श्री LAKSHMISHREE

Gateway to your Financial Goals

CALM BEFORE THE STORM

NOTE: Unlock your phone rotation to read the Report.

"NEVER DEPEND ON A SINGLE INCOME. MAKE AN INVESTMENT TO CREATE A SECOND CHANCE"

From Managing Director's Desk To Readers

Demand For IT Firms Will Hold, But Their Hiring Won't

There is good news for information technology companies. Despite the continuing global economic slowdown, with the International Monetary Fund projecting a growth rate of under 3 percent and many countries looking at a flat GDP curve in 2023, global IT spending across regions will increase by a decent 5.5 percent, up from the previous year's 5 percent, according to a forecast by Gartner. What's more, it will be true of all regions across the world.

However, this will not reflect in the sector's hiring trend. According to industry experts, the next six months will be grim, and net head count numbers may fall. Thus we have a contradiction. Demand for IT will increase but not translate into more jobs.

Let us take a look at the details of the growth forecast. Software will lead the growth parade with an expectation of client spending going up by a hefty 12 percent. As is to be expected, IT services (maintaining on-site infrastructure and what in India comes under the umbrella BPO or business process outsourcing rubric) will follow at 9 percent. Data centre systems (onsite and in the cloud) and communication services (everything to do with phone networks) will follow far behind at under 4 percent. The rear will be brought up by devices (the IT that goes into hardware development) recording negative growth. This will clearly not be a year of fancy new handset releases.

As is to be expected, the ripples of the bank failures will not stop at the shores of the IT sector. Exposure to this tumult will remain contained but IT firms will have to keep an eye on startups and doing business with them. The sector will have to live with clients facing a cash shortage as banks become more cautious. So clients will spend but IT firms will have to work harder to get a part of it.

This brings us to the most serious issue facing IT companies – how to handle their staffing. The pitch had been queered by remote delivery services companies and startups first recruiting madly during the pandemic and paying exorbitant sums to grapple with high attrition, followed by large scale issue of pink slips as the pandemic subsided. Majors of the tech world from Apple to Amazon have all been a part of the process. How will IT companies strategise in the present scenario of pink slips flying around? Plus, what is perhaps most serious in a long-term sense, with generative artificial intelligence having arrived from chatGPT onwards, what is likely to happen to lower-level IT jobs that involve code writing and the impact of that on the overall staffing numbers in the sector?

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Hiring trends have been flat or downward as most companies have adopted a wait and watch approach. Where the issues of hiring, the banking crisis and Indian IT firms' prospects have all coalesced is the large weightage that the BFSI (banking, financial services and insurance) sector has in Indian IT offerings. As banks have turned cautious, they will not be in a mood to ask their IT partners to come up with new offerings which will require fresh hiring by vendors. One expert anticipates as much as a 40 percent drop in net hirings in the first half of the just started financial year.

How will the year finally pan out? As hiring is set to be slow in the first two quarters, a resumption in momentum will have to wait for the second half of the financial year. Some IT firms may even look at offering contractual jobs instead of the regular kind marked by full time work and standard compensation packages. With all these elements in play, vendors may lay specific focus on better utilisation of the bench to meet demand spurts.

In this scenario the undisputed gainer will be the investor and shareholder of IT firms. The primary focus of companies as they go slow on hiring and use emerging technology like chatGPT to do away with the services of those who write codes and look after routine maintenance will be to improve margins. They will be able to do this with comfort as demand from clients will continue to maintain the current momentum.

The need to return better numbers will be strong when full year results for 2022-23 start coming in, with the tone expected to be distinctly tepid. The guiding focus for IT firms in the current year, as they seek to look after their investors, will be to graduate from the present unglamorous prospects for shareholders to reacquiring a bit of the sparkle of the past.

While shareholders will be looked after, the fall guy will be the engineers from second order institutions who had started out with the vision of an IT job in mind but will now have to look elsewhere. As a slack manufacturing scene also will not be able to help, we may be looking at an emerging social crisis in the middle class with more queuing up for civil service jobs.

Salil Shah

Managing Director

Lakshmishree Investments & Securities Pvt. Ltd.

Look What Our Research Analyst Has To Say...

Nifty on the daily charts has broken out of a bearish falling channel and is sustaining above the same. Whats even better sis Nifty has made a Higher High Higher Low on the daily chart and is now trading in a bullish rising channel. Major supports on the downside are placed at 17,550 and a short tern correction will initiate only on a breach of the said level. Rallies will find resistance around 18,400 for the month of may but looking at previous expiry history and current development of Open interest there will be fire works towards the end of the month with bulls in charge of the rally.

Nifty Has Been Complacent – Is This The Calm Before The Storm?

This week has been underscored by high company-level volatility. Triggered by the differential of companies' performance against expectations during the quarterly earnings season, some stocks have rallied to new highs, while others have broken below historical lows.

At one end of the spectrum, we saw companies like Carborundum Universal, ABB, and Siemens rallying by more than 5% during the week. And on the other end, companies like Elgi Equipments, Shree Cement, and Hindustan Zinc corrected by 4-8% during the period. Even within the large-cap universe of Nifty 50, the trend has been similarly extreme. While Tata Consumer, SBI, ITC, and Bajaj Finance have returned more than 4% during the week to emerge as the top gainers, Divi's Labs, Hindustan Unilever, and Sun Pharmaceuticals have corrected significantly to finish at the bottom of the barrel.

It is interesting to note that this storm has been brewing solely under the surface. At the index-level, there has been suspicious calm. India VIX at around 11.5 is nearing all-time lows, and Nifty had remained stuck between 17,600 and 17,850 for almost the entire month before finally breaking out this Thursday.

If we look at the current macroeconomic and geopolitical situation as well as company-level fundamentals, the complacency displayed by Nifty recently is not warranted.

