Annual Equity Outlook – CY2022

Continuing on the Road to Recovery

Aditya Birla Sun Life AMC Ltd.
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Summary - View on the Market

- In 2021, global equity markets attained new all-time highs driven by strong corporate earnings growth even in the face of Covid-related restrictions, supply chain disruptions, rising oil prices, and higher labor costs. Headline valuations ended at a 15-35% premium to long-term averages across US, Eurozone and Emerging Markets. India was amongst best-performing markets globally.
- **2022 Outlook**
- Global equity markets likely to continue climbing a wall or worries on number of fronts – growth peaking out, high inflation, accelerated tapering and rate hikes, slowdown in China, new Covid variants, high valuations, etc., which may lead to high volatility.
- India, on the other hand, has just come out of the second covid wave and is catching up with the rest of the world. India's economy is recovering quickly as evidenced by strong macro data - better-than-expected GDP growth, PMI consistently in expansion zone, improved core sector growth, GST collections above Rs 1 lakh cr. for sixth consecutive month, narrowing of fiscal deficit and falling unemployment rate.
- Over next three years, **India likely to go back to its real GDP growth trend of ~6.5% with all three drivers of economy firing**.
    - **Consumption:** Discretionary consumption is picking up post Covid and should sustain given young demographic with rising incomes and aspiration levels.
    - **Investment:** Real Estate is at a beginning of a new cycle, private sector investment expected to pick up, and government spend on infrastructure development is expected to remain strong. India should continue to see strong FDI inflows.
    - **Exports:** Given the robust global economic recovery, exports have already recovered, and outlook remains positive. IT service companies have good tailwind, China+1 strategy is helping sectors like Textiles, Chemicals, etc.

Summary - View on the Market

- Currently, India seems to be in a relatively better position even when compared to other markets like the US:
    - **US:** GDP growth has peaked out and is likely to slow down, inflation is very high, interest rates are all-time lows and are likely to move higher, and corporate profit-to-GDP is close to all-time highs and likely to start moderating,
    - **India:** Economic recovery has just started, inflation is under control, interest rates are likely to be in a moderate range, and corporate-profits-to-GDP is at all-time low and should move higher.
- India also provides better visibility to economic growth and corporate profit growth than other Emerging Markets.
- Corporate earnings are likely to grow at a 15% CAGR over the next three years, which is higher than the long-term average.
- Given depressed earnings and high liquidity, valuation multiples for Indian equities are elevated. However, 2022 can be a year of transition as excess liquidity gets withdrawn and interest rates inch up. Hence, valuation multiples can be expected to normalize.
- Given the rally in markets in 2021, easy money has already been made. In the short term, market action may be more stock-specific and returns may be modest.
- However, on a medium-to-long term basis, we continue to remain positive on Indian equities and expect markets to continue to scale higher. Market breadth would continue to improve as the domestic recovery gathers momentum and Domestic Cyclicals should do well. Overall, we believe Indian equity markets can give returns slightly below earnings CAGR over next 3 years.
- Investors should maintain their target equity allocation and use any correction as an opportunity to add to their equity exposure.

2021 Review

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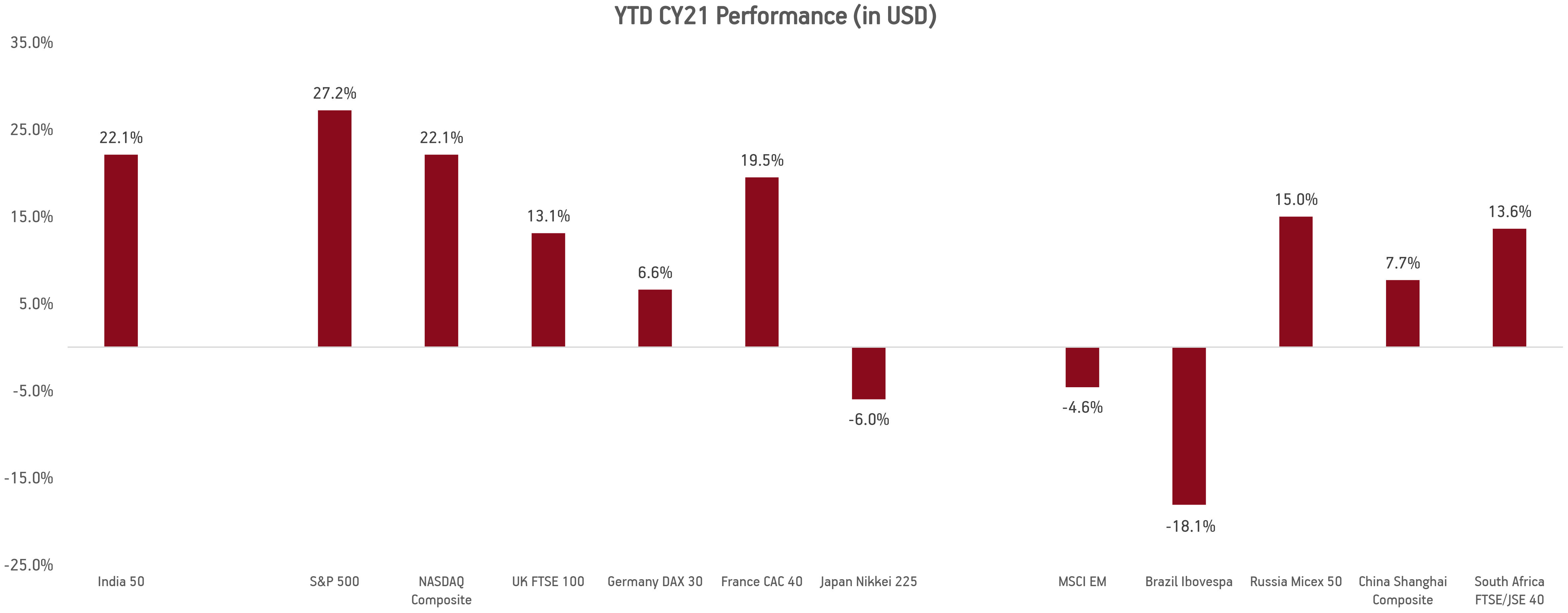
Global Equity markets have been strong; India amongst best performing markets



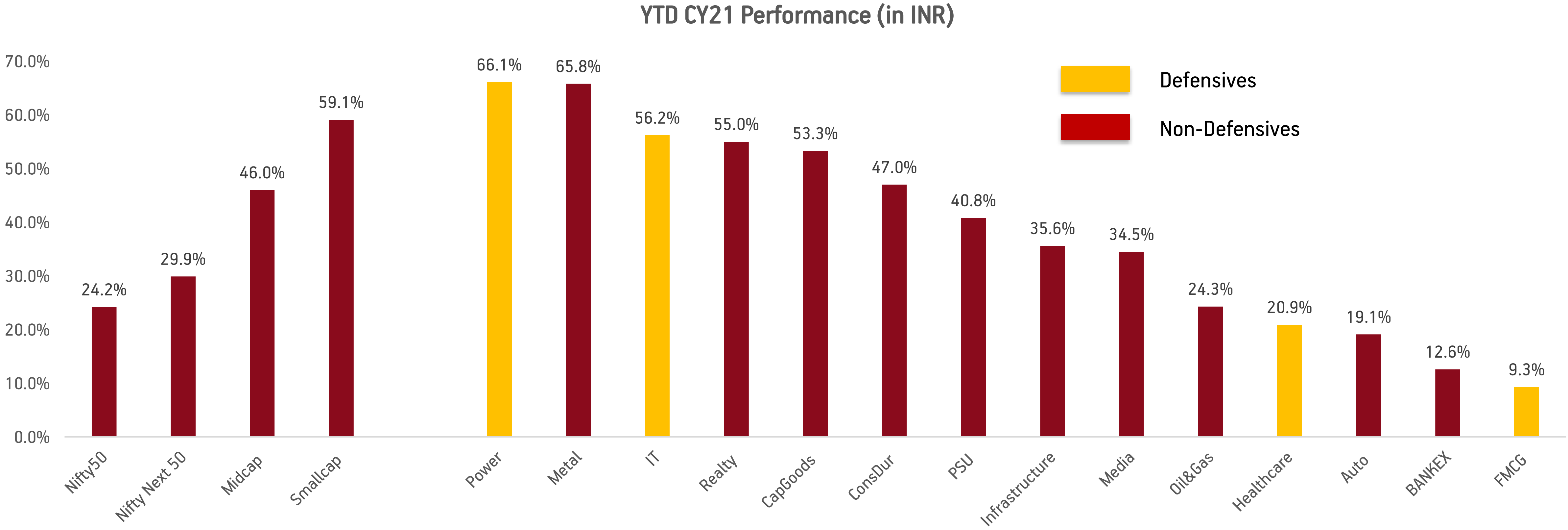
- In 2021, global equity markets attained new all-time highs driven by strong corporate earnings growth even in the face of Covid-related restrictions, supply chain disruptions, rising oil prices, and higher labor costs.

As of Dec 31st, 2021

Note: *NSE indices; Rest are BSE indices

Source: Bloomberg, ABSLAMC Research

In India, small-and-midcaps outperformed largecaps and Cyclicals outperformed Defensives significantly in CY21



- In India, market breadth improved significantly with mid-and-smallcaps giving more than 2x the returns of largecaps.
- Considering the quick recovery of the Indian economy from Covid, sectors such as Power, Metal, Realty, and CapGoods saw a sharp rise in earnings and returns.

Note: The sector(s)/stock(s)/issuer(s) mentioned in this presentation do not constitute any research report/recommendation of the same and the Fund may or may not have any future position in these sector(s)/stock(s)/issuer(s).

As of Dec 31st, 2021

Note: *NSE indices; Rest are BSE indices

Source: Bloomberg, ABSLAMC Research

Globally, valuations remain elevated as equity markets rallied post strong earnings results

12M Forward P/E across key geographies are at a premium to their Long-term Average

Country	Current	Start of the Year	Current vs Start of the Year	20Y Median	Current vs. Median
UK	11.7	14.1	-17%	12.6	-7%
Japan	14.2	18.2	-22%	14.7	-4%
EM	12.5	15.4	-18%	11.1	13%
Eurozone	15.1	17.6	-15%	12.8	18%
World	19.0	21.0	-10%	15.0	26%
US	21.0	22.8	-8%	15.5	35%
India	**21.8**	**25.7**	**-15%**	**16.9**	**22%**

- Headline valuations are at a 15-35% premium to long-term averages across US (driven majorly by rally in Technology stocks), Eurozone and Emerging Markets.

Source: JP Morgan, ABSLAMC Research

2022: Global Markets climbing a Wall of Worries

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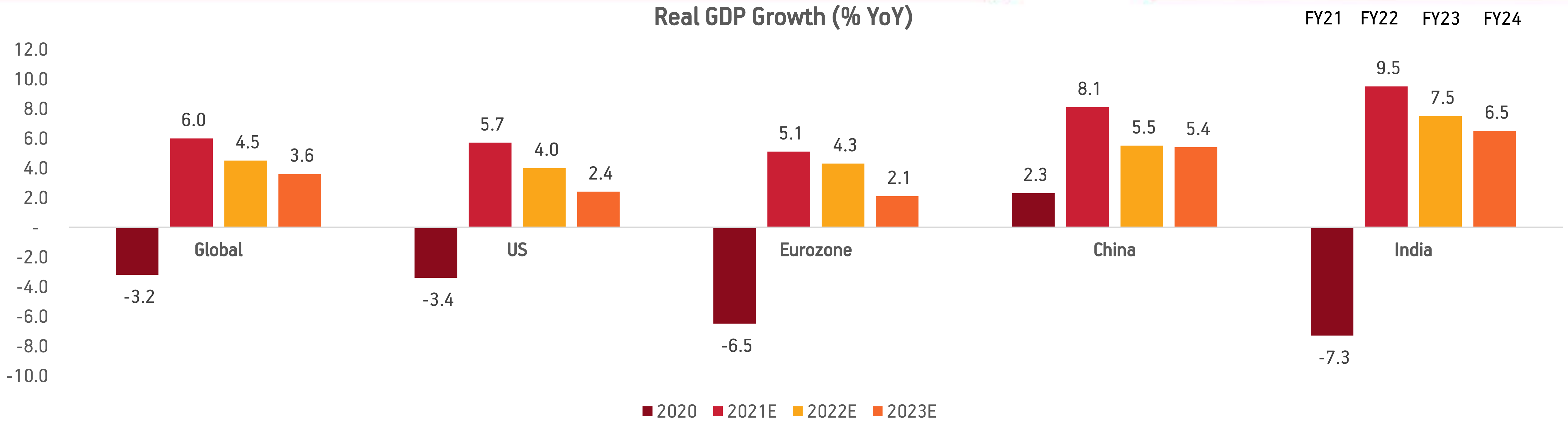
Global growth expected to slow down from the peak but remain strong

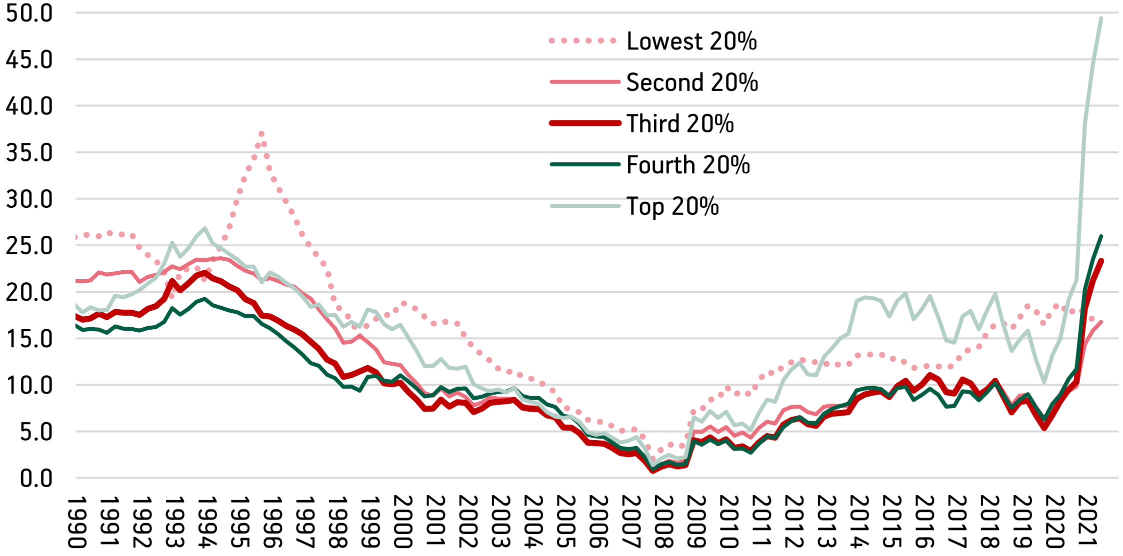


- Global economy is expected to remain strong in 2022 as drags from supply shocks fade and supports come from increased vaccination and normalizing household savings rate.
- In DM, households and corporates have built up excess savings and credit conditions are easy. Considerable pent-up demand remains in global services and inventories need to be rebuilt. As pandemic volatility fades, private sector should sustain above-potential growth.
- China's growth may remain subdued as its policy preferences shift toward addressing balance sheet overhangs and growth imbalances. However, India's growth should be strong as consumption, investments and exports are all firing.

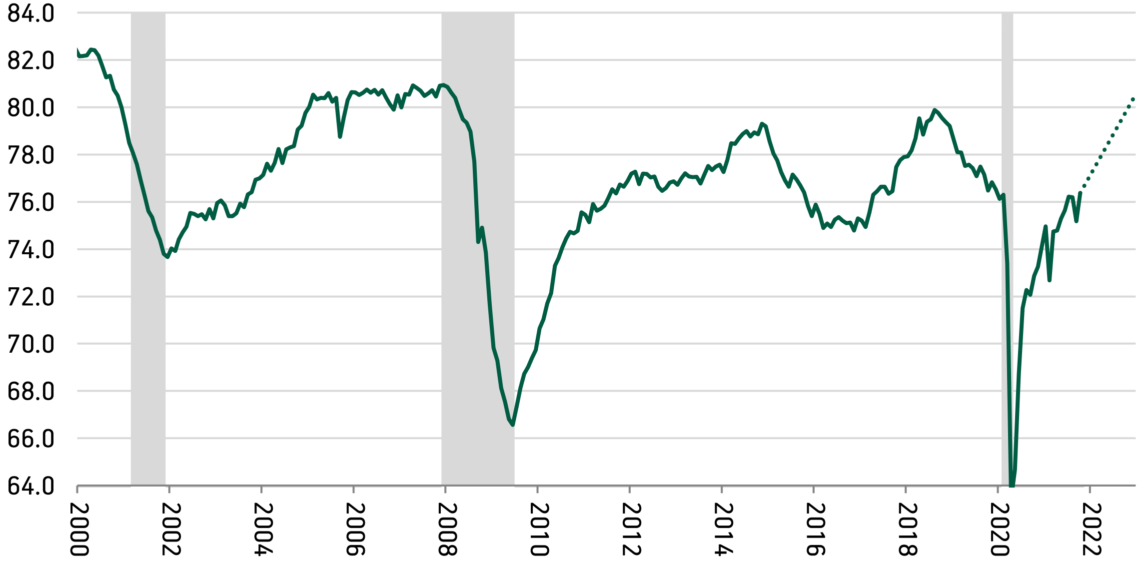
Source: Bloomberg, Goldman Sachs, ABSLAMC Research

USA – Growth to be driven by consumer spending and capex

Household Cash Holdings, % After-tax income



Capacity Utilization Rate (%)



- Consumer fundamentals are robust, with high savings, low leverage, rising house prices and low mortgage rates.
- A typical middle-income household has increased its cash savings from about three weeks' worth of after-tax pay, to three months. Excess savings, which in aggregate reached 12% of GDP, is one of the reasons why inflation is not causing demand destruction in US.
- Industries such as machinery, electrical equipment, apparel, chemicals have exceeded their pre-pandemic utilization rates and are looking to invest in new capacity. Govt capex is also expected to pick up with the passage of the infrastructure bill.

Source: Jefferies, ABSLAMC Research; Note: Grey bars indicate periods of recession

USA - Inflation should start moderating from Mar-Apr 2022

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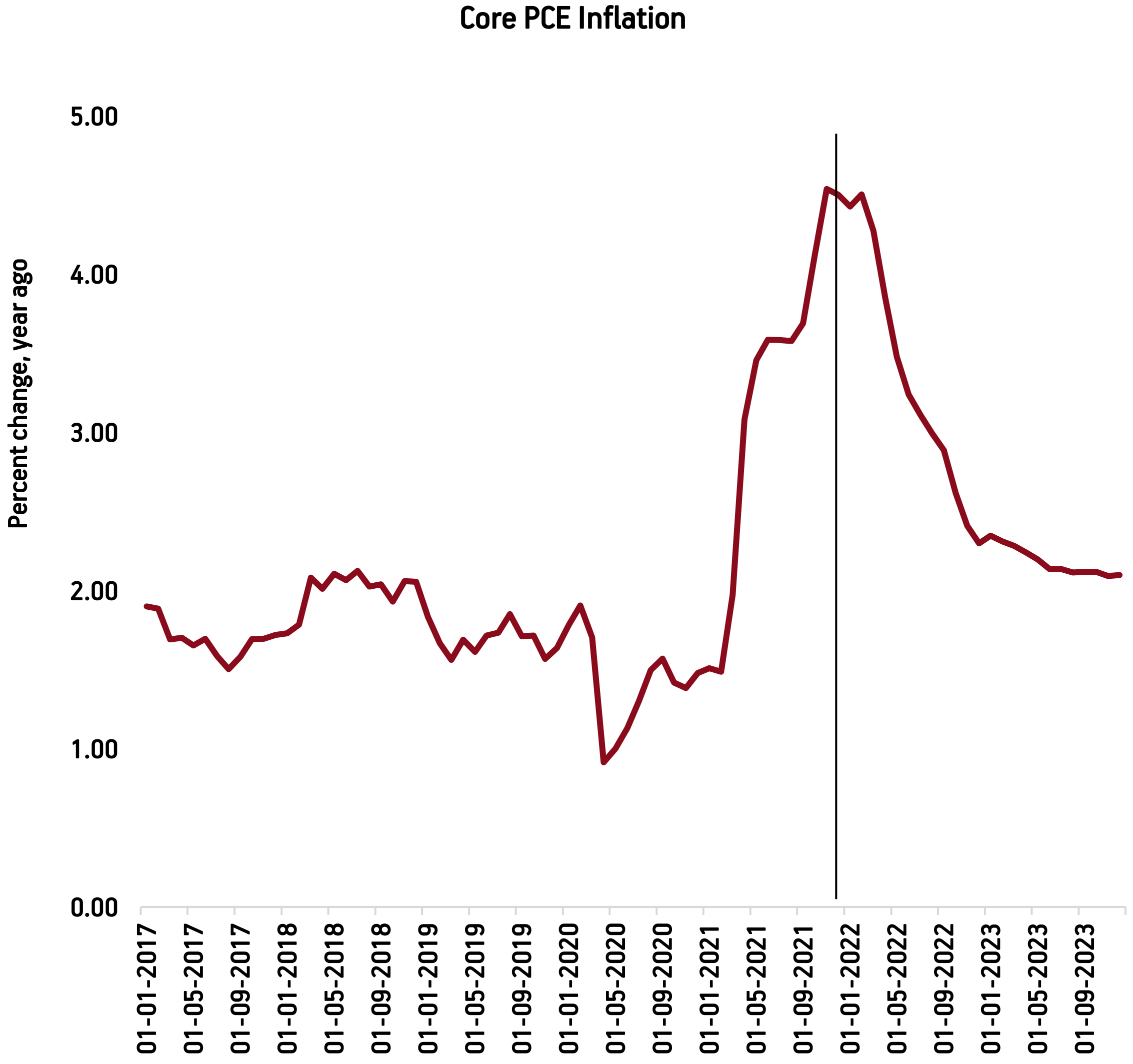
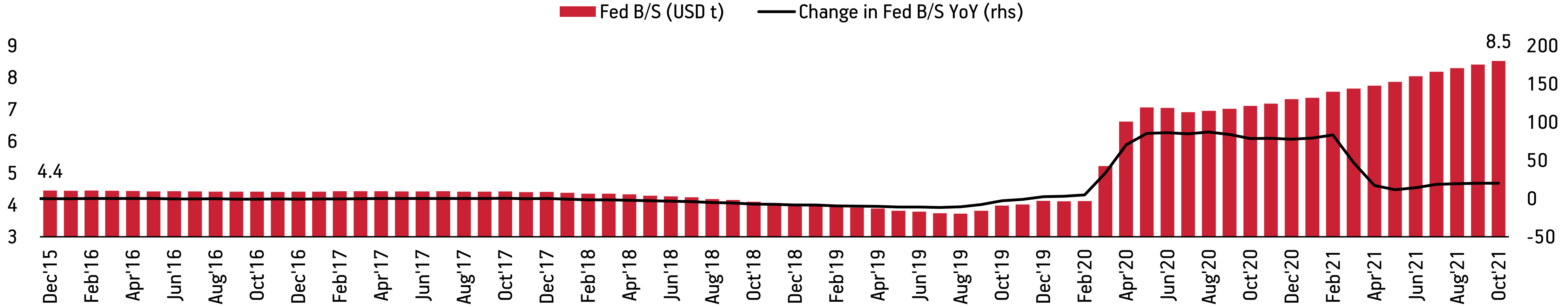


- Prolonged supply-demand imbalances, strong wage growth, and accelerating rents will leave core PCE high till early 2022.
- However, 2022 should see meaningful progress on resolving input shortages, labor shortages, and shipping delays. Production should start normalizing. As inventories normalize and demand moderates, prices should also normalize.
- US labour market is strong, but wage growth should slow as labor supply returns.
- Boost to inflation from the Commodities boom should also moderate in 2022.
- As supply-constrained categories shift from a transitory inflationary boost to a transitory deflationary drag, core PCE inflation show a declining trend.

