HDFC Bank – Research Presentation

May 2024

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	▲
Business Cycle 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	◆

Equity MF Strategy – May 2024

- The global economic growth has continued to show signs of robustness on the back of improved fundamentals, ample liquidity due to fiscal support by the governments, focus on improving manufacturing and infrastructure in key economies to improve their self-reliance in key sectors, away from China.
- Ample liquidity provided by the US Government's fiscal support has kept the US economy going. While interest rates in the US have peaked, the strong employment and inflation data is keeping the US fed from cutting the rates. Signs of steadiness are being witnessed in the incoming data on Manufacturing and Services. Some hiccup was seen in the GDP growth numbers, which needs to be monitored for any further follow through. 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.**
- Eurozone is showing early signs of stability due to easing of financial conditions, the continuation of which would be important. The ECB seems to be clearly hinting on cutting the interest rates as the inflationary pressure in the EU abates.
- While the GDP growth in China remains below expectations led by the issues in their Real Estate sector, some key data points are showing gradual recovery, such as growth in consumer spending and PMI. The Chinese economy is also witnessing fiscal and monetary support being provided by the Government. The Chinese government is also seemingly relaxing some policies to bring its real estate sector back from the slump. 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.
- With stable economic performance of the US and green shoots being witnessed in China, commodity prices are gradually seeing uptick from their recent lows; while the food price inflation globally is still weakening. The conflict in the Middle East and tight supply by OPEC+ members have driven volatility in crude oil prices. The trouble in the Red Sea is has led to the rise in logistics costs for businesses across the world. Rising industrial commodity prices and logistics costs can have a negative impact on margins of the consuming companies.
- Improved economic data from the US vs its peers and expectation of delay in policy rate cuts by the US Fed has led to uptick in the US dollar index, impacting foreign flows into the equity markets in the emerging economies.
- The overall economic indicators in India continued to remain strong. The GDP growth estimates have been upgraded by major multilateral agencies.
- Many of the key indicators like the strength in the real estate and construction activities bode well for rural economy, which has yet to fire completely. The unemployment rate for the rural labour also seems to be declining. With monsoons likely to be normal in FY25, the rural consumption can spring a positive surprise.
- Urban demand trends have remained stable where the premiumisation trend continues. Indicators like personal loan growth, high hotel occupancy rates, and air passenger traffic have been strong. Passenger vehicle sales growth, led by SUV's, too has held strong.
- Corporate and Banking sector balance sheets in India have shown strong improvement. The Corporate debt to equity remains low and as the current capacity utilisation peaks in various sectors, it is supporting to fund incremental 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 energy assets and focus on import substitution by Indian government, the capex cycle is expected to last long. The current cycle in the equity market seems to be largely driven by the capex upcycle and policy reforms by the Government and the fund managers playing this cycle have been able to create strong alpha. However, valuations in the capex related sectors/companies have become quite rich and further rerating looks a tough ask.
- While the liquidity conditions in India have been tight, due to the focus of the RBI on withdrawal of accommodation. As the liquidity conditions ease, the growth trajectory of the economy could see further bump up.
- The Equity markets have moved to near all-time highs on Key indices, led by stable earnings performance and strong Domestic investor participation. Small and Midcap indices have rallied sharply post the recent correction. At an aggregate level, the valuations of both Midcap and Smallcaps are markedly higher than Largecap indices.
- **The initial Q4FY24 results have seen weak performance in many key sectors, ex Banking. While we await the full results for the quarter, weakness in the Revenue growth and the Profit growth in key sectors may not be good news for investors. The differential of earnings performance between companies may see a gradual narrowing in the number of outperforming stocks in the equity market.**
- The result of the general elections in India, expected on 4th of June, and the speculations around it may be the single biggest factor impacting the investor sentiments in the near term. 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.
- **With Valuations still quite high, investment deployment strategy could be at 40% lumpsum and rest 60% to be staggered over the next 5-6 months. Investors can look to focus on categories like Largecap, Flexicap, Multicap, Equity Hybrid and Multi-asset funds. In the Smallcap segment, investors need to be cautious and use only large dips to invest. All allocations should be done in line with the risk profile and product suitability of the investor.**

Debt Mutual Fund Strategy

- With bond yields rising recently, investors who are comfortable with volatility and have a longer horizon of 24 months or above can take exposure to Dynamic Bond Funds and Gilt Funds to take advantage of improved fiscal deficit dynamics.
- Corporate Bond Funds, which typically have a higher yield to maturities, look a safe bet at the current juncture.
- Thus, investors can look at Corporate Bond Funds and Short duration funds for a horizon of 15 months and above.
- 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.

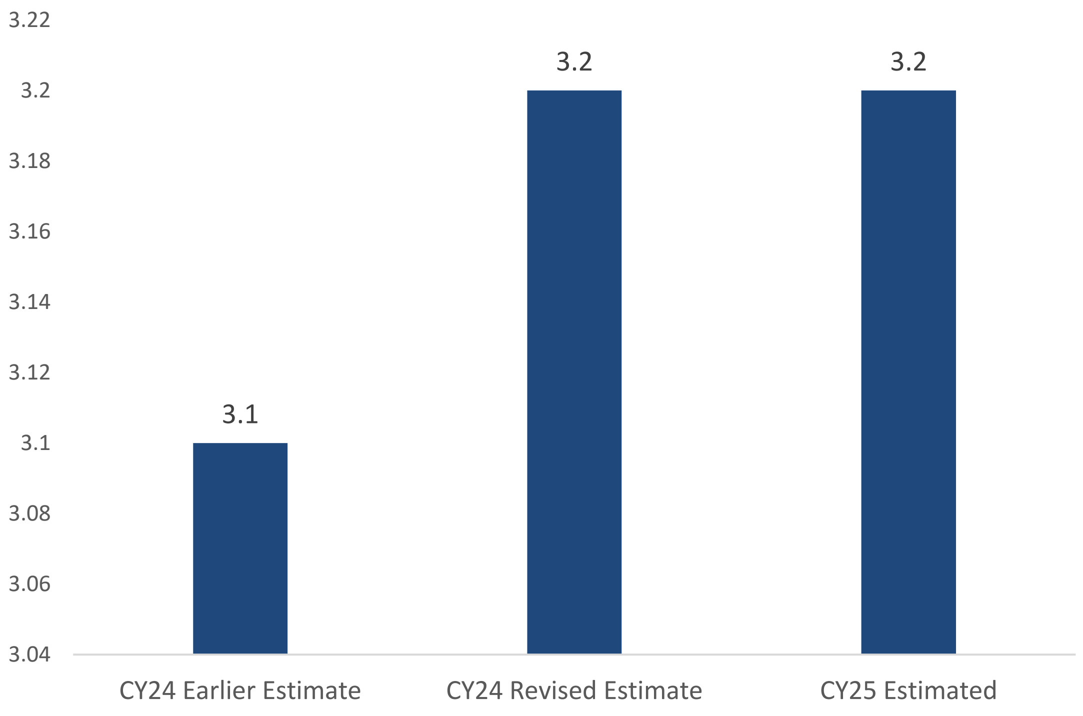
Research presentation – Content

- Global growth projections remain upbeat
- US – Rising inflation pushes back Fed rate cut expectations, driving market volatility
- Euro Zone – Weak, but improving
- China – Economic downgrade continues to be driven by real estate sector…green shoots visible… valuations cheap
- Commodities: Tensions in the Middle East drive volatility…improving global growth, a tailwind
- Uptick in the US dollar index, impacting foreign flows into the emerging economies
- Indian Equity Markets volatility driven by rising geopolitical risk, jump in Dollar Index leads to FPI outflows…Small cap index bounces back
- Sectoral performance and FPI flows in April 2024
- India – Macro indicators remain in fine shape
- Urban demand remains steady…
- Rural India : Improvement visible
- Capex continues to drive India's growth….
- Quarterly results
- General Elections - Key Variable
- India valuations – Elevated…Mid Cap & Small Cap valuations have bounced post the correction…Large Cap remains relatively reasonable
- Market Roundup – April 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 inflation pushed US Treasury yields higher…
- ….Leading to delay in rate cut cycle in the US
- Falling Yen and rising inflation are driving rate hikes in Japan
- Inflation pulses are back due to escalating geopolitical tensions and uptick in global growth
- While most of the central banks are on the verge of rate cuts, few central banks have raised rates
- Domestic inflation under control on account of softening of food prices and continuous decline in core inflation…
- … Expectations of normal monsoon to further pull down the food prices
- Liquidity continues to remain tight as the RBI ensures call rate remains around the repo rate
- Tax collection remains strong… supporting fiscal conditions
- Despite inflation remaining in control, yields rose, predominantly tracking the rise in US Treasury yields and FPI outflows
- Corporate bond spreads remained relatively higher while SDL spreads came off making SDL less attractive
- Disclaimer

Global growth projections remain upbeat

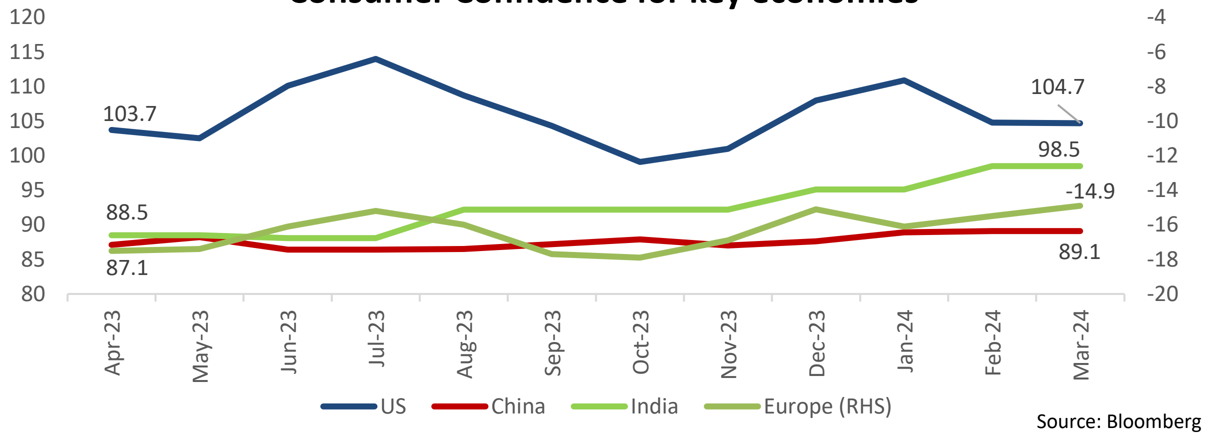
IMF's Global GDP growth projections

The IMF's outlook highlights the robustness of the global economic landscape



Source: IMF

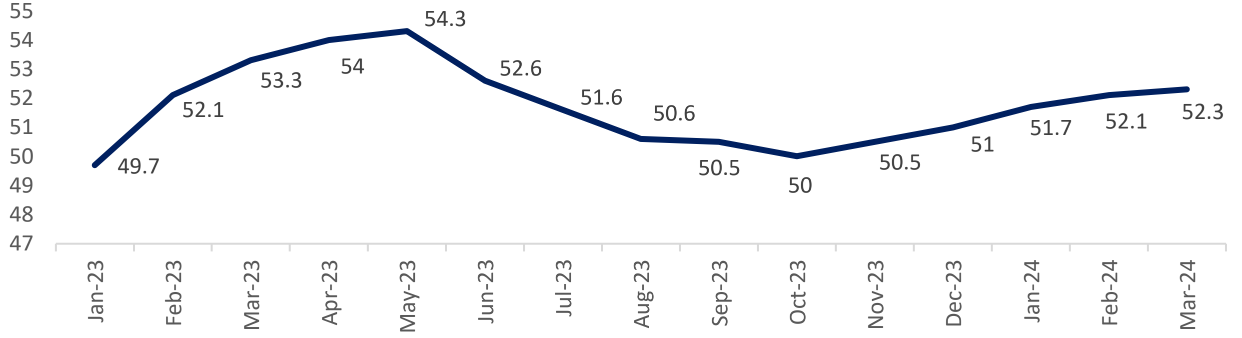
Consumer Confidence for key economies



Source: Bloomberg

JPMorgan Global Composite PMI

Global composite PMI in expansion zone led by strong Macro data across key economies

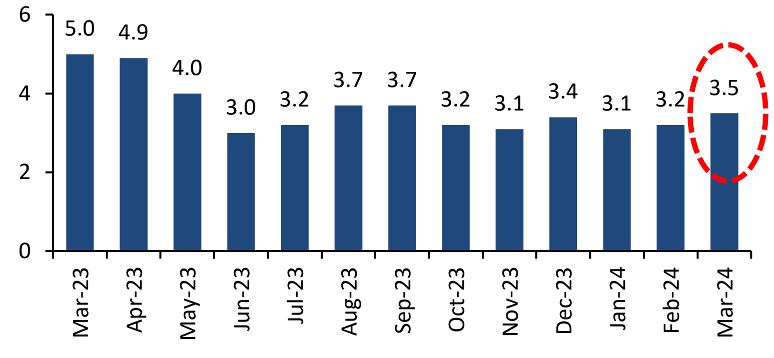


Source: Bloomberg

US – Rising inflation pushes back Fed rate cut expectations, driving market volatility

US CPI YoY (%)

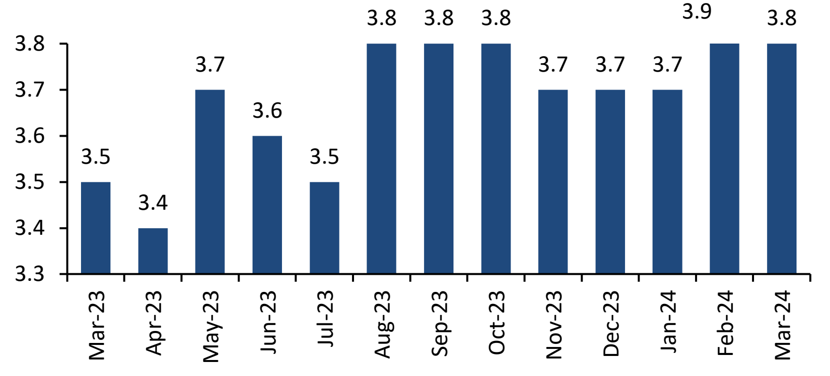
US inflation has surprised on the upside



Source: Bloomberg

US Unemployment Rate (%)

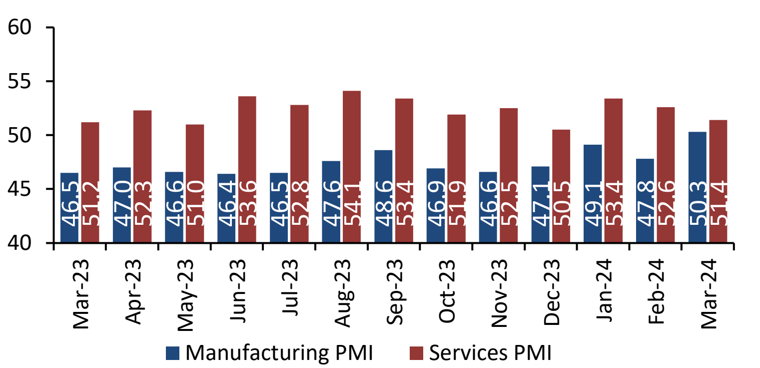
Labour market remains strong



Source: Bloomberg

US Manufacturing & Services PMI

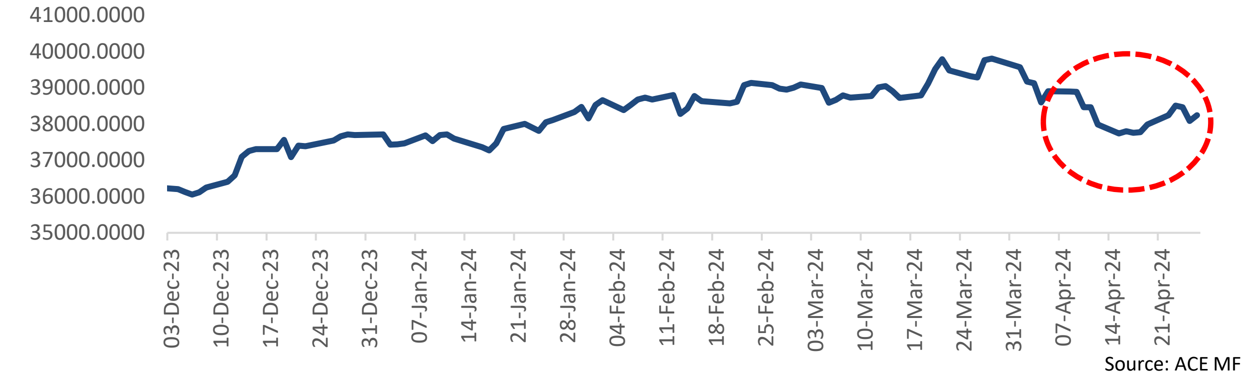
PMI activity remains in the expansion zone



Source: Bloomberg

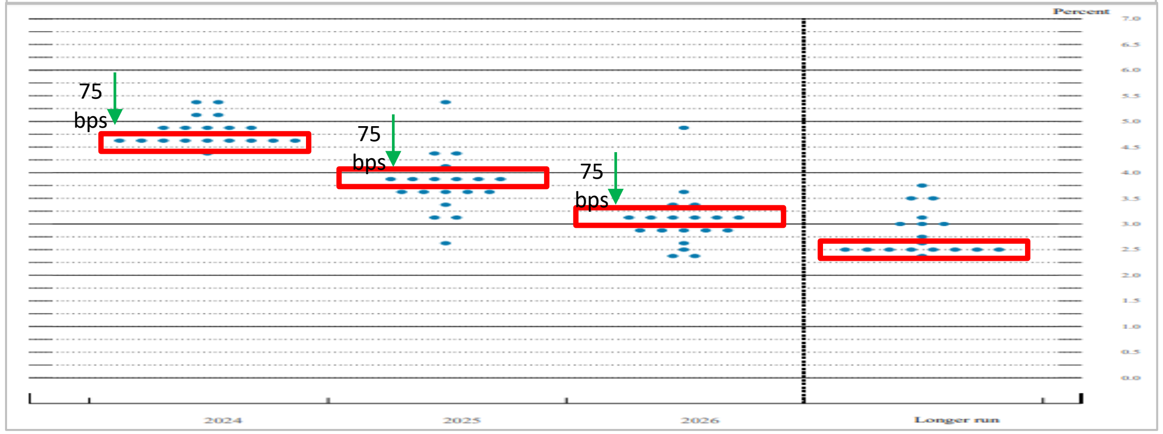
Dow Jones Industrial Average (DJIA) Movement

Delay in rate cuts has driven the equity market volatility in the month of April



Source: ACE MF

Fed's dot plot suggests 75 bps of rate cuts in CY24

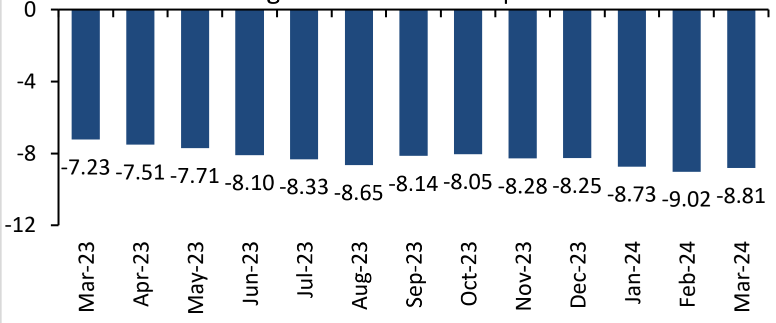


Source: Fed

Euro Zone – Weak, but improving

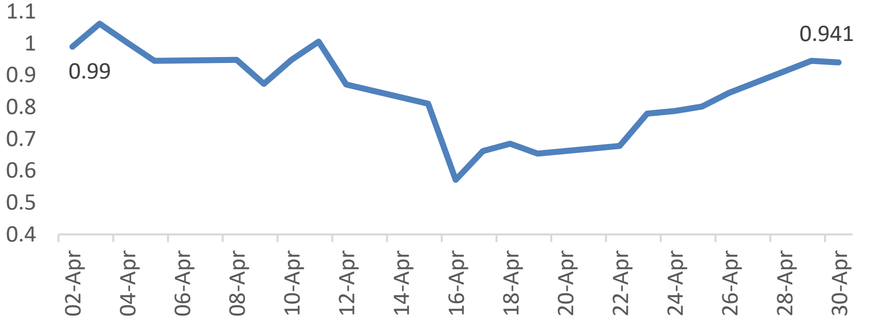
Eurozone Leading Economic Index YoY (%)

Headwinds to growth continue to persist



Source: Bloomberg

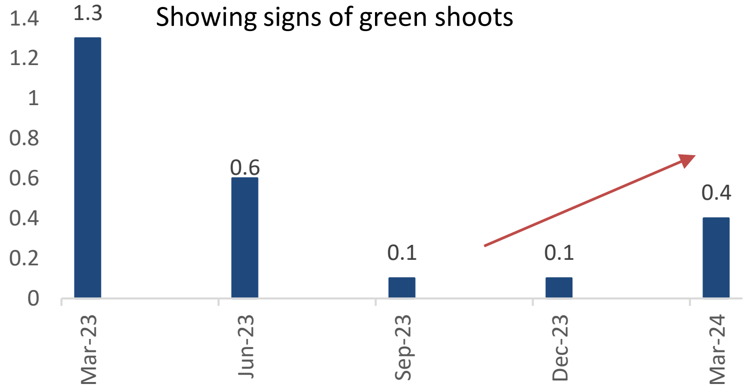
Euro Area Financial Conditions Index has seen improvement



Source: Bloomberg

Eurozone GDP YoY (%)

