MONTHLY NEWSLETTER – AUGUST 2015

MARKET COMMENTARY

Sensex : Up 1.2% Nifty : Up 1.96%	
Best performing sector: Media & Entertainment (8.9%)	Worst performing sector: Metal (-7.1%)
Best performing global index: French CAC 40 (6.1%)	Worst performing global index: Chinese Shanghai Composite (-14.3%)
Indian Rupee: 0.61%	Gold price: -7.7%

The month of July was positive for equity markets with Sensex rising by 1.2% and Foreign Institutional Investors (FIIs) pumping in a net amount of Rs. 5,589 crore. India remained among the most favoured destinations for overseas funds in July with equity markets receiving second-highest inflows globally. It was also a positive month for debt markets with the 10 year benchmark bond yield falling from 7.86 to 7.81%. Gold is losing its sheen and Indian retail investors continue to sell their gold exchange-traded funds (ETFs) as evident from 25 months of continuous outflows.

The rally in the stock market was obstructed because of concerns over the ability of the government to pass crucial reforms (like GST Bill, Land Acquisition Bill etc) due to Parliament logjam. The markets also suffered because Supreme Court-appointed Special Investigation Team on black money recommended tightening norms for Participatory notes (P-notes). Participatory notes, or P-notes, is a type of a financial instrument issued by registered foreign institutional investors (FIIs) or hedge funds to overseas investors who wish to invest in the Indian stock market without registering themselves with the Securities and Exchange Board of India (SEBI). The government has tried to address investors' fears, saying it will not react in a "knee-jerk" manner on the report.

Commodity prices have softened. In line with fall in international crude prices, petrol price was cut by Rs 0.31 a litre, while that of diesel was cut by Rs 0.71 per litre on 1st July. This was followed by yet another cut in petrol and diesel price by Rs. 2 per litre by mid-July. However, retail inflation increased to 5.4% in June (the highest in 4 months) mainly on account of food inflation. Exports data was released for the month of June – which showed a decline of 16% compared to June 2014. This was the seventh consecutive month of falling exports. Based on the corporate earnings one can conclude that domestic consumption has been lukewarm. In the early part of July rains were scanty but it picked up in agriculturally important regions like central and northwestern India by the end of the month – reducing the total deficit to 5%. Corporate balance sheets show signs of high debt burden. In fact, Indian companies fared the worst in a stress test conducted by the International Monetary Fund (IMF) for possible worsening of borrowing costs and earnings in case the dollar continues its recent strong and sustained appreciation.

Some of the measures and reforms announced by the Government are:

- New foreign investment Policy: The government allowed up to 49% foreign portfolio investment (FPI) through the automatic route in most sectors such as brownfield pharmaceuticals, single-brand retail, insurance, pension and facsimile editions of foreign newspapers.
- Promising a simpler foreign investment regime, the government introduced a concept of composite cap for all kinds of overseas inflows including through FDI, FII and NRI routes.
- The Cabinet, chaired by Prime Minister Narendra Modi, approved establishment of the proposed Rs 20,000-crore National Investment and Infrastructure Fund (NIIF).
- The government proposed to set up Bond Guarantee Corporation of India which will underwrite bonds issued by public and private sector companies in order to enhance their ratings to attract investments from insurers and pension funds that are mandated to park funds only in top-notch paper.
- A proposal to redevelop about 400 railways stations in metros and major cities besides pilgrim centres and tourist spots was cleared
- Proposal to transfer fertiliser subsidy directly into farmers' accounts and is planning a road map for the pilot project.

HOW FMPs SCORE OVER FIXED DEPOSITS

I-CAN FINANCIAL SOLUTIONS

What are FMPs?

FMP stands for Fixed Maturity Plan. These are very popular among corporate and high net worth individuals. An FMP fund manager invests across debt instruments issued by banks, financial institutions and companies. These are essentially close-ended income schemes with a fixed maturity date i.e. that run for a fixed period of time. When the fixed period comes to an end, the scheme matures, and your money is paid back to you. FMPs do not invest in equity. The portfolio is generally invested in debt and money market instruments maturing in line with the tenure of the scheme. The objective is to lock-in the investment at a specified rate of return thereby immunizing the scheme against market fluctuations.

