SBI MUTUAL FUND
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Monthly Presentation

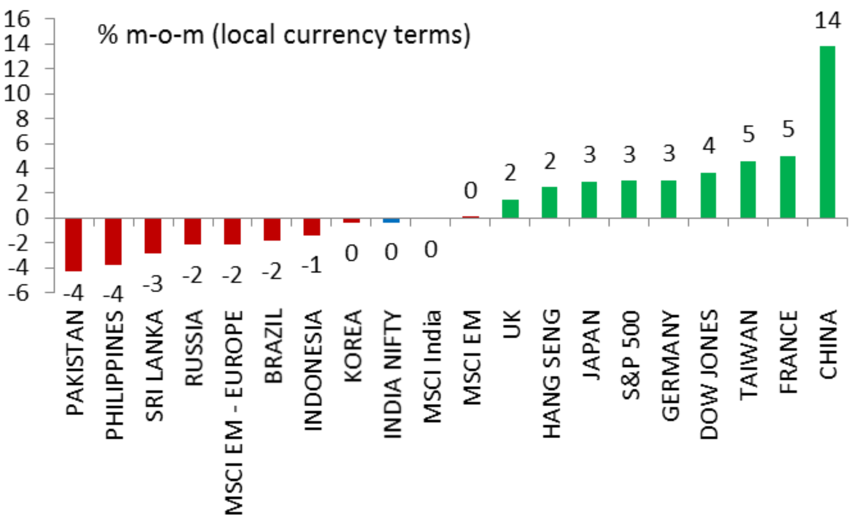
March 2019

SBI FUNDS MANAGEMENT PRIVATE LIMITED
A joint venture between SBI & AMUNDI

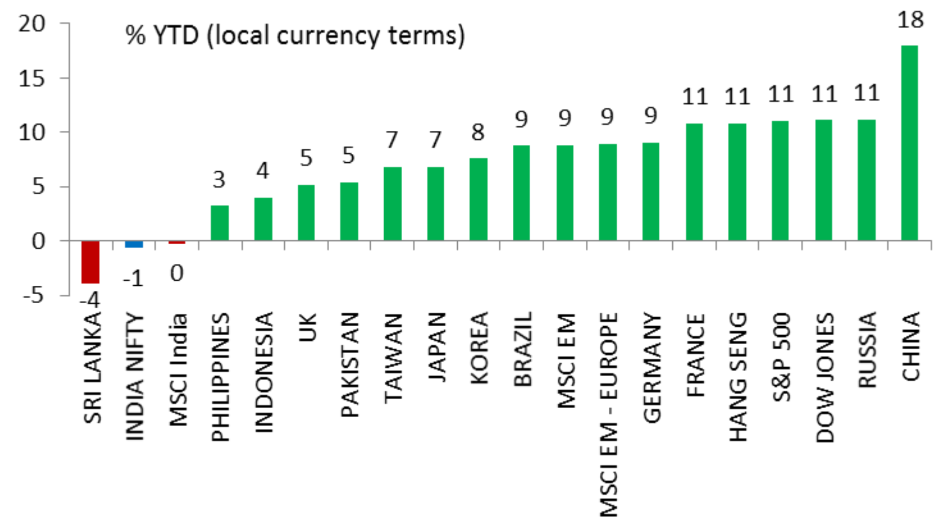
EQUITY MARKET

Global equity market snapshot: February 2019

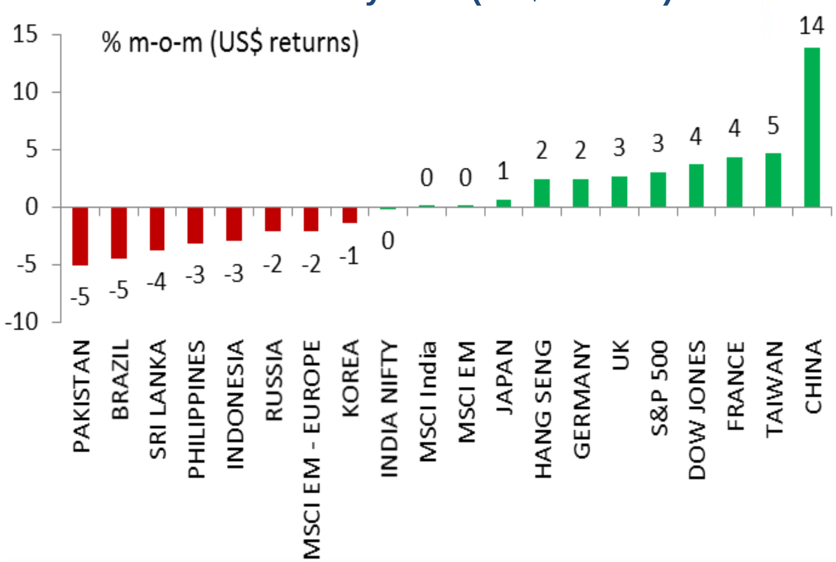
Performance in February 2019 (local currency returns)



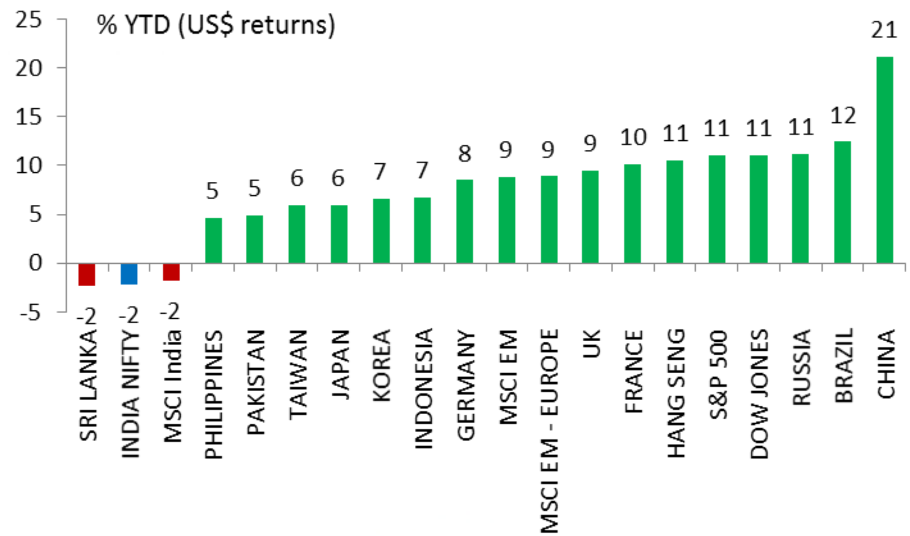
Performance YTD (local currency returns)



Performance in February 2019 (US$ returns)



Performance YTD (US$ returns)



Source: Bloomberg, SBIMF Research

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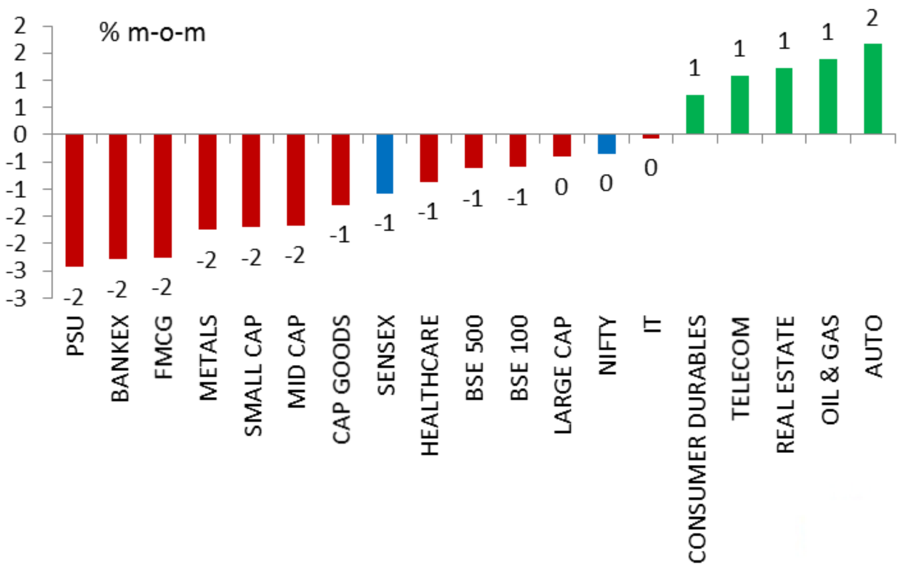
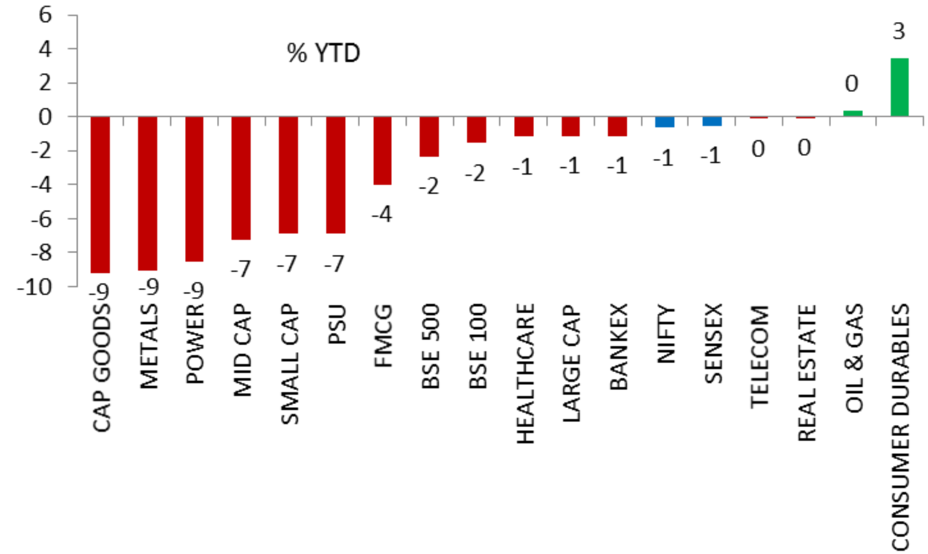
Indian stock market sector-wise returns: February 2019

Performance in February 2019 (local currency returns)



Performance YTD - local currency returns



- Indian equity market delivered negative returns across most of the sectors in February. Nifty and Sensex were down by 0.4% and 1.1% respectively during the month. On YTD basis, both Nifty and Sensex were down 0.6%.

- Large caps continued to outperform mid and small cap. Mid-cap index and small-cap index were down by 1.7% each during the month. On YTD basis, performance down the capitalization curve has been worse with mid and small cap index falling 7.3% and 6.9% respectively.

- PSUs and banks were the underperformers while auto and oil & gas were the outperformers during the month. On YTD basis, consumer durables and oil & gas were the sector outperformers while capital goods and metals were the sectoral laggards.

Source: Bloomberg, SBIMF Research

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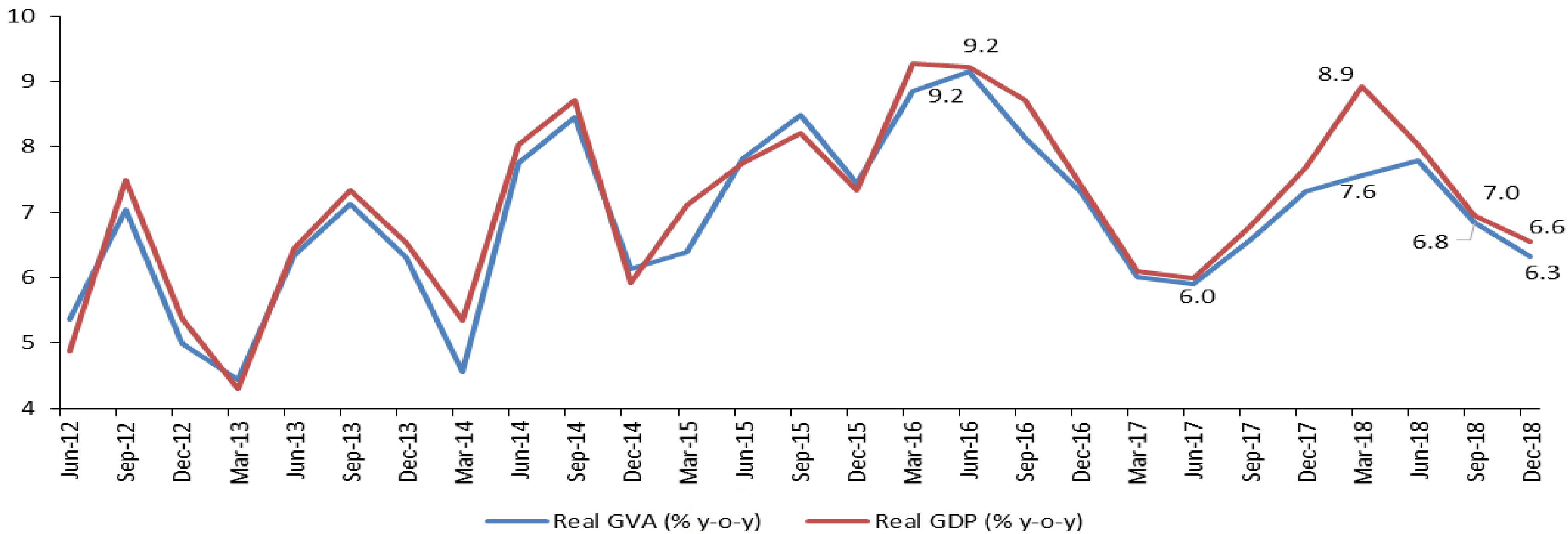
Q3 FY19 GDP growth moderated to 6.6%

Q3 FY19 GDP growth moderates to 6.6% vs. 7.0% in Q2 FY19



- Q3 FY19 GDP moderated to 6.6% vs. 7.0% in Q2 FY19 led by moderation in consumption spending. Consumption growth moderated from 9.4% in Q2 FY19 to 8.4% in Q3 FY19, though at +8%, it is still healthy. Investment growth improved marginally (10.6% vs. 10.2% in Q2) and net exports situation improved marginally.

- Investment growth has been holding up for nearly one and a half year and is supporting the incremental growth in India. On the other hand, consumption growth trends appears to have broadly stabilized 7-8%.

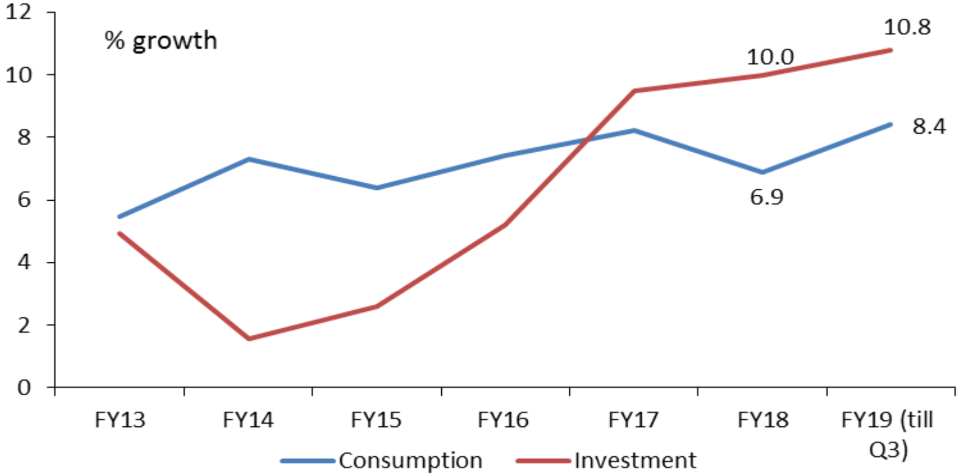
- GVA growth moderated to 6.3% (vs. 6.8% in Q2) led by softer agriculture and services growth. Industrial activities on the other hand improved. Within industrial sector, it was the robustness in construction activities and improvement in mining output which pulled the growth higher while utilities and manufacturing softened.

- Looking ahead, the government has lowered its FY19 advance estimate of growth from 7.2% to 7% for FY19. This implies a growth of 6.6% in Q4 FY19. For FY20 as well, overall growth is likely to hover around 7-7.3%.

