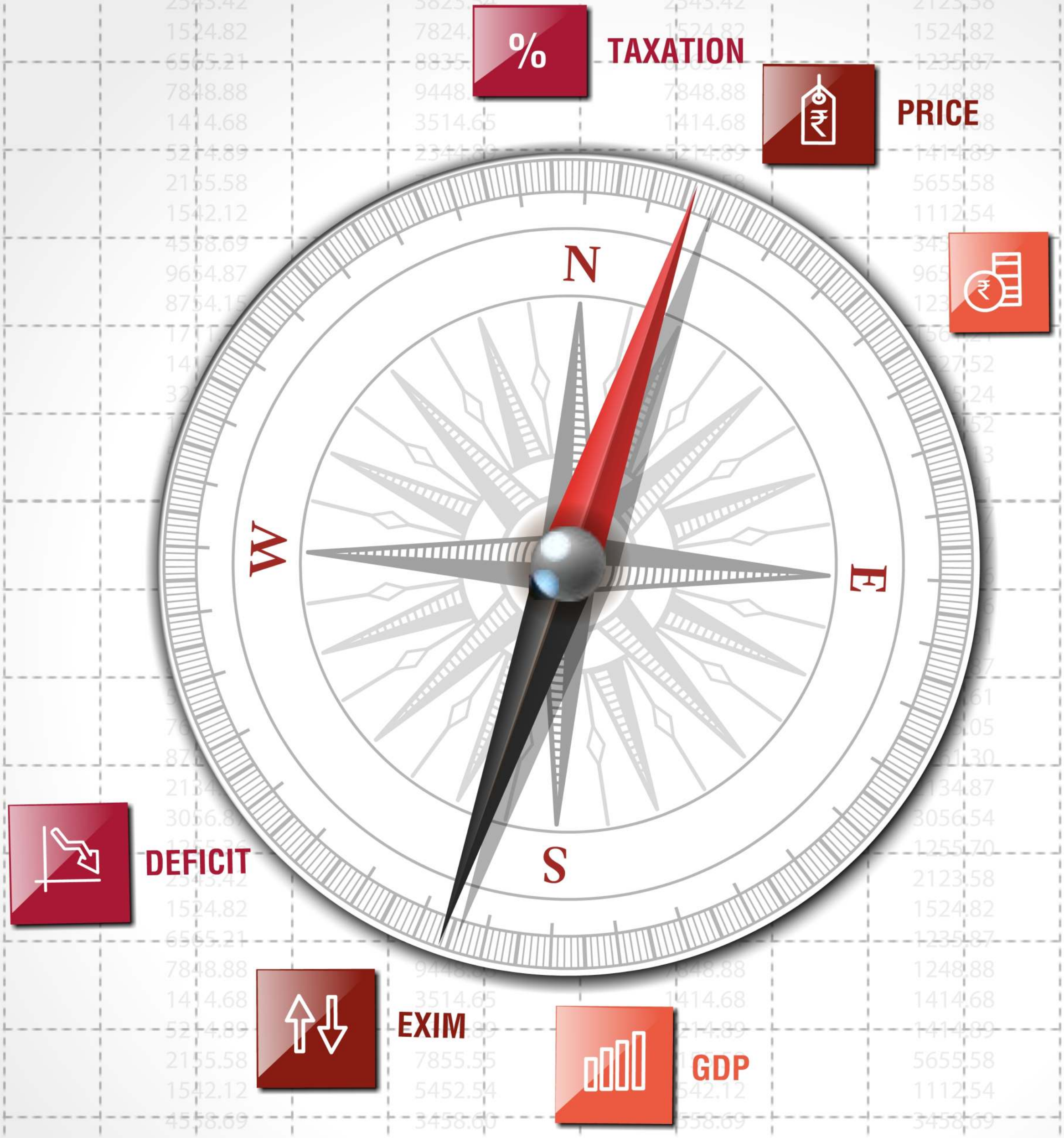
Investment Snapshot

For Quarter Ended June - 2018

India - a story of improving micros and challenging macros



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Dear **Valued Policyholder**,

