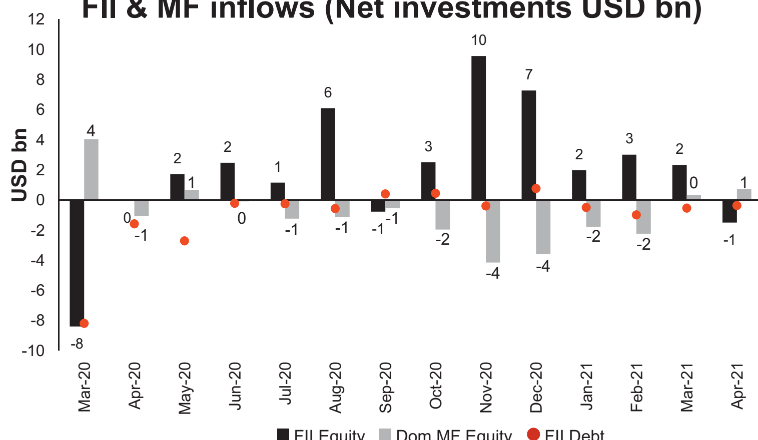
FUND MANAGER COMMENTARY

Equity Markets

Equity Market Indices

Indices	Last Close	1 Month (Change)	CYTD 2021 (Change)
Domestic			
S&P BSE Sensex TR	72199	-1.5%	2.3%
Nifty 50 TR	20811	-0.4%	4.9%
S&P BSE 200 TR	7665	0.2%	6.9%
S&P BSE 500 TR	23920	0.5%	7.9%
S&P BSE Midcap TR	24680	0.7%	13.7%
S&P BSE Smallcap TR	26047	5.0%	20.0%
NSE Large & Midcap 250 TR	9931	0.8%	10.8%
S&P BSE India Infrastructure Index TR	282	-1.3%	19.2%
MSCI India USD	702	-1.0%	3.9%
MSCI India INR	1686	0.3%	5.4%
INR - USD	74	1.3%	1.4%
Crude Oil	67	5.8%	29.8%



Market Review

Significant rise in COVID-19 cases and restrictions being imposed in several parts of the country hurt market sentiments. The second wave has now eclipsed the first wave in terms of new case load and number of fatalities and stretching the health infrastructure in many affected parts of the country. This is still an evolving situation and it is crucial to see when the new infections curve is likely peak out. Last 12 days of April saw more than 300,000 daily new cases and it hit a peak figure of 400,000 cases on the last day of the month. However, the exponential surge witnessed during the first half of April, seems to have moderated towards the end of the month as various states imposed local restrictions to curb the spread (but the absolute new case load figure still remains very high). The state wise rotation trend is providing some hope that the second wave can possibly peak in certain parts of the country soon. States that were first to see the second wave are already seeing deceleration in the number of new cases (Mumbai in Maharashtra and some stagnation seen in Delhi NCR as well) and this template is likely to play out in other regions too suggesting that we may be coming closer to the peak of the second wave. The inoculation drive has now been extended to everyone above 18 years of age and about 9.2% of the population has received at least one dose till now.

BSE Sensex and NSE CNX Nifty indices were down 1.5% and 0.4% respectively but broader market indices outperformed. BSE Small cap index outperformed gaining 5%, while BSE Midcap index gained 0.7% during the month.

The 4QFY21 earnings season has turned out to be broadly in-line so far. For the 19 Nifty companies that have declared results so far, the Net sales / adjusted EBITDA / adjusted PAT have grown 13% / 15% / 37% YoY respectively. There were no sector specific trends visible so far and beats to estimates were more driven by individual company specific factors. Private banks reported decent results with asset quality holding up well in-line with expectations. For Technology names, deal wins and commentary remained strong while revenue performance during the reporting quarter failed to surprise positively. Raw material price inflation impacted Auto profitability during the past quarter.

The high frequency indicators witnessed a slowdown during April owing to localized lockdowns / restrictions. However, given that the restrictions are not as vigorous as seen in the case of the national lockdown last year, most sectors are continuing operations at varying degrees and have not come to a complete halt. Google mobility indicators have seen a meaningful moderation especially since mid-April and is now trending closer to levels seen during September last year. E-way bill generation, fuel consumption, new vehicle registration and power demand also saw moderation. On the positive side, GST collections data showed an increase, rail freight volumes were steady while manufacturing PMI figure for April was stable on a sequential basis.

