Monthly Memo

May 2022

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Naveen has over 17 years of experience in the Financial Services and Telecom sectors. In his previous role, he was responsible for Institutional and Retail research as Head of Research with Reliance Securities Limited. He also served as Co-Head of Research with Phillip Capital India Private Limited in his 11-year long association with the organization.

A New Market Regime!

A few days back, I had an intriguing conversation with a bond trader from a leading international bank. His view on the market was interesting. “This is going to be a lucrative fiscal for bond traders as the trade through the year is rather simple. Keep it short and don’t tinker around. Interest will keep inching up and the short position will keep making money. I am already big time in the money. You get such opportunities only once in four years”. Bond prices have a negative correlation with interest rates. As interest rates go up, bond prices decline. While the trade is not as simple as it sounds, this year might actually be a windfall year for an experienced bond trader.

The picture for equities, however, is a little complicated. Equities fall and rise depending on the stage of the global and country’s economic cycle as well as monetary policy management by the central banks. The Reserve Bank of India (RBI) raised interest raised by 40bps last week which was unexpected. The equity market reacted negatively as it saw the focus shifting to inflation management instead of propelling growth. The current consensus believes the market to see persistent inflation moving forward, which in turn, will impact the economic growth rates around the world. Keeping this in view, IMF, too, has downgraded GDP growth estimates for all major economies around the world, including India. However, interestingly, India’s GDP growth at over 7% is still quite strong, indicating the Indian market to throw off enough opportunities to make money in FY23 as well.

Resilient Corporate Earnings

To begin with, the Q4FY22 corporate earnings paint an interesting picture. Amidst all the chaos of rising input costs and supply chain challenges, corporate earnings have been quite resilient and margin pressure has been lower than expected. For instance, margins reported by the Auto companies were better than consensus estimates as the industry managed its cost structure rather well. FMCG companies like HUL, too, have successfully managed to pass on the input cost pressures to the end consumers, indicating the market's willingness to absorb the price hikes. Moving forward, although Q1FY23 will continue to see margin pressure, cooling off in commodity prices coupled with companies undertaking some price hikes will mean that margins will continue to be in the manageable zone. All these factors imply that earnings for FY23/FY24 may not see material cuts and the earnings growth trajectory for the benchmark index will remain intact.

However, the pressure led by notable FII selling will remain intense over the short term and a wide range of sectors will be impacted. The Large Caps are likely to be most impacted by the FII selling as their positioning in this space is much more significant. The Small and Mid Cap space is more dominated by domestic institutional investors and may in fact outperform the Large Cap space over the medium term.

Ahead or behind the inflation curve

Higher inflation and interest rates inflict a significant impact on the economy. Over the short term, higher inflation can lead to a higher nominal growth rate and faster economic growth. However, persistent higher inflation eventually brings down the real growth rate, making it imperative to curb it in time. The central bankers seldom want to be ahead of the curve when it comes to raising interest rates. However, at times, in the situation of timing it too finely, they tend to lag behind the inflation curve by a significant margin, thereby exposing the economy to the demon of persistent inflation. This is the current scenario globally. Central banks in the US have fallen behind the inflation curve and now have to raise interest rates significantly to make up for the lag. India, on the other hand, has been able to time the rate hike better than the rest of the world and with the recent 40bps hike, it is very much in line with the curve.

Falling behind the inflation curve and then raising interest rates too fast tends to tilt the economy into a recession. This risk has become very real. However, in the case of India, the chances of an economic recession are much lower than its western counterparts. Thus, albeit lower than earlier expectations, India will still offer good growth and the economy will still deliver a healthy growth rate moving forward.

Value-focused growth or Growth at a Reasonable Price

The prevailing rise in inflation has notably impacted global growth and, in turn, has significantly changed the current market structure. As this has made growth scarce, stocks offering such growth avenues will rightly attract even more allocation moving forward. However, note that in a rising interest rate cycle, stocks commanding high PE undergo significant correction due to earnings multiple compression, leaving only a narrow band of stocks that deliver good returns. Against this backdrop, while 'Value' will remain a critical theme, the present scenario would favour secular themes more, which is expected to deliver better returns than the cyclical plays.

Moreover, the focus will be on the quality and sustainability of earnings and emphasis on management quality will be critical. The change in market regime marks a significant change to the overall portfolio stance and allocation to more secular themes instead of tactical plays will result in better returns over the next year.

