

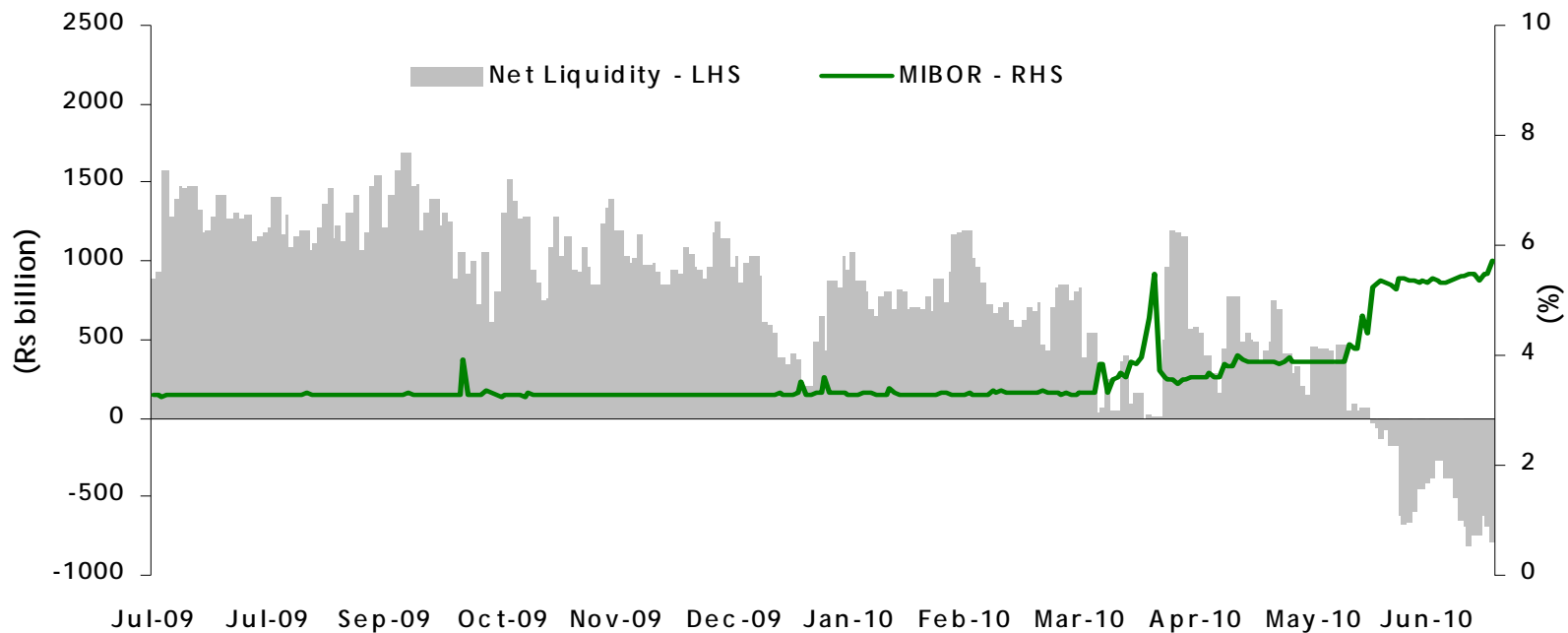
Fixed Income Markets : Current Environment and Outlook

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Macro Events

- The release of the 4Q FY10 GDP data showed the Indian economy growing strongly at 8.6% during the quarter. There were upward revisions to 2Q and 3Q, FY10 GDP data.
- Industrial production (IIP) once again surged, growing at 17.6% rate (YoY) in April compared to 13.9% (YOY) in the previous month. After growing at over 15% since December, the growth rate is likely to ease to a more sustainable level during the rest of the year.
- With IIP averaging 10.4% during FY10 (2.8% in FY09) and growing at over 15% in recent months, the economy is showing clear signs of a revival.
- Six major infrastructure industries, which constitute the core sector, registered a healthy growth rate of 5% in May from 5.4% in April.
- During April-May 2010-11, the core sector registered a growth rate of 5.1% as against 3.5% during the corresponding period of the previous year.
- Inflation, as measured by the WPI Index, was at 10.2% (YoY) in May. The rate is starting to tread lower after having peaked at 11% in March.
- Economic growth measured by GDP is now in the positive territory for the US, UK and the Euro zone, though the unemployment rate continues to remain high. US GDP was revised lower to 2.7% (YoY) in Q1'10 giving further evidence that the recovery is likely to be modest. GDP growth in the UK for Q1'10 was revised higher.
- The global economic recovery is building steam led by strong growth in Asia although the sovereign debt crisis in Europe is presenting risks to the recovery.

