# NETRA

# Early Warning & Signals Through Charts

MAY 2022

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# Indian Economy Is Recovering: Exports, Taxes Improving

While the world worries about growth amidst macro headwinds, Indian economy is resilient

# India's Growth Is On a Strong Footing!

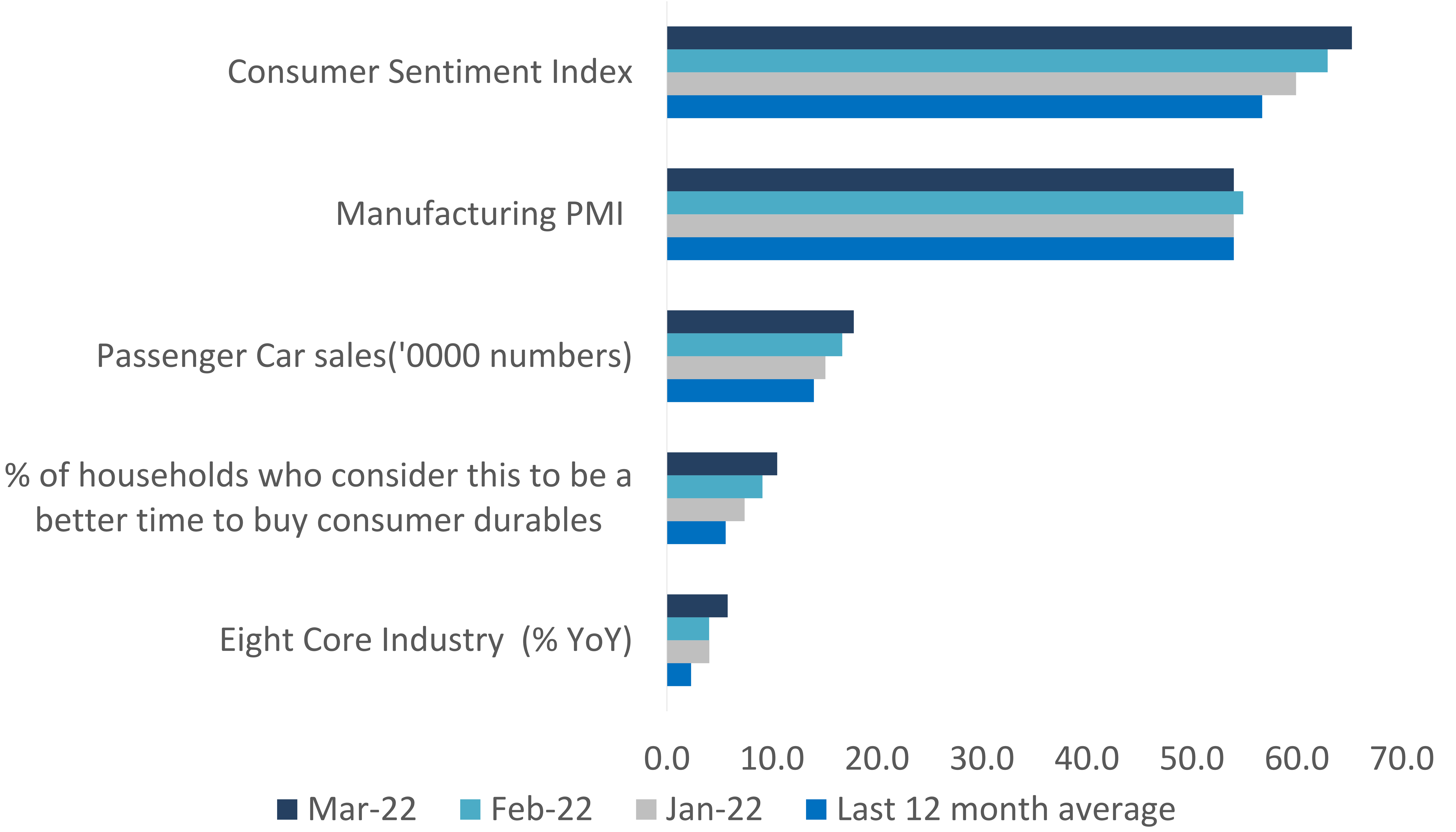
India's recovery has been rickety but resilient. Post-covid domestic recovery was not highly dependent on fiscal & monetary expansion. Therefore, unlike developed economies, damage from withdrawal of policy support is limited.

While the developed world seems to be entering another round of slowdown, most domestic high frequency indicators have shown strength. Credit growth is picking up & remains a strong indicator of sustained recovery

**Amongst the EM basket, India has the biggest opportunity size, given the strong fundamentals.**

There are some headwinds, but gradually India is finding its own economic rhythm and is de-linking from US economic cycle.

***Most domestic economic indicators are on a strong footing, with March numbers continuing to show resilience despite global slowdown***

