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Investment Strategy
9 November 2024

India Market Outlook

Balancing Act

How should investors navigate near-term volatility? | Macro and Key asset class views | Performance update

Important disclosures can be found in the Disclosures Appendix.

Investment strategy and key themes

Our top preferences

(12-month outlook)

Foundation allocation

- Prefer a diversified asset allocation
- *In equities:* Large-cap equities
- *In bonds:* Medium and Long-maturity bonds

Sector overweights

- Industrials
- Financials
- Consumer Staples

12m FX views

- Mildly bearish bias on INR (12-month)
-

Balancing Act

- Indian equities witnessed a pullback after scaling new highs in September, driven by record foreign investor outflows amid weakening risk sentiment on poor Q2 earnings and slowing growth. The Nifty Index is down 8% from its peak, underperforming its peers (MSCI World Index is flat, while MSCI EM is down 4% from its peak). Broader markets have outperformed large-cap equities, with the Nifty Midcap and Nifty Smallcap index down 7.5% and 6.1%, respectively from its peak. The 10-year IGB yield rose to 6.81%, while the INR depreciated 0.5%.
- The risk of a near-term pull-back remains high amid still elevated valuations, negative EPS revisions and uncertainty around Trump's policy priorities and its impact on risk assets. We believe a diversified asset allocation remains a prudent strategy to tide through the uncertainty.
- Within equities, we are overweight large-cap equities given a greater margin of safety in terms of earnings and valuations along with stronger balance sheets to cushion the impact of tighter financial conditions.
- We see the recent surge in domestic bond yields as an opportunity for investors to lock-in still attractive yields given positive supply-demand balance and robust foreign investors inflows from index-tracking funds. We are overweight medium and long-maturity bonds and high-quality corporate bonds given attractive absolute yields. Gold remains a key portfolio hedge.

Key Asset Class Views

Equities	◆
Developed Markets	▲
Emerging Markets	◆
Indian Equities	◆
Large Cap	▲
Mid/Small Cap	▼

Bonds	◆
Short Maturity	◆
Medium/Long Maturity	▲

Gold	◆

Cash	◆

Legend: ▲ Overweight ◆ Neutral ▼ Underweight

Perspectives on key client questions

How should investors navigate near-term volatility?

After scaling new all-time highs in mid-September, domestic equity markets corrected sharply, with the Nifty Index down 8% from its peak as risk sentiment worsened on slowing growth, weak Q2 FY2025 earnings season and stretched valuations. Further, rising geopolitical tensions and rotation into relatively cheaper markets like China drove a record US$11bn outflows by foreign investors from India equity markets in October 2024.

The risk of a near-term pull-back remains high for domestic equities, as expensive valuations (both in absolute and relative to peers) indicates a low margin of safety. Further, corporate profitability is under pressure after four consecutive years of high double-digit growth. Q2 FY2025 earnings season has been weak with over 50% of reported companies missing estimates and earnings delivery the lowest in 17 quarters. Earnings revisions have turned negative over the last few months.

Navigate market volatility with a balanced portfolio

The clean sweep of the Republican party in the US elections gives them a relatively free hand to implement their agenda of tax cuts, deregulation, imposing import tariffs and immigration curbs. However, which policy Trump prioritises could have varied impact on risk assets driving intermittent bouts of volatility. Geopolitical tensions in the middle east and key state election are added risks. We believe a diversified asset allocation - neutral allocation to bonds, equities, gold and cash - remains a prudent strategy for the remainder of 2024.

Add to large-cap equities and medium and long-maturity bonds

Nevertheless, pullbacks give rise to opportunities for investors to average into better value assets. Within equities, investors can look at opportunities in large-cap equities as they provide a greater margin of safety during periods of high volatility. In addition, large-cap equities are trading at relatively fairer valuations compared to mid-cap and small-cap equities. We see an improved risk-reward for bonds and investors can look to add medium and long-maturity bonds as yields are likely to fall further on positive government bond demand-supply balance and central bank easing led by US Fed rate cuts and the RBI commencing rate cuts in Q1 2025.

