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Policy Rates : Future Path
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Policy Rates: Future Path

Recently we have had rates decisions coming in from major central Banks with the US Fed and Bank of England keeping rates at same level and Bank of Japan finally moving **past the NIRP** and raising rates for the **first time in 17 years**. At the outset, **BoJ's decision to hike overnight rates to positive range** mark a monumental shift, the devil lies in the details. The BoJ while scrapping YCC on 10 year JGBs and buying of ETFs and REITs, it **did not commit to a hiking cycle and signalled slow hikes** if any. Bank of England on the other made a statement about considering rate cuts in the coming meetings **keeping in mind** the growth-inflation dynamics. Most important of all, the Fed **maintained the policy rate** while the dot plot also suggested 3 cuts this year which was already priced in by the market.

Above positioning by the leading Central Banks suggest to a more cautious and data driven approach to rate cuts going forward. Particularly striking is the Fed's approach of being sensitive to data. Fed's commentaries and stance has ensured that the market which was pricing in close to **6 rate cuts in 2024** end is now pricing in just **3 rate cuts**. Also, in spite of a clear downward trend in successive inflation prints the figures still remain **above the 2% target** which make it imperative for the fed to be more data driven. Apart from the persistent strength economic data, the fed is also **cognizant of the huge liquidity** which was injected into the economy to tackle inflation.

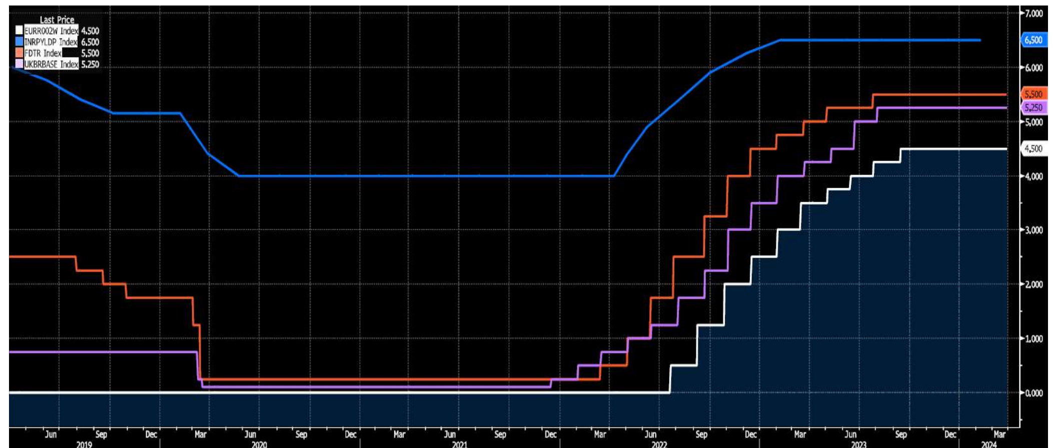
Above approach by central banks suggest towards a more balanced approach by Central Banks and not taking a decisively hawkish or dovish stance for the time being. This should be the template for other Central Banks to take a cue from going forward. But considering the increasingly independent nature of Emerging Markets in particular, it is likely that the Data Driven template remains confined to Developed Market economies.

Risks to Data Driven approach:

While the benign macro environment makes sense for Central Banks to wait and watch. Significant risks to above approach do exist in the form of – **i) Geopolitical Risk:** There is a significant risk of flare ups which can upend relatively stable commodities markets. Such events pose risks of sending inflationary shocks across economies particularly import dependent such as India **ii.) Financial Markets**

While leading CBs can provide sooner or later cut, RBI is expected to exercise discretion in its monetary policy

Contagion: If rates remain high for longer than the break point of certain sections of the financial markets, there is a possibility of defaults materialising. Similar risks have surfaced previously with US regional banks crisis last year **iii.) Stagflation:** With generous liquidity injection to tackle the Covid slowdown, the surplus cash in the system can lead to stagflationary conditions in case there is a global slowdown due to above reasons.



Source : Bloomberg

GOI Borrowing Calender FY 2024-25

Healthy Tax collection projections basis strength in economic growth also likely to support less borrowing

The government plans to borrow **Rs 7.5 Lac Crores** of the total borrowing plan of **Rs 14.13 Lac Crores total** borrowing plan. The 53% share for H1FY25 is around 15% less than the amount notified for H1FY24 and augurs well for the G-Sec yields going forward. As part of new developments the existing **14 year paper** has been **replaced** with the introduction of **15 year paper**. Also, the government plans to issue **Green Bonds worth Rs 12,000 Crore** in H1FY25 against the usual issuance in second half of the year. With first hald borrowing coming in lower than market **consensus of ~58%** and bond index inclusion related inflows G-Sec yields are expected to soften

