HDFC MUTUAL FUND
BHAROSA APNO KA

Market Review
January 2024

Macroeconomic Update

The global economy continues to perform better than expected driven by strength in the US economy. IMF revised up its global growth forecast for CY24 to 3.1% (from 2.9%). The US GDP grew at an annualized pace of 3.3% in Q4CY23 led by resilient personal consumption. The US labour market continues to be tight with non-farm payroll coming in better than expected, unemployment rate low and wage growth elevated. However, the housing and manufacturing sectors remain under pressure on the back of elevated interest rates. Broad based weakness was visible in the Eurozone with manufacturing as well as the services sector decelerating. The tight monetary policy, low consumer confidence, extended war, slowing global trade, etc. continue to weigh on its growth. China's economic conditions remain sanguine too with real estate weak and CPI in deflationary territory. However, manufacturing and infrastructure investments along with retail sales are holding up well. Chinese regulatory authority continued to rollout growth supportive measures such as further relaxation for housing sector, a higher than expected cut of 50 bps (consensus expectation: 25 bps) for its banks to improve liquidity, etc.

Inflation trended lower across major economies with both headline and core inflation softening. The Core inflation, while still higher than pre-pandemic as well as target, the trajectory is comforting for Central banks in AEs. Consequently, majority of central banks, such as those of the US, UK, ECB, and Bank of Japan, opted to keep their monetary policy unchanged.

Interim Budget remains focused on fiscal consolidation: Surpassing the market expectations, central government announced fiscal deficit target of 5.1% of GDP in FY25 (FY24RE: 5.8%) and reiterated its commitment to bring down the same to below 4.5% by FY26. The fiscal assumptions appear to be realistic and credible. The assumed tax buoyancy of ~1.2x and ~1.1x for direct and indirect tax collections respectively is broadly in line with recent trends. Achievement of capital receipts is contingent upon successful divestment in key companies. The government aims to maintain a tight leash on revenue spending (~3.2% growth YoY) and continue its thrust on capex (growth of 16.9% over RE).

INR trillion	FY23 Actual	FY24RE	FY25BE	FY24RE over FY23 Actual	FY25BE over FY24RE
Gross tax collection	**30.5**	**34.4**	**38.3**	12.5%	11.5%
Total Direct Tax	**16.7**	**19.6**	**22.1**	17.1%	13.0%
Corporate Tax	8.3	9.2	10.4	11.7%	13.0%
Personal Income Tax	8.5	10.4	11.7	22.3%	13.0%
Total Indirect Tax	**13.8**	**14.8**	**16.2**	7.1%	9.4%
GST	8.5	9.6	10.7	12.7%	11.6%
Less: Share of States and others	9.6	11.1	12.3	16.4%	10.4%
Net Tax collection	**21.0**	**23.2**	**26.0**	10.8%	11.9%
Non-Tax Revenue	**2.9**	**3.8**	**4.0**	31.7%	6.4%
Total Revenue Receipts	**23.8**	**27.0**	**30.0**	13.3%	11.2%
Capital Receipts	**0.7**	**0.6**	**0.8**	-22.4%	41.1%
Divestments	0.5	0.3	0.5	-34.8%	66.7%
Total Receipts	**24.6**	**27.6**	**30.8**	12.2%	11.8%
Revenue Expenditures	34.5	35.4	36.5	2.5%	3.2%
Capital Expenditures	7.4	9.5	11.1	28.4%	16.9%
Total Expenditures	**41.9**	**44.9**	**47.7**	7.1%	6.1%
Gross Fiscal Deficit	**-17.4**	**-17.3**	**-16.9**	-0.2%	-2.8%
Fiscal Deficit as % of GDP	**-6.4%**	**-5.8%**	**-5.1%**		

Source: CMIE, Kotak Institutional Equities; BE – Budget estimates, RE – Revised estimates

HDFC MUTUAL FUND
BHAROSA APNO KA

Macroeconomic Update (contd...)

Indian economic activity holding up well: India's growth momentum remains steady reflected in buoyant performance of most high frequency indicators. PMIs, digital spending, GST collections, 2W and 4W registrations, power demand, railway goods movement, etc. grew at a robust pace. Furthermore, rebound was visible in tractor sales and unemployment eased from the peak. However, some moderation was visible in CV sales.