Fig. 1 India equity markets are trading expensive to its major peers

12 mth Fwd P/E: Premium/Discount to 10yr average

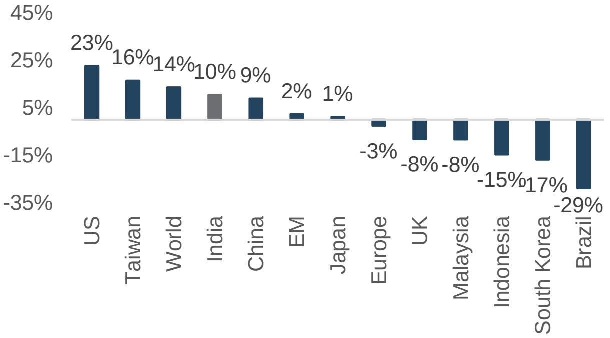
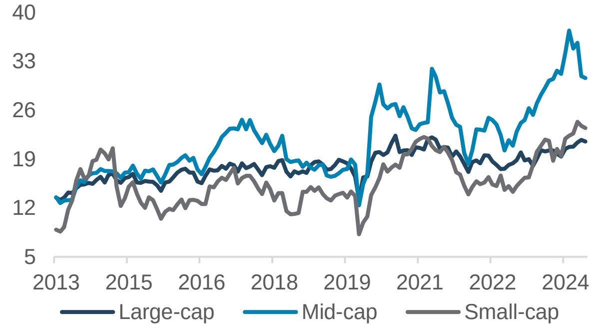


Fig. 2 Large-cap equities trading at discount to mid-cap and small-cap equities

12mth Fwd P/E ratio: Nifty 50, Nifty Midcap 100 and Nifty Smallcap 100



Source: Bloomberg, Standard chartered. Data as of 7 November 2024.

Macro Overview – at a glance

Key themes

We expect India's economic growth to stay above its long-term trend and ahead of its major peers over the next 12 months. Festive led demand revival, broadening government policy support and focus on capex are tailwinds for growth. In our view, CPI inflation could surge from the recent lows on fading base effects but stay within the RBI's inflation target range of 2%-6% on disinflationary pressures from policy tightening, lower food article prices given better monsoon and likely government policy interventions to manage supply side concerns.

In our assessment, fiscal policy remains the key driver for growth in 2024, as financial conditions are tighter than normal. Continuity of past policy measures undertaken by the government that include (i) greater public capex spend, (ii) structural reforms and (iii) incentives to boost manufacturing and infrastructure, supports India's medium-term growth outlook. In our view, the RBI is likely to keep policy rates on hold for remainder of 2024 and cut rates in Q1 2025 as inflation moves closer to its medium-term target of 4% amid slowing growth. However, the quantum of easing in this cycle is likely to be shallow.

Key risks to our macro-outlook are: 1) Global growth slowdown, 2) Persistent high inflation, 3) Escalating geo-political tensions.

Key chart

For FY2025, India's GDP is expected to grow at 6.9% and CPI is expected to average 4.5%.

Fig. 3 **India's growth-inflation dynamics stronger than peers**

GDP Growth (Y/Y) and CPI Inflation (Year average) – Bloomberg consensus estimate*

