Capital League outlook

May 2018

Indian Economy

- Increasing number of high frequency indicators are pointing to economic growth. Rise in construction, manufacturing activities, cement production, sale of commercial and passenger vehicles, air traffic and higher rural wages indicate pick up in growth momentum.
- Corporate profits for the 4Q FY18 have remained lacklustre. The Automobile, FMCG and Retail banks have reported good quarterly numbers. However, the profit of Corporate focused banks have missed estimates.
- India Nikkei Services Purchasing Managers' Index (PMI) rose to a three-month high of 51.4 in April from 50.3 in March. While the outbound shipments of goods are languishing, services exports are posting double digit growths.
- NPA resolutions for RBI's first list of defaulters are in the final stages. Stressed accounts in the second list have also been referred to the National Company Law Tribunal (NCLT) in January, and are likely to be admitted soon. NCLT has approved Tata Steel bid for Bhushan Steel Limited, clearing the deck for the bankrupt mill's acquisition.
- Rising oil prices are seen impacting India's current account deficit, since the country is a large importer of oil. This has led to depreciation of INR to a 15-month low against the US dollar (>68).
- Retail inflation rose to 4.58% in Mar'18 as compared to 4.28 % in Feb'18. It may rise further due to expected rise in MSP in FY19, higher import duties on host of food items (oilseeds, sugar, pulses, wheat) and rising crude oil prices.
- Rising crude prices, increasing global interest rates, depreciating Rupee has added to the volatility in the G-sec yield. 10-year yield has crossed 7.8%.
- RBI has announced liquidity injection through purchase of government bonds. Increase in Foreign Portfolio Investment (FPI) limits and relaxing tenor restrictions for FPI investments by the RBI can encourage wider participation by FPIs in debt market.

Global Economy

- United States has announced re-imposition of sanctions on Iran for its oil exports, shipping, port operators, central bank dealings, insurance and curbs on Iran's purchase or acquisition of US dollars, as well as any global trading in Iran's gold, coal, steel, cars, currency and debt.

- The European Union has started to activate measures to preserve the Iran nuclear agreement and to protect EU companies operating in the country.
- Higher commodities prices had raised concerns about inflation in US. The 10-year US treasury yield has touched 3%. Foreign investors' position in emerging market (EM) assets has turned more guarded and consequently, EM currencies in general are witnessing pressure.
- BoE maintained its key interest rate at 0.5% and quantitative easing as it forecasts slower economic growth and inflation than its previous projections.

Outlook

- Valuation-wise, the Indian equity market is expensive and corporate earnings recovery would be critical at this juncture. The Sensex is trading at 17.86X its expected earnings for the FY19.
- Contrasting macro and micro economic data, lower FII flows, strong domestic flows, global and domestic political developments will continue to create volatility in the equity market. Investors are recommended to maintain/rebalance their asset allocation.
- Investment in equities should be done in staggered manner and intermittent volatility to be used to increase equity exposure.
- Policy rate is expected to remain unchanged in near term.
- However RBI may act in case of

  a) government's policy measures in the run-up to 2019 general election and its impact on inflation thereof

  b) growth improving faster than our current expectations,

  c) global monetary policy normalization
- In debt, investors should look to invest in accrual funds and short duration funds for better yields. FMPs are also recommended to lock-in high yields.