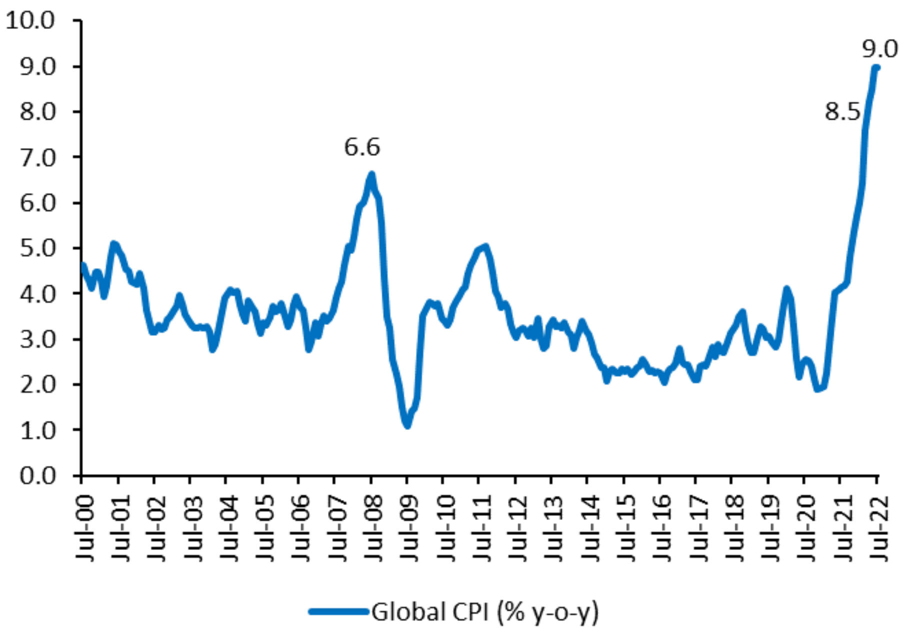
Economy and Markets

September 2022

Inflation stays elevated -drives monetary tightening across economies

Global CPI elevated at 9% y-o-y in Jul'22



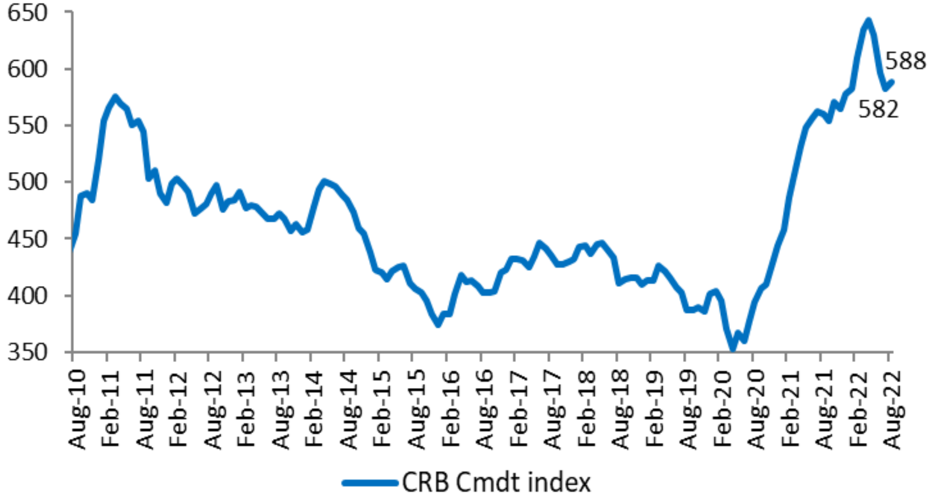
Widespread hike in policy rates across economies

Policy Rate (period end, in %)							
	2020	2021	Apr'22	May'22	Jun'22	Jul'22	Aug'22
China	4.35	4.35	4.35	4.35	4.35	4.35	4.35
India	4.00	4.00	4.00	4.40	4.90	4.90	5.40
South Korea	0.50	1.00	1.50	1.75	1.75	2.25	2.50
Taiwan	1.13	1.13	1.38	1.38	1.13	1.13	1.13
Thailand	0.50	0.50	0.50	0.50	0.50	0.50	0.75
Malaysia	1.75	1.75	1.75	2.00	2.00	2.25	2.25
Philippines	2.00	2.00	2.00	2.25	2.50	3.25	3.75
Russia	4.25	8.50	14.00	11.00	9.50	8.00	8.00
Turkey	17.00	14.00	14.00	14.00	14.00	14.00	13.00
South Africa	3.50	3.75	4.25	4.75	4.75	5.50	5.50
Brazil	2.00	9.25	11.75	12.75	13.25	13.25	13.75
Mexico	4.25	5.50	6.50	7.00	7.75	7.75	8.50
Argentina	29.00	34.50	38.00	39.50	34.00	43.00	50.00
Colombia	1.75	3.00	6.00	6.00	7.50	9.00	9.00
Chile	0.50	4.00	7.00	8.25	9.00	9.75	9.75
US	0.25	0.25	0.50	1.00	1.75	2.50	2.50
Eurozone	0.00	0.00	0.00	0.00	0.00	0.50	0.50
UK	0.10	0.25	0.75	1.00	1.25	1.25	1.75
Japan	0.10	0.10	0.10	0.10	0.10	0.10	0.10

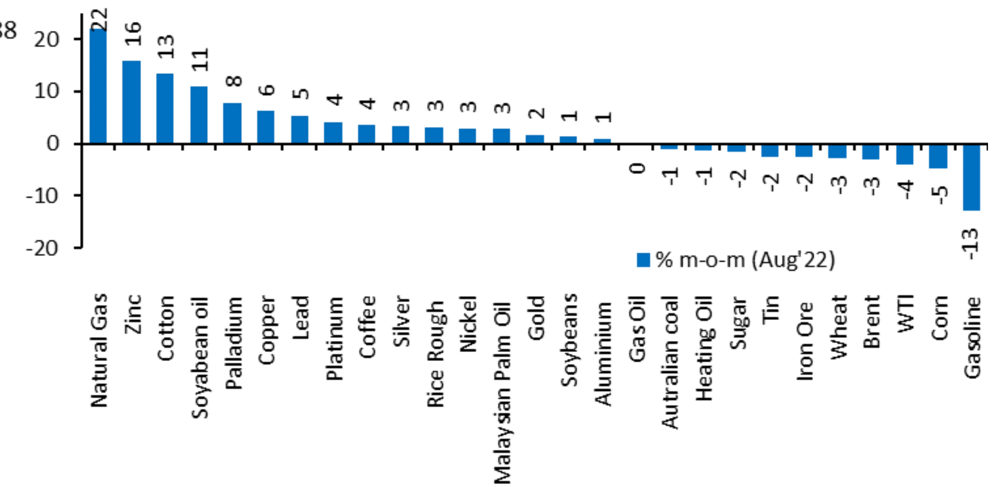
Source: CEIC, Bloomberg, SBIMF Research; Global CPI inflation is calculated by taking GDP weighted (in PPP) CPI inflation of key economies
NB: Green/Red color in 2-3 column stands for reduction/increase in policy rates viz-a-viz previous year.

Global commodity sees a marginal uptick in August

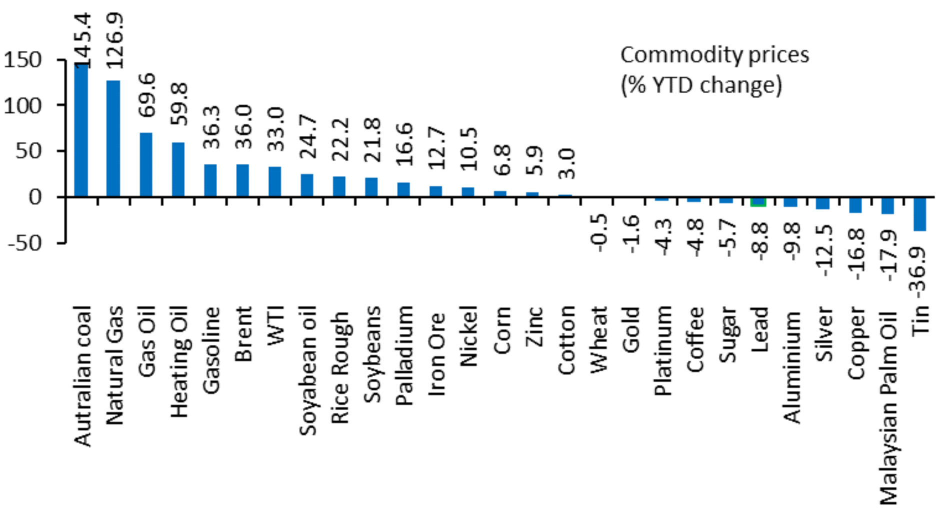
Bloomberg Commodity index sees an uptick in August after three months of softening bias



Multiple commodities across energy, metals and food basket sees a price rise in August



Energy prices have rallied on a YTD basis



- Aggressive rate hikes should eventually drive the commodities lower led by fears of softer demand
- There are emerging signs of softer trade growth across many economies and money supply growth has also been receding at a rapid pace

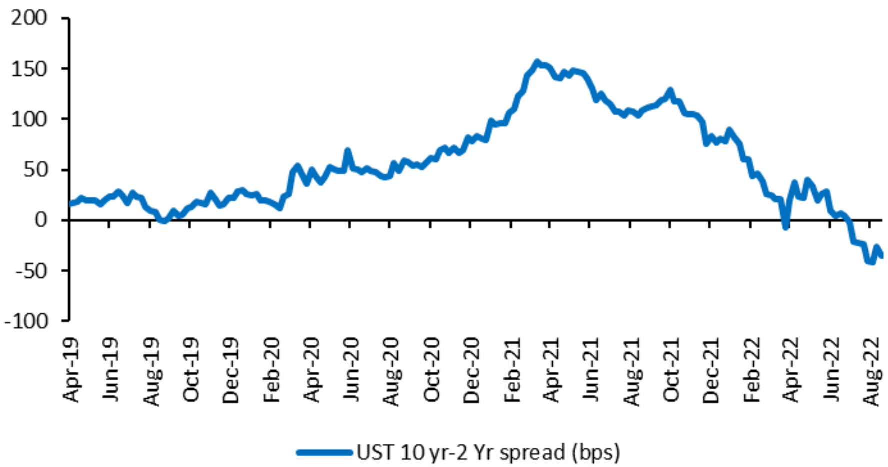
Source: Bloomberg, SBIMF Research

US Fed reiterates focus on price stability in Jackson Hole Symposium

Market continues to expect rate cuts in 2H 2023 despite the hawkish tone in latest Jackson Hole Symposium

US Fed Meeting dates	US Fed Implied Rate 30th Aug	US Fed Implied Rate 5th Aug	US Fed Implied Rate 25th July	US Fed Implied Rate 5th July
09/21/2022	3.01	3.03	2.94	2.85
11/02/2022	3.47	3.39	3.25	3.21
12/14/2022	3.69	3.56	3.37	3.37
02/01/2023	3.79	3.63	3.35	3.42
03/22/2023	3.83	3.64	3.30	3.42
05/03/2023	3.81	3.58	3.19	3.364
06/14/2023	3.78	3.48	3.09	3.262
07/26/2023	3.74	3.39	3.01	3.165
09/20/2023	3.66	3.28	2.91	3.06
11/01/2023	3.58	3.18	2.84	2.967
12/13/2023	3.49	3.08	2.77	2.897
01/31/2024	3.43	3.02	2.71	2.818

The 10yr- 2yr UST curve stays inverted since July'2022

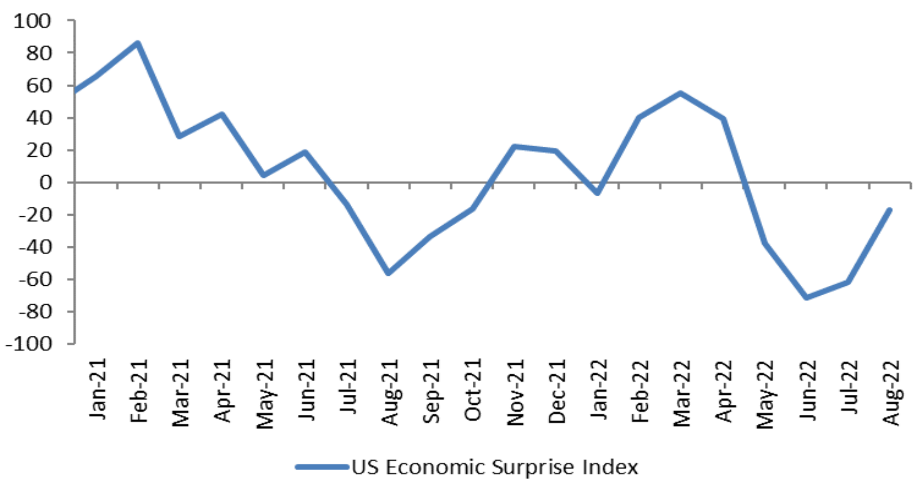


- During the latest Jackson Hole Symposium, US Fed chair gave a clear mission statement to get inflation under control.
- As per Powel's commentary, the US economy is currently showing strong underlying momentum and the labor market is particularly strong.
- There was a clear acknowledgment that tame inflation, the economy will have to live with some pain, both on the growth side and the employment side.
- The recent messaging from Fed officials - including Powell's Jackson Hole speech - has been virtually unanimous: rates will likely have to be "higher for longer".
- There has been a 20bps of upward revision to market expectation on peak Fed Funds rate post the Jackson Hole Symposium (from 3.64% to 3.83%).
- That said, market still expects this to be quickly reversed by rate cuts in 2H 2023- despite a hawkish undertones from latest Fed Commentaries.

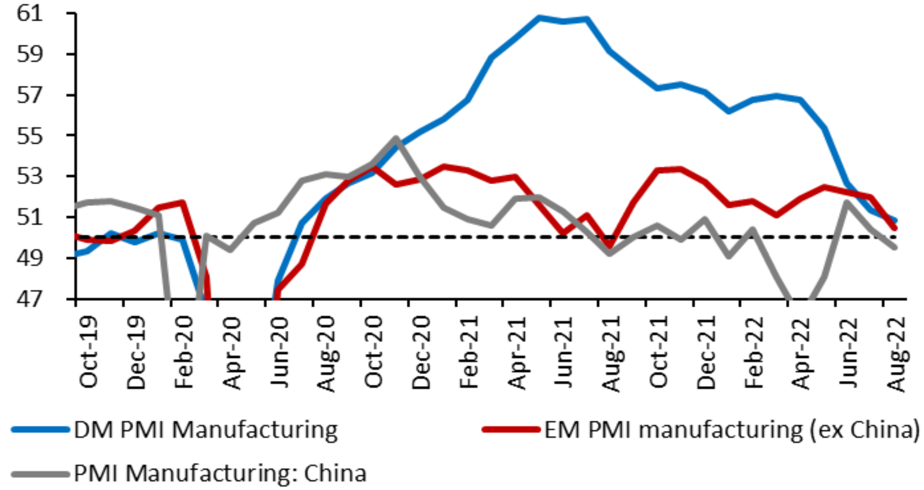
Source: US Fed, Bloomberg, SBIMF Research

Global growth underwhelms expectations; Europe in throes of energy shock

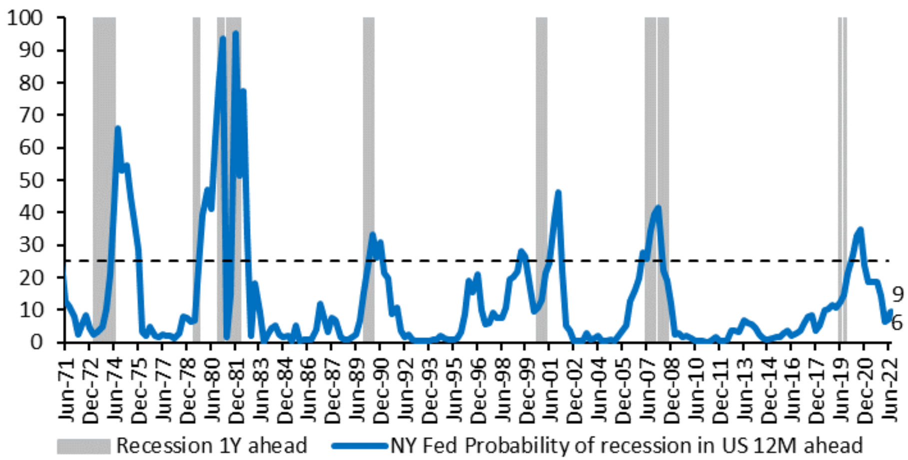
Economic activity underwhelms market expectation in last four months



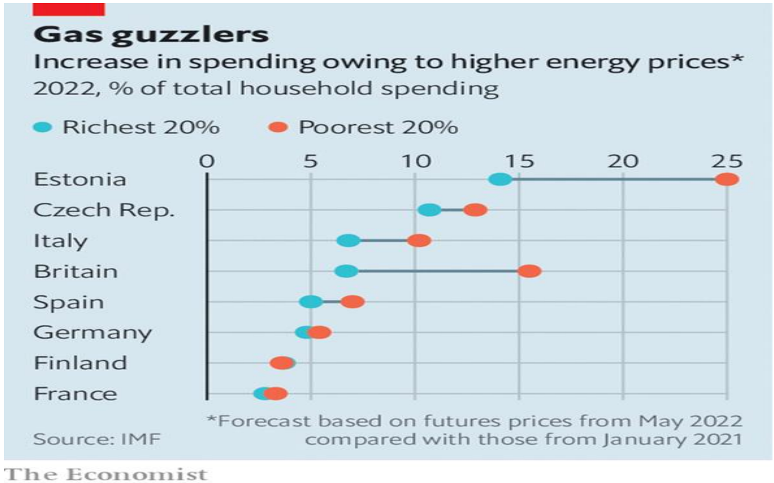
PMI manufacturing moderates though still in expansion zone



Growth moderates but low probability of recession (particularly in the US) 12 months ahead



Europe faces significant rise in energy cost denting household spending and manufacturing

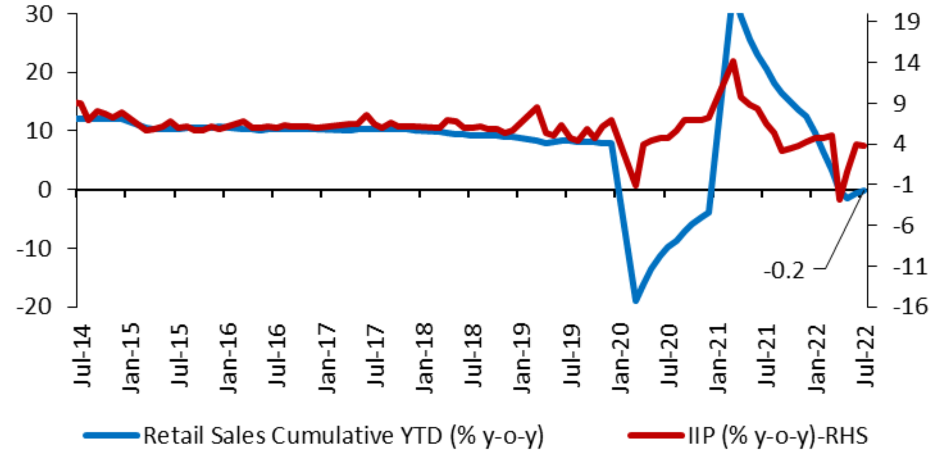


Source: CEIC, Bloomberg, SBIMF Research; NB: Negative economic surprise index indicates lower than market expectation

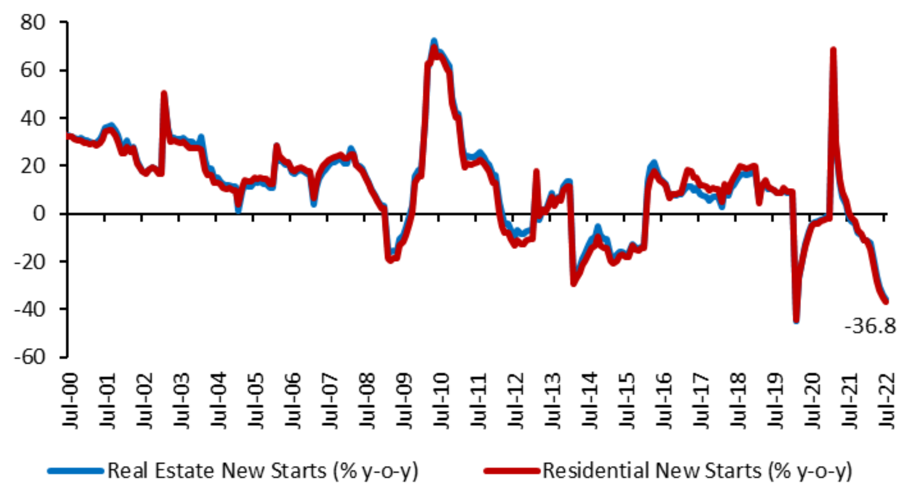
Chinese economy is beset by multiple challenges

Chinese economic activity underwhelms market expectation since May'22

Zero COVID strategy impacts industrial activity and consumer demand



Real estate stress continues; multiple instances reported around household boycotting mortgage payments

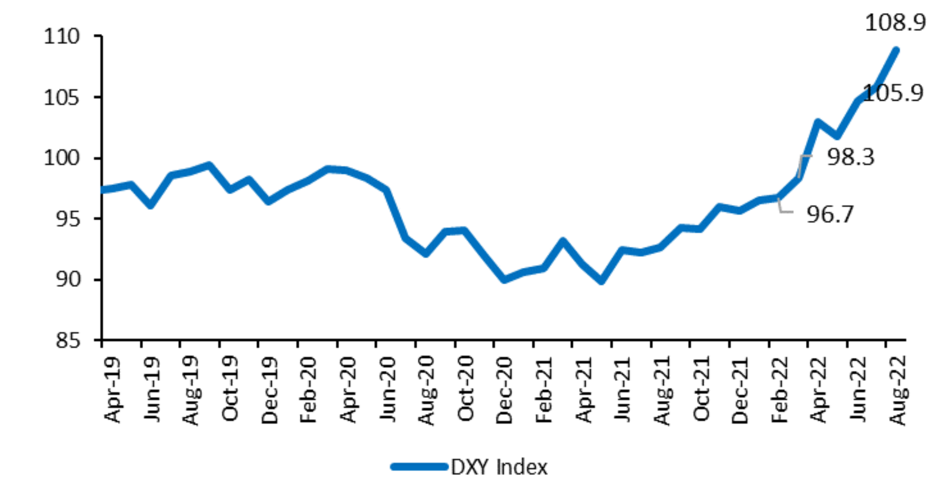


2022 growth expectation for China sees significant downgrades

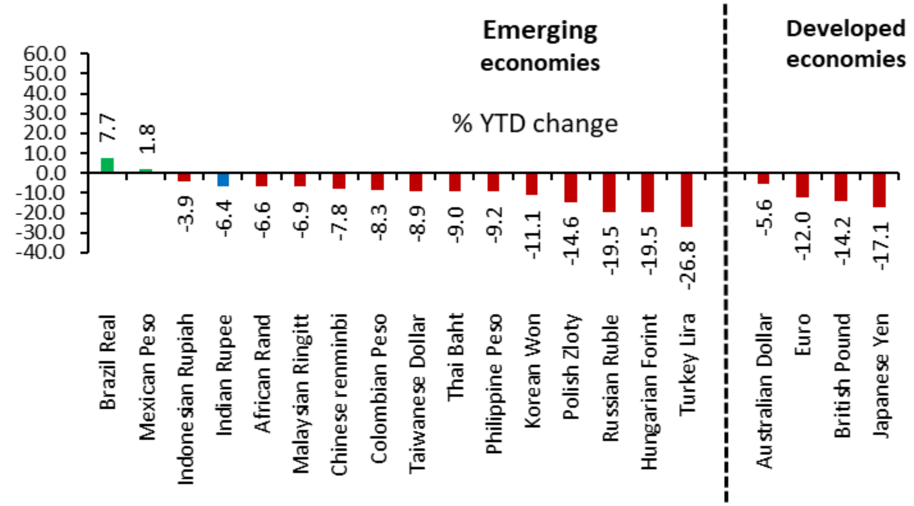
Source: Bloomberg, CEIC, SBIMF Research; ; NB: Negative economic surprise index indicates lower than market expectation

