

Current account back in deficit

- The current account finally reverted to a deficit of US\$1.7bn (-0.2% of GDP) in Q3FY21 from a surplus of US\$15.1bn (2.4% of GDP) in Q2FY21, driven by a widening in trade deficit, while the services surplus saw an improvement. Nonetheless, the material improvement in capital account in Q3FY21 led to a record-high BoP surplus of US\$32.5bn. The large capital account surplus was boosted by robust net FPI equity flows of US\$22bn. Although FPI flows moderated sequentially, they remained strong at ~\$17bn. The basic balance (CAD+FDI), which reflects durable current account funding, sharply moderated to US\$15.2bn from a whopping US\$40.1bn in Q2FY21.
- Going ahead, even as current account surplus will narrow further as domestic and global economies normalize, it will still likely to be in a surplus of 0.9% of GDP in FY21 amid a comfortable funding environment, implying FY21 BoP surplus of ~US\$90bn. However, the best seems to be over on external sector comfort. A gradual recovery means import growth will exceed export growth, while higher losses in oil led terms of trade imply current account/GDP to return to a deficit of ~0.8%. However, healthy capital flows should ensure FY22E BoP remains in surplus of US\$52bn.
- Net positive BoP dynamics should help keep a mild upward bias on INR vs. USD but the overall trajectory of INR will be caught between mixed external sector terms of trade, gradually changing global risk environment and RBI stance on FX. We see USD-INR in the range of 71.50-75.50 in FY22.

Q3FY21 current account turns into deficit on higher trade deficit

After posting a surplus in the previous three consecutive quarters, Q3FY21 current account finally gave way to deficit, printing (-)US\$1.7bn (-0.2% of GDP) vs. a surplus of US\$15.1bn (2.4% of GDP) in Q2FY21 and US\$2.6bn deficit (0.4% of GDP) a year ago. The sequential move toward CAD was primarily due to higher merchandise trade deficit of US\$34.5bn (4.7% of GDP) vs. US\$14.8bn (2.3% of GDP) in the preceding quarter, caused by a sharp rise in imports over exports stemming from higher oil prices and improving domestic demand. Imports rose to US\$111.8bn (US\$90.4bn in Q2FY21), while exports inched up marginally by US\$1.6bn (QoQ) to US\$77.2bn in Q3FY21. Turning to invisibles, net services receipts increased both sequentially and on a year-on-year basis, primarily on the back of higher net export earnings from computer services. Net remittances increased a tad to US\$19.3bn. However, net income drag worsened further to (-) US\$10.1bn from (-)US\$9.3bn.

Q3FY21 capital account bloats on FPI equity flows, leading BoP to super surplus

The material sequential improvement in capital account in Q3FY21 (US\$33.5bn; 4.5% of GDP) from Q2FY21 (US\$15.4bn; 2.4% of GDP) was largely due to robust equity FPI flows which largely picked pace in early November, FPI debt flows improved a tad. FDI flows moderated but remained healthy at US\$17.0bn (US\$24.6bn in Q2FY21). Other debt inflows like ECBs and banking capital continued to see outflows. ECB outflows stood at (-) US\$1.7bn, down from (-)US\$4.3bn in Q1FY21 with repayments exceeding fresh disbursements, while net accretions to NRI deposits increased to US\$3.0bn from US\$1.9bn in the previous quarter. Overall, BoP surplus in Q3FY21 remained high at US\$32.5bn (US\$31.6bn in Q2FY21). The basic balance (CAD+FDI), which reflects durable current account funding, moderated sharply sequentially to US\$15.2bn from a whopping US\$40.1bn in the prior quarter.

FY22 current account to reverse into 0.8% deficit amid normalization and oil effect

High-frequency external sector data imply Q4FY21 current account deficit will likely worsen further. Nonetheless, overall exports recovery for FY21 may still outdo that of core imports. We see FY21 current account/GDP at a surplus of 1.1% (US\$28bn), which would be led by huge terms of trade gains from a slump in oil imports while core import demand is still sluggish. Net funding remains comfortable amid still-easy global liquidity, with FY21 BoP in surplus of ~US\$96bn, helped by lower current account as well as solid FPI and FDI flows. As we move into FY22, a gradual recovery implies import growth will exceed export growth, while higher losses in oil led terms of trade will imply current account/GDP to return to a deficit of ~0.8%. However, healthy capital flows will ensure FY22E BoP remains in surplus of US\$52bn.

