MONTHLY UPDATE
SEPTEMBER 2021

20 YEARS
Protecting India with Pride

HDFC Life
Sar utha ke jiyo!

Sep, 2021

"Chains of habit are too light to be felt until they are too heavy to be broken."

- *Warren Buffet*

Equity markets

Indices	30th Sep 2021	31st Aug 2021	1 Month Return (%)	1 Year Return (%)
BSE Sensex	59,126	57,552	2.7%	55%
S&P CNX Nifty	17,618	17,132	2.8%	57%
BSE 100	17,881	17,375	2.9%	57%
BSE Mid Cap	25,253	23,853	5.9%	72%
BSE Small Cap	28,082	26,920	4.3%	89%

Source: Bloomberg

During Sep'21, domestic equity indices had another strong performance - large cap indices were up ~3% while the mid and small cap indices outperformed with BSE Mid Cap and Small Cap Index up 6%/4% respectively. On a 1-year basis, the mid and small cap index have outperformed the large cap indices. Over the past one year, Sensex and Nifty were up 55% and 57% respectively while BSE Mid cap and Small cap index were up 72% and 89% respectively.

During Sep'21, performance across the sector indices was mixed. The performance ranged from -2% to +33%. Realty and Consumer Durables sector gained the most; up 33% and 11% respectively while Healthcare and Metals sector fell the most; down 2% each respectively. On a 1-year basis, Realty sector is the best performing sector gaining 146% followed by Metals and Utilities sector respectively. FMCG followed by Auto are the bottom two sectors; up 34% each respectively.

The yield of benchmark 10-year G-sec moved to 6.22% at the end of Sep'21 from 6.21% at the end of Aug'21.

Most major global equity indices were down during the month, except Nikkei which gained the most, up ~5% during the month while Shanghai Index was flat MoM. On a 1 year basis, CAC 40 has gained the most; up 36%.

Commodities (USD)	1 Month Return (%)	One Year Return (%)
Gold	-3%	-7%
Silver	-7%	-5%
Crude Oil	10%	87%
Copper	-6%	35%
Primary Aluminum	5%	64%
Lead	-8%	17%
Nickel	-8%	24%
Tin	2%	101%
Zinc	-1%	25%

Source: Bloomberg

Most major commodities fell during Sep'21 except Crude Oil, Aluminum and Tin. Crude Oil rose the most, up 10% during the month.

On a YoY basis, all the major commodities except gold and silver have posted YoY gains. Tin has appreciated the most.

Macro Economic Data

Indicators	Jun-21	Jul-21	Aug-21	Sep-21	Comments
IIP (YoY, %)	13.6%	11.5%			Industrial output grew 11.5% yoy in Jul'21 vs. 13.6% yoy increase in Jun'21. The recovery is broad based as Mining, manufacturing and electricity recorded growth of 19.5%, 10.5% and 11.1%, respectively.
Core Sector (YoY, %)	9.3%	9.9%	11.6%		Core sector output grew 11.6% in Aug'21, following 9.9% growth in Jul'21. The recovery was driven by coal output (up 20.6% yoy), natural gas output (20.6% yoy) and electricity generation (15.3% yoy). However, output of crude oil and fertiliser declined by 2.3% and 3.1% respectively.
RBI monetary policy (Repo Rate) (%)	4.00	4.00	4.00	4.00	RBI kept repo rate unchanged at 4% as of Sep'21.
CPI inflation (%)	6.26%	5.59%	5.30%		CPI inflation marginally moderated to 5.3% in Aug'21 from 5.6% in Jul'21 led by the fall in food inflation from 3.8% in Aug'21 to 4.5% in Jul'21
Trade Deficit ($, bn)	-9.4	-11.0	-13.8	-22.9	In Sep'21, exports grew by 21.3% to $33.4bn, while imports grew by 84.7% to $56.4bn, as a result trade deficit widened to $22.9bn in Sep'21 vs. $13.8bn in Aug'21.
GST Collection ($, bn)	928	1164	1120	1170	Total gross GST revenue collections in Sep'21 stood at Rs. 1,170bn, following Rs. 1,120bn collection in Jul'21.
FII Flows-Equity ($, bn)	2.36	-1.51	0.28	1.79	On equity side, FPIs purchased $1.79bn in Sep'21, following an inflow of $0.28bn in Aug'21. On debt side, FII bought $1.74bn in Sep'21, following an inflow of $1.63bn in Aug'21.
FII Flows-Debt ($, bn)	-0.66	-0.11	1.63	1.74	
Exchange Rate (INR/USD)	74.35	74.39	73.15	74.25	Indian Rupee depreciated by 1.5% during Sep'21, as it closed at 74.25 in the end of Sep'21 from 73.15 at the end of Aug'21 per dollar.
GDP (%)	20.1%				Real GDP grew by 20.1% in Q1 FY22 vs. 1.6% growth in Q4 FY21 led by the sharp jump in investment (56.7% in Q1 FY22 vs. 13.8% Q4 FY21)and HH consumption (19.3% in Q1 FY22 vs. 2.7% in Q1 FY21)