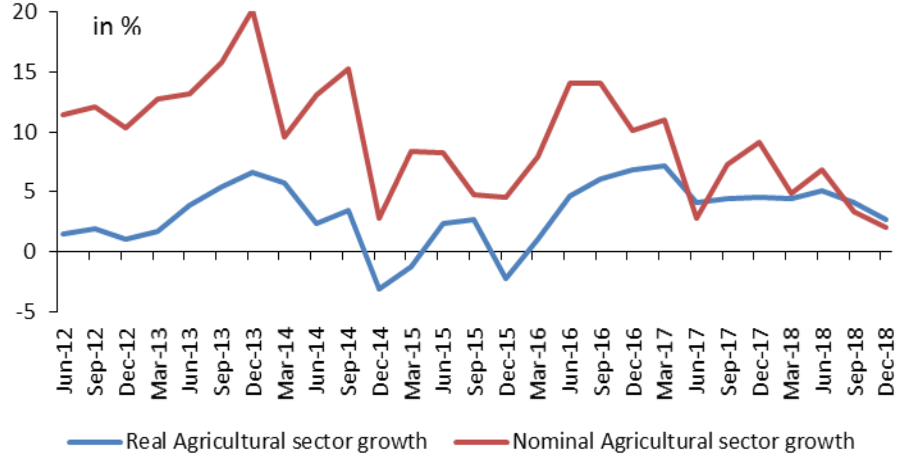
Source: CMIE economic outlook, SBIMF Research,

Q3 FY19 depicts strength in investment and construction activities

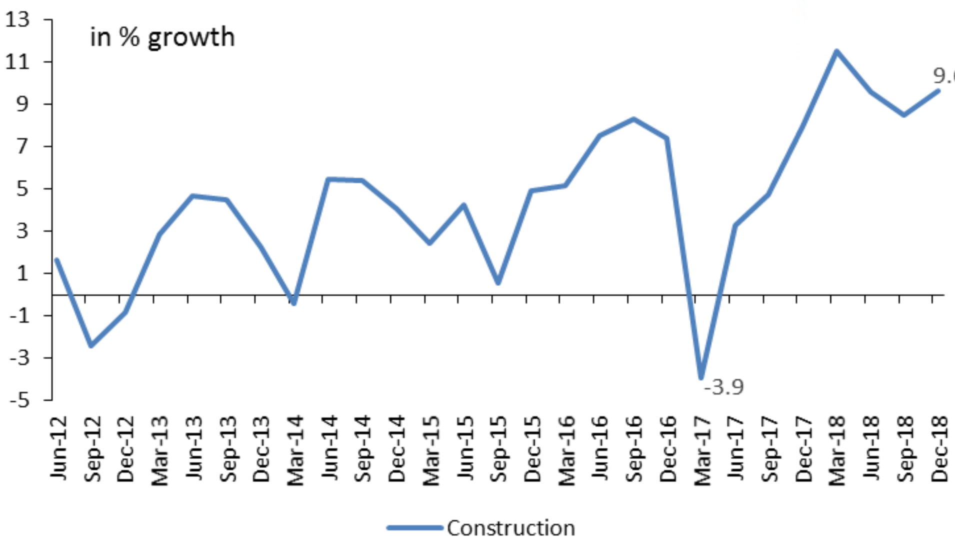
Investment growth recovery seen since FY18; Consumption growth trends broadly stable around 7-8%



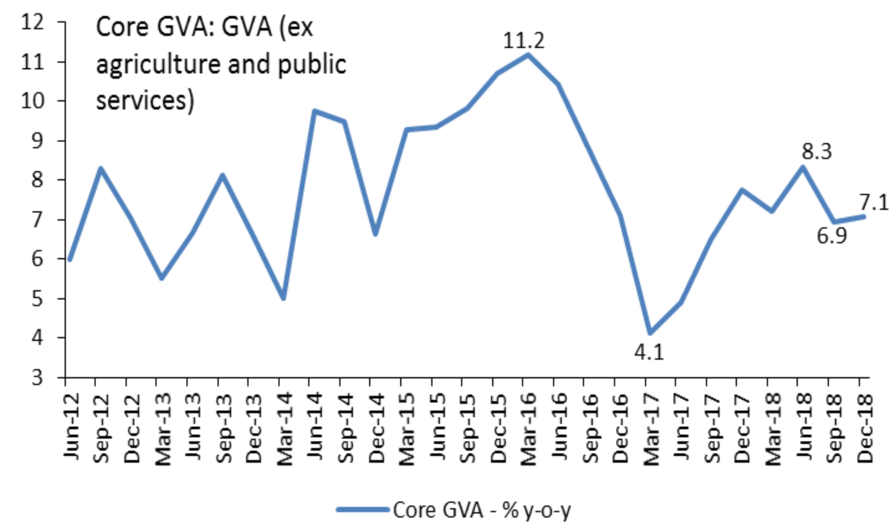
Agriculture output moderating, weak farm prices dragging the Agri-income growth even lower



Industrial activities are improving mainly due to robustness in the construction activities



Core GVA (GVA – ex agriculture & public services), a rough proxy of private sector activity, improved marginally



Source: CMIE Economic Outlook, SBIMF Research

Economic activity tracker gave mixed signals in January 2019

High frequency indicator gave mixed signals in January 2019. Construction and investment activities continue to stay robust. Weakness in wage growth, and moderation NBFC loan disbursement has weighed down on the demand for select consumer (across all segments). But, pre-election spending (reflected in high CIC growth), and banks filling in some of the void left by the NBFCs may keep the overall consumption growth supported. The launch of PM Kisan Nidhi Scheme (income support for small and medium farmers) have gone favourably thus far. Production of consumer non-durables (i.e. low ticket consumption items) are holding strong. IIP manufacturing, merchandise exports growth and freight activity has been softening but February PMI data was encouraging. In services, the overall PMI services indicates robustness.

% growth	Aug-18	Sep-18	Oct-18	Nov-18	Dec-18	Jan-19	5yr average
Indicators that are Robust							
Bank retail loans	18.2	15.1	16.8	17.2	17.0	16.9	16.5
Currency in circulation	22.7	21.2	20.0	21.1	19.6	19.1	11.6
IIP: Capital goods production	10.3	6.9	17.0	-3.1	5.9	0.0	2.9
Imports of capital goods	45.7	7.0	11.9	17.3	12.2	10.3	6.2
Services exports	20.6	19.3	18.8	8.3	12.0	0.0	6.3
Cement production	14.6	11.8	18.4	8.8	11.6	11.0	5.7
Bitumen consumption	-0.6	34.5	42.8	-15.3	2.0	15.1	8.0
Steel consumption	6.8	7.7	8.1	12.6	6.5	8.6	5.8
Indicators that have recently turned positive							
Bank industrial credit	1.9	2.3	3.7	4.0	4.4	5.1	3.2
IIP: Consumer non-durables production	6.5	6.4	8.8	-0.6	5.3	0.0	5.8
Indicators that have weakened in recent months							
Fertilizers production	-5.3	2.5	-11.5	-8.1	-2.4	10.5	1.9
IIP: Manufacturing production	5.2	4.8	8.2	-0.6	2.7	N/A	4.1
IIP: Mining production	-0.6	0.1	7.2	2.7	-1.0	N/A	2.9
IIP: Electricity production	7.6	8.2	10.9	5.1	4.4	-0.4	7.6
IIP: Consumer durables production	5.5	5.4	18.0	-2.1	2.9	0.0	3.9
Merchandise exports	19.3	-2.2	17.9	0.6	0.3	3.8	1.6
Freight handled at ports, railways and airways	6.7	4.2	8.4	3.8	0.5	0.7	3.6
Domestic Tractor sales	12.7	-10.5	23.6	24.5	4.8	2.8	6.8
Domestic sale of commercial vehicles	29.6	24.1	24.8	5.7	-7.8	2.2	10.2
Domestic sale of two-wheelers	2.9	4.1	17.2	7.1	-2.2	-5.2	8.8
Domestic sale of passenger Cars	-1.0	-5.6	0.4	-0.9	-2.0	-2.6	4.9
AUM of MFs	22.4	8.0	3.8	5.4	6.9	4.3	23.5
Foreign tourist arrivals	9.1	-0.1	1.7	1.4	2.0	5.3	8.9
Domestic air traffic	16.9	18.0	13.1	10.4	12.3	9.1	17.8
Indicators that are weak for long							
Rural wage growth	3.6	3.5	3.8	N/A	N/A	0.0	5.3

Source: CMIE economic outlook, SBIMF Research; NB: 1. Green denotes improvement in the growth and Pink indicates a moderation. 2. We use some subjectivity in categorizing the data by looking at both the trends in the recent months as well as trends relative to long term average. 3. We have shifted to steel consumption data from steel production data since Jan 2019.

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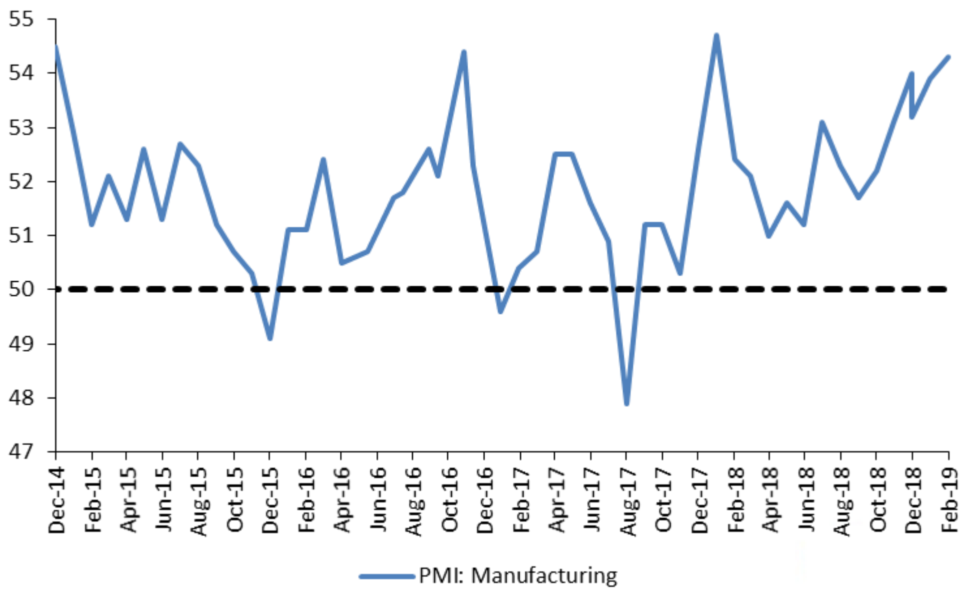
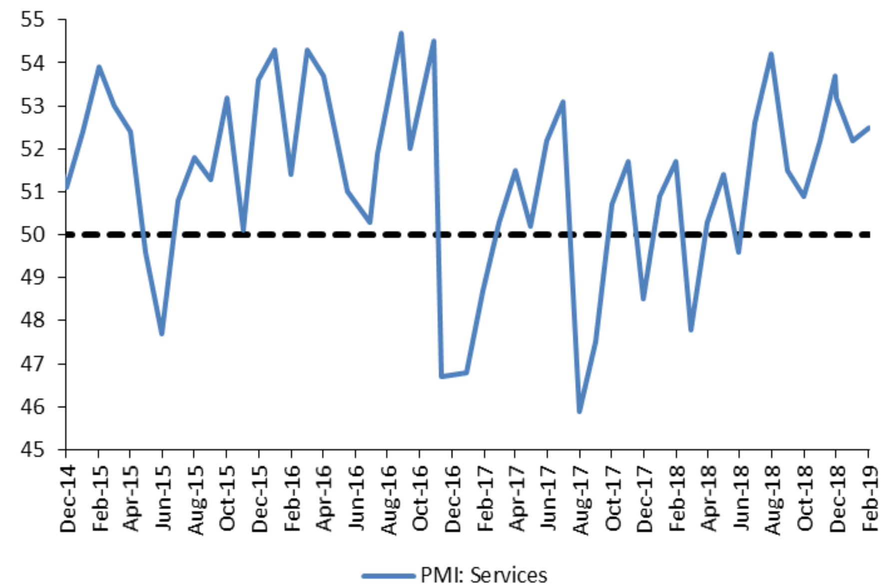
February PMI indicates improvement in economic activity

PMI manufacturing rose to a 14-month high of 54.3 in February



PMI services inched higher to 52.5 in February



- PMI manufacturing increased to a 14-months high of 54.3 (vs. 53.9 in January) in February, higher than its historical average of 51.9. This is mainly led by an increases in manufacturing output, new orders and employment. The growth in the order book came, to a large extent, from new export orders. Input and output prices grew at a faster pace compared to January, with output prices growing faster than input prices leading to manufacturing margins improving a notch.

- In February, PMI Services inched higher to 52.5 vs. 52.2 in January. New business received by services companies rose to a greater extent in February amid strengthening underlying demand. At the same time, growth of factory orders climbed to a 28-month peak. Business sentiment also improved, while rates of both input cost and output charge inflation cooled. One area of weakness was international trade, with exports down from January.

Source: CMIE Economic Outlook, Markiteconomics, SBIMF Research

US to end India's designation as GSP beneficiary; marginal impact

US to end India's designation as Generalized System of Preferences (GSP) beneficiary; marginal impact on exports

India's total exports to the US under GSP (USD mn)	
Live Animals	1
Vegetable Products	184
Food & Beverages	196
Mineral Products	15
Chemicals & Products	1,049
Plastic & Rubber Articles	537
Leather & Products	101
Wood & Paper Products	121
Textile & Products	105
Footwear & Other Articles	2
Glass & Products	272
Pearls & Precious Stones	79
Metals & Products	1,128
Machinery & Electrical Equipment	1,037
Transport Equipment	539
Optical, Medical and Musical Instruments	71
Arms and Ammunication	2
Other Manufactured Articles (toys, furniture, etc.)	195
TOTAL	**5,636**

US$ bn	India's Total Exports	India's Total Imports	India's Exports to US	India's Imports from US	India's trade balance with US	India's exports to US (as% of total exports)	India's Import from US (as % of total Imports)
2015	268	394	40	21	19	15	5.4
2016	264	362	42	23	19	15.7	6.2
2017	299	450	46	25	21	15.4	5.5
2018	326	510	52	33	18	15.8	6.5

- The US announced India's termination from the GSP programme due to lack of assurance in providing equitable and reasonable access to its markets in numerous sectors. This will take effect at least after 60 days from the date of notification.

- Economic impact of this termination appears to be limited and may affect only around 2% of India's total exports and led to a meager duty reduction of US$ 190 million. However, select sectors such as chemicals, metals, machinery, transport and electrical equipment bear a relatively larger brunt and would see some reduction in price competitiveness.

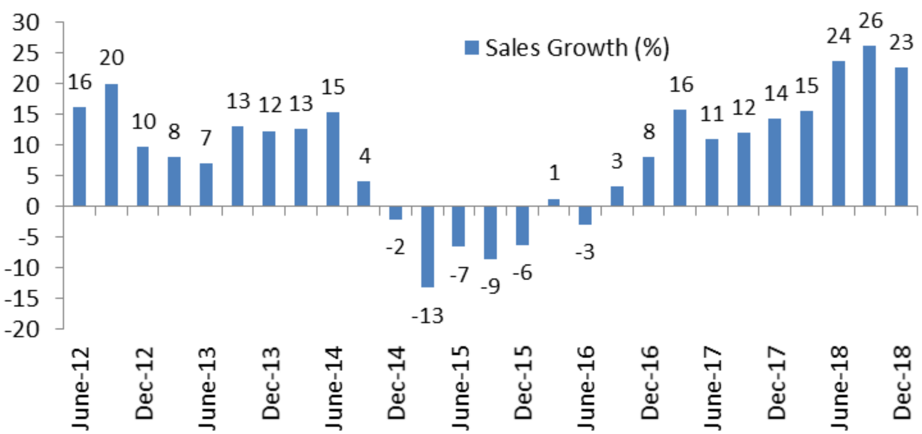
- Indian government has notified that it is not keen on seeking an overturn of the USTR's order. India has been cautious to not engage into any trade war with the US. The approach is on a very case to case basis. While the government is ready to make some relaxation in concerns around medical devices pricing and dairy certification, it finds the duty structure on various imports appropriate.

- The US had announced heavy tariffs on imported steel and aluminum items on March 9 2018. In retaliation, India had announced increased tariffs on select US imports in June 2018. It was supposed to be effective since August 2018, but were eventually deferred every month (i.e. six times) to accommodate on-going trade talks. This deferment is going to expire by March 2019 end and from media news flow we understand that most likely not defer this additional tariff any further.