Ideally, positive BoP dynamics should help keep a mild upward bias on INR vs. USD, especially as global liquidity continues to chase carry in EM economies albeit selectively. However, global winds may imply foreign investors start asking for a higher risk premium from EM and could start pressurizing EM assets, including India. We note India's real rates are negative and one of the lowest in the EM pack. Besides, continued tactical intervention by the RBI will ensure the INR remains somewhere in the middle of the EM pack in terms of spot returns. Overall, the INR's performance will be caught between mixed external terms of trade, gradually changing global risk environment, RBI stance on FX and fiscal fragilities.

Please see our model portfolio (Emkay Alpha Portfolio): [Nifty \(Page 4\)](#)

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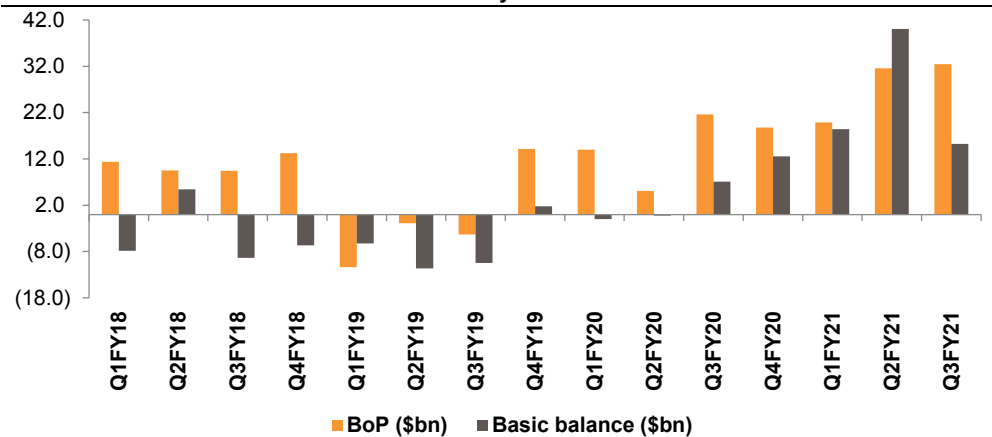
Key Highlights:

- Current account turns to deficit of 0.2% of GDP in Q3FY21.
- Capital account surplus improves further to 4.5% of GDP, led by robust FPI equity flows.
- BoP prints record surplus of US\$33.5bn, while the basic balance worsens to US\$15.2bn.
- FY21 current account/GDP to be in surplus of 0.9%; BoP to be in surplus of ~US\$90bn.
- FY22 CAD/GDP likely to be at 0.8%; BoP to be in surplus of ~US\$52bn.

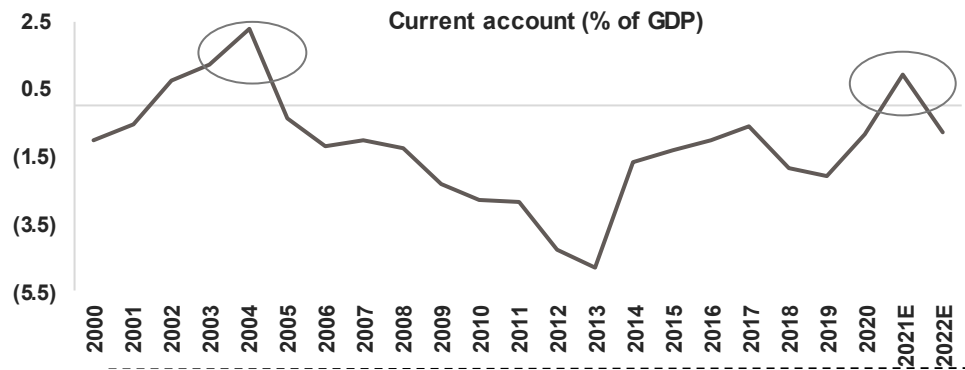
Exhibit 1: Current account reverts to deficit as trade deficit widens

