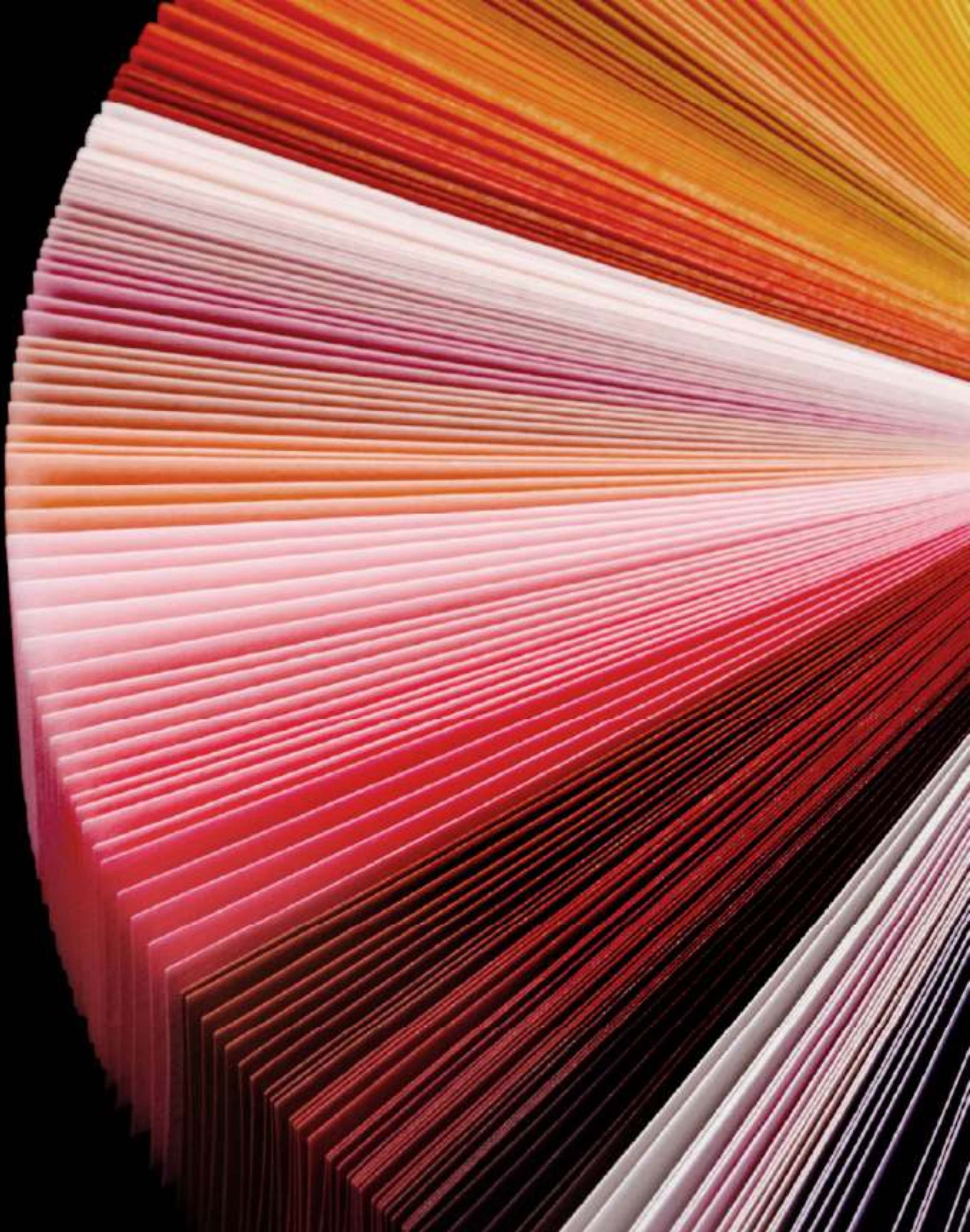
Fixed Income Market Update



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Fixed Income – Top down Macro Economic factors