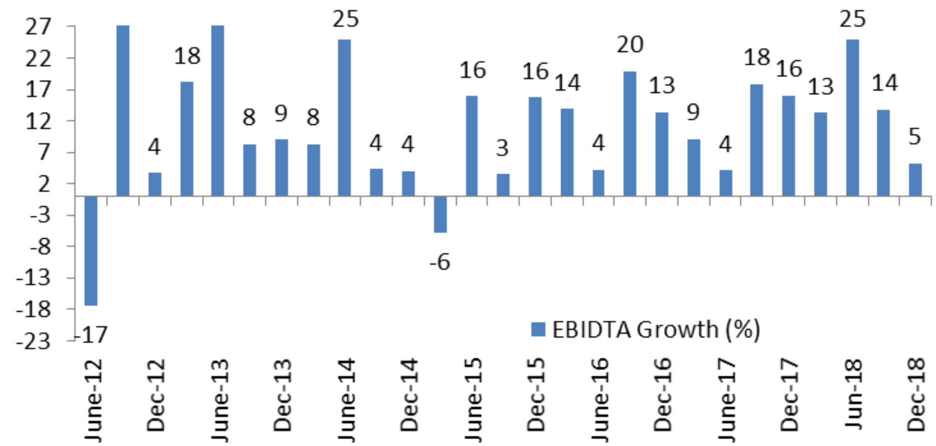
Source: USITC, CMIE Economic Outlook, SBIMF Research;

Q3 FY19 earnings depict continued robustness in revenue growth

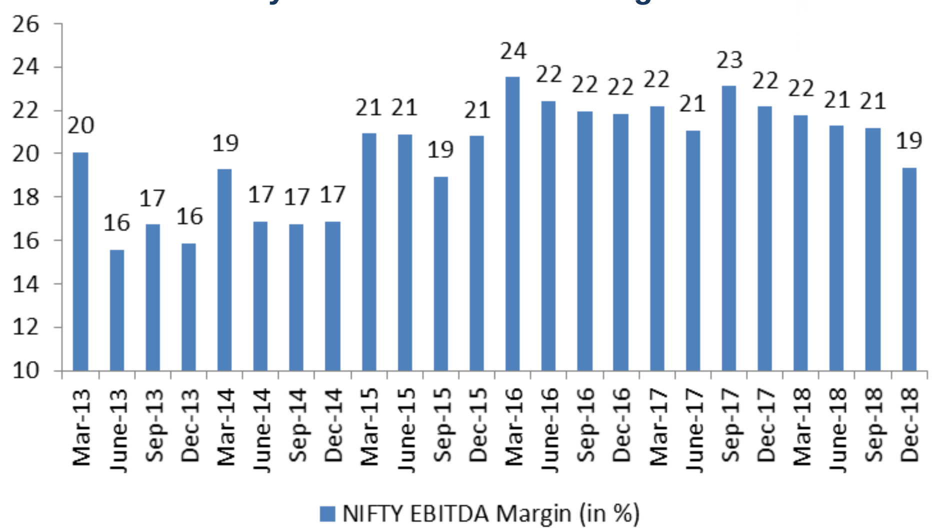
Nifty delivered +20% sales growth for third consecutive quarter



The robust top-line failed to translate into a parallel EBITDA growth; EBITDA growth was the lowest in six quarters



Nifty EBIDTA margin narrowed by 180bps; Autos, Metals and Oil &Gas were key sectors to see the margin decline

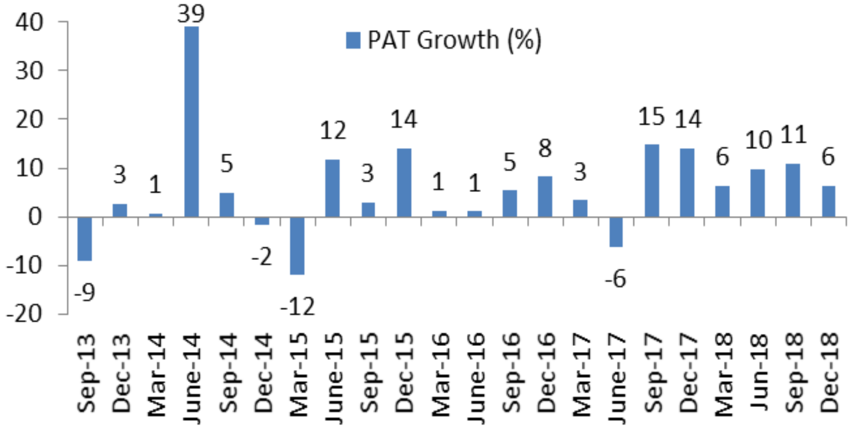


- Q3 FY19 corporate earnings outcome for NIFTY was broadly in line with market expectations.
- Top-line growth was at a multi-year highs. Barring 2 companies, all the NIFTY companies saw positive growth in their revenue.
- However, this failed to translate into concomitant EBITDA growth. Nifty EBIDTA margin narrowed by 180bps during the quarter. Autos, Metals and Oil &Gas were key sectors to see the margin decline. Most other sectors saw their operating margins being broadly stable.

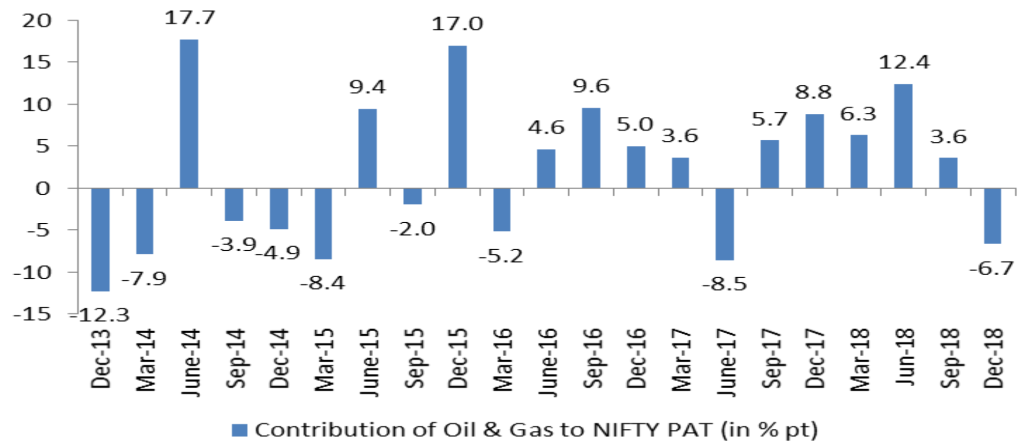
Source: MOSL ,SBIMF Research,

Corporate banks drove NIFTYPAT growth in Q3 FY19

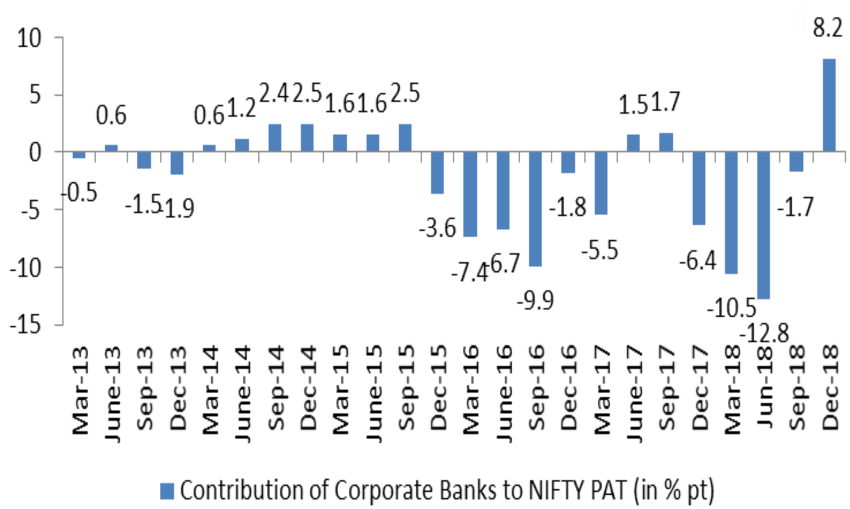
Nifty PAT growth at 6.4% vs. 11% in Q2 FY19



Oil & Gas subtracted from the overall profit after five consecutive quarters of positive contribution



PAT growth for Q3 FY19 can largely be attributed to the Corporate Banks

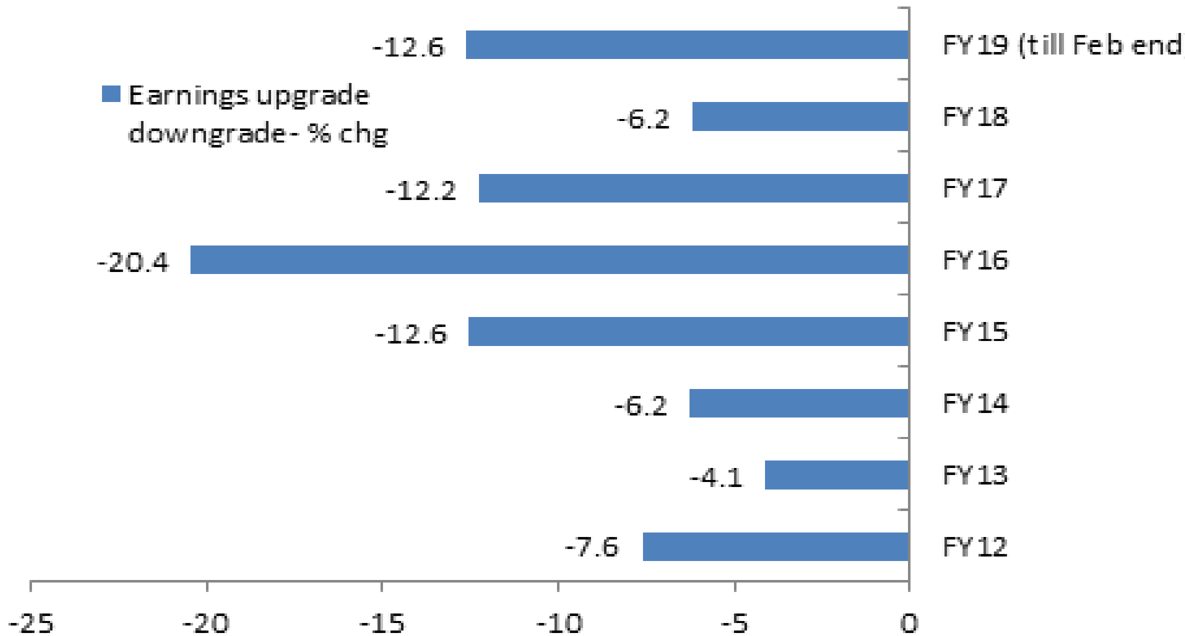


- Nifty PAT growth at 6.4% was lowest in six quarters. Oil & Gas was the key sector to drag down the profitability followed by autos and telecoms. On the other hand, the performance of corporate banks stood out.
- Corporate Banks showed a sequential improvement in the asset quality trends. This provides good visibility on the earnings outlook, as corporate banks were one of the key drivers for the earnings miss over the past few years.
- NBFC delivered in-line performance, but saw some moderation in the growth estimates owing to prevailing stress in the liquidity and cost of funds environment. Disbursement growth moderated sequentially.
- Telecom (Bharti airtel and Infratel) posted its ninth consecutive quarter of loss, while automobiles and oil & gas posted a decline of 32% y-o-y and 21.5% y-o-y, respectively, in profits.

Source: MOSL ,SBIMF Research,

Earnings downgrade continuing for eight straight year

The direction of earnings revision is still trending down



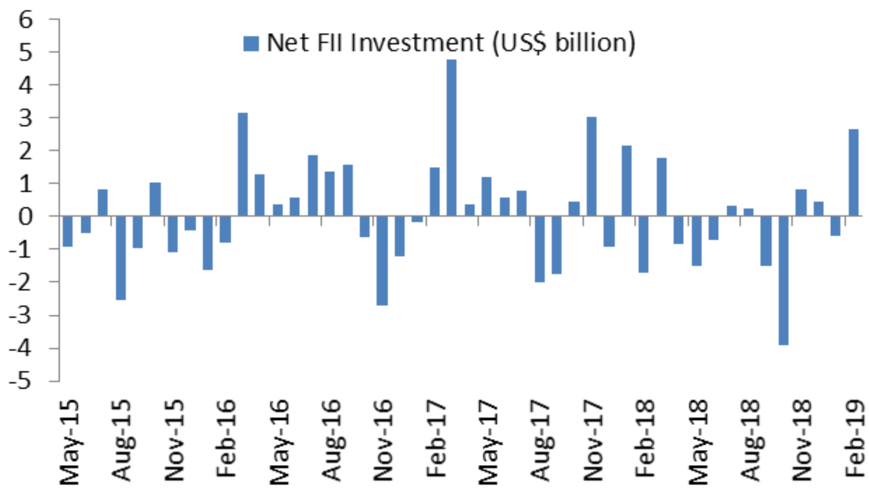
- Overall, the direction of earnings revision is still trending down driven by select companies. Up until Feb end, consensus has downgraded the NIFTY PAT by 12% FYTD.

- Our own expectation pencils FY19 NIFTY growth at ~15%, an 8-9% downgrade from the start of the year. However, we continue to expect FY20 growth to the north of 20% driven by favorable base and material pick-up in financial sector profitability.

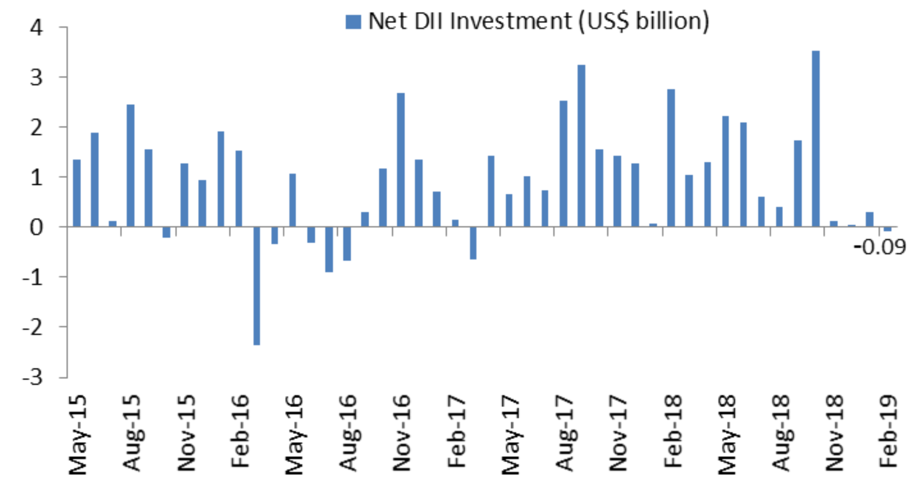
Source: Bloomberg, SBIFM Research;

Liquidity: FIIs invested while DIIs sold in February

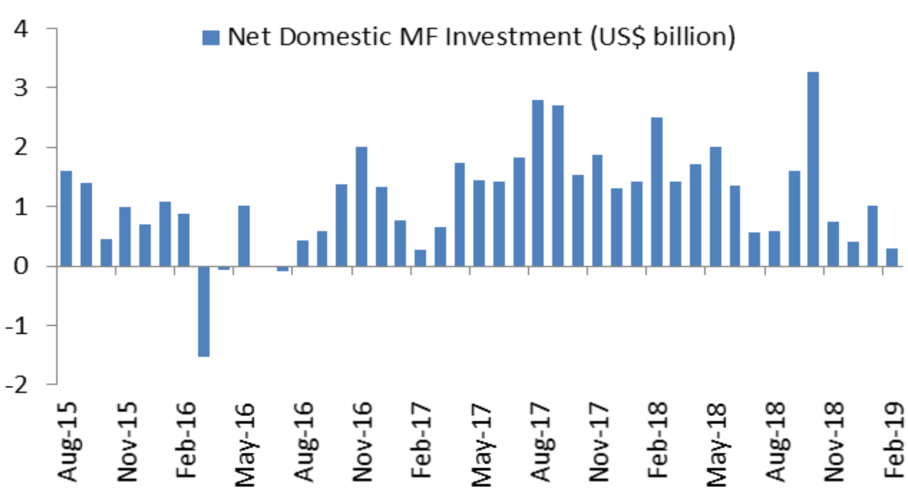
FIIs invested US$ 2.64 billion in February 2019



