MULTI ASSET DYNAMIC PORTFOLIO

Monthly Update - May 2022

Dear Investors,

So far, the year 2022 has been tough for both, financial markets as well as global growth. Till 2021, the high commodity prices were accompanied by strong rebound in the global economy as we saw jump in pent up consumer demand and resumption of business operations.

The narrative of reflation trade drove the equity prices higher and kept the bond yields lower. Fast forward to 2022, the global growth is slowing and the inflation is touching multi decade highs. The Russia-Ukraine war has put an upward pressure on the already high inflation. With no resolution in sight, the war is going to have a protracted impact on commodity prices including oil, gas and food prices.

Europe is heavily dependent on energy supply from Russia. Due to high energy dependence and geographical proximity, the war has hit European economy much harder and materially raised the risk of economic slowdown in the region.

In the US, the central bank is caught between a rock and a hard place. The Fed wants to pivot quickly to tame the high inflation, but is concerned about a hard landing if it moves too quickly, throwing the economy into recession.

The Zero Covid policy in China has hits its economic growth really hard. The IMF has recently revised down 2022 GDP growth estimates from 4.4% earlier in January to 3.6% in its latest April projection, while upping their inflation forecast numbers for developed and emerging markets. Closer home, high oil prices pose a real challenge to India's economic recovery.

India imports around 85% of its total oil needs. According to a research by Nomura, a 10% rise in crude price shaves off 0.2% from its GDP, distorts its current account balance by 0.3% and increases inflation by 0.4%. If crude price remains above $100 a barrel for a sustained period, it will have cascading effects on inflation and economic growth.

Most of the broking houses have already revised down India's GDP growth rate for this year and next year due to spill-over effects from high oil prices and slowing economic momentum globally.

Figure 1: IMF recently revised down GDP forecast for the year 2022 & 23 while increasing the Inflation forecast (Source: IMF)

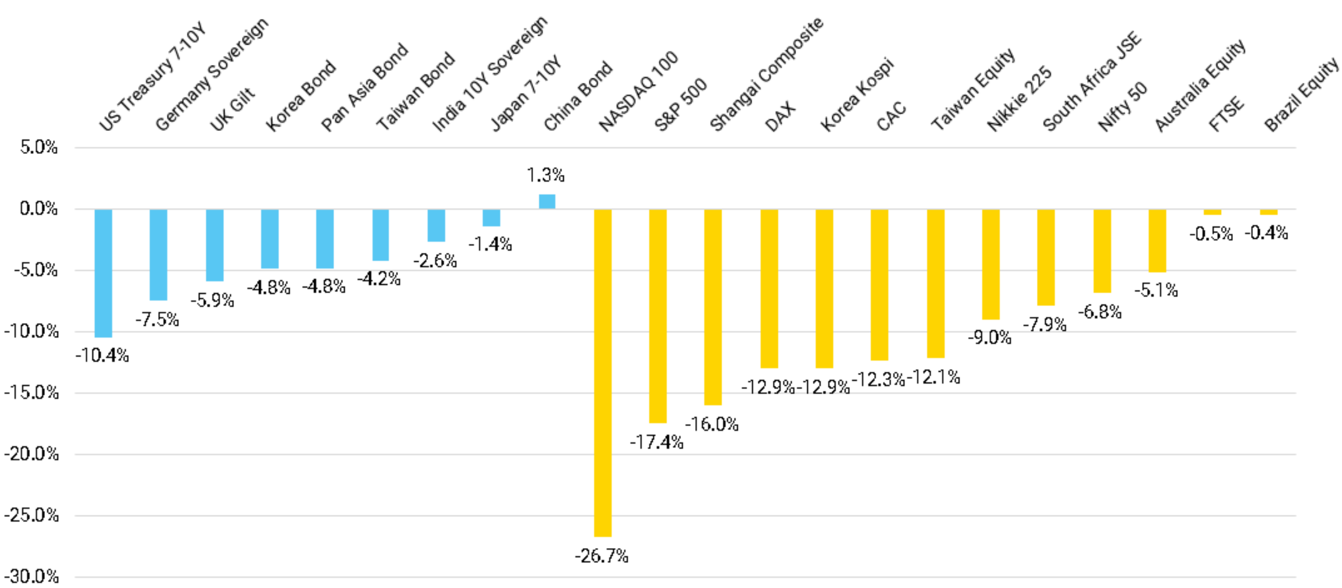
Year		GDP		Inflation	
		Emerging Economies	Advanced Economies	Emerging Economies	Advanced Economies
2022	Old	4.8	3.9	5.9	4.9
	New	3.8	3.3	8.7	5.7
2023	Old	4.7	2.6	4.8	2.0
	New	4.4	2.4	6.5	2.5

Clearly, the global narrative has changed from **Reflation in 2021 to Stagflation in 2022**. Stagflation, a combination of two words “stagnation” & “inflation”, is basically a period of sluggish economic growth along with surging inflation. Global economy went through a long period of stagflation in 1970s that started with Organization of Arab Petroleum Exporting countries putting an embargo on oil imports from Middle East countries. The result was a sharp rise in oil price from $4 a barrel to $12 a barrel in a matter of few months. While the embargo was lifted in March 1974, oil prices remained high leading to fuel rationing and what followed was a deep economic slowdown.

