Pranitya Wealth LLP
Market Outlook
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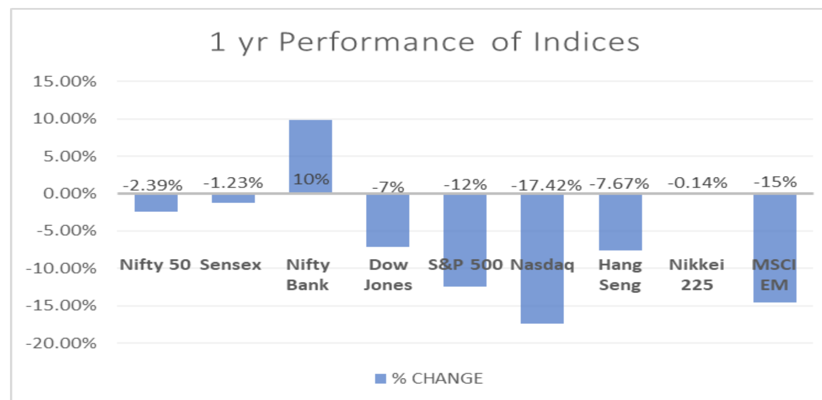
Initial Commentary

As we come to the end of the financial year 2022-23, we have seen equity and debt markets withhold their performances despite global weaknesses, high inflation, rising interest rates, continuing geopolitical tensions, battling the pandemic, currency swings, FII selling and last but not at all the least global banking turmoil. In this roller coaster financial year, we have seen performances of global indices as below –