Dollar strengthens; Indian rupee an out-performer amongst EM peers

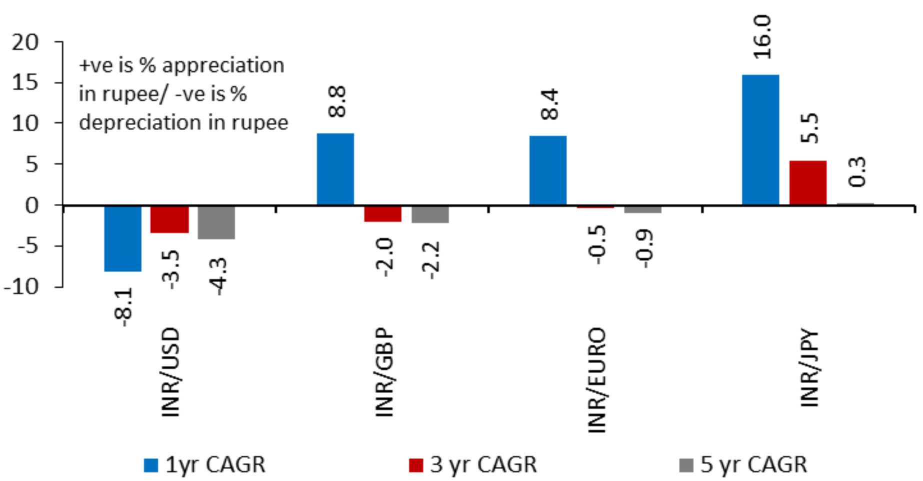
DXY has strengthened to 108.9 in Aug'22 from 105.9 in July



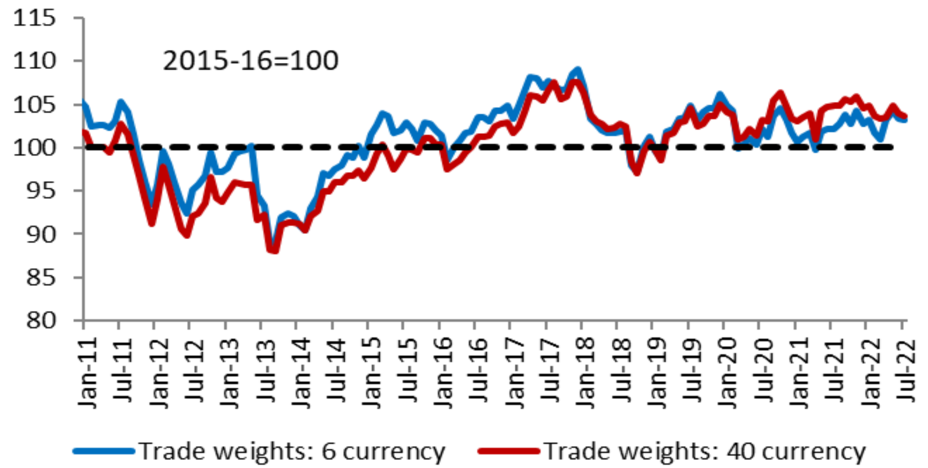
Indian Rupee depreciated by 6.4% overall in 2022 to 79.5/US$ till Aug'22; was flat m-o-m



INR appreciated against other developed market currencies



Rupee depicted marginal overvaluation of 4% in July



Source: CMIE Economic Outlook, Bloomberg, SBIMF Research

INDIA ECONOMIC ACTIVITY UPDATE

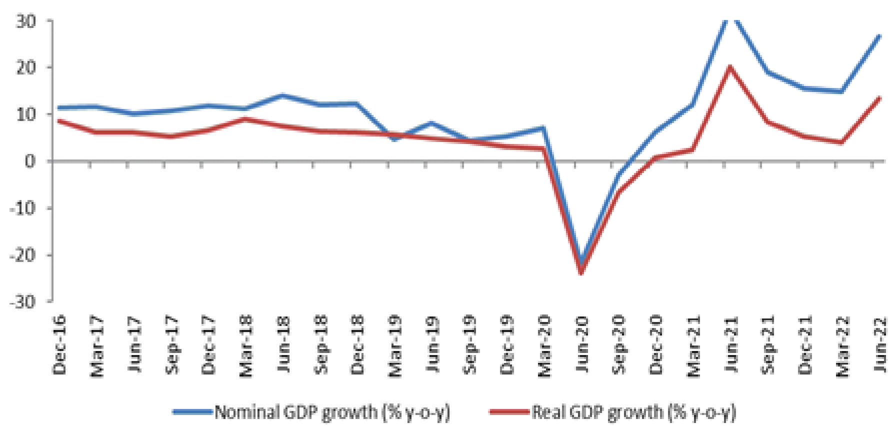
India Q1 FY23 Real GDP growth underwhelms expectation

Q1 FY23 GDP growth at 13.5% (below Bloomberg consensus 15.3% and RBI estimate 16.2%)

		% y-o-y				% 2 Yr CAGR			% 3Yr CAGR
	% Share in GDP (in FY22)	Q2 FY22	Q3 FY22	Q4 FY22	Q1 FY23	Q2 FY22	Q3 FY22	Q4 FY22	Q1 FY23
Real GDP	**100**	**8.4**	**5.4**	**4.1**	**13.5**	**0.6**	**3.0**	**3.3**	**1.3**
Private Consmption	**57**	**10.5**	**7.4**	**1.8**	**25.9**	**0.7**	**3.9**	**4.1**	**3.2**
Government Spending	**11**	**8.9**	**3.0**	**4.8**	**1.3**	**-8.4**	**1.3**	**16.2**	**3.1**
Gross Capital formation	**36**	**26.8**	**8.4**	**5.2**	**19.3**	**9.1**	**3.2**	**8.5**	**2.1**
GFCF	32.5	14.6	2.1	5.1	20.1	4.6	0.7	7.6	2.2
Change in Stocks	1.3	NA	NA	NA	NA	32.8	31.4	35.1	10.2
Valuables	2.0	171.7	53.0	-48.9	49.3	79.3	44.9	14.6	-7.4
Exports	**22**	**20.7**	**23.1**	**16.9**	**14.7**	**6.2**	**6.1**	**10.1**	**6.3**
Imports	**26**	**41.0**	**33.6**	**18.0**	**37.2**	**7.6**	**12.5**	**14.8**	**9.2**

Change in Stocks- y-o-y growth is NA as data turns from negative to positive

Nominal GDP growth at 26.7% y-o-y in Q1FY23 while real GDP growth is at 13.5%

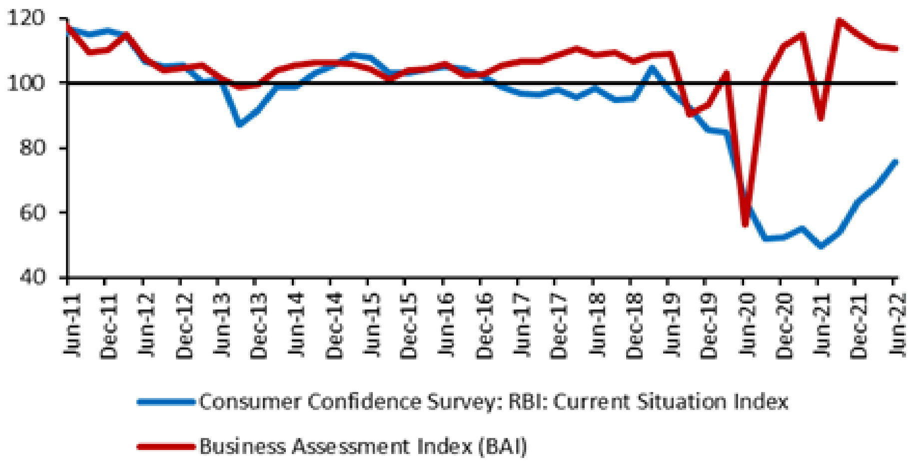


- Q1 FY23 GDP growth came at 13.5% y-o-y (Bloomberg Consensus: 15.3%, RBI 16.2%). The print was below expectation.
- Nominal GDP grew 26.7% y-o-y, led by a deflator which grew 11.6% y-o-y.
- There is a widening gap between Nominal and real demand growth, implying that high inflation dents the volume growth in national output

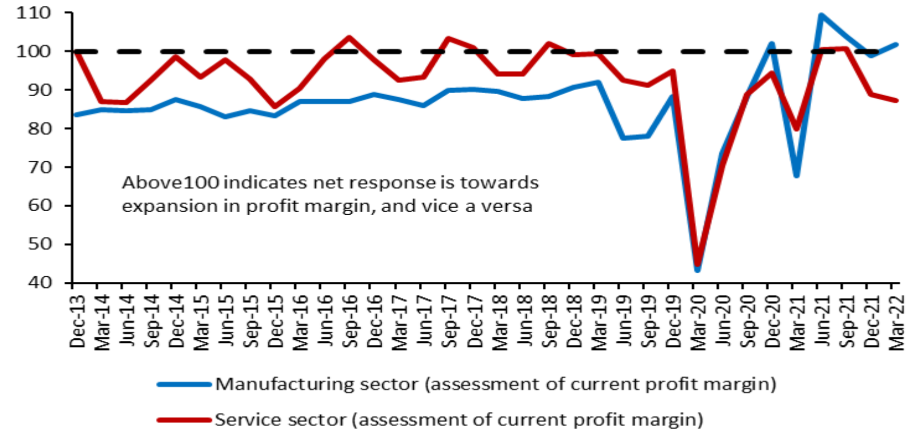
Source: CMIE Economic Outlook, SBIMF Research

Dichotomy in business and consumer confidence

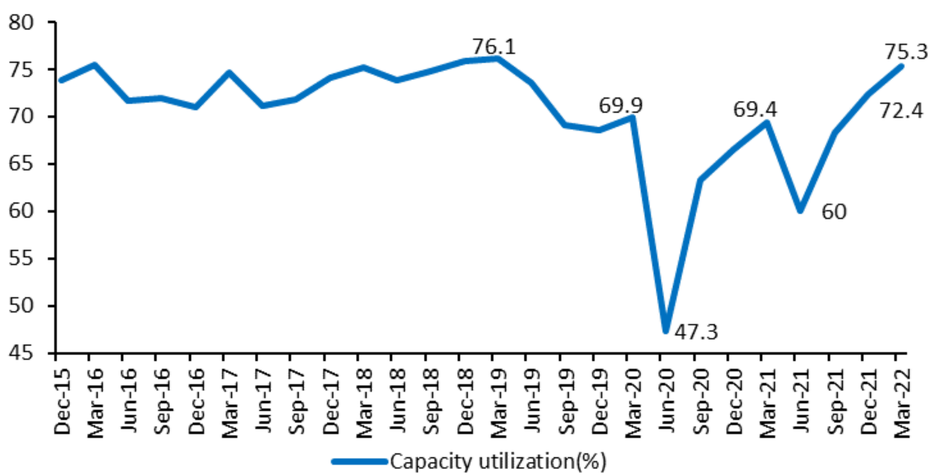
Consumer sentiments are pessimistic while business are significantly optimistic about current economic situation



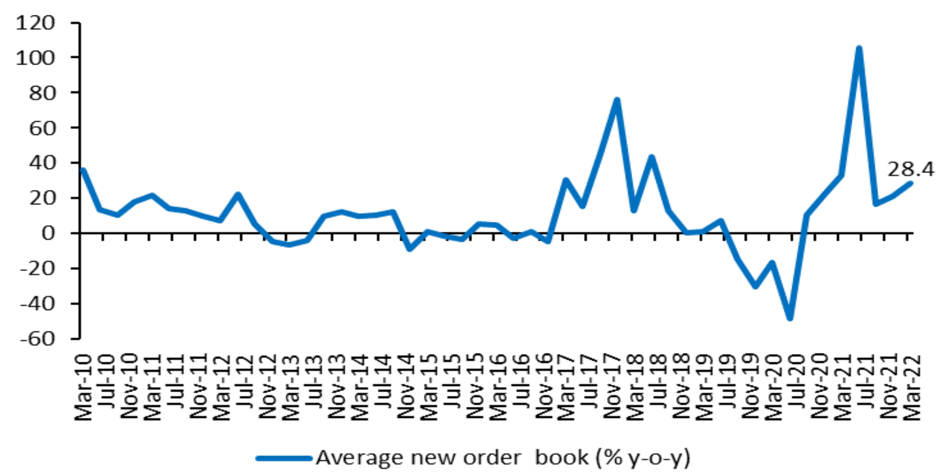
Manufacturing sector optimistic about current and future profitability



Capacity utilisation is at a three year high



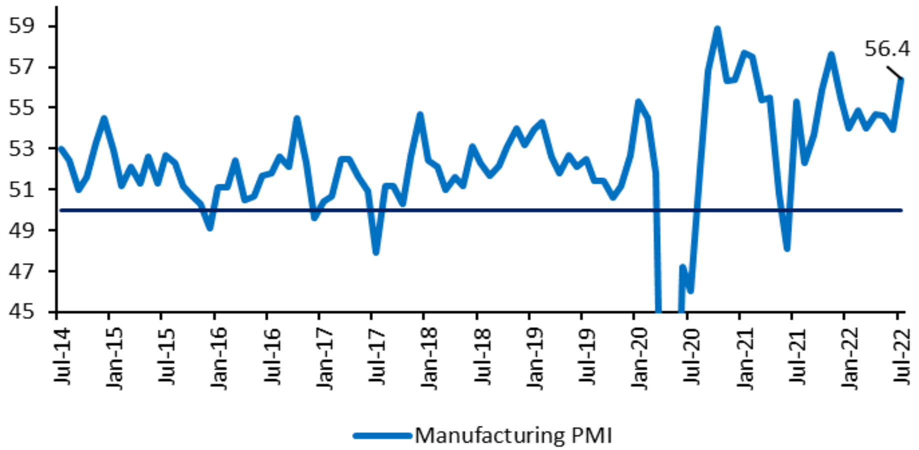
Average new order book (RBI OBICUS survey) for business is improving



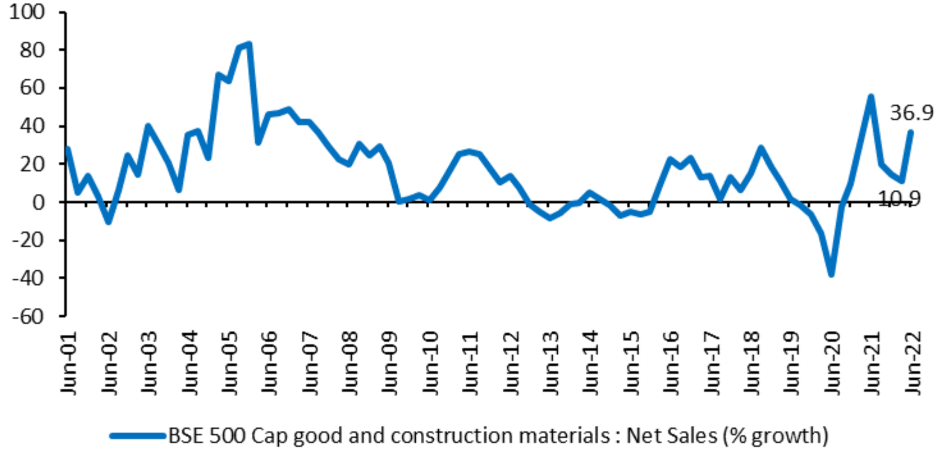
Source: CEIC, RBI OBICUS, SBIMF Research

Signs of pick up in business capex

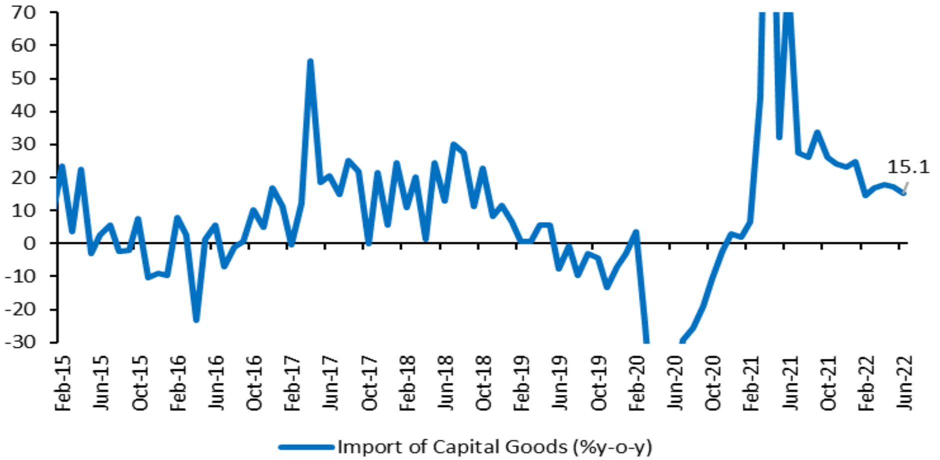
Manufacturing PMI indicates business in expansionary mode



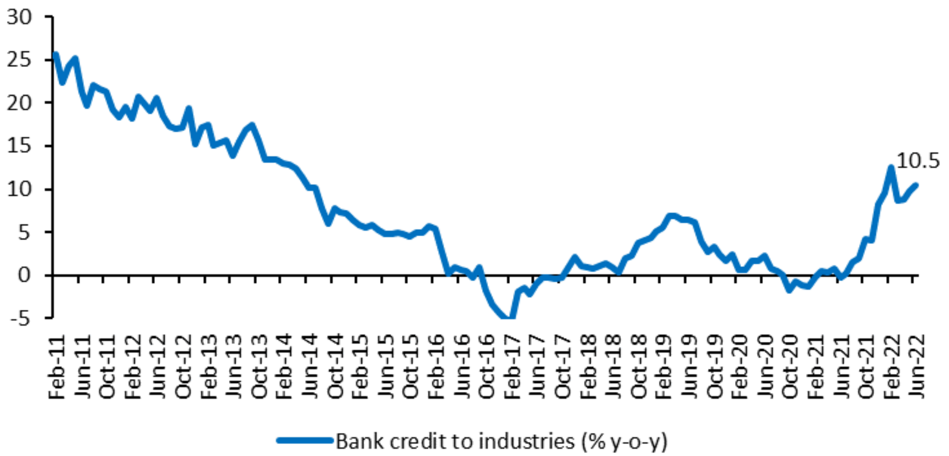
Increased sales for capital goods and construction materials (37% y-o-y)



Import of capital goods sees double digit growth



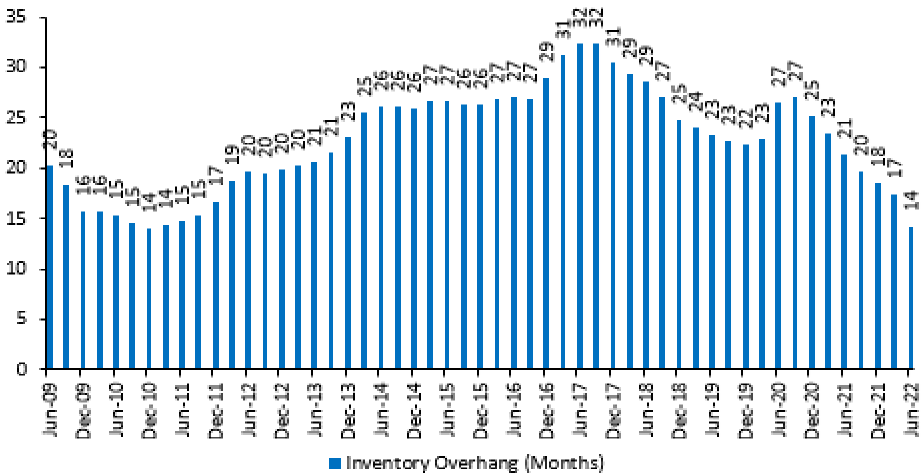
Banking lending to industries improving from abysmally low disbursals seen from 2019-21



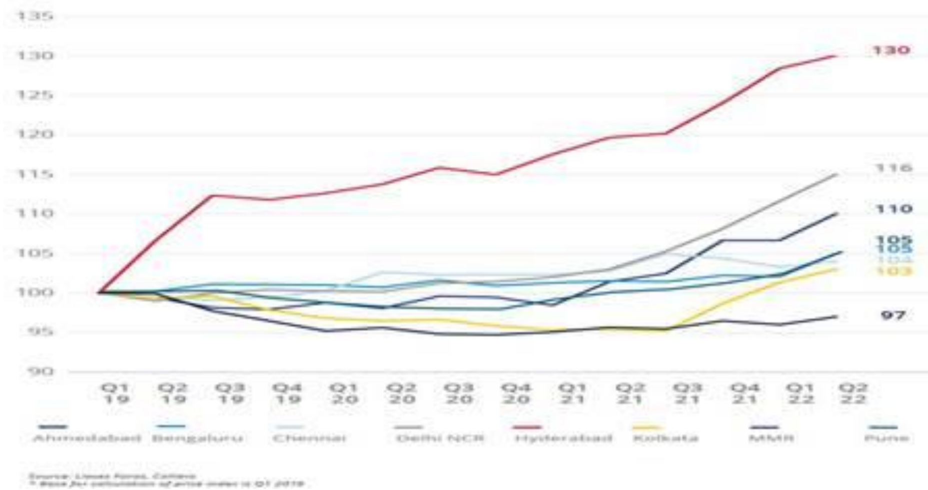
Source: CMIE Economic Outlook, RBI, SBIMF Research

Residential real estate sector prospects are improving

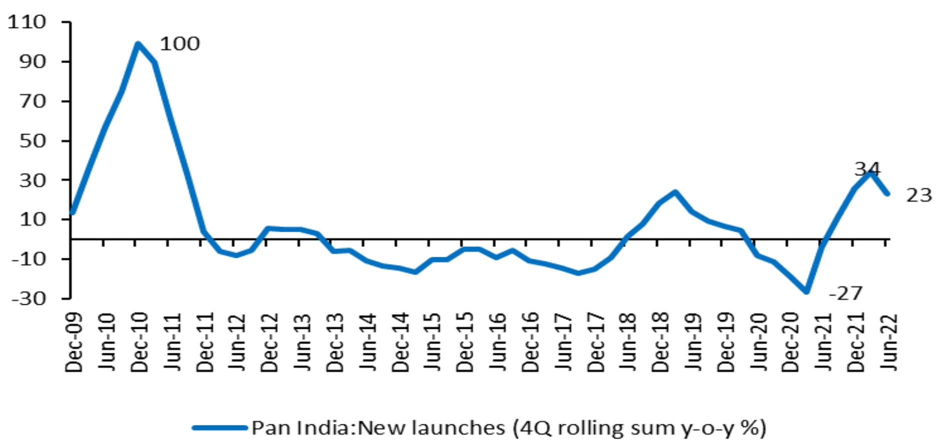
Unsold inventory has reduced materially in recent quarters



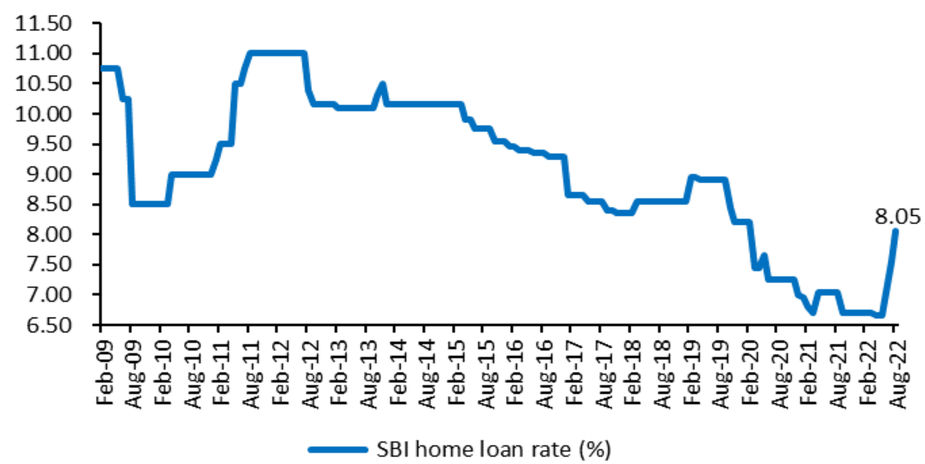
Housing prices have started to rise



New launches have increased at the margin in Q2 2022



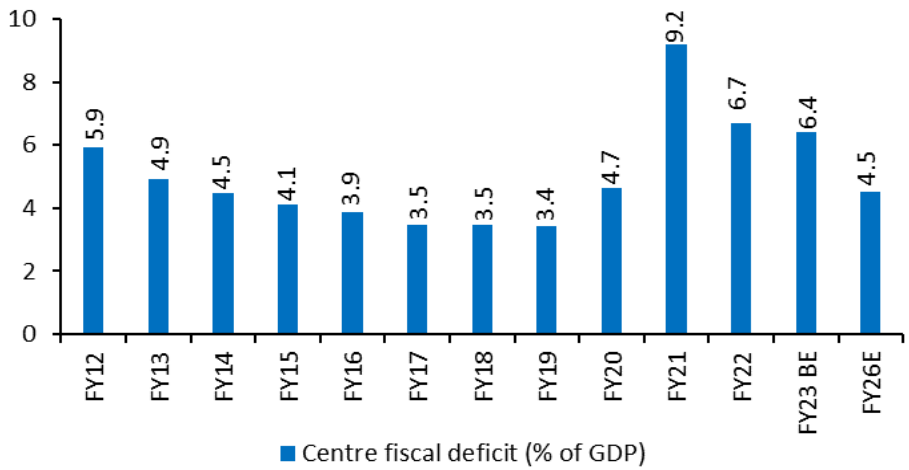
Home loans rate are increasing; but still at affordable level



