SOUTH ASIA

INDIA – 3.5 STARS (ATTRACTIVE)

- India's exports recorded growth of 10.29% YoY in August 17
- India's Consumer Price Index (CPI) for the month of August 17 came in higher at 3.36%
- IIP recovered to 1.2% in July 17 after a contraction of -0.1% in June 17.
- India's Wholesale Price Index (WPI) rose to 3.24% in August 17 from 1.88% in July 17.
- Consensus estimates for earnings growth for FY19 and FY20 are 24.52% and 14.60% respectively. (As of 25 September 2017).

MARKET OUTLOOK

In continuation with the positive growth exhibited by exports for the last twelve months, exports during August 2017 have shown growth of 10.29% in dollar terms valued at USD 23.81 billion as compared to USD 21.59 billion during August, 2016. Imports during August 2017 were valued at USD 35.46 billion which was 21.02% higher in Dollar terms over the level of imports valued at USD 29.30 billion in August, 2016. The merchandise trade deficit for August 2017 stood at USD 11.64 billion higher than USD 7.70 billion in August 2016. Taking merchandise and services together, overall trade deficit for April-August 2017-18 is estimated at USD 39.87 billion as compared to USD 12.72 billion during April-August 2016-17.

CPI for the month of August 2017 came in higher at 3.36% year-on-year against expectations of a 3.24% increase and 2.36% in the month of July 2017. The rise in CPI was led by rise in prices of food and beverages (1.96%), housing (5.58%), fuel and light (4.94%) and miscellaneous goods and services (3.85%). Within the food and beverages segment which has a weightage of 45% in the CPI basket, Vegetable prices rose by 6.16%, Fruits 5.29%, Milk Products 3.58% and Cereals 3.87% thus driving food inflation higher. Within the miscellaneous goods and services segment which has a weightage of 28% in the CPI basket, Transport and Communication prices increased by 3.71%, Healthcare prices rose by 4.33% and prices of household goods and services rose by 4.24%. Factors like HRA benefits to central government employees, and farm loan wavers by state governments pose upside risks to CPI thereby reducing the possibility of a policy rate cut in the October MPC meet.

India's Wholesale Price Index (WPI) rose to 3.24% in August 2017 from 1.88% in July 2017. The index for manufactured products rose by 0.20%. WPI Food Index increased from 2.12% in July, 2017 to 4.41% in August, 2017. The index for primary articles rose by 1.9%. The index for fuel and power rose by 0.90%.

IIP recovered to 1.2% in July 2017 after a contraction of -0.1% in June 2017. Eight out of twenty three industries have shown positive growth in the month of July 2017. The industry group 'other manufacturing' has recorded the highest positive growth of 20.9% during the month followed by manufacture of pharmaceuticals, medicinal chemicals and botanical products (18.9%) and manufacture of other transport equipment (10.5%). The sectors recording the highest negative growth rates during the month include manufacture of tobacco products (-43.4%), manufacture of electrical equipment (-11.1) and printing and reproduction of recorded media (-8.8%). On a use base classification, manufacture of primary goods increased by 2.3% while capital goods production declined by 1% and Intermediate goods production declined by 1.8%. Infrastructure/construction goods manufacture increased by 3.7%. Production of consumer durables declined by 1.3% while consumer non durables production increased by 3.4%. As the economy adapts to the new tax regime and as the demand for manufactured goods recovers, consequently, industrial production will likely improve going forward.

As of 25 September 2017 the benchmark SENSEX index stood at 31,626.63. The earnings estimates for HDFC Bank, the highest weighted stock in the index stood at 18.55% and 18.13% for FY19 and FY20 respectively. Housing Development Finance Corporation, the second highest weighted stock in the index has earnings estimates of 16.09% and 13.81% for FY19 and FY20 respectively. The top performers in the index during the month were Dr Reddy's Laboratories Ltd (16%), Bajaj Auto (11%) and Coal India Ltd (7%) while the top losing stocks included Bharti Airtel (-10%), followed by Mahindra and Mahindra Ltd (-8%) and State Bank of India (-8%).

According to consensus estimates, as of 25 September 2017, the estimated PE ratios for India's SENSEX Index are 20.81X, 16.71X and 14.58X for FY18, FY19 and FY20 respectively. Estimated earnings growth numbers are 12.97%, 24.52% and 14.60% for FY18, FY19 and FY20 respectively. **We maintain a 3.5 stars "Attractive" for the Indian equity market.**

RECOMMENDED FUND:
FIRST STATE REGIONAL INDIA FUND

India (3.5 STARS- ATTRACTIVE)

Why we like it

1. Reform Measures of the Government
    - The government is committed to improving business conditions in the country. India was ranked 140 out of 190 countries in the Ease of Doing Business Index in December 2014 and currently ranks 130.
    - The Pradhan Mantri Jan Dhan Yojna was a successful mass financial inclusion program of the government which was aimed at opening bank accounts for the unbanked population and making them part of the mainstream economy. The government has also implemented the Insolvency and Bankruptcy Code, which makes it easier for creditors to restructure defaulting loan accounts or recover their dues through liquidation of assets of the defaulters.
    - The government is investing heavily in the infrastructure space to improve road and rail connectivity in the country.
    - The GST implementation is expected to widen the tax base in the country by bringing the unorganized and informal segments of the economy into the mainstream economy.
    - Demonetization of higher denomination currency in November 2016 paved the way for a transition towards a cash-less economy and increased transparency in financial transactions.

2. Attractive Valuations
    - According to consensus estimates as on 25 September 2017 the PE ratios for India's equity market (S&P BSE Sensex) are 20.81X, 16.71X and 14.58X for FY18, FY19 and FY20 respectively. Estimated Earnings growth numbers are 12.97%, 24.52% and 14.60% for FY18, FY19 and FY20, respectively.

What we don't like

1. Rising Non Performing Assets (NPA) In The Banking System
    - Gross NPAs of Scheduled Commercial Banks as a percentage of Gross Advances stood at 7.5% in March 2016 compared to 2.5% in March 2007. The Reserve Bank of India has implemented various measures towards monitoring and reducing the bad loans in the banking system but a complete resolution to the problem does not seem visible in the near future.

2. Global Concerns Resulting In FII Outflows
    - The Fed's decision to commence its Balance Sheet Reduction in October. In addition, there is a possibility of another rate hike by December 2017 and Trump's administration improving growth prospects of the US economy. The above is expected to result in appreciation of the US Dollar and prompt a sell off by FIIs from emerging markets including India.
    - Geo-political tensions between North Korea and U.S pose a major concern for emerging markets including India as escalation of tensions can result in FIIs reducing their holdings in emerging markets to be channelized into safe heaven assets.