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WEALTHWISE®

Wiseinvest®
AMFI-registered Mutual Fund Distributor

Inside

Wealthwise

"Wealthwise" is a monthly publication brought to you by Wiseinvest, an AMFI-registered Mutual Fund Distributor. Our CEO, Hemant Rustagi, is a well known personal finance expert. He brings with him an experience of more than 30 years in this field. He regularly writes articles for major national dailies and business magazines as well as appears as a personal finance expert on many investments related TV shows. Providing quality service is our top priority. In keeping with that, we constantly take steps to provide up-to-date information to our clients. In the last seventeen years, thousands of our clients have made mutual funds the mainstay of their portfolios. You can benefit too from our service support for your existing as well as new investments. All you need to do is to just call up any of the offices or email your requirements at **information@wiseinvest.co.in.**

Dear Investor,

At the outset, I would to like to wish you and your loved ones a very Happy and Prosperous 2021, on behalf of Team Wiseinvest. 2020 will be remembered as a year that tested investors' nerves with the stock market swinging from extreme pessimism to record highs within nine months. The market corrected around 40% during February-March from its peak in January but after hitting a four-year low on March 23, it gradually recovered the losses and climbed new peaks in December. The recovery from the March crash stood at 84%.

The benchmark indices Sensex and Nifty gained 15.8 and 15% respectively during the year. Liquidity, fall in the dollar index, improving economic data points, better-than-expected September quarter earnings with first Nifty EPS upgrade after 23 quarters and vaccine progress, all worked in favour of Indian markets. Although DIIs turned net sellers for the year, FIIs net bought more than ₹ 1.6 lakh crore of Indian equities in 2020, including a record monthly inflow of over ₹ 70,000 crore in November after the US elections.

The governments and central bank, across the world, unleashed support for economies like never before. More than $20 trillion has been provided as stimulus and still counting. This helped in keeping the businesses and the markets afloat. Besides, the economies were supported by the WFM (work from home) experiment that allowed hundreds of millions of people across the world to work remotely.

India's current account of the balance of payments remained in surplus for the third consecutive quarter in the July-September period at 2.4% of the GDP as imports shrank more than exports due to Covid-induced economic contraction. The country's current account balance is likely to end in a surplus this fiscal year for the first time since 2003-04.

2021 is likely to be a good year for the economy and the stock markets. India could record a double digit GDP growth and witness much broader market participation led by economic and earning recovery. On health front, we bid farewell to 2020 on a positive note as three Covid-19 vaccines have been approved globally. India is likely to approve at least one vaccine anytime soon and that will expedite the economic recovery. On our part, we all need to continue to act responsibly and maintain physical distance as well as wear masks.

Warm regards,

Hemant Rustagi
Editor

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The Stock Market Performance During December 2020.

Indices	1st December 2020	31st December 2020	Change in (%)
Sensex	44,655.44	47,751.33	6.93
MIDCAP	17,073.08	17,941.43	5.09
SMLCAP	17,013.04	18,098.11	6.38
BSE-100	13,205.51	14,100.47	6.78
BSE-200	5,544.07	5,906.87	6.54
BSE-500	17,188.31	18,300.10	6.47

Equity Market Overview

CY20 was extraordinary – NIFTY declined nearly 40% from a peak of 12,400 to 7,500, and then rallied about 90% to 14,000 on coordinated global fiscal and monetary policy support, better-than-expected economic recovery from lockdowns, strong liquidity flow from foreign investors and optimism on Covid vaccine. The upcoming Union Budget in February, DXY trajectory, pace of economic recovery - both domestic and global, continuing liquidity surge and vaccine rollout are the key near-term catalysts for the equity markets.

The DXY has depreciated 12% since Apr-20, enabling a sharp resurgence in flows into emerging market equities, including India. Since bottoming out in Apr-20, FII inflows have totalled USD30bn and CY20 FII inflow of USD23bn is the highest of any calendar year since 2012. Domestic Mutual Funds, on the other hand, have witnessed sustained outflows in 2H20.

Policy stance across the globe - both fiscal and monetary, have been supportive of growth. Most of the recovery indices and indicators show that economic activity by and large are close to the pre-Covid levels in India. The high frequency economic indicators have improved sharply from the lows of May and June 2021. While part of the improvement was pent up demand, the sustenance of the trend post the festive season in November and December 2020 has been the key. The recent data points are pointing to continued strength. GST collections for November (collected in December) were at an all-time high aided by improving economic activity, festive demand impact, and better compliance.

During CY21, we expect the government to continue their policy focus and reforms initiatives. It is expected that we could see the introduction of legislation to reform the power distribution sector, continue with the Make in India program (through Production Linked Incentive schemes, Land reforms, policy on Port linked industrial clusters etc). Besides, CY21 could see some progress on the Judicial and Election reforms and PSU monetization.

