

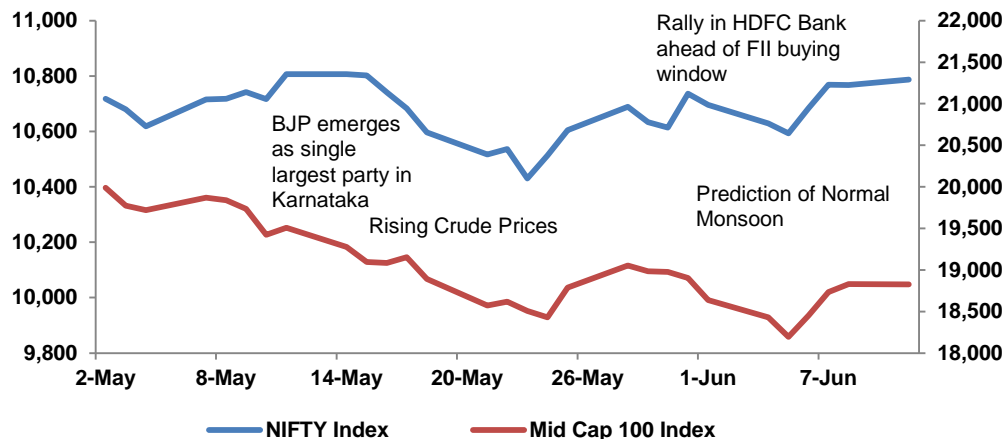
Equity & Debt Strategy

Mid June – July' 2018

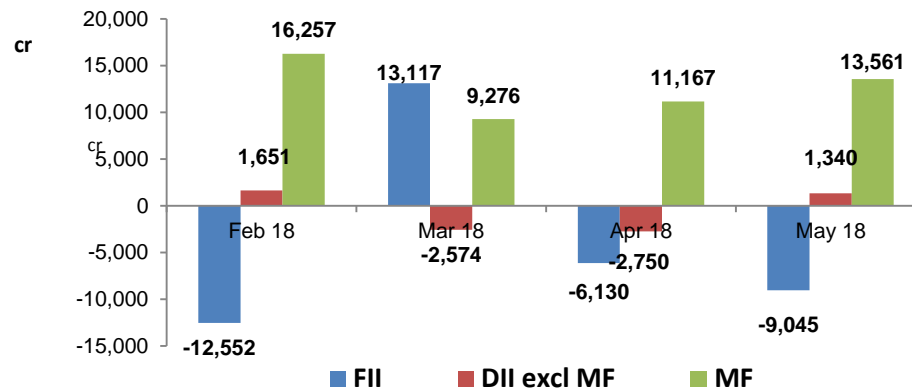
**Equity Market Update
&
Equity MF Strategy**

Wide divergence in Large Cap and Mid Cap performance in May-June. M&M, HUL, Kotak Bank, TCS, Bajaj Finance lifts Nifty50

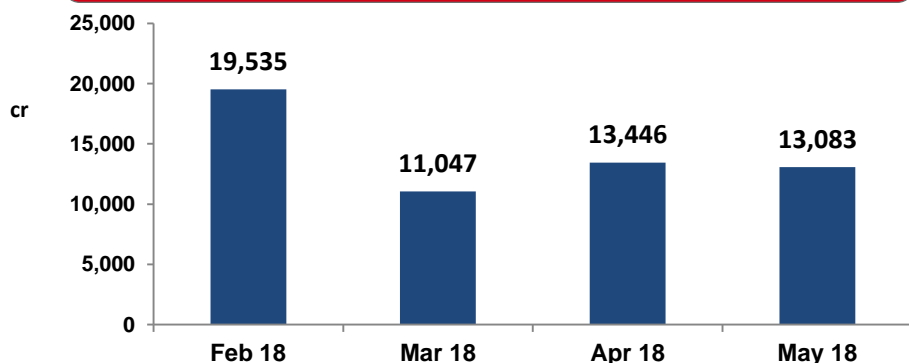
Nifty 50 flat in May but Midcap 100 corrected by 6.8%



FII selling and MF buying continues

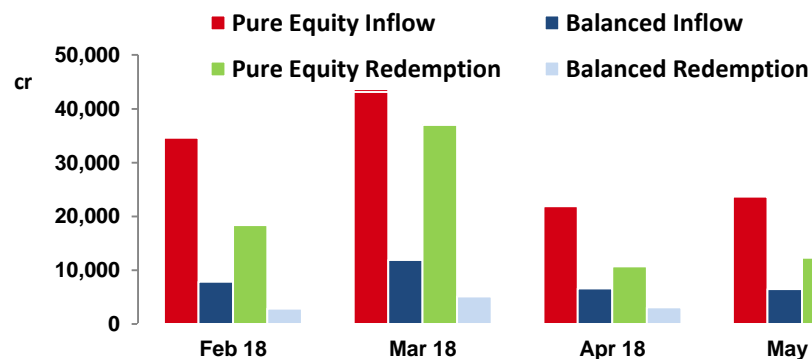


Net Flows to Equity Mutual Funds stabilizing at healthy ~13k cr level despite volatility, but at lower levels compared to peak of Dec-Jan



