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ANNUAL OUTLOOK

2025

EQUITIES OUTLOOK

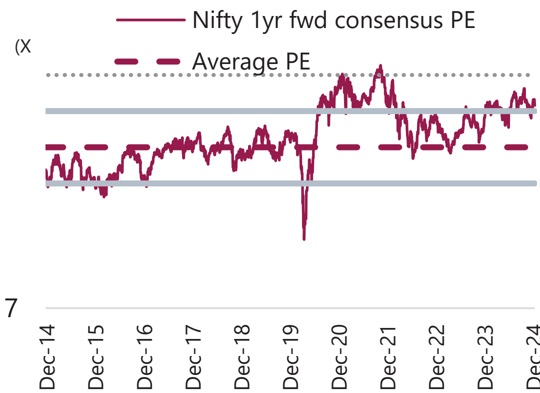
2025 – A year of tempered expectations

As we look ahead to 2025, several key factors are likely to drive global markets. The incoming US government in January 2025 and its policies will play a significant role in setting the global market tone. Additionally, the monetary policies of central banks and slowing global growth will be crucial. The imposition of tariffs by the US could lead to higher inflation, and any rate cuts might be modest. The US economic growth is expected to remain strong while Europe's growth may remain sluggish, with central banks shifting their focus from high inflation to low growth. Japan might raise interest rates throughout the year, with its economy continuing to normalize and experiencing better-than-expected growth. China could face challenges from tariffs, and any countermeasures will need to be monitored but China may continue with stimulus measures.

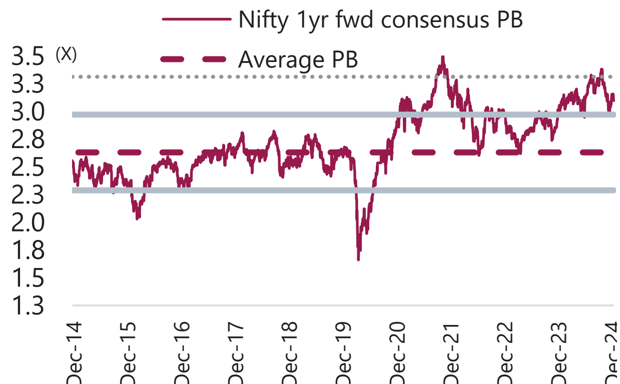
In India, 2024 was a year of optimism albeit for most of the year, but 2025 may bring more tempered expectations. We expect growth to remain moderate, given the fiscal consolidation and slower credit growth. Many segments of the economy are showing signs of a slowdown given the higher base and this has translated into weaker corporate earnings. Companies have seen superior earning growth led by margin improvement, strong recovery post Covid, along with government spending and policy actions. We believe factors like margin improvement may not continue for long, however continuation of prudent capital allocation policy by government to boost both capex and consumption, may drive earnings recovery. The strength of the US dollar coupled with stimulus measures in China have led to foreign fund outflows. However, these have been counterbalanced by the robust domestic fund inflows. Nonetheless, India remains one of the fastest-growing economies globally. The tariffs on China and other countries proposed by US President-elect could significantly impact global trade. However, during his first term, the tariffs on China benefited India, and this time, India might again be able to turn these trade restrictions into an opportunity.

It is pertinent to note that we begin 2025 after the strong rallies of 2023 and 2024, and elevated valuations thereof. Key events have caused volatility and rallies in equities. While our economy has been on a strong footing so far, equities are off the all-time highs and have seen a correction in the last three months. Tet valuations remain elevated. Going forward market performance could be influenced by earnings growth and absolute valuations. Given near-term growth challenges, likely muted foreign institutional investor (FII) inflows, and subdued earnings expectations, significant valuation expansion seems unlikely. We expect 2025 to be a year of stock picking across market caps. The recent corrections in mid and small caps could present opportunities to increase exposure to select stocks.

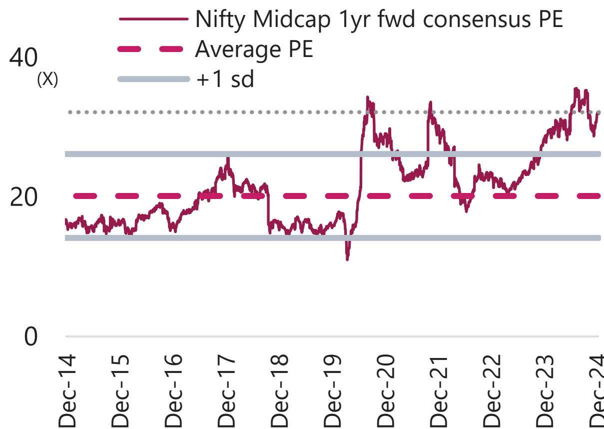
Nifty 1yr fwd PE at 20.3x - above +1 SD



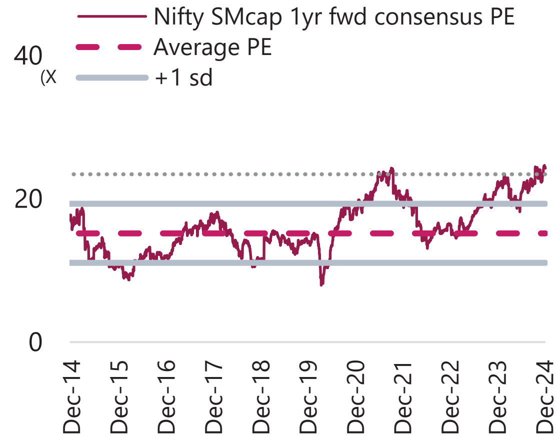
Nifty 1yr fwd PB at 3.1x - above +1 SD



Nifty Midcap 1yr fwd PE at 32x - closer to +2SD



Nifty Smallcap 1yr fwd PE at 24.3x - above +2SD



Source: Jefferies

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Over the long term, market returns generally align with nominal GDP growth, and we expect this trend to persist. After significant outperformance in sectors such as real estate, pharma, IT, auto, and capital goods, these sectors might see some consolidation in the near term. These have been the sectors with higher earnings growth and higher valuations than their pre-COVID levels. In contrast, sectors with relatively lower earnings growth, such as FMCG, lenders, energy, and metals, are not as expensive compared to their pre-COVID valuations. In the past three years, mid and small caps have been viewed as expensive but have demonstrated superior growth compared to large caps, leading to their outperformance. However, the substantial valuation gap caused by the underperformance of large caps relative to mid and small caps makes it essential to focus on absolute growth rather than absolute valuations in both segments. Consequently, the market is likely to become more stock-specific and we anticipate that high-valuation sectors may consolidate in the near term if they lack new earnings growth drivers. Nonetheless, we continue to find opportunities across the market.

Key themes in 2025 and in our portfolios

We believe that markets are gravitating towards companies with clear earnings growth visibility and a lower likelihood of significant earnings downgrades. Accordingly we believe the themes in 2025 are likely to be split into two halves.

For the first half of 2025, key themes to watch include sectors such as Information Technology, Pharma, Quick Commerce, Capital Market beneficiaries, Travel/Tourism, Renewable Capex, Power Transmission & Distribution, EMS, Defense, and select Auto companies with new product launches on the horizon. However, many of these sectors currently have high valuations.

We have seen that among all sectors, the capital goods sector has demonstrated strong earnings growth across various macroeconomic scenarios over the past three years. This has led to its outperformance and overvaluation, which peaked around May 2024. Following this peak, the sector began to consolidate. Nonetheless, the relative growth in the capital goods sector remains superior to other sectors, while some segments of the consumption part of economy have deteriorated recently. Consequently, after the consolidation, markets have shifted focus back to the capital goods sector. The demand is being driven by renewable power and the associated need to strengthen power transmission and distribution. Additionally, there has been an improvement in defense sector order announcements in recent months, and growth in electronics manufacturing services remains strong. Overall, we expect select capex and PSU companies to continue performing well in 2025.

The auto sector experienced strong growth post-Covid, but it began to slow down in mid-2024. Notably, two-wheelers and LCV/MHCV have shown signs of a slowdown, with sales volumes just reaching pre-Covid peaks. In contrast, growth in the 4W and tractor segments remains robust. We expect the winners in 2025 can be companies with favorable new product launch cycles, as the overall industry is showing tepid growth.

The pharmaceutical sector witnessed a strong year, with stock returns driven by a combination of earnings upgrades and valuation re-ratings. The Contract Research, Development, and Manufacturing Organizations (CRDMOs) sector experienced significant re-rating due to tailwinds from discussions around the US Biosecure Act. If implemented, this act would position Indian CRDMO companies at the forefront of research and development outsourcing opportunities. We can anticipate stable earnings growth for domestic pharmaceutical and hospital companies, while some US generic-focused and CRDMO companies would need to enhance their business development and execution to improve earnings growth visibility.

The Indian IT services industry is poised for a rebound in 2025 from the recent slowdown. This recovery is expected to be driven by improved hiring, a stronger US BFSI sector, and potential positive policy changes with the US president elect victory, such as lower taxes, healthcare regulation, and a neutral stance on H1B visas. Additionally, the transition of AI from hardware to software services, along with increased IT budgets across various industries and the expansion of IT budgets into core operating budgets, should further support growth and create a favorable deal environment for IT services companies. However, while growth in large caps has been trending towards single digits, select midcaps may offer double-digit growth potential on a year-over-year basis.

By the second half of 2025, markets may shift focus to potential triggers in underperforming sectors such as Lenders, FMCG, and IT. We can anticipate that FMCG sector revenue growth will accelerate to high single digits in FY26E, compared to mid-single digits in FY25E. This improvement will be driven by a low base, a recovery in urban demand trends, and a return to pricing-led growth. We expect volumes to recover to mid-single digits, with pricing increasing to low- to mid-single digits.

Risks to our view:

Rising geopolitical tensions hinder the free flow of goods, services, capital, and manpower, distorting demand and supply dynamics and leading to imported inflation and a weak currency. This type of inflation, driven by factors such as commodity prices and tariffs, poses a significant risk. However, when it comes to inflation in domestic commodities like food or services, investors can often find opportunities among the beneficiaries.

Another factor that can add pressure on equities is the supply – Earlier this year, we brought out two Acumen talking about Supply -- “Let’s talk about Supply too” and “Domestic flows – Necessary but no longer sufficient”. In both the series, we spoke about the increasing supply that is outpacing demand.

IPO pipeline for 2H is nearly 3x the amount raised in 1H with 91 companies looking to list and in aggregate raise US$17 bn. Another 70 listed companies in recent weeks have taken board approvals to raise in aggregate US$16 bn of equity through Qualified Institutional Placements (QIPs). Secondary stake sales from promoters and private equity are also only likely to grow larger given the expiring lock-ins and elevated trading multiples in the market.

