



May 17, 2023

Portfolio Commentary

Taking stock of market internals

- The market has spent longer in the current consolidation than its historical average
- Despite a lot of pressure from laggard sectors, markets have been resilient.
- More than half of the sectors that make up Nifty are already leading the market.
- As the selling in laggard sectors recedes, a fresh bull market may emerge led by new leading sectors.
- At Sanctum PMS, we continue to rejig portfolios based on our sectoral insights.

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In April, equity markets experienced a broad-based recovery. Headline indices recorded a 4% increase, while broader market indices outperformed them. Additionally, the earnings season commenced with many large companies announcing their earnings for the January-March quarter. The table below provides an overview of the consolidated earnings performance based on the results reported thus far.

Q4FY23 Results Snapshot				
	BSE500		Titans	
	YoY	QoQ	YoY	QoQ
Revenue Growth	13.9%	5.3%	12.4%	2.0%
Revenue Growth (Ex Financials)	10.1%	4.7%	7.3%	0.7%
EBITDA Growth (Ex Financials)	5.6%	14.0%	19.0%	12.3%
Net Profit Growth	13.3%	18.2%	19.0%	9.1%
Net Profit Growth (Ex Financials)	2.0%	31.6%	16.0%	11.4%

Source: Ace Equity, Sanctum Wealth Research

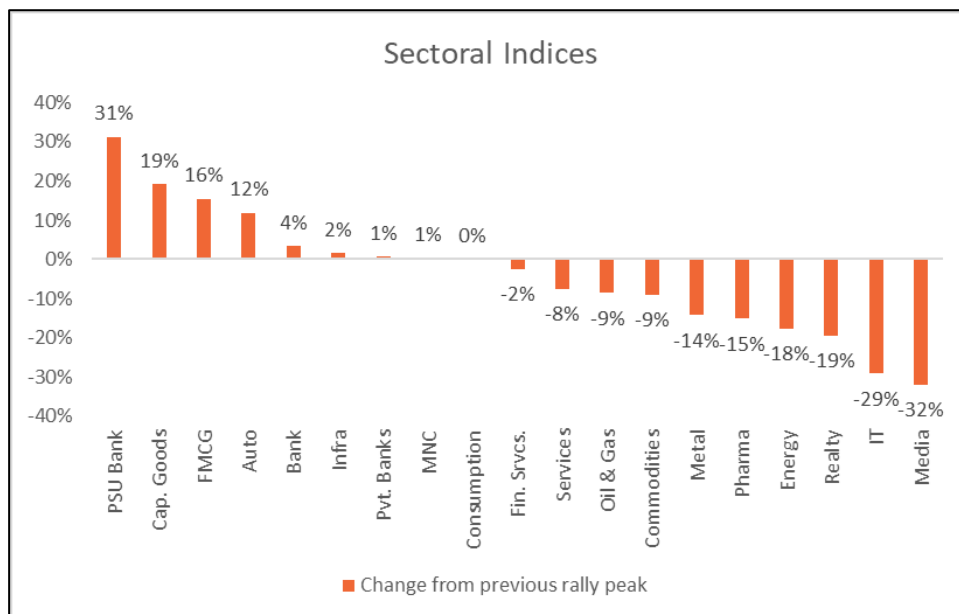
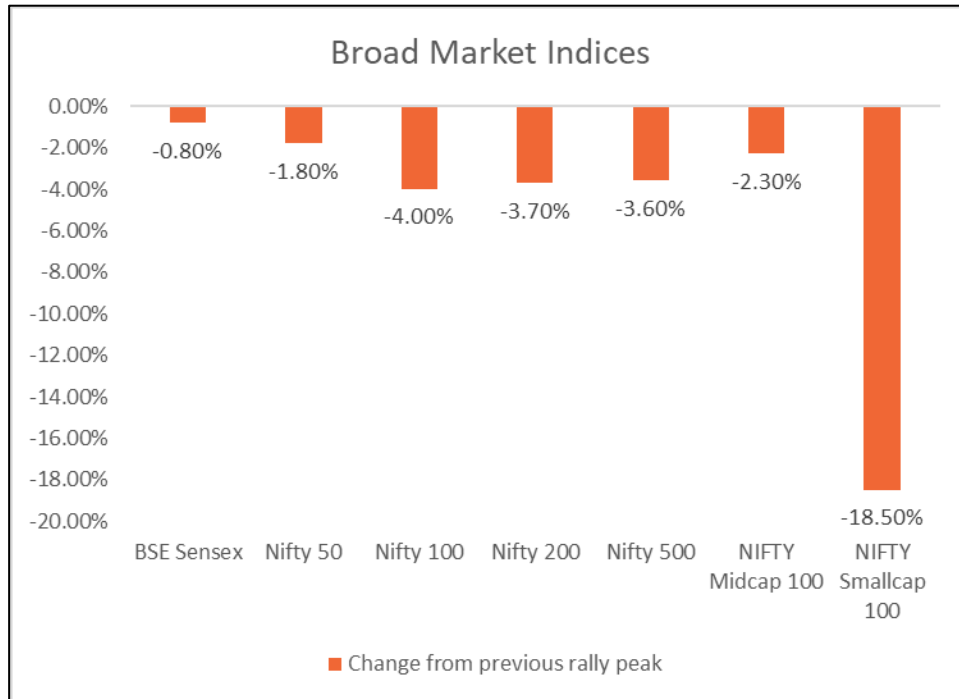
Although topline growth in the quarter was promising, year-on-year margins were under continued pressure. However, for the second consecutive quarter, the quarter-on-quarter margins showed improvement, resulting in QoQ EBITDA growth surpassing revenue growth.

