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PNB GILTS LTD
(Subsidiary of Punjab National Bank)

Economy & Gilt Watch

INSIDE THE ISSUE

Vaccine Update

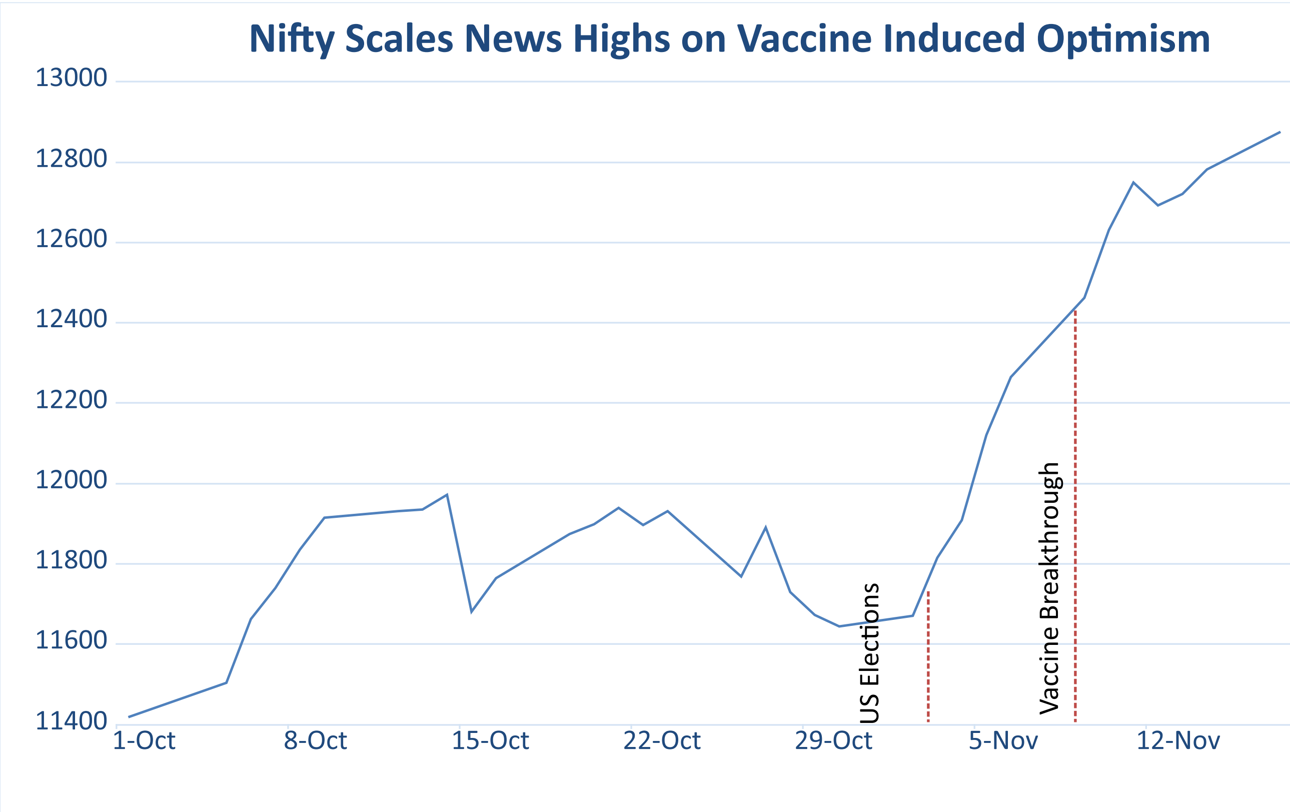
Last week marked a breakthrough in the COVID vaccine development space as Pfizer became the first drug maker to reveal encouraging results from the late stage human clinical trials of its vaccine that it has developed with German partner BioNTech. The Pfizer vaccine has been endorsed by the medical fraternity, given its high degree of efficacy. Joining Pfizer in the race towards the vaccine, is another US drug maker, Moderna Inc which has reported preliminary results from a large trial testing a vaccine, claiming of high effictiveness. Besides, trial results are also due in the next few weeks on a vaccine being developed by British drug manufacturer AstraZeneca and scientists at the University of Oxford. Encouraging data has also been released on the Russian vaccine, Sputnik V. The slew of positive news on vaccine has given a booster shot to the global markets inducing a strong risk on rally across emerging and developed markets. Benchmark index Nifty closed the previous fortnight at a lifetime high, while the Dollar Index weakened as risk appetite made a strong comeback.

