Debt Market Commentary

Indiabulls MUTUAL FUND

July 2017

31st July	Month Opening	Intra Month High	Intra Month Low	Month Closing
Overnight Rate (NSE MIBOR)	6.25	6.26	6.17	6.25
10 year Gsec	6.55	6.55	6.41	6.47
3 month CDs	6.45	6.45	6.22	6.22
6M CDs	6.55	6.55	6.40	6.40
12 month CDs	6.65	6.65	6.50	6.54
Currency	64.88	64.88	64.11	64.18
10 Year US Treasury	2.35	2.39	2.24	2.30

Inflation & Macros

Retail inflation as measured by CPI (consumer price index) for June 2017 declined by 64 bps as compared to May 2017 which was led by falling food & cereal prices. June CPI came in at 1.54% as compared to 2.18% of May 2017. Core CPI inflation (adjusted for food and fuel) has eased further to 3.8% from 3.9% last month. WPI (Wholesale Price Index) under the new series with 2011-12 as base year, dropped sharply to 0.9% as compared to May number of 2.17%. Revised IIP series with 2011-12 as base was released. IIP as per that came in substantially lower at 1.70% as compared to 2.8% for April 2017. This lower IIP indicates tepid growth is plaguing the economy.

RBI Monetary Policy

In the latest policy, RBI had cut rates by 25bps as expected by market participants. It however acknowledged that, the upside risk to inflation, which RBI was projecting early in April 2017 policy, have not materialised. However they have highlighted that Q4 inflation could be higher than 4% by 10 bps. Hence, although having chosen to cut rates currently, any further rate actions, but will depend on global events and domestic data points. They have included that HRA effects would not be 150 bps as suggested earlier but 100 bps staggered during 18-24 months.

Liquidity and Rates

Excess of surplus liquidity in the system led to banks parking nearly average of 3 lakh crores with RBI for the month of July. Money market rates however came down as people were expecting a rate cut by 25 bps in August policy which materialised and entire money market curve was down by 25 bps pricing an overnight rate of 6% in August. MSS limits were hiked to drain out surplus liquidity creation through forex intervention and increase in circulation of money. However dated curve was almost flat and traded in a narrow range with 10 year benchmark range of 6.42 – 49. Good monsoon, lower inflation estimates, good FPI flows in markets all these led to a bullish momentum and aiding for a rate cut which was obliged by RBI in early August policy.

Outlook

After RBI's cut of 25 bps we see markets to trade in narrow range. Any further substantial upside/downside movement will be dependent on data and global news flow. Inflation readings below market estimates would keep the market supported and in hunt for further cues on rate cuts. However risks especially in form of global factors of US & Euro zone unwinding their asset purchase programme will keep the markets in a less than 100% optimistic mode. Basis all this duration products are still attractive as we believe there cut be one more final rate cut for this year before rate easing cycle stops, however they are suitable only for those investors who can digest volatility. On a ongoing basis, liquidity looks to be comfortable, with system being flush with funds. This will keep the short end of the curve constantly bought and hence offers a sweet spot. 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.

Malay Shah
Head – Fixed Income

Equity Market Commentary

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July 2017

Key Domestic News

- The RBI delivered a 25bps repo rate cut to 6.00%, as expected, citing reduced upside risks to inflation. The RBI kept its policy stance unchanged at neutral, as it sees the inflation trajectory rising from current lows and expects inflation to rise to little above 4% by Q1 2018 versus its earlier projection of 4.5%.
- The country as a whole received rainfall 4% in excess of LPA between June 1 and July 27. Only 11 per cent of the total area, particularly Karnataka and Tamil Nadu have got deficient rains, IMD said. It also expects the rainfall in August to be likely close to 99% of the average.
- In a shrewd political maneuver, Nitish Kumar walked out on alliance with RJD in Bihar and moved back to NDA fold. This move dashes of grand coalition on opposition force against the BJP for 2019 elections. He also brought 10 Rajya Sabha MPs to its fold, strengthening the NDA in upper house as well.

Key Domestic Economic Data

- India's manufacturing PMI fell sharply to 47.9 in July from 50.9 in June, due to GST related uncertainty. However, the future outlook improved further to an 11-month high of 62.1 in July from 59.0 in June, indicating that this is sharp fall in PMI is a temporary blip caused by GST led uncertainties.
- The services PMI also contracted in July, falling to 45.9 from 53.1 in June, due to uncertainty on GST. The drop in services PMI is also expected to be transitory, as the future activity index rose to 62.3 from 56.2.
- India's CPI inflation fell to 1.5% y-o-y in June from 2.2% in May, slightly below expectations of a 1.6% print, led by fall in food price and petroleum products prices during the month.
- Indias IIP growth moderated to 1.7% y-o-y in May from a downwardly revised 2.8% in April, below expectations of a 2% growth as firms scaled back production ahead of the GST.

Key Global Events

- US Fed left short-term interest rates unchanged as expected and indicated it likely would begin to start trimming its balance sheet "relatively soon".
- The ECB left its benchmark interest rates and QE program unchanged, as expected. In the post meet press conference, Mario Draghi said tapering of the ECB's stimulus will be on the table this fall.
- US imposed fresh trade sanctions against Russia, which according to analysts were strongest action Congress has taken against Russia since the Cold War. US is also expected to order investigations into China's trade practices, these measures can heighten geo-political tensions.

Outlook

- Implementation of GST has been smoother than market expectations. Some teething troubles still remain, but are being proactively smoothened by the Government.
- Q1 FY18 results so far have been better than expected so far. While some sectors have been hit due to GST uncertainty, nearly 60% on the companies have beaten consensus expectations. We expect Q2 to be a very strong quarter for corporates as GST related uncertainty ebbs, and early onset of festival season this year should boost demand significantly.
- High frequency economic data like PMI and IIP are showing temporary weakness due to GST implementation issues. We expect strong recovery over next few months in these indicators. Q2 GDP growth is expected to be weak; we expect strong bounce back from H2 FY18 onwards.
- Monsoon continues to be above average and reasonable well distributed. This augurs well for food inflation and rural demand.
- We continue to be positive on Indian equities over medium to long term. STPs and SIPs should be preferred route.
- Any escalation of India-China conflict is the key risk over short term.

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