In the periods of very high inflation, the correlation between the equities and bonds turns positive and both of the asset classes undergo correction. Stagflation investing is not easy and there are very few winners in stagflationary periods. Whether or not Europe and the US would experience stagflation largely depends on how the central banks maneuver these tricky times and how long the Russia-Ukraine war continues and its subsequent economic impact.

However, the good news is India is still in much better shape, compared to rest of the world. At 8.2% GDP growth in 2022 & 6.9% in 2023, as projected by the IMF, the economic growth is expected to be fairly robust and continues to be one of the fastest in the world. Hence, in India, it is more a case of moderating growth with high inflation rather than stagflation.

Figure 2: Year to date returns - High Inflation spares neither equities nor bonds (Data as on 11th May 2022)



PORTFOLIO POSITIONING & METER READINGS:

On 4th of May, RBI surprised the markets by hiking repo rate by 40 basis points unexpectedly. Both equity markets and bond markets saw a heavy sell off post the rate hike announcement. The volatility has lingered on in May so far, with sharp correction in equities, especially mid and small caps. With ongoing risk off mood in the markets, there hasn't been a material change in our meter signals since the last month. Our **'Macrometer'** that captures domestic as well as global economic factors continues to indicate slowdown as global conditions remain tough amid slowing US economy and rising strength of US dollar.

The **"Monetary Meter"** stays in contractionary zone as the gap between the US junk bond yields and US treasury yields widens. The **"Momentum Meter"** continues to signal 'out of equities' since November 2021 due to a lack of uptrend in equities. The meter is currently signaling to invest in fixed income instruments.

Similarly, **"Technometer"** is signaling exit equities as the rally seen in late March and early April faded quickly. With heavy sell off in tech stocks and other risk assets such as Bitcoin, the global risk appetite has plummeted with our **"Global RORO"** indicating 'Risk off'.

Our other indicators are gradually turning in favor of equities. The quant sentiment indicator **'Sentimeter'**, being a contrary indicator, is suggesting being equal weight in equities as fear takes the center stage in markets with record FII redemptions and rising percentage of stocks below their 200 day moving average.

On the valuation front, **"Cyclometer"** readings have changed from Highly overvalued to Fairly Valued, with price to earnings and price to book ratio softening from 25x and 3.7x at the peak in October 2021 to 18x and 2.8x respectively.

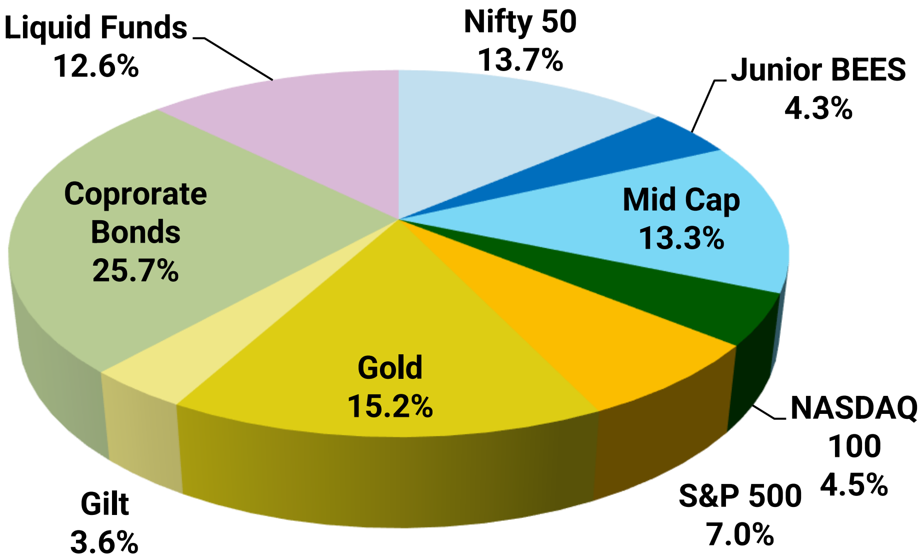
Our **'Relative Valuemeter'** that measures the relative attractiveness of smallcaps vis-à-vis large caps is presenting a similar story of smallcaps currently being fairly when compared to larger companies.

We have maintained our **defensive and risk off allocation mix** as we continue to monitor the global developments and any material change in our signal that warrant change in allocations. For the time being, we continue to emphasize that asset allocation is the best strategy to maneuver these volatile times as the world goes through a regime change with persistent higher inflation and lower growth.

Period	Nifty 50	Nifty Midcap 150	Gold	Corporate Bonds	MADP	Benchmark
1 M	-9.69%	-11.85%	-5.21%	-0.27%	-5.56%	-5.63%

Data from 14th April to 13th May 2022. Benchmark : Crisil Moderate 50:50 Index

CURRENT ALLOCATION



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