Debt Market Commentary

September 2017

30th September	Month Opening	Intra Month High	Intra Month Low	Month Closing
Overnight Rate (NSE MIBOR)	5.90	6.05	5.90	6.05
10 year Gsec	6.48	6.67	6.48	6.66
3 month CDs	6.18	6.18	6.12	6.12
6M CDs	6.35	6.35	6.30	6.33
12 month CDs	6.55	6.55	6.50	6.55
Currency	64.02	65.71	63.78	65.28
10 Year US Treasury	2.16	2.33	2.05	2.33

Inflation & Macros

Retail inflation as measured by CPI (consumer price index) for Aug 2017 inched up by 100 bps as compared to Jul 2017 and came in at 3.36% as compared to 2.36% earlier. The hardening of inflation was due to increase in prices across all categories. Core CPI inflation (adjusted for food and fuel, correctly including petrol and diesel) has increased further to 3.9% to 4.5% last month. WPI (Wholesale Price Index) under the new series with 2011-12 as base year, hardened sharply to 3.24% as compared to Jul number of 1.88%. Revised IIP series with 2011-12 as base was released. IIP as per that came in at 1.2% as compared to -0.2% for Jul 2017.

RBI Monetary Policy

In the latest policy, RBI had kept policy rate as status quo and cut SLR & HTM to 19.5%. We believe these would be the reasons for maintaining status quo as mentioned below:

- Upside risk to inflation existing in form of, fiscal deficit overshooting the target, farm loan waivers, possible increase of salaries and wages by different states, imported inflation in form of continuing increase in crude oil prices and lastly, stickiness of core inflation,
- Transient factors like, GST led destocking and subsequent disruption, uneven monsoon distribution led probable risks of decrease in food grain output and hence continuing pressure on food prices.

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 Sept. 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 6.48 to 6.65. The hardening of yields was due to increase in CPI number and further CPI prints also looking upwards though within the RBI range. Also there was news of fiscal slippages and hence extra government borrowing adding to pressure to yields. Hence people started expecting status quo in OCT policy 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 10 to 15bps 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 be at 6% repo rate for foreseeable future. Although RBI is has not shut the door on any further cuts, however for that to happen, multiple factors like:

a) US FED balance sheet normalisation not happening faster than expected,

b) crude oil prices not spiking substantially,

c) no substantially fiscal slippage,

d) CPI and core inflation cooling down and

e) Q2 quarter growth numbers disappointing; all this factors have to fall in place.

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 feel Indiabulls income and Short term fund are good vehicles for deployment of funds.

Malay Shah
Head – Fixed Income

Equity Market Commentary

September 2017

Key Domestic News

- With a view to achieve 'Housing for All by 2022', the central government announced a new policy for affordable housing that permits extending subsidy of up to ₹ 2.50 lakh per each house to be built by private builders on private lands. It also announced multiple models for potential private investments in affordable housing projects on government lands in urban areas.
- Direct taxes continue to register strong growth in the first five months of the current fiscal. It grew 17.5% to ₹ 2.24 lakh crore. After adjusting for refunds, the net growth in corporate tax collections was 18.1% while that in income tax collections was 16.5%. In the April-August period last fiscal, 2016-17, the direct tax collection had grown 15.03%.
- The RBI left the repo rate unchanged at 6.00%, in line with expectation, due to higher inflation, higher oil prices and fiscal risks. The RBI projected inflation at 4.6% in Q1 2018 and also lowered its FY18 GVA growth projection to 6.7% y-o-y from 7.3% in August.

Key Domestic Economic Data

- India's manufacturing PMI came in at 51.2 in September, unchanged from August, suggesting that manufacturing sector is yet to overcome lingering effects of GST implementation. Services PMI rose to 50.7 in September from 47.5 reflecting that the economy was recovering from the disruptions due to the GST.
- India's current account deficit widened in Q2 to 2.4% of GDP, from a deficit of 0.6% in Q1, led by higher non-oil, non-gold imports. Analysts expect India's current account deficit to widen to 1.6% of GDP in 2017, from 0.6% in 2016, but the capital inflows should be enough to fund this deficit.
- CPI for August 2017 stood at 3.4% (consensus estimate of 3.3%) against 2.3% last month. Core CPI inflation increased to 4.6% from 4.1%, reflecting higher petrol prices, the house rent allowance impact, and the impact of GST.
- Industrial production grew 1.2% y-o-y in July below consensus expectations of 1.6% growth, but up -0.2% reading in June. However, core sector growth rose to a five month high of 4.9% in August. The growth was driven largely by a sharp rise in coal and electricity output.

Key Global Events

- Spain sunk into a constitutional crisis, as more than 90% of Catalan voters chose independence from it. Though termed as illegal, this referendum has a potential to derail Spain's fragile economic recovery.
- US-North Korea tensions continued unabated with both sides escalating the war rhetoric.
- Moody's downgraded the UK's credit rating to Aa2 and lifted its ratings outlook to stable after the downgrade.
- The USFOMC left the funds rate unchanged at, and set October as the date to start trimming the balance sheet by $10B per month. Its funds rate forecasts suggest one more rate hike in CY18 and two - three rate hikes next year.
- High frequency data out of China like PMIs, factory output, fixed-asset investment, retail sales etc. reported soft numbers for the second straight month. Probably, a sign that it may be losing momentum in Q3.

Outlook

- High frequency indicators are showing early signs of recovery from GST implementation in Indian economy. We expect the recovery to gather pace in next 2 quarters. Our channel checks suggest that business re-stocking is picking up, albeit at a slower pace. Worst of GST related issues may be behind us.
- Corporate results for September quarter would be keenly watched to get clear insight on extent of economic recovery and future earnings trajectory. We expect a high single digit earnings growth for Sensex index constituents.
- GST is game changer reform, whose benefits are expected to accrue over next 12-18 months. We continue to be positive on Indian equities over medium to long term. STPs and SIPs should be preferred route.
- Any escalation of Geo-Political risk involving North Korea is the key risk over short term.

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