Moreover, historically, whenever VIX has touched such lows, the complacency was soon followed by increased volatility. The increased volatility, however, has led to Nifty going everywhere, but heading nowhere – Nifty has always closed negative or flat in the following year.

In April, we witnessed another such period of low VIX. India VIX has been below 12 for almost the entire month. If history is any indicator of what's to come, we should expect increased volatility in the following months. At the same time, the above analysis indicates that there is a need to pare expectations when it comes to the coming year's returns. History indicates that Nifty is likely to close flat or negative in the year to come.

A test of investor patience

The pandemic had drawn retail investors in hordes to the stock markets. Exceptional returns from the pandemic-lows as well as more time in the hands of investors as work-from-home took effect, had made stock markets seem "easy". But, since the end of 2021, Nifty has undergone significant time correction, leading to several retail investors opting out of the stock market. As Zerodha co-founder Nithin Kamath highlighted, the monthly new account openings with Zerodha are down to below 20,000 - levels last seen in March 2020.

If retail investors panic and opt out of SIPs as well, DII support to Indian stock markets could wane too. It is important to note that it is DIIs who have kept Nifty stable through the incessant FII selloff since October 2021. FIIs have net sold Indian equities worth Rs.4,29,000 Crore since then, while DIIs have ploughed in almost the same amount and supported the stock market during the period.

As stated earlier, the coming year is not expected to be a walk in the park. This could make many more retail investors drop the ball. But, investors who are able to ride through these tough times by sticking to and topping up on their quality bets at attractive valuations, would be able to achieve long-term capital appreciation.

Of course, one must also keep an eye out for how the macroeconomic situation evolves. As the recent quarterly results and management outlook of the technology sector prove, India's growth is not immune to troubles abroad. We may have a cushion from domestic demand and government support, but long-term sustainable growth can only come when the global economy is out of the woods. Key macroeconomic monitorables include inflation, high-frequency growth indicators, and central bank's stand on monetary policy – in India, as well as in the US and Europe. These are expected to impact India's exports growth. As for domestic GDP growth, rural incomes, private capital expenditure, and corporate credit growth need to pick up and sustain. Geopolitical developments could also impact global supply chains, inflation, and investor-sentiment.

Anshul Jain

Research Analyst

Stocks To Watch

www.lakshmishree.com

1. SYNGENE INTERNATIONAL

Syngene International is an integrated contract research, development and manufacturing organisation (CRDMO) serving the global pharmaceutical, biotech, nutrition, animal health, consumer goods and speciality chemical sectors.

It is based in Bangalore, India, where they have a research campus and two sites. They also operate a research campus in Hyderabad and a manufacturing campus in Mangalore.

Syngene has a team of more than 4,700 scientists who have the skills and experience to deliver optimal science, robust data management, intellectual property (IP) security and quality manufacturing to reduce time-to-market and the cost of innovation.

Their aim is to build strategic, long-term relationships with their clients and partners by offering a range of integrated research and development services, from the initial research programme planning to candidate selection, pre-clinical and clinical development, and manufacturing.

Particulars

Market Capitalisation	₹ 26,010 Cr
Debt (FY23)	₹ 816 Cr
Cash (FY23)	₹ 532 Cr
EV	₹ 26,294 Cr
52 Week Range H/L	682/ 508
Equity Capital	₹ 401.0 Cr

Shareholding Pattern

In (%)	June -22	Sep-22	Dec-22	Mar-23
Promoter	70.3	64.9	64.9	54.9
Public	28.9	34.7	34.7	44.7
Other	0.8	0.5	0.5	0.5

Profit and Loss Statement

Y/E March (₹ Cr)	FY 22	FY 23	FY 24E	FY 25E
Total Operating Income	2,604.2	3,192.9	3,692.5	4,359.1
Growth (%)	19.2	22.6	15.6	18.1
Raw Material Expenses	749.0	860.2	1,015.4	1,198.7
Gross Profit	1,855.2	2,332.7	2,677.1	3,160.3
Gross Profit Margins (%)	71.2	73.1	72.5	72.5
Employee Expenses	718.1	841.7	923.1	1,089.8
Other Expenditure	796.1	954.2	1,070.8	1,307.7
Total Operating Expenditure	2,263.2	2,656.1	3,009.4	3,596.2
Operating Profit (EBITDA)	**796.1**	**954.2**	**1,070.8**	**1,307.7**
Growth (%)	18.5	19.9	12.2	22.1
Interest	24.1	45.2	34.0	26.3
Depreciation	309.7	366.5	421.0	441.1
Other Income	52.8	70.9	82.0	96.8
PBT After Exceptional Item	**484.4**	**593.6**	**697.9**	**937.1**
Total Tax	88.6	129.3	164.0	220.2
PAT Before MI	395.8	464.3	533.9	716.9
Minority Interest	0.0	0.0	0.0	0.0
PAT	**395.8**	**464.3**	**533.9**	**716.9**
Adjusted PAT	426.5	464.3	533.9	716.9
Growth (%)	11.6	8.9	15.0	34.3
EPS (Adjusted)	**10.6**	**11.6**	**13.3**	**17.9**

