panorama

November 2023

Key Insights:

Share of small-cap funds in total equity fund flows has moderated due to stretched valuations

- Small-cap funds experienced the highest inflows during Apr-Oct'23, while large-cap funds faced outflows
- Share of small-cap funds in total equity inflows has, however, diminished since reaching a peak in July 2023
- Investors are choosing to keep their funds invested for a longer duration, avoiding rapid churning
- Equity FPI flows into emerging markets, including India, have turned negative due to global risk aversion

Reduction in the unemployment rate conceals the absence of good-quality jobs

- India's unemployment rate has decreased from 6% in 2017-18 to 3.2% in 2022-23
- The share of low-paying informal sector jobs in total employment has increased at the expense of salaried jobs
- Increase in the share of agriculture and construction in employment also indicates poor quality of job creation
- Steep improvement in female labour force participation, particularly in rural areas, but job quality is subpar

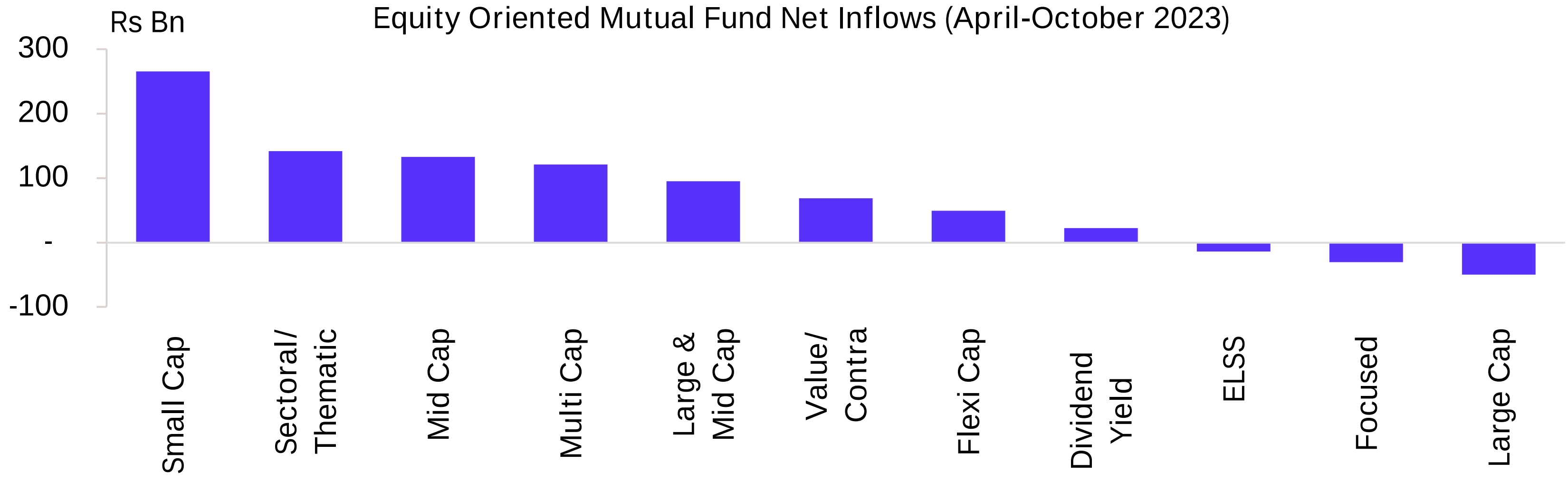
Banks are posting near-record profits even as deposit rates catch up to lending rates

- The rise in the term deposit (TD) rates is leading to a fall in the spread between lending and deposit rates
- Decreasing CASA ratio is also raising the cost of deposits due to a higher share of high-cost TDs in liabilities
- Banking sector credit growth remains robust, and deposit growth has also recovered
- Banks are reporting near-record profits on account of strong credit growth and a decline in provisions

Flow of Funds

Small-cap funds witness the largest inflows in FYTD24

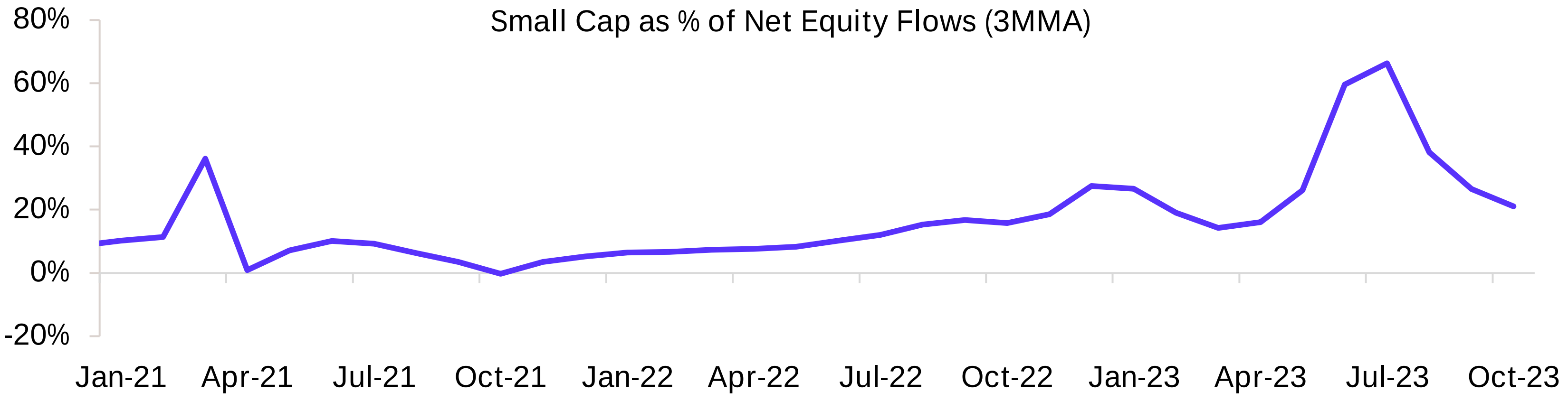
Large-cap, focused and ELSS funds experience net outflows in the financial year till October 2023



Small-cap funds witnessed the largest inflows during April-October 2023, followed by sectoral/thematic funds and mid-cap funds

Large-cap, focused and ELSS funds witnessed net outflows during the same period

Small-cap and mid-cap indices have witnessed a much stronger rally in the recent period in comparison to large-caps



