HDFC Bank Research

Presentation

November 2022

Risk Profile based Asset - allocation

Asset Class	Overall View	Asset Allocation		
		Aggressive	Moderate	Conservative
Equity Funds	◆	75%	55%	25%
Debt Funds	◆	20%	40%	70%
Gold	▲	5%	5%	5%

Note:	Optimistic	▲
	Cautiously Optimistic	◆
	Cautious	▼

Category wise view

MF Categories	View
Equity Oriented Funds	
Largecap Funds	▲
Large Cap Index Funds	◆
Multi/Flexicap Funds	◆
Large and Mid Cap Funds	◆
Mid cap / Small cap	◆
ELSS	◆
Value / Contra / Dividend Yield Funds	▲
Focused Funds	▼
Aggressive Hybrid Funds/Dynamic Asset Allocation/Balanced Advantage Funds	▲
Equity Savings Funds	▲
Sector/Thematic Funds	▼

MF Categories	View
Debt Oriented Funds	
Short Duration Funds/Medium Duration Funds	▲
Target Maturity Index Funds	▲
Medium to Long / Long Duration Funds	▼
Dynamic Bond Funds	◆
Gilt Funds	▼
Ultra Short Duration/Low Duration/Money Market Funds	▲
Arbitage Funds	◆
Liquid/Overnight Funds	▲
Conservative Hybrid Funds	◆
Credit Risk Funds	▼

Classification - Restricted

Equity MF Strategy & Recommended Asset Allocation

- The US Fed has continued on its path to hiking rates and tightening liquidity to control demand led inflation, yet key data points in the US suggest that this fight could take long.
- Europe remains in a bigger mess with higher energy costs, weakening consumer confidence and tightening monetary policy which can structurally impact the growth of the EU.
- Multilateral agencies continue to warn of a weaker global growth outlook for CY22 and CY23, led by the Russia Ukraine conflict, high inflation and tight money supply.
- Due to expectation of slowdown, the commodity prices have consolidated, which is likely to have a sobering impact on global inflation. Energy costs still remain high.
- OPEC believes that demand for crude oil could continue to rise for the next 20 years, despite transition into renewables.
- Despite the slowdown fears the global equity markets rallied in October, led by value buying and expectations of a Fed pivot as growth impulses weaken.
- Sharp appreciation of US Dollar is also putting a lot of pressure on global currencies and economies.
- China too has seen marked slowdown owing to Covid-19 led shutdowns and the issues in its housing market.
- The overall economic indicators in India continued to show positivity and urban demand showing reasonable strength. Rural demand is starting to see green shoots, while rising inflationary pressure could hurt demand dynamics.
- Corporate and Banking sector balance sheets in India have shown strong improvement, capacity utilisation data too have shown improvement and this is setting stage for increasing private capex demand.
- While consumer confidence continues to remain strong, rising inflation poses risk to this as it hurts the consumer/corporate surplus, this is a key monitorable from corporate earnings perspective.
- The Government is clearly focussed towards driving the capex in the economy through its own spending and incentive driven private capex.
- To control the rising impact of inflation on growth, the RBI raised the Policy Repo Rate and also started to take steps to move towards liquidity normalisation, to cushion the inflationary impulses.
- Given its strong growth differential and strong retail participation in the equity markets with other peer economies, India has been an outperformer in the EM basket. Any changes in these could have implication for the Indian market valuations.
- Q2FY23 results have seen stable topline growth, but margins pressure in many sectors is impacting the profit growth. Earnings expectations could see too could also see marginal downgrades. Key alpha sectors seems to be Banking, Auto, Infra, while Pharma seems to be emerging out of its slumber.
- The market saw steady performance in the frontline indices in the month of October, while the larger indices lagged, impacting alpha generation in the funds.
- Declining liquidity, earnings cuts and rising rate could still weigh on the market valuations. However, in the longer term improving domestic macro conditions, higher capex investments and stable consumption growth could drive the Indian corporate earnings higher and support the equity markets.
- We expect the return expectations over 2-3 year period to be in line with earnings growth, with marginal valuation compression. However, with slowing global growth future earnings potential would remain a key monitorable. We continue to maintain **an investment deployment strategy of 50% lumpsum and rest 50% to be staggered over the next 3-4 months with a cautiously optimistic stance.** Investors could focus on Large Cap, Large & Midcap, Value, Hybrid Equity funds as portfolio core, in line with their risk profile and product suitability.

Debt Mutual Fund Strategy

- **Given the expected volatility and uncertainty and expectations of flattening of the yield curve, staying invested at the short and the very short end of the yield could be better from risk reward perspective currently.**

- **Thus, investors should look at funds oriented towards the shorter end of the yield curve for relative stability in the near term and to benefit from the reset in interest rates on the higher side. For this one can look at Short Duration Funds, Money Market Funds, Ultra Short Duration and Low Duration Funds for a horizon of 12 months and above.**

- **For investors looking for accrual strategies, they can consider Target Maturity Index Funds that invest in a mix of better quality bonds with investment horizons matching the maturity of the funds.**

- **Investors who are comfortable with volatility and have a longer investment horizon could look at Dynamic Bonds for a horizon of 24 months and above.**

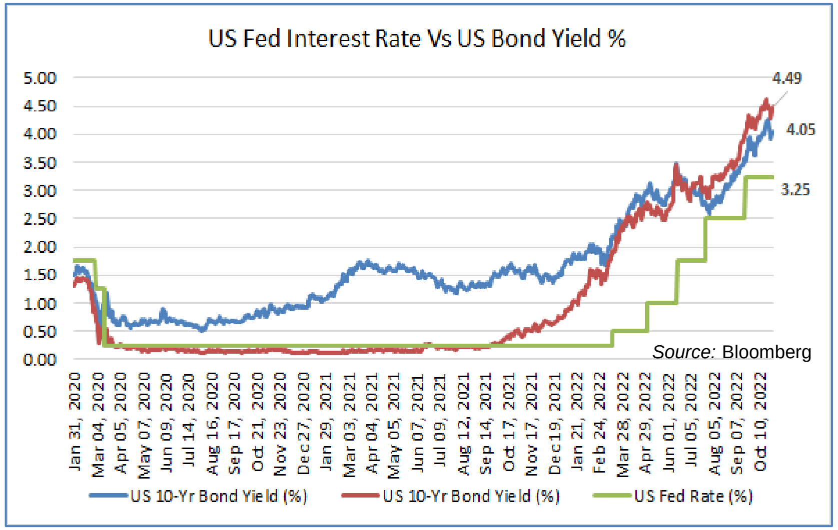
- **For a horizon of 3 months and above Arbitrage and Money Market Funds can be considered. Whereas, for a horizon of up to 3 months investors can consider Overnight Funds and Liquid Funds.**

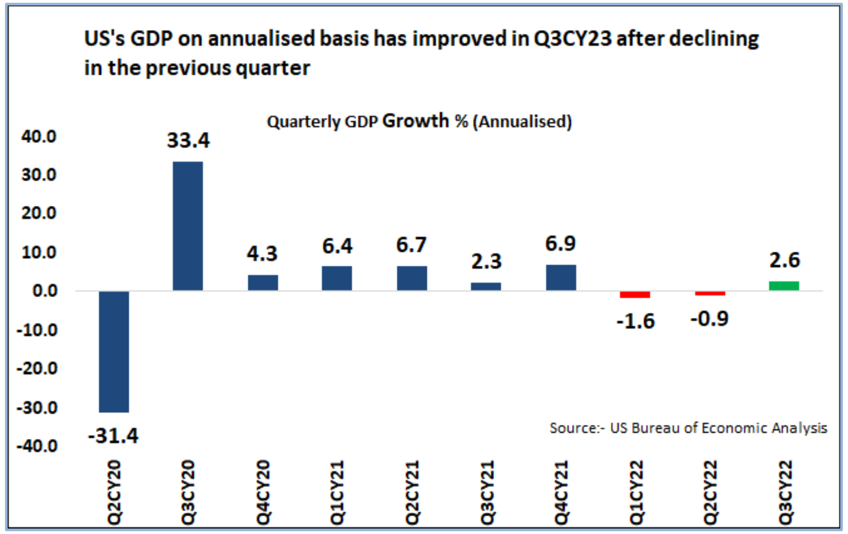
- **Investors should invest in line with their risk profile and product suitability.**

Classification - Restricted

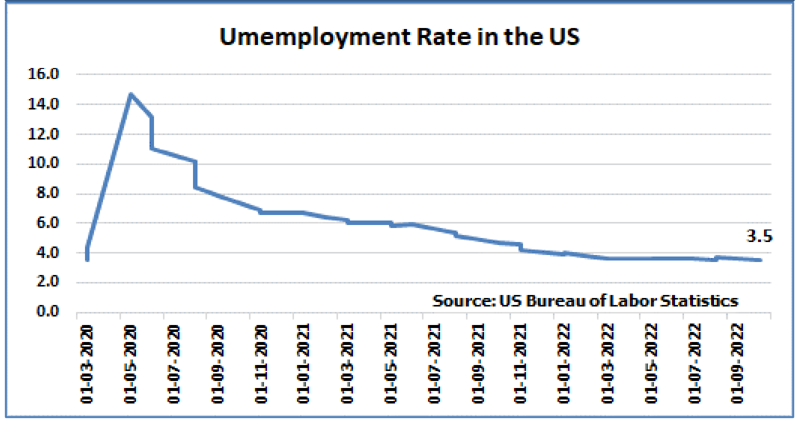
Research Presentation – Contents

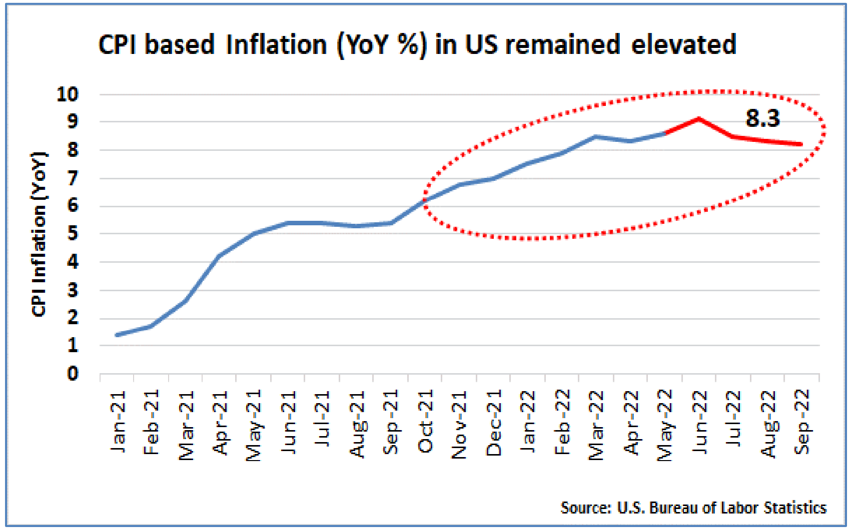
US Interest rates continue to rise as Inflation and other key macro data remains strong, while steady fundamentals, expectations of Fed Pivot and bottom fishing led to strong rally in the US markets

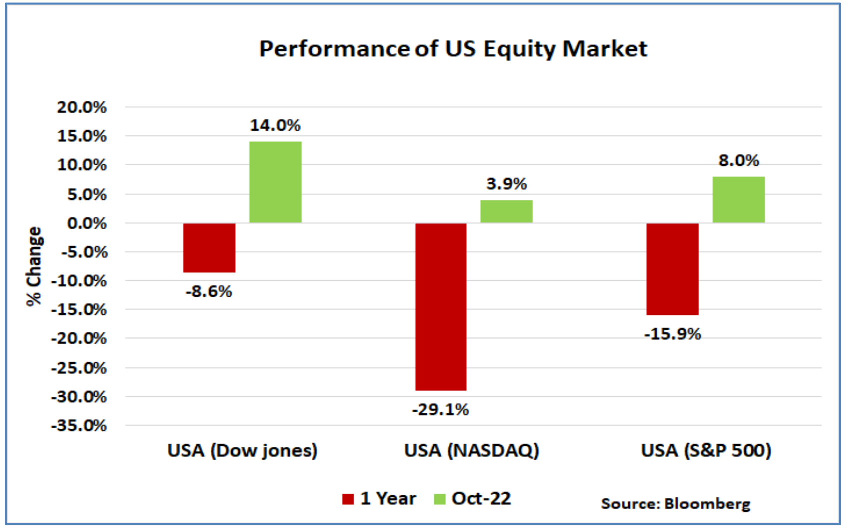


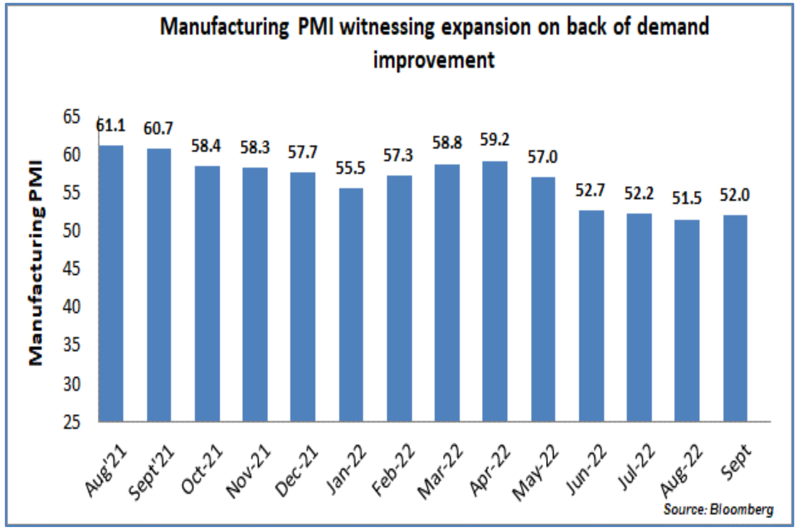


No. of unemployed persons per job opening, seasonally adjusted is at 0.5 whereas, unemployment rate stands at 3.5%.

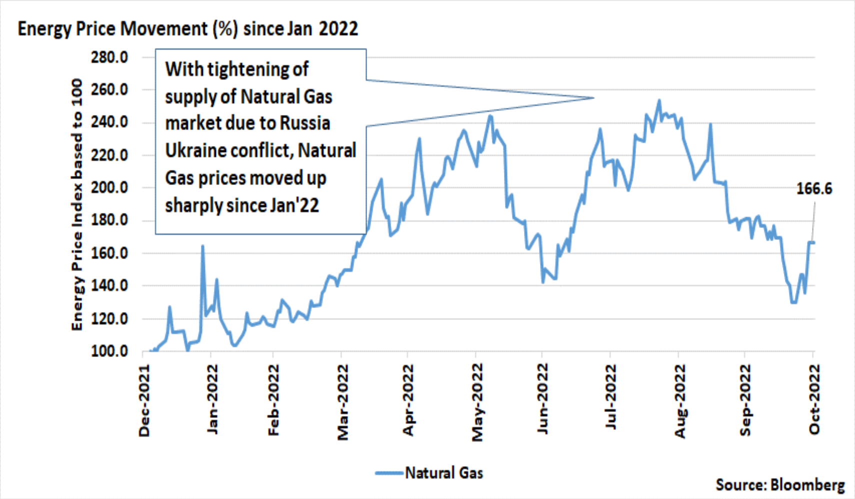


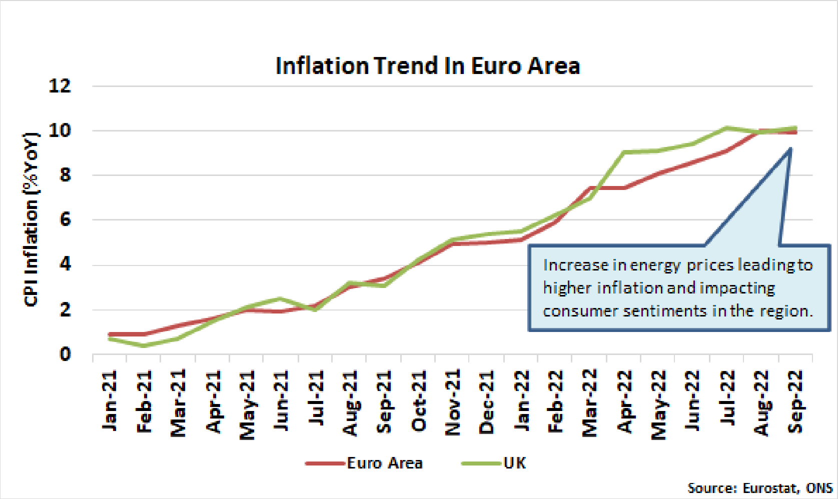


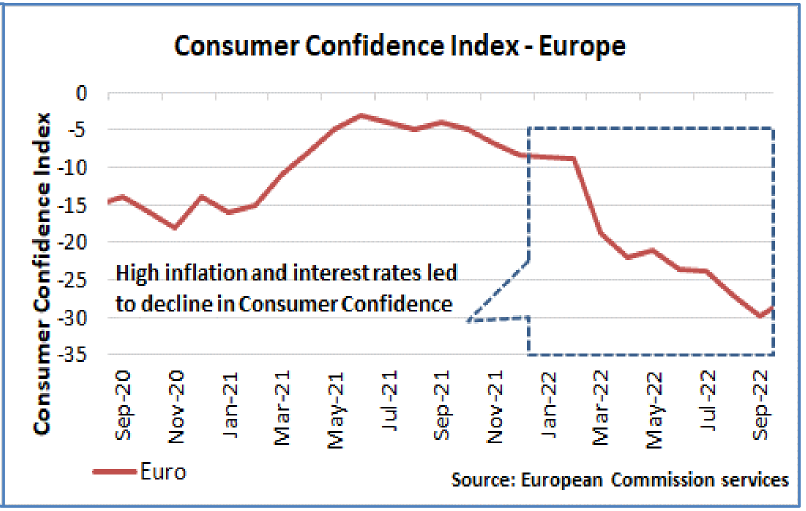


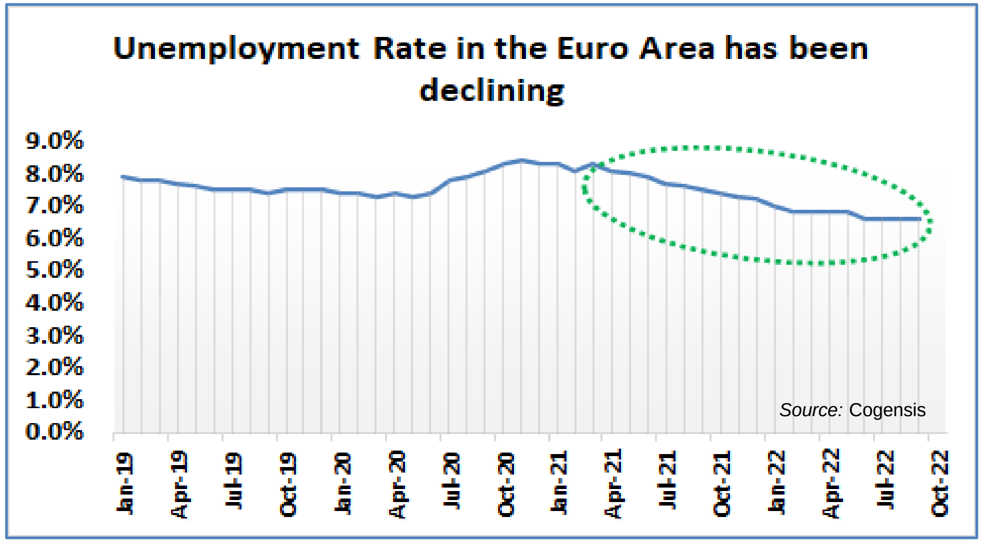


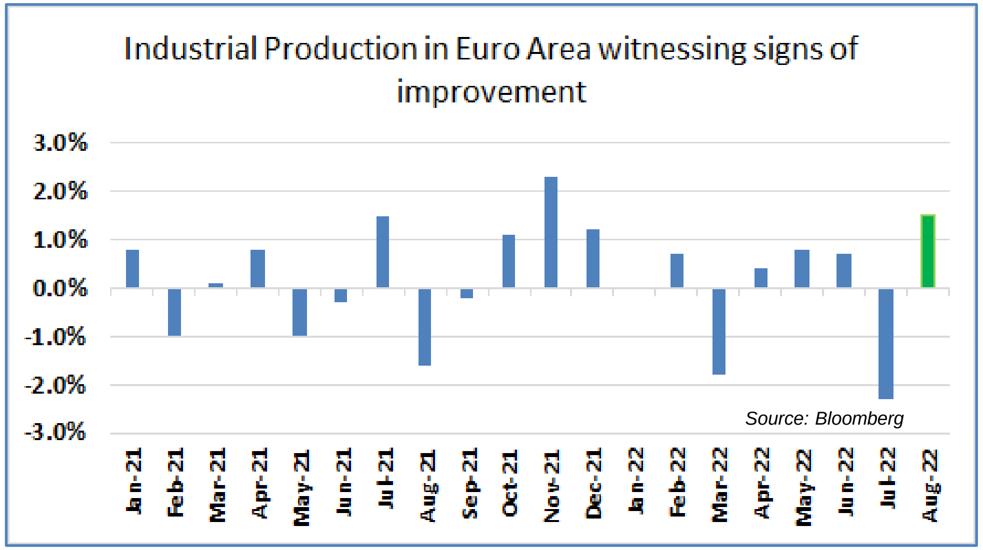
Europe continues to struggle with stagflation and high energy costs, on the back of ongoing Russia-Ukraine Conflict











Europe has unveiled Euro 200 bn energy-assistance plan for its households and businesses.

Despite strong inflationary headwind and cost of living issues in Europe, Subsidy for energy should help Consumer and Industries.

