

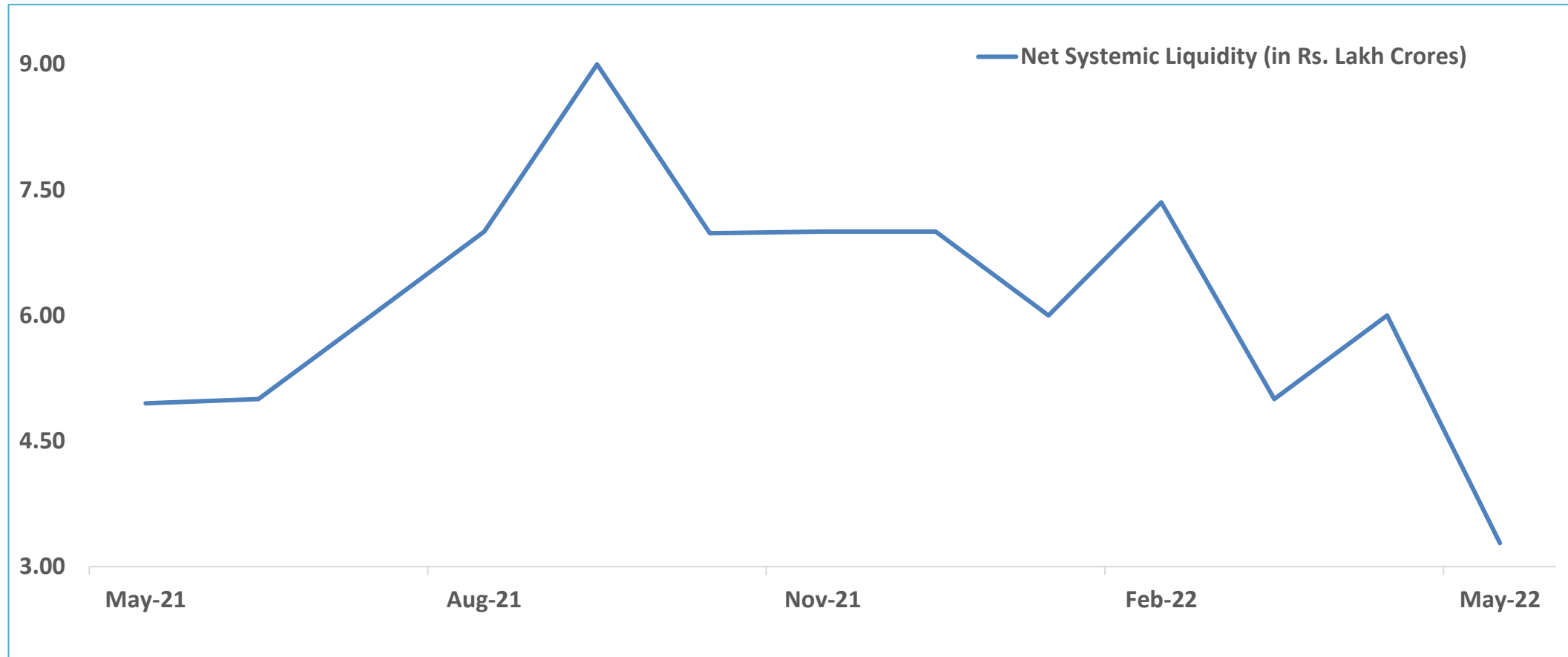
FIXED INCOME HOUSE VIEW

JUNE 2022

- The Monetary Policy Committee has highlighted rising inflation and is taking actions to achieve 'the medium-term target for CPI inflation of 4% within a band of +/- 2 per cent, while supporting growth.'
- The RBI MPC has unanimously maintained its accommodative stance while focusing on imminent withdrawal of accommodative stance. It is likely to move into a neutral stance in upcoming announcements.
- RBI has given importance to inflation management over GDP growth rates as it does not want the economy to slow down drastically. RBI feels lower inflation is required to support macro economic stability and ensure durable growth in the economy.
- RBI's support for the government's borrowing program is expected to be incrementally lower in the coming months. This is balanced with an intention to remove excess liquidity from the system over a multi-year period.
- RBI is expected to take measures to smoothen upward movement of the yield curve.

