MULTI ASSET DYNAMIC PORTFOLIO

Monthly Update - October 2022

01 **We remain marginally overweight on equities (at ~60%) vis a vis the benchmark**

02 **The positive factors that support the marginal overweight are improving sentiment,, momentum and market breadth.**

03 **The factors that caution us from being aggressively overweight include valuations, and global headwinds such as reduced risk appetite, inflation, and a contractionary monetary regime**

Following two consecutive months of positive returns, the Indian markets corrected in September. Nifty 50 fell 3.7%, while Nifty 500 slid 3.2%. The correction was more prominent in large-cap companies, as the Nifty 100 was down 3.7% compared to losses in Nifty Midcap 100 and Smallcap 100 of 2.6% and 1.9%, respectively. FII net flows turned negative again as foreign investors sold Rs. 18,308 crore worth of equities (net) on the back of a strengthening dollar, rising interest rates, and inflation uncertainty. The Indian market, however, continues to fare better than its global peers, with the S&P 500 and Nasdaq 100 shedding 9.3%, and 11.1% respectively in September. The Gold too, corrected sharply as a result of aggressive tightening by the global central banks, falling by 1.6% (in INR) during the month.

On 21st September, the Fed raised the interest rates by another 75bps. This was the third back-to-back 75bps rate hike this year by the US central bank. With the latest hike, the Fed Fund Rate (FFR) now stands in the range of 3.0%-3.25% and is the highest since January 2008. The FOMC revised the median FFR by 100bps to 4.4% at the end of 2022, up from 3.4% in June. This indicates a cumulative rate hike of 125bps over the next 2 FOMC meetings this year. For 2023, the median FFR is revised to 4.6% vs. 3.8% in June, suggesting no rate cuts in 2023 and maintaining the terminal rate of 4.6% till 2024. These projections are much more aggressive than what investors had been pricing earlier. The dot plot projections are suggesting that the Fed will ‘keep at it’ till it can see inflation coming down under its target range.

Closer home, the RBI hiked the repo rate by 50bps to 5.9% and maintained the withdrawal of the accommodative stance. The rate hike was on the expected lines as most market participants were expecting this raise after an aggressive rate hike of 75bps by the Fed. However, the highlight of the MPC meeting was the positive commentary on the domestic economic outlook by the central bank. While it cut the GDP projection for FY23 marginally to 7% from 7.2% earlier, mainly due to lower GDP print in the last quarter, it appeared confident that the growth momentum would continue despite external headwinds. The governor in his speech mentioned that the private urban consumption is holding up well in Q2FY23 and the rural demand is picking up pace gradually. The non-oil and non-gold imports are resilient highlighting healthy domestic demand. The bank credit is at a 9-year high, recording 16% growth year-on-year. The corporate balance sheet is leaner today, with the corporate debt-to-GDP ratio at a 15-year low. The capacity utilization for the manufacturing sector, at 74.3, is the highest in 3 years. The governor also assured that it has ample forex reserves to meet the near-term demands and it is not overspending to contain the rupee volatility.

The RBI refrained from giving any forward guidance on future rate hikes and said that going forward the rate hikes will be data-driven. Given the uncertainty in the global inflation trajectory and the action of global central banks in response to the incoming inflation data, the domestic monetary policy will be largely driven by the global monetary tightening cycle. Going by the Fed dot-plot and a terminal rate projection of 4.6% in the US, we may see another 50-60bps of cumulative rate hikes this financial year, and expect the terminal rate to be around 6.5% for India.