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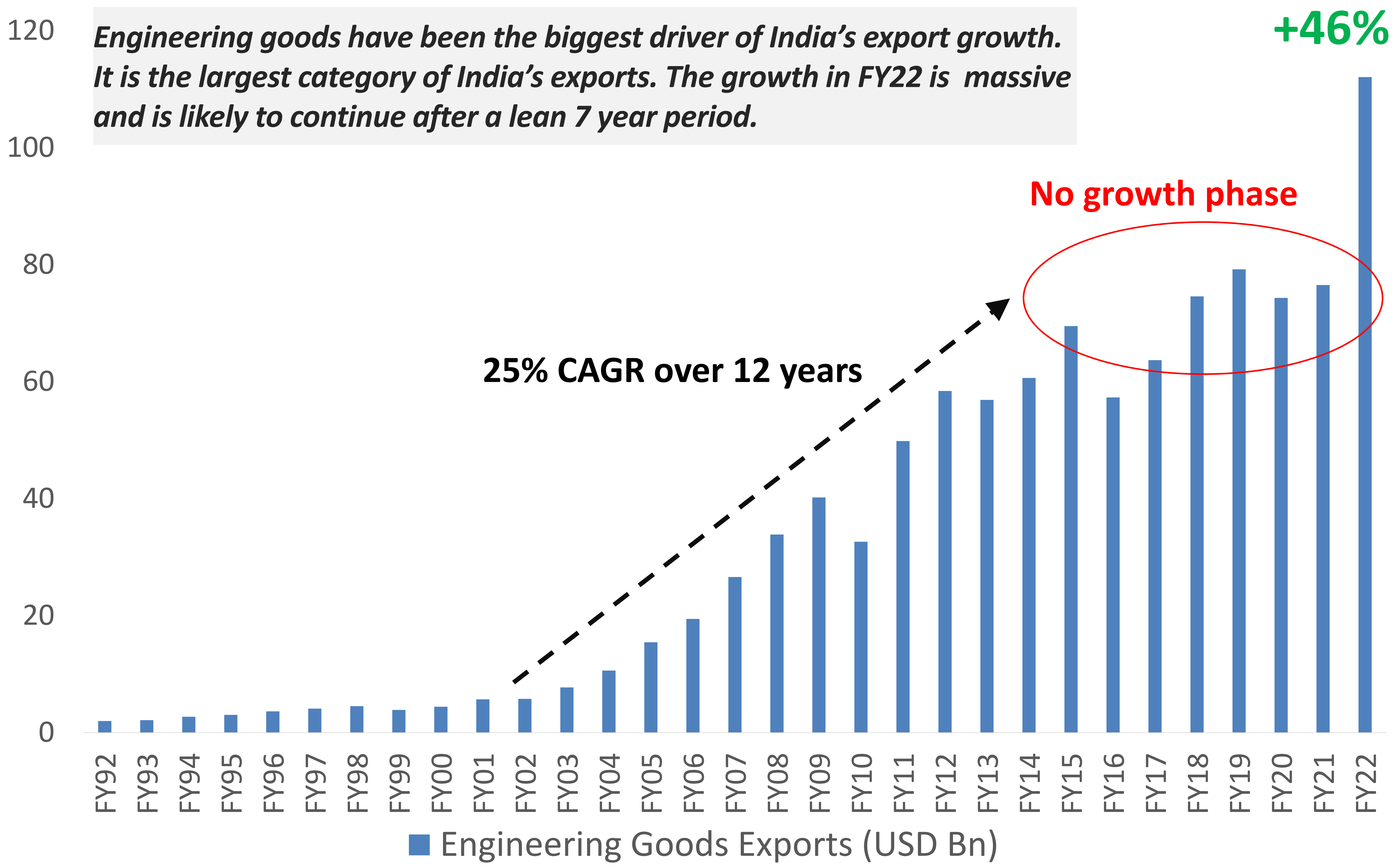
Source: CMIE, Data as on 30th April 2022

# India’s Engineering Goods Exports Top $112bn in FY22

Indian engineering goods exports comprise mainly of auto parts’ components & automobile exports. Due to exceptional price rise & strong demand trends globally, India’s engineering goods industry has reaped immense benefits.

Over time, this is the category in which export growth has been key. This sector is the one where India is developing size, scale & already has expertise.

This trend in export growth is positive for auto ancillary & the automobile sector in general.

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Source: CMIE, Data As On April 2022

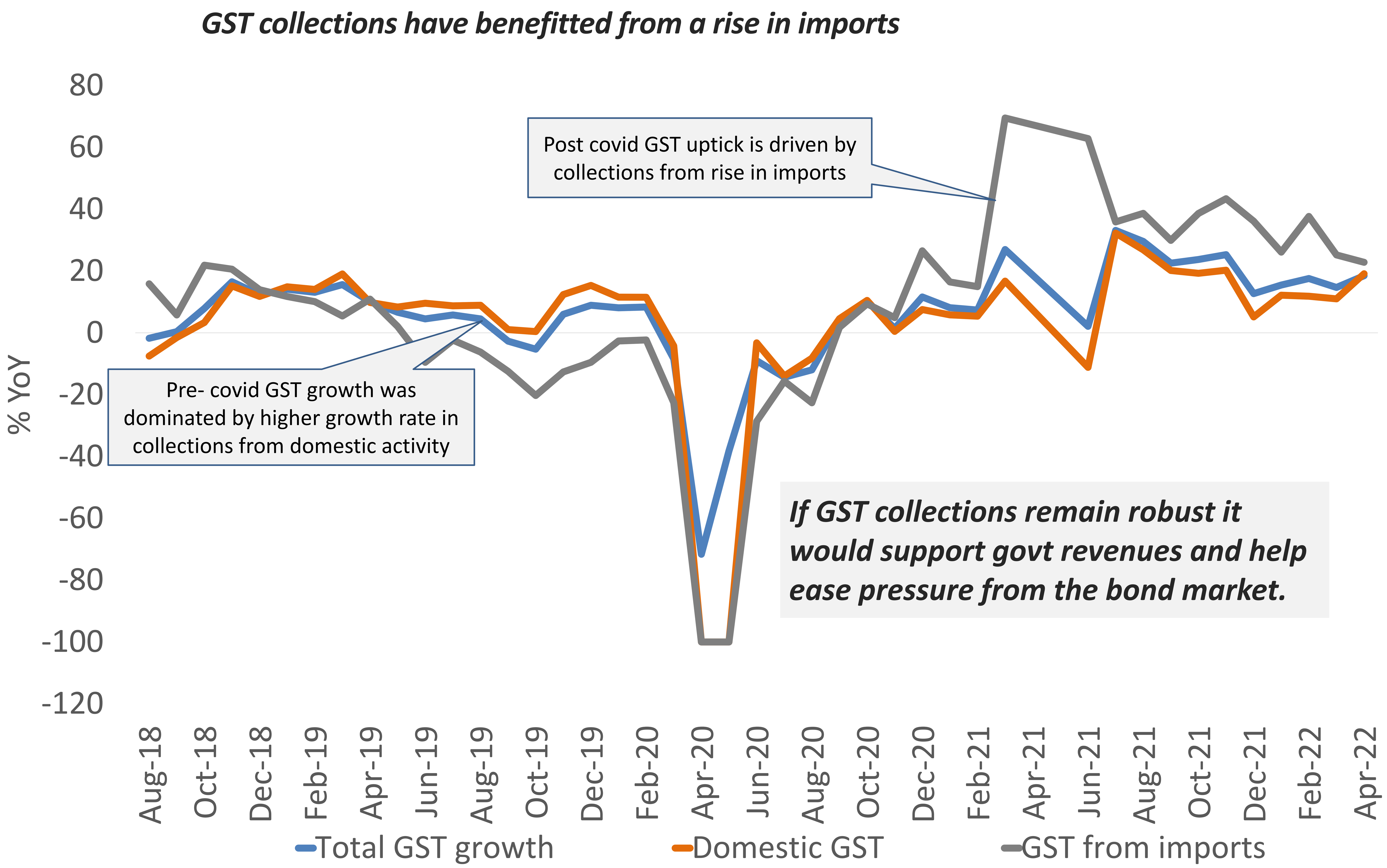
# GST Collections Robust: Additional Benefits From Rise In Imports