- In its off-cycle meeting on 4th May, the MPC Increase the policy repo rate under the liquidity adjustment facility (LAF) by 40 bps to 4.40% with immediate effect. This has effectively reversed the excessively accommodative stance taken during the Pandemic.
- Consequently, the standing deposit facility (SDF) rate stands adjusted to 4.15% and the marginal standing facility (MSF) rate and the Bank Rate to 4.65%.
- The CRR was raised by 50 bps from 4% to 4.50%. This is likely to drain Rs.0.9 trillion of excess liquidity from the system.
- There is increasing fiscal and monetary coordination between Government and RBI to control inflation. Government has cut petrol/ Diesel excise duty, levied export duty on steel, reduce duties on coal imports to zero. The government has banned the export of wheat now to make augment domestic supply and control food inflation.

- The government borrowing program for the financial year worth ~14.31 Lakh crores was announced, of which ~60% will be executed in the first half of FY23. The government wants to front load its capex due to its multiplier effect on the economy
- RBI will limit interventions in the market to control yields as such actions would be contradictory to their objective of reducing liquidity.
- RBI holds ~USD 50 billion of forward dollar purchases over the next 2 years, which gives it some independence to follow its own monetary policy. Current forex reserve is ~\$592 billion.
- RBI is unlikely to aggressively reduce liquidity through forex, but with increasing volatility and Current Acct. Deficit, it may look to elongate the maturity of the swaps it holds. When a central bank takes an aggressive position to fight inflation through policies such as rate hikes, the currency tends to strengthen.

