HDFC Bank – Research Presentation

February 2024

Classification - Public

Risk profile-based asset allocation

Asset Class	Overall View	Asset Allocation		
		Aggressive	Moderate	Conservative
Equity Funds	▼	75%	55%	25%
Debt Funds	▲	20%	40%	70%
Gold	▲	5%	5%	5%

Note:	Optimistic	▲
	Cautiously Optimistic	◆
	Cautious	▼

Category-wise view

MF Categories	View
Equity Oriented Funds	
Largecap Funds	▲
Large Cap Index Funds	▲
Multi/Flexicap Funds	▲
Large and Mid Cap Funds	◆
Mid cap / Small cap	▼
ELSS	◆
Value / Contra / Dividend Yield Funds	◆
Focused Funds	◆
Aggressive Hybrid Funds/Dynamic Asset Allocation/Balanced Advantage Funds	▲
Equity Savings Funds	▲
Sector/Thematic Funds	▼
Multi Asset Allocation Funds	▲

MF Categories	View
Debt Oriented Funds	
Short Duration Funds/Medium Duration Funds	▲
Banking & PSU Funds	◆
Corporate Bond Funds	▲
Target Maturity Index Funds	▲
Medium to Long / Long Duration Funds	◆
Dynamic Bond Funds	▲
Gilt Funds	◆
Ultra Short Duration/Low Duration/Money Market Funds	◆
Arbitrage Funds	▲
Liquid/Overnight Funds	◆
Conservative Hybrid Funds	◆
Credit Risk Funds	◆

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Equity MF Strategy – February 2024

- While the inflation in the US has come off from its highs, the macro data is holding up. While manufacturing has seen signs of deceleration, the consumption and the employment data remains robust. This has pushed the US bond yields higher and has created volatility in the equity markets. While the US Fed seems to hinting cuts in policy rates, the timing of it remains uncertain. Going forward, **a very important element that all risk assets will have to pay attention to is how the focus of both the US Fed and the US Government move towards managing liquidity, rates and growth dynamics.**
- Tight liquidity conditions and high interest rates are causing the growth rates in the Euro Zone to remain weak. While the ECB seems to be getting dovish and is guiding for rate cuts in the future.
- Chinese equity markets continue to be weighed down on incrementally weak macro data points. The Chinese government seems to be putting in measures to drive confidence back, including bringing in measures to support the stock market. With the valuations in the Chinese markets at multi year lows, any positivity that comes about due to the measures taken by the government, may drive global FPI flows in that market.
- Key elements of global headline inflation seem to be consolidating at lower levels, as most of the commodity and food prices have come off. However, impact of climate change on food production and new global geopolitical alignments, may have implication on future food inflation trend. The conflict in the Middle East and tight supply by OPEC+ members have driven volatility in crude oil prices. The troubles in the Red Sea may lead to rise in logistics costs for businesses across the world.
- With the Dollar Index rising, most of the emerging markets saw FPI outflows and weakened equity market sentiments for the month of January.
- The overall economic indicators in India continued to remain strong. The Q2FY24 GDP growth which came in at a higher than consensus growth rate of 7.6%, suggest the robustness in the economy. The growth was primarily by higher Gross Fixed Capital Formation, which ties well with our view that this is a investment driven upcycle in the economy. Consumption growth data remains tepid and remains a monitorable for the medium term, as higher capex should drive employment growth which should drive consumption growth.
- Many of the key indicators like the revival in the real estate and construction activities bode well for rural economy, which has yet to fire completely. The growth in Two-wheeler sales seems to give an early sign of improvement in the rural demand. Softening core inflation and expectation of rising employment in rural areas could further help lifting the demand sentiments. However, low reservoir level, muted Rabi sowing and lack of volume growth for FMCG companies remains a monitorable for the rural demand revival.
- Urban demand trends are showing mixed signals. Indicators like Credit card spends and air passenger traffic have been strong. However, passenger vehicle sales growth seem to be decelerating and needs to be monitored. Nevertheless, the deceleration in the services sector growth in the Q2FY24 GDP seem to be a concern and needs to be monitored.
- Corporate and Banking sector balance sheets in India have shown strong improvement, capacity utilisation data too has improved, and this has set the stage for increasing private capex demand. With policies like PLI, preference by global corporations to diversify out of China into economies like India and others, need to create more renewable energy assets and focus on import substitution by Indian government, the capex cycle seems to be on its way. Revival in capex demand from the private sector along with the steady spending from the Government (centre and state) is driving the capex cycle in India. This was also evident in the Q2FY24 GDP data. The Interim Budget for FY25 has also increased Government's Capex allocation by 11% YoY over FY24 budget estimates to INR 11.1 Tn.
- The RBI has paused its rate hikes and is projecting moderation in inflation going forward. It has also increased the risk weights in some categories to control unsecured lending. The recent focus of the RBI to keep liquidity on a tight leash in India could help contain inflation. While this has not had negative implication on growth trajectory so far, but with the economy geared up for high capital spending, implications of such tightness remain a key monitorable.
- The Equity markets have moved to near all time highs on Key indices, led by stable earnings performance. The quarterly earnings for Q3FY24 have been mixed so far with Banking, IT and FMCG reporting muted results, while Pharma, Metals, Auto and Cement reporting stronger performance**. The Indian equity markets could see consolidation in absence of any fresh incremental earnings triggers as the valuations of the Indian markets seem to be pricing in most of the medium-term positives, especially in the Mid and Smallcap segment**. The RBI is expected to gradually ease the liquidity and policy rates in CY24, which is likely to support the market on downside. CY24 may see a gradual narrowing in the base of the key performers in the equity market.
- Any large earnings cuts and consumer spending trends, relative valuations play (within the EM basket) and unfavourable general election results could weigh on the market performance. While, in the long term, improving domestic macro conditions, favourable demographics and higher capex investments could keep driving the Indian corporate earnings higher and support the equity markets.
- **Investment deployment strategy could be at 40% lumpsum and rest 60% to be staggered over the next 5-6 months. Investors have made strong returns from equity markets in the last 3 years and we think they should now consider rebalancing their portfolios, in terms of their asset allocation based on their risk profile. Investors can look to focus on categories like Largecap, Flexicap and Multi-asset funds. All allocations should be done in line with the risk profile and product suitability of the investor.**

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Debt Mutual Fund Strategy

- Corporate Bond Funds, which typically have a higher yield to maturities, look a safe bet at the current juncture.
- Additionally, with tight liquidity and a higher supply of corporate bonds and SDLs, the corporate bond spreads and SDL spreads are attractive vs the G-secs, thus providing accrual opportunity, and making the case for Corporate Bond Funds and SDL Index Funds.
- Thus, investors can look at Corporate Bond Funds and Short duration funds for a horizon of 15 months and above.
- Investors who are comfortable with volatility and have a longer horizon of 24 months and above can take exposure to Dynamic Bond Funds and longer-tenor SDL Index Funds to play the improved fiscal deficit dynamics.
- For lower volatility and a horizon of 3 months and above, investors can consider Arbitrage Funds.
- Whereas for a horizon of up to 3 months, investors can consider Overnight Funds and Liquid Funds.
- Investors can also look at Multi-asset allocation funds for a horizon of 36 months and above. Investors should invest in line with their risk profile and product suitability.

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Research presentation – Content

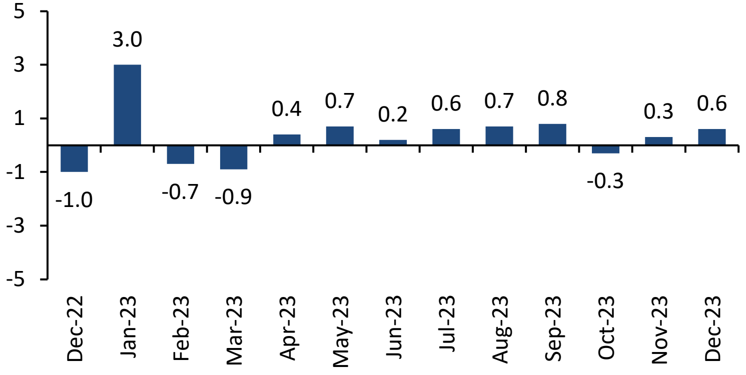
- US – Stronger than expected data, pushing back interest rate cut expectations
- Europe – Economy continue to grapple with on going slowdown
- China – Government trying to stimulate economy, amid declining market
- Commodities moving in a range, while crude rising due to geopolitical concern and tight supply
- Emerging markets – As dollar index rallied, Emerging Markets saw correction on back of FPI outflows
- Indian Market volatile due to FII outflows and stable domestic flow
- Sectoral performance and FPI flows in January 2024
- India Macros continue to exhibit strength
- Urban demand starting to show mixed picture
- Rural India : Green shoots seen on discretionary consumption, while agri growth slowdown expected
- Investments continue to remain driver of growth
- Q3FY24 Quarterly Earnings Review
- India valuations – Indian markets continue to remain expensive compared to peers
- Market Roundup – January 2024
- Sectoral outlook by fund managers – Part 1
- Sectoral outlook by fund managers – Part 2
- Monthly Sectoral Movement
- Key concerns for Indian equities
- Fixed Income Outlook
- Higher than expected US inflation and robust economy pulled the yields up
- In Europe, while the economy is slowing down, the uptick in inflation kept the yields flat
- US FOMC has pushed the rate cuts expectations away from March 2024
- Red Sea conflict poses a threat to inflation
- Interim budget surprised the market with lower-than-expected fiscal deficit
- Domestic inflation remains elevated due to low base and higher food inflation
- Banking system liquidity remains in deficit; the RBI is conducting VRR auctions to infuse temporary liquidity
- Despite strong dollar index, INR remained well balanced due to moderation in trade deficit
- Peaking of rate hiking cycle and rate cut expectations have pulled the G-sec yields down
- Widening of SDL and Corporate Bond Spreads vs G-secs is providing opportunity in the accrual space
- Strong demand for credit in a tight liquidity scenario may further push up the corporate bond spreads
- Disclaimer

Classification - Public

US – Stronger than expected data, pushing back interest rate cut expectations

US Retail Sales - MoM Change (%)

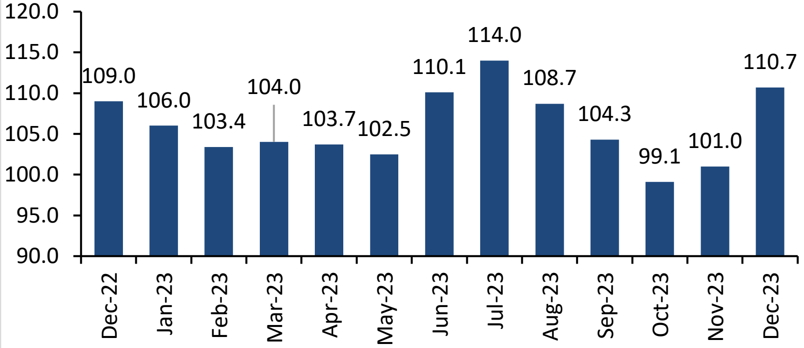
Trend remains favourable



Source: Bloomberg

US Consumer Confidence Index

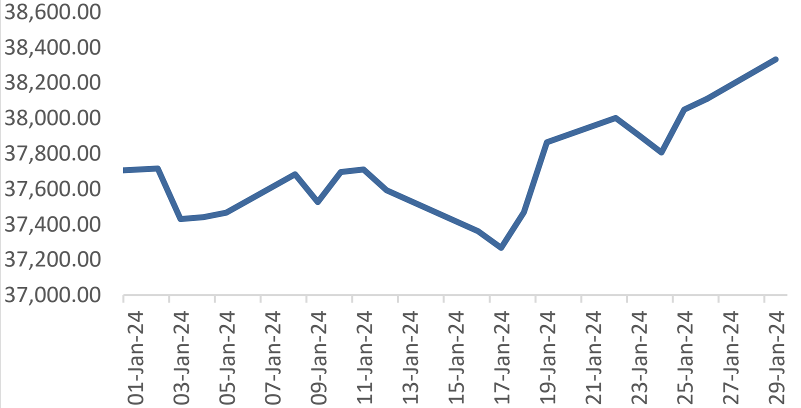
Strength in consumer confidence visible



Source: Bloomberg

Dow Jones Industrial Average Index

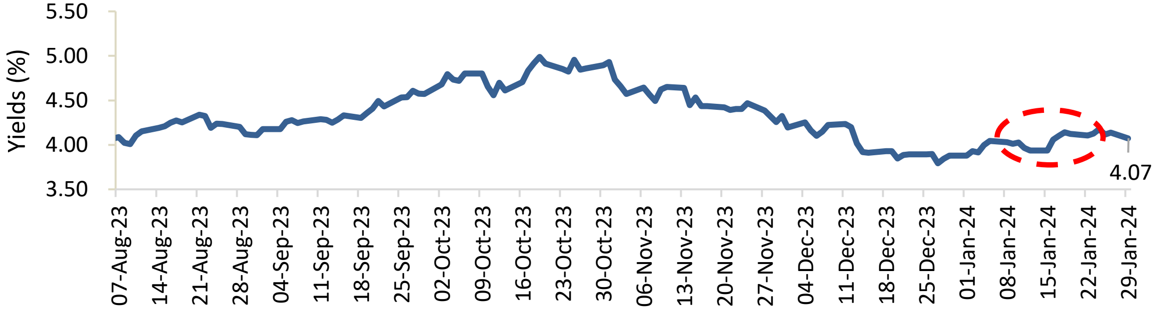
Strong Macro Data but rising bond yields has kept market volatile



Source: Bloomberg

US 10-Year Treasury Bond

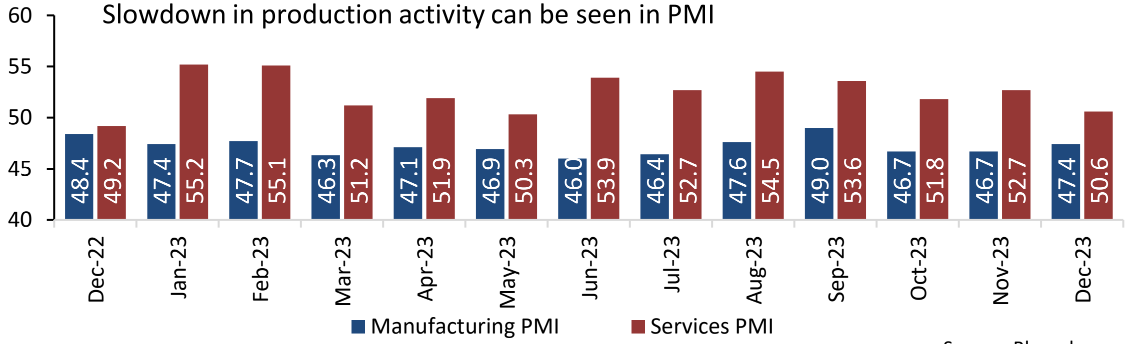
Strong Macro data have pushed yields higher … 2months show



Source: Bloomberg

US Manufacturing & Services PMI

Slowdown in production activity can be seen in PMI



Source: Bloomberg

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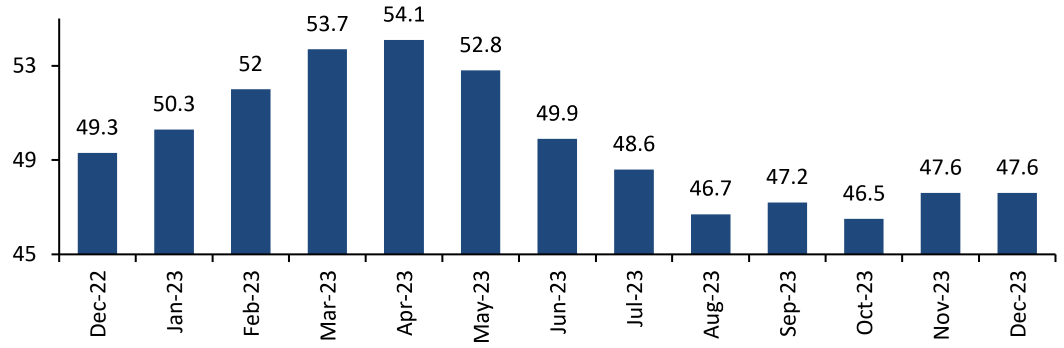
Europe – Economy continue to grapple with on going slowdown

S&P Global Eurozone Composite PMI

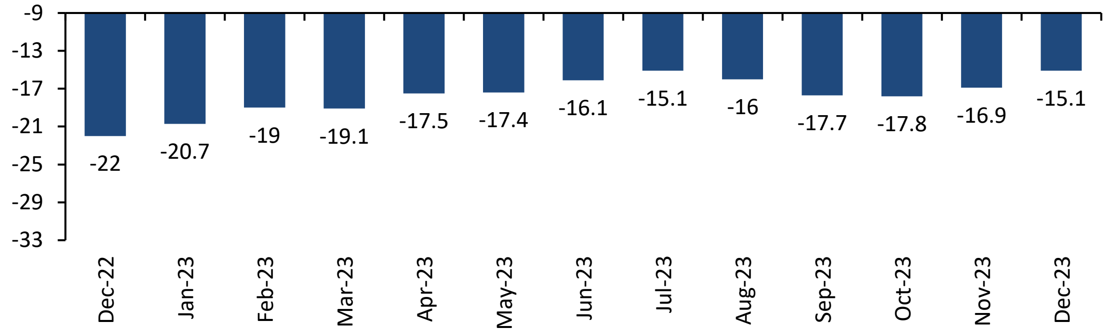
Manufacturing & Services continuing in the contraction zone



Source: Bloomberg

Eurozone Consumer Confidence Indicator

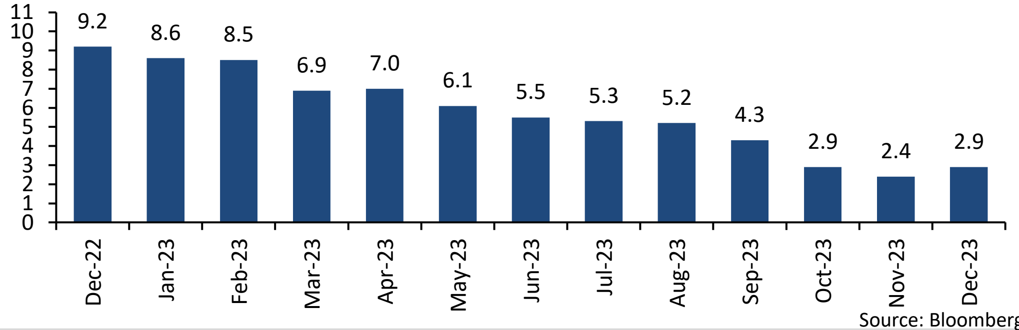
In the negative territory, but improving



Source: Bloomberg

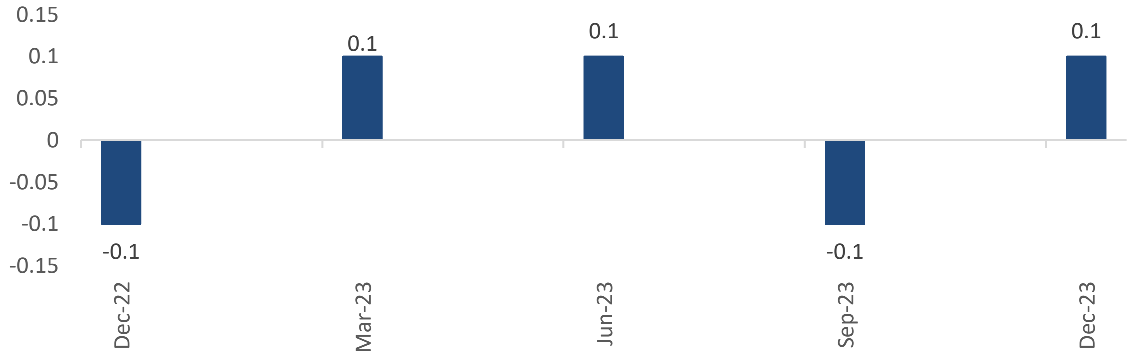
Eurozone CPI YoY (%)

Eurozone CPI (YoY %) continues to dip, tight monetary policy measures by ECB seems to be the key catalyst



Source: Bloomberg

Eurozone GDP YoY (%)



