

Data Revisions – Spanner In The Works

14th Mar'24

The global economy is increasingly getting data-dependent as major central banks reassess their monetary policy stance amid signs of peak interest rates and resilient inflation. We believe that the US Fed will most likely lead other major economies on the interest rate revisions, with the European Union and the Bank of England (BoE) expected to follow suit soon after. The Reserve Bank of India (RBI), meanwhile, seems steadfast in aligning the Consumer Price Index (CPI) to the targeted glide path of 4% and hence may lag behind its global peers on policy normalization. The Bank of Japan may finally look at revisiting its stance on yield curve control.

This brings to the fore an emerging trend of data revisions which has the potential to aid further volatility to risk assets. We had two major data revisions over the past couple of days, which when revisited, point to starkly contrasting outcomes, namely the US Non-Farm Payroll (NFP) job additions in Jan'24, which was revised downwards by 124k, while Japan's Q4 GDP growth was revised upwards to 0.4% from -0.4% (from technical recession to expansion). The policymakers as well as market participants, thereby, will have to assess a multitude of information sets before arriving at a consensus view of the economic scenario.

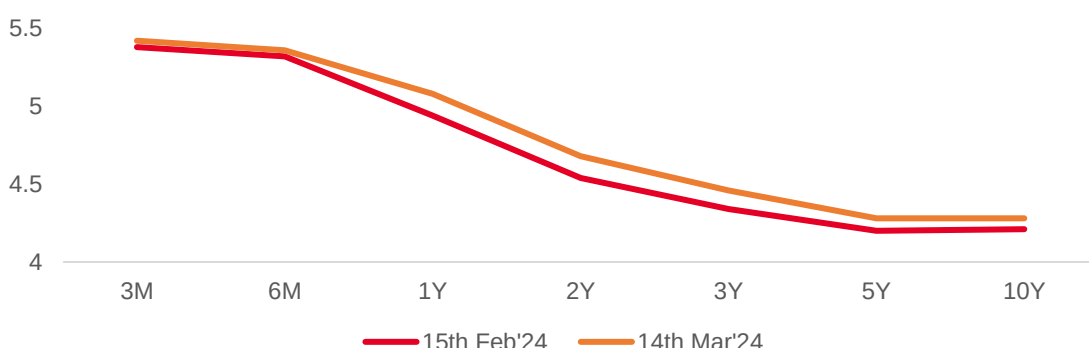
US Economic Data Release:

- The Non-Farm Payrolls for Feb'24 expanded by 275,000, against market expectations of 198,000. However, the previous two-month jobs data witnessed a downward revision of 167,000, thereby highlighting that the jobs trend isn't as robust as markets had initially interpreted. Hourly earnings rose by 0.1% in Feb'24, making for a 4.3% YoY gain – marginally lower than market forecasts of 0.2% and 4.4% growth respectively.
- The unemployment rate rose to a 2-year high of 3.9%.
- Headline inflation for Feb'24 grew 0.4% MoM and 3.2% YoY, broadly in line with expectations.

The Fed Chair Jerome Powell, in his recent speech to the House Financial Services Committee, hinted at interest rate reductions later this year, while reiterating the stance that the decision would be based on the interest rates broadly aligning to the 2% target range.

Market Impact: The US Yields were volatile last month, trending lower post the jobs and unemployment data, but moving higher post the CPI release. The US equities witnessed marginal rotation, with the S&P 500 taking a lead (up 2.4% MoM), while the NASDAQ followed closely (up 1.5%) and the Dow Jones up 0.34%. **We are seeing increasing divergence between the US yields and the US equities in YTD'24 with Yields moving sharply higher, repricing extension of peak rates while the US equities appear nonchalant.**

The global equity indices had an overall bullish run over the past month, led by Hang Seng (up 7.7%) followed closely by Euro 50 (up 4.3%) with Nifty, Nikkei, and FTSE moving higher by 3.6%, 2.2%, and 2.1% respectively. The USD index has been relatively steady and is currently trading around 103.4.



Global central banks interest rate outlook:

The policy meetings held in Feb’24 and Mar’24 continued to hint towards achieving peak interest rates and the scope of monetary policy easing in the latter half of the year without providing any clear glide path on the extent and timing of reduction in interest rates. The overarching sense has been one of caution, and not easing policy rates prior to a structural decline in interest rates is achieved, while acknowledging that a continued hawkish policy stance will have an impact on economic growth, which barring the US and India, is already showing signs of slowdown globally.