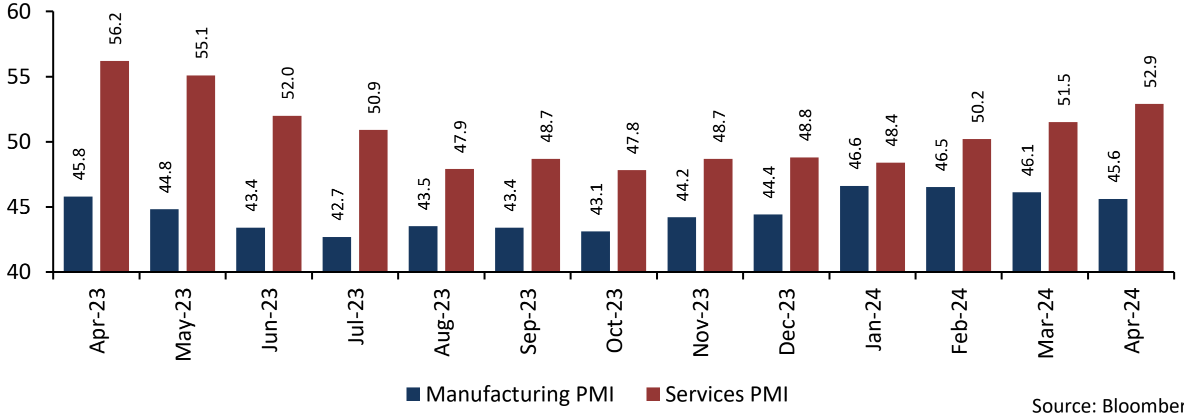
Showing signs of green shoots



Source: Bloomberg

S&P Global Eurozone PMI

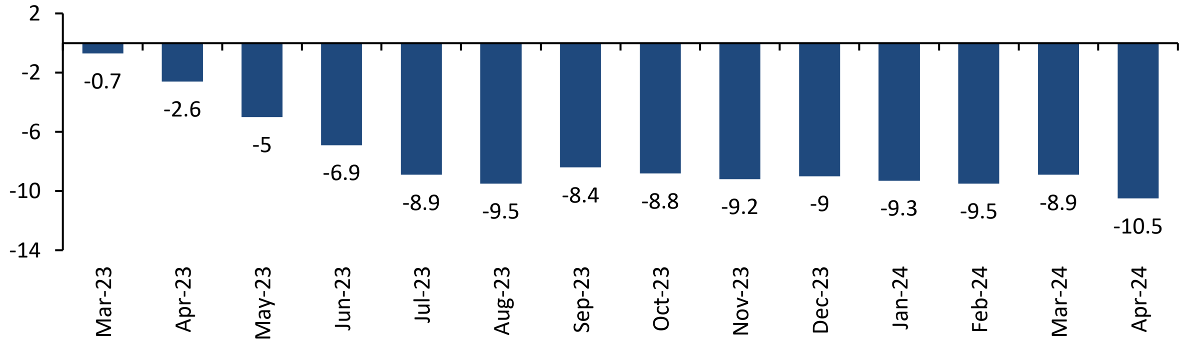
While Manufacturing PMI is weak, Services PMI uptick visible



Source: Bloomberg

Eurozone Industrial Confidence Indicator

Though business conditions have improved, it remains in negative territory



Source: Bloomberg

China – Economic downgrade continues to be driven by real estate sector… green shoots visible… valuations cheap

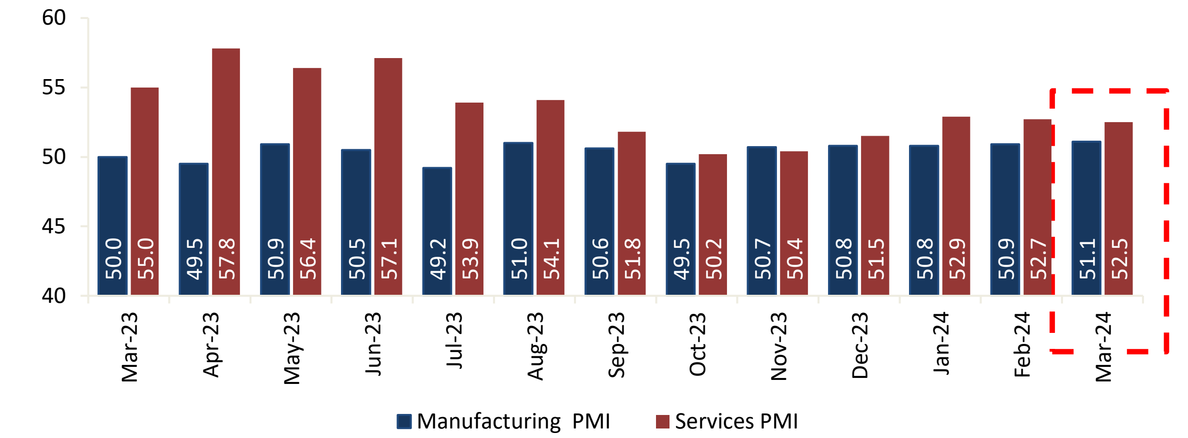
Rolling 1 year Forward P/E for Chinese Market

Valuations remain reasonable

Source: Bloomberg

China Manufacturing & Services PMI

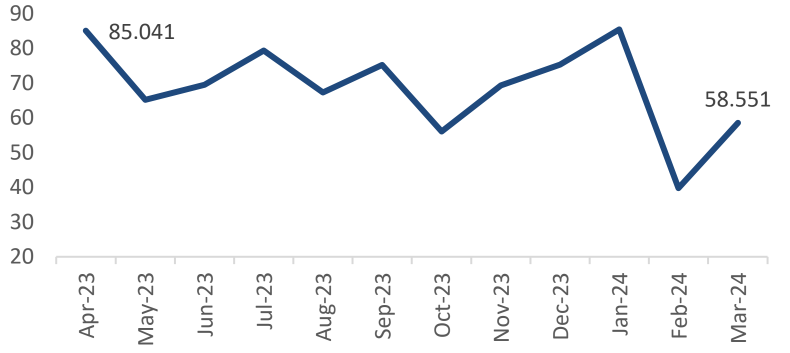
PMI remains in expansionary zone which is a positive sign for the economy



Source: Bloomberg

China Trade balance (USD Bn)

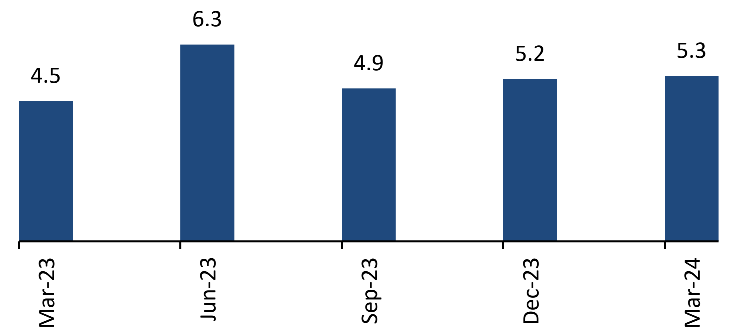
Steady performance continues



Source: Bloomberg

China Quarterly GDP - YoY Change (%)

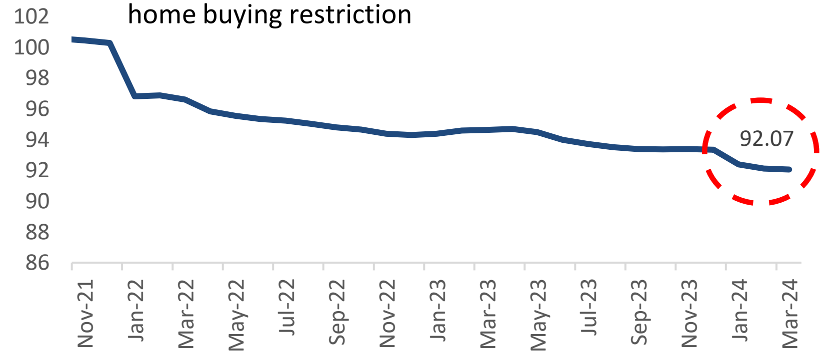
GDP growth holding up



Source: Bloomberg

China Real Estate Climate Indicator

Indicator weak, government supporting by removing home buying restriction

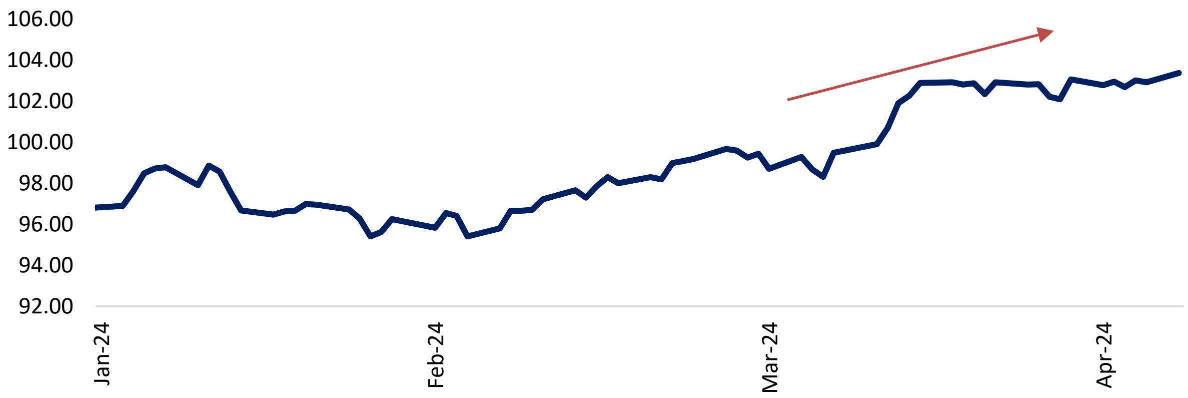


Source: Bloomberg

Commodities: Tensions in the Middle East drive volatility… improving global growth, a tailwind

Bloomberg Commodity Index

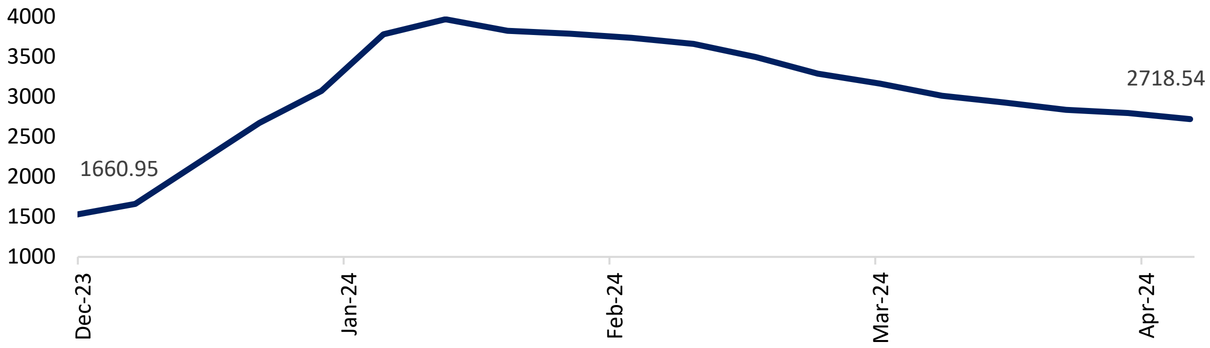
Improvement in global growth estimates pulling demand for metal



Source: Bloomberg

Drewry World Container Index per 40 Foot Box

Tensions in Red Sea is driving volatility in the frieght cost



Source: Bloomberg

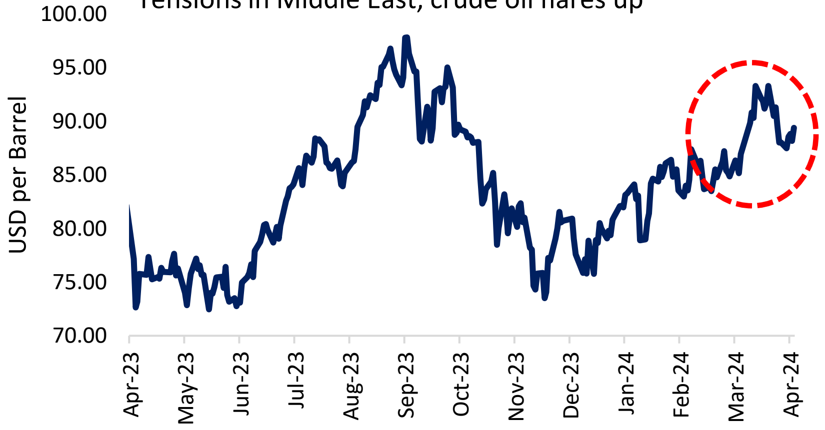
Global Supply Chain Pressure Index (GSCPI)

GSPCI suggesting improvement in supply chain
(Lower the better)

Source: Bloomberg

Brent Crude (USD Per Barrel)

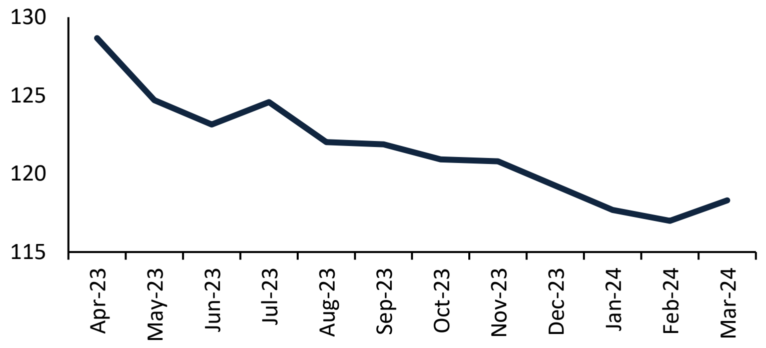
Tensions in Middle East, crude oil flares up



Source: Bloomberg

UN Food & Agriculture World Food Price Index

Food prices continue to remain weak due to better supply condition

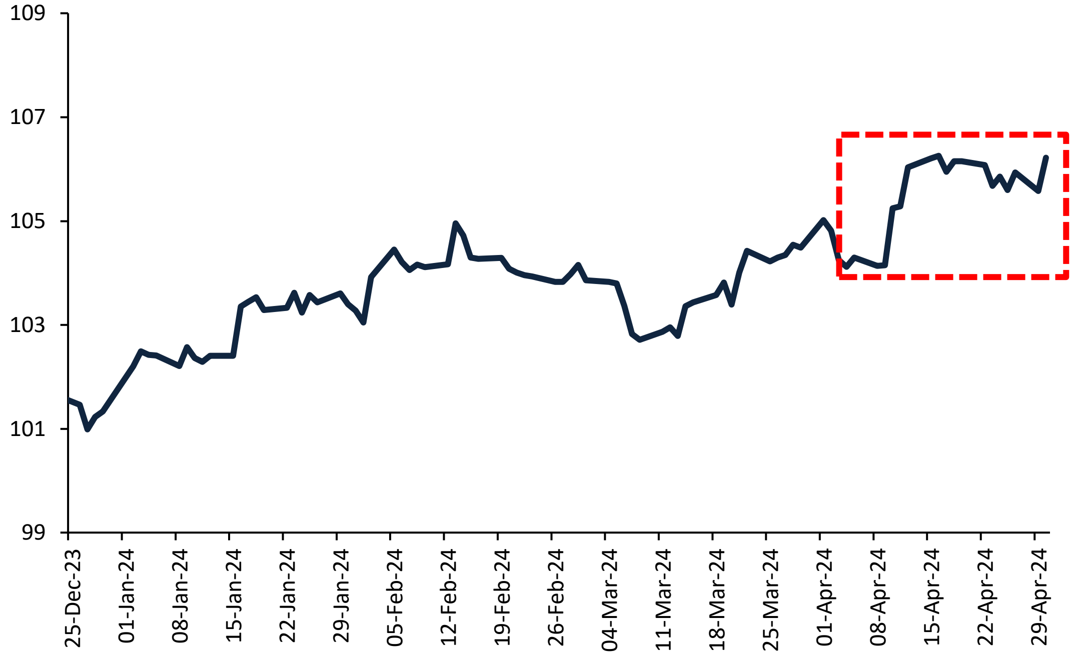


Source: Bloomberg

Uptick in the US dollar index impacting foreign flows into the emerging economies

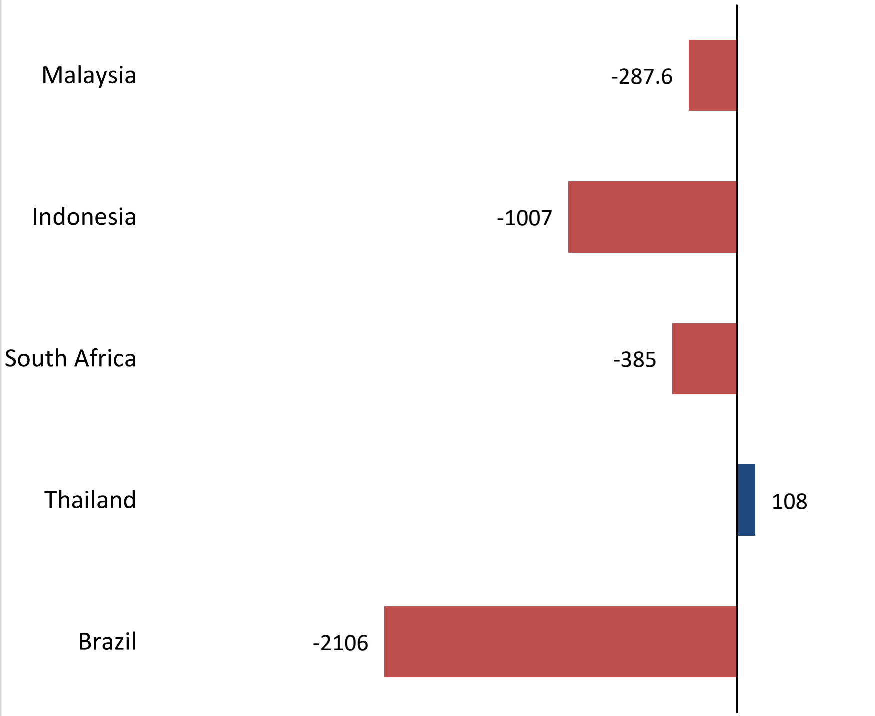
US Dollar Index

Improved macro data points from US & expectation in pushback of rate cuts has led to jump in dollar index…



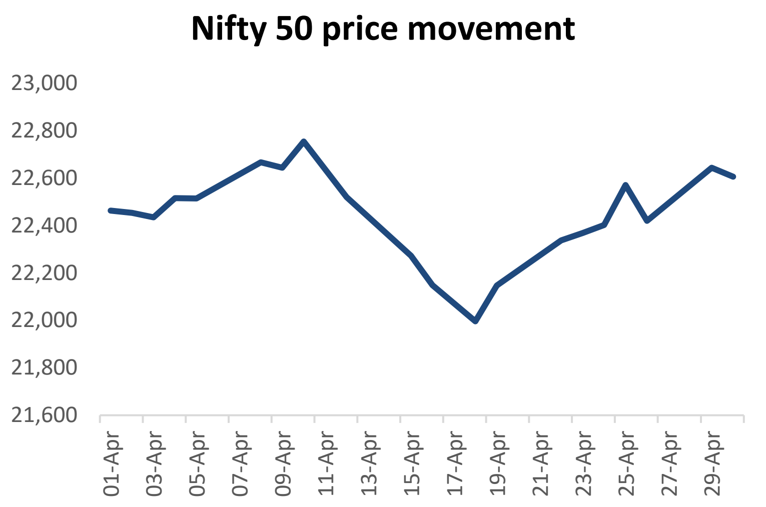
Source: Bloomberg

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

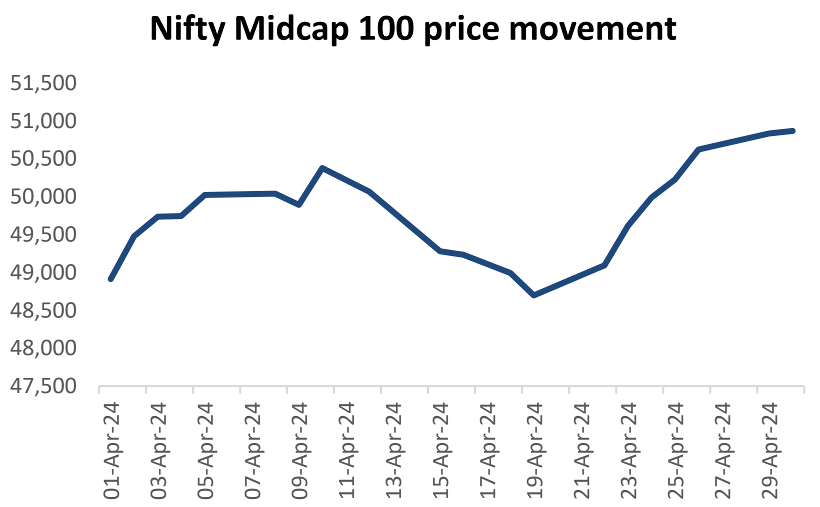


Source: Bloomberg

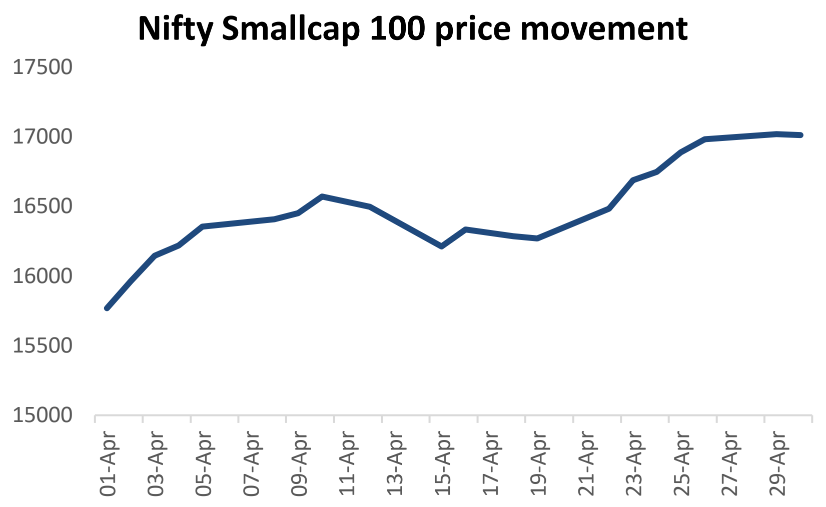
Indian Equity Markets' volatility driven by rising geopolitical risk… jump in Dollar Index leads to FPI outflows…Small cap index bounces back