Liquidity - tightens taking rates higher



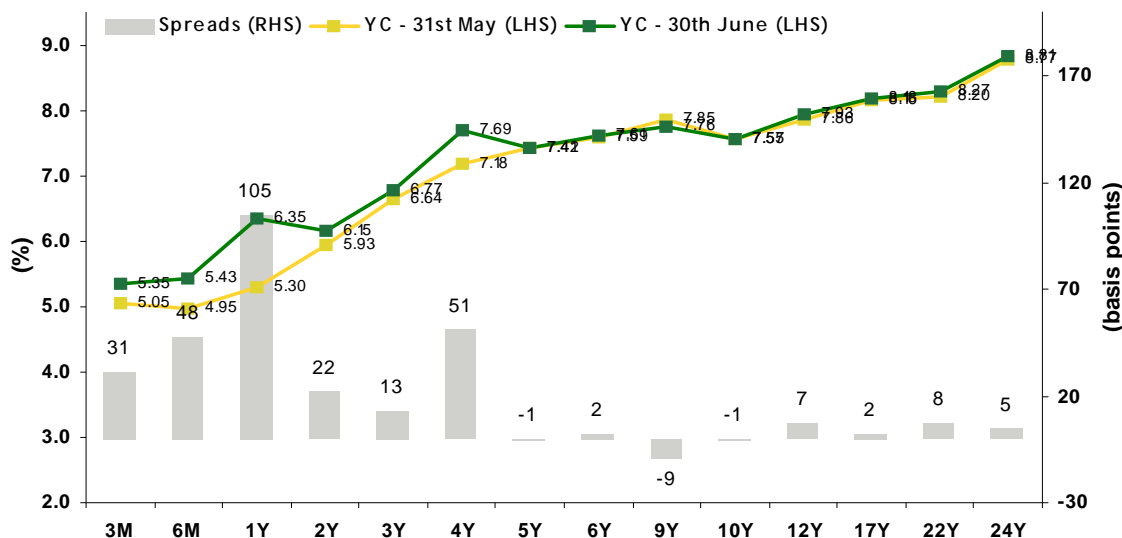
Source: Bloomberg

- Liquidity in the system dried up completely with no amount on the daily RBI LAF reverse repo at the end of June and an average of just around INR 500 crore during the month.
- MIBOR rates moved higher to 6% at the end of June from under 5% at the end of last month. Rates averaged 5.25% during June.

