Wealth India

MONTHLY INVESTMENT PERSPECTIVES FEB-24

GLOBAL MACRO: EASING MONETARY POLICIES OVERALL

The U.S. economy should slow materially yet skirt the recession in 2024. Europe and the UK should face stagnation. China is expected to slow further in 2024, adding challenges to overall Asia ex-India. In the shorter term, there could be slight deviations away from the larger expected trend-line path. For instance, the U.S. reported a stronger than expected Q4CY23 GDP at a surprising 3.3%. The Atlanta Federal GDP Nowcast now expects growth of 3% for Q1CY24, vs. less than 2% at end-CY23. Similarly, there are signs of growth in the Eurozone as bank lending starts to pick up. The Israel-Hamas issue has suddenly spawned across many regions, of particular financial relevance being the Red Sea. While these might be blips in the short run, the overall environment supports a constructive market outlook for the year.

GLOBAL EQUITIES: CRIES FROM THE CRE BUT U.S. TECH ROBUST

The U.S. labour market report for Jan-24 surprised with much higher job growth than expected. Market participants immediately abandoned hopes of a Mar-24 U.S. interest rate cut, with Jun-24 being the more likely pivot date. U.S. Commercial Real Estate (CRE) in aggregate is still declining – the risk of rolling (smaller regional) bank failures was flagged on July-23. This risk remains, but the U.S. megabanks most likely have a higher quality CRE portfolio. As such, fears of material systemic risks are overblown. On the other hand, U.S. tech Earnings have been resilient. There has been a reacceleration of public cloud services, a recovery in digital advertising and Gen AI innovation with a potential increase in IT Budgets. There are first indications that U.S. households are beginning to draw down/switch out of deposits or similar instruments, and this trend should accelerate over the coming months.

Overall, bonds look very attractive as rates should fall in mid-2024. Bonds are expected to offer a better risk-return profile due to convexity. We **remain OW on U.S. and Japan & India, neutral on Asia ex-Japan & UW on EM ex-Asia and Europe.** Sectorally, **we remain OW on Comm. Svcs., Info Tech, Health Care & Cons. Discretionary; remain neutral on Real Estate, Financials and industrials and UW on Energy, Materials, Utilities, & Cons. Staples.**

GLOBAL FIXED INCOME: YEAR OF THE BOND

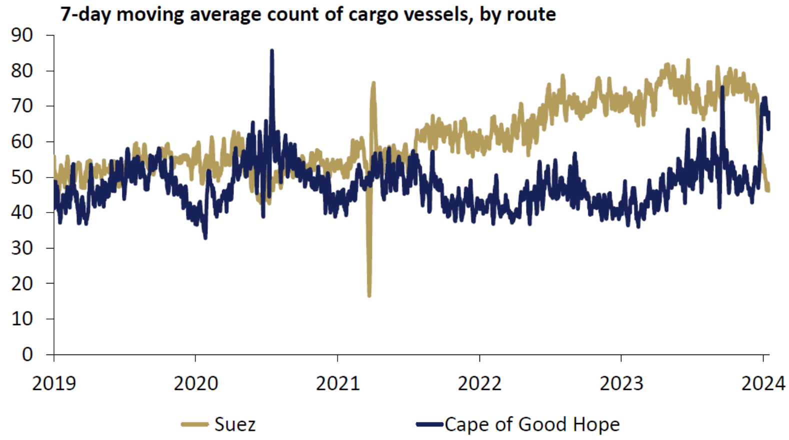
The US central bank's decision to maintain its key overnight interest rate at the 23-year high mark since July reflects a cautious stance in managing inflation. Emphasizing the need for greater confidence in sustainable inflation movement before considering rate cuts demonstrates a commitment to meticulously monitoring economic indicators.