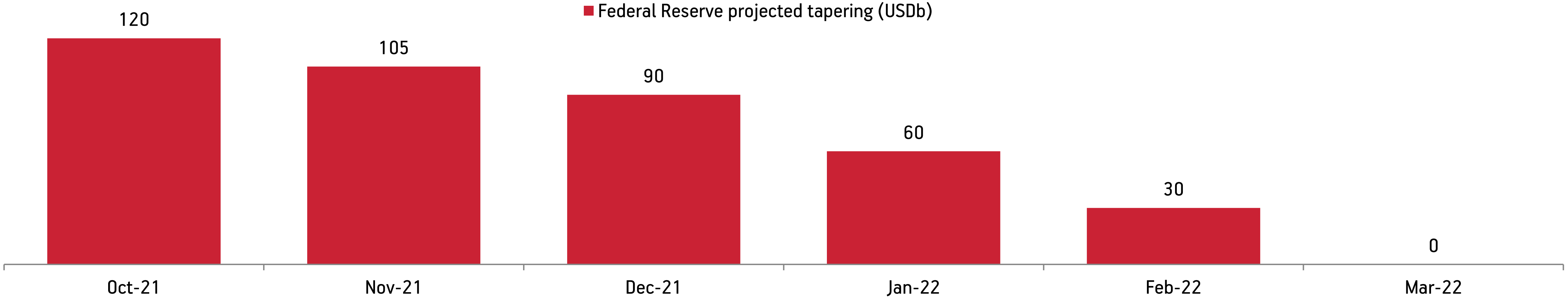
Source: Goldman Sachs, ABSLAMC Research

USA - Fed has accelerated its pace of tapering but Fed's Balance Sheet is expected to start shrinking only from 2023 onwards

Fed B/S has increased from USD 4.4t in Dec'15 to USD8.5t in Oct'21



Fed announced a doubling of its tapering from \$15Bn to \$30Bn per month



Source: Bloomberg, MOFSL, ABSLAMC Research

USA - Fed expected to start hiking rates in mid-2022

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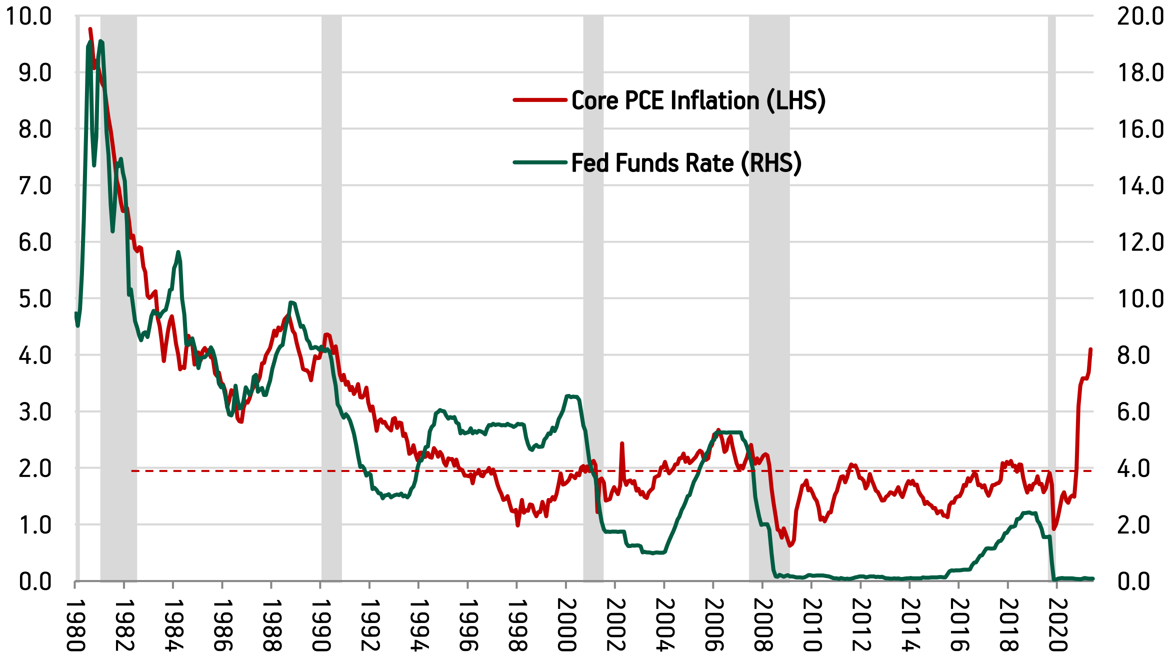
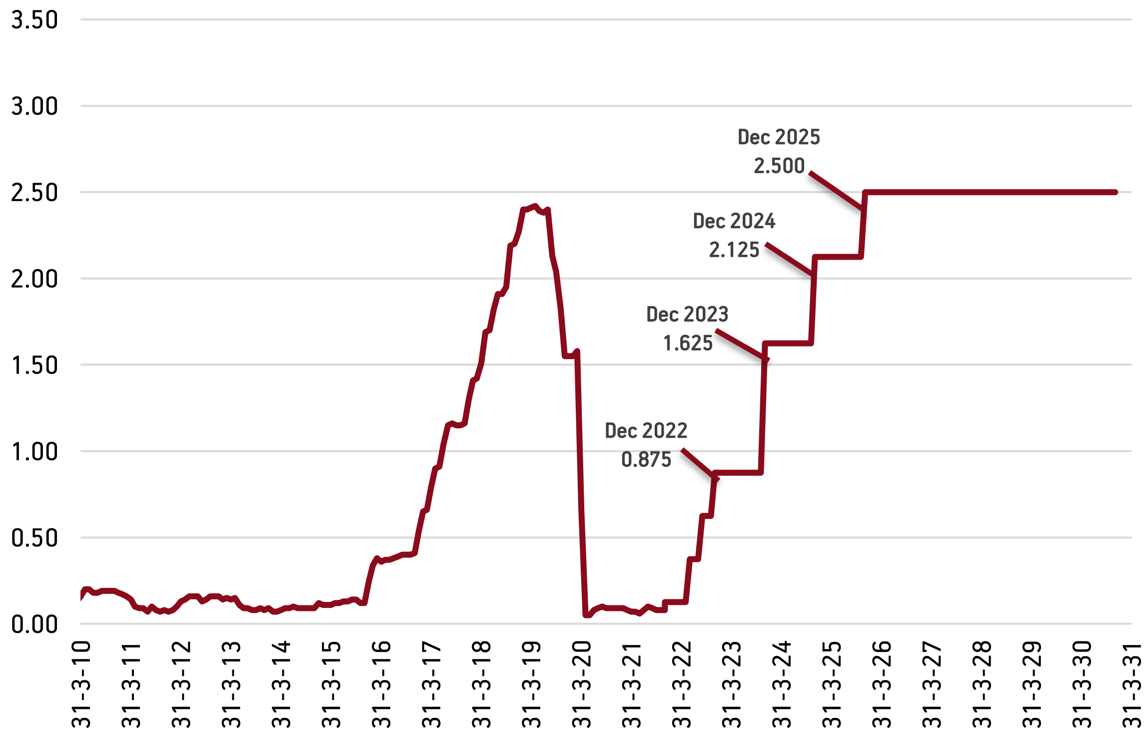
Fed Funds Rate vs Inflation



Fed Funds Rate projection



- Fed has highlighted inflation as the #1 risk currently.
- Fed expected to make the first-rate hike in the second half of CY2022 (with total 3 hikes in CY2022, followed by 3 hikes in 2023 and 2 hikes in 2024). Other global central banks likely to follow the Fed's lead.

Source: Jefferies, ABSLAMC Research; Note: Grey bars indicate periods of recession

USA - 10 year bond yields have been rising but are still below 10-year average

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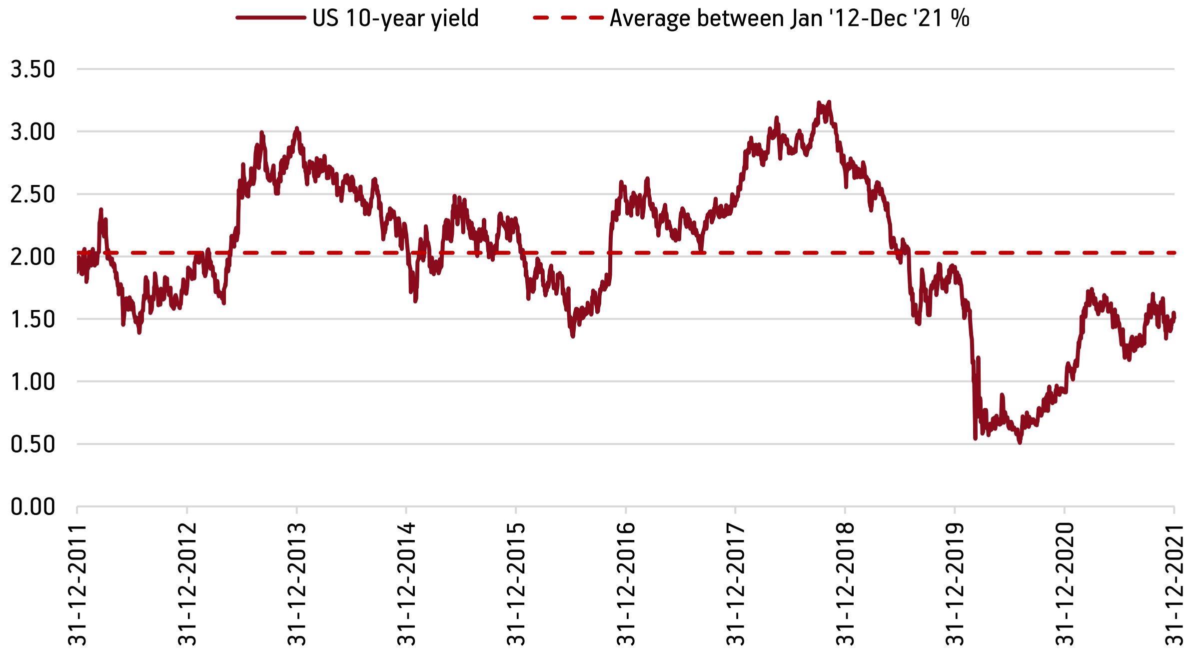
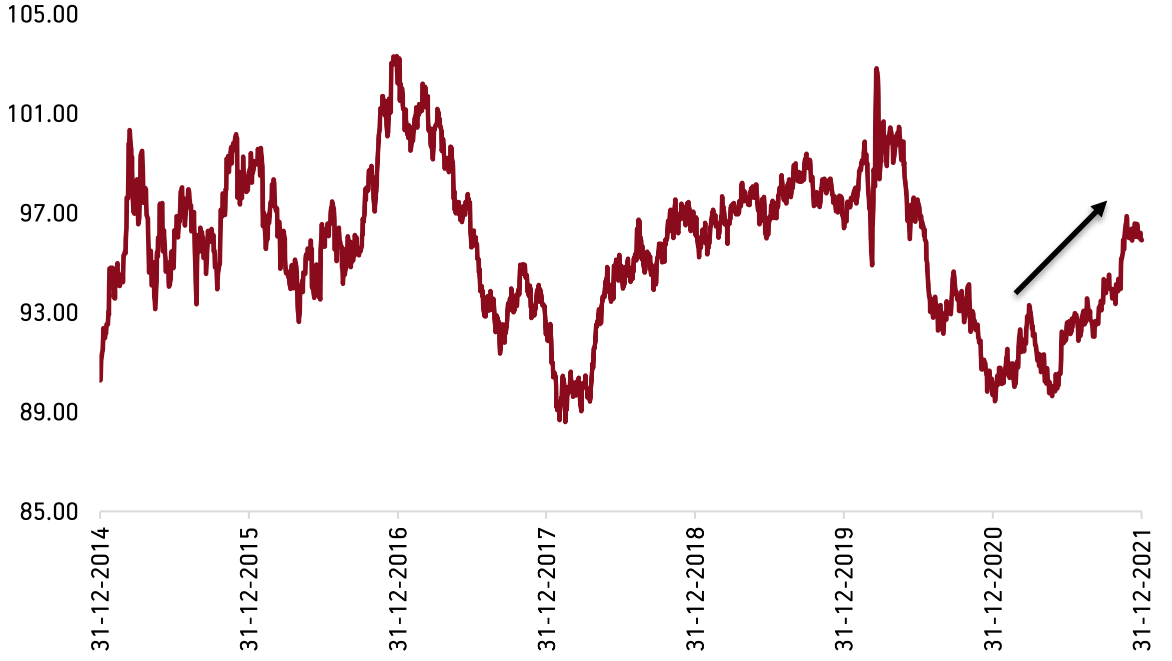
US bond yields have increased in CY21 but remain below 10-year average



Dollar Index which has been inching up is expected to increase further in 2022

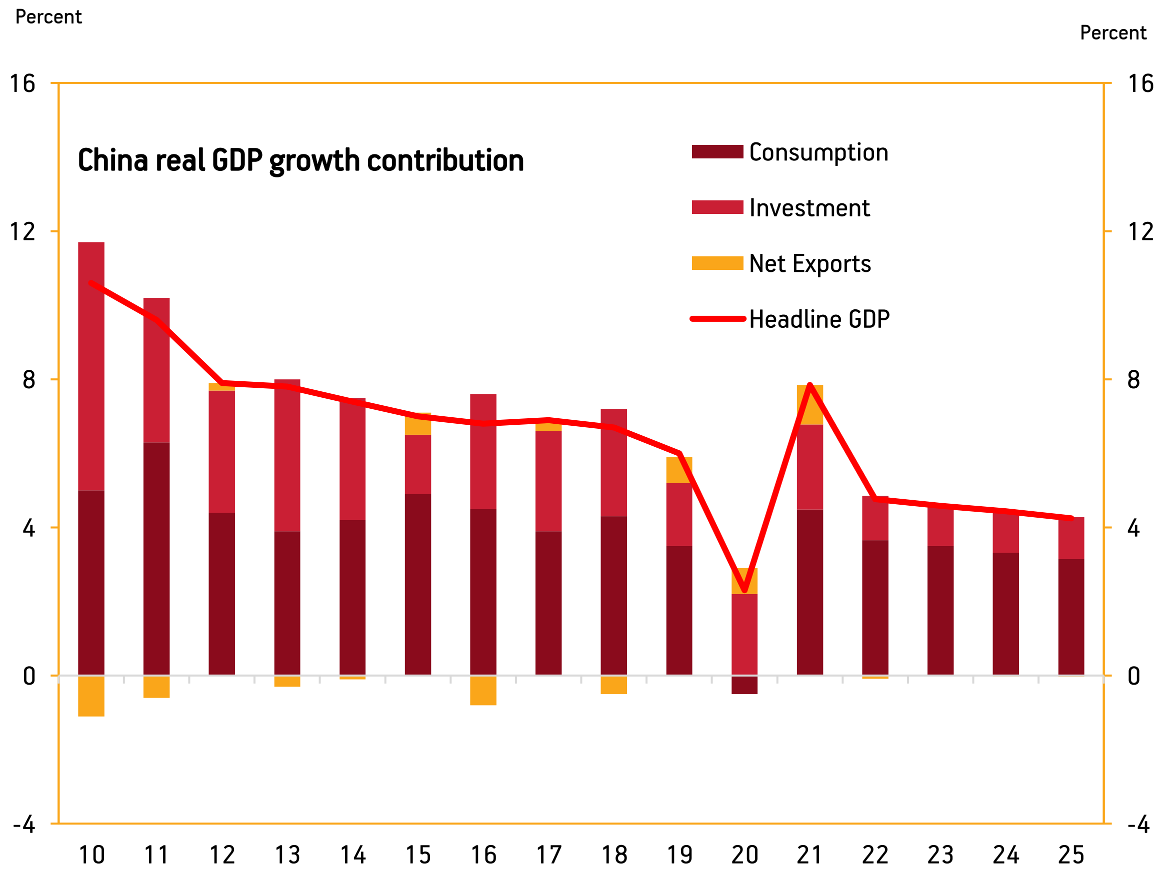


- US 10-year bond yields are still well below the long-term average and are expected to reach the long-term average level of 2% only by Dec 2022.
- With nominal yields rising and inflation falling in 2022, real yields are also expected to move up but remain negative till 2023.
- As real yields rise, USD is also expected to appreciate to a DXY level of 97-98 by mid-2022.

Source: Morgan Stanley, Bloomberg, MOFSL, ABSLAMC Research

China - a policy regime change is underway that is leading to growth slowing down

China – A slower and less investment driven growth model



- Economy has been impacted by slowdown in property activity, power shortages, Covid Zero approach leading to tight restrictions, elevated PPI inflation, and regulatory reset.
- While policies geared to fuel innovation and supporting high-value-added industries (green tech, biotech, computing) should support growth, most other policies have the effect of damping near-term growth in the hopes of longer-term gains (financial stability, de-carbonization, and a reduction in regional and income equality).
- Especially, the transformation in China's property sector is expected to potentially bring out a slower but more balanced and resilient growth model.

Source: Morgan Stanley, Goldman Sachs, ABSLAMC Research

China - Nearly a quarter of the economy would be affected by property slowdown

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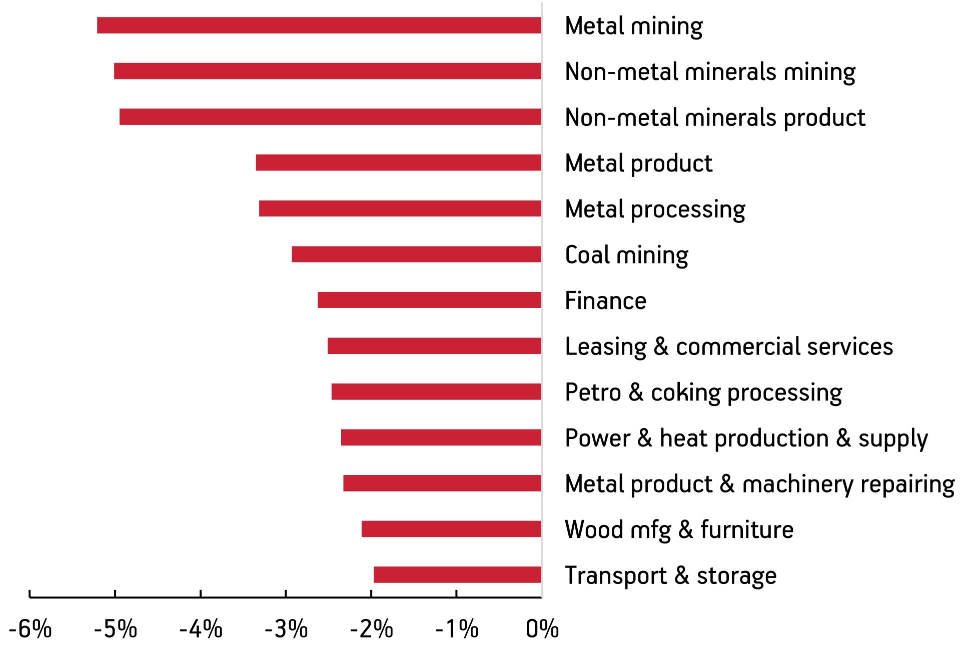
Construction and real estate shares of China's economy

Shares of GDP, based on China 2018 IO table

	Domestic value-added based on: Final Demand
Construction	**24.5%**
Residential buildings	12.4%
Non-residential buildings	5.3%
Infrastructure/other	6.8%
Real Estate Services	**5.6%**

Industries in China most affected by property slowdown

Impact of 10% decline in property activities on sector output (%)

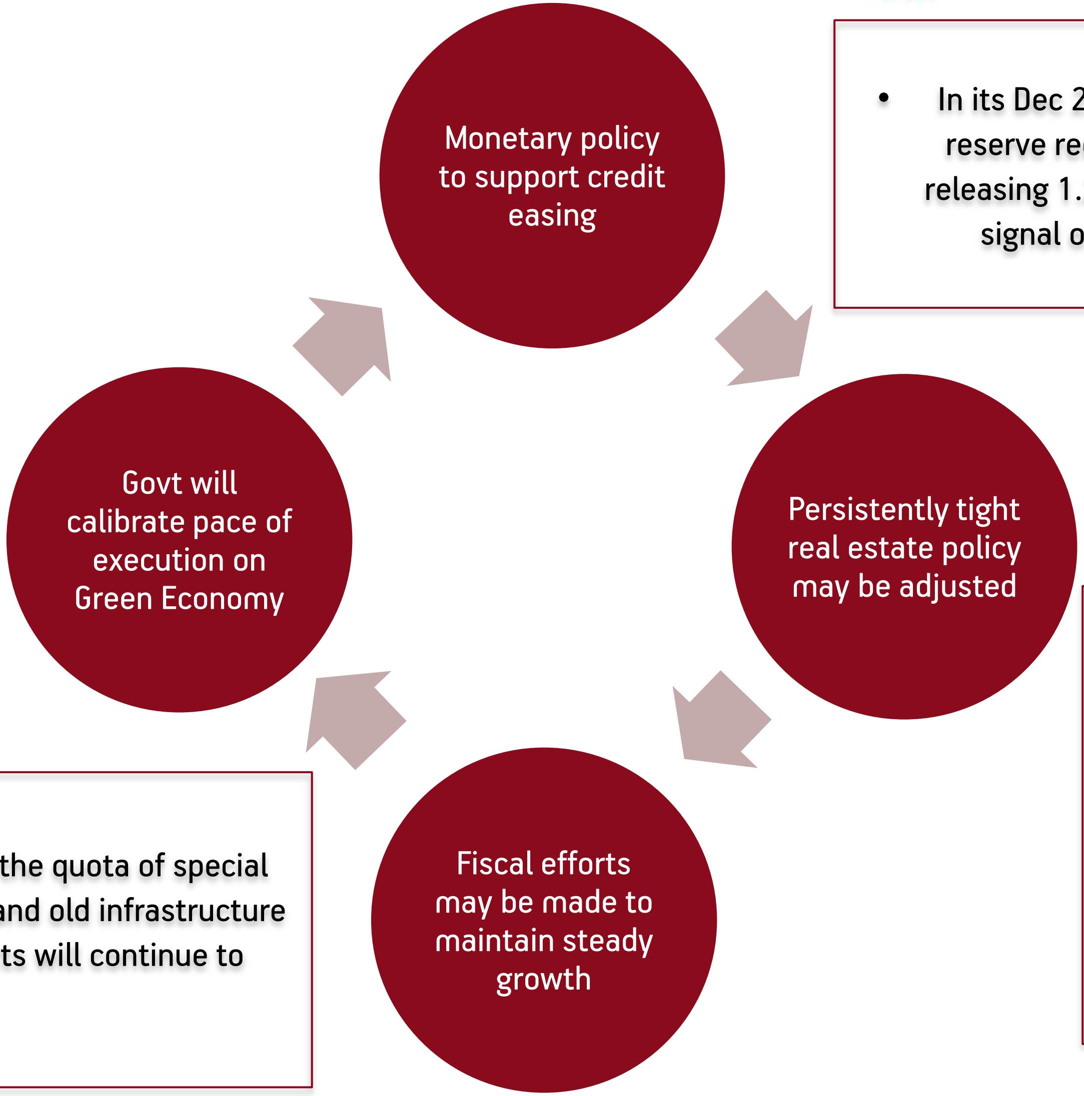


- As the property sector has many linkages to China's real economy, especially when all the goods and services used in building properties are taken into account, nearly a quarter of the economy would be affected by a property slowdown.
- The main channel of contagion of China's property downturn on global growth is likely through trade, especially imports of commodities (minerals and metals especially), as demand for construction materials, machinery, appliances and automobiles drops.