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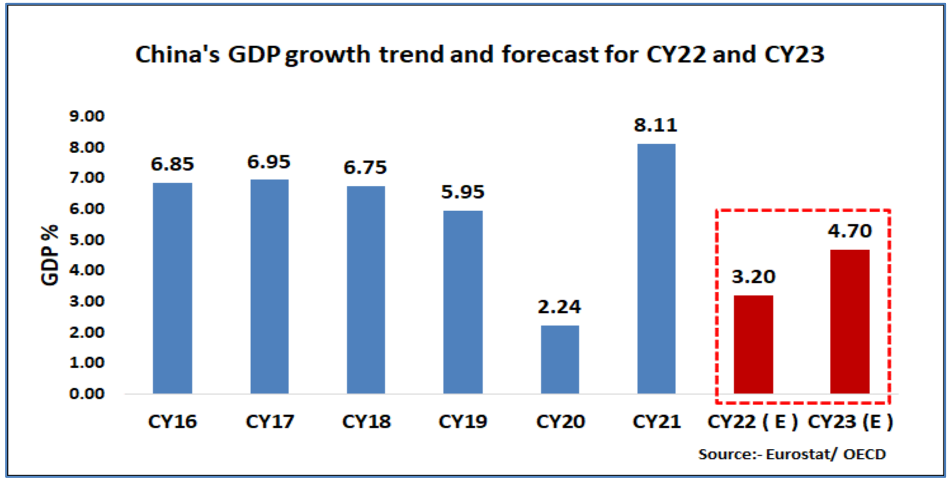
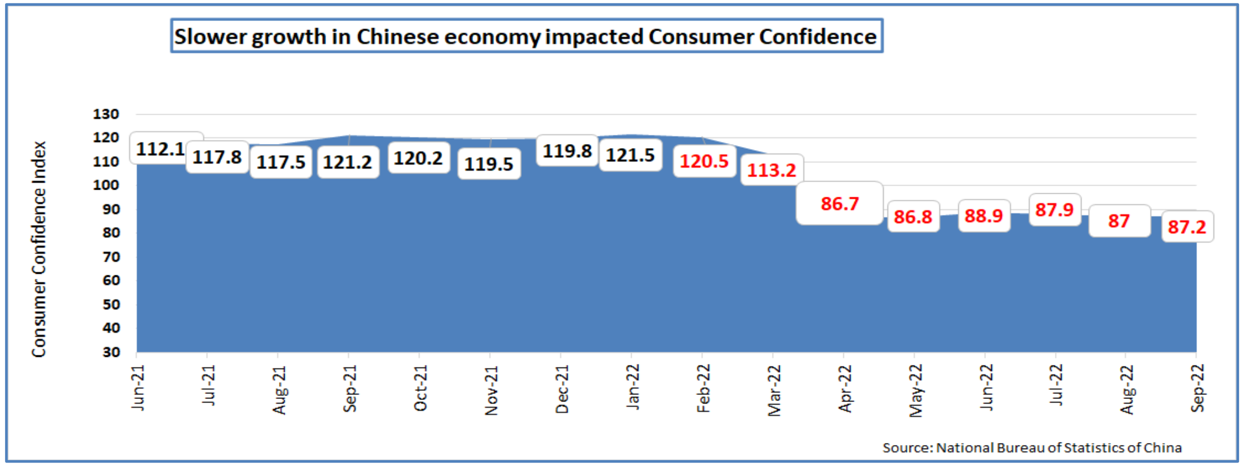
Classification - Restricted

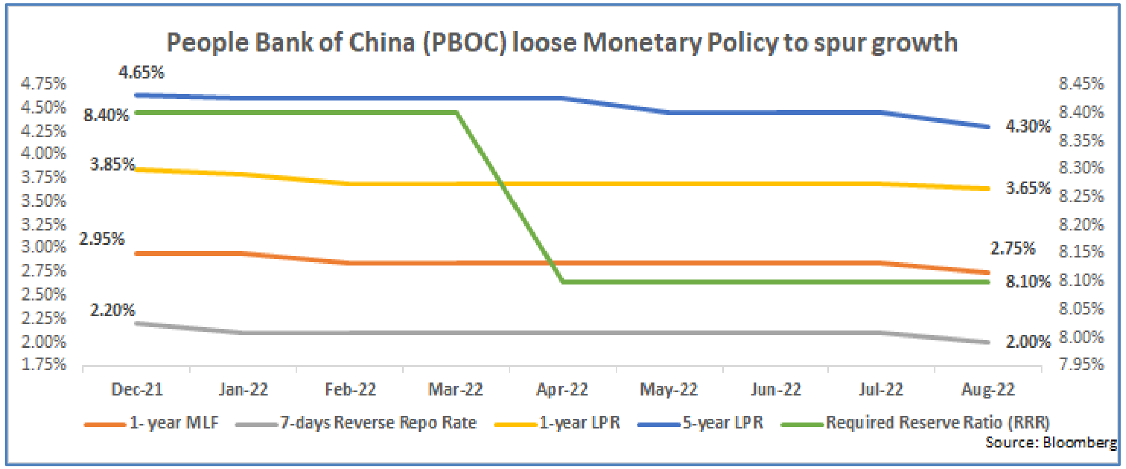
Chinese market correct as Xi Jinping reappointed for third term… while the economy continues to falter

Xi Jinping has tightened his grip on power, shutting-out known reformers to effectively take sole charge of the economy, making investors nervous.

COVID containment policies, crisis in China's real-estate market and growing fears of a recession impacting economic activities in China



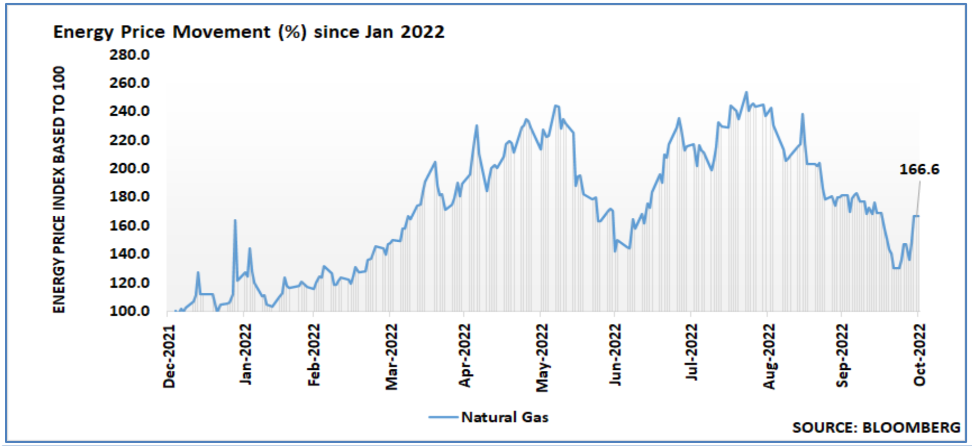


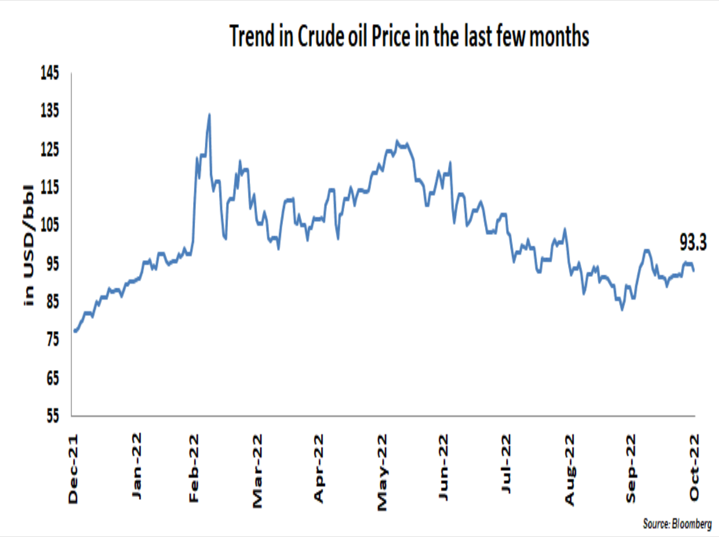


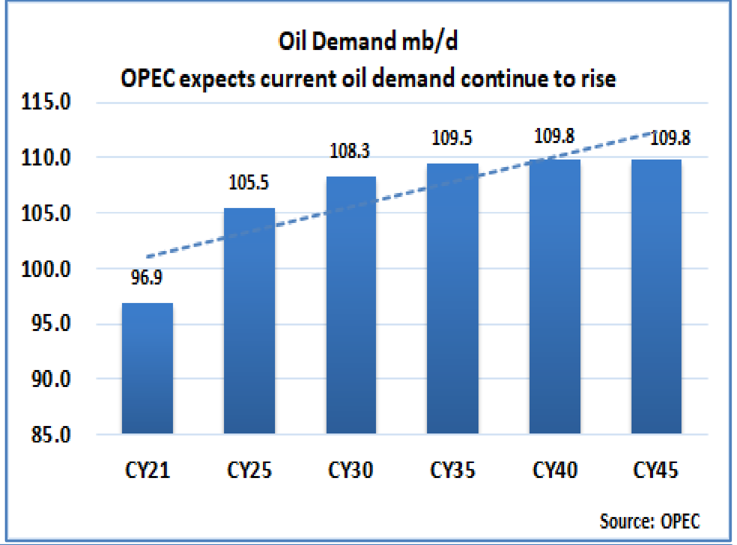
Classification - Restricted

Industrial commodity consolidating but Energy prices remained elevated…
… While Agri commodities saw mixed trends

Tightening of supply of Natural Gas market due to Russia Ukraine conflict led the Natural Gas prices elevated

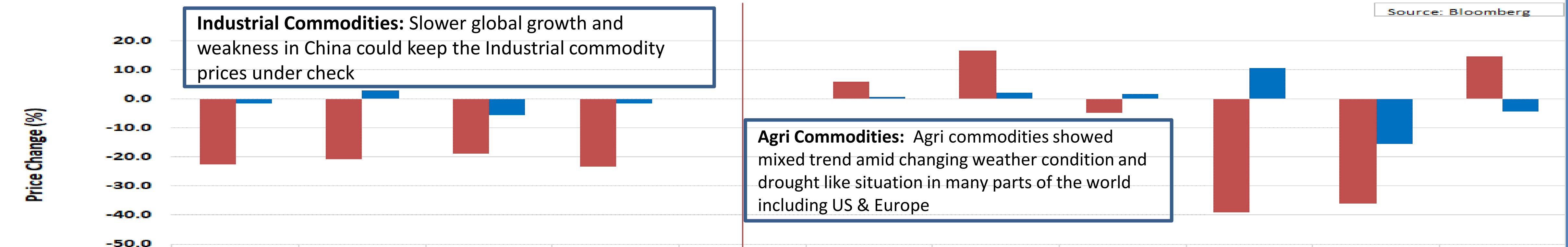






Industrial Commodities: Slower global growth and weakness in China could keep the Industrial commodity prices under check

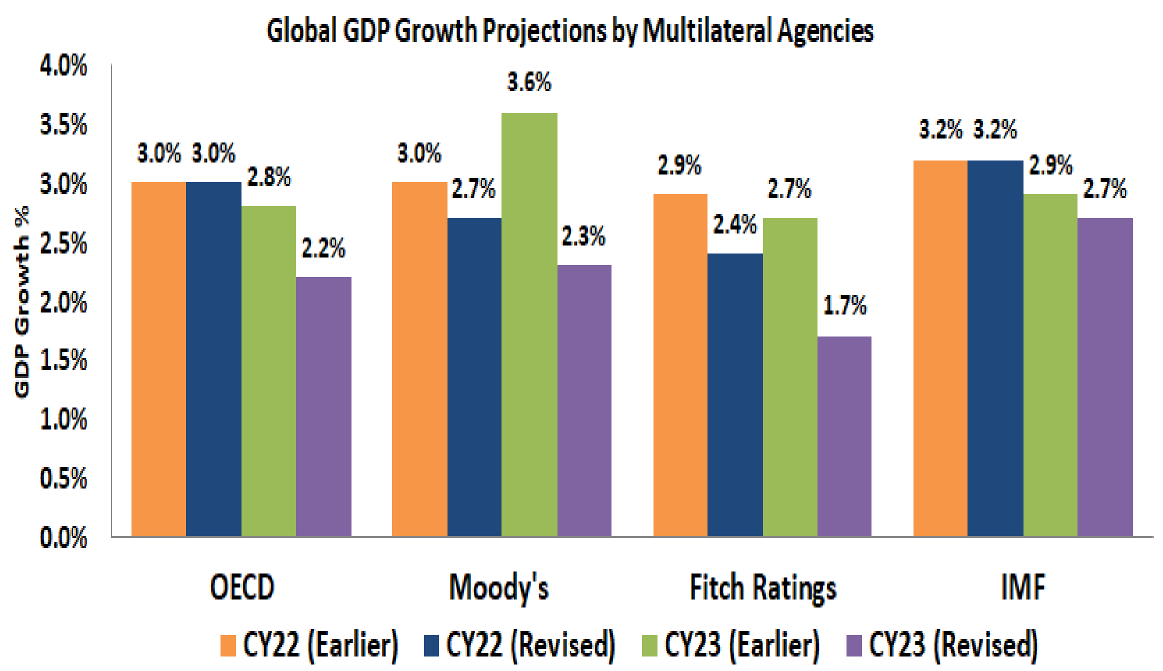
Agri Commodities: Agri commodities showed mixed trend amid changing weather condition and drought like situation in many parts of the world including US & Europe



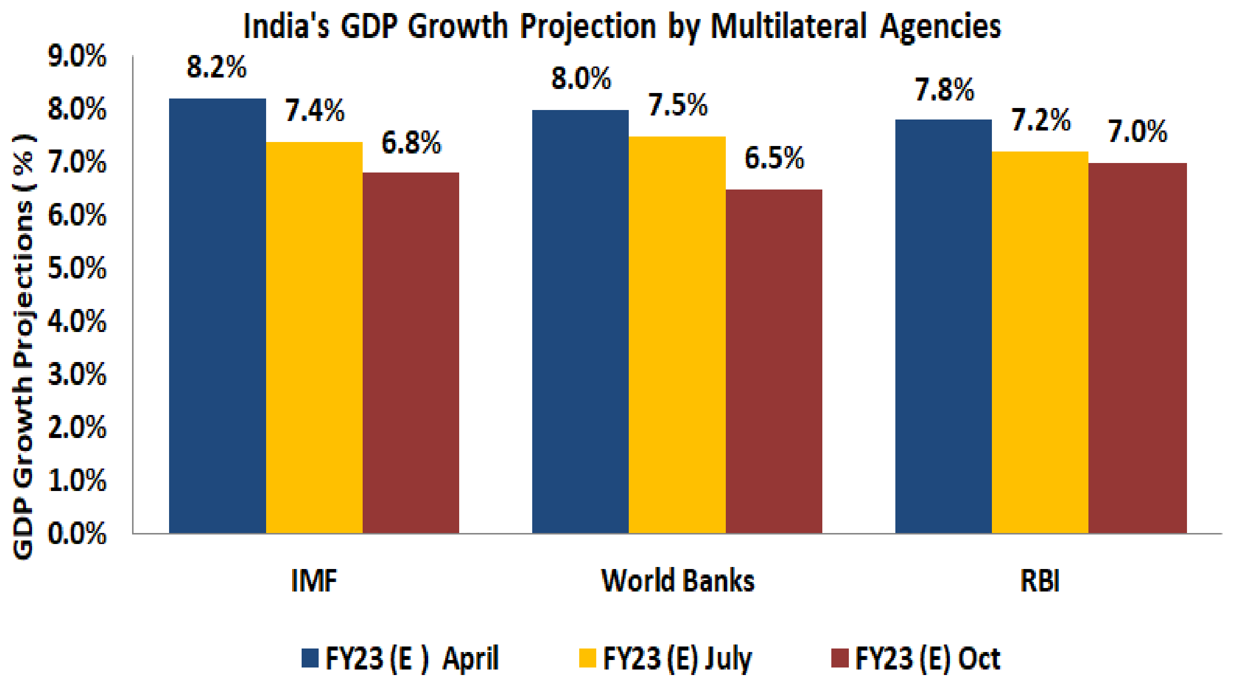
	LMEX Metal	Aluminium	Steel	Copper	BBG Agriculture	Corn	Sugar	Palm Oil	Cotton	Wheat
Since Jan'2022	-22.5	-20.9	-18.9	-23.4	5.9	16.6	-4.8	-39.1	-36.1	14.5
Oct-22	-1.5	2.8	-5.5	-1.5	0.5	2.1	1.6	10.5	-15.6	-4.3

Classification - Restricted

Multilateral agencies expect weak global growth going forward, driven by tightening monetary conditions…
…While India would still be one of the fastest growing economies in the world

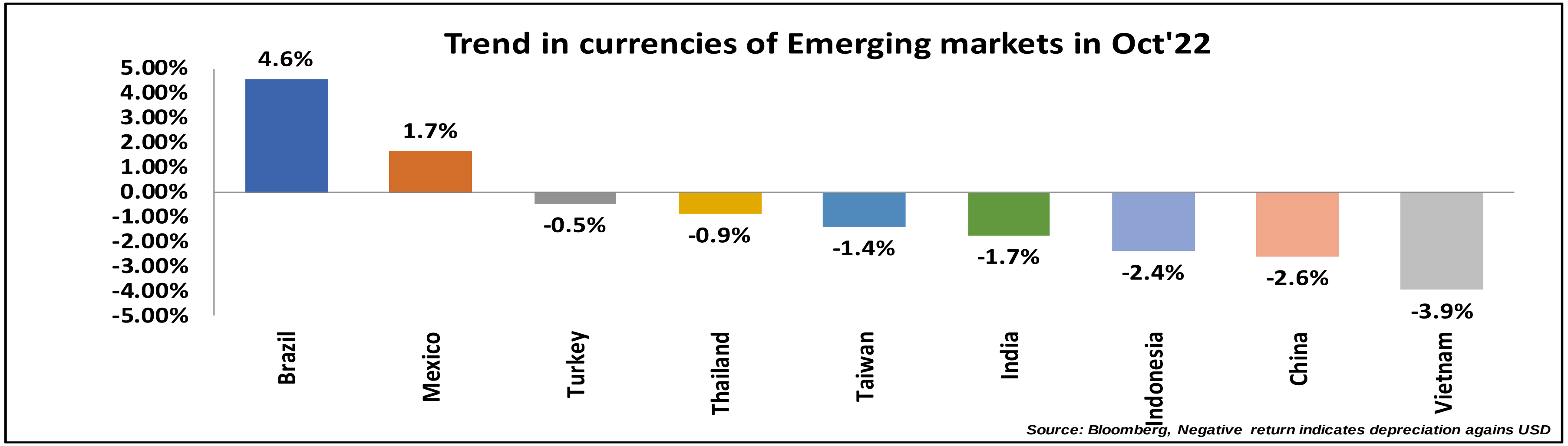


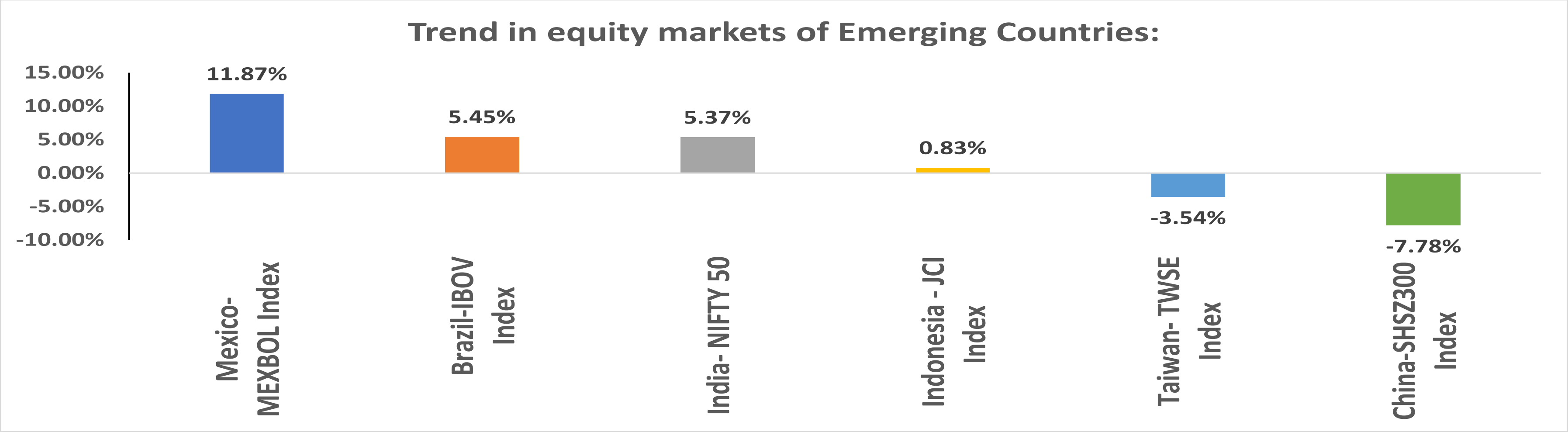
Source: Media Reports



Source: Media Reports

While most EMs currencies weakened…. Equity markets rose tracking similar movement in the developed markets