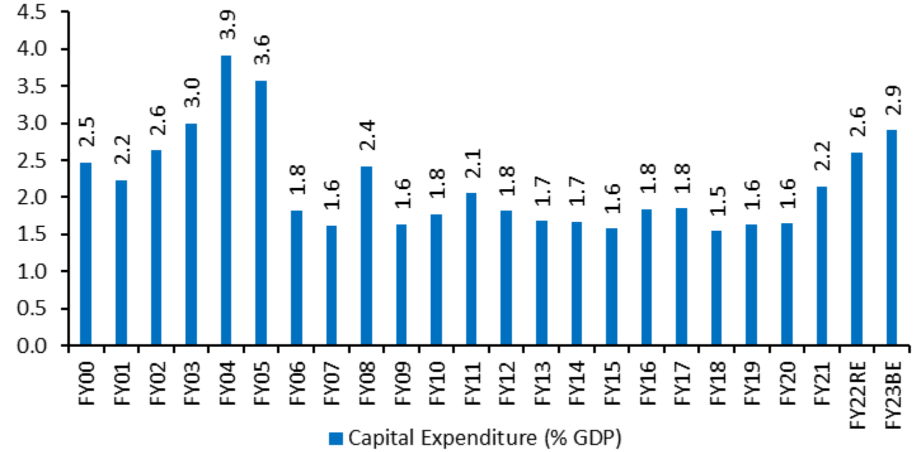
Source: PropEquity, JMFL, SBIMF Research; NB: Housing price index from CREDAI report

Government capex spend is growth supportive

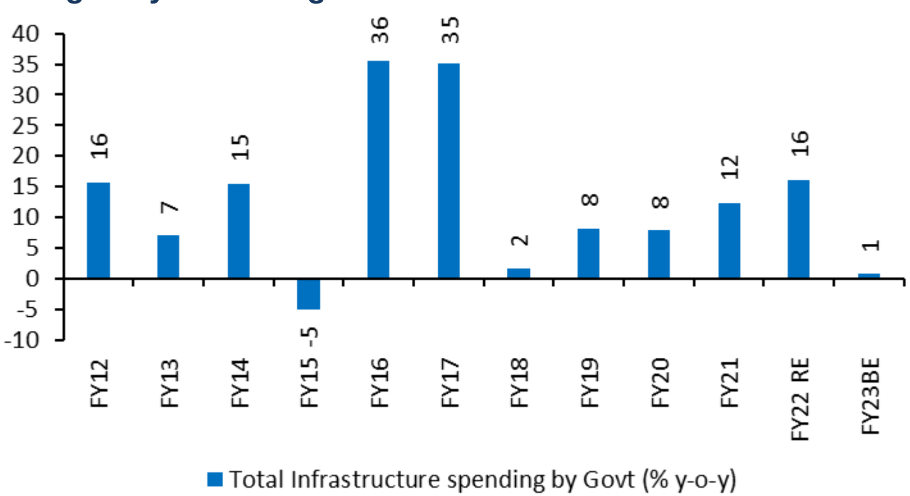
Government relaxes its fiscal consolidation agenda



Government capex as a % of GDP has increased significantly



Government infrastructure spending budgeted to increase marginally over a high base in FY22*

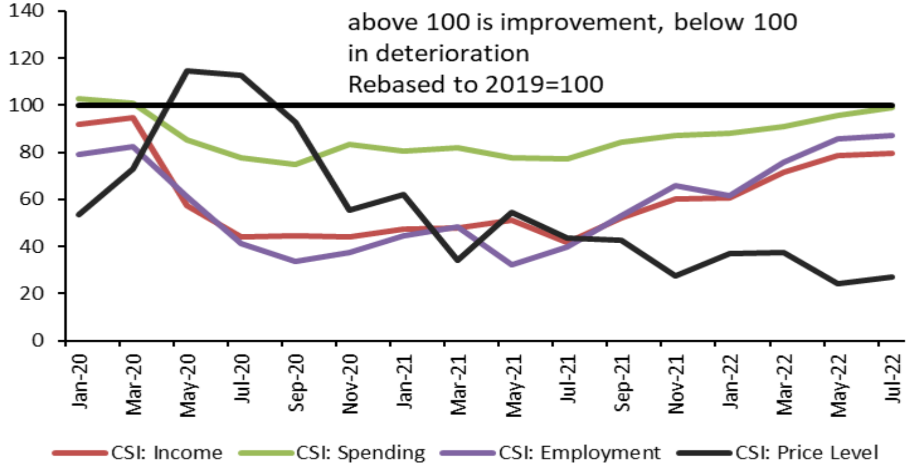


- FY23 fiscal deficit budgeted at 6.4% of GDP in FY23 compared to 6.7% fiscal deficit in FY22.
- Capex growth is strong. Out of Rs. 7.5 trillion budgeted at FY23 capex, Rs. 2.08 trillion has been spent in Apr-Jul’22 (62% higher than a year ago).
- Central Government infrastructure spending is budgeted at Rs. 9.8 trillion for FY23 in line with FY22 revised estimates.

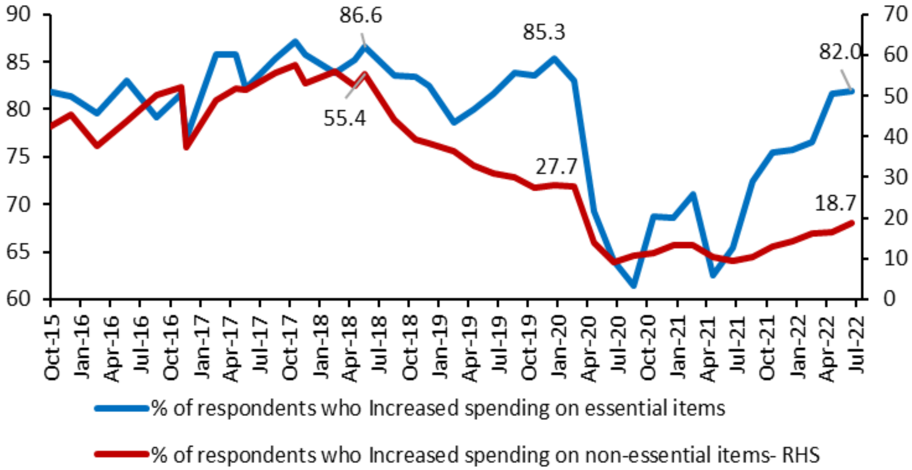
Source: CMIE Economic Outlook, RBI, SBIMF Research; NB:* SBIMF calculation

Rising prices are the biggest drag on consumer sentiments and spending

Consumer perception for income and employment is improving while that for price is deteriorating



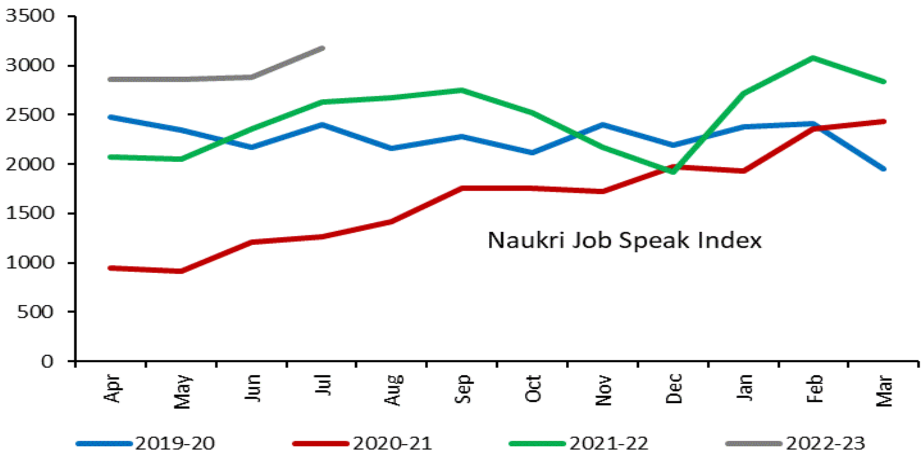
Spending on essential items is close to pre COVID levels while spending on nonessentials lag pre COVID optimism



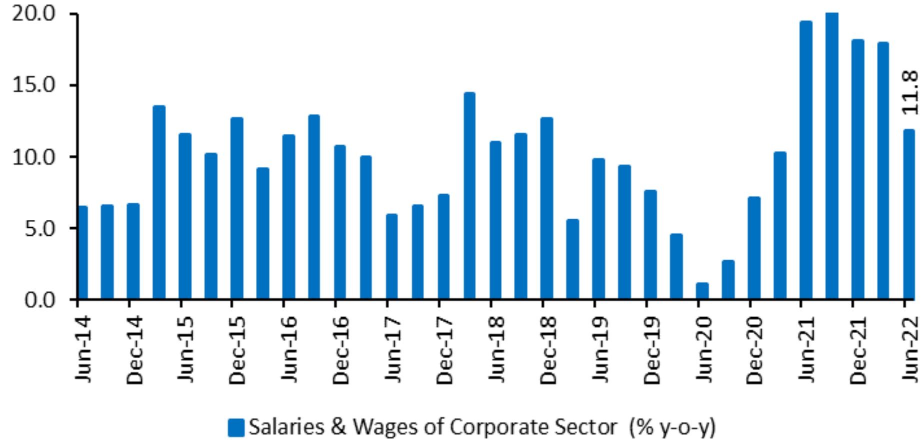
Source: RBI consumer confidence survey, SBIMF Research; NB: CSI refers to Current Situation Index

Formal sector jobs and wages improves; rural wage still benign

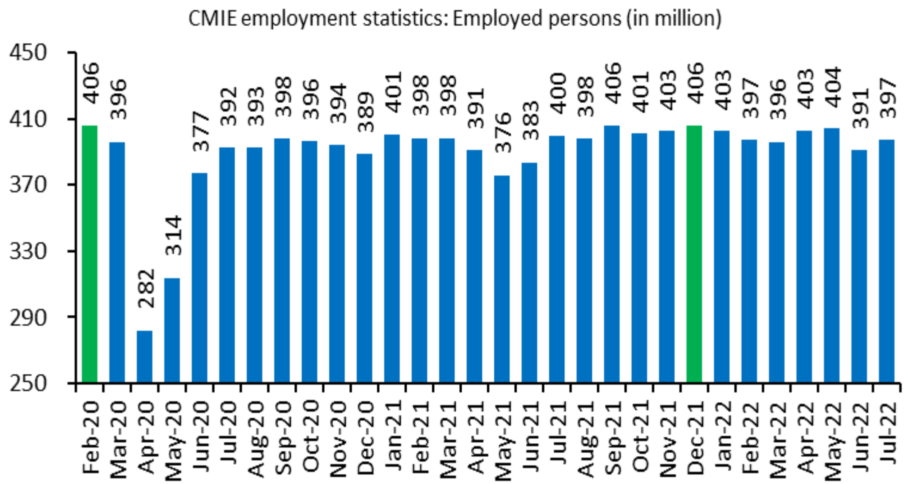
Naukri Job Speak Index is showing continued robustness in the formal job market



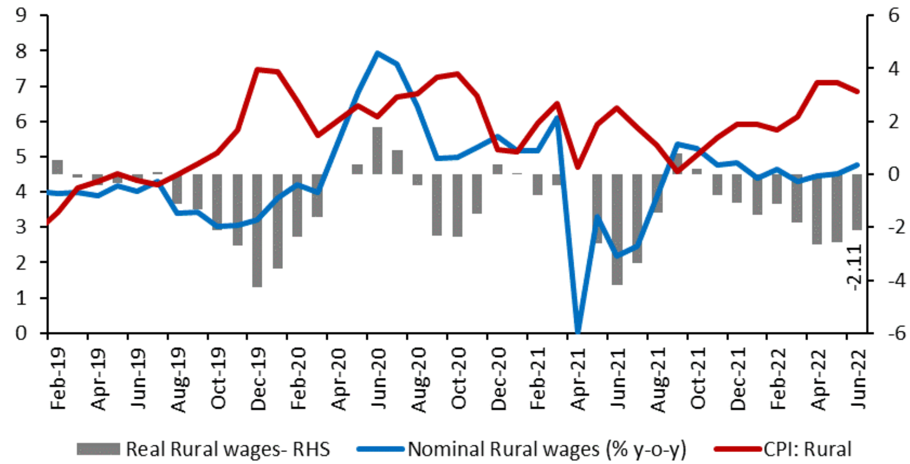
Nominal salaries and wages continue to grow in double digits in the Jun'22 quarter in the corporate sector



CMIE data shows that overall employment levels are yet to reach pre COVID levels in July'22



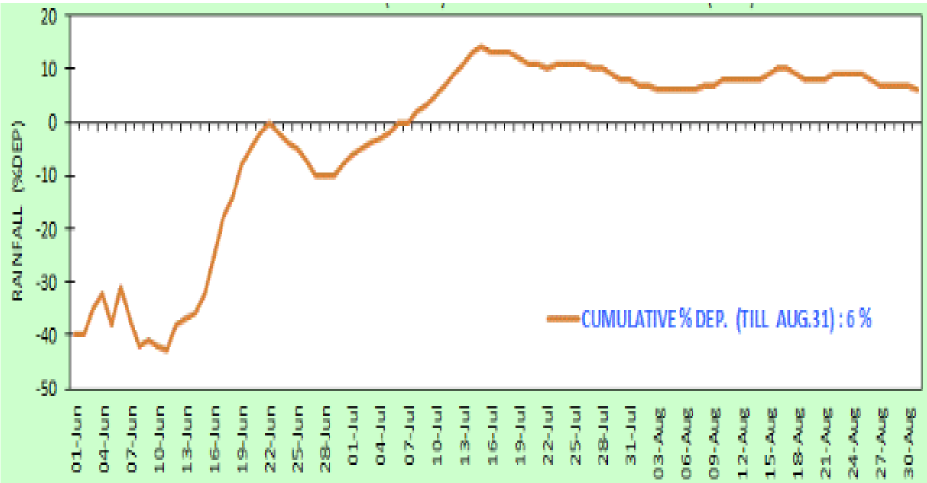
Rural wage depict 4-5% growth; real rural wages continue to be in negative territory



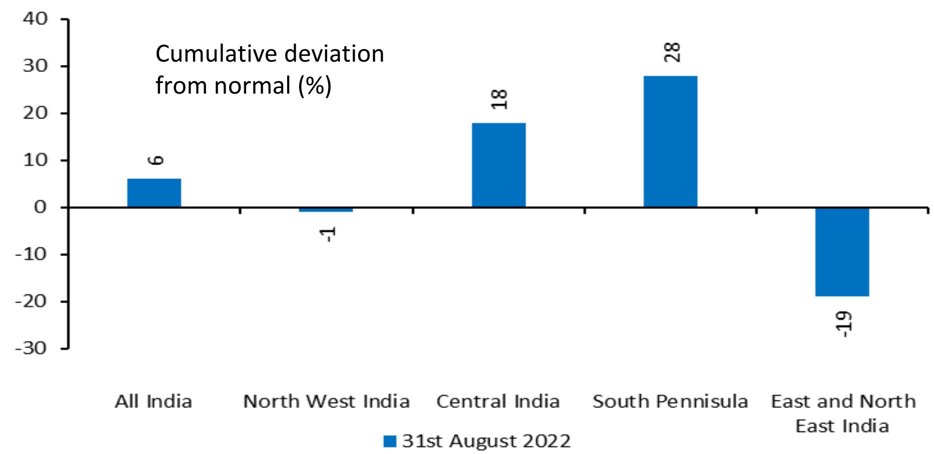
Source: CMIE Economic Outlook, SBIMF Research

Spatial distribution in rain to be watched out for rural economic health

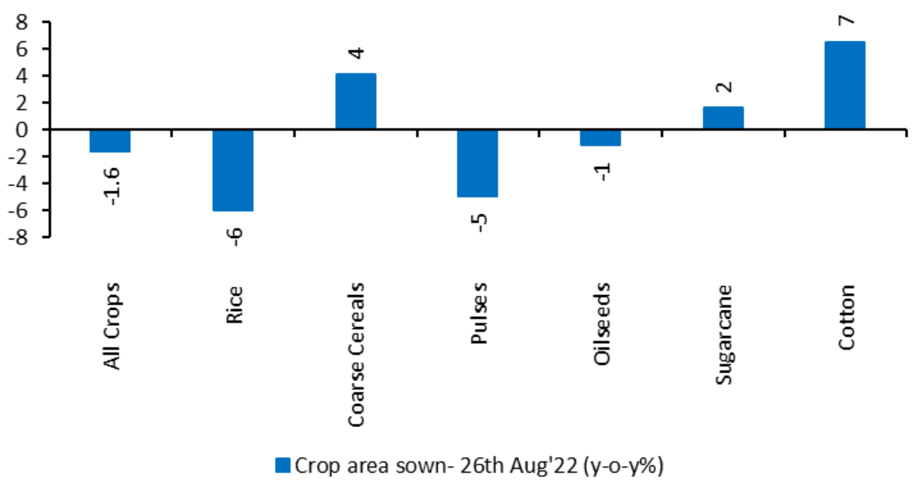
PAN India monsoon above normal…



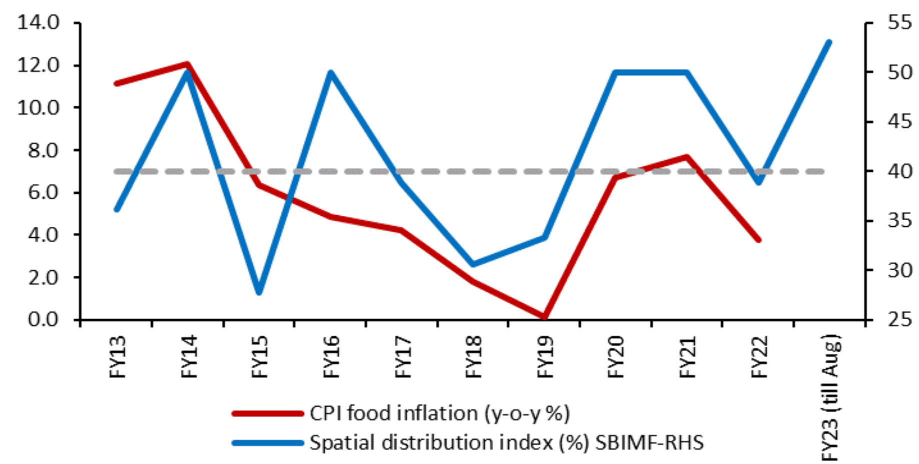
…but sharp diversion in spatial distribution of rain



Deficiency in Eastern belts; Rice sowing suffers



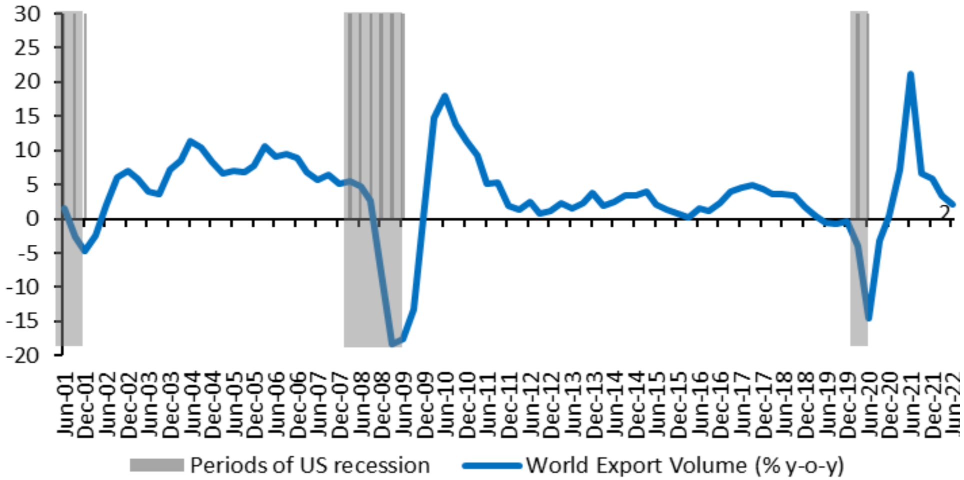
Dispersion in spatial distribution casts some initial worry on food prices



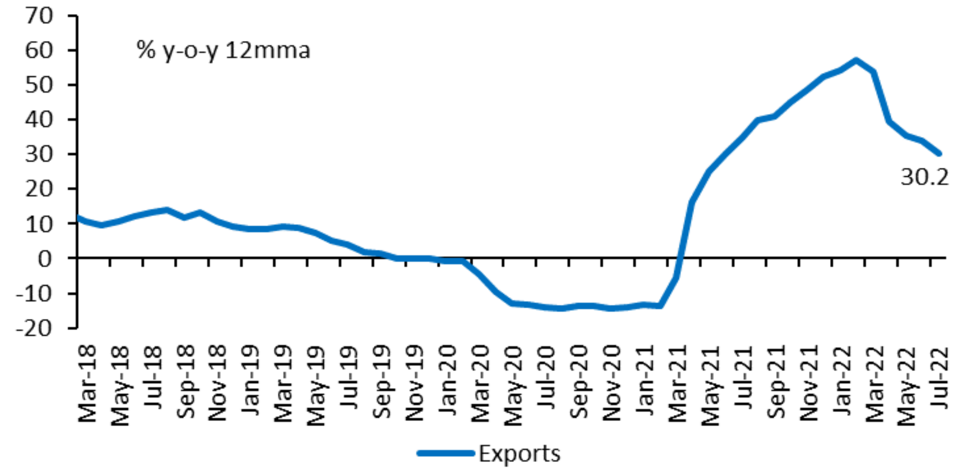
Source: CMIE Economic Outlook, IMD, CEIC, SBIMF Research; NB: A value for 50% for the spatial distribution index means that rainfall in half of the 36 subdivisions are either above or below 20% normal

Headwinds to Indian exports from weakening global trade cycle

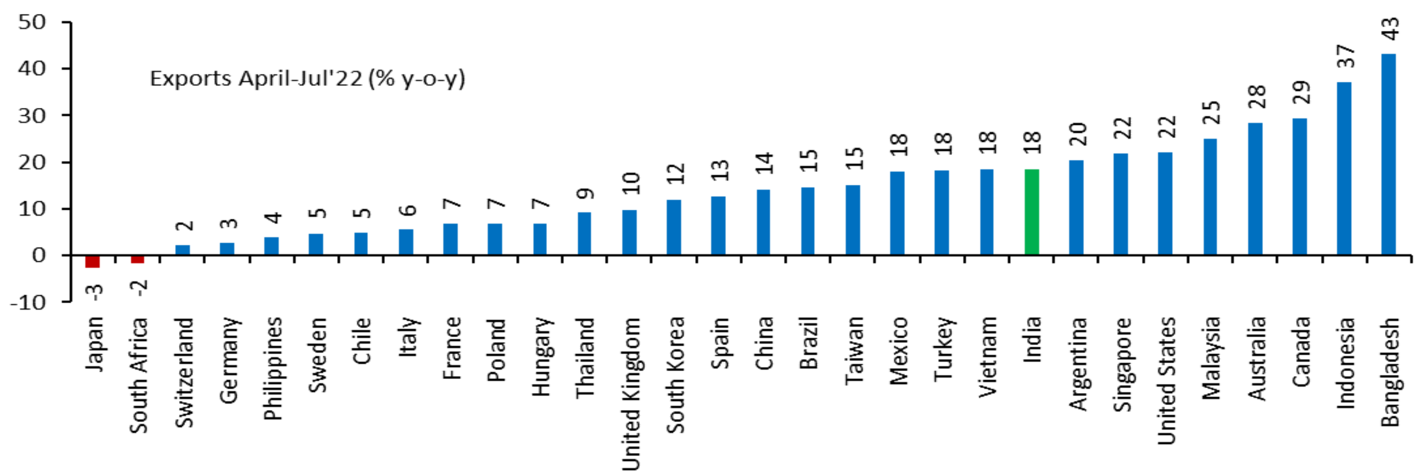
Global trade activity is likely to moderate as trade activity contracts during periods of recession



India's exports growth faces some moderation



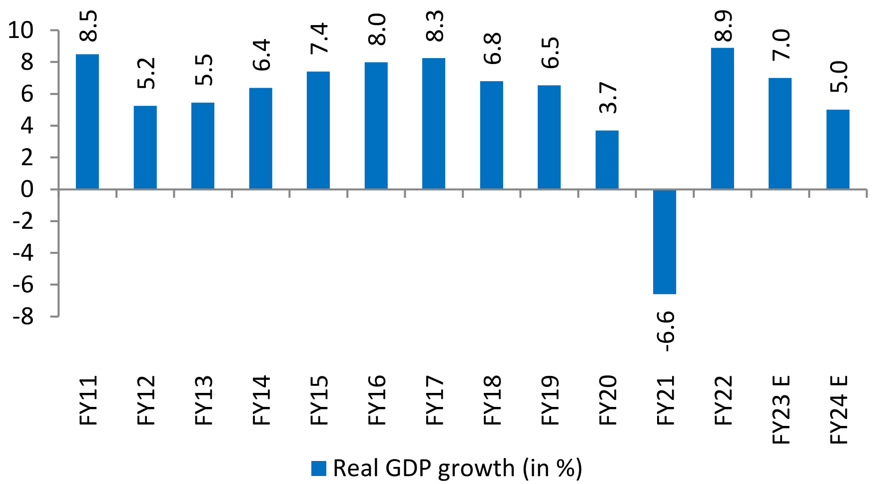
India's exports outperform peers owing to China plus one strategy and energy crisis in Europe



Source: CMIE Economic Outlook, CEIC, SBIMF Research

India’s growth to moderate in FY23 and FY24

Real GDP growth for FY24 to be ~5% vs. 7% in FY23 but that could still be better than global peers



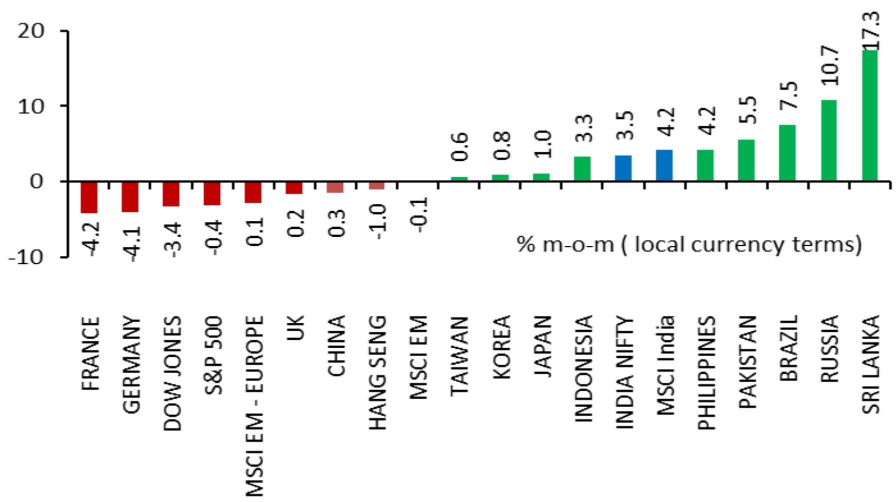
- Q1 FY23 GDP growth at 13.5% underwhelmed market and RBI expectations of 15-16% growth.
- High inflation impacts the volume growth in household spending.
- This coupled with the likelihood of peak in exports growth dents the overall growth outlook, even as we see signs of pick-up in overall capex activity.
- Even though India’s manufacturing sector and exports benefit from China plus one strategy and Europe’s energy crisis, global trade is moderating rapidly. This will lead to moderation in Indian exports.
- To sum, capex cycle (30% of India’s GDP) looks bright, export is likely to weaken from here on (20% of GDP) and consumption demand will depict a gradual recovery.
- Against this backdrop, and particularly given the weakening growth in China, Europe and US in 2024, India is likely to feel the heat.
- We stay a tad bearish on growth. There is a downside risk to FY23 growth expectation of 7% and we pencil a 5% growth for FY24- significantly lower than consensus expectation of 6-6.5%.

