

# Fixed Income Markets : Current Environment and Outlook

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# Macro Events

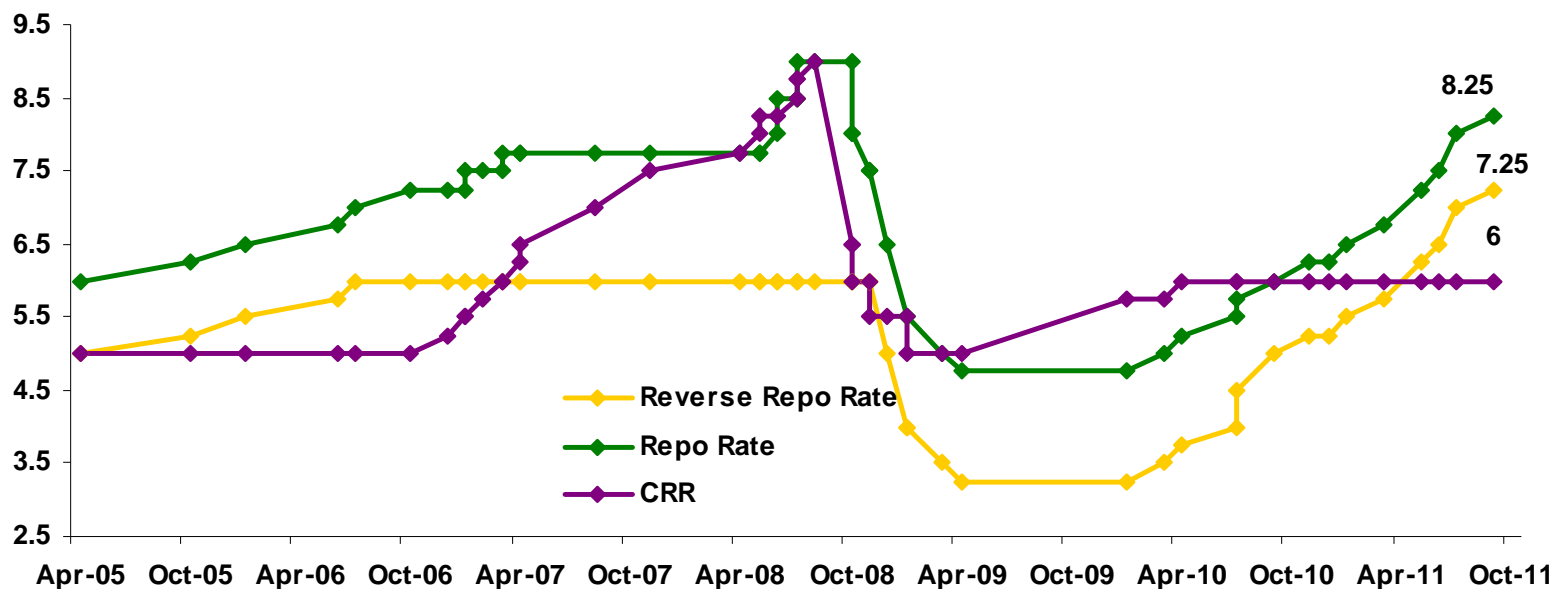
## Domestic

- The RBI, in its monetary policy meeting held on September 16, 2011, raised its key benchmark rates, continuing with its stance .
- India's economic (GDP) growth slowed to the slowest pace in 6 quarters to a 7.7% (YoY) rate in Q1FY12, lower than the downward revised 8.8% rate in Q1FY11, boosted mainly by a strong performance by the services sector which grew at an impressive 10% (10.4% in Q1FY11). Agricultural sector showed an improvement, rising to a 3.9% growth rate (2.4% in Q1FY11) while the Industrial sector has slowed substantially, recording a growth rate of just 5.1% in Q1FY12 down from 9.1% in Q1FY11.
- The Index of Industrial production (IIP) growth fell drastically to a 3.3% rate in June 2011 after having risen 8.8% YoY in the previous month (June 2011) and 9.9% in July 2010. The fall was mainly due to a substantial contraction in the output in the volatile capital goods segment and a mild contraction in intermediate goods output.
- Headline WPI inflation remains stubbornly high, and the rate rose to 9.78% YoY in August 2011 from 9.22% in July 2011. WPI Inflation was at 8.87% during the corresponding month of the previous year (August 2010). The June 2011 WPI Inflation rate was revised higher to 9.51% YoY from a provisional 9.44% earlier. The quantum of change in the revision to the data has come down substantially. The revision was just 7 bps compared to 50 bps in the previous month and as much as 108 bps in April.