Source: UBS, Goldman Sachs, ABSLAMC Research

China - Going forward, policy is expected to focus on stabilizing growth

- Green economy is part of the 14th Five Year Plan. Govt. will calibrate pace at which they pursue this goal and will not disrupt economy.



- In its Dec 2021 policy, People's Bank of China reduced the reserve requirement ratio by 0.5 percentage points, thus releasing 1.2 trillion yuan of liquidity. RRR-cut sends a clear signal of monetary policy easing to support growth.

- The government may reasonably speed up the approval of housing loans and moderately relax constraints on the amount of housing loans to give normal credit support to real estate enterprises, maintain the overall stability of the real estate market and protect the legitimate rights and interests of housing consumers.

- The government is expected to raise the quota of special bonds for 2022; also support for new and old infrastructure projects and basic livelihood projects will continue to increase.

Source: Haitong, Bloomberg, ABSLAMC Research

Emerging Markets – Facing slower growth with gradual tightening of global and local monetary conditions

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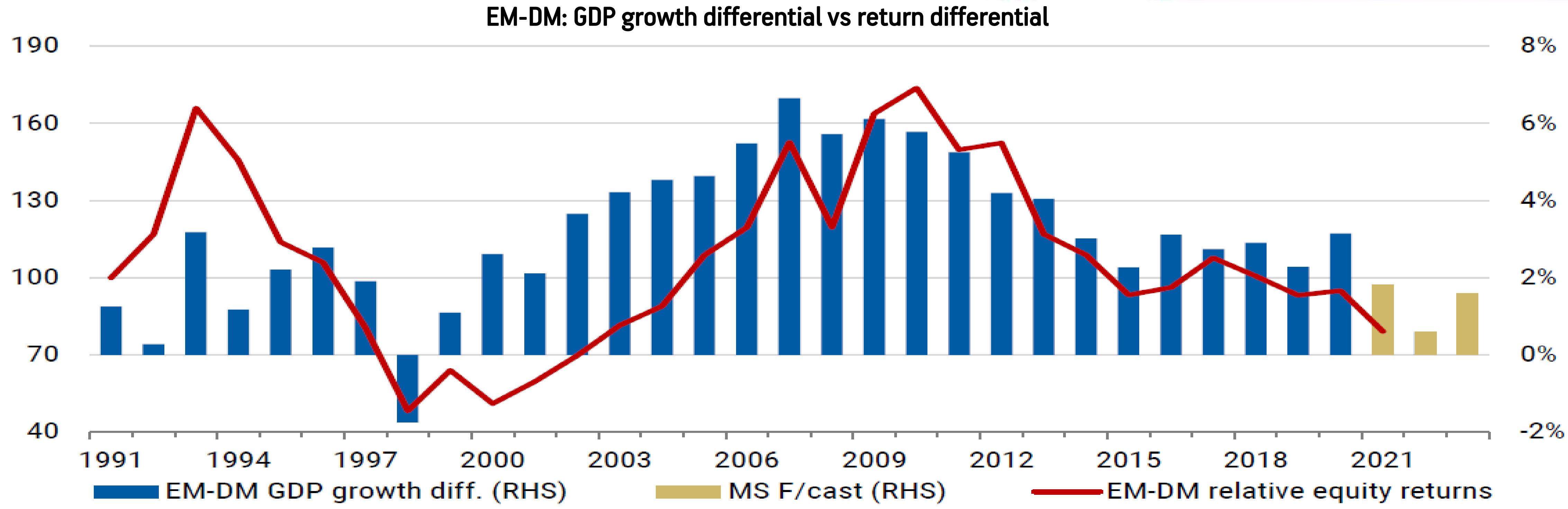

- Growth is slowing from peak rates globally as the reopening boost fades. Material reversion of spending from goods to services is expected going forward. Goods exports from EMs likely to be much weaker, especially in the WFH-boosted segments. Slowdown in China will also impact growth in other Asian EMs. **India would be one of the fastest growing countries in EM.**
- Rates expected to head higher both in DM and EM. US dollar strength would also be a continued headwind for EM.
- However, EMs like India and China whose external debt position (import cover, external debt/GDP) is superior to other EM countries are relatively better placed in case of policy tightening globally.

Source: Morgan Stanley, ABSLAMC Research

Covid - New Covid variants remain a risk in 2022 but playbook to manage Covid is well understood now

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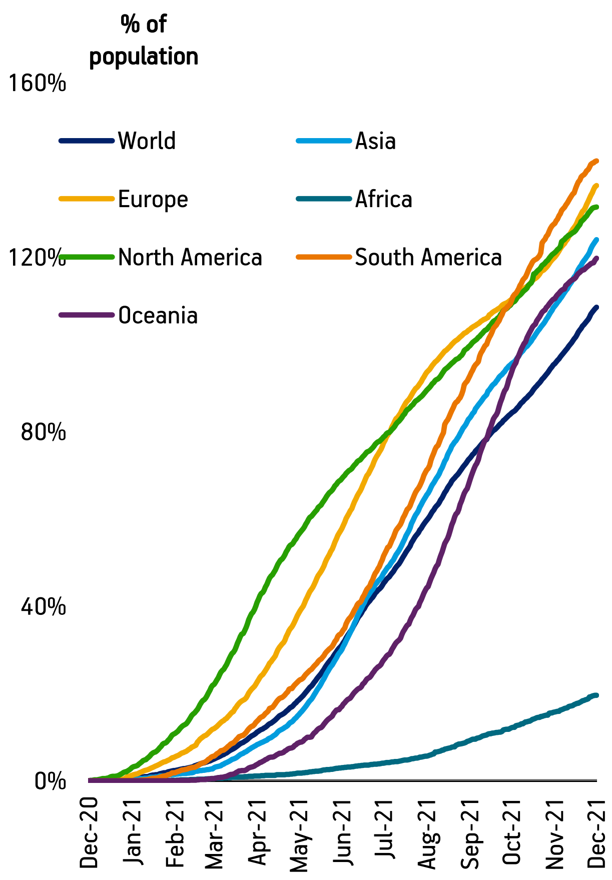
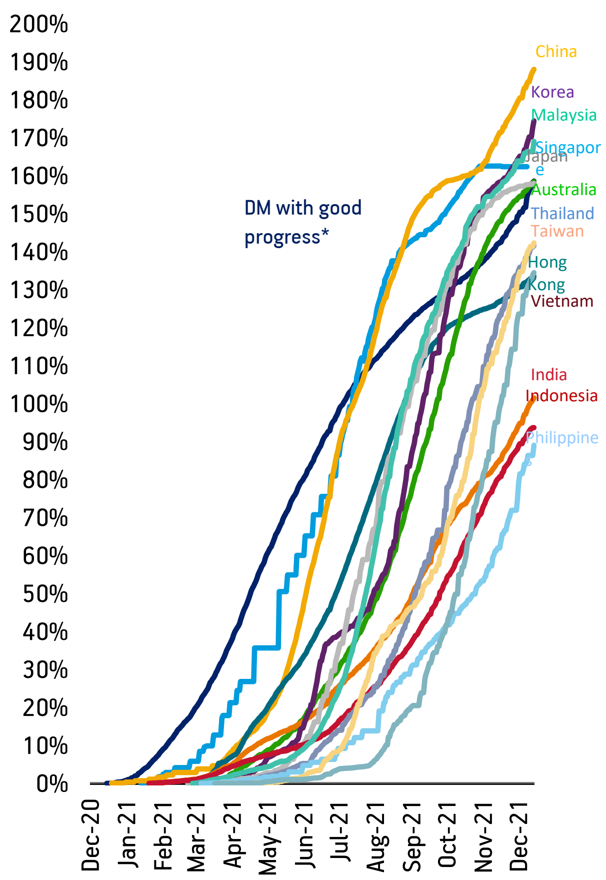
Vaccination Progress by Region



Vaccination Progress in Asia



- New Covid variants such as omicron could potentially disrupt the economic recovery.
- In a best-case scenario, variants such as omicron will turn out to be mild and vaccines would provide some protection against them. The economy might be moderately hurt in the short-term but should recover quickly.
- But even in a close-to-worse-case scenario, where these variants are partially vaccine-evasive and have a higher mortality rate, the downside for risk assets may not be enormous. Drugs companies believe they could roll out a tweaked vaccine within 100 days. Governments would provide fiscal and monetary stimulus.
- Overall, a big decline in Equity markets is not expected now since the risks and ways to manage them are better understood.

Source: BofA Securities, BCA, ABSLAMC Research

2022: India – On the Recovery Track

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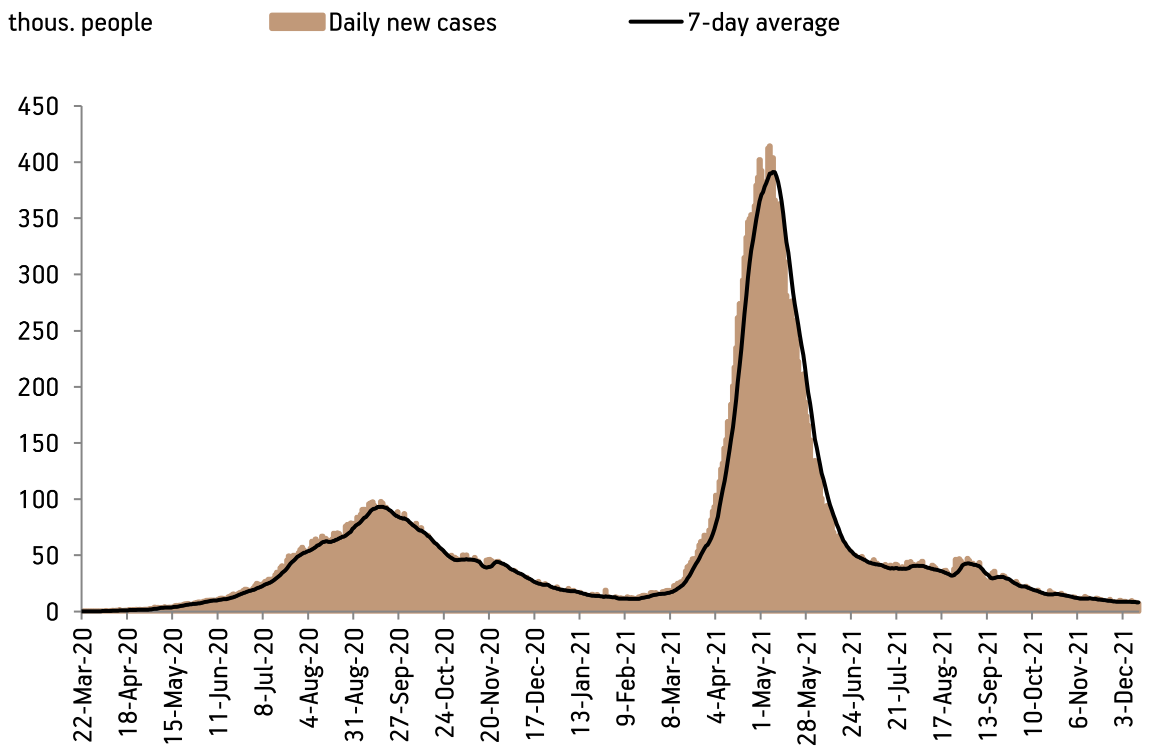
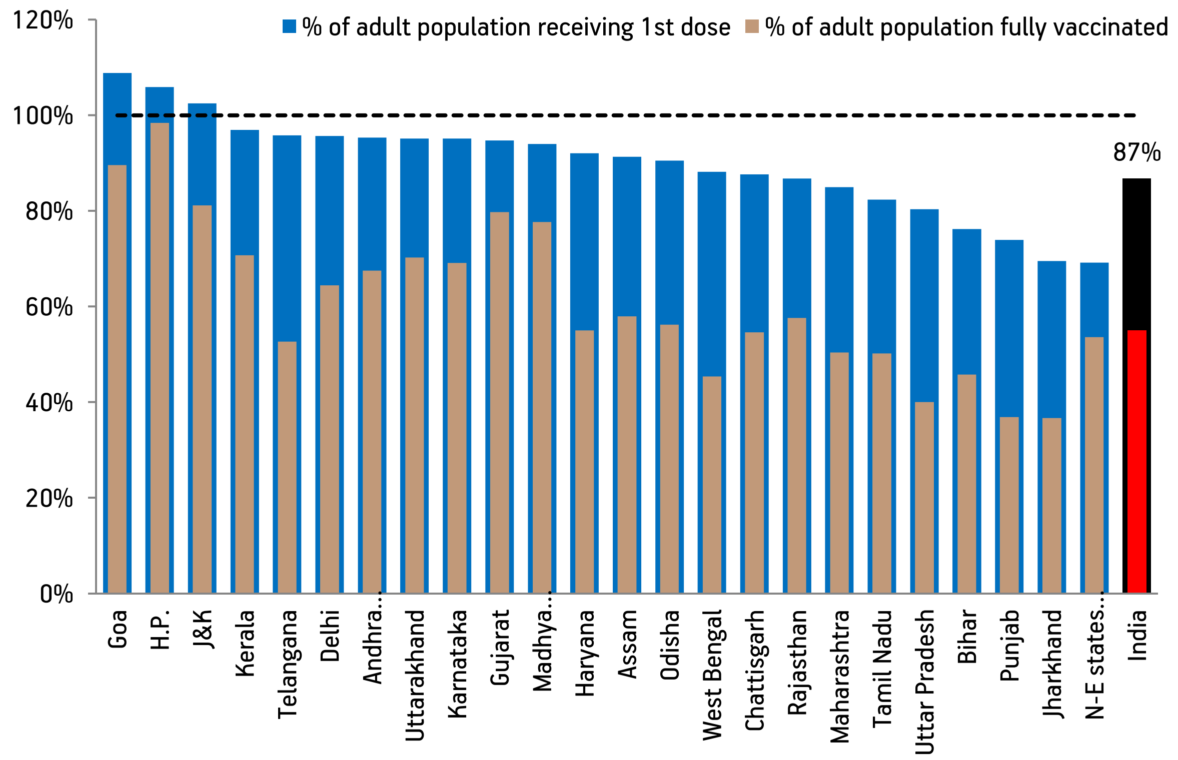


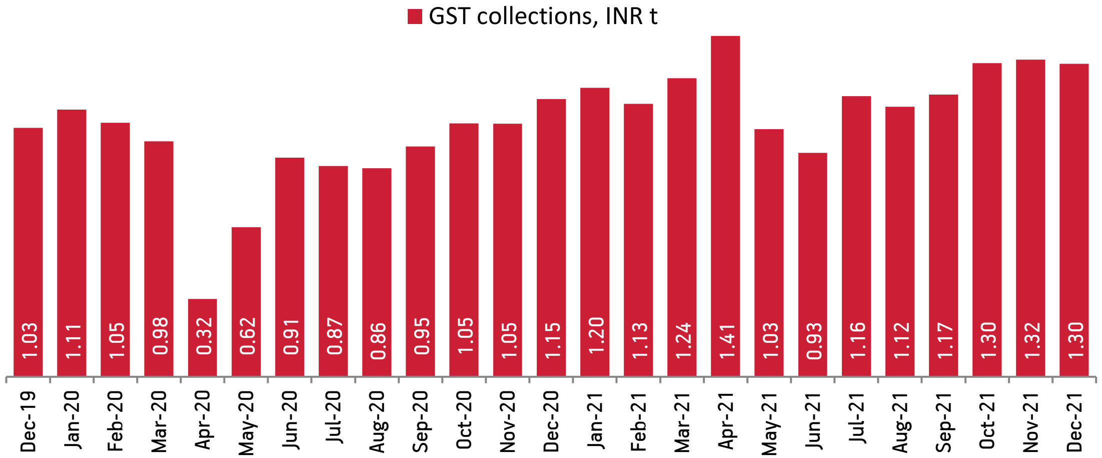


- Close to 90% of adult population in India (aged 18 and above) have had their first vaccination but only 55% of them are fully vaccinated.
- Marginal impact of successive COVID waves on mobility restrictions has been coming down, given growing fatigue with lockdowns and the fact that households and businesses have adjusted to the new normal.
- Apart from the new omicron variant, India is seeing very few fresh Covid cases.

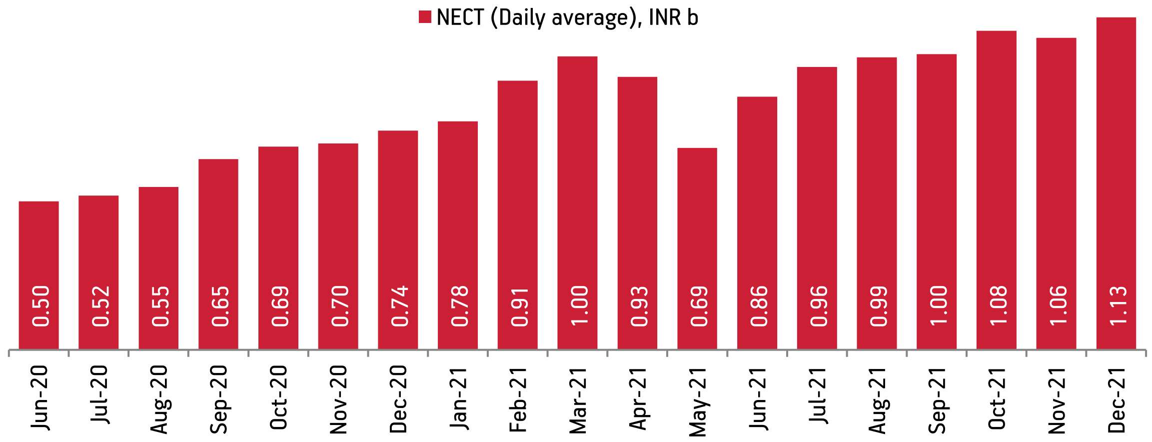
Source: UBS, ABSLAMC Research

Indian economy is recovering quickly from Covid impact; High performance indicators continue to improve