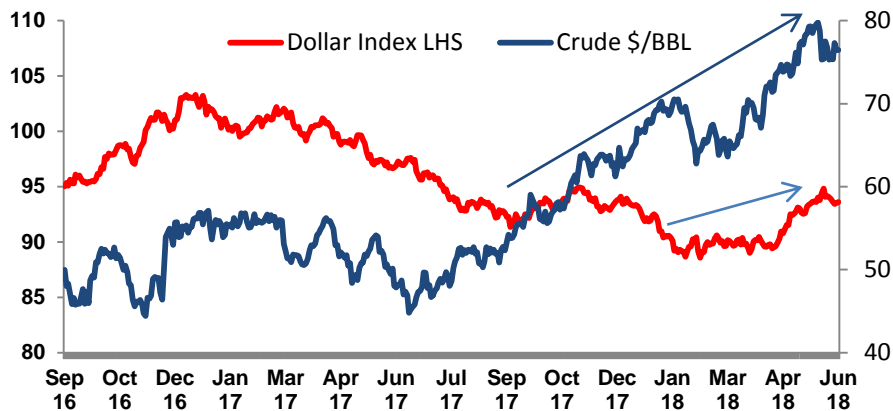
Note: April excludes Arbitrage Funds

MF Redemptions have not increased despite market volatility, Inflows sustained due to ~7k cr SIP book

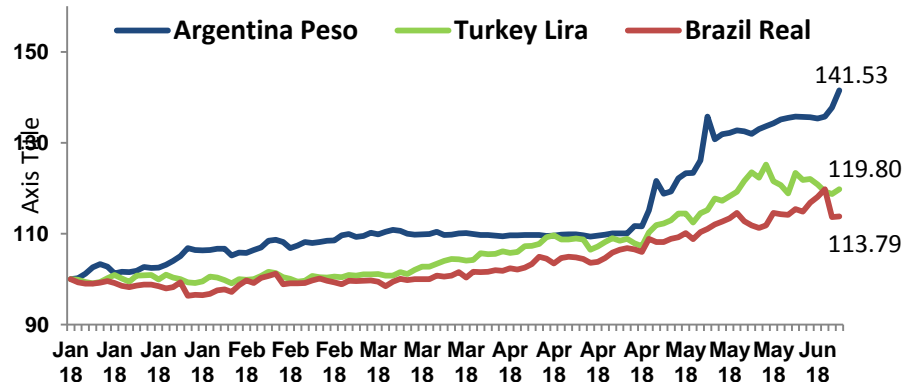


Emerging Markets under pressure as Monetary tightening is in motion, India protected till now due to strong Domestic flows

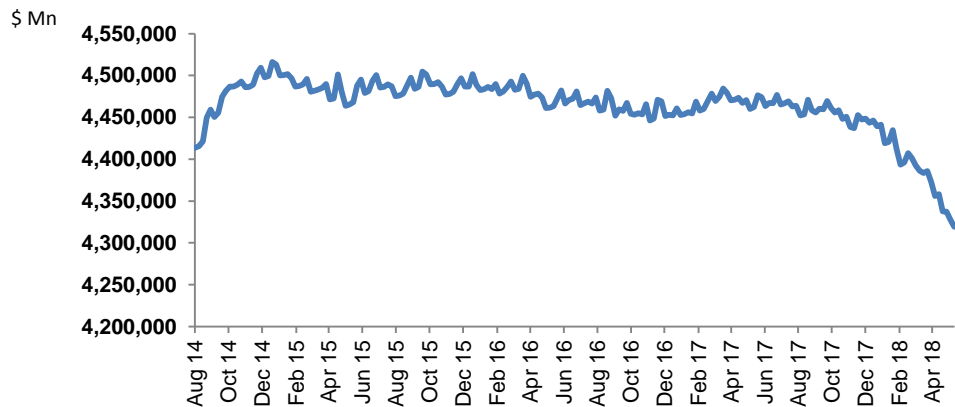
Rising Crude prices and Dollar strength is impacting India outlook for FIIs



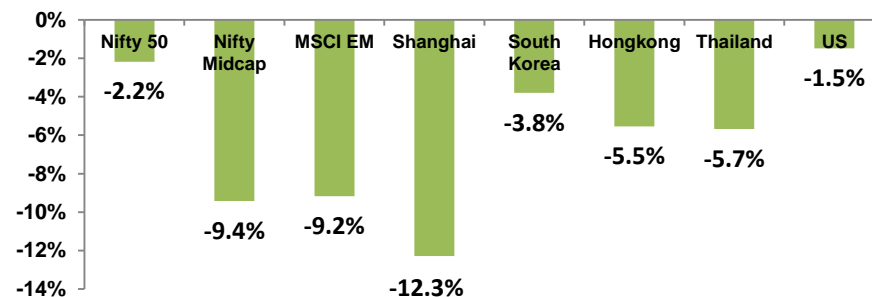
Emerging Market currencies especially for nations with weak macro under turmoil



QE Unwind program is gaining pace, Fed Balance sheet leaner by \$150 bn in last 1 Year

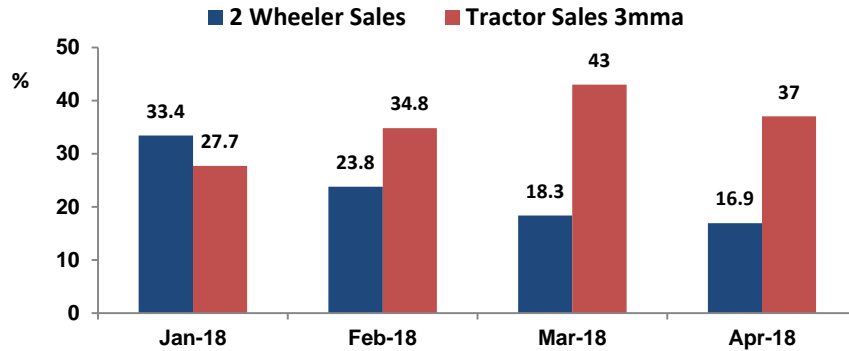


Since 31st Jan, Emerging markets have corrected by 9%, Nifty 50 has been an outlier