Balance Sheet

Y/E March (₹ Cr)	FY 22	FY 23	FY 24E	FY 25E
Equity Capital	400.8	401.4	401.4	401.4
Reserves and Surplus	2,896.8	3,216.6	3,720.4	4,407.2
Total shareholders Funds	3,297.6	3,618.0	4,121.8	4,808.6
Total Debt	1,021.6	816.1	666.1	516.1
Long Term Provisions	34.4	43.7	48.1	52.9
Other Non Current Liabilities	261.2	277.9	305.7	336.3
Source Of Funds	**4,614.8**	**4,755.7**	**5,141.7**	**5,713.9**
Gross Block	3,943.5	4,761.0	5,262.6	5,513.7
Accumulated Depreciation	1,550.7	917.2	2,338.2	2779.3
Net Block	2,392.8	2,843.8	2,924.3	2,734.4
Capital WIP	346.4	0.0	0.0	0.0
Fixed Assets	2,739.2	2,843.8	2,924.3	2,734.4
Investments	1,034.1	918.5	918.5	918.5
Other Non Current Assets	282.8	398.2	315.1	350.2
Inventory	179.4	332.8	222.6	262.7
Debtors	507.7	529.3	719.9	849.8
Loans and Advances	0.0	0.0	0.0	0.0
Other Current Assets	237.1	207.1	264.2	293.6
Cash	517.9	531.7	799.7	1458.2
Total Current Assets	1,442.1	1,600.9	2,006.3	2,864.3
Creditors	232.8	258.0	315.6	372.6
Provisions	58.2	51.0	51.0	51.0
Deferred Tax Assets	65.6	69.6	76.6	84.2
Other current Liabilities	658.0	767.2	733.1	814.7
Total Current Liabilities	949.0	1,076.2	1,099.7	1,238.3
Net Current Assets	493.1	524.7	906.6	1,626.0
Application of Funds	**4,614.8**	**4,574.8**	**5,141.1**	**5,713.3**

Cash Flow Statement

Y/E March (₹ Cr)	FY 22	FY 23E	FY 24E	FY 25E
Profit/ (Loss) After Taxation	395.8	464.4	533.9	716.9
Add: Depreciation & Amortization	309.7	366.5	421.0	441.1
Other Operating Activities	143.1	113.1	300.0	0.0
Net increase in Current Assets	-234.3	-220.4	-137.4	-199.5
Net Increase In Current Liabilities	54.6	202.2	23.5	138.6
CF from Operating Activities	**582.2**	**823.5**	**1,175.0**	**1,123.3**
(Inc)/ Dec In Fixed Assets	-475.5	-518.3	-501.6	-254.1
(Inc)/ Dec In Investments	-162.3	-173.9	0.0	0.0
Other Investing Activities	26.6	35.8	251.3	-7.3
CF from Investing Activities	**-611.5**	**-656.4**	**-250.2**	**-258.4**
(Inc)/ Dec in Equity Capital	0.0	0.0	0.0	0.0
(Inc)/ Dec in Loan Funds	-5.8	-258.1	-150.0	-150.0
Dividend & Dividend Tax	0.0	0.0	-30.1	-30.1
Others	-25.5	-84.4	-34.0	-26.3
CF from Financing Activities	**-31.3**	**-342.5**	**-214.0**	**-206.4**
Net Cash Flow	**-60.6**	**-175.4**	**710.7**	**658.5**
Opening Cash	321.9	261.3	89.0	799.7
Closing Cash	**261.3**	**85.9**	**799.7**	**1,458.2**
Free Cash Flow	**106.7**	**305.2**	**673.4**	**872.2**
FCF Yield %	0%	1%	3%	3%

Our Take...

Revenues grew 31.2% YoY to ₹ 994.4 crore in Q4FY23. This was largely driven by its integrated services and execution capabilities, which led to such a robust performance across all its divisions. On the segmental front, discovery services and its dedicated centres showed steady growth on the back of decent demand.

The performance from development services division was supported by repeat orders, which showed increased customer stickiness. This was on the back of its ability to provide high and on-time service delivery.

GPM came at 70.5% during the period, lower than the normal range of 72- 73% due to higher manufacturing mix and higher consumables charges. On operational front EBITDA grew 27.2% YoY to ₹318.3 crore whereas margins declined 101 bps YoY to ~32%. Net profit during the quarter grew 20.9% YoY to ₹178.7 crore

The company's focus remains on investing in new infrastructure, technology, capability building and talent development. At its Bengaluru location, it opened a sterile fill-finish facility, which is projected to increase the end-to-end capability of development services. It also established a specialised proteolysis-targeting chimaeras (PROTACs) laboratory in Hyderabad for its customers working on cancer therapies and other therapeutic fields.

Outlook & Valuation

Going ahead, Syngene's revenue mix is expected to showcase visible shift towards development and manufacturing business, with manufacturing starting to play a more prominent role. We believe Syngene remains a compelling play in the CRO space with elite client profile and is well positioned for sustainable growth. Syngene's share price grew at ~28.33% CAGR over the past three years.

We value Syngene at ₹740 i.e. 22x EV/EBITDA on FY25E EBITDA of ₹1307.7 crore. We reiterate our **BUY** rating on the stock. The Key monitorable things would be – Zoetis contract execution and developments on the Mangalore facility front

2. POONAWALLA FINCORP

Poonawalla Fincorp Limited, formerly Magma Fincorp Limited, is an India-based non-banking finance company. The Company is engaged primarily in the business of financing. It provides asset finance through its pan India branch network.

The Company's business focusses on the necessities of people and enable them to earn their livelihood through financial products offered by it to the micro, small and medium enterprise (MSMEs), such as truck/taxi drivers who owns and operates commercial vehicles, construction equipment and passenger vehicles, among others to marginal farmers, small shopkeepers and other MSMEs.

The products offered by the Company include business loan, professional loan, personal loan, home loan, loan against property, pre-owned car loan, medical equipment loan, insurance and auto lease.