(US\$bn)	3QFY20	Q4FY20	Q1FY21	Q2FY21	Q3FY21
Current account	(2.6)	0.6	19.2	15.5	(1.7)
CAD/GDP (%)	(0.4)	0.1	3.7	2.4	(0.2)
Trade balance	(36.0)	(35.0)	(10.8)	(14.8)	(34.5)
Trade balance/GDP (%)	(5.0)	(4.9)	(2.1)	(2.3)	(4.7)
- Exports	81.2	76.5	52.4	75.6	77.2
- oil exports	10.9	9.1	4.8	7.3	0.0
- non-oil exports	70.4	67.4	47.5	68.3	77.2
- Imports	117.3	111.6	63.1	90.4	111.8
- oil imports	31.5	33.8	13.2	18.8	0.0
- non-oil imports	85.8	77.7	49.9	71.6	111.8
Net Invisibles	33.4	35.6	30.0	30.3	32.8
- Services	21.9	22.0	20.5	21.2	23.6
o/w Software	21.5	21.1	20.8	22.3	23.4
o/w Non-software	0.4	0.9	(0.3)	(1.1)	0.2
- Transfers	18.9	18.4	17.0	18.4	19.3
- Net Income	(7.4)	(4.8)	(7.5)	(9.3)	(10.1)
Capital account	23.6	17.4	1.0	15.4	33.5
% of GDP	3.2	2.4	0.2	2.4	4.5
Foreign investment	17.6	(1.8)	(0.2)	31.6	38.2
- FDI	9.7	12.0	(0.8)	24.6	17.0
- FPI	7.8	(13.7)	0.6	7.0	21.2
Banking capital	(2.3)	(4.6)	2.2	(11.2)	(7.6)
- NRI deposits	0.8	2.8	3.0	1.9	3.0
Short-term credit	(1.4)	(1.0)	(0.2)	(1.8)	0.2
ECBs	3.2	10.3	(1.4)	(4.3)	(1.2)
External assistance	1.3	0.6	4.1	1.9	1.2
Other capital account items	5.2	13.8	(3.5)	(0.7)	2.8
E&O	0.6	0.9	(0.4)	0.6	0.7
Overall balance	21.6	18.8	19.8	31.6	32.5

Source: CEIC, Emkay Research

Exhibit 2: Basic BoP narrows in Q3FY21 but likely to remain comfortable in FY21

Source: CEIC, Emkay Research estimates

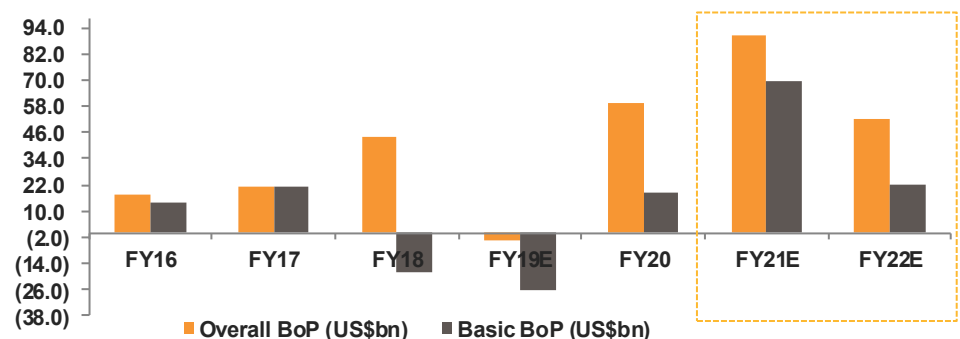
Exhibit 3: Current account/GDP poised to print 0.9% surplus in FY21, to be fully reversed in FY22

Source: CEIC, Emkay Research estimates

Exhibit 4: Current account/GDP to revert to 0.8% deficit in FY22 as trade deficit widens

