Fed pause in rate hikes has to led to risk-on trade but India geared to outperform

Synopsis
With the Fed pausing hike in interest rates in November and US inflation slowing down from 3.7% to 3.2% and core CPI falling to 4%; the US 10-year interest rates fell almost 50 bps to 4.4% and Barclay's Agg. Bond Index moved up 4%. This led to Euphoria in the Global Equity markets; NASDAQ moving up 9%, MSCI EM up 6% and MSCI World up 7%, outperforming MSCI India which was up only 2%.

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The **global markets** are up 7-9% in the last month, outperforming the Indian markets after almost 6 months. The global euphoria was probably due to **Fed** taking a pause in **interest rate hikes** and inflation nos. of US and the world getting softer. Indian market premium valuations too played a role for **India** not participating though it is amongst the best performing markets in the last 6 months. We believe India's strong earnings growth trajectory and macro environment should help India relatively regain its outperform in the months to come. Technical factors like FII ownership being amongst the lowest in a decade coupled with strong retail domestic inflows augur well for the Indian equity markets in the longer term.

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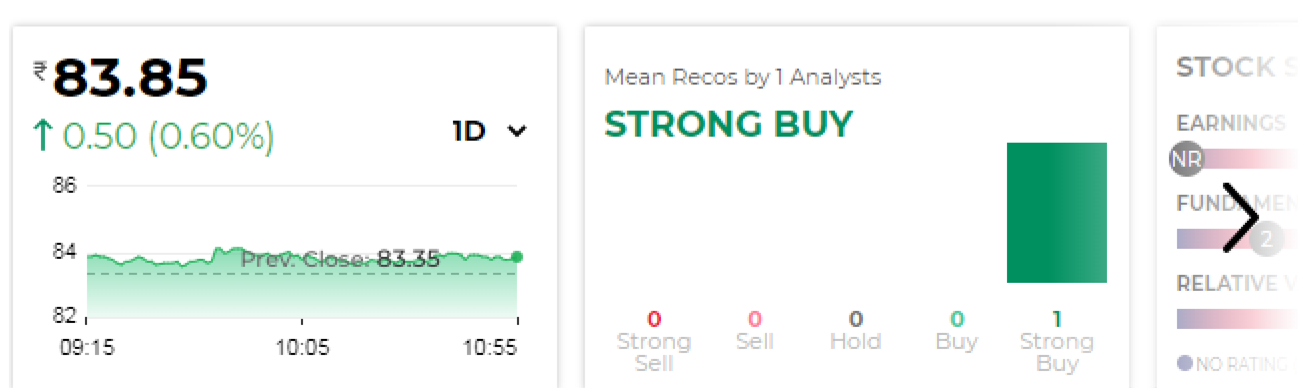
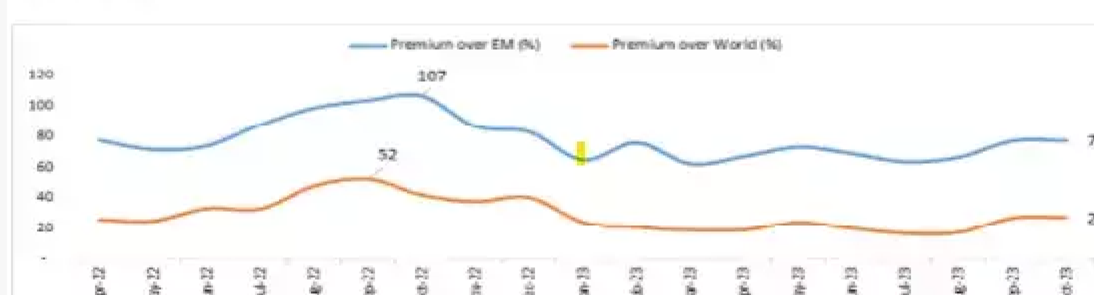


We, however, believe India's relative outperformance will continue in the medium to longer term because of the Country's strong macro environment; earnings growth trajectory; expected equity market inflows in the back drop of a slowing **World Economy** in 2024. (Source: Bloomberg, **JM Financial** research)

Index / Sector	Returns %								
	1w	1m	3m	6m	CYTD	FYTD	1Y	3Y CAGR	5Y CAGR
NASDAQ	3	9	5	12	35	16	27	6	15
MSCI World	3	7	3	4	13	6	11	4	8
MSCI EM	3	6	1	0	2	-1	4	-7	0
MSCI India	2	2	4	12	9	18	8	16	13
Barclay's Agg Bond Index	1	4	0	-1	1	-2	1	-5	1
BSE 500	1	2	5	13	13	20	12	18	14
BSE Midcaps	2	5	10	28	32	39	33	27	18
BSE Smallcaps	2	4	13	34	37	47	38	35	22

