# Pranitya Wealth LLP
# Market Outlook
# October 2024 | Volume 51

## Overview

As we mentioned in the last outlook, Nifty had crossed 24000 mark and Sensex had crossed 79000 by August end. In the month of September markets reached their all-time high with Nifty crossing 26000 and Sensex 85000. The final leg of the rally was swift, as anticipated, with large-cap stocks moving up, although many remain below their 52-week highs.

### Nifty returns

As of September 30, 2024, Nifty delivered a 18.7% return over the past year. Other indices, except for Banking and Finance, delivered significantly higher returns, highlighting the performance gap between large-cap and midcap stocks:

Nifty Midcap: up 46.32%

Nifty Small Cap: up 51.56%

Nifty Realty: up 91.44%

Nifty Energy: up 57.75%

Bank Nifty: up 16.38%

Nifty Finance: up 20.71%

### Is it time to exit mid and small caps?

In terms of valuation, large-cap stocks, representing 65% of the total market cap, are reasonably priced, while midcaps and small caps have seen some corrections in the past two weeks. Given that large-cap valuations are closer to their long-term averages, it may be prudent to gradually shift from higher-priced midcap and small-cap stocks. Companies with inflated valuations are at risk of significant corrections, making midcaps and small caps more vulnerable to downturns. This strategy aims to reduce the potential risks associated with volatility in smaller stocks.

## Macros

**Inflation:** Core inflation is decreasing at 4.7%, while food inflation remains high. However, a good monsoon could help bring food inflation down. Previously, inflation targeting was a key focus for the RBI, where interest rate movements were primarily determined by inflation figures alone. This approach aimed to control price stability by adjusting rates based on inflation trends. However, broader economic indicators are now considered to form a more holistic monetary policy framework.

**GDP:** India's GDP growth is projected to remain robust, exceeding 7% over the next 5 to 6 years, as anticipated by both the Reserve Bank of India (RBI) and the government. If this forecast holds true, the Indian stock market, supported by significant earnings growth over the past 14 to 15 years, could emerge as an optimal investment destination for those looking to allocate their funds effectively.

**Tax Numbers**: Advance Tax collections up to September 2024 have shown a robust growth of 20%, with a tax-to-GDP ratio exceeding 11.1% for the fiscal year 2023-24. This is compared to 11.20% in 2022-23, supported by a 6.60% increase in direct tax collections. This positive trend indicates strong revenue generation and fiscal management by the government. The total net GST revenue for September reached ₹1,47,098 crore, which is a 3.9% rise compared to the previous year. Overall, the growth in tax collections continues to show positive trends, contributing to the fiscal health of the country. GST collection is on track and likely to pick up in next two quarters.

**Private Investment:** Confirmation of revival of private investment is emerging from dividend payout cycle of spectrum of companies last year. The dividend payout ratio of 1300 companies slid to a nine-year low as they drew down surpluses for company expansion. Investment growth numbers are higher than Income growth even before government tapers its capex which means private growth is contributing significant amount

**Current Account Deficit:** As of the first quarter of FY25 (ending September 30, 2024), India recorded a current account deficit (CAD) of $9.7 billion, which is approximately 1.1% of its GDP. This increase in CAD was primarily driven by a rise in the merchandise trade deficit, which grew to $65.1 billion compared to $56.7 billion in the same quarter of the previous year. Despite this, net services receipts increased, and private transfer receipts also rose.

**Fiscal deficit:** As of September 2024, India's fiscal deficit stood at ₹6.39 lakh crore, accounting for 27% of the total budgeted fiscal deficit for the fiscal year 2024-25. This deficit represents 3.2% of the GDP, which aligns with the government's target of keeping the fiscal deficit under 5.1% for the year.

**FPIs and FDIs.:** September 2024 was a particularly strong month for FPI inflows, with investments worth ₹57,724 crore—marking the highest monthly inflow since December 2023, when FPIs invested ₹66,135 crore into Indian equities. This surge can be largely attributed to the Fed’s aggressive interest rate cut, which made Indian assets more attractive. India will be able to borrow long term bonds at attractive cost to support deficit. RBI is talking about 30 years bond for the first time

**Global Economy:** The Israel–Hamas conflict is worsening, and Iran's support for Hamas could lead to more trouble. The market isn't fully considering how this conflict might impact oil prices, which could rise due to supply disruptions, affecting many economies. India's market could also feel the effects of global slowdowns. Issues in the Red Sea are causing delays in trade, while China's economic slowdown is leading to more container ships sitting idle, raising shipping costs for exporters. China's market is emerging as an attractive investment destination, as reflected by the recent rebound in Chinese equities, signaling a shift in global portfolios. For the past two months, we have highlighted this positive tilt towards China in our outlook, recognizing the potential opportunities in the region amidst its evolving economic landscape.