We expect a strong recovery in the economy in FY22 following the likely large contraction in FY21E. We expect normalization in other macro-economic parameters including fiscal deficit and CPI inflation.

The Q2FY20 earnings season in India proved to be better than anticipated given the backdrop of the economic impact of Covid. The quarter saw more upgrades than downgrades and many of the companies saw improvement in balance sheet with lower leverage and better cash flows. Therefore after a stellar 2QFY21, the role of earnings delivery assumes an even greater importance for markets. With the run up in the indices, the Nifty is now trading at over 22XFY22E EPS.

Apart from high valuations, some of the other key risks for the market include a) delay in vaccine distribution, b) virus spread forcing re-lockdowns, c) earnings disappointments and hiccups in economic recovery d) re-emergence of USD strength e) policy stance by the new Biden administration in the US.

With this backdrop let us shift our focus onto the key themes for the new year CY21. With the up-move in the headline indices, bottom up stock picking is the way forward. We believe that FY22 should be a more normalized year for economic growth and when economy turns the corner and growth rate increases, in terms of bottom up stock picking we are focussing on companies most geared towards this earnings recovery.

Over the last year we have clearly seen the evolution of policy in order to boost domestic manufacturing. The policy support started out with the cut in corporate tax rates. Recently the announcement of labor reforms and the extension of the Product Linked Incentive (PLI) to other new sectors including automobiles and auto components, pharmaceutical drugs, white goods etc. suggest a renewed push towards this segment. These reforms also come at a time when companies across the world are seeking to diversify their supply chains away from China to other parts of the world. The allocation towards capital expenditure in the upcoming Union Budget will be closely watched in this respect. If this strategy is executed well, we expect that this could prove to be structural theme for the economy and could also emerge as a key driver for job creation in the economy.

In the pre-Covid days, we saw signs of market share shifts and consolidation start in a few sectors such as telecom, airlines, banks and NBFCs. Market share shifts are likely to continue and the theme of consolidation in sectors and sub sectors remains intact. Clearly the organised sector is benefiting due to shift in market share from the unorganised space and the companies with strong balance sheets and cash flows are faring much better.

Midcaps have outperformed the large caps this year after two years of underperformance. However, despite the outperformance, many of the midcap names are still below the highs touched in 2018 and the midcap index trails the large cap index over a two / five year period. The midcaps are more geared towards economic recovery. As the economy recovers and earnings growth picks up there could still be further room for midcaps to play catch up for some times. However, one has to selective in choosing the right midcap names to play this theme. We believe that one has to be patient and continue to focus on companies with strong corporate governance policies, strong balance sheets and low leverage and lower fixed cost structures.

ESG (Environment, Social and Governance) issues are growing in relevance in India and sustainability is clearly becoming a far more important factor in the investment decision making process. Not just sustainability but the impact of controversies (environmental, governance related, capital allocation policies etc.) is growing in relevance. We expect that as more and more asset managers focus on ESG and engagement with companies increases along with stewardship practices, this could become one of the dominant investment themes over the next few years.

Put simply, performance of all three bottom-lines – Profit, Planet (environment) and People (social) are equally important as against looking at only the Profit bottom-lines few years back. ESG investment principles look even at 'how companies make money' and not just at 'how much money the company makes'.

Wish you all a healthy and prosperous 2021! Happy investing!

Harsha Upadhyaya
President & CIO – Equity
Kotak Mahindra Asset Management Company

Debt Market Outlook

What a year of the rat (as per Chinese calendar) 2020 was! Menacing all the way along.

The year had 3 V's - Virus, Volatility, Vaccine hope, and investors needed to have 3P's – Patience, Perseverance, Positivity loads .

It was a year where cough gave you Khauf, sneeze made you freeze, fever made you quiver.

But Mann mein tha Vishwaas…even this shall pass.

Most asset classes danced, gold yet again went into a trance. Timing (market) proved killing, time in (investors) hardly lost a shilling.

Year 2020 was characterised by rates cuts till the first half which led to capital gains across fixed income yield curve. Surplus liquidity continued to hog centre stage which kept the yield curve well supported. Fixed income funds had a reasonably good innings. The 10 year benchmark bond yield eased ~50 bps and yield easing was seen across the yield curve. Every category of fixed income delivered positive returns, with longer duration funds clearly standing out in terms of relative performance. No marks for guessing – overnight and liquid funds delivered the least return as this category had relatively lesser duration. RBI continued to do special OMOs and Operation Twist, which ensured some support to the longer end of the yield curve. While FPIs did a Jhoom-BarabarJ-hoom act and were net buyers in Indian equities (INR ~1.71 tn), they were net sellers in fixed income to the tune of INR ~1.02 tn. CPI (retail inflation) – the real life villain of our portfolio returns continued to remain sticky which meant the readings remained above the RBI tolerance levels (4% +- 2% range).

