Bajaj Allianz Life Insurance Company Ltd

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Macro-economic developments

- In an unexpected move, the RBI's Monetary Policy Committee (MPC) kept the key policy rates unchanged but changed stance of monetary policy from 'accommodative' to 'neutral', with all six members of the MPC unanimously citing upside risks to CPI inflation target and external factors like rate hikes by US Fed and volatility in exchange rate.
- RBI's growth projection has been revised downward for FY17 to 6.9% from 7.1%, on account of short run disruptions in economic activity due to cash crunch and slump in demand due to adverse wealth effects due to demonetization. However, RBI expects growth to recover to 7.4% in FY18 on account of revival in discretionary demand held back by demonetization, MCLR reductions and Union Budget's higher allocation for capex, rural economy and housing.
- Currency in circulation reduced by ~ Rs 6.7 trillion from Rs 17.77 trillion in October, 2016 to ~Rs 11 trillion on February 17, 2017 on account of government's demonetization move, however the pace of remonetization has picked up with currency in circulation increasing by ~ Rs 1 trillion in February.
- System Liquidity continues in surplus mode by ~ Rs 6.1 trillion (including cash management bills of Rs 1.5 trillion)
- Fiscal deficit for April'16–January'17 was 5.64 lakh crore viz. 105.7% of 5.34 lakh crore of the budgeted fiscal deficit for FY17 (against 95.8% during the same period last year).
- January CPI inflation moderated to 3.17% YoY as against 3.41% in December; primarily on account of moderation in food inflation to 0.53% YoY in January as against 1.37% in December.
- IIP contracted by 0.4% in December as against expansion by 5.7% in November, primarily on account of contraction in manufacturing sector (2.0%).
- Q3FY17 growth in terms of Gross Value Added (GVA) slowed down marginally to 6.6% as against 6.7% in Q2FY17; with agricultural, industry and services sector growth at 6.0%, 6.6% and 6.8% respectively in Q3FY17 on y-o-y basis
- Brent crude ended flat in February to close at USD55.59/barrel; versus USD55.70/barrel in January.
- INR appreciated by 1.73% in February to close at INR66.69/USD; versus INR67.87/USD in January.

Equity market developments and Outlook

- The Nifty posted healthy gains in Feb'17. The index rose by 3.7% in the month – this was the second consecutive month of a rise; the index had risen by 4.6% in January. The broader market continued to outperform the benchmark index - the NSE500 rose by 4.5% in the month. The NSE500 has risen by a sharp 10.4% in the first two months of the calendar year vis-à-vis an 8.5% rise in the benchmark index. Mid and smallcap stocks posted stellar gains in Feb'17. The NSE mid and smallcap indices rose by 8.3% and 8.1%, respectively.
- Nearly all the NSE sectoral indices rallied in Feb'17. The CNX realty, IT and media indices were the top performers, rising by a sharp 9.8%, 8.5% and 8.1%, respectively, in the month. These were followed by the CNX energy and the bank Nifty, which rose by 5-7%. The CNX auto index was the only loser in February, declining by 1.9%.
- FIIs finally turned positive on Indian equities in Feb'17, after withdrawing money in each of the last four months. The equity purchases exceeded sales by US$1.3bn in the month. Mutual funds, on the other hand, continued to pour money into Indian equities for the 7th straight month in Feb'17. Their equity purchases exceeded sales by US$0.3bn in the month.
- Global equity markets continued their upward journey in Feb'17. US equities posted healthy gains, with the S&P500 rising by 3.7% in the month. The index has rallied by 11.2% in the last 4 months. European markets also gained in Feb'17; the Stoxx Europe 600 (index of 600 European companies) rose by 2.8% in the month. Almost all the European markets closed in the positive territory in February. Likewise, nearly all the Asian markets also closed in the green in February. India was the top performer, followed by Taiwan, China, Hong Kong and Singapore. Japan also closed higher in February.

Fixed Income market developments and Outlook

- 10 year G-Sec yields closed higher at 6.87% in February v/s 6.41% in January, as the absence of rate cut and a change in policy stance to neutral from accommodative took the markets by surprise.
- With the surge in inflow into the banking system, RBI is expected to continue with measures to absorb the surplus liquidity through MSS (Market Stabilization schemes), OMO sales etc.
- We believe that CPI inflation readings would start edging up in coming months due to uptick in commodity prices, waning favorable base effect impact, increasing rural wages & Minimum Support Price and rise in inflation globally.
- Our view is that the monetary pause shall continue for an extended period and at least until H1FY18. We think the yield curve will continue to steepen. The excess liquidity in the banking system and the upward movement in yields present a good investment opportunity in the shorter end of the yield curve.
- Key factors to watch out for will be –impact of demonetization on growth and inflation, pace of US Fed rate hikes, sustained uptick in commodity prices (especially crude), GST framework, and results of upcoming state elections.
- In view of the improving macro-economic dynamics, policyholders would be well placed to benefit from the economic revival, if they continue to remain invested in the India growth story.