HDFC Bank – Research Presentation

September 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 – September 2024

- Rising unemployment, consolidation in manufacturing PMI and deceleration in consumer sentiments suggest weakening growth impulses in the US. US Federal Reserve seems to be on its way towards a policy rate cut in September, to support growth and employment.
- Eurozone is showing mixed signals due to easing of financial conditions. While the service sector is doing well, the manufacturing sector is still struggling. The ECB has started to cut interest rates as the inflationary pressure in the EU seems to be abating, that has led to a gradual improvement in Eurozone economic sentiment indicators.
- Data points from China continue to remain steady, except from its real estate and consumption sectors, which has impacted its overall GDP growth. Stable PMI, stabilising GDP, improving trade data etc shows the gradual revival of the economy. Their Government and monetary authority also have been supportive of the growth effort. Multilateral agencies also expect better growth in the economy in the medium term.
- The base commodity prices have bounced from their recent lows on the back of decline in the Dollar Index and expectations of rate cuts in the US, which may help push demand. While the food price inflation globally is still weakening, the base effect could ensure that this data starts turning positive in time to come. The crude oil prices have been range bound on the back of supply pressure from OPEC+ and weakening growth impulses in key economies. The trouble in the Red Sea and shortage of containers has led to the rise in shipping costs for businesses across the world.
- With the US Fed signalling dovishness, the US Dollar index is likely to remain soft. That could potentially drive incremental FPI flows towards emerging economies.
- The Indian economy is on a consistent uptrend post the Covid period. Most multilateral agencies believe that this uptrend is likely to continue in the foreseeable future. Best in class GDP growth, strong PMI data, rising tax collections, improved Government balance sheet, all point towards a strong momentum going forward.
- While the GDP growth for Q1FY25 was marginally below expectations, the key reasons were the strong heat wave and lower government spending due to elections. With the government spending likely to normalise in the coming period, the GDP growth is likely to again start moving towards more normalised upward trajectory.
- Rural economy seems to be gathering momentum. Strong monsoons, higher crop acreage, strength in the real estate and construction activities bode well for rural economy. The Two-Wheeler sales and improving volume growth for FMCG companies are suggestive of improving consumption impulse in this segment. Fund managers, too, are gradually building these pointers into their investment decisions.
- Urban demand continues to see mixed impulses where the premiumisation trend continues. Passenger vehicle sales data has continued to decelerate, possibly on high base. Other indicators like personal loan growth and White collar job creation have remained steady. Consolidation in urban demand could be a cause for concern in the medium term and may push the Central and State Governments to bring in consumption supportive policies, at margin.
- Corporate and Banking sector balance sheets in India have shown strong improvement. The Corporate debt to equity has come off consistently, especially for the manufacturing sector. As the current capacity utilisation peaks in various sectors, releveraging by corporates can easily fund incremental private capex demand. As per data from the RBI, the capex intentions of the Private sector seems to be on an upswing. Sunrise sectors like Semiconductors, defence and electronics are likely to undertake new capacity creations. **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 re-rating looks a tough ask.**
- Liquidity conditions have begun to ease marginally and market participants expect RBI to gradually ease its policy stance. As the liquidity conditions ease, the growth trajectory of the economy could further see a 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 Smallcap indices are markedly higher than the Largecap index. The fund managers are generally looking to add into defensive sectors like Consumption, FMCG and Pharma.
- 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 remain 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. Aggressive investors may also look at Business Cycle Funds for allocation. All allocations should be done in line with the risk profile and product suitability of the investor.**

Debt Mutual Fund Strategy

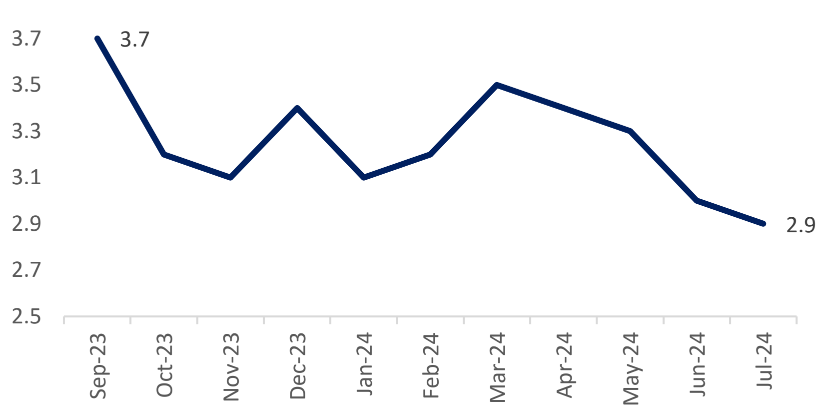
- With favourable demand-supply dynamics in Indian G-Secs, tactical opportunities can emerge at the longer end.
- Also, accrual opportunities at the 1-3-years segment of the corporate bond yield curve remains attractive for incremental investment, from risk-reward perspective.
- As corporate bonds are available at reasonable spreads of similar tenor G-Secs, 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 24 months and above, investors can look at Dynamic Bond Funds.
- Whereas for a horizon of 3 months and above, investors can consider Arbitrage Funds.
- 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

US economy: Declining inflation & rising unemployment pushes US Fed to hint for rate cut

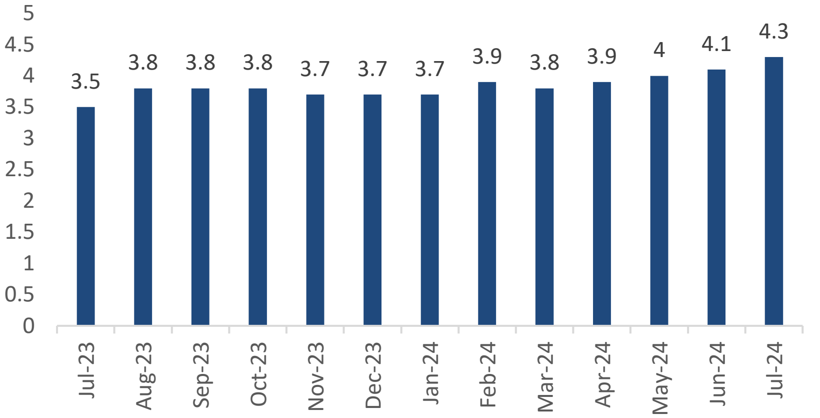
US Consumer Price Index (YoY %)

Inflation seems to be moderating



Source: Bloomberg

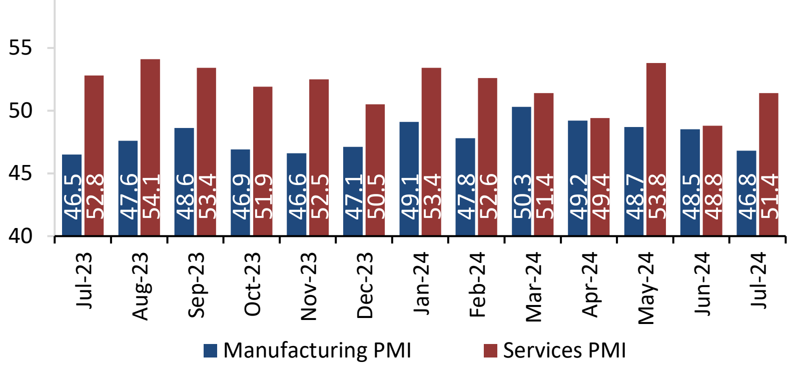
US Unemployment Rate Rising (%)



Source: Bloomberg

US Manufacturing & Services PMI

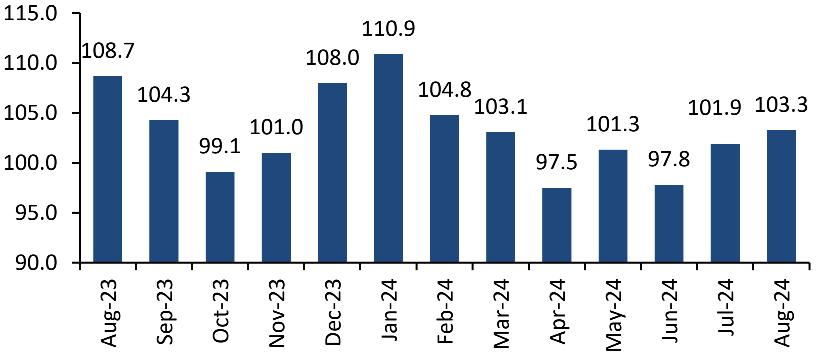
Slowdown in manufacturing can be seen while services still remain strong



Source: Bloomberg

US Consumer Confidence Index

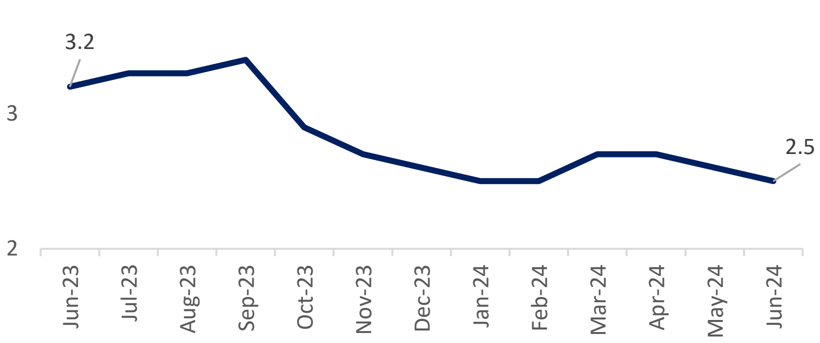
Stability in consumer confidence visible



Source: Bloomberg

US Personal Consumption Expenditure (YoY %)

Personal consumption in US continues to deteriorate, rate cut could drive consumption



Source: Bloomberg

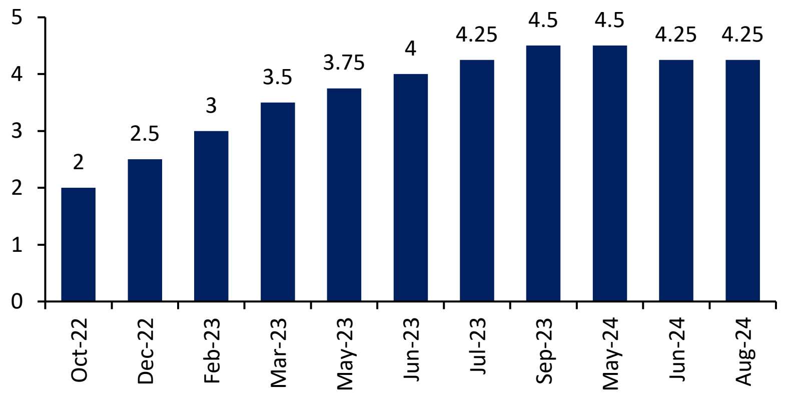
Takeaways from Fed Chair Powell's speech at Jackson Hole Symposium

- "Confidence has grown that inflation is on a sustainable path back to 2%," Powell said in his keynote speech at the Fed's annual economic conference in Jackson Hole.
- Powell suggested that rate cuts are all but inevitable. "The direction of travel is clear, and the timing and pace of rate cuts will depend on incoming data, the evolving outlook, and the balance of risks," he said.

Eurozone: Mixed signals emanating

ECB Main Refinancing Rate (%)

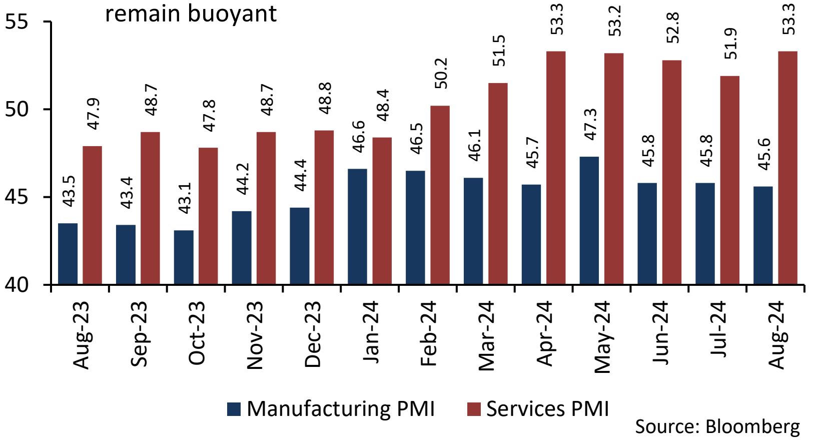
ECB holding rate post recent rate cut



Source: Bloomberg

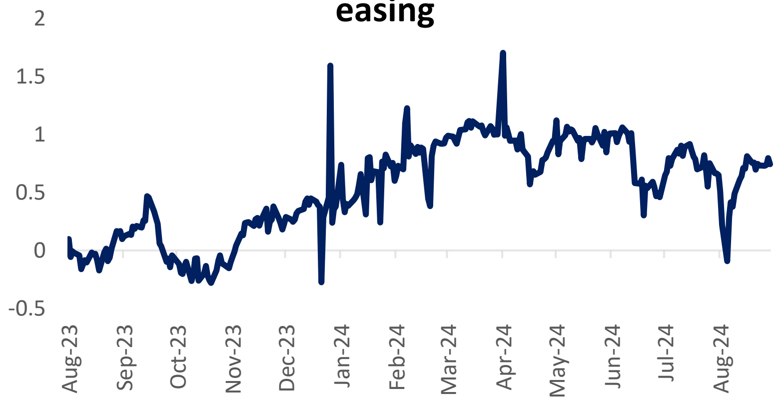
S&P Global Eurozone PMI

Manufacturing under pressure, Services remain buoyant



Source: Bloomberg

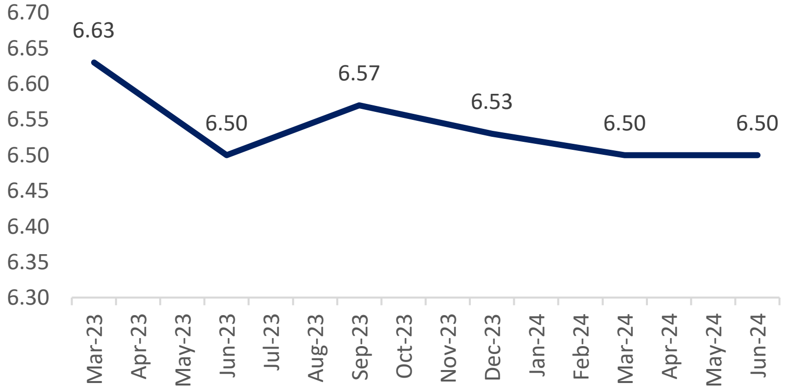
Euro area Financial Conditions Index easing



Source: Bloomberg

Eurozone Unemployment Rate (%)

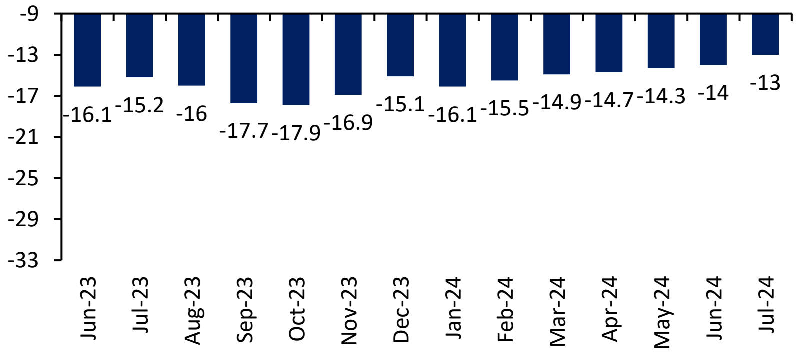
Improving marginally, however, at a slow pace



Source: Bloomberg

Eurozone Consumer Confidence Indicator

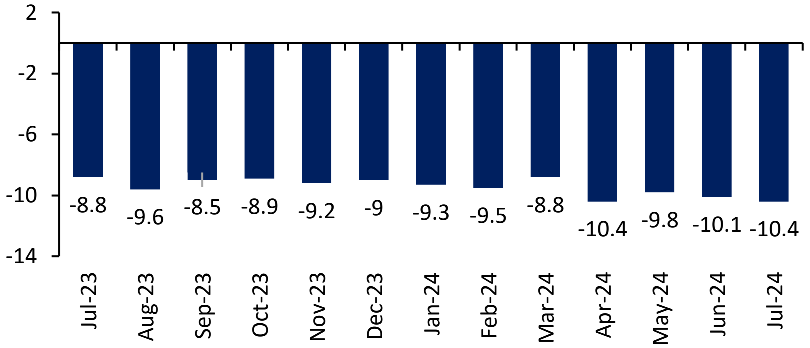
In the negative territory, but improving at the margin



Source: Bloomberg

Eurozone Industrial Confidence Indicator

Weakness persists with no signs of improvement

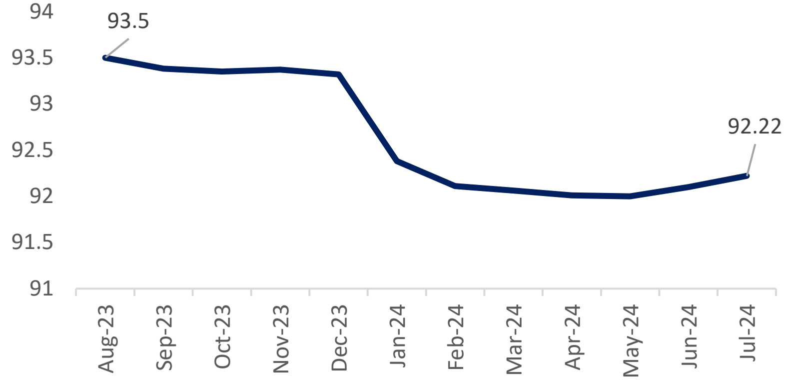


Source: Bloomberg

China: Domestic Consumption dragging, exports remain strong… GDP holding up

China Real Estate Climate Indicator

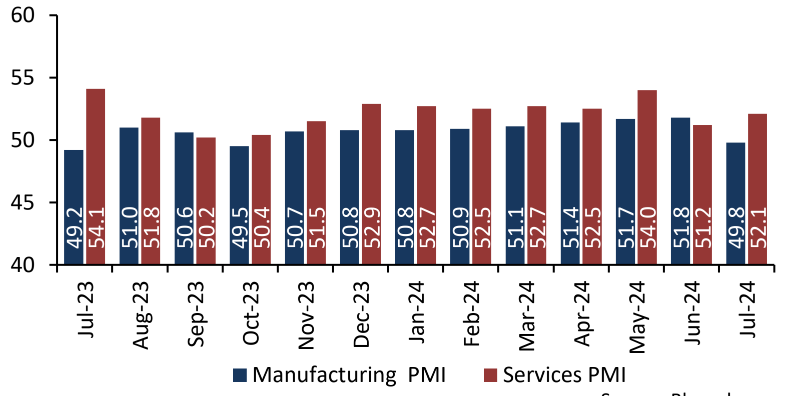
Chinese real estate market remain under pressure



Source: Bloomberg

China Manufacturing & Services PMI

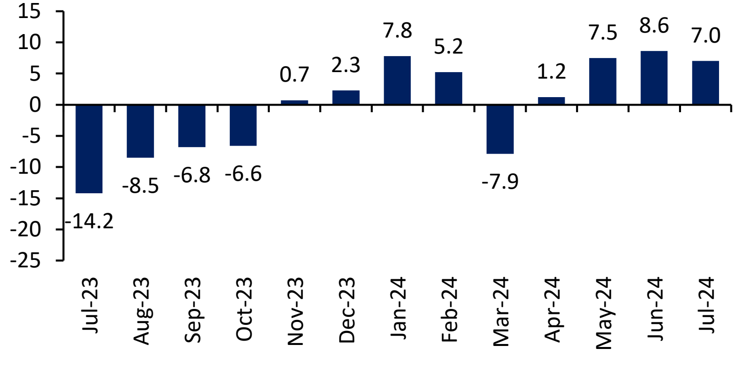
Manufacturing weak, services holding up



Source: Bloomberg

China's Export Growth (In USD Terms) - YoY Change (%)

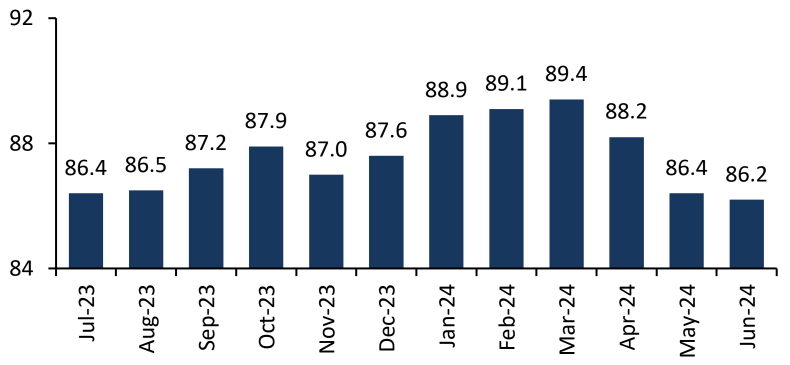
Momentum continues



Source: Bloomberg

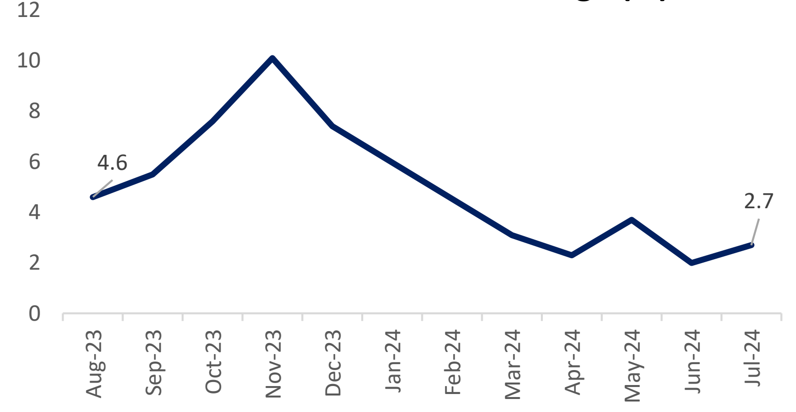
China Consumer Confidence Index

Declining of late…yet steady



Source: Bloomberg

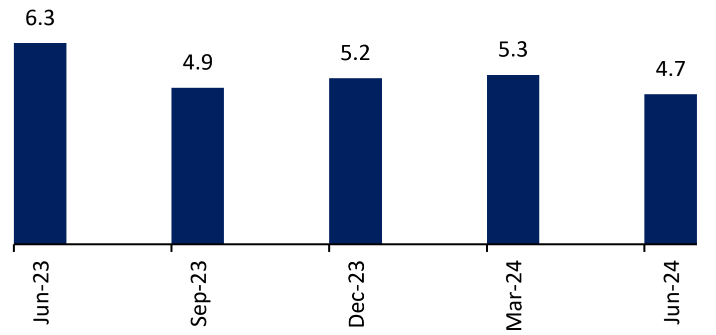
China Retail Sales - YoY Change (%)



