Equity Outlook

November saw the Sensex contract by (1.9)%, closing at 26,146. The month saw a fair bit of volatility mostly on account of language from within the Federal Reserve (Fed.), hinting at an increased rate hike possibility. On the domestic side, though the 'Grand Alliance' enjoyed a victory over the NDA in Bihar, the government's pushing for FDI reforms and the consumption impact of the 7th pay commission helped in partly offsetting any weakness. The financial markets saw a net outflow of $(1.7)bn. in November. The rupee saw a depreciation of 2.1% to 66.67, as the dollar strengthened by 3.3% during the month.

Global

November saw a return of volatility in the global markets. The month started with continued positivity on US macro prints with strong vehicle sales, construction and labour activity. These prints, alongside some hawkish notes from within the Fed., increased the probability of a rate hike in December. This gave strength to the dollar and currency weakness across the Emerging Market (EM) space. As we get closer to the Fed.'s December policy date, expected tightening worked as a dominant deterrent for capital flows in November. The month reflected on the consumption led recovery in the Eurozone and saw China unveiling its long awaited 13th five year plan; charting the course for the country's growth into the future. The month was a positive for China, with the IMF including the Yuan into its SDR basket. In the EM space, Brazil saw broad-based macro weakness, while Russia saw extended softness around its consumption. India however saw growth inching up marginally on the back of some government and investment spending.

The weak global backdrop has increased expectations around growth in the developed countries; especially the US. It is from this stand point that the Fed.'s December policy must be seen. Assuming that the Fed. makes no mistake in interpreting US macro strength, a December rate hike, as expected by the markets, would be positive for global growth. Rate action would be reflective of the Fed.'s confidence on US growth and would partly help cushion EM exports as well. Clubbing this with the easing trajectory of the European Central Bank (ECB), this presents the markets with some structural volatility on account of the imminent monetary policy divergence.

Central banks

Like seen last month, the Fed.'s monetary policy continues to be on the watch list of all the central banks. The change in language seen in the Fed.'s October policy has been supported with comments from within the Fed. in November. While the data dependency of the policy continues, the Fed. sees December rate action, as a 'live possibility'. While the Fed. is looking to hike, the ECB is moving in the other direction presenting the markets with structural policy divergence. The central banking space continued to be dominated by pauses, with 11 central banks on hold (U.S, Eurozone, Japan, Britain, Australia, Mexico, Russia, Brazil, Thailand, Malaysia, Kenya). The space also saw four central banks ease (China, Korea, Indonesia, Nigeria) and Ghana hike.

Domestic

November continued to remain positive on the macro front. Retail and wholesale inflation numbers saw an uptick, but were broadly reflective of the bottoming out base effects in the series. IIP growth saw a drop to more sustainable levels and the GDP numbers for Q2FY16 saw a pickup in growth. GDP growth reflects a nascent recovery on the back of an increase in the quality of government spends, services growth and a pick up in capital formation. The drop in input inflation is broadly reflecting in the new GDP series. This is visible in the form of the increase seen in real GDP growth, at a time of weak nominal headline numbers. The political backdrop in November witnessed the 'Grand Alliance' seeing a landslide victory over the NDA. Reform efforts by the government during the month, however, helped offset the muted outlook on the elections. The month saw FDI liberalisation in 15 sectors, charging the policy space. Also seen was the 7th Pay Commission's recommendations of a sizeable increase that would help support India's consumption leg, during this stage of growth.

Flows

Europe continues to see inflows into its equity markets and form a large share of the inflows into developed markets. Japan saw marginal inflows, while the US has seen a marginal increase in an already large level of outflows. With increased Fed. rate expectations, the EM space has seen an increase in outflows across the board, with China taking the largest share. Indian equity markets saw an outflow of $(1.1)bn., while the debt markets saw a marginal outflow of $0.6)bn. YTD inflows into these equity and debt markets remain positive at $3.2bn and $8.2bn. respectively.

Outlook

RBI continues to be supportive of growth while the Government's commitment to spur the infrastructure investment cycle is already reflecting in the current fiscal spends. The new Govt. has been laying the foundations for the road to sustainable growth through broader reforms & efficient administration. We have already entered the next business cycle and the soft commodity prices, especially oil, is visibly translating into fiscal comfort and business confidence on margins. While one maybe concerned about soft earnings growth seen, a detailed analysis shows corporate earnings (ex commodities) improving at a healthy pace. Better growth will gradually lead to a shift in the saving pattern of Indian households from physical to financial with a sharp bias towards equity. Mutual funds are well positioned to absorb this incremental shift. Corporate earnings are set to enter a positive growth trajectory driven by the domestic recovery. Our funds are very well positioned to reap these benefits.

Every bull market is interspersed with both time and value corrections while reasons could be varied. With the twin deficits well contained, inflation well under control, bottomed out growth, a relatively stable currency and an extremely strong political mandate, every point of volatility would be an opportunity to buy India. The recent correction in the markets underlines the same. With every turn of the markets, the India-differentiation story gathers more interest, momentum and conviction in that order. This would get louder in the coming quarters and a stable rupee would give comfort to the inflows. We continue to remain positive on our equity markets.

Equity Desk