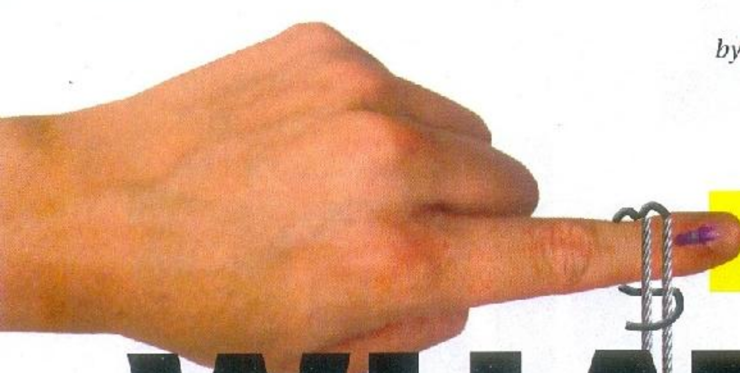
COVER STORY

by **TEAM OUTLOOK MONEY**



ELECTIONS 2014

WHAT'S IN STORE

There's the impression that a stable government at the Centre will quickly solve India's economic woes. But will it?

ECONOMIC GROWTH OUTLOOK

Unlikely to improve dramatically in the next one year. Most optimistic estimates for 2014-15:

6 per cent

- Govt doesn't have the money to boost economy with tax cuts and spending while high inflation prevents RBI from reducing interest rates
- Banks and financial institutions not financially strong enough to fund expansion as their money is stuck in many large infrastructure projects besides bad loans
- The corporate sector is still carrying a lot of debt on its balance sheets and cannot fund expansion until it reduces its debt burden
- Global growth prospects are still weak in many areas such as China
- Plenty of spare capacity in sectors, such as auto, due to weak demand as well as supply bottlenecks such as coal for power. New investment can only follow better capacity use

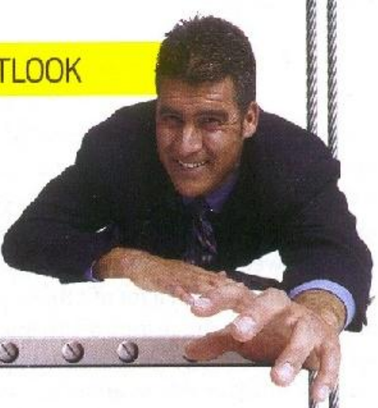
Graphics: VARUN VASHISHTHA

INFLATION OUTLOOK

Expected to go down in the next two years, but is **unlikely to fall much any time soon**. The fall will be slow and there could even be temporary reversal of the trend because of short-term shocks such as a bad monsoon. The new government's policies to contain food price rise, a major part of retail inflation, holds the key

FIXED INCOME OUTLOOK

With India Inc. working on its costs to regain its margins, continued high inflation, economic growth not expected to rebound substantially, **pay hikes are likely to be moderate**



LOAN RATES OUTLOOK

More of the same likely in store with rates for home and car loan remaining high. With inflation expected to stay high only an imprudent government can create conditions for precipitous fall in rates.

FIXED INCOME OUTLOOK

Expect tight liquidity conditions to continue in the near future and this will mean **continuance of high fixed deposit rates**
With inflation remaining high, the net returns will be negative

EQUITIES OUTLOOK

Don't be surprised to see a stock market correction in the days leading up to election results day (16 May). After a few days of euphoria in case of a decisive verdict, expect increasing negative global news and of a bad monsoon to take a grip of the market. That will in all likelihood force a correction. Expect a rebound once the new government's policies show effect after a gap of a quarter with **plenty of volatility in the interim**

REAL ESTATE OUTLOOK

Has been marked by a dearth of buyers in the new and resale markets and a flat price of residential properties and other categories. A decisive verdict should lift sentiments and prices, while a less-than-clear mandate will perpetuate *status quo*. Measures to boost the sector in the **Union Budget will hold the key**

GOLD OUTLOOK

In case of global turbulence due to economic slowdown in China and other places, this summer should see a periodic reversal of its recent decline, but **decline over the medium term** likely as global economy recovers

COVER STORY

You are probably carrying the indelible ink on your index finger still, proof that you voted in the General Elections 2014. And the persistently high inflation and continuing economic slowdown were probably on your mind too, as they were on those of a lot of others, when you cast your ballot. Awaiting the results on 16 May, the question uppermost on voters' minds is whether the new government would be able to effect an economic turnaround. Some experts are predicting a major resurgence and continued upsurge in the stock market that has already touched all-time highs in the run up to the elections. But is that going to happen just yet and what would it mean for your money?