Source: Bloomberg

China Quarterly GDP - YoY Change (%)

Holding up… though below expectations

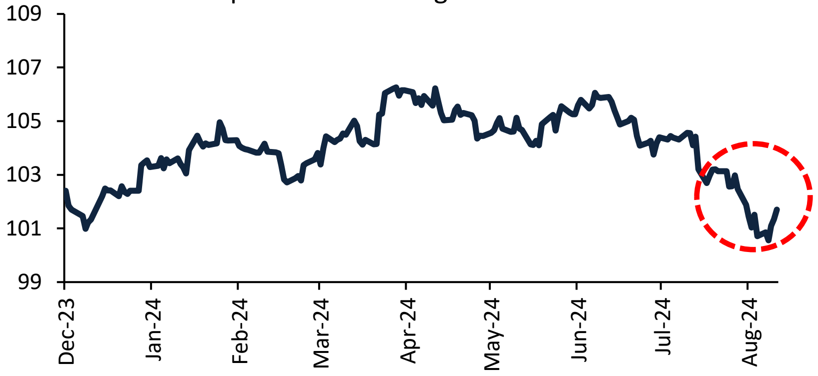


Source: Bloomberg

Commodities: Base metals bounce on the back of decline US Dollar Index and expectations of Rate cuts across key economies

US Dollar Index

Rate cut expectations leading to weakness in dollar index



Source: Bloomberg

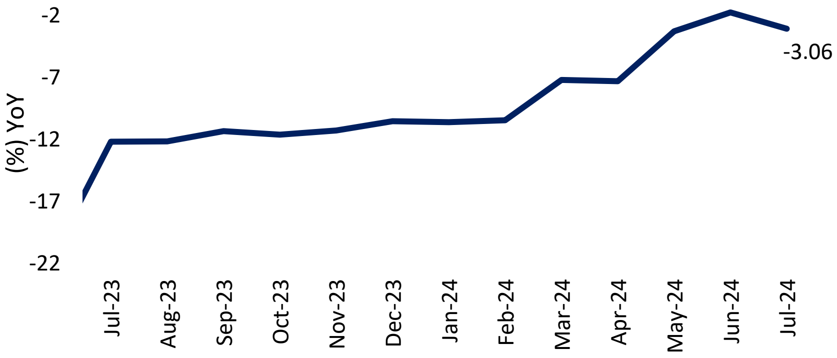
Bloomberg Industrial Metal Index

Prices bounced reflecting weak dollar index

Source: Bloomberg

UN Food & Agriculture World Food Price Index

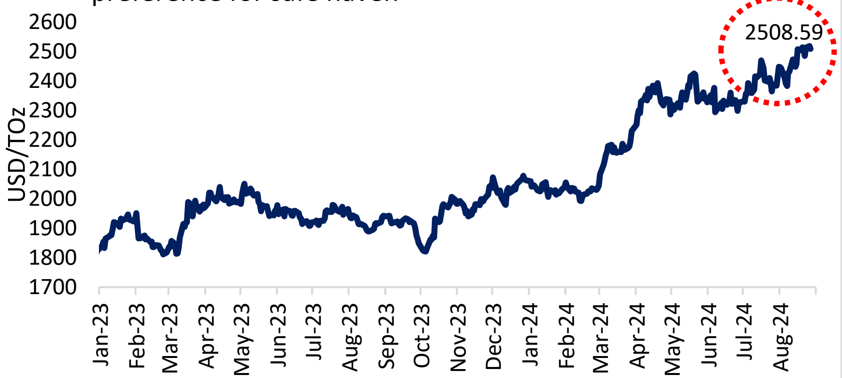
Food prices ease a little with seasonal availability



Source: Bloomberg

Gold (USD Per Troy Ounce)

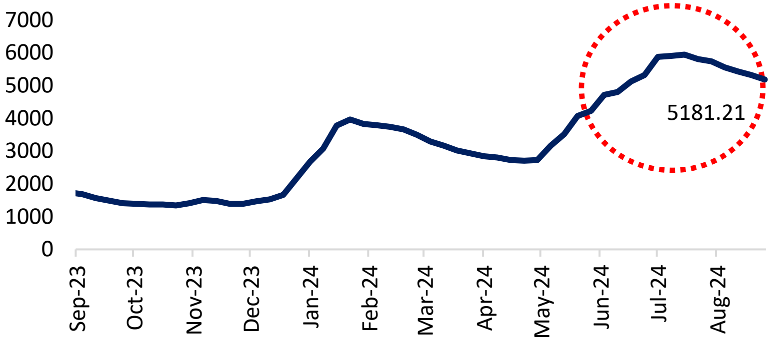
Prices at all time high on back of geopolitical tensions and preference for safe haven



Source: Bloomberg

Drewry World Container Index per 40 Foot Box

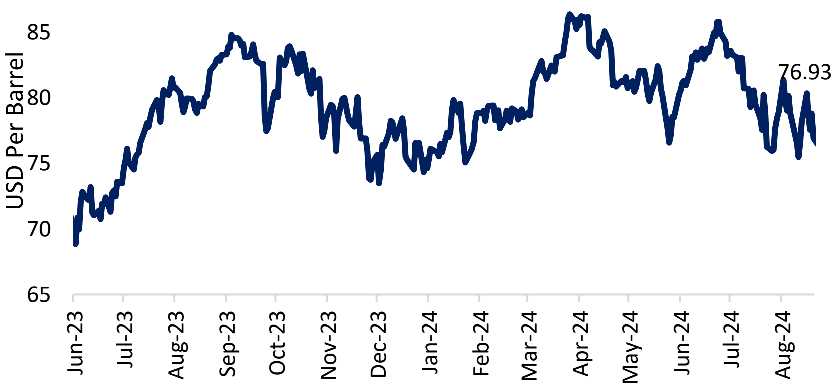
Red sea crisis coupled with container shortages pushing rates higher



Source: Bloomberg

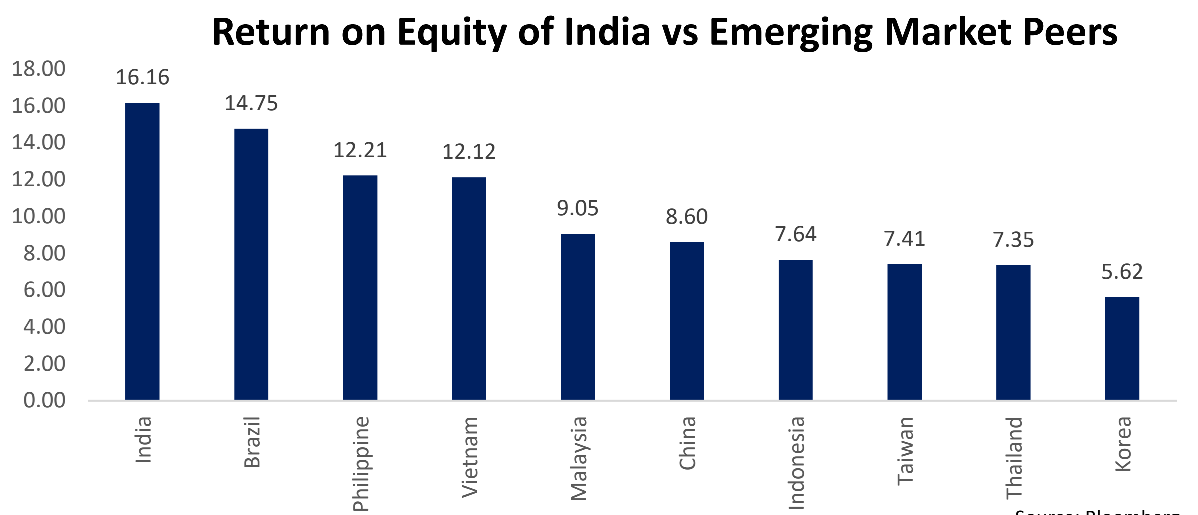
Brent Crude Oil (USD Per Barrel)

Tight supply from OPEC & weak growth keep oil prices in a range

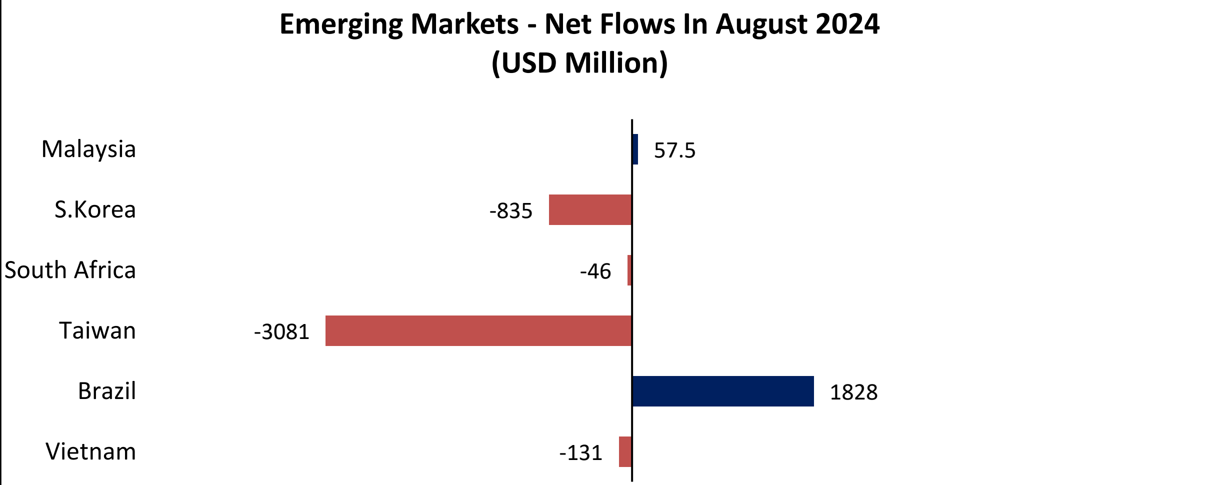


Source: Bloomberg

Indian valuations higher than EM basket due to superior ROE and growth prospects

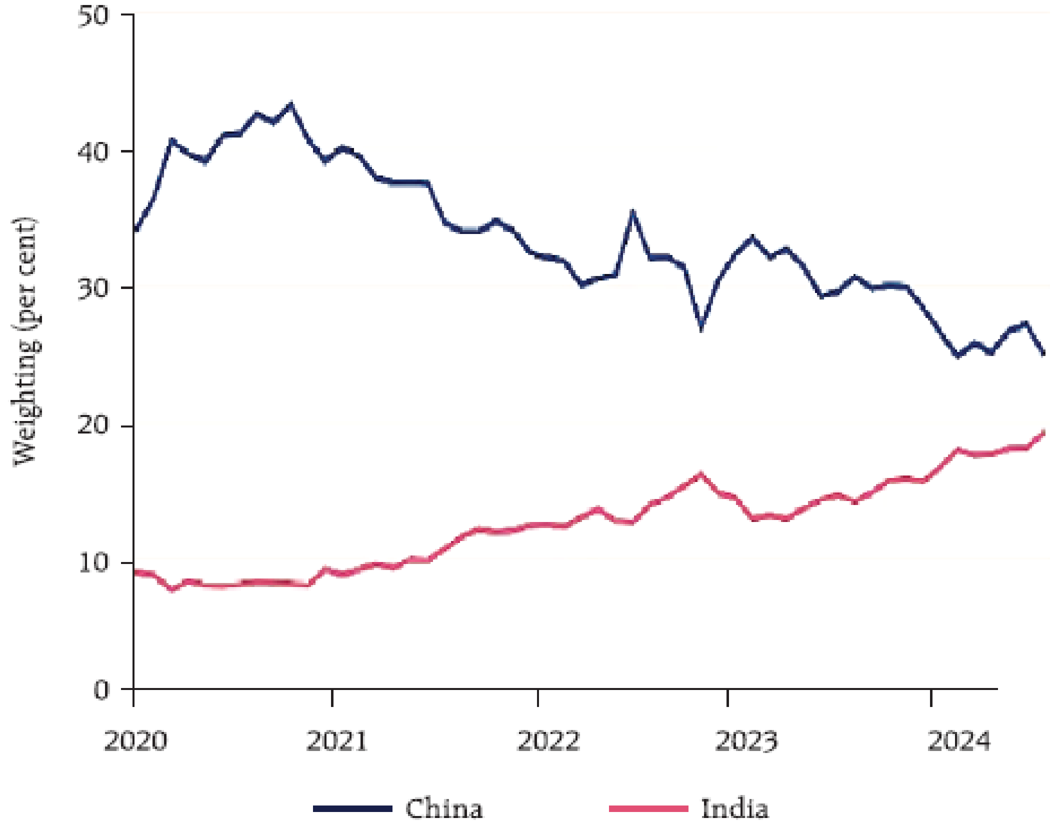


Source: Bloomberg



Source: Bloomberg

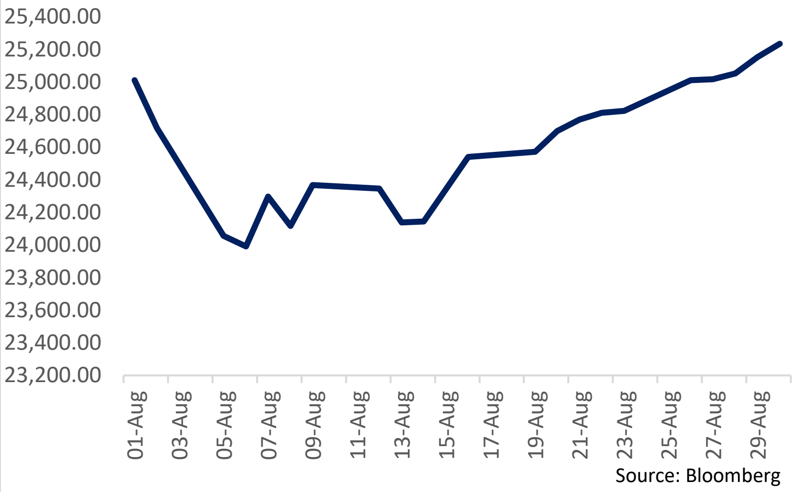
India's share in the MSCI emerging markets index has been increasing in recent years, driven by strong macro fundamentals and robust growth in earnings of Indian companies.



Source: MSCI; RBI

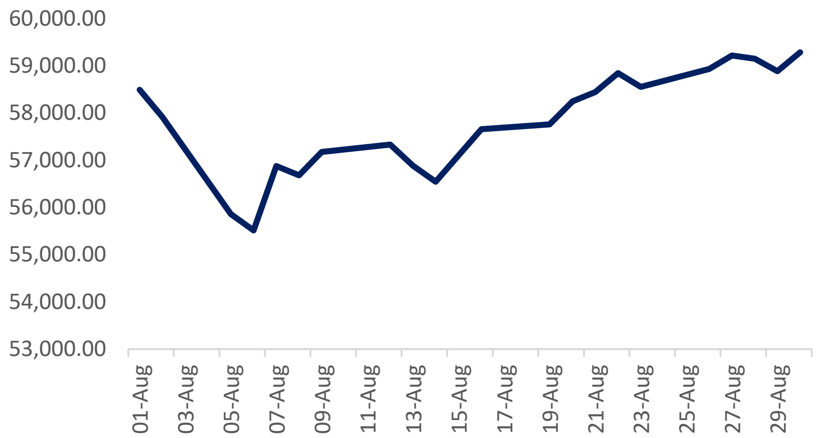
Indian markets remained on an uptrend in August on the back of continued flows from DII / FPI's and positive macro data…despite weak Q1 earnings

Nifty 50 price movement



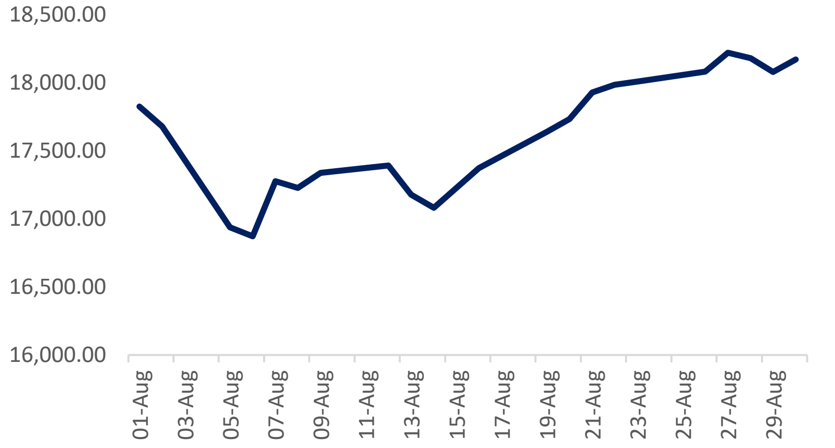
Source: Bloomberg

Nifty Midcap 100 price movement



Source: Bloomberg

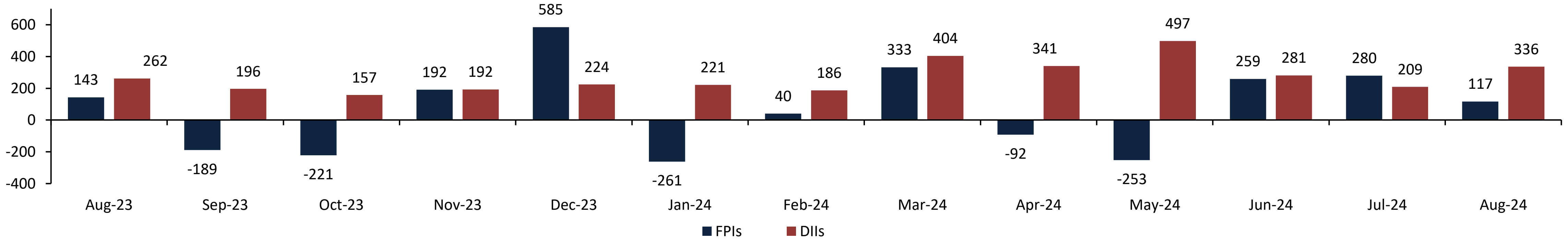
Nifty Smallcap 250 price movement



Source: Bloomberg

Net Flows In Equities (Rs Bn)

DIIs and FPIs were net buyers in the month of August



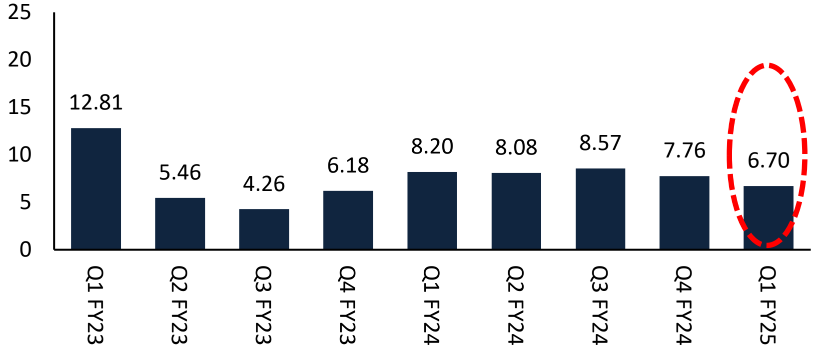
*For 2024, FPI and DII data is up to 30th August, 2024

Source: SEBI, CDSL

While GDP growth moderated in Q1FY25 on back of heatwaves and government spending restrictions due to elections…. Yet India remains fastest growing large economy

Real GDP Growth - YoY Change (%)

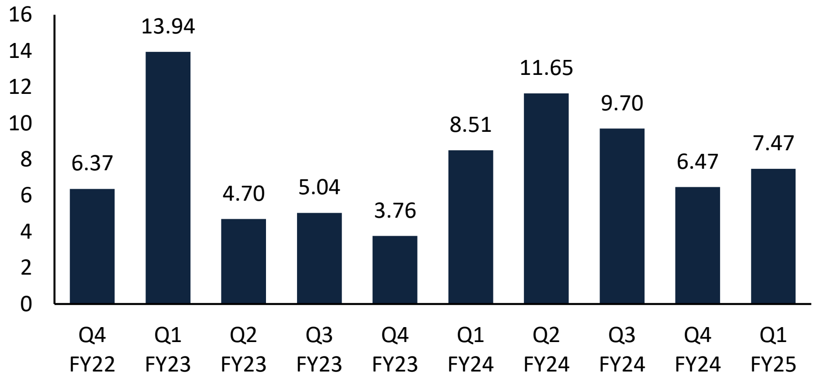
Q1FY25 GDP growth marginally below expectations



Source: Bloomberg

Gross Fixed Capital Formation - YoY Change (%)

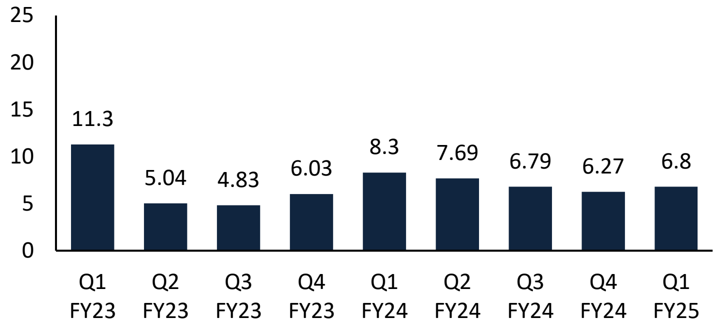
Momentum sustaining



Source: Bloomberg

Gross Value Added - YoY Change (%)

