RELIGARE Invesco Mutual Fund

Fixed Income Markets: Current Environment and Outlook

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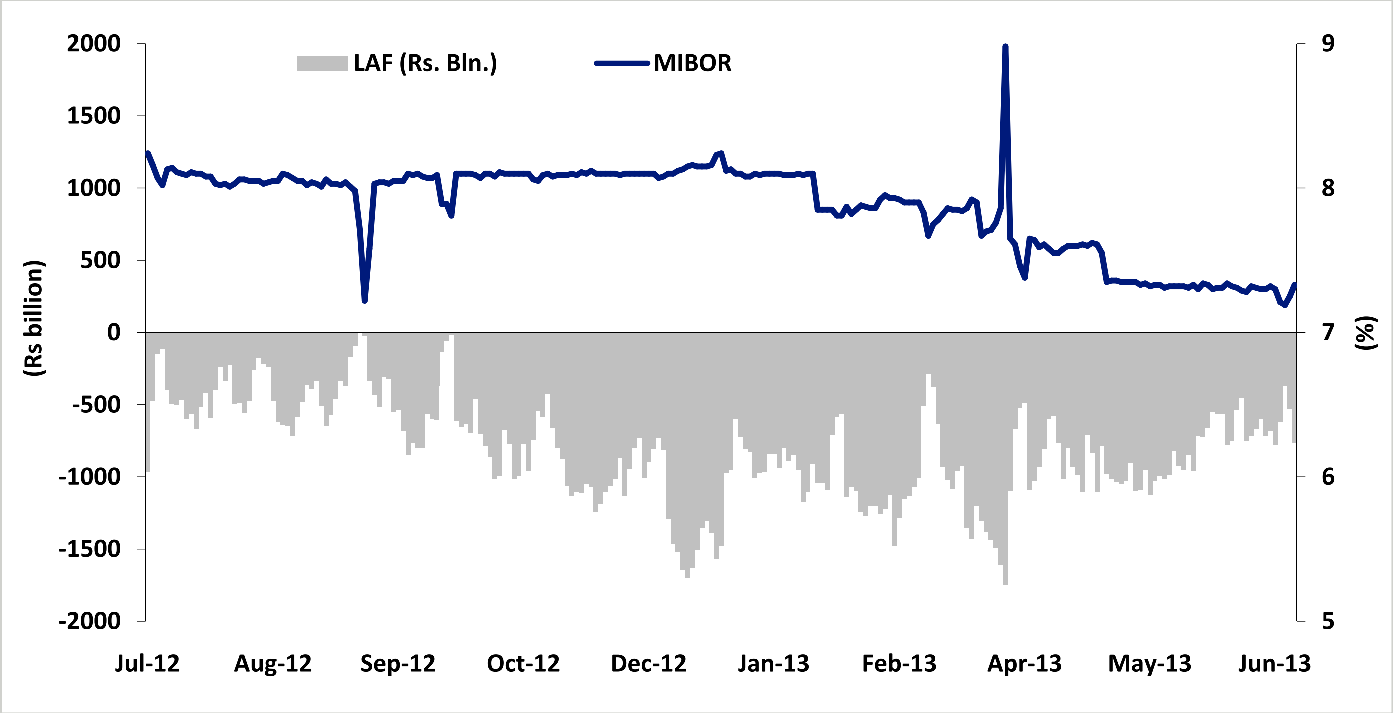
Macro Economic Events - Domestic

- The economic data is pointing at mixed results
- There has been a consistent drop in both WPI & CPI inflation and a sharp decline in CAD
- The IIP and exports growth points at a sluggish domestic production and external demand

	May 13	Apr 13
CPI	9.31%	9.39%
WPI	4.70%	4.89%
Imports	7.00%	10.96%
Exports	-1.10%	1.68%
	Apr 13	**Mar 13**
IIP	2.30%	3.40%
	Mar 13	**Dec 12**
GDP	4.80%	4.70%
	Mar 13	**Dec 12**
CAD	-18.17 USD Bn	-31.77 USD Bn

