

ECONOMY & GILT WATCH



(Subsidiary of Punjab National Bank)

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RBI's dividend payout: Nearly three times higher than FY'22

The announcement of surplus transfer by RBI to the Centre was eagerly awaited by the market participants, who had priced in and anticipated an amount as high as Rs. 1-1.5 lakh crore. On May 19th, post the announcement, the benchmark 10-year G-sec yield climbed 5 basis points higher at 7.05%, as a reaction to the lower than expected amount of dividend payout.

The 602nd meeting of the Central Board of Directors of RBI concluded on Friday, under the chairmanship of Governor Shaktikanta Das, where the Board gave a nod to surplus transfer of Rs. 87,416 crore to the Centre for FY 2023. The Contingency Risk Buffer was also raised from 5.50% to 6%. Further, "The Board in its meeting reviewed the global and domestic economic situation and associated challenges including the impact of current global geopolitical developments," the release mentioned.

Given the budget estimate of Rs. 48,000 crore by way of dividend receipts from the Central Bank and other state-owned lenders, RBI seems to have managed to overshoot the surplus even when the days were rainy. The last year was not an easy one, with sharp hikes in global interest rates posing an elevated risk in the form of higher mark-to-market losses on RBI's investments. On borrowing incidents from history, we may recall that FY2022 also witnessed rising global interest rates, following which the Central Bank had to make higher provisions of Rs. 1.15 lakh crore towards the Contingency fund. Consequently, only Rs. 30,307 crore were transferred in the form of dividend, which was considerably lesser than the budget estimate of Rs. 73,948 crore.

Joining the dots

RBI's surplus has surpassed its estimate primarily on the back of foreign exchange volatility, which aided in bagging good profits on sale of the greenbacks and paid a higher interest income on local as well as foreign treasuries. The gains, however, were limited due to considerable mark-to-market losses on foreign securities, which were charged with an additional layer of buffer.

Selling dollars has a double impact on the Central Bank's coffer. For one, the economists peg the historical average acquisition cost of US dollar to be in the range of Rs. 62-65 per dollar, and given the median monthly exchange rate to be in the

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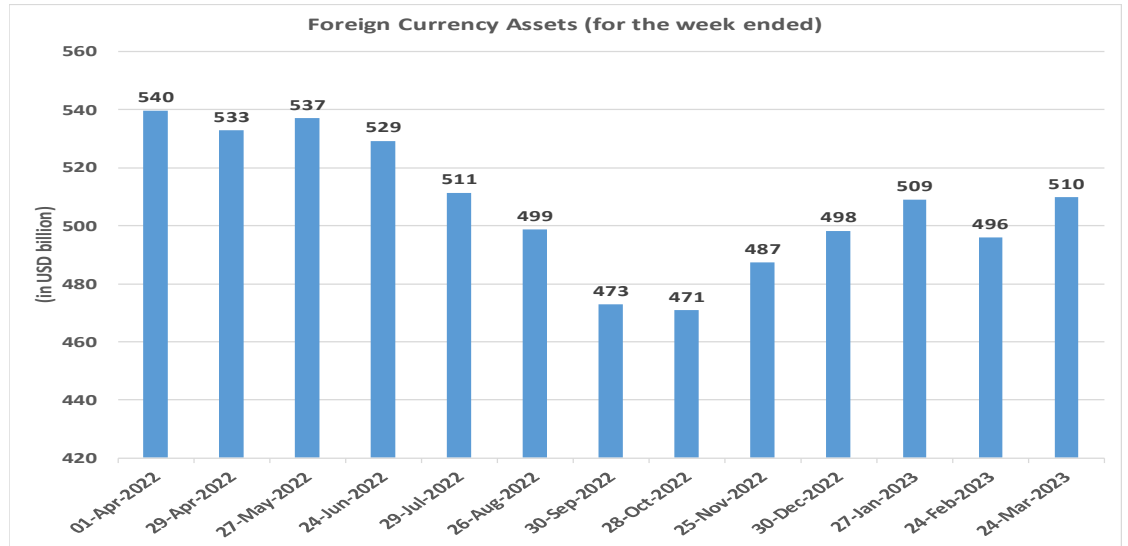
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of approximately Rs. 76 – 82 per dollar for FY2023, the sale of foreign currency would have generated substantial revenue for RBI. Second, a decline in the balance sheet asks for lesser provisioning charges.

