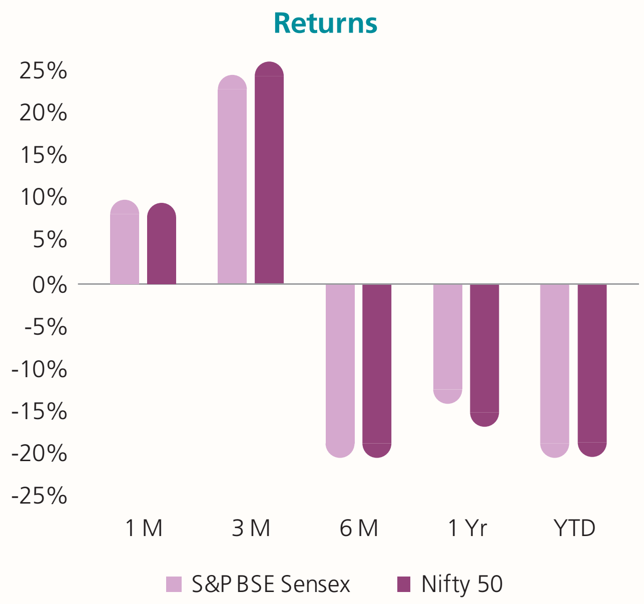
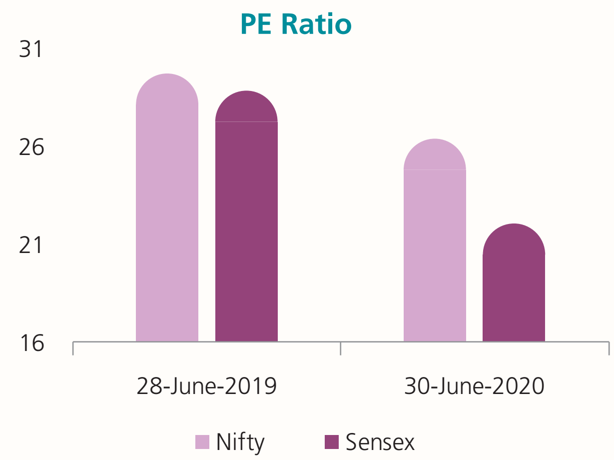
Indian equity market recorded a resilient performance in June, despite increase in COVID-19 cases, downgrades by rating agencies and geopolitical tensions with China. MSCI India (US$) rose 6.8% in June performing in-line with MSCI EM (7.0%) but marginally underperforming vs. MSCI APxJ (7.8%).

Moody's downgraded India's rating to Baa3 with a "negative" outlook. S&P also put Indian Bank ratings on 'Credit Watch' citing a high risk that public sector banks' credit profile could weaken due to COVID-19. Nifty 50 and S&P BSE Sensex ended the month of June with 7.5% and 7.7% returns, respectively.

Indian domestic market outperformed the peer group MSCI Emerging Market (6.9%). MSCI AWI Index ended with 3% returns. Among broader markets, Midcap index outperformed the Largecap index by 250 bps while Smallcap index outperformed Largecap index by 600 bps. BSE Midcap and BSE Smallcap indices ended the month of June with 10.2% and 13.7% returns, respectively.





GLOBAL MARKETS

Global equities continued the upward trajectory despite a volatile month as markets were driven by positive developments on economies re-opening post lockdown, better than expected US economic data, re-affirmation of Phase-1 trade deal between the US and China, and central back liquidity support, offset by concerns about a second wave of infections from the spread of COVID-19 and US-China tensions after imposition of a National Security Law in Hong Kong SAR.

Worldwide, all major indices closed in green. Hang Seng was the outperformer with 6.4% returns, followed by Euro Stoxx (6%), Nikkei (1.9%), and Dow Jones (1.7%). FTSE100 was the worst performer with 1.5% returns.

SECTOR PERFORMANCE

Indian equity markets performed in-line with peer group but outperformed major global indices. Realty was the best performing sector with 12% returns outperforming S&P BSE Sensex by 4.4%. Banks (9.7%) and Auto (8.4%) also outperformed the benchmark indices. Consumer Durables (7.2%), Oil & Gas (7%), Power (6.3%), Metal (5.9%), IT (5.8%), Tech (4.8%) and Capital Goods (4.3%) underperformed S&P BSE Sensex. Healthcare and FMCG were the worst performing sectors with 3.9%, and 3.3% returns, respectively.

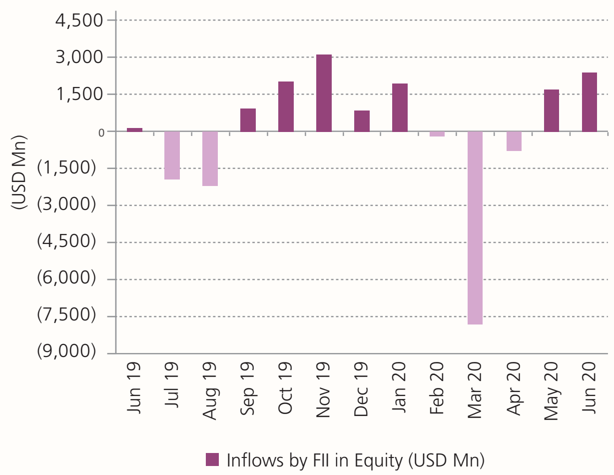
INSTITUTIONAL ACTIVITY

FII recorded net inflows of $2.7 bn in June vs inflows of $1.7 bn in May 2020 taking FY21 net inflows to $4.4 bn. After 2 months of consecutive outflows, May and June month witnessed net FII inflows. DIIs were also net equity buyers of US$321 mn in June vs inflows of $1.5 bn in May taking FY21 tally of inflows to $1.7 bn.

