PINC

May 2022

Market Commentary

PIONEER WEALTH MANAGEMENT

The Markets have been volatile this week as Central Bankers in India and the US handed down rate hikes to curb high inflation. In a surprise announcement on Wednesday (4th May), the Reserve Bank of India (RBI) increased the repo rate by 40 bps to 4.4% (still a historically low rate for the Indian economy). On the same day the US Federal Reserve also did a planned rate hike of 50 bps. With the result season in play, investors will be looking at the impact of these factors - rising rates, inflation - on company financials and guidance.

Usually, such sharp rate hikes evoke negative reactions from investors, given that it could slow the pace of growth. This time around, financial markets are celebrating the clarity among central bankers across the globe to shift focus from backing growth to controlling inflation. Economists feel that the shift in stance was necessary. In India, both wholesale and consumer prices are showing no signs of cooling off, while in the US, inflation hit the highest level in 40 years. Further, Fed Chair Jerome Powell's guidance of a possible 50 bps hike in the next two meets calmed markets as it puts to rest speculation of a 75 bps rate hike.

Even so, the puzzling question is what has changed so suddenly to warrant steady rate hikes? Significant contributor may be the Purchasing Managers Index (PMI) data for both manufacturing and services show private sector activity expanded at the fastest pace in five months in April, which adds to inflationary pressures. In the US too, the labour market remains extremely tight, which is feeding into wage inflation. Besides the US and India, most countries are on a rate-hike path -- the United Kingdom, Korea and Brazil, to name a few.

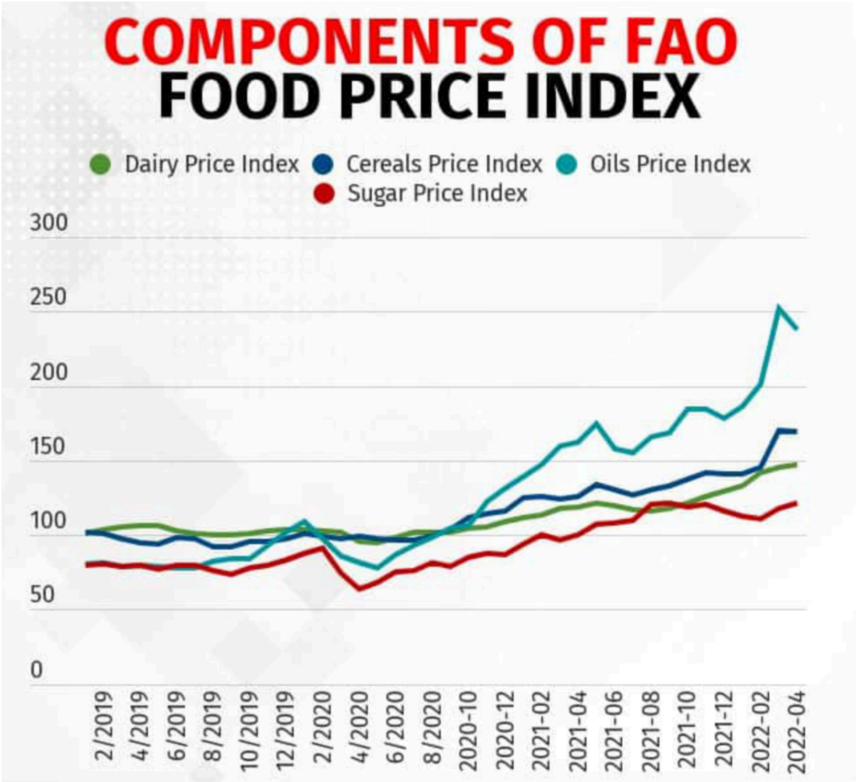
Investors appear to have been appeased by global central bankers' decision to rein in inflation. Perhaps, since there's little that the banks can do to control supply-side shocks due to COVID-19 restrictions and the Russia-Ukraine war, this is one way of striking a demand-supply balance, without slipping into a recession.

Moreover, The runaway trend in global food prices was tripped in April, a welcome relief for those worried by inflation, including central banks, governments and consumers. And, investors, of course. While there's no telling if prices will resume their upward journey, April's dip offers some hope of a cooling down.