Apr 2021 was the first month of net outflows (~USD 1.49 bn) from FIIs after Sep 2020. As a result, the CYTD net inflow tally for FIIs moderated to ~USD 5.84 bn. DIIs on the other hand compensated in equal proportion for the FII outflows by remaining net buyers in equities (~USD 1.48 bn) for the second month in a row. There was almost an equal contribution from MFs (~USD 737 mn) and Insurers (~USD 746 mn) to the DII tally during the month. So far this calendar year, the DIIs have been net sellers to the tune of ~USD 1.69 bn, entirely driven by MFs (~USD 2.94 bn of net outflows), while insurers have been net buyers in equities (~USD 1.25 bn of net inflows).

Global Market Update

The global equity markets traded higher on the back of improved outlook in the developed economies (especially Euro region) after the concerns on the second COVID-19 wave has receded. MSCI World and MSCI Europe indices gained 4.5% and 4.1% respectively while MSCI EM (+2.4%) underperformed. The key events during the month included two key central banks' policy meetings (US Fed and ECB). In the FOMC meeting, the US Federal Reserve left the rates unchanged while at the same time remained committed to the ongoing QE programme. The European Central Bank (ECB) also held rates and kept the QE programme unchanged there as well.

From a global perspective, we are still in the restoration phase of the economic cycle and activity remains below pre-COVID levels in major economies other than China. High unemployment, fragile confidence and risks around vaccine rollout and virus mutations mean the global economy needs ongoing policy support. This was accommodative stance was visible across various central bank decisions / commentaries during April. Near term volatility aside, inflation is likely to remain modest over the medium term, but upside risks have increased in the US and need to be monitored as it will be a key determinant of sustaining the optimism in equities. Also, as investors we need to be vigilantly positive at the current juncture as the measures of expected returns are lower than last year. Consensus beliefs are rooted in sustained policy support and vaccine effectiveness. But with valuations now richer, small disappointments to this scenario can affect market sentiments.

Macro market view

Rapid rise in the number of new COVID cases has emerged as a key concern and its impact on the economic recovery and on growth in general, need to be evaluated. The economic recovery and fundamentals were looking bright over the past few months. There were also some good indications of the beginning of a cyclical recovery. However, the second wave has put a spanner in the works on this optimism and brought in a near term uncertainty. We have witnessed the medical infrastructure getting stretched beyond its capacity owing to the sharp surge in the new cases in several impacted regions of the country. Amidst this humanitarian crisis, the hope is that the second wave should see a peak soon and that remains the base case at this juncture. This baseline assumption has gained confidence on the back of two factors. Firstly, the curve flattening trends seen during the first wave and the same is getting repeated in this second wave in regions such as Maharashtra (specifically Mumbai), which was first region to witness the surge in cases this time around. Secondly, vaccine intervention is a powerful tool this time around and so far, the data suggest that inoculation is an effective way to shield the population from contracting the virus and in bringing down the severity of the infection. The mobility / activity restrictions have been so far localized in nature unlike the national lockdown which we witnessed last year. However, this doesn't mean that the economic impact is not going to be felt. The economic output in 1QFY22 would be impacted adversely leading to downward revision in the overall GDP estimates for FY22. Currently, the consensus GDP growth estimates are at 10.5% and it won't come as a surprise, if this estimate was to be brought down by a percentage point or two. As a result, the economic recovery may get pushed back by a quarter or two, but with a baseline assumption of near term peak to be reach on the new COVID case load, the economic recovery is not expected to be derailed completely. The timeline for peaking of the infections curve along with subsequent flattening of the curve, duration of the current localized lockdowns / restrictions and the pace of vaccination roll-outs are the key variables to look out for in the near term. Inflation is still within a comfortable range and the current low interest regime along with an accommodative stance from the RBI is likely to sustain, especially in the context of this ravaging second wave. From a medium to long term perspective, the outlook on growth remains positive. The recent budget has envisaged a multi-year expansionary fiscal policy, providing a long runway for India to take its long term sustainable growth higher. Focus on capex and infrastructure spends, should add the multiplier effect as well as improve productivity in the medium to long term. So effective execution of the budget proposals, would be a big long term positive for India and for its economic growth trajectory.

