MONTHLY OUTLOOK

SEPTEMBER 2020

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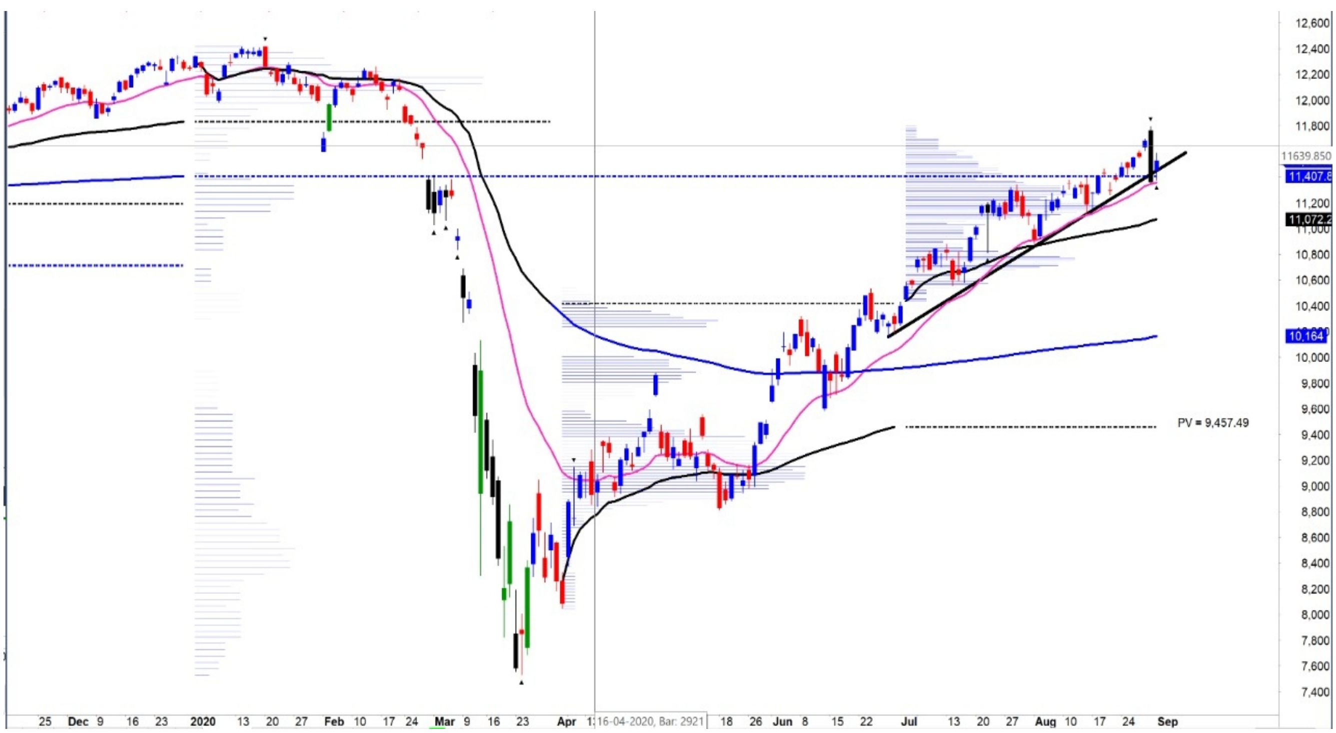
Nifty has started facing heat and 11800 around it has made a short term top(at the time of writing & any move above 11850 will negate the view) and is at a rising trend line on Daily charts. So any close below 11250 will plunge the markets to 11000. Pharma and private banks should hold on to its gains where as IT sector can be performer of the month with bottoming around mid of September and then the rally on upside will begin.



