The Earnings Card

June 2022

A brief update on quarterly earnings for markets and our funds

FY22 earnings end on a strong note

Earnings for FY22 have ended on a strong note

19% profit growth on a 3Y CAGR basis, significantly higher than top-line CAGR of 9% and real GDP CAGR of 2%. The pandemic profit boom is attributable to global reflation (which lifted exports as well as prices), market share gains from unorganized, and easy liquidity. This coupled with deleveraging has resulted in strong corporate and bank balance sheets.

Key highlights

Top-line growth is holding up, but is largely led by prices, rather than volumes

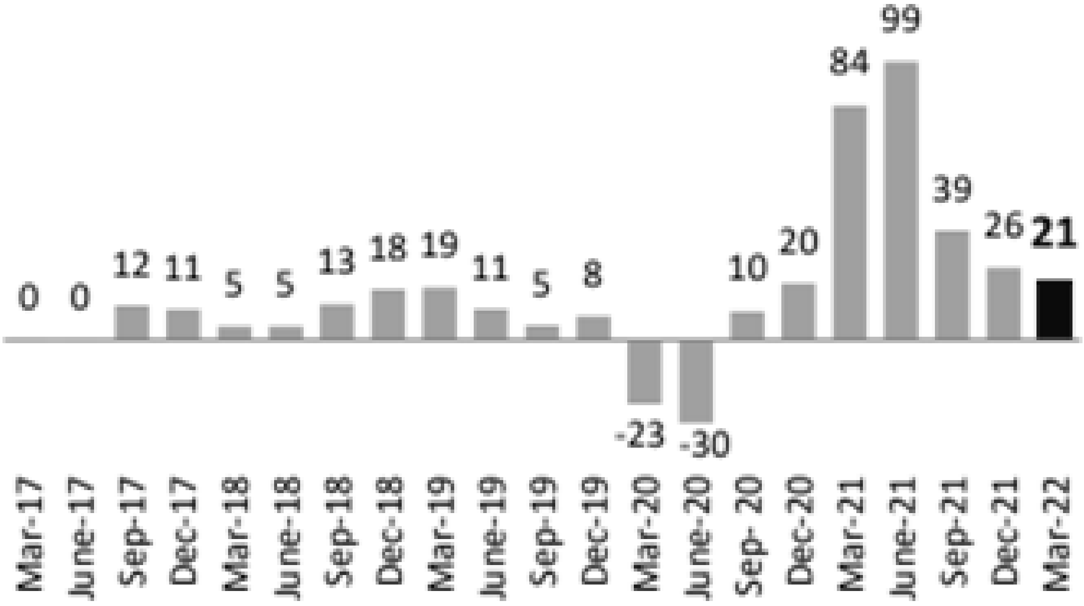
Margin pressure, though high, seems to be ebbing owing to price hikes and cost rationalisation