Tenure	Amount in Rs Cr	% of H1FY25
3-Year	36,000	4.80%
5-Year	72,000	9.60%
7-Year	66,000	8.80%
10-Year	192,000	25.60%
15-Year	104,025	13.87%
30-Year	66,975	8.93%
40-Year	146,025	19.47%
50-Year	66,975	8.93%
H1FY25 Total	750,000	

Fixed Income Outlook

Fundamental View

During the last fortnight, benchmark 10 Year yield touched the March high of 7.10-11 on 20th March. FPI related bond flows seemed to have slowed down during the later half of March month most likely due to investors sitting out the usual FX and Rates volatility associated with Financial Year end close. Particularly notable was the price action on 22nd March when USDINR pair closed at a record low of 83.43 and the post 3:30 PM sudden depreciation of INR prompted unhedged bond investors to square off their positions putting pressure on yields. With RBI coming in to decisively support the Rupee the following week, fears of currency risk were contained as G-Sec traded with their downward yield bias.

The market is going to react primarily to MPC followed by bond inflow

Looking forward, market positioning is likely to be around the all important MPC on 5th April which can give direction to the yields which have traded sideways with a downward trending bias. Also, post MPC, FPIs are expected to ramp up their investments after assessing the market sentiment. In absense of any surprises, the expected range is 7.00%-7.10% for the coming fortnight.

SDL Overview

The final fortnight of FY24 saw the 10Y SGS vs benchmark 10Y G-sec yield spread widening further and trading in the range of 37-43 bps, which is in accordance with our outlook shared in the previous newsletter. This is mostly due to heavy borrowings by State Governments in Q4, which reached Rs.4.03 lakh crores against the scheduled figure of Rs.4.13 lakh crores. During FY24, State governments have raised their Gross borrowings to a total of Rs.10.07 lakh crores vs Rs.7.58 lakh crores in FY23 (~32% higher). Accordingly, the Net Borrowing of State Governments stands at Rs.7.15 lakh crores in FY24 vs Rs.5.18 lakh crores in FY23 (~38% higher).

Above expectation state government borrowings are likely to keep CG-SG spreads elevated

With the bond market participants expecting about Rs 2 - 2.15 lakh crores Sate Govt Borrowings in Q1 of FY25, the release of the auction calendar indicating State Govt borrowings amounting to Rs 2.54 lakh crores has taken the market by surprise. Considering this event, we expect the 10Y SGS vs benchmark 10Y G-sec yield spread to continue staying elevated at 37-43 bps during the coming fortnight.

Technical View

Technical Synopsis 7.18% GS 2033 Yield:

7.18% settled at 7.0556% on Friday's session. As discussed in last newsletter, Benchmark may trade in range of 7.02% to 7.10%, the same was witnessed in passing Fortnight as 10yr settled shop in the middle of the range.

Momentum oscillator RSI is currently valued at 46. Post witnessing divergence between RSI and Yield we have seen a decent pullback However, on higher side 7.10%-7.11% to act as crucial resistance zone for coming days. Going forward with major events lined up for the coming week, any sustainability above 7.11% may trigger breakout and we may see surge towards 7.18%-7.19% in short span of time, on lower side immediate support is placed around 7.02% and 6.98% levels.

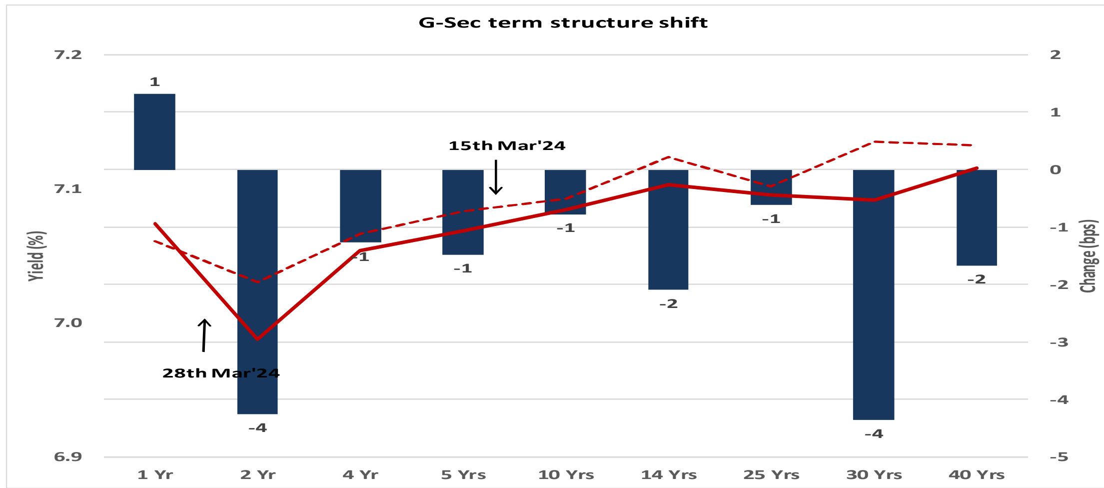
Running Chart GOI 10yr Daily. Source: Tickerplant