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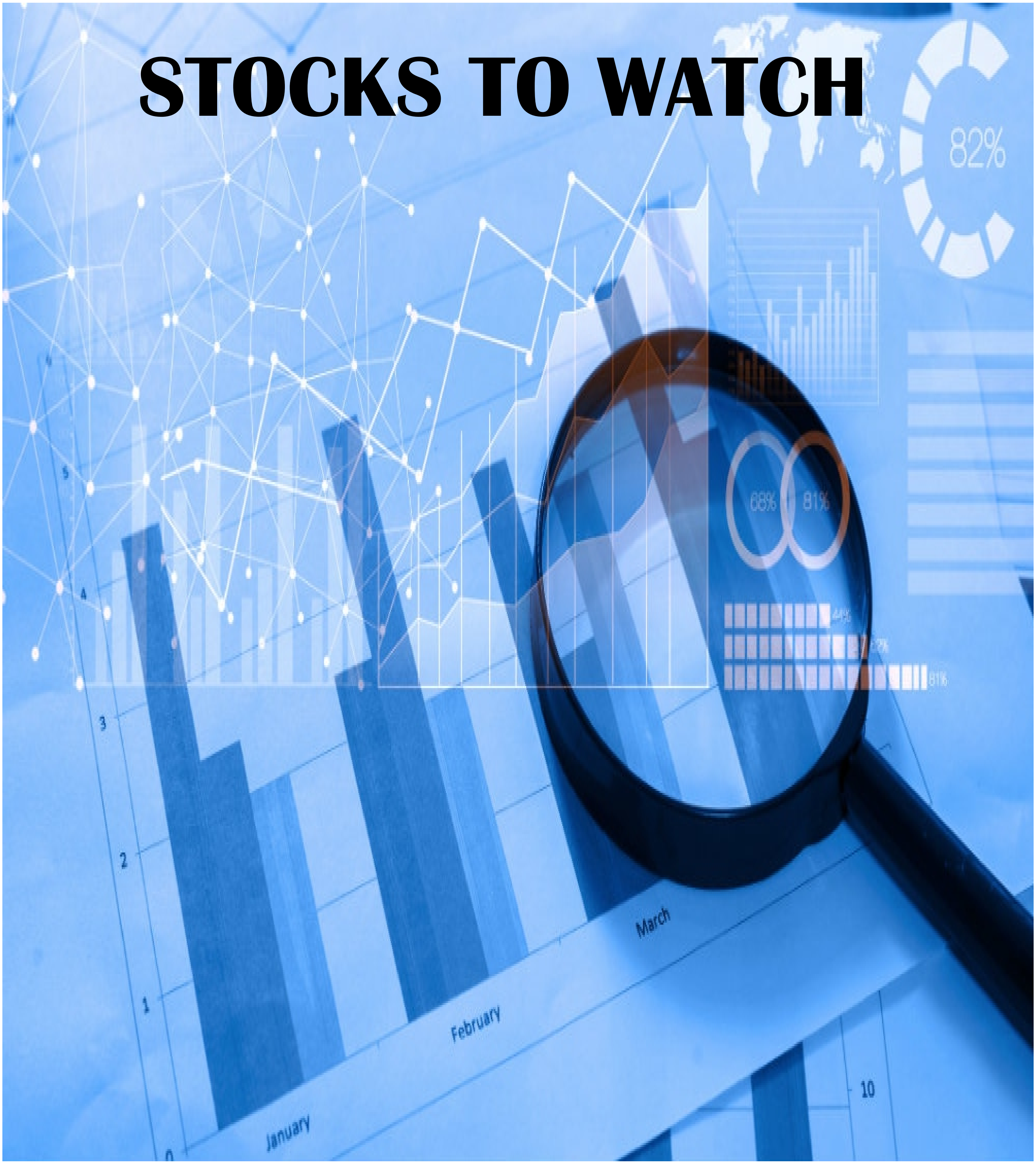
SEPTEMBER 2020

STOCKS TO WATCH



Indian Hotels

Current Market Price (Rs)	Target Price (Rs)	52 week H/L (Rs)	Mkt Cap (Rs cr)
106.75	122.75	163.00/62.10	13,278.07

Investment Rationale:

The hotel industry up-cycle was abruptly disrupted by Pandemic after five years of favourable demand-supply environment which led to steady increase in operating drivers. Hotel Industry has been the worst impacted as it struggled with lockdowns initially till April 2020 and extremely low demand post lockdown, with very few future bookings. However, occupancy could be in the range of 30-40% for the current fiscal year.