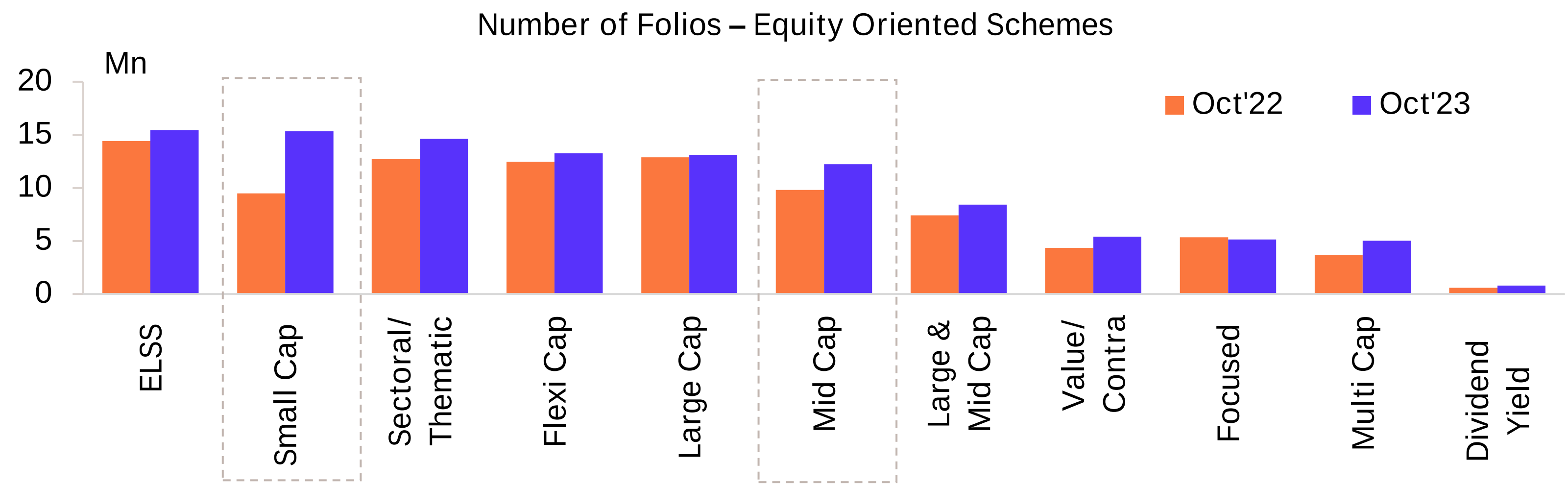
The share of small-cap funds in total equity inflows has diminished since reaching a peak in July 2023, due to stretched small-cap valuations

Source: CMIE, 360 ONE Asset Research

Note: 3MMA: 3 month moving average

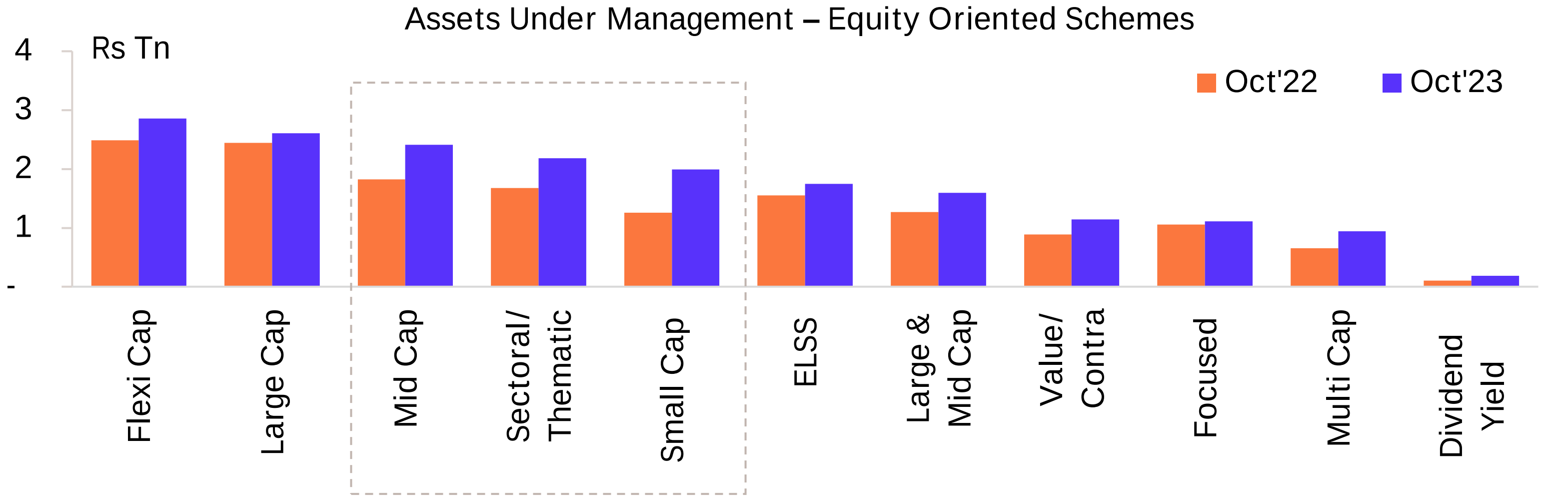
Small-cap funds witness steep increase in the number of folios

Small-cap, mid-cap, and sectoral/thematic funds have fueled the growth in AUM over the last year



Small-cap funds witnessed the steepest increase in folios since October 2022, followed by mid-cap funds

Sectoral/thematic funds also experienced a healthy rise in the number of folios, while the increase in folios for large-cap funds was comparatively muted



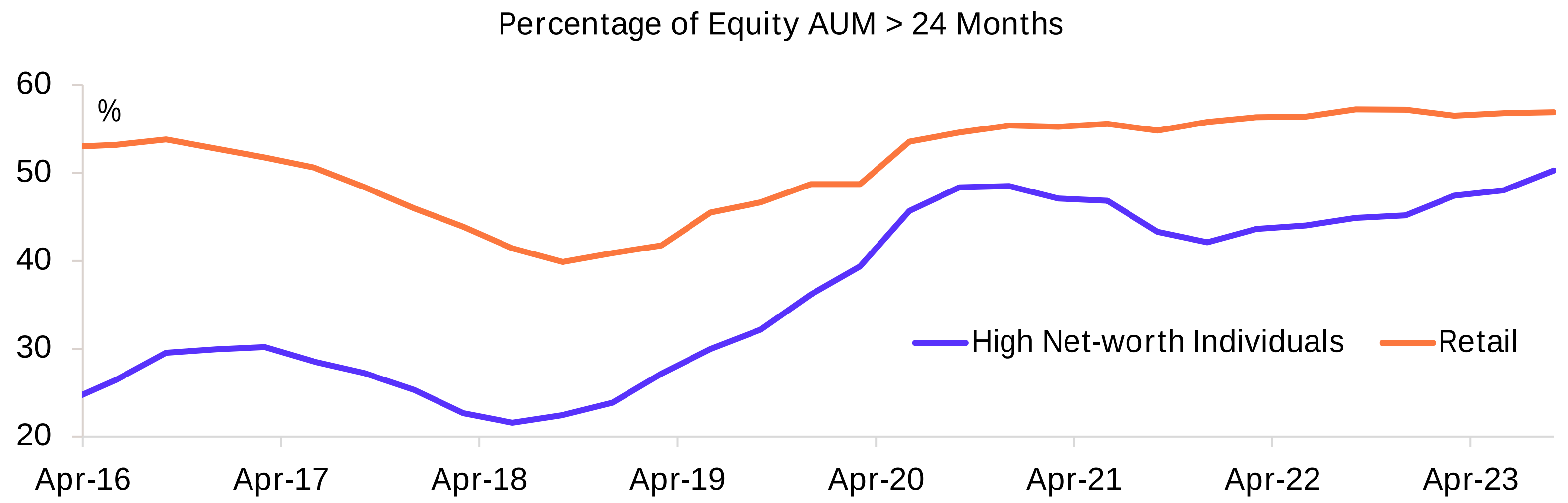
Small-cap, mid-cap, and sectoral/thematic funds witnessed the largest increase in AUM, in that order, over the last year