Impact on Bond markets

- Banking trends - Credit Deposit ratio
- Systemic Liquidity surplus
- CPI & Core inflation trends

- Global interest rate environment
- Growth
- Fiscal policy
- Current Account Deficit & Currency
- G-Sec/SDL Demand Supply dynamics

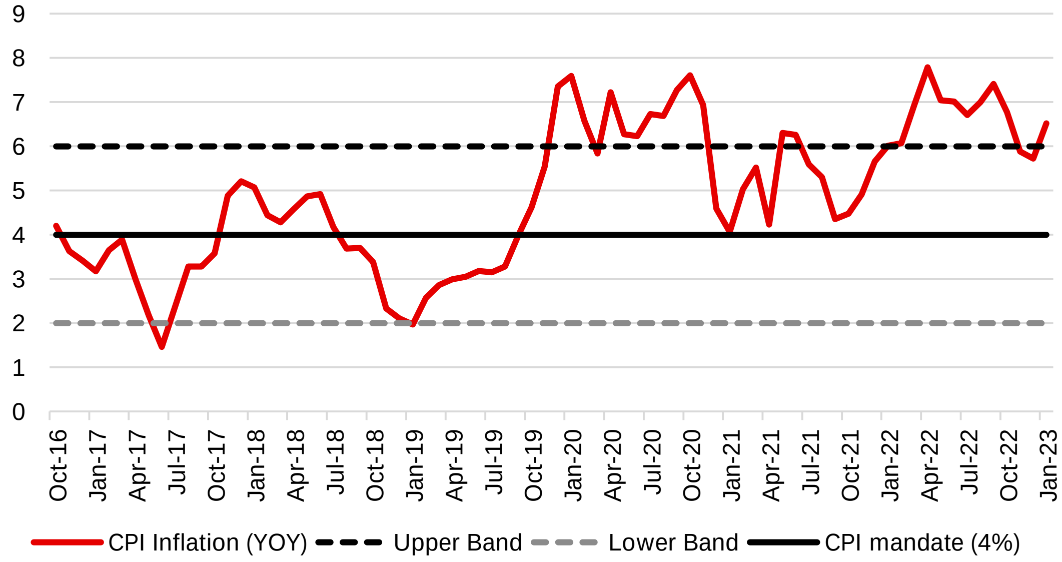
- Real rates/ Deposit Rates
- Monetary Policy

- Global Central banks likely to end the interest rate hikes this year but will likely keep rates at these higher levels to curb inflationary pressures
- Cumulative rate hikes in this cycle by major central banks: Fed – 450 bps, BOE – 390 bps, ECB – 300 bps, MPC – 250 bps
- MPC increased Repo rate in the Feb'23 policy by 25 bps to 6.50% and maintaining the withdrawal of accommodation stance by a vote of 4:2
- Real Rates, Deposit Rates and Small Savings rate turn favorable while we are in the last leg of hiking cycle
- Budget FY 2024 was on expected lines in terms of fiscal discipline, market borrowings and focus on Capex
- Recent Trade deficit number has narrowed, however funding CAD, neutral liquidity and Credit-deposit gap will keep any runaway rally in check

