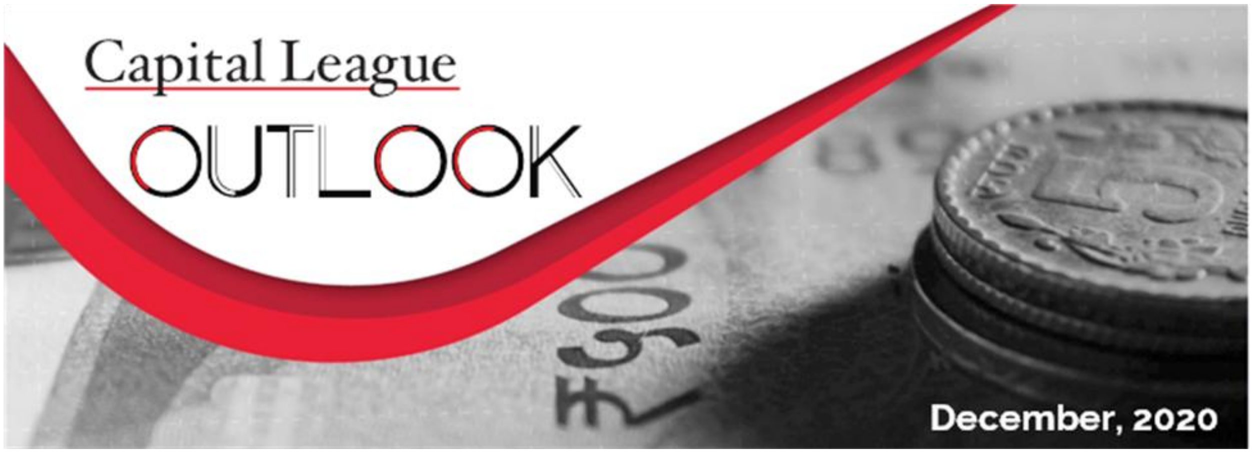
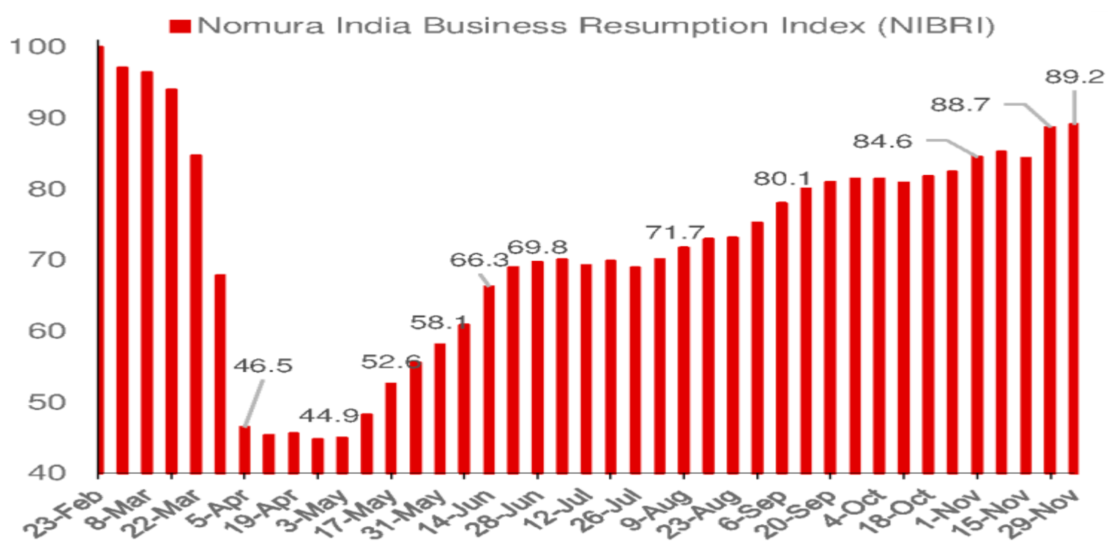


