Capital League outlook

July 2016

Indian Economy

- The government has eased FDI norms allowing 100% inflows in civil aviation, broadcasting carriage services such as cable networks, DTH and mobile TV and food processing sectors. It has also eased norms in defence and pharmaceuticals.
- New civil aviation policy has been cleared with a new formula for international operations and enhancing regional connectivity.
- Consumption demand from both rural and urban sectors is expected to pick up as the monsoon has picked up and covered the entire country and the Seventh Pay Commission payout has been approved by the cabinet.
- Industrial output growth measured by IIP rose to 1.2% in May’16 as compared to -0.8% in Apr’16 due to slight improvement in manufacturing.
- Exports rose in June’16 after 18 months by 1.27% as compared to -0.8% in May’16. The trade deficit has widened to USD 8.1 Bn in June’16 as compared to 6.27% in May’16 per month. However for the Q1 FY16-17 the cumulative trade deficit is substantially lower at USD 19.23 Bn down from USD 32.22 Bn during the same quarter last year.
- Retail inflation (CPI) came to 5.77% in June’16, a notch higher than 5.76% in May’16 due to rise in food prices.
- Liquidity conditions have improved helped by increased government expenditure hence causing reduction in centre’s cash balance with RBI. Open market operations (OMOs) of approximately INR 800 Bn have been conducted by the RBI to infuse liquidity. This has resulted in easing of money market rates which has in turn led to considerable easing in the short term rates as well.

Global Economy

- UK decided to leave the European Union (‘BREXIT’) based on the outcome of a referendum (public vote) conducted on 23rd of June. Global equity markets reacted sharply the day after the referendum and the British pound also fell to its lowest level in over three decades. However, the stability was restored within a week and equity market recouped the losses primarily due to hopes of further monetary and fiscal stimulus by global central banks & economies.

- The medium term impact of BREXIT, if any, will be clear only post the revised terms of trade between UK and EU are finalized over the next two years.
- The outlook for global commodity prices have been revised upward for base metals, coal, oil and precious metals as the demand is expected to outweigh supplies. Over last six months, the commodities have recovered sharply:

Commodity	% change in price YTD
Aluminium (USD/tonne)	9.65
Copper (USD/tonne)	0.94
Zinc (USD/tonne)	34.38
Brent crude (USD/BBL)	23.97
Silver (USD/oz)	46.45
Gold (USD/oz)	27.69

- Over one third of developed world government debt amounting to USD 10 Tn are carrying zero or negative yields; hence investors are looking for income elsewhere, which is further pulling down rates in longer maturity bonds, emerging markets and riskier corporate debt.

Outlook

- In line with the global markets, Indian stock markets are up nearly 8-9% over the last 3 months. As a result, Sensex is currently trading at ~18 times FY17 earning.
- We continue to recommend investment in equities in a staggered manner in a mix of diversified funds with 3-5 years horizon.
- Both Domestic Factors (certainty of good monsoon, passage of GST) and Global Factors (BREXIT leading to reduced Fed rate hike expectation and drop in global bond yields) will aid fall in bond yields further resulting in attractive returns across the debt funds.