DSP CONVERSE AT A GLANCE

NOV-2023

REMAIN LONG (WHY NOT?)

(i) We **don't see yields rising up meaningfully.** Yes, inflation will move higher - but that will not lead to rate hikes. We have already gone through a stress test last month. The US 10y yields reached 5%, and RBI surprised markets with the OMO announcement: yet the Indian yields were only 10bp higher from here. 10bp!! That's a noise we can bear. If it aint going up, its going down.

(ii) Demand outstrips Supply. We have a reducing fiscal deficit, muted corporate bond issuances, and restrained state borrowing . On top of it, the insurance and PF segment is growing at a much higher pace. Domestic demand is higher than supply. And a perfect storm is brewing due to impending global bond inclusion FPI inflows. Do not be fooled into thinking that the inflows are marginal to total borrowing - it is a significant part of free float.

(iii) Global macro data is finally weakening. US labour markets is no more sticky - and it is percolating to inflation. Fed Futures indicate no more rate hikes from Fed - only cuts (and soon!). UK data has fallen off a cliff. China has fallen off a cliff into an abyss. While there is no certainity where the data will move - but base scenario has surely worsened in past month!

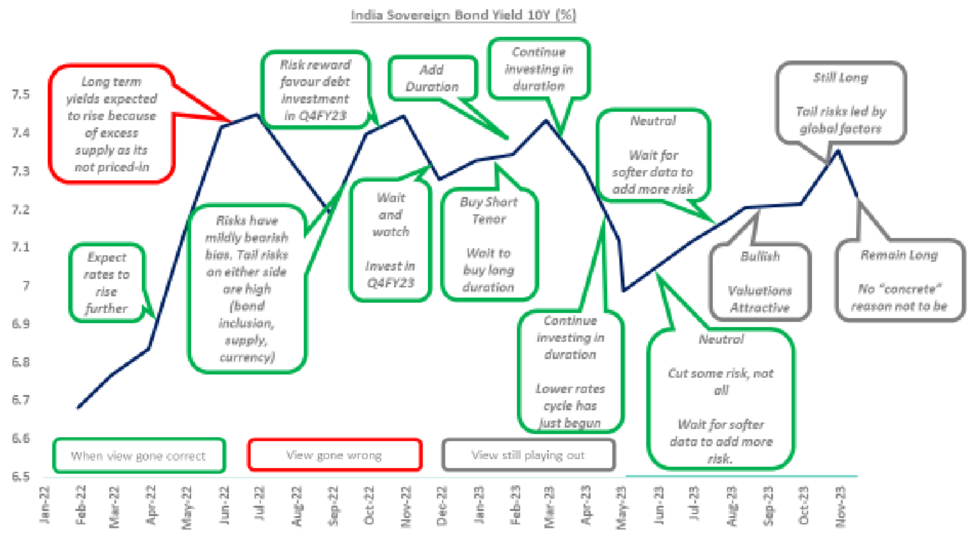
OUR POSITION

We bought bonds in Sept. Since then yields rose (RBI OMO) before settling to entry levels. We wait for view to play out.

We remain long bonds in our funds. We like 20Y+ bonds as the demand from bond inclusion and no RBI holding for OMO sell means that demand outstrips supply.

DSP remains the fund house for those who have a view that bonds are a good buy. We believe the risk of yields rising are much lesser than yields falling.

Risks? We are wary of rupee risks. Risks emanating from RBI OMO sells havent dissipated. Inflation will rise till Dec, but it should be transient. State election results are an big unknown risk right now.



SNAPSHOT OF OUR VIEW

View complete DSP Converse presentation at dspim.com->Tools and Resources->Insights->Converse

Periods: Q3FY24 | Q4FY24 | H1FY25 | H2FY25 | FY26

RATES VIEW: Short-term uncertainty. Medium term fall in yields.

		View	SLIDES IN CONVERSE
MONETARY POLICY	INFLATION	Inflation to rise, but MPC will overlook. Global yields and rupee bigger drivers.	#13
	GROWTH	Growth in "neutral zone" / Signs of growth sputtering in future - but no strong evidence yet.	#14
	CURRENCY	Trade deficit up, FX reserve low. No panic, but concern. / Much uncertainity on global macros, risk appetite and capital flows	#18, #19
FISCAL POLICY	SUPPLY	Low supply / Pre-election spend? / Consolidation of fiscal deficit continues	#26, #27, #28
	DEMAND	Bank demand muted HTM regulations / PF/Insurance growth will outstrip Gsec supply growth.	#26, #27, #28
	FPI FLOWS	Flows will come. Probably in Q4FY24	#30
GLOBAL DRIVERS	COMMODITIES	Oil and other commodities have retraced to neutral zone. Future course difficult to ascertain.	#9
	GEO-POLITICS	Escalation of Ukraine, US-China and Gaza seem to have abated.	#24
	GLOBAL YIELD	Global economy faltering / Difficult to project macros too much in future	#9
OTHERS	ELECTIONS	State elections? Unknown risk / General Election uncertainity	NA
	RBI REGIME	Liquidity/Rupee wary / Rupee wary now, but will follow global yields	#29

Nov 2023

Remain Long

No “concrete” reason not to be

DSP CONVERSE

Our Framework

Monetary Policy

Inflation
- Oct print at 4.87% vs 5.02% in Sep
- Overall food inflation remains sticky (pulses, cereals, spices)
- Upside risks remain
- But core inflation continues its downtrend

Growth
- Domestic activity is resilient so far
- Mixed outlook commentary in Q2
- Revised lending norms might impact credit growth/consumption

Currency/CAD/BOP
- External sector pressures remain low, but…
- INR vulnerable to EM reaction
- Trade deficit widened sharply to $31.5bn for Oct
- Don't panic but remain alert

Fiscal Policy

Supply
- Low supply of G-Secs
- SDL supply is expected to remain muted
- Healthy NSSF deposit accretion

Demand
- Banks SLR holding remains high, may reduce
- FPI inflows around corner

FPI
- FPIs are unlikely to sell: holdings are already low
- FPIs are unlikely to buy in current yield spread (at least this year)
- Passive flows only in the next year

Global Drivers

Global Yields
- US Data has finally weakened
- Further rate hike probability in US at zero

Geopolitics
- China/US in conciliatory tone
- Ukraine Russia conflict is in backburner
- Israel-Palestine Conflict so far remains contained

Commodities
- Price risks are evenly balanced

Others

RBI Regime
- Shift from Arjuna's eye to 4% CPI target
- Focused on using liquidity tools to manage stance

Misc.
- Election related risks:
  - State election results in Dec'23
  - Govt expenditure prior to General elections

Positive

Neutral

Negative

Takeaway:
Stable domestic macro. Global data is also weakening.

DSP

CAD – Current Account Deficit; BoP – Balance of Payment; SLR – Statutory Liquidity Ratio; SDL – State Development Loans; RBI: Reserve Bank of India; G-Sec: Government Securities; FPI: Foreign Portfolio Investment; NSSF: National Small Savings Fund; EM: Emerging Markets; CPI: Consumer Price Index

SUMMARY

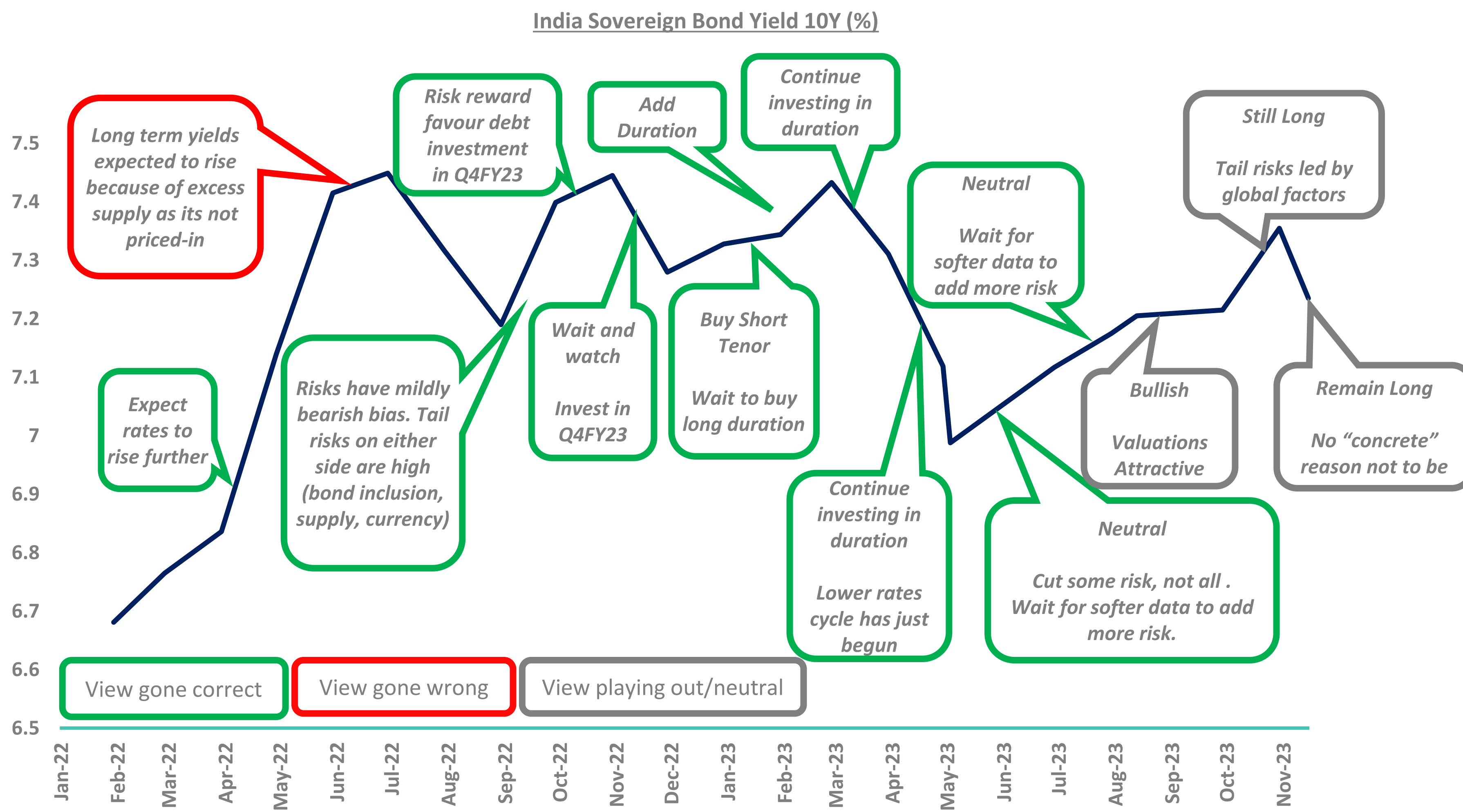
Still Long! Why?