Market Data

Market Cap.	Rs 2.36 bn
52 Week Range H/L	Rs 338 / 209
Shares Outstanding	768m
3-M Avg Volume	$7.7m

Shareholding Pattern

In (%)	Mar-23	Dec-22	Sep-22
Promoter	62.1	62.1	61.5
FIIs	7.1	7.3	7.5
DIIs	6.1	4.5	5.2
Public	24.6	26.2	25.9

Income Statement

Y/E March (Rs Mn)	FY 21	FY 22	FY 23	FY 24E	FY 25E
Net Interest Income	8,824	9,493	12,217	20,269	28,293
Growth (%)	-1.8	7.6	28.7	65.9	39.6
Other Income	1,199	1,085	1,822	2,004	2,205
Total Income	10,023	10,578	14,039	22,274	30,498
Growth (%)	-8.5	5.5	32.7	58.7	36.9
Operating Expenses	4,563	6,046	8,031	10,199	13,054
Salary	3,060	4,099	-	6,935	8,877
PPOP	5,460	4,532	6,008	12,075	17,444
Growth (%)	9.6	-17.0	32.6	101.0	44.5
Provisions	13,186	686	-1,445	1,622	3,712
PBT	-7,727	3,846	7,666	41,256	13,732
Tax	-1,943	914	1,816	2,543	3,502
PAT	-5784	2,932	5,849	7,840	10,230
Growth (%)	NM	NM	NM	34.0	30.5

Balance Sheet

Y/E March (Rs Mn)	FY 21	FY 22	FY 23	FY 24E	FY 25E
Share Capital	539	1,530	1,536	1,536	1,536
Other Equity	18,881	55,615	62,711	98,117	1,07,631
Net Worth	19,421	57,145	64,247	99,653	1,09,166
Borrowings	79,148	67,258	1,11,196	1,40,107	2,00,353
Growth (%)		-15.0	65.3	26.0	43.0
Other Liabilities	4,851	3,693	4,775	5,958	8,404
Total Liabilities	1,03,420	1,28,097	1,80,218	2,45,717	3,17,923
Cash & Cash Equivalent	6,124	5,372	6,574	15,001	6,810
Investments	4,289	8,197	3,109	3,420	3,591
Advances	85,653	1,06,784	1,52,295	2,08,144	2,86,840
Growth (%)		24.7	42.6	36.7	37.8
Other Assets	7,353	7,744	18,240	19,152	20,682
Total Assets	1,03,420	1,28,097	1,80,218	2,45,717	3,17,923
AUM	1,02,470	1,15,190	1,61,430	2,21,430	3,08,430

Our Take...

Driven by the increasing product portfolio and shift to more secured lending, the company's assets under management (AUM) increased a robust 37.2% y/y, 15.9% q/q. The focused AUM grew at a faster 73% y/y with growth across its key segments. Disbursements at Rs63bn grew 89% y/y, focusing on short-term loans. Customer acquisitions picked up pace as more than 0.6m customers were added. Niche financing products and the strong tech focus are likely to aid the expansion of loans at a 38% CAGR over FY23–FY25.

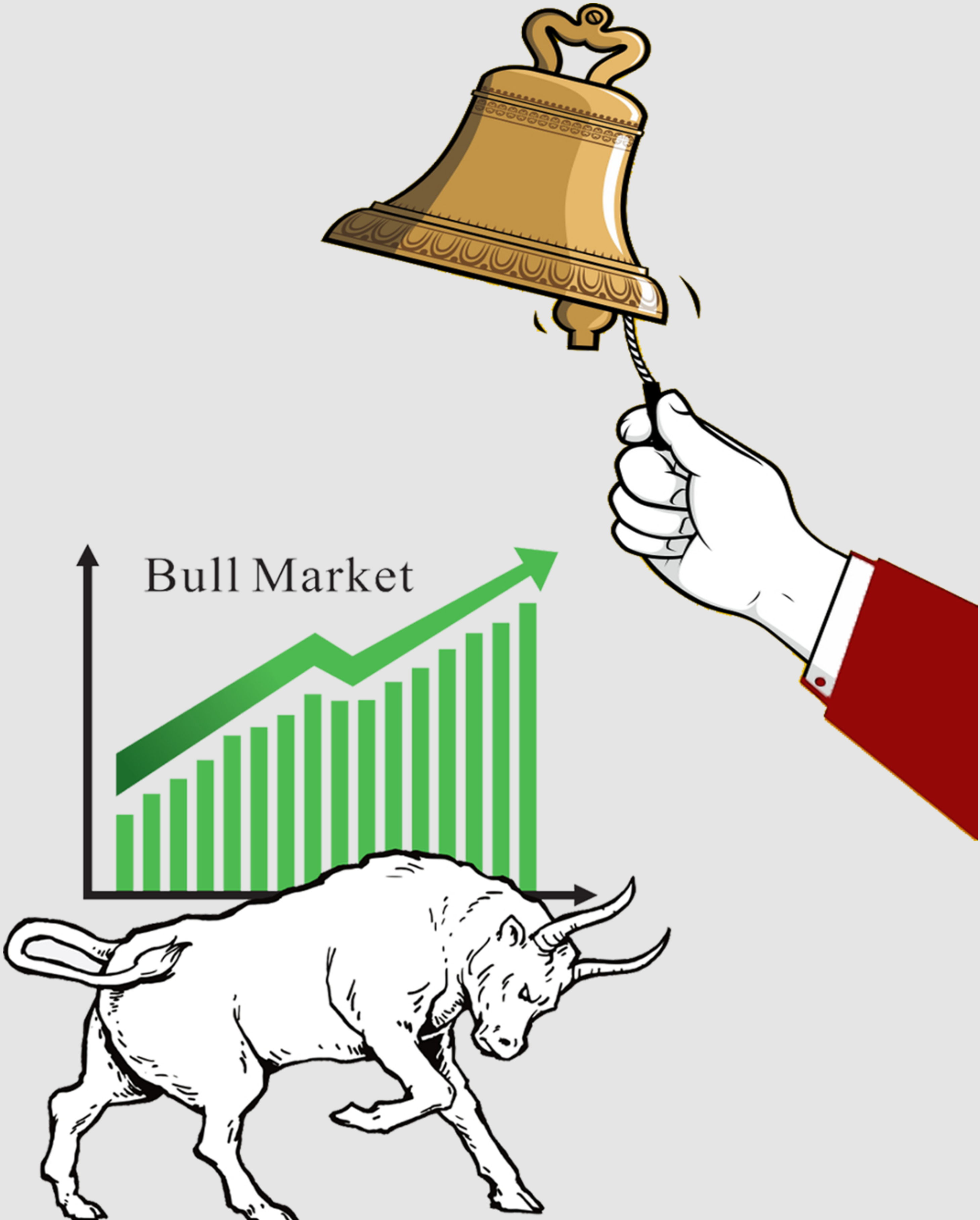
NIM further improved despite the increasing interest-rate environment. The NBFC has also recently seen a rating upgrade by CRISIL to AAA. As a result, we believe that it can maintain its NIM over FY24-25 at above 10%. Cost-income at 49.3% has improved sharply. As the loan book further scales up, we believe FY24 should see operating leverage kick in.