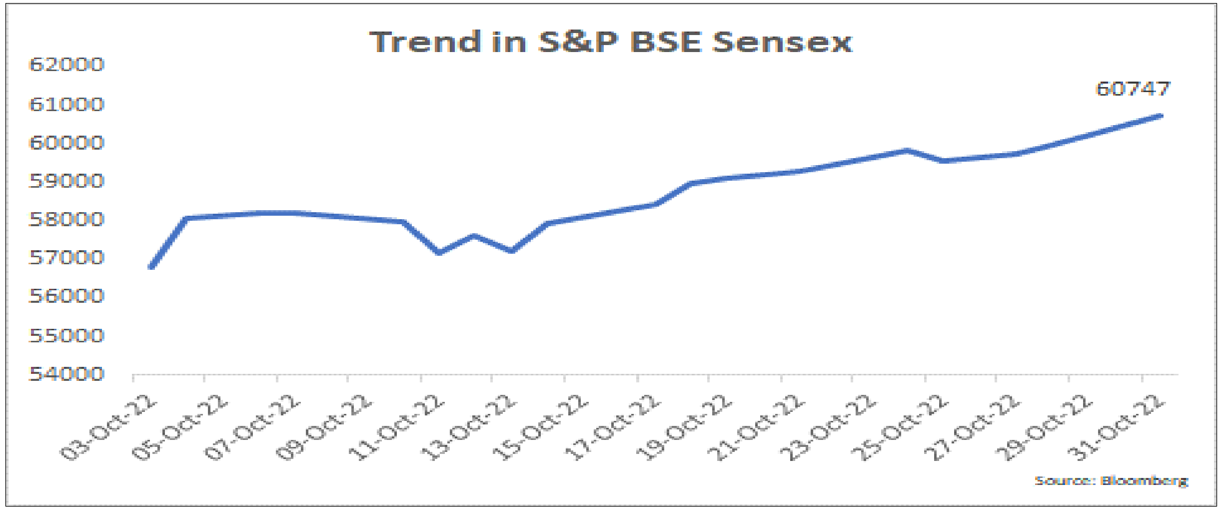


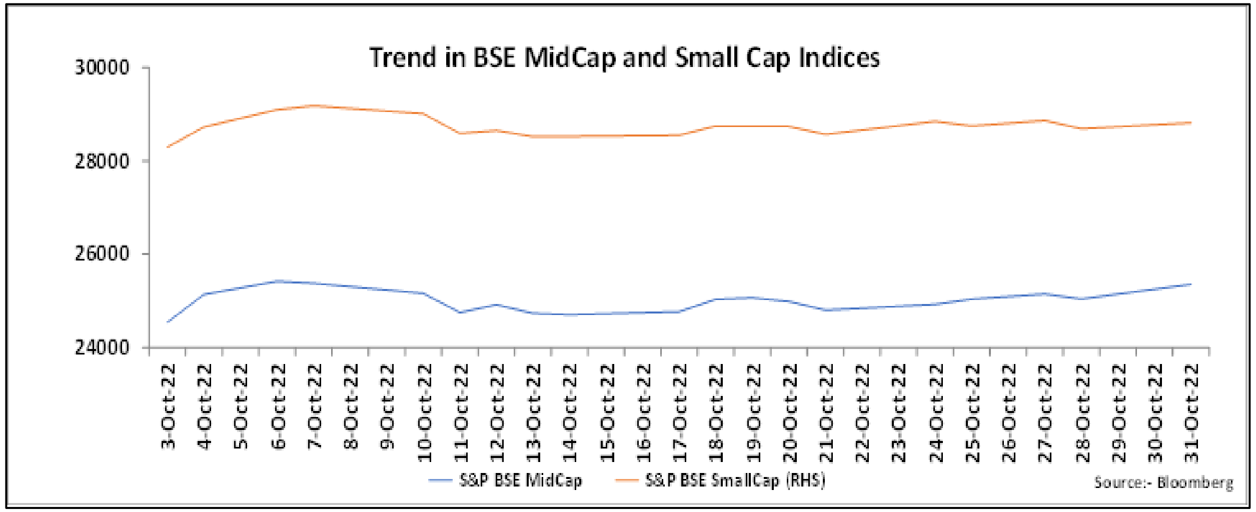


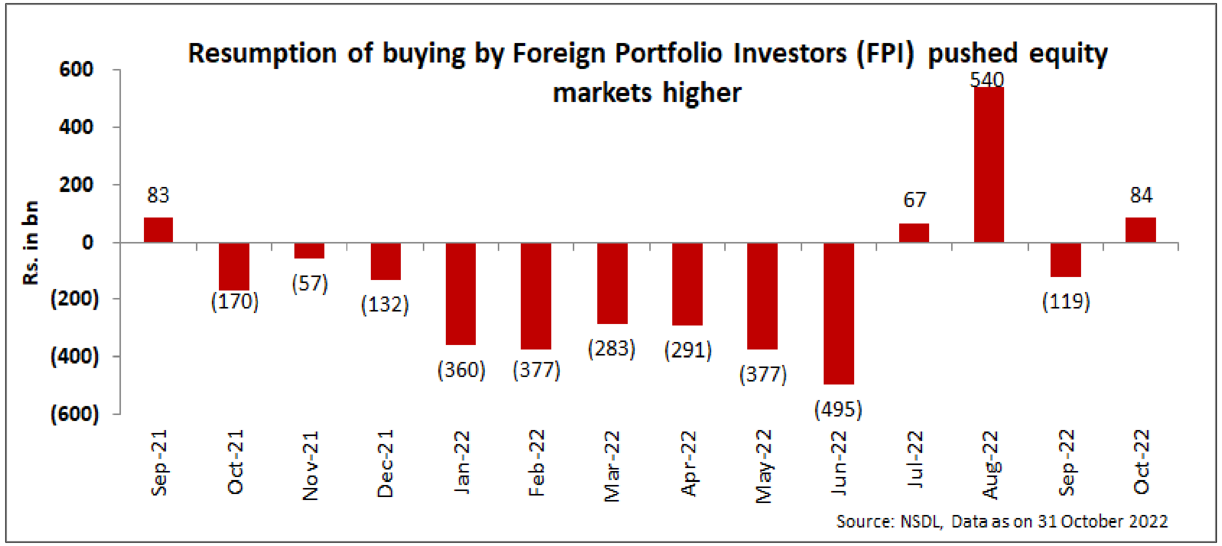
Source: Bloomberg

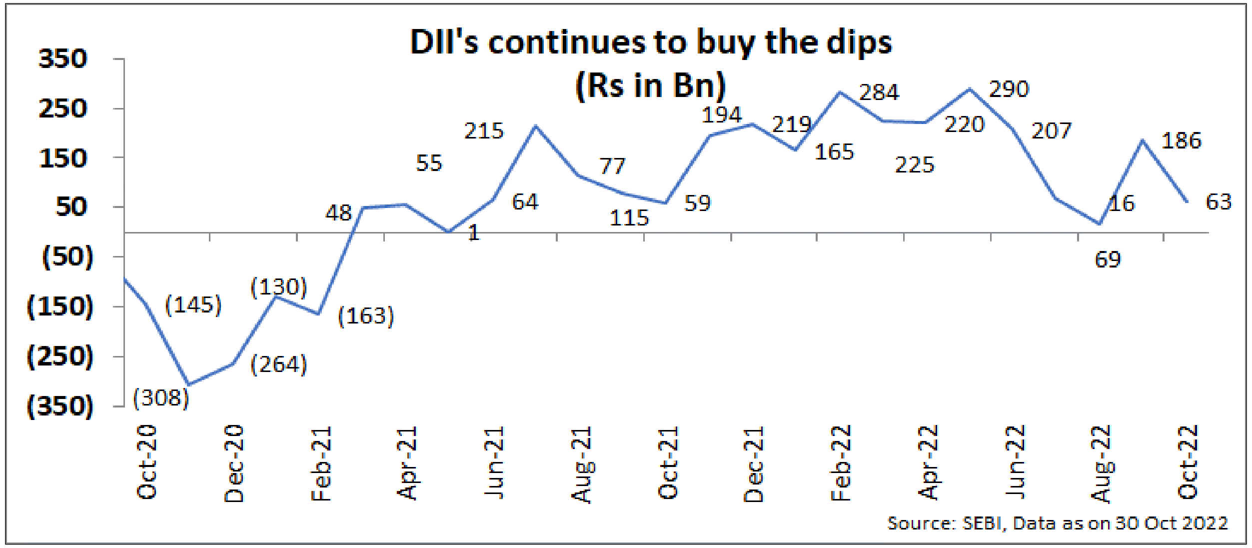
Classification - Restricted

Indian markets remained positive in October on the back of strong DII flows, stable macros and revival in FPI flows…

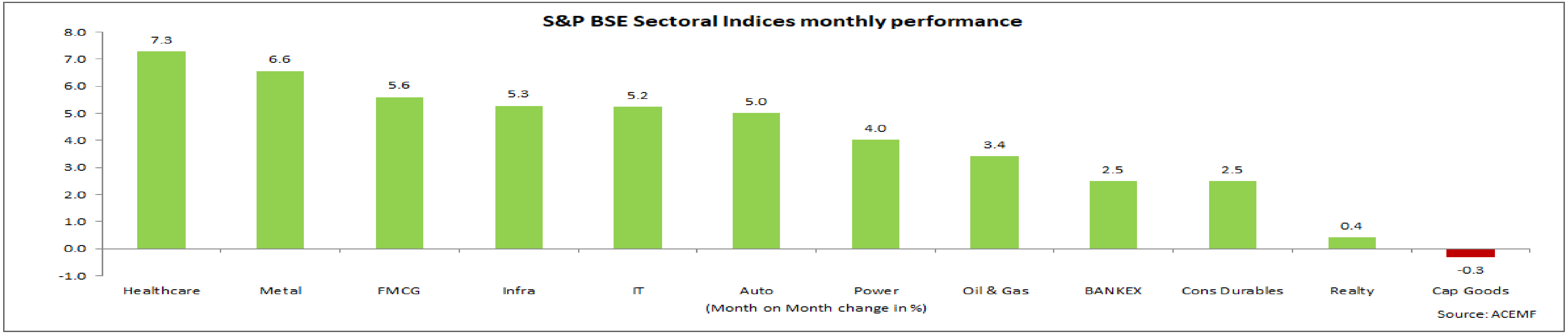


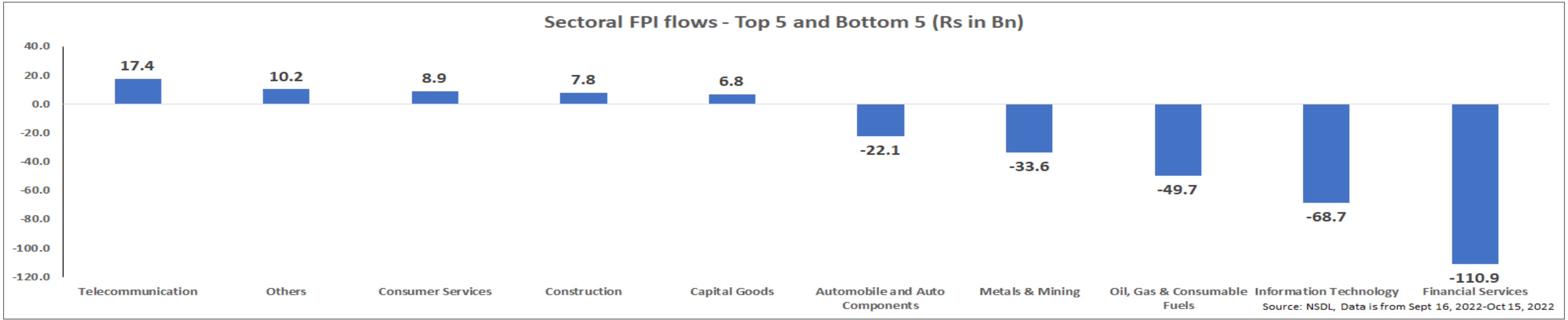






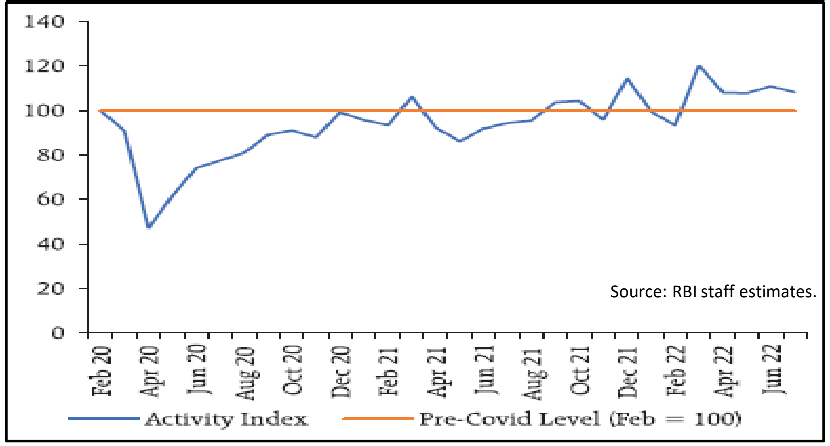
Sectoral equity indices - Performance and FPI flows for October 2022

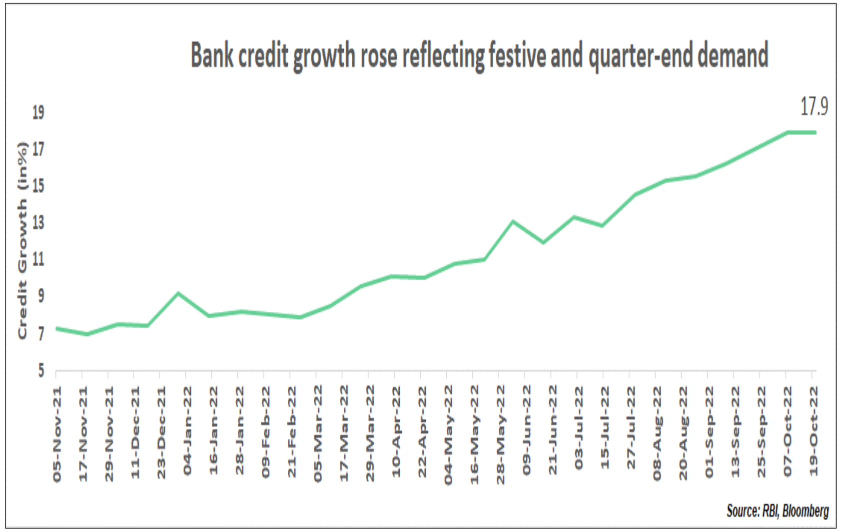


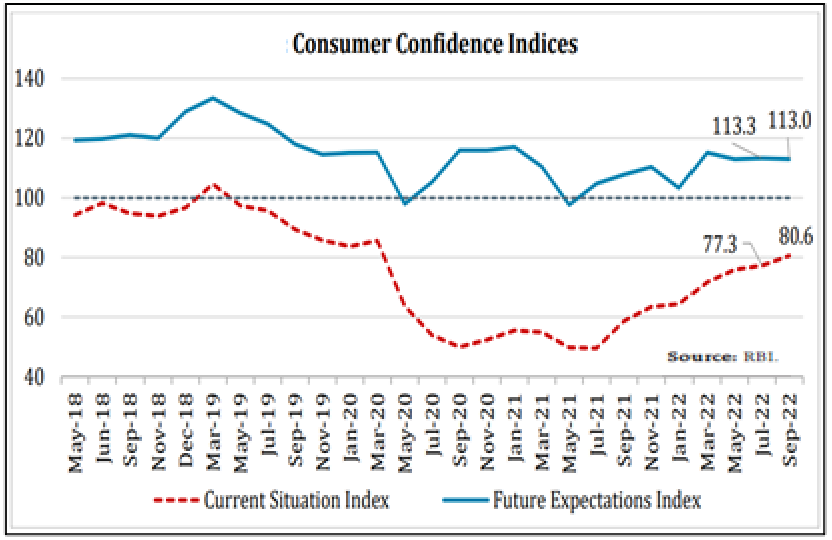


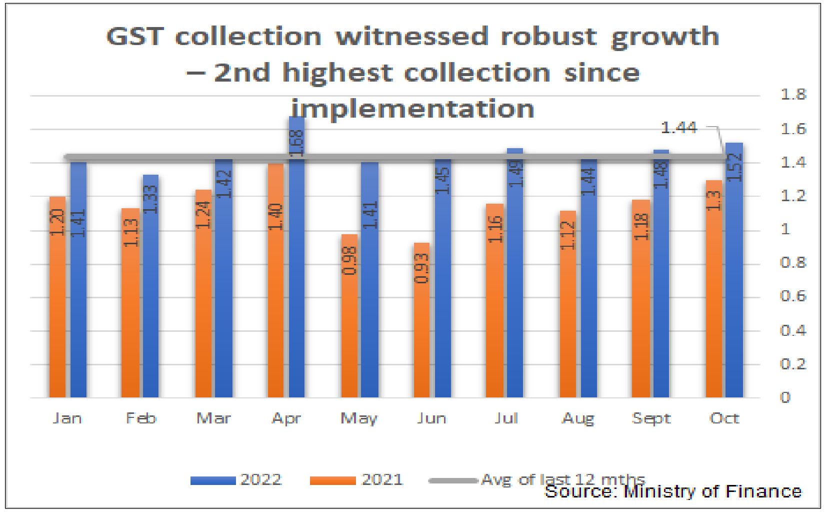
Domestic macro conditions remains strong ….

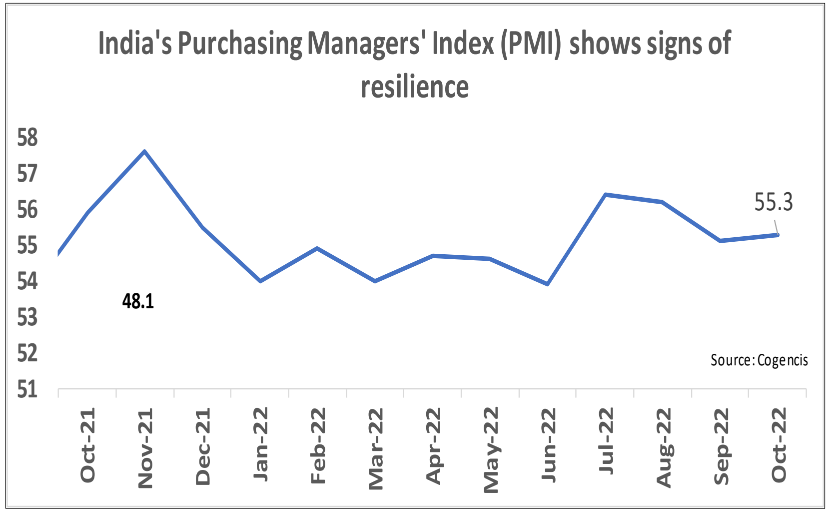
High frequency indictors of economic activity continues to show momentum



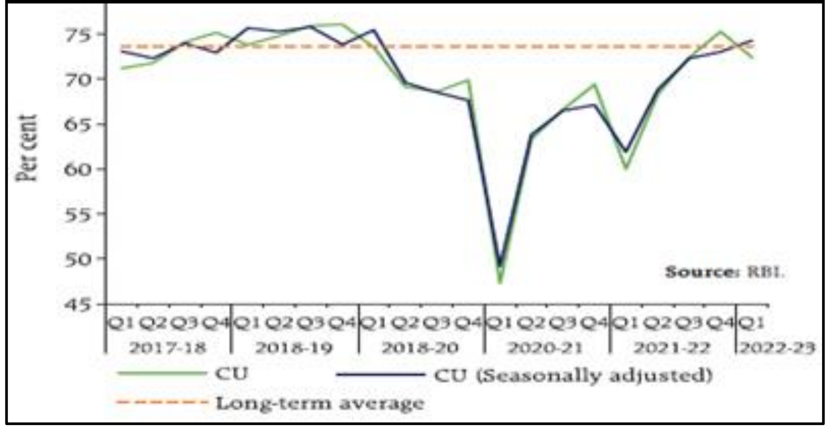




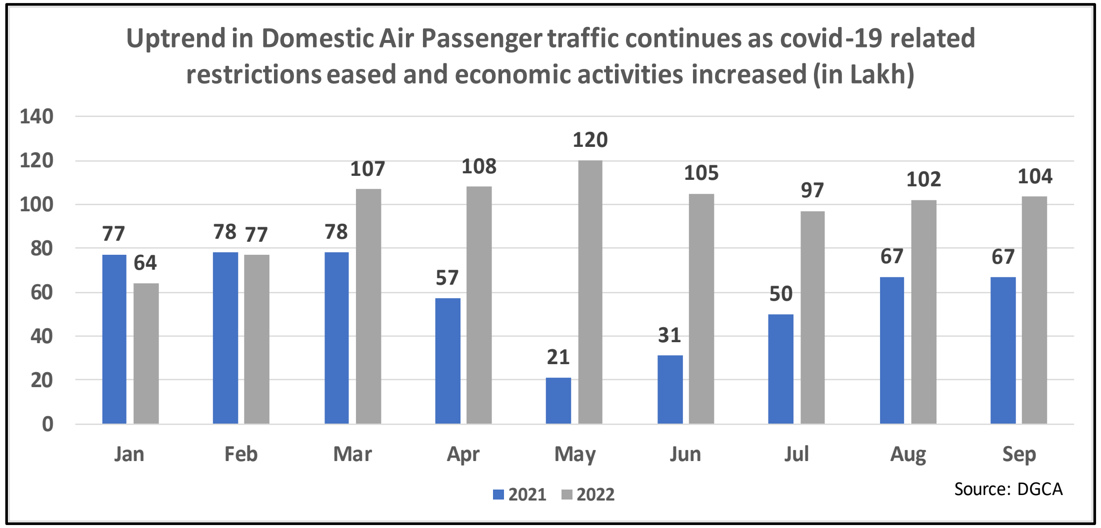


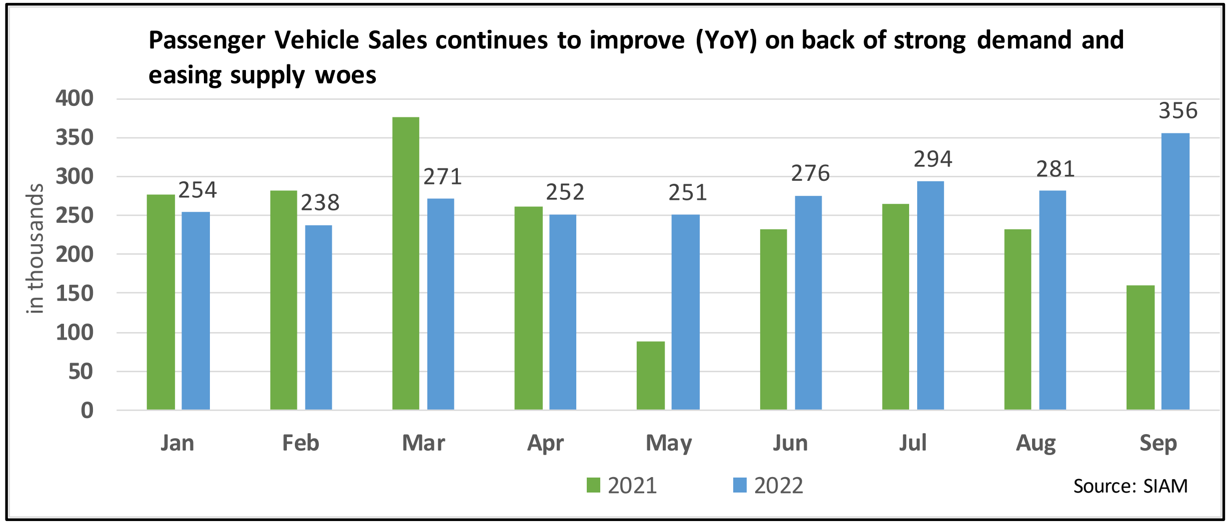


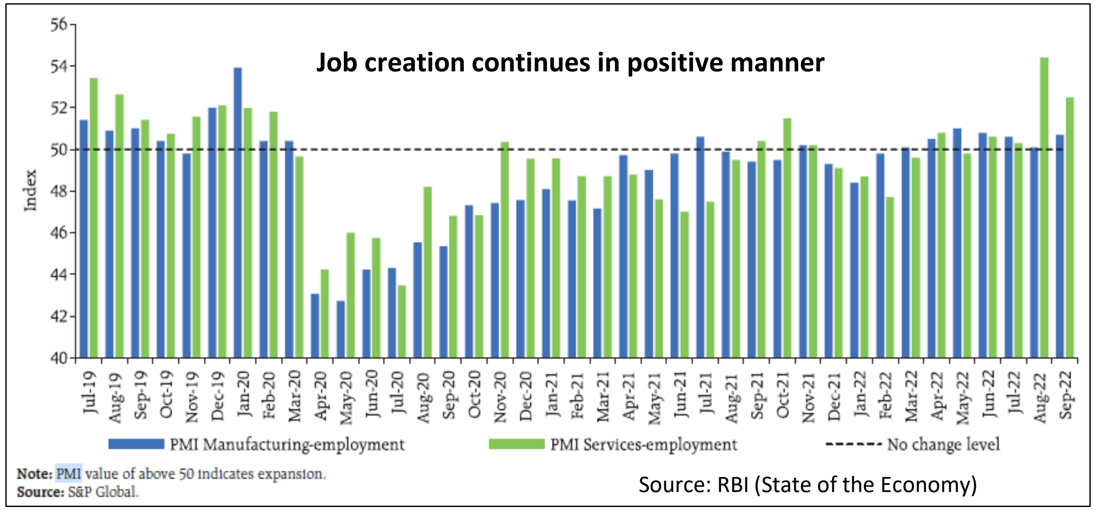
Capacity Utilization in Manufacturing is showing signs of Rebound