After a relatively tranquil CY2017, a bout of volatility has hovered over the markets in CY2018 amidst challenging global macros and rising domestic concerns. Q1FY19 was indeed an eventful quarter, which kept the markets on tenterhooks beginning with global Central Bank's tightening and tapering plans, followed by the growing trade war between US and China and then the OPEC meet on oil supply decisions. Domestically, RBI's monetary policy rate hike, the political outcome of the Karnataka elections, progress of the monsoons, and the rupee movement, further kept the markets on the edge. The key positive in the quarter was India's GDP growth continuing its upward momentum for the third consecutive quarter with Q418 GDP growth recorded at a seven-quarter high of 7.7% YoY and GVA at 7.6%. In addition, the corporate earnings continued to march towards an upward growth trajectory in Q4FY18 with a few exceptions such as BFSI and Telecom, while many companies in sectors like FMCG, Private banks and Automobile showed positive results and have seen earnings grow for FY19 and FY20.

While Nifty recovered 6% from its low of 10,000 during the quarter, broader markets i.e. midcaps and small caps continued to spiral downwards, as investor sentiment continued to remain somber and laden due to the fear of uncertainty leading to a flight of safety towards quality large cap stocks, which drove the Nifty performance. Improving growth dynamics and rising treasury yields in the US have led to the shift of capital from emerging markets to developed markets leading to FPI outflows and currency depreciation in most of the emerging markets. While FPIs continued to pull back from EMs in Q1FY19, Indian markets were less impacted than their EM counterparts, given the strong domestic liquidity with DII flows that were sustained due to positive real interest rates driving financial savings and strong and stable SIP equity flows, despite the incumbent domestic concerns.

The Indian debt market continued to remain under pressure in 2018, both at the short and the long end of the curve, with G-sec yields continuing to inch upwards. The ten-year benchmark bond yields rose 50bps during the quarter to close at 7.9%, as market participants remained worried about crude oil prices, rising inflation and global macro concerns and risk off, which led to weakness in EM currencies including rupee. Driven by a fear of rising inflation, RBI hiked repo rate by 25bps in June with a neutral stance, to which the markets were indifferent as bond yields were already pricing in a shallow rate hike cycle. Although inflation has been on a rising path and is expected to average around 5% in FY19, it still remains within RBI's tolerance band. The key solace for the bond markets was the fact that crude oil prices would remain under check, as the OPEC and the non-OPEC oil producers agreed to boost the supply of crude to bring the conformity level back to 100% at their June OPEC meet. Bond dynamics were further supported by the announcement of the second Open Market Operations (OMO) purchase of ₹10,000 cr and by a tentative return of a PSU bank into the market. Besides, improving GST collections (average run rate of ₹97,000 cr per month in Q1FY19 vs an earlier run rate of ₹89,000 cr) will bode well for bond yields, as the concerns around fiscal slippage will recede, with higher expected GST collections in FY19.

Despite the markets being currently plagued with the above concerns, key tailwinds manifesting in the form of recovery in economic growth, with visible green shoots in consumption and capital goods, credit growth picking up, strong domestic liquidity and corporate earnings recovery, will provide succour and help tide over global volatility.

Going forward, the recovery in corporate earnings would be a key positive trigger for the markets. The Q4FY18 earnings (ex-BFSI) and Q4FY18 GDP growth indicate that, the micro level indicators will continue to improve and are likely to see an improved earnings performance by the corporates going forward. FY19 earnings growth trajectory should pick up as banks (which were a drag on FY18 earnings) will come out of the high provisioning zone with the redressal of NCLT cases. Besides this, the prediction of a normal monsoon will augur well for rural focused stocks.