(US\$bn)	FY17	FY18	FY19E	FY20E	FY21E	FY22E
Current account	(14.4)	(48.7)	(57.3)	(24.7)	23.6	(22.5)
CAD/GDP (%)	(0.6)	(1.8)	(2.1)	(0.8)	0.9	(0.8)
Trade balance	(112.4)	(160.0)	(180.3)	(157.5)	(104.6)	(158.0)
Trade balance/GDP (%)	(4.9)	(6.0)	(6.7)	(5.4)	(4.0)	(5.5)
- Exports	280	309	337	320	286	325
- Imports	393	469	518	478	391	483
- oil imports	87	109	141	131	81	141
Net invisibles	98	111	123	133	123	131
- Services	68	78	82	85	87	93
- Transfers	56	62	70	75	71	73
- Net Income	(26)	(29)	(29)	(27)	(35)	(35)
Capital account	36.4	91.4	54.4	83.2	66.8	75.0
% of GDP	1.6	3.4	2.0	2.9	2.6	2.6
Foreign investment	43.2	52.4	30.1	44.4	78.8	60.0
- FDI	35.6	30.3	30.7	43.0	45.8	45.0
- FPI	7.6	22.1	(0.6)	1.4	33.0	15.0
Banking capital	-17	16	7	-5	-19	5
- NRI deposits	(12)	10	10	9	10	10
Short-term credit	6	14	2	(1)	(1)	1
ECBs	(6)	(0)	10	23	3	5
Others	8	6	1	18	-	-
Overall BoP	21.6	43.6	(3.3)	59.5	90.3	52.5

Source: CEIC, Emkay Research

Exhibit 5: Basic BoP to narrow sharply in FY22 but still remain positive

Source: CEIC, Emkay Research estimates

Emkay Alpha Portfolio – Nifty

EAP-Nifty (25 stocks)

Company Name	Nifty Weight	Nifty EAP Weight	OW/UW (%)	OW/UW (bps)
Agri Input & Chemicals	0.56	0.00	-100%	-56
UPL	0.56	0.00	-100%	-56
Auto & Auto Ancillaries	5.40	9.38	74%	398
Bajaj Auto	0.75	1.98	164%	123
Eicher Motors	0.57	1.61	182%	104
Hero Motocorp	0.60	0.60	1%	1
Mahindra & Mahindra	1.20	0.00	-100%	-120
Maruti Suzuki India	1.44	2.69	88%	126
Tata Motors	0.85	2.50	193%	164
BFSI-Banks	26.43	34.46	30%	803
Axis Bank	2.76	5.67	105%	291
Bandhan Bank	0.00	2.03	NA	203
HDFC Bank	10.24	9.4	-8%	-85
ICICI Bank	6.34	7.37	16%	103
Indusind Bank	0.85	4.03	376%	319
Kotak Mahindra Bank	4.05	0.00	-100%	-405
State Bank of India	2.20	5.97	171%	377
BFSI-Insurance	1.45	2.08	43%	63
HDFC Life	0.91	0.00	-100%	-91
SBI Life	0.54	2.08	284%	154
BFSI-NBFCs	10.15	9.32	-8%	-83
Bajaj Finserv	0.92	0.00	-100%	-92
Bajaj Finance	2.15	0.00	-100%	-215
Cholamandalam Investment	0.00	2.17	NA	217
HDFC	7.08	7.15	1%	7
Cement & Building Materials	2.72	5.50	103%	279
Grasim Industries	0.87	1.48	70%	61
Shree Cements	0.62	1.71	176%	109
Ultratech Cement	1.22	2.31	89%	109
Consumer Goods & Retail	11.49	6.98	-39%	-451
Asian Paints	1.80	1.82	1%	2
Britannia Industries	0.67	0.00	-100%	-67
Hindustan Unilever	3.42	0.00	-100%	-342
ITC	3.01	1.97	-34%	-103
Nestle India	0.96	0.00	-100%	-96
Tata Consumer	0.60	0.00	-100%	-60
Titan Company	1.02	2.12	107%	110
United Breweries	0.00	1.06	NA	106
Engineering & Capital Goods	2.70	2.24	-17%	-46
Larsen & Toubro	2.70	2.24	-17%	-46
Information Technology	16.77	13.15	-22%	-362
HCL Tech	1.68	3.21	91%	154
Infosys	7.98	7.44	-7%	-54
TCS	5.18	0.00	-100%	-518
Tech Mahindra	0.97	2.50	158%	153
Wipro	0.96	0.00	-100%	-96
Metals & Mining	2.86	3.67	29%	81
Coal India	0.43	0.65	51%	22
Hindalco	0.75	1.48	97%	73
JSW Steel	0.71	0.00	-100%	-71
Tata Steel	0.96	1.54	60%	58
Oil & Gas	11.78	4.68	-60%	-709
BPCL	0.63	1.98	215%	135
GAIL	0.00	0.40	NA	40
Indian Oil	0.37	0.00	-100%	-37
ONGC	0.59	0.59	1%	1
Reliance Industries	10.19	1.71	-83%	-848
Pharmaceuticals	3.26	3.86	18%	60
Cadila Healthcare	0.00	1.03	NA	103
Cipla	0.65	0.66	1%	1
Divi's Lab	0.73	0.00	-100%	-73
Dr. Reddy's Lab	0.86	1.64	91%	78
Sun Pharma	1.02	0.53	-48%	-49
Ports & Logistics	0.81	0.00	-100%	-81
Adani Ports	0.81	0.00	-100%	-81
Power	1.67	1.70	2%	4
NTPC	0.80	0.82	3%	3
Power Grid Corporation	0.87	0.88	1%	1
Telecommunications	1.97	2.96	51%	100
Cash		0.00		
Nifty	100.0	100.00		