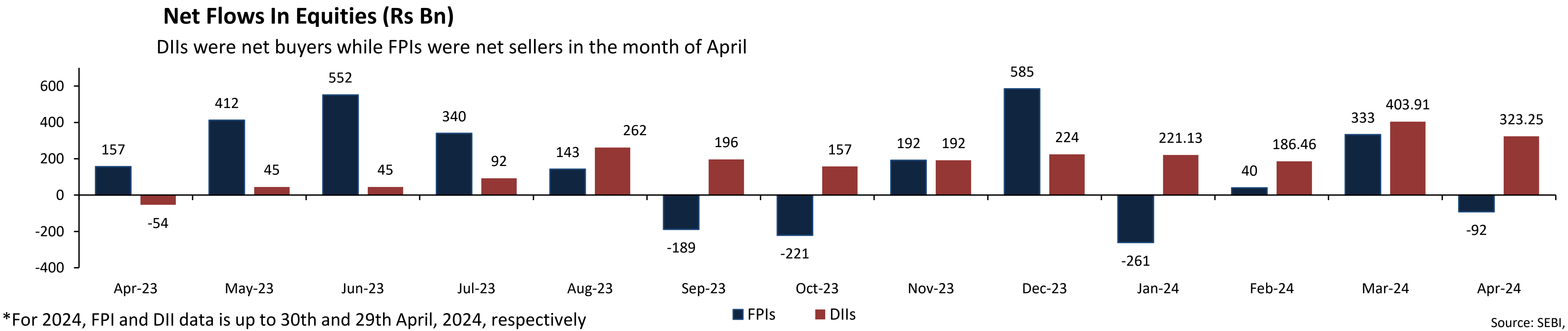
Source: Bloomberg



Source: Bloomberg



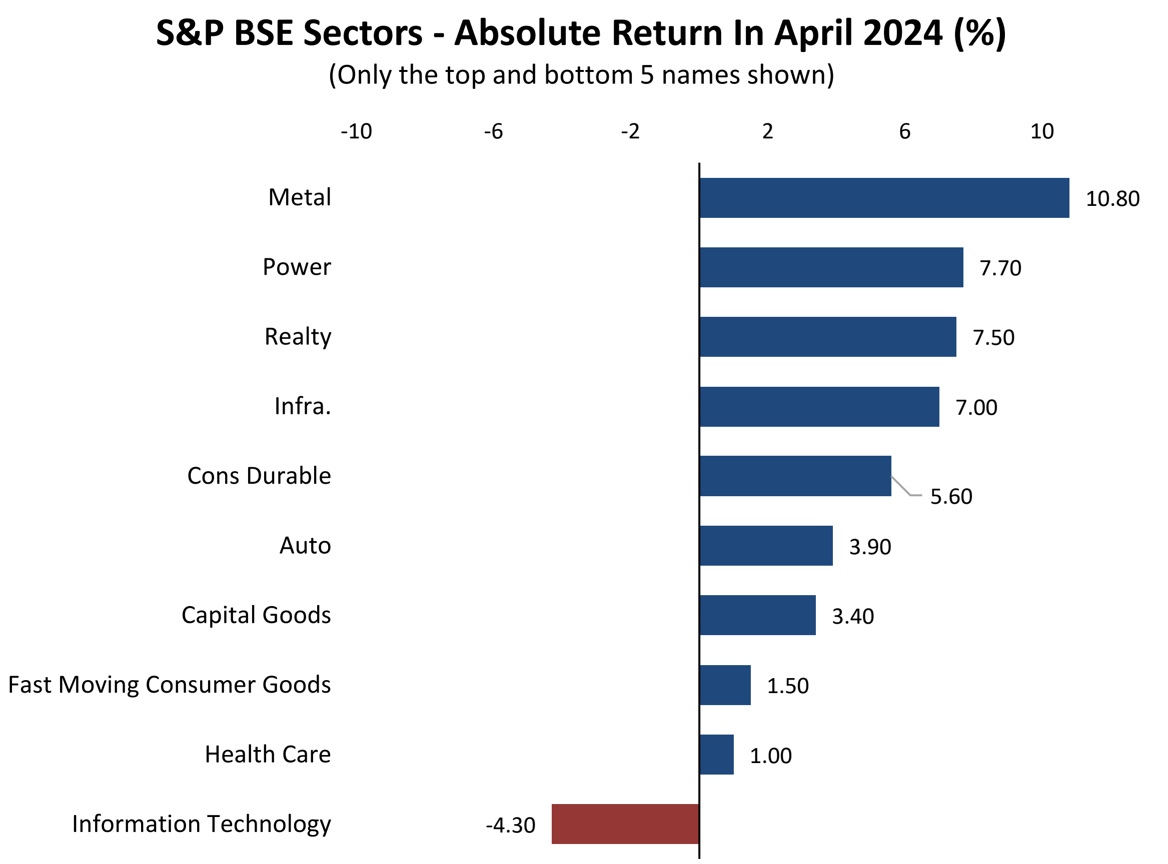
Source: Bloomberg



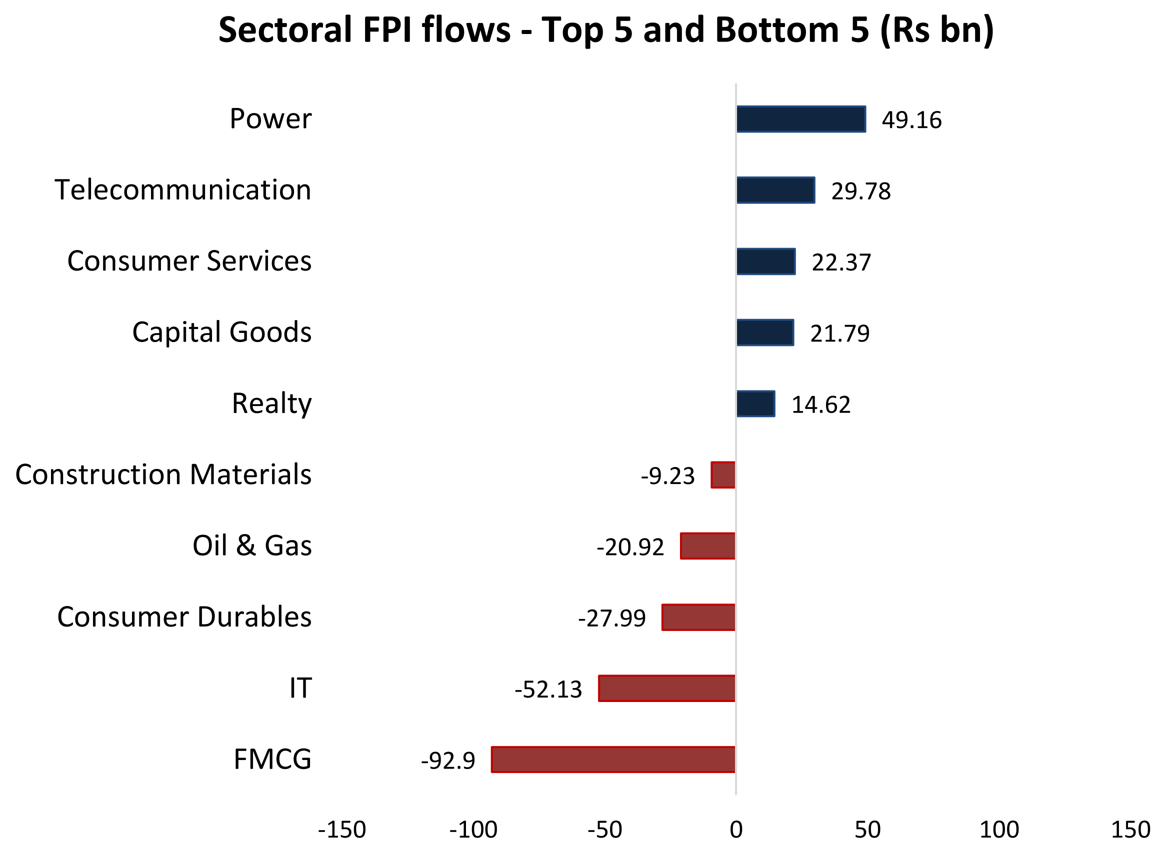
*For 2024, FPI and DII data is up to 30th and 29th April, 2024, respectively

Source: SEBI, CDSL

Sectoral performance and FPI flows in April 2024



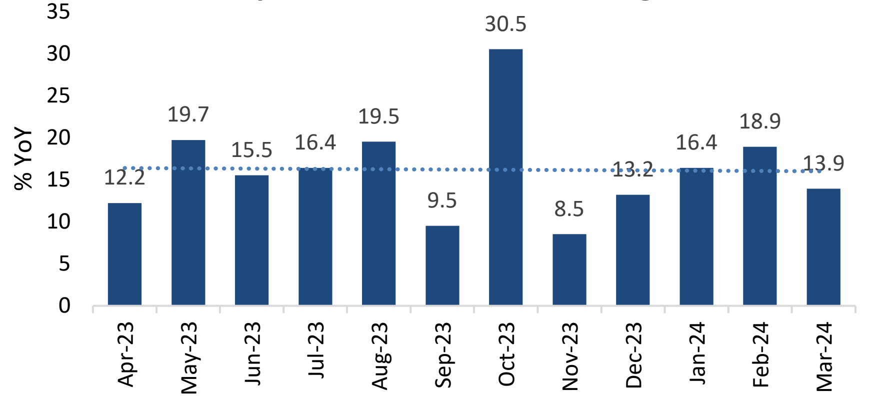
Source: Ace MF



Source: NSDL, Data is from Mar 16, 2024 - Apr 15, 2024

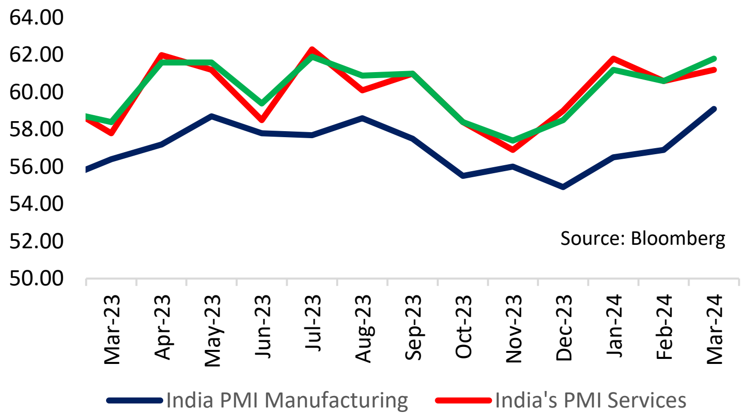
India – Macro indicators remain in fine shape

E-way bills reached all time high

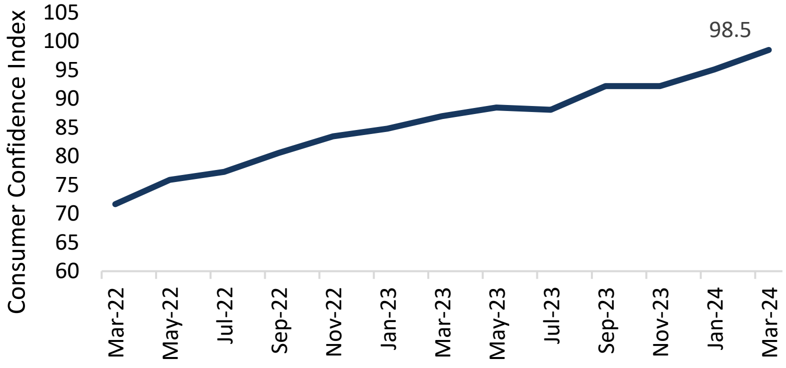


Source: Bloomberg

Manufacturing activity hit a 16-year high

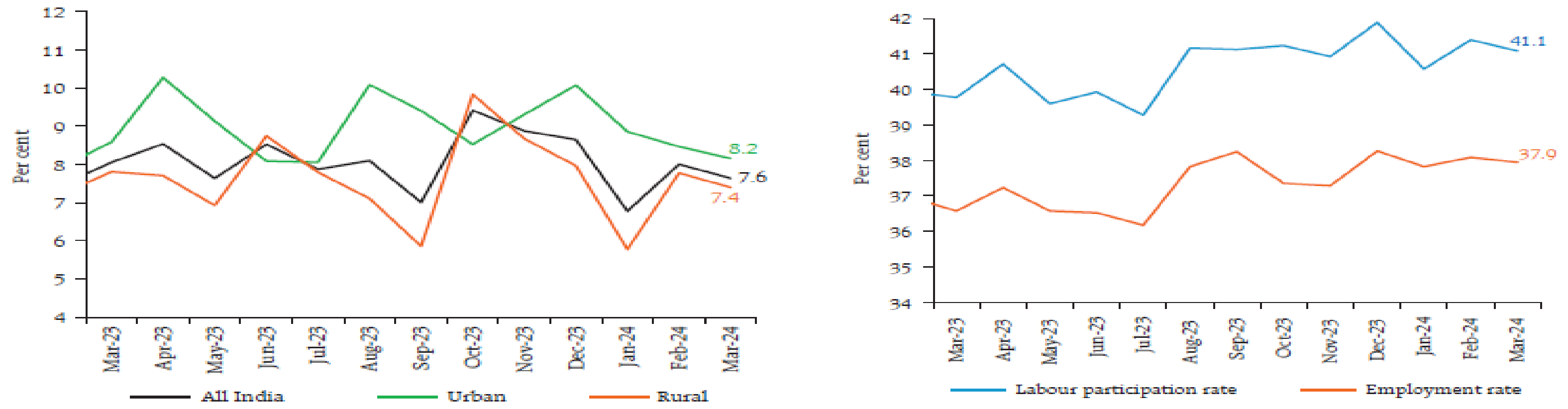


Consumer confidence improved further



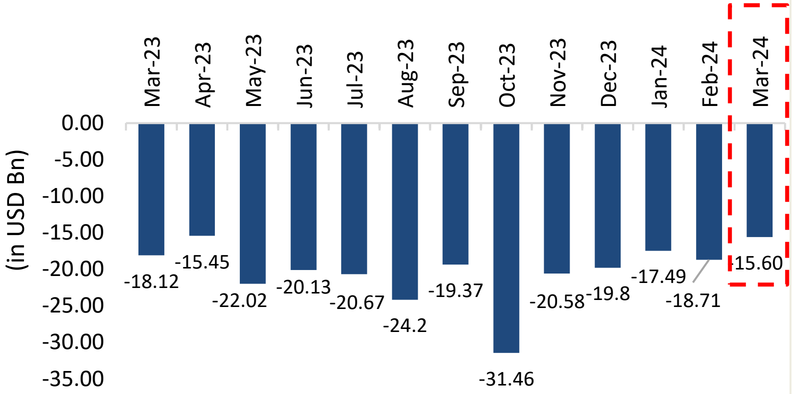
Source: Bloomberg

Unemployment rate declined in both urban and rural regions



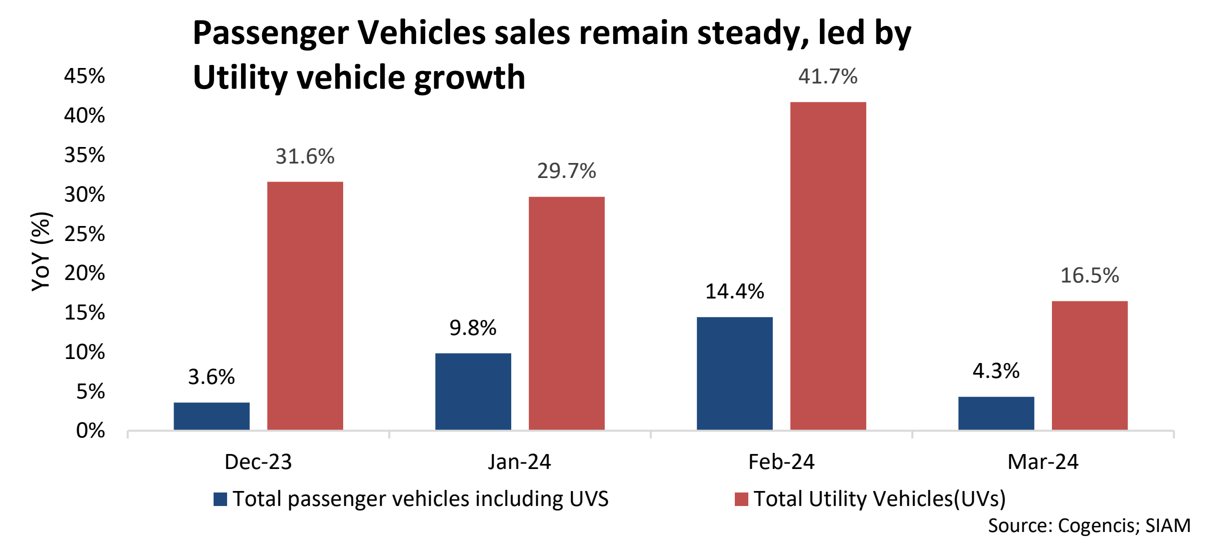
Source: RBI Bulletin April 2024

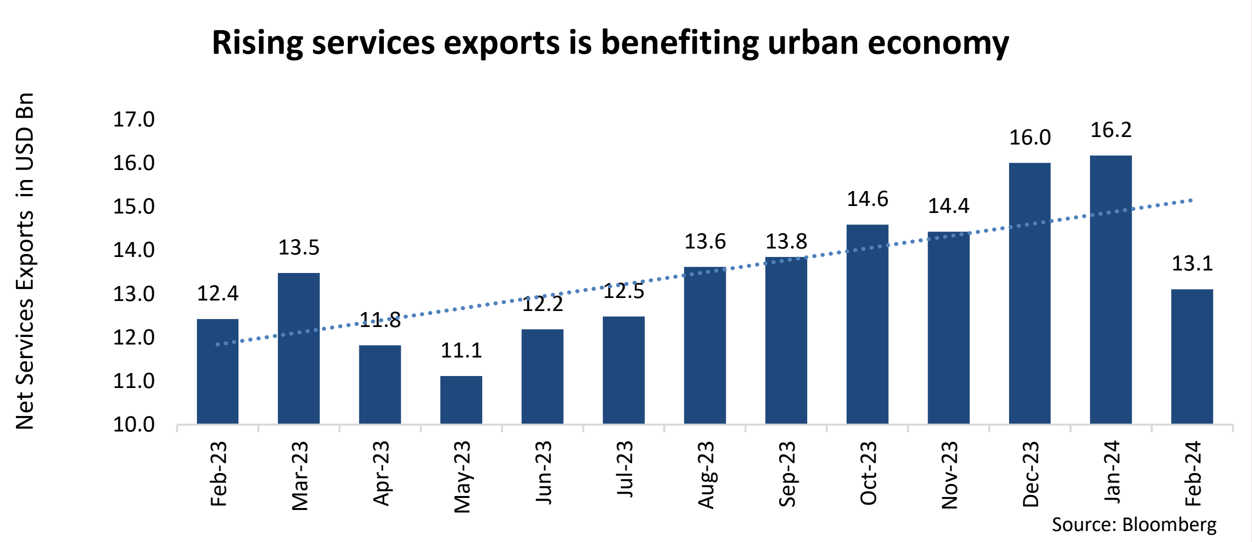
Merchandise trade deficit at an 11-month low

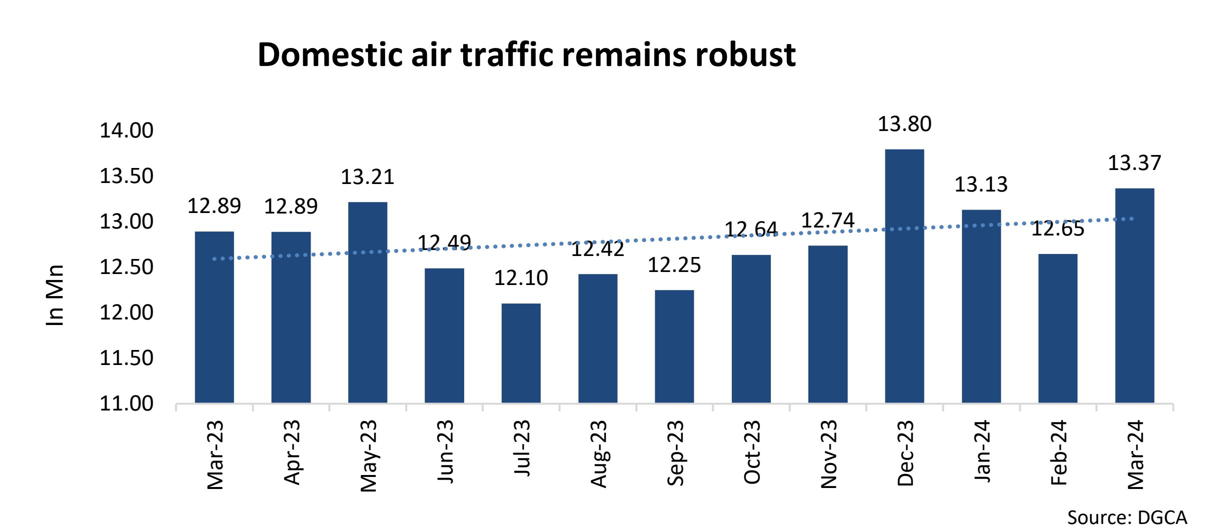


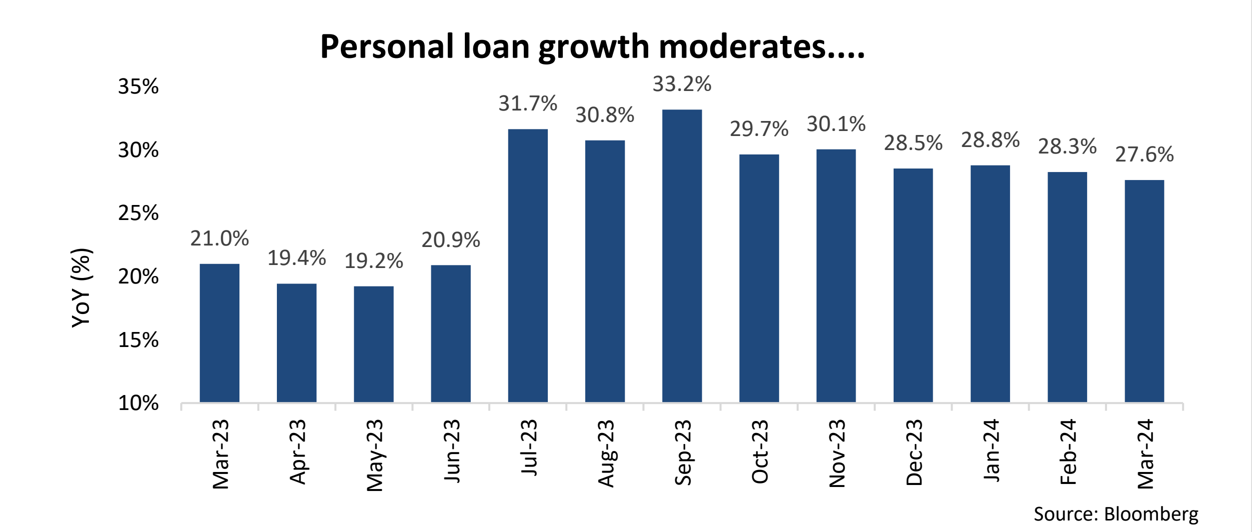
Source: Bloomberg

Urban consumption holding strong



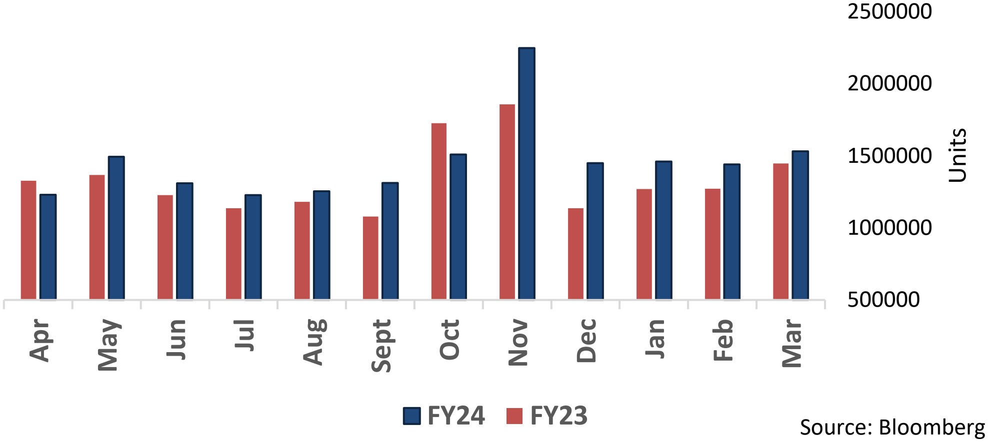






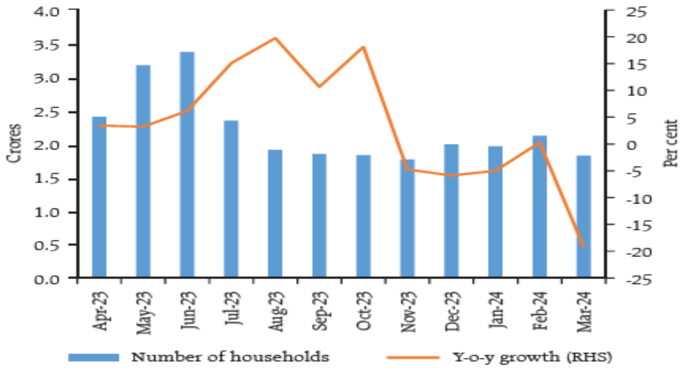
Rural India: Improvement visible

Two-Wheeler sales growth continues



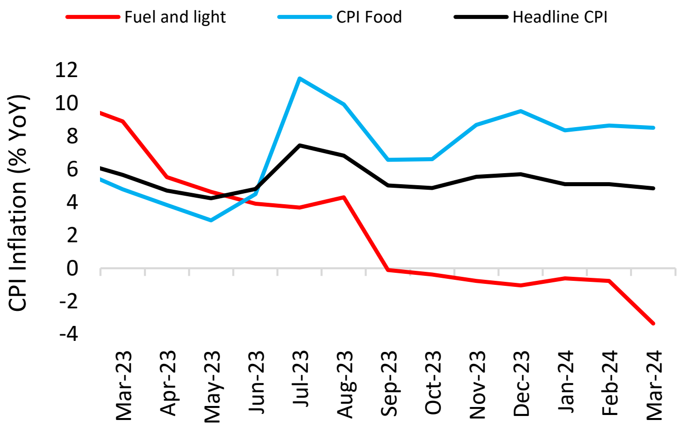
Source: Bloomberg

Demand for work under MGNREGS tapered off… suggesting of improving employment conditions