FY23E & FY24E Nifty EPS growth at 18% and 14% respectively

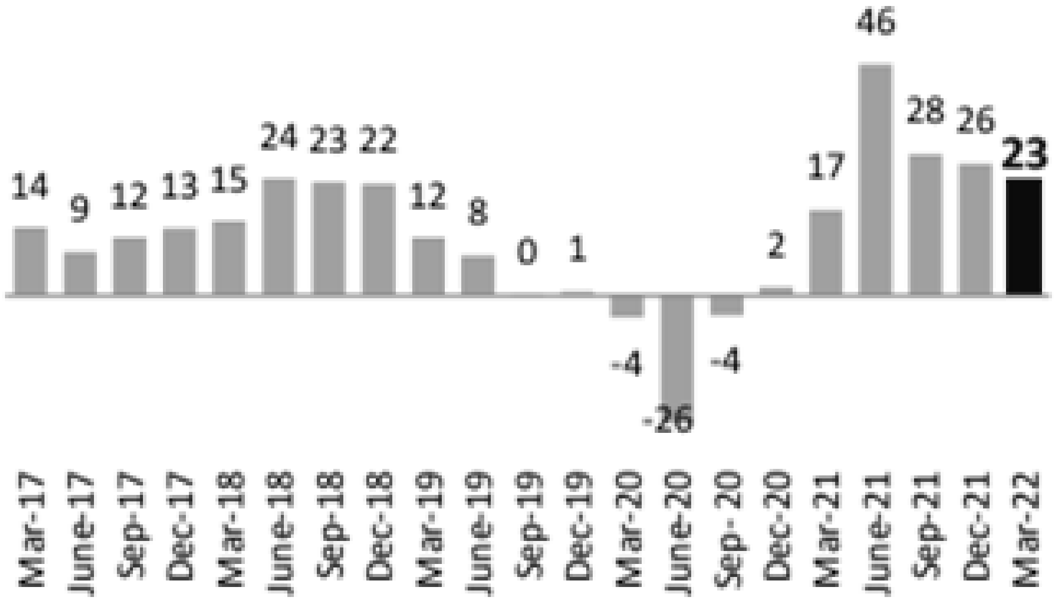
Source: Edelweiss Research

Strong PAT and Sales growth

Nifty 50 PAT up 21% YoY in March Quarter



Nifty 50 sales up 23% YoY in March Quarter



Source: Bloomberg

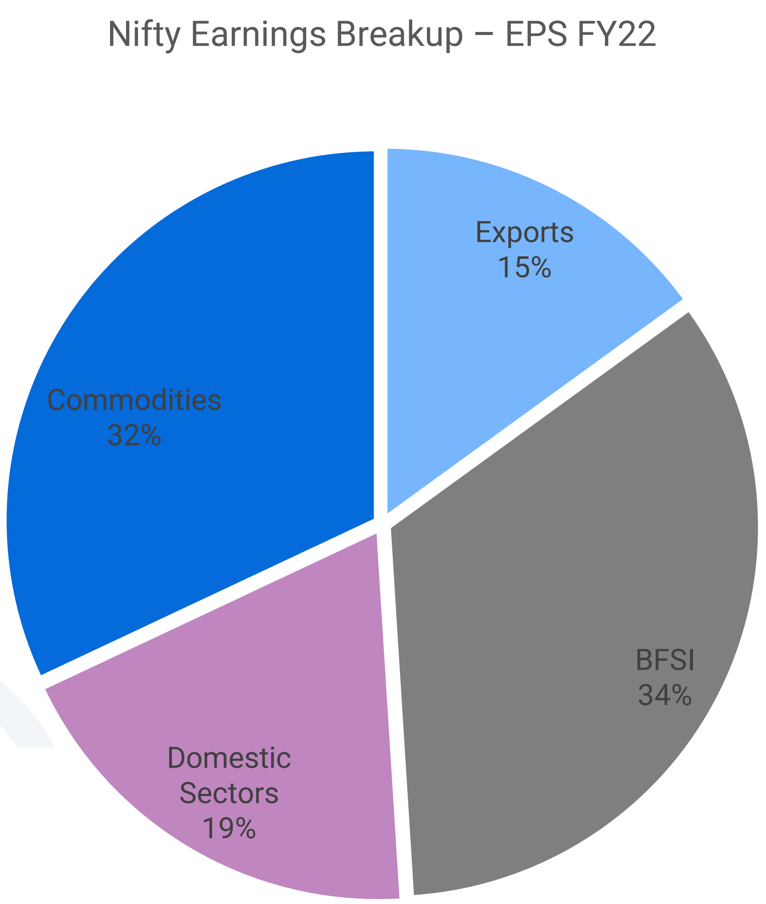
Sectoral earnings trend and share

		EPS Growth %			
Sector	**Share in Nifty 50 FY22 EPS**	**FY 21**	**FY22**	**FY 23**	**FY 24**
BFSI	**34%**	**29**	**33**	**26**	**18**
Banks	28%	38	38	26	18
NBFC	6%	4	17	21	17
Insurance	0%	4	(4)	36	16
Exports	**15%**	**10**	**23**	**34**	**20**
IT	14%	12	16	11	15
Pharma	3%	42	29	12	19
Export Auto	(2%)	72	(7)	(160)	93
Commodities	**32%**	**34**	**92**	**(2)**	**3**
OMC	2%	235	5	(21)	13
Energy	14%	25	45	27	6
Metals & Mining	16%	28	206	(25)	(4)

		EPS Growth %			
Sector	**Share in Nifty FY22 EPS**	**FY 21**	**FY22**	**FY 23**	**FY 24**
Domestic Consumption	**10%**	**3**	**10**	**32**	**23**
Domestic Auto	3%	(0)	(9)	37	24
Consumer Staples	5%	(7)	13	10	13
Telecom	0%	(111)	716	237	55
Consumer Discretionary	1%	(2)	32	32	22
Domestic Investment	**9%**	**2**	**12**	**17**	**15**
Utilities	4%	3	4	8	7
Agro Chemicals	1%	26	26	31	18
Industrials	3%	(14)	19	36	20
Cement	1%	41	22	(4)	27
Nifty	**100%**	**19**	**40**	**18**	**14**

Source: Edelweiss Research

Commodities and banks key contributors



- Contribution of global and domestic sectors in earnings is largely the same.
- Rising commodity prices, though a bane for the economy, are a boon for Nifty earnings.
- To that extent, a slowdown in the same pose high risks for earnings going forward.
- On the domestic front, banks are the critical driver of Nifty earnings.
- Excluding it, the share of domestic sectors is the same as that of exporters such as IT and pharma.

Source: Bloomberg

Sectoral trends

Domestic consumption: A large divergence was seen in EBITDA growth—auto companies posting improvement while that in durables moderated. The gap between the two has narrowed, and the trend should further continue in FY23.

Domestic investment: Cement companies posted weak EBITDA/t as input prices hurt. Industrial and power companies, on the other hand, reported better top-line and margin performance as government capex improved.

