Elara Capital

India: Manifesting its mojo

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Economics

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Elara Securities (India) Private Limited

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Global economy – rate cuts to offset growth pessimism in 2024

- **Growth outlook**: We see the US economy slowing materially, yet skirting recession in 2024 and Europe and the UK facing stagnation. China is expected to slow further in 2024, adding challenges to overall Asia ex-India. India is expected to remain a positive outlier.
- **Inflation outlook:** We expect inflation to come down incrementally globally, but core inflation downtrend is likely to be stickier than headline. Bias for oil prices continues to be on the lower side. Food prices are a key risk.
- **Central banks' outlook:** We see 2024 as the year of rate cuts across the global economy, with developed markets (DMs) cutting at a faster clip than emerging markets (EMs) to traction growth. We price in a 100bps cut by the Fed, 75bps by the RBI, and 125-150bps by ECB and BoE. BoJ is likely to go other way – we see BoJ abandoning Yield Curve Control and lifting policy rates in 2024.
- **India**: We project FY25E growth at 6.9-7%, inflation at average 4.5%, policy rate 5.75% by March 2025E, USD-INR 81 and 10-year yield 6.8-7.15%. Domestic private consumption and trade risks are likely risks to FY25 growth.
- **The mega theme:** India is manifesting an increase in indigenous manufacturing, improved resilience to crude oil prices, and rise in total factor productivity amid sustained enhancement in capital formation.

What can go wrong? Risk to our calls for 2024

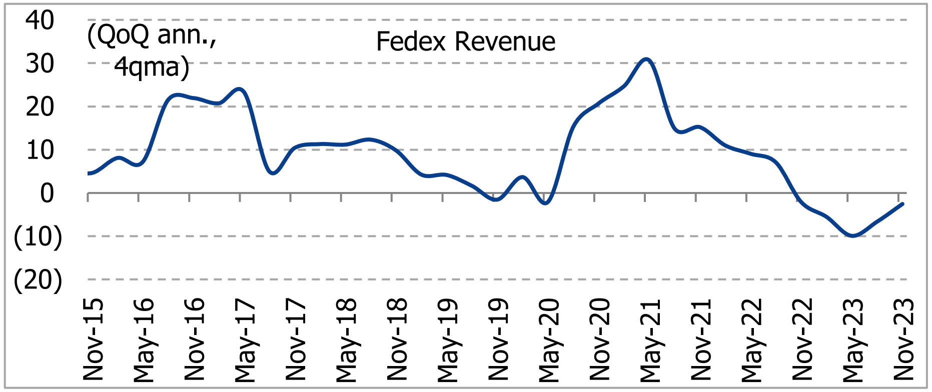
- Longer-than-expected wait for first cut by the Fed and other DM banks (ex-Japan).
- Flaring up of geopolitical tensions in the Middle East as a fall-out of Israel-Hamas conflict.
- China-led over production in Industrials threatening nascent uptick in domestic manufacturing in India.
- Elongated Red Sea /Panama Canal risks inject permanent upside to 2024 inflation projections.
- Return of GOP in the US likely leading to potential withdrawal of US troops from Ukraine, abandoning US-Israel relationship, pulling back spending and jeopardizing meeting climate goals.
- Capex allocation by the Indian government begins moderating even as private capex cycle slows down.
- Slowdown in consumption and growth amid tightening rules for unsecured credit.

CHAPTER I

GLOBAL ECONOMY AND INDIA: TOP-10 ELARA PROGNOSES FOR CY24/FY25

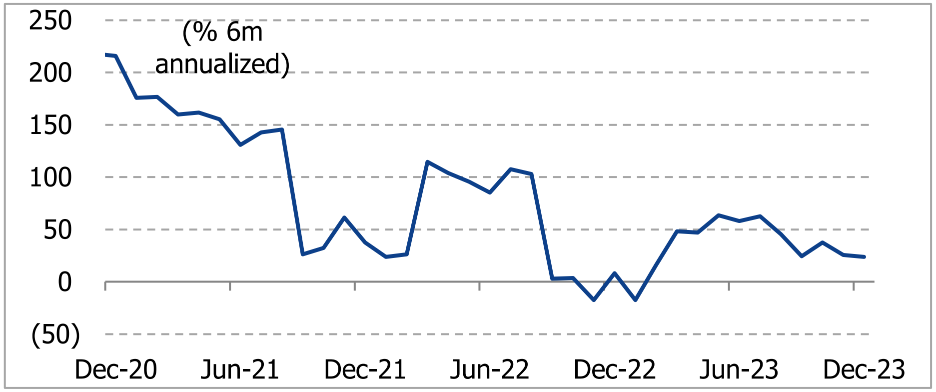
#1: Overall global economic momentum slow going into 2024...

Fedex revenue momentum has declined



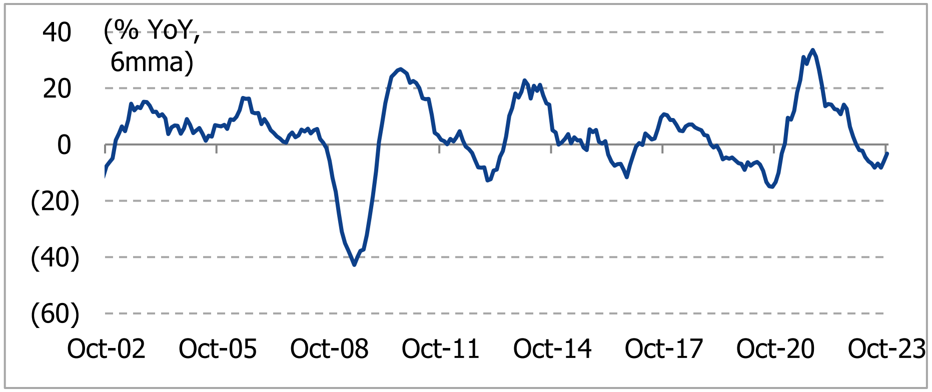
Source: Bloomberg, Elara Securities Research

South Korea: Exports growth on downtrend



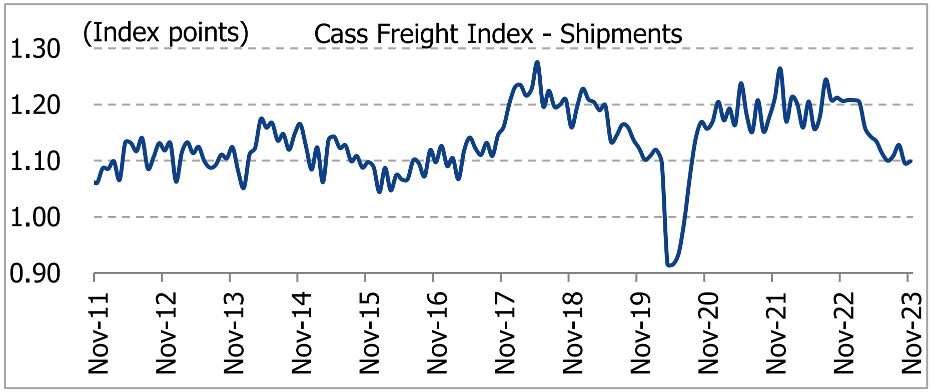
Source: CEIC, Elara Securities Research

Japan: New orders for Machinery muted



Source: CEIC, Elara Securities Research

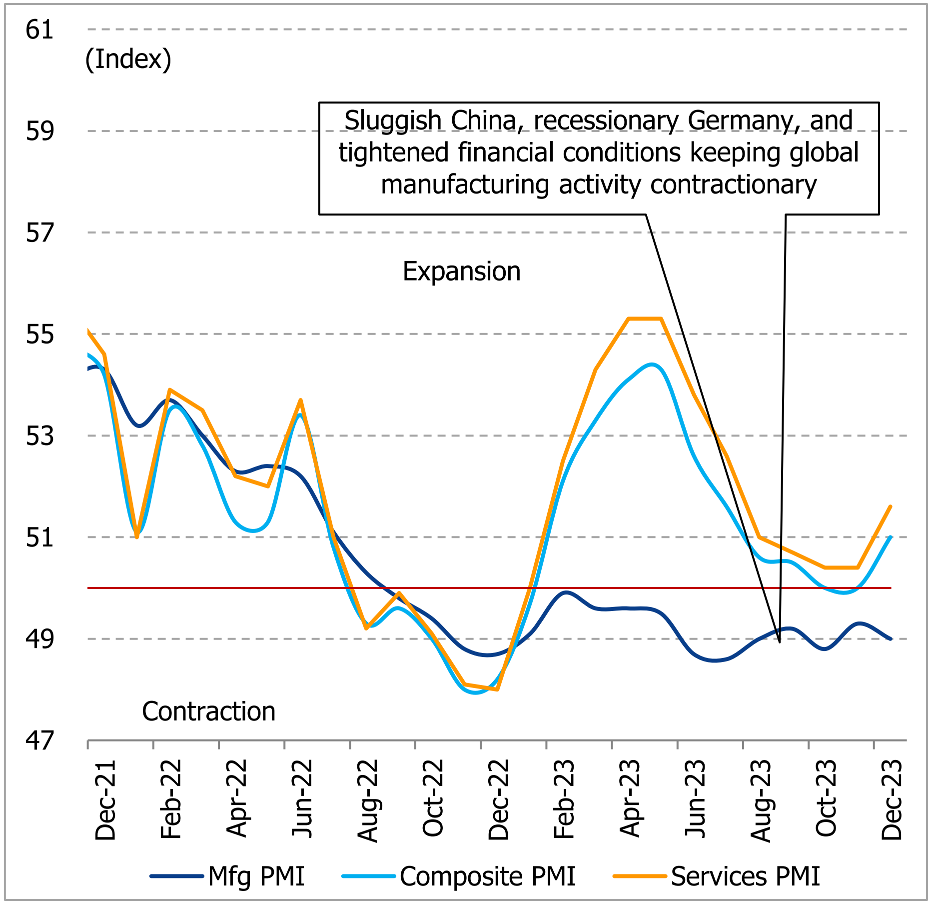
US: Shipments falling sharply



Source: CEIC, Elara Securities Research

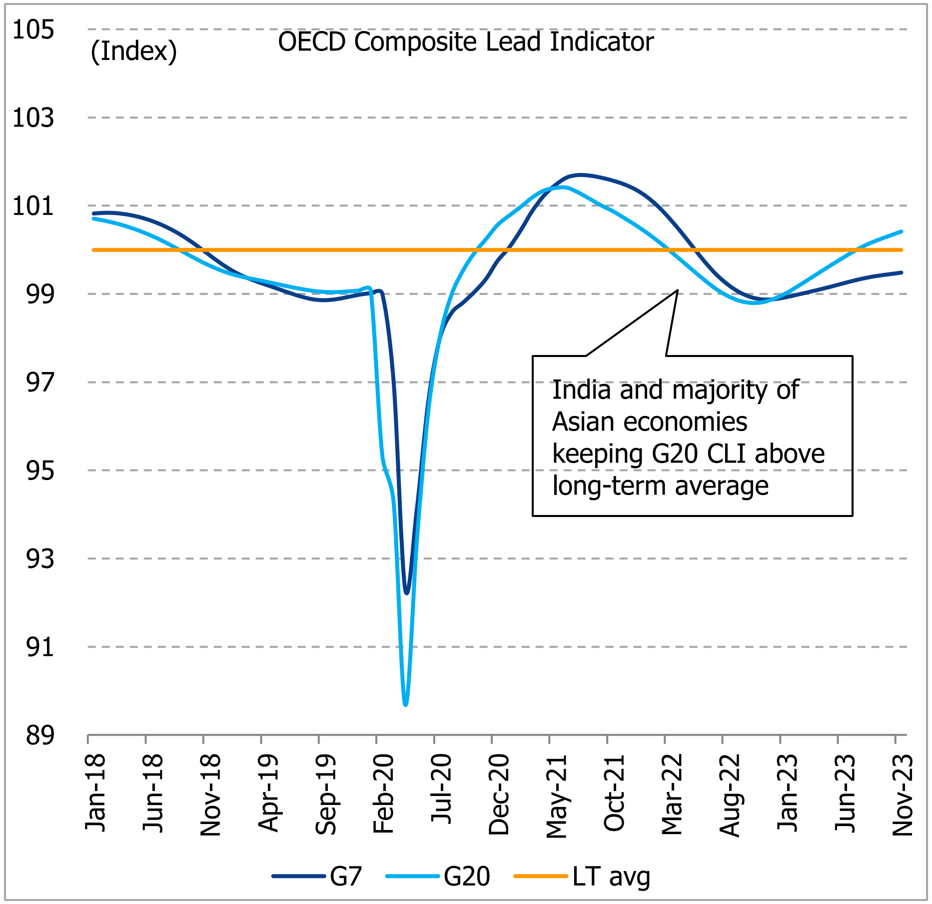
...with business and economic activity in G7 staying muted

Manufacturing activity consistently contracting



Source: Bloomberg via JP Morgan Indices, Elara Securities Research.

AEs yet to see sustained growth improvement



Source: OECD, Elara Securities Research.

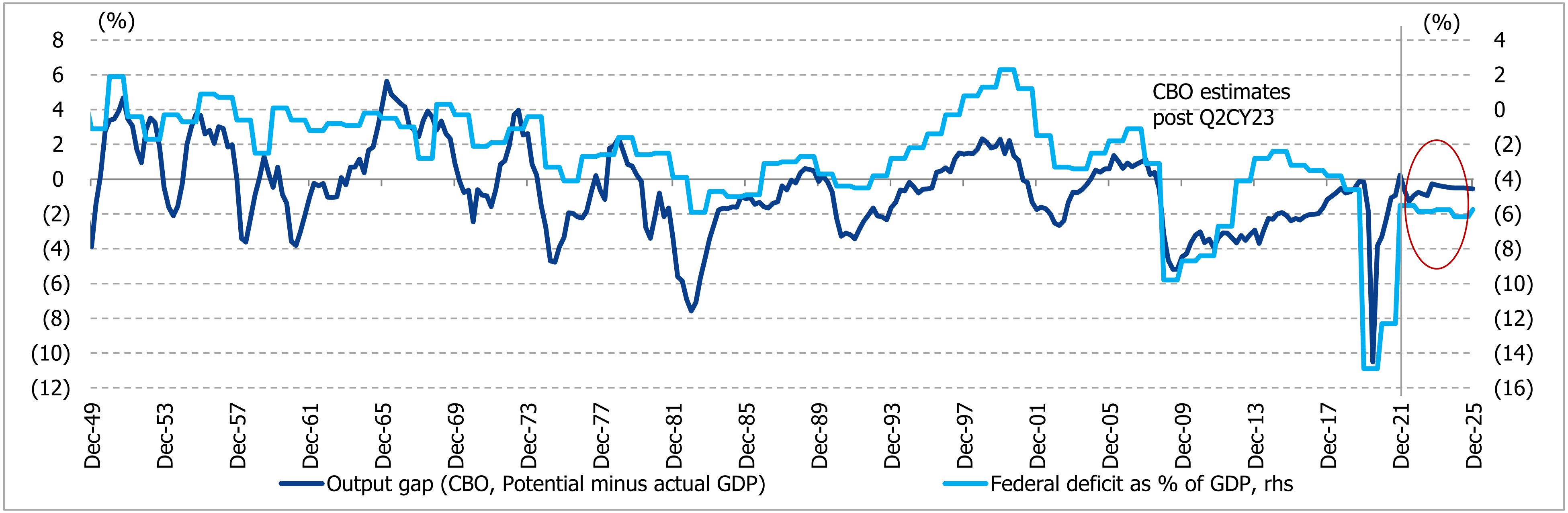
Financial sector and real sector relationship in disrepair…

Widely-followed post 2008 relationship between US 10y and copper/gold ratio fragmented since 2022

Source: CEIC, Elara Securities Research

#2: ...amid fiscal stress in the US

Elevated US fiscal deficit can stress bond markets

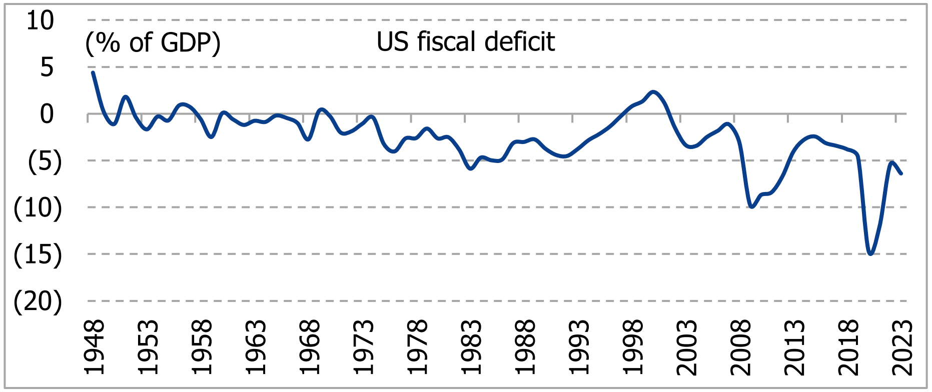


Source: CEIC, Elara Securities Research

- The fiscal situation in the US is set to worsen materially through 2030.
- By the early 2030s, the CBO projects that all Federal government revenues may be consumed by entitlement payments and interest on Federal debt.

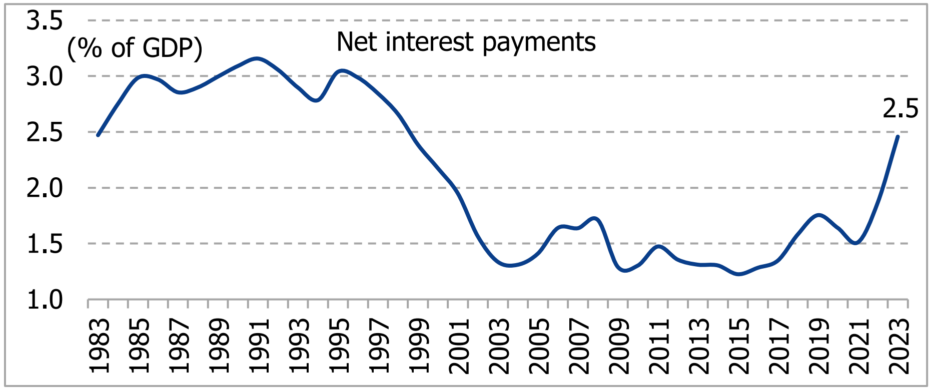
US fiscal health, a key monitorable risk

US fiscal deficit highest outside Covid and GFC (2008)



Source: CEIC, Elara Securities Research

Interest payments highest since 2000-01



Source: CEIC, Elara Securities Research

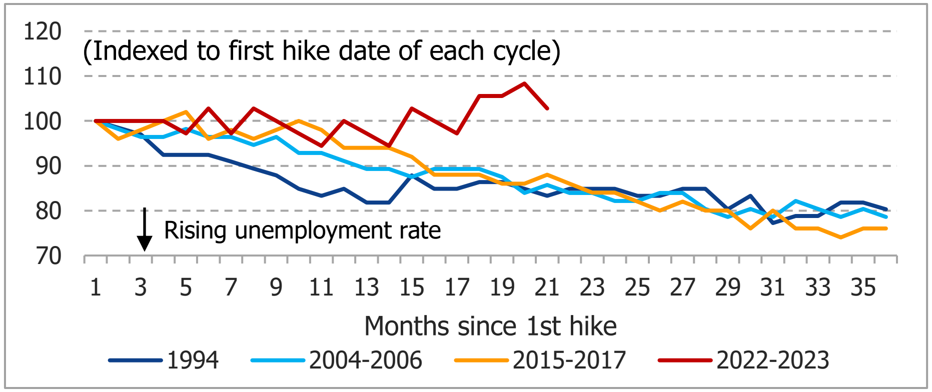
As per CBO projections, US fiscal situation may deteriorate further in next decade

Components	*USD tn*					*% of GDP*				
	2022	2023	2024E	2028E	2033E	2022	2023	2024E	2028E	2033E
Revenues	**4.9**	**4.4**	**4.9**	**5.9**	**7.1**	**19.6**	**16.6**	**17.8**	**18.2**	**18.1**
Income tax	2.6	2.2	2.5	3.1	3.8	10.5	8.1	9.1	9.6	9.7
Corporation tax	0.4	0.4	0.5	0.5	0.5	1.7	1.6	1.8	1.6	1.4
Outlays	**6.3**	**6.1**	**6.4**	**7.9**	**10.0**	**25.1**	**22.9**	**23.5**	**24.1**	**25.3**
Discretionary spends	1.7	-	1.9	2.1	2.4	6.7	-	6.8	6.5	6.0
Mandatory spends	4.1	-	3.8	4.7	6.1	16.5	-	14.0	14.6	15.6
Net interest	0.5	0.7	0.7	1.0	1.4	1.9	2.5	2.7	3.1	3.7
Surplus/Deficit (-)	**(1.4)**	**(1.7)**	**(1.6)**	**(1.9)**	**(2.9)**	**(5.5)**	**(6.3)**	**(5.8)**	**(5.9)**	**(7.3)**

Source: CBO Estimates, CEIC, Elara Securities Research

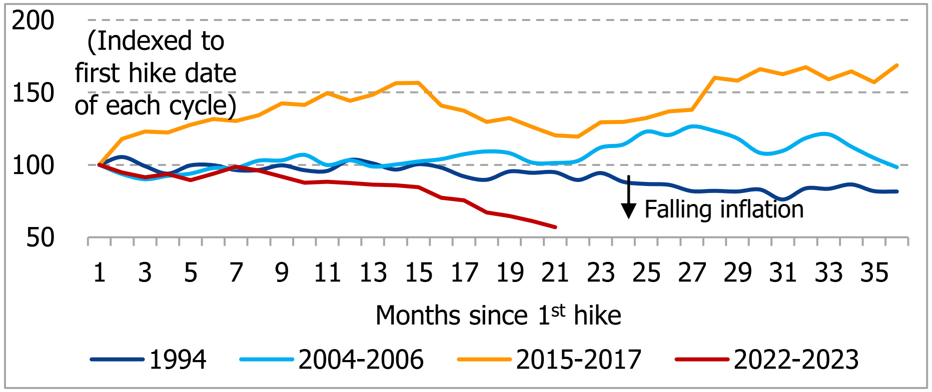
#3: The US – Probability of soft-landing rising in 2024

Unemployment rate lower than prior hike cycles



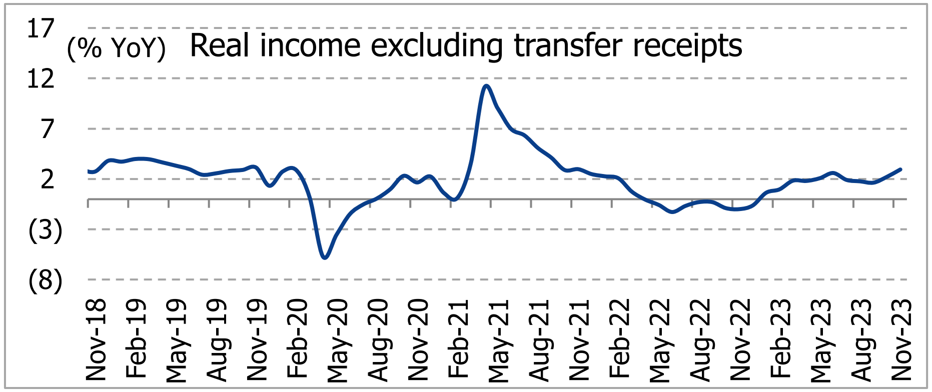
Source: CEIC, Elara Securities Research

Record high inflation* tamed at best pace



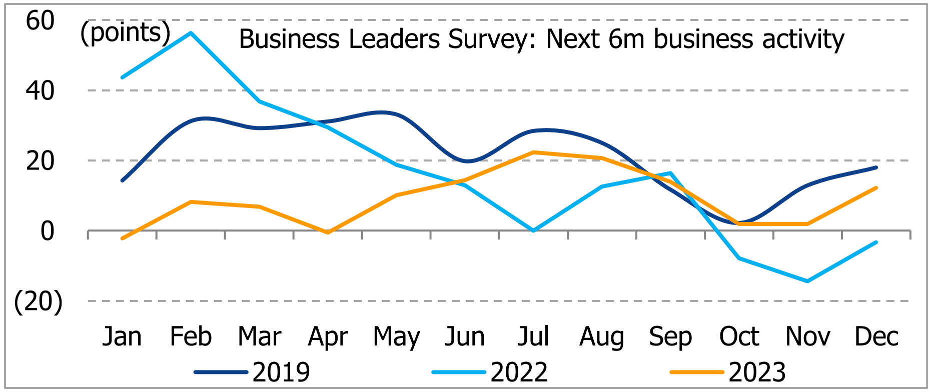
Note: *Core PCE % YoY; Source: CEIC, Elara Securities Research

Real income has started to rise as inflation cools off



Source: CEIC, Elara Securities Research

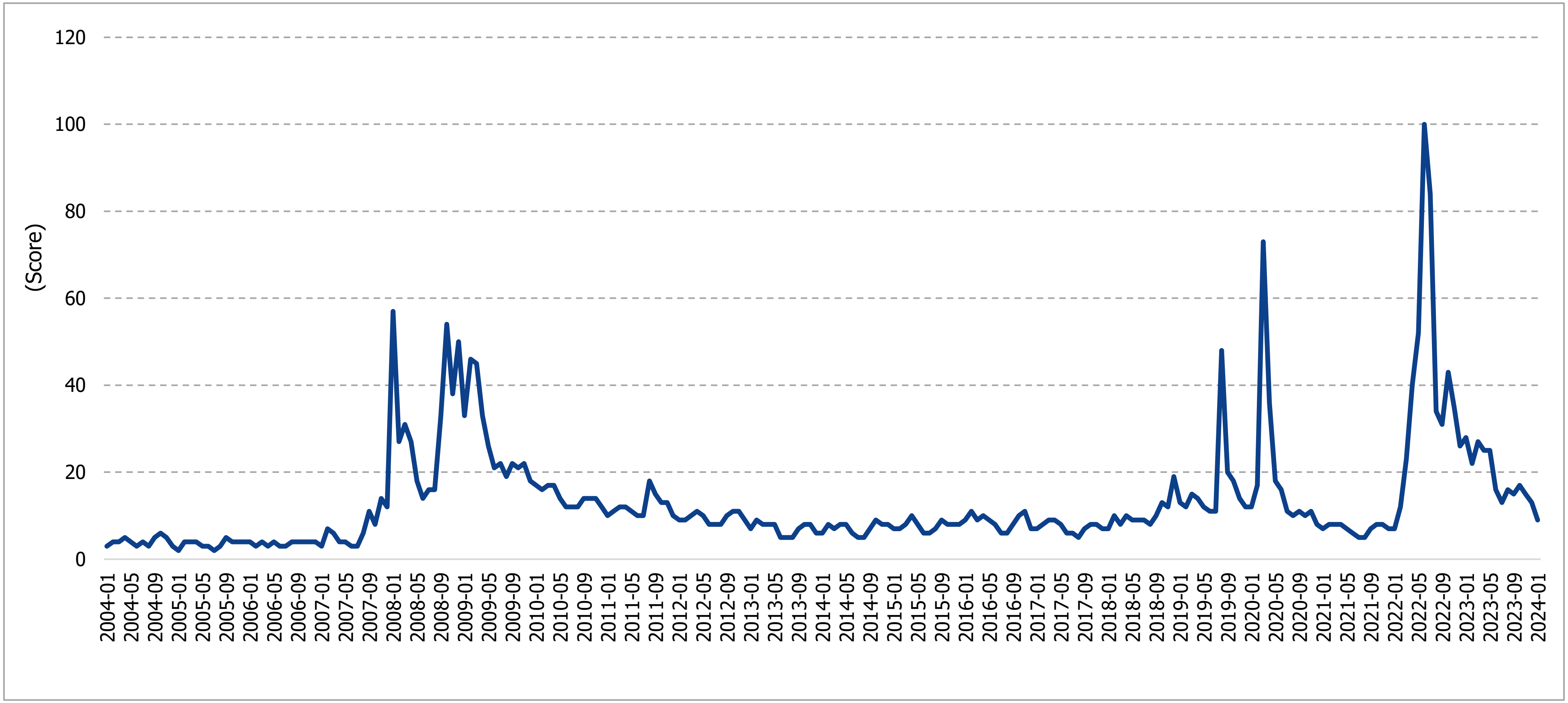
Business activity may improve in 2024



Source: CEIC, Elara Securities Research

Searches for recession have fallen sharply in the US

Searches for recession have come down drastically in the US

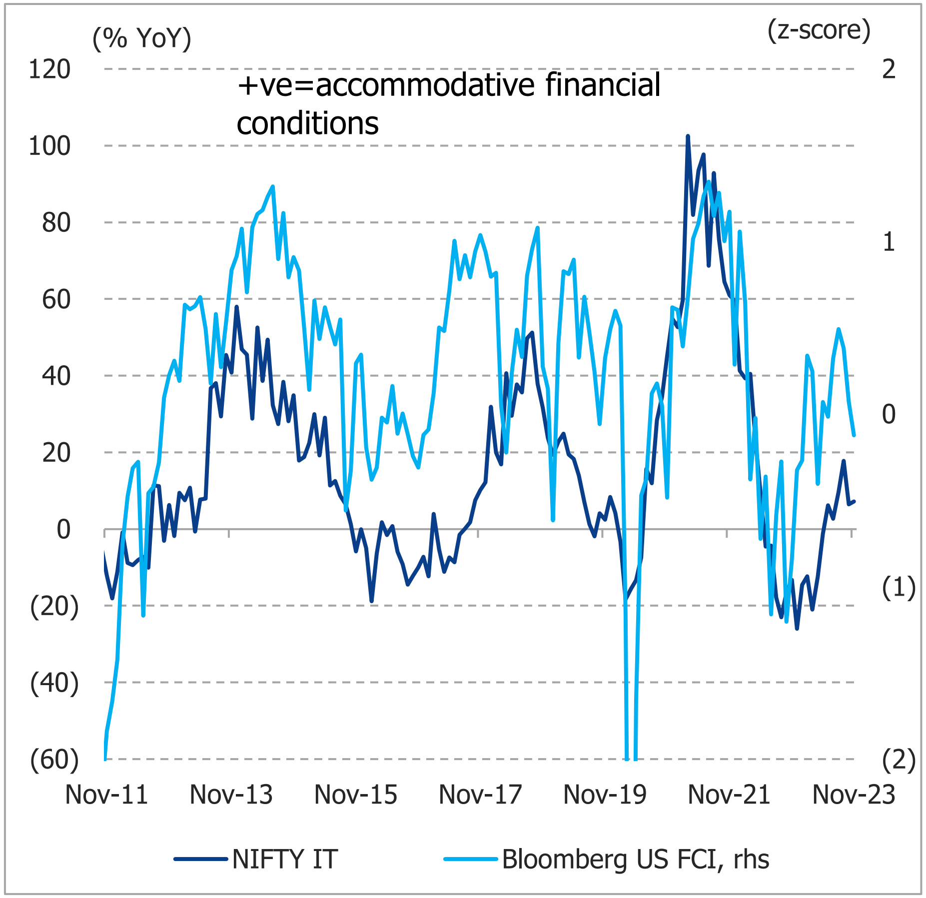


Note: Numbers represent search interest relative to the highest point on the chart for the given region and time. A value of 100 is the peak popularity for the term. A value of 50 means that the term is half as popular. A score of 0 means there was not enough data for this term. Source: Google Trends, Elara Securities Research

#4: So, a lucrative time to enter NIFTY IT

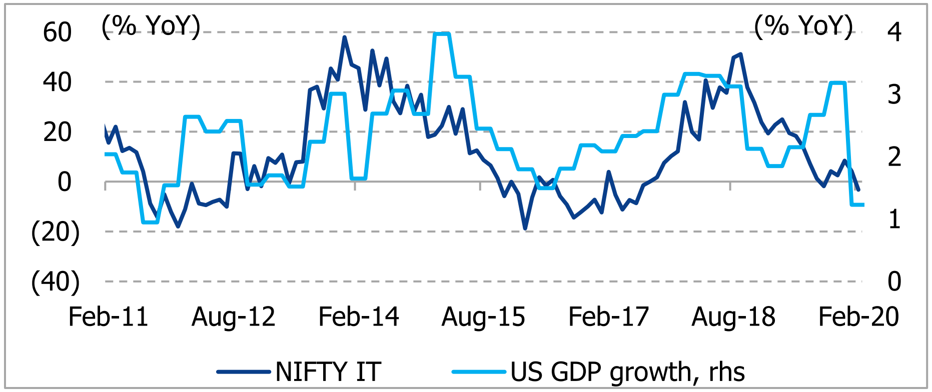
Resilient US growth + potentially easing US financial conditions bode well for Indian IT

Potentially accommodative US financial condition good for IT



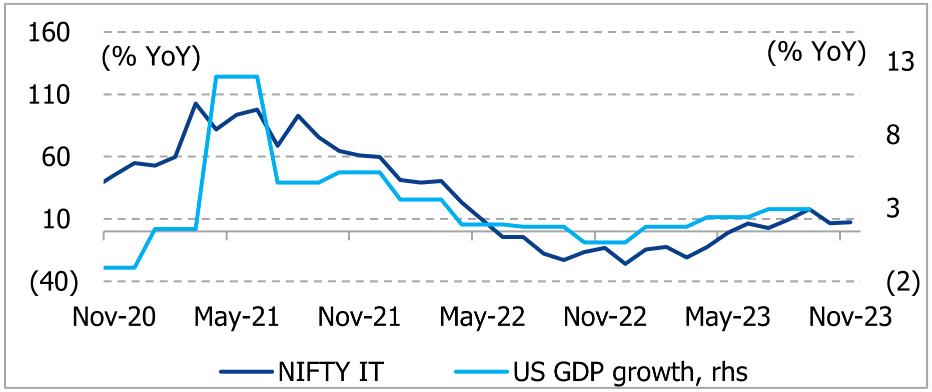
Source: Bloomberg, CEIC, Elara Securities Research

NIFTY IT closely follows US growth….