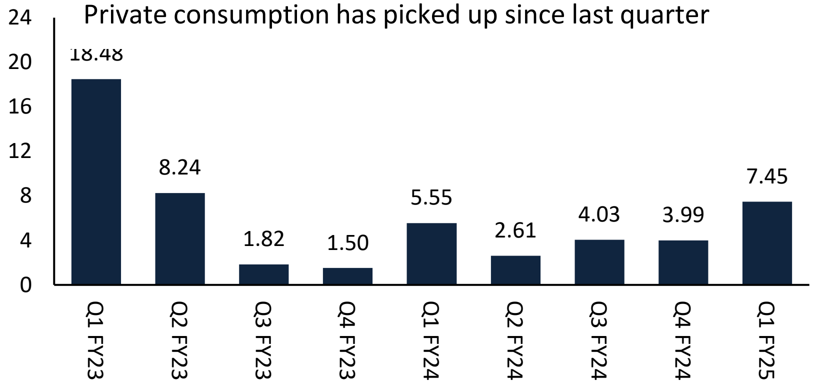
Continues to remain steady



Source: Bloomberg

Private Final Consumption Expenditure - YoY Change (%)

Private consumption has picked up since last quarter



Source: Bloomberg

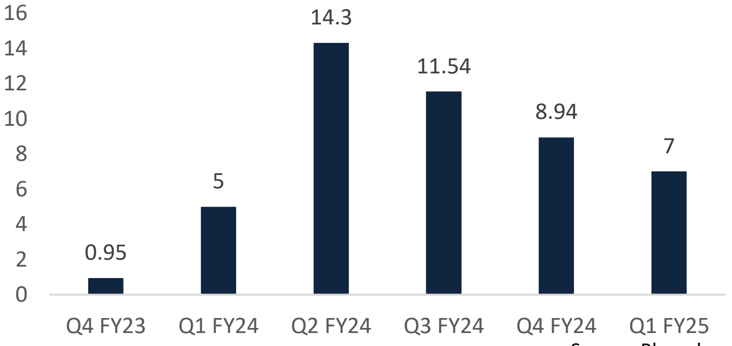
Govt Final Consumption Expenditure - YoY Change (%)

Strong public capex has been a key GDP growth driver, however public capex seems to be losing steam

Source: Bloomberg

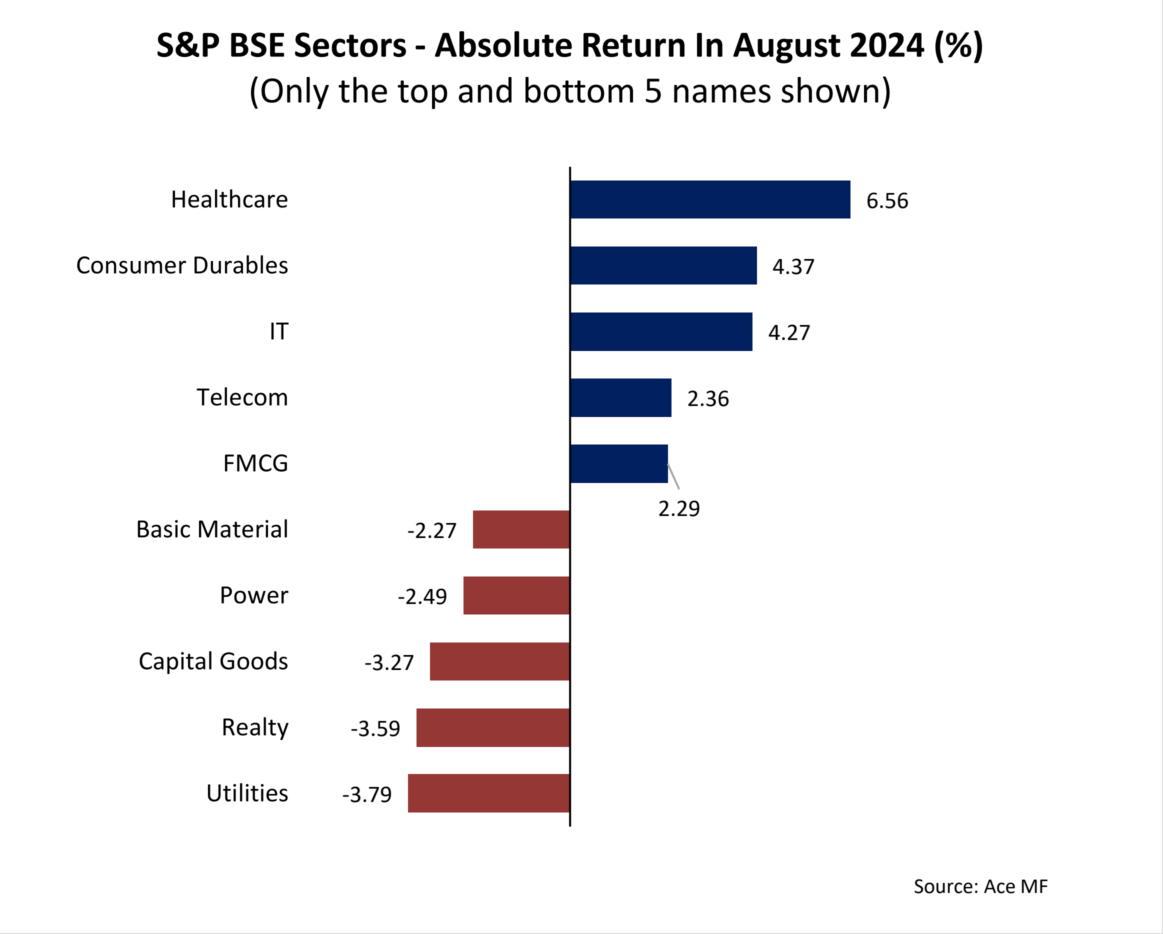
Manufacturing growth YoY Change (%)

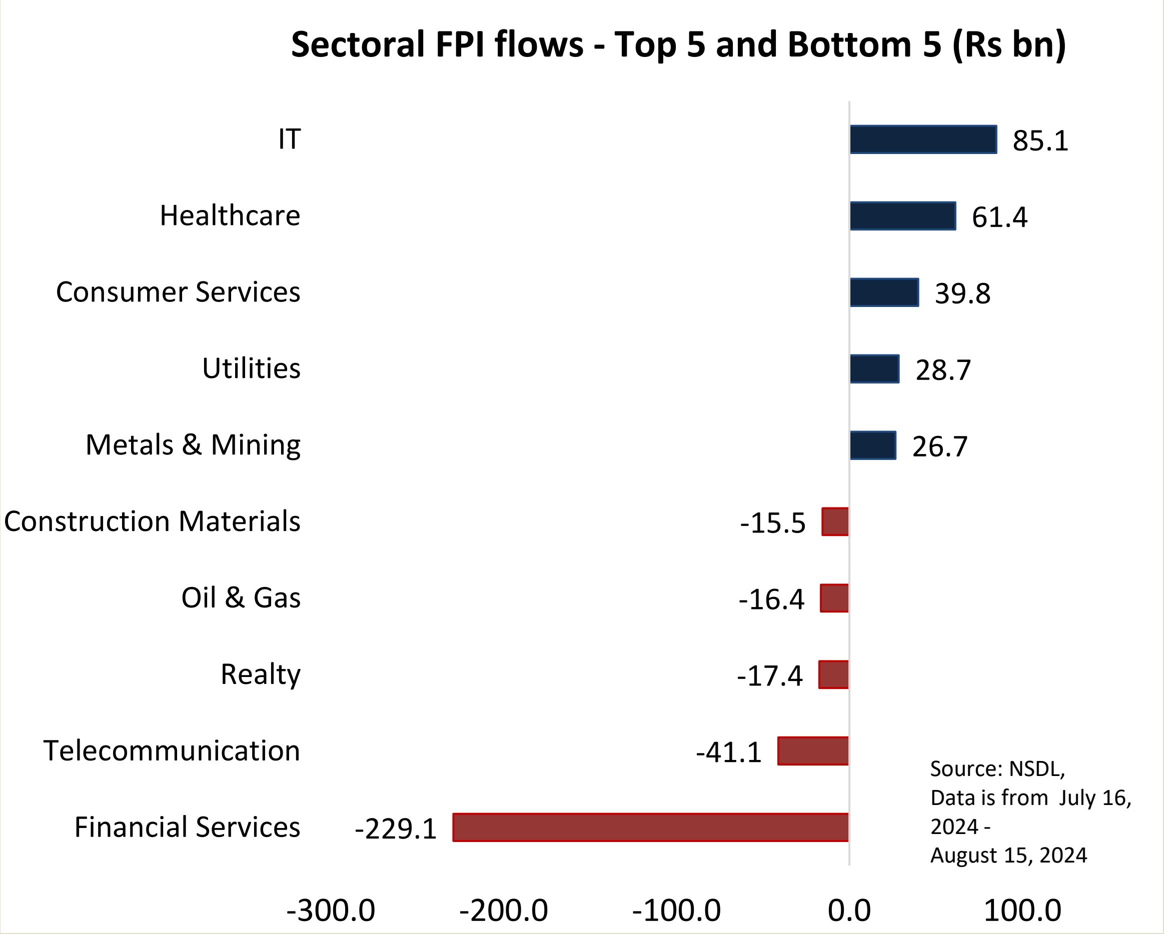
Manufacturing activities on a decline



Source: Bloomberg

Sectoral performance and FPI flows in August 2024

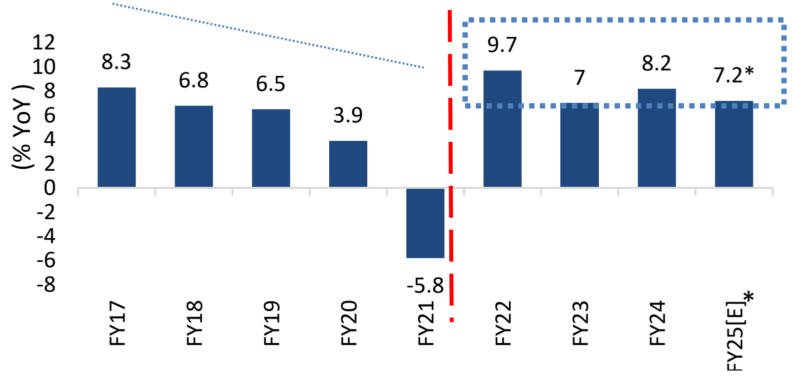




India – Macros continue to remain strong

Real GDP Growth

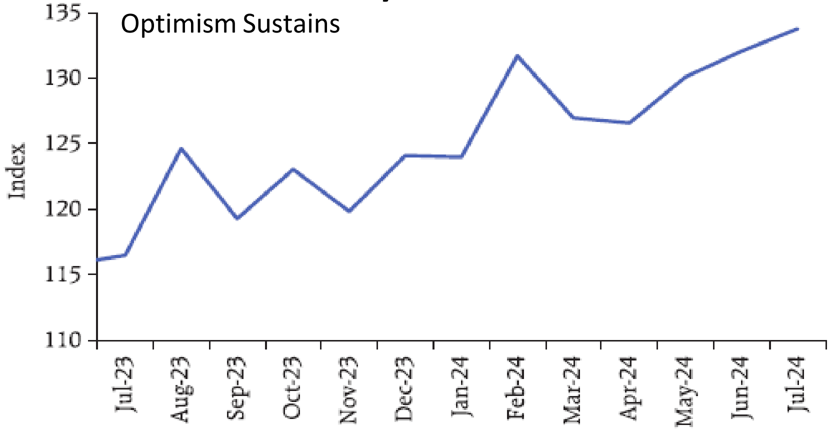
Structural shift in sustainable growth at higher level



Source: MoSPI, RBI*

Economic Activity Index

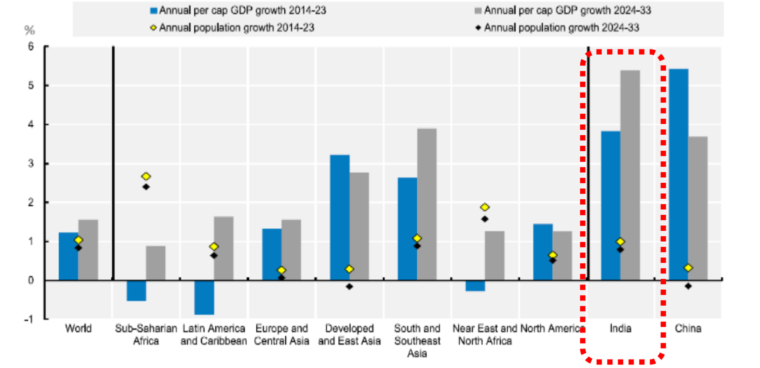
Optimism Sustains



Source: RBI

Annual GDP Per Capita & Population Growth Rate

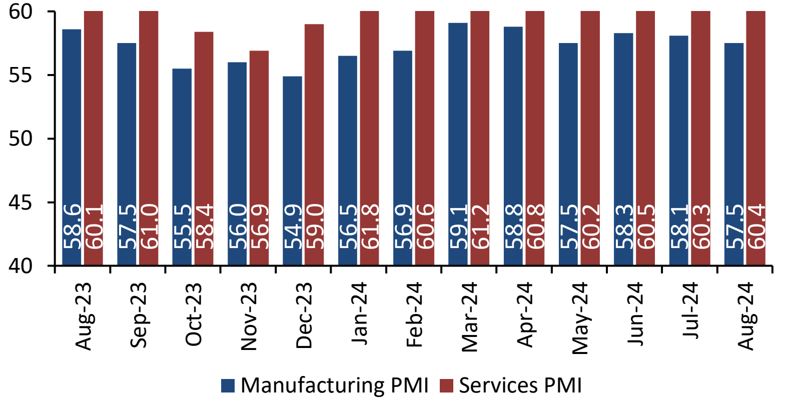
OECD projects higher GDP growth per capita for India, which could drive demand



Source: OECD and FAO secretariats calculations based on UN Population Prospects 2022, *IMF World Economic Outlook* 2023 and *OECD Economic Outlook* 2023 numbers.

HSBC India PMI

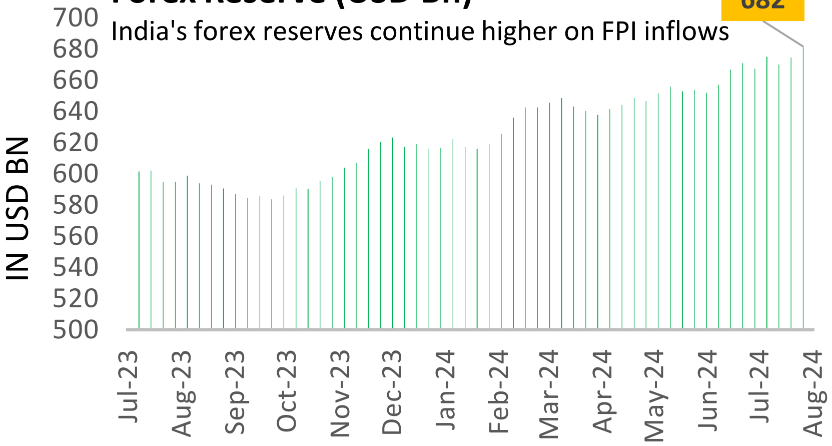
Manufacturing decelerates, services remain strong



Source: Bloomberg

Forex Reserve (USD Bn)

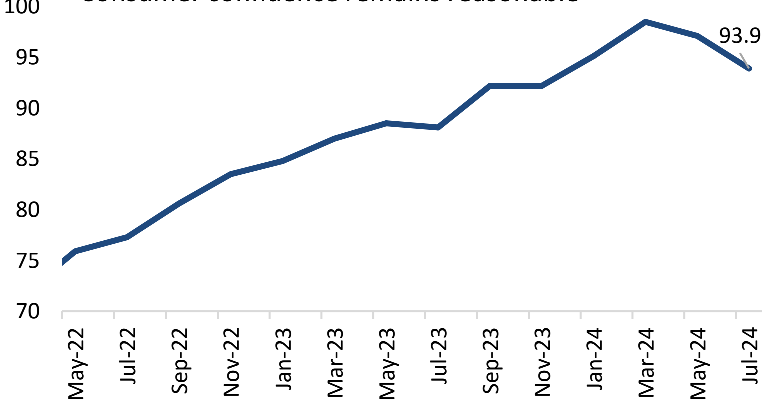
India's forex reserves continue higher on FPI inflows



Source: Bloomberg

Consumer Confidence Index

Consumer confidence remains reasonable

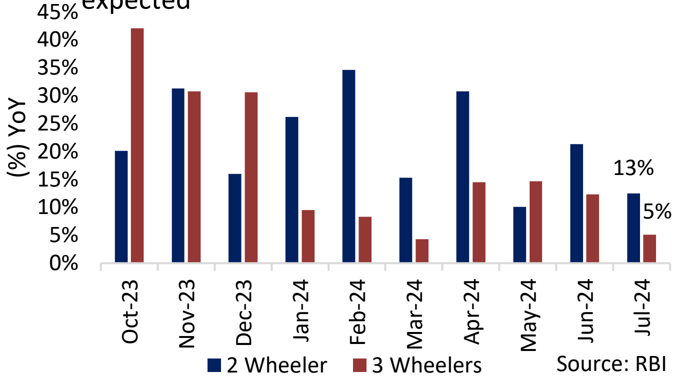


Source: Bloomberg

Rural India: Growth reviving

Two/Three Wheeler Registrations

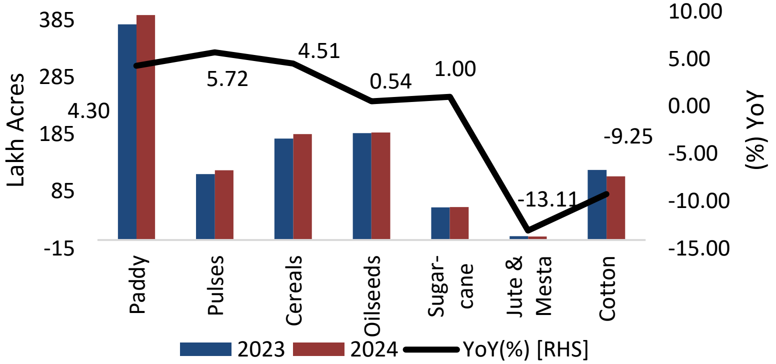
Registrations increasing slowly, further pick up expected



Source: RBI

Area Under Kharif Crops

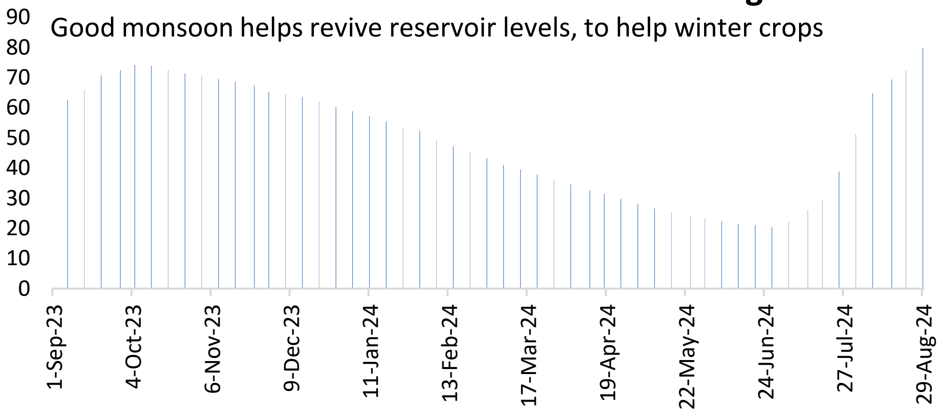
High kharif sowing, suggestive of strong output



Source: Ministry Of Agriculture

Total 133 Reservoirs - % Of Current Live Storage

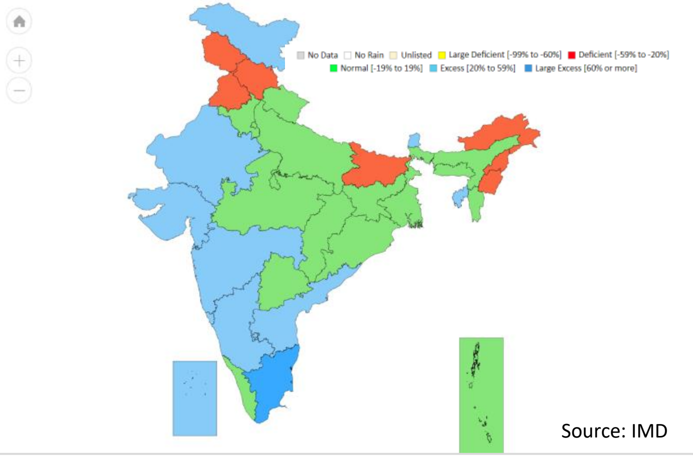
Good monsoon helps revive reservoir levels, to help winter crops



Source: Cogencies

Monsoon has been strong and projections continue to imply above normal activity

Cumulative rainfall as of yet has been above normal.