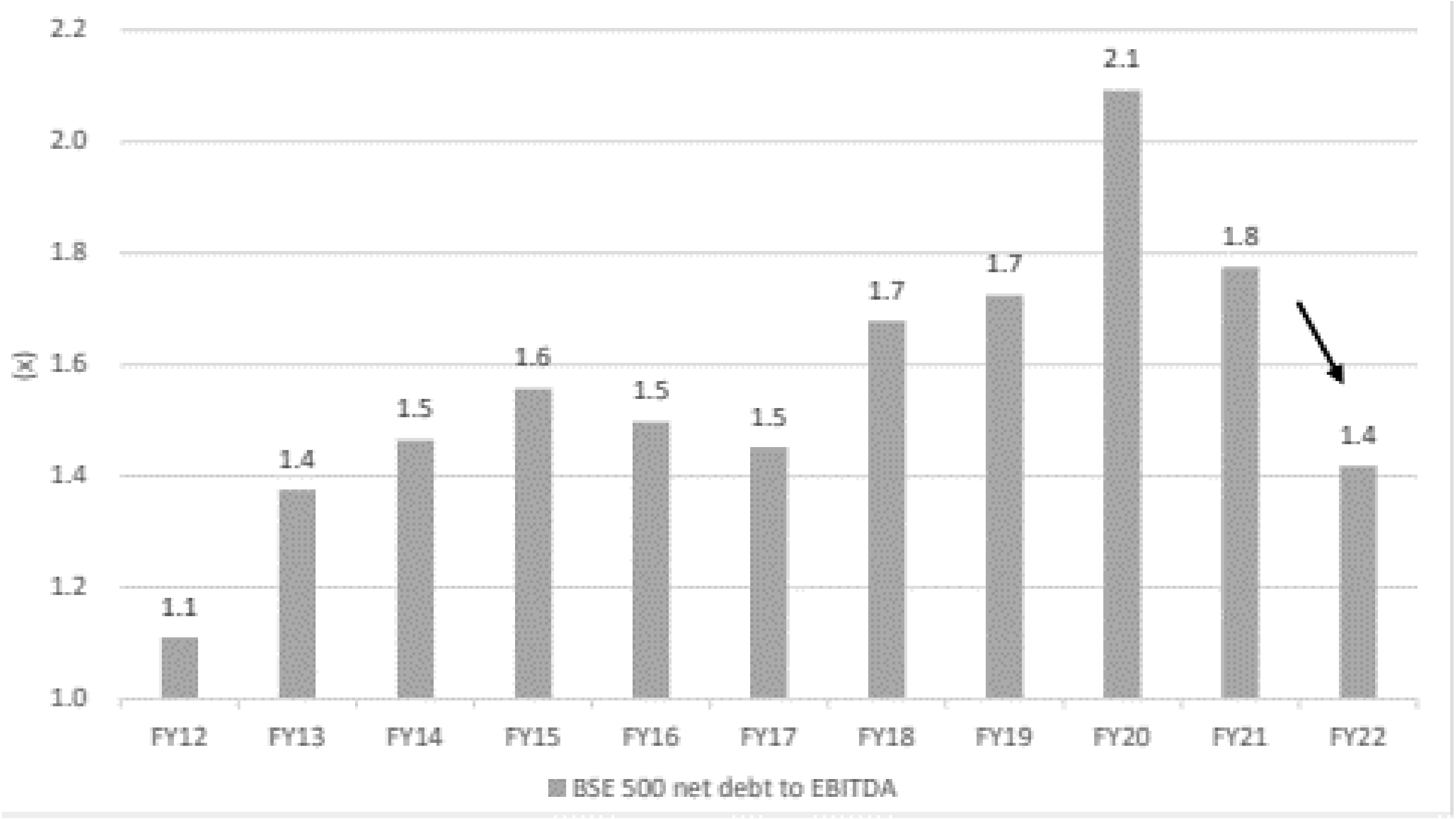
Global exporters: IT companies reported a strong top line, but margins moderated. Chip shortage weighed on export auto, while pharma was a mixed bag. Chemical companies posted strong growth. Hereof, we anticipate broad-based demand risks.

Commodities: OMCs disappointed on marketing margins (inventory loss), while upstream energy companies posted strong results. Metal companies' profits moderated significantly. Unwinding global reflation to weigh on commodity profits.

Financials: Slippages and credit costs continued to ease. However, Pre-Provision Operating Profit (PPoP) growth slowed and was disappointing. In FY23, with credit costs now normalised, PPoP growth will likely drive earnings; on that front, private banks are more favourably placed.

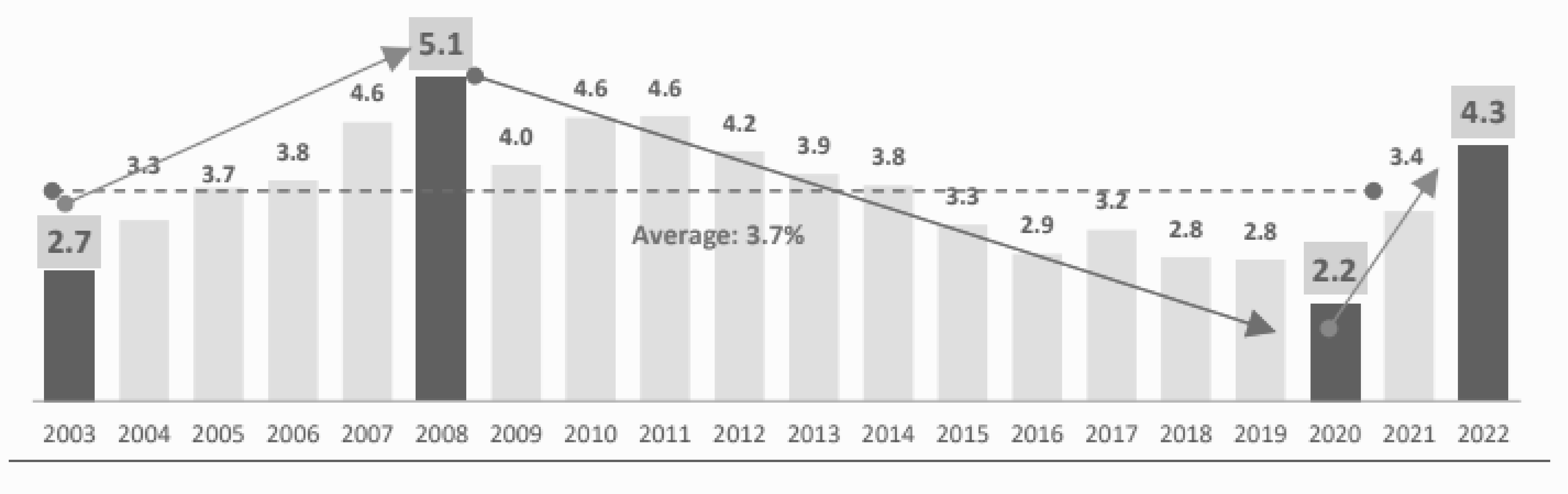
Corporate balance sheet has improved

- Corporate leverage position has improved significantly in FY22
- The combination of strong operating cash flows and low capex has resulted in significantly improved corporate balance sheets.