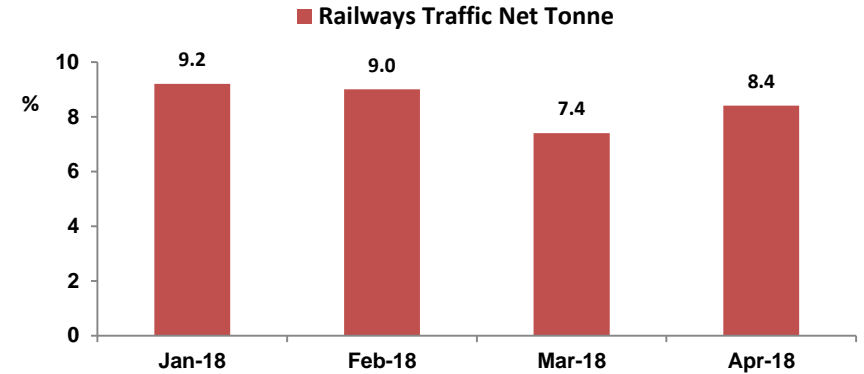


Domestic Economy showing greenshoots in both Consumption and Capital Goods, Credit also picking up

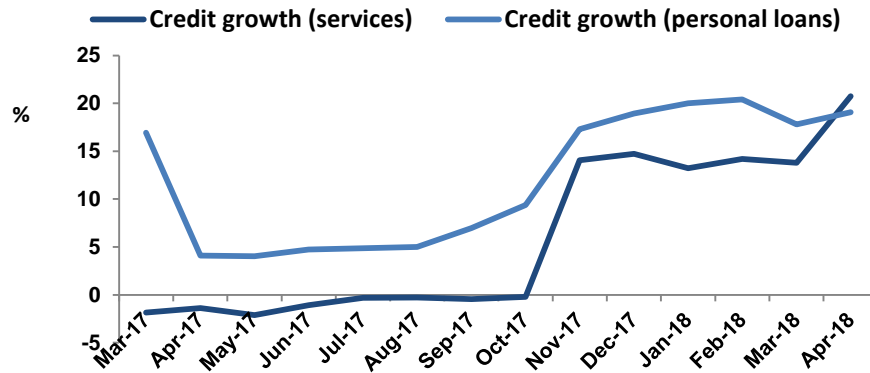
Strong 2 Wheeler and Tractor Sales indicate rural economy recovering



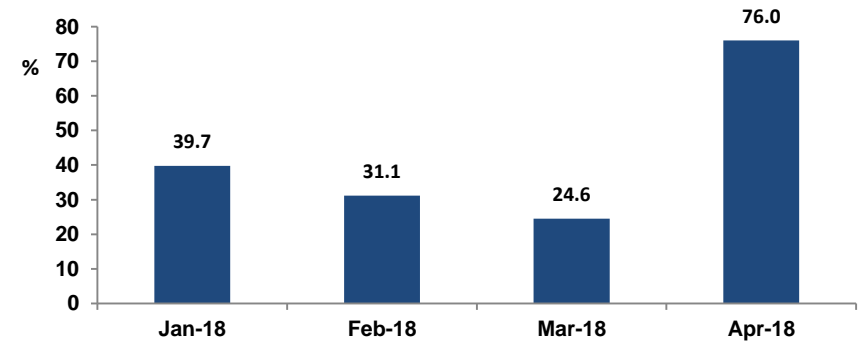
Strong recovery and growth figures on Investment side as well since this year



Credit Growth has started to pick up, higher bond yields also helping



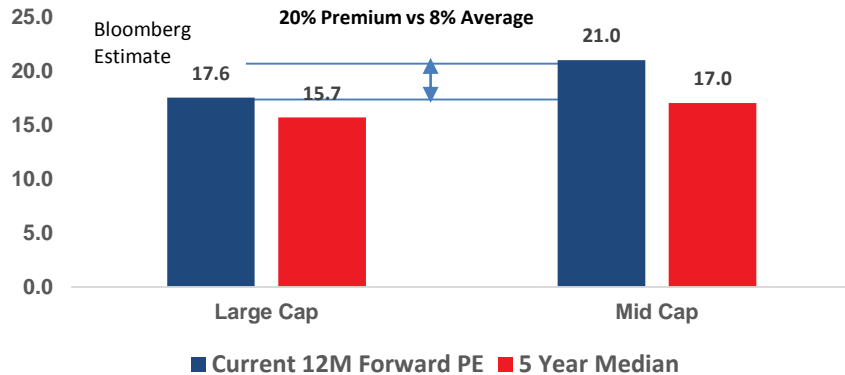
Commercial Vehicle Sales (an early indicator of industrial growth) showing impressive growth



