

# RBI Monetary Policy

December 2022

The Monetary Policy Committee (MPC) came out with their bi-monthly policy statement today. Some of the key announcements are as follows:

- ◆ The MPC decided by a majority of 5 out of 6 members to increase the policy Repo Rate by 35 bps to 6.25%
- ◆ Consequently, the Standing Deposit Facility (SDF) rate was adjusted to 6.00% and the Marginal Standing Facility (MSF) rate and Bank Rate adjusted to 6.50%
- ◆ The MPC also decided by a majority of 4 out of 6 members to remain focused on withdrawal of accommodation to ensure that inflation remained within the target going forward

Among the MPC members, Prof. Jayanth Varma voted against the Repo Rate hike. Similarly, the decision to remain focused on withdrawal of accommodation was not unanimous, with Prof. Jayanth Varma and Dr. Ashima Goyal voting against this part of the resolution.

For FY23, growth forecast has been revised lower by 20 bps to 6.80% while inflation estimate has been retained at 6.70%. The RBI has also projected inflation of 5.40% for Q2 FY24 while GDP growth for Q2 FY24 has been estimated at 5.90%, with risks evenly balanced.

The Governor acknowledged pressure from core inflation and food inflation. He mentioned that the MPC was of the view that further calibrated monetary policy action was warranted to keep inflation expectations anchored. However, he also mentioned that monetary policy actions, while keeping a sharp focus on inflation, will be nimble and keep in mind growth aspects as well. On the liquidity side, the Governor warned that market participants must wean themselves away from overhang of liquidity surplus, while adding that, if required, RBI would conduct LAF operations to inject liquidity during transient episodes of tight liquidity and will remain flexible in its liquidity management

## Market movement

The policy action was broadly in line with market expectations. However, some sections of the market had anticipated a shift in monetary policy stance to neutral and the market had been well bid in the run up to the policy. Given this, the market saw some amount of negative reaction with yields across G-Sec and corporate bonds higher by 5-8 bps. However, yields softened a bit towards the latter part of the trading session and closed only slightly negative. The short end money market papers moved higher by ~5 bps.



## Outlook

The hike of 35 bps was largely a unanimous expectation of the market in the immediate run up to the policy and the RBI delivered the same. The dissent by some of the MPC members on the rate hike and policy stance, were also in line with the views expected by those members during the previous MPC's minutes.

However, it was the tone and messaging during the Governor's statement and the ensuing press conference which did the job of signaling to the market that the RBI's battle against inflation was not done just yet. Deputy Governor Dr. Patra's press conference comment that the RBI was still some distance away from neutral rates and the focus on breaking core inflation persistence - suggest that the MPC does not want the markets to assume that the guard can be let down.

We view the current policy as mildly hawkish versus market expectations. With the stance being maintained as "withdrawal of accommodation", markets would need to factor in at least one more rate hike as a high probability, although dependent on incoming data between now and February.

Another important point in our view, was the repeated emphasis on the need to move to the 4% CPI target, and not just the upper bound of 6%. This seems to have been a deliberate attempt by the RBI to dispel the market's notion that headline CPI below 6% was good enough for the MPC to relax on the inflation front.

Overall – the policy has put a temporary brake on the bond market rally, which was driven by expectations of a possible MPC pause in February. While a lot of factors viz. oil prices, US inflation trends and the Fed's rate actions, domestic inflation trends in headline, food, services and core inflation – all will have a bearing on the next rate action by the MPC – for now we believe that markets need to price in a 25 bps hike in February. With a possible 6.5% Repo Rate, G-Sec yields are likely to consolidate around the 7.25-7.50% levels, thereby not leaving much room for a significant rally from current levels.

## Fund strategy

We continue to believe that at levels close to 7.25-7.50%, the 1-3 year part of the yield curve offers good carry and relative value vis-à-vis other points on the curve, for investors who are looking at a medium-term investment horizon. Also, compared to the longer end of the curve, corporate bond spreads in this segment have become more attractive. Accordingly, **HSBC Banking and PSU Debt Fund** and the **HSBC Short Duration Fund** which are both predominantly positioned in this segment, are attractive investment opportunities in this space.

At the longer end, AAA corporate bond spreads remain unattractive, and we expect them to widen over the coming few months based on the strong banking system credit growth. Also with banks needing to raise more resources to fund credit growth, pressure on FD and CD rates to continue to trend higher is likely to persist. We believe this is likely to provide a good tactical opportunity over the coming months for investors to enter into products in the 6 months to 1-year space.

Finally, with rate hikes nearing the peak, there are likely to be more opportunities for dynamically managed funds to be able to tactically, as well as strategically deliver alpha. For investors desiring alpha through duration calls, funds like the **HSBC Dynamic Bond Fund**, **HSBC Gilt Fund** and **HSBC Medium Duration Fund** are all attractive opportunities to be considered by medium to long term investors.

## Product Labels

Scheme name and Type of scheme

\*Riskometer of the Scheme

Riskometer of the benchmark

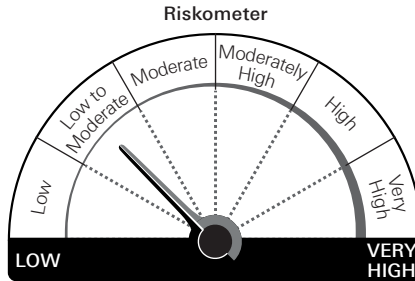
### This product is suitable for investors who are seeking<sup>#</sup>

**HSBC Short Duration Fund** (Short Duration Fund) - An open ended Short Term Debt Scheme investing in instruments such that the Macaulay duration of the portfolio is between 1 year to 3 years. Please refer to the SID for explanation on Macaulay duration. Moderate interest rate risk and moderate credit risk.

