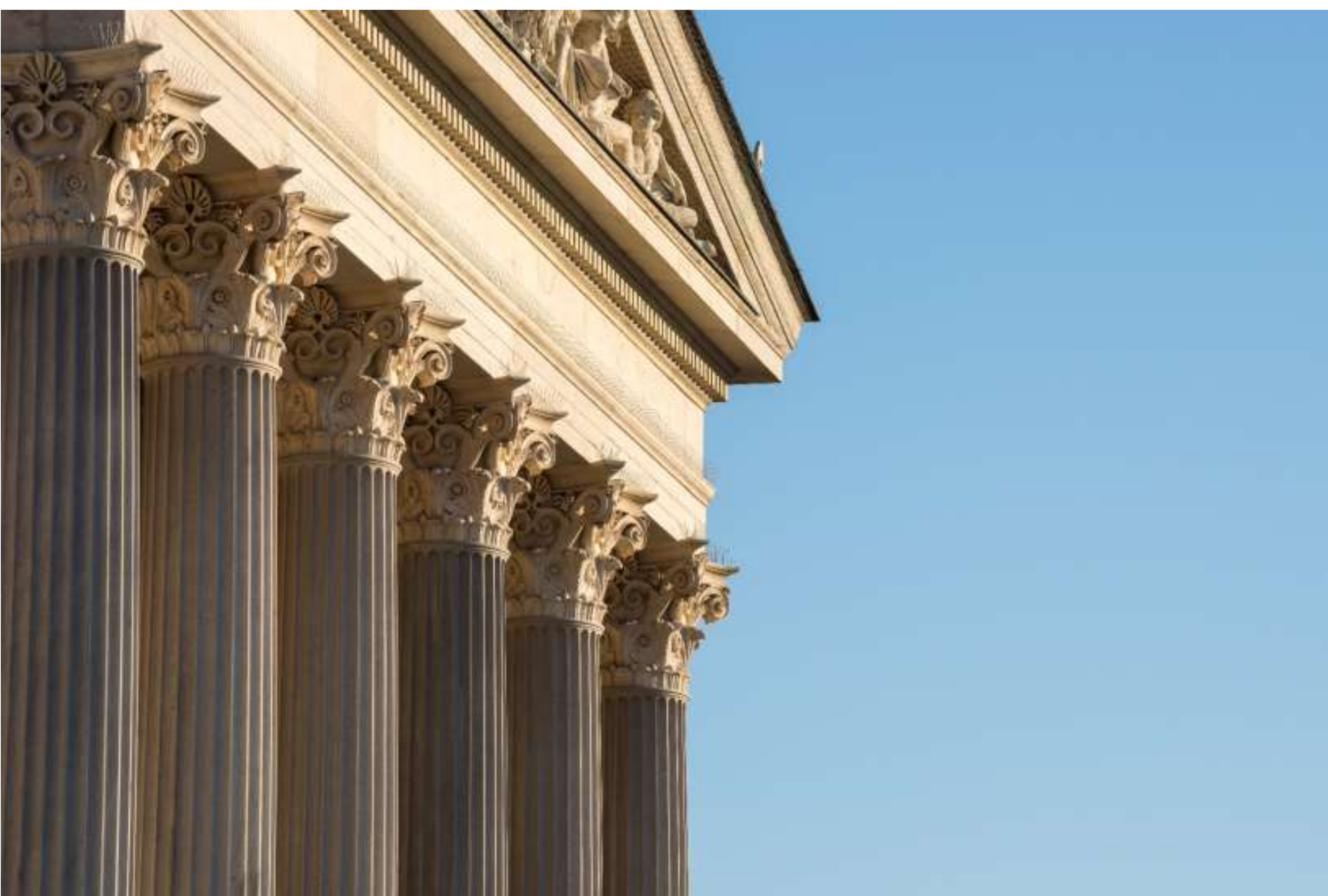
TRU INSIGHTS

May 2025



Contents

From the MD & CEO's desk

"Markets rebounded sharply after the U.S. paused its sweeping tariff hike, but rising India-Pakistan tensions and escalating U.S.-China trade measures remain key overhangs. India's relative resilience, stable macro backdrop, and progress on bilateral trade talks with the U.S. offer support, though geopolitical volatility may drive near-term sentiment."

Dear Investors,

Global equities experienced a sharp sell-off in the first week of April following U.S. President Trump's announcement on April 2nd of reciprocal tariffs ranging from 10% to 50% on all countries. The S&P 500 fell by approximately 14% post-announcement, while the Nifty dropped 7.5%. However, in a surprising policy reversal, President Trump put the proposed tariffs on hold for 90 days.

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This unexpected move triggered a rally in global markets, with the S&P 500 recovering nearly all of its losses, ultimately closing the month marginally down by 0.8%. Indian markets followed suit, with the Nifty rebounding by about 12% from its lows to end the month in positive territory. However, escalating geopolitical tensions between India and Pakistan have introduced new uncertainties for Indian equities.

A baseline 10% tariff is now applied to all U.S. imports, except for those from China, which retaliated with its own counter-tariffs, further escalating the trade war. Currently, imports into US from China are subject to tariffs as high as 145%, while U.S. exports to China face duties up to 125%.

The unpredictable sequence of tariff announcements and countermeasures has shaken global markets and dampened economic momentum. The U.S. GDP for Q1CY25 contracted by 0.3% QoQ on an annualized basis, a stark contrast to the 2.4% growth recorded in Q4CY24. Additionally, inflation, as measured by the GDP price index, surged to 3.7% from 2.3% in the previous quarter. Interestingly, the U.S. labour market remains resilient, with April's non-farm payroll numbers exceeding expectations.

In its latest World Economic Outlook, the IMF revised its global GDP growth projections downwards, citing heightened uncertainty. The IMF now expects growth of 2.8% in CY2025 and 3.0% in CY2026, compared to its previous forecast of 3.3% for both years.

Geopolitical tensions escalated further after the tragic terrorist attack on April 22nd, where 26 tourists were killed near Pahalgam by terrorists. In response, India severed diplomatic ties with Pakistan and suspended the Indus Waters Treaty. Pakistan retaliated by annulling the 1972 Shimla Agreement and cutting all diplomatic engagements with India.

Comments from the U.S. Trade Secretary indicating that trade negotiations with several key partners — including India — are progressing well, offer a silver lining. India is reportedly among the first in line to finalize a trade agreement with the U.S., which bodes well for our markets. However, potential geopolitical flare-ups, both domestically and in Eastern Europe following the U.S.-Ukraine minerals pact, could keep markets on edge.

In this edition of Tru Insights, we provide a comprehensive review of global and domestic macroeconomic trends, an outlook on fixed income markets, and an in-depth feature on "Sector Rotation Strategies in the Indian Context."

We trust that Tru Insights will continue to serve as a valuable resource to enhance your investment decision-making.

Warm Regards,

Dhiraj Relli
MD and CEO – HDFC Securities

Macro Economic Highlights

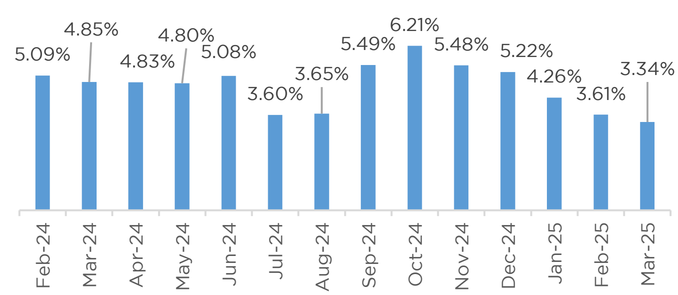
Global Trade Tensions and Policy Shifts Reshape Economic Outlook

Global markets faced heightened volatility in May 2025, driven by escalating trade tensions—particularly between the US and China—and shifting monetary policies. In India, inflation hit a multi-year low, while export momentum, strong industrial activity, and robust fiscal trends supported economic resilience.

Domestic Macro Highlights

Inflation: India's consumer inflation declined to 3.34% in March 2025, its lowest level in nearly six years, down from 3.61% in February. This marked the fifth consecutive month of easing inflation. The deceleration was primarily driven by food inflation, which dropped to 2.69% in March from 3.75% in Feb. Despite modest increases in fuel and housing prices, consumer prices overall fell by 0.26% for the month. With inflation now well below the RBI's 4% target, the monetary policy environment has become increasingly accommodative.

India CPI Inflation



Source: Tradingeconomics, Federal Researve

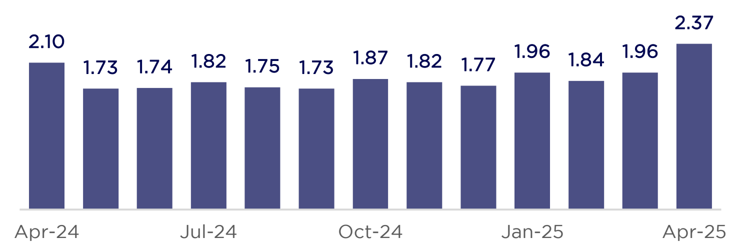
India's Record FY25 Export Surge: India recorded an all-time high of $824.9 billion in exports during FY25, reflecting a 6.01% year-on-year increase. Services exports led the surge, rising 13.6% to $387.5 billion, while non-petroleum merchandise exports grew 6% yoy to $374.1 billion (as against US$341.1 billion in the previous year). March alone saw a strong 18.6% yoy growth in services exports. However, this strength in outbound trade was accompanied by a widening trade deficit, which expanded to $21.54 billion in March 2025 compared to $15.34 billion in March 2024.