## International

- Economic growth measured by GDP, has weakened considerably from the post-crisis rebound, in the US, UK and the Euro zone. Also, recently revised figures have shown that the economic growth in the past was far lower than previously thought. Economic contraction during the slowdown was deeper and more prolonged while the growth during the rebound was weaker. The unemployment rate in the developed economies has failed to show any significant improvement.
- US GDP growth rate was revised higher to 1.3% (Ann/QoQ) for Q2'2011 up from a meager 0.4% (Ann/QoQ) in the previous quarter (Q1'2011). GDP growth in the UK was revised sharply lower to just a 0.1% (QoQ) rate in Q2' 2011 down substantially from a revised 0.4% rate in the previous quarter (Q1' 2011).

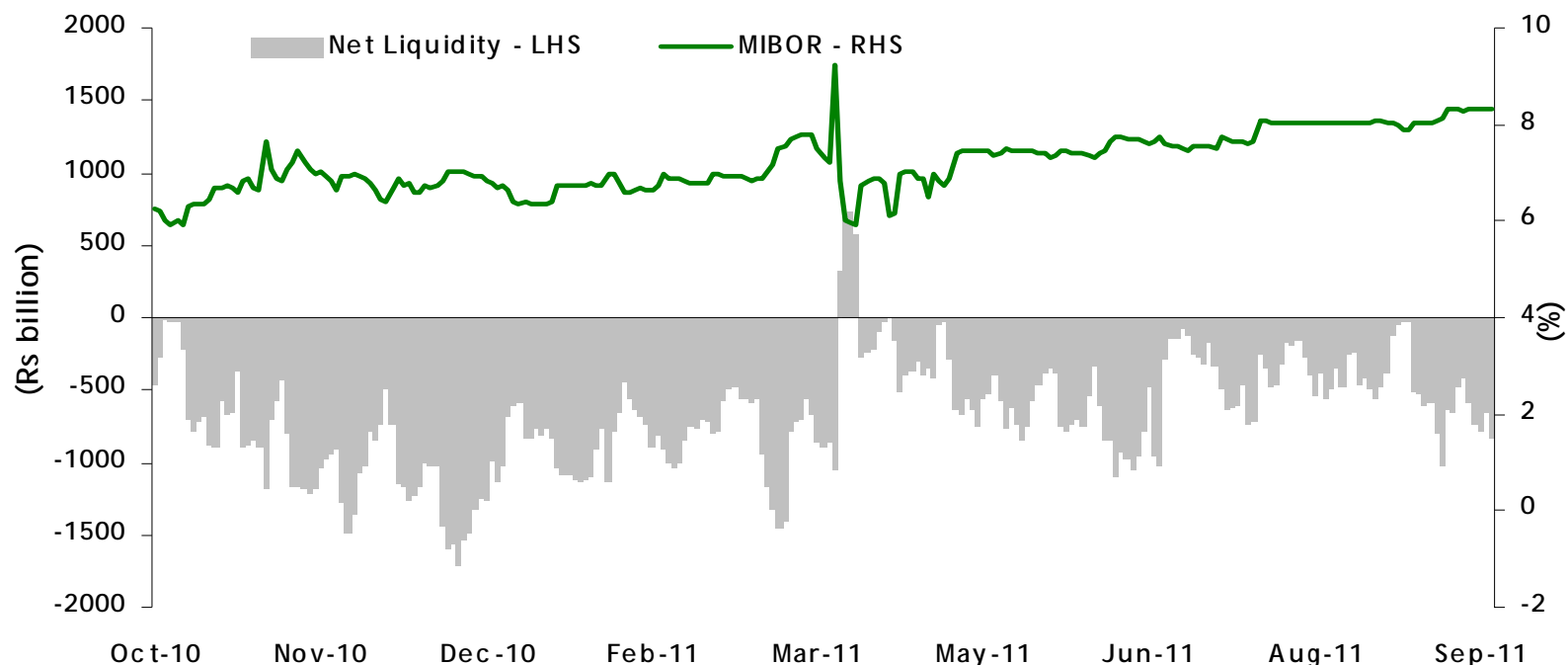
# RBI- continues on its path of tightening rates