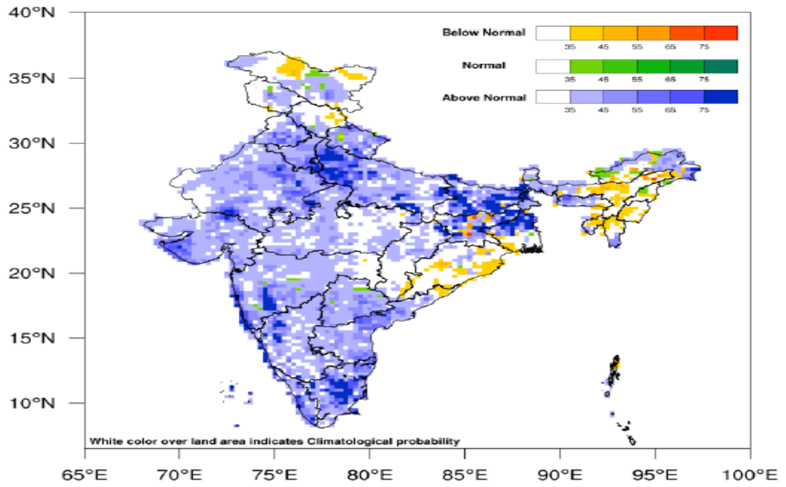
Source: RBI Bulletin April 2024

Lower inflation to help affordability



Source:-Ministry of Statistics and Program

Monsoon forecast to be normal in FY25, to support rural economy



Probabilistic rainfall forecast for monsoon season (June – September), 2024

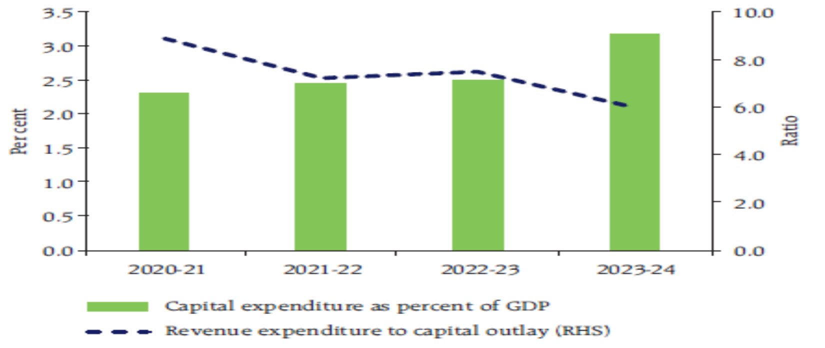
Category	Rainfall Range (% of LPA)	Forecast Probability (%)	Climatological Probability (%)
Deficient	< 90	2	16
Below Normal	90 - 96	8	17
Normal	96 -104	29	33
Above Normal	104 -110	31	16
Excess	> 110	30	17

Source: IMD

Capex continues to drive India's growth

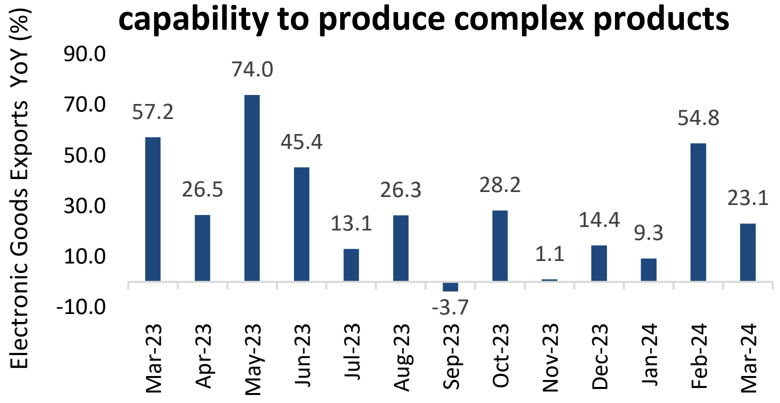
State Govt expenditure is focusing more towards capex

Capital Expenditure of States

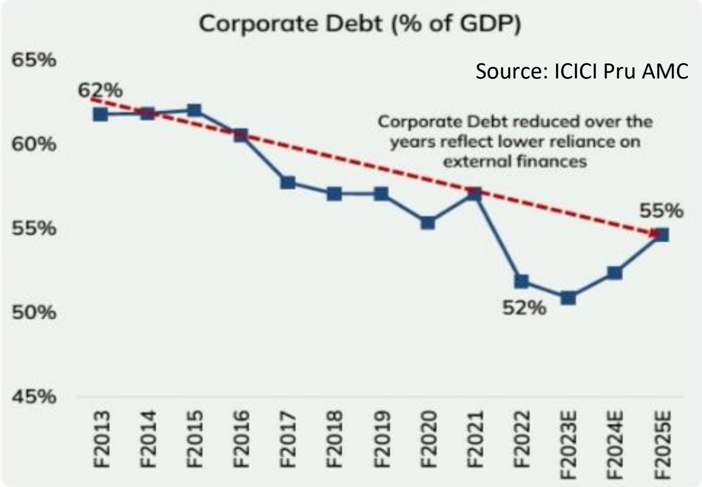


Source: RBI Bulletin April 2024

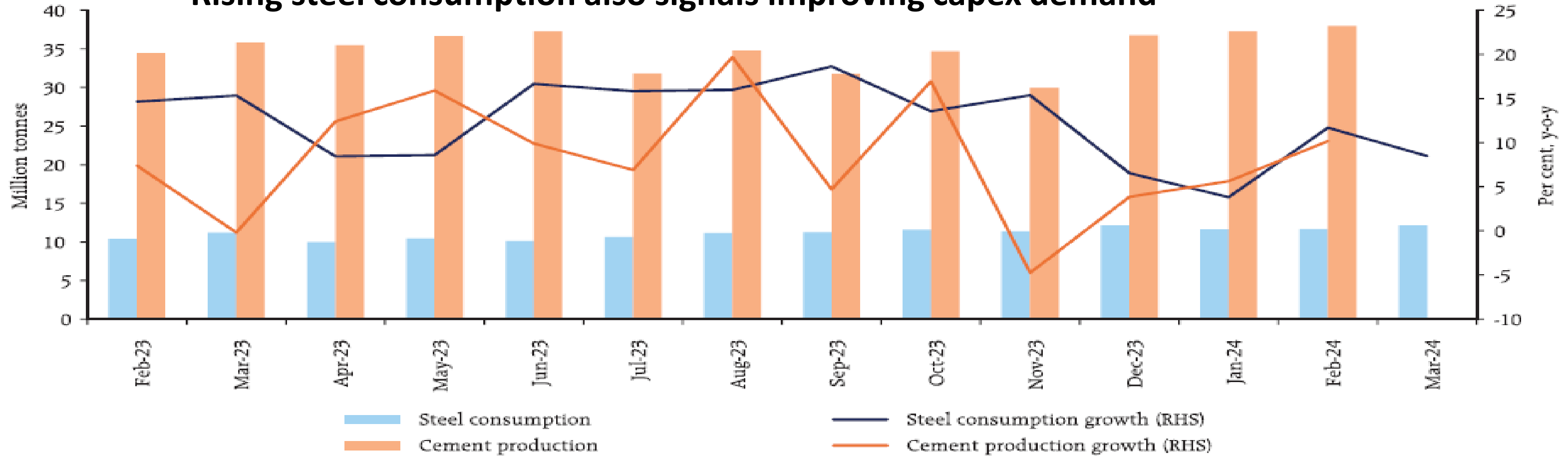
Rise in electronic exports shows capability to produce complex products



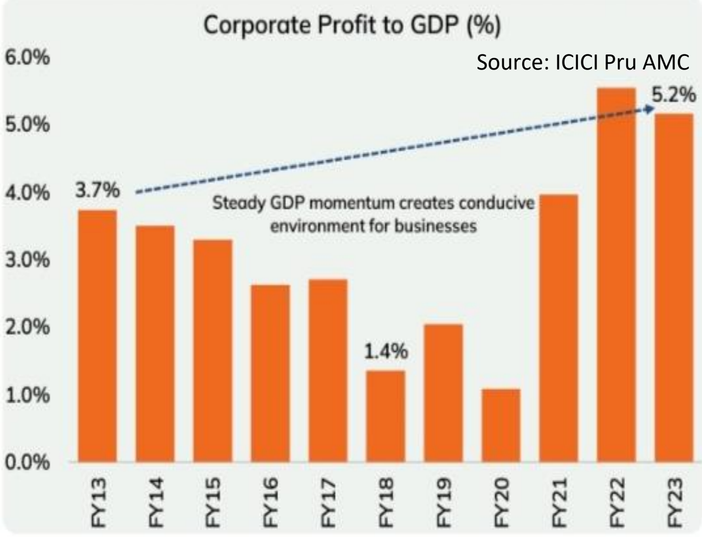
Source: Bloomberg



Rising steel consumption also signals improving capex demand



Source: RBI Bulletin April 2024



Quarterly results

Sector	Net Sales - YoY Growth (%)			EBITDA - YoY Growth (%)			PAT - YoY Growth (%)		
	Q4 FY24	Q3 FY24	Q4 FY23	Q4 FY24	Q3 FY24	Q4 FY23	Q4 FY24	Q3 FY24	Q4 FY23
Auto & Auto Anc	21.47	18.52	18.74	44.37	41.97	37.86	35.77	35.08	29.11
BFSI	32.57	33.45	28.76	62.41	23.75	19.15	74.48	31.51	-6.22
Cement & Products	11.60	7.94	11.52	39.35	105.19	-19.86	49.92	145.63	26.61
Chem & Fert	-28.55	-34.24	29.55	-41.44	-59.88	7.30	-33.49	-56.70	-14.96
FMCG & Retail	3.60	2.74	13.34	5.62	3.71	11.70	2.16	0.02	15.64
Healthcare	-0.79	-12.11	8.81	-17.26	-54.69	-16.76	-7.70	-56.30	-24.69
IT	2.02	2.37	18.32	1.60	0.60	14.62	8.19	-2.10	9.75
Metal & Mine	-7.22	1.73	-5.11	-12.81	15.34	-34.93	-24.57	-6.71	-43.91
Oil & Gas	11.13	3.85	2.63	7.59	11.79	15.15	0.08	10.93	17.79
Others	17.22	16.49	86.39	26.22	25.14	649.37	30.16	15.59	278.83
Telecom	24.05	23.26	6.90	-4.41	0.22	-4.15	-84.26	-349.33	-52.94
Grand Total	14.69	12.52	14.49	10.85	9.91	7.03	28.40	14.79	0.75
Ex-Financials	6.54	3.77	8.98	4.29	7.57	5.66	4.56	3.36	4.77

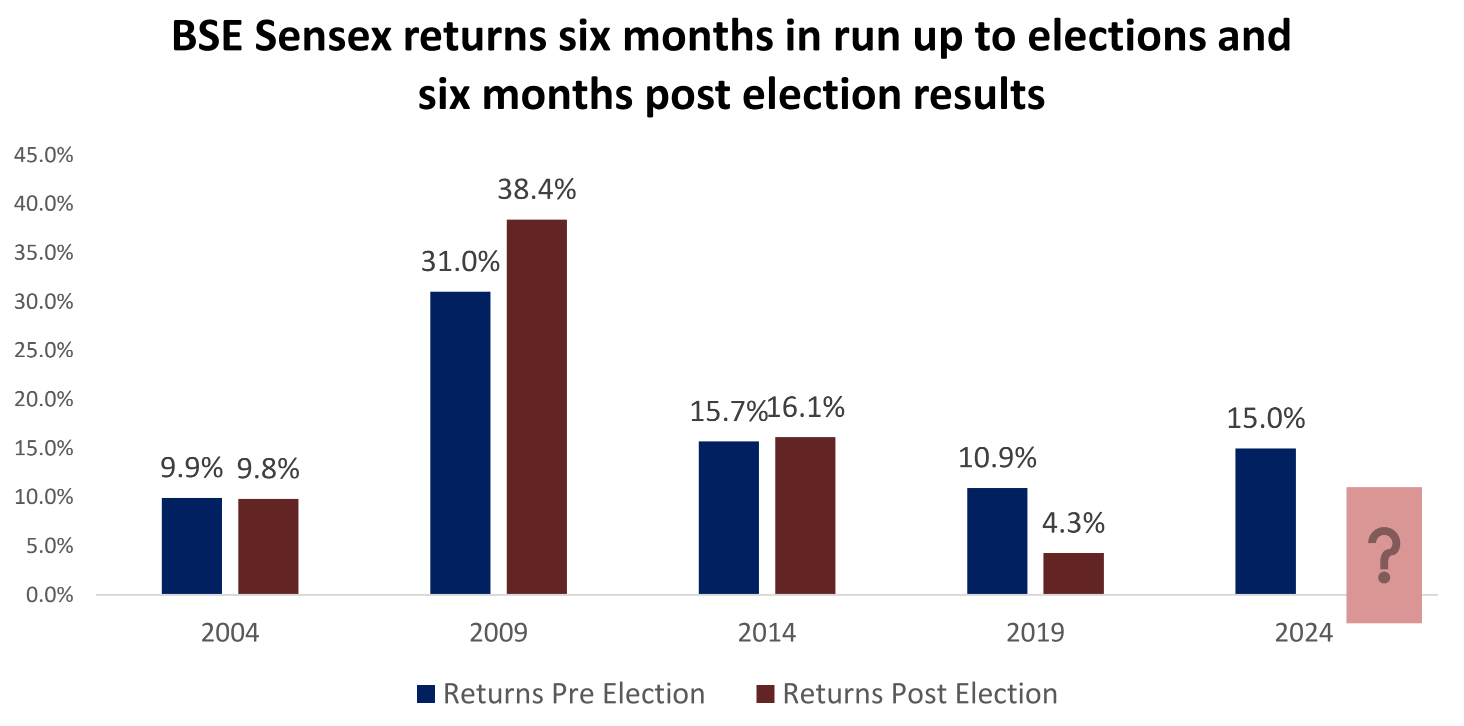
Data as on 29 April, 2024 and pertains to 47 companies within the Nifty 200 universe

Source: Capitaline, HDFC Bank Research

1. Results thus far, have been muted.
2. Banking sector performance remains strong.
3. Chemicals, IT, Telecom & Metal drives early weakness.

General Elections - Key Variable

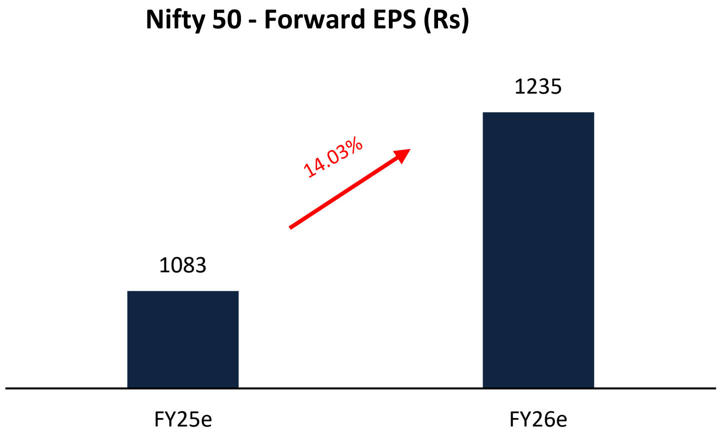
The 2024 Lok Sabha elections is being held in seven phases from April 19, 2024. The results will be announced on June 4, 2024. Adverse results may lead to weakening of market sentiments.



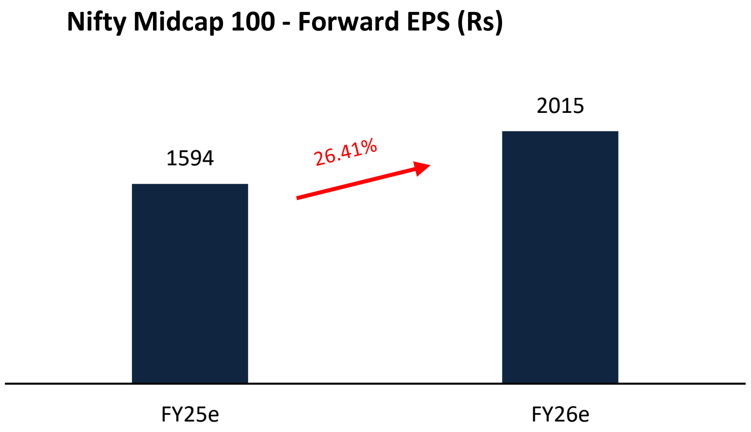
PHASES	POLLING DATES
I (102 seats)	April 19
II (89 seats)	April 26
III (94 seats)	May 7
IV (96 seats)	May 13
V (49 seats)	May 20
VI (57 seats)	May 25
VII (57 SEATS)	June 1

Note : Data for year 2024 is taken as of 22nd April as elections are on going currently...