Clearly, with so many variables bouncing around, the market breadth will narrow down significantly. It's not just the earnings growth but also the valuations that have become a constraint on account of lower liquidity in the system, implying only a few stocks that will deliver decent appreciation in FY23. This means stocks exhibiting both growth and cheap valuations will report decent returns. This brings us to the investment style – Growth at a reasonable price (GARP).

GARP investing entails investing in companies that have sustainable growth prospects over the long term as well as the trade at reasonable valuations. In the Indian context, sectors which exhibit consistent long-term growth are Consumer Staples, Consumer Discretionary, IT, Digital, Retail, Autos, and selective Pharma. Apart from these themes, clean energy and high-quality industrials can be considered secular long-term thematic plays. However, the challenge is to find reasonable valuations in these themes as most stocks trade at premium valuations. So, even if these companies deliver on earnings expectations, the stocks may experience significant price erosion due to PE compression.

Nonetheless, Autos, selective Pharma, and Industrials have a significant number of plays that showcase robust long-term prospects and reasonable valuations.

Conclusion

At this juncture, the consensus increasingly believes that the earnings will remain strong but macro challenges will persist. This clearly means returns in FY23 will be back-loaded and the second half of the fiscal will report better returns. Broad market themes are changing and dominant investment styles could also be undergoing a marked shift. However, no matter how challenging the prevailing market conditions might be, the opportunities would continue to remain immense. This is the right time to add to equity investments and reap the benefits of good returns in the latter part of the year.

Happy investing!

Naveen Kulkarni

Portfolio Changes:

Our portfolio changes indicate our strategic stance in the market.

Growth portfolio changes

Scrip Name	Action	Weight	Remark
HDFC BANK	BOUGHT	5.0%	The merger with HDFC limited to bring significant synergies; Valuations reasonable

Contra Portfolio changes

Scrip Name	Action	Weight	Remark
Rain Industries Limited	SOLD	3.0%	New challenges on account of raw material unavailability. Global growth challenges to keep stock under pressure in 2022
NMDC	SOLD	3.3%	China's lockdown challenges to keep iron ore prices under immense pressure.
CESC Ltd	BOUGHT	3.0%	Structural theme building in utilities. CESC will see many of its units turning profitable. FY23/24 looks to be a major turnaround year.

AXIS SECURITIES

Portfolio Performance

Particulars	1 month	3 months	6 months	1 Year	Since inception
Axis Pure Growth	-1.19%	0.20%	-1.42%	28.89%	91.52%
BSE200	-0.72%	1.02%	-2.01%	18.84%	80.02%

(* net of fees)

Top 10 Holdings

Scrip Name	Weight
ICICI Bank Limited	11.1
Varun Beverages Limited	7.6
Bharti Airtel Limited	7.5
Infosys Ltd	6.1
EIH LIMITED	5.8
Coromandel International Ltd	5.3
Abbott India Ltd	5.3
Carborundum Universal Ltd	5.2
Maruti Suzuki India Ltd	5.0
Kotak Mahindra Bank Ltd	4.7