Source: CMIE Economic Outlook, SBIMF Research

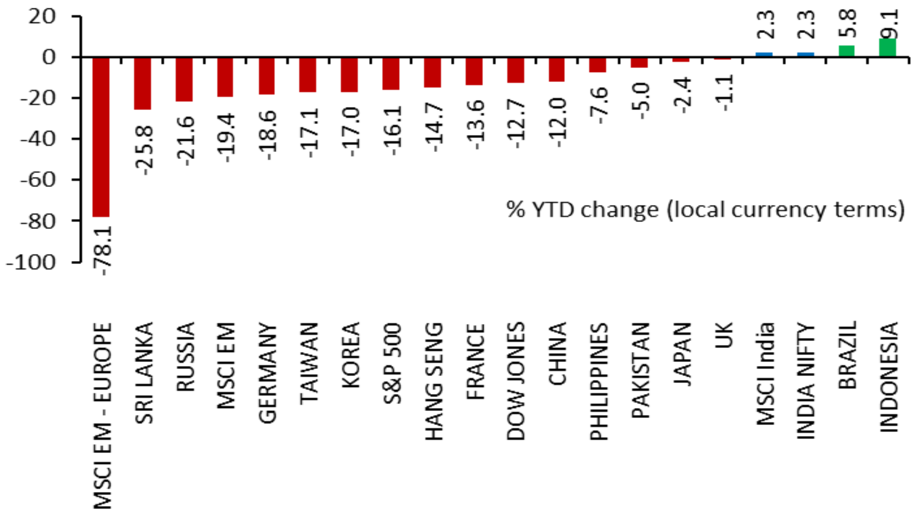
EQUITY MARKET

Indian equity outperforms global peers in August 2022

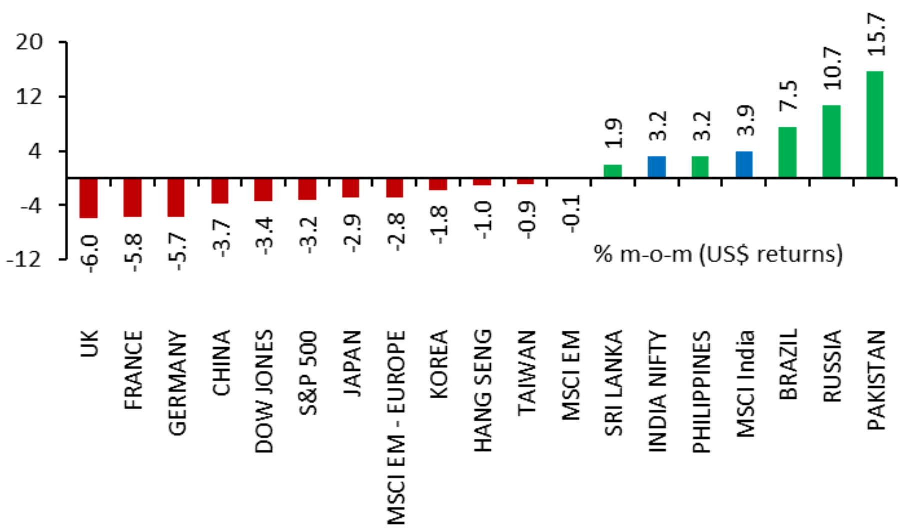
Performance in August 2022 (local currency returns)



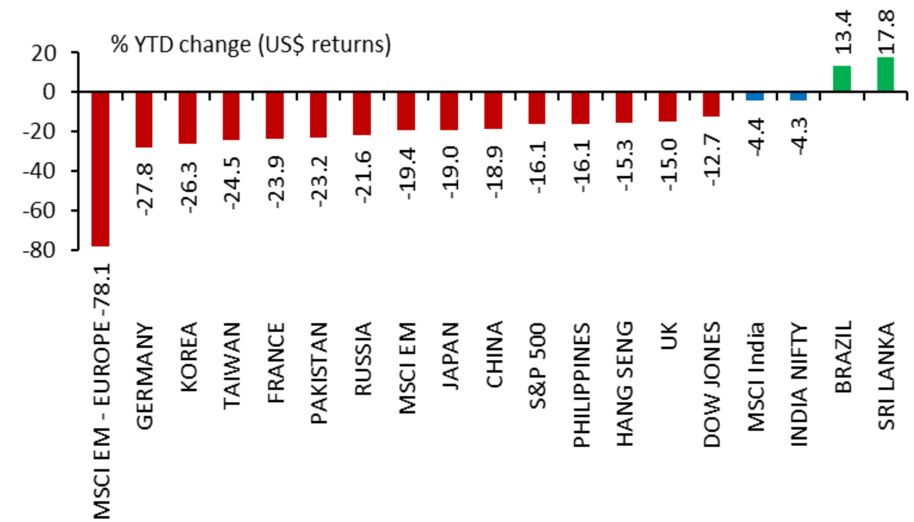
YTD performance (local currency returns)



Performance in August 2022 (US$ returns)



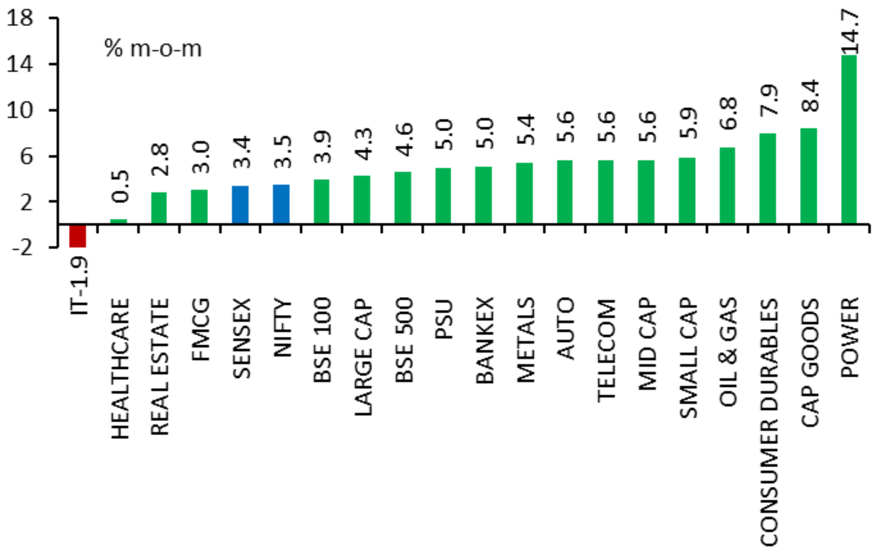
YTD performance (US$ returns)



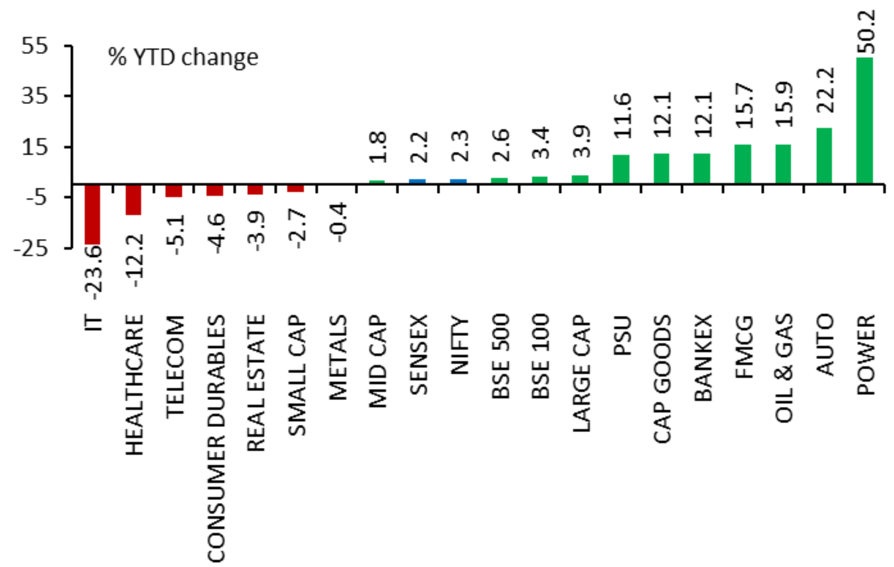
Source: Bloomberg, SBIMF Research

Indian equity market rallies for second month in succession

Performance in August 2022 (local currency returns)



YTD performance (local currency returns)

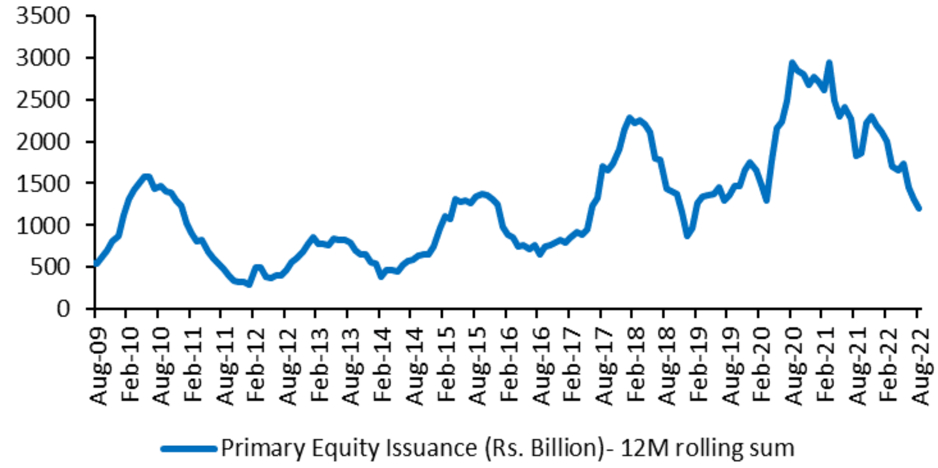


- Nifty and Sensex increased by 3.5% and 3.4% m-o-m respectively. Among sectors, all sectors outperformed on a m-o-m basis except IT, power (15%), capital goods (8%) and consumer durables (8%) delivering the highest returns.
- Small cap (5.9%) outperformed in Aug'22 vs. Jul'22 followed by mid cap (5.6%) and large cap (4.3%).
- On YTD basis, Nifty and Sensex increased by 2.3% and 2.2% respectively. Among sectors, Power (50.2%), Auto (22.2%), FMCG(15.7%) and Oil& Gas (15.9%) outperformed. On the other hand, IT (-)23.6%, Consumer durables (-)4.6%, Healthcare (-)12.2% and Telecom (-)5.1% delivered the sharpest negative returns on YTD basis

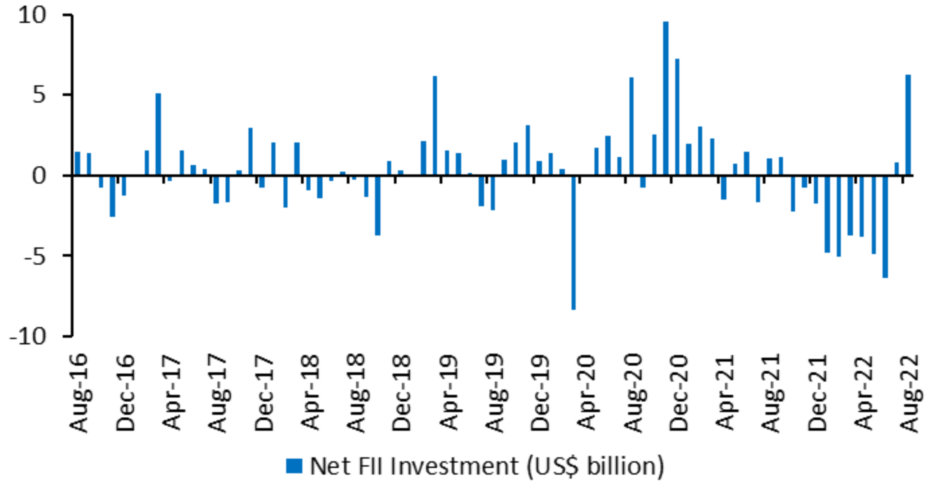
Source: Bloomberg, SBIMF Research

Liquidity: FII turn net buyers in July and August'22

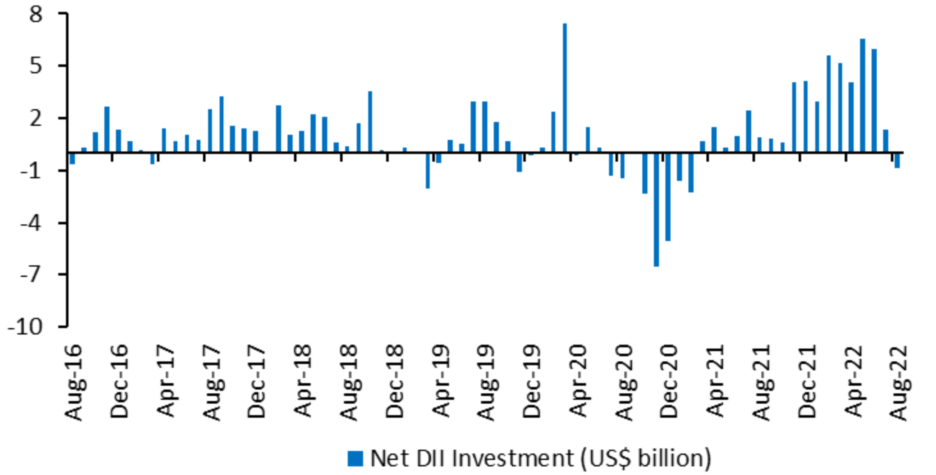
Primary issuances fall further in August'22 after observing an improvement in May'22



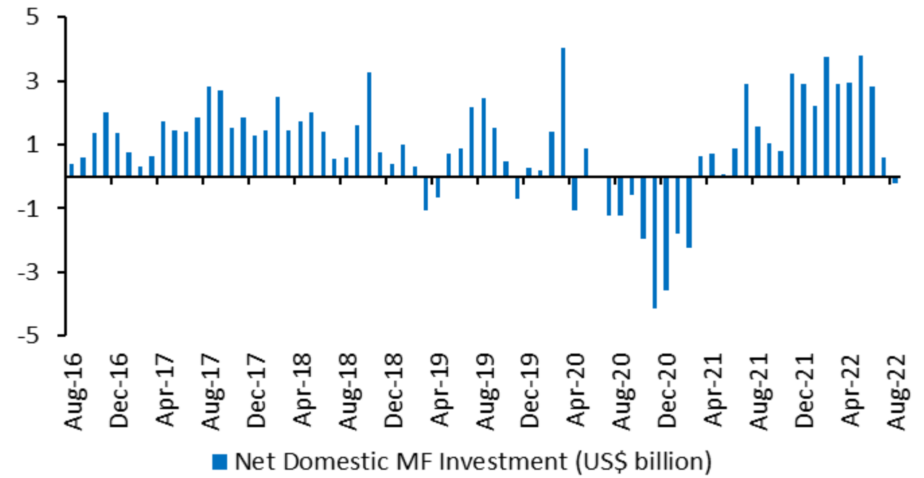
FIIs bought USD 6.26 billion in Aug'22 in equity segment vs. a buy of USD 0.84 billion in Jul'22



DIIs turn net sellers (sell of USD 0.9 billion in Aug'22 vs. buy of USD 1.3 billion in Jul'22)



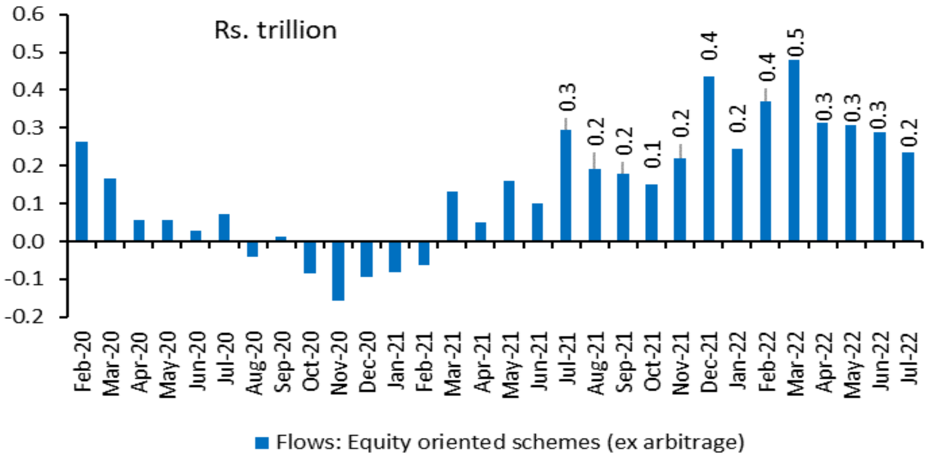
Mutual funds sold USD 0.2 billion in Aug'22 vs. a buy of USD 0.6 billion in Jul'22



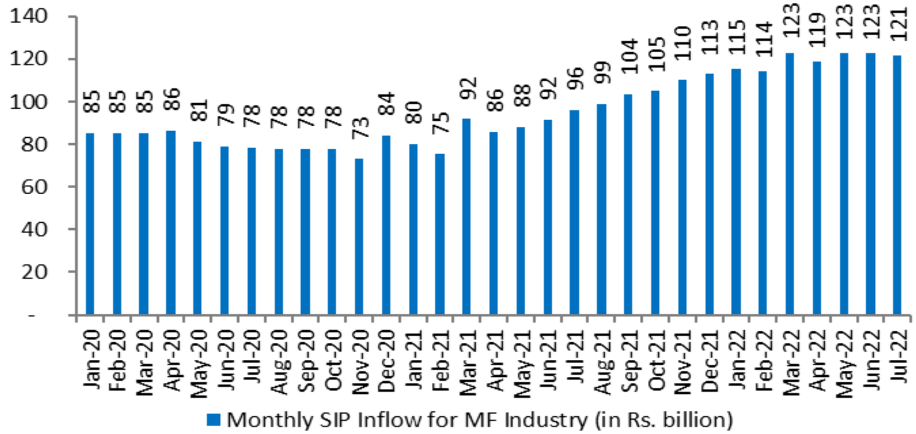
Source: Bloomberg, SBIMF Research; NB: Mutual find data available till 26th Aug'22

MF flows: Strong equity flows; marginal decrease in SIPs in Jul’22

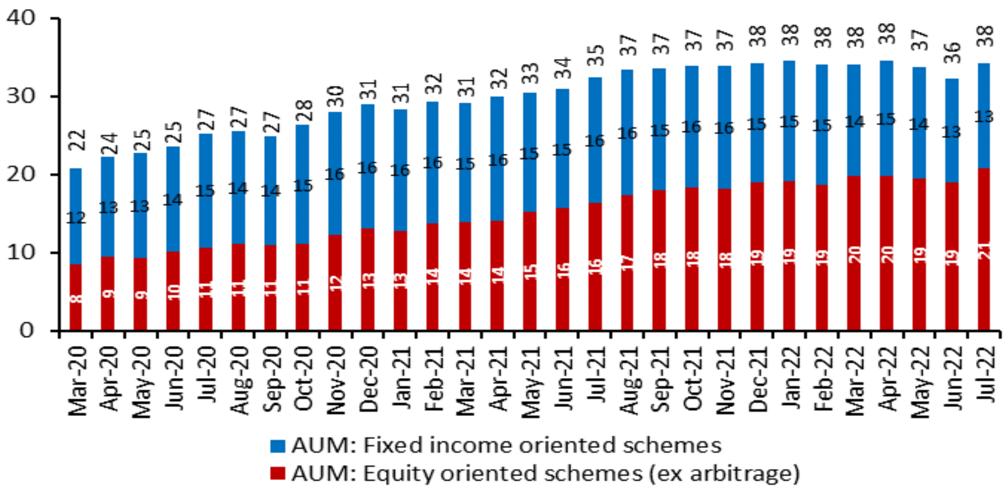
Equity MFs posted 17th straight month of inflows



SIPs lower with July levels at Rs. 121 billion vs. 123 billion in Jun’22



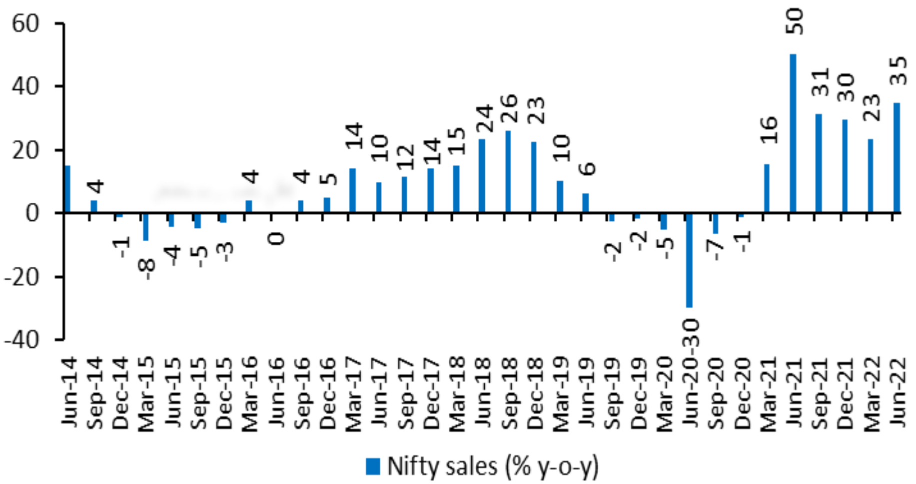
Equity AUMs and Debt AUMs in Jul’22 were slightly higher than Jun’22 values