What lies ahead for fixed income investors in 2021

For starters, we do not expect RBI to make any abrupt changes to the current policy regime. The banking system currently is flush with liquidity – a trend which is being witnessed globally as well. Liquidity may not exit the banking system in a tearing hurry, hence we may see range bound yield movements and a much need anchor for yields may well be available this year as well. The current yield curve is quite steep and a case for flattener is very much on the cards.

For this year, most likely the theme in fixed income would be to 'chase the carry' while capital gains may likely play second fiddle to the bond markets. There are incipient signs of global economic recovery in sight and therefore need to ease rates by central banks may be limited. Key cues to watch out for would be the inflation numbers. RBIs intent to look through the current inflation is good news as we are likely to see decelerating CPI in the coming few months. While we are currently seeing a mellowing bias, it is important to see this sustain. This bodes well for fixed income investors who have been apprehensive of possible rate hikes in the near future. Policy rates are likely to be in accommodative for good part of 2021 and any decisive departure is only likely once we see sustained uptick in inflation – a low chance event for now. India has touched an all time high foreign exchange reserves of ~$580bn which is great news for INR. A supported rupee may encourage FPIs to plough in money in Indian bonds. However, one needs to be mindful that the excess money created by world central bankers has to find a withdrawal plan. Though it may not be warranted anytime soon, that would be a key watch out factor going forward too. Volatility may exist, hence key to be disciplined in ones investment approach – keeping in mind the intended investment horizon

To summarise

In the year 2021, hopes are of a vaccine to makes us beam
World which has seen liquidity bloat, may not continue to have the same moat
Markets may defy gravity many a time, but Discipline is a virtue that will shine
So let's gear up for an optimistic Bharat.
Swag se karenge 2021 ka swagat

Lakshmi Iyer
Chief Investment Officer (Debt) & Head Products
Kotak Mahindra Asset Management Company

Mutual Fund investments are subject to market risks, read all scheme related documents carefully.

Performance Of Select Funds

Data as on December 24, 2020

EQUITY FUNDS

Large Cap, Large & Midcap, Multi Cap

Fund	Launch	6 Mth*	1 Year*	2 Year**	3 Year**	5 Year**	7 Year**	10 Year**	15 Year**
ABSL Frontline Equity Fund	Aug-02	32.56	12.09	10.90	5.57	10.67	13.45	10.83	14.70
ABSL Equity Fund	Aug-98	35.32	14.24	12.30	6.08	13.05	16.85	11.92	13.77
Axis Bluechip Fund	Jan-10	31.61	17.11	18.99	14.17	14.94	15.69	12.50	—
Axis Focused 25 Fund	Jun-12	34.97	18.68	17.66	11.57	16.09	17.07	—	—
Axis Growth Opportunities Fund	Oct-18	29.42	22.87	20.39	—	—	—	—	—
Canara Robeco Equity Diversified Fund	Sep-03	31.27	20.53	17.32	10.89	13.09	14.58	11.67	14.31
Canara Robeco Emerging Equities	Mar-05	35.38	23.44	16.42	6.65	13.56	22.99	17.61	16.05
HDFC Equity Fund	Jan-95	30.59	5.63	6.95	2.62	9.71	12.86	9.15	13.50
HDFC Top 100 Fund	Oct-96	28.21	4.64	7.09	4.06	10.10	12.13	8.93	13.44
ICICI Prudential Bluechip Fund	May-08	30.29	11.24	11.63	6.66	11.82	13.64	11.31	—
IDFC Core Equity Fund - Regular Plan	Aug-05	33.90	12.40	8.30	3.25	10.48	12.05	8.74	10.21
Kotak Bluechip Fund - Regular Plan	Dec-98	32.85	14.19	15.35	8.56	11.33	14.13	10.32	12.83
Kotak Equity Opportunities Fund	Sep-04	29.38	15.82	15.05	7.22	12.88	15.97	11.59	14.23
Kotak Standard Multicap Fund	Sep-09	27.89	10.09	12.09	6.93	12.70	16.64	12.60	—
Mirae Asset Emerging Bluechip Fund	Jul-10	34.56	21.28	18.32	9.58	17.07	24.44	20.19	—
Mirae Asset Focused Fund - Regular	May-19	35.78	19.53	—	—	—	—	—	—
Mirae Asset Large Cap Fund - Regular	Apr-08	31.66	12.21	13.23	8.09	13.63	17.06	13.56	—
Motilal Oswal Multicap 35 Fund	Apr-14	27.85	8.44	9.01	2.53	11.11	—	—	—
Nippon India Large Cap Fund	Aug-07	31.06	4.05	6.32	3.56	9.57	13.78	10.41	—
Invesco India Contra Fund	Apr-07	30.45	19.82	13.51	7.31	13.83	18.26	13.27	—
SBI Bluechip Fund	Feb-06	33.43	13.81	13.70	6.81	10.92	15.05	11.78	—
SBI Focused Equity Fund	Oct-04	26.09	13.69	15.68	8.41	13.73	17.84	15.41	14.39