On the macro front, we believe that the Indian economic growth will be driven by strong infra related spends, uptick in rural consumption and rural infrastructure development; urban consumption, translating into strong GDP growth and the nascent recovery of the private investment cycle, which will augur well for investment in Indian markets. At present, acceleration in rural consumption, MSP hikes and normal monsoon portend a sustainable growth in consumption in the economy. Besides, high frequency indicators show strength in consumption, services and investment (infrastructure, non-gold & non-oil imports growth). With green shoots of capex recovery being conspicuous especially in sectors such as steel, cement and refineries, we believe that the growth may surprise on the upside. Domestic liquidity still remains robust, as the monthly SIP in equity mutual funds remains strong. Nonetheless, headwinds of macro variables in terms of fiscal slippages & twin deficits may continue to weigh on the markets. While corporate earnings have surprised negatively in five out of the last six years, the scope for a negative surprise in FY19 is rather slim, due to a favourable base and a revival in economic activity which will provide strong tailwinds and hence valuation multiples could remain at a premium level.

Looking ahead, as Indian markets continue to tide over global volatility and confront challenges; We have always strived to achieve good risk adjusted return for our funds across categories in Life, Pension as well as Group funds over the long term. In addition, we have been declaring good bonuses to our traditional policyholders. Insurance being a long-term investment tool, it is advisable to remain invested and complete the term of the policy to optimize returns. With the baton moving from macros to micros, corporate earnings recovery as indicated by the high frequency indicators, would be a key positive catalyst for driving the performance of the markets, followed by the continued pickup in economic activity translating into positive debt and equity market performance over medium to long term. While one cannot rule out the possible correction in equity markets amid global concerns and that volatility may persist in markets due to several state elections and union elections in 2019, along with continued changes in macro variables, but earnings may provide succour. Indian equity markets remain an attractive long-term bet for an investor, as the benefits of structural reforms initiated by the incumbent government will begin to manifest in the next few years. We remain constructive on the markets over medium to long term and deem every correction as an opportunity to invest in good quality stocks. From a debt market standpoint, improving GST collections, lower probability of fiscal slippages (with increase in crude supply - OPEC June meet), inflation being in RBI's tolerance band and Dollar Index and US ten year being range bound, we expect the Indian bond yields to remain range bound.

We remain committed towards offering the best-in-class products and services to our valued customers. We would like to take this opportunity to thank you for entrusting your hard-earned savings with us and look forward to your unflinching faith and continued support in the future as well.

Regards,

Vaswani

Jyoti Vaswani

Chief Investment Officer

Global Economy

Global Central Banks remain in the spotlight

The US Federal Reserve (Fed) raised its benchmark of short-term interest rate by 0.25% for the second time in this calendar year, taking it to a range of 1.75% - 2% in June 2018. Fed Chairman, Jerome Powell indicated that two more increases are likely this year. As per the minutes of Fed's June policy meeting, the policymakers discussed whether a US recession was around the corner and expressed concern over the potential impact of global trade conflicts on the US economy.

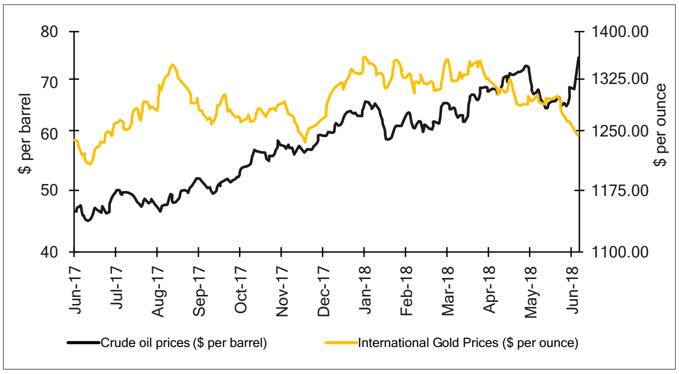
The Bank of England (BoE) maintained its key interest rate at 0.5% and quantitative easing program at £435 billion Meanwhile, BoE Governor Mark Carney remained bullish about UK's growth prospects, as he pegged the slowdown of the first quarter economic growth to bad weather, thereby raising expectations of an interest rate hike in the August policy meeting. The European Central Bank (ECB) kept its key interest rate unchanged and reaffirmed its decision to continue to make net asset purchases until the end of 2018 at a monthly pace of €30 billion until September 2018, following which they would be halved to €15 billion in the final quarter of 2018 before being curtailed completely. The bank also indicated that an interest rate hike would be unlikely, prior to the summer of 2019.