(Source: Bloomberg)



(Source: Bloomberg)

	PX_Last	Px Close 1M	Px Close 3M	Change in Bps 5 Days Change	Change in Bps 1 Month Change
US Generic Govt 10 Yr	4.39	4.91	4.34	(0.05)	(0.52)
US Generic Govt 2 Yr	4.90	5.07	5.00	0.07	(0.17)

Source: Bloomberg)

Will US slowdown in 2024?

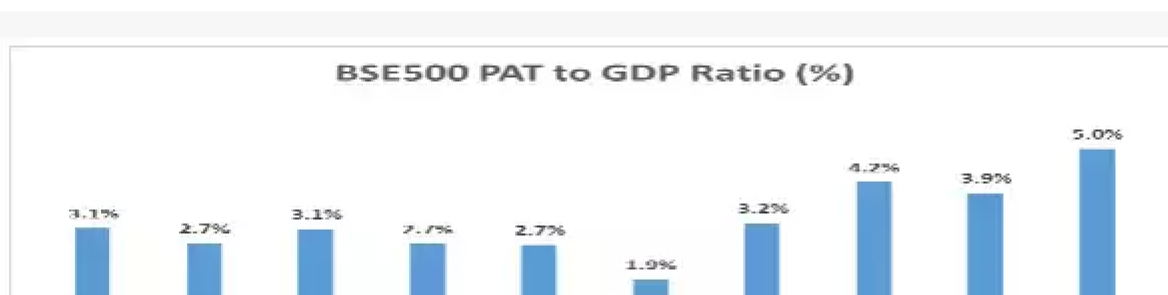
We expect the high interest rate environment prevailing world over to increase the fiscal deficits and slowdown both consumer spent and govt. spent in the next year till the overall Debt burden is addressed. US has an overall debt of 3.2x its GDP and its National Debt itself is higher than its GDP at almost US$ 33 trillion having a duration of ~6 years and approximated US$ 7.6 trillion coming up for renewal within a year. The incremental interest burden

of ~3% purely on the refinancing of Govt. debt could be a staggering US $ 200-250 billion which would add to their fiscal deficit. The US floating consumer loan rates; be it for mortgage or car loans or even education loans or credit card loans have all ballooned up 2.5-4 x times and that would be eating out of their savings and could arrest retail consumption and consumption in 2024 or force the US govt. to either print more currency or increase the Fiscal spend to make it a softer landing/slowdown. Thus, we believe till interest rates in US do not fall quickly, its aftermaths could be a global slowdown. (Source: JM Financial research)

Why should India buckle this trend? – Earnings, Earnings and Earnings

Apart from India's macro condition which is relatively stronger than the rest of the world, its earning growth trajectory is robust. In the recently concluded F2Q24 earnings season, the Country has witnessed a 40% YoY growth in earnings. Even if one were to remove the Energy space on account of its anomalies, India Inc. witnessed a Revenue/EBITDA/PAT growth of 9%, 29% and 21% YoY, and an impressive 24% 3 year CAGR in profitability. Margins expanded almost 220 bps for Non-Financials, due to fall in commodities though the top line growth was largely value lead. The growth drivers in the earnings were Broad-based including Financials, Energy, Capex centric Companies including Cement, Healthcare and the Auto sector which post COVID has virtually come back to normalcy.

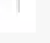
The BSE 500 Companies profit contribution to GDP has increased 2.5x from 1.9% of GDP in F2020 to almost 5% at our current run rate of H1F24. Our bottom up analysis suggests an impressive earnings growth of over 15% F2023-



(Source: Capitaline)

Technically, the inclusion of India to JPMorgan EM Bond Index and an over 10-year low FII ownership of India of 17% in the BSE 500 Companies; Highest ever SIP as well as Pension fund inflows from the domestic market suggest strong inflows round the corner, which should also help the equity markets.

(Source: Capitaline)



What are our three concerns?

Three of our biggest concerns for India are a) Exports slowing down due to Global slowdown; b) Geopolitical Risk and its impact on Crude specially and c) Elections Round the corner

The differential of the India to US 10-year interest rates has fallen from the 4.5% to 7% band last 10 years to 2.8% currently the lowest in over a decade. This could lead to a firming up of the dollar or possibly force RBI to harden interest rates in the country.