India Manufacturing PMI Surges Amidst Price Hikes: India's manufacturing sector showed renewed momentum, with the HSBC India Manufacturing PMI climbing to 58.2 in April—its highest level in ten months compared to 58.1 in March. Export orders rose robustly, marking the second-fastest growth in over 14 years. Production picked up sharply, particularly in the consumer goods segment. Notably, output prices increased at the fastest pace since October 2013, signalling improved pricing power. Employment levels also rose, and over 30% of manufacturers expressed optimism for higher output in the coming year.

GST Collections: GST collections soared to a record ₹2.37 lakh crore in April 2025, reflecting a 12.6% yoy increase from ₹2.10 lakh crore in April 2024.

India's GST Collections rose from Rs. 1.96 lakh crore in Mar-25 to Rs. 2.37 lakh crore in Apr-25

India's GST Collection in Rs. Lakh Crore



Source: Economictimes

RBI Cuts Rates Again, Signals Further Easing Amid Trade Uncertainty: Amid rising global uncertainty, the Reserve Bank of India reduced the repo rate by 25 basis points to 6.00% on April 9. This marked the second consecutive rate cut and was accompanied by a shift in the monetary policy stance from "neutral" to "accommodative." India joined a small group of central banks, including New Zealand, in easing rates following the onset of new US tariffs. The move aims to support domestic growth while inflation remains firmly under control.

RBI Maintains 6.5% Growth Projection for FY26, Cites Global Volatility: The Reserve Bank of India (RBI) projects India's real GDP growth for 2025-26 at 6.5%, consistent with the 2024-25 estimate but a slight downward revision of 20 basis points from February's 6.7% due to increased global volatility, with quarterly projections of 6.5% in Q1, 6.7% in Q2, 6.6% in Q3, and 6.3% in Q4, while maintaining its inflation forecast at 4%, down from the previous 4.2%. The Monetary Policy Committee emphasized the need to support growth amid challenging global conditions, leading to a marginal dip in the 10-year bond yield to 6.32% (as of May 5, 2025).

Global Macro Highlights

Trade & Tariff Implications

US-China Trade War Intensifies, China Excluded from US Tariff Pause: On April 2, the US unveiled a minimum 10% base tariff on all imports, soon escalating to a 145% tariff on Chinese goods following China's retaliatory increase to 125% by mid-April. While most trading partners were granted a 90-day reprieve from reciprocal tariffs, China was notably excluded, reigniting tit-for-tat measures. In a further blow, the US eliminated the de minimis exemption on low-value imports from mainland China and Hong Kong, signalling a hardening stance that may unsettle global trade flows.

Monetary Strategies & Inflationary Pressures

UK Inflation Falls Amid Tariff Uncertainty: In the UK, inflation eased to 2.6% in March from 2.8% in February, driven by declining fuel costs and subdued leisure spending. However, rising clothing and footwear prices and uncertainties around the US tariff regime have clouded the inflation outlook. With inflation hovering above the Bank of England's 2% target, markets are pricing in a high probability of a rate cut at the upcoming May 8 meeting, potentially bringing the base rate down to 4.25%.

ECB's Seventh Rate Cut: The European Central Bank enacted its seventh consecutive rate cut on April 17, lowering the deposit rate by 25 basis points to 2.25%. The move reflects persistent weakness across the Eurozone and aims to cushion the blow from growing trade-related headwinds. The rate now sits at the upper bound of the ECB's 1.75%-2.25% neutral range.

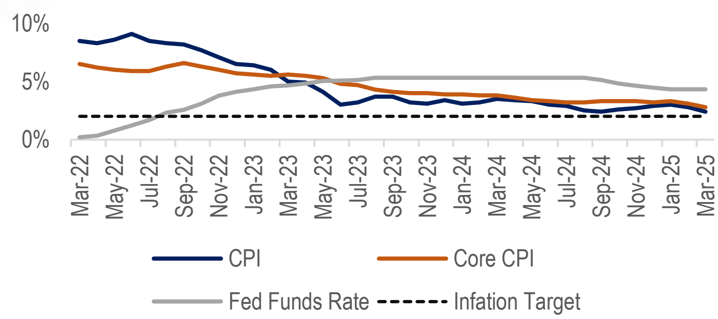
US Inflation and Interest Rates

US inflation measure hits 2.4% in March : The annual US inflation rate declined to 2.4% in March 2025, the lowest in six months, falling from 2.8% in February. Energy prices plunged 2.4% as gasoline prices plummeted by 6.3%. Food prices regained some momentum and registered a moderate 0.4% gain as grocery prices rebounded 0.5% amid lingering egg and dairy price pressures. Looking ahead though, higher tariffs will lead to a renewed inflation impulse in coming quarters, with core CPI inflation likely to end 2025 in the 3.5%-4% range, according to Lazard's Ron Temple.

Strong Jobs Data Shifts Rate Cut Expectations: The US labour market added 177,000 jobs in April, tempering expectations of an imminent Fed rate cut. While President Trump continues to advocate for looser monetary policy, the Federal Reserve remains cautious, citing resilient employment data and persistent inflation concerns. The Fed's decision to hold rates steady is likely to draw further criticism from Trump, though he has recently stated he will not attempt to remove Fed Chair Jerome Powell. The next interest rate decision of the US Fed's FOMC is scheduled for May 7th.

US inflation & Interest Rates

Benchmark interest rates and YoY change in the CPI Inflation



Source: Tradingeconomics, Federal Researve

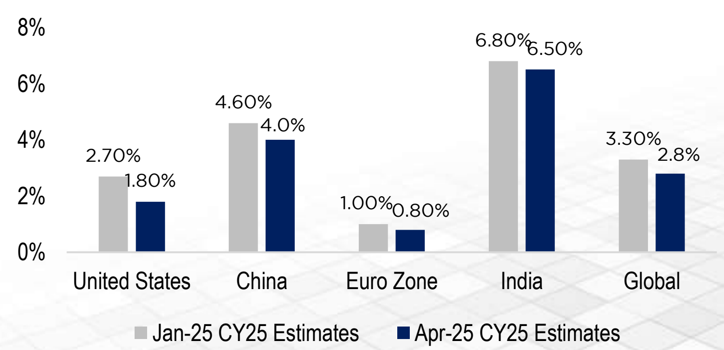
Geopolitical Landscape

India-Pakistan Tensions: Tensions between India and Pakistan have sharply escalated following a deadly attack on tourists in Kashmir, with India accusing Pakistan of involvement, a charge Pakistan denies. Both nuclear-armed nations have downgraded diplomatic ties and expelled each other's citizens. Adding to the severity, India has suspended the Indus Waters Treaty amid the heightened tensions. Cross-border exchanges along the Line of Control have persisted for over ten nights, raising fears of broader escalation.

Global Growth Projections

IMF Lowers Global Growth Forecasts: The International Monetary Fund revised its global GDP growth forecasts downward to 2.8% for CY2025 and 3.0% for CY2026, a notable retreat from the earlier 3.3% projections for both CY25 and CY26. The downgrade reflects rising tariff barriers and heightened financial market volatility. IMF further expects Global headline inflation to decline at a slightly slower pace than what was expected in January. Mounting trade disputes and tightening financial conditions remain key risks to both short- and long-term growth.

World Economic Outlook Growth Projections by IMF



Source: IMF World Economic Outlook update Apr 2025

Equity Market

India Outperforms Amid Global Jitters and Trade Shifts

Indian equities posted strong gains in April 2025 despite global volatility triggered by US tariff announcements and geopolitical tensions. A rebound in global markets, domestic demand recovery, and India's growing role in global supply chains supported the rally. While near-term risks persist, the structural narrative for India remains intact, favoring large-caps and select cyclical sectors.

Equity Outlook

"Amid global trade tensions and heightened volatility, Indian equities remained resilient, backed by strong domestic demand and easing inflation. Policy support and RBI's accommodative stance continue to aid recovery, with large-caps providing relative stability."

Markets Hold Ground Amid Global Crosscurrents

Indian equities continued their upward journey in April, with the Nifty gaining 3.5%—marking the second straight month of gains. But the calm at the surface masked a turbulent start to the month. On April 2nd, global markets were rattled after U.S. President Trump announced reciprocal tariffs on all countries. The initial response was sharp: the S&P 500 plunged nearly 14%, and the Nifty corrected by about 7.5%.

Markets, however, found their footing quickly. A sharp spike in U.S. 10-year bond yields—up over 50 basis points—put pressure on the White House to recalibrate. In a notable shift, the U.S. postponed the implementation of tariffs by 90 days for all countries except China. This move provided a breather to global trade partners and set off a relief rally. By month-end, the S&P 500 had recovered nearly all its losses (closing down just 0.8%), while the Nifty staged a remarkable rebound of ~12% from its lows.

Reading Between the Lines – What's Driving Markets

The global backdrop has become more complex. The U.S. economy showed signs of strain, with Q1CY25 GDP contracting 0.3% (QoQ annualized)—a notable miss versus expectations of 0.4% growth. The IMF, too, trimmed its global growth forecast to 2.8% for 2025, down from 3.3%, citing weaker trade momentum and policy uncertainty.

Meanwhile, the U.S. Fed maintained status quo on rates at its April 7th meeting but flagged a challenging duality—upside risks to inflation on one hand and downside risks to growth and employment on the other, both exacerbated by the unfolding tariff war.