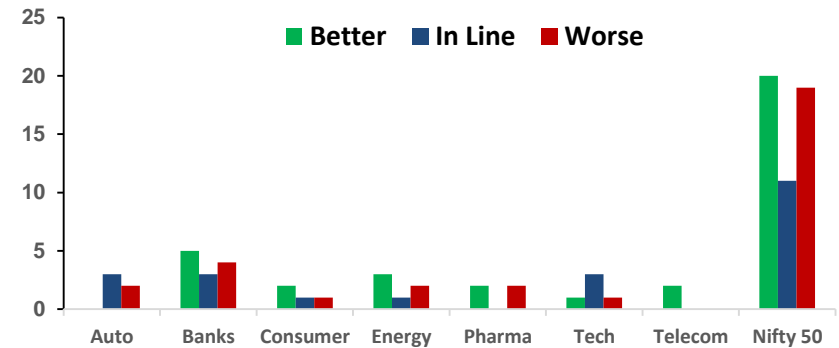
Source: KIE, Nomura
YoY% growth

Earnings and Valuation

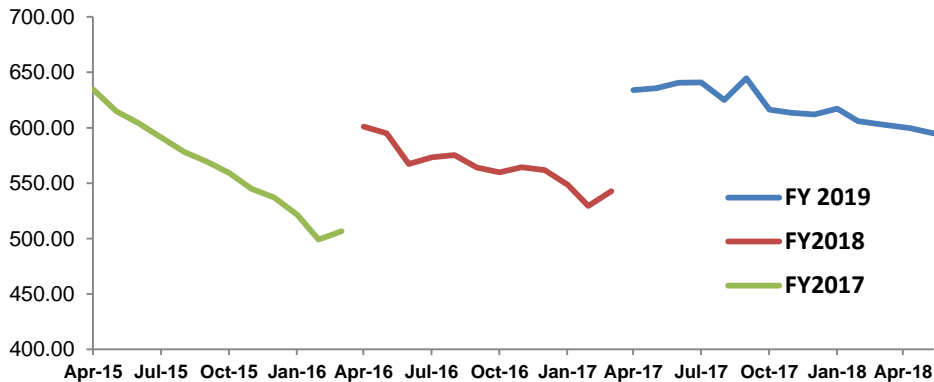
Post recent correction, Mid Caps still at a 20% premium over large caps



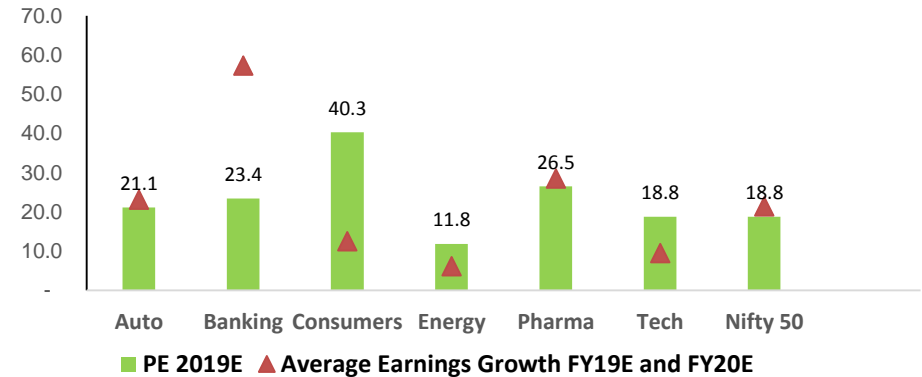
4QFY18 Nifty 50 results have been in line with expectation, Coal India and Axis were significantly below expectation due to write offs



Post stable outlook in the beginning, FY19 earnings expectation has also started to taper off



KIE expects 23% and 20% Nifty 50 Earnings growth for FY19 and FY20



Source: Bloomberg, KIE * Based on KIE Estimates on free float basis.
Better if Actual vs Expected >5%, Worse if Actual vs Expected <-5%
As of 11th June 2018

Key Triggers

Positive Triggers

- **Global Economic data** : World economy improving
- **Resolution of NPA**: Effective addressal of NCLT lists
- **Weaker Rupee**: To benefit IT and Pharma
- **Monsoon/Rural recovery**: Government focus on rural economy including increase of MSP could benefit rural consumption

Risks

- **FII Outflow from EM**: US tax reforms and rising global rates could trigger capital flight from Emerging Markets like India
- **Earnings**: Consensus expected earnings growth for domestic equities is high at around 22% for FY19, any downgrade would make the valuations more expensive
- **Trade Wars**: Further tariffs imposed by US/China and strict enforcement of Iran sanctions
- **Monetary Policy**: Faster than expected monetary tightening in Europe and US
- **Weaker Macro**: Higher crude prices and low GST collection could lead to de-rating of Equity valuations
- **Higher Provisioning** : Due to recent RBI rule and continued slippages, Banks could show high provisioning this FY also thus impacting Nifty EPS
- **Elections**: A combined opposition can be threat to BJP in next elections

India Equities: Valuations & Strategy – Maintain Neutral Stance

Nifty was flat for the month of May, however the midcap index lost ~6%. The month was driven by depreciation seen in INR which is down ~5% for 2018. Crude maintained its upward trajectory with a gain of ~3%. On the positives, Q4FY18 GDP came in at 7.7% above expectations. FII flows remained negative for the second month in a row, however this was compensated by positive DII flows.

At current levels of approx. 10,818 (15th June 2018), Nifty is trading at a 1 year forward PE of 18.8X. In the current scenario, **we continue to maintain a Neutral stance.**

Mutual Funds: As domestic liquidity continues to drive markets, we advise new investments to be staggered in Mutual Funds via SIPs/STPs.

Recommended allocation within equity mutual funds is as under:

- 50% Large Cap allocation (Prefer Large Caps due to relatively Favorable Valuations)
- 50% Multi Cap allocation (such funds currently have a bias toward large cap)
- For investors who want equity exposure but have low appetite for volatility, they can take equity exposure through Balanced Funds. Balanced funds have around 25% to 30% of their portfolio into Debt instruments which provides cushion to the portfolio return during market volatility.

