January 2019 saw the Sensex grow marginally by 0.5% to 36,257. An temporary end to the US Govt. partial shutdown, IMF's growth downgrade and positivity heard around US-China trade talks were the highlights of the month globally. On the domestic front, continued tweaks to the GST framework and RBI's relaxation of rules for external borrowing by companies were the key domestic notables. The markets saw a net outflow of $0.4bn. in January. The Rupee saw a depreciation of 1.9% to 71.1 to the dollar, while the DXY weakened 0.6% during the month.

Global

2019 began with concerns over IMF slashing its growth forecast by 20bps to 3.5%. A slowing Chinese economy, soft demand in Europe and recent financial market turmoil were the reasons it attributed to the move. IMF left US and China growth estimates unchanged while pegging India to grow at 7.3% for FY19. Most of January witnessed political tensions around the partial shutdown in the US, that started during the last week of December. After a few unsuccessful attempts to arrive at a middle ground, the 35 day shutdown ended with bills passed to fund US government for three weeks ending February 15th. From where we stand today, the risk of another US shutdown cannot be ruled out. On the US-China trade war front, the narrative remained largely positive with China resuming imports of US agricultural and energy commodities. The month saw China growth ease to its slowest pace in three decades, bringing to focus the measures being taken on both the fiscal and monetary front to support the economy. Alongside pumping resources into new infra projects, the government announced tax cuts for small companies and measures to boost automobile sales. The PBoC also deployed monetary stimulus by cutting its RRR for the fifth time in January to incentivize lending. Over to the UK, the uncertainty around Brexit continued with May's Brexit deal crushed by an overwhelming majority in the parliament.

Central banks

Central banks around the world were on guard as they tweaked their language and guidance to counter the softness in global growth. Jerome Powell's hawkish tone post the December policy, saw a shift in January. His commentary that the Fed would be 'patient' clubbed with a slew of in-line commentary from the Fed members on a wait and watch mode gave markets the sense of a pause in the near term on rates; alongside a possible drop in its rate forecast for the year. The Fed policy witnessed an expected pause from the Fed with language indicating dovishness on both rates and it's balance sheet. More important and surprising was the Fed's commentary on its Balance Sheet. Commentary indicated that the Fed's Balance Sheet rundown may end sooner than what the Fed and the markets had expected. The reasoning behind the soft commentary from the Fed on rates was global growth softness, financial market volatility and muted inflation pressures. In addition, the recent US market shutdown and data availability also probably worked on the sidelines. The ECB policy also held on to its rates. However, on commentary, Draghi acknowledged that Eurozone growth was likely to be weaker than earlier estimated due to factors ranging from geopolitical to protectionism. Markets interpreted the ECB's policy language to raise the probability of rate normalisation well into 2020. Further, he mentioned that if the economic situation were to "go very wrong" they could still resume other instruments in their tool box. This is seen as an indication of resuming its bond buying QE program that ended on Dec'18.

Domestic

On the domestic front, macro prints remained mixed. Retail inflation continued to ease with a drop in wholesale numbers as well. Industrial production on the other hand saw a contraction largely due to unfavourable base effects. January also saw policy tweaks that could work in favour of the current government. Tweaks were also made to GST that increased the limit for annual turnover of the compensation scheme to Rs.15mn from Rs.10mn earlier. The exemption limit for GST registration was also increased. The RBI extended the deadline to allow banks to set aside provisions to restructure MSME loans in default, to 2020. Moving into February, the budget would see a number of initiatives for those in the bottom of the pyramid, all the way up to the middle class. This would bring about the well needed relief to a number of distressed segments of the population, experiencing farm distress.

Flows

2019 has seen a sharp shift in language and stance from the Fed. This is likely to reflect clearly in the Fed's March policy and projections. While the Fed's December policy saw two rate hike forecasts for 2019, the markets expect one or less for the year. This, clubbed with positive news flows on the US-China trade spat, witnessed a sharp increase in inflows to the DMs. The EMs broadly saw outflows of nearly half that quantum. In India, equity witnessed marginal outflows to the tune of $0.1bn, alongside debt outflows of $0.4bn. The global DM central bank backdrop has now become much softer than before.. With muted commodity moves, this could translate into a more stable and range-bound rupee; giving impetus to a renewed differentiation.

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 Govt. has been laying the foundations for the road to sustainable growth through broader reforms & efficient administration. 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 is seen gathering steam over the last 12 months.

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..

In the medium term, India, with its twin deficits reasonably managed, lower base levels of inflation, improving corporate growth, stands taller than the rest of the EM pack.

With the ongoing correction in the broad markets - more severe in small and midcaps - valuations are getting more comfortable than before with PE multiples tending to long term averages and lower. Domestic liquidity continues to be reasonably strong and we would keep faith in the corporate earnings recovery and look ahead into forward valuations of FY20 and beyond. The run up to the General elections and 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 stable rupee would give comfort to the inflows. We continue to remain positive on our equity markets with a medium to long term outlook.