Assuming secondary sales (by promoters and PEs) at US$22 bn in 2H stays similar to what we have seen in first half, the total supply will rise to US$55 bn in the second half of the year or about 2.5x the estimated inflows in MFs. Ensuring that equity supply will overwhelm domestic fund flows and market direction will again be subject to vagaries of foreign flows.

2HFY25 Pipeline is 2x that of 1HFY25

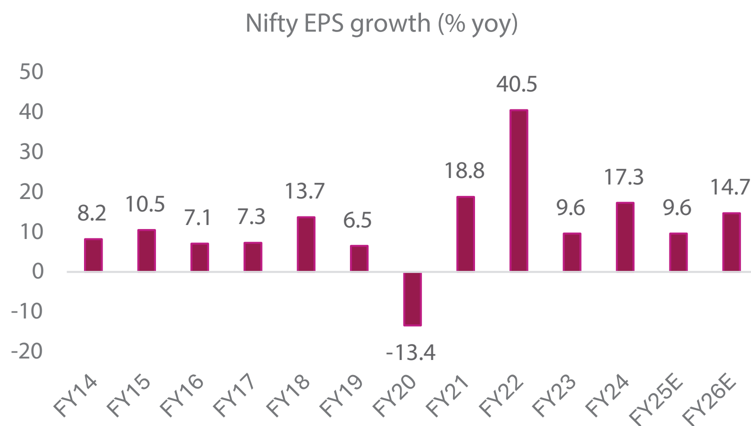
Source: Kotak Securities, Axis MF internal research , Figures in Rs Cr

This magnitude of equity raises possibilities of the private investment cycle gathering pace and unlike the past cycles this would be more equity funded rather than debt fueled. Of the US$39 bn raised by corporates (IPOs/QIPs), in the past 18 months US$25bn was primary capital. 2HFY25 pipeline indicates another US$24 bn of investible capital being potentially available for capex, acquisitions and other purposes. The breadth of companies looking for capital is wide. The power sector (US$4.7 bn) and real estate (US$4.1 bn) stand out with largest capital raises each planned for this year. Services companies (IT, Logistics) at US$2.3 bn, Retail (Q-commerce, FMCG) US$2.9 bn, Healthcare at US$2.3 bn, metals at US$2.2 bn and auto at US$3.1 bn are other sectors witnessing material capital raises.

Weak earnings reflect slowing growth

The July-September results season was muted and disappointing in many aspects as both topline and bottomline earnings growth was visibly under pressure. The quarter saw a slowdown across all three major economic pillars - consumption, capex and exports – leading to a broad-based impact on the overall earnings.

We believe corporate earnings can witness an uptick when government spending improves. Consequently, earnings growth will likely moderate to ~10% in FY25E due to the slowdown, but FY26E is expected to be better.



Source: Jefferies

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Recap of 2024

After a spectacular 2023 where Indian equities shared a remarkable performance and economic growth surpassed expectations, 2024 remained promising for most of the year against a backdrop of general elections and union budget. However, the journey wasn't without its challenges. Elevated valuations, indices hitting lifetime highs, disappointing earnings growth, and persistent geopolitical tensions cast a shadow on the markets, causing a dip in October and November. Despite these challenges, the year ended on a high note. Equities rallied and setting new records month after month.
The Sensex soared past the 85,000 mark, while the Nifty 50 crossed 26,000. By year's end, the BSE Sensex had climbed 8.9%, the Nifty 9.6%, the Nifty Midcap 100 an impressive 23.4%, and the Nifty Smallcap 100 surged 23.9%.

Market performance %

Index	%
Sensex	8.9
Nifty 50	9.6
Nifty Midcap 100	23.4
Nifty Smallcap 100	23.9
Nifty 500	15.5

Source: Bloomberg , Data for CY 2024

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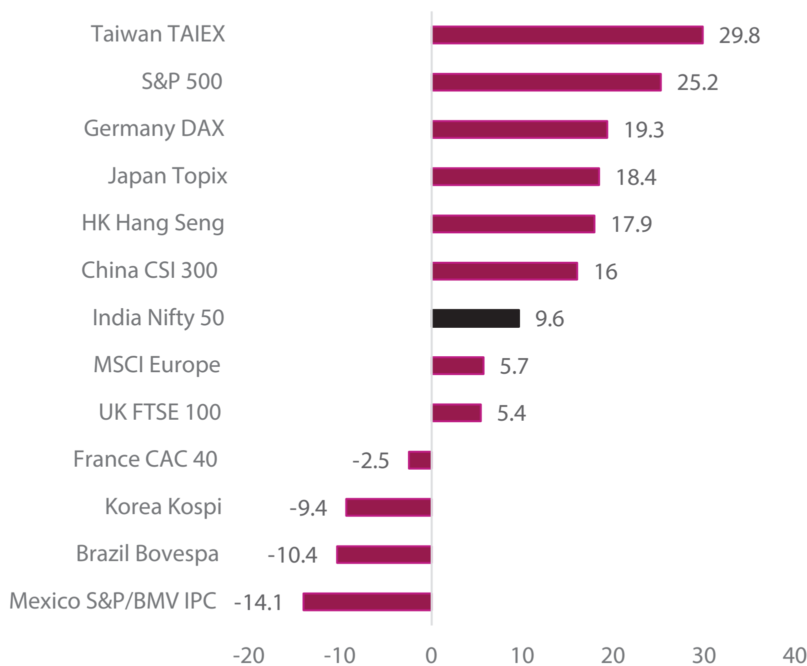
Globally, all countries participated in the year's rally of varying degrees in equities led by the best performing markets of 2023 - the US and Taiwan. Brazil and Mexico were the most impacted countries over the year and were down by 24-25%. US equities, particularly the S&P 500 had a spectacular rise, making it one of the best performance in years, the upswing starting from October 2023 amid expectations of a Fed pivot and peaking inflation. Meanwhile the tech heavy Nasdaq rose 31%. Both the US and India have seen valuations at elevated levels relative to historical average. The US in particular saw PE expansion due to the superlative gains seen in mega cap tech companies.

Year to date returns, % in local currency



Source: Bloomberg

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The themes that drove markets in 2024 are as below

Prospects of political continuity and revival in reforms – the first half of 2024 rose on expectations of political continuity and a revival in reforms and changes

Strong economic growth - We remained one of the fastest growing economies in comparison to the West. However, that said, GDP growth has been slowing down in the last two quarters. In particular, Q2FY25 was disappointing, where a slowdown in investment activity as a result of elections led to weakening growth.

Better managed inflation regime – Inflation remained sticky but in control and the better-than-expected monsoon also helped tame food prices. However, the last quarter has seen inflation head up, much to the dismay of the central bank. The RBI expects it to fall back to the 4% target in the next couple of quarters. Based on the strong growth and higher inflation, expectations of lower interest rates were pushed back.

Disappointing earnings – The results season during the period was weaker than expected. A slowdown in the capex ahead of elections resulted in disappointing numbers in the last quarter.

Robust domestic inflows – Strong persistent inflows by DIIs (mutual funds in particular) have been one of the reasons for the strength in equities. Over the year, inflows totaled US$ 55bn while FII flows managed to be in the positive territory aggregating US$ 1.3 bn.

While these were the domestic factors at play, the global events that shaped the course of the markets were as below

Expectations of slowing growth in the US – These expectations carried forward into 2024 and the US Federal Reserve was the last one to cut interest rates in September amongst the Developed markets. Growth remained decent while macro indicators did show tepid numbers.

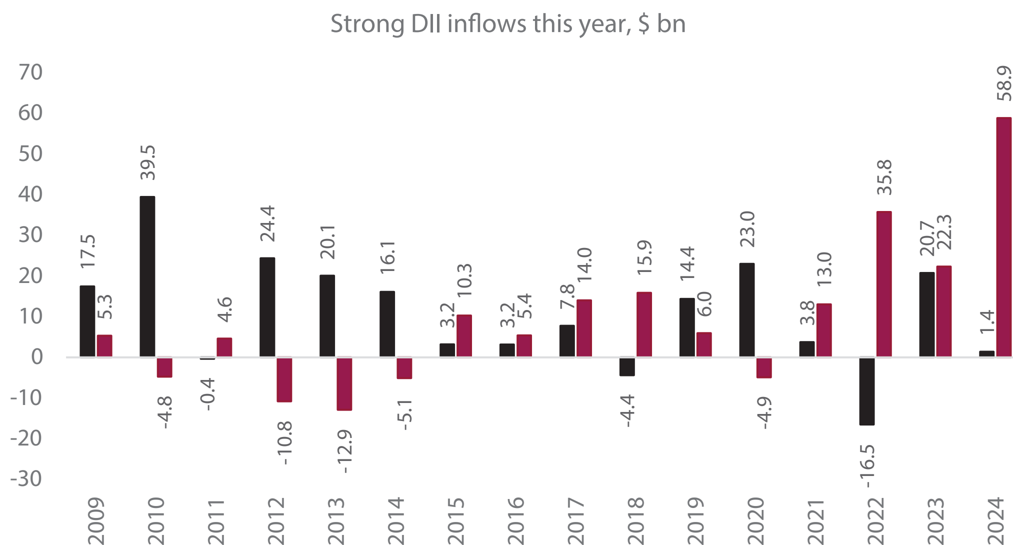
Geopolitical conflicts – The unexpected crisis between Israel Hamas intensified leading to volatility in markets and the further escalation did impact global crude and commodity prices

US elections – Election of the new President buoyed US equities but caused some reactions globally. Expectations of trade tariffs, higher inflationary pressures and a slower pace of rate cuts have been gaining ground once he assumes office in January 2025.

Lower interest rates – The Developed economies adjusted to slowing growth and trimmed rates during the course. The European Central Bank, the Bank of England, Swiss National Bank, Bank of Canada and Australian National Bank all lowered rates followed by the Fed. Interestingly, the Asian economies haven't still lowered rates. The Bank of Japan was the one to raise interest rates while China announced stimulus measures to bring back growth.

