LIQUIDITY, VALUATIONS AND EVENTS

October – December

2018

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MOVEMENTS OF MAJOR INDICES

Index Name	Country	30th Sep'17	30th June'18	30th Sep'18	3-Month Return (%)	1-Year Return (%)
MerVal	Argentina	26,078	26,037	33,462	29%	28%
Bovespa	Brazil	74,294	72,763	79,342	9%	7%
Dow Jones	US	22,405	24,271	26,458	9%	18%
Nikkei 225	Japan	20,312	22,305	24,120	8%	19%
Nasdaq	US	6,496	7,510	8,046	7%	24%
KLSE Composite	Malaysia	1,759	1,692	1,793	6%	2%
Swiss Market	Switzerland	9,133	8,609	9,088	6%	0%
NYSE	US	12,209	12,504	13,083	5%	7%
RTS Index	Russia	1,137	1,154	1,192	3%	5%
CAC 40	France	5,298	5,324	5,493	3%	4%
Jakarta Composite	Indonesia	5,894	5,799	5,977	3%	1%
S&P BSE Sensex	India	31,284	35,423	36,227	2%	16%
Nifty 50	India	9,789	10,714	10,930	2%	12%
Taiwan Weighted	Taiwan	10,322	10,837	11,006	2%	7%
Seoul Composite	South Korea	2,388	2,326	2,343	1%	-2%
Straits Times	Singapore	3,212	3,269	3,257	0%	1%
DAX	Germany	12,742	12,306	12,247	0%	-4%
Shanghai Composite	China	3,348	2,847	2,821	-1%	-16%
FTSE 100	UK	7,368	7,637	7,510	-2%	2%
Hang Seng	Hong Kong	27,519	28,955	27,789	-4%	1%

MOVEMENT OF SECTORAL INDICES

Sectoral Index	30th Sep'17	30th June'18	30th Sep'18	3-Month Return (%)	1-Year Return (%)
S&P BSE Energy	3,768	3,948	4,670	18%	24%
S&P BSE IT	9,947	13,920	15,629	12%	57%
S&P BSE OIL & GAS Index	14,843	13,660	14,855	9%	0%
S&P BSE TECk Index	5,608	7,165	7,731	8%	38%
S&P BSE Health Care	13,488	14,004	15,025	7%	11%
S&P BSE FMCG	9,773	11,213	11,503	3%	18%
S&P BSE Sensex	31,284	35,423	36,227	2%	16%
Nifty 50	9,789	10,714	10,930	2%	12%
S&P BSE METAL Index	13,564	13,064	13,279	2%	-2%
S&P BSE Power Index	2,206	1,947	1,929	-1%	-13%
S&P BSE Capital Goods	17,172	17,488	17,109	-2%	0%
S&P BSE BANKEX	27,025	29,251	27,992	-4%	4%
S&P BSE Mid-Cap	15,436	15,451	14,763	-4%	-4%
S&P BSE Consumer Durables	17,555	20,207	19,134	-5%	9%
S&P BSE India Infrastructure Index	221	205	190	-7%	-14%
S&P BSE AUTO Index	24,180	23,838	21,477	-10%	-11%
S&P BSE Small-Cap	16,114	16,032	14,431	-10%	-10%
S&P BSE Telecom	1,364	1,185	1,022	-14%	-25%
S&P BSE Realty Index	2,065	2,073	1,703	-18%	-18%

FOREIGN INSTITUTIONAL INVESTOR (FII) FLOWS

FII Flows in Equity

(in Rs. Crore)	Jul – 18	Aug – 18	Sep – 18	TOTAL
Gross Purchase	1,08,342	1,00,340	1,16,970	3,25,653
Gross Sale	1,06,078	98,565	1,27,795	3,32,438
Net Investment	2,264	1,775	-10,825	-6,785

FII Flows in Debt

(in Rs. Crore)	Jul – 18	Aug – 18	Sep – 18	TOTAL
Gross Purchase	20,225	19,190	14,065	53,479
Gross Sale	20,177	15,776	24,263	60,216
Net Investment	48	3,414	-10,198	-6,736

Total Net FII Flows in Jul - Sep 2018	- Rs. 13,522 Crore

Source: SEBI

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DOMESTIC INSTITUTIONAL INVESTOR (DII) FLOWS

(in Rs. Crore)	Jul – 18	Aug – 18	Sep – 18	TOTAL
Gross Purchase	2,38,573	1,60,628	87,938	4,87,139
Gross Sale	2,22,319	1,46,809	73,629	4,42,757
Net Investment	16,254	13,819	14,309	44,382