Recommended Large Cap, Multi Cap & Balanced Fund Performances

Scheme Name	Corpus (In crs.)	1 Year	3 Years	5 Years	Investor Suitability
Large Cap Funds					
ICICI Prudential Bluechip Fund (erstwhile ICICI Prudential Focused Bluechip Equity Fund)	17427	12.35	16.64	12.76	All Risk Profiles except Secure
Large & Mid Cap Funds					
Aditya Birla Sun Life Equity Advantage Fund (erstwhile Aditya Birla Sun Life Advantage Fund)	6,061	5.12	16.78	13.99	All Risk Profiles except Secure
Multi Cap Funds (Multi Cap/ Value/ Focused/ Dividend Yield/ Contra)					
Axis Focused 25 Fund	4,217	20.10	24.09	17.12	All Risk Profiles except Secure
Franklin India Equity Fund (erstwhile Franklin India Prima Plus Fund)	11,569	9.12	13.10	11.13	All Risk Profiles except Secure
Kotak Standard Multicap Fund (erstwhile Kotak Select Focus Fund)	19,614	8.93	18.07	14.97	All Risk Profiles except Secure
L&T India Value Fund	7,892	5.54	19.05	16.45	All Risk Profiles except Secure
Mirae Asset India Equity Fund (erstwhile Mirae Asset India Opportunities Fund)	7,733	11.42	18.64	15.13	All Risk Profiles except Secure
Motilal Oswal Multicap 35 Fund	13,181	10.17	22.12	16.42	All Risk Profiles except Secure
Mid & Small Cap Funds (Mid Cap/Small Cap)					
Aditya Birla Sun Life Small Cap Fund (erstwhile Aditya Birla Sun Life Small & Midcap Fund)	2,274	7.85	21.75	21.08	All Risk Profiles except Secure
HDFC Small Cap Fund	4,043	23.50	29.46	23.16	All Risk Profiles except Secure
Kotak Emerging Equity Scheme	3,252	8.36	18.43	16.77	All Risk Profiles except Secure
L&T Midcap Fund	2,805	8.77	25.16	19.58	All Risk Profiles except Secure
Aggressive Hybrid Funds					
Aditya Birla Sun Life Equity Hybrid '95 (erstwhile Aditya Birla Sun Life Balanced 95)	14,637	6.04	12.63	11.78	All Risk Profiles except Secure
HDFC Hybrid Equity Fund (erstwhile HDFC Balanced Fund)	294	-0.26	11.30	7.29	All Risk Profiles except Secure
L&T Hybrid Equity Fund (erstwhile L&T India Prudence Fund)	10,656	6.20	14.33	12.13	All Risk Profiles except Secure
SBI Equity Hybrid Fund (erstwhile SBI Magnum Balanced Fund)	24,461	11.74	12.99	11.25	All Risk Profiles except Secure
Balanced Advantage Funds (Balanced Advantage OR Dynamic Asset Allocation)					
ICICI Prudential Balanced Advantage Fund	27,600	8.07	11.41	10.17	All Risk Profiles except Secure
Indices					
Nifty	-	12.94	14.81	10.51	

Source: MFI Explorer

Returns are CAGR as on June 15, 2018 and for Regular Plans with Growth option. Corpus size is as on May 31, 2018.

**Debt Market Update
&
Debt MF Strategy**

Debt Market: Key Variables

Indicators



Policy Action

- Rate hiked by 25bps to 6.25%
- Tone remained cautious with focus on upside inflation risks
- We now expect another 25 bps rate hike in August



10 Year G-Sec Benchmark Yield

- G-Sec segment expected to be volatile
- We expect that this will be a shallow rate hike cycle



Liquidity

- Liquidity now surplus due to increased Government expenditure
- Given the increased allowance in SLR for LCR, Bank's CD issuance should reduce



Inflation

- CPI was at 4.87% in May 2018 in line with expectation
- RBI increased expectation of 2HFY19 to 4.7% from earlier 4.4%
- We expect March 2019 CPI at 4.6% vs RBI's 4.7%



INR

- FII outflows and CAD put pressure on INR, RBI expected to support INR
- Broad range of 66-68 to hold



G-Sec Supply

- RBI has done one OMO of 10,000 cr post which 2 Gsec primary issuances of 22k cr has been completed
- Still weak demand sentiment and low volumes

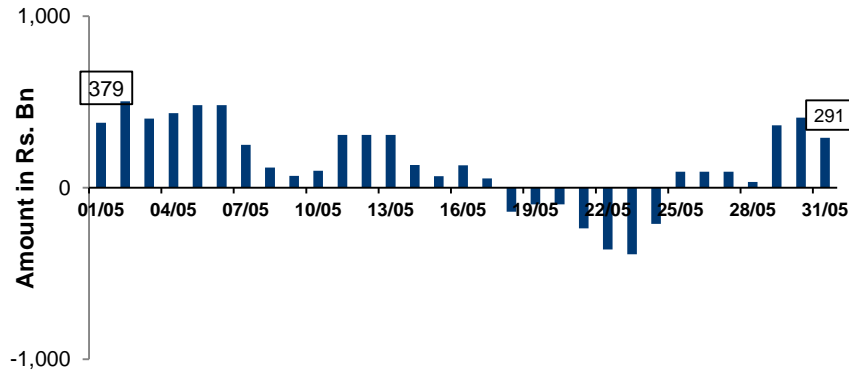


Key Risks

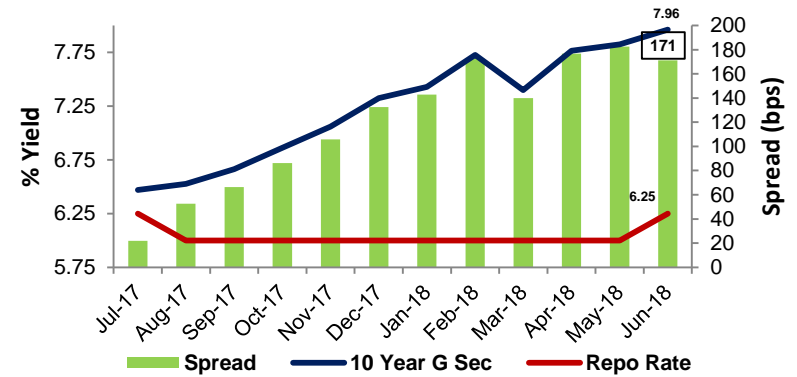
- Global monetary tightening
- Increase in Inflation expectation
- Crude Prices
- Impact of GST revenues and spending on Fiscal Deficit
- Adverse Monsoons