Global Market Indices

Indices	Last Close	1 Month (Change)	CYTD 2021 (Change)
International (in USD)			
MSCI World	2,939	4.5%	9.2%
Dow Jones	33,875	2.7%	10.7%
S&P 500	4,181	5.2%	11.3%
MSCI EM	1,348	2.4%	4.4%
MSCI Europe	1,983	4.1%	7.8%
MSCI UK	1,127	4.1%	9.3%
MSCI Japan	3,827	-1.5%	-0.7%
MSCI China	109	1.3%	0.9%
MSCI Brazil	1,766	5.8%	-5.9%

Equity Market view

The impact of the second COVID-19 wave is the key variable to monitor in the near term. The equity markets have been relatively resilient to the second wave and this suggests that market is assessing the disruption to be short term in nature. The market is also drawing some comfort from the corporate commentary in the quarterly results season so far, which have maintained a positive outlook beyond the near term uncertainty.

The baseline assumption is that of a temporary impact from the second wave and the new case load to peak out in 1QFY22 itself. In that scenario, the set-back in the recovery process will be limited to a few months after which we should see the economic rebound. Two other alternate scenarios can also be envisaged, the first one involving a protracted recovery due to an elongated impact of the COVID-19 restrictions and a second scenario of a permanent dislocation owing to the extended impact of the pandemic. Both these scenarios are adversarial ones for a cyclical recovery and hence from an equity market perspective. However, we assign a higher probability for a short term impact (which we are already witnessing) followed by a sharp rebound in the economic activity. Vaccine effectiveness and improved pace of inoculation are central to this thought process of a curtailed impact followed by a swift recovery.

The short term could witness volatility given the evolving scenario around the second wave. However, the outlook from a medium to long term is attractive and the recent budget has provided a fillip to the growth momentum. The strong capex push envisaged in the budget is the best since FY08 and there is an emphasis on the productive use of the deficit for structural gains for the economy. We reckon that the budget vision will put in place the structural growth drivers to be re-ignited by multiplier effect of infrastructure spends and continued consumption demand.

Market movements are dictated by surprises (both positive and negative to what is already priced in), while the lack of it may mean a range bound performance owing to absence of triggers. Currently the consensus earnings expectations for FY22 is factoring in a strong rebound, hence the room for positive surprises have potentially narrowed. The 4QFY21 earnings season has held up well but we see a probability of earnings downgrades in the near term owing to the impact of the second wave. However, in-line with the baseline assumption of only a short term impact, we reckon that the earnings will again be reset higher, once the uncertainty from the second wave recedes (similar to what we saw in FY21). We believe that by having a bottom up approach to stock selection with a focus on names that can deliver positive earnings surprises can lead equity outperformance. Markets may also provide buying opportunities in the interim through short spurts of correction, due to fear or sentimental factors (combination of the second wave and valuations) and those instances can be utilized to add to conviction bets in the portfolio from a medium to long term perspective.

Second COVID wave along with extended impact of restrictions despite the vaccine intervention, hardening of inflation expectations globally and in India and tapering off in liquidity are the key risks in the short term.

Valuations

Expansion in valuations though make the risk- reward for the equity markets, balanced at this juncture. On conventional valuation metrics like Price to Earnings / Price to Book ratios, the equity indices are trading above historical averages, which make it expensive. However, the lower interest rate environment is likely to remain in the short term as a result the low cost of capital scenario should remain as well. This makes equities relatively attractive compared to other asset classes despite the valuations. On P/E basis, Nifty is currently trading at 20.3x / 17.6x FY22/23 earnings estimates, with significant earnings rebound assumed over the next 4 quarters. We have witnessed 2 consecutive quarters of earnings upgrades, but this trend could halt due to the second wave disruption. On P/B, Nifty is trading at 2.9x / 2.6x FY22/23 estimates.

(Source: Bloomberg, MOSL & HSBC MF estimates as on Apr 2021 end).

Key Factors to Consider

- COVID-19: Extended impact of the second wave, risk of elongated of restriction or nationwide lockdowns (timeline & regions) and resultant economic impact.
- COVID-19: Vaccination programme and execution / efficiency of the inoculation roll-outs.
- Remainder of the 4QFY21 earnings season and the corporate commentary.
- Key risks are – Spike in interest rates, rise in global commodity prices (including crude oil), stimulus being withdrawn too early or the lack of add-on stimulus and geo-political risks.

Portfolio Strategy and Update

We continue to prefer dominant businesses having scalable businesses, available at reasonable valuations. Over the past few years, we've witnessed a trend of profit pool consolidating with the dominant players in respective sectors/industries. We believe that this trend will accelerate as the COVID related disruption is of higher magnitude as well as encompasses more sectors. This has increased our resolve to be true to our philosophy. We believe that those stocks would stand to gain market share even in the sluggish phases of the economy and achieve revenue traction when the economy returns to normalcy. From a medium to long term perspective, the current phase of disruption shall also pave way for accelerated digital adoption by consumers as well as enterprises both in India and globally. Another long term theme is that of diversification of the global supply chain due to 'China + 1' strategy which could be adopted by corporates as well as economies and India could stand to benefit out of that.

