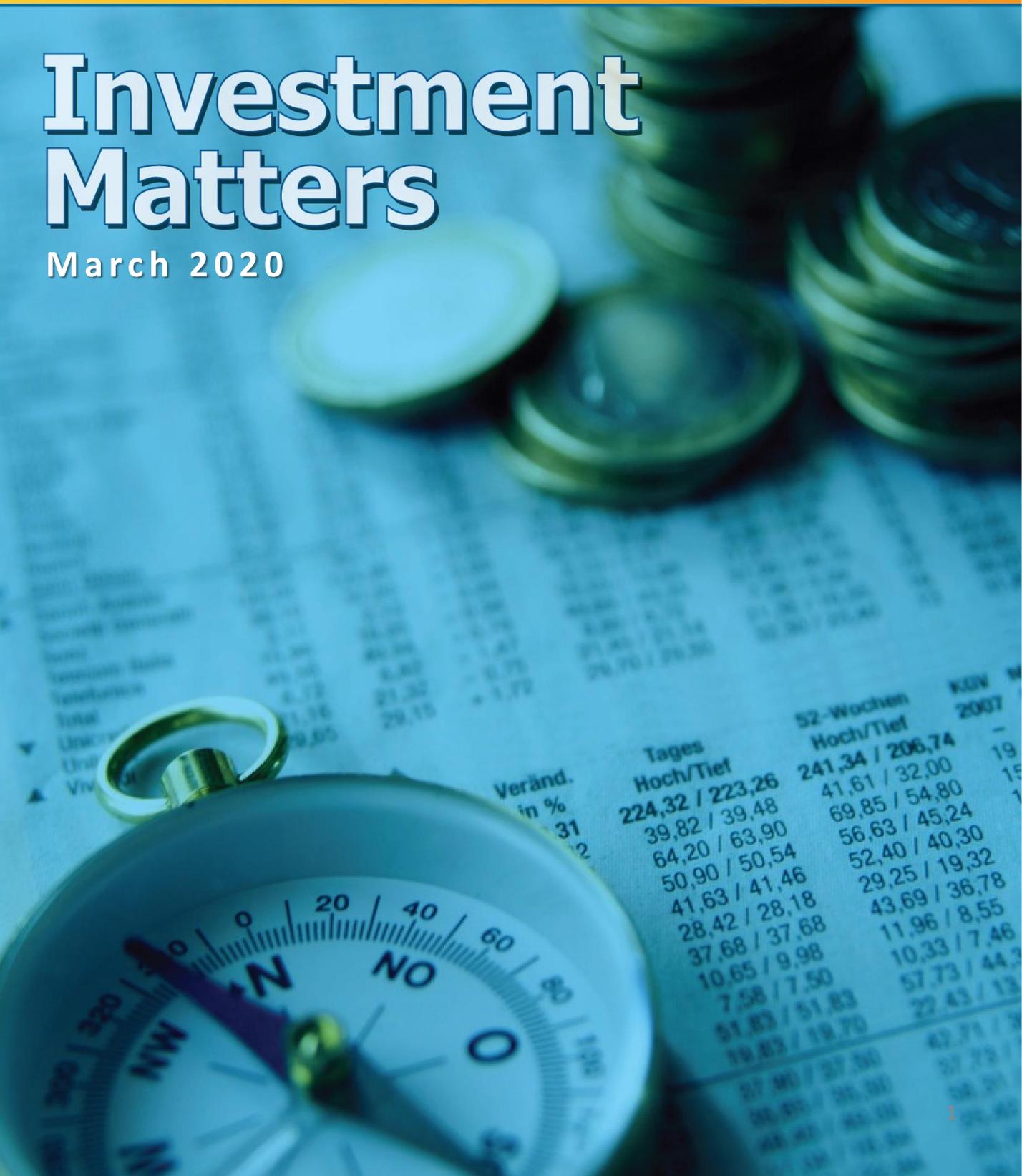


Investment Matters

March 2020



Veränd. in %	Tages Hoch/Tief	52-Wochen Hoch/Tief	KGV 2007
31	224,32 / 223,26	241,34 / 206,74	19
2	39,82 / 39,48	41,61 / 32,00	15
	64,20 / 63,90	69,85 / 54,80	1
	50,90 / 50,54	56,63 / 45,24	
	41,63 / 41,46	52,40 / 40,30	
	28,42 / 28,18	29,25 / 19,32	
	37,68 / 37,68	43,69 / 36,78	
	10,65 / 9,98	11,96 / 8,55	
	7,58 / 7,50	10,33 / 7,46	
	51,83 / 51,83	57,73 / 44,3	
	19,83 / 19,70	22,43 / 13	
	37,80 / 37,50	42,71 / 3	
	38,90 / 38,50	57,73 /	
	48,80 / 48,50	58,20	
	18 / 18,20	25,40	
	20,20	25,40	