Midcap & Smallcap

Axis Midcap Fund	Feb-11	30.71	24.90	18.55	12.87	14.63	19.74	—	—
DSP Midcap Fund - Regular Plan	Nov-06	30.58	23.50	16.48	6.42	13.37	19.31	14.16	—
HDFC Mid-Cap Opportunities Fund	Jun-07	34.70	21.98	10.75	2.51	11.17	17.88	14.96	—
Kotak Emerging Equity Fund Regular	Mar-07	36.55	22.05	15.07	5.33	12.93	20.66	14.54	—
L&T India Value Fund	Jan-10	32.87	12.99	9.35	1.71	9.95	17.86	13.18	—
Motilal Oswal Midcap 30 Fund	Feb-14	32.37	9.03	10.02	1.19	7.45	—	—	—

Sectoral / Thematic Fund & Tax Saving

ICICI Prudential Banking and Financial	Aug-08	36.04	-6.96	3.99	1.68	13.32	16.66	13.06	—
Nippon India Banking Fund	May-03	35.61	-11.91	-0.69	-1.23	9.21	13.33	9.00	15.02
ICICI Prudential Pharma Healthcare	Jul-18	34.81	71.79	34.19	—	—	—	—	—
Nippon India Pharma Fund	Jun-04	32.17	67.44	31.02	21.03	11.09	17.15	16.11	19.80
SBI Healthcare Opportunities Fund	Jul-99	34.01	66.86	29.41	14.46	5.49	14.57	15.76	13.07
Kotak Pioneer Fund - Regular Plan	Oct-19	38.76	31.75	—	—	—	—	—	—
Axis Long Term Equity Fund	Dec-09	34.37	18.27	17.32	11.85	14.02	19.10	16.41	—
IDFC Tax Advantage (ELSS) Fund	Dec-08	36.50	17.27	9.66	2.64	10.88	14.22	11.88	—
Kotak Tax Saver Regular Plan	Nov-05	30.11	14.22	14.18	7.16	12.26	16.00	10.43	11.48
Mirae Asset Tax Saver Fund	Dec-15	36.32	19.83	17.48	10.23	—	—	—	—

ARBITRAGE FUNDS

Funds	Launch	3 Mth*	6 Mth*	1 Year*	2 year**	3 Year**	5 Year**
ICICI Prudential Equity Arbitrage Fund	Dec-06	0.78	1.54	4.21	5.08	5.44	5.75
IDFC Arbitrage Fund - Regular Plan	Dec-06	0.73	1.48	3.71	4.91	5.38	5.61
Kotak Equity Arbitrage Fund Regular	Sep-05	0.77	1.57	4.25	5.16	5.55	5.84

HYBRID

Fund	Launch	6 Mth*	1 Year*	2 Year**	3 Year**	5 Year**	7 Year**	10 Year**	15 Year**
ABSL Equity Hybrid '95 Fund	Feb-95	29.17	10.80	8.19	3.16	8.68	12.77	10.30	13.01
Canara Robeco Equity Hybrid	Feb-93	23.82	18.38	15.66	10.16	11.70	15.26	12.43	14.11
DSP Equity & Bond Fund	May-99	24.11	15.72	15.71	7.79	11.68	14.89	10.79	13.41
DSP Dynamic Asset Allocation	Feb-14	13.42	12.17	10.85	8.11	8.98	—	—	—
ICICI Prudential Bal. Advantage	Dec-06	19.20	10.80	11.29	7.88	10.04	—	—	—
ICICI Prudential Equity & Debt	Nov-99	22.94	8.86	9.43	5.03	10.57	13.72	12.46	12.33
IDFC Dynamic Equity Fund	Oct-14	14.71	12.51	11.10	7.31	8.54	—	—	—
Kotak Bal. Advantage Fund	Aug-18	17.41	12.87	12.90	—	—	—	—	—
Kotak Equity Hybrid Fund	Nov-99	29.17	14.48	14.71	6.97	10.88	11.84	9.70	11.22
SBI Equity Hybrid Fund	Dec-95	22.67	11.86	13.31	8.30	11.04	14.66	11.87	12.93
IDFC Equity Savings Fund	Jun-08	9.63	9.37	7.49	5.78	5.88	—	—	—
Kotak Equity Savings Fund	Oct-14	11.92	9.77	9.18	7.28	8.49	—	—	—

