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Macro-economic developments

- US labour market has improved, with 4.8 million jobs added in the month of June (higher than expected). Unemployment rate fell to 11% in June vs 13.3% in May & 14.7% in April.
- Economic activity improved globally, as lock-downs were eased or removed. Global Manufacturing PMI recovered to 47.8 in June from 42.4 in May and 39.8 in April. PMI data below 50 means contraction in activity.
- In its June 2020 outlook, the IMF further revised down global growth forecasts from the April 2020 forecast. Global GDP growth is now expected to contract by 4.9% in CY2020 (vs -3.0% earlier), but expected to recover to +5.4% in CY2021. The contraction in global economy is to be led by advanced economies. US economy is now expected to de-grow by 8.0% in CY2020 (vs -6% earlier), and Euro Area to contract by 10.2% (vs -7.5% earlier).
- The IMF said that emerging markets are now expected to contract by 3% in 2020 (vs -1% earlier). The Indian economy is now expected to contract by 4.5% in FY21 (vs growth of 1.9% projected earlier in April). However, the economy is expected to recover to +6.0% growth in FY22 (mainly helped by lower base effect).
- Domestically in India, Covid-19 cases continued to escalate (now third highest in the world), which is a cause of concern. However, fatality rates remain in control so far at ~3% (at national level), and recovery rate is ~60%. We have seen calibrated opening up of Indian economy, except in containment zones. This has helped in partial recovery in various high-frequency economic indicators.
- After more than a decade, India's current account turned positive (surplus) @ 0.1% of GDP in Q4 FY20, with trade deficit moderating (on lower crude oil price prices) and invisibles (services & transfers) increasing. For full FY20, current account deficit (CAD) moderated to 0.9% of GDP from 2.1% of GDP. Capital account was also in healthy surplus in Q4 FY20. Therefore, Balance of Payments (BOP) was in healthy surplus in Q4 FY20. For full FY20, BOP surplus increased to $59.5 bln from a deficit of $3.3 bln in FY19.
- With the lock-down being gradually eased, India Manufacturing PMI recovered to 47.2 in June vs 30.8 in May and a record low of 27.4 in April. India Services PMI also recovered sharply to 33.7 in June, vs 12.6 in May and a record low of 5.4 in April. PMI lower than 50 indicates contraction in activity.
- Only partial consumer price inflation data was released again for the month of May. Food & beverage inflation moderated to 7.4%YoY in May vs 8.6%YoY in the previous month. Tepid growth was seen in housing and fuel inflation during May.
- Crude prices continued to see smart recovery in the month of June on the back of recovery in economic activity, OPEC production cuts, and some recovery in global risk appetite. Brent crude rose 16.5% in June, to close the month at around the $41/bbl mark.
- The rupee was stable and closed the month on a flattish note (at INR 75.5/USD), although it was a relative underperformer amidst peer emerging market currencies in June.

Equity market developments and Outlook

- Gradual easing of the lock-down, strong global liquidity & flows, return of some global risk appetite and partial recovery in high-frequency economic indicators, helped Indian markets to emerge as one of the top performing markets globally in the month of June.
- The benchmark Nifty 50 index returned +7.5% during the month. The broader markets fared better, with the Nifty Midcap 50 index and the Nifty Smallcap 100 index returning +10.3% and +15.3% respectively in June.
- The sectors that outperformed during the month of June were realty, banking, PSUs and auto. The sectors that underperformed during the month were FMCG, healthcare, capital goods and IT.
- Global markets continued to rally, with economic activity picking-up and liquidity being strong. With some global risk appetite returning, emerging & Asian markets outperformed developed markets during the month of June. The MSCI Emerging Markets index and MSCI Asia ex-Japan index returned +7.0% and +7.9% respectively, while the MSCI World index returned +2.5% in June.
- The US markets underperformed in June, with the S&P 500 index returning +1.8%. Within the major European markets Germany and France outperformed. Within Asia—India, Hong Kong, and Taiwan outperformed in June, while Thailand, Japan, and Malaysia underperformed.
- Foreign portfolio investors (FPIs) registered a net equity inflow of ₹18,684 crore in the month of June, compared to a net inflow of ₹13,000 crore in the previous month.
- Domestic Institutional Investors (DIIs) registered a net inflow of ₹2,434 crore in the month of June, compared to a net inflow of ₹11,357 crore in the previous month.
- Markets have seen a strong rally from their March 2020 lows. They seem to be ignoring a possible recession in FY21, and factoring in a quicker recovery. The market up-move has been helped by strong global and domestic liquidity, recovery in global risk appetite, and some improvement in high-frequency indicators.
- Market valuations have recovered from their lows helped by the recent market rally and earnings downgrade for FY21.
- Corporate earnings for Q4 FY20 were below expectations, and there have been sharp cuts in earnings for FY21—due to the economic slowdown.
- Some of the factors to watch out for include the trajectory of Covid-19 cases in India & globally, if the recovery in economic data continues to improve, geo-political tensions, global flows & risk appetite, and if more fiscal stimulus or other measures are announced by the Indian government.
- We recommend investors to use an asset allocation approach to investing or stagger their equity investments, at this juncture.

Fixed Income market developments and Outlook

- G-Sec yields rose a bit during the month on the back of concerns of fiscal slippage and higher govt bond supply, rise in crude oil prices, downgrade in India's sovereign rating outlook, and foreign outflows. The new 10 year G-Sec yield closed the month at 5.89%--up 13 bps. However, yields have softened more at the shorter end of the yield curve, and corporate bond spreads have also come down—implying some reduction in risk aversion for corporate bonds.
- The RBI has been taking various measures to soften long-term G-Sec yields and manage the yield curve—which has steepened a bit lately, with short term yields softening more. It has been conducting OMO (Open Market Operation) purchases from time to time. Recently, the RBI announced another Operation Twist in a bid to bring drown long term G-Sec yields. Under the Operation Twist for ₹10,000 crore on 2nd July 2020, the RBI will purchase longer dated G-Secs maturing between 2027 and 2033 and simultaneously sell shorter dated securities maturing between 2020 and 2021. Liquidity has reduced a bit in June (due to quarter-end), but still remains in healthy surplus.
- Global ratings major Fitch revised India's sovereign rating outlook to "negative" from "stable" earlier, but kept the rating unchanged at BBB- (one notch above junk grade). Thus, Fitch's rating/outlook is now similar to Moody's, as the latter had downgraded India's sovereign rating/outlook in the beginning of June. However, S&P kept India's sovereign rating unchanged at BBB-, and outlook as "stable".
- India's fiscal deficit touched 58.6% of the full year target in the first two months of FY21 (April – May), compared to 52% in corresponding period in the previous fiscal year. The government reined in on expenditure, even as tax revenues plunged amidst the lock-down. Fiscal deficit for FY20 had come in at 4.6% of GDP, compared to revised estimate of 3.8% projected earlier.
- Finance Ministry data showed that GST collection dropped by 41%YoY in Q1 FY21, as a result of the lock-down. However, month-on-month collections showed a pick-up in June to ₹99,940 crore, from a record low of ₹32,394 crore in April.
- Foreign Portfolio Investors (FPIs) registered a net outflow of ₹1,691 crore in the month of June, compared to a large net outflow of ₹20,573 crore in the previous month.
- RBI has indicated that there is space for more monetary action if inflation remains within the projected trajectory. From an investment perspective on the fixed income side, we presently prefer the medium-term part of the yield curve.

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