"The essence of investment management is
The management of risks, not the management of returns"
- Benjamin Graham

The Indian markets, after briefly moving independently, started tracking the US yields (slide #29). Reason? Surprise announcement of OMO by RBI. While the OMO announcement was meant to suck out liquidity, but the collateral damage to the yield curve was substantial. RBI's statement that 3-month vs 10-year Indian yields were "stable" gave more food for thought about the underlying reasons for OMO.

However, when one notices that Rs. 2 lac cr. Of bond redemption in Nov/Dec will increase banking liquidity, it is obvious that the RBO OMO will align with redemptions.

What is also obvious is the reasons for tighter banking liquidity, despite the structural liquidity being in surplus. Govt is holding cash for the redemptions.

Finally it is obvious why Banks SLR requirement is so high. It will reduce sharply by about 1% when redemptions occur (Slide #26).

So what now for yields?

We believe that the yield curve will be more aligned to the US yields for short term. OMO will bring volatility. However, large part of OMO is already priced in.

We continue to believe that the Indian yields will gravitate lower for the next few quarters. We are not taking a call on growth and inflation – which even central banks are not able to project. Our view stems from fact that the demand for Indian bonds remains far stronger than the issuances.

While it may seem that the Indian yields have risen recently – but the rise has been just to the tune of 10bp. Yields may remain volatile at these levels, but we are nonetheless closer to the peak yields in our opinion.

In such volatile times, it is preferable not to time the markets.

We prefer to maintain a core long position in our funds. Nonetheless, markets are volatile, and one needs to do risk management, along with express views.

Thus, we prefer to be nimble and add or reduce our core position through the whiplash market movement. We also intend to reduce risks going into events and news, to remove the element of chance. Afterall, it is as important to benefit from yield fall as it is to avoid being trapped in another global yield spiral upwards.

What segment do we like the best?

We prefer longer tenure bonds as (i) RBI does not owns these bonds to sell in OMO, (ii) JPM bond index will include reasonable size of these bonds, (iii) demand from PF and Insurance for these bonds remains upbeat.

We also like upto 1 year segment: (i) Govt redemptions will add liquidity, and (ii) spreads are already wide.

What are the major risks to our position?

US yields uptick. US yields are volatile. They swing wildly, and the narratives change daily. The narratives and volatility seem to feed each other – on both sides. The US yields remain the biggest concern.

OIL. Gaza war has made oil vulnerable, even though it has remained stable so far. It may take a small spark to create a fire. While we are not worried, yet we are cognizant of binary risks.

Rupee. Rupee has been best performing currency. And that worries us. It is performing because RBI is propping it. The last time rupee when did so well in global meltdown, it led to dramatic crash in rupee and hikes in rates. We are not in similar scenario, but RBI and banks have lesser dollars – and world is uncertain. We remain concerned on rupee and track it very closely.

Oct 2023

DSP

#INVESTFORGOOD

Still Long

Clouded by global uncertainties

DSP CONVERSE

Our Framework

Monetary Policy

Inflation
- Sep print of 5.02% much lower vs the expectations
- Led by vegetable and fuel & light
- Weather related risks remain
- Core inflation moderated sharply to 5.02%

Growth
- Domestic activity is resilient
- PMI remains in expansionary zone
- GST collections continue to indicate 10-11% YoY growth

Currency/CAD/BOP
- External sector pressures remain low, but…
- Oil is higher/Discount for Russian oil & fertilizer no more there/INR vulnerable by EM reaction
- 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
- 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 continues to weaken, but less than expected
- Despite narratives being on the either side

Geopolitics
- China/US trade war can cause supply disruption
- Ukraine Russia conflict is not over yet
- Israel-Palestine Conflict

Commodities
- Price risks are evenly balanced

Others

RBI Regime
- Higher for longer rates
- Shift from Arjuna's eye to 4% CPI target
- Focused on using liquidity tools to manage stance
- Tail risks could emerge from large FOMC action

Misc.
- No more surplus liquidity
- Election related risks on card
- RBI tightens HTM norms

Takeaway:
Stable domestic macro. Highly uncertain global outlook

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; OMO: Open Market Operation; FPI: Foreign Portfolio Investment; FOMC: Federal Open Market Committee; I-CRR: Incremental Cash Reserve Ratio; PMI: Purchasing Managers' Index; GST: Goods and Services Tax; NSSF: National Small Savings Fund

Still Long! Why?

Comfortable demand-supply metrics

Tail Risks from (currency/oil/global yields/RBI OMO sale)

View Summary: Still Long

Our Strategy: We are still long

Indian yields remained stable, despite US yields rising up. It finally took RBI OMO announcement to raise the yields further. We believe this has made Indian yields much more sensitive to global yields – and this can be evidenced from the high correlation of India and US yields post RBI announcement.

However, domestic factors are still strong. Low Inflation. Stable Growth. High demand for bonds, notwithstanding RBI sales. Nothing has changed domestically, apart from RBI sales. And that too has been priced in domestic yields.

We prefer remaining long. But not all-in. There is high volatility globally, and India is nor more as isolated as a month back.

***For money markets investment:** Even as the RBI is focused to keep liquidity stance aligned with the policy stance, well-matched demand supply would keep money market rates range bound. We will play for accrual across our money market category funds and stay invested.*

➢ Reasons for our view

1. **Demand-Supply** remains well-matched. There is high demand for bonds in India. In a few months time bond inclusion will add to the demand.
2. **India term premium** is still high, especially considering the fiscal strength. With benign rate outlook, current yields are attractive.

➢ Risks to our view

1. **Its too volatile to make a conviction view?** Volatile US yields, volatile oil. Rupee is not volatile – but one never knows when it can buck the trend. Anything can happen. It is playing poker. One can take a bet with cards on hand, but it is difficult to anticipate the next draw. At such high yields, we play odds that higher demand will keep yields clamped.

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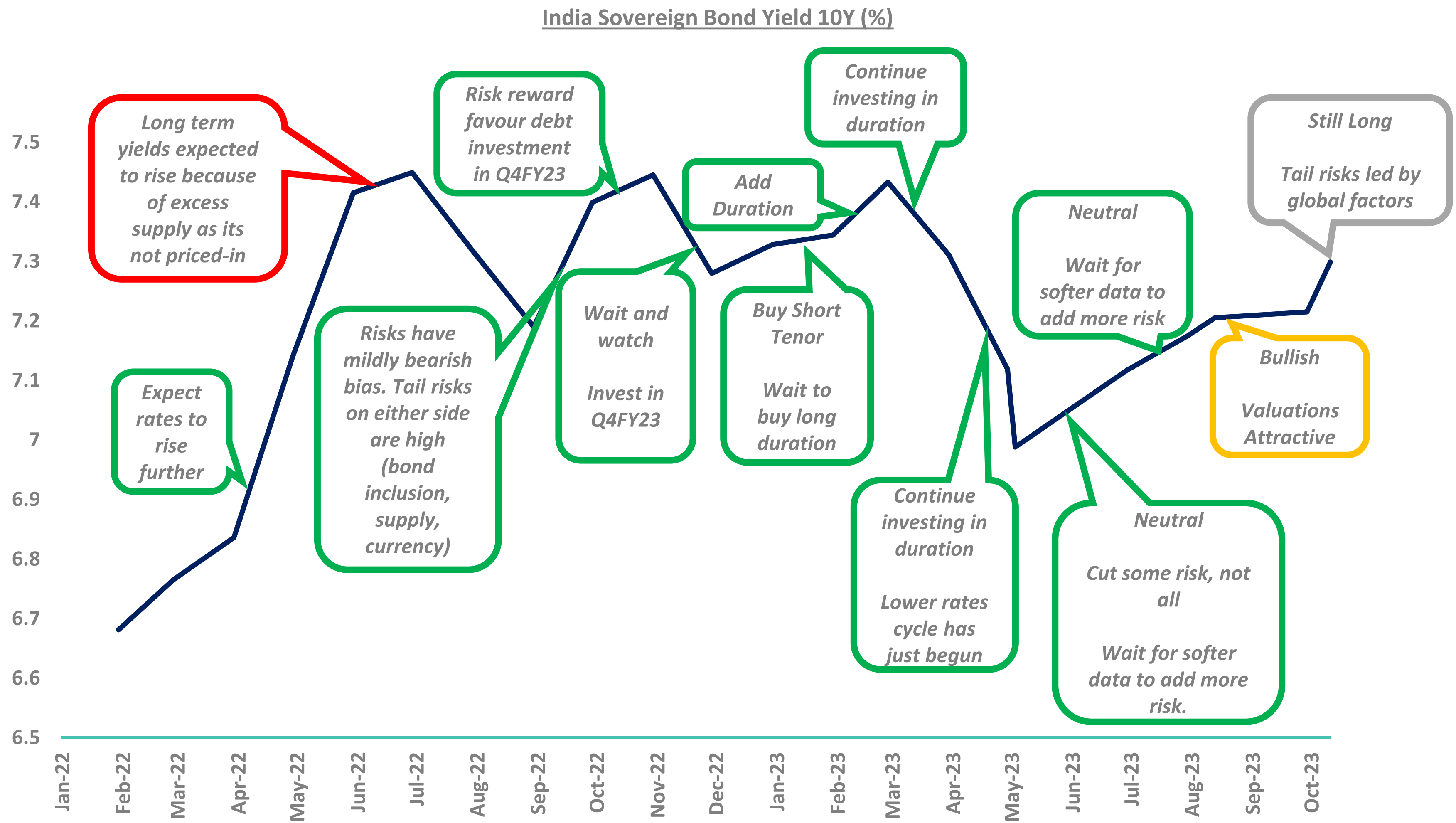
G-Sec: Government Securities; CPI: Consumer Price Inflation; FED: Federal Reserve; RBI: Reserve Bank of India; CRR: Cash Reserve Ratio

Let’s revisit our rates call trajectory

TRAJECTORY



Source – Bloomberg

When view gone correct

View gone wrong

View uncertainty playing out

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To start with,

Recap of events since last release.