DEBT

Debt Oriented & Ultra Short Term Debt Fund

Funds	Launch	1 Mth*	3 Mth*	6 Mth*	1 Year*	2 Year**	3 Year**	5 Year**
ABSL Short Term Fund	May-03	0.38	2.38	6.15	10.96	9.78	8.61	8.55
Invesco India Short Term Fund	Mar-07	0.22	2.03	3.39	9.39	9.39	7.98	7.70
Axis Corporate Debt Fund - Regular	Jul-17	0.29	2.40	5.05	11.47	8.76	8.42	—
HDFC Corporate Bond Fund	Jun-10	0.49	2.72	4.67	11.66	11.04	9.42	9.12
Kotak Corporate Bond Fund	Sep-07	0.40	2.31	4.25	9.61	9.66	8.88	8.61
Kotak Banking and PSU Debt Fund	Dec-98	0.41	2.48	4.35	10.44	10.66	9.26	8.81
SBI Banking and PSU Fund	Oct-09	0.32	2.59	3.93	10.44	10.03	9.11	8.42
ICICI Prudential Savings Fund	Sep-02	0.65	2.09	4.03	8.60	8.70	8.18	8.16
Kotak Savings Fund Regular Plan	Aug-04	0.22	1.03	2.15	5.86	6.89	7.02	7.20
L&T Ultra Short Term Fund	Apr-03	0.21	0.91	1.80	5.56	6.60	6.82	7.14

*Absolute ** Annualised. Past performance may or may not be sustained in future.

Dividends declared by equity and equity-oriented funds during the month of December 2020

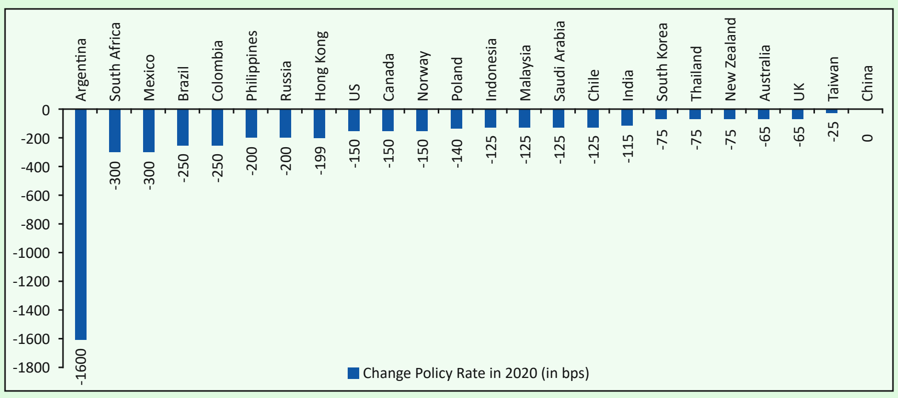
Scheme name	Date	Dividend declared in ₹ Per unit
ICICI Prudential Equity & Debt Fund - Dividend	01/12/2020	0.35
ICICI Prudential Long Term Equity Fund (Tax Saving) - Dividend	02/12/2020	0.70
Tata Hybrid Equity Fund - Dividend	03/12/2020	0.25
Sundaram Equity Hybrid Fund - Dividend	03/12/2020	0.13
BOI AXA Multi Cap Fund - Dividend	07/12/2020	0.45
Tata Equity PE Fund - Dividend Option A	15/12/2020	0.85
Tata Equity PE Fund - Dividend Option B	15/12/2020	1.60
PGIM India Hybrid Equity Fund - Dividend	17/12/2020	0.12
Sundaram Diversified Equity - Dividend	18/12/2020	0.25
ICICI Prudential Multicap Fund - Dividend	21/12/2020	2.25
ICICI Prudential Infrastructure Fund - Dividend	22/12/2020	0.65
L&T Large and Midcap Fund - Dividend	23/12/2020	0.15
L&T Hybrid Equity Fund - Dividend	23/12/2020	0.10
Kotak Bluechip Fund - Dividend	24/12/2020	1.52
Kotak Equity Hybrid - Dividend	24/12/2020	0.09
Aditya Birla Sun Life Midcap Fund - Dividend	24/12/2020	1.74
L&T Tax Advantage Fund - Dividend	24/12/2020	0.90
L&T India Large Cap Fund - Dividend	24/12/2020	1.10
HDFC Hybrid Equity Fund - Dividend	28/12/2020	0.25
DSP Equity & Bond Fund - Dividend	28/12/2020	0.15
Baroda Hybrid Equity Fund - Plan A - Dividend	28/12/2020	0.27
Axis Equity Hybrid Fund - Dividend	29/12/2020	0.08
LIC MF Equity Hybrid Fund - Plan A - Dividend	30/12/2020	0.10
LIC MF Tax Plan - Dividend	30/12/2020	0.25
Aditya Birla Sun Life Dividend Yield Fund - Dividend	31/12/2020	0.19

Please check whether you have received dividend for the fund/s that you may have in your portfolio out of this list. In case, you do not maintain any portfolio statement, Wiseinvest can do that for you free of charge. Once we have the details, we would send your updated statement every month. You can contact our corporate office or our branch to avail of this free service.

