MONTHLY NEWSLETTER – OCTOBER 2015

I-CAN FINANCIAL SOLUTIONS

MARKET UPDATE

Sensex : Down 0.49% Nifty : Down 0.28%	
Best performing sector: Real Estate (10.78%)	Worst performing sector: Metal (-8.22%)
Best performing Global index: South Korea Seoul Composite (1.10%)	Worst performing Global index: Japan Nikkei 225 (-7.95%)
Indian Rupee: 1.27%	Gold price: -1.88%

The headline equity indices fell in the month of September. FIIs were net sellers. The net outflow was Rs. 3,376.96 crore from equity markets and the net inflow in debt markets was Rs. 66.26 crore.

The month of September ended on a cheerful note in India as RBI Governor Raghuram Rajan reduced the repo rate, at which the central bank lends to commercial banks, to 6.75% from 7.25% in the fourth cut since the start of January. The repo rate has been cut by a total of 125 basis points this year. RBI will maintain an accommodative stance, but the focus of monetary action for the near term will shift to working with the Government to ensure that impediments to banks passing on the bulk of the cumulative 125 basis points cut in the policy rate are removed. This was a necessary move as we see there is a slowdown in the growth engine and inflation has been under control. The WPI inflation for August was -4.95% while CPI inflation was 3.66%. Asian Development Bank cut India's growth projection to 7.4% for 2015-16 from 7.8% predicted earlier. Even the RBI has reduced its growth forecast from 7.6% to 7.4%.

Another highlight of the month was PM Narendra Modi's visit to the United States. The PM held meetings with key US business leaders, seeking and enlisting their support for his "Make in India" and "Digital India" campaigns. He set an ambitious target for India to become a $20-trillion economy with increased focus on agriculture, manufacturing and services. He reiterated the ambitious plan of providing optic-fibre connectivity to 600,000 villages in five years that could help the country witness growth. Top American chief executive officers (CEOs) have sought "additional steps" to hasten economic reforms in India. One of the reports states that India received $19.78 billion (Rs 1.3 lakh crore) in FDI in 2014-15 from major FDI source countries that Modi has visited since his election. This accounts for two-thirds of the $30.93 billion FDI the country received in the fiscal year, which was 27 per cent more than the year before.

Widespread rains in mid-September reduced the monsoon deficit to 14% from 16%. Merchandise exports plunged 21% to $21.3 billion in August from $26.8 billion in the year-ago period, the ninth consecutive monthly decline and the steepest in the first five months of this fiscal year. India has climbed an impressive 16 places to the 55th position among 140 economies in this year's World Economic Forum (WEF) Global Competitiveness Index, after five years of decline.

Important measures announced by RBI:

- RBI is proposing to reduce the risk weights applicable to lower value but well collateralised individual housing loans with a view to improving "affordability of low cost housing".
- Indian corporates will be allowed to issue rupee denominated bonds with a minimum maturity of 5 years at overseas locations within the ceiling of foreign investment permitted in corporate debt (US$ 51 billion at present).
- Increase in the limits of Foreign Portfolio Investors (FPI) in central government securities to 5% of the outstanding stock by March 2018.
- The limits for FPI investment in debt securities will now be announced/ fixed in rupee terms.

On 17th September, the US Federal Reserve left interest rates unchanged due to worries about the global economy, financial market volatility and low inflation at home. It left open the possibility of modest rate rises later this year.

Global auto stocks were hit after revelations of cheating by Volkswagen in emission tests by using software to hide the true extent of diesel pollution.

Overall, 2015 is turning out to be a bad year for global markets as commodities, stocks and bonds are all in the red. Deutsche Bank cut its December 2015 Sensex target to 28,000 from 31,000 earlier on concerns over global growth.

Motor Insurance

Motor Insurance is insurance purchased for cars, trucks, motorcycles, and other road vehicles. Its primary use is to provide financial protection against physical damage and/or bodily injury resulting from traffic collisions and against liability that could also arise.

Car Insurance or motor insurance covers for losses that you might incur if your car gets damaged or stolen. The premium amount of your car insurance is decided on the basis of Insured Declared Value or IDV of the vehicle. If you increase the IDV, the premium rises and if you lower it, the premium reduces.

There are different types of Motor Insurance in India:

- Private Car Insurance
- Two Wheeler Insurance
- Commercial Vehicle Insurance

Key Benefits of Car Insurance

Car insurance plan offers following benefits:

- Coverage against loss or damage to the insured vehicle.
- Coverage against loss or damage to your vehicle caused by accident, theft, fire, explosion, self-ignition, lightning, riots, strikes or act of terrorism, natural calamities.
- Coverage against financial liability caused by injury/death of a third party or damage to the property.
- Personal accident cover.

