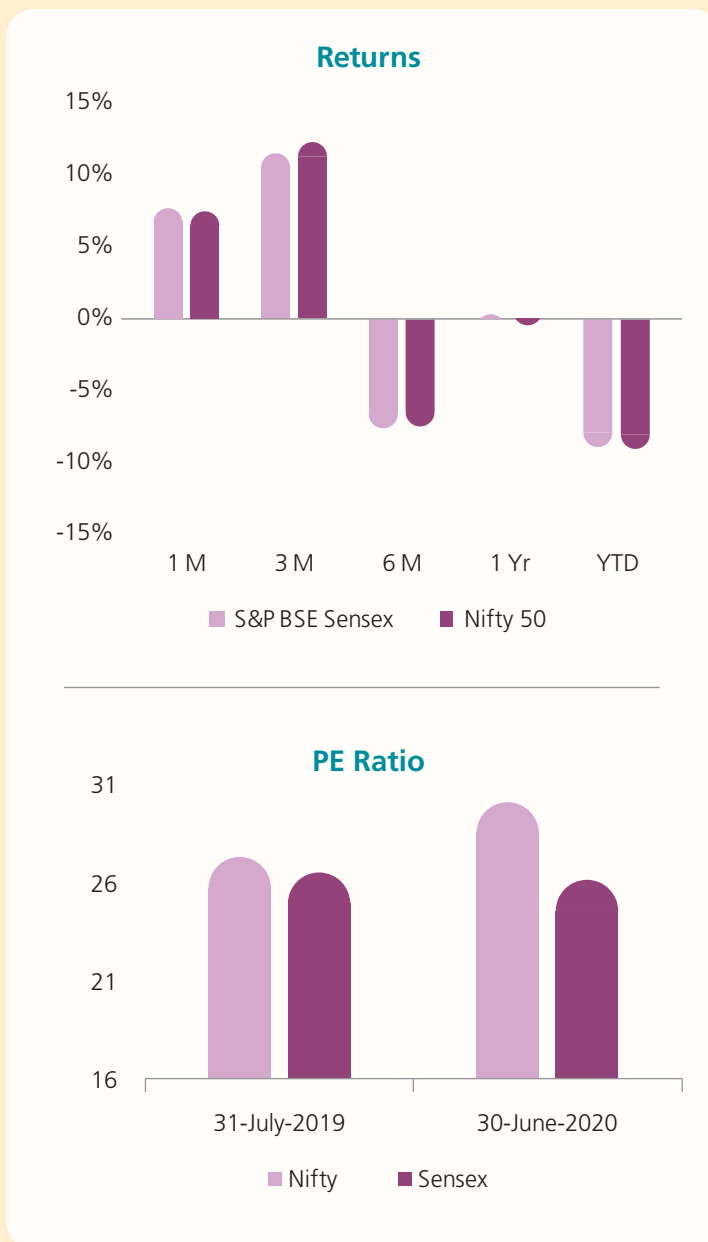




Indian equity market continued their upward momentum in July with markets rebounding by 46% from March lows and only 10% below YTD/all-time peak in mid-January. Markets continued to move higher despite the relentless increase in daily new COVID-19 cases and earnings downgrades. However, the rally in July lacked breadth, given 2/3rd of the market uptick is contributed by small set of stocks.

India volatility index moderated for the 4th consecutive month and declined 17% in July. MSCI India (US\$) rose 10.1% in July outperforming peers MSCI Emerging Market (8.4%) and MSCI APxJ (7.5%), with YTD underperformance paring to 6-9%. Nifty 50 and S&P BSE Sensex ended the month of July with 7.5% and 7.7% returns, respectively.

Indian domestic market outperformed the peer group MSCI Emerging Market (+7.5%). MSCI AWI Index ended with 3.8% returns. Among broader markets, Midcap index underperformed the Largecap index by 230 bps while Smallcap index underperformed the Largecap index by 250 bps. BSE Midcap and BSE Smallcap indices ended the month of July with 5.4% and 5.2% returns, respectively.