WHAT HAS CHANGED

RBI focus on liquidity (ICRR, intent of OMO sales)

India's inclusion in JPM bond Index

CPI has cooled-off

Hawkish hold by Fed, Mixed US data

ECB signals end of hike cycle

RBI's not-so-status quo policy

- ➢ **REPO rate unchanged at 6.5%**

- ➢ **Stance retained at "focused on withdrawal of accommodation"**
  - ✓ By a majority of 5 out of 6 members

- ➢ **Inflation Projections retained at 5.4% for FY24**
  - ✓ Revised down by 10bps to 5.6% for Q3FY24
  - ✓ Improved near term outlook (vegetable price correction and LPG price reduction)
  - ✗ Future trajectory uncertain due to lower reservoir levels, el-nino conditions, volatile global energy and food prices
  - ✗ Re-iterated inflation target at 4% and not 2%-6%

- ➢ **Growth Projections retained at 6.5% for FY24**
  - ✓ Buoyancy in services, revival in rural demand, Govt's thrust on capex and healthy corporate & bank B/S
  - ✗ Headwinds from geopolitical tensions, volatile financial markets and energy prices

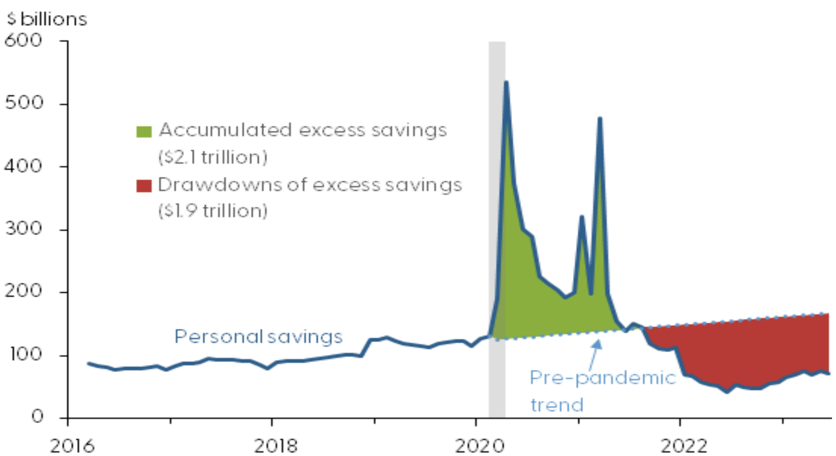
- ➢ **Other key highlight(s)**
  - ✓ May consider OMO-sales to manage liquidity

RBI: Reserve Bank of India; GDP: Gross Domestic Product; B/S: Balance Sheet; OMO: Open Market Operations

Depleting excess savings and hawkish dot plot

➢ US household savings: Excess no more

- Out of USD 2.1tn of accumulated savings, USD1.9tn already drew-down as of Jun'23
- Lesser savings could result in lesser retail spending / inflation



➢ FOMC delivered a "hawkish hold"

- Both 2024 and 2025 median dots revised 50bps higher
- Higher for longer theme re-instated
- Upgraded the economic growth description to "solid" vs "moderate" in the previous policy
- Downgraded the job growth description to "have slowed" vs "have been robust" in the previous policy

FOMC Federal Funds rate forecast

Meeting Date	2023	2024	2025	2026	Longer run
Jun'22	3.8	3.4			2.5
Sep'22	4.6	3.9	2.9		2.5
Dec'22	5.1	4.1	3.1		2.5
Mar'23	5.1	4.3	3.1		2.5
Jun'23	5.6	4.6	3.4		2.5
Sep'23	5.6	5.1	3.9	2.9	2.5

Takeaway:
Higher for longer theme to continue even as the data remains mixed

Source – US Fed Reserve, Federal Reserve Bank of San Francisco

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Now our framework

And

What we track

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- External sector pressures remain low, but…
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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; OMO: Open Market Operation; FPI: Foreign Portfolio Investment; FOMC: Federal Open Market Committee; I-CRR: Incremental Cash Reserve Ratio; PMI: Purchasing Managers' Index; GST: Goods and Services Tax; NSSF: National Small Savings Fund

Resilient domestic economic activity

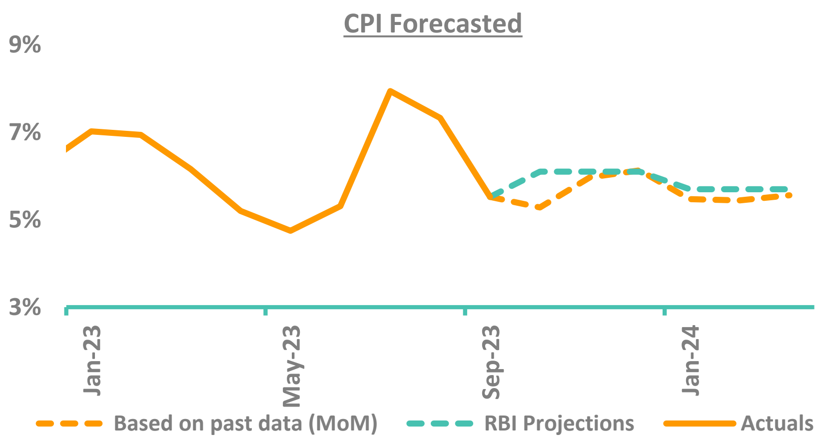
Expansion in urban demand while rural showing signs of revival

Sep CPI moderated sharply, core now at 4.5%

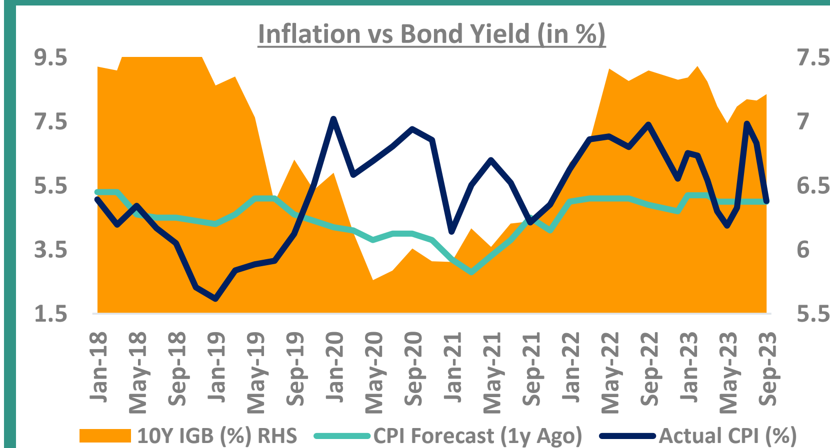
To consider OMO sales to manage liquidity

Softer-than-expected inflation print, upside risks remain

- **Softer than expected print for Sep at 5.02%**
  - Sequential contraction of 1.1% (-0.1% in Aug)
  - Led by vegetable prices and fuel & light component (LPG price cut)
  - Crude and pulses/cereals prices remains a risk
    - ✓ Even as the vegetable prices moderate further
- **Core CPI moderates sharply to 4.5%**
  - Flat sequentially (+0.4% in Aug)
- **Watchful of impact of el-nino on rabi sowing**



- **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 weather related risks and increase in crude/cereals/pulses prices

DSP

Source – Bloomberg, RBI, Internal

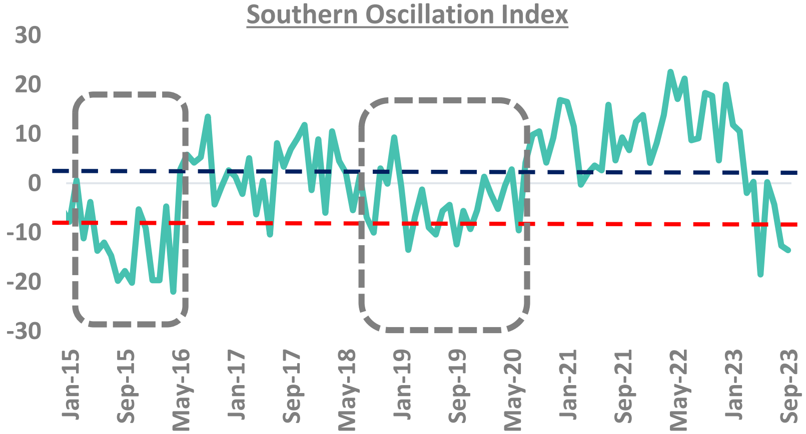
CPI: Consumer Price Inflation; RBI: Reserve Bank of India; IGB: India Government Bond; LPG: Liquefied Petroleum Gas

El Nino a very high possibility albeit may not be a major risk to inflation

➢ El Nino is a possibility, but impact dubious

- Southern Oscillation Index value lower than −7 often indicate El Nino episodes.