- In its last monetary policy review, the Reserve Bank of India (RBI) hiked the benchmark repo rate to 8.25%, while the Reverse Repo rate and the Marginal Standing Facility were automatically revised to 7.25% and 9.25%, respectively. The Bank Rate remains unchanged at 6%; Cash Reserve Ratio (CRR) remains unchanged at 6% of Net Demand and Time Liabilities (NDTL).
- The central bank has raised its key policy rate (repo rate) 12 times, totaling 350 basis points since March 2010. (pre-crisis the repo rate stood at 9%).
- The next RBI monetary policy meeting is due on October 25, 2011.



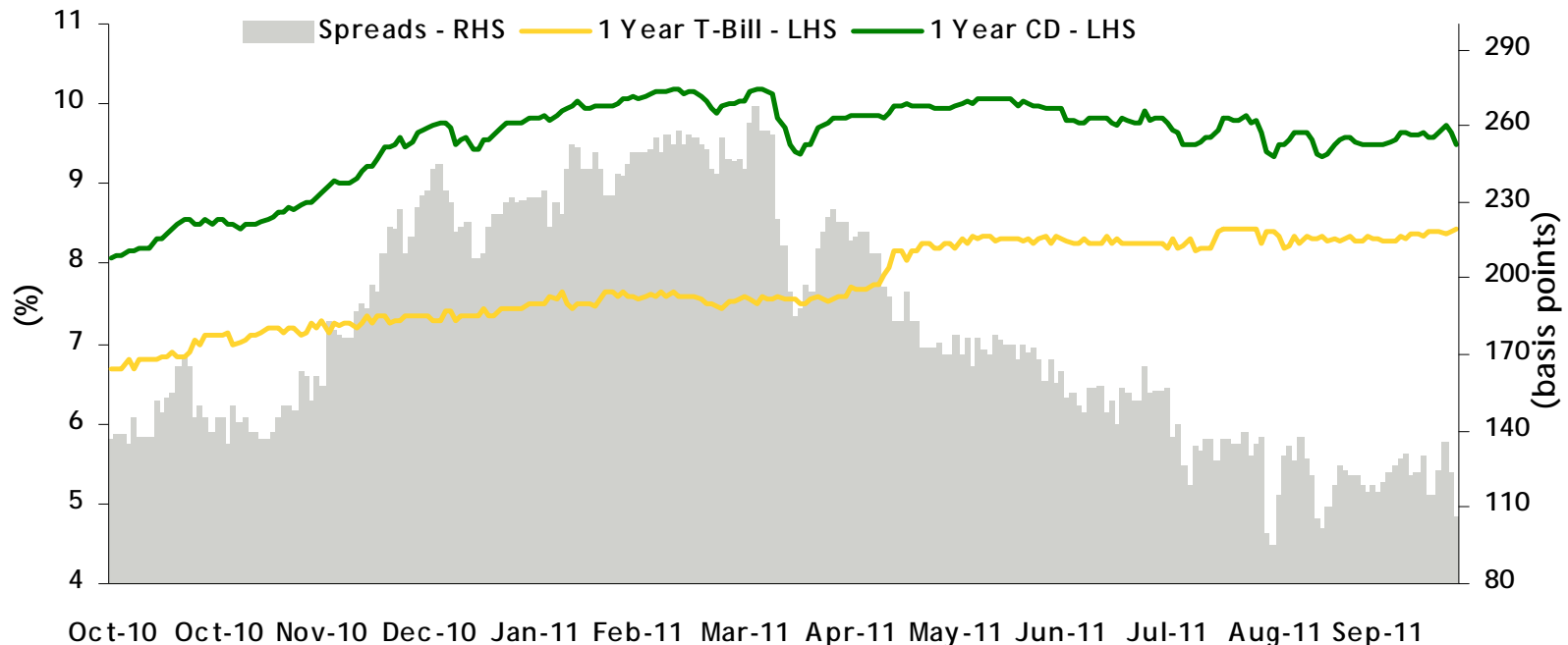
# Liquidity



- The daily average borrowings by all the banks from RBI under LAF in the month of September'11 was around Rs.52,000 crores (Rs.38,000 crores previous month).
- The daily average MIBOR over the month of Sept.'11 was at 8.15% (8.04% previous month).



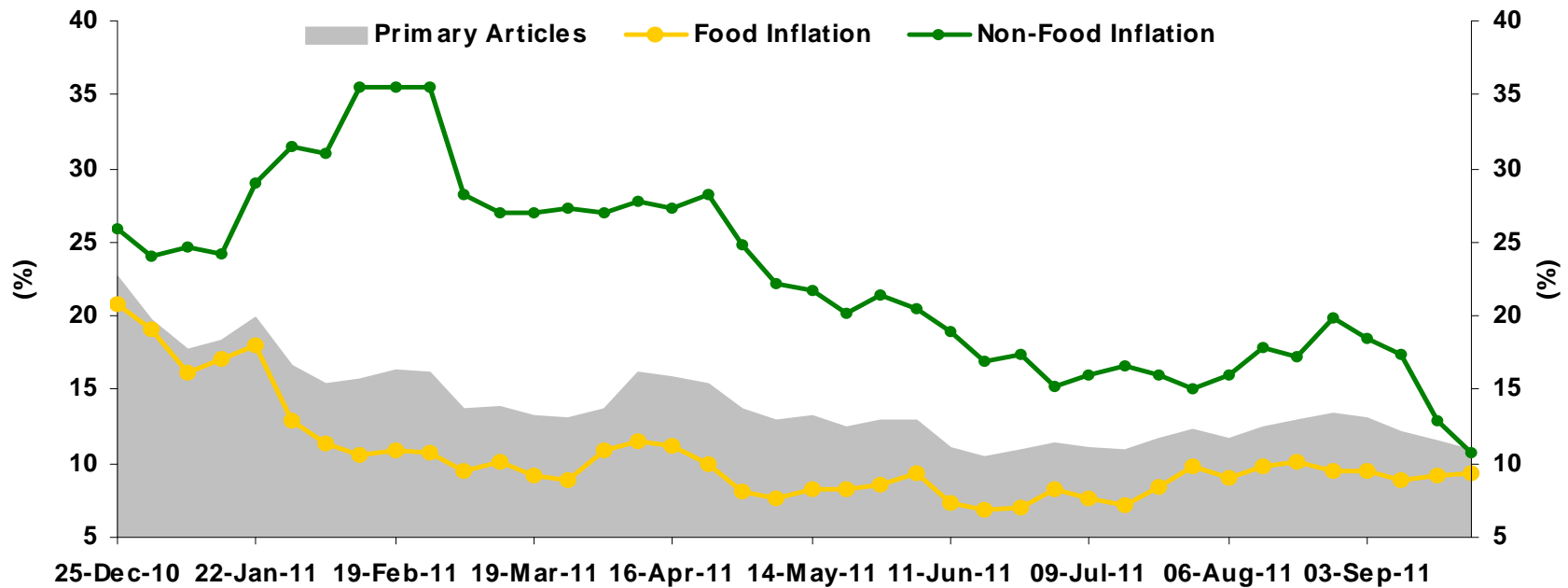
# Money Market



- The money market rates softened over the month of Sept'11. The yields of money market papers from 3 months till 12 months moved lower over the month. However, the shift was not parallel. The yields of 12month money market assets had moved higher sharply during the month.
- The yields of T-Bills traded with a hardening bias and moved higher by about 5-6bps over the month.



