Sampath Reddy, CFA
CIO, Bajaj Allianz Life Insurance

Macro-economic developments

- Global bond yields fell sharply during the month on the back of concerns of the Coronavirus epidemic—leading to risk-off sentiment. The US 10 year treasury yield closed the month down 36 bps, at 1.15%. Post the close of the month, the US Fed did an emergency rate cut of 50 bps on 3rd March 2020 to try and shield the US economy from being impacted by the Coronavirus epidemic—causing the 10 year yield to drop significantly below 1%, to a record low. Other global central banks have also started to ease monetary policy recently.
- Supply disruption was seen in China due to the stalled production/manufacturing in various provinces. Recent data showed that China Manufacturing PMI crashed to 35.7 in Feb 2020 from 50 in the previous month, making it the largest decline since the 2008 global financial crisis. Auto sales in China also fell by a record 80%YoY in the month of Feb 2020, compared to a 21.6%YoY fall in the previous month.
- China is the world's second largest economy and accounts for ~16% of global GDP and ~12-13% of global trade. So a large slowdown in China could impact global growth as well. It remains to be seen if any material impact on China's growth is seen beyond Q1 CY2020, and how much it will impact the global GDP growth as well (as Coronavirus has turned into a global pandemic now, as announced by WHO).
- Domestically, India's Q3 FY20 GDP growth slowed down to a ~7-year low of 4.7%YoY. There were large upward revisions in growth rates for Q1 FY20 (to 5.6% from 5.0% earlier) & Q2 FY20 (to 5.1% from 4.5% earlier)—due to earlier downward revisions seen in FY19 data. Slowdown was led by Investments (Gross Fixed Capital Formation), which is in sharp contraction for past 2 quarters (-4.1% in Q2 FY20 and -5.2% in Q3 FY20). Private consumption (~55% weight in GDP) growth improved to 5.9% from 5.6% in the previous quarter, but down from 7.0% a year back. Government spending growth was healthy at 11.8%, vs 13.2% in the previous quarter.
- GVA growth slowed to 4.5%YoY in Q3 FY20 from 4.8%YoY in Q2 FY20, and here too--there were revisions in historical data. Manufacturing sector growth remained in contraction at -0.2% in Q3 FY20 vs -0.4% in the previous quarter. Services sector growth remained stable at 6.4% in Q3 FY20 vs 6.8% in the previous quarter. Meanwhile, agriculture sector growth picked up to 3.5% in Q3 FY20 from 3.1% in the previous quarter.
- Consumer Price Index (CPI) headline inflation rose to 7.6%YoY in Jan 2020 from 7.4%YoY in the previous month. Food inflation (weight of 39% in CPI) remained elevated at 13.6%YoY in Jan 2020, compared to 14.1%YoY in the previous month. Meanwhile, core inflation (ex food & fuel) rose to 4.2%YoY in Jan 2020 from 3.8%YoY in previous month.
- Index of Industrial Production (IIP) growth came in at -0.3%YoY in Dec 2019 vs +1.8%YoY in the previous month. The heavy-weight manufacturing sector (78% weight in IIP) growth fell to -1.2%YoY, from +2.7%YoY in the previous month. For FYTD20 (upto December), IIP growth was significantly lower at +0.5%YoY, compared to +4.7%YoY in the corresponding period, a year ago.
- Crude prices continued to fall, on the back of concerns of the Coronavirus epidemic impacting global growth, and thereby drag crude demand. Brent crude closed the month at $50.52/bbl—down around 13%. Post the close of the month, a price war started between Saudi Arabia and Russia (as they increased crude production), and this has caused brent crude prices to crash to below $35/bbl level. This sharp fall in crude prices is beneficial for a net oil importing country like India, where crude oil accounts for a large part of our imports.
- The rupee depreciated during the month on the back of foreign outflows and global risk aversion. The rupee closed the month down 1.1% at INR 72.18 / USD. Post the close of the month, the rupee depreciated further (breaching the INR 74/USD mark) in early March, on the back of global risk aversion and foreign portfolio outflows.