Company Profile

IHCL and its subsidiaries, collectively known as the Taj Group, is one of Asia's best-known hotel companies. It was founded in 1899 by Jamsetji Tata and is headquartered in Mumbai. Its flagship property, the Taj Mahal Palace in Mumbai, was opened in 1903. The group's current inventory stands at over 25000 rooms with total 158 hotels - 141 in India and 17 abroad and 42 in pipeline.

Financial Summary:

Annual	MAR 2020	MAR 2019	MAR 2018	MAR 2017	MAR 2016
Sales	4,463	4,512	4,103	4,020	4,023
Other Income	132.00	83.00	61.00	54.00	99.00
Total Income	4,595	4,595	4,165	4,075	4,122
Total Expenditure	3,858	4,003	3,711	3,721	3,838
EBIT	736.00	591.00	453.00	354.00	284.00
Interest	341.00	190.00	269.00	323.00	375.00
Tax	44.00	157.00	121.00	113.00	90.00
Net Profit	350.00	244.00	63.00	-83.00	-181.00

SEPTEMBER 2020

Federal Bank

Current Market Price (Rs)	Target Price (Rs)	52 week H/L (Rs)	Mkt Cap (Rs cr)
56.10	64	98.55/35.70	11,933.27

Investment Rationale:

Its strong granular liability franchise, comfortable capital positioning and management's long term strategy of focusing on increasing retail book size, while consciously slowing down in the wholesale segment.

Company Profile

Federal Bank Limited is a major Indian commercial bank in the private sector headquartered at Aluva, Kerala having more than thousand branches and ATMs spread across different States in India. The Bank is a pioneer among traditional banks in India in the area of using technology to leverage its operations and was among the first banks in India to computerize all its branches.

Financial Summary:

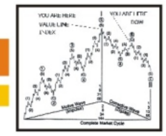
Particulars (Rsmn)	Q1FY21	Q1FY20	YoY-%	Q4FY20	QoQ-%	FY19	FY20	FY21E	FY22E
NII	12964	11542	12.3%	12160	6.6%	41,763	46,489	49,452	53,531
PPOP	9,324	7,828	19.1%	9,593	-2.8%	27,631	32,047	33,251	35,162
PAT	4,008	3,842	4.3%	3012	33.0%	12,439	15,428	11,994	15,474
EPS						6.3	7.7	6.0	7.8
ROAE (%)						9.8	11.1	8.0	9.6
ROAA (%)						0.84	0.91	0.64	0.75
Adj. BVPS						58.6	64.7	64.4	75.0
P/E (x)						9.0	7.4	9.5	7.3
P/Adj BV (x)						1.0	0.9	0.9	0.8

