



The Federal Open Market Committee (FOMC) minutes published for the May meeting, indicated that the federal funds rate would most likely be increased by 50 bps each in the next two policy meetings. The minutes showed that the members were wary of the soaring inflation and would remain committed to address concerns on that front. The ongoing war between Russia and Ukraine and lockdowns in China would remain a key monitorable going forward.

The Personal Consumption Expenditures (PCE) price inflation projection was revised up and is now expected to be 4.3% in 2022 while falling thereafter to 2.5% in 2023. The minutes also indicated that the FOMC's focus would remain to swiftly move the stance of the monetary policy towards neutral (through frontloading of rates and reduction in the Fed's balance sheet) and from then to a restrictive policy stance depending on the incoming data on economic outlook and inflation. US CPI inflation for April 2022 came in at 8.3% (marginally lower than 8.5% in March 2022, although higher than consensus estimates). Core inflation also remained higher at 6.2%. The 10-year US Treasury yields traded in the 2.75% to 3.15% band during the month, and are currently trading a shade above 3.0%. Crude prices continued to remain elevated and traded in the USD 100/bbl to USD 120/bbl band during the month. Although OPEC+ agreed to increase oil output to stem the rising crude prices, Brent has continued to trade around USD 120/bbl.

MARKET PERFORMANCE

Post the surprise inter-meeting rate hike by the MPC last month, yields have continued their sharp trajectory upwards, as expectations of frontloading of rate hikes are getting priced in.

On a month-on-month basis (as on May 31, 2022), money market rates have moved up by 90-110 bps and 2-3 year G-Sec and Corporate bonds are higher by 80-100 bps. Yields in the 5-10 year segment have also moved up by 30-60 bps. OIS levels have also seen a similar move.

The 10-year benchmark G-Sec yield closed at 7.42%, up by 28 bps from its previous close of 7.14% while that on the short-term 1-year bond ended 112 bps higher at 6.07%.

In the corporate bond segment, yields rose across the yield curve over the month. The 10-year AAA bond yield ended 42 bps higher at 7.75%, while the short-term 1-year AAA bond yield ended 115 bps up at 6.40%.

The spread between 1-year and 10-year AAA bond narrowed. Within the short-term segment, the yield on 3-month commercial paper (CP) was up 100 bps to 5.15% while the 1-year CP yield was up 125 bps at 6.40%.

10-Year G-Sec



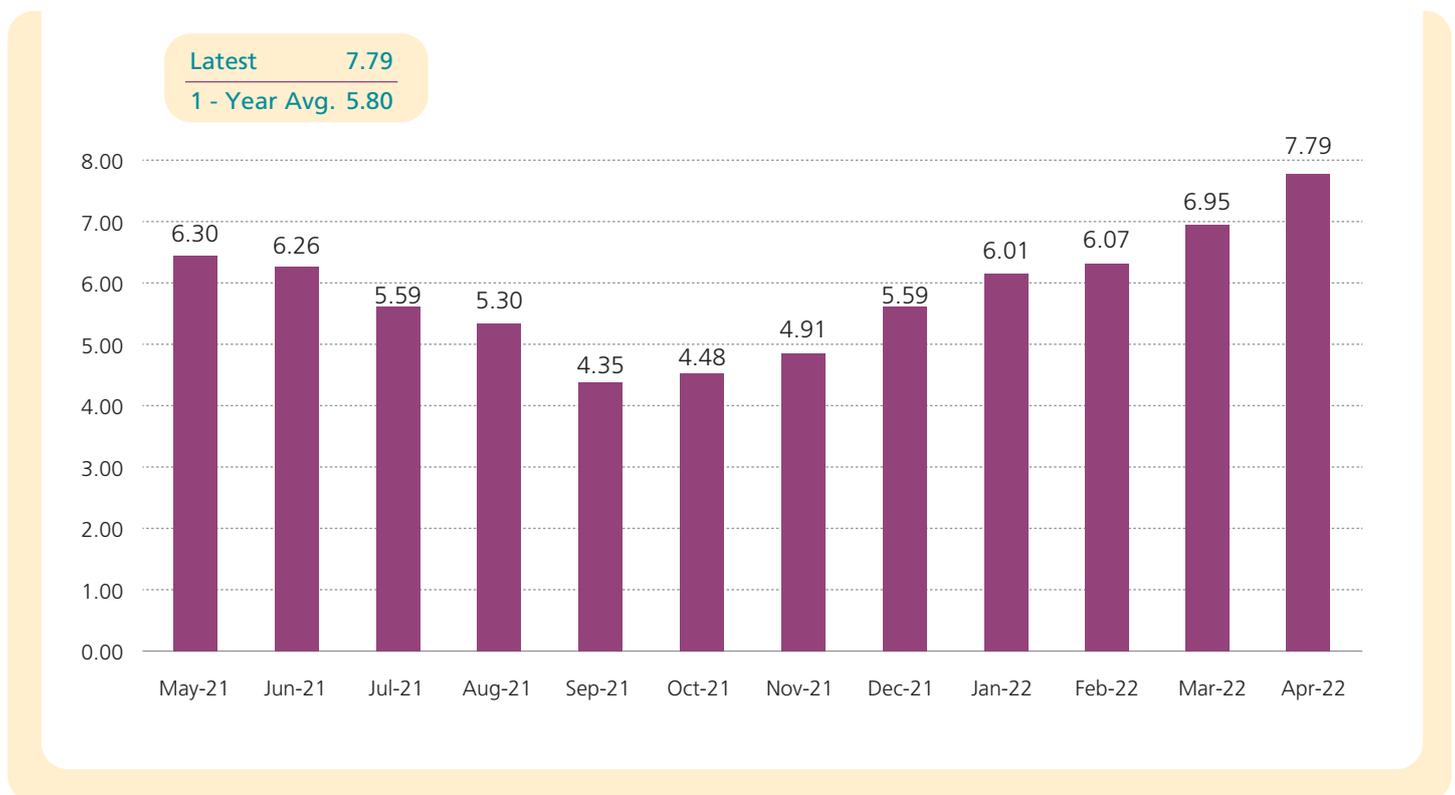
Past performance may or may not be sustained in the future.