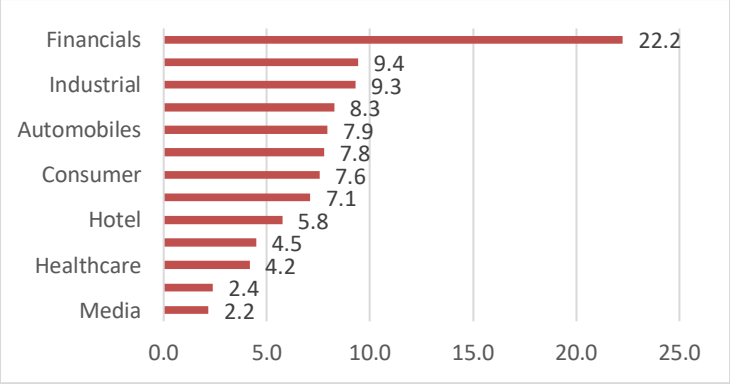
Key Portfolio Ratios

Wt. Avg. PE	19.5
Wt. Avg. PB	3.2
Wt. Avg. ROE	12.2
Wt. Avg. Mcap	2,06,981.93

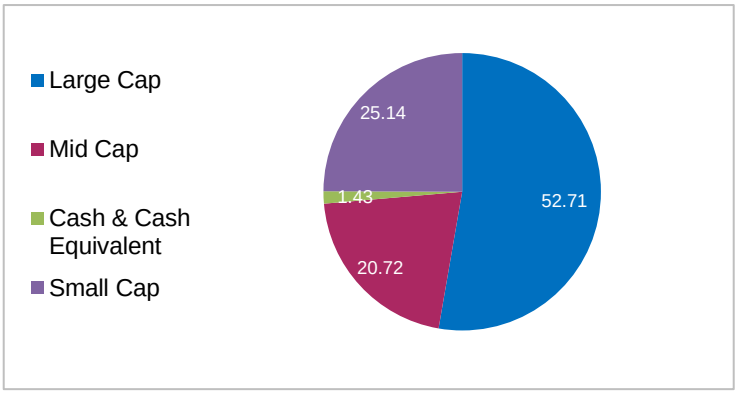
Risk Assessment

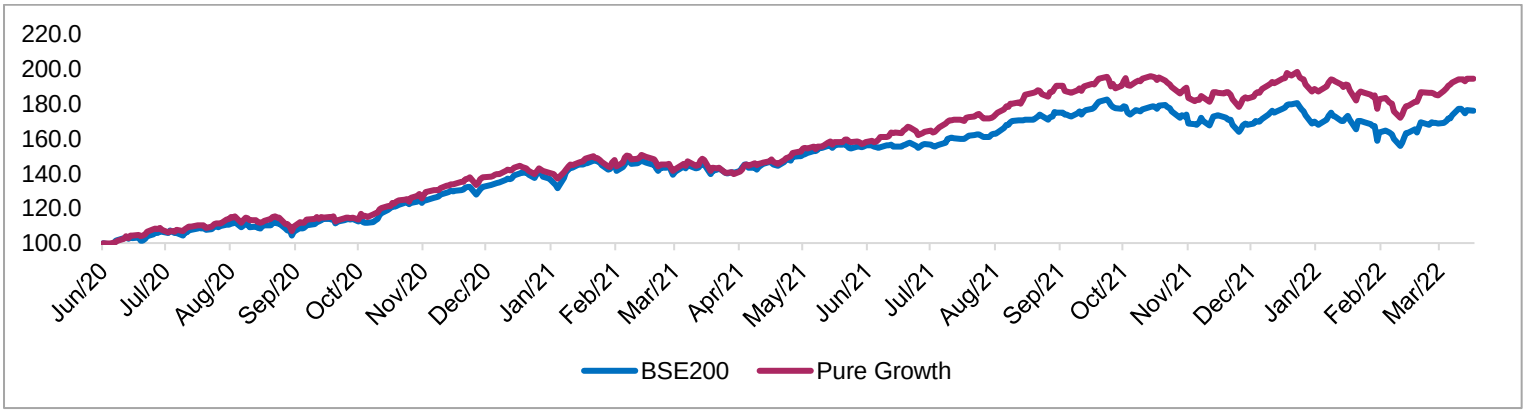
Portfolio Beta	0.88
Information Ratio	1.17
Volatility	15.87
Sharpe Ratio	1.78

Sector Allocation



Market Capitalization





Portfolio Performance

Particulars	1 month	3 months	6 months	1 Year	Since inception
Axis Pure Contra	-2.44%	-2.89%	-2.81%	28.29%	125.18%
BSE200	-0.72%	1.02%	-2.01%	18.84%	80.02%

(* net of fees)

Top 10 Holdings

Scrip Name	Weight
State Bank of India	9.9
ICICI Bank Limited	9.7
Infosys Ltd	6.0
Bajaj Auto Ltd	5.8
Bank of Baroda	5.4
United Spirits Limited	5.3
Aditya Birla Fashion and Retail Limited	5.1
EIH LIMITED	5.1
SBI Life Insurance Company Limited	5.1
Carborundum Universal Ltd.	5.0