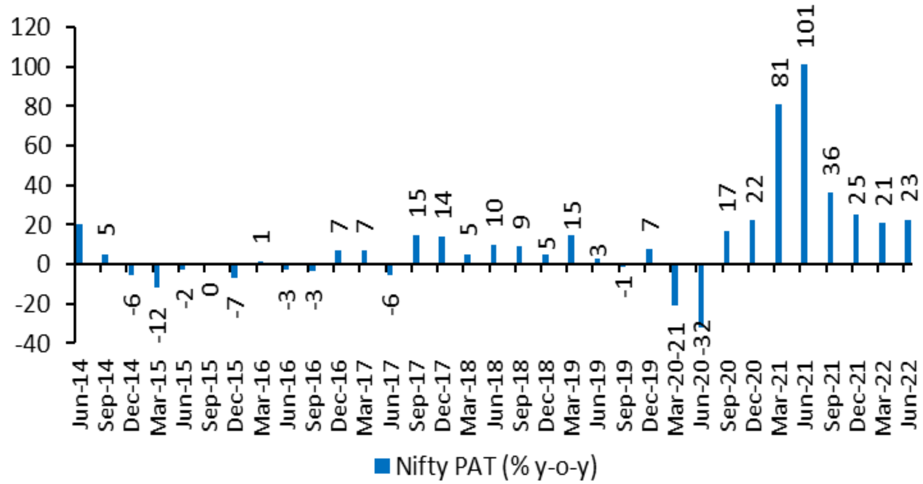
Source: CMIE Economic Outlook, Association of Mutual Funds of India(AMFI), SBIMF Research

Q1 FY23 earnings outcome: Moderation in profit growth

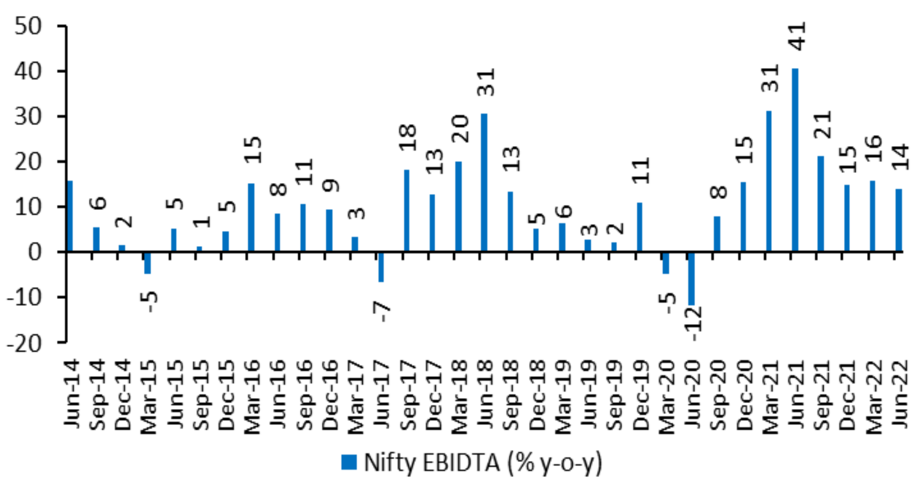
NIFTY Sales growth increased in Q1 FY23 (in line with expectations)



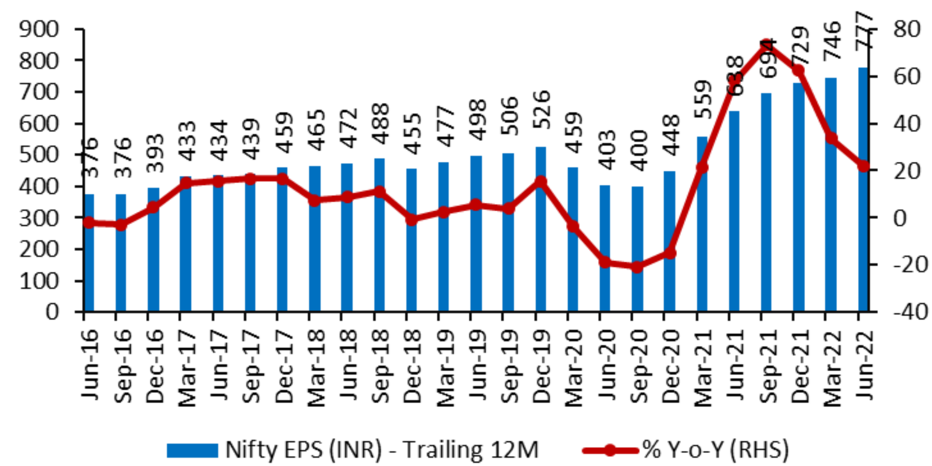
Profit growth increased in Q1 FY23 vs. Q4FY22, continues to be above the FY20 trends



EBITDA growth marginally improved as input costs remain elevated



EPS growth has been moderating



Source: MOSL, SBIMF Research; Interim earnings for 31 companies

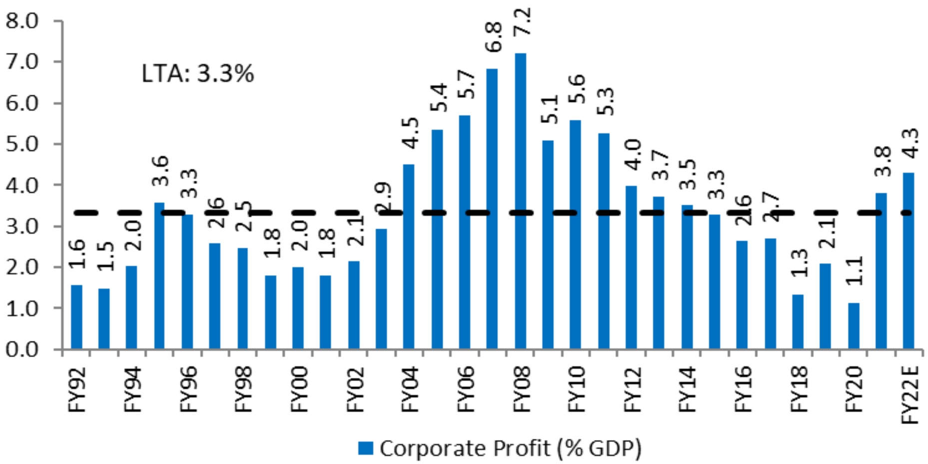
Q1 FY23 earnings' review: Snapshot

- All NIFTY(50) companies have declared the result by Aug'22 end.
- The results were broadly in line with street expectations in terms of aggregate topline sales (35%), but EBITDA (14%) and PAT growth (23%) underwhelmed market expectations.
- Broadening the horizon beyond NIFTY 50 companies indicate a healthy volume growth for retailers and leisure-oriented companies. These companies benefitted from a full normal quarter of demand without any COVID related restrictions.
- Infrastructure spend by government bodes well for materials and construction companies. Order inflows stay healthy.
- However, higher input cost including power and fuel cost, plus rise in employee cost impacts earnings.
- Financials are also exhibiting improving top-line growth (NII growth) as well as PAT growth driven by lower credit costs
- Recent cool off in commodities, if it persists could take away some of the margin pressures. That said, there could be further downgrades in near term given global headwinds, rupee depreciation and impact of inflation in demand.
- Near-term caution aside, our long-term positivity on earnings stays intact.

Source: MOSL, SBIMF Research;

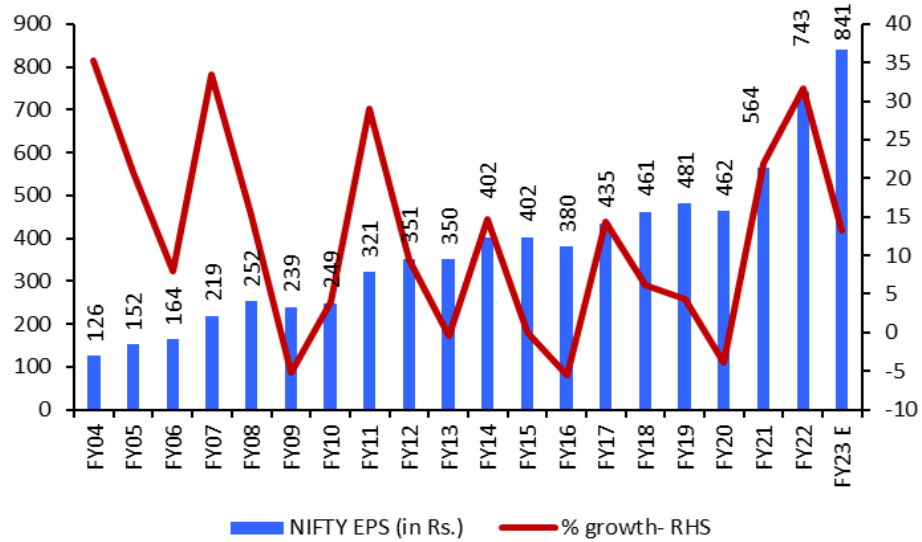
Earnings should continue to recover in FY23; albeit at a softer pace

Extremely low corporate profits to GDP makes a strong case for mean reversion



FY92-FY21 data is based on a sample of ~30,000 listed companies in CMIE (includes both financial and non financial companies)

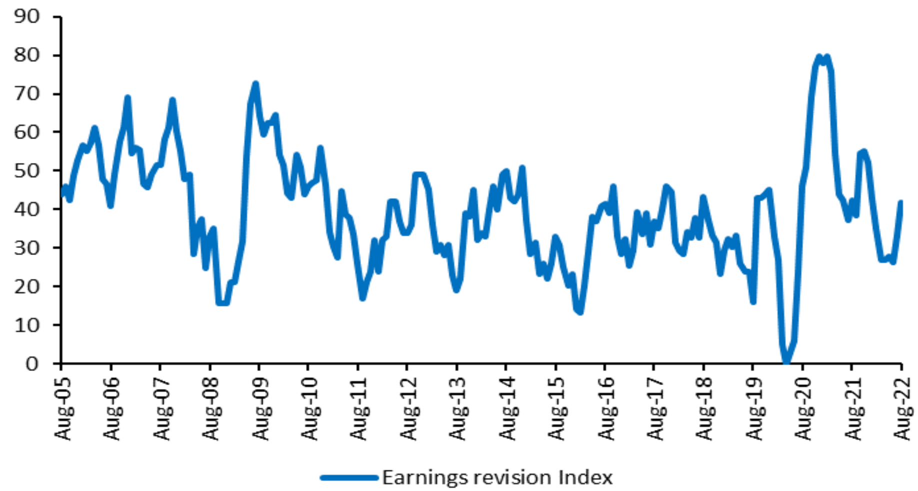
Earnings recovery likely to be healthy in FY23*



Source: CMIE Economic Outlook, Bloomberg, SBIMF Research; *FY23 earnings estimates are SBIMF

Extent of upgrades in earnings have fallen

Earnings Revision have fallen



Sectoral breakup of NIFTY earnings outlook

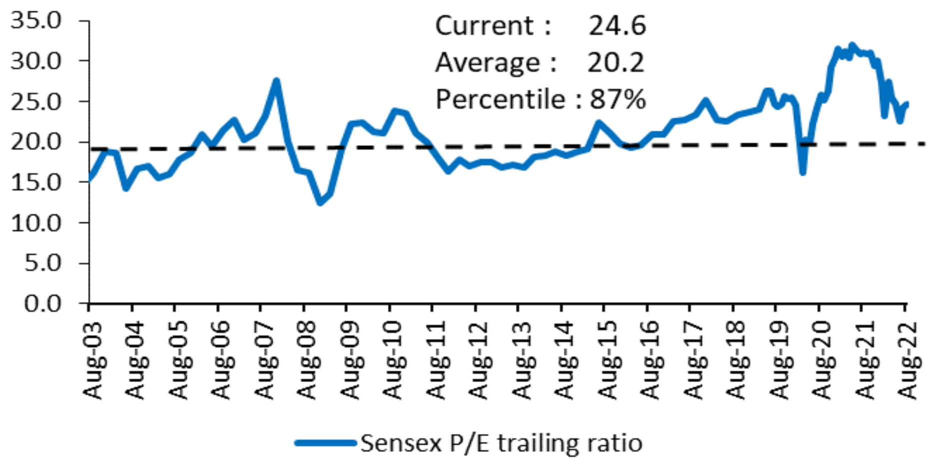
	No. of Cos.	EPS Change				
		FY20-21	FY21-22	FY22-23	FY23-24	FY21-24 (CAGR)
Nifty		20.0%	36.1%	16.0%	14.5%	21.8%
Consumer Discretionary	7	20.7%	-33.4%	180.1%	48.3%	40.4%
Materials	8	55.2%	222.9%	-30.2%	3.6%	32.7%
Health Care	5	5.9%	51.7%	15.5%	18.8%	27.7%
Financials	11	13.8%	27.3%	23.2%	18.5%	22.9%
Information Technology	5	9.6%	37.1%	6.6%	15.1%	18.9%
Energy	4	56.9%	11.4%	18.9%	7.0%	12.3%
Consumer Staples	5	-5.0%	-3.9%	12.3%	12.8%	6.8%
Industrials	2	22.9%	-30.1%	33.6%	21.1%	4.2%
Utilities	2	18.0%	-9.7%	4.4%	9.2%	1.0%
Communication Services	1	NA*				

- Earnings revisions have fallen from peak.
- Earnings upgrades only seen in Consumer discretionary and Financials.
- Materials, Energy, Healthcare and Industrials saw downgrades.
- Consensus expects 20%+ EPS growth CAGR for the Nifty over FY21-FY24.

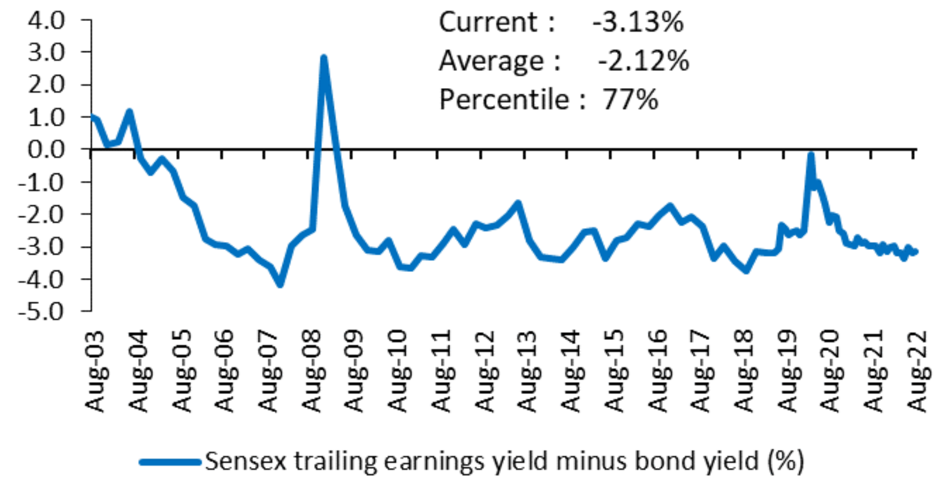
Source: Bloomberg, FactSet, SBIMF Research; NB: *data for communication services can't be calculated due to negative number in the base year, Earnings Revision Index: There has been a revision in the methodology of calculating Earnings' Revision Index. Earlier, 12 month forward estimate number of all the BSE 100 constituents as of the current month-end &3 months back were taken. Now, new version considers FY23 consensus EPS for the current date and a weighted format for history (1 month, 2 month & 3 months back with 1 month having the highest weight).

Equity valuations remain expensive

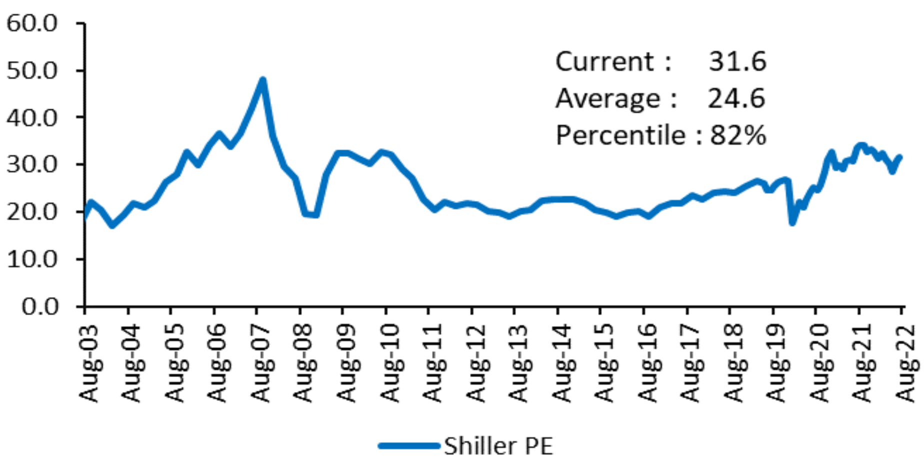
Sensex trailing PE ratio stood at 24.6 in Aug’22 vs. 24.2 in Jul’22



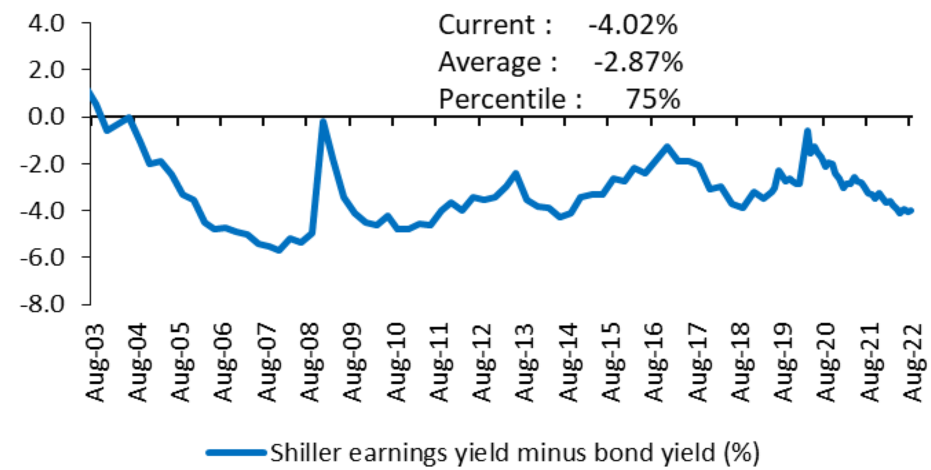
Earnings yield to bond yield spread expensive



Shiller PE ratio stood at 31.6 in Aug’22 vs. 30.8 in Jul’22



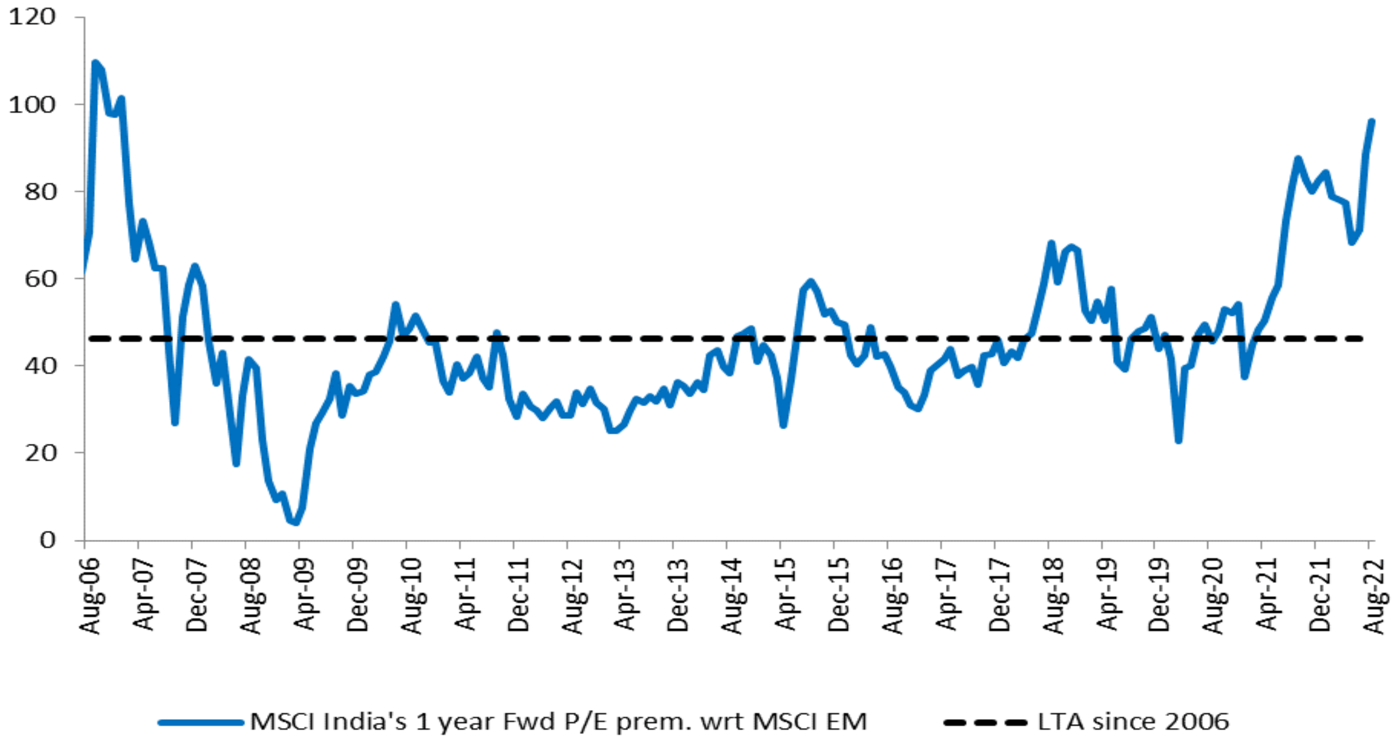
Shiller earnings yield to bond yield spread moderately expensive



Source: Bloomberg, SBIMF Research

MSCI India's valuation at a significant premium relative to MSCI EM

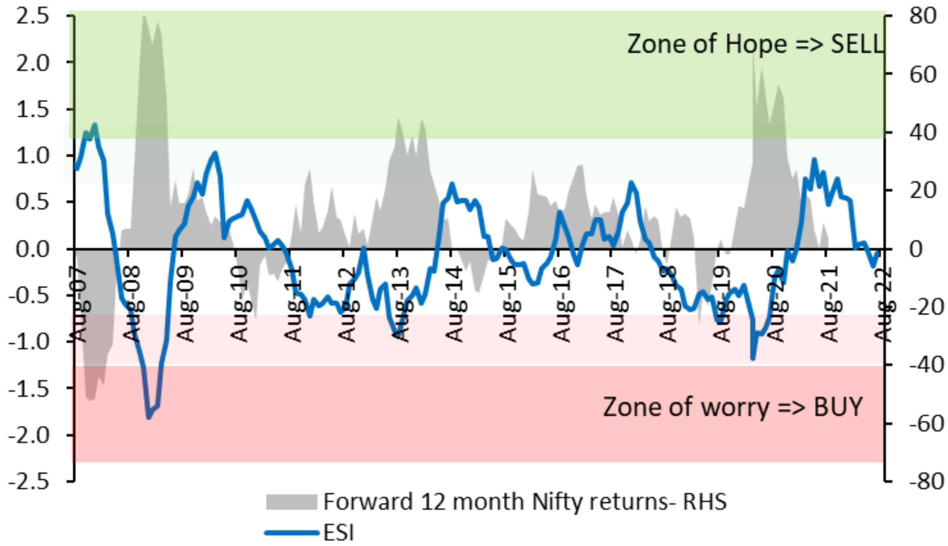
MSCI India's 1 year Fwd P/E premium with respect to MSCI EM at 96 in Aug'22 vs. 88 in Jul'22 (faring much higher than LTA of 46)

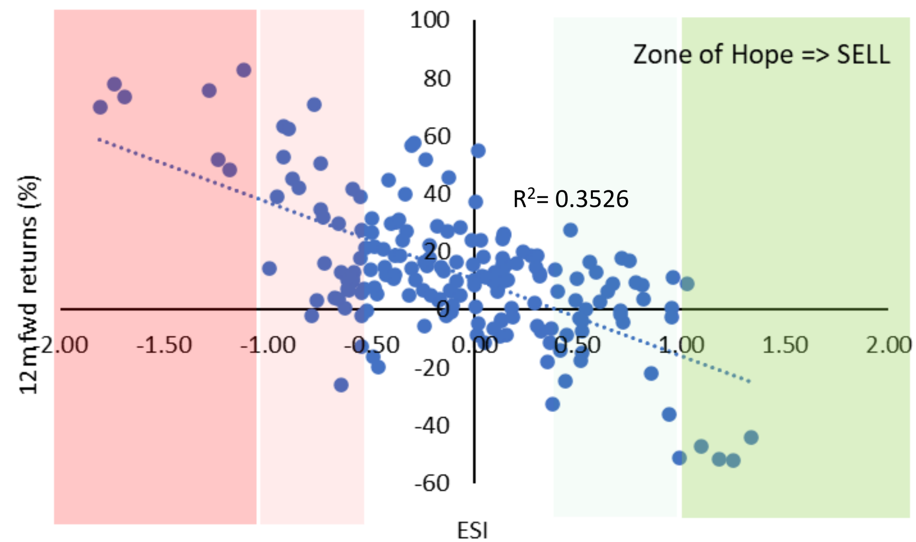


Source: Bloomberg, SBIMF Research

Equity market sentiment at neutral level

Earnings sentiment index has turned neutral (vs. heightened optimism until a few months ago)





- The sentiment measure works as a contrarian indicator. The action in the past few months has helped to take away the froth and brought the indicator back to neutral levels

Source: Bloomberg, FactSet, SBIMF Research; ESI = Earnings sentiment Index

Equity Outlook: Near-term cautiousness

- Indian equity markets delivered positive returns in Aug'22. Nifty-50 and Sensex improved in Aug'22 by 3.5% (vs 8.7% in Jul'22) and 3.4% (vs 8.6% in July).
- Performance down the capitalization curve was a tad better (Small cap:5.9% and mid cap:5.6%). Among sectors indices, all sectors delivered positive returns on m-o-m basis except IT.
- FIIs turned net buyers of Indian equities in August (USD$6.26bn, following $0.8bn in July). DIIs turned net sellers after recording 17 consecutive months of positive inflows (-$0.9bn, following +$1.3bn seen in July).
- Geopolitical stalemate, possibility of an energy crisis in Europe, and Fed monetary tightening create a volatile environment for investors. Three big global economic block is either struggling with growth (China) or face the prospects of material slowdown (Eurozone and the US).
- Global sluggishness is likely to have a rub-off on Indian growth as well. US yield curve is now decisively inverted and historically this has been a harbinger of recession. And the fact that the US Fed is still tightening (and shrinking the size of its balance sheet) in the wake of already low money supply growth only adds to slowdown risks.
- Growth projections for FY23 lowered in India to 7% mainly on account of slower global growth and inflationary pressures resulting in weak domestic demand.
- In this context, we believe it may be premature to declare an end to the current volatility. Investors should stay patient and stick to their long-term asset allocation; investors would do well to not get carried away after the recent sharp rally given the global growth risks.
- It is patience through the turbulence that is likely to be rewarded on the other side given that corporate earnings have likely turned the corner and are likely to trend higher over the next few years. .

