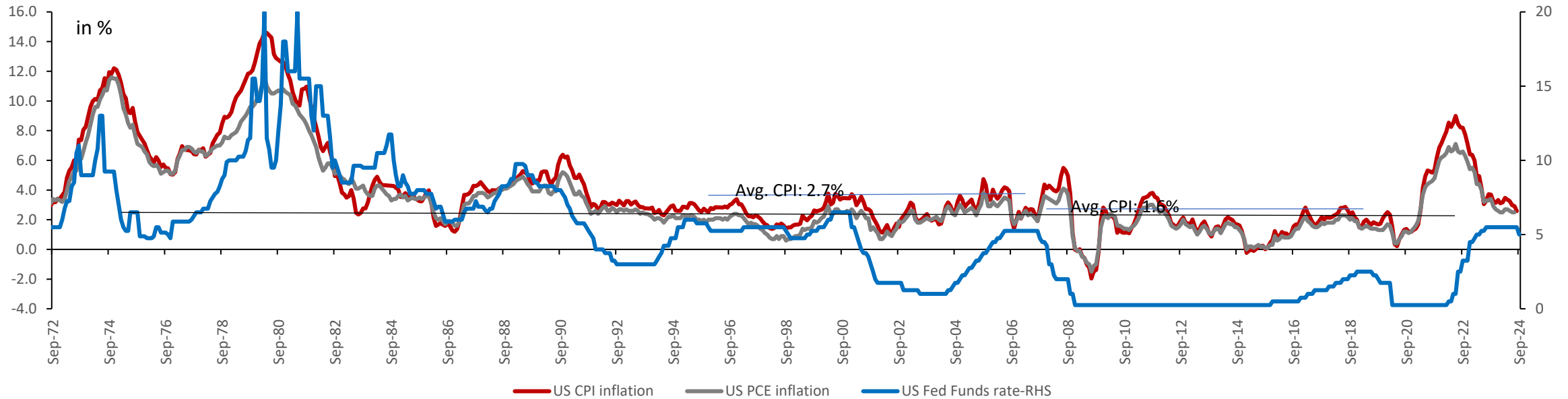


# ECONOMY AND MARKETS

October 2024

# Federal reserve cuts Fed funds rate by 50bps to 4.75-5.00% in September 2024

## US Fed funds rate sees a much-anticipated 50bps cut in Sep'24



- On September 18, the US Federal Reserve started its rate-cutting cycle. It reduced the Fed Funds rate by 50 basis points, bringing it down from 5.25-5.50% to 4.75-5.00%.
- Fed Chair Jerome Powell noted that the labor market has cooled, no longer serving as a major inflationary factor.
- Another key notable is that the Fed has acted before reaching its inflation target of 2%, indicating a willingness to ease as long as disinflation towards this target remains plausible, potentially by 2026.
- This shift means that 2% PCE inflation is now viewed as a floor rather than a ceiling, suggesting average inflation in the coming years could settle around 2.5% to 3%.

# Summary of economic projections by the US Fed

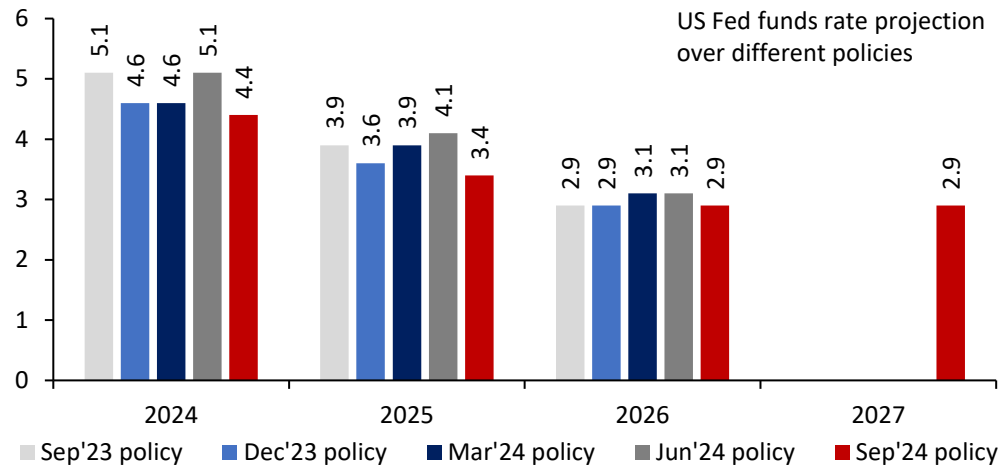
## Projects an additional 50bps cut over the next two policies in 2024

Variable	Median <sup>1</sup>					Central Tendency <sup>2</sup>					2024
	2024	2025	2026	2027	Longer run	2024	2025	2026	2027	Longer run	
Change in real GDP	2.0	2.0	2.0	2.0	1.8	1.9–2.1	1.8–2.2	1.9–2.3	1.8–2.1	1.7–2.0	1.8–2.6
June projection	2.1	2.0	2.0		1.8	1.9–2.3	1.8–2.2	1.8–2.1		1.7–2.0	1.4–2.7
Unemployment rate	4.4	4.4	4.3	4.2	4.2	4.3–4.4	4.2–4.5	4.0–4.4	4.0–4.4	3.9–4.3	4.2–4.5
June projection	4.0	4.2	4.1		4.2	4.0–4.1	3.9–4.2	3.9–4.3		3.9–4.3	3.8–4.4
PCE inflation	2.3	2.1	2.0	2.0	2.0	2.2–2.4	2.1–2.2	2.0	2.0	2.0	2.1–2.7
June projection	2.6	2.3	2.0		2.0	2.5–2.9	2.2–2.4	2.0–2.1		2.0	2.5–3.0
Core PCE inflation <sup>4</sup>	2.6	2.2	2.0	2.0		2.6–2.7	2.1–2.3	2.0	2.0		2.4–2.9
June projection	2.8	2.3	2.0			2.8–3.0	2.3–2.4	2.0–2.1			2.7–3.2
Memo: Projected appropriate policy path											
Federal funds rate	4.4	3.4	2.9	2.9	2.9	4.4–4.6	3.1–3.6	2.6–3.6	2.6–3.6	2.5–3.5	4.1–4.9
June projection	5.1	4.1	3.1		2.8	4.9–5.4	3.9–4.4	2.9–3.6		2.5–3.5	4.9–5.4

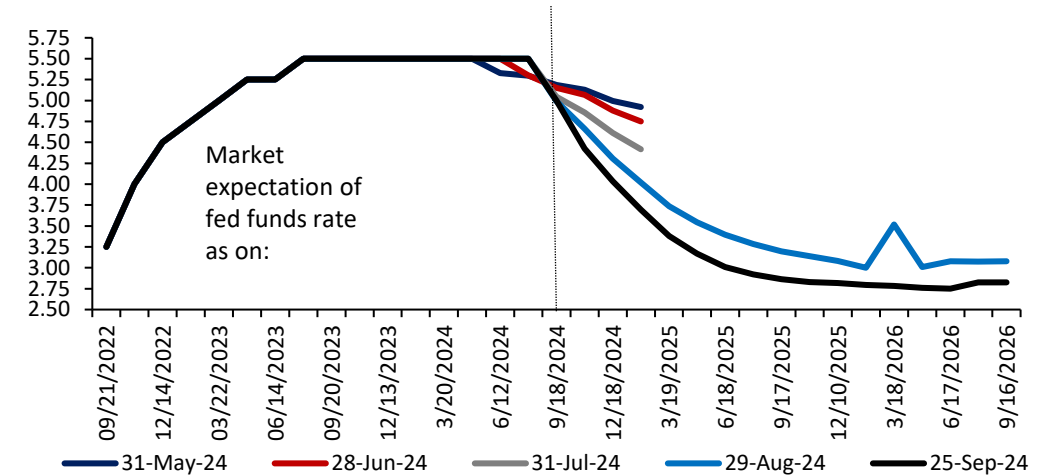
- Summary of Economic Projections (SEP) projects US growth at 2% - in line with the run-rate observed in last eight quarters, unemployment rate to move up to 4.4% (from current 4.2% in August) and PCE inflation to moderate to an average of 2.3%, 2.1% and 2% by 2024, 2025 and 2026 respectively.
- They project to deliver an additional 50bps cut over next two policy in 2024, followed by 100bps in 2025 and 50bps in 2026 taking the terminal Fed Funds rate to 2.9%.
- The messaging in the latest monetary policy appears inconsistent.
- The Fed projects US growth at 2%, aligning with recent trends, while expecting only a slight rise in unemployment to 4.4%, still below their NAIRU (Nonaccelerating inflation rate of Unemployment) estimate.
- They have also raised the long-term neutral rate projection by 10 basis points to 2.9%.
- Notably, 9 of 16 Fed members predict no further rate cuts in 2024, and one member dissented on the 50-basis point cut—a rarity for the Fed.
- Yet, we saw a 50bps cut, with an impression that Fed has been behind the curve.

# Market expects rate cutting cycle to be over in a year; Fed guides cut to be staggered till 2026

Dot plot suggests 250bps rate cut by 2026



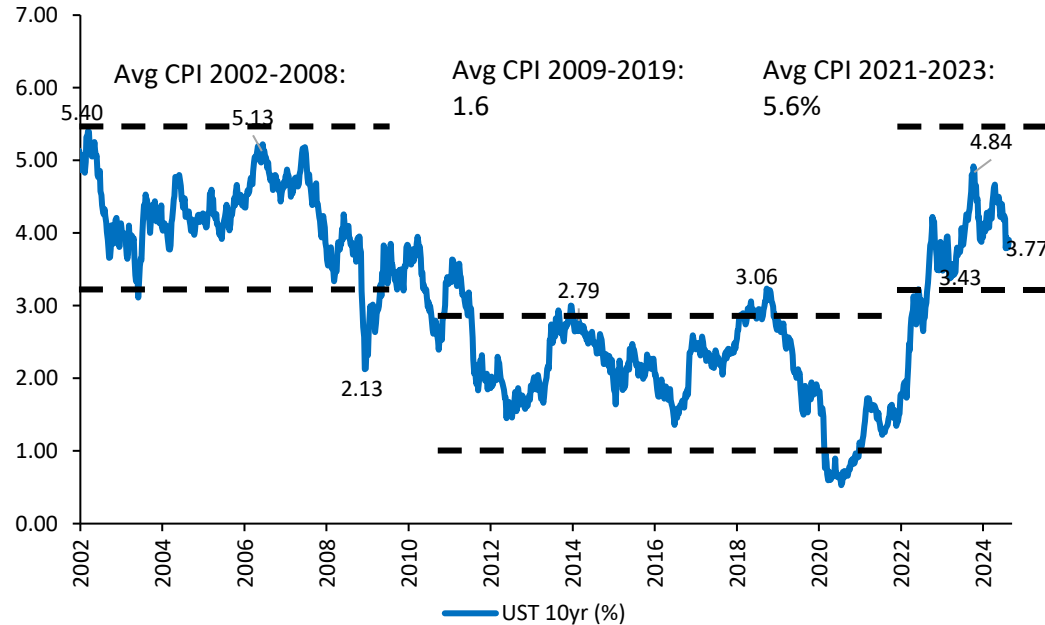
Market expectation points towards 250bps rate cut in the span of one year



- The dot plots for 2024 have been volatile, undermining the reliability of forward guidance, leaving the market data-dependent but uncertain.
- The bottom-line is that currently stated rate path is not a given.
- Market expects a more aggressive rate cutting cycle with 250bps cut in a year vs. fed projection of 250bps rate cut by 2026.
- As monetary easing has just begun, it's worth noting historical instances where markets anticipated significant rate cuts that ultimately didn't materialize—specifically in 1995 and 1998. However, there have also been times when cuts exceeded expectations.

# US sovereign yield curve sees bull steepening on monetary easing

Structural factors suggest a likely yield range of 3.5-5.5%; near term further fall in yield cannot be ruled out



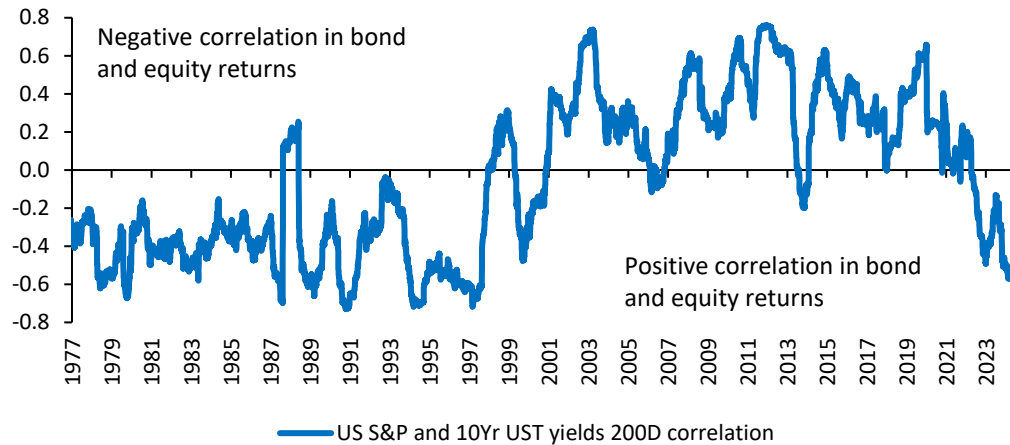
The yield curve inversion ended in August 2024; curve steepens



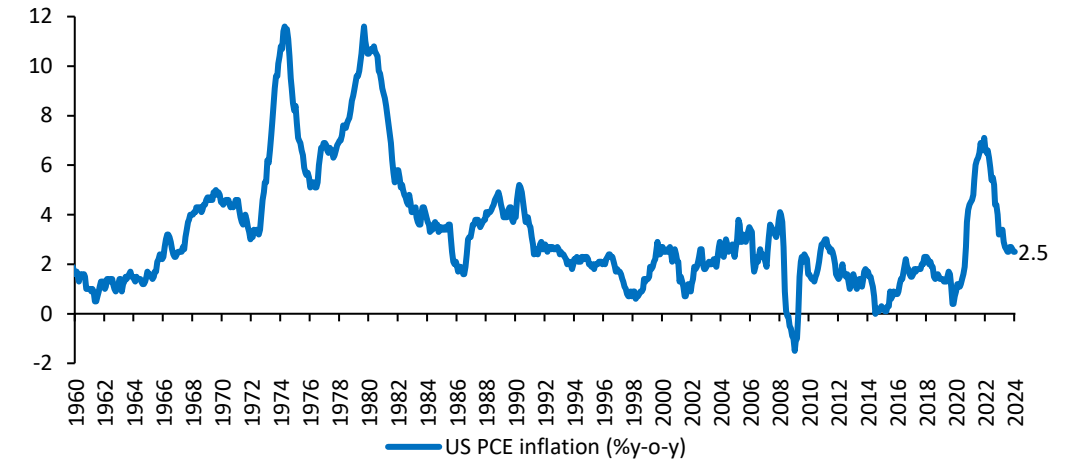
- Multiple data suggest that our long-standing comfortable range of 10 UST at 3.5-5.5% still holds true. Thus, with 10-year UST at 3.7%, most of the gain is already in the price.
- It's essential to distinguish between cyclical and structural influences on yields. The growing fiscal deficit presents a structural risk for inflation, compounded by potential tax cuts or increased public spending depending on the outcome of the upcoming elections.
- Currently, the bond market is experiencing curve steepening, with long-term bonds selling off and equities rising, reviving the negative correlation between the two. This shift could be attributed to inflation settling below 3%.

# Restoration of negative correlation between bond and equity is a cyclical positive for US bonds

Restoration on negative correlation between bond and equity are a cyclical positive for bonds, even as structural headwinds remain



Inflation print is below 3% consistently in 2024

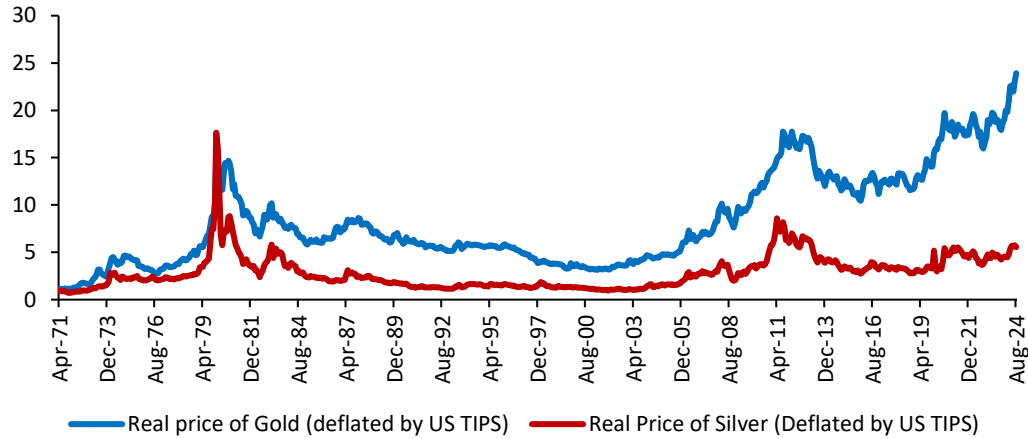


Cyclically risk of election outcome: If Trump comes it is bond negative as he would cut corporate taxes at a time when fiscal deficit is high

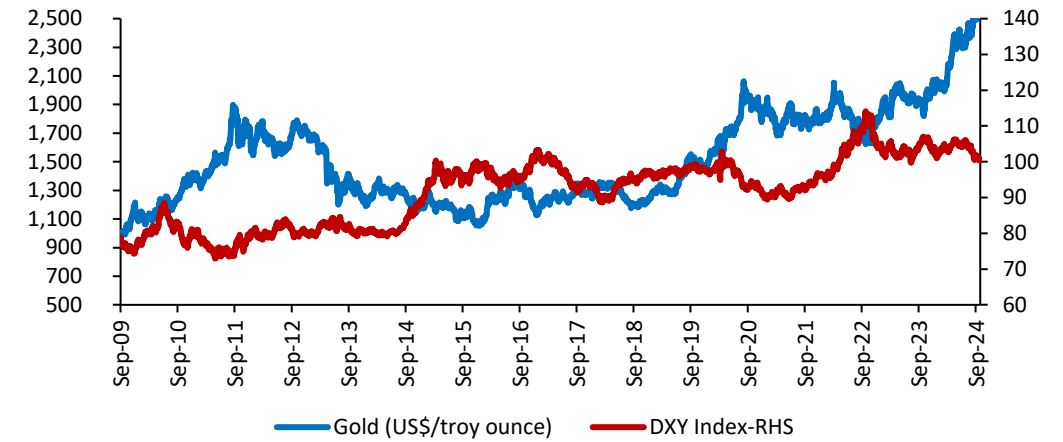
	Democratic policy and beneficiaries	Republican policy and beneficiaries
US corporate tax rate policy	Increase to 28%: benefits stocks with direct US competitors <i>Taiwan, Korea, Japan, Mexico</i>	Decrease to as low as 15%: Benefits stocks with significant US operations <i>Australia, India</i>
US import tariffs	No incremental tariffs, nor changes to tariffs/export controls <i>China, Taiwan, Korea, Japan</i>	60% on China, 10% on rest of the world <i>(less affected): Saudi, Poland, Indonesia, Philippines</i>
Focus on climate initiatives	Continued focus on initiatives like IRA <i>South Africa, Indonesia, Taiwan</i>	Reduction of fiscal support to climate initiatives; maximise oil production <i>Malaysia, Singapore, Mexico</i>
USD intervention	No active intervention <i>Korea, Taiwan, Japan</i>	Actively devalue <i>Indonesia, Hong Kong, Brazil</i>
Higher global defense spending	US stays actively engaged in global geopolitics; supports allies <i>n/a</i>	US isolationism to benefit defense stocks globally <i>Japan, India, Korea</i>

# We recommend to stay invested in precious metals despite stretched valuations

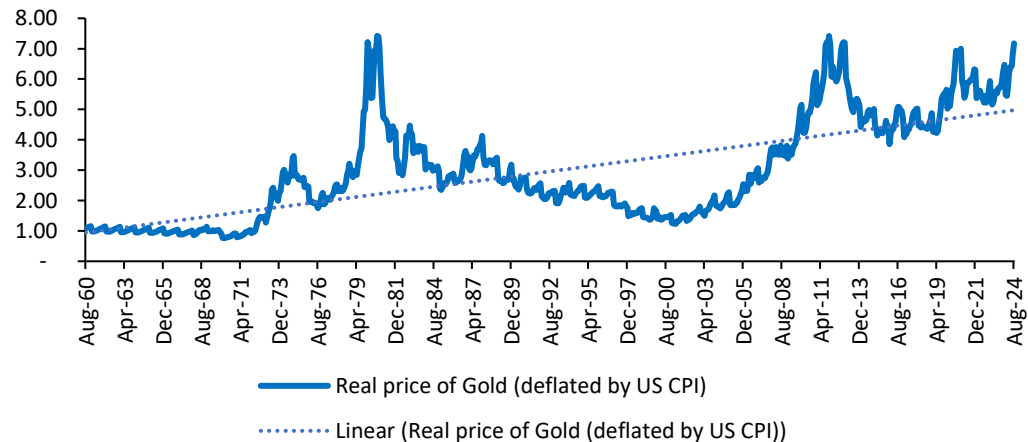
Recent rise in Gold price is in line with slight moderation in US real yields..



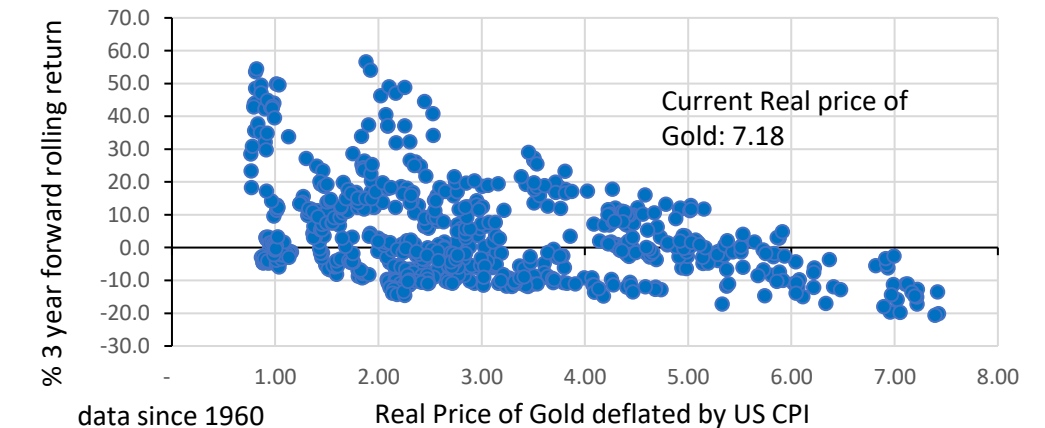
... and softening of US dollar in August and September



Valuation of gold is high vis-à-vis its history

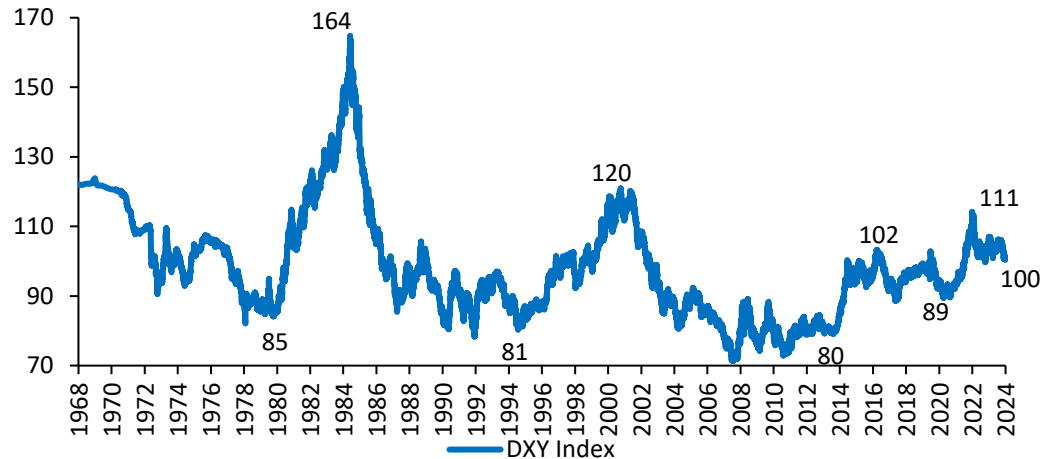


Gold valuations high compared to past trends; Yet we continue to prefer the asset as a portfolio diversifier



# We expect dollar to stay sideways in the near term

**Dollar see an offsetting forces of easy monetary policy but weaker growth outside the US**

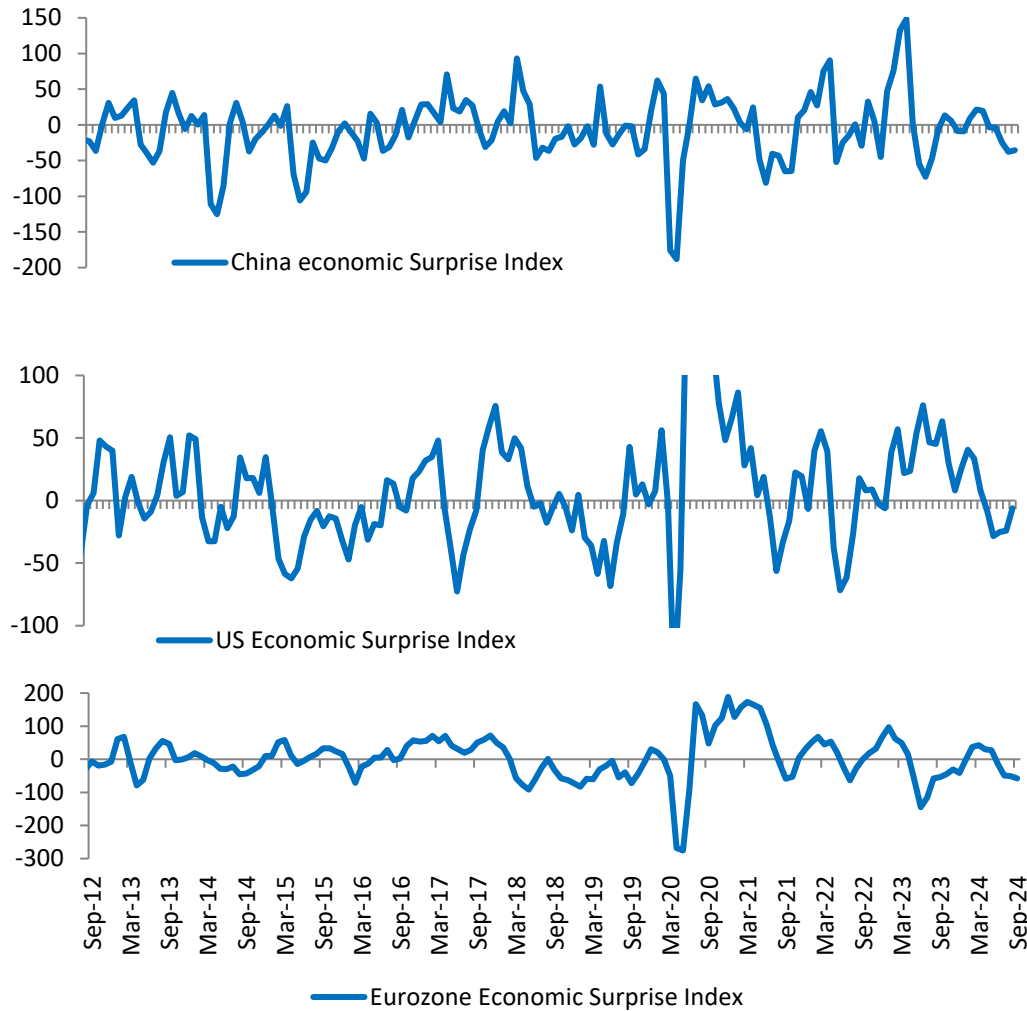


- Regarding the dollar, US monetary easing typically weakens the currency.
- Another factor required for a strong dollar depreciation is better growth outlook outside the US.
- However, during this cycle, global growth appears weak, particularly in China and Germany, which complicates the situation.
- Further, a weakening dollar usually leads to stronger global equity performance, the Fed's support for US equities may counter this trend, suggesting a sideways movement for the dollar in the near term.