10 Year Benchmark close to 8% level , RBI sees upside risk to inflation

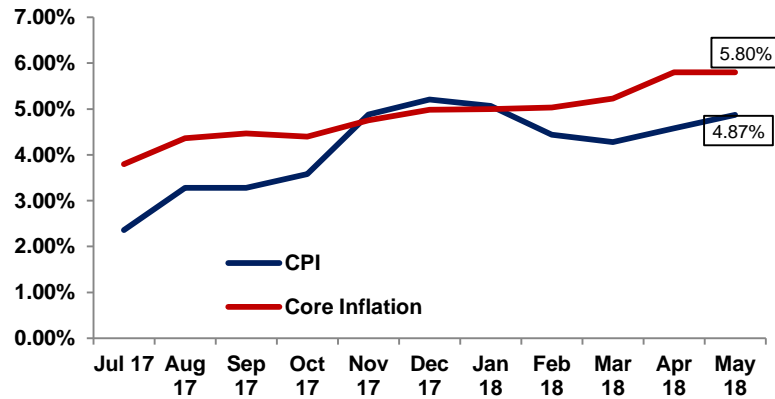
Liquidity maintained at surplus level



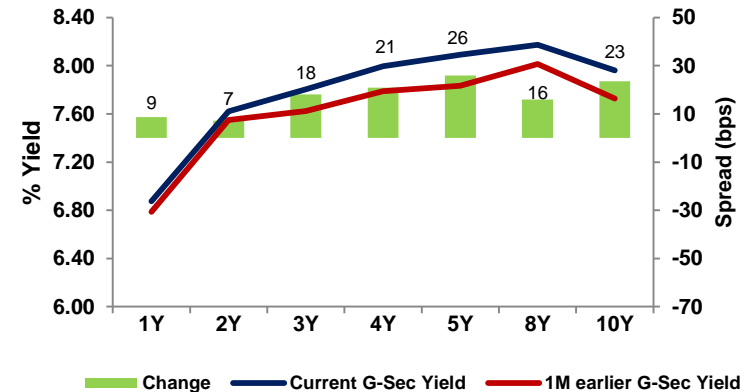
Despite rate hike, 10 Year spread over repo still at high level



Rising household inflation expectation and core inflation are a concern

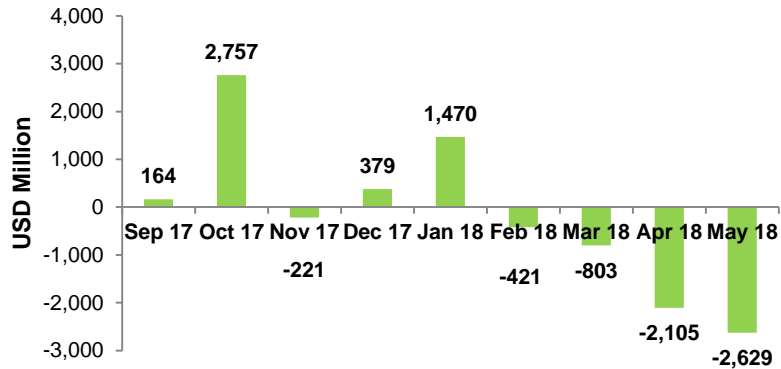


Longer tenure Gsec yields was impacted more due to change in LCR requirement

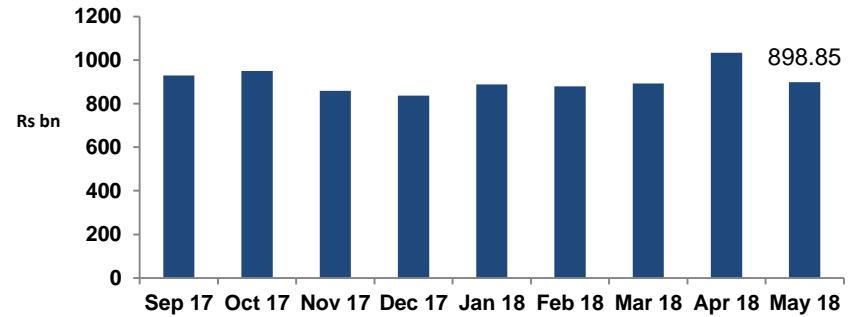


INR under pressure due to higher crude prices and FII outflows

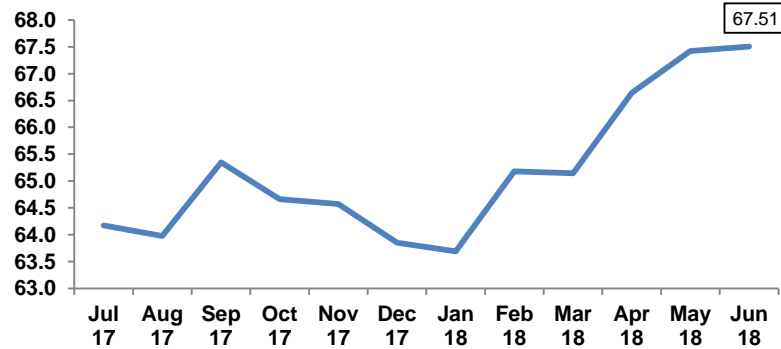
FII have sold ~6 bn USD since 31st Jan 2018