Source: Bloomberg, SBIMF Research

FIXED INCOME MARKET

Global yields rise after hawkish commentary at Jackson Hole

Developed market bond yields increased in August compared to a month ago; YTD, bond yields have seen a significant rise

10 Year Gsec Yield (% mth end)	2020 end	2021 end	May-22	Jun-22	Jul-22	Aug-22	m-o-m change (in bps)	YTD change (in bps)
Developed market								
US	0.91	1.51	2.84	3.01	2.65	3.10	45	159
Germany	-0.57	-0.18	1.12	1.34	0.82	1.53	71	171
Italy	0.54	1.17	3.12	3.26	3.02	3.86	83	268
Japan	0.02	0.07	0.24	0.23	0.19	0.23	4	16
Spain	0.05	0.57	2.23	2.42	1.92	2.72	80	215
Switzerland	-0.55	-0.14	0.89	1.07	0.44	0.81	37	94
UK	0.20	0.97	2.10	2.23	1.86	2.79	92	182
Emerging Market								
Brazil	6.91	10.84	12.56	13.07	12.99	12.29	-69	146
China	3.15	2.78	2.80	2.82	2.77	2.64	-12	-14
India	5.87	6.45	7.42	7.45	7.32	7.19	-13	74
Indonesia	5.86	6.36	7.03	7.20	7.11	7.11	1	75
South Korea	1.72	2.26	3.33	3.62	3.13	3.71	59	146
Malaysia	2.65	3.58	4.19	4.24	3.90	3.99	9	41
Russia	5.92	8.45	15.99	15.99	15.99	15.99	0	754
Taiwan	0.49	0.49	0.49	0.49	0.49	0.49	0	0
Thailand	1.32	1.89	2.85	2.82	2.50	2.43	-7	53
Mexico	5.55	7.57	8.65	9.05	8.58	9.09	51	152
Poland	1.24	3.67	6.62	6.93	5.54	6.18	64	251
South Africa	8.75	9.81	10.27	11.00	10.79	10.90	11	108
Colombia	5.39	8.19	11.08	11.55	12.23	12.07	-16	388
Hungary	2.08	4.51	7.16	8.01	8.17	8.83	66	432

Source: Bloomberg, SBIMF Research

India Rates Snapshot: August 2022

Marginal fall in long-end yield ; Short-end continues to rise

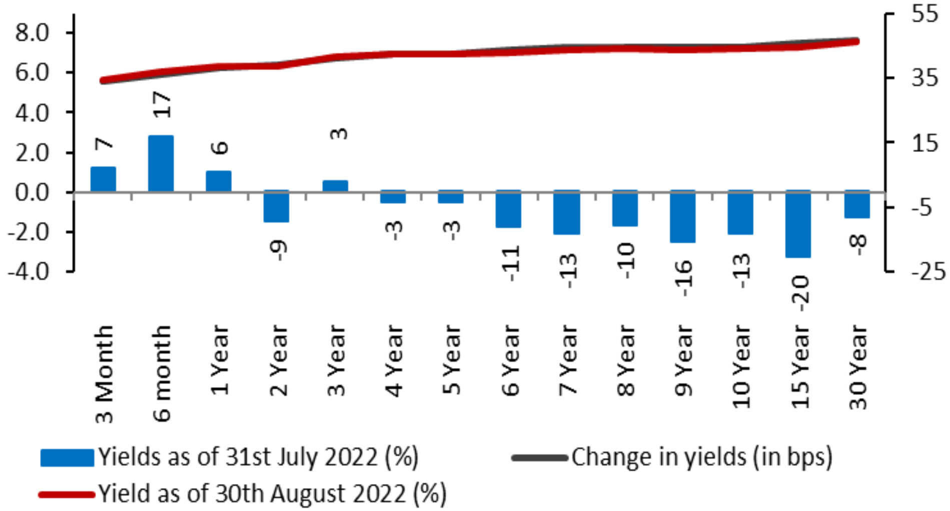
	2020 end	2021 end	Jun-22	Jul-22	Aug-22	m-o-m (in bps)	YTD change (in bps)
Repo rate	4.00	4.00	4.90	4.90	5.40	50	140
Reverse repo rate	3.35	3.35	3.35	3.35	3.35	0	0
SDF			4.65	4.65	5.15	50	515
1 Yr T-Bill	3.46	4.27	6.29	6.33	7.21	88	295
3M T-Bill	3.08	3.66	5.16	5.62	5.62	0	197
3 year GSec	4.46	5.30	6.96	6.76	6.78	2	148
5 year GSec	5.04	5.79	7.18	6.95	6.92	-3	113
10 year GSec	5.87	6.45	7.45	7.32	7.19	-13	74
3 Yr Corp Bond*	4.69	5.76	7.44	7.18	7.21	3	145
5 Yr Corp Bond*	5.51	6.22	7.54	7.39	7.44	5	122
10 Yr Corp Bond*	6.59	7.00	7.78	7.68	7.55	-13	54
1 Yr IRS	3.69	4.34	6.34	6.18	6.32	14	198
5 Yr IRS	4.61	5.37	6.88	6.34	6.44	10	107
Overnight MIBOR Rate	3.51	3.60	4.95	5.25	5.34	9	174
10 year SDL	6.58	7.01	7.83	7.80	7.65	-15	64
INR/USD	73.07	74.3	79.0	79.3	79.5	0.2^	7^
Crude oil Indian Basket**	49.90	73.3	116.1	105.5	97.4	-8^	33^

- 3year G-sec yields increased by 2 bps whereas 5 and 10year G-sec yields decreased by 3 bps and 13 bps respectively in Aug'22 vs. Jul'22.
- Rupee depreciated by ~0.2% to INR 79.5/$ in Aug'22.
- Oil prices decreased ~8% in Aug'22 vs. Jul'22 to US$ 97/bbl level.

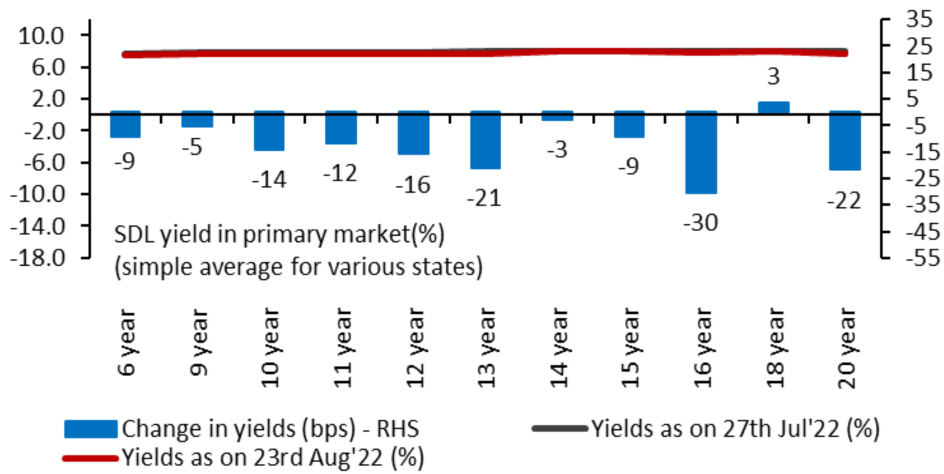
Source: Bloomberg, PPAC, RBI, CEIC, SBIMF Research; NB: *Corporate bond rate is for AAA rated bonds, **Crude oil price is average $/barrel for the month and INR, remaining data are % month end, ^INR and Oil price changes are % change, + denotes appreciation in rupee, -ve denotes depreciation

Fall in Indian G-sec and SDL yields in August'2022

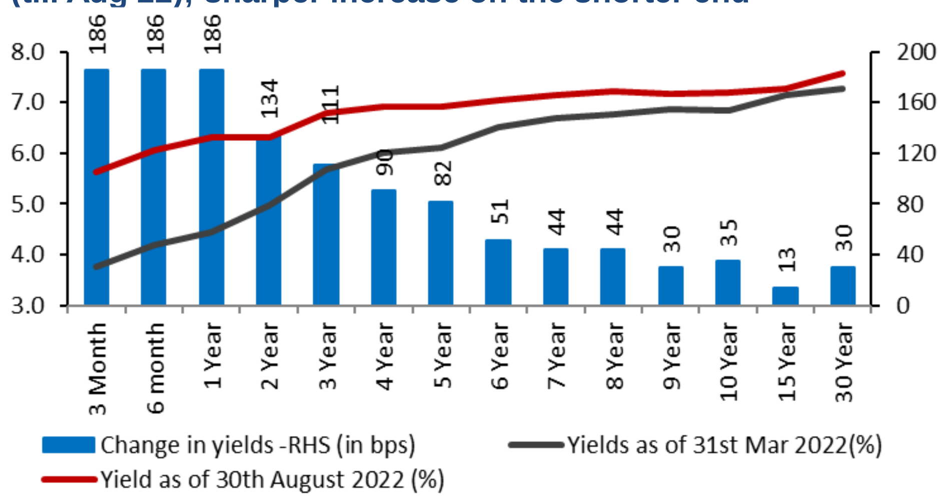
G-sec yields sees a small rally in 3 year and below



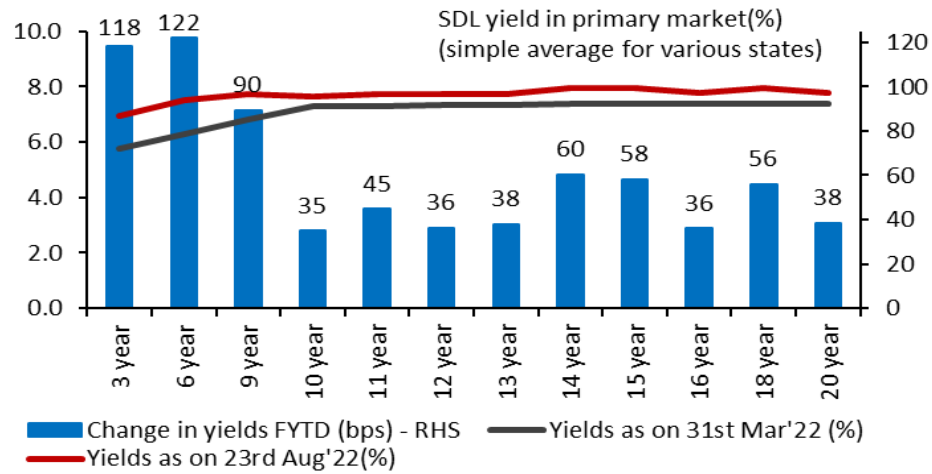
SDL yields decrease across almost all tenures m-o-m



G-sec yields increased materially across all tenures FYTD (till Aug'22); sharper increase on the shorter end



SDL yields increased materially across all tenures FYTD



Source: Bloomberg, RBI, SBIMF Research

RBI hikes Repo Rate by 50bps in Aug’22 policy

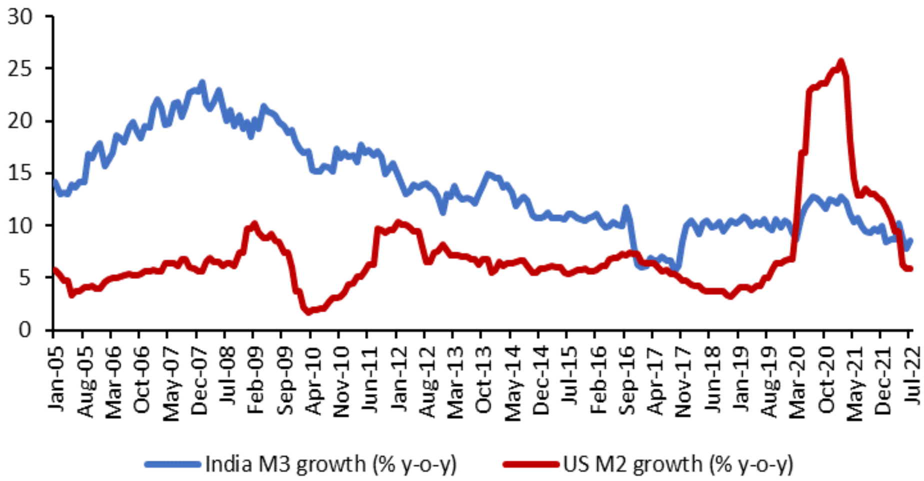
- Repo rate hike by 50bps in August review (to 5.40% in line with expectation)
- Stance continued to guide for withdrawal of accommodation
- Inflation projections were revised up for Q3 from 6.2% in Jun’22 to 6.4% in latest policy (unchanged at 6.7% for FY23).
- Quarterly projections of inflations recognizes the possibility of breach in 6% upper target beyond three quarters.
- Inflation control has been rightly emphasized as the primary policy objective of August monetary policy.
- Quicker policy rate adjustment seems more likely rather than a long-drawn-out rate adjustment process considering the domestic and external backdrop.
- Expect the policy rate adjustment process to be completed over the fiscal year and Repo rate to go to ~6% in current hiking cycle.

Policy date	8th Jun'22	5th Aug'22	Change
Repo	4.90%	5.40%	+ 50bps
Reverse repo	3.35%	3.35%	No change
MSF	5.15%	5.65%	+ 50bps
CRR	4.50% of NDTL	4.50% of NDTL	No change
SDF	4.65%	5.15%	+ 50bps
Guidance	Withdrawal of accommodation	Withdrawal of accommodation	No change
Our subjective assessment of policy stance	Hawkish	Hawkish	

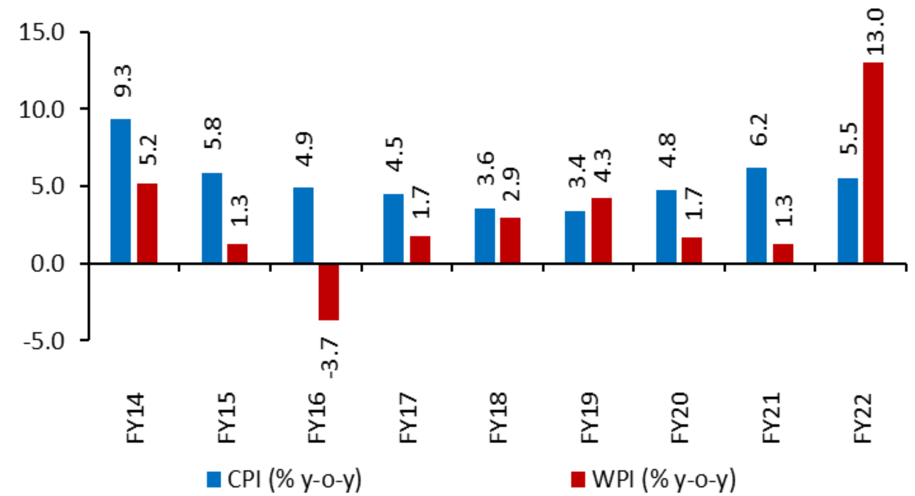
Source : RBI, SBIMF Research

CPI and WPI has stayed elevated in 1H 2022

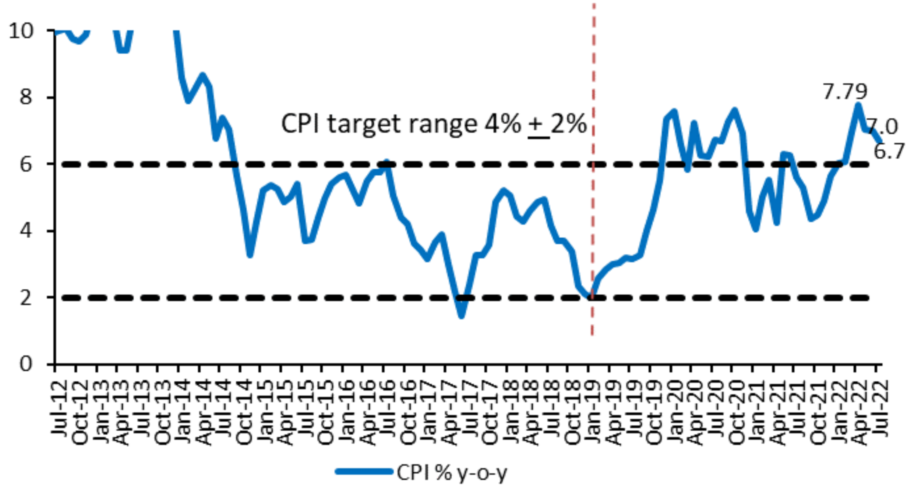
India did not have run away money supply growth unlike the US economy



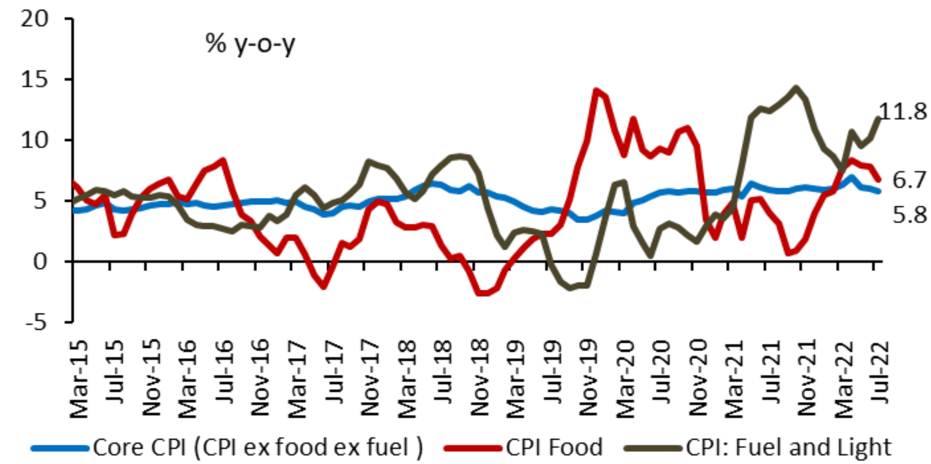
Commodity rise and consequent cost push pressure kept inflation elevated post COVID



CPI breached RBI's upper target for seven consecutive months



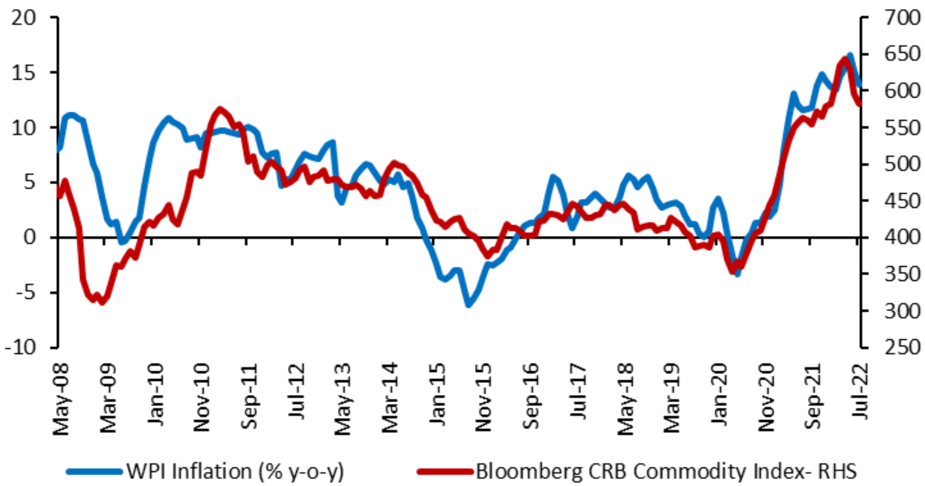
Broad based rise in inflation



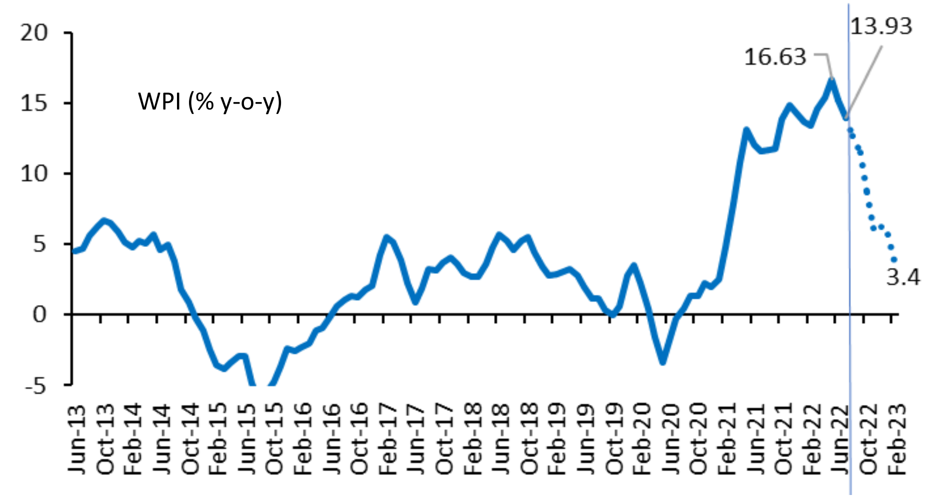
Source: CMIE Economic Outlook, Bloomberg, SBIMF Research

CPI moderation may be more gradual than WPI

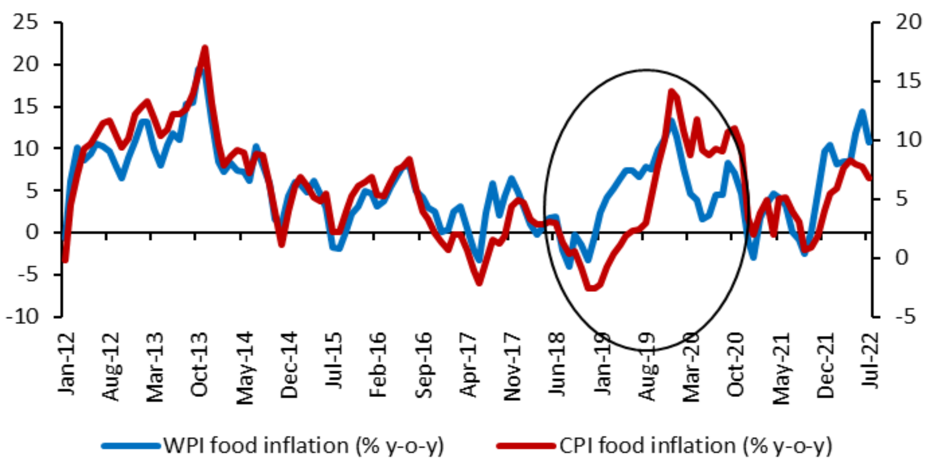
WPI Inflation is strongly linked to commodity prices