Federal Reserve Chair Jerome Powell's firmly pushing back against cutting rates in the spring signals a deliberate strategy to avoid premature policy adjustments. This transparent communication aims to manage market expectations and curb speculations that led to the recent rise in yields above the 4% mark. **We remain OW on DM IG bonds, Neutral on HC EM Bonds, Subordinated Debt & DM Sovereign Bonds, and UW on HY Bonds. We also remain OW on Duration** in advance of Fed easing.

GLOBAL COMMODITIES: ANOTHER RATE-SENSITIVE ASSET

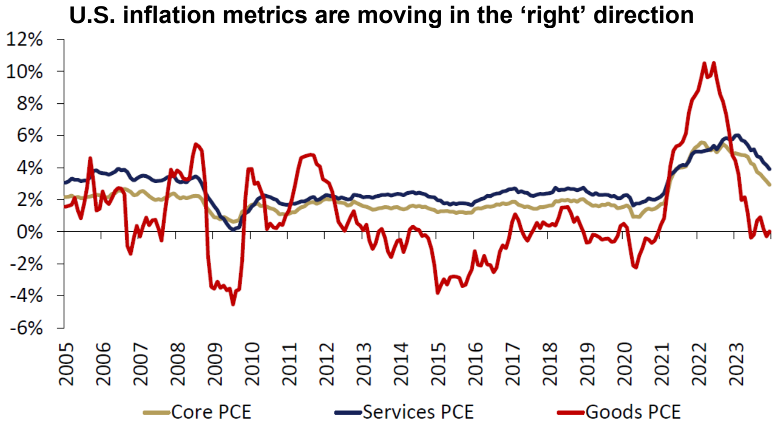
The oil prices were down 7% last week. This downward decline was influenced by US economic data that suggested a lower likelihood of imminent rate cuts by the Fed Reserve. The robust job creation figures in the U.S. have led to a strengthened dollar, impacting global crude demand. Concerns about China's economic recovery continued to exert pressure on the oil market. Evergrande's $300 billion debt crisis has led to its liquidation, with over 50 Chinese property firms declaring default since 2021. The collapse of the Chinese real estate market could affect metal imports, global brands, and international suppliers. Gold was flat with a downward bias, influenced by the robust US labour market and higher wages. Consequently**, we remain one notch OW on Gold** on the back of dollar weakness.

Red Sea piracy continues: Reflection in inflation yet to be seen



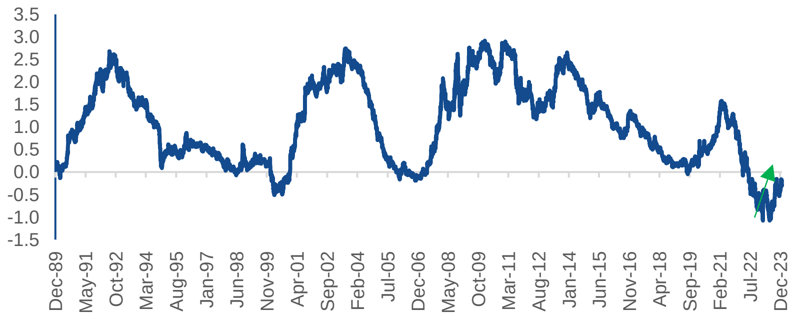
Source: International Monetary Fund, LGT

U.S. inflation metrics are moving in the 'right' direction



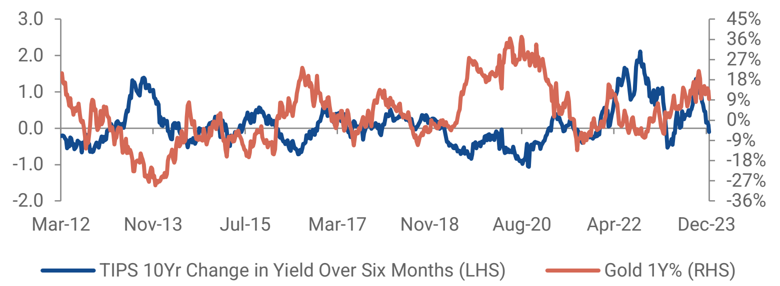
Source: Bureau of Economic Analysis, LGT