Outlook & Valuation

Driven by strong, 52% y/y, NII growth, Poonawalla Fincorp's Q4 FY23 net profit rose 103% y/y to Rs1,813m (far exceeding ARe). We expect robust growth, competitive cost of funds and tech savviness to drive the standalone unit's 38% loan CAGR over FY23-25. We retain our Buy stance on the company with a 12-mth target price of Rs417, valuing it at 3x FY25e standalone P/ABV, derived using a multi-stage DDM method.

The major risks present which may hamper the price of the stock is higher slippages and less than expected loan growth.

This May Impact Your Investments!!



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NSE Smoothens Corporate Action Impact On Indices

Indian markets are witnessing two corporate events in three of the biggest companies listed on the bourses. Since these companies are in the benchmark indices, a big worry for the index providers was how to incorporate the changes without causing any disturbance in the market.

Indian domestic investors have over the years moved their preference towards passive funds that track the benchmark indices, thanks to the poor performance of the high-cost active funds. Investment in passive equity funds has grown at the fastest rate of 34 percent in FY23 to over Rs 7 lakh crore.

Any changes in the index composition generally results in money flowing into the companies that are included in the index and leaving those that are exiting. A corporate action such as a merger or a de-merger in a company that is part of the index can result in volatility in that company's stock.

But this time, three of the biggest companies that account for 25 percent of market capitalization of the index are going through either a merger or a de-merger. Any changes in the fund flows to these companies'stocks can result in increased volatility in these stocks as well as in the indices.

To smoothen the event, NSE Indices, a subsidiary of the National Stock Exchange, has announced changes in its methodology of Nifty equity indices for mergers.

The companies under consideration are HDFC Bank's merger with HDFC and the de-merger of Reliance Industries and its financial services arm Jio Financial Services Ltd, which will be re-listed.

NSE Indices require the index company to be excluded from the index on the ex-date of the merger which is the closing of T-1 day. This means HDFC will not be traded after it will get merged with HDFC Bank in the ratio agreed upon by the two companies. Since both companies are listed, the combined weightage after considering the ratio will be considered. The move will prevent sharp moves in both the counters, especially by traders and investors who bet on an arbitrage opportunity emanating from the price inequality between the two companies.

The big change that has come out is in the ex-date. In earlier cases, if the equity shares of the merged entity allotted to the shareholders of the transferor company (post-merger) account for more than or equal to five percent of the current equity of the merged entity, then these shares are updated for calculation of market capitalisation with effect from the last trading day (T Day) of the calendar month of listing of these shares.

If they were less than five percent of the current equity of the merged entity, then these shares are updated for calculation of market capitalisation with effect from the last trading day of the corresponding calendar quarter (March, June, September, and December).
In the case of the demerged companies (Reliance and Jio Financial), NSE Indices has revised the methodology for handling demergers, allowing the demerged entities to be retained in the index. According to existing norms, demerged entities are excluded from indices soon after shareholders approve the scheme of arrangement for the demerger.

According to the new norm the demerged company would be retained in the index if a special pre-open session is conducted by the exchange. Such a session is conducted for price discovery of all stocks in cases involving corporate restructuring.

If the demerger happens before that of HDFC Bank and HDFC, it would mean that Nifty50 would have more than 50 components in the index and one company, the one with the lowest market capitalization will be removed. However, the company can be included after the HDFC twins merger. If HDFC twins can go through the process before Reliance, the reverse will hold.

NSE Indices needs to be complimented for bringing in a mechanism that will allow the corporate action to go through without disturbing the market.

Services Exports The New Hope, But Not For All

India has never been good at manufacturing and a lot of intellectual effort has been expended in recent decades trying to figure out how manufacturing could be made more efficient and globally competitive so as to aid overall goods exports. This would enable the country to follow in the footsteps of Japan, South Korea, and most recently China in successfully pursuing export led growth.

But success along these lines now seems doubtful as we are in an age of decline in manufacturing, brought on by the disruption in commodities markets following the Ukraine war, and rise in services prompted by the covid19 pandemic. Thankfully, quite fortuitously, India is much better and more competitive in services delivery. Thus, looking ahead, what we see is the arrival of the age of services which can be an engine of not just robust export growth but of job creation too.

What is even more fascinating is that, within services, proficiency in ICT is the mature part; what really holds out the big promise for the future is the robust prospects for an uptick of non-IT services. The hope is that the export of these services such as consulting and research and development will keep up the overall export momentum by taking up the slack in manufacturing exports as a result of the global economic slowdown. Services exports rose 25 per cent in the October-December quarter, with software services growing by 21 per cent and business services by 31 per cent.