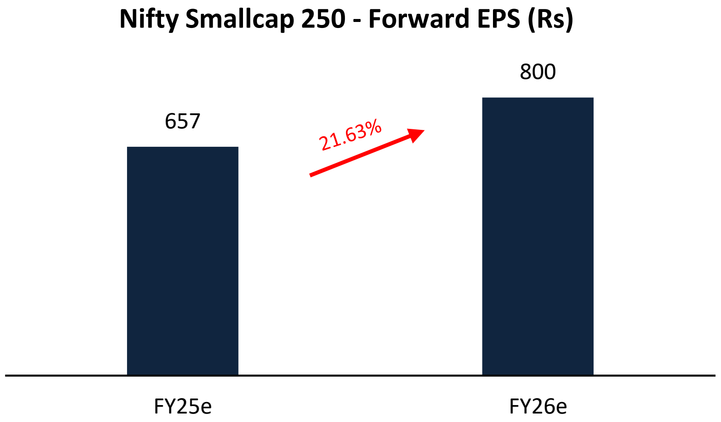
India valuations – Elevated… Mid Cap & Small Cap valuations have bounced post the correction… Large Cap remains relatively reasonable



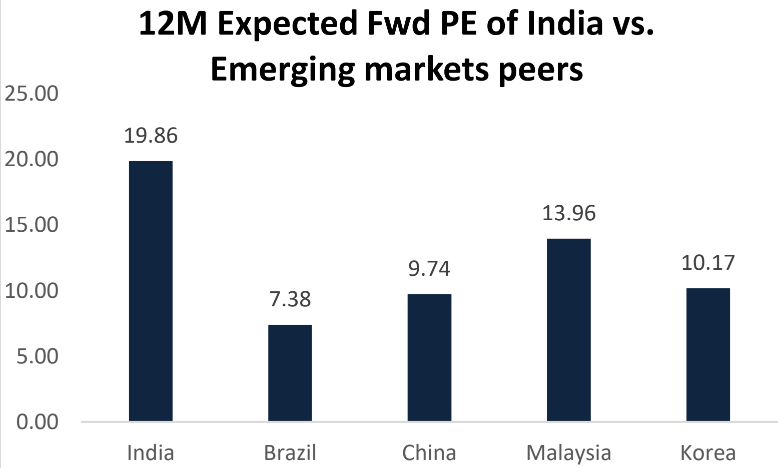
Source: Bloomberg



Source: Bloomberg



Source: Bloomberg



Data as on 26th April 2024

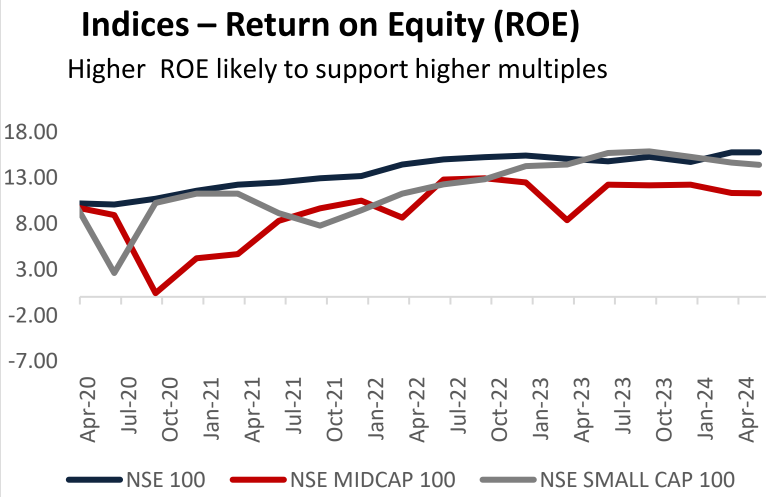
Source: Bloomberg

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

Index	FY25 (Est)	FY26 (Est)
Nifty 50	19.86	18.34
Nifty Midcap 100	32.06	25.36
Nifty Smallcap 250	24.11	19.82

Source: Bloomberg

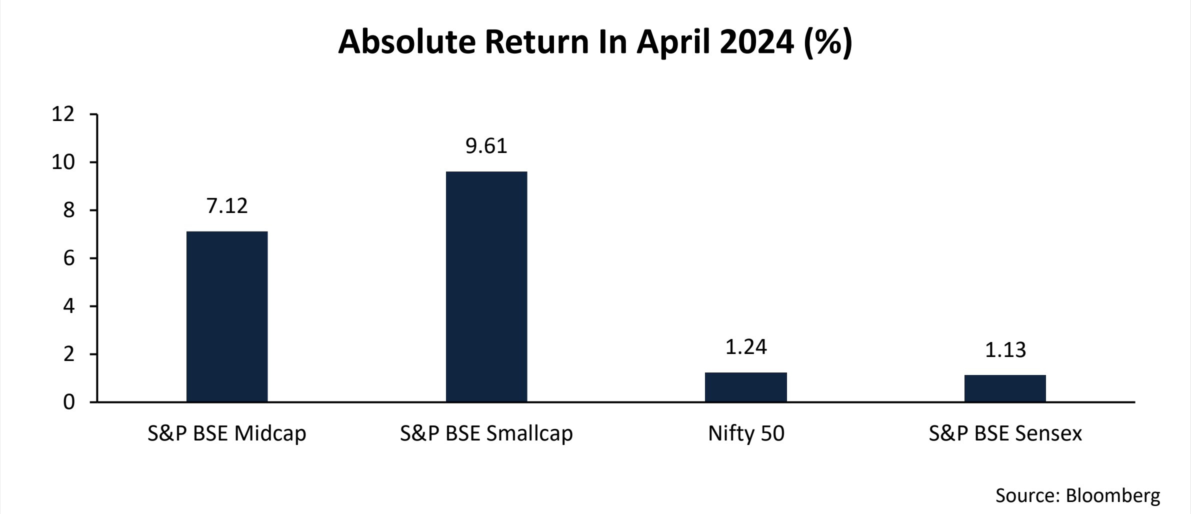
Source: Bloomberg

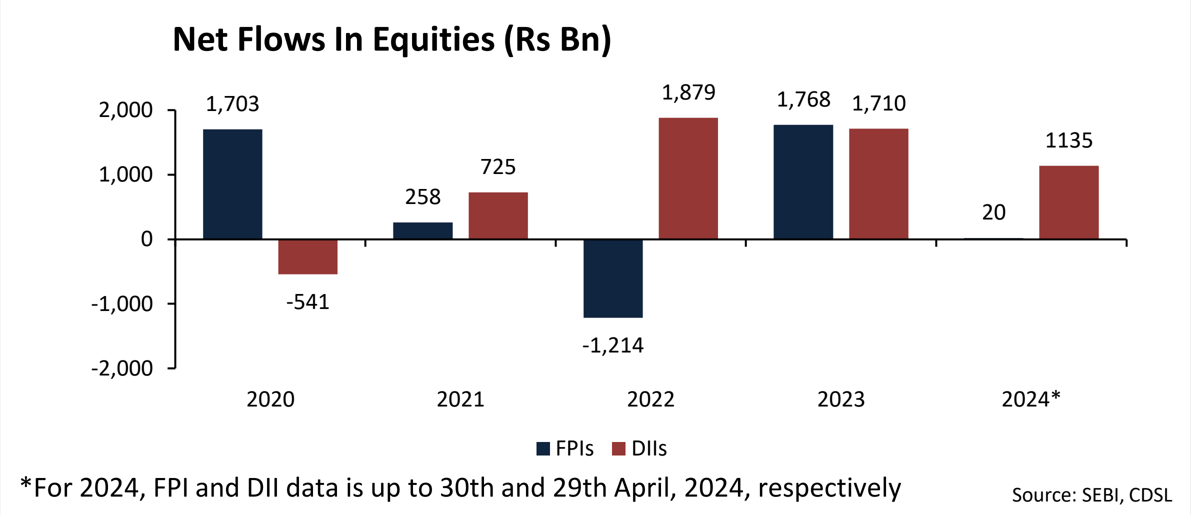


Source: Bloomberg

Market Roundup – April 2024

- Indian equities ended the month on a positive note. Large cap-oriented S&P BSE Sensex and Nifty 50 ended higher to the tune of 1.1% & 1.2% (MoM) respectively.
- While the S&P BSE Midcap & S&P BSE Small cap indices ended higher by 7.1%, & 9.6% (MoM) respectively.
- In terms of BSE sectoral indices, Metals was the top performer. In contrast, IT, Healthcare and FMCG underperformed the most.
- Indian equities ended the month on a positive note after witnessing no major signs of escalation in tensions in West Asia. Investors became more exposed to domestic equities due to India's strong growth prospects and in expectation of political stability in the upcoming general election.





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 Private sector banks. • NIM concerns have resurfaced as the cost of funds have risen due to tight liquidity scenario and with policy rates likely to be cut, further pressure to NIM possible. • Credit cost (provisioning) are holding up, Unsecured loans are under scrutiny by the RBI. • Most fund managers are cutting underweights/ Equal weight in the sector. Pvt sector banks gradually being given preference due to lower valuations.
IT	**View – Negative to Neutral** • Q4FY24 results have been weak. Large global bellwethers have suggested caution for growth going forward. • Order book growth holding up, margins need to sustain, execution cycle seem to be pushed back by customers. • Stocks are expected to consolidate going forward as valuations have run up. • Funds are taking tactical positions, but mostly running underweight.
Pharma	**View – Overweight** • Reasonable valuations, domestic demand holding up well. • 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 to sustain, but on a high base the volume growth likely at low single digits. • 2-Wheeler stocks are seeing renewed traction and driving alpha. Once the base is high, the volume growth can taper. • SUV oriented companies expected to still hold on to earnings growth, as improved product mix in the sales would help drive earnings. • Initial signs of weakness seen globally in the EV theme. Indian policymakers still supportive of this segment. • Commercial vehicle sales getting sluggish, fund managers underweight. • Auto ancillaries gaining due to China+1, Europe+1, PLI and EV initiatives.

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. Though some are gradually building exposure into direct Real Estate stocks.
Consumption	**View – consumer services -Positive, consumer durables and FMCG- negative** • Staples – Low volume growth, pricing power weak, Valuations high. Funds generally underweight. • Hotels/Travel – Valuations rich, funds holding on to their overweight. 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's near term performance expected to be weak, finding favour in portfolios due to expectations of change in consumer behaviour in long term. **Long-term positives** • Rising per capita income. • Premiumization across categories.
Capital goods, industrials, utilities	**View – Neutral** • Capex cycle uptick implies that domestic capital goods are gaining traction. • Export prospects appear promising, albeit on a bottom-up basis. • Order books are robust, and earnings remain stable. • New ideas also emerging and some old themes getting churned. • Power, Automation, Electronics continues to be the dominant theme for capex. • **Valuations are steep, while earnings momentum holding up. Funds with high exposure not keen on raising further weights, trimming/churning at margin.**
Metals	**View – Positive** • With outlook of Chinese economy improving, US economy continuing to see growth, metal stocks are finding favour with the Fund managers. Fund manager have reduced their underweight positions and are gradually getting upbeat on the sector.

Monthly Sectoral Movement

Absolute Monthly Return By Sector (%)

Index	Apr-23	May-23	Jun-23	Jul-23	Aug-23	Sep-23	Oct-23	Nov-23	Dec-23	Jan-24	Feb-24	Mar-24	Apr-24
S&P BSE 500	**7.08**	**3.51**	**3.86**	**3.80**	**-0.81**	**2.04**	**-2.93**	**6.75**	**8.01**	**1.90**	**1.93**	**0.84**	**3.43**
Auto	10.29	7.94	6.76	3.14	-1.40	3.65	-1.25	10.08	5.43	4.18	8.12	4.96	3.92
Bankex	9.18	2.11	0.12	1.85	-4.01	0.35	-3.44	3.47	8.12	-4.38	1.92	2.02	4.64
Basic Material	7.83	1.70	2.39	3.19	1.06	1.70	-3.70	7.25	11.39	0.33	-0.42	1.06	7.86
Capital Goods	9.71	1.31	9.79	8.15	2.66	6.20	-4.07	8.88	11.31	1.88	-1.21	6.15	3.42
Consumer Discretionary	9.25	7.18	5.94	4.46	2.10	2.40	-1.38	9.36	5.91	2.35	4.89	1.69	5.05
Consumer Durables	2.91	6.47	5.67	-0.25	4.24	3.18	-2.32	7.42	6.11	0.70	0.00	2.05	5.59
Energy	7.19	-0.07	-0.24	6.89	-4.38	3.20	-2.17	9.17	11.06	12.18	6.18	-0.19	3.33
FMCG	6.81	5.89	2.47	1.58	-2.75	0.97	-0.86	3.58	6.84	-2.81	-2.33	-0.67	1.52
Finance	9.05	2.13	1.97	3.16	-2.64	1.08	-3.09	4.82	6.92	-2.40	0.47	1.35	4.93
Healthcare	6.33	2.81	9.71	7.45	0.57	2.45	-4.30	10.92	3.87	7.18	5.94	-0.08	1.01
IT	-0.13	6.70	2.16	1.34	4.13	2.62	-3.13	6.77	8.38	3.74	3.38	-7.20	-4.35
Infra	6.06	0.89	4.51	10.73	1.64	8.45	-3.38	10.40	14.88	18.15	1.23	0.48	7.03
Metal	7.21	-2.94	3.99	7.88	-1.64	7.45	-4.17	8.74	11.35	-0.85	1.15	4.95	10.83
Oil & Gas	6.39	-1.64	0.27	6.67	-5.03	1.23	-4.17	12.51	12.02	12.57	6.86	-0.07	4.83
Power	5.37	2.01	4.33	9.20	-0.63	5.96	-4.90	11.16	18.24	8.57	4.33	1.70	7.73
Realty	19.64	7.67	9.35	9.01	-1.50	5.21	3.70	19.99	9.37	9.37	9.16	-1.21	7.52
Telecom	8.44	4.12	9.08	5.61	3.20	10.55	-5.69	7.21	6.15	6.94	1.44	1.81	8.36
Utilities	6.22	-0.59	5.02	10.36	-0.64	7.20	-3.98	11.85	20.00	9.71	3.61	0.25	8.84

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

Colour scales assigned vertically

Source: Ace MF, HDFC Bank Research

Key concerns for Indian equities

- Results of the Indian General Elections
- Low growth in consumer demand
- Expectation of weakening margin profile for corporates
- Delay in rate cuts by Global Central Banks
- Upward pressure on food inflation (El Nino, export restrictions by some nations)
- Rising 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

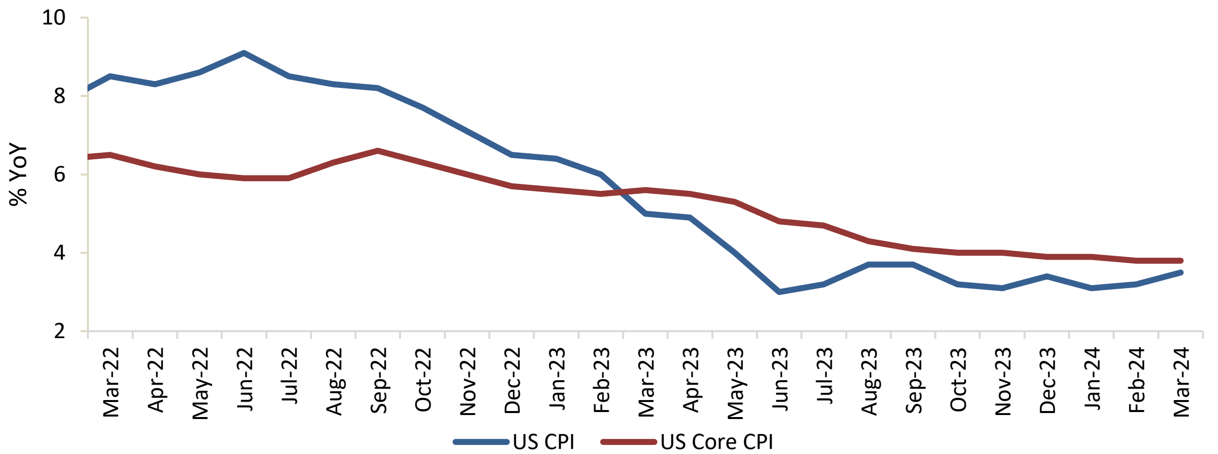
Fixed Income Market

Fixed Income Outlook

- The Reserve Bank of India (RBI) is keeping banking system liquidity tight to ensure that the call money rates remain around the repo rate. The RBI is expected to remain nimble in liquidity management and utilise tools such as VRRR or VRR as needed. Going forward, the inclusion of G-secs in JPMorgan's Government Bond Index-Emerging Markets is likely to improve liquidity unless the RBI decides to sterilise inflows.
- Consumer Price Index (CPI)-based inflation slowed to below 5% YoY after four months due to a decline in food and fuel prices. Additionally, moderation across broad-based categories and base effect kept the pressure off the inflation print. On the core inflation front, the easing continues as the core CPI came in lowest at 3.25% YoY in March 2024 as against 3.34% YoY in February 2024, which remains positive for the market. The subdued momentum in the core CPI can be attributed to lower input price pressure and rangebound global commodity prices. However, the recent uptick in gold, silver, and other commodities prices and sustained growth momentum can reaccelerate inflation. Additionally, the escalations in geopolitical tensions may adversely impact inflation due to supply constraints. Nonetheless, the RBI's lower inflation forecast suggests that inflation will likely ease in the coming months. The favourable base effect will also likely reduce the pressure over inflation print.
- The merchandise trade deficit narrowed to an 11-month low in March 2024 as exports were almost flat on a sequential basis, but imports fell. For FY24, while exports declined due to a slowdown in global demand and geopolitical tensions, the falling imports kept the merchandise trade deficit in check. On the other hand, the resilient services exports provided a cushion against the wider merchandise trade deficit. The trend of services exports will likely continue and strengthen the external sector.
- India seems to be in a Goldilocks scenario of low inflation and high growth. However, the RBI seems to be apprehensive about cutting rates as food price shocks exhibit significant volatility to headline inflation. Thus, the RBI is likely to track the update on the upcoming monsoon for its impact on food inflation, and it is also likely to wait for the headline inflation to trend downwards on a durable basis before cutting rates. Nonetheless, the rate cuts are likely to be shallow. The RBI is also likely to take cues from the monetary policies of the major global central banks, as early cutting of rates may have repercussions on currency.
- The narrowing of fiscal deficit remains positive for the bond market as this would lead to lesser market borrowing by the government, thus limiting the supply of bonds and pulling the yields down.
- In the US, while the Fed's median projection in March 2024 policy suggested three policy rate cuts (total 75 bps) in CY24, the recent upside surprises on inflation and the labour market are likely to push the rate cuts forward, resulting in fewer rate cuts in this calendar year. Thus, while the current rate cycle has peaked, there is uncertainty regarding the timing and quantum of rate cuts. On the other hand, the Fed is likely to slow down the pace of balance sheet reduction, which is expected to loosen the financial conditions marginally.
- In Japan, the falling of the Japanese Yen vis-a-vis the US Dollar is likely to warrant rate hikes or intervention by the Bank of Japan (BoJ) in the currency market. The rising inflation may also lead to further rate hikes by the BoJ. However, if BoJ raises rates rapidly, the reversal of carry trade may put upward pressure on US Treasury yields as Japan is one of the largest holders of US Treasuries. The revival of the Chinese economy needs to be monitored for the resurgence in commodity demand, as it may bring back global inflationary pulses.
- Domestically, the recent uptick in bond yields in India can be attributed primarily to the expectations of a delay in rate cuts in the US. In the medium term, the market is likely to take cues from the US market, the flows related to the JP Morgan bond index inclusion, and the liquidity measures of the RBI. The trend of food inflation, the forecast of the upcoming monsoon and heat waves, and geopolitical tensions are also likely to affect the domestic G-sec yields due to their effect on inflation. The Indian G-sec yields are expected to move in a range with a declining bias due to favourable supply-demand dynamics, and fund managers who can navigate the volatility and play duration are likely to generate substantial alpha.
- With the G-sec yields rising in the mid to longer end, investors who are comfortable with volatility and have a longer horizon of 24 months and above can take exposure to Dynamic Bond Funds and Gilt Funds to play the improved fiscal deficit dynamics.
- Corporate Bond Funds continue to look like a safe bet at the current juncture for investors looking to invest in shorter-tenure funds. Hence, investors can look at Corporate Bond Funds and Short duration funds for a horizon of 15 months and above.
- For 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.

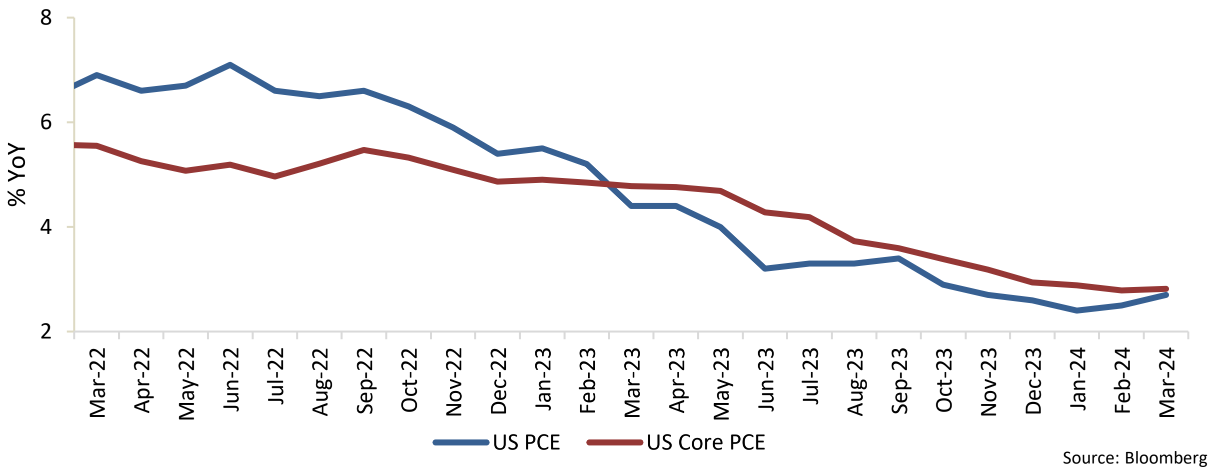
Higher than expected inflation pushed US Treasury yields higher…

