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Macro-economic developments

- The Non-farm payrolls in the United States rose by a weak 20,000 in February 2019, much lower than market expectations of around 180,000. The government shut-down was attributed as one of the key reasons for the weak payroll data. The unemployment rate fell to 3.8% from 4.0% in the previous month.
- In the March 2019 policy, the dovish undertone of the US Fed further increased, as it cut the interest rate projection for 2019—indicating no rate hike in 2019, and also cutting the median fed rate for both 2020 & 2021 quite substantially to 2.6% (from 3.1% earlier). Simultaneously, the Fed announced that it will start to moderate its balance sheet normalization from the current total of $50 billion per month to $35 billion per month from May 2019, and altogether end the balance sheet normalization in Sep 2019. The central bank further cut the GDP growth forecast for US in CY2019 to 2.1%YoY (from 2.3% in December 2018 projection), and for CY2020 to 1.9%YoY (from 2.0% earlier). The US economy had grown by a healthy 2.9%YoY in CY2018.
- The European Central Bank (ECB) has also turned dovish in its statements lately. The central bank, which was tapering its quantitative easing (QE) programme, ended it in Dec 2018, and had earlier indicated that interest rates would be kept unchanged at least through summer of 2019. However, recently in March 2019, ECB also turned quite dovish--cut inflation & growth forecasts, and said that interest rates would be unchanged at least through end of 2019.
- India's current account deficit (CAD) moderated to $16.9 billion (2.5% of GDP) in Q3 FY19 from $19.1 billion (2.9% of GDP) in the previous quarter, and was $13.7 billion (2.1% of GDP) in the year-ago quarter period (Q3 FY18). The merchandise trade deficit remained elevated at $49.5 billion in Q3 FY19, compared to $50.0 billion in the previous quarter; but the invisibles component improved in the latest quarter—helping the overall CAD to moderate from the previous quarter. However, the capital account balance / flow deteriorated to $13.6 billion in Q3 FY19, from $16.7 billion in the previous quarter, due to drop in foreign portfolio flows and short term loans. As a result of this, the Balance of Payment (BoP) deficit widened to $4.3 billion in Q3 FY19, from $1.9 billion in the previous quarter, and was a surplus of $9.4 billion in the year-ago quarter period (Q3 FY18).
- Meanwhile, India's trade deficit narrowed to $9.6 billion in the month of Feb 2019, from $14.7 billion in the previous month, primarily on the back of drop in gold and oil imports.
- The Index of Industrial Production (IIP) growth slowed down to 1.7%YoY in Jan 2019, from 2.6%YoY in the previous month. Manufacturing sector (having 78% weight in IIP) growth moderated to 1.3%YoY in Jan 2019, from 3.0%YoY in the previous month. For FYTD19 (upto January) IIP growth was 4.4%YoY, compared to 4.1%YoY in the corresponding period, a year ago—indicating that industrial activity still remains sluggish.
- Consumer Price Index (CPI) headline inflation rose to 2.6%YoY in Feb 2019, from 2.0%YoY in the previous month, as food deflation ebbed. Food inflation (biggest component of CPI, with 39% weight), came in at -0.7%YoY in February, vs -2.2%YoY in the previous month. Core inflation (ex food & fuel) also rose to 5.4%YoY from 5.2%YoY in the previous month.
- Crude prices, continued to rise in March, with OPEC surpassing its production cut target, and also on the back of fall in US oil inventories. Brent crude closed the month up 3.6%, at the $68.4/bbl mark.
- The rupee closed the month up 2.3%, at 69.15/US dollar, on the back of strong foreign inflows and dovish monetary policy statements of some major global central banks.

