PNB GILTS LTD

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ECONOMY & GILT WATCH

PNB GILTS LTD
(Subsidiary of Punjab National Bank)

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January Headline Inflation: Review

After witnessing upside shocks in the months of November and December with the headline inflation shooting up to 5.69 per cent in December 2023, CPI inflation witnessed moderation in the month of January 2024 majorly on the back of correction in vegetable prices and a favourable base effect. Bearing signs of convergence towards RBI's 4 per cent inflation target, the latest CPI print did bring some respite when it trended down to 5.10 per cent in January 2024, in line with the market expectations of 5.09 per cent. While the lower inflation print has induced expectations of diminishing price pressures, large and repetitive food price shocks keeps them anchored. Further, upside risks to the inflationary trajectory have resurfaced, with the persistent risks from geo-political conflict and volatile commodity prices which is likely to keep RBI vigilant going forward.

On m-o-m basis, all sub-groups, except Food and Beverages witnessed an uptick. Food basket inflation went south by 0.58 per cent, owing to a substantial correction in vegetable prices (-4.21 per cent), followed by fruits and fuel. Key vegetables such as onion and tomato registered a disinflation of 26 per cent and 16 per cent respectively. While the prices of spices and pulses are off the blaze, the cereal prices continue with its rising streak. In an attempt to tame cereal inflation, the Centre has decided to sell subsidised 'Bharat Rice' in the retail markets.

The core inflation has moderated considerably over the months owing to a favourable base effect.

What lies ahead?

Tracking the price movement in key food items for the current month (based on data available till date), it can be observed that cereals continue to be on the uptrend, with both rice and wheat exhibiting signs of increase. Under spices, salt has also moved up. Other categories including vegetables, oil, pulses and sugar continue to witness moderation in prices.

In the last policy meet, the Reserve Bank held its policy rate constant at 6.50 per cent with no change in stance. The CPI projection for FY 2024 was also retained at 5.4 per cent which is likely to be undershot marginally. Medium term prospects of food inflation look optimistic with the fading off the El Nino and phasing in of La Nina event, which will be accompanied with improved rainfall in the current year.

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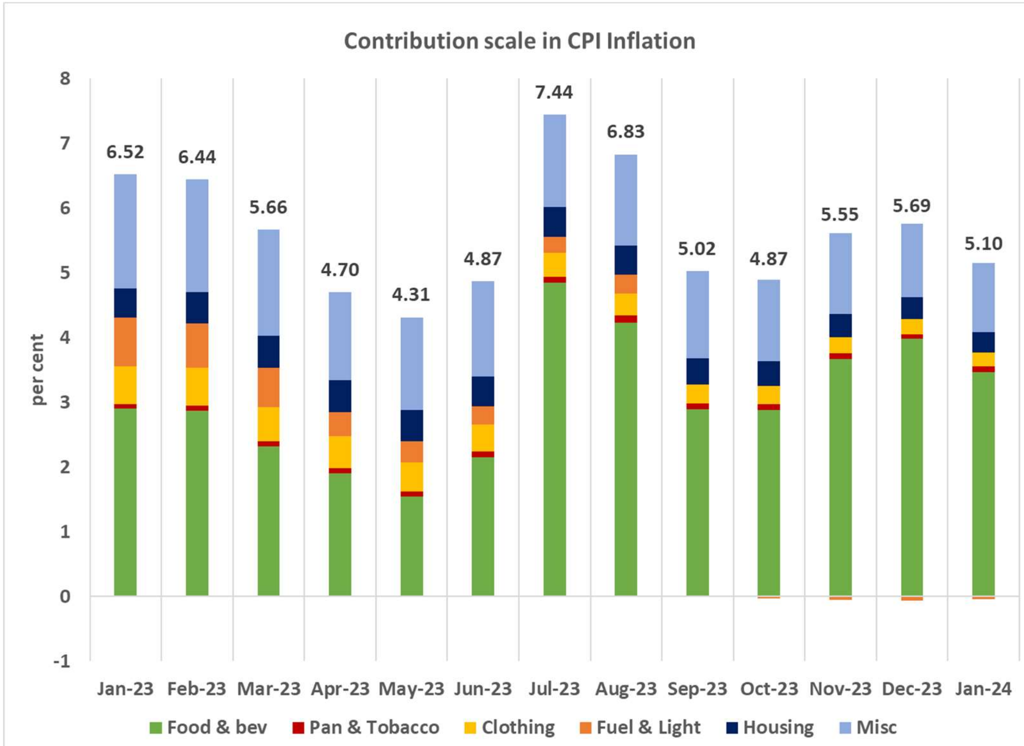

