Debt Market Commentary

Indiabulls
MUTUAL FUND

January 2017

31st January	Month Opening	Intra Month High	Intra Month Low	Month Closing
Overnight Rate (NSE MIBOR)	6.21	6.25	6.15	6.25
10 year Gsec	6.40	6.47	6.36	6.41
3 month CDs	6.30	6.40	6.30	6.35
6M CDs	6.45	6.48	6.45	6.45
12 month CDs	6.50	6.50	6.50	6.50
Currency	68.23	68.33	67.87	67.87
10 Year US Treasury	2.45	2.53	2.33	2.45

Inflation

Retail inflation as measured by CPI (consumer price index) for December 2016 dipped by more than 20 bps and came at 3.41% as compared to 3.63% of November. With this dip, CPI is now at 25 months low. Steep fall in food prices caused such a sharp fall in inflation. According to Consumer Price Index (CPI) data released by the Central Statistics Office (CSO), among the CPI components, inflation of food and beverages declined to 1.98% in December 2016 from 2.56% in November 2016. The Wholesale Price Index (WPI)-based inflation eased for the third straight month to 3.2% in November 2016 from 3.4% in October 2016. The Wholesale Price Index (WPI)-based inflation for December reversed the earlier easing trend and rose to 3.39% from 3.15% in November, with rising prices of petrol and diesel. December WPI rise is in contrast to a fall in the Consumer Price Index (CPI) for the month. The index composition is the reason for divergence. WPI has a higher food and manufacturing composition and hence, is rising due to increase in global crude oil prices. CPI has a greater composition of food, which has been facing downward trend.

Macros

India's trade deficit narrowed to approx $10.37 billion as compared to $13 billion in November 2016. Exports rose 5.72 %t YoY to $23.88 billion, imports remained flat at $34.25 billion, leading to a sharp fall in trade deficit. Gold imports dropped to $1.95 billion, in November, gold imports spurted to $4.36 billion $3.50 billion in October this year. The November spike was widely believed to be rise in gold purchases in the initial days of demonetisation. Cumulatively, for the period April-December, exports picked up marginally by 0.75% to $198.8 billion while imports shrank 7.42% to $275.3 billion, leading to a trade deficit of $76.5 billion. India's fiscal deficit-difference between revenue and expenditure, for the April-December period stood at Rs 5.01 lakh crore, or 93.9 per cent, of 2016-17 Budget estimates (BE). The fiscal deficit stood at 87.9 per cent in the corresponding nine months a year ago, as per 2015-16 BE. Contrary to consensus expectations, India's factory output, as measured by the IIP, rose 5.7% in November, the first month of the government's demonetisation drive. Index of Industrial Production in October had declined by 1.81%. However this seems to be an aberration, mainly due to lower base effect of previous year and abnormal jump in certain segments such as 185 percent rise in cable, rubber insulated component had distorting effects on the IIP numbers. One needs to wait for December/ January numbers to get a clear trend on industrial pickup.

Liquidity and Rates

At the beginning of the month, SBI cut its MCLR by 90 bps across all tenors leading to similar lending rate cuts by other banks. Bond markets reacted to this with a rally pulling the yields down. Additionally the cut in the gsec borrowing (18000 crores) for remainder of fiscal year and expectations of comfortable inflation prevented the yields from spiking up. 10 year sovereign closed at 6.41%, this is a 10 bps fall from previous month closing. The 5 year AAA corporate bond benchmark closed at 7.33%, 4 bps lower as compared to previous month. 12 month CD rates were flat and closed at 6.50%. Markets are currently enjoying a bout of neutral to surplus liquidity and that's keeping the rates down for yields across the tenor.

Outlook

Muted economic growth, undershooting CPI inflation and fiscal prudence, all these make the time right for RBI to cut rates on February 8. The risks to this remain in form of rising US Federal Reserve rates, changed direction of global crude oil prices and increasing global political and indirectly macro economic volatility. So the exact timing of rate cut will be a hazy area and hence markets will be volatile. Basis this, there bouts of profit booking by those investors who entered at the earlier stages of rally. Long maturity funds will be suitable for those who can withstand extreme volatility. So even though from medium term perspective we continue to expect rate cuts and resulting fall in yields, the ride will be volatile and not bound by predefined timelines. Liquidity looks to be comfortable, with bank being flush with substantial deposits post demonetisation, and that should support the markets. For new investors short term fund offers a wonderful vehicle to earn high constant accrual. Benefit in terms of constant high accrual and effective vehicle as compared to bank fixed deposit (in light of lower and lower rates of FDs in banks) make short term fund a very attractive fund. Liquid and ultra short term fund, as always will be vehicles for smart utilisation of temporary surpluses.

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Equity Market Commentary

Indiabulls MUTUAL FUND

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Key Domestic News

- Government came out with a 'Bharat' focused Union Budget. Supporting agricultural economy and augmenting rural infrastructure are the key themes.
- Rural India, worst affected by demonetization, saw significant jump in allocation by 24%. Infra spending on Railways, Roads, Rural infra and affordable housing increased by ~25%.
- Government stuck to Fiscal discipline as against apprehensions of it turning populist. Fiscal deficit for FY18 targeted at 3.2% and 3% for FY19. Net market borrowing pegged at Rs3.48 lac crore, lower than 4.25 lac crore last year.
- Government finally granted infrastructure status to affordable housing.
- FIPB to be abolished in 2017-18. Government to announce new guidelines to attract FDI.
- No tinkering with LTCG, and no anti capital market measures.

Key Domestic Economic Data

- India's manufacturing PMI rose to 50.4 in January, after falling to a 12-month low of 49.6 in December after demonetization. Recovery was led by improvement growth in both new orders and output. According to IHS Markit, which compiled the survey, anecdotal evidence highlighted a return to normal market conditions and a subsequent improvement in demand.
- India's Services PMI improved to 48.7 compared to December's 46.8. "A rebound in the near term is likely as rates of reduction softened and business confidence improved on the back of hopes that market conditions will soon normalize." IHS Markit said.
- India's CPI inflation fell to 3.4% y-o-y in December from 3.6% in November, below expectations of a 3.5% reading.
- IIP expanded by 5.7% (1.5% expected), the fastest pace in more than four years, largely on account of a low base effect, jump in lumpy capital goods & restocking of consumer durables.

Key Global Events

- US President Donald Trump started off his term with an intent to fulfill his poll promises. US moved out of TPP, put VISA restrictions on a few countries, put NAFTA up for re-negotiation, threatened MNC with border tax and promised cutting regulations by 75% to fire up the US economy.
- The ECB left the key interest rates unchanged. The outlook is getting better, said Mario Draghi at his post-ECB meeting press conference, but the central bank stands ready to increase asset buys in both size and duration should things at all turn. "A very substantial degree of monetary accommodation is required" to meet the ECB's inflation target, he added.
- Theresa May outlined her priorities for BREXIT, as she prepared for 'clean break' of UK from EU. However, the legislation to initiate the BREXIT process must be approved by the parliament.

Outlook

- We believe that worst of economic effects of demonetization is over and expect a gradual recovery over next few months as currency crunch eases in broader economy.
- Post the union budget, we are turning cautiously optimistic on the equity markets. Now, it is uncertainty around US economic policies under Trump administration, spate of general elections in Europe and concerns on flight of capital out of China that are an overhang to the outlook. Outcome of state elections would be keenly watched.
- Indian macros are stables and would get stronger over going forward. Government's reform agenda continue unabated. Medium to long term outlook for Indian equities remains fairly robust. Next few months can be a good time for staggered investments in Indian equities.

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