Market Review

July 2024

Macroeconomic Update

Global growth momentum slowed down led by moderation in economic activities in the US and China. US Nonfarm payroll (NFP) fell to near 3-year lows in July 2024 with unemployment rate rising to 4.3% (from 4.1% in June 2024). Also, US's PMIs eased further, and interest sensitive housing sector remained under pressure. On the other hand, China's manufacturing PMI also dipped in to contractionary territory while the pace of growth in manufacturing and infrastructure investments trended lower. Moreover, its real estate sector remained weak and industrial production slowed down. Economic activity in the Eurozone continues to remain lack luster. Inflation in the U.S. inched lower driven by a broad-based easing in goods, housing and services, while it remained subdued in China.

The U.S. Federal Open Market Committee (FOMC) kept its monetary policy unchanged in July 2024 but commentary was relatively dovish. Post the NFP data in August, US rate cut expectations have risen sharply and based on Fed Fund future rates, market is now factoring 125 bps rate cut by 31 December 2024 (as on 5th August 2024). Most other central banks are already in rate cutting mode with UK and China reducing rates during July 2024. However, Bank of Japan was the exception which raised rates by 15 bps to 0.25% during the month and reduced its quantum of security buying.
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Indian economic activity improves sequentially: Indian economic activity witnessed healthy growth during the month. While PMIs continue to remain well into the expansionary zone, retail auto sales of 2W & 4W, and GST collections also picked up during the month. Further, power demand, digital spending and employment also improved / remained healthy. Tractor sales, however, continue to contract on YOY basis.

Indicators	Units	Jan-24	Feb-24	Mar-24	Apr-24	May-24	Jun-24	Jul-24
Retail registration - Auto@								
2W	YoY, %	15.4	13.6	5.8	33.6	2.7	5.0	17.3
PV		16.1	15.1	-3.7	19.0	2.3	-3.7	11.0
MHCV		2.3	0.2	-14.6	-5.3	-3.4	-4.3	10.0
LCV		-3.9	-0.4	-7.5	-1.7	1.7	-8.1	1.9
Tractors		23.9	12.8	-1.8	2.5	-1.0	-27.5	-13.6
Gross GST Collection		11.7	12.5	11.5	12.4	10.0	7.6	10.3
Average E-Way bill generated		16.4	14.8	13.9	14.5	17.0	16.3	NA
Power demand		6.1	4.7	9.1	10.5	15.3	8.9	8.5
Digital Spending &		35.5	40.6	33.5	32.6	31.6	32.1	29.9
Railway Freight Tonnage		6.4	10.1	9.5	1.4	3.7	10.1	NA
Railway Freight Earnings		4.1	9.0	-	1.3	3.8	11.1	NA
Manufacturing PMI^	Index	56.5	56.9	59.1	58.8	57.5	58.3	58.1
Services PMI^	Index	61.8	60.6	61.2	60.8	60.2	60.5	60.3
Unemployment*	%	7.4	8.1	7.4	8.1	7.0	9.2	7.9

Source: www.gstn.org.in, www.icegate.gov.in, CMIE, PIB, RBI, www.vaahan.parivahan.gov.in, www.posoco.in
^Number >50 reflects expansions and number <50 reflects contraction compared to previous month. @ - figures are preliminary data and are subject to revision. &- Sum of UPI+IMPS spending; * based on CMIE survey

India's economic activity is showing resilience despite global weakness. India's growth in FY25 is expected to remain steady, though lower than FY24, supported by robust industrial and investment activities along with resilient services sector and urban consumption. Outlook on rural recovery remains optimistic in view of good progress of monsoon during the month.

Trade deficit eases slightly, likely to remain range bound: Trade deficit declined month on month in June 2024 primarily driven by sharp fall in oil imports (USD 15 billion vs ~USD 20 billion in May). This was marginally offset driven by higher net NONG imports. NONG exports declined on back of lower engineering and rice exports which was partially set off by lower import of transport equipments.

Amount in USD billion	May-24	Jun-24	Change
Trade Deficit / (Surplus)	23.8	21.0	-11.8%
Net Oil Imports	13.2	9.5	-27.7%
Net Gold Imports	2.6	2.8	8.4%
NONG^ net imports	8.0	8.6	7.7%

Source: CMIE, Ministry of Commerce; NM – Not meaningful. *Net Gold includes gold, silver and pearls precious & semiprecious stones adjusted for gems and jewellery exports.
^NONG refers to Non-Oil Non-Gold (as defined above) imports/exports

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Macroeconomic Update (contd...)

