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### Macro-economic developments

- US non-farm payrolls rose by lower than expected 661,000 in the month of September compared to 1.5 million in the previous month. Unemployment rate fell to 7.9% in September vs 8.4% in August, and a record high of 14.7% in April.
- Economic activity improved globally, and Global Manufacturing PMI rose to a 25-month high of 52.3 in September from 51.8 in August. PMI data below 50 means contraction in activity.
- In its September meeting, the US Fed kept rates unchanged, and its forward guidance also suggested that it could keep rates unchanged for the next few years (through 2023). The US Fed also revised upwards its GDP projection for CY2020 to a contraction 3.7%YoY, compared to an earlier forecast (in June) of a contraction of 6.5%YoY during the year.
- As per economic think-tank, OECD, global recession in 2020 may not be as deep as expected earlier. As per OECD's Economic Outlook Update (as of Sep 2020), global GDP growth is now projected to contract by 4.5% in CY2020 Vs earlier projection of 6% contraction (as per June 2020 forecast). This is being helped by healthy economic recovery in developed economies, especially the US--where GDP is now expected to contract 3.8% in CY20 vs earlier projection of 7.3% contraction. Healthy recovery of 5% in global GDP growth is projected for CY2021. OECD downgraded India's GDP growth forecast to -10.2% in FY21 from earlier projection of around -4.0% (in June 2020 forecast). However, India's GDP growth is expected to recover by a robust 10.7% in FY22 (helped to some extent by base effect).
- India's current account was in healthy surplus of 3.9% of GDP in Q1 FY21, compared to 0.1% in the previous quarter and a deficit of 2.1% a year ago. The record current account surplus during the quarter was helped by sharp fall in imports (relative to exports)—leading to a significant reduction in the trade deficit. Capital account flows were negligible in Q1 FY21 due to drop in FDI flows into negative territory, and lackluster FPI flows. Capital account surplus narrowed to $0.6 bln in Q1 FY21, compared to $17.4 bln in the previous quarter and $28.6 bln in the corresponding year ago period. Balance of Payments (BOP) continued to be in healthy surplus of $19.8 bln in Q1 FY21, compared to $18.8 bln in the previous quarter and $14.0 bln in the corresponding year ago period. Recent data showed that India's trade deficit moderated to $2.9 bln in the month of September 2020 (as YoY export growth returned to positive territory) from a deficit of $6.8 bln in the previous month. In FY21, current account could be in surplus, if oil prices remain stable and do not rise much from current levels.
- India Manufacturing PMI rose to 56.8 in August (highest reading since January 2012) from 52.0 in August. India Services PMI rose to 49.8 in September, vs 41.8 in August. PMI lower than 50 indicates contraction in activity.
- Consumer price inflation (CPI) data for the month of August 2020 remained unchanged at 6.7%YoY. Food inflation (which has 39% weight in the CPI index) moderated a bit to 9.1%YoY in August versus 9.3%YoY in the previous month. However, core inflation (ex food and fuel) continued to rise to 5.7%YoY in August from 5.5%YoY in the previous month.
- Crude prices corrected due to OPEC increasing production for the third consecutive month in September, some soft economic data and global risk aversion during the month. Brent crude price fell 9.5% in September, to close the month around the $41/bbl mark.
- The rupee closed the month on a flattish note at INR 73.77/USD, as FPI equity flows turned negative in September.

### Equity market developments and Outlook

- Indian equity markets saw some marginal correction in the month of September, but still fared better than most other global markets during the month.
- The benchmark Nifty 50 index returned -1.2% during the month. The broader markets outperformed, with the Nifty Midcap 50 index and the Nifty Smallcap 100 index returning +0.6% and +4.2% respectively in September.
- The sectors that outperformed during the month of September were IT, pharma and consumer durables. The sectors that underperformed during the month were PSU, banking, oil & gas and metals.
- Global markets saw some volatility during the month with signs of a second wave in Covid-19 cases being seen in certain major European countries. Developed markets underperformed Emerging & Asian markets during the month of September. The MSCI World index returned -3.6% in September, while the MSCI Emerging Markets index and MSCI Asia ex-Japan index returned -1.8% and -1.7% respectively.
- The US markets underperformed in September, with the benchmark S&P 500 index returning -3.9% during the month. Major European markets like France, UK and Germany also ended the month in the red. Within Asia—Japan, South Korea Taiwan and India outperformed in September, while Indonesia, Hong Kong and Thailand underperformed.
- Foreign portfolio investors (FPIs) registered a net equity outflow ₹ 4,690 crore in the month of September, compared to a record net inflow of ₹ 45,637 crore in the previous month.
- Domestic Institutional Investors (DIIs) registered a marginal net inflow of around ₹ 110 crore in the month of September, compared to a large net outflow of ₹ 11,047 crore in the previous month.
- Covid-19 cases continue to rise in India although it has seen some flattening recently in terms of new cases/active cases. The mortality rate in India has been quite low at ~1.5% and the recovery rate is high--at above 80%, which helps to provide hope of some peaking-out in the next few months.
- The government also continues to announce gradual opening up of the economy via Unlock 5.0. We have seen a heathy recovery in various high frequency economic indicators from their April lows. Various economic activity trackers/indices indicate that business/economic activity in India is now back to ~80-90% of pre-Covid levels.
- We expect Nifty earnings to grow by 2% / 30% in FY21/FY22E. This assumes normal business conditions which looks difficult under the current scenario. Downside risks to our estimates exist.
- With the sharp recovery in markets and muted corporate earnings growth, the Nifty index currently trades at 21x (12 m forward PE), which is higher than its historical average.