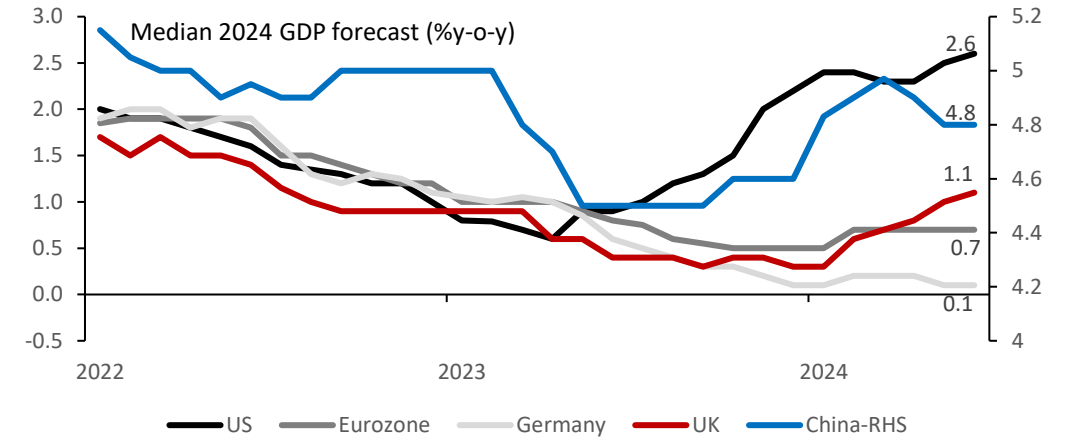


# Global activity momentum has softened and underwhelming expectations across continents

## US, Eurozone and China see softer economic data in September...



## 2024 growth expectations are getting revised down for everywhere except the US



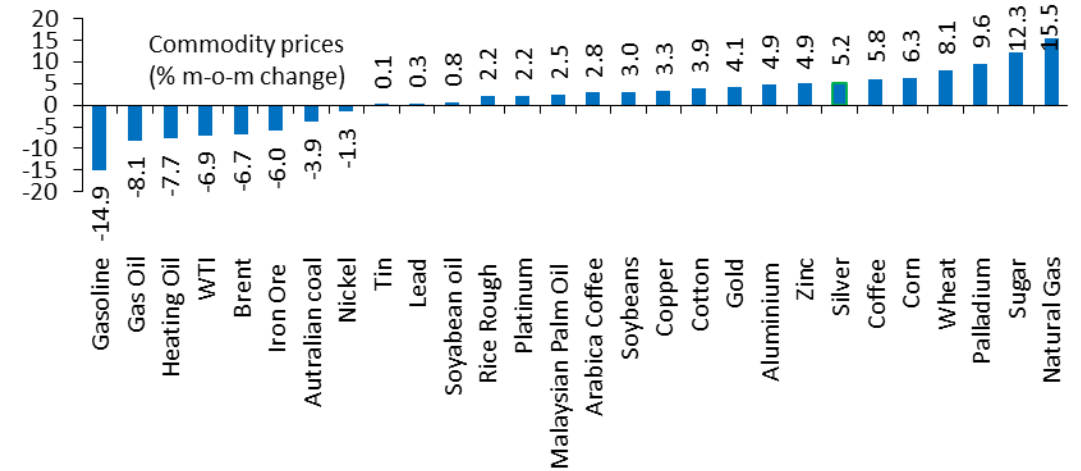
- Many economic indicators out of the US and other developed economies have come in lower than expected lately, and the big revision to US payrolls data showed that the job market has cooled significantly.
- Nevertheless, hard evidence that the US is facing an impending recession remains scanty.
- The US economy is likely to slow over the next six months. However, the base case picture is that growth will remain modestly positive, with the US avoiding a recession in the near term.
- While arguably this is good news, wider global growth is unlikely to hold up well as the US slows. Other economies are poorly placed to take up the growth baton.

# Commodities gain in September on Fed monetary easing and Chinese stimulus

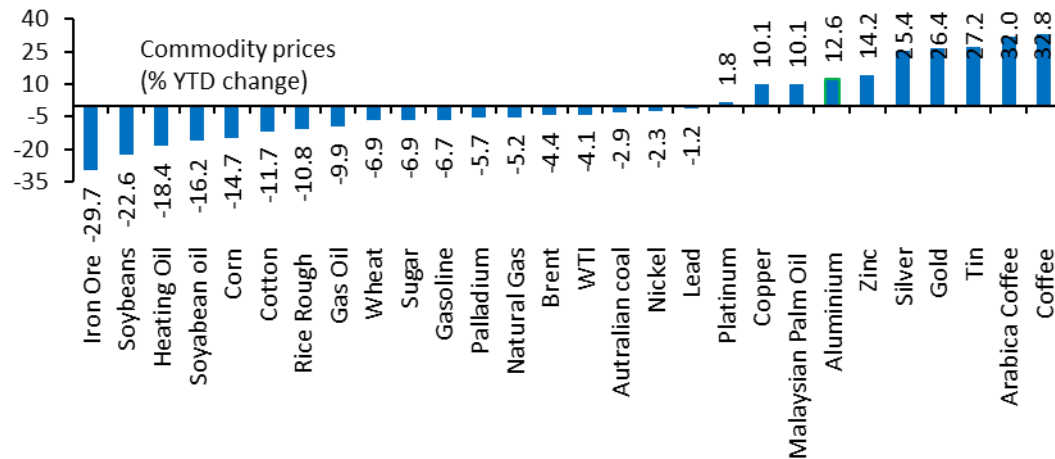
**Bloomberg commodity index rises m-o-m in September 2024**



**On a m-o-m basis, majority of the commodities see an upward movement; Select prices moderated**



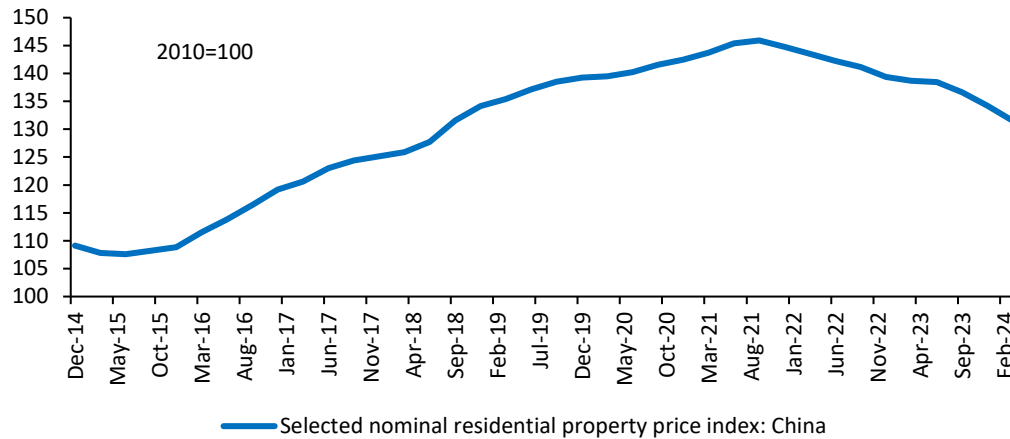
**On a YTD basis, precious metal prices have risen; while select food and energy have seen a moderation**



- Bloomberg commodity index rose by ~4.3% m-o-m.
- Select metal prices continue to be elevated. Silver gained 5%, and copper 3% m-o-m. Gold rose 4% (m-o-m) in September but has risen 26% YTD.
- Multiple factors could explain better return in commodities. Even as recent activity data has softened in the US, economic activity is humming fine in the region.
- In the medium term, commodities could benefit from inflation, decarbonization, deglobalization, rapid adoption of artificial intelligence and data centers.

# Chinese growth continues to struggle; strong support needed to stabilize growth

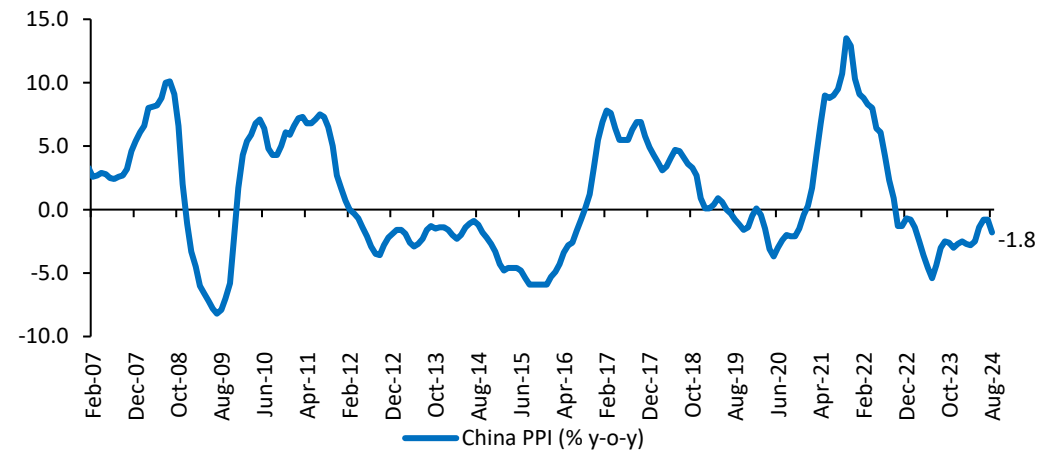
## China residential property prices retraced to 2018 levels



## Consumer confidence severely low in China



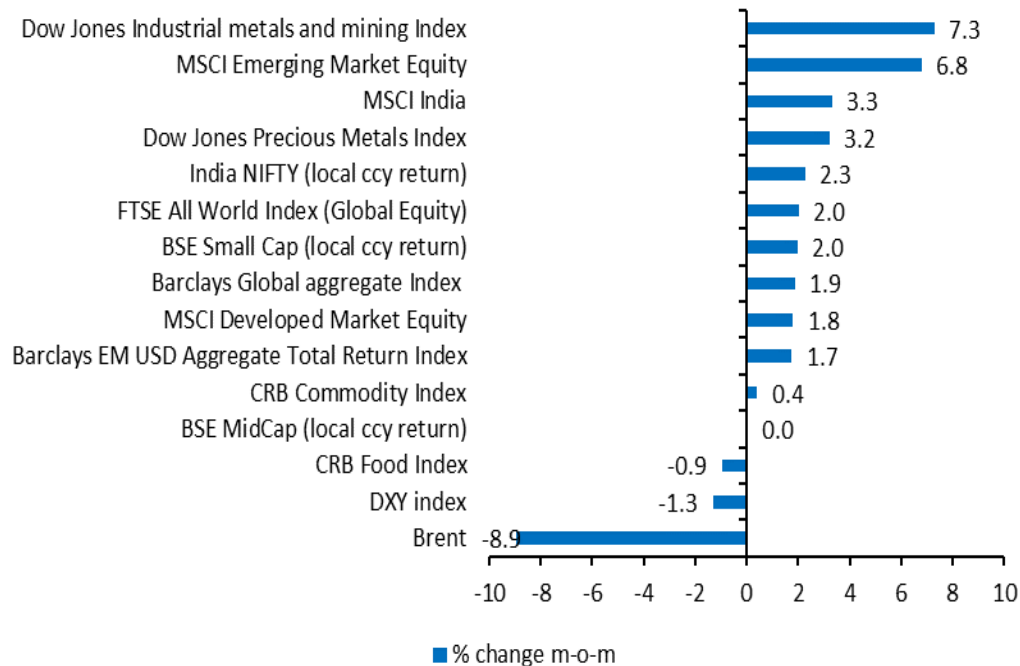
## China continues to cut prices and push exports at a cheaper price



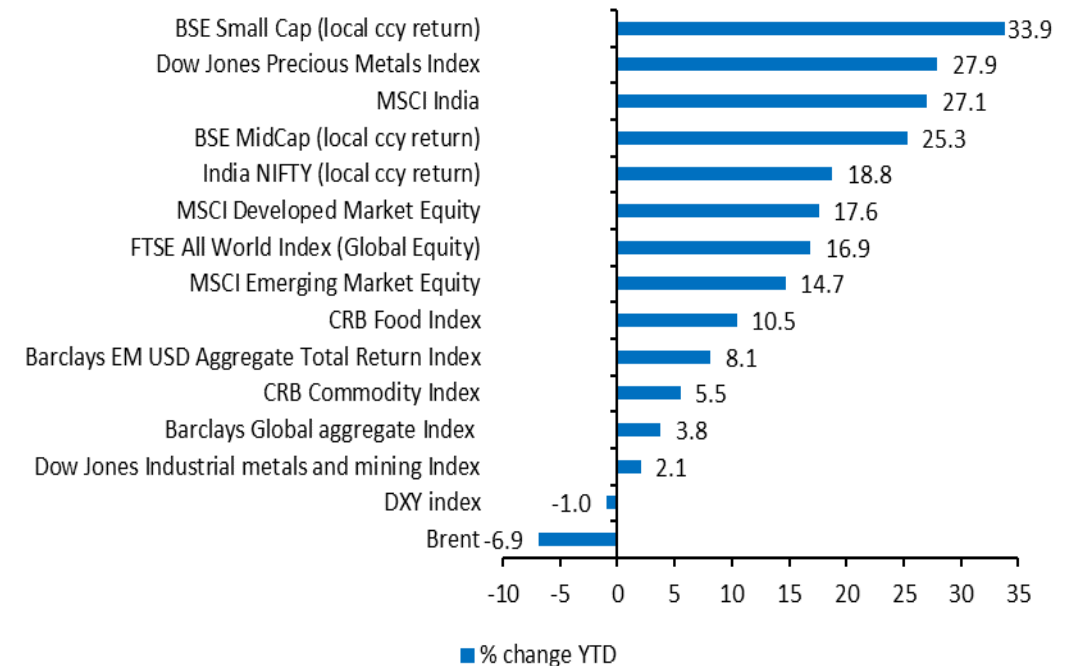
- Last month saw a few more cuts in rates and a measure by China's central bank to support the stock market by creating new instruments to offer funds both to companies making stock buybacks, and to institutional investors in need of liquidity. There were measures to reprice the existing mortgage and lower the downpayment for second home purchases.
- Markets reacted positively, but whether the support to markets lasts depends less on sentiment and more on whether policymakers can turn around the trend of decelerating nominal growth. On current trends, nominal GDP growth could slip below 4% in Q2.
- Decline in real-estate investment unfolds while industrial policy to boost manufacturing investment gets promoted. There is capacity underutilization in some industrial sectors leading them to compete and cut prices and push exports at cheaper prices. This is a risk to multiple sectors in Indian manufacturing space.

# Industrial metals & EM equities rallies in September; YTD precious metals & developed market equity out-performs

## Gold rose, dollar and brent weakened; Indian assets remain unaffected



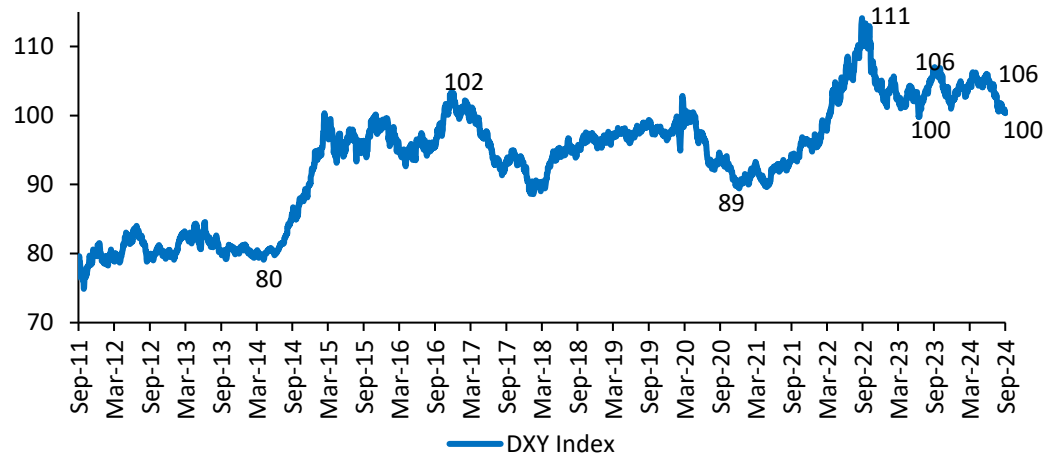
## Year-to-Date; precious metals is the best forming asset; dollar and industrial metals is the weakest



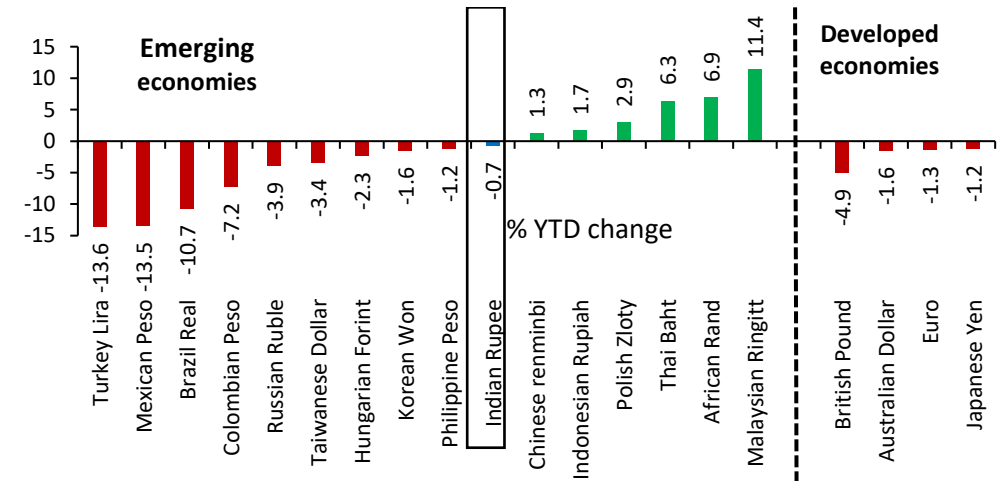
Source: Bloomberg, SBIFM Research; NB: Barclays global aggregate index includes treasury, government related, corporate and securitized fixed rate bonds from both developed and emerging ,market issuers, Barclays EM USD Aggregate total return index includes USD-denominated debt from sovereign, quasi-sovereign, and corporate EM issuers.

# DXY could stay sideways in the near-term; monetary easing offset by weaker global growth

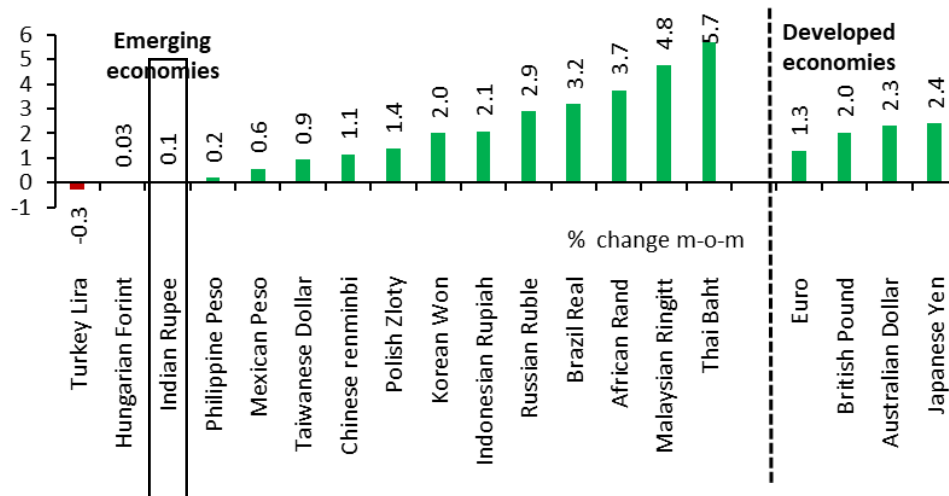
DXY moderates m-o-m by 1%; broadly flat YTD



Majority currencies depreciate against greenback YTD, Rupee's move most contained



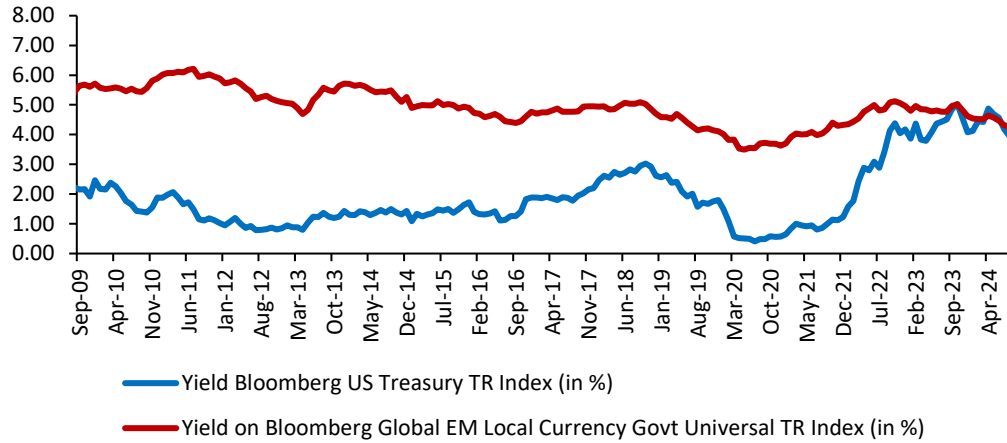
Weakening of the dollar index m-o-m drives appreciation across most emerging and developing market currencies in August



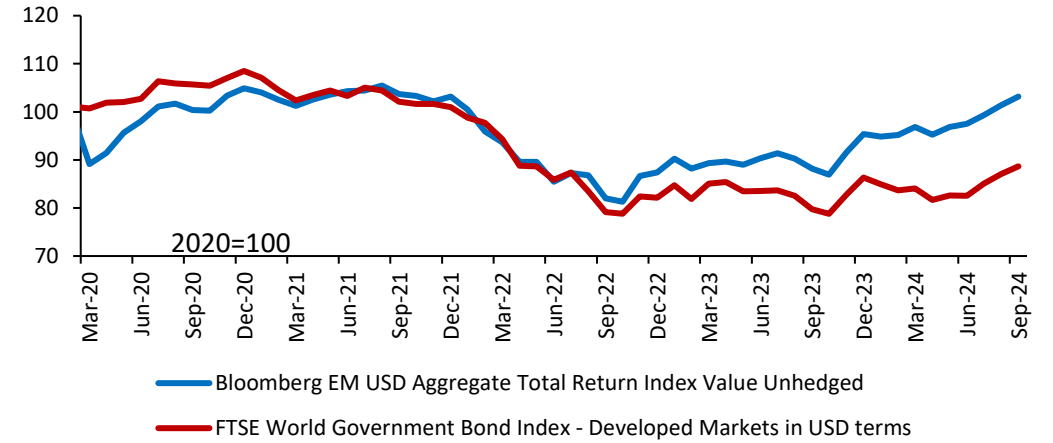
- DXY moderated by 1.3% m-o-m in September.
- While the Fed rate cut makes a case for weaker dollar, weaker global growth works in a counter fashion.
- In the very near term, it is the political developments that are dictating dollar moves. All the election promises by both the parties are working against the US dollar.
- Beyond the election, we expect the US dollar to remain sideways.

# Emerging market bonds erase risk premium; Monetary easing in the US will favour FII flows

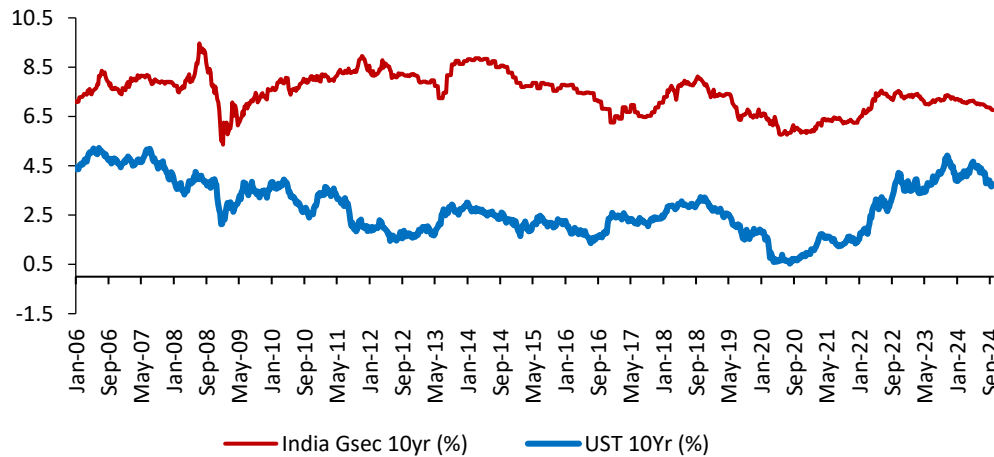
## Spread between EM bond yields and UST yields at low levels



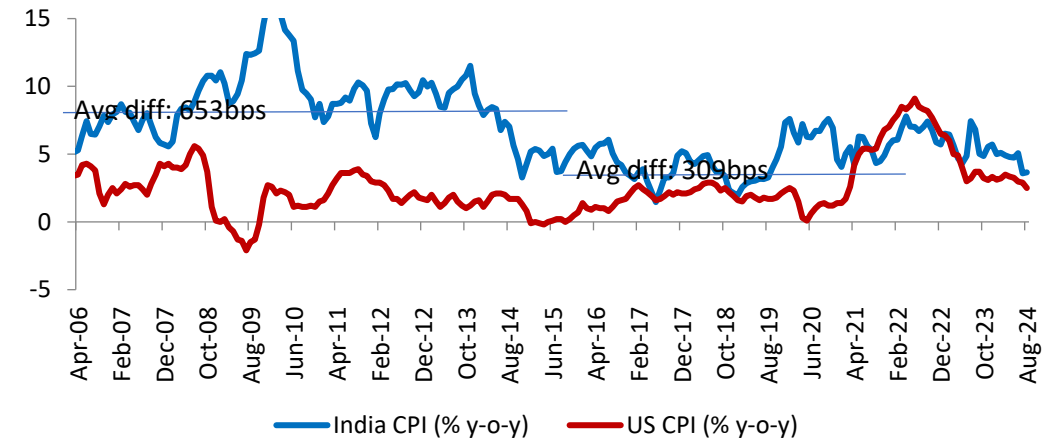
## EM bonds outperform



## India vs. US 10yr bond yield differential is low



## India sees reduced inflation differential vis-à-vis US



# INDIA ECONOMIC ACTIVITY

# Economic activity moderates in Q2 FY25

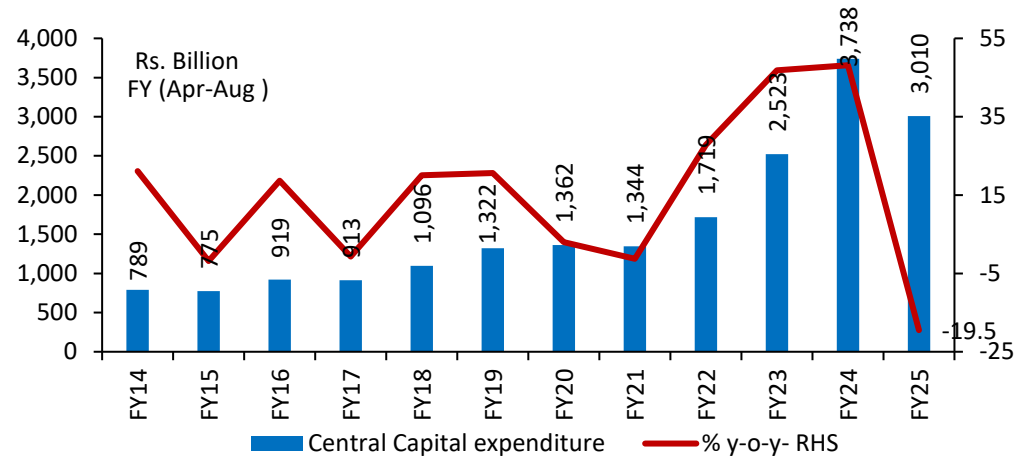
%y-o-y	Aug-23	Sep-23	Oct-23	Nov-23	Dec-23	Jan-24	Feb-24	Mar-24	Apr-24	May-24	Jun-24	Jul-24	Aug-24
<b>Macro indicators</b>													
Bank credit deflated by WPI	20	20	20	20	19	20	20	20	18	18	14	12	12
GST Deflated by WPI manufacturing	13	11	14	16	11	13	14	12	13	9	6	9	9
Consumption of petroleum products	8	8	5	-2	4	7	8	2	8	2	2	8	-3
Electricity generation	19	13	25	11	5	7	8	8	10	15	9	8	-5
<b>Urban Consumption demand</b>													
Domestic air traffic	24	19	11	9	8	5	6	5	4	6	7	8	7
Domestic sale of passenger Cars	-10	-22	-8	-21	-28	-8	-18	-9	-23	-11	-14	-12	-19
Naukri Job Speak Index	-6	-9	1	-23	-16	-11	-8	-11	-3	-2	-8	12	-3
Payments via digital means	42	36	38	43	39	1	43	27	35	33	34	31	27
Urban Consumer sentiment Index	92	95	99	99	101	101	100	100	98	100	105	105	103
<b>Rural Consumption demand</b>													
Domestic Tractor sales	-4	-16	-5	1	-21	-14	-26	-20	-3	1	3	1	-5
Real rural wage	0	1	1	0	0	1	1	1	0	0	-1	1	na
Domestic sale of two-wheelers	1	1	20	31	16	26	35	15	31	10	21	12	9
Rural Consumer sentiment Index	96	104	106	107	109	107	107	108	117	118	112	115	111
<b>Business indicators</b>													
Cargo traffic - rails	6	7	8	4	6	6	10	8	1	4	10	5	-5
Cement production	20	5	17	-5	4	4	8	11	0	-1	2	5	na
Steel consumption	19	19	14	15	7	4	13	11	11	12	21	14	10
Sale of CV	na	4	na	na	3	na	na	-4	na	na	4	na	na
Bank industrial credit deflated by WPI	6	7	6	6	7	8	9	8	6	7	5	8	na
<b>External Sector indicator</b>													
Cargo traffic - ports	4	0	14	17	1	3	2	4	5	4	7	6	7
Merchandise exports	3	-3	6	-3	1	4	12	-1	2	13	2	-2	-9
Services exports	8	-3	11	4	1	11	3	-1	18	10	4	17	7
Non-oil non-gold imports	2	-11	4	-4	-5	-2	4	-5	1	0	7	6	3
<b>Government</b>													
State government: Capitial expenditure	33	102	77	-1	14	31	29	-1	-20	-13	-31	3	na
Central government : capital expenditure	30	29	-15	2	105	-41	315	-4	26	-50	-66	108	-30
Centre Revex ex of interest payments	1	-13	-24	-21	-12	-15	2	-12	10	-6	-7	-21	44
State Revex ex of Interest Payments	21	4	6	10	3	14	7	3	8	11	-1	21	na