Will the markets stay immune?

While the recent development on the vaccine front is a big leap in the fight against COVID, multiple challenges still confront us on this front which may disrupt the exuberance in the markets. While, the vaccine development is being conducted in record time and giving promising results, the COVID infections too are seeing a strong resurgence across the developed countries led by the US which is pacing towards the 200,000 new daily cases mark. Additionally, the journey of the vaccine from developmental stage to large scale immunization across the countries is laden with multiple challenges. The sheer scale of production, logistics and distribution of the vaccine, which will be required, along with concerns on safety and effectiveness of the vaccine shall be key hurdles in way of normalization of economic activity. Another concern is that the immunization at the global level is expected to be completed by not before the end of 2021. Nevertheless, the vaccine news has led to new found confidence amongst the risk takers who have been rewarded by taking risks when uncertainty was at its peak few months back.

Ample liquidity and the new found optimism has the potential to further propel the risk markets like equity with emphasis likely to shift to emerging markets as risk appetite makes a strong comeback. On the real economy also, the vaccine news is expected to have a soothing impact as producers shall have better visibility for planning capacity utilization as well as expansions. Though it could be a tad early to start talking about capacity expansion as the vaccine will take a long time to reach the masses.

Still, even with asset inflation and green shoots in the real economy, the central banks are expected to keep rates lower for longer, till economies are back on a firm footing. However, in India's context, it could be a slightly different story with CPI inflation running out of the upper range successively and inflationary expectations taking firm roots. In such a scenario, RBI maybe earlier than other central banks a bit wary of too much liquidity sloshing in the system, though the policy reversal on repo/reverse repo rates seems to be a possibility in the distant future.

