PGIM
India Mutual Fund

Market Outlook

January 2022

Equity Market

Focus on growth consistency augur well

The start of the calendar year was flattish, with the NIFTY returning -0.1% during the month. The buoyancy seen in the first half of the month retracted later on concerns of rate hikes by the US Fed, rising bond yields, and higher crude prices. The midcap and small-cap indices were a tad weaker, returning -0.6% and -1.5% respectively. Sector-wise; Power, Energy, Banks and Auto were key outperformers while IT, Pharma & Healthcare and Consumer were the key laggards.

On the Macro front, IMF has trimmed India's GDP growth estimates for FY22 to 9% given the impact of the new Covid wave.

Bank credit grew 8.01% to INR 115 trn and deposits rose 9.28% to INR 159.83 trn in the fortnight ended 14 January 2022. In the previous fortnight ended 31 December, 2021, advances rose 9.16% and deposits increased 10.28%. In FY21, bank credit increased 5.56% and deposits grew 11.4%. These are early signs of credit growth picking up.

The wholesale price inflation rate in India came in at 13.56% in December 2021 from 14.23% in the previous month, which was the highest in 23 years. This was the 9th straight month of double digit WPI inflation – first time in 29 years. Headline CPI print for December 2021 came in at 5.6% and continues to be within the RBI's comfort zone.

GST collections in January 2022 were at a record high at INR 1.4trn. India's vaccination pace continues to chug along with 92% of the adult population receiving at-least one dose.

India's industrial production increased 1.4% in November of 2021 vs 4% in October – the smallest gain in industrial output since March 2021.

FIIs were net sellers of USD 4.8bn in January 2022 – taking their net sell figure in last 4 months to USD 9.6bn – highest ever 4-month net outflow. DIIs were net buyers +USD 2.9bn, driven by both MFs and Insurance.

Budget

The Union Budget was announced on 1 February 2022, focusing on growth, investments, and credibility. There would be upward pressures on bond yields as government borrowings will be on the higher side. However, the focus on asset creation, infrastructure, and capex is expected to provide long-term growth and development, which are more important than near-term fiscal slippages.

Despite several important state elections, the government did not resort to populist measures, which is a positive. Also, the Union Budget seemed pragmatic in its approach and focused on transparency, and numbers on the conservative side (Tax revenues are budgeted to grow ~10% YoY and disinvestment target of INR 650bn for FY23).

With a gross budgetary support capex kitty of INR 7.5trn (vs INR 5.5trn in FY22) and positive announcements on infrastructure space augur well for the country's gross fixed asset formation.

Extension of tax incentives for start-ups, reforms in customs duty for a few sectors/products, infra status to new age sectors such as data centers/ battery infrastructure, higher domestic allocation in defense capex augur well for a range of industries. Extension of ECLGS scheme and extension of the same to the beleaguered hospitality sector also shows the intent of the government to provide support to MSMEs. It would be positive for the banking system to help them manage asset quality better. Overall, the Budget is moving in the direction of becoming a non-event from a stock market point of view, which is a positive.

Earnings

The Earnings season has been in line with estimates, with 25 Nifty companies having declared their results so far. Sales growth came in at 29% YoY vs est of +28%

EBITDA +14% YoY vs est of 16%

PBT +21% YoY vs est of 21%

Net Income +17% YoY vs est of 16%

Of the 25 companies, 12 reported profits above estimates, 8 in-line and 5 below.

Going forward

The Budget has been seemingly silent on bond inclusion and higher gross borrowings, making a case for bond yields inching up. However, with GDP growth estimated to be upwards of 9% in FY23, some hardening of yields and acceptance of an expansionary policy is an acceptable trade-off.

While inflation-related worries remain in the near term, India's medium-term growth prospects are strengthening. We remain positive on Indian Equities. As of 31 January, NIFTY has corrected ~6% from its peak, which we reckon is healthy and has taken some of the froth in certain sectors and makes risk-reward better than before. Corporate earnings growth continues to be strong. We continue to focus on companies with visible growth at reasonable prices.

Debt Market

Yields set to rise further

Indian bond yields, continuing their upward journey, were higher by 10 to 20 bps across the curve in January 2022 as global bond yields hardened on the back of increasing expectations of a rate hike by the US Fed. The RBI’s conduct of reverse repo auctions led to overnight rates staying close to 4% for a major part of the month. Covid 19 cases increased sharply at the beginning of the month but tapered off towards the end. The Union Budget presented on 1st February spooked the bond markets as the fiscal deficit and the borrowing number were higher than market expectation and the 10-yr bond sold off by 15 bps??. The fiscal deficit for FY23 at 6.40% was higher by 30-40 bps than market expectations and the absolute number of the Central government’s budgeted borrowings was also higher than the market expectations. There was also an anticipation in the market with respect to an announcement of inclusion of Indian government securities in the global bond indices but there was neither a mention nor a timeline in the Budget. The gross supply of SLR securities (Centre +states) is likely to be near INR 23 trn and given the fact that, in our view, there will possibly be no RBI support in FY23 through outright OMOs, and with credit offtake slowly picking up, there is a substantial demand supply mismatch. This, is our view, will continue to put upward pressure on yields , especially the longer end and we expect that in the near term the steepness in the curve can continue.

INR depreciated marginally by 0.38% during the month. Brent crude rallied sharply by 16% during the month on the back of geopolitics over Ukraine. FPI flows into debt bucked the trend as they bought bonds to the extent of USD600mn during the month while the equity markets saw a sharp sell-off from the FPIs to the extent of USD 5bn.

We are underweight duration as we expect yields to continue to rise. We also expect Inflation to overshoot RBI expectations as the economy starts to operate at pre-Covid levels.

Fixed Income Market

	December 2021	January 2022	Change (in bps)
Overnight rate (NSE MIBOR)	3.60%	3.40%	-20
1 yr CD	4.56%	4.83%	27
10 yr GOI Yield	6.46%	6.68%	22
USD/INR	74.28	74.62	34 paise
IIP (Monthly with 2 month lag)	4.00%	1.40%	-260
CPI (Monthly with 1 month lag)	4.91%	5.59%	68
5 Yr AAA PSU spread (bps)	15	15	0
5 Yr OIS	5.37%	5.68%	31
US 10 Yr yield	1.51%	1.79%	28
CRR	4.00%	4.00%	0
Reverse REPO	3.35%	3.35%	0
REPO	4.00%	4.00%	0

Source: RBI Weekly Statistical Supplement & Bloomberg

Note: IIP has been revised higher for the previous reading.

Source: BSE, RBI & Bloomberg