May saw the Sensex rise by 0.5% to 35,322. Trump trade wars with China and the brief political turmoil in Italy were the highlights of May globally. On the domestic front, JD(S) coalition with the Congress in Karnataka, rising core inflation and a surprise positive print in GDP growth were the were the key domestic notables. The markets saw a net outflow of $4.1bn. in May. The rupee saw a depreciation of 1.1% to 67.4 to the dollar as the dollar index (DXY) strengthened by 2.3% during the month.

**Global**

The global markets took a beating in May with significant volatility emerging from politics, oil and trade war narratives. US markets however closed positive on the back of macro strength. The month started with noise from the Trump administration on wanting to exit the Iran nuclear deal. This sent crude prices higher on supply concerns that remained for most part of the month. Rising crude set the backdrop for rising global bond yields. Like the earlier months, this month was also dominated by Trump-talk on tariffs leading to an on-off scenario for the markets on trade wars. Trump though struck a conciliatory tone at the start of talks with China but at the end of the first round said that he was not satisfied with the China-trade talks. Topping it all up, ahead of his second round of talks with China in June, Trump announced that he planned to proceed with imposing tariffs of $50bn on China, curbs on investment in sensitive technologies and setting limits to China visa applications. The US trade war narrative was not limited to China alone, Trump also proposed a national security probe on US vehicle imports with new tariffs on auto and auto-ancillary imports from over the world including Germany. The US administration also let the exemption of its earlier aluminium and steel tariffs on Canada, Mexico and the European Union expire. This brought about retaliatory tariff talk from all the three countries. The month ended with significant market turmoil on a coalition break-down in Italy that quickly normalised with a Government being formed soon after.

**Central banks**

Central bank activity continued to focus on the Fed. and the ECB. The Fed minutes showed an inflation tolerant Central Bank amidst positive and growing macros. The ECB minutes on the other hand acknowledged growth moderation, indicating a possible scenario of this weakening further. The weakening macro outlook for the Eurozone and the sudden political volatility around Italy led to a sharp drop in the Euro that fed into a much stronger dollar index. Interestingly, EM Central Banks saw a string of hikes, all directed at their currencies. Argentina, Turkey and Indonesia are at various stages of depreciation-tolerance in their currencies. June is a packed month with the Fed., ECB, BoJ and BoE all coming out with their policies. Central bank focus in June would also fall on India. The increase in retail inflation and the comments of the RBI Deputy Governor in its last minutes all appear to culminate in a market expectation of hawkish language and varying market probabilities of rate hikes in its June policy.

**Domestic**

The Indian equity markets remained positive in the month of. Macro prints during the month were mixed. Industrial production numbers saw weakness driven by a drop in capital goods and infrastructure. However, PMI numbers remain positive and appear to cut out the volatility that the industrial production numbers present us with. Retail inflation was higher than consensus with a 30bps rise in core inflation. While transport inflation has moved the headline y/y numbers the most, inflation momentum appears to have increased across the board. This inflation concern, geo-political and crude price risks kept Indian bond yields elevated during May. India saw strong headline growth during the month, but the internals need more strength. GVA growth stood in line with consensus, but GDP growth stood 40bps above consensus. Growth was driven by an increase in Government spending and a continued surge in capital formation. The month witnessed Karnataka state elections where BJP emerged as the single largest party, but could not form a Government as they fell short of majority by 8 votes. The JD(S) and the Congress soon formed a post-poll alliance and formed a coalition. Further on by-elections the BJP was able to win only 1 seat of 11, with the rest 10 going to the Congress.

**Flows**

May saw continued inflows in global equities. However, long-only funds saw sharp outflows which was made up by more than commensurate inflows into ETFs. While the EM pack as a whole saw outflows, inflows were seen in specific markets like Brazil and China. As expected, the DM space saw a sharp pickup in equity inflows with the bulk of the flow moving into the US and out of Europe and Japan in that order. In India, May saw continued outflows that continued from the month of April to the tune of $2.6bn in debt and $1.4bn in equity. With the twin deficits relatively well contained compared to its peers the structural differentiation story continues to hold for India.

**Outlook**

The Government's firm commitment to spur the infrastructure investment cycle is already reflecting in improved execution on the ground. Focus on rural incomes and spend is also helping broad-basing growth and serves as a long term driver of the consumption story. The stress in the banking system has seen significant and targeted addressing, as expected, with recognition, provision of bad loans, resolution and subsequent capitalization. The Govt. has been laying the foundations for the road to sustainable growth through broader reforms & efficient administration. GST transition impact though real in few quarters, we believe is a short term phenomenon and hence investors are advised to see it through patiently and have faith in the strong India growth story. Growth will be spurred by strong infra related spend, urban consumption, rising rural incomes and improved demand going forward

with the bottom behind us clearly. The uptrend in corporate results and earnings trend has seen gathering steam in the second half of FY18.

Softer than historic inflation and 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 moving into a double digit growth trajectory driven by the domestic recovery, as we exit this fiscal. Our funds are very well positioned to reap these benefits. The FED. is likely to move ahead gradually, keeping in mind not to pull down economic growth that has just seen some momentum. FY18 was a year of the fiscal with most governments acknowledging the need to create demand through fiscal spending. India was not behind in this move and continues to remain prudent in such deficit spending. With the twin deficits reasonably contained, inflation well under control, bottomed out growth, a relatively stable currency and an extremely strong political mandate, India stands taller than the rest. With the ongoing correction - more severe in small and midcaps - valuations are getting more comfortable than before. Domestic liquidity continues to be strong and we would keep faith in the corporate earnings recovery and look ahead into forward valuations of FY19 and beyond. State election outcomes could create some short term weakness in markets as also the noises on the trade war front. Near term Indian markets may undergo a time consolidation or be range bound, which could be a good time to get invested in a disciplined manner. Every bull market is interspersed with both time and value corrections while reasons could be varied. Every point of volatility would be an opportunity to buy India. 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 fairly stable rupee would give comfort to the inflows. We continue to remain positive on our equity markets with a medium to long term outlook.