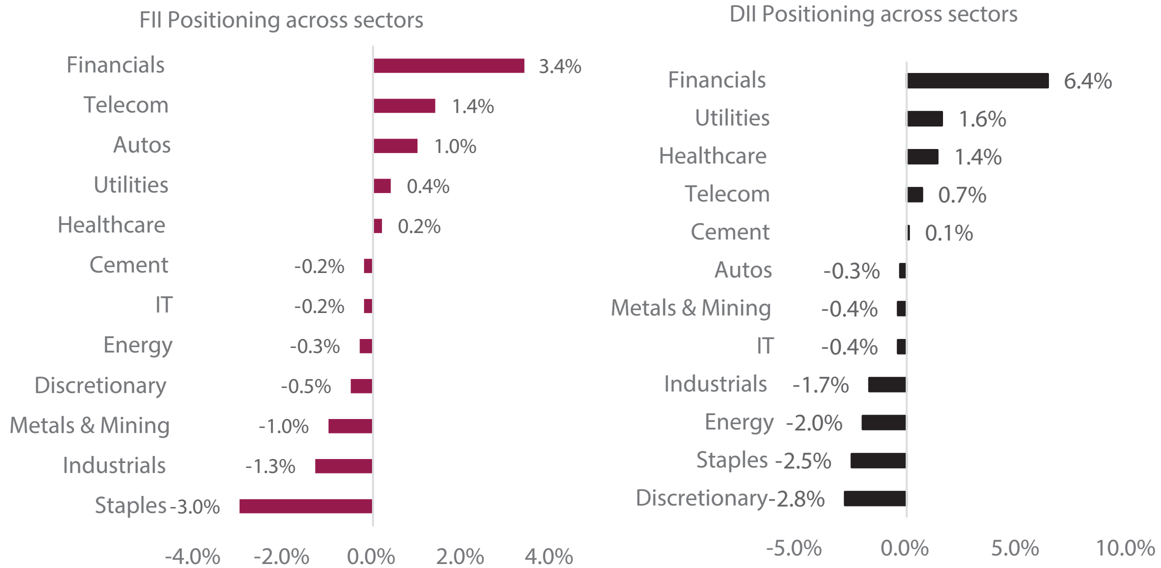
Domestic flows counterbalance FPI flows

After robust inflows of US$20.7 bn in 2023, Foreign Portfolio Investors (FPIs) adopted a cautious stance in 2024, riding a financial seesaw. As election season approached, they pulled back, resulting in a US$4 bn outflows. However, post-election optimism from June to September saw a resurgence, with inflows reaching US$14 bn. This optimism was short-lived, as October and November witnessed another retreat, with outflows totaling US$13.5 bn. Despite the volatility, FPI flows managed to stay just above water, ending the year with a modest net positive of US$1.4 bn. In contrast, Domestic Institutional Investors (DIIs) played the perfect counterbalance to the FPIs, consistently adding inflows each month. The October-November outflows from FPIs were countered by a substantial US$18 bn inflows from DIIs. By the end of the year, DIIs had amassed a total of US$59 bn in inflows.



Source: NSDL, Kotak Institutional Securities

FII and DII positioning

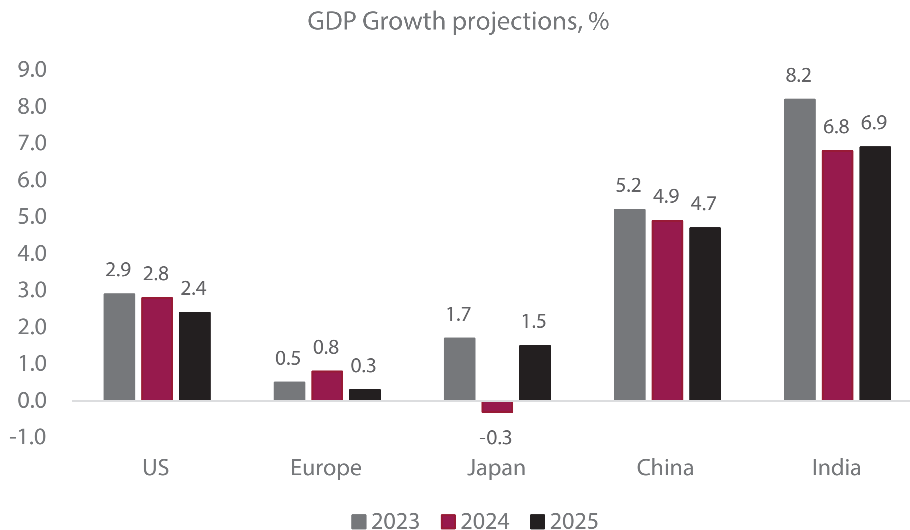


Source: BofA

The FPI outflows from India against a backdrop of valuations and redirection into other economies suggests lower risk from here due to India's relative positioning in FPI portfolios being at its lowest in over a decade. Furthermore, strong domestic flows in recent years have brought DII shareholding to levels comparable with FPIs. In addition . In addition, the rise of India's weight in MSCI indices could make important for global funds to own stocks in the country.

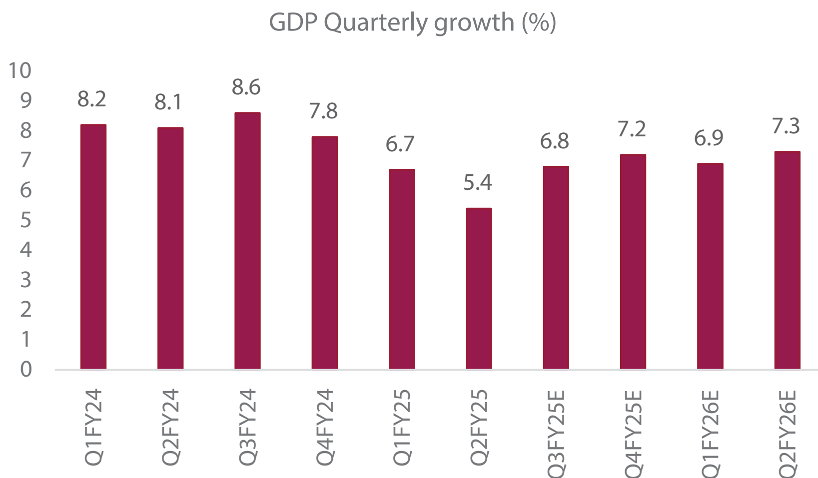
Global growth - still not as slow as expected to be

Global growth surpassed expectations in 2024 too although one can now really witness the pace of slowdown as indicated by macro data across economies. Data releases in the US point to a real slow pace of slowdown. In contrast, India stood out stronger maintaining its growth momentum and positioning itself as one of the fastest growing economies. However, the last quarter data has put India in a tight spot, and one hopes this is an aberration and growth could bounce back in the next few quarters. Economic activity levels slowed in 2024 due to a combination of factors. The elections in Q2CY24 led to reduced government spending. Additionally, a regulatory-driven slowdown in credit growth impacted both economic growth and consumption.



Source: OECD

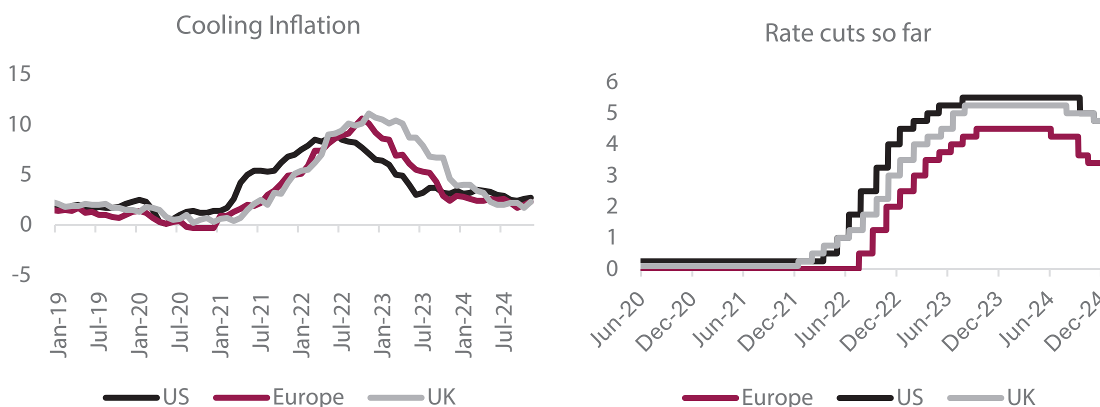
The slowdown in GDP growth is expected to reverse over the next few quarters as govt. spending picks up, and drag from credit growth contraction is behind us



Source: Bloomberg, RBI projections

Global inflation and central bank responses

Inflationary pressures did cool down paving the way for easing monetary policy. Geopolitics did play spoilsport to crude oil prices and commodities over the year. Central banks of the developed markets started easing rates, with the ECB being the first. The US has lowered rates by 100 bps so far this year and we expect another 50-75 bps of rate cuts.



Source: Bloomberg

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In India, inflationary pressures rose in the latter part of the year driven by higher food prices. Throughout the year, the central bank stayed unchanged on its interest rate stance but moved into a neutral stance in October and lowered CRR by 50 bps which could help ease banking liquidity by Rs 1,16,000 cr.

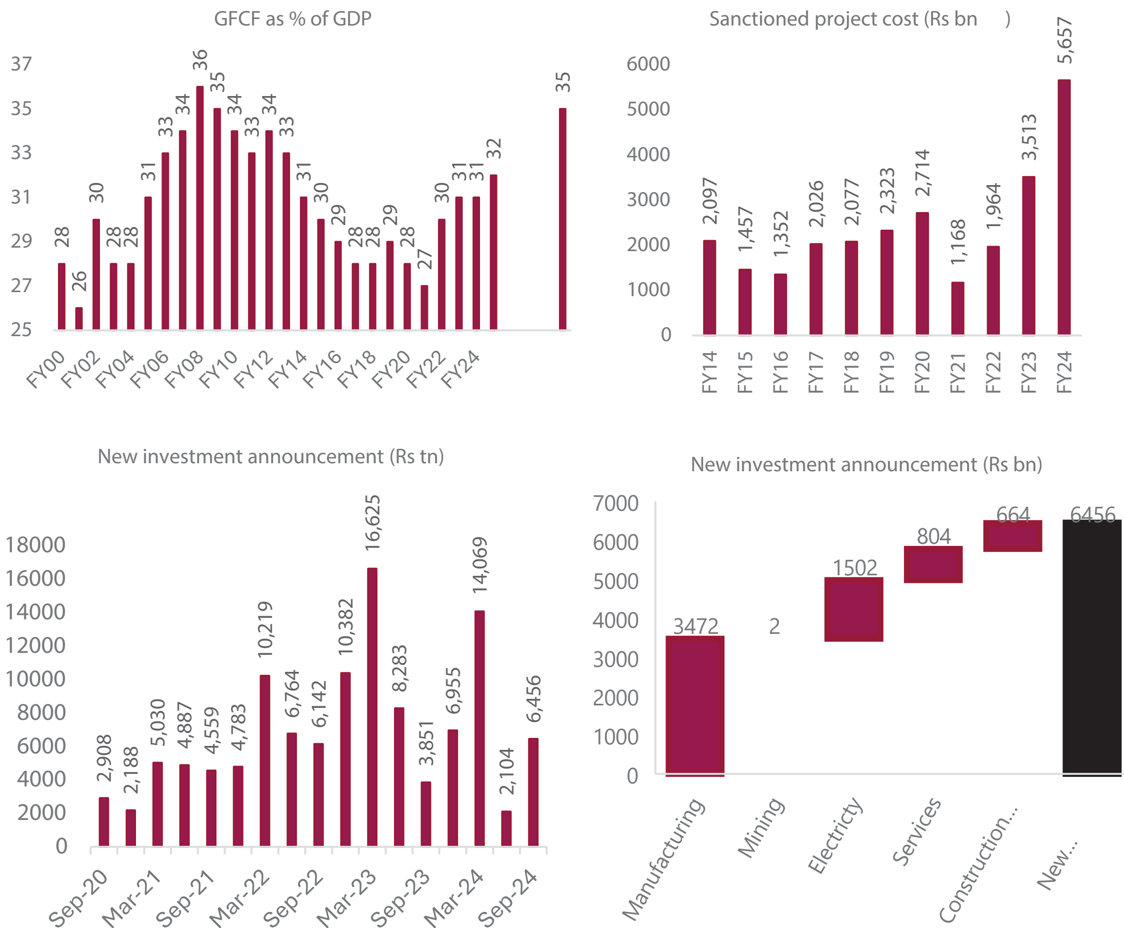
Capex cycle slowed in 2024

Capex (or GFCF) growth has slowed from 9.0% in FY24 to 6.8% in 1HFY25, largely driven by a 15% YoY contraction in govt. capex spending in 1H. We expect capex to gain momentum in 2HFY25, mainly led

by the Centre. However, Central Government capex may not meet its FY25 target of Rs.11.1tn, as it requires a Rs.1.2tn monthly capex run rate to achieve this target.