That said, there's been some positive signalling. U.S. Treasury Secretary Scott Bessent mentioned progress in trade negotiations with 17 out of 18 major partners—China being the exception. While there's been little movement on the U.S.-China front so far, the tone from both sides has softened recently, and markets are hoping for formal talks to resume soon.

India – Weathering the Tariff Storm, Though Geopolitics is a Near-Term Risk.

Amid global uncertainty, India continued to demonstrate resilience and relative outperformance. This reflects not just cyclical recovery expectations but a structural re-rating narrative. Two key drivers stand out:

- **Supply Chain Realignment**: Global manufacturers continue to diversify supply chains away from China. India is increasingly seen as a credible alternate hub, aided by policy incentives, improving infrastructure, and geopolitical alignment with the West.
- **Domestic Demand Recovery**: A confluence of supportive fiscal measures and monetary accommodation is gradually reviving domestic consumption, particularly in rural and semi-urban segments. This is crucial in sustaining earnings momentum in FY26

However, geopolitical risk re-emerged in South Asia following a terrorist attack near Pahalgam, which sharply escalated tensions between India and Pakistan. While markets absorbed the initial shock, this remains a short-term overhang that could impact investor risk appetite.

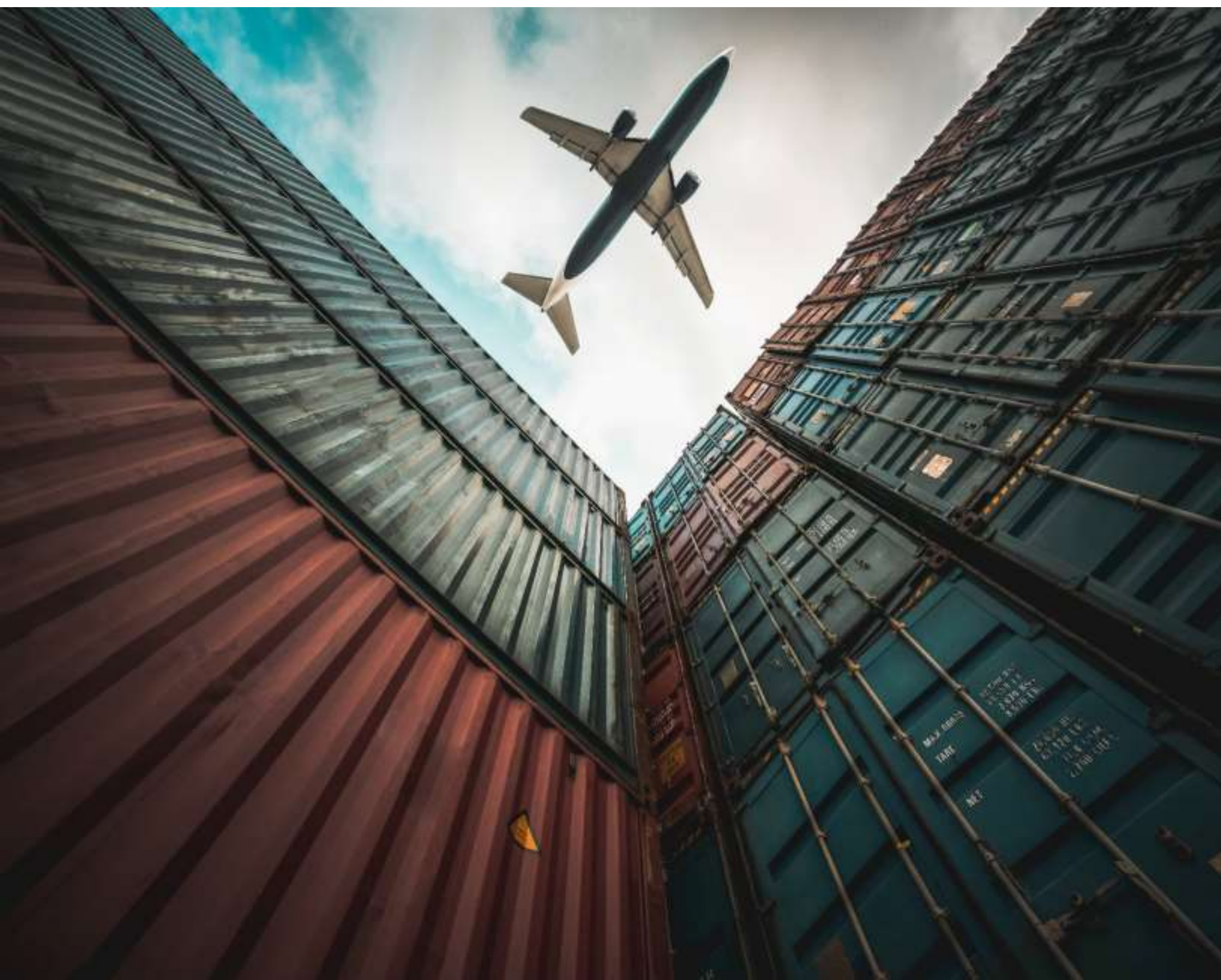
Equity Outlook

What Lies Ahead – Stay Selective, Stay Anchored

Looking forward, two factors will be key for market direction:

- **Progress on trade negotiations**, particularly between the U.S. and key partners like India, could bring clarity and support capital flows.
- **Geopolitical stability** within the region will remain crucial in determining near-term sentiment.

Amid an increasingly polarized global environment, India's macro narrative stands differentiated. However, investors should brace for some possible near-term volatility in case of any escalation in tensions between India and Pakistan. We continue to prefer large-caps given valuation comfort vis-à-vis mid & small caps. From a sectorial perspective we remain positive on large Banks, Real Estate, Industrials, EMS and Consumer Discretionary while we maintain our underweight stance on Consumer Staples, Oil & Gas, Mid-cap IT, Building Materials and Metals.



Debt Market

Rate Cuts and Liquidity Drive Fixed Income Momentum

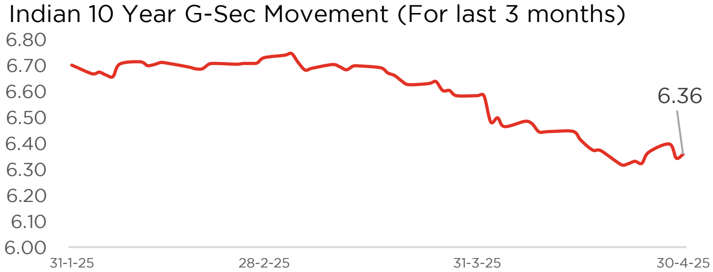
Falling inflation, surplus liquidity, and a dovish RBI stance have driven down yields across India's fixed income market, while global volatility continues to influence bond dynamics. Expectations of further cuts and strong demand for long-duration bonds are likely to sustain positive momentum in the debt market.

Fixed Income Outlook

India’s 10yr G-sec yield fell by 22 bps to 6.36% in Apr’25 from 6.58% in Mar’25. The decline in yield was led by banking system liquidity turning surplus and RBI’s repo rate cut coupled with dovish monetary policy stance. RBI’s Monetary Policy Committee (MPC) cut repo rate by 25 bps to 6.0% in Apr’25 unanimously. It also changed the monetary policy stance to ‘accommodative’ from ‘neutral’. RBI has projected FY26 GDP growth at 6.5% (down from 6.7% in Feb’25) and CPI inflation at 4.0% (down from 4.2% in Feb’25). Slower growth and moderating inflation will allow RBI to deliver further rate cuts, maintain dovish monetary policy stance, and keep adequate liquidity surplus.

India’s 10-Year G-Sec Yield Fell by 22 bps to 6.36% in April 2025

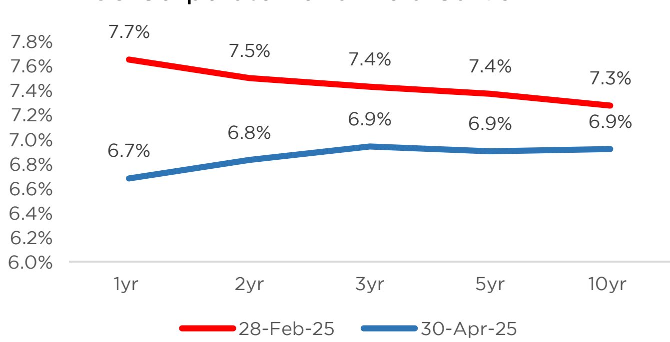
Indian 10 Year G-Sec Movement (For last 3 months)



Source: CCIL

Corporate bond yield curve has seen a notable shift recently with the yield curve steepening supported by RBI’s repo rate cut and large liquidity infusion measures.

AAA PSU Corporate Bond Yield Curve

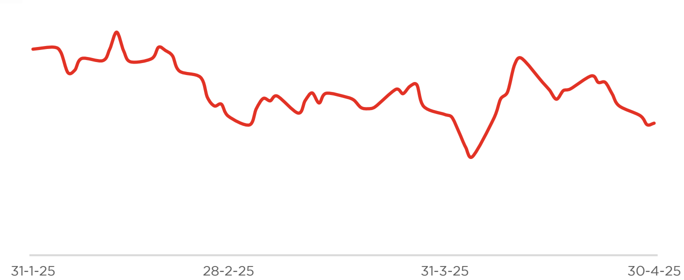


Source: Bloomberg

US 10yr yield fell by 4 bps to 4.17% in Apr’25 from 4.21% in Mar’25 but remained highly volatile during the month led by concerns on global trade tariffs. From the lows of around 4% at the start of the month, the yield rose to a high of 4.5% during the month before moderating to ~4.2% towards month end.