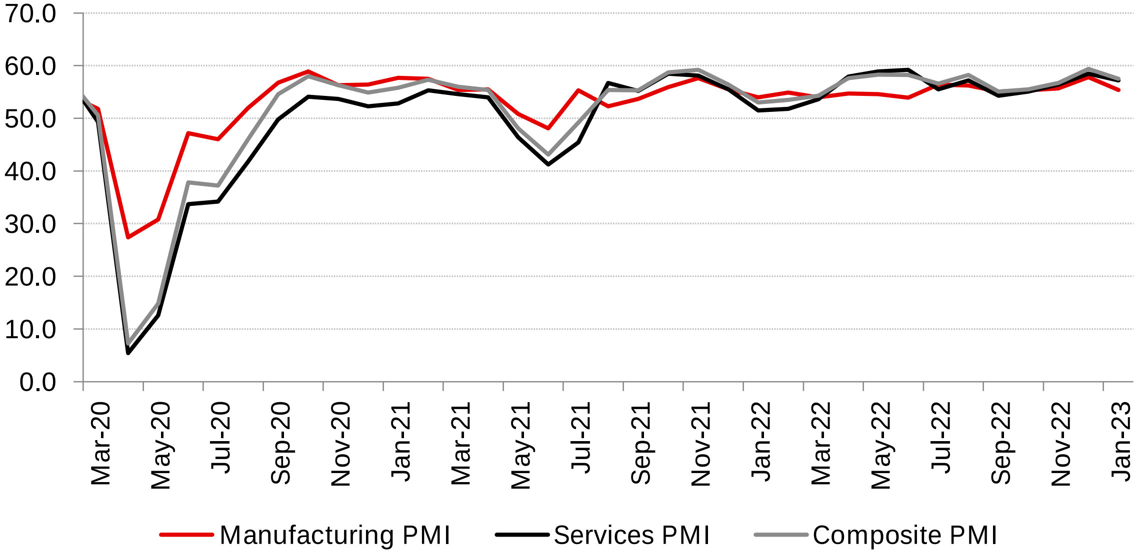
Source: Bloomberg, RBI, data as on 23 Feb 2023

Fixed Income – Growth / Inflation dynamics

Inflation trajectory vs Targeted mandate



PMI numbers remain in expansion



- Inflation eased in the interim due to seasonal fall in vegetable prices, however the recent print came higher than expected due to cereal inflation. Core inflation continues to remain sticky at around 6%
- As per RBI estimates, GDP Growth is expected to be at 7% for FY2023 and 6.4% for FY2024; GST collections remain robust
- However, risks due to spillover of global slowdown and impact of cumulative rate hikes done till now remain key factors

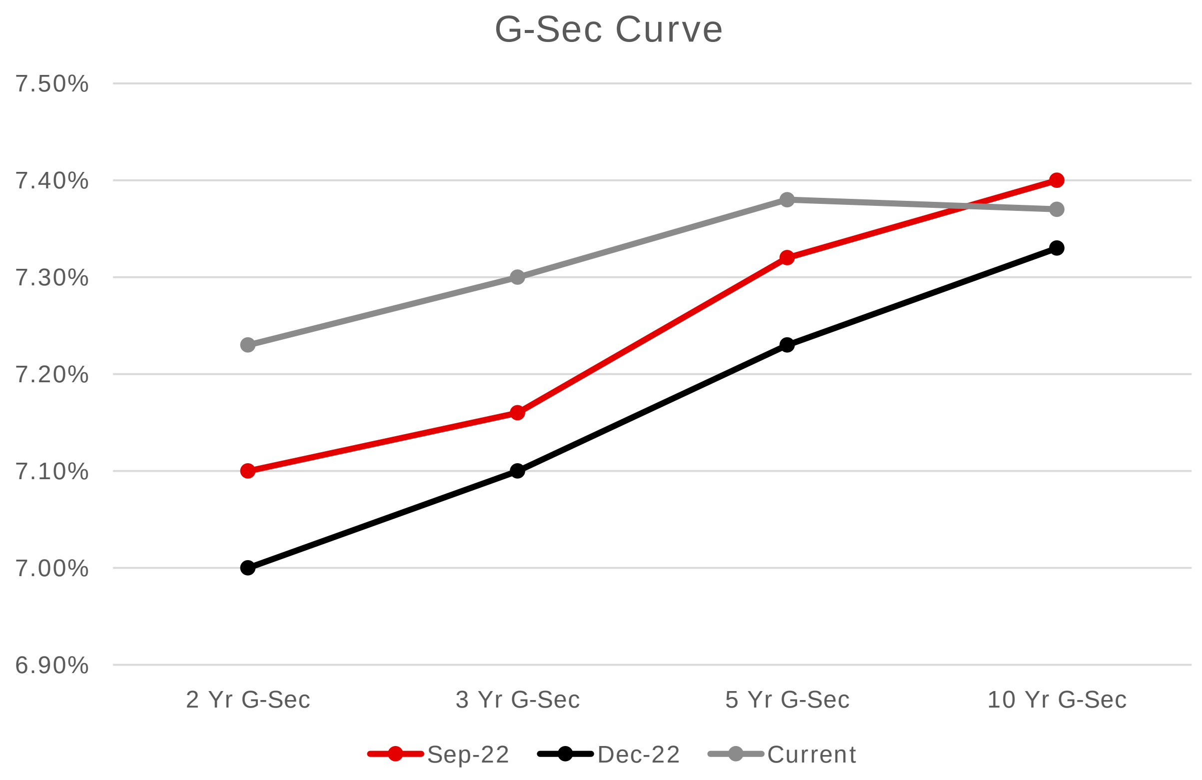
Peak of inflation seems to be behind us, however temporary deviation from expected levels cannot be ruled out