GST collections shot up to INR 1.68 trillion in April, 2022, were a good sign & remain a function of the year end phenomenon, better compliance & inflation.

GST collections have two components, one that is dependent on domestic activity & the other that benefits from imports.

**Post covid, GST collections from imports related activity is clocking a higher growth** as shooting up of global commodity prices increased the import bill.

GST collections can structurally improve, helping the fiscal math further. However, we take note of higher than budgeted subsidies & do not think that borrowing numbers are likely to be affected. If GST collections remain robust it would support govt revenues & help ease pressure from the bond market.

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Source: CMIE, Data as on 30th April 2022

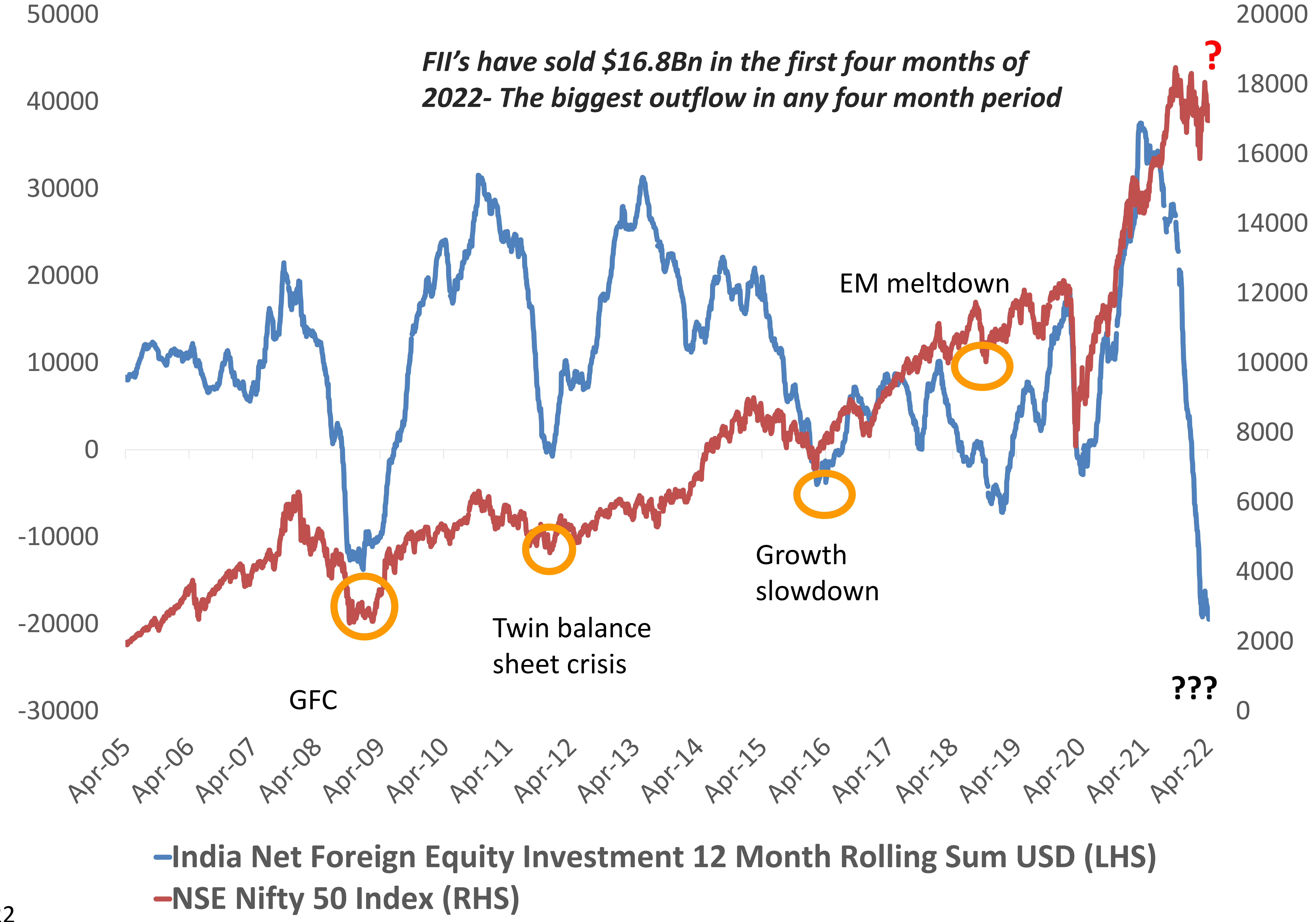
# Best Time To Buy Indian Stocks? Are We There Yet?

