# Debt Market Commentary

Indiabulls MUTUAL FUND

October 2017

| 31st October | Month Opening | Intra Month High | Intra Month Low | Month Closing |
|---|---|---|---|---|
| Overnight Rate (NSE MIBOR) | 6.00 | 6.10 | 5.93 | 6.00 |
| 10 year Gsec | 6.65 | 6.88 | 6.65 | 6.86 |
| 3 month CDs | 6.22 | 6.22 | 6.18 | 6.18 |
| 6M CDs | 6.45 | 6.50 | 6.45 | 6.50 |
| 12 month CDs | 6.55 | 6.60 | 6.55 | 6.60 |
| Currency | 65.50 | 65.50 | 64.74 | 64.75 |
| 10 Year US Treasury | 2.34 | 2.46 | 2.28 | 2.38 |

**Inflation & Macros**

Retail inflation as measured by CPI (consumer price index) for Sep 2017 remained flat at 3.28% vs 3.36% (m-o-m). The headline inflation number was flat but a rise in core CPI inflation (adjusted for food and fuel, correctly including petrol and diesel) has increased further to 4.6% from 4.5% last month. WPI (Wholesale Price Index) under the new series with 2011-12 as base year, softened to 2.60% as compared to Aug number of 3.24%. Revised IIP series with 2011-12 as base was released. IIP as per that came in at 4.3% as compared to 1.2% for Aug 2017.

**RBI Monetary Policy**

After the RBI policy market participants become jittery and hence a call of duration cut echoed market post the CPI numbers. The hardening stance of RBI on CPI numbers with fiscal deficit widening due to increasing crude oil prices from 50$ centric to 60$ made the market in a cautious mode. The government gave a Diwali bonus to PSU banks with a bank recap plan of 2.10 trillion where government would inject capital to that tune to start lending process of banks while maintaining their capital ratios due to the stress on balance sheets due to NPL's. This also divided the market where some section see bank recap plan as a catalyst to rate cut whereas some have said rate hike cycle would now start. We believe that it would be a pause as banks would need further capital to start lending process and meet its basel 3 capital requirements. In this aftermath we see banks raising more capital in form of their perpetual bonds which would see a glut of supply in coming months. The lingering effects of FED nomination for the chair also weighed in EM due to policy uncertainty as name of Taylor started doing the rounds and famous Taylor rule seeing funds rate at 3.75%. Market was cajoled after Fed finally announcing Powell as successor to Yellen which is effective continuation of Fed policy of increasing rate albeit at a slower pace and not disrupting markets.

**Liquidity and Rates**

Excess of surplus liquidity in the system led to banks parking nearly average of 2.1 lakh crores with RBI for the month of Oct. Money market rates however stayed in the same zone as people were expecting RBI to remain status quo. Hence we saw an upward pressure on dated curve and yields hardened from 6.65 to 6.85. The hardening of yields was due to increase in Core CPI number and further CPI prints also looking upwards though within the RBI range. Also there was news of fiscal slippages and increase in crude oil which could widen fiscal deficit or imported inflation seeping in economy adding pressure to yields. Hence people started expecting status quo in December policy with hawkish comments and lot of portfolio shifting from longer duration to shorter duration was seen. The corporate bond market also tracked G-sec yields and hence yields hardened by 5 to 10bps in 2 to 5 year bonds.

**Outlook**

At this juncture, a pause seems to be on cards as far as rate cuts are concerned. We might remain at 6% repo rate for foreseeable future. We need crude oil march to stabilise before we see any substantial difference in comments from government and RBI monetary policy members, till then we will continue to see a pause and markets in a range bound movement with specific maturity buckets offering safety in form of good risk reward equation. AAA top rated bonds having 2-4 year maturity offers a wonderful vehicle for those investors who want to tread lightly and want to focus on earning a reasonable return on capital without substantial volatility and unnecessary credit risks. Hence in light of that we reiterate our view of Indiabulls Income fund and Short term fund as good vehicles for deployment of funds. As always liquid and ultra short term funds would continue to remain better vehicles for deployment of temporary surpluses.

