DEBT MARKETS

RBI Monetary Policy Update

- Monetary Policy Committee (MPC), all 6 members, voted to keep the policy repo rate unchanged at 6.25%
- Withdraws incremental CRR introduced earlier effective fortnight beginning 10th Dec
- Inflation
  - o CPI projected at 5% in Q4FY17 with risk tilted upside
  - o Pending implementation of HRA under 7th CPC award, not yet taken in the estimate
- Growth
  - o GVA growth for 2016-17 revised down from 7.6% to 7.1%
- Liquidity
  - o Committed to keep neutral liquidity
  - o Sees current surplus liquidity as transitory
- Risk Highlighted
  - o Tightening of US monetary policy
  - o Demonetization impact - prudent to wait and understand its full impact
  - o Food prices other than vegetables exhibiting sustained firmness and pick up in momentum
  - o Downward inflexibility in inflation excluding food and fuel
  - o Volatility in Crude prices
- RBI cleared that there would be no liability reduction in Balance sheet on account of extinguished notes, if any
- RBI also updated that deposits of old notes have reached INR 11.55 lakh crores

Macro Data

- IIP contracted by 1.9% YoY in Oct'16 compared to 9.9% growth in Oct'15 and growth of 0.7% YoY in Sept'16 Global Data
- Italy voted "No" in a referendum on constitutional reform, forcing Prime Minister Matteo Renzi to quit
- ECB kept rates unchanged; extends QE till December 2017 but tapers bond purchase rate to €60 bn a month from the current €80 bn beginning April 2017

Yield Movement

The bond yields rose sharply post monetary policy as the expectation of rate cut was not met. The benchmark 10-year yield ended the week at 6.44% compared to 6.24% last Friday. The 10-year corporate bond (AAA) ended at 7.27% compared to 7.05% last Friday. The money market rates too rose sharply by 25-30 bps post policy. The 1-year CD ended at 6.53% compared to 6.30% last Friday.

Liquidity

RBI has been proactively reacting to the liquidity situation and using its tools accordingly. It has increased the Cash Management bills issuances to replace the surplus that will be released post the incremental CRR withdrawal. At present about 3.65 lakh crores out of the 6 lakh crores limit under MSS has been utilized to absorb liquidity. The weighted average CBLO rate for the week was 6.06% compared to 6.21% in the previous week.

Fund Manager Comments

Post the RBI monetary policy outcome, the yield curve adjusted upwards across tenure as the rate cut didn't materialise. Though the current domestic inflation trend is downwards, global commodity prices are inching up. Crude prices have risen post the OPEC decision to cut output. The rate hike from Fed is expected in the December policy. It was prudent from the RBI to wait and look through these events, before going for a policy cut. It also gives time to analyse the real impact of demonetisation. The market participants will closely watch Fed meeting outcome on 14th December and its forward guidance. We will also have CPI and WPI data for the November month this week.

Market Indicators as on 9th December, 2016

	9-Dec-16	2-Dec-16	change
INR/USD	67.42	68.23	1.18%
Brent Crude Oil ($/bbl)	54.33	54.46	-0.24%
Gold ($/oz)	1160.01	1177.25	-1.46%
CBLO (Average)	6.06%	6.21%	-0.15%
10-year G-Sec(GOI)	6.44%	6.24%	0.20%
10-year AAA PSU(Ind)	7.27%	7.05%	0.22%
US 10-year Gilt	2.47%	2.38%	0.09%

Source: Bloomberg

Sensex and Nifty went up by 517 points (2.00%) and 175 points (2.20%) to close at 26,747 and 8,262 respectively. This is despite a surprise NO-CUT stance of RBI. But positive global cues helped. Major US indices set fresh records and European stocks posted their best week since February.

The central bank was widely expected to cut rates last week as CPI inflation is likely to undershoot the RBI's trajectory with economy showing signs of slowing down. However, the central bank surprised with no rate cut. The move led to sharp pull back in yields with the 10-yrs yield inching up to more than 6.4% levels by the end of the week.

The repo rate remains at 6.25%. The RBI revised downwards the outlook for Gross Value Added (GVA) growth from 7.6% to 7.1%, mainly due to loss of momentum in the previous quarter. It also announced that the incremental cash reserve ratio (CRR) requirement imposed on banks on November 26 will be withdrawn, effective the fortnight beginning December 10.

Even with FPI outflows in excess of USD2.2bn during the week, the INR bounced back against the USD which can be largely explained by intervention by the central bank.

The Nikkei/Markit Services PMI sank to 46.7 in November from October's 54.5, the first time since June 2015 that the index has gone below the 50 mark that separates growth from contraction. Manufacturing PMI was 52.3 down from 54.4 in October.

US 10-yrs yield inched up over the week. A large part of the increase can be attributed to continued traction in the economy with both services and manufacturing reporting stronger than anticipated economic data.

The ECB caught financial markets off-guard on Thursday by announcing it would trim asset buys from April next year, even as it reserved the right to increase purchases again if the euro zone's recovery faltered. The ECB said it would cut monthly purchases to 60 billion euros from the current 80 billion euros but extend the buys until the end of 2017. Markets had expected purchases to stay at 80 billion but only for 6 more months, suggesting a compromise between hawks and doves in the Governing Council. The euro initially jumped to a three-week high after the announcement, but quickly retreated to be flat on the day. Bond yields across the single currency area also rose, but pared gains later.

Italian voters rejected a referendum on constitutional reform early last week, prompting Prime Minister Matteo Renzi to resign. The result continues the anti-establishment trend in the United States and Europe. Moody's cut Italy's sovereign rating outlook to negative from stable after the vote. The outlook change means the credit rating agency could downgrade Italian debt if current conditions remain the same. The country's debt is currently rated two notches above junk status.

China's producer price index (PPI) rose 3.3% last month from a year earlier, at the fastest pace since late 2011. China's consumer inflation rate also quickened to 2.3% on-year, the highest since April, due to higher food prices.

Australia's economy shrank for the first time in over 5 yrs last quarter as businesses, consumers and government all cut back on spending, an unexpected blow that will challenge policymakers' optimism for growth. The local dollar sank about half a cent after the Australian Bureau of Statistics reported GDP fell 0.5% in the third quarter, from the second when it rose a revised 0.6%.

Taurus Benchmark Indices Movement

Indices	9/12/16	2/12/16	Points change	% change
S&P BSE Sensex	26747.18	26230.66	516.52	1.97
Nifty 50	8261.75	8086.80	174.95	2.16
S&P BSE 100	8512.42	8327.01	185.41	2.23
S&P BSE 200	3569.62	3491.73	77.89	2.23
Nifty Free Float Midcap 100	14931.40	14514.85	416.55	2.87

Weekly FPI & MF net flows (₹ in crs.)

	Equity	Debt
FPIs (05/12/2016 - 09/12/2016)	899.97	-16824.25
MFs (01/11/2016 - 07/12/2016)	36.60	18156.60

Source : FPI - CDSL
Source : MF - SEBI