Overall services exports are expected to surpass goods exports by the end of the next financial year 2024-25. This will enable India to put in a growth performance which will allow it to fulfil the promise of becoming the fastest growing major economy in the world. The boost in services exports has been enabled by global capability centres which have now begun to offer high-end services like support for accounting, audit and legal activities. According to Nasscom, India is now home to nearly half of the global capability centres. Over time these have been moving up the value chain and are now offering services like tech enablement, capability development, sales support, quality assurance, and R&D and business development. Their delivery has been enabled by the rapid rise in digitisation during the covid19 pandemic and the future offers unlimited prospects as India's share of global commercial services exports is now only 4 per cent.

The actual enabling of services exports is being led by the big global consulting firms like Deloitte, KPMG, EY, PWC and Grant Thornton which foremost serve foreign companies. They are expanding operations in India in response to a shortage of chartered accountants in the US. Plus, Indian CAs come cheap, at about a tenth of the salary that has to be paid out in the US.

If this is the positive side of the picture, there is a negative side too. One would expect the government to give a helping hand to the emerging opportunities in non-IT services exports. But such help is yet hard to come by despite a new foreign trade policy being announced. The government's focus for non-IT services exports remains on Gujarat's GIFT city when capability centres have come up in tech strong cities across the country. The Service Export from India Scheme has been discontinued.

Plus, more important, are the new developments creating jobs where they are needed the most -- for skilled workers? The decline in manufacturing export prospects is bad news for fresh jobs for such people. Even tech jobs are not what they used to be. There is serious concern that the programming jobs (writing software code) which used to be the mainstay of graduates from the run of the mill engineering colleges (not IITs) will take a beating with the use of artificial intelligence software like ChatGPT for the same purpose.

Jobs are still being created in IT but they are of a higher order---required, for example, to redesign a company's business processes to improve efficiencies. Also, the jobs being created in the global capability centres that are currently thriving is India require high end skills, like those able to deliver audit and accounting functions. When at the turn of the century the IT jobs in code writing and maintenance emerged, it was a boon for the India middle class. Today the scenario facing the same middle class is not at all bright.

The emergence in opportunities in non-IT services exports will boost India's macroeconomic numbers like the balance of payments and even the overall growth rate. But the new income generated will be very unevenly distributed. Most Indians will continue to wait for a better day with factory jobs not being easily forthcoming. There will be new jobs in construction sites enabled by the public investment in infrastructure, but these will be mainly for those who have migrated from rural India in search of unskilled work.

The Financial Turmoil Is Not Over

There's an old investment saying that bull markets last longer than you think possible and bear markets hit harder than you can imagine. This is one reason why investors should be positive most of the time. However, once every eight to 10 years it pays to be cautious. The recent spate of bank failures suggests that now is one such moment.

Policymakers want to present these bank failures as idiosyncratic and unlikely to trigger a broader systemic crisis. We are unconvinced. First, we have a different view of the nature of systemic risk. And second, a decade of low rates and easy money has distorted capital allocations in ways that increase the risk of systemic crisis.

Successive financial crises have shown that systemic risk is multiplicative. The failure of a small entity can have severe consequences for the whole system. Faultlines tend to show up in the weakest links in systems, not necessarily the largest. Despite this, policymakers continue to obsess about the larger institutions as systemically important, only to be blindsided by smaller players that are less well-capitalised and less tightly regulated.

The recent spate of US bank failures is also a symptom of what we call quantitative destruction: the systematic unwinding of the institutional structures that emerged and thrived in a decade of near-zero rates and easy liquidity. The largest, fastest and broadest tightening of policy rates seen in 40 years, combined with central bank balance sheet reduction, is challenging parts of the financial system. Many models for business operations, funding and default have not been road-tested adequately for such a sudden shift. We saw this last year when crypto and the strategies of UK pension funds came under pressure.

And if 2022 was about the repricing of capital, 2023 is likely to be about the reduction in the quantity of capital, as "quantitative destruction" puts alternative assets and non-bank financial institutions to the test after their recent rapid growth.

A decade of zero rates triggered a search for yield which led to pension fund portfolio allocations to commercial real estate and alternatives rising from 15 per cent in 2007 to 23 per cent by 2022, according to Willis Towers Watson's Thinking Ahead Institute. Real estate could be one key flashpoint in 2023. Residential property prices have already been hit hard by higher rates, and now commercial property prices are also falling. Eventually, asset owners and lenders will need to reprice their property assets. With about 60 per cent of $2.9tn US commercial real estate loans funded by smaller banks, stress looks set to rise.

Private debt and equity also gained from their higher yields and lower reported volatility (since their valuations are often not marked to market). When liquidity was plentiful, private companies could easily access debt and equity markets. This becomes harder as rates rise and liquidity evaporates.

Asset owners may have to make good their commitments to invest in funds when called on. To do this, they may need to sell publicly listed assets, liquidating what they can sell, rather than what they want to (as happened in the UK pension fund crisis over so-called liability driven investment strategies). A recent New York Federal Reserve Board paper highlighted how these kind of asset fire sales by non-bank financial institutions — which now account for $60tn of global assets — could inject systemic risk back into the banking system.

Increased financial risks are also a symptom of broader debt deleveraging. Between 2008 and 2021, the expansion of central bank balance sheets led to a sharp rise in borrowing. Global non-financial debt rose in that period from 182 per cent to 257 per cent of gross domestic product.

As central banks shifted to quantitative tightening, that non-financial debt has fallen back to 238 per cent of GDP (with US non-financial debt consistently falling as a percentage of GDP for the first time since the early 1950s). While central bankers may see balance-sheet reduction largely as a technical process, the financial sector is experiencing it as classic debt deleveraging.

