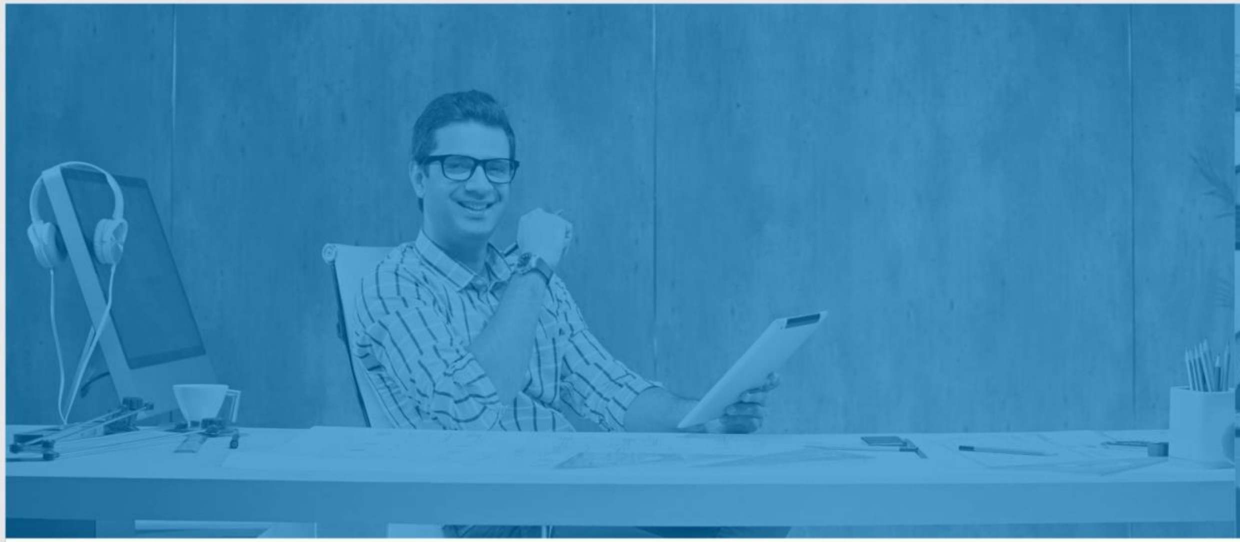
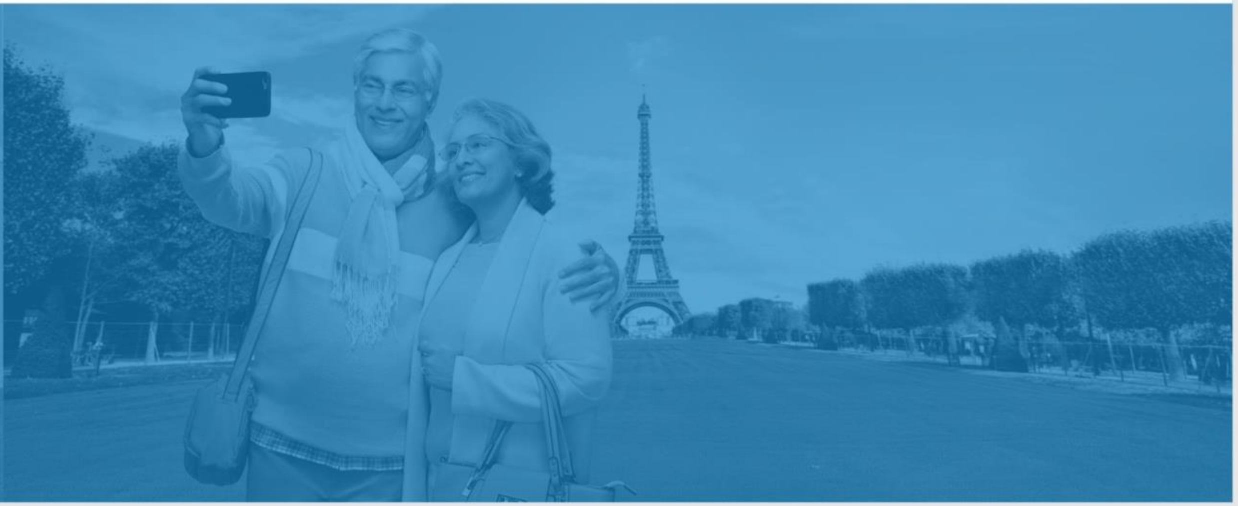



Year-End Review and Outlook for 2019

December 2018

LIFE GOALS. **DONE.**

BAJAJ | Allianz

Global Macro & Markets

US Fed has turned a bit dovish lately, leading to some softening of US bond yields

US 10 year Treasury Yield

US Fed – Dec 2018 meeting projections

Percent

Variable	Median[1] 2018	2019	2020	2021
Change in real GDP	3.0	2.3	2.0	1.8
September projection	3.1	2.5	2.0	1.8
Unemployment rate	3.7	3.5	3.6	3.8
September projection	3.7	3.5	3.5	3.7
PCE inflation	1.9	1.9	2.1	2.1
September projection	2.1	2.0	2.1	2.1
Core PCE inflation[4]	1.9	2.0	2.0	2.0
September projection	2.0	2.1	2.1	2.1
Federal funds rate	2.4	2.9	3.1	3.1
September projection	2.4	3.1	3.4	3.4

- US Fed hiked rates by 25 bps (as expected) in its Dec 2018 policy review, making it the fourth rate hike in CY2018.
- However, the Fed turned a bit dovish, by cutting its interest rate projection for 2019 to 2 rate hikes (from 3 rate hikes earlier), and also cut the median target rate for 2020 and 2021.
- US 10 yr bond yield softened from 3.2% to 2.7%. Global bond yields in Germany, Japan and UK have softened too, lately. Global growth slowdown concerns have also weighed.
- European Central Bank (ECB), which was tapering its QE, finally ended it in Dec 2018. It maintained that interest rates would be kept at record lows at least through summer of 2019.

Source: US FOMC, Bloomberg

Some global growth slowdown expected in 2019, although India still projected to be the fastest growing major economy

IMF GDP growth forecast (in %)

		Projections		Difference from July 2018 *WEO Update*[1]	
	2017	2018	2019	2018	2019
World Output	3.7	3.7	3.7	–0.2	–0.2
Advanced Economies	2.3	2.4	2.1	0.0	–0.1
United States	2.2	2.9	2.5	0.0	–0.2
Euro Area	2.4	2.0	1.9	–0.2	0.0
Germany	2.5	1.9	1.9	–0.3	–0.2
France	2.3	1.6	1.6	–0.2	–0.1
Italy	1.5	1.2	1.0	0.0	0.0
Spain	3.0	2.7	2.2	–0.1	0.0
Japan	1.7	1.1	0.9	0.1	0.0
United Kingdom	1.7	1.4	1.5	0.0	0.0
Canada	3.0	2.1	2.0	0.0	0.0
Other Advanced Economies[2]	2.8	2.8	2.5	0.0	–0.2
Emerging Market and Developing Economies	4.7	4.7	4.7	–0.2	–0.4
Commonwealth of Independent States	2.1	2.3	2.4	0.0	0.2
Russia	1.5	1.7	1.8	0.0	0.3
Excluding Russia	3.6	3.9	3.6	0.3	–0.1
Emerging and Developing Asia	6.5	6.5	6.3	0.0	–0.2
China	6.9	6.6	6.2	0.0	–0.2
India[3]	6.7	7.3	7.4	0.0	–0.1
ASEAN-5[4]	5.3	5.3	5.2	0.0	–0.1
Emerging and Developing Europe	6.0	3.8	2.0	–0.5	–1.6
Latin America and the Caribbean	1.3	1.2	2.2	–0.4	–0.4
Brazil	1.0	1.4	2.4	–0.4	–0.1
Mexico	2.0	2.2	2.5	–0.1	–0.2

- IMF cut global growth forecast by 0.2% (from July forecast) for both 2018 & 2019 to 3.7%
- Advanced economies growth expected to slow in 2019, led by the US.
  - IMF projects US GDP growth to slowdown from 2.9% in 2018 to 2.5% in 2019, on account of trade wars
  - US Fed projects US GDP growth to slowdown from 3.0% in 2018 to 2.3% in 2019
- IMF forecasts India's GDP growth to pick up from 6.7% in FY18 to 7.3% in FY19 and 7.4% in FY20.
- This is despite IMF cutting growth forecast for Emerging Markets for both 2018 & 2019 recently.
- China's GDP growth projected to slowdown to 6.2% in 2019, from 6.6% in 2018

Source: IMF World Economic Outlook, October 2018. For India, fiscal year ended March is considered, so 2018 = FY19 and 2019 = FY20. For other countries it is calendar year.

Amidst the correction in global markets, India has fared relatively well and been one of the top performers in 2018

Performance of International Indices (ended Dec 2018 in %)					
Index Name	Country / Region	3 mths	1 Yr	3 Yrs	5 Yrs
BOVESPA	Brazil	10.8	15.0	26.6	11.3
Nifty 50	**India**	**-0.6**	**3.2**	**11.0**	**11.5**
JSX Composite	Indonesia	3.6	-2.5	10.5	7.7
FTSE Bursa Malaysia KLCI	Malaysia	-5.7	-5.9	0.0	-2.0
S&P 500 PR	US	-14.0	-6.2	7.0	6.3
RTS RTSI PR USD	Russia	-10.3	-7.4	12.2	-5.8
TSEC TAIEX	Taiwan	-11.6	-8.6	5.3	2.5
FTSE/SGX STI	Singapore	-5.8	-9.8	2.1	-0.6
MSCI World PR USD	World	-13.7	-10.4	4.2	2.5
CAC 40	France	-13.9	-11.0	0.7	1.9
FTSE SET All Share	Thailand	-11.1	-11.1	6.6	3.5
Nikkei 225	Japan	-17.0	-12.1	1.7	4.2
FTSE 100 PR GBP	UK	-10.4	-12.5	2.5	-0.1
Hang Seng	Hong Kong	-7.0	-13.6	5.7	2.1
MSCI Asia Ex Japan PR USD	Asia Ex Japan	-9.0	-16.4	6.1	1.6
MSCI EM PR USD	Emerging Mkts	-7.8	-16.6	6.7	-0.7
KOSPI Korea	Korea	-12.9	-17.3	1.3	0.3
FSE DAX TR	Germany	-13.8	-18.3	-0.6	2.0
Shanghai Composite	China	-11.6	-24.6	-11.0	3.3

Source: Morningstar Direct. Returns are in local currency of index, and returns greater than 1 year are CAGR
Date sorted on the basis of 1 Year return in descending order

- Despite the correction in global markets in 2018, India has managed to fare well, and been one of the top performing markets in 2018.
- China has been one of the bottom performing markets this year, and some other peer Asian and emerging markets (EMs) have also seen significant correction this year.
- Over the long term (5 years) too, India has been one of the top performing markets globally.