Yield Curve inversion and recession



Source: Bloomberg

TIPS yields change over 6 months has just turned negative which is positive for Gold given their inverse correlation



Source: Bloomberg

INDIA MACRO: SCAVENGING FOR LIQUIDITY

India's liquidity deficit has jumped to a nearly 8-year high. From the supply side, government small savings schemes have offered higher interest rates, making them more attractive than deposit rates. Interestingly, household financial savings have fallen to a nearly 5-decade low of 5.1% of GDP (coming from highs of 11.5% seen in FY21). While this does question the theme of sustainable financialization of Indian household savings, the flip side is that much of these savings have trickled down (instead, swelled) into physical assets, viz. real estate and hence a strengthening of India's GFCF. Nevertheless, with India's growth model tilting from (retail) credit-led to investment-led, how these investments are funded remains to be seen. At the moment, a party in equity funding is reflected in extremely low return expectations from this asset class, but these are also classic signs of a bubble. In that event, a reversion to debt-driven financing is on the cards for which, at the moment, liquidity does not seem capable enough to handle. Deposits (and liquidity in general) need to be beefed up for resilient growth, so all eyes would remain on the RBI to unleash some novel instrument to cushion the liquidity deficit or, if nothing else, some OMO purchases.

INDIA EQUITIES: POCKETS OF FROTH – SEEK VALUE

Rate cuts have typically been very conducive for equities. Much of the rally is primarily demand-driven, i.e. FII-led, as they tend to seek growth. This time around, arguably, some of the rate cuts have already been priced in, seen in near-heady valuation multiples of specific segments of stocks. The best would be to avoid such securities and ring-fence portfolios to mitigate valuation-related risks. For a holding period of 1 year, capital market theory suggests that small and mid-cap future return expectations are now unattractive. This is not a cause for surprise, given the surging domestic and FII flows. The RBI would naturally operate to absorb this out.

We remain Neutral between Equities and Bonds, maintaining strategic Asset Allocation. Within Large and Midcaps, **we stay two notches OW on Large caps vs midcaps**(prefer large caps).

INDIA FIXED INCOME: 2024 - YEAR OF THE BOND

Indian fixed-income market had a positive start to the month following the Interim budget. The budget revealed a lower-than-expected fiscal deficit target of 5.1% for the fiscal year 2024-25, with this year's target also being reduced by ten basis points to 5.8%. The gross and net market borrowings through dated securities for the fiscal year 2024-25 are estimated at Rs 14.13 lakh and Rs 11.75 lakh crore, respectively.

A lower fiscal deficit is generally viewed positively by the fixed-income market as it suggests more restrained government borrowing, which can contribute to lower interest rates and improved market sentiment.

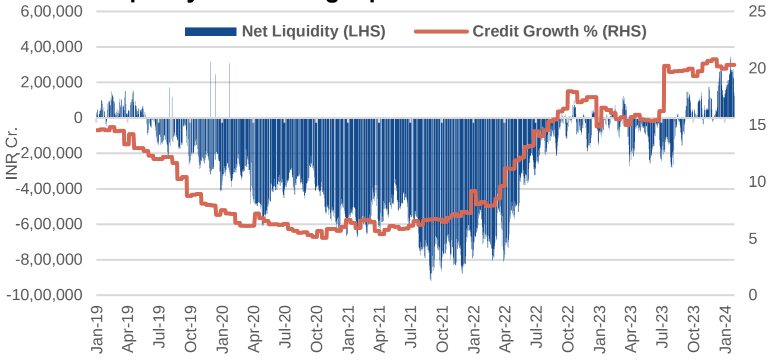
India's domestic macro indicators reflect resilient economic growth compared to major peers. The Reserve Bank of India (RBI) expects to maintain steady rates in the first half of 2024, with potential rate cuts later in the year due to disinflationary trends.