GST collections more than 1 lakh crore for sixth consecutive month

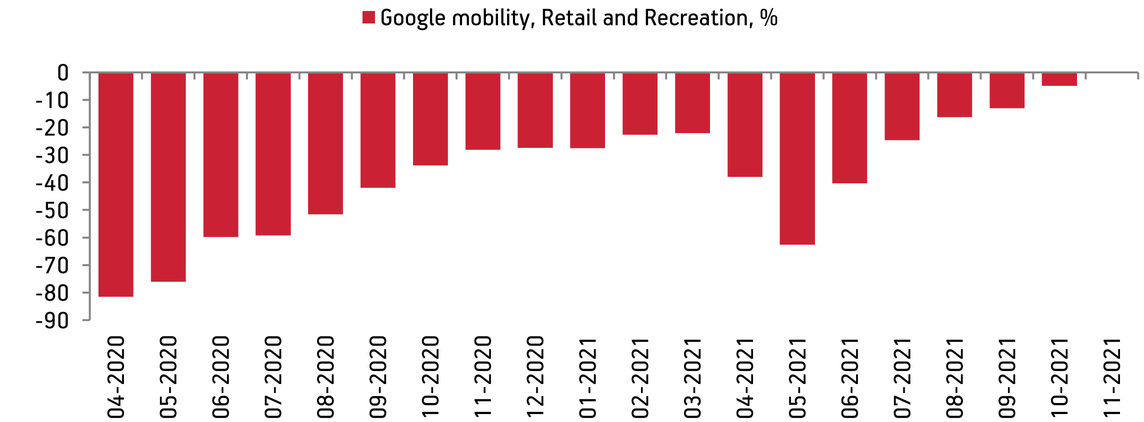


National Electronic Toll Collection (Daily) at record high of INR 1.13 Bn

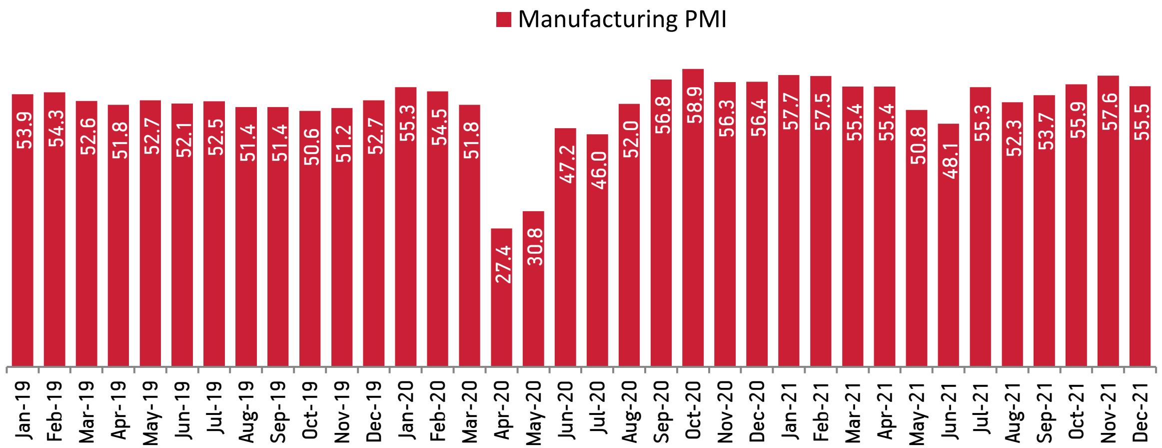


Dec'21 data is average upto 6th Dec'21

Mobility indicators are showing a quick recovery

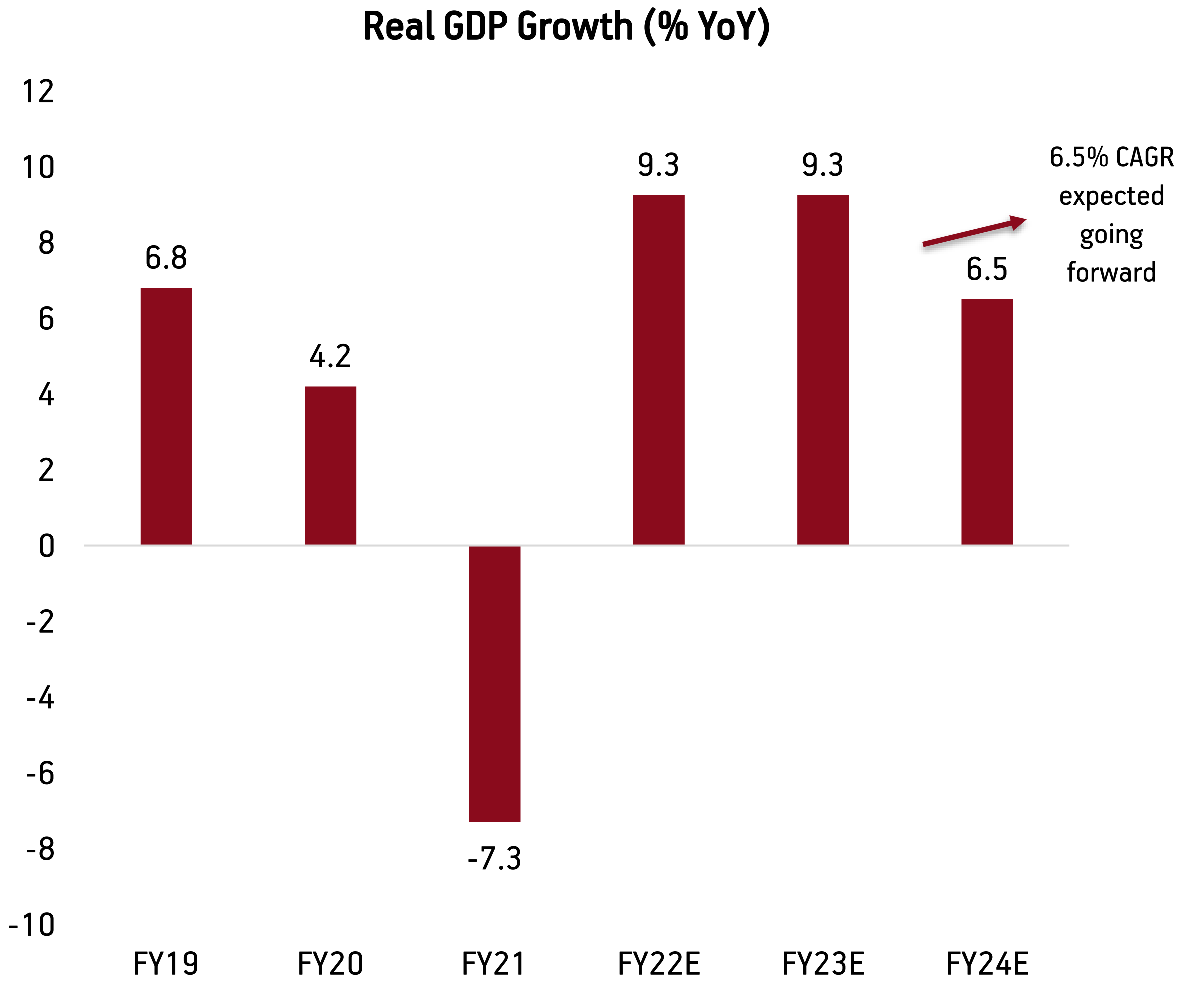


Manufacturing PMI continues to be in the expansionary zone



Source: Motilal Oswal, ABSLAMC Research

India's GDP growth to remain strong in FY23 and normalize by FY24



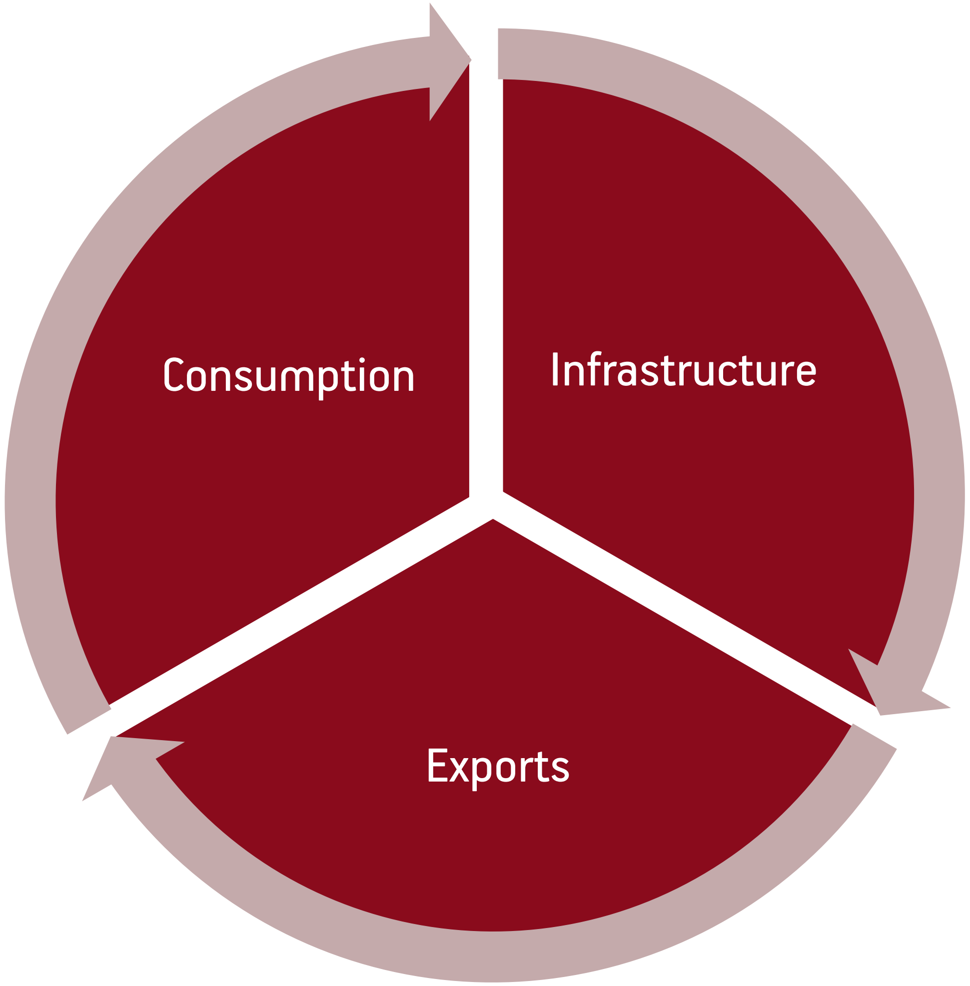
All the three growth drivers are expected to fire over the next 3 years:

- **Consumption:** As remaining mobility restrictions are removed and activity recovers, discretionary consumption should normalize.
- **Investment:** Uptick in real estate sector, government spend on infrastructure, and uptick in private capex should boost investment.
- **Exports:** With global economic growth expected to remain above trend, exports should also be strong.

Source: ABSLAMC Research

Consumption, Infrastructure and Exports to act as growth levers going ahead

- Several structural drivers (Gen Z, women workforce participation, change in customer tastes/ preferences) in place to drive discretionary consumption over the medium-to-long term;
- Share of discretionary spend in the consumer wallet expected to accelerate further to ~40% in FY30 vs. 24% in FY20 and 15% in FY05.



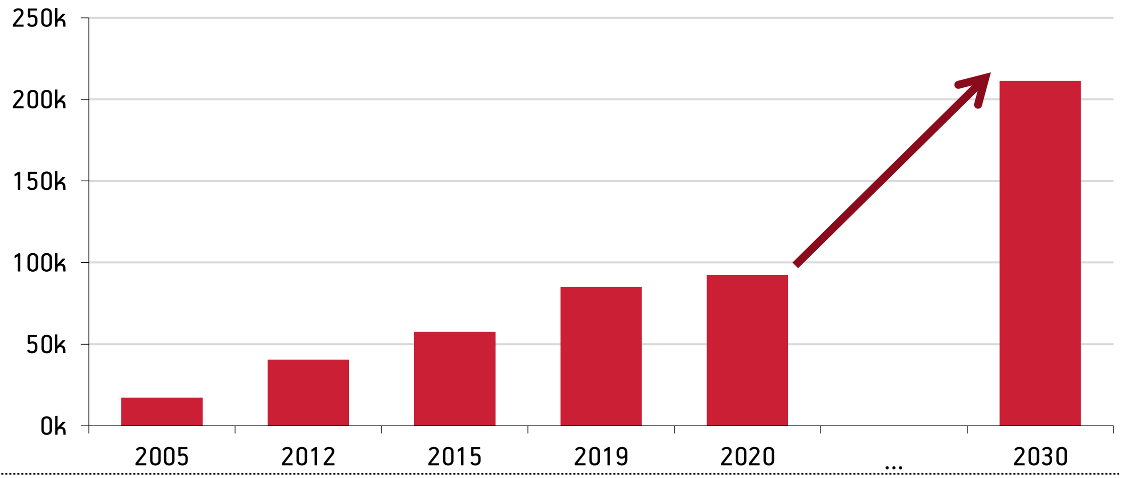
- Improved affordability expected to drive housing demand;
- Corporates are in a good position to invest as demand conditions improve and capacity utilization rises;
- Capex cycle has bottomed out and should pick up. PLI Schemes should help.

- Latest PMI indicators globally point towards robust manufacturing activity across most geographies, hence exports expected to pick up going ahead;
- India also likely to be a key beneficiary of China+1 model, especially in sectors such as textiles, specialty chemicals, manufacturing etc.

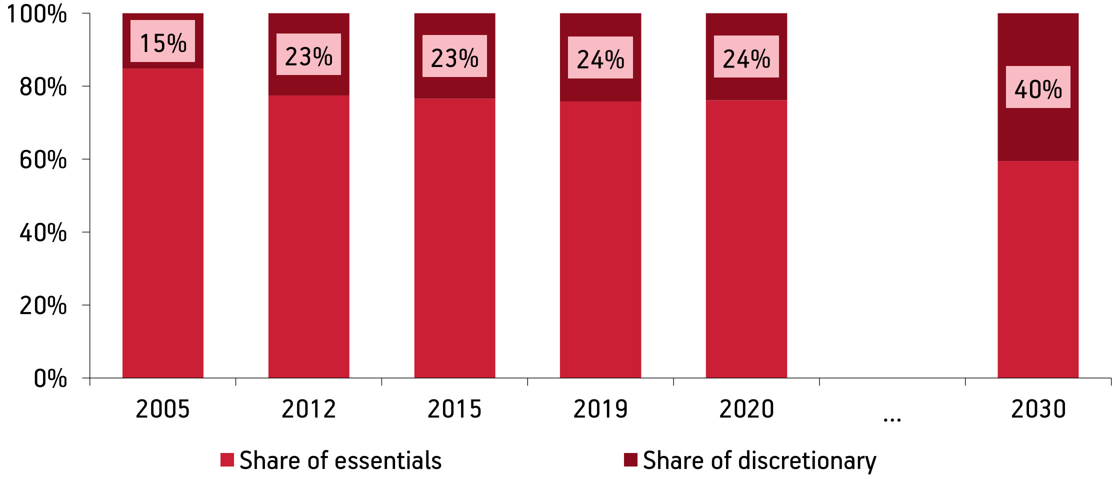
Source: ABSLAMC Research

Consumption - Demographics Tailwind to boost discretionary consumption

Aggregate Annual Household Consumption (Rs/capita)



Annual Household Spending Share



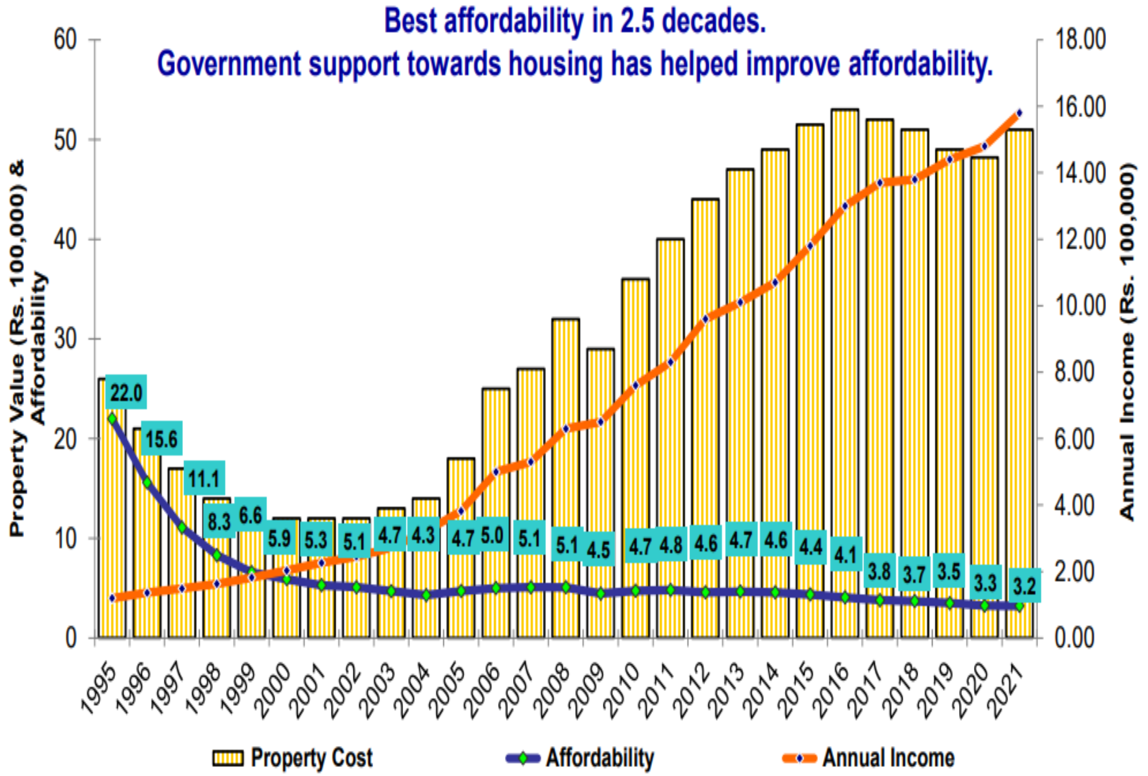
Several structural drivers in place to drive consumption over the medium-to-long term.

- India has one of the youngest populations globally and should enjoy this benefit going forward. The cohort of Gen-Z/millennials is well exposed to brands and hence amenable to a quicker path towards premiumization.
- India's consumer wallet would increasingly move towards discretionary consumption with the share of discretionary spend in the consumer wallet accelerating further to ~40% salience in FY30 vs. 24% in FY20 and 15% in FY05.
- Increase in consumption of discretionary categories like beauty and personal care, where current penetration levels are low.
- Growing preference for organized retailers/known brands in grocery, apparel, footwear, and jewellery.
- Increased eating-out frequency/packaged food consumption, as we see increased workforce participation among women.

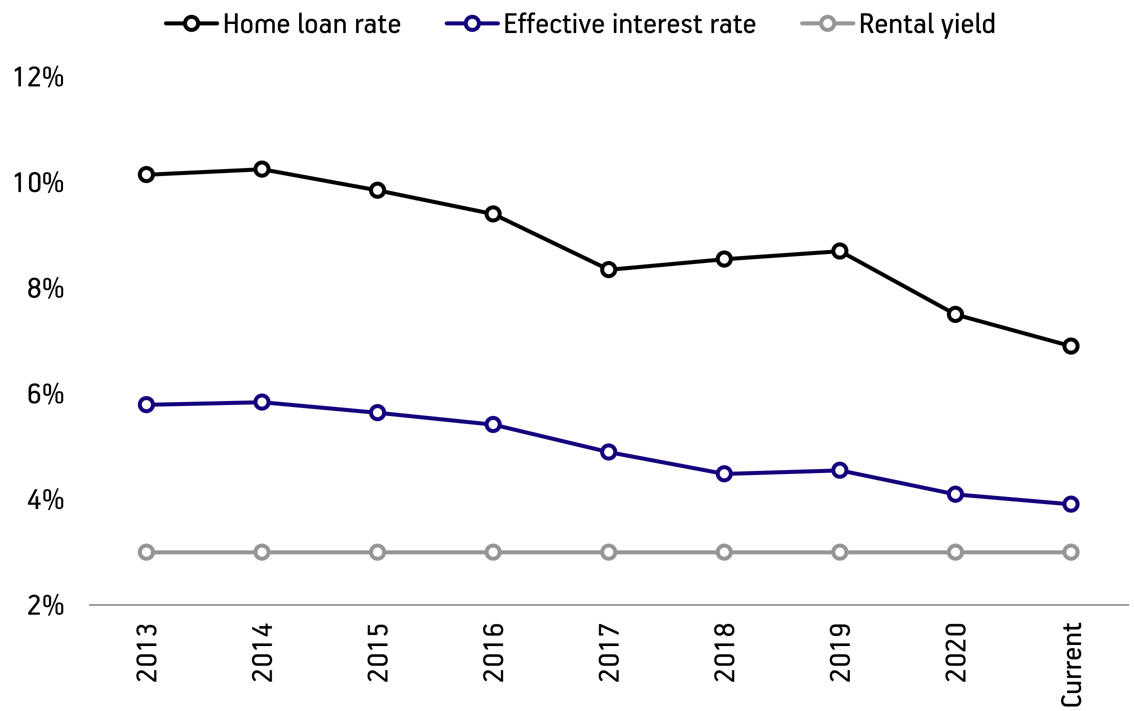
Source: CSO, IndiaDataHub, Macquarie Research, ABSLAMC Research

Investment - Improved affordability and consolidation to drive housing demand

Affordability has increased



Decadal low interest rates have further enhanced the affordability of home ownership

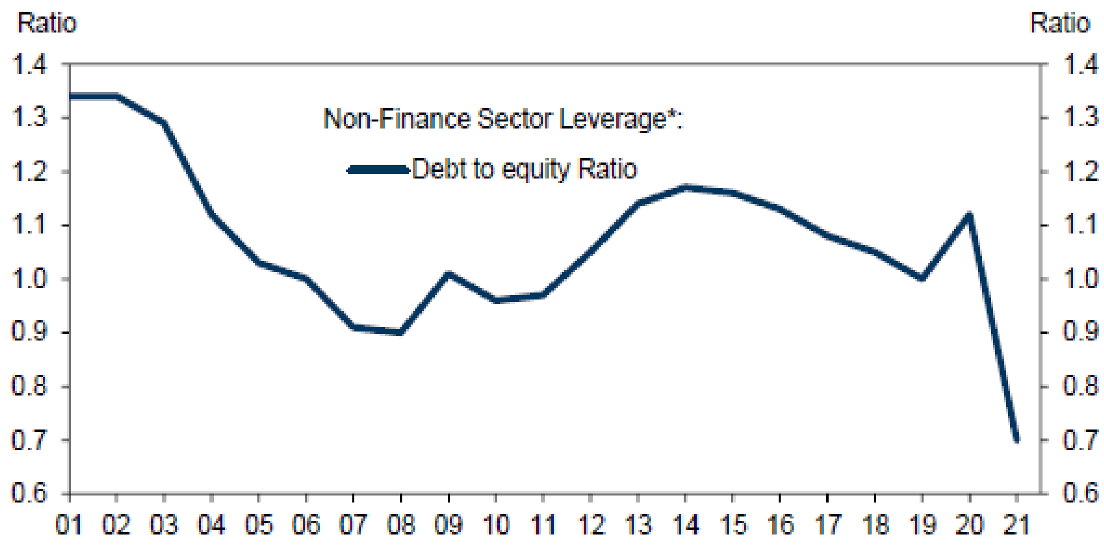


- Overall, affordability levels are at the best ever as prices have remained stagnant over the past five years, but incomes have increased.
- Home loan rates are also at decadal lows. Work from home trend has led to increased residential sales in urban areas.