Source: IMD

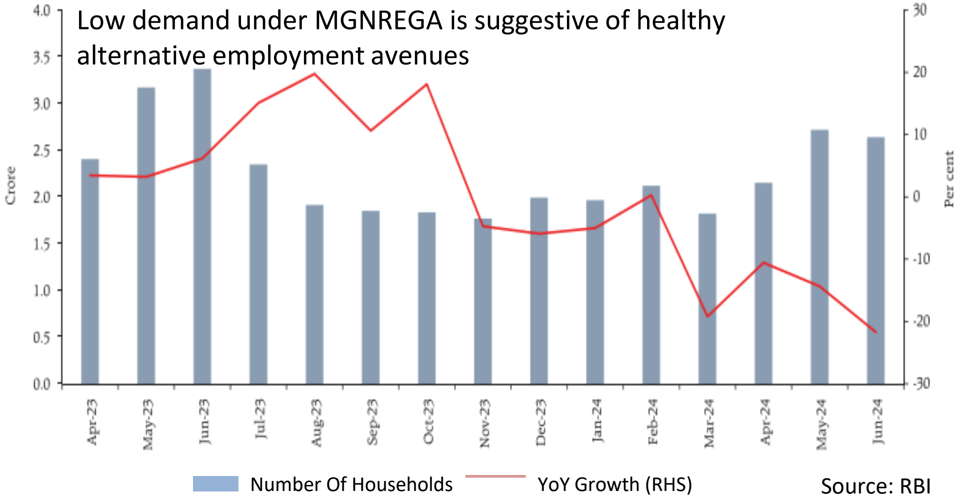
Probabilistic rainfall forecast for monsoon season (June - September), 2024

Source: IMD

Category	Rainfall Range (% of LPA)	Forecast Probability (%)	Climatological Probability (%)
Deficient	< 90	2	16
Below Normal	> 90 - 95	8	17
Normal	96 -104	31	33
Above Normal	> 105 -110	32	16
Excess	> 110	29	17

Household Demand For Work Under MGNREGA

Low demand under MGNREGA is suggestive of healthy alternative employment avenues

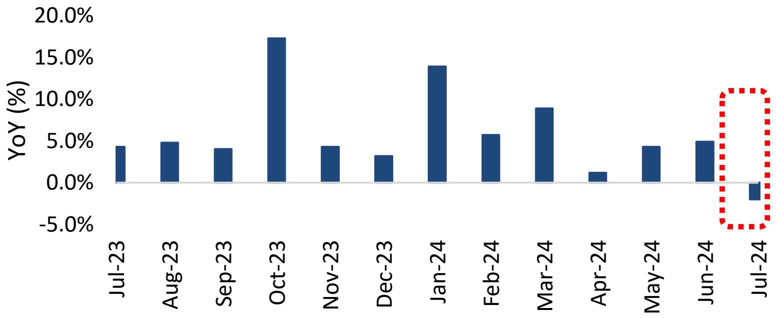


Source: RBI

Urban India showing early signs of deceleration…

India Passenger Vehicle Sales Dip

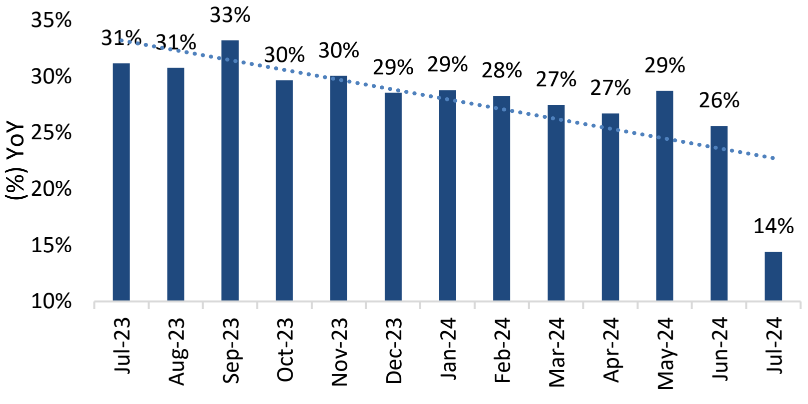
Dealers having high inventory and offering discounts to promote the sales



Source: RBI

Banking Sector Personal Loan Growth

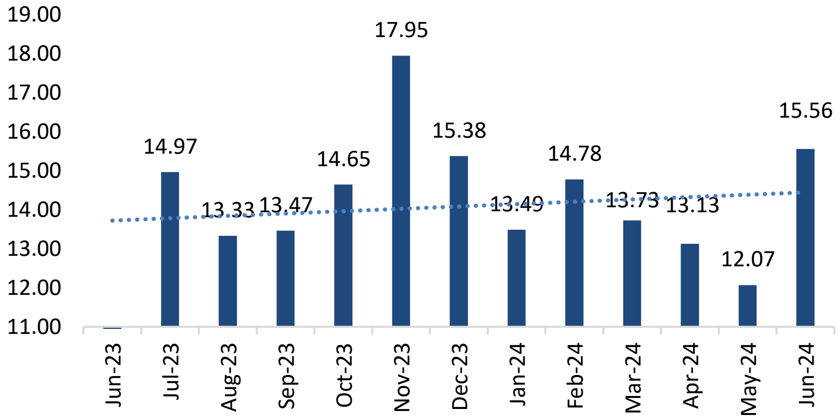
Personal loans slow down



Source: Bloomberg

Net Service Exports Recover (USD Bn)

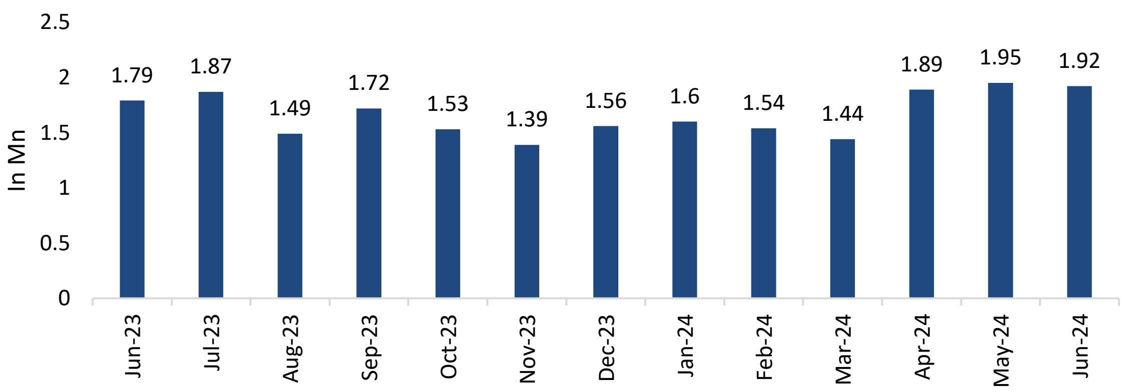
Improved service exports add to urban incomes



Source: Bloomberg

Formal Job Creation (EPFO Payroll net subscriber growth)

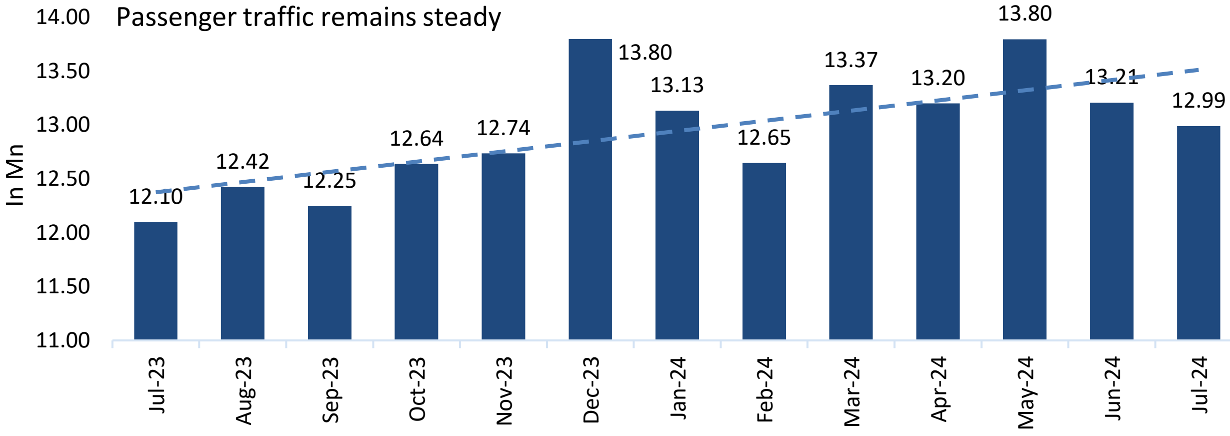
Job creation remains healthy



Source: EPFO, PIB

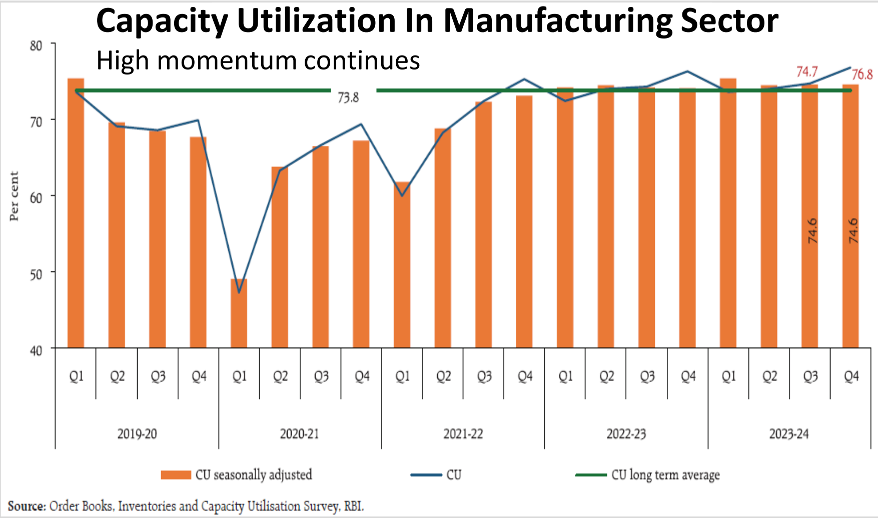
Domestic Air Passenger Traffic

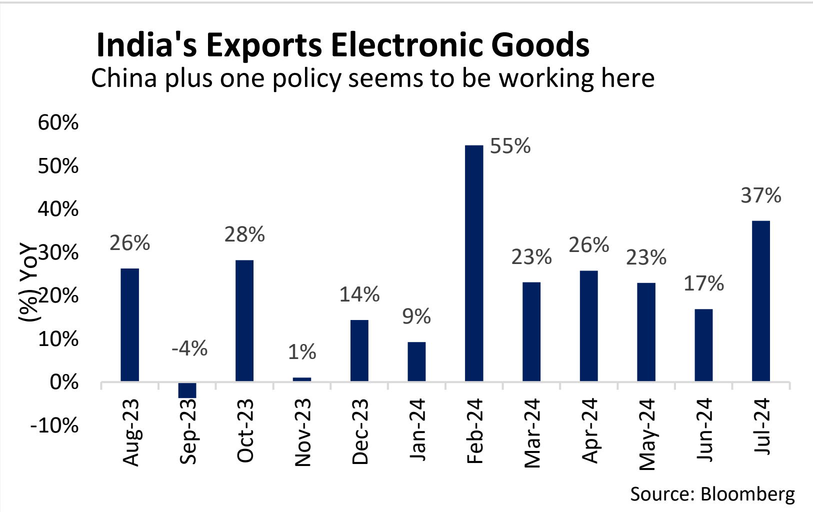
Passenger traffic remains steady

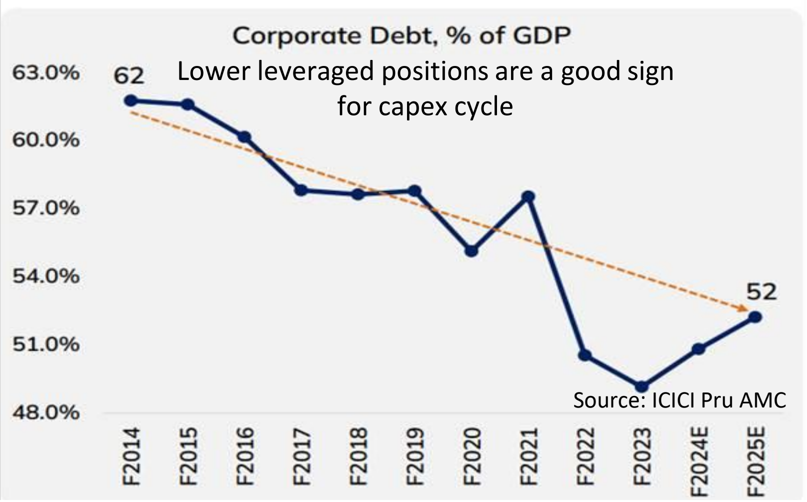


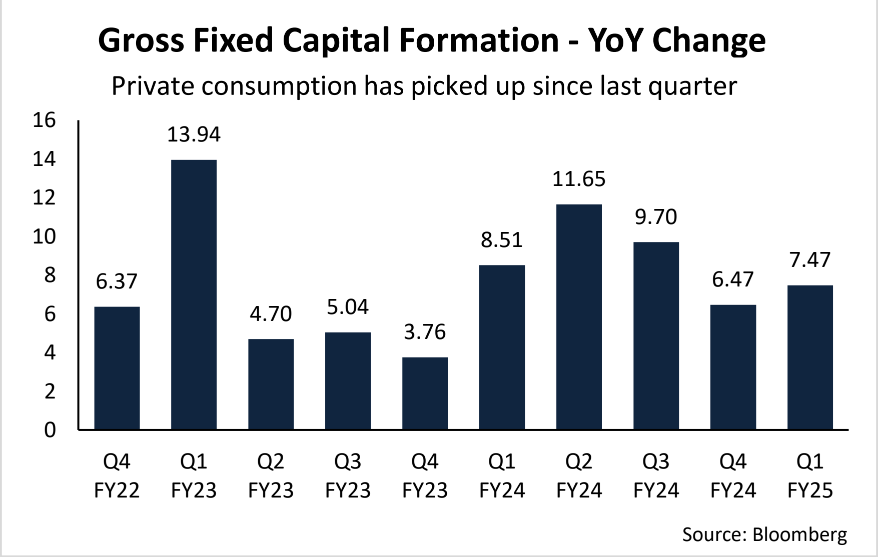
Source: DGCA

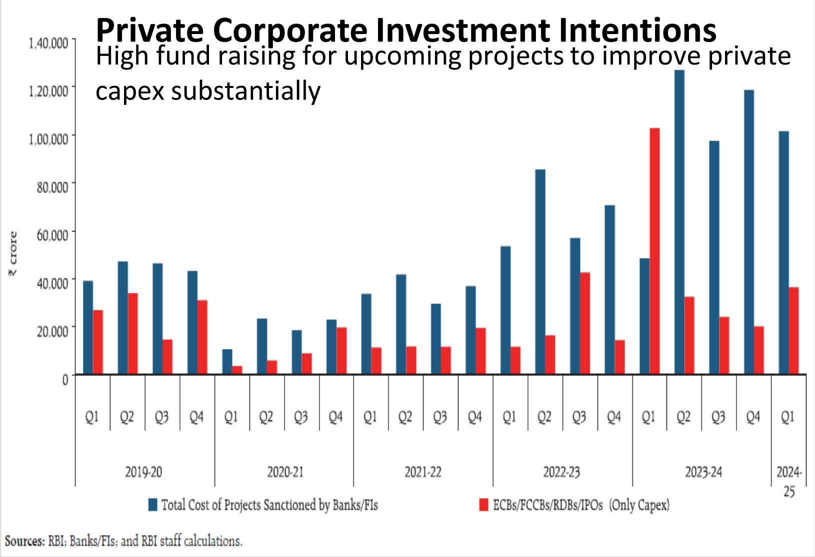
Capex: Rising Profitability, Improved capacity utilisation and strong government policy support seems to be pushing private capex demand

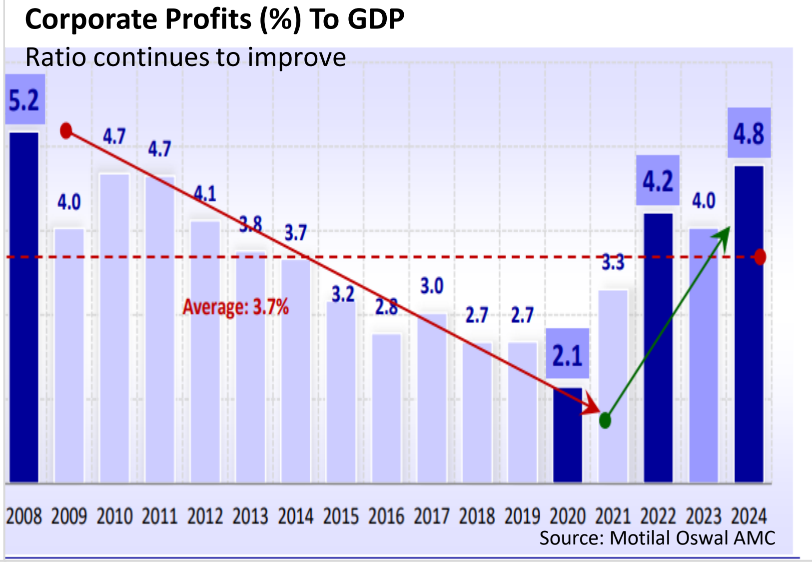












Quarterly Results: Heatwaves, Elections and weakening margins impact Q1FY25 results

Sector	Net Sales - YoY Growth (%)			EBITDA - YoY Growth (%)			PAT - YoY Growth (%)		
	Q1 FY25	Q4 FY24	Q1 FY24	Q1 FY25	Q4 FY24	Q1 FY24	Q1 FY25	Q4 FY24	Q1 FY24
Auto & Auto Anc	10.60	14.28	27.59	31.55	41.22	234.49	30.62	86.77	586.63
BFSI	21.32	24.12	26.41	16.52	-5.61	74.47	19.96	34.09	70.71
Capital Goods	18.49	18.00	24.04	23.60	28.31	27.30	29.75	27.43	39.63
Cement & Products	-0.44	9.54	14.53	-19.23	34.50	18.30	-19.14	48.11	24.89
Chem & Fert	-2.27	-14.03	-6.76	-24.33	-41.29	-26.07	-52.26	-83.67	-35.76
Ecomm	22.17	28.57	40.48	-45.06	61.86	61.26	-6.62	85.39	80.99
FMCG & Retail	8.51	7.17	5.49	8.25	7.90	10.64	7.92	-5.76	12.29
Healthcare	10.72	12.15	16.39	19.69	27.85	36.92	37.34	50.54	14.78
Infrastructure	11.34	18.97	23.52	35.16	25.82	125.39	46.61	76.88	80.00
IT	3.91	2.14	10.35	8.92	1.88	9.69	9.66	8.64	9.79
Media & Ent	3.30	6.05	8.84	1.57	12.62	4.01	15.01	38.90	-4.51
Metal & Mine	1.16	-3.43	-4.32	19.22	0.09	-33.75	7.84	-6.08	-30.19
Oil & Gas	3.64	3.11	-8.58	-40.78	-5.81	195.85	-41.93	-1.50	219.40
Others	12.15	2.25	-40.15	40.36	-8.38	24.94	78.90	-31.69	39.95
Power	13.47	9.95	3.19	13.57	6.99	33.03	1.23	16.98	17.76
Realty	8.45	5.14	9.09	41.18	41.60	-10.98	67.40	23.64	9.37
Telecom	3.57	5.61	10.05	3.55	4.30	42.39	104.45	-397.26	-19.20
Textiles	9.00	12.75	10.78	3.14	33.31	5.72	-11.98	15.54	-6.61
Transport	15.92	21.97	23.44	-1.89	52.91	1,209.60	-3.58	83.62	476.12
Grand Total	9.50	9.70	5.75	-1.90	5.55	48.74	4.21	20.26	58.91
Ex-Financials	5.96	5.31	0.82	-4.61	7.29	45.58	-4.56	12.58	53.02

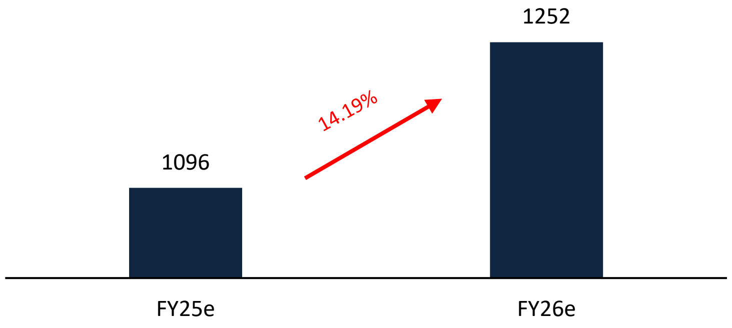
Data as on August 20, 2024 and pertains to 198 companies within the Nifty 200 universe

Source: Capitaline, HDFC Bank Research

- The Q1 FY25 earnings have ended on a weak note, where the weakness in margins seem to be impacting the overall profitability and would be a concern for the market, going forward.
- Sectors which have seen weak performance are Cement, Metals, Oil & Gas and Chemicals and Fertilizer
- Sectors which have seen steady earnings are BFSI, Capital Goods, Healthcare, Infrastructure, Real Estate, Telecom.

