Monthly Debt Market Update

January 04, 2023 I Economics

Global Overview

- At the December FOMC meeting, the US Federal Reserve increased interest rates by 50 bps while providing a hawkish outlook for rates in 2023. The central bank now expects the Fed funds rate at 5.1% by end-2023, implying three more 25 bps rate hikes are on the cards -- more than what was expected prior to the meeting.
- US CPI inflation eased to 7.1% y-o-y in November as compared to a market consensus of 7.3%, on the back of falling energy prices. Meanwhile, core CPI inflation softened to 6% y-o-y. On the jobs front, nonfarm payrolls rose by 2,63,000 in November as compared to a consensus of 2,00,000.
- The 10-year US Treasury yield rose 24 bps in December, triggered by the Fed's hawkish outlook on rates. There was also the Bank of Japan's (BOJ) unexpected policy move where it raised its bond yield cap. Meanwhile, increasing borrowing costs in Europe amidst a hawkish ECB and increasing bond supply resulted in steepening of the yield curve.
- US stock markets witnessed a decline in December on rising bets of further monetary policy tightening by global central banks, which could push the economy into a recession. That said, better-than-expected earnings results, strong consumer sentiment data and easing inflationary pressures helped limit the fall in stocks. In Europe, commentary by the ECB on upcoming 'significant' rate increases dampened investor sentiments.
- The dollar index weakened by 2% in December on waning safe-haven appeal as markets weighed recession risks. In contrast, the euro benefitted from rising Eurozone yields on the back of the ECB's hawkish meeting.
- Crude oil prices declined on concerns of a global slowdown. Brent and WTI crude oil ended the month at $86/bbl and $80.4/bbl, respectively.
- Going forward, in the US, incoming inflation and jobs data would be key triggers. While inflation has shown signs of peaking, continued tightness in the labour market suggests that wage growth could keep underlying demand elevated. This implies that the Fed may not signal a pivot until the latter half of 2023. Meanwhile, the revival of economic activity in China poses as a double-edged sword – on one hand supply chain bottlenecks could ease, while on the other, demand from the Asian giant could prop up global raw material and energy prices.

	Close	MTD	YTD
Equities			
S&P 500	3839.50	-5.9%	-19.4%
Nasdaq	10466.48	-13.0%	-35.9%
Dow Jones	33147.25	-4.2%	-8.8%
Euro Stoxx	423.50	-3.8%	-13.2%
FTSE 100	7451.74	-1.6%	0.9%
DAX	13923.59	-3.3%	-12.3%
CAC40	6473.76	-3.9%	-9.5%
Nikkei 225	26094.50	-6.7%	-9.4%
Hang Seng	19781.41	6.4%	-15.5%
Sensex	60841.00	-3.6%	5.3%
NIFTY	18105.00	-3.5%	5.2%

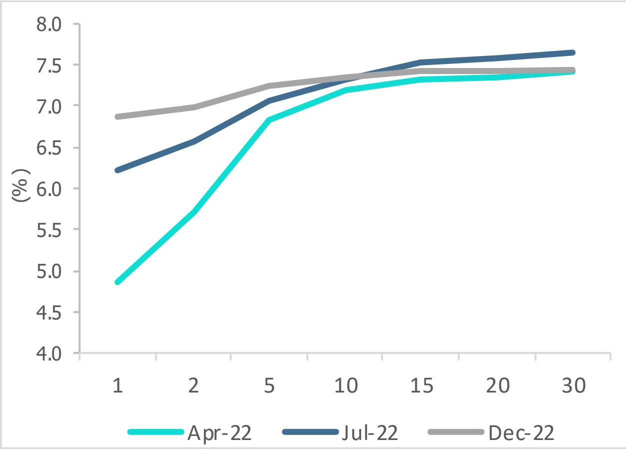
	Close	MTD (bps)	YTD (bps)
Treasuries			
10-yr UST	3.84%	24	233
10-yr Bund	2.57%	64	275
UK 10-yr Gilt	3.67%	51	270
10-yr JGB	0.45%	20	38
	Close	**MTD**	**YTD**
Currencies			
DXY	103.49	-2.2%	7.8%
EUR/USD	1.07	2.9%	-5.6%
GBP/USD	1.21	0.2%	-10.6%
USD/JPY*	131.12	-4.5%	13.9%
USD/CNY*	6.90	-2.7%	8.5%
USD/INR*	82.75	1.7%	11.1%
*(+) indicates weakening and (-) denotes strengthening			
	Close	**MTD**	**YTD**
Commodities			
Gold ($/Oz)	1830	4.0%	0.1%
Silver ($/Oz)	24	11.0%	3.5%
Brent ($/bbl)	86	-1.1%	10.6%
WTI ($/bbl)	80	-0.1%	7.0%
Aluminium($/mt)	2372	0.8%	-12.1%
Copper($/mt)	8386	4.2%	-12.2%