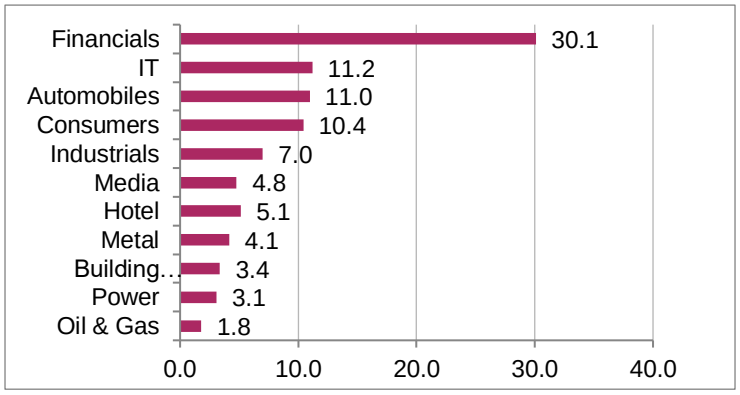
Key Portfolio Ratios

Wt. Avg. PE	21.71
Wt. Avg. PB	3.12
Wt. Avg. ROE	12.16
Wt. Avg. Mcap	1,63,144.44

Risk Assessment

Portfolio Beta	1.09
Information Ratio	1.24
Volatility	19.74
Sharpe Ratio	1.62

Sector Allocation



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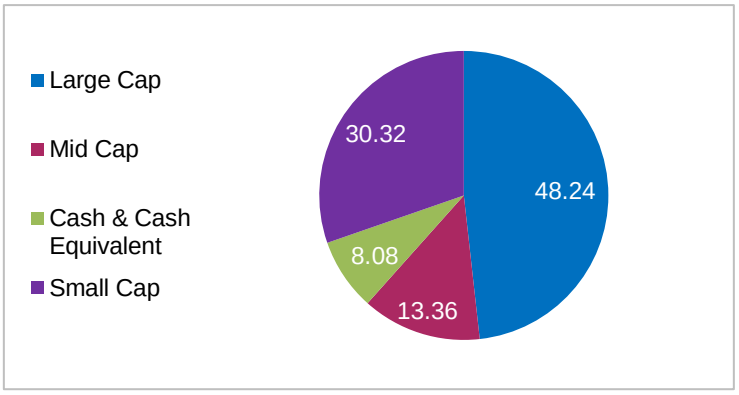
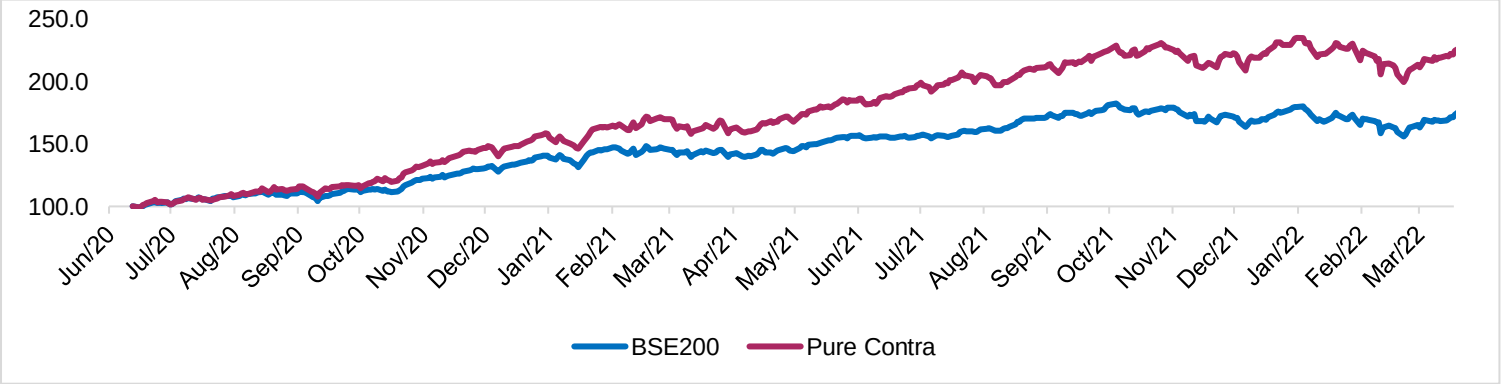




Portfolio Performance

Particulars	1 month	3 months	6 months	1 Year	Since inception
Axis Retirement	0.10%	0.24%	-0.05%	12.78%	48.76%
BSE200	-0.72%	1.02%	-2.01%	18.84%	80.02%

(* net of fees)

Top 10 Holdings

Scrip Name	Weight
Reliance Industries	11.1
ICICI Bank Ltd.	9.9
Tata Consultancy Serv Lt	8.2
United Spirits Limited	6.1
Cipla	6.0
State Bank Of India	6.0
Brookfield India Ret	5.7
Bharti Airtel	5.7
Bajaj Auto	5.4
Sbi Life Insurance Co Ltd	5.4