The trade deficit is likely to remain within a similar range in view of resilient domestic demand and easing in oil prices while exports might also pickup on back of expectations of improvement in global trade. Further, services exports are growing at a healthy pace of 13% YoY in Q1FY25. Overall, current account is likely to remain within manageable range in FY25.

Central government finances in a comfortable position: Fiscal deficit narrowed sharply on back of robust tax collections growth primarily driven by rise in direct taxes and non tax receipts. Personal as well as corporate tax collections witnessed a healthy YoY growth, albeit on a weaker base. Further, non-tax receipt rose on back of large increase in dividends from RBI. On the spending side, capex fell mainly because of delay in spending due to elections, while revenue spending grew only at a marginal pace.

INR billion	Q1FY24	Q1FY25	Change (YoY)
Gross tax revenue	6,719	8,308	23.7%
Total Direct Tax	3,302	4,621	39.9%
Total Indirect Tax	3,416	3,687	7.9%
Less: Share of States & others	2,383	2,812	18.0%
Net Tax collection	4,336	5,496	26.8%
Non-Tax Revenue	1,550	2,800	80.7%
Total Revenue Receipts	5,886	8,297	41.0%
Total Capital Receipts	107	45	-57.8%
Total Receipts	**5,993**	**8,342**	**39.2%**
Total Revenue Expenditures	7,722	7,889	2.2%
Total Capital Expenditures	2,785	1,811	-35.0%
Total Expenditures	**10,507**	**9,699**	**-7.7%**
Gross Fiscal Deficit	**-4,514**	**-1,357**	**-69.9%**
Fiscal Deficit as % of GDP	**-1.6%**	**-0.4%**	

Source: CMIE

While the fiscal deficit has been substantially low till Q1, it is likely to normalise in the coming months as government spending picks up. Government announced the full budget for FY25 in July 2024 wherein it estimates the fiscal deficit to narrow to 4.9% (interim budget estimate: 5.1%) of GDP. The revenue and spending assumptions for FY25 appears realistic and achievable.

Retail inflation inches up, likely to ease in coming quarters: India's June CPI rose to 5.1% YOY primarily driven by food inflation. Food and beverage inflation rose on the back of a sharp and broad-based increase in vegetable prices. Further, inflation of cereals and pulses continue to remain at an elevated level. Core CPI remained at similar level as last month with subdued momentum.

CPI is expected to decline over the coming quarters aided by favorable base effects, benign input price pressure, arrival of new crops easing food inflation and sluggish core CPI momentum.

YoY, %	May-24	Jun-24	Change in %
CPI	4.8	5.1	0.3
Food & Beverages	7.9	8.4	0.5
Fuel and Light	-3.7	-3.7	-
Housing	2.6	2.7	0.1
Transportation & communication	1.0	1.0	-
Core CPI[@]	3.8	3.8	-

Source: CMIE; @-CPI excluding food, fuel, transportation & housing

Commodity prices: Weak economic activity weighed on the commodity prices with most major commodities declining month on month. Gold prices rose on back of haven demand.

	Market price (USD)*	July-24^	FYTD25 (%)&
Brent Crude (per barrel)	80.7	(6.6)	(7.7)
Gold (per ounce)	2,448	5.2	9.8
Steel (per tonne)	510	(2.9)	0.0
Zinc (per tonne)	2,635	(9.8)	10.2
Copper (per tonne)	9,015	(4.9)	3.3
Aluminium (per tonne)	2,228	(10.4)	(2.9)
Lead (per tonne)	2,024	(6.3)	3.0

Source: Bloomberg; *Market prices as on July 31, 2024. ^M-o-M change. & - Change in YTD25

Macroeconomic Update (contd...)

Summary and Conclusion:

Global economic activity momentum continued to moderate in July 2024 after a subdued Q2CY24. The outlook on growth remains uncertain especially in view of ongoing weakness in the US labour market which has been the primary driver in sustaining global growth. Further, economic activity in China remains weak and impact of growth supportive measure has been relatively low till now.

India's growth, however, remains steady supported by buoyant manufacturing and service sectors. Well progressing monsoon is supportive of agriculture activity and rural incomes. Investments remain supported by real estate activity, government capex spending and improvement in organised private corporate capex. Private corporate sector capital expenditure has potential to grow faster in view of low leverage, increasing capacity utilization, consistent corporate profitability, and a robust banking sector balance sheet. India's external sector also remains robust on the back of comfortable current account deficit and adequate forex reserves. Rise in geopolitical tension disrupting supply chains, sharp deceleration in global economic activity, etc. are key near-term risks.