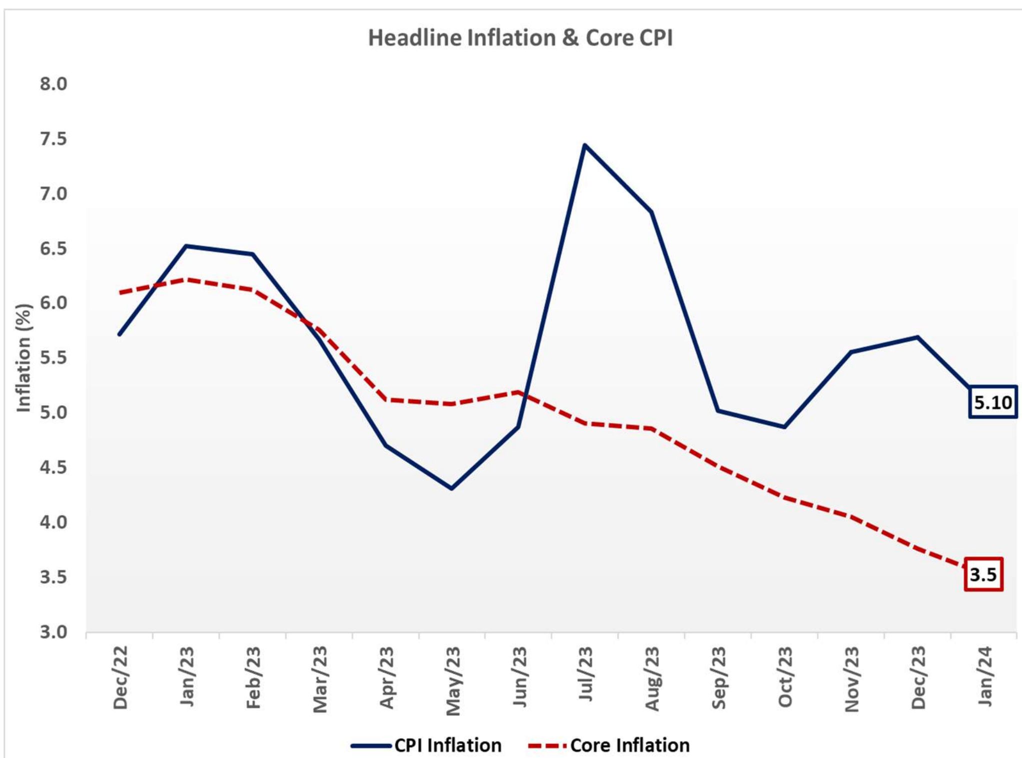

Macro Monitor

Undeterred by the global headwinds, merchandise trade deficit narrows to a nine-month low

Despite the global headwinds in the form of red sea crisis, recessionary risks in advanced economies and falling commodity prices, India's trade deficit narrowed to 17.5 USD billion in January 2024 after peaking in October 2023 at 31.5 USD billion. The trade gap reduced on the back of fall in merchandise imports and exports.

While merchandise imports fell by around 7 per cent, merchandise exports declined marginally by 4 per cent primarily on the back of the Red Sea crisis. The government's efforts towards exports growth have helped in creating a positive environment for exporters while mitigating external risks.

