



DECEMBER 2016

# I-CAN MONTHLY NEWSLETTER

# MONTHLY NEWSLETTER – DECEMBER

## 2016

### Market Update

<b>Sensex : Down 4.6%</b>	
<b>Nifty : Down 4.8%</b>	
Best performing sector: Metal (4%)	Worst performing sector: Realty (-17%)
Best performing Global index: US Dow Jones (5%)	Worst performing Global index: Jakarta Composite (-5%)
Indian Rupee: -2.4%	Gold price: -3.6%

On 8<sup>th</sup> November, the Indian government sprung a massive surprise by scrapping Rs. 500 and Rs. 1,000 currency notes in order to eliminate black money and tackle the issue of counterfeit notes. This accounts for over 80% of the currency in circulation amounting to Rs 14 lakh crore. It was decided that new currency notes of Rs. 500 and Rs. 2,000 denominations will be available starting 11 November. People were given a 50-day window to return the old notes. ATM withdrawal limits were set at Rs 2,000 per day – later revised to Rs 2,500 per day. A daily cash exchange limit of Rs. 4,000 was set for exchanging old currency notes – which was later revised to Rs 4,500. Later the government told banks to provide details of individuals who deposit Rs 2.5 lakh or more in savings accounts or fixed deposits between November 9 and December 30. All cash deposits of more than Rs 2.5 lakh made till 30 December in a bank account will be reported to the tax department by banks. It will then be

matched with the depositor's income tax returns and suitable action taken. In case of large cash deposits of more than Rs10 lakh that are not explained by the income declared in the income tax returns, it will be treated as tax evasion and the tax amount plus a penalty of 200% of the tax payable would be levied. Banks were also instructed to keep an eye on new bank accounts being opened and suspicious transactions. The government has also been monitoring Jan Dhan accounts for large deposits. This unprecedented move stirred a lot of debate among experts, politicians and economists. The government urged people to cooperate with the inconvenience that will be caused for some weeks but insisted this was beneficial for the economy and honest taxpayers in the long run.

The Taxation Laws (Second Amendment) Bill was introduced in Lok Sabha, which proposes a new voluntary disclosure and investment scheme, named Pradhan Mantri Garib Kalyan Yojana (PMGKY) 2016. It offers black money hoarders yet another opportunity to come clean, albeit at a higher tax cost than the recently concluded Income Disclosure Scheme (IDS). Additional tax revenues under this scheme will be used for social welfare projects. Those who deposited their black money will now have to pay income tax at 50% and 25% of the portion of the unaccounted income would remain with the government for 4 years. For those with unaccounted incomes who do not

opt for PMGKY, any unexplained credit (including in bank accounts) will attract 60% tax plus 25% surcharge and 10% penalty, making it an effective rate of 85%.

FIIIs were heavy sellers in the month of November. A net of Rs 18,244 crore was sold in equity markets and Rs 21,151 crore was sold in debt markets. This was partly a result of their general selling in emerging markets. Some selling may also have been influenced by concerns over the near term economic impacts of demonetisation.

International agencies like IMF supported India's efforts to battle corruption and black money. According to Christopher Wood (Managing Director, CLSA) the Indian equity market could suffer for around 6 months due to this move. Deutsche Bank cut its December Sensex target to 25,000 from 27,000. According to a Morgan Stanley report towards November end, the Indian equity market is exiting the low return trap and equities are likely to deliver 15% return next year. Goldman Sachs forecasted a deceleration in India's GDP growth to 6.8% this fiscal, down from 7.6% last financial year, due to demonetization. Due to excess liquidity, State Bank of India slashed bulk deposit rates by upto 1.9% - taking the 1-year rate to 4.25%. This was followed by other banks like Axis Bank, HDFC Bank and others slashing rates.

Another significant event was the election of Donald Trump as the US President on 8<sup>th</sup> November. This, coupled with demonetization had a negative impact on the Indian markets. The Indian IT industry would be impacted if Trump implements stricter immigration norms.

Nasscom revised the growth forecast to 8-10% this year.