Looking ahead, the medium-term outlook for India's economy appears promising. This optimism is fuelled by policy continuity, benefits from Production-Linked Incentive schemes, opportunities arising from shift in the global supply chain, enhanced infrastructure investments, the potential of resurgence in private sector capex, and the enduring robustness of consumption.

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Equity Market Update

In July, Nifty and BSE Sensex indices ended ~3.5/4% respectively higher compared to the end of June 2024. The midcap and small index returns surpassed the large-cap benchmarks. The market remains supported by continued FII and DII buying, steady economic growth, etc. Most sectors gained during the month with IT, Oil & Gas, FMCG, Healthcare, Power, Auto and Capital goods being the key outperformers. Key events and factors which influenced the market during the month include – rate hike by Bank of Japan, range bound US yields, escalation of tension between Israel and Iran, etc. Notably, in early August 2024, weak employment data in the US and hawkish Bank of Japan, has resulted in heighted volatility in all major equity markets.

Global market performance was mixed. Equity markets in the US and Europe ended in positive while Japan, Korea, China and Hong Kong equities declined. Below are detailed tables outlining the performance of key domestic and global indices:

% Change in Indices	Jul-24	FYTD25^
BSE India Auto	5.0	22.5
BSE India Bankex	(1.3)	10.0
BSE India Capital Goods	4.6	24.1
BSE India FMCG	9.5	16.5
BSE India Healthcare	9.2	15.6
BSE India Metal	(0.8)	16.2
BSE India Power	6.1	26.0
BSE India Oil & Gas	10.5	17.8
BSE India IT	12.9	17.0
BSE SENSEX	3.4	**11.0**
NIFTY 50	3.9	**11.8**
NIFTY Midcap 100	5.8	**22.7**
NIFTY Smallcap	4.5	**25.3**

% Change	Jul-24	FYTD25^
S&P 500	1.1	5.1
Nasdaq	(0.8)	7.4
FTSE	2.5	5.2
DAX	1.5	0.1
CAC	0.7	(8.2)
Nikkei	(1.2)	(3.1)
Hang Seng	(2.1)	4.9
KOSPI	(1.0)	0.9
Shanghai	(1.0)	(3.4)
MSCI Emerging Market Index	(0.1)	4.0

Source: Bloomberg; ^Returns in FYTD25

FPIs bought equities worth USD 3.9 billion in July 2024 (June 2024: USD 3.2 billion) and have cumulatively bought equity worth USD 3.0 billion in 4MFY25 (4MFY24: USD 18.2 billion). DIIs, on the other hand, bought net equity worth USD 2.8 billion in July 2024 (June 2024: USD 3.2 billion) and have cumulatively bought USD 18.2 billion in 4MFY25 (4MFY24: USD 0.1 billion).

Mutual funds flows were steady at ~INR 51,500 crore in June 2024 (May 2024: ~INR 45,200 crores) and cumulatively amounted to ~INR 128,000 crore in Q1FY25 (Q1FY24: ~INR 20,000 crore).

Outlook

As on July 31, 2024, NIFTY 50 was trading at ~23x FY25E price to earnings multiple. Further, Market cap-to-GDP stood ~136% (based on CY24 GDP estimates) and the gap between 10Y G-sec yield and 1Y-Forward NIFTY 50 earnings yield* remains at elevated level [*Earnings yield = 1/ (one year forward P/E)*]. Thus, current valuation indicators are at a premium to their historical averages. However, this is partially due to structurally attractive nominal GDP growth, a healthy corporate earnings outlook and robust de-levered corporate and banking balance sheets.

Chart 1

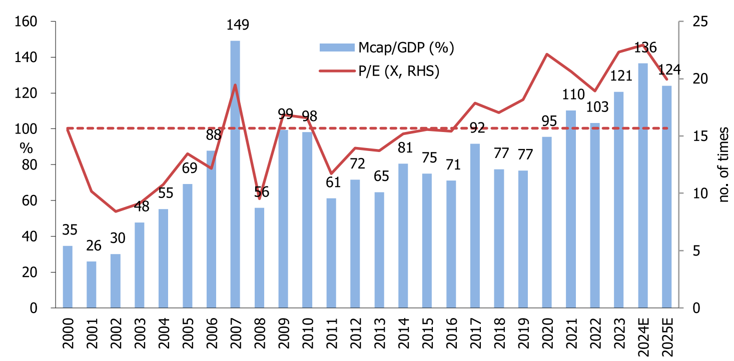
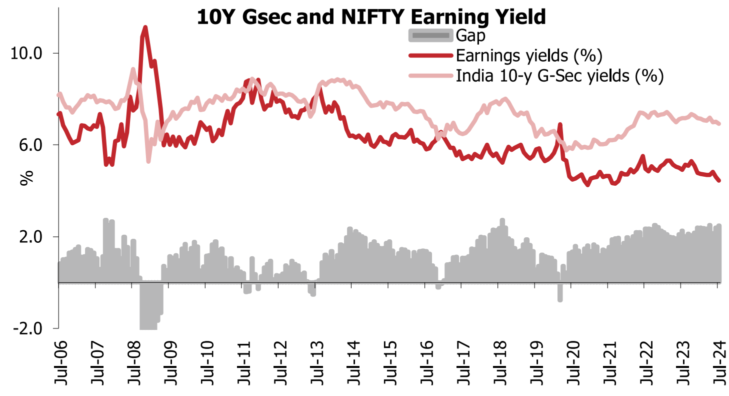