Bank of Japan (BoJ) maintained its ultra-loose monetary policy with the key interest rate at -0.1%. China resolved to continue deepening financial reform and opening its economy to overseas investment. Central Bank Governor, Yi Gang stated that the economy had entered a stage of "new normal".

- The US economy grew at a 2% annual rate in Q1 2018 compared to 2.9% recorded in Q4 2017.
- The UK's annual GDP growth slowed down to 1.2% in Q2 2018 from 1.3% in the preceding quarter.
- The Eurozone economy expanded by 2.5% in Q1 2018 compared with 2.8% in Q4 2017.
- Japan's economy contracted at an annualized rate of 0.6% in Q1 2018 versus 0.6% growth in Q4 2017.
- China's economy expanded at a 6.8% annual pace in Q1 2018, steady compared with Q4 2017.

Crude oil prices rose due to supply concerns; gold lost sheen on rising investor risk appetite and international crude oil prices rose to 14.2% in the quarter on fears of lower supply owing to US sanctions on Iran and the disruptions in Venezuela. Prices also climbed after the OPEC decided on a smaller-than-expected increase in the output. International gold prices fell 5.5% in the quarter as the risk appetite returned after the US and North Korea came to an agreement to denuclearise the Korean peninsula. The prices fell further on upbeat US and global economic cues, and after the US Fed indicated two more interest rate hikes during the remainder of the calendar year.

Chart 1 - Crude oil versus gold prices



Source: NYMEX, LBMA

Global Equity

Chart 1 - Crude oil versus Gold prices

Indices	29-June-18	Quarterly % Change	Yearly % Change
DJIA (USA)	24271	0.70	13.69
Nikkei 225 (Japan)	22305	3.96	11.34
Hang Seng (Hong Kong)	28955	-3.78	12.38
FTSE 100 (UK)	7637	8.22	4.43
Shanghai Composite Index (China)	2847	-10.14	-10.81
DAX (Germany)	12306	1.73	-0.16
iBovespa (Brazil)	72763	-14.76	15.68
MICEX (Russia)	2296	1.10	22.16

Source: Yahoo Finance, Bloomberg, Moscow Exchange

Global equity indices ended mixed.

China's Shanghai Composite Index declined over 10% as sentiments were hit by trade tensions between the US and China. Political uncertainty surrounding Italy's membership in the Eurozone added to the selling pressure on Chinese stocks. Japan's Nikkei index advanced nearly 4% on encouraging corporate announcements and intermittent weakness in the Yen. UK's FTSE index advanced by 8% on sector-specific gains and as some domestic cues led to hopes that an interest rate hike by the BoE may be delayed.

Indian Economy

India clocked a robust economic growth in the fourth quarter of the previous year. Various international and domestic institutions expressed optimism about India's economic prospects, including the Reserve Bank of India (RBI) and the International Monetary Fund (IMF). Noting the threats posed by the rise in crude oil prices and the resurgence in domestic inflation, the RBI hiked its benchmark repo rate by 25 basis points (bps) to 6.25%, marking the first increase in the policy rate since 2014. The apex bank, however, maintained a neutral policy stance. The minutes of the latest meeting indicated that the panel opted not to shift to a 'tight' regime as it awaited clarity on the inflationary impact of a government proposal to increase the minimum purchase price of food grains, along with cues on direction of oil prices.

Among major developments, the US told India and other countries to cut oil imports from Iran to 'zero' by 4th November or face sanctions. The government put in place a detailed protocol for clearing all Foreign Direct Investment (FDI) proposals, as a part of an exercise to speed up approvals and bring about greater transparency. The Centre also approved revising guidelines on time bound closure of sick and loss-making central public sector enterprises and cleared amendments to the Insolvency and Bankruptcy Code (IBC), including an ordinance to give homebuyers a creditor status under the IBC. On the GST front, the GST Council approved a simpler framework for filing returns and cleared a proposal to convert the GST Network (GSTN) into a government company.