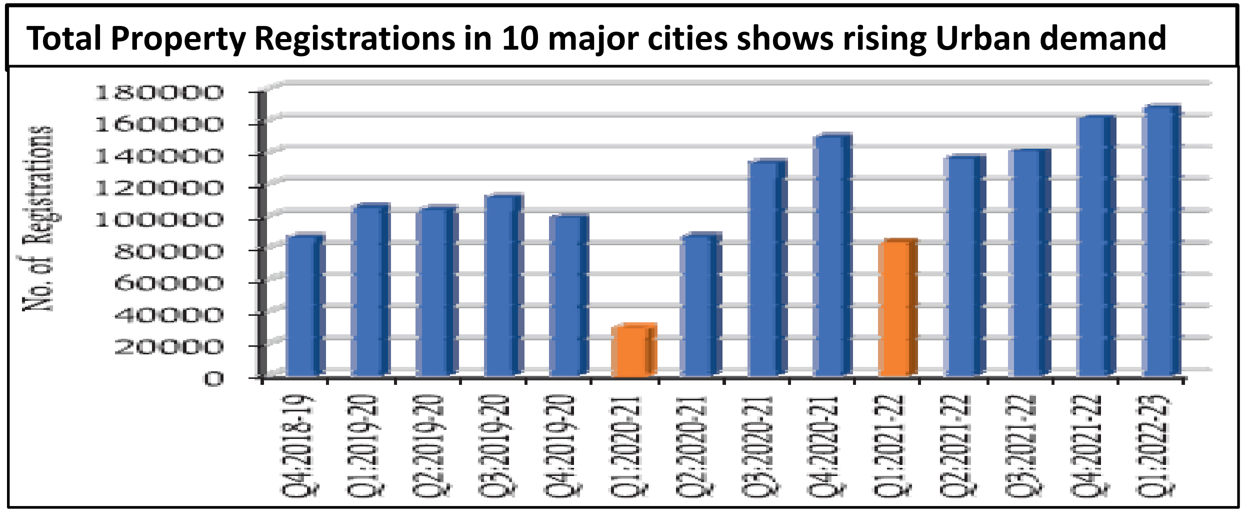


…led by strong Urban demand



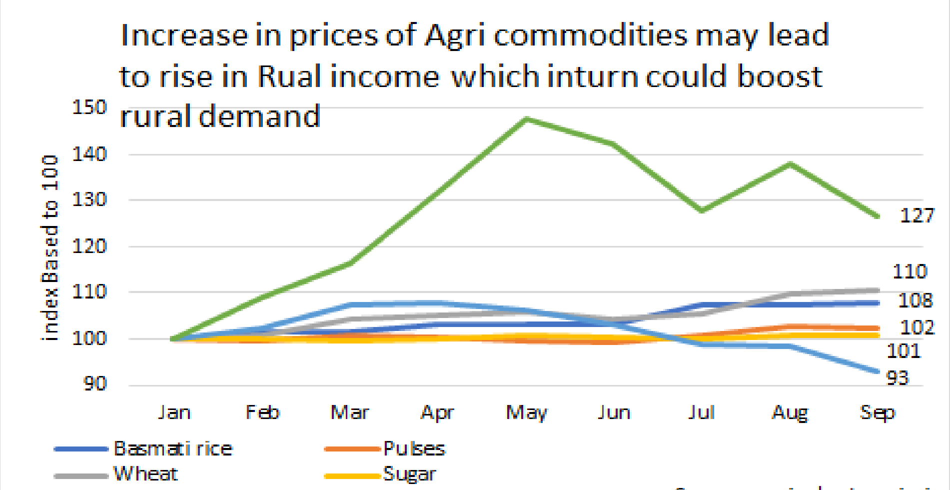






Source: Registration authorities of State govt and RBI Staff Estimate

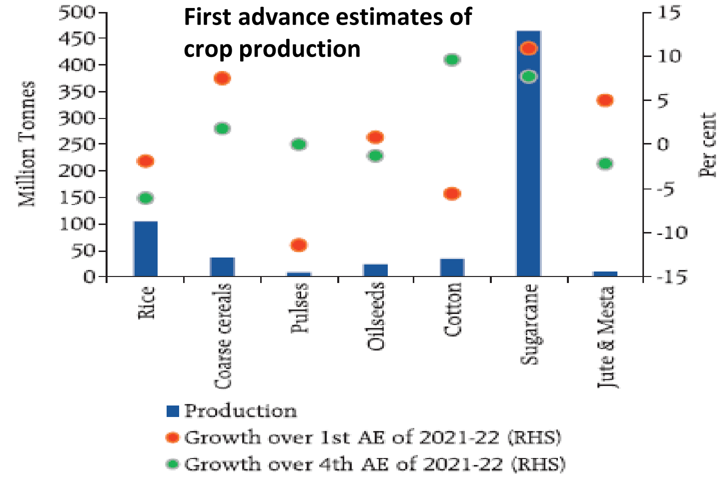
Rural India is seeing signs of improvement with high crop prices, rising MSP and lower MGNREGA demand…. Low acreage in some crops could lead to better realisation going forward.



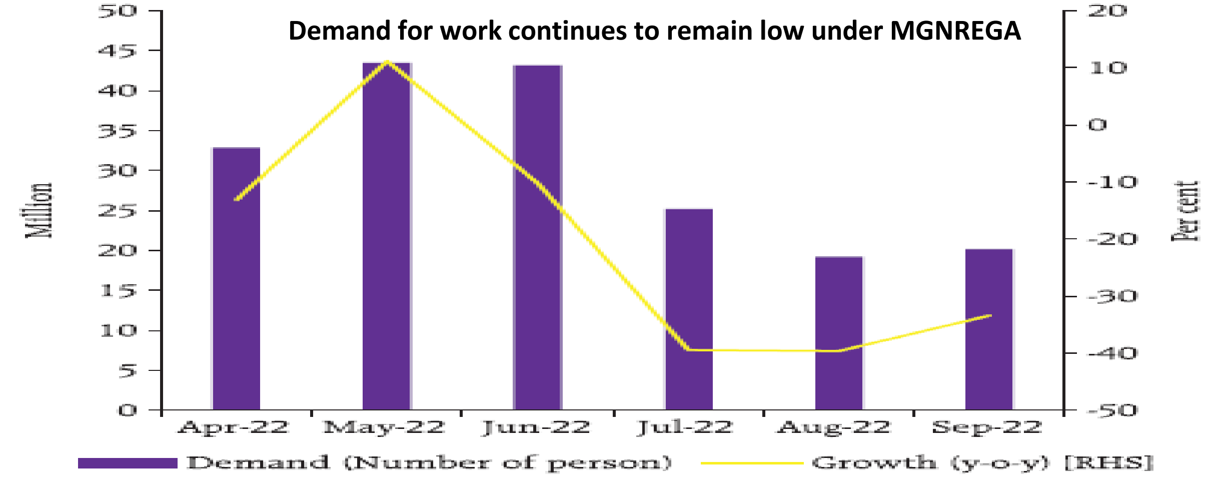
Source: eaindustry.nic.in

Crops	MSP RMS 2022-23	MSP RMS 2023-24	% Change
Wheat	2015	2125	5.46%
Barley	1635	1735	6.12%
Gram	5230	5335	2.01%
Lentil (Masur)	5500	6000	9.09%
Rapeseed & Mustard	5050	5450	7.92%
Safflower	5441	5650	3.84%

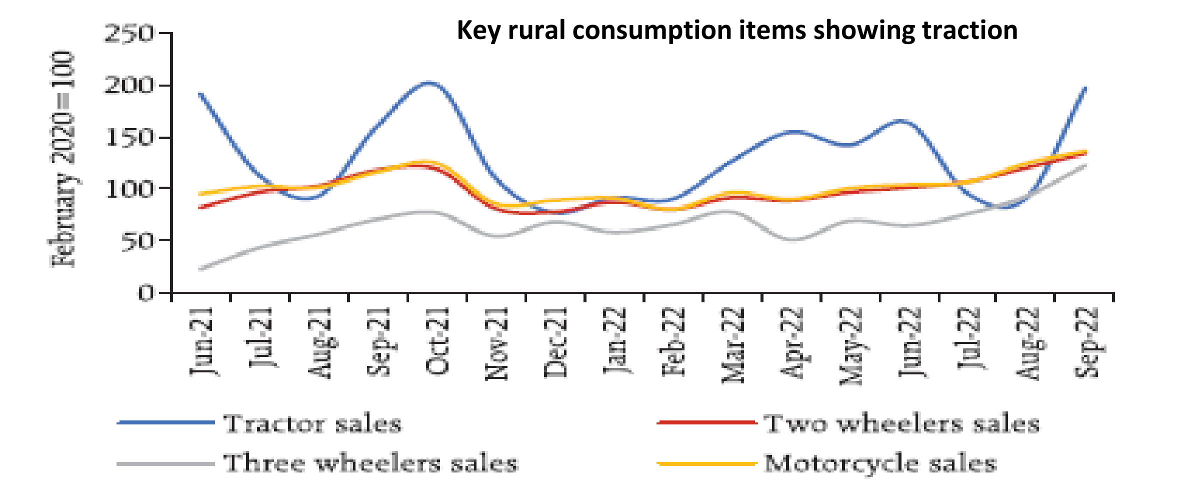
Source: Govt of India



Source: Ministry of Agriculture and Farmers' Welfare (MOAFW).



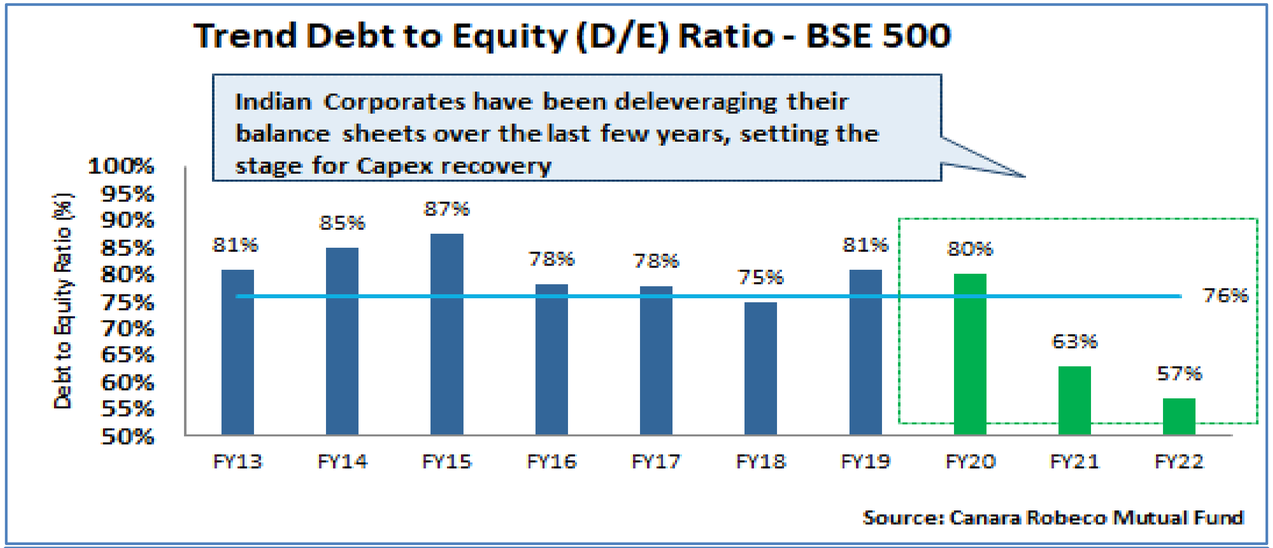
Sources: Government of India; and RBI staff estimates.

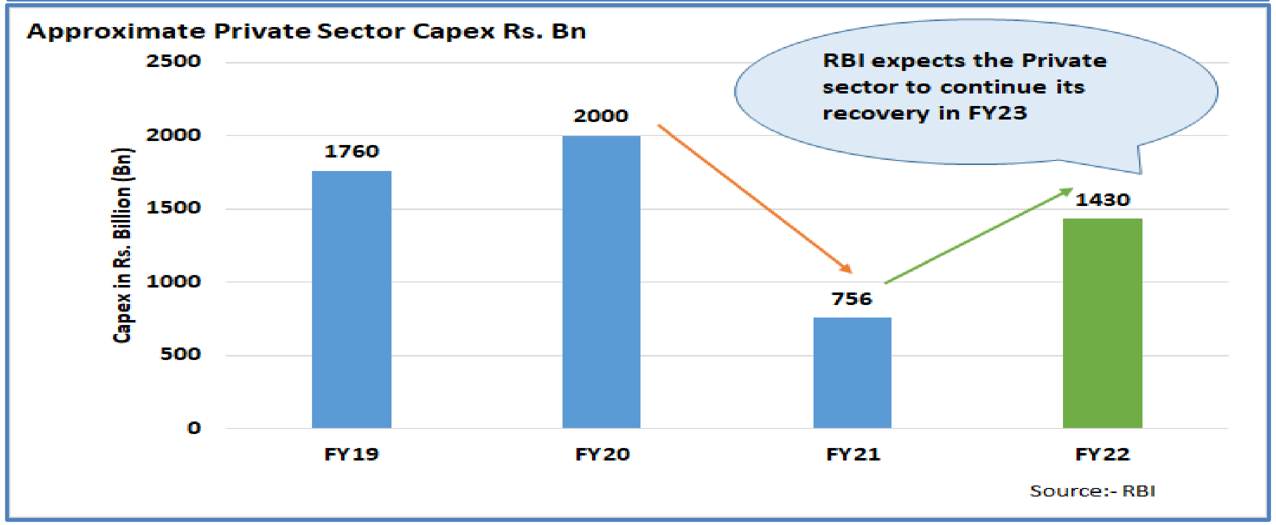


Source: SIAM,TMA & RBI STAFF ESTIMATES

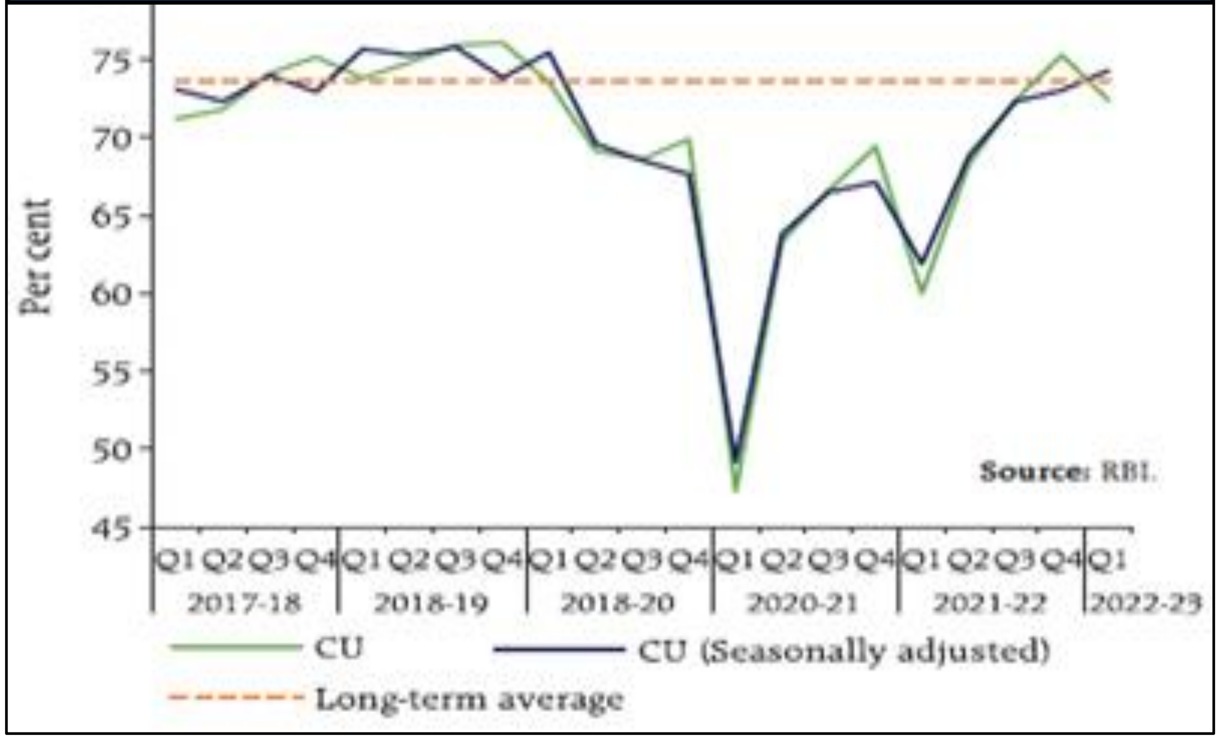
Classification - Restricted

Strong corporate and Banks Balance Sheets and rising capacity utilisation creating condition for revival in private capex…





Capacity utilisation in the manufacturing sector is now above its long-term average, indicating the need for fresh investments for additional capacity creation



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Q2FY23 earnings season started on mixed note… Topline growth remained steady but margin impact has led to weak profitability

YoY growth in %	Net sales			EBITDA			Rep PAT		
	Q2FY23	Q1FY23	Q2FY22	Q2FY23	Q1FY23	Q2FY22	Q2FY23	Q1FY23	Q2FY22
Cyclicals									
Auto & Auto Anc	38.9	37.6	11.9	100.3	65.3	(29.5)	51.7	33.7	(3.3)
BFSI	17.3	12.7	6.4	44.3	41.1	(6.4)	46.8	58.6	15.3
Capital Goods	17.2	65.1	32.8	(5.9)	106.4	17.3	(4.1)	127.3	17.3
Cement & Products	12.8	21.9	10.2	(53.0)	(22.6)	1.6	(71.8)	(27.3)	7.0
Metal & Mining	25.8	34.9	50.9	(42.3)	(16.1)	73.2	(69.9)	(27.5)	186.7
Oil & Gas	46.2	73.7	55.8	(7.4)	24.9	27.7	(32.1)	2.9	29.1
Power	36.8	45.4	16.8	19.5	15.3	4.7	6.1	31.5	7.4
Realty	(10.9)	65.4	16.1	(10.1)	74.1	50.2	17.4	133.5	95.7
Others	(13.8)	8.0	55.6	(16.9)	8.2	71.4	(8.0)	11.3	74.6
Growth & Defensive or Non-Cyclical									
Chem & Fertilizers	38.6	32.9	14.8	75.7	63.5	20.3	122.7	78.8	68.6
FMCG & Retail	20.4	37.7	18.8	16.6	35.5	12.3	25.7	36.0	10.3
Healthcare	11.1	4.8	14.8	22.6	5.9	10.3	6.3	52.1	15.8
IT	19.8	19.3	19.2	9.7	4.2	16.5	7.4	1.9	18.8
Telecom	12.2	2.8	79.2	(16.7)	(25.8)	135.4	(29.5)	(40.9)	77.4
Ecomm	31.9	23.7	11.8	(30.8)	(34.3)	(0.1)	(16.8)	(46.9)	17.8
NIfty 200 Index									
Grand Total	**29.1**	**38.8**	**26.9**	**13.1**	**21.1**	**11.6**	**1.7**	**17.5**	**27.6**
Ex BFSI	**33.2**	**47.8**	**35.8**	**(4.5)**	**9.3**	**25.2**	**(16.7)**	**2.7**	**33.4**

Source: Capitaline

Data as of 30 October 2022

- Q2FY23 results have seen stable topline growth, but margins pressure in many sectors has been seen impacting the profit growth.
- Earnings expectations could see too could also see marginal downgrades post the result season. Key alpha sectors seem to be Banking, Auto, Infra, while Pharma seems to be emerging out of its slumber.
- So far 84 companies in Nifty 200 index have reported their quarterly earnings as of 30 October 2022, and the net sales for these companies grew by 29.1% YoY, EBITDA grew by 13.1% YoY and PAT grew by 1.7% YoY in Q2FY23.
- On the margin front, key user industries like Cement, IT, Power and Metals & Mining witnessed moderation due to sharp rise in raw material and wage costs during the quarter.