It's important to note that the rise in AUM is a result of both fresh inflows into the funds and an increase in valuations

Source: CMIE, 360 ONE Asset Research

Mutual fund investments are increasingly held for a longer duration

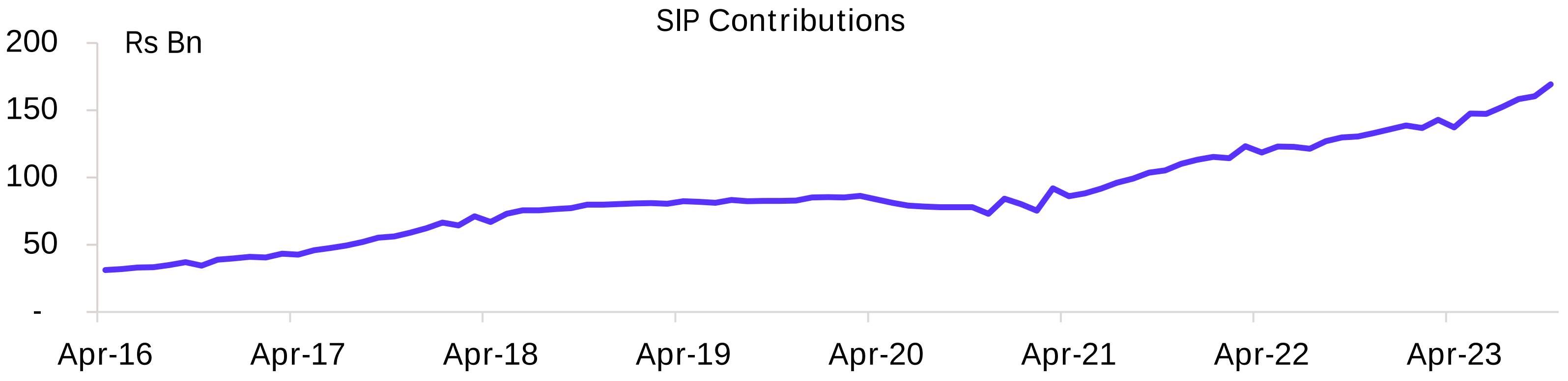
Steady improvement in SIP flows with total contribution reaching an all-time high in October 2023



The percentage of Equity AUM held for greater than 24 months has increased from 22% in September 2018 to 50% in September 2023 for high net-worth individuals

For retail, the share has improved from a low of 40% to 57% during the same period

Thus, investors are choosing to keep their money invested in mutual funds for a longer time frame rather than frequently buying and selling or 'churning' their investments



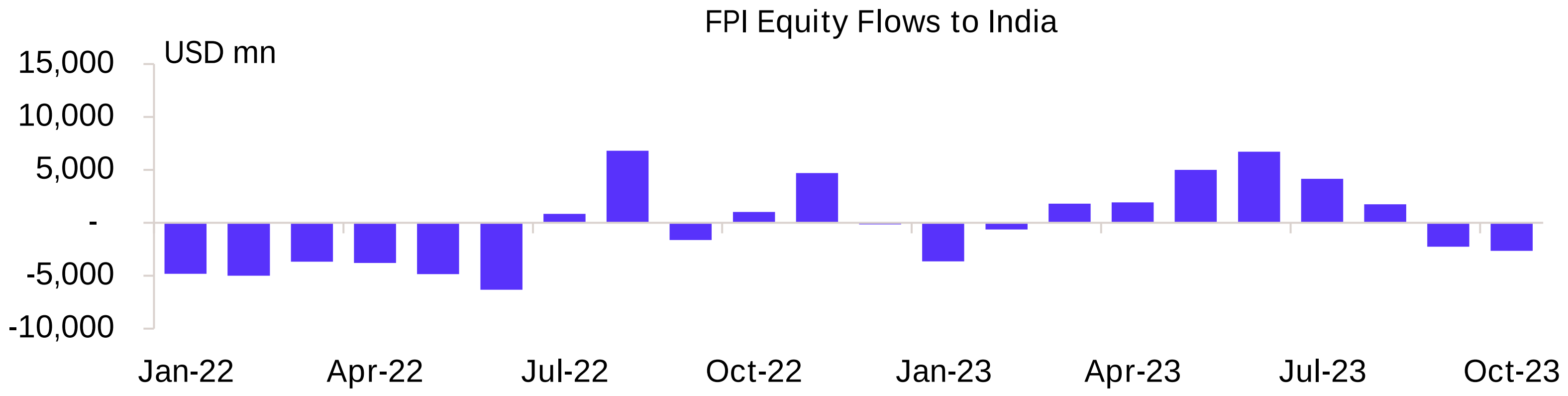
SIP contributions have also steadily increased since April 2021, with inflows reaching a peak every month since July 2023

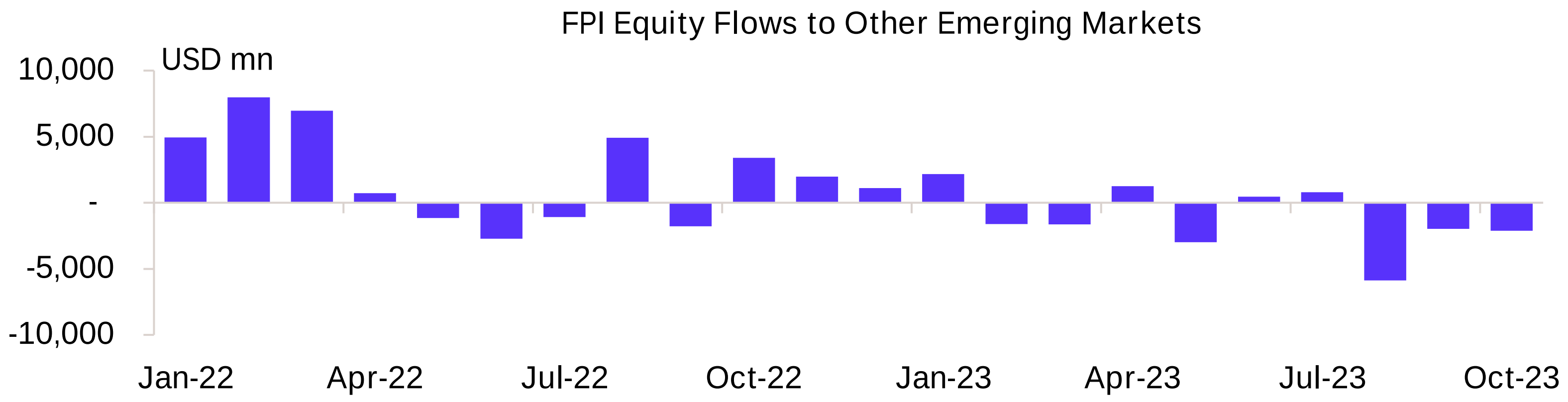
Source: AMFI, 360 ONE Asset Research

Note: High Net-worth Individuals are defined as Individuals investing 2 lakhs and above