EQUITY OUTLOOK

Markets headed for a tough period

The spread of the Corona virus, and its second-order impact on both India and the world, is a new and significant headwind for the market. A sharp slowdown in discretionary consumption could hurt near-term earnings, even for high-quality companies. An resultant valuation compression would leave the market very vulnerable. We remain cautious in our deployment – while we continue to focus on quality growth stocks, we are now trying to scope out near term risk and adjusting our entry accordingly.

The direct impact of the corona virus is still to be fully assessed. The relative ease of transmission has raised legitimate worries about the ability of authorities to contain the spread, best intentions notwithstanding. The medical outcomes are, therefore, uncertain but there is a possibility of the virus spreading quickly within India.

The economic outcomes could be severe, at least in the short term. The countermeasures to contain the virus are likely to slow down travel, entertainment and discretionary purchases as consumer confidence starts to erode. The exact dimension of this drop in growth is difficult to gauge at this stage; it will depend on whether the response involves extreme measures like temporarily shutting establishments. In any case, we are bracing for a short-term consumption slowdown; the extent and the length of this slowdown are hard to predict. Supply-chain disruptions are likely to exacerbate the problems.

There is a mitigant in the sharp fall in crude prices – Brent crude fell 42% since February 20 and are down 50% YTD. Over the medium term, this is positive for India on multiple fronts – lower current account deficit and inflation, better domestic liquidity, and lower RM prices for many consumer companies. It is not an unmixed blessing, however, as this could have collateral damage in the short term. The areas of risk include expatriate remittances from the Gulf countries; export earnings from oil rich countries in the Middle-East, Central Asia and Africa; a possible contagion to other commodities like metals, in which India has substantial domestic manufacturing exposure; and the general growth risks that come from a global recession, of which the oil price correction is an integral part. In the short-term, we will have to be aware of these risks as well.

Our view on the economic outlook is now changed. While the Indian economy was showing some signs of bottoming out, the continued escalation in the number of COVID-19 cases outside China is likely to prolong the domestic recovery process by at least a couple of quarters. The drag on domestic growth from supply chain disruptions and the slowdown in global growth is more likely to be felt in 1QFY21 rather than 4Q if the current situation persists.

EQUITY OUTLOOK

The recent downgrade of FY19 GDP growth to 6.1% from 6.8% shows that the economy had slowed down much earlier than was previously believed. Moreover, the government clearly lacks the resources to revive the economy quickly. India's tax revenues are pro-cyclical, hence, a consumption slowdown limits the government's ability to increase spending to combat the private expenditure deceleration. We do expect some counter-balancing monetary policy measures from the RBI, but that is unlikely to have an immediate impact until the medical threat recedes from the popular psyche. Further, monetary transmission tends to work with long lags – of the 135bps of cumulative rate cut delivered by the RBI last year; only 45bps have been passed on by the banks so far. All the above suggest that there exist significant downside risks to overall earnings of the market.

The immediate worry is that of a combination of earnings risks and multiple compression. A sharp consumption slowdown is a clear and present danger to the earnings outlook, even for the high quality companies and market leaders. If this plays out over the next 1-2 quarters, we are faced with a temporary multiple contraction in these companies. This would have a significant impact on the broader market indices, which have been held up by a narrow range of high-quality companies. Therefore, while we remain focused on high-quality names as these are better off in a downturn, we will remain careful on our entry prices for these stocks.

The broader market recovery is difficult to predict at this stage. Of course, we have seen a sharp recovery in previous episodes like SARS and H1N1, but that is no assurance that it will play out in the same manner this time. It is too early to scope the medical risks and assert, with any certainty, that this is a temporary slowdown. We are bracing ourselves for a weak market, but hoping that the virus impact is not extreme and the economy recovers quickly.

Despite the risks mentioned above, we continue to focus on quality stocks for our portfolio. Players with strong execution capabilities, coupled with fortress balance sheets, will gain share and lead the recovery. This is a recurring theme across multiple segments like financial services, retail and FMCG. The recent market correction thus provides an opportunity to add quality names to our portfolio, albeit with strict price discipline and scoping of near-term risk.

