Capital League outlook

October 2016

Indian Economy

- The Reserve Bank of India cut its benchmark repo rate by 25 basis points to 6.25%. There is change in the stance of monetary policy, (a) on the timeframe to reach the 4% inflation target (March 2018 earlier), (b) the targeted real rate of return has been shifted lower from 1.5% to 1.25%.
- The monetary policy committee expects supply management measures would further bring down food inflation and the RBI maintains their targeted CPI at 5% by March 2017 and at 4% over the next 5 years.
- Indian bond market has rallied by almost 100 bps, year-to-date on the back of easing global yields, easing of domestic liquidity conditions and market expectations of more rate cuts.
- Retail inflation (CPI) eased to 4.31% in Sep'16 as compared to 5.05% in Aug'16. However, economists had expressed concern that prices could rise quickly after a pay hike for millions of government employees and pensioners.
- Index of Industrial Production contracted to -0.7% in Aug'16 as compared to -2.44% in July'16 due to continued fall in mining and capital goods.
- Exports grew by 4.62% in September while Imports continued to decline by 2.5% resulting in trade deficit of USD 8.33 Bn, the highest in last nine months. The growth in exports is on account of healthy growth in sectors such as Engineering and Gems and Jewellery.
- Net profit and Sales for Nifty 50 companies is expected to grow by approx. 6% and 3% respectively during Q2, FY17, the highest level in last eight quarters. The earnings performance will be driven by domestic cyclicals like Automobiles, Consumer Sector, select Private Sector Banks and NBFCs.
- Emerging-market equities including India have outperformed their developed-market peers as improving fundamentals and higher yields drove fund flows into emerging markets.

Market	**% change from 31st Dec'15 to 19th Oct'16 in USD terms**
United States (DJIA)	+4.5
Britain (FTSE 100)	-6.2
China (SSEA)	-16.0
Japan (Nikkei 225)	+4.0
Euro Area (FTSE Euro 100)	-3.8
Brazil (BVSP)	+82.9
India (BSE)	*+6.3*
Emerging markets (MSCI)	*+15.0*

- The GST council comprising of Centre and the states failed to reach any consensus on the tax structure in their last meeting. The council will meet again in Nov'16.

Global Economy

- The yield on US Government 10-year bond has reached 1.79%, the highest level for the past five months. This will raise the long term interest rates which could have negative implication for risky assets as emerging market equities.
- Oil prices have increased to nearly USD 52 per barrel this month with the weakening of USD and expectations of OPEC output curbs.
- Chinese economy grew 6.7% in the last quarter compared with a year ago which is in line with the estimates. However, the exports have declined 10% in Sep'16 on y-o-y basis. The Chinese economy is slowly transforming to a greater reliance on consumption than on manufacturing.
- British Parliament will "very likely" have to ratify an eventual agreement with EU over Brexit. This has helped the British pound to gain. The falling pound has sparked fears that Britain could be heading for a period of higher inflation as the price of imported goods begins to rise.

Outlook

- Consumption demand is expected to improve with the payment of first tranche of pay-commission stimulus and as rural economy receives their Kharif income in October and November. Public sector capex is also pacing up. Hence, we expect a gradual pick-up in sales volume growth for corporates.
- Low raw-material cost vis-à-vis sales, falling interest expense and low base from last year will aid the corporate profitability in next 2-3 quarters. We expect earnings to improve by 12-13% in FY17.
- The current valuations at ~18 times FY17 earnings are at a premium to the historical average.
- US elections and possibility of a FED rate hike are two events likely to keep the equity and bond markets on edge. We continue to advise investment on dips or in a staggered manner.
- For debt allocation, a mix of short term, credit oriented funds and duration funds should continue to do well.