Source: CEIC, Elara Securities Research.

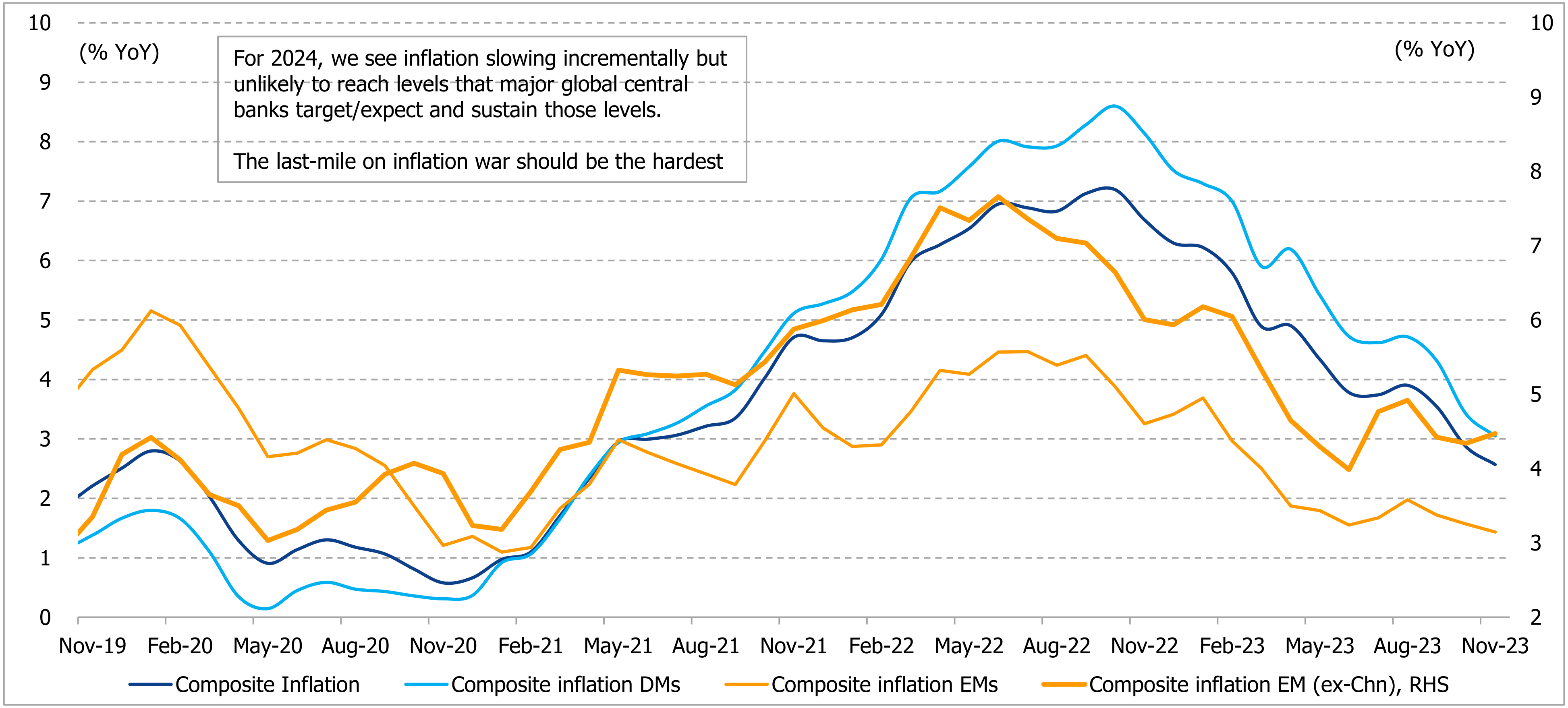
….which continues post Covid too…



Source: CEIC, Elara Securities Research

#5: Disinflationary trend continues globally

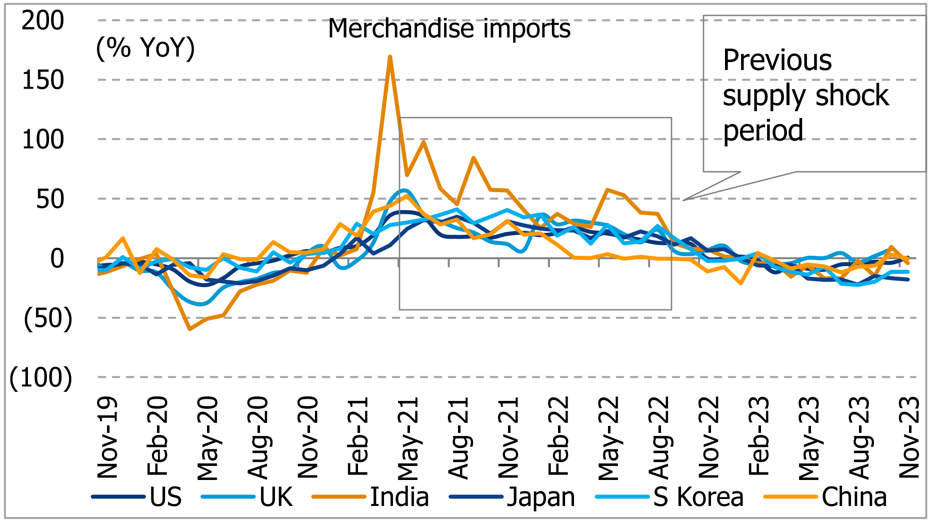
Global headline inflation – Durable signs of downtrend



Note: Composite inflation is the weighted average of countries based on 2019 GDP nominal GDP share for Canada, the US, the EU, the UK, Germany, France, Italy, Japan, China, Indonesia, India, South Korea, South Africa, Brazil and Mexico; Source: BIS, Elara Securities Research

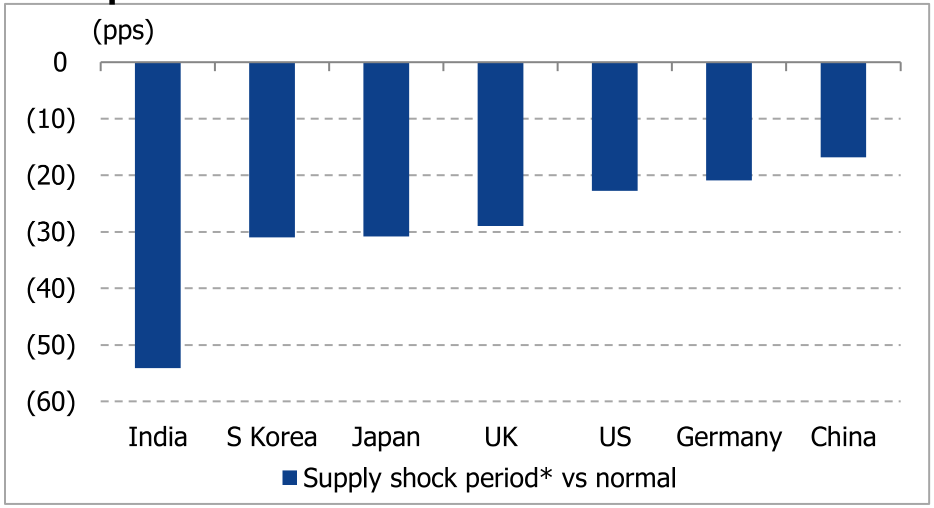
Supply shocks have limited impact as goods demand remain weak

Goods demand slowed down materially in 2023



Source: CEIC, Elara Securities Research

Goods import growth differential – normal versus supply shock period

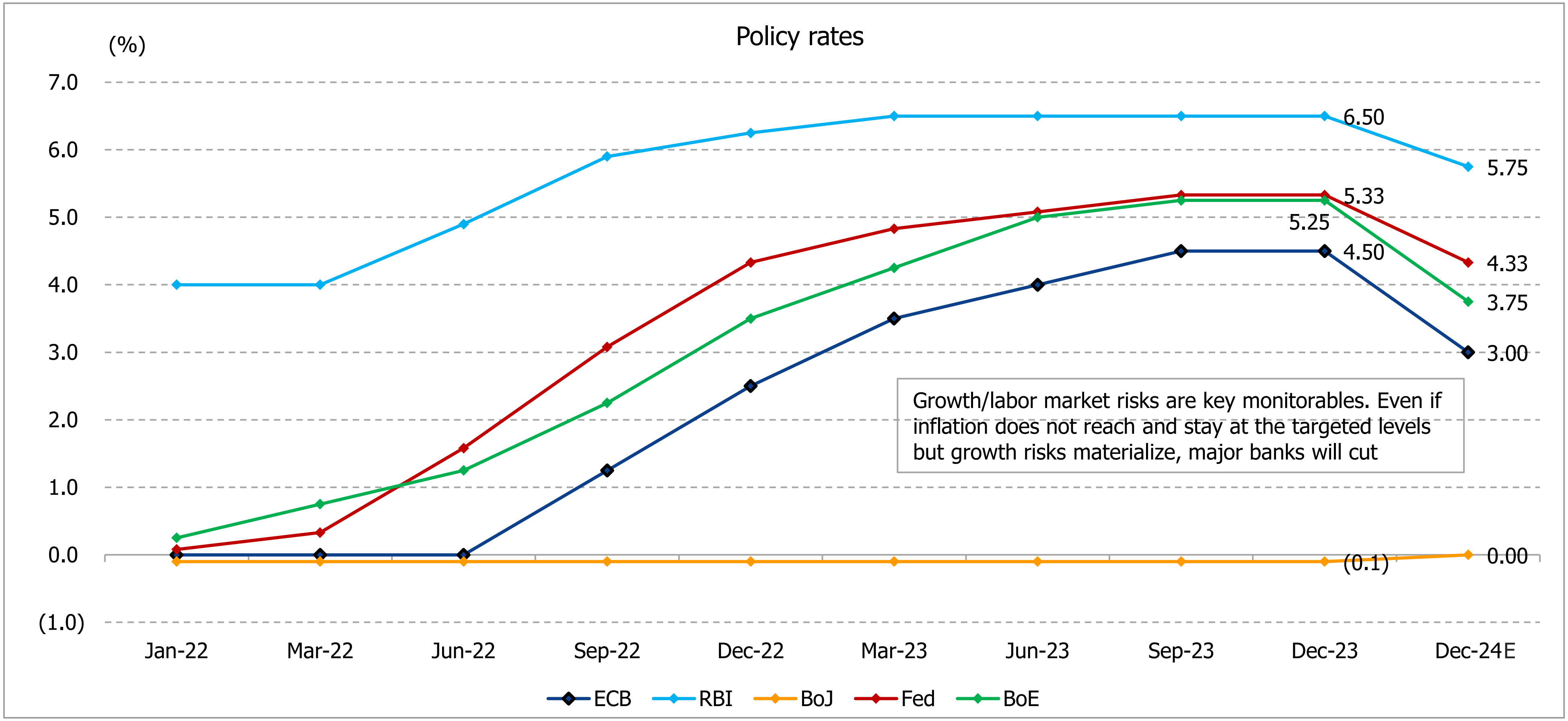


Note: *May-21 to Aug-22; Source: CEIC, Elara Securities Research

- Recent supply shocks owing to geopolitical tensions and climate risks (Red Sea and Panama Canal) has emerged as the key risks to global supply chain in 2024.
- In our view, these shocks are transitory and have minimal upside impact on inflation as goods demand remain benign and bigger transport companies are aligning their supply chains accordingly.
- We do not see alteration in the course of global monetary policies due to these shocks.

Major central banks will cut rates in 2024

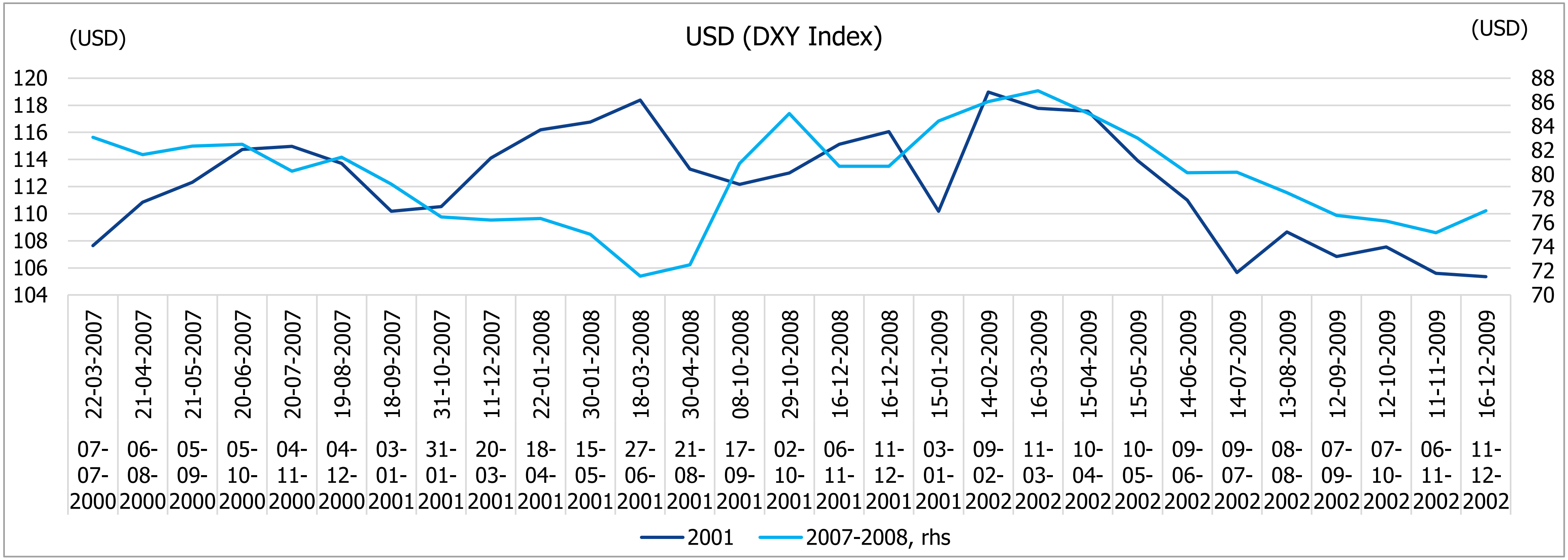
Moderation in inflationary pressures with growth risks likely to lead central banks to cut rates in 2024



Note: Dec-24 are estimates; Source: CEIC, Elara Securities Estimates

US Dollar – limited downside with weaker Euro playing spoilsport

DXY performance pre/post rate cut cycles in the past (towards 100/100+ = strengthening)

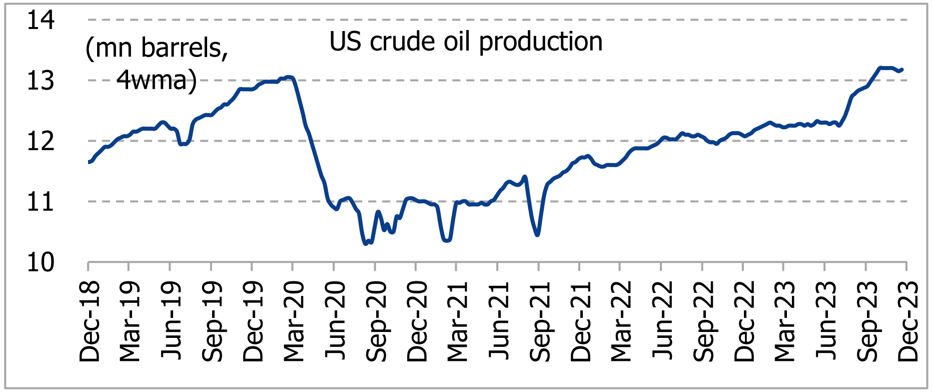


Note: Rate cut cycles: Jan-Dec 2001 and Sep-07 to Dec-08; Source: Bloomberg, Elara Securities Research

- Analyzing past prominent rate cut cycles of 2001 and 2007-08 shows that the USD declined by 9.2% and ~5% in 2001 and 2007-08 respectively, one year post the rate cut cycle stopped. Interestingly, through the cycle, dollar appreciated due to risk off.
- In 2024, the likelihood of sharp USD depreciation remains low as the Euro may see sharper weakness versus the USD. Fed-BoJ rate differential and expectation of Fed cuts weigh in from Q1CY24 on the downside.
- We see DXY averaging 101 in CY24 versus 103.43 in CY23.

#6: Crude oil – OPEC math has some ruptures; will impart downside…

US producing oil at record pace



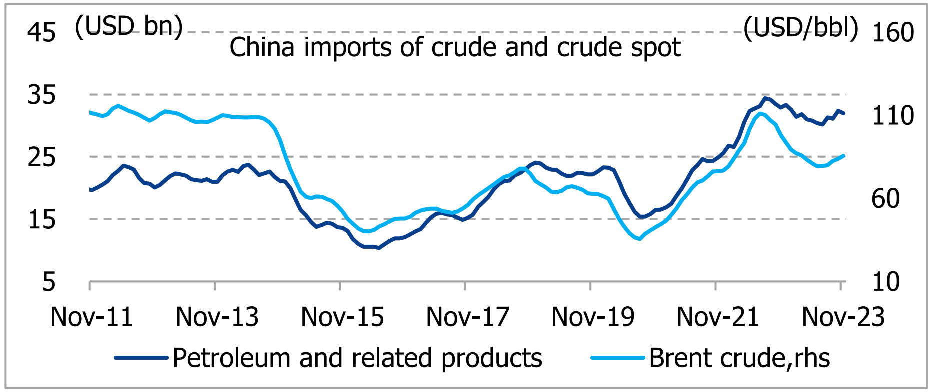
Note: Data till 15 December 2023; Source: CEIC, Elara Securities Research

Geopolitical risk premium does not exist anymore

Shock (SD) to crude when GPR>100	Geopolitical Risk Index (avg.)	Brent crude (USD/bbl, avg.)
1-1.5	136.9	91.3
1.5-2	169.0	106.7
> 2	130.1	117.9
Sep-23 till date	150.9	85.7

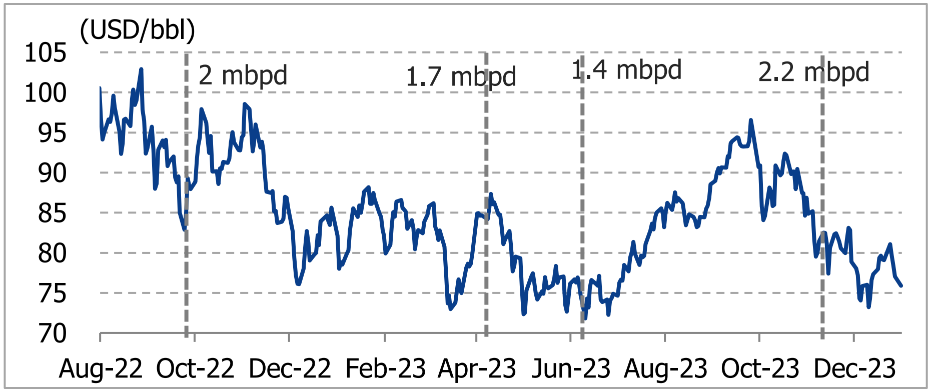
Source: Policyuncertainty.com, Bloomberg, Elara Securities Research.

Benign demand is keeping crude prices in check



Source: CEIC, Elara Securities Research

Recent output cuts have failed to support prices



Source: OPEC, Elara Securities Research

…as OPEC is overestimating global demand conditions

OPEC may have got its projections wrong

First quarter, 2024 oil market forecasts by the IEA, OPEC and EIA (mb/d)				
		IEA	OPEC	EIA
A	Growth in global oil demand	1.2	2.02	2.08
B	Global oil demand	101.5	103.6	101.98
C	Growth in Non-OPEC supply	1.2	0.76	1.54
D	Non-OPEC production	68.2	68.48	68.7
E	OPEC NGLs	5.6	5.49	5.49
F	Call on OPEC crude and change in inventories	27.7	29.63	27.79
G	October OPEC crude production	28.21	27.9	27.77
H	Difference between F and G	-0.51	1.73	0.02

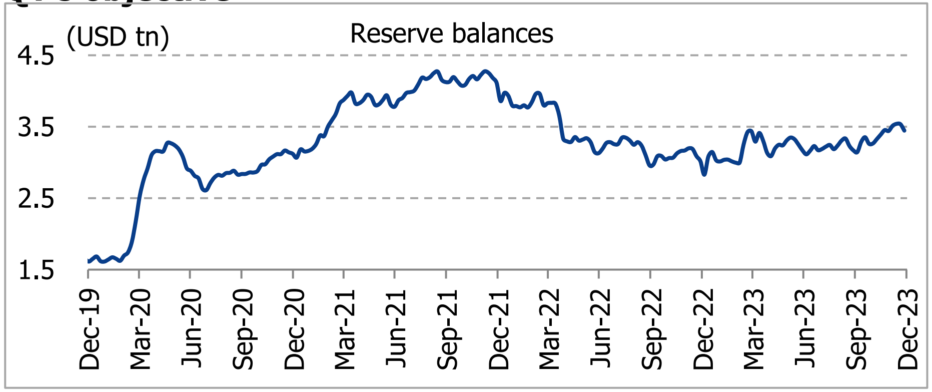
Source: EOA, 2023. IEA, OPEC and EIA, 2023, Energy Outlook Advisors

- Row H shows how much OPEC production and inventories have to change relative to October data.
- Per IEA, to keep global oil inventories flat at October levels, OPEC has to cut production by 510, 000b/d.
- However, OPEC's estimate of call on OPEC crude may be higher due to its optimistic demand projection
- We think OPEC may be clearly over-estimating demand conditions

#7: Expect Fed to resume QE by mid-CY24

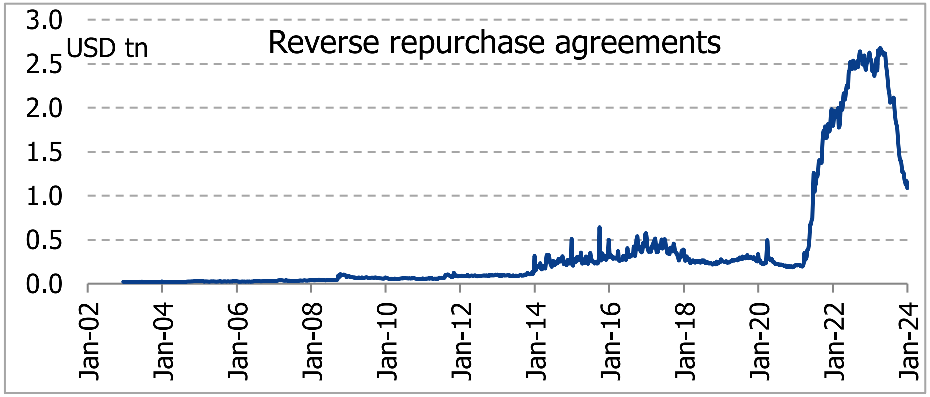
- In its latest meet (12-13 Dec 2023), FOMC members deliberated on tapering QT if the need arises as per minutes.
- Assuming 2023 weekly average drawdown rate persists in 2024 + used for buy up T-bills, we estimate Reverse Repurchase Agreements (RRPs) to exhaust by Q1CY24. With Bank Term Funding Programme (BTFP) ending in Mar-24, we foresee possibility of liquidity incrementally drying up in the system along with slowing real sector.
- Hence, we expect the Fed to start QE in mid-2024 to traction the liquidity in the system.
- Fed's assets, as of 3 January 2024, stood at USD 7.68tn. We expect the Fed to start tapering QT starting Apr-23 and start reinvesting USD 30bn (25bn UST + 5bn MBS) per month from Jul/Aug-23, injecting USD 150bn in H2CY24E. We see Fed's assets at USD 7.03tn as at end-2024E versus USD 4.15tn in end Feb-20.