US inflation print came in higher than the market expectations



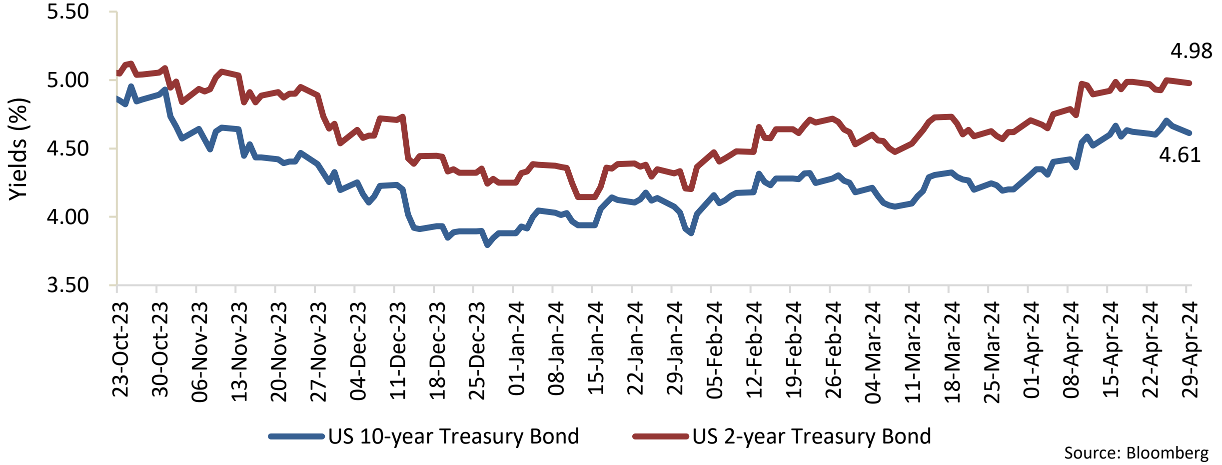
Source: Bloomberg

Key Fed inflation measure exhibiting signs of flaring



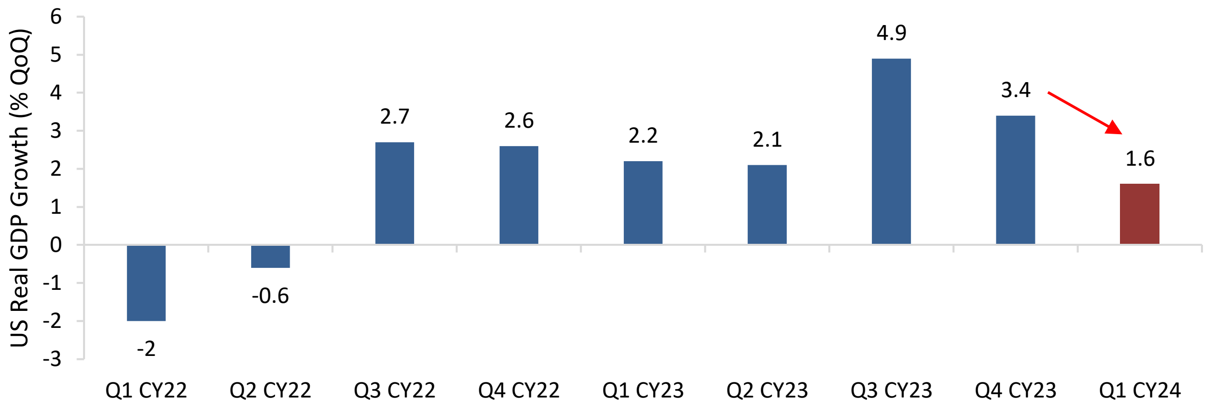
Source: Bloomberg

US Treasury yields surged on the back of elevated inflation



Source: Bloomberg

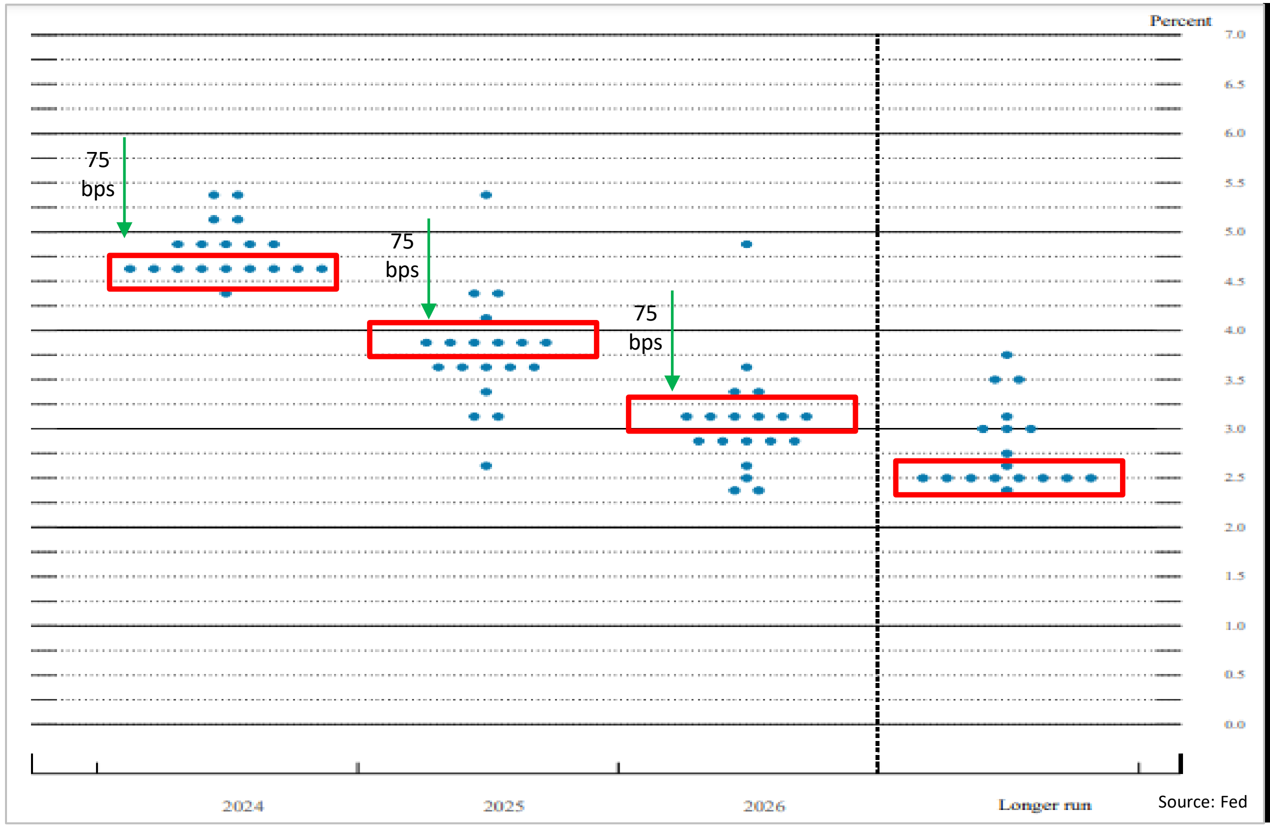
Q1 GDP growth fell short of expectations and requires monitoring for impact on labour market and demand



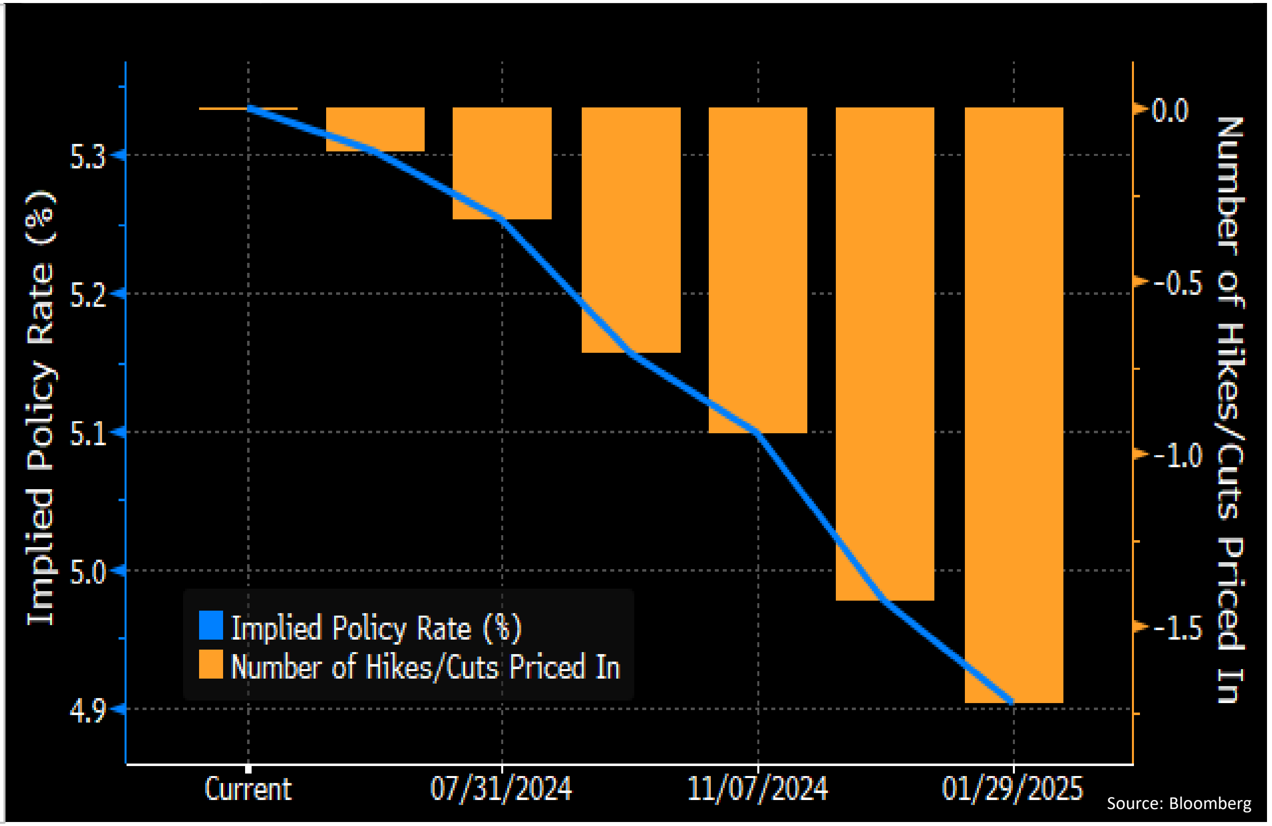
Source: Bloomberg

….Leading to delay in rate cut cycle in the US

While Fed's dot plot suggested 75 bps of rate cuts in CY24…

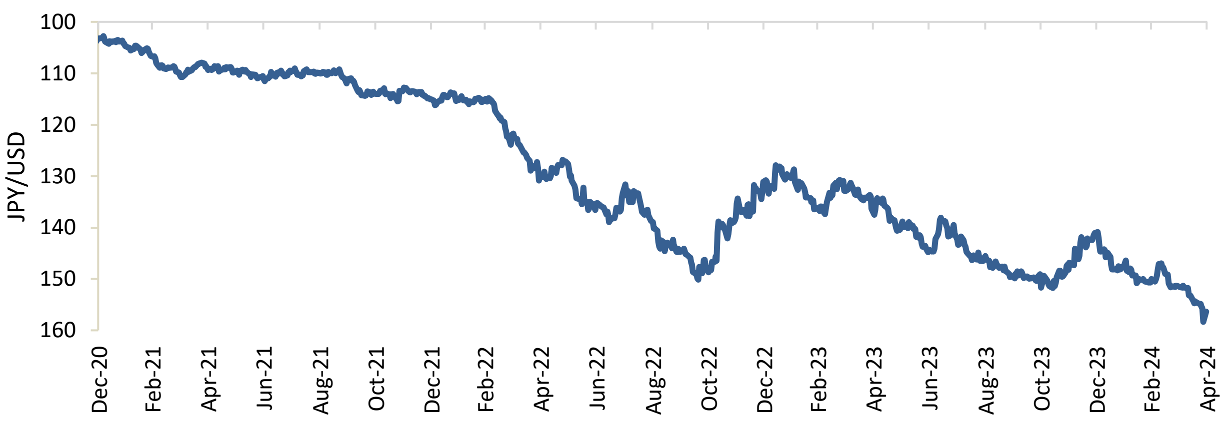


… Reversal in inflation trend and strong labour market seems to have pushed rate cuts further



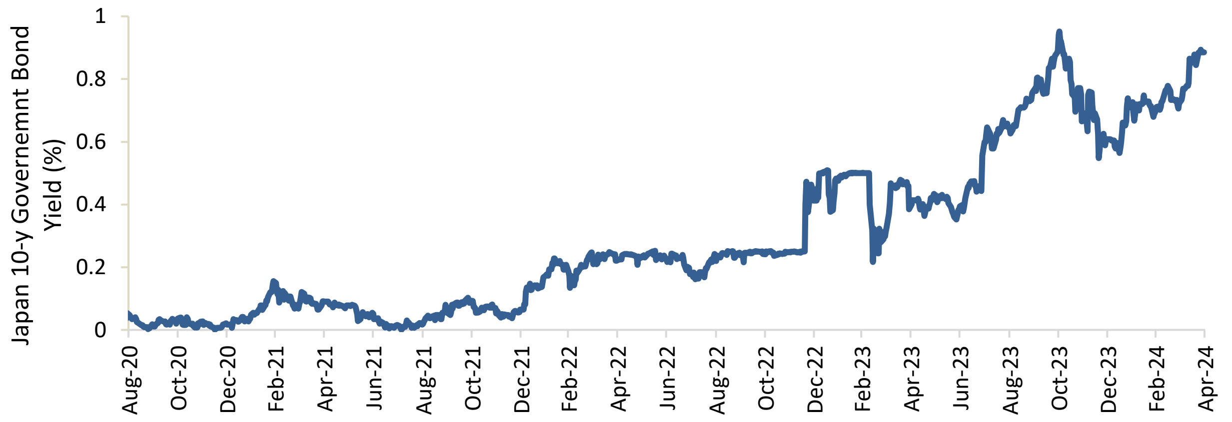
Falling Yen and rising inflation are driving rate hikes in Japan

Falling Japanese Yen may warrant BoJ's intervention



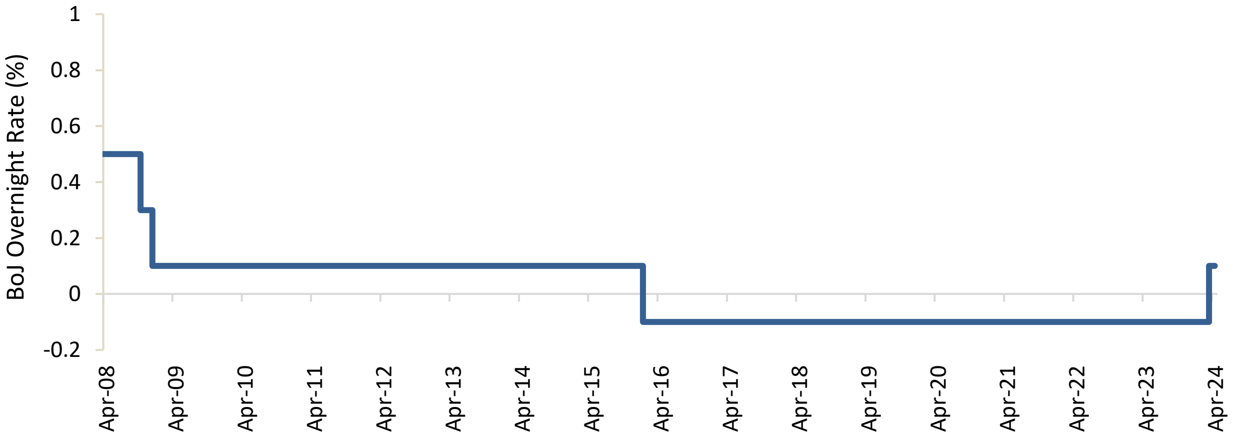
Source: Bloomberg

Japanese yields moving higher due to rising inflation



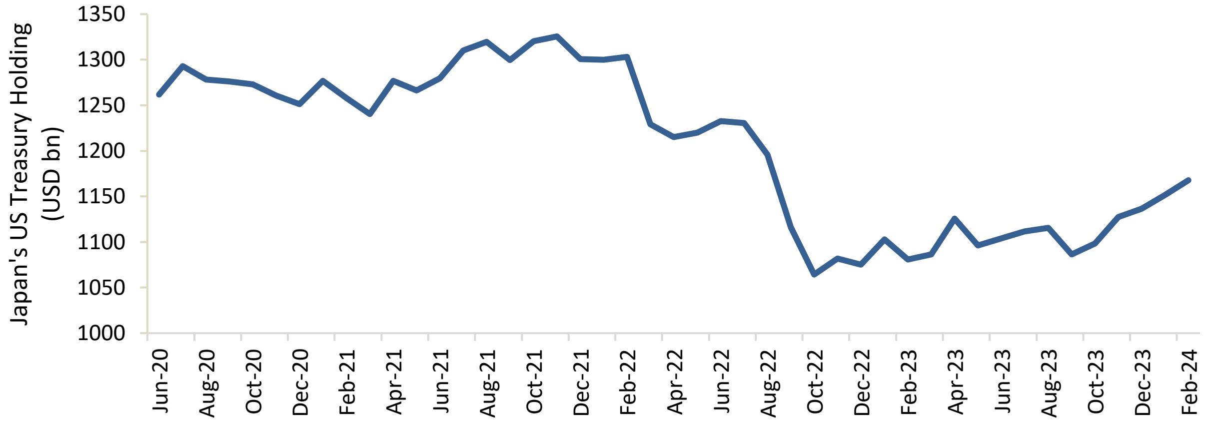
Source: Bloomberg

BoJ raised rates due to depreciating Yen and rising inflation



Source: Bloomberg

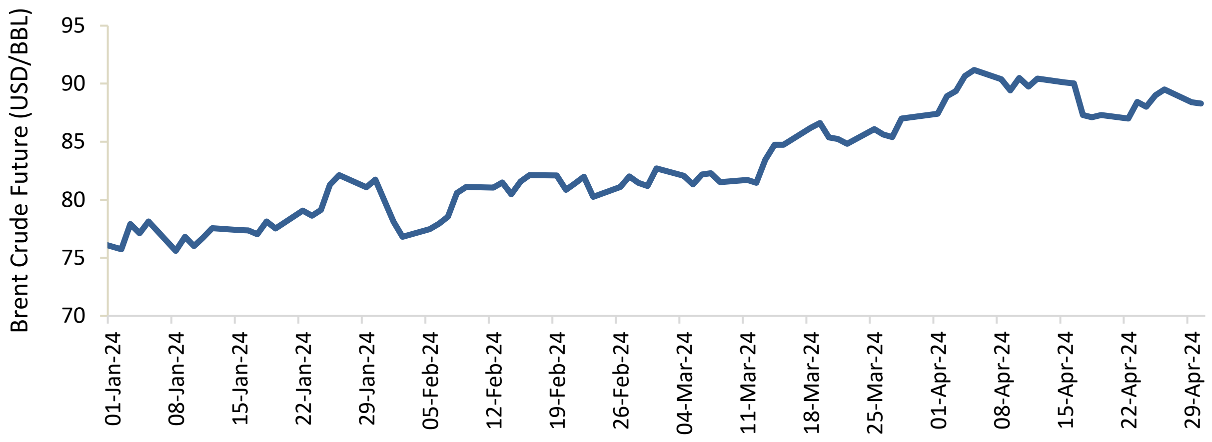
Rising rates may affect carry trade as Japan's holding of US Treasury is high



Source: Bloomberg

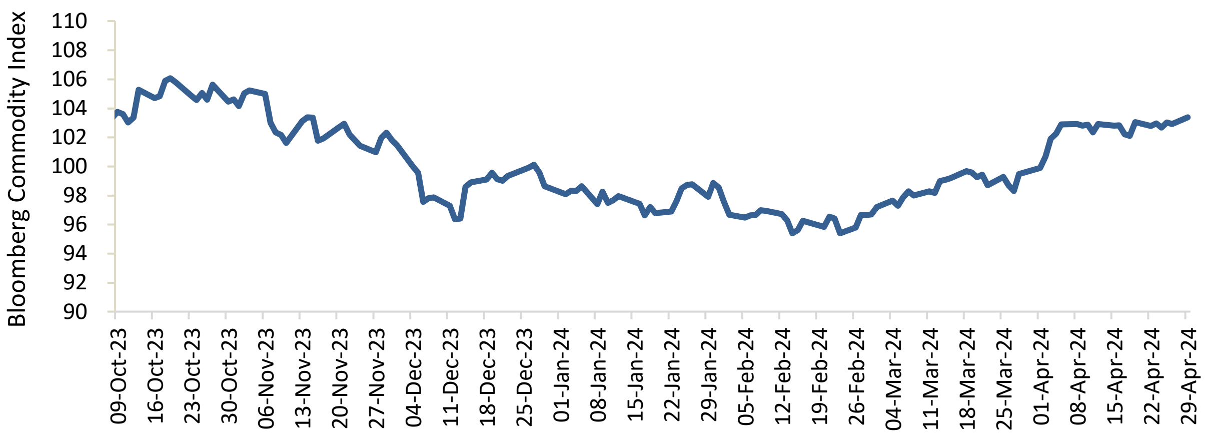
Inflation pulses are back due to escalating geopolitical tensions and uptick in global growth