Indian Economic Update

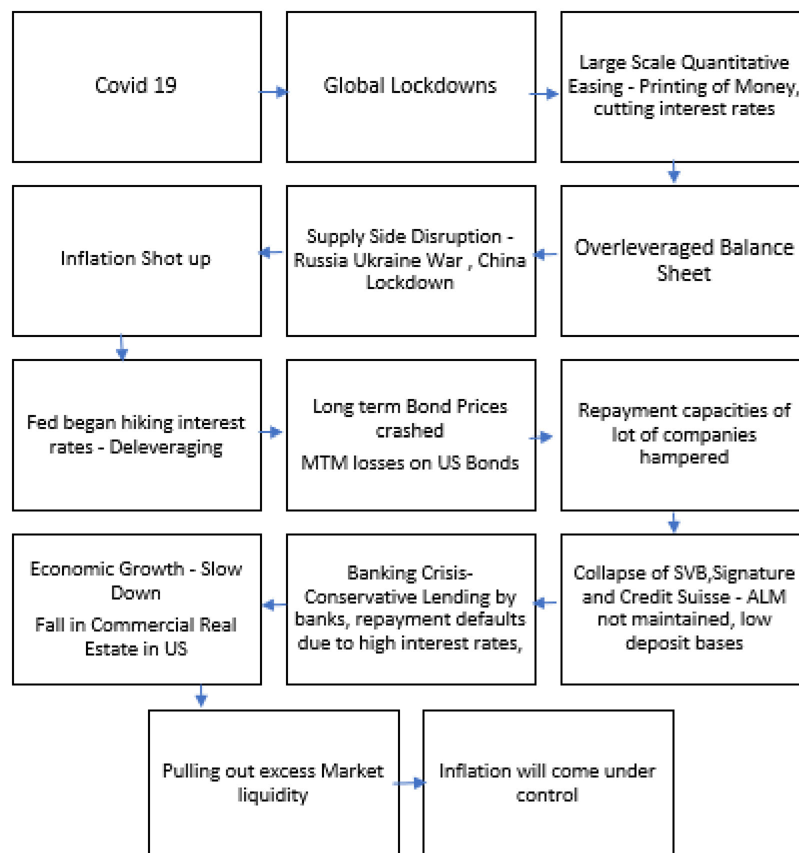
Inflation versus Growth

All central banks around the world have a heavy balancing beam to hold, upon which rests the entire country's economy. They have to strike a perfect balance between inflation and growth without tipping the beam, which is usually quite a tricky affair. And it seems to be getting trickier each week!
India's GDP growth slowed to 4.4% in Q3, FY23 GDP growth target is at 7%. Slowdown in growth numbers mainly due to declining private consumption expenditure with higher interest rates. Another factor affecting growth is the slowdown in exports due to economic slowdown in Europe who is one of the biggest trade partners for India.
India's retail inflation declined marginally to 6.44 per cent in February as against 6.52 per cent in January, the inflation rate has remained above the Reserve Bank of India's (RBI) tolerance band of 2-6 per cent for the second straight month. We expect one more rate hike of 25 bps by RBI in the upcoming MPC on April 6th.
Along with our central bank, it is crucial to keep an eye on US Fed Policies.

US Fed Policies and Global Banking Crisis

When Covid-19 hit and global lockdowns came into effect, US central bank started printing money, lowering key interest rates, and issuing stimulus cheques to help keep the economy going. There was a large influx of money as a result of cheap loans and suddenly balance sheets where over leveraged. This coupled with supply side disruptions due to war and geo

political tensions, China going into a lockdown again last year, pushed the inflation upwards to a 40 year high of 9% and prices for even basics after opening up skyrocketed. Thus began the process of US Fed raising interest rates in order to curb inflation. Till March 2023, Fed has raised interest rates to 4.75% from nearly 0.25% a year ago. It is expected that there will be one or two more rate hikes of smaller size before Fed changes it stance and pauses the rate hike cycle. It may start cutting interest rates from 2024.
With credit getting expensive, loan repayment defaults by companies, poor deposit bases (due to accelerated deposit outflows) and neglect of banking regulations caused ultimate collapse of some of the banks in US.
This US banking crisis however is very different from what US went through in 2008. This turmoil seems more of a "crisis of confidence" than anything else. Indian Banking system has been largely insulated from this volatility with consistent deposit flows. Banks have emerged stronger post the NPA cycle of the past decade, NPAs are now 5% down from a peak of 11.5%. Regulatory tightening has also helped liquidity parameters improve and LCRs are now 140% vs 125% 5 years ago (Source: Annual financial reports).



Equity Markets

Indices have dropped by average 2% since April 2022, and Nifty 50 dropped by 6% in last 3 months. Decoupling of Indian market theory is too optimistic to assume. Indian markets will mostly follow global trend. With geopolitical tensions, global banking instability, high inflation, US Fed unwavering stance on bringing down inflation, and the resultant FII outflows, Indian equities are now undervalued/fairly valued considering historical average valuations.

At current level Nifty 50 (17081) is trading at a multiple of 21.96 trailing whereas 10-year average PE is around 20. After the current correction, we opine in our last market outlook, to accumulate stocks of companies with good earnings growth at a very reasonable valuation for long term (by long term we mean minimum holding period of 3-5 years). Investors should definitely focus on the long term economic upcycle in India. Avoid high beta and expensively valued mid cap and small cap stocks amid this volatility. We will see return only when invested at a right value and the time of buying quality at any price is now over. Strong earnings, domestic buying and inflows from FPIs are some of the major positive triggers essential for markets to bounce back in this globally weak scenario. India is quite resilient on the economic front among all emerging nations.

Direct Tax collections up to 10th March 2023 shows a gross collection is at Rs. 16.68 lakh crore which is 22.58% higher than the gross collections for the corresponding period of last year. This collection is 96.67% of the total Budget Estimates and 83.19% of the total revised estimates of Direct Taxes for F.Y. 2022-23.

At Rs 1.49 lakh crore, India's goods and services tax (GST) collection for the month of February jumped by 12% year on year (although down from 1.56 lac crore in January 2023)

Foreign Institutional Investors' / Domestic Institutional Investors' Activity -

FIIs have turned net buyers for the month of March 2023, mainly due to a large investment in Adani group. But we feel with global investors becoming less bullish on the US due to the expected elongated rate hike cycle, rising trade deficit, elevated debt levels, selling will slowly cool off with trickling inflows of FPI/FII money.

With US Fed commentary indicating rate cuts from 2024 onwards and only another one or two rate hikes in coming months, we expect stronger FII inflows coming back from 2024 when Fed policy reverses or they indicate a pause in rate hikes. Most of the flows have come in Financial, IT, Capital Goods and Healthcare sector.