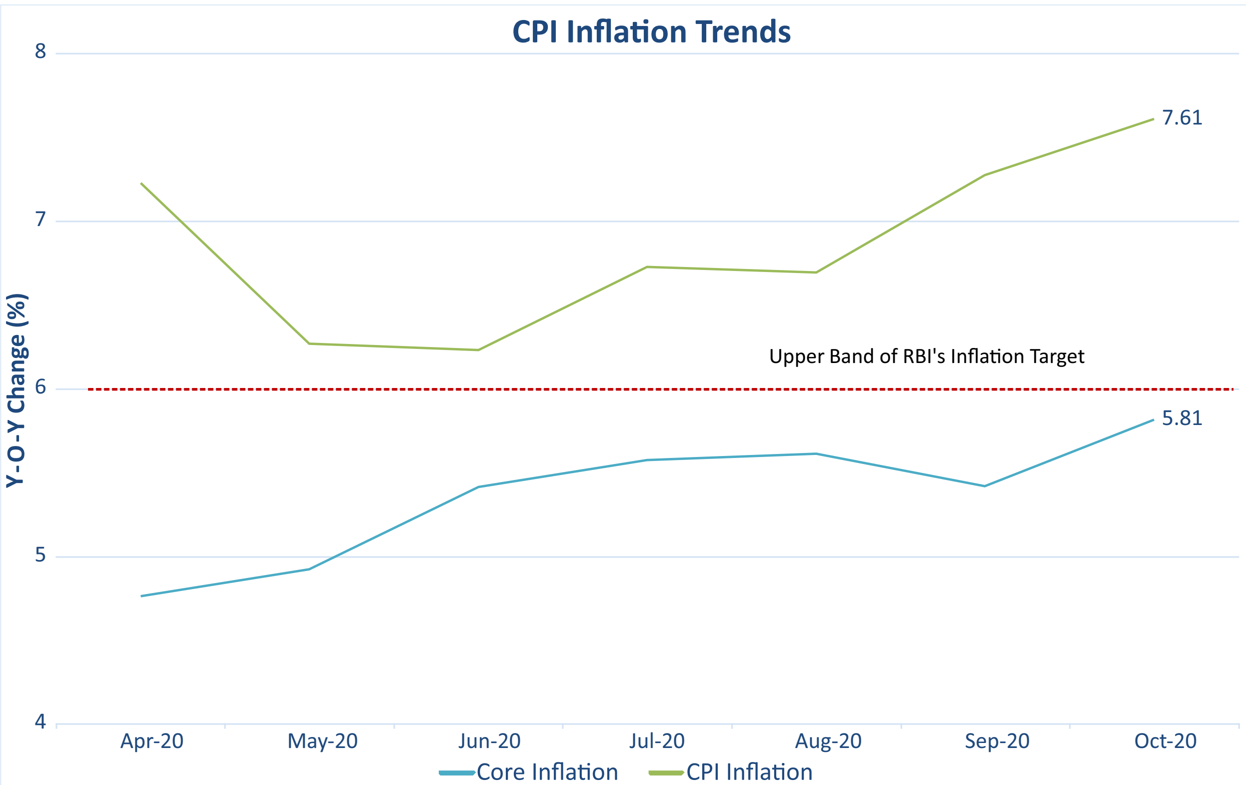


Macro Monitor

Higher Food Prices Push CPI Inflation to a Seven Year High

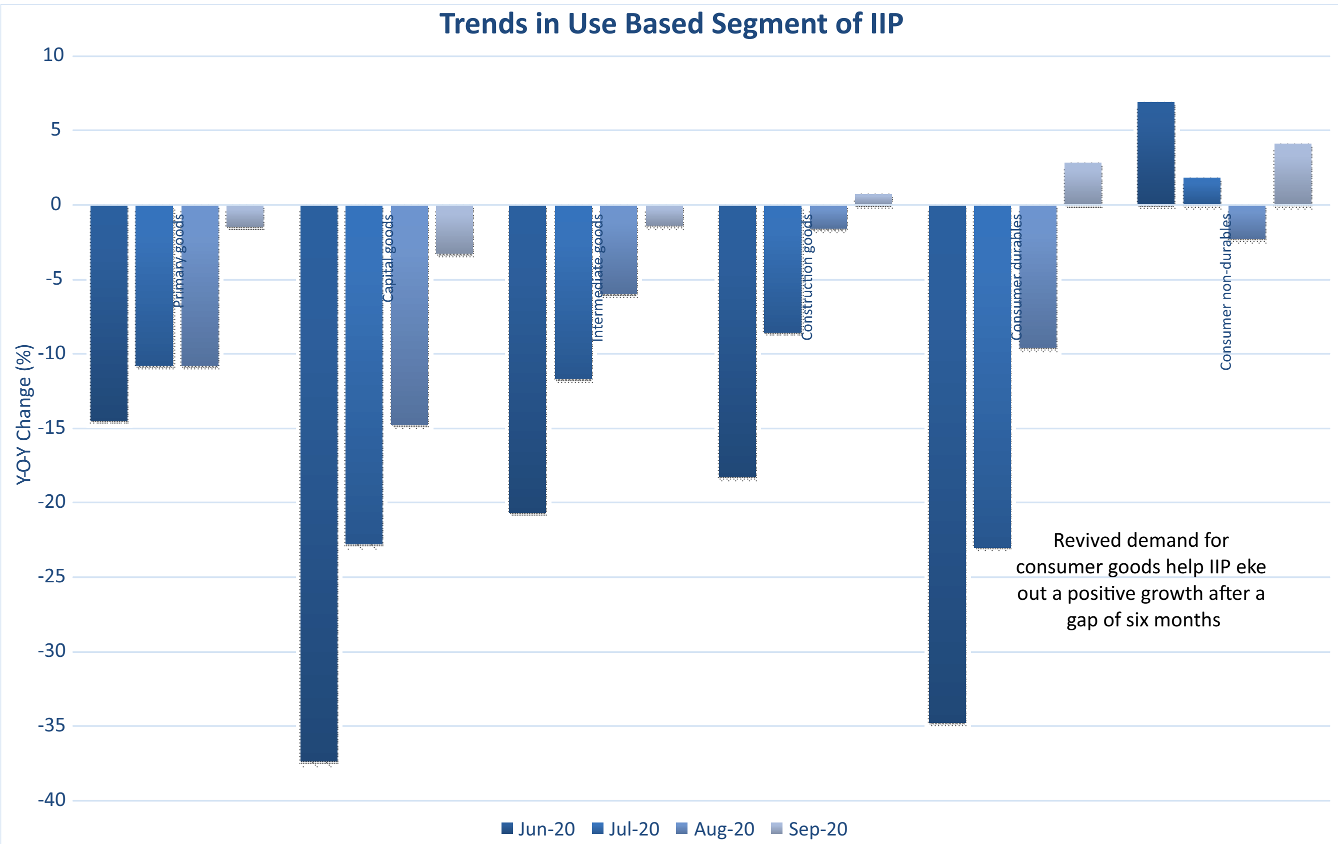
CPI inflation surged further to a seven year high in the month of October to 7.61% as increase in food prices continued to persist. Food inflation which clocked y-o-y rise of 11.1% was led by an increase in vegetable prices (22.5% y-o-y). The rise in food prices was not just limited to perishables. Prices of eggs, meat and fish surged by 21.8% and 18.7% respectively, while prices of pulses also witnessed a spike of 18.3% on y-o-y basis. Core inflation, also moved higher to 5.81% in October vis-à-vis 5.42% in the month of September. Core inflation has remained uncomfortably high as prices of largely non-discretionary consumption items (such as petrol, personal care items, mobile charges, transport charges etc.) continue to remain sticky amid supply disruptions & higher taxes.