Source: CMIE Economic Outlook, CEIC, SBIFM Research; NB: Red denotes a deterioration in y-o-y growth rate compared to the prior month while green denotes an acceleration in growth rate. Bank credit data adjusted for HDFC merger, Payment via digital means includes credit card, debit card, wallet and UPI payments; consumer sentiment is an index

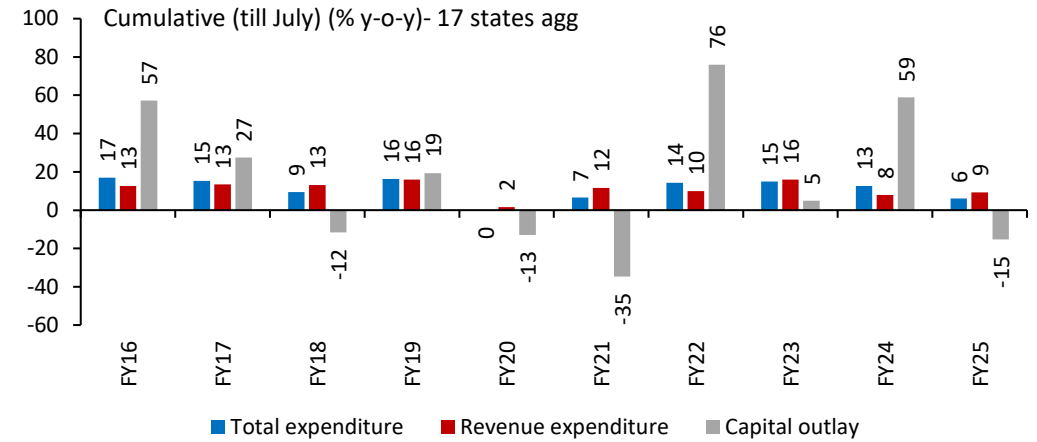


# Soft patch for capex in H1 FY25; govt capex moderating, private capex outlook is still positive

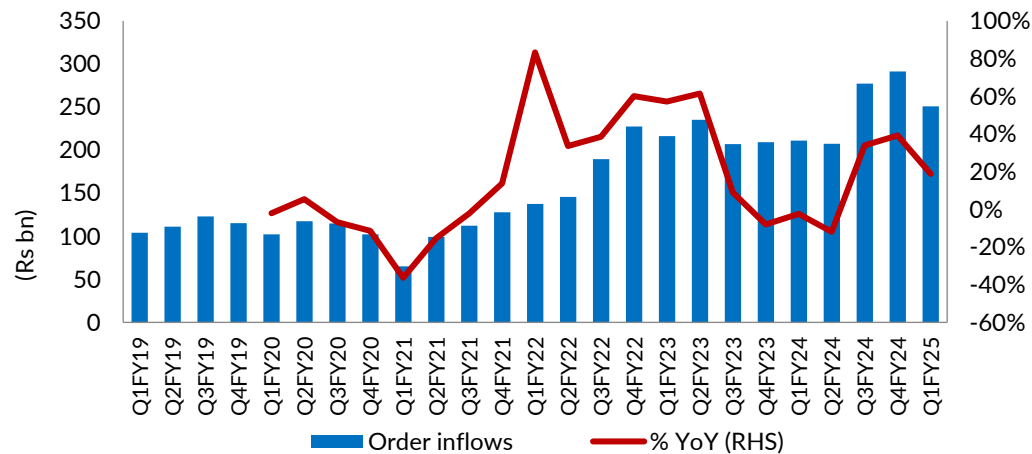
Central capital expenditure was weak from Apr-Aug'24 owing to lower spending pre general election 2024



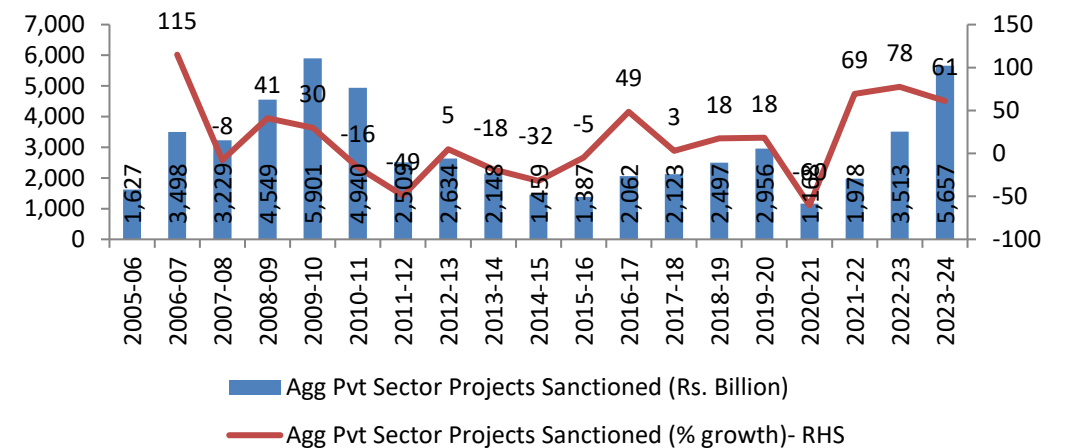
States capex is getting compromised by welfare spending compulsion



Order flows expected to revive as gauged from company reports

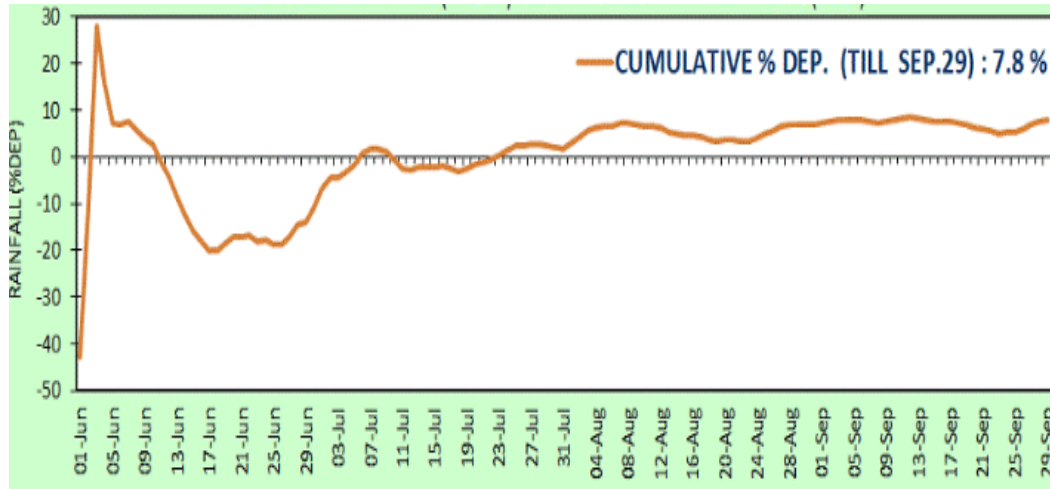


RBI's tracking of private corporate capex intentions gives a positive read

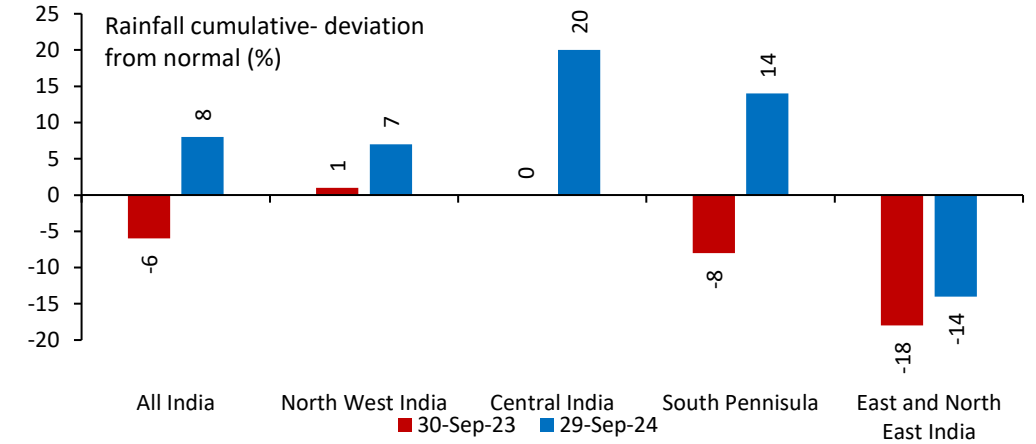


# Healthy rainfall pattern this year, improvement in crop sowing and reservoir levels

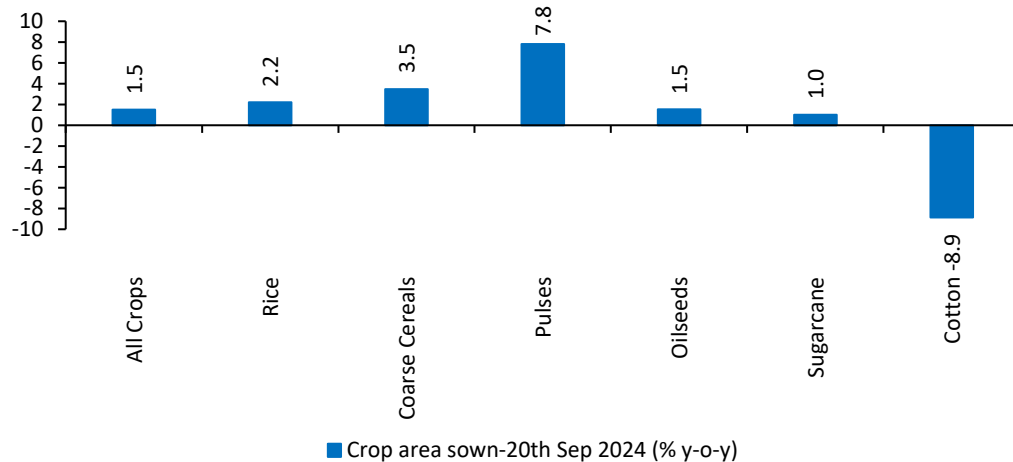
Cumulative monsoon rains are 8% above normal as of Sep'24 end (vs. 7% surplus last month)



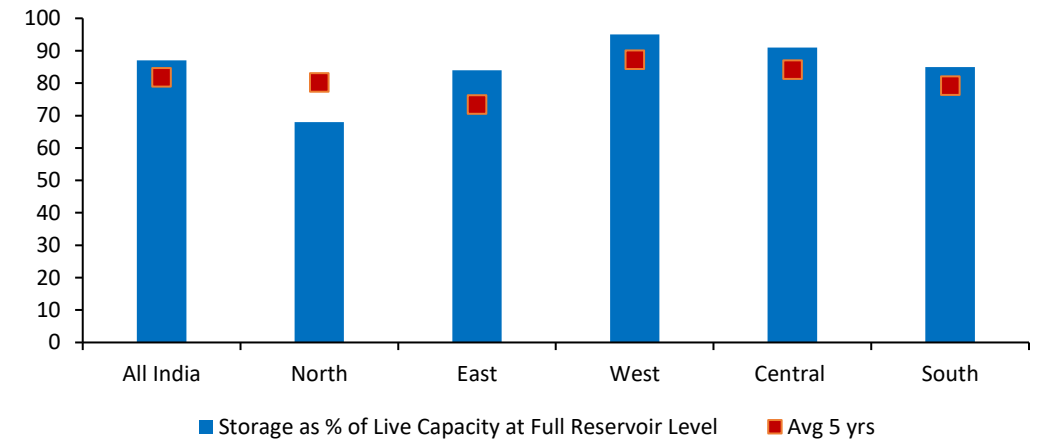
Barring east and north east India, all region sees a healthy surplus



Crop sowing reflects strength; only cotton sowing is declining on a y-o-y basis

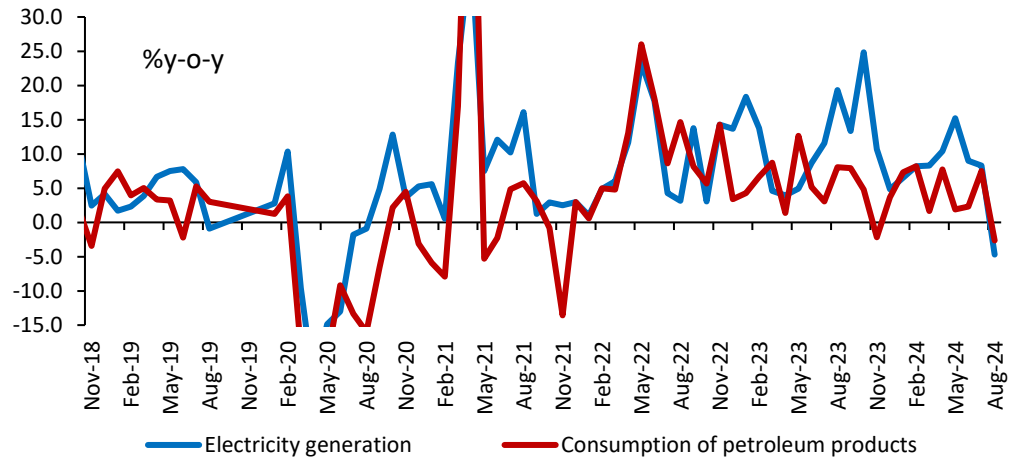


Reservoir levels are close to trend at an all-India level; though significantly lower in North India

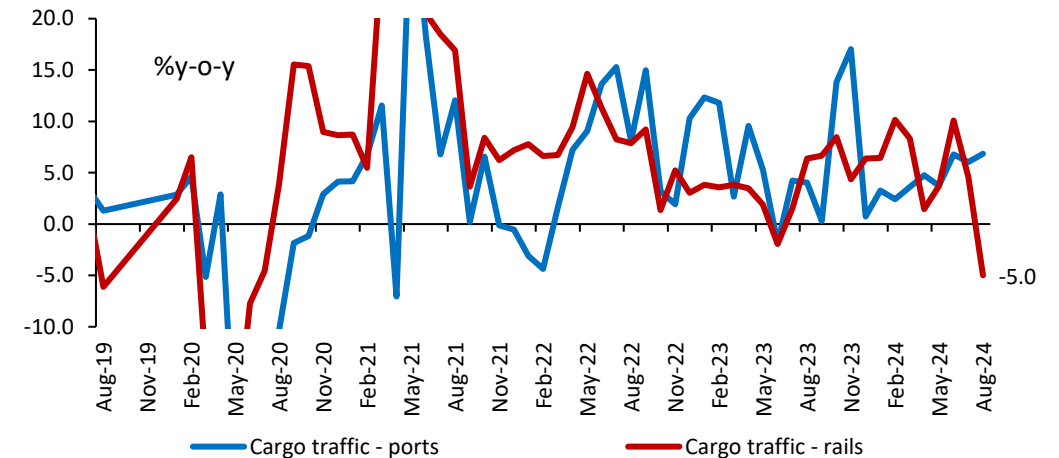


# Higher rainfall adversely impacts several high frequency indicators

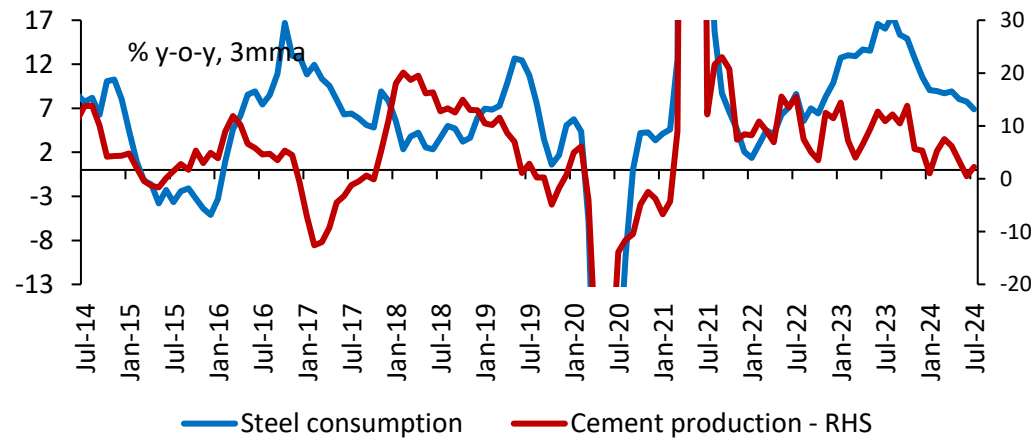
**Power demand (electricity generation and consumption of petroleum products) declines on a y-o-y basis in August 2024**



**Rail freight traffic sees a sharp moderation**

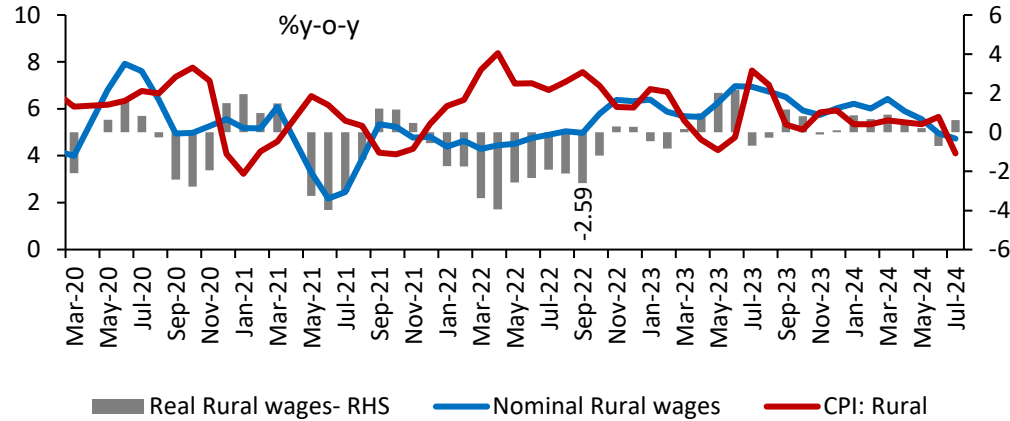


**Construction related indicators see a slowdown**

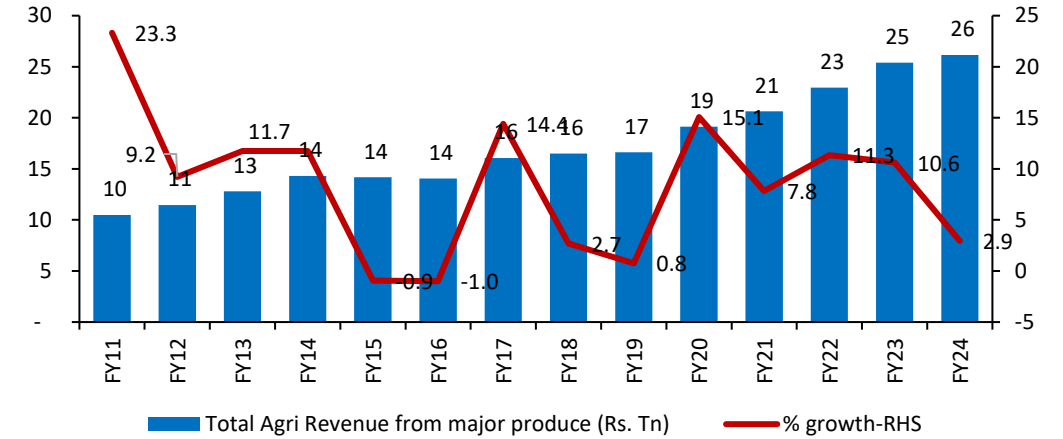


# Rural sector is strengthening at the margin

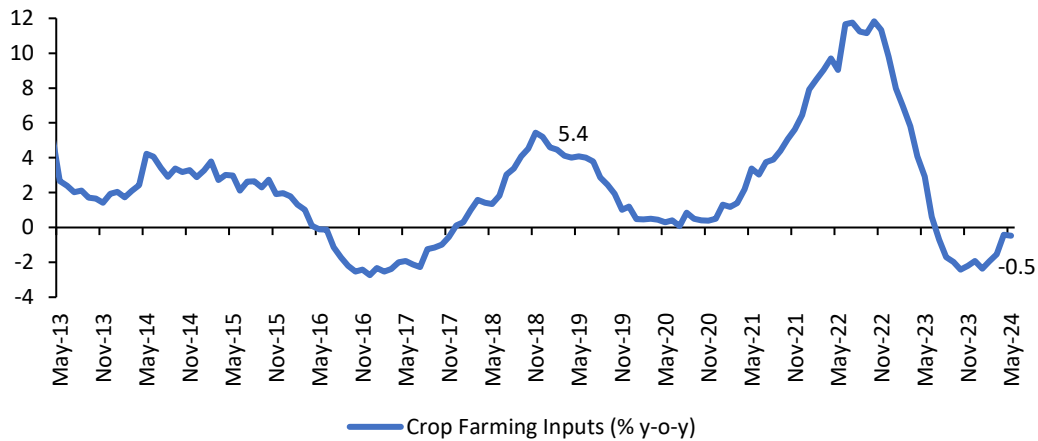
## Real rural wages have turned marginally positive



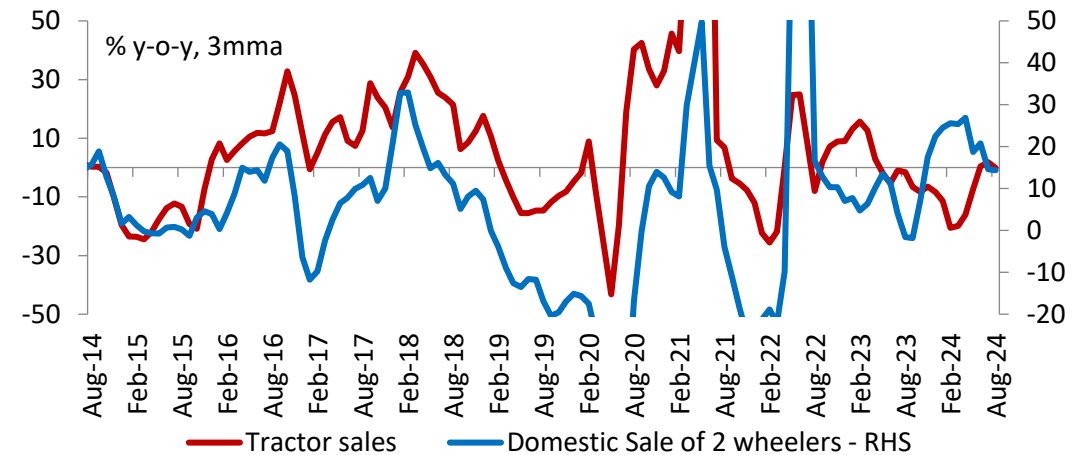
## Agriculture revenue continues to grow



## Cost of inputs moderated

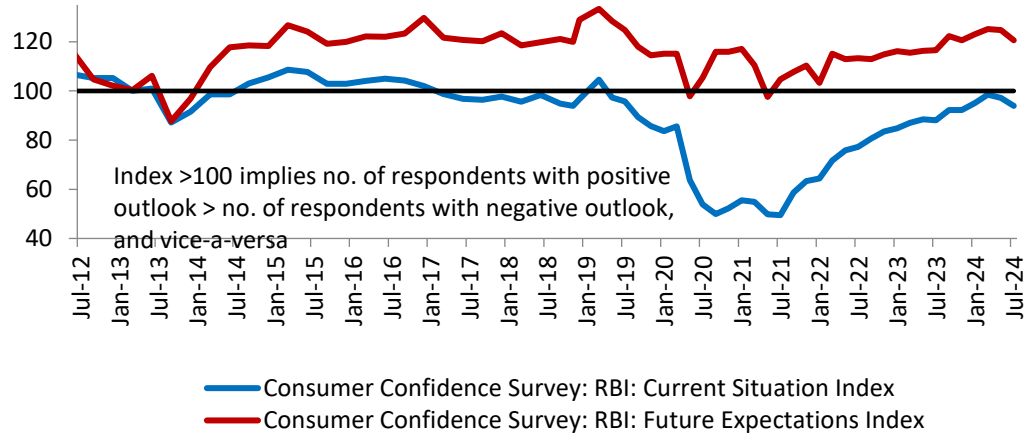


## 2W sales continue to grow but momentum moderates; Tractor sales continue to underwhelm

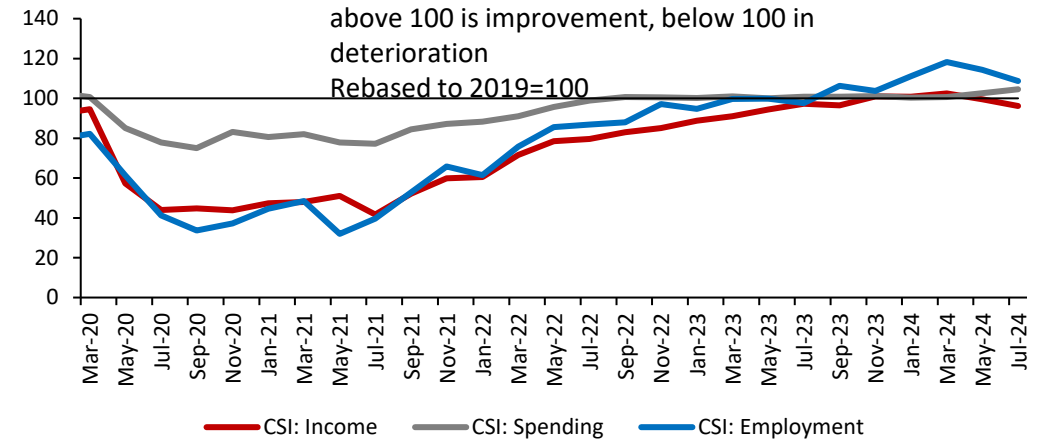


# Consumer confidence recovery in India has been very gradual

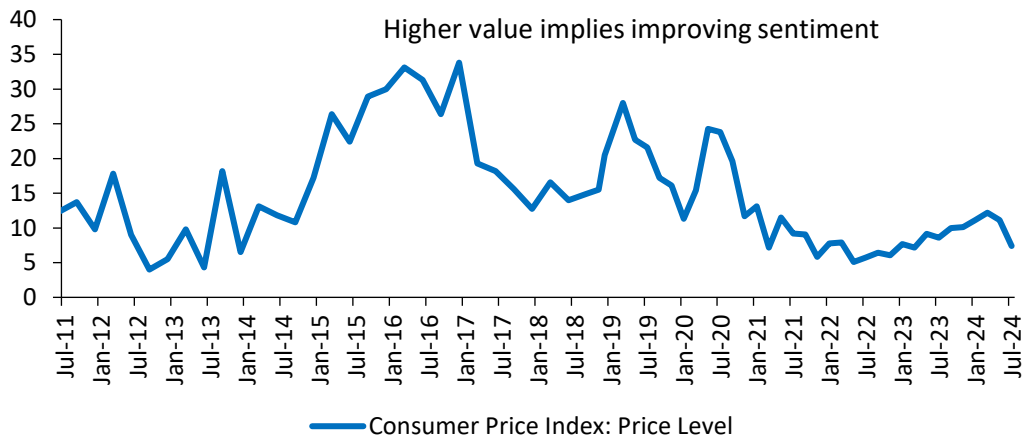
Consumer confidence still below 100 implying muted positivity; but the survey shows a moderation in July'24 (from 97 to 94)