The housing market remains robust, with inventories at their lowest in 14 years. Private corporate capex is also on the rise, driven by strong corporate balance sheets and opportunities in sectors such as power, electrification, Production Linked Incentive (PLI) schemes, and building materials. According to RBI data, there is a significant investment intention for the coming years, with private capex approved by banks increasing by 60% year-on-year in FY24. This growth is fueled by multiple factors, including the participation of new industries. The PLI scheme has notably boosted smartphone production by global companies, which in turn has attracted investments in other sectors. Over the past 18 months, India has seen $20 billion in investments announced for five semiconductor facilities, leading to substantial supply chain investments. In the housing sector, new pre-sales have surged by over 50% in the past three years, translating into a construction boom that benefits a wide range of industries, including building materials, electricals, cement, and tile companies.

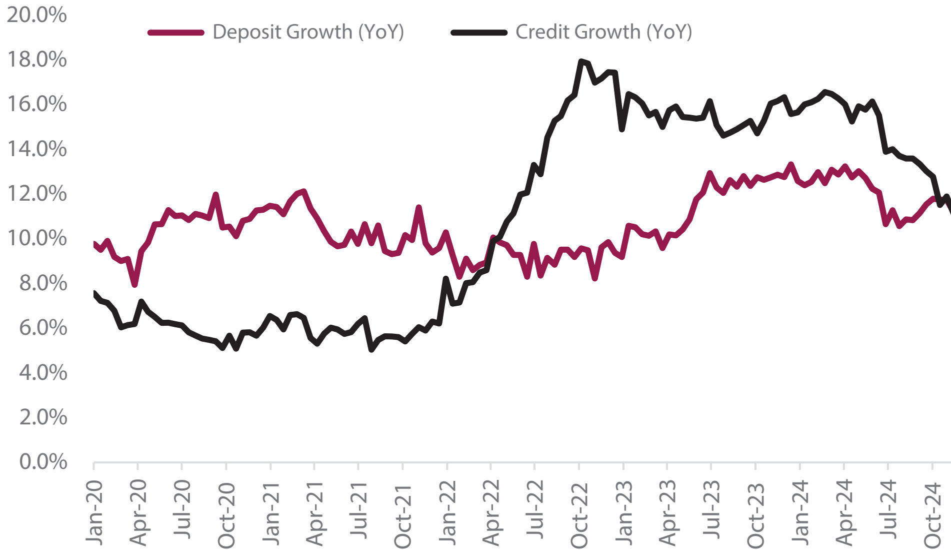
India in a capex upcycle



Source: Avendus Spark, Axis Capital

Bank credit

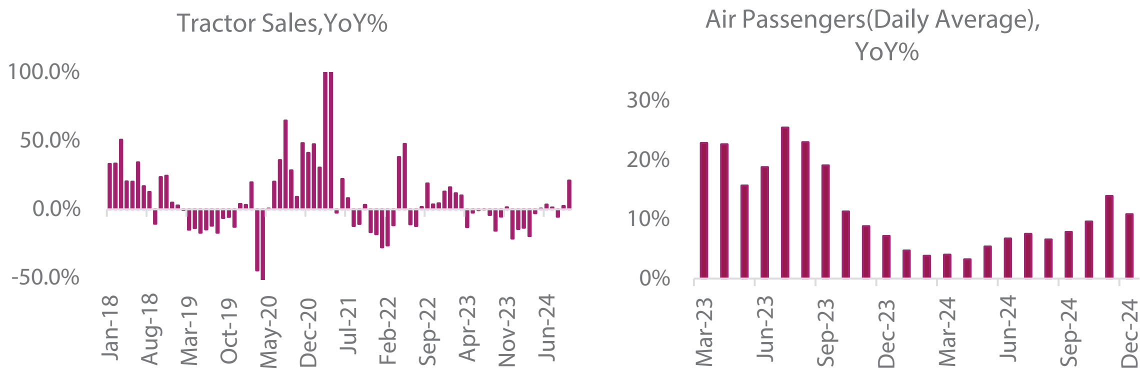
The RBI identified the significant gap between deposit and bank credit growth as a systemic risk and subsequently tightened lending standards for personal loans and NBFCs. As a result, credit growth decreased from 16.5% in March 2024 to 11.2% by November 2024, with personal loan growth also declining by 5% during the same period. However, with the convergence of bank credit and deposit growth, further contraction is unlikely. This convergence is a positive indicator for growth and bank earnings.



Source: RBI

Consumption

We have seen that the premium segments of all consumption categories are faring better than the mass segments. This is happening across auto, FMCG, real estate, electrical goods, travel, and alcoholic beverages. We do believe that the premiumization theme will continue but also expect rural demand to pick up going forward.



Source: Morgan Stanley

FIXED INCOME OUTLOOK

2025 will be the year of Opportunity

In 2025, we anticipate several key themes to unfold: (a) US President Elect's America First policies to lead to stronger growth (b) slowing growth in the rest of the world, (c) weakness in China on account of tariffs measures imposed by the US (d) lower growth in India leading to rate cuts, and (e) tight liquidity conditions in India for most of the year unless the central bank intervenes or India benefits from forex inflows. To address these themes, we believe the central bank will cut rates by 50 basis points and that the RBI will employ additional liquidity tools such as OMO purchases, swap facilities, and VRR. Despite strong growth, we expect US inflation to settle at 2.5-2.8% and the Us Federal Reserve (Fed) to lower rates by 50-75 bps in 2025.

Macro Outlook 2025

US: The return of President elect introduces a new dimension to the US economy and the Fed policy. US growth is currently supported by strong fiscal spending, and the healthier balance sheets of corporates have also bolstered growth. His 'America First' policies include pledges to impose tariffs on imports and restrict immigration. He aims to increase domestic manufacturing capacity and make the US an attractive investment destination by imposing tariffs on imports from China and other countries.

We believe that in the near term, such measures could lead to higher inflation in the US as imports become more expensive, while potentially harming growth in export-driven economies like China and Germany. We expect a wider fiscal deficit and a strong US dollar. In addition, Fed Chair Jerome Powell has indicated that the central bank is not in a hurry to lower rates given the economy's strength. Overall, we expect lower interest rates of 50-75 bps in this interest rate cycle, inflation in the range of 2.5-2.8% and growth at 3%.

China: The world is in a wait and watch mode as far as China is concerned. On the one hand, the government unveiled a comprehensive debt restructuring plan, which we believe could modestly boost growth and have potential for further fiscal expansion. On the other hand, China would be impacted by the US President Elect's trade tariffs. This could have a negative impact on the country, particularly exports which have been a key driver of growth. Furthermore, one can expect the currency to weaken against the US dollar. We believe that during the course of the year, the government could further bring out stimulus measures aimed at stabilizing the property market, increasing investment, and possibly measures to stimulate consumption. The government's stabilization efforts announced in September were well received by markets spurring a rally in Chinese equities. However, for consumption to rebound the government may need a larger stimulus. We expect the People's Bank of China to lower interest rates during the course of the year. But while this would boost domestic demand, the currency could weaken.

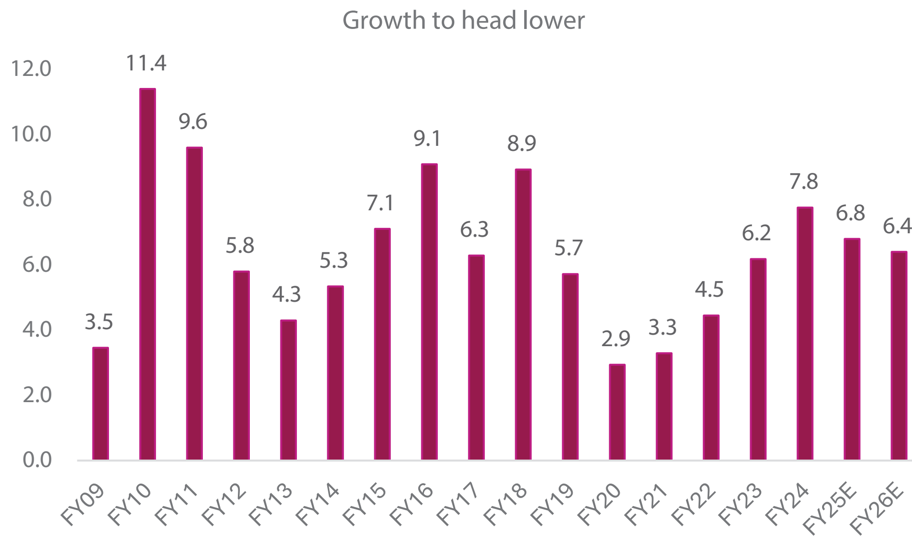
Commodities: 2024 was favorable for precious metals, with gold reaching record highs. We anticipate global oil prices to remain low, and although industrial metals began the year strongly, their rally eventually faded. Looking forward, we expect commodities to remain subdued. Additionally, actions taken by China and escalating geopolitical conflicts could influence commodity prices.

Rest of the world: A lot depends on the US policies that could impact countries to varying degrees. In Europe and the UK, we expect the focus to remain on growth and the central banks to follow further monetary policy easing. In contrast, headline inflation in Japan is expected to remain higher allowing the central bank of Japan to raise policy rates during the course of 2025.

Macro Outlook for India

We believe that fixed income markets will be in a sweet spot on account of various drivers as outlined below –

Growth: The three negative impulses for slower growth are (a) slowing credit growth, (b) fiscal consolidation (c) exports could be hit due to tariffs imposed by the US. However, we believe that growth could be in the range of 6.6% in FY25 and 6.25% in FY26. It is important to note here that the growth is coming off a high base and will still be positive and not expected to fall materially.