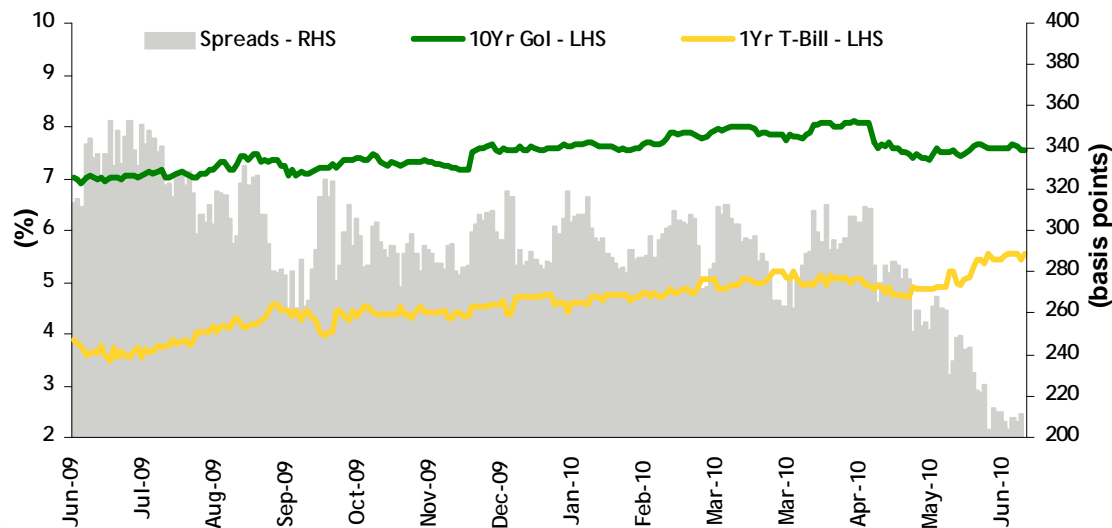


Source: Bloomberg

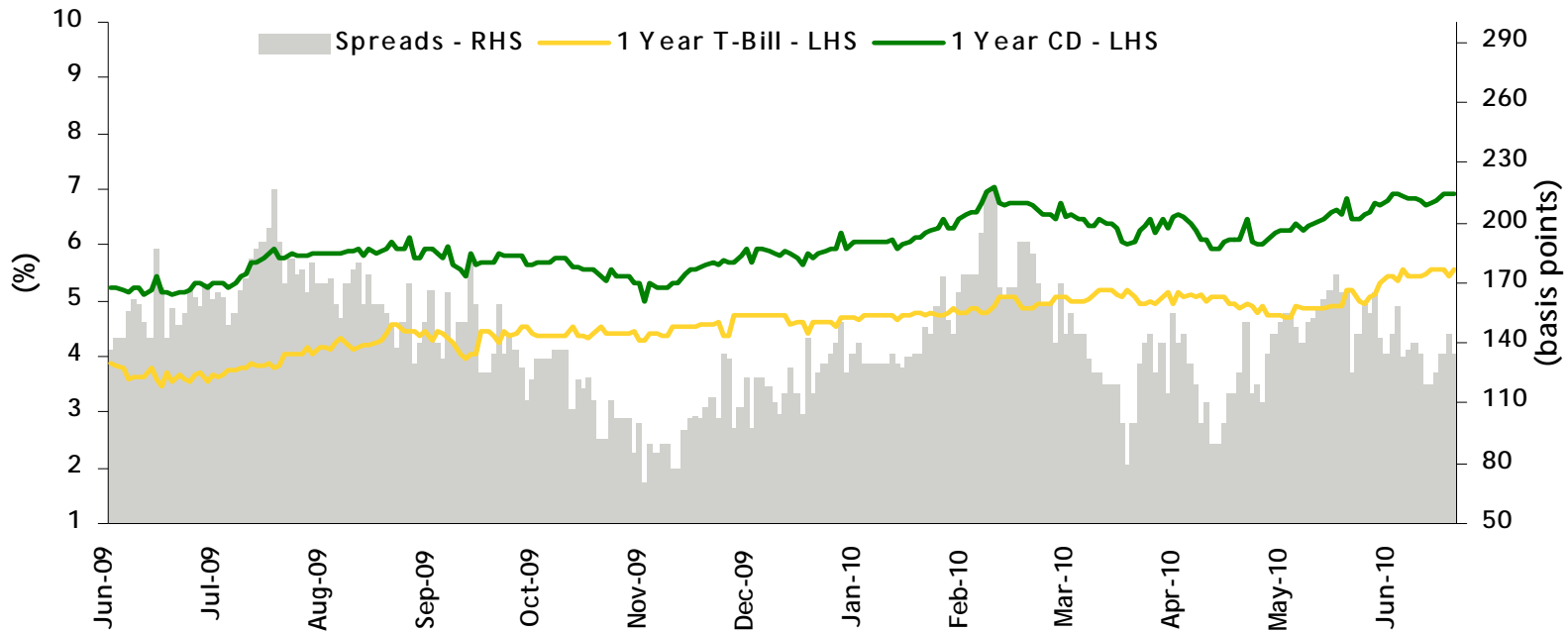
G-Sec Yield Curve - significantly flatter



- The G-Sec yield curve flattened, with a steep rise in yields on the short end of the curve, while there was only a marginal rise in yields on the long end of the curve.
- The yield on the 10yr benchmark closed unchanged for the month at 7.5%.
- In the T-Bill Auction held on June 30, the 91-day T-bill was issued at 5.28% and the 364-day paper yielded 5.65%.
- Current 1yr vs. 10yr GOI spread fell by 30 bps to 210 basis points during the month. The spread has averaged 270 bps in the last year.



Money Market - rates higher amidst tight liquidity



Source: Bloomberg

- Money market rates rose sharply amidst tight liquidity in the market.
- Spreads between 1 Year CD's and T-Bill's ended the month at 130 bps while spreads between 1 Year CP's and CD's were 35bps. Overall, 1 Year CP's traded at a spread of 165 bps over 1 year T-Bills.