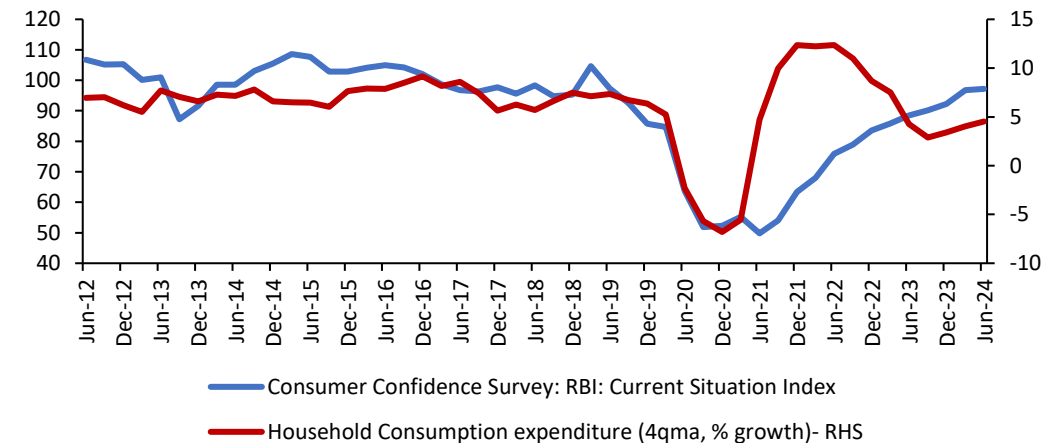
Consumer expectation on employment moderates; Spending and income is broadly flat



Moderation in CPI inflation would also help in improving the real purchasing power

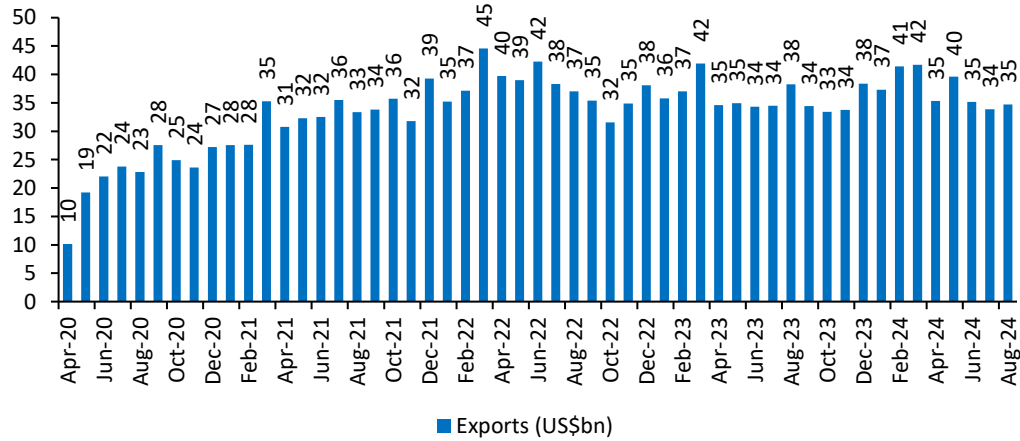


We expect a gradual recovery in consumption demand

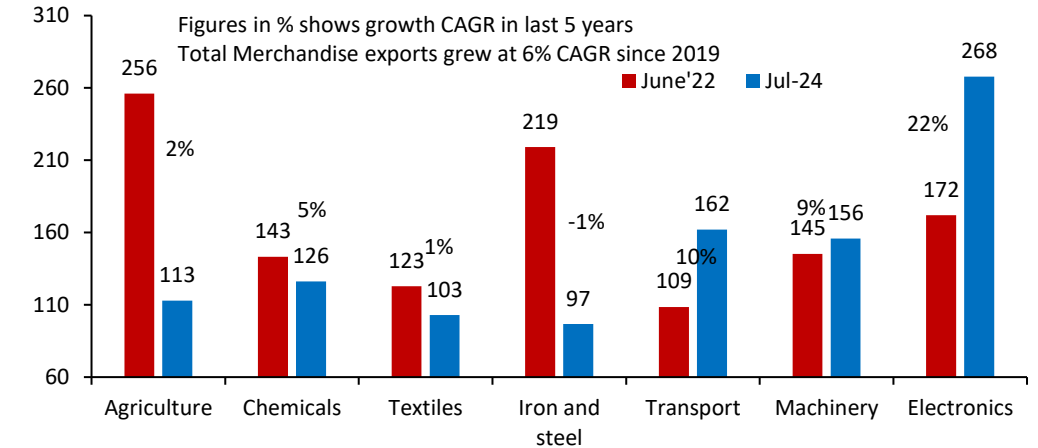


# Marginal positivity in exports as global inventory normalizes

## Merchandise exports are flat on an absolute level in August compared to last month

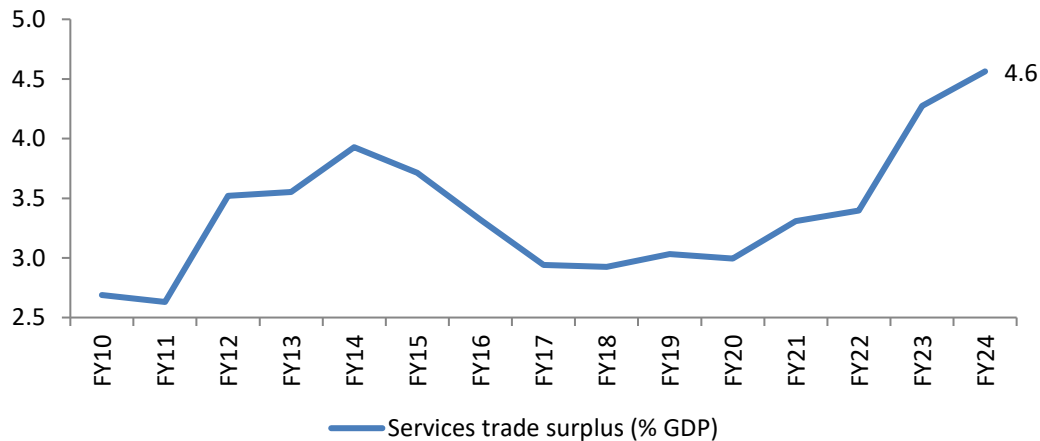


## Electronics exports are healthy; transport, chemicals and machinery exports sees some rebound



NB: Index value for every month compares to corresponding month in 2019

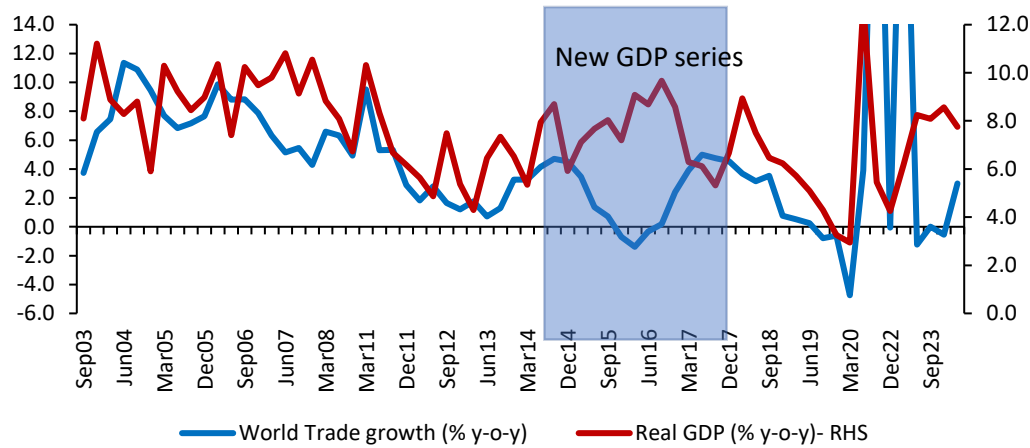
## Services exports continue to be resilient



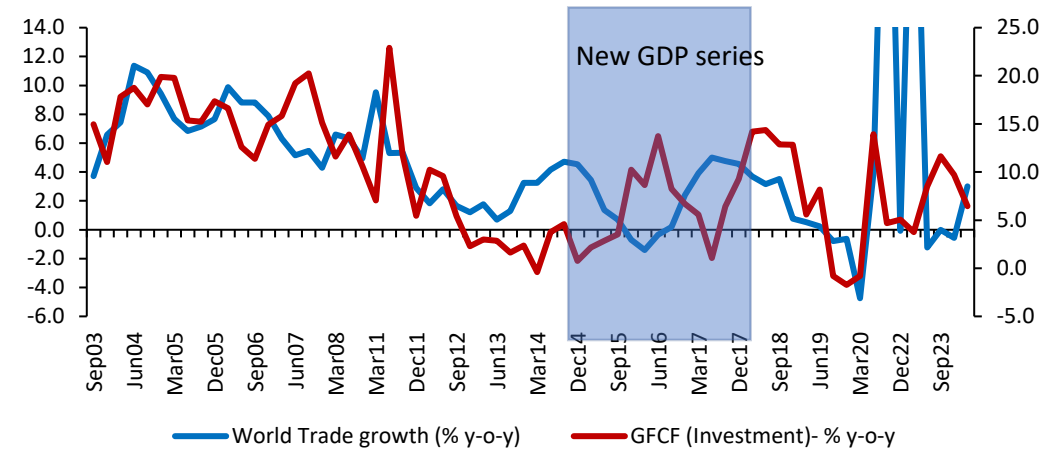
- Global export cycle is showing very nascent signs of positivity. It is due to continued positivity in the US demand and normalizing US inventory.
- India's exports have been recovering since December. Most of these gains have been due to higher exports to the US, China and select other Asian economies.
- Exports to Africa and Europe are still lagging. Within Europe, exports to Netherlands have improved significantly, but gets offset by lower shipments to Germany and France.

# Global headwinds aside, we are constructive on medium term growth outlook for India

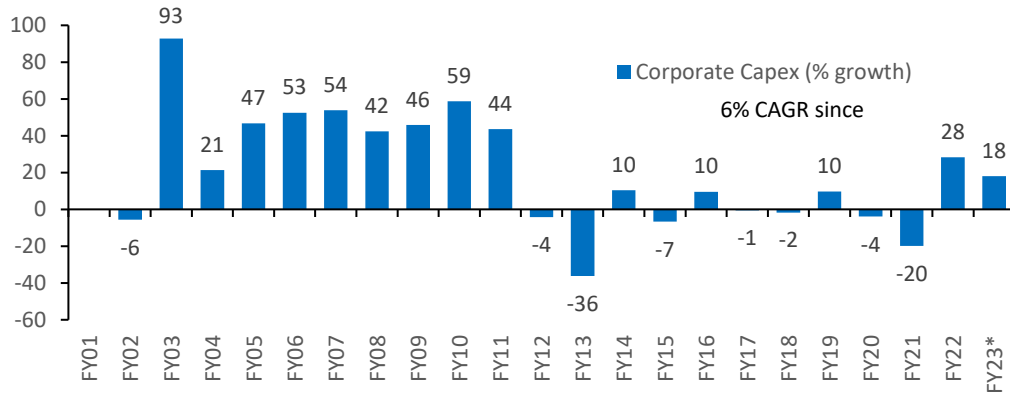
## India's GDP moderates with moderating global trade



## India's capex cycle has very strong linkage to global trade cycle

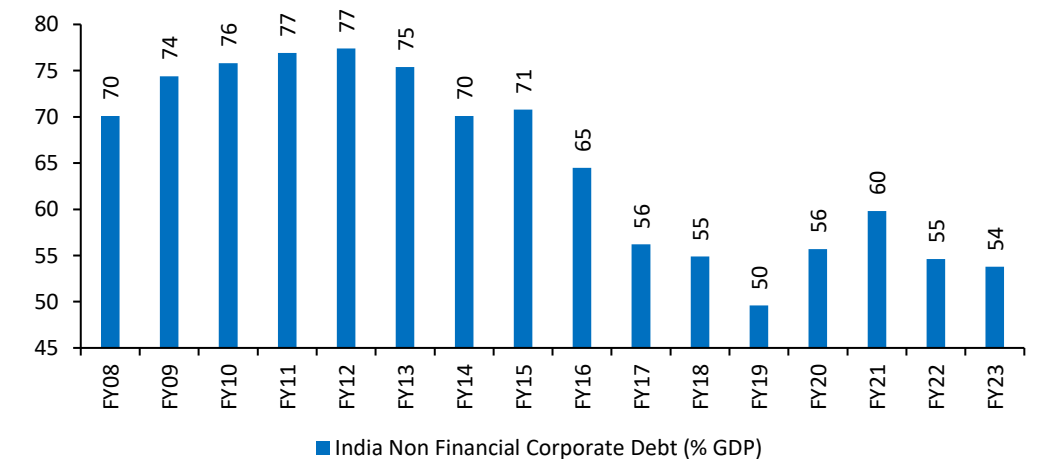


## Long period of underinvestment in India- Total Corporate Capex grew ~18% in FY23



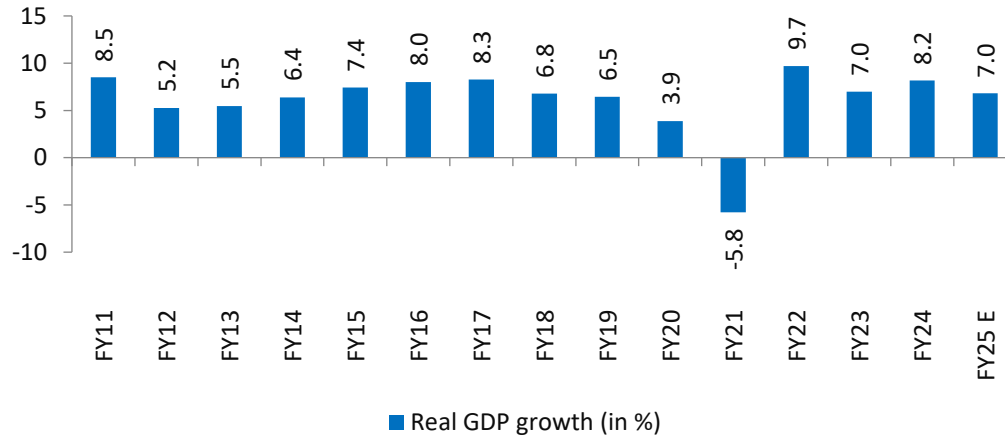
~5K listed companies and ~3K unlisted companies  
 FY23 data available only for 4.9K listed and 427 unlisted companies  
 Based on Purchase of fixed assets data for ~9K listed unlisted Co.s

## Corporate debt to GDP is at a multiyear low

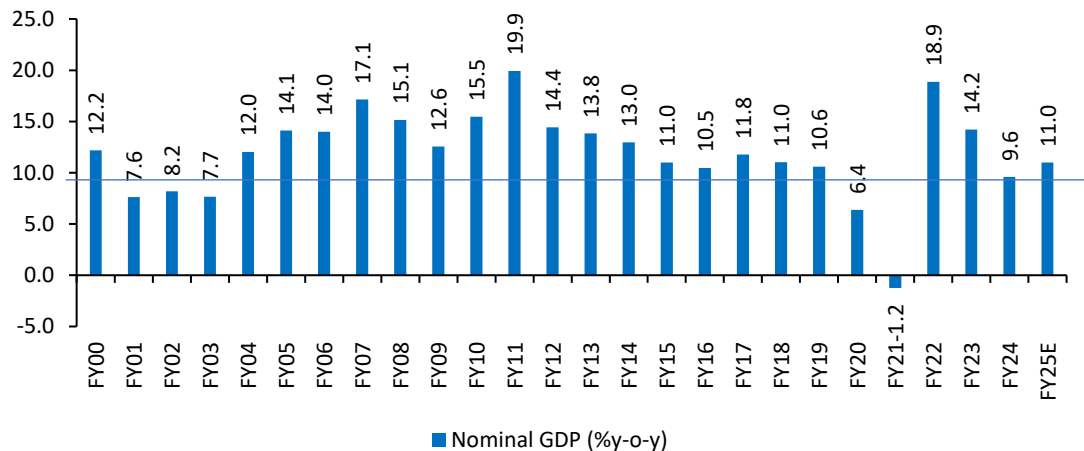


# FY24 depicts dichotomy in nominal and real growth strength

## Real GDP growth for FY24 at 8.2% y-o-y vs. 7.0% in FY23



## India's Nominal growth falls to single digit growth for the first time after FY03 (if we ignore FY20 and FY21 for COVID impact)



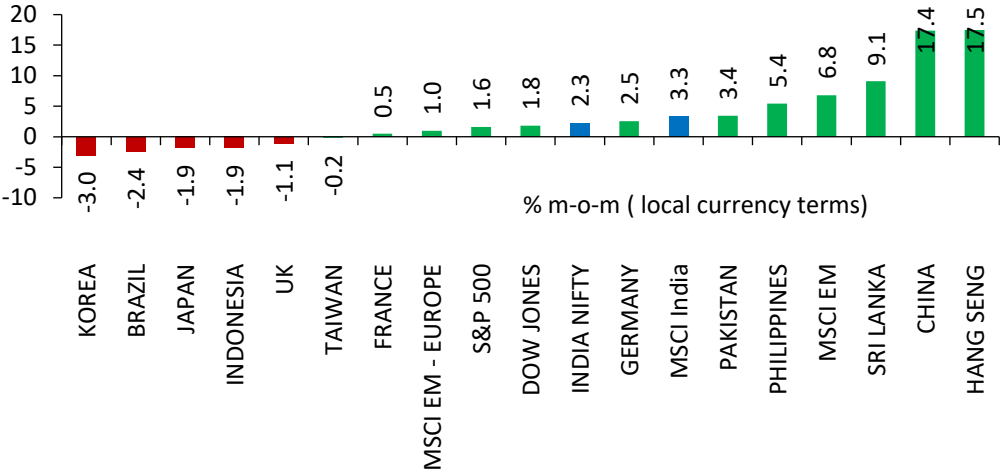
- In FY24 real GDP came in at 8.2% y-o-y (vs. 7.0% in FY23).
- Fixed investment is the key driver of growth with a positive contribution from net exports.
- Household consumption recovery was very slow. Consumption demand is gradually improving but 4% expansion in real demand is much softer than 7% pre-COVID.
- Global growth has held up better than expected keeping exports and manufacturing sector volumes resilient.
- Investment activity improved owing to significant front loading of government capex and real estate recovery as gauged from rising launches. State govt. spend was also frontloaded in FY24.
- The last few years were characterized by increased infrastructure spending and market share gains in exports which catalyzed the construction activity and manufacturing sector. If current infrastructure spend continues FY25, real GDP is expected to post ~6.8-7% print.
- **Overall volume growth is holding up in India, while low price hikes and flat commodity prices lead nominal growth to fall to 10%.**



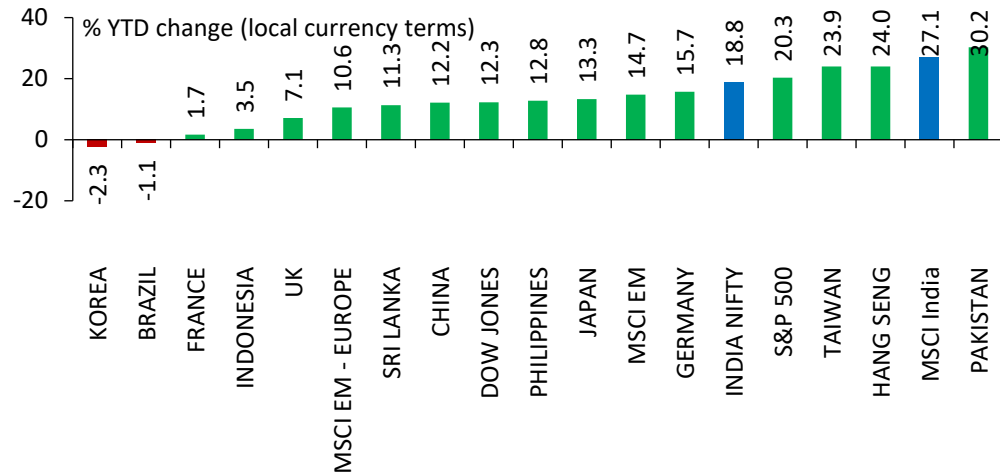
# EQUITY MARKET

# Global equity market snapshot: September 2024

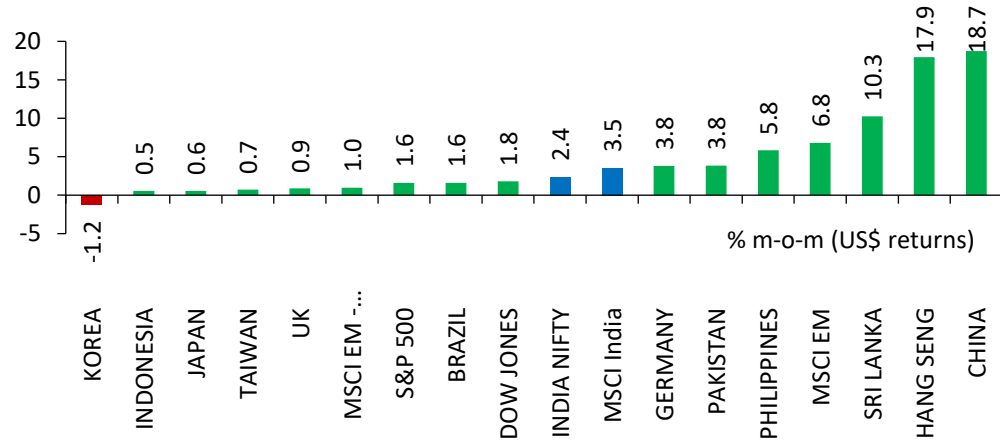
Performance in September 2024 (local currency returns)



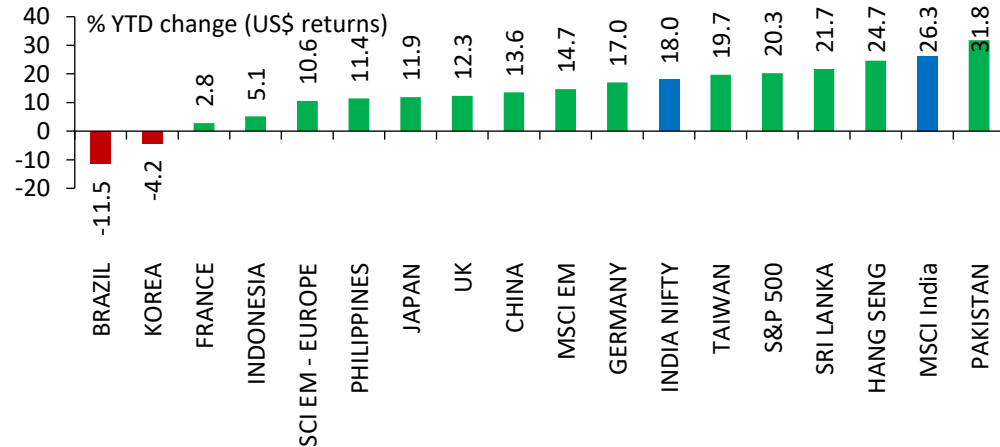
YTD performance (local currency returns)



Performance in September 2024 (US\$ returns)



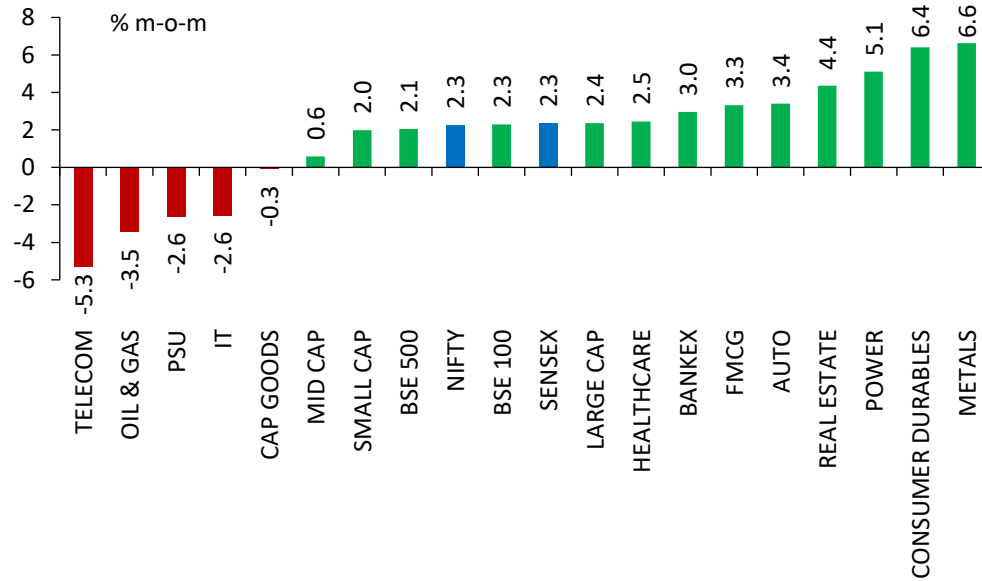
YTD performance (US\$ returns)



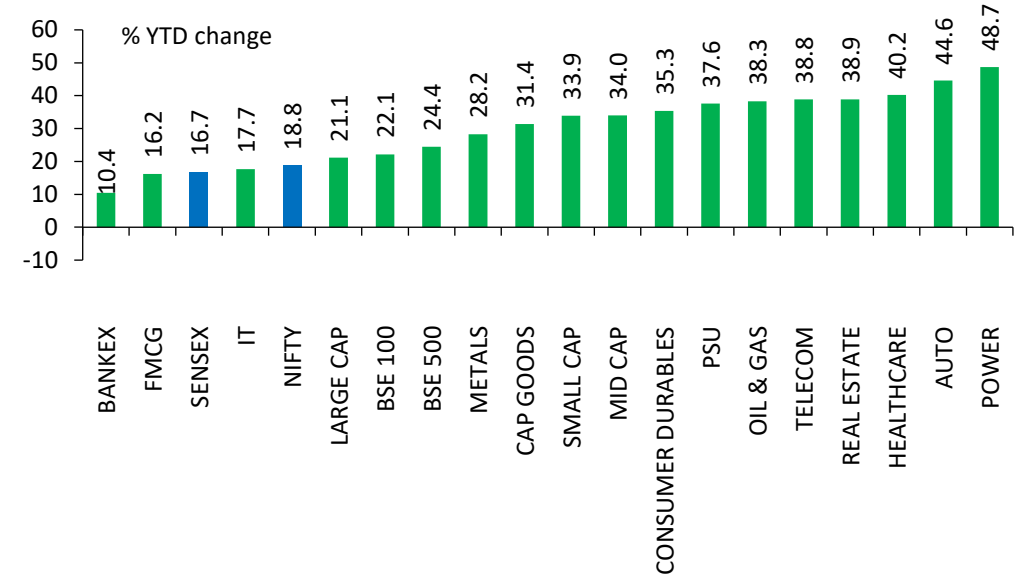
Source: Bloomberg, SBIFM Research

# Indian equity market snapshot: September 2024

Indian equity market performance in September 2024 (local currency returns)



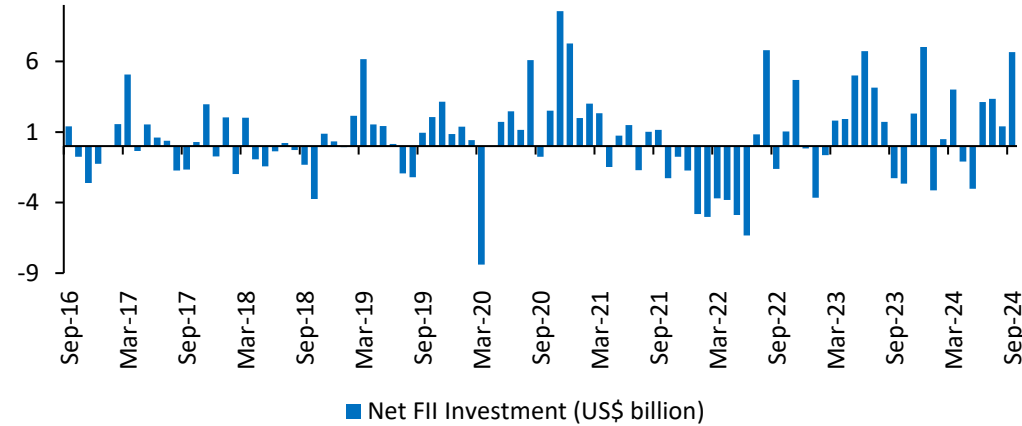
YTD performance (local currency returns)



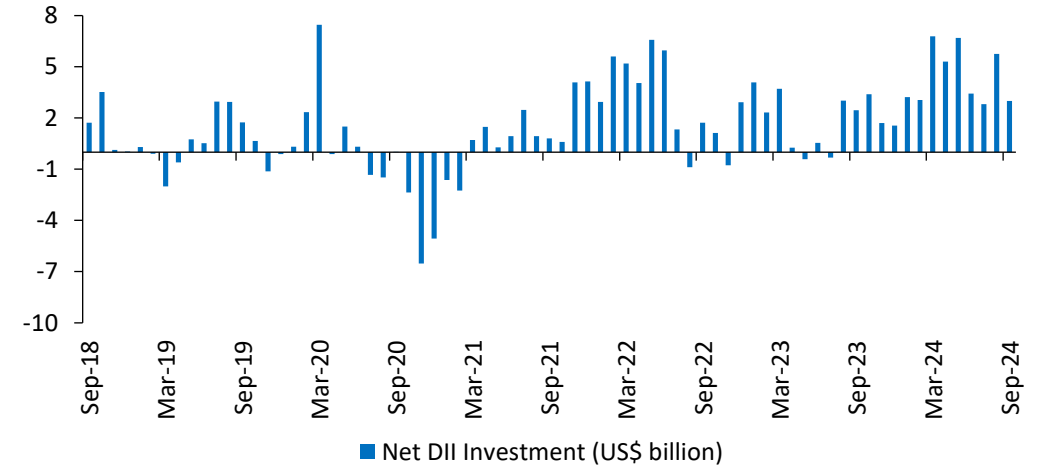
- Nifty and Sensex increased by 2.3% each m-o-m in September. Strongest gains visible in metals (7%), consumer durables (6%) and power (5%), while negative returns were delivered by telecom (-5%), oil and gas (-4%) and PSU (-3%).
- BSE Large cap (2.4% m-o-m) marginally outperformed small cap (2.0%) and mid cap (0.6%).
- On a YTD basis, Nifty and Sensex increased by 19% and 17%, respectively. All sectors have yielded positive returns on a YTD basis. Power (49% YTD) has been the biggest gainer, followed by auto (45% YTD) and healthcare (40%).

