

# Market Outlook

July 2022

## Equity Market

### Resilient earnings and flows continue to support markets

July 2022 was the best month in this calendar year, with the Nifty gaining ~8.7% in the month. Midcaps outperformed the Nifty, gaining 12% during the month, while the Smallcap Index was broadly in line with the Nifty. While all sectoral indices closed in the green for the month; metals, realty, banks and capital goods were the outperformers while Pharma, IT and energy underperformed. Globally as well, there was a rally in which most markets surged barring Russia and China.

On the macro front, the Government imposed taxes on the export of petrol, diesel, and ATF and on the domestic production of crude oil on July 1 which was later lowered as international prices declined. GST was also raised on a number of items, and goods such as branded packaged foods were bought under the GST ambit. GST collections for July 2022 stood at Rs1.48tn, up 28% YoY, and was the second highest collection since its rollout.

Globally, a number of central banks raised interest rates in July and the WHO declared monkeypox a global health emergency. The IMF cut India's FY2023 GDP growth forecast to 7.4% from 8.2% earlier. CPI stood at 7.01% in June 2022 from 7.04% in May, and it is the 6th consecutive month that the CPI print is above the RBI's upper margin of 6%. WPI print came in at 15.18% in June 2022.

With the INR hovering around 80/USD, the RBI announced steps, including rules for foreign investors, to invest in government and corporate debt to boost inflows to stem further depreciation of the INR.

After 9 months of continuous selling, FPIs turned buyers and bought equities to the tune of \$780mn while DIIs continued to buy, and added equities worth US\$1.32bn during the month.

### Going forward

Markets have rallied with the belief that the pace of interest rate hike globally (with Fed raising interest rates by 75bps for the second consecutive month) will moderate on the back of subdued/growth or possibility of recession. We can debate if the recession or slowdown will be shallow or broad-based, or if inflation will be sticky or transient in the developed markets.

While the domestic markets have had a breather from the relentless selling, it may be pertinent to note that the risks of inflation and growth moderation still remain. After the rally end July, the markets are just 5.5% down from its peak. The results season so far has seen decent growth and earnings resilience (in double digits) and hence the market upmove is at least backed by a reasonable uptick in earnings as well.

On the positive side, commodities and energy prices have also corrected thereby providing some relief. While we cannot with certainty pronounce that the margin pressures have abated, the movement is certainly in the right direction, at least for the commodity consuming segments, and it also makes a case for earnings growth visibility in H2FY23.

While being constructive on the markets and economy on the long term, we are also mindful of the risks emanating from inflation, rates and geopolitical tension in the shorter term and will be erring on the side of caution as far as valuations are concerned.

## Debt Market

### Recession fears lead to lower yields

Yields came down across the board in the Indian Bond markets for the first time in almost three months on the back of the fall in developed market yields with the recession trade gaining traction after a slew of soft data coming out of US and commodity prices coming off from their highs.

The US Fed hiked rates by 75 bps though the market took the comment of near to “Neutral rates” by the Fed chairman as a dovish signal and the yields rallied. The fall in the developed market yields had a rub-off effect on Indian yields as the benchmark Indian 10-yr sovereign yield came off by 30 bps from its highs in June.

Though the yields have come down by 70 bps to 80 bps from their highs in June 2022 in the US and Europe, Central banks across the world continue to tighten policy rates and RBI too hiked rates on August 5 policy meeting by 50bps. We expect the RBI to take the policy repo rate to 6.00%/6.25% by the end of the year, though we think that the risk can be on the upside, as the Credit/Deposit ratio of the banking system has deteriorated (credit growth @14% and deposit growth@8.4% YOY). There is also the matter of the trade deficit rising, with the July trade deficit coming in at USD 31bn, and given the portfolio outflows, the BOP deficit can be to the tune of USD 50-60bn which may warrant the RBI to hike rates more than expected.

The CPI Inflation print for June (released in July) came in line with expectations @7.01%. Commodity prices continue to correct factoring in a higher probability of recession in the US & Europe on the back of the aggressive monetary stance of the US Fed and ECB. The slowdown in China also contributed to the weakness in the commodity space.

INR ended the month at 79.27 depreciating by 0.38% during the month, though off from its lows of 80 to a dollar.

We expect the yield curve to flatten further as the RBI continues to hike rates.

We continue to be underweight duration as we expect further rate hikes along with liquidity tightening and will look to tactically add duration at yields above 7.50% on the 10yr bond.

## Fixed Income Market

	June 2022	July 2022	Change (in bps)
Overnight rate (NSE MIBOR)	4.95%	5.25%	30
1 yr CD	6.53%	6.60%	7
10 yr GOI Yield	7.45%	7.32%	-13
USD/INR	78.97	79.27	30 paise
IIP (Monthly with 2 month lag)	6.70%	19.60%	1290
CPI (Monthly with 1 month lag)	7.04%	7.01%	-3
5 Yr AAA PSU spread (bps)	10	15	5
5 Yr OIS	6.88%	6.34%	-54
US 10 Yr yield	3.01%	2.65%	-36
CRR	4.50%	4.50%	0
REPO	4.90%	4.90%	0
SDF (Standing Deposit Facility)	4.65%	4.65%	0

Source: RBI Weekly Statistical Supplement & Bloomberg

**Note:** IIP has been revised lower for the previous reading.

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Source: BSE, RBI & Bloomberg

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