Capital League outlook

Oct, 2019

Indian Economy

- Government announced cut in the base corporate tax rate from 30% to 22% effective April 1, 2019 for companies which are not availing exemptions. It also reduced base tax rate to 15% for manufacturing companies incorporated after October 1, 2019 and which commence production before March 31, 2023. Minimum Alternate Tax (MAT) will also not be applicable on such companies.
- Government estimates that these tax cuts are likely to result in gross revenue loss of INR 1.45 Lac Cr for FY20, but with Indian tax rate now competitive with other countries like Vietnam, Singapore, China etc., it can act as a big catalyst to attract fresh investments from foreign and domestic players.
- The government raised INR 4,368 Crs through the fourth tranche of the Bharat-22 exchange traded fund to meet its disinvestment targets.
- Dearness allowance for central government employees has been hiked by the government by 5% benefitting over 1 Cr government employees and pensioners which may boost consumption.
- Index of Industrial Production (IIP) contracted by 1.1% Y-o-Y in Aug’19 due to a sharp decline in production of capital goods and consumer durables.
- The growth in gross revenue remains low at 4.2% with direct tax collections growing at 9.6% and Indirect tax collections growing by 0.7% only. With corporate tax rate cut, direct tax collections might moderate further thus raising the concern of fiscal slippage.
- Indian equity markets saw improved sentiment and registered gain after the announcement of reduction in the corporate tax rate. It also resulted in positive FII flows in Indian markets.
- While FIIs bought net Indian equities worth USD 1.04 Bn in Sep'19 after being net sellers for Jul and Aug’19. DIIs invested USD 1.8 Bn in equities in Sep'19.
- The CPI inflation rate rose to a 14-month high of 3.99% in Sep’19 as food inflation jumped to 21 month high.
- India’s current account deficit (CAD) stood at USD 14.3 Bn (2.0% of GDP) during Q1 FY20 as compared to USD 15.8 Bn (2.3% of GDP) during Q1 FY19 due to stable net oil imports and improvement in net exports services.
- RBI lowered rates by 25 bps to 5.15% in its Oct’19 meeting and maintained accommodative stance as inflation is expected to be within the target range.
- RBI also revised GDP growth forecast to 6.6%-7.2% for H2FY20 as against earlier estimates 7.3-7.5% in H2 FY20. It acknowledged that economic activities in both global and domestic economy are slowing.

Global Economy

- The International Monetary Fund (IMF) World Economic Outlook revised its global growth forecast from 3.2% to 3.0% in 2019 citing a synchronized slowdown and uncertain recovery.
- Crude Oil prices remained range bound due to global economic slowdown and the uncertainty over US-China trade talks.
- The European Union and Britain are trying to finalize the Brexit deal before 31st Oct'19 deadline.

Outlook

- While corporate tax rate cut doesn't directly address the near-term demand weakness, it has provided a sentiment boost which is an important step towards reviving investment cycle.
- Indian equity markets continue to show volatility. However, valuations are still favorable versus historical averages across several metrics such as relative to other EMs, earnings-bond yield gap, market cap to GDP, and in the mid & small cap segment.
- Investors are recommended to maintain their asset allocation and to continue staggered investments in equities.
- RBI policy stance provided guidance with respect to maintaining an accommodative policy stance as long as necessary to revive growth.
- On the fixed income side, investment in short term funds, tax free bonds and fixed deposits are recommended based on the tax slab of the investor.