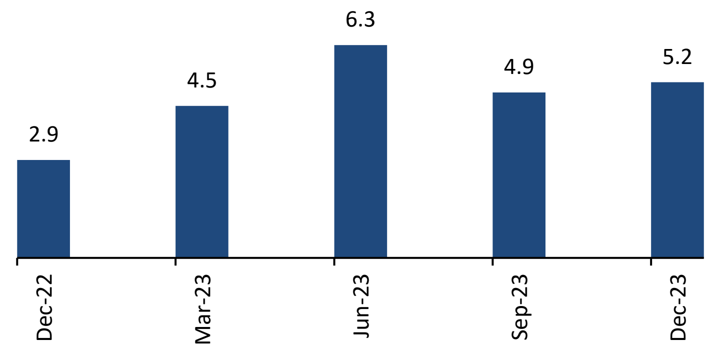
Source : Bloomberg

Classification - Public

China – Government trying to stimulate economy, amid declining market

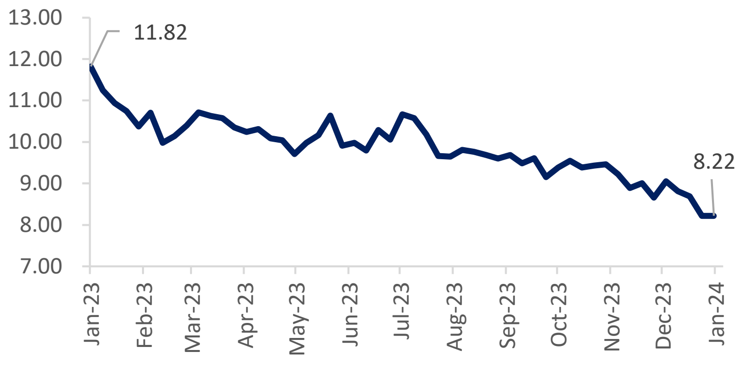
China Quarterly GDP - YoY Change (%)

Chinese GDP remains below expectations



Source: Bloomberg

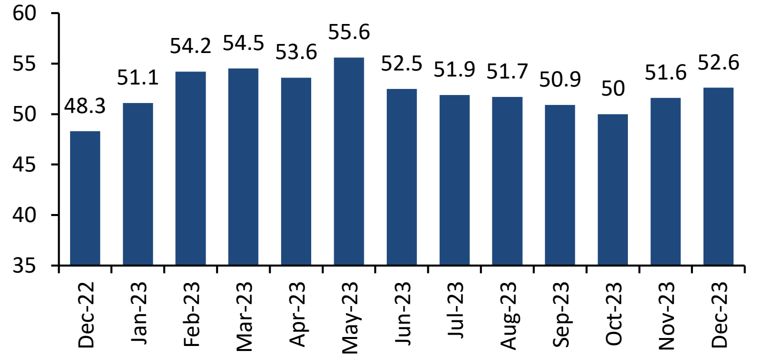
Driving the Chinese Market Valuations Lower (12M Fwd PE)



Source : Bloomberg

China Composite PMI

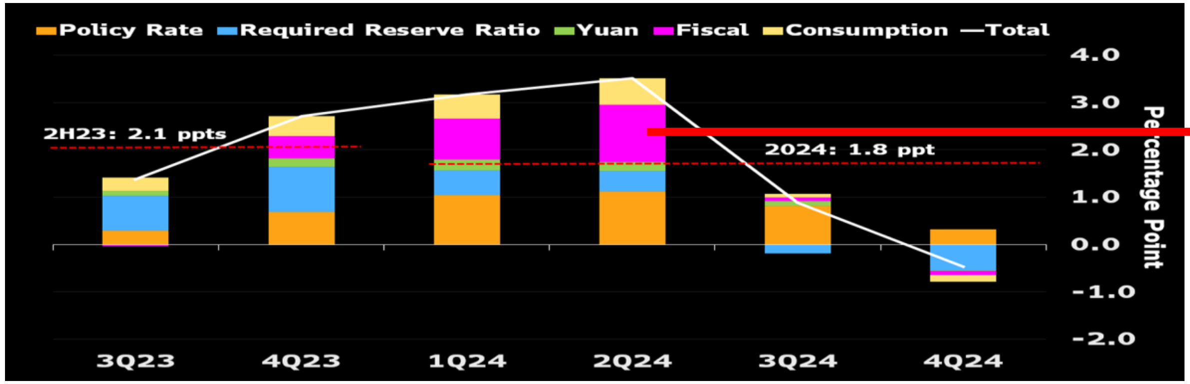
PMI growth, though expanding, remain below expectations



Source: Bloomberg

Chinese government trying stimulate the economy

Source: Bloomberg



China's issuance of 1 trillion yuan ($139.8 billion) sovereign debt plan will raise the budget deficit ratio to about 3.8% of GDP (well above the 3% target set in March 2023) and is expected to drive economic growth.

HDFC BANK RESEARCH

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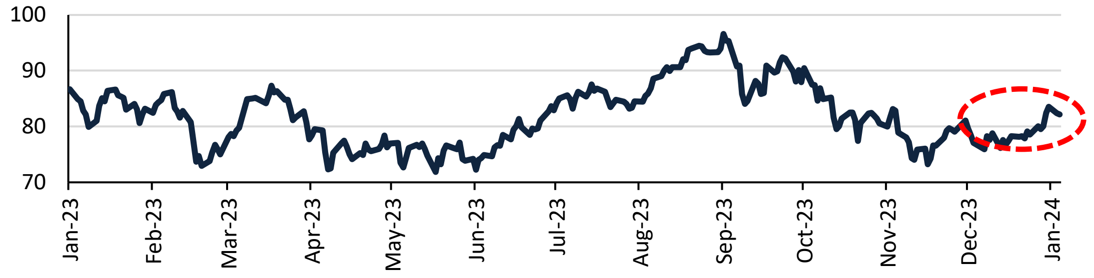
Commodities moving in a range, while crude rising due to geopolitical concern and tight supply

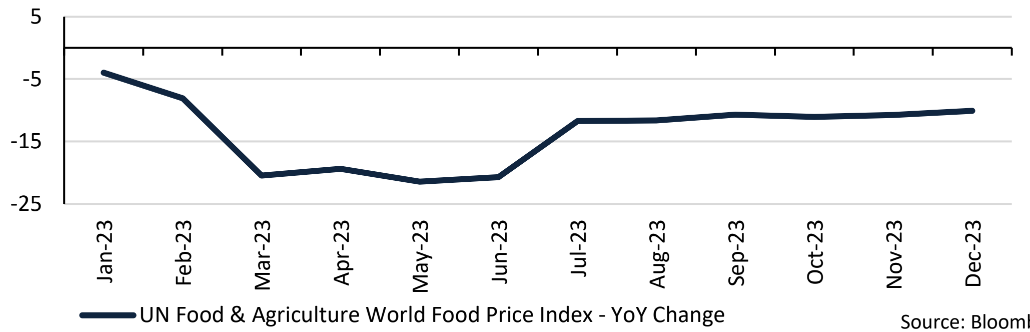
Brent Crude (USD Per Barrel)

Price rising on back of geopolitical tension, weaker dollar and OPEC prediction of oil demand to expand quickly



Source: Bloomberg

Food Inflation Remains Low



Source: Bloomberg

London Metals Exchange Index

Metals prices moving in a range

Source: Bloomberg

Gold Price (USD Per Troy Ounce)

Expectation of rate cuts in U.S driving uptick in gold

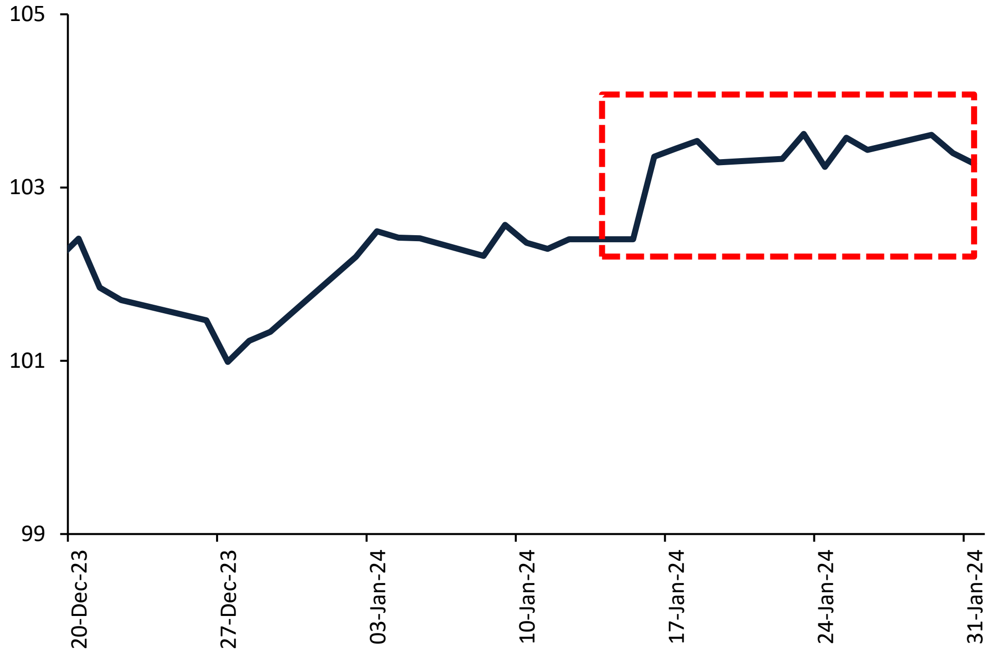
Source: Bloomberg

Classification - Public

Emerging markets – As dollar index rallied, Emerging Markets saw correction on back of FPI outflows

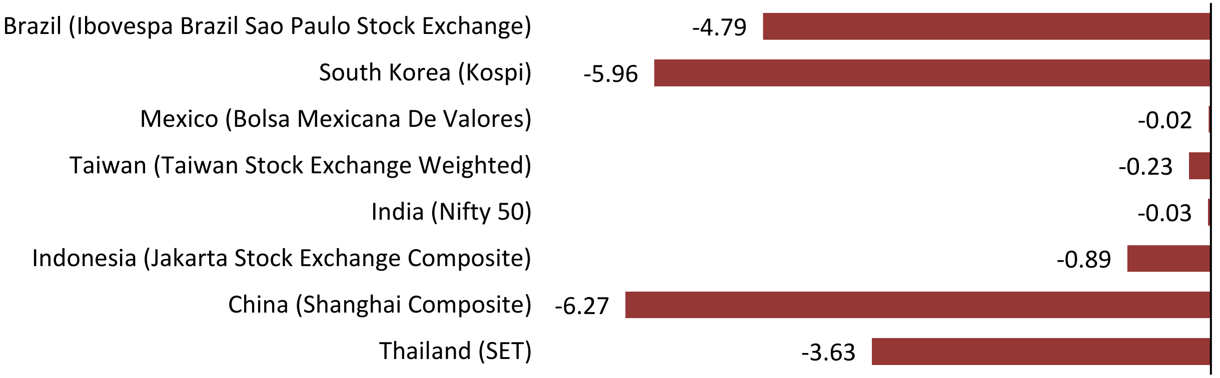
US Dollar Index

Rising dollar index impacting the emerging markets flow



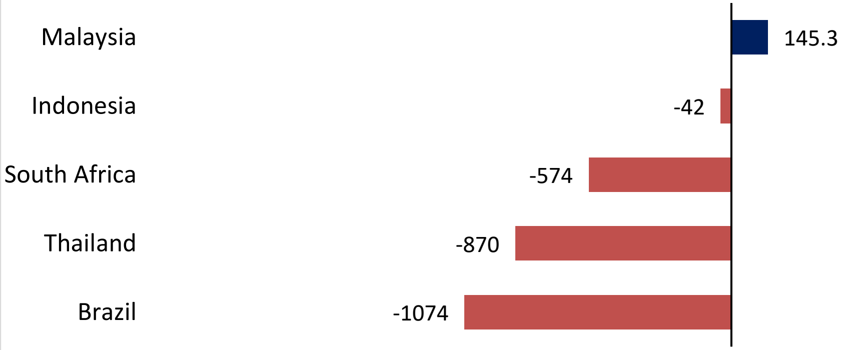
Source: Bloomberg

Emerging Markets - Absolute Returns of major equity indices in January 2024 (%)



Source: Bloomberg

Emerging Markets - Net Flows In January 2024 (USD Million)

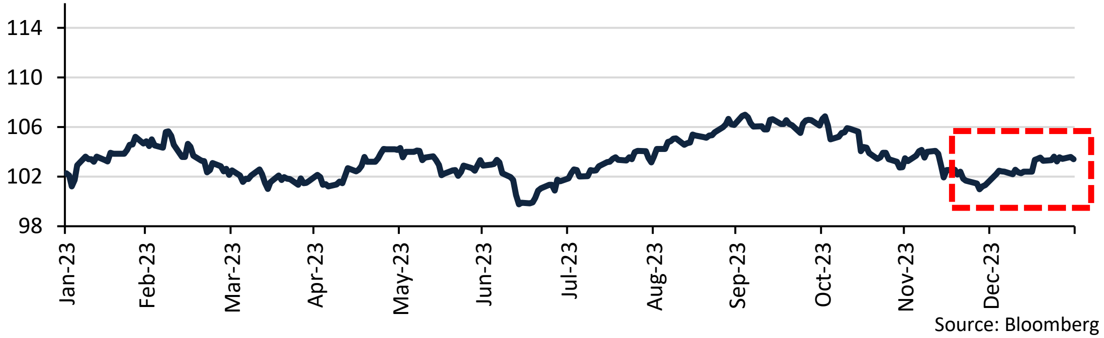


Source: Bloomberg

Indian Market volatile due to FII outflows and stable domestic flow

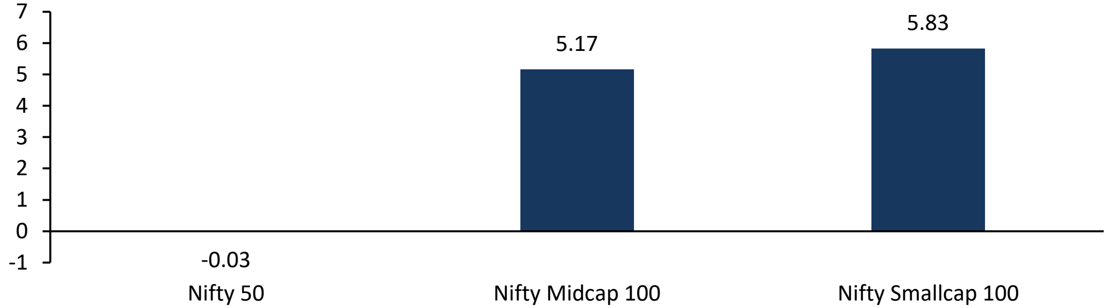
US Dollar Index

Rising dollar index has led to FPI outflows in India too



Source: Bloomberg

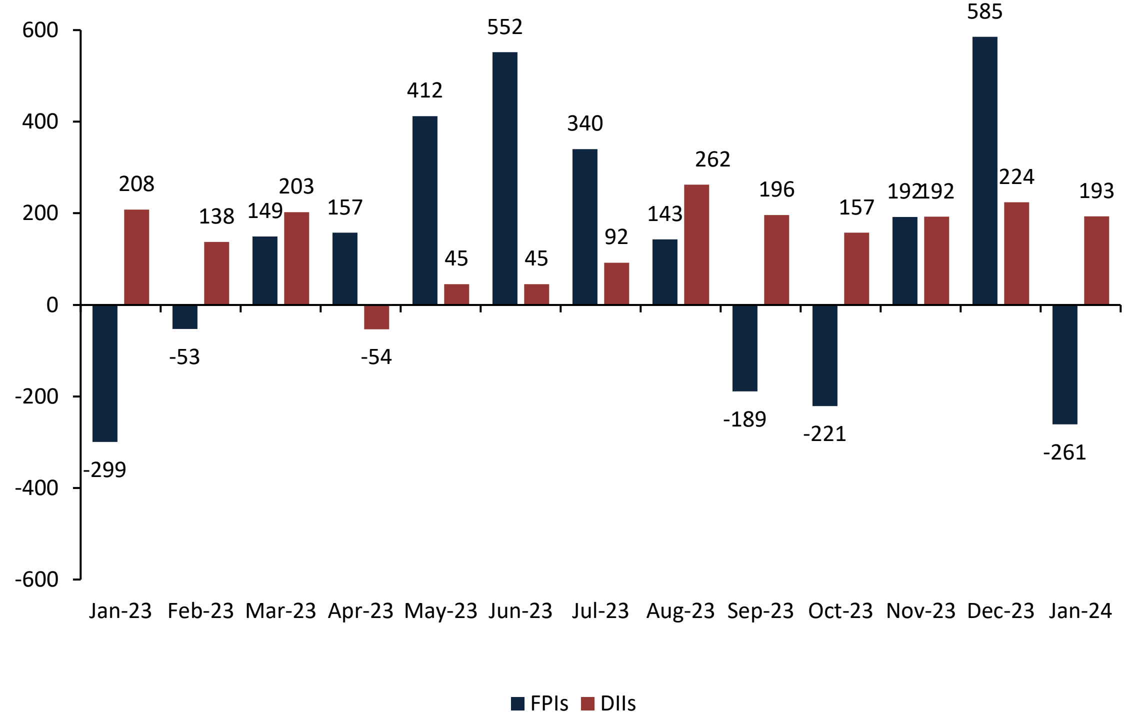
Absolute Return In January 2024 (%)



Source: Bloomberg

Net Flows In Equities (Rs Bn)

In line with other Emerging Markets, FII were net sellers in the month of January