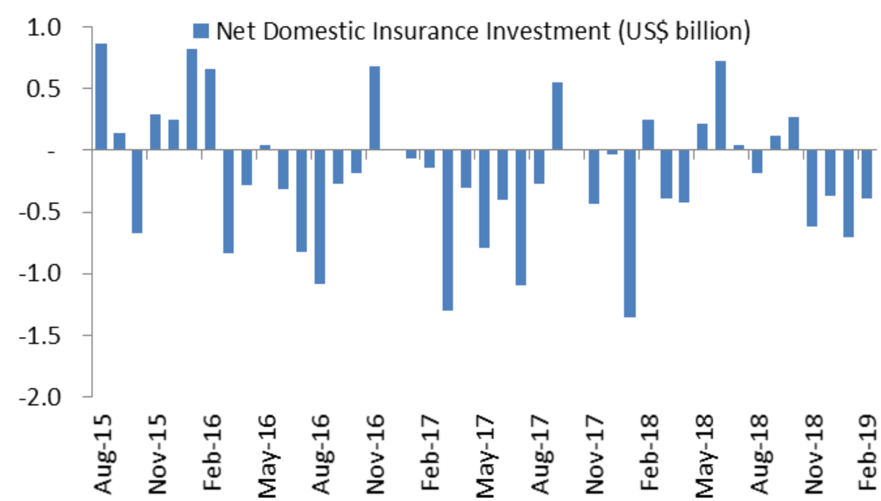
Domestic institutional investors were a net sellers, for the first time in last 23 months



Mutual Funds investments in Indian equities have been moderating…



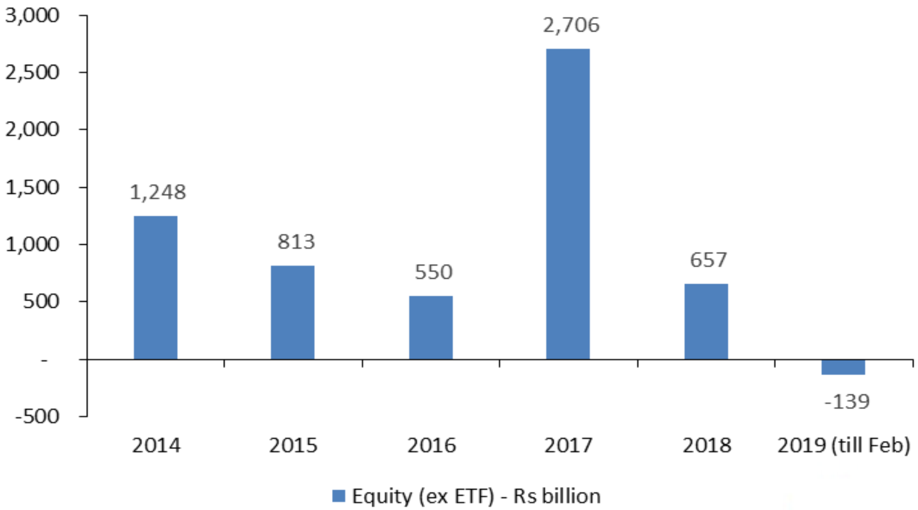
…while Insurance companies have been net sellers for the past four months



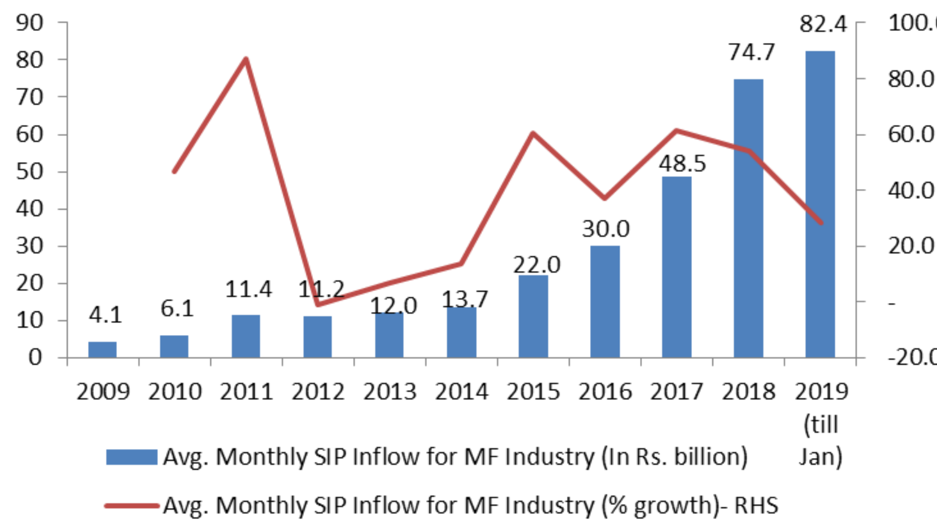
Source: Bloomberg, SBIMF Research

Inflows in domestic equity mutual funds has slowed down

Domestic mutual fund witnessing gradual moderation in net equity inflows…



…SIP inflows continue to rise, though at moderate pace

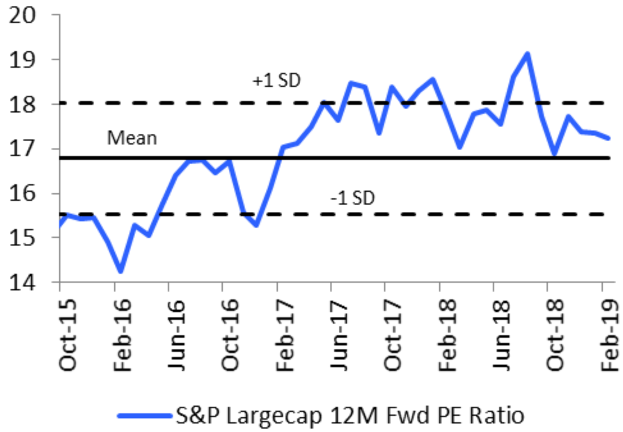


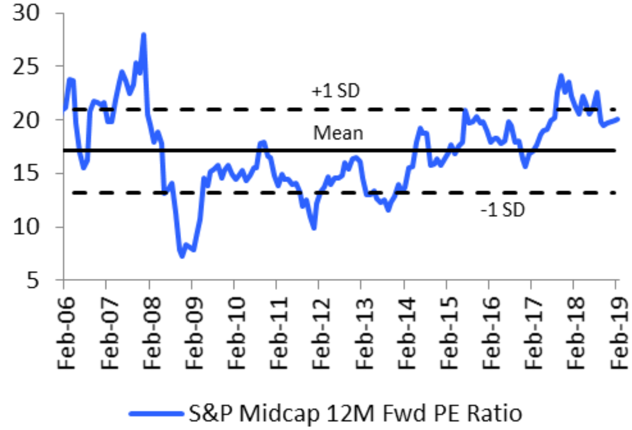
- Inflows into the domestic equity mutual funds, which have been supporting the stock market over the last couple of years, have slowed down. On a net basis, equity (ex-ETF) mutual fund witnessed a marginal outflow during Jan-Feb 2019.
- Equity flows in domestic mutual funds have turned negative to Rs 139 billion in 2019 (till Feb) vs. an inflow of Rs 657 in 2018.
- SIP inflows continue to provide support.

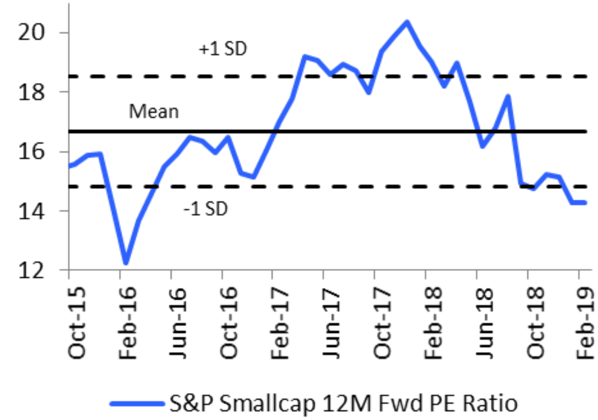
Source: CMIE Economic Outlook, MF Dex, SBIMF Research

Sharp moderation in the small cap valuation; looks attractive

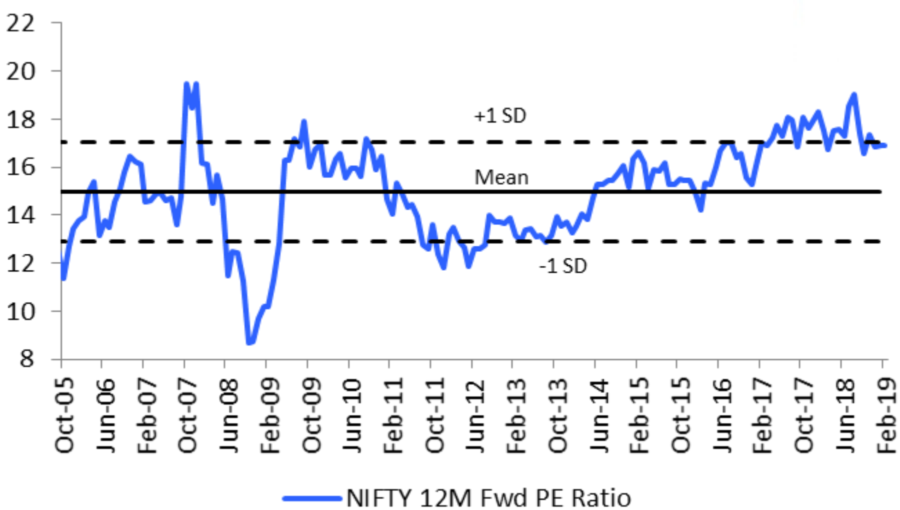
Valuations moderated for large-cap, improved marginally for mid-cap and remained stable for small-cap in February 2019



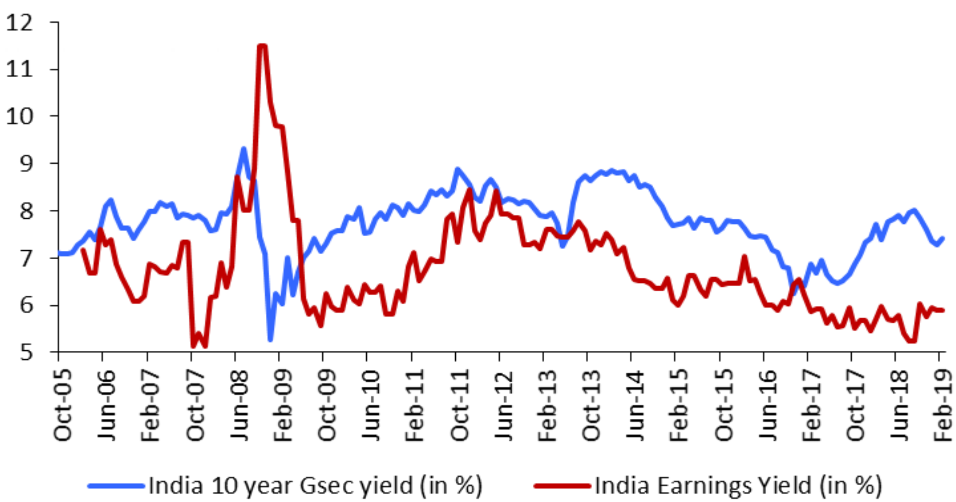




Nifty is trading at ~17 times forward earnings



NIFTY is trading at a premium of 25% vis-à-vis 10 year G-sec (vs. the long term average premium of 16%)



Source: Bloomberg, SBIMF Research,

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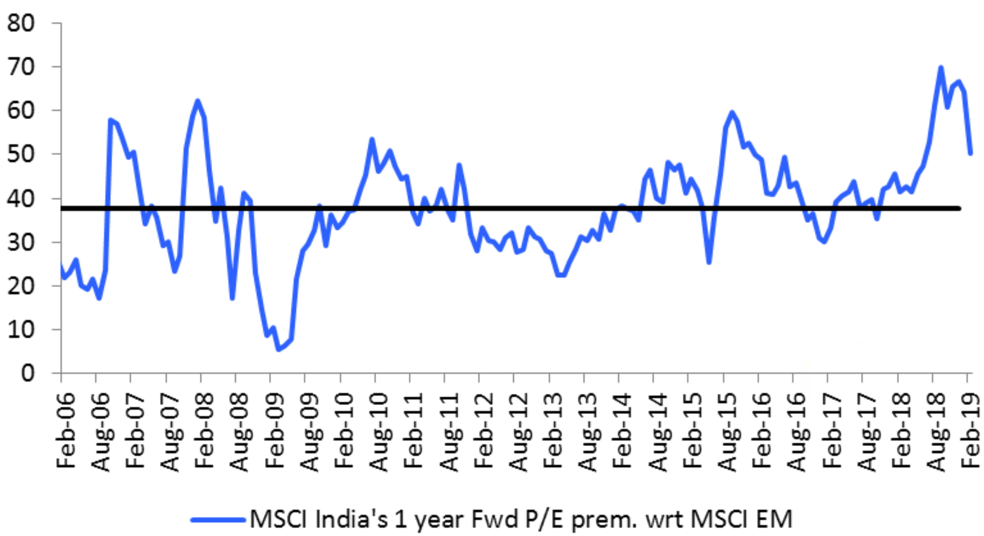
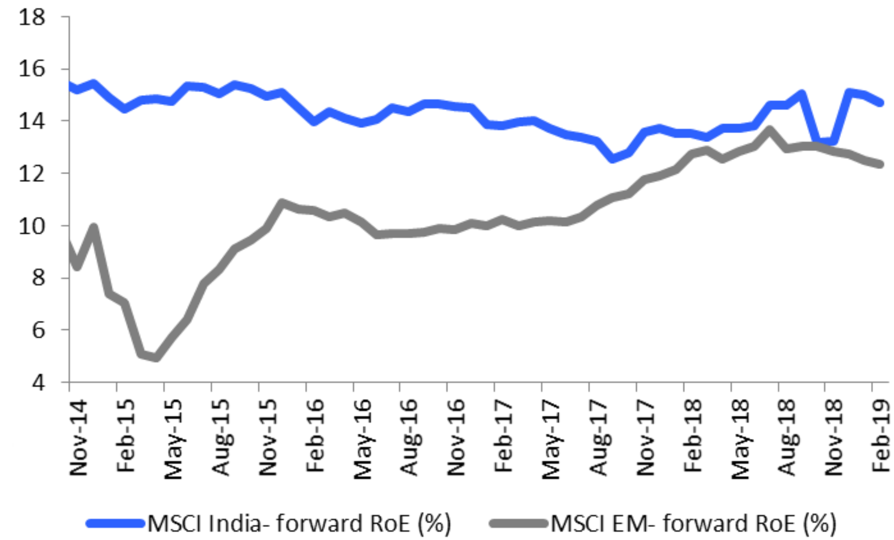
MSCI India saw sharp corrections vis-à-vis MSCI EM

MSCI India saw sharp corrections vis-à-vis MSCI EM during January and February



The RoE differentials have also improved in favour of India



Source: Bloomberg, SBIMF Research,

Equity Market outlook

- Indian equity underperformed during January and February (MSCI India is down 0.2% YTD) relative to its peers. NIFTY is down -0.6% YTD.

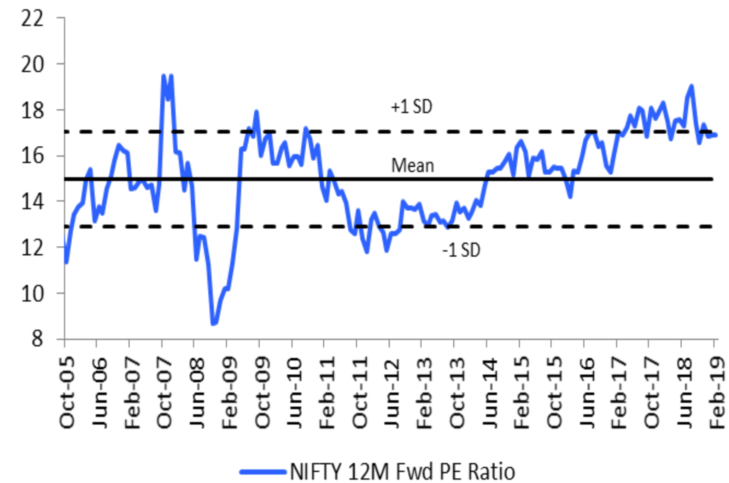
- The uncertainty about the election outcome and the recent domestic geo-political developments had adversely affected the investor sentiments. Inflows into the domestic equity mutual funds, which have been supporting the stock market over the last couple of years, have slowed down. To add, unfavorable company specific news flow, issues of corporate governance and the continued pressure on the NBFC sector also had an impact.