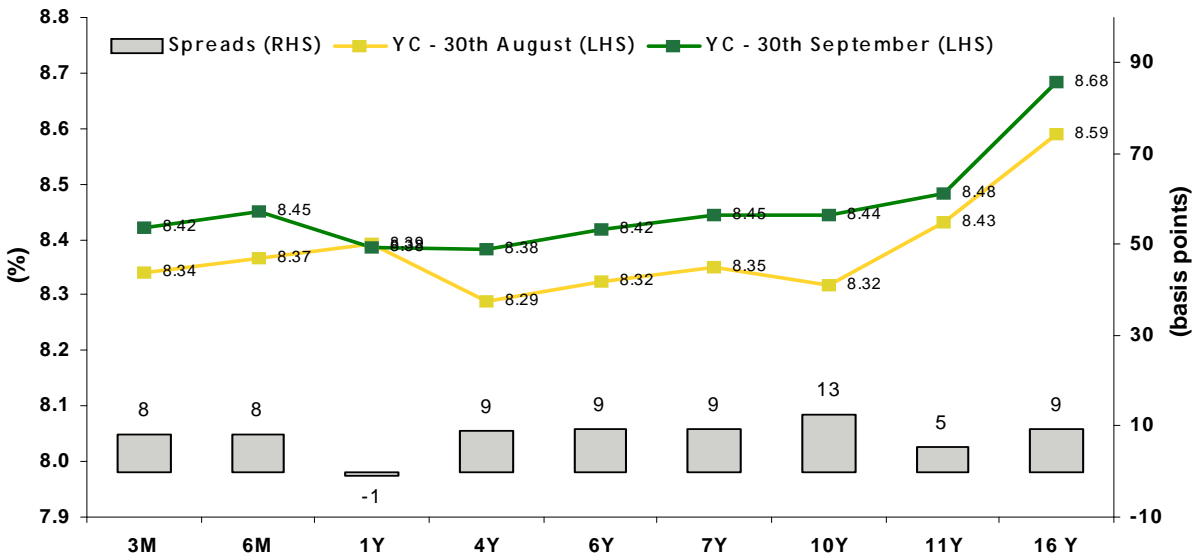
# Inflation Dynamics - Non-Food Inflation witnesses a steep fall