Reserves continued to rise steadily in 2023 negating QT's objective



Source: FRED, Elara Securities Research

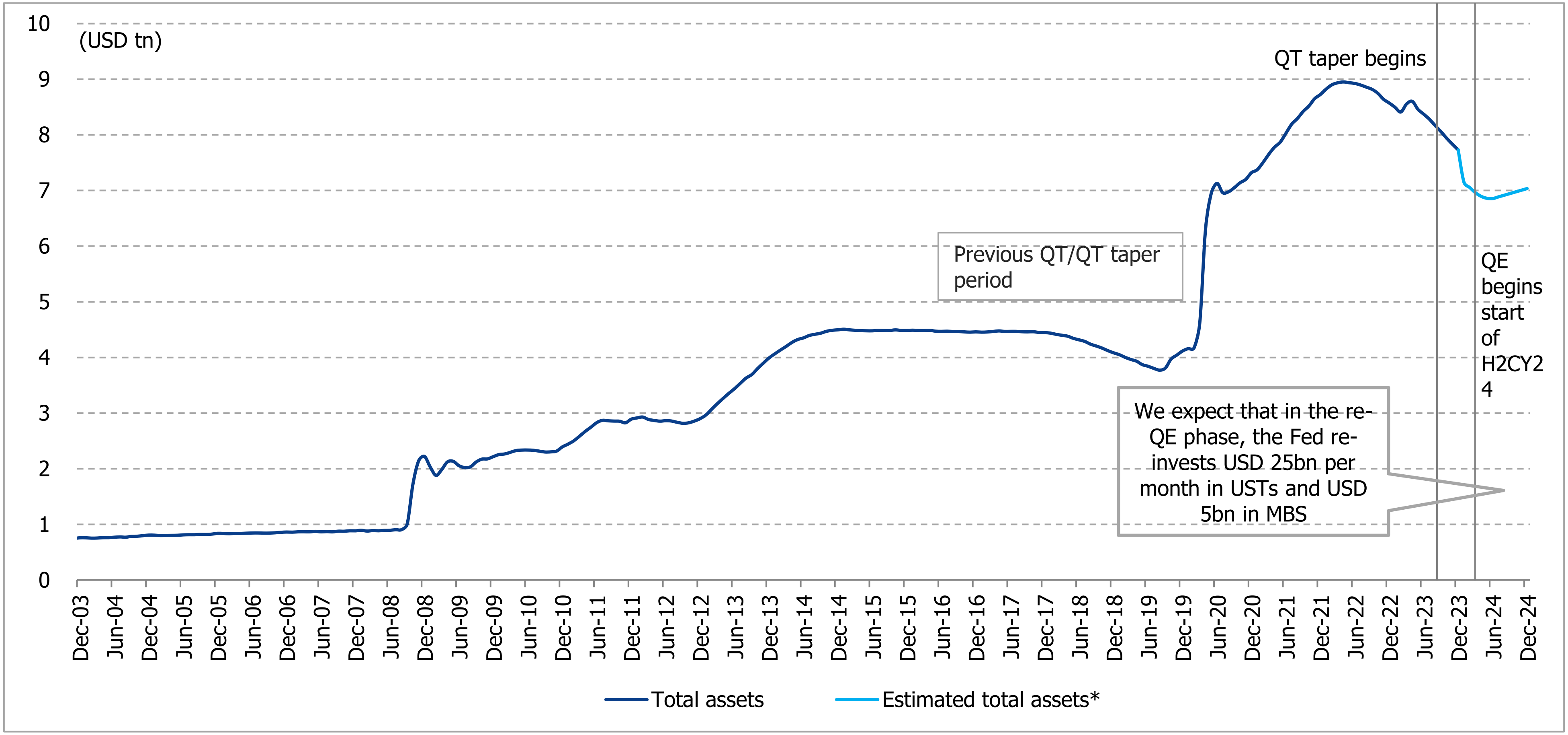
Excess money evaporating at a faster pace



Note: Data till 3 Jan 2024; Source: FRED, Elara Securities Research

Fed's balance sheet unlikely to fall back to pre-Feb 2020 levels

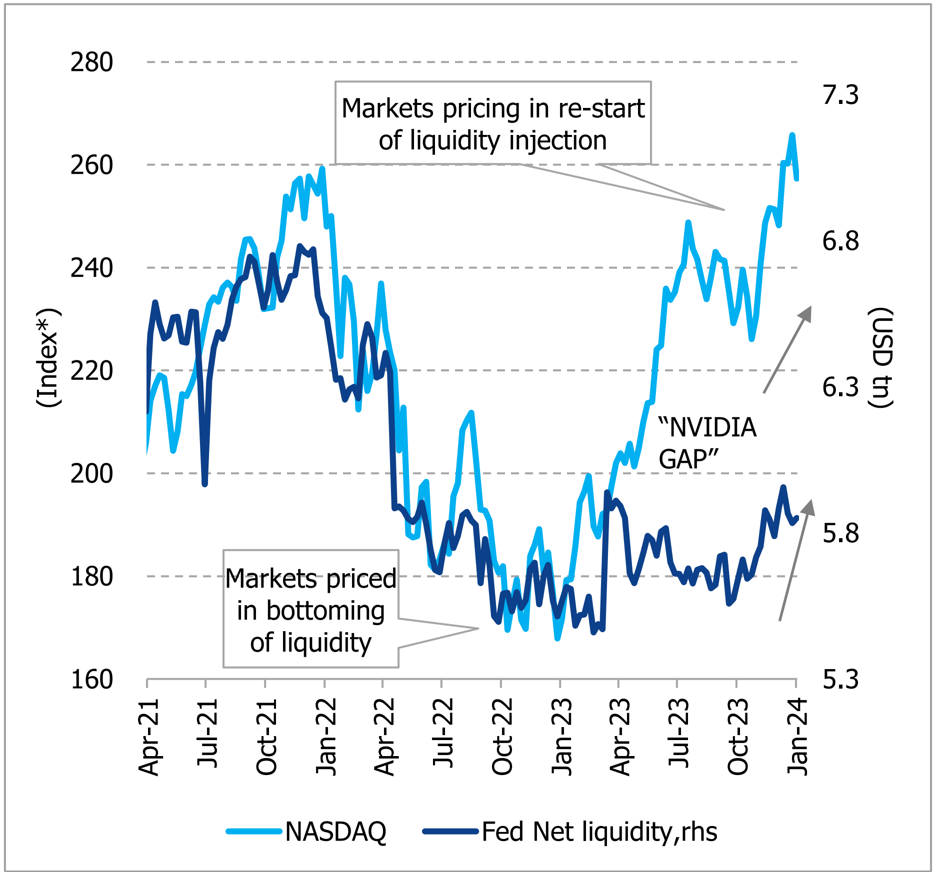
If Fed restarts QE from mid-2024, Fed's assets as of end-CY24E may touch USD 7.03tn, adding USD 150bn in system



Note: *Estimates assume the Fed reinvests on average USD 30bn per month as QE throughout H2CY24E; Source: FRED, Elara Securities Estimate

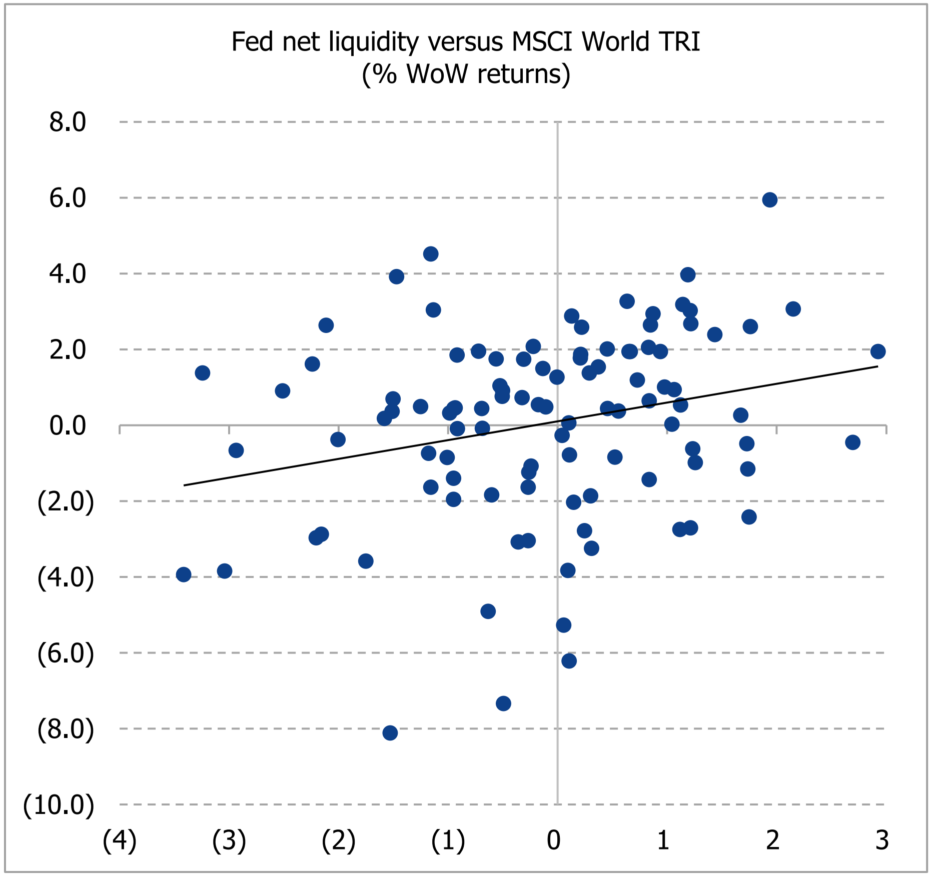
Return of QE to traction equities and risk assets

Nasdaq in step with Fed's liquidity except NVIDIA gap; directional co-movement starts again post Oct-23



Note: *2-Jan-2019=100 ; Source: Bloomberg, CEIC, Elara Securities Research

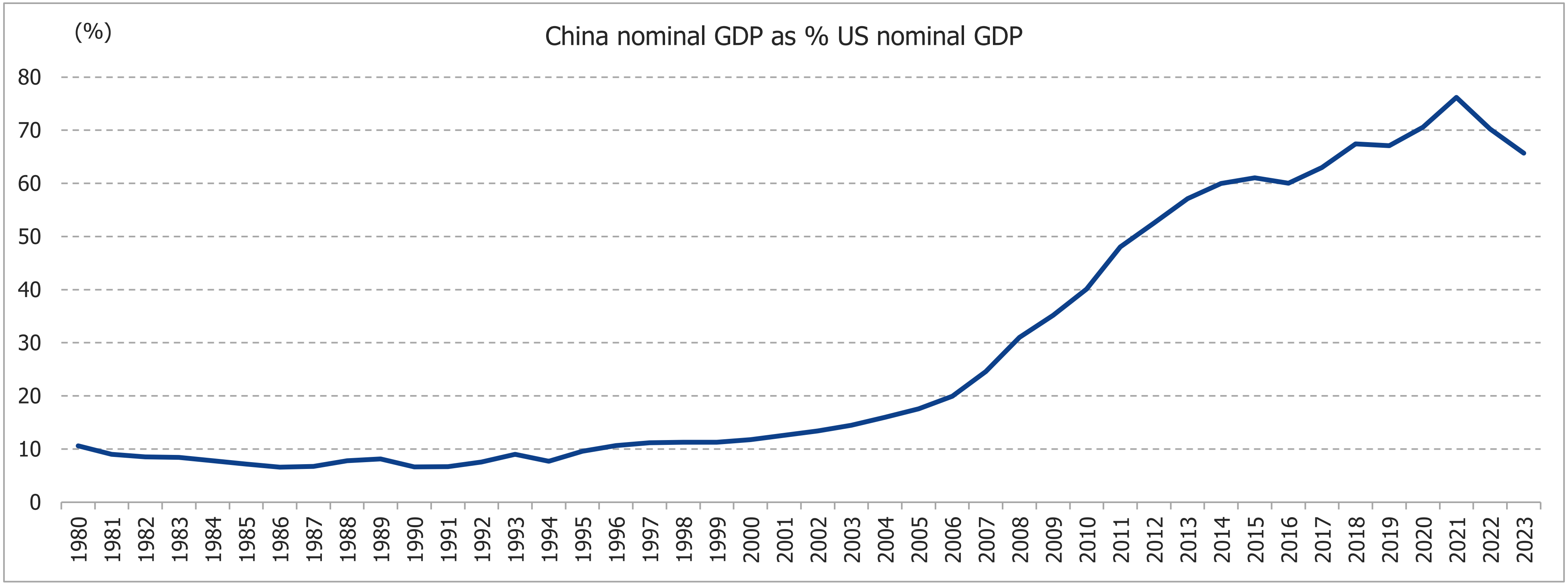
Since 2022, weekly returns/changes in Fed's balance sheet versus global equities have been positive



Note: Negative correlation in 2019-21; Source: Bloomberg, CEIC, Elara Securities Research

#8: China's great catch-up with the US has come to an end...

China's nominal GDP catch-up with US nominal GDP catch-up is reversing

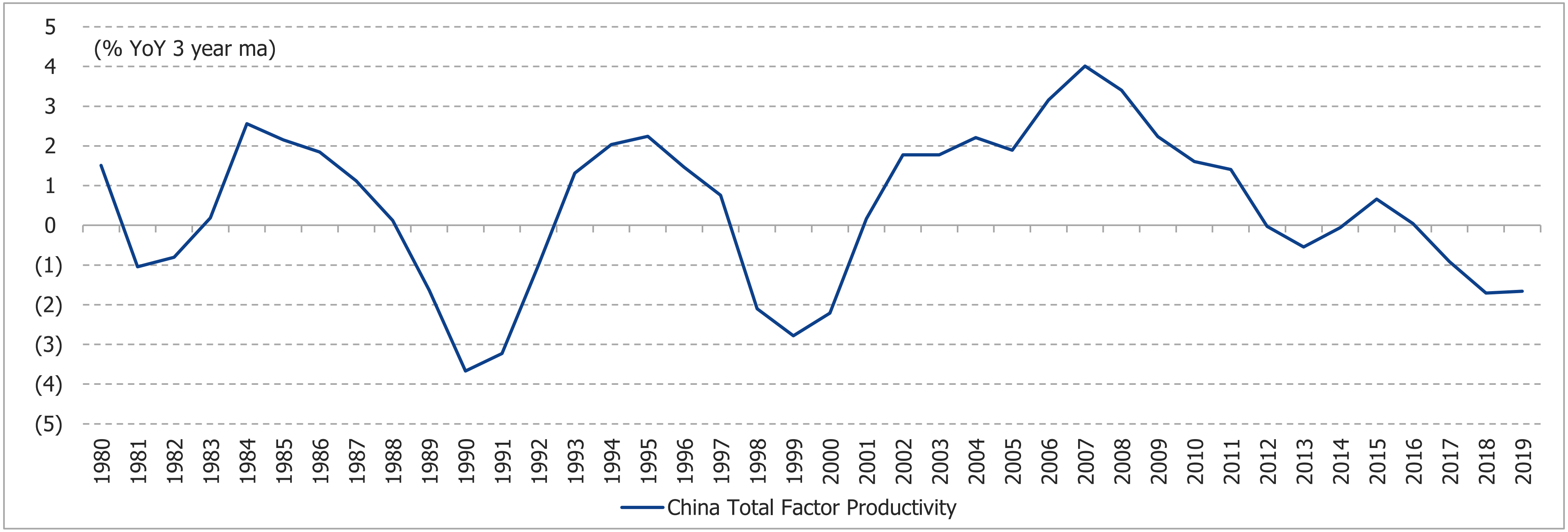


Source: CEIC, Elara Securities Research

- The countries that sustained 2.5% growth after reaching China's current per capita income level of (USD 12,500) had total debt-to-GDP ratio much lower (170% of GDP) versus China's 280% currently.

...as tides turn regarding its productivity and debt checks capital

China's Total Factor Productivity growth has started to moderate

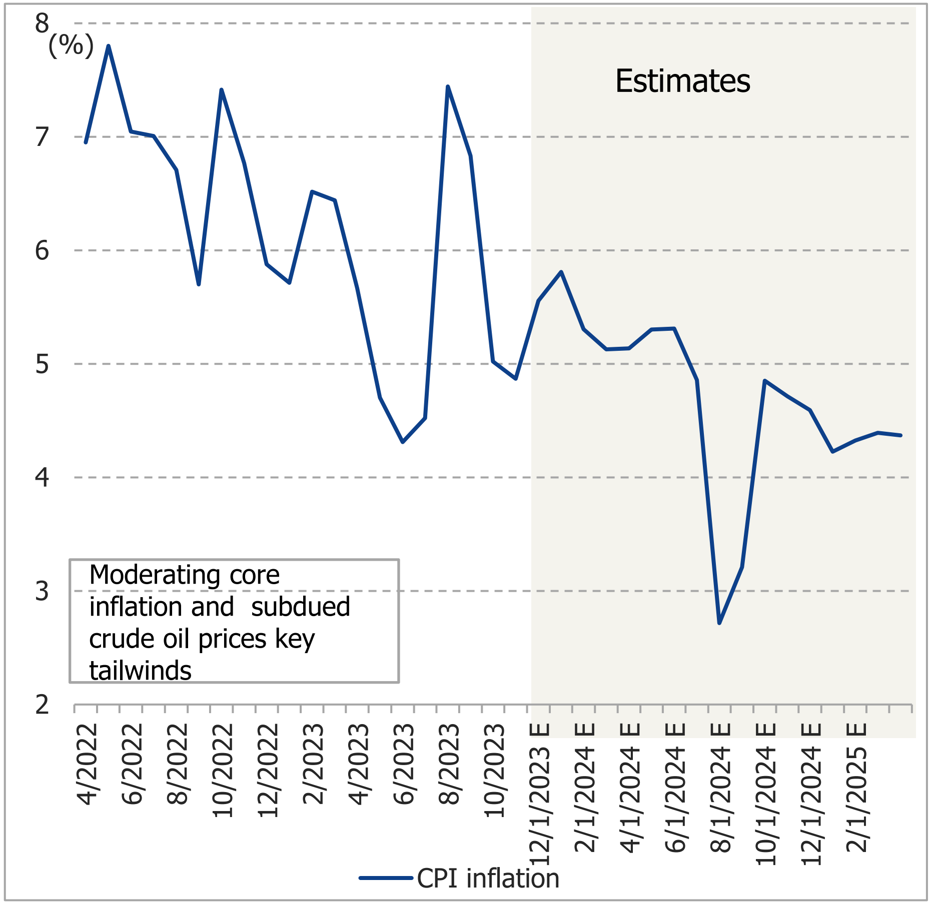


Source: CEIC, Elara Securities Research

- China, with shrinking population and declining productivity growth, has been growing by injecting more capital into the economy at an unsustainable rate.
- This, however, is unsustainable now.

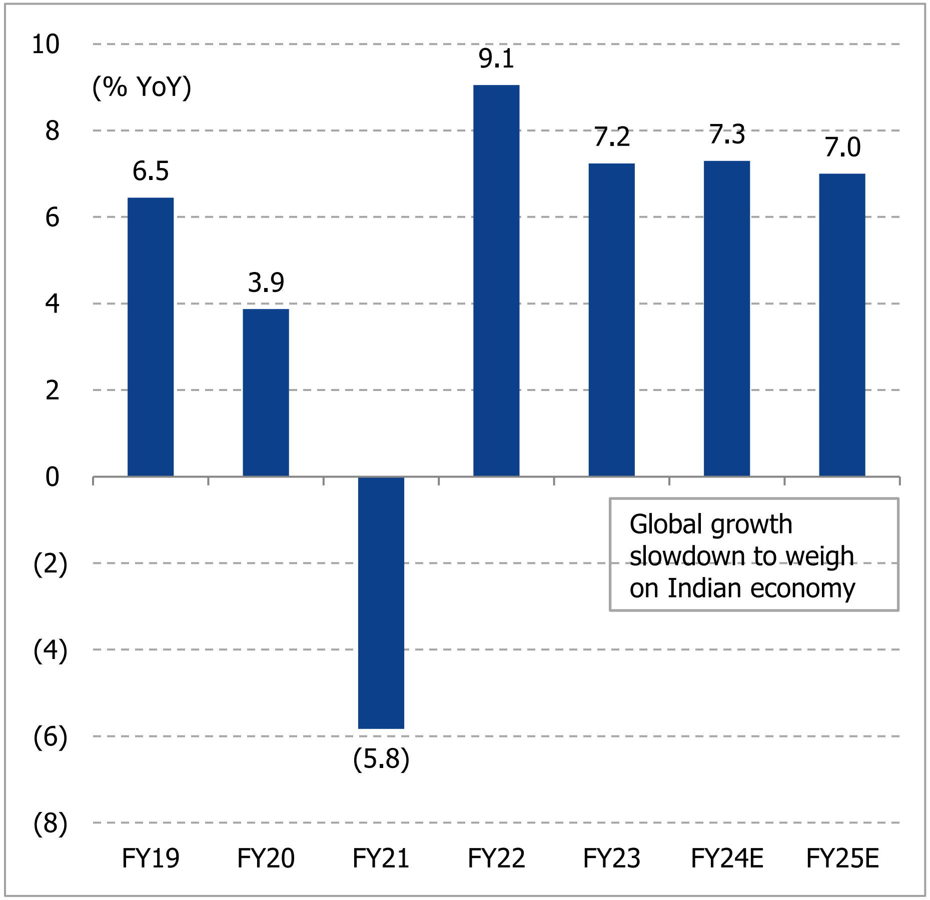
#9: India – FY25E CPI at 4.5%; GDP at 6.9-7%

CPI to be in downtrend in FY25E



Source: CEIC, Elara Securities Estimate

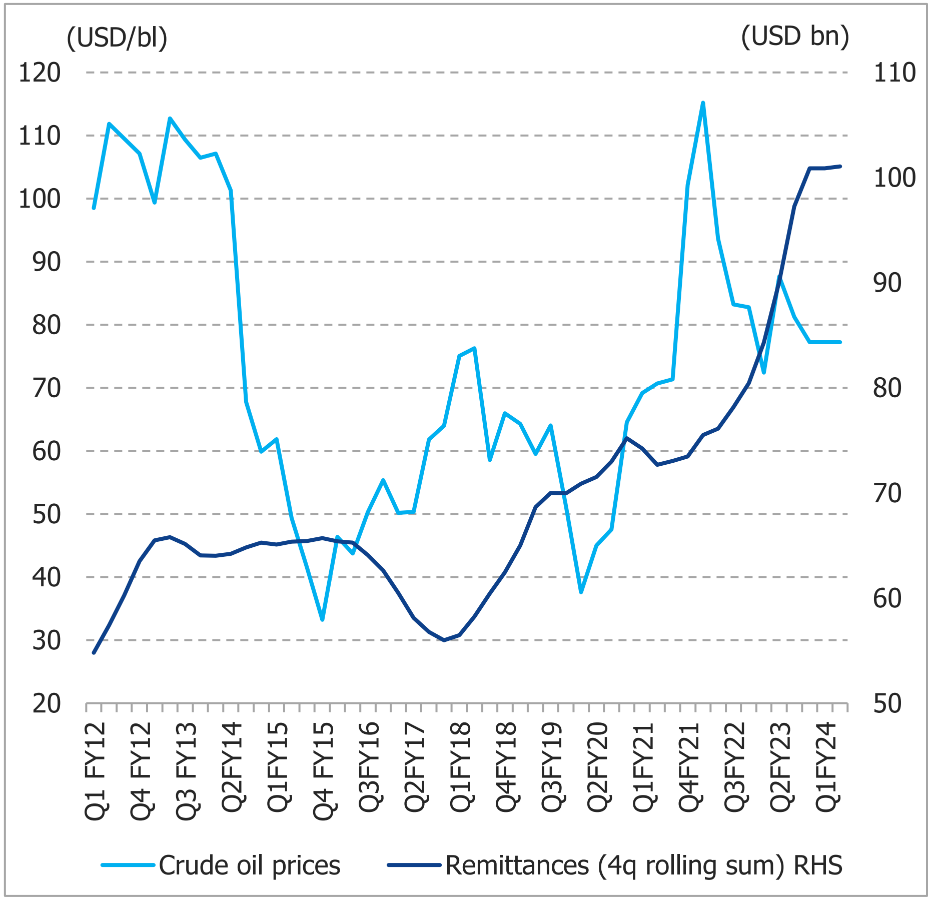
7% real GDP growth is the new normal



Source: CEIC, Elara Securities Estimate

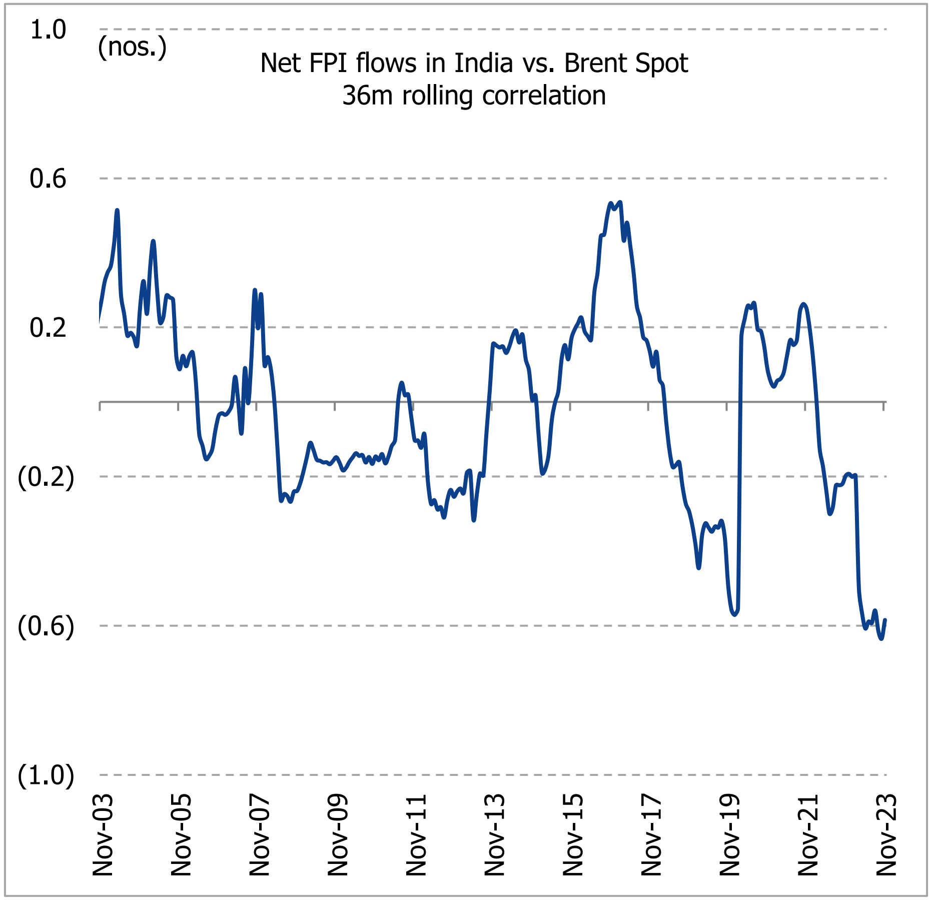
Expect oil price shocks to have far less impact on Indian economy

Remittances slowly getting delinked with oil



Source: CEIC, Elara Securities Research

FPI inflows and crude oil price correlation, record low



Source: CEIC, Elara Securities Research

#10: India may overtake China to have top weight in MSCI EM Index in five years

GDP growth and MSCI weightage

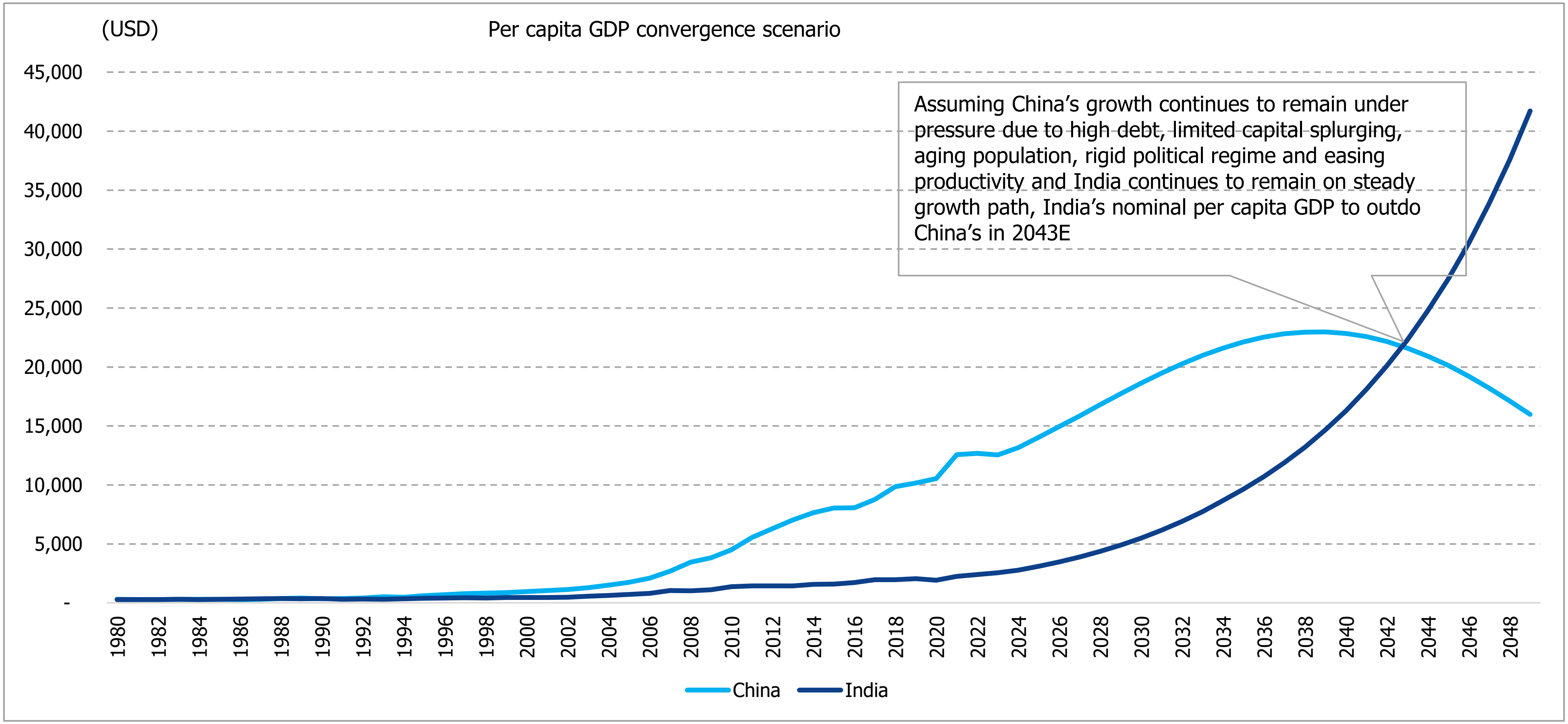
Country	Indicator	2000	2004	2009	2014	2019	2023	2028
China	**Nominal GDP (USD bn)**	**1,206**	**1,949**	**5,089**	**10,524**	**14,341**	**17,701**	**23,609**
	% five-year CAGR	*7.0*	*10.1*	*21.2*	*15.6*	*6.4*	*4.3*	*5.9*
	MSCI weight*	**3.3**	**4.9**	**15.3**	**18.8**	**31.4**	**26.2**	**??**
	bps change	*210*	*160*	*1040*	*350*	*1260*	*(520)*	-
India	**Nominal GDP (USD bn)**	**477**	**722**	**1,365**	**2,039**	**2,832**	**3,732**	**5,944**
	% five-year CAGR	*3.6*	*8.6*	*13.6*	*8.4*	*6.8*	*5.7*	*9.8*
	MSCI Weight*	**7.8**	**7.5**	**8.2**	**11.7**	**9.3**	**17**	**??**
	bps change	*(30)*	*(30)*	*70*	*350*	*(240)*	*770*	**-**

Note: *Weights based on iShares MSCI Emerging Market ETF as of 10th Jan-2024. Nominal GDP in 2023 and 2028 are IMF projections as per WEO Oct-23; Source: IMF, Elara Securities Research

- China's move from a USD 1.2tn economy to a USD 5tn economy in 2009 saw its weight in the MSCI Index rise ~5x from 3.3% in 2000 to 15.3%. Overall, through 2000 to pre-Covid period (CY19), i.e., in the two decades, China's average five-year CAGR growth has been 12%, which pushed up its MSCI Index by 9.5x from 3.3% to 31.4%.
- In the two decades since 2000 to 2019, India's economy size grew 6x, while its weightage in the MSCI increased 150bps. With domestic reforms, macro-financial stability and large consumer market (due to growing population) in India and opposite situation in China, it would be surprising if India does not surpass China in MSCI weightage.