Indian Economy

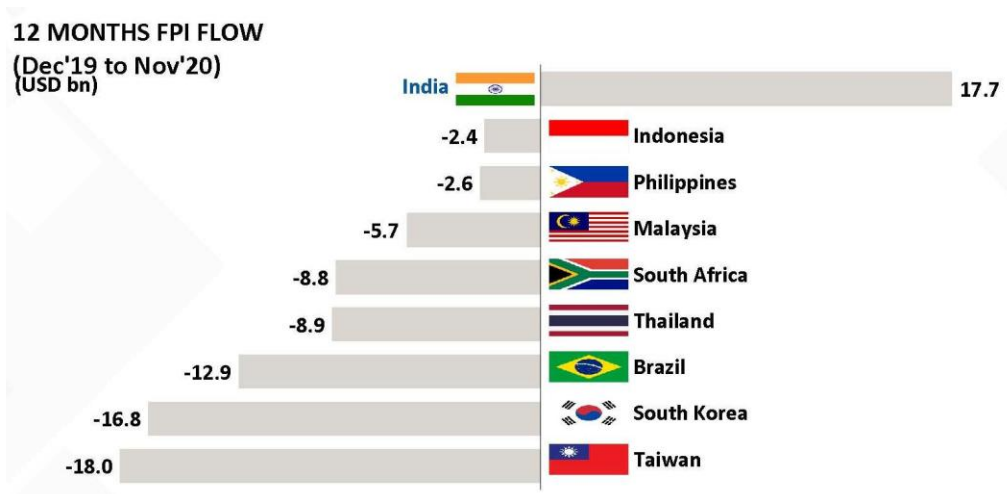
- India's GDP saw the fastest sequential growth among large economies in September quarter. Q2 GDP contracted 7.5% (Lower than analyst expectations) led by growth of 0.6% in manufacturing and 4.4% in electricity.
- Rural India continues to do well supported by good agriculture and government spending.
- GST numbers sustained above the INR 1 Lac Cr mark for the second month in a row. Economic activity has reached nearly 95% of pre-Covid level.
- The Business Resumption Index shows continued business recovery



- The Finance Minister announced Atmanirbhar 3.0 - focus remained on supply-side reforms, including a temporary wage subsidy program to buffer unemployment, efforts to enhance and extend the credit guarantee scheme, more production-linked incentives to attract multi-national companies to relocate to India, and more resources to bolster infrastructure and housing.
- Earnings season was a welcome positive as Q2 FY21 PBT for stocks under coverage beat consensus estimates. Cyclical like Finance, Auto & Auto Ancillaries, Consumer Discretionary & Cement, saw strong results. Even traditional defensives like IT & Healthcare saw strong results on the back of renewed demand for products and services across key export markets.

Consumer Durables companies pointed to strong festive demand in their management commentary.

- The key feature of the results was the focus on cost mitigation measures, apart from demand recovery and a healthy tailwind from gross margin expansion.
  - Nifty's - 31 companies out of 50 reported numbers above expectations.
  - EBITDA grew 8% YoY (vs est.-0.3%)
  - PAT increased 17% YoY (vs est. – 5%)
- Corporate India has seen first earnings upgrade after 23 quarters of downgrade. Corporate earnings are expected to rebound in FY22 and show strong growth in FY 23 as well.
- Post US elections and the vaccine announcements, the flows to Emerging Markets have jumped manifold. India has received over USD 8 Bn in November'20, the highest ever monthly flow.
- Combination of increasing flows to Emerging Markets, India's increased weightage in MSCI Emerging Market Index, strong economic recovery, better than expected pace of government reforms and better corporate results have all resulted into India receiving one of the highest FPIs (Foreign Portfolio Investment) in the last 12 months.



Source: Axis Capital

- Strong equity market inflows have resulted in a broad based rally. Approx. 91% of the stocks in BSE 200 have risen in Nov'20.
- **RBI** kept repo rate unchanged at 4% in December and guided for continuation of the accommodative stance at least into the next financial year. In an exceptional year like this, the central bank has prioritized growth concerns over inflation.