US Yields fell by 4bps to 4.17% in April 2025

US 10 Year G-Sec Movement (For Last 3 Months)

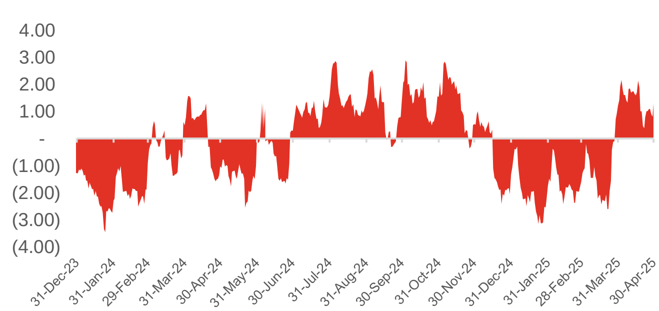


Source: Investing.com

India’s banking system liquidity turned into large surplus during Apr’25 because of OMO purchases conducted by RBI and increase in government expenditure. The average liquidity surplus during Apr’25 was Rs 1.4 lakh cr vs. avg. deficit of Rs 1.2 lakh cr in Mar’25. RBI conducted OMO purchase worth Rs 1.2 lakh cr in Apr’25 and further announced Rs 1.25 lakh cr OMOs to be conducted in May’25. RBI’s annual dividend transfer for FY25 to government (expected in the range of Rs 2.5-3 lakh cr, as per market) is expected to further improve liquidity conditions in coming months.

RBI's Measures Finally Easing Liquidity Crunch

India’s banking system liquidity (Rs Lakh cr)



Source: RBI

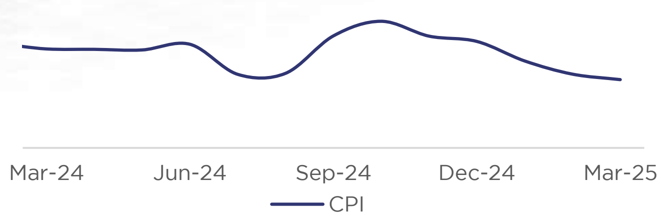
India’s CPI inflation moderated to 3.3% YoY in Mar’25 vs. 3.6% in Feb’25 on the back of sequential decline in food prices. This was the lowest inflation reading since Aug 2019.

RBI is expected to deliver two more rate cuts in 2025 (next cut likely in Jun 2025) with the terminal repo rate expected at 5.5%. The sub-4% CPI inflation projections for next three quarters provide ample space for the RBI to cut rates even below 5.5%, if global trade tensions continue to escalate.

Fixed Income Outlook

India's Inflation Rate Eases in Mar 2025 Due to Drop in Food Prices

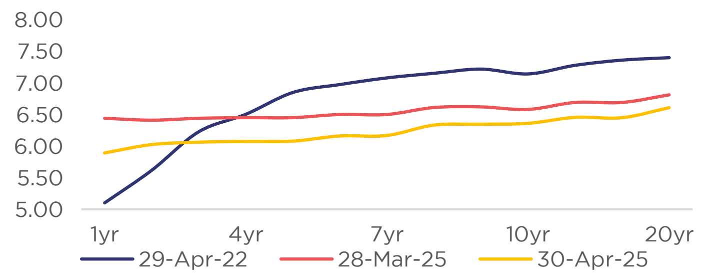
CPI Inflation YoY%



Source: Investing.com

G-Sec Yield Curve continues to remain flat

G-Sec Yield Curve



Source: Bloomberg

With expected banking system liquidity surplus in the near to medium term, the AAA corporate bond yield curve is likely to fall and steepen further. Long duration G-Secs may continue to benefit from decline in yields driven by interest rate cuts, RBI's OMO purchases and favourable demand-supply dynamics.

Long-duration G-secs are well-positioned to benefit from an anticipated decline in yields, supported by rate cuts, OMO purchases, and favorable demand-supply dynamics.

Looking ahead, various factors—including global monetary policy decisions, geopolitical developments, commodity prices, currency fluctuations, bond demand-supply scenarios, and domestic growth-inflation dynamics will play crucial roles in shaping the fixed income landscape.

In Conversation with Sapna Punjabi - VP, Investment Strategy

Q: What is the approach you take while creating bespoke portfolios for your Ultra HNI clients?

A: We don't subscribe to one-size-fits-all solutions. Each Ultra HNI client comes with a distinct risk profile, investment horizon, and financial ambition, and we take time to understanding these nuances in depth before designing their portfolio. Our core strategy is rooted in strategic asset allocation - akin to crafting a balanced diet for wealth. Each asset class – equity, debt, real assets, and alternatives – serves a distinct role, whether it's growth or stability. This disciplined mix helps portfolios remain resilient across market cycles. As Harry Markowitz once said, "Asset allocation is the only free lunch in investing." It's the most effective way to reduce portfolio risk without necessarily compromising on returns.

Q: Let's talk equities—how are you positioning yourselves and what are you advising clients who want to take fresh exposure to Indian equities?

A: The correction in Indian equities from all-time highs in September 2024 must be viewed as a constructive reset. The volatility related to Trump's tariff policies clearly jolted global risk assets, including Indian equities. That said, our markets have demonstrated resilience and we've seen a smart recovery post the tariff rollback. From a valuation standpoint, large caps present a compelling entry point. These businesses boast strong fundamentals and consistent earnings, forming the core of our current equity allocation. At the same time, we're uncovering bottom-up opportunities in the SMID segment, where price corrections have unlocked attractive value. Given near-term volatility, we advise a staggered investment approach. In the long run however, India's structural growth narrative remains intact, bolstered by ongoing fiscal and monetary support.

Q: Ultra HNIs are known to prefer higher exposure to risk assets and tend to shy away from debt. What's your current stance on fixed income?

A: While fixed income has traditionally been seen as defensive, we're leveraging it strategically. Over the past year, we've been overweight long-duration bonds, anticipating a dovish pivot in interest rates. With inflation softening and global growth moderating, central banks are easing their stance. The RBI too has already cut rates twice with more expected. In this environment, longer-duration bonds stand to gain meaningfully, offering potential for both income and capital gains. Today, in addition to providing stability, fixed income is a growth lever in well-balanced portfolios.

Q: How important is global diversification in portfolios?

A: Global diversification is a key element in a well-diversified portfolio, particularly for Ultra HNIs with global lifestyles and legacy considerations. It spreads investment risk across economies and currencies, not just sectors or asset classes. No country is immune to macro or regulatory shocks. By diversifying globally, we protect the portfolio from being overexposed to a single market's downside. It also opens up access to world-class businesses and innovation – from U.S. tech to European luxury and Asian manufacturing. Exposure to global assets can be achieved through Indian mutual funds investing abroad, or directly through the LRS route. For clients with the desired risk appetite, we generally recommend a 10% allocation to global securities.

Q: We've seen a mind-blowing rally in commodities like gold and silver. Do you think they merit investment at current levels?

A: Commodities, particularly gold and silver, are strategic diversifiers. Gold continues to attract strong central bank buying, especially from countries looking to reduce their dollar dependence. Combined with geopolitical tensions and macro uncertainty, gold remains an effective hedge against volatility and currency risk. Silver benefits from both monetary appeal and industrial demand, especially in sectors like solar and EVs. The current gold-silver ratio at over 100 (median being ~70) is an indicator that silver could see a catch-up going forward. In short, we view gold as a long-term stabilizer, and silver as a tactical growth asset - both playing unique roles in the portfolio construct.

Q: Any closing thoughts?

A: In today's dynamic environment, investment strategy must combine discipline with agility. The focus is to blend global macro understanding with deep client insights to deliver portfolios that are not just performance-driven, but purpose-built. Whether it's asset allocation, tactical positioning or global exposure, our goal is to help clients achieve their financial ambitions with clarity and confidence.

Deep Dive

Timing the Turn: Decoding Sector Rotation

Understanding "Sector rotation" is vital for potentially generating better returns than the market by strategically investing in different sectors as the economic cycle evolves. This approach recognizes that various industries respond uniquely to different economic phases, with some thriving during expansions while others perform better in slowdowns. This analysis examines the historical trends within the Indian market to provide valuable context for making informed decisions about sector allocation.

Timing the Turn: Decoding Sector Rotation

Executive Summary:

Sector allocation is a big driver of alpha and sometimes can be more important than stock picking itself. Sector performance rotates with the business cycle, as each sector responds differently to economic shifts. Therefore, insights into which sector has performed well historically can be a great input into decision making. In India, where macro-economic shifts are often policy-driven and structurally influenced, sector rotation presents unique alpha opportunities. Sector rotation is rooted in the idea that economic cycles impact industries differently and this cyclical alignment forms the bedrock of rotation strategies. Globally, sector rotation is a key strategy for active fund managers.

This note delves into the core concepts of sector rotation, explores historical trends from an Indian market perspective, which could be useful for decision making.

Why is Sector Rotation Important?

- **Economic Cyclicality**: Not all sectors perform the same during different economic cycles. For instance, consumer staples tend to do well during slowdowns, while cyclical sectors like industrials and materials rally during economic expansions.
- **Alpha Generation**: Identifying and capitalizing on sectoral shifts can help investors generate excess returns over benchmark indices.
- **Risk Management**: Diversifying across sectors that perform well in varying macro scenarios can cushion the downside during market corrections.