We remain positive on the medium to long duration of the yield curve as the yields in the mid to long end of the curve react early to changes in the interest rate cycle. Therefore, the 3-6-year range in the medium-duration segment of the yield curve is deemed attractive from a risk-reward perspective. In the short term, yields are expected to trade within a narrow range. Specifically, the 10-year government security (g-sec) will likely trade in the 7.00-7.25% range. Short-term movements in the yield curve may be influenced by liquidity surplus or deficit conditions, as no immediate rate easing actions are expected. **Maintaining an overweight position on the medium to long-duration segment of the yield curve is advised, considering recent yield levels and attractive carry. From a pure duration perspective, we remain overweight in government securities (G-Sec) compared to corporate bonds.**

CURRENCY: INR REMAINS TO BE A LIKELY MANAGED CURRENCY

The ultimate goal for India is to increase exports – for which the INR (like the CNY) would have to maintain a depreciation bias over the longer run consistently. The INR's depreciation bias or "weakening" can be measured via the REER – a basket of currencies against which the INR gets benchmarked. During the relatively short span of the last two years, India's inflation had been moderate and lower than the U.S. As a result, "management" of the REER was comparatively easy as, firstly, India was not able to boast of a carry return potential given lower inflation. Secondly, over shorter periods, the carry effect dominates interest rate parity (which would have dictated a REER appreciation). Going forward, with CPI likely to moderate towards Mar-24, the INR could remain rangebound (if not weaken further). However, U.S. rate cuts would remain a key to watch out for and may overshadow INR dynamics given the greenback's much larger liquidity (and demand). **Consequently, we remain one notch OW on the INR.**

India's Liquidity Crunch might put the brakes on Credit Growth



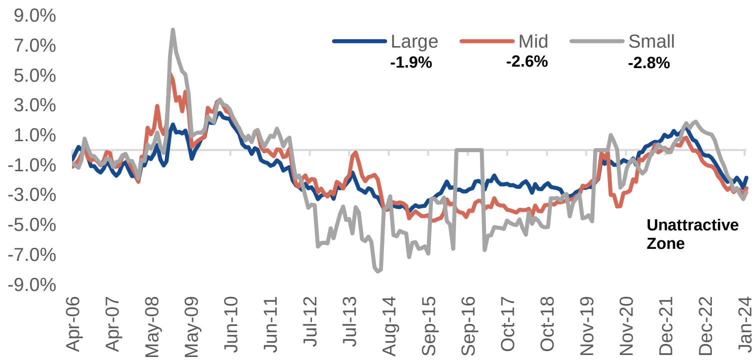
Source:RBI, Bloomberg

Rate Cut Cycle Nurtures FII flows and Forward Returns

Date		Bps	%	FIIs INR Cr.	
Start	End	Rate Cut	Nifty Return	Prior Period	Period
05-Mar-02	26-Oct-04	150	51.1	NA	
20-Oct-08	18-Mar-10	325	68		
17-Apr-12	19-Sep-13	75	15.6	19,761.90	154,027.70
15-Jan-15	05-Jun-18	175	24.7	22,061.59	91,310.35
07-Feb-19	02-May-22	225	54.2	-26,628.10	166,967.56