SEPTEMBER 2020

CHANGES TO WITNESS

Global Impact of Biden's Green Deal

Accepting the Democratic Party's nomination as presidential candidate for the 2020 elections, vice-president Joe Biden described climate change among the four historic crises, an existential threat, to overcome which America could lead the world and, in the process, 'create millions of good paying jobs'. Biden had earlier unveiled his climate and environment plan that includes a proposal for federal spending of nearly $2 trillion over four years, and leveraging additional private sector and State and local investments to total to more than $5 trillion.Should Biden win the presidency in November, it will mean the US would rejoin the Paris Agreement, step up to contribute to the Green Climate Fund, and lead climate and clean energy initiatives. Much has changed since 2017. Clean energy is now a viable option, a jobs generator, and there is growing awareness of climate change and its impact. Biden's promise of 'historic investment' and achieving net-zero emissions by 2050 will fundamentally change geopolitics, technology and much else. For one, it will alter the Middle East, particularly Saudi Arabia's, 'special relationship' with Washington and US engagement with the region. The energy axis changing, it will open up options for partnership.Oil- and gas-dependent Russia will hurt, and force it to rediscover its capacity for innovation. The US would impede China's fossil fuel-based investments as part of the Belt and Road Initiative. On the other hand, China is in a position to capitalise given its domestic investments in clean energy. How that pans out will depend on the manner in which trade issues are resolved. Biden's plan will strengthen the EU's Green Deal and this will fundamentally alter trade — with environmental considerations gaining primacy.For India, the best course is to create an infrastructure and framework that recognises the economic opportunity that a green recovery and clean energy presents. It must step up and be a partner in this transformation — through its trained and skilled manpower, and initiatives such as International Solar Alliance.



Implement GST, to Boost Direct Tax

The government's tax transparency initiative with faceless assessment and appeals and a taxpayer charter is welcome. Corruption depends on human interface and the misuse of arbitrary powers by taxmen. That must go.Contactless assessment will minimise the interface between the assessing officer and the assessee, and improve compliance. Tax officers must also desist from making high-pitched assessments in their zeal to meet collection targets. Launching the platform for 'Transparent Taxation — Honouring the Honest', Prime Minister Narendra Modi urged people to introspect and pay their tax dues. However, the way to increase direct tax collections is to clean up the goods and services tax (GST), which generates audit trails to income currently escaping tax. Nearly 66% of the total tax collections in the country come from indirect taxes that are borne by the rich and poor alike. The share of direct taxes in total tax revenues must rise. The mining of GST data and electricity bills makes it eminently feasible. The gross value added for the economy is equal to the gross profits plus wages and salaries.It holds at the firm level and can be used to estimate the value added by each production unit, and its distribution to taxable entities. Electricity bills and employee provident fund payouts must tally with the claimed production and value added levels.Many small units are outside the formal banking system.

The remedy is to extend the reach of formal finance, make small units keep books and bring these into tax net. Data analytics must be used to track the physical volumes of raw materials along their production chain ending in tax-evaded goods. If garments evade taxes, the suppliers of the fibre that is spun into yarn later converted to fabric should be asked to furnish the details of all their customers. These should be traced, and their customers, and so on. Reverse charge should be used more widely, also be universal so that buyers can pay tax on their purchases directly to the government while recognising the vendor on whose behalf the tax is being paid.

Stock exchange for social enterprise

A working group at capital markets regulator Sebi has brought out a welcome report on the social stock exchange (SSE), a platform for fundraising for social enterprises, and measuring and reporting social impact. The objective is to fund enterprises that seek to create 'positive social impact' via innovative securities, and to have robust standards of social impact assessment and attendant reporting.While social impact bonds have been floated in India for a while – the first such project implemented by Educate Girls circa 2015 'covered' 7,300 children in rural Rajasthan — the Sebi paper seeks to build an entire ecosystem to gainfully fund social enterprises, complete with information repositories, social auditors and reporting standards for social capital formation. Four key stakeholders come together for social impact bond issuance: investor, service provider, independent evaluator and outcome payer, such as a foundation or the government; the goal is to duly meet an envisaged social development objective. The SSE can be housed within existing stock exchange. Social entities can be either for-profit enterprises (FPEs), or non-profit organisations (NPOs). For FPEs, the SSE is to raise equity and social venture funds. For NPOs, zero-coupon, zero-principal bonds are also proposed, for investors who are interested in social impact and do not wish to have the funds returned to them.The paper suggests allowing funding to NPOs on SSE to count towards corporate social responsibility commitments, which seems unexceptionable. Also, allowing philanthropic donors to claim 100% tax exemption for donations to NPOs makes perfect sense. At present, donations to private NPOs are allowed 50% tax deduction, whereas government entities get 100%. The anomaly surely needs prompt correction.

