



Sanctum view

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Investment Strategy

Global Macro Update

The shock of the Russia-Ukraine conflict is wearing off from people's minds and growth concerns are beginning to surface. Global GDP growth forecasts are expected to be revised downwards - Fitch recently cut its world GDP growth forecast for 2022 by 0.7pp to 3.5%, with the eurozone cut by 1.5pp to 3.0%.

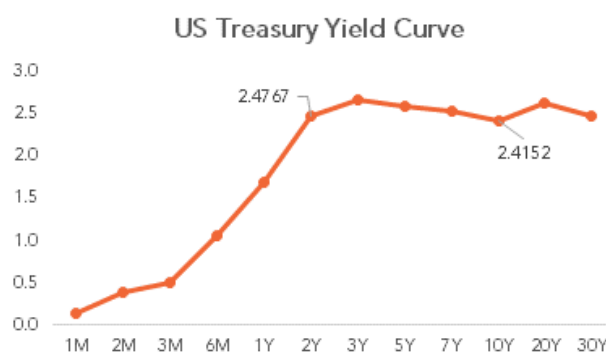
Even as the world battles the economic impact of the geopolitical tensions and ensuing sanctions, China shut down Shanghai in response to a new covid wave outbreak threat. This is serving to further exacerbate the already stressed supply chain issues.



Source: Vesselsvalue

Higher energy and commodity prices are going to crank up inflation further and squeeze household purchasing power. A few German retail chains have already guided for 20%-50% higher prices on some staples such as egg, butter, and select meats.

US Fed kickstarted its rate hike cycle with a 25 bps increase and at least 6 more hikes are expected within a year. Seven out of the last 10 rate-hike cycles have ended in a recession. On cue, the yield curve inverted a couple of days ago.



Source: Bloomberg, Sanctum Wealth

A 2/10 inversion (2-year yield > 10-year yield) traditionally has been a good predictor of recessions, if sustained for about a quarter. However, these recessions have followed anywhere between a few months and a 2-year lag. By the time recession reflects in numbers, almost always, the yield curve resumes a normal pattern.

India Update

Higher commodity prices and the resulting inflation will also trigger domestic GDP revisions. The upcoming RBI policy is expected to revise upwards its average inflation expectation for the year from 4.5% to 5.25% - 5.5%. While our rate hikes could be another quarter away, the tone of the policy could change from 'accommodative' to 'neutral'.

The decibel around the Fed rate hikes influences the expectations around the rate hike cycle in India as well. However, as seen in the table below, India real interest rates are nowhere close to being as negative as they are in the US and consequently, we expected India to hike rates by only about 100-125 bps this cycle, whereas the terminal US Fed rate is expected to reach 2.75% -3.0% by September 2023.

	US	India
CPI Inflation	7.9%	6.1%
Policy Rate	0.5%	4.0%
Real Interest Rate	-7.4%	-2.1%

Source: US Bureau of Labor Statistics, RBI, US Fed

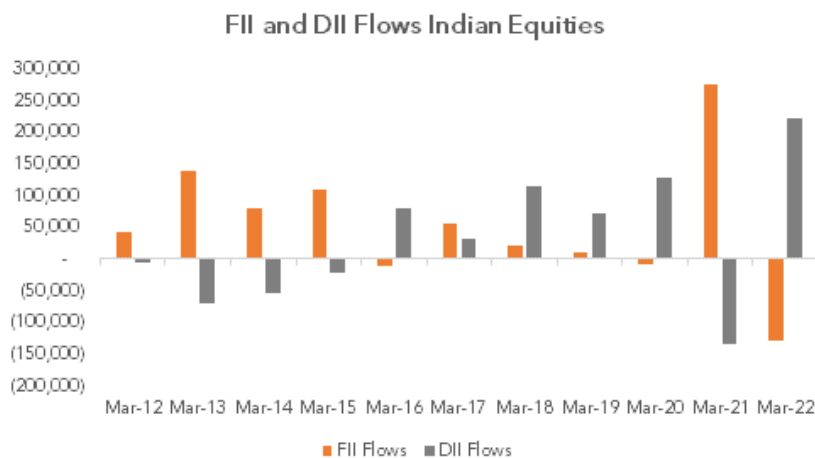
Equities

Indian equity market has been one of the top performing markets in FY 2022. While emerging markets delivered negative returns Indian equities delivered strong returns for the year. This is despite the fact that FIIs were net sellers this year. Large part of the FII outflows was driven by outflows from EM as a basket post the Russia-Ukraine crisis. Profit booking after a strong performance also led to outflows. However, FII flows were fully compensated by DII inflows.

Performance as of 31 st March 2022	1 Year	3 Year	5 Year
NSE Nifty 50 Index	18.9%	14.5%	13.7%
S&P 500 INDEX	14.0%	16.9%	13.9%
NASDAQ Composite Index	7.4%	22.5%	19.2%
Shanghai Stock Exchange Compos	-5.5%	1.7%	0.2%
Nikkei 225	-4.7%	9.5%	8.0%
MSCI Global Index	5.7%	11.8%	9.7%
MSCI AC Asia Pacific Index	-11.4%	4.1%	4.2%
MSCI Emerging Markets Index	-13.3%	2.6%	3.6%
Gold/US DOLLAR	13.5%	14.4%	9.2%

Source: Bloomberg, Sanctum Wealth

The above returns are local currency price returns, returns for MSCI indices are USD returns.



After the polarization we saw in equity markets in 2018, 2019 and early part of 2020, we had expected depolarization in FY22. As expected, we saw a broad-based equity rally with all major sectors delivering positive returns. Metals and commodity stocks saw the largest gains led by global rise in commodity prices.

Conclusion

We did not go underweight during the Russia-Ukraine crisis and remained neutral weight on equities. We continue to hold the neutral weight. However, a key risk that we are watching out for is the impact of cost pressures led by inflation on profit margins of corporates. As results for the quarter ended March 2022 are declared we would get a better sense of the trend in margins going ahead.

Our view on other asset classes also remains unchanged. We are constructive on gold as it acts as a hedge against inflation, and we continue to suggest barbeling fixed income portfolios.

Sanctum Wealth

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