Outlook

Markets continued their upward momentum in September, reaching a new all-time high. Indian equities' performance is in sharp divergence with other Emerging markets (which saw correction). In fact, in H1FY22, Nifty is up ~20% (vs. EM being flat) and is one of the best performing equity markets across the globe. Nonetheless, while Nifty was relatively rangebound in the quarter there were significant developments on both global and domestic front.

First on the global front, the US Fed indicated that it would embark on tapering soon. Infact, they plan to end their asset purchases by mid next year. They believe that "substantial progress" on inflation has already been achieved and labor markets too are well on the path of recovery. To that extent, monetary accommodation now seems to be ending across the globe. Unlike 2013, we don't think this likely to have material impact on Indian economy as domestic liquidity conditions are very benign and unlike 2013 our macro-economic vulnerabilities (CAD, inflation) are much lower this time around. While, this may be temporarily negative for risk sentiments, it's unlikely to derail the economic recovery.

Second, on the global front China's Evergrande crisis made the headlines. Evergrande is China's largest real estate developer with USD300bn of liabilities. Hence, its default is certainly big news and sections of international media are classifying this as China's Lehman moment. This however may not be the case as the Chinese policymakers are considered to be pragmatic and are expected to ringfence the fallout of the impending default, thus preventing it from turning into a global crisis. Nonetheless, Chinese growth is likely to slow down sharply, which in turn could weigh on global growth, given China's size.

On the domestic front, economic recovery continues post the second wave. Some of the high frequency datapoints like exports, non-oil and gold imports, electricity generation, e-way bills are registering mid to high teens growth on 2yr CAGR basis. Even the data on real estate in top 7 cities suggests improved momentum. This is very encouraging and clearly suggests that economic recovery is broadening. However, auto sales still remain weak with passenger vehicles plagued with chip shortages and two wheelers hurt by weak demand.

Apart from, easy domestic liquidity conditions, improving growth government capex spending too seems to be going strong. Both central and state government capex spending are running at 25-30%+ on 12 month moving average basis. This should result in better jobs and also help revive consumption. However, transfers by government to rural India have moderated significantly this year. This may not necessarily be unjust given that pandemic is now behind and to that extent spending requirement in rural India is lower.

With regards to markets, they continue to remain strong, with a flurry of IPOs lined up. However, India's valuations remain high on absolute basis - 22x 1Yr forward PE (highest in last two decades). So is our valuation premium to EM at 70% (vs. long term average of 40%). In such a scenario, the tolerance for earnings disappointment is quite low. Hence, high valuations along with global liquidity tightening, moderating global growth warrants caution in the near term. However, medium to long term growth story remains intact.

