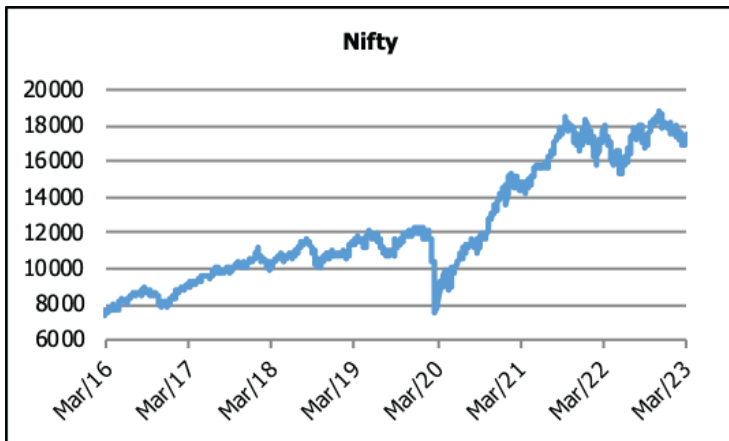




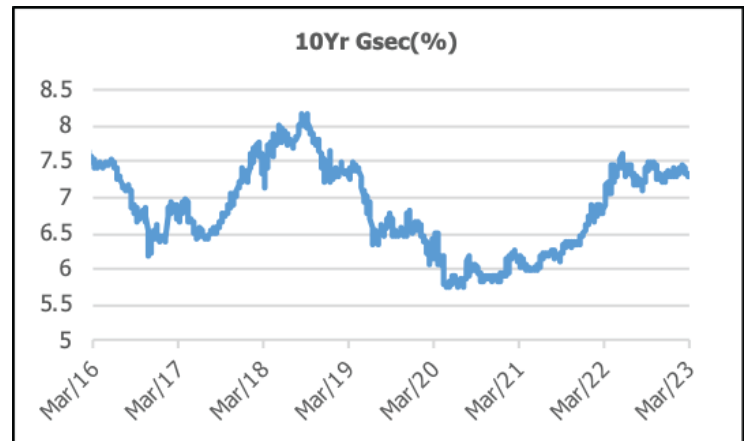
Market Outlook

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Market Update



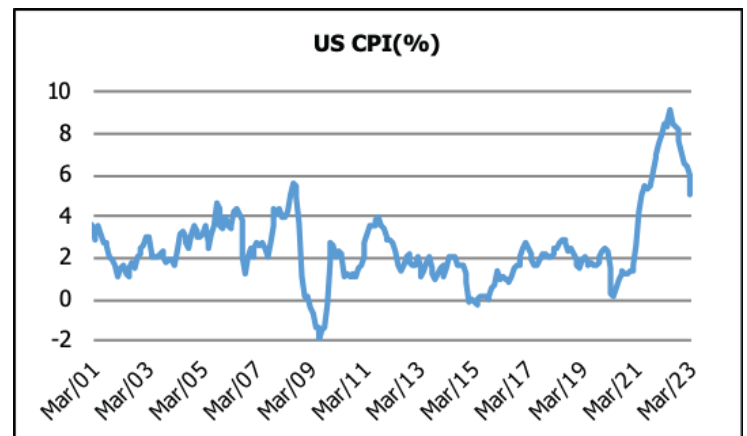
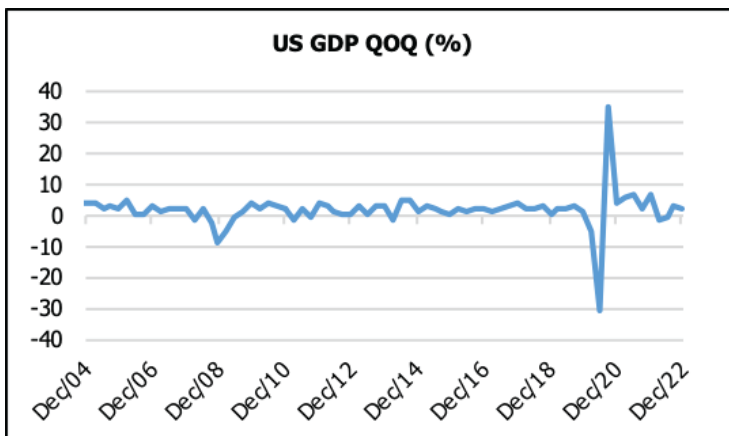
H2 FY23 Nifty returns = 1.55%