Source: Bloomberg

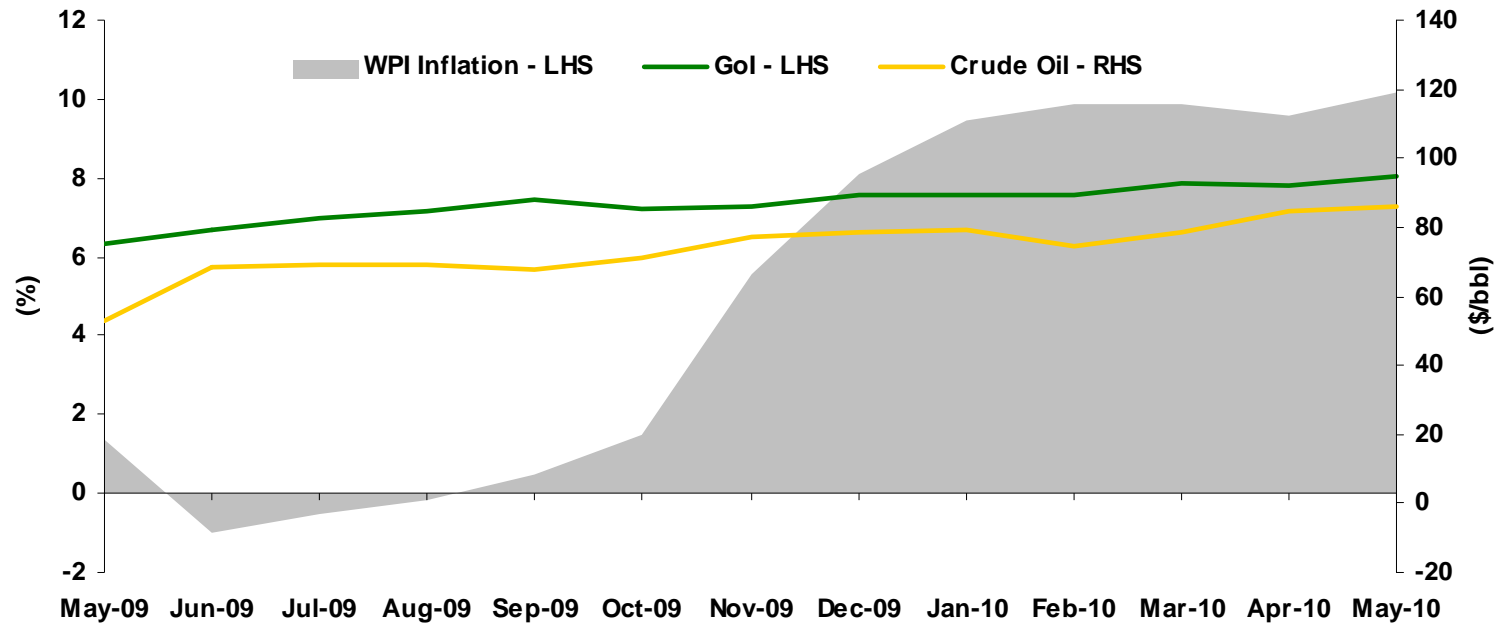
Corporate Bonds spread - unchanged



Source: Bloomberg

- Spreads of 5-Year AAA corporate bonds over their corresponding benchmark sovereigns, widened by 5 bps during June to 85 bps.
- The yield on the 5 year AAA corporate paper closed the month unchanged at 8.2%.

Crude and Inflation Dynamics



Source: Bloomberg

- Inflation, as measured by the WPI Index, was at 10.2% (YoY) in May. The rate is starting to tread lower after having peaked at 11% in March.
- Crude Oil prices (NYMEX Crude Oil Barrel) tread marginally higher during the month and closed at \$75.6 a barrel at the end of June.

Religare MF: Fixed Income Outlook and Opportunities

Fixed Income Market Outlook

- Global economic data is coming in mixed with a slowing down of the Chinese economy and pockets of positive data flows coming in from the US.
- The European fiscal crisis has pushed back expectations of aggressive rate actions in emerging economies while prolonging the extremely accommodative stance in the developed world.
- U.S. yields expected to stay low as there is still no clear sign of a recovery being underway.
- Systemic liquidity is likely to continue to remain under pressure for the month of July and then return to neutral mode.
- Yields at the short end likely to normalise by end July as liquidity conditions are likely to improve.
- Yields at the long end are expected to remain range bound and takes cues primarily from global developments. Demand side inflationary pressures, however, need to be watched closely.
- The RBI which has embarked upon its rate hiking cycle with a rate hike as recent as the one on the 2nd of July is likely to increase the policy rates once again in its July Credit Policy review.

Portfolio Actions during the month

- **Religare Ultra Short Term Fund**
The Fund reduced duration in anticipation of tighter liquidity conditions. The Fund would target adding liquid papers when there are signs of liquidity normalising.
- **Religare Short Term Plan**
The Fund maintained exposure to the 1-2 year segment while increasing exposure to liquid CDs in the 3-6 month segment.
- **Religare Liquid Fund**
The Fund maintained a low duration in anticipation of tighter liquidity conditions in the month of June. The Fund would look to increase duration during the month once liquidity normalises.
- **Religare Credit Opportunities Fund**
The Fund had considerable maturities in the month of June which we redeployed at attractive yields. The fund would continue to look at names available at attractive yields.
- **Religare Active Income**
The Fund continued to have a lower duration in line with the liability profile of the Fund.

Ideas for investors

- Risk-averse investors should continue to look at short end of the yield curve.
- Yields at the long end have been range bound given the mixed global economic scenario and the path of tightening embarked upon by the RBI. Yields are likely to head lower on a) expectations of less hawkish central bank following euro-zone scare b) lower supply side inflationary pressures due to a normal monsoon and c) lower than expected government borrowing program. Investors with a 6-12 month horizon should continue to stay invested.
- Investors with an investment horizon of 3-6 months may also look at investment in Religare Short Term Fund and Religare Credit Opportunities Fund as the current liquidity squeeze is likely to end by the end of the month leading to a sharp correction in yields at the short end.

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