Can’t find any “real” reason no to be

Risks from (announced RBI OMO sale/RBI Dec Policy/State Election results)

TRAJECTORY

Let’s revisit our rates call trajectory



Source – Bloomberg, Internal

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To start with,

Recap of events since last release.

WHAT HAS CHANGED

RBI tightens unsecured lending norms

US Data has finally weakened

Oil is now around $80 vs $90+ during last converse

US Rate hike expectations now out of the way

RBI tightens unsecured lending norms

Key Changes

- Risk weight on consumer credit exposure of SCBs/NBFCs increased by 25%
  - ✓ Including credit card receivables
  - ✓ But excluding housing/vehicle/education/gold and MFI loans (for NBFCs)
- Risk weight on SCBs lending to NBFCs (with existing risk weight <100%) increased by 25%
  - ✓ Excluding CICs
  - ✓ Loans classified as priority sector

Market Impact

- Initial reaction is of increased spreads, fearing supply
- While spreads in short papers may remain elevated, longer end bonds should get demand from insurance, pension funds, etc.
- Long term trends will, inter alia, depend on pace of growth of NBFCs, which may decline post this change

Credit Impact

- For our portfolio of large, well managed companies, we expect no meaningful credit impact

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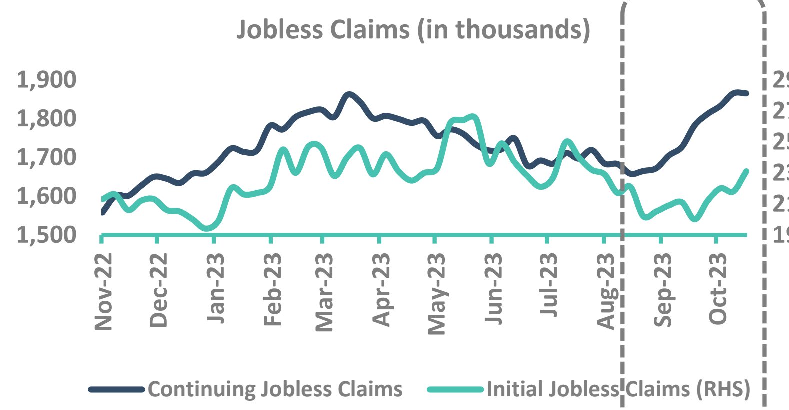
Source – RBI, Internal

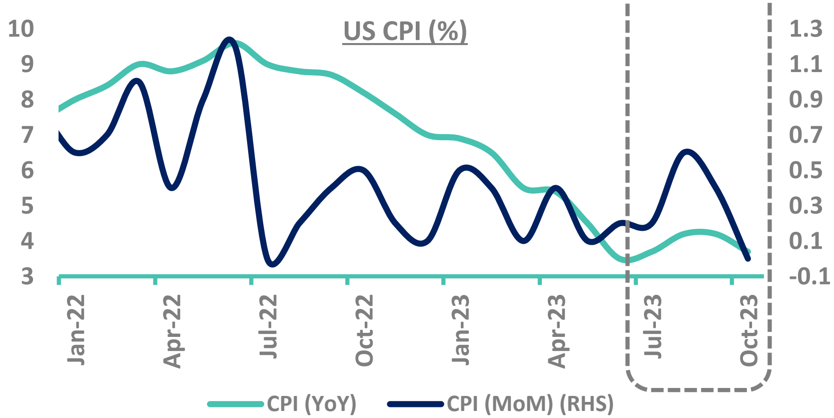
RBI: Reserve Bank of India; NBFC: Non-Bank Finance Companies; MFI: Micro Finance Institutions; SCB: Scheduled Commercial Bank; CIC: Core Investment Companies

US data has finally weakened/Oil is back at $80 levels

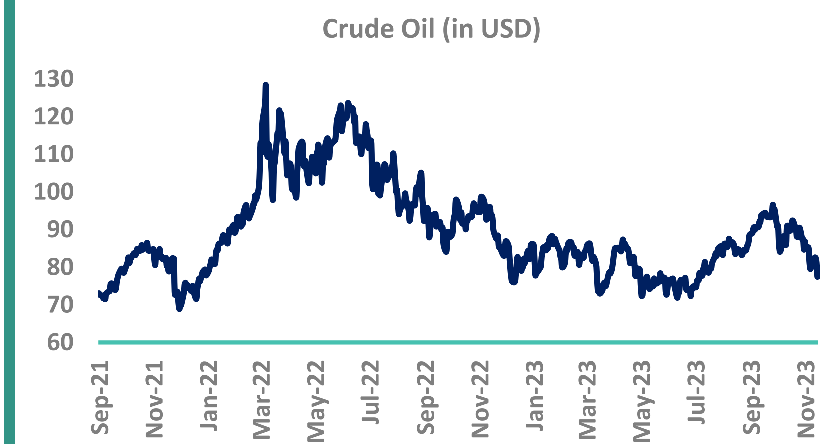
➢ The US job market has weakened



➢ And is now percolating to inflation



➢ Oil has retraced from 90+ levels



➢ US rate hike expectations now out of the way

Fed Fund Projected Rates

Fed Policy	As of Oct End		As of 16th Nov	
	Implied Rate	No. of cuts/hike	Implied Rate	No. of cuts/hike
Dec'23	5.387	0.234	5.333	-
Jan'24	5.418	0.355	5.323	-0.040
Mar'24	5.379	0.200	5.245	-0.350
May'24	5.274	-0.219	5.118	-0.856
Jun'24	5.152	-0.709	4.967	-1.461
Jul'24	5.013	-1.265	4.818	-2.060

Takeaway:
US data has weakened and rate hike expectations now out of the way

Source – Bloomberg

DSP

CPI: Consumer Price Index

Now our framework

And

What we track

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- Domestic activity is resilient so far
- Mixed outlook commentary in Q2
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Currency/CAD/BOP
- External sector pressures remain low, but…
- INR vulnerable to EM reaction
- Trade deficit widened sharply to $31.5bn for Oct
- Don't panic but remain alert

Fiscal Policy

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Resilient domestic economic activity so far

Expansion in urban demand while rural still not out of woods

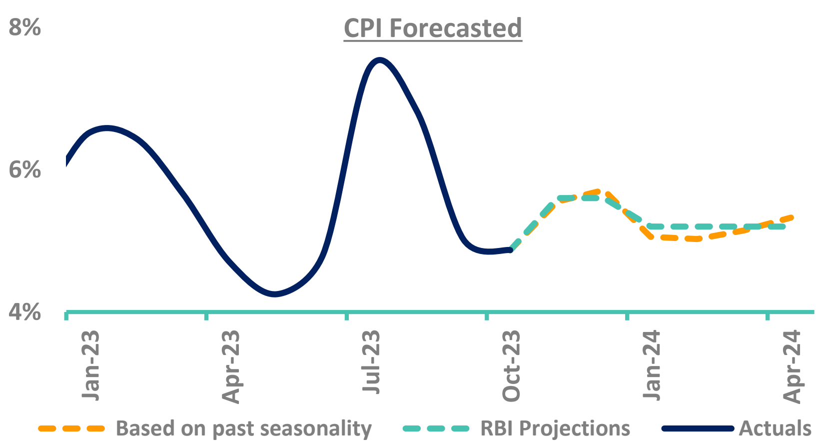
Oct CPI now below 5%, core moderates further

To consider OMO sales to manage liquidity

Inflation print below 5% mark, but upside risks remain

- **Inflation moderated in-line with expectations**
  - Oct print came in at 4.87% vs 5.02% in Sep
  - Sequential uptick of 0.7% (vs -1.1% in Sep)
  - Food inflation overall remains sticky
    - ✓ Led by cereals, pulses and spices
  - Upside risks remain due to
    - ✓ Geopolitical conflicts & uncertainty on rabi sowing (low reservoir levels)

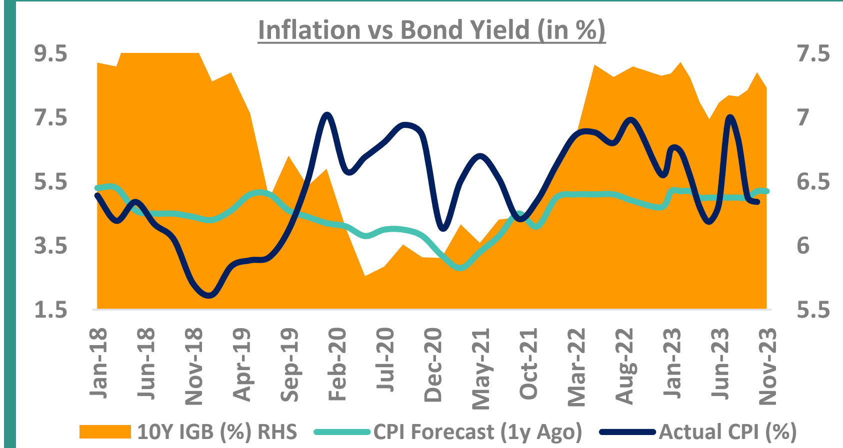
- **Core CPI continues it's downtrend**
  - Came in at 4.3% vs 4.5% in Sep



- **Do yields track inflation projection? No.**
  - Orange area (chart) is 10Y yields, Blue line is CPI

- **Can forecasters predict Indian CPI? No.**
  - Green line is forecasters CPI 1-Yr ahead prediction
  - Blue line is where inflation actually came
  - Guess the error of margin!