Source: Bloomberg. IIP: Index of Industrial Production, CPI: Consumer Price Index, WPI: Wholesale Price Index, GDP: Gross Domestic Product, CAD: Current Account Deficit

Liquidity



- Over the last few months, the liquidity position within the banking industry has improved to a certain degree. The liquidity on an average for the month has remained negative by Rs. 638 billion

- It appears that the new month might witness some further easing of liquidity

Source: Bloomberg. LAF: Liquidity Adjustment Facility. MIBOR: Mumbai Inter-Bank Offer Rate

Money Market (spread between 12M T bill & CD)

- The spreads of bank CDs contracted over T-bills over the month
- The improvement of liquidity has led to the contraction

Source: Bloomberg

Inflation Dynamics

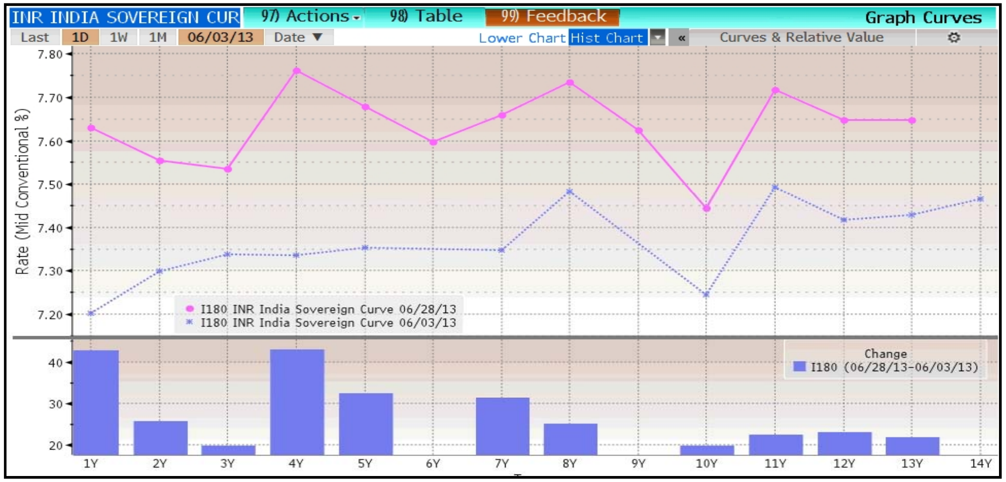
- The decline in WPI continues over the month
- The present level is below RBI's target level (i.e. 5%)

Source: Bloomberg.