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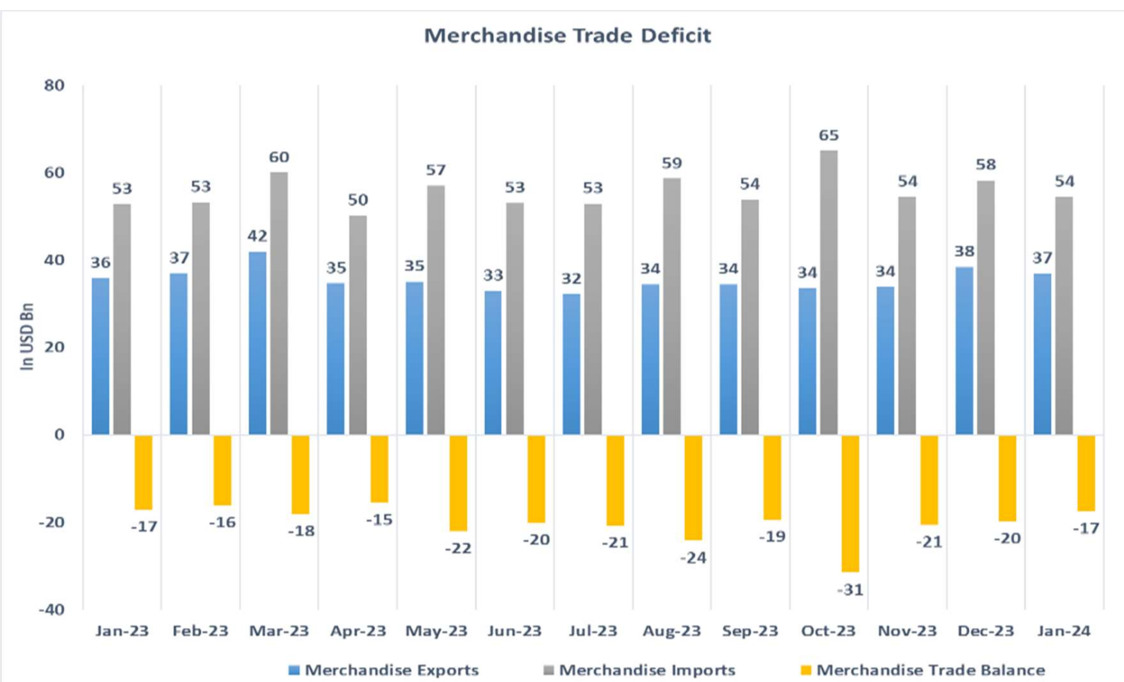
Petroleum products, engineering goods, iron ore, electronic goods, drugs and pharmaceuticals exhibited resilience and topped the merchandise export list for January 2024. Along with a positive 3 per cent y-o-y growth in merchandise exports, there was a considerable push from the service export segment to the overall trade deficit. Quite recently, service exports are seen picking up and offsetting the gap caused by higher merchandise imports and thereby, contributed significantly towards shrinking of the Current Account Deficit (CAD). Going forward, a resilience in service exports can help in overcoming the weaknesses of merchandise exports in order to narrow the CAD gap.



Source: Ministry of Commerce and Industry

Fixed Income Outlook

Fundamental View

Any reversal in flattening looks unlikely at the moment as RBI is unlikely to put its guard down anytime soon or unless liquidity deficits are brought down further