Global Central Bank Policy Snapshot

Central Bank	Rate	Last Change	Next Meeting	Expectations
Bank of Canada	5.00%	12 th Jul'23, 25 bps Hike	10 th Apr'24	Status Quo
Bank of England	5.25%	2 nd Aug'23, 25 bps Hike	21 st Mar'24	Status Quo
Bank of Japan	-0.10%	29 th Jan'16, 20 bps Cut	19 th Mar'24	Status Quo
European Central Bank	4.00%	14 th Sep'23, 25 bps Hike	11 th Apr'24	Status Quo
US Federal Reserve	5.50%	26 th Jul'23, 25 bps Hike	20 th Mar'24	Status Quo
People's Bank of China	3.65%	25 th Jan'24, 50 bps Cut		
Reserve Bank of Australia	4.35%	7 th Nov'23, 25 bps Hike	19 th Mar'24	Status Quo
Reserve Bank of India	6.50%	8 th Feb'23, 25 bps Hike	6 th Apr'24	Status Quo
Swiss National Bank	1.75%	22 nd Jun'23, 25 bps Hike	21 st Mar'24	Status Quo

Gold prices rise

After trading flat in January and February, the gold prices have risen sharply in March. As of 12th March, the precious metal is up by more than 6% for the month, having broken through the \$2200/ounce handle on its way. The Fed Chair Jerome Powell’s indication that the central bank may cut interest rates in the coming months boosted the market confidence, resulting in gold reaching a fresh all-time high.

Crude rises on expectations of output cuts

After finishing January up around 5.9%, crude oil continued the momentum in February, ending the month higher by around 3.2%. This was on the back of the expectations that the Organization of the Petroleum Exporting Countries+ (OPEC+) is considering extending voluntary oil output cuts into the second quarter to provide additional support to crude prices. March is currently trading slightly in the red (down 0.5% as of 12th March) after China reported weak demand data.

China consumer price index climbs

China recorded its first month of inflation in February after four months of deflation with the consumer price index climbing 0.7% YoY after a 0.8% annual decline in January. However, according to market strategists, this can be attributed to the Lunar New Year period, and deflation still looms over the Chinese economy. On the GDP front, the Chinese government recently announced that it is targeting 5% growth in 2024, having achieved 5.2% in 2023.

Bitcoin Prices Skyrocket

Bitcoin prices have been on a tear of late, with 1-month returns of 48% and 1-year returns of 177%. The US Securities and Exchange Commission’s (SEC’s) approval of Bitcoin ETF has been the key catalyst to this move which has led to added credibility of Bitcoin as an asset class.

INR gains marginally against the USD

INR marginally strengthened against the USD over the past month, currently trending at around 82.79 (as of 12th Mar'24) against 82.97 (as of 12th Feb'24). This is on the back of a sustained inflow of foreign funds in the domestic capital markets. Over the medium term, the RBI has managed the depreciation of the rupee against the USD in a controlled manner via regular interventions.

Indian Macro Update:

We continue to tread a path of robust macro-economic landscape as is evident from strong readings across multiple components even as fiscal balance turns sturdy owing to buoyant direct and indirect tax collections and fiscally prudent governance at the center. Some key highlights are provided below:

- India's GDP registered a growth of 8.4% in Q3'FY24, which was significantly higher than the market expectations of 6.5-6.6%. Manufacturing, industry, and construction led the growth, up 11.6%, 10.4%, and 9.5% respectively while the agriculture sector contracted by 0.8%. The FY'24 GDP growth has been subsequently revised upwards to 7.6% from 7.3% post the robust Q3 GDP release.
- One key aspect of India's GDP growth has been the gap between Gross Value Added (GVA) and the overall GDP number, with GVA expansion being 6.5%. The gap was owing to a surge in net indirect tax collections by 32% during the quarter, a figure which, albeit robust, may be an exception, and to that extent, the overall GVA growth figure may be taken as a more accurate barometer of underlying buoyancy in the economy, which we reiterate, continues to be robust.
- India's eight core industries continue to grow, although the rate of growth has decelerated in Jan'24, with YoY growth at 3.6% compared to 4.9% in Dec'23. All sectors barring refinery products and fertilizers registered growth, led by Coal and Steel which grew by 10.2% and 7%, respectively.
- The Index of Industrial Production (IIP) data for Jan'24 rose to 3.8%, marginally lower than 4.2% in Dec'23. Consumer durables registered the strongest growth trend, growing by 10.9% YoY while Intermediate and Capital goods grew by 4.8% and 4.1%, respectively. A decline in growth was observed in non-durable consumer goods (-0.3%) while primary and infrastructure goods registered positive but declining growth trends MoM.
- India's manufacturing Purchasing Managers' Index (PMI) for Feb'24 rose to 56.9, the highest reading in five months led by growth in new orders and outputs which were also at a five-month high. This marks a consecutive 32 months of expansion for the manufacturing sector underlining the inherent robust manufacturing landscape in the economy.
- Services PMI slowed down marginally in Feb'24, with the index falling to 60.6 from 61.8 in Jan'24 as growth in new orders and outputs softened MoM. The current reading, however, is extremely robust and underlines the overall strength in the services sector which has also been in expansion for the previous 31 consecutive months.
- GST collections continued their robust growth, with Feb'24 collections at INR 1.68 Tn, posting a YoY growth of 12.5%. For Apr'23-Feb'24, the cumulative GST collections reached INR 18.4 Tn, a growth of 11.7% as compared to the same period in the previous financial year.
- India's fiscal deficit for Apr'23-Jan'24 stood at INR 11Tn, which accounts for 64.5% of the targeted deficit in FY'24. This was lower than INR 11.9 Tn in deficit for the same period last year. The Finance Ministry is targeting to rein in fiscal deficit to 5.8% of the GDP in FY'24. The Revenue expenditure growth has been tepid at 1.4% for the ten months this fiscal, versus the targeted 2.6%. The capex spending fell sharply in Jan'24, at INR 0.48 Tn as compared to INR 0.8 Tn as of Jan'23.

