Global

Global markets remained fairly positive through the month of February, with the Indian markets remaining divergent for most part. While the second half of the month saw a sharp pickup, the weakness and divergence of the first half dragged down the monthly returns that remained in the negative. February saw the Senate pass the funding bill that averted another partial US government shutdown. Subsequently, Trump declared a national emergency, bypassing the congress to acquire funding for the wall. 16 US states have sued Trump administration over this and the House has launched investigations against Trump for abuse of presidential powers. The month saw increasing positivity over US-China trade talks with two high level talks first with negotiations that covered some of the most contentious topics of forced technology transfers, IP protection, non-tariff barriers, agriculture and trade balance. Trump has also delayed the proposed tariff increases on Chinese good on the back of progress made in these talks. While the US-China trade narrative witnessed positivity, signs of friction were seen emerging between the US and EU, ahead of trade talks around the corner. On the macro front, weak prints and waning fiscal tax-stimulus in the US, brought back concerns over the US economy losing steam. Although the Fed's commentary on US growth remained largely positive, the weak macro prints have led the markets expecting the Fed to extend its rate pause through 2019. Europe's economy also remained under pressure with its largest economy Germany, narrowly avoiding a technical recession in Q4 2018. The Eurozone has also cut its growth forecast for 2019 to 1.3%y/y from an earlier forecast of 1.9%. Moving to China, various types of fiscal stimuli were announced to support its slowing economy that included announced tax breaks for small businesses run by recent graduates and low-income workers with more announcements.

Central banks

Central banking language especially in developed markets have seen a clear shift towards incremental accommodation. With likely global softening round the corner, this accommodative stance appears likely to continue through this year with emerging central banks likely following suit. The Fed indicated 'patience' in January and providing forward guidance to the markets on a possible stop to its balance sheet run-off. A large segment of the markets are expecting no hikes in 2019 with some even considering the possibility of a rate cut. While the Fed remained largely positive on domestic growth, in its semi-annual monetary policy report to the Congress, it acknowledged weakening in consumer and business spending. It also flagged "softer global and economic conditions" as one of the reasons behind its decision of pausing the rate hike cycle last month. After holding its rates in January, the ECB continued to remain soft on Eurozone growth. With Eurozone economies under stress, the ECB is expected to push its rate normalisation cycle well into 2020. Markets also expect TLTROs or Targeted Long Term Refinancing Operations to make a comeback soon. The TLTROs this time are expected to be of shorter term with variable rates that track ECB's main refinancing operation. Markets await more details to be released in the March or June ECB meetings. On the domestic monetary policy front, RBI under its new Governor, Mr. Shaktikanta Das cut rates by 25 bps bringing the repo rate to 6.25%. The rate cut was on the back of an opening that the RBI saw in the output gap, the need to boost private investment and the sharp downward revisions it observes in households' inflation expectations.

Domestic

Apart from the India-Pakistan related tensions over the Pulwama attacks and India's retaliation on the same; the domestic front in February saw the interim budget presented in the parliament. FY20 Budget saw the fiscal deficit remain flat at 3.4%GDP, after a 10bps slip in FY19RE. The budget was an overall positive with focus was from the bottom of the pyramid up to the middle classes. Farmers received direct investment support scheme, rural households were targeted with higher interest subvention, unorganized labourers received a social security pension blanket and middle classes with upto Rs.5 lakh of taxable income got full tax rebate. Retail inflation continued to ease further in January, indicating that inflation had not bottomed out yet as markets had originally expected. Wholesale inflation also continued to ease in February. The RBI board approved a transfer of Rs.280bn for its half year ending Dec'18 to the government. The total surplus transfer to the govt. now stood at Rs.680bn. February saw RBI cut rates by 25 bps. The justification for this could be found in RBI's minutes that showed MPC members take a relatively dovish stance on inflation. All members without exception appeared to appreciate and take cognisance of the shift in inflationary expectations. The month also saw the Union Cabinet approve a new electronics policy that aimed at creating 10 million jobs, a scheme to build 19.5 million houses for the rural poor, a Rs.300bn rapid transport system for the National Capital Region and policy changes to make oil exploration more attractive. In additions to the above, the Cabinet Committee on Economic Affairs also allowed captive coal mines to sell up to 25% of their output in the open market, 40,000 MW of new rooftop solar projects, a new solar power scheme for farmers and the extension of key schemes for three more years. The Cabinet also approved an additional dearness allowance (DA) of 3% over the existing rate of 9% for government employees and pensioners, effective from January 1st 2019.

Market Outlook

We continue to believe that markets like these are good for long term investors, as they provide an opportunity to participate in well run companies at discounted prices.

Positives:

1. **Decent Earnings season:** we have had a decent earnings season. Nifty ex-oil companies delivered 10% earnings growth and BSE100 ex-oil delivered 10% earnings growth. Oil companies had major write off in inventories due to sudden and sharp fall in oil prices.
2. **RBI cuts rate & more to come:** With inflation being fairly under control and economic growth rate weakening, a case for rate cut was available and RBI has snatched it. This in our opinion should help consumption demand.
3. **Budget 2019 "Focus on Consumption":** Budgets before general elections have become socialistic and this year budget too was not an exception. Keeping budget numbers under check, government has proposed two measures to put more money in the hands of farmers and people below Rs0.5mn income level. The measures in our opinion are stimulative and would reflect in increased demand for low ticket consumption items during 2019.
4. **"Pause" The Fed:** In what can be termed as a turnaround of sorts, US Fed has paused rate hikes in Jan against expectations and also sounded less hawkish on future rate hikes. This is good news for emerging markets, particularly India.
5. **Trade talks "move forward":** Recent negotiations witnessed a narrative of progress with China mentioning that there was a "consensus in principle", and Trump calling talks as "very productive". The March 1st deadline is also expected to be extended by another 60 days. We expect the final deal will be after prolonged deliberations and not going to be a quick fix. Any trade deal needs to be "substantial, verifiable, and enforceable", urged Democratic Senators in a letter to Trump. With concerns of global growth arising, a quick deal between the two largest economies in the world would be helpful.

Negatives:

1. **Volatile Oil:** Brent Oil prices after rising to peak $85 in October 2019, crashed by 40% in one month to $50 and then now again moved up 30% in last 2 months. Indian markets are again getting jittery over quick move in oil prices. We expect oil prices to remain volatile due to supply cuts announced by Saudi Arabia, but would settle at lower levels in H2 when US shale supplies starts flooding into market. A range between $60-70 is good for Indian economy and markets.
2. **Global growth slows down:** The Eurozone composite PMI numbers (final) moved to its lowest since July 2013. A Fed survey of banks indicated that increasing number of US banks were reporting weakening demand for auto and credit cards loans in 2018. The bellwether Caterpillar's global sales saw a drop for its seventh consecutive month. The company highlighted a slowdown it was experiencing in Asia. would be its first contraction in the region since mid-2016.