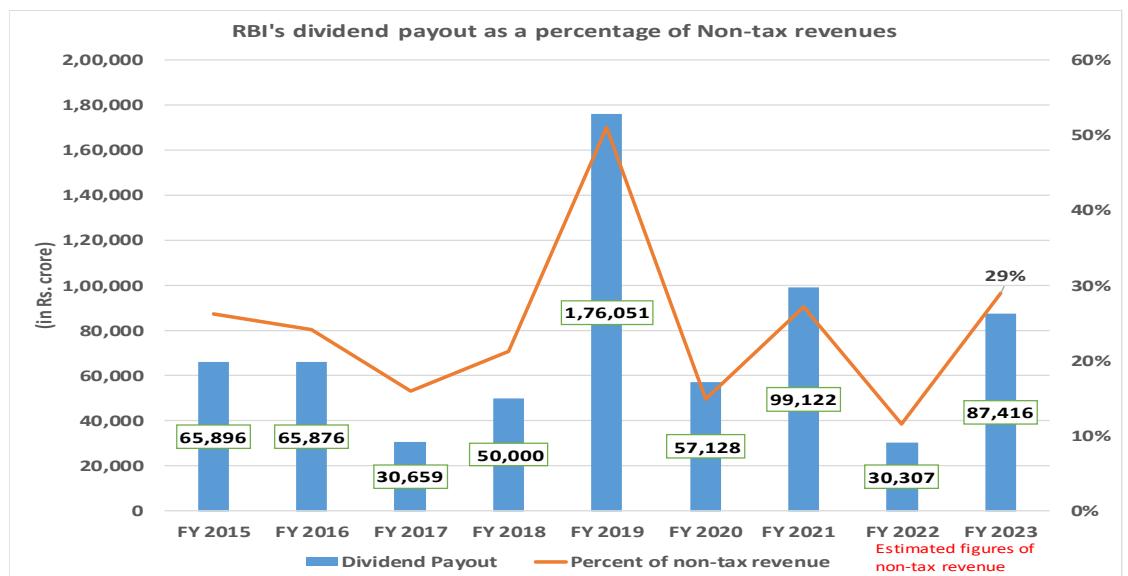
This additional bounty of Rs. 40,000 crore would come as a sigh of relief for the Government to contain the fiscal deficit with some ease.



Source: RBI database

From a fiscal perspective

This additional bounty of Rs. 40,000 crore would come as a sigh of relief for the Government to contain the fiscal deficit with some ease, with the dividend corpus accounting for an additional revenue of around 0.2% of GDP. While the Public Sector Banks have also reported good profits, higher dividends are also expected from the oil marketing companies, resulting in possibly higher flows from these source as well. Therefore, a higher non-tax revenue bears the news of joy for the Centre to make more space for offsetting disinvestment losses, without taking any hit on the subsidies.



Source: RBI & Budget documents

Macro Monitor

India's April 2023 Merchandise Trade Deficit hits a 21-month low

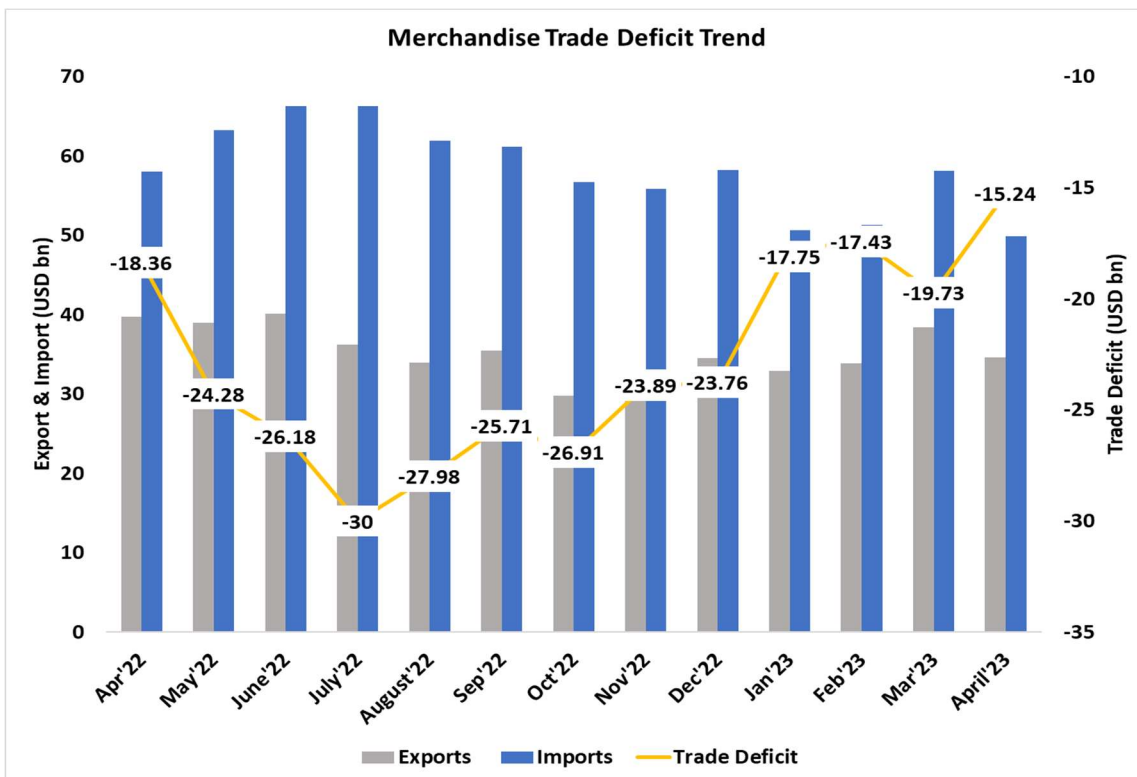
India's merchandise trade deficit was recorded at the lowest in 21 months at 15.24 USD billion, on the back of slacking domestic demand and a moderation in commodity prices, pulling down the import bill.

