Dear Investor,

India continues to shine!!

The global equity markets have continued strengthening in July riding on improved macroeconomic stability and positive investor sentiments. Many global indices like the US S&P 500 and Japan's Nikkei 225 have recently touched its 52-week high. Japan markets touched new high after 33 years. Indian equity markets too have fared well with Nifty50 also touching all-time high in July 2023.

Post the peak of equity markets in the last quarter of CY2021, many global markets (except India) saw steep correction. The MSCI Emerging Market excluding China Index witnessed a steep drop post 2021 and has been undergoing recovery in last 1 year. US S&P500 showcases a similar trend as it is yet to touch its all-time high reached in 2021. China is still struggling with Shanghai Shenzhen CSI 300 Index having a negative return in the same period. On the other hand, Indian Nifty50 has surpassed its peak of 2021 and the returns have been far superior compared to the other markets.

The recent improvement in global macroeconomic scenario can be viewed as an impetus to growing positivity in investor sentiment driven by multitude of factors. The inflation levels across the globe have been declining due to strong monetary policies by the Central Bank of the various economies. US inflation levels fell below its long-term average of 3% in June 2023. Similar trend can be viewed in other parts of the world:

- Inflation in the UK came down to a 15-month low of 7.9%.
- Australia June quarter inflation drops to 6% as compared to 7% in the previous quarter.
- Inflation rate in Canada fell to 2.8% in June '23, which was below market expectations of 3%.

Though Consumer Price Index (CPI) in India jumped to 4.8% in June, mainly led by food inflation, it was still within RBI's tolerance limit. Further, Wholesale Price Index (WPI) being negative for third straight month (-4.1% in June'23), should trickle down to the retail consumers in the coming months, and CPI would come within RBI's medium-term target of 4%.

Most of the Indian Indices continued their upward trajectory. Nifty 50 was up by 3.0% and was also close to entering the 20K mark in the 3rd week of July. Nifty Midcap outperformed the large cap, with a gain of 5.5% (NIFTY Midcap 100). Nifty Small Cap outperformed the broader market with a return of 8.0% (Nifty Small Cap 100). Capital Goods saw a major uptick with the BSE Capital Goods index gaining over 8.2%, on the back of strong manufacturing growth with a sharp rise in order inflow. The realty sector continued its positive momentum as Nifty Realty gained 9% this month.

India Equity market gains buoyed by complex interplay of interconnected factors

With the Indian markets reaching an all-time high, it begets a question: is this rise backed by fundamentals or merely flows, is it temporary or permanent? What have been the causal factors of such returns?

Markets worldwide has been buoyant this calendar year and India has been no different. However, when viewed from the lens of longer-term perspective, India stands out. We believe following global and local factors have been the driving the markets:

Global:

- **Inflation on downtrend:** Inflation trajectory worldwide has been on downtrend. US inflation moderated to 3% in Jun-23 vs record high of ~9% YoY in Jun-22. The downward trend in US inflation is raising markets' expectation of end in Fed rate hike cycle hence supporting the risk on rally US equities. Moderation in DXY below 100 is also giving further impetus to EM rally.

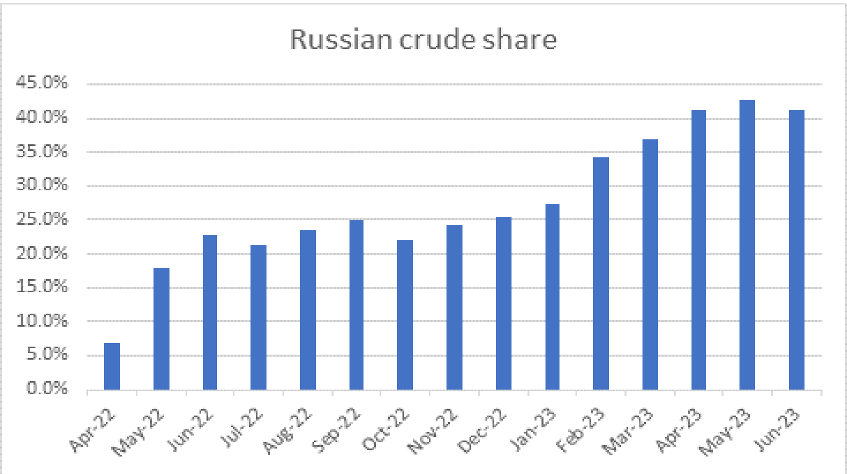
- **Receding geopolitical risks:** Overall geopolitical risks have reduced considerably. The heightened tensions between US & China have seen some reduction and surprise resilience from Ukraine aided by the West and recent Wagner uprising are increasing the probability of a prolonged stalemate and gradual weakening of Russian power.

Local:

- **Global growth leadership:** With the advent of fear of recession in the developed economies of the west, clubbed with weaker than expected recovery of China in last couple of years created a state of economic instability in the world. As a result, there was a fall in the global demand for goods and services as well. This did some impact on the goods exports. However, India's real GDP growth rate was over 7% in 2022-23 and expected to remain over 6% in 2023-24. Among large economies, India is expected to grow fastest.

- **Real sector remains resilient:** Lead indicators of real economy like Purchasing Manager's Index (PMI), GST collections remains elevated pointing to resilience of the economy. Manufacturing and Services PMI remained comfortably above 50 indicating expansion, GST collection touched INR 1.6 lakh crs in Jun-23 staying consistently above INR 1.5tn in CY23. E-way bill generation remained robust averaging ~16% YoY in Q1FY24 vs 18% in Q4FY23.