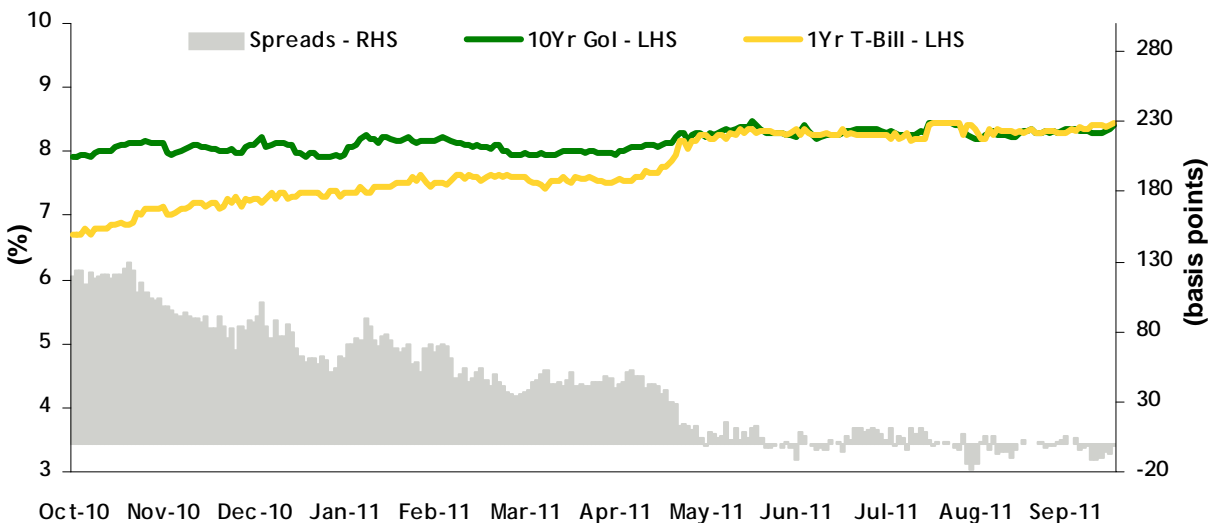
- India's Food Inflation, softened to 9.4% for the week ending September 24, 2011. It had been as high as 20.8% on December 25, 2010 and then fell to a low of just 6.9% on June 18, 2011. Non-Food articles Inflation, which had been disturbingly high in the first quarter of 2011 has softened substantially. Non-Food article Inflation fell sharply to 10.8% for the week ended September 24, 2011 from 19.9% on August 27, 2011. It had been as high as 35.5% on Feb 26, 2011.
- The differential in the rate of Inflation between Non-food articles and food articles has now fallen to as low as 1.4% during the week ended September 24, 2011 from as high as 24.9% in the week ended February 12, 2011.