Fixed Income Market

Fixed Income Market Review –

Bond yields eased during the initial part of the month, on expectations of lower than expected inflation. The softer inflation expectations also led to the markets pricing in a longer period for RBI maintaining an 'accommodative' policy stance. Rising expectations on inclusion of our sovereign bonds in global bond indices added to the positive sentiments. Yields, however, rose towards the end of the month on higher commodity prices as well as the outcome from the US FOMC meeting, where the committee indicated that the Fed would start tapering its massive bond purchases in the coming months. During the month, RBI purchased bonds including the liquid benchmark papers, at lower prices which was seen as an indicator of RBI's unwillingness to manage the benchmark rates any more. During the month RBI conducted multiple duration Variable Reverse Rate Repos (VRRR) ranging from 3-14 days to absorb the excess liquidity in the system. The cut-offs for these VRRRs came much higher than the prevailing short term rates. The cut-off for the 7 day VRRR at the end of the month, came in at the highest possible rate of 3.99% just shy of the current Repo rate at 4%, again indicating RBI's tolerance for higher yields.

The new 10yr benchmark bond closed flat at 6.22% from its previous close after touching a low of 6.12% during the month. The 10yr UST yield rose sharply to 1.50% from its previous close of 1.32% and Brent Crude Oil prices too rose to close at USD 78.6 per barrel compared to its previous close of USD 71.6 per barrel.

Among data releases, India's CPI inflation cooled down to 5.3% in Aug-21 from its previous reading of 5.6% for the month of July-21 on account of a favorable base effect. Food Inflation stood at 3.80% as compared to 4.46% in the previous month. Core inflation (CPI Ex-Food Ex-Fuel) moderated to 5.8% from the previous month's print of 6%. Headline WPI inflation came marginally higher at 11.4% YoY in Aug-21 from 11.2% YoY in July-21.

India's trade deficit in September came at an all time high of $22.94 bn as gold imports jumped to $5.11bn. Among other economic data, IIP growth for July 2021 printed at 11.5% as against the revised reading of 13.6% in June 2021 as gradual waning of favorable statistical base led to moderation. Goods and Services Tax (GST) revenue collection for September came at Rs 1,17,000 cr. Gross GST collections in 1HFY22 stood at Rs6.8 tn—12.6% higher than 1HFY20 (50.1% higher than 1HFY21). India's Nikkei Markit Manufacturing PMI rose to 53.7 in Sep 2021, against 52.3 in the previous month, and the Services PMI softened to 55.2 in Sep of 2021 from 56.7 in the previous month. Composite PMI also remained flattish at 55.3 in Sep vs 55.4 in the previous month.

Market Outlook –

Recent data releases have been pointing to a return to pre-Covid levels of economic activity, as most lockdown restrictions are progressively being eased. As the economy improves, RBI is expected to roll-back the accommodative policy measures. Rising inflation concerns due to high crude oil prices along with recovering growth, is likely to add some urgency to the normalization process. The other key concern for the markets has been the supply of GSecs. During the second half, the weekly supply of bonds has reduced marginally, though any reduction of RBI's buying support erodes the benefit of the lower borrowing amounts.

Globally, the US Fed is likely to begin tapering its bond purchases as early as its next meeting in November. Moreover, the rising commodity prices and a rise in inflation is likely to push US yields higher, adding to pressure for a rise in EM bond yields.

Domestic bond yields are expected to harden in the coming months, though RBI may still be able to moderate the pace of hardening. However, any positive development on the global bond index inclusion is likely to cap a rise in yields.

At the monetary policy meeting, in October, the MPC expectedly kept the key rates unchanged and reiterated its accommodative stance. RBI increased its quantum of variable rate reverse repo (VRRR) of 14-day tenor to Rs6 tn by December in a staggered manner from the current Rs 4 tn. Despite this move, RBI assured that liquidity under the daily fixed rate reverse repo would be supportive of growth.

The governor also stated that “need for GSAPs at this juncture does not arise” thereby withdrawing any explicit support RBI had in order to keep rising yields in check.

Finally, the governor reiterated “this process has to be gradual, calibrated and non-disruptive, while remaining supportive of the economic recovery”.