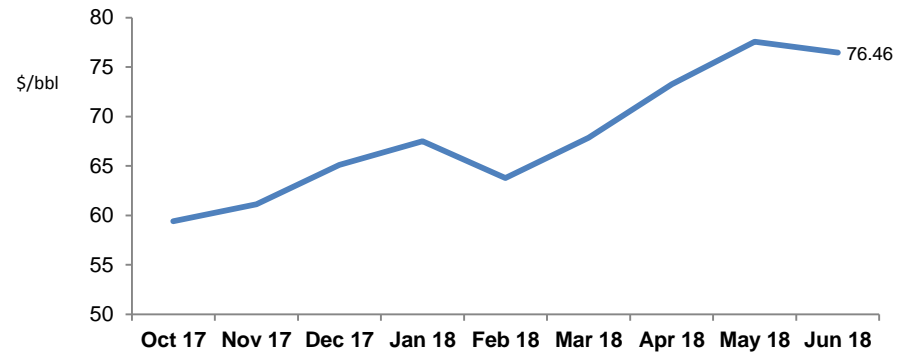
GST collections improve but could be due to seasonality effect



Indian currency has depreciated by ~ 5% in 2018



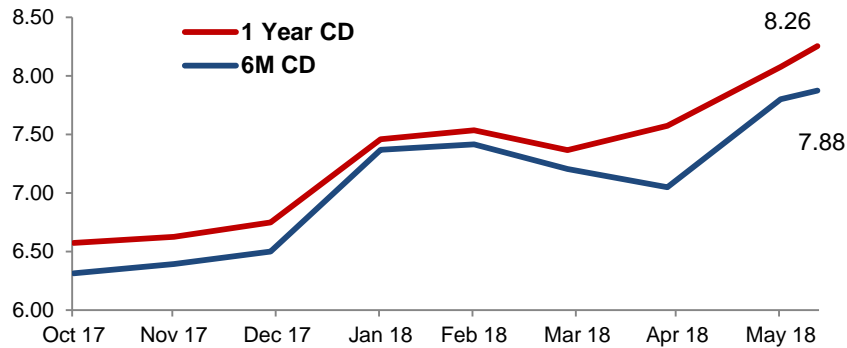
Brent at \$76/bbl is above Fiscal estimates based on \$68/bbl



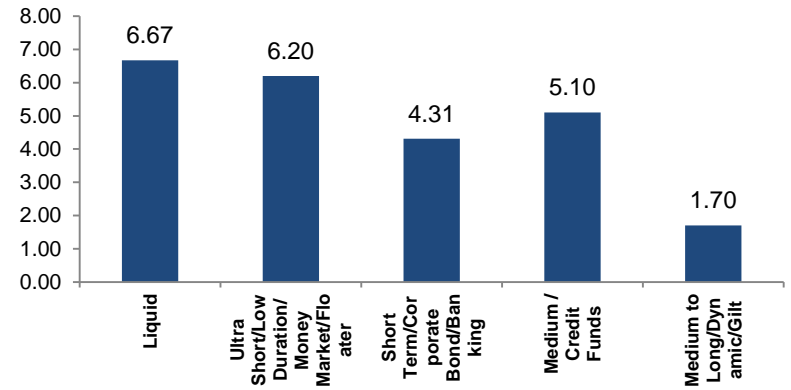
Note: As of 5th Apr 2018, Source Bloomberg, Nomura

Debt Market Trends

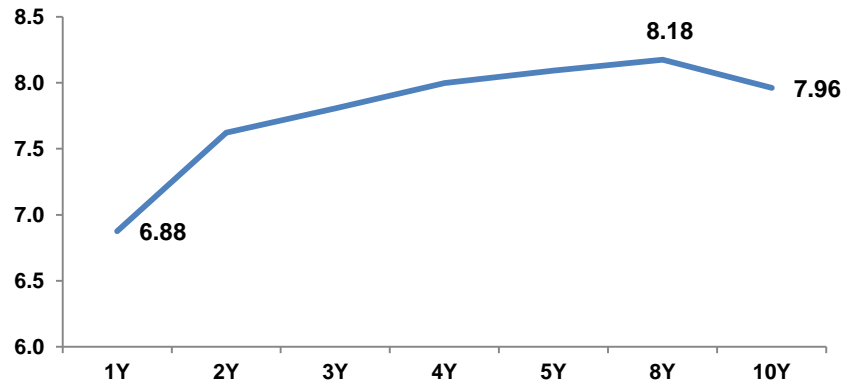
1 Year rate has increased to 8.26%



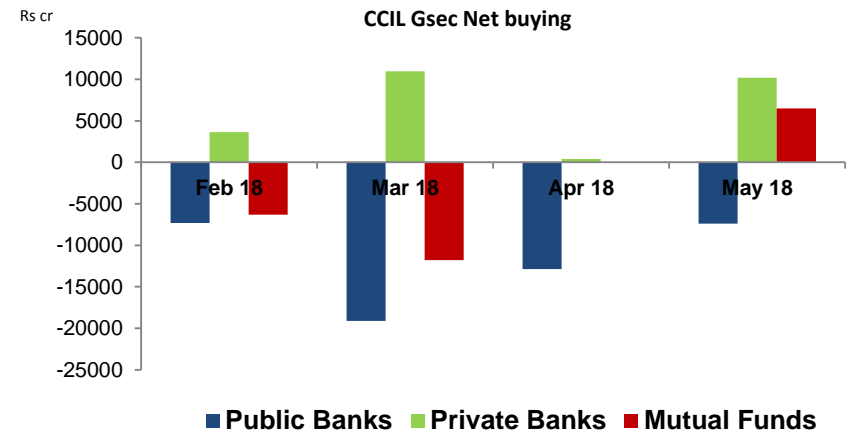
In Last 1 Year, Liquid Funds have outperformed other Debt categories due to marked to market impact



