Modi’s magic

Investors had priced in Narendra Modi's landslide election with exit polls pointing to his return as India’s Prime Minister and the leader of the Bharatiya Janata Party.

Economic and macro issues

Modi’s victory comes as India grapples with weakening domestic consumption, rising unemployment, slowing economic growth and its trade deficit. There is also the additional risk of being drawn into a trade dispute with the US. Modi’s win should translate as policy continuity, which should be viewed positively by investors. India may see a lift from improving domestic consumption and the resumption of private capital expenditure as ripple effects. In the more immediate term, the stability of the Rupee should encourage funds inflow into the country as an emerging market.

Positioning

With India’s equities trading close to one standard deviation above the 5-year price-to-earnings ratio average, valuations are not supportive and our position is on a neutral weighting. However, within the Asia ex-Japan portfolio, India’s equities are considered more attractive against regional peers as the country has been relatively spared from US trade skirmishes. Hence, we will turn overweight on India’s equities if prices correct downward. For sectors, we are more bullish on financials, especially corporate lenders, as we expect non-performing loans to decline. We would also look to add some mid-cap stocks which are relatively cheap.

Risks ahead

On the trade front, while the US has largely fixated its attention upon China, India could be next on the list with Trump blasting the country as “the tariff king”. Therefore, the export and healthcare sectors are a risk with the trade deficit India has with the US.

The Reserve Bank of India (RBI) had lowered interest rates by 50 basis points since the start of 2019, maintaining a dovish outlook. So any unexpected rise in inflation triggered by a bad monsoon or oil price spike may force the central bank to tighten which poses a risk to the stock market. But as food inflation currently appears muted, this should allow the RBI to be more accommodative.

Another risk to note is the liquidity tightness in the banking system and the RBI needs to continue to improve monetary conditions. Lastly, with the country still in a fiscal deficit, we are watching out for the government meeting its targets on goods and services tax (GST) collections to bridge the fiscal gap.

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