Source: Bloomberg, RBI, data as on 23 Feb 2023

Fixed Income – Market movement and Flattening of yield curve

	Sep-22	Dec-22	Current	Curent vs Dec'22 (bps)
3 mth T-Bill	6.03%	6.26%	6.85%	59
1 Yr T-Bill	6.70%	6.85%	7.25%	40
2 Yr G-Sec	7.10%	7.00%	7.23%	23
3 Yr G-Sec	7.16%	7.10%	7.30%	20
5 Yr G-Sec	7.32%	7.23%	7.38%	15
10 Yr G-Sec	7.40%	7.33%	7.37%	4
3 mth CD	6.30%	6.68%	7.37%	69
1 Yr CD	7.05%	7.58%	7.82%	24
2 Yr AAA PSU	7.38%	7.58%	7.81%	23
3 Yr AAA PSU	7.50%	7.58%	7.81%	23
5 Yr AAA PSU	7.58%	7.58%	7.76%	18
10 Yr AAA PSU	7.73%	7.63%	7.72%	9

Credit Spreads (bps)	Sep-22	Dec-22	Current
1 Yr	35	73	57
3 Yr AAA PSU	21	35	38
5 Yr AAA PSU	13	22	24
10 Yr AAA PSU	19	17	21



- Sovereign yield curve has flattened with 1 year T-Bill moving up by ~40 bps since Dec'2022 while 10-year G-Sec has moved up by 4 bps
- Shorter end of the curve (3-month to 1 year) has moved up due to repo rate hikes, tighter liquidity and higher CD issuances
- Credit spreads across the curve have widened with 3 year spreads moving up to 38 bps