FPI equity flows have turned negative due to risk aversion

The recent rally in treasury yields and weakening of the US dollar should support FPI flows into equity markets





Foreign Portfolio Investors (FPIs) turn risk-averse and withdraw from emerging markets, including India, on heightened global financial volatility

A 'higher for longer' monetary policy stance, surging bond yields worldwide, escalating geopolitical tensions, and a strengthening US dollar contributed to capital outflows

The recent rally in treasury yields, decline in crude oil prices, and weakening of the US dollar should support FPI flows into emerging market equities

Source: NSDL, Bloomberg, 360 ONE Asset Research

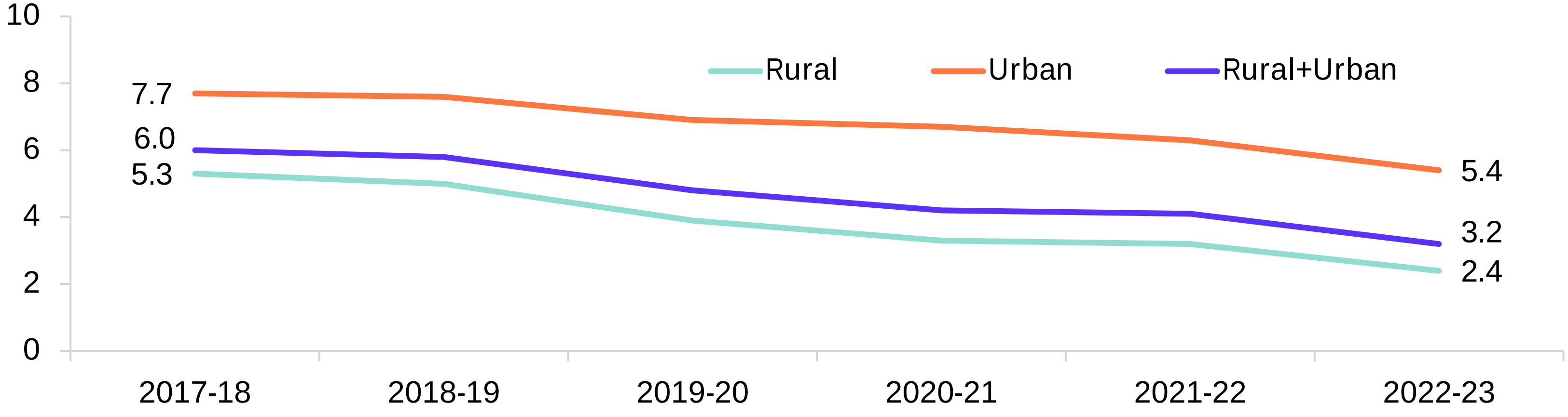
Note: Other emerging markets include Thailand, Vietnam, Indonesia, Brazil and South Africa

Labour Trends

Unemployment rate drops across both rural and urban regions

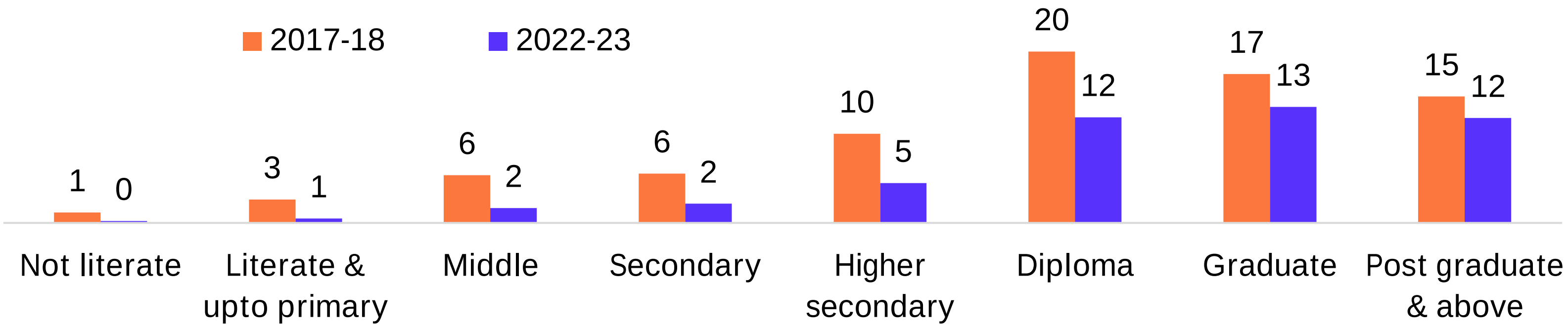
Unemployment falls across education levels but persists at elevated levels for individuals with higher education

Unemployment Rate (%) – 15 years & above



India's unemployment rate has decreased from 6% in 2017-18 to 3.2% in 2022-23, with the decline observed in both rural and urban areas

Unemployment Rate (%) by Education Level



The decline in the unemployment rate has been witnessed across all education levels, although the unemployment rate tends to remain high among the more qualified

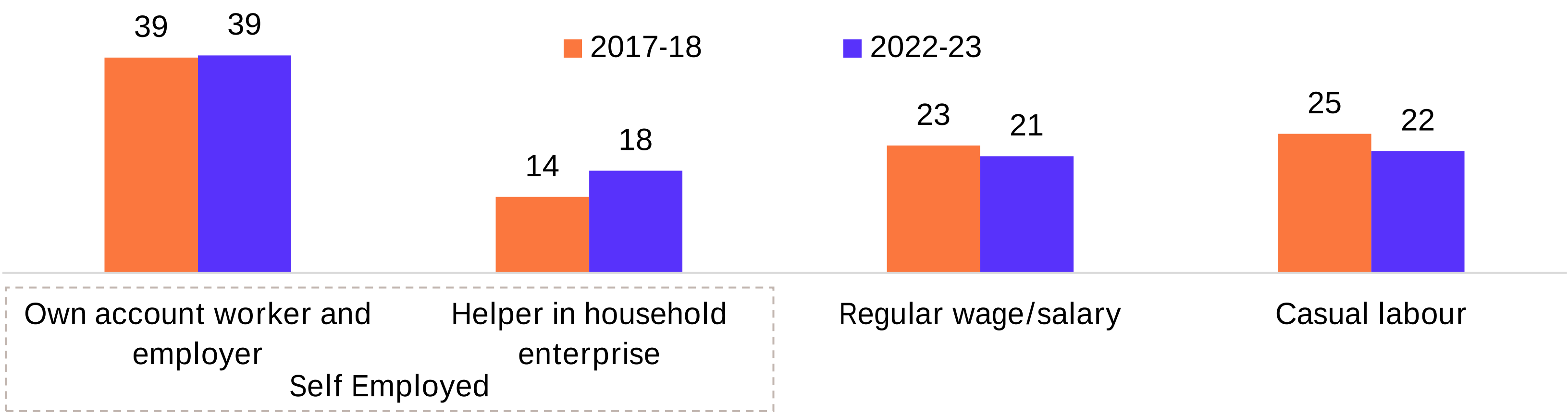
Note: 2022-23 refers to the period July 2022 – June 2023 and likewise for 2021-22, 2020-21, 2019-20, 2018-19 and 2017-18
All data pertains to usual status (ps+ss) for persons of age 15 years and above