We are closely watching the evolving situation related to the second wave. Our baseline assumption is that of a short term impact of the crisis followed by a quick rebound afterwards. As a result, we have not made changes to the portfolio positioning for now and maintain a pro-cyclical bias. This is on the back of a medium to long term view that the economy would see a cyclical recovery due to revival in capex cycle over the next 3-4 years (first by the government followed by private capex). This, we believe has brought in a multi-year earnings growth visibility, providing a constructive outlook for equities in general and domestic cyclical segments in particular. Benign cost of capital and reasonable valuations (in the context of multi-year earnings outlook), should act as additional support to the equity performance, in the medium term. We continue to have bottom up approach along with focus on earnings growth, for stock selection. Companies which can provide strong earnings growth along with positive earnings surprises would continue to do well and would be able provide outperformance. So while earnings growth will still the most important element that we focus on, but within that there is an emphasis on ideas with scope for positive earnings surprises. Our investment strategy will also focus on earnings growth implied by the valuations in the context of prevailing cost of capital and excess liquidity. Due to the evolving scenario connected to the second wave, the markets may remain volatile in the near term and any sharp corrections would be used to add to our conviction bets or where valuations turn reasonable.

We currently hold positive view on Financials, Industrials, Healthcare, Real Estate, Technology and Consumer Discretionary sectors in-line with the thought process outlined above. We are also looking beyond the current disruption on account of the second wave, which we believe would be temporary in nature. We are neutral on Materials. The recent budget has all the ingredients to revive the capex cycle, which was so far missing and should also gradually lead to pick up in the investment cycle. This in turn can potentially raise the long term sustainable growth rate of the economy by close to couple of percentage points in our view. That reflects our positive view on Financials and Industrials sectors. Banks also should benefit from the budget focus around the system clean-up and growth orientation. We believe that Financials and Industrials have the potential to surprise positively on earnings momentum, post the current disrupted phase. In Financials (specifically in private banks), we believe that the earnings surprises will be driven by lower than expected credit costs coupled with recovery in credit growth. In Real Estate it will be driven by demand factors (residential affordability) and industry consolidation benefiting the larger listed players. We are also positive on Cement and Specialty chemicals, owing to strong demand recovery in the former while the latter being a beneficiary of the global supply chain diversification away from China. Our exposure in the Consumer Discretionary basket is oriented towards Auto and within non-auto segment the preference is for market leaders / dominant players. Technology is another sector that we like. We believe that the current trend of digital adoption and "migration to cloud" are structural in nature and this should result in improving growth momentum over medium term. We hold negative view on Consumer Staples, Telecom (both due to lack of earnings surprises), Energy and Utilities.

** Returns mentioned in the report are the Total Return or TR variants of the respective domestic indices. USD return for global indices.*

Source – Bloomberg, HSBC Asset Management India.

Sector Allocation

Sector^	HSBC Large Cap Equity Fund	HSBC Flexi Cap Fund	HSBC Small Cap Equity Fund	HSBC Tax Saver Equity Fund	HSBC Equity Hybrid Fund ^^	HSBC Large & MidCap Equity Fund	HSBC Focused Equity Fund
Consumer Discretionary	O/W	UW	O/W	E/W	O/W	O/W	O/W
Consumer Staples	U/W	U/W	O/W	U/W	U/W	U/W	U/W
Energy	U/W	U/W	U/W	U/W	U/W	U/W	U/W
Financials	E/W	O/W	E/W	O/W	O/W	O/W	E/W
Healthcare	O/W	O/W	O/W	O/W	O/W	E/W	E/W
Industrials	O/W	O/W	E/W	O/W	O/W	O/W	O/W
Information Technology	E/W	E/W	U/W	E/W	E/W	O/W	E/W
Materials	E/W	O/W	E/W	U/W	U/W	E/W	U/W
Real Estate	O/W	O/W	O/W	O/W	O/W	O/W	O/W
Utilities	U/W	U/W	U/W	U/W	U/W	U/W	U/W
Communication Services	U/W	U/W	U/W	O/W	U/W	U/W	U/W

O/W - Overweight U/W - Underweight E/W - EqualWeight N/A - Not applicable

^ GICS - Global Industry Classification Standard (GICS) ^^ For equity portion only