We see India converging to China's per capita GDP by 2043E

India expected to converge to China's nominal per capita GDP in 2047E



Note: For China data till 2028 is from IMF; India till 2022 is actual; Source: IMF, Elara Securities Estimates.

CHAPTER II

US ECONOMY

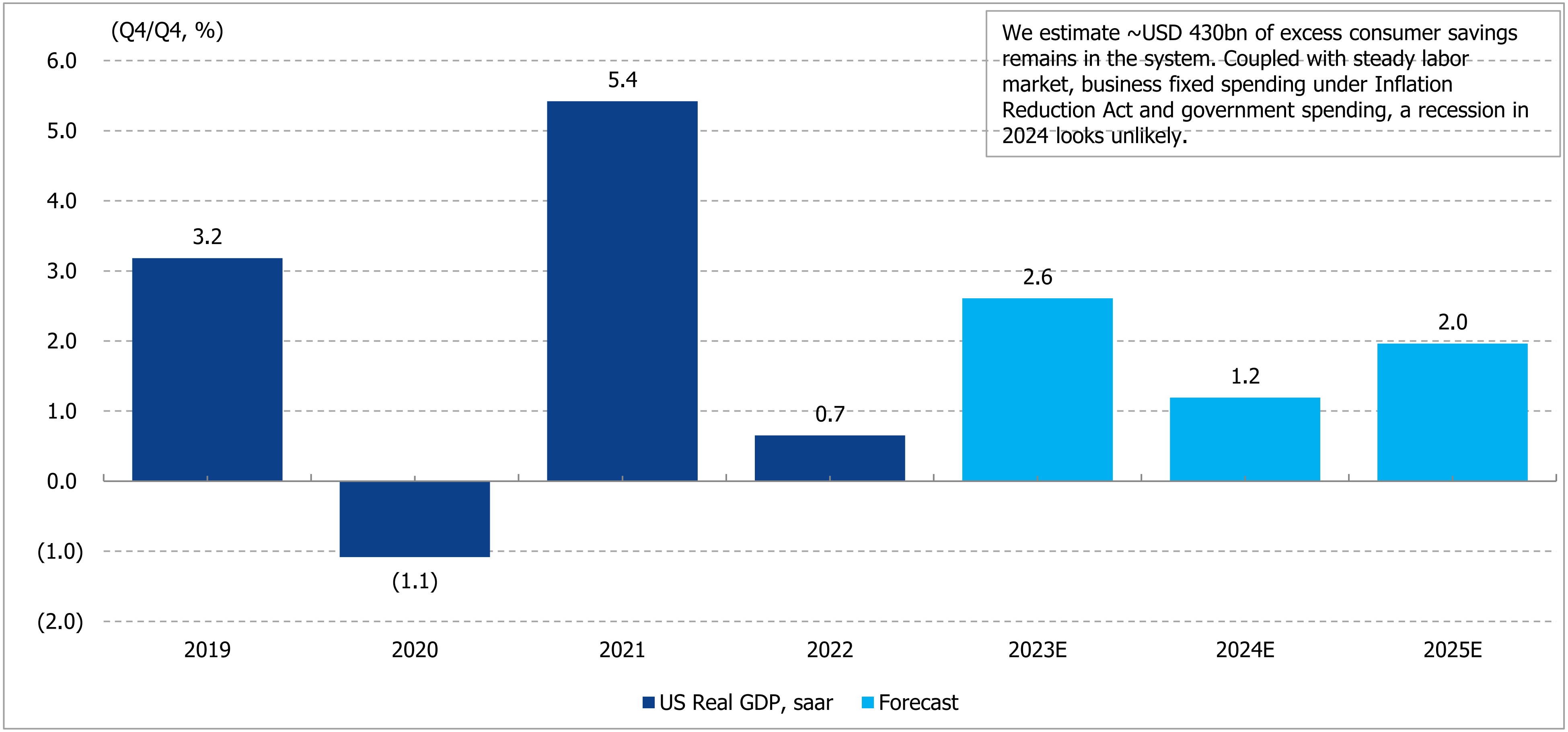
- **Expect the US economy to slow down in 2024, but do not expect a deep recession**
- **First ‘rate cut’ by the Fed seen in Q2CY24**

Soft landing for the US in 2024

- We project the US economy to grow 2.6% in 2023E (Q4/Q4), **1.2% in 2024E (Q4/Q4)** and 2% in 2025E (Q4/Q4) with risks on the downside.
- Expect below-trend US growth in H2CY24 and H1CY25.
- We **project unemployment rate at 5% in 2024E (end-Dec)** with risks on the upside.
- We do not see inflation coming down and sustaining at 2% in 2024E. **For 2024E, expect PCE inflation at 2.4% and core PCE inflation at 2.7%.**
- Fed Funds Rate (upper bound, spot 5.5%): **4.5% for 2024E, 3% for 2025E**. We see first cut in Q2CY24 with overall 100bps cut in 2024E.
- We expect US 10y to remain elevated ~4% in the near term and ease materially only by H2CY24E.
- For full 2024E, we expect USD (DXY Index) to average 101.
- US fiscal health is the key uncertain factor for 2024, which is also an election year. Pull-back on government spending or, such announcements by GOP (the Republican party) can come as a negative shock for the markets and economy.

US growth to moderate, skirt recession in 2024

US growth to moderate in 2024E



Source: CEIC, Elara Securities Estimate

US inflation to settle higher than 2% in 2024E

Inflation projections (%) – 2023E* and 2024E

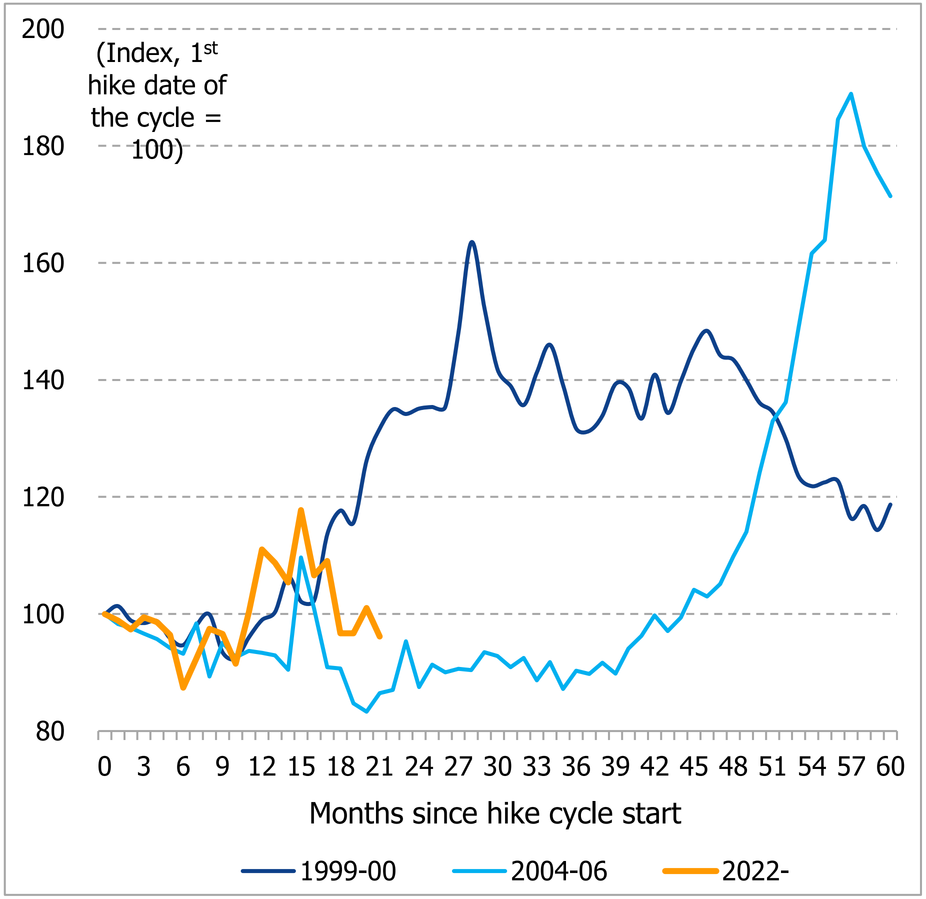
Year	Elara Estimates				Federal Reserve (Dec-23 SEP)	
	CPI	Core CPI	PCE	Core PCE	PCE	Core PCE
2022	7.1	6.0	5.9	5.1	-	-
2023E*	3.2	4.0	2.8	3.6	2.8	3.2
2024E	3.0	3.1	2.6	2.7	2.4	2.4

Note: Projections for both measures of inflation are percent changes from the fourth quarter of the previous year to the fourth quarter of the year indicated; *2023 CPI and Core CPI are actual.
Source: CEIC, Elara Securities Estimate

- Key to inflation moderation, in our view, is softening labor market conditions and consequent easing of private demand, owing to full pass-on of 550bps rate hike.
- Headwinds to inflation in 2024 are from re-emerging and elongated supply chain shocks and slower-than-expected consumer spending. If wage growth doesn't moderate at a faster pace in 2024, reaching 2% on a sustainable basis remains illusive.

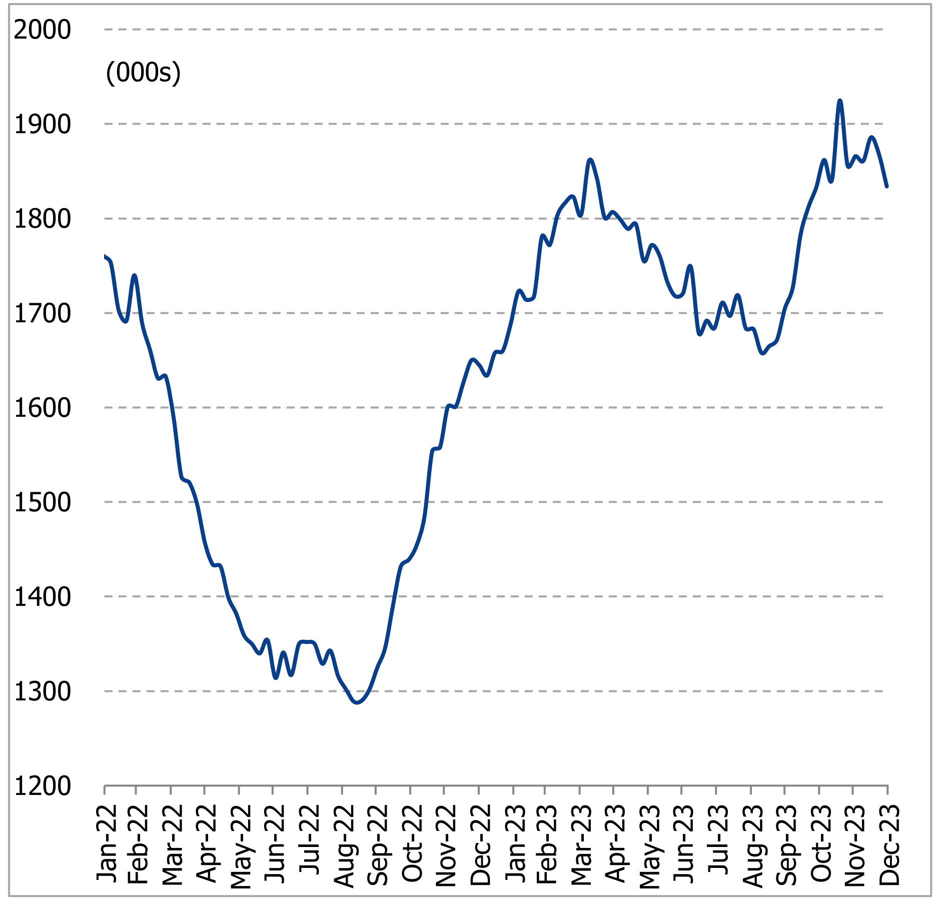
US labor market on course to gradual softening (1/2...)

Effect of rate hikes come with lag in initial jobless claims



Source: CEIC, Elara Securities Research

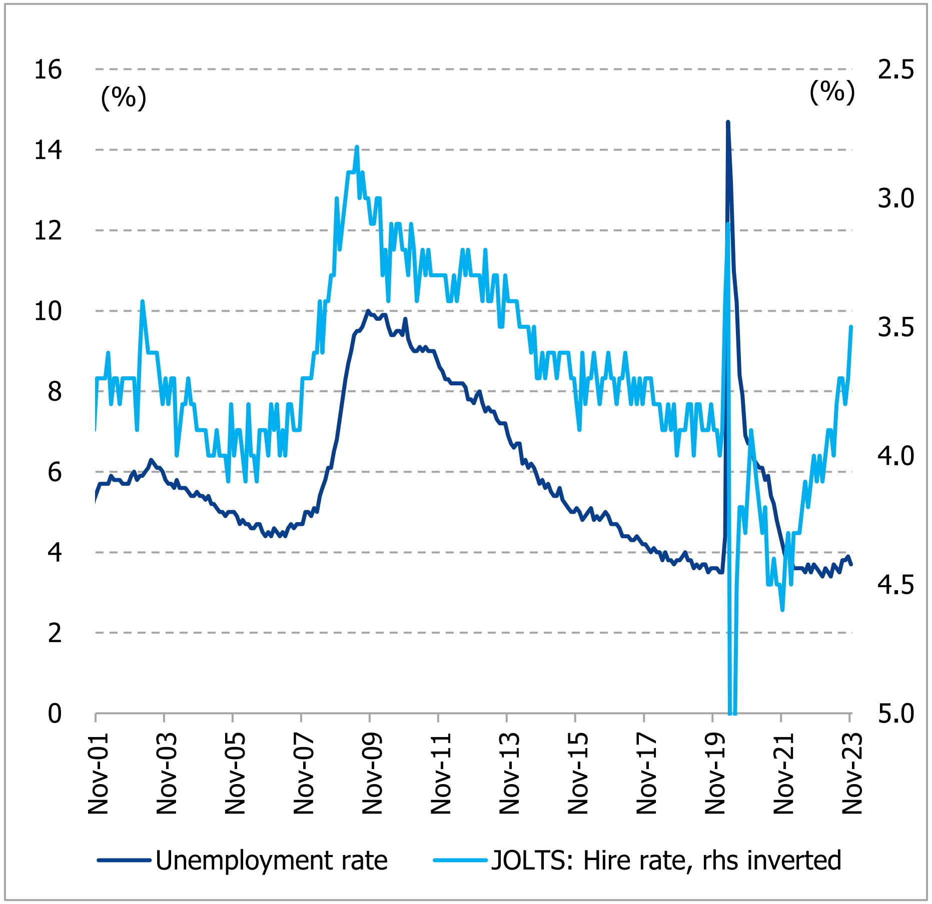
Continuing jobless claims easing but remains on uptrend



Note: Data till 28 October 2023; Source: CEIC, Elara Securities Research

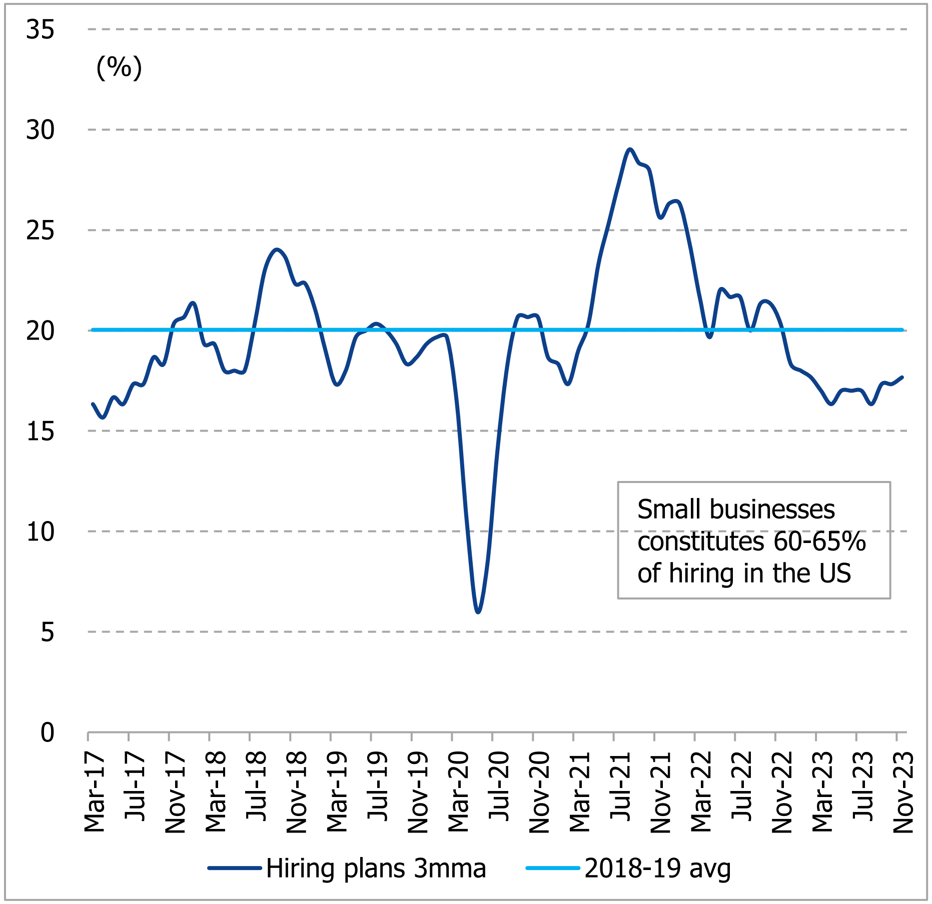
US labor market on course to gradual softening (2/2)

US hiring rate is falling sharply



Source: CEIC, Elara Securities Research

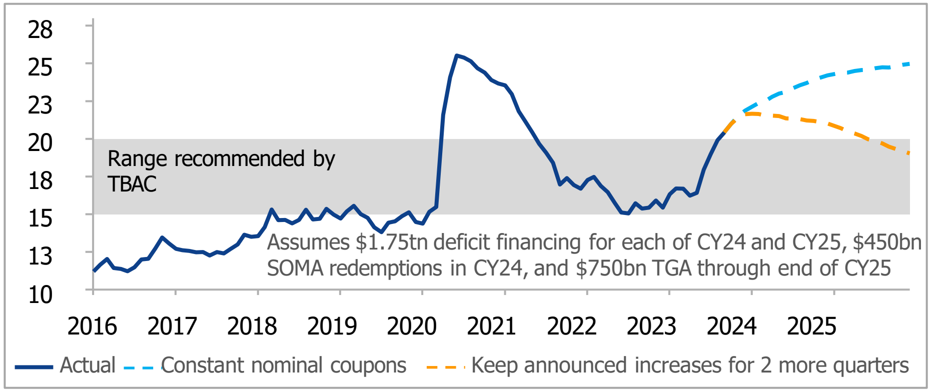
Small businesses: Hiring muted



Source: CEIC, Elara Securities Research

Fiscal stress = Prefer short over long end of the UST curve

T-bill share as percentage of marketable debt



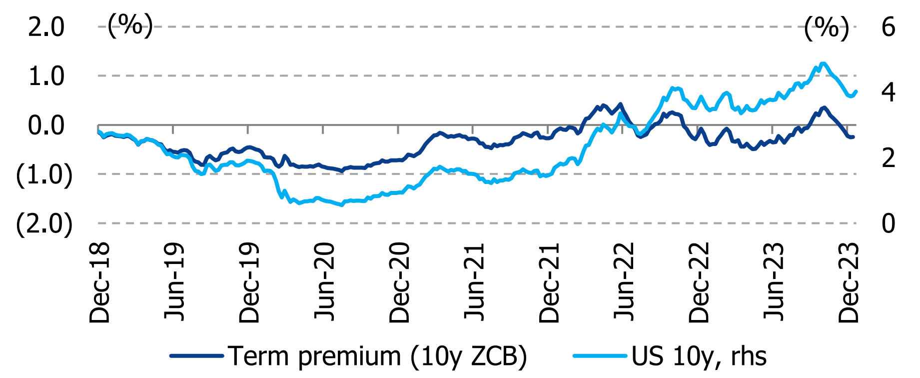
Source: TBAC

T-bill gross issuances (USD bn)

Instrument	2022*	2023*	% YoY
Bills	11,780	17,405	47.75
10y	485	418	(13.72)
20-30y	478	412	(13.73)

Note: *Jan-Nov; Source: SIFMA via US Treasury, Elara Securities Research

Term premia for 10y evaporating



Source: FRED, Elara Securities Research

- Fiscal situation of the US is the key hindrance for US 10y to moderate to 3% in 2024.
- The only factor that can inject some rally in the longer end is moderation in inflation, resulting in start of Fed's cut cycle.
- Hence, near term, prefer shorter end/cash at 5% with real return of 150-200bps than long end amid persistent fiscal uncertainties.

2024 US election year – Asset classes during US elections

Asset class average returns pre/post US elections – Time frame maximum 12m before/after

Years	Period	S&P500	NASDAQ (QQQ)	US10y	MSCI EMFX Index	MSCI EM TRI	MSCI World TRI	Gold	USD-JPY
		%	%	bps	%	%	%	%	%
2008	Pre-election	(32.8)	(36.2)	(20.7)	(11.3)	(49.8)	(36.3)	(12.9)	9.1
	Post election	3.5	16.6	(53.9)	6.2	34.3	7.5	32.7	4.9
2016	Pre-election	1.6	4.7	(1.3)	2.2	7.8	1.3	4.2	4.8
	Post election	13.5	19.0	52.2	2.6	13.8	14.5	(2.2)	(7.4)

Source: Bloomberg, Elara Securities Research

- We selected 2016 and 2008 elections for our analysis given that the possibility of GOP returning to power has emerged and below-trend US growth brings up the 2008 scenario.
- Post 2016, over 3m, 6m and 12m period, risk assets outperformed safe havens on an average, with NASDAQ returning ~20%.
- Post 2008 elections, when GFC 2008 was ongoing, safe assets outperformed. Interestingly, NASDAQ and EM outperformed S&P500 by miles during that time.
- In the upcoming elections in 2024, elevated inflation and tightening financial conditions are key issues – given the recent downtrend in inflation, it is increasing likely that the Fed cuts the rates.
- Talks of rate cut and eventually the cut itself have the potential to lower mortgage rates (30y FRM), thus directly providing a filip to consumer sentiments and in turn, risk assets.

CHAPTER III

INDIA – ECONOMIC OUTLOOK

India – Ready for a steady take-off

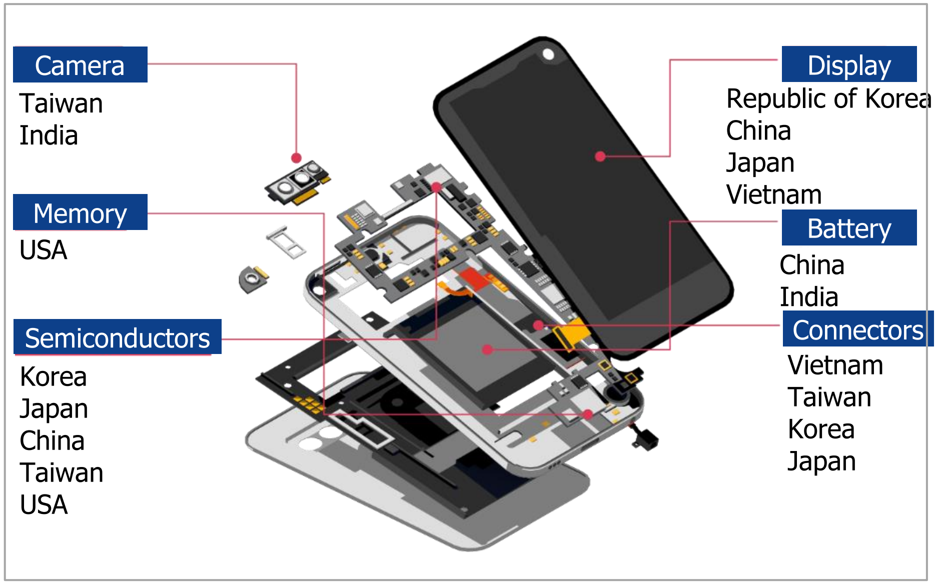
- We project FY24E growth at 7.3% and **FY25E at 6.9-7%. We see government continuing its capex push, at least though FY25**
- Rising domestic value addition in new-age sectors, reducing vulnerability to oil price shocks and improving factor productivity amid capex push are likely to be key triggers for India’s long-term growth trajectory.
- FY24E inflation is projected at 5.4% and **FY25E at 4.5%.** Slowing core inflation and lower crude prices are key positives.
- Fiscal deficit projected for FY24E at 5.9% and **5.4% of GDP in FY25E. If the government does not relax its fiscal glide path, we see government capex spending remaining flat between FY25E and FY26E.**
- India’s external sector is gaining resilience. We see current account deficit at 1.5% and 1.4% of GDP in FY24E and FY25E, respectively.
- Incremental flows, easing policy rates and normalisation in US rates may push India 10y yields lower to trade in 6.8-7.15% range **in FY25E.** We see USD-INR at 82.8 by end-FY24E and **81 by end-FY25E.**
- **We see first rate cut by the RBI in Q2FY25.**
- Weak domestic private consumption and trade risks are the potential risks to growth in FY25.

INDIA'S STRUCTURAL GROWTH DRIVERS HEREON: THREE PROPELLORS

#1: INDIGENOUS MANUFACTURING – ASSEMBLY AND VALUE ADDITION

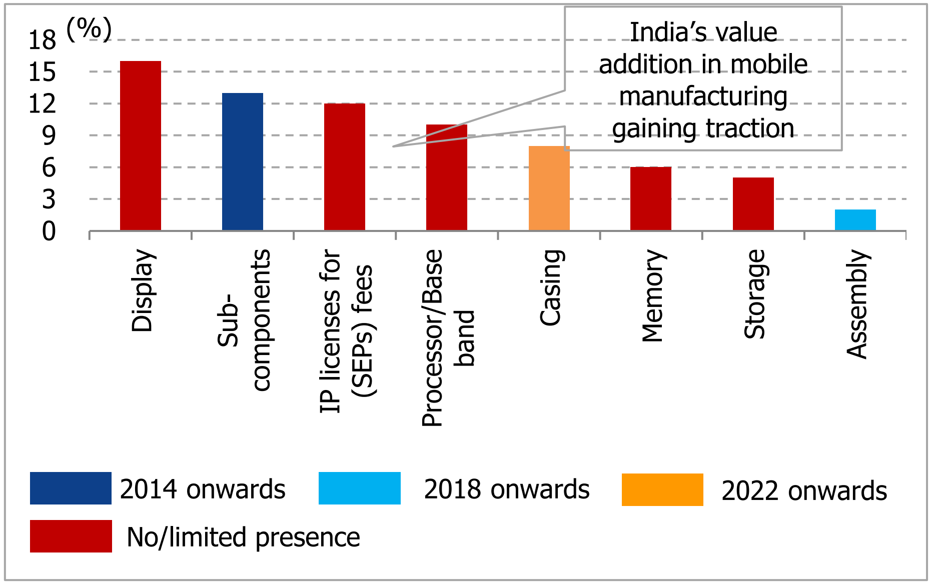
Domestic value addition in new-age sectors such as mobiles (1/2...)

Manufacturing origin of mobile phone components



Source: PWC, Elara Securities Research

Domestic value addition across mobile value chain

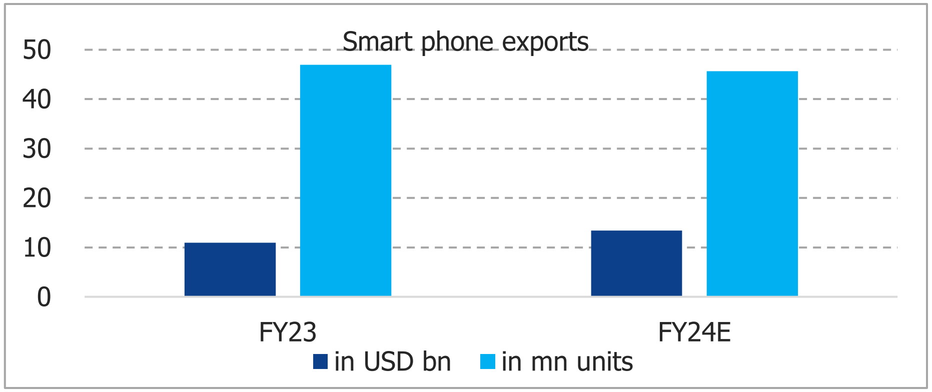


Source: PWC, Elara Securities Research

Mobile manufacturing production linked incentive scheme, which was the first one to take off (in FY21), has seen very good traction with domestic value addition picking pace.