Source: Bloomberg, Standard Chartered

Macro views at a glance

Factors	View	Comments
Economic growth	◑	**Economic activity improves in October.** India's Manufacturing and Services PMI rose in October 2024 to 57.5 and 58.5 amid improving demand. Industrial production contracted by 0.1% y/y in August 2024 compared to the 4.7% growth recorded in the previous month.
Inflation	◓	**India's consumer price inflation rose to 5.5% in September 2024,** partly due to a high base effect and a rise in food article prices. Core inflation rose to 3.6%, rising for the third consecutive month since hitting an all-time low of 3.1% in May 2024.
Fiscal deficit	◑	**The government prioritized fiscal consolidation while supporting growth in the latest budget.** FY 2025 fiscal deficit is estimated at 4.9% of GDP vs interim budget target of 5.1%. GST collections surged in October 2024 to INR 1.87trn, the second highest monthly collection.
External	◓	**India's trade deficit fell to USD 20.8bn in September 2024 compared to USD 29.7bn in August 2024.** Imports rose 1.6% y/y to USD 55.4bn, while export fell 0.5% y/y to USD 34.6bn. India's current account recorded a deficit of USD 9.7 bn or 1% of GDP in Q1 FY2025 compared to a surplus of USD 4.6bn or 0.5% of GDP in Q4 FY2024. This was driven primarily by a widening of merchandize trade deficit.
Monetary Policy	◓	**The RBI kept policy repo rate unchanged at 6.5% in its September 2024 policy review for the tenth consecutive meeting.** The RBI shifted its monetary stance to 'neutral' from 'withdrawal of accommodation' while retaining its focus on inflation. Further, the RBI retained its GDP growth forecast for FY 2025 at 7.2% y/y and retained its average inflation forecast for FY 2025 at 4.5% y/y.

Source: Bloomberg, Standard Chartered India Investment Committee

Legend: ○ Not supportive ◐ Somewhat supportive ◓ Balanced ◑ Supportive ● Very supportive

Bonds – at a glance

Key themes

We are neutral on bonds as attractive absolute yields are counterbalanced by below-average yield premiums. Improving bond demand-supply balance given lower government borrowing, higher RBI dividend and India bonds' inclusion in the global bond indices is a tailwind for bonds. We stay overweight medium and long-maturity bonds given their attractive carry and potential for higher price gains as bond yields fall. We prefer corporate bonds (i.e., bonds that offer a yield premium over government bonds), especially high-quality (AAA) corporates, given higher absolute 'carry' yields and cyclically high spreads.

In our view, the RBI's prolonged pause on policy rates, indicates the likelihood that bond yields have peaked. We expect 10-year IGB yield to trade in the range of 6.50%-6.75% over the next 6-12 months. In our assessment, high quality (AAA) corporate bonds offer a better risk-reward given attractive spreads and improving corporate fundamentals. In addition, India's nominal bond yields is among the highest in Emerging Markets.

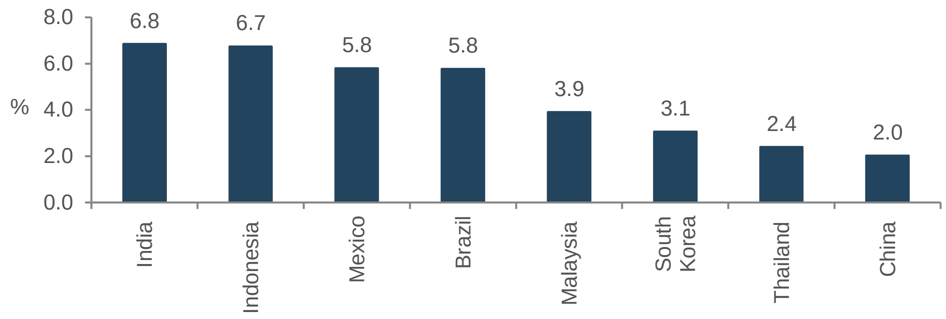
However, three factors for bonds remain unfavorable: 1) High fiscal deficit over the medium-term, 2) Tight banking system liquidity and lack of outright support from the RBI, and 3) A populist tilt in government policy focus could drive inflation higher.

Key chart

India's nominal bond yield the highest among Emerging Market peers.

Fig. 4 India's nominal bond yield the highest

10-year government bond yields (%)



Source: Bloomberg, Standard Chartered.