- **CPI forecast corelated (not causality) to yields**
  - Low predictive power, high current corelation



Takeaway:
Watch out for upside risks even though core provides comfort. However, volatility in CPI has not impacted yields (especially in 2023)

Source – Bloomberg, RBI, Internal

DSP

CPI: Consumer Price Inflation; RBI: Reserve Bank of India; IGB: India Government Bond

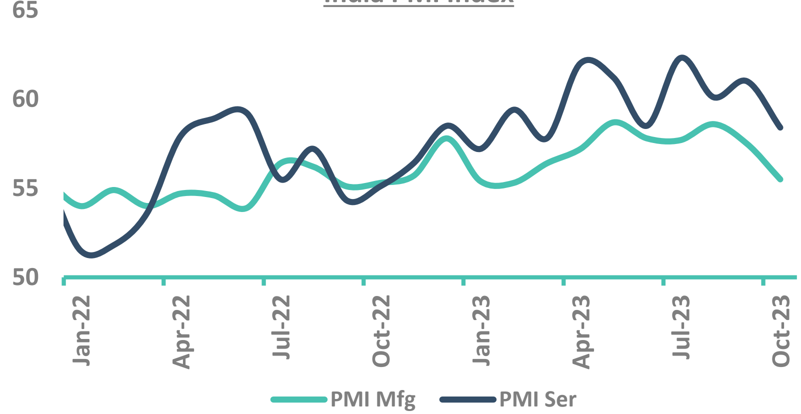
Domestic growth resilient so far: But watch out for trends

➢ Watch out for domestic growth

- PMI is in expansionary mode, but sequentially lower
- GST collections at ₹ 1.72tn (2nd highest); up 13% YoY
- Outlook commentary in Q2 has been divergent. E.g.:
  - ✓ FMCG (urban↑, rural↓), Auto (PV ↑, 2-wheeler ↓), Apparel (luxury ↑, value ↓)

➢ Loan growth still near decadal high

- Led by retail and services segment
  - ✓ Revised lending norms might impact this
- Credit growth to large corporates remain sluggish

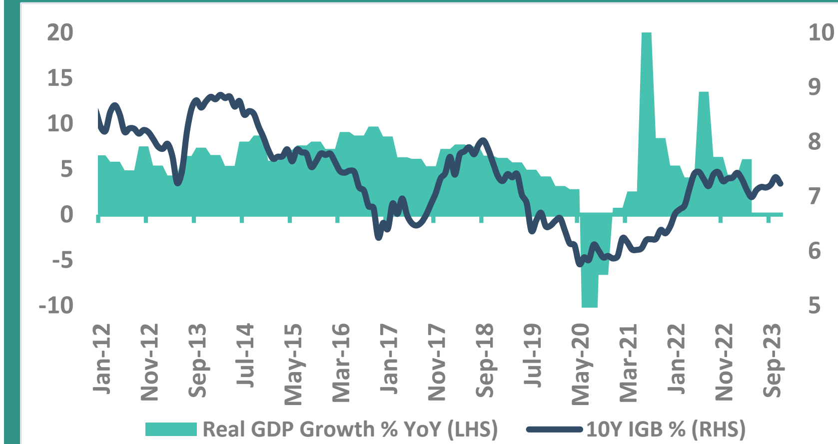


➢ How closely do yields track growth?

- Yields have usually tracked GDP growth, with correlation being stronger when growth slows, barring
  - ✓ 2013, rupee depreciation and debt outflows
  - ✓ 2017, during demonetization

➢ FY24, growth may not be big driver for yields

- FY23 GDP growth came in at 7.2%, in line with RBI projections.
- Q1FY24 GDP Growth came in at 7.8%.



Takeaway:
Domestic growth seems to be resilient so far but watch out for emerging trends

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Source – Bloomberg, PIB, Internal

GDP: Gross Domestic Product; PMI: Purchasing Managers' Index; GST: Goods and Service Tax; IGB: India Government Bond; Mfg: Manufacturing; FMCG: Fast Moving Consumer Goods; PV: Passenger Vehicle

What made RBI Pause?

Series of hygiene factor lead to RBI pause: They point to pause

The checklist for pause:

A. When the US Fed starts pausing

- Reduces risk of capital outflows

B. When inflation is within comfort

- Reduces risk of inflationary policy
- Barring 2014 ***(refer to the dotted area)***, when RBI did not have 6% CPI target
  - ✓ But CPI was falling in 2014

C. When BoP (and currency) is stable

- Reduces inflationary / external risks

How is the checklist now?

↔ **A: US markets indicating no more hikes**

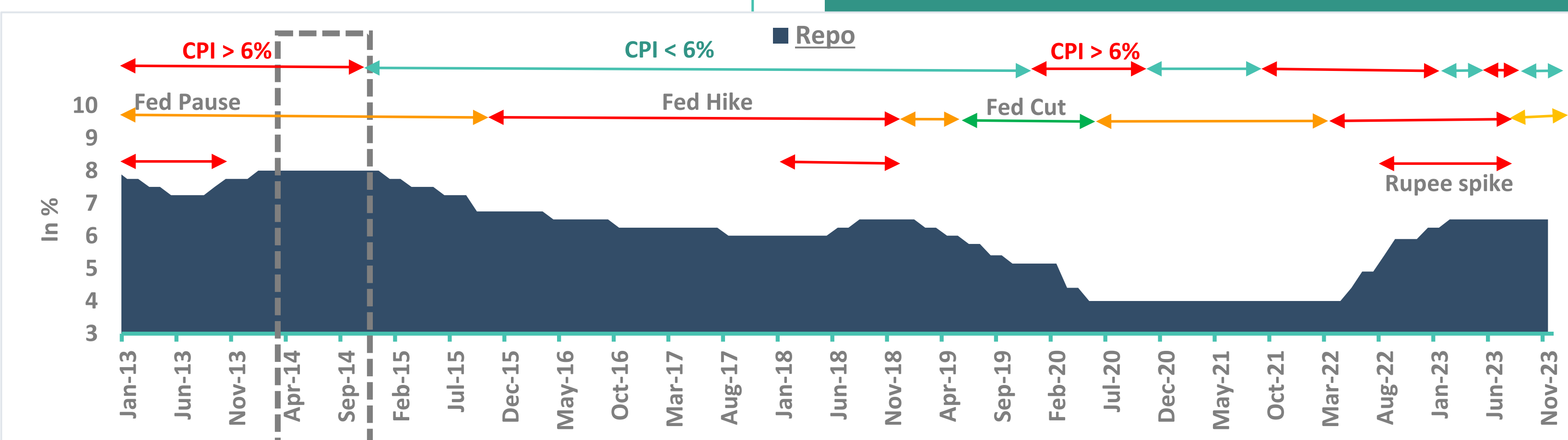
- Even though FED remains data dependent
- FED to remain on "WAIT and WATCH" mode

↔ **B: Inflation not a worry as of now**

- Headline as well as Core CPI is easing
- Although uncertainty remains

↔ **C: BoP is stable, but rupee has fallen**

- BoP in surplus in Q1FY24
- But rupee remains vulnerable to EM reaction



Takeaway:
There is no conclusive reasons for any rate action by RBI

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Source – Bloomberg

RBI: Reserve Bank of India; US FED: US Federal Reserve; BoP – Balance of Payment; CPI: Consumer Price Inflation; EM: Emerging Markets

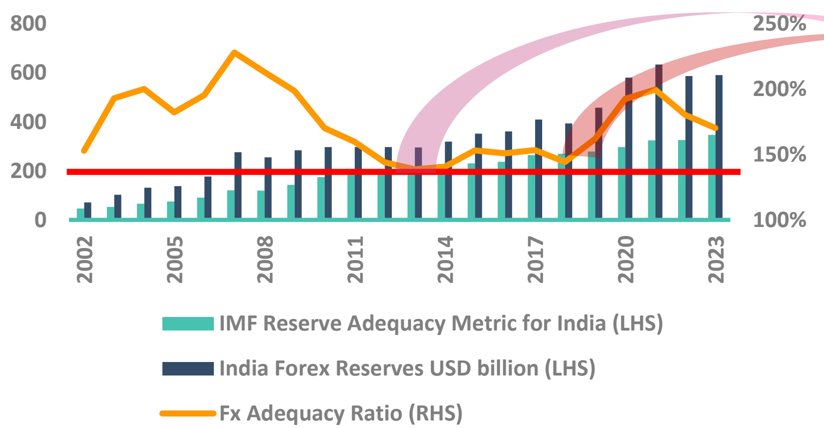
Can RBI Hike? Unlikely.

RBI hikes rates usually for FX and FED (primarily), and CPI (at times)

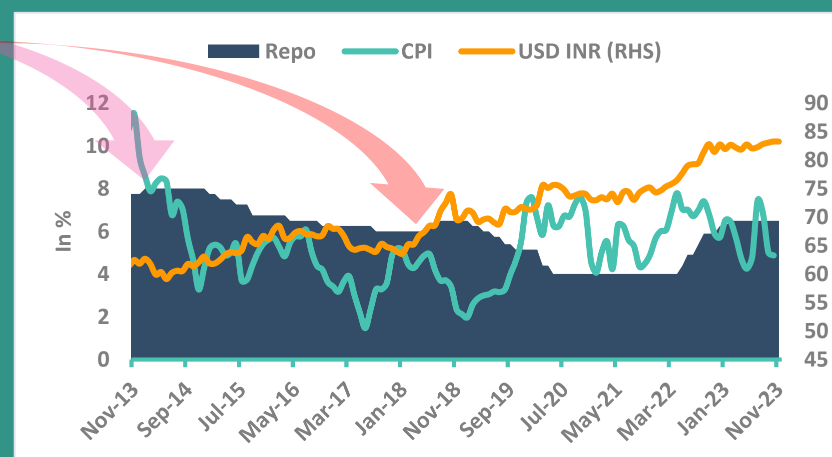
External sector metrics are worsening, but not yet a concern.

Did you know – FX reserves dip lead to RBI hikes. Current Risk low.

- **RBI FX reserves have reduced lately**
  - Forex reserves reduced to ~$591bn from $640b+ during covid peak
- **IMF FX adequacy metric for CY23 announced**
  - FX adequacy ratio declined from 180% to 170%
  - However, a buffer of almost $70 bn to reach 2013 and 2018 levels (~150% ratio)



- **RBI only hiked rates twice in past 10 years, barring latest cycle**
  - Increased rates to control rupee, not inflation
- **RBI has tolerance for inflation, not rupee fall**
  - In 2018, inflation was within RBI's target levels
  - In 2013, inflation was high for long yet RBI cut
- **When RBI FX reserve fall**
  - RBI switches from using reserves to rate hikes to control rupee.



