Bajaj Allianz Life Insurance Co. Ltd.

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Macro-economic developments

- The Non-farm payrolls in the United States rose by 250,000 in October 2018, higher than market expectations of around 190,000. The unemployment rate remained steady at 3.7%, the lowest since December 1969.
- Revised estimates showed that US GDP growth for Q3 2018 remained unchanged at 3.5%YoY compared to 4.2% in previous quarter and 3.2% in Q3 2017. Consumer spending, which accounts for more than two thirds of U.S. economic activity, grew by 3.6%YoY in Q3 2018.
- At the G-20 summit, US and China agreed to halt new trade tariffs for 90 days, to allow for talks. President Trump agreed not to hike tariffs on $200 billion of Chinese imports from current 10% to 25% from beginning of 2019 (as scheduled earlier), during the ongoing talks.
- Domestically in India, GDP growth for Q2 FY19 came in below expectations, and slowed down to 7.1%YoY during the quarter from 8.2%YoY in the previous quarter. Growth in private consumption, which is the largest component of GDP (~55% weight), slowed down to 7.0%YoY in Q2 FY19 from 8.6%YoY in the previous quarter. However, investments picked up—with Gross Fixed Capital Formation rising to 12.5%YoY in Q2 FY19 from 10.0%YoY in the previous quarter.
- GVA growth also slowed down to 6.9%YoY in Q2 FY19 from 8.0%YoY in the previous quarter. This was primarily due Manufacturing sector, where growth slowed down sharply to 7.4%YoY from 13.5%YoY in the previous quarter. Agriculture sector growth also dropped to 3.8%YoY in Q2 FY19 from 5.3%YoY in the previous quarter. However, Services sector (largest component of GVA) growth remained steady at 7.5%YoY during the quarter.
- Trade deficit data, after surprising positively for the month of September (coming in at $14.0 billion), widened to $17.1 billion for the month of October. However, the recent sharp fall in crude oil prices in November has not been factored into the trade data yet.
- The Index of Industrial Production (IIP) growth slowed down a bit to 4.5%YoY in Sep 2018, from 4.7%YoY in the previous month. Manufacturing sector (which has 78% weight in index) saw growth slowdown to 4.6%YoY in Sep 2018 from 5.1%YoY in the previous month. However, IIP growth for FYTD 19 (upto Sep) was higher at 5.2%YoY, versus 2.6%YoY in the year ago period.
- Consumer Price Index (CPI) headline inflation continued to moderate and came in below expectations at 3.3%YoY in Oct 2018, compare to 3.7%YoY in the previous month. The fall in headline inflation was helped primarily by fall in food inflation (has highest weightage in CPI), which fell to -0.9%YoY in Oct 2018 from 0.5%YoY in the previous month. However, core inflation (ex food & fuel) rose a bit to 6.1%YoY in Oct 2018, from 5.8%YoY in the previous month.
- Crude prices fell sharply in the month of November, with Iran sanction concerns easing, global crude production and inventories rising. Brent crude closed the month at $57.8/bbl—down by a massive 22%.
- The rupee appreciated strongly—by more than 6% against the USD in November, on the back of sharp fall in crude oil prices, reversal of foreign portfolio outflows, and a general recovery seen in most emerging market currencies.

Equity market developments and Outlook

- Indian markets recovered in the month of November, on the back of sharp fall in crude oil prices, strengthening rupee, easing of global trade tariff tensions, reversal in FII outflows and some recovery seen in Emerging and Asian markets. The benchmark Nifty index closed the month up around 5%, while the mid/small-cap segment underperformed a bit, with the Nifty Midcap 50 index and Nifty Small-cap 100 index returning 1.0% and 2.5% respectively in November. Sectors that outperformed during the month included consumer durables, realty, capital goods and banking. Meanwhile, the bottom performing sectors during the month were metals, pharma and power.
- Global markets fared relatively better in the month of November, after seeing a deep correction in the previous month. MSCI Emerging Markets and MSCI Asia Ex Japan indices outperformed, and returned 5.3% and 4.1% respectively, while the MSCI World index returned around 1% during the month.
- In the US, the S&P 500 index returned 1.8%. However, most European markets ended marginally in the red, with the UK's FTSE 100 index falling the most (by 2.1%) during the month. Within Asia, Hong Kong (+6.1%), India (+4.7%) and Indonesia (+4.5%) were the top performers in November.
- Foreign portfolio investors (FPIs) registered a net inflow of ₹6,200 crore in the month of November, after seeing a record net outflow of around ₹27,600 crore in the previous month.
- Domestic Institutional Investor's (DIIs) net investment in equities slowed down considerably to ₹ 800 crore in the month November (primarily due to slowdown in buying by mutual funds), after registering a record high net investment of around ₹26,000 crore in the previous month.
- Some of the earlier 'headwinds' like crude oil, weak rupee, foreign outflows, rising interest rates & bond yields etc. have improved considerably and turned into 'tailwinds' lately. This broadly augurs well for the Indian economy and markets in general.
- Recently concluded Q2 FY19 corporate earnings were slightly below expectations, but we expect earnings growth to pick up in H2 FY19 and FY20, and this should help to guide the direction of markets.

Fixed Income market developments and Outlook

- Bond yields continued to soften during the month on the back of sharp fall in crude oil price, strengthening rupee, lower than expected inflation, liquidity infusion by RBI via OMOs, and reversal of foreign outflows. The benchmark 10 year bond yield closed the month at 7.61%--down 24 bps for the month. The 10 year yield has softened significantly from its recent peak of above 8.2% in early October.
- With liquidity being tight within the system, the RBI has been proactive on the liquidity front, by announcing liquidity infusion through OMO (Open Market Operation) purchases. It conducted OMO purchases of ₹36,000 crore in October, ₹ 40,000 crore in November, and announced OMO purchases of ₹ 40,000 crore in December.
- India's fiscal deficit for FYTD 19 (upto October) reached 104% of the budgeted full year target, compared to 96% in the year ago period. The fiscal deficit was elevated, primarily due to lower GST collections, lower than budgeted divestment proceeds and increase in capital expenditure.
- Foreign Portfolio Investors (FPIs) in debt markets registered a net inflow of ₹6,468 crore, after seeing a net outflow of around ₹ 10,000 crore in the previous month.
- Post the close of the month, in its December 5, 2018 policy review, the RBI kept the policy repo rate and stance unchanged, as expected. CPI headline inflation forecast was cut substantially, giving a dovish undertone to the monetary policy. GDP growth forecast for FY19 was retained at 7.4%. RBI also announced SLR cut by 25 bps from beginning of 2019 to 19.25%, followed by progressive cuts every quarter until the SLR comes to 18%.
- The RBI governor indicated that if upside risks to inflation (mentioned in the policy) do not materialize, then it could open up space for future policy action—therefore keeping it data dependent. We had increased duration in our portfolios over the past month, and with yields having already factored in the outcome of the policy, we now prefer the shorter to medium term segment of the yield curve.

Ver: Nov 2018