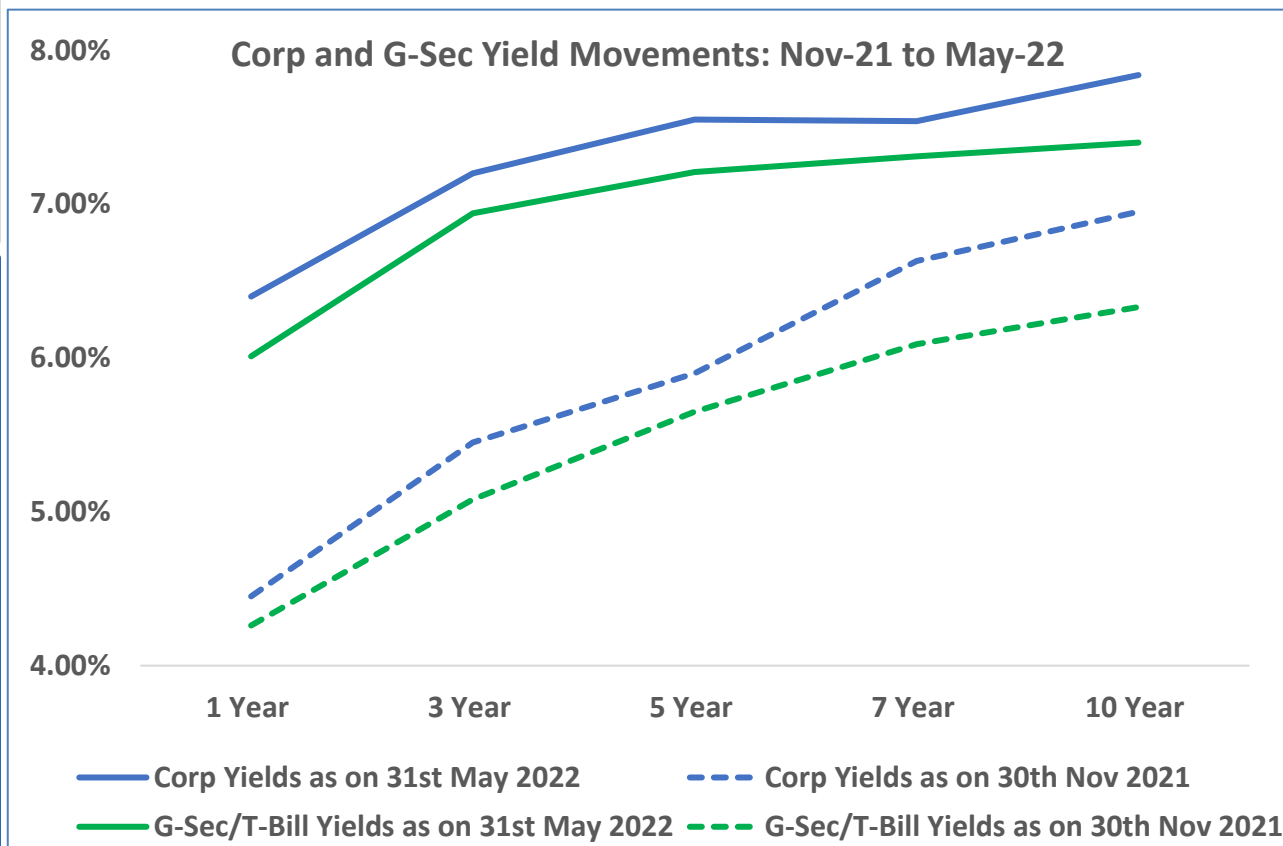


- In the beginning of FY22, the RBI injected liquidity in the markets in order to encourage economic growth.
- RBI has been taking steps to reduce systemic liquidity in order to control inflation. Systemic liquidity has reduced from a peak of ~9 lakh crores in September-21 to ~3 lakh crores in May-22.

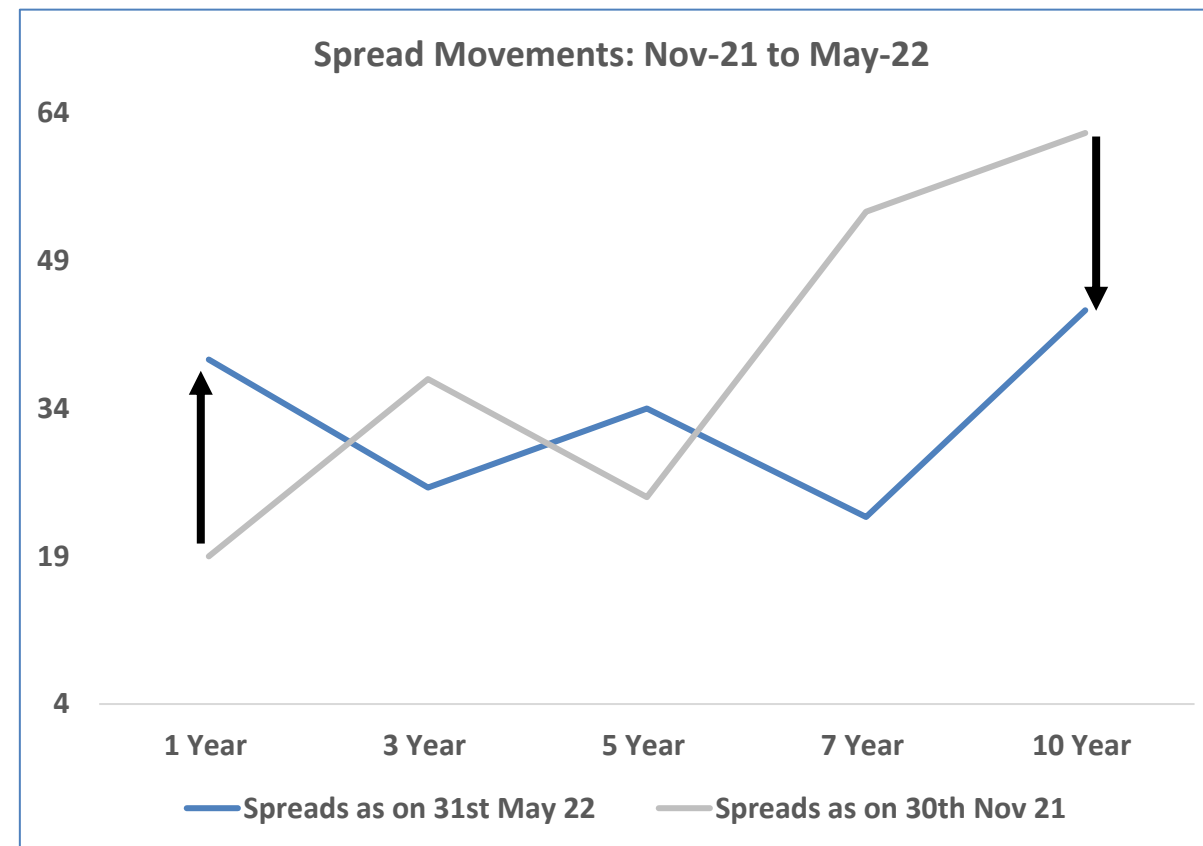
Rates	As on 4 th May 2022	As on 8 th April 2022	As on 22 nd May 2020	As on 27 th March 2020
MSF Rate (Marginal Standing Facility)	4.65%	4.25%	4.25%	4.65%
Repo Rate – Rate at which Banks borrow from RBI	4.40%	4.00%	4.00%	4.40%
Reverse Repo Rate – Rate at which banks deposit funds with RBI	3.35%	3.35%	3.35%	4.00%
Standing Deposit Facility (SDF)	4.15%	3.75%	--	--
Policy Corridor - difference between Operating Rate and MSF Rate	50	50	90	65
LAF Corridor - difference between Operating Rate and SDF Rates	25	25	65	40

