeting future capital requirement for growth.
- PNC has incurred Rs 78 cr of new capex in FY20 and targets to do capex of Rs 70-75 crore in FY21E in order to execute its orders. Based on current gross block of ~Rs 1100 cr, it can execute over ~Rs 7000-8000 cr of work on its own in a year.
- In our view, the company's robust order backlog, strong execution track record, net cash balance sheet in construction business and long term growth opportunity in the sector gives comfort for maintaining growth in its financials on a long term basis.
- We have BUY rating on the stock with target price of Rs 185. Key risk to our estimates and recommendation are any further negative impact of COVID-19 on construction of highways, slowdown in road capex, delay in approvals of projects, etc.

Note: The above is brief note on the company, based on the research report and update available (dated: 29th June 2020) on our website at:

https:// https://www.kotaksecurities.com/ksweb/ResearchCall/Fundamental.

VOLTAS LTD

CMP: Rs.598 **Fair Value: Rs.440** **Reco: SELL** **Mkt Cap: Rs.19,729 Cr**

- High inventory build-up may mean weak 1HFY21 Unitary Cooling Products (UCP) revenues. We believe revenues in 1HFY21 may thus be tepid with fresh dispatches reviving only possibly around the festive season.
- Lots of inventory bought by everyone in 4QFY20 anticipating shortfall in product supply on account of perceived China supply chain issue. Now that sales have suffered, many brands are giving large discounts.
- Capital employed by the UCP segment has increased in FY2019 (on account of weak demand due to a weak summer season) as well as FY2020 (weak March dispatches on account of Covid).
- EMP (Electromechanical projects) segment may remain adversely impacted in FY2021 as there may be delays in execution of both international orders (tighter finances led by weak oil prices) as well as domestic orders (tighter government finances). There may also be delays on account of delayed mobilization of resources and labor.
- Post lockdown reopen, remobilization of workforce is a big challenge. Some delay in execution and collection is inevitable.
- Excess capacity and weak export outlook have been challenging for the textile sector. Voltas is focusing on after sales service and that has offset low textile machinery demand.
- FY2021 revenues may be negatively impacted on account of low demand and high inventory build-up. We cut FY2021/22E EPS by 16%/5% respectively.
- We revise down our revenue estimates for FY2021-22 by 7-8% as we bake in lower revenues for both EMP and UCP segments. UCP remains a good play given long-term growth potential of this segment. We remain cautious on near-term uncertainties on discretionary demand as well as EMP segment order execution. SELL stays with a revised fair value of Rs440 (Rs455 earlier).

Note: The above is brief note on the company, based on the research report and update available (dated: 2nd June 2020) on our website at:

https://www.kotaksecurities.com/research_report/recommendation/indiadaily.html

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PRIVATE CLIENT GROUP

Rating Scale (Kotak Securities – Private Client Group) / Kotak Institutional Equities

Definitions of ratings

BUY – We expect the stock to deliver more than 15% returns over the next 12 months

ADD – We expect the stock to deliver 5% - 15% returns over the next 12 months

REDUCE – We expect the stock to deliver -5% - +5% returns over the next 12 months

SELL – We expect the stock to deliver < -5% returns over the next 12 months

NR – **Not Rated.** Kotak Securities is not assigning any rating or price target to the stock. The report has been prepared for information purposes only.

SUBSCRIBE – We advise investor to subscribe to the IPO.

RS – **Rating Suspended.** Kotak Securities has suspended the investment rating and price target for this stock, either because there is not a Sufficient fundamental basis for determining, or there are legal, regulatory or policy constraints around publishing, an investment rating or target. The previous investment rating and price target, if any, are no longer in effect for this stock and should not be relied upon.

NA – **Not Available or Not Applicable.** The information is not available for display or is not applicable

NM – **Not Meaningful.** The information is not meaningful and is therefore excluded.

NOTE – Our target prices are with a 12-month perspective. Returns stated in the rating scale are our internal benchmark.

Fundamental Research Team (Private Client Group)

Rusmik Oza
Head of Research
rusmik.oza@kotak.com
+91 22 6218 6441

Arun Agarwal
Auto & Auto Ancillary
arun.agarwal@kotak.com
+91 22 6218 6443

Amit Agarwal, CFA
Transportation, Paints, FMCG
agarwal.amit@kotak.com
+91 22 6218 6439

Priyesh Babariya
Research Associate
priyesh.babariya@kotak.com
+91 22 6218 6433

Sanjeev Zarbade
Cap. Goods & Cons. Durables
sanjeev.zarbade@kotak.com
+91 22 6218 6424

Jatin Damania
Metals & Mining, Midcap
jatin.damania@kotak.com
+91 22 6218 6440

Purvi Shah
Pharmaceuticals
purvi.shah@kotak.com
+91 22 6218 6432

K. Kathirvelu
Support Executive
k.kathirvelu@kotak.com
+91 22 6218 6427

Sumit Pokharna
Oil and Gas, Information Tech
sumit.pokharna@kotak.com
+91 22 6218 6438

Pankaj Kumar
Midcap
pankajr.kumar@kotak.com
+91 22 6218 6434

Krishna Nain
M&A, Corporate actions
krishna.nain@kotak.com
+91 22 6218 7907

Technical Research Team (Private Client Group)

Shrikant Chouhan
shrikant.chouhan@kotak.com
+91 22 6218 5408

Amol Athawale
amol.athawale@kotak.com
+91 20 6620 3350

Siddhesh Jain
Research Associate
siddhesh.jain@kotak.com
+91 22 62185498

Derivatives Research Team (Private Client Group)

Sahaj Agrawal
sahaj.agrawal@kotak.com
+91 79 6607 2231

Malay Gandhi
malay.gandhi@kotak.com
+91 22 6218 6420

Prashanth Lalu
prashanth.lalu@kotak.com
+91 22 6218 5497

Prasenjit Biswas, CMT, CFTe
prasenjit.biswas@kotak.com
+91 33 6625 9810

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Kotak Securities Limited. Registered Office: 27 BKC, C 27, G Block, Bandra Kurla Complex, Bandra (E), Mumbai 400051. CIN: U99999MH1994PLC134051, Telephone No.: +22 43360000, Fax No.: +22 67132430. Website: www.kotak.com/www.kotaksecurities.com. Correspondence Address: Infinity IT Park, Bldg. No 21, Opp. Film City Road, A K Vaidya Marg, Malad (East), Mumbai 400097. Telephone No: 42856825. SEBI Registration No: INZ000200137 (Member ID: NSE-08081; BSE-673; MSE-1024; MCX-56285; NCDEX-1262), AMFI ARN 0164, PMS INP000000258 and Research Analyst INH000000586. NSDL/CDSL: IN-DP-NSDL-23-97. Our research should not be considered as an advertisement or advice, professional or otherwise. The investor is requested to take into consideration all the risk factors including their financial condition, suitability to risk return profile and the like and take professional advice before investing. Investments in securities market are subject to market risks, read all the related documents carefully before investing. Derivatives are a sophisticated investment device. The investor is requested to take into consideration all the risk factors before actually trading in derivative contracts. Compliance Officer Details: Mr. Manoj Agarwal. Call: 022 - 4285 8484, or Email: ks.compliance@kotak.com.

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