- The Indian economy grew by 7.7% during January-March 2018 compared with a 7% growth in the previous quarter. It grew 6.7% in fiscal year 2018 against 7.1% a year earlier.
- The World Bank predicted that the Indian economy will see a robust GDP growth of 7.3% in 2018-19 and 7.5% in the next two years.
- The RBI retained GDP growth for 2018-19 at 7.4%. It expects the GDP growth to be in the range of 7.5-7.6% in the first half (H1) and 7.3-7.4% in the second half (H2), with risks evenly balanced.
- India's current account deficit for the last year widened to 1.9% of the GDP from 0.6% in 2016-17.

Indian Equity

Table 2 - Indian benchmark indices returns

Sector Indices	29-June-18	Quarterly % Change	Yearly % Change
Nifty 50	10714	5.94	12.53
S&P BSE Sensex	35423	7.45	14.56
S&P BSE IT	13920	15.04	41.56
S&P BSE FMCG	11213	8.97	7.53
S&P BSE BANKEX	29251	7.55	11.31
S&P BSE Healthcare	14004	6.43	-1.32
S&P BSE Auto	23838	-0.91	1.84
S&P BSE Metal	13064	-1.93	14.86
S&P BSE CG	17488	-5.35	2.41
S&P BSE Oil & Gas	13660	-6.53	3.46
S&P BSE Realty	2073	-7.02	1.48
S&P BSE Power	1947	-8.43	-12.53
S&P BSE CD	20207	-9.23	26.19

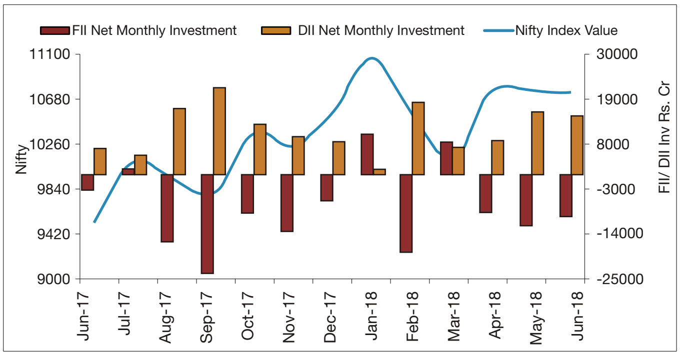
Source: BSE, NSE

Indian equities rose on RBI's neutral stance.

Indian equities - represented by the Nifty 50 and S&P BSE Sensex - advanced to 6% and 7% respectively in the quarter, aided by announcements of positive earnings, intermittent recovery in the rupee, and some encouraging domestic economic indicators such as the latest economic growth figures. Intermittent correction in global crude oil prices and India Meteorological Department's (IMD) view that India would likely receive 'normal monsoon' buoyed sentiments. The market got a further lift after RBI's interest rate setting committee unanimously voted to hike rates, while maintaining a neutral stance. Intermittent gains in global equities after US President Donald Trump and North Korean leader Kim Jong Un pledged to work towards complete denuclearisation of the Korean peninsula, also brought in some gains.

However, further gains were prevented by fears of global trade war after US and China imposed multiple rounds of tariffs on imported goods. The market also fell owing to uncertainty over the formation of the government in Karnataka and on concerns about the long-term health of the Eurozone due to the political turmoil in Italy. Intermittently, a few other developments, such as US President Donald Trump's decision to scrap the Iran nuclear deal and a more hawkish policy stance by the US Fed, which is expected to implement two additional interest rate hikes this year, also triggered some sell-offs.

