

# PROSPERITY INSIGHTS

## IMF lowers estimates for World GDP growth

The month of December has begun with the European Central Bank delivering lesser-than-expected stimulus measures (10 bps deposit rate cut, extension of QE program by six months) in its much-anticipated monetary policy meeting. This fuelled a global risk-off sentiment, as markets were disappointed by ECB president Draghi who was widely expected to over-deliver on the measures. However, the renewed slide in energy prices and recent reading on core inflation ticking lower (0.9% in Nov. vs. 1.1% in Oct); the downside risks to ECB's inflation forecast of 2% have arisen, and is likely to weigh on ECB's decision on stimulus going forward.

As the EU undertakes further stimulus measures, US Fed officials' hawkish statements have driven the dollar to eight-year highs, signaling an imminent rate hike in December. Nonfarm payrolls of November also posted strong numbers (211K vs. market expectations of 200K increase), thereby reaffirming improvement in labour market and raising the likelihood of lift-off by US Fed at its upcoming meeting. In anticipation of a rate lift-off, financial markets across emerging economies are seeing downside pressures, with their currencies moving lower and gold hovering near six-year lows. Going forward, global market volatility would pick up further as we approach the day of the US FOMC meeting.

Meanwhile, revised 3Q-2015 GDP data from Japan showed its economy grew 0.3% revised up from the initial estimate of -0.2% driven by stronger investments and moderate decline in inventories. Chinese export data which was being closely watched for signs of stabilization surprised with yet another weak print in November (Actual -6.8% YoY vs. expectation of -5%). The concomitant impact of trade slowdown in China was visible across other key exporting nations. South Korea's export continued to remain weak and fell 4.7% in November and Taiwan's exports contracted (Actual: -11%, Forecast: 11.1%) for the 9th straight month in October.

On the domestic front, lead indicators continue to highlight a recovery, albeit still not broad-based. Amid persistent weakness in external demand and a lack of appetite for private investment, PMI manufacturing eased to near 2-year low. After touching an eight-month high in October, November PMI services also fell sharply, as growth in commercial vehicle sales and domestic aviation passenger traffic was offset by a slowdown in tourist arrivals, cargo and railway freight traffic. Bank credit growth continues to remain weak on tepid off-take in industry sector and recourse to cheaper and non-bank sources of funding. On the positive side, while core sector growth in October was partly supported by a favorable base, month-on-month momentum in certain sectors (fertilizers, cement) has shown successive increases.

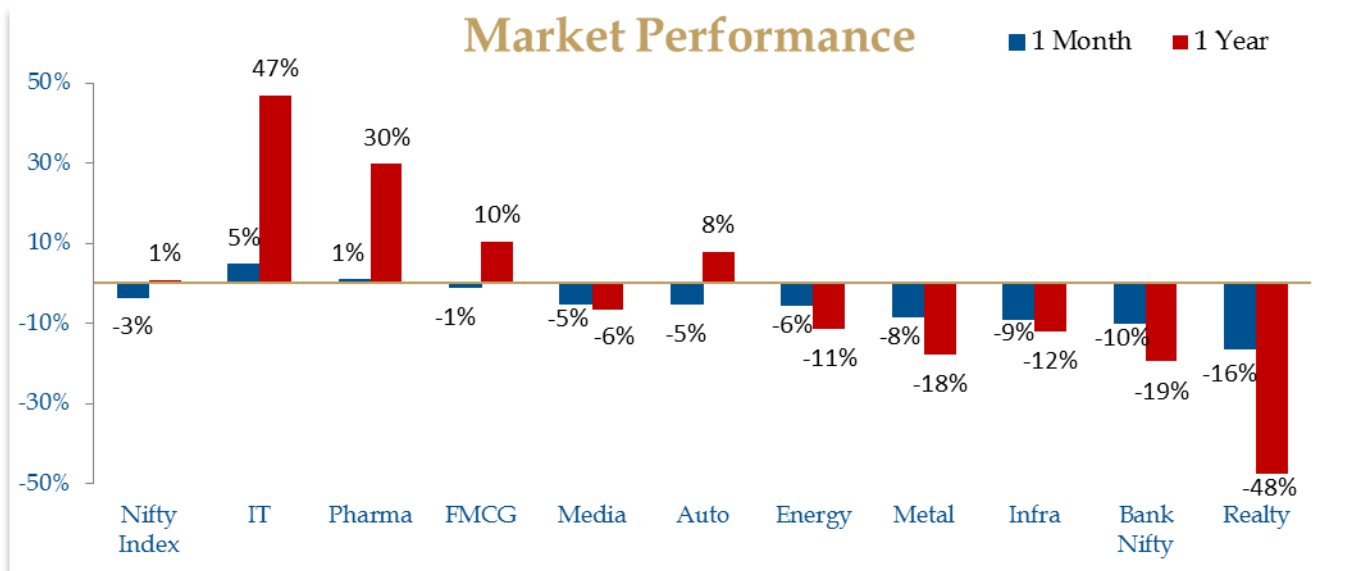
On the fiscal front, 7th Central Pay Commission (CPC) report released in November has put the focus on the viability of the fiscal consolidation path for FY17. For the FY17 Union Budget, the total financial implications of the 7th CPC is projected to be INR 736 bn (0.49% of GDP; ex railways), with the government likely to face a tightrope maintaining public spending. A likely solution could be staggering the payments over the next few years. To some extent, the wage-increase led increase in tax revenues would also help the fiscal position. For the economy as a whole, the 7th CPC wage hike is likely to be a boost to discretionary consumption, as also noted during previous pay hikes. In the medium term, continued focus on reforms such as ease of doing business, Make in India and progress on labor reforms should allow recovery to acquire a more sustained character, propelling growth closer to 8% in FY17.