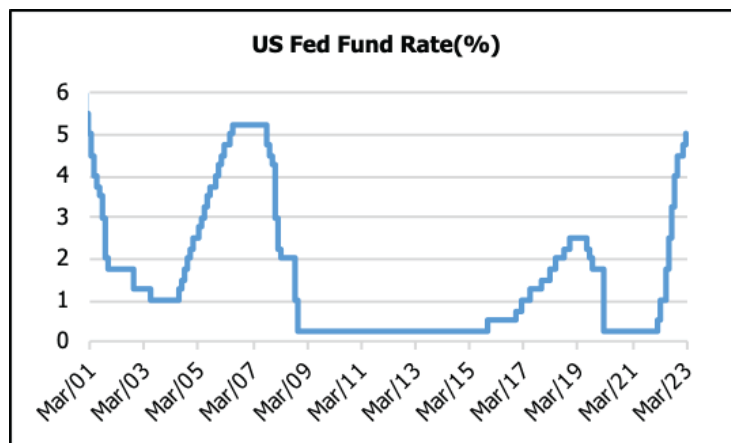
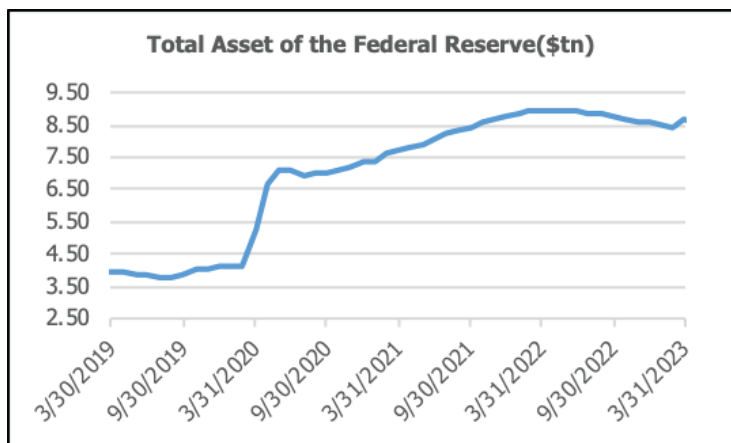


H2 FY23 Change in 10-yr GSec yield = -0.09 bps

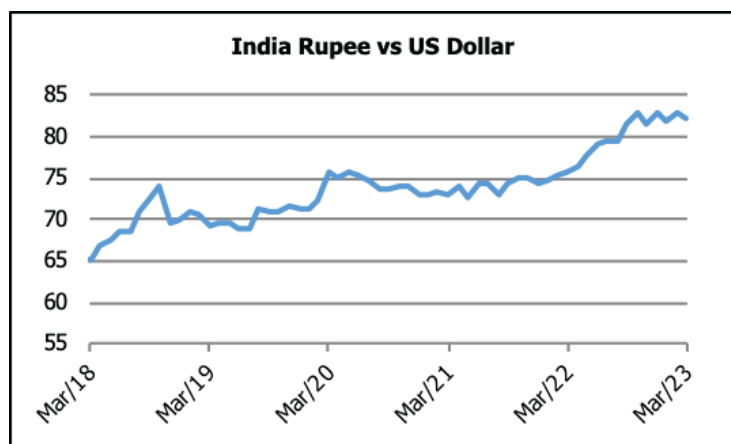
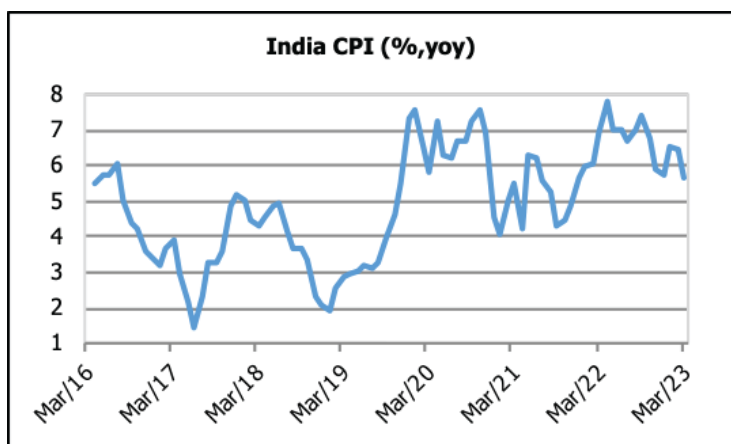
Key Developments