The Emerging Big Picture

Economic growth. With its revenues trailing its expenses primarily due to the slowdown in economic activity and incomes, the government is financing its shortfall by borrowing. Since borrowings are already high, the government's ability to spend to drive economic growth will be limited. So, things may not get better just yet. The Indian Metrological Department (IMD) has just forecast a sub-par monsoon this year, which, if it turns out to be correct, would impact the agricultural production, farm incomes and rural consumption. Any big spike in government expenses due to a consequent emergency will further aggravate the fiscal problem. The country's central bank, Reserve Bank of India, can't spur growth either. Stubbornly high inflation has effectively tied its hands.

As for India Inc., many of its members are still trying to rid their balance sheets of big debt, a legacy of the high-growth years. Besides deleveraging, they would also be adjusting their capacities to square up with the weak consumer demand and costs to high input prices through cost-containment and productivity-enhancing measures. Many banks that have financed economic expansion are finding themselves saddled with money stuck in stalled projects and bad loans. Now in fix-the-finances mode, banks are unlikely to get aggressive. The implication for you: Continuation of the trend of the recent past of moderate pay hikes and muted hiring. Not making things any easier are global economic conditions. With important economies, such as China, Japan and some European countries, showing signs of slowing down, global growth factors are unlikely to be favourable.

ACTION PLAN

JOBS

Have realistic pay hike expectations, avoid ill-considered job hopping and invest in core skills.

ACTION PLAN

FIXED INCOME

Lock in to fixed deposits currently paying high interest rates. Invest in FDs with different maturities to manage reinvestment risks. Consider highly-rated, short-term debt funds, FMPs and liquid funds for more tax-efficient returns. Stick to only highest rated non-bank debt be it NCDs or FDs with financial pressures continuing on the private sector.

Inflation, loans and fixed deposit rates. A major reason for the stubborn high inflation has been rising food prices. A below-par monsoon is unlikely to help change that. It could even force RBI to contemplate increasing the policy rates. Supply constraints, be it shortage of roads, ports, power generation capabilities, essential raw materials like coal to power plants, quality hospitals, skilled manpower like doctors, and so on, major sources of the present inflation, can't get sorted out overnight. This will require time and help from the new government in terms of policies and their execution. "We expect inflation for 2014-15 to be at 8 per cent," says Dharmakriti Joshi, chief economist, Crisil. So, expect continuance or even a small increase in home, car and other loan costs. Term deposits and other fixed income paper are likely to continue offering high returns, but when adjusted for inflation, will give negative returns as in the recent past.

The stock market. "If we see a stable government, the euphoria might see the Nifty crossing 7,000 levels; with a fractured mandate, we may see a large selloff and the Nifty might go down by 6-8 per cent," says D.K. Aggarwal, chairman and managing director, SMC Investments & Advisors. As the stock market starts looking

"We expect a gradual trail-up in economic growth in the next few years"

DHARMAKRITI JOSHI

CHIEF ECONOMIST, CRISIL

"The investment cycle should pick up in 2015"
SONAL VARMA
EXECUTIVE DIRECTOR AND INDIA ECONOMIST, NOMURA

beyond the election results, it will start seeing many of the economic realities we have already listed. Experts also point to stretched valuations. Says Sunil Kewalramani, noted global equity advisor: "The markets have run well ahead of themselves. Most news has been baked in the cake." The situation could then become ripe for correction. Says Aggarwal, "We could see some kind of corrections adjusting to the real fundamentals before again taking off for a long-term bull run." That may not happen in a linear and seamless manner and there could be many air pockets due to bad news (see *Riding The Rough Seas*).

Real estate. "The last six months have displayed rather muted demand against the backdrop of a global financial slowdown, high interest rates, tight liquidity and large-scale debt," says Aakash Ohri, executive director, DLF Home Developers. That pretty much sums up the sentiment in this sector. Pankaj Srivastava, COO, Maitreya Realtors & Constructions, a Mumbai-based real estate company, adds: "End users are still buying in good projects." Anshuman Magazine, CMD, CBRE South Asia, provides a detailed picture: "The residential space is down. There are, however, sales happening in the mid-income category, especially where the developer is credible. Sales are low where the prices are inflated. On the commercial side, however, things are slow, but they are moving." Adds Sachin Sandhir, MD, RICS South Asia: "It is mostly the grade A office space that is in demand. Buyers in the residential space are looking at those projects nearing completion or have better appreciation prospects." Of course, there are exceptions. Says Kamal Khetan, CMD, Sunteck Realty, a Mumbai-based realty firm: "We have witnessed one of the best sales in recent months."