# Liquidity: FIIs remain net buyers in September; Primary market supply inched up

FIIs purchased ~USD 6.7billion in Sep'24 in equity segment vs. purchase of USD 1.4 billion in Aug'24



DIIIs are net buyers (purchase of USD 3 billion in Sep'24 vs. USD 5.8 billion in Aug'24)



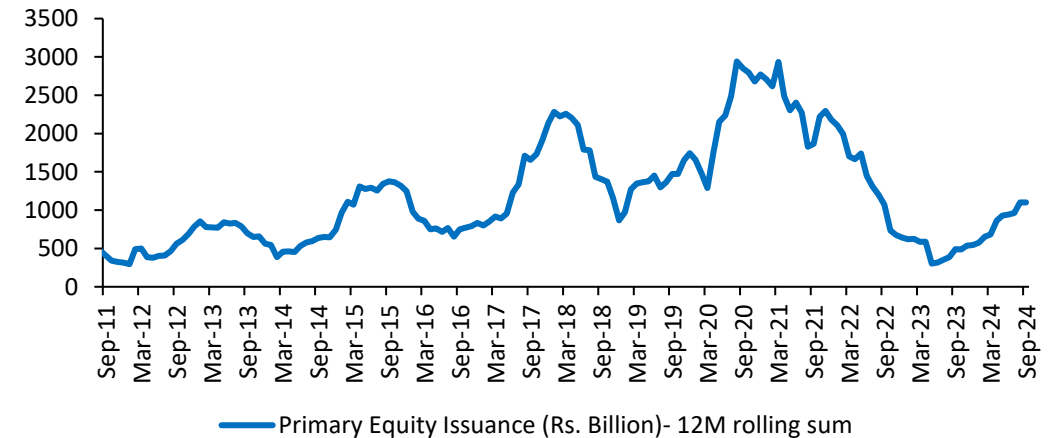
Retail flows into Equity (both Cash and Derivates) surge; Category wise net inflows into Indian equities:

	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024*
<b>In Rs cr</b>													
FIIs	1,28,361	1,13,136	97,069	17,946	20,493	49,234	-34,252	1,01,111	1,70,260	24,004	-1,21,439	1,71,107	35,565
DIIIs	-55,800	-73,052	-28,557	67,587	35,363	90,738	1,09,662	42,257	-35,663	94,846	2,75,726	1,81,482	2,60,473
Individuals#	-24,900	-22,000	-30,100	-8,243	-26,382	-37,988	-8,523	-25,280	52,897	1,42,755	88,376	5,243	1,00,182
<b>In US\$bn</b>													
FIIs	24.4	20.1	16.1	3.2	3.2	7.5	-4.6	14.4	23.0	3.8	-16.5	20.7	4.3
DIIIs	-10.6	-12.8	-4.8	10.4	5.2	14.0	16.0	6.0	-4.8	12.6	35.7	22.0	31.3
Individuals#	-4.7	-3.8	-4.9	-1.3	-3.9	-5.8	-1.4	-3.6	7.1	19.3	11.7	0.6	12.0

\* As of July 31, 2024

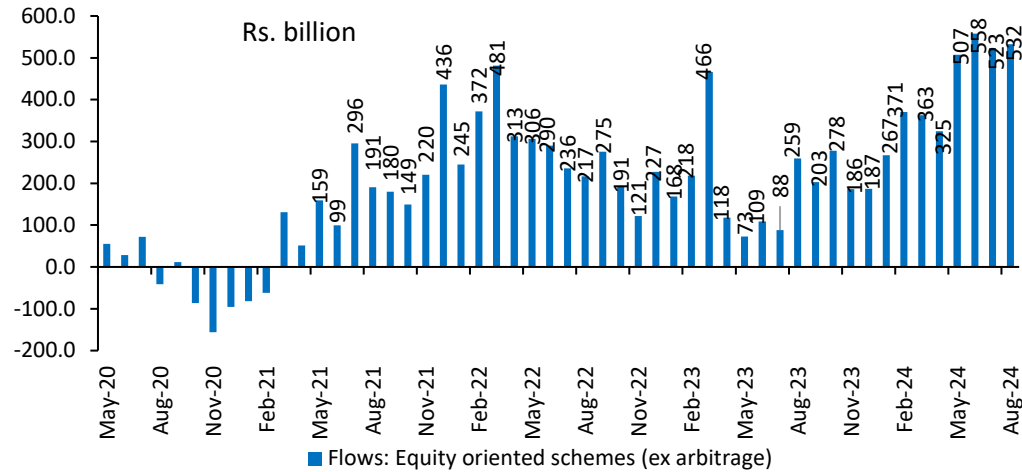
#Data pertaining to individuals include net flows on the NSE in the secondary market only. Individuals include individual /proprietorship firms, HUF and NRI.

Primary market supply trending up from last year lows

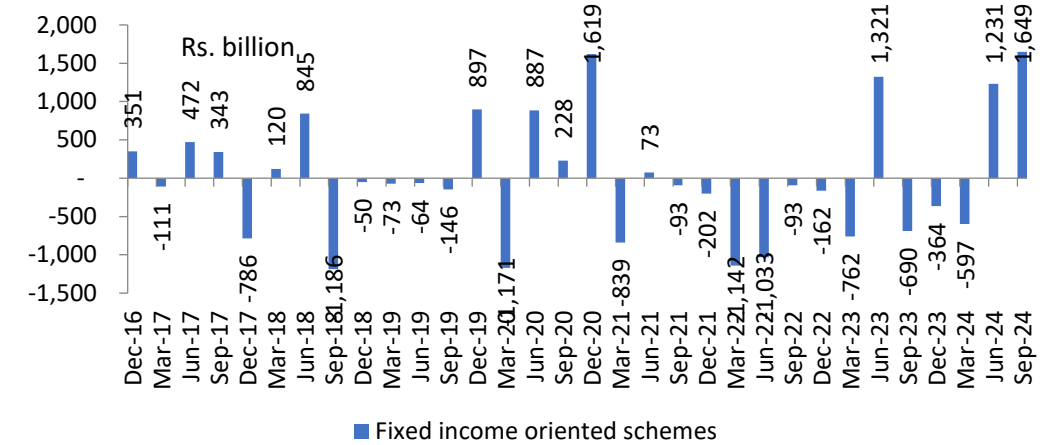


# MF flows: Improvement in SIP and non SIP equity inflows; Debt inflow rises sharply this quarter

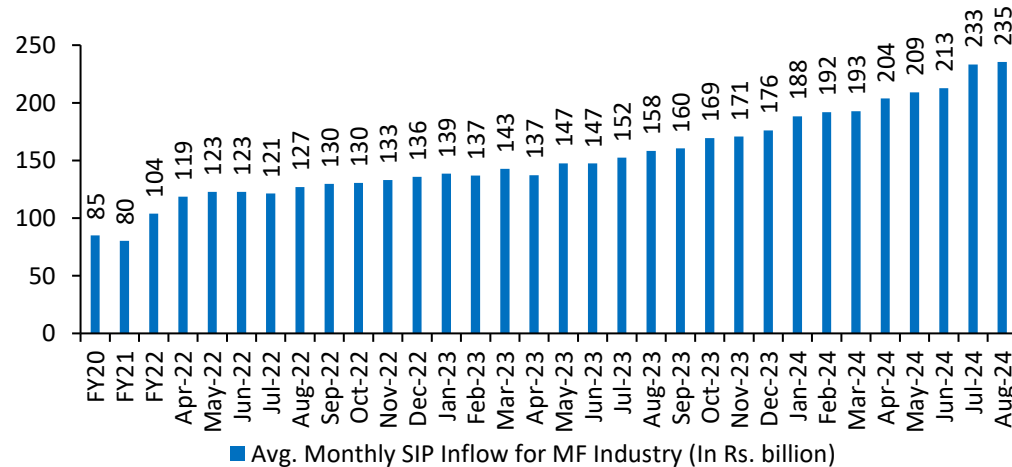
## Equity inflows improve in August 2024 compared to a month ago



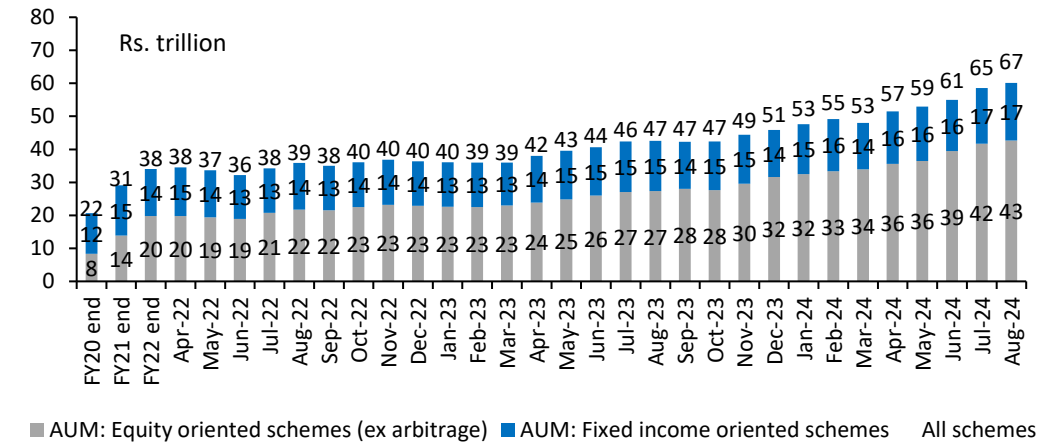
## Sharp debt inflow of INR 1.7tn in July-August 2024 (higher than inflow of 1.2tn in Q1 FY25)



## Monthly SIP inflow increases m-o-m in July



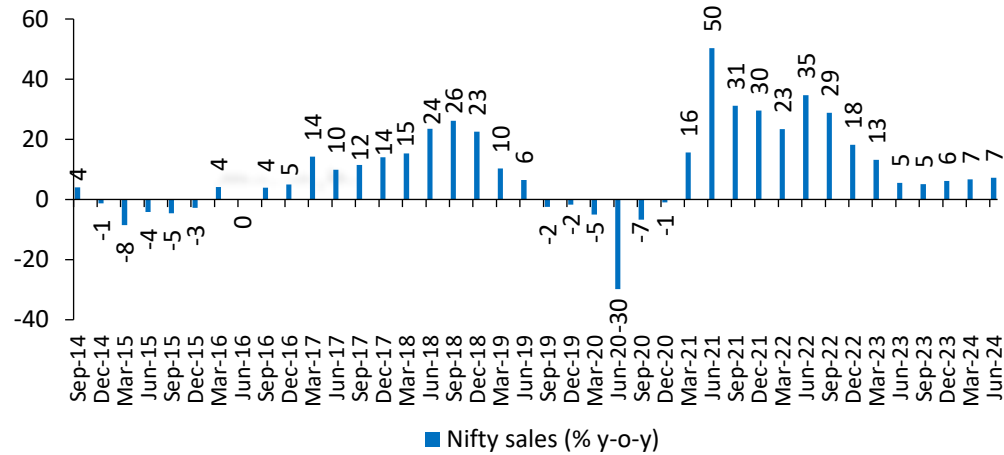
## Equity and debt AUM increases m-o-m



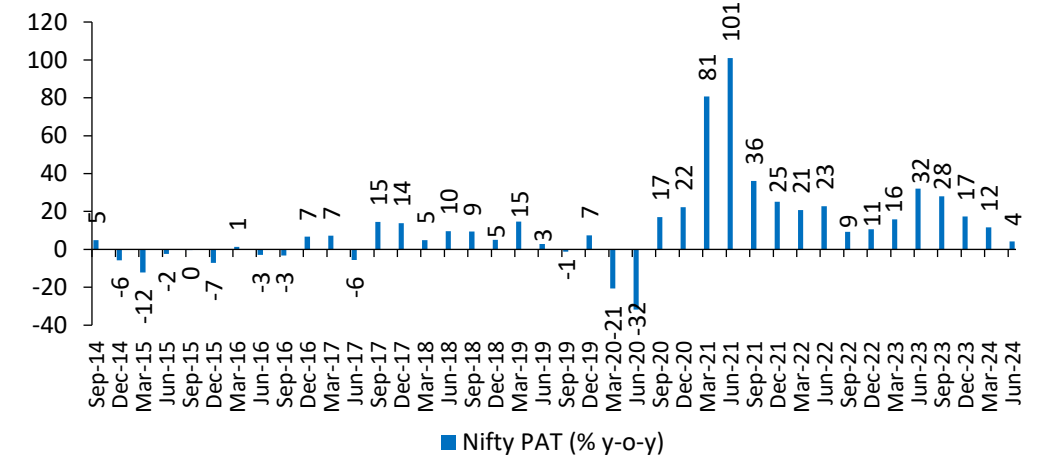
Source: CMIE Economic Outlook, Association of Mutual Funds of India (AMFI), SBIFM Research; NB: Fixed Income oriented schemes data till August 2024

# Q1 FY25 earnings: Weak PAT growth; Topline has been weak for 5 consecutive quarters

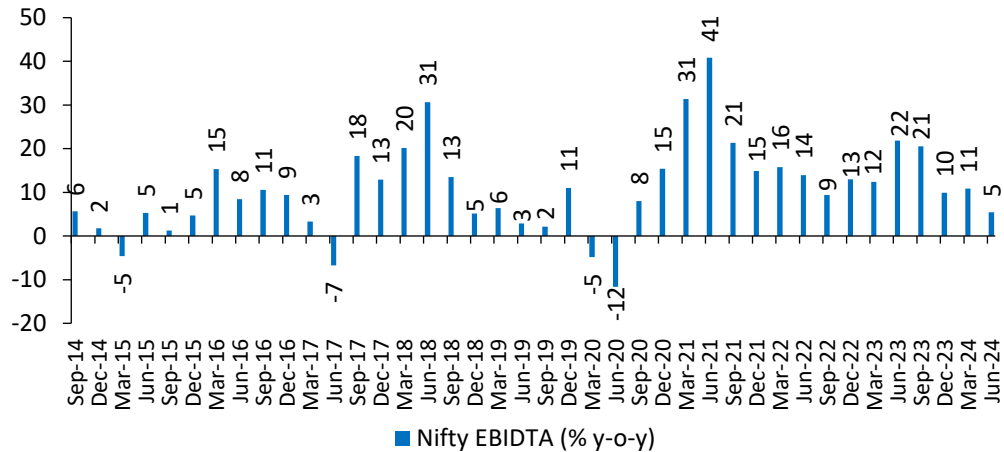
Q1 FY25 NIFTY sales growth in line with expectations



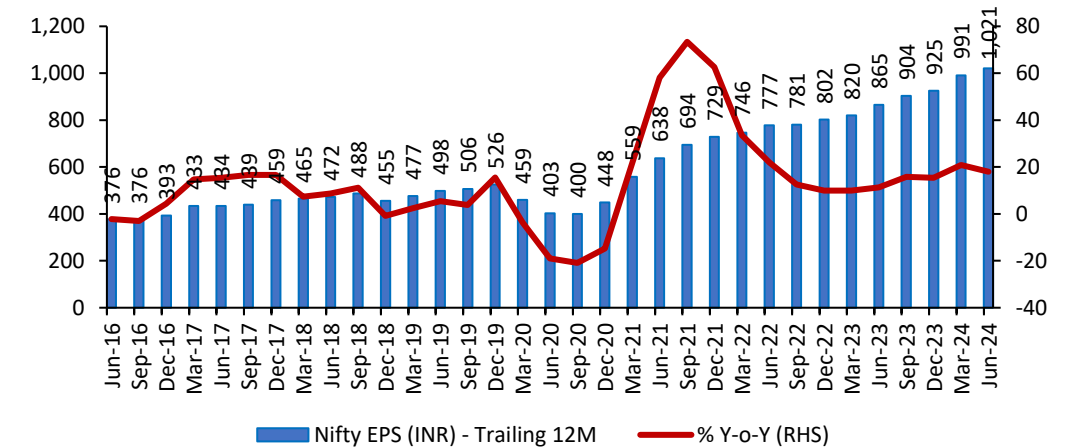
PAT growth moderates on account of high base effect in metals and oil & gas



EBITDA growth moderates as commodity tailwind dissipates



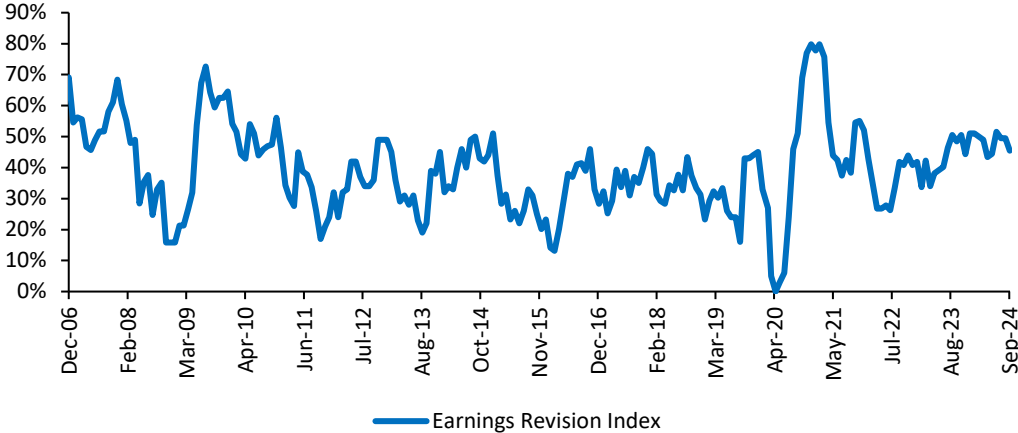
EPS growth moderates; 12m rolling EPS grows 18% but Q1 FY25 EPS growth moderates to 13% (vs. 30% in Q4 FY24)



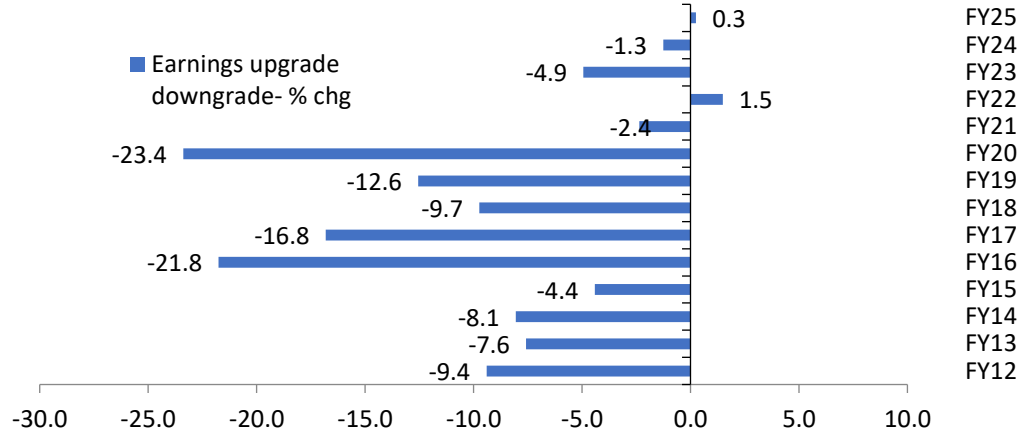
Source: MOSL, SBIFM Research; NB: Results released for 50 NIFTY companies for June 2024 quarter, historical data is for all the NIFTY 50 companies, EPS growth is adjusted for Axis bank losses for FY23

# Earnings upward revisions fall in September

Earnings Upgrades to downgrades ratio falls in September



In FY25 (till September), EPS projection saw a marginal upgrade

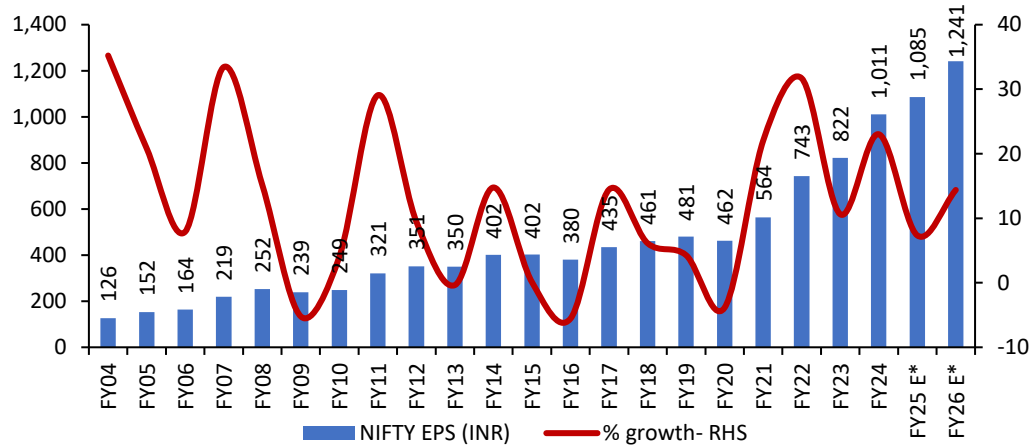


- Earnings revisions for FY25 have fallen with Materials seeing downward revisions. Healthcare continues to get upward revisions.
- Consensus expects 12.3% EPS growth CAGR for the Nifty over FY24-FY26.

Source: Bloomberg, FactSet, SBIFM Research; NB: \*data for communication services can't be calculated due to negative number in the base year, Earnings Revision Index: There has been a revision in methodology of calculating Earnings' Revision Index. Earlier, 12 month forward estimate number of all BSE 100 constituents as of the current month-end & 3 months back were taken. Now, new version considers FY23 consensus EPS for the current date and weighted format for history(1 month, 2 month & 3 months back with 1 month having the highest weight).

# Domestic support to earnings as the outlook for global cyclicals weakens

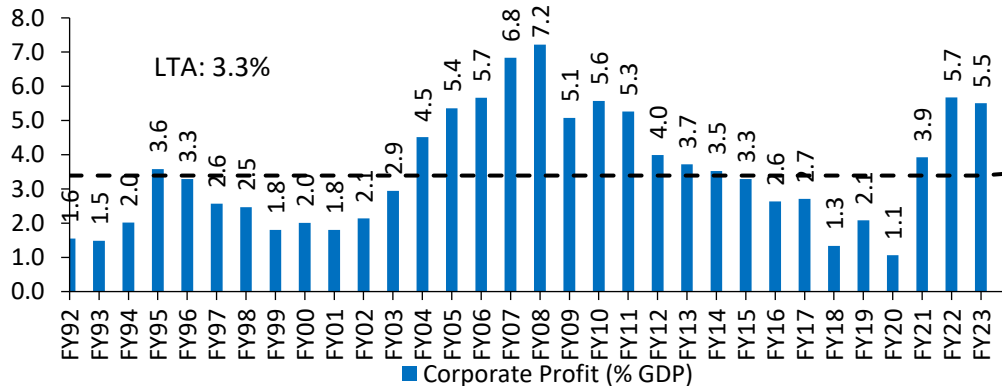
## Near-term headwinds to earnings while medium term prospects look decent



## Sectoral breakup of NIFTY earnings outlook

	No. of Cos.	EPS Change					FY24-26 (CAGR)	
		FY20-21	FY21-22	FY22-23	FY23-24	FY24-25		
Nifty		20.0%	35.7%	5.9%	29.5%	9.1%	15.6%	12.3%
Materials	6	55.2%	222.9%	-54.7%	-13.8%	46.5%	31.1%	38.6%
Industrials	3	22.9%	-30.1%	-0.9%	-0.9%	38.1%	24.7%	31.2%
Financials	11	13.8%	27.3%	23.1%	53.0%	11.8%	14.1%	12.9%
Health Care	5	5.9%	51.7%	23.6%	2.5%	13.5%	11.7%	12.6%
Utilities	2	18.0%	-9.7%	6.0%	-28.7%	6.0%	13.0%	9.4%
Consumer Staples	5	-5.0%	-3.9%	5.6%	32.6%	6.4%	9.0%	7.7%
Energy	4	56.9%	11.4%	8.1%	33.6%	2.8%	11.8%	7.2%
Information Technology	6	9.6%	37.1%	13.3%	13.5%	0.0%	12.7%	6.1%
Consumer Discretionary	7	20.7%	-33.4%	186.5%	58.8%	-5.5%	17.6%	5.4%
Communication Services	1		NA*		-6.1%	70.7%	43.3%	56.4%

## Earnings have recovered from ultra-lows of FY17-FY20



FY92-FY23 data is based on a sample of ~30,000 listed unlisted companies in CMIE (includes both financial and non financial companies)

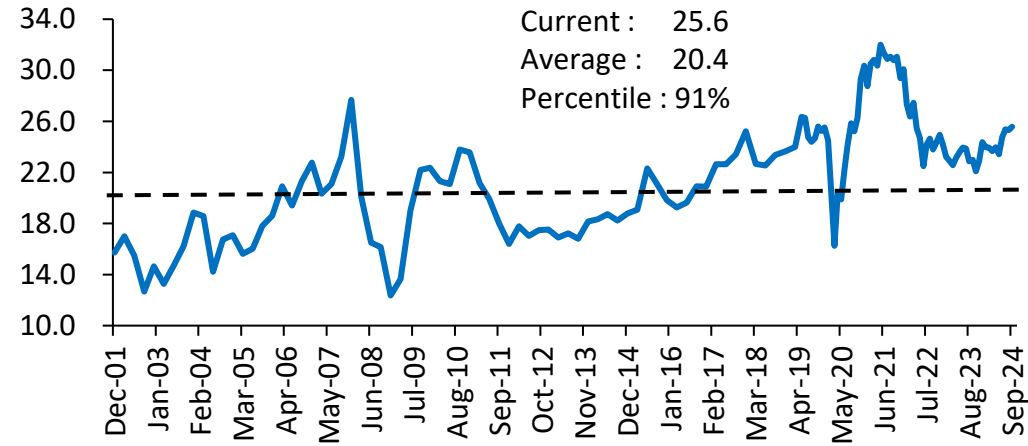
- Consensus expects 12.3% EPS growth CAGR for the Nifty over FY24-FY26.
- We are constrictive on medium-term earnings trajectory deriving comfort from our growth expectation for India and return of pricing power for many sectors.

Source: CMIE Economic Outlook, Bloomberg, SBIFM Research; \*FY25 and FY26 earnings estimates are SBIMF. \*\* EPS change is unadjusted to externalities, : \*\*\*data for communication services can't be calculated due to negative number in the base year, Earnings Revision Index: There has been a revision in methodology of calculating Earnings' Revision Index. Earlier, 12 month forward estimate number of all BSE 100 constituents as of the current month-end & 3 months back were taken. Now, new version considers FY23 consensus EPS for the current date and weighted format for history (1 month, 2 month & 3 months back with 1 month having the highest weight).