At the start of every systemic crisis, financial failures tend to be labelled as idiosyncratic. As the pace and scale of financial failure spreads, that narrative becomes harder to maintain. A decade of zero rates and easy liquidity have provided the preconditions for systemic crisis, with rapid asset growth and financial innovation encouraging new entrants into lightly regulated areas. We believe that "quantitative destruction", fuelled by a toxic mix of rising rates, debt deleveraging and elevated equity valuations, has the potential to turn those financial risks from idiosyncratic to systemic.

What China's Rocking GDP Numbers Mean For India's Steel Producers

Iron ore prices have been signalling a bearish outlook for steel stocks, having fallen from a level of $130 a tonne in mid-March to $120 a tonne now. The steel-making ingredient's price offers a reasonably good signal of the direction of steel prices too. It's no surprise then to see that steel prices in Asia have turned weak. But, the real surprise is that these took place despite a bright 4.5 percent GDP growth reported by China, a large producer and consumer of steel.

Now, steel and iron ore prices did inch up on 18th April after the Chinese economy's better-than-expected recovery. But, steel and iron ore prices would not have turned weak in the first place if demand conditions were strong. Low iron prices are typically a sign of steel mills going easy on stocking up due to weaker than expected demand for steel at current prices.

One reason for this could be that China's GDP growth outperformance was mainly driven by its services (tertiary) sector, which grew by 5.4 percent YoY in the March quarter, while GDP growth in manufacturing (secondary) came in at 3.3 percent, according to a Nomura Research note. Similarly, while retail sales growth in March beat expectations, coming in at 10.6 percent compared to the expectation of 7.5 percent, value added in the industrial sector grew at 3.9 percent compared to the consensus estimate of 4.4 percent.

The second spot of bother for the steel sector is the performance of the real estate sector In March 2023, as property sales recovery was weaker than expected based on National Bureau of Statistics data, according to Nomura. Sales volume and value declined despite a low base effect and the data indicates deterioration in momentum in lower-tier cities, it said. While weakness in manufacturing and real estate are indeed negative for the steel sector, a sustained recovery in China's economy could see consumption recover more rapidly initially and then spill over to other parts.

How the steel industry views the demand outlook for 2023 is also available from the April version of the short range outlook released by the World Steel Association. Steel demand in 2023 is expected at 1822.3 million tonnes, growing by 2.3 percent over a year ago. While this may seem a big improvement over the October 2022 estimate of 1 percent, that's only because 2022 proved to be worse than expected, lending a low-base effect. The October forecast's demand was 1815 mn tonnes, only slight lower than the April estimate.

China's output is expected to increase by 2 percent in 2023 after declining 3.5 percent in 2022. The rest of the world is expected to grow by 2.6 percent, with India growing at 7.3 percent and Turkey at 9 percent. However, what's a bit uncertain is the belief that developed economies' demand can grow by 1.3 percent. A lot depends on how these economies are affected by the tightening of monetary policy and the ongoing Russia-Ukraine war.

In fact, a recent ING note had mentioned how iron ore prices fell to a 4-month low on news reports that China plans to curb steel output in 2023, keeping it at the same level as 2022. One way to look at that is China intending to keep a check on emissions. Other reasons could be to keep iron ore prices in check or to avoid a huge surplus of steel inventory which could then depress prices. These don't augur too well for steel demand prospects.

What does all of this mean for Indian steel producers? The demand outlook for India remains strong and is growing in absolute terms even if the pace of demand growth is slowing as the base expands. Finished steel consumption in March increased by 13.3 percent over a year ago, which is very good growth. The moderation in raw material prices will also yield some relief from cost pressures. The pace of imports too has slackened in recent months, even as exports have risen. If there is one concern, and it's a big one, then it is from moderating steel prices. Steel prices have been trending downward since Q2 of FY22 and while Q4 has seen a slight pick-up, it's still down compared to a year ago. If they slip again, then it's a risk for the steel industry's EBITDA margin, even as deflation in raw material prices will offer some relief.

Tata Steel's India operations' volume sales in the March 2023 quarter were nearly flat compared to a year ago, while sales in Europe declined. JSW Steel reported output growth of 12 percent growth YoY but it does not release sales volumes, for which one has to wait for its results to be declared. Government data shows domestic steel consumption in January, February and March grew by 2.6 percent, 11.1 percent and by 13.3 percent over a year ago. Stable to rising steel prices and falling raw material prices is the combination steel companies need to report a good set of numbers in FY23.

IT Downturn Likely To Be A Short-Term Affair

The fall in information technology stocks after the disappointing results churned out by TCS and Infosys for Q4 2023 has raised a key question – is this a blip or a signal that cracks are beginning to appear on an edifice which was hitherto considered shock proof. The quick answer is that this is a short-term downside and there is nothing on horizon to signal a fundamental change for the celebrated Indian IT industry.

Now for a slightly more detailed picture. According to Jefferies, the latest results of the industry leaders appear to have been influenced by a number of downsides like worsening sentiments in the US which sees a recession ahead accompanied by clients becoming more cautious about discretionary IT spending. More specific to the Indian industry, the weakness in client sentiment in North America is focused on the two verticals of communications and BFSI (banking financial services and insurance). The latter in particular, affected by the banking crisis and seeking to conserve cash, is a key source of client spending which traditionally keeps the Indian industry sailing.

Revenue growth for TCS, Infosys and Accenture from clients in North America has steadily worsened over the last five quarters and actually turned negative in the last quarter. More specifically, the decline in the rate of growth of digital revenues for Infosys is seen as a signal that clients are becoming more cautious about discretionary spending.