- Low reservoir levels (12th Oct)
  - ✓ Reservoir live storage at 132.04 BCM (at 82% of the live storage of corresponding period last year and 94% of storage of average of last ten years)



➢ Rice (including paddy) stock at adequate levels
➢ Wheat stocks are on the lower side

Table 1 (lac tonne)	FY15	FY16	FY20	FY21	FY22	FY23	FY24
Wheat							
Production Growth (YoY)	-10%	7%	4%	2%	-3%	6%	
Opening Stock (Oct)	**323**	**325**	**393**	**437**	**469**	**227**	**240**
Rice							
Production Growth (YoY)	-1%	-1%	2%	5%	5%	4%	
(Rice + Unmilled Paddy)							
Opening Stock (Oct)	**202**	**149**	**290**	**275**	**394**	**323**	**360**

➢ Overall Kharif sowing already higher vs last year, but pulses are on the lower side

Weekly Area Coverage under Kharif Crops (29th Sep'23)			
Crops	Area Sown (lakh Ha)		Inc/Dec
	2023	2022	
Rice	411.96	404.27	**1.90%**
Pulses	123.57	128.98	**-4.19%**
Coarse Cereals	188.02	184.77	**1.76%**
Oil Seeds	193.23	196.39	**-1.61%**
Sugarcane	59.91	55.66	**7.64%**
Total	**1,107.16**	**1,104.79**	**0.21%**

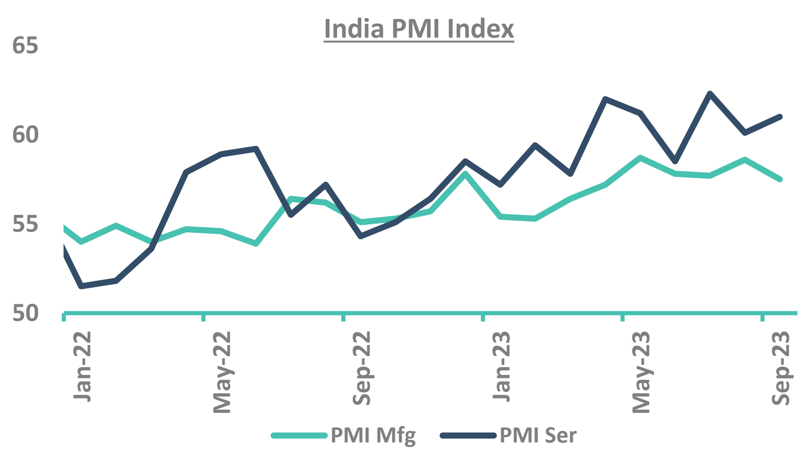
Takeaway:
El Nino risks remain, however, not a major risk to inflation

DSP

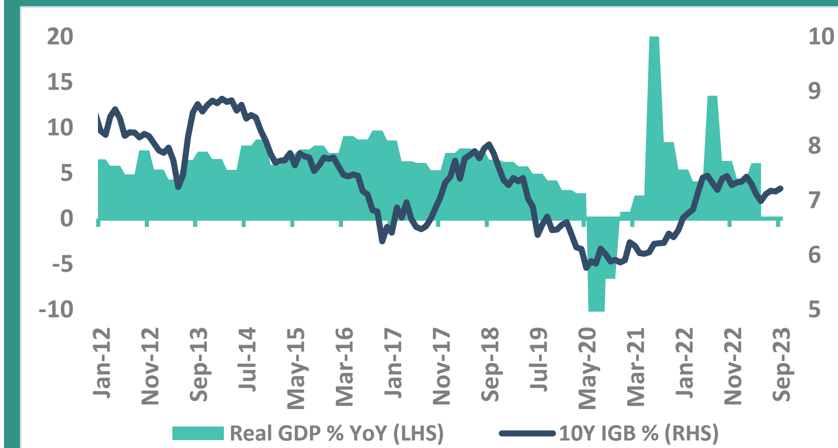
Source – FCI, Australian Govt BoM, NFSM

Will global slowdown test domestic growth: No signs right now

- **Domestic growth data is still robust**
  - PMI continues to be in expansionary mode
    - ✓ Manufacturing PMI softened for Sep
    - ✓ While Services PMI remained strong
  - GST collections at ₹ 1.63 tn; YoY growth at 10%
- **Loan growth still near decadal high**
  - Credit growth to large corporates slow at ~5% YoY
    - ✓ Led by infra segment
  - Retail and services segment remained robust



- **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 came in at 16.1%, in line with RBI projections



Takeaway:
Domestic growth seems to be resilient, festive demand set to provide further boost

DSP

Source – Bloomberg

GDP: Gross Domestic Product; PMI: Purchasing Managers' Index; GST: Goods and Service Tax; IGB: India Government Bond; Mfg: Manufacturing; MSME – Micro, Small & Medium Enterprises; RBI: Reserve Bank of India

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, 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

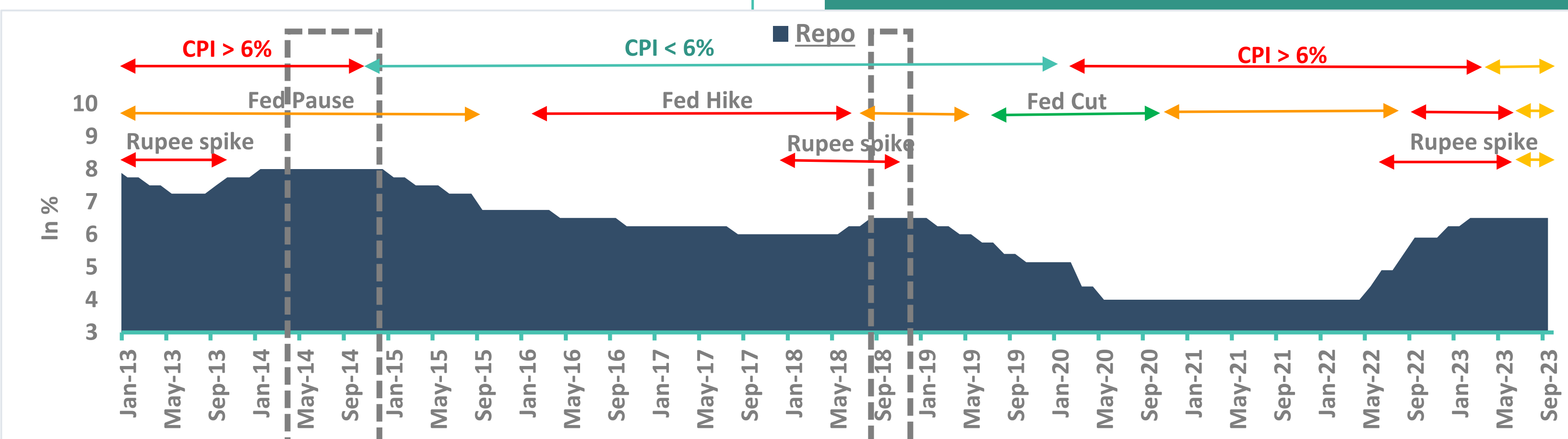
- Even though FED remains data dependent
- FED to remain on "WAIT and WATCH" mode

↔ 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 Q4FY23
- But EM currencies are weakening, and so has rupee



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

Source – Bloomberg

DSP

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

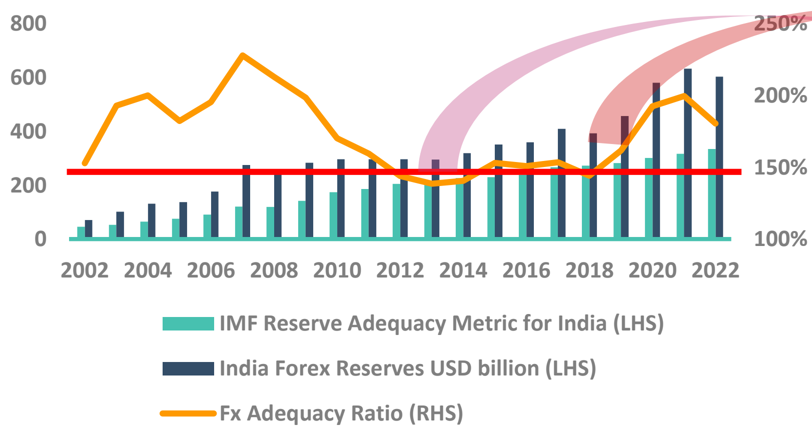
Can RBI Hike? Unlikely.