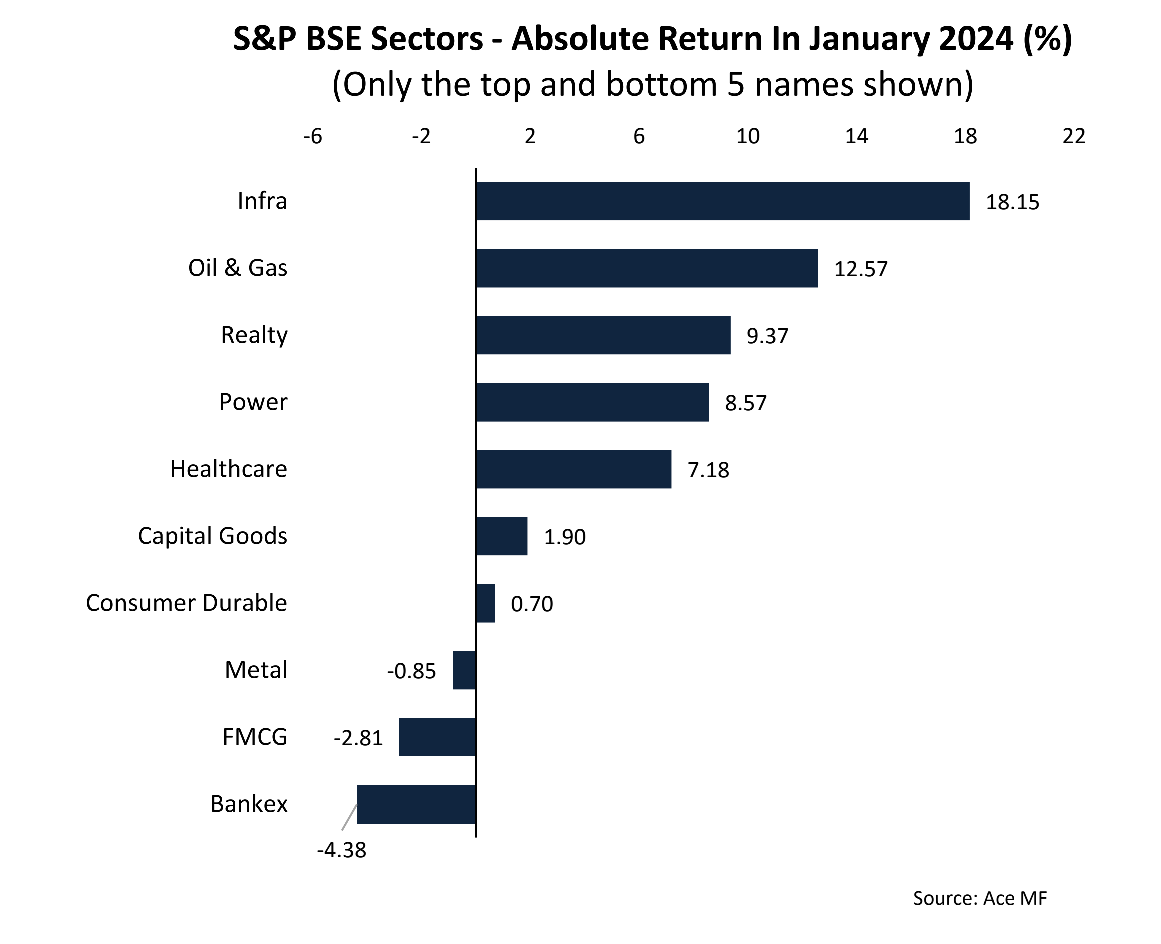


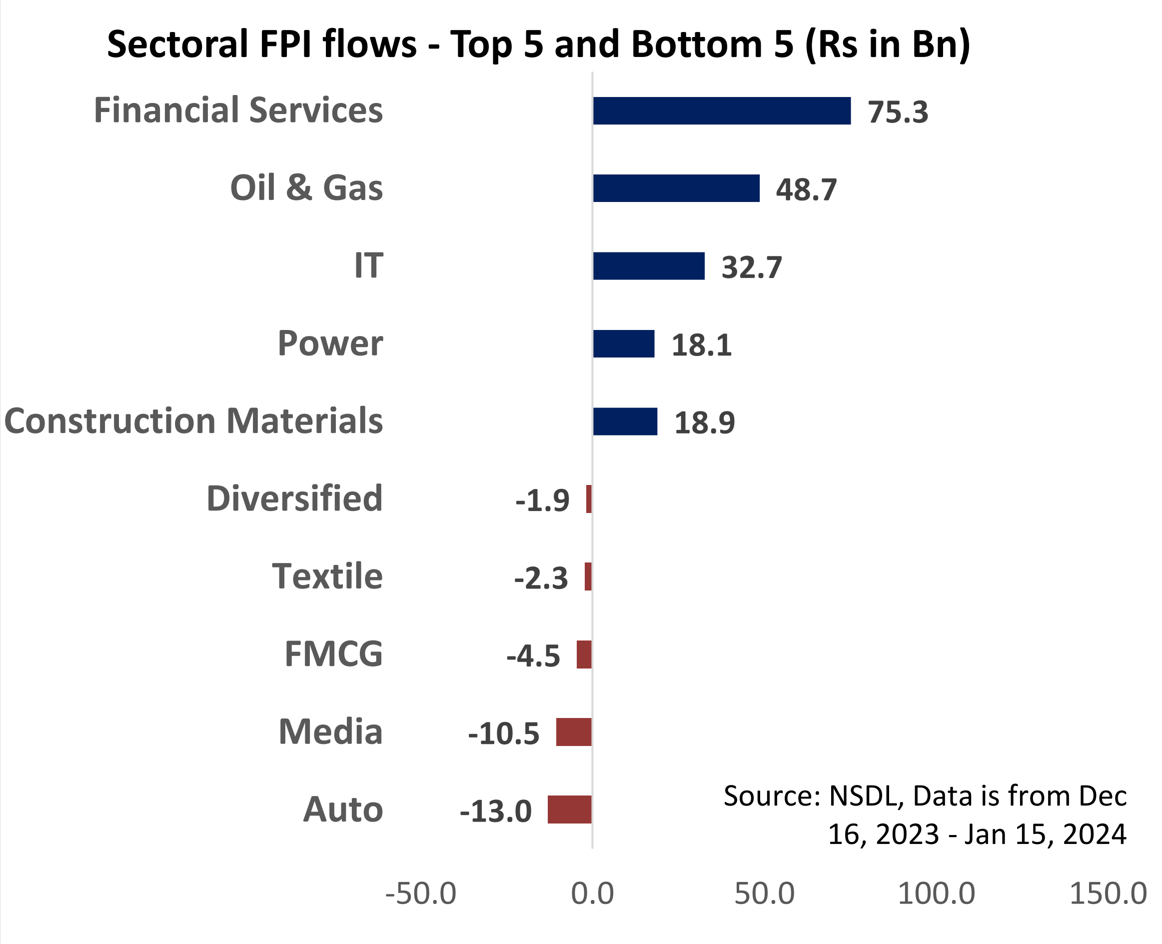
*For 2024, FPI and DII data is up to January 31 & 29, 2024, respectively

Source: SEBI, CDSL

Classification - Public

Sectoral performance and FPI flows in January 2024

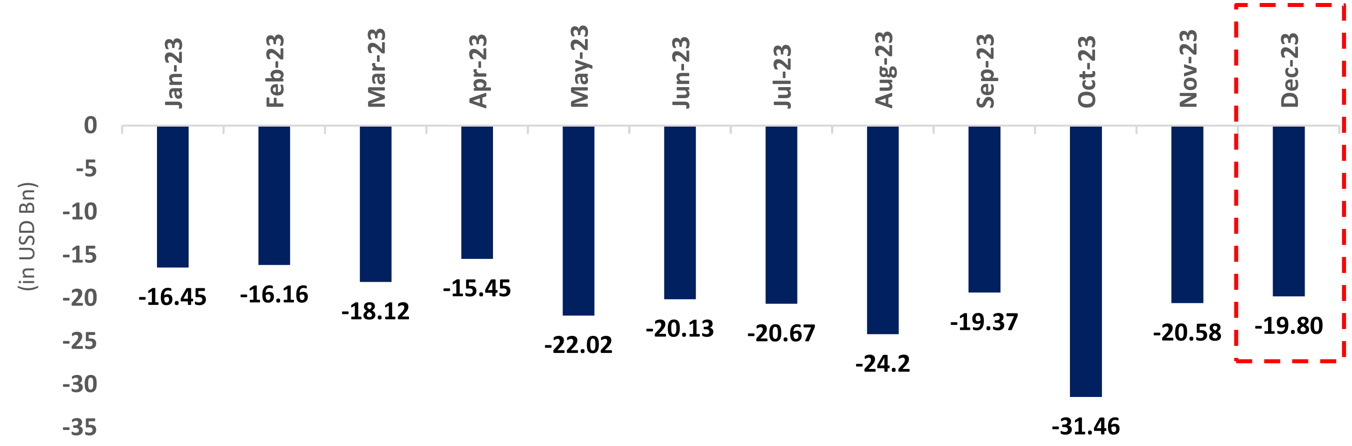




Classification - Public

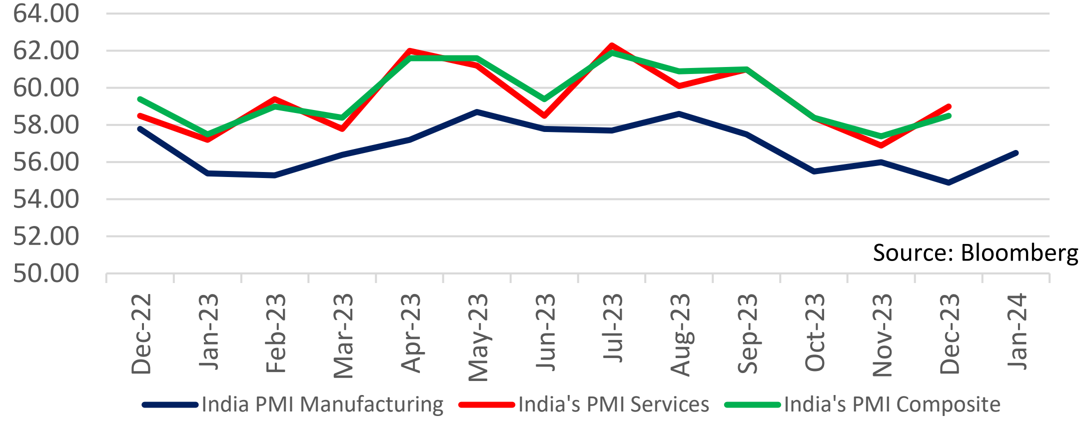
India Macros continue to exhibit strength

Trade deficit is improving



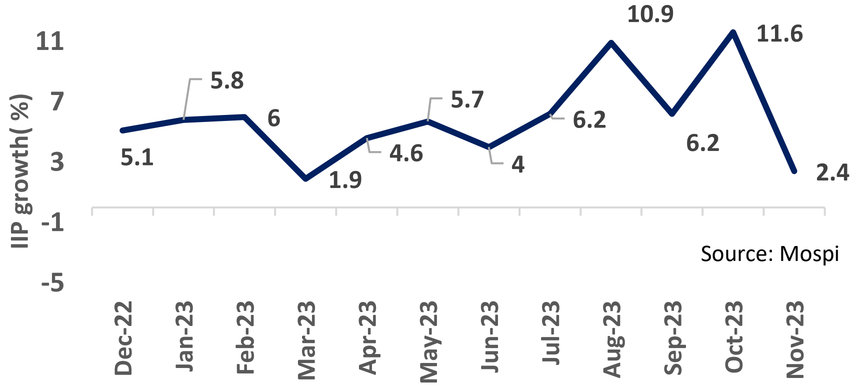
Source: Ministry of Commerce & Industry

Composite PMI continues in expansion zone while manufacturing PMI is lagging



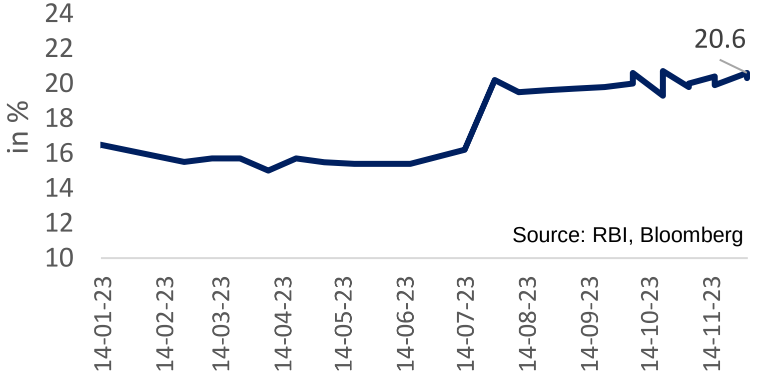
Source: Bloomberg

IIP growth impacted by weak manufacturing growth



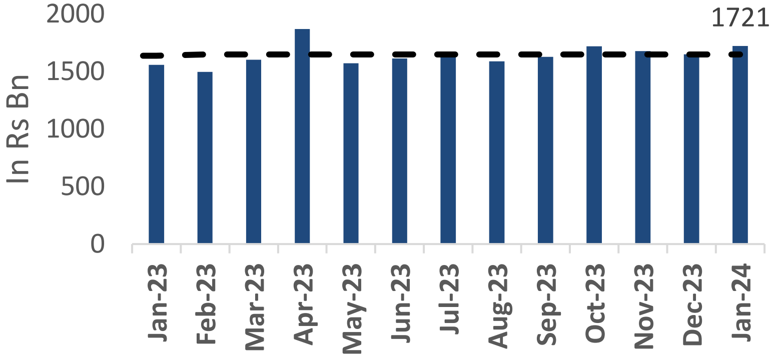
Source: Mospi

Bank credit growth shows strength



Source: RBI, Bloomberg

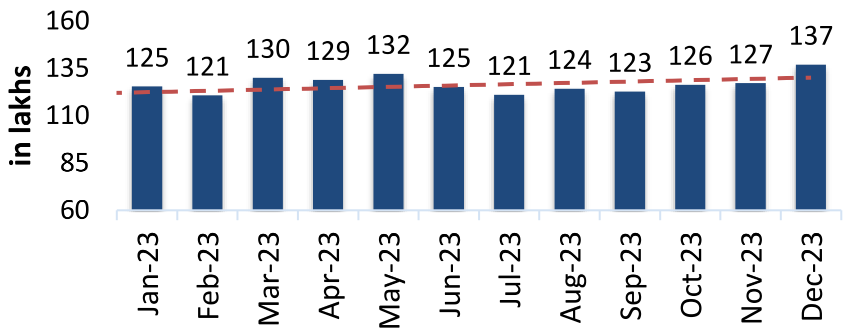
GST collection remains healthy



Source: Ministry of Finance

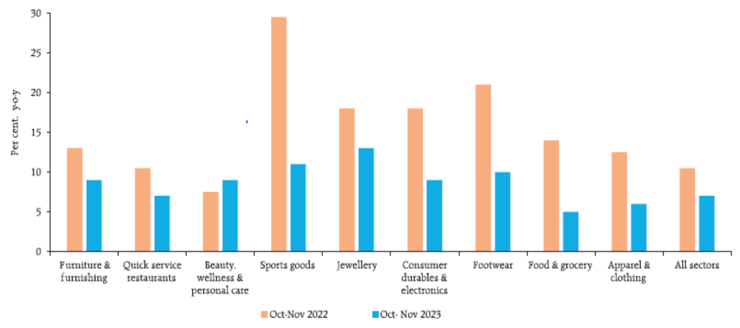
Urban demand starting to show mixed picture

Domestic Air Passenger Traffic crosses pre pandemic levels…



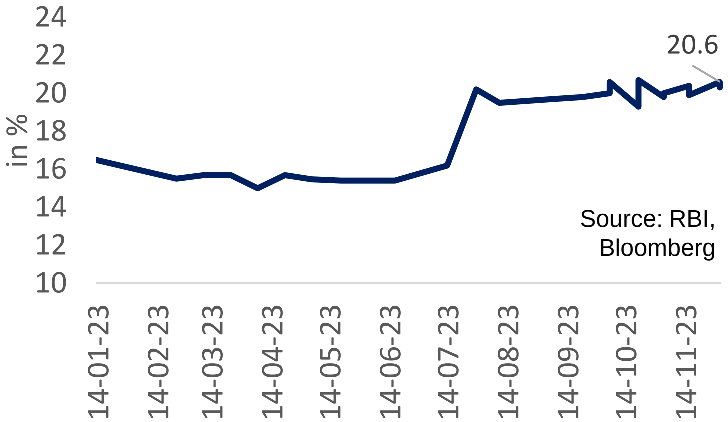
Source: DGCA

Annual sales growth moderated across most consumption categories



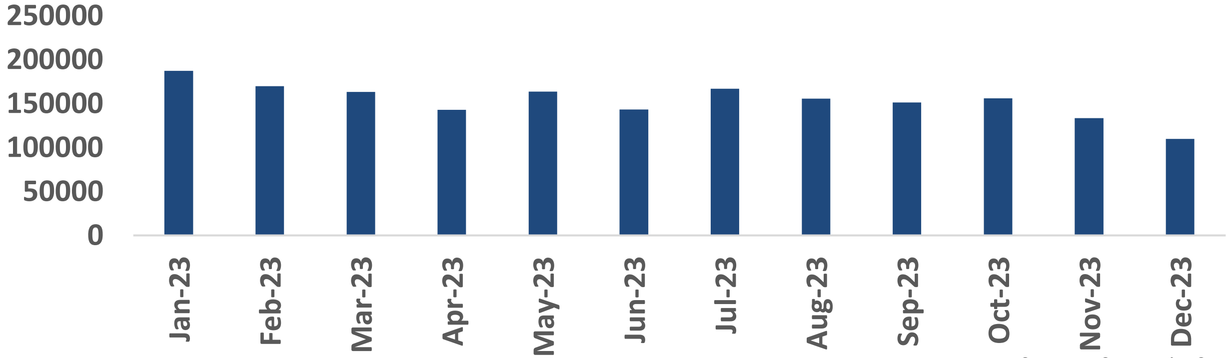
Source: RBI Bulletin January 2024

Credit card spend continues to remain strong



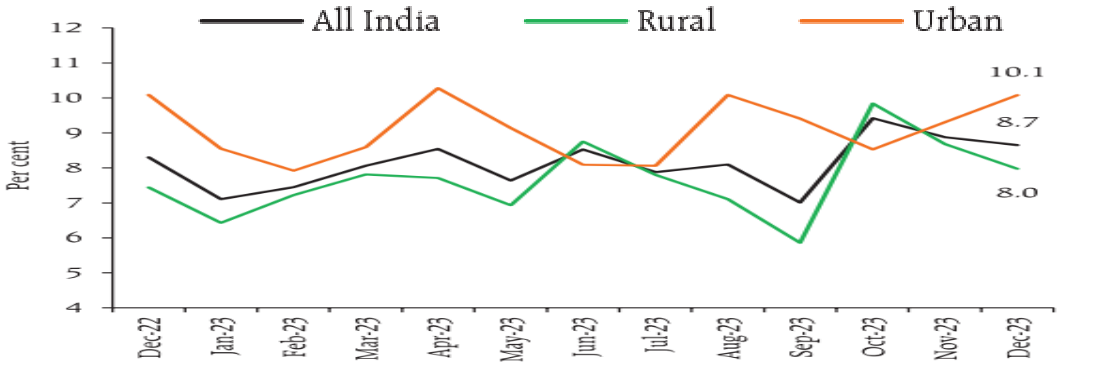
Source: RBI, Bloomberg

Passenger vehicles wholesale sales seen decelerating… remains an important monitorable for discretionary consumption



Source: Cogencis, SIAM

Urban unemployment rises



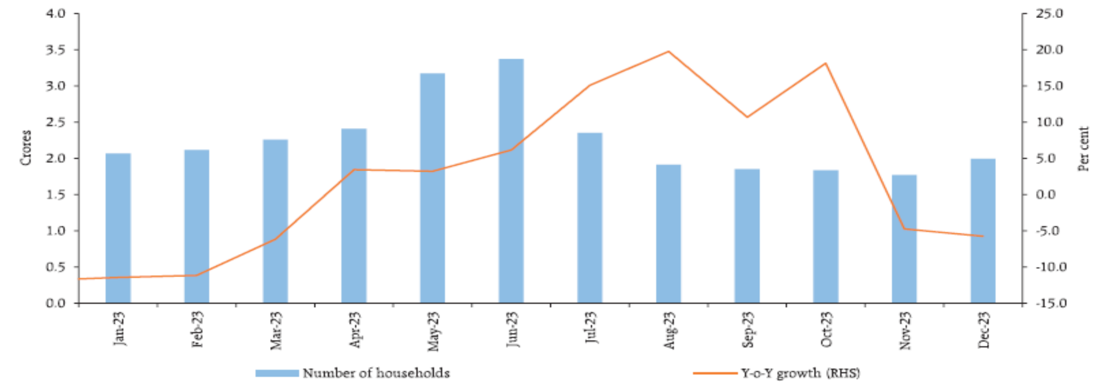
Source: RBI Bulletin January 2024

HDFC BANK RESEARCH

Classification - Public

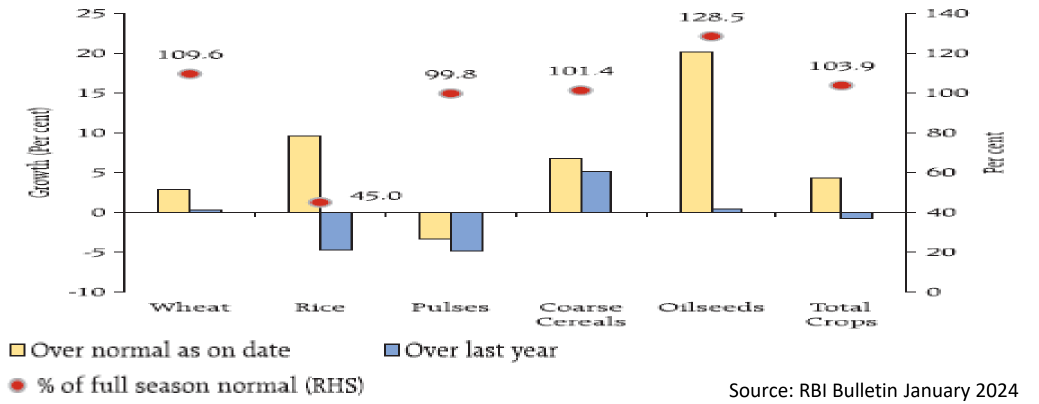
Rural India : Green shoots seen on discretionary consumption, while agri growth slowdown expected

Demand for workers under MGNREGS fall, suggesting improved job availablity



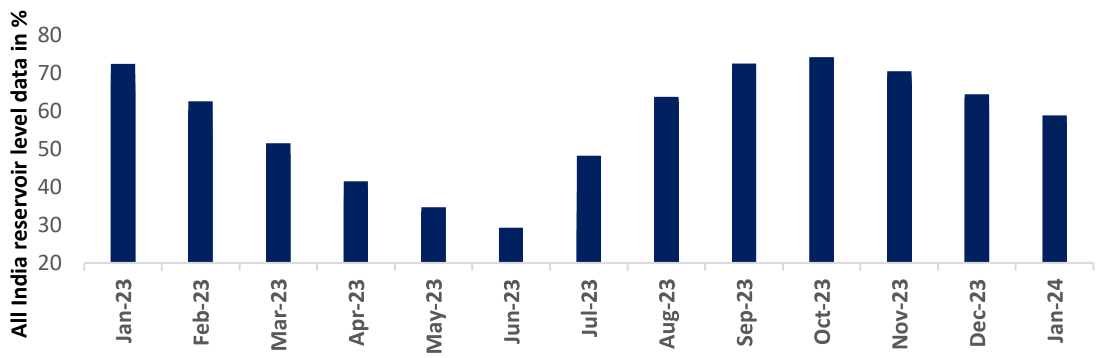
Source: RBI Bulletin January 2024

Sowing is above long period average but remains lower than last year



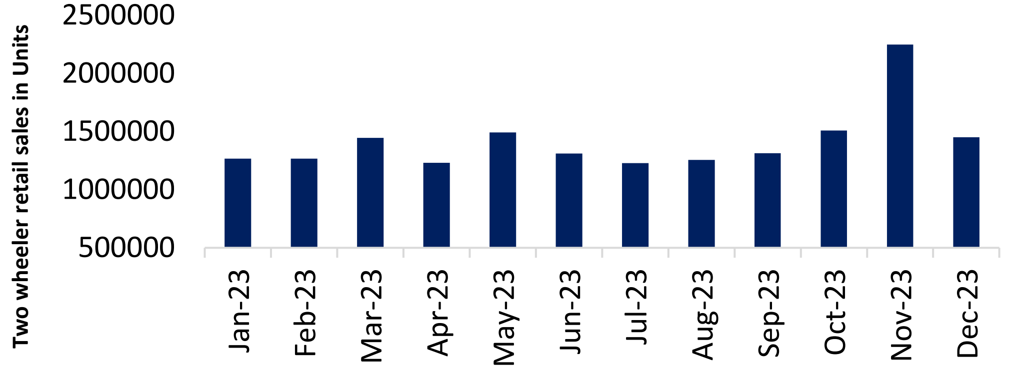
Source: RBI Bulletin January 2024

Reservoirs level seen depleting…may impact rabi output.