Source: Emkay Research; Note: *We have internally capped single stock exposure to 10% in our EAP

Sector portfolio NAV

	Base					Latest
	1-Apr-19	1-Apr-20	30-Sep-20	29-Dec-20	1-Mar-21	31-Mar-21
EAP - Nifty	100.0	69.7	91.3	112.1	122.7	121.0
Nifty50	100.0	70.7	96.4	119.4	126.5	125.9

*Performance measurement base date 1st April 2019

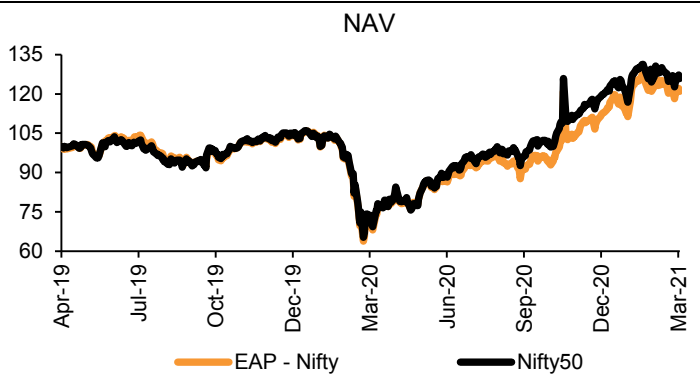
Source: Emkay Research

Price Performance (%)

	1m	3m	6m	12m
EAP - Nifty	-1.4%	7.9%	32.6%	73.6%
Nifty50	-0.5%	5.4%	30.6%	78.0%

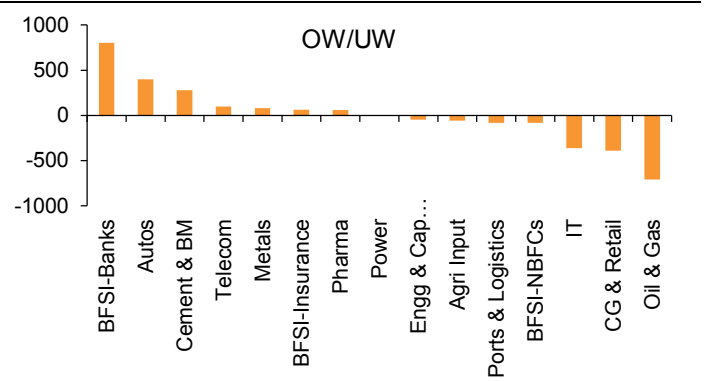
Source: Emkay Research

NAV chart



Source: Emkay Research

Sector OW/UW



Source: Emkay Research

Please see our model portfolio (Emkay Alpha Portfolio): [SMID](#)

“Emkay Alpha Portfolio – SMID and Nifty are a supporting document to the Emkay Alpha Portfolios Report and is updated on regular intervals”

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Ratings	Expected Return within the next 12-18 months.
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SELL	Below -5%

Completed Date: 01 Apr 2021 12:43:16 (SGT)

Dissemination Date: 01 Apr 2021 12:44:16 (SGT)

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