Bond views at a glance

Factors	Views	Comments
Real Yields	◓	**India's inflation-adjusted yield is lower than most Emerging Market peers**. The 10-year IGB real yield at 1.3% is lower than the average real yield of 3.0% for other major EMs.
Supply dynamics	◓	**Government bond supply dynamics have turned favorable**. The government pegged its gross borrowing for FY 2025 at ~INR 14.0trn compared to INR 15.4trn in FY 2024. Both, FY 2025 fiscal deficit and government borrowing target was lower than market expectations.
Monetary policy	◓	**Market expects no rate cuts by the RBI in the near-term**. 1-year Overnight Indexed Swap (OIS) spread suggests market participants expects the RBI to stay on hold over the next 12 months.
Liquidity	◓	**The RBI's focus remains on withdrawal of excess liquidity**. The banking system liquidity remains in surplus, currently at INR 2.74bn after hitting a deficit of INR 1.6trn in June. Improving government spending could keep the banking system liquidity benign in H2 2024.
Demand dynamics	◑	**Foreign investors remain buyers in October 2024**. YTD 2024 foreign investors inflows are positive and is likely to stay robust given India's bond inclusion in global indices. Demand from domestic institutional investors (banks, insurers and mutual funds) will be a key determinant of bond yields in 2024.
Yield premiums	◓	**Yield premiums trade below-average**. The spread between 10-year IGB yield and repo rate is at 31bps vs. 5yr avg. of 155bps. High-quality (AAA) bonds have turned attractive with the yield spread between 3Y AAA rated bond and 3Y G-sec at 76bps, higher than 43bps in Oct 2023 and 5yr avg. of 56bps.

Source: Bloomberg, Standard Chartered India Investment Committee

Legend: ○ Not supportive ◐ Somewhat supportive ◓ Balanced ◑ Supportive ● Very supportive

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Equity - at a glance

Key themes

We stay neutral on Indian equities. India's superior macro fundamentals to peers, robust earnings delivery and strong domestic investor inflows are counter balanced by stretched valuation premiums, both absolute and relative to peers and foreign investor outflows. We expect volatility to stay elevated in Q4 2024 amid weak Q2 FY2025 earnings season, heightened geopolitical tensions and uncertainty on Trump's policy priorities. Within equities, we are overweight large-cap equities given higher margin of safety in terms of earnings and stronger balance sheets to withstand market transitions.

In our view, Indian equities is likely to be supported by the below positive drivers: 1) GDP growth and earnings outlook remains robust and is likely to outpace its major peers. 2) Stable inflows from domestic investors driven by inflows into systematic investment plans and 3) Resumption of foreign investor inflows amid superior macro fundamentals, US Fed rate cuts and low foreign investor positioning towards Indian equities.

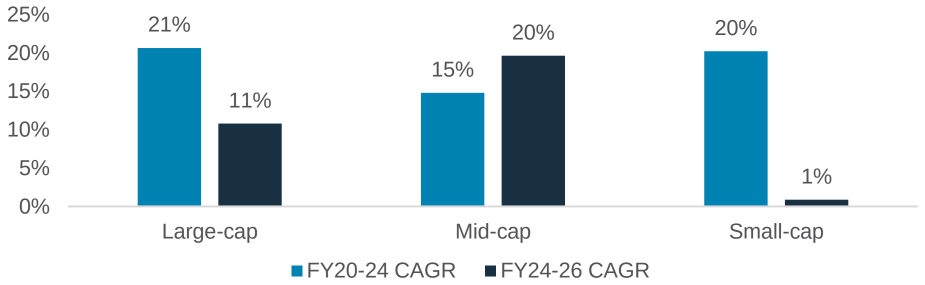
Risks to our positive equity view are: 1) Growth slowdown and probable downgrades of earnings expectations, 2) Elevated equity valuations, both absolute and relative to peers, 3) Foreign investor selling amid slowing domestic investor flows

Key chart

Bloomberg Consensus expectation is for Nifty earnings to rise by 11% over the next 2 years.