- **Receding external vulnerabilities:** India's emerged as a stable and reliable economy during a period when the global geopolitical situation was very volatile, owing to Russia – Ukraine War. Geopolitically India has managed the situation very well. Also, as the war unfolded, US and European sanctions and oil price caps affected world trade patterns majorly. Thus, Russian Brent Oil was available at a discounted price. With India increasing imports of Russian Oil, it kept the oil bill for the country in check along with helping in bringing down domestic inflation. Also, India is able to carry out trade in INR with 18 countries including Russia, UAE, Germany and UK. India's handling of geopolitical situation and managing foreign trade partly in INR, reduced its external vulnerabilities sharply.

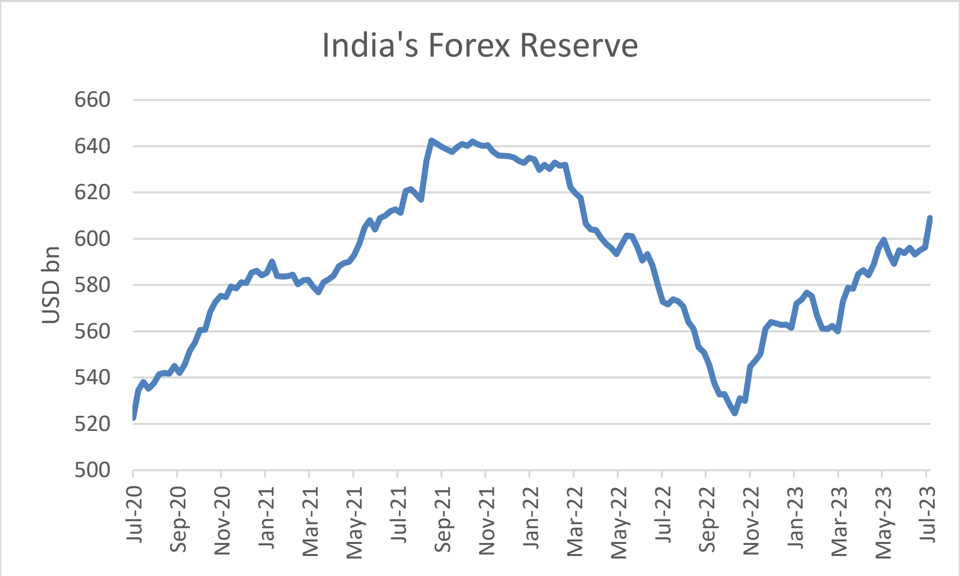


Source: Petroleum Planning & Analysis Cell; ASK IM Research

- **Inflation on a downtrend:** India's inflation trajectory has remained on a downtrend barring recent spike in June due to transitory rise in vegetable prices. In Q1FY24, headline CPI averaged 4.6% YoY vs previous two-quarter average of 6.2% YoY. Although the base effect played its part in lowering the YoY inflation, falling global commodity prices, and moderation in core inflation supplements the downward trend. When compared globally, India's 1HCY23 inflation averaged 5.4% YoY, lower than developed markets like European Union and UK where inflation averaged 8.3% and 9.3% YoY in 1HCY23 respectively. India's wholesale prices moved into deflation territory with Q1FY24 decline averaging 2.8% YoY vs 3.3% average rise in Q4FY23 suggesting further downside to core inflation.

- **End of rate hike cycle:** Post 250bps rate hike cycle, Reserve Bank of India's Monetary Policy Committee (MPC) opted for pause in FY24 and expectations of staying in a pause remains ripe. Expectation of rate pause has lowered 10y yields to 7-7.1% range vs 7.61% in June 2022.

- There has been a steady rise in the India's forex reserves in the last one year. After a major drop in the forex reserves in 2022, it has been steadily building up in the last 9 months. This month, it crossed the $600 bn mark. Consequently, there has been increased stability of Indian currency in the foreign exchange market, resulting in INR being one of the least volatile currencies in last one year.



Source: Bloomberg; ASK IM Research

- **China+1** sentiment should aid India's manufacturing growth trajectory. As many companies look to reduce their dependency on one nation for their operation, India stands a chance to cash in on this opportunity as well.

- **Capex activity improving:** There has been a rise in capital expenditure by the Indian Government. This should have a crowding-in effect that would revive private investment which has lagged in the last 2 years. Other factors that should contribute to growth of private investment are the recent reduction in corporate tax rate and better positioned banks with healthier asset quality.

- **Strong demographics:** India's strong demographics profile will play an important role in its growth. India has a relatively young population with median age of 29 years. Further India should reach its highest level of working age population by 2030. This should translate into competitive advantage for the economy. This will also drive the consumption expenditure which would fuel the growth of the economy. Moreover, India's per capita Income should increase resulting in upward push of households from lower/middle and low-income strata to high and upper/middle income bracket. This kind of demographic advantage among large economies is unique to India.

- **Relative strength of corporate earnings:** Earnings for Nifty are expected to experience a substantial YoY increase of 20%+ in Q1FY24. This robust growth would primarily be propelled by domestic cyclical sectors such as BFSI, and Auto. Conversely, globally linked sectors like Metals, Chemicals and IT are anticipated to dampen overall growth to some extent. Notwithstanding, with a 15% YoY earnings growth expected for the Nifty in FY24, the outlook for earnings growth of India Inc is alright. India stands in a strong position to lead the global earnings landscape.

In or opinion, Indian equities at all-time highs isn't necessarily a cause of worry. Valuations, though optically, are now slightly above long period average, they are backed by earnings, fiscal and geopolitical stability. Financial, Auto and Energy are expected to drive the earnings. Rural slowdown is moderating and expected to improve going forward. Overall, we believe the long-term growth trajectory of Indian markets should remain intact.

Happy investing!

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