PGIM India Mutual Fund

Macro stability in focus, RBI remains on course for further rate hikes

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The MPC Policy today was hawkish than market expectations. The MPC hiked the policy repo rate unanimously by 50 bps which was higher than market expectation of 35bps. The MPC retained the last policy stance as **“to remain focused on withdrawal of accommodation to ensure that inflation remains within the target going forward, while supporting growth“.** Prof. J R Varma expressed reservations on this stance though it’s not clear what his position was on the stance. The MPC retained both the GDP growth and inflation forecast for FY23 at 7.20% and 6.70% respectively.

Since the last MPC meeting, central banks across the world have hiked rates aggressively and emerging market currencies have been under pressure including INR. The recession narrative has gathered pace with the long end bond yields in US and Europe coming off by 70bps to 80bps from their peak touched in June. Commodity prices have also corrected from their peak levels over the last couple of months which can have a soothing impact on inflation.

RBI Governor mentioned that we may have seen peak Inflation in India though it will still stay above 6% till Q3 of 22-23, and given the uncertainties globally the MPC has taken a measured and calibrated approach.

The RBI Governor, in the post policy press conference, again highlighted the dominant nature of supply side factors in the current inflation readings.

Market Reaction: Bond markets were expecting a 35 bps rate hike and also some sort of glide path on future rate actions by RBI but were disappointed by a lack of clarity on that aspect. In the run up to the policy, bond yields had rallied across the curve with the 10yr benchmark yield touching a low of 7.11% pre policy. Post policy yields were up across the board with the 10yr benchmark security trading at 7.29% up 13bps from the previous close. Yields have rallied over the last one month on back of lower commodity prices and fall in US yields as the recession narrative took hold and we believe that bonds will continue to track global cues and movement in commodity prices going ahead.

Our View: As mentioned by the RBI Governor, we may have seen the peak in inflation, we also believe that going forward inflation will slow down if the fall in commodity prices proves to be durable, though geopolitical risks still remain.

RBI’s conduct of the monetary policy will continue to depend a lot on how things shape up on the external account with focus on INR trajectory and the current account deficit. The elevated trade deficit and analysts projection of CAD at 3.4%-3.5% for FY23 will certainly have a bearing on RBI’s future actions.

Currently the swaps market is pricing in a 1yr forward rate of 6.20% (1yr rate 1yr hence) down from 7.20% after the last policy meeting in June. We believe that RBI will moderate the pace of rate hikes going ahead and we expect the policy repo rate to be at 6.00% to 6.25% by April 2023.

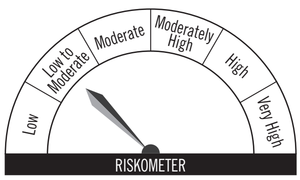
We would recommend that investors can increase their investments in short duration products while selectively looking at dynamic bond funds as per their risk appetite.

PGIM India Dynamic Bond Fund
(An open ended dynamic debt scheme investing across duration. A relatively high interest rate risk and relatively low credit risk scheme.)

This product is suitable for investors who are seeking*:

- Regular income for short term.
- To generate returns through active management of a portfolio of debt and money market instruments.
- Degree of risk – LOW TO MODERATE

* Investors should consult their financial advisers if in doubt about whether the product is suitable for them.



Investors understand that their principal will be at low to moderate risk