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### Macro-economic developments

- RBI's Monetary Policy Committee (MPC) voted 5-1 in favor of reducing policy repo rate. Accordingly, repo rate now stands at 6.00% from 6.25% earlier. The reduction in upside risks to inflation, normal monsoon and smooth roll out of GST gave MPC the room to reduce the policy repo rate.

However, the MPC maintained a cautious forward outlook by taking note of the potential inflationary pressures that may emerge from seasonal spikes in food prices, 7th Pay Commission recommendations, increase in household inflation expectations in June 2017 and high general government deficit exacerbated by farm loan waivers.

- Currency in circulation reduced by ~ ₹2.5 trillion from ₹17.77 trillion in October, 2016 to ~ ₹15.23 trillion on July 14, 2017 on account of government's demonetization move; however the pace of re-monetization seems to have stabilized.
- System Liquidity continues in surplus mode by ~ ₹4.7 trillion (including MSS issuances). With RBI announcing Open Market Operations (OMO) sale of ₹30,000 crore till date, RBI is expected to take further measures such as issuances of securities under Market Stabilization Scheme (MSS), Open Market Operations (OMO) sale etc. to revert the system liquidity to a position closer to neutrality.
- June CPI inflation moderated to 1.54% YoY as against 2.18% in May; primarily on account of decrease in food inflation.
- IIP growth moderated to 1.7% y-o-y in May from a downwardly revised 2.8% y-o-y in April. Manufacturing output growth slowed as firms scaled back production ahead of the GST. While capital goods (-3.9%) and consumer durables output (-4.5%) contracted, consumer non-durables growth (7.9%) held up well.
- US Fed in its July FOMC meeting decided to keep the Fed rate unchanged at 1.00%-1.25%; citing low inflation. US Fed has given indications of starting the exercise of balance sheet reduction soon.
- Brent crude increased by 9.87% in July to close at USD 52.65/barrel; versus USD 47.92/barrel in June.
- INR appreciated by 0.61% in July to close at INR 64.19/USD; versus INR 64.58/USD in June.

### Equity market developments and Outlook

- NIFTY resumed its northward journey in July, rallying +4.59% - it's best monthly performance in over a year. The broader markets were in-line with the NIFTY M50 and Smallcap indices up +4.49% and +5.25% respectively. Change in SEBI regulations that prevented non-SEBI registered investors from taking naked derivative positions also contributed to the rally via short-covering.
- Banking and metal stocks led the rally in July – Bank NIFTY and NSE Metal up 7.29% and 6.55% respectively. Metal stocks were

aided by positive growth data coming out of China which caused a rally in industrial metals (iron-ore, copper). Within banks, PSU Banks were the biggest gainers (Nifty PSU Bank: +10.82%) on the above short-covering theme. The FMCG index was the biggest loser (-7.59%) led by losses in ITC after the GST council increased the cess applicable on cigarettes.

- Flows stayed supportive in July as FIIs poured in ~\$230mn in the markets, while DIIS bought another \$745mn. YTD, FIIs & domestic MFs have bought US\$8.7 bn and US\$7.3 bn in equities respectively
- Global markets also continued their positive trajectory: the S&P returned +1.67% in spite of more political turmoil in the US towards the end of the month. The FTSE stayed flat, but Emerging Markets also rallied with MXAPI up 4.61%, led a 5.64% rally in Hang Seng and a 2.36% rally in the SHCOMP.

### Fixed Income market developments and Outlook

- 10 year G-Sec yields closed lower at 6.44% in July v/s 6.51% in June, due to RBI revising its inflation projection downward opening up room for accommodative policy, higher FII flows, low inflation and abating concerns in US regarding fiscal expansion.
- With the surge in inflow into the banking system, RBI is expected to continue with measures to absorb the surplus liquidity through MSS issuances, OMO sales etc.
- We believe that CPI inflation readings would start edging up in H2FY18 due to waning favorable base effect impact & increasing rural wages and rise in inflation globally.
- Our view is that the interest rate easing cycle has broadly come to an end, possibly with some room for accommodation left, depending on the evolving inflation trajectory over the coming months. We think the yield curve will 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 –progress of monsoon, upcoming US Fed & ECB policy decisions, impact of demonetization on growth and inflation, impact of farm loan waivers on fiscal situation of states, implementation of GST framework and 7th Pay Commission recommendations.
- 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.