Source: PLFS, 360 ONE Asset Research

The quality of job gains has been subpar

The share of 'helper in HH enterprise' in employment has increased, whereas the share of regular wage/salary has decreased

Percentage Distribution of Workers by Employment Status

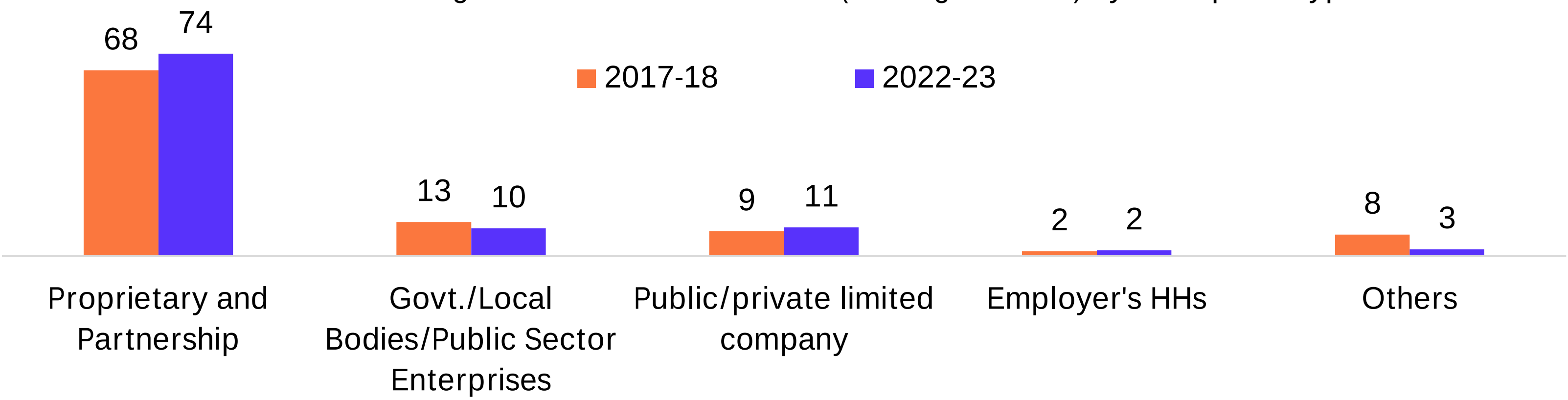


The share of individuals working as 'helpers in household enterprises' has increased, and these positions typically constitute low-paying jobs in the informal sector

The share of regular wage/salaried employment has decreased, and these tend to be the higher-paying formal jobs

On a positive note, the share of casual labour (daily wage workers) has decreased

Percentage Distribution of Workers (Non-agriculture) by Enterprise Type



In PLFS, proprietary and partnership enterprises are considered as informal sector enterprises

By this criterion, the share of the informal sector in employment has increased from 68% in 2017-18 to 74% in 2022-23, in contrast to the general expectations of a decline in the informal sector

Source: PLFS, 360 ONE Asset Research

Sectoral employment share also indicates poor quality of job creation

Share of agri and construction sectors in employment has increased, while manufacturing sector's share has declined

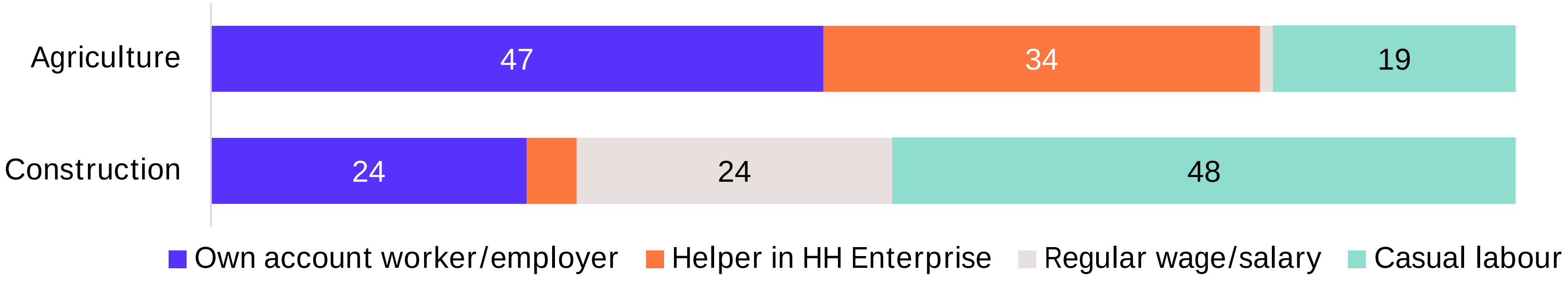
Employment Share (%)	2017-18	2018-19	2019-20	2020-21	2021-22	2022-23
Agriculture	44.1	42.5	45.6	46.5	45.5	45.8
Mining & quarrying	0.4	0.4	0.3	0.3	0.3	0.3
Manufacturing	12.1	12.1	11.2	10.9	11.6	11.4
Electricity, water, etc.	0.6	0.6	0.6	0.6	0.6	0.5
Construction	11.7	12.1	11.6	12.1	12.4	13.0
Trade, hotel & restaurant	12.0	12.6	13.2	12.2	12.1	12.1
Transport, storage & communications	5.9	5.9	5.6	5.4	5.6	5.4
Other services	13.2	13.8	11.9	12	11.9	11.4
Total	100	100	100	100	100	100

The share of agriculture in total employment has increased from 44.1% in 2017-18 to 45.8% in 2022-23. The share of construction during the same period has increased from 11.7% to 13%

An increase in the share of employment in agriculture and construction sectors indicates a decline in job quality, as both sectors are characterized by informal, low-paying, and low-productivity work

Weak consumption trends and a K-shaped recovery reflect the poor quality of job creation

Percentage Distribution of Workers by Employment Status (2022-23)