- Q3 FY19 corporate earnings outcome for NIFTY was broadly in line with market expectations. Revenue growth was at multi-year highs. However, this failed to translate into concomitant EBITDA growth.

- Nifty PAT growth was at 6.4% with oil & gas being the key sector to drag down the profitability followed by autos and telecom. On the other hand, the performance of corporate banks stood out. Overall, despite the in-line performance of most of the companies, the direction of earnings revision is still trending down. Our own expectation pencils FY19 NIFTY profit growth at ~13%. However, we continue to expect FY20 growth to the north of 20%, driven by favorable base and material pick-up in financial sector profitability.

- We forecast equity to see upside by end-2019. Investors (thus liquidity) are on the sidelines as they wait for a better clarity on the likely outcome of the pending election. Interestingly, there is a huge convergence on economic policies across political parties and structural factors should ensure a sustained growth in economy and markets over a medium term. Of course, there could be intermittent sentimental impact leading to high volatility in the short run. Valuations have been de-rated, particularly in the small-cap space. Good news and good price can rarely be simultaneity. In such a scenario, we advise to stay invested in equities.

Nifty is trading at ~17 times forward earnings



Source: Bloomberg, SBIMF Research

Fixed Income Market

Developed Market Bond Yields: February 2019

10 Year Gsec Yield (% mth end)	2016 end	2017 end	2018 end	Jan-19	Feb-19	m-o-m change (in bps)	Change in 2019 (in bps)
Developed market							
US	2.44	2.41	2.68	2.63	2.72	9	3
Germany	0.21	0.43	0.24	0.15	0.18	3	-6
Italy	1.82	2.02	2.74	2.59	2.75	16	1
Japan	0.05	0.05	0.00	0.01	-0.02	-3	-3
Spain	1.38	1.57	1.42	1.20	1.17	-2	-24
Switzerland	-0.19	-0.15	-0.25	-0.24	-0.24	1	1
UK	1.24	1.19	1.28	1.22	1.30	8	2

- US bond yields stayed range bound in February. While it ended the month marginally higher at 2.72%, it has moved back to the 2.63-2.65% levels in the first half of March. There is a recent tilt of dovishness in the US Fed's policy. Further, the US Fed Chairman has also indicated towards an end to balance-sheet reduction by 2019.

- Bond yields in Italy were rising in February on account of risks of rating downgrade by Fitch and reached to as high as 2.96% on 8th February 2019. However, it corrected marginally from there as the rating was left unchanged at BBB. That said, there are still risks prevailing on weak fiscal and high government debt which keeps the Italian bond yield higher than its European peers .

- UK bond yields inched up by 8 bps as Fitch placed the UK's AA credit rating on negative watch over the growing uncertainty over no transition deal Brexit.

- Bond yields in other key developed markets stayed broadly flat during the month of February.

Source: Bloomberg, SBIMF Research

Emerging market bond yields: February 2019

10 Year Gsec Yield (% mth end)	2016 end	2017 end	2018 end	Jan-19	Feb-19	m-o-m change (in bps)	Change in 2019 (in bps)
Emerging Market							
Brazil	11.40	10.26	9.24	8.86	9.00	14	-23
China	3.06	3.90	3.31	3.11	3.18	7	-13
India	6.52	7.33	7.37	7.28	7.41	13	4
Indonesia	7.91	6.29	7.98	7.99	7.79	-20	-19
South Korea	2.09	2.47	1.96	2.00	1.99	-1	3
Malaysia	4.23	3.91	4.08	4.07	3.90	-17	-19
Phillippines	4.64	4.93	7.01	6.37	6.34	-3	-67
Russia	8.36	7.49	8.70	8.19	8.43	24	-27
Taiwan	1.22	0.98	0.83	0.83	0.83	0	0
Thailand	2.65	2.32	2.48	2.38	2.47	9	-1

- The movement in the emerging market bond yields have been diverse.
- China rallied by 7 bps during the month on account of monetary easing and improvement in investor sentiments.
- Indian bond yields worsened by 13 bps as deteriorating demand-supply dynamics are keeping the yields high despite easing monetary policy.
- Bond yields in Brazil increased by 14 bps in February on account of uncertainty over passage of select domestic reforms leading to depreciation pressure in the Brazilian Real. On the other hand, bond yields in Indonesia softened by 20 bps on account of improving fiscal status and relatively less hawkish comments by the central bank in its last policy meet.

Source: Bloomberg, SBIMF Research

India Rates Snapshot: February 2019

	Nov-18	Dec-18	Jan-19	Feb-19	m-o-m change (in bps)	Change in 2019 (bps)
3M T-Bill	6.77	6.65	6.56	6.40	-17	-25
1 Yr T-Bill	7.22	6.94	6.78	6.55	-23	-39
10 year G-Sec	7.61	7.37	7.28	7.41	13	4
Overnight MIBOR Rate	6.55	6.73	6.50	6.35	-15	-38
Weighted Average Call money rate	6.36	6.49	6.50	6.39	-19	-34
3M CD***	7.28	7.05	7.10	7.08	-2	3
12M CD***	8.33	8.08	7.93	7.73	-20	-35
3 Yr Corp Bond*	8.64	8.50	8.22	8.18	-4	-32
5 Yr Corp Bond*	8.68	8.43	8.32	8.45	13	2
10 Yr Corp Bond*	8.70	8.51	8.56	8.73	17	21
1 Yr IRS	6.92	6.56	6.49	6.24	-25	-32
5 Yr IRS	7.11	6.62	6.60	6.31	-29	-31
INR/USD	69.6	69.8	71.1	70.7	0#	-1.4#
Crude Oil Indian Basket**	65.4	57.8	59.3	64.5	9#	12#

- Despite the 25 bps rate cute and an indication of more in offing, 10-year G-sec has moved up by 13 bps during the month of February. Growth-inflation dynamics are supportive of rate cuts making the valuation attractive and global environment is bond positive. Demand supply is the key risk to the bond outlook and is keeping the yields high despite easing monetary policy. Part of it emanates from weak fiscal, which translates into higher supply risk. The other part hinges on banks' appetite for government bonds in the current tight credit to deposit environment.

- Money market rates, on the other hand, inched down during the month as it aligned to the surprise 25bps rate cut in February.

- Crude oil prices increased by 9% during the month. YTD, crude price has risen by 12%. Rupee appreciated by nearly 0.5% in February 2019, partly undoing the sharp depreciation in January. The appreciation has continued has into the March and as of 11th March, the levels have been restored to ~69.5-70/ US$.

Source: Bloomberg, PPAC, RBI, SBIMF Research; NB: **Crude oil price is average $/barrel for the month, rest of the data are % month end; *Corporate bond rate is for AAA rated bonds ,*** Refers to PSU Banks' CD rate; # INR and Oil price changes are % change

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Policy Rate Outlook: April rate cut likely

- The RBI cut the policy rate by 25bps to 6.25% and brought the stance back to neutral from ‘calibrated tightening’ adopted two policies ago in its latest February meeting. While all the six MPC members voted unanimously for the change in stance, four out of six members voted for the cut. Dr. Viral Acharya and Dr. Chetan Ghate voted to keep the rate unchanged.

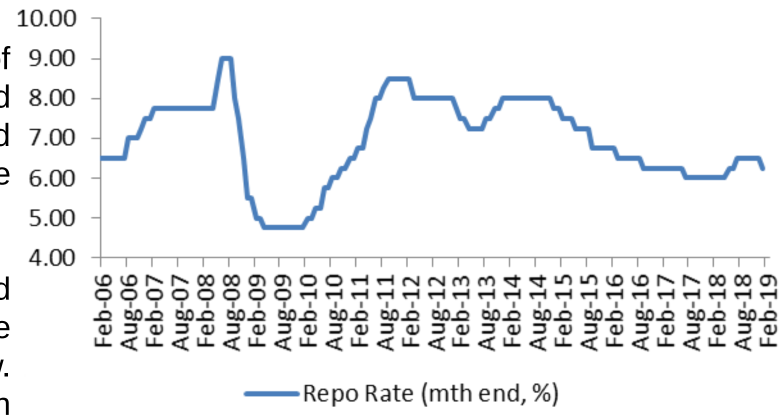
- The rate cut came on the back of increased comfort on inflation stability and rising growth concerns.

- The central bank significantly lowered its inflation projections on the back of moderation in household inflation expectations, benign food inflation and recent moderation in fuel groups. With the central fiscal slippage being limited to 10bps for FY19, the RBI did not appear to be materially concerned on the inflationary impact of the budget announcement.

- The RBI stressed on the need to strengthen private investment and consumption activity. The other key change in RBI assessment is that the output gap has opened up modestly, which is at variance from the last review. Even as the central bank sounded concerned on growth, FY20 growth projections have been kept at 7.4%, and CSO’s projection of 7.2% for FY19 has been incorporated.

- Tone of the policy was quite dovish. Since the last policy meet, we have had two more inflation prints, indicating continued softness. Q3 FY19 GDP was released and indicated the growth moderation to 6.6% (vs. 7.0% in Q2). The government lowered its FY19 advance estimate of growth from 7.2% to 7% for the full fiscal year. This implies a growth of 6.6% in the final quarter of FY19. For now, given that the official GDP may print 2-3 quarters of sub 7% growth, high frequency indicators point towards moderation and inflation much below 4% central target, another 25bps cut in April looks highly likely.

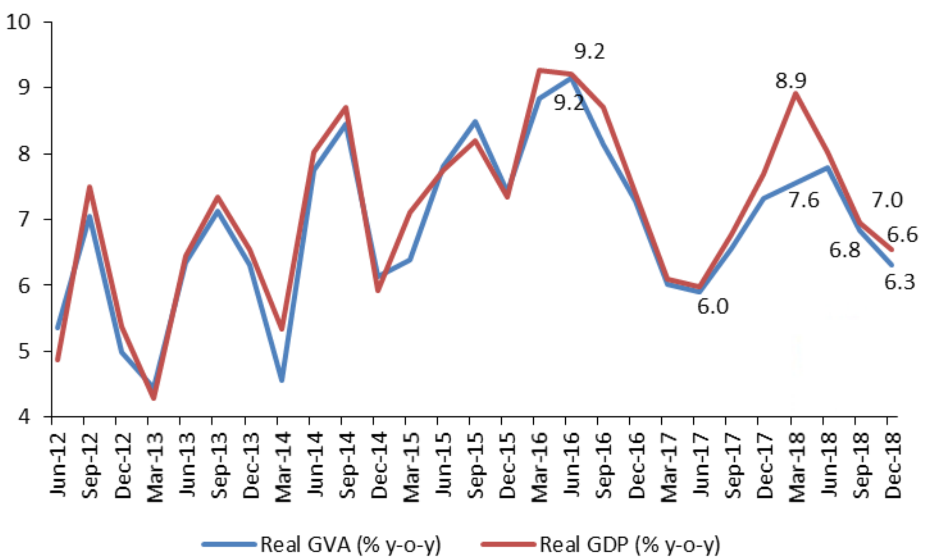
RBI cut the policy rate by 25bps to 6.25%



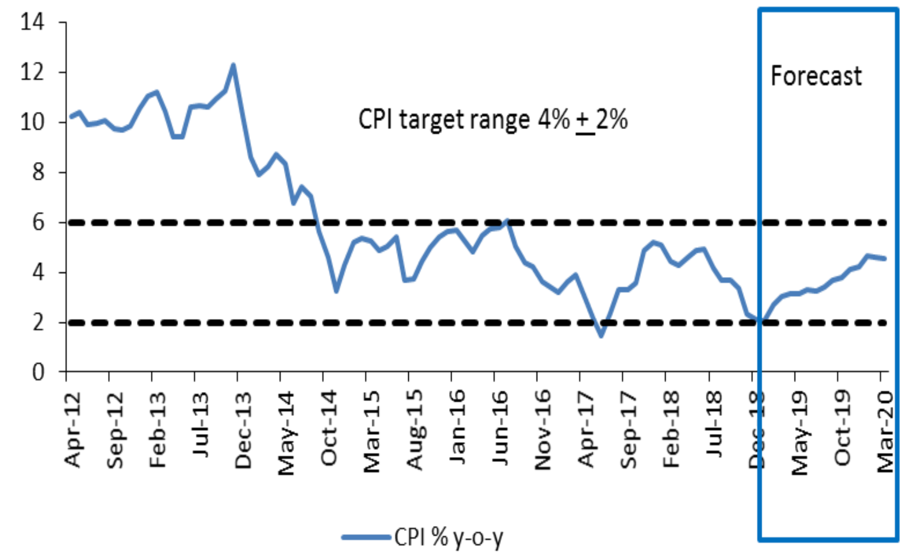
Source: RBI, SBIFM Research

Indian growth-inflation dynamics are favorable for a rate cut

GDP growth has moderated to 6.6% and is likely to remain sub-7% for the next 1-2 quarters



CPI inflation likely to stay within RBI's comfort zone through out FY20



Source: CMIE economic outlook, SBIMF Research,

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Global developments incrementally supportive of bond market

While the first two months is early to assess, the direction of the global policy rate appears to be marginally tilting towards hold or easing

Policy rate (in %), end period	2015	2016	2017	2018	2019 (till Feb)
US	0.50	0.75	1.50	2.50	2.50
Canada	0.50	0.50	1.00	1.75	1.75
China	4.35	4.35	4.35	4.35	4.35
Japan	0.10	0.10	0.10	0.10	0.10
India	6.75	6.25	6.00	6.50	6.25
Australia	2.00	1.50	1.50	1.50	1.50
South Korea	1.50	1.25	1.50	1.75	1.75
Indonesia		4.75	4.25	6.00	6.00
Taiwan	1.625	1.375	1.375	1.375	1.375
Thailand	1.50	1.50	1.50	1.75	1.75
Malaysia	3.25	3.00	3.00	3.25	3.25
Singapore	0.08	0.08	0.08	0.08	0.08
Hong Kong	0.75	1.00	1.75	2.75	2.75
Phillippines	4.00	3.00	3.00	3.00	3.00
New Zealand	2.50	1.75	1.75	1.75	1.75
Eurozone	0.05	0.00	0.00	0.00	0.00
UK	0.50	0.25	0.50	0.75	0.75
Switzerland	-0.75	-0.75	-0.75	-0.75	-0.75
Sweden	-0.35	-0.50	-0.50	-0.25	-0.50
Norway	0.75	0.50	0.50	0.50	0.50
Russia	11.00	10.00	7.75	7.75	7.75
Turkey	7.50	8.00	8.00	24.00	24.00
Saudi Arabia	2.00	2.00	2.00	3.00	3.00
Poland	1.50	1.50	1.50	1.50	1.50
South Africa	6.25	7.00	6.75	6.75	6.75
Brazil	14.25	13.75	7.00	6.50	6.50
Mexico	3.25	5.75	7.25	8.25	8.25
Argentina	21.00	26.00	26.75	50.00	44.00
Colombia	5.75	7.50	4.75	4.25	4.25
Chile	3.50	3.50	2.50	2.75	3.00

Source: Bloomberg, SBIMF Research; NB: * Indonesia had announced to use new policy benchmark i.e. 7-day reverse report rate as its benchmark policy rate in April 2016; Red highlighted cells indicates interest rate hike and green denotes a rate cut.