Source: Cogencis

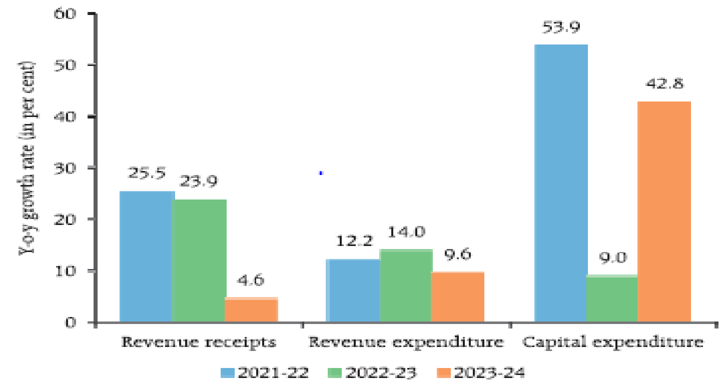
Rising two wheeler sales showing green shoots in rural discretionary demand



Source: Bloomberg

Investments continue to remain driver of growth

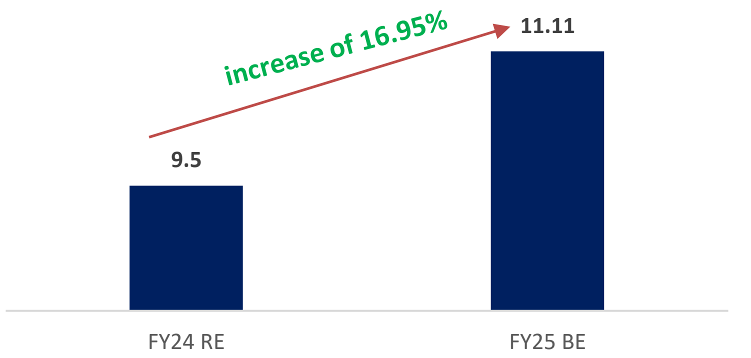
State Govt's Capex shows robust growth in FY24



Source: RBI Bulletin January 2024

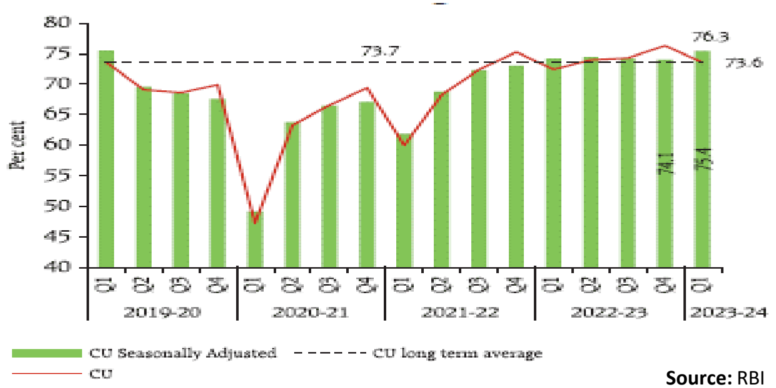
Government capex targets continue to remain robust

in trillion Rs.



Source: Budget at a glance

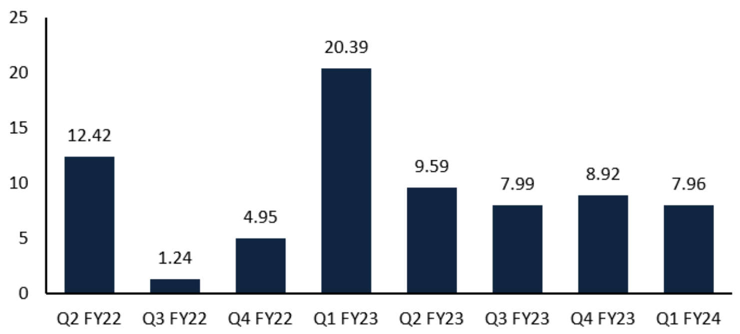
Capacity Utilisation in Manufacturing sector above averages, driving needs for further Capex…



Source: RBI

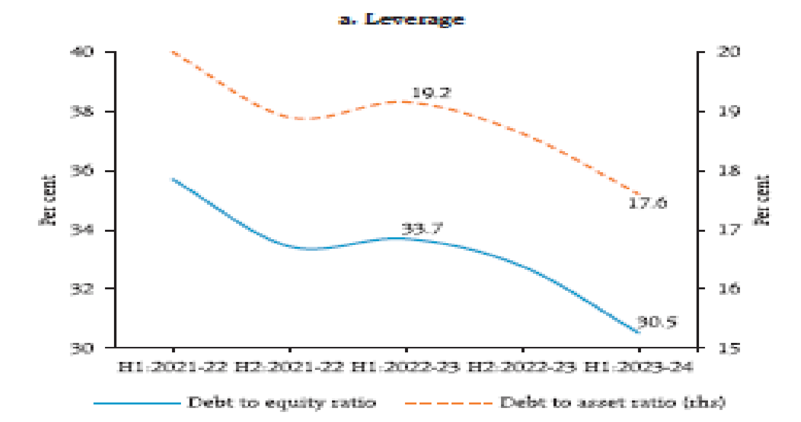
Gross Fixed Capital Formation - YoY Change (%)

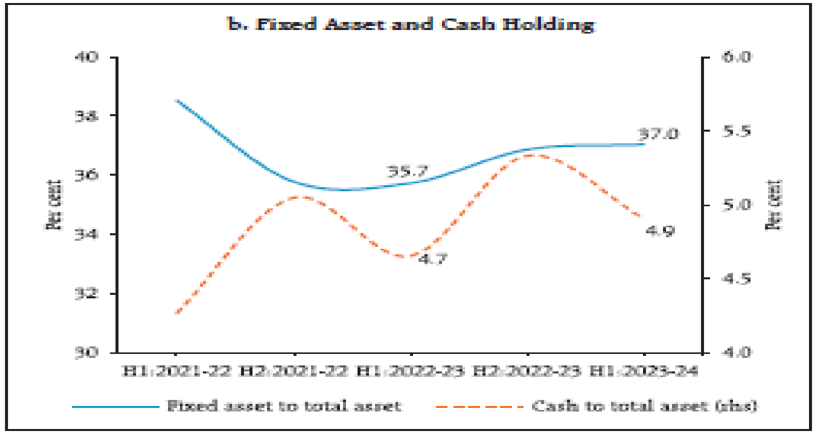
Momentum sustaining



Source: MoSPI

Leverage and Fixed Asset of Listed Private Manufacturing Companies have improved setting stage for fresh capex





Note: Results are based on 1,571 listed private manufacturing companies.
Sources: Capitaline database; and RBI staff estimates.

Classification - Public

Q3FY24 Quarterly Earnings Review

Sector	Net Sales - YoY Growth (%)			EBITDA - YoY Growth (%)			PAT - YoY Growth (%)		
	Q3 FY24	Q2 FY24	Q1 FY24	Q3 FY24	Q2 FY24	Q1 FY24	Q3 FY24	Q2 FY24	Q1 FY24
Auto & Auto Anc	25.58	8.15	20.31	50.58	24.72	42.46	49.67	13.24	37.26
BFSI	30.45	35.48	31.25	23.39	22.07	24.63	34.12	41.55	42.01
Capital Goods	11.62	15.78	24.96	6.53	42.48	48.68	9.32	48.34	48.21
Cement & Products	7.87	13.16	15.82	65.82	117.19	4.89	85.53	146.40	14.20
Ecomm	36.40	30.57	37.78	27.96	41.79	43.27	49.95	55.81	54.02
FMCG & Retail	6.77	6.25	9.74	14.82	18.97	22.77	18.89	6.15	22.77
Healthcare	6.12	7.66	10.10	8.14	12.79	6.01	7.53	15.71	8.27
IT	2.63	6.03	10.62	0.76	3.24	9.96	-1.95	2.72	10.01
Metal & Mine	0.98	-0.62	-4.64	49.43	52.36	-47.74	144.35	-150.84	-52.28
Oil & Gas	0.74	-7.25	-6.86	54.02	190.76	207.62	55.12	223.05	229.84
Others	14.98	14.00	5.79	19.45	16.83	-0.35	18.89	21.43	9.69
Power	13.11	36.52	-3.25	115.54	147.18	12.36	24.37	87.66	-47.66
Realty	-17.58	28.84	-0.91	-29.06	50.24	-4.25	-26.35	39.67	-10.22
Telecom	12.74	-3.16	5.71	664.61	10.74	74.31	-592.21	8.29	70.00
Transport	10.28	10.50	-3.57	22.49	7.18	-25.70	13.01	22.62	-17.63
Grand Total	8.91	6.06	5.04	29.00	57.44	33.46	33.01	40.75	39.00
Ex-Financials	2.41	-2.01	-1.36	29.59	61.48	34.24	32.13	40.10	37.18

Data as on January 29, 2024 and pertains to 71 companies within the Nifty 200 universe

Source: Capitaline, HDFC Bank Research

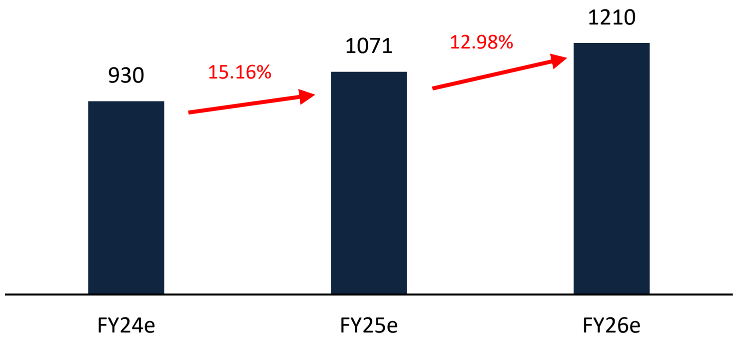
Key Observations:

- IT companies reported results which were above expectations, though at an absolute level results remain weak.
- Banking too saw muted results on back of declining NIM.
- FMCG results were also weak on back of muted volume growth.
- Cement sector reported strong results on back of margin expansion

Classification - Public

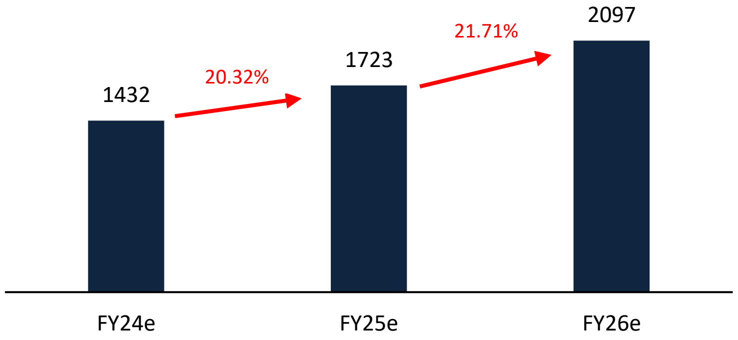
India valuations – Indian markets continue to remain expensive compared to peers (To Change as discussed)

Nifty 50 - Forward EPS (Rs)



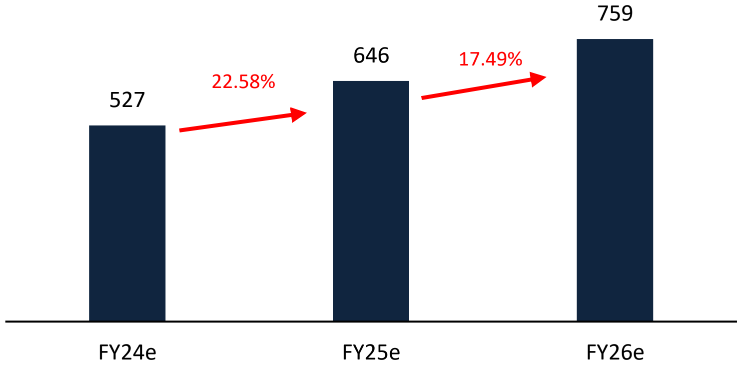
Source: Bloomberg

Nifty Midcap 100 - Forward EPS (Rs)



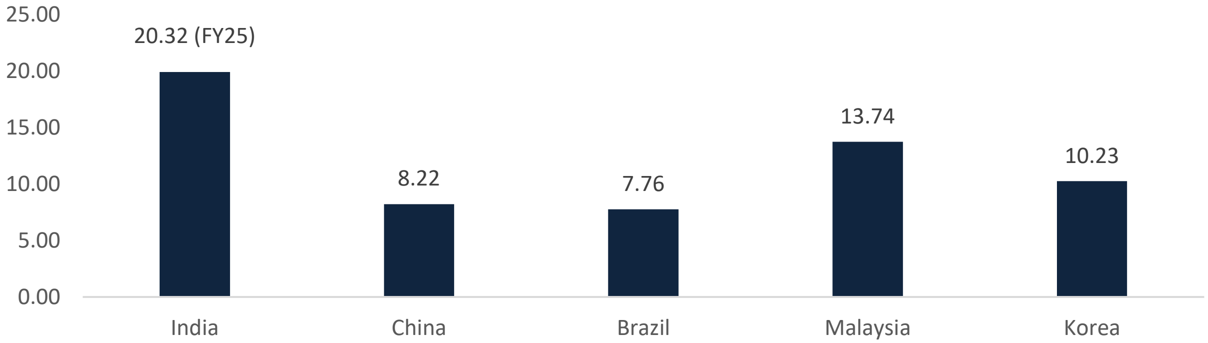
Source: Bloomberg

Nifty Smallcap 250 - Forward EPS (Rs)



Source: Bloomberg

12M Expected Fwd PE of India VS Emerging markets peers



Data as on 26th January 2024

Source: Bloomberg

12M expected Fwd P/E (x) Comparison By Market Cap

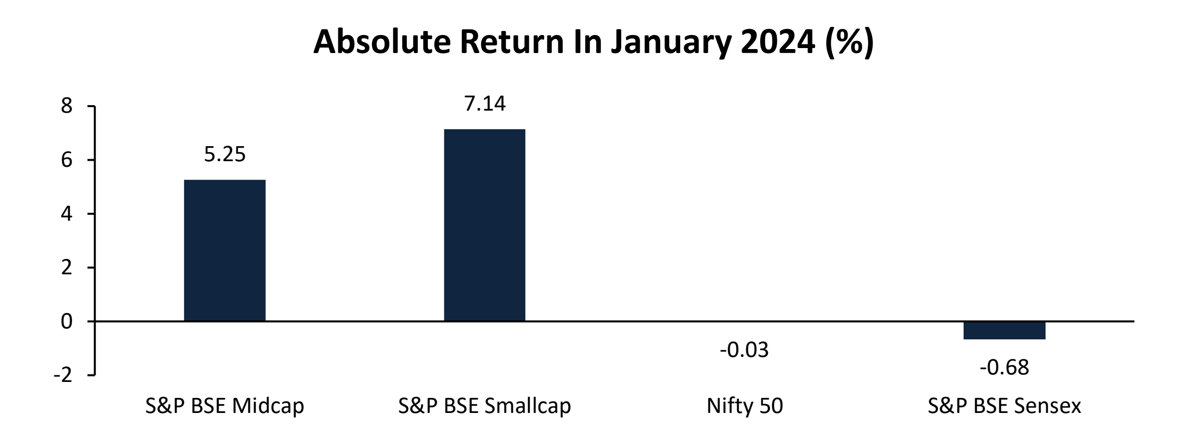
Index	FY24 (Est)	FY25 (Est)
Nifty 50	23.55	20.32
Nifty Midcap 100	34.72	28.23
Nifty Smallcap 250	31.30	25.83

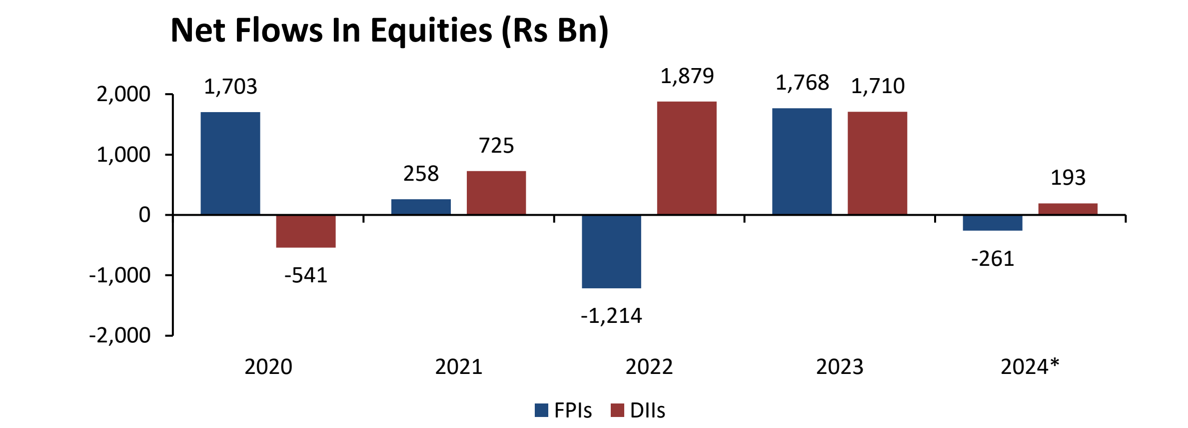
Source: Bloomberg

Classification - Public

Market Roundup – January 2024

- Indian equities ended the month on a mixed note. S&P BSE Sensex ender lower to the tune of 0.7% and Nifty 50 ended flat month-on-month (MoM).
- The S&P BSE Midcap and Smallcap indices ended higher by 5.3% and 7.1% MoM, respectively.
- In terms of BSE sectoral indices, Infra was the top performer. In contrast, Bank Index, FMCG and Metal underperformed the most.
- Weaker than expected earnings, geopolitical tensions in Middle East, significant rise in oil prices due to conflict in the Red Sea, led to volatility in the Indian Markets.





*For 2024, FPI and DII data is up to January 31 & 29, 2024, respectively

Source: SEBI, CDSL

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Classification - Public

Sectoral outlook by fund managers – Part 1

Sector	Particulars
Financials	**View –Neutral to Positive** • Valuations in most of the Banks are reasonable, especially the Largecap banks. • While the concerns around NIM were waning, the Q3FY24 results have again brought the concerns back to fore. • Credit cost (provisioning) are holding up, some stress on the unsecured book of few institutions have been witnessed in the Q3FY24 results. • High borrowing costs and tightening regulations could impact NBFC performance. AMCs and PSU Banks are finding favour. • Most fund managers are running underweight in the sector, with overweight stance in the private sector banks, within the sector.
IT	**View – Negative to Neutral** • Q3FY24 results were weak at an absolute level for larger companies, but better than expectations. Companies have been able to protect margin. • Guidance has seen marginal improvement, but nothing material. • Stocks have rallied in the recent past, but are expects to consolidate going forward. • Some funds took tactical positions and have reduced their exposure post the recent rally, while some funds have reduced their underweight position
Pharma	**View – Overweight** • Reasonable valuations • US is seeing abatement of price erosion in the generic space and some shortage of drugs has built up, which should be positive for Indian pharma stocks. • Decline in the raw material prices to drive margins and earnings. • Fund Managers expect the sector to outperform on the back of improved earnings given lower base and relative under ownership.
Auto	**View – Overweight** • Passenger vehicle demand has started to see some early weakness while 2-Wheeler stocks are seeing renewed traction and driving alpha. • SUV oriented companies expected to still hold on to earnings growth. • EV continues to be a strong emerging theme and players linked to it seem to be getting higher allocation. • Commercial vehicle sales seems to be topping out. • Auto ancillaries stand to gain due to China+1, Europe+1, PLI.