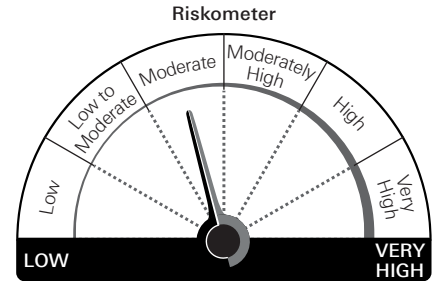
- Generation of regular returns over short term
- Investment in fixed income securities of shorter term maturity. (Benchmark: NIFTY Low Duration Debt Index B-II)

**HSBC Banking and PSU Debt Fund** (Banking and PSU Debt Fund) - An open ended debt scheme predominantly investing in debt instruments of banks, public sector undertakings, public financial institutions and municipal bonds. A relatively high interest rate risk and relatively low credit risk.

- Generation of reasonable returns and liquidity over short term
- Investment predominantly in securities issued by Banks, Public Sector Undertakings and Public Financial Institutions and municipal corporations in India. (Benchmark: Nifty Banking & PSU Debt Index)



Investors understand that their principal will be at Low to Moderate risk



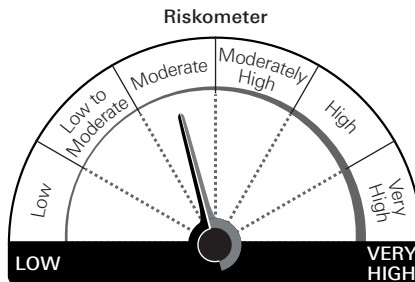
**HSBC Dynamic Bond Fund** (Dynamic Bond Fund) - An open ended dynamic debt scheme investing across duration. Please refer to the SID for explanation on Macaulay duration. Relatively high interest rate risk and relatively low credit risk.

- Generation of reasonable returns over medium to long term
- Investment in fixed income securities. (Benchmark: NIFTY Composite Debt Index A-III)

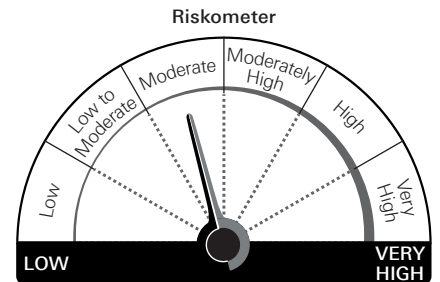
**HSBC Gilt Fund** (Medium to Long Duration Fund) - An open ended debt scheme investing in government securities across maturity.

A relatively high interest rate risk and relatively low credit risk.

- Generation of returns over medium to long term
- Investment in Government Securities. (Benchmark: Nifty All Duration G-Sec Index)

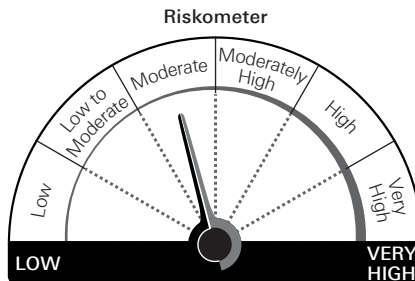


Investors understand that their principal will be at Moderate risk

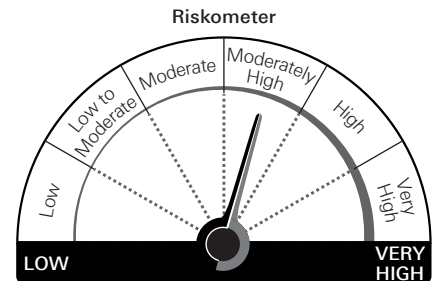


**HSBC Medium Duration Fund** (Medium Duration Fund) - An open ended medium term debt scheme investing in instruments such that the Macaulay duration of the portfolio is between 3 years to 4 years. Please refer Page no. 9 of the SID for explanation on Macaulay duration. A relatively high interest rate risk and moderate credit risk.

- Generation of income over medium term
- Investment primarily in debt and money market securities. (Benchmark: NIFTY Medium Duration Debt Index Fund B-III)



Investors understand that their principal will be at Moderate risk



<sup>#</sup>Investors should consult their financial advisers if in doubt about whether the product is suitable for them.

**Scheme name Potential Risk Class**
**HSBC Short Duration Fund**

Potential Risk Class			
Credit Risk →	Relatively Low (Class A)	Moderate (Class B)	Relatively High (Class C)
Interest Rate Risk ↓			
Relatively Low (Class I)			
Moderate (Class II)		<b>B-II</b>	
Relatively High (Class III)			

**Scheme name Potential Risk Class**
**HSBC Banking and PSU Debt Fund  
HSBC Dynamic Bond Fund  
HSBC Gilt Fund**

Potential Risk Class			
Credit Risk →	Relatively Low (Class A)	Moderate (Class B)	Relatively High (Class C)
Interest Rate Risk ↓			
Relatively Low (Class I)			
Moderate (Class II)			
Relatively High (Class III)	<b>A-III</b>		

**Scheme name Potential Risk Class**
**HSBC Medium Duration Fund**

Potential Risk Class			
Credit Risk →	Relatively Low (Class A)	Moderate (Class B)	Relatively High (Class C)
Interest Rate Risk ↓			
Relatively Low (Class I)			
Moderate (Class II)			
Relatively High (Class III)		<b>B-III</b>	

**Past performance is not an indicator of future returns.** Source: HSBC Mutual Fund, RBI, Bloomberg. Data as on December 7, 2022

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