The headline inflation has remained rather stubborn and is defying expectations. However, it is expected to recede in the coming months on back of likely cooling off of vegetable prices and a favourable base effect. From policy perspective, RBI has clearly attributed the current inflationary as a supply side phenomenon in the last MPC meet, however, it has cited the "generalization of price pressures and un-anchoring of inflation expectations" as key risk to economic recovery in the November Bulletin released last fortnight.



IIP Climbs Back to Positive Territory

The industrial activity broke into the positive territory, registering a growth for the first time in six months since the onslaught of the COVID crisis. The IIP grew by 0.2% in the month of September as against a de growth of 7.4% in August. On a sectoral basis, electricity & mining registered positive growth during the month growing by 4.9% & 1.4% y-o-y respectively. However, manufacturing sector continued to contract albeit marginally by 0.6% in the same month. Use based trends reflected pick up in seasonal demand as consumer durables and non-durables posted growth of 2.8% and 4.1% respectively. Contraction in all other use segments, i.e. primary, Capital and Intermediate goods narrowed during the month, while construction goods posted a positive growth of 0.7%. The trend in IIP is likely to sustain going in to the festive month of October & November, however whether the trend will sustain in absence of the festive push remains a question.



Fixed Income Outlook

Fundamental View

In line with our expectations, the range of 5.80% to 5.94% continues to hold and there are no compelling reasons for the bond yields to deviate from this range. Nonetheless, the chances that there may be a breakout on the upside are increasing as risk appetite makes a strong comeback in the financial markets. However, RBI's strong resolve to maintain the yields at the current levels may keep an unnatural cap on yields. From a directional perspective, yields may be directed upwards in a gradual fashion as a rejuvenated global risk appetite coupled with sticky domestic inflationary pressures may lead to probable steepening of the yield curve.

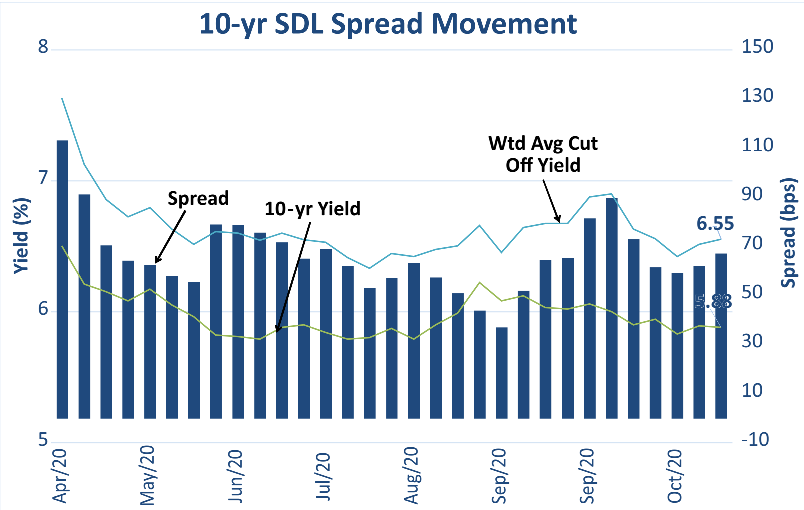
Technical View

Analyst 1: 5.77% GOI 2030 yield settled at 5.88% on Friday's session. Last fortnight benchmark Yield traded range bound between 5.84%-5.92% zone.