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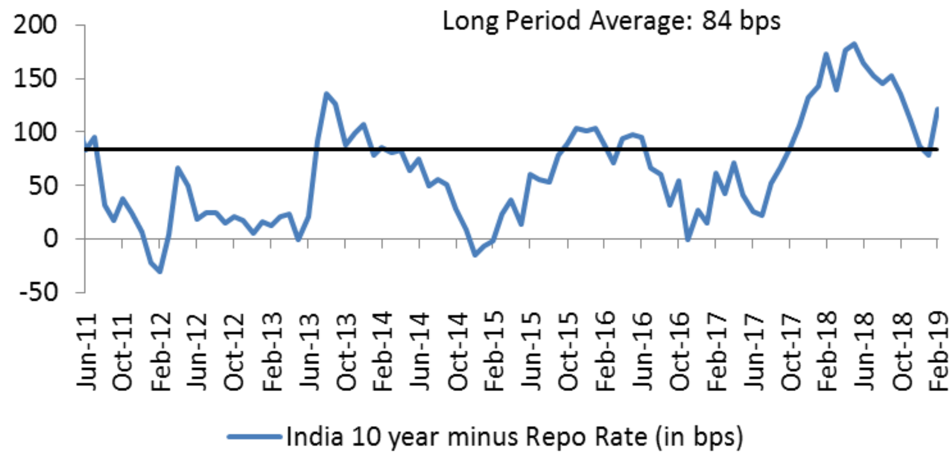
Valuations are attractive

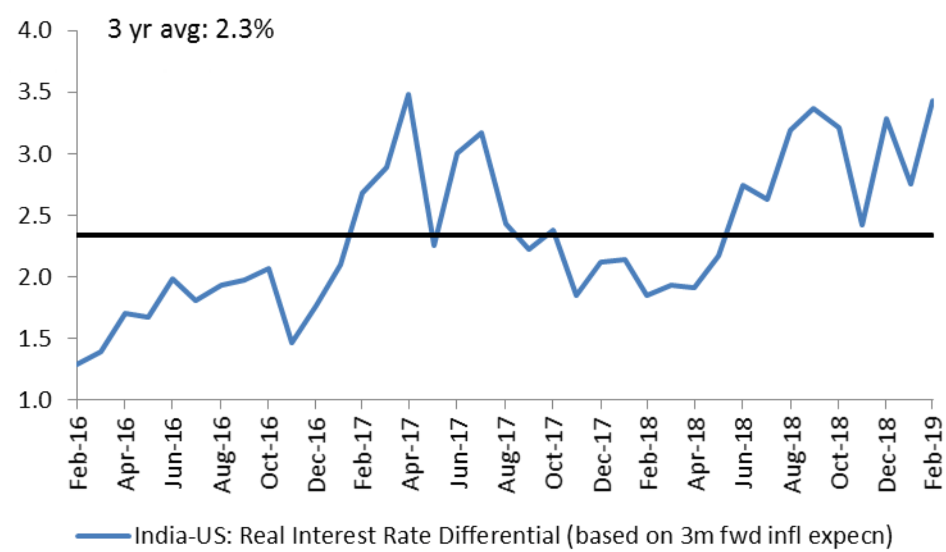
CPI Inflation adjusted real rate in India at 5.4%

Real rates	10 Year Gsec Yield (% mth end, Feb end)	CPI Inflation - Jan	Real Rate (in %)	Sovereign Credit Rating by S&P
India	7.41	2.1	5.4	BBB-
South Africa	9.26	4.0	5.3	BB
Brazil	9.00	3.8	5.2	BB-
Indonesia	7.79	2.8	5.0	BBB-
Malaysia	3.90	-0.7	4.6	A-
Mexico	8.18	4.4	3.8	BBB+
Colombia	6.86	3.2	3.7	BBB-
Russia	8.43	5.0	3.4	BBB-
Thailand	2.47	0.3	2.2	BBB+
Poland	2.96	0.9	2.1	BBB+
Phillippines	6.34	4.4	1.9	BBB
Italy	2.75	0.9	1.9	BBB
China	3.18	1.7	1.5	A+
South Korea	1.99	0.8	1.2	AA
US	2.72	1.6	1.1	AA+
Taiwan	0.83	0.2	0.6	AA-
Spain	1.17	1.0	0.2	A-
Hungary	2.70	2.7	0.0	BBB-
Japan	-0.02	0.5	-0.5	A+
Switzerland	-0.24	0.6	-0.8	AAA
UK	1.30	2.5	-1.2	AA
Germany	0.18	1.4	-1.2	AAA
Turkey	14.97	20.4	-5.4	BB-

G-sec is trading at 122bps spread to the Repo even when 50bps rate cut looks likely (vs. LTA of 84bps)



Valuations vs. US yield are attractive



Source: Bloomberg, SBIMF Research

India’s demand-supply dynamics are deteriorating

Government Securities Demand Supply Analysis								
in Rs billion	FY13	FY14	FY15	FY16	FY17	FY18	FY19 E	FY20E
Demand Sources								
1. Banks	761	3,039	1,725	2,344	2,198	3,709	1,000	1,200
2. Insurance Companies	1,822	1,896	2,412	2,451	2,679	2,932	2,500	3,200
3. Provident/Pension/ Gratuity	2,232	446	900	160	1,360	1,267	1,300	1,300
4. RBI's Net OMO	2,073	436	-364	499	1,092	-924	3,016	1,800
5. Others	1,265	445	1,886	1,852	1,035	1,268	619	618
A. TOTAL DEMAND	8,153	6,263	6,559	7,306	8,365	8,253	8,435	8,118
Supply Sources								
1. Central Govt Sec (net of redemptions)	6,607	4,610	4,427	3,747	3,785	4,858	4,227	4,731
2. State Govt Securities (net of redemptions)	1,545	1,649	2,136	3,559	4,579	3,395	3,900	4,100
B. TOTAL SUPPLY	8,153	6,258	6,563	7,306	8,364	8,253	8,127	8,831

- In FY19, RBI’s OMO purchase came as a very strong demand support absorbing nearly one third of the Government supply or say 70% of G-sec supply (as RBI only buys G-sec not SDL). This helped off-set the weak bank demand. Banks (SCBs) had purchased only Rs. 400 billion up until Jan 2019 and can at best purchase another 600 billion in the last two months. This is sharply lower than last 5 year trend of Rs. 2-3 trillion. Banks’ SLR holdings have fallen from the peak of 28.5% in July 2019 to 25.8% i.e. 3.7% pt. in last three months.

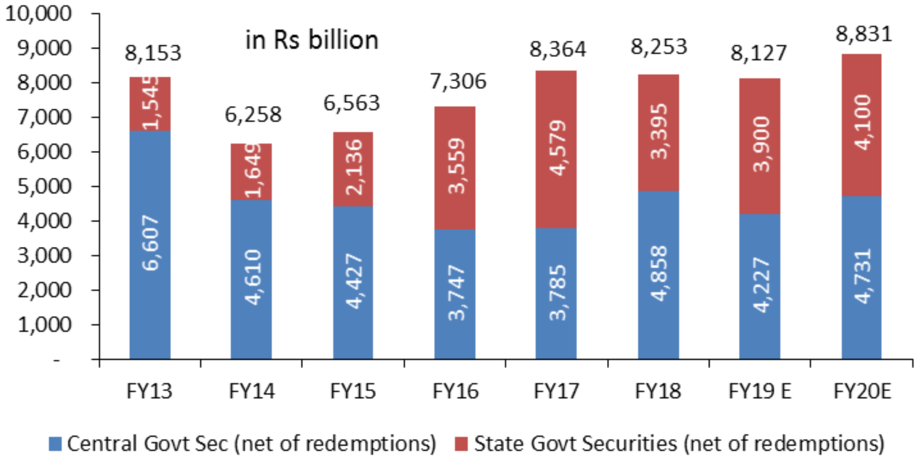
- In general, since FY14, we find that insurance and pension fund together have become a relatively larger player in the Government bond market, absorbing 40-60% of the total supply. Increasing penetration of these long-term financial products are helping the expansion of their AUM base and given the regulatory backdrop, they mandatorily invest in government securities. FY19 supply (net of redemption) was also Rs. 300 billion lesser than last two years.

- For FY20, total net supply is likely to go up by Rs. 800billion with risks tilted to upside. Coming to the demand side in FY20, OMO purchases are likely to continue in FY20 (expectation of Rs. 2 trillion). However, banks’ buying appetite is at risk given the tightness in CD ratio, regulatory relaxation in SLR holdings, and disbursement constraints in NBFC.

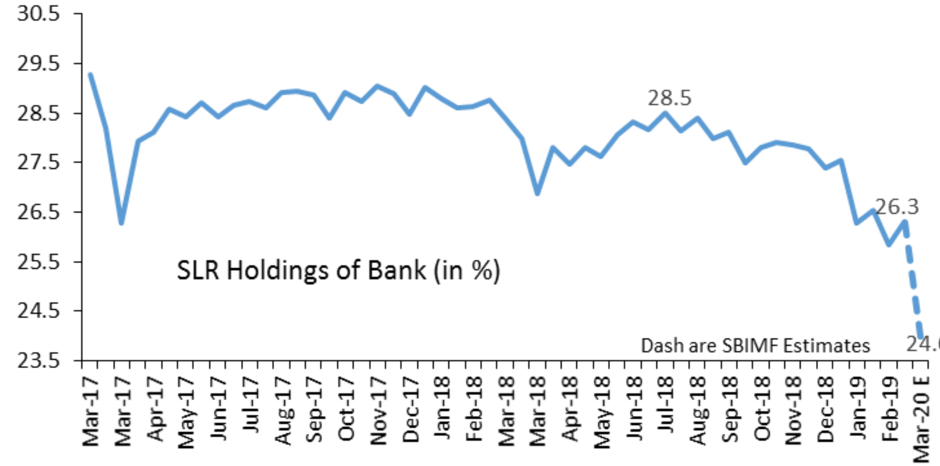
Source: RBI, IRDA, CMIE Economic Outlook, SBIMF Research

FY20 faces higher bond supply in the midst of reduced bank appetite

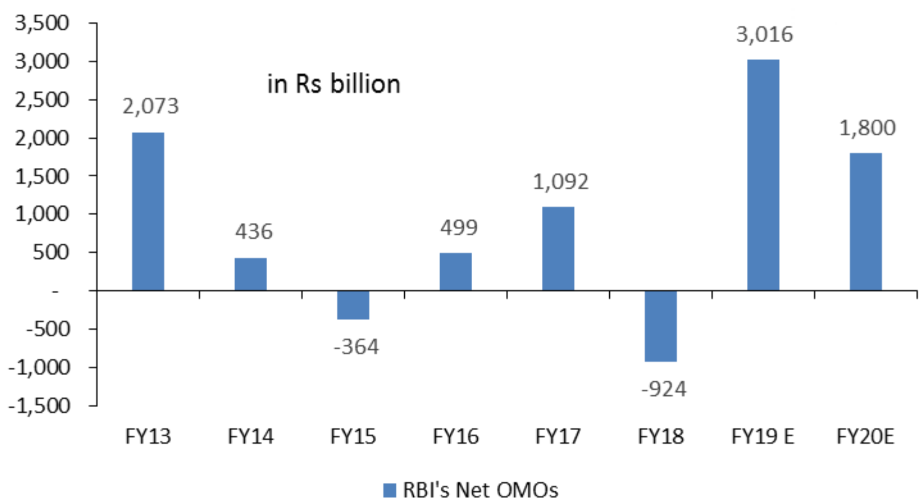
In FY20, total net supply is likely to go up by nearly Rs. 800 billion with risks tilted to upside.



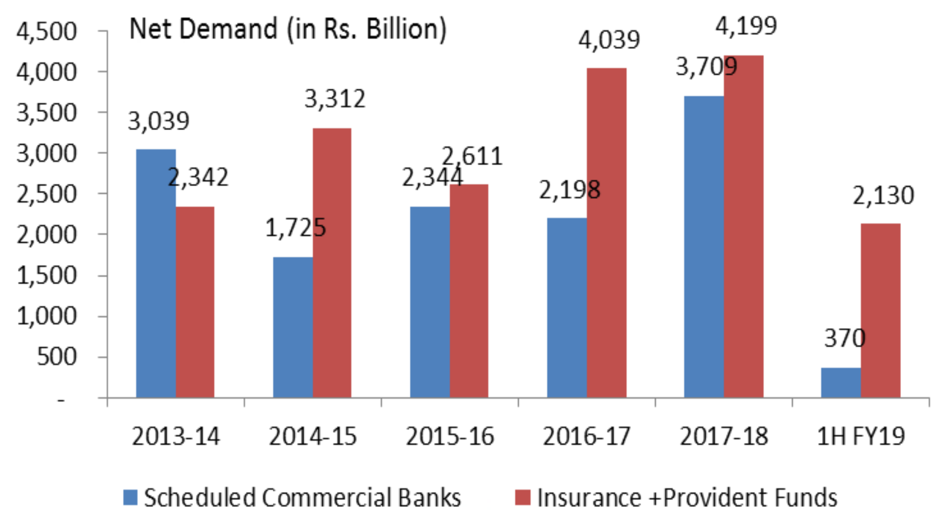
Banks' appetite for government bonds in the current tight C/D environment likely to come down



The quantum of OMO purchases may moderate in FY20



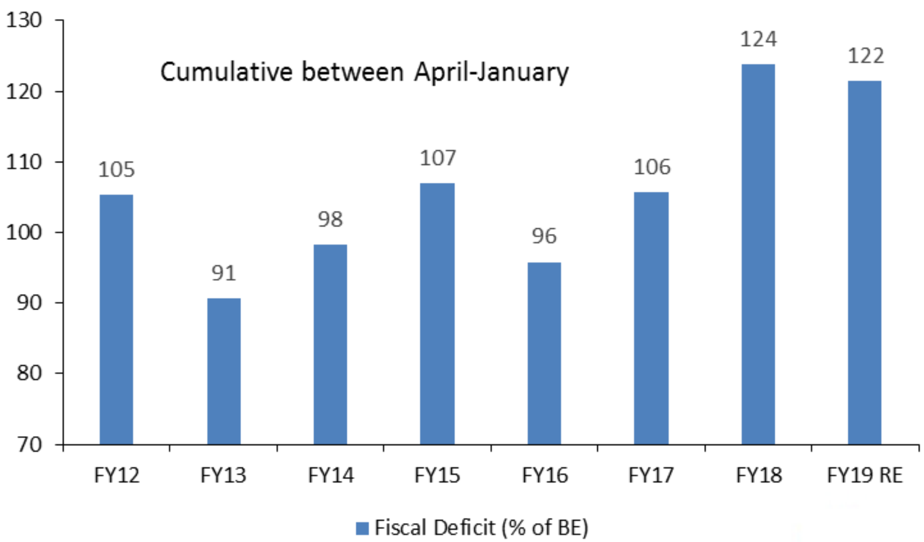
Insurance and Pension Funds are becoming larger players in the bond market over the scheduled commercial banks



Source: RBI, CMIE Economic Outlook, SBIMF Research

Central fiscal situation continue to be stressed

Cumulative fiscal deficit during Apr-Jan FY19 is running at 122% of RE



Major shortfall in revenue is led by lower GST collections, followed by excise and income tax collection

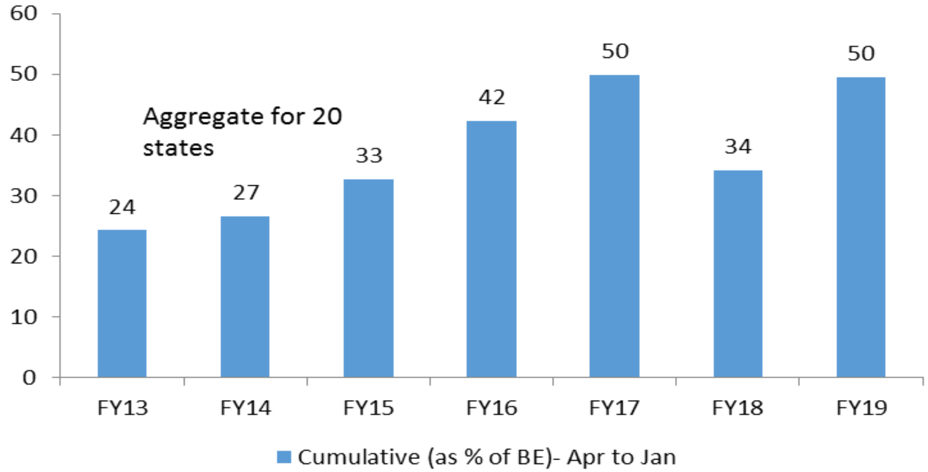
	Apr-Jan 2019 Cumulative (% y-o-y)	Growth estimate as per FY19 RE (in %)
Gross Tax Revenue	7.3	17.2
Income Tax	14.3	22.8
Corporate Tax	16.7	17.5
Custom	-9.3	0.8
Excise duties	-13.1	0.1
Total Direct Tax	15.7	19.8
Total Indirect Tax	1.5	14.3

- In the 2019 Interim budget, Union government fiscal deficit was revised higher by Rs. 101 billion from Rs. 6.24 trillion to Rs. 6.34 trillion, and from 3.3% to 3.4% of GDP. Despite the upward revision, the current fiscal deficit up until January 2019, is running 22% higher than the full year target. It is relatively higher than the past year trends.
- From the on-going tax collection, it appears that the government is going to miss its income tax, excise and GST collection targets.
- While the revised target of 3.4% may be adhered to in FY19, perhaps by postponing the payables to next fiscal, it adds to the stress in fiscal situation going forward.