The domestic bond markets gave up budget induced gains in the previous fortnight, as RBI MPC continued with its disinflationary narrative in the February monetary policy and kept its stance unchanged at “withdrawal of accommodation.” Post budget bull flattening was thus followed by post MPC bear flattening, which rendered the 1 yr-30 yr term premia squeezed to ~5 bps by the end of the fortnight. The 10-yr benchmark yield edged up from lows of 7.06 per cent to close the fortnight at 7.10 per cent. A surge in US bond yields on account of higher than expected US CPI data for the month of Jan also soured sentiments in the domestic market. The coming fortnight, will see release of both US Fed and RBI MPC minutes. RBI MPC minutes will be especially watched, as the February policy saw vote in favour of a 25 bps rate cut by Prof. Varma. Dr. Ashima Goyal’s commentary amidst rising real rate of interest will be of key interest as her dovish tilt is likely to build further dissent in the MPC decision making in forthcoming meets. A slight positive for the bond markets is absence of C-Gsec supplies in the remaining part of FY, which may keep demand in secondary market buoyant and yields softer. Any reversal in flattening looks unlikely at the current as RBI is unlikely to put its guard down anytime soon or unless liquidity deficits are brought down further to align the overnight money market rates with the policy repo rate.

SDL Overview

During the last fortnight, 10 Yr. State Loans traded in the broad range of 7.40%-7.50%, whereas the 10 Yr. CG benchmark, remained in the range of 7.04%-7.14%. The spread between yields on the 10-year state bonds and the benchmark 10-year government bond eased and traded in the range of 35-40 bps from 40-50 bps last fortnight.

So far, in the Q4, the amount raised by state governments has been ~37% lower than the indicative amount (Rs 1,49,701.738 vs 2,05,345)The lower supply was partly on account of the upward revision in tax devolution in the revised estimates for FY 24 by the Centre in the interim budget.

However, we expect states to step up borrowing in the second half of 4th quarter, as indicated by the trend in previous years. This is likely to result in widening of yield spread between the 10-year state governments’ loans and the benchmark 10-year G-sec to 37-42 bps.

Technical View

Technical Synopsis 7.18% GS 2033 Yield:

7.18% G Sec 2033 settled at 7.0968% on Friday's session. As discussed in last Newsletter that Benchmark may see time wise correction in zone of 7.04% to 7.14%, The same was witnessed in passing Fortnight.

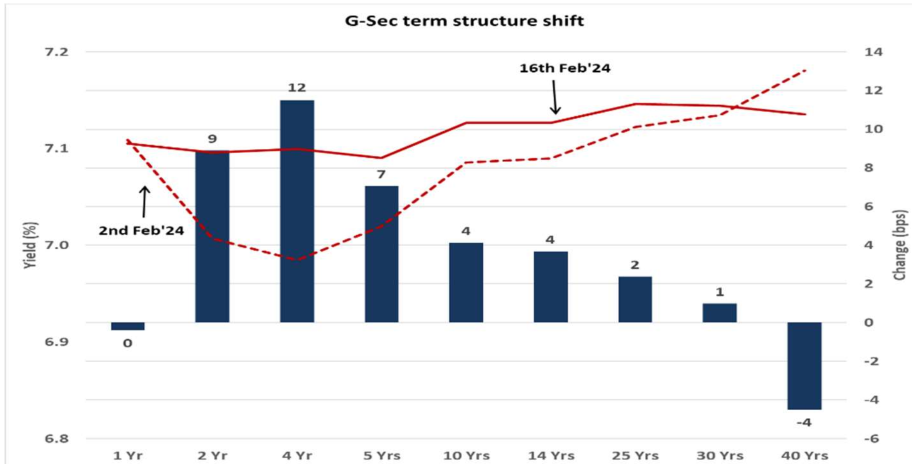
Momentum oscillator RSI is hovering around 40-42 zone. We have witnessed a Symmetrical triangle breakout below 7.14% on 1st Feb'24, which also coincide with 30EMA level, indicating trend in favour of softening yields. Going forward, we may continue to see consolidation between 7.04% to 7.15% zone. However, any sustainability below 7.04% will open gate for 6.98% level, on higher side 7.15% to act as crucial rest level