G-Sec Yield Curve

10 Year G – Sec Yield Curve

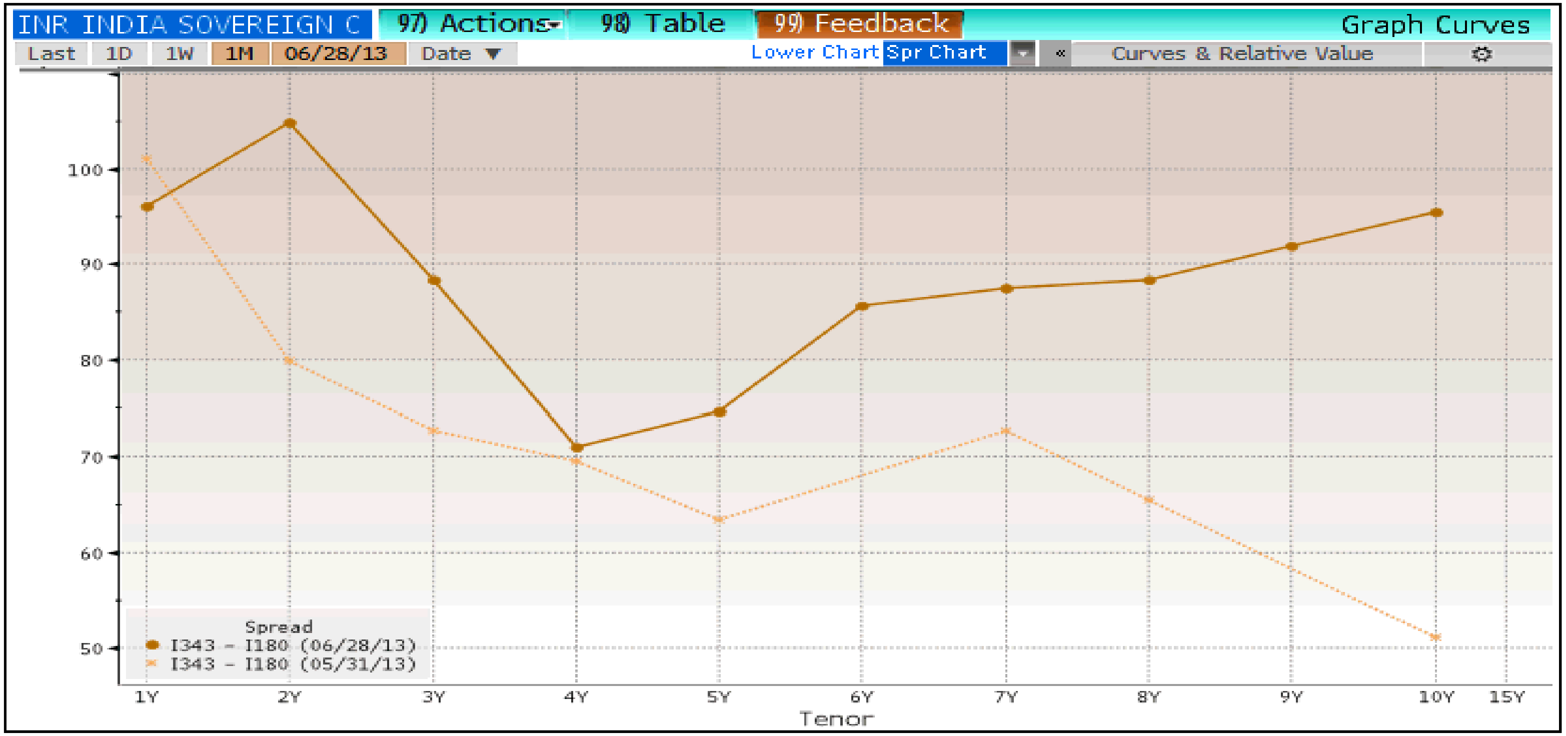
G – Sec Yield Curve Change



- There was selling by FII’s in the bond market
- The FII selling along with the swift decline in the value of INR led to hardening of yields over the month
- The yields hardened by about 40bps at the worst
- The entire yield curve shifted northwards

Source: Bloomberg

Corporate Bond spreads widened



- The selling from the FII segment initially started in the gilts segment and later included corporate bonds as well

- The credit spreads widened over the month and touched a high of 90bps+ from 70-75bps about 1 month back

Source: Bloomberg. I343: Indian PSU AAA Curve, I180: INR Indian Sovereign Curve

Fixed Income Outlook and Opportunities

Fixed Income Market Outlook

Negatives

- The possible improvement in the landed rupee cost of the oil imports has worsened due to the depreciating currency despite improvement in the dollar value of crude oil
- The recent trend might have short to medium term hardening effect on inflation. The drop in the WPI inflation is also expected to get nullified in case the present trend is to continue over the quarter
- While it appears, there is a bigger room for rate reduction given the drop in the WPI inflation, the current account deficit issues and the fiscal deficit will continue to play an important role in the policy actions

Positives

- The recent government actions in terms of improving the accessibility of Indian debt and gilts for foreign investors is expected to increase the demand for Indian papers over the medium to long term subject to currency risk

