

August 19, 2022

Cooling off commodity prices provide comfort amid marginal decline in earnings post Q1; remain positive

The recent cool off in key commodity prices viz. metals, crude among others comes as a breather for global equity markets, which are currently wary of ongoing geopolitical issues and interest rate hikes by central banks to control inflation. Management commentary is upbeat on demand prospects and recovery in margin profile amid muted corporate earnings for Q1FY23, which witnessed low single digit QoQ growth in topline and double digit bottomline decline with pressure on gross margins. Nifty EPS for Q1FY23 came in at ~₹ 177/share, down 14% QoQ. Major disappointment came in from the oil & gas sector wherein marketing margins came in lower than estimated. However, capital goods, metals & mining and pharma space surprised on the positive side. Domestically, with a capex cycle revival on the anvil (public + private) coupled with strong consumer demand across most categories (passenger vehicles, retail, etc), Indian markets witnessed a smart recovery and were up ~18% from recent lows. We remain constructive on the overall markets and believe the present market offers an attractive risk-reward play to build a long term portfolio of quality companies, which have lean balance sheets, are capital efficient in nature and have growth longevity.

Exhibit 1: Nifty and Sensex targets

Revised Sensex & Nifty Target (Rolling 12 Months')				
Earning Estimates	FY21	FY22	FY23E	FY24E
Nifty EPS (₹/share)	515	720	785	925
Growth (% YoY)	17.1%	39.8%	9.0%	17.8%
Earnings CAGR over FY21-24E				21.5%
Earnings CAGR over FY22-24E				13.3%
Target P/E Multiple on FY24E EPS				21.0
Nifty Target (using FY24E EPS)				19,425
Corresponding Sensex Target				64,700

Source: ICICI Direct Research

Incorporating revised PAT estimates post Q1FY23, our forward estimates witness a decline of ~2%. Over FY22-24E, albeit on a high base, Nifty earnings are seen growing at a CAGR of 13.3%. We now value the Nifty at 19,425 i.e. 21x PE on FY24E EPS of ₹ 925 wherein we marginally increase our PE multiple to 21x vs. 20x earlier tracking cool off in commodity prices and consequent positive impact on inflation and resultant modest rate hike velocity by central banks vs. the aggressive stance depicted earlier.

Sectoral earnings

Incorporating Q1FY23 results, single digit downgrades were seen across most sectors with upgrades visible only in the auto, FMCG and pharma space.

Exhibit 2: Sectoral EPS (₹/share)

₹/share	Sectoral Weight (%)	Old EPS			New EPS			Avg Change (%)
		FY22	FY23E	FY24E	FY22	FY23E	FY24E	
BFSI	36.0%	236	288	346	236	283	338	-1.4%
IT	15.2%	95	109	123	95	104	119	-2.6%
Oil and Gas	13.3%	107	137	138	107	112	132	-7.4%
FMCG	8.7%	37	42	46	37	42	48	1.9%
Capital Goods	2.9%	17	22	27	17	22	27	0.8%
Auto	5.8%	29	36	52	29	46	56	11.5%
Metals and Mining	3.3%	110	84	80	110	78	80	-2.4%
Power	2.0%	36	34	37	36	34	37	0.1%
Telecom	2.2%	4	15	21	4	11	20	-8.8%
Pharma	3.8%	19	22	26	19	23	26	1.5%
Others	6.8%	29	32	38	29	30	40	0.1%
Aggregate	100%	720	820	935	720	785	925	-1.8%

Source: ICICI Direct Research

Nifty Sectoral Weights*

Sectors	Weight (May 2022)	Weight (Aug 2022)	Change (bps)
BFSI	35.7%	36.0%	33
IT	15.8%	15.2%	-60
Oil and Gas	14.0%	13.3%	-74
FMCG	8.4%	8.7%	25
Capital Goods	2.7%	2.9%	21
Auto	5.5%	5.8%	32
Metals and Mining	3.2%	3.3%	12
Power	2.0%	2.0%	-5
Telecom	2.3%	2.2%	-8
Pharma	3.9%	3.8%	-9
Others	6.5%	6.8%	32
Total	100%	100%	

*Index weights are dynamic in nature consequent to market price movement & susceptible to change.

Highlights

- Global & domestic markets witnessing volatility over ongoing geopolitical issues and interest rate hike by key central banks. RBI increased the repo rate by another 50 bps to 5.4% in August 2022 with total rate hike pegged at 140 bps in the current upcycle
- On the economic parameters front, data points are encouraging in terms of GST collection, PV sales order-book and e-way bill generation (four-months high of 7.6 crore in July 2022)
- Monthly GST collection came in at a three month high of ₹ 1.5 lakh crore for July 2022 vs. ₹ 1.45 lakh crore in June 2022 & ₹ 1.41 lakh crore in May 2021
- Incorporating the revised estimates, our Nifty earnings undergo a small downward revision of ~2%. We now value the Nifty at 19,425 i.e. 21x PE on FY24E EPS of ₹ 925/share vs. 20x PE earlier taking some comfort from recent cool-off in commodity prices. Corresponding target for the Sensex is at 64,700. These are our rolling 12 months' index target
- As structural bets, we like capex linked capital goods, domestic consumption plays including autos and PLI oriented domestic manufacturing play

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