RBI Rate hikes are done for FX and FED (primarily), and CPI (at times)

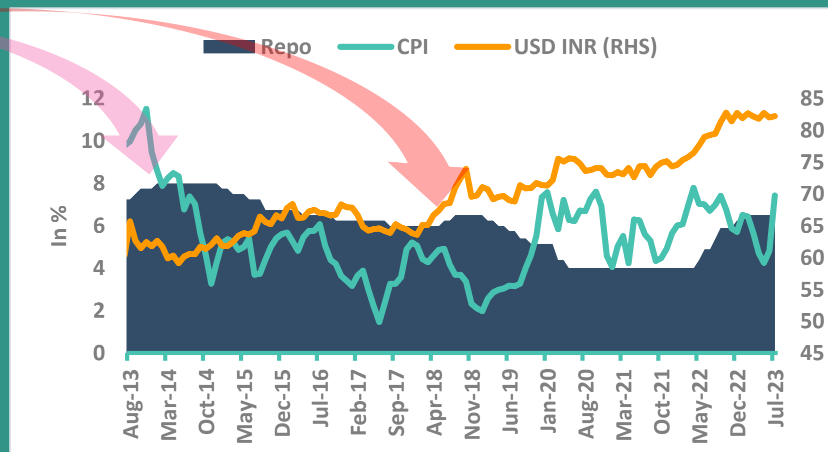
External sector metrics are worsening, but not yet a concern.

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

- **RBI FX reserves have reduced lately**
  - Forex reserves reduced to ~$587bn from $600b+
- **RBI FX Reserve / IMF FX adequacy ratio declined sharply**
  - Buffer of more than $85 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

DSP

Source – Bloomberg

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

Data has improved since last DSP Converse

CPI is lower, India included in JPM Bond Index, US data remains mixed

We reiterate what we said last time:

"*tail risks remain from any large FOMC action*"

Let's turn to Fiscal policy

Generally, it drives the long bond yields

It is reflected in demand/supply mismatch.

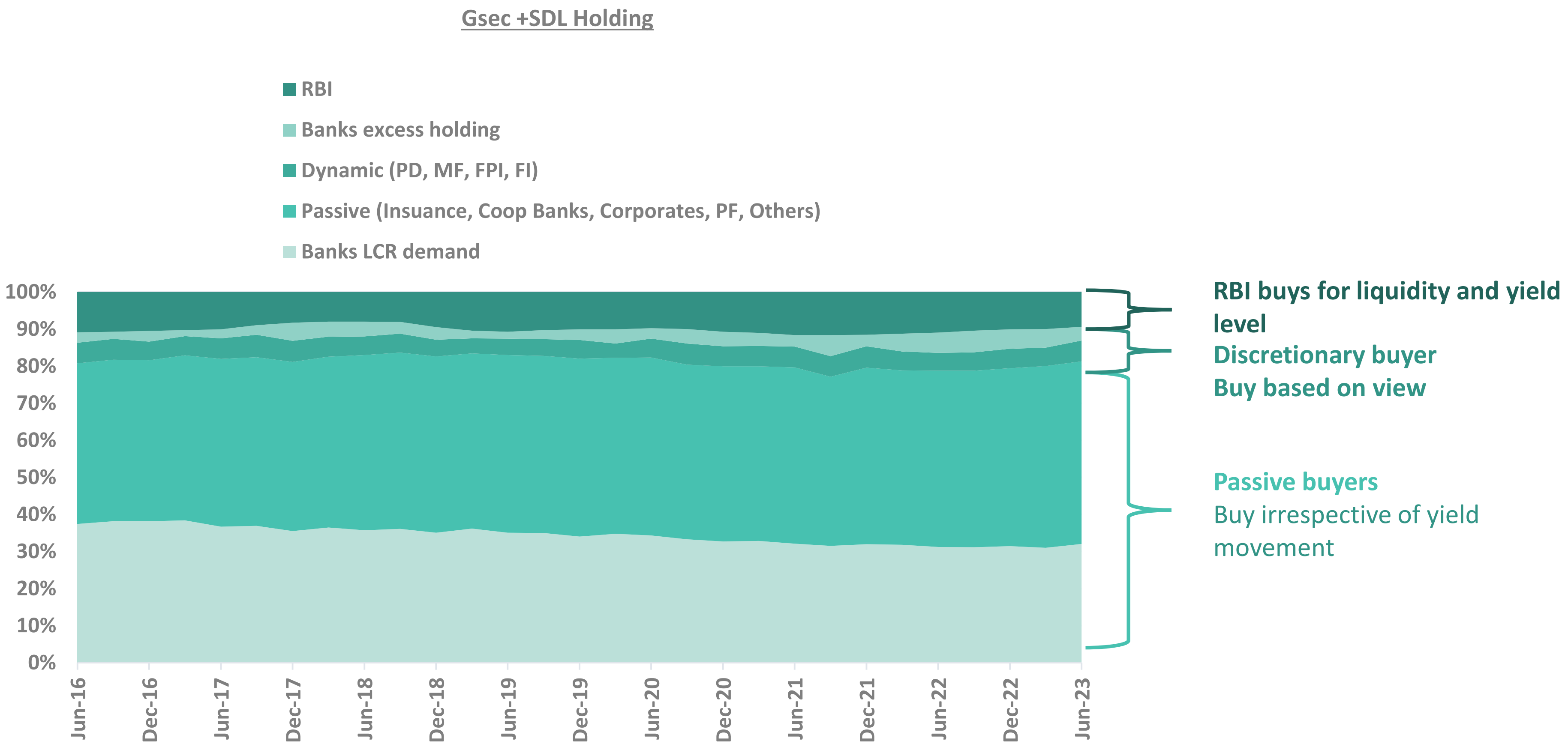
Fiscal policy is less of a driver right now – though election risks will precipitate in next few months

Only a small part of bond buyers are discretionary buyers

They drive yields

Supply fluctuation is borne by these buyers

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

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

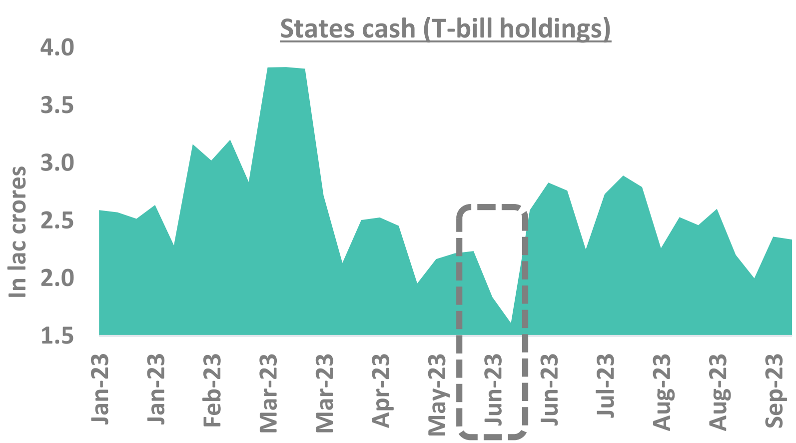
Comfortable supply/demand dynamics for FY24

But it will be bumpy ride

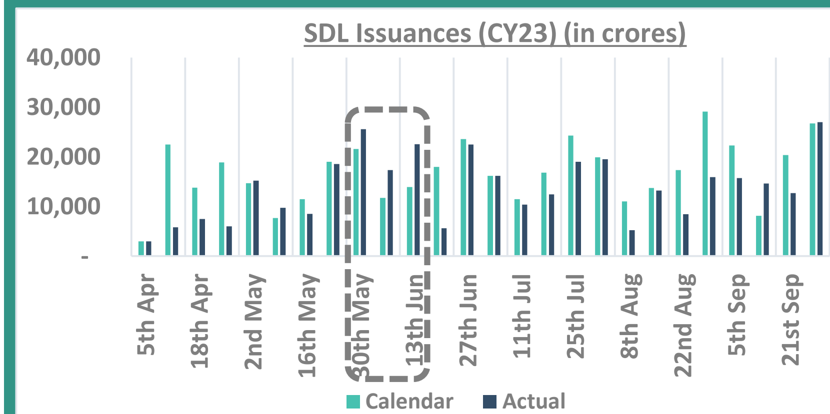
Last 6 months demand/supply has been rosy (latent purchases, low SDL issuances)

SDL supply only increases when states cash dip: Not so currently.