For nearly nineteen months, the market has been trapped in a prolonged consolidation phase, having briefly reached new highs in November 2022, which it couldn't sustain. However, a positive aspect of the current decline is the strong rebound from the previous low, raking the market closer to the previous high.

As mentioned in our earlier note, the structure of a market rally evolves with each consolidation, correction, and bear market. In the 2004-2007 bull run, infrastructure and realty companies were the star performers and market leaders, but in the 2009 recovery, IT and auto companies took on the mantle. Similarly, in the current market, there has been a noticeable shift in market internals compared to six months ago.

In this note, we will discuss the performance of different market components and provide insights into the prospects for broader indices.

Below is a chart showing the performance of different indices from their 2021 highs.



Source: nseindia.com, Sanctum Wealth Research

The charts above illustrate that the broad market indices are still below the previous rally highs, and many sectoral indices are also experiencing negative returns.

Among the seventeen sectors shown, only seven have delivered positive returns from their 2021 peaks. Notably, PSU Banks, Capital Goods, FMCG, and Autos have achieved significant returns of 10% or more, while others have seen marginal single-digit returns.

On the other hand, more than half of the sectors continue to struggle, with many of them experiencing deep declines and remaining well below their 2021 peaks.

Despite the widespread weakness in most sectors, the Nifty, Sensex, and Midcap index have displayed resilience. This can be attributed to the heavy representation of key leading sectors such as Banking, FMCG, and Auto, which collectively form more than half of the Nifty and Sensex indices.

What's pulling the spring?

A closer examination of the laggards reveals that the sectors currently lagging in this consolidation phase are the ones that led the market rally of 2020-2021. The table below illustrates the peak-to-peak performance of these sectors compared to the broad market indices during the 2020-2021 rally.

Index	Peak to Peak Performance	Index	Peak to Peak Performance
Nifty 500	57.3%	Nifty IT	133.7%
Nifty 50	49.7%	Nifty Energy	74.0%
Midcap 100	52.2%	Nifty Commodities	52.6%
Smallcap 100	24.8%	Nifty Realty	49.6%
Nifty Bank	28.3%	Nifty Services	45.5%
Nifty FMCG	26.7%	Nifty Infra	42.6%
Nifty Auto	0.2%	Nifty Pharma	38.5%

Source: nseindia.com, Sanctum Wealth Research

As evident in the table, the sectors currently weighing down the market, namely IT, Energy, Commodities, and Realty, were the ones that delivered impressive returns in 2021. Conversely, the sectors that have been leading the market during the current challenging grind, namely Banks, FMCG, and Autos, underperformed in the previous rally.

Despite the emergence of new leaders, the market has struggled to sustain its recent new highs due to continued selling pressure in the laggard sectors. Historically, bull markets in major indices often commence when the negative contribution from the laggard sectors ceases. During this period, these sectors tend to enter a state of limbo, while the market relies on the performance of leading sectors to reach new highs.

Fortunately, the selling pressure in the major laggard sectors appears to be subsiding as most of the adjustment for high valuations and deteriorating fundamentals has already taken place.

Is the move in leading sectors over?

Given the current state of the market and the stretched returns in some of the leading sectors, concerns about the rally in these sectors going too far and its potential for further outperformance are valid. However, a historical analysis of peak-to-peak performance in different sectors during bull markets from 2000 to 2021 provides some insights.

Peak to Peak Performance	Early 2000 Peak	2008 Peak	Perf.	2009-2010 Peak	Perf.	2015 Peak	Perf.	2018 Peak	Perf.	2021 Peak	Perf.
Nifty 500	1,759	5,564	216.3%	5,212	-6.3%	7,428	42.5%	10,175	37.0%	16,004	57.3%
Nifty 50	1,818	6,357	249.7%	6,338	-0.3%	9,119	43.9%	12,430	36.3%	18,604	49.7%
Midcap 100		9,782	NM	9,854	0.7%	14,237	44.5%	21,840	53.4%	33,243	52.2%
Smallcap 100		6,048	NM	4,620	-23.6%	6,112	32.3%	9,657	58.0%	12,048	24.8%
Nifty Bank	1,247	10,774	764.0%	13,303	23.5%	20,908	57.2%	32,613	56.0%	41,829	28.3%
Nifty FMCG	3,679	6,779	84.2%	9,660	42.5%	22,717	135.2%	33,168	46.0%	42,021	26.7%
Nifty Auto		2,392	NM	4,257	77.9%	9,111	114.0%	12,109	32.9%	12,139	0.2%
Nifty IT	9,550	5,857	-38.7%	7,592	29.6%	12,908	70.0%	16,882	30.8%	39,446	133.7%
Nifty Pharma	1,140	3,519	208.7%	5,173	47.0%	14,020	171.0%	10,786	-23.1%	14,938	38.5%
Nifty Realty		1,878	NM	633	-66.3%	291	-54.0%	375	28.9%	561	49.6%
Nifty Energy	1,274	12,012	843.2%	10,196	-15.1%	10,687	4.8%	16,842	57.6%	29,304	74.0%
Nifty Infra		6,261	NM	3,880	-38.0%	3,524	-9.2%	3,749	6.4%	5,346	42.6%
Nifty Commodities		3,689	NM	3,347	-9.3%	3,239	-3.2%	4,233	30.7%	6,458	52.6%
Nifty Services	4,543	7,588	67.0%	7,617	0.4%	11,917	56.5%	17,743	48.9%	25,823	45.5%