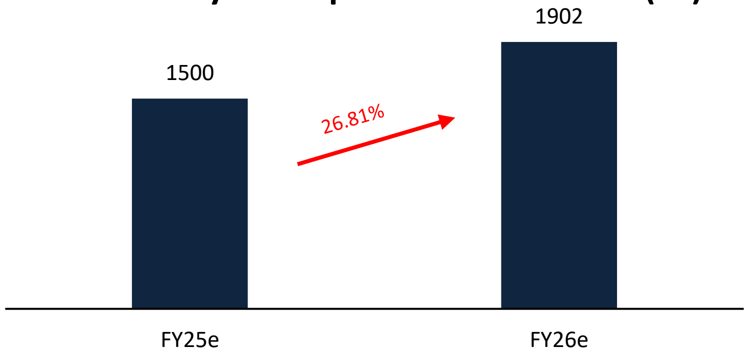
India valuations - Valuations remain high as market remain buoyant, despite weak quarterly results… MF raising cash levels

Nifty 50 - Forward EPS (Rs)



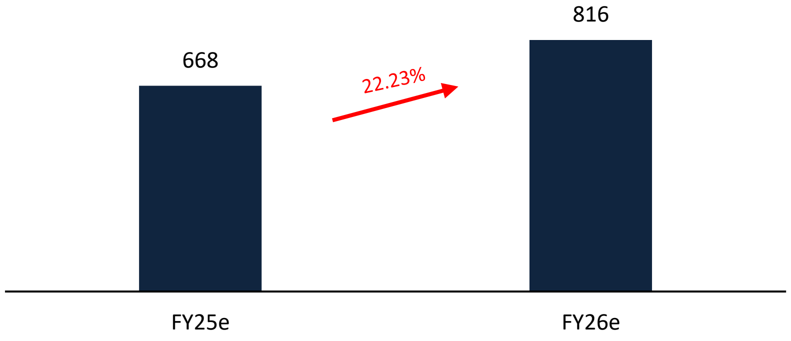
Source: Bloomberg

Nifty Midcap 100 - Forward EPS (Rs)



Source: Bloomberg

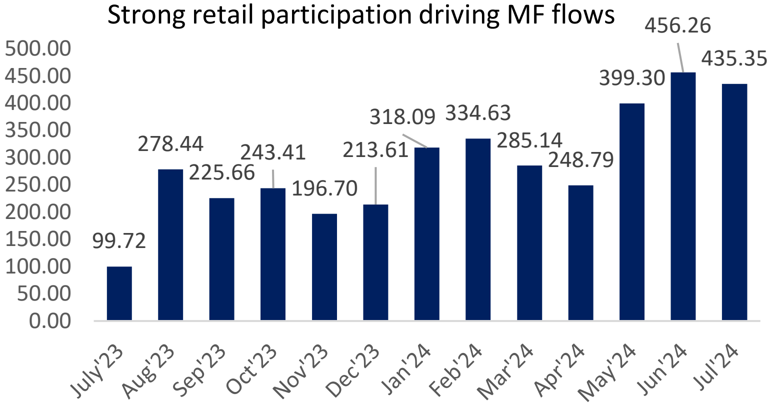
Nifty Smallcap 250 - Forward EPS (Rs)



Source: Bloomberg

MF Net Flow* (in Rs Bn)

Strong retail participation driving MF flows



Source: ACE MF

Valuations getting expensive

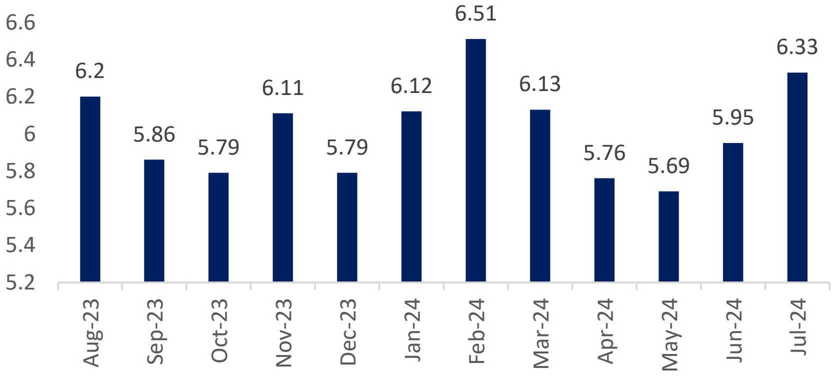
12M expected Fwd P/E (x) Comparison By Market Cap

Index	FY25 (Est)	FY26 (Est)
Nifty 50	23.07	20.20
Nifty Midcap 100	39.42	31.09
Nifty Smallcap 250	27.20	22.26

Source: Bloomberg

Mutual Funds Aggregate Cash Value (%)

Cash in Equity + Hybrid (ex arbitrage) rising

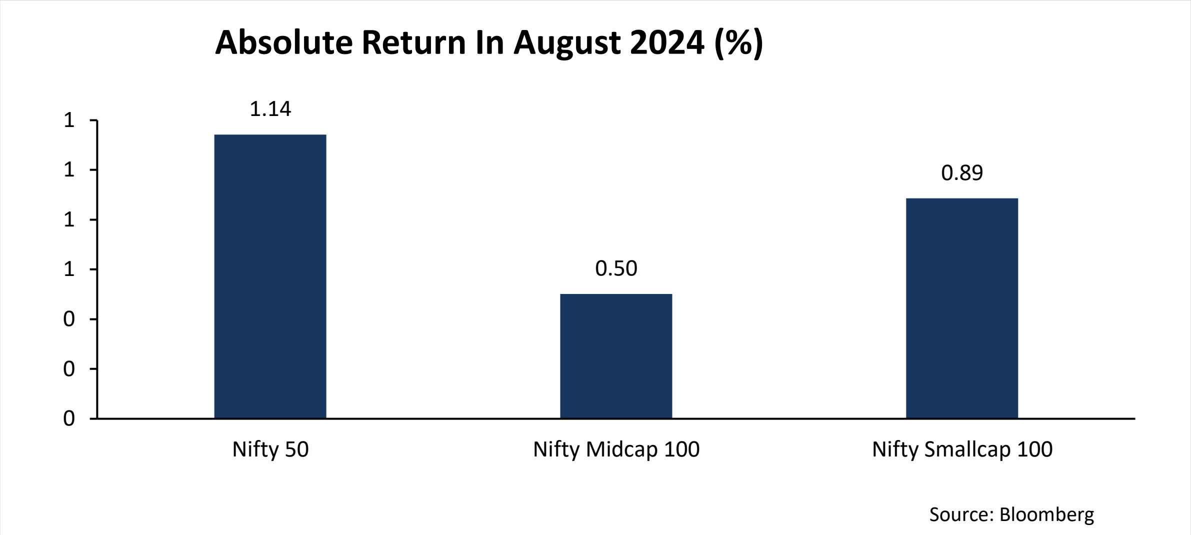


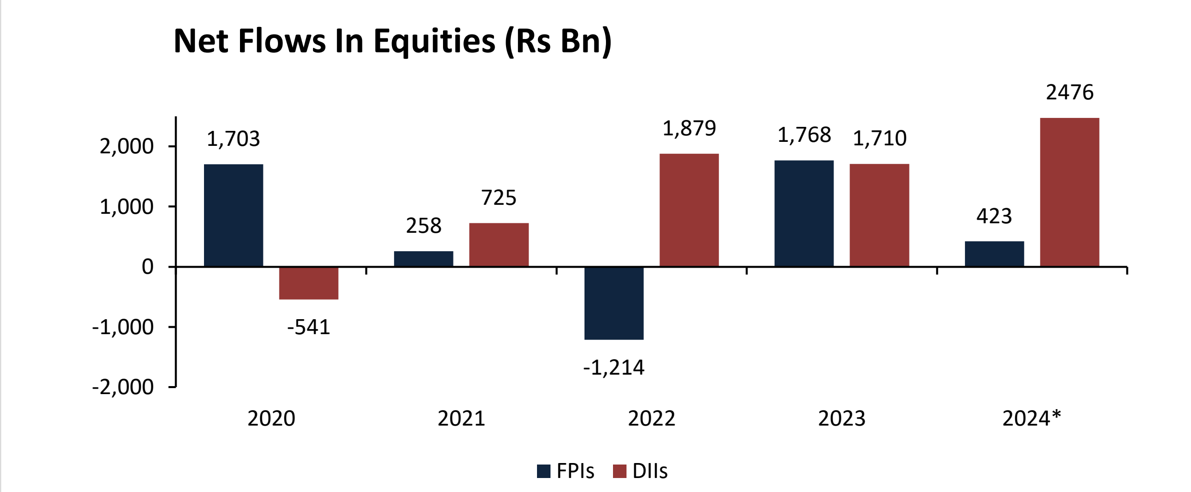
Source: ACE MF

Cash Definition = (Equity Funds + Hybrid Funds) – Arbitrage Funds
* Indicates Equity + Hybrid (ex arbitrage) flows

Market Roundup – August 2024

- Indian equities ended the month on a positive note. Large cap-oriented BSE Sensex and Nifty 50 ended higher to the tune of 0.80% & 1.1% (MoM) respectively.
- The BSE Midcap indices ended higher by 0.90% (MoM), BSE Small cap ended higher by 1.2% (MoM).
- In terms of BSE sectoral indices, Healthcare was the top performer. In contrast, Realty, Capital Goods and Power underperformed the most.
- Indian equities ended the month on a positive note after the US Federal Reserve Chair Jerome Powell signalled an imminent rate cut at the Jackson Hole Symposium. The prospects of solid domestic economic growth amid a healthy monsoon boosted the sentiments further.





*For 2024, FPI and DII data is up to 30th August, 2024

Source: SEBI, CDSL

Key concerns for Indian equities

- Low growth in consumer demand
- Expectation of weakening margin profile for corporates
- Adverse outcome of upcoming state government elections in 4 states
- Delay in rate cuts by Global Central Banks
- Upward pressure on food inflation (El Nino, export restrictions by some nations)
- Rising tensions in Middle East
- Movement of global liquidity
- The impact of Dollar Index and US Bond Yields on FPI flows in emerging markets

Annexure…

Sectoral outlook by fund managers – Part 1

Sector	Particulars
BFSI	**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 NIMs possible. • Credit costs (provisioning) have started to show initial signs of weakness. • Most fund managers are continuing to add weight in the Pvt sector banks and Insurance Companies
IT	**View –Neutral to Positive** • Large global bellwethers have shown improved order booking. • Order book growth of Indian companies holding up, margins need to sustain, execution cycle seem to be pushed back by customers. • Results have been better than expectations. • Funds are cutting underweights.
Pharma	**View – Neutral** • Reasonable valuations, domestic demand holding up well. • US is seeing abatement of price erosion in the generic space, which should be positive for Indian pharma stocks. • Decline in the raw material prices to drive margins and earnings. Stock prices have seen strong performance and seem to be pricing many positives • Fund Managers expect the sector to now be market performers and are looking at very stock specific opportunities. • Hospitals as a segment seems stretched on valuations and is not finding further favour with the fund managers.
Auto	**View – Neutral to Negative** • The base for Passenger vehicle volume seems to be loaded against its favour, and volume growth going forward seems to be a concern. Fund managers are looking to reduce allocation. • 2-Wheeler stocks have seen strong outperformance and the volume growth continues to remain steady there. • 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 starting to see stability, incremental allocation from the funds may happen. • Auto ancillaries may do well due to China+1, Europe+1, PLI, export opportunities and EV initiatives. Valuations here have seen sharp runup, incremental upside could be very stock specific, fund managers cutting exposures.

Sectoral outlook by fund managers – Part 2

Sector	Particulars
Construction & real estate	**View – Neutral to Positive** • Favourable demand scenario for housing in terms of volume growth. • Government's focus on infrastructure and investment cycle. • Real estate stocks have found space in the Fund Portfolios, as growth in the sector quite strong. However, some managers are also cutting exposure as they believe that valuations look quite rich. **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 – consumer services -Positive, consumer durables and FMCG- positive** • Staples – improving volume growth, Valuations consolidated. Few AMCs are going overweight while rest are cutting underweights • Hotels/Travel – Valuations rich, funds trimming at margin. Earnings visibility is strong. • Consumer Durables – Funds are looking to bottom fish, as they expect turnaround of demand. Results have been strong. • Retail and Quick Service Restaurant: Retail valuations high, rural plays looked at, while QSRs expected to see better performance due to low base, 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. Power value chain still finding favour**
Metals	**View – Neutral to negative** • Post recent upmove, managers seem to be wanting to sell on rise. Demand conditions globally consolidating, prices of base metals weak. If Chinese real estate market sees delay in pickup, some managers believe that stocks could underperform.

Monthly Sectoral Movement

Absolute Monthly Return By Sector (%)

Index	Aug-23	Sep-23	Oct-23	Nov-23	Dec-23	Jan-24	Feb-24	Mar-24	Apr-24	May-24	Jun-24	Jul-24	Aug-24
S&P BSE 500	**-0.81**	**2.04**	**-2.93**	**6.75**	**8.01**	**1.90**	**1.93**	**0.84**	**3.43**	**0.61**	**6.87**	**4.32**	**0.77**
Auto	-1.40	3.65	-1.25	10.08	5.43	4.18	8.12	4.96	3.92	3.84	8.05	5.05	-1.90
Bankex	-4.01	0.35	-3.44	3.47	8.12	-4.38	1.92	2.02	4.64	-0.40	6.94	-1.30	-0.94
Basic Material	1.06	1.70	-3.70	7.25	11.39	0.33	-0.42	1.06	7.86	0.73	6.63	2.06	-2.27
Capital Goods	2.66	6.20	-4.07	8.88	11.31	1.88	-1.21	6.15	3.42	11.16	3.24	4.58	-3.27
Consumer Discretionary	2.10	2.40	-1.38	9.36	5.91	2.35	4.89	1.69	5.05	0.77	8.99	4.93	0.99
Consumer Durables	4.24	3.18	-2.32	7.42	6.11	0.70	0.00	2.05	5.59	-0.51	7.12	3.57	4.37
Energy	-4.38	3.20	-2.17	9.17	11.06	12.18	6.18	-0.19	3.33	-0.78	4.42	7.34	0.88
FMCG	-2.75	0.97	-0.86	3.58	6.84	-2.81	-2.33	-0.67	1.52	-0.42	5.23	9.53	2.29
Finance	-2.64	1.08	-3.09	4.82	6.92	-2.40	0.47	1.35	4.93	-1.49	7.10	0.48	0.75
Healthcare	0.57	2.45	-4.30	10.92	3.87	7.18	5.94	-0.08	1.01	-1.46	6.37	9.19	6.56
IT	4.13	2.62	-3.13	6.77	8.38	3.74	3.38	-7.20	-4.35	-2.63	11.30	12.87	4.27
Infra	1.64	8.45	-3.38	10.40	14.88	18.15	1.23	0.48	7.03	5.62	2.83	13.17	-2.07
Metal	-1.64	7.45	-4.17	8.74	11.35	-0.85	1.15	4.95	10.83	4.68	1.03	-0.85	-0.96
Oil & Gas	-5.03	1.23	-4.17	12.51	12.02	12.57	6.86	-0.07	4.83	-1.18	2.91	10.48	1.27
Power	-0.63	5.96	-4.90	11.16	18.24	8.57	4.33	1.70	7.73	6.64	3.31	6.13	-2.49
Realty	-1.50	5.21	3.70	19.99	9.37	9.37	9.16	-1.21	7.52	4.40	8.21	-1.10	-3.59
Telecom	3.20	10.55	-5.69	7.21	6.15	6.94	1.44	1.81	8.36	3.29	10.90	4.69	2.36
Utilities	-0.64	7.20	-3.98	11.85	20.00	9.71	3.61	0.25	8.84	2.80	2.40	6.87	-3.79

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

Colour scales assigned vertically

Source: Ace MF, HDFC Bank Research

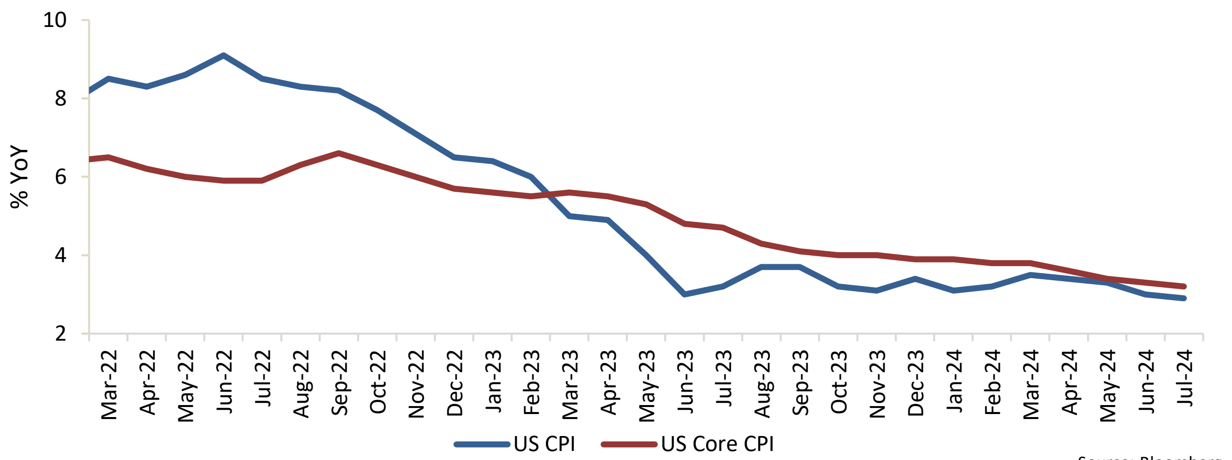
Fixed Income Market

Fixed Income Outlook

- The banking system liquidity has improved recently on the back of government spending and FPI flows led by JP Morgan Bond Index inclusion. However, the RBI remained nimble in liquidity management to remove the excess liquidity. The RBI has also been using screen-based Open Market Operations (OMO) to bring liquidity into the comfort zone. The call money rates are moving between the Repo and Standing Deposit Facility (SDF) corridor.
- The CPI-based inflation for July 2024 decelerated to 3.54% YoY due to favourable base-effect even though the inflation accelerated sequentially. On the other hand, the core inflation inched up on an annual basis in July 2024 due to rise in prices of broad-based categories as demands pick-up. While the headline inflation fell below the RBI's target of 4% YoY, it may inch back to above 4% market from Q3 FY25 onwards as the base-effect subsides. The government is also actively taking supply side measures to keep food prices in check, which would likely help to bring overall inflation down.
- India's external sector remains robust on the back of narrowed Current Account Deficit (CAD), strong Rupee currency and higher foreign exchange reserves. Going forward, while the CAD make increase as trade deficit widens due to increasing domestic demand, it would likely remain manageable.
- The RBI remains hawkish as the food prices remain elevated and inflation expectations of household have inched up. Furthermore, with the inflation forecast for the Q2 FY25 moving above 4%, the market expectations of policy pivot by the RBI in the October policy have reduced significantly.
- With the government remaining on its fiscal consolidation path and aiming to reach a fiscal deficit target of below 4.5% of GDP by FY26, the market borrowing of the government may remain lower in the upcoming years; thus, limiting the supply of government securities (G-secs). Additionally, the lower fiscal deficit as of July 2024 of FY25 to further favour demand-supply dynamics of G-secs. With the government remaining fiscally prudent, the global rating agencies may look to upgrade India's sovereign rating, which remains a positive for the bond market.
- The Federal Reserve's (Fed) Chairman at the Jackson Hole symposium has guided for a policy rate cut in the near future as the downside risks to employment have increased while the upside risks to inflation have diminished. While the Fed rate cut is likely to commence in September policy, the quantum of rate cut would be data-dependent. The Bank of England (BoE) cut the policy rate in August 2024, but the European Central Bank (ECB) remains on wait and watch mode after cutting the rates in June 2024 as the last leg of inflation remains sticky. Both the central banks highlighted that future decision will be data-dependent due to stalled disinflationary process.
- The Bank of Japan (BoJ) may hold off from further raising the rates as the appreciation of Yen would be disinflationary. Thus, with divergence in growth and inflation dynamics across economies, the central banks' monetary policy actions may depend on each country's macroeconomic factors.
- Domestically, the flows regarding the index inclusion and the lower supply of the government papers would continue to act as a support for bond prices, ensuring that both demand and supply variables remain favourable for the bond market. In the medium term, the market is also likely to take cues from the US bond market, movement of the USD/INR pair and the liquidity measures of the RBI. As the deceleration in the inflationary trend starts, the RBI may become accommodative on the system liquidity. Hence, the shorter end of the yield curve may react more than the longer end.
- With expected policy rate cuts in the US, favourable demand-supply dynamics in Indian G-Secs, and strong FPI flows into the bond market, tactical opportunities can emerge at the longer end. Also, accrual opportunities at the 2-4-years segment of the corporate bond yield curve remains attractive for incremental investment, from risk-reward perspective. Hence, investors can look at Corporate Bond Funds and Short duration funds for a horizon of 15 months and above.
- For a horizon of 24 months and above, investors can look at Dynamic Bond Funds. 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.

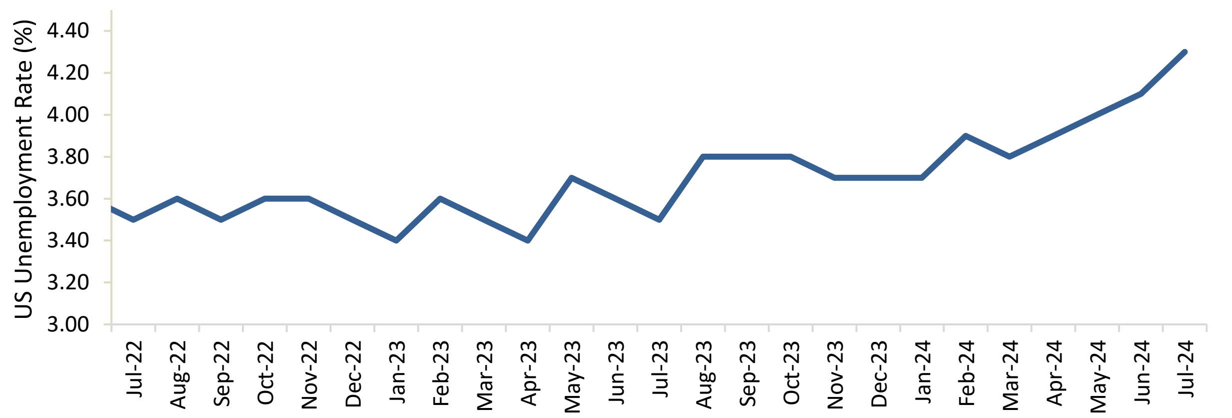
Dovish statement from the Fed sets the stage for September rate cut in the US

With falling inflation, the upside risks to inflation remain diminished



Source: Bloomberg

Rising unemployment highlights increasing downside risks to employment



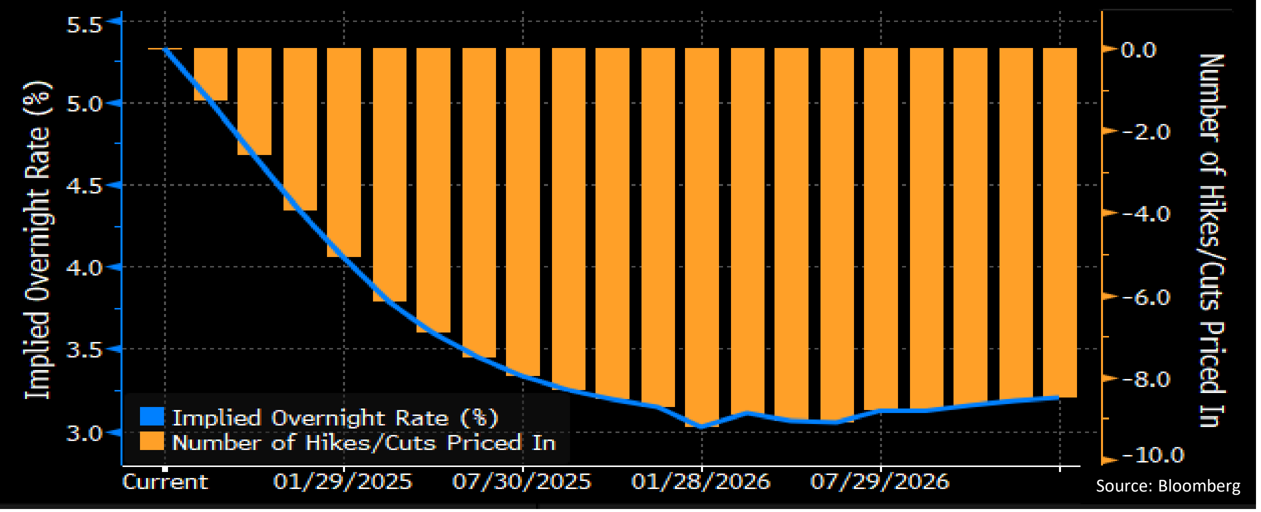
Source: Bloomberg

"Overall, the economy continues to grow at a solid pace. But the inflation and labor market data show an evolving situation. The upside risks to inflation have diminished. And the downside risks to employment have increased. As we highlighted in our last FOMC statement, we are attentive to the risks to both sides of our dual mandate.