Equity market developments and Outlook

- Indian markets registered a healthy correction during the month, on the back of global risk aversion—due to the escalating Coronavirus epidemic. The benchmark Nifty 50 index returned -6.3% during the month, while the broader markets underperformed--with the Nifty Midcap 50 index and Nifty Smallcap 100 index returning -8.1% and -8.9% respectively. Post the close of the month, global markets (incl. India) registered a sharp correction in early March 2020, on the back of Coronavirus concerns and sharp drop in crude oil prices.
- Sectors that outperformed during the month included consumer durables, pharma and banking. The sectors that underperformed during the month were realty, auto and metals.
- Globally, markets registered a strong correction (weighed down by the Coronavirus and growth concerns). Developed markets underperformed emerging markets and Asian markets. The MSCI World index returned -8.6% in February, while MSCI Emerging Markets index and MSCI Asia ex-Japan index returned -5.4% and -2.9% respectively.
- In the US, the S&P 500 index closed the month down 8.4%. Major European markets like UK, Germany and France also closed with similar losses. Within Asia—Taiwan and Hong Kong were the out-performers, while the under-performers within the region were Thailand and Japan. Other emerging markets like Russia and Brazil also saw a sharp correction during the month.
- Foreign portfolio investors (FPIs) registered a net equity outflow of ₹ 1,521 crore in the month of February, compared to a net inflow of ₹ 14,095 crore in the previous month.
- Domestic Institutional Investors (DIIs) registered a strong net inflow of ₹ 16,933 crore in the month of February, compared to a net inflow of ₹ 2,250 crore in the previous month.
- The Coronavirus epidemic has triggered global risk aversion, and led to a sharp correction in global markets (incl. India). We may not be out of the woods yet completely, and may see further short-term market volatility as new coronavirus cases continue to increase globally. Recent data shows that new cases ex-China are escalating, while new cases in China have seen a sharp slowdown. There could also be some risk to global growth this year, although it's still a developing situation, and needs to be tracked (on how big the impact will be).
- However, with the market correction, valuations have turned reasonable. Equities have become relatively more attractive as indicated by bond yield (minus) equity earnings yield valuation indicator, which has turned negative. The Nifty index forward P/E ratio has also dropped to below 15X multiple. We feel this may offer some buying opportunity and investors can start to deploy partial money in equities (especially if you are underweight equities as per your risk profile).
- Market timing, as we know, is difficult; and it's hard to catch the bottom and top of markets accurately. However, the prudent thing is to atleast get started, or not to panic and sell-off. Historical data has shown that investments made in challenging/volatile times, has generally been quite rewarding for investors over the medium to long term.
- At some point the focus will start shifting to how the corporate earnings trajectory is shaping up, and if there are any significant downside risks to the same (starting to show up). Eye needs to be also kept on the progress of Coronavirus epidemic, global monetary policy stance, global growth trajectory, and global risk appetite.
- From an investment perspective, we continue to prefer large-caps, but also see some bottom-up opportunities in the mid-cap segment—from a valuation standpoint.

Fixed Income market developments and Outlook

- Bond yields fell sharply during the month on the back of a favourable RBI policy review, sharp fall in global bond yields and crude prices, some risk-aversion, comfortable liquidity, and long-term repo operations (LTRO) done by the RBI as announced in the Feb 2020 policy. The 10 year yield closed the month of February 2020 at 6.37%--down 23 bps.
- Post the close of the month, RBI recently announced that it is ready to take action to maintain financial stability, on the back of escalating Coronavirus concerns. Bond yields fell further post this announcement, and as the US Fed and some other global central banks announced monetary easing. The 10 year yield inched closer to the 6% mark at one point, before rising a bit lately on account of FPI selling.
- The RBI has already conducted/announced 4 tranches of LTRO of ₹ 25,000 crore each (total of ₹ 1 lakh crore), with 2 tranches done in the month of Feb 2020, and 2 tranches in early March 2020—so far.
- Fiscal deficit for FYTD 20 (upto January) was elevated at 128.5% of the budgeted estimate for entire FY20, compared to 121.5% in the corresponding period in the previous fiscal year. In the recent Union budget, the government had revised the fiscal deficit target for FY20 from 3.3% (of GDP) earlier to 3.8%.
- Government data showed that GST collections for the month of February 2020 (reflecting activity for the month of Jan 2020) once again breached the ₹ 1 lakh crore mark—for the fourth consecutive month.
- Foreign Portfolio Investors (FPIs) registered a net outflow of ₹ 169 crore in the month of February, compared to a net outflow of ₹ 11,104 crore in the previous month.
- The RBI recognized that there is monetary policy space for future action, but it will be data dependent. With other global central banks engaging in monetary easing recently, and with the Coronavirus outbreak escalating to a global pandemic now, it opens up some space for further monetary easing by the RBI (although inflation and rupee depreciation are a bit of an overhang).
- From an investment perspective, we presently prefer the medium-term part of the yield curve.