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Status-quo on policy rates and accommodative policy stance re-iterated the criticality of growth recovery. Broadly, a more balanced policy with growth projections confirming to improving fundamentals. Inflation remains elevated amid supply-side disruptions & global commodity prices, though seen to be transitory and moderating over the period with RBI focussed on achieving its medium-term target. More quantum and clarity on variable rate reverse repo (VRRR) auctions dispel uncertainty regarding abrupt liquidity withdrawal and is an initial step towards liquidity re-calibration. Assurance on maintaining ample liquidity indicates benign & easy financial conditions.

Key decisions/Highlights

Policy **Repo rate remains unchanged at 4%** and Reverse repo rate at 3.35%. All MPC members **unanimously voted in favor of keeping the policy rates unchanged.**

No change in other policy rates; Marginal Standing Facility (MSF) rate and Bank rate stands unchanged at 4.25%.

Monetary Policy Committee (MPC) **to continue with the accommodative stance as long as necessary** to revive and sustain growth on a durable basis and continue to mitigate the impact of COVID-19 on the economy, while ensuring that inflation remains within the target going forward. **The MPC voted 5:1 to continue with the accommodative policy stance.**

The Consumer Price Index (CPI) based inflation revised upwards for FY22 by 60 bps and is now projected at 5.7% (5.1% earlier); 5.9% in Q2 (5.4% earlier); 5.3% in Q3 (4.7% earlier); and 5.8% in Q4 (earlier 5.3%) with risks broadly balanced. CPI inflation for Q1 FY23 is projected at 5.1%

Real Gross Domestic Product (GDP) growth projection retained at 9.5% for FY22 consisting of 21.4% in Q1 (earlier 18.5%), 7.3% in Q2 (earlier 7.9%), 6.3% in Q3 (7.2% earlier) and 6.1% in Q4 (6.6% earlier). Real GDP growth for Q1 FY23 is projected at 17.2%

Regular operations for liquidity management to continue; timelines for couple of liquidity measures extended with a view to support nascent economic recovery.

The **amount absorbed under the fixed rate reverse repo is expected to remain more than Rs. 4 lakh crores** at end-September 2021

To conduct two more auctions of Rs. 25,000 crores each on August 12 and August 26, 2021 under G-sec Acquisition Programme (G-SAP 2.0). Besides, open market operations (OMOs) and operation twist (OT), among others, to continue and will be calibrated in line with the evolving macroeconomic and financial conditions.

On Tap targeted long-term repo operation (TLTRO) scheme extended by a period of 3 months till December 31, 2021.

Extension in period of relaxation on Marginal Standing Facility (MSF) by 3 months till December 31, 2021.

Re-commencement of VRRR given higher demand in terms of the bid-cover ratio in the auctions and forms part of system liquidity. RBI will conduct fortnightly VRRR auctions of Rs. 2.5 lakh crore on August 13, 2021; Rs. 3.0 lakh crore on August 27, 2021; Rs. 3.5 lakh crore on September 9, 2021 and Rs. 4.0 lakh crores on September 24, 2021.

Balanced policy with no change in rates and policy stance

This MPC policy was set amidst the backdrop of rising inflation concerns as the last 2 inflation readings came above the 6% mark which is outside of the RBI's inflation targeting framework of 2% - 6%, led by the global commodity prices & supply side disruption and along with that rising concerns on resurgence of new Delta variant of Covid-19 in many countries which brings back the uncertainty to the overall growth outlook.

As in the past and on expected lines, RBI decided to continue with its growth supportive stance by maintaining status quo on the policy rates and re-assuring of the continuation of low rates as long as necessary to revive and sustain growth on a durable basis and continue to mitigate the impact of COVID-19 on the economy, while keeping a close watch on the inflation trajectory. This is the seventh consecutive policy when MPC has maintained the status quo on rates, and we feel that RBI will prioritize growth and will continue with its accommodative stance while keeping the rates steady for the rest of year.

More confidence on growth recovery, though still nascent

This time RBI seems more confident on growth with GDP projections retained at 9.5% for FY22 and projected at 17.2% in Q1 FY23 on the back of continued robust outlook on rural demand & likely improvement on urban demand with vaccination drive gaining pace. However, amid lingering uncertainty due to Covid-19 disruptions, RBI highlighted that economic recovery may remain uneven and continued policy support is needed to sustain durable economic recovery.