- **State cash balance is comfortably above 2tn**
- **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
  - H1 issuance ~18% lower vs the calendar amount
- **SDL issuance impact is expected to be limited**



Takeaway:
SDL supply may remain muted in FY24

Source – DBIE, RBI

FISCAL POLICY

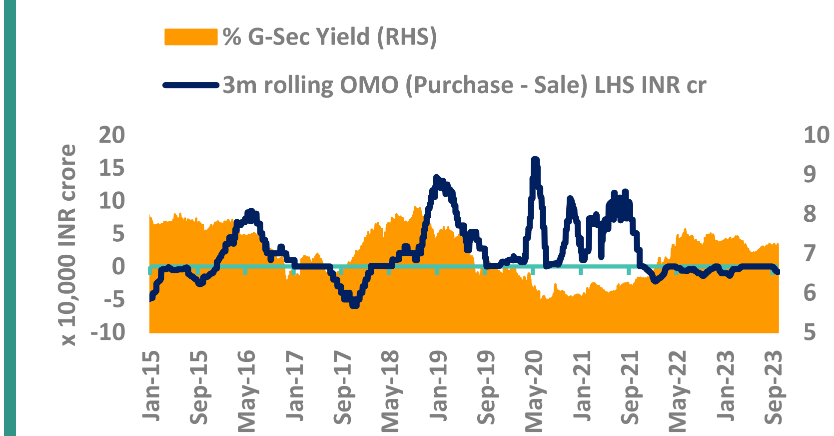
T-bill: Treasury Bill; SDL: State Development Loans

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 H1FY24**
  - But this includes bump of HDFC merger
- **Banks will continue to buy as SLR holding will fall**
  - Rs 2 lac cr of Gsec maturity will sharply reduce SLR holding
  - Natural NDTL growth will still lead to demand

Banks SLR (in %)(SCBs Investment-Deposit Ratio)

- **Yields track RBI OMO purchases**
  - Yields have strong correlation with RBI OMO
  - Demand/Supply mismatch is filled in by RBI
- **RBI announced OMO sell**
- **We expect Rs. ~50K cr of OMO sell**
  - Liquidity will ease and Govt redemption of Rs. 2 lac cr in Nov/Dec
  - But CIC increase due to (i) Festive season, (ii) state elections, and (iii) harvest, will reduce liquidity.



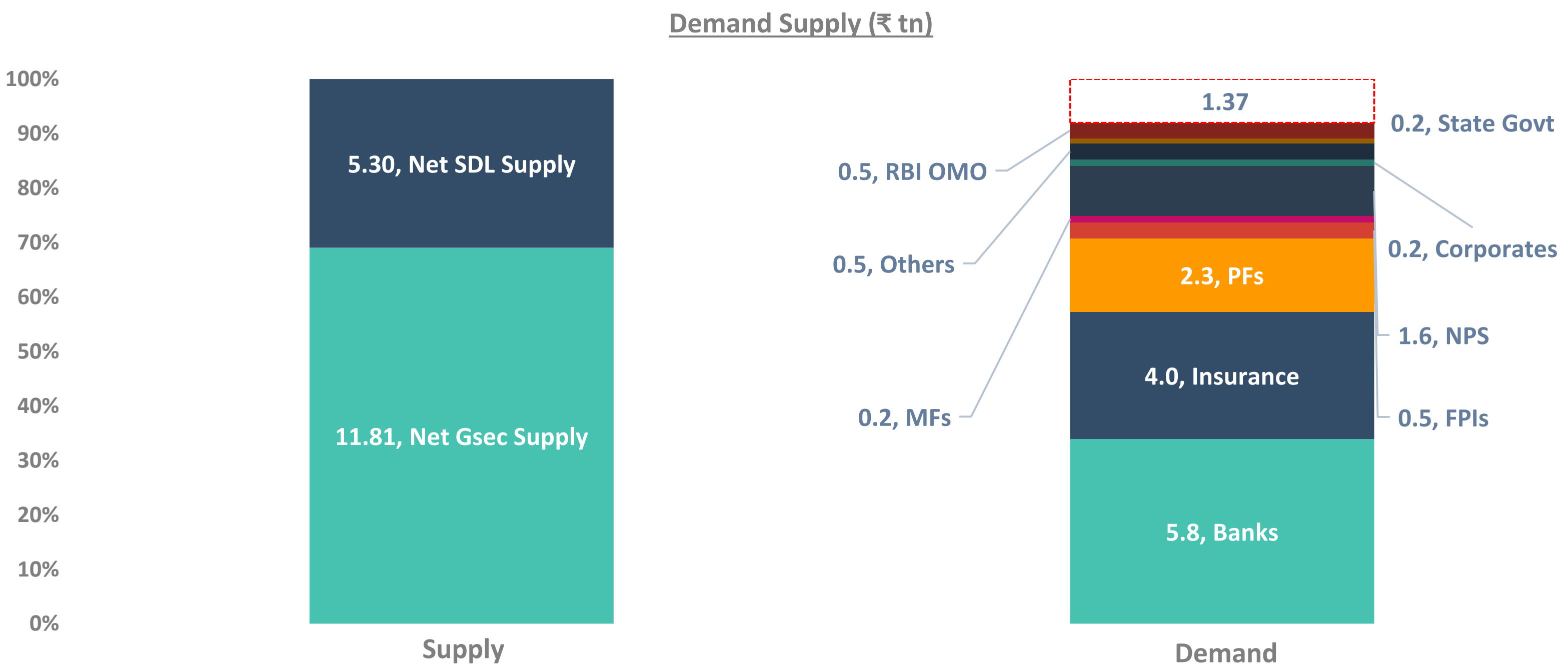
Takeaway:
Banks' probably lesser demand in future to be negative.

Source – Bloomberg, DBIE, Internal

OMO – Open Market Operations, SLR – Statutory Liquidity Ratio; G-Sec – Government Securities; RBI: Reserve Bank of India; FRA: Forward Rate Agreement; TRS: Total Return Swap

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 ₹ 1.37 tn is not very significant. Banks may sustain a SLR ratio of 30.5% (we have taken 30%)

Source – Internal, CGA

DSP

G-Sec: Government Securities; OMO: Open Market Operation; RBI: Reserve Bank of India; FPI: Foreign Portfolio Investment; NPS: National Pension System; MF: Mutual Fund; SDL: State Development Loans; SLR: Statutory Liquidity Ratio; PF: Provident Fund; EPFO: Employees' Provident Fund Organisation; NSSF: National Small Savings Fund

Impact of RBI OMO?

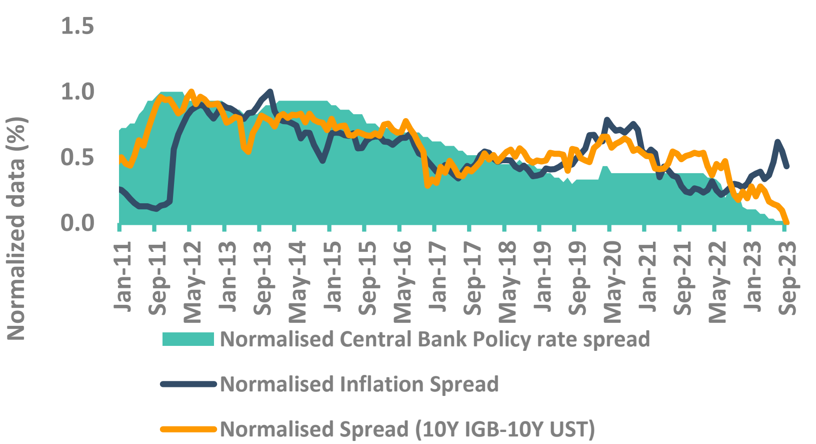
Indian yields have again started tracking Global yields.