# G-Sec Yield Curve - upward shift

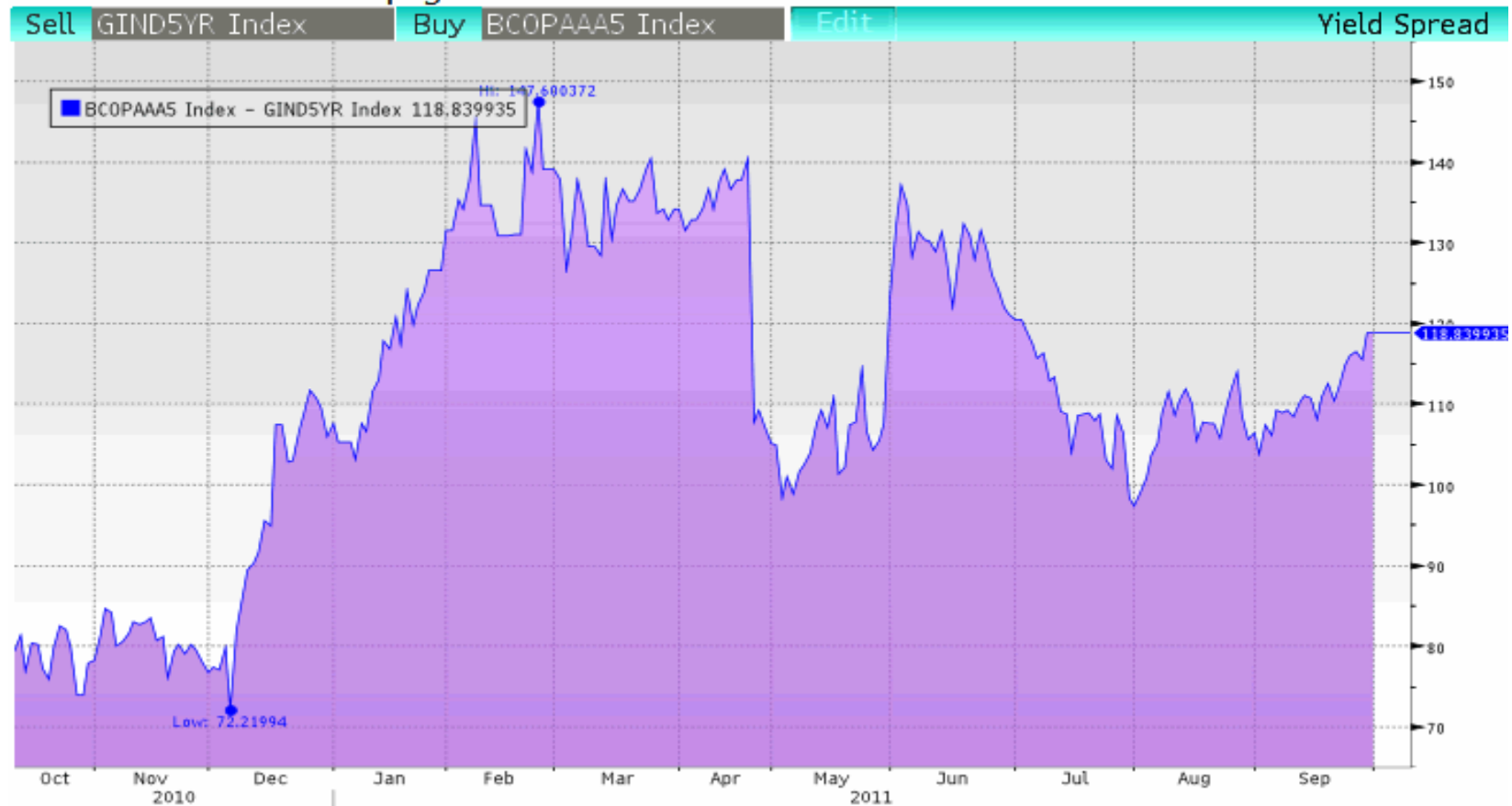


- The G-Sec yield curve shifted higher in the month of September, with yields rising across all the segments.
- The yield on the 10yr benchmark rose 12 bps over the month of September to 8.44% from 8.32% at the end of August.
- In the latest T-Bill Auction held on September 21, 2011 the 91-day T-bill was issued at 8.44%, and the 364-day paper yielded 8.46%.