Over the course of the second half of FY23, the world put behind most of the woes due to the pandemic. The primary challenges, stemmed primarily from the continuing war in Ukraine. The US GDP grew by 2.6%YoY in 4Q2022 vs. 3.2% in the previous quarter with GDP mainly supported by private consumption and inventory investment but partially offset by decline in housing investment. The Euro area GDP grew by 1.9%YoY in 4Q2022 vs. 2.4% in the previous quarter. The Eurozone, which has borne the maximum brunt of the war, managed to avert a recession so far as the warmer than expected winter helped avoid a worst-case outcome. The recent fall in gas prices also bodes well for easing the energy crisis. The ECB's baseline projection for growth in 2023 is at 1.00%. The Chinese economy rebounded in 2HFY23 supported primarily due to reopening of the economy, after a period of stringent covid lockdown, under the zero covid strategy. GDP for 1Q2023 grew by 4.5%YoY up from 2.9% in the previous quarter. China has set a modest GDP target of 5% growth for 2023.

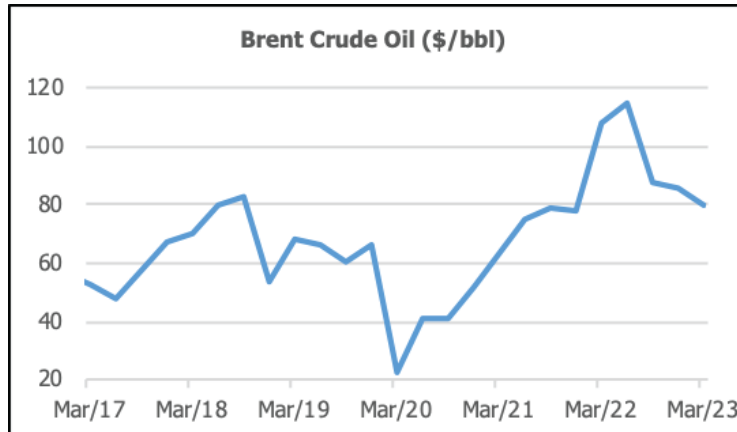
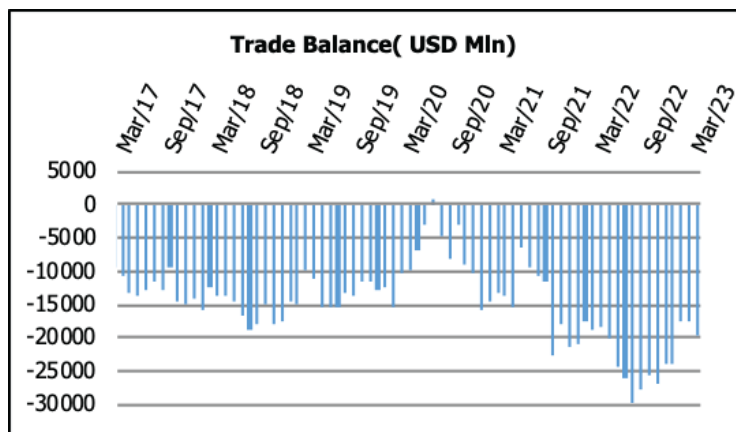