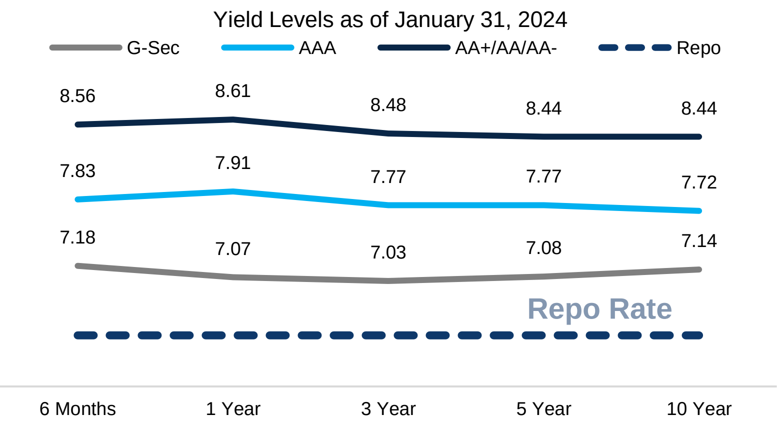
Source: Bloomberg

Capital Market Expectations: Very Low for Small and Mid Caps



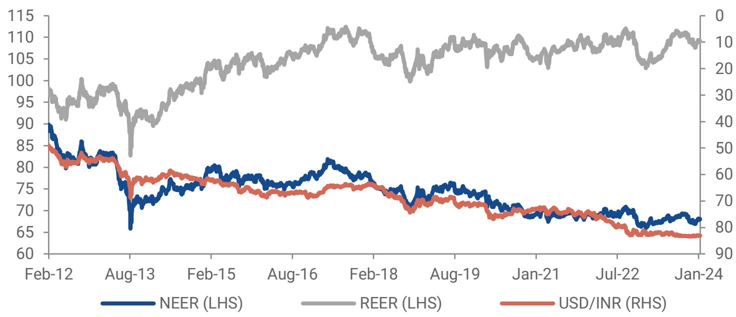
Source: NIFTY Indices, Bloomberg

Debt Market Snapshot



Source: Bloomberg, as on 31st January 2023

NEER largely stable, REER a tad stronger in H2CY23



Source: Bloomberg

TACTICAL ASSET ALLOCATION (TAA) VIEWS & PERFORMANCE

Asset Class Pairs	View	Favouring	Start Date	End Date / Open	Call Status	Alpha Return
Equities Vs Bonds	Positive	Equities	31-Dec-18	30-Apr-19	Close	5.90%
Large Cap Vs Mid Cap	Negative	Mid Cap	31-Dec-18	31-Jan-20	Close	-8.00%
Short Term Vs Long Term	Positive	Short Term	30-Nov-18	31-Dec-21	Close	-6.00%
USD / INR	Positive	USD	30-Nov-18	31-Jan-19	Close	2.20%
USD / INR	Positive	USD	31-Mar-19	30-Apr-19	Close	0.60%
USD / INR	Positive	USD	31-Jul-19	31-Dec-19	Close	3.70%
Gold Vs Cash	Negative	Cash	30-Nov-18	28-Feb-19	Close	-7.60%
Gold Vs Cash	Positive	Gold	31-Mar-19	30-Jun-21	Close	32.00%
Equities Vs Bonds	Positive	Equities	30-Nov-20	30-Apr-21	Close	11.80%
USD / INR	Negative	INR	31-Dec-20	31-Jan-21	Close	0.20%
USD / INR	Positive	USD	28-Feb-21	31-May-21	Close	-1.20%
USD / INR	Negative	INR	31-Aug-21	30-Sep-21	Close	-1.70%
Large Cap Vs Mid Cap	Negative	Mid Cap	31-Oct-20	30-Nov-21	Close	26.70%
Equities Vs Bonds	Positive	Equities	31-May-21	30-Nov-21	Close	8.90%
Short Term Vs Long Term	Positive	Short Term	30-Nov-18	31-Dec-21	Close	-5.90%
USD / INR	Positive	USD	31-Oct-21	31-Dec-21	Close	-0.70%
Gold Vs Cash	Positive	Gold	31-Jul-21	31-Jan-22	Close	-2.60%
Large Cap Vs Mid Cap	Positive	Large Cap	31-Dec-21	30-Apr-22	Close	0.90%
Gold Vs Cash	Positive	Gold	28-Feb-22	31-May-22	Close	-1.80%
Short Term Vs Long Term	Positive	Short Term	28-Feb-22	30-Jun-22	Close	2.20%
USD / INR	Positive	USD	31-Jan-22	31-Jul-22	Close	6.20%
Large Cap Vs Mid Cap	Positive	Large Cap	30-Jun-22	31-Jul-22	Close	-2.80%
Equities Vs Bonds	Positive	Equities	31-Dec-21	30-Sep-22	Close	0.80%