Domestic Macro-economic Scenario

Some of the earlier headwinds have stabilized, and turned into tailwinds

Crude oil prices have fallen sharply

Rupee has appreciated after touching life-time lows

The credit & liquidity crunch post the ILF&S default has stabilized

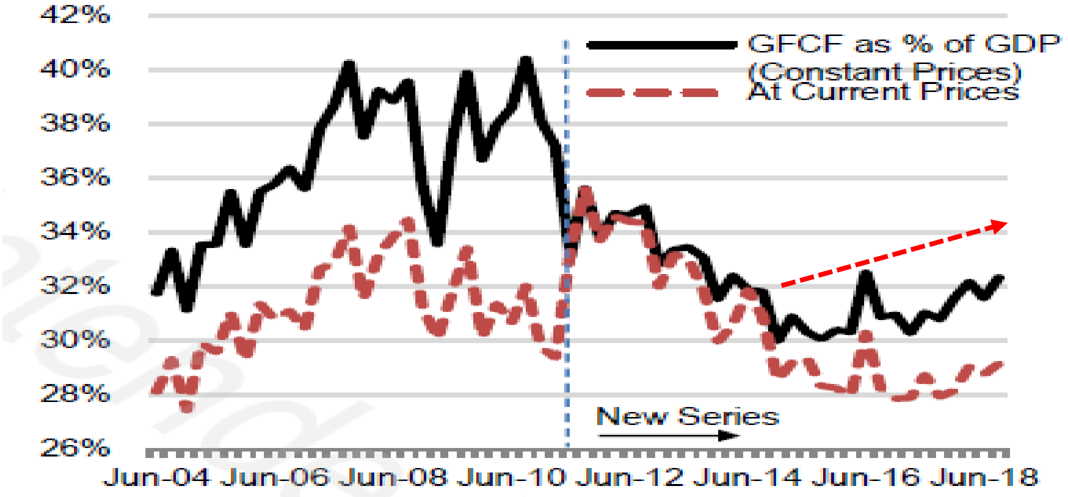
Bond yields have softened significantly

Some reversal seen in foreign outflows

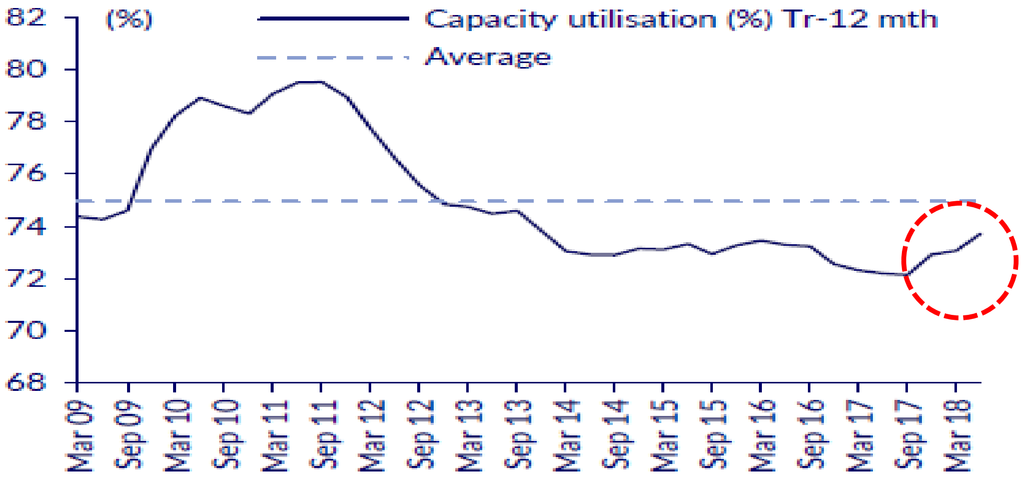
Valuations have become more reasonable

The capex (investment) cycle seems to have bottomed out, and we expect a gradual recovery

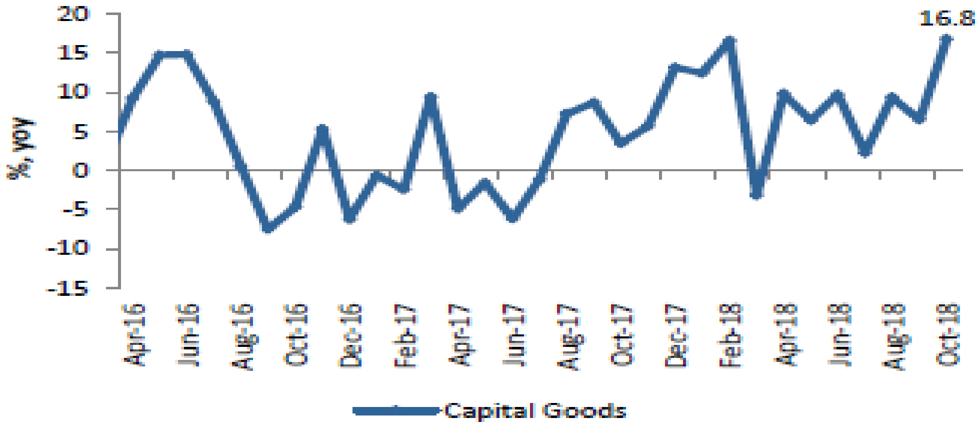
Gross Fixed Capital Formation (Investments) as % of GDP has bottomed out, and is recovering



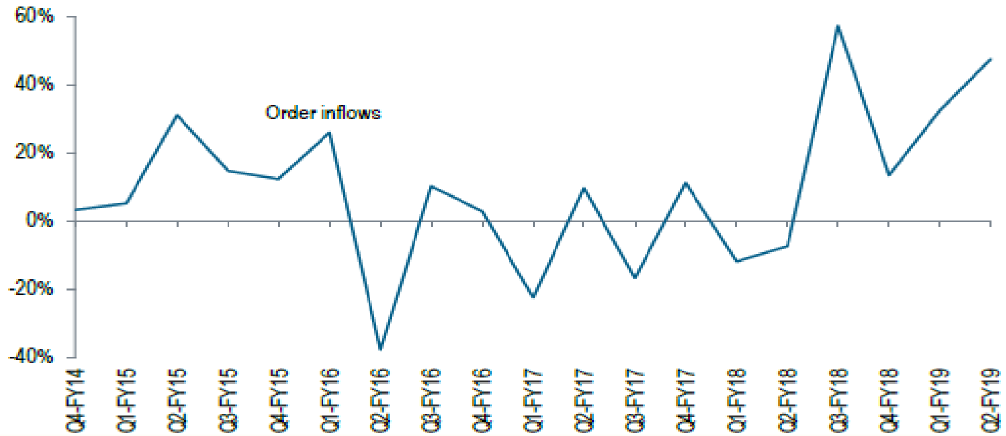
Industry Capacity Utilization Rate also showing signs of recovery



Capital Goods sector Output is picking up



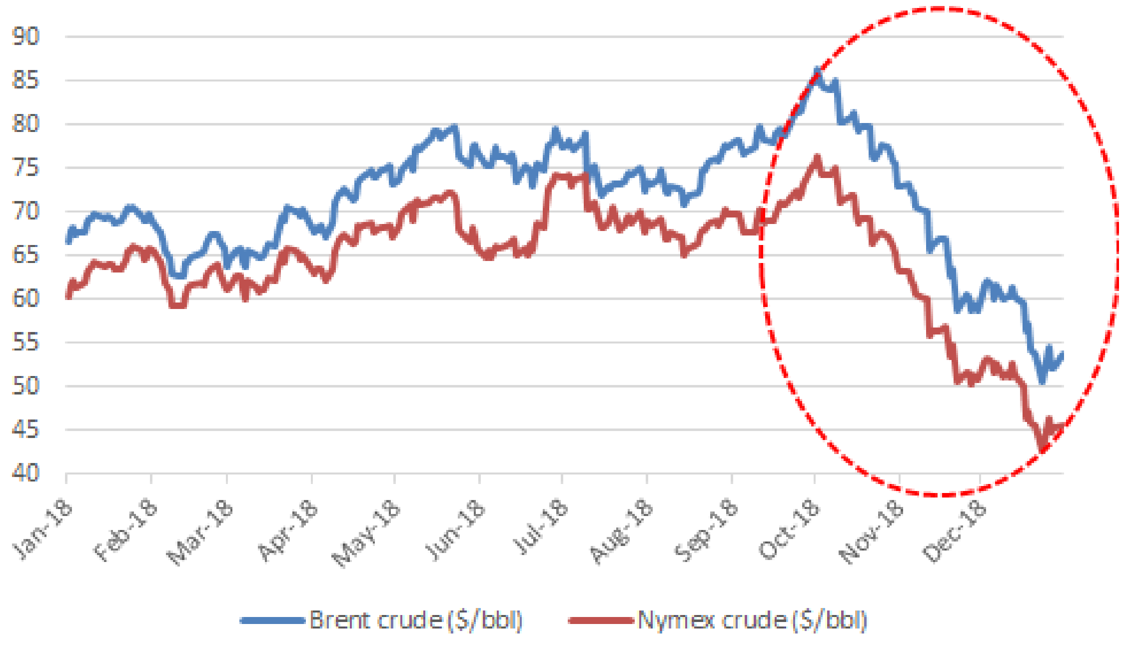
Order inflows of large industrial companies* picking up



Source: Credit Suissse, CLSA, Phillip Capital, Standard Chartered. * Order inflows growth (YoY %) is of the six largest industrial companies

Crude has fallen off a cliff over the past few months

Brent & Nymex Crude Price ($/bbl.)



Source: Bloomberg

- Brent crude has fallen from a recent high of around $86/bbl in early October to ~$54/bbl mark at the end of 2018. This has been helped by easing sanctions on Iran, unwinding of long speculative positions, significant increase in crude production particularly from the US, and expectation of some slowdown in global growth.
- This a boon for India, which is a large net oil importer, and oil imports account for around 80% of domestic oil demand. Will help to mitigate earlier concerns on current account deficit & inflation (to some extent).

The rupee has also recovered from its life-time lows, and stabilized lately

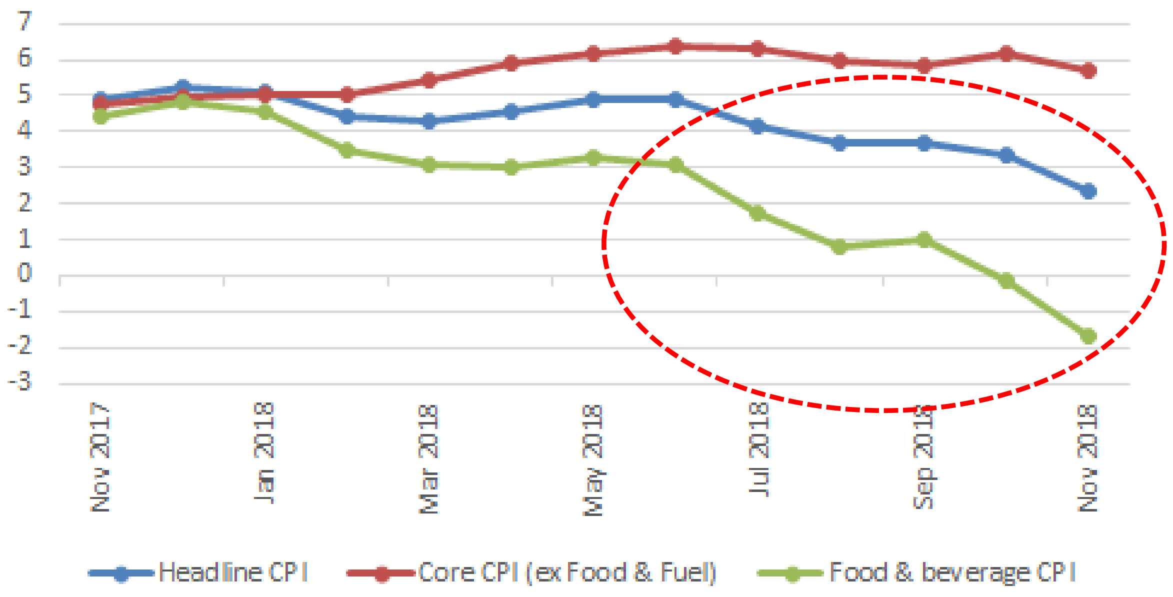
Peformance of Various Currencies against USD (in %, as of Dec 2018)					
Name	2 mths	6 mths	1 Yr	3 Yrs	5 Yrs
Japanese Yen	2.9	1.0	2.7	3.1	-0.9
Thai Baht	1.8	1.8	0.1	3.4	0.2
Hong Kong Dollar	0.1	0.2	-0.2	-0.3	-0.2
Swiss Franc	2.0	0.7	-1.1	0.5	-2.0
Singapore Dollar	1.6	0.0	-2.0	1.3	-1.5
Malaysian Ringgit	1.3	-2.3	-2.1	1.3	-4.5
Euro	0.9	-2.1	-4.8	1.7	-3.7
Yuan Renminbi	1.6	-3.5	-5.2	-1.8	-2.5
Indonesian Rupiah	5.7	-0.3	-5.7	-1.4	-3.3
Pound Sterling	-0.3	-3.5	-5.9	-4.8	-5.1
Indian Rupee	**5.9**	**-1.9**	**-8.6**	**-1.8**	**-2.4**
Australian Dollar	-0.7	-4.7	-10.0	-1.1	-4.7
South African Rand	2.7	-4.7	-13.9	2.5	-6.1
Brazilian Real	-4.2	-0.7	-14.4	0.7	-9.5
Russian Ruble	-5.2	-9.6	-17.0	1.7	-13.9
Pakistan Rupee	-4.6	-12.5	-20.5	-9.0	-5.4
Turkish Lira	5.3	-13.9	-28.7	-18.1	-16.6
Argentine Peso	-4.0	-23.4	-50.0	-30.0	-29.6