- ▶ The US CPI inflation was largely on a moderating trend in 2HFY23 declining from 8.2% in Sep'22 to 5% in Mar'23. In the same period US core CPI inflation moderated from 6.6% in Sep'22 to 5.6% in Mar'23. The main reason for the fall has been fall in crude and commodity prices. However, inflation still remains elevated and far above the Fed's target of 2%.
- ▶ The Fed continued raising rates aggressively, to combat the high inflation, taking cumulative tightening in the cycle to 475 bps, by the end of March. The Fed has continued with quantitative tightening. The Fed has shrunk its balance sheet by US\$0.4tn in the past six months (slower than announced). However, the emergency lending by the Fed after the regional banking crisis off-set some of the tightening of the previous months.
- ▶ India CPI inflation was also on a moderating trend in 2HFY23, moderating from 7.4% in Sep'22 to 5.7% in March'23. The moderation in inflation was largely because of lower food inflation and favorable base effects.

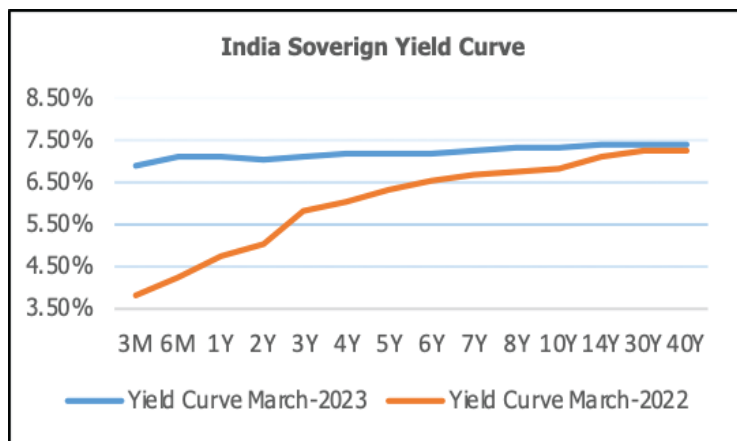
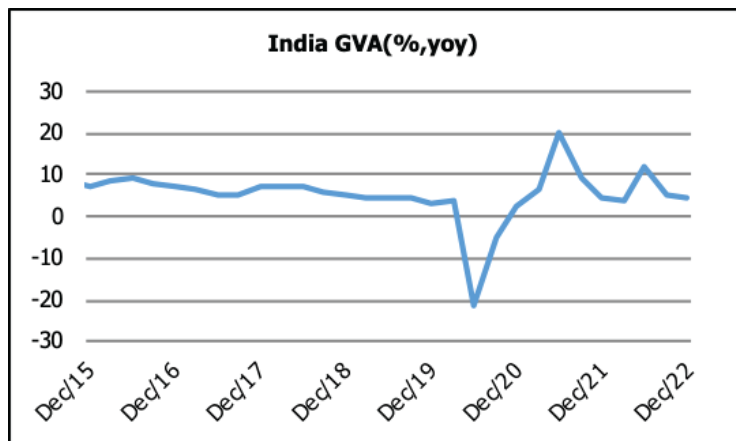


- ▶ The INR came under depreciation pressure between Oct'22 - Dec'22 amid concerns over elevated crude oil prices, widening trade deficit, FPI outflows and falling FX reserves. Sustained rate hikes by the US Federal Reserve and the strengthening US Dollar also added to the depreciation pressure on the INR. However, the depreciation pressure eased in Jan- Mar as the trade deficit moderated, the services exports rose and the USD softened. USD - INR averaged ~82.2 in 2HFY23 vs. 78.6 in 1HFY23 depreciating by ~ 4.7%.
- ▶ India's trade deficit has moderated from an average of ~US\$23.5bn in 1HFY24 to ~US\$21bn in 2HFY23. While exports have moderated, there has been a corresponding dip in non-oil, non- gold imports as the import intensity of India's exports is relatively high. Moderation in crude oil prices and higher gold prices (which pulled down gold demand) have also supported a lower trade deficit. The services surplus which averaged ~US\$10.4bn in 1HFY23 has risen to US\$13.6bn in 2HFY23. This has aided a moderation in the CAD. The higher services surplus may be attributed to healthy software exports and strong growth in business services aided by rise in offshoring to India in the post-covid era. Remittances supported by favorable crude oil prices are also supporting a moderation in CAD. The CAD stood at 2.9% of GDP in 1HFY23 and is likely to come in at ~2% of GDP in FY23
- ▶ India's GVA in 3QFY23 moderated to 4.6% from an average of ~8.8% in 1HFY23 mainly on account of a high base. Core



