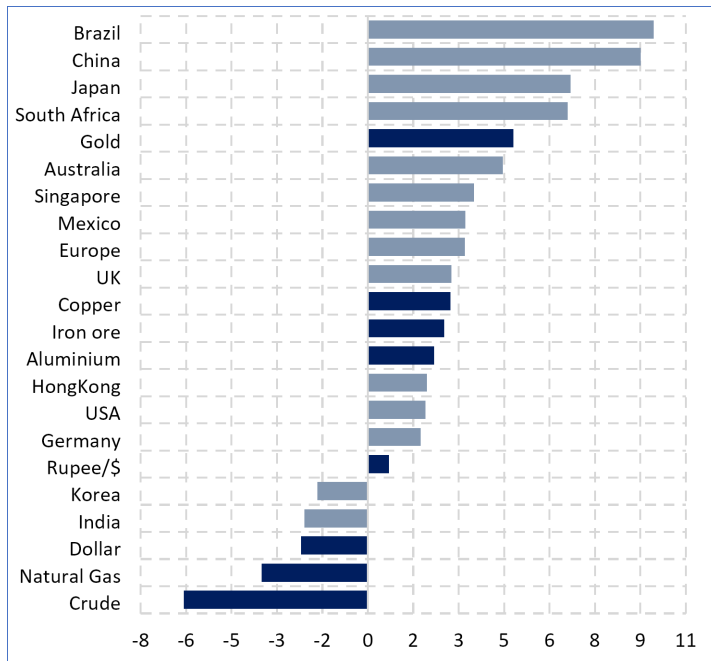


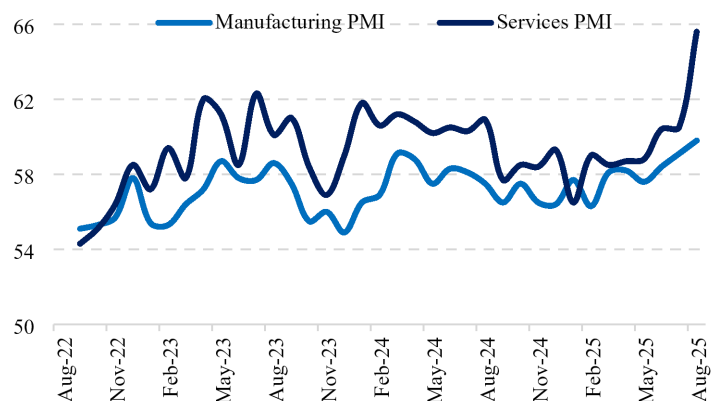
Brazil, China and Japan topped returns in August (% m/m, in USD)



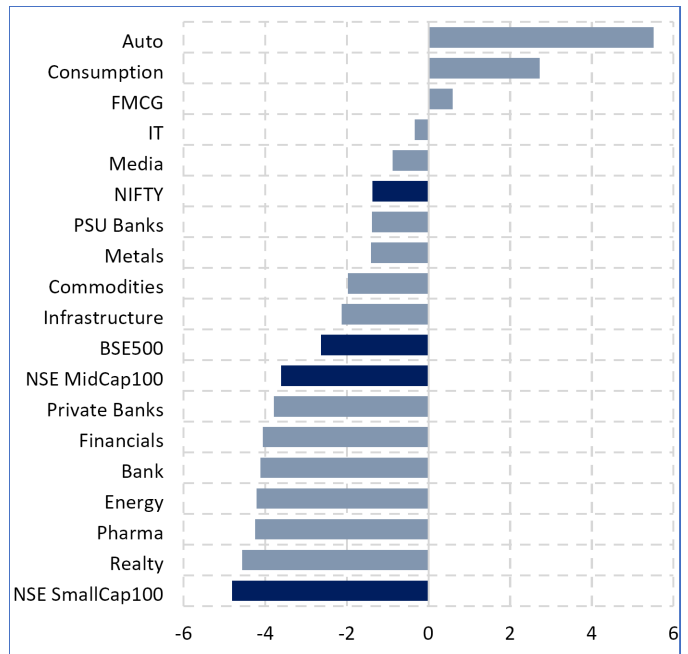
Brazilian equities topped global markets, driven mainly by a risk-on sentiment, post the Jackson Hole (JH) conference. Further, improved liquidity conditions, softer inflation and increased domestic rate cut expectations bolstered Brazilian markets. Chinese markets strengthened on stimulus expectations and Japanese markets closed positive on positive real wages and an expected US tariff-cut on Japanese cars.

