Chola | Securities
Enter a better life

FINSPHERE

Your Monthly Guide on Global and Local markets from our Business Head's Desk.

Issue 06 | 7 Aug 2024

Global Market Volatility:

Navigating Currency Headwinds, Geopolitical Tensions, & Economic Shifts

Mr. Senthilkumar Naidu
Business Head, CSec

EXPLORE BEYOND THE SURFACE!

Dear Valued Clients and Stakeholders,

Volatility has gripped global equities as South East Asia is negotiating currency headwinds, Middle East troubled by deteriorating rather threatening geopolitical situation and entire west from Europe to America navigating economic headwinds. This month, global markets is facing a complex landscape shaped by varying economic performances and strategic monetary policy measures across major economies. On one hand Bank of England had cut interest rate interest in line with earlier interest rate cuts by ECB, Switzerland and Sweden while Japan raised their bench mark interest rate to 0.25% from 0% to 0.10% earlier range.

These measures triggered large scale rebalancing of currency carry trades. The US market is undergoing portfolio rebalancing/-sector rotation from technology heavy to economy facing companies. Further, jump in annual unemployment rate to 4.30% in July from 4.10% is characterized by noteworthy volatility in jobs market.

In the middle of all these developments, India's equity market has emerged as a standout performer, even in correction reflecting strong investor confidence. This monthly overview provides a comprehensive analysis of the key economic indicators and trends shaping the global economic environment, enabling insights into your investment decisions.

United States

Mixed Economic Indicators

In the past month, the economic landscape in the United States presented a blend of stability and challenges. The Federal Reserve's decision to maintain the benchmark interest rates at 5.25%-5.50% for the eighth consecutive meeting on July 31 was anticipated by Wall Street, as Fed Chair Jerome Powell suggested a potential rate cut in September if inflation continues to decline and the job market cools.

This comes against a backdrop of rising unemployment, which reached a near three-year high of 4.3% in July, reflecting a significant slowdown in hiring rather than layoffs. Job creation also decelerated sharply, with the economy adding only 114,000 jobs in July compared to June's 179,000, highlighting the impact of the Fed's previous rate hikes. Inflation data showed moderate price increases, with the PCE price index rising by 0.1% in June, supported by declining goods prices but offset by rising service costs. The core PCE inflation remained at 2.6%, aligning with the Fed's target.

On the GDP front, the US economy grew at a 2.8% annual rate in Q2 2024, driven by increased consumer spending, particularly in health care, housing, and recreation services, despite a downturn in residential fixed investment. In June 2024, the U.S. housing market exhibited mixed signals. Pending home sales rebounded sharply, increasing by 4.8% from the previous month, indicating renewed buyer interest, while median prices hit a record $426,900. Building permits rose by 3.4% to 1.446 million, driven by a surge in multi-family unit approvals. Consumer confidence rose to 100.3 in July, indicating improved economic sentiment, while retail sales remained virtually unchanged from the previous month but increased 2.3% YoY. The S&P Global US Composite PMI rose to 55.0 in July, suggesting continued growth.

The US trade deficit in goods narrowed to $96.84 billion in June, with exports and imports both rising, while industrial production increased by 0.6%, driven by advances in manufacturing output. Overall, the US economic landscape reflected a complex interplay of positive and cautionary trends, with some indicators showing resilience and others highlighting areas of concern.

Euro Area and Great Britain

Balancing Stability & Challenges Amid Economic Shifts

The European Central Bank (ECB) kept interest rates unchanged, with the main refinancing rate at 4.25%, amidst mixed inflation indicators. GDP growth for Q2 2024 was 0.6% year-on-year, the highest in five quarters, driven by robust performances in France, Italy, and Spain, although Germany contracted by 0.1%. This is followed by 0.50% GDP growth in Q1. Inflation in the Euro Area saw a rise to 2.6% in July, from 2.5% in June, while core inflation remained steady at 2.9%.

Manufacturing remained under pressure, with the Manufacturing PMI at a year-to-date low of 45.8, signaling continued contraction. The Composite PMI dropped to 50.1, indicating near-stagnation, while the Services PMI fell to 51.9, reflecting a slowing expansion. Industrial production declined by 2.9% year-on-year in May 2024, highlighting ongoing challenges in the sector.

A significant policy move saw the EU imposing steep tariffs on Chinese electric vehicles, potentially reshaping trade dynamics and affecting market competition.

In Great Britain, the Bank of England made a notable move by cutting interest rates to 5% in July 2024, marking its first rate cut in over four years. The unemployment rate remained steady at 4.4% from March to May 2024. The British economy expanded by 1.4% year-on -year in May 2024, the most substantial growth since June 2023. Inflation held steady at 2% in June, with significant contributions from the hospitality sector, although fuel prices saw a decline.

Overall, Europe is cruising along though at snail's pace.