- The base operating rate changed from Reverse Repo Rate to SDF with its introduction in April-22.
- With the introduction of SDF, policy and LAF corridor narrowed significantly, after being widened considerably during the pandemic.
- RBI hiked the Repo rate and other policy rates on 4th May in response to heightened CPI inflation.

YIELD AND SPREAD MOVEMENTS- 6 MONTHS



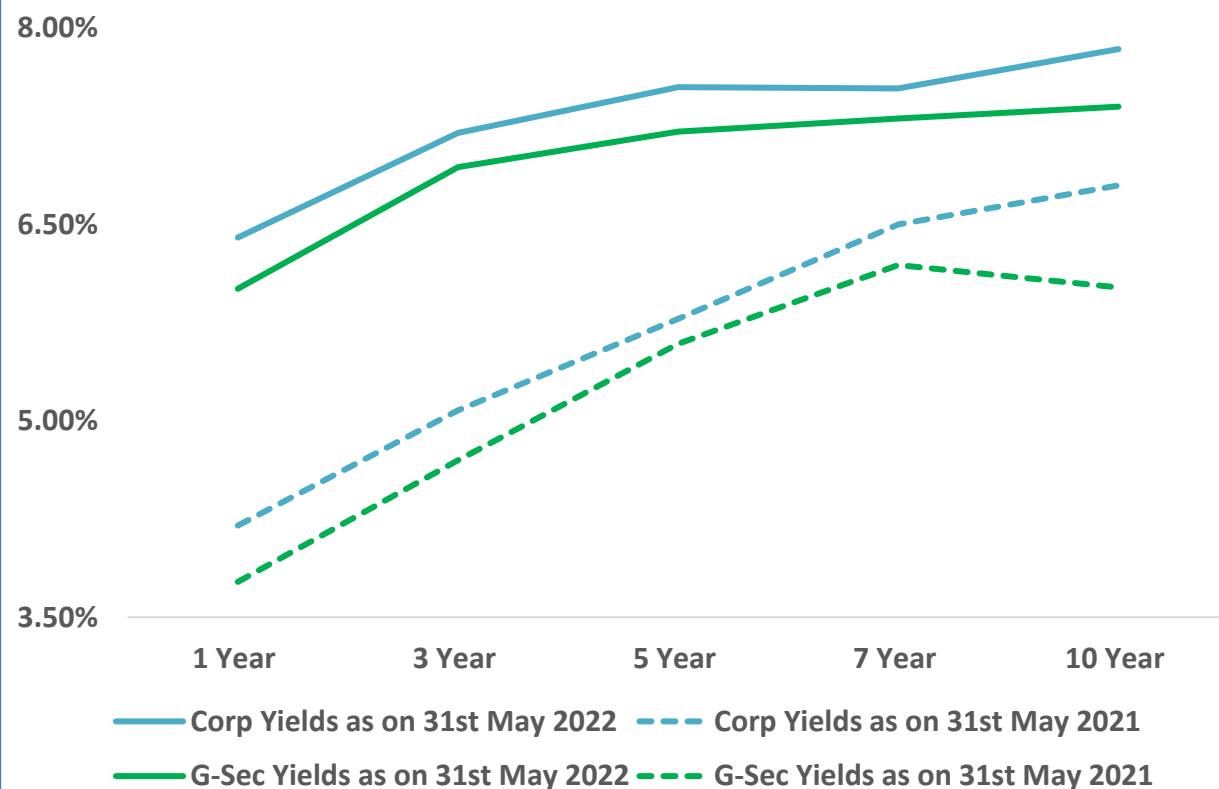
- Corporate yields in the 1–5-year segment rose by ~165-200 bps, while rising by ~90 bps in the 7-10-year segment.
- G-Sec yields rose by ~155-185 bps in the 1-5-year segment, and by 100-125 bps in the 7–10-year segment.