Source: HDFC, MOFSL, ABSLAMC Research

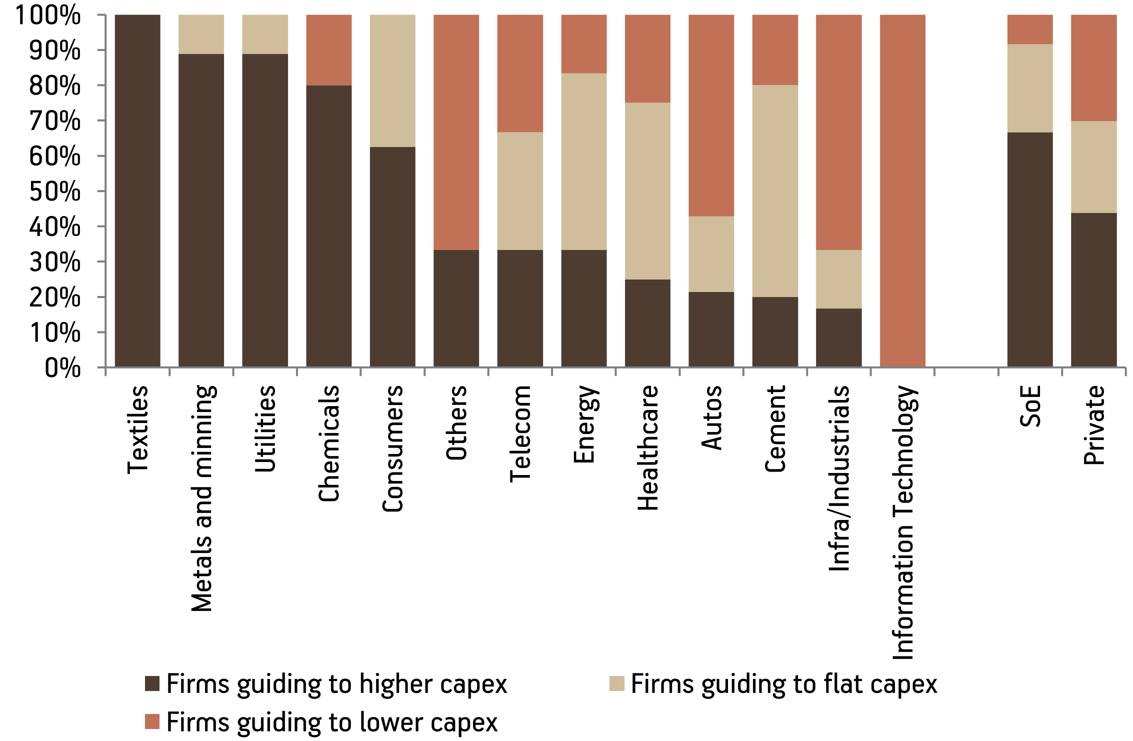
Investment – Corporates in a good position to invest as demand conditions improve and capacity utilization rises

Indian Corporate have deleveraged during the Covid pandemic



*Years are in Fiscal year. Fiscal year 2022 refers to April 2021 to March 2022. FY21's estimate are out of short sample (~5,000 corporates) compared to FY12 to FY20's estimates (~20,000-25,000 corporates).

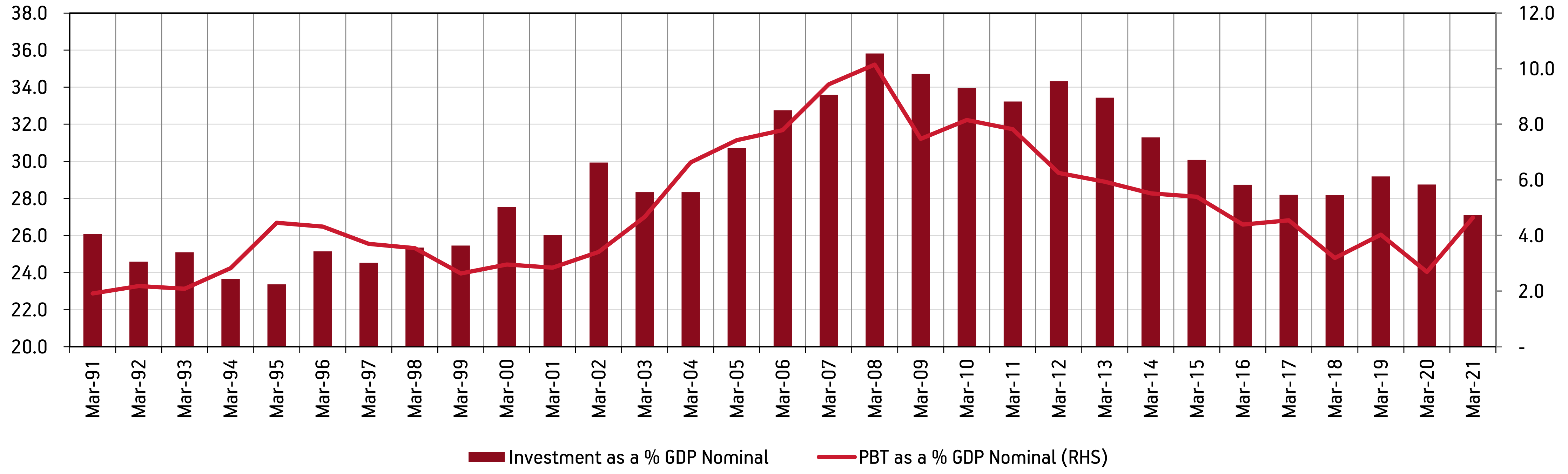
Sector-wise guidance on Capex



- Corporate leverage is at the lowest level in the last two decades.
- Fast pace of normalizing economic activity and improving end demand (consumption and exports) is likely to push capacity utilization rates higher, alongside a conducive policy environment which should push up private capex in FY23. Sectors with a positive capex outlook include metals, utilities, chemicals and consumer.

Source: Goldman Sachs, UBS, ABSLAMC Research

Investment – Capex cycle has bottomed out and should pick up

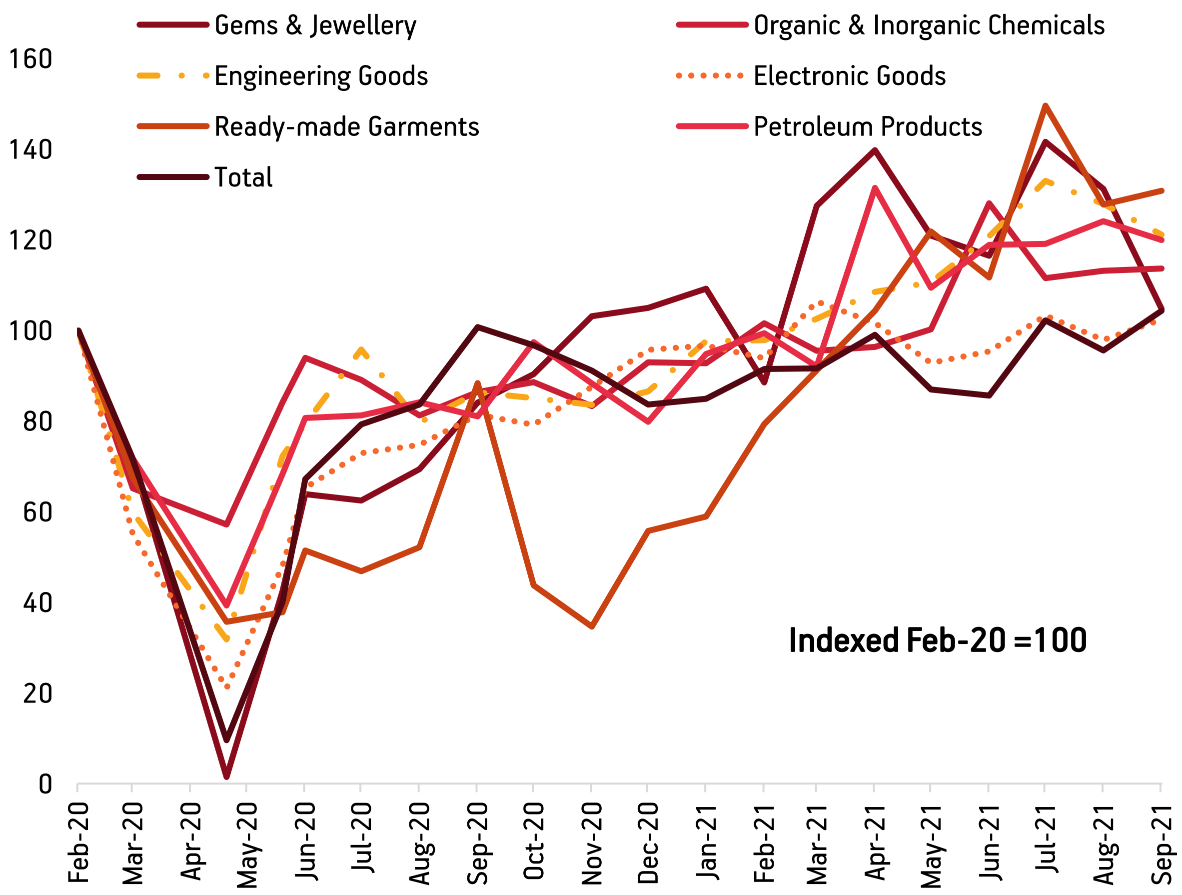


- Multiple drivers such as corporate tax rate cuts, lower interest rates and the deleveraging trend across sectors likely to act as catalyst to drive capex recovery going forward.
- PLI scheme bodes well to encourage indigenous manufacturing capabilities and exports. Sectors such as Electronics, Telecom, IT Hardware, Pharma, White Goods, Steel, and Food Processing should see an increase in exports driven by the PLI Scheme.
- As the capex cycle picks up, corporate profitability should also get a boost.

Source: B&K Securities, ABSLAMC Research

Exports – Overall outlook remains positive given robust global growth expectations

All segments are back to, or above their, pre-Covid levels



- With the global economy being ahead of India in terms of recovery from Covid, exports have been on an uptrend. Exports from all segments are above pre-covid levels.
- Latest PMI indicators also point towards robust manufacturing activity across most geographies. US economy is expected to do well and India's exports to US, which constitute ~20% of total exports, have also seen decent traction.
- India also has reasonable similarity with Chinese merchandise exports and comparable competency with other manufacturing peer countries. Hence, India is expected to benefit from China+1 model, especially in sectors such as textiles, chemicals, etc.

Source: Morgan Stanley, Department of Commerce-GoI, ABSLAMC Research

Covid has driven key shifts in the landscape which are beneficial for India

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Acceleration on Digitization front, hence beneficial for Indian IT services

- Rapid adoption of digital channels in financial services such as use of online banking, other digital payments;
- IT spending related to remote work has been one of the biggest and disruptive organizational shifts;
- Cloud adoption is likely to remain the key underlying tech trend to drive digital and modernization agenda.

Foreign companies diversifying away from China, hence Indian companies a key beneficiary of the move

- 32 countries have cancelled most-favored-nation treatment for China in Dec 2021;
- India has reasonable commonality with Chinese exports and competency compared to manufacturing peers;
- Hence, strong growth is achievable in sectors such as specialty chemicals, pharmaceuticals, textiles etc.

Boost to Start-up ecosystem in India which would drive innovation

- Consumer patterns/tastes have shifted since Covid whether its shopping, entertainment, education, healthcare, etc.;
- Many start-ups have been critical in helping organizations/ governments shift towards full-digital work;
- The start-up ecosystem is also creating large number of jobs in segments outside of the traditional manufacturing sectors.

Source: ABSLAMC Research

Capital flows in the country have been strong and should sustain going forward

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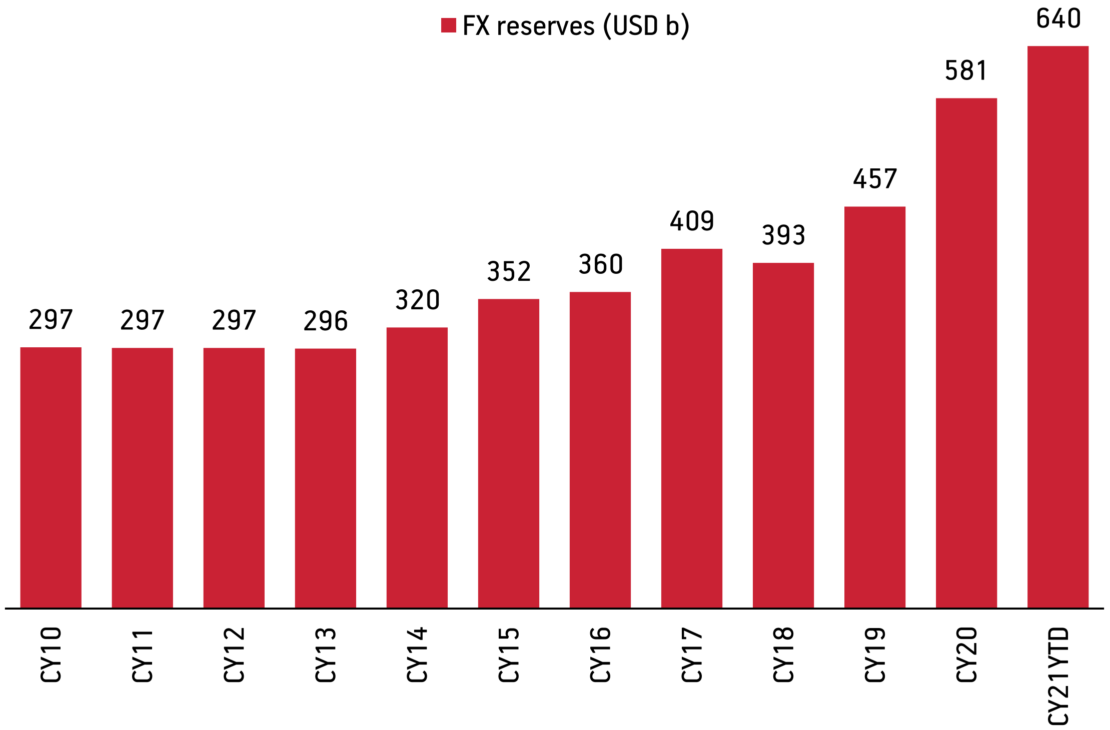
FDI flows have been strong

Trend in FDI flows, March fiscal year-ends, 2015-21 (US$ Bn)	2015	2016	2017	2018	2019	2020	2021
Gross FDI inflow into India for overseas entities	45.1	55.6	60.2	61.0	62.0	74.4	82.0
Gross FDI outflow out of India for overseas entities	-9.9	-10.7	-18.0	-21.5	-18.7	-18.4	-27.0
Net FDI inflow for overseas entities	**35.3**	**44.9**	**42.2**	**39.4**	**43.3**	**56.0**	**54.9**

India's forex reserves stand at an all-time high of $640 Bn

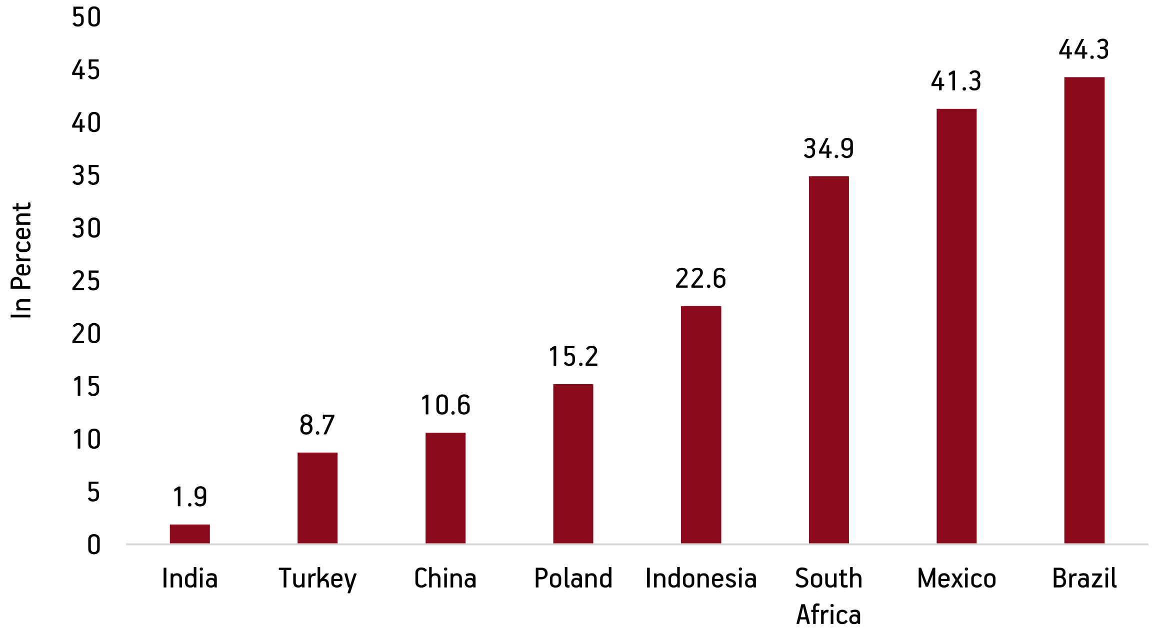


- Gross FDI inflow of $70 bn over trailing 12 months. Share of Manufacturing has reduced while share of Services (esp. IT/BPO) and Real Estate & Construction has increased.
- India has added USD 246b of FX reserves between CY19-CY21YTD.

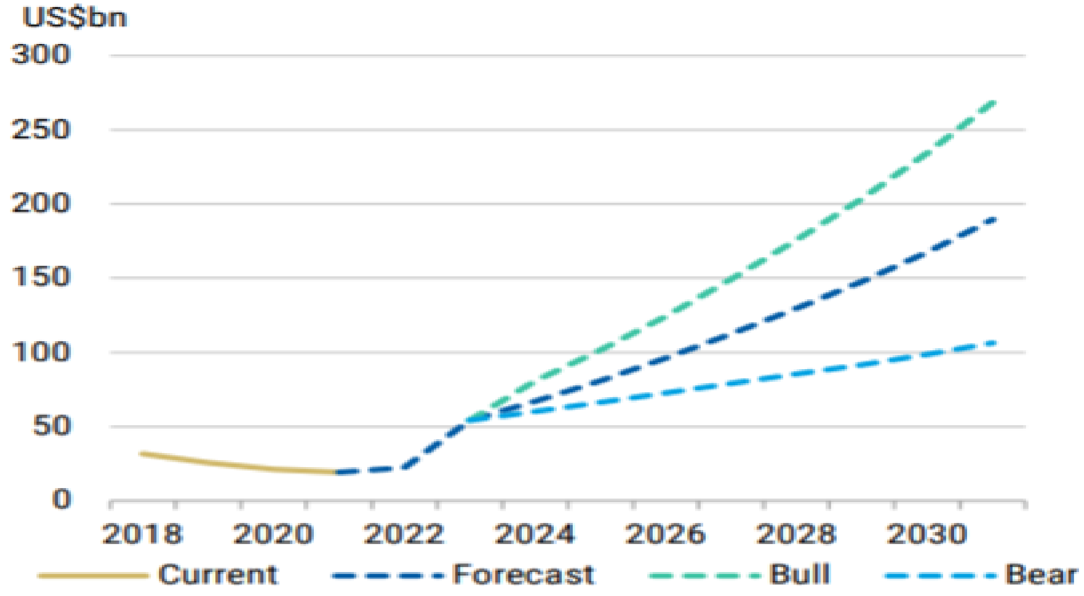
Source: Kotak, Morgan Stanley, ABSLAMC Research

India's inclusion in global bond index in 2022: A Boon for Equity markets too

Foreign ownership of central government bonds of India is very less as compared to EM peers



Total inflows could be US$200-250 Bn and foreign ownership of Indian government bonds may reach 9% at the end of 2031

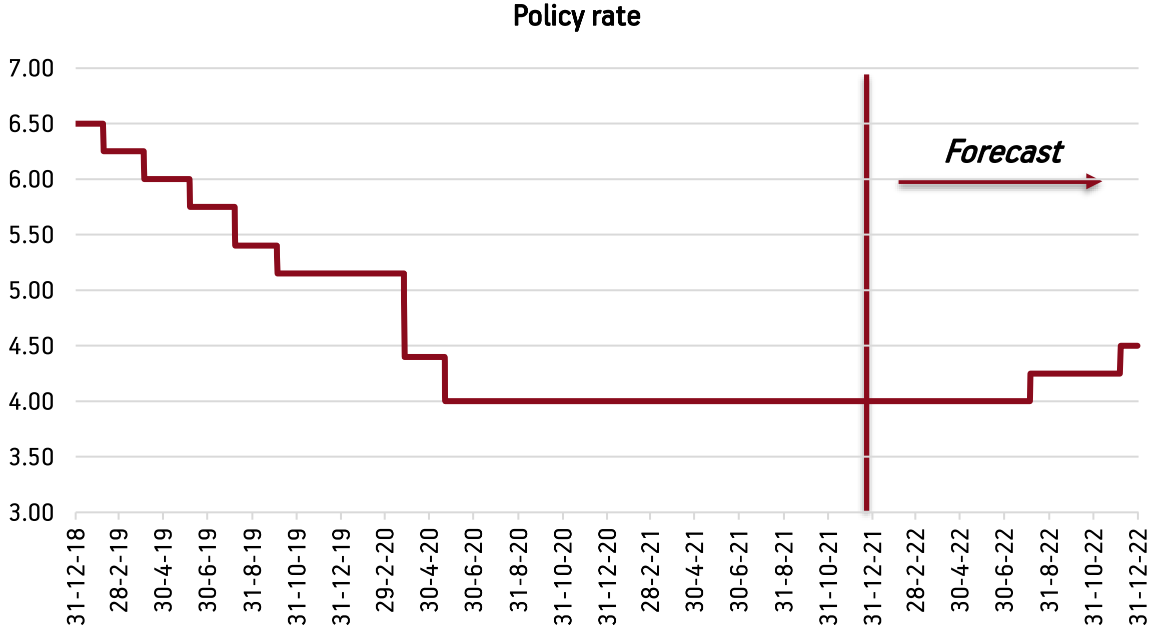


- India expected to get included in the Global Bond Index in 1QCY22. Index inflows in 2022/23 should be US$40 billion, followed by annual inflows of US$18.5 billion in the following years. This would push foreign ownership of IGBs to 9% by 2031.
- Foreign portfolio inflows would lead to lower borrowing costs and help India's debt sustainability further, a credit-positive. India's credit spread could tighten by 30-40bp and foreign inflows into onshore corporate credit would pick up.
- Banks and NBFCs would also benefit from stronger growth and lower borrowing costs.