Source: Morningstar Direct. Data sorted on the basis of 1 Yr Return.
Returns greater than 1 year are CAGR

- After touching a life-time low of ~74.5/USD in early October, the rupee has appreciated recently and closed the year around the 70/USD mark.
- This has been on the back of sharp fall in crude oil prices, reversal in foreign outflows, and a general recovery in most emerging market currencies.
- Some of the other emerging market (EM) currencies like Argentine Peso, Turkish Lira, Pakistan Rupee, Brazilian Real, Russian Ruble, and South African Rand have seen a sharper depreciation in 2018.
- The rupee is relatively better positioned than during the Taper Tantrum of 2013, when it had lost more than 20% intra-year.
- Also, over the long term (5 years), the rupee has fared relatively better than most other peer EM currencies.

Inflation has moderated, and came in below expectations

CPI Inflation & its Components (% YoY)



Source: Bloomberg

- Consumer Price Index (CPI) headline inflation continued to moderate and came in below expectations at 2.3%YoY in Nov 2018, down from 5.2%YoY at the end of 2017. Inflation remains well below the RBI's 4%(+/-2%) target.
- The fall in headline inflation was helped primarily by fall in food inflation (has highest weightage in CPI), with food & beverage inflation falling to negative territory of -1.7%YoY in Nov 2018 from ~5%YoY at the end of 2017.
- Core inflation (ex food & fuel) has also moderated to 5.8%YoY in Nov 2018, but still remains relatively a bit elevated.

GDP & GVA growth has been recovering, but slowed down in Q2 FY19

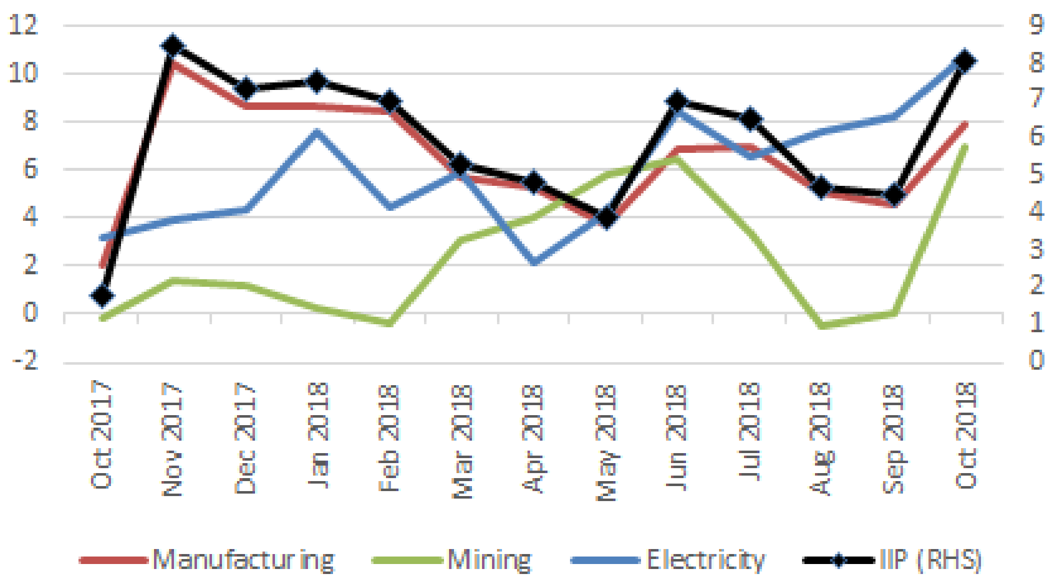
% y-o-y	2017 Q2	2017 Q3	2017 Q4	2018 Q1	2018 Q2	2018 Q3
Real GDP (market prices)	**5.6**	**6.3**	**7.0**	**7.7**	**8.2**	**7.1**
Private consumption	6.9	6.8	5.9	6.7	8.6	7.0
Government spending	17.6	3.8	6.8	16.9	7.6	12.7
Fixed Investment	0.8	6.1	9.1	14.4	10.0	12.5
Exports	5.9	6.8	6.2	3.6	12.7	13.4
Imports	18.5	10.0	10.5	10.9	12.5	25.6
Real GVA (basic prices)	**5.6**	**6.1**	**6.6**	**7.6**	**8.0**	**6.9**
Agriculture	3.0	2.6	3.1	4.5	5.3	3.8
Industry	(0.4)	7.1	7.3	8.0	10.8	6.5
Mining	1.7	6.9	1.4	2.7	0.1	(2.4)
Manufacturing	(1.8)	7.1	8.5	9.1	13.5	7.4
Utilities	7.1	7.7	6.1	7.7	7.3	9.2
Services	8.5	6.4	7.5	8.2	7.5	7.5
Construction	1.8	3.1	6.6	11.5	8.7	7.8
Trade, Hotels, Transport, Comm	8.4	8.5	8.5	6.8	6.7	6.8
Finance, Real Estate & Prof. Service	8.4	6.1	6.9	5.0	6.5	6.3
Public Administration, Defence etc	13.5	6.1	7.7	13.3	9.9	10.9

Source: Nomura

- GDP growth for Q2 FY19 slowed down to 7.1%YoY from a robust 8.2%YoY in the previous quarter
  - Growth in private consumption, (largest component of GDP with ~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 to manufacturing sector, where growth slowed down to 7.4%YoY from 13.5%YoY in the previous quarter. Agriculture sector growth also dropped.
  - However, services sector (largest component of GVA) growth remained steady at 7.5%YoY during the quarter.
- RBI retained GDP growth forecast of 7.4% for FY19 in its Dec 2018 policy review. Recently, CSO projected GDP growth at 7.2% for FY19 (as per advance estimates), up from 6.7% in FY18.

Industrial Production picks up

IIP & Industry Components Growth (%YoY)

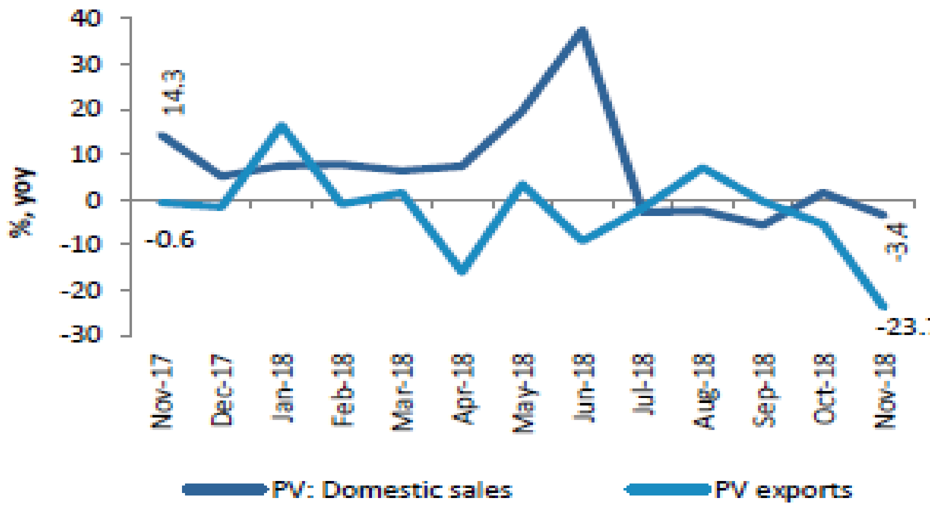


Source: Bloomberg

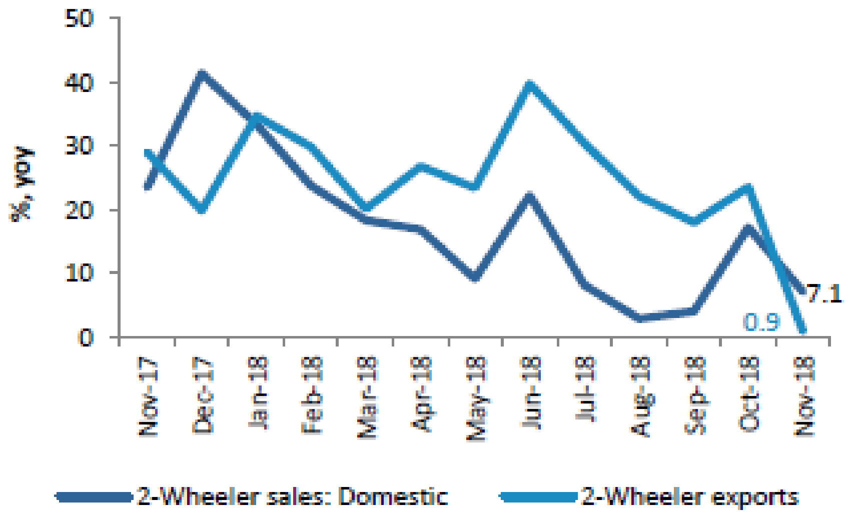
- Index of Industrial Production (IIP) was a bit volatile during the course of the year, but recently picked up to 8.1%YoY in October 2018, from 4.5%YoY in the previous month—helped by a favourable base effect.
- Manufacturing sector (78% weight in IIP) growth rose to 7.9%YoY, from 4.5%YoY in the previous month.
- For FYTD19 (upto October) IIP growth was stronger at 5.6%YoY, compared to just 2.5%YoY in the corresponding period, a year ago.