Equity market developments and Outlook

- Indian markets performed strongly during the month of March, on the back of strong foreign portfolio inflows (helped by dovish commentary from the US Fed & ECB), de-escalation of geo-political tensions, and optimism on US – China trade tariff front. The benchmark Nifty 50 index delivered 7.70% return, while the broader markets outperformed, with the Nifty Midcap 50 index and Nifty Smallcap 100 index returning 10.2% and 12.4% respectively. Sectors that outperformed during the month included real estate, banking, consumer durables, and oil & gas. The sectors that underperformed during the month were auto, IT, FMCG and healthcare.
- Global markets mostly closed in the green, with the MSCI World index, MSCI Asia ex-Japan index and MSCI Emerging Markets index returning +1.1%, +1.6% and +0.7% respectively.
- In the US, the S&P 500 index rose by 1.8% in March. Most of the European markets were also buoyant during the month, with UK's FTSE 100 index returning 2.9%, and France's CAC 40 index rising 2.1%. Within Asia, India was one of the top performing markets in March, followed by China (+5.1%) and Taiwan (+2.4%). However, Asian markets like Malaysia, Korea and Thailand relatively underperformed during the month.
- Foreign portfolio investor (FPI) flows picked up strongly to ₹ 33,116 crore in March, from an already healthy ₹15,328 crore net inflow in the previous month.
- Domestic Institutional Investor's (DIIs) net investment in equities continued to slow down, and registered a large net outflow of ₹13,930 crore in March, after seeing a net outflow of ₹566 crore in the previous month.
- The recent dovish monetary policy stance of some major central banks has been beneficial for some emerging markets like India, after the risk aversion that we saw for most of CY2018. Even amidst the expected global growth slowdown, India's economic growth is projected to pick up in FY19-20, and is poised as the fastest growing major economy.
- The stronger economic growth potential, higher Return on Equity (ROE) for India markets, and a stable currency--puts India in a relatively better position than most of its EM peers. However, an eye needs to be kept on the magnitude of the global growth slowdown, and its impact on global risk appetite—as a more severe one than anticipated, will have an impact on emerging markets (including India) in general.

Fixed Income market developments and Outlook

- Bond yields moderated during the month, on account of positive developments like the rupee appreciating, strong foreign inflows into debt markets, and sharp decline in global bond yields. This was offset by rise in crude oil price, higher govt. bond supply, and also some seasonal liquidity tightness. The new 10 year benchmark yield closed the month at 7.35% - down 6 bps.
- On the liquidity front, the RBI conducted OMO purchases of ₹ 37,500 crore for the month of March. The central bank also did forex (dollar-rupee) swap of $5 billion during the month to inject rupee liquidity, and announced another round of forex swap of $5 billion for the month of April. With this, expectations of OMO purchases for the month of April have dwindled.
- The government will borrow 62.3% of budgeted gross borrowing or ₹4,420 billion in H1 FY20. This is significantly higher than ₹2,880 billion (47.6% of budgeted gross borrowing) in the corresponding period of FY19, and also slightly higher than the historical average of 60%. The net borrowing is also front-loaded and higher than the historical average—which may not bode so well for bond yields.
- India's fiscal deficit for FYTD 19 (upto February) reached 134% of the budgeted full year target, compared to 120% in the corresponding year ago period. Fiscal deficit has been elevated due to higher revenue expenditure, and lower than budgeted GST collections, primarily. However, GST collections for the month of March 2019 (indicating activity in Feb) picked up 16%YoY to ₹ 1.07 trillion—the highest monthly collection since the implementation of GST.
- Foreign Portfolio Investors (FPIs) in debt markets registered a net inflow of ₹15,352 crore compared to a net outflow of ₹ 9,290 crore in the previous month.
- With inflation being within target, we can expect further rate cut/cuts from the RBI going forward. Also, the dovish monetary policy stance of global central banks—leading to sharp decline in bond yields, pick-up in foreign inflows and appreciation in currency—is generally beneficial for bond yields.
- However, the higher bond supply, rising crude oil prices, concerns on the fiscal deficit front may provide some headwinds to the bond markets, and need to be tracked.
- From an investment perspective, we continue to prefer the shorter to medium term end of the yield curve.

Ver: March 2019