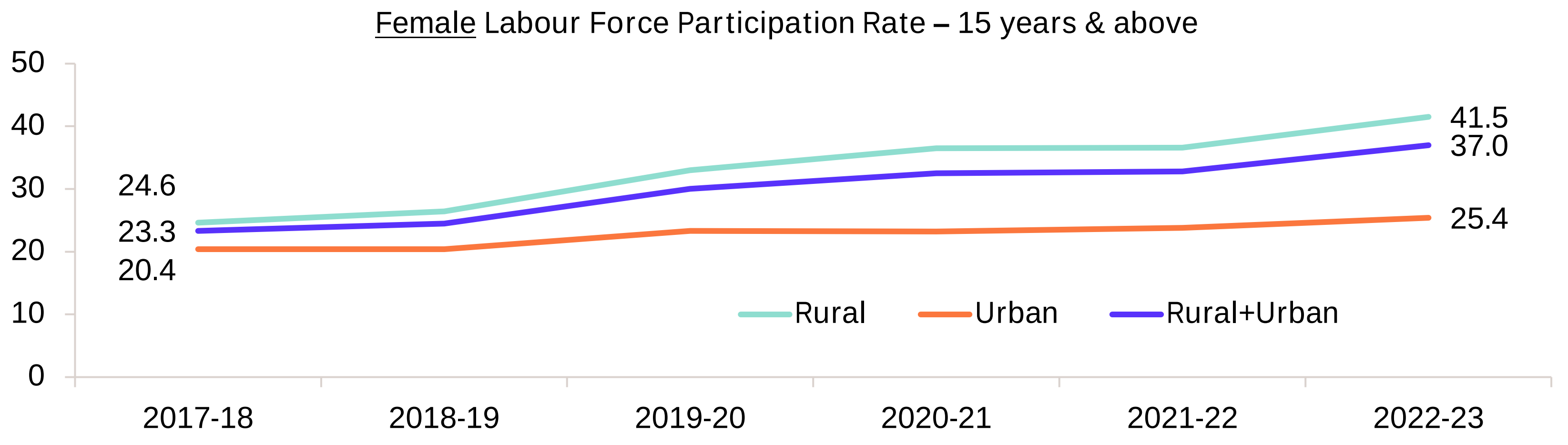
The agriculture sector is mainly characterized by self-employment, either as an own-account worker or as a helper. The sector also faces high levels of disguised unemployment

The construction sector is characterized by a higher share of daily wage casual labour

Source: PLFS, 360 ONE Asset Research

Steep improvement in female labour force participation in rural areas

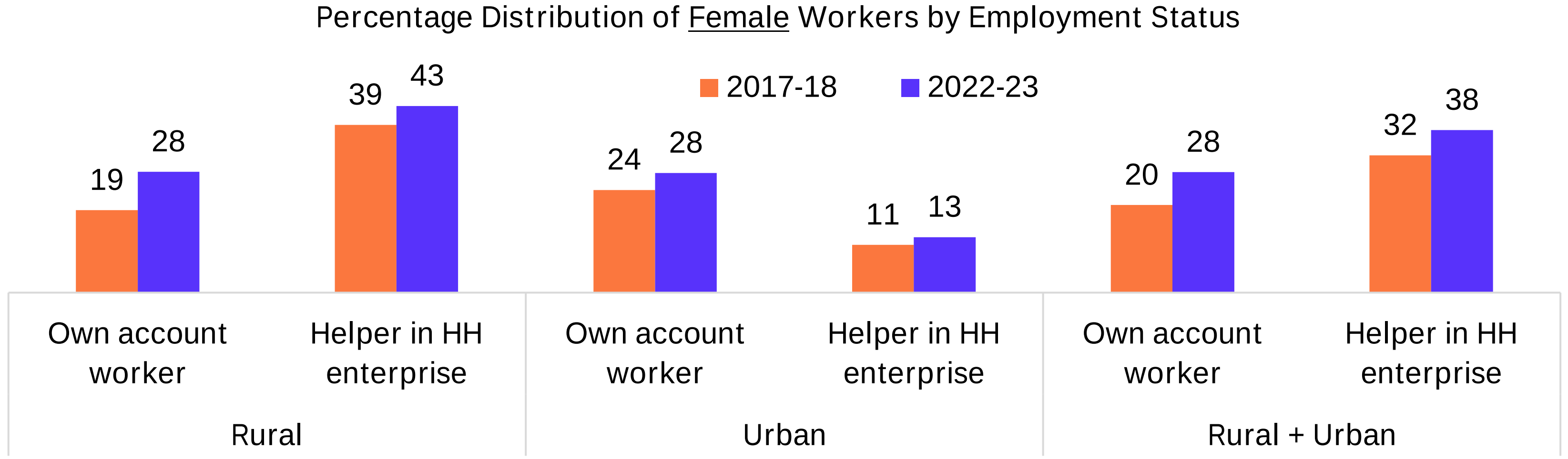
The increase in employment is driven by self-employment, which tends to offer lower pay compared to salaried jobs



Female labour force participation has improved considerably, particularly in rural region

Female unemployment has decreased from 5.6% in 2017-18 to 2.9% in 2022-23

However, the job gains seem to be concentrated in low-quality positions



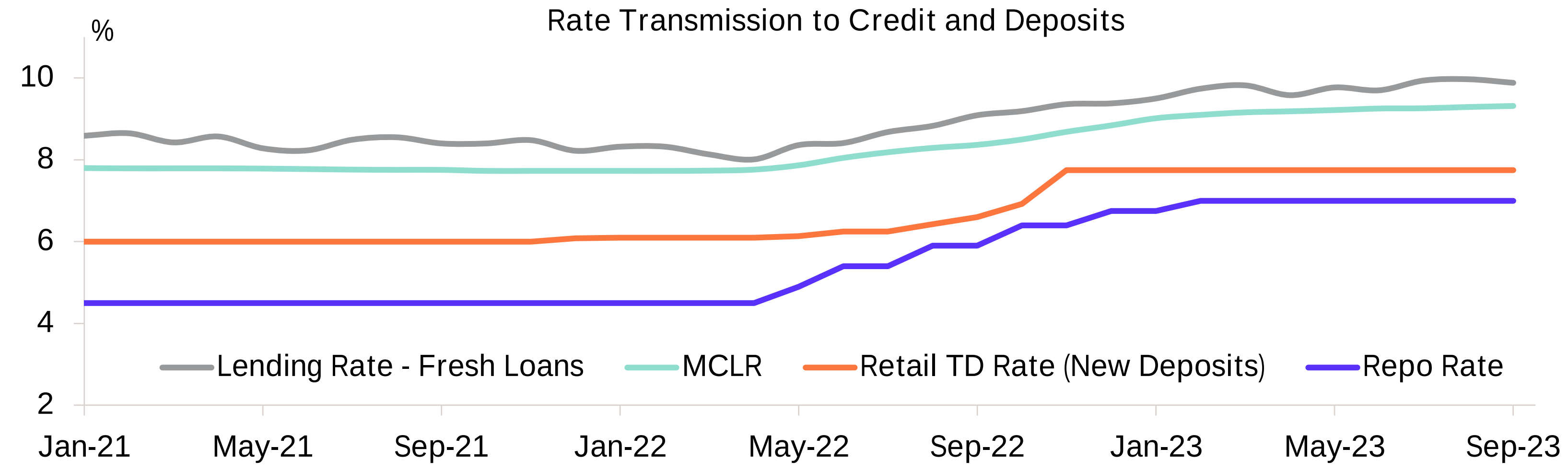
The share of self-employment (own account worker + helper in HH enterprise) in the female workforce has increased in both rural and urban regions at the expense of better-paying salaried jobs