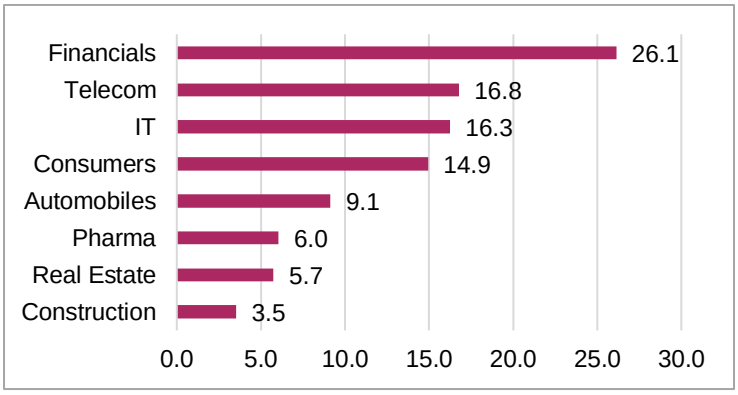
Key Portfolio Ratios

Wt. Avg. PE	28.9
Wt. Avg. PB	5.2
Wt. Avg. ROE	16.7
Wt. Avg. Mcap	5,31,175.10

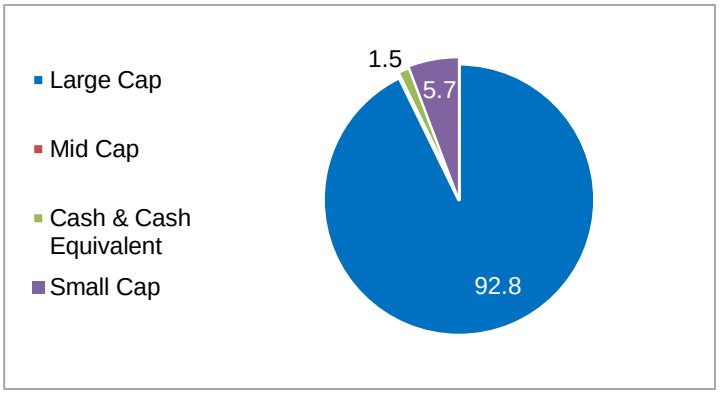
Risk Assessment

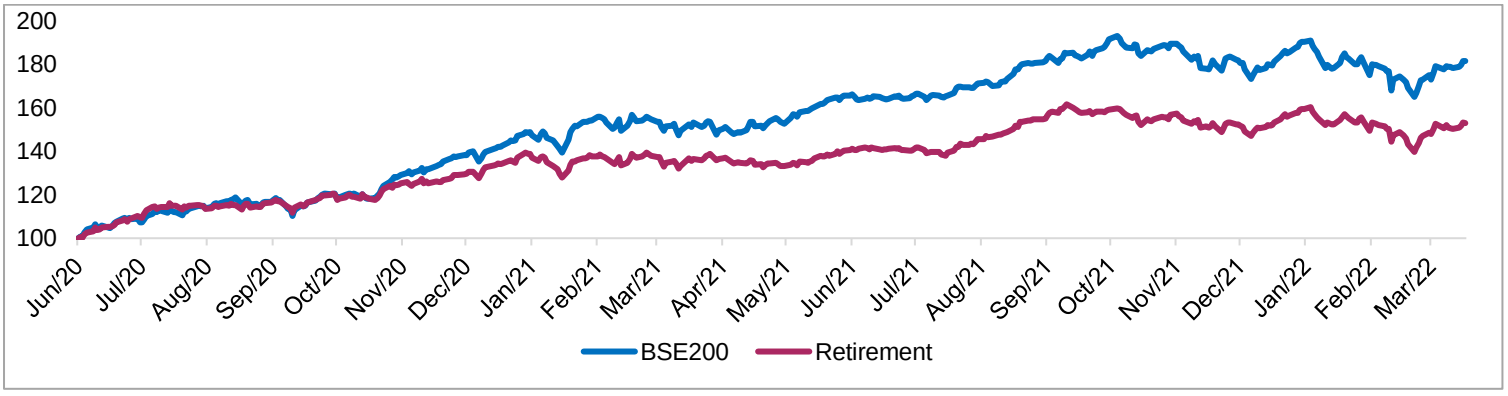
Portfolio Beta	0.82
Information Ratio	-0.63
Volatility	13.66
Sharpe Ratio	0.91

Sector Allocation



Market Capitalisation





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