India Equity & Fixed Income Markets

Market Commentary: November 2022

Global Economy

The US GDP expanded at a revised 2.9% in Q3 2022 on an annualized basis, compared with a contraction of 0.6% in Q2. The US Fed, in its November policy meeting, raised its target interest rate by 75 bps for the fourth consecutive time, taking its benchmark lending rate to 3.75% - 4%, highest since January 2008. The US Fed also indicated in its November policy meet minutes that the rate hikes going forward may slow down in order to reduce the risk of instability in the financial system.

The Eurozone economy expanded 2.1% y-o-y in Q3 2022, moderating from an upwardly revised 4.3% in Q2 2022. The European Central Bank raised its main refinancing operations rate by 75 bps to 2.00%, its highest since 2009.

The UK's economy contracted by 0.2% on a sequential basis in Q3 2022. The Bank of England in its November meeting raised interest rates by 75 basis points to 3% in its November meet, its largest single hike since 1989. It also warned of a prolonged recession as policymakers looked to temper market expectations for further aggressive monetary policy tightening.

China's GDP expanded at a faster than expected rate of 3.9% on a y-o-y basis in Q3 2022 owing to Government support measures and easing Covid restrictions. However, towards the end of the quarter Covid restrictions were reintroduced in several cities on account of rising cases. The People's Bank of China (PBoC) kept its interest rates unchanged for the third straight month as policymakers remained wary of stoking further weakness in the yuan by easing monetary conditions.

Japan's economy contracted by 1.2% on an annualized basis in Q3 2022, from an upwardly revised 4.6% expansion in Q2 2022. The Bank of Japan kept its ultra-low rates unchanged at a policy meeting. It also debated upon the side effects of prolonged monetary easing and the potential effects of an exit from ultra-low interest rates in the minutes of its policy meet. (Source: CRISIL Research)

Indian Economy

India's real GDP (at market prices) slowed from 13.5% YoY in the Jun-22 quarter to 6.3%YoY in the Sept-22 quarter due to the waning of favourable base effect. Growth was led by private household consumption and fixed capex expenditure while net exports remained a drag to GDP growth.

A variety of high frequency data, suggest robust economic momentum underpinned by pent-up demand for high contact services that had been lagging thus far. India's factory output growth as measured by the Purchasing Manager's Index rose to a three month high of 55.7 in November compared to 55.3 in October, maintaining robust growth despite global headwinds. Output in the services sector expanded at the quickest pace in three months, with the Services PMI index coming in at 56.4 from 55.1 in October. (Source: CRISIL Research)

Market Performance

Indian equities extended their gains for the second consecutive month in November 2022, with headline indices S&P BSE Sensex and Nifty 50 reaching their all-time highs, rallying by 3.9% and 4.2% respectively *(Currency: INR; Source: Morningstar Direct).* Markets were buoyed by upbeat corporate earnings growth in the latest quarter ended September and expectations of global central banks pivoting to a less hawkish policy stance. Sentiments were further supported after a moderation in global crude prices and domestic retail inflation for October raised the possibility of a smaller rate hike by the central bank going ahead.

With respect to the broader EM peers, MSCI India underperformed in the month (up +5.2%), while MSCI EM rose by +14.8%, led by Chinese equities. *(Currency: USD; Source: Morningstar Direct)*

All sectors delivered positive returns in the month, except Power and Consumer Durables. Metal stocks were the biggest gainers, tracking positive global cues amid demand expectations. Oil and Gas marketing companies also rallied due to an intermittent fall in global crude prices.

Mid-caps (1.9%) and Small caps (3.0%) underperformed the Large caps during the month. *(Source: Morningstar Direct; Currency: INR)*

FPIs remained buyers of Indian equities in the month of November (+USD 3.6bn, following +USD 1.0bn inflows in October). Domestic institutional investors reversed their buying trend from the previous month, recording negative flows (-USD 0.3bn). Domestic selling was led by insurance funds (-USD 439mn), with domestic mutual funds remaining net buyers (+USD 165mn). *(Source: JP Morgan research)*

Bond Markets

Bond prices rallied in November as lower than expected inflation and expectations of moderating quantum of rate hikes by central banks boosted investor sentiments. The benchmark 10-year G-Sec yield fell 17 bps to 7.28% on Nov 30, 2022 from 7.45% as on Oct 31, 2022. (Source: CCIL, CRISIL Research)

Corporate bond yield curve continued to flatten, as shorter end yield rose while longer-end yields cooled down. Credit spreads over G-Secs have widened due to softe

r transmission of G-Sec yield movements onto corporate bond yields.

Interbank call money rates remained below the RBI repo rate in November amid comfortable liquidity in the system. Liquidity situation has improved due to continued dollar inflows on the back of renewed foreign investments. The RBI intermittently conducted variable-rate reverse repo auctions during the month to drain out excess liquidity.

Monetary Policy

The Reserve Bank of India (RBI) has raised its benchmark repo rate for the fifth consecutive time, albeit by 35bps instead of the previous 50bps hikes, to 6.25%. The monetary policy stance remains maintained at 'withdrawal of excess accommodation'. The RBI also lowered its growth forecast for FY23 to 6.8% from its earlier projection of 7%. Inflation is projected to remain above its 4% target for the next 12 months with the inflation forecast for FY23 maintained at 6.7%. (Source: RBI)

Currency

INR appreciated in the month (up 1.7% MoM) and ended the month at 81.43 per USD in November. (Source: Bloomberg, JP Morgan research)

Inflation

Retail CPI inflation, eased to a three-month low of 6.77% in the month of October. The WPI inflation eased to 8.39% in October from 10.70% in September 2022. The core inflation (ex-food and ex-energy) has gone below the Central Bank's upper target of 6% (at 5.9%) in October. (Source: MOSPI, CRISIL)