India Overview – Key Highlights and Expectations

- At the RBI MPC meeting on December 5-7, the central bank hiked the repo rate by 35 bps to 6.25%, albeit slowing the pace of tightening from 50 bps rate increases in the previous meetings.
- India's CPI-I inflation eased by 90 bps to 5.9% (y-o-y) in November on the back of a softer increase in food prices. However, core CPI remained sticky above the RBI's tolerance limit. Core-CPI, which strips out food and energy components, rose 6.3% (y-o-y) in November from 6.2% (y-o-y) a month prior.
- The current account deficit (CAD) widened to a 9-year high of $36.40 billion in the quarter ending September 2022 (4.4% of GDP). Given our expectations of continued pressure on exports, CareEdge sees CAD at 3.6% of GDP in FY23. In FY24, we project CAD to moderate to 2.2% of GDP (still higher than 1.2% seen in FY22).
- The Centre has announced that it will bear expenses worth Rs 2 lakh crore for providing free food grains under the National Food Security Act (NFSA) till December 2023. The move comes at a time when the Pradhan Mantri Garib Kalyan Anna Yojana (PMGKAY) is set to conclude in 2022. This is seen as a fiscally prudent step, which would help contain the government's food subsidy bill in the coming fiscal year.
- Yield on the 10-year benchmark bond remained volatile in December, trading between 7.18% and 7.33% levels through the month as inflation data, RBI policy, BOJ yield cap removal and a hawkish US Fed stance posed as triggers. The shorter end of the yield curve saw significant steepening as liquidity in the banking system slipped into a deficit.
- Looking ahead, we remain watchful of upcoming inflation prints and the Union Budget for FY24. With core inflation remaining high, we do not rule out the possibility of another 25 bps rate hike in the Feb meeting. Meanwhile, the government market borrowing program to be announced at the Union Budget in Feb 2023, the last before general elections in 2024, will be a key event for bond markets. Apart from the fiscal landscape, we will also remain on the lookout for any volatility in crude oil prices and the rupee over the coming months. Nonetheless, we believe the 10-year benchmark bond yield will remain capped at 7.50% for the remainder of the fiscal year.

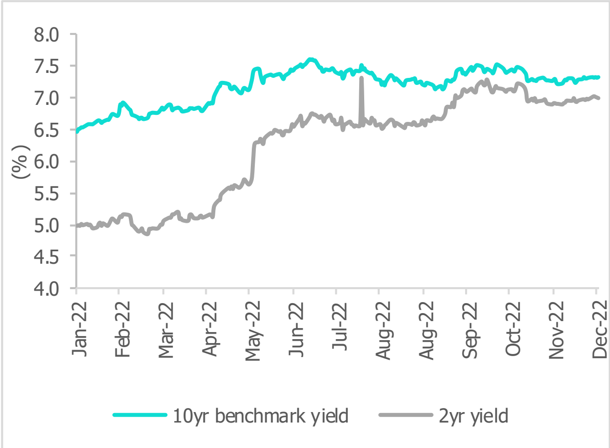
Indian Debt Market Chartbook

Yield Curve Flattens in December



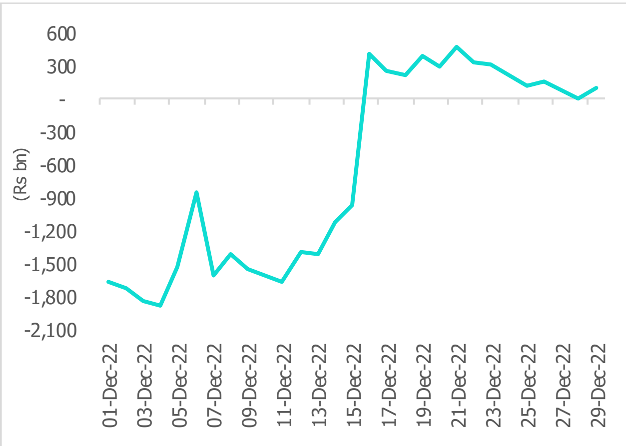
The yield curve flattened in December on account of a sharp rise in short-tenor bond yields, amidst policy rate hikes and a steady withdrawal of liquidity from the banking system.