Going forward, we may continue to see consolidation between 7.04% to 7.15% zone

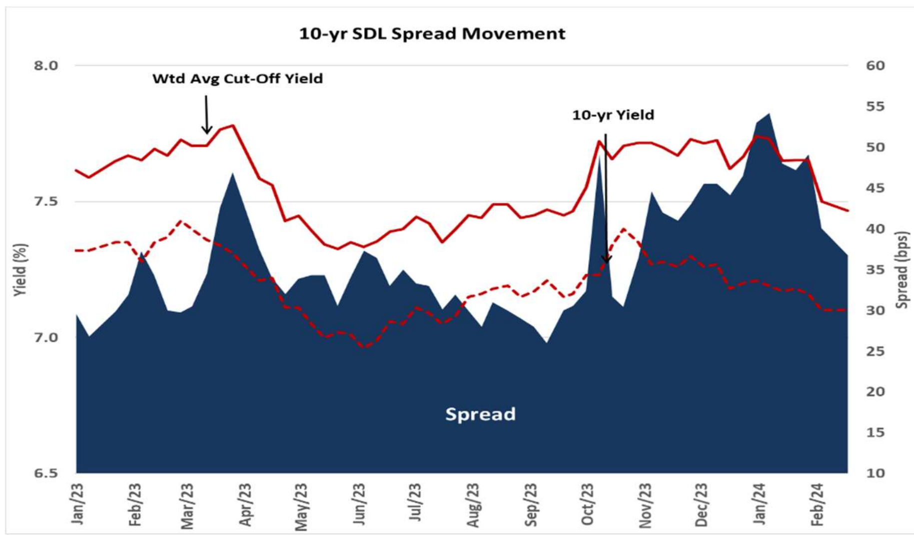
Running Chart GOI 10yr Daily. Source: Tickerplant

Spread Monitor

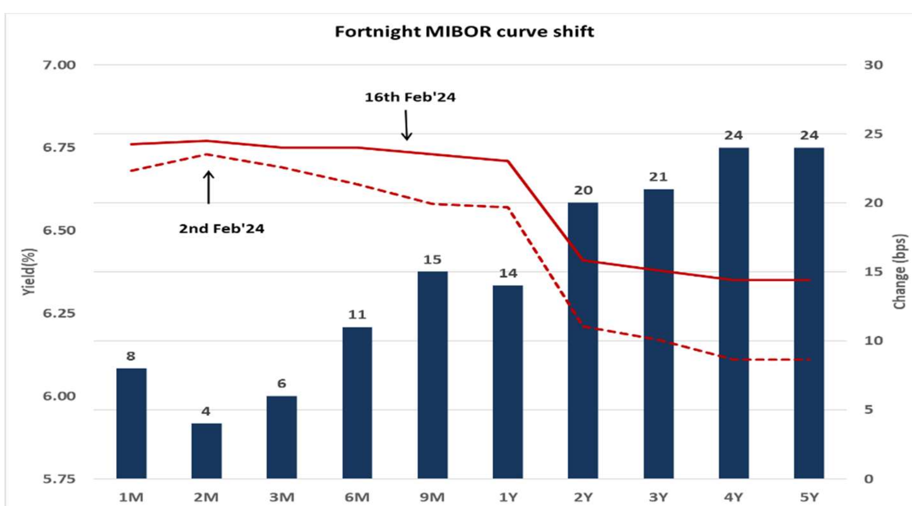
The G-sec curve shifts upwards with a flattening bias



The spread between yields on the 10-year state bonds and the benchmark 10-year government bond eased and traded in the range of 35-40



OIS curve shifts upwards tracking rise in US treasury yields



PNB Gilts Ltd, a renowned and preferred name in the Indian debt market was one of the first entities to be granted the Primary Dealership License by the Reserve Bank of India. The company is also a subsidiary of one of the largest Indian commercial banks, Punjab National Bank. Company has played a pivotal role in strengthening of the domestic fixed income markets and is a dominant player, marking its presence with significantly high market share in the overall trading turnover.

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