Source: PLFS, 360 ONE Asset Research

Rate Transmission & Banking Sector

Deposit rates are catching up to lending rates

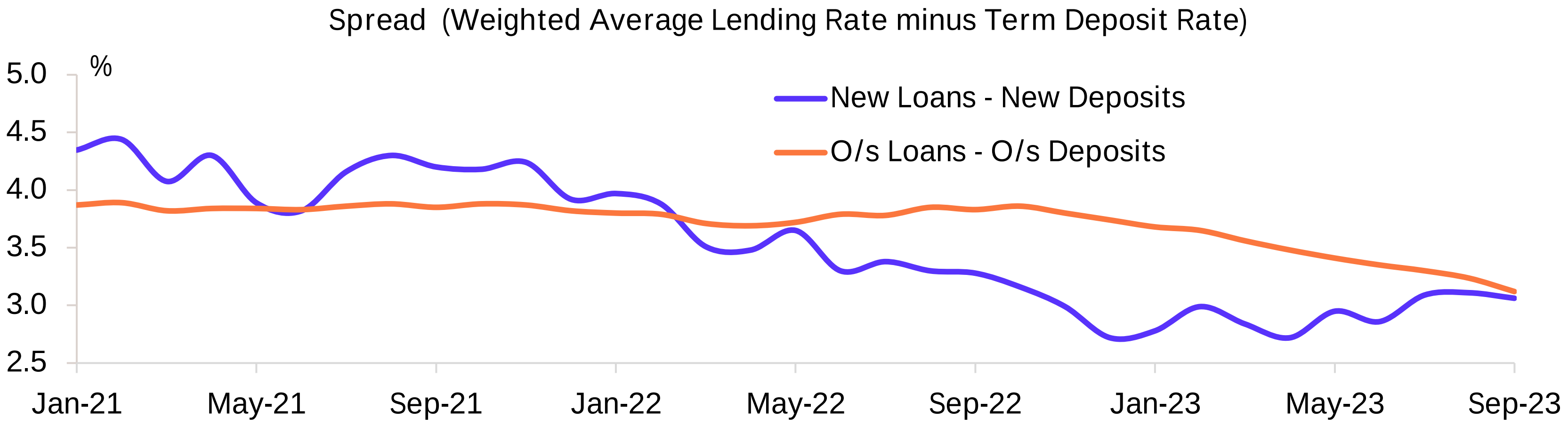
Rate hike transmission to deposit rates is reducing the spread between lending and deposit rates



Repo rate hikes were quick to transmit to the credit market as External Benchmark Linked Rates (EBLR) are reset on a quarterly basis

However, there is a delay in the transmission to the deposit rates

As liquidity conditions tighten, banks are offering higher term deposit rates to attract deposits



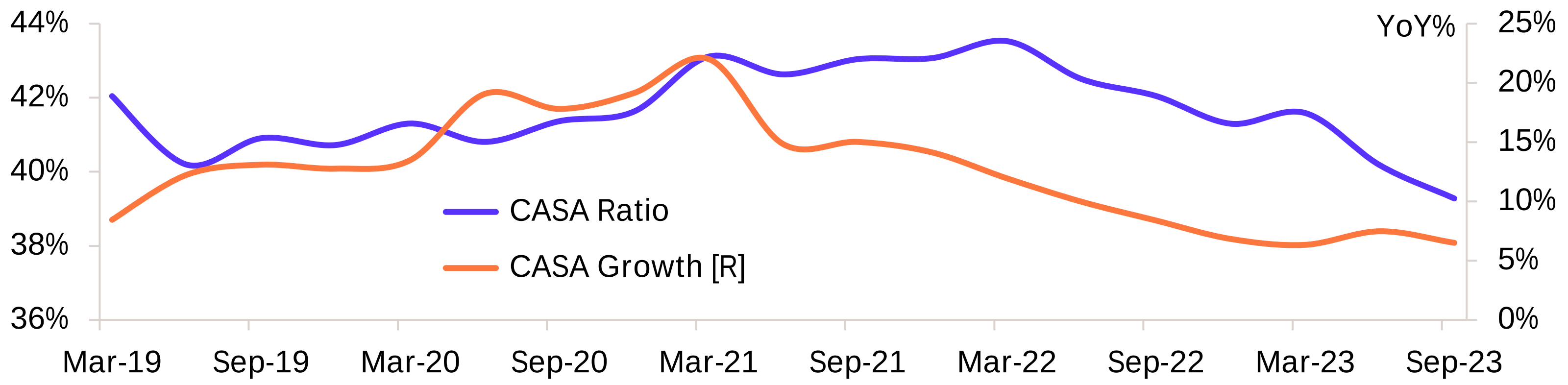
The rise in the term deposit rates is leading to a fall in the spread between lending and deposit rates

The fall in the spread is much sharper in the case of new loans and fresh deposits, while the decline in spread between outstanding loans and deposits is slower, as deposits undergo repricing with a delay after the maturity of old term deposits

Source: RBI, 360 ONE Asset Research   Note: 'Lending Rate – Fresh Loans' is weighted average lending rate for fresh rupee loans, MCLR – Marginal Cost of Funds based Lending Rate, calculated as an average of 8 large banks

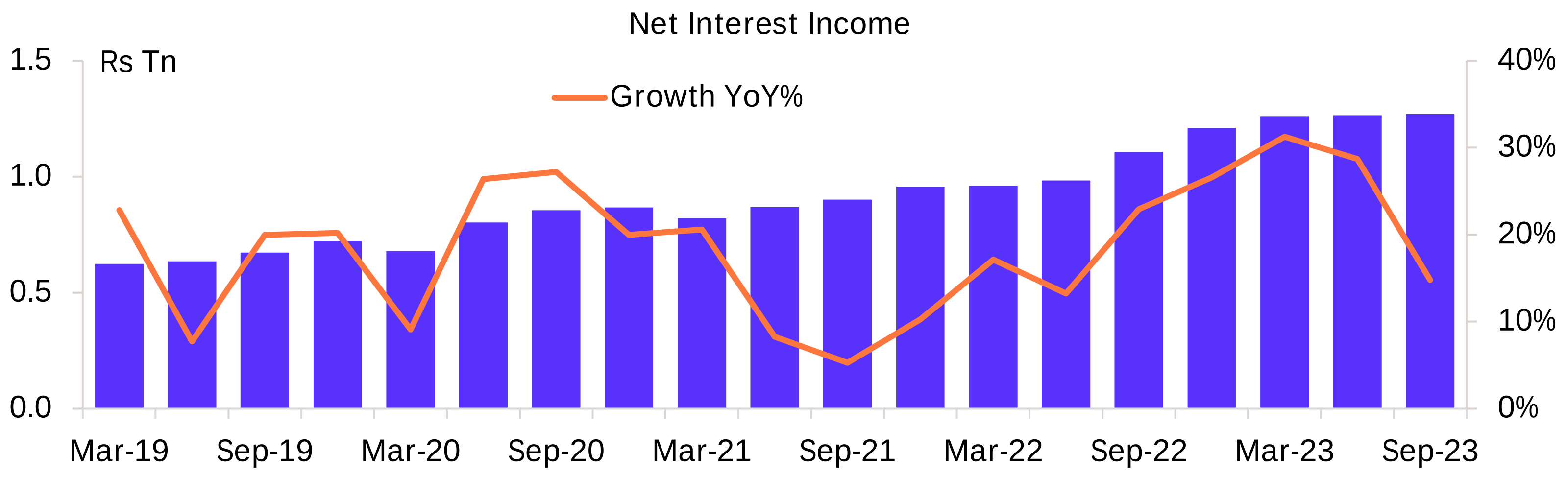
Falling CASA ratio also adds to rising cost of deposits