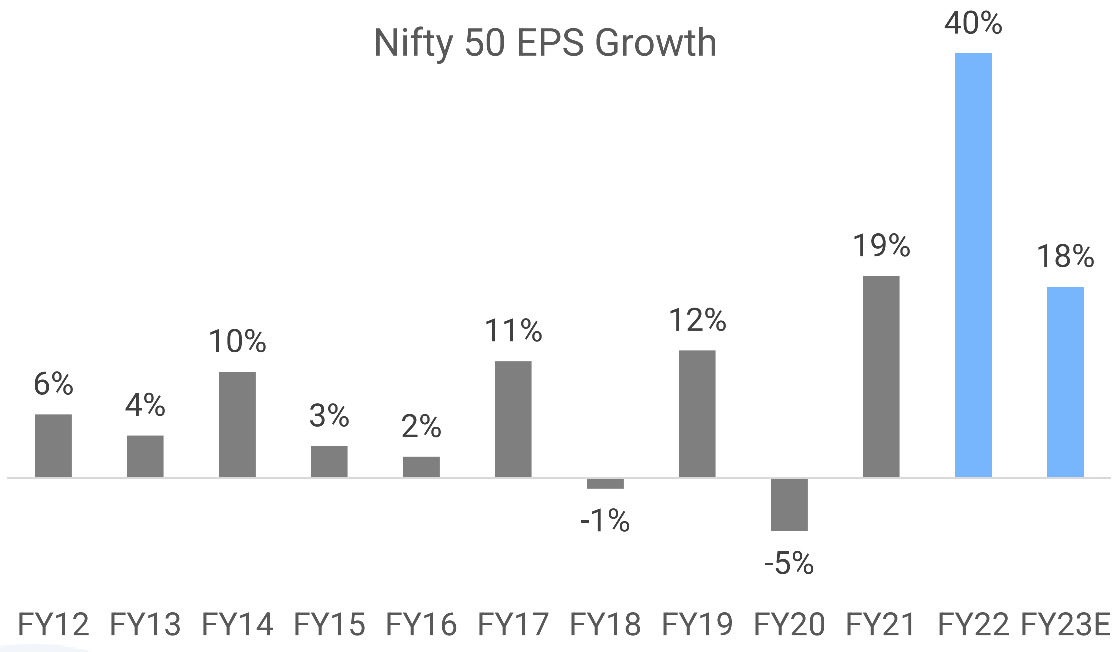
Corporate profit to GDP ratio at a decade high

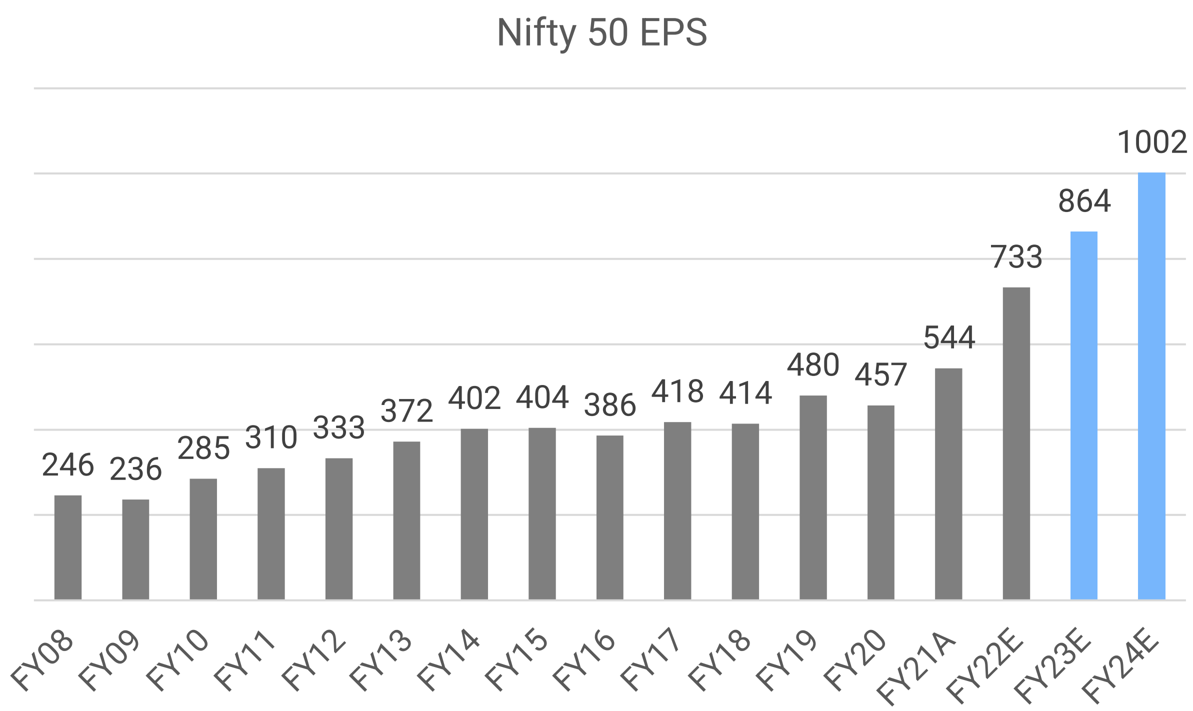
- The corporate profit to GDP ratio rebounded to a decade high of 4.3% and 4.5% for the Nifty-500 Universe.
- The recovery was driven by the expansion in the economy, as the denominator i.e. GDP grew 19.5% YoY in FY22, while corporate profit rose at a faster rate of 48% YoY (for the Nifty-500 Universe)



