MARKET UPDATE

Alok Singh
HEAD - INVESTMENTS

All the major global economies have seen some amount of growth coming back, it is expected that the global recovery may gain more momentum in 2017 on the back of faster US growth, stable DM (Developed Market) growth and rebounding EM (Emerging Market) momentum. India is expected to lead the EM pack with GDP growth over 7%. This improved growth outlook led to the global portfolio increasing their allocation to emerging markets and Indian markets were also the beneficiaries of the same. The foreign flow into the economy at the time when India had witnessed continued improvement in its macro-economic fundamentals resulted in appreciation in the INR against all the major currencies. INR has performed very well amongst its EM peers. It should be noted that some of the EM currencies (Brazil, South Africa & Russia) have appreciated only on back of the rise in commodity. The INR shall continue to have much lower volatility than experienced by other EM currencies reflecting improving fundamentals and progress in reducing its external vulnerabilities

The April 5-6 policy meeting minutes reiterated MPC's (Monetary Policy Committee) concerns on upside risk to inflation. While the sticky behaviour of core inflation and possible mean reversion of food inflation remain key concerns, most committee members remain watchful of second round impact of 7CPC HRA increases. There were two strong and contrasting views on inflation. On one hand, Dr Patra sounded extremely hawkish on inflation risks and even called for a pre-emptive 25 bps rate hike to avoid the need for back-loaded policy action later. On the other hand, Dr Dholakia sounded dovish as he deviated significantly from the RBI's inflation forecast and noted comfortable inflation dynamics (including core) through FY2018. The bond market reacted negatively to this has witnessed rise in yield across the yield curve with 10 year GOI bond yield reverting closer to 7%. Though around 7% bond yields are attractive from the valuation perspective, since they are offering over 150bps of real positive rate of return, but the demand supply dynamics doesn't paint a comforting picture.

The IMD (India Meteorological Department) forecasts the June-September monsoon at 96% of LPA, which qualifies as 'normal' southwest monsoons. The IMD noted that weak El Niño conditions could likely develop in the latter half of the season. It sees 38% probability of near-normal monsoon. The normal monsoon may help in containing the inflation expectations in the economy and may sustain the consumption indicators which have started to normalize, as the effect of the currency replacement is now waning. However, Capex indicators have remained subdued, as robust growth in public capex has been more than offset by continued weakness in private capex. Urban consumption recovering quickly, rural demand normalizing. Passenger vehicle sales, a proxy for urban discretionary consumption, continued to grow at a robust level in Feb after rebounding to double-digit growth in Jan. Two-wheeler sales, a proxy for rural demand, improved in Feb as sales remained flat on a YoY basis, after three months of contraction.

Topline growth has started to trend up and we expect this to pick up pace further in the next couple of quarters as demonetization vows are behind us. External demand has also shown strength and this will likely create positive spillovers for domestic demand recovery, as it tends to influence trends in industrial production and corporate sales growth. As a result we expect equity market to remain positive in coming months.

Source: Bloomberg, RBI (Unless indicated otherwise)