Classification - Public

Sectoral outlook by fund managers – Part 2

Sector	Particulars
Construction & real estate	**View – Positive** • Favourable demand scenario for housing in terms of volume growth. • Government's focus on infrastructure and investment cycle. • Real estate stocks are also finding space in the Fund Portfolios, as growth in the sector quite strong. **Approach followed by most AMCs -** Prefer investing in this space through proxy sectors such as housing finance companies, cement, steel, pipes, and building materials, among others.
Consumption	**View – Gradually reducing underweights- Neutral** • Staples - Rural India demand patchy. Volume growth missing. Valuations high. Funds generally underweight. • Hotels/Travel – Valuations rich, funds not looking to raise weights. Earnings visibility is strong. • Consumer Durables – Funds are looking to bottom fish, as they expect turnaround of demand. • Retail and Quick Service Restaurant: Retail demand expected to improve, while QSR seem to be finding favour in portfolios due to expectations of change in consumer behaviour. **Long-term positives** • Rising per capita income. • Premiumization across categories.
Capital goods, industrials, utilities	**View – Neutral** • Capex cycle uptick implies that domestic cyclicals are gaining traction. • Reduction in commodity prices adding to margin tailwinds. • Export prospects appear promising, albeit on a bottom-up basis. • Order book is robust, and earnings remain very. • New ideas also emerging as the sectoral tailwinds broaden. • **Valuations are steep, while earnings momentum holding up. Funds with high exposure not keen on raising further weights, trimming at margin.**
Metals	**View – Neutral to positive** • China stimulus leading to improved outlook. Indian government giving adequate protection to the domestic players from global dumping. Most fund managers are running underweight positions. Some fund manager have reduced their underweight positions.

Classification - Public

Monthly Sectoral Movement

Absolute Monthly Return By Sector (%)

Index	Jan-23	Feb-23	Mar-23	Apr-23	May-23	Jun-23	Jul-23	Aug-23	Sep-23	Oct-23	Nov-23	Dec-23	Jan-24
S&P BSE 500	**-3.36**	**-2.55**	**0.33**	**7.08**	**3.51**	**3.86**	**3.80**	**-0.81**	**2.04**	**-2.93**	**6.75**	**8.01**	**1.90**
Auto	5.29	-2.32	-3.35	10.29	7.94	6.76	3.14	-1.40	3.65	-1.25	10.08	5.43	4.18
Bankex	-5.78	-0.32	0.93	9.18	2.11	0.12	1.85	-4.01	0.35	-3.44	3.47	8.12	-4.38
Basic Material	-5.30	-7.07	2.54	7.83	1.70	2.39	3.19	1.06	1.70	-3.70	7.25	11.39	0.33
Capital Goods	1.39	0.54	1.50	9.71	1.31	9.79	8.15	2.66	6.20	-4.07	8.88	11.31	1.88
Consumer Discretionary	-2.15	-1.13	-1.74	9.25	7.18	5.94	4.46	2.10	2.40	-1.38	9.36	5.91	2.35
Consumer Durables	-5.01	1.30	0.45	2.91	6.47	5.67	-0.25	4.24	3.18	-2.32	7.42	6.11	0.70
Energy	-9.46	-12.14	1.95	7.19	-0.07	-0.24	6.89	-4.38	3.20	-2.17	9.17	11.06	12.18
FMCG	0.20	0.34	2.01	6.81	5.89	2.47	1.58	-2.75	0.97	-0.86	3.58	6.84	-2.81
Finance	-4.50	-0.60	-0.08	9.05	2.13	1.97	3.16	-2.64	1.08	-3.09	4.82	6.92	-2.40
Healthcare	-2.35	-4.66	1.31	6.33	2.81	9.71	7.45	0.57	2.45	-4.30	10.92	3.87	7.18
IT	3.43	-0.57	-3.15	-0.13	6.70	2.16	1.34	4.13	2.62	-3.13	6.77	8.38	3.74
Infra	-4.78	-5.56	4.24	6.06	0.89	4.51	10.73	1.64	8.45	-3.38	10.40	14.88	18.15
Metal	1.43	-10.40	1.04	7.21	-2.94	3.99	7.88	-1.64	7.45	-4.17	8.74	11.35	-0.85
Oil & Gas	-9.25	-13.17	2.77	6.39	-1.64	0.27	6.67	-5.03	1.23	-4.17	12.51	12.02	12.57
Power	-10.84	-18.60	9.39	5.37	2.01	4.33	9.20	-0.63	5.96	-4.90	11.16	18.24	8.57
Realty	-4.85	-3.09	-1.60	19.64	7.67	9.35	9.01	-1.50	5.21	3.70	19.99	9.37	9.37
Telecom	-7.13	-0.47	-3.65	8.44	4.12	9.08	5.61	3.20	10.55	-5.69	7.21	6.15	6.94
Utilities	-12.89	-21.37	10.02	6.22	-0.59	5.02	10.36	-0.64	7.20	-3.98	11.85	20.00	9.71

The abovementioned sectoral indices pertain to the S&P BSE universe

Colour scales assigned vertically

Source: Ace MF, HDFC Bank Research

Classification - Public

Key concerns for Indian equities

- Tepid management commentary for Indian corporates
- Results of the Indian General Elections
- Upward pressure on food inflation (El Nino, export restrictions by some nations)
- Volatility in commodity prices, especially Crude Oil
- Rising tensions in Middle East
- Movement of global liquidity
- The impact of Dollar Index and US Bond Yields on FPI flows in emerging markets
- Economic slowdown fears in developed markets

Classification - Public

Fixed Income Market

Classification - Public

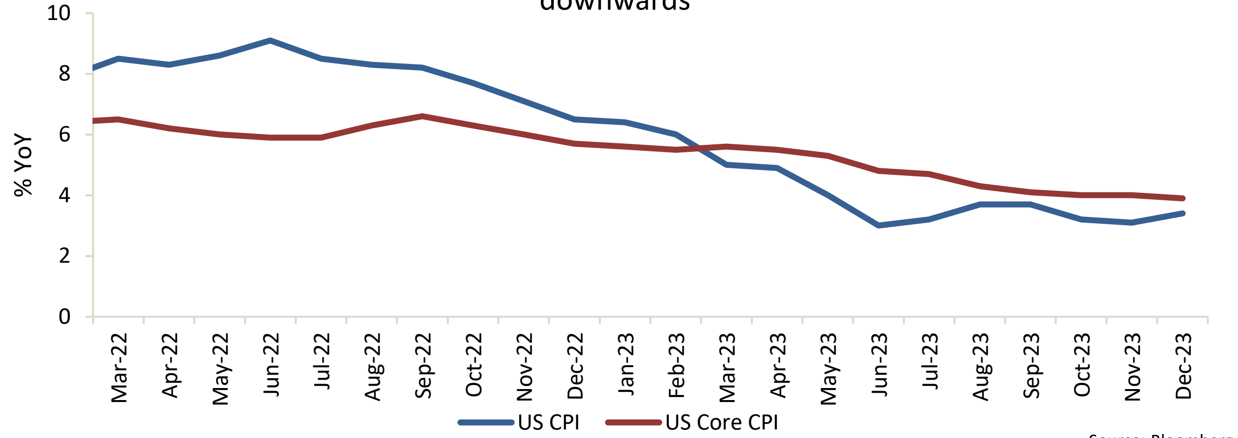
Fixed Income Outlook

- Liquidity remains in deficit due to tax outflows, a lack of government spending moving into the system and the RBI's stance of 'removal of accommodation'. Furthermore, before moving for the rate cuts, the RBI may ease liquidity into the system. In addition to this, the move from the Fed on liquidity is also likely to affect the RBI's view on liquidity. Going forward, with the inclusion of G-secs in JPMorgan's Government Bond Index-Emerging Markets, liquidity is likely to improve unless the RBI decides to sterilize the inflows.
- Headline inflation accelerated to 5.69% YoY in December 2023 primarily due to low base and elevated food inflation. Going forward, more upside risks are emerging on food prices as Rabi sowing may fall short of the target due to low reservoir levels, patchy rains, and a low base. The Red Sea crisis have further accentuated the risk to inflation as freight charges are increasing due to longer route taken by the ships, which may adversely affect the commodity prices. While headline inflation print in the upcoming months may witness a slight uptick on the back of higher food prices and low base, over the course of the year, inflation is expected to be contained within the tolerance band (2%-6%) of the RBI.
- India's trade deficit continues to narrow as festival driven import demand has started to come off. At the same time, India's exports are struggling on account of demand slowdown in Western countries and geopolitical tensions. The outlook of the trade deficit is likely to depend on the ability of the manufacturing sector (engineering goods manufacturers) to drive higher exports.
- Net FDI inflows declined in the current fiscal year on the back of moderation in gross FDI and an increase in repatriation. Currently, FPI and FII inflows are providing support to the INR. In the long term, the inclusion of Indian G-secs in global bond indices is likely to have positive implications for INR. The Balance of Payments' situation is likely to be impacted by movements in FDI, FPI, and net inward remittances.
- With the global rate cycle peaking, domestic monetary policy is likely to witness rate cuts in CY24. However, the robust domestic growth and elevated inflation may lead to shallow and back-ended rate cuts.
- India continues to remain on its fiscal consolidation path with the interim budget targeting fiscal deficit of 5.1% of GDP for FY25 and a revised fiscal deficit target of 5.8% of GDP for FY24, which is lower than the budgeted estimate of 5.9% of GDP. In FY24, the lower fiscal deficit was achieved on the back of robust tax collection, non-tax revenue (dividend income) and some cut-back on capex front. This was better than expectations and has been positive for the bond market.
- The US FOMC kept the policy rate unchanged while pushing the rate cut expectation away from March 2024. While the current rate hiking cycle has peaked, the quantum and timing of rate cuts are still uncertain. Going forward, the US may have to also address the substantial fiscal challenges due to escalating debt in the future. Globally, the current rate hiking cycle seems to have peaked out, but the major central banks remain inclined to bring down inflation close to their threshold values. For this reason, future policy decisions are likely to be data-dependent.
- Domestically, post the announcement of interim budget, the yields at longer end have been weighed down due to lower-than-expected fiscal deficit estimates of 5.1% of GDP for FY25. However, the yields at the short-end of the curve would be determined by the availability of liquidity, which at the current juncture remains under pressure.
- Corporate Bond Funds, which typically have a higher yield to maturities, look a safe bet at the current juncture. Additionally, with tight liquidity and a higher supply of corporate bonds and SDLs, the corporate bond spreads and SDL spreads are attractive vs the G-secs, thus providing accrual opportunity, and making the case for Corporate Bond Funds and SDL Index Funds.
- Hence, investors can look at Corporate Bond Funds and Short duration funds for a horizon of 15 months and above.
- Investors who are comfortable with volatility and have a longer horizon of 24 months and above can take exposure to Dynamic Bond Funds and longer-tenor SDL Index Funds to play the improved fiscal deficit dynamics.
- For lower volatility and a horizon of 3 months and above, investors can consider Arbitrage Funds. Whereas for a horizon of up to 3 months, investors can consider Overnight Funds and Liquid Funds.
- Investors can also look at Multi-asset allocation funds for a horizon of 36 months and above. Investors should invest in line with their risk profile and product suitability.

Classification - Public

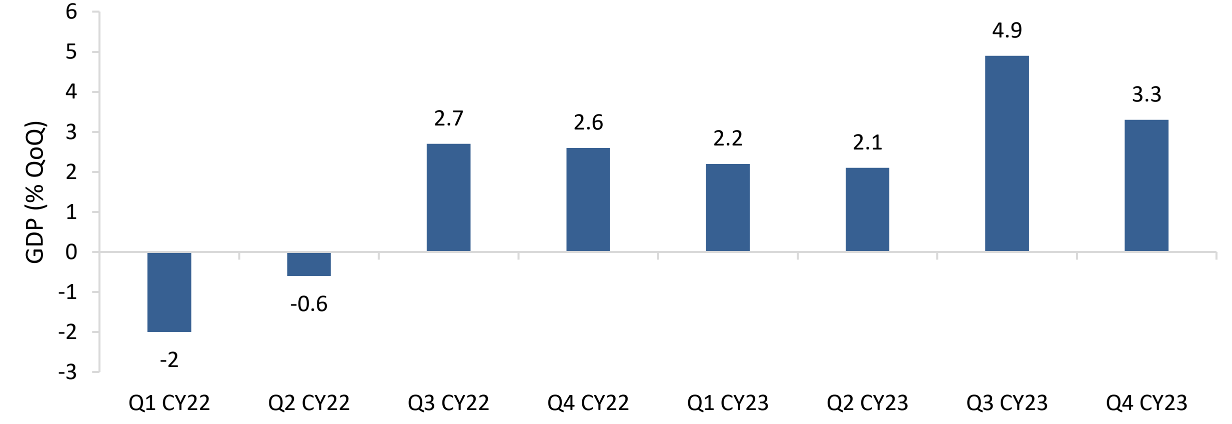
Higher than expected inflation and robust economy pulled the yields up in US

While the headline inflation picked up, the core inflation continues to trend downwards



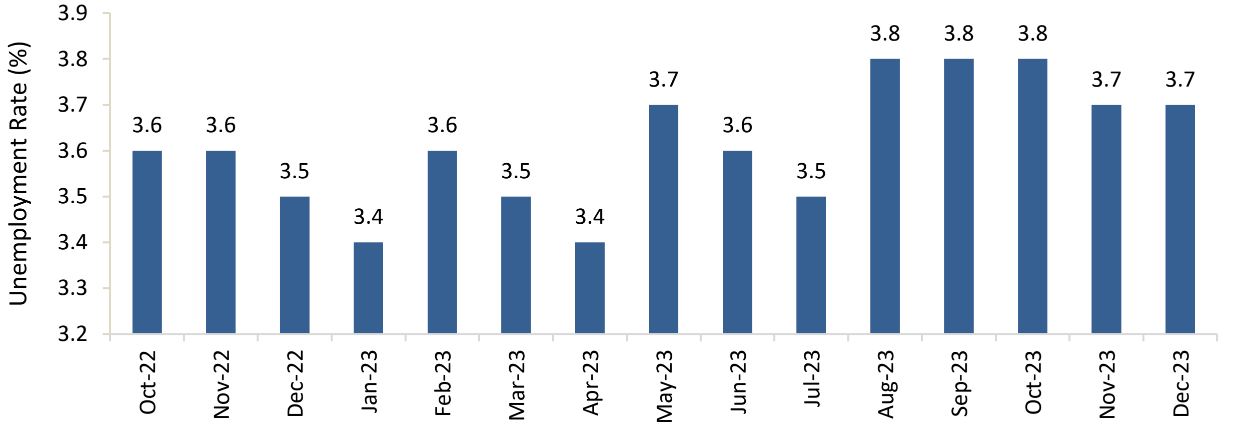
Source: Bloomberg

US economy continues to surprise on the upside



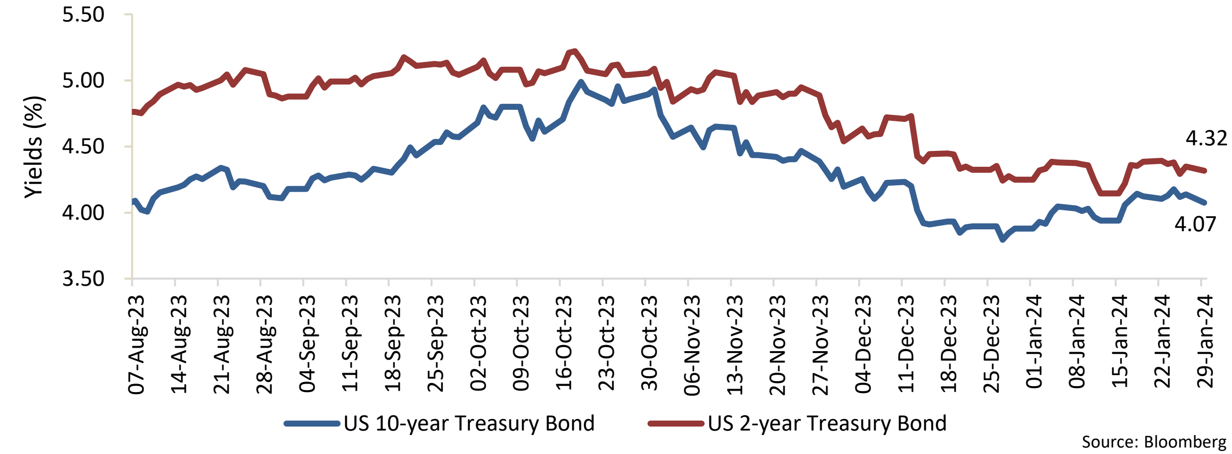
Source: Bloomberg

US jobs market remains tight



Source: Bloomberg

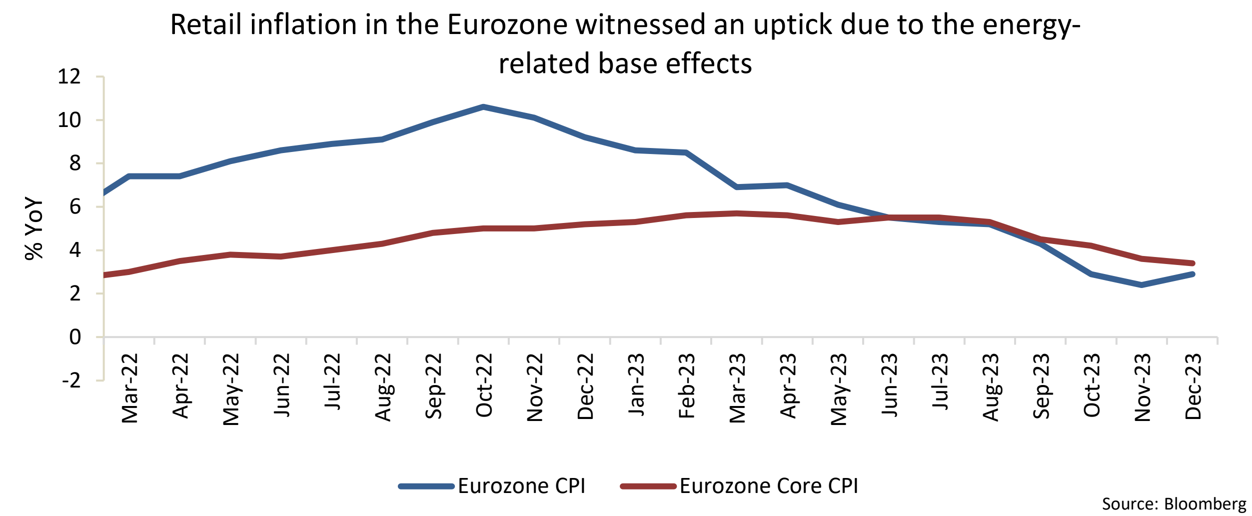
After falling post December policy, US yields again moved up