Tariff narratives apart, the entire focus of the markets were on the US' Jackson Hole conference. In the run up to Jackson Hole, US macro data continued to hold up, though the labour market remained relatively soft. The IMF revised global growth upwards, alongside China and India, while it revised US growth lower. The Fed was seen in wait-and-watch mode and left rates unchanged and acknowledged some moderation in economic activity. While the US' tariff impositions continued, the US extended its tariff-pause with China for another 90D, till 1st Nov'25. China deflation continued even as it attempted to support its domestic consumption through subsidies. The awaited JH meeting saw the Fed Chair acknowledge the need to shift monetary policy stance and start cutting rates, in a cautious manner. JH also witnessed the Fed tweak its policy framework, calling for moving back to a flexible inflation target. This implies that the Fed would not be too fussy about inflation not sticking to a specific number, but would give it more room to move. The month ended with a US federal appeals court ruling that most of the US' retaliatory tariffs were illegal. The US government has appealed the ruling in the Supreme Court.

Manufacturing PMI pickup, while Services PMI sees a surge



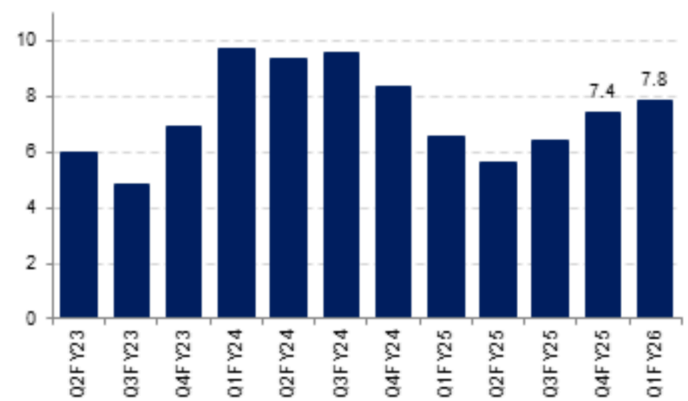
Auto, Consumption, FMCG top U/P in August (% m/m)



NIFTY fell (1.4%) in rupee terms for the month of August. Automobiles, Consumption and FMCG were key outperformers, while Realty, Pharma and Energy were the key sectoral drags on the index. On cap curves, Small caps witnessed sharp corrections, followed by Mid caps. FIIs were net sellers of equity to the tune of \$(4.3)bn, larger than seen in July. FII investment in debt witnessed a pickup to \$1.7bn, from just \$0.1bn in July.

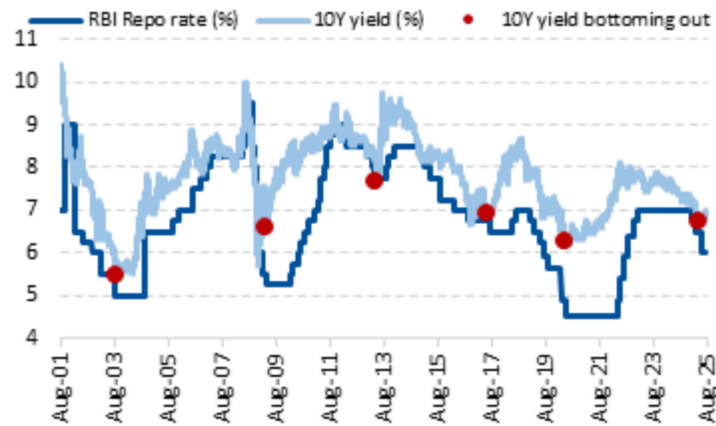
August started with US' 25% tariffs being imposed on India's exports to the US (except smartphones and pharma), with an indication of additional penalties towards India's purchase of Russian energy. Soon after, the US announced the quantum of this penalty, as an extra 25% tariff. Around mid-month, the narrative started shifting towards India's thawing relations with China and the Indian Prime Minister's attending of the SCO summit in Tianjin, China. Mid-month also witnessed the Prime Minister's Independence Day speech, with an outline to new economic/security initiatives, GST overhaul, Rs.1 Tr scheme for first-time job seekers, indigenous semiconductor production etc. The government also announced a complete reform of the GST rate system. Macro data broadly held up and CPI inflation moved well below expectations, The RBI held on to rates, and sharply lowered its inflation forecast, while maintaining its forecasts on growth. The RBI's MPC minutes showed members broadly vigilant of tariff related risks on the economy. The RBI's working group on liquidity recommended continuing with the current weighted average call rate as the target.

Three drivers to the recent surge in India real GDP numbers



India Composite PMI touched a record high in August, on the back of record highs in both manufacturing and Services. New orders rose at a record pace, on an increase in foreign sales growth due to a demand pickup in Asia, Middle East, Europe, and US. Manufacturing strength was on the back of a combination of foreign and domestic demand. Services PMI witnessed exceptionally strong expansion, and firms were reported hiring more staff to meet rising workload. Firms on the whole were reported to be more confident about future activity.

RBI rate cycles and 10Y yields, a framework to keep in mind



The current juncture of the RBI rate easing cycle brings up two questions. Firstly, on the pace of rate transmission and secondly on how market yields have responded to the RBI's previous repo rate cycles.