Source: SEBI

MF ACTIVITY

Equity

(in Rs. Crore)	Jul – 18	Aug – 18	Sep – 18	TOTAL
Gross Purchase	59,897	50,317	61,772	1,71,986
Gross Sale	55,902	47,465	50,134	1,53,501
Net Investment	3,995	2,851	11,638	18,485

Debt

(in Rs. Crore)	Jul – 18	Aug – 18	Sep – 18	TOTAL
Gross Purchase	1,42,717	1,37,116	1,70,019	4,49,853
Gross Sale	1,46,353	1,09,580	1,51,333	4,07,265
Net Investment	-3,635	27,536	18,686	42,588

Source: SEBI

Total Net MF Activity in Jul - Sep’18	Rs 61,073 Crore

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DOMESTIC EVENTS

FAST DEPRECIATING RUPEE

- The Indian Rupee, which was till last year resilient, has emerged as one of the worst performing emerging market (EM) currencies in 2018.
- In the year-to-date (YTD) period ending 30th September'18 the Rupee depreciated by almost 12% against the US dollar- touching almost Rs. 73 against the dollar by the end of September.
- What is causing the depreciation?
  - A strengthening US dollar on account of monetary policy tightening by the US Federal Reserve
  - Increasingly protectionist trade policies
  - Massive increase in the oil import bill due to rising crude oil prices
  - Outflow of foreign institutional money
  - Widening current account deficit

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WIDENING CURRENT ACCOUNT DEFICIT

- The Current Account Deficit (CAD) rose to 2.8% of the Gross Domestic Product (GDP) this year
- Last year it was 1.9% of GDP
- The average CAD in the 4 quarters of 2015-16 was $5.54 billion whereas the average for the last three quarters has been $14.2 billion.
- An increasing CAD combined with rising US interest rates has put further downward pressure on the Indian Rupee.
- Some measures taken by the government to curtail the widening CAD:
  - Increase in import duties of 19 non-essential items such as consumer electronics, diamonds, jewellery, jet fuel and leather footwear.
  - This move is likely to yield around Rs 40 billion in revenue.

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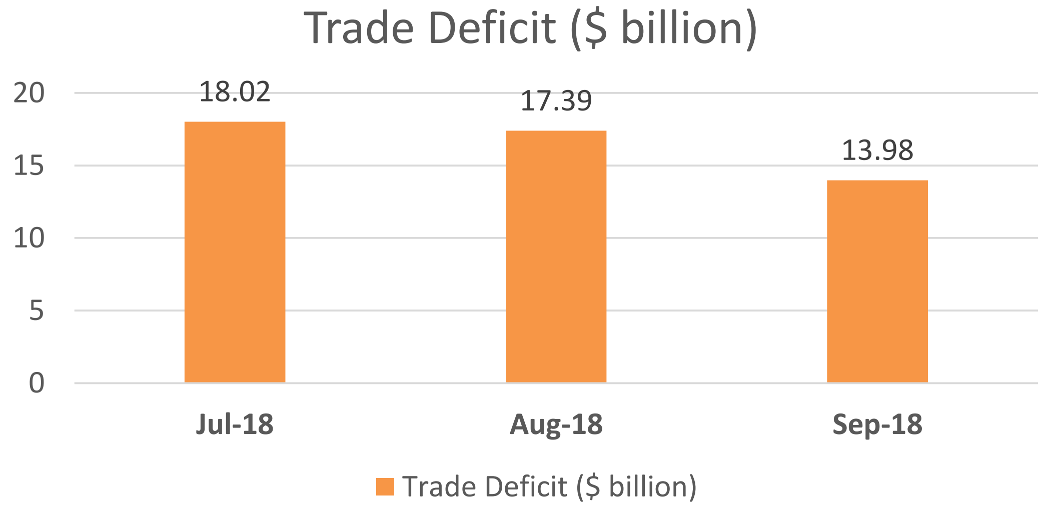
REDUCED TRADE DEFICIT

- The trade deficit measures the amount by which the imports of the country exceed the exports. This number has been on a declining trend last quarter (refer to the chart below).
- The September value was the lowest in 5 months.



HEALTHY GROWTH RATE

- India emerged as the fastest growing economy in the world, clocking in an annualized growth rate of 8.2% in the April-June 2018 quarter.
- The RBI retained GDP growth forecast for 2018-19 at 7.4%.
- Fitch Ratings has revised its projection upward from 7.4% to 7.8% for FY19.