Chart 2



Source: Kotak Institutional Equities; For 2024 and 2025, the market cap as on July 31, 2024 is taken and divided by GDP estimates for CY24 and CY25

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Equity Market Update (contd...)

Except for private banks, valuations for major sectors are higher than long-term averages as shown in the table below:

	12 months forward Price to Earnings		
	31-Jul-24	**LTA**	**Discount / Premium^**
IT Services	27.9	20.5	36.0
PSU Banks@	1.5	1.1	35.7
Pharma	31.1	23.9	30.2
Metals	13.0	10.0	29.6
Oil and gas	15.8	12.2	29.4
Consumer staples	42.8	35.3	21.5
Consumer Discretionary	64.2	53.1	20.9
Auto	23.6	19.6	20.5
Private Banks@	2.4	2.6	-6.9

Source: Kotak Institutional Equities. Stocks are part of Kotak Institutional Equities universe.
LTA – 10 Years average. Cells in green are sectors which are trading at premium. All figures are calculated based on 12 months forward estimates.
^to Long term (LT) average, @-Price to Book value

The rally over the past year and half has been broad and small cap and mid cap indices have significantly outperformed. Despite corrections seen in early August 2024, these trade at a noteworthy premium to their long-term average valuation and large caps. Given the aggregate valuation being higher than historical average, the importance of stock selection increases even more.

Our medium to long term positive outlook on Indian equities remains unchanged driven by the structurally robust domestic growth outlook, healthy corporate profitability, and supportive pro-growth policies. However, near-term risks include a significant global growth slowdown, heightened geopolitical tensions, slowdown in government's reforms momentum, etc.

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Debt Market Update

Gsec yields saw a broad-based decline during the month and 10Y Gsec yield ended the month at 6.93%, down 8 bps from the previous month. The yields at the short end fell more than the long end, resulting in steepening of the yield curve. During the month, RBI released draft circular which proposed to increase the percentage of High Quality of Liquid asset (HQLA) to be kept by banking sector against deposits which are enabled for internet and mobile banking. Further, it increased the haircut on key assets qualifying for HQLA (Gsec, T-bills and SDLs). Thus, in effect, RBI circular, if implemented, will result in large increase in demand of SLR securities. This resulted in yields rallying during the month. Apart from aforesaid, key factors and events which influenced the fixed income markets, include lower than expected fiscal deficit of central government, benign domestic core CPI, consistent buying by FIIs, fall in US yields and oil prices, etc. The 10-year corporate bond spreads over Gsec widened compared to last month. The table below gives a summary view of the movement of key rates and liquidity:

	Jun-24	Jul-24	Change (in bps)
MIBOR Overnight Rate (%)	6.86	6.55	-0.31
3M Gsec yield (%)	6.80	6.67	-0.13
10Yr Benchmark G-Sec Yield^ (%)	7.01	6.93	-0.08
AAA 10Year Corporate Bond Yields#,& (%)	7.49	7.46	-0.03
AAA 10Y Corporate bond spread against 10Y benchmark@ (bps)	48	53	5
Average net liquidity absorbed/infused by RBI* (INR billion)	-547	1,027	NA

NM – not meaningful. ^-bi-annual yield; #-annualised yield; & - Average yield of 8.62% NABARD bond maturing on 14-Mar-2034 provided by independent valuation agencies has been taken. @ - Spreads calculated by subtracting non-annualised Gsec yields from annualised corporate bond yields.
*Average net daily liquidity infused / absorbed through Liquidity Adjustment Facility, exports refinance, marginal standing facility and term repos/reverse repos. Source: Bloomberg, RBI

Average interbank liquidity turned positive in July 2024 driven by redemption of government securities, forex purchases by RBI and decline in currency in circulation.