Since IT stocks have taken a tumble after the announcement of quarterly results by TCS and Infosys, it pays to look closely into how exactly the two have individually fared. Infosys's performance seems to have missed all parameters. Sequential revenue sharply declined by 3.2 percent. According to Kotak, this was due to sharp cuts by clients in discretionary tech spending because of macro uncertainties. Further, there was a one-time project cancellation. What is perhaps more disturbing is that the firm itself does not see a very bright immediate future, reflected in its guidance for the current financial year for both revenue and margins.

TCS results were somewhat better but not as much as to overcome the downside in sentiment created by Infosys, according to Centrum. Figures for both revenue and margins disappointed markets. The firm's explanation for this was the same as in the case of Infosys – lower discretionary spending by clients. Plus, TCS has attributed pressure on margins from the stickiness in its own spending, an inability to cut costs in a way which would have entailed sizeable layoffs. Attrition has declined further and there has in fact been a very small rise in headcount.

Infosys, on the other hand, saw a small decline in headcount. Importantly, Tech Mahindra, Mphasis and LTIMindtree have also been affected by the various headwinds mentioned above.

Where does this leave us? Overall, Indian IT companies have been hit by a cautiousness engulfing the financial sector after the collapse of Silicon Valley Bank and the fall of Credit Suisse. This cautiousness has affected North American financial firms' willingness to spend on taking forward their digital technology. Indian IT firms have been particularly badly affected because in regular times North American financial clients' spending makes BFSI a key vertical for them.

This must be seen in its historical context. The advent of the COVID pandemic caused global business to grind to a halt but IT moved forward as businesses sought to digitally equip themselves and move their processes and data to the cloud as part of the attempt to support work from home. This led to a rapid expansion of IT firms' operations, a need to quickly acquire additional hands, willingness to pay staff more and in the process try to wean staff away from each other resulting in high attrition.

Then when the pandemic ended and business returned to normal and firms sought to get their staff to physically come back to work at offices, a reverse process began. Clients' spending on digital technology lost priority and they became cautious on IT spending overall. Large global tech firms saw revenue outlook declining, started issuing pink slips. Resultantly attrition in IT firms cooled down and they sought to control costs by delaying freshers' joining.

Thus, today's slack in revenue growth is in part a process of correction from the excesses that happened during the pandemic. Businesses' need to keep up their IT spending will not go away as technology will not stand still. Right now, the new emerging giant is generative artificial intelligence in the form of chatGPT. Ergo, after a hiatus business across the developed economies are likely to go back to the level of spending needed to keep abreast with emerging technology.

Analysts should be able to see this and not ring alarm bells over a couple of below consensus results. They have not done so as they are by nature short-sighted and on their say-so, markets go through their short-term gyrations. Individual investors with an eye on long-term value are not part of this dynamic. They know that in the long run they will be dead but meanwhile they will not lose sleep or churn their portfolios in response to markets jumping up and down at the say-so of analysts.

HUL Is Finding It Difficult To Get Off The Inflation Tiger

Price and growth will re-balance', says the 37th slide in Hindustan Unilever's March quarter results presentation. Price is indeed playing its part, with price-led growth at 7 percent during the quarter, down from 11 percent in the December quarter. But volume growth at 4 percent is not playing ball and is actually lower by a percentage point.

The contribution from price is going to go even lower, as a growing number of inputs are seeing prices ease off their peaks. Several commodities such as crude oil, palm oil, chemicals such as soda ash, foods such as barley and wheat have seen prices come off their peak levels. HUL will need to lower prices, to pass on benefits to consumers, to remain competitive, but even after all this still hope that volume sales growth will recover to higher levels. It's a difficult situation.

Years of high inflation have hurt lower income consumers hard. Why, even in the March quarter, when prices of key products such as detergents and soaps softened, the FMCG market's volume growth was flat while rural growth declined by 3 percent. The only constant support for companies such as HUL has been the push to sell more premium products, contributing to a better sales mix and supporting margins in the face of rising costs.

In the March quarter, Hindustan Unilever's sales rose by 11 percent over a year ago and its gross margin improved sequentially thanks to lower costs. But weak demand meant HUL reinvested those savings behind higher advertising and promotions. The net effect was EBITDA margin at 23.7 percent, just 10 basis points higher sequentially. This phenomenon may continue for some time, as savings in input costs are partially passed on to consumers and partially invested behind advertising and promotion.

At some point, lower prices should see volume growth recovering, hopefully with lower-income consumers also seeing their economic conditions improve due to lower inflation. Also, there are limits to how much a push given to premium products can continue to drive performance.

But there could be another hurdle in HUL's path to higher growth—its unwillingness to let margins drop below a certain level. If competition is willing to do that then it could lead to share erosion too. In HUL's categories of home care and foods & refreshment, its segment margin in the March quarter mirrored the December quarter's level, even as sales growth slumped. And, the beauty & personal care's segment margin even increased by a percentage point, but growth was unchanged.

In some ways, it's a conscious choice HUL has made, to keep margins at a certain level and try and push for higher growth within that. Indeed, one reason why volume growth will anyway recover is the higher grammage in fixed-price packs due to falling input costs. But HUL also needs to do its bit to spur volume growth, apart from waiting for external factors to work in its favour. If letting the margin slip a bit can help revive growth and ensure it remains competitive, then that short-term sacrifice will be worth it. Otherwise FY24 may end up being a case of price growth going low and volume growth keeping it company.

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Registered Office:

Unit No 407, IV Floor, Marathon Icon Marathon Nextgen Campus, Ganpat Rao Kadam Marg, Mumbai-400013
Opposite Peninsula Corporate Park, Lower Parel
Contact No: (022) 43431818

Corporate Office:

57, 2nd Floor Gandhi Nagar Sigra, Varanasi, UP- 221010
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