The merchandise imports fell by 14.1% y-o-y in April 2023, tracking a drop in petroleum, crude and products. Oil imports went south by 2.46% y-o-y to 15.17 USD billion. Amidst a bleak global outlook, significant decline was observed in imports of discretionary items such as gems and jewellery.

However, despite the global headwinds, engineering goods, exhibiting resilience, topped the merchandise export list for April 2023. Even though, the merchandise exports recorded a y-o-y fall of 12.7% in the same month, there was a considerable push from the service export segment in the overall trade deficit.

During Q3 FY2023, service exports were seen offsetting the gap caused by higher 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.

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Fixed Income Outlook

Fundamental View

Indian bond yields continued to drift lower in the previous fortnight, with the 10-yr yield dipping below the 7% mark, levels last seen in April 2022. Better than expected domestic inflation data, expectations of growth facing headwinds gave way to cementing of prolonged pause by the MPC. Markets were also positive as RBI was expected to announce a higher than budgeted dividend for FY2024. On Friday, the RBI dividend to the government was announced at Rs. 87,416 crore as against total budgeted dividend income of Rs. 48,000 crore for the current fiscal. Another key event was withdrawal of Rs. 2000 denomination notes from circulation, the exchange or deposit deadline for which has been set at 30th Sep'23. The total value of these notes has been pegged at Rs. 3.62 lakh crore by RBI and this move is expected to infuse liquidity back into the banking system in a graded manner. The extent of liquidity infusion would however depend on the extent of deposits/exchange made by the public with the banks. Going ahead into the next fortnight, the Q4 GDP data release will be keenly watched and any signs on weakness is likely to give another leg up the the ongoing bond market rally. We expect the short end of the curve to outperform, given the expected infusion of liquidity and rising expectations of a rate cut in the current financial year itself.

SDL Overview

During the last fortnight, 10 Yr. State Loans traded in the broad range of 7.30-7.41, whereas the 10 Yr. CG benchmark, remained in the range of 6.94-7.06. The spread between 10 year SGS and G-Secs currently hovers in the band of 30 to 35 bps as indicated by us in the previous issue of Economy & Gilts Watch dated 8th May 2023. Fundraising by states through issuance of SGS has remained lower, so far, vis-à-vis their scheduled figure. In the first seven weekly auctions held in Q1 FY24, so far, the state government have borrowed Rs. 55,700 Cr which is a sharp 40% lower than the budgeted amount of Rs. 92,100 Cr.

We expect States to continue to raise a lower amount than the calendar amount in the next fortnight as well. With banks restocking their sold inventory preferentially with SGSs (Many PSU banks booking profit after switching from HTM to AFS), demand for SGSs remained stable, we expect the spread between 10 Yr SGS and CG to trade in the range of 30-35 in the upcoming fortnight as well.

Technical View

Technical Synopsis 7.26% GS 2033 Yield:

7.26% G Sec 2033 Yield settled at 7.0106% on Friday's session. Passing week Benchmark met its bear flag target as it touched level of 6.95%.