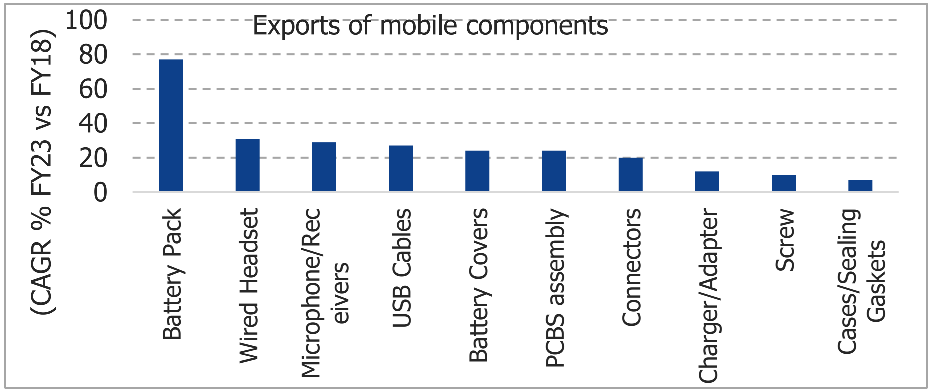
Domestic value-addition in new age sectors such as mobiles (2/2)

Smart phone exports are picking pace



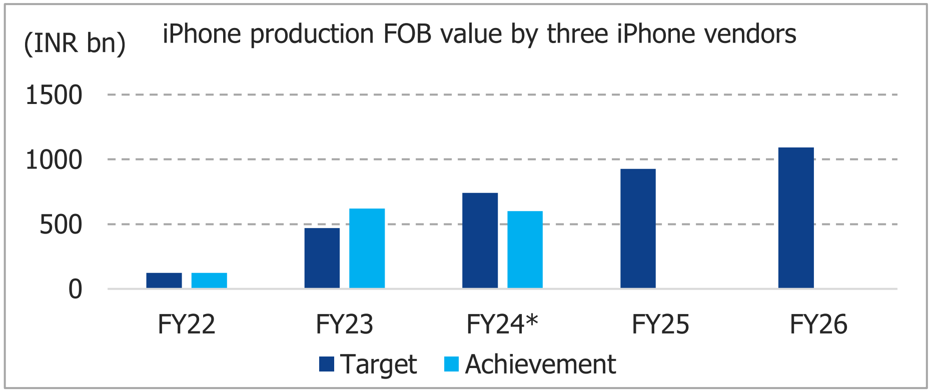
Source: Ministry of Commerce, Elara Securities Research

Domestic production in components scaling up



Source: Ministry of Commerce, Elara Securities Research

Apple iPhone production is scaling up



Source: Ministry of Commerce, Elara Securities Research

- India's smart phone exports have shot up sharply in the past two years and not all of these are just assembly.
- Exports of mobile components (battery packs, headsets, chargers, USD cables, SIM sockets, battery covers and microphones) and domestic value addition versus pre-Covid are gaining pace. These may rise further as Apple scales manufacturing base in India.

Scale effect of indigenous manufacturing and assembly can be significant

Scenario analysis of domestic assembly and manufacturing

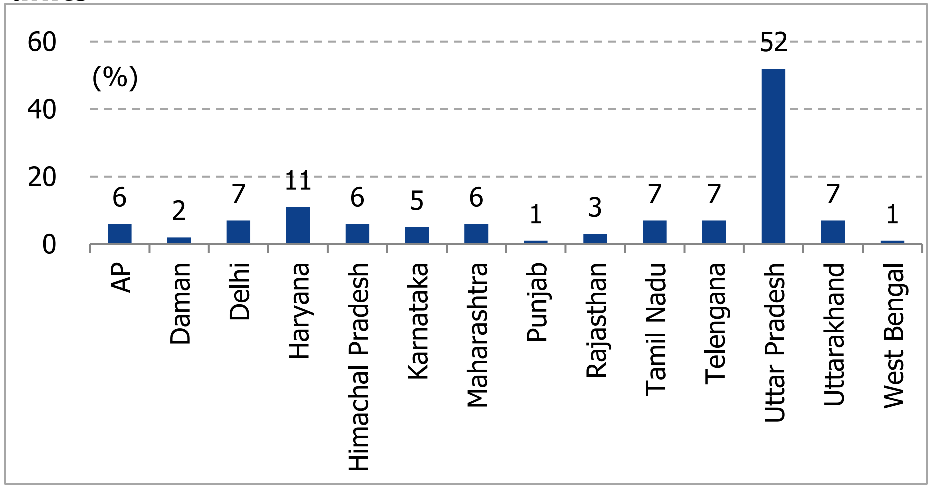
Scenarios	*1*	*2*	*3*	*4*
iPhone units (mn)	200	300	400	500
Assembly value addition (INR bn)	217	326	434	543
Assembly plus component manufacturing value addition (INR bn)	1,565	2,348	3,131	3,914
% of FY23 GDP	0.57	0.86	1.15	1.44

Source: Ministry of Commerce, CEIC, Elara Securities Estimate

- Assembly of all iPhone 15 handsets that Apple sold globally in 2022 can lead to INR 217bn value gain in India.
- However, India's presence has grown from just assembly value (2-3% value addition) to 15% in 2022 and ~20% at present.
- India makes 300mn handsets a year, whereas the total number of smart phones manufactured globally are ~1.35bn.
- The scope of scaling-up is enormous and one with significant forward and backward linkages.
- At 500mn units, manufacturing of phones can add ~ 1.5% to GDP.

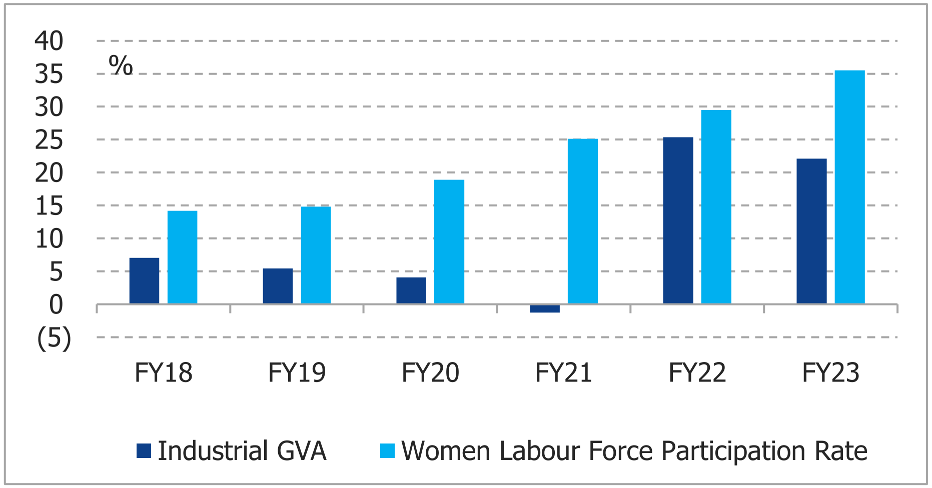
It can also address India's low female labour participation issues

Geography-wise break-up: Mobile phone, component units



Source: CEIC, Elara Securities Research

Female labour participation in Uttar Pradesh is rising



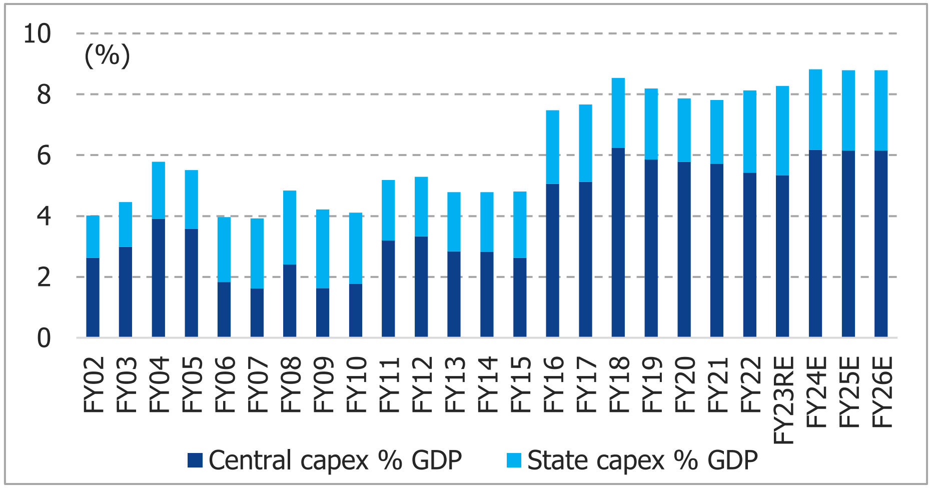
Source: CEIC, Elara Securities Research

- India's female labour force participation is the lowest globally, especially when compared with countries of India's size and structure.
- About 32.8% of females aged 15 years and above in India are participating in the labor force, as against 77.2% males and global average of 46%.
- Higher penetration of assembly-led manufacturing helps boost female labour participation, especially in rural areas – Uttar Pradesh being the key example.

#2: VISIBLE HAND OF GOVERNMENT

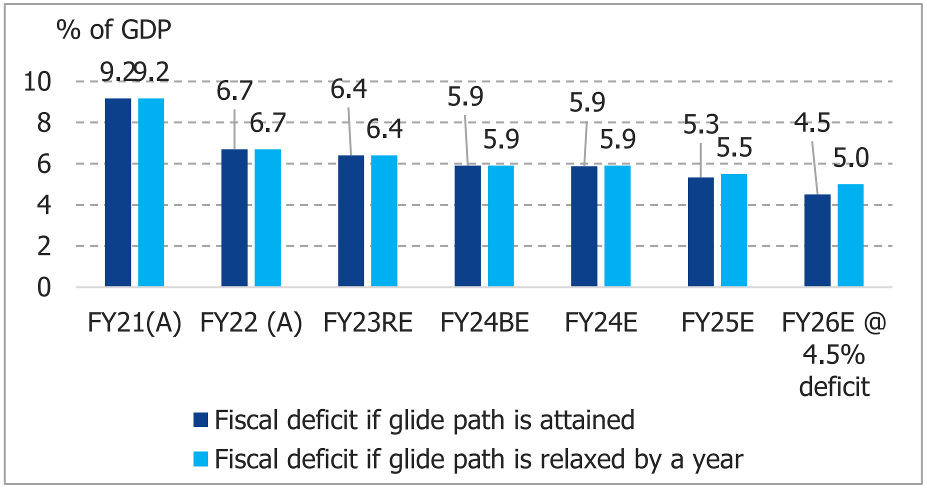
Sustaining economic thrust may need diluting fiscal deficit mandate

Government capex has risen meaningfully lately



Source: CEIC, Elara Securities Estimate

Fiscal deficit glide path may need a compromise

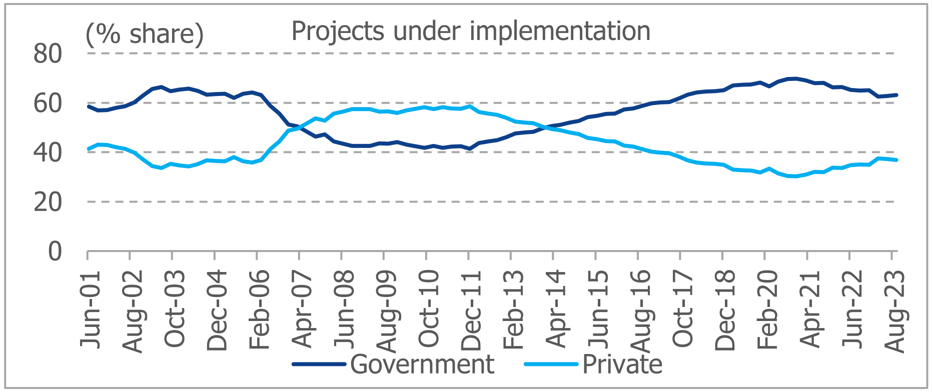


Source: CEIC, Elara Securities Estimate

- With private sector capex demand yet to kick off in a broad-based way, we believe there is still some leg room for government capex to go.
- While sustaining government capex in FY25E does not seem difficult, attaining fiscal deficit mandate by FY26E may impact government capex if the private capex has not taken off.

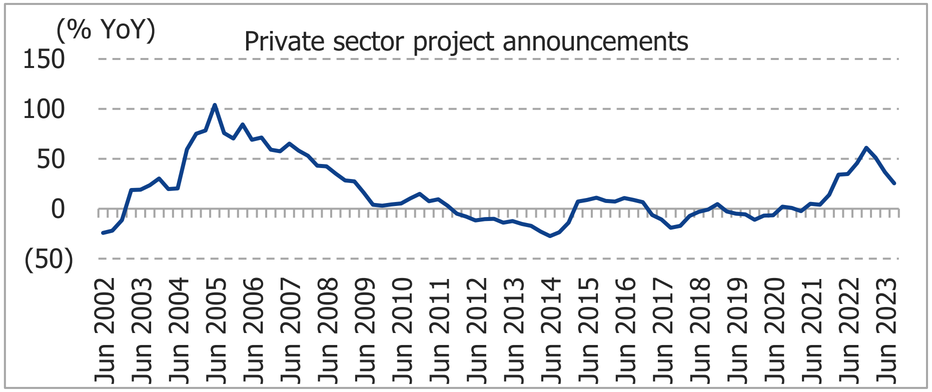
...as private sector capex has not yet picked up meaningfully

Government leads project implementation



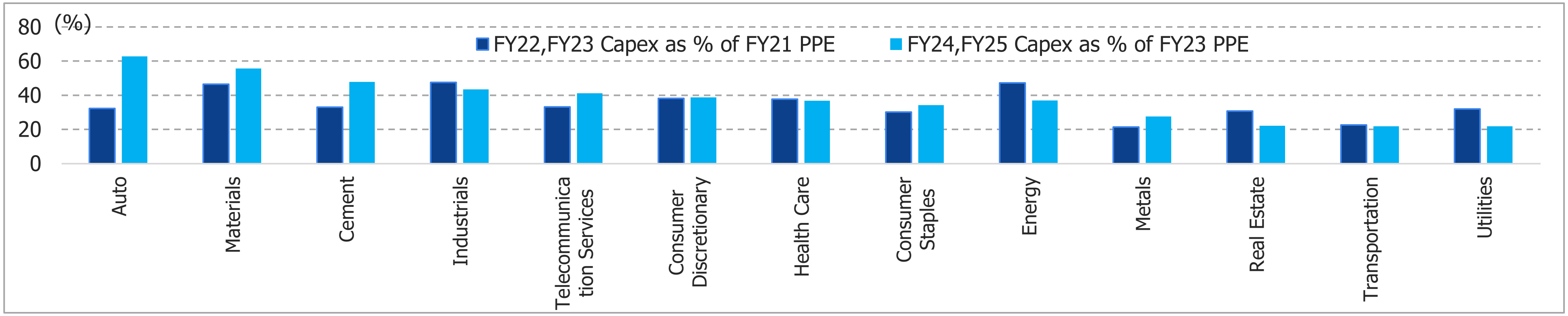
Source: CMIE, Elara Securities Research

Private projects announcements have eased latest



Source: CMIE, Elara Securities Research

Private sector capex higher in Auto, Metals, Cement, Material but has declined in Energy, Utilities, Real Estate



Source: Bloomberg, Elara Securities Research

...and remains concentrated in a few sectors yet...

Sectors	Avg. share % (FY03-08)	Avg. share % (H1FY23)	Avg. share % (H1FY24)	pps change in % avg share (H1FY23 versus H1FY24)
Manufacturing	42.5	61.4	54.5	(6.9)
Food & Agro-based Products	1.1	0.9	0.7	(0.2)
Textiles	1.2	0.7	0.5	(0.2)
Chemicals & Chemical Products	7.2	23.6	22.7	(0.9)
Petroleum Products	3.1	10.3	4.5	(5.9)
Consumer Goods	0.7	0.4	0.3	(0.1)
Construction Material	2.3	1.9	1.4	(0.6)
Metals & Metal Products	26.1	18.6	13.0	(5.5)
Ferrous Metals	22.3	17.1	12.0	(5.0)
Non-ferrous Metals	3.7	1.5	1.0	(0.5)
Machinery	1.1	10.2	11.9	1.7
Non-electrical Machinery	0.4	0.2	0.2	0.0
Electrical Machinery	0.2	0.1	0.1	0.0
Electronics	0.5	9.9	11.6	1.7
Transport Equipment	1.9	3.6	2.5	(1.1)
Automobiles & Ancillaries	1.9	3.5	2.3	(1.2)
Miscellaneous Manufacturing	0.8	1.5	1.6	0.1
Mining	3.3	2.3	1.2	(1.1)
Electricity	25.7	20.8	23.4	2.5
Electricity Generation	25.6	20.6	23.3	2.7
Conventional Electricity	24.7	8.2	9.8	1.7
Renewable Electricity	0.9	12.4	13.5	1.0

Sectors	Avg. share % (FY03-08)	Avg. share % (H1FY23)	Avg. share % (H1FY24)	pps change in % avg share (H1FY23 versus H1FY24)
Electricity Transmission & Distribution	0.1	0.2	0.1	(0.2)
Electricity Transmission	0.1	0.2	0.1	(0.2)
Electricity Distribution	0.0	0.0	0.0	0.0
Services (other than financial)	21.5	13.4	19.9	6.5
Hotels & Tourism	1.0	0.3	0.2	(0.1)
Wholesale & Retail Trading	4.1	0.7	0.4	(0.3)
Transport Services	8.8	8.2	15.3	7.1
Road Transport & Allied Services	2.8	0.3	0.2	(0.1)
Railway Transport & Allied Services	0.2	0.5	1.5	1.0
Air Transport & Allied Services	2.8	2.0	9.8	7.8
Shipping Transport & Allied Services	2.9	4.6	3.1	(1.5)
Transport Logistics Services	0.1	0.8	0.7	(0.1)
Communication Services	0.6	0.0	0.0	0.0
Telecommunication Services	0.6	0.0	0.0	0.0
Courier Services	0.0	0.0	0.0	0.0
Information Technology	2.1	3.0	3.1	0.1
Computer Software	1.9	0.4	0.3	(0.1)
ITES	0.2	2.6	2.8	0.2
Miscellaneous Services	5.0	1.2	1.0	(0.3)
Construction & Real Estate	7.0	2.1	1.0	(1.1)
Real Estate	7.0	2.1	1.0	(1.1)
Housing Construction	2.7	1.1	0.4	(0.7)
Commercial Complexes	4.3	1.0	0.6	(0.4)
Industrial & Infrastructural Construction	0.0	0.0	0.0	0.0

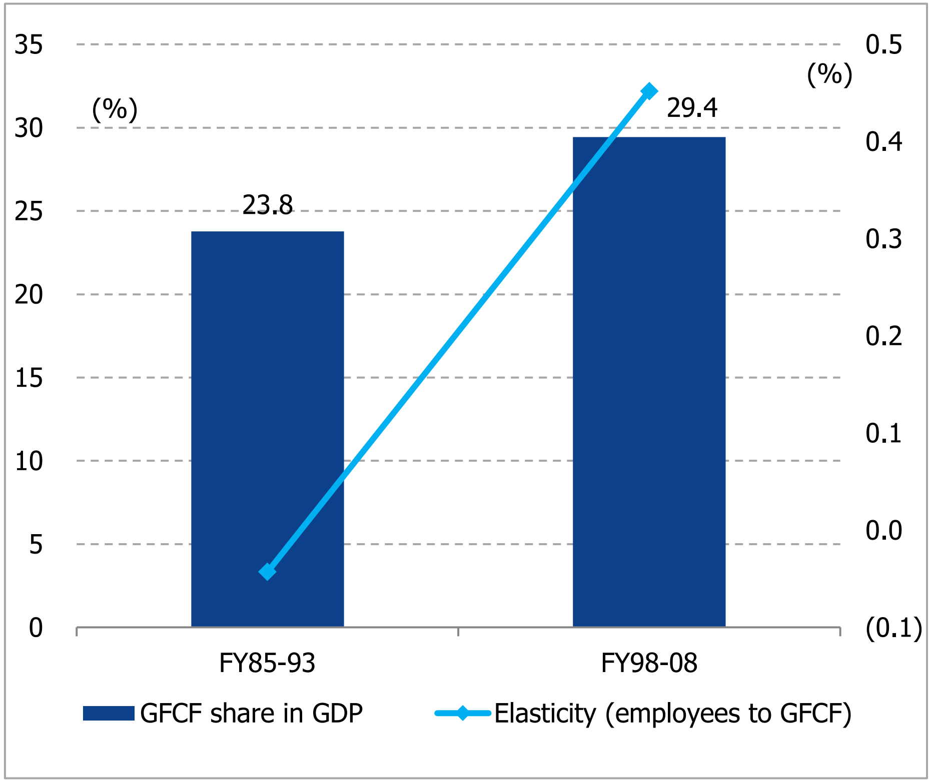
Source: CMIE, Elara Securities Research

…sustained 30% nominal investment rate can ensure 12% nominal growth

- India may need to maintain its gross fixed capital formation, as a percentage of GDP, consistently at 30% through the next decade (present 30%) on a nominal basis to be able to attain 12% nominal GDP growth in the next 8-10 years.
- This requires the government to continue to spend in the near term as private sector capex is yet to pick up in a sustained manner.
- Sustained higher capital formation may allow for higher employment elasticity as past cycles of capex have shown.
- Sustained high capital expenditure may also lead to gains in total factor productivity.
- Assuming technology to be an exogenous factor that improves consistently, per our analysis, consistent higher capital formation (30% as share of GDP) may spike total factor productivity in India 11% by FY30E from pre-Covid (FY19) and ~26% by FY40E, *ceteris paribus.*

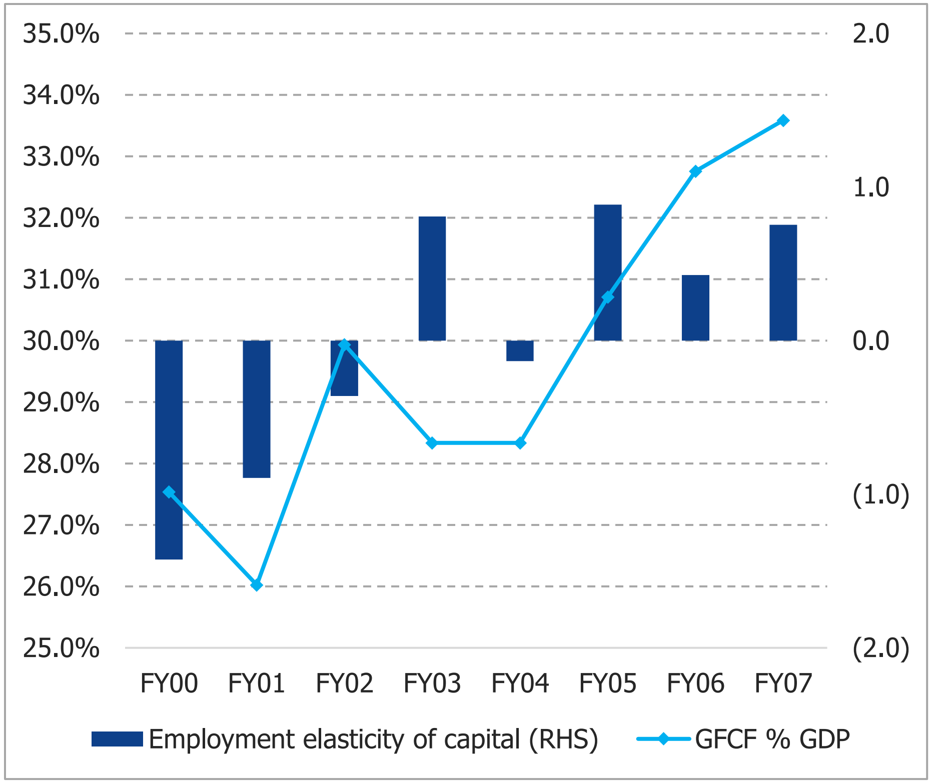
...while boosting employment elasticity...

Episodes of higher capex have seen better employment...



Source: CEIC, ASI, Elara Securities Research

...as was seen in 2004-2008 phase



Source: CEIC, ASI, Elara Securities Research

- Higher capex years of FY03-08 saw employment elasticity of capital formation improve from -0.36 in FY02 to 0.75 in FY07.

...as also total factor productivity

Capital formation cycle can aid total factor productivity and in turn per capita income

Indicator	Unit	FY90	FY00	FY10	FY20	FY30E	FY40E
TFP	Index	0.26	0.46	0.81	0.93	1.16	1.34
Nominal GDP	USD tn	0.3	0.5	1.3	2.8	7.2	21.2
Per capita GDP	USD	354	449	1,116	2,050	5,117	15,152

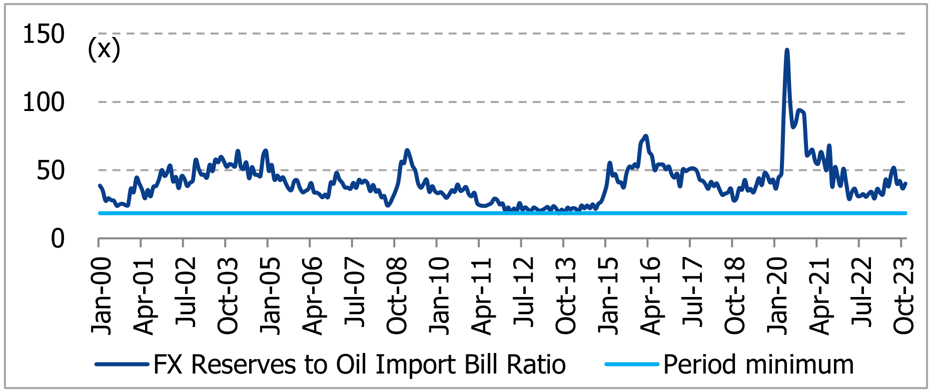
Note: TFP=1 in 2019; Source: IMF, ASI, Elara Securities Estimates

- Assuming nominal GDP growth of 11% from FY35E, we see India reaching a nominal per capital GDP of USD 15,152 by FY40E.
- This is to be aided by total factor productivity of 1.34 by FY40E (1 in FY19), the necessary condition for which is constant GFCF as percentage of GDP rate of 25-30% through FY25E-40E.
- In our TFP model, we split Capital (K) and Labor (L) by 40:60 ratio as we see absorption of the youth population as key. And this may only be possible if fixed capital in the economy rises. Technology is the key unknown and given the technological progress + technological transfer already witnessed by India till now, we expect it to contribute positively to TFP.

#3: REDUCED VULNERABILITY TO OIL SHOCKS

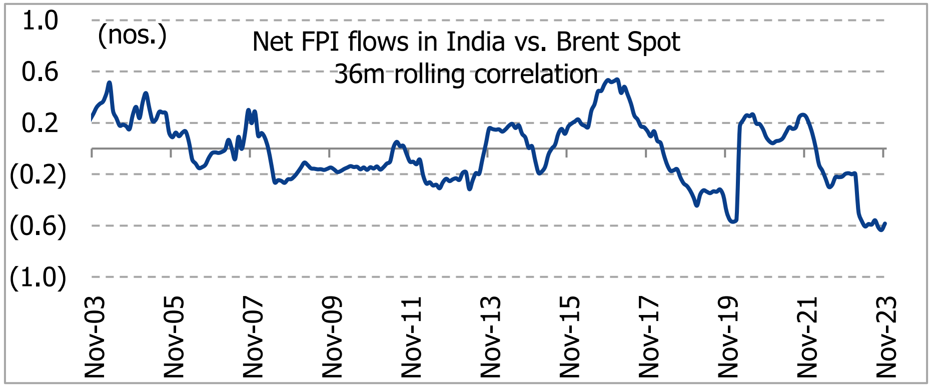
India's ability to withstand higher oil prices has improved...

FX reserves in comfortable position



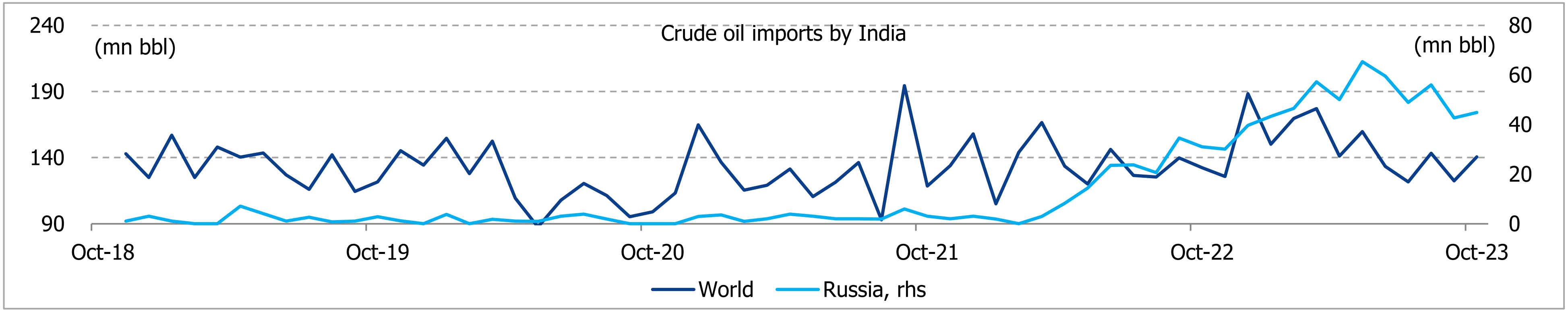
Source: CEIC, Elara Securities Research

FPI inflows and crude oil price correlation record low



Source: CEIC, Elara Securities Research

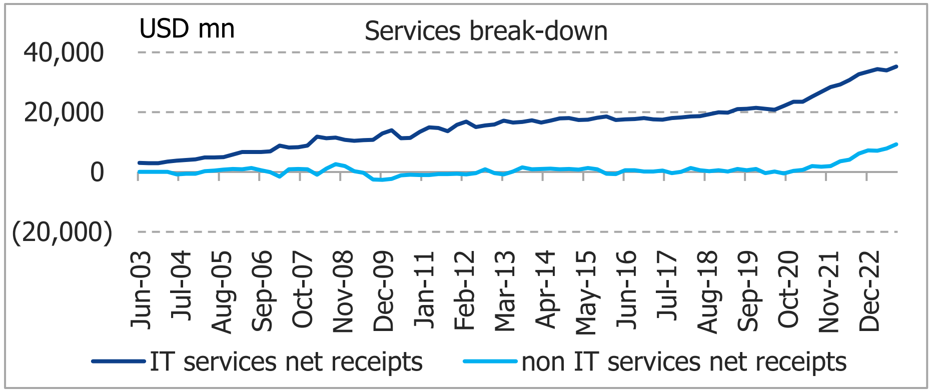
The Russia factor



Source: CMIE, Elara Securities Research

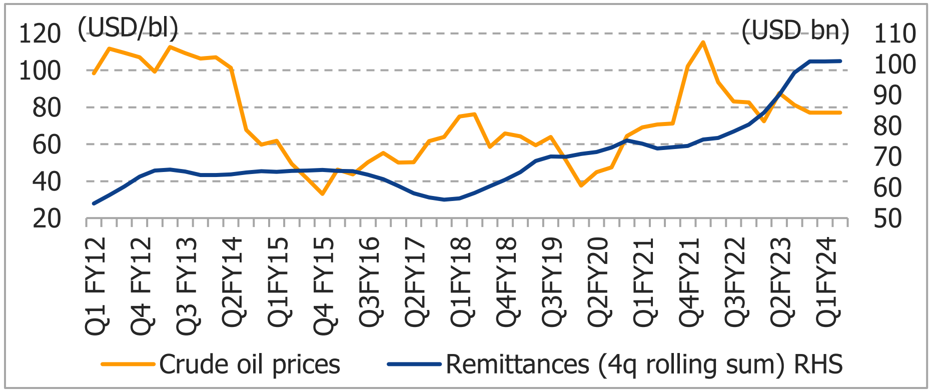
...with external sector getting incrementally resilient

Non-IT services export providing support



Source: CMIE, Elara Securities Research

Remittances slowly getting delinked with oil



Source: CMIE, Elara Securities Research

- ***Pravasi Kaushal Vikas Yojana*** is an umbrella under which skilled workers are being exported to advanced countries other than the Middle East.
- Government's strategic tie-ups to provide skilled workers to Europe and other advanced countries such as Taiwan and Israel may offer a leg-up to remittances that are de-linked to crude oil.
- Skill sets include varied jobs ranging from carpentry to plastering, ceramic tiles.
- Shortage of workers in Greece prompted it to approve a law allowing illegal immigrants to receive three-year residency and work permits for jobs in certain sectors.