Source: Motilal Oswal Report

Earnings growth expectations remain strong





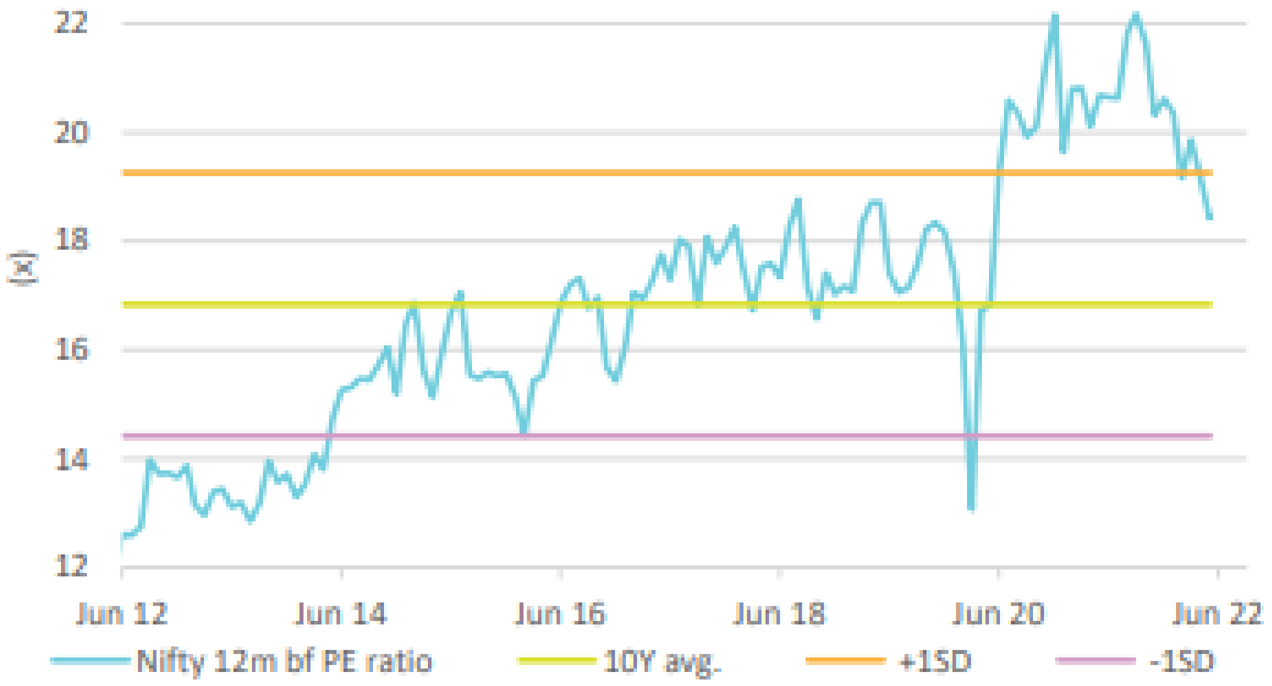
* With regards to Nifty earnings, FY22 has posted a very strong 40% growth on a high base of 19% in FY21 – leading to the best phase of profitability in the last decade.
* Going ahead, while market participants are building in moderation in earnings, the earnings growth may still grow are strong double digits.

Source: Bloomberg estimates

Valuations are more reasonable now

* Market correction so far has been entirely driven by valuation de-rating.

* Hence, as a result, 1Y forward valuations are now at 18x – 1Y forward – in line with the last 5Y average.



Source: Edelweiss Research

How are our portfolios positioned

Earnings growth for our portfolios

Fund	EPS Growth				PE Ratio	
	FY22Q4	FY22	FY23	FY24	FY23	FY24
Edelweiss Flexi-Cap Fund	23.8%	25.0%	25.4%	23.1%	21.80	17.73
Edelweiss Large & Mid Cap Fund	21.2%	21.6%	19.5%	23.0%	22.52	18.32
Edelweiss Long Term Eq Fund (Tax Saving)	25.1%	26.8%	22.7%	23.7%	21.04	17.02
Edelweiss Mid Cap Fund	0.5%	11.5%	-1.6%	23.0%	24.74	20.14
Edelweiss Small Cap Fund	15.6%	18.7%	8.6%	23.1%	22.95	18.68

Source: Internal Estimates

Sector OW/US positions

Scheme Name	Sector	% Over wt	Sector	% Under wt
Edelweiss Mid Cap Fund	Chemicals & Fertilisers	6.27	Oil & Gas	-6.30
	Industrial/Infra	3.90	Textiles	-1.94
	BFSI	2.98	Auto & Auto Ancillaries	-1.77
Edelweiss Flexi-Cap Fund	Industrial/Infra	7.06	Oil & Gas	-5.01
	Chemicals & Fertilisers	2.12	Consumer	-4.66
	Healthcare	2.10	Technology	-2.50
Edelweiss Large & Mid Cap Fund	Industrial/Infra	4.49	Oil & Gas	-4.67
	BFSI	2.02	Technology	-2.60
	Chemicals & Fertilisers	1.05	Power	-1.76
Edelweiss Small Cap Fund	Industrial/Infra	6.79	BFSI	-6.66
	Chemicals & Fertilisers	2.72	Media & Entertainment	-2.82
	Transportation	2.15	Leisure Services	-2.11
Edelweiss Long Term Equity Fund	Industrial/Infra	4.54	Oil & Gas	-5.15
	BFSI	3.39	Power	-3.31
	Auto & Auto Ancillaries	1.77	Consumer	-2.17

% OW/UW is in comparison to respective benchmark

How are we navigating high inflation and rising rates

Our funds have active exposure to these 3 sectors that are beneficiaries or show resilience during rate hike cycles and high inflationary environment

Consumers

- Consumer companies that have pricing power continue to do well during high inflation-interest rate regime
- Margins are stable as demand for such goods is inelastic to inflationary pressures.
- Positive on businesses that have pricing power and have better brand acceptance.