Similarities between FDs and FMPs

- Defined Maturity and end date
- Debt instruments that have no exposure to equity markets

Difference between FDs and FMPs

- FMPs are issues by mutual fund companies while FDs are issued by banks
- FMPs have an 'expected' rate of return while FDs announce a fixed rate of return upfront.
- If a need arises before the maturity date a FD can be broken and funds may be accessed at a penalty. Pulling out of an FMP is not possible – in theory, however, FMPs can be sold on stock exchanges.
- FDs upto Rs. 1 lakh are insured. No insurance is available for FMPs

Taxation of FMPs

Dividend : Tax-free in the hands of the individual investor.

Investment in growth option of the FMP for less than 3 years : The gains are added to the investor's income and taxed at the investor's slab rate.

Investment in the growth option of the FMP for over 3 years : Either 10% capital gains tax without indexation or 20% with indexation.

Assuming the investor is in the 30% tax bracket, the following illustration shows that if one goes for a 3 year FMP the tax implication is drastically reduced.

	Fixed Deposit	FMP
Investment Amount	1,00,000	1,00,000
Value on Maturity after 3 years assuming 9% return	1,29,502.9	1,29,502.9
Indexation benefit at inflation rate assumption of 5%	Not allowed	1,15,762.5
Total Taxable Profit	29,502.9	13,740.4
Tax to be paid	8,851	2,748
Absolute Post-tax return at the end of 3 years	21%	27%

HOME INSURANCE

Home insurance is extremely useful for people living in areas that are prone to the risks of floods, earthquakes or burglaries. Most of the homebuyers in India ignore home insurance; it accounts for less than 1% of industry premium in terms of sales. People are either not aware of home insurance or are reluctant to buy it. They don't see the risk to their property—be it fire or an act of terrorism. The unfortunate part is that even the insurance industry is not pushing this.

Home insurance can cover losses to the structure and contents of one's home from any natural or man-made calamity. The disasters that can be insured against are fire, earthquakes, storms, cyclones, tempests, tornadoes, hurricanes, floods or inundation, lightning strike, explosion, landslides, impact by vehicles or aircraft, and bursting or overflowing of water tanks and pipes. However, care needs to be taken that only the cost of structure is insured and not the cost of land.

<u>Mainly two types of home insurance policies are available in India:</u>

Building Insurance

Insuring the building or building structure is important since it protects the policy holder against inevitable losses in case the insured building is destroyed or damaged in any natural or man-made calamities.

Content Insurance

Contents insurance under home insurance plans includes protection to movable goods, possessions or contents in the house; anything that is not a fixed part of the home, for example appliances, electronic goods, furniture and clothing etc.

<u>What to look for?</u>

Take care of a few things while buying home insurance so that the policy can be effective.

Time period: Home insurance can be bought for a minimum of one year to a maximum of five years. Do remember to renew.

Suitability: A bank may encourage you to buy its home insurance product along with the home loan. Choose only a policy that suits your needs.

Fine print: Home insurance policies are worded differently. For example, structure insurance may only be for building and not land, or only jewellery kept in the locker may be covered.

Tenants: If you are living in a rented house, you can insure only the contents and not the structure as you don't own it.

These are only some of the specifications. As with any kind of insurance policy, with a home insurance policy, too, the best results come through when the initial details are taken care of.

AMC VIEWS

Equity Outlook: ICICI Asset Management

The Greece crisis was averted after, Greece and European Central Bank (ECB) agreed to a new bailout deal. In another continent an important negotiation ended with positive results, Iran successfully negotiated with the major powers over its nuclear program. This has sent the crude prices under pressure and has been on a declining trend. With China's slowdown and no other country taking over its place, there has been a steady fall in commodity prices too. This bodes well for India's long-term growth, as majority of our imports comes from the energy segment.