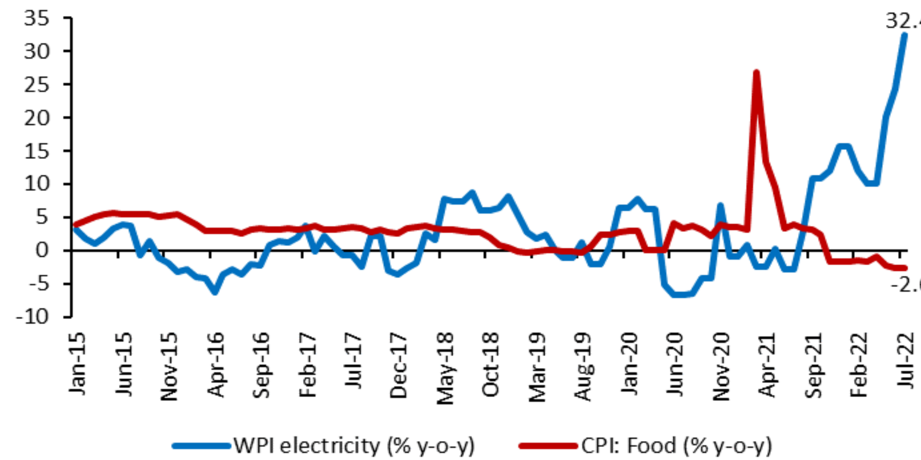
Peaking of global commodities could help contain WPI inflation



Some risks emanate from retail food inflation lagging wholesale food price pressures



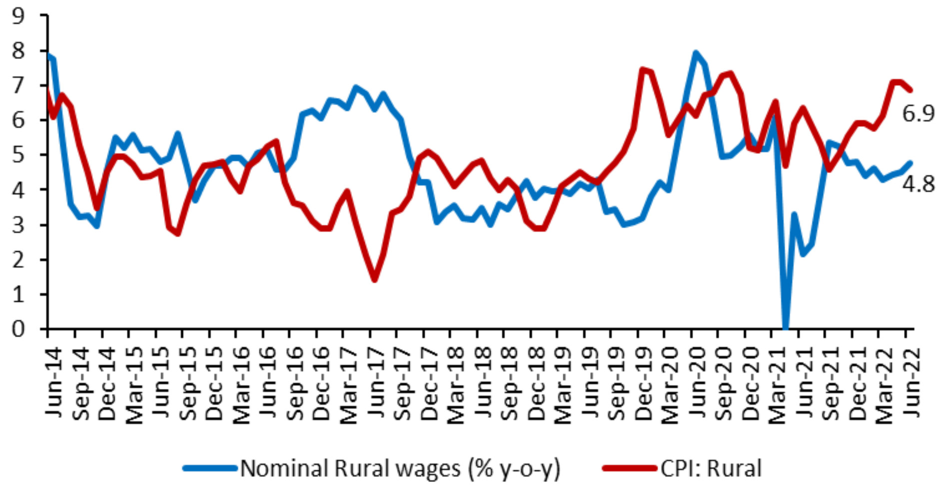
Wide disparity between retail and wholesale electricity prices



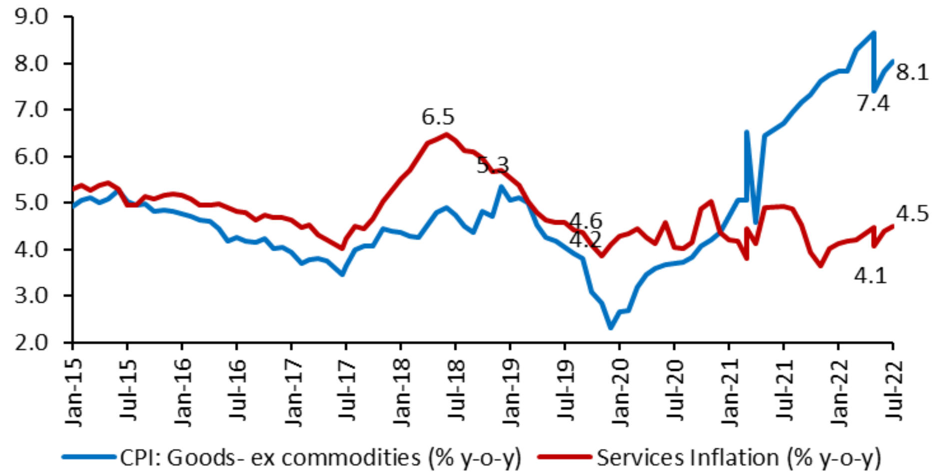
Source: CMIE Economic Outlook, Bloomberg, SBIMF Research

Food and wage pressure may keep CPI above the target band

Rise in rural wages, particularly in low skilled jobs is expected to push inflation higher



Services inflation has started to catch up while goods inflation continues to rise

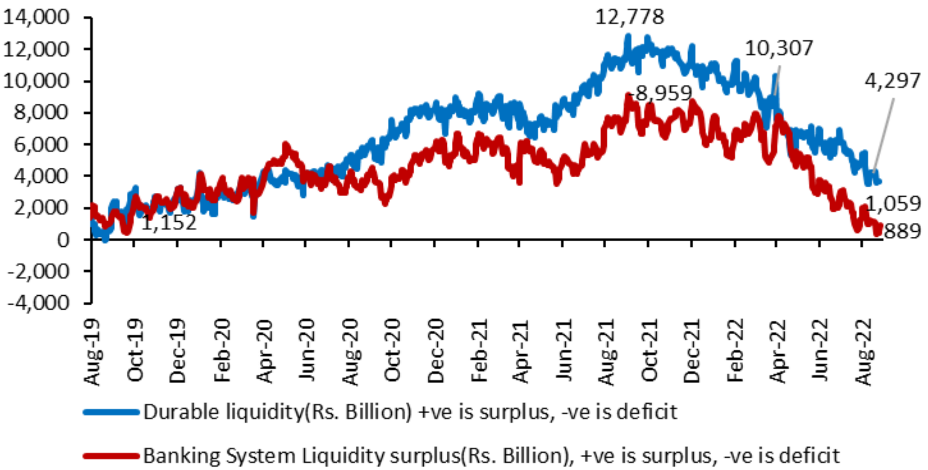


- We expect India's CPI inflation to stay above RBI's target band throughout 2022 and moderate in 2023, helped partly by favourable base and waning momentum in commodity linked segment.
- FY23 inflation expectation at 6.7% y-o-y.

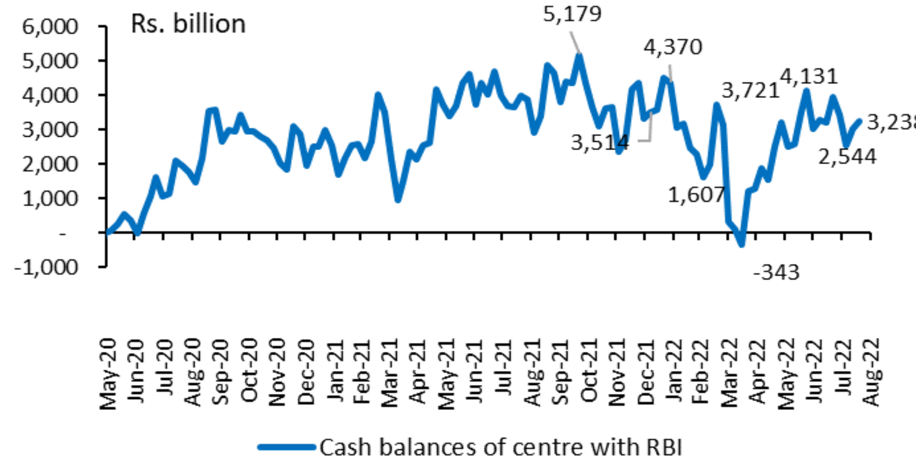
Source: CMIE Economic Outlook, Bloomberg, SBIMF Research

Sharp moderation in banking system liquidity FYTD

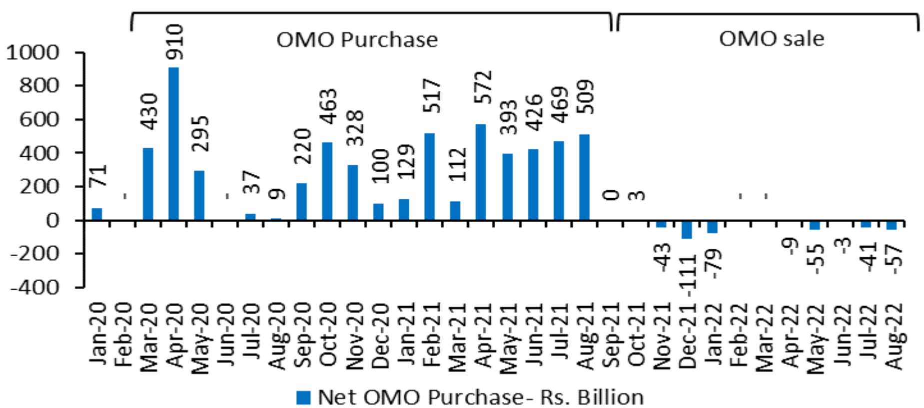
Moderation in Net LAF and durable liquidity



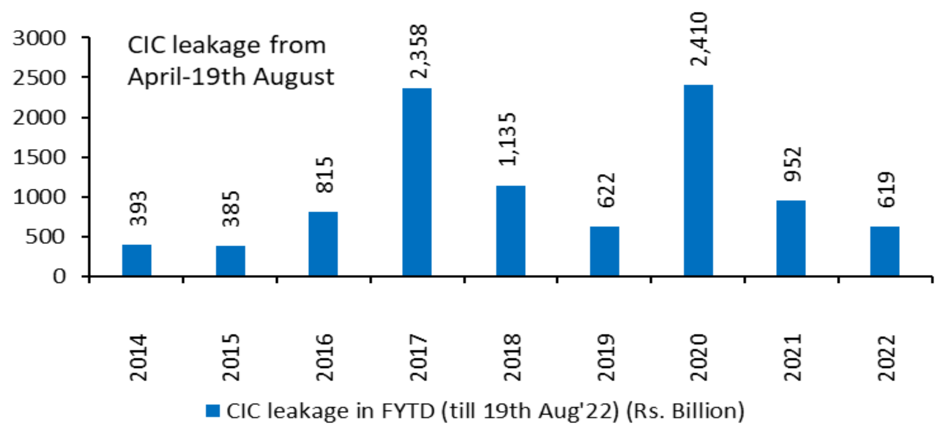
Govt cash balances high due to seasonally lean govt spend and healthy tax collection



OMO purchase discontinued since Sep'21; replaced by marginal sell



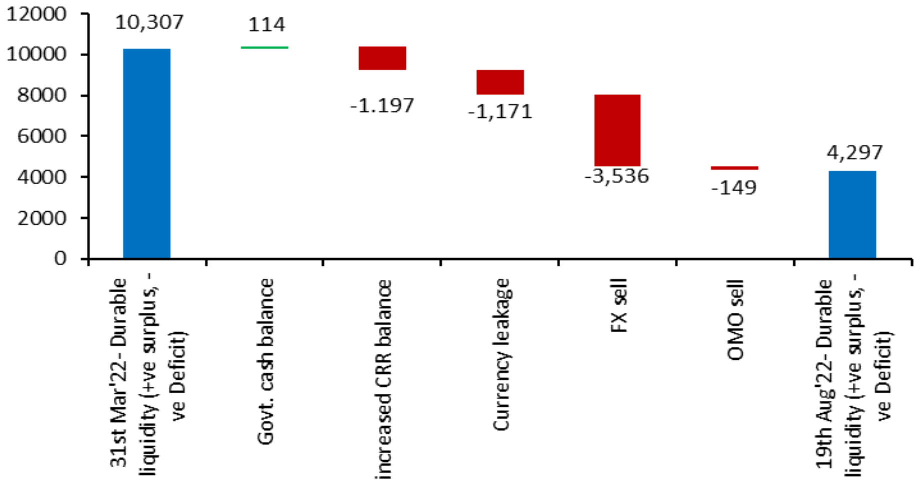
Currency leakage is lower than past trends; could be mean reverting post COVID



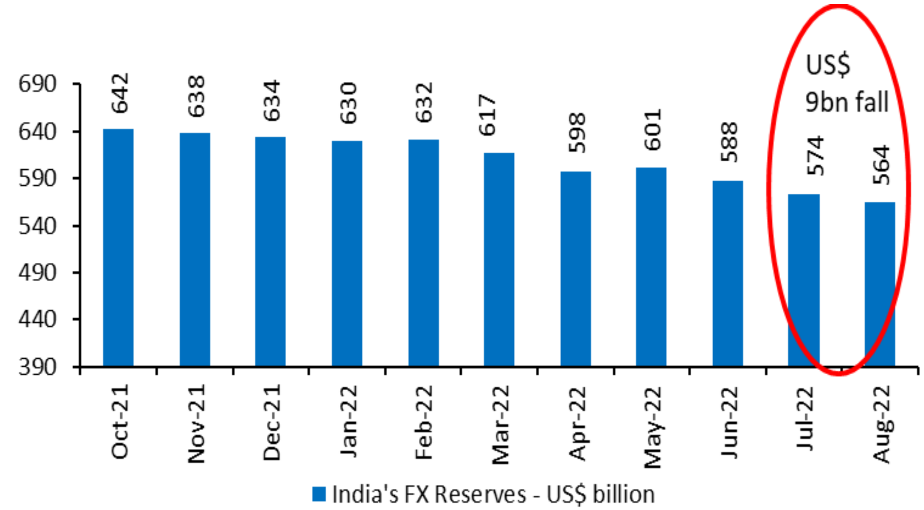
Source: RBI, SBIMF Research; NB: Durable Banking system liquidity is LAF adjusted for excess CRR reserve and Govt. cash balance and is uptil 19th Aug'22, OMO/GSAPs, CIC leakage, and Govt. cash balance data uptil 19th Aug'22, Banking system liquidity uptil 26th Aug'22

FX sell and CRR hike drives fall in liquidity

Sharp FX sell, CRR hike and discontinuation of OMO purchase explains fall in liquidity



US$ 9bn drop in FX reserves m-o-m (54bn $ drop FYTD)



- LAF (as % of NDTL) fell to 0.4% (Durable liquidity at 2.36% of NDTL). and may hover around similar range throughout FY23.
- 2H of FY23 may see drawdown in govt. cash balance in line with historical spending patterns- thereby adding to Net LAF liquidity
- However, currency leakage also tends to seasonally increase in 2H, and may provide an offsetting impact.
- We expect a BoP deficit of US$ 50-60 bn in FY23, however majority of it is likely to be skewed in 1H FY23.
- Commodity prices may likely soften in coming months and capital outflow could peter out (if not reverse) thereby reducing the monthly external account deficit.

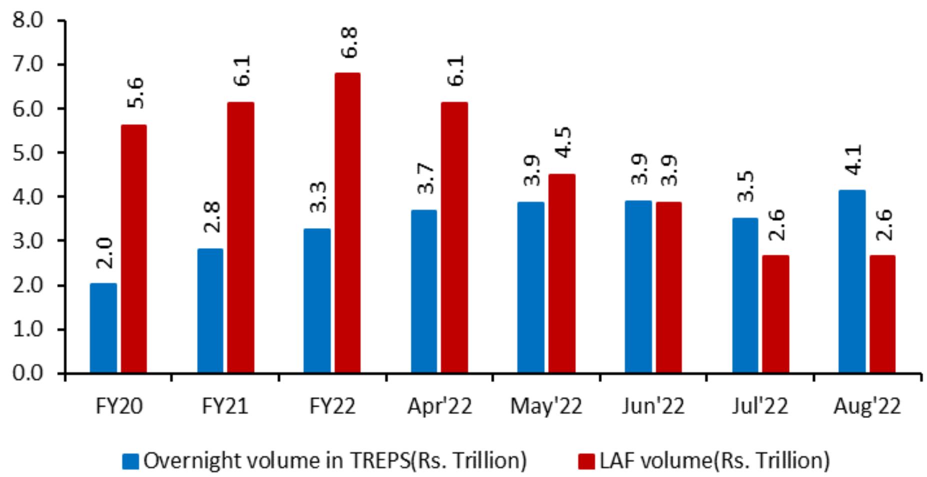
Source: RBI, SBIMF Research; NB: Durable Banking system liquidity is LAF adjusted for excess CRR reserve and Govt. cash balance and is uptil 19th Aug'22, FX intervention data available uptil June end, OMO/GSAPs, CIC leakage, CRR balance and Govt. cash balance data uptil 19th Aug'22, Banking system liquidity uptil 26th Aug'22, assume Rs. 2 tn FX sell in July and Aug

Moderation in surplus liquidity drives short term rates upwards in Aug'22

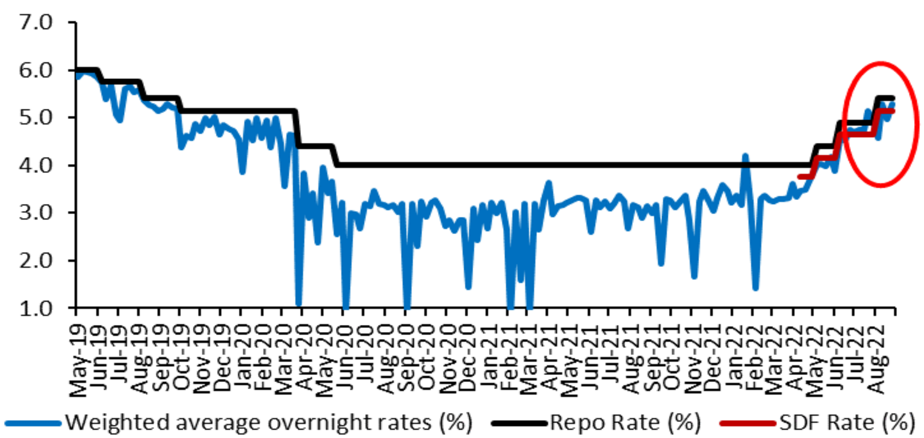
Short term rates move upwards

Rates (%)	Latest (31st Aug'22)	3 months ago	6 months ago	12 months ago
Overnight segment				
Triparty repo	5.28	4.15	3.23	3.10
WACR	5.15	4.09	3.29	3.18
T-bill				
91 day	5.63	4.89	3.70	3.30
182 day	6.09	5.43	4.19	3.45
364 day	6.32	5.91	4.52	3.65
Others				
CD (3m)	5.93	4.15	4.00	4.37

Volume in overnight segment (TREPS) higher than LAF volumes



Weighted average overnight rate trades 10-15bps below repo rate (higher than SDF rate by 13bps)



- Moderation in banking system liquidity continues to increase overnight rates.
- Weighted average overnight rates have increased by ~33bps in August compared to a month ago.
- Overnight rates are 12bps below Repo as of August vs. 4bps above repo in end July 2022.

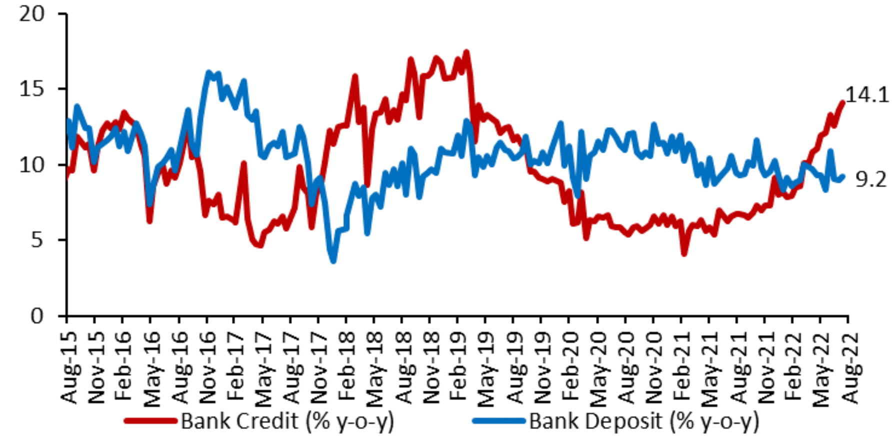
Source: : RBI, CEIC,RBI, SBIMF Research; NB: TREPS and LAF volumes uptil 26th Aug, weighted avg overnight rates data uptil 26th Aug'22

RBI’s balance sheet contracts; Incremental credit deposit ratio is high

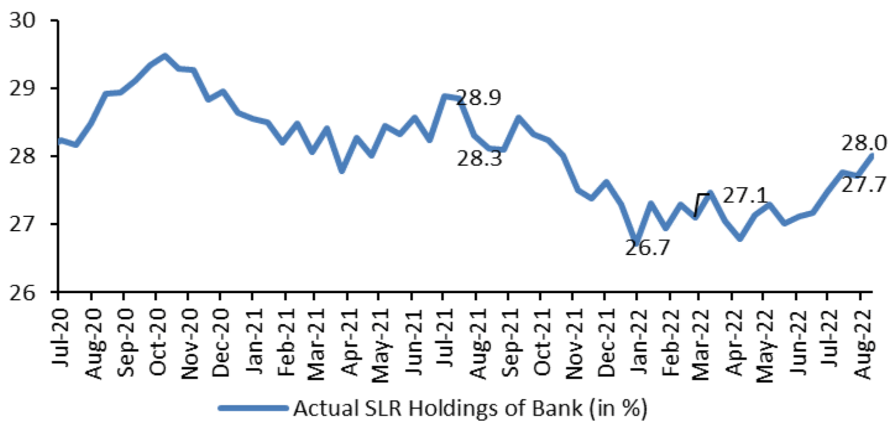
RBI balance sheet contracted by 4.6% y-o-y; money supply and reserve money growth also moderate

% growth	FY21	FY22	Apr'22	May'22	Jun'22	Jul'22	Aug'22
RBI's balance sheet	14.7	10.2	3.8	5.1	0.4	-3.6	-4.6
Reserve money	15.2	12.3	13.2	10.4	10.9	11.2	10.7
Money supply (M3)	11.7	9.1	10.7	8.8	8.6	7.9	8.4
Bank credit	5.6	8.6	10.1	11.0	12.1	12.6	14.1
Bank Deposit	11.4	8.9	9.8	9.3	8.3	9.1	9.2

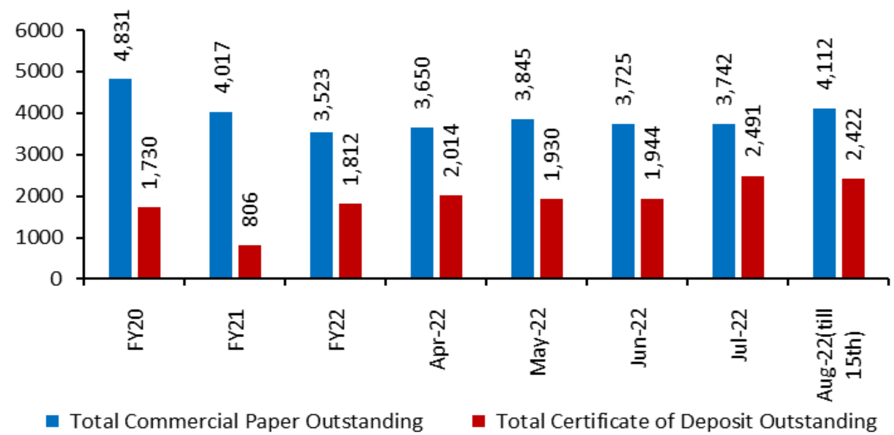
Bank credit growth is at 14.1% y-o-y; incremental credit deposit ratio at 111% FYTD