Liquidity

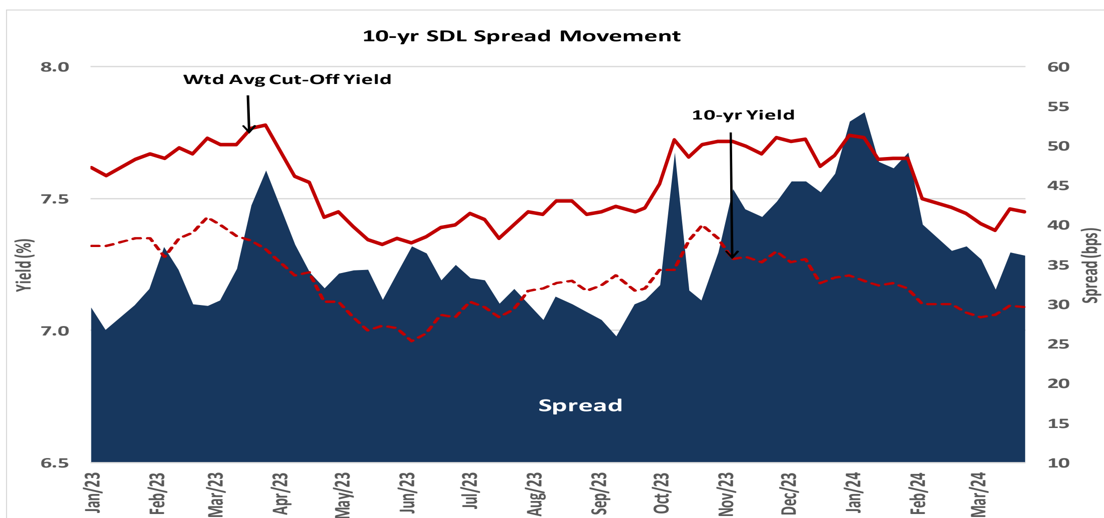
There was pressure in the money market rates due to Tax outflows and on account of Financial Year Closing, overnight MIBOR shoots to 7.90 highest in this FY 24.Going forward we will see some easing in money market rates as banks will be on Lending side.

As RBI reiterated in last MPC that the Reserve Bank remains nimble and flexible in its liquidity management through two-way main and fine-tuning operations, in both repo and reverse repo.

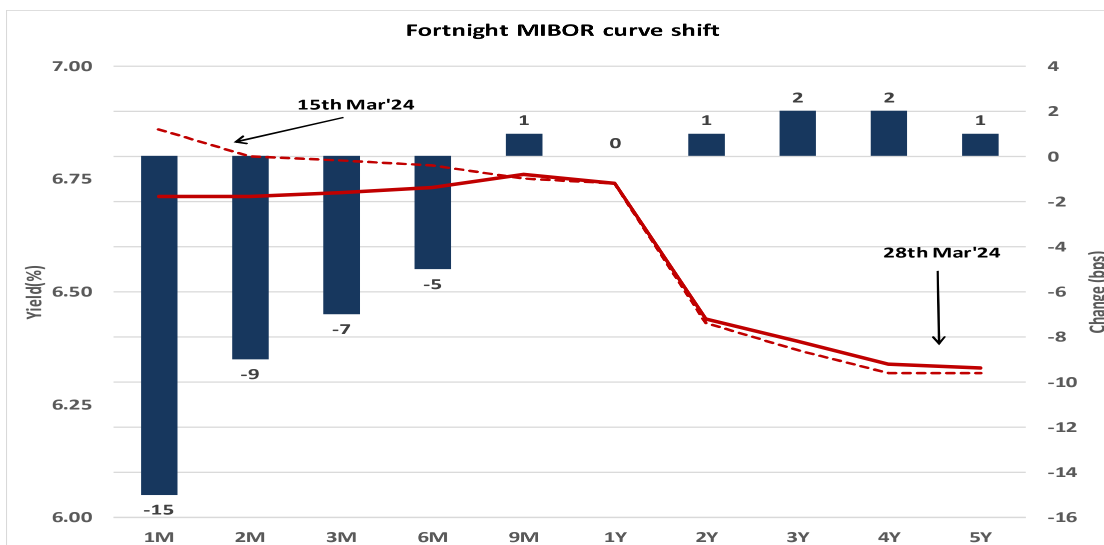
Spread Monitor



G-Sec yields continued to edge downwards despite multiple developments



In the last fortnight of FY 24, SDL spreads traded in the vicinity of 40 bps



OIS rates remained largely flat in 1 to 5 year segment

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