The time has come for policy to adjust. The direction of travel is clear, and the timing and pace of rate cuts will depend on incoming data, the evolving outlook, and the balance of risks."

– Fed Chair Jerome Powell at Jackson Hole Symposium

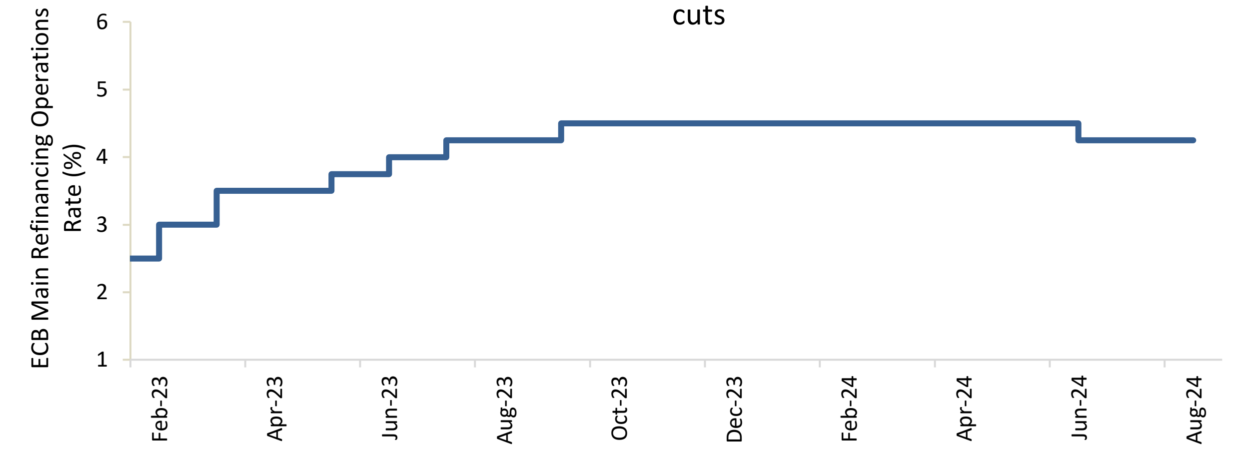
After Jackson Hole symposium, Fed 's rate cut in Sep'24 seems likely



Source: Bloomberg

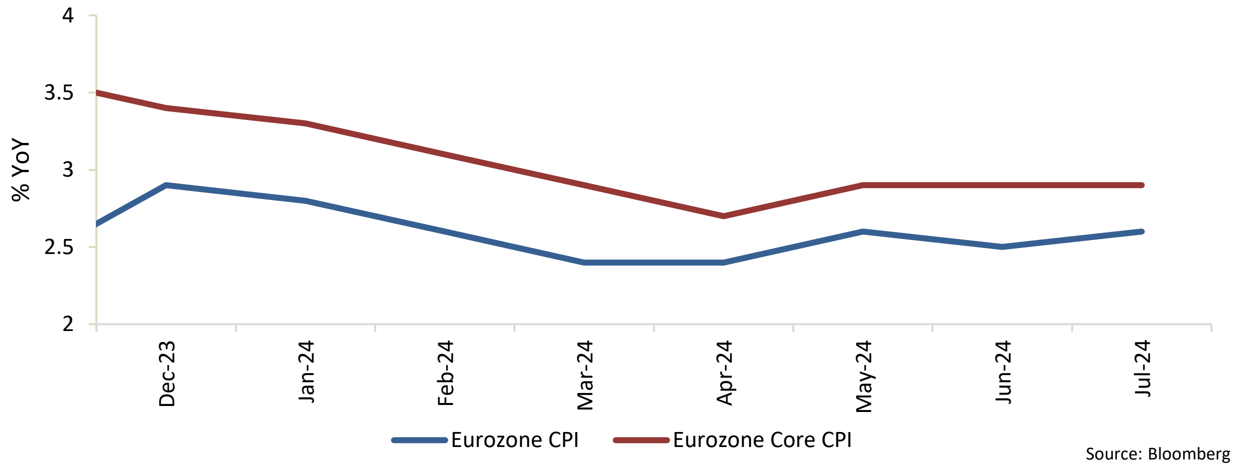
ECB still waiting for confirming data for further cuts

ECB seems to be on a wait and watch mode before moving for further rate cuts



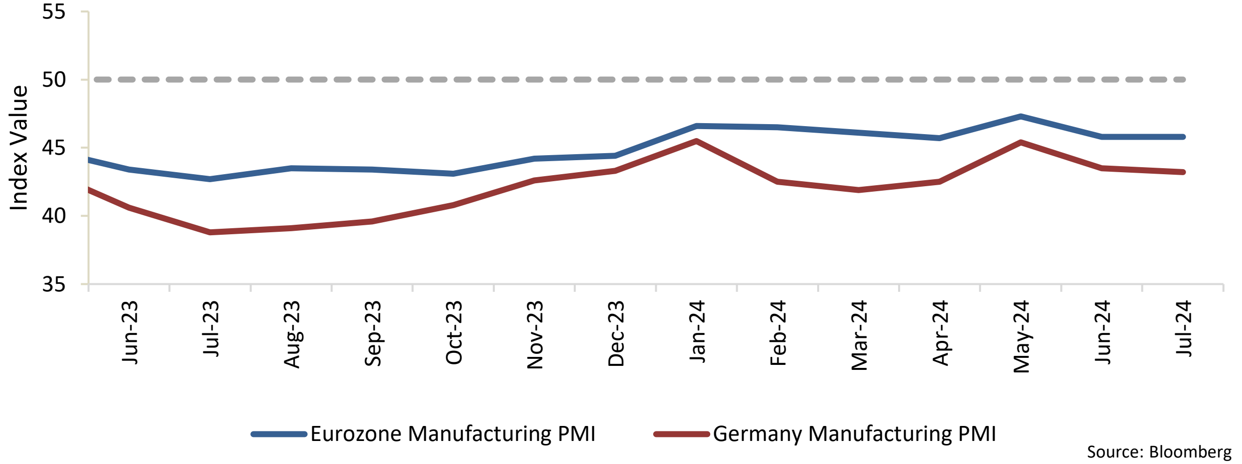
Source: Bloomberg

Last leg of inflation remains sticky in Europe



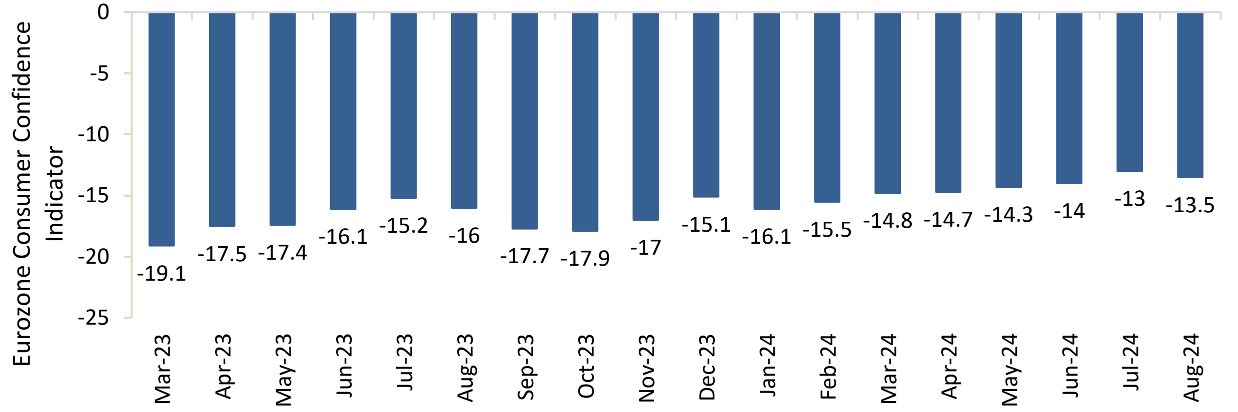
Source: Bloomberg

Eurozone economy continues to struggle



Source: Bloomberg

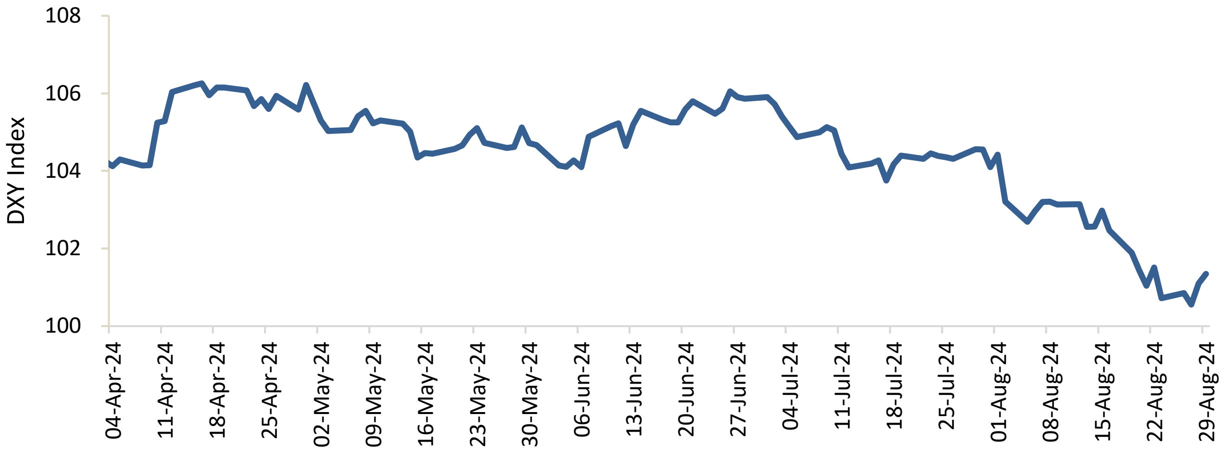
Weak consumer confidence indicates weak demand conditions, which may help in further dip in core inflation



Source: Bloomberg

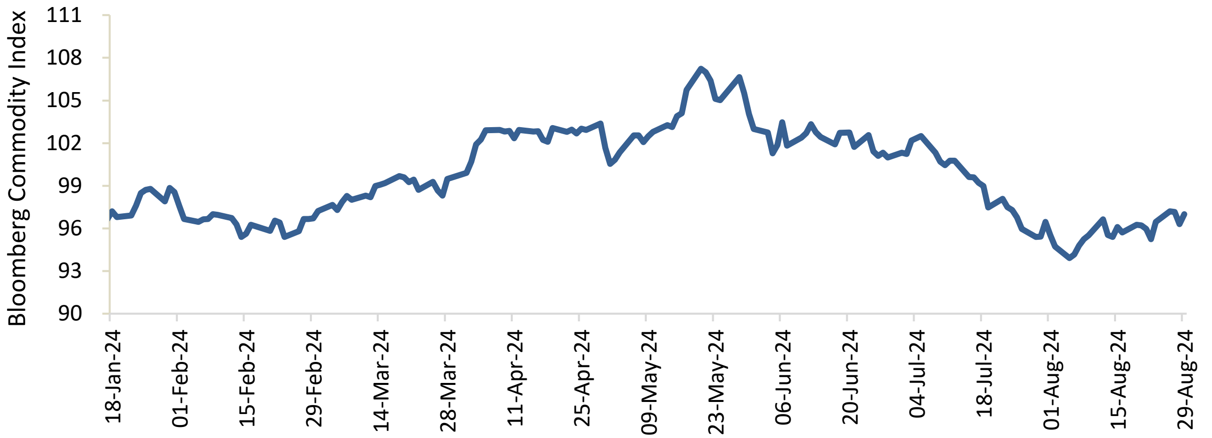
Declining dollar index and rising geopolitical tensions led to uptick in commodity prices

US Dollar weakens on the hopes of Fed rate cuts



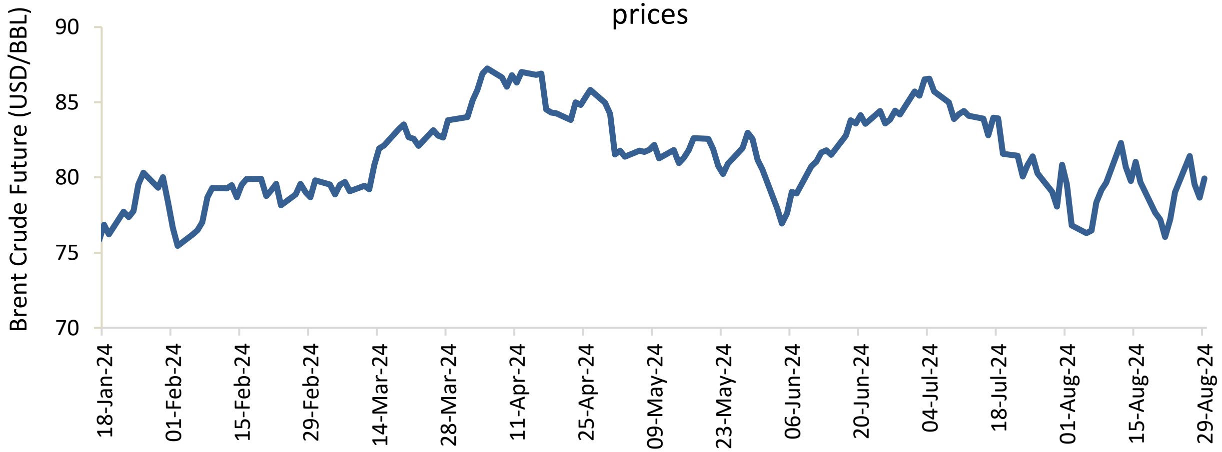
Source: Bloomberg

Weak global growth outlook keeping commodity prices under check



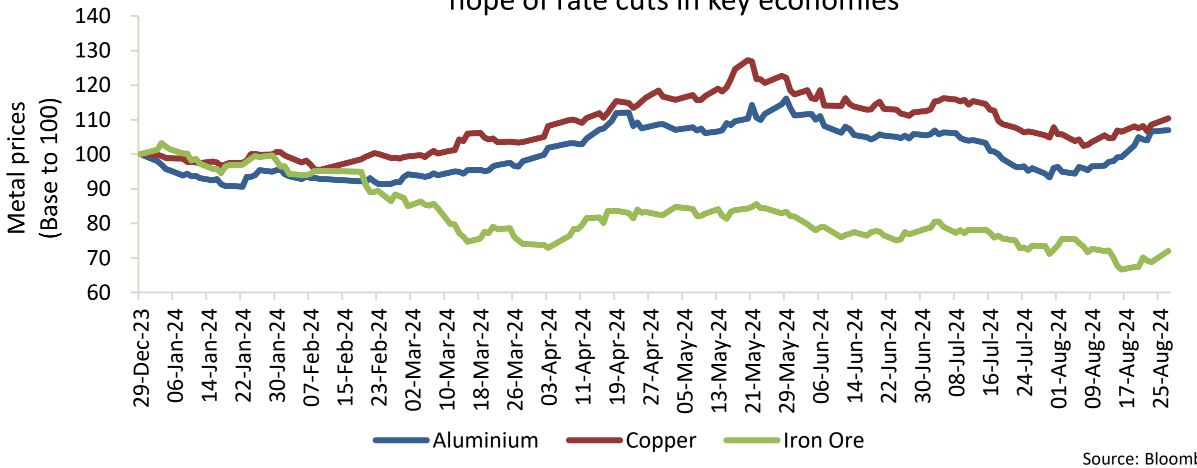
Source: Bloomberg

Recent geopolitical incidents in Middle East may lead to flare up in crude oil prices



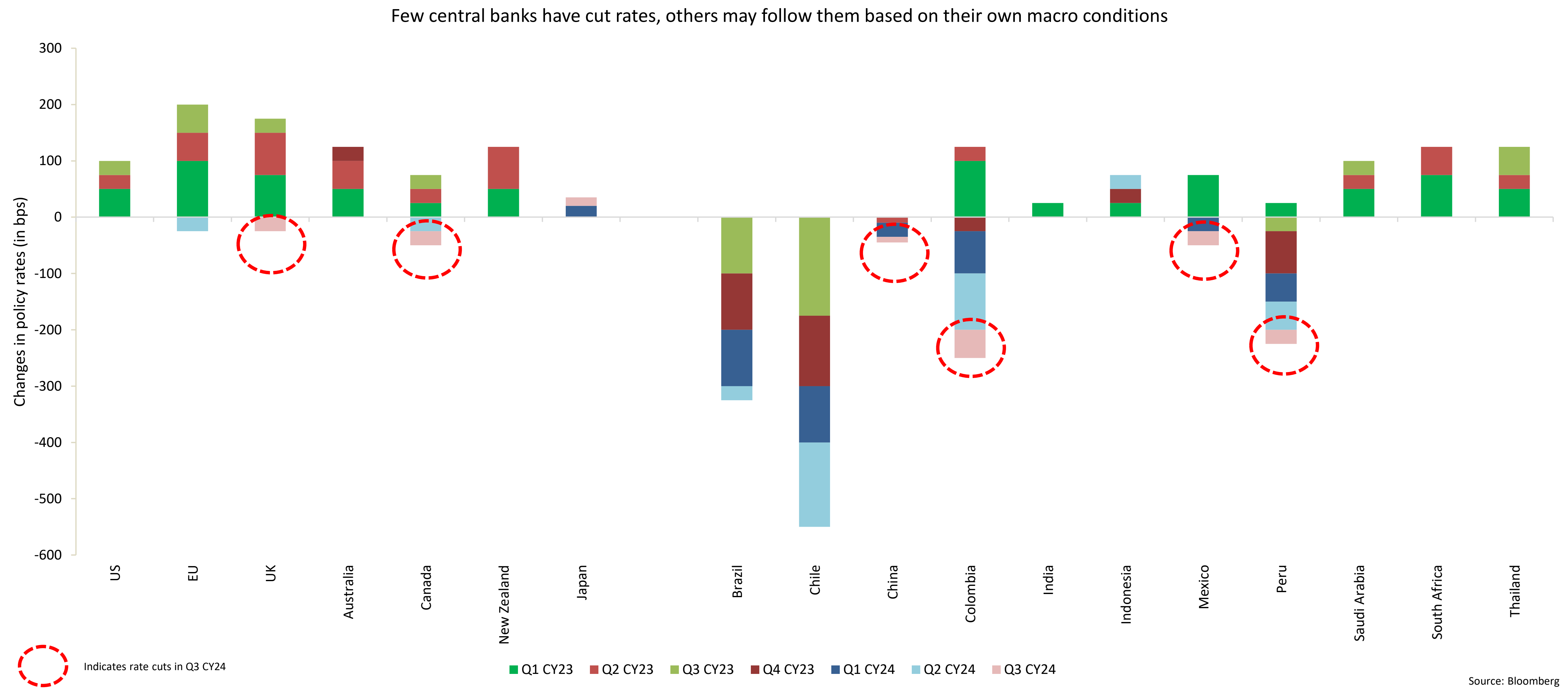
Source: Bloomberg

Metal prices have bounced back from recent lows due to weak dollar and hope of rate cuts in key economies



Source: Bloomberg

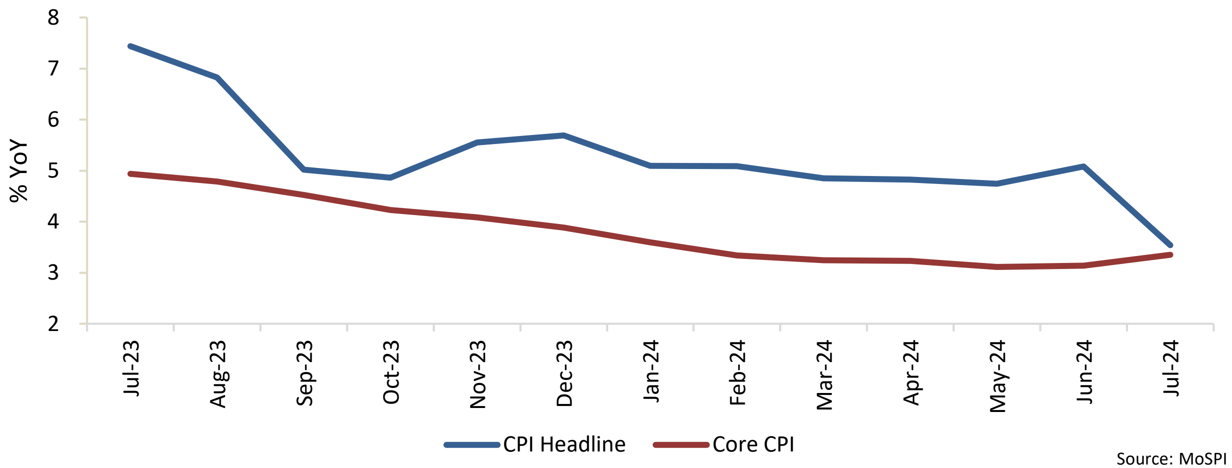
Majority of the global central banks are at the cusp of rate cuts