Strategic move

Flurry of mobility and migration agreements signed by India in recent years

Agreements signed			
2018	France	2021	United Kingdom
2022	Germany	2022	Finland
2023	Australia	2023	Austria
2023	Italy		

Under discussion

Netherlands, Taiwan, South Korea, Greece, Denmark

Source: MEA, Business Standard dated Dec 25 2023, Elara Securities Research

INDIA – OVERALL OUTLOOK FOR FY25

ElaraCapital

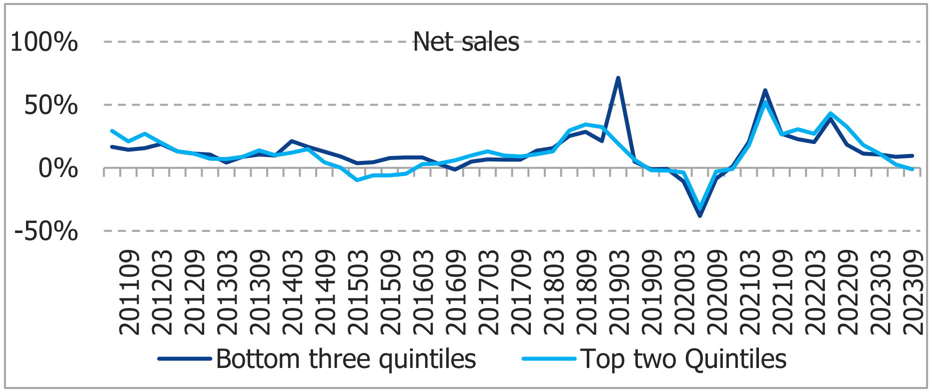
India: Current growth is backed by strong fundamentals…

Year	Real GDP YoY	CAD % GDP	CPI YoY %	FD % GDP	Net NPA%	Corp debt to GDP	World GDP %
FY01	3.8	(0.6)	3.8	5.6		62.8	4.8
FY02	4.8	0.7	4.3	6.1	3.0	65.3	2.5
FY03	3.8	1.2	4.0	5.8	2.5	71.6	2.9
FY04	**7.9**	**2.3**	**3.9**	**4.4**	**1.5**	**72.9**	**4.3**
FY05	**7.9**	**(0.4)**	**3.8**	**4.0**	**1.3**	**79.8**	**5.4**
FY06	**7.9**	**(1.2)**	**4.4**	**4.0**	**0.9**	**94.0**	**4.8**
FY07	**8.1**	**(1.0)**	**6.7**	**3.4**	**1.1**	**102.0**	**5.4**
FY08	**7.7**	**(1.3)**	**6.2**	**2.6**	**1.2**	**107.7**	**5.6**
FY09	3.1	(2.3)	9.1	6.1	1.5	112.0	3.1
FY10	**7.9**	**(2.8)**	**12.4**	**6.6**	**1.3**	**111.9**	**(0.1)**
FY11	**8.5**	**(2.9)**	**10.5**	**4.9**	**0.8**	**113.2**	**5.5**
FY12	5.2	(4.3)	8.4	5.9	0.7	113.0	4.3
FY13	5.5	(4.8)	10.1	4.9	0.8	110.2	3.5
FY14	6.4	(1.7)	9.4	4.5	1.1	104.2	3.4
FY15	**7.4**	**(1.3)**	**5.8**	**4.1**	**1.1**	**104.3**	**3.5**
FY16	**8.0**	**(1.1)**	**4.9**	**3.9**	**1.8**	**97.4**	**3.4**
FY17	**8.3**	**(0.7)**	**4.5**	**3.5**	**2.6**	**88.0**	**3.2**
FY18	6.8	(1.8)	3.6	3.5	3.2	88.4	3.8
FY19	6.5	(2.1)	3.4	3.4	1.7	84.1	3.6
FY20	3.9	(0.9)	4.8	4.6	1.3	93.6	2.8
FY21	(5.8)	0.9	6.2	9.2	1.1	100.5	(2.8)
FY22	**9.1**	**(1.2)**	**5.5**	**6.8**	**0.7**	**91.7**	**6.3**
FY23	**7.2**	**(2.0)**	**6.7**	**6.4**	**0.4**	**90.3**	**3.5**
FY24	**7.3**	**(1.5)**	**5.4**	**5.8**	**0.4**	**92.0**	**2.7**

Source: IMF, BIS, CMIE, CEIC, Elara Securities Research

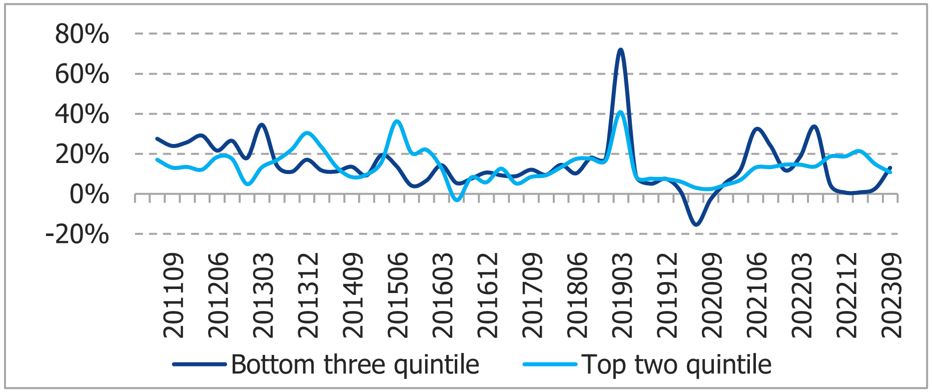
...wherein small and mid-sized businesses growing faster than large ones

Sales: Smaller companies outdid large ones in FY24...



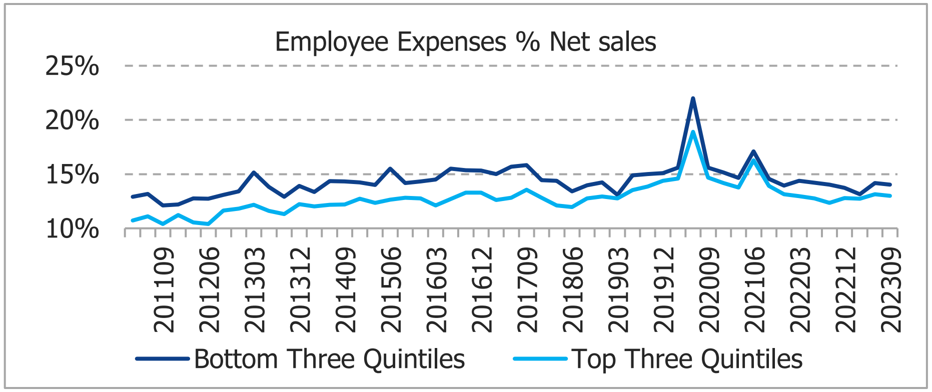
Source: CMIE, CEIC, Elara Securities Research

...and do did their employee expenses



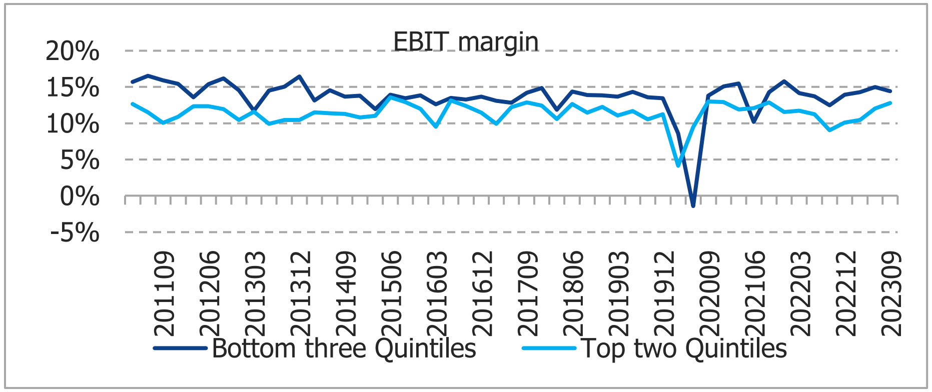
Source: CMIE, CEIC, Elara Securities Research

Employee expenses rose faster for small/mid-sized firms



Source: CMIE, CEIC, Elara Securities Research

...yet margin recovery has been impressive

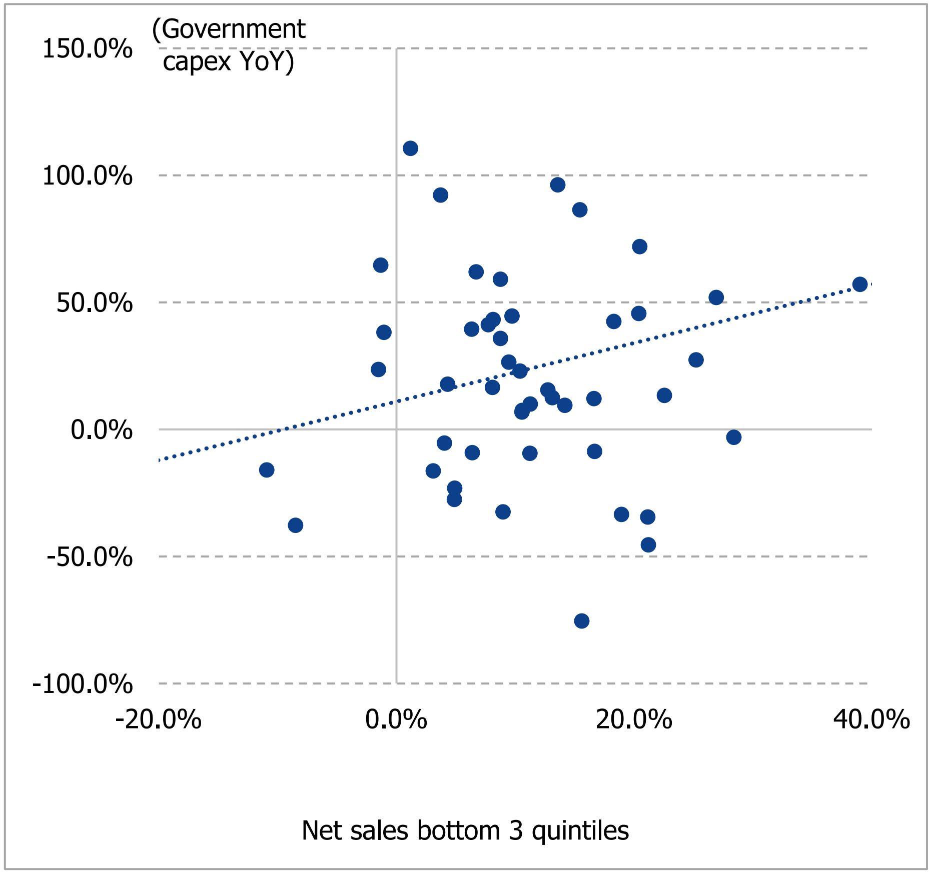


Source: CMIE, CEIC, Elara Securities Research

Horizontal axis in all charts are in YYYYMM format.

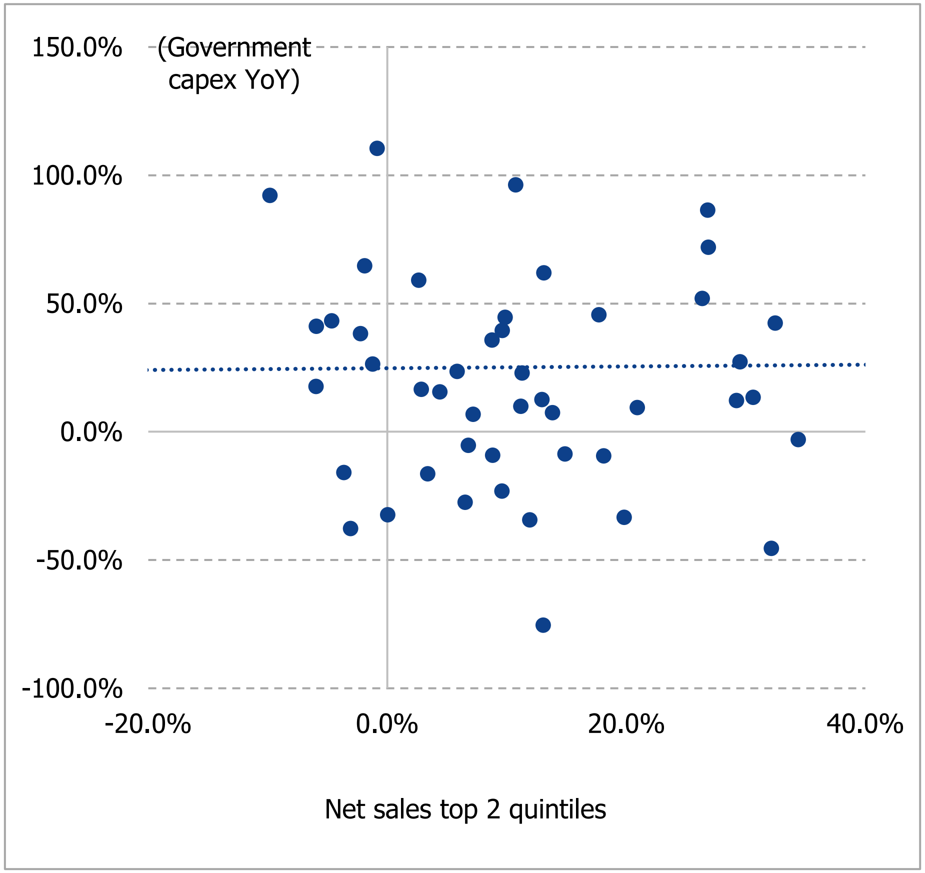
…as government capex has expanded opportunities for small-mid firms

Net sales of small and mid-sized companies positively correlated with government capex



Note: BSE 500 ex financials data; Source: CMIE, CEIC, Elara Securities Research

Sales of large companies not correlated with government capex

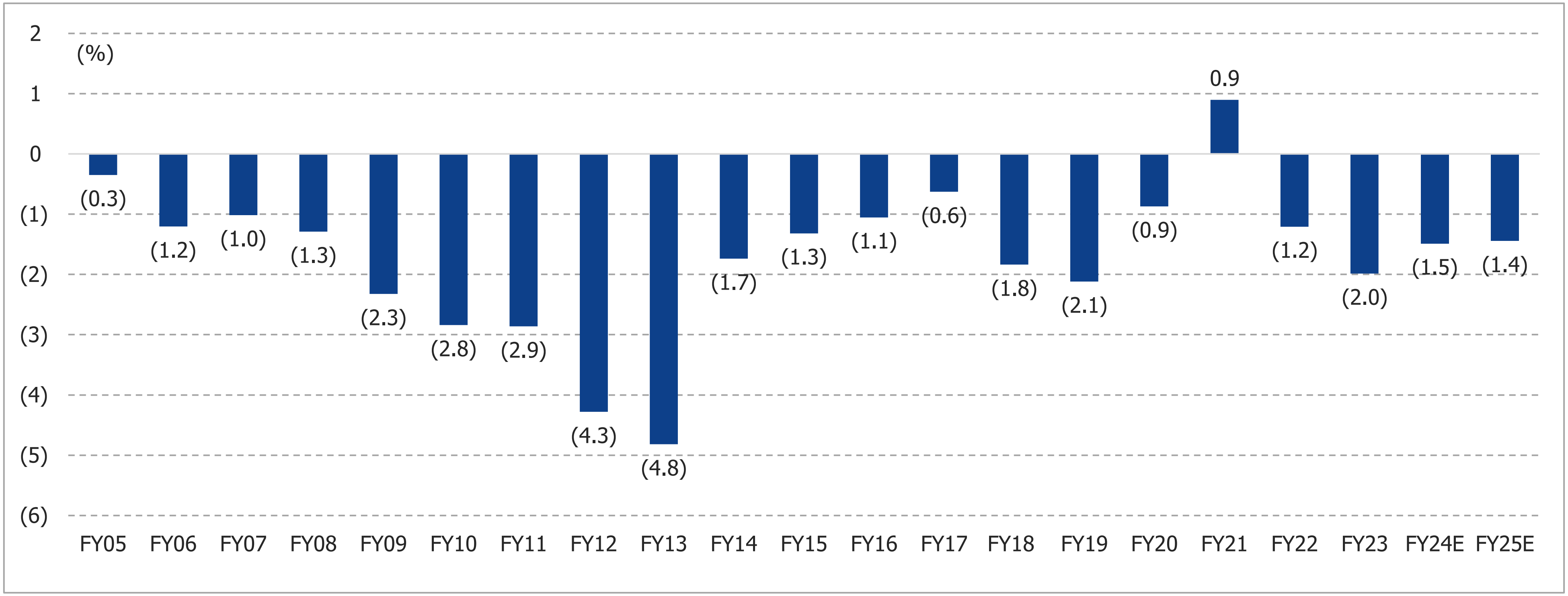


Note: BSE 500 ex financials data; Source: CMIE, CEIC, Elara Securities Research

INDIA – EXTERNAL SECTOR OUTLOOK

India's current account deficit in comfortable zone...

Current account deficit projected at 1.5% and 1.4% of GDP in FY24E and FY25E

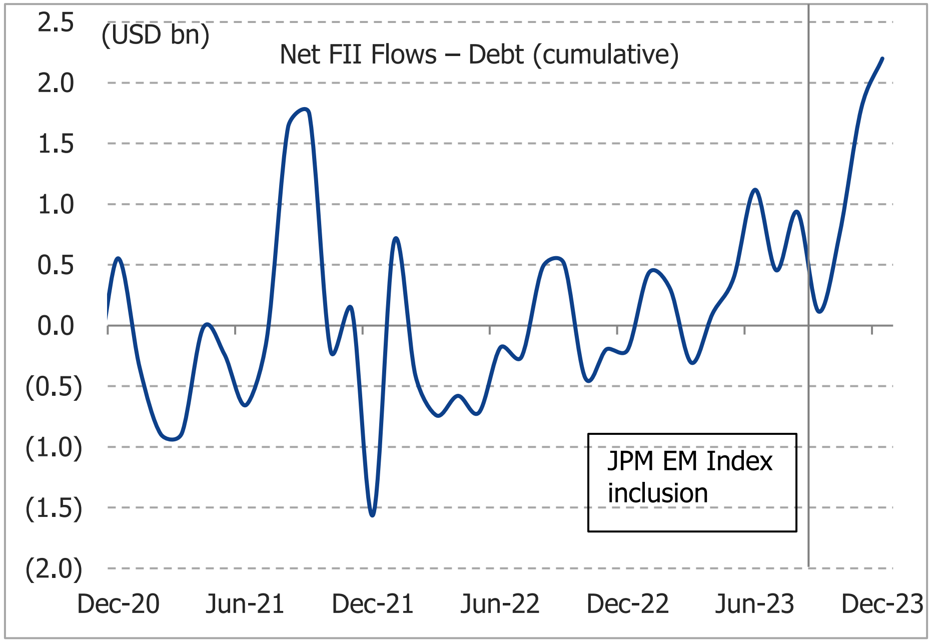


Source: CMIE, Elara Securities Estimate

Lower oil prices, recovery in IT exports, consistent non-IT exports and possibility of rising remittances are the key factors that may keep CAD under check.

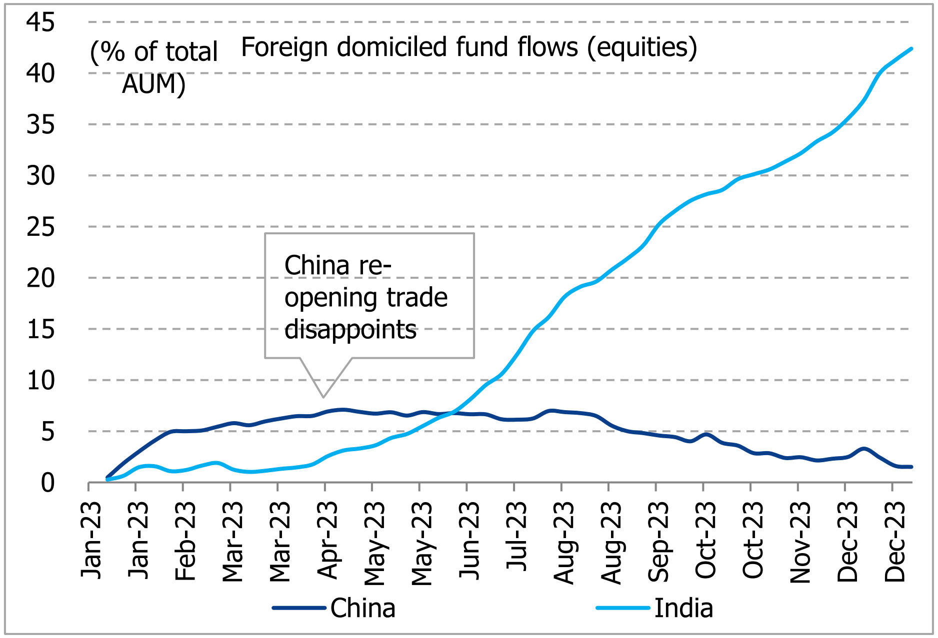
FII flow outlook is positive for 2024

FII inflow into debt has taken off post JPM EM inclusion



Source: CEIC, Elara Securities Research

India dedicated FII equity flows eclipsed China



Note: Data till 3 January 2024; Source: EPFR, Elara Securities Research

- Recent FII outflows from India's equity market have mainly been led by hedge funds and prop desks.
- India's inclusion in bond indices to bode well for debt inflows.
- Rising UST yields, augmenting geopolitical risks, and crude oil prices are key risks for FII flows.
- Dovish Fed and strong domestic macros are the key tailwinds for flows into India

India's macro-financial and policy stability, its unique edge…

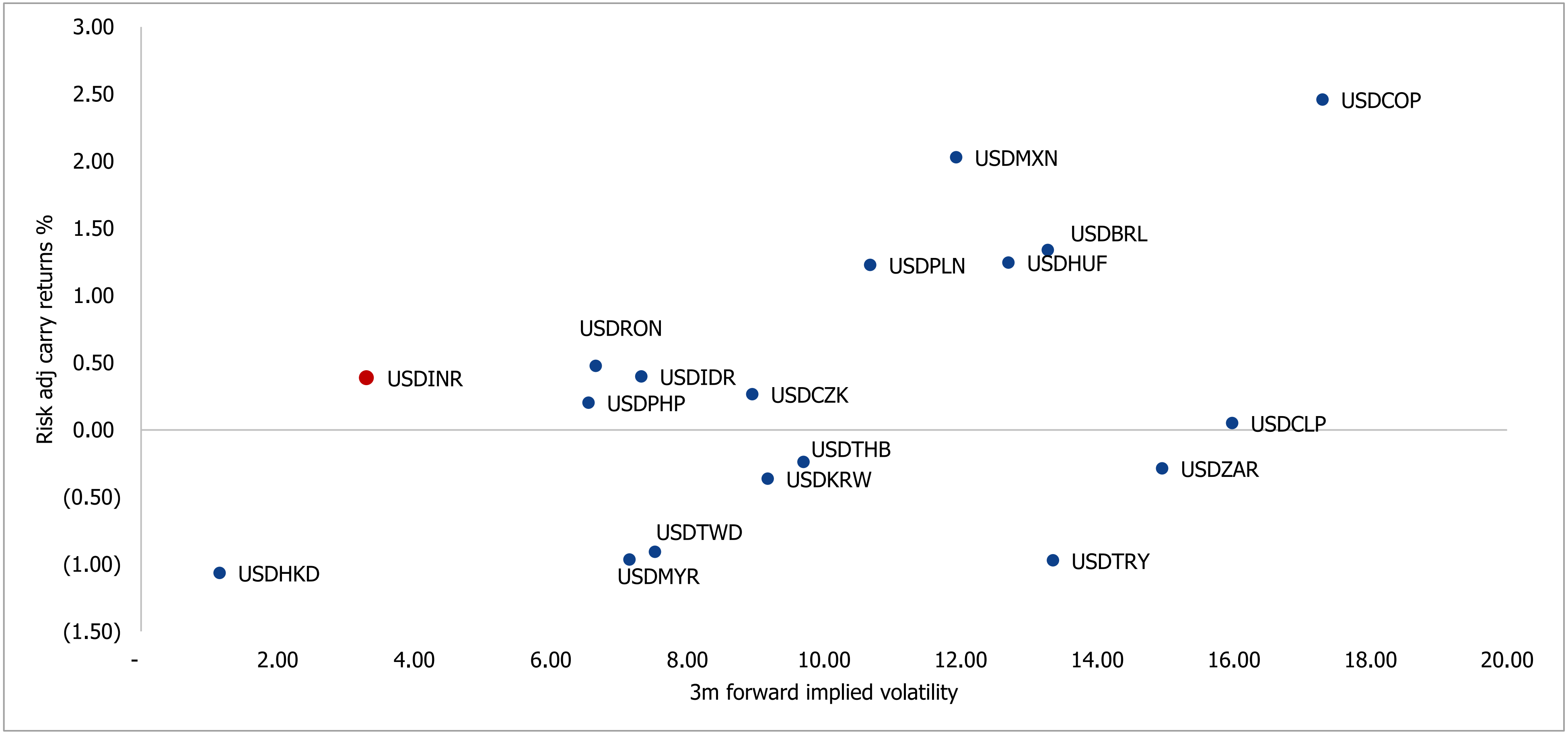
Relative macros and external sector metrics stronger than EM peers and DMs

Indicators	Period	Units	Emerging markets					Developed markets		
			India	Brazil	China	Indonesia	South Korea	Europe	UK	US
Growth	2024-25E	%	7.2**	1.7	4.2	5.0	2.3	1.7	1.3	1.7
Inflation	2024-25E	%	4.4	3.8	2.0	2.5	2.2	3.4	2.9	2.6
Import cover ratio	Latest	x	11.1	16.7	14.9	6.5	7.5	-	-	-
External short term debt cover	Latest	x	4.9	4.1	2.4	2.5	2.8	-	-	-
Fiscal deficit % of GDP	Pre vs Post covid*	bps	339	101	51	234	332	447	795	653
Policy uncertainty index	Jan-Nov 2023 avg	No.	65.9	182.6	309.3	-	127.7	273.7	262.0	154.2
Per capita GDP	2028E	% CAGR	7.3	3.2	5.5	6.2	2.2	3.7	4.3	4.3

Note: *average CY18, 2019 versus CY20-22. **FY basis. Source: IMF, CEIC, Policyuncertainty.com, Elara Securities Research, Elara Securities Estimates.