Takeaway:
FX Reserves have reduced lately but there is enough ammunition to protect rupee

Source – Bloomberg, RBI

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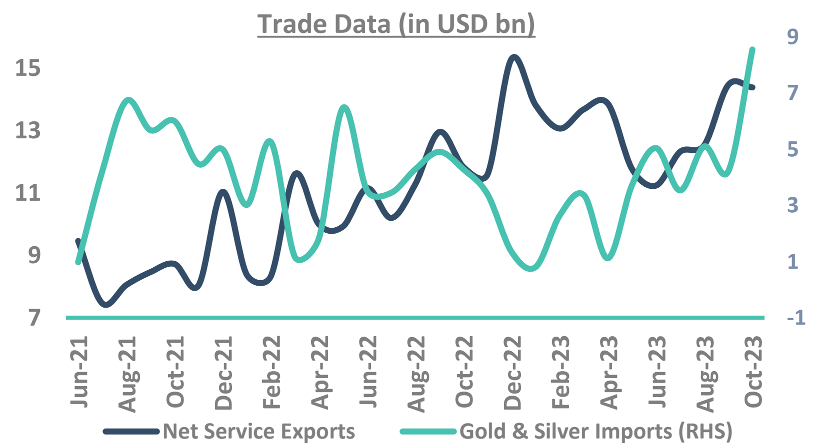
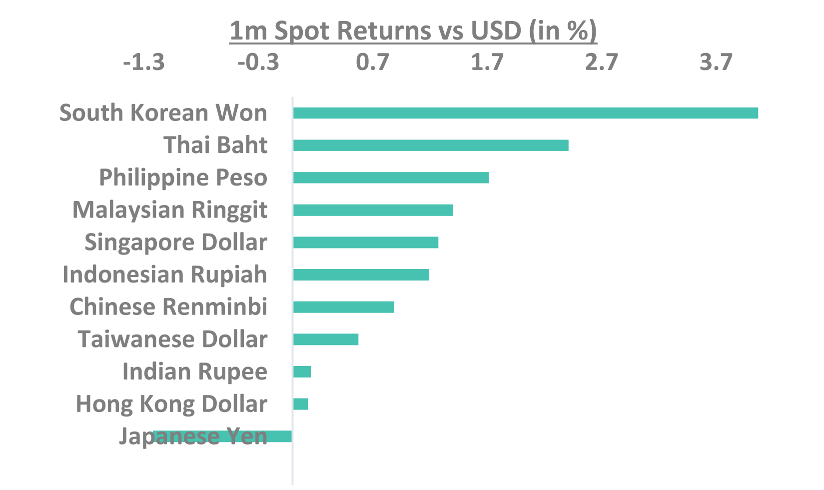
RBI: Reserve Bank of India; IMF: International Monetary Fund; US FED: US Federal Reserve; FX: Forex; CPI: Consumer Price Inflation

Trade Deficit and Currency: Antennas up

- **BoP is probably worse**
  - FX reserves low despite MTM gains (UST ↑, Gold ↑)
- **Trade deficit widens in Oct ($31bn vs $19bn)**
  - Led by imports (12.3% yoy) against exports (6.2% yoy)
    - ✓ Festive gold/silver demand
    - ✓ High oil imports (lower Russian oil discount)
  - Expected to normalize in from current levels
  - Services surplus remains firm



- **Rupee seems to track EM currencies**
  - INR Depreciation in line with EM currencies (chart)
- **But this is not true picture…**
  - Flatline USD/INR indicates RBI is setting price
  - INR would have underperformed EM but for RBI
- **We are not yet concerned.**
  - Bond inclusion flows around the corner



Takeaway:
External Sector metrics weakening but not yet a concern

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Source – Bloomberg

BoP: Balance of Payment; MTM: Mark to Market; EM: Emerging Markets; UST: US Treasury

Data remains to be supportive

CPI moderated further

INR vulnerable by EM reaction

US data has weakened

Risks from RBI Policy surprise/OMO sale announcement/State election results

Let’s turn to Fiscal policy

Generally, it drives the long bond yields

It is reflected in demand/supply mismatch.

Fiscal policy is favouring bonds right now – though election risks will precipitate in next few months

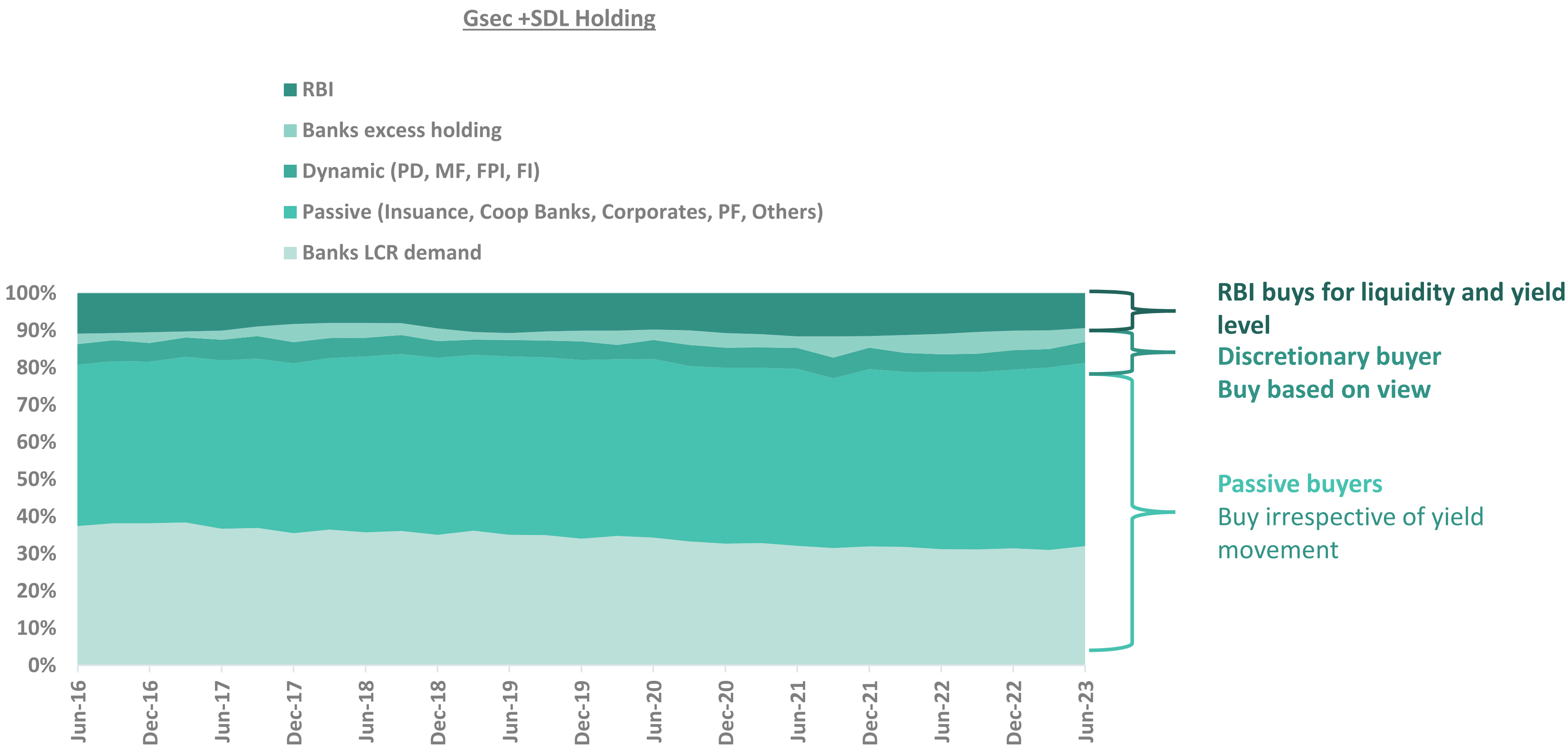
Only a small part of bond buyers are discretionary buyers

They drive yields

Supply fluctuation is borne by these buyers

FISCAL POLICY

Gsec market is still driven by lumpy institution purchases



Takeaway:
Increase in supply impacts the discretionary buying. Banks excess holding, passive buyers have been absorbing the supply

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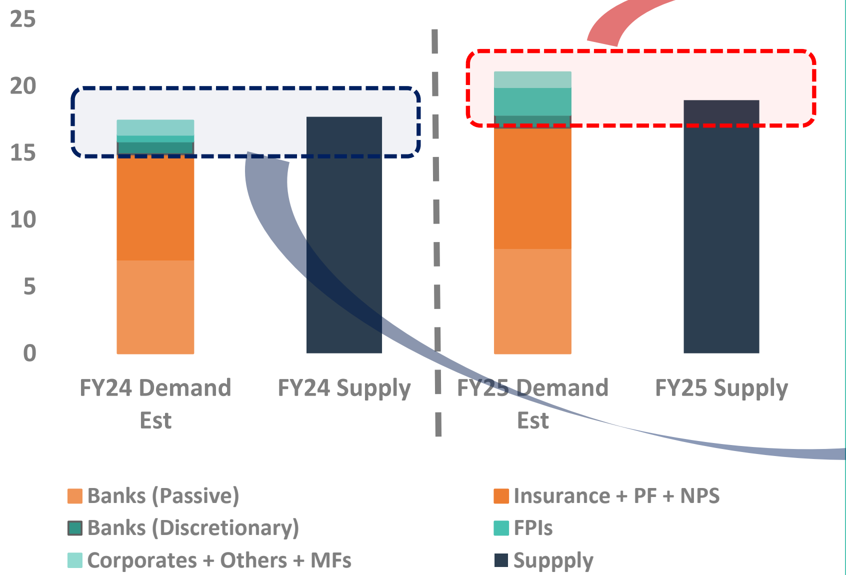
Source – DBIE

LCR – Liquidity Coverage Ratio; SDL – State Development Loans; PF – Provident Funds; PD – Primary Dealerships; MF – Mutual Funds; FPI – Foreign Portfolio Investors; FI – Financial Institutions; RBI: Reserve Bank of India; G-Sec: Government Securities

Why FPI inflow is the big thing: Look at the right metrics

FPI demand *seem* insignificant to total supply

- Assuming supply higher by just 6-7%
- Non-discretionary buying growth at 14-15%
  - Non-discretionary => need to buy for regulation (Insurance/PF/NPS/Bank-LCR) no matter the yield
- Rs. 2 lac cr. of FPI flow may seem pittance in from of Rs. 19 lac cr of supply

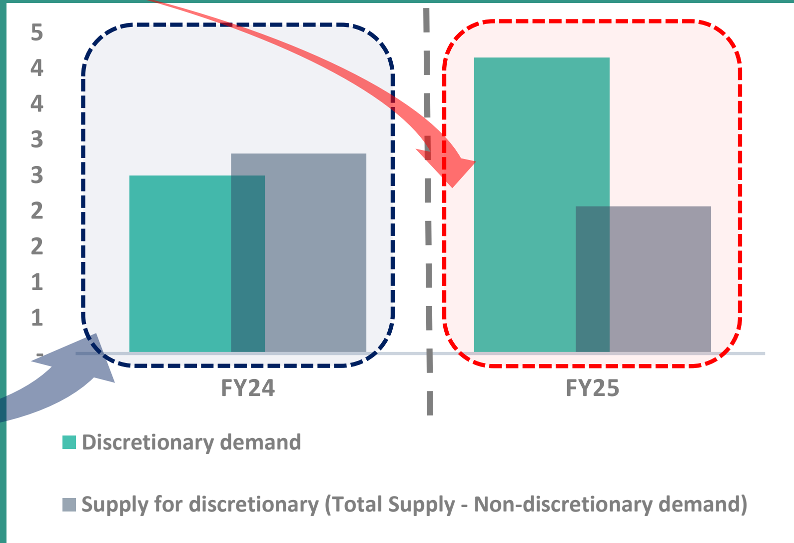


… yet FPI inflow is mammoth

- Supply available for discretionaries is less in FY25
  - Bank non-discretionary demand growing faster
- But the demand from discretionary will increase
  - Discretionary = Look at yields to buy i.e.