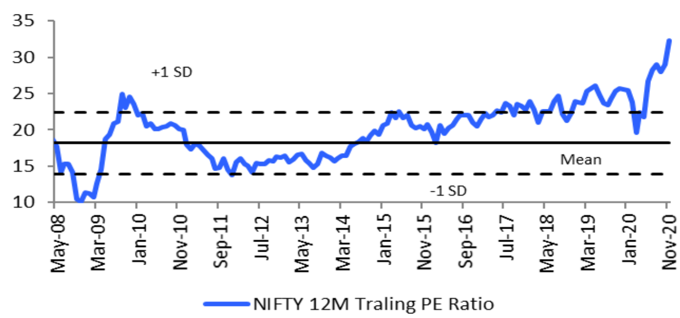
Global Economy

- Broad global recovery continues to play out. Though, tighter restrictions in response to increase in new cases in the US, Germany & US will lead to some moderation in activity.
- China and Japan are both showing strong economic data.
- **Federal Reserve's** balance sheet has tripled over the past 10 years and has crossed USD 7 Tn. They have kept key interest rates near zero in their latest policy meeting.

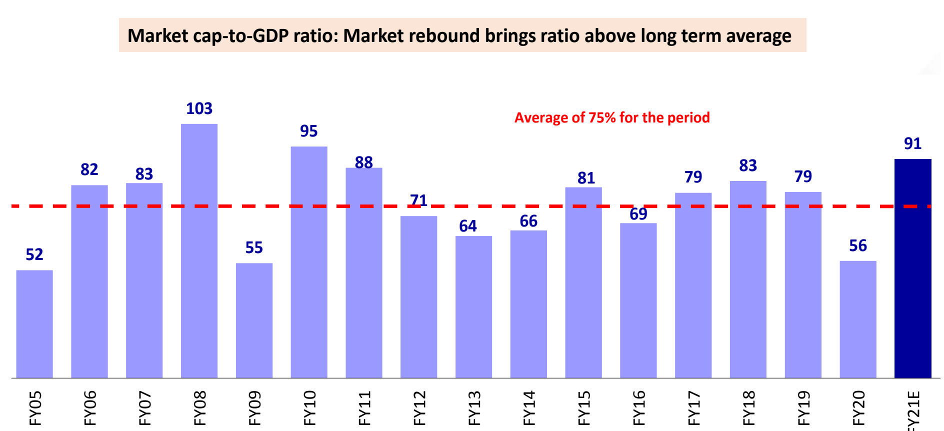
- **Gold:** Successful trials and release of various COVID-19 vaccines and the US elections explain the correction in gold prices.
- Gold yields no interest or dividends. But if bonds pay interest that doesn't even keep up with inflation, bullion looks increasingly attractive. Gold has a history of maintaining its purchasing power over long periods. Continued near zero interest rates in the US and a weaker Dollar as a result of massive printing keep the outlook for Gold positive from a medium term point of view.

Outlook

- Indian stocks were aided by better-than-expected corporate earnings as margin expansion resulted in double digit profit growth, comfortably offsetting the decline in revenues. Cost rationalization and demand normalization are at play. Also providing support were earnings upgrades that continue at an unprecedented pace as activity continues to normalize.
- Nifty 12M trailing PE ratio increased from 29 in Oct'20 to 32.3 in Nov'20.



- **Market Cap to GDP ratio** at 91 has crossed 90 after a span of 10 years and is now above its long term average. However, both the numerator (Market cap going up) and the denominator (negative GDP growth in the current year) have played a role.



- Valuation attractiveness has receded with trailing P/E multiples and Market Cap/ GDP ratios having crossed historical means. Hence, continued returns from equities will depend on sustained earnings recovery and foreign flows.
- Looking ahead, after the strong bounce back from March 2020 lows, it will likely take a strong growth and earnings cycle beyond the reopening led normalization for further upsides. That said, broader markets continue to appear much better placed relative to large caps.

- On the **fixed income** front, short term interest rates have fallen substantially on account of abundant liquidity of approx. INR 6 Lac Cr in the system. RBI has promised to keep rates low as long as required. Since much of the gains from capital appreciation are already in the returns, 2021 is not expected to be as good as 2020. Investors should be prepared for lower returns in the range of 4-5.5%.
- We recommend medium term funds, over and above short term, corporate bond and Banking & PSU funds, where the fund manager has some flexibility to play with duration and paper quality to give enhanced returns.