Fig. 5 **Large-cap equities earnings expectations robust amid strong delivery**

EPS Growth CAGR: Nifty 50, Nifty Midcap100 and Nifty Smallcap100 Index



Source: Bloomberg, Standard Chartered

Equity views at a glance

Factors	Views	Comments
Economic environment		**Growth-inflation dynamics remain supportive of equities.** Growth focused fiscal policy, improving real income levels and broadening growth momentum is likely to support corporate profitability. Volatile food article prices, remains a key risk.
Earnings growth		**Earnings growth expectations are robust.** Nifty index delivered 23% EPS growth in FY 2024, significantly ahead of estimates. Bloomberg consensus earnings growth expectations for the Nifty Index for FY 2025 and FY 2026 stands at 7% and 14% respectively. EPS estimates for large-cap equities (Nifty index) have seen modest downward revision compared to broader markets.
Valuations		**Valuations stretched**. Nifty 12-month forward P/E at 21.4x, is below its peak of 23x, but higher than its long-term average of 18.0x. Price-to-book value ratio (P/B) at 3.9x and Market cap to GDP ratio at ~140%, are above long-term averages. Mid-cap equities 12-month forward P/E trades at 42% premium to large-cap equities, significantly higher than its 10-year average premium of 19%.
Flows		**Foreign investors sold a record USD 11bn in October.** YTD 2024, foreign investors have bought about USD 0.2bn worth of equities compared to USD 21bn inflows in CY 2023. **Domestic institutional investors remain buyers in 2024**. YTD 2024, domestic institutional investor inflows touched an all-time high of USD 54bn compared to USD 22.3bn inflows in CY 2023.

Source: Bloomberg, Standard Chartered India Investment Committee

Foundation: Asset allocation summary

Legend: ○ Not supportive ◐ Somewhat supportive ◓ Balanced ◑ Supportive ● Very supportive

Summary			**View vs. SAA**	**Conservative**	**Moderate**	**Moderately Aggressive**	**Aggressive**	**Very Aggressive**
Cash			◆	25.0	5.0	5.0	5.0	0.0
Fixed Income			◆	55.0	55.0	40.0	25.0	15.0
Equity			◆	15.0	35.0	50.0	65.0	80.0
Commodities			◆	5.0	5.0	5.0	5.0	5.0
Level 1	**Level 2**	**Level 3**						
Cash & Cash Equivalents			◆	25.0	5.0	5.0	5.0	0.0
Fixed Income	Short-term Bonds		◆	37.1	31.7	25.8	15.6	9.1
	Mid/Long-term Bonds		▲	17.9	23.3	14.2	9.4	5.9
Equity	DM Equity		▲	2.5	4.9	7.4	9.9	12.5
	Asia Ex-Japan / Other EM Equity		◆	1.4	2.8	4.2	5.6	7.0
	Indian Equities	Large-cap equities	▲	9.3	22.8	32.1	41.4	50.7
	▲	Mid/small-cap equities	▼	1.8	4.4	6.3	8.1	9.9
Commodities (INR Gold)			◆	5.0	5.0	5.0	5.0	5.0
				100	**100**	**100**	**100**	**100**

▼ Underweight ◆ Neutral ▲ Overweight

Source: Bloomberg, Standard Chartered

All INR converted exposure. For illustrative purposes only. Please refer to the disclosure appendix at the end of the document

Performance of our calls

	Open calls	Open date	Close date	Absolute	Relative
Equities	Indian large-cap equities to outperform mid-cap and small-cap equities	18-Dec-23			✗
Bonds	Indian mid-and long- maturity bonds to outperform short-maturity bonds	18-Dec-23			✓