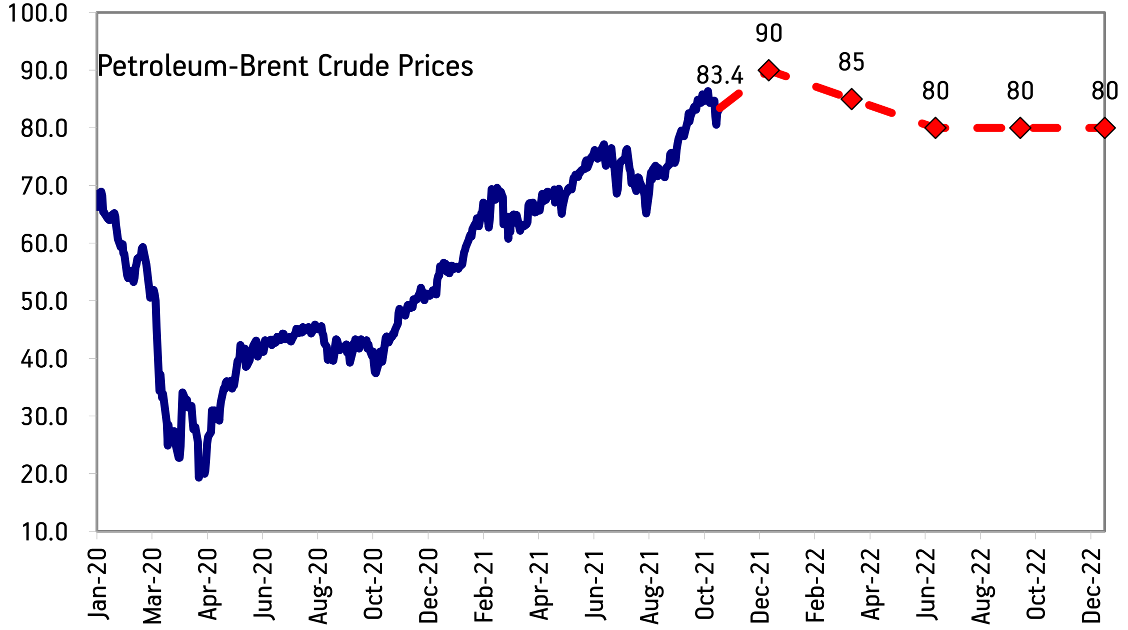
Source: Morgan Stanley, ABSLAMC Research

Policy tightening and elevated oil prices are risks but they should be manageable

Monetary policy is likely to tighten next year; We expect 2 rate hikes from RBI in 2022



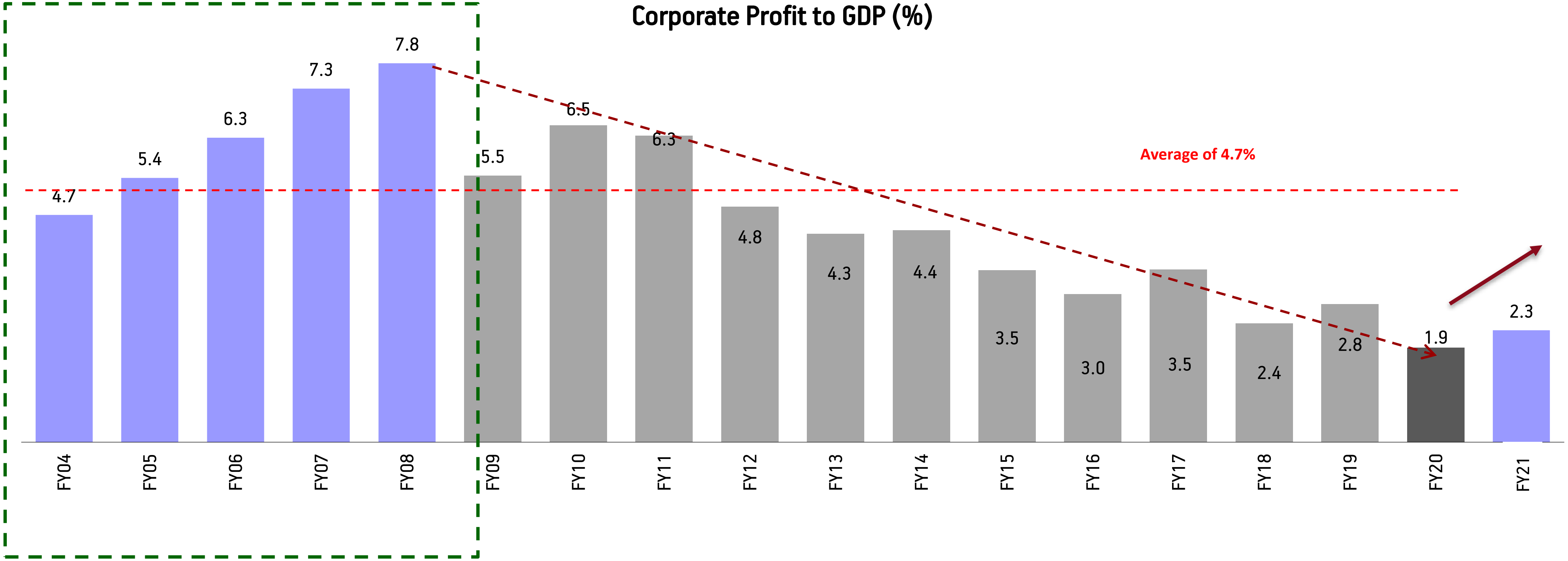
Oil prices are expected to stay elevated in 2022



- India is less vulnerable to a US taper this time compared to 2013 or late 2018 given the taper announcement was well anticipated by the markets. Also, external balances for India are much healthier now, fiscal deficit and CAD are under control, and inflation is also not high. Rate hikes are also expected to be gradual.
- Oil prices at persistently higher levels above $80/bbl could not only adversely impact India's macro (higher CAD and inflation, growth drag), but also weigh on earnings (through higher input costs). However, $80/bbl for crude should still be manageable.

Source: Goldman Sachs, ABSLAMC Research

Corporate Profit to GDP showing a turnaround and India seems well-positioned to enter a new profit cycle



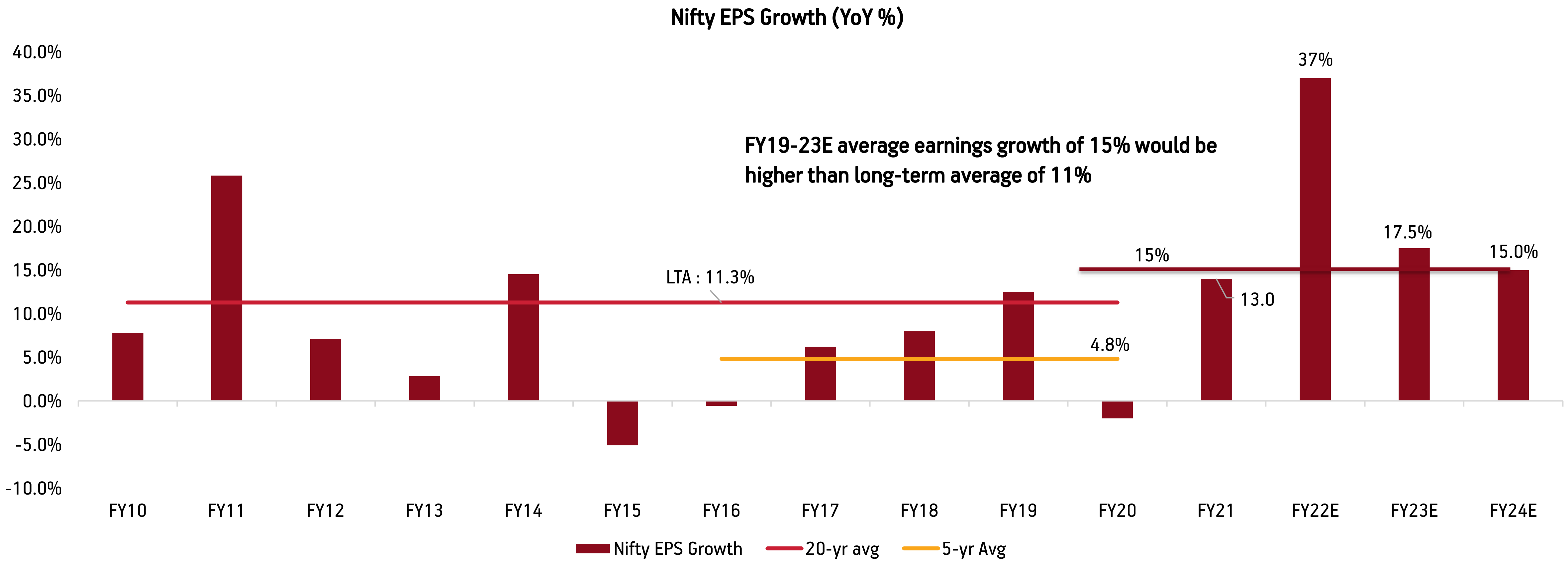
Expect mean reversion with sufficient headroom for corporate profits to rise.

- Telecom and PSU banks were a major part of loss pool. Cyclicals like Oil & Gas, Metals and Cap Goods had also seen a decline in profitability. These sectors should see an improvement in profitability going forward.
- Profitability of secular themes like technology, private banks, consumer, NBFC, etc. has anyways been on an uptrend.

Note: Corporate profit compiled from Capitaline for available listed + unlisted companies;

Source: MOFSL, ABSLAMC Research

Earnings growth expected to be above the long-term average over next couple of years

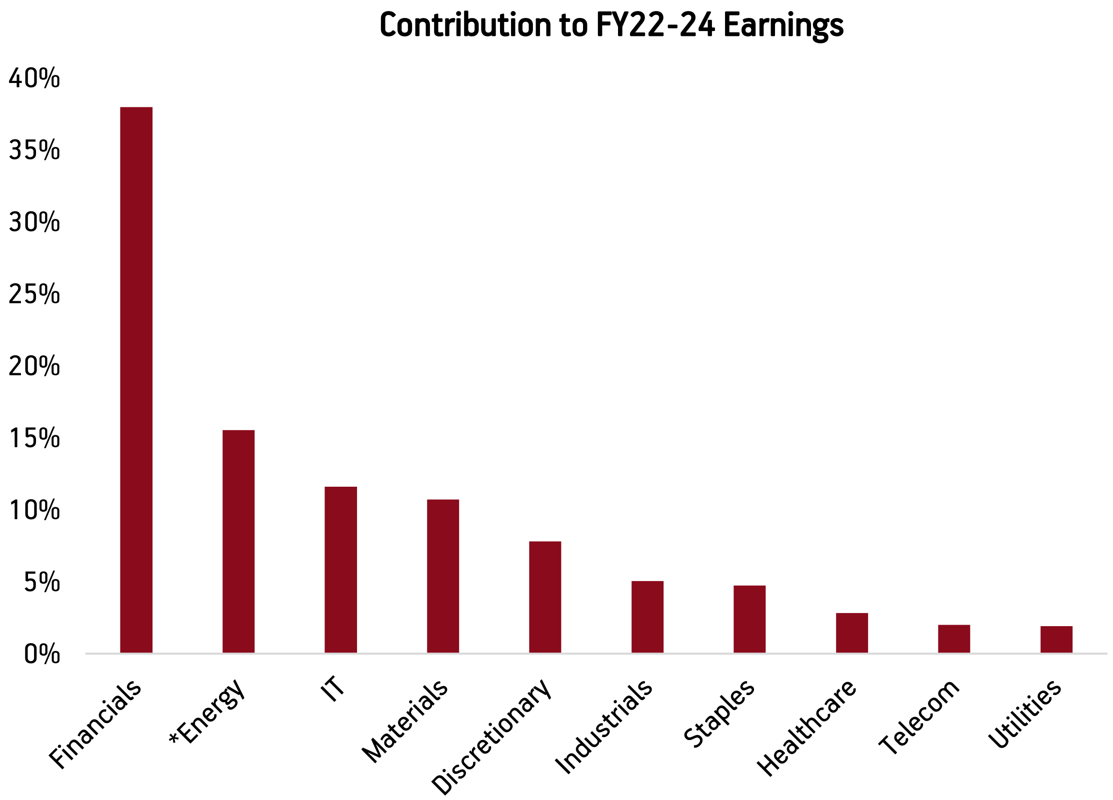


- Most of the drag on earnings in the past few years was due to the Banking and Telecom sectors, which should see an improvement in profitability going forward.

Source: Bloomberg, ABSLAMC Research

Banks expected to drive a substantial portion of Nifty earnings increase over next two years

Sectoral contribution to FY22-24 earnings



Note: *Majorly Reliance Industries Limited (RIL)

- Substantial revival in bank earnings expected post the clean-up over the last few years, followed by growth in Energy*, IT, Materials and Consumer Discretionary.

- In the Banking sector, volatility in earnings over the last few years was induced by rising provisions. This has now fallen sharply, as bad loans of the prior lending surge have been provisioned for. Pre-provision operating profits (PPoP) have seen healthy growth for the sector as a whole and are less volatile; forward-looking expectations are also conservative.

Source: Credit Suisse, ABSLAMC Research

Corporate profits In India to grow at a much more robust rate than in other regions in Asia

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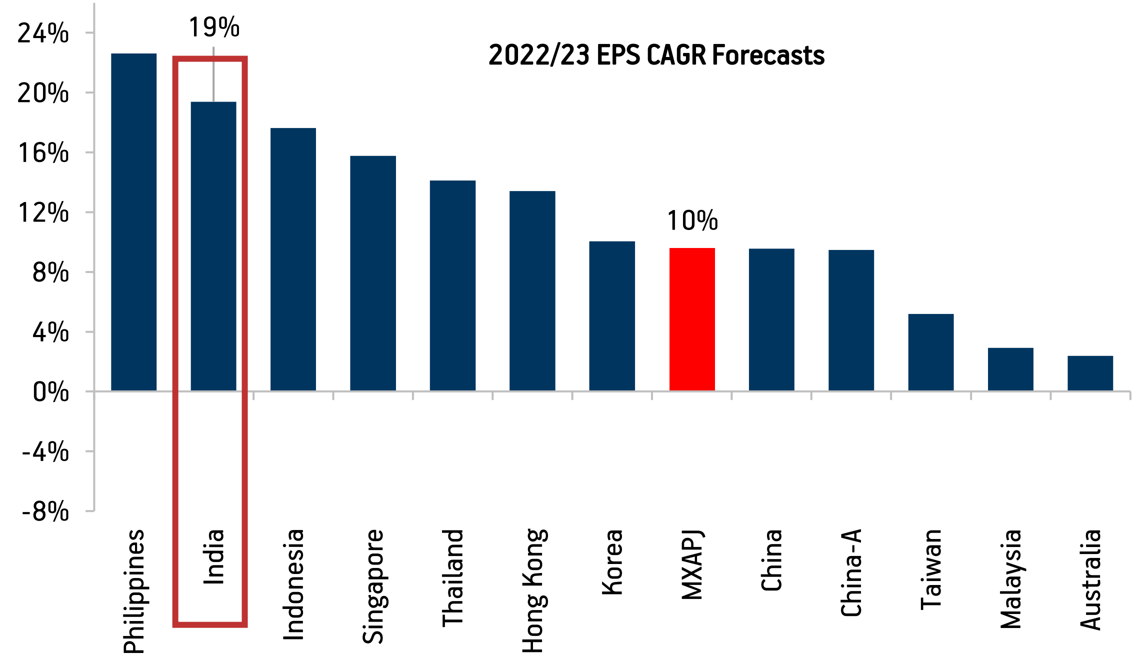
Market participants expect MSCI India's profit growth to be one of the highest in Asia ex Japan



- The aggregate MSCI India Index EPS has seen the largest upgrades in recent months against earnings downgrades in most other regional markets.
- India's projected profit growth of 19% CAGR in 2022-23 is the second highest in the region and almost twice the 10% forecast for the region.

Source: Goldman Sachs, ABSLAMC Research

Valuation metrics of Indian Equity markets remain elevated

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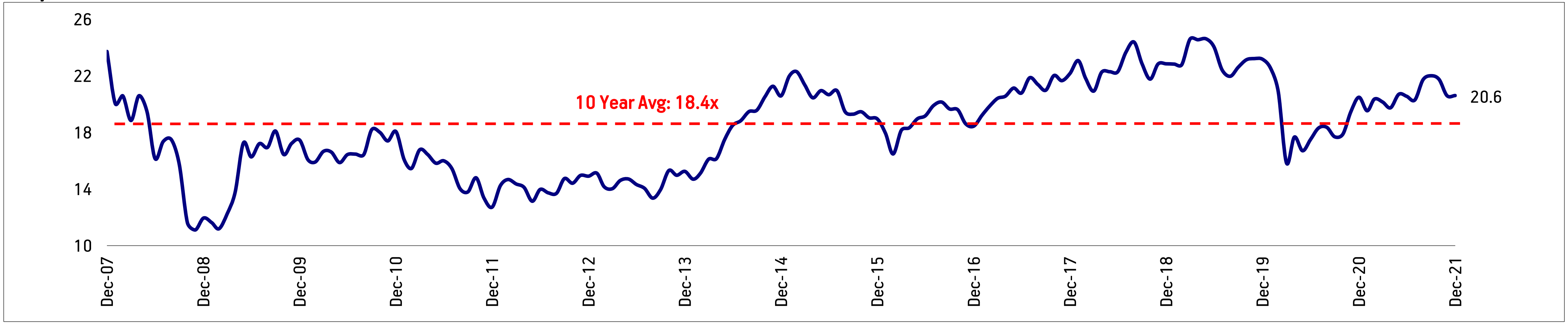
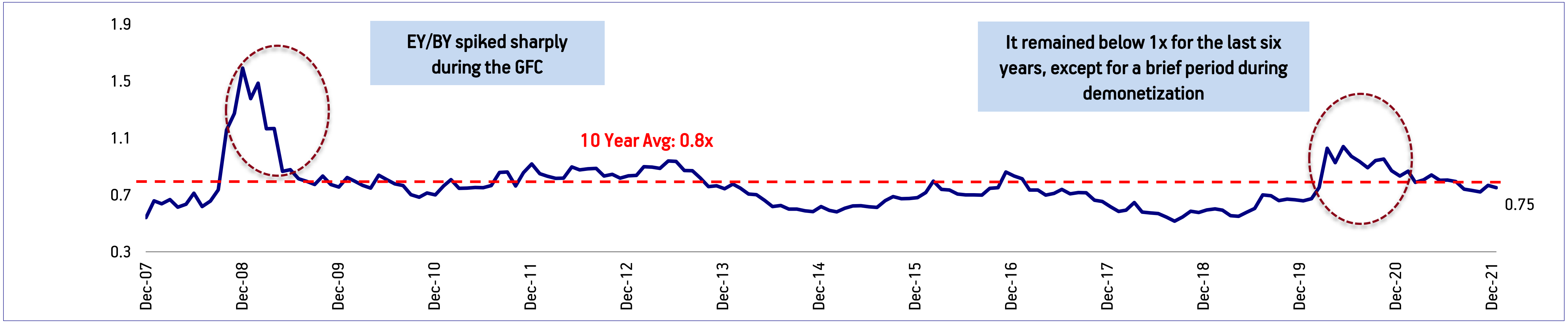
Nifty 1-Yr Fwd P/E

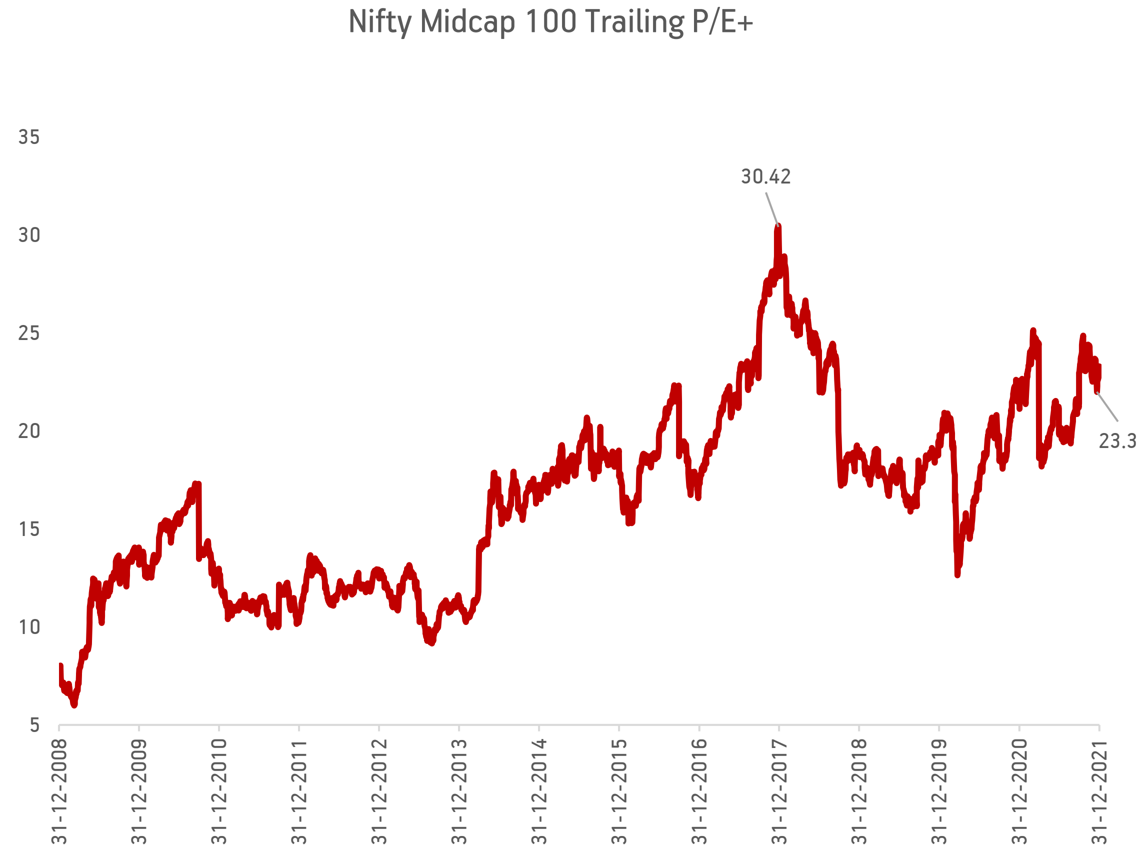


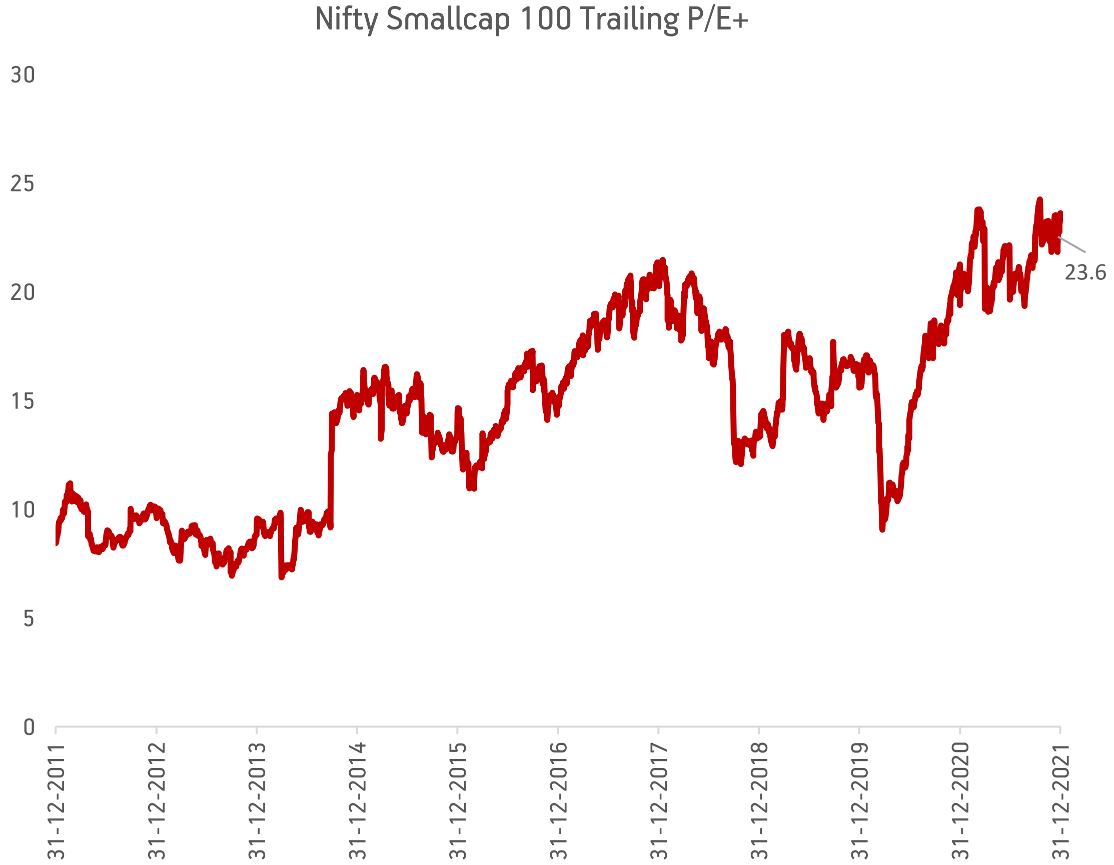
Nifty Earnings Yield (1-Yr Fwd) to G-Sec Yield



Source: MOSL, ABSLAMC Research

Mid-and-smallcap headline valuations have seen some moderation but remain elevated





- Easy money has been made in mid-and-smallcaps. But they can still go higher if the Indian economy does well as they are closely tied to the Indian economy.