Source: Bloomberg, Axis MF Projections

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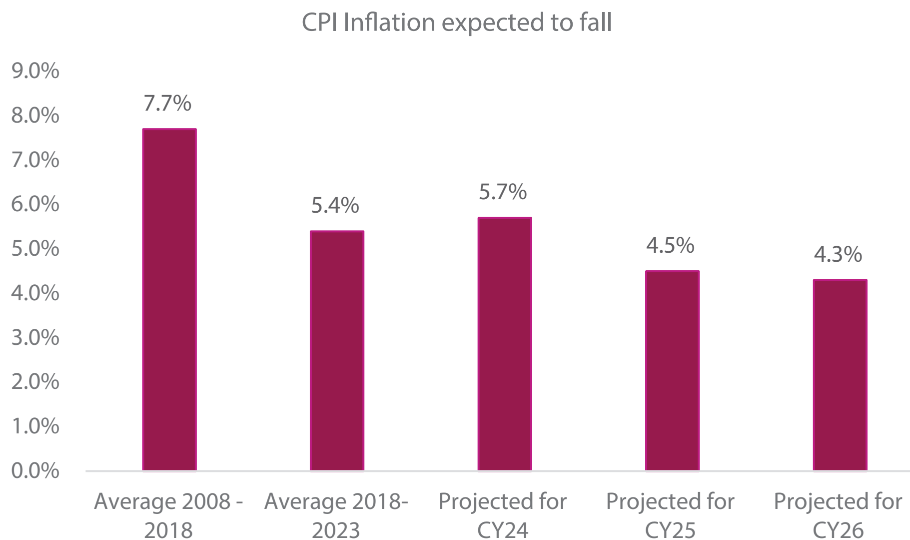
Inflation: Although headline inflation has seen near term rise, it will be in the 4.5% range next year while core inflation continues to remain below 4% for more than 12 months. We expect headline inflation to fall further on account of good harvest in both rabi and kharif crops and lower vegetables prices thereof. Core inflation can see some uptick on account of rupee depreciation. But weaker commodities and slower growth would not lead to any major inflation surprises.



Source: Bloomberg, Axis MF Projections

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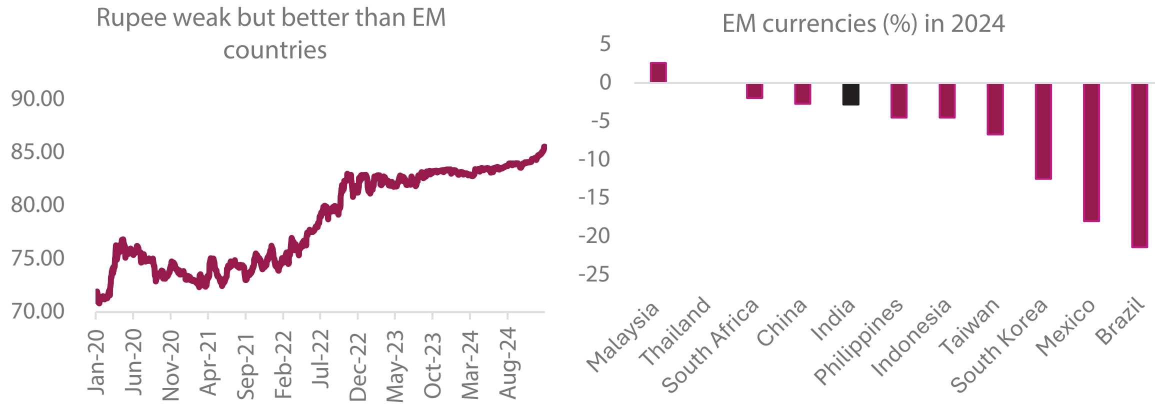
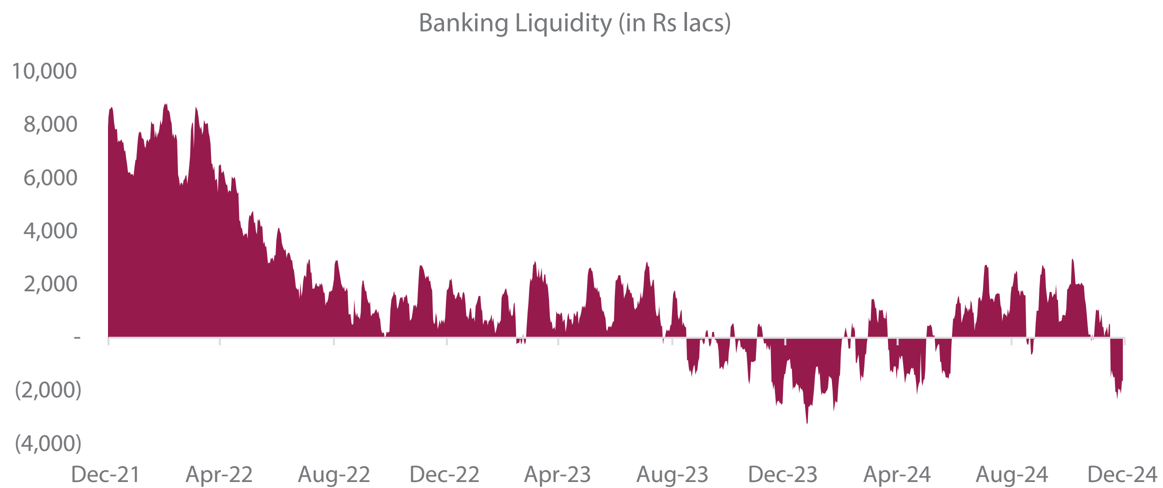
Currency: Rupee has been a stellar performer for the last few years. However, it can see some near term depreciation on fears of (a) tariffs imposed by the US (b) strong US dollar (c) weak growth and (d) FPI outflows. Having said that, the rupee has done reasonably well compared to other emerging market countries and we do not expect significant depreciation hereon.



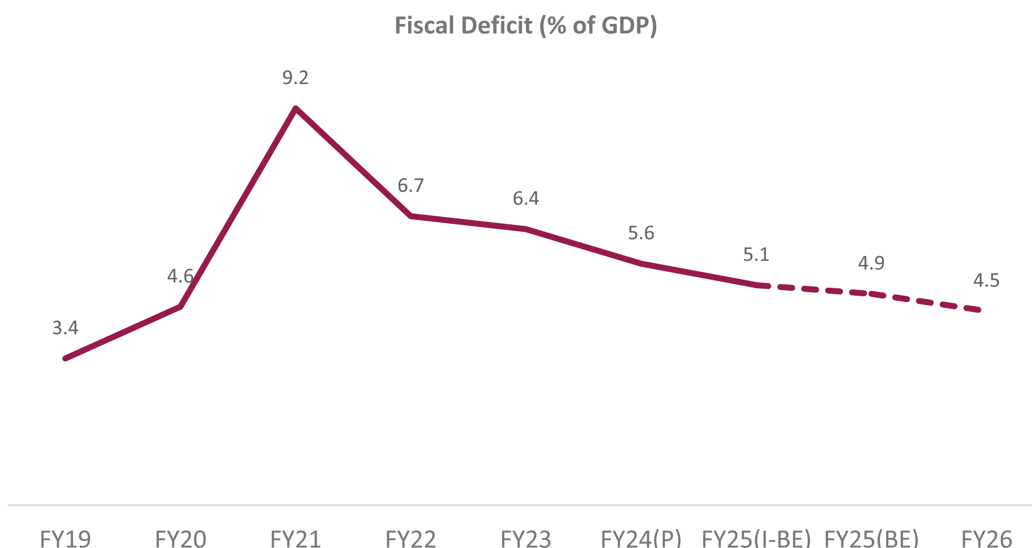
Source: Bloomberg

Banking Liquidity: We expect liquidity to remain in a tight range particularly in the first half of the year unless the central bank intervenes by way of OMO purchases or uses tools such as VRR/CRR. High seasonal growth in currency in circulation and continuous forex outflows would lead to banking liquidity to remain in deficit for most of the first half of 2025.



Source: Bloomberg

Fiscal Position: Despite the possibility of some tax measures to spur consumption we believe the government will adhere to its path of fiscal consolidation of 4.9% of GDP in FY25 and 4.5% in FY26. While slow growth can lead to some risks to revenue budgets, we do believe that government would like to continue to adhere to fiscal consolidation and do not see any major deviations in fiscal deficit for rating upgrades.

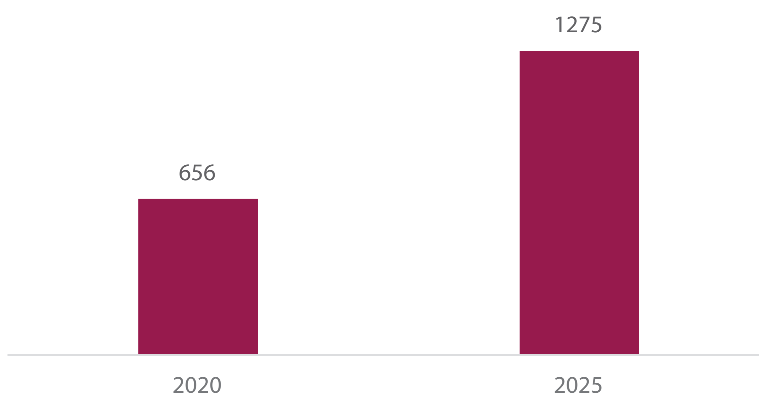


Source: Bloomberg, India Budget

The above graph should not be used for development or implementation of an investment strategy. Past performance may or may not be sustained in future.

Favourable demand supply dynamics: Bond markets will continue to have favourable demand supply dynamics due to (a)fiscal consolidation to 4.9% and 4.5% thereof (b) real money AUM growth. (Real Money AAUM is defined as Insurance, pension fund and provident fund AAUM). Additionally, the dynamics would become more favourable due to the proposed change in Liquidity Coverage Ratio guidelines or the possibility of inclusion in Bloomberg indices that could result in probable fresh inflows of US$20-25 billion.

Growth in real money AAUM (US$ bn)



Source Axis MF Research & Projections

The above graph should not be used for development or implementation of an investment strategy. Past performance may or may not be sustained in future.