Key Drivers of Sector Rotation:

Several macro and micro factors influence sector leadership:

- **Interest Rates**: Lower rates favour rate-sensitive sectors like banks and real estate.
- **Inflation**: Commodities benefit during inflationary spikes.
- **Fiscal / Capex Push**: Capital goods and infrastructure respond positively.
- **Global Trends**: Export-oriented sectors like IT and Pharma depend on external demand.
- **Earnings Revisions**: Upgrades signal sector momentum, while downgrades signal weakness.
- **Valuations**: Sectors trading below their long-term averages often signal mean-reversion opportunities. Identifying undervalued sectors helps investors position ahead of cyclical upturns and avoid overheated segments.

Historical Sector Leadership Trends in India: No one sector leads forever...

Sector leadership in equity markets refers to the dominance of specific industry sectors in driving market returns over a period. In India, sector leadership has varied widely over the decades and recognizing these patterns is crucial for tactical investors.

The below table shows the historical fiscal year performance of all the key sectors over the last 18 years (FY2008-25), sorted by bull phase, consolidation phase and bear phase:

Fiscal Year		Nifty 500 TRI	Defensives: FMCG	Healthcare	IT	Early Cyclicals: Cons. Durables	Auto	Banks	Fin. Services	Chemicals	Media	Late Cyclicals: Infrastructure	Metals	Oil & Gas	Realty
2010	Bull Phase (>+15%)	90%	42%	93%	153%	167%	139%	129%	124%	125%	122%	44%	184%	52%	114%
2021		78%	28%	66%	103%	74%	108%	74%	69%	89%	49%	73%	151%	70%	90%
2024		40%	18%	58%	22%	35%	75%	16%	16%	11%	6%	64%	50%	60%	133%
2015		35%	10%	69%	30%	57%	49%	43%	43%	62%	22%	24%	-8%	7%	14%
2017		26%	19%	-3%	-5%	32%	22%	33%	33%	50%	37%	22%	62%	44%	37%
2008		23%	23%	7%	-28%	8%	-5%	25%	33%	17%	1%	37%	69%	53%	38%
2022		22%	4%	16%	40%	27%	7%	9%	9%	52%	54%	23%	62%	28%	39%
2014		19%	18%	26%	29%	3%	37%	12%	11%	8%	10%	18%	13%	13%	-16%
2018	Consolidation Phase (-5% to +15%)	13%	11%	-16%	17%	36%	10%	13%	17%	33%	4%	7%	13%	11%	37%
2019		10%	16%	10%	25%	12%	-23%	25%	23%	-1%	-24%	-4%	-13%	12%	-8%
2011		8%	26%	13%	22%	33%	20%	24%	24%	15%	-14%	-10%	-12%	8%	-27%
2013		6%	34%	16%	11%	9%	0%	11%	14%	11%	32%	-12%	-27%	1%	-6%
2025		6%	-1%	13%	6%	10%	-1%	9%	19%	12%	-18%	1%	10%	-8%	-5%
2023		-1%	27%	-10%	-21%	-11%	16%	12%	5%	-6%	-29%	1%	-14%	-9%	-16%
2016	Bear Phase (<-5%)	-7%	-1%	-13%	-6%	7%	-6%	-11%	-13%	0%	6%	-22%	-18%	1%	-28%
2012		-8%	24%	7%	-9%	13%	9%	-13%	-10%	4%	-14%	-18%	-29%	-14%	-24%
2020		-27%	-10%	-17%	-18%	-21%	-43%	-37%	-26%	-4%	-58%	-26%	-48%	-31%	-35%
2009		-39%	-12%	-25%	-37%	-58%	-29%	-38%	-42%	-45%	-60%	-44%	-54%	-27%	-81%

Source: *NSE indices data. Note: i) Fiscal year returns provided above; ii) Cell colours signify the highest to lowest returns in that period (blue to red).*

Ranking Analysis:

To identify consistent outperformers across different market environments, we conduct a ranking analysis, where sectors are assigned, ranks based on their relative performance during distinct market phases. Each sector is ranked from best to worst in terms of returns during these phases, and a cumulative rank is calculated. By analyzing ranks rather than just raw returns, the method reduces volatility bias and offers a comparative lens to assess sector resilience and momentum over time.

Snapshot Table of our Ranking Analysis Framework: Sector Ranks have been given based on FY Returns (%); Rank “1” denotes best performing sector while Rank “13” indicates worst performing sector.

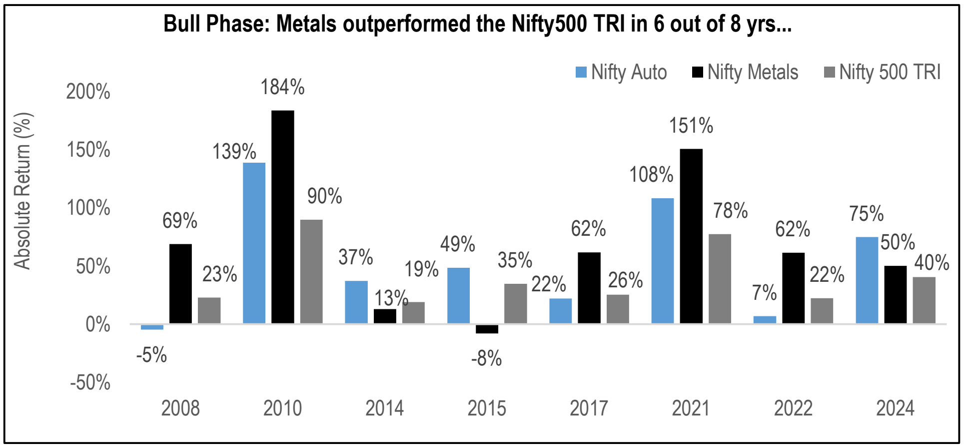
Fiscal Year		Defensives: FMCG	Healthcare	IT	Early Cyclicals: Cons. Durables	Auto	Banks	Fin. Services	Chemicals	Media	Late Cyclicals: Infrastructure	Metals	Oil & Gas	Realty
2010	Bull Phase (>+15%)	13	10	3	2	4	5	7	6	8	12	1	11	9
2021		13	11	3	7	2	6	10	5	12	8	1	9	4
2024		9	5	8	7	2	11	10	12	13	3	6	4	1
2015		11	1	7	3	4	6	5	2	9	8	13	12	10
2017		11	12	13	8	9	6	7	2	5	10	1	3	4
2008		7	10	13	9	12	6	5	8	11	4	1	2	3
2022		13	9	4	7	12	10	11	3	2	8	1	6	5
2014		5	3	2	12	1	8	9	11	10	4	6	7	13
2018	Consolidation Phase (-5% to +15%)	9	13	4	2	10	7	5	3	12	11	6	8	1
2019		4	7	2	6	12	1	3	8	13	9	11	5	10
2011		2	8	5	1	6	3	4	7	12	10	11	9	13
2013		1	3	6	8	10	5	4	7	2	12	13	9	11
2025		10	2	7	4	9	6	1	3	13	8	5	12	11
2023		1	8	12	9	2	3	4	6	13	5	10	7	11
2016	Bear Phase (<-5%)	5	9	7	1	6	8	10	4	2	12	11	3	13
2012		1	4	6	2	3	8	7	5	9	11	13	10	12
2020		2	3	4	5	11	10	6	1	13	7	12	8	9
2009		1	2	5	11	4	6	7	9	12	8	10	3	13
Cumulative Ranks		**FMCG**	**Healthcare**	**IT**	**Cons. Durables**	**Auto**	**Banks**	**Fin. Services**	**Chemicals**	**Media**	**Infrastructure**	**Metals**	**Oil & Gas**	**Realty**
Bull Phase		82	61	53	55	46	58	64	49	70	57	30	54	49
Bear Phase		9	18	22	19	24	32	30	19	36	38	46	24	47
Consolidation Phase		27	41	36	30	49	25	21	34	65	55	56	50	57

Source: *NSE indices data.*

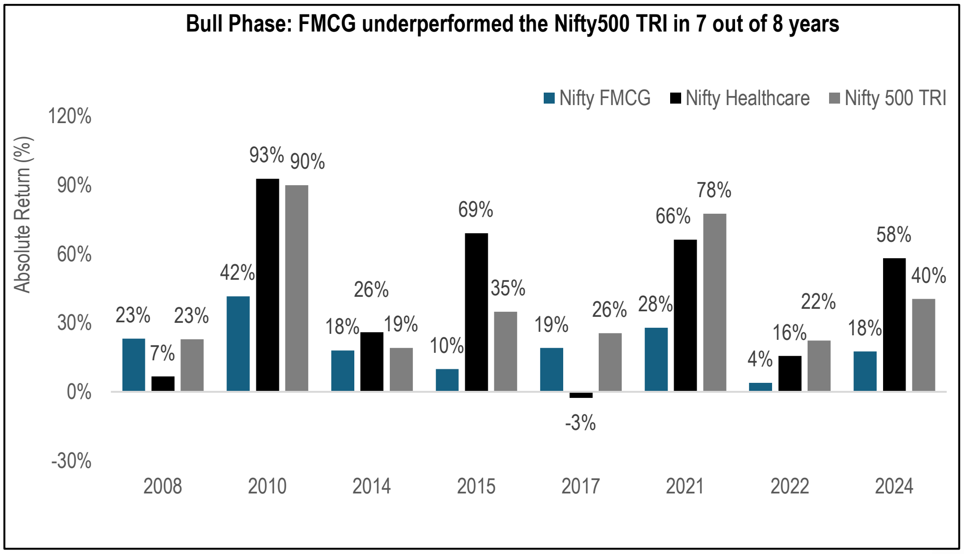
Our analysis indicates that:

- **Bull Phase:** Metals perform the best during the bull years (ranking #1 in 5 out of 8 years), while FMCG is the worst performer.
- **Bear Phase:** FMCG performs the best (ranking among the top-2 in 3 out 4 bear periods), while Metals and Realty tend to be the worst performing sectors (both ranked in bottom-3 in 3 out of 4 bear years).
- **Consolidation Phase:** BFSI and FMCG sectors perform the best, while cyclicals like Infrastructure, Realty and Metals deliver the worst returns.