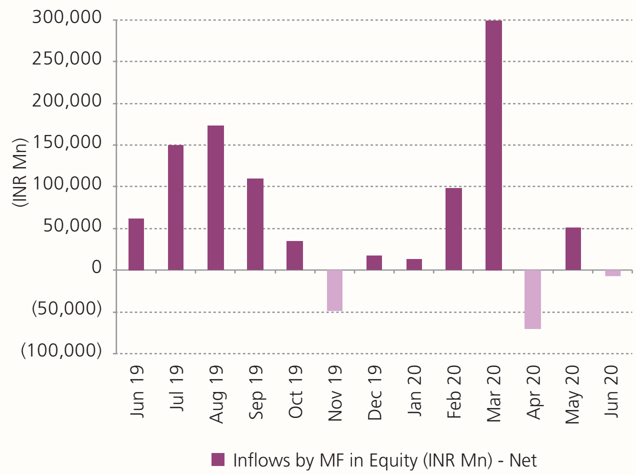
Within DIIs, Mutual funds were net equity sellers at $487 mn while insurance funds were net equity buyers at $401 mn in June.

Note: Mutual fund and insurance fund flow data is as of June 26, 2020

Inflows by FII in Equity (USD Mn) - Net



Inflows by MF in Equity (INR Mn) - Net



MACRO-ECONOMIC DEVELOPMENTS

Headline CPI for May could not be released due to data compilation difficulties like April. However, there was a limited release, which comprised 69% of the CPI basket, largely comprising food. Aggregate food prices, after rising sharply in April by 1.2% (MoM) eased in May by -0.4% (MoM). Softening of food inflation in May was broad-based. Food inflation eased from 8.6% in April to 7.4% in May (YoY).

May Composite PMI for India improved marginally from an all-time low of 7.2 in April to 14.8 in May. India's services PMI remained lacklustre in May, improving to just 12.6 from the record-low of 5.4 in April. Similarly, the Manufacturing PMI printed at 30.8, marginally above its all-time low of 27.4 in April. The print remains significantly below the print that was seen during the GFC of 44.4 (Dec '08). Forward-looking demand indicators remain very soft with new orders printing at just 21.4 in May compared to 12.4 in April. Similarly, export orders were largely unchanged coming in at 11.8 in May vs. 10.3 in April.

April IIP contracted by 55.5% (YoY). This follows an 18.3% decline in March (YoY). While the collapse was across the board, certain essential sectors like electricity (-23% YoY) and consumer non-durables (-36% YoY) were hit less as compared to sectors like consumer durables (-96% YoY), infra goods (-84% YoY) and capital goods (-92% YoY) which recorded large declines.

India's monthly trade deficit for May came in at $3.2 bn declined by $3.6 bn (MoM). The aggregate trade balance (goods and services) was in a surplus of US$4bn in May (vs. US$0.3bn surplus in April). These two months were the first time in four years that the aggregate trade balance was in a surplus, with May being the highest recorded surplus in the series. India's FX reserves are close to their all-time peak at $505.6 bn as of 19 June. INR appreciated by 0.1% and ended month at 75.51/$ in June.

Benchmark 10-year treasury yields averaged at 5.83% in June (5 bps lower vs. May average). 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 0.66% (-135 bps over the last 1 year).

Brent oil price gained 12% (MoM) in June to end the month at US$40.9/bbl following a 55% (MoM) gain in May.

OUTLOOK

Continued resilient performance of Indian equities market is mainly on the back of improving economic activity and good monsoon progress. Late-June data shows E-way bill generation picked up with run-rate now at 83% of pre-COVID rates, improvement of 15ppt over 1HJune levels. Electronic toll collections gathered momentum (WoW) and are now only 18% below Feb'20 levels. TV ads have surged to the highest level of the year and at 111% of pre-COVID rate for top 10 advertisers. Unemployment data continues to show steady improvement. Petrol and Diesel consumption are now only -18% & -15% (YoY), respectively.

Monsoon rainfall has covered the entire country with cumulative rainfall (+20%) above long-period average (LPA) levels on an aggregate basis (over June 1-28, 2020) as the monsoon season has covered the nation ahead of schedule. The all-India monsoon coverage is 12 days ahead of its normal schedule. Previously, such early coverage happened in 2013. Summer crop sowing has done quite well, being double of last year levels. This will augur well for rural economy and demand.

India's economy is on the path of recovery as indicated by improving economic activity indicators. Further, the early onset of monsoon augurs well for both the rural economy and the overall demand. However, the concern continues to stay with the number of COVID-19 cases count still rising.

Several re-lockdowns have happened in Chennai and Assam while Mumbai has now restricted non-essential movement to 2Km. National shutdowns of schools, metro trains & large gatherings have been extended by a month. Despite the challenges posed by COVID-19, we have witnessed the resilience in the Indian economy but the sustainable recovery will depend on the following factors:

(1) Extent of risk aversion in household behavior

(2) More importantly whether initial COVID-19 shock amplifies through credit and labor markets. Worries have also risen on Chinese trade front as Indian government has retaliated with tougher custom clearances and internet app controls

Despite having near term 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 ***Make in India*** as many global companies are in process to re-structure their supply chain to reduce the geographical risk of high dependency on China.

We continue to believe, 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 early economic activity indicators support our view. Companies having core competitive advantage, strong balance sheet and ability to sustainably generate cash flows will not only survive through this crisis but will emerge further stronger with higher market share post COVID-19.

Source: Bloomberg, MSCI