MACRO-ECONOMIC DEVELOPMENTS

On the domestic front, CPI inflation for April 2022 came in at a multi-year high (higher than expectations) of 7.79% (vs 6.95% in March 2022) due to higher food and fuel price inflation. Core CPI also edged higher to 7.0%. WPI inflation continued its upward trajectory clocking 15.08% in April 2022 (vs 14.55% in March 2022). Higher crude prices have continued to put pressure on inflation.

CPI Combined (YoY)



IIP for March 2022 remained sluggish at 1.9% (vs 1.7% in February 2022). Consumer durables and non-durables continued to remain in contraction. For the full year FY2022, IIP recorded an expansion of 11.3% y-o-y.

Trade deficit for April 2022 widened to USD 20.11 bn (vs USD 15.29 bn last year). Although exports have been robust, higher oil prices continue to put pressure on the import bill, resulting in markets now penciling in higher CAD estimates for FY2023.

PMI numbers have been encouraging with Manufacturing PMI at 54.6 and Services PMI at 58.9 in May 2022.

The GDP growth for Q4 FY2022 came in at 4.1% (in line with market expectations), taking the full year GDP growth for FY2022 to 8.7%. Fiscal deficit for FY2022 came in at 6.7% of GDP (slightly below the revised Budget estimate of 6.9%).



In an attempt to tackle inflationary pressures, Government of India (GOI) reduced excise duty on petrol and diesel by INR 8/liter and INR 6/liter respectively. Some of the states followed this up with cut in state taxes. The impact of the excise cut on inflation is estimated to be around 20-30 bps and the annual revenue loss to the Government is expected to be INR 1 Lakh Cr. However, the actual revenue deficit would be lower as the impact would be spread across 10 months and would only be incremental to the excise cut already factored in the Budget. RBI announced surplus transfer to the GOI to the tune of around INR 30,000 Crs (lower than budget estimates). The Government also announced the approval of additional spending on fertilizer subsidy to the tune of INR 1.1 Lakh Crs, taking the total possible outgo to INR 2.15 Lakh Crs. Subsequently, there was also news around the subsidy number being even higher. **With disinvestments lagging and food subsidy also expected to be higher, fiscal pressures have once again come to the forefront. A higher nominal GDP might partly offset the shortfall, while a cut in capital expenditure also remains a lever with the Government. However, the evolving supply-demand dynamics will remain a key monitorable going forward.**

Source: MOSPI, Internal, Bloomberg

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