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

Indian yields – Again dancing to the tune of US Yields

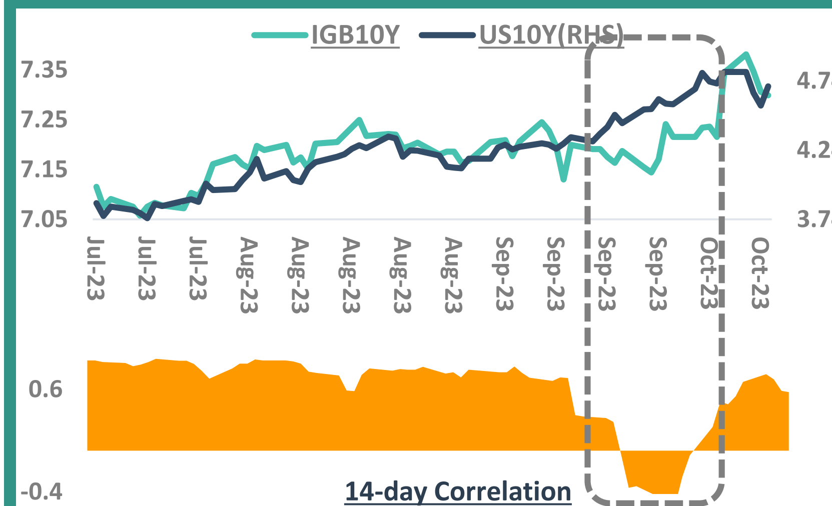
- **FOMC rate at 5.50% - more hikes at play?**
  - Incoming data shows a mixed picture
  - Tails risks of services inflation remaining sticky

- **Are spreads of US Treasury and Indian Govt. Bonds low?**
  - No, Bond yields difference mimics the inflation and policy rate differential.
    - ✓ 10Y yields seem to have priced in the inflation spread



- **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



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

DSP

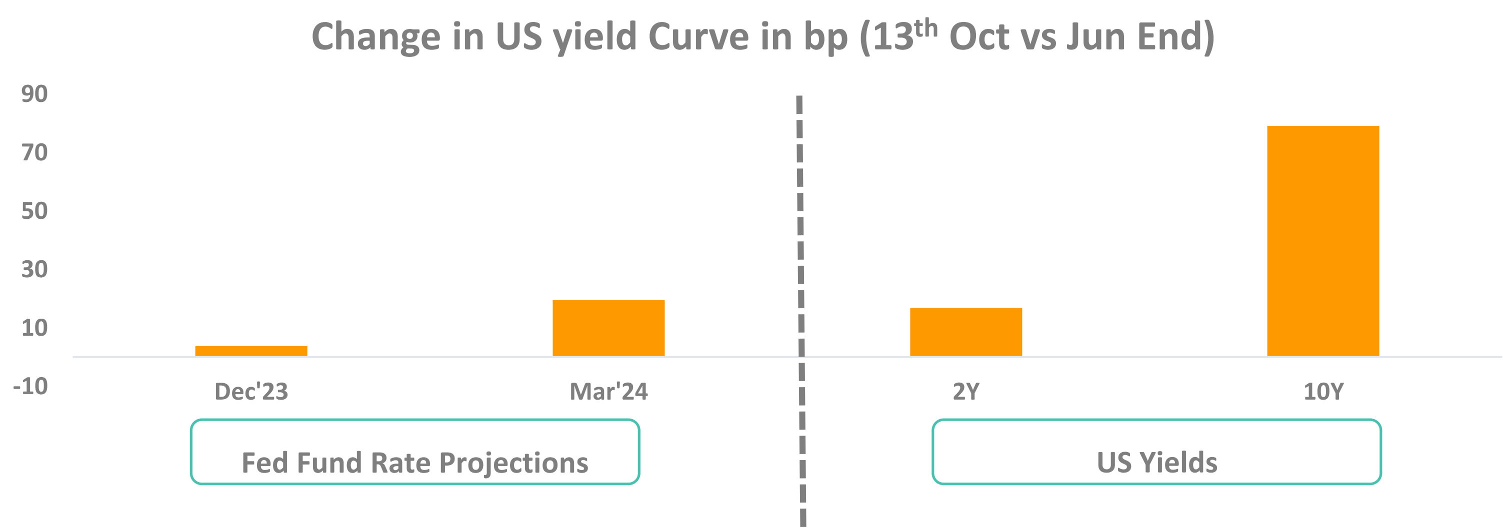
Source – Bloomberg, Internal

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

In US, macro data is not a concern: Supply and Fiscal deficit is

➢ US yield curve has bear steepened

- No major change in expectation of rate action by the FED
- However, longer end of the yield curve has moved up
  - ✓ Excess US fiscal supply, and demand constrained as Quantitative Tightening on
  - ✓ Partly reflects a "high for longer" view. Not totally – else 2 Year and 10 Year wouldn't have steepened so much.



Takeaway:
US yield curve impacted by higher for longer and demand-supply issues

Source – Bloomberg

DSP

Money Market Assessment Framework

System Liquidity

Currency in Circulation (CIC)
Seasonal increase in CIC to further drain out 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

Continuing credit growth to keep issuances of CDs by banks at current levels

Demand

Mutual funds demand stable

Extent of GOI borrowing through T-bills as expected

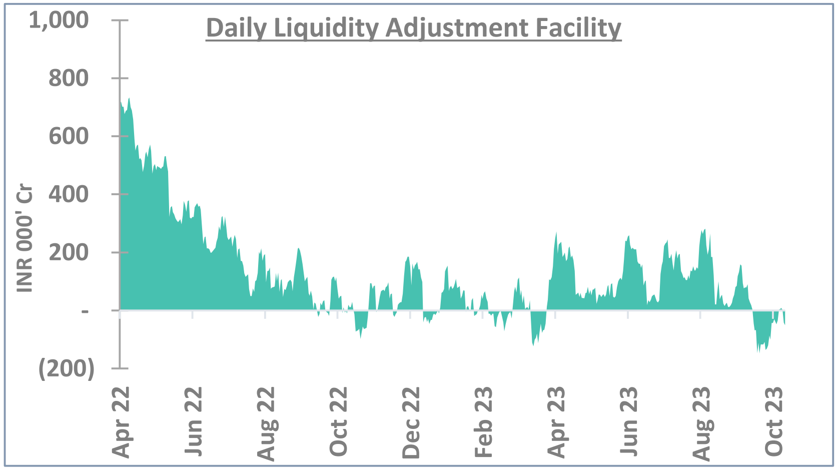
MPC Action

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

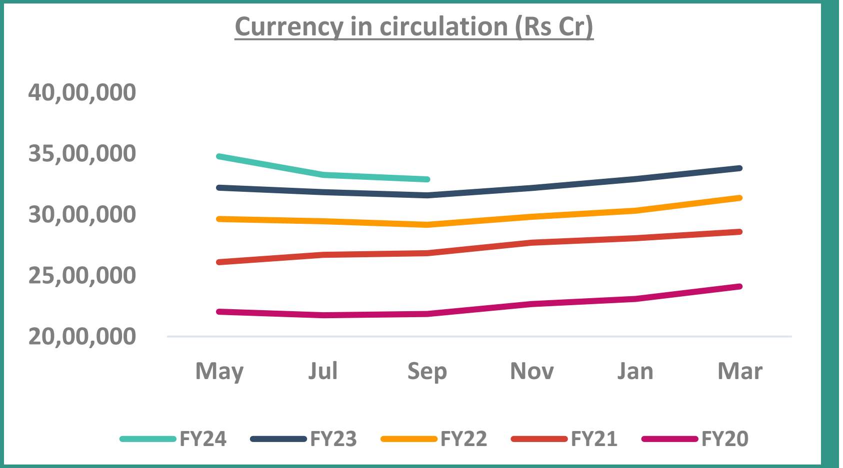
DSP

Liquidity to have opposite drivers: Festive season and Gsec redemption

- **Durable liquidity is sufficient at > Rs. 2.5 lac crore**
  - Govt. spending necessary to ease of pressure on banking liquidity
- **Gsec redemption of Rs. 2 lac cr in Nov/Dec will loosen banking liquidity**
  - RBI OMO expected during that time



- **CIC is typically higher in October and November due to festive demand**
- **State elections to further tighten liquidity.**
- **Thus Gsec redemption will be partly set off by the CIC increase.**



Takeaway:
Banking liquidity expected to remain tight due to disproportionate increase in CIC in festive season