Source: nseindia.com, Sanctum Wealth Research

Looking at the table, it is evident that leading sectors tend to deliver high returns in bull markets. The median return of leading sectors ranges from 1.4 times to 3.7 times the market return, depending on the strength of the bull market. For instance, if the Nifty returns 10%, a relatively weak bull market has historically led to at least a 14% return in leading sectors, while a robust bull market has resulted in a 37% return in leading sectors.

It is worth noting that the bull market in the Nifty has not yet begun, and as is typical in the market's nature, the bull market in leading sectors often starts much earlier than in broader markets. As previously demonstrated, these leading sectors have already generated some returns in the current lackluster market. Based on historical trends, a broader bull market is likely to amplify these returns, suggesting that the current returns in leading sectors are not overly stretched and there is potential for further growth.

The extent of this move will depend on the fundamental factors driving these sectors. Currently, the Banking sector appears to be in a favorable position due to high credit growth, lower provisioning, and improved financial health. If credit growth remains strong, this rally may also sustain, especially considering that many PSU banks and small private sector banks are still trading at low valuations.

The Capital Goods sector is experiencing strong traction driven by significant infrastructure spending by the government and capacity expansion in certain sectors. The sector has also shown robust earnings performance.

As for the Auto sector, despite having faced various challenges such as demonetization, changes in emission norms, increased ownership costs due to GST and insurance norms, COVID-19 disruptions, input price increases, and semiconductor shortages, the sector is now showing signs of improvement. With increasing income levels, middle-class aspirations, and easy access to finance, demand for personal mobility is likely to be strong in the future.

FMCG, although not expected to be the star sector in the next rally, has been leading due to a combination of flight-to-safety, earnings growth, and reasonable valuations in certain segments. It may continue to provide stable returns going forward.

Overall, the leading sectors appear to be riding on improved fundamentals, suggesting that there is still potential for further upside in the rally. Additionally, other sectors may join the bandwagon when a fresh bull market emerges.

Sanctum's Take

In the current environment, where markets have undergone a lengthy consolidation period, there are signs pointing towards the start of a new bull market. The resilience shown by leading sectors and the reduced decline in laggards indicate a potential turnaround. Furthermore, the market internals are displaying encouraging signals, and in the absence of any significant local or global news, the market seems poised to embark on a fresh rally following a textbook pattern.

However, it's worth noting that India will witness a series of state elections this year, followed by the general election next year. While the markets currently anticipate a stable political outcome in the general elections, the results of the state elections could potentially alter the market's perspective. Nonetheless, as the election outcomes lie beyond our control, we choose to focus on the information presented by the market and adjust our portfolios accordingly.

With our understanding of the leading sectors, we have strategically positioned our portfolios by identifying new structural opportunities and increasing exposure to existing names within these sectors. Simultaneously, we have reduced exposure and maintained underweight positions in laggard sectors, safeguarding our portfolios against significant downside risks. We

remain vigilant in monitoring market internals to discern the direction of the market and make necessary adjustments to our portfolios accordingly.

In terms of performance, we have successfully navigated through turbulent times, delivering stable returns. Our positive view on leading sectors, combined with our risk-first approach, allowed us to maintain a cautious stance on overhyped sectors during the 2021 bull run, contributing to our consistent performance.

Here is how our flagship strategies have performed over different time periods.

Portfolio Performance

Performance as on					CAGR			
April 30, 2023	1 Month	3 Month	6 Month	1 Year	2 Year	3 Year	5 Year	Since Inc.*
Sanctum Indian Titans	4.6%	3.0%	-1.7%	2.7%	12.5%	22.0%	10.7%	13.3%
BSE500TR Index	4.6%	2.1%	-1.1%	4.2%	12.3%	25.4%	11.4%	14.5%
* Since Inception Returns are from 18-Nov-16								
Performance as on					CAGR			
April 30, 2023	1 Month	3 Month	6 Month	1 Year	2 Year	3 Year	5 Year	Since Inc.*
Sanctum Indian Olympians	4.8%	2.7%	-2.7%	4.3%	9.4%	17.6%	10.5%	10.8%
Nifty 50TR Index	4.1%	2.4%	0.5%	6.9%	12.4%	23.7%	12.3%	14.7%
* Since Inception Returns are from 16-Sep-16								

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