- **Going forward, strong corporate balance sheets, high household savings and government's focus on infrastructure development and job creation is likely to drive capex demand and thereby push incremental consumption demand as well in medium term, which would be positive for corporate earnings.**

Consensus views of Fund Managers on Key Sectors

Banking & Financial Services

- Positive on large private sector banks, insurance companies and select large NBFCs/HFCs.
- Expect strong credit growth to continue on back of economic recovery
- Steady margins (NIM), corporate asset quality holding up better, Banks are well capitalized, well placed on technology front.
- Issues around Fund raise and some smaller banks with weaker deposit franchise could get impacted negatively
- Reasonable valuations, but rising rates could play spoilsport

Information Technology

- Cautious - Growth and margins both might moderate in few quarters as global growth slows meaningfully.

Consumer Sector

- Cautiously optimistic - Volume growth has shown muted performance, while gains have come due to better pricing gains. Gross margin headwinds have eased.
- Organized players to gain market share as unorganized get hit by elevated inflation.
- Valuations is some pockets are lower relative to their own historical performance.
- Companies having higher urban dependence is expected to perform better. Rural demand continues to remain slow but recent correction in commodities to aid gross margins expansion. FMCG better than Durables.

Auto

- Positive - Positive on select Passenger Vehicle OEMs which have a larger part of the demand coming from urban consumers.
- Demand for vehicles is currently strong and is expected to retain momentum, due to high backlogs. Improvement in supply chain situation, volume improvement in PV segment suggests strong growth. Decline in commodity prices likely to help margins.

Classification - Restricted

....Contd

Pharma

- Neutral to Positive - US generics market experiencing higher than expected price erosion due to inventory liquidation by large players, that seems to have been priced in by the stocks.
- Normalisation of production expected in next few months.
- Domestic oriented business momentum continues to be strong. Domestic focused companies could generate Alpha.

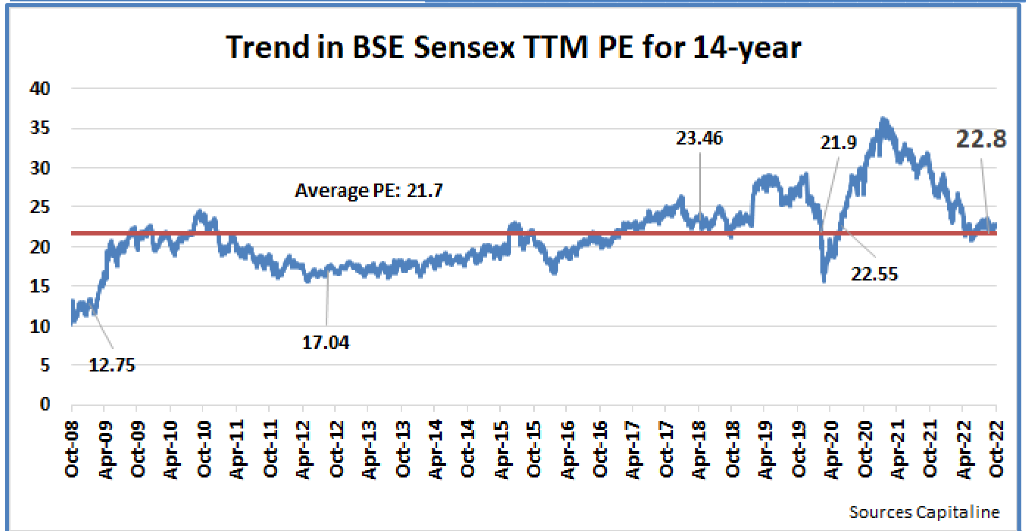
Housing & Construction

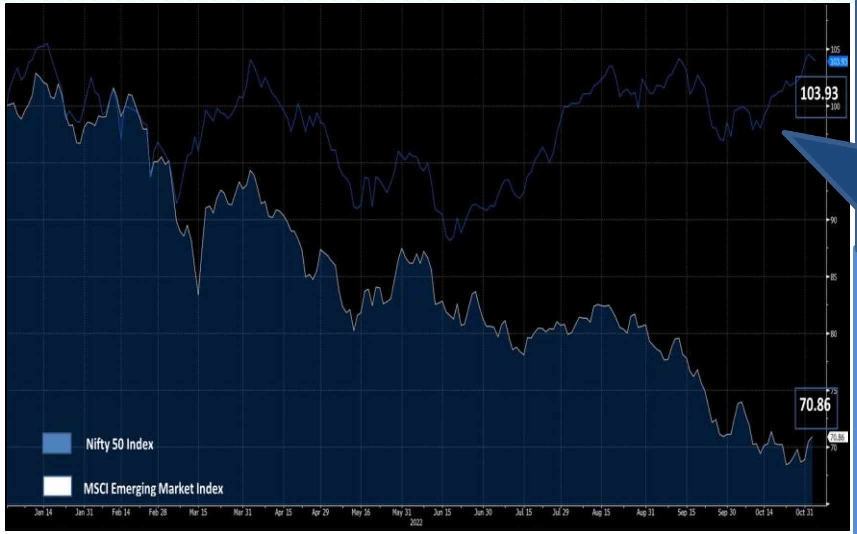
- Positive - Higher household savings have increased the affordability for Housing sector.
- Focus on Infrastructure is clearly visible with government accelerating spending at the cost of fiscal deficit. Risk-reward is still highly favourable and medium-term outlook remains positive.
- Volatility in raw material cost could impact profitability.
- Sector is coming out of long period of consolidation

Metals

- Cautious- Due to High cyclicality and global risks.
- Uncertainty over volatility in raw material cost, including thermal and coking coal and iron ore, leading to earnings volatility.
- Possibility of demand slowdown due to widespread global inflation is a major concern for metals sector. Commodity cycle has largely played out - Prices likely to correct further as global growth moderates

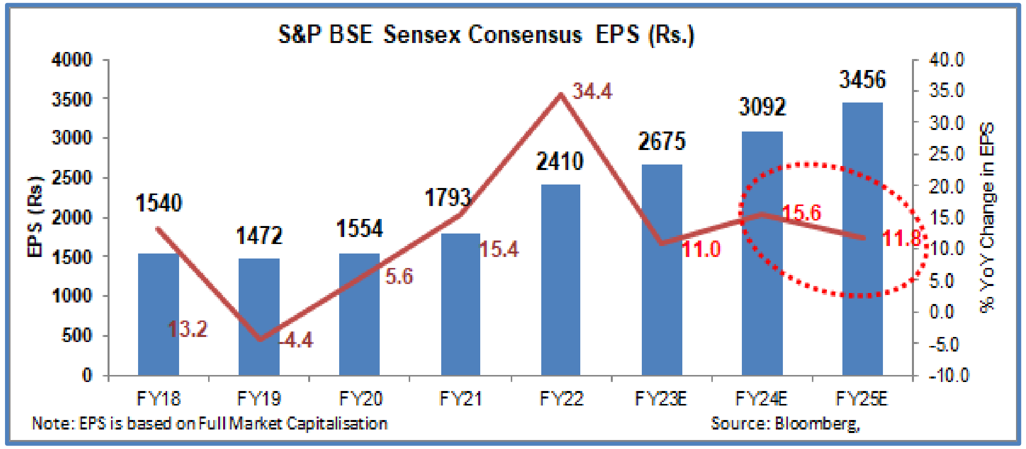
While India's GDP growth / Earnings estimates have been downgraded, any uptick in growth trajectory could support equity market performance…

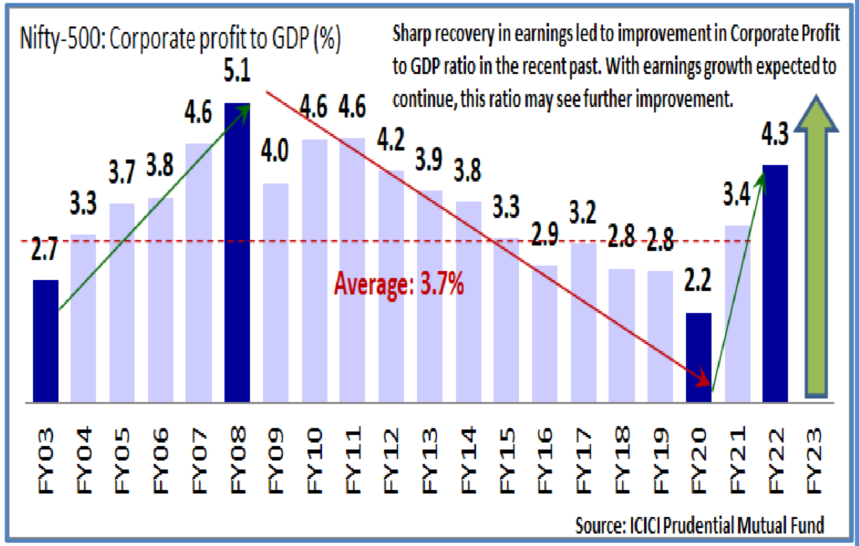




India has outperformed the EMs substantially since last 10 months, given the strong economic growth outlook, despite the recent downgrades, as the other key EMs have seen sharper weakness. To maintain this outperformance, the Indian earnings growth trajectory needs to start shifting upwards.

Going forward, Incremental earnings growth momentum is likely to see slowdown on back liquidity tightening



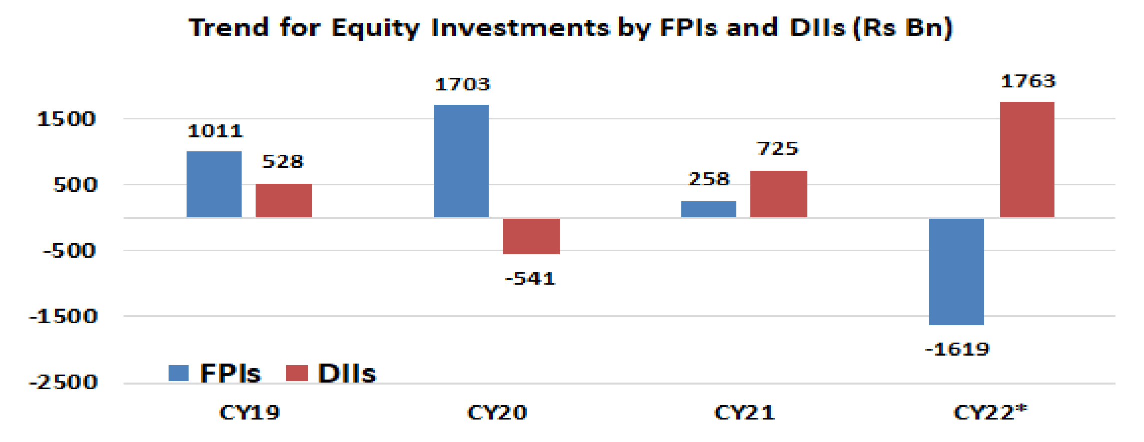


- S&P BSE Sensex is trading at 22.7x of FY23E Bloomberg consensus EPS of Rs.2675.
- India's monetary policy tightening continues its focus to ensure that inflation returns to the target while supporting growth. That, along with the weak global outlook is likely to impart considerable volatility to the market in the near to medium term.
- Our long term view on Indian markets remain positive on the back of strong monsoon, rise in capacity utilisation and credit growth, government's capex push, strong corporate and bank balance sheets and buoyant consumer and business confidence and superior demographics. Hence, any sharp dips in markets could be used as buying opportunities by investors with a 2-3 year's investment horizon.
- Investors could have larger focus at Large Cap, Value and Hybrid Equity funds in line with their risk profile and product suitability.

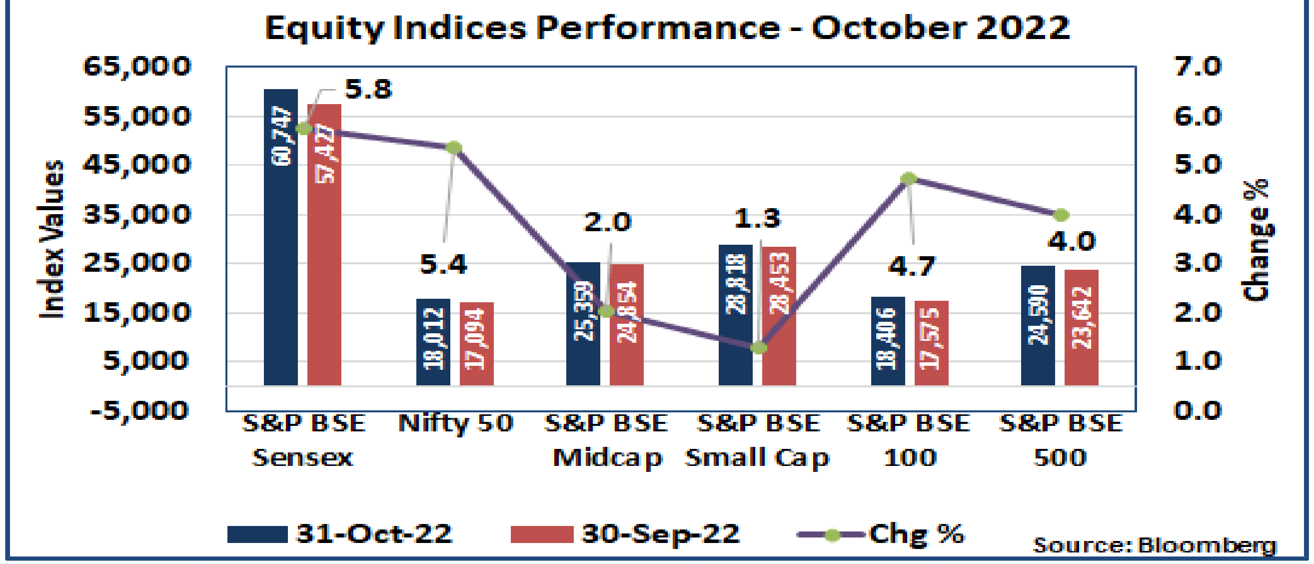
Classification - Restricted

Market Round up – October 2022

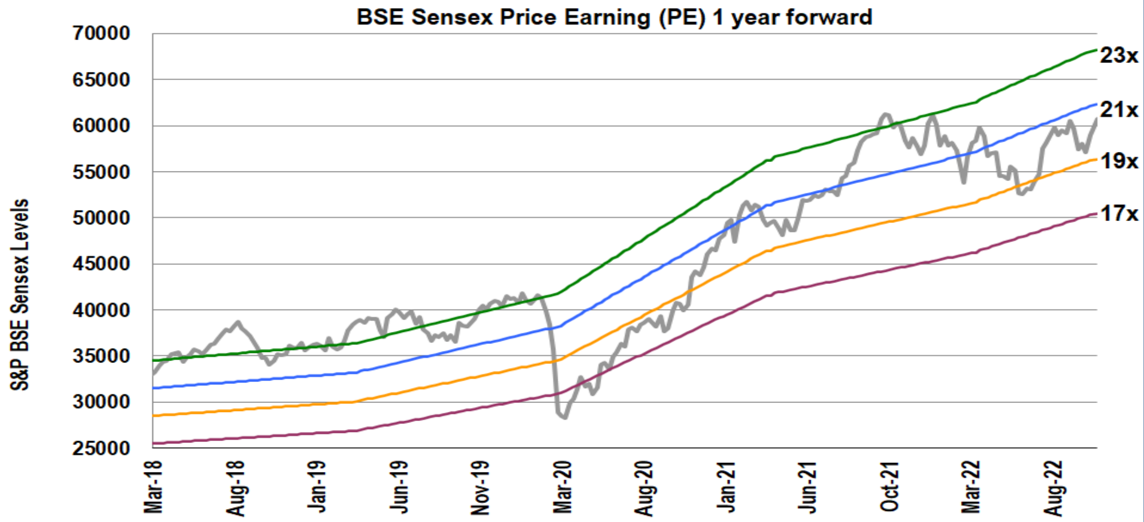
- Indian equity markets were steady and ended on a positive note during the month of October 2022, as S&P BSE Sensex index and Nifty 50 index closed up by 5.8% MoM and 5.4% MoM, respectively.
- The S&P BSE Midcap index and S&P BSE Smallcap index closed up by 2.0% MoM and 1.3% MoM, respectively.
- On the sectoral indices front, S&P BSE Bankex index and S&P BSE Capital Goods index, were top two outperformers with a gain of 7.3% MoM and 6.6% MoM, respectively. The S&P BSE Consumer Durable index moved up by 0.4% MoM whereas, S&P BSE FMCG index declined marginally by 0.3% MoM, were the top two underperformers.
- During the month of October 2022, Foreign Portfolio Investors (FPIs) were net buyers to the tune of ~Rs 84 bn and Domestic Institutional Investors (DIIs) were net buyers to the tune of ~Rs.63 bn (as of 30 October 2022).



Source: SEBI, NSDL (*DIIs data as of 17 Oct'22)



Source: Bloomberg



Source: Bloomberg

Key concerns to watch out ….

Global factors

- **Ongoing conflict between Russia and Ukraine may have adverse impact on global trade and economic growth**
- **Rise in volatility in commodity prices (especially Energy prices)** could put pressure on the global financial markets
- **Sharp volatility in the US Bond yields** may lead to rise in risk off sentiments
- **Sharp appreciation in US dollar index, which may lead to FPI outflow from EMs**
- **Acceleration in the pace of unwinding of liquidity at global level**
- **Rising trend of protectionism across economies** could pose a risk to overall global growth
- **Rise in global food prices** may lead to further rise in food inflation.

Domestic factors

- **Higher crude oil prices** could put pressure on India's current account balance
- If **Rupee depreciates disorderly**, then it may impact India's twin deficit
- **High Inflationary pressure** may push the RBI to act faster on interest rates.
- **Any delay in implementation of key reforms** may delay the structural recovery in growth
- Any **negative credit rating action** by global rating agencies could impact interest rates and currency.

Classification - Restricted

Annexure

Classification - Restricted

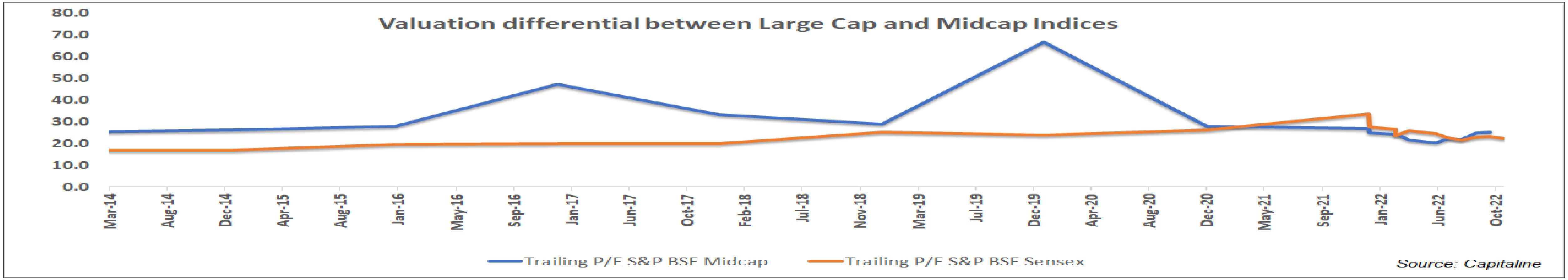
Sectoral rotation has been the trend in last one year…. Sectors like Banking, Auto and Infra seems to be generating alpha in the near term.

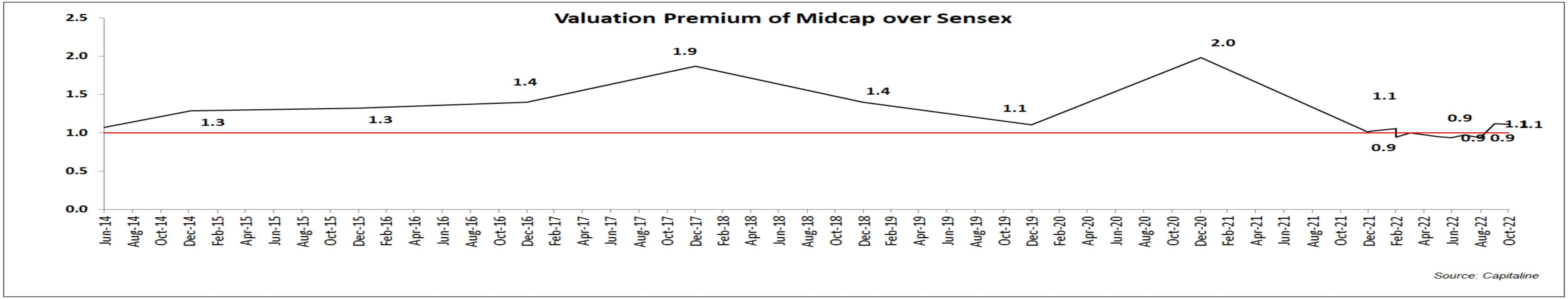
MoM changes	Sep-21	Oct-21	Nov-21	Dec-21	Jan-22	Feb-22	Mar-22	Apr-22	May-22	Jun-22	Jul-22	Aug-22	Sep-22	Oct-22
Nifty Metal	-1.8%	-0.9%	-6.5%	6.2%	-0.9%	7.7%	8.9%	-1.5%	-15.7%	-12.6%	17.7%	8.2%	-2.8%	2.2%
BSE Power	9.5%	4.3%	3.6%	0.7%	13.1%	-2.1%	4.9%	18.1%	-11.5%	-3.8%	12.0%	14.7%	-9.2%	2.5%
Nifty IT	1.3%	-1.8%	1.8%	10.4%	-10.0%	-2.8%	7.3%	-12.9%	-6.1%	-6.2%	4.7%	-2.6%	-5.0%	-0.9%
Nifty Realty	32.8%	-2.9%	-2.2%	-0.7%	-0.8%	-9.1%	6.2%	-4.3%	-7.2%	-6.4%	17.0%	2.7%	-8.5%	3.5%
BSE Cons Durable	10.7%	4.5%	-0.3%	3.9%	-6.4%	2.8%	-1.9%	0.9%	-10.9%	-8.7%	14.0%	7.9%	-0.5%	0.4%
BSE Telecom	10.6%	-2.6%	6.7%	-0.8%	0.4%	-7.7%	9.5%	-4.3%	-7.1%	-4.3%	4.1%	5.6%	1.4%	2.2%
Nifty Infra	6.7%	0.4%	-1.7%	-0.2%	2.2%	-5.1%	4.6%	2.2%	-4.9%	-5.3%	5.9%	4.8%	-3.3%	5.6%
Nifty Media	33.5%	5.0%	-3.3%	2.2%	0.7%	-10.1%	18.3%	-9.7%	-4.5%	-7.6%	9.6%	-0.5%	-0.3%	0.0%
BSE Oil & Gas	7.1%	-0.9%	-3.5%	0.0%	6.6%	-7.3%	8.2%	4.0%	-4.6%	-3.1%	5.4%	6.8%	-8.5%	5.0%
Nifty 50	2.8%	0.3%	-3.9%	2.2%	-0.1%	-3.1%	4.0%	-2.1%	-3.0%	-4.8%	8.7%	3.5%	-3.7%	5.4%
BSE Sensex	2.7%	0.3%	-3.8%	2.1%	-0.4%	-3.0%	4.1%	-2.6%	-2.6%	-4.6%	8.6%	3.4%	-3.5%	5.8%
Nifty Auto	5.6%	6.6%	-6.1%	3.1%	7.0%	-7.5%	-2.5%	5.0%	4.6%	1.0%	7.2%	5.4%	-3.9%	5.4%
Nifty Finan Sev	1.3%	2.7%	-6.7%	-1.2%	2.9%	-5.0%	1.2%	-3.0%	-1.0%	-6.1%	12.7%	4.6%	-4.0%	5.9%
Nifty Bank	2.7%	4.5%	-8.7%	-0.6%	7.0%	-4.7%	0.5%	-0.8%	-1.7%	-5.8%	12.2%	5.5%	-2.3%	6.9%
Nifty Pharma	0.8%	-4.1%	-1.6%	4.1%	-7.3%	-1.9%	5.1%	-0.9%	-6.4%	-3.5%	5.1%	-0.6%	2.1%	1.9%
NIFTY FMCG	2.3%	-5.5%	-2.2%	0.5%	-3.0%	-2.6%	2.2%	5.3%	1.3%	-2.7%	12.8%	3.1%	1.3%	-0.2%

Source: ACEMF

Largecap vs Midcap

Valuation gap between large cap and mid cap have now started expanding… high inflationary condition could lead to increase in pressure in mid and small cap companies leading to reversion in valuation gap…..