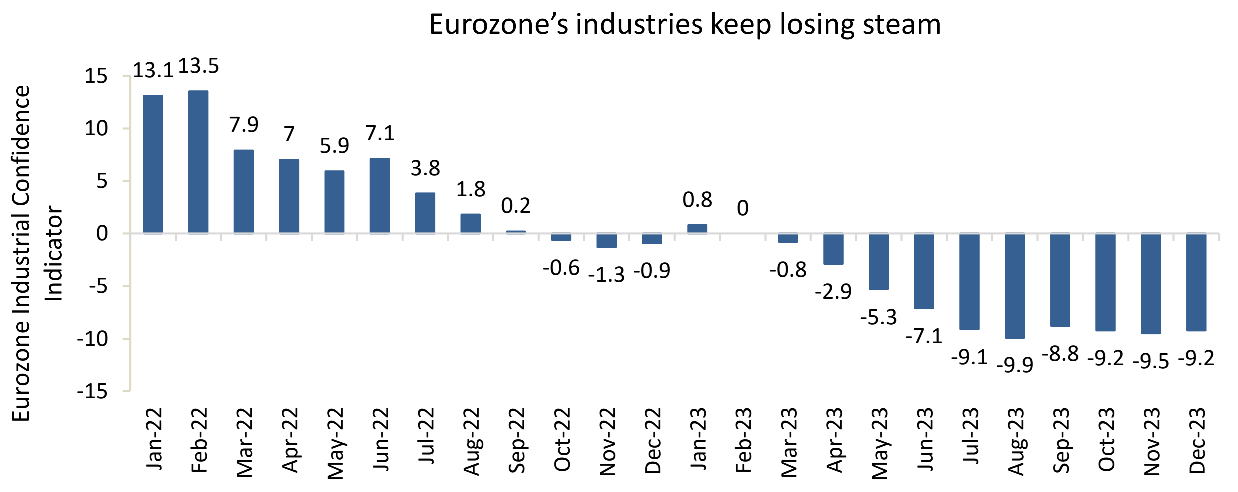
Source: Bloomberg

Classification - Public

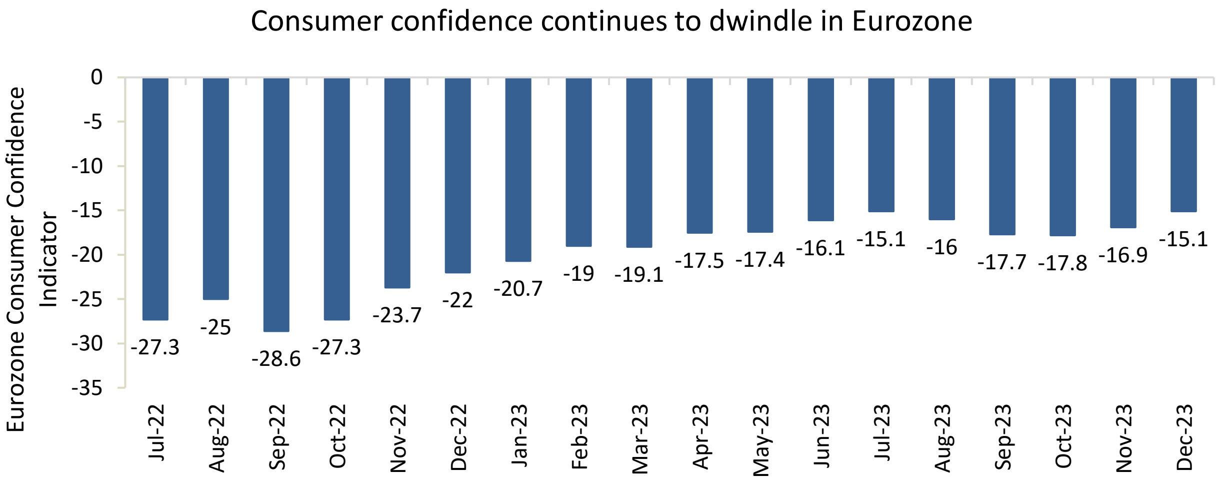
In Europe, while the economy is slowing down, the uptick in inflation kept the yields flat



Source: Bloomberg



Source: Bloomberg



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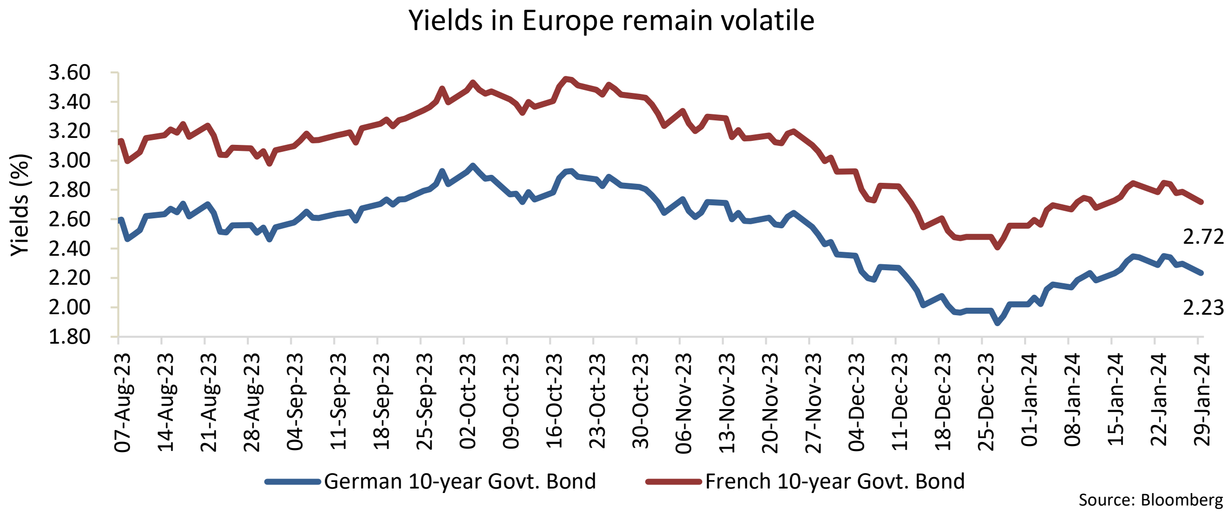

Source: Bloomberg

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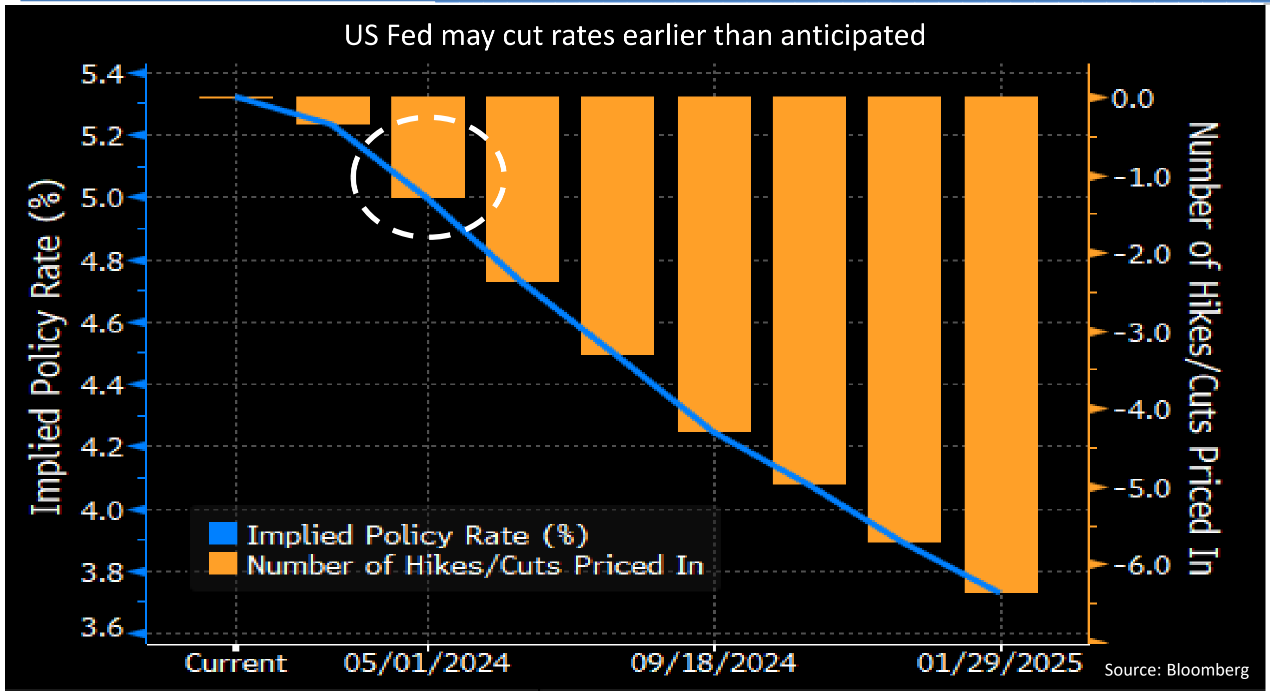
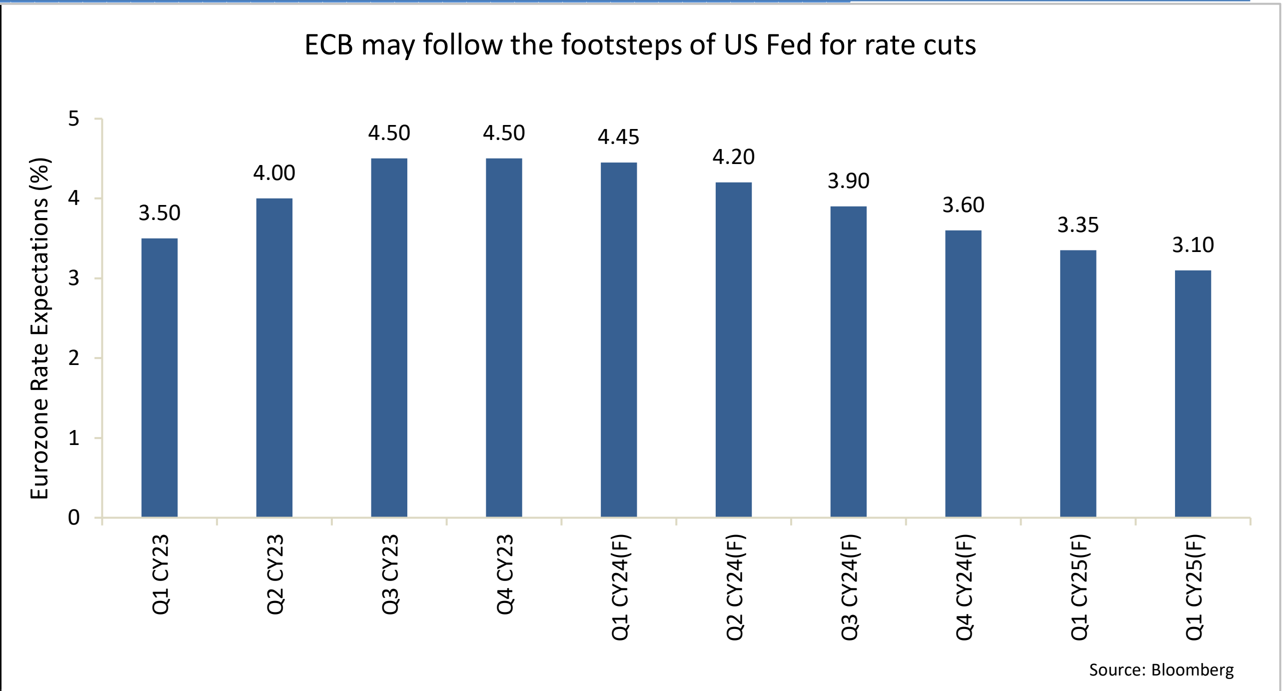
Classification - Public

US FOMC has pushed the rate cuts expectations away from March 2024





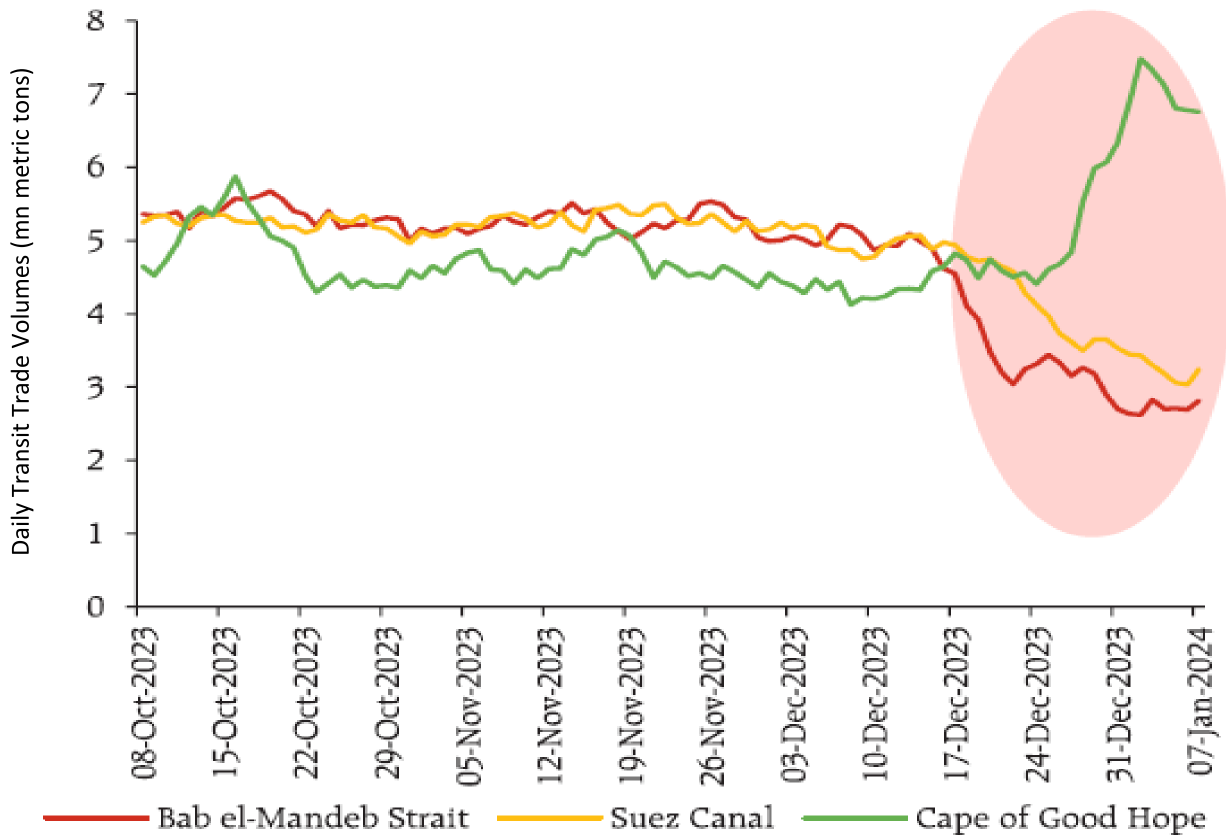
"Based on the meeting today, I would tell you that I don't think it's likely that the committee will reach a level of confidence by the time of the March meeting to identify March is the time to do that… But that's to be seen."

"The lower inflation readings over the second half of last year are welcome, but we will need to see continuing evidence to build confidence that inflation is moving down sustainably toward our goal."

- Fed Chairman Jerome Powell after FOMC Meeting (Jan 30–31, 2024)

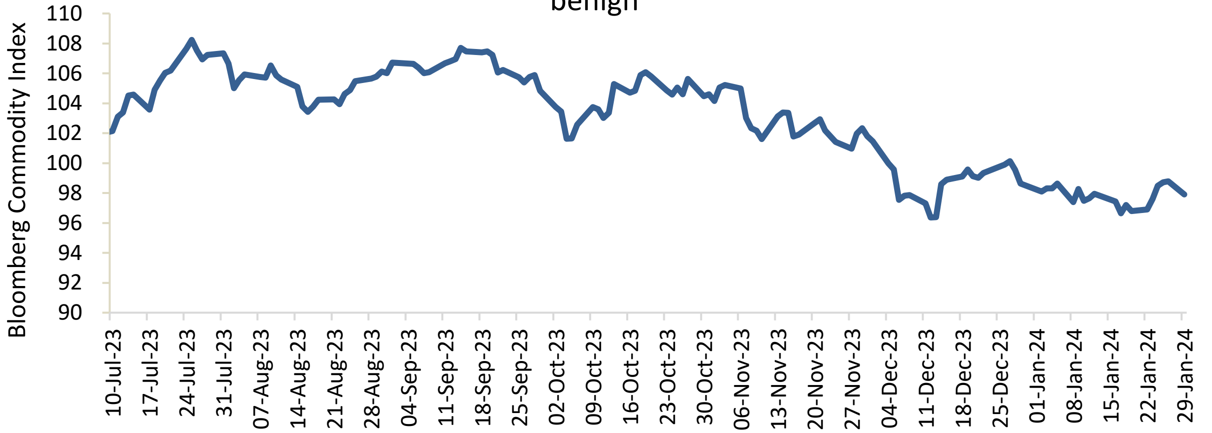
Red Sea conflict poses a threat to inflation

Disruptions in the Red Sea pushing transit through longer routes, leading to higher freight charges



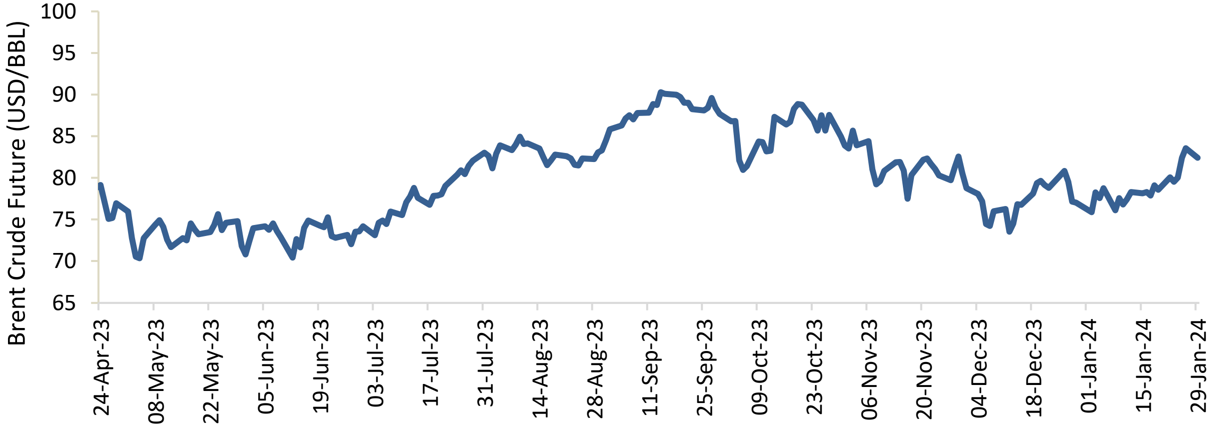
Note: Data are 7-day moving averages.
Source: RBI; IMF PortWatch

Despite geopolitical tensions, lower demand keeping commodity prices benign



Source: Bloomberg

Red Sea crisis has pushed the crude oil prices upward



Source: Bloomberg

Classification - Public

Interim budget surprised the market with lower-than-expected fiscal deficit

Particular	INR bn				%GDP			
	FY23	FY24 (BE)	FY24 (RE)	FY25 (BE)	FY23	FY24 (BE)	FY24 (RE)	FY25 (BE)
Nominal GDP	**2,72,407**	**3,01,751**	**2,96,577**	**3,27,718**				
Revenue receipt	23,832	26,323	26,997	30,013	8.7	8.7	9.1	9.2
Tax (net)	20,978	23,306	23,239	26,016	7.7	7.7	7.8	7.9
Non-tax	2,854	3,017	3,758	3,997	1.0	1.0	1.3	1.2
Capital receipt	722	840	560	790	0.3	0.3	0.2	0.2
Total receipt	**24,554**	**27,163**	**27,557**	**30,803**	**9.0**	**9.0**	**9.3**	**9.4**
Revenue expenditure	34,531	35,021	35,402	36,547	12.7	11.6	11.9	11.2
Capital expenditure	7,400	10,010	9,502	11,111	2.7	3.3	3.2	3.4
Total expenditure	**41,932**	**45,031**	**44,905**	**47,658**	**15.4**	**14.9**	**15.1**	**14.5**
Fiscal deficit	**17,378**	**17,868**	**17,348**	**16,855**	**6.4**	**5.9**	**5.8**	**5.1**
Centre's borrowing mathematics								
Gross borrowings	**14,210**	**15,430**	**15,430**	**14,130**	**5.2**	**5.1**	**5.2**	**4.3**
of which Repayments	3,127	3,621	3,625	2,378	1.1	1.2	1.2	0.7
Net Market Borrowings	**11,083**	**11,809**	**11,805**	**11,752**	**4.1**	**3.9**	**4.0**	**3.6**

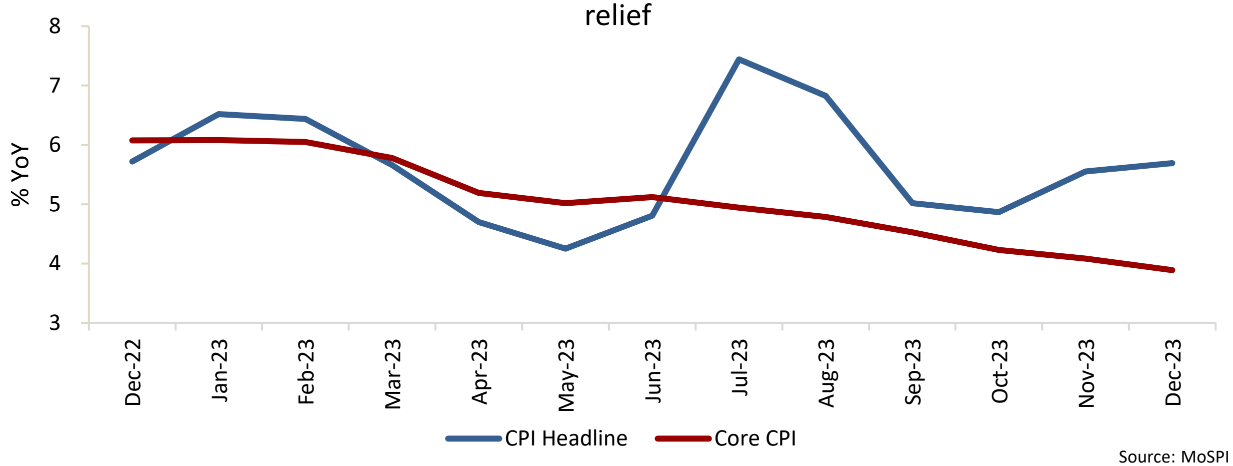
Note: Red colour means negative surprise, Green colour means positive surprise and Orange colour means in-line with expectations

