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GILTS MARKET UPDATE

January 30, 2023

(16/01/2032 – 20/01/2023) G Secs yields trading started with yields rising on Monday as traders turned nervous about higher borrowing in the next financial year, while elevated oil prices also dampened the sentiment. Market was seized by the expectations of higher gross borrowings by the Central Government as this will be last full-fledged budget before the next parliamentary elections that can put the fiscal deficit under stress due to some welfare measures.

Market participants are also worried about higher state debt issuances along with central government securities sales which will take the focus back on demand-supply dynamics, as the market sentiment turned cautious on fears of one more year of elevated borrowings. There are fears about an elevated borrowing calendar, which has led to a rise in yields and made the market nervous.

Government Securities – Secondary Market Yields

	January 20, 2023	January 27, 2023
2 Years	6.90	7.04
5 Years	-	7.24
10 Years	7.35	7.39
14 Years	7.40	7.46
29 Years	7.40	7.46

G Sec yields fell in the trading sessions on Wednesday & Thursday tracking the U.S. treasury yields - U.S. treasury yields dropped after data showed that the retail sales & PPI in the United States fell more than expected in December and as the Bank of Japan maintained its Yield Curve Control target that bounds their sovereign yields cap.

But the G Sec yields ended higher on Friday after easing for the last two sessions as investors remained cautious ahead of the weekly debt auction and budget extending the selloff towards the end of the day. The benchmark 10-year 7.26% GS 2032 closed at 7.35 % as against the previous week (Friday – December 13, 2022) closing of 7.30%

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

January 20, 2023				January 27, 2023			
Nomenclature				Nomenclature			
7.38% GS 2027	7000	7.1679	100.78	6.89% GS 2025	4000	7.0097	99.78
7.26% GS 2032	12000	7.3529	99.36	7.10% GS 2029	6000	7.3407	98.80
7.36% GS 2052	9000	7.4083	99.41	7.41% GS 2036	11000	7.4507	99.64
				7.40% GS 2062	9000	7.4446	99.15

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(23/01/2023 – 27/01/2023): The G Sec yields rose on Monday, the beginning of a week laden with supply, including heavy state borrowings that dampened the investors' sentiment. Further, a surge in US-Treasury yields and crude oil prices weighed on the domestic yields. Gilts closed marginally changed from the previous closing levels. This week was truncated and laden with a heavy supply of G Sec & State Govts. SDLs of Rs 63650 Crs; with SDLs issuances of Rs 25650 Crs, Sovereign Green Bonds of Rs 8000 Crs and G Secs for Rs 30000 Crs. We are seeing such a heavy quantum of issuances from the States Govts. after a long gap.

The Govt. securities traded in a narrow price range with low volumes amid lack of significant domestic cues ahead of the Union Budget on February 1, 2023. Budget remains the major focus area, with wide expectations of an elevated market borrowing, which is keeping the market nervous.

The G Sec yields rose for the second consecutive week, as market participants feared about an elevated borrowing calendar for the next fiscal where a demand shortage may play out.

The benchmark 7.26% G S 2032 yield ended at 7.39%, 4 basis higher than the closing on last weekend (January 20, 2023)

State Government Securities

SDL - Primary Market Auction Cut off (Range - Yields)

	January 17, 2023	January 24, 2023
2 Years	--	--
5 Years	--	--
10 Years	--	7.64 – 7.67
15 Years	7.55	7.64 – 7.70
20 Years	--	--

SDL - Secondary Market (Range Yields)

	January 20, 2023	January 27, 2023
2 Years	--	--
5 Years		7.54
10 Years	7.56 – 7.60	7.64
15 Years	--	7.70
20 Years	--	--

Tracker

Trackers	January 20, 2023	January 27, 2023
Average Call Rate (%)	**6.13**	**6.44**
Net Banking System liquidity - Deficit (-) Surplus(+) (Rs Crs)	**5,892**	**18,916**
Bank Deposit Growth (%)	**9.20**	**10.60**
Bank Credit Growth (%)	**14.90**	**16.50**