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## Equity Market Insights

- ✓ The month of November saw the Indian stock markets continue on a bumpy ride. The BSE Sensex closed at 26,146, lower by 1.9% for the month while the Nifty closed at 7,935; down by 1.6% during the same period. The CNX Mid-Cap and CNX Small-cap indices relatively outperformed with gains of 0.1% and 3.4% respectively.
- ✓ During November, FIIs interest remained subdued with regards to the capital markets. There was a net outflow of US\$ 1.2 bn from equity markets and US\$ 0.6 bn from debt markets taking the total tally to an outflow of US\$ 1.7 bn from capital markets. DII's were net buyers and ~ \$2.4bn during the same period.



### Factors to Watch

- ✓ Markets remained volatile with growing fears related to global growth. The fears were further exacerbated with data from China continuing to indicate that the economy is seeing signs of a slowdown. In addition to this the other major event that the global investors are watching out for is the hike in interest rates in the US. With data from the US showing signs of improvement, there are increased expectations that the rate hike may happen in the current calendar year. A high probability of a rate hike followed by a dovish stance post that is what is being priced in by the global markets.
- ✓ Investors would also be keeping a close eye on commodity prices particularly that of crude. Increasing geo-political tensions in the region as well as the upcoming OPEC meet would be crucial factors guiding the prices of crude in the near term.
- ✓ Other events that investors would keep an eye on would be data related to China and other geo-political events.

### Outlook & Expectations

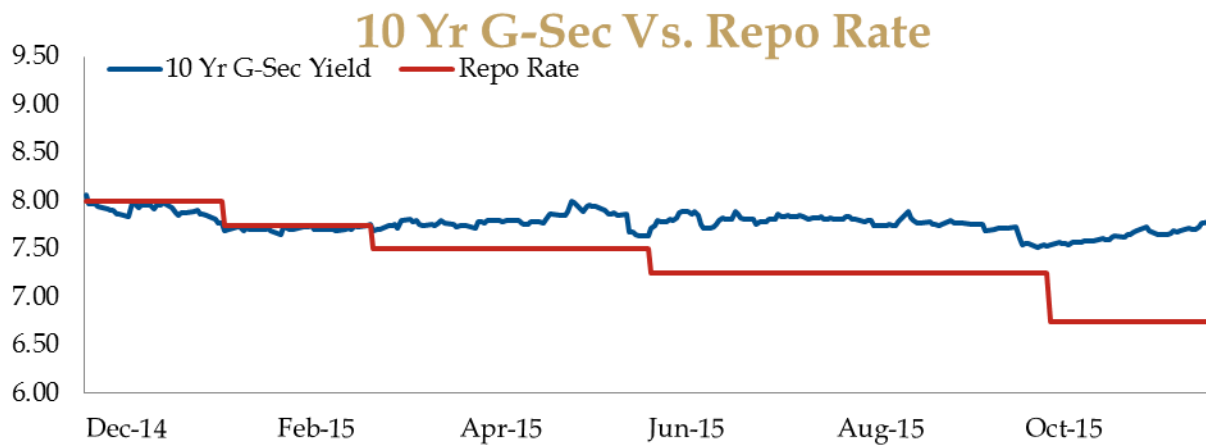
- ✓ In terms of valuations, the Sensex is trading at a trailing twelve month PE multiple of 20.6 times which is slightly higher than its long term historic average of 18.2 times. On a forward earnings basis the Sensex is trading at a multiple of around 17.4 times, which suggests that markets are not expensive but fairly valued at current levels. Building an assumption of a robust improvement in earnings in FY17, we believe that the markets are still attractive from a longer term perspective, i.e. for 2 to 3 years. We believe that any correction in the market should be viewed as an ideal time to pick up quality stocks.
- ✓ From a long term perspective we continue to remain positive on companies in infrastructure, capital goods and auto stocks. Investors could also look at investing in select stocks in the IT space.