Gsec Yield curve is steep till 4 Year and then almost flattish, hence it better to stay at the short end



PSU banks still net sellers, good buying from Mutual Funds supported by inflows



Note: As of 11th June 2018, Source Bloomberg, MFI

India Fixed Income: Strategy

Substantial part of the portfolio should be deployed through a mix of high rated and credit accrual strategies. Exit from duration funds only for investors who have completed 3 years and can deploy with another 3 years view.

Investment Focus:

Passive Accrual-Oriented Debt funds

- High quality portfolios (~100% AAA / Sovereign)
- Portfolio is run on a passive accrual basis i.e buying a bond and holding it till maturity thereby earning from the accruing of interest
- Higher predictability of return, lower volatility & lower interest rate risk

High Yield Credit-Oriented Funds

- Low volatility on account of maturity of portfolio between 3 – 5 years, attractive and stable accrual yields
- Experienced teams to carefully evaluate and tightly monitor high yielding debt instruments

Short Term Bond Funds

- Actively managed to run a low avg. maturity of 2-3 years, attractive risk-reward
- Lower volatility and interest rate risk than Dynamic Bond Funds, better suited from a risk-adjusted basis in volatile markets

For investments up to 3 months, prefer Ultra Short Term Funds

For investments for atleast 6 months, prefer a mix of Ultra Short Term Funds and Arbitrage Funds.

Recommended Short Term Bond, High Yield & Debt Others Performances

Scheme Name	Corpus (In crs.)	1 Year	3 Years	5 Years	Investor Suitability
Short Term 1-3 yrs (Corporate Bond/ Banking & PSU/Short Duration)					
Aditya Birla Sun Life Corporate Bond Fund (erstwhile Aditya Birla Sun Life Short Term Fund)	16,602	4.86	7.88	8.42	All Risk Profiles except Secure
Axis Banking & PSU Debt Fund	634	5.77	7.37	8.03	All Risk Profiles
Edelweiss Corporate Bond Fund	294	3.67	6.94	-	All Risk Profiles except Secure
IDFC Corporate Bond Fund	11,335	4.38	-	-	All Risk Profiles
HDFC Banking and PSU Debt Fund	3,327	3.72	7.57	-	All Risk Profiles except Secure
ICICI Prudential Banking & PSU Debt Fund	5,891	3.48	8.30	8.18	All Risk Profiles except Secure
Kotak Banking and PSU Debt Fund	1,114	4.28	7.42	8.23	All Risk Profiles except Secure
Sundaram Corporate Bond Fund (erstwhile Sundaram Flexible Fund - Flexible Income)	388	1.59	7.27	7.26	All Risk Profiles
Medium & Credit Risk Funds (Medium Duration/Credit Risk)					
Aditya Birla Sun Life Credit Risk Fund (erstwhile Aditya Birla Sun Life Corporate Bond Fund)	7,016	5.41	8.44	8.79	All Risk Profiles except Secure
BOI AXA Credit Risk Fund	1,533	7.39	9.70	-	All Risk Profiles except Secure & Conservative
ICICI Prudential Credit Risk Fund (erstwhile ICICI Prudential Regular Savings Fund)	10,677	5.47	7.90	8.32	All Risk Profiles except Secure
Kotak Credit Risk Fund (erstwhile Kotak Income Opportunities Fund)	5,223	4.88	8.10	8.37	All Risk Profiles except Secure
L&T Credit Risk Fund (erstwhile L&T Income Opportunities Fund)	3,770	4.85	8.03	8.47	All Risk Profiles except Secure
UTI Credit Risk Fund (erstwhile UTI Income Opportunities Fund)	4,939	4.86	7.97	8.40	All Risk Profiles except Secure
Dynamic Debt (Medium to Long Duration/ Dynamic Bond/Gilt)					
Aditya Birla Sun Life Dynamic Bond Fund	6,867	-1.13	6.71	7.72	All Risk Profiles except Secure
HDFC Income Fund	1,128	-2.06	6.26	6.03	All Risk Profiles except Secure
ICICI Prudential All Seasons Bond Fund (erstwhile ICICI Prudential Long Term Plan)	2,242	1.79	9.33	10.68	All Risk Profiles except Secure
ICICI Prudential Bond Fund (erstwhile ICICI Prudential Income Opportunities Fund)	3,461	1.47	7.08	7.24	All Risk Profiles
ICICI Prudential Gilt Fund (erstwhile ICICI Prudential Long Term Gilt Fund)	1,436	-0.53	8.70	7.11	All Risk Profiles except Secure
LIC MF Bond Fund	318	-0.39	5.66	6.12	All Risk Profiles
SBI Magnum Gilt Fund (erstwhile SBI Magnum Gilt Long Term Plan)	2,165	-1.39	8.24	8.52	All Risk Profiles except Secure
SBI Magnum Income Fund	1,761	1.54	7.99	6.68	All Risk Profiles except Secure
UTI Dynamic Bond Fund	1,363	1.10	8.44	8.79	All Risk Profiles except Secure

Source: MFI Explorer

Scheme Returns are as on June 15, 2018 and for Regular Plans with Growth option. Crisil indices returns are as on June 14, 2018. Returns are CAGR. Corpus size is as on May 31, 2018.

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