Japan & China:

Economic Balancing Acts Amid Currency and Policy Shifts

The Bank of Japan (BOJ) raised its key interest rate from zero to approximately 0.25%, aiming to curb the yen's depreciation against the US dollar. This move has led to a notable appreciation of the yen, impacting Japan's export competitiveness. This recent surge in the yen has led to market upheavals, with many investors unwinding their yen carry trades. Meanwhile, Japan's industrial production experienced a significant decline of 7.3% year-on- year in June 2024, marking the steepest fall since September 2020.

Japan's factory activity too, contracted slightly in July, with the Manufacturing PMI slipping to 49.2 from 50.0 in June. However, the service sector expanded, with the Services PMI rising to 53.9, indicating growth in the private sector. Tokyo's core consumer price index (CPI) rose by 2.2% year-on-year in July, up from 2.1% in June, reflecting ongoing inflationary pressures. Japan's wholesale inflation accelerated to 2.9% in June due to the weak yen increasing the cost of raw material imports. Deputy Governor of Bank of Japan has been on record saying further interest rate hikes will be on hold as policy makers want stable equity markets.

In China, industrial profits grew by 3.6% year-on-year in June, a notable increase from the 0.7% gain in May. However, the Chinese economy expanded by only 4.7% year-on-year in Q2 2024, missing market forecasts of 5.1% and slowing from a 5.3% growth in Q1. This

deceleration is attributed to a persistent property downturn, weak domestic demand, and trade frictions with the West. The People's Bank of China cut the one-year loan prime rate to 3.35% and the five-year LPR to 3.85% to stimulate the economy.

China's factory activity continued to contract in June, with the manufacturing PMI remaining at 49.5, while the services PMI fell to 51.2, the lowest in eight months. This indicates a slowing pace of expansion in the services sector, affected by a decline in new orders and weaker overseas demand. China's pace of economic growth is susceptible.

India's Q1 Earnings

A Challenging Quarter

In the past month, India has experienced a mixed economic landscape characterized by strong equity market performance but underwhelming earnings growth. As of Q1FY25, India emerged as the best-performing equity market globally, with a 10.35% rise in CY'24. However, this was juxtaposed with a disappointing earnings season, as the aggregate PAT growth of 400 companies registered a mere 2.13% YoY and a significant decline of -7.87% QoQ.

Sustainability and quality of earnings growth is another grey area. Financials which have been pole bearer of earnings growth is marked by divergence between large banks and mid to small NBFC's. Quality of earnings growth reported by NBFC's has come under scanner as large private and public banks have reported slippage in asset quality particularly in retail and agriculture loans which had been the key credit growth driver for BFSI sector at large.

India's Budget FY25 introduced several fiscal adjustments, including a revised fiscal deficit target of 4.90% for FY25 and changes in tax structures affecting long-term and short-term capital gains. Meanwhile, direct tax collections saw impressive growth, with gross collections up by 23.2% to ₹6.45 lakh crore, and net collections rising by 19.54%. GST revenue also increased, reaching a three-month high of ₹1.82 lakh crore in July 2024.

The IMF and ADB raised their growth forecasts for India, projecting GDP growth at 7% for FY25, citing strong public investment and potential output growth. The RBI's bulletin highlighted an increased natural rate of interest, indicating expectations of sustained economic momentum. Rainfall patterns have been uneven, with central and southern regions experiencing surplus rains, while the northwest and eastern parts faced deficits, impacting agriculture and water management. Despite these challenges, India's economic indicators suggest resilience, although caution is warranted given the mixed performance across various sectors. Valuation wise market is trading at plus + 1 S.D @ PER. Q1FY25 earnings so far has largely been a disappointment. A look at net profit aggregate of 348 companies under consideration shows only ~3.40% YoY growth while a decline of -5.85% QoQ.

The market capitalization to GDP ratio has breached the 15-year high of 150% as of July 2024 and the equity risk premium has climbed to 2.87%. Q1FY25 earnings update by SBI is alarming. Having regard to all above factors, we remain cautious on Indian equities from a short to medium term perspective.

However, deep corrections, will be an opportunity to accumulate quality companies at lower levels. The government's fiscal measures and the continued focus on public investment are expected to support growth, even as inflationary pressures and sectoral disparities pose ongoing challenges.

Warm Regards,

Mr. Senthilkumar Naidu
Business Head, CSec

FINSPHERE | ISSUE 06 7 Aug 2024

Chola | Securities
Enter a better life

"Cholamandalam Securities Limited (CSEC) is a SEBI registered Stock Broker and Depository participant. CIN – U65993TN1994PLC028674

SEBI Registration No : NSE/BSE : INZ000168236; NSDL/CDSL : : IN –DP-556-2021; Research Analyst - INH200000402; AMFI No – ARN-52825; IRDAI Registration No (Corporate Agent): CA0618. Registered Office: Chola Crest, C54-55 & Super B-4, Thiru-Vi-Ka Industrial Estate, Guindy, Chennai – 600 032. CSEC is only a distributor of Insurance, PMS & AIF, Mutual Funds, Fixed Income and Loans. Brokerage will not exceed the SEBI prescribed limit. Margins as prescribed by Exchange/SEBI will be applicable.

Investments in securities market are subject to market risks, read all the related documents carefully before investing.