Bank Credit/ Deposit Growth

Banking system credit growth remained steady at 17% YoY while deposits growth lagged at 8.2% YoY in the latest fortnightly data as of 18th November. (Source: RBI)

Liquidity

Liquidity situation has improved due to continued dollar inflows on the back of renewed foreign investments. Overall system liquidity is now into surplus, with the average daily absorption under the liquidity adjustment facility now at INR 1.2tn as of 30th November 2022. (Source: RBI)

GST Collections

GST revenue collection for the month of November 2022 accounted for INR 1.46tn. The revenue collection has witnessed a surge of 11% on an annual basis. (Source: Ministry of Finance)

Government Deficit

Federal fiscal deficit for the first seven months of the financial year (Apr-Oct) rose to USD 93bn billion (45.6% of annual budget), though rising tax collections helped offset a higher subsidy bill. Net tax collections during April-October rose to INR 10.5tn, about 31% higher than a year before in the corresponding period.

Trade deficit in October widens to USD 26.91bn, exports down 17% to USD 29.8bn as compared to USD 35.4bn in September. (Source: MOSPI, RBI)

Equity Outlook

Investors' anticipation of a Fed pivot has attracted capital back into equity asset class, with a bias towards Largecaps. Indian equities have benefitted from this risk-on mood and continues to see optimism in the near future amidst relatively robust economic activity and demand momentum. Sentiments were further supported after a moderation in global crude prices and domestic retail inflation for October raised the possibility of a smaller rate hike by the central bank going ahead.

Indian equities valuations continue to remain high as compared to other global markets. However, over the long term, we remain constructive on Indian equities owing to a conducive domestic environment, supportive Government policies focused on capex led economic growth, favorable external indicators - high forex reserves, increased share of Foreign Direct Investment (FDI) flows and increasing participation of domestic investors in equity markets which is a more structural trend. As major developed & emerging economies grapple with multiple problems like rising inflation/interest rates and slow growth, India is doing relatively better and remains a favored destination to play the China +1 theme.

We would continue to accumulate companies with strong balance sheets, agile managements, low leverage and sustainable business models. We are positive on sectors which are closely linked to the economic recovery like Banks, Auto/Auto Ancillaries and Telecom.

Going forward, the pace of US Fed rate hikes in their further meetings and its normalization of balance sheets, trajectory of crude oil prices, geopolitical developments in Europe, inflation trajectory in India and finally retail investor sentiments may provide cues for market performance. Market performance ahead could also be determined by earnings growth in coming quarters as the current high inflationary environment could lead to downgrades in the earnings estimates for some sectors.

Fixed Income Market- Outlook

- Bond prices rallied in November on account of lower-than-expected inflation and anticipation of slowing rate hikes by central banks. The yield curve is very flat at the present, presenting an opportunity to be positioned in the shorter end of the curve rather than the longer end.
- A similar trend was visible in corporate bond yields – the shorter end of the duration rising higher than the longer end.
- Credit spreads over G-Secs have widened due to softer transmission of G-Sec yield movements onto corporate bond yields. Wide spreads are a feature of the growth phase of the economic cycle. In this phase, accrual strategy is more attractive compared to duration.
- We expect accruals to become a dominant source of returns going ahead.
- Also, going forward, we expect the RBI to continue hiking rates due to inflation persisting above the RBI's comfort level; and also to offset the US Fed's rate hikes in a bid to protect the INR against a stronger US dollar.
- We continue to hold floating-rate bonds as a defensive stance due to rising-rate environment and expect them to outperform all other fixed-income instruments in the current rising interest rate scenario.

Disclaimers

This article is for information purposes only and is not an offer to sell or a solicitation to buy any security or a recommendation or advice. The information that is used here is believed to be from reliable sources and is publicly available, including information developed in-house. These views alone are not sufficient and shouldn't be used for the development or implementation of an investment strategy. It should not be construed as investment advice to any party. All opinions and estimates included constitute our view as of this date and are subject to change without notice. While utmost care has been exercised while preparing the article, the sender does not warrant the completeness or accuracy of the information and disclaims all liabilities, losses and damages arising out of the use of this information. The recipient of this article should rely on their investigations and take their own professional advice.

In the preparation of the material contained in this document, the AMC has used information that is publicly available, including information developed in-house. Some of the material used in the document may have been obtained from members/persons other than the Fund and/or its affiliates and which may have been made available to the Fund and/or to its affiliates. Information gathered and material used in this document is believed to be from reliable sources. The Fund however does not warrant the accuracy, reasonableness and/or completeness of any information. For data reference to any third party in this material no such party will assume any liability for the same. All recipients of this material should before dealing and or transacting in any of the products referred to in this material make their own investigation, seek appropriate professional advice and carefully read the offer document. We have included statements/opinions/recommendations in this document, which contain words, or phrases such as "will", "expect", "should", "believe" and similar expressions or variations of such expressions that are "forward looking statements". Actual results may differ materially from those suggested by the forward looking statements due to risk or uncertainties associated with our expectations with respect to, but not limited to, exposure to market risks, general economic and political conditions in India and other countries globally, which have an impact on our services and / or investments, the monitory and interest policies of India, inflation, deflation, unanticipated turbulence in interest rates, foreign exchange rates, equity prices or other rates or prices, the performance of the financial markets in India and globally, changes in domestic and foreign laws, regulations and taxes and changes in competition in the industry.

The AMC (including its affiliates), the Fund and any of its officers, directors, personnel and employees, shall not be liable for any loss, damage of any nature, including but not limited to direct, indirect, punitive, special, exemplary, consequential, as also any loss of profit in any way arising from the use of this material in any manner.