Every time Indian stocks witness large FII outflows, the causes some dislocation in valuations and ownership trends.

In the past, large FII outflows have coincided with deep cuts for Indian stocks and bear markets. This was because local ownership of equities was small. Over time domestic institutional & Indian households have increased their equity holdings providing a cushion on markets.

At this time the rolling 12 month FII flows are the most negative on record. FIIs have sold stocks worth $17bn in the first 4 months of 2022, a record in itself. History says when FII outflows rise to such levels, it's usually a good time to buy Indian stocks.

**Positive for Indian equities.**

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Source: Bloomberg, Data as on April 2022

# Global Growth Is Slowing As Monetary Policy Tightens, Threatening Commodity Prices

But inflation up surge may stall, offering some respite

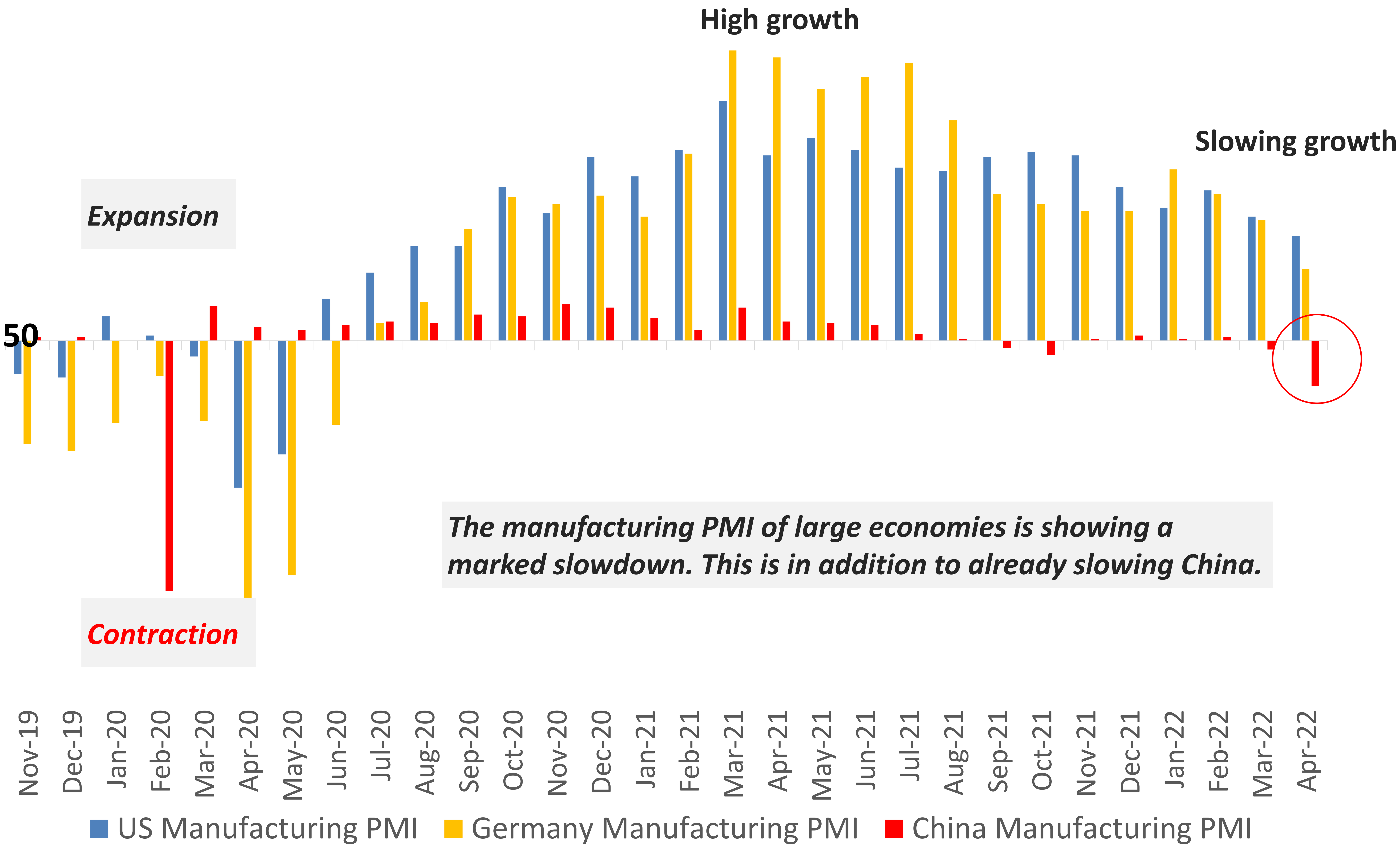
# Growth Is Slowing Down In The Developed World

With rising interest rates, removal of all government funded stimulus & end of the 'pent-up' demand in developed economies, the growth is slowing.

The graph on the right shows how manufacturing PMIs have slowed in US & Germany. This has coincided with Chinese manufacturing activity registering de-growth.

This can have a severe impact on some markets. Particularly, commodity markets which are dependent on huge demand from developed economies & China could see demand shocks.

This is negative for commodity prices.