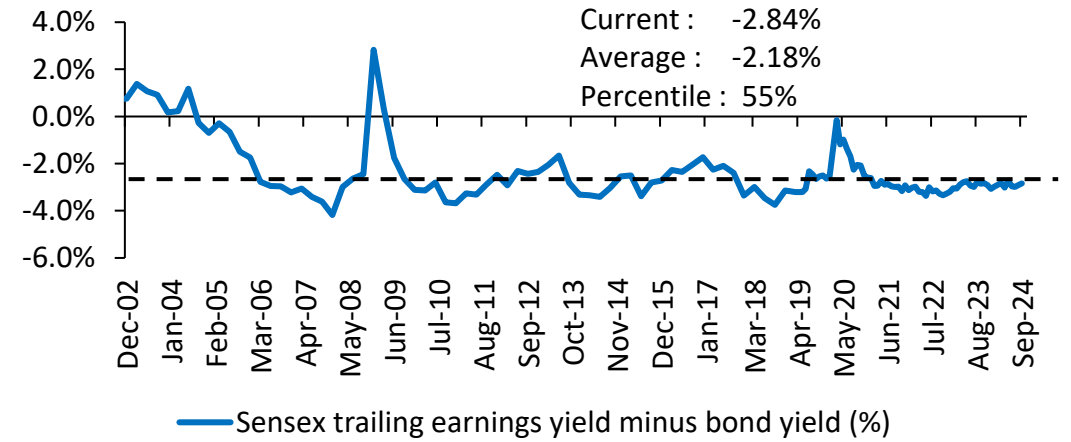


# Equity valuations remain expensive

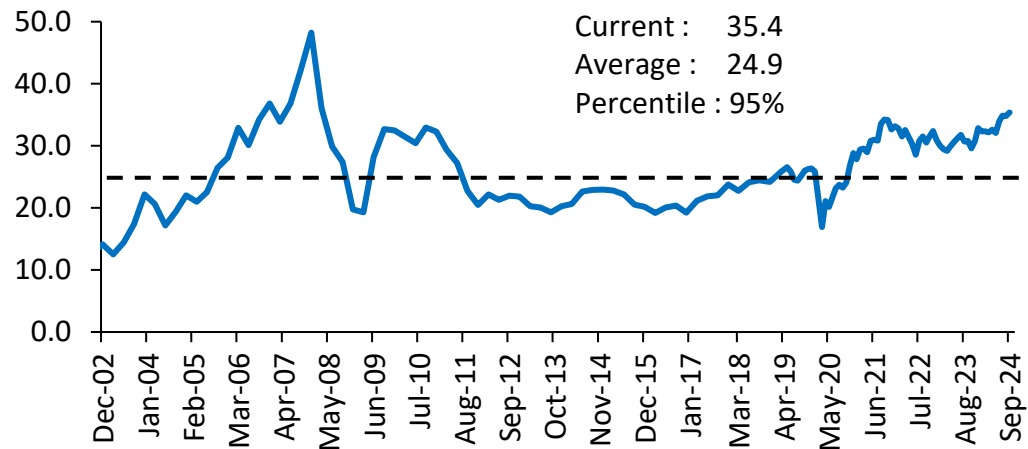
**Sensex trailing PE ratio stood at 25.6 in Sep'24 vs. 25.3 in Aug'24**



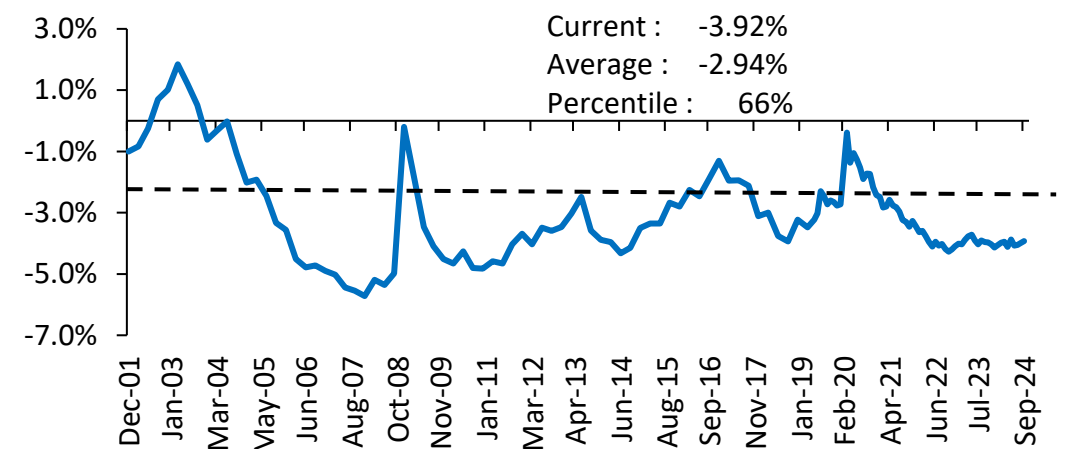
**Earnings yield to bond yield spread is moderately expensive**



**Shiller PE ratio stood at 35.4 in Sep'24 vs. 34.8 in Aug'24**

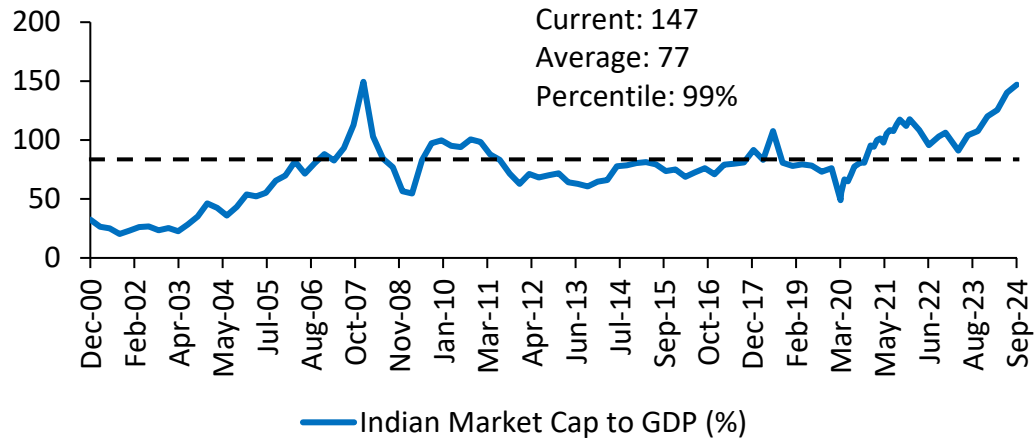


**Shiller earnings yield to bond yield spread moderately expensive**

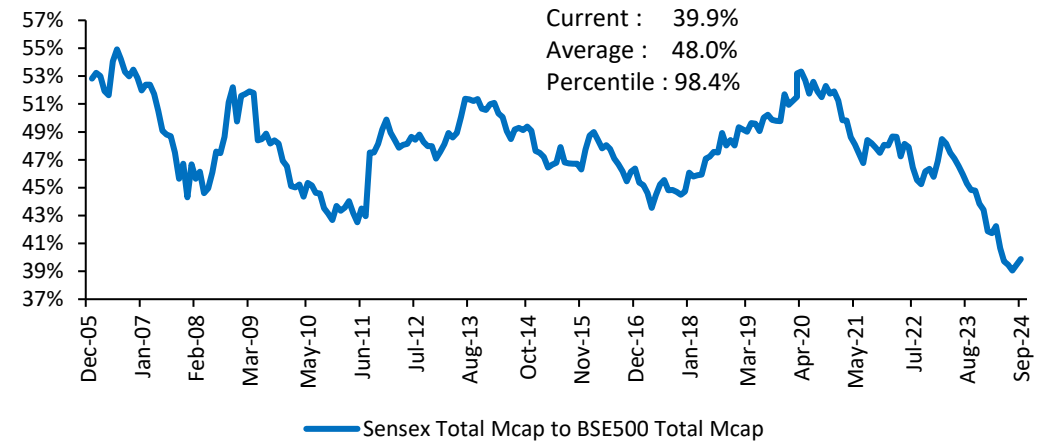


# Polarization remains low

Market capitalization/GDP expensive vs. history at 99<sup>th</sup> percentile reading



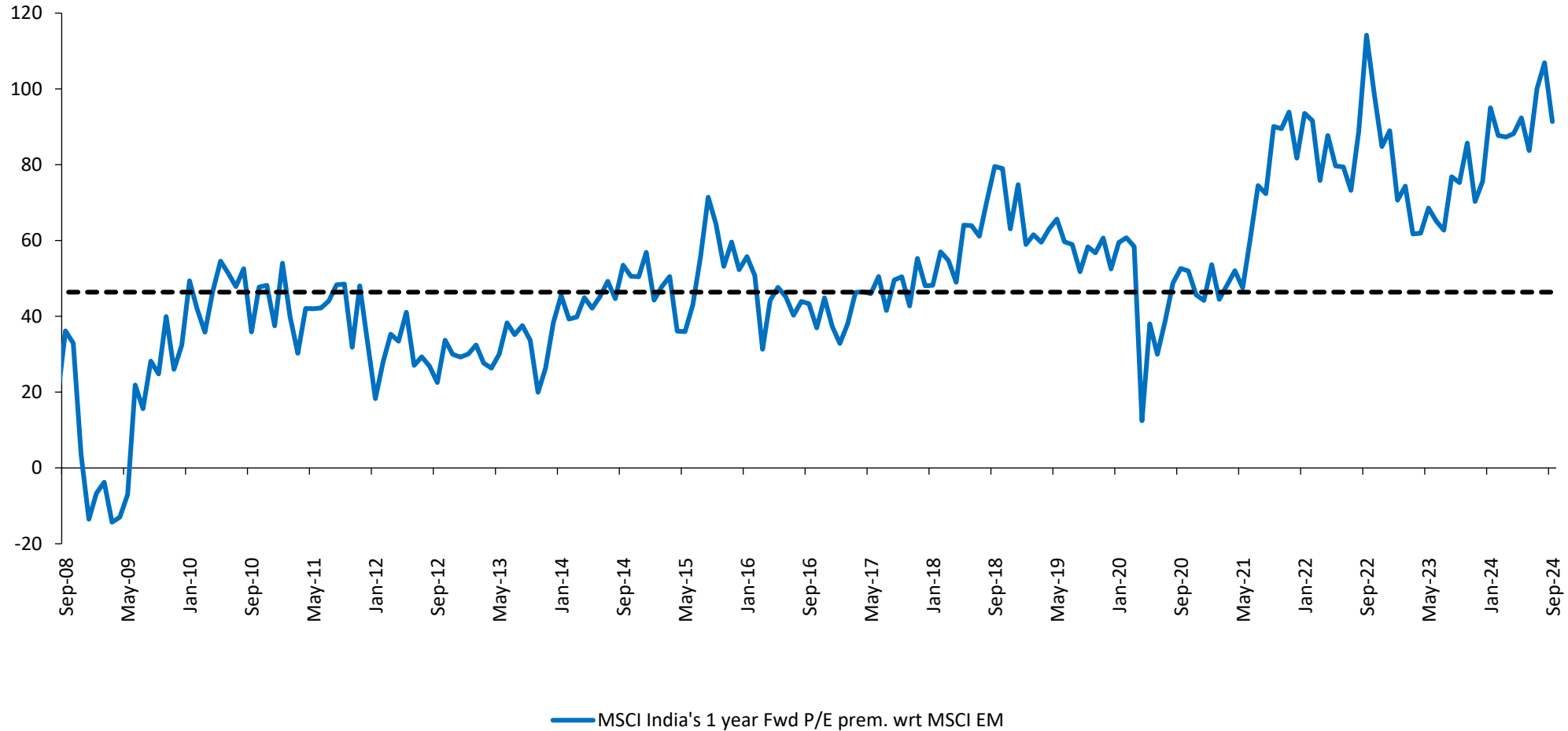
Mid caps and small caps: Market polarization low



- Market polarization remains low with broader markets outperforming the frontline large cap indexes.
- The ratio is now back to historical lows, suggesting the risk-reward is more towards large caps now.

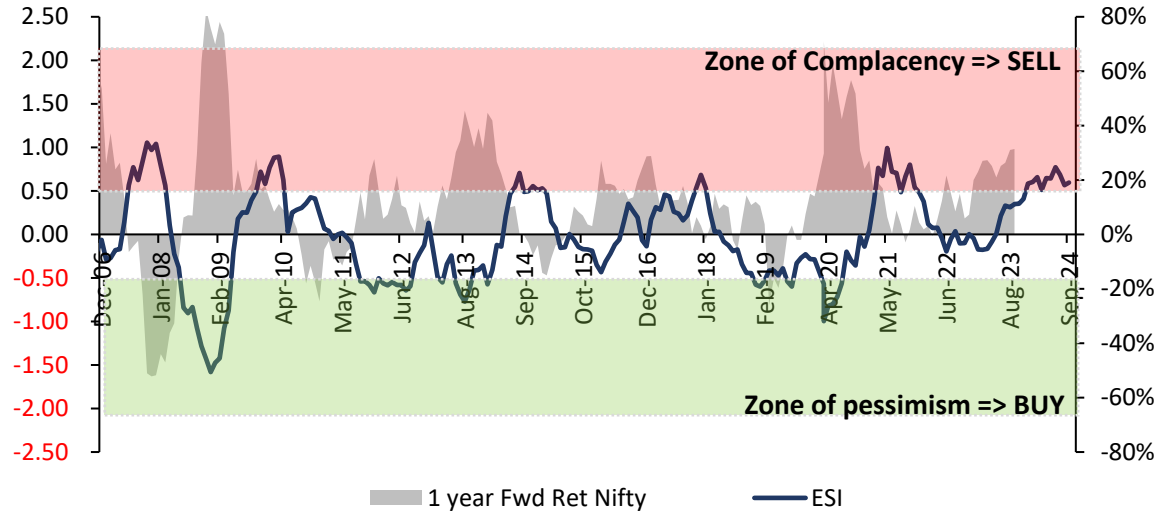
# MSCI India's valuation premium relative to EM moderates in September

India's P/E premium to world has moderated from its peak in Oct'22; global multiples remain vulnerable to higher rates, weaker growth and potentially rising Equity risk premium

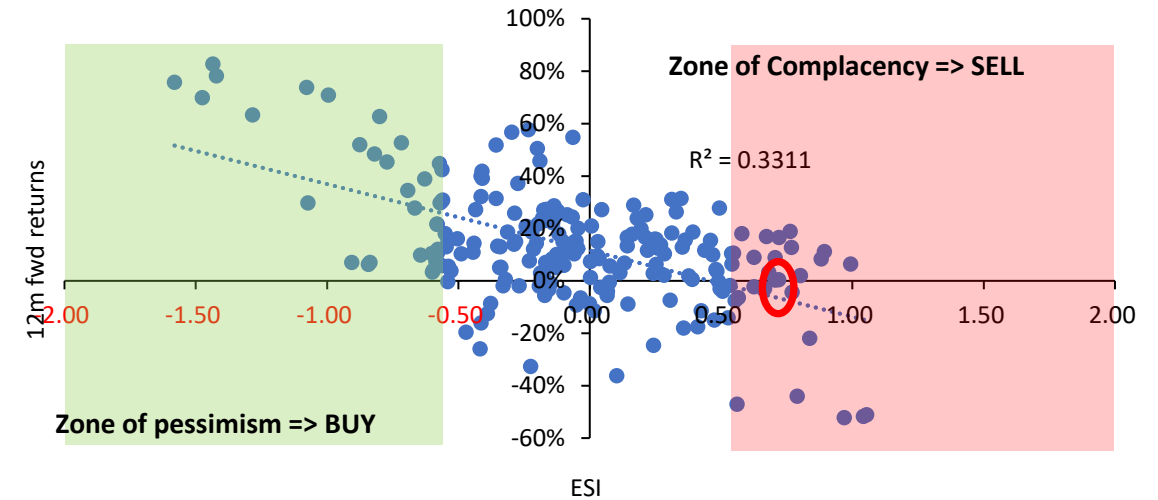


# Equity market sentiment remains in the Zone of Complacency

## Equity sentiment index remains in the Zone of Complacency



## Equity sentiment index remains up



- The sentiment measure works as a contrarian indicator. The action from the past few months suggests optimism remaining elevated.

# Equity Outlook: Stick to investment discipline amidst volatile market

- Indian equity gave positive returns in September. NIFTY and SENSEX increased by 2.3% each m-o-m. Strongest gains visible in metals (7%), consumer durables (6%) and power (5%), while negative returns were delivered by telecom (-5%), Oil & Gas (-4%) and PSU (-3%).
- BSE Large cap (2.4% m-o-m) marginally outperformed small cap (2.0%) and mid cap (0.6%).
- FIIs are net buyers in Sep'24 (purchased a net of ~USD 6.7 billion in Sep'24 in equity segment vs. a purchase of USD 1.4 billion in Aug'24). DIIs remain net purchasers.
- In India, growth has moderated recently, with public sector capex declining after a period of significant growth- a part of it is also due to weather and general election. Consumption indicators (auto retail sales, card spends) were also soft. This will likely adversely impact the Q2 FY25 results and GDP as well. Centre's capex thrust is moderating. States capex is getting compromised by welfare spending compulsion.
- On the other hand, the private sector capex still looks positive. Real estate launches were affected by general election, but outlook still stays positive. At the same time, the outlook on consumption gets positive at the margin as government spending tilts, inflation moderates and income situation normalize from the COVID stress. Though, a softer commodity could positively feed into gross margins of commodity users (like cap goods companies).
- To sum it all, these macro factors place a certain downside risk to corporate profits in the equity market which is already struggling with high valuation.
- Fundamentals dictate a caution on the market while liquidity and surge in flow makes it difficult to predict when the equity rally stops. But clearly, both due to global rate dynamics and India changing fiscal expenditure style, equity allocation should see a sector rotation.
- We stay constructive on discretionary consumption as a secular theme given the disproportionate boost the category derives from rising incomes. A related category that should benefit from rising incomes is savings plays and investment products. A third theme that we are positive on is natural resources and physical assets which, after more than a decade of underperformance, should benefit from a fiscally expansionary global policy backdrop that supports higher growth as well as inflation.
- We continue to stay bottom-up on stock selection with a leaning towards quality. We remain of the view that increasingly the market will become more discerning and move back towards companies which have strong business models, long-term earnings growth visibility and sustainable cashflows.

# FIXED INCOME MARKET

# Global Bond Market Snapshot: Bond rallies in September across key economies

Bond yields fell across the developed market in September as softer economic data prompts monetary easing cycle for key developed market central banks

10 Year Gsec Yield (% mth end)	2022 end	2023 end	Jun-24	Jul-24	Aug-24	Sep-24	m-o-m change (in bps)	YTD change (in bps)
<b>Developed market</b>								
US	3.87	3.88	4.40	4.03	3.90	3.78	-13	-10
Germany	2.57	2.02	2.50	2.30	2.30	2.16	-14	13
Italy	4.72	3.70	4.07	3.65	3.70	3.49	-21	-21
Japan	0.42	0.61	1.06	1.06	0.90	0.86	-4	25
Spain	3.66	2.99	3.42	3.12	3.13	2.96	-17	-3
Switzerland	1.62	0.70	0.60	0.45	0.48	0.42	-6	-28
UK	3.67	3.54	4.17	3.97	4.02	4.01	0	47
<b>Emerging Market</b>								
Brazil	12.69	10.37	12.33	11.88	12.22	12.29	7	193
China	2.84	2.56	2.21	2.15	2.18	2.21	3	-35
India	7.33	7.17	7.01	6.93	6.86	6.75	-12	-43
Indonesia	6.92	6.45	7.05	6.89	6.62	6.44	-19	-2
South Korea	3.74	3.18	3.26	3.06	3.09	3.00	-9	-18
Malaysia	4.09	3.73	3.86	3.72	3.76	3.71	-5	-2
Thailand	2.64	2.68	2.67	2.58	2.55	2.47	-8	-21
Turkey	9.83	25.06	28.28	28.35	28.52	28.37	-15	331
Mexico	9.04	8.95	9.92	9.79	9.68	9.34	-34	39
Poland	6.86	5.20	5.75	5.43	5.44	5.27	-17	6
Colombia	13.01	9.96	10.82	10.73	10.13	10.10	-3	14
Hungary	8.98	5.86	6.81	6.39	6.29	6.14	-15	28

# India Rates Snapshot: Yields moderate across all tenors

## Shorter and longer term yields moderate in September 2024

	2023 end	Aug-24	Sep-24	m-o-m (in bps)	YTD chang e (in bps)
Repo rate	6.50	6.50	6.50	0	0
3 year GSec	7.07	6.76	6.66	-10	-40
5 year GSec	7.09	6.79	6.68	-11	-42
10 year GSec	7.18	6.86	6.75	-11	-43
3 Yr Corp Bond*	7.78	7.64	7.57	-7	-21
5 Yr Corp Bond*	7.79	7.62	7.51	-10	-27
10 Yr Corp Bond*	7.76	7.45	7.31	-14	-45
1 Yr IRS	6.64	6.49	6.39	-10	-26
5 Yr IRS	6.19	6.08	6.03	-5	-16
Overnight MIBOR Rate	6.90	6.80	6.76	-4	-14
10 year SDL	7.65	7.21	7.10	-11	-55
INR/USD	83.21	83.87	83.80	0.1^	-0.7^
Crude oil Indian Basket**	77.43	78.27	73.72	-5.8^	-4.8^

- Bond yields moderate over the month across all tenors in September 2024.
- Rupee appreciated at the margin by ~0.1% to INR 83.80/\$ in Sep'24 (vs. 83.87 a month ago).
- Oil prices moderated by ~6% in Sep'24 vs. Aug'24, now at ~US\$73.7/bbl level.



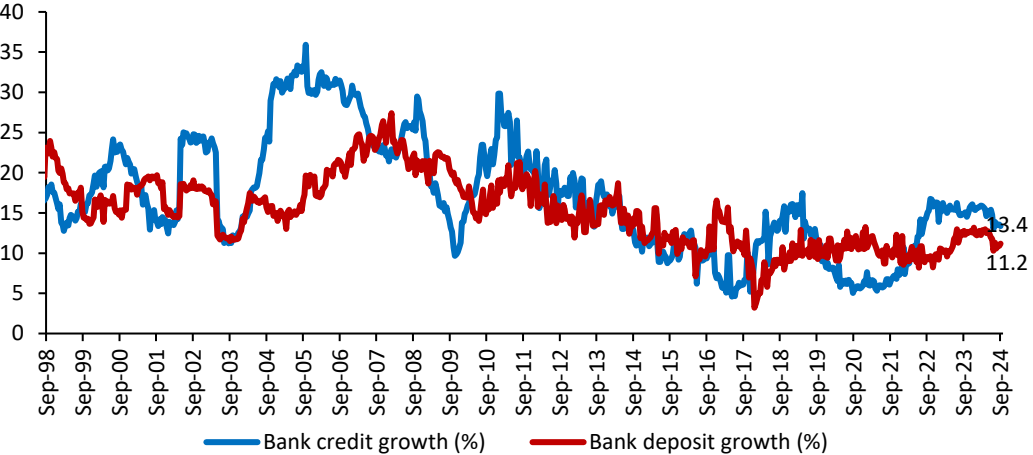
# Indian G-sec yield curve steepens in line with global trends

G-Sec yields fell further in September 2024; Compared to peak rate in October, long term yields are lower by ~50bps

Yield (%)	3 Month	6 month	1 Year	2 Year	3 Year	4 Year	5 Year	6 Year	7 Year	8 Year	9 Year	10 Year	15 Year	30 Year
30-Sep-23	6.80	7.03	7.02	7.25	7.26	7.24	7.23	7.25	7.25	7.27	7.22	7.22	7.31	7.41
31-Oct-23	6.89	7.08	7.14	7.35	7.32	7.35	7.35	7.38	7.39	7.41	7.38	7.36	7.43	7.51
30-Nov-23	6.97	7.13	7.13	7.22	7.24	7.27	7.26	7.30	7.30	7.34	7.33	7.28	7.39	7.50
31-Dec-23	7.00	7.08	7.09	7.00	7.04	7.09	7.09	7.14	7.14	7.21	7.17	7.18	7.27	7.41
31-Jan-24	7.02	7.18	7.15	7.00	7.03	7.04	7.04	7.11	7.11	7.17	7.14	7.14	7.21	7.27
29-Feb-24	6.86	7.14	7.11	7.00	7.03	7.07	7.07	7.08	7.08	7.11	7.10	7.08	7.14	7.16
31-Mar-24	6.90	7.04	6.99	7.08	7.02	7.05	7.05	7.07	7.07	7.07	7.11	7.06	7.11	7.13
30-Apr-24	6.98	7.01	7.06	7.08	7.13	7.19	7.19	7.21	7.21	7.21	7.21	7.15	7.21	7.29
31-May-24	6.89	7.00	7.02	7.02	7.03	7.05	7.05	7.06	7.06	7.07	7.07	6.98	7.03	7.13
30-Jun-24	6.79	6.89	6.93	6.98	6.96	7.01	7.01	7.05	7.02	7.07	7.04	7.01	7.03	7.05
31-Jul-24	6.65	6.77	6.79	6.86	6.82	6.84	6.84	6.90	6.90	6.95	6.92	6.93	7.00	7.06
31-Aug-24	6.66	6.71	6.72	6.75	6.75	6.79	6.79	6.83	6.83	6.88	6.85	6.86	6.91	7.00
30-Sep-24	6.50	6.55	6.56	6.66	6.66	6.67	6.68	6.71	6.69	6.73	6.71	6.75	6.79	6.89
m-o-m change (in bps)	3 Month	6 month	1 Year	2 Year	3 Year	4 Year	5 Year	6 Year	7 Year	8 Year	9 Year	10 Year	15 Year	30 Year
30-Sep-23	3	4	1	10	11	7	7	7	8	9	4	8	8	8
31-Oct-23	9	5	12	10	6	11	12	13	14	14	16	14	12	10
30-Nov-23	8	5	-1	-14	-8	-8	-9	-8	-10	-7	-5	-8	-4	-1
31-Dec-23	3	-5	-4	-22	-21	-18	-17	-16	-16	-13	-16	-11	-13	-10
31-Jan-24	2	10	6	0	-1	-5	-5	-3	-3	-3	-3	-3	-5	-14
29-Feb-24	-16	-4	-4	0	0	3	3	-3	-3	-7	-4	-7	-8	-11
31-Mar-24	4	-10	-12	8	0	-1	-1	-1	-1	-4	1	-2	-3	-3
30-Apr-24	8	-3	7	0	11	14	14	15	15	14	10	9	11	17
31-May-24	-9	-1	-4	-6	-10	-15	-15	-16	-16	-15	-14	-17	-18	-16
30-Jun-24	-10	-11	-9	-4	-7	-4	-4	-1	-4	0	-3	3	0	-8
31-Jul-24	-14	-12	-14	-12	-13	-16	-17	-15	-12	-12	-12	-8	-3	1
31-Aug-24	1	-6	-7	-11	-7	-6	-5	-7	-7	-6	-7	-6	-9	-6
30-Sep-24	-16	-16	-16	-9	-9	-12	-11	-12	-14	-15	-14	-11	-12	-11
Change in FYTD (in bps)	-40	-49	-43	-42	-36	-38	-37	-36	-37	-35	-40	-31	-32	-23

# Bank credit growth outpaces deposit growth; regulations prevent dipping into SLR holdings

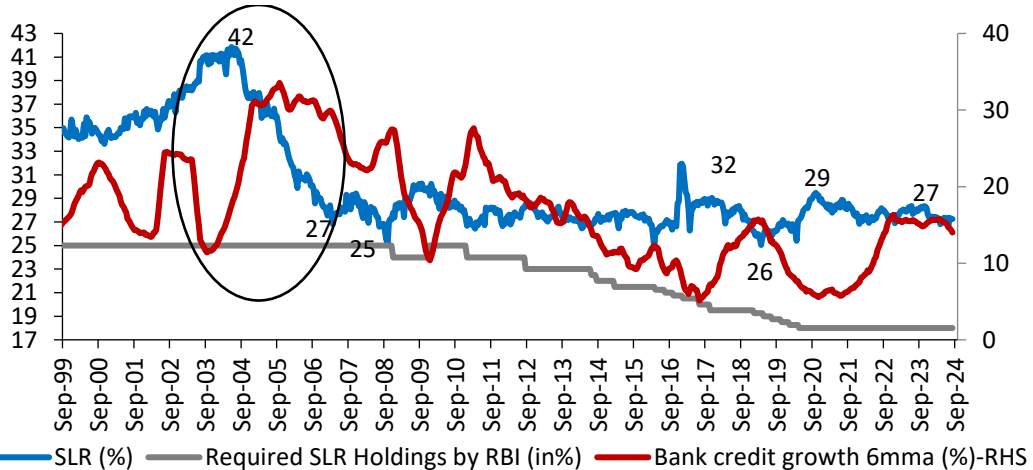
Bank credit growth continues to outpace deposit growth for two years now



Bank credit growth in current financial year mostly on account of personal loans and loans to NBFC

CAGR (%)	2009-11	2017-19	2022-24	2025 (Aug)
Bank Credit	18	15	11	14
Non-Food Credit	18	15	11	14
Agriculture and allied activities	19	8	10	18
Industry	22	2	6	10
Micro & small	13	2	9	13
Medium	0	-1	8	19
Large	26	3	5	8
Services	18	15	14	14
Personal Loans	10	18	16	14
Consumer durables	4	-28	13	10
Housing (Including priority sector housing)	12	16	16	13
Advances to individuals against share, bonds, etc.	10	1	8	27
Credit card outstanding	-13	31	19	20

Previous credit cycles have seen banks lower their SLR holdings. LCR since 2014 has kept SLR holdings high this cycle



Government has reduced the supply of short-term papers to help ease the short-term rates

