

Indian Economy

- The Government is showing strong commitment for meeting deadline for GST implementation. It is considering advancing of the winter session of Parliament to pass the Central and Integrated GST Bills.
- Real GDP growth came at 7.1% y-o-y in Q1 FY17 led by sustained consumption demand and reduced trade deficit. This reaffirms India's position as the world's fastest-growing major economy.
- The Nikkei India Manufacturing Purchasing Managers' Index (PMI) has climbed to a 13-month high of 52.6 in August from 51.8 in July which indicates economic expansion. The Nikkei India Services PMI also rose to 54.7 in August from 51.9 in July. New business was the main driver of activity growth.
- Retail inflation (CPI) came down to 5.05% in Aug'16 as compared to 6.07% in July'16, mainly due to slowing rise of food prices. This may create headroom for RBI to cut rates in its forthcoming monetary policy.
- Monsoon rainfall has been favorable this year with only 4% below normal range. So kharif harvest is expected to rise by 9% over last year's output, which may result in lower food inflation and higher farm income after two successive drought years.
- The Current account deficit for the Apr – Jun'16 Qtr has declined sharply to the tune of USD 0.3 Bn or 0.1% of GDP. This is due to continued drop in gold imports & lower oil import bill.
- FII inflows have been positive for Aug'16 to the tune of USD 1.4 Bn in Indian equities. However, while the future FII flows will be dictated by the global developments, the DIIs and retail investors will continue to remain net buyers driven by structural reasons like regulatory changes, rising disposable incomes and lower returns in other asset classes.
- In a global environment wherein sovereign debt is trading at negative yields, and quantitative easing by some central banks (European Central Bank, Japan) is continuing, the availability of high positive real yields on Indian sovereign bonds is attractive to foreign investors.

Global Economy

- The US Fed has kept the rates unchanged in this month's meeting. However, it has hinted that the case for raising interest rates has strengthened in light of a good job market and an improved outlook for the U.S. economy and inflation.

- Bank of Japan kept its deposit rate unchanged at negative 0.1%, but introduced a new policy of targeting the yield curve. It also maintained its stimulus program of buying long-term Japanese government bond.
- Despite recent concerns on bonds scarcity, the European Central Bank have kept all policy rates and parameters of the quantitative easing program unchanged in its Sep'16 meeting.
- China's economic growth has continued to stabilize with industrial production growth picking up from 6.0% to 6.3% in August and import growth recording its first positive y-o-y growth of 1.5% since November 2014.
- Globally energy prices have been broadly stable but metal prices have risen. Precious metals saw maximum rise as investors look for safe haven post BREXIT.

Outlook

- The 10 year benchmark G-Sec yield has come down to 6.96% from a high of 8.8% in December 2013. Despite this large fall in yields, there is further downside bias for bond yields because of expectation of more rate cuts by RBI, high real yields (approx. 1.0% to 2.6%), low level of core inflation, expectation of decline in inflation post monsoon, continuing weak IIP and strong capital inflows from debt FPIs. Hence, we recommend investors to remain invested in duration based funds.
- Markets have already priced in the optimism on Indian growth and consequently earnings and current valuations look rich in certain stocks and sectors. This has induced domestic fund managers to turn cautious and may lead to short term volatility. Valuations are at an above average forward PE of 18x FY17 consensus earnings.
- Improving fundamentals of the Indian economy and attractive market cap/GDP lead to a positive outlook for the equity markets over the medium to long term. Any volatility in Indian equities induced by global events will be a good opportunity for investment.