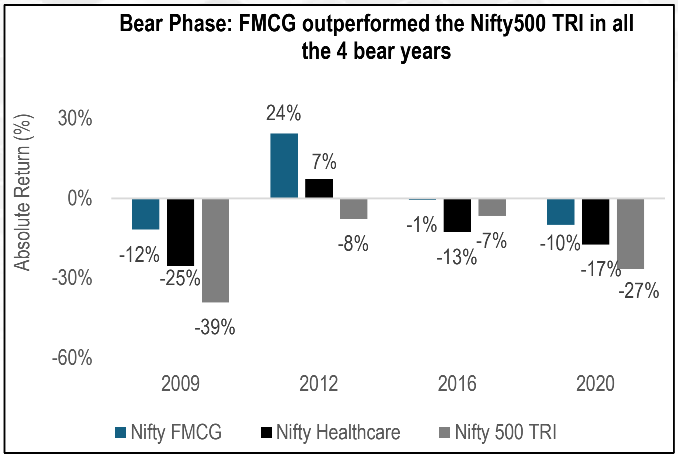
Economic Cycle	Top Quartile Sectors	Bottom Quartile Sectors
Bull Phase (>+15%)	Metals, Auto, Realty	FMCG, Healthcare, Financial Services
Consolidation Phase (-5% to +15%)	Banks, Financial Services, FMCG	Media, Realty, Metals
Bear Phase (<-5%)	FMCG, Healthcare	Metals, Realty

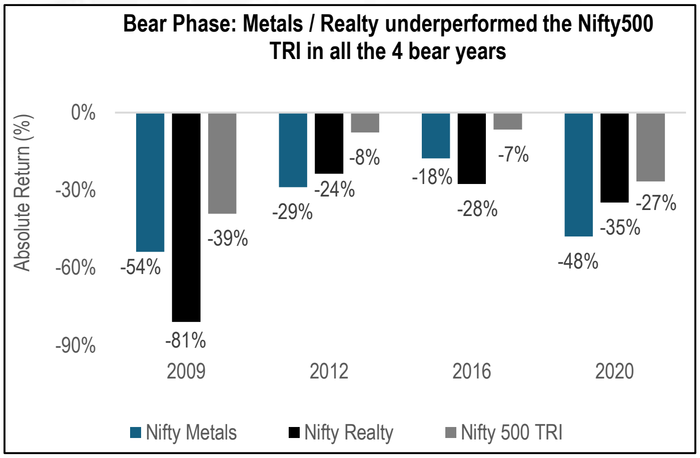


Source: NSE indices data.



Source: NSE indices data.





Source: *NSE indices data.*

Sector upcycles and downcycles are a multi-year phenomena – making sector selection even more critical….

Sector picking is a cornerstone of successful long-term investing, given that sectors often move through multi-year upcycles and downcycles. For instance, during the 2019-21 period, the Indian IT sector benefitted from an accelerated global digital transformation, leading to an earnings CAGR of >10% and a sharp re-rating of sectoral valuations, the Nifty IT Index's 12-month forward PE multiple expanded from ~19x pre-COVID to over 30x.

Industry tailwinds typically span multiple years, leading to significant P/E re-rating. However, more often than not, investors exit the sector after just 12-months of strong outperformance.

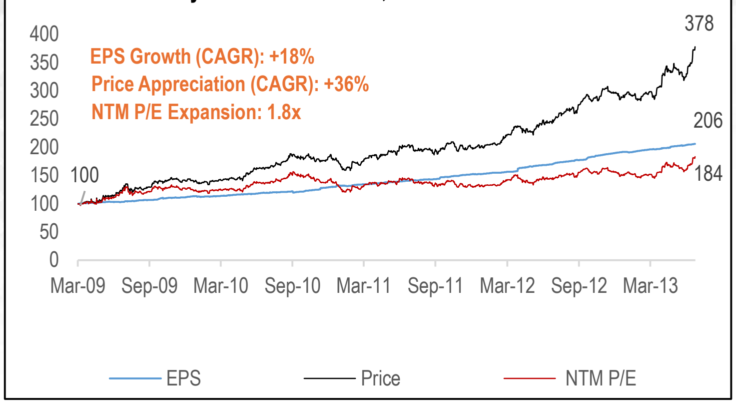
Historical Examples of Indian Sector Upcycles and Downcycles:

Upcycles are typically accompanied by earnings momentum and P/E re-rating, offering strong capital appreciation. Similarly, downcycles are characterized by earnings compression and valuation de-rating, making capital preservation critical. We illustrate this by showing performance of both defensive (FMCG / IT) and cyclical sectors (Infra / Metals) during their respective up/down cycles.

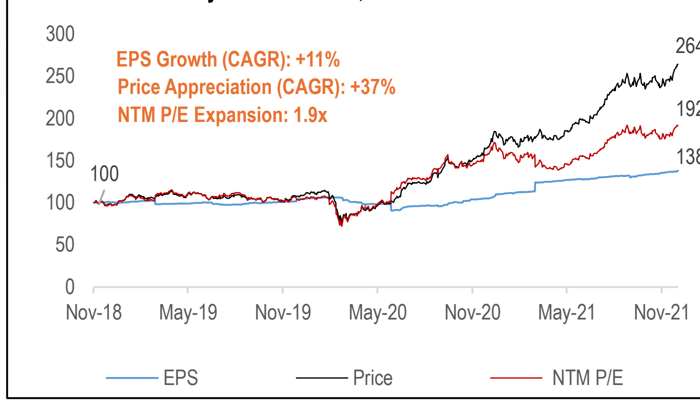
Sector	Period	No. of Months	Cycle Type	PE Expansion / Contraction	EPS CAGR Growth (%)	Price CAGR Returns (%)	Alpha vs. Nifty500 TRI
FMCG	Apr'09 – Jul'13	52	Upcycle	1.8x	18%	36%	17%
IT	Dec'18 – Dec'21	37	Upcycle	1.9x	11%	37%	18%
Infrastructure	Jun'09 – Aug'13	51	Downcycle	-43%	-3%	-15%	-19%
Metals	Jan'18 – Mar'20	27	Downcycle	-53%	-6%	-33%	-20%

Source: *Bloomberg*

Nifty FMCG Index: Price, EPS and NTM P/E

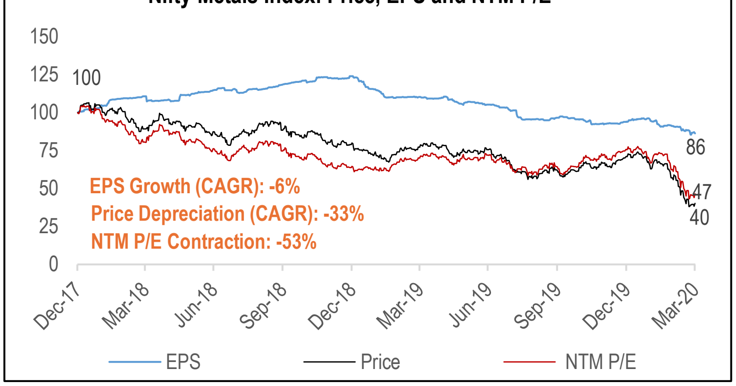


Nifty IT Index: Price, EPS and NTM P/E

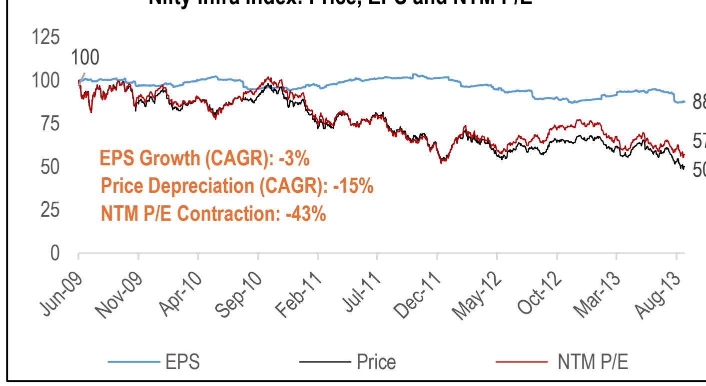


Source: *Bloomberg.*

Nifty Metals Index: Price, EPS and NTM P/E



Nifty Infra Index: Price, EPS and NTM P/E



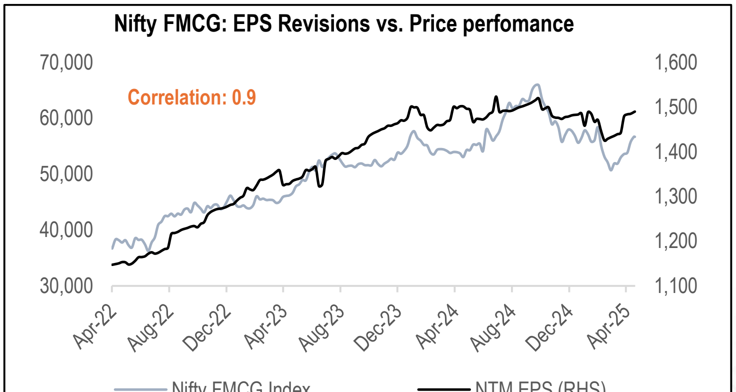
Source: *Bloomberg.*

Key Tools and Indicators to Identify Sector Cycles:

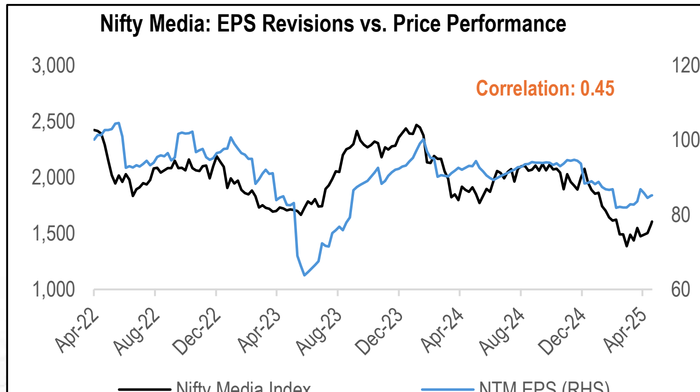
Sector rotation strategies rely on identifying the relative performance of different sectors across phases of the economic cycle, aiming to allocate capital to sectors poised to outperform. While there are a myriad of indicators available to track sector leadership, we focus on some of the most relevant tools that offer clarity and predictive strength.