The realty sector is facing both supply and absorption issues. Says Prashan Agarwal, co-founder, PropTiger, a realty portal: "In terms of supply there has been a 20 per cent drop in the fourth quarter (of FY14) compared to the third. There has also been a similar drop in terms of absorption." Builders are also adapting to the situation. "Earlier, when developers launched their projects, they used to market all the units in the project in one go, (but), of late, they are marketing the units in phases," says Aditya Verma, CEO, Makaan.com. So, it is hardly surprising that developers are still offering new projects at the price points that existed 6-9 months ago.

Gold. A stable mandate followed by positive economic initiatives by the new government should make investors move away from gold to equities, but, as we have mentioned, other developments could bring investors back to the security of gold from time to time. However, if the mandate is perceived to be less than stable, the likelihood of gold doing better improves substantially.

Is a stable government enough? Given some of the formidable realities, a stable political dispensation running the government will help, as would growth-friendly policies. The bulk of those indications and announcements are likely to be in the Union Budget in June or July. If these two things happen, it would take a quarter or two for them start showing results since many of them deal with supply-side issues. When that happens, the sentiments in the economy and the stock market would start improving, powering an upmove. A greater control over inflation through measures to address food prices would aid this further. This could mean a higher economic growth rate by mid-2015 and the RBI beginning to feel bold enough to cut rates. "The investment cycle should pick up in 2015," says Sonal Varma, executive director and India economist, Nomura. Many experts see the 8 per cent-plus growth rate of the past as history. Most of them and institutions talk about a growth rate in the range of 6-7 per cent in the medium term (2-4 years). "We expect a gradual trail-up in economic growth," says Crisil's Joshi.

With this emerging big picture, you will need to develop a game plan to not only align and adapt your

ACTION PLAN

EQUITIES

Book gains if your investments have run up. Sit out of any further run up. Don't panic if and when any correction happens (likely in June-July); it could be steep. Keep a hawk eye for such points, i.e., 20-25 per cent down from current levels, and then move in to hunt for bargains and invest, especially in capital goods and bank stocks. As inflation moderates over the next 18 months or so and economy slowly regains its mojo, keep investing in equities and highly rated diversified equity funds or even index funds to make significant gains. Don't mess with your SIPs.

ACTION PLAN

REAL ESTATE

HOME BUYING

If you can afford the down payment and the home loan (sum of all EMIs need to be less than 45 per cent of net income), go for it. Bargain hard as you could land up with a great buy as the builder could be desperate to sell. Opt for units that are ready to move into, or 70-80% complete

INVESTING

Wait and watch. Act only if policy measures, such as those announced in the Union Budget, appear to give a sustainable boost to sentiments

finances, but also adopt strategies to thrive. Here are our suggestions.

Jobs and pay. Since a job explosion is unlikely in the near future, job switches will need to be well considered with adequate due diligence on prospective employers, your prospects and role. It is important to have realistic pay hike expectations and also look for lateral growth opportunities in the existing organization, besides investing in core skills by enrolling in mid-career and other programmes. "The increment levels this year are almost at the same levels as last year," says P. Thiruvengadam, senior director, Deloitte in India.

Fixed income. With the interest rates being offered by fixed deposits fairly high, it would be good to lock into them at these levels. Invest in FDs with different maturities to manage reinvestment risks. Consider highly-rated, short-term debt funds, FMPs and liquid funds as well for more tax-efficient returns. For non-bank debt paper, stick only to the highest-rated NCDs or FDs.

Equities. Book gains if you can if your equity investments have run up. Sit out of any further run up since there is likely to be turbulence ahead. Don't panic if and when any correction happens (likely in June-July); it could be steep. Keep a hawk eye for times of steep corrections say, 20-25 per cent down from current levels. These are opportune moments to hunt for bargains and invest, especially in capital goods and bank stocks. Says Gaurav Mehta, vice-president, institutional equities, Ambit Capital: "Look for quality cyclical and defensive stocks and avoid the ones with low return on capital employed (ROCE) and high beta."