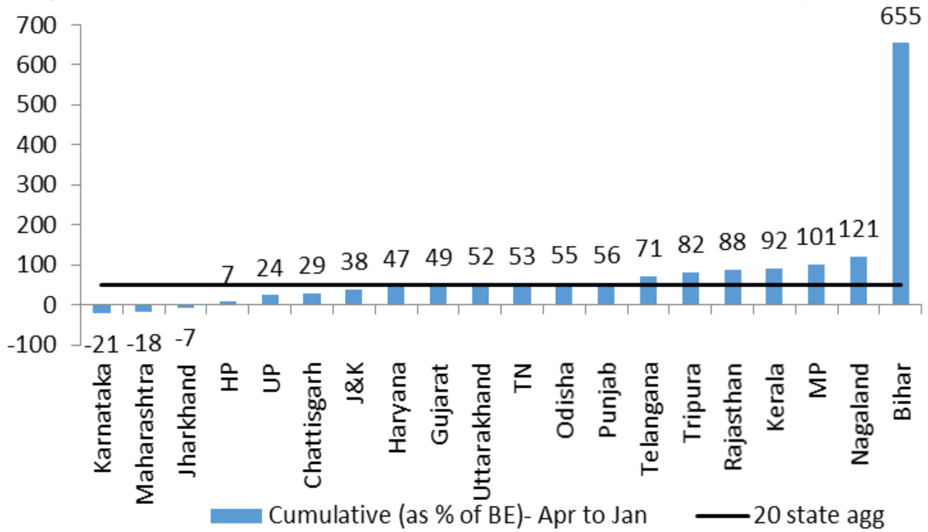
Source: CMIE economic outlook, pib.nic.in, SBIMF Research; # Yellow highlights are some of worrisome tax collection buckets

State fiscal situation points towards risks of slippage in FY19

Fiscal health of 20 states combined in the first 10 months is worse than last year and point towards the risk of slippage*



State-wise dispersion is wide. State like Bihar, Kerala, MP, Nagaland, and Rajasthan paint a worrisome picture



Tax revenue and overall receipts collection growth is running lower while expenditure is running higher than budgeted#

	Cumulative Revenue receipts in FY19 (% y-o-y)	Budgeted rev receipts for FY19- (% y-o-y)	Cumulative expenditure in FY19 (% y-o-y)	Budgeted exp for FY19 (% y-o-y)
Bihar	-57.3	15.2	37.5	9.1
Chattisgarh	13.2	10.2	11.1	19.2
Gujarat	11.2	6.9	14.6	6.8
Haryana	7.9	11.8	6.7	7.5
Himachal Pradesh	12.9	9.7	14.6	17.3
Jammu and Kashmir	7.8	10.7	15.2	2.4
Jharkhand	15.7	5.4	-4.1	-1.2
Karnataka	14.1	12.3	9.1	14.0
Kerala	17.1	9.9	16.6	0.9
Madhya Pradesh	14.9	12.1	21.2	11.5
Maharashtra	15.5	17.3	8.4	6.9
Nagaland	2.2	15.9	-18.7	-19.2
Odisha	14.9	12.7	22.5	11.4
Punjab	18.8	20.4	28.8	14.5
Rajasthan	12.5	16.5	25.8	9.6
Tamil Nadu	17.4	10.6	18.9	5.4
Telangana	15.9	15.8	5.6	13.9
Tripura	20.6	3.4	6.3	-0.6
Uttar Pradesh	20.1	9.1	22.2	14.4
Uttarakhand	13.0	12.9	5.5	11.4
Agg 20 states	**11.8**	**12.7**	**16.0**	**9.0**

Source: CEIC, SBIMF Research; * NB: 20 states in the analyses are Bihar, Chhattisgarh, Gujarat, Haryana, Himachal Pradesh, Jammu & Kashmir, Jharkhand, Karnataka, Kerala, Madhya Pradesh, Maharashtra, Nagaland, Odisha, Punjab, Rajasthan, Tamil Nadu, Telangana, Tripura, Uttar Pradesh, and Uttarakhand. # Yellow highlighted states are the most worrisome states.

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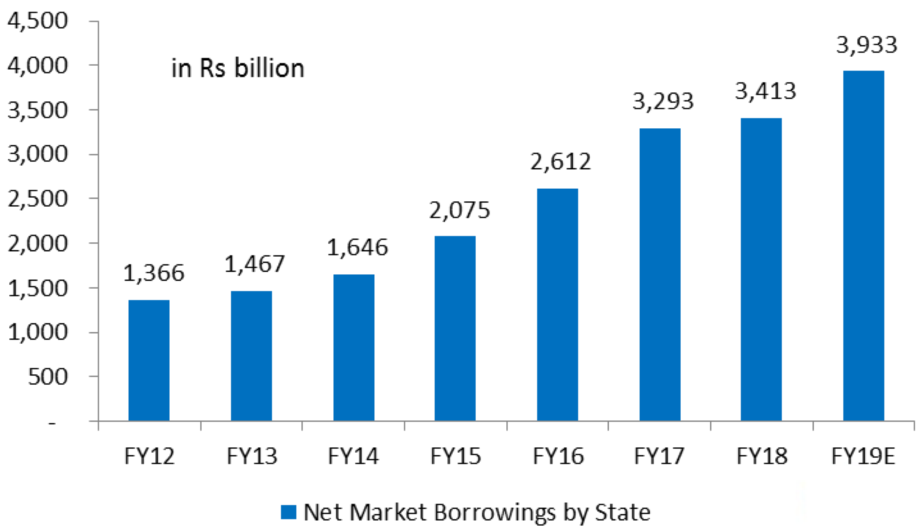
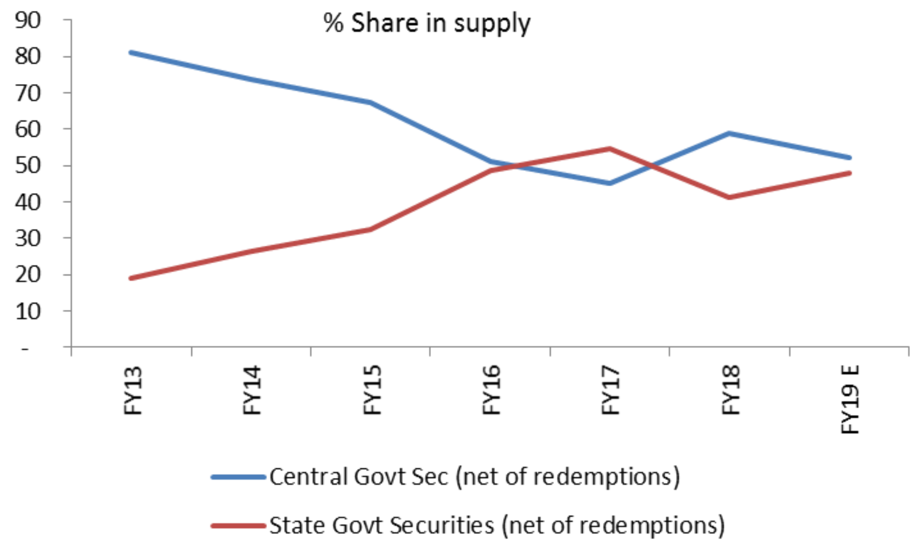
Despite fiscal risk, states may borrow Rs. 600 bn less than budgeted

SDL supply has become nearly 2.5x in last five years



SDL account for 50% of total government bonds supply vs. 25% five years ago

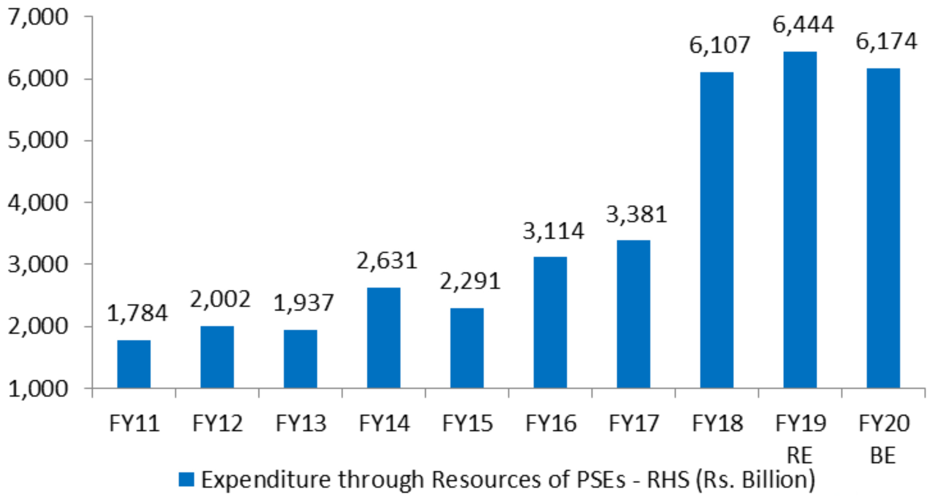


- Given the risk of fiscal slippage and unavailability of NSSF money to fund the deficit., it is surprising that state governments are borrowing much less than their budgeted targets.
- The states were in aggregate expected to borrow Rs. 5.5 trillion (gross). Going by the current weekly SDL trends, it appears that states may end up borrowing Rs. 4.9 trillion, i.e. Rs. 600 billion lower than budgeted. The net market borrowing figures is likely to stand at Rs. 3.8 trillion vs. 3.4 trillion in FY18.
- That said, the states are becoming an increasingly large player in the government bonds space. Their supply (both gross and net) has become nearly 2.5x in last five years and they now account for 50% of total government bonds supply vs. 25% five years ago.

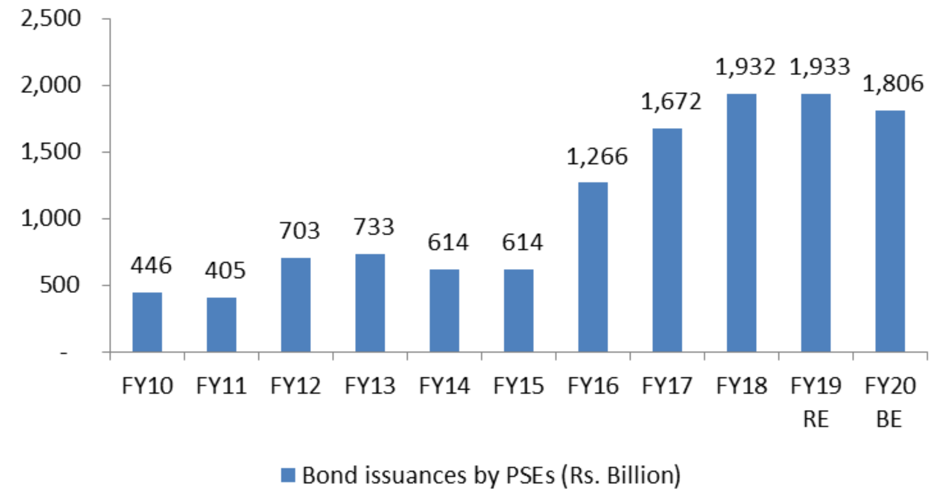
Source: RBI, SBIMF Research

Markets are facing higher borrowing from PSEs

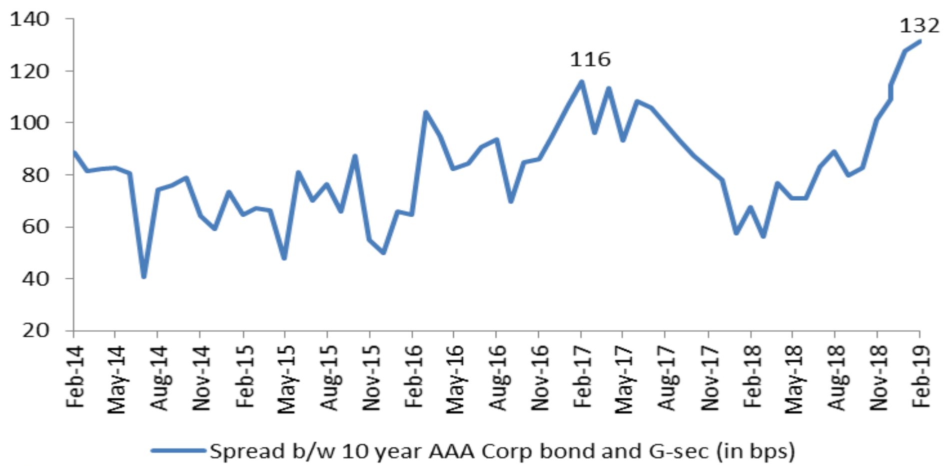
The government is increasing the expenditure via resources of various public sector enterprises (PSEs)…



….and particularly, the issuance of bonds by PSEs has tripled over the last four years…



…leading to widening spreads between AAA corporate bonds and G-sec

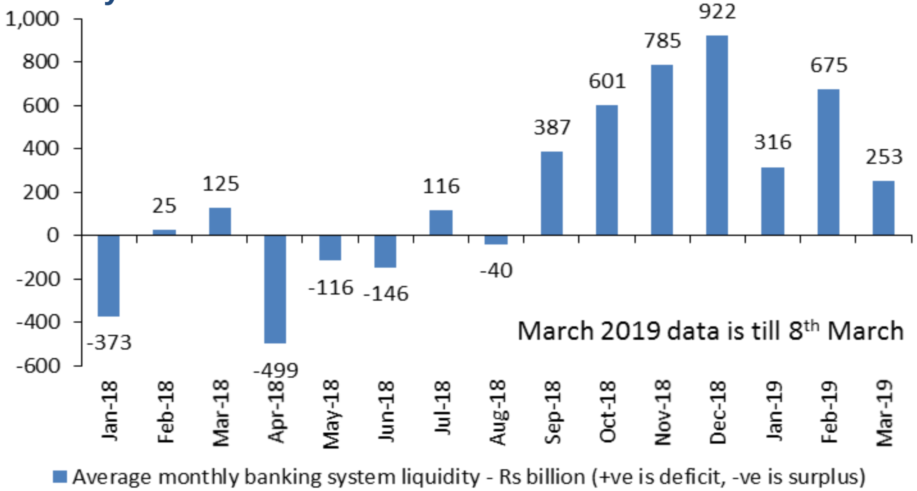


- Even though the central government's interim budget has placed FY20 fiscal deficit at 3.4% of GDP, there is a increased recourse to expenditure funding through off-balance sheet means, keeping bond supply elevated.
- As a result, corporate bond spreads are getting wider, making the non G-sec segment relatively attractive.