**Malay Shah**
**Head – Fixed Income**

# Equity Market Commentary

October 2017

**Key Domestic News**

- The Government announced a large capitalisation program for PSU Banks worth INR 2.1 trn (1.3% of GDP) which is expected to be implemented over next 12 months, through a combination of issuance of recapitalization bonds( INR1.35trn), budgetary allocation (INR181bn) over FY18 & FY19 and raising through market resources (INR580bn). Over the next quarter, the government has also promised to announce additional banking reforms. After the infusion, we expect PSU Banks to be lot more amenable in NPA resolution, by taking haircuts, entering into one time settlements and making adequate provisions. It should also help in pushing up growth over medium term.
- The government approved the plan to develop approximately 83,677 km of roads at an investment of Rs 6.92 lakh crore by 2022. The highway construction program is aimed at pushing economic activity and generating at least 14.2 crore man-days employment across the country over the next five years. This plan is expected to be implemented from mid FY19 and should lead to spurt in growth, and also kick start the capex cycle.
- In the 2018 World Bank Doing Business rankings, India jumped 30 places to 100th from 130th last year. During the past year, India has made major progress in the areas of paying taxes and resolving insolvency. This should help India attract significantly more FDI investments.

**Key Domestic Economic Data**

- India's manufacturing PMI eased to 50.3 in October, from 51.2 in September, indicating that the recovery in manufacturing activity from GST related disruptions continues to be volatile. However Services PMI rose to 51.7 in October from 50.7 in September, indicating that Services are coping much better with GST implementation.
- India's trade deficit narrowed to USD9.0bn in September from USD11.6bn in August. Export growth rose sharply to 25.7% in September from 10.3% in August. The pick-up was broad-based across sectors. Based on Q3 trade data, Analyst expect the current account deficit (CAD) to narrow to 1.6% of GDP in Q3 from 2.4% in Q2.
- CPI for September 2017 came in at 3.3% vs consensus estimate of 3.5% reading unchanged from last month and 4.4% last year, led by sharp drop in food inflation.
- India's Industrial production grew 4.3% in August, up from 0.9% in July, reflecting restocking by manufacturing firms after GST implementation. Both consumer and capital goods contributed to the growth. Also, Core sector growth data for September came in at a strong 5.2% vs. 4.4% last month, suggesting that strength in IIP should continue for September as well.

**Key Global Events**

- US Q3 GDP growth came in at robust 3% vs 2.5% expectation and 3.1% growth last quarter. Economic growth was expected to have weakened on account of two hurricanes that hit US last quarter.
- US FOMC left the Fed Funds rate unchanged. The policy statement mentioned solid economic activity despite the hurricanes, soft core inflation, and continued strength in the labor market. This suggests another rate hike is on the table in December meeting.
- Bank of England raised the Bank Rate by 25 basis points to 0.50% as expected. The boost just takes the rate back to where it had been for years since the financial crisis. The bank had cut the rate to 0.25% after the shock Brexit vote last year.
- The ECB announced the reduction in its QE program to €30B per month down from the current €60B pace. QE is expected to continue at this reduced rate for another nine months beginning January 2018.

**Outlook**

- Indian economy is on path of gradual recovery from GST implementation led disruptions. We expect the recovery to gather pace in next 2 quarters. Our channel checks continue to suggest that business re-stocking though picking up, is still at a slow pace. Worst of GST related issues may be behind us.
- Government is proactively trying to solve needling GST related issues; according to media reports a comprehensive tweak is in the works and likely to be announced this month.
- Corporate results for September quarter till now have broadly been in line with our expectations; Management commentary is encouraging and augurs well for December quarter.
- Demonetization, GST implementation, steps to improve ease of doing business, PSU recapitalization, ambitious projects like Bharatmala are all strong steps, whose benefits are expected to accrue over next 18-24 months. They make India story even more compelling from both FDI and FII investment perspective. We continue to be positive on Indian equities over medium to long term. STPs and SIPs should be preferred route.
- Spike in Oil prices above $65 and escalation of Geo-Political risk involving North Korea are the key risk over short term.

**Sumit Bhatnagar, CFA**
**Head - Equity**