USD / INR	Negative	INR	31-Jul-22	30-Sep-22	Close	-2.60%
Large Cap Vs Mid Cap	Negative	Mid Cap	31-Jul-22	30-Nov-22	Close	-0.60%
USD / INR	Positive	USD	30-Sep-22	30-Nov-22	Close	0.10%
Gold Vs Cash	Negative	Cash	30-Jun-22	30-Sep-22	Close	6.50%
Equities Vs Bonds	Positive	Equities	31-Oct-22	31-Dec-22	Close	-2.00%
Large Cap Vs Mid Cap	Positive	Large Cap	30-Nov-22	31-Dec-22	Close	-1.80%
USD / INR	Negative	INR	31-Dec-22	31-Jan-23	Close	1.00%
Large Cap Vs Mid Cap	Negative	Mid Cap	31-Dec-22	31-Jan-23	Close	1.00%
Large Cap Vs Mid Cap	Positive	Large Cap	31-Jan-23	28-Feb-23	Close	-1.10%
USD / INR	Positive	USD	28-Feb-23	31-Mar-23	Close	-0.60%
Large Cap Vs Mid Cap	Positive	Large Cap	31-Mar-23	30-Apr-23	Close	1.70%
Corp Bonds Vs G-Secs	Positive	Corp Bonds	30-Nov-18	30-Jun-23	Close	7.80%
Short Term Vs Long Term	Positive	Short Term	30-Nov-22	30-Jun-23	Close	-0.97%
Equities Vs Bonds	Positive	Equities	31-Mar-23	30-Jun-23	Close	8.10%
Gold Vs Cash	Positive	Gold	30-Nov-22	31-Jul-23	Close	8.80%
USD / INR	Negative	INR	30-Apr-23	31-Aug-23	Close	-1.20%
Large Cap Vs Mid Cap	Negative	Mid Cap	31-Jul-23	31-Jul-23	Close	6.10%
Gold Vs Cash	Negative	Cash	30-Sep-23	31-Oct-23	Close	-6.32%
USD / INR	Positive	USD	30-Sep-23	31-Dec-23	Close	0.20%
Short Term Vs Long Term	Negative	Long Term	30-Jun-23	31-Jan-24	Open	0.41%
Corp Bonds Vs G-Secs	Negative	G-Secs	31-Jul-23	31-Jan-24	Open	-0.20%
Large Cap Vs Mid Cap	Positive	Large Cap	30-Sep-23	31-Jan-24	Open	-7.20%
Gold Vs Cash	Positive	Gold	31-Dec-23	31-Jan-24	Open	-1.70%
USD / INR	Negative	INR	31-Dec-23	31-Jan-24	Open	0.20%

M-o-m Summary	Equity vs Bonds	Large vs Mid	Corp. Bond vs. G-Secs	ST vs LT	USD vs. INR	Gold vs Cash
% of Months calls issued	52.4%	79.4%	98.4%	88.9%	63.5%	84.1%
Success Ratio (%)	63.6%	46.9%	57.4%	54.5%	59.0%	57.7%
Avg. positive alpha	4.3%	2.4%	0.5%	0.6%	1.1%	3.8%
Avg. negative alpha	-2.7%	-2.4%	-0.5%	-0.9%	-0.9%	-3.3%
Avg. alpha	1.8%	-0.2%	0.1%	-0.1%	0.3%	0.8%

Source: Bloomberg. Assuming a 6% annualised yield for cash.

