Equity Outlook

JANUARY 2024

Mahesh Patil
Chief Investment Officer
Aditya Birla Sun Life AMC Limited

As we look forward into 2024 the picture looks much brighter as some of the concerns which dominated headlines in better part of 2023 such as global growth concerns, US recession, stubborn inflation, rate hikes, USD strength, geopolitical risk have reduced at the margin. The biggest surprise globally was on growth as we saw upgrades to global growth including India. Looking back, 2023 turned out to be a healthy year for equity markets and most asset classes.

The key highlight of our markets was the strong outperformance of small and midcaps and the market breadth, which was at a historical high. Last year we witnessed large macro sectoral themes play out like Realty, Capital goods, Auto, PSUs which gave outsized returns compared to the Nifty. In 2024, we think the macro trends have less influence and the market breadth can narrow down which means that bottom-up stock picking will play an important role for generating alpha and some consolidation of our portfolio holdings will be necessary.

For an emerging market, India also exhibited profound macro-economic stability last year which reflected in the fact that the volatility in our currency (INR) and Bonds was one of the lowest compared to other developed and emerging markets. Even the volatility of our equity market also trended lower as India VIX hit historic lows. This can make a case for lower risk premium for Indian markets going forward.

Moving forward the macro-outlook for India seems to be enjoying a Goldilocks scenario with reasonable growth momentum (expecting 6.5% GDP growth in FY25), stable commodity prices, especially crude, slowing inflation and a weakening dollar bias. Relatively, most of the global economy faces some headwinds like lagged impact of tighter monetary policy, limited fiscal space considering high public debt, lower nominal GDP growth and depletion in excess savings. We expect "mild slowdown" as a base case for global growth for CY24. Also, in 2024, more than 60% of the world economy will have elections, which makes us believe that these governments will try to maintain stability and not escalate any geopolitical risk.

The recovery in India's GDP is driven by investments which is now trending above the pre-covid trend while consumption is still to catch up as the rural economy and the bottom of the income pyramid is still recovering. Election-related spending this year should lead to some stimulus, and we remain hopeful of revival in consumption growth in the second half of CY24. The foundation for a sustained capex recovery from the private sector is also in place with banking balance sheets in good shape and corporate debt to equity at its lowest level in a decade. All these factors give us greater confidence in the long-term sustainable growth for our economy despite some global headwinds.

In this backdrop, the outlook for FII flows will be further supported by a weakening USD. India's overweight in emerging market funds is lower than historical levels and there is room to increase it as foreign investors look for markets that offer better growth. The domestic flows are also more resilient with MF SIP, EPFO, NPS and Insurance averaging USD 3.5bn on monthly basis. The confluence of strong liquidity flows from domestic and FIIs will ensure that India's premium to other emerging markets continues to be at a significant premium.

Post-covid corporate earnings growth have been strong with high teens CAGR, however, as the base effect and efficiency gains plateau, earnings growth going forward should track marginally above nominal GDP growth. The big difference between the pre-covid period and now is that the growth is more broad-based, driven by many sectors where the outlook is looking better.

The key themes of interest for us are: - a) Banking and Finance: riding on the strong credit growth driven by revival of corporate credit and benign credit cost; b) Domestic manufacturing: as the private sector capex revives and PLI-led investment gain traction in various sectors including the new age sectors like renewables, semiconductor, EVs, etc. c) Discretionary consumption: a secular theme for the next decade as India's per capita GDP crosses the inflection point of 2,500 USD and the young India which is aspirational drives premiumization. Discretionary consumption is still below its pre-Covid peak and with inflation on a declining trend, we should see a pickup in discretionary consumption. Apart from these, other sectors which we prefer are Real estate, Pharma and Autos.

Currently, despite markets making a new high, the valuation of Nifty is only marginally above the long-term average. Hence market returns will track earnings growth. In the last two years, large cap stocks have significantly under-performed the midcap and small caps and their ratio to total market cap is at a decadal low. Also, the relative valuation of large cap stocks vis-a-vis Small and Midcap is also favorable. All this data makes us believe that despite equity returns being moderated in the coming year, risk reward favors large cap stocks, and we would advise more flows to large cap biased funds. Also, with interest rates at their peak and expectations of moderate equity returns, fixed income looks attractive. Overall, risk reward seems balanced across asset classes, hence, a multi-asset allocation approach with exposure to Equity, Fixed Income, and Gold continues to remain well-suited for the coming year.

Our Recommendations

Market Cap Specific	Hybrid Solutions	Thematic & Sectoral Solutions	Diversified across Market Cap
Aditya Birla Sun Life Small Cap Fund	Aditya Birla Sun Life Balanced Advantage Fund	Aditya Birla Sun Life India GenNext Fund	Aditya Birla Sun Life Multi-Cap Fund
Aditya Birla Sun Life Mid Cap Fund	Aditya Birla Sun Life Multi Asset Allocation Fund	Aditya Birla Sun Life Digital India Fund	Aditya Birla Sun Life Flexi Cap Fund
Aditya Birla Sun Life Frontline Equity Fund			

None of the aforesaid recommendations are based on any assumptions. These are purely for reference and the investor are requested to consult their financial advisors before investing.

Mutual Fund investments are subject to market risks, read all scheme related documents carefully.