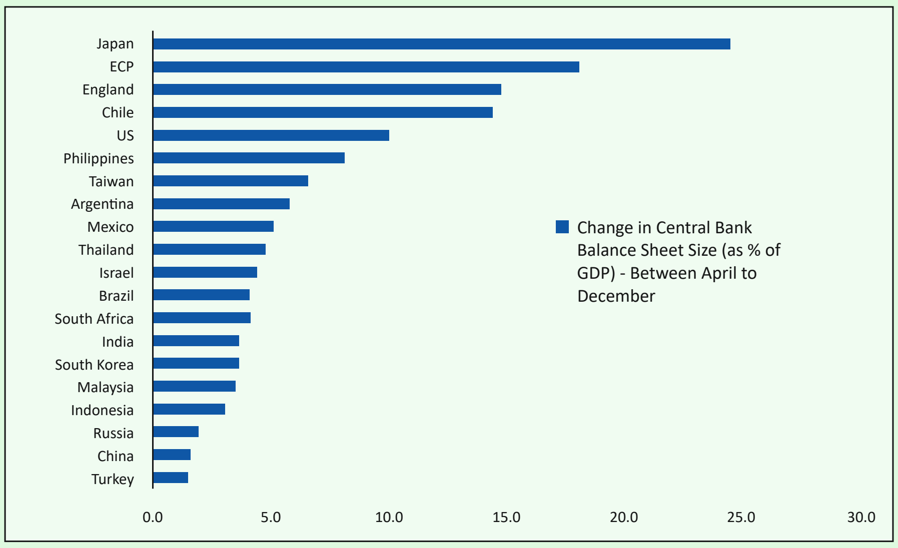
Market Outlook

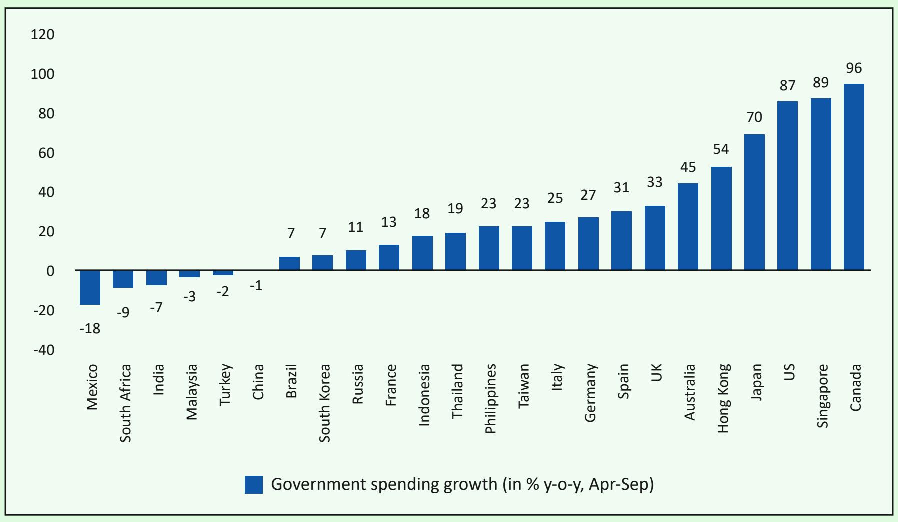
Central bank interventions backstopping financial markets have been the abiding theme in global markets for a while, which got accentuated last year. As financial markets went into a tailspin with the Pandemic induced effects during Feb- March 20, Central Banks turned on the liquidity spigots led by the FED. This was accompanied by large fiscal policy interventions in the developed world. Fiscal policy support till the end of June 20 amounted to about 19.8% of GDP in Advanced economies and about 5.1 % in EM's (Source RBI). This has led to markets bouncing back over the rest of the year. While the economic recovery from the shutdown and rollout of vaccines provide a positive tailwind for markets, the effects of low discounting rates on asset price valuations should not be undermined. The 'low for ever 'discourse on risk free rates remains preponderant as well as the 'Central Bank Put'. Large fiscal stimulus measures have been backstopped with central bank bond purchases, with even direct monetization been resorted to, by EM central banks like Bank Indonesia. Mainstreaming of 'Modern Monetary Theory' with central bank printing presses backstopping fiscal measures is not probably far away.