Agency	GDP Growth Projection for 2018-19 (%)
Reserve Bank of India	7.4
Fitch Ratings	7.8
International Monetary Fund (IMF)	7.3
Asian Development Bank (ADB)	7.3

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HEALTHY GROWTH RATE

- Purchasing Managers' Index (PMI): The Service sector activity has been on a declining trend. The manufacturing activity fell in August and again picked up in September. (A reading above 50 indicates expansion)

PMI (SERVICES)		PMI (MANUFACTURING)	
Jul-18	54.2	Jul-18	52.3
Aug-18	51.5	Aug-18	51.7
Sep-18	50.9	Sep-18	52.2

- Index of Industrial Production (IIP)
  - The factory output as measured by IIP declined in the previous quarter.

	Jun-18	Jul – 18	Aug – 18	Sep – 18
IIP (%)	7	6.6	4.3	To be released

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INFLATION & RBI POLICY

- The inflation in the economy cooled down a bit in August and later increased slightly in September.

(%)	Jul – 18	Aug – 18	Sep – 18
Wholesale Price Index (WPI) based inflation	5.09	4.53	5.13
Consumer Price Index (CPI) based inflation	4.17	3.69	3.77

- The RBI increased the repo rate (the rate at which banks can borrow money from RBI) by 25 basis points in August to 6.5% as it had concerns over retail inflation staying above the target of 4% for 8 consecutive months.

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MAJOR REFORMS

The government reduced the borrowing programme for the year by Rs 70,000 crore and re-affirmed the plans to stick to the fiscal deficit target of 3.3% of GDP.

The government laid out a plan to infuse Rs. 11,300 crore in 5 PSU banks which are ailing – Allahabad Bank, Corporation Bank, Indian Overseas Bank, Punjab National Bank and Andhra Bank.

SEBI capped the maximum total expense ratio (TER) – the fees levied from investors annually to manage their funds – for close ended schemes at 1.25% and for other schemes at 1%

The GST Council cut tax rates on 191 goods that were in the 28% slab, leaving only 35 items in the highest slab – such as AC, digital camera, video recorders, dishwashing machine, automobiles.

SEBI proposed to make it mandatory for large corporates to raise 25% borrowing made in 2019-20 through the bond market to reduce dependence on banks.

The Prime Minister launched the Ayushman Bharat-PM Jan Arogya Yojana which proposes to provide an annual health cover of Rs 5 lakh per family. It is projected to benefit 500 million people.

The RBI freed up Rs 2 trillion for the banking system by revising the calculation method of solvency ratio.

The government authorized construction of around 6.28 lakh more affordable houses for urban poor in 11 states under the Pradhan Mantri Awas Yojna.

The government has launched a single form through which foreign investors can register themselves with SEBI, open a bank account and obtain a PAN Number. Earlier they had to approach 3 different entities.

IL&FS ISSUE

- Infrastructure Leasing and Financing Services (IL&FS), founded in 1987, is one of India's leading infrastructure finance companies. It is a giant with around 150 subsidiaries.
- The first signs of a crisis appeared in June when IL&FS defaulted on inter-corporate deposits and commercial papers (borrowings) worth about Rs 450 crore. There were other defaults in September.
- Its credit rating was reduced to D category (default) from AAA in a very short span of around a month by rating agencies ICRA and Care Ratings. This has made it difficult for the company to raise more money from the market.
- A sense of panic spread among market participants in relation to other non-banking financial companies as well.
- There was hope that major shareholders – LIC, HDFC, Japan's Orix Corporation and Abu Dhabi Investment Authority – might be able to work out a Rs 4,500 crore rights share sale.
- The government had to step in. It moved the National Company Law Tribunal (NCLT) to supersede and reconstitute the board of the firm which has defaulted on a series of its debt payments over the last one month. Uday Kotak, MD and Vice Chairman of Kotak Mahindra Bank, retired IAS officer Vineet Nayyar, former SEBI and LIC Chairman G N Bajpai, former IAS officer and ICICI's nonexecutive chairperson G C Chaturvedi; Director General of Shipping and Maharashtra cadre IAS officer Malini Shankar and former Deputy Comptroller and Auditor General (CAG) Nand Kishore are part of the new board.

IL&FS ISSUE

- A total of 44 mutual fund schemes had exposure to IL&FS bond papers to the tune of a total of Rs. 3,354 crore as on August end. The net asset values (NAVs) of those funds which held papers on which IL&FS defaulted took a hit.
- What was happening at IL&FS?
  - IL&FS used to borrow mainly from banks – until recently when it began to turn to the corporate bond market.
  - Increase in short term borrowing (less than a year). The proportion of this debt increased to 33% from 20% a year ago. The short tenure loans were used to fund long-term illiquid projects.
  - Even in the good old days many of its projects had a tendency to overshoot their budgets
  - Liquidity mismanagement has caused a major problem
- The new board will have to work out a solution through a combination of measures like asset sales, infusion of capital, liabilities re-structuring etc.