G-sec Spread Narrows on Rise in Short-tenor yields



The shorter end of the yield curve has witnessed significant steepening. Despite rate hikes through 2022, the 10 year saw steepening of 86 bps as compared to 200 bps spike in the 2 year.

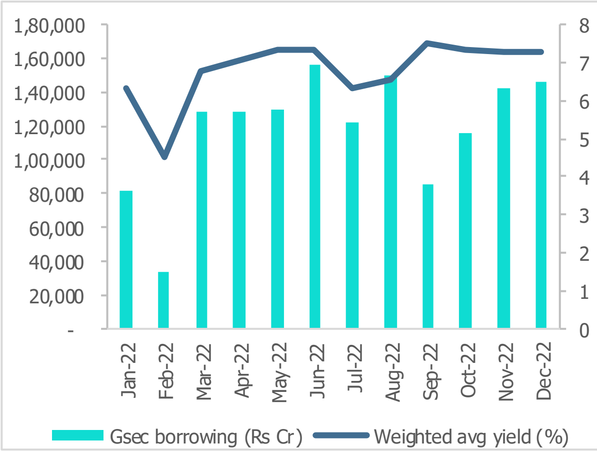
Banking System Liquidity Remains in Deficit



(+ indicates deficit/- denotes surplus)

Net outstanding liquidity injected by RBI i.e. banking system liquidity turned to a deficit this month, largely driven by strong credit offtake, possible RBI intervention and quarter-end advance tax payments.

G-Sec Borrowing and Weighted Average Yield

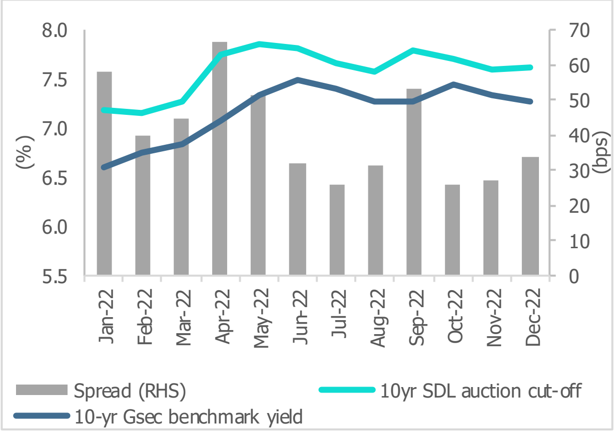


Weighted average yields for G-Secs have increased steadily through the year given the RBI's rate hike cycle.

SDL Borrowing and Weighted Average Yields

Borrowing via SDL slowed down on account of higher GST collections and lower spending. For Q3, SDL borrowing stood at Rs 1,81,111 crore -- 28% lower than what was penciled in the indicative borrowing calendar.

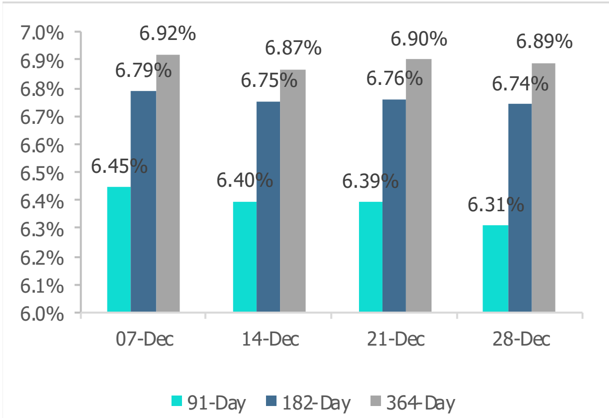
10-year SDL-G-Sec Spreads Widen Marginally



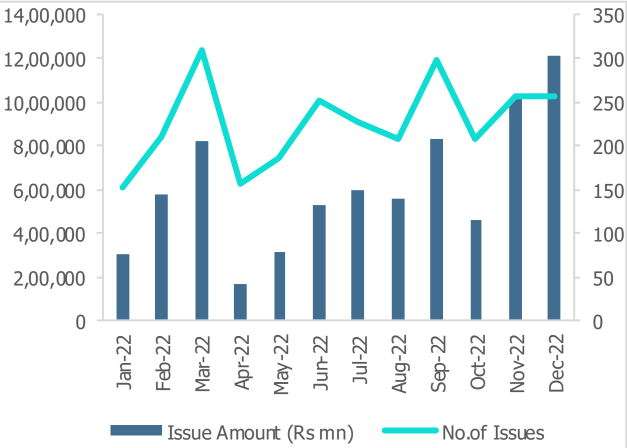
Spread between the 10yr SDL and 10-year benchmark G-Sec yield increased marginally in December from lows seen in Oct-Nov