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Source: Bloomberg; Data as on April 2022

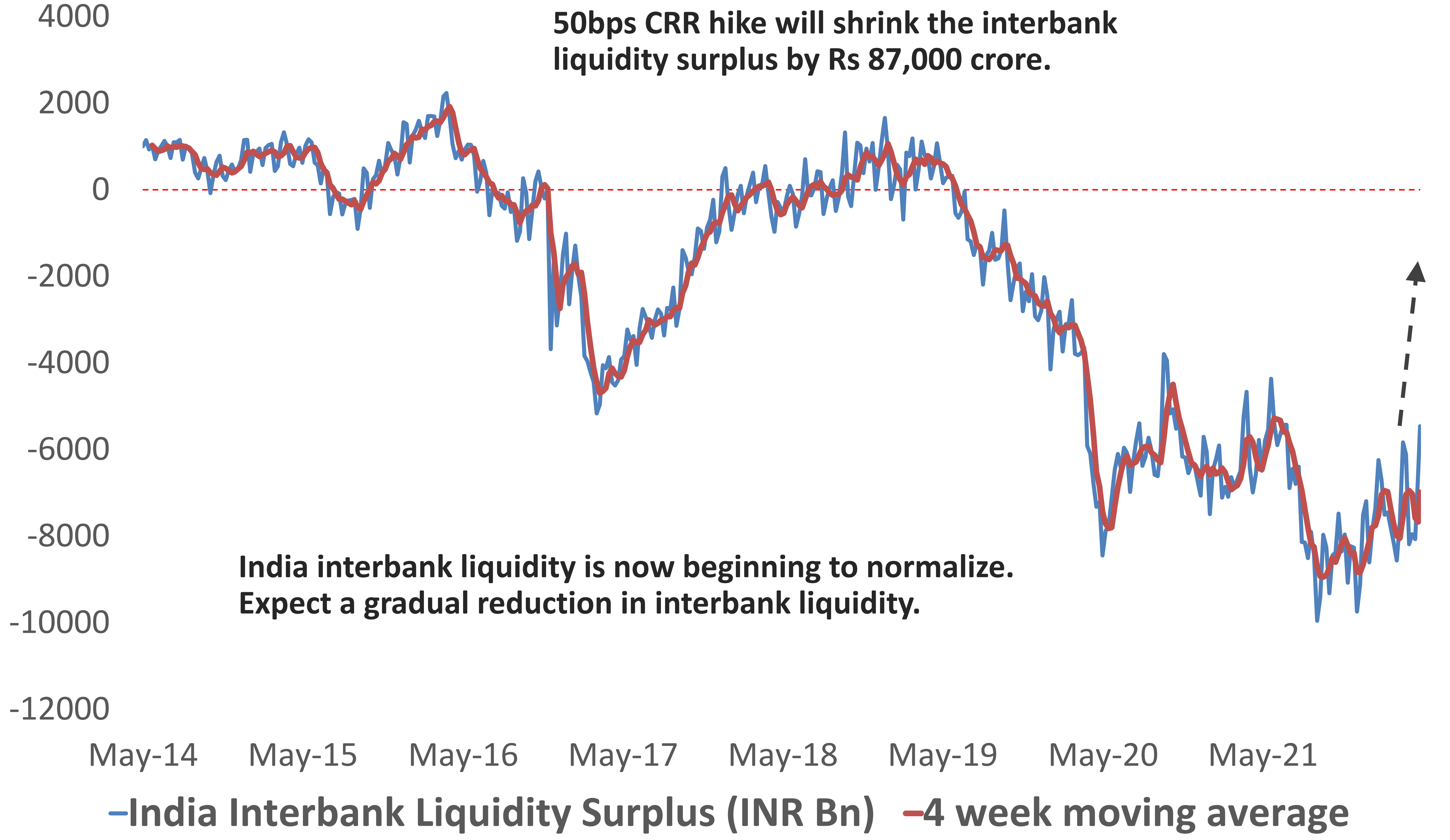
# Policy Headwinds – India Interbank Liquidity

Interbank markets are among the most important in the financial system. They allow liquidity to be readily transferred from banks with a surplus to banks with a deficit. This helps in smooth functioning of banks and financial stability to be maintained.

High levels of interbank liquidity surplus cause short term rates to remain low. This can nudge banks to keep their cost of lending lower across tenors.

RBI raised CRR by 50bps which will shrink the liquidity surplus by 87,000 crores. Markets have been anticipating this since Oct'21 but this normalization is now taking hold.

**Impact: Ultra lose monetary policy is giving way to a neutral policy environment. This will keep short term rates higher.**

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Source: Bloomberg on 30th April 2022