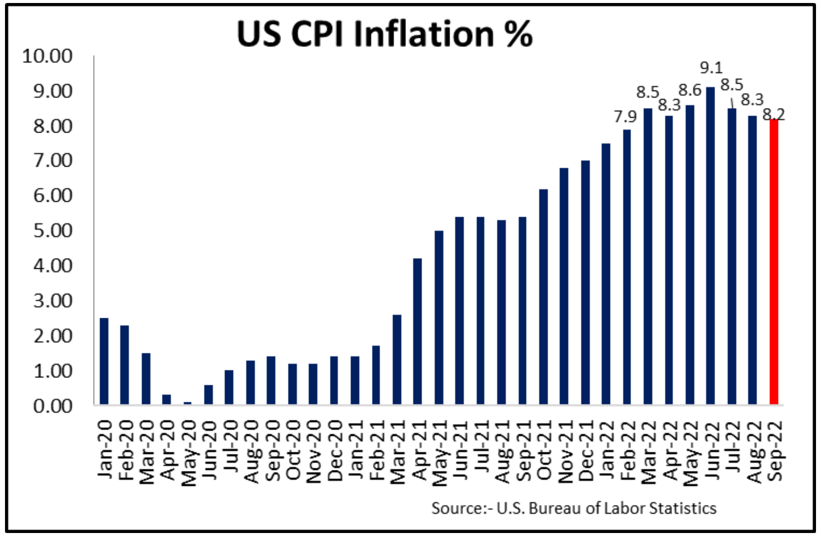


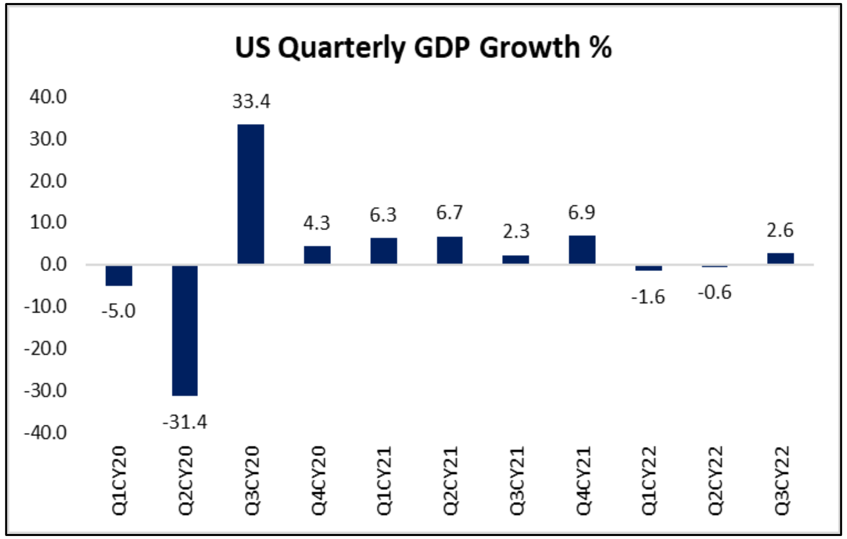


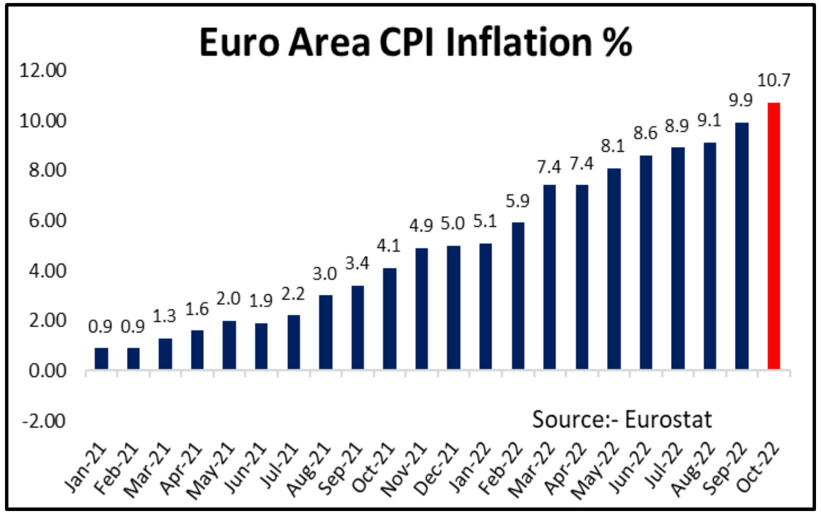
Fixed Income Markets

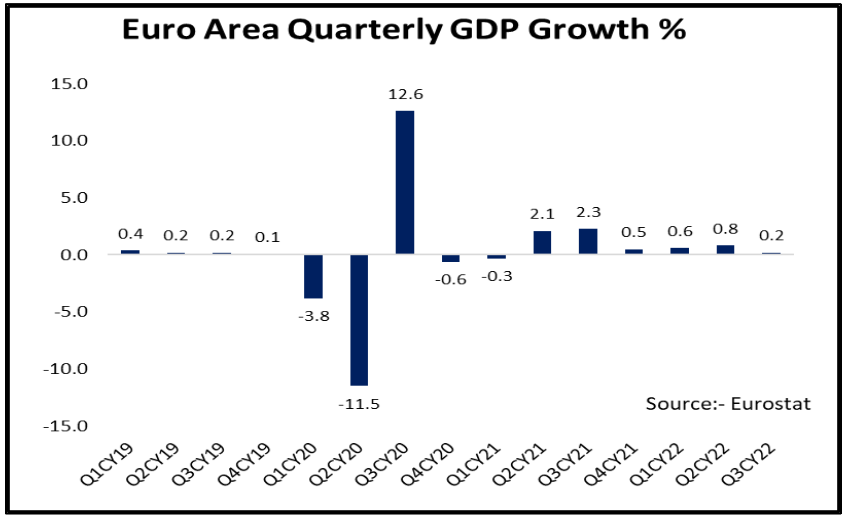
Classification - Restricted

High Inflation – Low Growth : The World is starting to be divided between controlling Inflation and Driving Economic Growth…





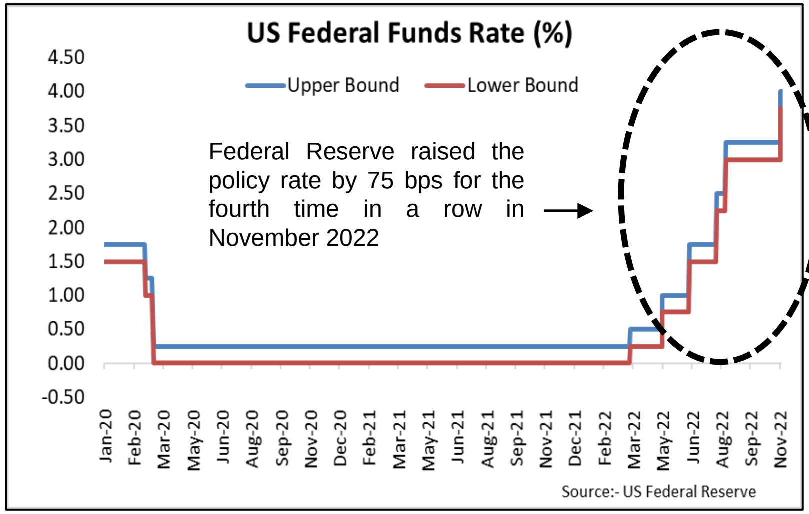


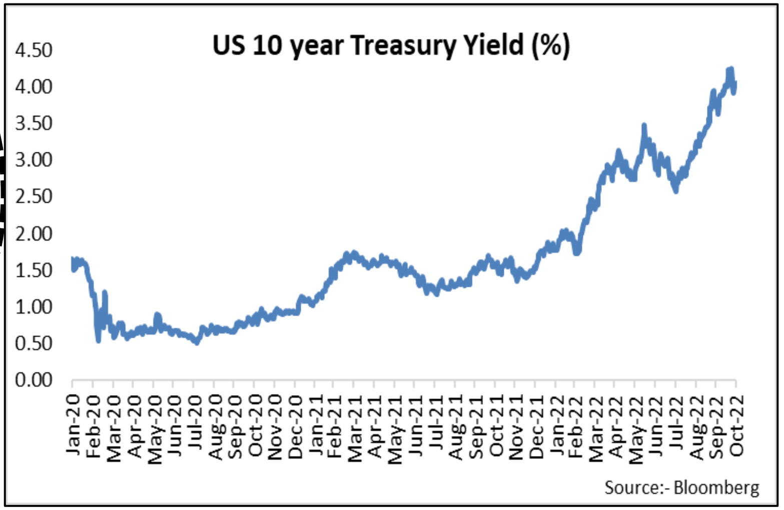


IMF - Overview of the World Economic Outlook Projections	Projections in October		Difference from July Estimates	
	2022	2023	2022	2023
World Output	**3.2**	**2.7**	**0.0**	**-0.2**
Advanced Economies	2.4	1.1	-0.1	-0.3
United States	1.6	1	-0.7	0.0
Euro Area	3.1	0.5	0.5	-0.7
Germany	1.5	-0.3	0.3	-1.1
France	2.5	0.7	0.2	-0.3
Italy	3.2	-0.2	0.2	-0.9
Spain	4.3	1.2	0.3	-0.8
Japan	1.7	1.6	0	-0.1
United Kingdom	3.6	0.3	0.4	-0.2
Canada	3.3	1.5	-0.1	-0.3
Other Advanced Economies	2.8	2.3	-0.1	-0.4
Emerging Market and Developing Economies	3.7	3.7	0.1	-0.2
Emerging and Developing Asia	4.4	4.9	-0.2	-0.1
China	3.2	4.4	-0.1	-0.2
India[4]	6.8	6.1	-0.6	0.0
ASEAN-5	5.3	4.9	0.0	-0.2
Emerging and Developing Europe	0	0.6	1.4	-0.3
Russia	3.4	-2.3	2.6	1.2
Latin America and the Caribbean	3.5	1.7	0.5	-0.3
Brazil	2.8	1.0	1.1	-0.1
Mexico	2.1	1.2	-0.3	0.0
Middle East and Central Asia	5	3.6	0.2	0.1
Saudi Arabia	7.6	3.7	0.0	0
Sub-Saharan Africa	3.6	3.7	-0.2	-0.3
Nigeria	3.2	3	-0.2	-0.2
South Africa	2.1	1.1	-0.2	-0.3

Source:- International Monetary Fund – IMF

Monetary Policy Tightening continued with inflation rates surging to multi-decade highs…



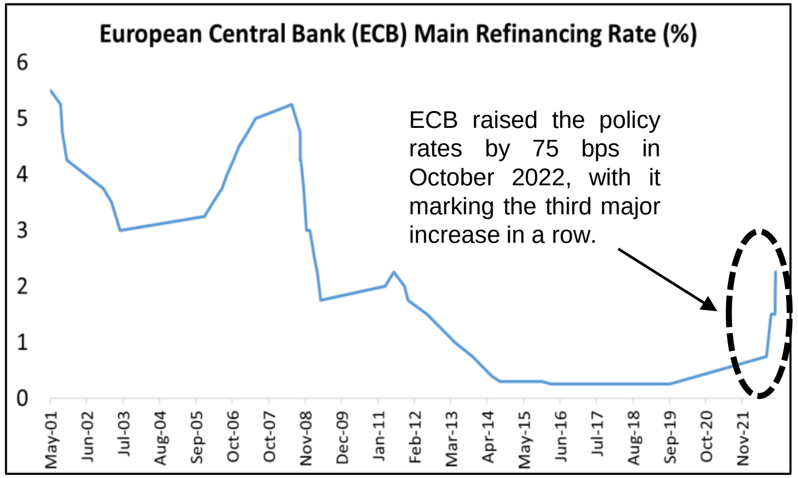


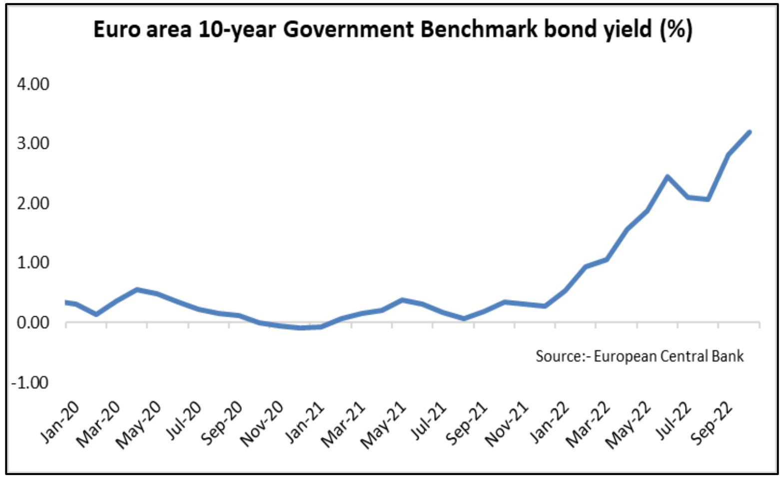
US FOMC Comments

"The Committee anticipates that ongoing increases in the target range will be appropriate in order to attain a stance of monetary policy that is sufficiently restrictive to return inflation to 2% over time. In determining the pace of future increases in the target range, the Committee will take into account the cumulative tightening of monetary policy, the lags with which monetary policy affects economic activity and inflation, and economic and financial developments.

European Central Bank (ECB) Comments

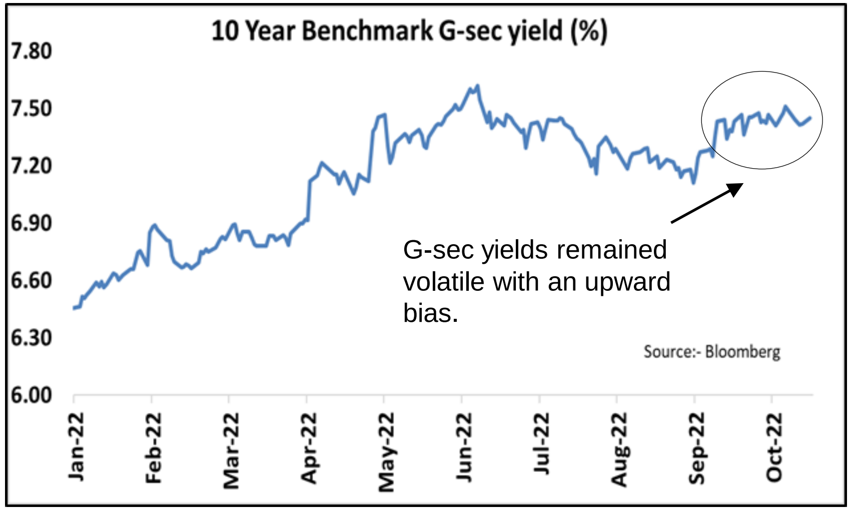
"We expect to raise interest rates further, to ensure the timely return of inflation to our 2% medium-term inflation target. We will base the future policy rate path on the evolving outlook for inflation and the economy, following our meeting-by-meeting approach."

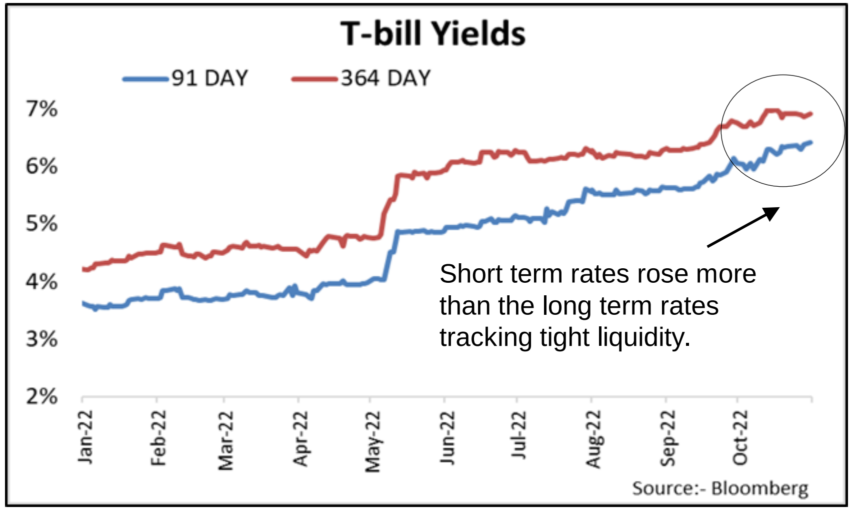


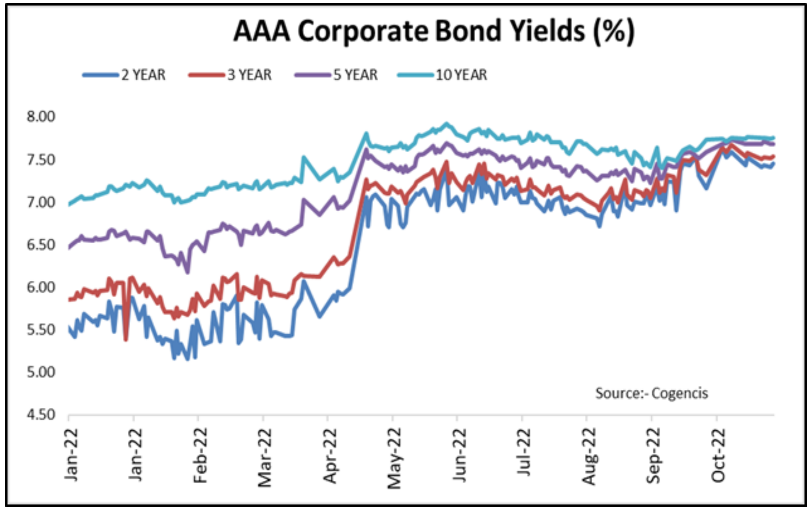


Country	Latest Interest Rate Actions by Central Bank (Bps)
Euro Area	75
United States	75
Saudi Arabia	75
South Korea	50
Canada	50
Indonesia	50
Australia	25