- The 10yr vs.1yr GOI spread remained negative in the month of September. The spread has averaged around 50 bps during the last year.



# Corporate Bonds spread - stable

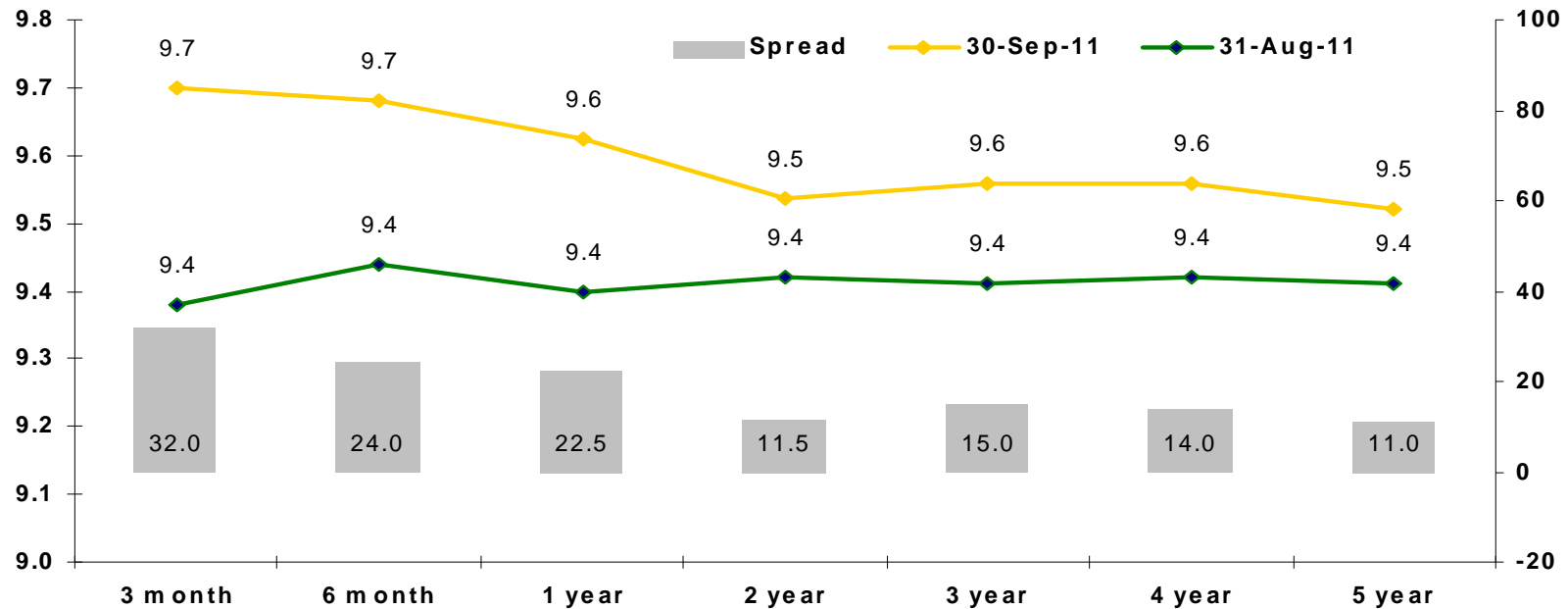
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- The 5 year AAA spreads are currently at 118bp. About 10bp higher than the previous month.