Coverage under Car Insurance

There are primarily 3 types of car insurance:

- **Third Party Liability Coverage -** Third Party car insurance provides cover against any legal liability to a third party caused when you are at-fault driver. It covers damage/injury caused by you to another person/property. A Third Party Liability cover is legally mandatory in India under the Motor Vehicles Act.

- **Collision Coverage -** Collision coverage protects the insured financially against damage of their own car. It pays the insured for damage caused by collision which is usually an accident. Damage or loss due to theft or vandalism is not included in collision coverage.

- **Comprehensive Coverage -** A comprehensive coverage is extensive and includes damage of car, theft of vehicle, third party legal liability and personal accident cover. The policy coverage can be further extended by opting for add-ons like accessories cover, engine protector, zero depreciation cover, medical expenses, etc. This type of coverage is the most popular as it offers end-to-end coverage and thus less stress for the policyholder.

No Claim Bonus

For every claim free year, the insured is rewarded with discount on the renewal premium. This discount is called - No Claim Bonus (NCB). It is cumulative and increases every year. It usually ranges from 10% to 50% and can save a substantial amount of money on your premium.

What is not covered in Car Insurance?

Following features are usually not covered in car insurance:

- Loss or damage if a policy is not in force.
- Gradual wear and tear of car and its parts.
- Loss or damage to vehicle when driven by person without a valid driving license.
- Loss or damage to vehicle as a result of intoxication due to drugs, alcohol etc.
- Loss or damage to engine as a result of oil leakage.
- Loss or damage to vehicle as a result of abuse of car manufacturer's guidelines.

Tax Free Bonds

Bonds are a kind of debt instrument. By investing in this type of asset, the investor gives a loan to the issuing entity. The investors will be repaid at the end of the tenure. These bonds are mostly issued by government enterprises and pay a fixed coupon rate (interest rate). As the proceeds from the bonds are invested in infrastructure projects, they have a long-term maturity of typically 10, 15 or 20 years.

There are different kinds of bonds. Those bonds which are exempt from taxation on the interest income under the Income Tax Act, 1961 are called tax-free bonds. These are usually issued by government-backed entities.

In India there are two types of bonds through which the tax liability of a person can be reduced:

1. Tax Free Bonds
2. Capital Gain Bonds

Tax Free Bonds: Tax Free Bonds are the bonds on which the interest received is fully exempted from tax under Section 10. However, the principal amount invested in these bonds cannot be claimed as a deduction from total income of the bondholder for purpose of payment of income tax.

Capital Gain Bonds: Capital Gain Bonds are the bonds on which the interest received is not exempted, however the amount that is invested in these bonds can be claimed as an exemption from Capital Gains under Section 54EC.

Features of the tax-free bonds:

1. **Tax benefits:** The income by way of interest on tax-free bonds is fully exempted from income tax. The interest earned from these bonds does not form part of your total income. There is no deduction of tax at source (TDS) from the interest, which accrues to the bondholders. But remember that no tax deduction will be available for the invested amount.
2. **Interest rate:** The coupon (interest) rates of tax-free bonds are linked to the prevailing rates of government securities. So these bonds become attractive when the interest rates in the financial system are high.
3. **Interest payment:** The interest on these bonds is paid annually and credited directly in the bank account of the investor.
4. **Tax free bonds vs bank fixed deposits (FDs):** The interest earned on bank FDs and other normal bonds are added to the income of the investor and taxed as per the income-tax slabs. As interest earned

from tax-free bonds are not taxed, investors in higher tax brackets mostly earn a better post-tax return than from FDs. But remember, the bank FDs score over tax-free bonds in terms of liquidity as these bonds have a longer maturity tenure.

5. **Credit risk:** Since tax-free bonds are mostly issued by government-backed companies, the credit risk or risk of non-repayment is very low.
6. **Liquidity:** The tax-free bonds get listed and then traded on the stock exchange(s) to offer an exit route to investors. But these bonds might not enjoy high liquidity as they are long-term in nature.
7. **Do you need a demat account?** The bonds could be issued both in demat and physical mode.
8. **Secondary market:** Investors can buy and sell these tax free bonds on the stock exchanges. Though the interest earned on these bonds is tax-free, any capital gain from sale in the secondary market is taxable. Short-term capital gains from sale of tax-free bonds on exchanges are taxed at the normal rate, while long-term capital gains are taxed at 10% without indexation and 20% with indexation, whichever is lower. By indexing, you adjust the purchasing price with annual inflation.