Chart 2 - FII, DII versus Nifty movement



Source: NSE

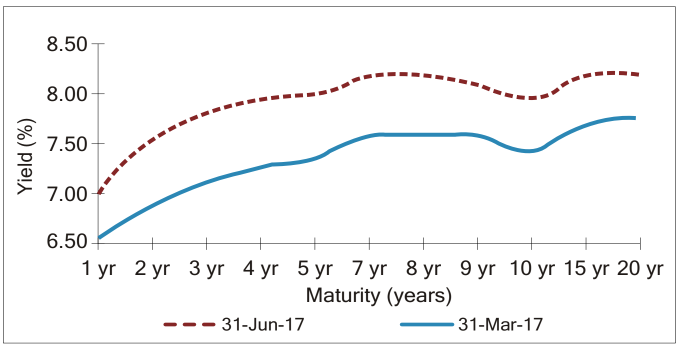
- The S&P BSE information technology index was the top gainer during the quarter (up 15%) as exporters were aided by the rupee's depreciation against the greenback.
- The S&P BSE FMCG index advanced nearly 9% as investors opted to place defensive bets in the face of equity volatility.
- The S&P BSE auto index declined nearly 1% as sentiment was dented on speculation that the US may launch auto tariffs.
- The S&P BSE Oil and Gas index fell nearly 7%, as shares of oil marketing companies declined as crude oil prices strengthened globally. Speculation that the Centre may ask oil marketing companies to share the burden of higher petrol and diesel prices also pulled the benchmark down.
- FIIs sold ₹31,894 crore in Indian equities in June quarter vs a net sales of ₹1,146 crore in the previous quarter.

Equity Outlook

With the baton moving from macros to micros, recovery of corporate earnings as indicated by high frequency indicators, would be a key positive catalyst for driving the performance of markets, followed by the continued pick-up in economic activity translating into positive equity market performance over medium to long term. While one cannot rule out the possible correction in equity markets amid global concerns and that volatility may persist in markets due to several State and Union elections in 2019, along with continued changes in the macro variables, but earnings may provide some succour. The Indian equity market will continue to be an attractive long-term bet for investors, as the benefits of structural reforms initiated by the incumbent government will begin to manifest in the next few years.

Indian Debt

Chart 3 - Domestic yield curve movement



Source: CRISIL Fixed Income database

Gilts fell on rising inflation and higher crude oil prices.

Government bond prices declined in the quarter, with the yield of the 10-year benchmark bond settling at 7.90% on June 29, 2018 vs 7.40% on March 28, 2018. The prices declined due to the following reasons:

Prices declined because:

- The rupee weakened sharply against the US dollar. A weak rupee erodes foreign investors' returns on Indian assets, making these investments less lucrative.
- The Central Bank hiked its policy repo rate by 25 bps to 6.25%, marking the first increase in interest rates since 2014. Apart from raising interest rates, the Central Bank revised its inflation projections.
- The resurgence in domestic inflation amid a rise in global crude oil prices triggered rising concerns about further policy tightening by the Central Bank.
- A revision of norms pertaining to the valuation of the State Government securities by the Central Bank, a move that will increase the mark-to-market losses that banks suffer on these papers, weighed on demand.
- The uncertainty surrounding the outcome of the Karnataka state assembly elections also dented sentiments.
- The US Fed hinted at two more interest rate hikes this year instead of the one suggested earlier.

Further losses were prevented by:

- Bond repurchase announced by the Central Bank to relieve supply pressure.
- Private weather forecaster Skymet's prediction of a normal monsoon rainfall.
- The RBI's notification that the limit for foreign portfolio investors (FPI) in gilts had been raised by 50 bps for the current fiscal to 5.5% of the outstanding stock, and to 6% by 2019-20 (April-March).

On the regulatory front,

- The Central Bank's move to ease rules for foreign investment in government securities (G-secs) sparked hopes of more inflows in the near term. The RBI withdrew a rule that mandates FPIs to invest in government bonds and state development loans (SDLs) with at least three years of residual maturity. It also capped investment by FPIs in corporate bonds with residual maturity of below one year at 20% of that foreign investor's total holding of corporate securities.
- In the June policy review, the RBI hiked CPI projection for fiscal year 2019 to 4.8-4.9% in H1 and 4.7% in H2, including the HRA impact for central government employees, with risks tilted to the upside. Excluding the impact of HRA revisions, CPI inflation was projected at 4.6% in the first half and 4.7% in the second half.

Debt Outlook

The ten-year G-sec yields have been on a rising trend previously, due to the risks emanating from rising crude oil prices, inflation and tightening liquidity and global macro concerns. However, going forward we expect the Indian bond yields to be range bound, given the improving run rate of GST collections, lower probability of fiscal slippages (with increase in crude supply - OPEC June meet), inflation being in RBI's tolerance band and the Dollar Index and US Ten year being range bound.

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