Indicators	Units	Apr-23	May-23	Jun-23	Jul-23	Aug-23	Sep-23	Oct-23	Nov-23	Dec-23	Jan-24
Retail registration - Auto@											
2W	YoY, %	-7.0	9.6	7.1	8.5	6.6	21.9	-12.6	21.5	27.5	15.0
PV	YoY, %	0.6	6.3	6.6	5.7	8.3	19.0	-2.0	19.7	2.1	13.3
MHCV	YoY, %	10.3	11.0	0.9	5.4	8.1	7.7	17.9	-2.0	-0.4	-1.0
LCV	YoY, %	-4.4	2.4	-4.7	-5.4	-1.3	-3.3	2.4	-9.1	-4.4	-6.4
Tractors	YoY, %	1.8	10.3	43.1	25.1	16.5	-7.3	3.5	-22.3	1.4	24.0
Gross GST Collection	YoY, %	11.6	11.5	11.7	10.8	10.8	10.2	13.4	15.1	10.3	10.4
Average E-Way bill generated	YoY, %	12.2	19.7	15.5	16.4	19.5	9.5	30.5	8.5	13.2	NA
Power demand	YoY, %	-1.8	-0.4	4.3	8.0	16.3	10.3	20.9	6.1	1.6	6.1
Digital Spending&	YoY, %	35.0	34.9	34.2	35.7	37.7	32.8	34.4	38.3	35.3	35.5
Railway Freight Tonnage	YoY, %	3.5	1.9	-1.9	1.5	6.4	6.8	8.5	4.3	6.4	6.4
Railway Freight Earnings	YoY, %	6.8	4.0	-1.0	3.2	2.7	5.1	6.6	3.8	3.6	4.1
Manufacturing PMI^	Index	57.2	58.7	57.8	57.7	58.6	57.5	55.5	56.0	54.9	56.5
Services PMI^	Index	62.0	61.2	58.5	62.3	60.1	61.0	58.4	56.9	59.0	61.8
Unemployment	%	8.5	7.6	8.5	7.9	8.1	7.0	9.4	8.9	8.7	6.8

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

India's growth trajectory is expected to be stable supported by strong industrial as well as services activity and consumption. Nevertheless, the adverse impact of spatial and temporal distribution of the monsoon on crop yields could potentially dampen rural consumption.

Retail inflation flat, likely to inch lower in the near term: CPI remained largely unchanged in December 2023 as the impact of higher food inflation was offset by lower core inflation. Food inflation picked up with an increase in vegetable prices along with elevated cereal, fruits, pulses and spices inflation. However, core inflation moderated on the back of a favourable base and continuing soft momentum. The correction in commodity prices over the past few months is keeping the input price pressure under check.

The prices of key vegetables like tomato, onion, potatoes, etc. have moderated in recent months and are likely to push headline inflation lower. Core inflation is likely to remain rangebound as momentum remains subdued. Thus, overall inflation is expected to ease in the coming months.

YoY, %	Nov-23	Dec-23	Change in %
CPI	5.6	5.7	0.1
Food & Beverages	8.0	8.7	0.7
Fuel and Light	-0.8	-1.0	-0.2
Housing	3.6	3.6	0.1
Transportation & communication	2.1	2.0	-0.1
Core CPI@	4.8	4.3	-0.5

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

Trade Deficit eases, likely to remain rangebound in the near term: Trade deficit narrowed sequentially in December 2023 driven by an improvement in net NONG imports. This was partially offset by higher net oil and gold imports. The reduction in NONG deficit was led by an increase in exports of engineering goods, chemicals, rice and garments. This was partly counterbalanced by higher imports of electronics goods, machinery, fertilisers, etc.

The Q4 of the financial year is a seasonally strong quarter for exports in India, thus, the trade deficit should narrow in coming months. However, given the rise in shipping time due to the Red Sea conflict, India's exports to select geographies especially Europe, might get impacted.