Source: Indiabudget.gov.in

Classification - Public

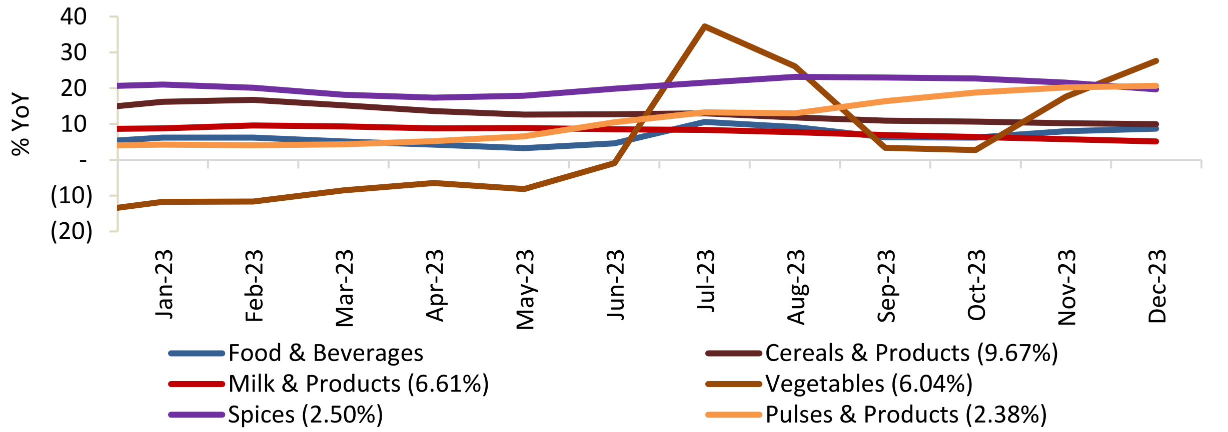
Domestic inflation remains elevated due to low base and higher food inflation

Headline inflation continues to trend upwards but core inflation providing relief



Source: MoSPI

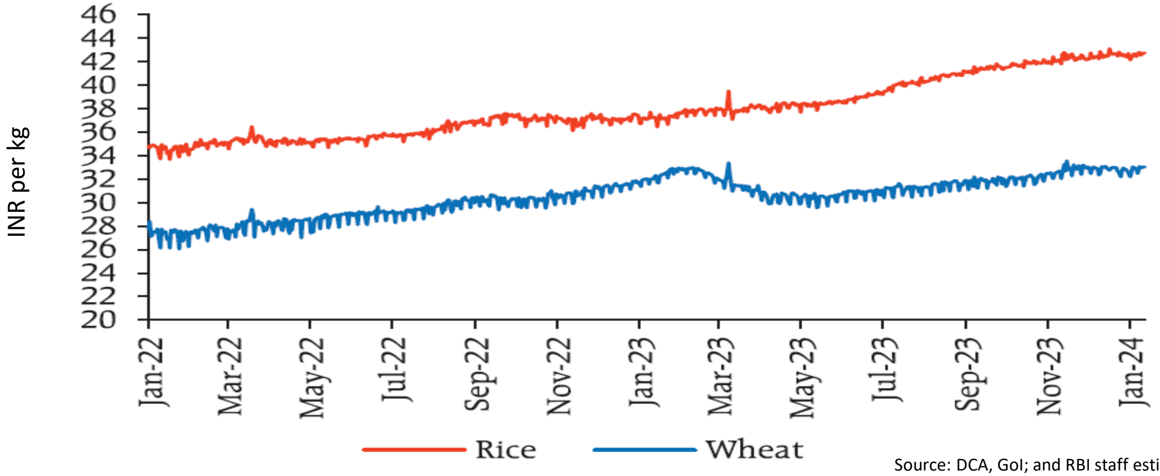
Food inflation pushing the retail inflation higher



Note: Data in parenthesis denotes weight of category in CPI basket

Source: MoSPI

Higher cereal prices pose threat to inflation

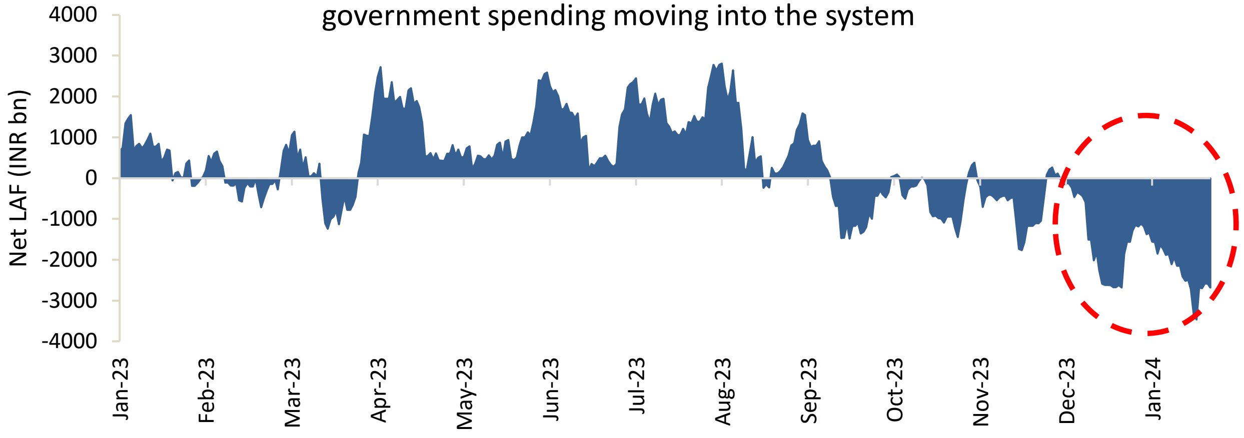


Source: DCA, GoI; and RBI staff estimates

Classification - Public

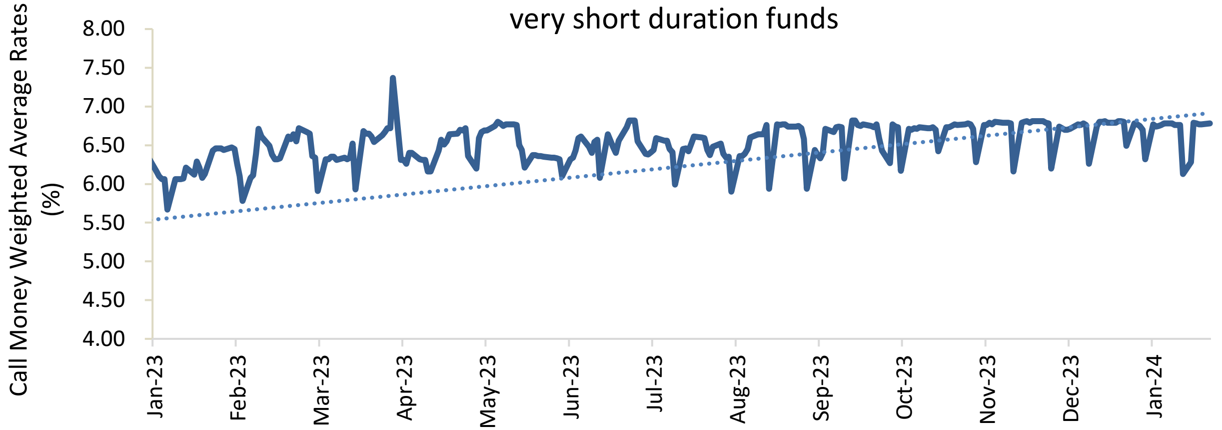
Banking system liquidity remains in deficit; the RBI is conducting VRR auctions to infuse temporary liquidity

Liquidity remained in deep deficit due to tax outflows and lack of government spending moving into the system



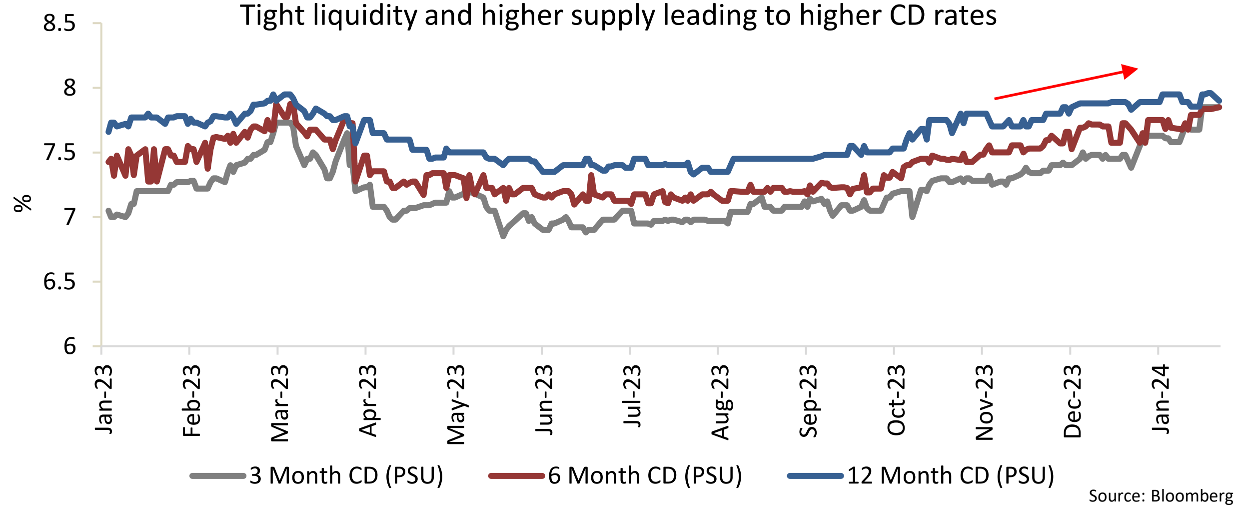
Source: Bloomberg

Liquidity tightening pushes call money market rate up making the case for very short duration funds



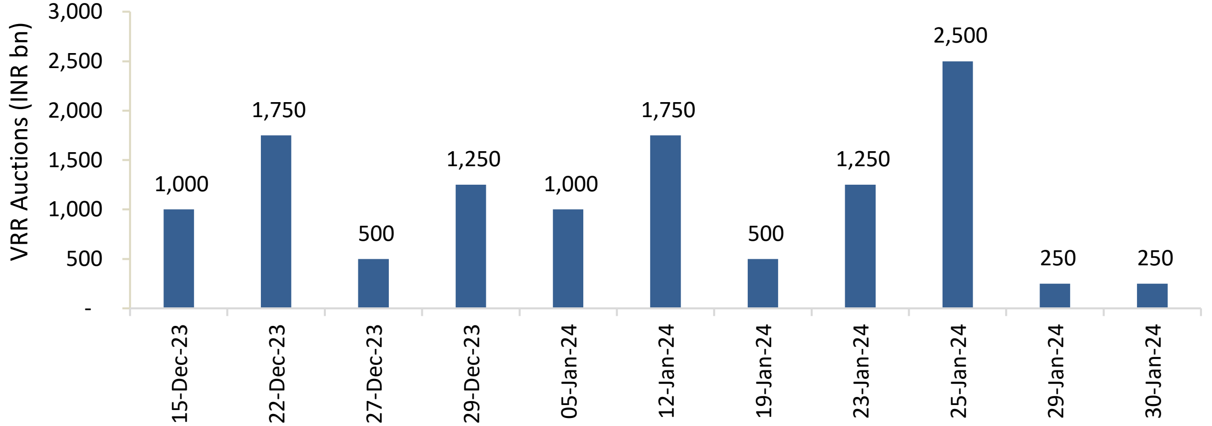
Source: Bloomberg

Tight liquidity and higher supply leading to higher CD rates



Source: Bloomberg

RBI infusing temporary liquidity via VRR route

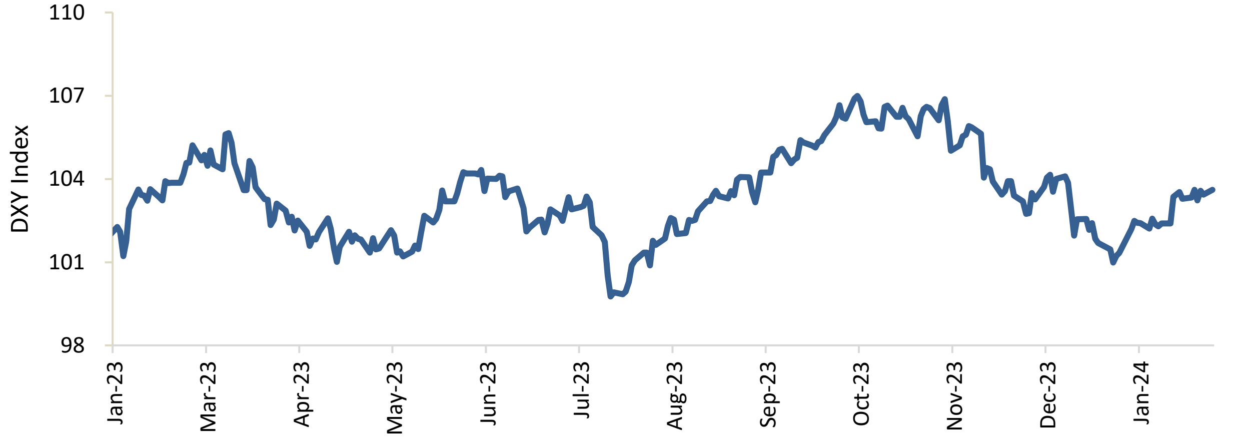


Source: RBI

Classification - Public

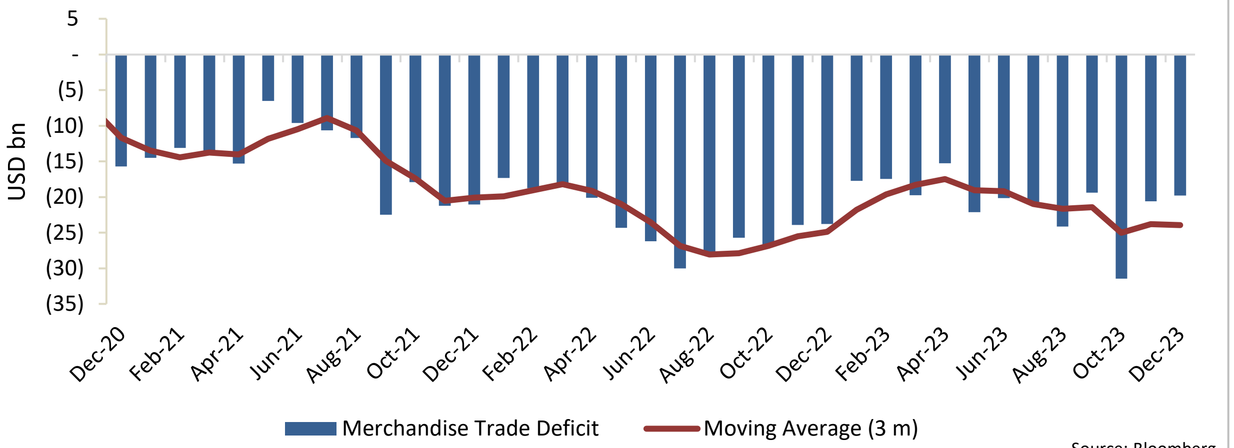
Despite strong dollar index, INR remained well balanced due to moderation in trade deficit

With rate cut expectations subsiding, Dollar Index regained strength



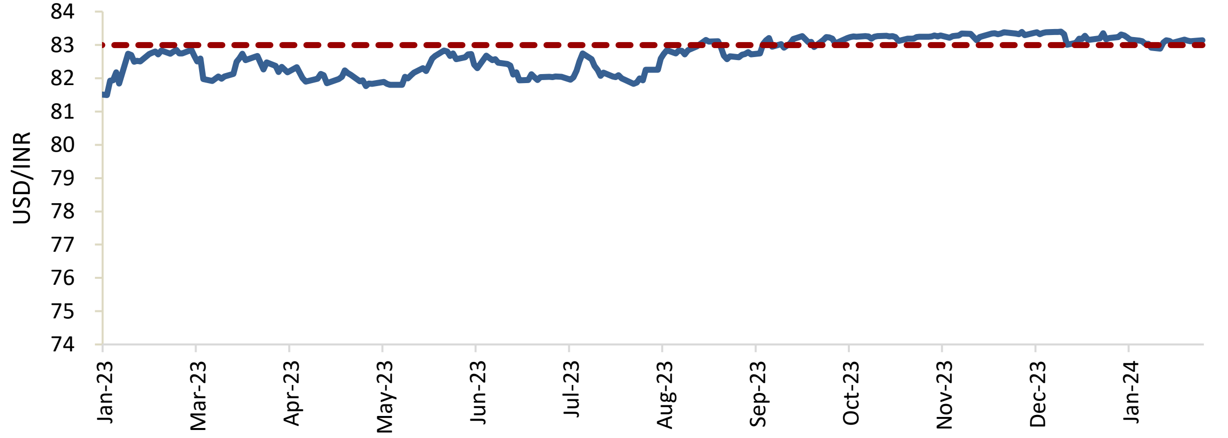
Source: Bloomberg

Trade deficit contracted on the back of slowing imports



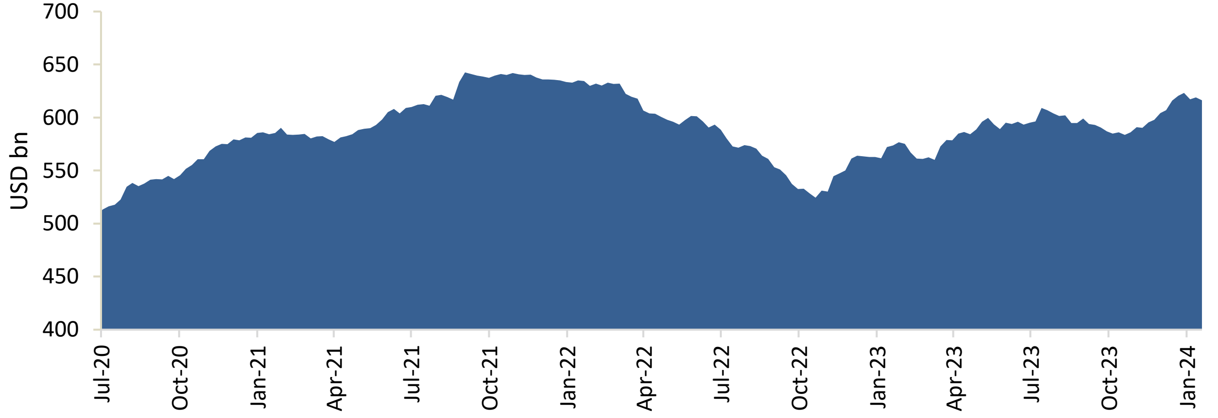
Source: Bloomberg

External sector continues to keep INR well balanced



Source: Bloomberg

Comfortable forex reserves providing further support to INR

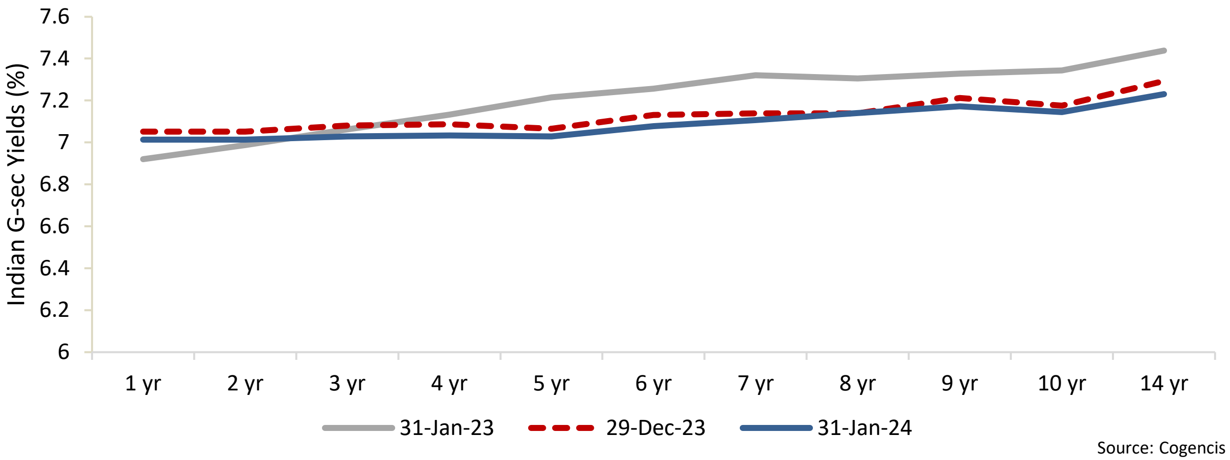


Source: Cogencis

Classification - Public

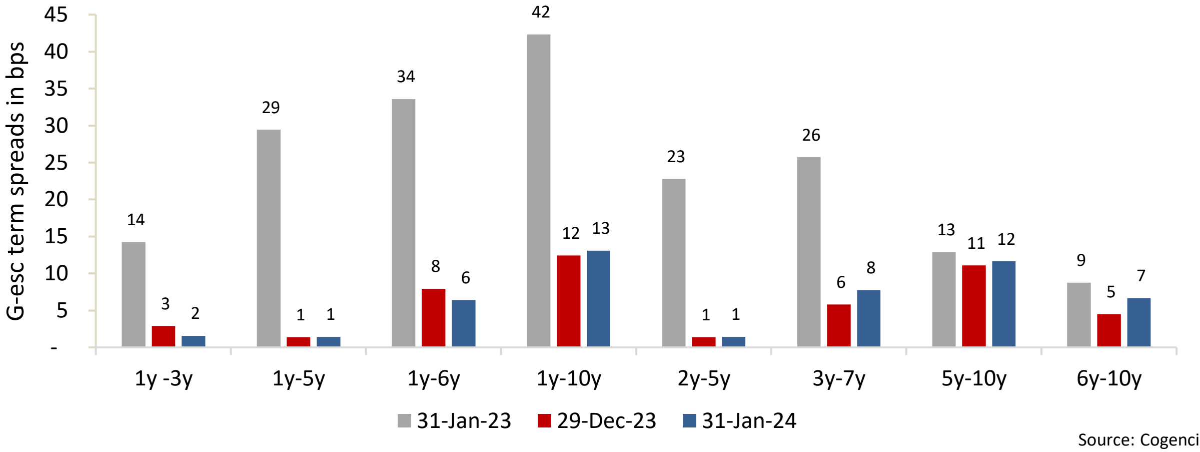
Peaking of rate hiking cycle and rate cut expectations have pulled the G-sec yields down