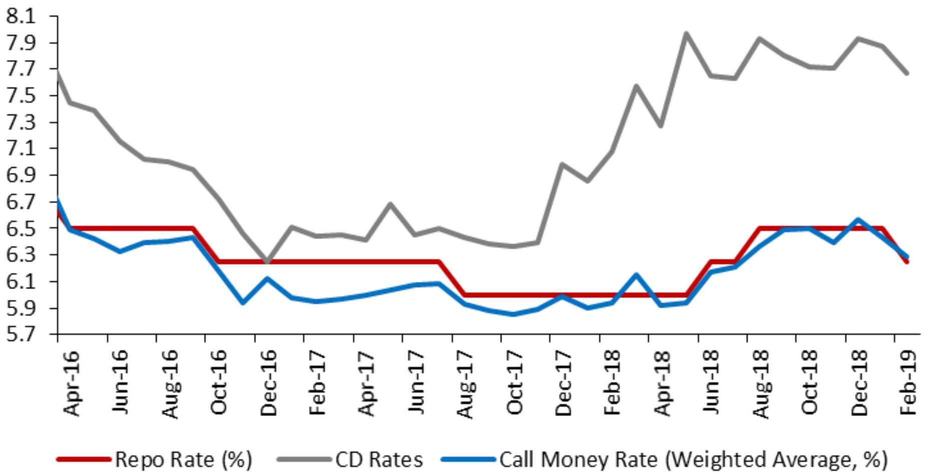
Source: RBI, indiabudget.nic.in, SBIMF Research

Banking system liquidity is tight

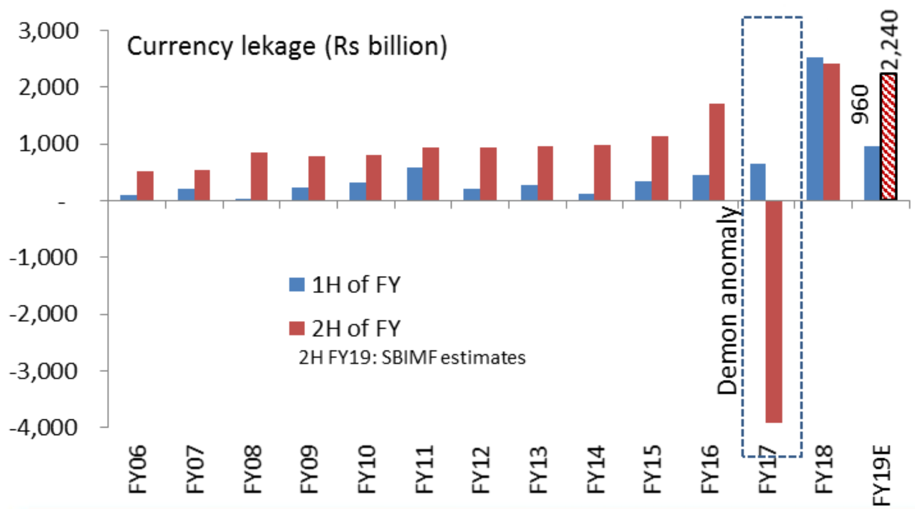
Liquidity deficit widened in February 2019 as compared to January



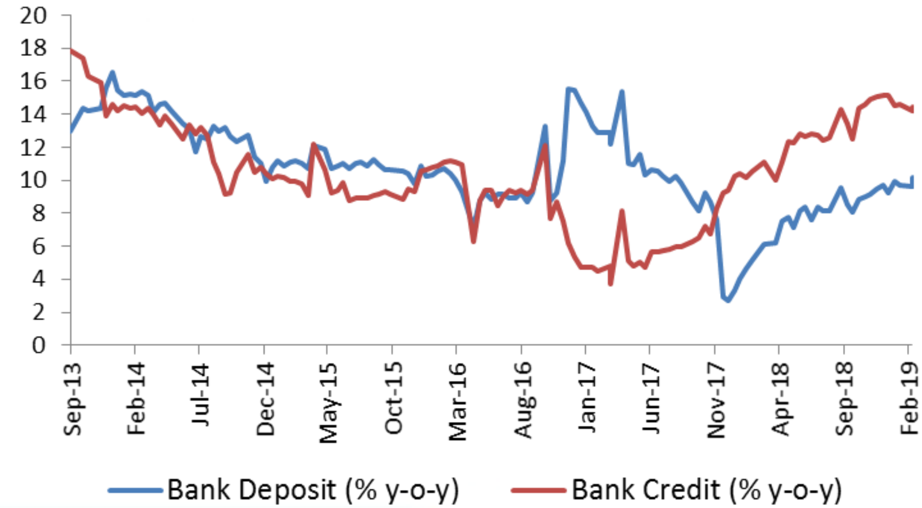
Call money rates are well anchored with repo rate but, CD rates spreads have widened



Higher currency leakage is keeping the liquidity in deficit, despite aggressive OMOs



Credit growth continue to outpace deposit growth. As a result, credit-deposit ratio at high level of 77.6x



Source: RBI, SBIMF Research

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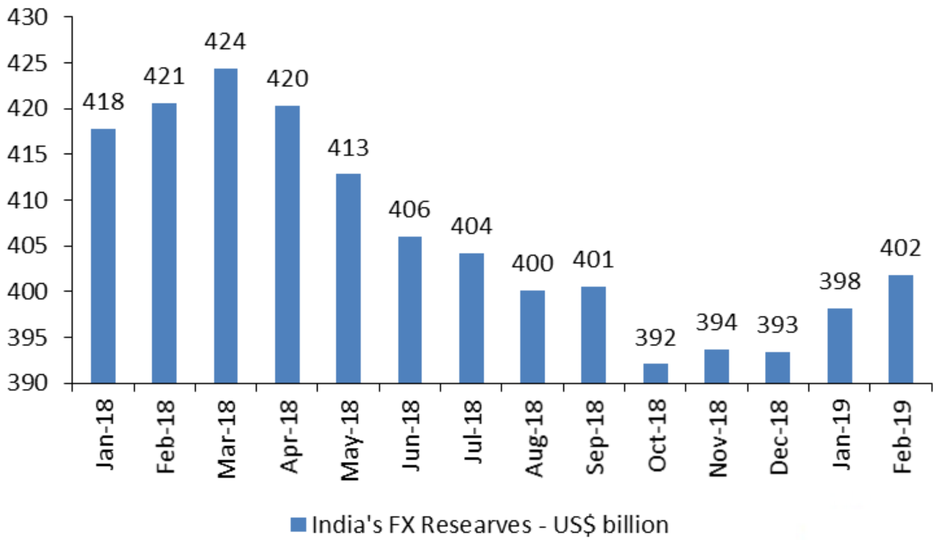
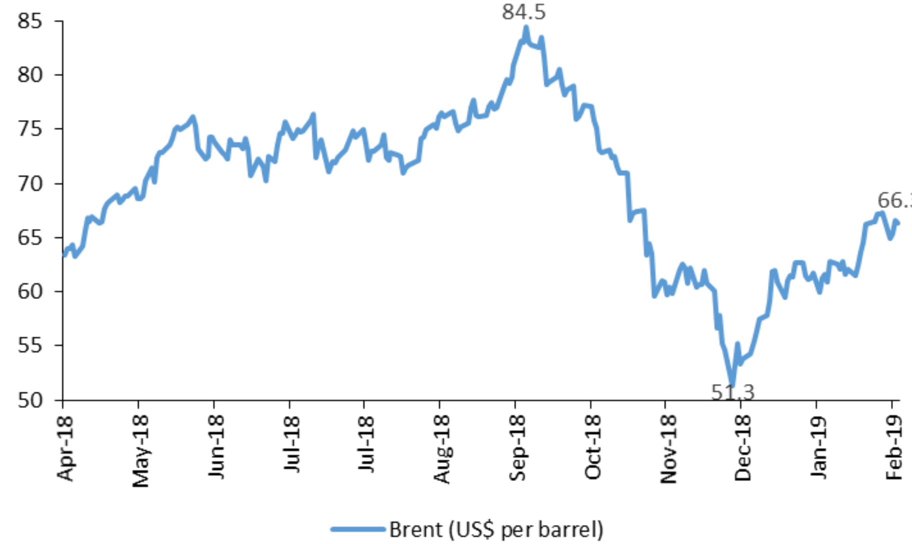
External account worry has faded in recent months

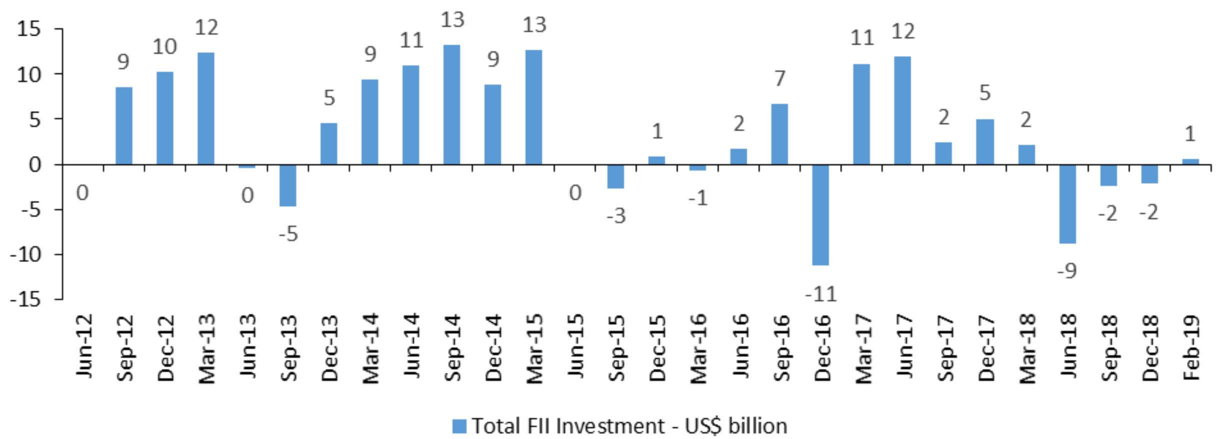
FX reserves are building-up and has crossed US$ 400billion by Feb end



Brent prices rose by 22% in 2019 (till Feb end), however, it still remains ~20% lower than its peak in October 2018



After the selling pressure in 2018, FIIs movement has nearly flattened in the first two months of 2019



Source: RBI, NSDL, Bloomberg, SBIMF Research

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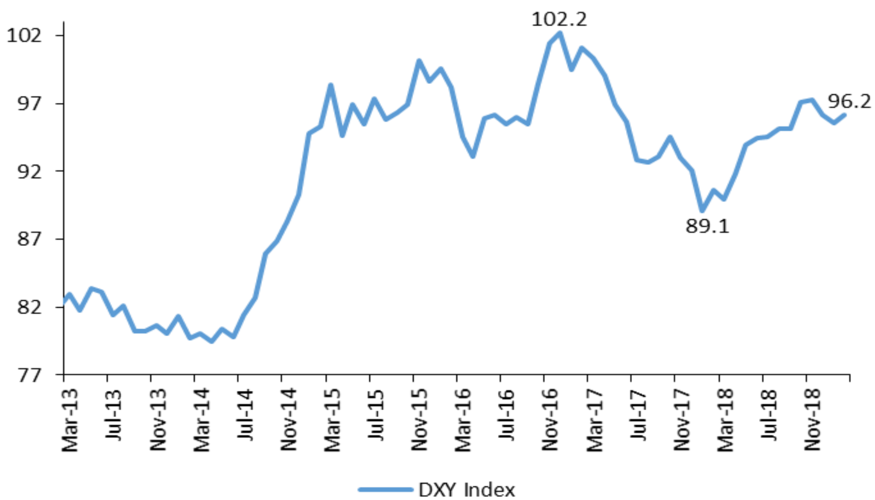
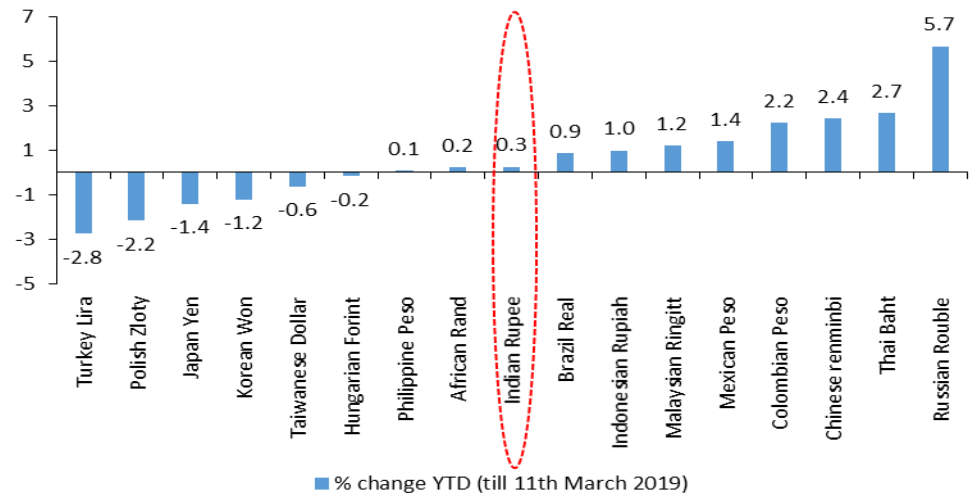
Performance of rupee is in middle when compared to other EMs

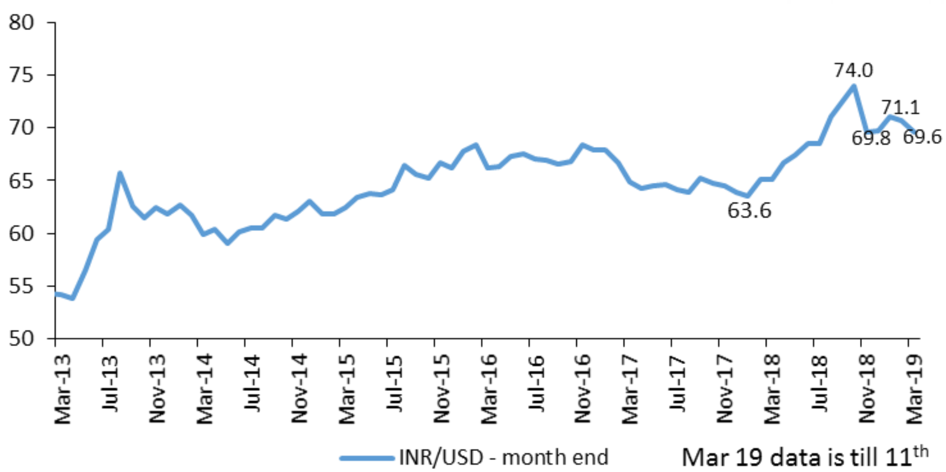
DXY strengthened by 0.6% during the month



YTD, the performance of Indian rupee is in the middle when compared to the other Emerging markets



As of 11th March, Rupee has restored to ~69.5-70/US$ - similar to 2018 end levels.



- Rupee appreciated by nearly 0.5% in February 2019 and 1.7% in March 2019 (till 11th), undoing the sharp depreciation of 1.8% in January.
- During March (till 11th), Rupee has restored its levels to ~69.5-70/ US$

Source: Bloomberg, SBIMF Research

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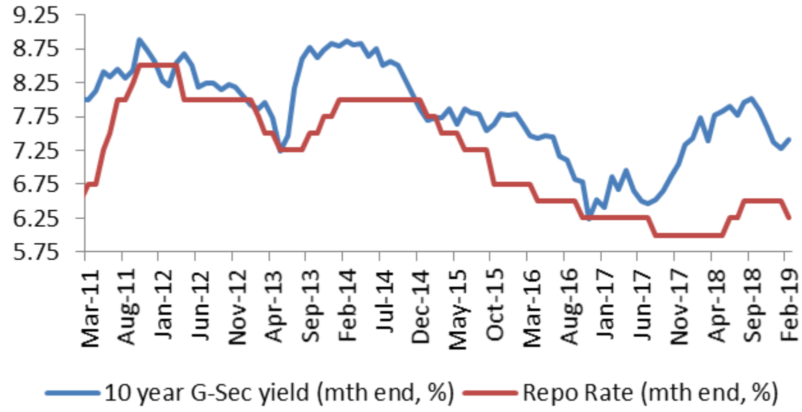
Debt Market Outlook

- Coming to the bond market, despite the 25bps rate cut in the latest February monetary policy and an indication of more cuts in the offing; 10-year G-sec has moved up by 10bps since the policy date.
- Growth-inflation dynamics are supportive of rate cuts making the valuation attractive and global environment is bond positive.
- Demand supply is the key risk to the bond outlook and is keeping the yields high despite a hint of easing monetary policy. Part of it emanates from weak fiscal, which translates into higher supply risk. The other part hinges on banks' appetite for government bonds in the current tight credit to deposit environment. Any favorable development on demand supply front should guide us towards the government bonds purchase.
- Even though the central government's interim budget has placed FY20 fiscal deficit at 3.4% of GDP, there is increased recourse to expenditure funding through off-balance sheet means, keeping bond supply elevated. This is getting reflected in wider corporate spreads and makes the non G-sec segment relatively attractive.
- In the short-term segment, household demand for cash is blunting the RBI's liquidity injections and stabilizing balance-of-payment conditions. Currency in circulation is nearing pre-demonetization trend (as percentage of GDP). We believe, a stronger drive on GST compliance post elections should reverse this trend. In the interim, however, the currency spike is effectively delaying the intended impact of the RBI's liquidity push. In the near-term, the liquidity could tighten further, as government builds its cash balance before the month end.

Valuations look attractive at G-sec vs. Repo rate



Source: Bloomberg, SBIFM Research

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Thank you

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