91-day T-bill Borrowing and Yields

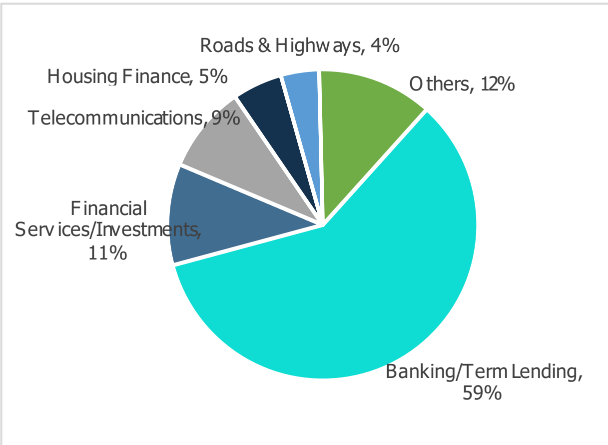
T-bill Cutoff in Dec



Corporate Bonds Issuances Pick Pace in Dec

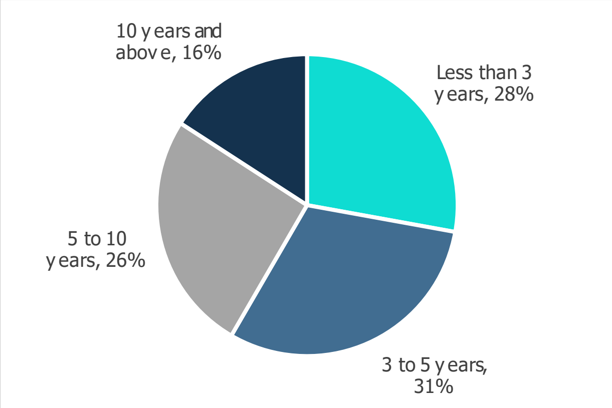


Industry-wise Corporate Bond Issuance (Dec)

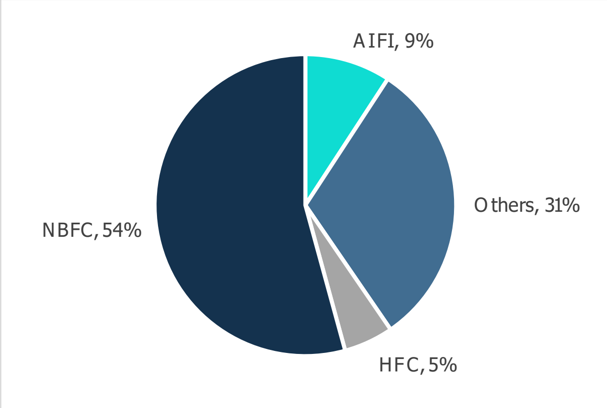


Corporate Bond issuances increased in Nov and Dec. With bank lending rates rising, we could expect some shift to the corporate bond market.

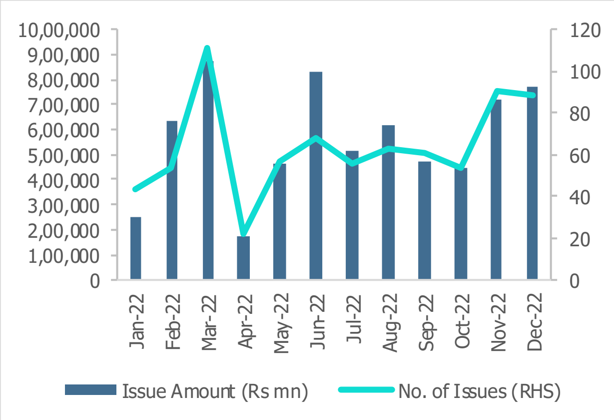
Tenor-wise Corporate Bonds - % Share in Dec



