AUM - FORTNIGHTLY GILTS MARKET UPDATE

AUM CAPITAL
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February 13 , 2023

(30/01/2022 – 03/02/2023)

The Govt. Securities yields on Monday opened with a bearish note and ended higher for the third consecutive trading session as investors remained cautious ahead of the Union Budget announcement with concerns of higher borrowings by the central govt. and the states government's Govt. Securities yields ended lower on Tuesday after rising for the last three sessions, triggered by short covering and as the government plans to issue a new 10-year paper this week.

However, the Budget's Gross and Net Market Borrowings announcement soothed the markets as the market borrowing announced for FY24, was slightly lower than the market expectations. With the budget announcements, yields softened and the 10year benchmark Govt Securities traded at a low of 7.28% during the intra-day trades. Further, G-Sec auction cutoffs came on expected lines with the new 10-year Govt Securities auction coupon at 7.26% added to the positive sentiment.

Hence, there was an immediate softening by 6 basis points on the Budget day itself. Further on the global front, the US-Treasury yields softened as the FOMC moderated the pace of the rate hike for the second straight policy with a rate hike of 25 bps. Also Bank of England and European Central Bank hiked its policy rate by 50 bps each. Additionally, inflation of both ECB and BOE came lower than the market expectations however far above the target inflation. Crude oil prices softened on strong US crude oil inventories. The yield dropped 11 basis points (bps) this week.

The benchmark 10-year 7.26% GS 2032 closed at 7.28 % as against the previous week (Friday - January 27, 2023) closing of 7.39%

Government Securities – Secondary Market Yields

	February 3, 2023	February 10, 2023
2 Years	6.99	7.16
5 Years	7.16	7.32
10 Years	7.28	7.36
14 Years	7.35	7.45
29 Years	7.47	7.43

Government Securities - Primary Market Auction Cut Off (Yields & Price)

February 3, 2023				February 10, 2023			
Nomenclature	Notified Amount	Cut Off (Yield)	Cut Off (Price)	Nomenclature	Notified Amount	Cut Off (Yield)	Cut Off (Price)
7.38% GS 2027	7000	7.1442	100.86	6.89% GS 2025	4000	7.14	99.55
New GS 2033	12000	7.26	100	7.10% GS 2029	6000	7.3399	98.81
7.36% GS 2052	9000	7.4018	99.49	7.41% GS 2036	11000	7.4411	99.72
				7.40% GS 2062	9000	7.4267	99.65

(06/02/2023 – 10/02/2023)

The Govt Securities yields surged on Monday, tracking the U.S. yields as strong economic data raised fears of another rate hike by the Federal Reserve. However, the market participants remained cautious ahead of the MPC meeting outcome. Also, G Secs were slightly overbought, after the budget and there was some correction as well as unwinding of some positions. Overall the Gilts closed about 2-7 bps weaker across the curve. On Wednesday, tracking the surge in crude oil price and US-Treasury yields, the domestic G Sec market opened on a negative note. The Govt Securities yields ended higher on Wednesday after the RBI maintained the hawkish stance and surprised the market by leaving the door open to more tightening, saying core inflation remained high. The yields ended higher on Thursday, a day ahead of the Govt Securities debt auction, while the central bank's hawkish outlook on monetary policy continued to weigh on the market sentiment.

The Govt Securities yields rose on Friday, with the benchmark yield posting its biggest weekly jump in over four months, as the RBI kept the door open for yet another hike after raising interest rates during the week. The yield rose by eight basis points (bps) this week, it had dropped 11 bps last week.

The benchmark 7.26% G S 2032 yield ended at 7.36 %, 8 basis points higher than the closing on last weekend (February 03, 2023)

State Government Securities

SDL - Primary Market Auction Cut off (Range - Yields)		
	January 31, 2023	**February 7, 2023**
2 Years	--	--
5 Years	--	--
10 Years	**7.65 – 7.69**	**7.64 – 7.67**
15 Years	**7.72 – 7.73**	--
20 Years	**--**	--

SDL - Secondary Market (Range Yields)		
	February 3, 2023	**February 10, 2023**
2 Years	**--**	**7.34**
5 Years	**--**	**7.52**
10 Years	**7.56**	**7.65**
15 Years	**7.60**	**--**
20 Years	**--**	**--**

Tracker

Trackers	**February 3, 2023**	**February 10, 2023**
Average Call Rate (%)	**5.78**	**6.61**
Net Banking System liquidity : Deficit (-) Surplus(+) (Rs Crs)	**39,665**	**(-18,035.40)**
Bank Deposit Growth (%)	**10.60**	**10.60**
Bank Credit Growth (%)	**16.50**	**16.50**

CPI (%)	**5.72**	**5.72**
Core Inflation (%)	**6.00**	**6.00**
WPI Inflation (%)	**4.95**	**4.95**