GLOBAL MARKETS

Global equities witnessed mixed trends in July post the continued upward trajectory seen across markets till the last month. In equities, emerging market outperformed, led by China, while the tech-heavy S&P 500 also did well. July was quiet a month for developed market central banks as Fed, ECB and BoJ all held policy rates unchanged.

Worldwide, major indices saw divergent trends. Dow Jones was the out-performer with 2.4% returns, followed by Hang Seng 0.7%, Euro Stoxx (-1.8%), and Nikkei (-2.6%). FTSE100 was the worst performer, dipping by 4.4%.

SECTOR PERFORMANCE



Indian equity markets outperformed both the peer group and major global indices. Information Technology was the best performing sector with 22.6% returns outperforming Sensex by 14.9%. Tech (16.8%), Healthcare (12.4%), Metal (8.5%) and Auto (8.0%) also outperformed the Sensex.

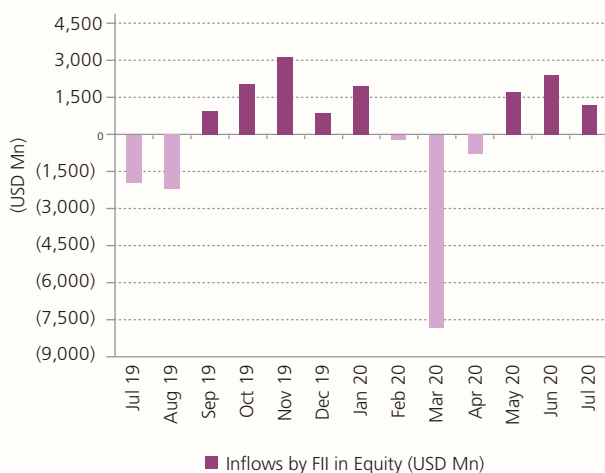
Consumer Durables (5.6%), Oil & Gas (4%), FMCG (1.7%) and Banks (1.3%) underperformed the Sensex. Capital Goods and Power were the worst performing sectors with (-1%), and (-2.3%) returns, respectively.

INSTITUTIONAL ACTIVITY

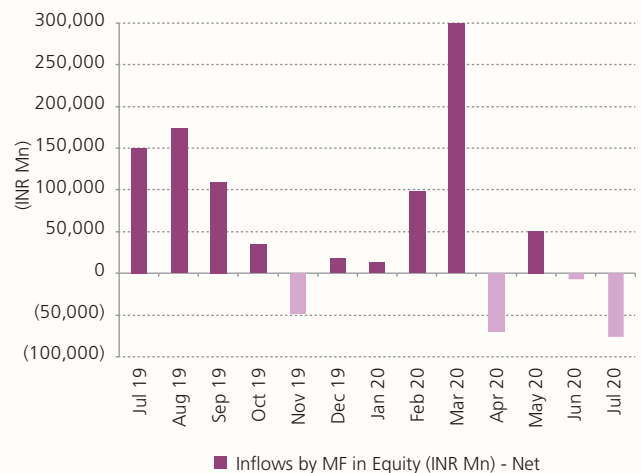
FII recorded net inflows of \$1.3 bn into Indian equities in July vs inflows of \$2.5 bn in June taking FY21 net inflows to \$5.5 bn. July is the third consecutive month of net FII inflows. DIIs were net equity sellers of US\$1.3 bn in July vs inflows of \$321 mn in July taking FY21 tally of inflows to \$0.4 bn.

Within DIIs, Mutual Funds were net equity sellers at \$1 bn while Insurance Funds were net equity sellers at \$314 mn in July. Mutual fund and insurance fund flow data is as of July 29, 2020.

Inflows by FII in Equity (USD Mn) - Net



Inflows by MF in Equity (INR Mn) - Net



MACRO-ECONOMIC DEVELOPMENTS

Headline CPI for June at 6.1% was higher than market expectations. Core inflation increased from 3.9% in March to 5.4% in June, highest since Feb-19. Despite weakening demand, the supply shock has been large enough to increase pricing pressure in near term. Food inflation at 7.4% in June has eased from 10.5% in April to 8.5% in May.