Its not share of supply that matters

- It's the share of residual supply
- That's why, OMO fear of < Rs. 1 lac cr rose yield by 20bp



Takeaway:
Additional FPI demand to compete with discretionary buyers

Source – Bloomberg

SDL – State Development Loans; PF – Provident Funds; PD – Primary Dealerships; MF – Mutual Funds; FPI – Foreign Portfolio Investors; G-Sec: Government Securities; OMO: Open Market Operations

Comfortable supply/demand dynamics for FY24

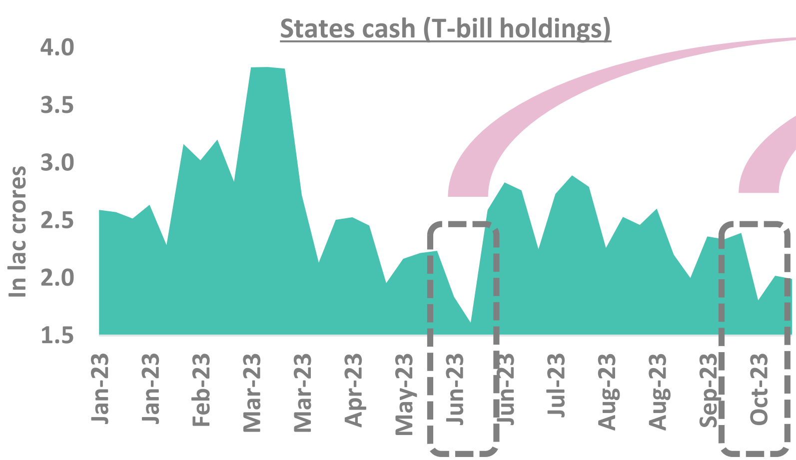
But it will be bumpy ride

Last 7 months demand/supply has been rosy (latent purchases, low SDL issuances)

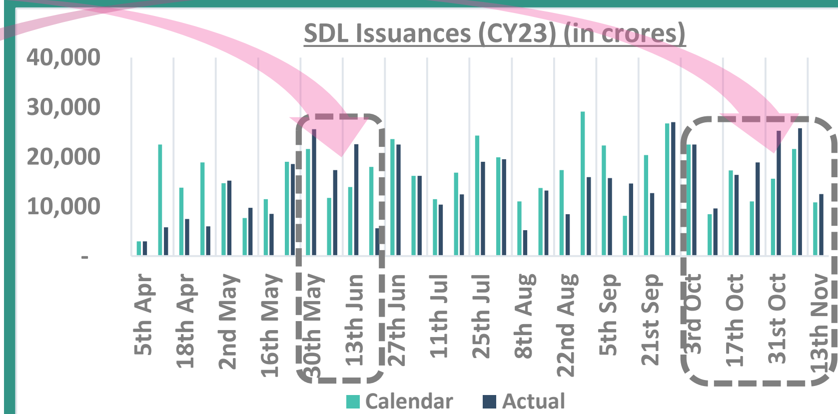
FISCAL POLICY

SDL supply only increases when states cash dip

- **State cash balance hovers around 2tn mark**
- **Center has front-loaded devolution of tax**
- **Issuance is expected to be in line with the calendar /marginally lower at best**



- **Actual SDL borrowing in line with expectations**
  - Higher than the calendar only when state cash balances dipped below 2 trillion
  - 7mFY24 issuance ~12% lower vs the calendar amount
    - ✓ Oct'23 issuance 24% higher vs the calendar due to lower than 2tn state cash balance
- **SDL issuance impact is expected to be limited**



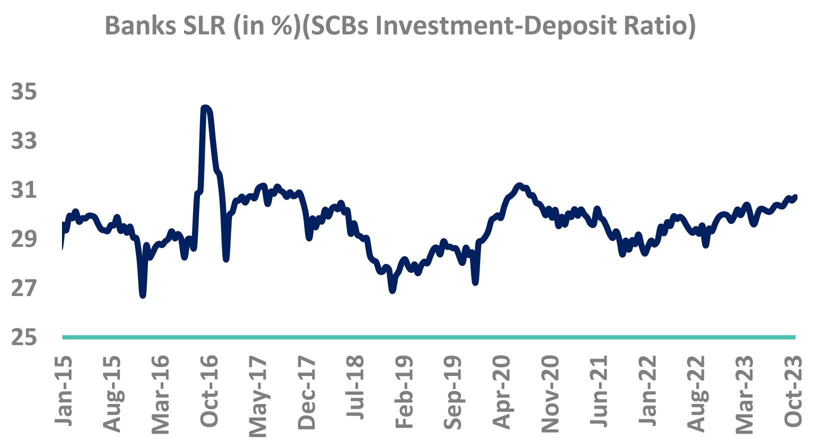
Takeaway:
SDL supply may remain muted in FY24

Source – DBIE, RBI

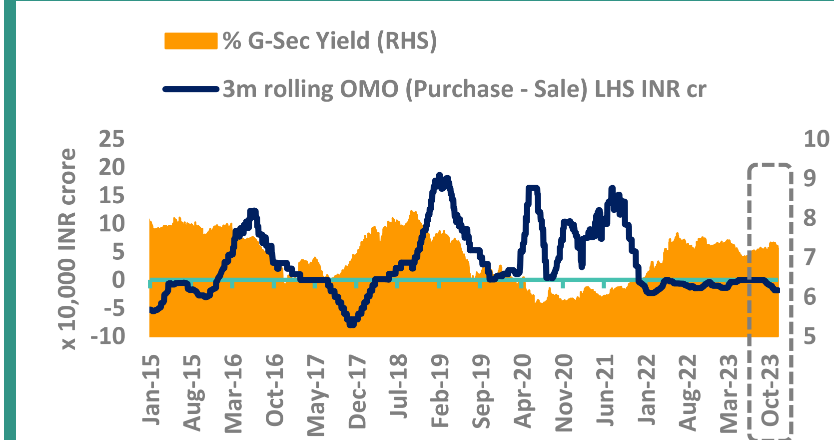
T-bill: Treasury Bill; SDL: State Development Loans

Banks will continue to buy. RBI may sell more.

- **Banks SLR holdings has risen sharply**
  - Banks SLR holding remains high (>30%)
- **Banks have bought nearly ₹ 5 tn in 7mFY24**
  - But this includes bump of HDFC merger
- **And the same pace is expected to continue**
  - As natural NDTL growth will still lead to demand



- **Yields usually track RBI OMO purchases**
  - Yields have strong correlation with RBI OMO
  - Demand/Supply mismatch is filled in by RBI
- **RBI announced possibility of OMO sales**
  - Already sold ~8.5k crores since then *(dotted area)*
- **Uncertainty on OMO size and time**
  - Liquidity will remain tight till Dec mid
  - Yet, by Jan liquidity will be in surplus as Govt will have less need to keep cash post maturities



Takeaway:
Banks' demand for SLR investments to continue

DSP

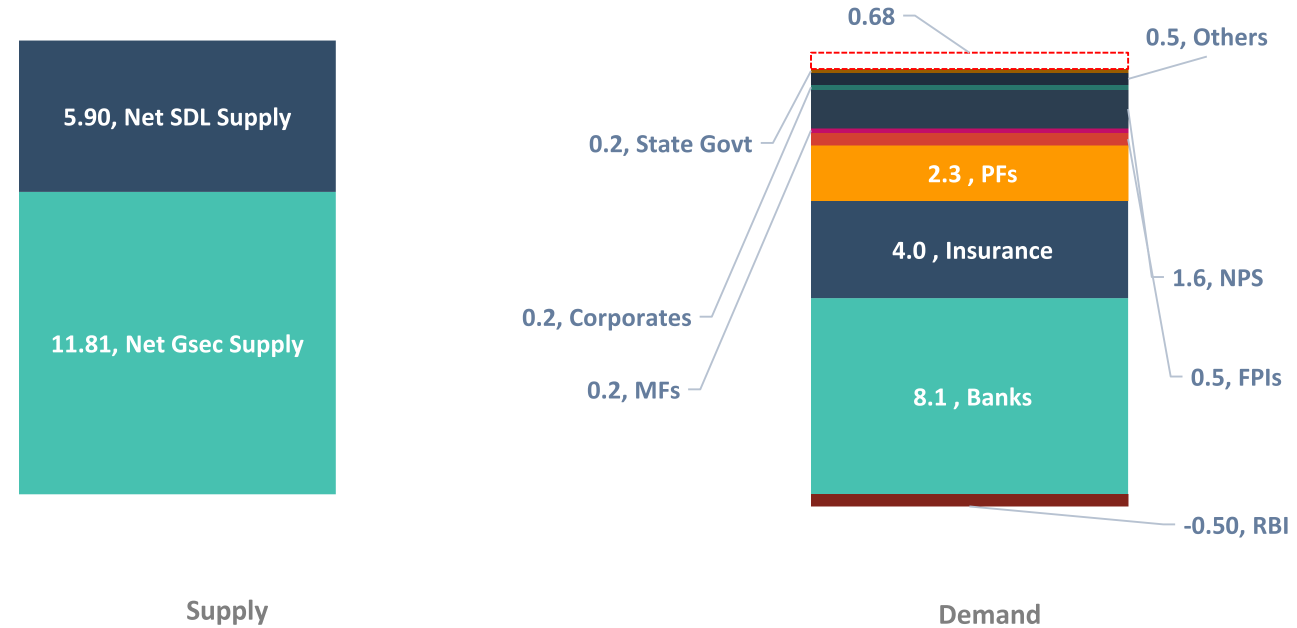
Source – Bloomberg, DBIE, Internal

OMO – Open Market Operations, SLR – Statutory Liquidity Ratio; G-Sec – Government Securities; RBI: Reserve Bank of India; SCB: Scheduled Commercial Bank; CIC: Currency in Circulation

How much is the excess supply

➢ Excess supply can be matched

- ✓ G-sec supply is higher only by 7% over FY23, however demand is expected to rise much more
- ✓ Continuing strong demand from long end investors like EPFO, Insurance and PFs
- ✓ Healthy NSSF deposit accretion



Takeaway:
Estimated excess supply of ₹ 0.68 tn is not very significant. Banks may sustain a higher SLR ratio (we have taken 29.5%)

Source – Internal, CGA

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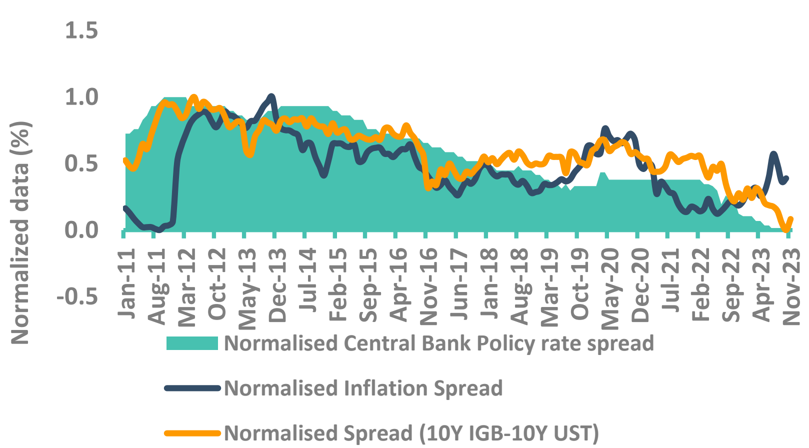
Impact of RBI OMO announcement?