- Spreads widened by 20 bps in the 1-year segment and ~10 bps in the 5-year segment.
- Spreads in the 3-year segment compressed by ~10 bps and by 20-30 bps in the 7–10-year segment.

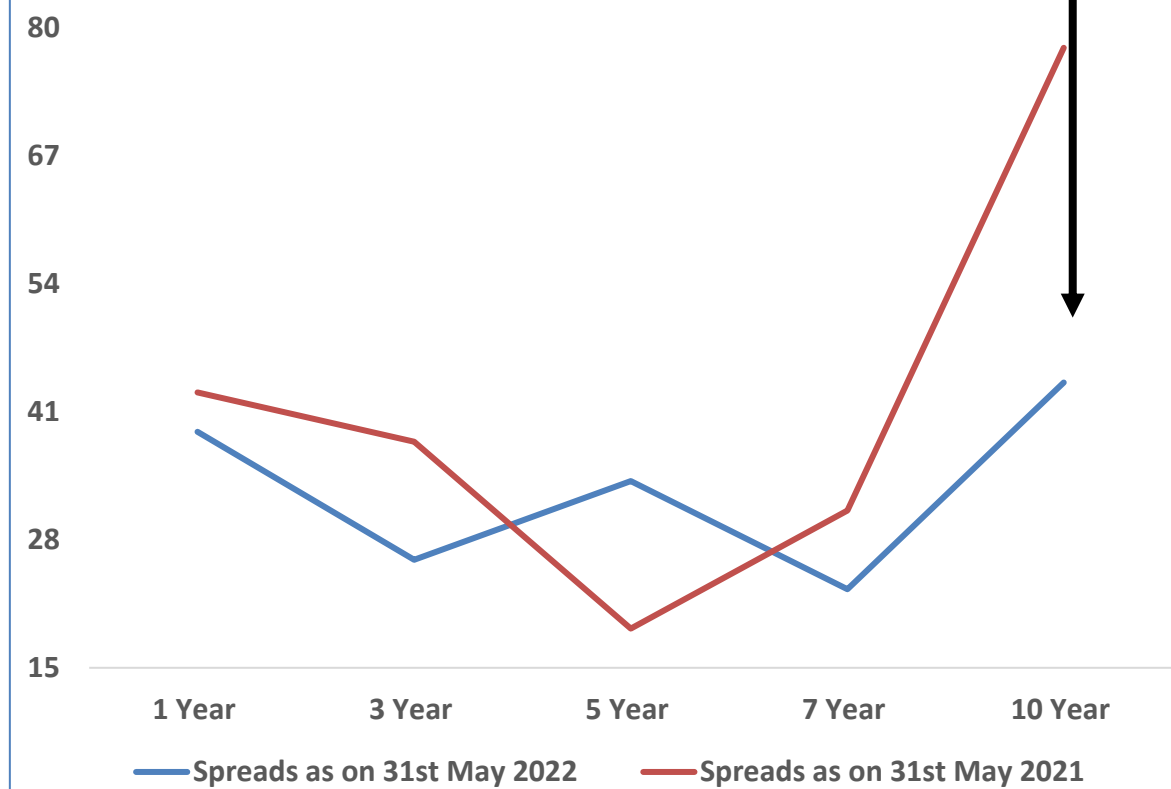
YIELD AND SPREAD MOVEMENTS- 12 MONTHS

Corp and G-Sec Yield Movements: May 2021-22



- Corp Yields in the 1-5-year segment rose by 175-210 bps. Yields in the 7-year segment rose by ~90 bps and by ~50 bps in the 10-year segment.
- G-Sec yields in the 1–5-year segment rose by ~130-145 bps. Yields in the 7–10-year segment rose by ~105 bps.