Seshadri Sen
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Alchemy Capital Management Pvt. Ltd

Source :
Alchemy Research
Bloomberg

Q3FY20 Performance of Portfolio Companies

The following table summarizes the performance of portfolio companies in Q3FY20 :

Stock	Sales (Rs Mn)			EBITDA (Rs Mn)			PAT (Rs Mn)		
	Q3FY20	Q3FY19	% Chg	Q3FY20	Q3FY19	% Chg	Q3FY20	Q3FY19	% Chg
Asian Paints	54,203	52,630	3%	11,894	11,044	8%	7,797	6,473	20%
Avenue Supermarts	67,519	54,509	24%	5,931	4,533	31%	3,943	2,571	53%
Axis Bank	102,395	96,044	7%				17,570	16,809	5%
Alia Engineering	6,940	7,002	-1%	2,188	1,652	32%	1,561	1,290	21%
Bajaj Auto	76,397	74,358	3%	13,672	12,125	13%	12,616	11,019	14%
Bajaj Electricals	12,736	21,565	-41%	684	1,378	-50%	155	639	-76%
Bajaj Finserv	145,607	111,416	31%				11,256	8,505	32%
Bajaj Finance	45,369	31,992	42%				16,141	10,598	52%
Bandhan Bank	18,980	15,257	24%				7,310	4,279	71%
Berger Paints India	16,959	16,167	5%	2,963	2,502	18%	1,824	1,332	37%
Container Corporation of India	15,279	16,571	-8%	3,717	4,184	-11%	1,755	2,747	-36%
Delta Corp	2,051	2,052	0%	791	855	-8%	551	512	8%
Dynamatic Technologies	3,078	3,665	-16%	443	439	1%	121	83	46%
Godrej Consumer	27,781	27,240	2%	6,313	6,162	2%	4,496	4,176	8%
Garware Technical Fibres	2,358	2,222	6%	381	368	4%	290	247	17%
HDFC Bank	208,422	174,978	19%				74,165	55,859	33%
Hindustan Unilever	98,080	95,580	3%	24,450	20,460	20%	16,910	14,010	21%
ICICI Bank	131,546	107,581	22%				41,817	16,049	161%
Info Edge India	3,205	2,811	14%	1,059	833	27%	880	743	18%
L&T Technology Services	14,229	13,169	8%	2,863	2,417	18%	2,041	1,856	10%
Mahindra and Mahindra	123,453	130,704	-6%	16,496	15,172	9%	8,464	11,328	-25%
Multi Commodity Exchange	893	769	16%	392	209	87%	553	418	32%
Nestle India	31,493	28,788	9%	6,730	6,608	2%	4,696	3,860	22%
Pidilite Industries	19,266	18,483	4%	4,632	3,368	38%	3,445	2,181	58%
Qess Corp	29,500	21,722	36%	1,794	1,183	52%	749	650	15%
Ramco Cements	12,746	12,074	6%	1,995	2,110	-5%	948	1,011	-6%
Sterling & Wilson Solar	10,764	16,440	-35%	598	2,079	-71%	503	1,885	-73%
Sundaram Fasteners	6,928	10,188	-32%	1,161	1,932	-40%	1,031	1,115	-8%
Syngene International	5,191	4,671	11%	1,433	1,402	2%	918	870	6%
Tata Consultancy Services	398,540	373,380	7%	108,710	100,830	8%	81,180	81,210	0%
Tata Elxsi	4,235	4,070	4%	942	1,033	-9%	754	660	14%
TCNS Clothing	3,290	3,002	10%	679	507	34%	550	371	48%
Thermax	14,101	14,366	-2%	1,132	1,073	5%	850	750	13%
Thomas Cook	17,270	15,556	11%	493	420	17%	65	92	-30%
Titan Company	64,546	58,398	11%	7,584	5,912	28%	4,746	4,132	15%
Trent	8,697	6,565	32%	1,735	726	139%	557	403	38%
United Breweries	14,548	14,512	0%	2,215	2,478	-11%	1,070	1,092	-2%
United Spirits	25,825	24,969	3%	4,240	3,582	18%	2,588	2,126	22%
Varun Beverages	12,203	7,856	55%	1,157	478	142%	-593	-715	17%
V-Mart Retail	5,622	4,658	21%	1,168	733	59%	909	417	118%
3M India	7,454	7,916	-6%	979	1,675	-42%	719	1,102	-35%

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