GVA (excluding agriculture and government spending) stood at 5.4% suggesting relatively resilient underlying growth. On a 3-year CAGR basis, all sectors were above pre-pandemic levels with sustained recovery in contact-intensive services.

- During 2HFY23, India 10yr benchmark bond yields have been largely rangebound, but the short end yields rose reacting to tighter liquidity conditions and rate hikes by RBI. During Q4 FY23 the 40 year GOI bond witnessed heavy buying by insurance companies due to change in taxation for insurance products leading to flattening of the yield curve. The spread between 10 year and 40 year stood at near parity during the last few days of the financial year.
- The 10-year AAA Corp bond spread widened by 10 bp in 2HF FY23 owing to lack of demand.
- Indian equity markets were largely range bound in 2HFY23. FPI selling of US\$5.1bn was more than offset by DII buying of ~US\$13.4bn. Nifty 50 was up by 1.55% and BSE Sensex was up by 2.7%. Broader markets underperformed large cap indices with Nifty Midcap 100 index falling by 2.06%. A more balanced budget, robust domestic flows and better than expected earnings were the main drivers for the outperformance of large cap indices.



Peering ahead

- Going forward, the global growth momentum is expected to ease further as the impact of rate hikes starts to kick in. The US Fed projects a median real GDP growth at 0.4% for CY 2023 and 1.2% for CY 2024. Meanwhile, compared to the US, the extent of the rate hikes in India, at 250 bps, have been far more modest. The RBI projects India's economy to grow 6.4% for FY24, slightly lower than the 7.0% expected for FY23. Given the global linkages in terms of trade and fund-flows, we will not be immune to the impending slowdown in the US and in the Eurozone and the risks to the future projections seem biased towards the downside, even as the large domestic demand provides strong support. The moderation in growth outlook is expected to have a similar impact on the corporate revenue and earnings forecasts. The re-assessment of future earnings trajectory could increase volatility in the near term. In this overall context, valuations at ~18.0x FY24 earnings are largely in line with longer term averages, making us cautious in the short term. Nonetheless, medium term outlook remains quite strong and hence any volatility could provide an attractive opportunity to invest for the long term.

➤ The trend of inflation, in both the developed as well as the emerging economies has been on the downward path, though still at levels higher than the respective targets for the central banks. Consequently, the central banks are seen to be in the last stages of the tightening cycle. Current indications from the central banks show that rates may be steady at the peak levels for an extended period, till the inflation trend is seen to sustainably headed to the target levels. However, any un-intended consequences of the tight rates, like the series of regional bank failures in the US, or a sharp growth contraction, may hasten the onset of an easier policy.

➤ Interest rates in India, too, are expected to be in hold for an extended period, though the RBI forecast for average inflation in FY24 at 5.2%, is within its target range. RBI, though, has mentioned that the objective of the monetary policy is guide inflation to 4%. Again, similar to the global outlook, an earlier change in policy stance could be triggered by a surprise in the growth / inflation trajectory, or some un-intended consequences. Meanwhile, at the probable peak of interest rates, interest accruals from fixed income investments are attractive. On a longer term horizon, the expected turn in the economic cycle is likely to lead to lower interest rates and bond yields, thereby adding to the fixed income returns in this period.



Sar utha ke jyo!