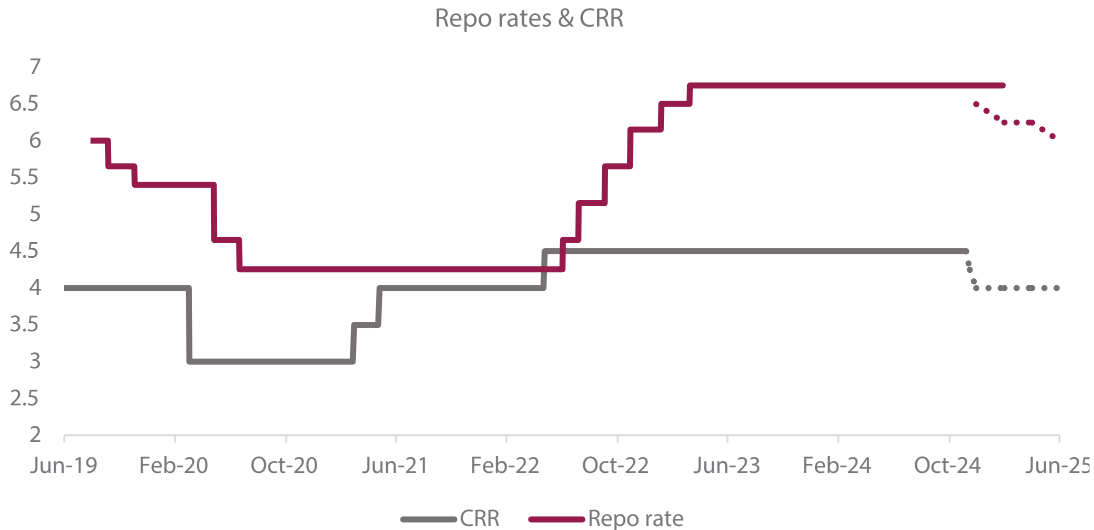
Based on these themes, our outlook for interest rates and credit in India is as below

Rates: We believe the rate cut cycle is almost around the corner and the fact that RBI has moved its stance from withdrawal of accommodation to neutral and cut CRR rates to inject liquidity into the system further amplifies a move forward to rate cut. Lower growth, controlled inflation and fiscal consolidation have paved path for monetary policy easing

We believe that from February, every policy meeting will be an opportunity for a rate cut based on the below

1) By the next policy meeting, the central bank would have clarity on inflation and growth numbers to some extent
2) The Union Budget would be rolled out and if government continues on the path of fiscal consolidation, which we believe it would, monetary easing will be the likely outcome
3) The new President of the US would be sworn in on January 20, 2025, and by the time of our policy meeting, all the currency movements and market reactions would be priced in.

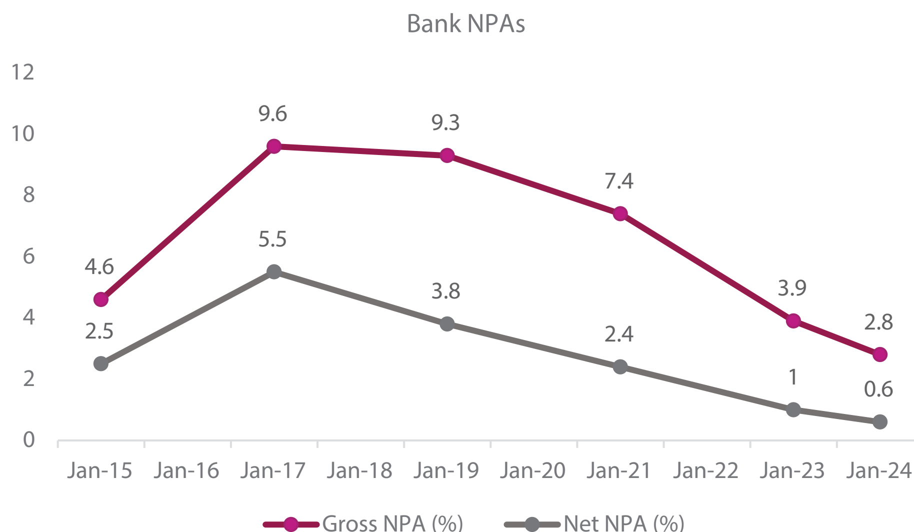
As growth at 6-6.5% continues to remain strong, we believe this cycle could be shallow and do not anticipate more than 50 bps of rate cuts in the next 6-12 months.



Source: Bloomberg, Axis MF Projections

The above graph should not be used for development or implementation of an investment strategy. Past performance may or may not be sustained in future.

Credit: Credit growth started to see moderation but even now overall leverage on corporate balance sheets is significantly lower while banking NPAs are at a 10-year low. Even if there is an uptick in NPAs we do not expect deterioration in credit quality. And we could remain neutral on the credit cycle at this point in time. If growth weakens more than expected then one can see impact on credit in the next 6-12 months.



Source Bloomberg, Internal research

The above graph should not be used for development or implementation of an investment strategy. Past performance may or may not be sustained in future.

Risks to our view: The risks to our view at this point are as below

1) Currency and liquidity are the near-term problems. On REER basis, we are slightly more expensive and hence can be some currency depreciation. Pressure on currency is keeping RBI on a cautious mode and liquidity could be a risk investors should watch out for.
2) US political theme and Inflationary policies of the incoming government which can lead to a stronger US dollar
3) China rebound can impact India in a vicious cycle of lower flows, weak growth and high inflation

Strategy – We have been maintaining a higher duration across all our funds and guiding the rally in bonds since March 2024. We have already witnessed a more than 50 bps of rally in yields in 10-year bonds since the beginning of the year but positive demand-supply dynamics for government bonds and expected rate cuts will continue to keep bond markets happy, and we can expect another 20-25 bps of rally in the next 3–6 months. We believe that banking liquidity would be addressed somewhat in the Jan- March 2025 quarter due to CRR cuts but the RBI will have to do more to manage banking liquidity. Due to favourable demand supply dynamics, we continue to have a higher bias towards government bonds in our duration funds.

Accordingly, from a strategy perspective, we have maintained an overweight duration stance within the respective scheme mandates with a higher allocation to Government bonds.

Expectations in 2025

Macro-Economic Indicator Projections

Repo Rate	6%
GDP	6.25%
Inflation	4-4.2%
Fiscal Deficit	4.5%
Currency	86-86.5
Gsec 10-year yield	6.5-6.6%
Crude	US$60-70

Source: Axis MF Research

Source Bloomberg, Axis MF Projections
The above data points are used to explain the concept and is for illustration purpose only and should not be used for development or implementation of an investment strategy. Past performance may or may not be sustained in future. These views are solely of the fund manager

Recap of 2024

If 2024 were a story, it would be titled "The Year of Surprises." Picture a year where inflation finally took a backseat, and central banks around the world decided to ease up on interest rates. It was a year when everyone braced for a US recession that never came, and anticipated China's economic resurgence that never quite materialized. Despite the backdrop of escalating geopolitical tensions, commodity prices remained surprisingly stable. 2024 was a year that defied expectations on many counts.

Reflecting on the year, the dominant theme that carried over into 2024 was the anticipation of slowing global growth. Key developments included rate cuts in the US and other major economies, favorable election outcomes across various regions, unexpected stimulus measures in China, escalating geopolitical tensions and sharp appreciation in prices of precious metals.

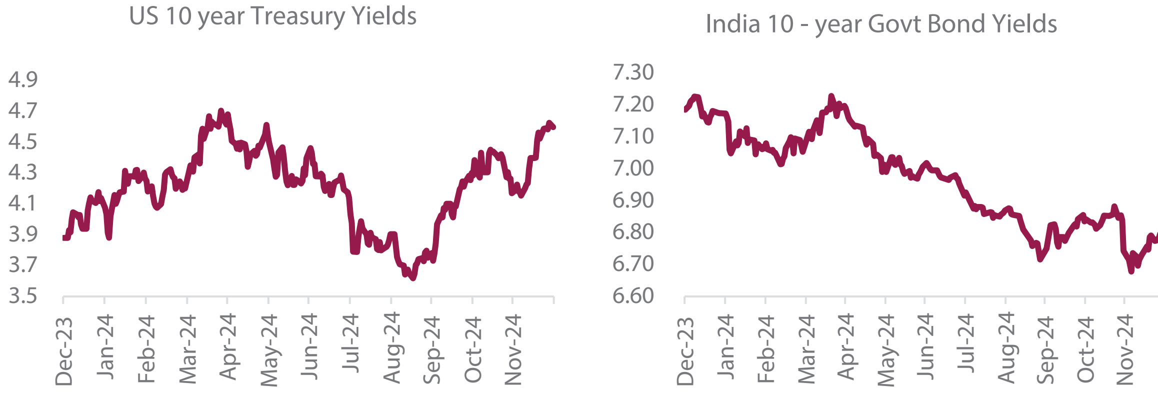
Easing price pressures and signs of slowing macroeconomic indicators eventually paved the way for major central banks to initiate interest rate cuts. The US Federal Reserve reduced rates by 50 basis points in September, followed by two additional cuts of 25 basis points each. Notably, the US was not the first to lower rates; the Swiss National Bank led the charge, reducing borrowing costs three times in 2024 to 1% since it began easing in March. The European Central Bank, Bank of England, and Bank of Canada have also been prominent in lowering interest rates this year. Interestingly, the Bank of Japan raised interest rates twice during the year, ending an eight-year period of negative interest rates. The People's Bank of China cut key interest rates starting in late September, only after the Fed began its easing cycle, allowing China to lower domestic borrowing costs without causing a sharp decline in the Chinese yuan.
reduction will inject liquidity amounting to Rs 1,16,000 crore into the banking system, with an even
In India, macros were significantly influenced by the higher for longer rates in first half of the year, elections in India and the union budget outlining the path of fiscal consolidation. The government reduced the fiscal deficit from 5.1% to 4.9% and the glide path suggested 4.5% in FY26.

The year saw significant fluctuations in banking liquidity, influenced by various macroeconomic factors as outlined below: In Q2CY24, banking liquidity experienced a deficit as elections embargo led to reduced Government spending, Huge buildup of Government Surplus post transfer of RBI dividend (Govt Surplus touched a high of Rs 5 trillion in June 2024), Fall in durable liquidity in Q4CY24 on account of huge forex outflows (Oct/ Nov 2024) and Increase in Currency in Circulation (CIC) due to elections.

Given that Banking liquidity was in surplus since Q3CY24, the operative rate stood below the Repo rate of 6.5% and was inching towards deficit on account of forex interventions by the RBI. However, in its last monetary policy of 2024, the RBI cut the CRR by 50 basis points to 4% in two equal tranches. This

larger multiplier effect. The RBI has a cushion of 50 bps of additional CRR, maintained since May 2022. A CRR has been the most appropriate tool, as it would also help banks manage liquidity in light of the expected tweaks in LCR guidelines next year.

