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Macro-economic developments

- The Non-farm payrolls in the United States rose by a strong 304,000 in January 2019, much higher than market expectations of around 170,000. The unemployment rate moved up a bit, to 4% in January, from 3.9% in the previous month.
- US GDP growth for Q4 2018 came in at a healthy 2.6%YoY, higher than estimates of 2.2%. Growth was helped by consumer spending (biggest component of US GDP), which rose by 2.8%YoY during the quarter. Meanwhile, residential fixed investment and imports were a drag on GDP. For the full year 2018, GDP growth was a healthy 2.9%YoY, compared to 2.2%YoY growth in 2017.
- Data released recently showed that the US merchandise (goods) trade deficit rose by 10%YoY in CY 2018 to an all-time high of $891 billion. The merchandise trade deficit of US with China also rose by 11.6%YoY in CY 2018 to an all-time high of $419 billion. This is despite the US imposing trade tariffs in a progressive manner on China during the course of the year, and China also imposing retaliatory tariffs on the US. Presently, negotiation / talks are ongoing between the US and China authorities on the future course of action on trade tariffs. The data release also showed that the overall trade deficit of US (both goods & services) rose 12.5%YoY in CY 2018 to a decade-high of $621 billion.
- Trade deficit for the month of January 2019 in India widened to $14.7 billion, versus $13.1 billion in the previous month. Export growth rose 3.7%YoY in January vs just 0.3% in the previous month, primarily due to higher non-oil exports. Import growth was absolutely flat at 0.01% vs -2.4%YoY in the previous month. Gold imports rose 38.2%YoY in January, while oil imports fell by 3.6%YoY during the month.
- The Index of Industrial Production (IIP) growth picked up to 2.4%YoY in Dec 2018, from 0.3%YoY in the previous month. Manufacturing sector (having 78% weight in IIP) growth rose to 2.7%YoY in Dec 2018, from -0.6%YoY in the previous month. For FYTD19 (upto December) IIP growth was stronger at 4.6%YoY, compared to 3.7%YoY in the corresponding period, a year ago.
- Consumer Price Index (CPI) headline inflation fell marginally to 2.0%YoY in Jan 2019, from 2.1%YoY in the previous month. Food inflation (biggest component of CPI), came in at -2.2%YoY in January, vs -2.6%YoY in the previous month. Core inflation (ex food & fuel) moderated to 5.3%YoY from 5.6%YoY in the previous month. Fuel inflation also moderated substantially to 2.2%YoY from 4.5%YoY in the previous month.
- Crude prices, continued to rise in February, with OPEC cuts and Venezuela sanctions continuing to put pressure on oil prices. Brent crude closed the month up 6.6%, near the $66/bbl mark.
- The rupee closed the month up ~0.5%, at 70.75/US dollar.

Equity market developments and Outlook

- Indian markets closed the month on a flattish note with the benchmark Nifty 50 index falling 0.4%. The broader markets continued to underperform, with the Nifty Midcap 50 index and Nifty Small-cap 100 index falling 1.7% and 3.2% respectively in February. Sectors that underperformed during the month included power, banking, FMCG and metals. The sectors that outperformed during the month were auto, oil & gas, and realty.
- Global markets continued with their gains in February (although more tempered than in the previous month), with the MSCI World index, MSCI Asia ex-Japan index and MSCI Emerging Markets index returning +2.8%, +2.1% and +0.1% respectively.
- In the US, the S&P 500 index rose by 3.0% in February, after a sharp rise in the previous month. Most of the European markets were also buoyant in the month, with France's CAC 40 index rising a healthy 5.0%. Asia also performed well, with China's Shanghai Composite index leading the pack, and surging 13.8% in February, on the back of market expectations of some resolution to the US-China trade dispute, and hopes of further rate cut by the Chinese central bank to support the slowdown in growth. Other Asian markets which fared well during the month were Taiwan, Japan and Hong Kong, although markets like Indonesia, Korea and India were relative underperformers within the region. Other emerging markets like Russia and Brazil also relatively underperformed in February.
- Foreign portfolio investor (FPI) flows picked up strongly to ₹15,328 crore in February, after seeing a net outflow of ₹505 crore in the previous month.
- Domestic Institutional Investor's (DIIs) net investment in equities continued to slow down, and registered a net outflow of ₹566 crore, after seeing a net investment of ₹2,147 crore in the previous month.
- Q3 FY19 corporate earnings were slightly below expectations, although at a broader level, they were relatively better than the previous quarter. We expect Nifty earnings growth for FY19 to come in at 11%YoY (vs 8%YoY growth seen in FY18), and accelerate to 20%YoY growth in FY20.
- Although we still prefer large-caps more from a risk-reward perspective, the deep correction in mid-caps and small-caps has presented some attractive bottom-up opportunities.

Fixed Income market developments and Outlook

- Bond yields continued to harden during the month on the back of rise in crude oil price, foreign outflows in the debt markets, higher govt. bond supply, some credit events and also some liquidity tightness. The new 10 year benchmark yield closed the month at 7.41% - up 13 bps.
- The RBI announced OMO purchases of ₹25,000 crore for March, to infuse liquidity, but it was below market expectations—as the month typically witnesses seasonal liquidity tightness.
- India's fiscal deficit for FYTD 19 (upto January) reached 122% of the budgeted full year target, compared to 114% in the corresponding year ago period. Fiscal deficit has been elevated due to higher revenue expenditure, and lower than budgeted GST collections, primarily.
- In the Interim Budget announced on 1st Feb 2019, the government had revised the fiscal deficit for FY19 to 3.4% of GDP (vs 3.3% earlier), and fiscal deficit for FY20 had been budgeted at 3.4% (vs 3.1% earlier).
- Foreign Portfolio Investors (FPIs) in debt markets registered a net outflow of ₹9,290 crore, compared to a net outflow of ₹2,601 crore in the previous month.
- RBI has been quite dovish in its tone, and cut inflation forecasts recently. Further rate cuts could be expected from the RBI, and it will continue to be data dependent.
- However, corporate bond spreads continue to remain elevated due to risk aversion due to recent credit crunch/events. The supply of paper will also be higher and March is typically the month of seasonal liquidity tightness. The higher total borrowings of the government is currently crowding out private investments to some extent, although we expect the current government to consolidate fiscal deficit further post 2019.
- From an investment perspective, we continue to prefer the shorter to medium term end of the yield curve.