Spread Movements: May 2021-22



- Spreads in the 1–3-year segment compressed by 5-10 bps and by 10-30 bps in the 7-10 year segment.
- Spreads in the 5-year segment widened by ~15 bps.

	Corp Yields as on 31st May 22	Corp Yields as on 30th Nov 2021	Corp Yields as on 31st May 2021	Fall / rise in Yields: 30th Nov 21 to 31st May 22 (bps)	Fall / rise in Yields: 31st May 2021-22	Spreads as on 31st May 22	Spreads as on 30th Nov 21	Spreads as on 31st May 21
1M CD	4.36%	3.62%	3.39%	74	97	13	30	5
1M CP	5.03%	3.75%	3.23%	128	180	80	43	-11
3M CD	5.15%	3.55%	3.40%	160	175	25	3	1
3M CP	5.33%	4.00%	3.40%	133	193	43	48	1
6M CD	5.72%	4.05%	3.72%	167	200	29	22	12
6M CP	6.13%	4.65%	3.78%	148	235	70	82	18
12M CD	6.32%	4.41%	4.15%	191	217	41	28	42
12M CP	6.65%	4.80%	4.08%	185	257	74	67	35
1 Year	6.40%	4.45%	4.20%	195	220	39	19	43
3 Year	7.20%	5.45%	5.08%	175	212	26	37	38
5 Year	7.55%	5.90%	5.78%	165	177	34	25	19
7 Year	7.54%	6.63%	6.50%	91	104	23	54	31
10 Year	7.84%	6.95%	6.80%	89	104	44	62	78

- Yields rose across maturities in the past 6 months and 1 Year periods.
- The rise was greatest in the 6 months to 3 year segments.

G-SEC & T-BILL YIELD MOVEMENTS

	G-Sec/T-Bill Yields as on 31st May 2022	G-Sec/T-Bill Yields as on 30th Nov 2021	G-Sec/T-Bill Yields as on 31st May 2021	Fall / rise in Yields: 30th Nov 21 to 31st May 22 (bps)	Fall / rise in Yields: 31st May 2021-22
1M T-Bill	4.23%	3.32%	3.34%	91	89
3M T-Bill	4.90%	3.52%	3.39%	138	151
6M T-Bill	5.43%	3.83%	3.60%	160	183
12M T-Bill	5.91%	4.13%	3.73%	178	218
1 Year	6.01%	4.26%	3.77%	175	224
3 Year	6.94%	5.08%	4.70%	186	224
5 Year	7.21%	5.65%	5.59%	156	162
7 Year	7.31%	6.09%	6.19%	122	112
10 Year	7.40%	6.33%	6.02%	107	138

- Yields rose across maturities in the past 6 months and 1 Year periods.
- The rise was greatest in the 6 months to 3 year segments.

	Corporate Yields	G-Sec Yields
Expected Movement	Expect corporate curve to shift upwards due to rate hikes and lower systemic liquidity.	Expected to move up due to higher government borrowing program and rate hikes.
Short End Rates	Likely to see upward movement due to lowered systemic liquidity and rate hike. CD yields may rise as banks resume issuing papers as overnight liquidity moves to match SDF levels.	May have some upward pressure on yields as the high borrowing program means government may be compelled to borrow in the short end also.
Long End Rates	Corporate bond yields may see an uptick due to increase supply of papers in the medium term, combined with lower liquidity.	Long end of the yield curve expected to move up due to huge borrowing program and rate hikes. Expect that 10-year yields could be in the 7.30-7.50% range. If credit demand increases, yields could go higher.
RBI Actions	RBI action of liquidity withdrawal could lead to upward pressure on yields. Lack of market intervention could also lead to yields drifting upwards.	

- RBI is expected to cumulatively hike Repo rate by 200 bps over coming quarters. It is expected to maintain accommodative stance and focus on withdrawal of accommodation. Interest upcycle is likely to last for coming 12- 18 months.
- RBI is expected to continue to reduce excess liquidity over a multi-year period. Inflation is likely to remain sticky for an extended period.
- Government is likely to borrow a majority of its stated requirement for the year in the coming months.
- This is likely to put upward pressure on yields across the curve, with the shorter end rising to a greater extent.
- Overall, we remain neutral on debt markets and expect accruals to be major driver for return generation for next few months.
- We will continue to focus on the quality of securities across portfolios.

THANK YOU

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