Amount in USD billion	Nov-23	Dec-23	Change
Trade Deficit / (Surplus)	20.6	19.8	-3.8%
Net Oil Imports	7.5	8.1	8.2%
Net Gold^ Imports	2.1	2.5	15.7%
NONG* net imports	11.0	9.3	-15.7%

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

Commodity prices: Most industrial commodity prices remained subdued during the month as China's growth continued to surprise on the downside. The risk of escalation in the Red Sea crisis led to oil prices rising during the month.

	Market price (USD)*	Jan-24^ (%)	FYTD24& (%)
Brent Crude (per barrel)	81.7	6.1	2.4
Gold (per ounce)	2,040	(1.1)	3.6
Steel (per tonne)	570	0.9	(13.0)
Zinc (per tonne)	2,552	(3.4)	(12.2)
Copper (per tonne)	8,513	0.4	(4.7)
Aluminium (per tonne)	2,241	(4.4)	(5.7)
Lead (per tonne)	2,173	7.0	1.3

Source: Bloomberg; *Market prices as on January 31, 2024. ^M-o-M change. & - change during FY24

HDFC MUTUAL FUND
BHAROSA APNO KA

Macroeconomic Update (contd...)

Summary and Conclusion:

Global growth momentum witnessed a divergent trend with the US economic activity beating expectations while Europe and China surprised on the downside. Given healthy growth in the US and easing inflation, the narrative of "soft landing" is increasingly becoming consensus. Eurozone economic activity remains subdued with weak PMIs, low consumer confidence and a tight monetary policy. Chinese economic recovery remains fragile with real estate woes weighing on growth.

India's growth momentum is holding steady and is poised to continue, driven by urban consumption and a resilient industrial and services sector. However, there are risks to this outlook, particularly the potential impact of erratic rainfall patterns on Kharif crop yields, which could disrupt rural recovery efforts. Investment activity is being supported by both central and state governments, with front-loaded capital expenditure spending, while household real estate activity continues to show resilience. Although private capital expenditure remains somewhat subdued, there is potential for it to pick up given conducive conditions such as low leverage, increasing capacity utilization, steady corporate profitability, and the robust balance sheet of the banking sector. The external sector is comfortably placed, with expectations for an improved year-on-year current account performance and the Balance of Payments (BoP) likely to remain in surplus.

Looking ahead over the medium term, outlook for the Indian economy remains optimistic. This is driven by several factors, including the favourable policy environment, the positive effects of Production-Linked Incentive (PLI) schemes, opportunities arising from the global supply chain's shift, the government's emphasis on infrastructure spending, the potential for a recovery in private sector capital expenditure, and the resilience of personal consumption, among others.

HDFC MUTUAL FUND
BHAROSA APNO KA

Equity Market Update

After two consecutive months of gains, the Nifty / S&P BSE Sensex closed almost flat in January 2024. Midcap and Smallcap index outperformed the large cap benchmarks. Key events and factors included escalating tensions in the Middle East, diminishing likelihood of a US recession, the NSO projecting India's GDP growth for FY24 at 7.3%, surpassing consensus expectations, among others. Sector indices exhibited a mixed performance, with strong gains in Oil & Gas, Power, Healthcare, and Auto, while Banking, FMCG, and Metal underperformed.

Global market performance was varied, with month-on-month gains seen in Japanese, US, and European indices, while Chinese and Korean markets underperformed. The tables below provide details of performance of key domestic and global indices.

% Change in Indices	Jan-24	FYTD24^
S&P BSE India Auto	4.2	55.8
S&P BSE India Bankex	(4.4)	13.0
S&P BSE India Capital Goods	1.9	64.9
S&P BSE India FMCG	(2.8)	20.7
S&P BSE India Healthcare	7.2	54.5
S&P BSE India Metal	(0.9)	39.5
S&P BSE India Power	8.6	75.2
S&P BSE India Oil & Gas	12.6	49.1
S&P BSE India IT	3.7	31.2
S&P BSE SENSEX	(0.7)	**21.6**
NIFTY 50	(0.0)	**25.1**
NIFTY Midcap 100	5.2	**61.7**
NIFTY Smallcap	5.8	**78.2**