June Composite PMI for India improved from 14.8 in May to 37.8 in June. India's services PMI improved to 33.7 in June (vs 12.6 in May). Similarly, the Manufacturing PMI printed at 47.2 in June up from 30.8 in May. Forward-looking demand indicators printed sharp recovery with new orders up 25pts (MoM) to 46.4 and new export orders were up 27pts (MoM) to 38.9.

May IIP contracted by -34.7% (YoY). Consumer non-durables was back at 92% of its pre-COVID-19 levels in May, but consumer durables production was subdued at 35%. Similarly, consumption goods were at 68% of their pre-pandemic levels even as capital goods were at 39%.

India's monthly merchandise trade balance printed a surplus of US\$790mn in June, first surplus in 18 years. Merchandise exports were down -12% (YoY) in June (vs. 36% decline in May and 60% decline in April) and imports were down 48% (YoY) in June (vs 51% decline in May and 59% decline in April).

Imports ex Oil and Gold declined 41% YoY (vs. 34% decline in May), the 17th consecutive month of (YoY) declines. India's FX reserves are close to their all-time peak at \$522.6 bn as of 24th July. INR appreciated by 0.9% and ended month at 74.82/\$ in July.

Benchmark 10-year treasury yields averaged at 5.82% in July (1bps lower vs. June avg.). Global yields have eased meaningfully as central banks globally have cut policy rates aggressively and have announced large QE programs, to counter the negative impact on global growth from the COVID-19 outbreak. US 10Y yields are at 0.53% (-149bps over the last 1 year).

Brent oil price gained 4.7% (MoM) in July to end the month at US\$42.8/bbl following a 11.6% (MoM) gain in July. YTD, oil prices are still 36% down.

OUTLOOK

The sustained up-move in Indian equity market is mainly on the back of improving economic activity supported by good monsoon progress. High frequency activity indicators suggest improvement in urban activity post the removal of local lockdown/stable COVID-19 situation. Late July data shows improving trends in electricity consumption, e-toll collections, PV registrations, retail e-transactions, customs collections, and TV Ads.

Further, Auto sales data in July improved significantly and June GST data shows that inventory levels still need to rise to reach normal levels which could help activity ahead. Unemployment data continues to have stagnated near pre-COVID-19 levels. Petrol and Diesel consumption are now only -11% & -21% (YoY), respectively.

Monsoon trends are positive as cumulative rainfall is in-line with long period average (LPA) levels on an aggregate basis (over June 1 – Aug '20). Out of the 36 meteorological subdivisions, rainfall has so far been excess/normal in 29 meteorological subdivisions and deficient in 7. Summer crop sowing has done quite well with 85% planting done and +10% YoY. This augurs well for rural economy and demand.

India's economy is on the recovery path as indicated by high frequency activity indicators. Further, the good progress of monsoon bodes well for both the rural economy and the overall demand. Although, total COVID-19 cases have now risen to 1.85mn infections, sero sample survey shows high prevalence (16-50%+) of anti-bodies in metros. The doubling rate has increased to 24 days from ~20 days a week ago. A steadily improving recovery rate (66%) along with falling death rate (2.1%) has also been a positive.



Despite near term economic challenges, India's growth story is backed by multiple structural reforms led by stable government, higher demographic dividend, improving ease of doing business and low inflation, which has got further tailwinds in the form of lower crude oil prices. Indian Government is actively focusing on Atmanirbhar Bharat and Make in India as many global companies are in the process to re-structure their supply chain to reduce the geographical risk of high dependency on China.

Overall, the trend shown by high frequency activity indicators is highly encouraging and supporting our view that FY21 will be a year of two halves given the COVID-19 disruptions in the first 3-5 months and expected gradual recovery in the remaining months of the fiscal year. The current market conditions exhibit high correlation among stocks in different sectors and thus, the selection of stocks is important. We stick to companies having core competitive advantage, strong balance sheet and the ability to generate cash flows sustainably.

Source: Bloomberg, MSCI

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