Corporate Bond Issuance Led by NBFCs in Dec

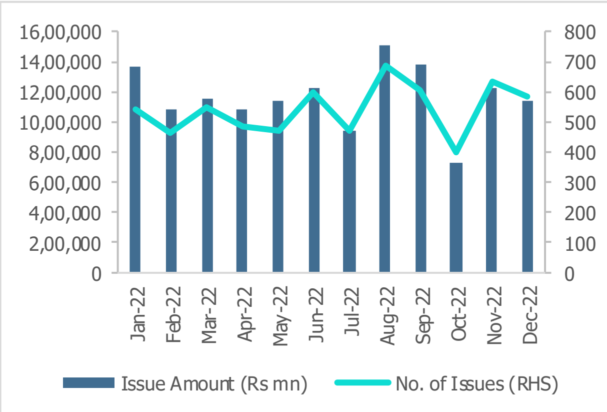


CD Issuances Pick Pace in Q3 FY23



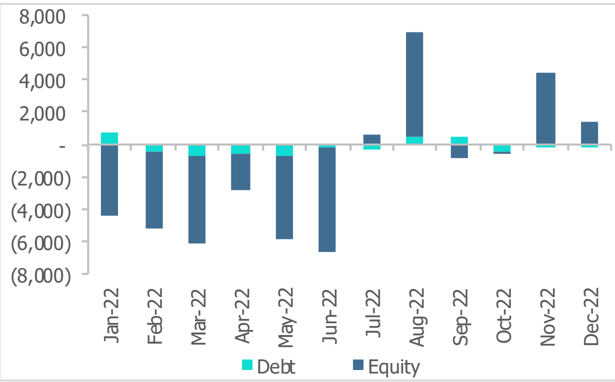
Shrinking surplus liquidity amidst a pickup in credit demand and quarter-end funding requirement led to increase in CD issuances, as compared to previous quarter.

CP Issuance Pace Remains Low



As of end-Dec 2022, issuances totaled Rs 10,439 billion in FY23, nearly 40% lower than the corresponding period a year ago.

Net FPI Flows in Debt Market (USD million)



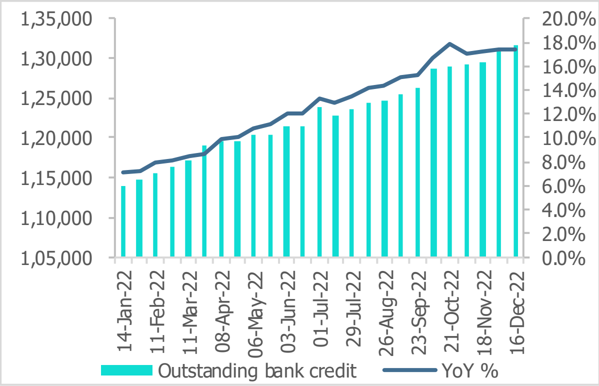
(Does not include debt-VRR and hybrid segment)

FPIs stood as net buyers of $1,155 million in December on account of inflows in equity markets. For 2022 however, FPI's sold $18,522 million. The outflow can be attributed to weakness in the local currency amidst rising interest rates in the US.

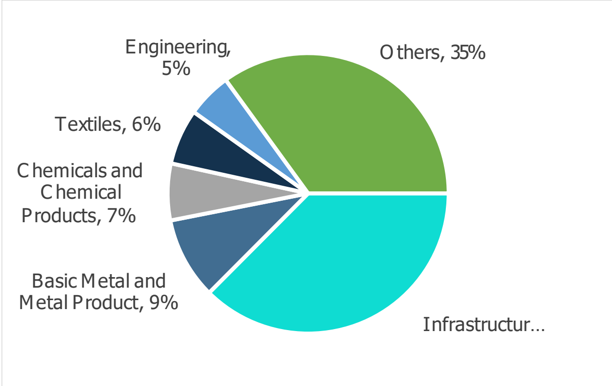
Rupee Weakens 11% in CY 2022

INR depreciated 11% since the start of 2022, its worst decline since 2013. Escalating geopolitical tensions, rising inflation and interest rates globally stood as key triggers for FPI outflows, that weighed on the domestic currency.

Bank Credit Offtake Gains Traction in 2022



Bank Credit Deployment by Industry- % share



(*Data as on Nov 18, 2022)

10-Year Corporate Bond Spreads Over G-sec

	Apr-22			Dec-22		
	PSU, FIs & Banks	NBFC	Corporates	PSU, FIs & Banks	NBFC	Corporates
AAA	0.05	0.12	0.07	0.07	0.38	0.27
AA+	0.37	0.58	0.47	0.56	0.94	0.65
AA	0.74	0.97	0.84	0.93	1.28	1.01
AA-	1.19	1.36	1.27	1.42	1.69	1.42
A+	1.94	3.11	2.52	2.17	3.44	2.67
A	2.19	3.36	2.77	2.42	3.69	2.92
A-	2.44	3.61	3.27	2.67	3.94	3.17
BBB+	2.94	4.11	3.77	3.17	4.44	3.92
BBB	3.19	4.36	4.02	3.42	4.69	4.17
BBB-	3.69	4.86	4.52	3.92	5.19	4.67

Note: Data for this report has been sourced from RBI, CEIC, PRIME DATABASE, FIMMDA

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