% Change	Jan-24	FYTD24^
S&P 500	1.6	17.9
Nasdaq	1.0	24.1
FTSE	(1.3)	(0.0)
DAX	0.9	8.2
CAC	1.5	4.6
Nikkei	8.4	29.4
Hang Seng	(9.2)	(24.1)
KOSPI	(6.0)	0.8
Shanghai	(6.3)	(14.8)
MSCI Emerging Market Index	(4.7)	(1.5)

Source: Bloomberg; ^ - Returns in FY24

FPIs sold equities worth USD 3.1 billion in January 2024 as opposed to net purchase of USD 7.9 billion in December 2023. FPIs have bought equities worth USD 20.8 billion in 10MFY24 (10MFY23: USD -5.4 billion). DIIs, on the other hand, bought net equity worth USD 3.3 billion in January 2024 (December 2023: USD 1.6 billion) and have cumulatively bought equity worth USD 15.5 billion in 10MFY24 (10MFY23: USD 26.1 billion).

Flows to mutual funds (MF) increased to ~INR 24,800 crore in December 2023 compared to ~INR 21,700 crores a month before. Cumulatively, MF flows in equity-oriented schemes in 9MFY24 stood at ~INR 158,000 crores.

Of the Q2FY24 results declared so far, earnings of Banks, IT, Cement and Pharma sectors were better than expected while that of NBFCs, Metals, Oil & Gas, Capital goods, Consumer staples and durables were in line with expectations. Results of Logistics and Chemicals were lower than expected.

Outlook

As on January 31, 2024, NIFTY 50 was trading at ~18x FY26E price to earnings multiple. Further, Market cap-to-GDP stood over 100% (based on CY25 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)*]. In general, current valuation indicators are at premium to their historical averages. However, one should view these valuations in the context of structurally attractive nominal GDP growth, a healthy corporate earnings outlook and robust de-levered corporate and banking balance sheets.

Chart 1

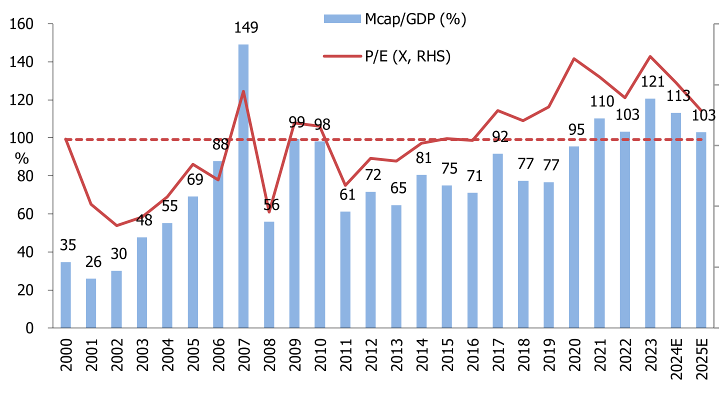
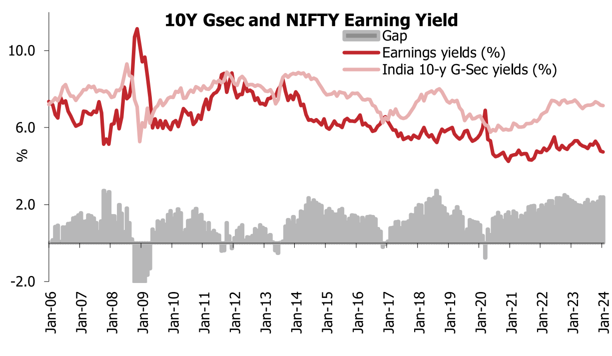


Chart 2



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

HDFC MUTUAL FUND
BHAROSA APNO KA

Equity Market Update (contd...)