Recall our commentary from the [June E.M.I.](#), where we detailed how the increasing share of External Benchmark Lending Rate (EBLR) in floating rate loans has greatly improved rate transmission. Measuring this transmission, we notice that the Repo rate changes are seen trickling into changes in Weighted Average Lending Rates (WALR) of banks within a quarter. This is a significant improvement from 3-4Q lags in the last rate cut cycle. Going by this relationship, by end-Sep'25, most of the 100bps of Repo rate cuts should see reflected in the WALR, implying a broad-based drop in bank lending rates. This is because rate transmission is one of the key drivers for a consumption recovery ahead that we detailed in our [June E.M.I.](#)

The next logical step is to analyse how the Repo rate affects market yields, 10Y yields in particular. Analysing data on this, brings us to a very interesting observation. Debt markets appear to start pricing in rate cycles nearly a year ahead of when they take place. They seem to have the ability to read into macro and central bank moves well in advance. Examining the last five RBI Repo rate cut cycles, against the India 10Y yield shows us that the 10Y yield bottoms out well ahead of the next Repo rate hike. The exact time the RBI ends its Repo rate cut cycle, appears to be the time when market yields start its phase of bottoming out. The current global backdrop continues to remain fairly uncertain and is likely to see an impact on domestic GDP growth for FY26. As and when the RBI sees this downside risk to growth, it would be pushed to lower its growth forecasts and deliver probably one more 25bps cut in the Repo rate, before entering an extended pause well into FY26. However, given the uncanny relationship of how market yields seem to pre-empt the Repo rate, one must have a close eye on this very relationship. In other words, India appears to be close to its Repo rate cut cycle, implying limited room for any appreciable fall in yields. However, two events need a close watch. Any sharp drop in global crude prices from current levels, though unlikely, could provide a short window for rate easing. Secondly, any sharp drop in US yields could help India on the sidelines, and help prolong the RBI's rate pause.

Jun'25 quarter GDP growth stood 130bps above market expectations, at 7.8% y/y. There were three inherent drivers: 1) frontloading impact of the tariffs 2) statistical impact of a sharply lower deflator and 3) inherent domestic strength seen more in the services segment. While the first two drivers are real in nature, the effect of the statistical deflator can be adjusted out to arrive at a more realistic growth number. This then places Jun'25 quarter GDP growth more in the range of 6.5-6.8% y/y.

Equity Market Outlook

Valuations

Equity markets witnessed appreciable corrections in August. Alongside some earnings revisions, valuations were seen to moderate during the month, across cap curves. India's 1Y forward price-to-equity valuations for Mid and Small cap appear to be converging, even as they remain well above NIFTY valuations. Valuations still remain well above their long-term averages (LTAs) for all cap curves. We continue to reiterate the need to adopt a balanced asset allocation approach for short-horizon portfolios. Long-term portfolios on the other hand, as always, can make use of equity market volatilities into the months ahead.

Outlook

Our last few monthly E.M.I.s (particularly [June E.M.I.](#)) have stressed on the increased medium-term visibility for consumption in India, over other segments. Early September witnessed the government come out with details on its planned GST-reform framework with a sharp drop in segmental rates across the board. This GST reform, set to begin 22nd Sep'25, would help give consumption yet another boost. In line with our June E.M.I. that listed out eight key drivers for consumption, this GST reform would now be the 9th driver, over the medium-term.

The recently announced GST framework has a simplified 2-slab structure: 5% merit and 18% standard; alongside an additional 40% on demerit goods. These new rates are set to be implemented from end-Sep'25, except for the pan masala, cigarettes, gutka,... items. GST appears to be fully exempt on life and health insurance policies, making it more affordable. Lifesaving drugs, medicines and medical devices/supplies would see rate slashed to 0-5%. This would reduce treatment costs and help increase the access to critical health care. Lower rates seen for agriculture, fertilizers, MSMEs, textiles, renewables, transport, & labour-intensive industries. Household items like consumer appliances, packaged foods, personal care products see appreciable drop in rates. GST rate cuts are also seen for small cars, motorcycles (up to 350cc), with rates dropping to 18% from 28%. Renewable energy devices would see a tax rate cut to 5% from 12% and coal would be taxed now at 18%, from 5% earlier. Further, 40% GST rate has been imposed on sin and super luxury goods, and cigarettes/pan masala..., with delayed implementation for the latter.

GST rate rationalisation exerts pressures on both centre and state tax collections. Given that the Centre would no longer be sharing compensation cess from the next fiscal year, fiscal pressure for the Centre in the medium-term from GST appear manageable. However, one of the key open questions in the mind of the markets are around state finances. For states like Karnataka, Maharashtra, Bihar etc, GST accounts for a large part of their revenues. And for states like Punjab, Odisha, Jharkhand etc, compensation cess accounts for a non-negligible share of their revenues. In simple words, in addition to the ongoing fiscal pressures on states due to elections (read: populist spends), GST related fiscal pressures could add another layer.