The RBI — Physician, Heal Thyself

The Reserve Bank of India (RBI), in its annual report, has rightly emphasised the role of public investment in infrastructure in reviving growth and crowding in private investment. It has also suggested some methods to finance such investment. One is foreign direct investment (FDI). It suggests Railways as an ideal candidate.Why foreigners would want to invest in a loss-making enterprise is a question that is neither asked nor answered. The Railways should hive off suburban transport as a separate entity with a series of joint ventures with the state governments and municipal corporations governing the towns where suburban trains operate and receive massive amounts of subsidy. The rest of the Railways could then be structured to operate efficient cargo and passenger services. Then, perhaps, rail could qualify for FDI.Privatisation of ports under an independent regulator is another mechanism suggested to raise resources for investment in infrastructure. Monetisation of assets in steel, power, coal and land is also advocated.Such measures would make sense, except for their effect of channelling available private capital into transfer of existing assets than into creation of fresh assets. Fresh asset creation is what an economy in a slump requires.The government should borrow and spend on infrastructure, and, on a vastly more expansive scale, channel foreign capital desperately seeking higher returns than what bond markets in the developed world offer into fully articulated projects from the infrastructure pipeline identified by the NITI Aayog. The National Investment and Infrastructure Fund must raise its game in this regard. RBI also suggests developing the debt market.Further, there is also a need for expanded footprints for specialised NBFCs classified as Infrastructure Finance Companies'. Presumably, these IFCs would raise funds from the bond market and lend to infrastructure projects. Why should the bond markets not directly fund the infrastructure projects? In any case, India needs a functional bond market for