Indian yields have again started tracking Global yields.

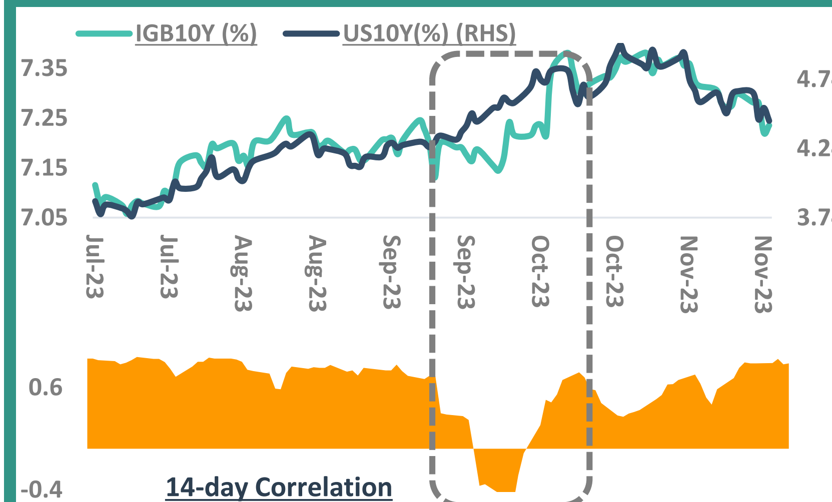
They stopped tracking in Sept, but OMO announcement changed things.

Indian yields – Again dancing to the tune of US Yields

- **FOMC rate at 5.50% - more hikes at play?**
  - Not any more, further rate hike probability at "0" now
  - Data has finally weakened
- **Are spreads of US Treasury and Indian Govt. Bonds low?**
  - Yields spread mimics inflation and policy rate spread.
    - ✓ Currently divergence with inflation spread.
    - ✓ US CPI is falling so correction may come from fall in US yields rather than rise in India yields.



- **Are Indian yields tracking US Rates? Yes**
  - After a brief period of negative correlation, Indian yields again tracking US yields
- **What led to correlation again?**
  - RBI OMO announcement



Takeaway:
With domestic data being on the neutral side, India yields tracking US yields

Source – Bloomberg, Internal

DSP

Fed: Federal Reserve; CPI: Consumer Price Inflation; RBI: Reserve Bank of India; IGB: India Government Bond; FOMC: Federal Open Market Committee; UST: US Treasury

Money Market Assessment Framework

System Liquidity

Currency in Circulation (CIC)

Seasonal increase in CIC drained out close to Rs. 73k crore of liquidity

Foreign exchange inflows / outflows

RBI Liquidity Management Tools – VRR, VRRR, OMOs, CRR change; Fx buy/sell

Frequent intervention by RBI

Possibility of OMO Sales by RBI announced

Demand-Supply

Supply

Outstanding CDs close to Rs. 2.9lac cr; 15% higher than last year

Led by high credit growth

Demand

Mutual funds demand stable

Extent of GOI borrowing through T-bills as expected

MPC Action

With improving domestic macros, both inflation and growth, no action anticipated

Takeaway:

With surplus durable liquidity, stable domestic macros and well-matched demand-supply dynamics expect money market rates to remain range bound. We will remain long in our funds to gain accrual at existing spreads.

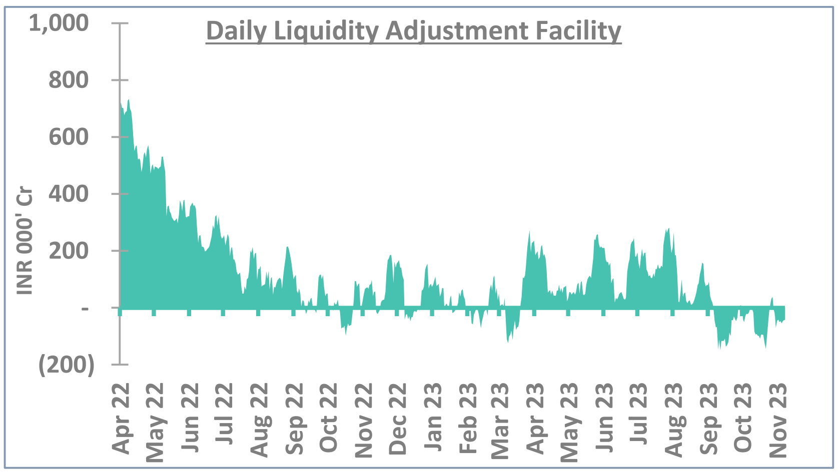
DSP

CIC: Currency in Circulation; CD: Certificate of Deposits; OMO: Open Market Operations; VRR: Variable Rate Repo; VRRR: Variable Rate Reverse Repo; RBI: Reserve Bank of India: GOI: Govt of India

Liquidity to have opposite drivers: Festive season and G-sec redemption

➢ **Durable liquidity is sufficient at ~₹ 2.6* tn**

- However, banking system liquidity remains in deficit of ~₹60k crores
  - ✓ G-sec maturity of ₹ 2tn in Nov/Dec
  - ✓ And month end Govt spending, after adjusting for scheduled outflows, to push banking system liquidity to surplus zone, though not significantly

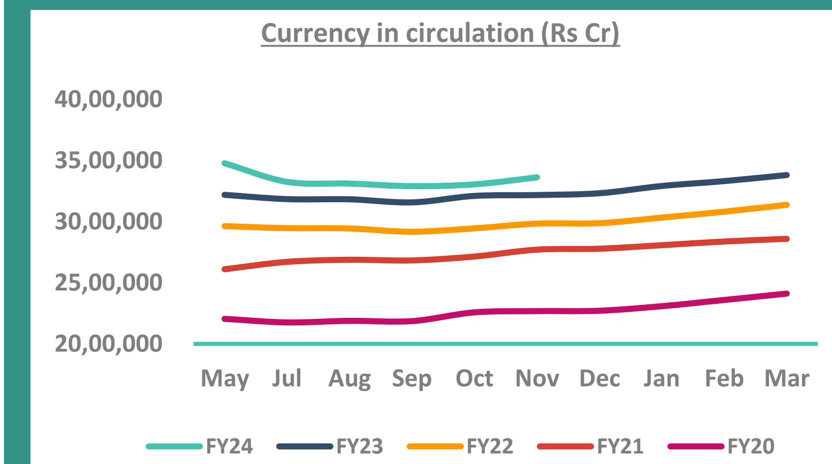


➢ **CIC is typically higher in October and November due to festive demand**

➢ **We saw a CIC drag of ₹ 73k crore from October onwards**

- Typically first fortnight of December also sees CIC outflow in the range of ₹ 15-20k crores

➢ **State elections to further tighten liquidity**



Takeaway:
Banking liquidity expected to remain tight fuelled despite G-sec redemption

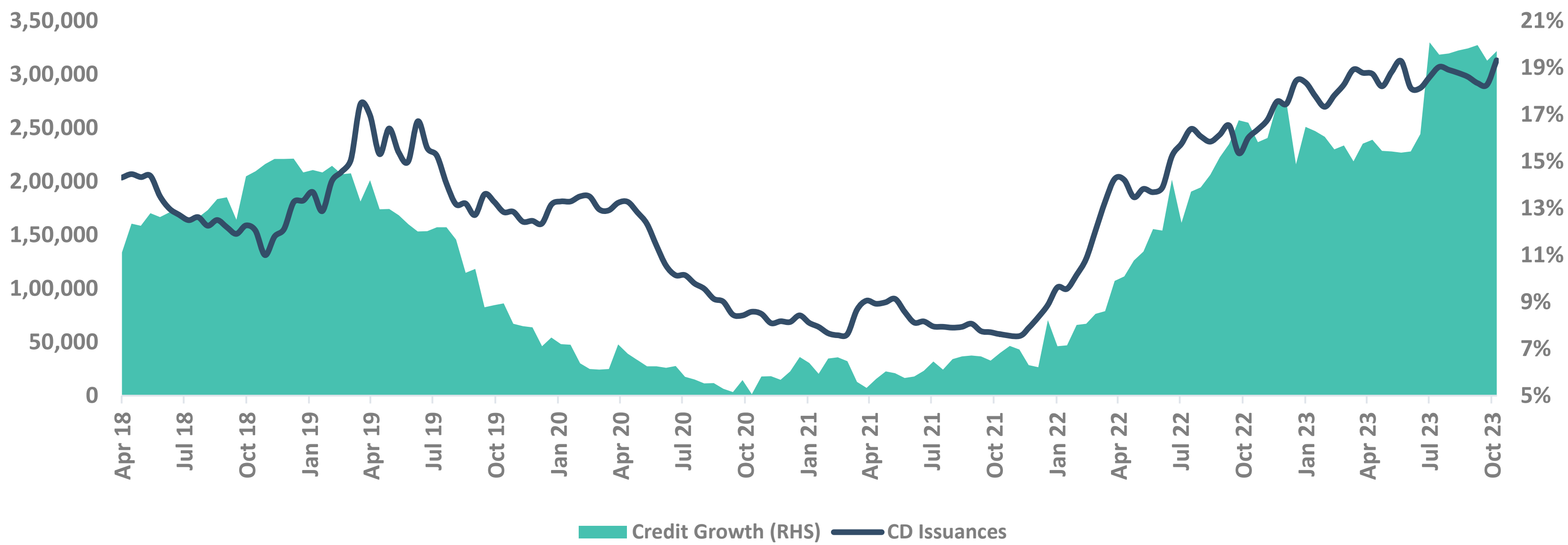
Source – Bloomberg, RBI, *Internal Estimates

G-Sec – Government Securities; CIC: Currency in Circulation

Well matched demand supply has money market rates range bound so far

- High credit growth has contributed to increase in Certificate of Deposits issuances over the last year
- Nearly ₹ 2.9tn CDs are outstanding; up 15% YoY. CD rates have moved up to ~7.65% – 7.70% - nearly 15bps increase YoY
- With well matched demand from flows in money market categories, we expect rates to remain range bound

Credit Growth (%) vs CD Outstanding (in Rs Cr)

