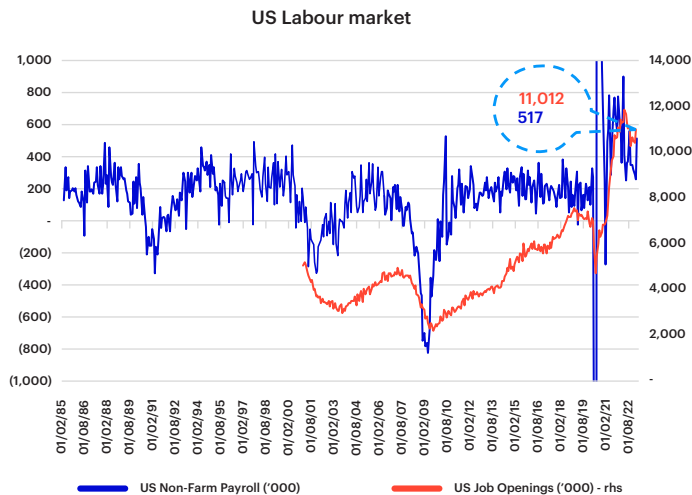




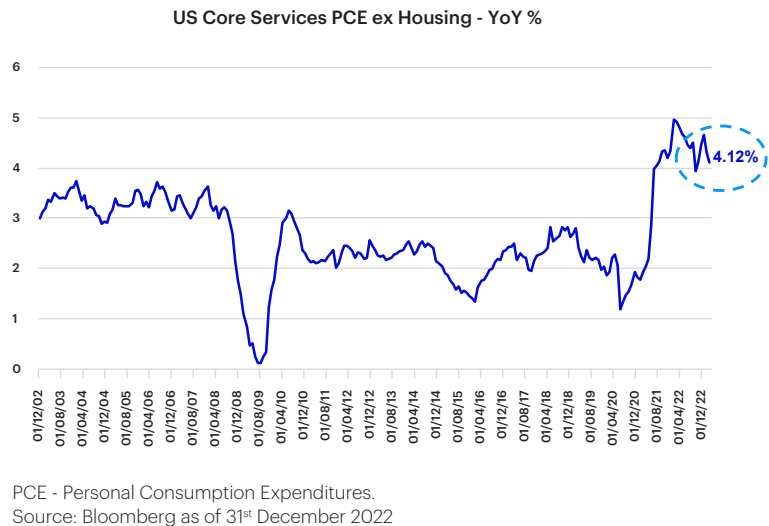
Herin Shah
Head - Credit Research

An interesting tug of war is happening in rates market between FED and the participants. Recent FOMC meeting concluded with FED hiking US interest rates to 4.75% (upper bound) and mentioned another couple of hikes. However interest rates across the US curve came down and the USD weakened.

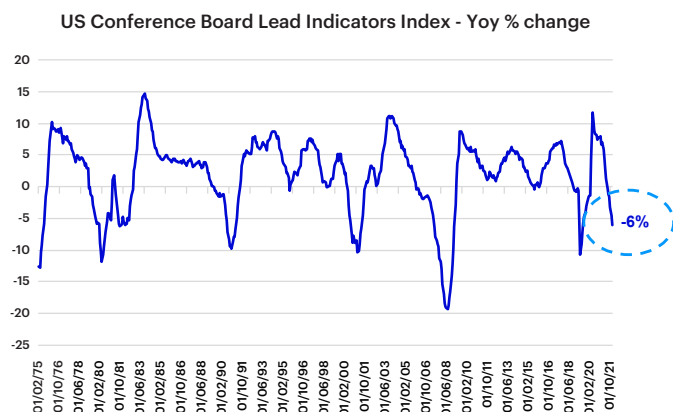
FED remains focused on strong labour market and sticky core services PCE which remain elevated



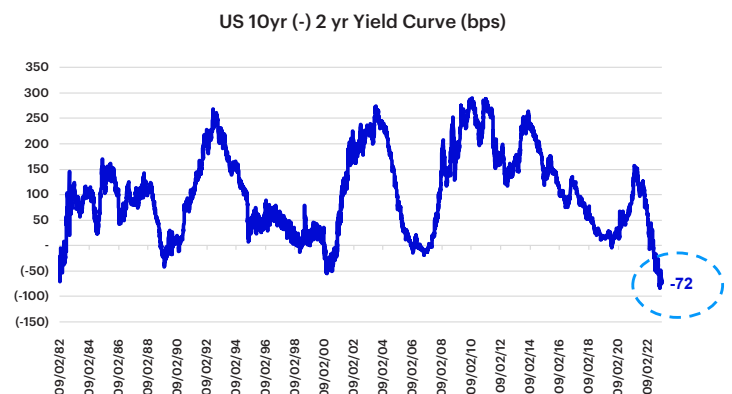
Source: Bloomberg as of 31st January, 2023 for US Non-Farm Payroll
Source: Bloomberg as of 31st December, 2022 for US Job openings



Markets are focusing on lead indicators which signal sharp slow-down and not believing in FED hawkishness.