As of 31st Dec 2021

Source: Bloomberg, ABSLAMC Research

Valuation across sectors shows high dispersion

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Specialty Chemicals, Consumer Durables, Technology, Retail, and Infrastructure are at a high premium to their long-term average valuations while Banks, Metals, and Media are at a discount.

At a Premium

At a Discount

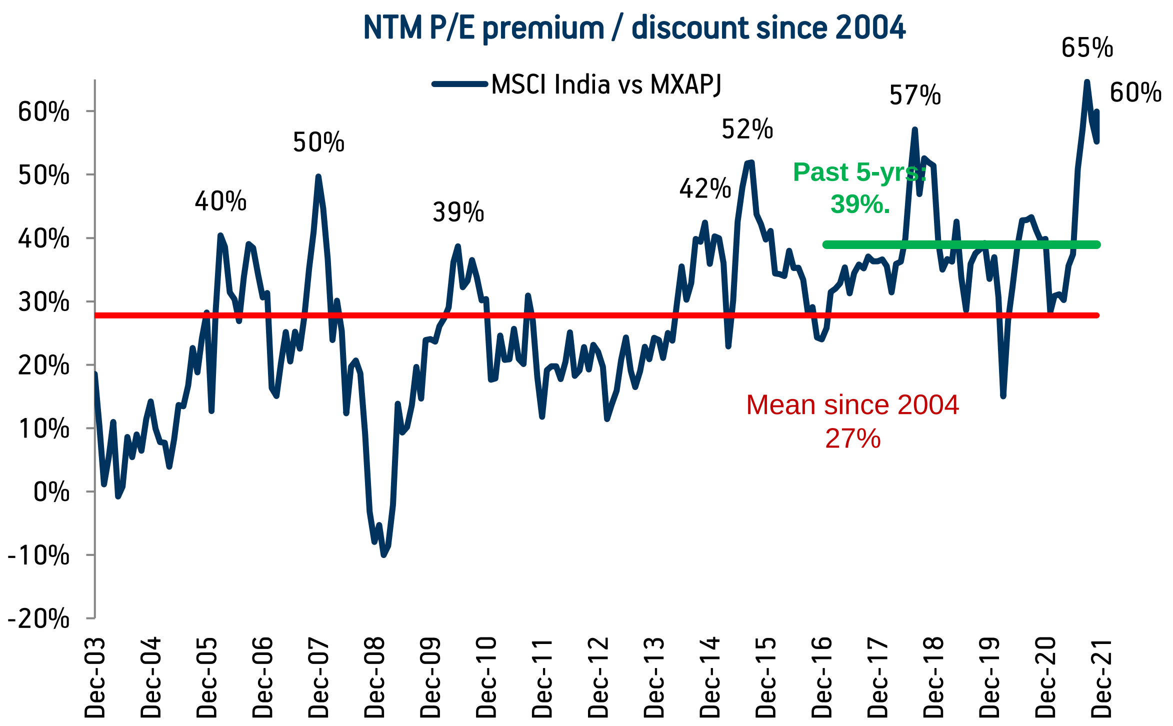
Sector	Current P/E (x)	10 YR Avg P/E (x)	Prem / Disc (%) to Avg	Current P/B (x)	10 YR Avg P/B (x)	Prem / Disc (%) to Avg
Sp. Chemicals	37.1	14.5	155.4	7.4	2.8	168.1
Consumer Durables	53.5	32.6	63.8	9.8	5.8	68.5
Technology	28.4	17.9	58.9	9.0	4.8	89.1
Retail	106.4	73.8	44.2	18.7	8.3	125.4
Infrastructure	15.2	10.6	43.7	1.0	1.2	-22.3
NBFC	25.6	20.2	26.8	3.3	2.7	22.3
Logistics	33.6	29.0	15.8	4.8	3.5	37.2
Consumer Staples	42.9	37.5	14.2	10.8	10.0	8.0
Oil & Gas	13.1	11.7	11.5	1.5	1.4	8.6
Capital Goods	29.3	28.0	4.5	3.2	2.7	19.7
Cement	24.5	23.5	4.3	3.6	3.4	6.5
Healthcare	23.9	24.3	-1.9	3.6	3.9	-6.3
Automobiles	21.6	22.4	-3.8	3.2	3.1	3.8
Banks-Private	19.0	20.2	-6.1	2.7	2.5	11.0
Media	18.4	24.8	-25.5	2.8	4.7	-41.0
Metals	6.8	11.1	-38.2	1.5	1.1	30.9
Banks-PSU	7.6	12.4	-38.7	0.8	0.8	4.1

Note: Valuations are based on 1-Yr forward estimates

Source: MOSL, ABSLAMC Research

India can sustain its relative valuation premium to Asian EMs if it maintains its growth differential

**MSCI India is trading at a peak valuation 22.9x NTM P/E.
Fwd PE premium has expanded to record level of 60%.**



- Valuation premium has expanded more from de-rating in the rest of region (driven by China) because of trade-tensions or the recent China sell-off (regulatory/property tightening).
- India's relative premium is correlated to the growth (GDP/earnings) differential between India and the rest of the region. India's potential growth has improved while rest of region is slowing (led by China), leading to a structurally higher premium.
- In the medium-term, India's valuations could be higher structurally given new economy sectors will start getting included in the Index. A case in point is that China's PE expanded when its new economy stocks were included in the index.

Source: Goldman Sachs, ABSLAMC Research; Note: NTM is Next Twelve Months

FPI flows to EM are moderating but India remains a standout

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FII flows (US$ bn)				
Markets	2018	2019	2020	2021
India	(4.6)	14.2	23.4	3.7
Korea	(5.7)	1.0	(20.1)	(22.8)
Taiwan	(12.2)	9.4	(16.0)	(15.3)
Philippines	(1.1)	(0.2)	(2.5)	(0.0)
Indonesia	(3.5)	3.5	(3.2)	2.7
Thailand	(8.9)	(1.5)	(8.3)	(1.6)
Malaysia	(2.9)	(2.7)	(5.8)	(0.8)
ASEAN	(16.3)	(1.0)	(19.8)	0.3
Emerging Asia	(38.8)	23.7	(32.5)	(34.2)

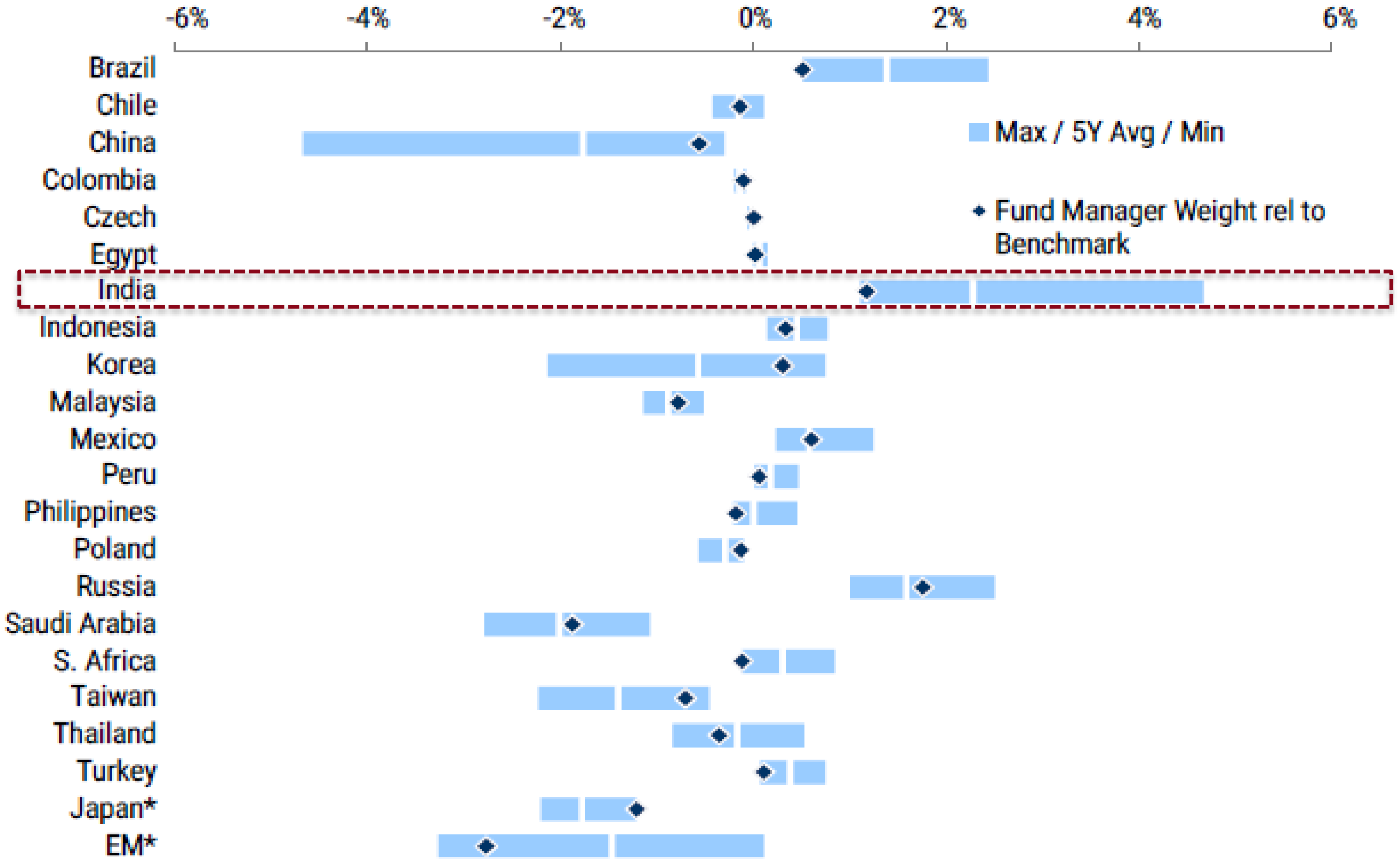
- US policy tightening can lead to a reversal in flows to EM in 2022.
- With DXY expected to strengthen till mid-2022, FPI flows to EM may remain under pressure.
- In contrast to most EMs, India has got strong FPI flows over the past three years. Given the higher visibility to growth that India provides, FPIs are likely to find India to be relatively more attractive.
- Hence, while FPI flows to EMs is expected to be muted in 2022, India is likely to do relatively better in the EM pack.

As of Dec 31st 2021

Source: Goldman Sachs, ABSLAMC Research

Allocation to India in GEM portfolios has increased but still is at the lower end of its historical range; FPI flows should pick up in 2022

GEM Fund Managers' Market Allocation vs MSCI EM



- Historically, India's relative position vs benchmark MSCI EM within Global Emerging Markets (GEM) portfolios has been in the range from as high as 4.7% overweight to as low as 1.1% overweight.
- Current 1.2% overweight is quite close to the historical record low which implies significant room for further allocation increase.
- Since India is relatively better placed and provides higher visibility to economic and earnings growth than other Emerging Markets, allocation to India is expected to increase and FII inflows are expected to pick up.

Source: Morgan Stanley, ABSLAMC Research

Story of Retail participation in Indian equities continues

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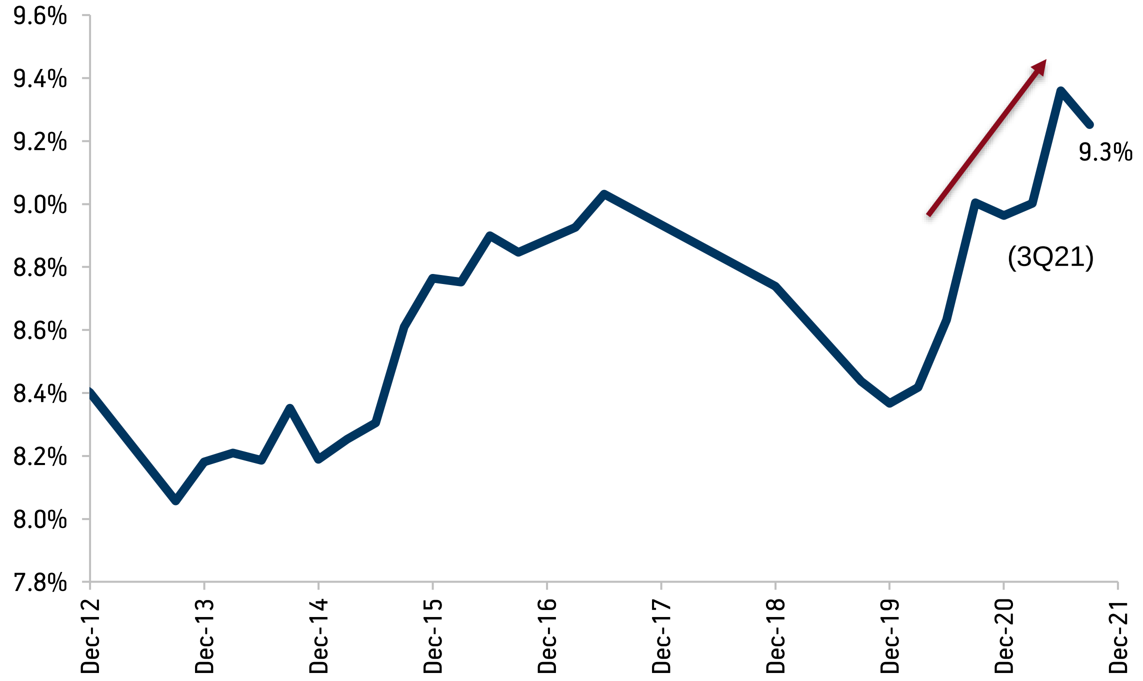
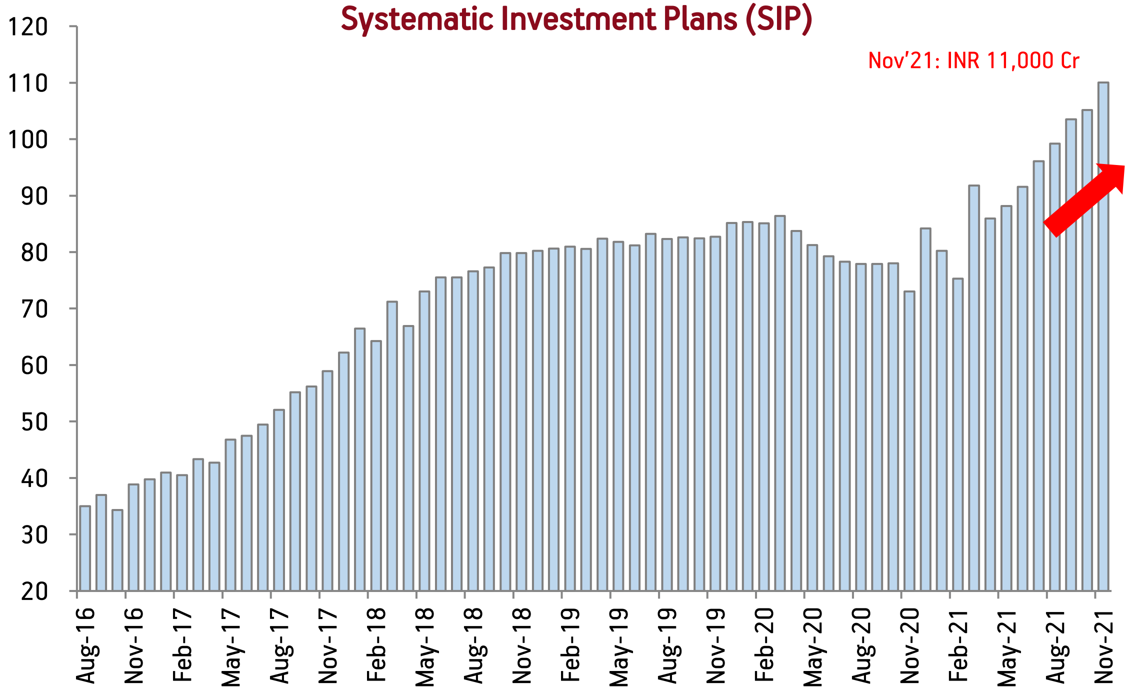
Retail ownership of Indian equities (%)



SIP flows are strong

Monthly flows in domestic MFs through Systematic Investment Plans (SIP)

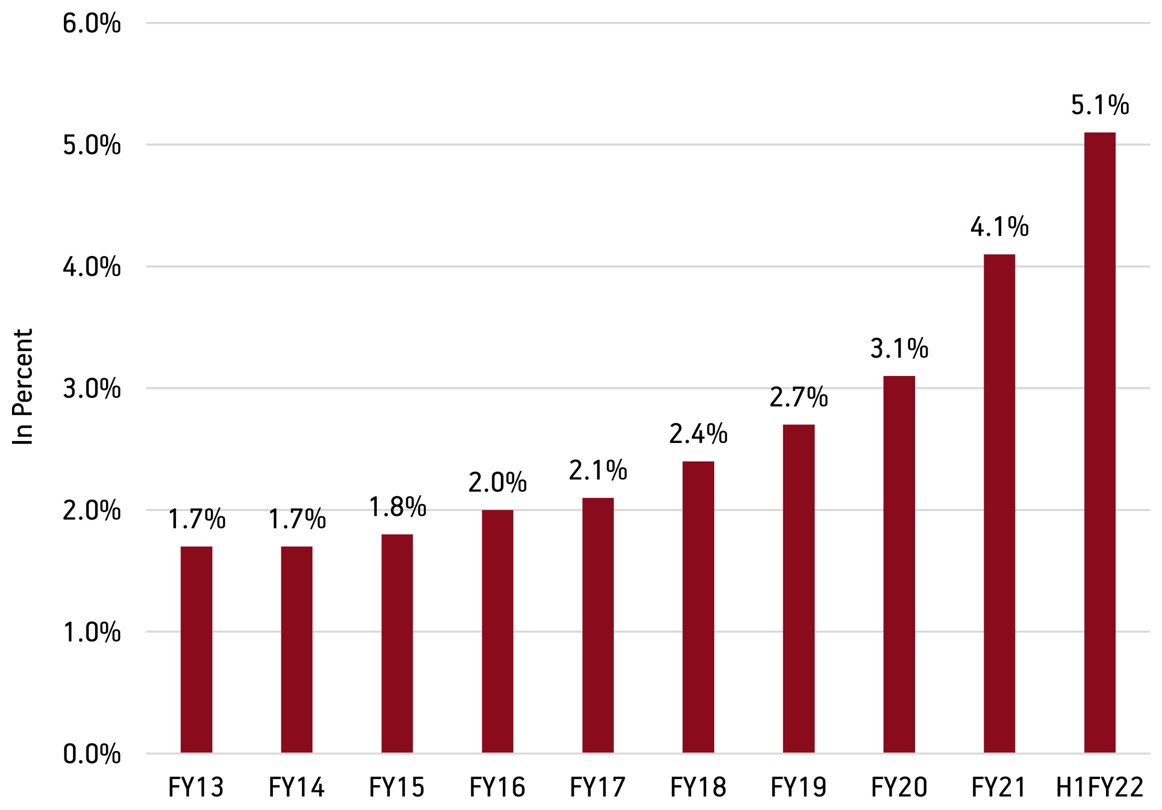


- Retail ownership of Indian equities has increased sharply to decade highs since last year and expected to sustain going forward.
- Monthly SIP flows have risen to a record high of Rs 11,000 cr. The number of SIP accounts continue to rise, with deeper penetration resulting in the average flow per account/folio falling to Rs. 2,000 - Rs. 2,500 per month. SIP flows expected to sustain going forward.