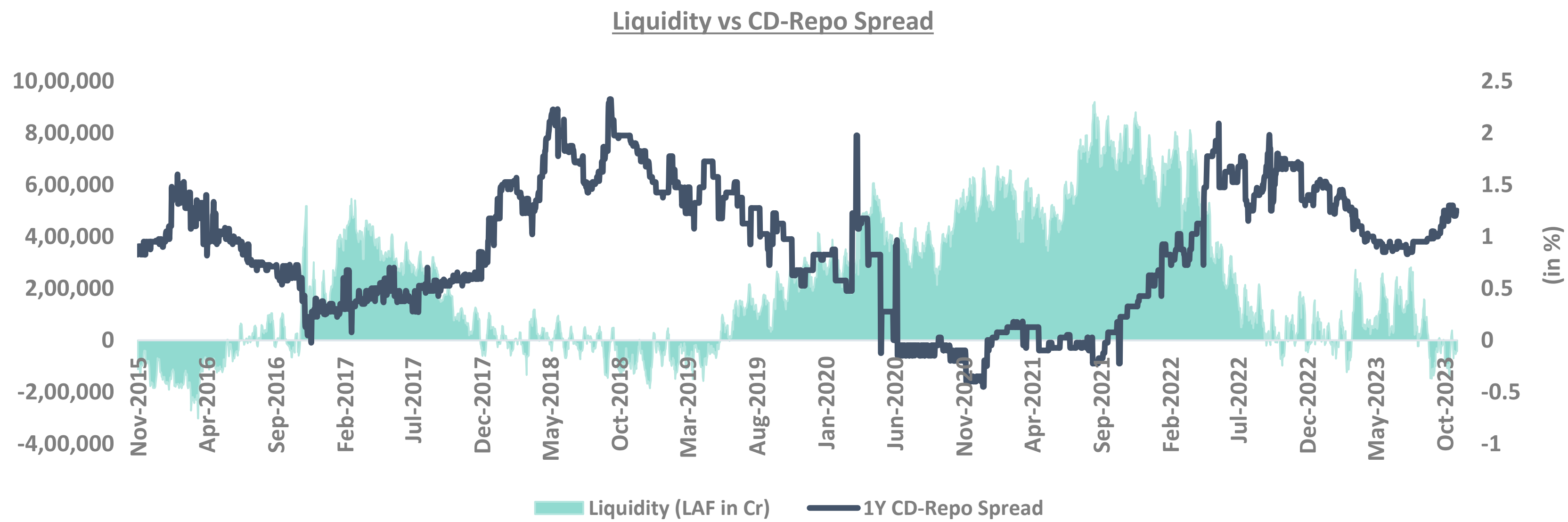


Takeaway:
With supply expected to be at current levels, demand from mutual fund participants to be the key determinant of money market yields

CD: Certificate of Deposits

With money market rates anchored, play for accrual

- **Durable liquidity comfortable at ~₹ 2.6* tn, nonetheless banking system liquidity remains in deficit**
- **Money market rates are closely linked to banking system liquidity**
- **We expect neutral banking system liquidity, keeping money market rates anchored at existing levels**



Takeaway:
Our current strategy is to gain accrual at elevated levels as we expect money market rates to remain range bound

DSP

*Internal Estimates

CD: Certificate of Deposits

What else

that

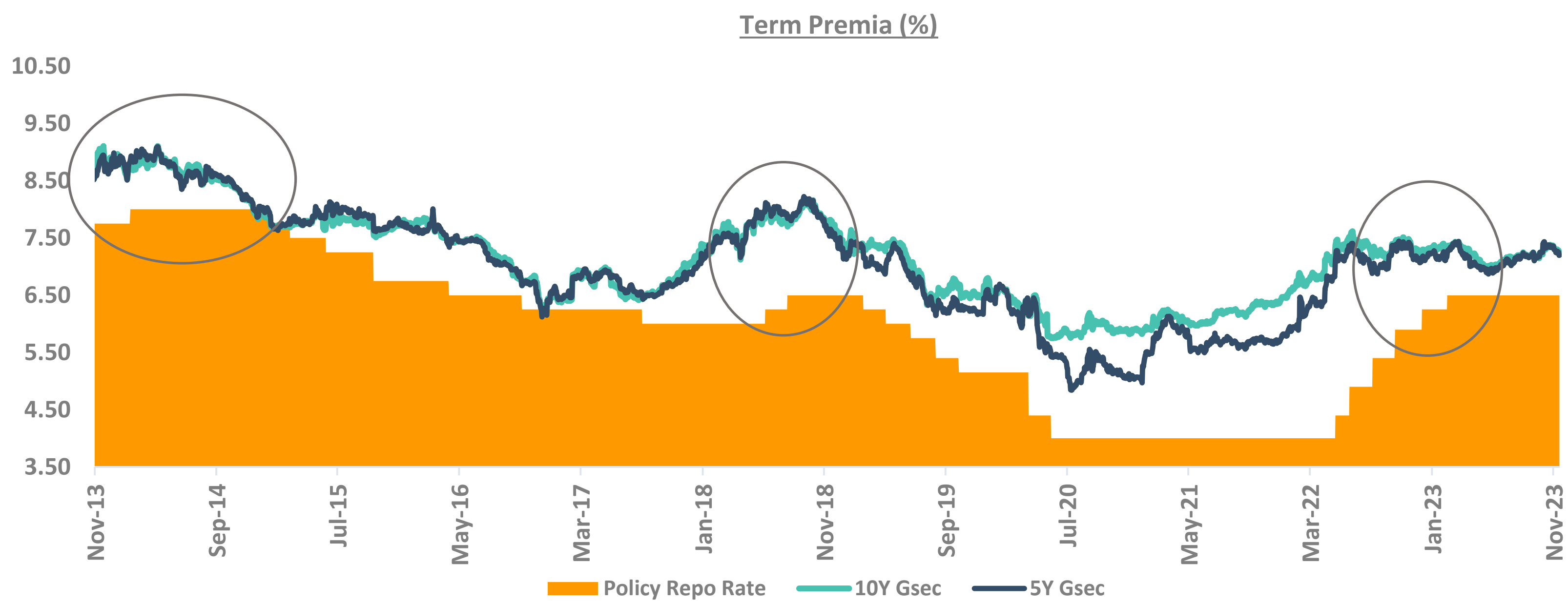
can’t be bunched up

Term premia is still high

- **This slide is the additional reason why we have a strong long bias – Valuations**
  - Even though, most arguments in our presentation indicate short term neutral view

- **Even if RBI hikes (unlikely and even then, probably last hike)…**
  - The spread with 5-Year IGB is 70bp!
  - Take away covid (hikes were expected) and reverse demonetization: currently the spread is neutral…
  - …then price in future rate cuts in FY25 (as in 2014-2017 and 2019) – suddenly bonds are a good buy

- **Since last DSP converse, domestic data has remained favourable and US data has weakened. The odds remain in favor of purchase.**



Takeaway:
India term premium is still high.

Source – Bloomberg

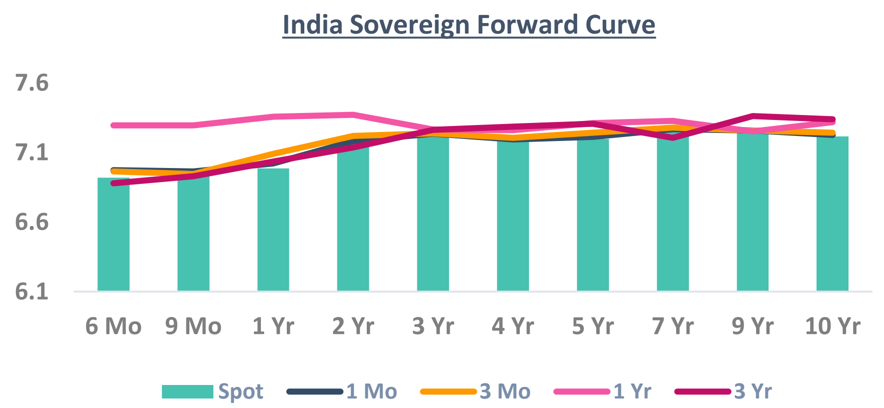
DSP

RBI: Reserve Bank of India

DSP FI Framework checklist

Drivers	1Y	5Y	10Y	>10Y	Remarks
Monetary Policy	**Neutral**	**Neutral**	**Neutral**	**Neutral**	
Inflation	Neutral	Neutral	Neutral	Neutral	Oct print was below 5% mark and core continued to moderate. Upside risks remain
Growth	Neutral	Neutral	Neutral	Neutral	Resilient growth so far; divergent trends emerging now
CAD/BOP/ Currency	Neutral	Neutral	Neutral	Neutral	External sector pressures low, however, EM reaction makes rupee vulnerable
Fiscal Policy	**Positive**	**Positive**	**Positive**	**Very Positive**	
Supply	Positive	Positive	Positive	Positive	H2FY24 has higher issuances in longer tenor; SDL issuances to have limited impact
Demand	Neutral	Neutral	Neutral	Positive	Banks demand should lessen, yet sufficient to absorb supply
FPI Flows	Neutral	Neutral	Neutral	Neutral	Passive flows only in the next year
Global	**Mildly positive**	**Mildly positive**	**Mildly positive**	**Mildly positive**	
Global yields	Mildly Positive	Mildly Positive	Mildly Positive	Mildly Positive	US data has finally weakened
Geopolitics	Neutral	Neutral	Neutral	Neutral	Geopolitical risks have abated
Commodities	Neutral	Neutral	Neutral	Neutral	Risks balanced
Others	**Mildly Negative**	**Neutral**	**Neutral**	**Neutral**	
RBI Regime	Neutral	Neutral	Neutral	Neutral	RBI will be influenced by Fed action
Miscellaneous	Mildly Negative	Neutral	Neutral	Neutral	RBI’s hawkish stance on liquidity (OMO sales)
Total	**Positive**	**Positive**	**Positive**	**Positive**	

DSP Duration decision: Negative data priced in. Valuation attractive



The chart shows how much expected yield fall/rise is already priced in the current curve.

Large gap between the current yield and forward yield shows that yield change is priced in – and thus yield change will not give capital gain/loss.

Similarly small gap means that the market is not pricing change in yields.

Market expects yield curve to remain flat

- The future rate curve is close to current yield curve, expecting yields to remain range bound

Maturity	1Y	5Y	10Y	>10Y	Remarks
What's expected (Total)	**Positive**	**Positive**	**Positive**	**Positive**	**From previous slide**
Is expectation (above row) priced in ?	Yes	Yes	Yes	Yes	At current yields levels (after recent rise) the higher rates have been priced in.

Source – Bloomberg; as on 16/Nov/23

We have discussed duration and yield movement.

How do we choose corporates and credit?