...and so is stable USD-INR thanks to the visible hand of RBI

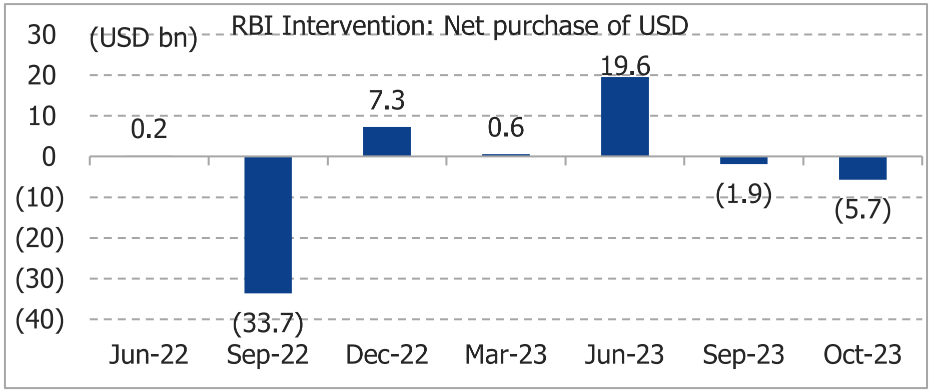
USD-INR – Least volatile unpegged FX among EMs in 2023



Note: Data as on 2 January 2024, 12.00 IST; Source: Bloomberg, Elara Securities Research

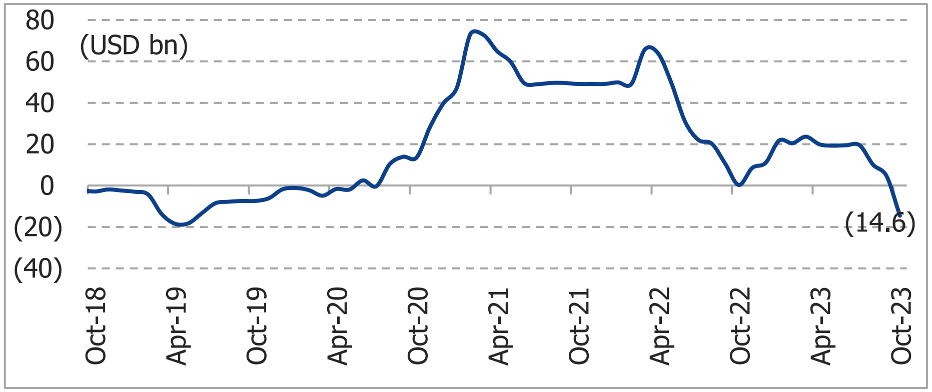
USD-INR – Appreciation bias persists

RBI sold USD consecutively in Q2FY24 and Oct-23



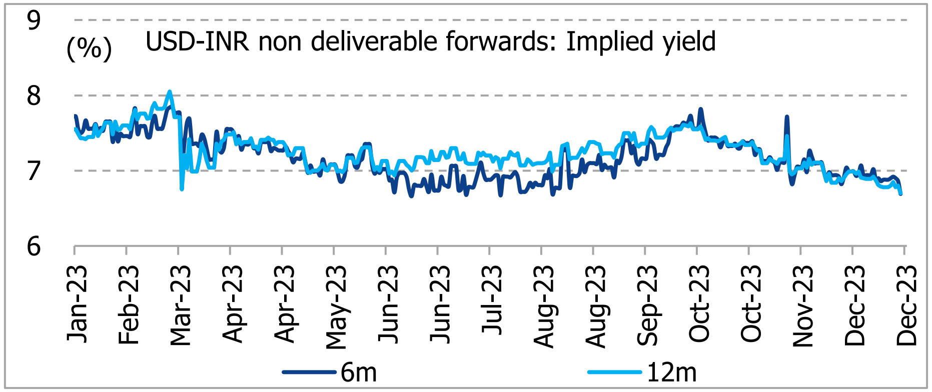
Source: Bloomberg, Elara Securities Research

RBI's forward book negative for first time since 2020



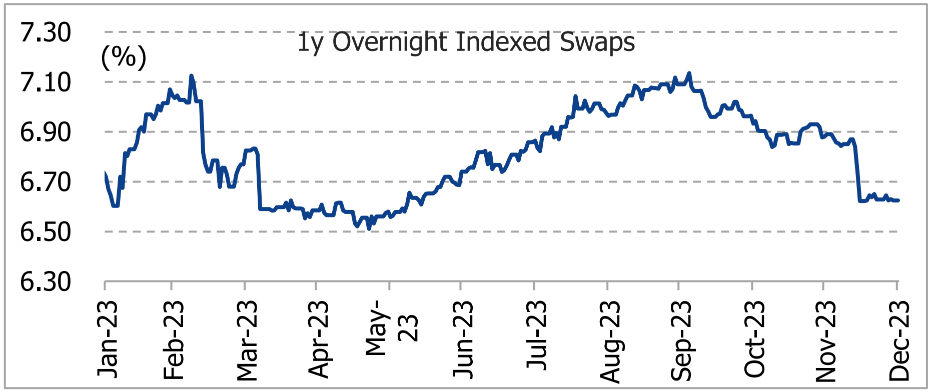
Source: Bloomberg, Elara Securities Research

Forward rates moderating consistently post Q2FY24



Source: Bloomberg, Elara Securities Research

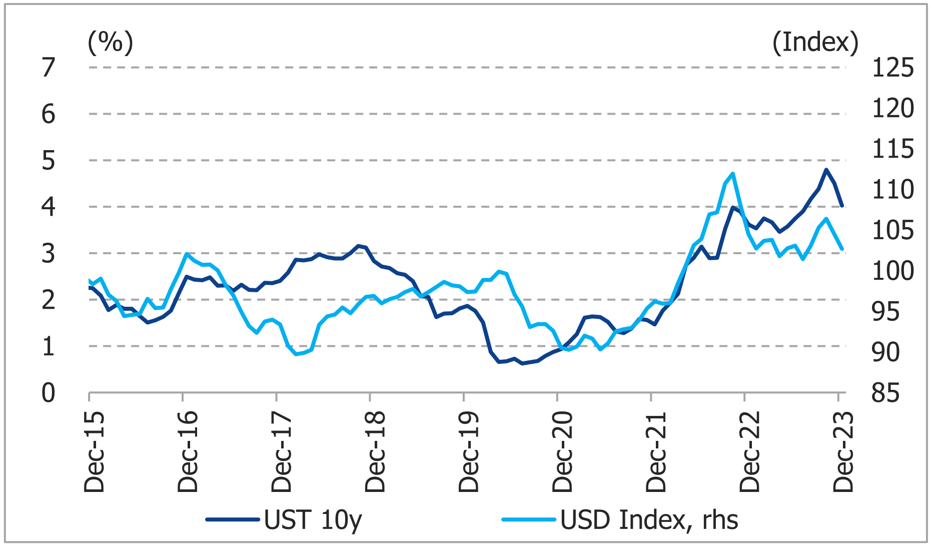
Rate cut expectations from RBI yet to surface



Source: Bloomberg, Elara Securities Research

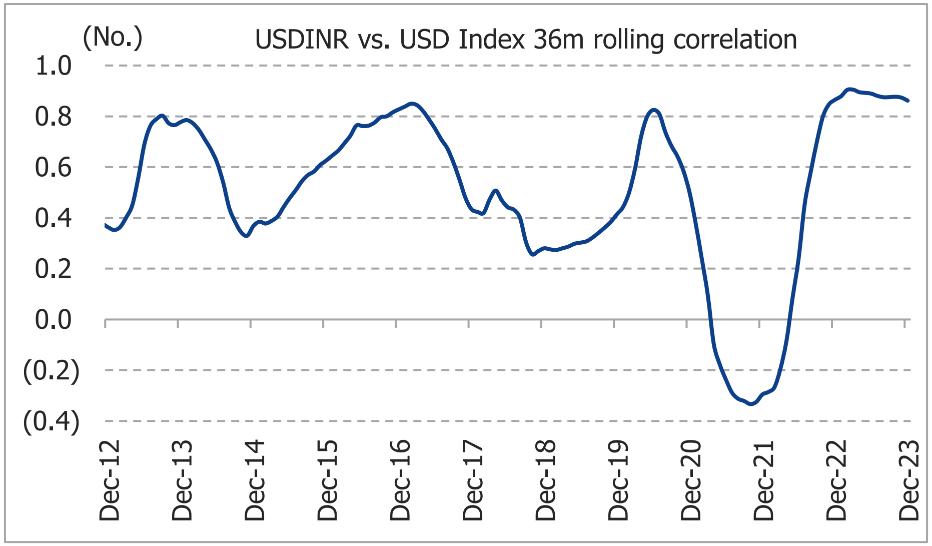
See USD-INR – FY24E at 82.8, FY25E at 81-81.5

Easing US yields USD negative…



Source: CEIC, Elara Securities Research

…softer USD good for INR with correlation >0.8



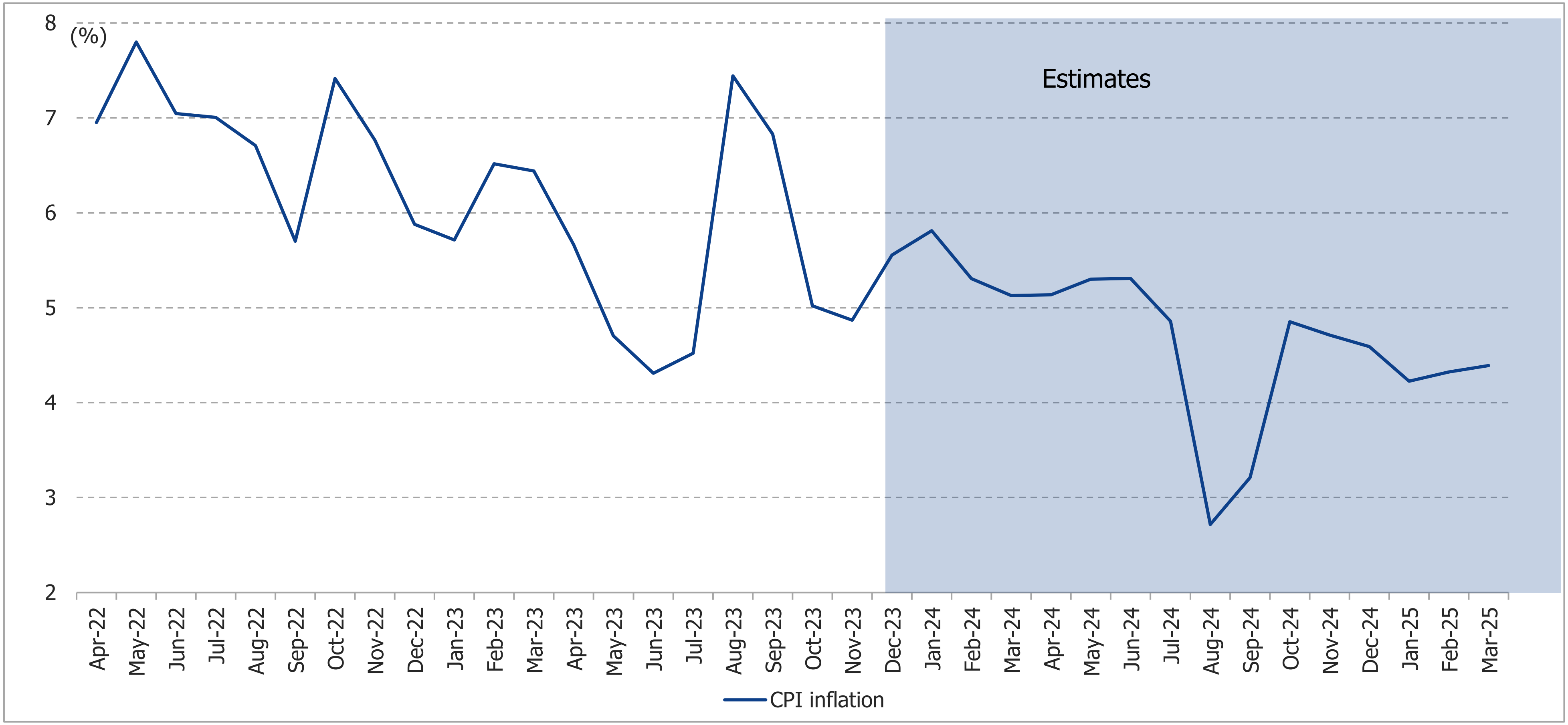
Source: CEIC, Elara Securities Research

- We see Fed's next action as cut, hence, injecting downside pressure on USTs and in turn the USD.
- Lower USD, manageable CAD, lower oil prices and downward trajectory of fiscal deficit keep outlook for INR positive in the next two years.
- But risks remain in the form of RBI – which has been intervening to stem volatility – in a year when exports may remain sluggish due to global slowdown. Also, uncertainties remain over RBI's tolerance on INR's appreciation pressure.

INDIA – INFLATION OUTLOOK

See average FY24E CPI at 5.3-5.4% and FY25E at 4.5%

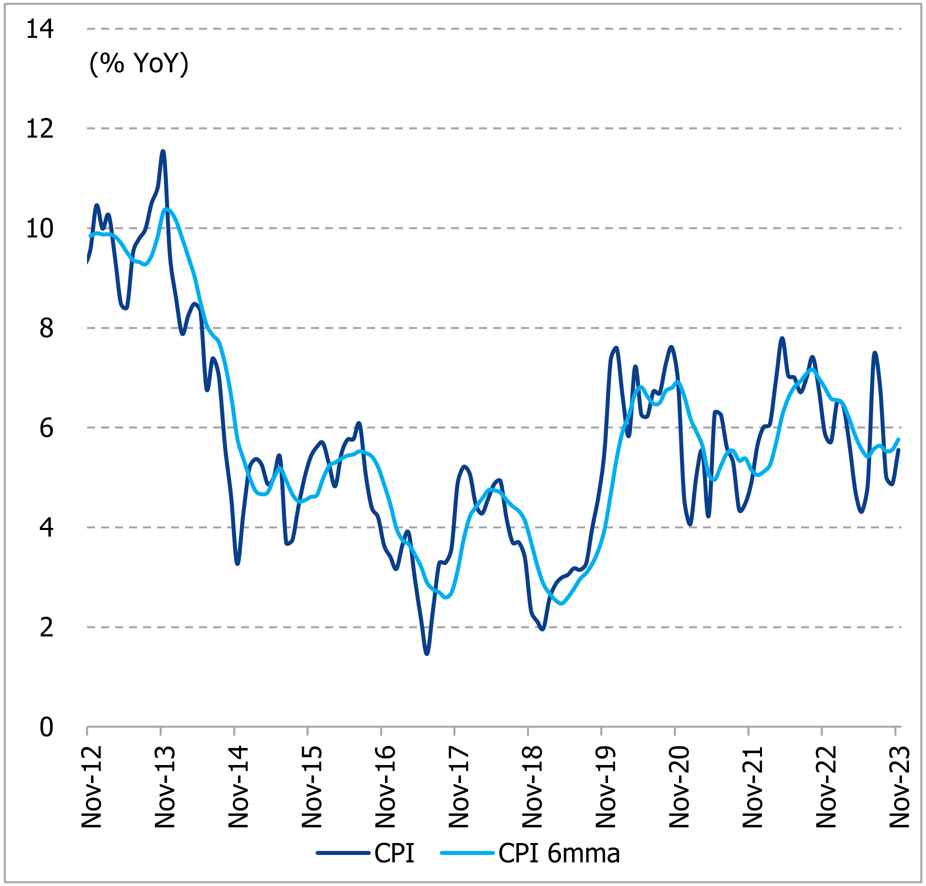
FY24E and FY25E CPI inflation trajectory



Source: CEIC, Elara Securities Estimates

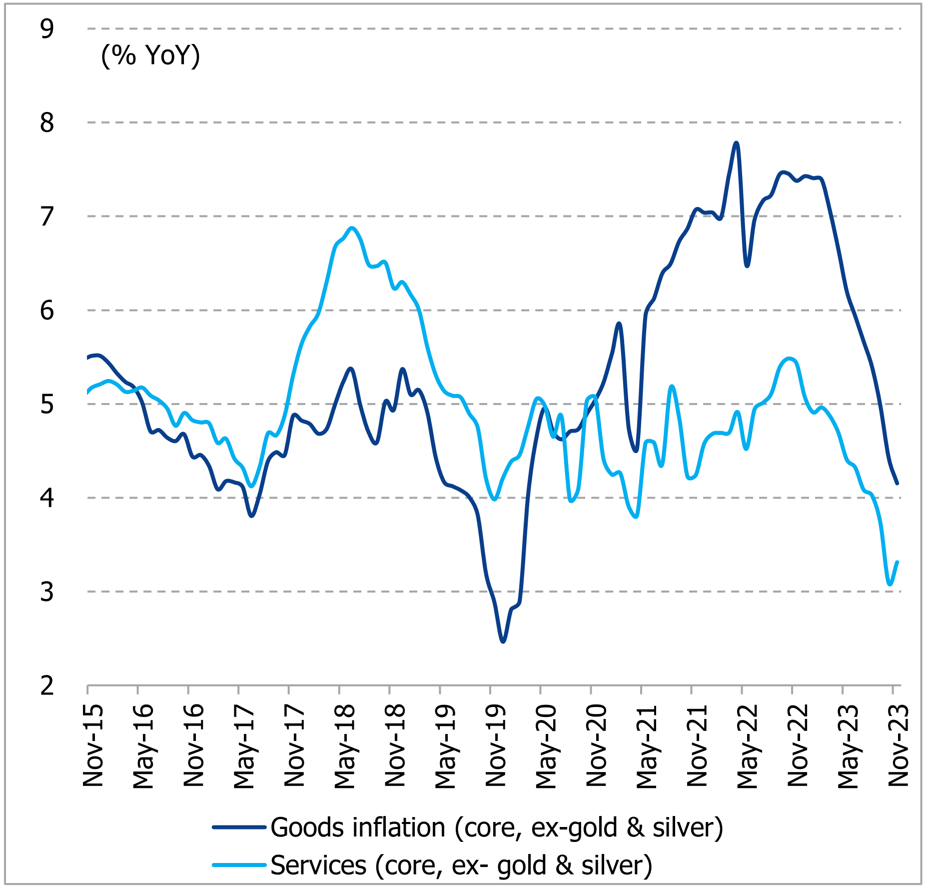
Headline inflation has been volatile this year...

Headline inflation settling at 5.5-6%



Source: CEIC, Elara Securities Research

Super core goods and services inflation easing sharply



Source: CEIC, Elara Securities Research

...amid spike in food inflation...

Staples food inflation elevated in 2023

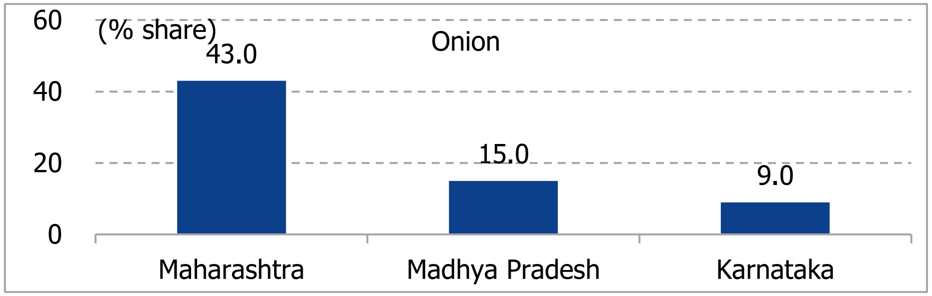
Commodity *(INR/kg, INR/ltr)*	Dec-22	Nov-23	Dec-23	Dec-Nov % MoM	Dec 22 - Dec 23 % YoY	2022	2023	% YoY
Rice	38.0	43.0	43.4	0.9	14.1	36.8	40.6	10.3
Wheat	32.0	33.6	31.1	(7.7)	(2.8)	29.9	32.3	8.0
Tur/Arhar dal	112.0	155.2	154.8	(0.2)	38.3	106.3	131.6	23.8
Moong dal	103.4	116.5	116.5	(0.1)	12.7	102.4	110.1	7.5
Mustard oil	175.5	148.7	137.8	(7.4)	(21.5)	183.4	156.3	(14.8)
Vanaspati	141.1	126.8	125.9	(0.7)	(10.8)	151.0	131.1	(13.2)
Potato	26.0	25.0	24.0	(4.0)	(7.7)	24.7	22.5	(8.9)
Onion	27.6	59.0	50.8	(13.9)	84.2	28.2	31.6	12.3
Tomato	29.6	39.5	38.2	(3.3)	29.1	36.1	42.3	17.5
Milk	55.5	58.4	58.3	(0.2)	5.1	52.3	57.4	9.6
Tea Loose	276.6	279.5	278.6	(0.3)	0.7	283.2	276.7	(2.3)
Salt Pack	21.5	22.4	22.5	0.5	4.5	20.0	22.0	10.3

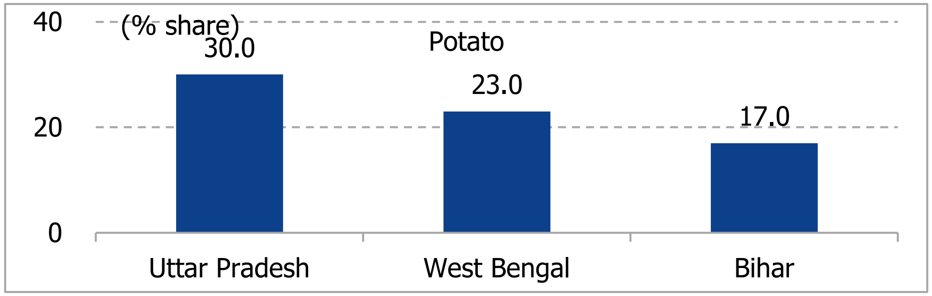
Source: CEIC, Elara Securities Research. Green = prices falling.

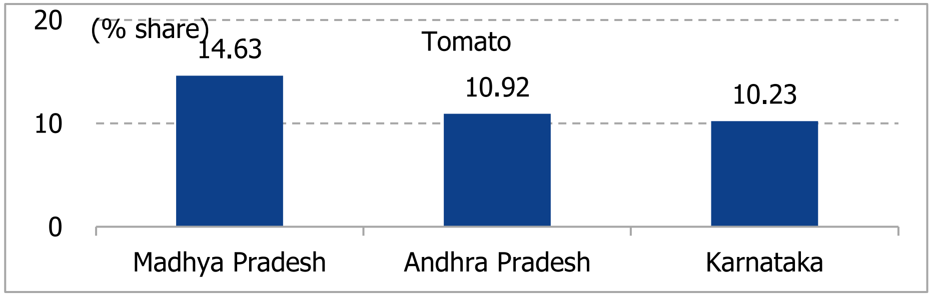
Government focus needs to be on ensuring reduction of supply risks. Even as pulses are imported, for example, recent trade risks need to be monitored.

...owing to climate shocks amid concentrated veggies production

India – Vegetable production concentrated

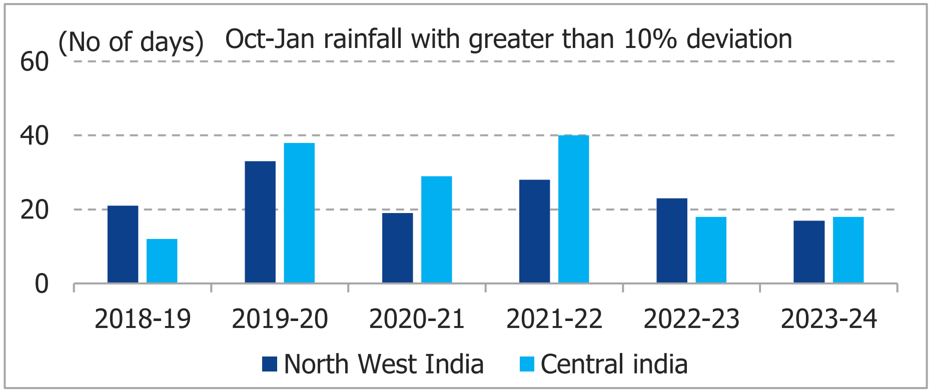






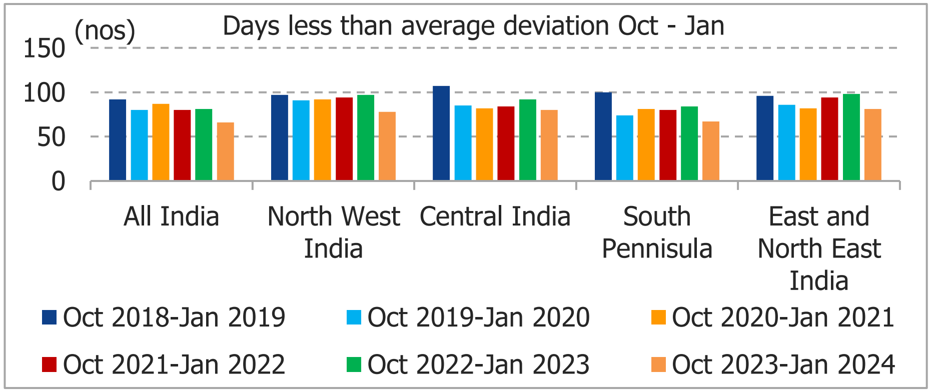
Source: Ministry of Agriculture, Elara Securities Research

Monsoon variability is adding to output swings



Source: CEIC, Elara Securities Research

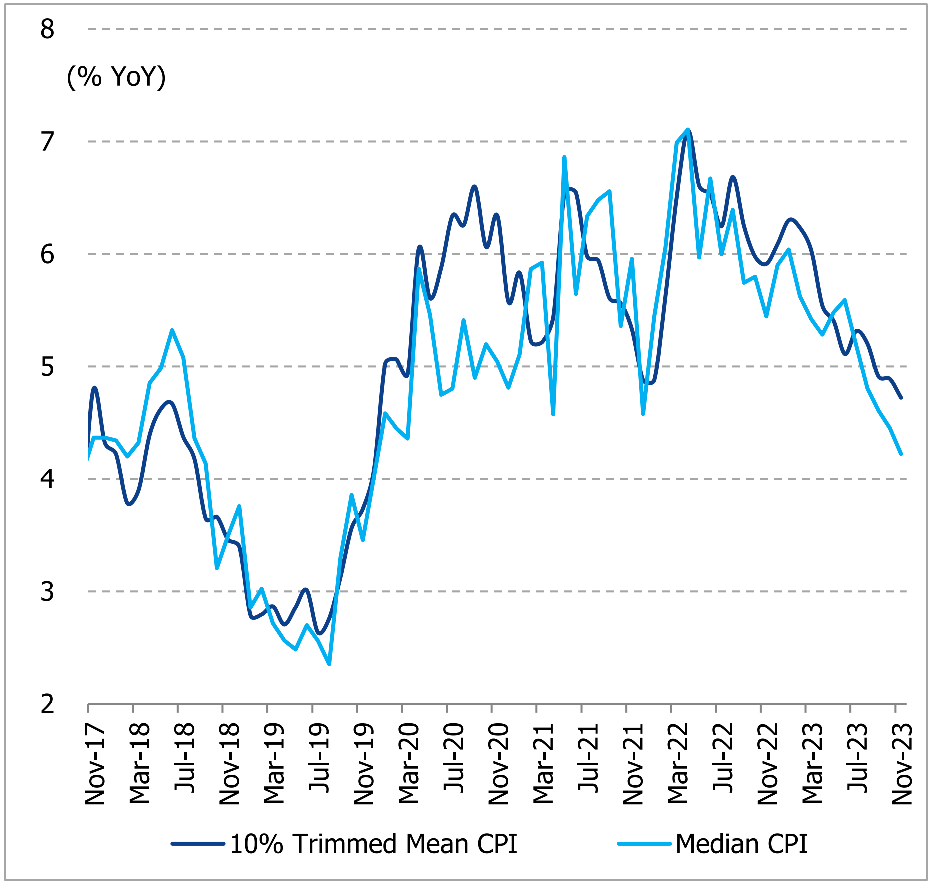
Erratic rainfall risks remain at bay for now



Source: CEIC, Elara Securities Research

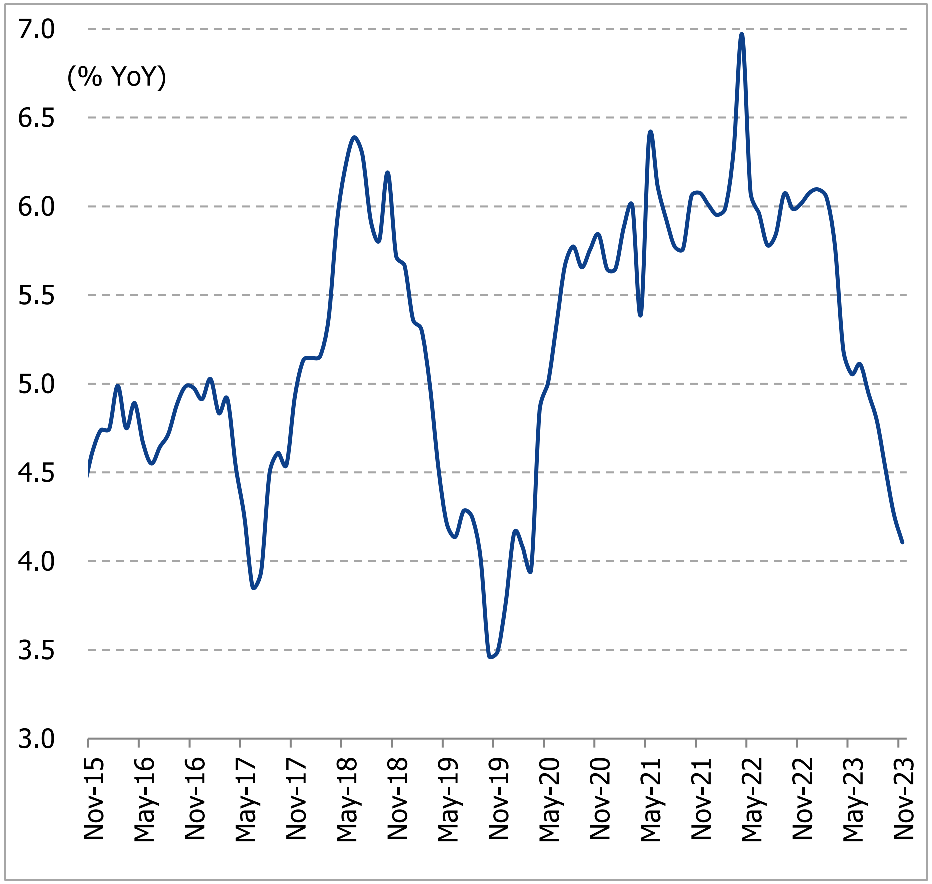
Alternate inflation measures point to moderation

Excluding volatile components, inflation on downtrend



Source: CEIC, Elara Securities Research

Core inflation moderating sharply

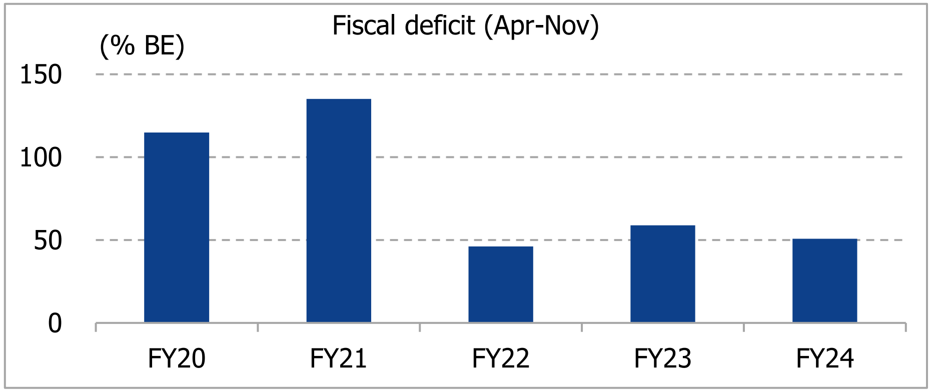


Source: CEIC, Elara Securities Research

INDIA – FISCAL OUTLOOK

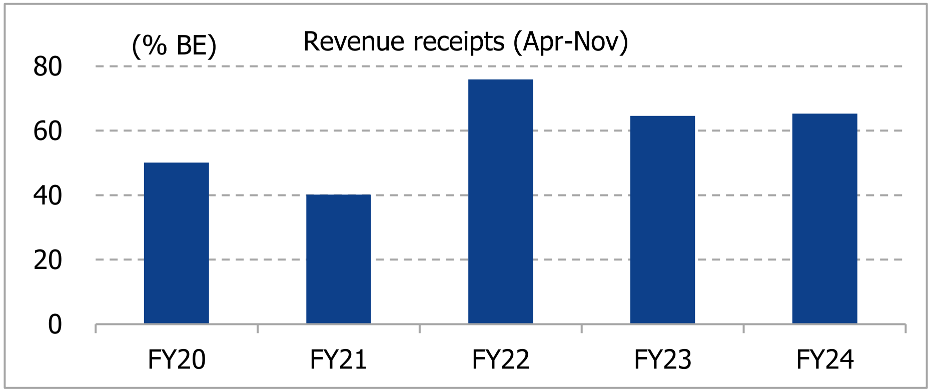
India's fiscal health comfortable

Fiscal deficit remains comfortable



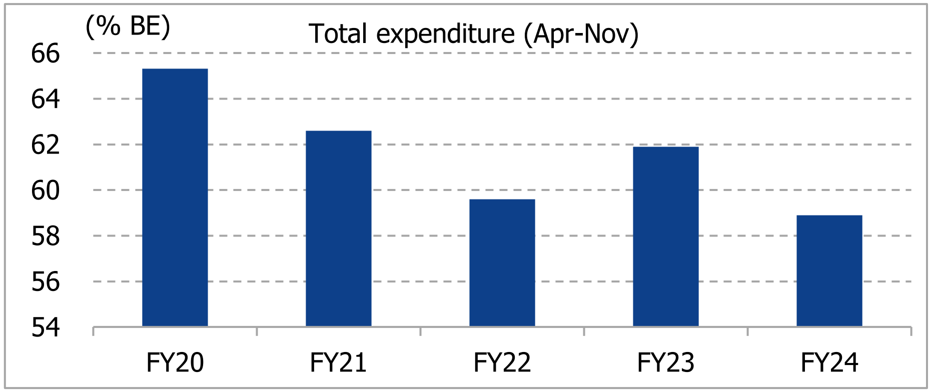
Source: CMIE, Elara Securities Research

Amid surge in revenue receipts...