In the beginning of the month the markets and macroeconomic data was looking good. The Nikkei India Manufacturing Purchasing Managers' Index (PMI) rose to 54.4 for October, the highest level in 22 months. The Nikkei India Composite PMI Output Index which reflects activity both in the manufacturing and services sectors, came in at 55.4 for October – highest level in nearly four years. India improved its ranking by one spot in a global index of business optimism. According to the latest Grant Thornton International Business Report, India was ranked second on the optimism index during the third quarter (July-September 2016). Equity mutual funds attracted a net inflow of Rs. 9,400 crore – the highest since July 2015. Wholesale inflation fell to 3.39% in October from 3.57% in the previous month. CPI inflation came in at 4.2%, which dropped from 4.31% in the previous month. Investments in domestic capital markets through participatory notes (P-Notes) fell to its lowest level in two-and-half years to Rs 2 lakh crore in end-October.

Reforms:

- SEBI has tightened the rules for Credit Rating Agencies as per the new guidelines. It includes standardizing the rating criteria, method of public disclosures, the internal functioning of rating committees and disallows the suspension of ratings.
- The GST Council announced a four-tier tax structure – 5%, 12%, 18% and 28%. However, the Council failed to arrive at an agreement over the crucial issue of

administrative control over assessee under the new indirect tax regime.

- To ease the PAN verification process at the time of account-opening of FPIs, markets regulator SEBI said

intermediaries can verify the PAN of FPIs online through a website authorised by the Income Tax department.

## Impact of Demonetisation and Trump Victory on Investments

After the unexpected victory of Donald Trump as the President of the United States on 8<sup>th</sup> November 2016, left the investors panicked but gave way to a strong market rally. The same day our Prime Minister Narendra Modi announced demonetisation of the old Rs 500 and Rs 1000 notes due to which the markets are witnessing heightened volatility. The impact of these two events is spread across various financial products & asset classes.

### Equity

The day after the victory of Trump over the US presidential election & announcement of the demonetisation move, the BSE Sensex opened with a heavy loss of 1300 points, but managed to recover later. It rallied on 10<sup>th</sup> November 2016 but closed 700 points down the next day. The investors should not ignore these two events as the global unfolding of these two events could still have its impacts on the various equity products and on the economy as well. Though the old currency notes are being exchanged for the new ones, the government could still reduce the credit flow in the short term.

There can be a negative impact on the GDP (Gross Domestic Product) in the October- December quarter and if the Government and RBI does not take steps to ease the liquidity situation the export oriented sectors could also face a negative impact.

According to Ridham Desai (Head of India Research, Morgan Stanley), "Equity valuations are looking good against bonds now, the best since 2013. They also look attractive against emerging markets (EMs). I don't think demonetisation destroys India's growth story; it defers it by a bit."

After the US presidential election the main focus would now be on the US fed policy due in December. The 10 year bond yield has gone up by 2% after a gap of eight months the investors have started factoring a 80 % chance of rate hike this month, which means the volatility might return soon.

Kalmesh Rao, CEO, Kotak Securities expects banks to be the biggest beneficiaries of the demonetisation move as the cash in circulation would now be converted into bank deposits.

## **Gold**

Gold as an asset class has been adversely affected by these two events. The gold rallied on Trump's victory but gave up most gains later. The demonetization move boosted the investment sentiments in gold among the Indian investors. Many individuals who were held up with the old currency notes converted them into gold after the announcement of the demonetisation move. Therefore, as a result of these two events the price of gold hiked. According to Kishore Narne, Associate Director, Motilal Oswal Commodities Broker, "Global uncertainty is increasing, so we are bullish on gold, in the long-term."

## **Debt**

The debt markets reacted positively to the twin events. The bond prices may increase as a result of the deflationary impact of demonetisation. The improvement in the finances of the government due to the increased tax compliances, better revenues for the government and shifting of the black economy is also considered as a positive aspect post the demonetisation move.

Many debt fund managers expect further rate which would be a positive news for the investors in the debt market. The bond market is likely to rally post the demonetisation move. Lakshmi Iyer, Head of Fixed Income and Product, Kotak Mahindra Mutual Fund, for instance, expects a 50 basis point rate cut.

## **Real Estate**

This sector is the biggest receiver of black money and could be affected massively post the announcement of the demonetisation move. This sector can have a negative impact in the near term, but however in the long run this sector would have a good performance as the demonetisation move will lead to increased transparency reduce the use of cash. With the reduction in use of black money and increasing transparency, the prices of the land and residential properties would eventually come down.

The buyers would benefit from the expected fall in home prices.

### Did you know?

Memorizing something every day sharpens your brain and increases memory functioning

### Cartoon of the Month

#### **Investments and Financial Services**



**“You’re trying to attract bulls with bear food!”**

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