Crude oil prices moved higher due to Middle East tensions



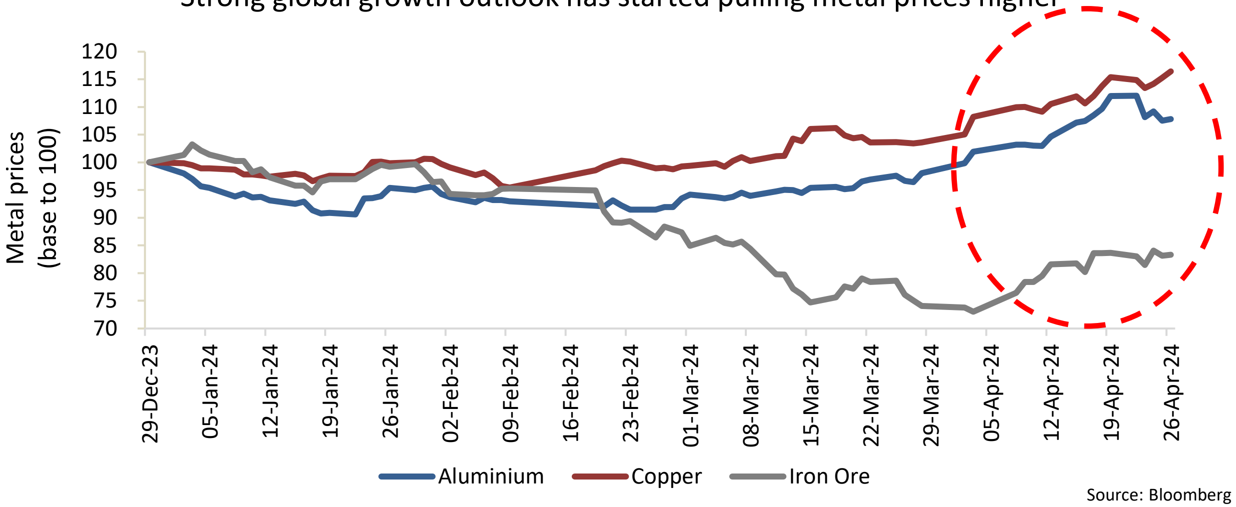
Source: Bloomberg

Deflationary nature of commodities seems to be nearing its end



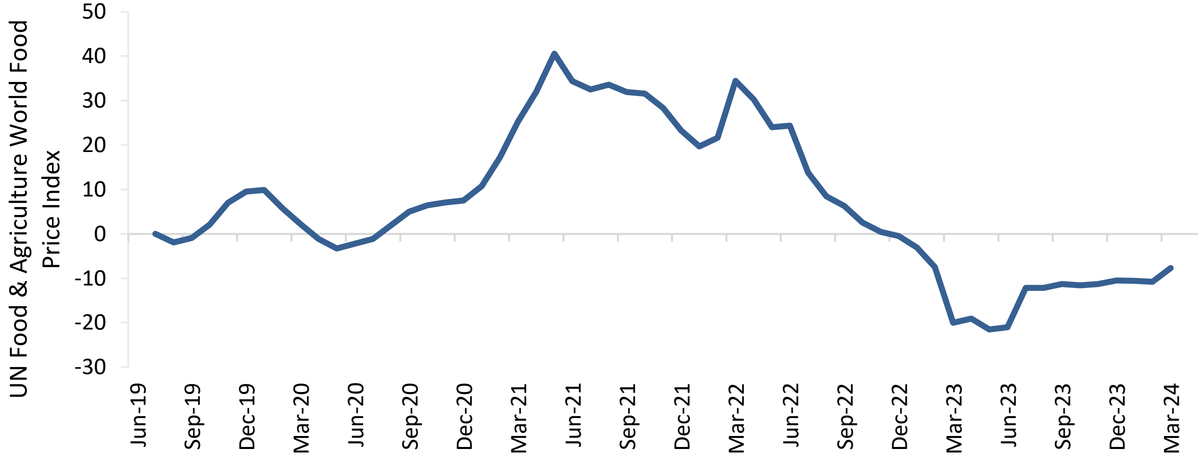
Source: Bloomberg

Strong global growth outlook has started pulling metal prices higher



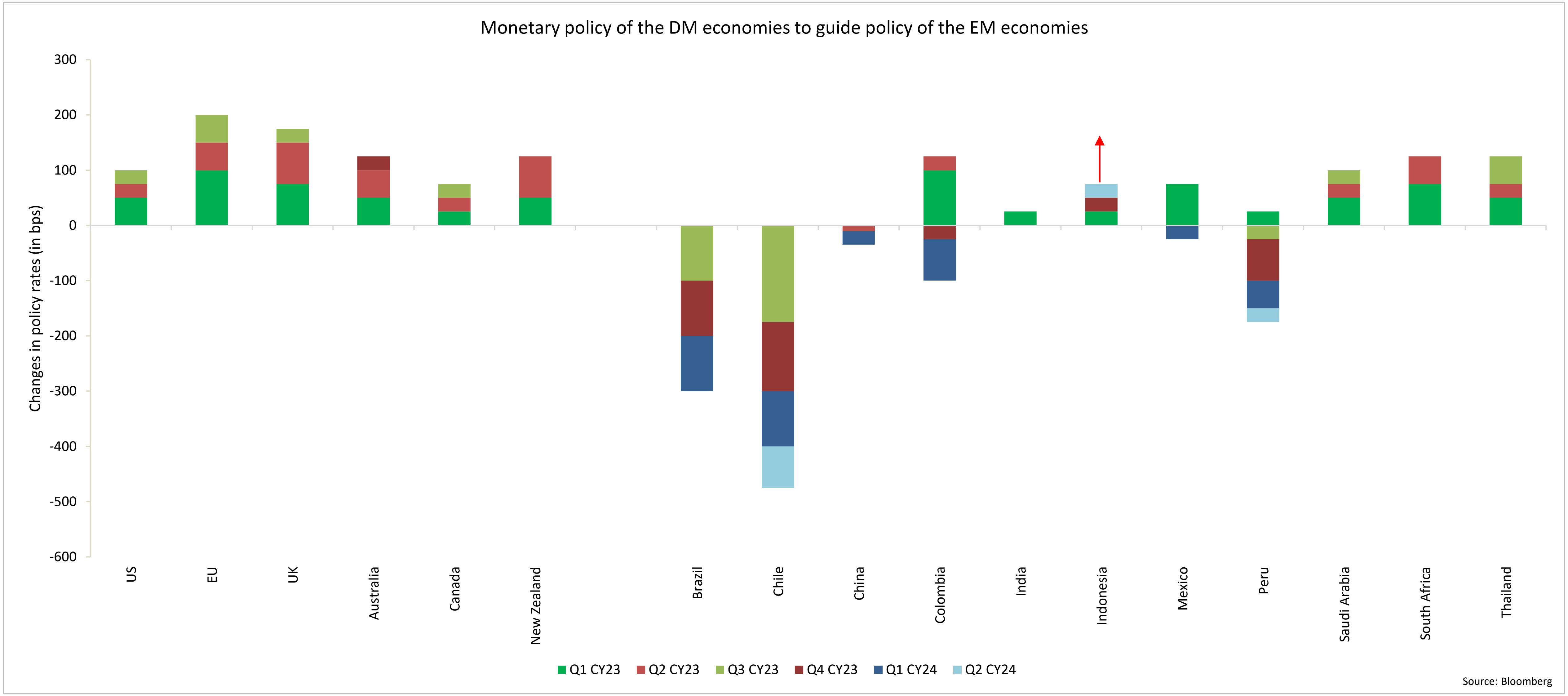
Source: Bloomberg

Benign food prices keeping overall inflation under check



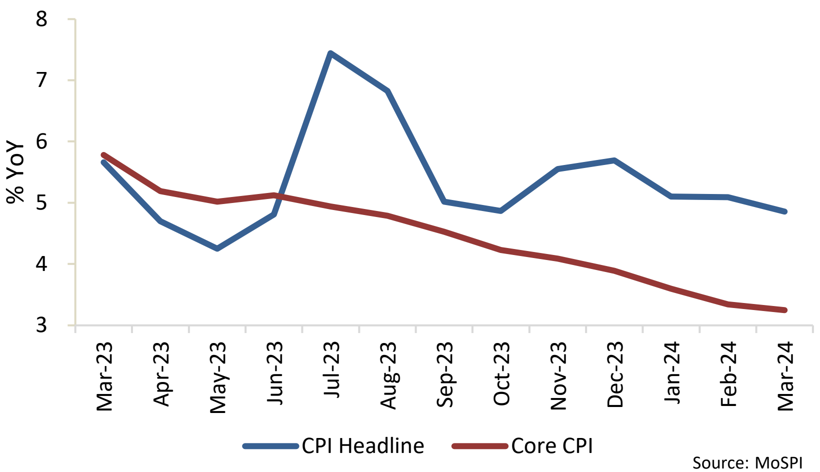
Source: Bloomberg

While most of the central banks are on the verge of rate cuts, few central banks have raised rates



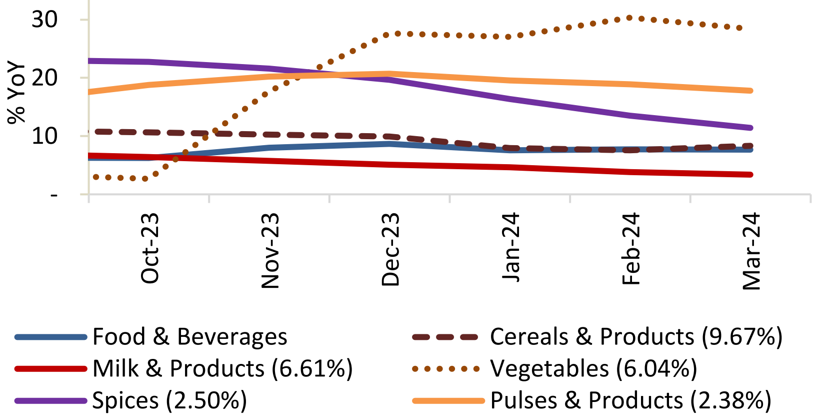
Domestic inflation under control on account of softening of food prices and continuous decline in core inflation…

Headline inflation moved below 5%



Source: MoSPI

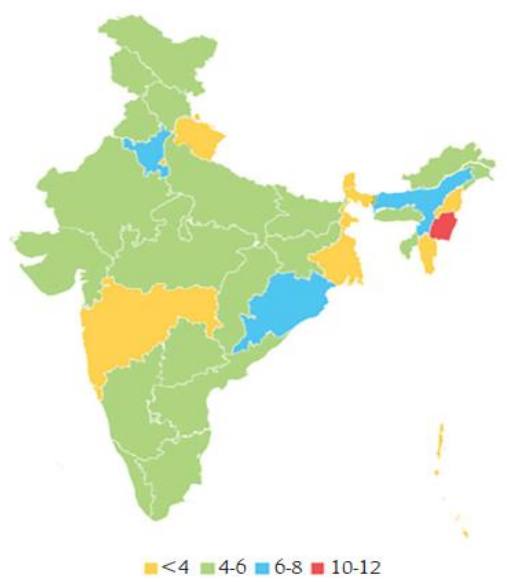
While food inflation moderated, vegetables prices remain high



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

Source: MoSPI

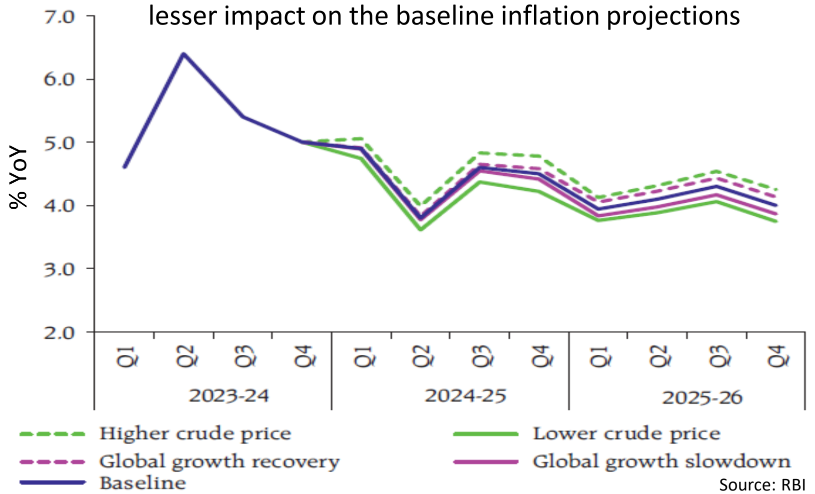
Majority of the states continued to record inflation in 4-6% range



Note: Map is for illustrative purposes only

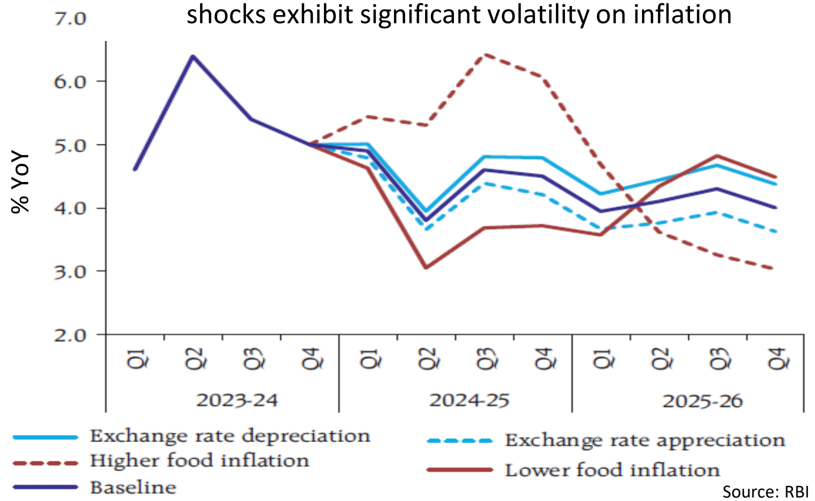
Source: NSD; RBI

Crude oil prices and global demand shocks to have lesser impact on the baseline inflation projections



Source: RBI

While exchange rates have moderate impact, food price shocks exhibit significant volatility on inflation



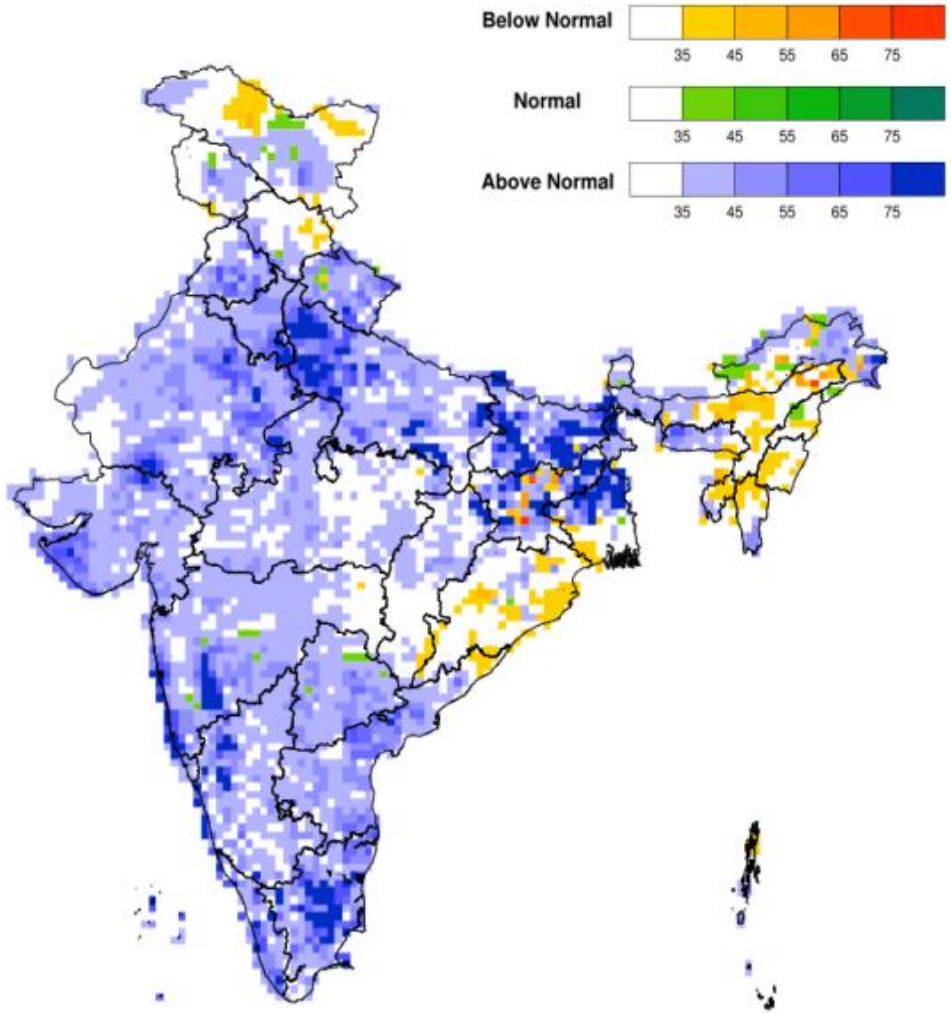
Source: RBI

"It is essential, in the best interest of the economy, that CPI inflation continues to moderate and aligns to the target on a durable basis. Till this is achieved, our task remains unfinished."

\- RBI Governor Shaktikanta Das

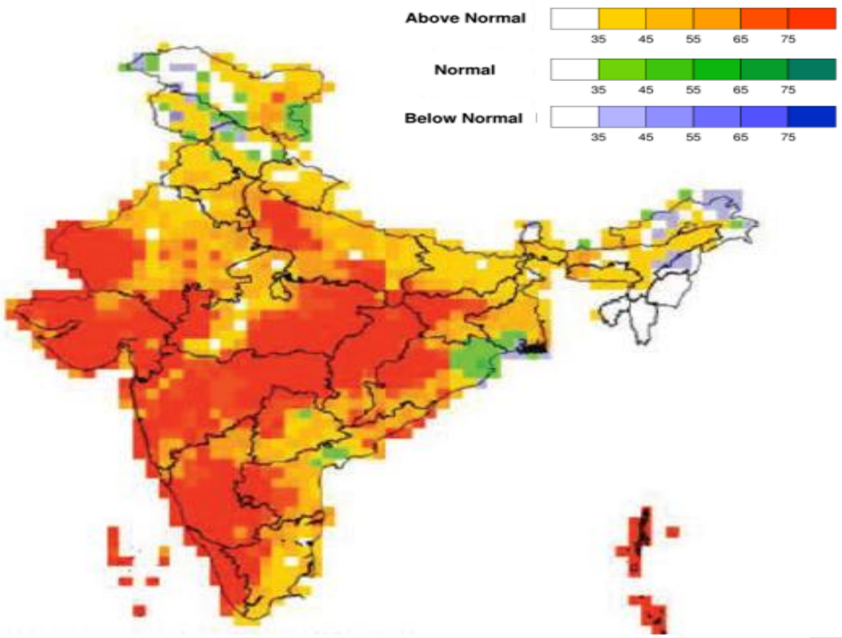
… Expectations of normal monsoon to further pull down the food prices

Early indication of above normal monsoon augurs well for the kharif season…



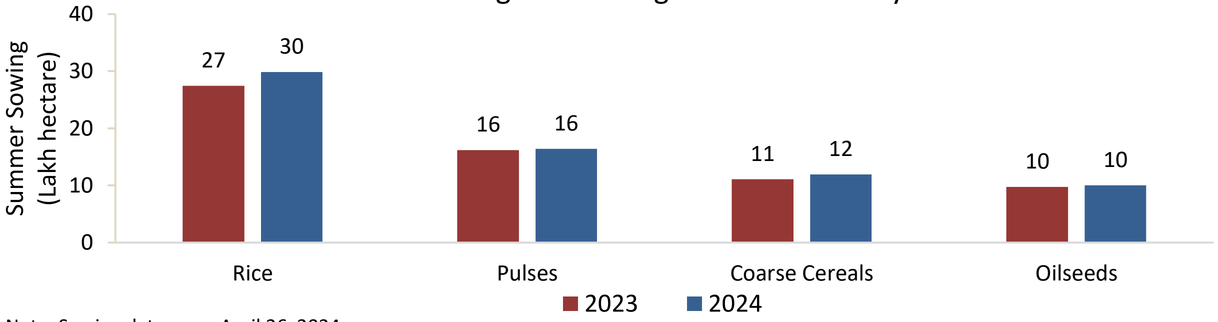
Source: IMD

…However, heatwaves could adversely affect farm productivity and vegetable prices



Source: IMD; RBI

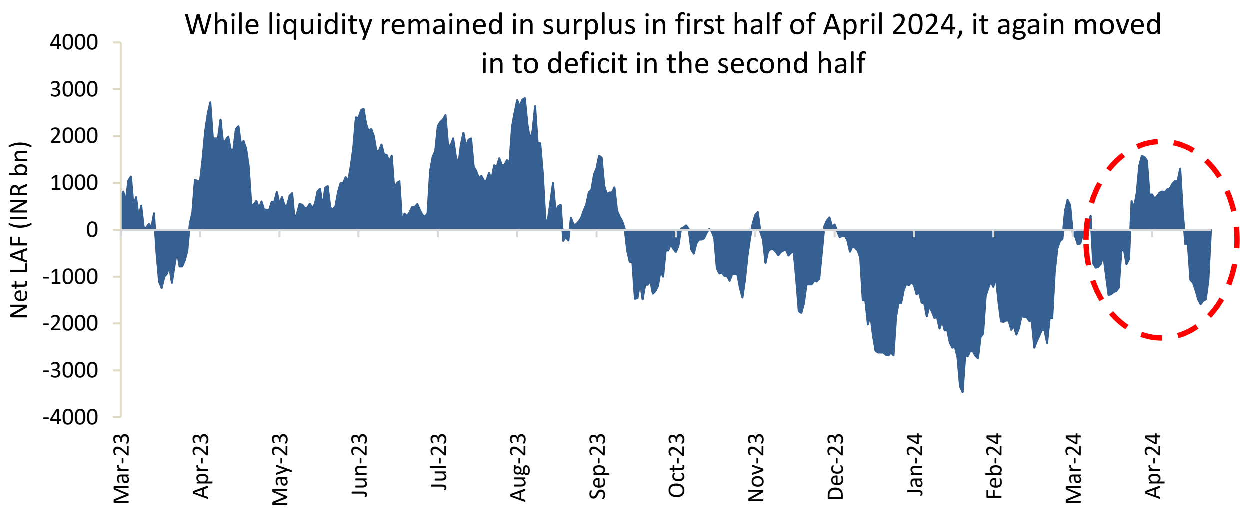
Summer sowing remains higher than the last year



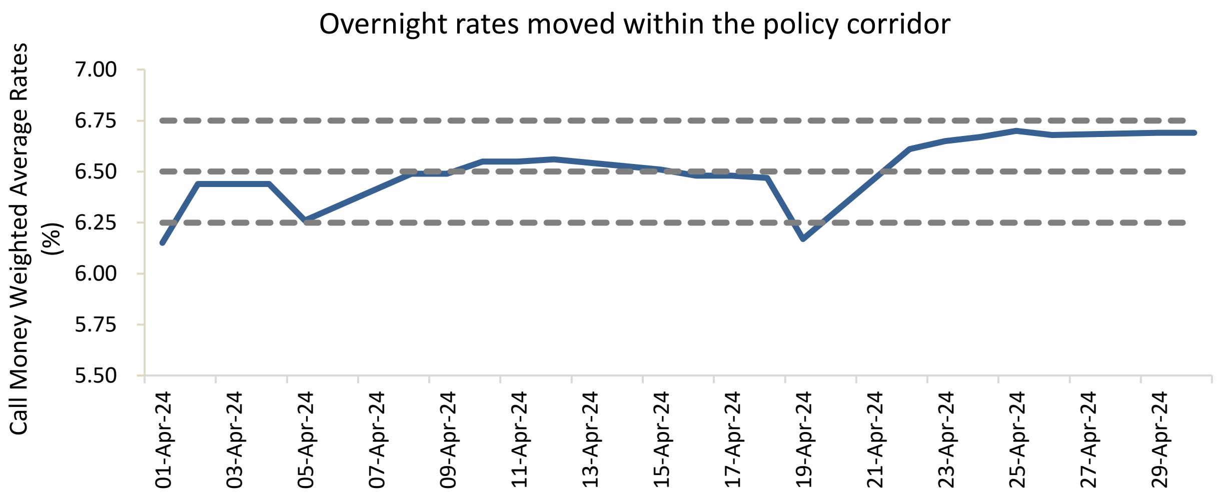
Note: Sowing data as on April 26, 2024

Source: Department of Agriculture & Farmers Welfare

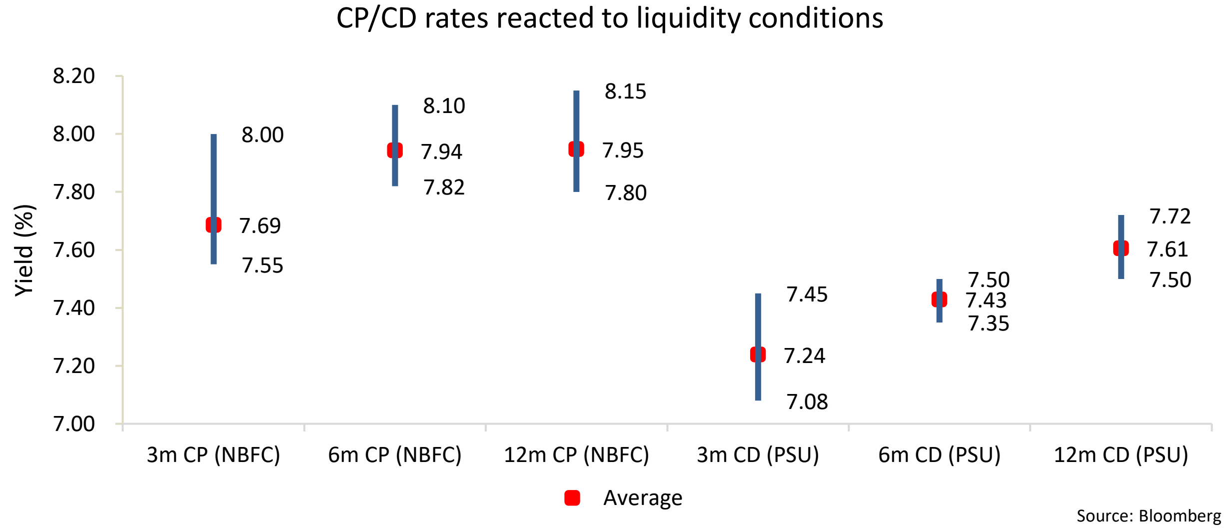
Liquidity continues to remain tight as the RBI ensures call rate remains around the repo rate



