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1st November 2023

Dear Investor,

Greetings! Let me wish you and your beloved a Happy Diwali and New Samvat Year 2080 in advance. Most markets correct in Sept/October and Indian markets were no exception and corrected sharply. The Nifty benchmark index corrected 3% to close at 19079 after touching a low of 18837 during the October month. While stocks came under pressure last week, this was more likely due to the sharp rise in US 10 years bond yields at 5.05%, more pronounced moves in geopolitically sensitive asset classes like oil (Brent crude up 11%) and gold (up 9%) post the West Asia attacks.

Financial markets least impacted due to war

Its' important to remember that geopolitical events have rarely caused a global recession or left a lasting mark on markets. Therefore, the best course of action is almost always to stay invested and use the opportunities to invest in long term. In this case, the Israel-Hamas war comes at a time of already elevated geopolitical tensions, with the ongoing war in Ukraine, and the intense rivalry between the US and China. Despite all this the US economy has remained very resilient and expect inflation to continue to cool, and yields to trend lower over the next 12 months. We do not see wider economic or market impacts stemming from the conflict in its current form. Unlike Russia's invasion of Ukraine, with its significant direct and indirect impacts on global supplies of energy, fertilizer and food stuffs, the war between Israel and Hamas— assuming it does not spread into a wider regional conflict—will likely be less disruptive to the global supply chain.

All eyes on oil

Could Oil prices spiral? When it comes to the market reaction from here, oil remains the main transmission mechanism, and any significant move higher is the key risk to watch. Hopefully, we don't expect oil prices to spiral out of control. We believe the most likely scenario is that Brent crude oil fluctuates between USD 90/bbl and USD 100/bbl, alongside any local escalations such more broader support of Arab countries. While pressure toward the USD 105–110/bbl range is possible with an incremental reduction in Iranian exports, there is currently spare capacity sitting with OPEC+ to help offset the impact. And if at all the oil prices rises it cannot sustain for long duration. Stephen Dover, Head of Franklin Templeton Institute evaluates the market implications of the conflict in the Middle East which has raised geo-political concerns. The key highlights have been summarized below.

- We do not see wider economic or market impacts stemming from the conflict in its current form.
- In the event the current conflict was to escalate beyond its present scope, oil prices could spike and potentially supplies could be disrupted.
- Increase in the global geopolitical temperature will accelerate the trend towards regionalization of trade, another reason for further reversal of globalization.
- We do not believe that the conflict in its current form is likely to have significant impacts on global economic growth, inflation, corporate profits, interest rates or exchange rates.

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India Market Outlook:

Domestic economy projects resilience through a mix of robust macro and micro indicators that show pick up in investments and recovery in domestic demand. Healthy increase in the domestic activity tracker, Purchasing Managers' Index (PMI) in an expansionary mode, moderation in Consumer Price Index (CPI) inflation, improvement in consumer sentiment index and an uptick in rural economic activity bodes well for growth projections. Together, they reflect a cyclical uptrend along with the positive effects of structural changes. Headwinds are mainly from the global economy and geopolitics. Hence, the key risks to domestic growth projections are from slowing global growth and high US treasury yields that could impact flows to emerging markets. Rise in crude oil prices could increase inflation and delay easing of interest rates. With four states heading for elections in November-December 2023, domestic markets could likely experience heightened volatility in the coming quarter.

In its latest monetary policy release earlier this month, the Reserve Bank of India (RBI) kept the repo rate unchanged at 6.50%. It continued to keep policy rates unchanged after having raised the repo rate by 250 bps (basis points) since May 2022.

Stronger than ever foreign reserves (closer to $600bn), intelligent mix of crude imports (thus creating a margin of safety against rising crude prices), strong domestic investor flows counterbalance to FPI outflows, resilient government fiscal balances, strong non-food credit growth (15%+), unleveraged corporate Balance Sheets, strong deposit base for banks to lend etc. are few other factors that help support our conviction on medium term India story. The equity market should remain well supported in coming weeks as we believe India's solid macro fundamentals along with corporate profitability should aid buying interest on dips.

India’s Macro Resilience

• Despite below normal and erratic monsoon season this year, consensus GDP forecast for FY 2023 saw 10 bps upgrades to 6.2%. India's macro environment remains resilient largely driven by humongous government spending, better tax collections and some pick up in private spending

• India's fiscal deficit for the first five months of FY 2024 stood at 36% of full year target versus 34% last month and we expect the spending should accelerate ahead of the general elections next year and as the several state elections lined up during the remaining months of the current fiscal year. August saw sharp improvement in government tax collections, which enables it to spend aggressively as planned. capex for the six months of the current fiscal year jumped 48% YoY or 23% as budgeted.

• Festive season buying and the upcoming cricket world cup are the major triggers for the consumption and service related sectors. The E-way bills generation reached a record high in the recent months of Sept/Oct shows robust growth supporting encouraging GST collections in coming months.

• India's recently published service PMI clocked 13-year high of 61, which is encouraging.

Valuation

The financials, manufacturing companies along with mid/small cap have shown remarkable performance during the first half 2024 as expected. The new private capex and improving utilization should provide good operating leverage across sectors and keep equities strong. We continue to believe it is time for alpha with earnings growth being higher outside the Index. This is where we have positioned our investment portfolio. Happy Investing!!!

Thanks with Regards,

CA Rakesh Doshi
Principal Officer & Fund Manager
KRIIS – The Portfolio Management Company