Indian Equity Update :

The Nifty 50 index closed the month of February up 1.18% at 21,982. In the current month, the index is up 0.75% (till 14th Mar'24), trading around 22,146. The Foreign Institutional Investors (FIIs) were net sellers in February, with net sales of around INR 15,962 crores. Then Domestic Institutional Investors (DII) were net buyers, registering net purchases worth INR 25,379 crores.

In contrast to the benchmark Nifty 50 index, the Smallcap and Midcap indices were slightly down in February & fell sharply in March so far. The Nifty Smallcap 250 index was down 0.65%, while the Nifty Midcap 100 index was down 0.48% in the month of February. In the current month, the Nifty Smallcap 250 is down 7.17% while the Nifty Midcap 100 is down 2.97% (as of 14th Mar'24).

The downward trend in small & mid-cap stocks was triggered by concerns raised by the market regulator SEBI regarding the froth building up in small-cap and mid-cap segments. The mandated AMFI-SEBI stress test is also weighing on the market sentiment.

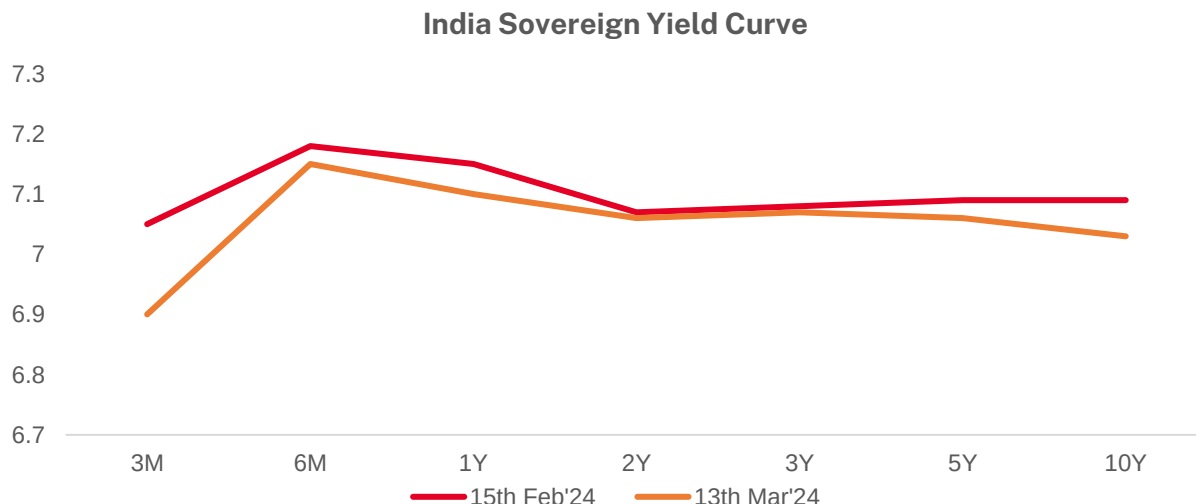
SEBI had directed the Association of Mutual Funds India (AMFI) to ensure that asset management companies (AMCs) prepare risk disclosures for investors regarding mid-small cap schemes and conduct stress tests which will be useful in figuring out if the portfolios are liquid enough to meet a sudden rise in redemptions.

Following this, a few mutual fund schemes have started reducing exposure to midcap and small-cap stocks. Amidst this increased scrutiny, the Enforcement Directorate (ED) raids against a Dubai-based trader added to a sell-off in a few small-cap stocks.