The other notable actions have been the US Fed changing the monetary policy framework to an average inflation targeting approach and the Euro Zone 750 Bn Euro Recovery Fund, potentially opening the door to an eventual debt mutualization or at least a closer fiscal framework. In the near-term, fiscal policy actions would take centre stage to provide the much-needed support for growth recovery, with all eyes on the incoming new US administration and its policy actions. This sets the stage for capital flows into India and other EM's to be a constant variable to track as we head into CY21.



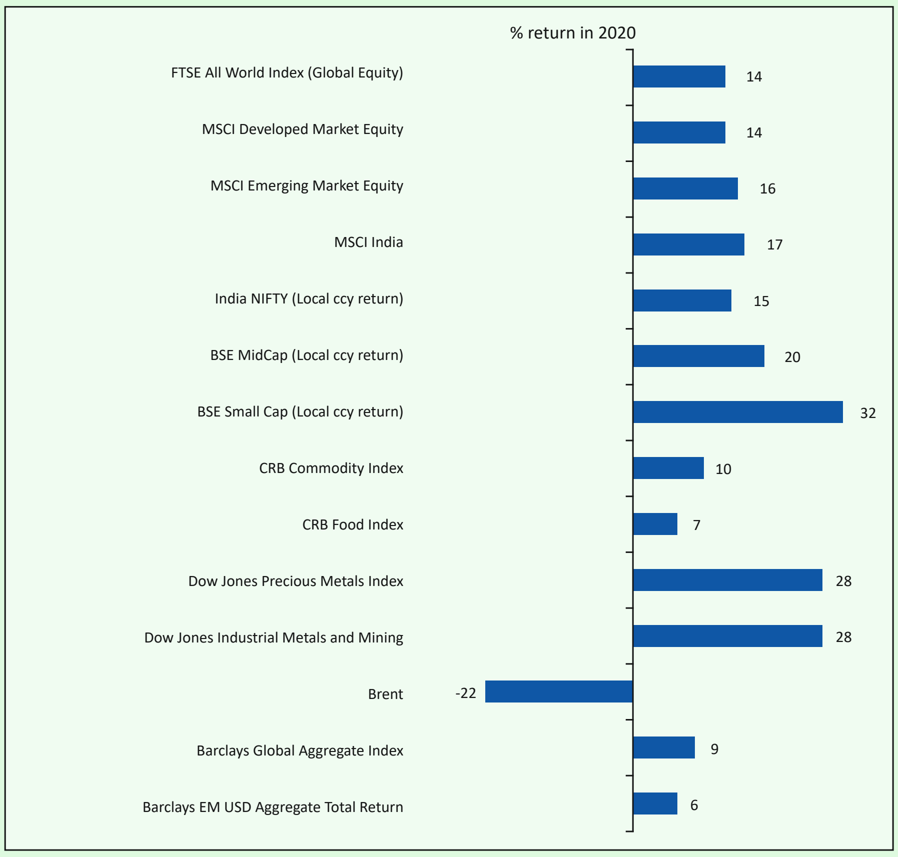
Source- Bloomberg, SBIMF Research





Source- Bloomberg, SBIMF Research

From the financial markets viewpoint, the narrative has quickly changed from deflation to reflation as a result. An important consequence of this massive policy support has been a surge in government debt burdens to levels last seen only during World War II. Liquidation of this debt may necessitate keeping nominal rates 'lower for longer' and real rates negative for several years to come. On the other hand, the policy action has led to an unprecedented surge in broad money growth, again to the extent not seen over the last several decades. While negative real yields themselves have portfolio implications and force investors to diversify into other assets, the belief that rates will stay low even as growth picks up and/or inflation flares up has helped a surge in risk assets across the board.



Source- Bloomberg

Equity

Equities are now expensive on conventional valuation metrics and continue to be driven by the narrative on equity risk premium, which compares the currently low earnings yield to even lower bond yields. We believe while these narratives can help frontload equity returns, continued sustained up move requires a substantial uptick in corporate earnings. Indeed, starting at multi-year lows on the corporate profits to GDP ratio in India currently, there is room for catch-up in earnings. Last few years have seen a clean-up in Indian banks' balance sheets, corporate balance sheets are much healthier, cost structures are leaner and there have been significant reforms around corporate taxes, PLIs, labour laws, agriculture and so on. Additionally, if the current efforts by global policy makers for a successful reflation do fructify, that may just do the trick for India's corporate profit cycle to revive.

As we move into 2021, it is evident that sentiment has swung firmly, from extreme despair in March to optimism now and valuations have rerated alongside. Sticking to investment discipline and asset allocation stay as important as they have always been. A successful global reflation is still not a given. Loose fiscal policy from governments could bring too much inflation too soon while being too restrictive on the other hand may lead to failure to beat deflationary forces. Treading a prudent middle path is critical. Market internals suggest that polarizations still stay high. Market capitalization stays polarized towards large caps versus mid-small caps. Similarly, relative underperformance of value versus quality is at multi-decade highs. Emerging market equities have been massive underperformers versus developed world peers, especially the US, over the past decade. These polarizations should reverse if a successful reflation does materialize. Given the still elevated uncertainties and in the context of high market polarization, being bottom-up should be more rewarding versus staying focussed on aggregates.