High Frequency Indicators: Auto sector sees some slowdown

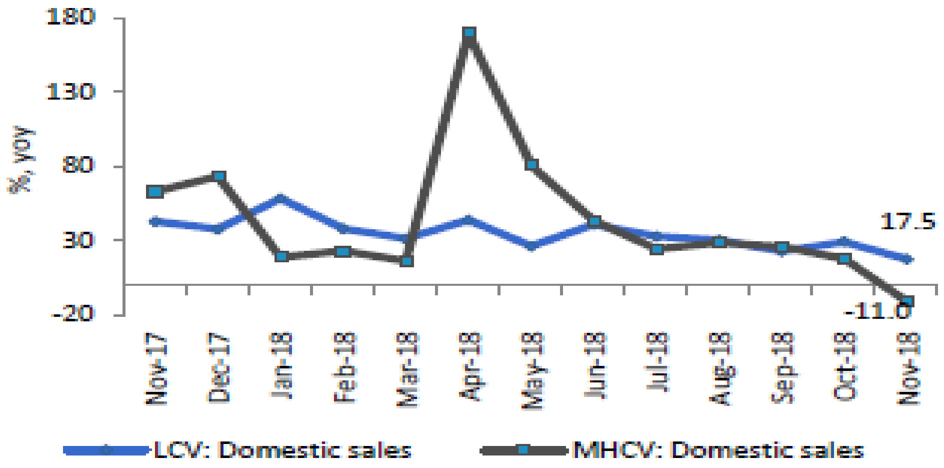
Monthly Passenger Vehicles Sales Growth(%YoY)



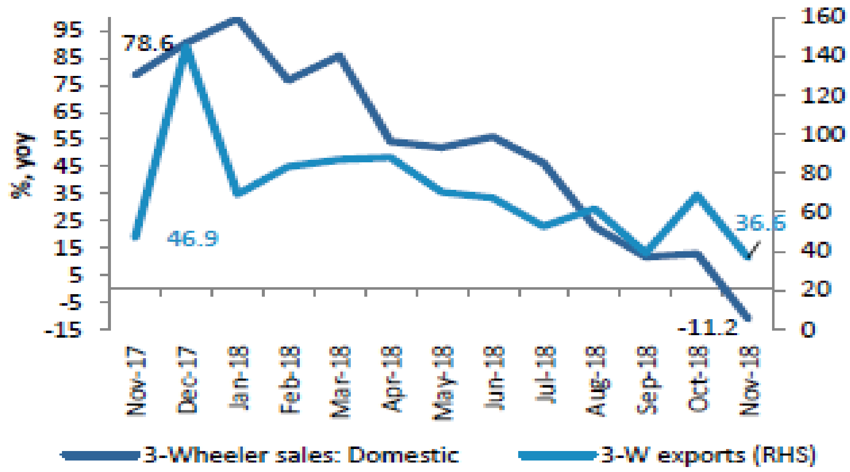
Monthly 2-Wheeler Sales Growth(%YoY)



Monthly Commercial Vehicles Sales Growth(%YoY)



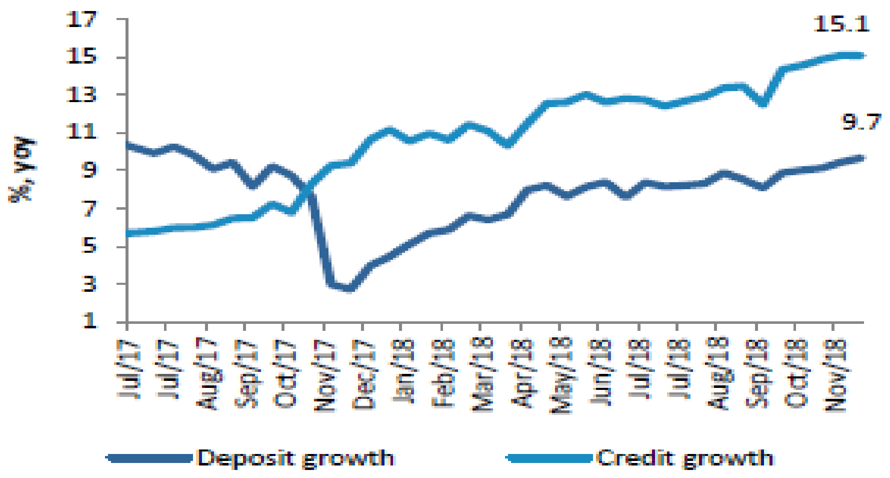
Monthly 3-Wheeler Sales Growth(%YoY)



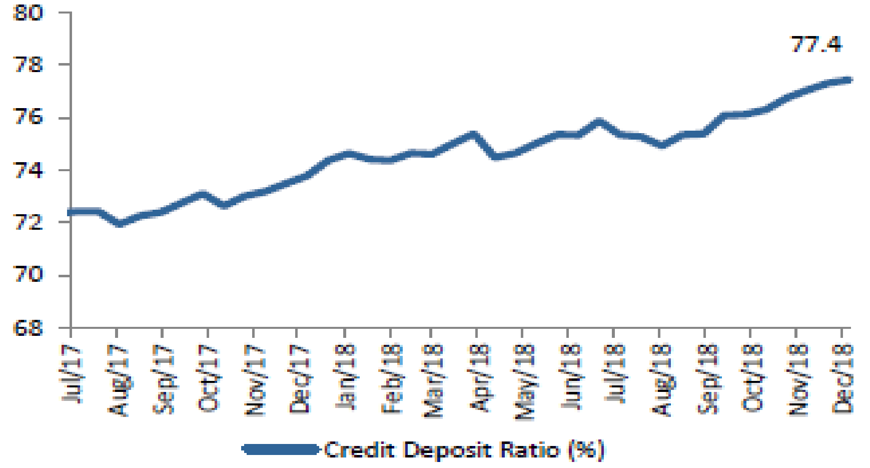
Source: SIAM, Spark Capital. LCV – Light Commercial Vehicle, MHCV = Medium & Heavy Commercial Vehicle

High Frequency Indicators: Credit growth picks up strongly. Steel & Cement output registers moderate growth, while coal output dips

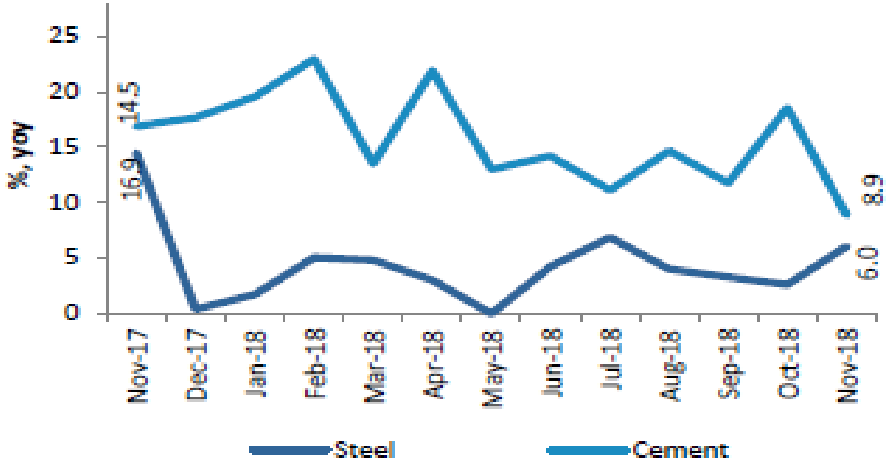
Credit & Deposit Growth (%YoY)



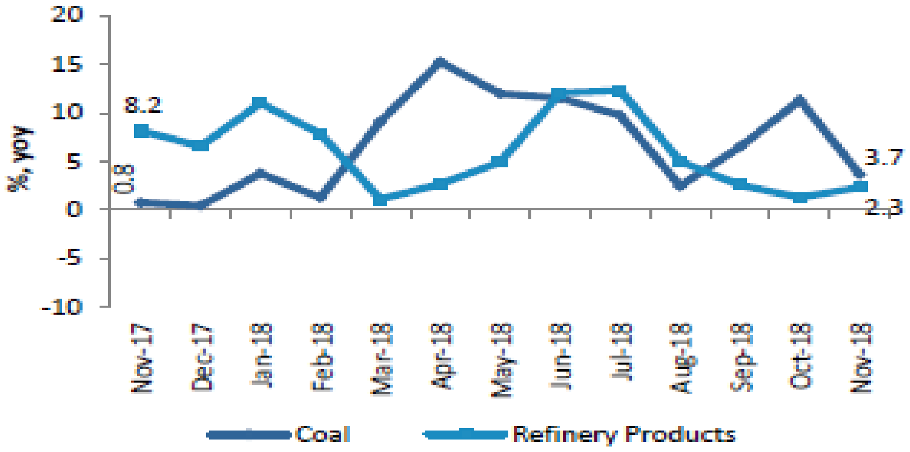
Credit to Deposit Ratio – Picks up



Monthly Steel & Cement Output (%YoY)



Monthly Coal & Refinery products Output (%YoY)



Source: Spark Capital

CAD & BoP outlook to improve with the sharp fall in crude & improvement in capital flows

India CAD & BOP Quarterly Trend ($ in billion)

(US$ Billion)	Q2FY17	Q3FY17	Q4FY17	Q1FY18	Q2FY18	Q3FY18	Q4FY18	Q1FY19	Q2FY19
Exports	67.4	68.8	77.4	73.1	76.1	77.5	82.2	83.4	83.4
Imports	93.1	102.0	107.1	115.1	108.5	121.6	123.8	129.1	133.4
Trade Balance	-25.6	-33.3	-29.7	-41.9	-32.5	-44.0	-41.6	-45.8	-50.0
Net invisibles	22.2	25.3	26.3	27.0	25.5	30.3	28.6	29.8	30.9
Current Account Balance	-3.4	-8.0	-3.5	-15.0	-7.0	-13.7	-13.1	-15.9	-19.1
CAD (% of GDP)	0.6	1.4	0.6	2.5	1.1	2.0	1.9	2.4	2.9
Capital Account	12.8	6.1	10.4	26.9	16.9	22.5	25.0	5.4	16.3
Balance of Payment (BoP)	8.5	-1.2	7.3	11.4	9.5	9.4	13.2	-11.3	-1.9

Source: RBI, Phillip Capital

CAD & BOP Fiscal Year Trend & Forecast

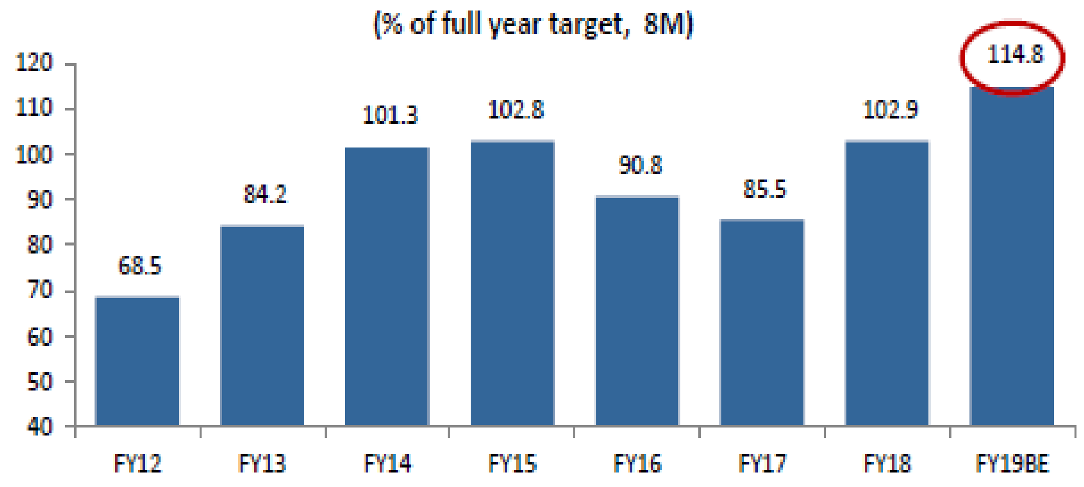
India Current Account Balance & Balance of Payments Trends ($ bn)				
	FY17	FY18	FY19 (F)	FY20 (F)
Exports	280.1	309	333.1	351.4
Imports	392.6	469	516.3	547.2
Trade Account	**-112.4**	**-160**	**-183.2**	**-195.8**
% of GDP	-4.9	-6.2	-6.9	-6.7
Invisibles	98.1	111.4	121	130.4
% of GDP	4.3	4.3	4.5	4.5
Current Account	**-14.4**	**-48.7**	**-62.3**	**-65.4**
% of GDP	**-0.6**	**-1.9**	**-2.3**	**-2.2**
Capital Account	**36.4**	**91.3**	**42.7**	**77.1**
% of GDP	**1.6**	**3.5**	**1.6**	**2.6**
Overall BOP	**21.5**	**43.6**	**-19.6**	**11.7**

Source: RBI, Bajaj Allianz Life Insurance Research. F = Forecast

- Current Account Deficit (CAD) widened to 2.9% (of GDP) in Q2 FY19 from 2.4% in the previous quarter, primarily due to higher imports—leading to widening of the trade deficit. However, this data does not factor-in the sharp fall in crude oil prices (from Oct). CAD for FY19 now projected at around 2.3% of GDP (compared to 2.8-3.0% of GDP earlier).
- Capital account flows jumped to $16.3 bln in Q2 FY19, from a 2-year low of $5.4 bln in the previous quarter. This was helped by lower FPI outflows, higher short-term trade credits and healthy FDI flows
- With the pick-up in capital account flows, the Balance of Payments (BoP) position improved to -$1.9 bln during the quarter, from -$11.3 bln in the previous quarter.