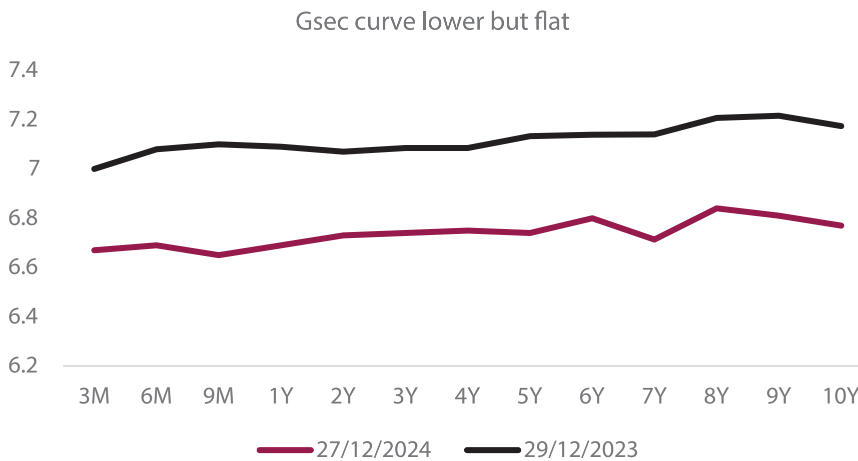
Moves by sovereign bonds



Source: Bloomberg Data as CY24

The above graph should not be used for development or implementation of an investment strategy. Past performance may or may not be sustained in future.

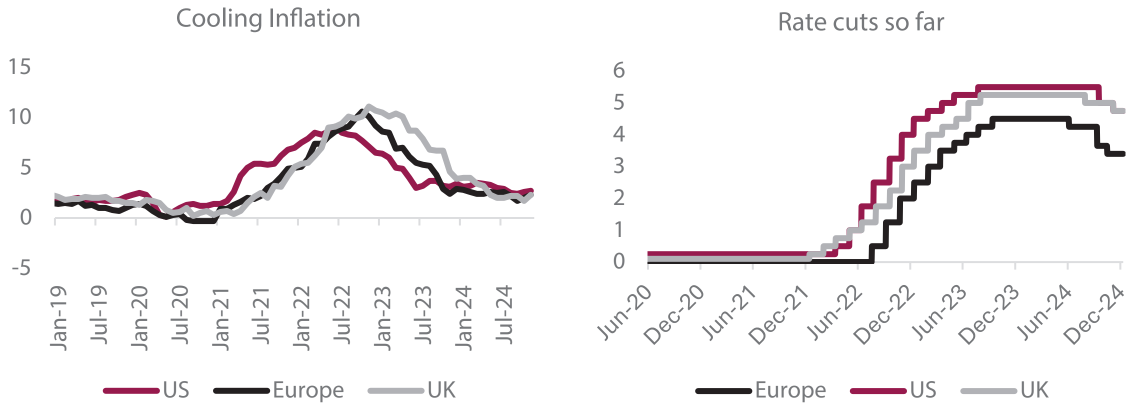
The yields across the curve fell over the year in anticipation of a rate cut cycle.



Source: Bloomberg

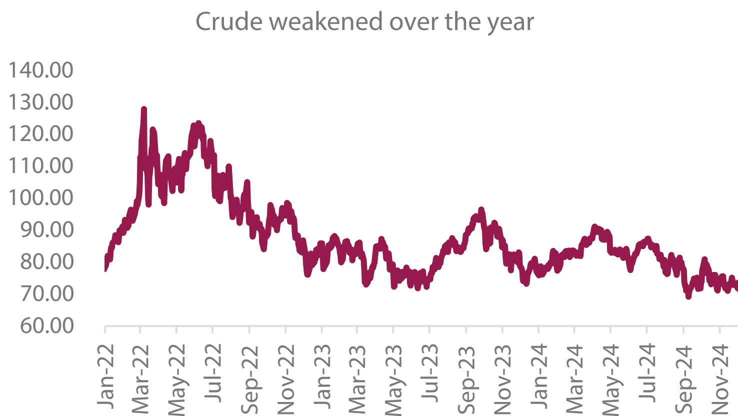
The above graph should not be used for development or implementation of an investment strategy. Past performance may or may not be sustained in future.

Inflation and rate cuts: Cooling inflation in the developed economies allowed the central banks to lower rates during the course of the year. In India, inflation remained stubborn at various points prompting the central bank to stay on hold.



Source: Bloomberg

Commodities: Some commodities had a strong performance this year, after the beginning of easing cycles. This, coupled with the geopolitical landscape, made precious metals the standout performers, with gold reaching record highs multiple times. While industrial metals began the year on a strong note, their momentum waned. Since mid-October, crude oil prices have traded within a narrow range of US$ 71-76. Furthermore, concerns that the escalating geopolitical tensions in the Middle East and Europe could disrupt global oil supply have been offset by prospect of supply glut in 2025.

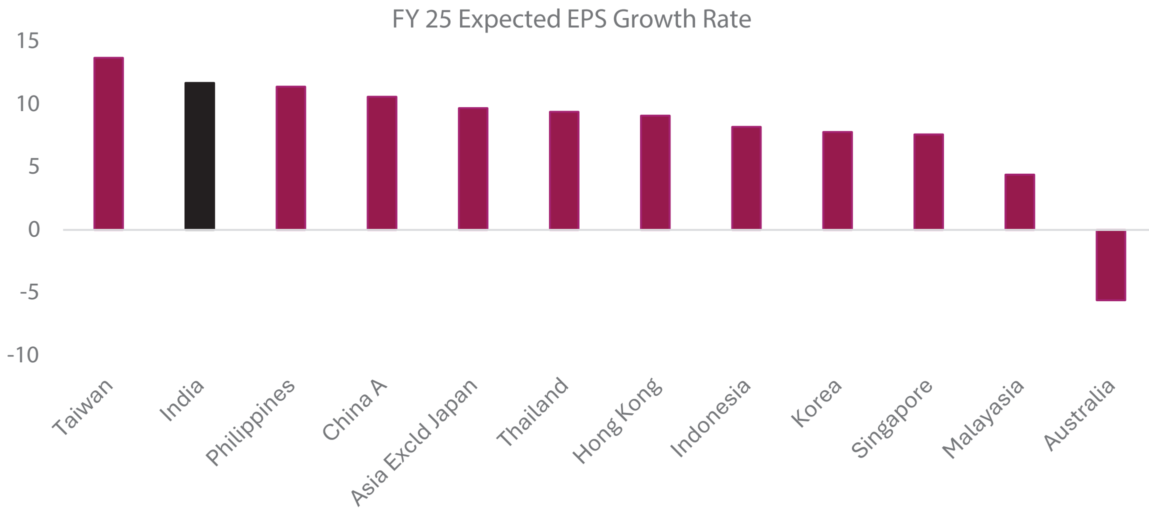


Source: Bloomberg

QUANTITATIVE OUTLOOK

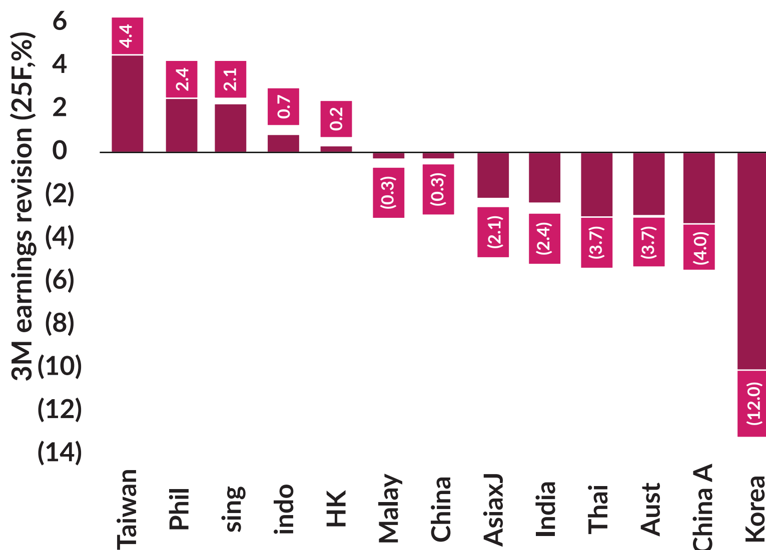
2025 will be off to an interesting start as markets, globally, remain focused on the 1) New US Presidential, his policy especially with regards to global trade and its political and financial repercussions 2) Central Bank action especially with regards to both the extent and pace of rate cuts. Domestically the focus will remain on Earnings growth outlook and government / RBI actions to support the same especially in light of tepid recent earnings season and slowing macro statistics.

While our markets have one of the highest growth expectations amongst Asian markets it has seen sharp cuts over the last quarter.



Source: Axis MF Research

Asia markets – L3M earnings revision (25F)



Note: Ratios are bottom up aggregated with free float adjustment using current MSCI universe
Source: Jefferies

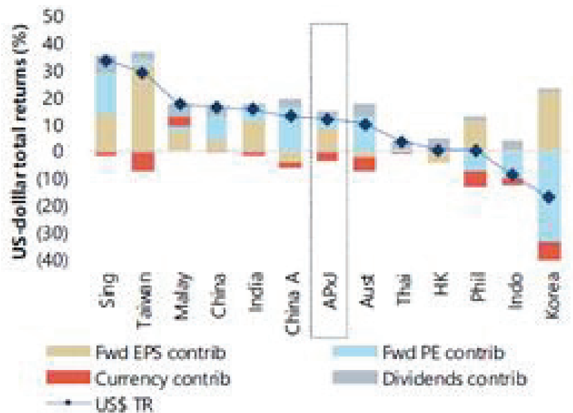
Recap of 2024:

2024 was an eventful year for Global and Indian markets with Political events & central bank actions dominating the headlines. Our markets had another good year as the large caps as of year to date have returned close to 8-9% while Mid & Small caps have continued their great run delivering close to 23-

24%. However, investors who have followed markets closely will agree that it's been far from smooth sailing as this year has also seen immense volatility, political uncertainty and a tricky macro landscape. In fact, despite the overall strong performance many market participants are still probably a bit disappointed given the correction post September.

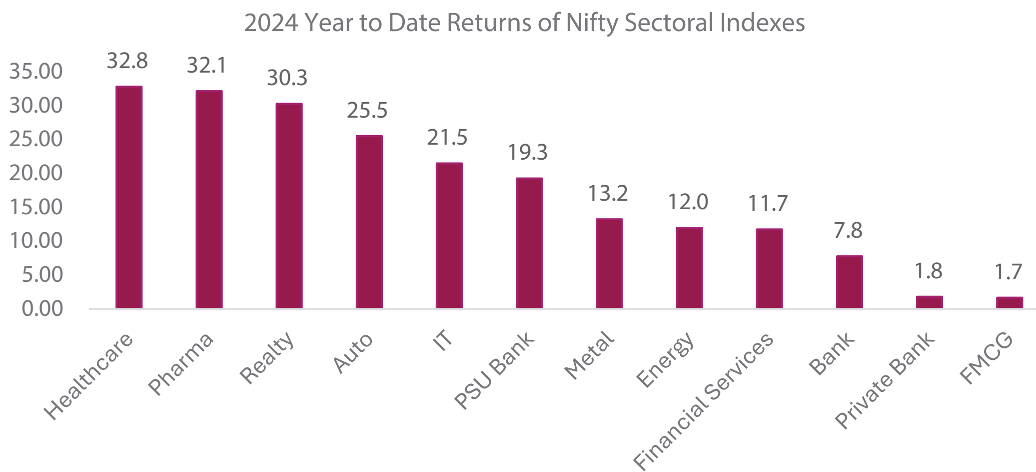
The correction was driven by a weaker than expected earnings season and foreign capital outflows in favor of China and the US. However, DII's continued to be the calming influence soaking in the FII outflow as they made their presence felt in the market.