Domestic bond yields remained volatile and traded with an upward bias…



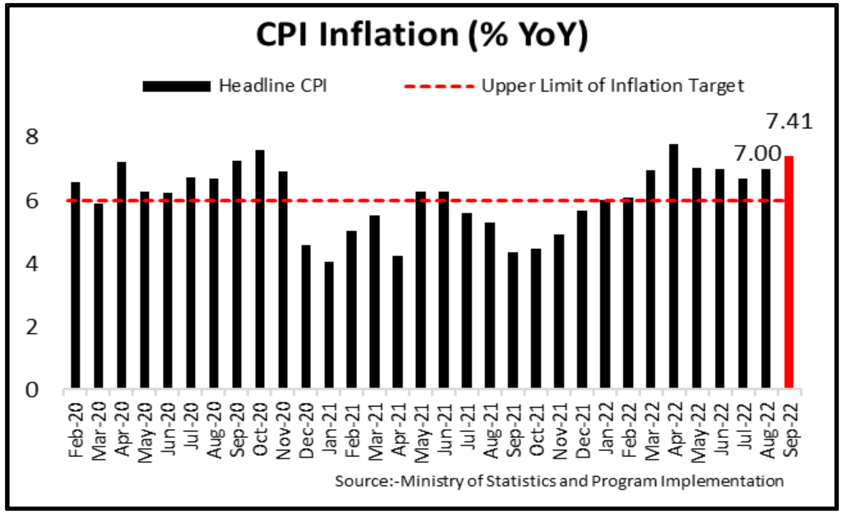


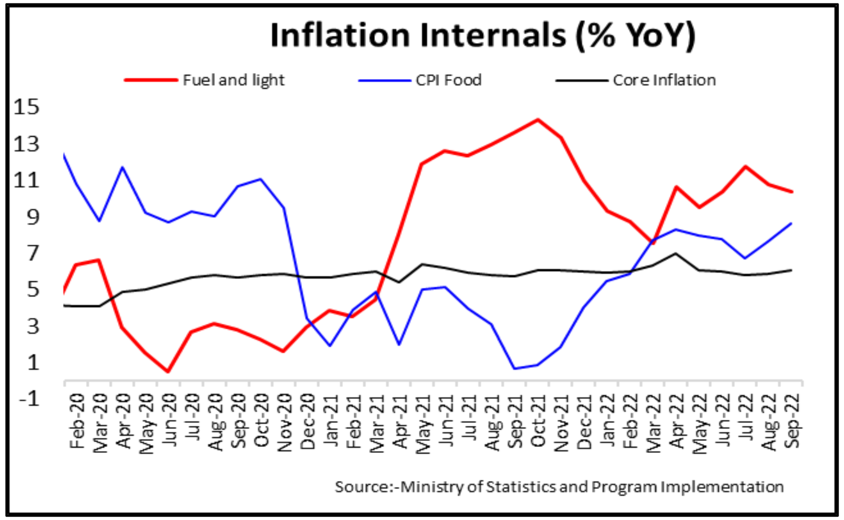


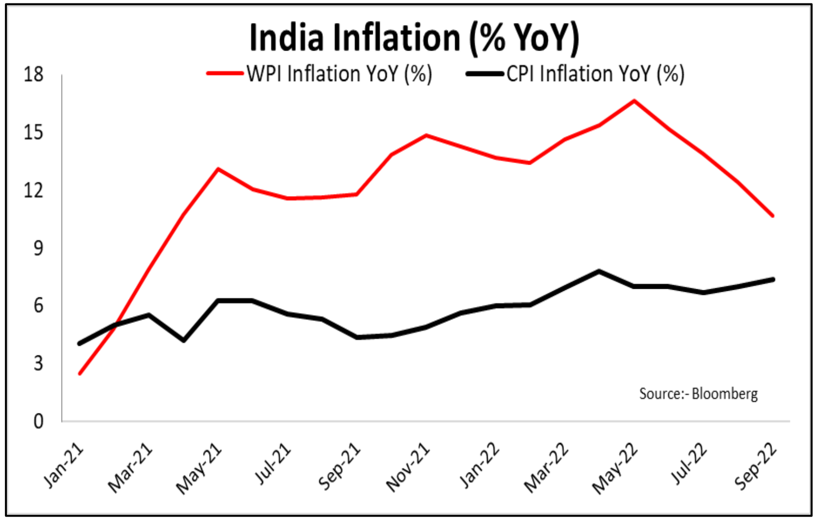
Instruments	31-Oct-22	30-Sep-22	Change in Yields (Bps)
91 Days T-bills	6.42%	6.05%	37
364 Days T-bills	6.91%	6.77%	14
3 Months CD	6.83%	6.20%	63
6 Months CD	7.30%	6.63%	67
1 Year CD	7.65%	7.10%	55
10 Year BenchmarK G-sec	7.45%	7.43%	2
AAA Non PSU Bond Yields			
1 Year	7.63%	7.33%	30
2 Year	7.65%	7.43%	22
3 Year	7.66%	7.48%	18
5 Year	7.68%	7.63%	5
10 Year	7.78%	7.73%	5

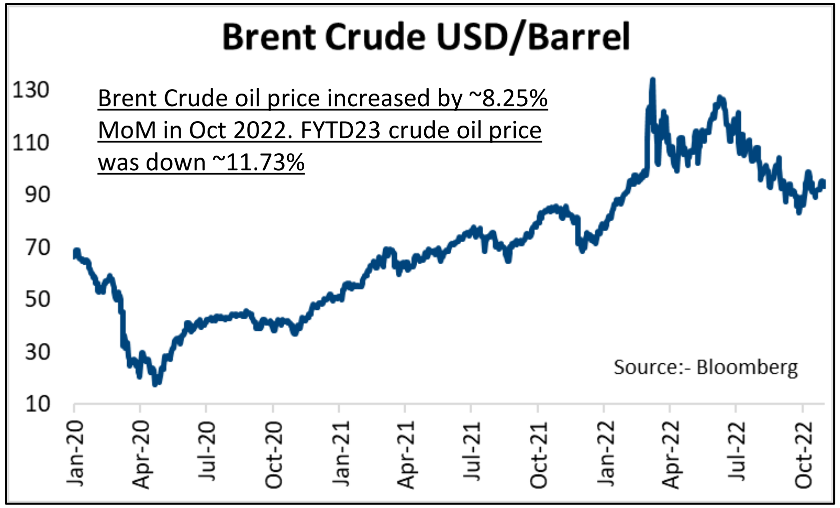
A host of uncertainties regarding the global and domestic economies are likely to keep the bond yields volatile in the near term. The direction of bond yields going forward is likely to be dependent on the monetary policies of central banks and the liquidity conditions.

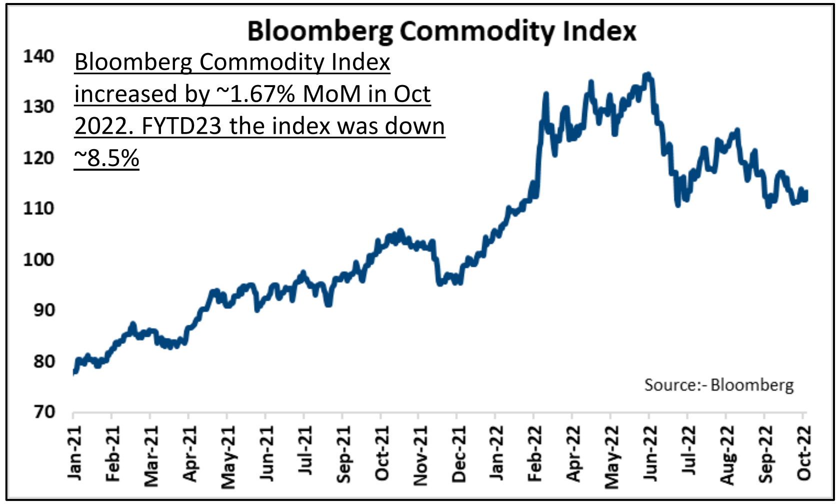
Retail Inflation Continued to Surge in September 2022.. While WPI has started to show some deceleration led by consolidation in commodity prices …

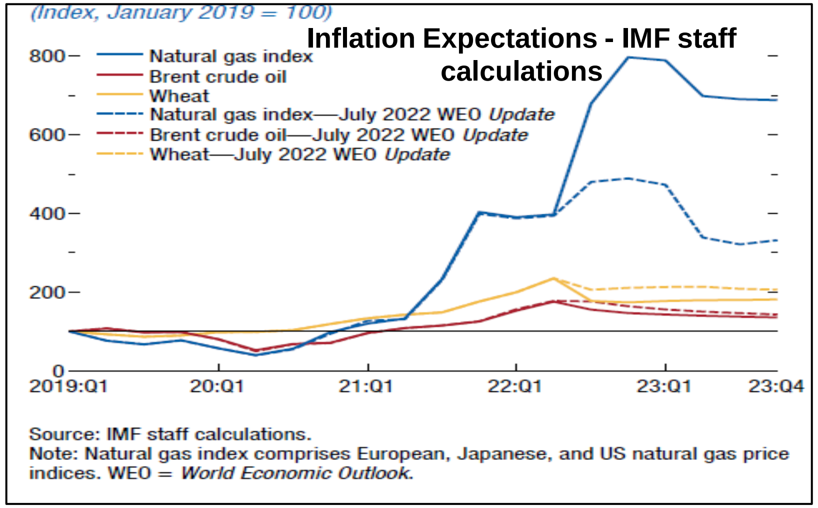




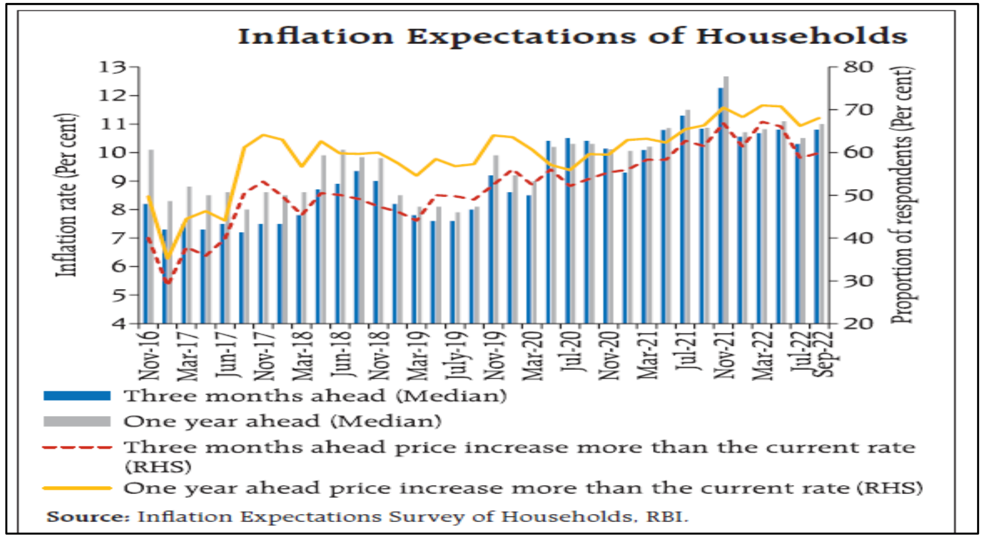


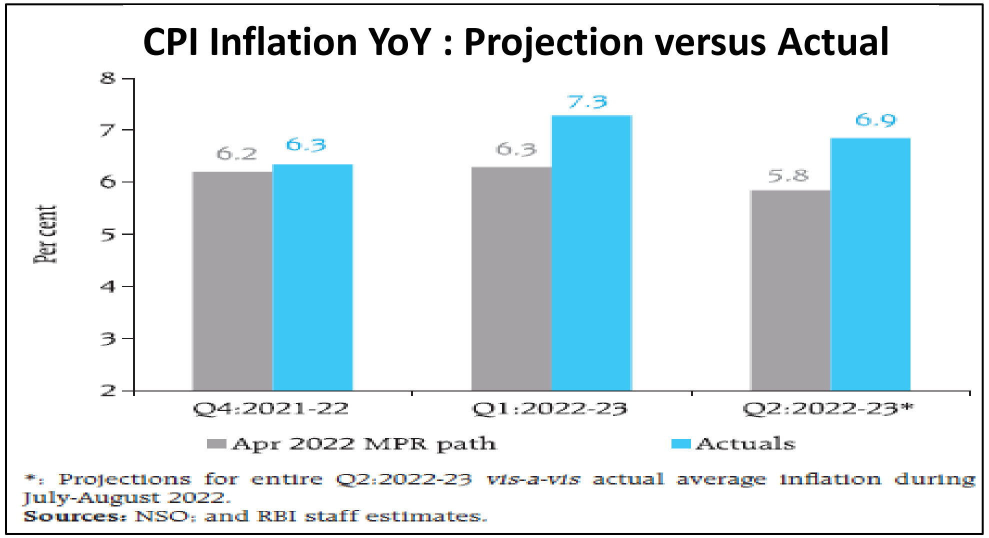


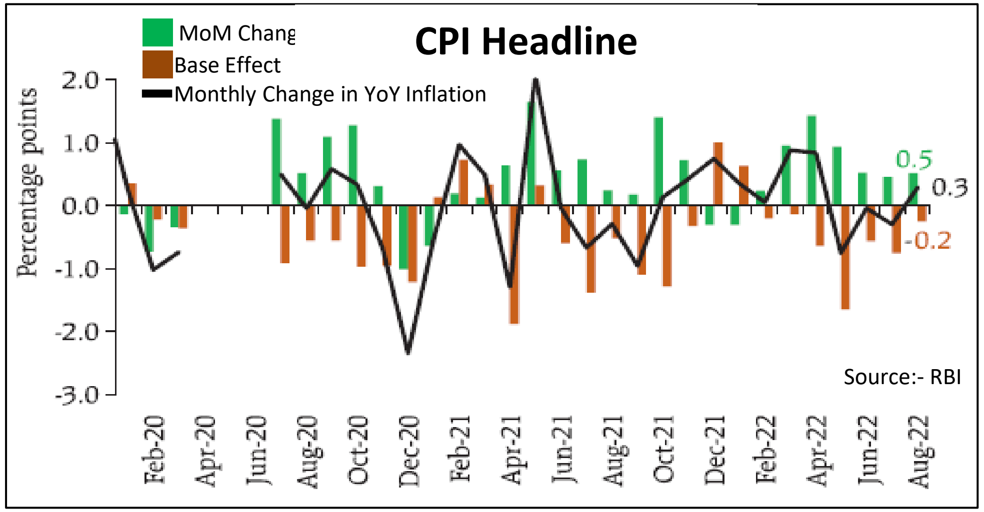


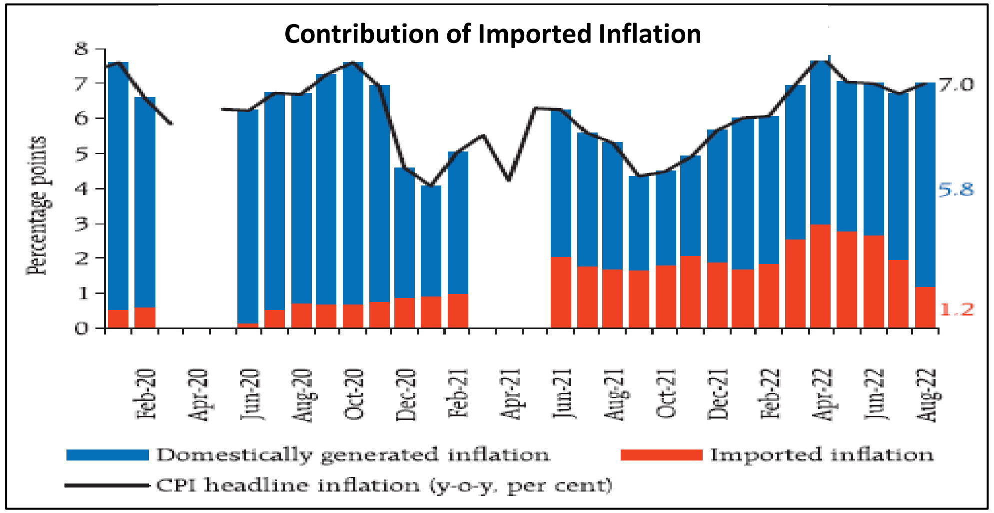


RBI is also likely to remain focused on controlling inflation…



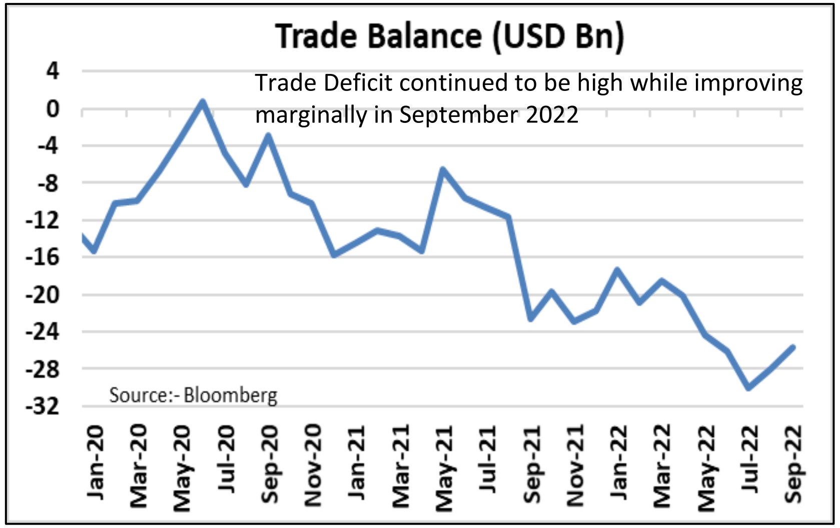


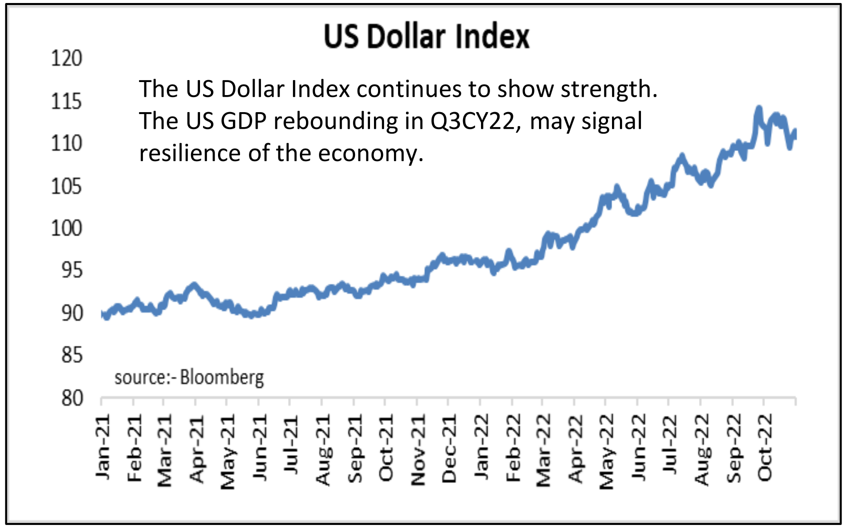


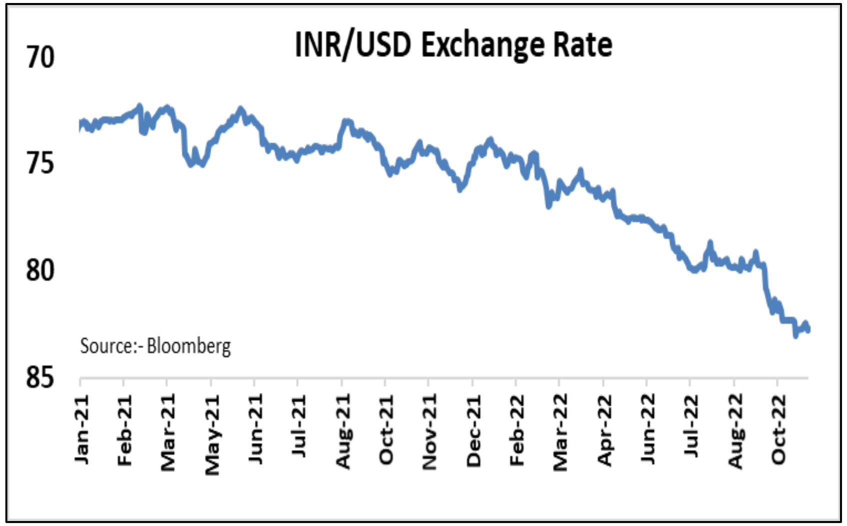


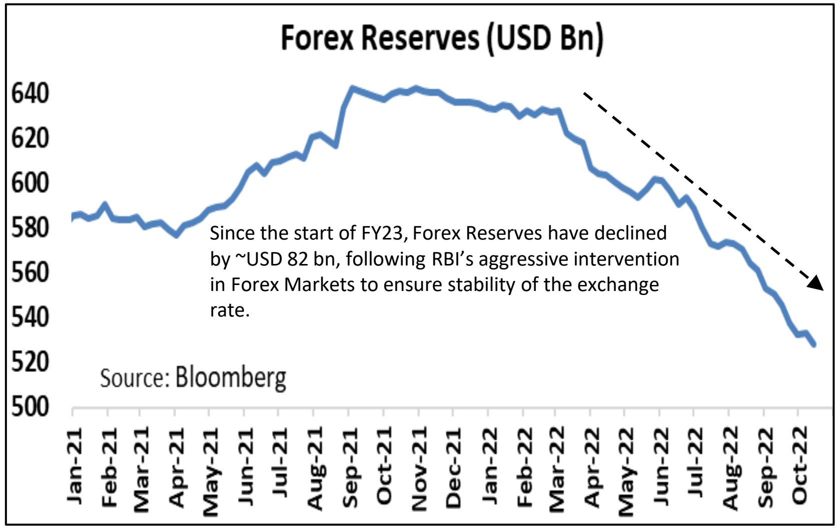
RBI is likely to continue its aggressive fight against inflation, given the elevated inflation exceptions of households, inflation coming in higher than RBI's projections on a sustained basis and risk of imported inflation.