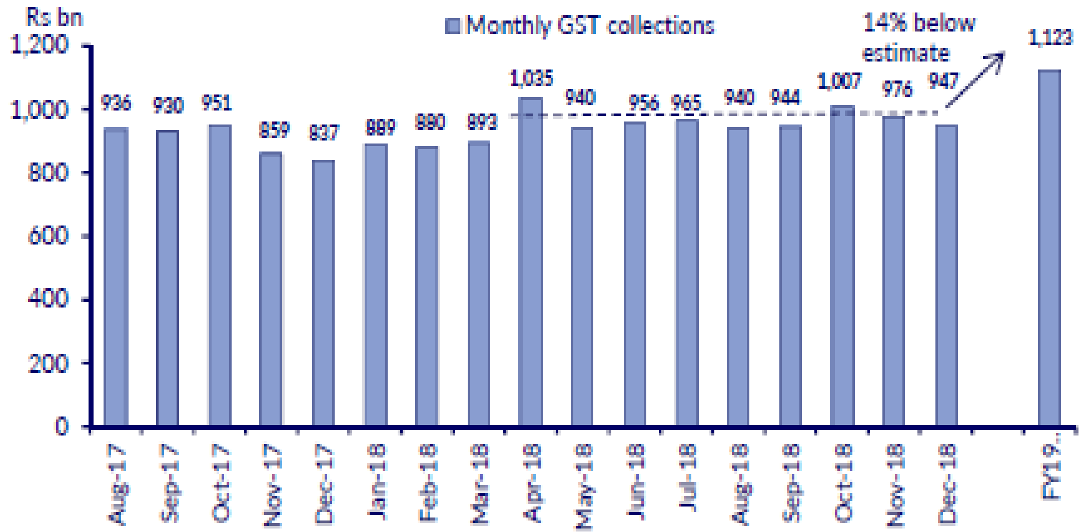
Fiscal deficit a bit elevated, and we may see some minor slippage

8 mth (Apr – Nov FYTD) Fiscal Deficit as % of Full Year Target



Source: CGA, Spark Capital

Monthly GST Collections Trend (INR in bln)



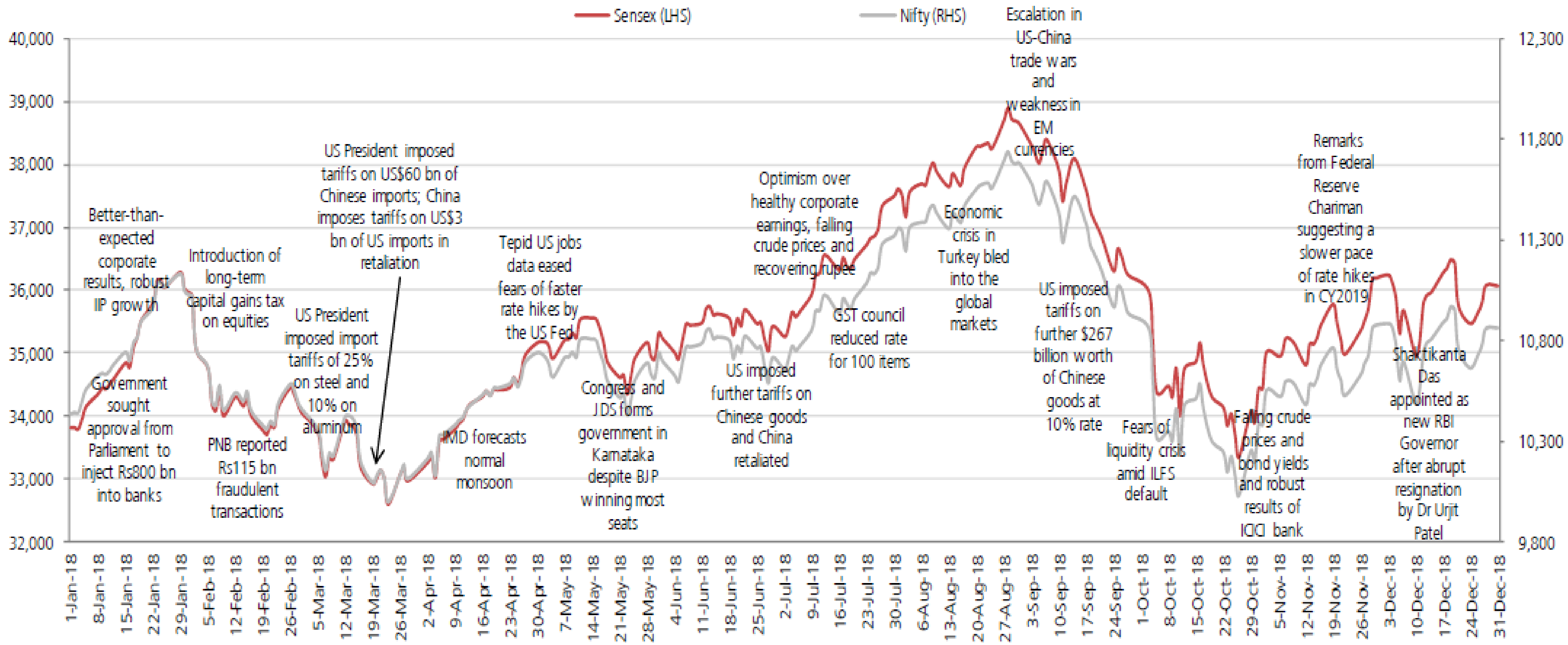
Source: CLSA, Ministry of Finance

- Fiscal deficit for FYTD 19 (up to Nov) was 115% of the full year target—making it one of the highest, compared to the corresponding period of past fiscal years. The fiscal deficit was elevated, primarily due to lower GST collections and lower than budgeted divestment proceeds.
- GST collections were at a monthly run-rate of Rs. 968 bln/month, missing the government budgeted estimates of Rs. 1.12 trln / month.
- Fiscal deficit is budgeted at 3.3% of GDP in FY19 (compared to 3.5% of GDP in FY18), and we may see some minor fiscal slippage this year.

Equity Markets, Valuations, Earnings & Flows

Indian Equity Markets- The Year that Was:

Movement of Sensex & Nifty Indices along with Key Events in CY 2018



Source: Bloomberg, Kotak Institutional Equities

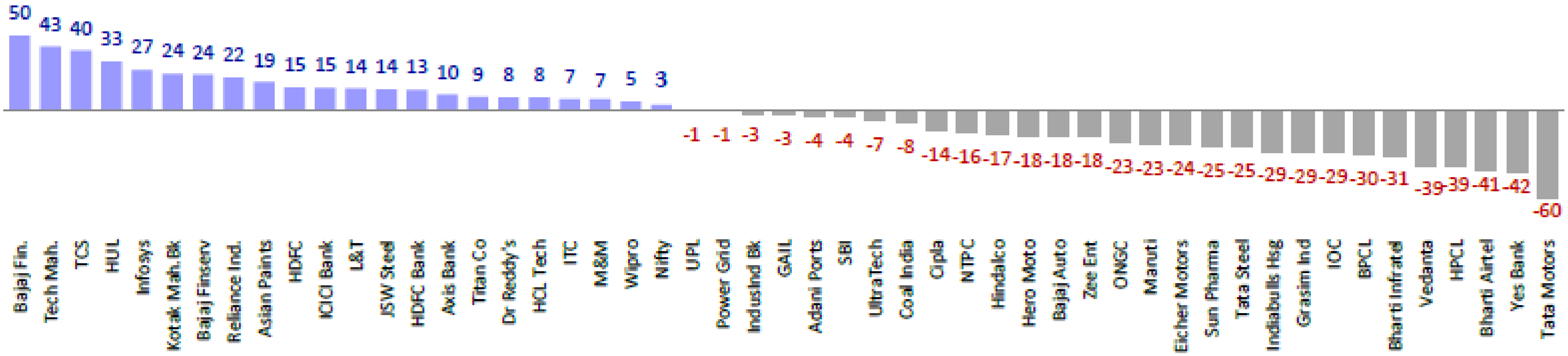
Domestically it was a narrow market. IT, FMCG and banking were the top sectors; mid/small-caps underperform

Performance of Domestic Indices in % (ended Dec 2018)					
Index Name	**3 mths**	**6 mths**	**1 Yr**	**3 Yrs**	**5 Yrs**
S&P BSE IT	-9.8	1.2	24.9	8.4	9.2
S&P BSE FMCG	2.8	5.5	10.6	14.5	12.5
S&P BSE BANKEX	8.5	3.8	5.3	16.3	18.5
Nifty 50	-0.6	1.4	3.2	11.0	11.5
S&P BSE Capital Goods	10.0	7.6	-1.6	10.0	12.9
Nifty 500	0.6	0.1	-3.4	10.9	13.3
S&P BSE Healthcare	-7.3	-0.6	-5.9	-6.3	6.9
S&P BSE Consumer Durables	8.2	2.4	-8.8	19.9	28.9
Nifty Midcap 50	6.7	1.7	-11.0	13.0	16.4
S&P BSE Oil and Gas	-7.5	0.7	-15.6	12.9	9.2
S&P BSE Power	3.6	2.7	-16.1	0.7	3.3
S&P BSE Metal	-10.8	-9.4	-20.7	17.0	3.5
S&P BSE Auto	-3.0	-12.6	-22.1	4.0	11.2
NIFTY Smallcap 100	4.8	-10.2	-29.1	4.5	13.6
S&P BSE Realty	5.6	-13.3	-31.1	10.2	4.6

Source: Morningstar Direct. Data sorted in descending order on the basis of 1 Year return.
Returns more than 1 year is CAGR