Notwithstanding the recent bout of volatility our market was still one of the better performers amongst emerging markets peers with the rally being supported by a healthy mix of earnings contribution and multiple expansion.



Source: Jefferies

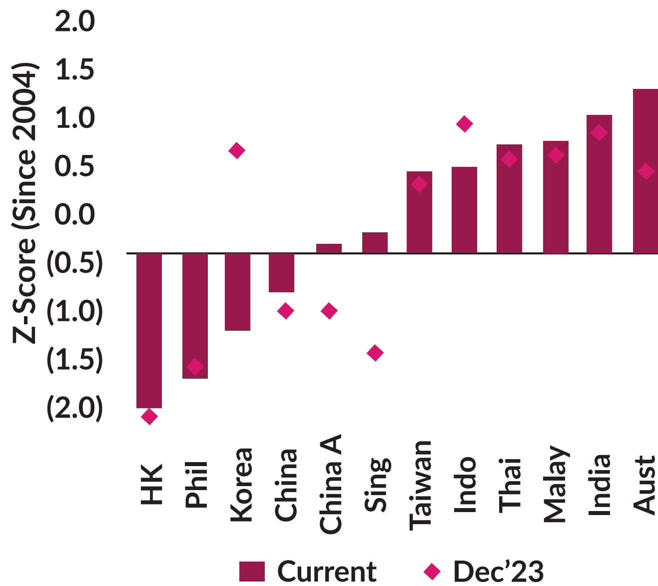
From a sector perspective Pharma, Realty and Autos were the top performers while FMCG & Consumer facing sectors were the laggards given weaker consumption trends especially in urban areas.



Source: Bloomberg

The Sectors mentioned above are used to explain the concept and is for illustration purpose only and should not be used for development or implementation of any investment strategy. It should not be construed as investment advice to any party.

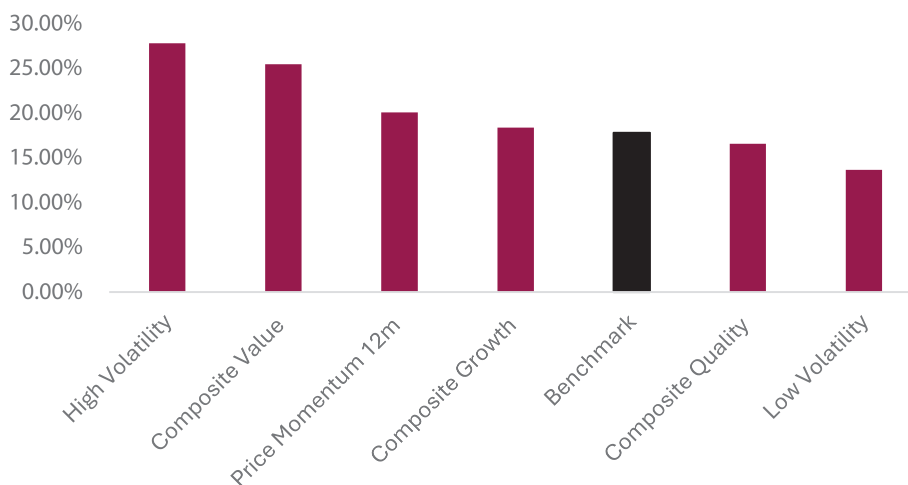
However, thanks to our continued strong performance, our valuation remains at the higher end of the spectrum both on a standalone and relative basis.



Source: Jefferies

From a style perspective, the markets were largely in a risk-on mode as is evident from the outperformance of 1.) High volatility stocks over low volatility stocks and 2.) Small and Mid Cap over large cap. This trend was also persistent during the recent correction indicating that this was more likely an overdue market correction rather than a complete change in market sentiment.

Momentum and Value continued to hold sway over the markets while quality continued to struggle for yet another year.

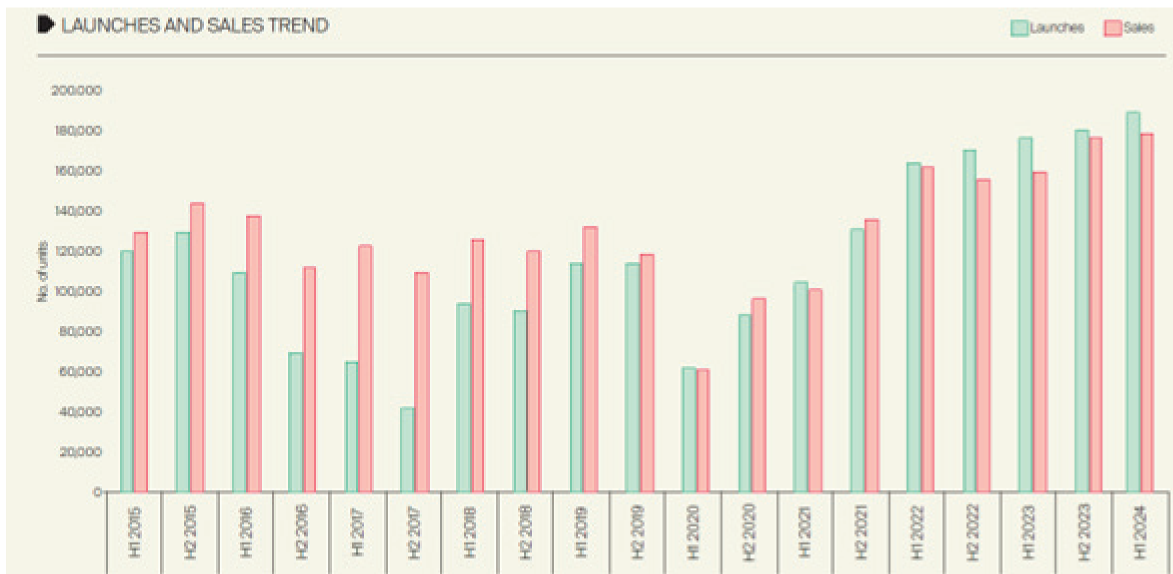


Source: Bloomberg

From a Quantitative perspective, the start of this downgrade cycle calls for renewed focus on Earnings revisions and Growth as a style. Also, during times when business environment is uncertain Quality and Low Volatility as a group can also outperform broader markets.

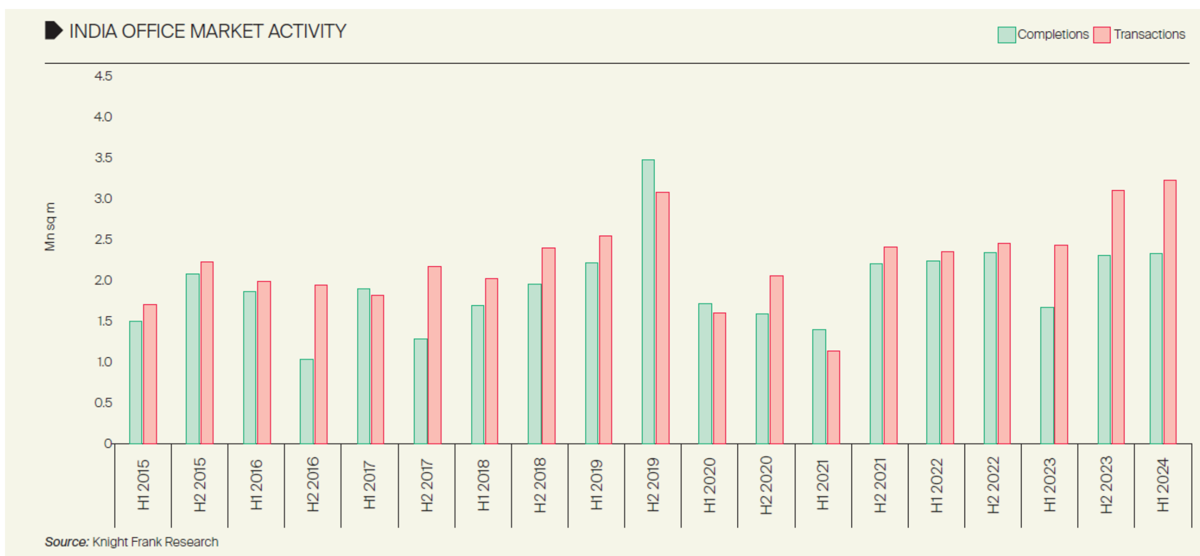
REAL ESTATE OUTLOOK - MAKE HAY WHILE THE SUN SHINES

The real estate sector particularly the residential real estate has been on an upswing since 2022. The last calendar year (2023) and current year (2024) to date performance of residential sale has been the best in last ~13 years. This can be attributed to the underlying cycle observed in the residential real estate wherein from approx. from 2014 to 2020 it was stagnation or correction. Further, the pandemic has reemphasized the basic need of having a roof over-head. Upgradation and having a larger space possibly in an independent format (plots, villas, bungalows) has shifted the demand tilt more towards the high value inventory rather than the low value inventory. The upswing has helped all the developers to strengthen their balance sheets importantly through debt reduction.



Source: Knight Frank Research

Like residential, commercial real estate also has scaled new highs in the calendar year 2024. Back to office theme in IT-ITeS, growing demand amongst the captive offshore units- GCCs, ever increasing appetite of co-working spaces has been fueling the demand in this space.



Source: Knight Frank Research

We remain cautiously optimistic while looking ahead at 2025. We expect the upward trend to continue for the large part of the calendar year. Further, consolidation amongst the top branded players will further enhance. Focus of Government on infrastructure will largely dictate the axis and micro-markets of development. Transit oriented development - the metro trains corridors, few of the tier II cities along

with newly constructed highways (like Mumbai-Delhi) will see maximum traction. Transaction volumes from the mid-income and affordable sectors are expected to improve in tandem with softening of interest rates providing tailwind.
The growing demand for sustainable development along with “flight to quality” has seen and will continue to see better absorption in new age developments under commercial real estate.
While the current upcycle helps and strengthens the broader industry, we stick to our investment thesis of focusing more on the margins in the business than catch the cycle of asset price escalations.

Disclaimer

Source of Data: Axis MF Research, Morgan Stanley, Jefferies, BofA, Bloomberg, NSDL, Axis Capital.
Date: 30 December 2024

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