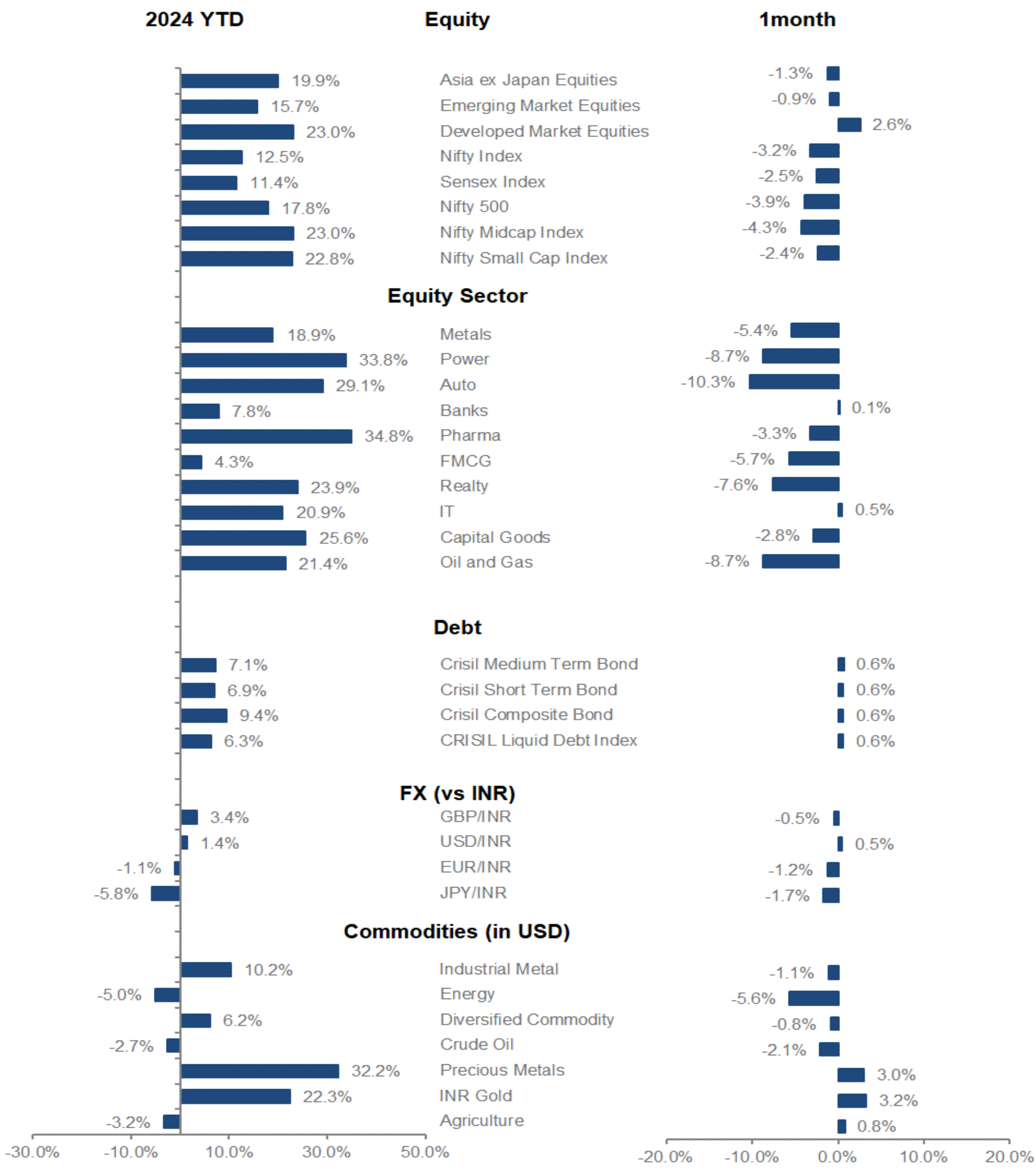
	Open calls	Open date	Close date	Absolute	Relative
Equities	Indian equities to outperform all other asset classes	18-Dec-23	5-Jun-24		✗

Source: Bloomberg, Standard Chartered. Performance measured from 18 December 2023 (release date of our 2024 Outlook) to 8 November 2024 or when the view was closed.

Legend: ✓– Correct call; ✗ – Missed call; n/a – Not Applicable.

Past performance is not an indication of future performance. There is no assurance, representation or prediction given as to any results or returns that would actually be achieved in a transaction based on any historical data.

Market performance summary*



Source: MSCI, NSE, S&P BSE, Crisil, Bloomberg, Standard Chartered

*2024 YTD period from 31 December 2023 to 8 November 2024. 1-month period from 10 October 2024 to 8 November 2024.

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