The Future of Kishore Biyani

Kishore Biyani, founder and chairman of the Future group managed to repay the Rs 100 crore interest due on his $500 million foreign currency bonds just before the grace period given after his initial default was about to run out. This gives him breathing space to close the deal he is reportedly working on – to sell the retail operations of the Future group as well as its logistics arm. According to reports, a buyer may also pick up a minority stake in Future Consumer, Biyani's fast-moving consumer goods firm, which is what Biyani will be left with if the deal goes through. The Future group had piled up too much debt which it is finding hard to service. Biyani does not have many options left – if he cannot close the deal, the group will probably default on its other debt obligations coming up and have to file for bankruptcy.Either way, it will mark the end of the incredible run of Kishore Biyani's retail journey. He will still have a fast-moving consumer business– and will probably remain a rich man. But he won't be running the retail empire he had built up from scratch and almost lost once earlier.Biyani's started his entrepreneurial journey by making readymade trousers in the late 1980s but his retail journey only started in the late 1990s when he set up a Pantaloons store and a Big Bazaar in Calcutta. In the early 2000s, though the number of Future Group stores under different labels – Pantaloons, Big Bazaar, Food Bazaar, Central – was exploding, many businessmen refused to take him seriously. The buzz was around Shoppers' Stop, the department store started by the Raheja Group, or RPG Retail or even the Tata group's foray into retail.The organised retail play was getting crowded with the Piramal group (Pyramid Retail), the Landmark group (Lifestyle stores) and others entering the field. But by 2005, it had become impossible to ignore his frenetic, debt-fuelled expansion. Biyani's Future group had pulled ahead of the others easily in revenues, in the number of outlets and the sheer number of formats he was experimenting with.Equity investors were not enamoured by him though – many institutional investors thought the Future group was largely a one-man show, with relatives in charge of key responsibilities. It was true to an extent – the Future group's strategy depended on Biyani's vision of what retail should be. But it was also true that even in 2005, organised retail was just about finding its feet in the country and there was no professional who could say that he or she had mastered the entire retail operations. Biyani was better placed than most professionals because he had the passion and was extremely grounded and hands-on in managing his business.By 2009 though, the debt-fuelled expansion had begun to take its toll. Biyani was forced to restructure the group soon afterwards to reduce debt. By 2012, he even had to sell off his lifestyle format and brand, Pantaloons, to the AV Birla group.But the ever ebullient Biyani could not be held back. He continued his expansion and got back into fashion through the FBB or Fashion Big Bazaar brand. His format experiments continued – from small format to Supermarkets to Hypermarket sized formats. He had plays in affordable furniture (HomeTown) and consumer durables (EZone). His stores were the anchor tenants in many big malls.The problem with retail is that it is a cut-throat business with low margins. To build scale requires huge infusions of capital – and Biyani was always short of capital, depending heavily on debt to expand. Debt funding was good when the cost of funds was low, and retail revenues were booming. Anytime the cycle reversed, he would get into trouble.Meanwhile, the retail game itself was changing. Reliance Industries had got into retail with big ambitions and enough capital. E-commerce was also finding its feet slowly in the country, and by 2015-16, Biyani had realised that his model of pure physical retail would not carry on for too long.But Biyani's attempts at selling online never caught on – e-commerce was not in Future group's DNA and his efforts to build an alliance with Amazon did not work out too well either. He talked of Omni-channel but little came of it. He was gung ho on the hypermarket format and picked up the Hypercity chain from the Rahejas in 2017, spending Rs 655 crore to do so.And while Big Bazaar was a big success at least in terms of footfalls, not everything enjoyed similar loyalty. Both HomeTown and EZone did not make much headway. Over the last few years, the rise of e-commerce had also ensured that the Future Group's products were not necessarily the cheapest in the market.In terms of presence and visibility and even customer footfalls, the retail operations were still up there with the best but margins were shrinking and the debt position was getting worse.In the last couple of years, Biyani had changed tack and entered the FMCG business, focusing primarily on foods. In 2015, he picked up Grasim's consumer products division. He wanted to compete with the likes of Britannia and ITC in food products and set himself ambitious targets.The problem was that all his expansion was fuelled with high-cost debt, raised mostly from private equity investors. Even before the COVID induced lockdown, his financial position was not great. In end 2019, the credit rating agency ICRA had downgraded its rating. A lot of Biyani's shares were also pledged to raise money.After the lockdown, Biyani's retail revenues would have been hit massively. It was clear that he was in no position to service Future group's expensive debt.At any rate, Biyani can be unsentimental. He had sold his P antaloons, his first retail brand, to save his other business. Now, he is getting ready to sell his retail business and walk away.