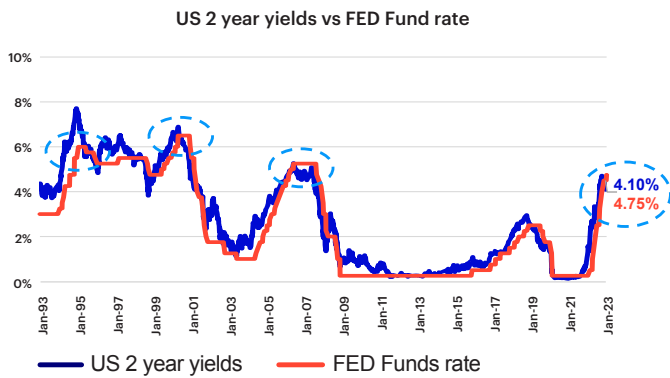


Source: Bloomberg as of 31st December 2022



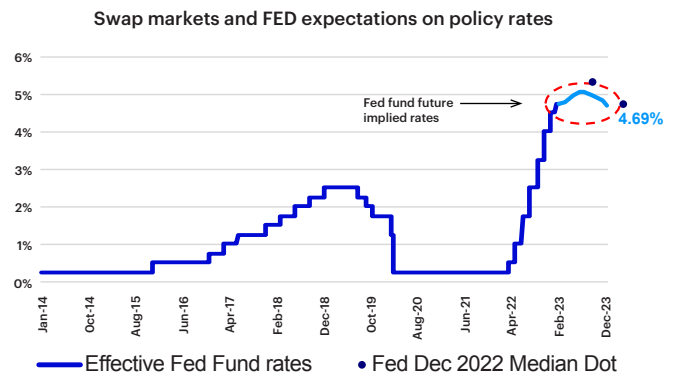
Source: Bloomberg as of 2nd February 2023

Swaps pricing one more FED hikes and a rate cut in 2023. FED indicating at least 2 more rate hikes and no rate cut in 2023



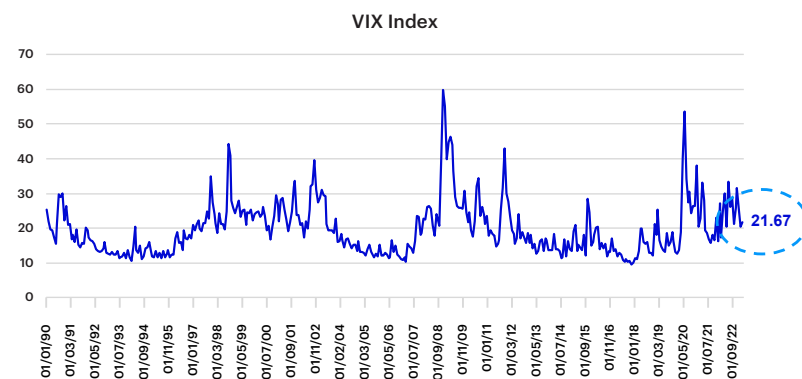
Source: Bloomberg as of 2nd February, 2023

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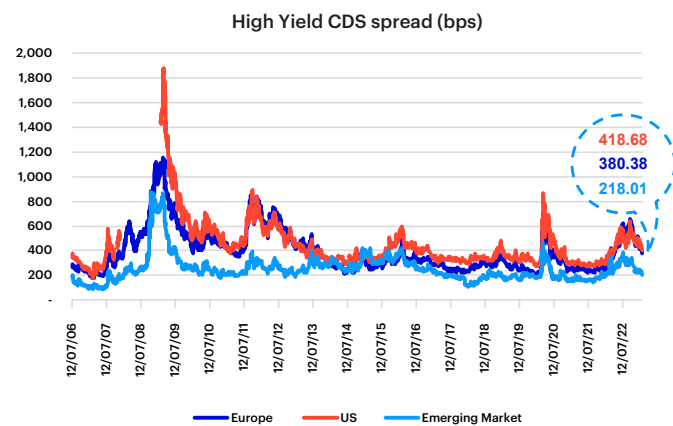


Source: Bloomberg as of 2nd February, 2023

Financial conditions have loosened recently as risk assets price in China re-opening and soft landing in US and Europe



Source: Bloomberg as of 30th December 2022



VIX: Volatility Index. Source: Bloomberg as of 6th February 2023

Our Thoughts:

- Markets to remain volatile as the tug of war plays out. Further policy path will become data dependent and either market or central banks will have to adjust meaningfully.
- We think markets are under-pricing US labour market tightness and hence sticky services inflation. Markets seem to be also under-estimating FED resolve to not pivot. Markets are priced for soft landing along with FED pivot.
- USD weakness can reverse as markets re-price rates expectation and risk assets re-adjust.
- With India's FY24 fiscal deficit target and borrowing programme in line with market expectation, range-bound oil prices cushioning CAD and stable FX reserves, bonds are fairly priced. FX markets can be the conduit for domestic volatility especially if USD strengthens.
- MPC hiked rates by 25 bps and kept further path open largely due to evolving global factors. This shall help to cushion meaningful FX weakness.

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