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

Nifty	**18,027**	**17,604**
Sensex	**60,621**	**59,330**

Re/US$	**80.98**	**81.51**
FPI Investments (US$ Bln) (Figures cumulative for Debt & Equity – Current FY)	**(-4.298)**	**(-4.209)**

Foreign Exchange Reserves (US$ Bln)	**572.00**	**573.73**

Gold/10 gm (Rs)	**58,715**	**58,810**
Gold/Oz (US$)	**1926.73**	**1927.34**
Crude Oil - Brent (US$/bbl)	**87.63**	**86.66**
2 Yr USA - Treasuries	**4.18**	**4.20**
10 Yr USA - Treasuries	**3.48**	**3.51**

WPI inflation continued to decline for the third month in a row and is also at the lowest since March 2021. Wholesale inflation eased to the lowest level in almost 2 years due to lower food, textile and mineral prices. CPI inflation has also softened to a 1 year low. Both the wholesale and retail inflation show a sharp decline in food and especially due to lower vegetable inflation. Further some other components like metals are also showing signs of decline. This should mean lower input costs for producers and also some loss of pricing power as demand moderates in the face of continued tightening in FY23. However, the core inflation was still slightly more than 6% for the 4 th straight month.

While consumer and wholesale inflation have fallen in the last two months, we now have to see how much time it will take to get sticky core inflation down. Core inflation tends to get more ingrained in the system making it difficult to reverse the trend. While goods inflation has been falling, services inflation has been inching up. But it is also likely to moderate in 2023 as pent-up demand fizzles out.

Our manufacturing sector which had already been reeling under pressure due to high raw material prices in H1 2022, is now feeling the pain of lower external demand. While overall manufacturing will feel the pain of lower external demand, the sectors with high export intensity will specifically be hit hard by the ensuing global slowdown.

During April-December this fiscal, our country's exports surged by 9% to US $332.76 billion. Imports during the period increased by 24.96% to US $551.70 billion. Despite global headwinds, our exports have still been at high. Merchandise trade deficit in December widened to US $23.89 billion as against US $21.10 billion year-on-year. However, the number was largely flat as compared to $23.89 billion in the previous month. The contraction in exports was mostly broad based with de-growth recorded in most items. But the worst for current account deficit seems to be behind us and it is likely to narrow going further. Forex reserves have climbed to a 5-month high of US $ 573.73 billion in the week ending January 27, 2023. These reserves are good enough for more than 9 months of country's imports. Macroeconomic stability is getting bolstered with inflation being brought into the tolerance range and lead indicators suggesting that the current account deficit is on course to narrow.

The external environment will remain challenging, with major economies projected to record a sharp deceleration in growth if not a recession. This implies that external demand for India will remain weak. The tightening of financing conditions globally will continue to impede growth while causing volatility in the financial markets. International food, energy and commodity prices have eased but uncertainties do remain. Inflation remains high and broad-based across countries. High policy rates for a longer duration appear to be a distinct possibility going forward.

However, with the global and domestic interest rate hiking cycle likely to stop in H 2 2023 we could see some relief for the debt market. Even though the global growth scenario looks weak, our country at present seems to be in a sweet spot being one of the very few relatively fast growing economies.

Recent data arrivals indicate that the first milestone of monetary policy is being passed – bringing inflation into the tolerance band, said the article titled 'State of the Economy' published in the January 2023 Bulletin of the RBI. The objective during 2023 is to tether inflation therein so that it aligns with the target by 2024 – the second milestone – as per the RBI Bulletin

Lastly expect the Government will to stick to its fiscal consolidation glide path of bringing down the fiscal deficit to GDP ratio to 4.5% by the FY 2025 -2026 in a staggering way starting from the FY 2023 – 2024.

Expect the RBI to remain focused on inflation and RBI have been stating so about bringing down the headline inflation to 4% and controlling the sticky core inflation, which means that the RBI is unlikely to give any dovish signal anytime soon. We expect the RBI to hike the repo rate by another 25 basis points to 6.50% in the February 2023 MPC meeting followed by a prolonged pause and do not see the central bank turning dovish in the near term.

In view of the foregoing, we expect the 10 year to trade within the range of 7.25 -7.50% in the immediate short - term period.

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