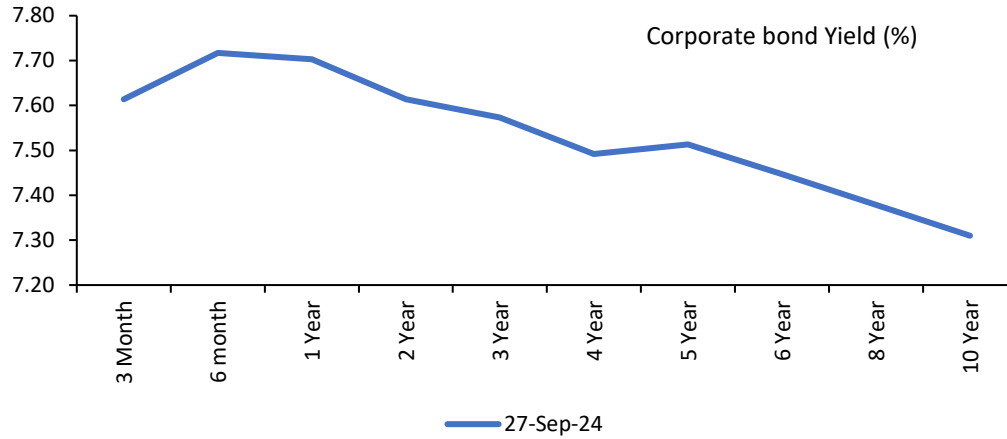
INR billion	FY25BE	FY25 (interim)
<b>FINANCING OF FISCAL DEFICIT</b>	16,133	16,855
Net market borrowings (dated securities, net of buybacks)	11,632	11,750
Gross market borrowings	14,010	14,130
Less Repayment of domestic mkt borrowings	2,378	2,378
Less Net Buybacks	-	-
Short-term borrowings	-500	500
Securities Against Small Savings	4,201	4,662
Receipts from state provident fund	50	52
Net external assistance	160	160
Other capital receipts (internal Debts and Public Account)	-813	306
Drawdown on cash balances	1,404	37

Source: RBI, SBIFM Research; NB: bank credit and deposit data as on 6<sup>th</sup> Sep'24, sectoral deployment of credit as on August'24 end

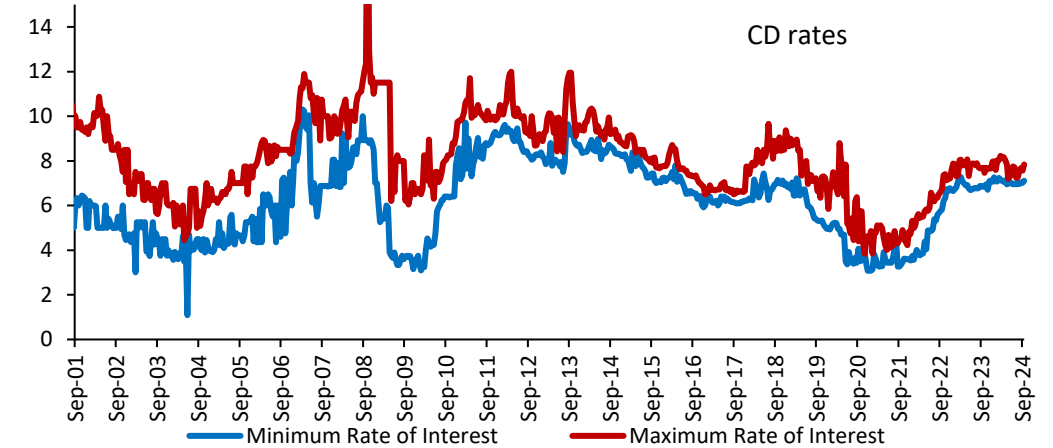


# Dichotomy in G-sec and corporate bond yield Curve; Bank deposit struggles plays a role

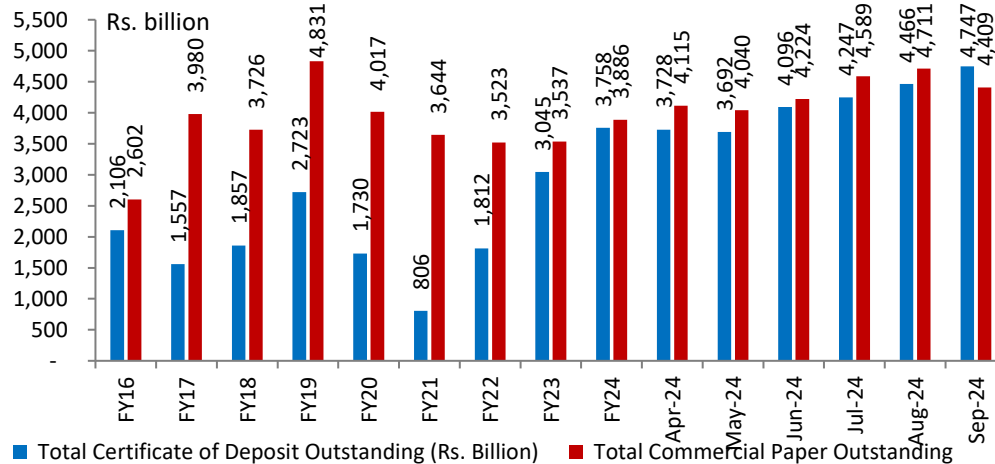
Corporate bond yield curve is inverted; Supply higher in shorter end; Regulatory requirement places greater demand in long end



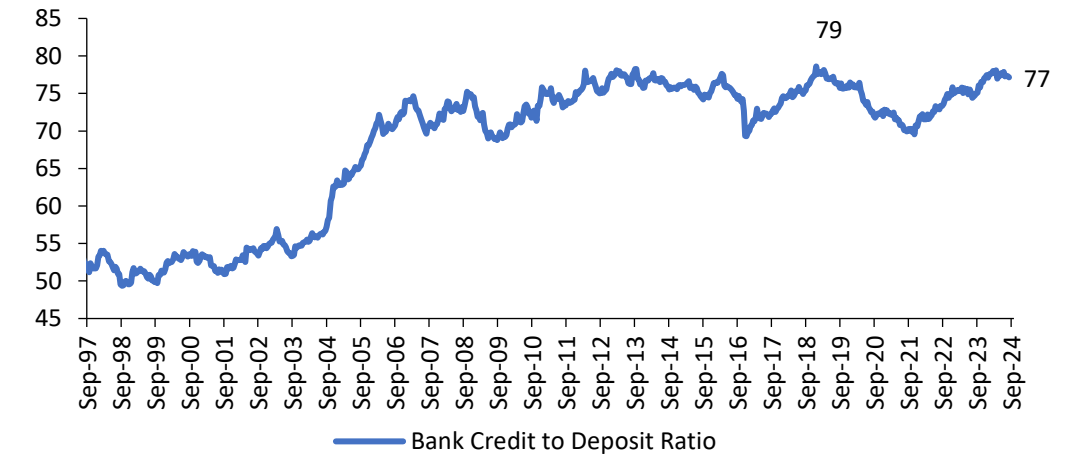
Certificate of deposit (CD) rates range from ~7-8% since 2023



CDs and commercial paper issuances see a rise

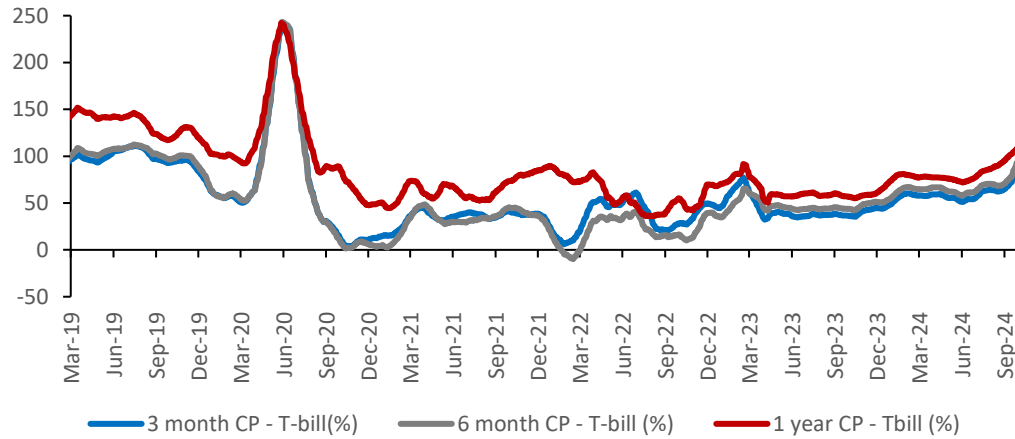


Bank credit to deposit ratio is elevated

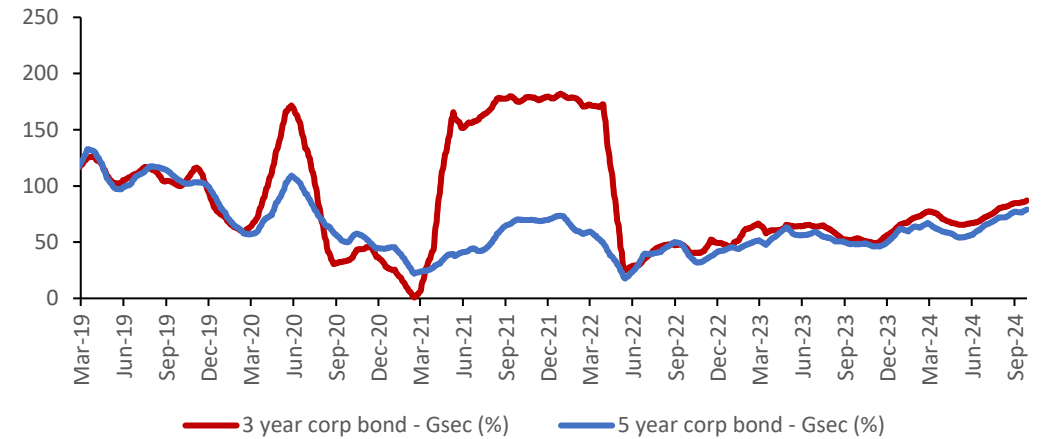


# Robust bank credit growth & elevated credit-deposit ratio results in higher corporate bond yields

Spreads between commercial paper (CP) and Tbill yields have widened

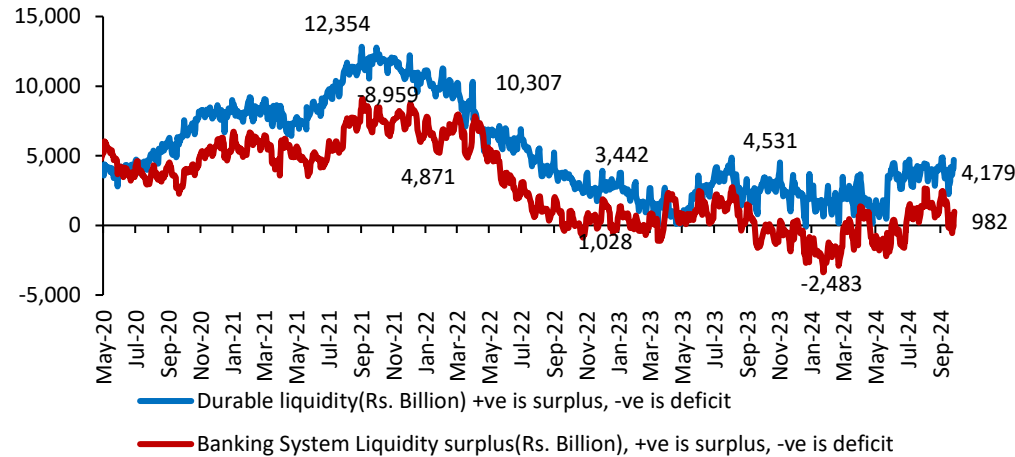


In the 3-5yr segment too, spread between corporate bond and Gsec yields moves upwards

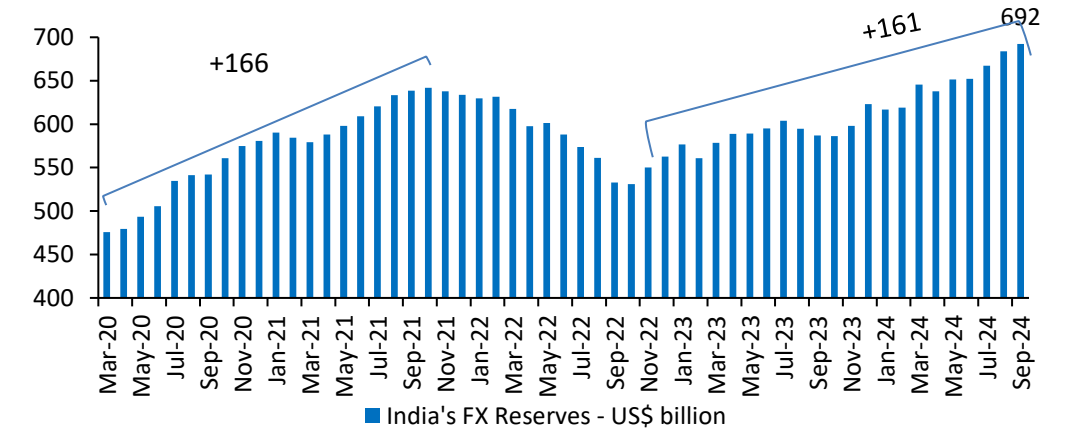


# RBI conducts marginal VRR operations in September to keep banking system liquidity in surplus

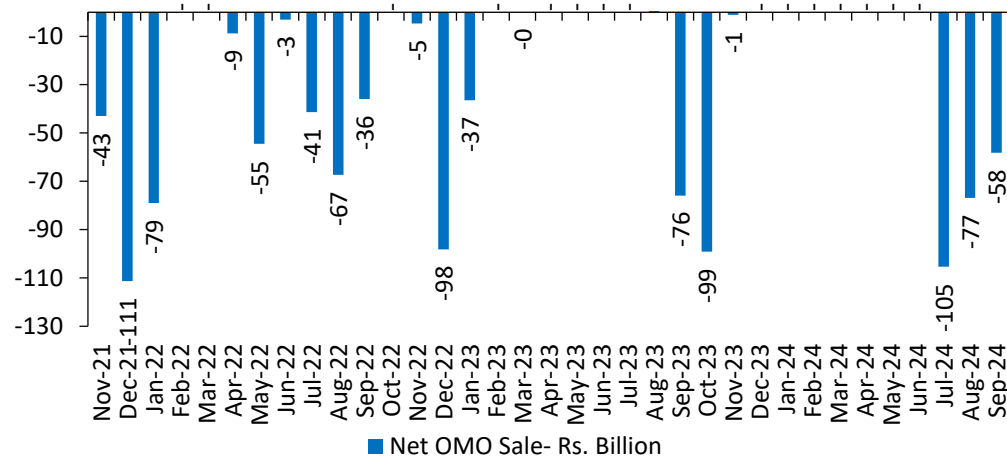
## Banking system liquidity in marginal surplus by end September



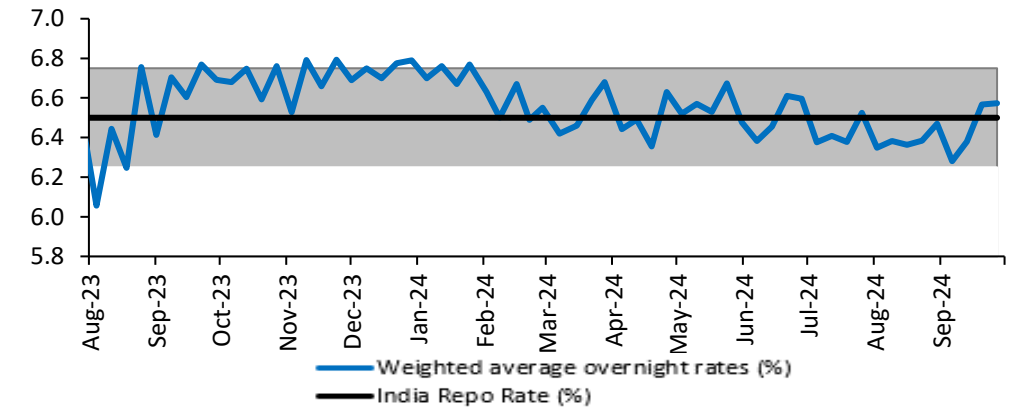
## A strong dollar capital inflow coupled with no material currency leakage has likely aided the improvement in banks liquidity



## RBI tends to conduct OMO sales in instances of prolonged surplus liquidity



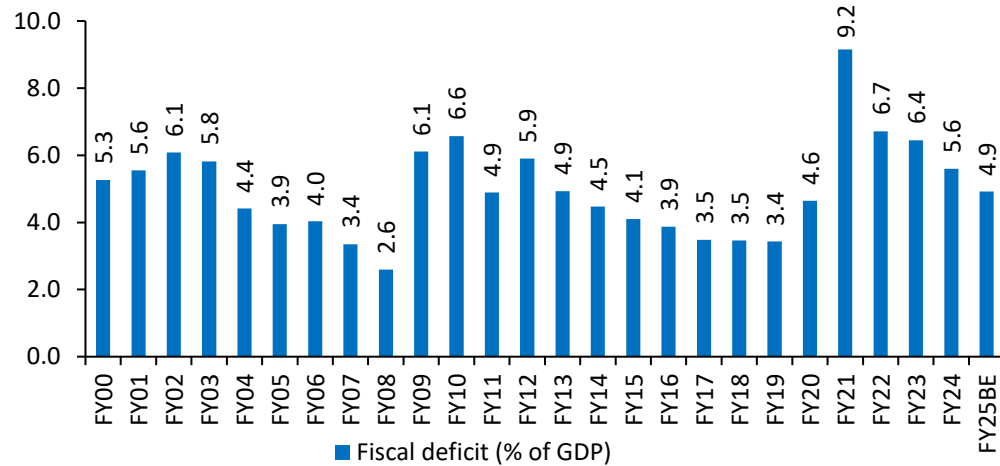
## Slight moderation in liquidity (owing to advance tax outflow) led to VRR auctions to keep overnight rates close to repo rate



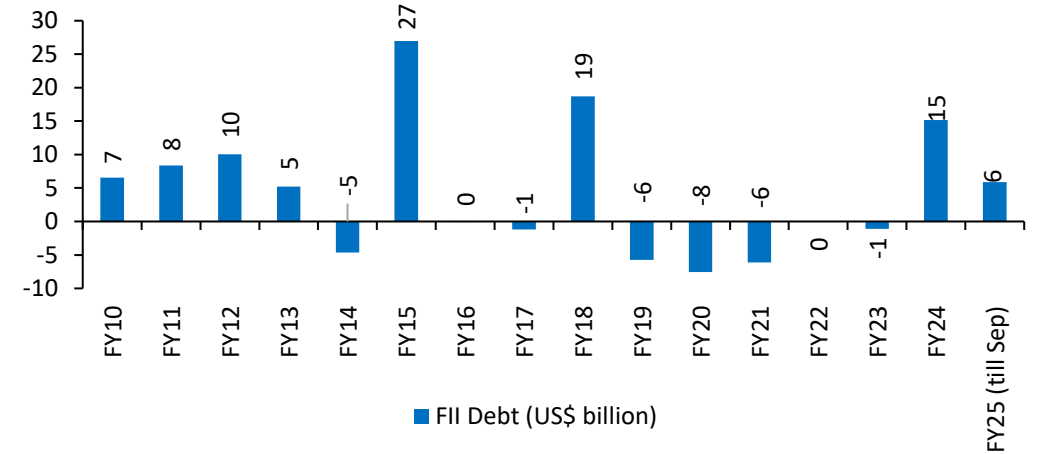
Note: The shaded area represents the policy corridor- where upper end represents MSF and lower end represent

# 2024 is the year of favorable demand- supply for long term Indian government bonds

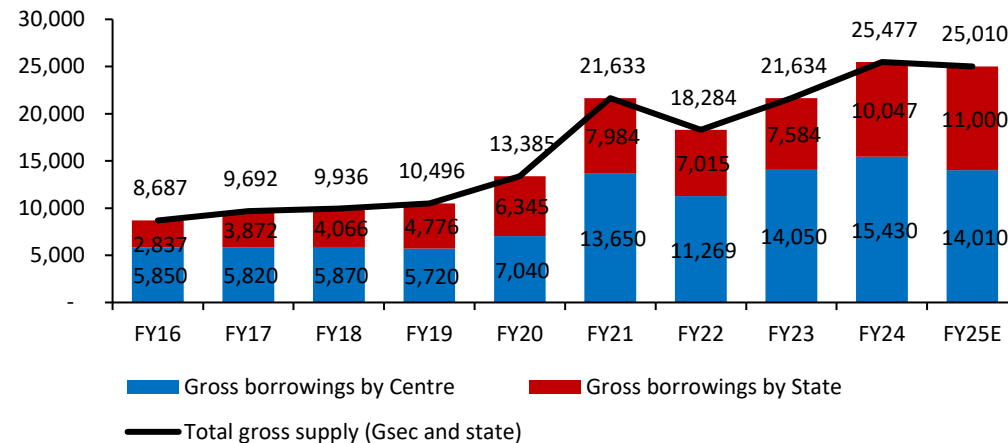
## Central government advocates a faster consolidation in its deficit



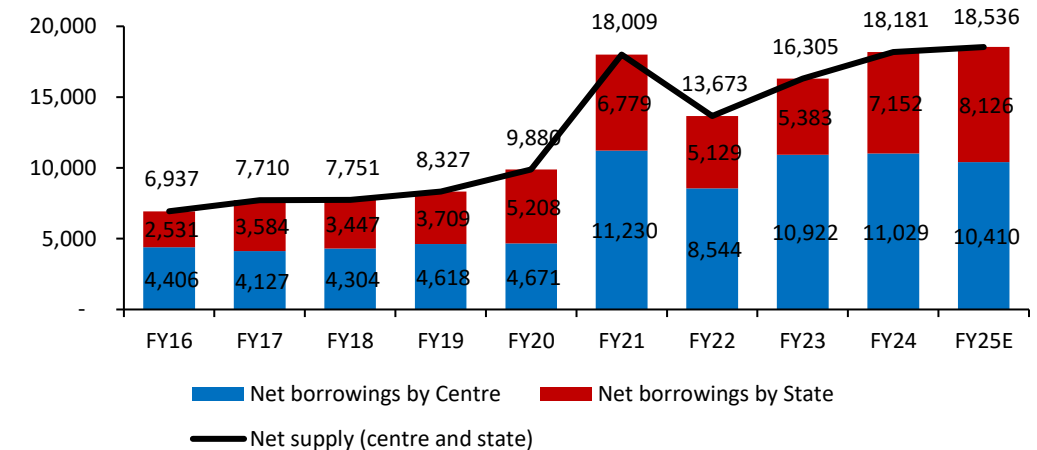
## FII return to Indian debt after 5 years



## Gross supply of government bond is likely to come down marginally in FY25 vs. 18% rise last year



## Net supply broadly flat at an expected INR 18.5tn in FY25



# Central government expenditure underwhelms in 5MFY25; tax collection is moderating

**Capital expenditure declines 19% y-o-y (Apr-Aug); Revex is not strong either (4% y-o-y)**

Cumulative growth (b/w Apr-Aug)-%	FY19	FY20	FY21	FY22	FY23	FY24	FY25
Gross fiscal Deficit	13	-6	57	-46	16	19	-32
Total expenditure	13	10	6	2	9	20	-1
Revenue expenditure	12	11	7	-1	3	14	4
Capital expenditure	21	3	-1	28	47	48	-19
Total Receipts	13	30	-39	114	5	21	18
Net Tax revenue	8	10	-30	127	9	15	9
Non-tax revenue	42	102	-57	73	-21	79	60
Non-debt capital receipts	-3	22	-64	128	108	-51	-42

**Under revex, maximum growth can be seen in interest outgo; Revex ex of interest payment has grown by a mere 2%**

Revex by Key Ministries/ Dept (Rs. Bn)	Amount Spent (FY25(Apr-Aug))	BE	Actual Spend (% BE)
Total Revex	13,514	37,094	36
Agri Dept	372	1,324	28
Fertilizer Subsidy (Dept. of fertilizer)	608	1,641	37
Food Subsidy (Dept of food & public distn)	1,172	2,130	55
Defence Revex	2,026	4,397	46
Interest payments	4,002	11,629	34
Transfers to state and UT governments	415	1,604	26
Pensions	397	792	50
Police	594	1,299	46
Rural Devt	655	1,802	36
Others	3,273	10,475	32

**Tax collection is moderating rapidly; Cumulative tax revenue growth in Apr-August 2024 is lower than the required run-rate**

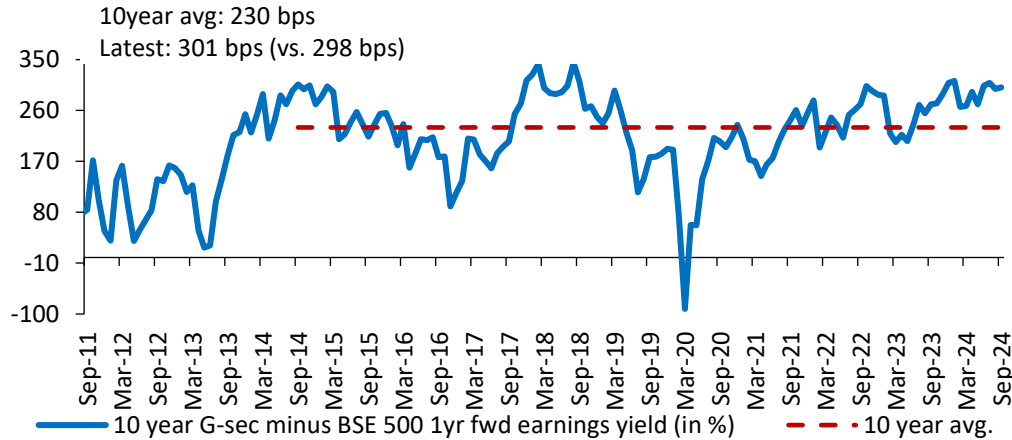
Cumulative Apr -Aug 2024	% y-o-y	Required growth as per FY25 Final Budget and FY24 Actuals
Net Tax Revenue	9	11.0
Gross Tax Revenue	12	10.8
Income Tax	26	13.1
Corporate Tax	-6	13.0
Custom	13	5.8
Excise duties	4	5.0
GST	10	11.6
Total Direct Tax	13	13.1
Total Indirect Tax	9	9.4

**Capex loan disbursement to states have declined while most other sectors are flat FYTD**

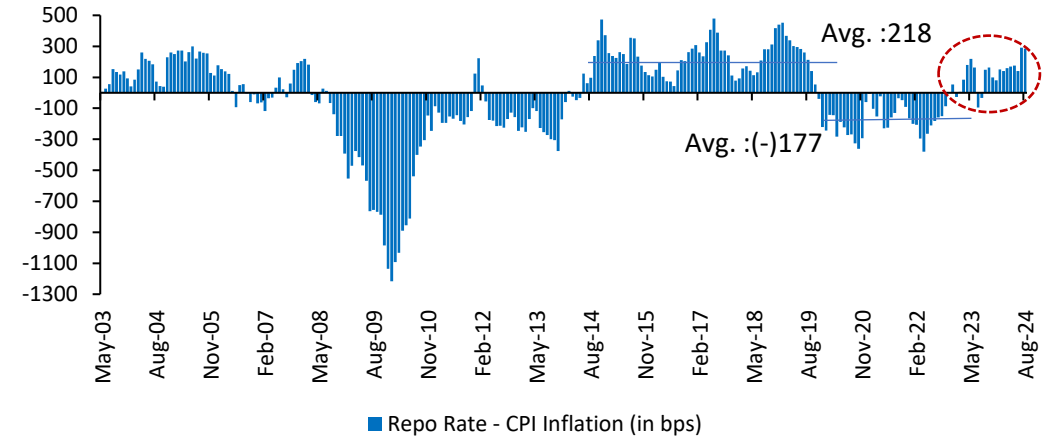
Capex by Key Ministries/ Dept (Rs. Bn)	Amount Spent FY25 (Apr-Aug)	BE	Actual Spend (% BE)
Total Capex	3,010	11,111	27
Defence	346	1,822	19
State Capex loan	289	1,624	18
Road	1,057	2,722	39
Railways	1,028	2,520	41
Telecom ( mainly equity infusion)	22	845	3
Housing and Urban affairs	102	286	36
New Schemes under DEA	12	662	2
Petroleum & Natural Gas	-	11	0
Others	155	2,422	6

# Indian G-sec valuations neutral to marginally attractive

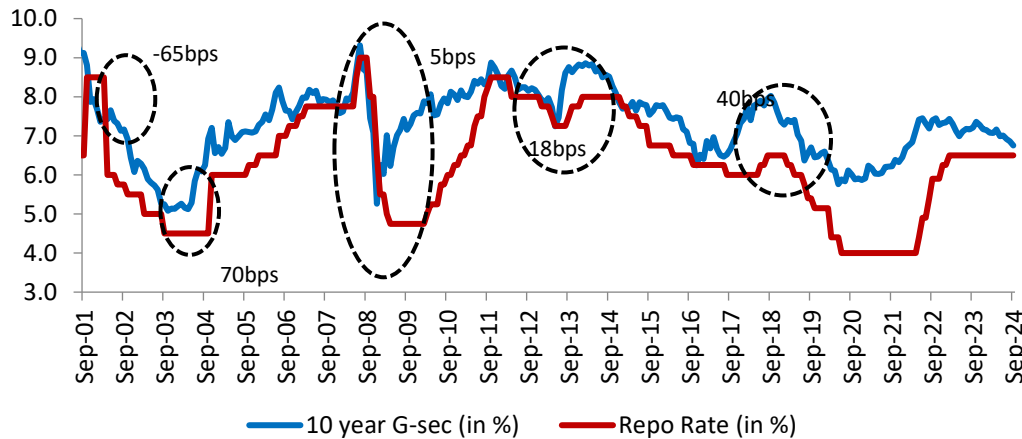
## G-sec spread vs. equity is attractive