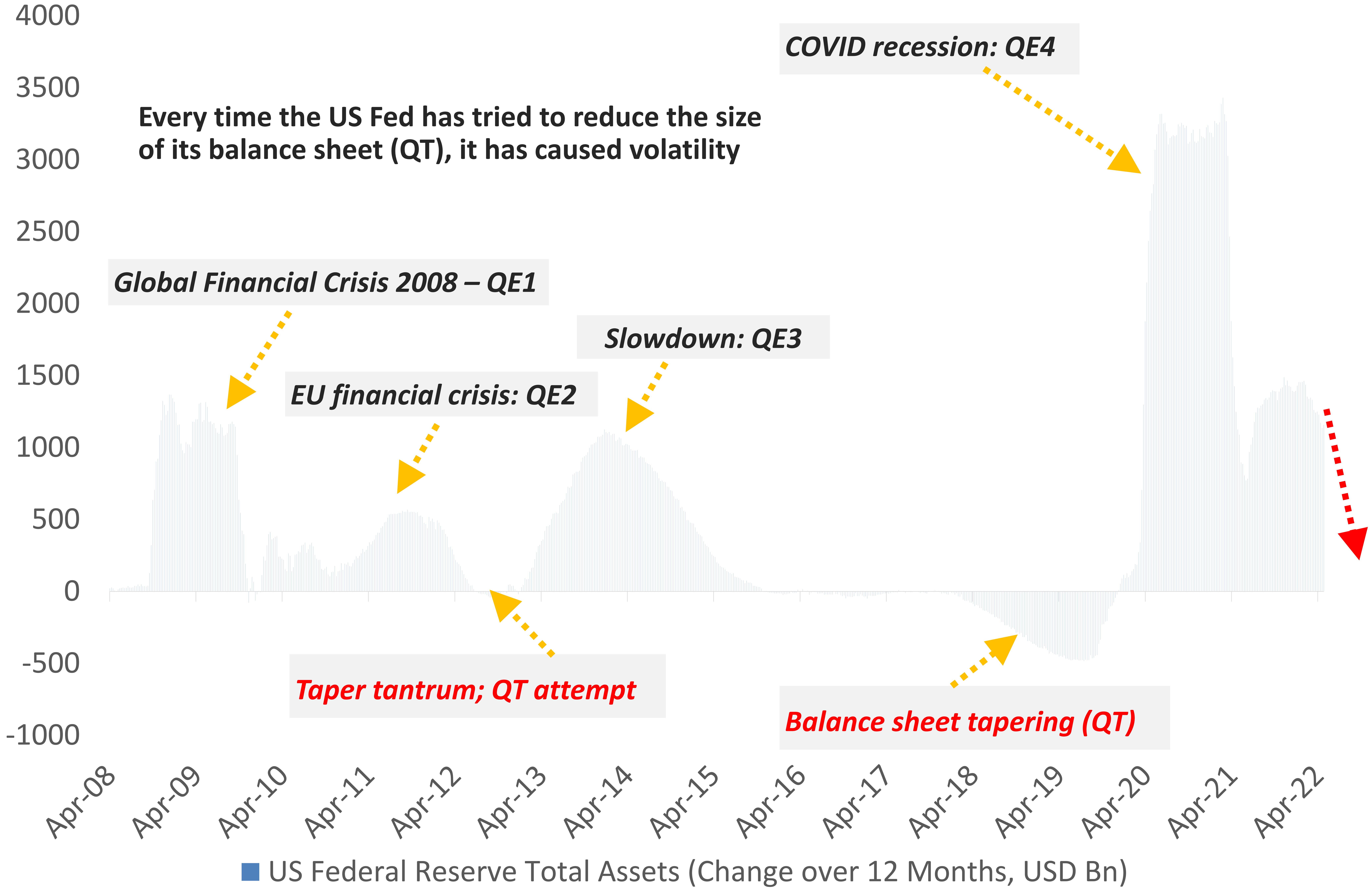
# Policy Headwinds – US Federal Reserve Unwind

Every time the US Federal Reserve has tried to wean off the market from an ultra loose monetary policy it has caused either an economic slowdown or a disruption in the financial markets.

Over the last decade, attempts by US Fed to remove monetary policy stimulus have almost always led to a growth slowdown.

The US Fed & most other central banks, with an exception of a few are steadily moving towards removal of all extraordinary stimulus provided during COVID.

This is making other markets volatile. Equity markets especially are witnessing steady compression in P/E multiples. Till the time Fed remains on tightening cycle, markets are likely to remain jittery.




Source: St Louis Fed, April 2022

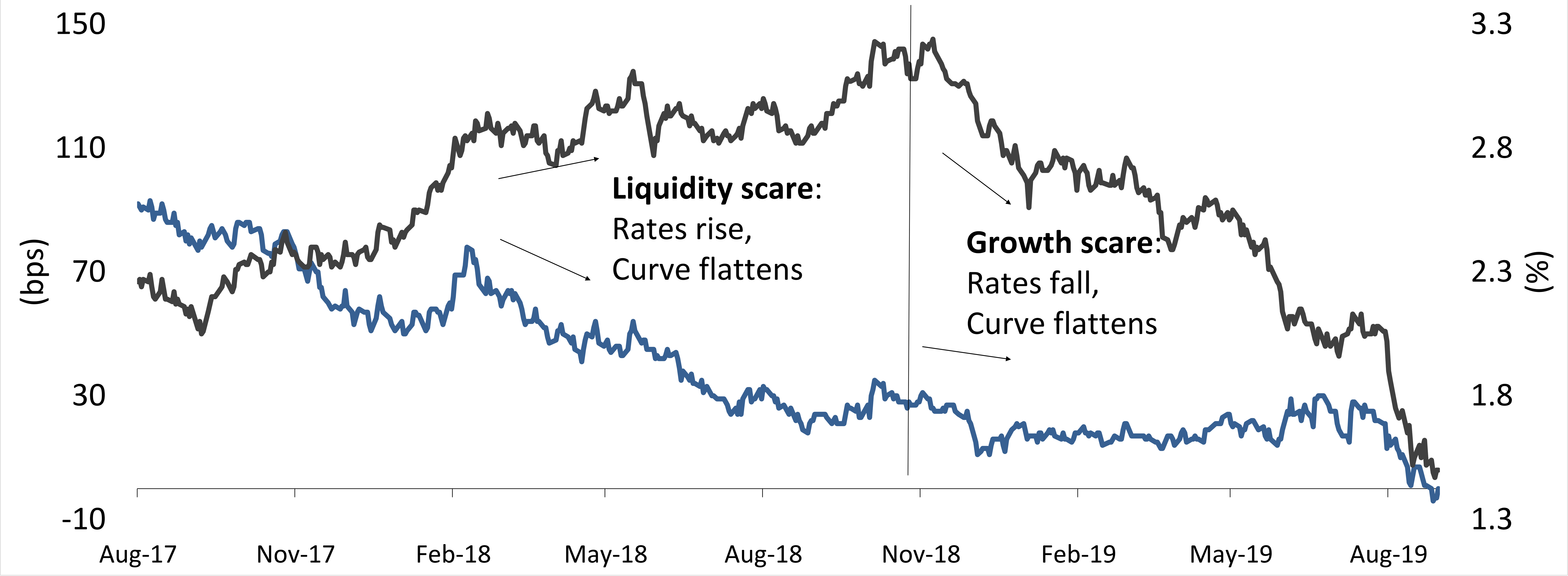
# Policy Headwinds – Rising Rates Can Cause A Growth Slowdown