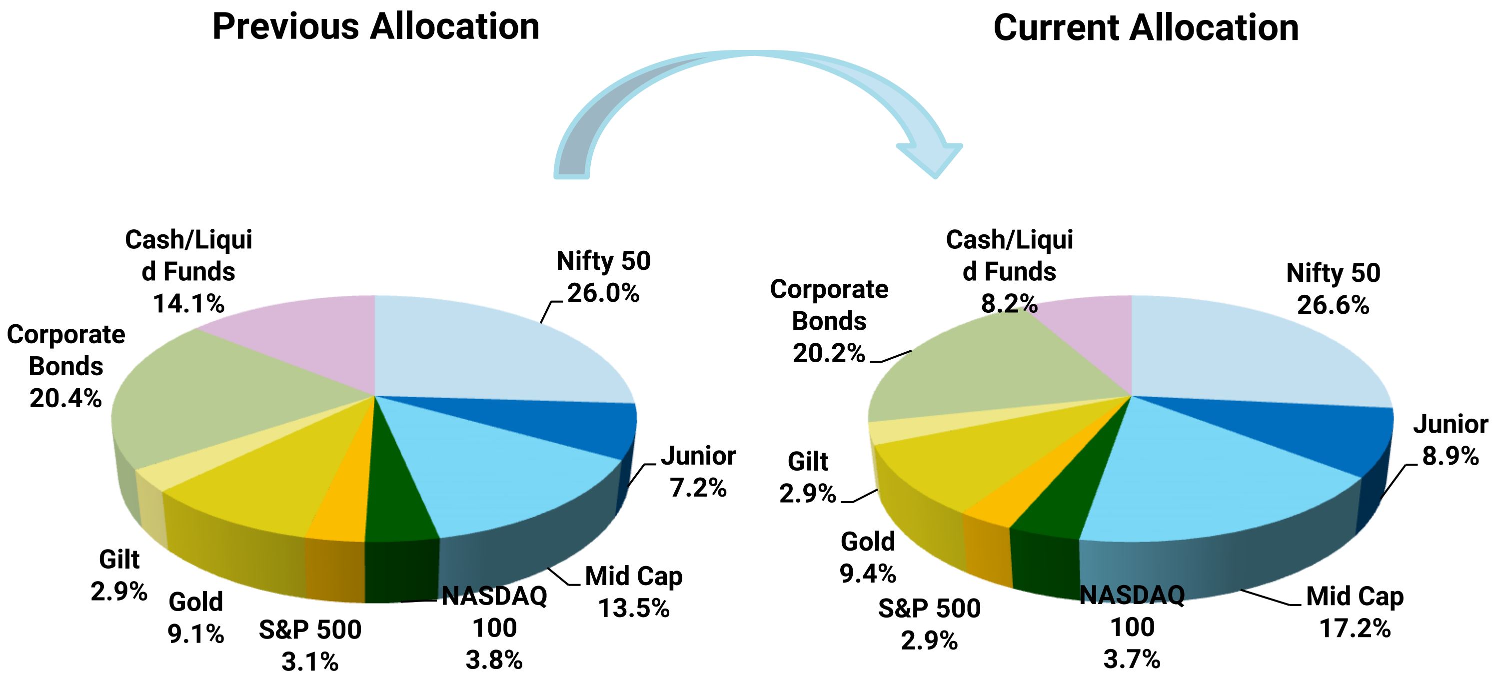
PORTFOLIO POSITIONING & METER READINGS:

We continue to be marginally overweight on equities vis-à-vis the benchmark. Our quant model suggests improved sentiments, momentum, and market breadth in domestic equities. Our **'Macrometer'**, which captures domestic as well as global economic factors, indicates robust economic growth in India. Last month saw a jump in auto sales as we enter into the festive season. The manufacturing and services PMI moderated to 55.1 and 54.3 respectively. Our technical indicator **'Technometer'** maintains a buy in Indian equities. The **'Momentum Meter'** is signaling to invest in equities after outperformance of domestic equities over other asset classes. The quant sentiment indicator, **'Sentimeter'** , is suggesting improved market breath, though reversal of FII flows acted as dampener in the sentiment.

On the valuation front, equity markets' price-to-earnings and price-to-book multiples are at 20.2x and 3.0x respectively, which still conveys a not so attractive value proposition signaled by the **'Cyclometer'**. The **'Relative Valuemeter'**, which measures the relative attractiveness of smallcaps vis-à-vis large caps, is presenting a similar story of smallcaps currently being slightly expensive when compared to larger companies. The '**Global RORO**' is Risk Off due to deep correction in risk assets during August and September in developed markets. The '**Monetary Meter**' continues to point towards tighter monetary conditions globally, thus suggesting to keep it light on duration.

The combined portfolio weight is pointing to being relatively overweight in equities vis-à-vis the benchmark. We have kept our allocation of bond portfolio to 23% at portfolio level with maximum exposure (approx. 20%) to short to medium duration and target maturity funds and 3% allocation to long duration funds. We maintain our allocation to gold at 9.4% with gold prices being vulnerable to interest rate hikes. We have reduced our cash allocation equivalent to the increase in the equity allocation.

CURRENT ALLOCATION



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