Nifty	**17,854**	**17.856.50**
Sensex	**60,841**	**60,682.70**

Re/US$	**82.21**	**82.51**
FPI Investments (US$ Bln) (Figures cumulative for Debt & Equity – Current FY)	**(-5.760)**	**(-6.680)**

Foreign Exchange Reserves (US$ Bln)	**576.76**	**575.27**

Gold/10 gm (Rs)	**57,930**	**56,780**
Gold/Oz (US$)	**1865.53**	**1864.49**
Crude Oil - Brent (US$/bbl)	**79.82**	**86.39**
2 Yr USA - Treasuries	**4.29**	**4.53**
10 Yr USA - Treasuries	**3.52**	**3.74**

The government's Budget for FY 2023-24 reinforced its commitment for fiscal deficit consolidation target of 5.90% of GDP down from 6.4% in the current fiscal year. Meanwhile, a capex boost of 37% to Rs 10 lakh crores is a positive for growth prospects over the long term. Moreover, the government market borrowings programme at Rs 15.43 lakh crores for FY24 was in line with market expectations. Fiscally prudent budget and a market borrowing in line with market expectations improved the sentiments.

The CPI inflation moderated to the year low of 5.72% in December 2022. The softening in inflation was due to easing of vegetable prices despite an increase in other components of the food basket. Core inflation, however, remained sticky at over 6% as service sector demand remained robust. Higher core inflation can be attributed to the pent-up demand, momentum in services inflation and second-round effects triggered by the supply-side shocks. The sticky core inflation poses a challenge to achieving the medium term inflation target of 4%.

The RBI MPC on 8th February 2023 decided to raise the repo rate by 25 bps in line with market expectations and kept its stance unchanged at "withdrawal of accommodation" in line with our expectations. The policy tone was more hawkish than what most market participants had expected as the RBI was concerned that they are still away from achieving their objective of durable lower inflation.

On inflation, the RBI said that while headline inflation is moderating, core inflation remains sticky. The RBI Governor stated that the RBI's current objectives remained to keep inflation expectations anchored, break the core inflation's persistence & containing the second order effects of inflation. However, the RBI remains cautious signaling readiness to act given the uncertain global macroeconomic environment and risk of re-emergence of commodity price pressure. In the coming fiscal, sticky core inflation and the evolving global scenario will remain critical for the RBI's policy action.

RBI's optimistic growth projection for GDP for FY 2024 of 6.4% are aligned with the Union Budget for FY 2023 -24. The domestic growth story has been resilient so far despite headwinds on the global front. With increasing demand, the seasonally adjusted capacity utilisation level has inched up to 74.5% in Q2 FY23 from 74.3% in the previous quarter. While domestic consumption is gaining traction, the external demand remains weak as reflected by the merchandise exports data.

CAD shot up to USD 36.4 billion i.e. 4.4% of GDP in Q2 FY23 doubling from USD 18.2 billion in Q1 FY2023. The widening in CAD was mainly led by a sharp widening in the merchandise trade deficit to USD 83.5 billion about 10.2% of GDP. However, our economy's relative resilience amid weakening growth prospects for advanced economies could aid in bringing the net portfolio investment inflows back into the positive side. Our foreign exchange reserves have shown improvement in the recent months climbing to USD 575.27 billion as on February 10, 2023. The current size of forex reserves is comfortable for an import cover for about 9.5 months. Although there has been some comfort on the forex reserves front, concerns about widening CAD and FPI volatility remains. In this backdrop, RBI will continue to maintain its vigil on the external sector developments.

The growth in credit demand has outpaced the growth in deposits and has also been pressuring the liquidity scenario. Going ahead, the liquidity surplus is expected to narrow further on the back of an increase in demand for cash towards the fiscal year-end and redemptions of Long-Term Repo Operations and Targeted Long-Term Repo Operations. However, the increased government spending and anticipated return of forex inflows could aid in easing the tightening pressure on liquidity to some extent. RBI has committed to continue to remain proactive and maintain liquidity for productive sectors.

However, the uncertain global environment and rise in commodity prices remains a risk going forward. The central bank has highlighted geopolitical tensions, tightening global financial conditions and weakening of the external demand to be the key downside risks for the domestic growth outlook.

Looking ahead, with core inflation remaining high, the incoming data, on the global and domestic front, impact of China's reopening, and domestic market volatility will be the key triggers for financial markets in the near term. Global inflation levels of the world's leading economies have been trending downwards, but the major central banks continued to maintain a cautious stance given the evolving global scenario. Nonetheless, global growth is expected to slow down during 2023. Despite softening of inflation central banks are reiterating their commitment to bring down inflation close to their targets.

Even as headline inflation is likely to moderate over the coming months, core inflation could remain sticky and if the RBI chooses to continue seeing signs of durable moderation in core inflation as an indicator for policy tightening, another 25bps rate hike in April could be a possibility. We think that a change in stance to neutral is unlikely until the RBI pauses its rate hike cycle.

Bond yields are likely to remain volatile. We expect the 10 year to trade within the range of 7.25 -7.50% in the short - term period till March 2023.

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