Industrials

- When interest rates rise the economy is usually on a stronger footing and industrial activity tend to remain strong and resilient.
- Industrial manufacturing can pass on the higher cost without impacting demand
- Positive on industrial manufacturers who have pricing power and demand is picking up for their products.

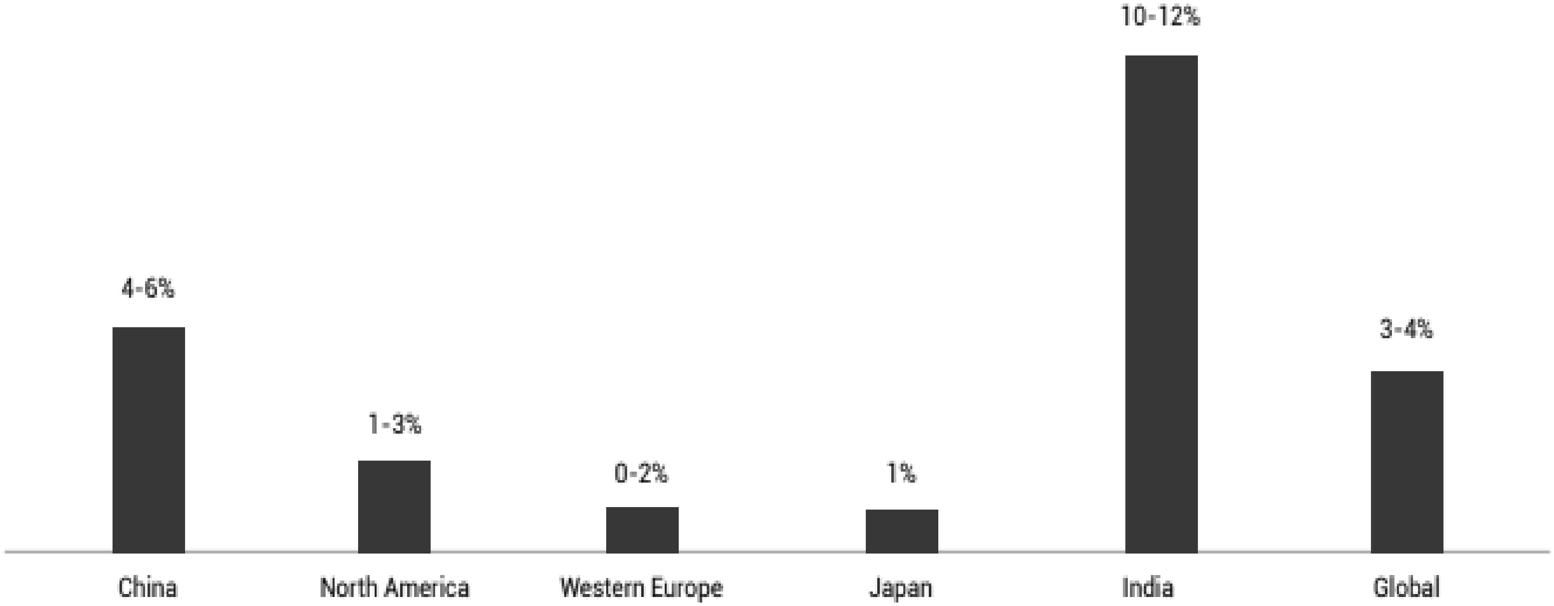
Lending Financials

- Financial sector has historically been among the most sensitive to changes in interest rates.
- Profit margins that expand as rates climb, entities like private banks and lending financials benefit from higher interest rates.
- We have active exposures to select private sector lenders and some dominant lending franchise

Why we own; What we own – Specialty Chemicals

- Global Specialty chemical market is ~USD 800 bn. where India's share is 1/4th that of China.
- Indian companies have just scratched the surface. Some of the largest specialty chemical companies in India have less than USD 1 bn sales compared to global market size of USD 800bn.
- Indian Chemical industry at the cusp of taking majority of the world's market share, with several legal and pollution issues in China. [Read detailed note here]

Region-wise expected growth in specialty chemicals (CY 2020-2025 CAGR)