SLR holding ratio stands at 28% as of 12th Aug’22



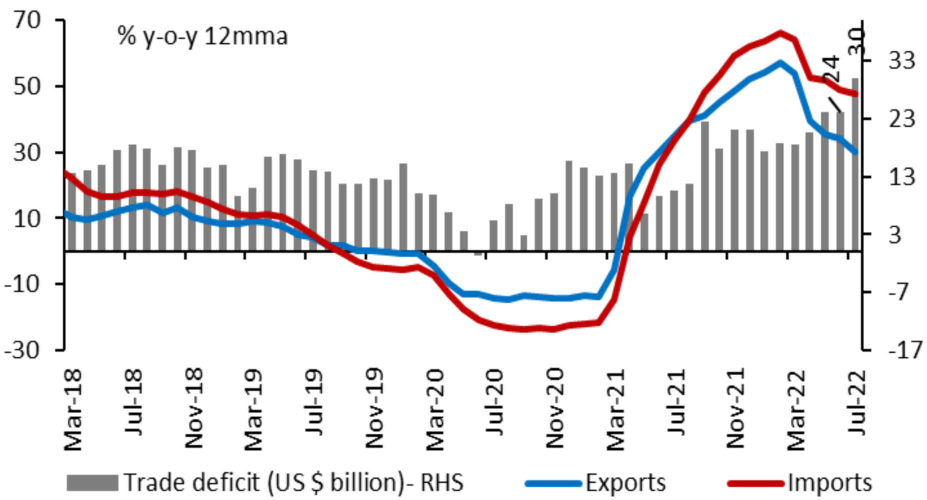
Outstanding CP issuances increased by Rs. 297bn in last one month; CD issuances near FY19 outstanding levels



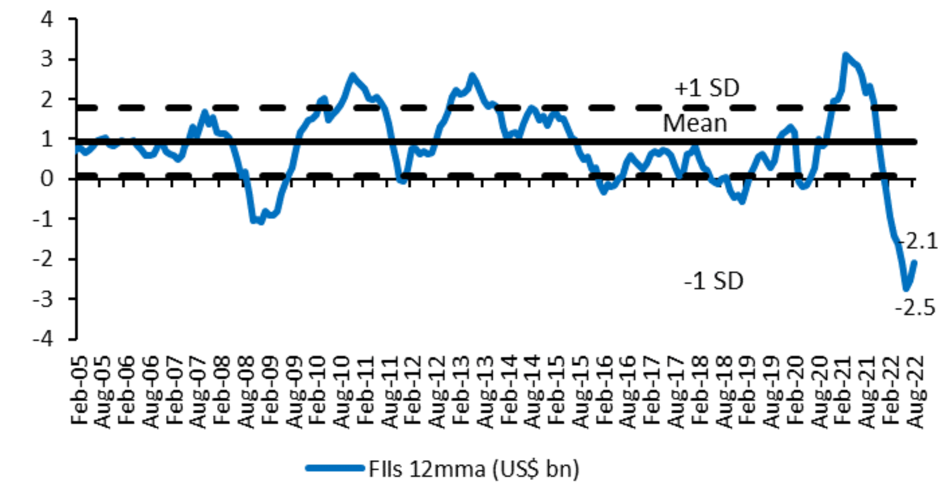
Source: : RBI,CMIE Economic Outlook, SBIMF Research; NB: Overall bank credit data, bank deposit data, M3 and SLR ratio as of 12th Aug’22, CP and CD issuances till 15th Aug’22, reserve money, RBI balance sheet till 19th Aug’22

High commodity prices and capital outflows leads to fall in forex reserve

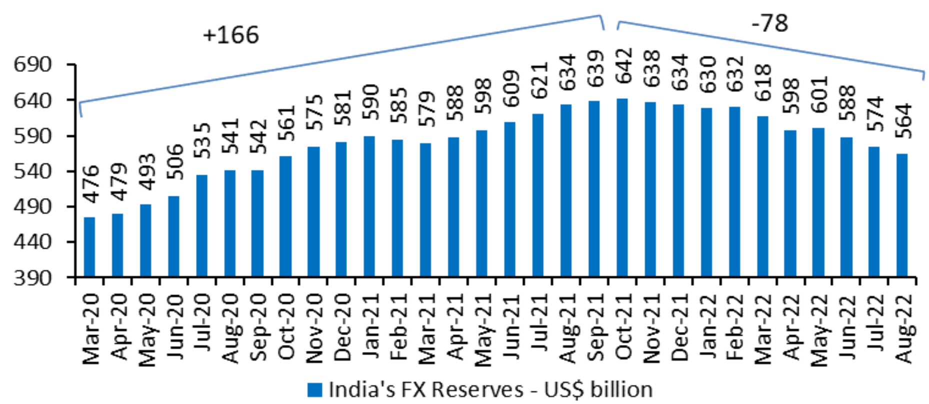
Trade deficit surges due to high commodity prices



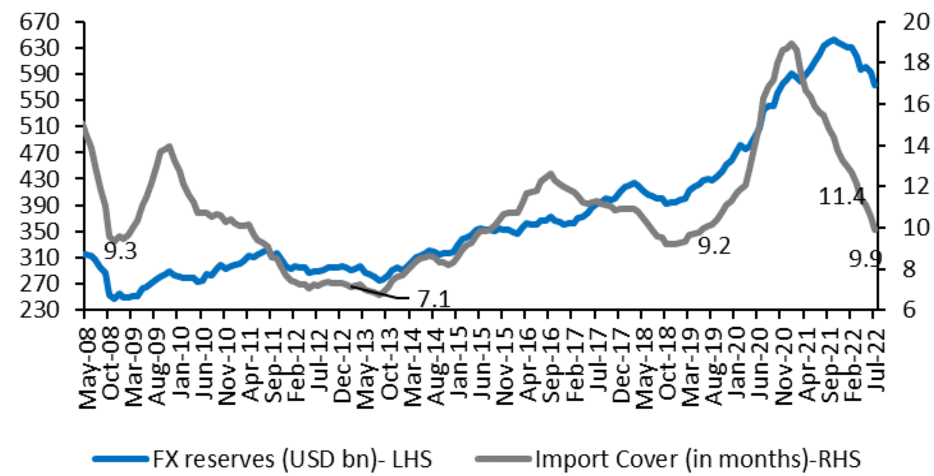
India sees FII outflows of US$24 bn since Oct'21



FX reserves fell US$ 78bn since Oct'21 peak



Import cover moderates to 9.9 months



Source: CMIE Economic Outlook, Bloomberg, SBIMF Research

CAD likely to widen to ~3% of GDP in FY23; expect BoP deficit ~US$ 50b

Widening trade deficit will add to BoP deficit in FY23; INR to come under further pressure

Balance of Payment (US$ bn)	FY20	FY21	FY22	FY23E
CURRENT ACCOUNT				
Exports (RBI)	320	296	429	453
% y-o-y	-5.0	-7.5	44.8	5.6
Imports (RBI)	478	398	619	731
% y-o-y	-7.6	-16.6	55.3	18.2
Oil (Customs)	131	83	162	209
Gold (Customs)	28	35	46	65
Non-Oil Non-Gold (Customs)	313	276	401	452
1. Trade Balance (RBI)	-158	-102	-189	-278
% GDP	-5.6	-3.8	-6.0	-8.0
2. Services Balance	85	89	108	132
% GDP	3.0	3.3	3.4	3.8
3. Primary Income	-27	-36	-37	-45
4. Secondary Income (Transfers)	75	74	81	85
A. Current A/c Balance (1+2+3+4)	**-25**	**24**	**-39**	**-106**
% GDP	-0.9	0.9	-1.2	-3.1
CAPITAL ACCOUNT				
5. FDI (Net)	43.0	43.8	38.9	35.0
% GDP	1.5	1.6	1.2	1.0
6. FPI (Net)	1.4	36.1	-16.8	-20.0
% GDP	0.0	1.4	-0.5	0.0
7. Loans	25.7	6.8	33.8	30.0
8. Banking Capital	-5.3	-21.1	6.7	10.0
B. Capital Account Balance (5+6+7+8+9+10)	**83**	**63**	**88**	**55**
% GDP	2.9	2.4	2.8	0.0
C. Error and Omissions	1.0	-0.2	-0.1	0.0
D. Overall Balance (A+B+C)	**59**	**87**	**48**	**-51**
% GDP	2.1	3.3	1.5	-1.5
Increase in Reserves due to BoP	**59**	**87**	**48**	**-51**
Rupee vs. US$ (average)	**71**	**74**	**75**	**78**

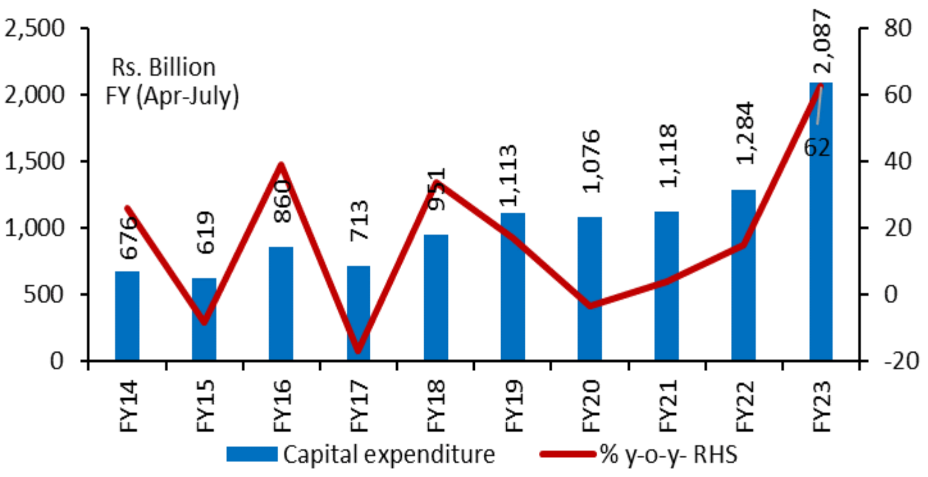
Source: CMIE Economic Outlook, RBI, SBIMF Research

Strong government receipts keeps Centre's fiscal position on track

Gross tax revenue grew at 25% y-o-y (Apr-Jul'22)

Apr-July 2022	% y-o-y	Required growth (FY23 BE vs. FY22 Actual)
Net Tax Revenue	25.9	6.3
Gross Tax Revenue	24.9	1.8
Income Tax	50	3.9
Corporate Tax	35	1.1
Custom	-12	7.0
Excise duties	-15	-14.3
GST	29	11.2
Total Direct Tax	43	2.5
Total Indirect Tax	11	2.8

Capex growth is 62% y-o-y (Apr-Jul'22)

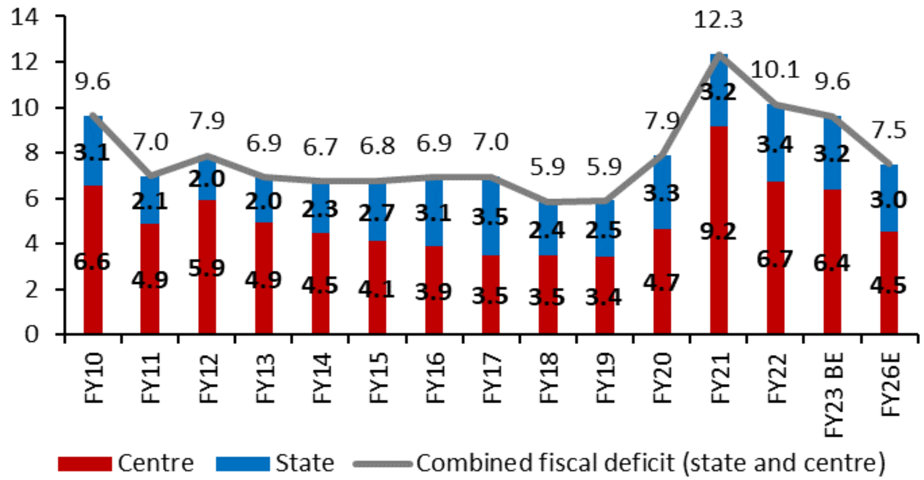


- Fiscal deficit during Apr-Jul'22 is 20.5% of BE, significantly better than pre-COVID trend of ~78%.
- Owing to extremely conservative tax assumptions, net tax collections are tracking 34% of BE (vs. ~30% in pre-COVID times). Customs and excise duty collections have declined y-o-y due to multiple revision in tax rates in these categories to ease inflation
- Govt. has collected ~Rs. 250bn in disinvestment receipts thus far (Rs. 205 bn from LIC, 30bn from ONGC and 5 bn each from PPL OFS and GAIL buyback).
- Hence healthy receipts (partly explained by conservative budget estimates) explain the contained fiscal deficit and a relative high cash balance with centre (at Rs. 3.2trillion).
- Government has spent Rs. 2.08 trillion during Apr-Jul'22 of Rs. 7.5 trillion budgeted under FY23 capex.
- Capex spend are up 62% y-o-y (in Apr-Jul) and are mostly directed towards roads (807bn) and railways (462 bn) followed by some spend on defence, housing and urban affairs, food and public distribution and loan to states.

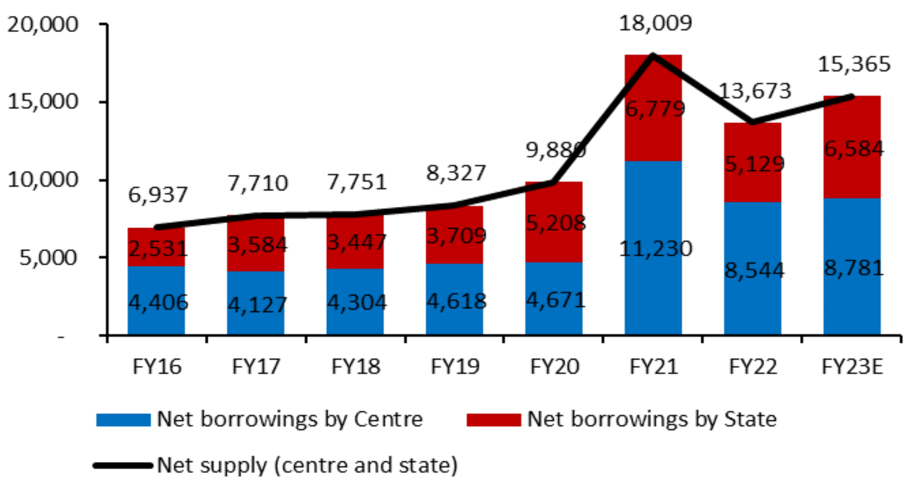
Source: CMIE Economic Outlook, SBIMF Research

Govt aims at gradual fiscal consolidation

General government fiscal deficit expected at 9.6% in FY23



Net government bond supply expected at ~INR 15 trillion (vs. INR 13.7 trillion in FY22)



- Government bond supply stays elevated; Net supply projected to rise to ~Rs. 15 trillion vs. Rs. 13.7 trillion in FY22.
- Demand under current macro backdrop may not be easily forthcoming
- RBI has an agenda to moderate system liquidity which may cap its ability to purchase government bonds.
- The central Government plans to stick to its gross borrowing target (INR 14.3 trillion) despite hit on revenue on account of higher subsidies and reduction in excise duty on petroleum products.
- INR 8.45 trillion to be borrowed from the bond market in HIFY23 to fund the revenue gap.

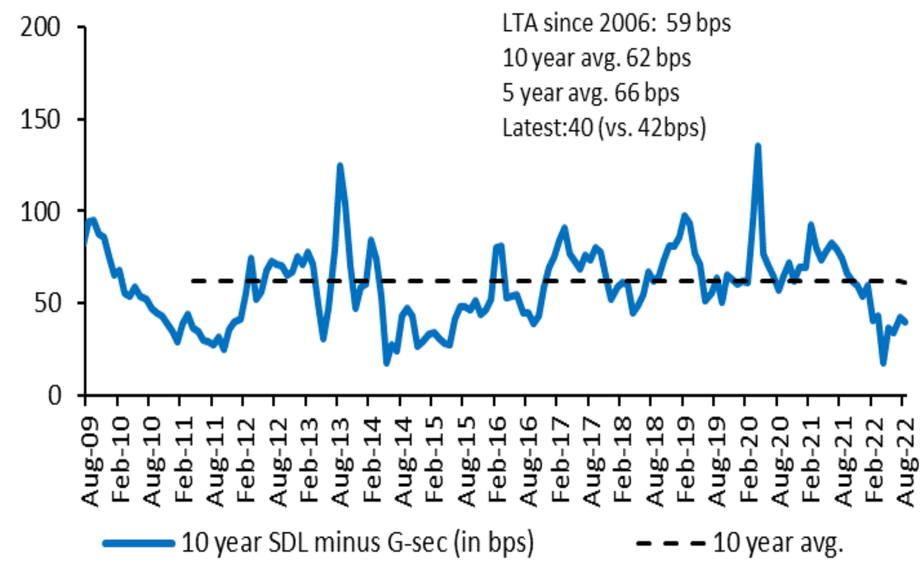
Source: CMIE Economic Outlook, RBI, SBIMF Research

SDL issuances expected to rise in 2H FY23 driving SDL spreads higher

SDL borrowings 82% of indicated calendar in Q2FY23 till date

Rs. Billion	Expected quantum of SDL borrowing as per calendar	Actual Borrowing	Actual Over Expected (in %)
Total borrowing in Q1FY23	1,904	1,102	58
05-Jul-22	130	135	104
12-Jul-22	103	80	78
19-Jul-22	154	128	83
26-Jul-22	240	187	78
02-Aug-22	169	209	124
08-Aug-22	122	138	113
18-Aug-22	128	40	31
23-Aug-22	152	68	45
29-Aug-22	245	140	57
06-Sep-22	128		
13-Sep-22	103		
20-Sep-22	156		
27-Sep-22	287		
Total borrowing in Q2FY23 till date	1,442	1,125	78
Q2FY23	2,116		

SDL spread compressed marginally in August to 40bps (vs 42bps in July) due to reduced SDL supply

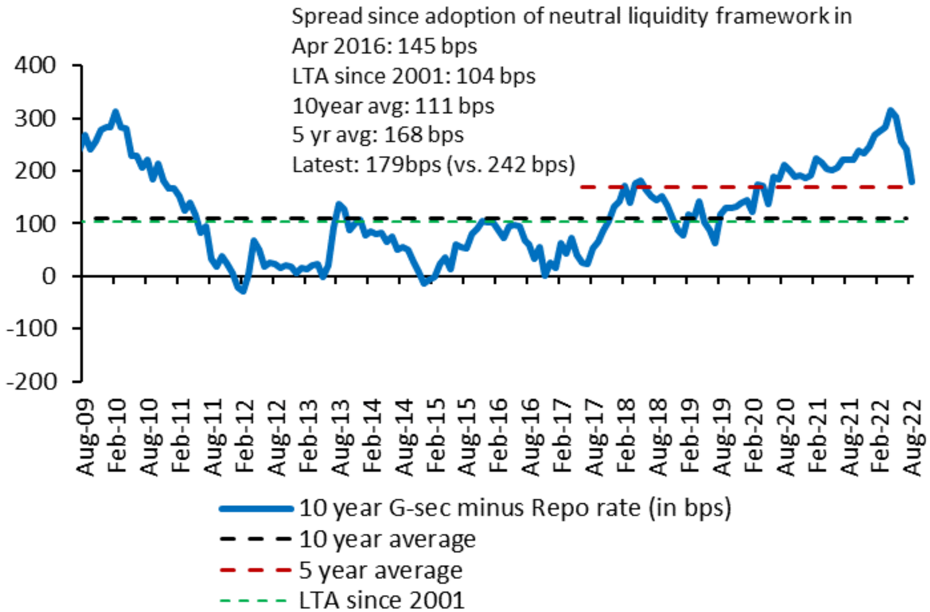


- In Q2FY23, overall SDL issuances has been lower than indicated amount in 6 out of 9 weekly auctions held.
- 5 months FYTD , SDL issuances has been ~67% of the indicated calendar.
- Clearing of past GST dues towards state and increased tax devolution has lead to improved cash flow for states between Apr-August’2022. This in turn has led to overall SDL issuances being lower than indicated calendar FYTD.
- As most of these gains peter out and compensation cess gains ends going forward, we expect SDL issuances to rise in coming months through FY23.

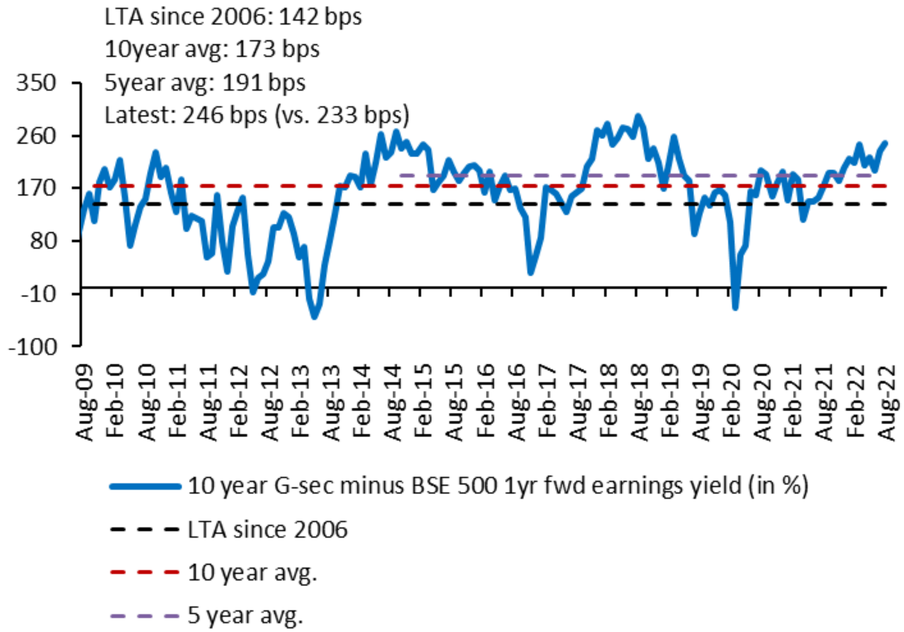
Source: RBI, Bloomberg, SBIMF Research

G-sec valuations relative to Equity turns marginally attractive

10-year GSec relative to Repo has fallen in recent months to fall in line with 5 year average



G-sec spread vs. equity increased to 246bps in Aug'22 vs. 233 in Jul'22



Source: Bloomberg, RBI, SBIMF Research

India witnessed debt inflows in Aug'22

India witnessed Debt inflows in Aug'22

EM FII Debt inflow US$ million	2020	2021	May-22	Jun-22	Jul-22	Aug-22
South Korea	62,283	1,06,256	5,041	8,198	4,715	3,513
Mexico	(10,027)	(12,668)	(34)	(929)	(2,733)	3,294
Russia	5,403	9,489	5,225	2,642	2,642	2,642
Indonesia	(4,684)	(4,906)	(805)	(1,118)	(1,933)	730
Thailand	(1,005)	6,550	876	(440)	(96)	591
India	(13,853)	(1,525)	(699)	(257)	(291)	539
Ukraine	(1,117)	283	(69)	(40)	(3)	(60)
South Africa	(2,323)	(13,276)	(1,190)	(2,110)	(1,602)	(495)
China	1,87,219	1,32,282	(28,637)	(52,882)	(51,703)	(52,602)
Philippines	6,297	3,900	-	1,654	-	-
Malaysia	3,248	2,976	122	(196)	(736)	-
Brazil	(3,822)	(15,114)	2,110	-	-	-
Bulgaria	2,060	272	(7)	(1)	-	-
Czech Republic	8,577	1,279	2,603	(5,905)	-	-
Poland	(7,380)	(7,089)	3,586	307	-	-

Source: CEIC, Bloomberg, RBI, SBIMF Research; NB: '-' implies data not available for the respective country

Debt Outlook: Staggered approach to build duration

- August was a volatile month for the bond market. US 10 year see-sawed from above 3% to finally settle at 3.10% by end August.
- US Fed raised rates by 75bps in July for second consecutive meeting taking the Fed rate to nearly 2.5% , right on top of long-term neutral Fed funds rate. During the latest Jackson Hole Symposium, US Fed chair gave a clear mission statement to get inflation under control.
- There has been a 20bps of upward revision to market expectation on peak Fed Funds rate post the Jackson Hole Symposium (from 3.64% to 3.83%). That said, market still expects this to be quickly reversed by rate cuts in 2H 2023- despite a hawkish undertone from latest Fed Commentaries.
- RBI has sold dollar aggressively to cushion the impact of stronger dollar. FX reserves has dropped nearly 30 bn dollar in last two months. If the recent brake pulled on both capital outflow and commodities persists, depreciation pressures could be capped.
- Central govt. finances are healthy despite sudden costs incurred on multiple front due to higher commodities. That has enabled continued infrastructure spending.
- RBI has delivered 140bps of rate hike. But more significantly, liquidity has seen a rapid correction owing to FX sell, 50bps of CRR hike and an absence of any G-sec purchase by the central bank also adds. Normalization in RBI policy will happen over the next six months. We expect policy rate to settle around 6%.
- As we have maintained earlier, policy rates moving closer to neutral, RBI emphasizing the midpoint target of 4%, while being alert towards external sector stability were the key variables to provide more confidence. This has largely been met with the MPC meeting in August. And provides us some space to incrementally add duration.
- However, volatility in rates markets, especially in the context of continuous repricing of policy rate expectations in overseas markets would warrant a staggered approach alongside adequate focus on liquidity.

Source: Bloomberg, SBIFM Research

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