Source: Bloomberg

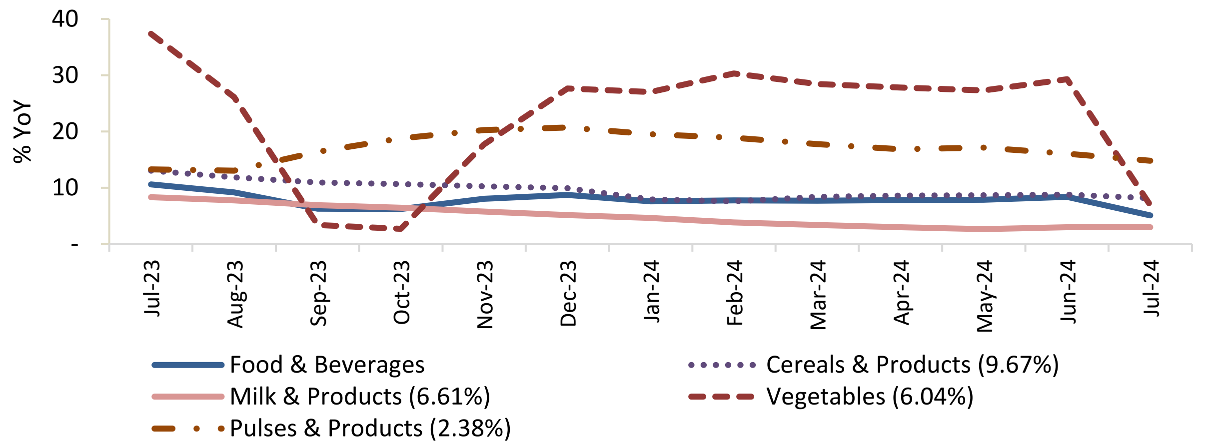
Favourable base brought domestic inflation down, continuity of the trend important

Inflation fell below the RBI's target due to favourable base effect



Source: MoSPI

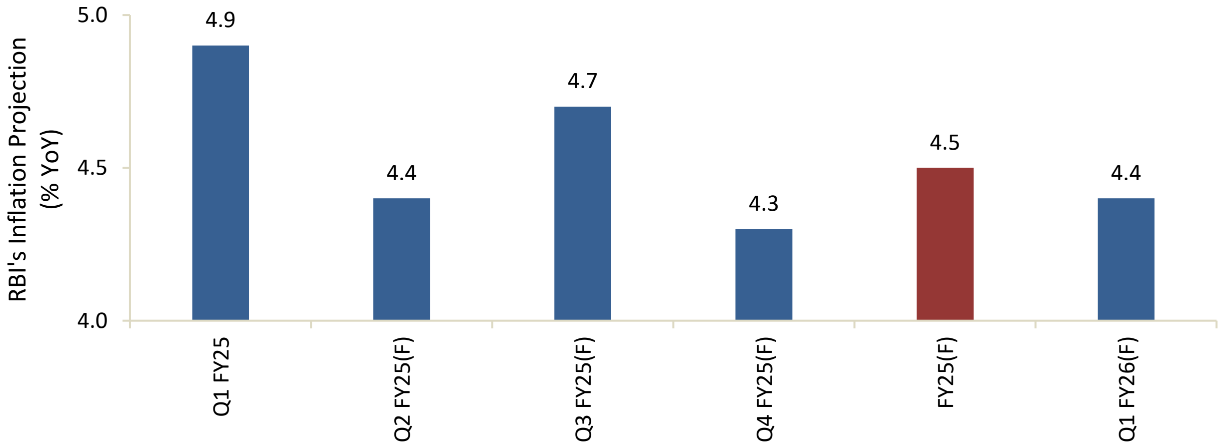
Higer base pulled the vegetable inflation down



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

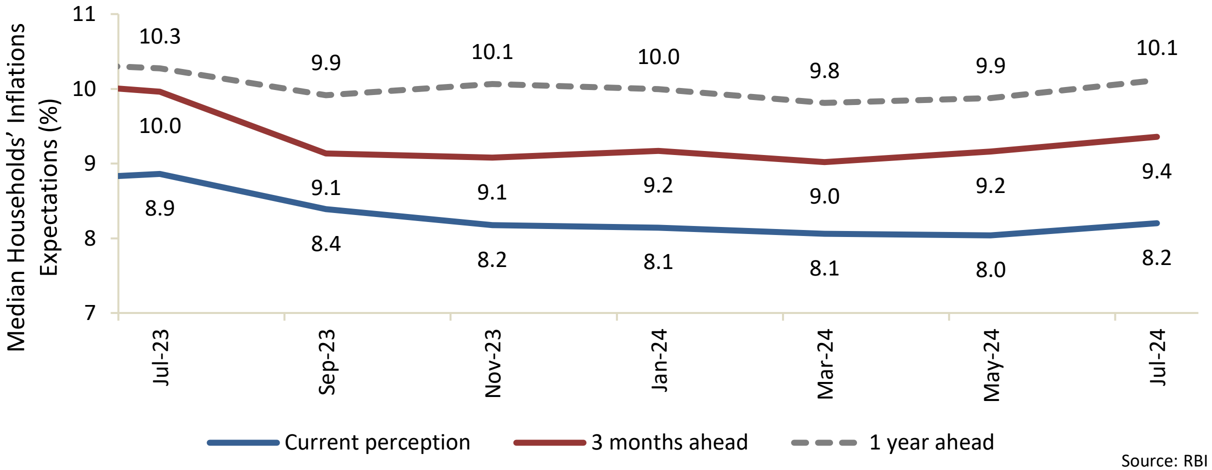
Source: MoSPI

While CPI decelerated, the RBI expects inflation to rise as base effects fades



Source: RBI

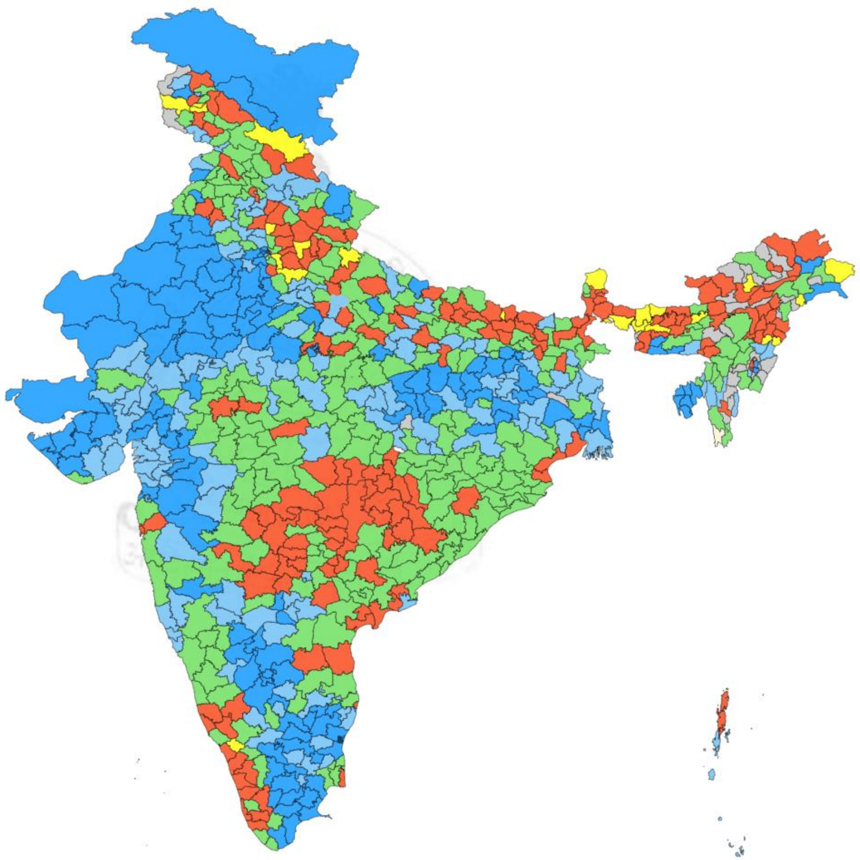
Inflation expectations of households have inched-up



Source: RBI

Favourable monsoon to further weigh down on food inflation

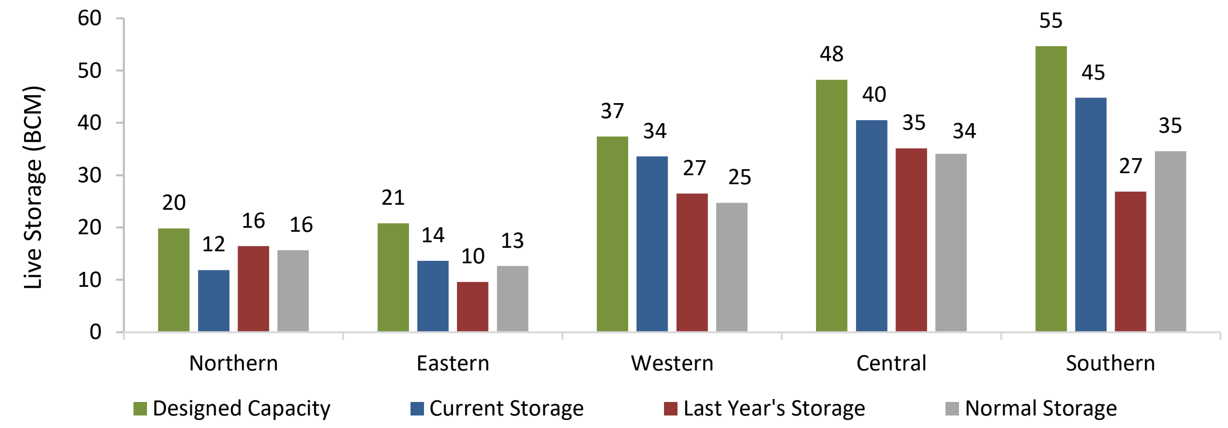
While rainfall covered its deficit in most regions, the likely development of La Nina needs to be monitored



Note: Cumulative Rainfall from 01 June 2024 to 30 Aug 2024

Source: IMD

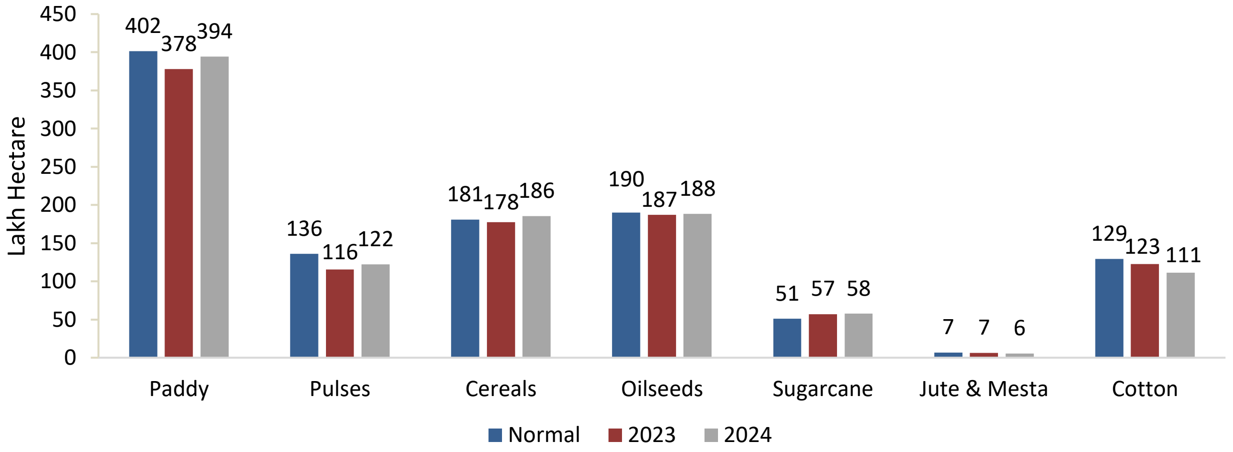
Majority of the reservoirs have surpassed the normal storage levels



Note: Data as on 29-August-2024

Source: Central Water Commission

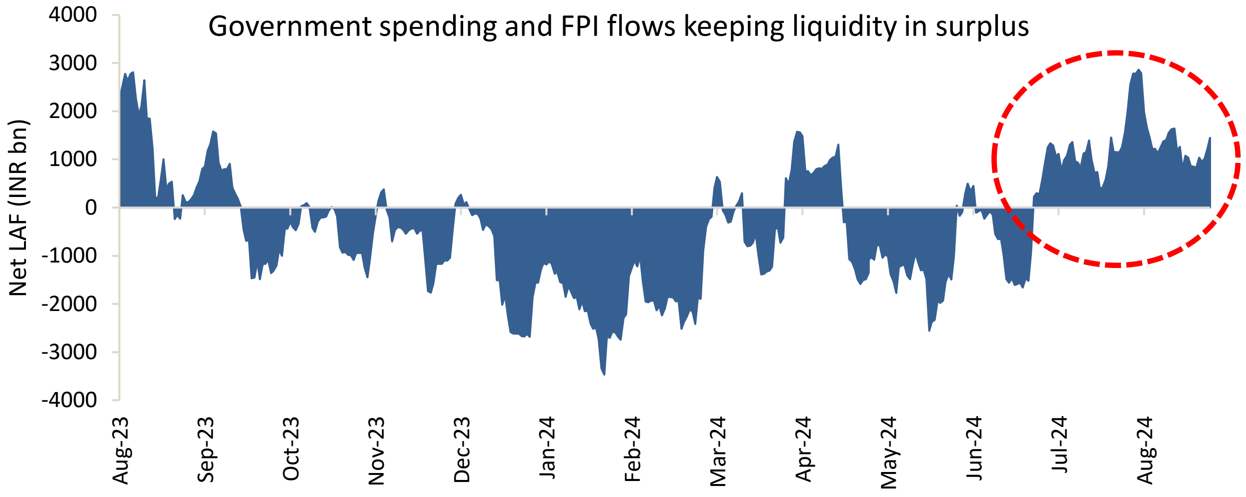
With good monsoon, kharif sowing has gathered pace



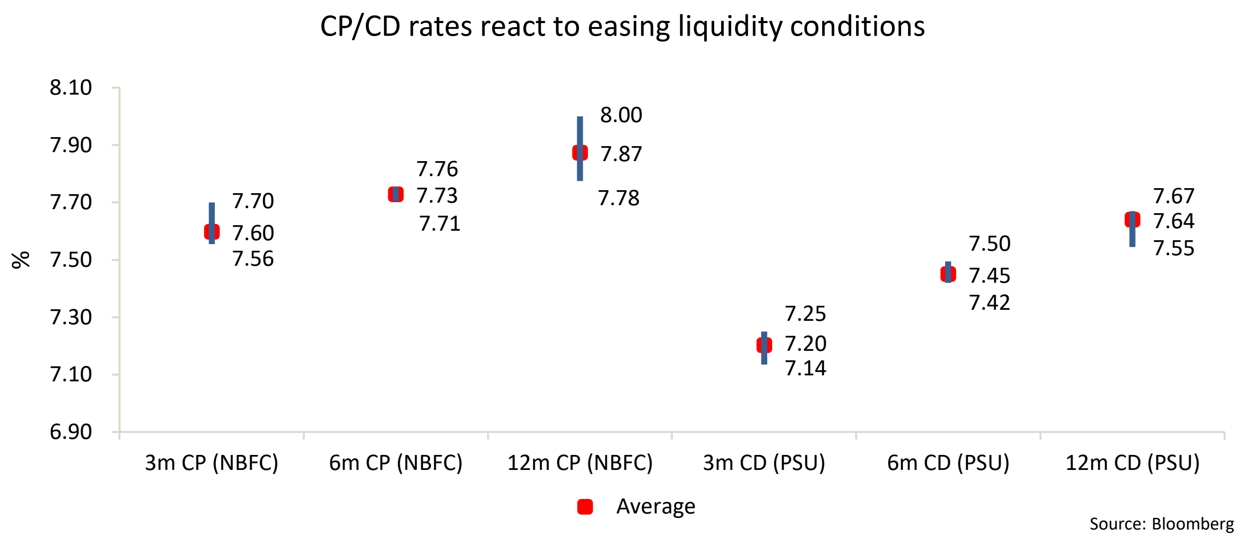
Note: Progress of Kharif Sowing (as on 23 August 2024)

Source: Ministry of Agriculture and Farmers' Welfare

Post elections, liquidity has risen due to government spending…. the RBI remained nimble in liquidity management



Source: Bloomberg



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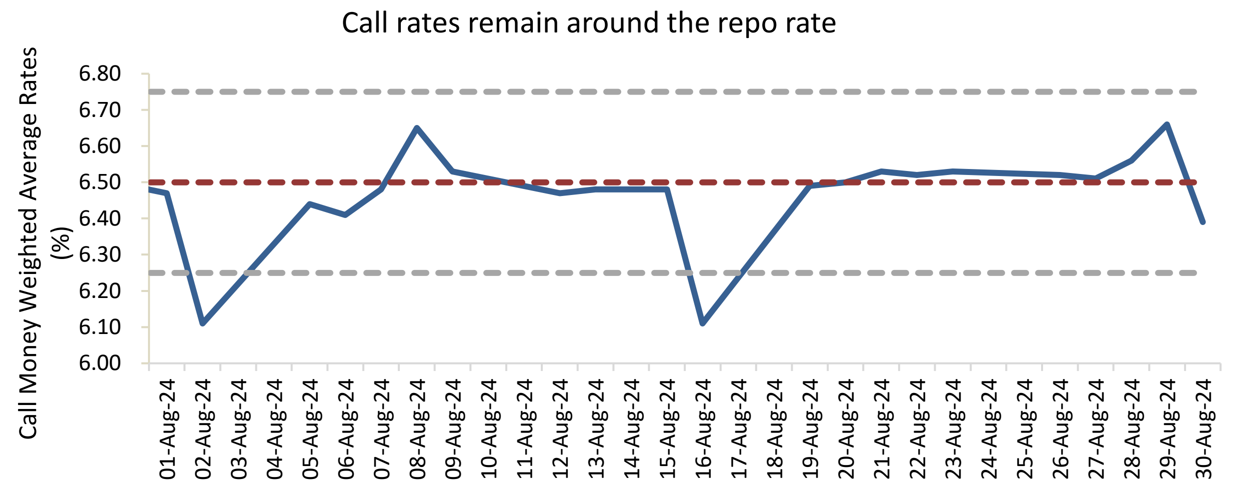
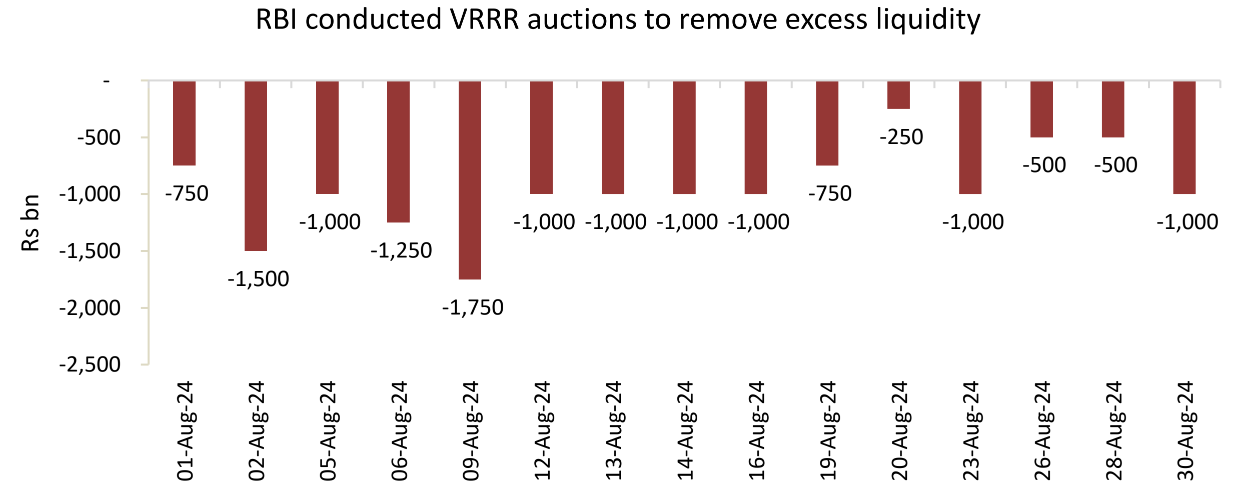