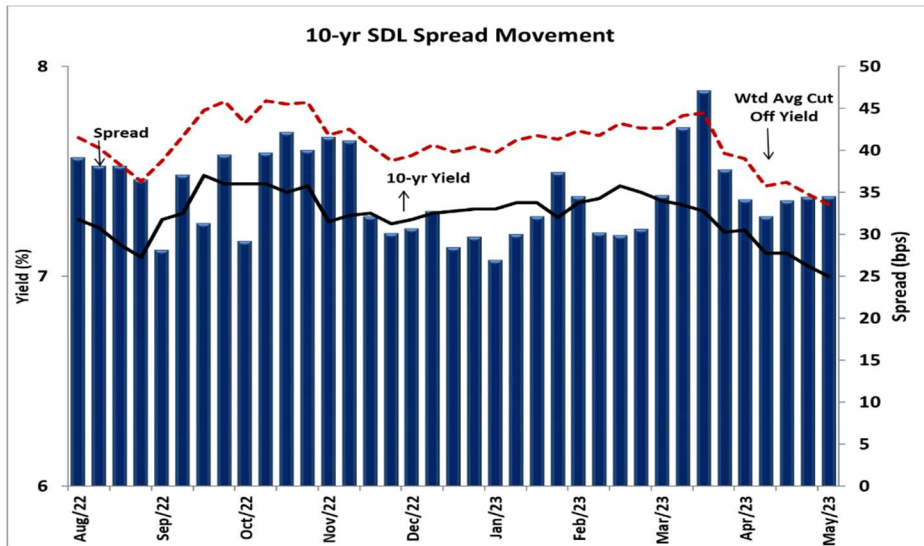
On weekly chart it is trading in falling channel pattern (as visible above), with 10yr taking support around lower band of the pattern, indicates 6.94% won't be easy to breach on lower side. On higher side immediate resistance is placed around 7.02%-7.06% levels. Going forward, we may see 10yr to trade in broader range of 6.94% to 7.06% and either side break will decide the further directional move in the Benchmark.

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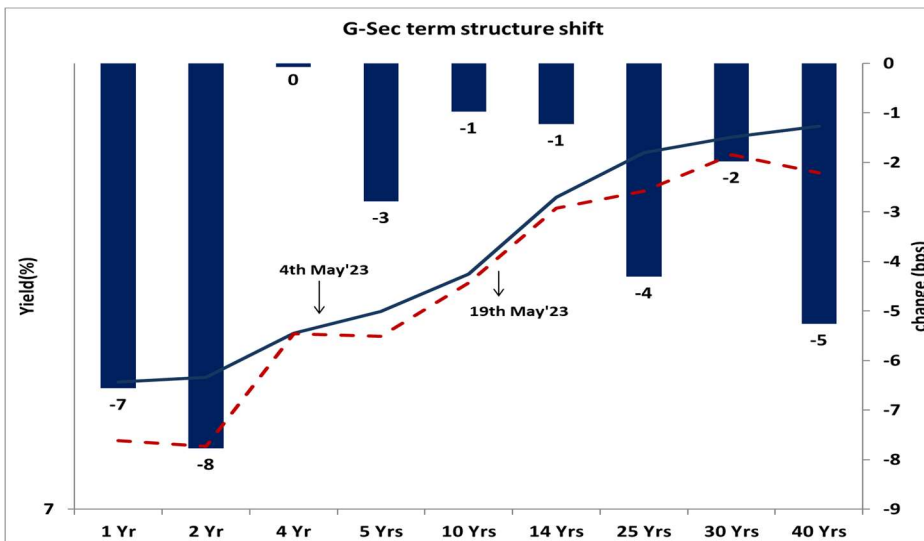


Running Chart GOI 10yr Daily. Source: Tickerplant

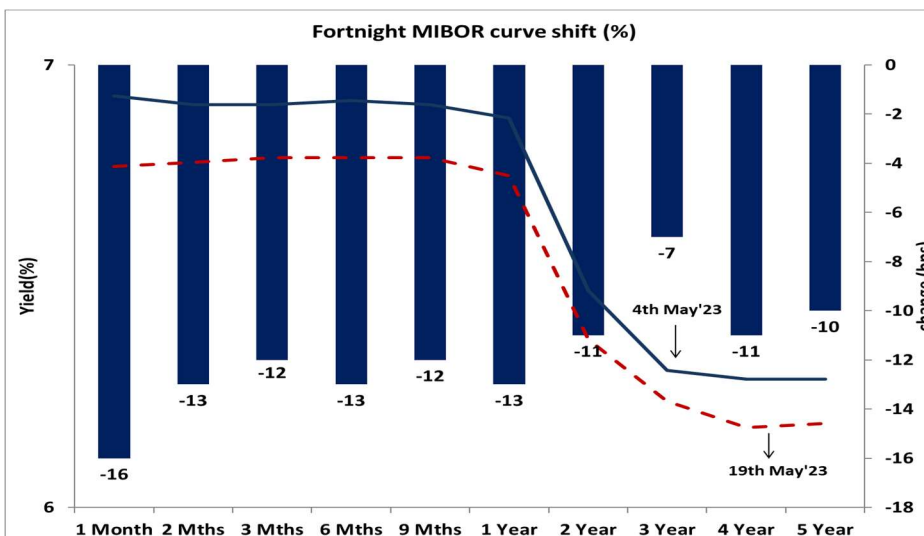
Spread Monitor



10-yr SDL spreads are expected to trade in the range of 30 to 35 bps in the upcoming fortnight as well.



G-sec bond yields continued to drift lower in the previous fortnight, with the 10-yr yield dipping below the 7% mark.



2-5 yr OIS rates slashed tracking the fall in Indian treasury yields



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