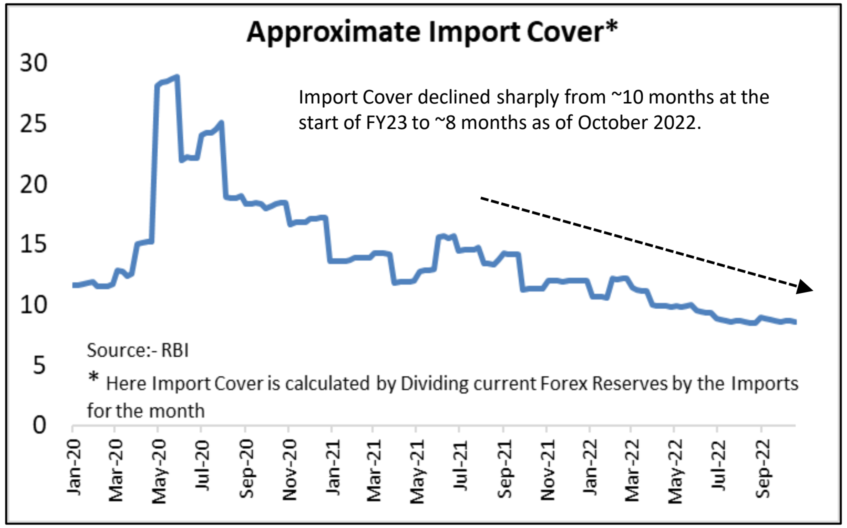
Declining Forex Reserves amidst strengthening US Dollar remains a key monitorable for Bond Markets…





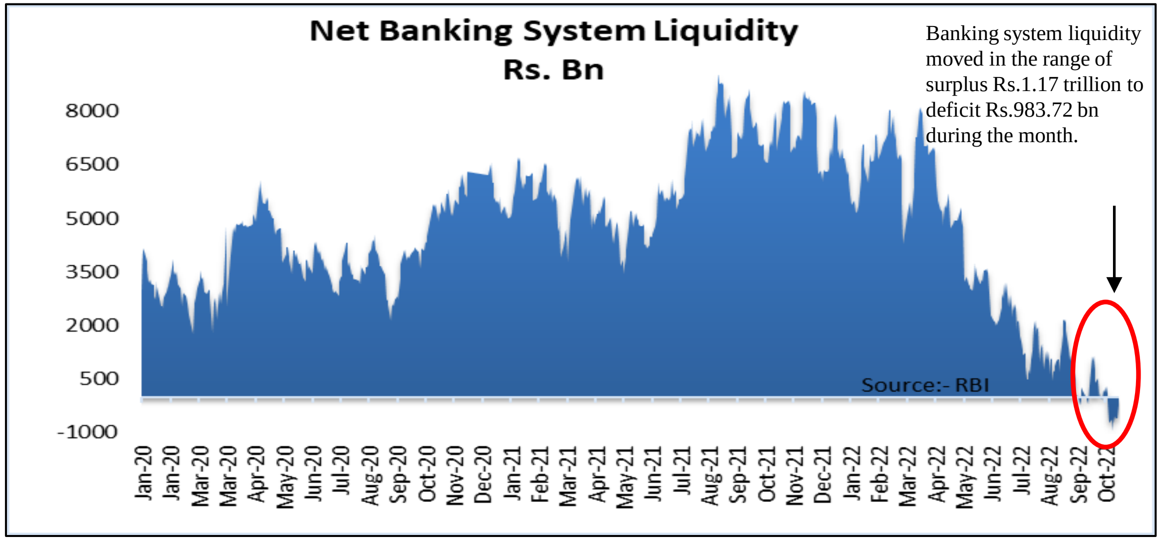


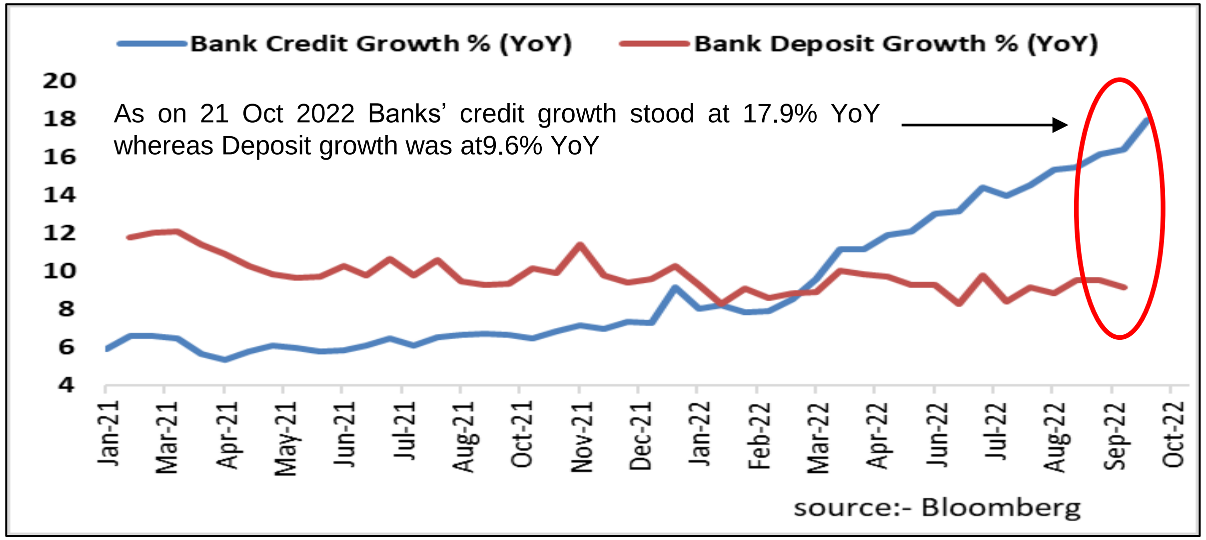


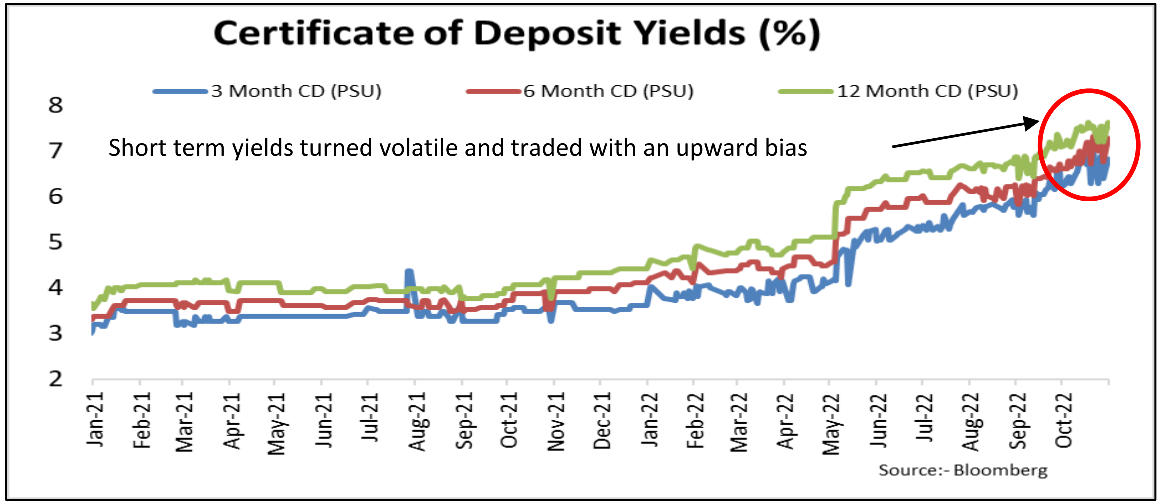


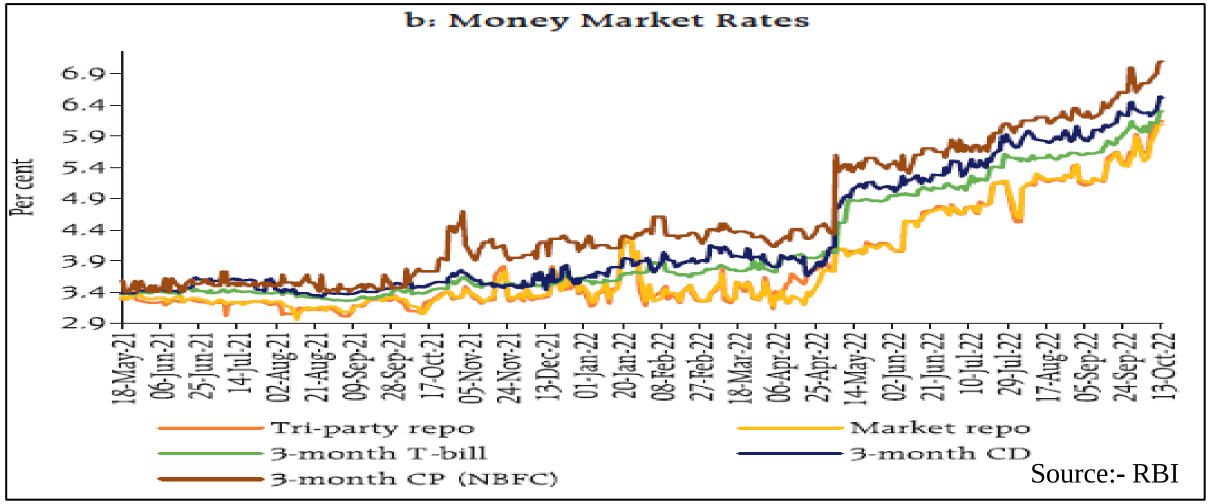
- Currently, the INR seems to be relatively better placed than some of the Emerging markets in terms of contained inflation, a positive growth differential with its peers, and low external sovereign debt.
- That said the INR could remain under pressure given the global economic uncertainty.
- The RBI has been so far successful in ensuring an orderly depreciation of the Rupee and is likely to continue doing so.
- This would mean further drawdown on the Forex Reserves.
- Thus the level of Forex Reserves, movement in USD, and India's Balance of Payments remain key monitorables.

Banking system liquidity remained in Deficit mode for most part of October 2022…









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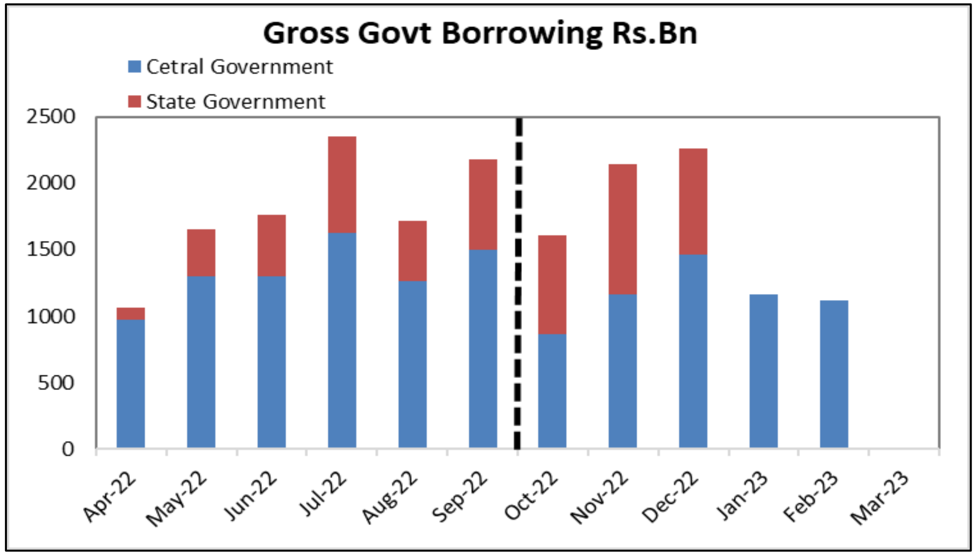
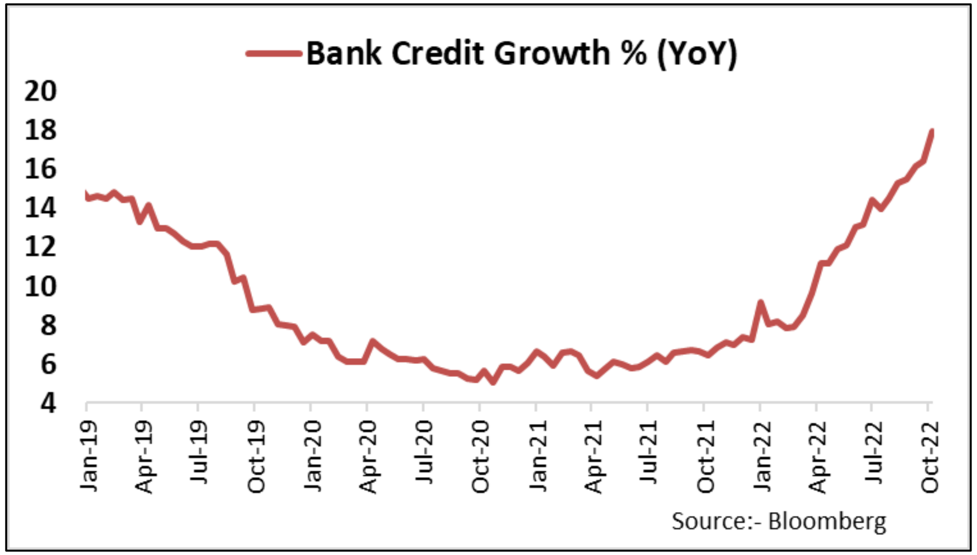
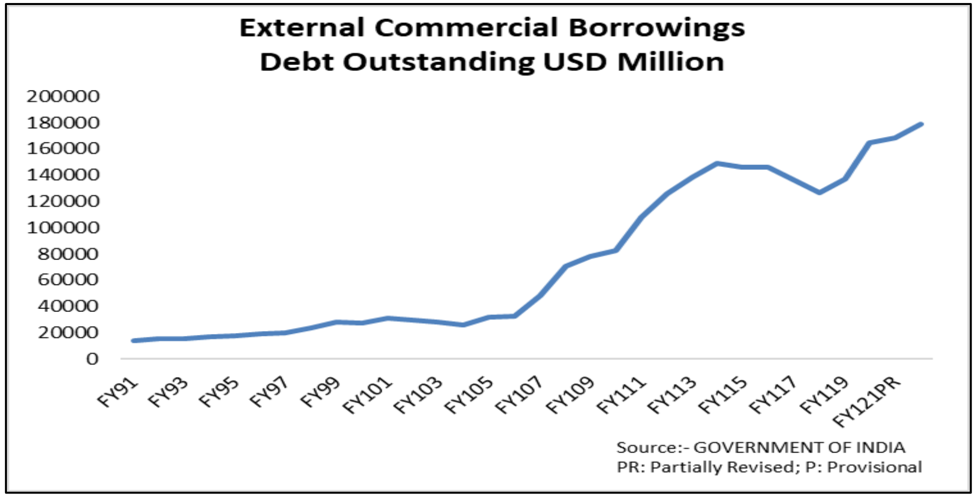
Rising credit growth and G-sec supply may continue to exert upward pressure on shorter end of the yield curve…

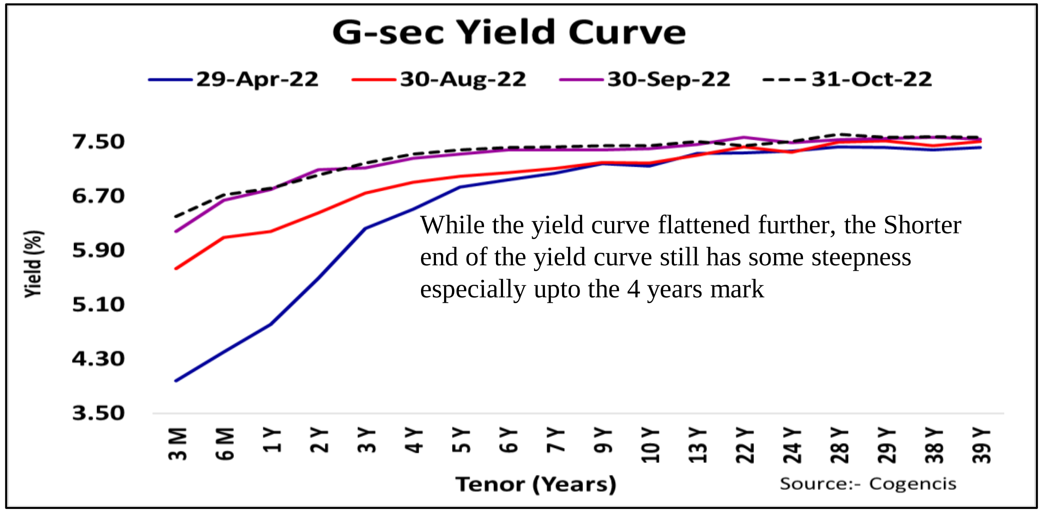


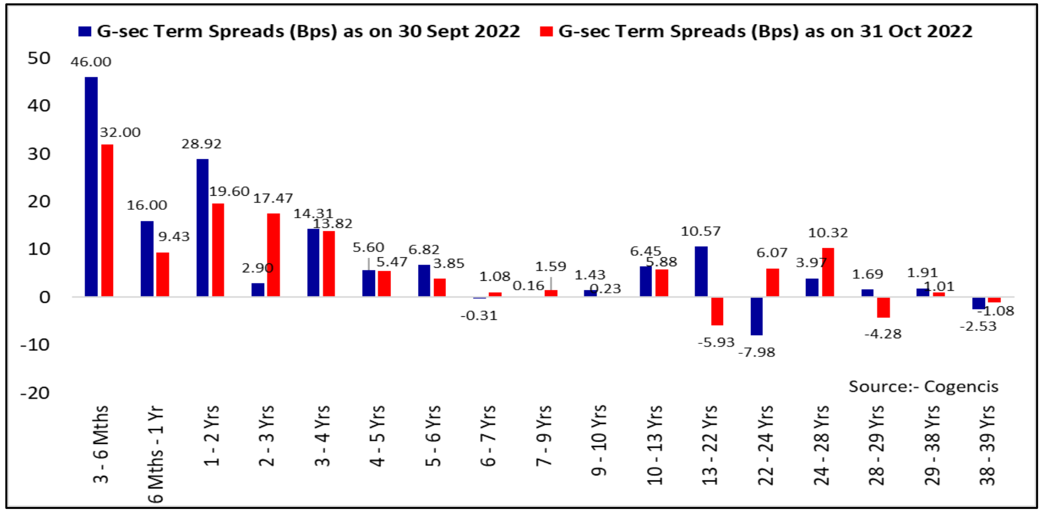


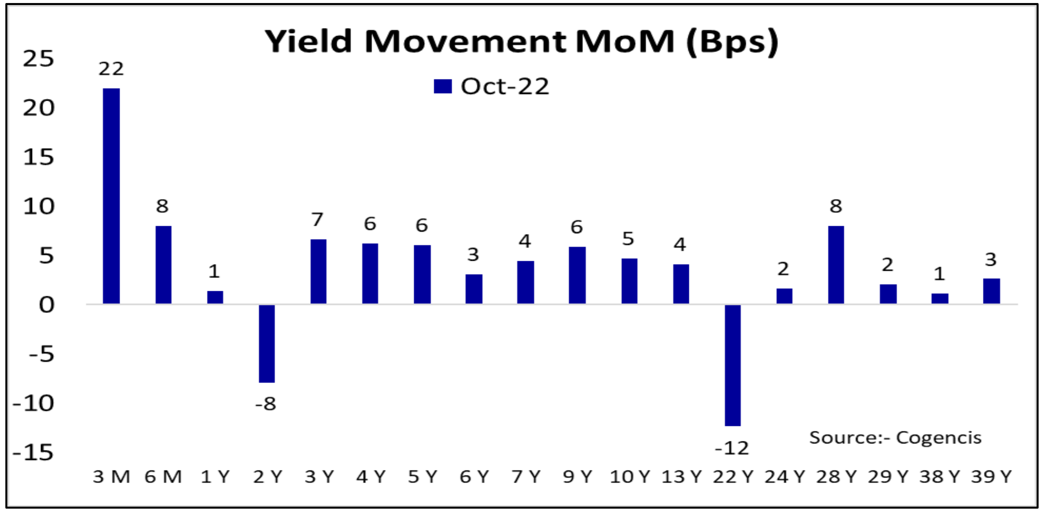


- The demand for liquidity is likely to remain high, given the rising credit growth and G-sec supply.
- With the cost of borrowings rising globally, it will be crucial to track how the short term External Commercial Borrowings (ECB) are getting refinanced.
- Should this demand for funds also come to Indian markets, the pressure on system liquidity could get accentuated.
- Thus, the pressure on liquidity is likely to continue in the near to medium term which in turn can add to the upward pressure on the shorter end of the yield curve.

Yield Curve flattened further as the short term yields continued to rise amidst negative banking liquidity…







- G-sec yield curve flattened further in October 2022 wherein term spreads declined on a MoM basis.
- That said the shorter end of the yield curve was relatively steep as compared to the other segments of the yield curve.
- Spread between the 1 year and the 4 years G-secs stood at 51 bps as of 31 Oct 2022.
- Beyond 4 years the yield curve is almost flat.
- ***The Shorter end of the yield curve is better placed from risk-reward perspective due to relatively stability on account of lower duration and benefit of reset in yields on the higher side due to monetary policy tightening.***

Classification - Restricted

Fixed Income Outlook

- Liquidity is likely to remain under pressure going forward given the rising credit growth and G-secs supply pressure. Also, RBI's Forex interventions are likely to continue in the near term to smoothen Rupee volatility, which could to be another factor leading to lower liquidity surplus. We may see liquidity moving in a range between the deficit and surplus levels with the RBI stepping in on either side as and when the need so arises.
- With unseasonal rains having impacted crops and festival season demand, food inflation is likely to remain elevated in the near term. Low base effect of last year even in October 2022, is another pressure point for the next inflation print. The recent rise in commodity prices if sustained could also add to the inflationary pressures. Additionally, the depreciation in the INR could also add to the overall inflation through imported inflation. Thus, in the near term we expect inflating to remain above the RBI's flexible inflation target of 2%-6%.
- India's Current Account (CAD) deficit is likely to widen, leading to implications on Rupee exchange rate and thereby pries of imported items. Here the Balance of Payments' situation and RBI's Forex management will be critical. Thus, currently a host of variables both global and domestic are imparting uncertainty to the inflation trajectory.
- Going forward, the RBI is likely to continue with the monetary policy tightening unless it sees a structural decline in domestic inflation. Given the fact that even the US Fed is likely to continue monetary policy tightening, other nations grappling with high inflation albeit with relatively better growth rates could also adopt a similar approach to tame the current unbridled inflation.
- The supply of government bonds continues to remain elevated, which is likely put upward pressure on G-sec yields. That being said so far the demand-supply have remained balanced with the weekly G-sec auctions seeing strong demand. So far, the RBI does not seem to be in favour of conducting OMO purchases despite the liquidity tightness. In terms of fiscal deficit, while the tax collections have been strong, should the government need to take further measures for ensuring macro-economic stability amidst global uncertainty, it may have implications on its revenues.
- Despite of growth slowdown and possibility to further impact on economic growth due to tight monetary policies, major global central banks have shown strong intent of decisively bringing the elevated inflation down to their respective target range. For this, further rate hikes are being talked about by the policy makers. Thus, the trajectory of yields and yield curves is likely to be determined by the growth-inflation dynamics, commodity prices, energy prices (including food prices) and currency exchange rate going forward.
- Domestically, flattening of the yield curve is likely to continue given the interest rate hikes by RBI and tightening liquidity conditions. The markets are pricing in a terminal Repo rate in the range of 6.25%-6.50%. Thus, currently, there is a lot of uncertainty surrounding the global as well as domestic economies, leading to volatility in capital markets.
- Given the expected volatility and uncertainty and expectations of flattening of the yield curve, staying invested at the short and the very short end of the yield could be better from risk reward perspective currently.
- Thus, investors should look at funds oriented towards the shorter end of the yield curve for relative stability in the near term and to benefit from the reset in interest rates on the higher side. For this one can look at Short Duration Funds, Money Market Funds, Ultra Short Duration and Low Duration Funds for a horizon of 12 months and above.
- For investors looking for accrual strategies, they can consider Target Maturity Index Funds that invest in a mix of better quality bonds with investment horizons matching the maturity of the funds.
- Investors who are comfortable with volatility and have a longer investment horizon could look at Dynamic Bonds for a horizon of 24 months and above.
- For a horizon of 3 months and above Arbitrage and Money Market Funds can be considered. Whereas, for a horizon of up to 3 months investors can consider Overnight Funds and Liquid Funds.
- Investors should invest in line with their risk profile and product suitability.

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