Concerning sectoral indices, Nifty Financial Services & Metal ended the month slightly down, falling 0.44% & 0.64% respectively. On the other hand, Nifty PSU Bank, Realty, and Auto had a stellar month, closing February up 10.49%, 6.35%, and 6.16%, respectively. In the current month (as of 14th Mar'24), Nifty Realty & Nifty PSU Bank is down 8.68% & 2.10% respectively, while Nifty Financial Services is up 1.56%.

India Fixed Income Update :

Indian sovereign yields trended lower over the past month across the maturity curve and noticeably in the shorter end, especially up to the 3-month maturity as can be seen below:-



We have highlighted a few key factors impacting the Indian Fixed Income yields below:-

- **Resilient FPI Inflows:** The Foreign Portfolio Investment (FPI) inflows into the Indian debt markets have witnessed a major upsurge. For YTD CY'24, FPIs have invested nearly US\$6 Bn in Indian bonds, continuing a trend we witnessed in CY'23 where the net FPI inflows were US\$7.8 Bn, the first year of positive flows since CY'17. The inflows in YTD CY'24 are significantly higher than US\$0.6 Bn during the same period last year.
- **India CPI:** Retail headline inflation continues to trend in a narrow range with Feb'24 CPI growing 5.09%, 1bps below Jan'24 growth at 5.1%. The headline range has now been within the RBI's band of tolerance (defined between 2-6%) for the sixth consecutive month. The pace of decline, however, is muted and hence may lead to an extended 'higher for longer' stance from the RBI.
- **System liquidity improves:** Indian system liquidity turned positive as of 12th Mar'24 at INR 0.05 Tn as compared to a deficit of INR 2.23 Tn during the same period last month. Tighter liquidity conditions have kept the short-term rates elevated for a few months with shorter-end yields (up to 1 year) trading significantly higher than the mid and the longer end. This scenario has reversed over the past week, although we would have to await RBI's stance on system liquidity in the near term.
- **RBI hawkish 'status quo' policy stance:** The RBI's Monetary Policy Committee (MPC) members, in their recently concluded policy meeting upheld their targeted CPI inflation range of 4%. They also provided a forecasted CPI range till Q4'FY25, wherein the CPI isn't envisaged falling below 4%. This has led to market participants repricing the probability of a policy pivot from RBI further into Q4'FY25.

OIS curve comes off marginally:

The Indian Overnight Indexed Swap (OIS) Curve is normally taken as a lead indicator for the future interest rate trajectory. Compared to the 1-year OIS level of 6.73 and 5-year OIS level of 6.34 as of 15th Feb'24, they stood at 6.71 and 6.27 respectively as of 12th Mar'24. This reflects market pricing in an extended 'higher for longer' stance from RBI.

Investment Outlook :

We encourage investors to adhere to 'Asset Allocation' and calibrate investment decisions by carefully monitoring the ever-evolving economic and geopolitical data points. Marrying our in-house Asset Allocation framework with our current stance on markets (as explained above), we build an investment outlook as follows –

- Indian equities, especially well-managed mid and small-cap portfolios, have contributed phenomenally towards investor portfolio returns in CY'23 while large-cap portfolios lagged the broader markets. Over the past month, the large-cap index has turned around with the Nifty 50 up 0.8% while the Nifty Midcap 100 and Nifty SmallCap 100 are down 3.9% and 8.6% respectively. We believe sector rotation is a key barometer for a healthy and sustainable bull market cycle and hence certain sectors that missed out on last year's rally may do better in the current year. We continue to be bullish on equities as an asset class and believe a staggered allocation over the next 4-6 months to be the preferred route towards fresh allocations.

- Indian fixed income as an asset class presents a two-fold opportunity. Tighter liquidity conditions have ensured attractive yields up to 1 year across the credit curve, while the mid to longer-end yields are well-bid owing to the favorable demand-supply scenario that is emerging currently. We continue to prefer allocations to funds running maturities in the 2–5-year bucket. The longer-end yields have also moved lower, although we believe that going forward, the movements would be a function of the policy pivot as well as expected global ETF flows starting Jun'24. The investors could also look to invest in well-managed credit funds to lock in a relatively attractive coupon rate (on the AIF platform) with a focus on capital preservation and periodic cashflows.
- Global growth has started a phase of decline while interest rates remain resilient. This situation coupled with continued geopolitical escalations in the Middle East and Eastern Europe is expected to keep global markets tentative. Although Indian markets have been relatively unaffected this far, enhanced volatility in risk assets can't be ruled out, especially with general elections around the corner. Hence, Volatility Hedge strategies primarily played out through a judicious mix of market neutral and select long-short positions, taking advantage of sector rotations, need to be maintained.
- Our view on maintaining a steady allocation to gold has reaped steady returns for investment portfolios over the past year and we continue to be bullish on the commodity as a vital asset allocation tool, especially in the current economic and geopolitical backdrop.

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