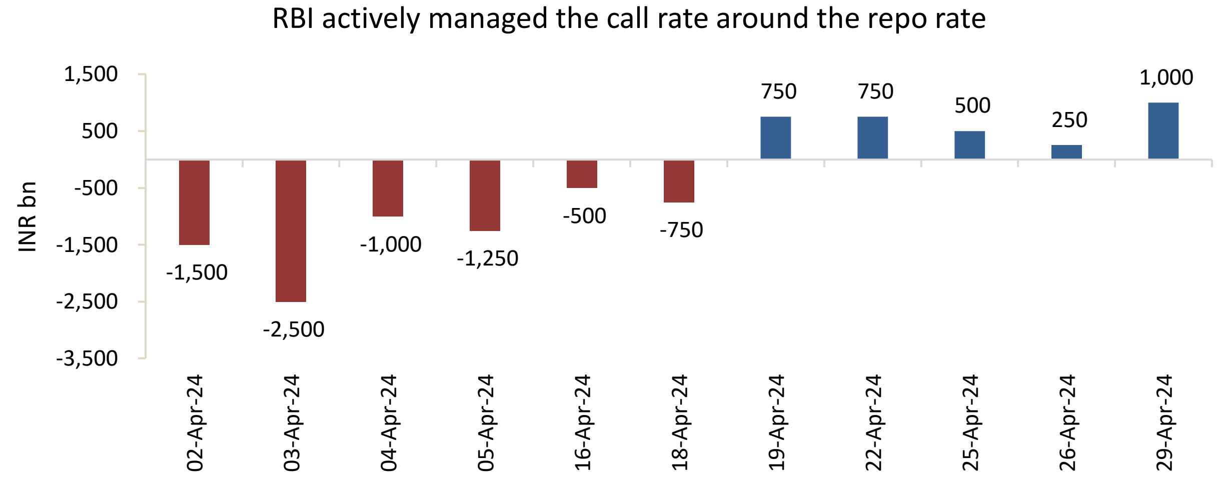
Source: Bloomberg



Source: Bloomberg



Source: Bloomberg

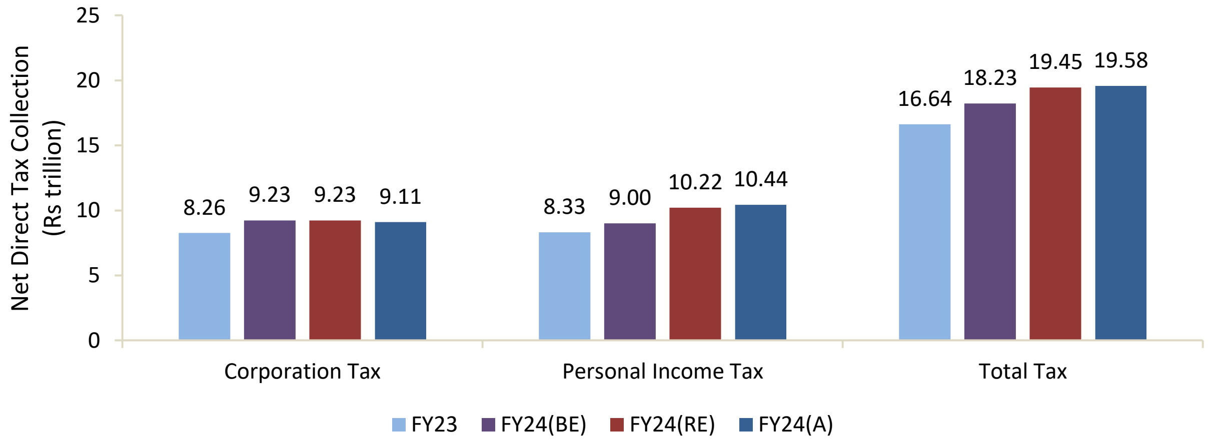


Note: VRR is denoted by positive value and VRRR is denoted by negative value

Source: RBI

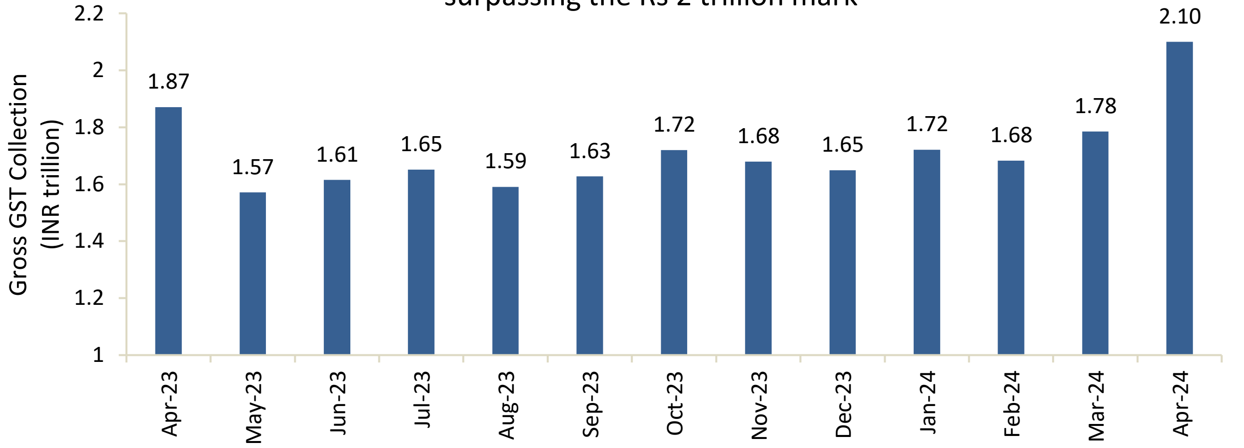
Tax collection remains strong… supporting fiscal conditions

Tax collection for FY24 surpassed the revised estimates



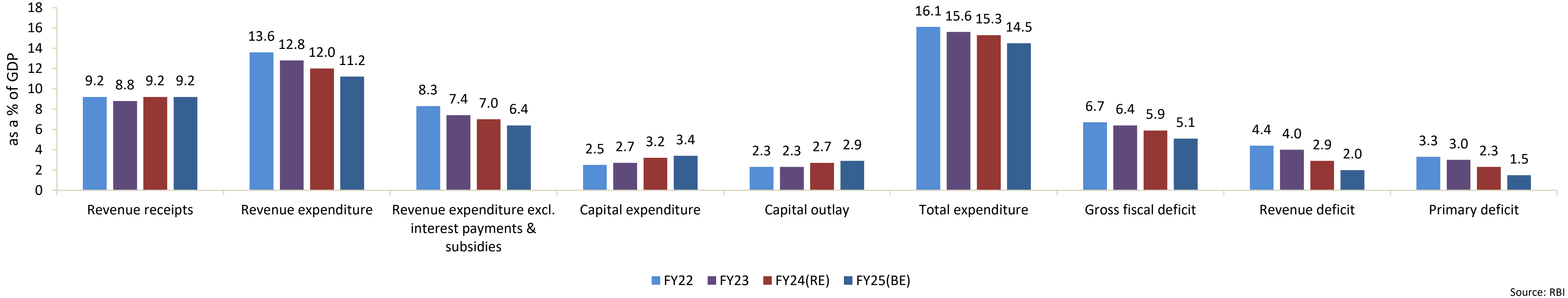
Source: Finance Ministry; Union Budget, Media Reports

Robust GST collection trend continues in FY25, with April 2024 collection surpassing the Rs 2 trillion mark



Source: Cogencis

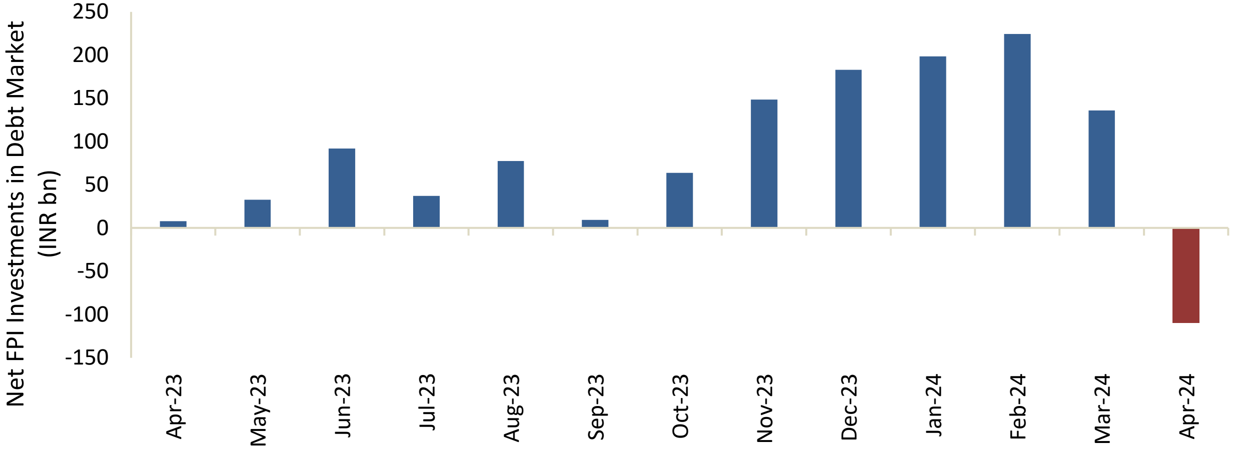
Strong direct and indirect tax collection providing support to fiscal deficit



Source: RBI

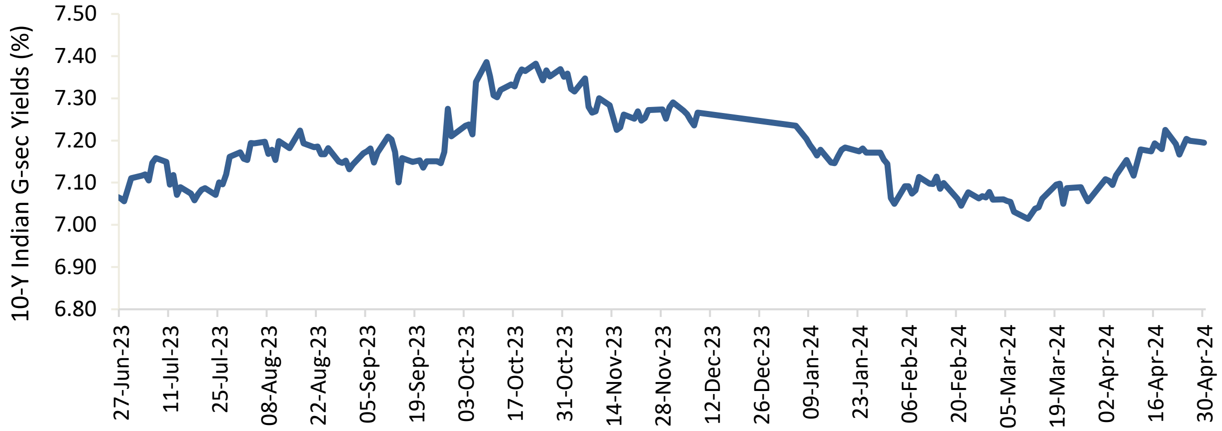
Despite inflation remaining in control, yields rose, predominantly tracking the rise in US Treasury yields and FPI outflows

FPIs turned net sellers after being net buyers for a year



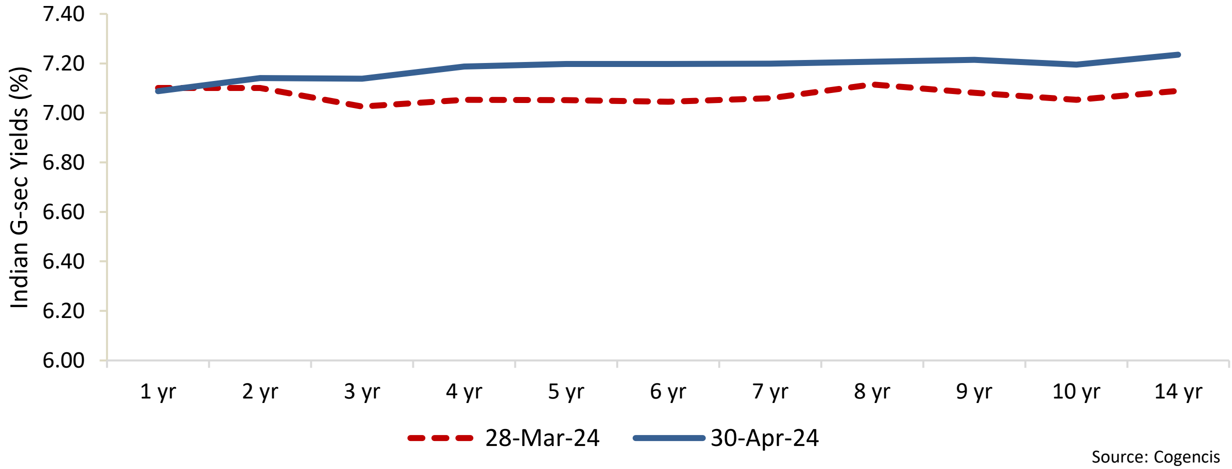
Source: NSDL

Higher US Treasury yields and FPI outflows pulled the yields higher



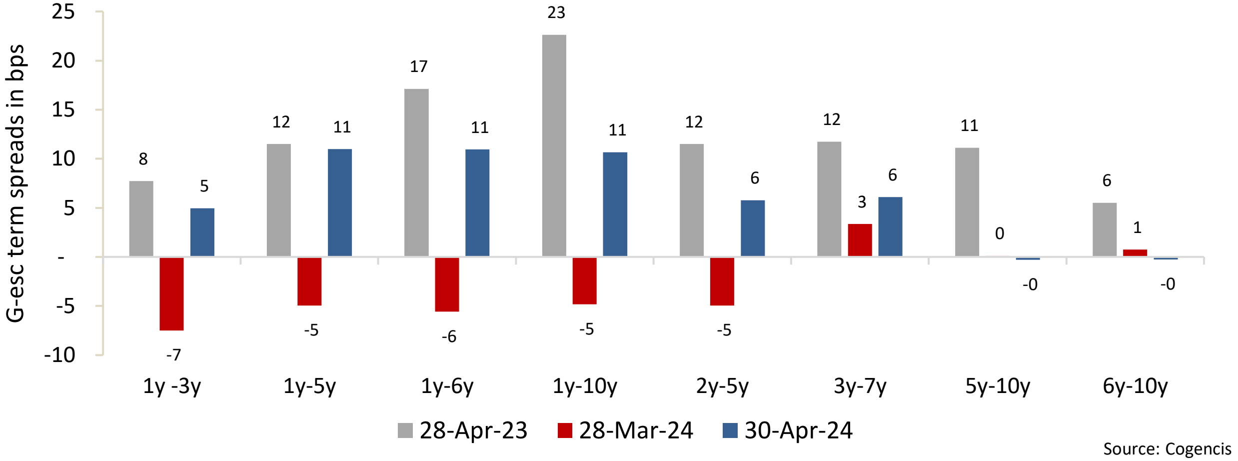
Source: Cogencis

Yield curve witnessed an upward parallel shift



Source: Cogencis

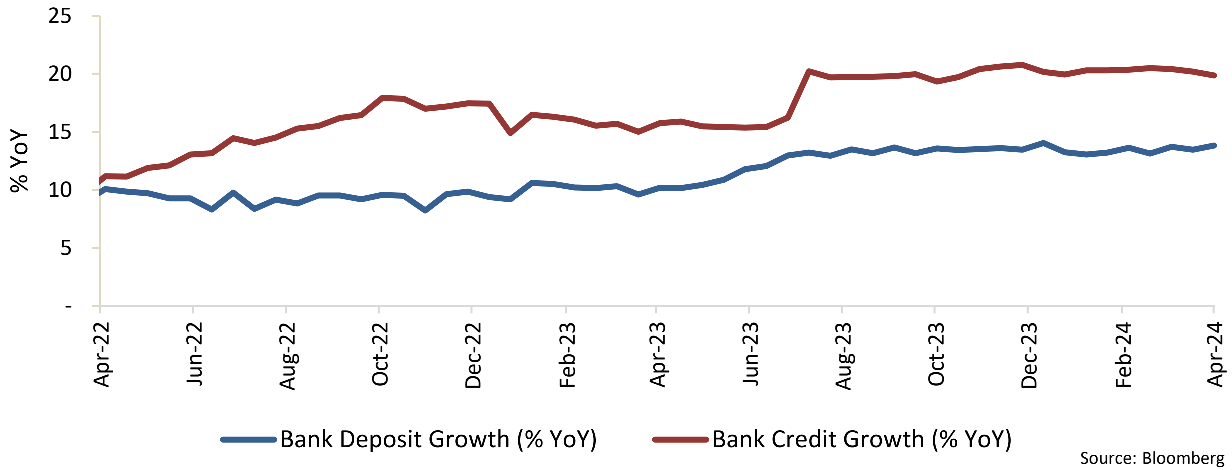
Yields at medium to longer inched higher, pulling up the term spreads on a MoM basis



Source: Cogencis

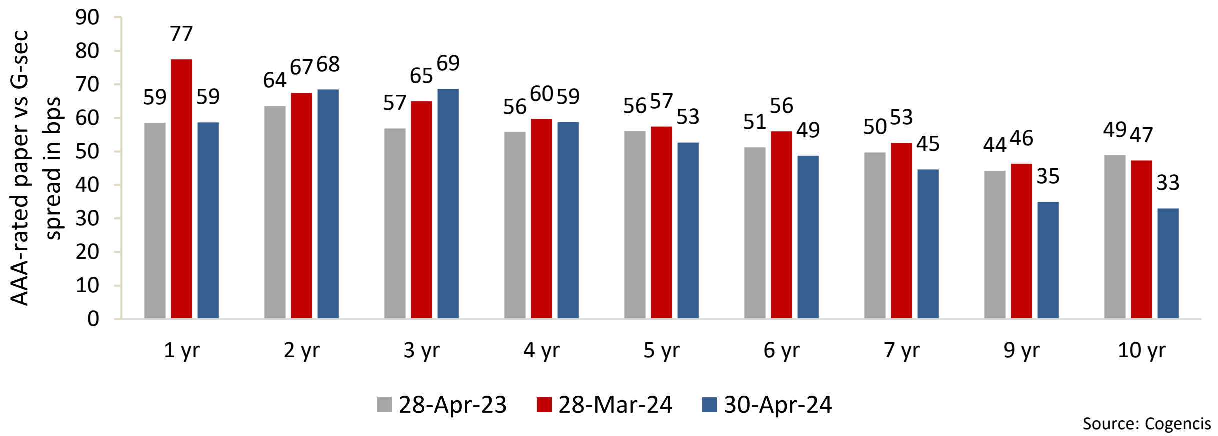
Corporate bond spreads remained relatively higher while SDL spreads came off making SDL less attractive

Demand for bank credit remains strong



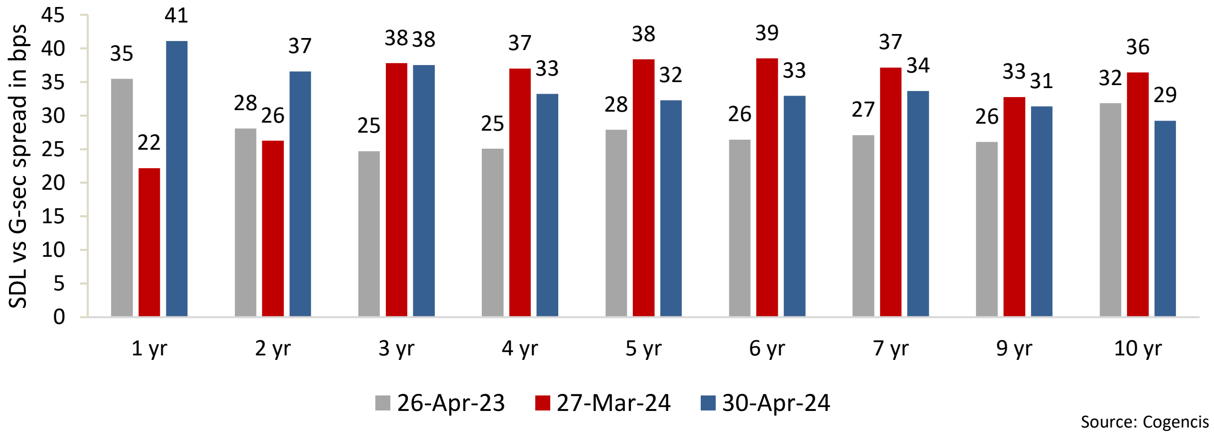
Source: Bloomberg

Higher demand for spread assets has pulled the corporate bond spreads down, yet they remain attractive at the shorter end



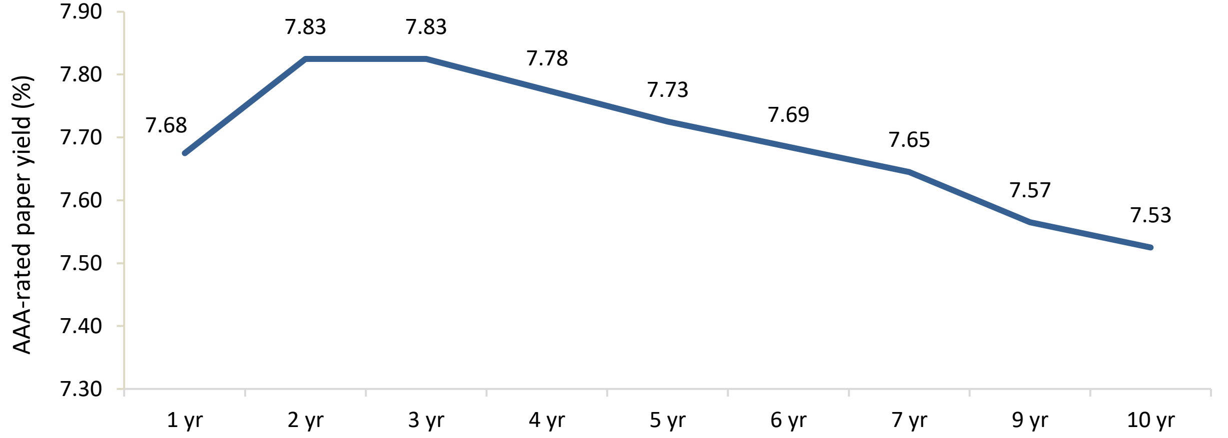
Source: Cogencis

Lower supply and higher demand for SDLs led to narrowing of spreads making SDL less attractive



Source: Cogencis

Tight liquidity keeping the corporate bond yield curve inverted



Source: Cogencis

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