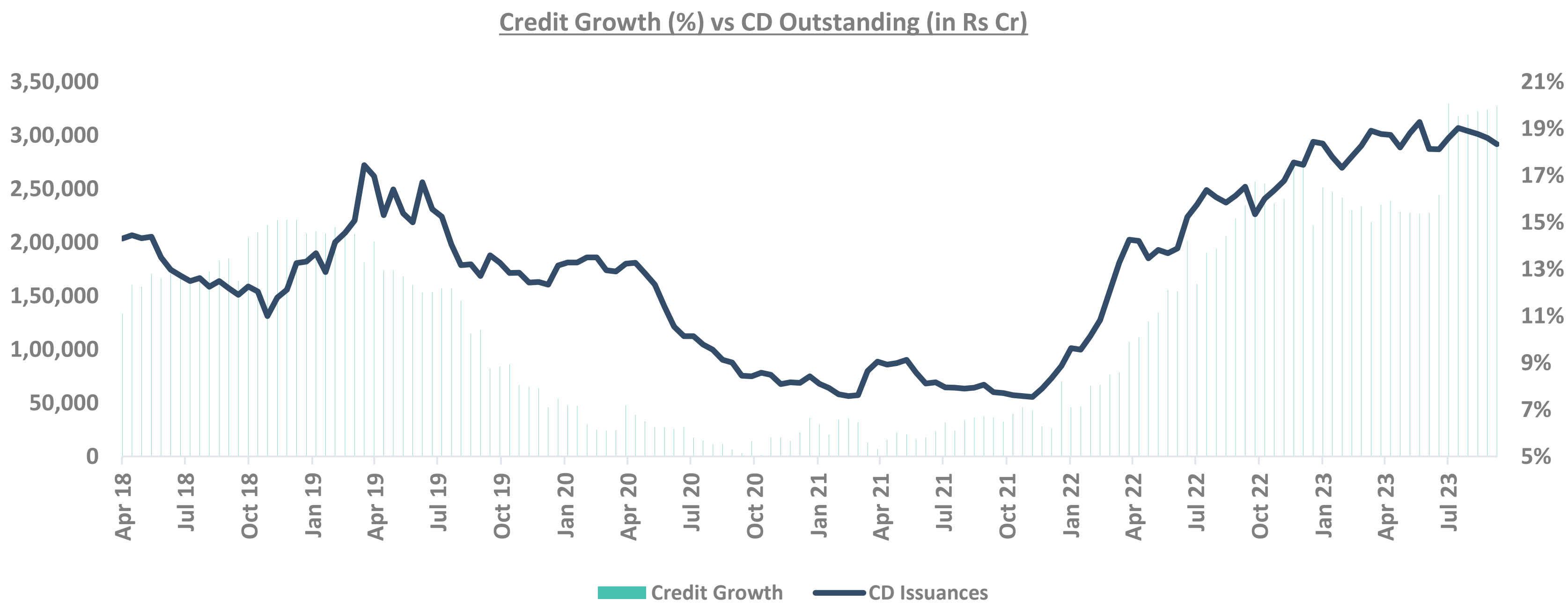
Source – Bloomberg, RBI

DSP

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

- **High credit growth has contributed to increase in CD issuances over the last year. We expect CD issuances to continue at current levels**

- **Flows in money market categories have kept rates range bound, despite continuous supply of CDs by banks**



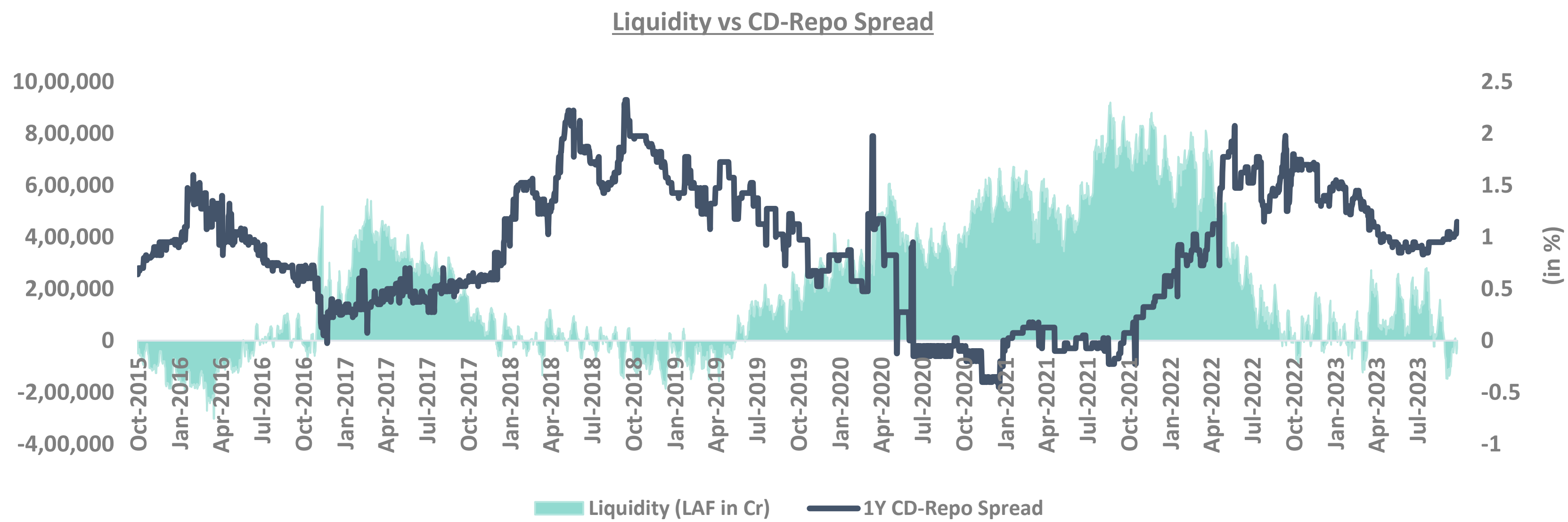
Takeaway:
With supply expected to be at current levels, demand from mutual fund participants to be the key determinant of money market yields

DSP

With money market rates anchored, play for accrual

- ➢ Durable liquidity comfortable at Rs. 2.5 lac crore, 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

- However, with Gsec redemptions there is a risk of marginally surplus banking liquidity.



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

What else

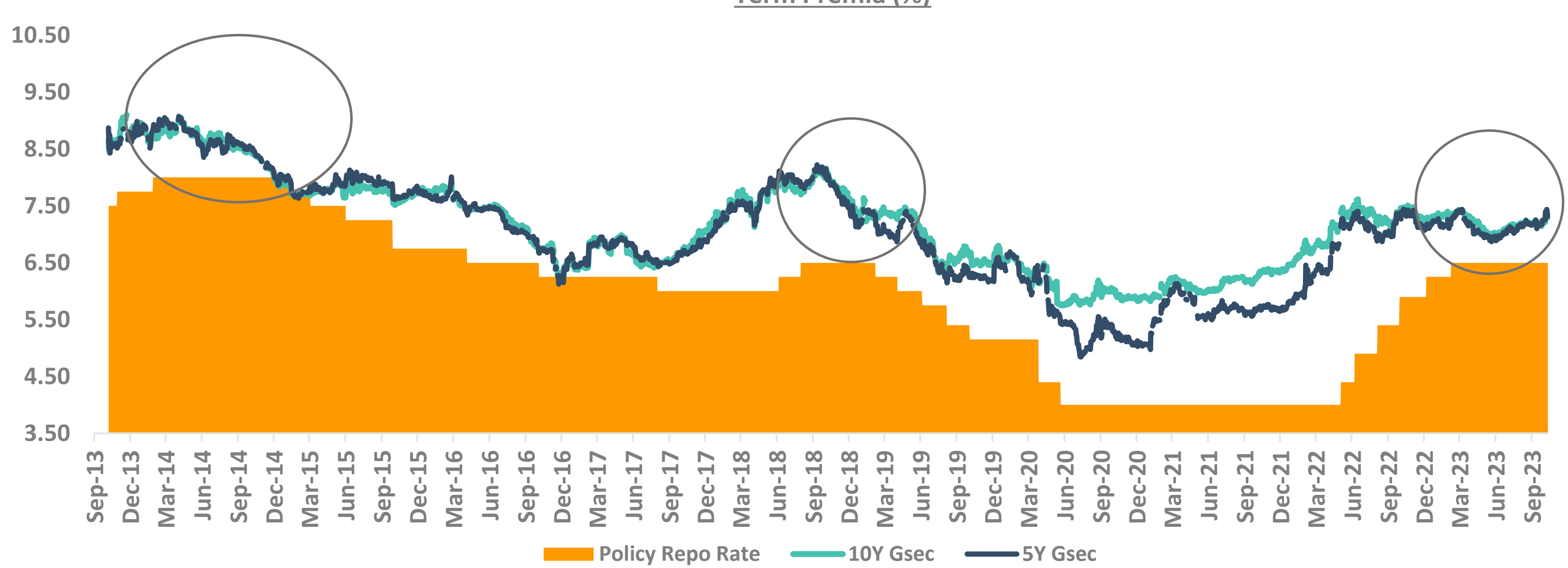
that

can't be bunched up

MISC.

Term premia: It's a BUY!

- **This slide is the reason why we have long bias – Valuations**
  - So far, every point in our presentation was neutral or hawkish…
- **…But that bad news has been priced in**
- **Even if RBI hikes (unlikely and even then probably last hike)…**
  - The spread with 5-Year bond is 50bp!
  - 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, data/sentiments have improved in India. The odds are in favor.**



Takeaway:
India term premium is still high.