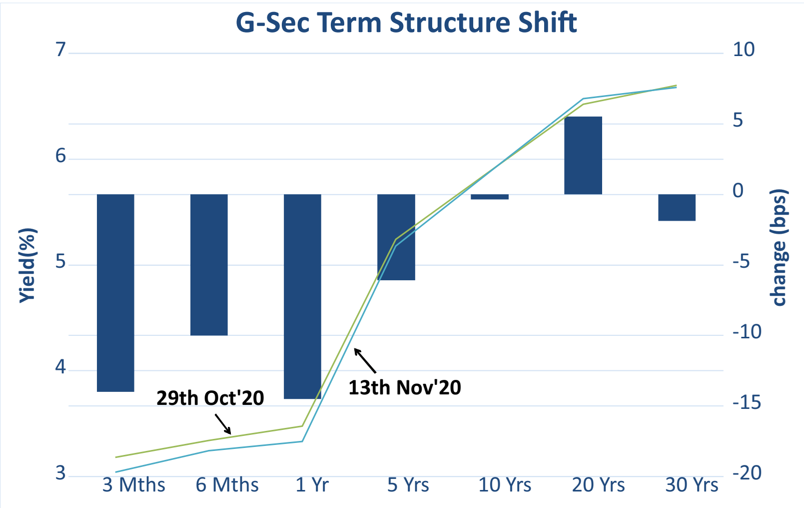
Momentum oscillator RSI is placed around 45 zone and short term moving average i.e. 30 EMA is placed around 5.91% zone. Since first week of October, benchmark is trading in lower low, lower high formation, indicating downward bias. Recent lower high and major resistance zone is placed around 5.91/5.92% zone, which also coincides with 30 EMA level, indicating till yield is sustaining below 5.92% zone markets may witness range bound to downward moves between 5.92% to 5.82% levels.

Analyst 2: As market continues to hover within the same range , the view remains unchanged to stay long , with a closing stop loss of 5.94% and take profit at 5.75%.

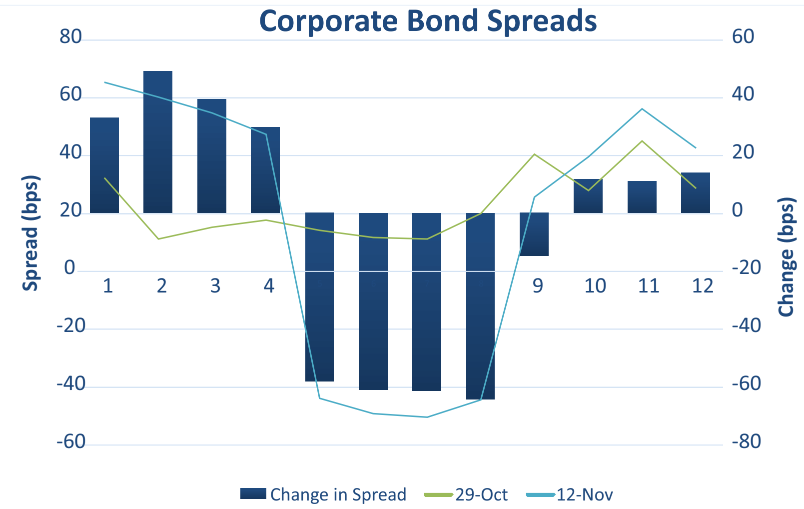
SPREAD MONITOR



SDL yields have inched up as supply in weekly auctions remains considerably large



G-sec curve is poised for further steepening on revival in risk sentiments and unabated domestic inflationary pressures



Corporate bond spreads narrowed in the 5 to 10 year segment in the last fortnight

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