## Debt Market Insights

- ✓ The average systemic liquidity deficit in Nov rose to INR 758 bn from INR 299 bn in previous month on account of currency leakage in the system.
- ✓ Average 10 yr yield during Nov rose to 7.69% from 7.57% in Oct tracking the depreciation of the Rupee.
- ✓ In line with our expectations, the RBI maintained status quo on key policy rates in its fifth bi-monthly policy review after the front loaded action in September and the anticipated monetary policy divergence in advanced countries.

### Outlook and Expectations

- ✓ In line with our expectations, the RBI maintained status quo on key policy rates in its fifth bi-monthly policy review after the front loaded action in September and the anticipated monetary policy divergence in advanced countries. We continue to expect 25 bps cut in the repo rate in Q4 FY16
- ✓ Further 25 bps easing is likely in Q1 FY17 provided the government sticks to the path of indicated fiscal consolidation despite the onus of increased wage and pension bill, global commodity prices remain soft, and food inflation remains under check



## Model Portfolios - December 2015

Asset Class	Conservative	Cautious	Moderate	Growth	High Growth
<b>I) Debt (%)</b>	<b>95</b>	<b>70</b>	<b>50</b>	<b>25</b>	<b>10</b>
Ultra Short Term Funds	20	15	15	5	-
Dynamic /Income Funds	35	30	20	15	5
NCD/ Bank Deposit	40	25	15	5	5
<b>II) Equity (%)</b>	<b>-</b>	<b>15</b>	<b>30</b>	<b>45</b>	<b>55</b>
Large Cap	-	15	25	30	35
Mid cap	-	-	5	10	15
Sector/ Thematic	-	-	-	5	5
<b>II) Alternate (%)</b>	<b>5</b>	<b>15</b>	<b>20</b>	<b>30</b>	<b>35</b>
Gold ETF	5	5	10	10	10
Structured Products	-	10	10	10	10
PE/ Real Estate Funds	-	-	-	10	15
<b>Total (%)</b>	<b>100</b>	<b>100</b>	<b>100</b>	<b>100</b>	<b>100</b>

## Glossary:

- ✓ Consumer Price Index (CPI): A measure that examines the weighted average of prices of a basket of consumer goods and services, such as transportation, food and medical care.
- ✓ Wholesale Price Index (WPI): An index that measures and tracks the changes in price of goods in the stages before the retail level.
- ✓ Open Market Operations (OMO's): is the buying and selling of government securities in the open market in order to expand or contract the amount of money in the banking system. Purchases inject money into the banking system and stimulate growth while sales of securities do the opposite.
- ✓ Cash Management Bills (CMB): A short-term security sold by RBI to meet any temporary shortfalls.
- ✓ Purchasing Managers Index (PMI) is based on surveys on private sector service / manufacturing companies. An index level of 50 denotes no change since the previous month, while a level above 50 signals an increase or improvement and below 50 indicates a decrease or deterioration.
- ✓ Net Demand and Time Liabilities (NDTL): It is the sum of demand and time liabilities (deposits) of banks with public and other banks wherein assets with other banks is subtracted to get net liability of other banks.
- ✓ Current Account Deficit (CAD): A measurement of a country's trade in which the value of goods and services it imports exceeds the value of goods and services it exports. A current account deficit represents negative net sales abroad. A country can reduce its current account deficit by increasing the value of its exports relative to the value of imports.
- ✓ West Texas Intermediate (WTI): also known as Texas light sweet, is a grade of crude oil used as a benchmark in oil pricing. This grade is described as light because of its relatively low density, and sweet because of its low sulfur content.

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