FPIs bought debt (including under voluntary retention route) worth USD 1.9 billion in July 2024 (June 2024: USD 1.7 billion). FPIs have bought net debt worth USD 4.3 billion in 4MFY25 as against net buying of USD 2.1 billion during the same period last year.

Outlook

The Union budget presented during the month projects the fiscal deficit to consolidate to 4.9% of GDP (FY24: 5.6%) in FY25. Further, government reiterated that the target of bringing down centre fiscal deficit to less than 4.5% of GDP by FY26 remains unchanged. This comforted the market which was watchful of any deviation from fiscal consolidation path and thus, Gsec rallied during the month. This was further supported by release of draft circular by RBI on Liquidity Coverage Ratio (LCR) which, if implemented, can increase the SLR demand by banks.

Fixed income remains favourably placed over the medium term considering:

- Global growth is increasingly showing signs of slowdown and most AE central banks have begun to reduce policy rates, RBI is also likely to cut policy rates in H2FY25.
- Inclusion of India's sovereign securities in JP Morgan global bond indices bodes well for demand outlook for G-Sec in FY25. Further, likely increase in demand of HQLA assets due to higher LCR requirements is also likely to add to strong demand for SLR securities.
- Higher-than-expected RBI dividend and expectations that it can remain at an elevated level in next year as well - should aid fiscal consolidation and keep market borrowings within manageable levels.
- Core CPI momentum remains subdued on back of lower input price pressure.
- External sector remains comfortable in view of steady growth in services exports, fall in oil prices and adequate foreign exchange reserves.
- Revision of India's sovereign rating outlook to positive (Rating unchanged at BBB-) from stable by S&P enhances the possibility of rating upgrade for India in next couple of years.

Key risks to the favourable outlook:

- Regular ffood price shocks keeping headline CPI at an elevated level.
- Robust credit growth and elevated SLR holdings can keep the incremental demand for G-Secs from banks subdued.
- Rise in commodity prices driven by escalation of geopolitical tensions .

Overall, in our view, yields are likely to trade with a downward bias and the long end of the yield curve is likely to outperform over the medium term. Thus, as highlighted in past, investors with a relatively longer investment horizon, can continue to increase allocation to longer duration funds in line with individual risk appetite. Further, while yield curve has steepened during the month, it is still relatively flat and in view of elevated short-term rates along with expectations of rate cuts in H2FY25, one may also consider investment in short or medium duration categories of debt funds.

Source for various data points: Bloomberg, NSDL, CMIE, RBI, Kotak Institutional Research, World Bank, Daily valuation provided by ICRA/CRISIL.

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Glossary

AE	Advanced Economies
BoE	Bank of England
BoJ	Bank of Japan
BoP	Balance of Payment
bps	Basis points
CAGR	Compound Annual Growth Rate
CMIE	Centre for Monitoring Indian Economy
CPI	Consumer Price Index
CRR	Cash Reserve Ratio
CV	Commercial Vehicle
DIIs	Domestic Institutional Investors
EA	Euro Area
ECB	European Central Bank
FOMC	Federal Open Market Committee
FPI	Foreign Portfolio Investment
GDP	Gross Domestic Product
GST	Goods and Services Tax
GVA	Gross Value Added
IMD	India Meteorological Department
INR	Indian Rupee
IMF	International Monetary Fund
IMPS	Immediate Payment System
JGB	Japanese Government Bonds
LCV	Light Commercial Vehicle
Mbpd	Million Barrels Per Day
MHCV	Medium and Heavy Commercial Vehicle
MIBOR	Mumbai Interbank Offered Rate
M-o-M	Month on Month
MPC	Monetary Policy Committee
MSP	Minimum Support Prices
NABARD	National Bank for Agriculture and Rural Development
NBFC	Non-Banking Financial Company
NONG	Non-Oil Non-Gold
NSO	National Statistical Organization
OMO	Open Market Operation
PIB	Press Information Bureau
PLI	Production Linked Incentive
PMI	Purchasing Managers' Index
PPI	Producer Price Index
PSU	Public Sector Undertaking
PV	Passenger Vehicle
RBI	Reserve bank of India
RE	Revised Estimates
RRR	Reserve Ratio Requirement (for banks in China)
SLR	Statutory Liquidity Ratio
UPI	United Payments Interface
US	United States of America
USD	United States Dollar
UST	US Treasuries
YoY	Year on Year

For complete details on budget, please refer to the budget documents available on https://www.indiabudget.gov.in/