- **Earnings Revisions –** Market's Forward Indicator: Earnings upgrades and downgrades serve as powerful indicators of market sentiment and corporate performance expectations. When analysts revise earnings estimates upward, it often reflects improving fundamentals, stronger demand, or operational efficiencies, signalling potential upside in stock prices. Conversely, a wave of downgrades can indicate macro headwinds, industry-specific challenges, or company-level concerns. The below charts, provide further evidence of strong positive correlation between price performance and earnings revisions.

Nifty FMCG: EPS Revisions vs. Price perfomance

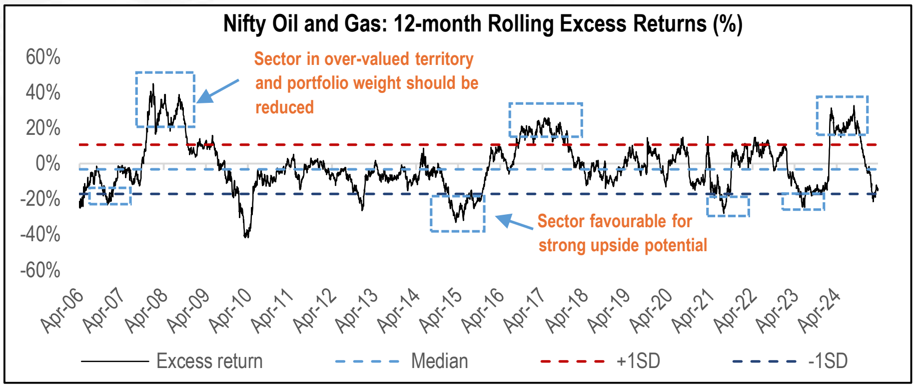


Nifty Media: EPS Revisions vs. Price Performance



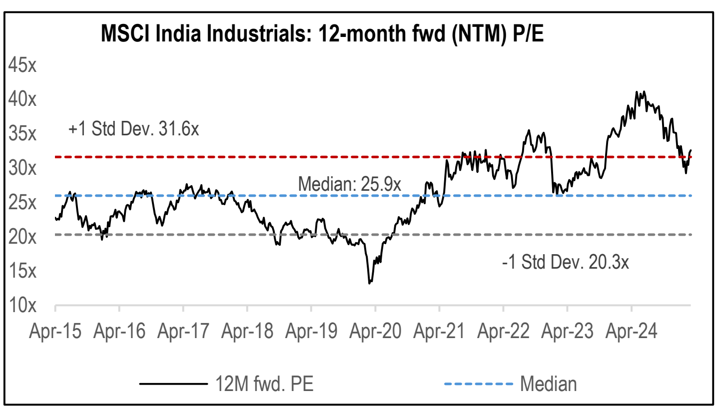
Source: *Bloomberg. Data Period: Apr'22 to Apr'25*

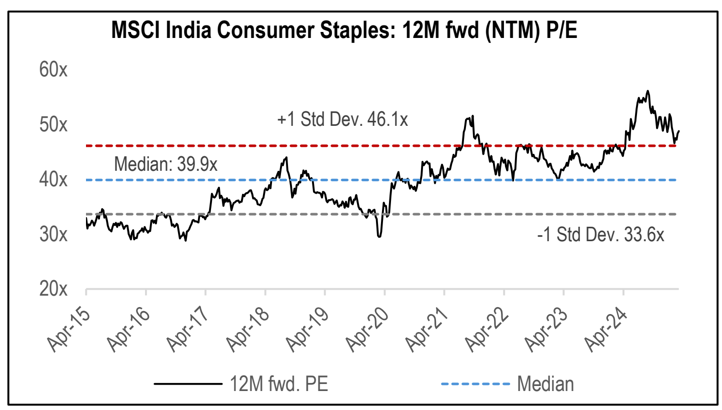
- **Relative Strength – Excess Returns:** It is a pivotal indicator in sector rotation strategies as it helps identify sectors that are outperforming the broader market or a benchmark index over a specified period. By measuring the price performance of a sector relative to a baseline, such as Nifty500, investors can detect emerging leadership and momentum. A sector exhibiting consistently positive excess returns signals growing investor confidence, improving fundamentals, or favourable macro-economic tailwinds, making it a candidate for portfolio overweight. In contrast, sectors with declining relative strength may indicate weakening fundamentals or rotation of capital into better-performing segments.



__Source:__ NSE Indices Data. Data Period: Apr'06 to Mar'25.

- **Valuations:** It plays a critical role in sector rotation, offering a quantitative lens to identify overvalued / undervalued sectors. While mean reversion is a statistically significant concept and a powerful tool to predict cyclical shifts, it is equally important to factor in the presence of cyclical tailwinds. These tailwinds can justify a sector trading well above its historical averages for extended periods. For instance, the "Industrials Sector" moved from -1 Std. Dev below their long-term P/E median to +2 Std. Dev above their long-term averages driven by a strong capex cycle / policy-driven upswing (Apr'20 to Mar'25; refer chart below). Ignoring such cyclical dynamics may result in premature exits or missed opportunities in sectors that are poised for sustained outperformance.





__Source:__ Bloomberg. Data Period: Apr'15 to Mar'25.

<u>Conclusion / Our Take:</u>

- **Understand the Macro Cycle:** Sector rotation is closely tied to the economic cycle - early cycle favours cyclicals, mid-cycle favours quality growth, and late-cycle favours defensives. This also applies to stock selection and analysis, as it guides valuation expectations, helps avoid value traps, and supports rotation between investment styles such as value and growth.
- **Track Earnings Upgrades:** Sector leaders typically see sustained earnings revisions before broader re-ratings.
- **Valuation Discipline:** Mean reversion in valuations often catalyses rotation as under-owned sectors start outperforming.
- **Application for HNI / UHNI Investors:** For investors, sector rotation strategy can be executed through; i) Sectoral/Thematic funds such as Business Cycle or Sector Rotation funds; ii) PMS strategies.
- **Key Risks:** Misjudging the cycle, high churn costs, volatility.

Appendix

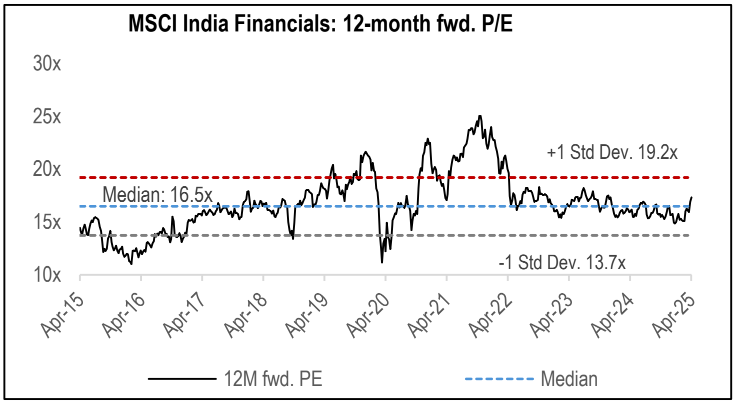
1. Top-3 Business Cycle Mutual Funds by Returns:

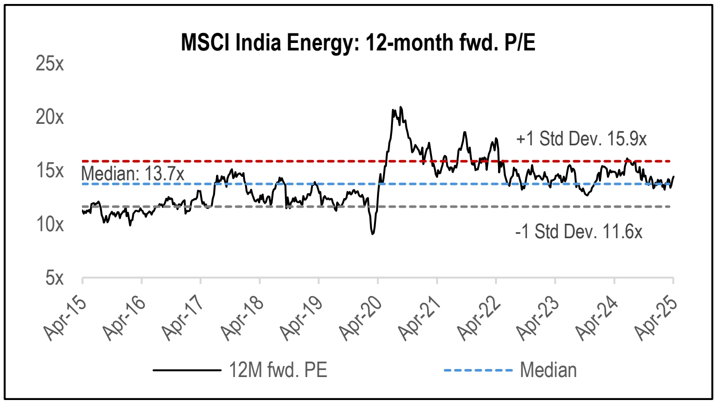
Business Cycle MF Schemes\	Corpus (INR cr)	Expense (%)	3M (%)	6M (%)	1Y (%)	2Y (%)	3Y (%)
ICICI Pru Business Cycle Fund	11,894	1.73	5.8	0	8	28.3	21
HSBC Business Cycle Fund	967	2.79	7.2	-5.7	8.2	26.4	20.9
Tata Business Cycle Fund	2,735	1.95	5	-5.7	2.4	24.5	19.1
Median (%)			**5.8**	**-5.7**	**8**	**26.4**	**20.9**
Nifty 500 TRI (%)			5.8	-2.1	7.1	21.6	15.1
Alpha (%)			**0**	**-3.6**	**0.9**	**4.8**	**5.8**

Source: Source: ACE MF. Priced as of 28 April, 2025.
Note: (i) Past performance is not an indicator of future returns; (ii)The above returns are shown for Regular Growth.