Who should invest?

Tax-free bonds are suitable for investors looking for a steady source of income annually and can afford to lock-in their capital for the long term.

The interest received on tax free bonds is slightly lower than interest received on normal bonds. However, if you compare the after tax returns, tax free bonds are better than normal bonds as no tax is required to be paid on interest earned from these bonds.

As interest received from these bonds is tax free, these bonds are highly advisable for taxpayers who fall in the higher slab categories of 20% and 30%.

AMC VIEWS

Equity Outlook: Axis Mutual Fund

Global: World equity markets continued to remain under pressure in September following the sell-off in August. Markets are worried about global growth especially the unfolding Chinese slowdown. Frontline indices (such as Sensex and Nifty) ended the month marginally lower after the 6% fall in August. Most sectors and segments of the market have been affected in this sell-off. The sell-off has been global in nature but emerging markets have taken a bigger hit. Emerging market funds have witnessed large redemptions as investors have become wary of growth prospects and there remain risks of crisis in certain countries affected by the commodity crash. India has out-performed other emerging markets in this environment as it is seen as relatively better placed to handle the challenges arising out of Chinese slowdown and US rate normalization. Global worries led to the US Federal reserve postponing policy normalization. It is now expected to raise rates only towards the end of the year.

Domestic: Despite the gyrations of the market, local retail investor interest in equities has remained robust. Equity mutual funds continue to get inflows. Creation of meaningful domestic institutional investors will be crucial to the continued market development going forward. In this regard, the decision to make a part allocation of PF/ retirement corpus towards equity is a huge step. Rainfall deficit for the entire monsoon season was at around 14% - slightly below the IMD forecasts. The spread was uneven with higher deficit in certain northern states. However sowing has remained on track and the kharif crop is not likely to get much affected by the deficit. Further better food supply management as well as discipline in MSP setting have kept food inflation broadly contained.

Corporate: Growth indicators have remained mixed. Industrial production surprised positively and indirect taxes have shown sharp growth so far this year. Election for Bihar state assembly will be held in the month of October and November. The verdict may affect market sentiment in the near term. Investors will also be looking at the winter session of Parliament to see if there is a change in the deadlock that affected the entire monsoon session. With inflation contained as well as the sharp fall in global commodities and worries of a global slowdown, RBI cut rates by a more than expected 50 bps. Further there are expectations of additional rate cuts going forward as inflation remains contained.

Debt Outlook: Murthy Nagarajan - Head - Fixed Income – Quantum Mutual Fund

The month of September was an action packed week due to higher CPI reading of 3.66 vs expectation of 3.5%, WPI inflation reading coming at negative 4.95 % levels, Federal Reserve not hiking rates and its dovish stance on inflation expectations and RBI policy action. However, the major action for the market was the move by RBI on its credit policy held on 29th September 2015. The RBI's monetary policy was loaded with surprises, especially for the bond market. Few in the market expected a 50 bps cut in policy. And it doesn't end there, the RBIs inflation forecast of 4.8% for January-March 2017 quarter suggests further room for rate cuts in CY 2016.

The monetary policy review by also providing a 2 year road-map for foreign investment in government bonds and state development loans has ensured that government bonds will remain supported and banks can reduce its SLR holdings in a calibrated manner without market disruption.

Bond yields have fallen by close to 20 bps with the 10 year government bond yield trading below 7.53% and given that the overnight rate is now 6.75%, we would expect bond yields to trend lower on attractive term spreads and potential demand from foreigners.

Guidance

With this 50 bps move; we expect further rate moves only post April 2016. By then, the fiscal policy for FY 17 would be clear and the initial monsoon forecasts would have been released. If favorable and one which provides comfort to meet the 5% January 2017 target, we should expect a further 50 bps rate cuts in CY 2016.

We have been arguing that the Real interest rate should be market rate and in press conference Governor Rajan suggested that for the Real rate calculation; they would look at the 1 year T-bill rate instead of the overnight Repo rate. In easy liquidity conditions, the 1 year T-Bill rate trades at about 25 bps spread over Repo.

One major reason for INR stability has been the combination of the reduction in India's inflation differential with the developed world and the emergence of positive Real interest rates thus reducing the INR risk premium.

INR will have to track global dollar and EM move and might feel the brunt of a large fall in global and Indian equities on equity outflows but based on the sustainable macro trend; the INR will continue to outperform its EM peers as it has since the low of August 2013.

Did you know?

India is the only country which has UNESCO World Heritage of all major religions.

Cartoon of the Month