### Fixed Income market developments and Outlook

- Bond yields softened a bit during the month helped by various RBI measures to manage yields (like OMO purchases and Operation Twist), FPI debt inflows and some correction in crude oil prices. However, concerns on fiscal slippage and elevated inflation (above 6%) remained a bit of an overhang on debt markets, and capped the fall in yields. The benchmark 10 year G-Sec yield closed the month at 6.02%--down 6 bps. Banking system liquidity came down during the month (due to quarter-end advance tax payments to some extent), but still remained in comfortable surplus. Post the RBI policy in October, bond yields came down due to various liquidity & credit measures announced.
- Key highlights of the RBI monetary policy on 9th October 2020 were as follows:
  - RBI kept policy rates unchanged as expected. It also mentioned that it will continue with the 'accommodative' stance for current fiscal year and into next fiscal year as well, to revive growth on a durable basis.
  - RBI said that current elevated inflation primarily due to supply side disruptions and is transient in nature. It projects headline consumer inflation at 6.8% in Q2 FY21, and expects it to moderate to 5.4% in Q3 FY21 and to 4.5% in Q4 FY21.
  - On the economic front, RBI highlighted that various high frequency indicators are pointing to a recovery in the economy. The central bank gave an official GDP forecast of 9.5% contraction during FY21, with risks titled to downside. It expects economic activity to gradually normalize in H2 FY21, and GDP growth to turn positive (+0.5%) in Q4 FY21.
  - RBI mentioned that it will maintain comfortable liquidity through OMOs and will increase the size of OMO auctions to ₹ 20,000 crore (double of before). It also announced a bold measure of starting OMOs for SDLs (State Development Loans), which should help to rationalize spreads between SDLs and central govt. securities (G-Secs).
  - The central bank announced a liquidity measure of On-Tap 3-year TLTROs of ₹ 1 lakh crore upto March 31, 2020 for investment in corporate bonds and commercial paper of certain sectors. It also extended the earlier enhanced HTM limit of 22% of NDTL on SLR securities to March 2022 end.
  - RBI announced various credit enhancing measures--by increasing credit limit of retail loans, and also rationalizing risk-weight of housing loans, which will be positive for the sector.
- RBI kept borrowing calendar unchanged for H2 FY21 at ₹ 4.3 trillion and for full FY21 at ₹ 12 trillion. The overall borrowing for H2 FY21 has been less than expected and stands at historic low of 36% of the full year borrowing. An increase in government borrowing cannot be ruled out later in the year, especially if there is any further fiscal stimulus announced by the government.
- India's fiscal deficit for first five months of the fiscal year (April 2020 to August 2020) has already breached the full fiscal year target and stood at 109% of the budgeted estimate, compared to 79% of the annual target in the corresponding period in the previous fiscal year. The high fiscal deficit has been due to sharp drop in non-tax revenue & tax revenue collections—with total revenue receipts (upto August) at only 16.8% of the budgeted estimate so far, compared to 29.9% in corresponding period of previous fiscal year. However, government spending (upto August) was at 41% of the budgeted estimate (similar to last year's levels)—thereby causing a large shortfall/deficit.
- Finance Ministry data showed that GST collections in September rose to ₹ 95,480 crore (highest since the lockdown in March) from ₹ 86,449 crore in August.
- Foreign Portfolio Investors (FPIs) registered a net inflow of ₹ 3,009 crore in the month of September, compared to a net outflow of ₹ 4,156 crore in the previous month.
- The RBI monetary policy had a dovish undertone and it has been very supportive of growth, with ample liquidity measures. RBI also indicated that revival of the economy from the Covid pandemic disruption assumes the highest priority in conduct of monetary policy. This opens-up space for further rate cuts going forward, considering inflation remains within the projected territory.
- From an investment perspective on the fixed income side, we continue to prefer the medium-term part of the yield curve, as the curve is relatively flat at the longer end.

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