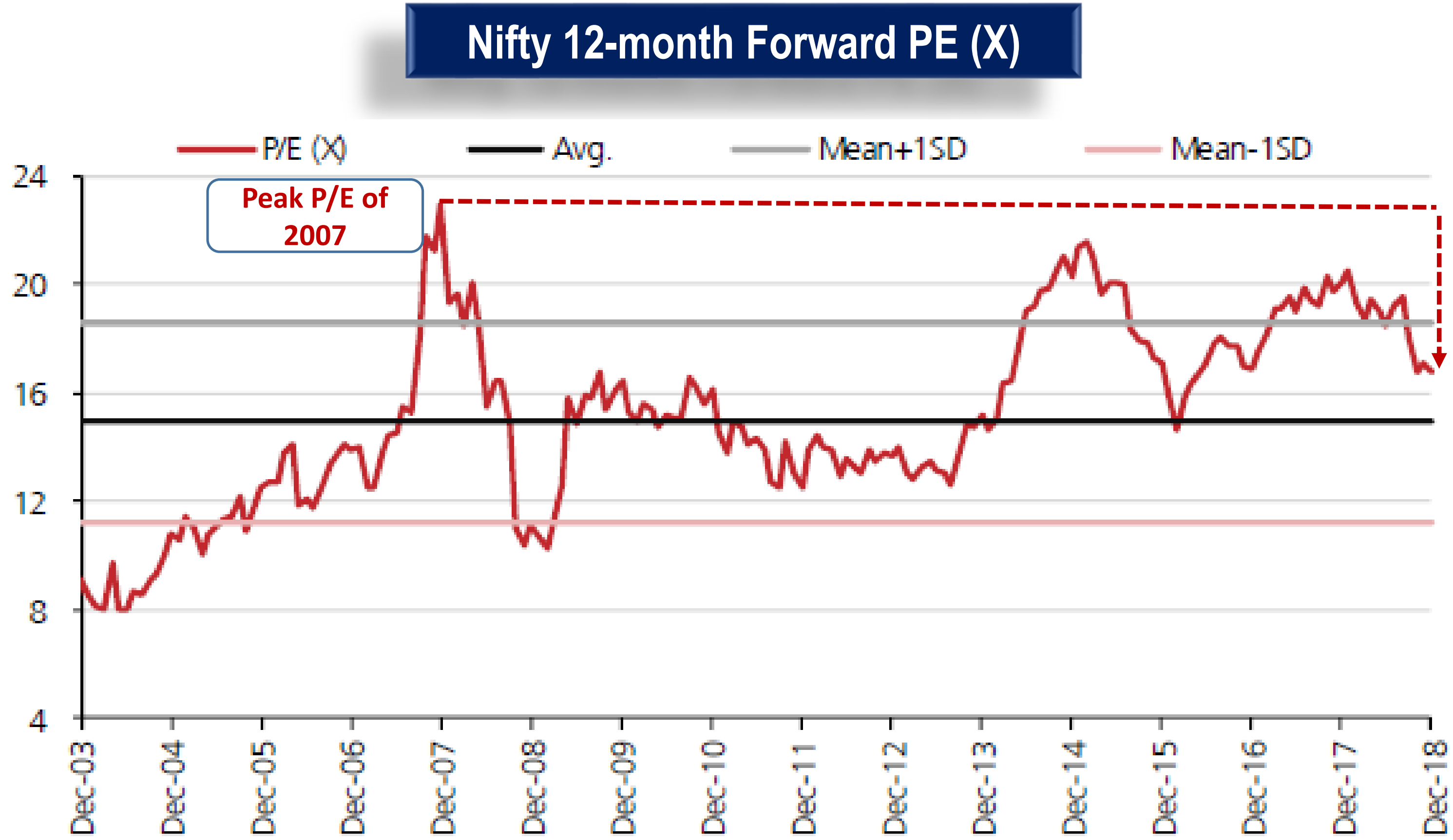
- It was a narrow market in 2018, with bulk of the Nifty returns being contributed by a handful of stocks.
- The mid / small-cap segment underperformed significantly in 2018.
- The top performing sectors in CY 2018 were IT, FMCG and banking.
- The bottom performing sectors in CY 2018 were Realty, Auto and Metals.

Top & Bottom Performing Nifty Index Stocks in CY 2018, (%)



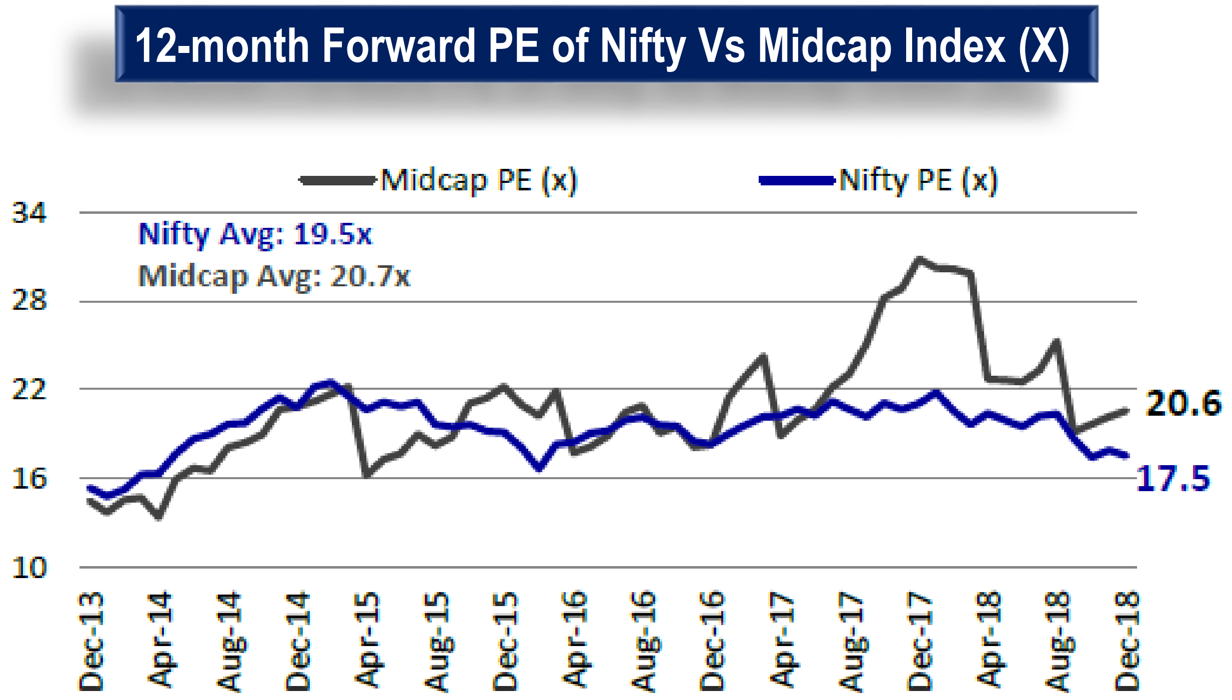
Source: Motilal Oswal

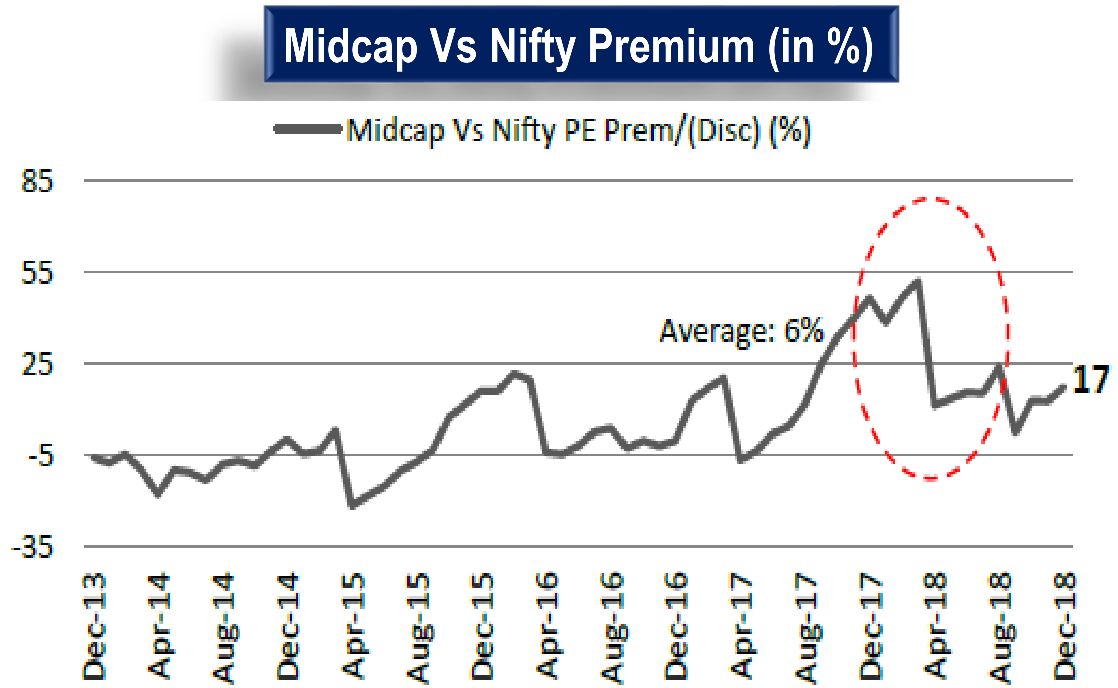
Market Fwd P/E has become more reasonable after the correction, and still quite far away from the peak P/E of 2007



Source: Kotak Institutional Equities

Midcap companies have seen their valuation premium fall, amidst the correction



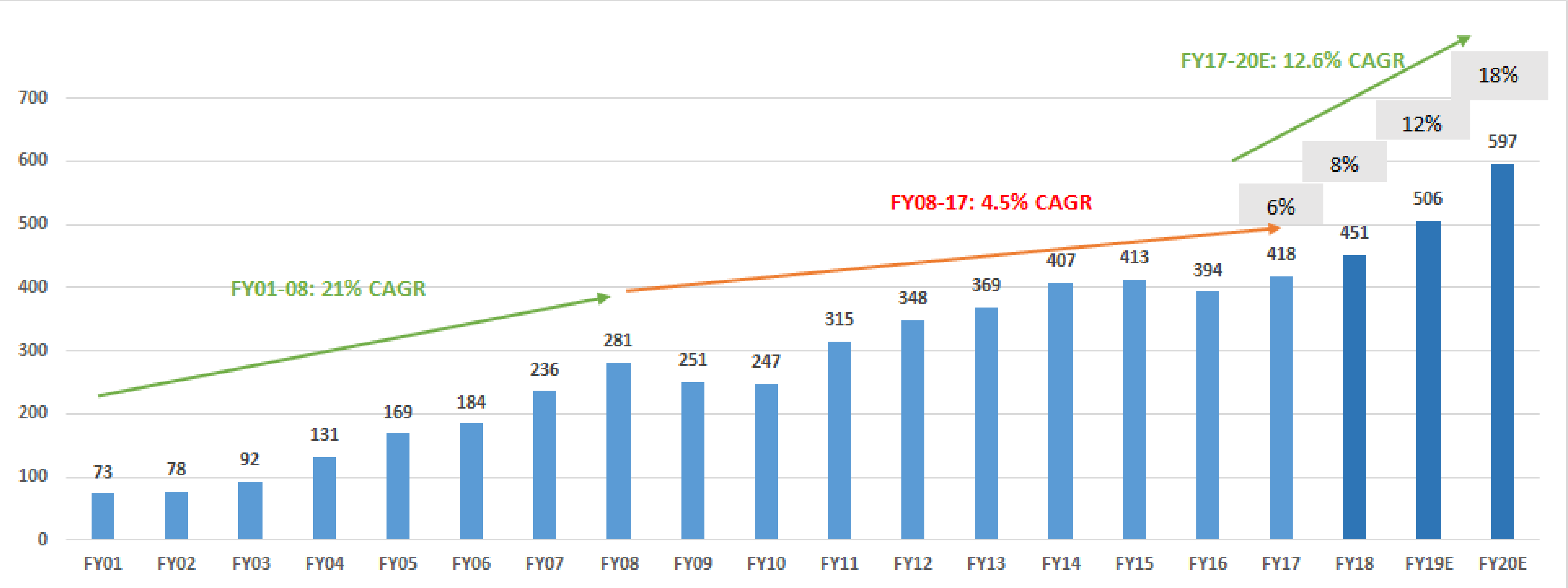


Source: Bloomberg, Motilal Oswal

- After the sharp correction that we have seen in small and midcap space in 2018, the valuation premium of mid-caps over large-caps has come down.
- Although we still prefer large-caps more from a risk-reward perspective, the deep correction in the midcaps and small-caps is starting to present some selective bottom-up opportunities.