DSP Asset Allocation: Corporate bonds spreads wide

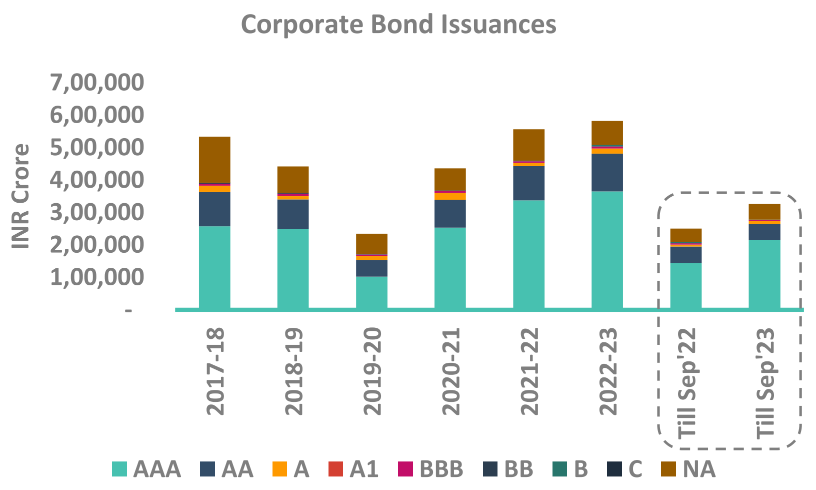
ASSET ALLOCATION

➢ Supply has remained manageable so far

- H1FY24 issuance at ~1.3x of H1FY23 led by AAA rated segment
- Supply in Oct remained on the lower side at ~40k crores

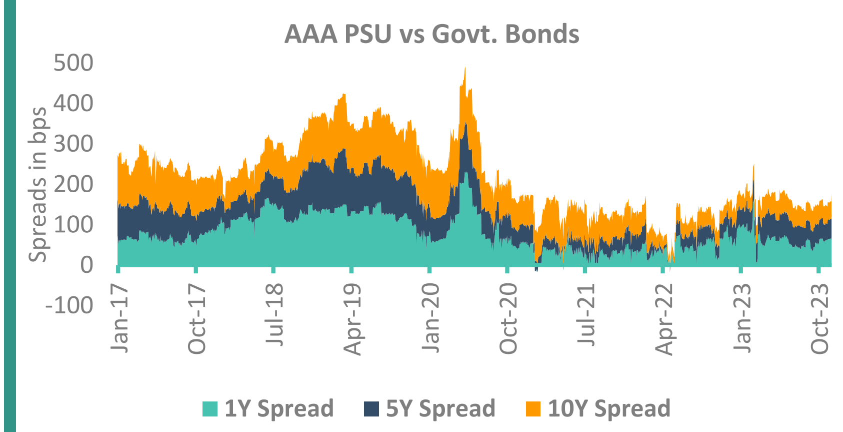
➢ New NBFC regulations to lead to more issuances

- NBFC to shift part borrowing to bonds form bank loans
- Will lead to rise in NBFC spreads of some companies



➢ The corporate bond spreads are reasonable

- 2-5Y NBFCs providing steady accrual
  - ✓ But tight liquidity pressures remain
- AAA PSU Spreads remain to be in the narrow band of 55-60bps
- Spreads in short papers may remain elevated,
  - ✓ We still like long bonds: demand from insurance, PF



Takeaway:
Corporate bond spreads near their long term average, spread curve flat.

Source – Bloomberg, CCIL, Internal

PSU: Public Sector Undertaking, NBFC: Non-Bank Financial Companies

DSP Credit Investment Process – Focus on Governance

Credit evaluation

- Macroeconomic & Industry Outlook
- Promoter /Management Reference Check
- Business Profile & Market Strategy
- Financial Statement Analysis
- Fund Raising Strength

Decision

- Internal Credit Rating Model
- Credit Committee: Limit approvals
- Fund Manager: Investment Decision

Monitoring

- Material Events
- Early Warning Indicators
- Management Guidance
- Movement in Spreads
- Change in Investor profile

Information sources: Financial results, Management Discussion, Rating Agency Feedback, Sell Side Research, Equity analyst feedback, Lender's feedback, etc.

CREDIT PROCESS

DSP Credit view on sectors

Sector	Cash Flow Strength	Balance Sheet Strength	Outlook	Remarks
Automobile and Auto Components	🟢	🟢	🟠	Growth depends on the segments e.g. SUV (doing better) vs small cars, 2W higher end doing better than lower (rural demand poor).
Capital Goods	🟢	🟠	🟠	Infrastructure spending by the Government has supported companies.
Chemicals	🔴	🔴	🔴	For export-oriented businesses, inventory destocking as supply chains normalize and global slowdown are impacting profitability. Chinese oversupply is also to be watched. However, the longer-term story is intact- steady demand and India as a manufacturing base.
Construction, Metals	🟢	🟠	🟠	Commodity cycle has by and large been stable. Margins are broadly intact as any price volatility is also seen with lower raw material prices. Cement companies are expanding capacity and for metals, pick up in Chinese economy is important to sustain prices.
Consumer Durables	🟢	🟢	🟠	Commercial demand has been strong given the pickup in infra segment. Retail remains largely stable with churning in the market share
Consumer Services	🟠	🟠	🟠	All eyes are on the festive demand. So far it has been weak due to high inventory levels.
FMCG	🟢	🟢	🟠	Volume growth has been weak only overall. But balance sheet and cashflows are strong
Financial Services	🟢	🟠	🟠	Strong credit cycle and better underwriting practices have resulted in stronger balance sheets and ability to withstand downturn. While pockets of strong growth are causing concern (e.g. personal loans), as long as sensible pricing remains, the Companies should be able to withstand cyclical shocks.
Media, Entertainment & Publication	🔴	🟠	🟠	Exposure only towards are large private conglomerate and comfort out of its parentage as well as leadership position
Oil, Gas & Consumable Fuels	🟢	🟢	🟠	As end fuel prices are fixed, profitability of OMCs depend on price of oil which has been volatile. However, companies have built in strong cushions in H2FY23 and H1FY24. Higer refining margins are helping refineries. Capex for state owned PSUs needs to be watched.
Power	🟢	🟠	🟠	Power demand supply remains favorable, especially in peak load demand, resulting in a favorable cycle for power companies and equipment suppliers (e.g. transmission grid). Key risk remains political as States still do not appear to be charging proper prices for electricity - a fundamental flaw in India. However, with Central Government initiatives, receivables for power companies have declined.
Realty	🟢	🟠	🔴	Strong real estate cycle has positively impacted residential companies, but lack of clarity on the new SEZ bill and global slowdown has impacted commercial real estate.
Telecommunication	🟢	🟢	🟠	Virtually a two company story in India, we expect credit profiles of those two to remain solid.

Done with our market view framework?

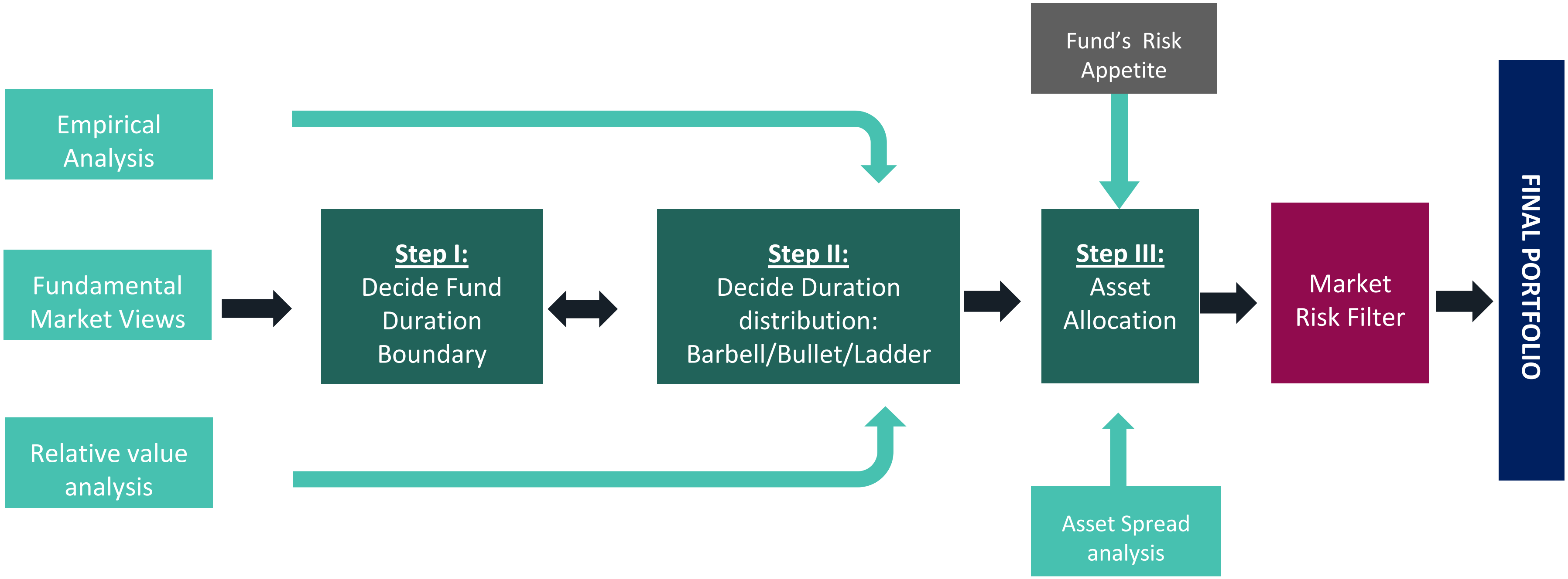
Now

Our Portfolio creation framework

DSP Portfolio Creation: Multi-step process

PORTFOLIO CREATION

DSP Fixed Income Funds follow a defined methodology for fund portfolio construction



- We apply market risk filter which can help the Fund Managers not to take extreme risks. Thus, Value at Risk is limited by ensuring the positions are balanced.

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Investment approach / framework/ strategy mentioned herein is currently followed & same may change in future depending on market conditions & other factors.

Key Risks associated with investing in Fixed Income Schemes

Interest Rate Risk - When interest rates rise, bond prices fall, meaning the bonds you hold lose value. Interest rate movements are the major cause of price volatility in bond markets.

Credit risk - If you invest in corporate bonds, you take on credit risk in addition to interest rate risk. Credit risk is the possibility that an issuer could default on its debt obligation. If this happens, the investor may not receive the full value of their principal investment.

Market Liquidity risk - Liquidity risk is the chance that an investor might want to sell a fixed income asset, but they're unable to find a buyer.

Re-investment Risk: If the bonds are callable, the bond issuer reserves the right to "call" the bond before maturity and pay off the debt. That can lead to reinvestment risk especially in a falling interest rate scenario.

Rating Migration Risk - If the credit rating agencies lower their ratings on a bond, the price of those bonds will fall.

Other Risks

Risk associated with

- floating rate securities
- derivatives
- transaction in units through stock exchange Mechanism
- investments in Securitized Assets
- Overseas Investments
- Real Estate Investment Trust (REIT) and Infrastructure Investment Trust (InvIT)
- investments in repo of corporate debt securities
- Imperfect Hedging using Interest Rate Futures
- investments in Perpetual Debt Instrument (PDI)

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