Yield curve has witnessed a parallel downward shift



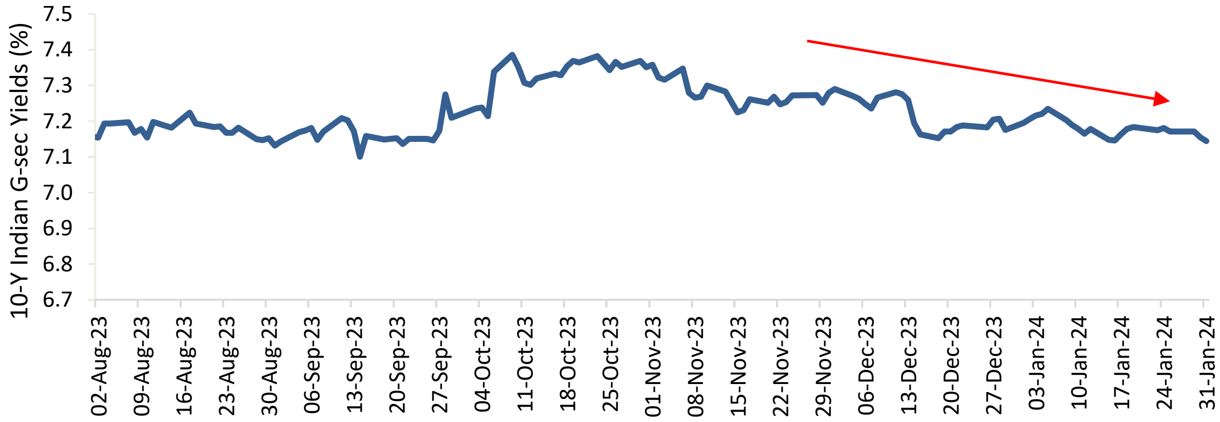
Source: Cogencis

Yield curve continues to remain relatively flat



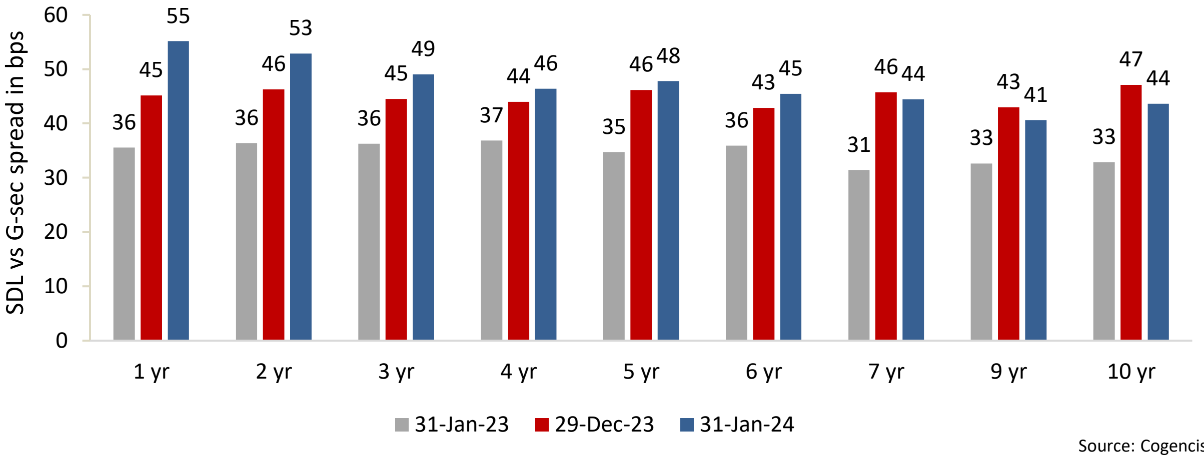
Source: Cogencis

G-sec yields moved lower



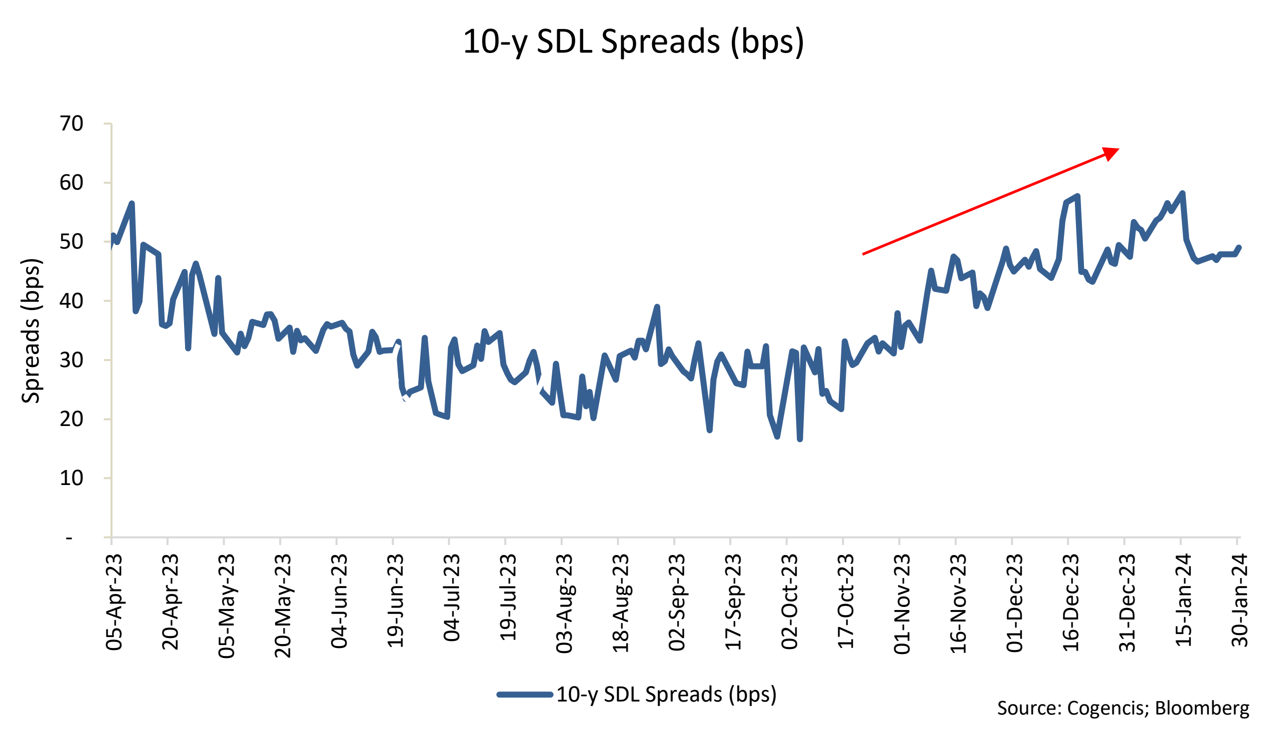
Source: Cogencis

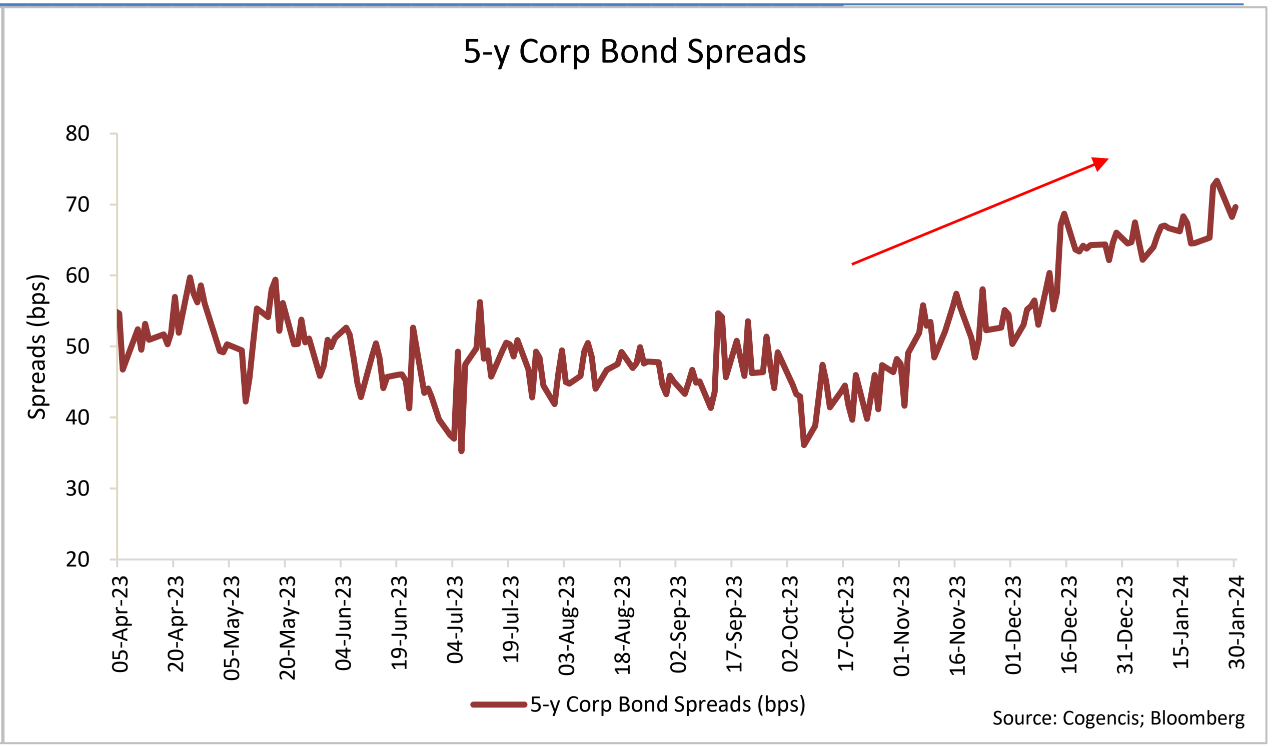
Higher supply has widened the SDL spreads



Source: Cogencis

Widening of SDL and Corporate Bond Spreads vs G-secs is providing opportunity in the accrual space





	03-Apr-23	03-Jul-23	01-Dec-23	30-Jan-24
10-y G-sec Yield (%)	7.31	7.12	7.29	7.16
10-y SDL Yield (%)	7.78	7.32	7.74	7.65
SDL Spreads (bps)	47	20	45	49

Source: Cogencis; Bloomberg

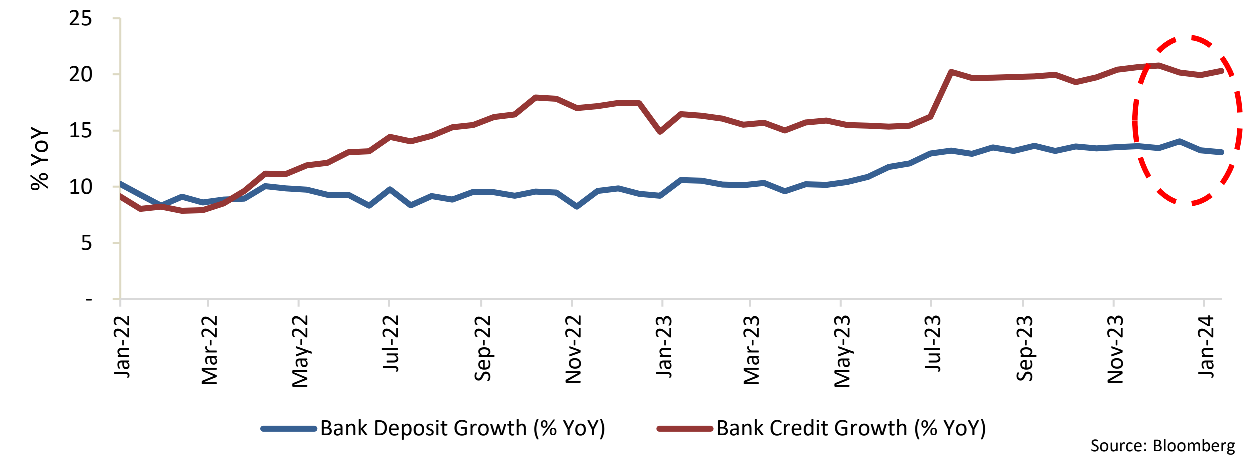
	03-Apr-23	03-Jul-23	01-Dec-23	30-Jan-24
5-y G-sec Yield (%)	7.17	7.09	7.27	7.03
5-y Corp Bond Yield (%)	7.73	7.46	7.78	7.73
Corp Bond Spreads (bps)	55	38	50	70

Source: Cogencis; Bloomberg

Classification - Public

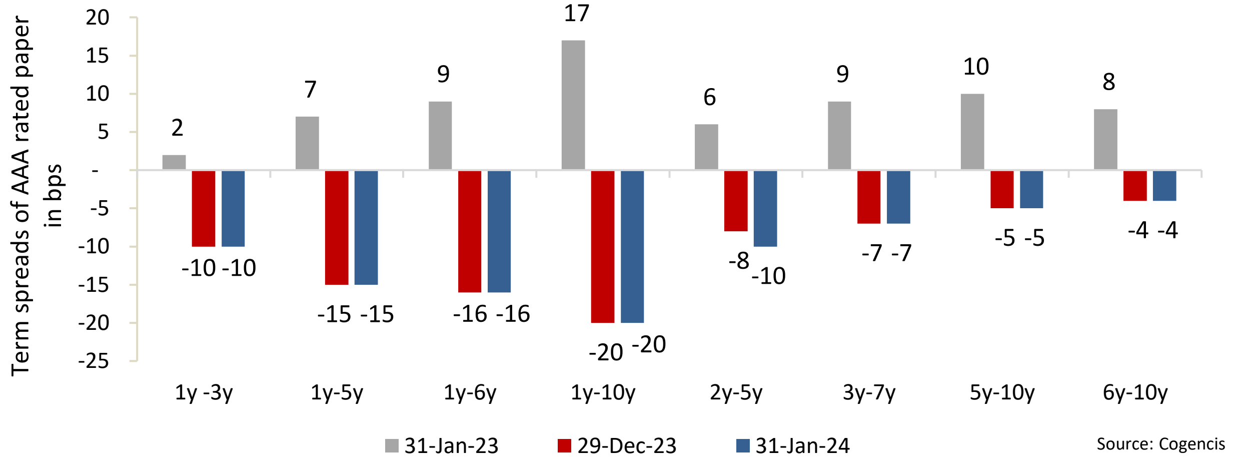
Strong demand for credit in a tight liquidity scenario may further push up the corporate bond spreads

Banks’ credit growth rate continues to outpace deposit growth rate



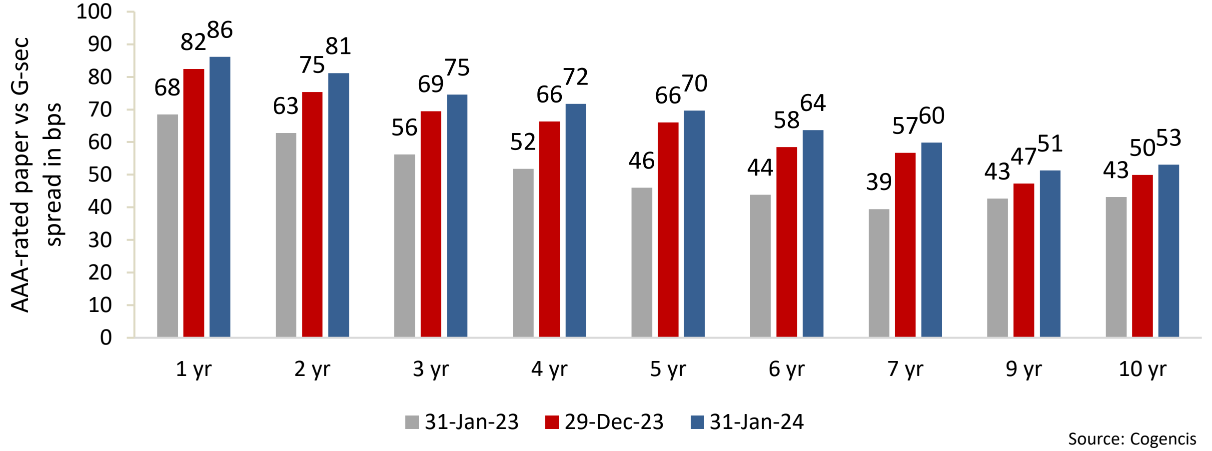
Source: Bloomberg

PSU term spreads remain flat over the past month



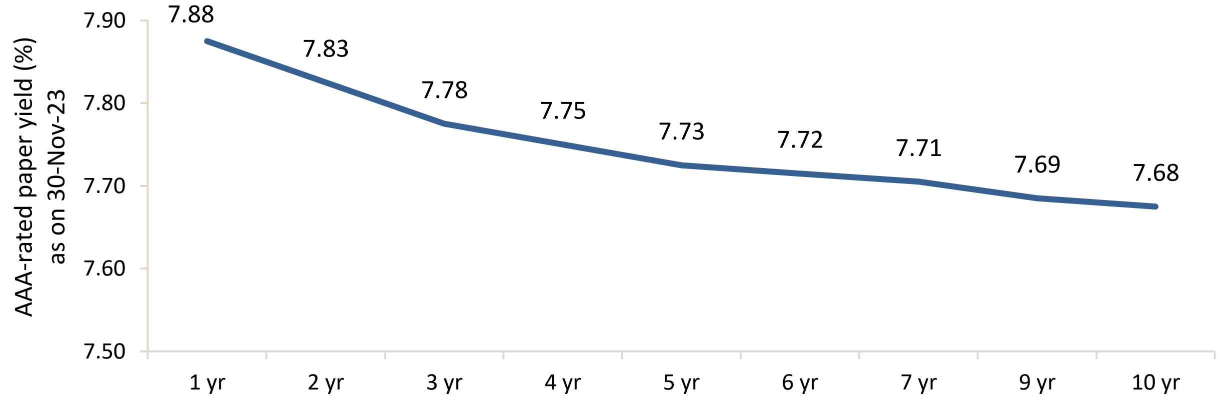
Source: Cogencis

Tight liquidity and higher supply have widened the corporate bond spreads



Source: Cogencis

Higher supply of short-term papers has inverted the corporate bond yield curve



Source: Cogencis

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