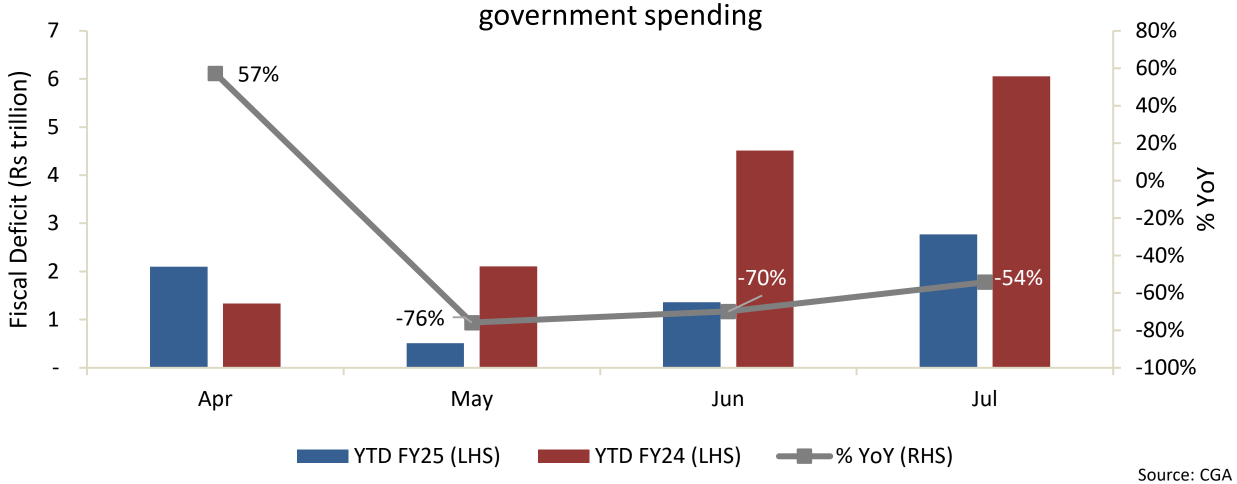
Source: Bloomberg



Source: RBI

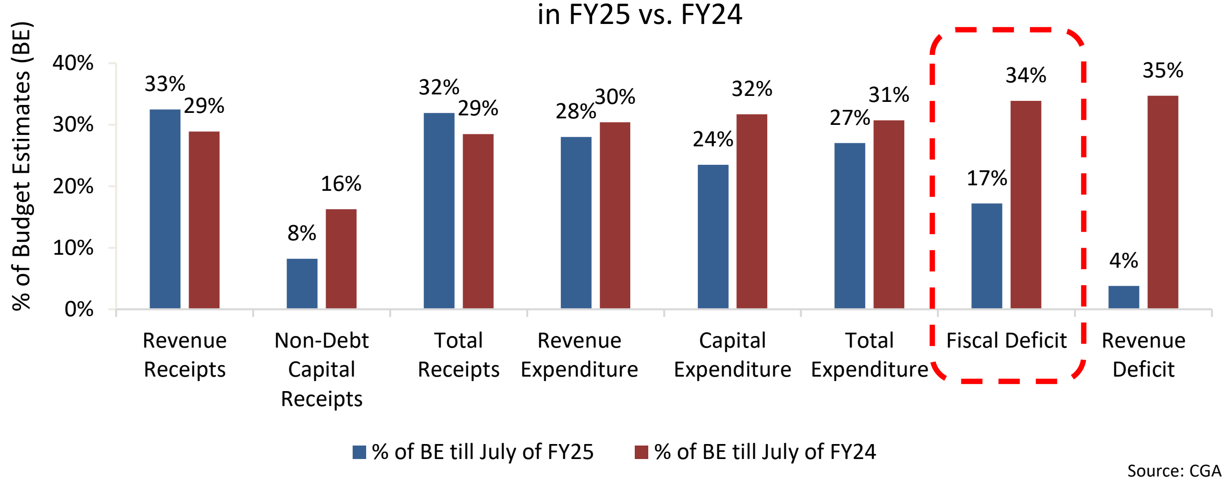
Fiscal remains comfortable, the potential lack of supply can weigh down on bond yields

As the year progressed, the fiscal deficit has been under check due to lower government spending



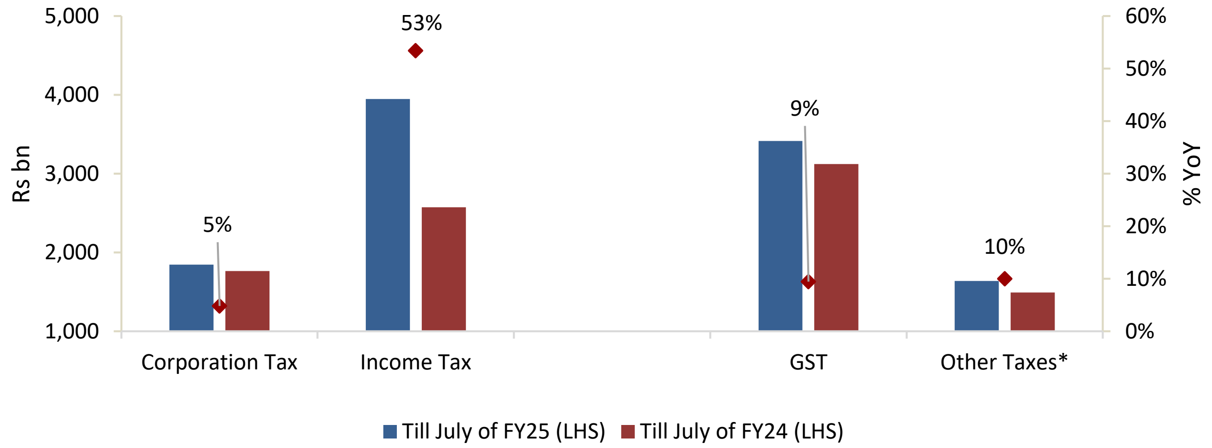
Source: CGA

Higher revenue and lower expenditure leading to narrowing of fiscal deficit in FY25 vs. FY24



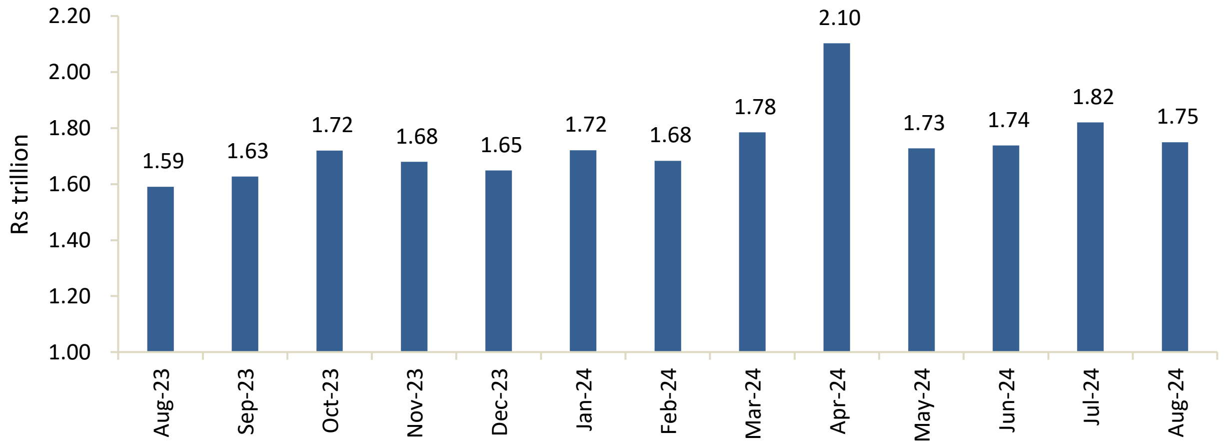
Source: CGA

Significant jump in income tax suggests a structural shift in tax revenue



Source: CGA

GST collection remains robust and continues its momentum

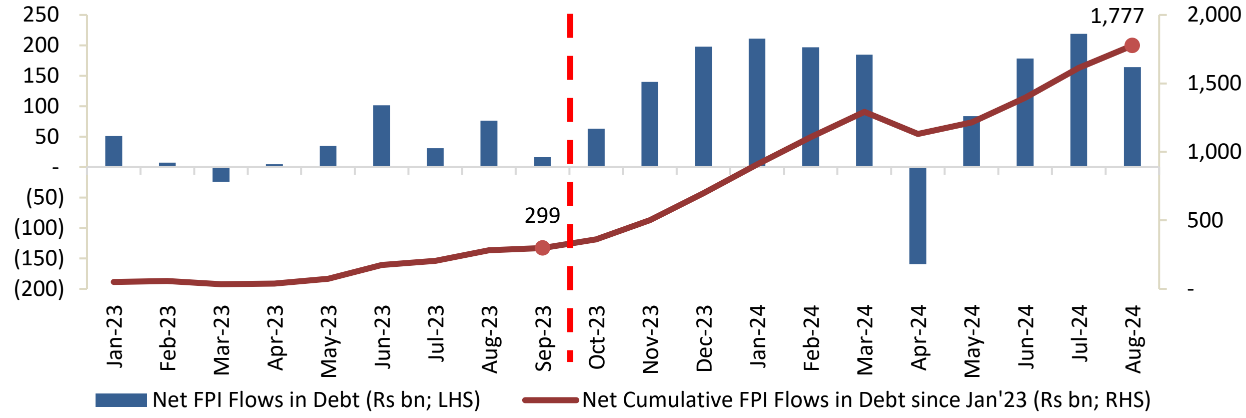


Source: Cogencis

Classification - Public

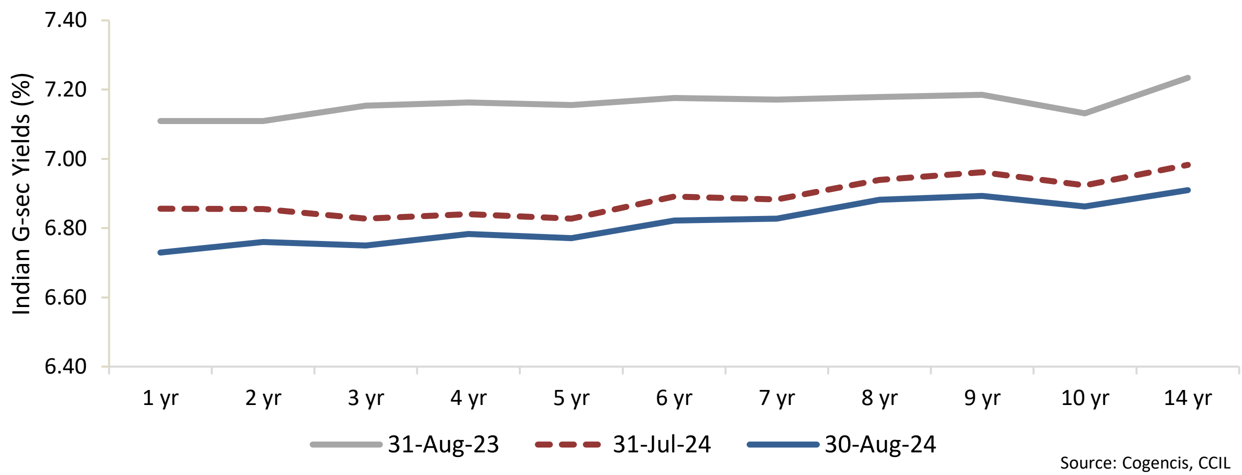
Fiscal consolidation and JP Morgan global index inclusion have ensured that G-sec yields continue to remain under pressure

FPI Investments picked-up pace post the announcement of G-secs' inclusion in the JPMorgan's Government Bond Index-Emerging Markets (GBI-EM)



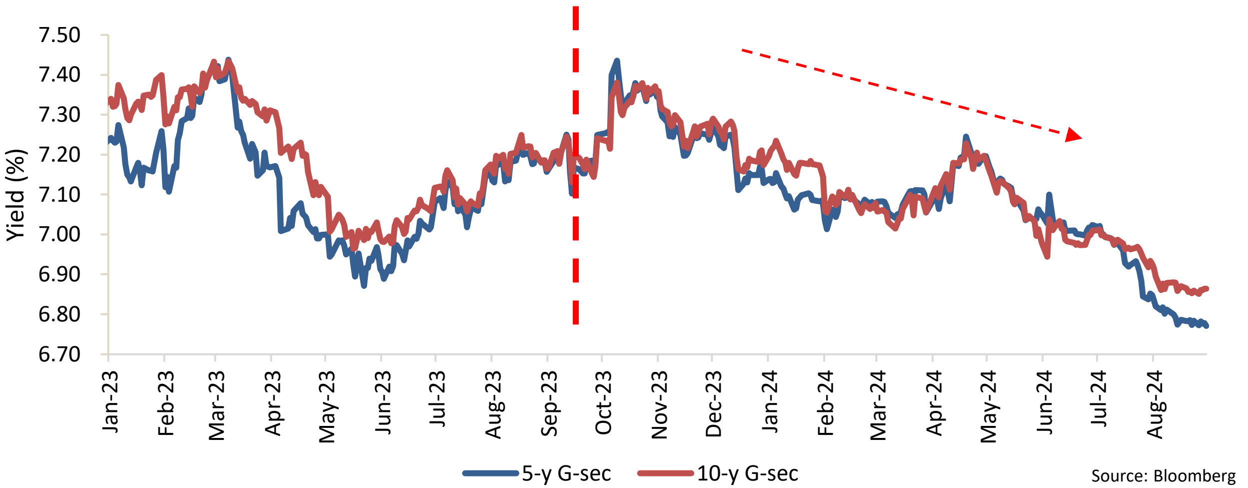
Source: Bloomberg

As the G-sec yield curve declined, Dynamic Bond Funds have benefitted



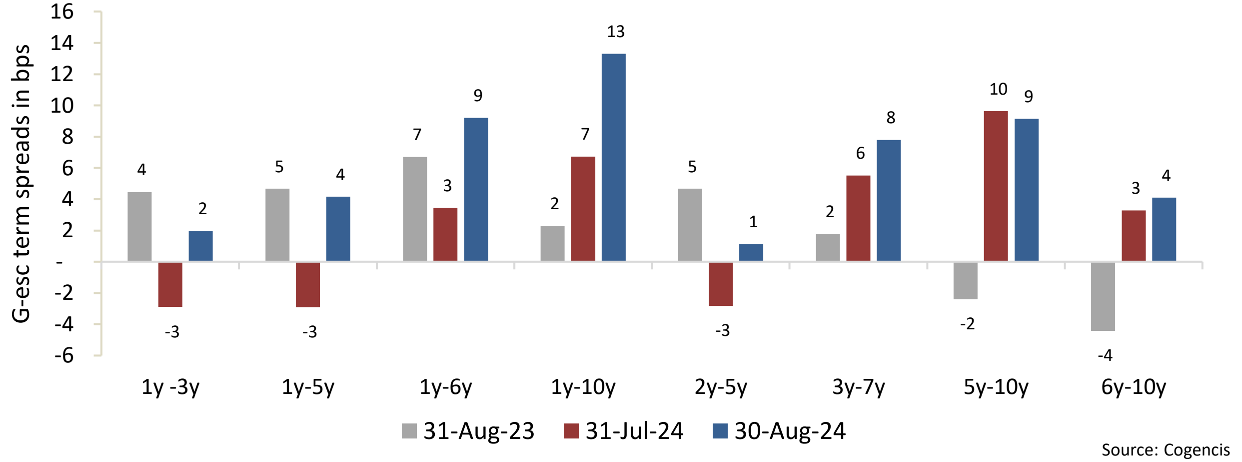
Source: Cogencis, CCIL

With higher demand and limited supply, G-sec yields have moved lower



Source: Bloomberg

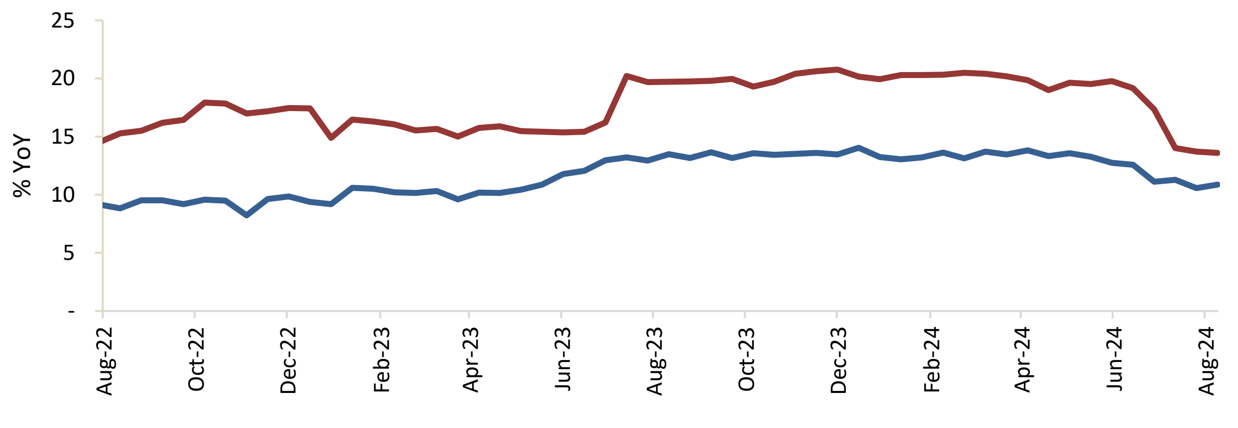
Term spreads widened due to easing liquidity conditions



Source: Cogencis

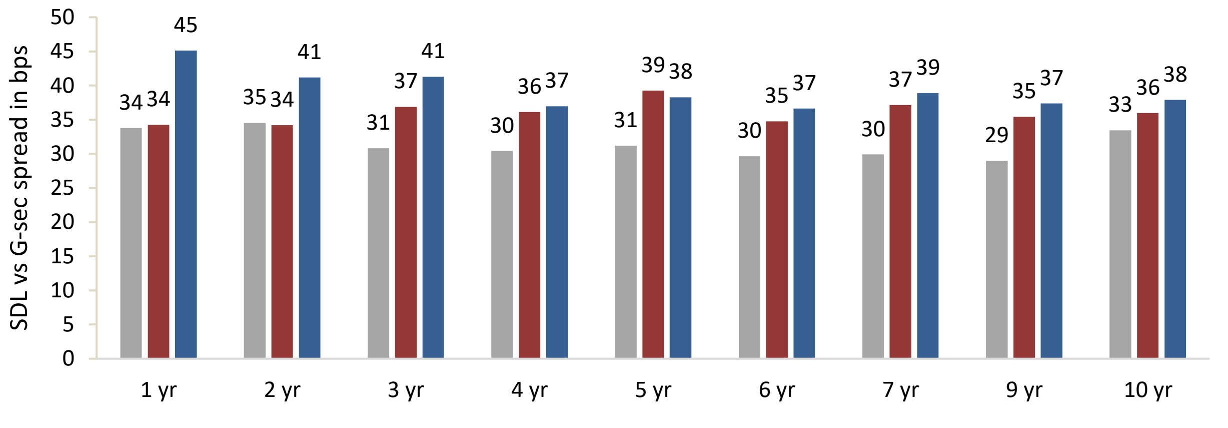
Corporate bond spreads have consistently improved, making the case for accrual products due to significant exposure to corporate bonds

With anaemic bank deposit growth, cost of credit for corporates may rise



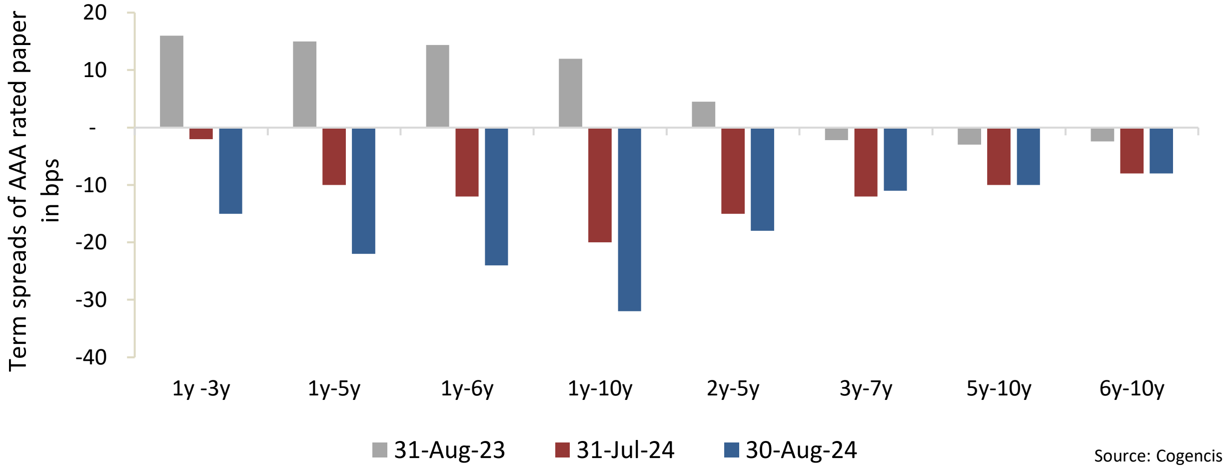
Source: Bloomberg

SDL spreads widened as supply increased incrementally



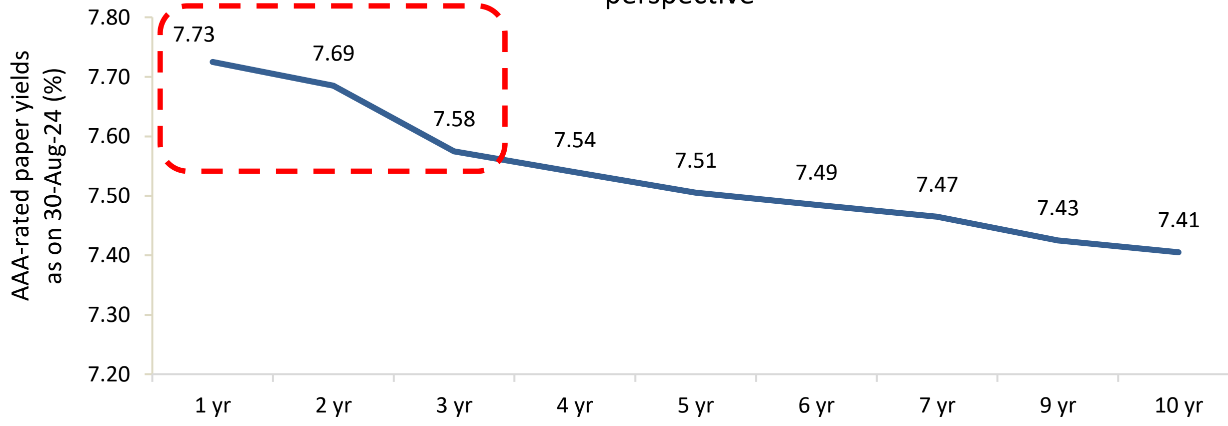
Source: Cogencis

Term spreads inverted further due to higher supply at shorter end



Source: Cogencis

1-3-y segment of corporate bond curve remains attractive from an accrual perspective



Source: Cogencis

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