Growth in net interest income has slowed as the spread between yield on advances and cost of deposits has declined



The CASA ratio of banks is declining because attractive term deposit rates are causing funds to shift from low-yield savings accounts or interest-free current accounts to term deposits

A declining CASA ratio also leads to an increase in the overall cost of deposits, as the share of high-cost term deposits in liabilities increases



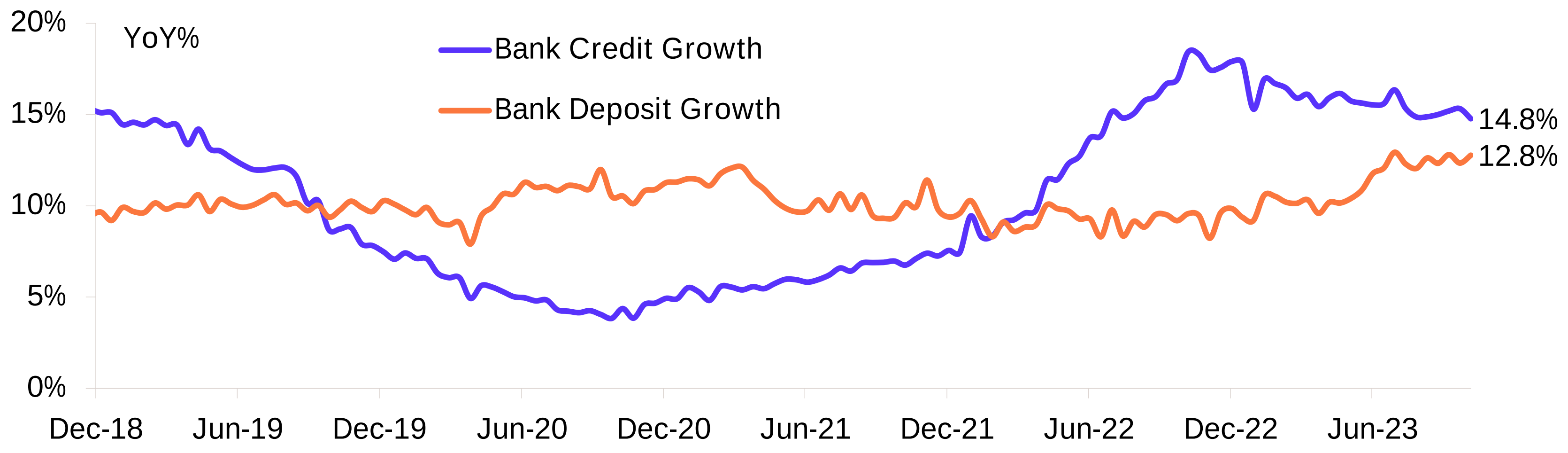
The growth in net interest income has decelerated due to the compression of net interest margins. This is a consequence of the cost of deposits for banks catching up with the increase in yield on advances

Source: Ace Equity, 360 ONE Asset Research

Note: Net interest income and CASA ratio based on a sample of banks

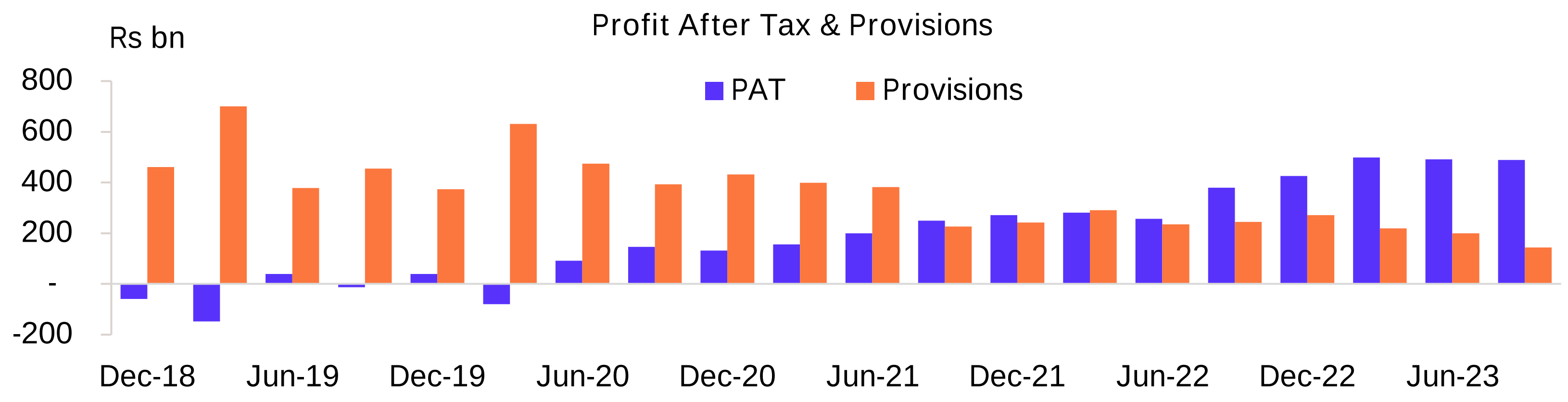
Credit growth remains healthy with recovery in deposit growth

Banks are posting profits near-record levels, driven by robust credit demand and a reduction in provisions



Banking system recording strong double digit credit growth since April 2022

Deposit growth has also recovered in FY24



Banks are reporting near-record profits on account of strong credit growth and a decline in provisions for non-performing assets

High capacity utilization, robust growth momentum, and healthy corporate balance sheets will support the demand for credit. Strong **banks'** balance sheets with a low GNPA (Gross Non-Performing Assets) ratio also bode well for the growth of the banking sector

Source: RBI, 360 ONE Asset Research

Note: Numbers adjusted for merger of a non-bank with a bank. PAT and provisions data based on a sample of 14 banks

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