Current Gulf issue may not impact Indian growth to a larger extent, and this could be a short term set back. India will be able to borrow long term bonds at attractive cost to support deficit. RBI is talking about 30 years bond for the first time

**Areas of Concern**

India's trade deficit is a major concern, mainly caused by high gold imports and delays in exports.

On a positive note, production inflation is expected to fall as the monsoon season wraps up, and the recent heavy rainfall could provide a boost to the rural economy.

With the festive season starting, there is hope for economic improvement in the next two quarters. Additionally, government initiatives like the Production-Linked Incentive (PLI) scheme are critical for increasing job opportunities by 40%, a trend observed over the past three years. These efforts can help strengthen various sectors and support overall growth in the country.

The RBI has done a good job keeping inflation in check and stabilizing the currency without using dollar reserves.

Recent tax changes have made it more expensive to switch investments, affecting PMS and AIFs more than mutual funds, which can help lower tax costs if held for the long term. Banks are seeing strong growth in loans and deposits, which may slightly impact their profits, while NBFCs seem unaffected.

The Fed might cut rates by 50 basis points, but India may not follow. Banks will offer higher rates to attract deposits, keeping their valuations lower.

Peak power production and consumption suggest strong economic activity in the country.

On going Geopolitical tensions (Israel- Iran) and economic uncertainty may prompt central banks to reconsider rate cuts, influenced by rising oil prices and conflicts in the Middle East. This could lead to a shift towards tightening policies, impacting global markets, particularly in emerging economies like India.

**What direction is the market heading in?**

Local support for the market is increasing daily, with SIP inflows rising to ₹31,000 crore per month, and this could soon reach ₹50,000 crore. Sector rotation is crucial, especially at the current market levels, as there is no fixed rate for asset allocation; multiple factors must be considered. While some profit booking is advisable, staying entirely out of the market would be a mistake. Positive trends in consumption patterns, demand, and business confidence indicate promising growth ahead. Sensex or Nifty may not experience a correction, but small and midcaps, which are not part of these indices, could undergo either a time correction or a price correction. We plan to invest cautiously, aiming for long-term targets higher than current levels.

India has made significant strides in manufacturing exports, largely driven by the Production Linked Incentive (PLI) scheme and similar incentive programs. These initiatives have boosted production capacity, attracted foreign investments, and helped position India as a competitive player in global manufacturing, especially in sectors like electronics, automotive, and pharmaceuticals. Banking sector has seen significant jump in credit growth along with deposit growth but nothing on similar lines for NBFCs. Overall, market is expected to perform well and pick up more in coming 2 months with the onset of festive season.

**Asset allocation**

Please always keep asset allocation in mind. When your country is growing at over 7% GDP with a stable government at the center, it’s an optimal time to allocate more to equity than debt, especially if your time horizon is 3 to 5 years. Under-allocation can hamper long-term compounding, and frequent changes in asset allocation in anticipation of any short-term volatility which can negatively impact long-term returns.

**Fixed Income**

Bond yields have slightly decreased following the Federal Reserve's interest rate cuts, with the 10-year bond currently trading at 6.86%. As a result, returns on long-term bond funds are becoming more attractive. However, yields may not decline rapidly since banks are maintaining elevated deposit rates to attract savers. Recent changes in the taxation of Funds of Funds (FoFs), Exchange-Traded Funds (ETFs), and Real Estate Investment Trusts (REITs) have provided investors with more tax-efficient options, such as ETFs and precious metals like gold and silver, which have seen a surge in demand. We still favor hybrid funds, regardless of equity taxation, as they allow investors to manage tax liabilities effectively by opting for growth options.

## Gold and Silver

We maintain a positive outlook on gold, particularly due to ongoing geopolitical tensions. Central banks are showing signs of increasing their gold purchases, especially as the Federal Reserve's aggressive rate cuts have contributed to a weakening dollar. Our previous analysis highlighted several reasons for our bullish stance on gold, and those reasons remain valid. Meanwhile, silver prices have risen by 7% in September 2024, and we anticipate that demand for silver will outstrip supply, potentially leading to favorable returns from silver exports over the next few years.

## Conclusion

We remain optimistic about Indian equities over the long term, but investors should be prepared for near-term volatility driven by current macroeconomic factors and geopolitical tensions. The market is expected to stay largely range-bound in the near term, with large-cap stocks likely attracting more attention as the preferred choice for cautious investors. While there will be some sector rotation, overall market stability should continue.

Investing gradually through SIPs helps mitigate risk significantly while allowing you to stay invested in the market, benefiting from long-term growth potential and compounding returns.

It's also wise to include gold and silver in your portfolio for added security. Patience is important, as the market may slow down while waiting for new developments. A focused approach on specific stocks is advisable since some areas of the market are currently undervalued.