Source: CRISIL Researc

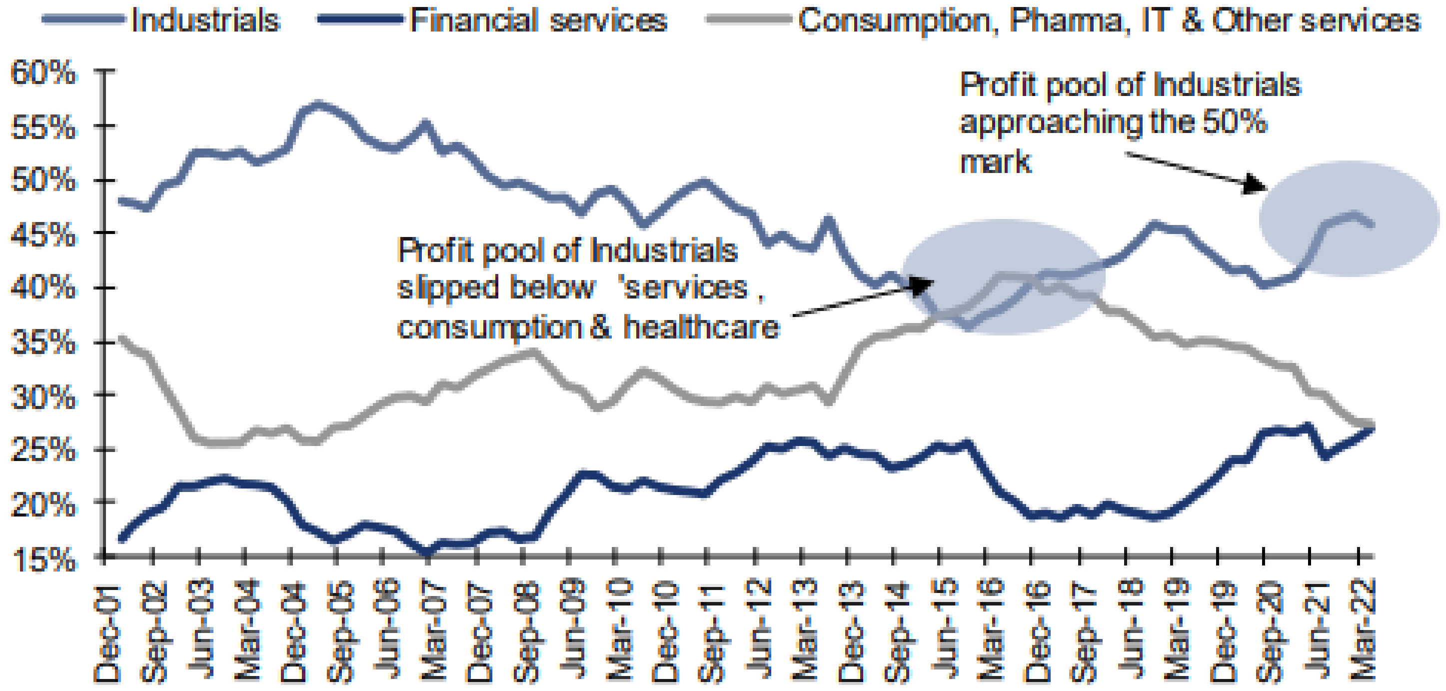
Stocks we own in portfolios	
Navin Fluorine International Ltd.	Tata Chemicals Ltd.
Atul Ltd.	Vinati Organics Ltd.
Aarti Industries Ltd.	Deepak Nitrite Ltd.
SRF	Fine Organic Industries Ltd.
Nocil Ltd.	Sudarshan Chemical Industries Ltd.

The above stocks are currently part of the portfolio. There is no assurance or guarantee of future position in the above stocks.

Why we own; What we own – Industrials

- Government's thrust on capital expenditure to boost economy and high spends on infra bodes well for industrials
- When interest rates rise the economy is usually on a stronger footing to withhold this regime change and hence, industrial activity tend to remain strong and resilient.
- Industrial manufacturing businesses are also mostly beneficially of high commodity prices since they can pass on the higher cost without impacting demand to a large extent.

Rising share of industrials in aggregate profits amongst top 1000 companies



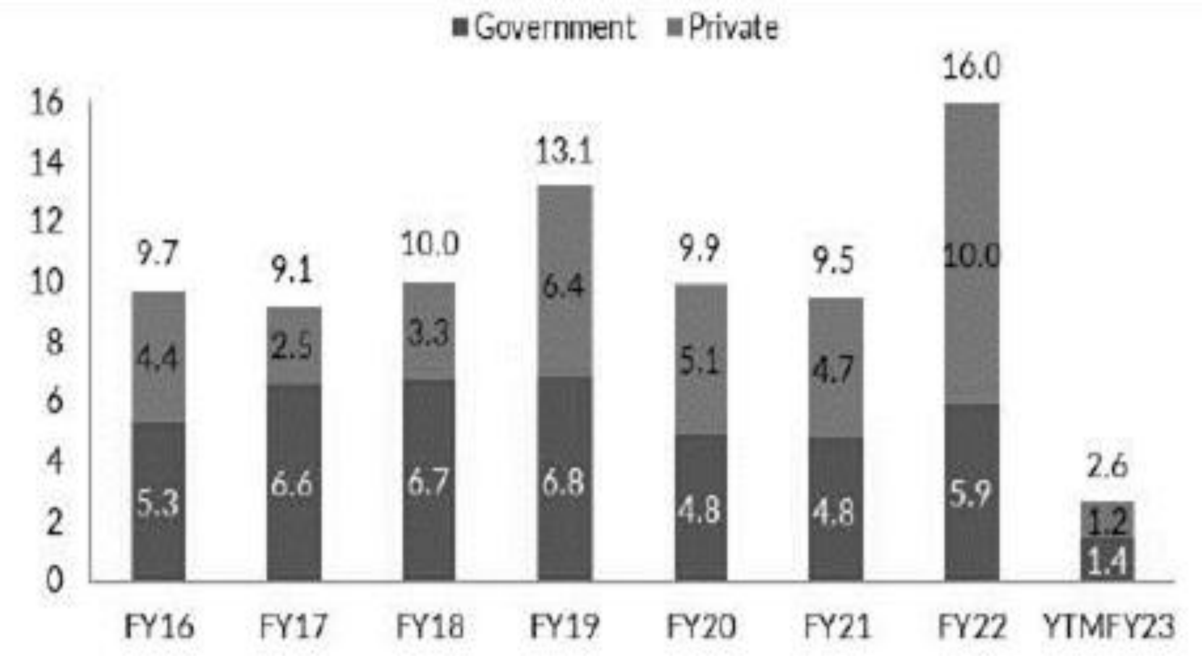
Stocks we own in portfolios
ABB India Ltd.
Cummins India Ltd.