GLOBAL ASSET PERFORMANCE SNAPSHOT

	Asset	Current	1m	3m	6m	1y		Current	1m	3m	6m	1y
	Equities						Commodities					
Global	S&P 500 INDEX	4,846	1.6%	15.5%	5.6%	18.9%	TR Commodity CRB Index	272.4	3.3%	-3.1%	-3.5%	-2.0%
Global	EURO STOXX 50 Price EUR	4,648	2.8%	14.5%	4.0%	11.6%	Indian Crude Oil Basket	82.5	6.8%	-6.5%	-3.7%	0.9%
Global	FTSE 100 Index	7,631	-1.3%	4.2%	-0.9%	-1.8%	Brent	81.7	6.1%	-6.5%	-4.5%	-3.3%
Global	Nikkei 225	36,287	8.4%	17.6%	9.4%	32.8%	Gold	2,039.5	-1.1%	2.8%	3.8%	5.8%
India	NSE Nifty 50 Index	21,726	0.0%	13.9%	10.0%	23.0%	Aluminium	2,252.4	-4.2%	0.2%	-0.2%	-14.0%
India	NIFTY Midcap 100	48,569	5.2%	24.9%	28.8%	58.3%	Copper	390.6	0.4%	7.0%	-2.5%	-7.6%
India	NIFTY Smallcap 100	16,026	5.8%	26.7%	36.9%	68.7%	Corn	448.3	-4.9%	-6.4%	-11.1%	-34.1%
India	NSE Nifty 500 Index	19,802	1.9%	17.9%	16.1%	32.6%	Soyabean	1,222.3	-5.8%	-7.7%	-8.5%	-9.9%
	Fixed Income						Currencies					
Global	US Generic Govt 10 Yr	3.91%	3.88%	4.93%	3.96%	3.51%	Dollar Index	103.27	1.9%	-3.2%	1.4%	1.2%
Global	German Bunds	2.17%	2.02%	2.80%	2.49%	2.28%	EUR/USD	1.08	-2.0%	2.3%	-1.6%	-0.4%
Global	JGB 10Yr Comp Yield	0.74%	0.65%	0.95%	0.61%	0.51%	USD/JPY	146.92	4.2%	-3.1%	3.3%	12.9%
Global	UK Gilts 10 Yr	3.79%	3.54%	4.51%	4.31%	3.33%	GBP/USD	1.27	-0.3%	4.4%	-1.1%	3.0%
Global	China 10Y	2.43%	2.56%	2.69%	2.66%	2.90%	USD/CHF	0.86	2.4%	-5.4%	-1.2%	-6.0%
India	India 10Y	7.14%	7.17%	7.36%	7.18%	7.34%	USD/CNY	7.17	1.0%	-2.0%	0.4%	6.1%
India	India 1Y	7.15%	7.09%	7.14%	6.88%	6.89%	USD/HKD	7.82	0.1%	-0.1%	0.3%	-0.3%
India	India 10Y AAA	7.68%	7.76%	7.78%	7.68%	7.78%	USD/INR	83.04	-0.2%	-0.3%	1.0%	1.4%
India	India 1Y AAA	7.89%	7.91%	7.69%	7.43%	7.77%	USD/CAD	1.34	1.4%	-3.2%	1.9%	1.0%

Source: Bloomberg Equity/Fixed Income Returns/Yields in local currencies. Commodities in USD. Numbers for Fixed Income are Yields as of January 31, 2023.

Glossary:

***US**: United States, **GDP**: Gross Domestic Product, **CY**: Calendar Year, **IT**: Information Technology, **AI**: Artificial Intelligence, **OW**: Overweight, **UW**: Underweight, **PCE**: Personal Consumption Expenditure, **DM**: Developed Markets, **HC**: Hard Currency, **EM:** Emerging Markets, **IG**: Investment Grade, **HY**: High Yield, **TIPS**: Treasury Inflation Protected Securities, **GFCF**: Gross Fixed Capital Formation, **RBI**: Reserve Bank of India, **OMO**: Open Market Operations, **FII**: Foreign Institutional Investors, **BPS**: Basis Points, **INR**: Indian Rupee, **CNY**: Chinese yuan renminbi, **REER**: Real effective exchange rate, **CPI**: Consumer Price Index, **NEER**: Nominal effective exchange rate*

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