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

	12 months forward Price to Earnings		
	31-Jan-24	**LTA**	**Discount/Premium^**
Electric Utilities	16.9	12.2	38.6
Consumer Discretionary	59.0	43.1	36.7
IT Services	25.7	19.0	35.3
Consumer staples	39.6	31.6	25.5
Pharma	27.5	22.0	24.8
Oil and gas$	13.9	11.6	20.3
Auto	20.2	16.9	19.3
Metals	11.7	10.1	15.6
PSU Banks@	1.3	1.2	11.0
Private Banks@	2.3	2.4	-5.6

Source: Kotak Institutional Equities. Stocks are part of Kotak Institutional Equities universe. $-Oil & Gas sector PE is high mainly due to one company. Excluding that, the multiple is 7.2x vs 15-year average multiple of 8.7x.
LTA – 15 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 sharp broad-based rally in the current financial year has resulted in small cap and mid cap indices significantly outperforming and they now trade at a noteworthy premium to their long-term average valuation. Given the aggregate valuation being higher than historical average, the importance of stock selection increases even more.

We maintain a positive outlook on equities for the medium-to-long term, 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, and a resurgence of inflation either globally or domestically.

HDFC MUTUAL FUND
BHAROSA APNO KA

Debt Market Update

Gsec yields moderated during the month with 10Y Gsec yield ending at 7.14%, 3 bps lower compared to end-December 2023. The yield at the short end remained at elevated levels due to tight liquidity, thus flattening the curve further. The key factors and events which influenced the fixed income markets included consistent buying of Gsecs by FIIs, a benign domestic CPI, rise in oil prices and strong US economic activity. Corporate bond spreads over Gsec remained largely unchanged during the month. The table below gives a summary view of the movement of key rates and liquidity:

	Dec-23	Jan-24	Change (%)
MIBOR Overnight Rate (%)	6.90	6.85	-0.05
3M Gsec yield (%)	6.93	7.04	0.11
1Y G-sec Yield (%)	7.09	7.09	-
10Yr Benchmark G-Sec Yield^ (%)	7.17	7.14	-0.03
AAA 10Year Corporate Bond Yields#, & (%)	7.65	7.63	-0.02
AAA 10Y Corporate bond spread against 10Y benchmark@ (bps)	48	49	1
Average net liquidity absorbed/infused by RBI* (INR billion)	-1,208	-2,073	NA

NA – not applicable. ^-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 fell month on month driven by rise in currency in circulation and elevated government balances. This kept overnight rate close to upper end of RBI's policy corridor.

FPIs bought (including Voluntary retention route) debt worth USD 2.3 billion in January 2024 (December 2023: USD 1.7 billion). Cumulatively, FPIs have bought debt worth USD 9.5 billion in 10MFY24 (10MFY23: outflow of USD 0.1 billion).

On February 1, 2024, in its interim budget central government announced fiscal deficit and market borrowings for FY25 which was lower than market expectations. Further, it reiterated its commitment to bring down fiscal deficit below 4.5% by FY26. These resulted in broad based rally in yields.

Outlook

The outlook for fixed income remains favourable over the medium term in view of the following key drivers:

- The lower-than-expected budget deficit and market borrowings are a significant positive because of improved demand-supply balance as demand is likely to remain robust in FY25 due to India's inclusion in the JP Morgan bond index.
- Core CPI momentum remains subdued driven by lower input price pressure and benign global commodity prices. Inflation expectations also remain well anchored and are trending lower.
- Major global central banks, especially the US Fed, have indicated the end of the rate hiking cycle and are likely to start easing in due course.
- RBI is also expected to follow soon by easing liquidity and eventually reducing the policy rate in coming quarters. It will also get more confidence due to the commitment to fiscal consolidation outlined by the government.
- India's external sector vulnerability remains low due to high foreign exchange reserves, rangebound oil prices, robust services exports and the likelihood of FPI inflows into the debt markets in FY25.

However, there are following risks to the favourable outlook.

- SLR holdings of the banking system are high and credit growth is robust. With interbank liquidity in deficit, the incremental demand for G-Secs is likely to remain muted.
- Regular food price shocks can keep headline CPI elevated and can adversely impact inflation expectations.
- Escalation of geopolitical tensions can impact exports as well as increase oil prices.
- Continuation of tight monetary policy for a period longer than expected can result in global yields rising.

Overall, in our view, yields are likely to trade with a downward bias and the long end is likely to outperform over the medium term. While we continue to recommend investments in short to medium duration debt funds, investors could consider a higher allocation to longer duration funds, in line with individual risk appetite.

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

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
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
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

DISCLAIMER