McKinsey Global Institute :is the Making the peacock dance

McKinsey Global Institute has brought out a new report titled 'India's turning point: An economic agenda to spur growth and jobs'. It features a peacock on its title page, a few days after the prime minister was seen feeding peacocks. The Indian economy has usually been compared to an elephant and the peacock is a welcome change.The report is actually a warning---unless India is able to considerably raise its growth rate, it risks massive unemployment. The researchers estimate that India needs to provide 90 million non-farm jobs by 2030. Of this number, 60 million will be the new additions to the workforce, while 30 million will shift out of agriculture. If women choose to increase their participation in the workforce from the current very low levels, then an additional 55 million non-farm jobs would be needed. That's a total of 145 million non-farm jobs needed by the end of the decade.Will the economy be able to provide so many jobs? The report says it is tough to make any forecasts till 2023, because of the pandemic. If India's GDP annual growth rate is 5.5-6 percent between 2023 and 2030, with growth for the decade at 5 percent or so, then the economy will be able to absorb a mere 6 million new workers. That would mean huge unemployment.On the other hand, if the economy can have a compound annual growth rate (CAGR) of 8.5 percent between 2023 and 2030, it will be possible to absorb all the new workers and net employment will grow at a CAGR of 1.5 percent.Leaving aside the big question of whether a CAGR of 8.5 percent is feasible, consider that the McKinsey report points out that between 2013 and 2019, when the economy grew at a CAGR of 6.9 percent, additional net employment over the period was zero. Also, between 2006 and 2012, when the economy grew at a CAGR of 8.2 percent, net employment grew at a CAGR of only 0.3 percent. How is it then the report assumes that an 8.5 percent GDP growth rate will increase net employment at a CAGR of 1.5 percent?Simply put, the researchers are saying we won't be able to absorb the millions of new job seekers if we continue with our lack adaisical business-as-usual approach.What needs to be done? McKinsey has identified three growth boosters that could make it possible for India to grow at 8.5 percent per annum and also create enough employment. These are: the creation of global hubs serving India and the world and seizing opportunities in the shift in supply chains; create efficiency engines for India's competitiveness, such as next generation financial services; and new ways of living and working, such as e-commerce, climate change mitigation, renewable energy.Their recipe for increased productivity include making sure that the average size of firms increases, land is unlocked, labour made more flexible, reduction of commercial and industrial power tariffs, privatization, monetization of government assets, financial sector reforms et al.The problem is that all this has been said many times. For instance, the 2012-13 Economic Survey, when Raghuram Rajan was Chief Economic Adviser, has sketched out three scenarios---'Business as usual', 'Reforms' and 'Decline'. When the Modi government first came to power in 2014, hopes were high that it would finally put reforms in the fast lane, creating the conditions for rapid capital accumulation and growth. But that hope has fizzled out long ago.This time, the difficulties are far greater. For instance, automation and robotics could lead to jobs being destroyed. Globalization, which helped millions come out of poverty in India, is being challenged and countries are retreating behind protectionist barriers. The Indian government too has been raising tariffs. Export growth has been sluggish for years. The government's finances are already stretched to the limit and it now has no alternative but to spend more on defence. There is talk of a new normal of lower global growth. In India, the story of the last few years has been one of steadily falling growth rates. Job growth, as the McKinsey report points out, has been absent.What the McKinsey study does is underline that this time, there is no alternative to root and branch reform. Dithering and kicking the can down the road will lead to massive unemployment over the years, very likely leading to social unrest.It's time to make the peacock dance.

No surprises in Moody's downgrade of SBI

Moody's Investor Services downgraded State Bank of India's baseline rating by a notch citing risks to asset quality and profitability. It also retained a negative outlook. It turned out to be water off a duck's (or should we say, elephant's) back. SBI is a proxy for the Indian economy. Given the expected deep economic contraction due to the COVID-19 pandemic, it would be a surprise if SBI maintains asset quality and profitability in the coming 12-18 months, not if they deteriorate. In any case, two months earlier Moody's had already downgraded SBI's deposits ratings in line with India's sovereign rating. Nevertheless, it merits paying attention to the pressure points highlighted by the ratings agency.For one, it says that SBI's gross non-performing loans ratio of 5.4 percent (a 2 percentage point improvement from a year earlier) could be understated. That's because it does not include credit under moratorium which amounted to 9.5 percent of total loans as of June. But even that number could be lower than actual because SBI has excluded loans that are under moratorium but where borrowers have paid up a couple of instalments.Second, the ratings agency says that SBI has lower capital than similarly rated global peers. Given the expected drop in asset quality and profitability, the lender will need external capital in the days to come. It has made a start by raising close to Rs 9,000 crore through sale of bonds last week.In a Motilal Oswal conference, the bank's chairman Rajnish Kumar said that it expects slippages & the restructured book together to remain within 2.5 percent of total loans. But we have heard such projections in the past from various chairmen of Indian lenders who have proved to be consistently wrong.Perhaps it is not wholly their fault. Public sector lenders like SBI are often unwilling grooms for shotgun marriages conducted by the government and RBI.