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GLOBAL EVENTS

INTENSIFIED TARIFF WAR

- Trade tensions began in March this year
- The Trump administration has imposed tariffs this year on nearly half of the products that China sells to the United States annually which totals to around $250 billion. President Donald Trump has threatened to expand the tariffs to cover all U.S. imports from China. Beijing has responded with tariffs on American goods worth more than $110 billion.
- According to the IMF, the tit-for-tat trade war is likely to affect the growth of both the major economies.
  - Despite healthy momentum in the United States, which received a boost from recent tax cuts, IMF economists now expect growth to slow to 2.5% next year from 2.9% this year.
  - It expects China's growth rate to fall to 6.2%, from 6.6% this year.
  - It is also expected that overall global growth rate will slow down due to the trade war

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CHINA

- The US imposed tariffs worth $200 billion on Chinese imports in September. This was the biggest round and is likely to be scaled up in 2019. The Donald Trump administration has indicated that it wishes to stop other big economies like Japan and the European Union from negotiating trade deals with China.
- GDP Growth
  - The government is likely to miss the growth target of 6.5% this year
  - There is a slowdown in the credit expansion and government spending
- The Chinese stock market has taken a beating due to poor sentiment on account of multiple factors:
  - Trade war by the US
  - Liquidity drain from stocks due to crack down on shadow banking
  - There is a feeling that the government is focusing on strengthening public sector companies and is turning against entrepreneurs
  - Pressure on the Yuan
- Loose Monetary Policy
  - It is the only economy following an expansionary monetary policy
  - The People's Bank of China (PBOC) recently reduced the banks' reserve requirements by 1%

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US ECONOMY

- Employment
  - There was an improvement in the number of jobs added monthly
  - The unemployment rate fell to a 50-year low of 3.7% in September.

	Jul-18	Aug -18	Sep-18
Jobs added	165,000 (revised)	270,000 (revised)	134,000

- Growth
  - The GDP grew by a strong 4.2% (annual rate) in the April-June'18 quarter – higher than the 2.2% growth reported in the previous quarter
  - The major drivers of growth have been consumer spending, exports and government spending.

- Monetary Policy
  - The US Federal Reserve raised the key policy rate by 25 basis points (bps) to 2-2.25% in September. This was the third rate increase in 2018.
  - It has indicated three further rate hikes in 2019

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RISING CRUDE OIL PRICES

- The Brent Crude oil prices continued to rise and increased by almost $5 to end the quarter at $83/barrel. The year-to-date increase in oil prices is almost 24%
- Some of the factors contributing to a surge in oil prices:
  - Supply constraints is the major driver:
    - Economic and political crises have reduced Venezuela’s productive capacity.
    - Price rise in anticipation of tighter sanctions on Iran by the US, scheduled to take effect in November.
    - At a recent meeting OPEC members decided not to increase supply in response to higher prices
    - Falling inventories
- Oil importing countries like India have been affected. It has affected current account deficits and the currency depreciation. The timing of the oil price increase is really bad for the emerging oil importing countries.
- As global manufacturing exports have slowed oil importers have taken a bigger hit.

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EVENTS TO LOOK OUT FOR

- DOMESTIC
  - Progress of reforms in the Winter session of the Parliament
  - State elections in Rajasthan, Madhya Pradesh, Chhattishgarh and Mizoram
  - Indian Rupee Depreciation
  - Corporate earnings data
  - Inflation numbers
  - GDP growth numbers
- INTERNATIONAL
  - Global Tariff War Developments
  - US Fed Policy
  - Crude Oil Prices
  - Chinese economic indicators

OUTLOOK FOR ASSET CLASSES

Asset Class	Performance in Q3CY18	Start to End Value In Q3	Outlook for Q4CY18	Remarks
Debt	10-Year Gilt: Up 12 bps 3-M T Bill: Up 35 bps 6-M T Bill: Up 5 bps 3-M CP: Up 7 bps 1-Yr CP: Up 55 bps 10-Yr AAA Corp: Up 18 bps Call Rate: Up 31 bps	7.9 – 8.02 6.46 – 6.99 6.86 – 7.36 7.6 – 8.3 8.55 – 9.1 8.61 – 8.79 6.12 – 6.43	The rates are expected to harden for the shorter duration papers while the yields are expected to be stable or downward biased for 10 Yr G Secs	This outlook will be negated if RBI changes its view on inflation or the NBFC crisis of confidence spirals out of control.
Equity	Sensex: Up 2% Nifty: Up 2%	35,423 – 36,227 10,714 – 10,930	Flat with a downward bias for most part of the trading session	Verdicts favourable to the NDA combine in the state elections can flare up the markets

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DISCLAIMER