Corporate earnings growth expected to pick-up, after subdued growth over the past few years

Nifty Earnings Per Share (EPS) Trend



Source: Bloomberg, Bajaj Allianz Research

FIIs have been net sellers in equities, but countered by strong buying by DIIs

Source: SEBI, BSE	Rs in Crore			
Year	**FIIs**	**DIIs**	**MFs**	**Insurance**
FY2008	52,572	47,794	15,948	31,846
FY2009	(48,250)	60,040	6,962	53,078
FY2010	110,752	24,211	(10,235)	34,446
FY2011	110,121	(18,709)	(19,974)	1,265
FY2012	43,738	(5,347)	(1,384)	(3,963)
FY2013	140,032	(69,069)	(22,008)	(47,061)
FY2014	79,709	(54,161)	(21,069)	(33,092)
FY2015	111,445	(21,446)	40,087	(61,533)
FY2016	(14,171)	80,416	66,143	14,273
FY2017	60,196	30,787	56,209	(25,422)
FY2018	21,074	113,258	140,517	(27,259)
FY2019 (upto Dec)	(48,029)	84,464	85,793	(1,018)

Source: SEBI, BSE	Rs in Crore			
Month-end	**FIIs**	**DIIs**	**MFs**	**Insurance**
31 January 2018	12,984	399	9,023	(8,624)
28 February 2018	(12,878)	17,813	16,181	1,632
31 March 2018	13,372	6,694	9,256	(2,562)
30 April 2018	(6,468)	8,511	11,294	(2,782)
31 May 2018	(9,660)	15,055	13,619	1,436
30 June 2018	(2,577)	14,146	9,231	4,915
31 July 2018	1,429	4,213	3,995	218
31 August 2018	(2,029)	2,823	3,808	(673)
30 September 2018	(9,623)	12,505	11,638	867
31 October 2018	(27,623)	26,034	24,047	1,987
30 November 2018	6,223	801	5,243	(4,443)
31 December 2018	2,299	376	2,918	(2,543)

- DIIs have been a strong force (helped by robust MF flows), and have helped to counter FII equity outflows. However, net buying by DIIs have slowed down over the past couple of months.
- FIIs have been net sellers this year, but flows turned positive over the past couple of months.

With FII outflows from other peer Asian EM markets in 2018, India too has been impacted

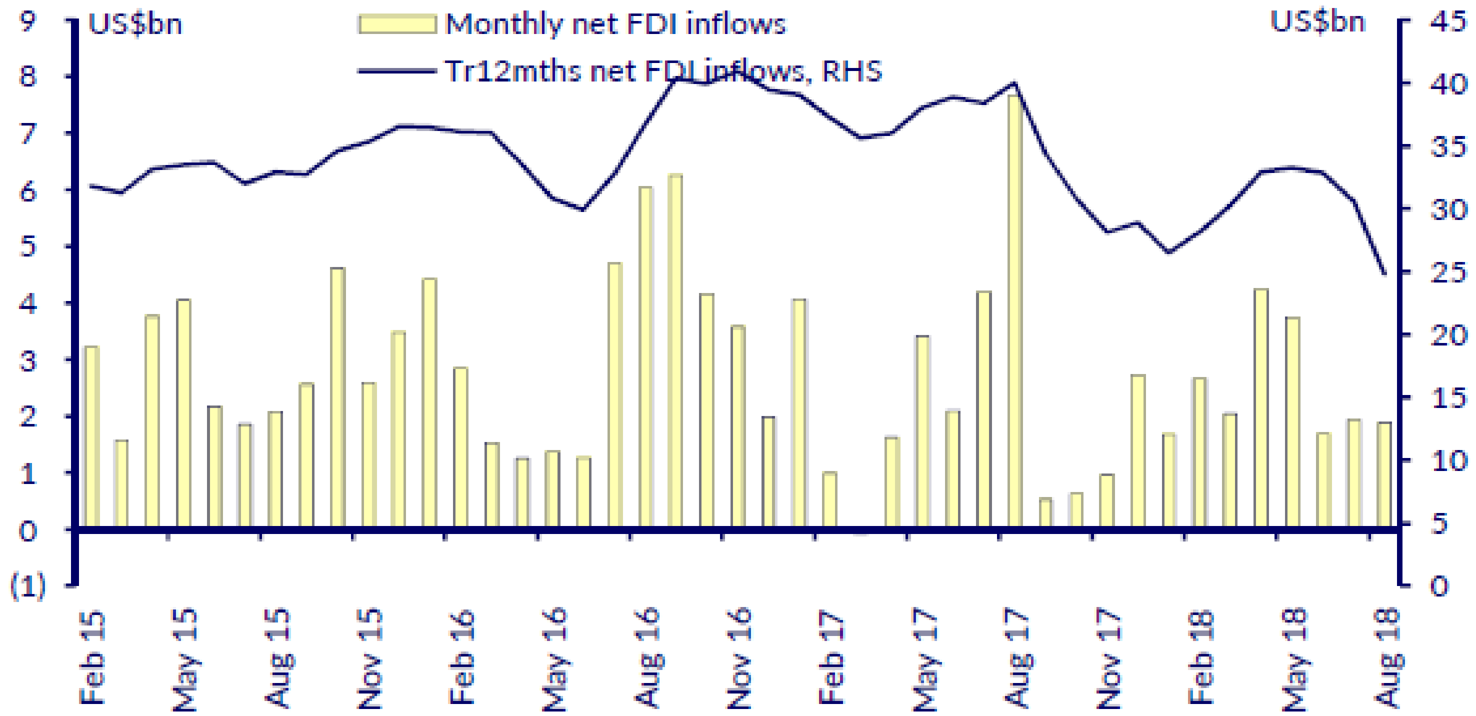
Foreign Equity Flows within Emerging Asian region ($ in bln)

Country	2016	2017	2018
India	2.9	8.0	(4.6)
Korea	10.4	8.1	(5.7)
Taiwan	11.0	6.1	(12.2)
Philippines	0.1	1.1	(1.1)
Indonesia	1.2	(3.0)	(3.5)
Thailand	2.2	(0.8)	(8.9)
Malaysia	(0.6)	2.5	(2.9)
ASEAN	2.9	(0.2)	(16.3)
Emerging Asia	**$27**	**$22**	**-$39**

Source: Goldman Sachs, Bloomberg

- Due to global risk-reversion, EM Asian markets have registered large FII outflows to the tune of $39 billion in 2018, compared to a net inflow of $22 billion in 2017.
- India too has been impacted due to this global risk aversion, but the FII outflows from India in 2018 have been lower than some other peer markets like Taiwan, Thailand, Korea etc.

FDI Flows have been healthy, but have seen some slowdown lately

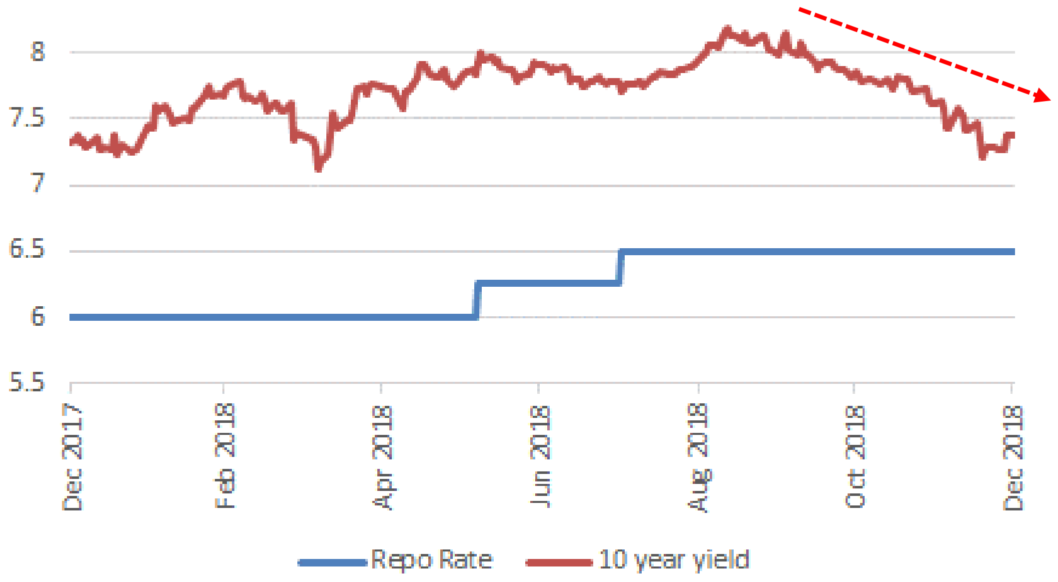


Source: RBI, CLSA

Fixed Income Markets

Debt markets see some relief: Bond yields have softened considerably; RBI turns dovish

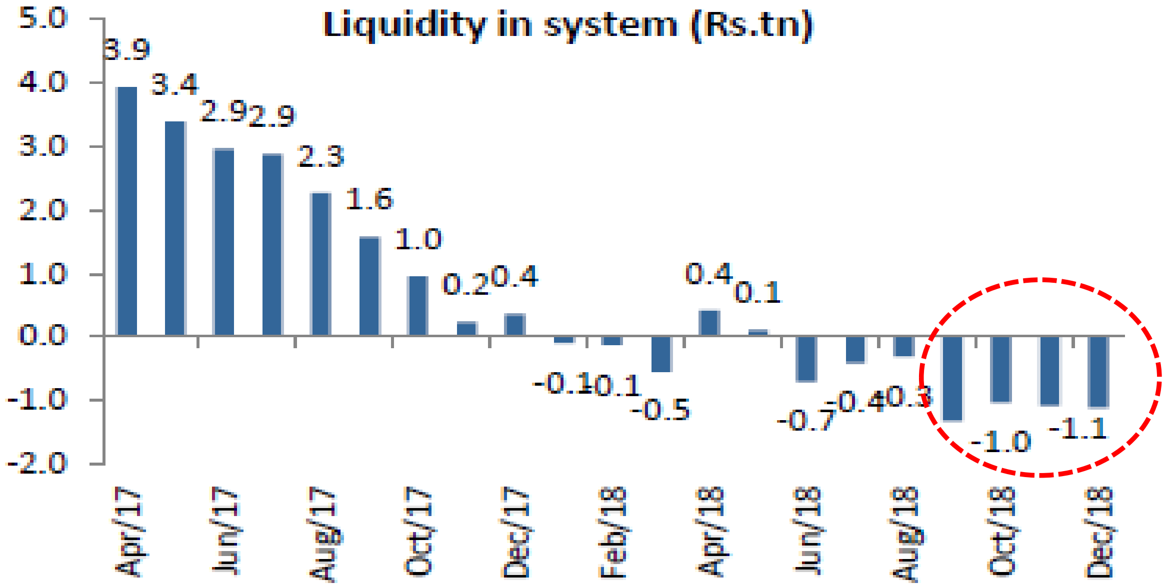
India 10 Yr G-Sec Yield Vs Repo Rate (%)



Source: Bloomberg

- 2018 was a roller coaster ride for the bond markets. The benchmark 10 year bond yield started 2018 at 7.3% mark, went up to 8.2% in October, and finally closed the year on a flat note – at 7.37%.
- Bond yields have softened considerably over the past few months due to sharp fall in crude oil, lower than expected inflation, RBI turning dovish and cutting its inflation forecasts, recovery in rupee, liquidity infusion by RBI, some reversal in FII outflows, and the credit crunch stabilizing.
- However, corporate bond spreads still remain a bit elevated.