The Yes Bank bailout is a case in point. Similarly, they are the channels for directed lending as the government tries to boost the economy by pushing banks it owns to lend more. At the time of the June quarter results, Rajnish Kumar had even said “for lending, this is the best time.” In the middle of a raging pandemic, no less.Of course, SBI is best placed among PSU lenders to navigate these difficulties thanks to the sheer size of its balance sheet and access to low cost funds and so on. It also has a good source of capital in the form of subsidiaries in the credit card and insurance businesses where it could sell stakes if push comes to shove.Investors would also do well to monitor whether Rajnish Kumar gets an extension when his term expires in October 2020.

Capital Good stocks rally, and but haze over sector remains

In spite of a nationwide lockdown, capital goods companies surprised positively with an earnings beat for the June quarter. Investors gave a thumbs up and shares of most firms rallied sharply from the lows hit in in end-March. But the optimism is overdone.That most company managements, including large conglomerates such as Larsen & Toubro Ltd, abstained from giving a guidance for fiscal (FY)2021 indicate that the haze has not lifted. There are several factors that endorse a cautious outlook.Weak June quarter order flows raise concerns on revenue visibility in the quarters ahead. One could overlook this given that the lockdown had brought economic activity to a standstill for a large part of the quarter. The double-digit drop in order flows of most companies therefore was hardly surprising.What's worrisome is that weak order flows may continue in the next couple of quarters. A fragile order book will impact revenue traction ahead. Barring L&T (which has a robust and diversified order book), most companies such as Thermax Ltd, Siemens Ltd and ABB India Ltd have order books that are presently just around or a little over a year's revenue. Note that most of them, especially multinationals, had moved away from large project orders to short-cycle orders in the last few years to mitigate delays and cost overruns in big projects. Unfortunately, the pandemic has choked this pipeline too.Sector analyst Umesh Raut of Yes Securities (India) Ltd explains, "short-cycle order inflows are likely to remain under pressure in the near term owing to (a) subdued capital expenditure (capex) plans for large sectors such as metals, power and cement (b) deferrals of those in the pipeline due to significant demand uncertainty for end users and (c) weak industrial activity."Capex apart, slowing discretionary spends by consumers may keep operational expenditure (opex) by the private sector at a minimal level. Also, orders from pharmaceutical and food and fast moving consumer goods segments will not be able to compensate for the poor offtake in core sector industries.To be sure, the government's strategy of boosting local manufacture and stepping up orders in railways and defence brings a ray of hope for few companies in this segment. But power generation and transmission ordering may be dim as demand for electricity is relatively low. With healthcare spends taking priority, there could be slowdown in smart city and mobility expenditure.Meanwhile, the outlook on exports is as hazy as it is in the domestic economy. Lavina Quadros, analyst at Jefferies India Pvt. Ltd points out that while the long term export story (particularly for global firms) is intact, “export opportunity to areas outside Asia might stall a bit as global companies look to retain some supply chains near developed markets, despite higher costs, as a contingency plan for any future disruptions like COVID-19.”Whether a second round of covid-19 infections will again stem growth in the recovering countries is anybody's guess. The path to normalcy could be a slow one. Expectations and earnings estimates have already rolled over from the second quarter to the fourth quarter of FY21, by some large companies.The latest Reserve Bank of India's survey of 802 manufacturing firms also indicates weak business expectations for the September quarter and sharp dip in consumer confidence in the current environment. Another key factor is the cautious approach by bankers given that the end of the moratorium waiver period would bring to light the financial viability of companies under duress.So, how did companies manage a performance beat in June quarter? Firms have aggressively trimmed variable and fixed costs to shore up profits in spite of plummeting r evenue and weak operating leverage. But then, there is limited scope to cut costs further, say analysts. A shrunk pie in the near to medium term will also increase competition in the sector.The positives in the company have already been factored into the stock prices after the recent rally. The only consoling factor is that even after the sharp rally in the last few months, most stocks are trading below the five-year average multiples. Execution and order flows must pick up, in the absence of which the already wafer-thin margins may further erode.

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