Meanwhile on the local front, Monsoon seems to be at par with long period average (LPA), hence the probability of it being a concern anymore is negligible. Till date the monsoon is near normal. Also the RBI in its recent policy review mentioned that it will support growth and keep an accommodative stance, thereby signaling that interest rates could fall further.

On the downside, muted earnings can affect the sentiments of investors, and thereby increase volatility. Another factor that may push towards negative sentiment can be political headwinds, as the Government faces problems in passing key legislative bills -- GST, Land Acquisition bill, etc in the parliament. The US Fed rate hike also remains a key event in the international arena that can affect the domestic stock market.

Hence we continue to believe there could be reasonable volatility in equity markets in the near term even though over the long-term equity remains a suitable investment avenue for investors. We recommend funds with higher large-cap allocation as large caps remain relatively attractive compared to midcaps. We also recommend asset allocation products as a suitable option with an aim to ride the near term volatility of the market.

Debt Outlook: IDFC Asset Management

The downswing in the commodities market worsened during the month, with WTI crude oil witnessing the biggest monthly fall of 21% in 7 years, Brent crude oil falling 18% and Gold by 6.5% during the month (in USD terms). Bloomberg Index of Commodities has fallen 10.62% over the month, the most since September 2011. The continued fall in commodities is largely on account of low demand due to weak economic data across globe (especially from China, the largest metal user), strengthening dollar on expectation of Fed rate hike and an oversupply (especially for oil - rising output from OPEC and the expected output from Iran post lifting of international sanctions). For India, this fall in commodities can be seen as a positive for bond markets in terms of keeping the inflationary pressures off.

For large part of the month the market focus was on Greece. While Greek Prime Minister ended talks with creditors in June to hold a public referendum, which went the 'No' way, he later turned course to once again enter into deals with creditors for a bailout. Another global event that garnered attention is the continued turbulence in the Chinese stock markets and the slowdown of the second largest economy, with the latest Chinese PMI continuing to indicate contraction.

While there was an acknowledgement of improved economic data points in the latest FOMC meeting, there was no clear indication of the rate cut timing. While some market participants were expecting a rate hike as soon as September'15 post the FOMC meet, the recent quarterly wage growth data in the US (at its lowest since 1982) could dampen this expectation. Even as the prospects for the first US rate hike draw near, we believe it is possible for RBI to cut rates further. While the US rate hike cycle between 2004 to 2006 coincided with RBI also hiking rate, the phase had witnessed a significant rise in commodity prices. Hence, RBI's rate hikes were necessary to keep policy rates static. In contrast today, we are clearly in a global commodity downswing. Further, our Basic Balance (i.e. Current Account Deficit plus FDI) currently is at comfortable levels and is consistent with a much narrower real interest rate differential.

In its 4 August'15 monetary policy review, RBI kept all rates unchanged as expected. In our view, the assessment was on the margin more dovish and more focused on the medium term than the previous one. RBI has reduced its inflation projection for January – March 2016 by 0.2% and changed its assessment of risks to the 6% January 2016 inflation target from 'upside' to 'broadly balanced'. It has also retained the growth forecast for the year at 7.6%. While RBI is worried about the recent firming up in inflation at both core and headline level, as well as the recent rise in near term household inflation expectations, it has balanced its assessment on inflation by focusing on 'significant mitigating influence'. These include the sharp fall in crude oil prices since June and the likelihood of this to persist in view of global supply glut, increase in planting of pulses and oilseeds and prospects of rainfall in August and September according to some forecasters, effects of government's current pro-active supply management to contain shocks to food prices, and its decision to keep increases in minimum support prices (MSP) moderate.

Did you know?

Science day in Switzerland is dedicated to Ex-Indian President, APJ Abdul Kalam. The father of India's missile programme had visited Switzerland back in 2006. Upon his arrival, Switzerland declared May 26th as Science Day.

Cartoon of the Month