RBI has been infusing liquidity through the OMO route, but liquidity still remains a bit tight

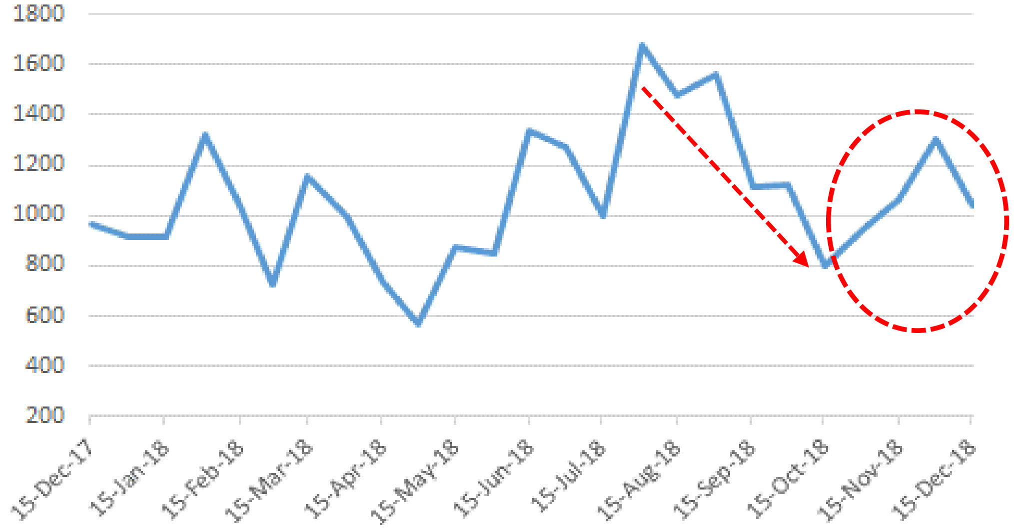


Source: Spark Capital

- With liquidity being tight within the system, the RBI has been proactive, by announcing liquidity infusion through OMO (Open Market Operation) purchases. Liquidity conditions have eased, but still remains a bit tight.
- It conducted OMO purchases of Rs. 126,000 crs between Oct – Dec 2018, increasing it steadily. RBI also announced OMO purchases of Rs. 50,000 crs for Jan 2019, and that infusion via OMOs would continue for remainder of FY19—intending to bring liquidity back to neutral.
- In its Dec 2018 policy review, RBI also cut SLR by 25 bps from beginning of 2019 to 19.25%, followed by progressive cuts (of 25 bps) every quarter, until the SLR comes down to 18%. This will help to further release liquidity in the system.

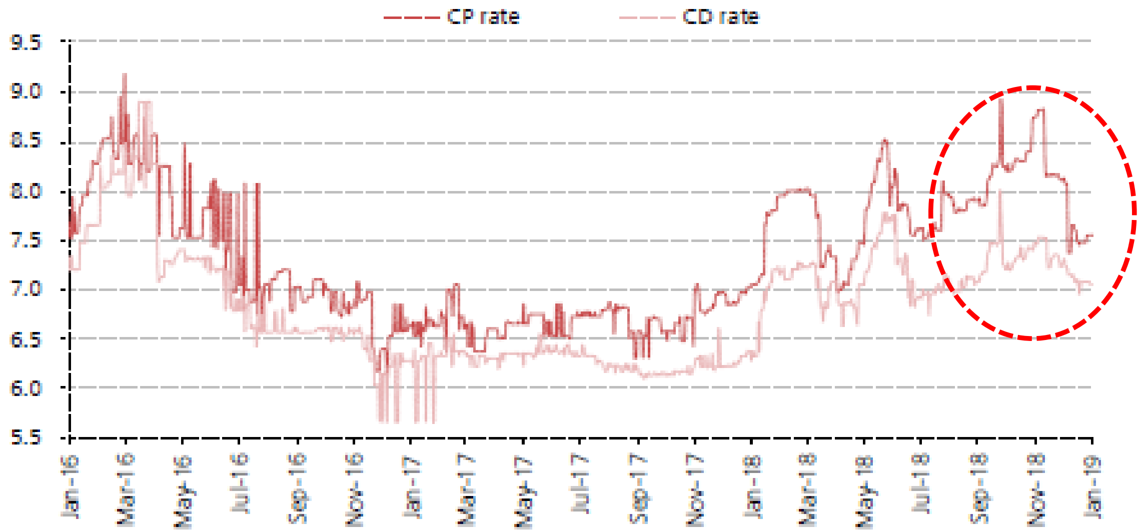
Things have stabilized a bit a in the NBFC/HFC space: CP/ CD rates have declined and issuances have picked up

Fortnightly CP Issuances (Rs. In billion)



Source: Bloomberg

3 Mth CP & CD Rates(in %)



Source: Bloomberg, Kotak Institutional

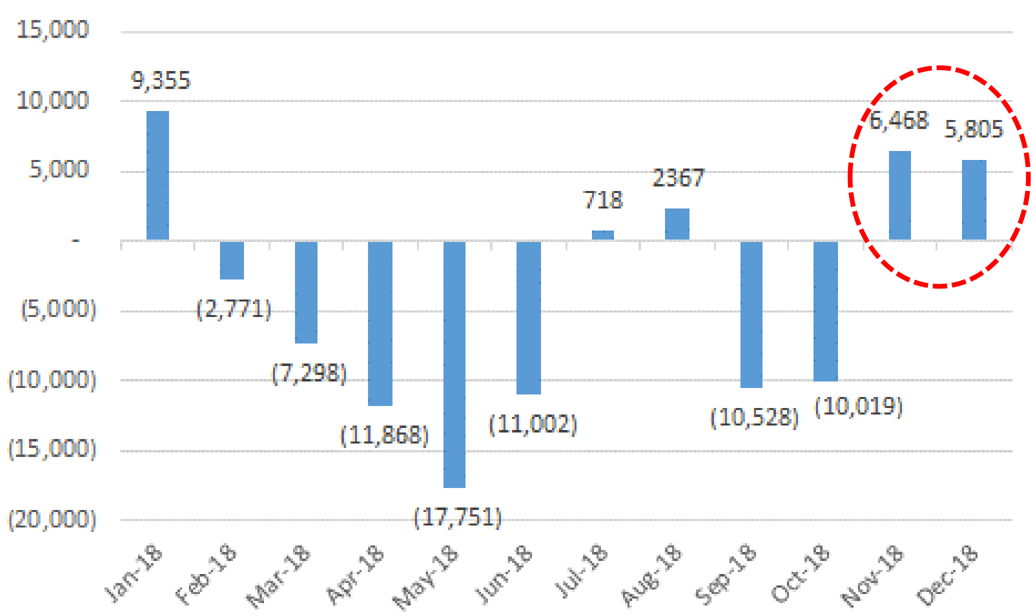
- Commercial Paper (CP) / Certificate of Deposit (CD) rates had spiked post the ILF&S default and turmoil in the NBFC / HFC space. However, CP /CD rates have declined in the past few months.

- CP issuances have also recovered somewhat after a sharp drop.

LIFE GOALS. DONE.
BAJAJ Allianz

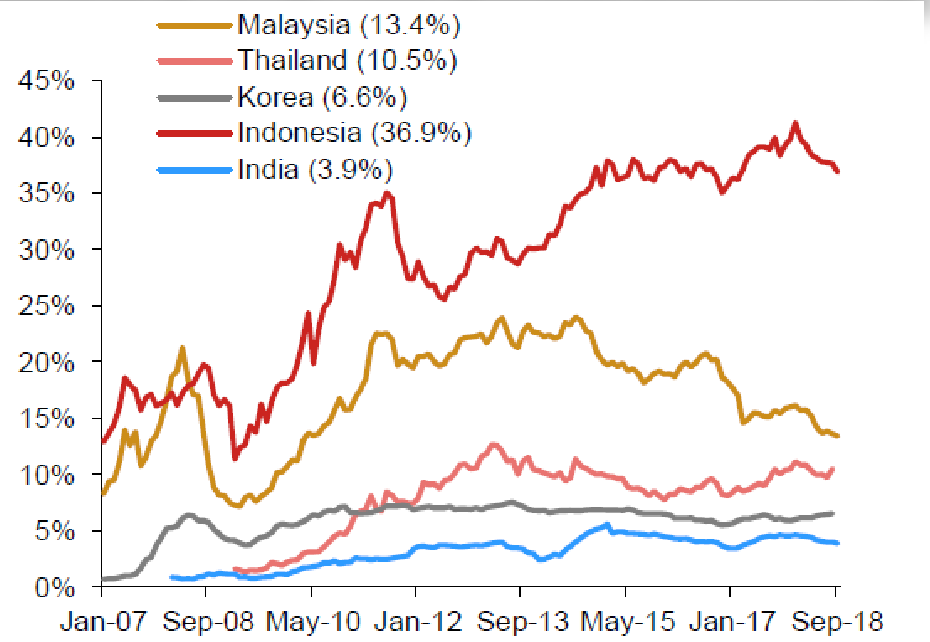
We have seen large foreign outflows in the debt markets in 2018, but flows have reversed somewhat over the past couple of months

Monthly FII Debt Net Flows in 2018 (Rs. In Crore)



Source: Bloomberg

Outstanding Foreign Holding in Debt securities (in %)



Source: Bloomberg, Nomura

- In CY 2018 we have large FII net outflows from the Indian debt markets to the tune of almost Rs. 46,500 crore, although we some inflows in the past couple of months . In CY 2017 we had seen record high FII net inflows of Rs. 1,48,484 crore
- However, India's foreign holding in debt securities is relatively much lower than other peer Asian markets like Indonesia, Malaysia and Thailand. This makes us less susceptible to foreign outflows, relative to peers—in case of any EM contagion risk.

Market Outlook

Factors to watch out for

Trade tariffs	• The trade tensions between US & China have stabilized, with US halting further tariffs for 90 days, to allow for talks. But there is uncertainty on the future course of action.
Turbulence in global markets & risk appetite	• We have seen some turbulence and deep correction in global markets, due to global risk aversion, and concerns of some global growth slowdown.
Global monetary policy	• Although the US Fed has turned slightly dovish recently, any pick-up in pace of monetary tightening by other major central banks may cause some volatility in emerging markets (including India).
Fiscal Slippage	• There may be some minor fiscal slippage due to some populist measures (ahead of elections), and lower GST collections, but we do not expect a major impact of the same in the long term.
General Elections in 2019	• With the recent loss of BJP (to Congress) in the crucial states of Chhattisgarh, MP, and Rajasthan, there maybe some uncertainty & volatility during the upcoming general elections. But we expect it to be more short term in nature.
Crude Oil	• Although crude oil prices have fallen significantly, their future trajectory needs to be tracked.

Market Outlook & Strategy

- **Corporate Earnings Growth to accelerate:**
  - We believe that earnings growth will accelerate in H2 FY19 and particularly in FY20, and this should be the key driver for markets in 2019.
  - Earnings growth over the past years was primarily driven by domestic consumption sectors; but we expect that growth will be more broad-based in 2019, and also that the capex cycle (which has been the drag earlier) has now bottomed out.
  - Nifty earnings (ex OMCS's) are expected to grow ~ 15% in Q3 FY19 led by double digit growth in consumer, financials, IT and capital goods
- **Sector Outlook:**
  - We continue to like well-run private sector banks and NBFCs due to their good asset quality and healthy credit growth.
  - Pharma sector, which was struggling due to the US FDA issues and weak pricing for generics, seems to have bottomed out.
  - We are incrementally turning positive on capital goods, on expectations of a capex turnaround.
  - We have been liking IT services sector for its attractive valuation.
- **Valuations have now become more reasonable:** We have been preferring the large-cap segment since the beginning of 2018, on a relative valuation basis. Although we still like the large-cap segment; with the correction in the small/mid-cap segment there are some good selective bottom-up opportunities also emerging in this space.
- **Investors should continue to invest in a staggered manner in equities, and could look to add positions on any large market dips.**
- **RBI turns dovish:** The RBI has turned dovish on inflation, and there are increased market expectations of some monetary policy accommodation if inflations pans out as per RBI's revised inflation trajectory.
- **Debt markets:** With the recent sharp fall in bond yields, we feel that much of the rally in bond markets is behind us now. We expect bond yields to be range-bound; albeit data dependent. Presently, we are positive on the short to medium term part of the yield curve.

Wishing you a happy & prosperous New Year!

THANK YOU

Bajaj Allianz Life Insurance Co. Ltd., Regd. Office Address: Bajaj Allianz House, Airport Road, Yerawada, Pune – 411006, IRDAI Reg. No.: 116 CIN : U66010PN2001PLC015959, Mail us : customercare@bajajallianz.co.in, Call on : Toll free no. 1800 209 7272/ Fax No: 02066026789