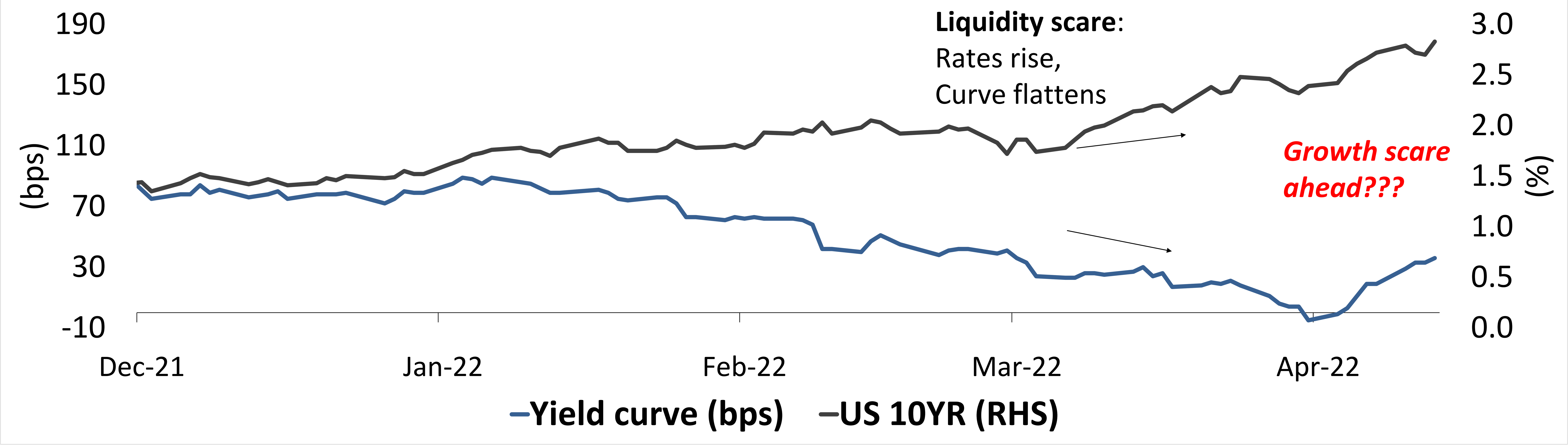
Past episodes of US Fed balance sheet unwind were met with rising rates. This occurred due to reduction in liquidity and was then followed by a growth slowdown.

This eventually forced the US Fed to abandon tightening and take a U-turn to again implement quantitative easing, even before COVID struck.

This time a similar market pattern is repeating. US interest rates are rising in anticipation of tighter policy and potential QT.

**We reckon that this is already slowing growth in US & may push the US central banks to abandon tightening much earlier than market perceives today.**

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Source: Bloomberg, Edelweiss Research April 2022

# Can Inflation Sustain In Face of Slowing Growth?

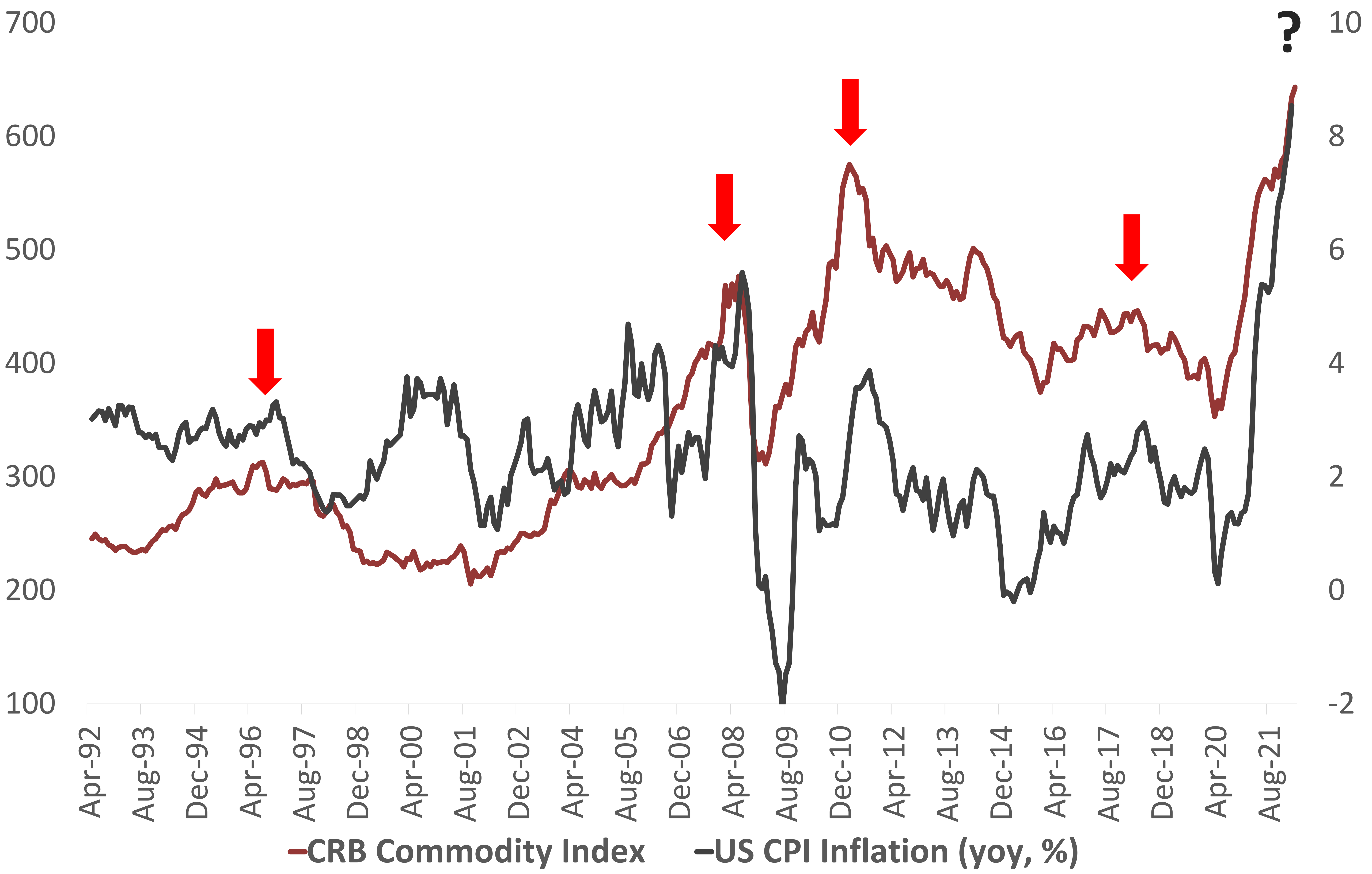
Inflation rhymes with commodity prices. More so in emerging markets where consumption basket is dominated by food & fuel.