# Corporate Bond yield curve – shifts upward



Source: Bloomberg. Indian AAA Composite Curve.

- The AAA corporate bond yield curve shifted upwards in September 2011.
- The curve witnessed an inversion with the short-term rates rising more steeply.
- The credit curve has become more steeper now.

# Religare MF: Fixed Income Outlook and Opportunities

# Fixed Income Market Outlook

- While the liquidity situation continued to be adverse, rising deposit growth is expected to improve the situation within the system.
- Some improvement is visible in the M3 growth and money multiplier as well.
- It appears that the whole economy is getting re-adjusted to a new 'normal' inflation in an environment of higher food prices, and higher real wages.
- The government bond yields are expected to experience further bearish tendencies and credit spreads are also expected to widen from the current levels.
- The inflation might witness some softening due to sluggish global growth, dropping commodity and energy prices and a higher statistical base effect.

# Portfolio Actions during the month

- **Religare Liquid Fund**
  - The fund has continued to maintain a low duration, Liquid fund is maintaining a well diversified portfolio.
- **Religare Ultra Short Term Fund**
  - The fund has also maintained a lower duration well diversified portfolio.
- **Religare Short Term Plan**
  - The fund has increased duration to over 8 months over the month, by aligning in high liquid, high credit 2-3 year corporate bonds.
- **Religare Credit Opportunities Fund**
  - The fund has been successfully investing in mispriced credits with low interest rate risk.
- **Religare Active Income**
  - The fund has maintained a duration below 1 year, and invested in a mix of low duration money market assets and short maturity debentures. The fund had also indulged in some g-sec trades over the month.

# Ideas for investors

- In an environment of stiff inflation and deficit liquidity, investors are encouraged to select funds in line with their investment horizon.
- The ***Religare Credit Opportunities Fund*** offers an attractive opportunity for investors with short investment horizons of 1-3 months and moderate level of credit risk appetite. The fund is ideally positioned to capture mis-priced risk in an environment of deficit liquidity and varying credit spreads of short maturity papers.
- The ***Religare Short Term Income Plan*** offers attractive accrual with reduced interest rate risk. Ideal for investors with 2-4 months investment horizon.
- The ***Religare Medium Term Bond Fund*** offers higher current yield and moderate interest rate risk. The present duration of between 8-9 months opens up opportunities of capital appreciation over a 3-6 month investment horizon for investors with moderate risk appetite.
- The ***Religare Active Income Fund*** The portfolio intends to run a duration between 5-8 months. It opens up opportunities of capital appreciation in an environment of yield curve steepening and active duration management. It is intended for investors with moderate risk appetite.

# Disclaimer

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