The April print of FAO Food Price index declined by 0.8 percent sequentially, attributed to declines in the prices of edible oil and cereals while the other categories reported quite moderate increases, said the FAO statement. Edible oil prices have been a chief driver of food inflation. Their prices dipped in April because of a 'weakening demand outlook' from China, where lockdowns to control the spread of COVID-19 have hit activity. Curtailment of demand due to higher prices played a role too.

Sugar prices have sustained their recent increase, mainly due to higher ethanol prices and strengthening of the Brazilian real against the US dollar. Domestic food inflation, however, shows a spike in the prices of wheat due to a combination of rising global prices, higher exports and expectations of a lower crop yield due to the heatwave. But the price increases in pulses and some edible oils are much lower due to a high base effect, although soya and palm continue to show gains of around 20 percent over a year ago. Potato and tomato prices too are showing a sharp increase over a year ago.

But what's next for equity markets? With monetary policy tightening and rate hikes becoming a certainty, the impact on earnings is what markets would keep a close watch on. For now, there aren't many reasons for sharp downgrades. Demand is rising on a low base, so are corporate revenues. The concern on margins, albeit real at this juncture, may not worsen from here on.


COMPONENTS OF FAO
FOOD PRICE INDEX
Dairy Price Index
Cereals Price Index
Oils Price Index
Sugar Price Index
300
250
200
150
100
50
0
2/2019
4/2019
6/2019
8/2019
10/2019
12/2019
2/2020
4/2020
6/2020
8/2020
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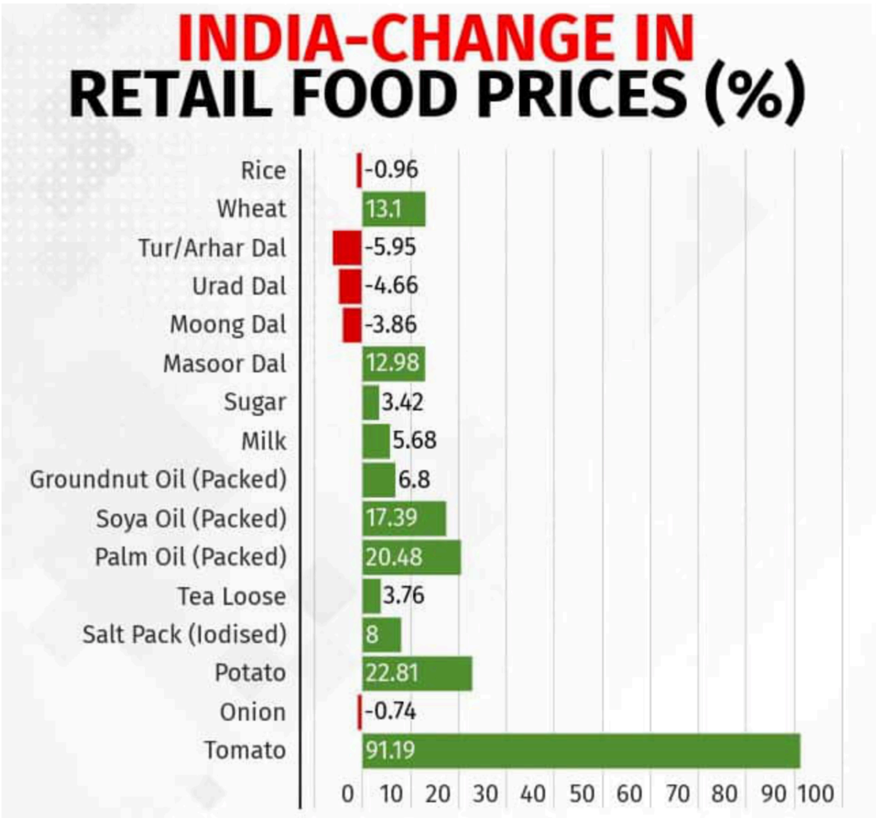
INDIA-CHANGE IN
RETAIL FOOD PRICES (%)
Rice -0.96
Wheat 13.1
Tur/Arhar Dal -5.95
Urad Dal -4.66
Moong Dal -3.86
Masoor Dal 12.98
Sugar 3.42
Milk 5.68
Groundnut Oil (Packed) 6.8
Soya Oil (Packed) 17.39
Palm Oil (Packed) 20.48
Tea Loose 3.76
Salt Pack (Iodised) 8
Potato 22.81
Onion -0.74
Tomato 91.19
0
10
20
30
40
50
60
70
80
90
100