As a mutual fund investor, stick to the asset mix you had. You don't have to do anything special or risky now. Says Sankaran Naren, chief investment officer, equity, ICICI Prudential AMC: "Infrastructure funds could be a good play provided certain conditions, such as the cost of capital (interest rates) should mellow down a bit, which RBI is targeting." Otherwise, sticking to your existing index funds, exchange-traded funds, or even highly-rated diversified equity funds will work too.

Real estate. If you plan to buy a home, do so if you can

"Infrastructure funds could be a good play provided certain conditions, like the cost of capital (interest rates), mellow down a bit."

SANKARAN NAREN

CHIEF INVESTMENT OFFICER, EQUITY, ICICI PRUDENTIAL AMC

RIDING THE ROUGH SEAS

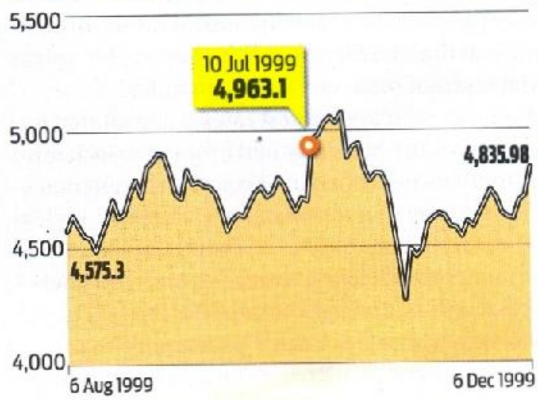
Do stock markets run around like wild horses as a country approaches elections? Evidence suggests that they do. In 2009, in India, the stock market gained 17.33 per cent, while there was panic in 2004 when it tanked by 16 per cent. The run-up in the months leading up to the 2014 Lok Sabha elections has been attributed to foreign institutional investors pumping in money in the hope of a better policy environment after the polls. But some analysts point to the improvement of India's fiscal position (through steps such as diesel price hikes) and improvement in external finances (such as lower current account deficit) that also strengthened the rupee and made India attractive to FIIs. So, what should you do this time? Our answer: Nothing. Wait for things to subside.

What to expect. Sunil Kewalramani, CIO, Global Money Investor, feels that in the days before the declaration of election results on 16 May there could be some correction as some investors would start doubting the strength of the current upmove. If a decisive verdict occurs, expect an euphoric phase of 7-10 days. This is likely to be followed by a correction as the harsh domestic realities dawn on investors. If there is a sharp correction, of, say, 20-25 per cent, hunt for bargains.

For bravehearts. For those of you who would you like to ride the rough seas, futures and options are the best bets. Says Siddarth Bhamre, head-equity derivatives and technical, Angel Broking: "The quantum of open interest is quite under control and is nowhere near the overbought zone." This means bullish strategies, such as the straddle and strangle, can be used. Protective puts can be used to hedge your portfolio if your stocks have run up by the time of the results. Selling calls against portfolio and synthetic long calls are other strategies to use. If you want to reduce the cost of hedging, use futures. Says Bhamre, "Futures can be shorted to hedge a portfolio. The quantum of short is dependent on the beta of the portfolio. There is no cost of hedging here, but the price gets locked."

ELECTION 1998

ELECTION 1999



ELECTION 2004

ELECTION 2009

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afford it. There exists the usual caveats of a thorough research of the property and the builder and your affordability of the down payment and home loan EMIs (the sum of all EMIs need to be less than 45 per cent of net income). Don't forget to bargain hard as you might just land up with a great deal just in case the builder is desperate to reduce inventory. Ensure that you zero down on a residential unit that is either ready to move in or is 70-80 per cent complete so that you are not hit too badly by project delays. If you are looking to invest or sell your investments, watch for a quarter to get an idea of market sentiments and government policies.

Gold. Stay invested in gold if you already have such investments. If the yellow metal runs up briskly in the next 3-4 months, especially due to news of some adverse international or domestic developments, you could even consider booking some gains after taking into account taxation aspects, keeping the gains parked in liquid funds till new investment opportunities arise. Banish the thought of making quick gains.

Clearly, the declaration of election results and the formation of the new Union government would be just another episode that you encounter in the normal course. So, cut through the noise and the fog and you will find yourself holding cruising speed in the months ahead despite the air pockets.

ACTION PLAN

GOLD

Do not sell off gold if you have already invested in it. If the yellow metal runs up briskly in the next 3-4 months, you could even consider booking some gains after taking into account taxation aspects and keep the gains parked in liquid funds till new investment opportunities arise. Banish the thought of making quick gains from new investments

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