DIIs have remained loyal buyers in this market, and they have taken advantage of this correction to buy at lower levels. We have seen a steady increase in net buying by DIIs, especially in the past 3 months.

It is important to keep an eye on FII and DII activity as they have a major share in the Indian markets today. FII holding is around 20% of the Indian market and that DII's is 16%.

	FII Rs Crores			DII Rs Crores		
Date	Gross Purchase	Gross Sales	Net Purchase / Sales	Gross Purchase	Gross Sales	Net Purchase / Sales
Mar-23	1,64,136.84	1,62,497.00	1,639.84	1,30,862.48	1,02,793.67	28,068.81
Feb-23	1,62,167.67	1,73,258.31	-11,090.64	1,30,472.45	1,11,233.17	19,239.28
Jan-23	1,55,345.35	1,96,810.08	-41,464.73	1,43,909.70	1,10,497.85	33,411.85
Dec-22	1,39,091.40	1,53,322.49	-14,231.09	1,36,300.97	1,12,141.84	24,159.13
Nov-22	2,21,844.65	1,99,298.31	22,546.34	1,27,432.18	1,33,733.50	-6,301.32
Oct-22	1,78,270.46	1,78,759.52	-489.06	1,01,182.03	91,905.06	9,276.97
Sep-22	1,91,146.65	2,09,454.95	-18,308.30	1,61,757.96	1,47,638.21	14,119.75
Aug-22	1,93,337.27	1,71,311.65	22,025.62	1,17,263.25	1,24,331.88	-7,068.63

Fixed Income

We have always stressed upon the importance of asset allocation. This financial year has been a lesson to every investor about having the right amount of assets in different categories. Significance of gold and debt in the portfolios was effective in protecting the downside of our

financial investment. We are currently at a point in investing where both equities and debt look equally attractive.

With Fed announcing rate cuts in 2024 and nearing to the end of interest rate hike cycle, it indicates a peak out for the bond yields. Investing in medium to long term funds and locking in yields at 7% to 8.5% currently makes good sense. Yields have improved significantly making the risk- reward ratio very favorable.

There was an amendment in taxation of debt mutual funds in the Finance Bill 2023, which a huge punch to the debt mutual fund industry. As per the amendment, it is proposed to do away with the long capital gain tax benefit of indexation and now any capital gain for debt will be taxed at as per marginal rate of tax being deemed as short-term gain. Mutual fund market saw a large amount of inflow in the last week of March as investors preponed their debt investments in order to not lose on the indexation benefits.

Current yield curve is flat, one year Gilt being at 7.18% and 10 year at 7.33% leaving spreads are at the lowest levels. There was an active shortage of liquidity as mutual funds to dump very short term papers due to redemptions of liquid funds and switch into long term debt funds by investors. Thus, the return on liquid funds went negative for a day or two due to unforeseen phenomenon.

Summary-

1. Invest in long term debt funds as far possible before 31st March 2023, which we have been suggesting past week to all our clients.
2. Secondly, all is not lost in terms of investing in debt funds and a lot of advantage lies for mutual funds still over bank deposits.
3. Equity as suggested in our March 2023 outlook looks quite attractive and gradual allocation on every fall will help to build good long-term portfolio.
4. One need to moderate expectations on returns looking at the current earnings growth and inflation. One also needs to broaden the horizon of investing as volatility will remain in the short term.
5. It is difficult to imagine investing in larger markets currently, as globally 70% of the markets are having lot of issues.
6. There may be volatility in the short term but looking at last month till date performance, large cap stocks have seen good returns and steadily investing in equities would be beneficial over long term.
7. For Indian market to grow we feel private investment has to kick in and political stability needs to be maintained.
8. Looking at historical short positions held by FPIs in the futures market, we feel any positive news will take markets up by 2%-5% just on account of short covering
9. On the other hand, bad monsoon, escalation of war and other geopolitical situation can deepen the market sentiment.
10. India still will remain one of the fastest growing economies and may attract flows once global volatility settles down.

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