Outlook

- The yield movement in the fixed income market is largely expected to be guided by the behavior of the currency and FII interest for Indian debt
- While the credit spreads have widened over the previous month, the spreads are not expected to contract soon given the continued selling by the foreign investors
- Notwithstanding, the recent volatile market conditions ,we expect the yields to be soft over the remainder of the year and will also be determined by the progression of the monsoon and the ensuing food prices thereafter
- Whilst the fiscal & current account deficit and currency risks continue to remain in the market, RBI actions over the quarters are expected to remain benign in a phase of contained inflation risk
- The risk-reward matrix is in favor of staying invested in the bond market, and investors are encouraged to select funds with duration longer than their investment horizon in an environment of declining interest rates

Portfolio Actions during the month

- **Religare Invesco Liquid Fund:** The fund has started increasing the non-bank exposure. The rate decline has improved the financing conditions amongst select credits

- **Religare Invesco Ultra Short Term Fund:** The fund is maintaining a marginal exposure to MTM assets and moderating the exposure actively. The fund is increasing the higher yielding papers in the portfolio of shorter maturities

- **Religare Invesco Short Term Fund:** The fund has maintained duration around 18 months, mostly through corporate bonds

- **Religare Invesco Credit Opportunities Fund:** The fund has been successfully investing in mis-priced credits with low interest rate risk

- **Religare Invesco Active Income Fund:** The fund has been actively trading in the liquid PFI credit segment apart from the 10 year plus gilt segment. We actively managed the portfolio duration between 2.5 - 6 years. The exposure to gilts has been pared down given the market volatility

- **Religare Invesco Gilt Fund – Long Duration Plan:** The fund has been actively trading in the liquid 10 year plus gilts. Its investing upto 30 years gilts. Currently maintaining a portfolio modified duration between 4 - 8 years

- **Religare Invesco Gilt Fund – Short Duration Plan:** The fund has been actively trading in the liquid segment of the gilts market. The average maturity has been mostly within 2 years

- **Religare Invesco Bank Debt Fund:** The fund is largely invested in the Bank CD and Bank Bonds segment. Its maintaining a portfolio modified duration between 2 – 3.5 years

- **Religare Invesco Medium Term Bond Fund:** The fund has maintained a duration of around 3 years through a combination of debt, gilts and money market securities of up to 5 years residual maturity

Ideas for investors

- The market volatility has gone up significantly over the last 1 month. Investors are encouraged to select funds with duration slightly higher than their investment horizon. The volatility is expected to subside as liquidity conditions improve and the swap rates also soften over the month. All short-duration funds should be able to sail through this period well and are in a position to deliver some capital appreciation.

- The *Religare Invesco Credit Opportunities Fund* offers an opportunity for investors with short investment horizons of 1 - 3 months and moderate level of credit risk appetite. The fund is ideally positioned to capture mis-priced risk in an environment of deficit liquidity and superior credit spreads of short maturity papers

- The *Religare Invesco Short Term Fund* offers accrual along with a contained interest rate risk. Ideal for investors with 3 - 6 months investment horizon

- The *Religare Invesco Medium Term Bond Fund* offers higher current yield and moderate interest rate risk. The present duration of around 36 months opens up opportunities of capital appreciation over a 3 - 9 month investment horizon for investors with moderate risk appetite

- The *Religare Invesco Active Income Fund* – It opens up opportunities of capital appreciation in an environment of the yield curve steepening through active duration management within 2 - 6 years. It is intended for investors with varied investment horizon (at least 3 months) with moderate to high risk appetite

- The *Religare Invesco Bank Debt Fund* – a thematic high credit quality portfolio comprising of bank CD and bank bonds, along with a small allocation to gilts/PFI. It's a superior investment allocation for credit risk averse long term investors, looking for stable returns, along with some capital appreciation from a well regulated industry over a 1 year investment horizon

- The *Religare Invesco Gilt Fund – Long Duration Plan* – It opens up opportunities of capital appreciation in an environment of credit risk aversion and hence higher demand for gilts. An actively managed gilt portfolio during phases of credit risk aversion is intended for investors with varied investment horizon (at least 3 months) with moderate to high interest risk appetite

Note: The above product positioning and intended duration is based on current view and is subject to change from time to time.

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Mutual Fund investments are subject to market risks, read all scheme related documents carefully.

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Mutual Fund

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