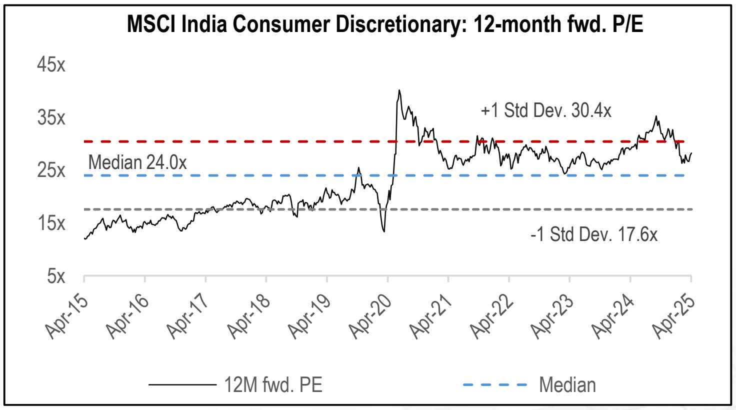
2. Valuation Charts:

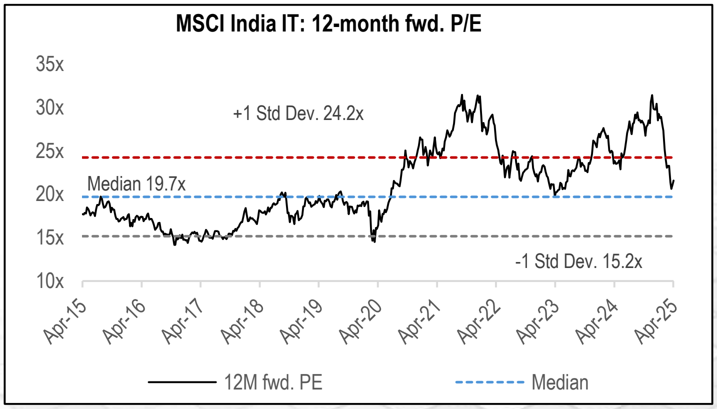
Sectors currently trading at fair valuations (in-line with long-term averages):





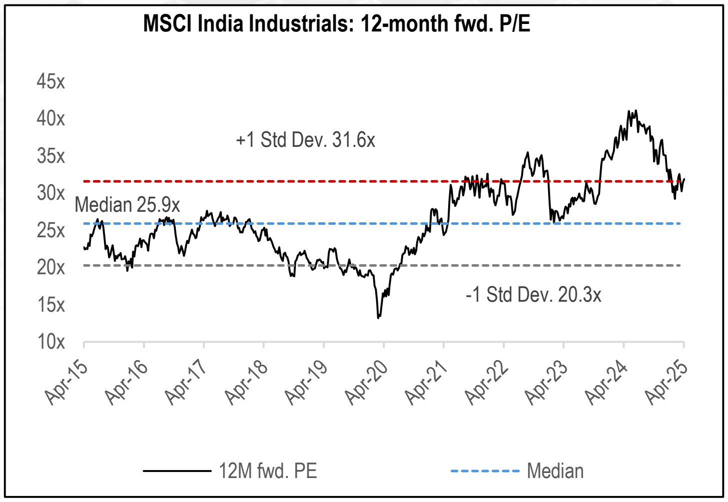
Source: Bloomberg. Data Period: Apr'15 to Apr'25.

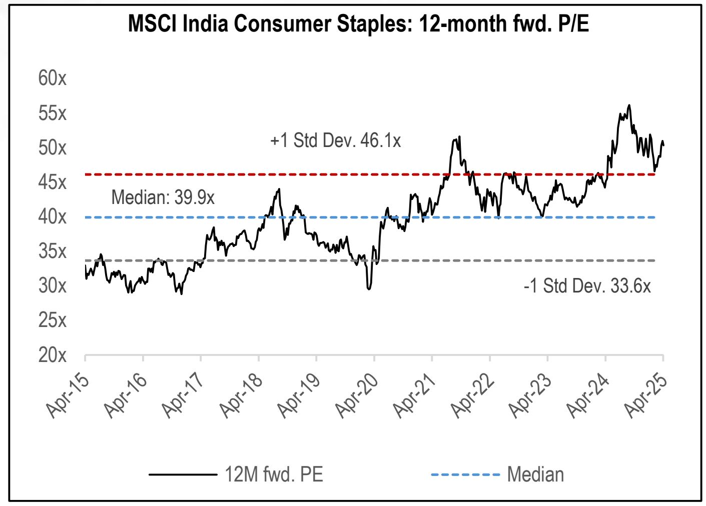




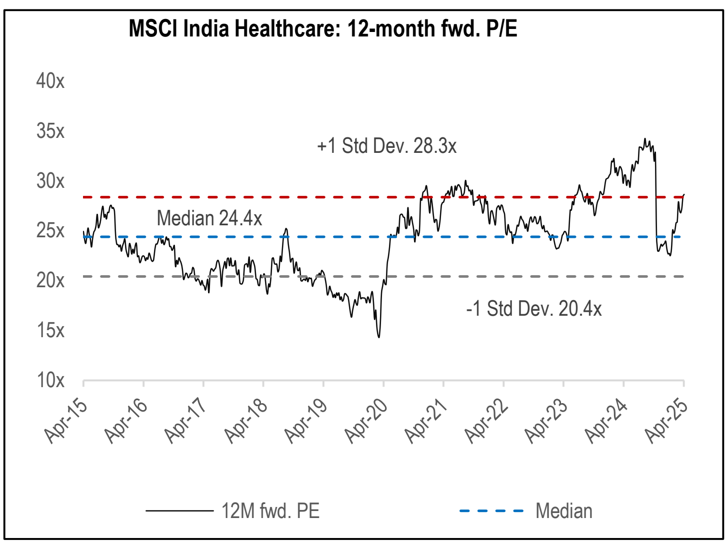
Source: Bloomberg. Data Period: Apr'15 to Apr'25.

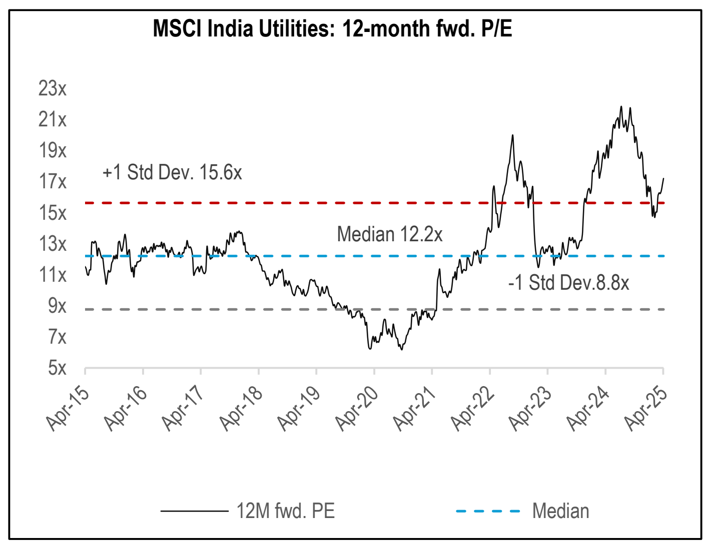
Sectors currently trading at +1 Std. Deviation above their long-term median:



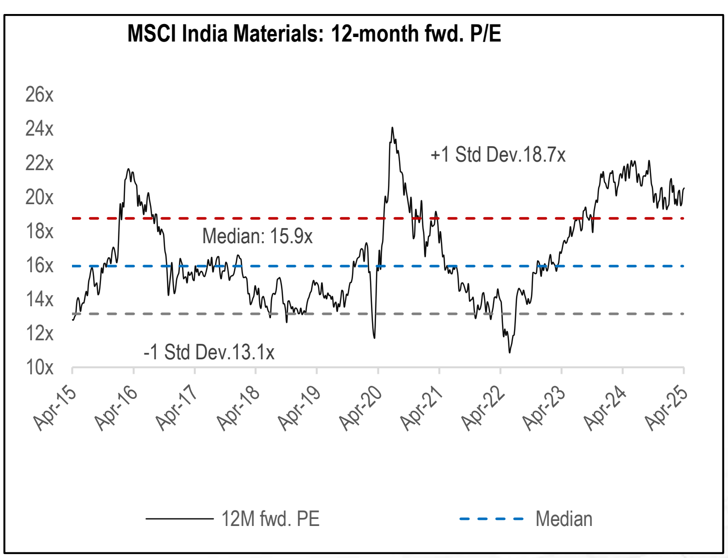


Source: *Bloomberg. Data Period: Apr'15 to Apr'25*





Source: *SBI Cards Annual Report and Axis MF.*



Source: *Bloomberg. Data Period: Apr'15 to Apr'25.*

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