Data Source: I-Sec research. The above stocks are currently part of the portfolio. There is no assurance or guarantee of future position in the above stocks.

Industrials - Corporate India well geared to step up capex

- Order inflows for large, listed capital goods companies at Rs 258 bn is the highest in the last 15 quarters and recorded a 52% growth vs. Dec-20 and 35% QoQ.
- Similarly, order backlog at Rs 925 bn as of Dec-21 is at record levels since FY15 and witnessed growth of 16% vs. Mar-21 and 7% vs. Sep-21.
- Data Centre proliferation:-India's data centre capacity is 650 MW. Europe is more than 10x the size at 8,500 MW, although India's internet user base stands at 700 mn vs Europe's 400 mn. USD 13.9bn spends are committed with 1,000 MW capacity, while another 1,350 MW is in advance stages of discussion.

New investments announcement by private sector is improving

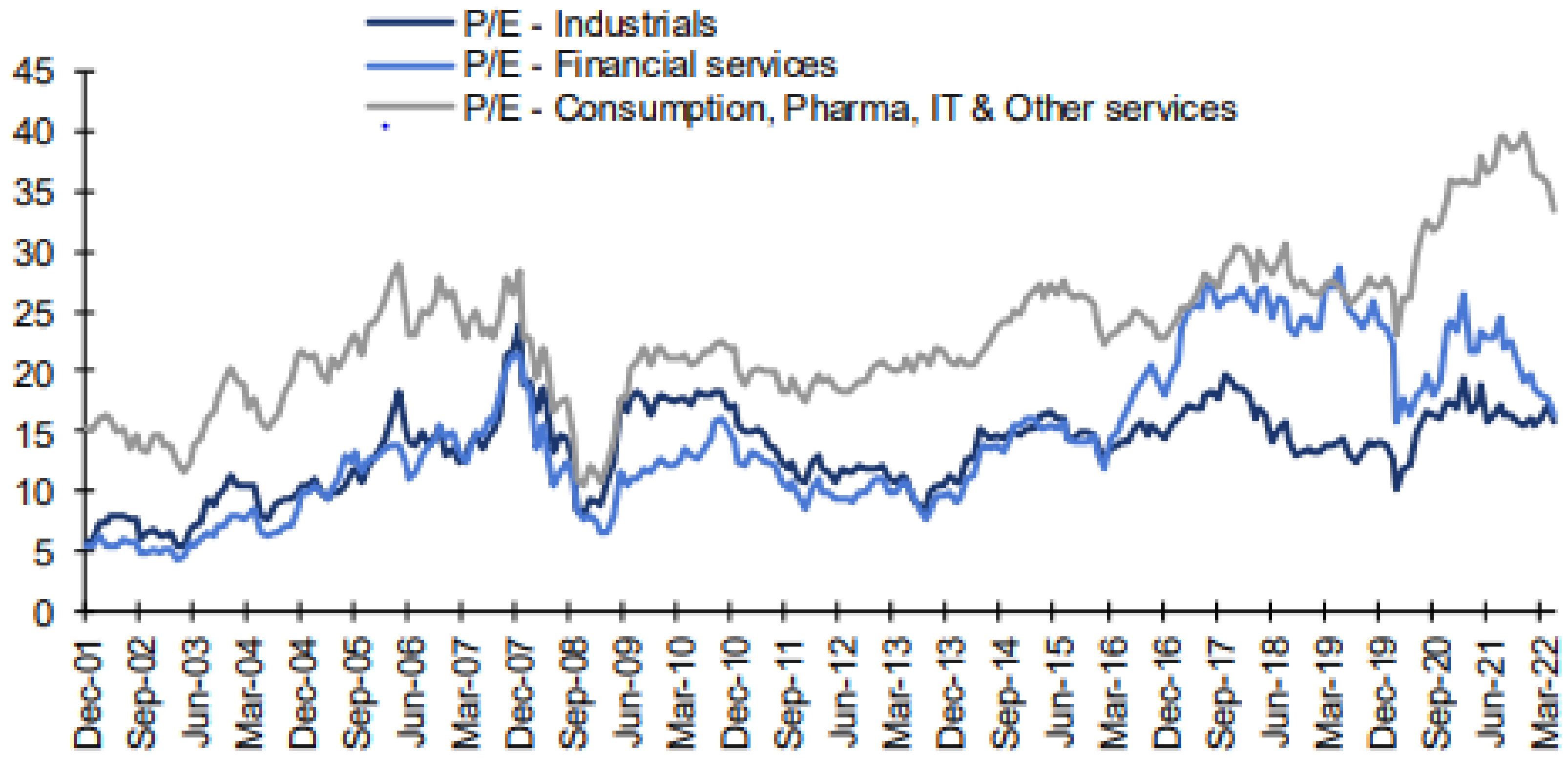


Source: Axis Capital

BFSI and Industrials are relatively cheaper

Trailing P/E of industrials and financials are at reasonable levels compared to history and other sectors.

Our portfolios are largely O/W on lenders and industrials



Data Source: I-Sec research.

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