In US, the consumer price inflation broadly moves with high volatile commodity prices. In fact due to the current supply side issues in Crude Oil, wheat, corn and Aluminum the consumer price inflation has accelerated to a 40 year high in US.

But can a combination of easing of supply side issues, slowing growth and thus weaker demand cause inflation to cool down?

Expect global inflation to cool off in next few quarters if this trend plays out!

This means – Interest rates could soften. Time to take advantage of higher yields.

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Source: Bloomberg; Data as on April 2022

# Commodity Prices Are Cyclical: Gains Are Followed By Losses

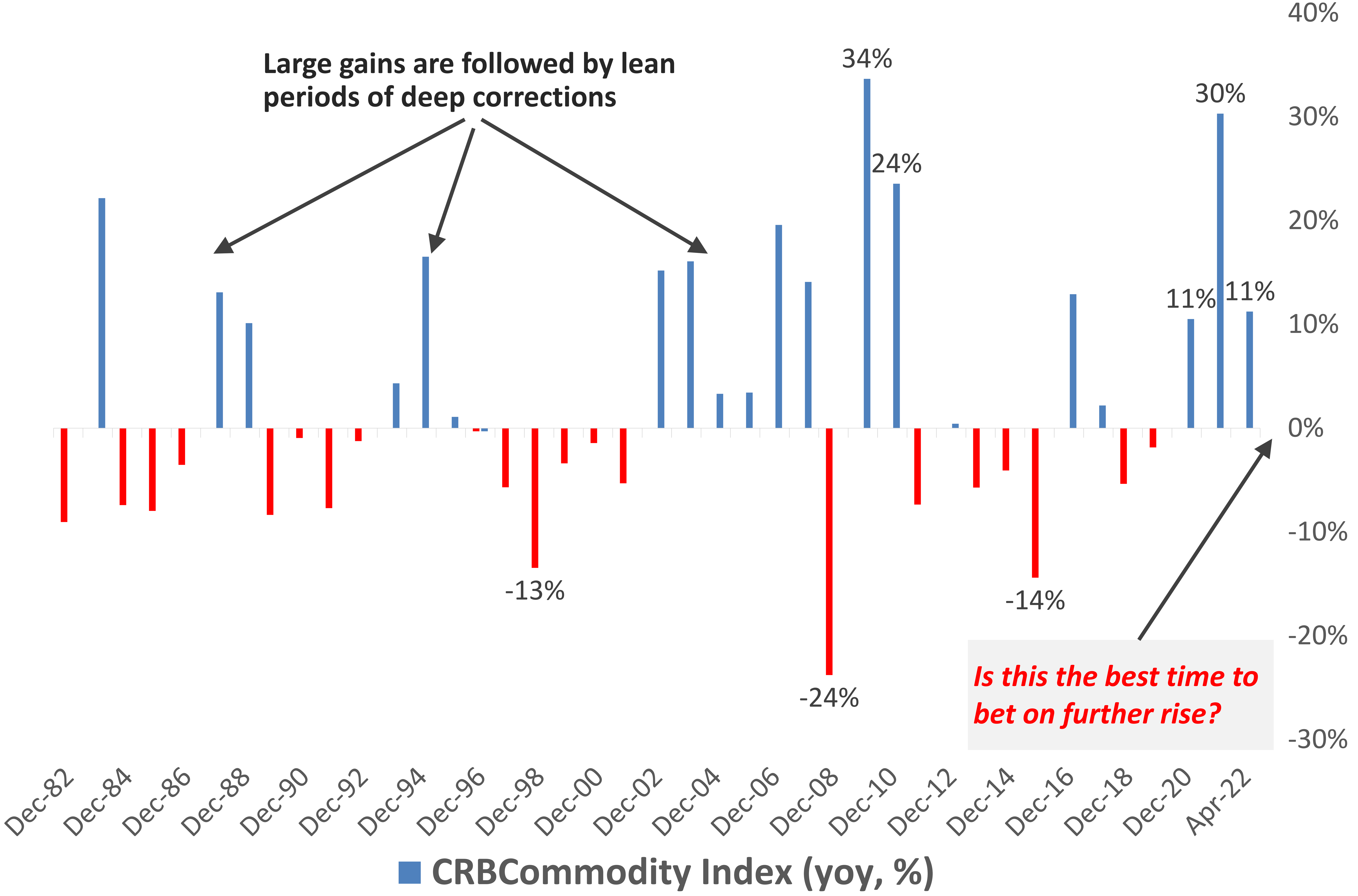
CRB commodity index has climbed to a lifetime high with a cumulative gain of more than 80% since the COVID bottom in 2020.

Commodity prices are highly cyclical. Higher prices attract higher supply & eventfully prices cool off.

Recently we have seen three major headwinds for commodities – slowing growth in large economies, shift in commodity futures curve from backwardation to contango & nascent signs of supply side issues easing.

This begs the question – Is this the best time to bet on a further rise in commodity prices?

If not, then commodity users like India are likely to benefit.

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Source: Bloomberg, Data as on April 2022

# No Straight Lines

The most beautiful destinations are not reached in a straight line. For the ones with a calm mind, the journey itself is the destination.

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