Cont. on page 6...

Market...

...Cont. from page 5

Debt

CY 20 has been an eventful year for the domestic debt markets. India has been an outlier as the larger growth shock has been accompanied by CPI inflation above 6% all through the year. This has complicated RBI policy choices along with the liquidity deluge arising out of unsterilized capital flows. The large negative economic shock on account of the pandemic led the RBI to cut policy rates by 115 bps to 4% and institute multiple liquidity infusion windows such as TLTRO's and LTRO's and a CRR reduction. Large capital flows subsequently led to additional liquidity infusion as the RBI has pushed back against currency appreciation. This has pushed the effective operating rate to even below the reverse repo of 3.35%, thereby providing a larger effective policy easing than implied by the Repo rate cuts as well as significant tightening of corporate credit spreads. FPI debt flows have stayed negative through the year.

The RBI also stands apart from its peers in having allowed a large amount of the additional market borrowings to be absorbed by the market. Active interventions through outright OMO's in dated securities have been limited so far with liquidity neutral Twist Operations being conducted. While the government borrowings through dated securities have been ramped up by additional ₹ 5.10 trillion, the same has been largely to cover the revenue shortfalls including the GST compensation. Effectively the burden of stimulus measures has been borne by monetary and liquidity policy as fiscal constraints have handicapped government spending. This is evident from the year to date government expenditure data with total government spending for the year likely to be even lower than the Budget estimate of ₹ 30.4 Trillion.

At the same time, reforms measures on various supply side issues as well as incentivizing manufacturing through PLI schemes have been announced. Government relief measures have been targeted at welfare measures such as food support scheme under PMGKY and credit guarantee schemes. These measures have rightly focused on providing support to the needy while recognizing the resource constraints on the fiscal.

CY 21 starts with the positive news flow surrounding the impending rollout of India's first Covid vaccine approval. This should lead to a more accelerated normalization of economic activity. Government budget for FY22 would be framed in the context of a gradually recovering, though fragile economic context. While tax revenue would be expected to pick up from FY21 actuals, the requirement of larger market borrowings may remain, especially as government spending is likely to be scaled up to support a recovery. This can be mitigated through better realization under the asset sale/ divestment program. Improvement in India's fiscal dynamics would be a multi-year process, given that the fiscal problems have been simmering for a while, largely masked by prospects of higher nominal growth, accounting adjustments as well as the support from a funding source that is predominantly domestic and in local currency. Return to rapid growth and widening the tax base are the only medium-term solutions towards a sustainable and moderate Public Debt/ GDP ratio. In this context, measures would be anticipated to increase the direct tax / GDP ratio through better compliance. Recent measures to plug revenue leakages in the indirect tax regime are rightly designed and would over time lead to better tax realisations both on the indirect and direct taxation fronts.

For the coming year as recovery normalizes, government borrowings may continue to require RBI support in the absence of additional demand sources. From a debt market perspective, RBI actions in CY 20 has rightly prioritized growth with the central bank looking through above target inflation. The prospects for CY21 would be dependent on the evolution of the sequential growth momentum. The monetary and liquidity setting required for preventing/ limiting economic damage during a pandemic induced shock could be different from that required to nurse a recovery, especially in a context where CPI readings remain elevated. While we remain confident that the peak in CPI is behind us, it is important to recognize that the RBI MPC resolution in Dec has provided an expected range for CPI between 4.6%-5.2% for H1 of FY22.

The prospects for the debt markets accordingly should be based on the anticipation that the extra ordinary monetary support would be incrementally unwound as recovery in growth materializes. The near-term prospects on capital flows, the existing overhang of liquidity and the requirement of market intervention (both government securities and Fx) may necessitate activation of sterilization tools to absorb liquidity at the margin. A transition from excessively surplus to moderate surplus liquidity stance is likely with a gradual alignment of money market rates at least to the reverse repo rate and over time closer to the policy rates. Policy repo rate may remain on hold for a reasonable time in the absence of further inflation shocks. The RBI current stance of a passive yield curve control with targeted / tactical OMO/Twist Operations may remain the preferred market intervention strategy for a while. This should anchor long end rates in a range, with a gradual flattening of the curve. While segments of the sovereign rates curve continue to provide relative value, investors in debt products would need to potentially moderate return expectations given the existing lower absolute yields and the likely normalization in monetary conditions over time.

Wishing all a very Happy New year.

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(Mutual funds' investments are subject to market risks, read all scheme related documents carefully.)

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