Yield Curve has flattened over the last few months

Source: Valuation Reports, data as on 23 Feb 2023

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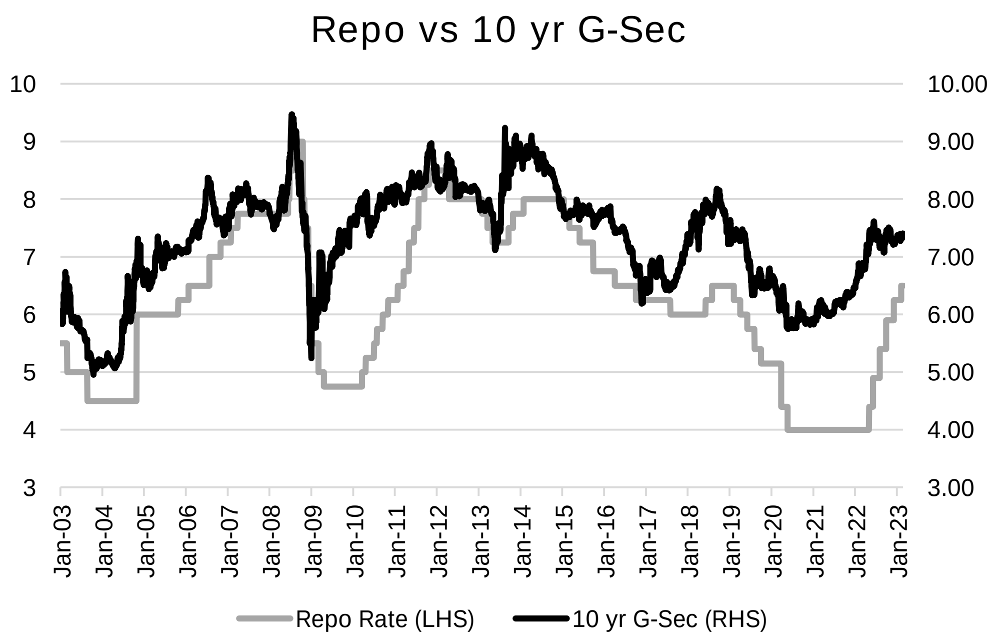
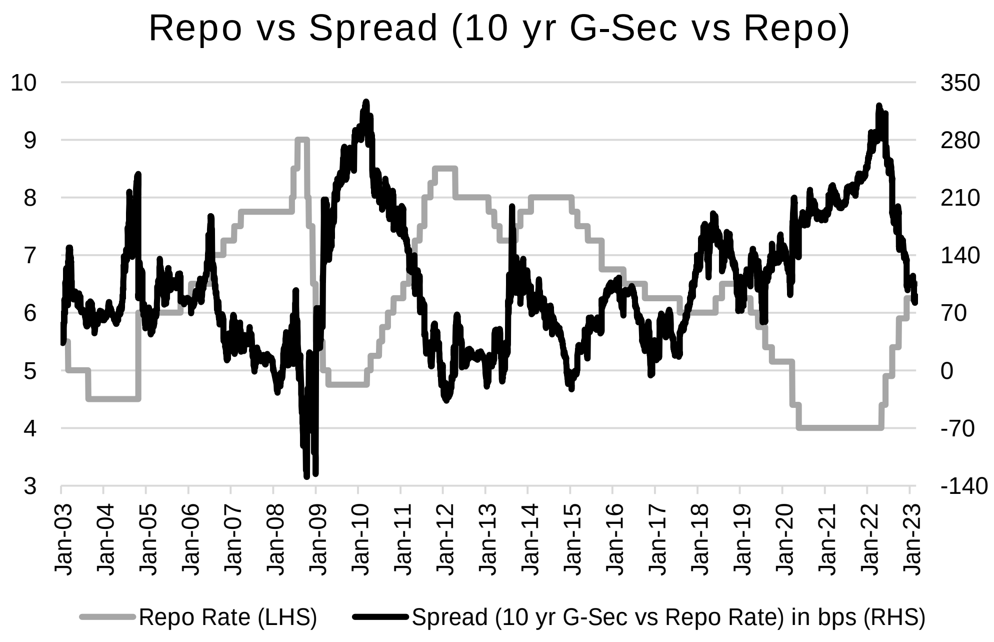
Fixed Income – G-Sec markets pre-empt rate actions





- Movement in G-Sec starts much before the actual rate action; Spreads are typically high before the first rate hike and are low before the first rate cut
- Barring the 2013 period where rates in India shot up rapidly, 10 year G-Sec yields have remained broadly below 8% over the last 10 years
- Strengthening macro-economic factors, strong FX reserves and stable currency remain the key differentiators from the 2013 episode

Although rate cuts might not be imminent, adding positions gradually might be better than timing entry points

Source: Bloomberg, data as on 23 Feb 2023

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