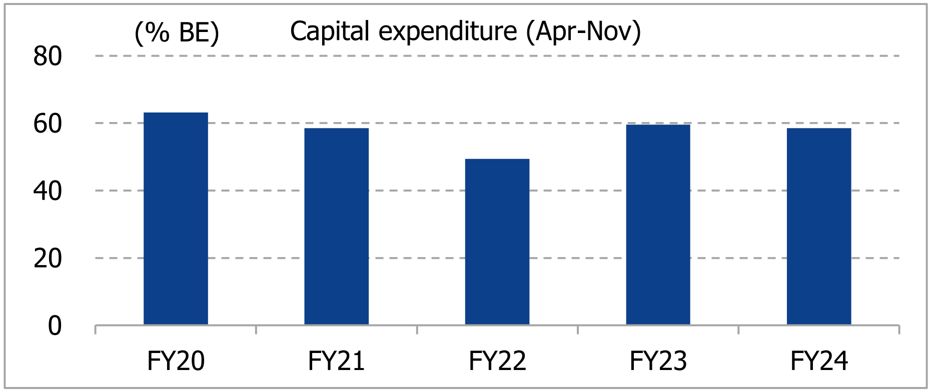
Source: CMIE, Elara Securities Research

...and relatively contained revenue expenditure



Source: CMIE, Elara Securities Research

Capital expenditure on strong footing



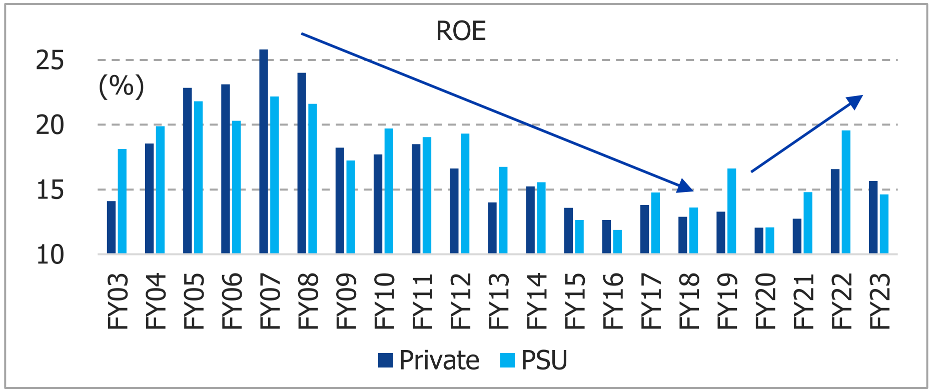
Source: CMIE, Elara Securities Research

FY24 fiscal target to be met; FY26 target may need capex pull-back

- If the current trend of revenue is sustained, we see no fiscal slippage despite the expected shortfall in disinvestment revenue as it would be more than adequately compensated by gains in tax and non-tax revenue
- Higher expenditure (net cash outgo of INR 583.78bn under supplementary demand for grants) can be comfortably managed.
- We anticipate the government to target a fiscal deficit of 5.3% of GDP in FY25E. If the government does not push ahead its glide path, then capital expenditure may see moderated growth.
- However, sustained capex push by the government demands finding newer resources.
- Renewed push for PSU disinvestment especially exiting non-strategic sectors could come in handy.

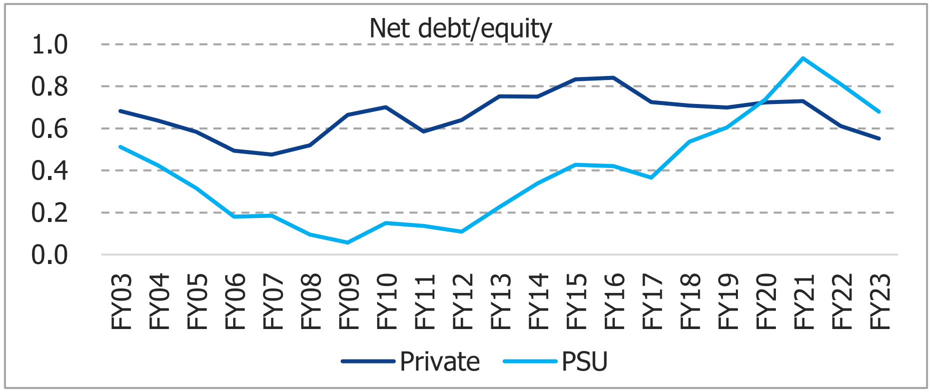
...or new sources of revenue such as renewed push to divestment

PSUs have shown notable improvement in efficiency...



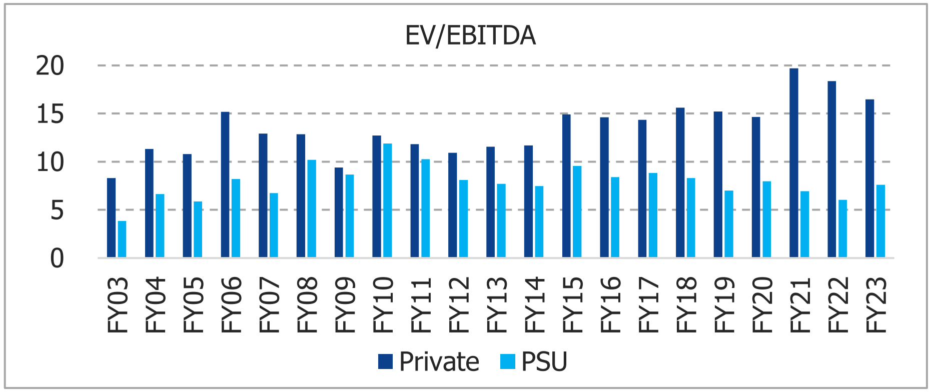
Source: Capitaline, Bloomberg, Elara Securities Research

...as well as effective deleveraging



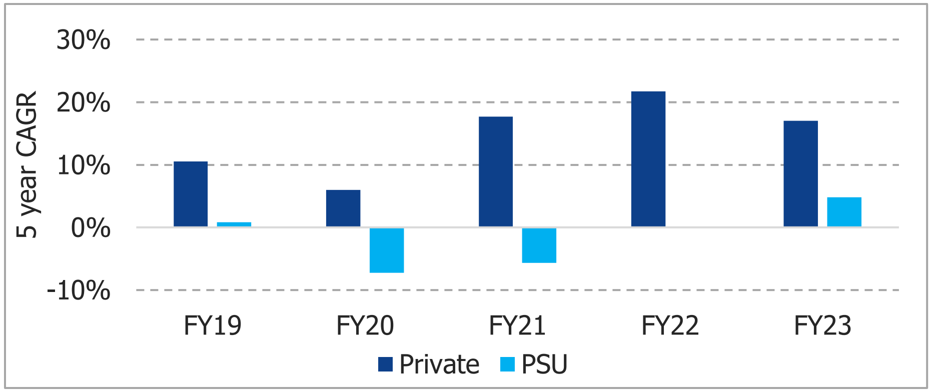
Capitaline, Bloomberg, Elara Securities Research

Despite recent run-up, valuation comfort remains



Capitaline, Bloomberg, Elara Securities Research

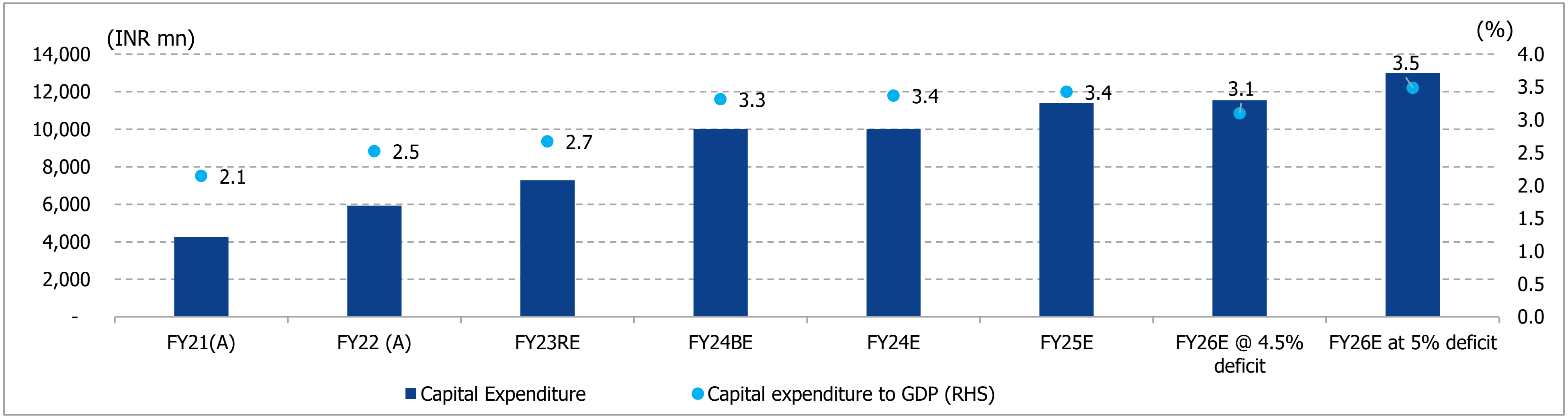
PSUs: Market cap has seen a sharp swing post Covid



Capitaline, Bloomberg, Elara Securities Research

Recommend delaying FRBM target of FY26 by one year

Capital expenditure trajectory

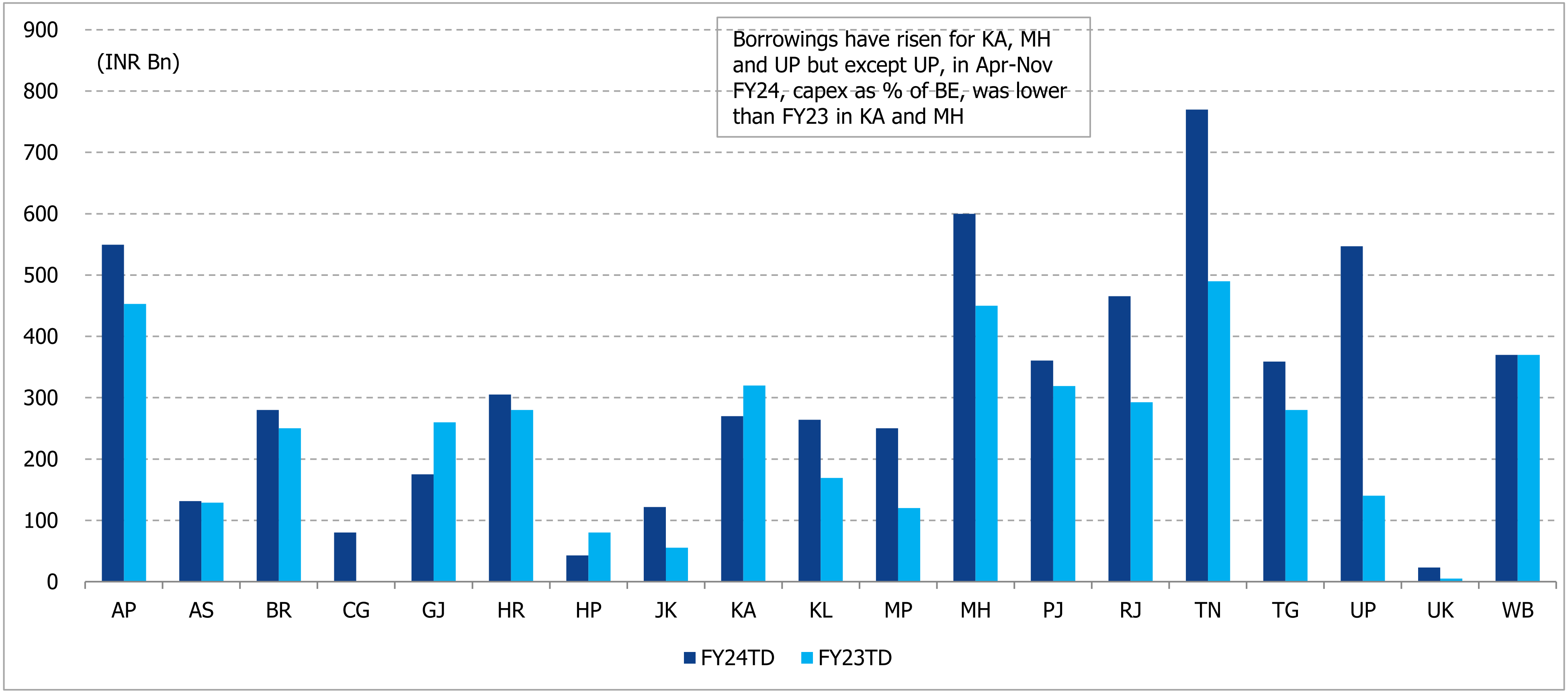


Source: CEIC, Elara Securities Estimate

Policy space for increasing capex may have to narrow down if 4.5% fiscal deficit is to be attained

Most states are borrowing higher than last year...

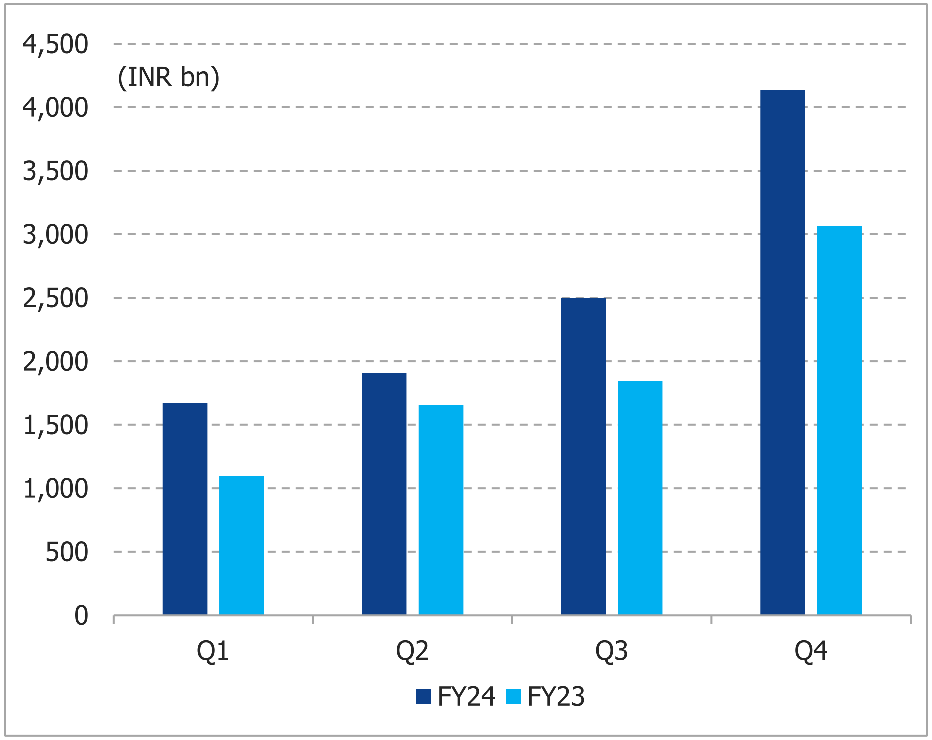
Tamil Nadu, Uttar Pradesh and Maharashtra have borrowed significantly higher in current fiscal year, so far...



Note: (abbreviations) *States includes Andhra Pradesh, Assam, Bihar, Chhattisgarh, Gujarat, Haryana, Himachal Pradesh, Jharkhand, Karnataka, Kerala, Madhya Pradesh, Maharashtra, Odisha, Punjab, Rajasthan, Tamil Nadu, Telangana, Uttar Pradesh, Uttarakhand, West Bengal; Source: RBI, Elara Securities Research

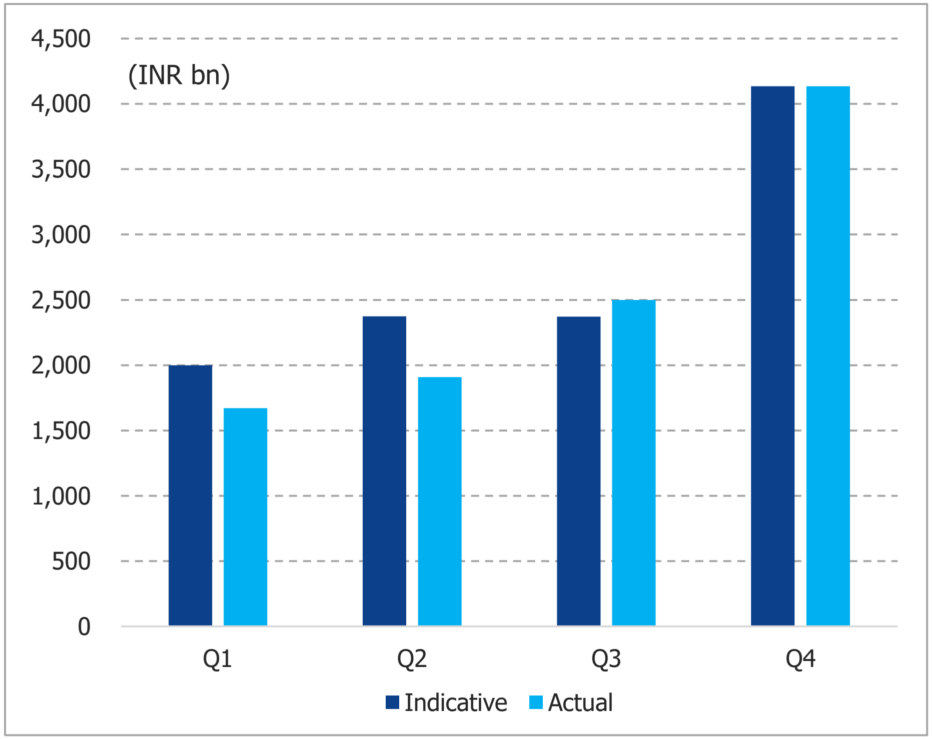
...with supply higher than last year, yet lower than indicative...

Quarterly SDL issuances higher in FY24



Source: CEIC, Elara Securities Research

Actual borrowing is slowly catching up with indicative



Source: CEIC, Elara Securities Research

Despite capex spending uptick, spending may underwhelm in states in FY24E...

India – Fiscal position

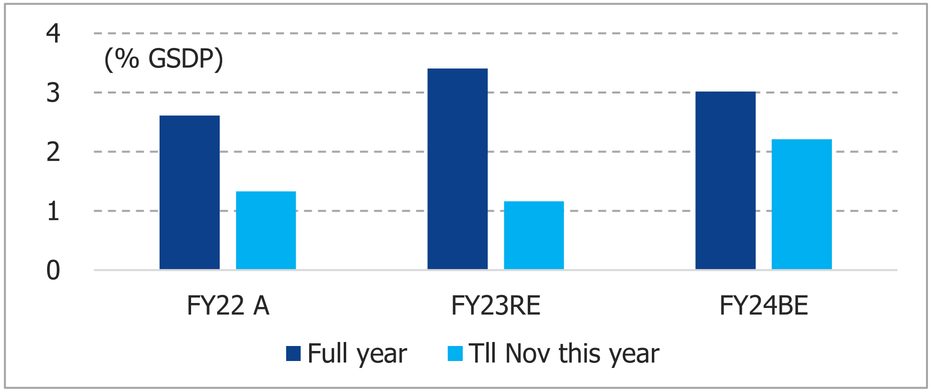
As percentage of GSDP	FY21	FY22	FY23BE	FY23RE	FY23A	FY24BE
Total revenue receipts	12.1	13.5	14.1	14.2	13.1	14.1
(a) Own tax revenue	5.6	6.4	6.6	6.8	10.0	7.1
SGST revenue	2.2	2.5	2.8	2.8	3.1	3.0
(b) Own non-tax revenues	0.8	1.1	1.3	1.1	1.0	1.2
(c) Tax devolution	2.8	3.7	3.3	3.5	3.0	3.4
(d) Grants in aid	2.8	2.3	3.0	2.8	2.1	2.4
Capital receipts	4.9	4.3	4.6	4.9	2.9	4.8
Revenue expenditure	14.0	14.0	14.6	14.8	13.6	14.26
Interest cost	1.9	1.8	1.8	1.8	1.6	1.8
Capital expenditure	3.6	3.8	4.3	4.5	2.2	4.8
Capital outlay	1.9	2.2	2.5	2.6	1.3	2.8
Total expenditure	17.6	17.8	18.9	19.3	15.8	19.0
Revenue deficit	1.8	0.5	0.5	0.7	0.5	0.2
Fiscal deficit	3.81	2.72	3.29	3.48	2.88	3.11
Interest cost as percentage of SOTR	33.8	29.0	27.4	26.3	15.8	24.8
Capex as percentage of fiscal deficit	93.4	140.2	131.0	128.6	76.1	152.8

Source: CEIC, Elara Securities Research

- S-20 spent only 1.3% of GSDP in FY23A versus 2.6% indicated in FY23RE. The best capital outlay in the recent years has been in FY22 at 2.2% of GDP.
- We see serious constraint in the states' ability to spend on capex in FY24BE too.

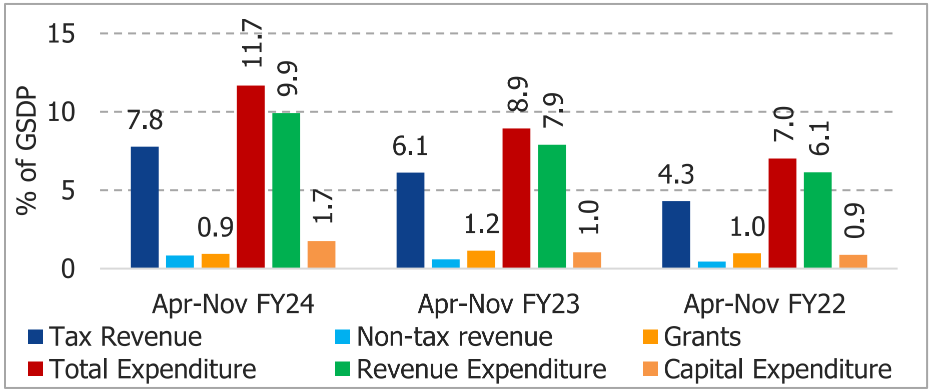
…yet states may end up exhausting the fiscal deficit limit

States' fiscal deficit higher this year…



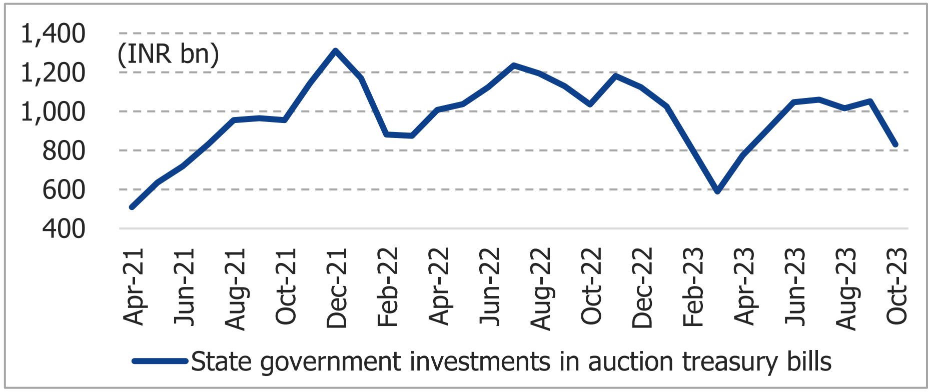
Source: CEIC, Elara Securities Research

…led by higher expenditure



Source: CEIC, Elara Securities Research

…with depleting surpluses

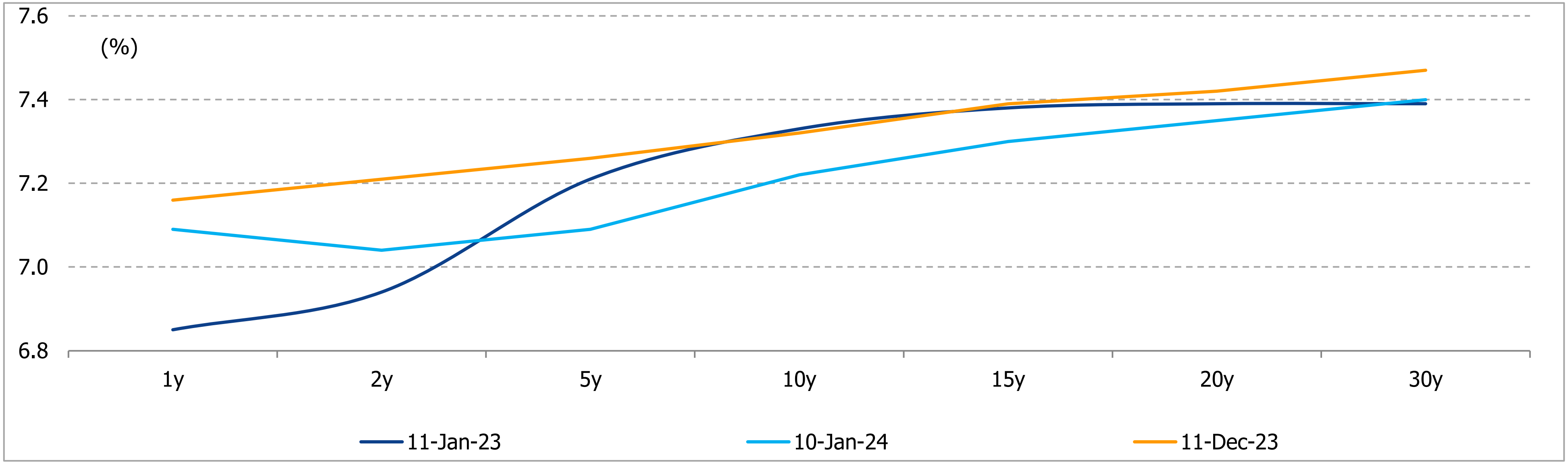


Source: CEIC, Elara Securities Research

- Yet, for a list of 17 states under review, the overall expenditure has been significantly higher, led by higher revenue expenditure.
- Additionally, states such as Maharashtra, Haryana and Rajasthan have announced supplementary demands for extra spending.

India 10-year yield to trade in range of 6.8-7.1% in FY25E

Rising FII debt inflows, political stability, stable currency and dovish Fed aided India's yield curve rally MoM



Source: CEIC, Elara Securities Research

- We except the MPC to cut policy repo rate by 50-75bps for full FY25 starting towards end-Q1FY25E.
- The pivot by the Fed, rate cuts by the MPC receding fears of OMO sales, and continued surge in debt flows amid inclusion in JPM index/other indices may help yields to cool off towards H2FY25.
- We expect 10-year to ease to 6.7-7% by H2FY25E from the current range of 7.1-7.3%.
- Expect yield curve to steepen.

CHAPTER IV

ASSET CLASSES – 2024 OUTLOOK

Fed is the key in 2024; prefer bonds over equities; India alpha source

Equity (30%)

- Prefer US mega tech.
- India, in our view, is the alpha destination in 2024
- Some case of allocation towards China remains in 2024 as PBoC and the government embark on accommodative policies.
- Easing wage growth and steady inflation provides positivity to Japanese equities, helping Nikkei to reach highest since 1990s. If this trend continues, Japan can become attractive.

Bond (50%)

- Fed's rate cuts and potential stoppage in QT create a case for UST duration.
- BoJ's policy normalization is likely to help JGBs. But BoJ needs to come down heavily on inflation.
- Among EM bonds, India scores well in our view due to recent bond index inclusions and overall macro stability.
- Given the risk-reward outlook, overall, preference for a receiver in DM (ex-Japan) rates remains.

FX (15%)

- Negative on EUR and GBP
- Expect USD (DXY Index) to trade with downside bias and average 101 for full 2024E.
- We see case building for long USD-JPY emerging with rates moving opposite way in the US and Japan in 2024.
- We see Bitcoins as attractive bets at the back of green light on spot ETFs.

Commodities (5%)

- We do not see much upside to crude and see it hovering at USD 75-85/bl in 2024E.
- We expect incremental demand for gold to rotate towards Bitcoin since spot ETFs are approved by SEC.
- Base metals price to remain benign as demand uncertainties persist. Liquidity may aid at the margin.
- Unless weather shocks are deep and consistent, do not expect global food prices to rise.

Note: Percentage in brackets indicate possible allocation/preference for each asset classes and are for representation purpose only.

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