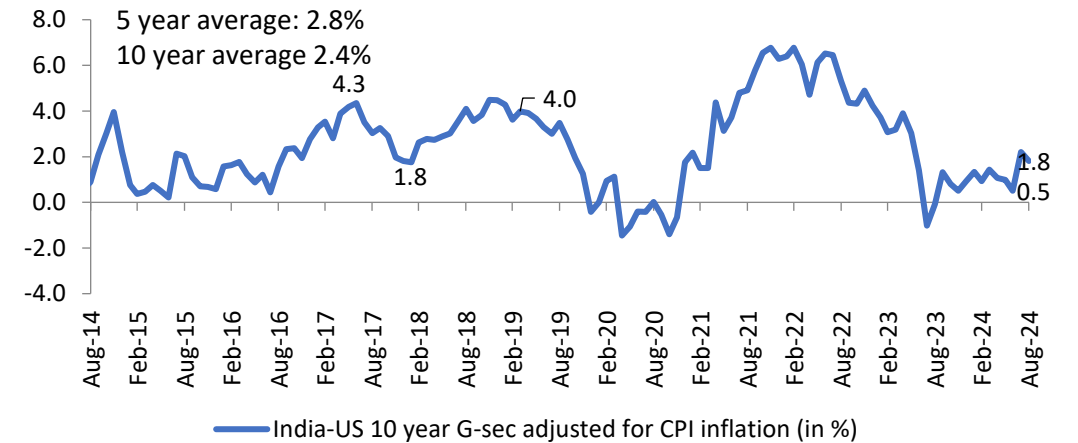
## Real rate turns positive and could further improve as inflation moderates to 4% in coming months



## While near-term outlook stays of an unchanged Repo rate, G-sec spread can compress when there is a greater clarity on rate cuts



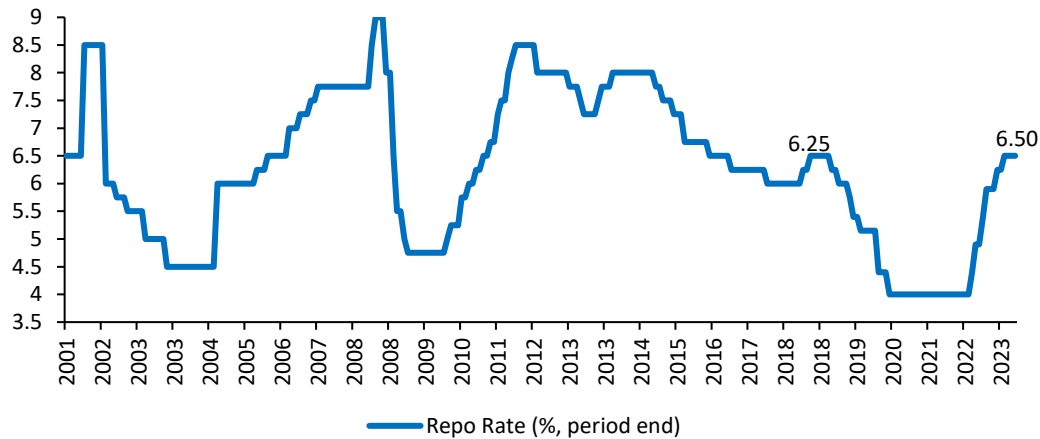
## India-US Real interest rate spread at ~2% pt – lower than its 5yr and 10yr average





# RBI maintains status quo: Fed's rate cut will spark debates on India's monetary easing possibility

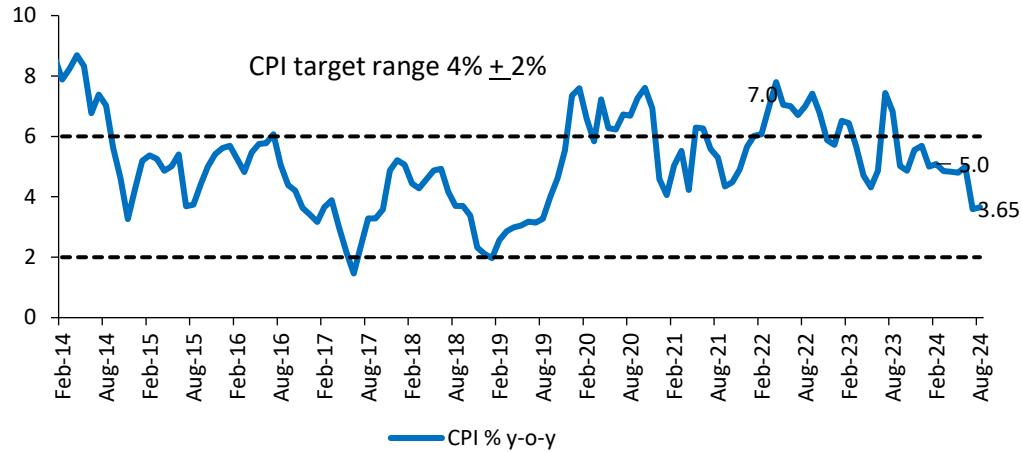
## Repo rate unchanged since April 2023 policy at 6.50%



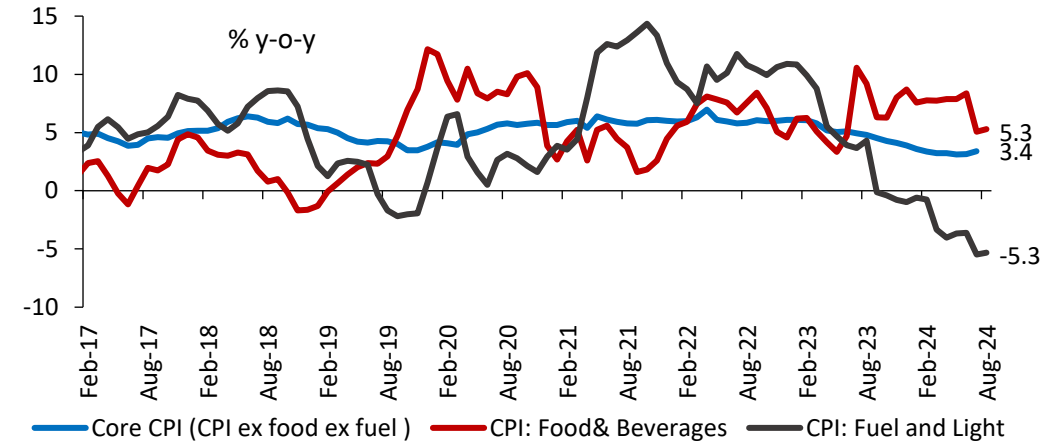
- Status quo on rates (Repo rate: 6.50%, SDF rate: 6.25% and MSF rate: 6.75%) with a majority of 4:2. The stance was retained at 'withdrawal of accommodation'. Expectedly, the focus remained on sustained disinflation to the 4% target.
- Growth expectations for FY25 were retained at 7.2%. Resilient growth allows RBI to "wait" to ensure disinflation towards target.
- CPI inflation projections remain unchanged at 4.5% for FY25 and risks are fairly acknowledged by the RBI.
- The a)60bps upward revision to Q2FY25 CPI projection b)the categorical reinstatement of importance of food inflation in overall inflationary expectations c)the ongoing challenges within the banking system to secure sticky long-term deposit d)OMO sale in July to keep the overnight rate aligned to Repo are strong signals that monetary easing is comfortably some time away in India.
- The chances of rate cut by the US Fed in September is high- they have telegraphed as much. If the US Fed is firmly on the path of monetary easing, market expectations on monetary easing in India could build up. That said, the assumptions of monetary easing in the US begs deeper probing.
- In the September meeting, the Fed may do its best to both sound dovish but nonetheless advocate that further cuts are 'data dependent'. This, means that, RBI could continue to focus on the domestic dynamics of misaligned credit to deposit ratio within banks and elevated food inflation.
- Biggest risk to this call is weather and crude price, while the easing in developed markets could enable more capital flows.

# We maintain a sanguine outlook on India's CPI for remaining 7M FY25

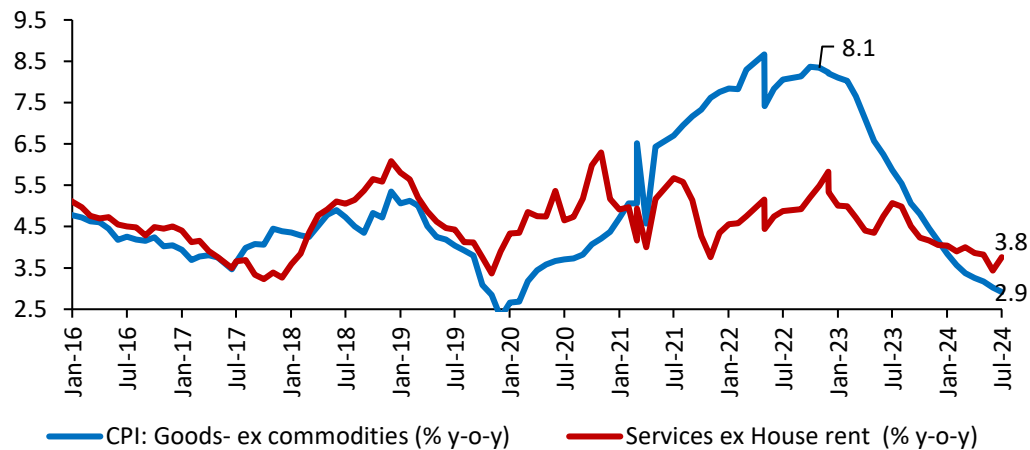
India's headline inflation has fallen below RBI's central target point of 4% since Jul'24



Food inflation softened to 5.3% y-o-y in August compared to ~8% avg. last quarter



Goods and services inflation likely to be contained



- Food inflation softened in this quarter due to the favorable base in vegetables. Unless disrupted by weather conditions, food inflation is expected to average around 5% y-o-y in 2H FY25.
- Core inflation increased slightly to 3.3%/3.4% y-o-y in Jul/Aug from 3.1% due to telecom tariff hikes, but overall, core inflation remains very subdued.
- The inflation outlook for the second half of FY25 appears benign, likely around 4%, suggesting FY25 inflation may undershoot RBI estimates.
- While we do not foresee rate cuts in the next two policies, they cannot be ruled out entirely for Q4 FY25.

# External account dynamics stays healthy; FY25 current account deficit manageable at ~1% of GDP

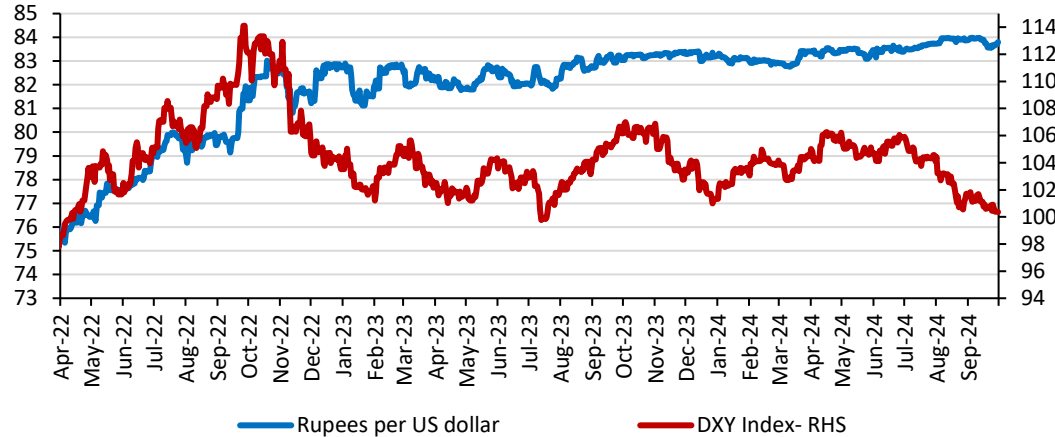
## Current account deficit of under 1% of GDP and US\$ 30-55 bn of BoP surplus expected in FY25

Balance of Payment (US\$ bn)	Jun-23	Sep-23	Dec-23	Mar-24	Jun-24	FY24	FY25E
<b>CURRENT ACCOUNT</b>							
Exports (RBI)	105	108	107	122	111	441	445
% y-o-y	-14.5	-3.2	1.0	5.0	5.9	-3.2	0.8
Imports (RBI)	162	173	178	174	176	686	720
% y-o-y	-13.0	-9.1	0.8	3.1	9.1	-4.9	4.9
1. Trade Balance (RBI)	-57	-65	-72	-52	-65	-245	-275
% GDP	-6.6	-7.3	-8.0	-5.7	-7.0	-6.9	-7.1
2. Services Balance	35	40	45	43	40	163	185
% GDP	4.2	4.8	5.3	4.9	4.4	4.6	4.8
3. Primary Income	-10	-12	-13	-15	-11	-50	-51
4. Secondary Income (Transfers)	23	25	29	29	26	106	105
<b>A. Current A/c Balance (1+2+3+4)</b>	<b>-9</b>	<b>-11</b>	<b>-10</b>	<b>5</b>	<b>-10</b>	<b>-26</b>	<b>-36</b>
% GDP	-1.1	-1.3	-1.2	0.5	-1.1	-0.7	-0.9
<b>CAPITAL ACCOUNT</b>							
5. FDI (Net)	4.7	-0.8	4.0	2.3	6.3	10.1	25.0
6. FPI (Net)	15.7	4.9	12.0	11.4	0.9	44.1	40.0
7. Loans	2.2	3.3	-5.6	1.8	6.0	1.6	10.0
8. Banking Capital	12.9	4.3	16.4	6.9	2.9	40.5	5.0
<b>B. Capital Account Balance (5+6+7+8+9+10)</b>	<b>34</b>	<b>13</b>	<b>15</b>	<b>25</b>	<b>14</b>	<b>87</b>	<b>80</b>
% GDP	4.1	1.5	1.7	2.8	1.6	2.4	2.1
C. Error and Omissions	-0.8	1.0	-0.3	0.5	0.6	0.5	0.0
<b>D. Overall Balance (A+B+C)</b>	<b>24</b>	<b>3</b>	<b>6</b>	<b>31</b>	<b>5</b>	<b>64</b>	<b>44</b>
% GDP	2.9	0.3	0.7	3.5	0.6	1.8	1.1
<b>Increase in Reserves due to BoP Rupee vs. US\$ (average)</b>	<b>24</b>	<b>3</b>	<b>6</b>	<b>31</b>	<b>5</b>	<b>64</b>	<b>44</b>
	<b>82</b>	<b>83</b>	<b>83</b>	<b>83</b>	<b>83</b>	<b>83</b>	<b>84</b>

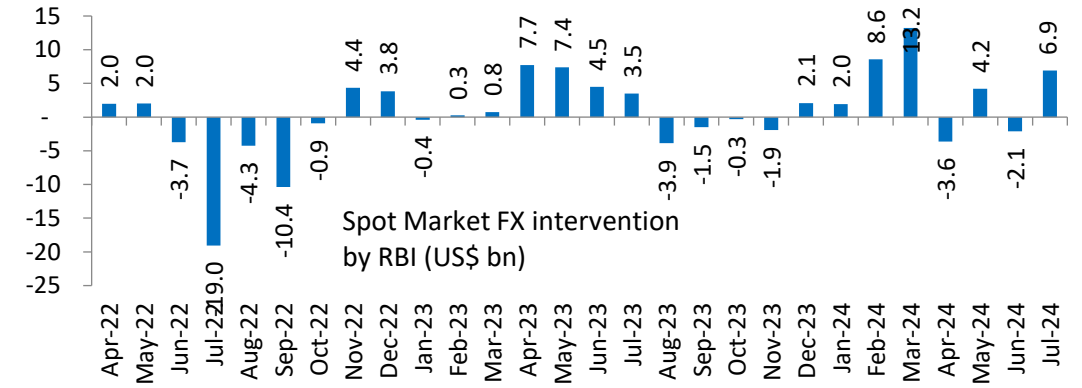
- Q1 current account balance switched back from a surplus of US\$ 4.6bn (in Q4 FY24) to a deficit of US\$ 9.4 bn, led almost entirely by a US\$ 13bn of deterioration in trade balance (Q1 FY25 deficit at US\$ 65 bn vs. US\$ 52 bn in Q4 FY24).
- Net invisibles moderated by US\$ 1 bn but stays broadly steady at a surplus of US\$ 55 bn.
- Capital account surplus also moderated in Q1 FY25, largely on account of softer FII inflow. During Q1 FY25, the momentum in debt FII inflow has moderated as the bond inclusion related inflow has normalized.
- As a result of higher current account deficit and weaker capital inflow, BoP surplus softened from US\$ 31 bn in Q4 FY24 to US\$ 5.2 bn ( still a surplus).
- FX reserves increased by US\$ 6bn during the quarter from US\$ 646bn to US\$ 652bn.
- We expect a marginal deterioration in Q2 and Q3 FY25 CAD to 1.5-2% of GDP, but a seasonal improvement in final quarter of the fiscal.
- To sum, FY25 CAD is likely to aggregate to 1% of GDP- which portrays a healthy external account and manageable levels from India's macro stability point of view.

# Rupee stays highly range bound since 2023; Marginal depreciation stays in cards

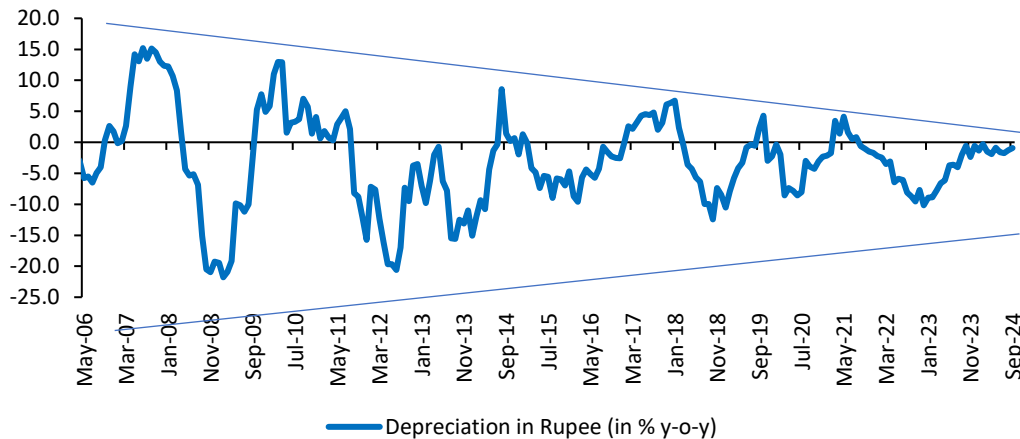
Rupee trades in a very tight range of 81-84/US\$



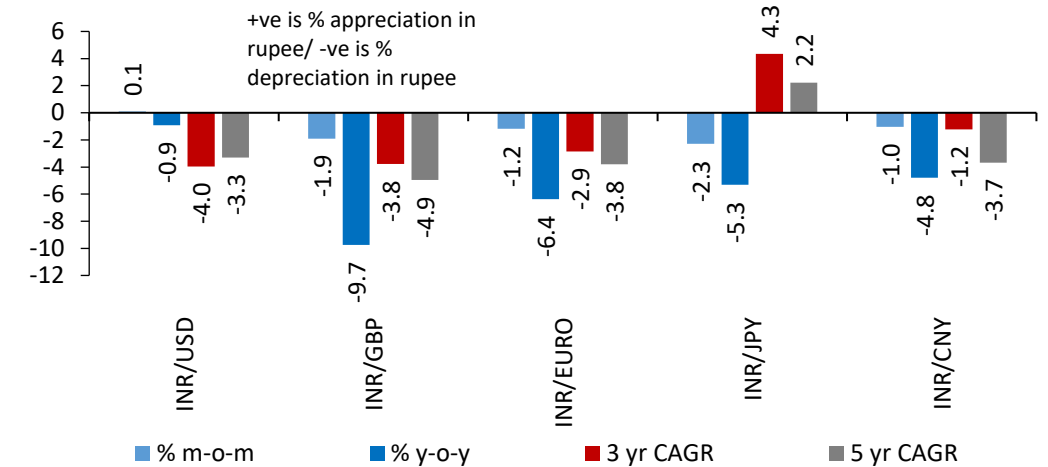
RBI's intervention keeps rupee anchored



Macro stability and active RBI intervention drives lower volatility in rupee and lesser bouts of depreciation

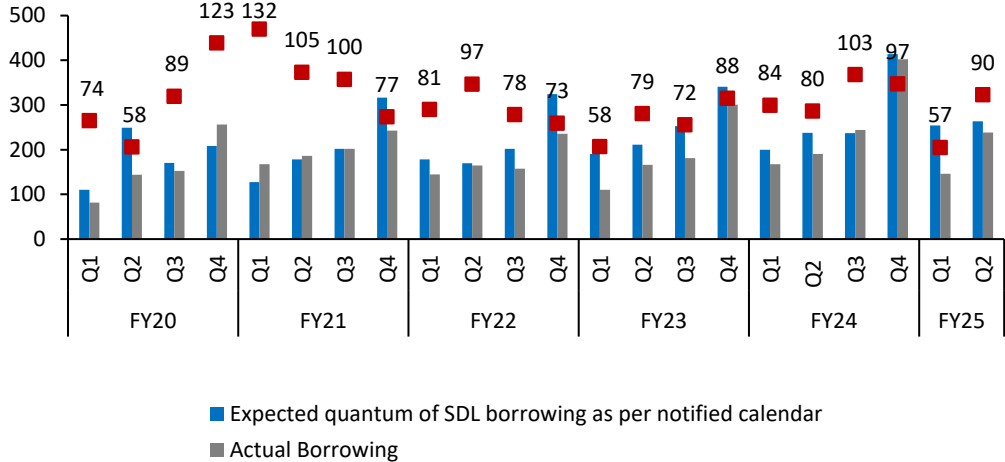


Rupee's movement against other key currencies

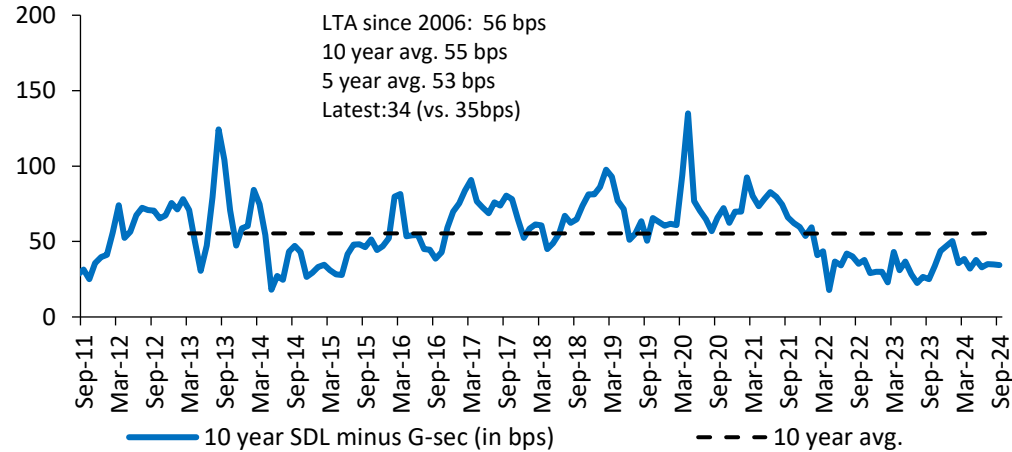


# SDL issuances picked up in Q2 FY25; Q3 FY25 calendar relatively higher at INR 3.2 trillion

1HFY25 SDL issuances at 74% of their indicated calendar amount



SDL spreads flat m-o-m in August and September



Source: RBI, Bloomberg, CEIC, CAG, SBIFM Research

# FII are net buyers of Indian government bonds since May 2024

## India witnessed Debt inflows in Sep'24

EM FII Debt inflow US\$ million	2022	2023	Jun-24	Jul-24	Aug-24	Sep-24
China	(1,46,410)	24,760	1,35,792	1,61,097	1,91,471	1,92,349
South Korea	54,020	60,647	3,046	1,958	6,463	6,995
Mexico	3,949	5,019	590	(2,183)	1,933	2,539
Indonesia	(7,070)	5,142	117	305	2,492	1,377
Thailand	6,227	319	(287)	779	762	420
South Africa	(15,812)	(17,598)	(45)	1,069	95	161
India	(2,012)	8,445	2,136	2,615	1,958	85
Ukraine	(1,096)	(387)	(99)	(24)	(108)	(51)
Brazil	18,358	(9,967)	(3,973)	(301)	(2,145)	-
Malaysia	(732)	3,767	(549)	1,099	1,394	-
Poland	6,936	9,388	2,442	2,761	-	-
Czech Republic	(14,477)	(1,535)	3,243	1,060	-	-
Philippines	6,334	3,073	38	-	(19)	-
Bulgaria	1,053	1,940	1	33	-	-
Russia	-	-	-	-	-	-

## FII flows in EM bonds are muted despite healthy inflation adjusted returns

Real rates	10 Year Gsec Yield (% mth end, Aug'24)	CPI Inflation Aug'24	Real Rate (% , 10 year G-Sec Yield minus CPI)	12M FX forward premium (in %) - Aug 2024	10 year G-sec yield adjusted for 12m fwd premium (in %)- Aug 2024
Brazil	12.2	4.2	8.0	5.9	6.3
South Africa	10.6	4.4	6.2	7.7	2.9
Mexico	9.7	5.0	4.7	10.1	-0.5
Indonesia	6.6	2.1	4.5	6.3	0.3
Colombia	10.1	6.1	4.0	9.3	0.8
Phillippines	6.8	3.3	3.5	4.5	2.3
India	6.9	3.7	3.2	2.2	4.7
Hungary	6.3	3.4	2.9	5.6	0.7
Thailand	2.5	0.4	2.2	2.1	0.4
Malaysia	3.8	1.9	1.9	2.7	1.0
China	2.2	0.6	1.6	1.6	0.6
Poland	5.4	4.3	1.1	5.7	-0.3
South Korea	3.1	2.0	1.1	2.6	0.5
Taiwan	0.5	2.4	-1.9	1.2	-0.7
Turkey	28.5	52.0	-23.5	49.5	-20.9

# Debt Outlook: Near-term fundamentals dictate neutral to marginally favorable outlook

- On September 18, the US Federal Reserve cut the Fed Funds rate by 50 basis points, bringing it down from 5.25-5.50% to 4.75-5.00%. Fed Chair Jerome Powell noted that the labour market has cooled, no longer serving as a major inflationary factor.
- Consequently, for now the data seems to suggest that the bond market seems to have overestimated the extent of rate cuts (250bps in one year vs. Fed projection of 250bps by end 2026). Thus, multiple data suggest that our long-standing comfortable range of 10yr UST at 3.5-5.5% still holds true. Thus, with 10-year UST at 3.7%, most of the gain is already in the price.
- The growing fiscal deficit presents a structural risk for inflation, compounded by potential tax cuts or increased public spending depending on the outcome of the upcoming elections.
- Currently, the bond market is experiencing curve steepening, with long-term bonds selling off and equities rising, reviving the negative correlation between the two. This shift could be attributed to inflation settling below 3%. Further, the restoration on negative correlation between bond and equity are a cyclical positive for bonds, even as structural headwinds remain. Thus, investment rationale in the bond market has resurfaced.
- For gold, this may mean a temporary slowdown in price increases, though we still recommend maintaining exposure in the precious metals as a portfolio diversifier and uncertainty hedge due to ongoing structural challenges in the bond market of persistently high US deficit and government debt.
- Regarding the dollar, US monetary easing typically weakens the currency. But another factor required for a strong dollar depreciation is better growth outlook outside the US. However, during this cycle, global growth appears weak, particularly in China and Germany. Further, a weakening dollar usually leads to stronger global equity performance, the Fed's support for US equities may counter this trend, suggesting a sideways movement for the dollar in the near term.
- Indian government bond yields fell across both shorter and longer maturities.
- Additionally, banking system liquidity was near neutral/marginal surplus levels in September. With strong dollar capital inflows, liquidity in the Liquidity Adjustment Facility (LAF) is expected to remain in surplus.
- In India, expectations for rate cuts are building, which may compress spreads (currently, the 10-year G-sec trades at 6.75%). The inflation outlook for the second half of FY25 appears benign, likely around 4%, suggesting FY25 inflation may undershoot RBI estimates. While we do not foresee rate cuts in the next two policies, they cannot be ruled out entirely for Q4 FY25.
- Further, macro prudential measures have led to moderation in bank credit growth from 16-17% in FY24 to 13% in FY25. Banks have their own deposit struggle. At the margin Indian growth appears to be moderating. All these suggests that, either in the form of the rate action or liquidity action or macro prudential measures, we could get monetary easing in India. Even for the India specific demand supply reason, Indian bonds could do well in the near-term. To sum, we are positive on Indian bonds and see scope of further fall in Indian yields despite compressed spreads.

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