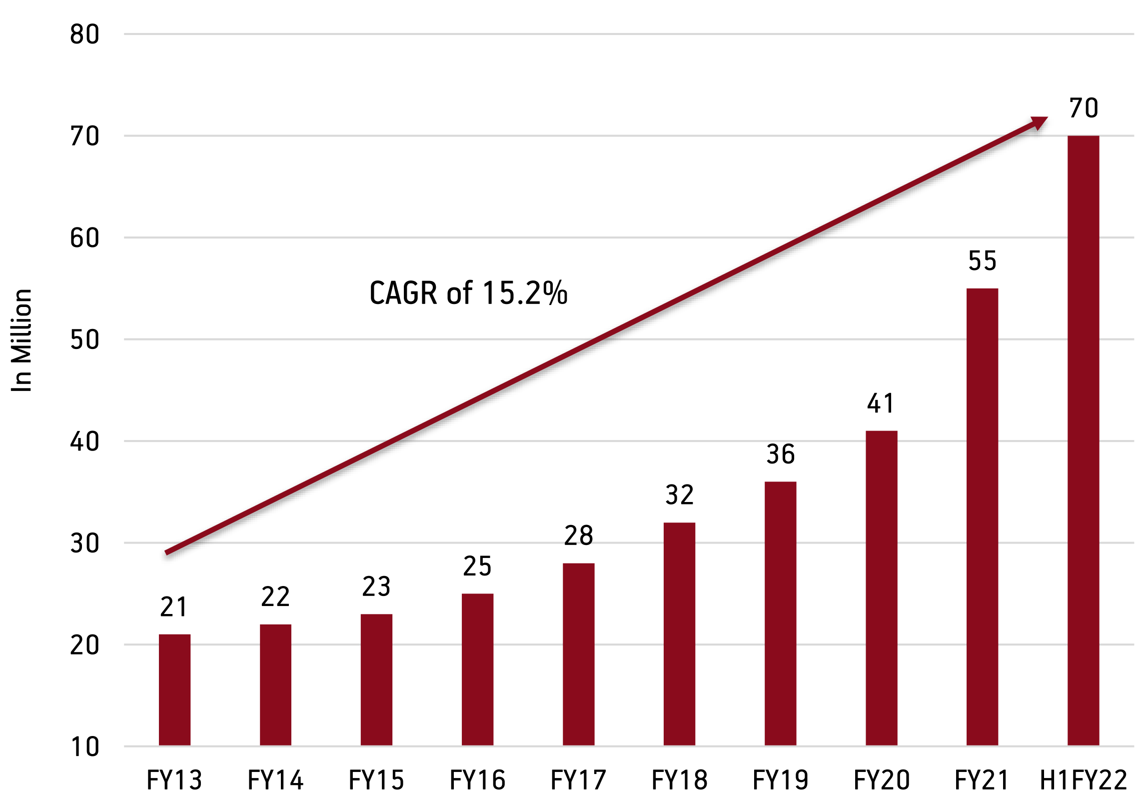
Source: Goldman Sachs, UBS, ABSLAMC Research

Investor base is becoming broad-based and should provide support to equity markets

Rising penetration of Demat Accounts in India



Steady growth in Demat Accounts in India

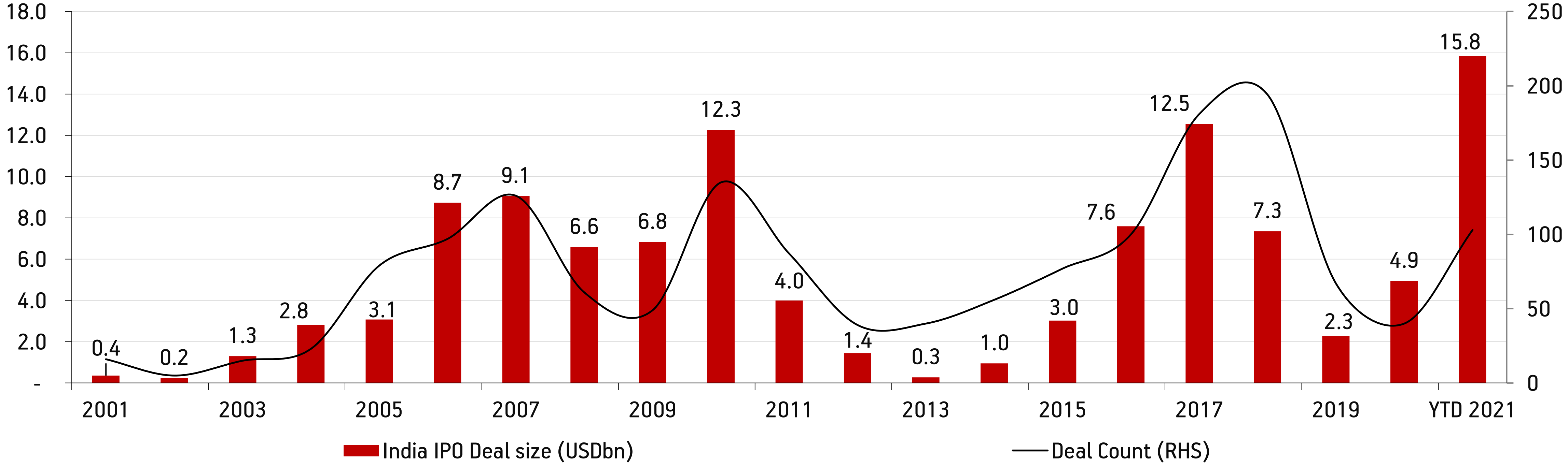


- India has seen a steady growth (~15% CAGR) in demat accounts since FY13. Significant rise witnessed over the last two years, hence leading to a broad-based market.
- Broad-basing of investor base is providing stability to equity markets and is also offsetting the FPI outflows.

Source: Angel Broking, ABSLAMC Research

IPO activity has risen to all-time highs

2021 has seen 103 IPOs with a total offer size of USD 16 bn



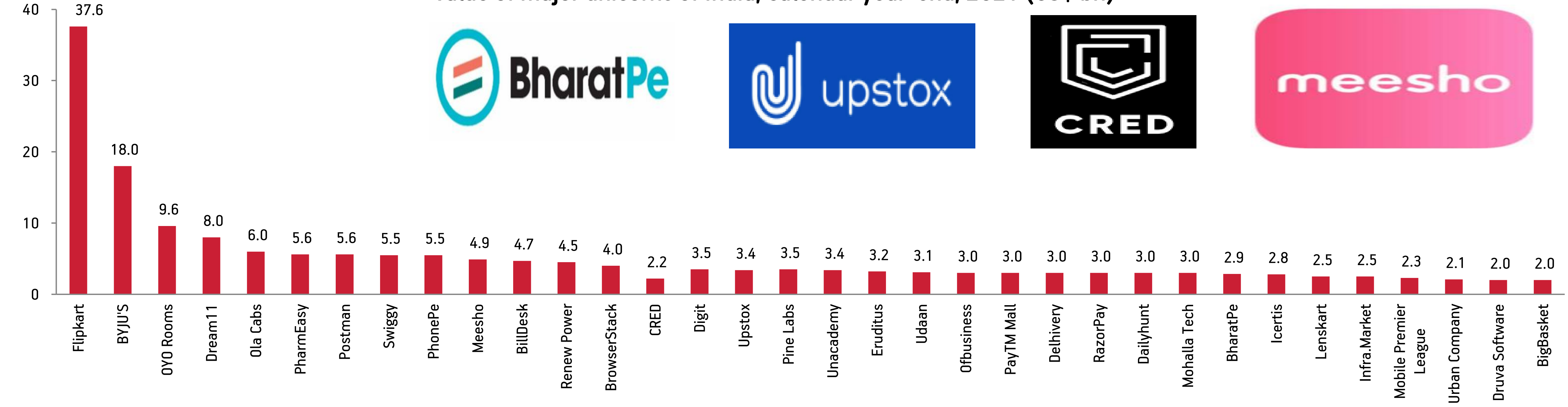
Note: Data as of 1st Dec 2021

- Public markets are willing to provide risk capital to businesses with potential which are not yet profitable. The largest unicorns have been concentrated in the new economy sectors (Fintech, E-Commerce, SaaS).
- The IPO pipeline has also been robust this year and the amount raised of $16 Bn has already surpassed the past 3 years. In addition, about 150 private companies could potentially list in public markets over next few years with financials and new-economy tech-enabled sectors accounting for most of the estimated value in the new listings.

Source: HSBC, ABSLAMC Research

Long pipeline of private companies which should get listed over the next three years

Value of major unicorns of India, Calendar year-end, 2021 (US$ bn)



- Listing of private companies over the next few years should further contribute to India's market capitalization.
- India already has several unicorns and deca-corns in many new-tech sectors propelled by a vibrant start-up eco-system.
- The successful listing of new-tech companies in India shows that:
  1. Indian new-tech companies have achieved considerable scale
  2. Indian market has sufficient breadth and depth to absorb such listings and
  3. Investors are savvy enough to value new business models.

Source: Kotak, ABSLAMC Research

Summary - 2020-21 vs. 2022: Comparison of key macro parameters

	2020-21	2022
Global Demand	Strong	Moderates
USD	Weakening	Strengthens
China Growth	Weakening	Stabilizing Growth
Exports	Strong	Strengthens
Private Capex	Weak	Likely to pick up
Govt Capex	Strong	Strong
Consumption	Weak	Discretionary segment to pick up
Global Inflation	High	Moderates
India PPI	High	Moderates
India CPI	High	Moderates
Interest Rates	Falling	Expected to rise
INR	Stable	Depreciates

Source: ABSLAMC Research

Summary - Has the Indian market peaked out or is it different this time?

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India – Comparison of Market Peaks

	FY2008	Current
Avg. GDP growth rate in prior 3 years	9.5	2.1
CPI Inflation (YoY%)*	6.2	5.2
Interest rates* (10-yr G-sec yield)	7.9	6.1
Corp Profits-to-GDP	7.8	2.3
Nifty 1Y Forward P/E	23.7	20.6

- In previous market peak during FY08, economy was in expansionary phase before the market peaked, inflation was high and interest rates were also high. Currently we are at beginning of economic recovery, inflation is well under control, and interest rates are relatively low.
- India also provides better visibility to economic growth and corporate profit growth than other Emerging Markets.

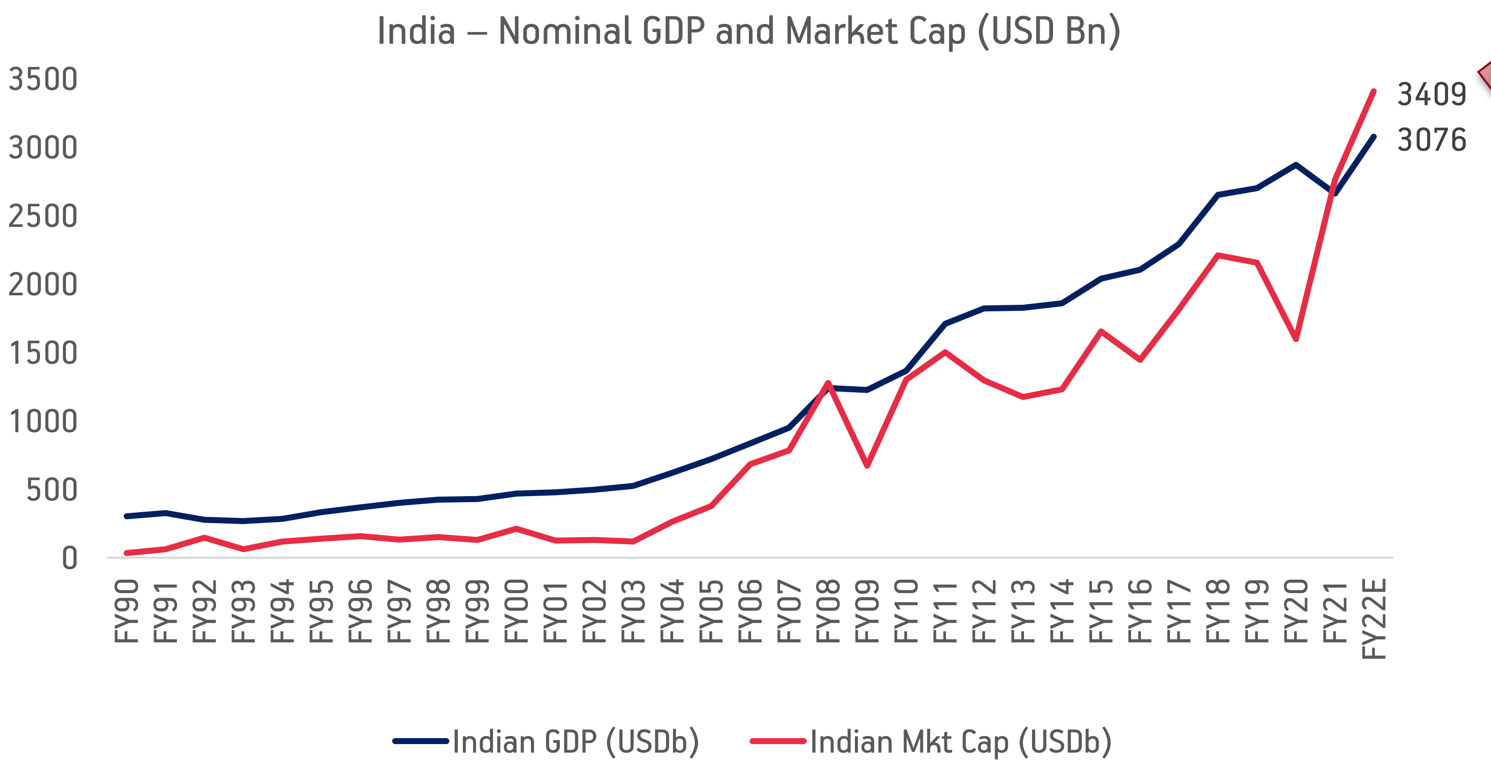
Source: MOSL, ABSLAMC Research

Summary – India at the Cusp of a New Growth Cycle

- Over next three years, **India is likely to go back to its real GDP growth trend of ~6.5% with all three drivers of economy namely Consumption, Investments and Exports firing**.
- Corporate earnings are likely to grow at a 15% CAGR over next 3 years, which is higher than the long-term average.
- Given depressed earnings and high liquidity, valuation multiples for Indian equities are elevated. However, 2022 can be a year of transition as excess liquidity gets withdrawn and interest rates inch up. Hence, valuation multiples can be expected to normalize.
- Given the rally in markets in 2021, easy money has already been made. In the short term, market action may be more stock-specific and returns may be modest.
- However, on a medium-to-long term basis, we continue to remain positive on Indian equities and expect markets to continue to scale higher. Market breadth would continue to improve as the domestic recovery gathers momentum and Domestic Cyclicals should do well. Overall, we believe Indian equity markets can give returns slightly below earnings CAGR over next 3 years.
- Investors should maintain their target equity allocation and use any correction as an opportunity to add to their equity exposure.
- In the current environment where market breadth is improving, bottom-up stock picking is likely to do well and active mutual funds could generate alpha.

Source: ABSLAMC Research

Overall, India's Nominal GDP and Market Cap can rise to $5 -6trn range in next 5-6 years



- **India's nominal GDP can hit the ~$5 trn milestone over the next 5-6 years.**
- **India's market cap can potentially rise faster than nominal GDP to $5-6 trn in the same period.**

- Going forward, India's market capitalization can grow faster than nominal GDP growth driven by four factors – (1) a larger economy, (2) larger share of formal economy, (3) larger share of Indian companies in the economy, and (4) listing of new companies.

Source: ABSLAMC Research

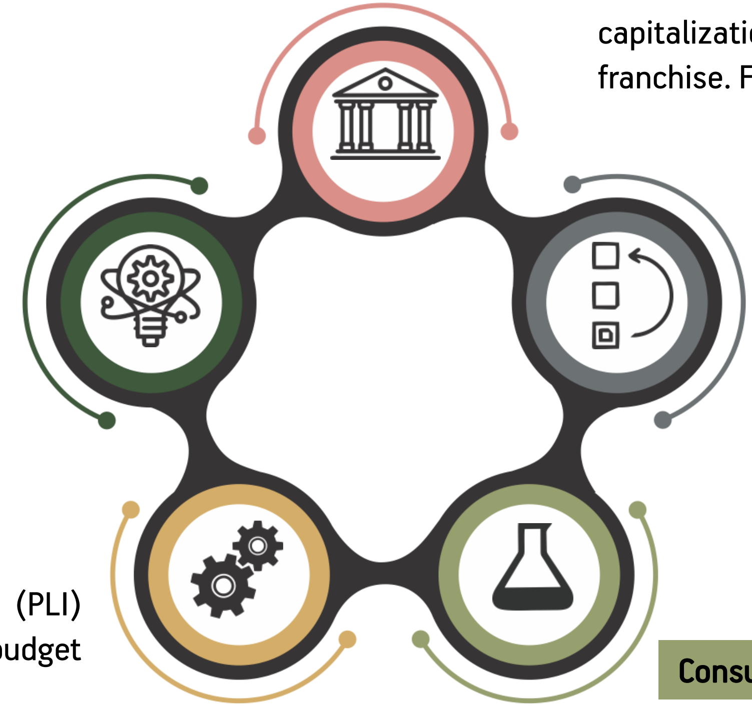
Key Sectors/Themes of Interest

Corporate Banks, Fintech

Structural story of increasing market share based on high capitalization, better asset quality and healthy liability franchise. Fintech disrupting space.

Digital Transformation

Factors driving higher tech spend: a) Modernization of core infrastructure; b) Adoption of public and hybrid cloud model; and c) increased adoption of AI.



Cyclical Revival in Real Estate

Structural tailwinds such as low interest rates, stagnant prices, increased 'work-from-home', reduced stamp duty, industry consolidation and unsold inventory.

Rise of Domestic Manufacturing

Govt. announced Production Linked Incentives (PLI) favourable for domestic manufacturing, High budget outlay for infra.

Consumer Discretionary

Pickup in low-ticket discretionary, retail, autos etc. based on rising income levels, low penetration, increased electrification, etc.

Note: The sector(s)/stock(s)/issuer(s) mentioned in this presentation do not constitute any research report/recommendation of the same and the Fund may or may not have any future position in these sector(s)/stock(s)/issuer(s).

Source: ABSLAMC Research

Key Risks

Aditya Birla Sun Life AMC Ltd.
(A part of Aditya Birla Capital Ltd.)

ADITYA BIRLA CAPITAL

Global Macro

- Higher than expected inflation lasting longer than expected, accelerated rate hikes. US interest rate cycle could be a source of volatility in the coming months.
- Larger than expected slowdown in China.
- Supply-constrained rise in oil prices could be bad for India's macros and markets.

Domestic Factors

- Mutant virus that is resistant to vaccines, leading to new mobility restrictions.
- Stalling of government projects/initiatives in case of adverse election results (U.P. elections next year).

Our Offerings

Equity Fund Category	Allocation %	Select ABSLAMC Funds
Largecap	25-30	Aditya Birla Sun Life Frontline Equity Fund Aditya Birla Sun Life Focused Equity Fund
Diversified	35-40	Aditya Birla Sun Life Flexi Cap Fund Aditya Birla Sun Life Equity Advantage Fund Aditya Birla Sun Life Multicap Fund Aditya Birla Sun Life ESG Fund
Midcap and Smallcap	15-20	Aditya Birla Sun Life Midcap Fund
Thematic	15-20	Aditya Birla Sun Life India GenNext Fund Aditya Birla Sun Life Banking & Financial Services Fund Aditya Birla Sun Life Digital India Fund

- Investors who are looking for lower volatility should consider **Aditya Birla Sun Life Balanced Advantage Fund and Aditya Birla Sun Life Asset Allocator Multi Manager FoF** as they are well suited for the current environment of low interest rates.
  - They have potential to provide **reasonable returns as compared to Fixed Income with low volatility**.
  - They are especially suitable for first-time investors in Equity as they provide a relatively **low-risk entry strategy.**

Riskometer

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Aditya Birla Sun Life Multi-Cap Fund
(An open ended equity scheme investing across large cap, mid cap & small cap stocks.)

- Long term capital growth and income
- Investment predominantly in equity and equity related instruments as well as debt and money market instruments

Investors understand that their principal will be at **Very High** risk

Aditya Birla Sun Life Equity Advantage Fund
(An open ended equity scheme investing in both large cap and mid cap stocks.)

- Long term capital growth and income
- Investments predominantly in equity and equity related securities as well as debt and money market instruments

Investors understand that their principal will be at **Very High** risk

Aditya Birla Sun Life ESG Fund
(An open-ended equity scheme investing in companies following Environment, Social & Governance (ESG) theme.)

- Long term capital appreciation
- An equity scheme that invests in companies following the Environment, Social & Governance (ESG) theme

Investors understand that their principal will be at **Moderately High** risk

Aditya Birla Sun Life Flexi Cap Fund
(An open ended dynamic equity scheme investing across large cap, mid cap, small cap stocks.)

- Long term capital growth
- Investments in equity and equity related securities

Investors understand that their principal will be at **Very High** risk

Aditya Birla Sun Life Banking & Financial Services Fund
(An open ended equity scheme investing in the Banking & Financial Services sectors.)

- Long term capital growth
- Investments in equity and equity related securities of companies engaged in banking and financial services

Investors understand that their principal will be at **Very High** risk

Aditya Birla Sun Life Digital India Fund
(An open ended equity scheme investing in the Technology, Telecom, Media, Entertainment and other related ancillary sectors.)

- Long term capital growth
- Investments in equity and equity related securities with a focus on investing in IT, Media, Telecom related and other technology enabled companies

Investors understand that their principal will be at **Very High** risk

Aditya Birla Sun Life Frontline Equity Fund
(An Open ended equity scheme predominantly investing in large cap stocks.)

- Long term capital growth
- Investments in equity and equity related securities, diversified across various industries in line with the benchmark index, Nifty 50 TRI

Investors understand that their principal will be at **Very High** risk

Aditya Birla Sun Life Focused Equity Fund
(An Open ended Large cap Equity Scheme investing in maximum 30 stocks.)

- Long term capital growth with exposure limited to a maximum of 30 stocks
- investments in equity and equity related securities to form a concentrated portfolio

Investors understand that their principal will be at **Very High** risk

Aditya Birla Sun Life India GenNext Fund
(An open ended equity scheme following Consumption theme.)

- Long term capital growth
- Investments in equity and equity related securities of companies that are expected to benefit from the rising consumption patterns in India fuelled by high disposable incomes

Investors understand that their principal will be at **Very High** risk

Aditya Birla Sun Life Midcap Fund
(An open ended equity scheme predominantly investing in mid cap stocks.)

- Long term capital growth
- Investments primarily in mid cap companies

Investors understand that their principal will be at **Very High** risk

Disclaimer

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MUTUAL FUND INVESTMENTS ARE SUBJECT TO MARKET RISKS, READ ALL SCHEME RELATED DOCUMENTS CAREFULLY

Thanks

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