Source – Bloomberg

DSP

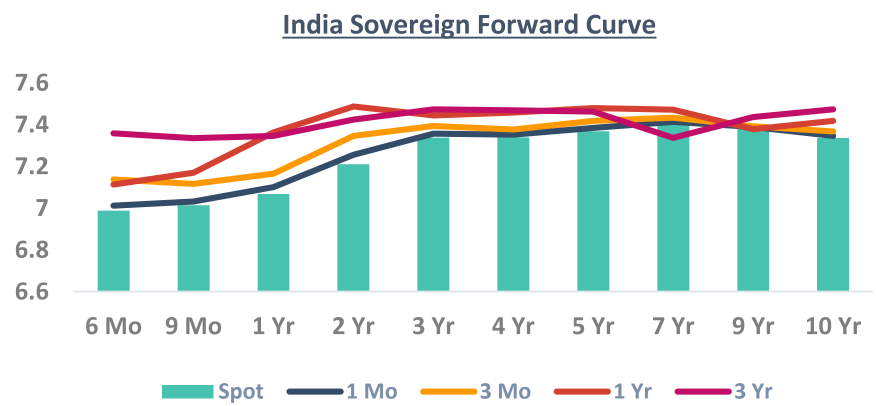
RBI: Reserve Bank of India

DSP FI Framework checklist

CHECKLIST

Drivers	1Y	5Y	10Y	>10Y	Remarks
Monetary Policy	**Neutral**	**Neutral**	**Neutral**	**Neutral**	
Inflation	Neutral	Neutral	Neutral	Neutral	Sep print moderated sharply, upside risks remain
Growth	Neutral	Neutral	Neutral	Neutral	Growth continues to be robust; global slowdown can pose a risk
CAD/BOP/ Currency	Neutral	Neutral	Neutral	Neutral	External sector pressures low, however, EM reaction makes rupee vulnerable
Fiscal Policy	**Neutral**	**Neutral**	**Neutral**	**Neutral**	
Supply	Positive	Positive	Positive	Positive	H2FY24 has higher issuances in longer tenor; SDL issuances to have limited impact
Demand	Negative	Negative	Negative	Negative	Banks demand should lessen, yet sufficient to absorb supply
FPI Flows	Neutral	Neutral	Neutral	Neutral	Passive flows only in the next year
Global	**Negative**	**Negative**	**Negative**	**Negative**	
Global yields	Negative	Negative	Negative	Negative	US data remains mixed
Geopolitics	Negative	Negative	Negative	Negative	Highly uncertain (US-China, Russia-Ukraine, Israel)
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	**Mildly negative**	**Mildly negative**	**Mildly negative**	**Mildly negative**	

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)	**Mildly Negative**	**Mildly Negative**	**Mildly Negative**	**Mildly Negative**	**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 13/Oct/23

DURATION DECISION

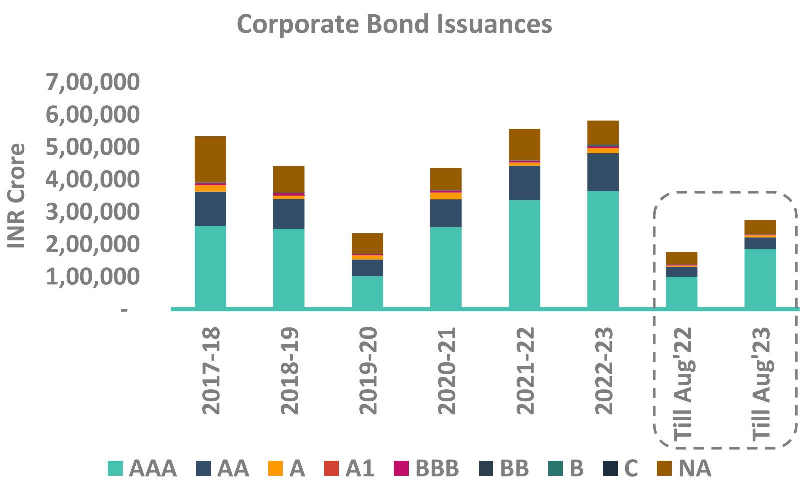
We have discussed duration and yield movement.

How do we choose corporates and credit?

DSP Asset Allocation: Corporate bonds looking a good buy

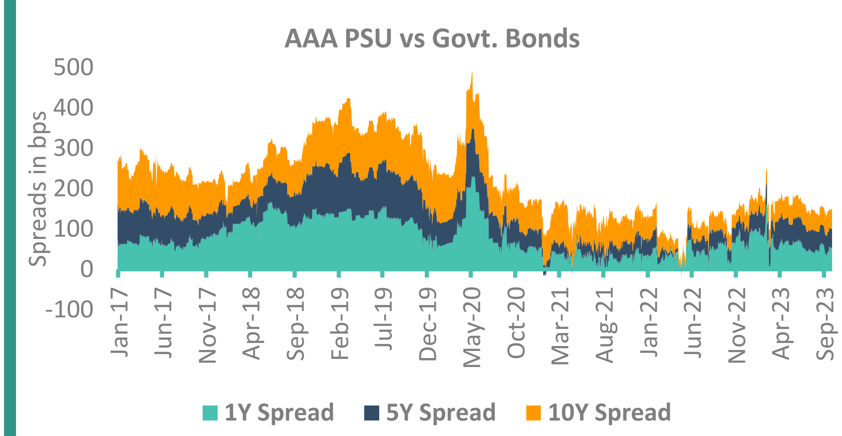
➢ Corporate bonds supply remains manageable

- 5mFY24 issuance at ~1.6x of 5mFY23 led by AAA rated segment
- PSU supply dried-up in Sep as large borrowers preferred bank line and ECB channels
- Supply remains on the lower side Sep at 60k crores



➢ The corporate bond spread are reasonable

- 2-5Y NBFCs providing steady accrual
- AAA PSU Spreads remain to be in the narrow band of 50-55bps
- Demand-supply well-matched & expected to remain the same



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.

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 normalise 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 favourable, especially in peak load demand, resulting in a favourable 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?

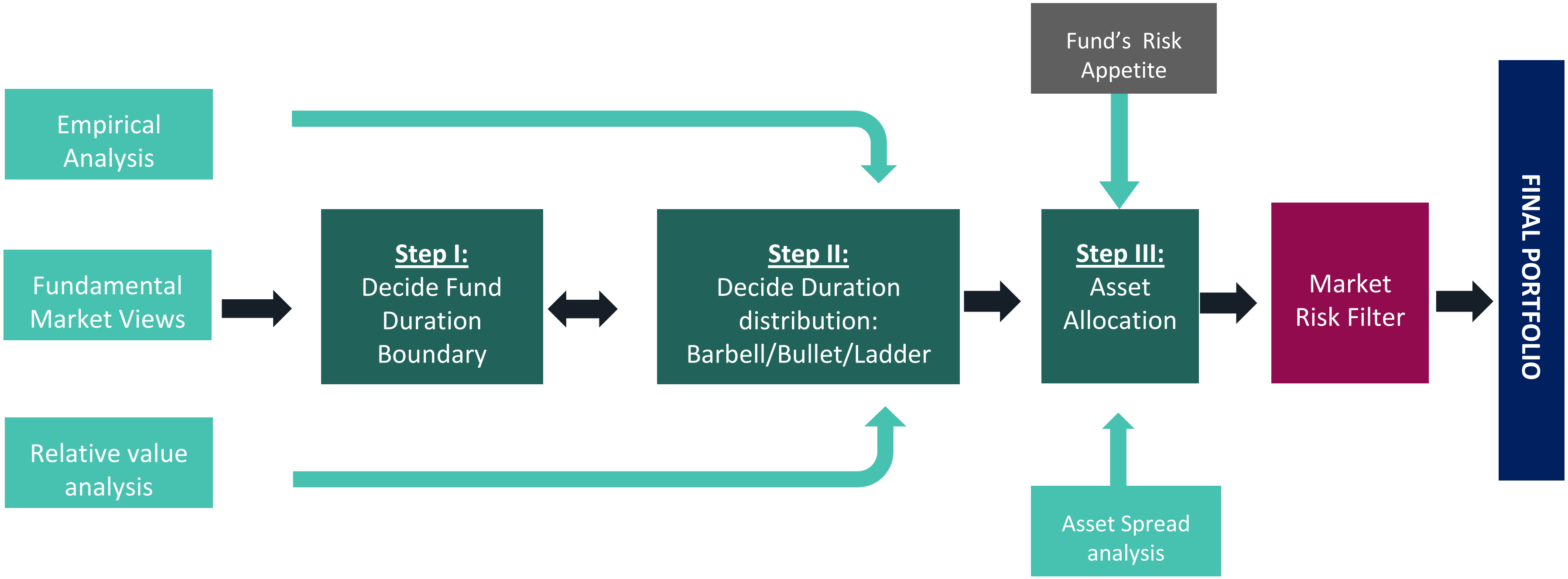
Now

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.

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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