Inflation stays elevated; exogenous & largely transitory

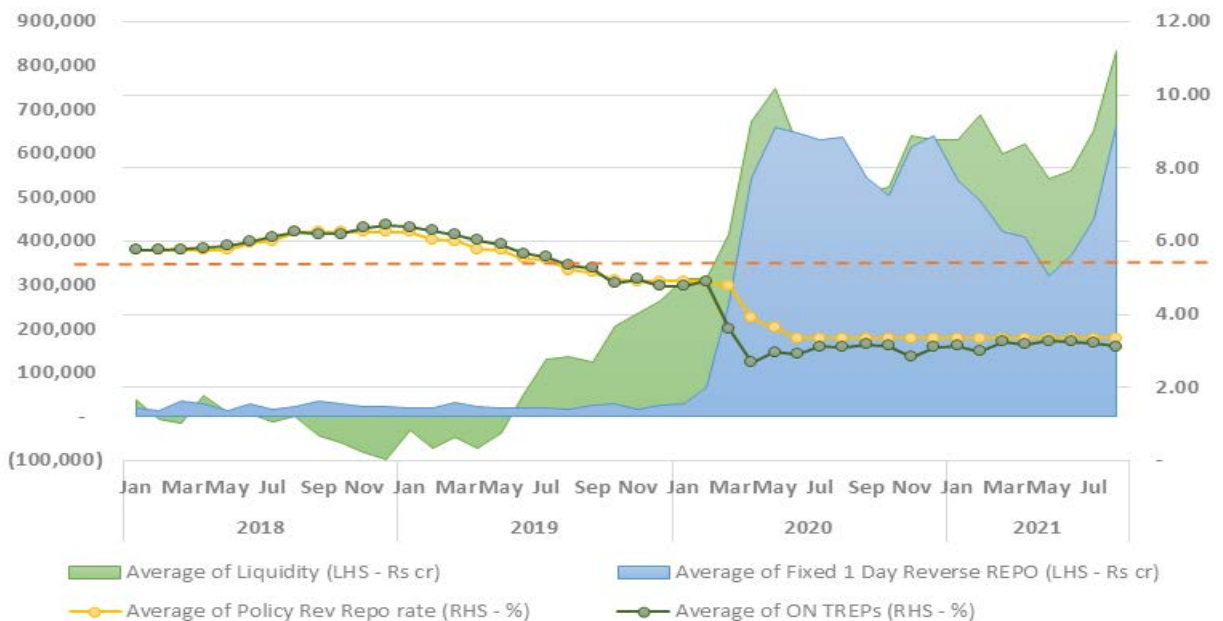
The RBI has revised FY22 inflation forecast upwards by 60 basis points acknowledging global commodity pressures and supply side constraints. MPC notes that recent inflationary pressures evoke concerns, but appears to be transitory and largely driven by adverse supply side factors - "exogenous and largely temporary supply shocks driving the inflation process, validating the MPC's decision to look through it". Dr Patra during the press conference, alluded to the fact that RBI has been able to maintain the inflation close to 4% over the period FY2016- FY2020, which shot up to 6.3% only in FY21 due to covid led disruptions and is now expected to have a moderating trajectory with FY22 inflation projected at 5.7%. We feel that, in such a scenario of unprecedented disruption, MPC might overlook current high inflation and will continue to give higher priority to the concerns around growth recovery, while remaining focussed on its inflation mandate over the long term. Directionally, Q1FY23 inflation projection does show some moderation.

Higher quantum of VRRR is more of a routine liquidity operation, not a fundamental shift

One of the critical part for us to watch out for was RBI's liquidity measure considering that the systemic liquidity has risen to more than Rs. 8 lakh crores and any abrupt announcement of longer than 14 days or higher quantum of VRRR could have been market disturbing (recall: January 2021 first VRRR measure which sent the short end rates soaring by almost 1%). While RBI increased the quantum of 14-day VRRR from current Rs. 2 lakh crores to Rs. 4 lakh crores in phases till September 2021, it made amply clear that this measure is a part of routine liquidity operation and should not be construed as a reversal of the accommodative policy stance. In-fact the very mention that the amount absorbed under the fixed rate reverse repo is expected to remain more than Rs. 4 lakh crores at end September 2021 is re-assuring the market of ample surplus liquidity and takes away the uncertainty on liquidity front at least over next few months.

We feel that RBI has taken gradual approach and it is an initial step towards liquidity re-calibration amid massive built-up of surplus liquidity in the system and as such we don't see much impact on short-term rates due to higher quantum VRRR.

Monthly Systemic Liquidity & Liquidity under 1-day fixed rate Reverse Repo



Source: Bloomberg. ON TREPs- Overnight TREPs

As clearly reflected in the above chart, Rs. 4 lakh crores of liquidity under 1 day Fixed Reverse Repo will be much higher than the pre-Covid times (~Rs 65,000 crores in Feb 2020) and will be closer to that in the months of March / April 2021. While the liquidity under 1 day Fixed rate Reverse repo had steadily been increasing since July and had risen to ~Rs 6.6 lakh crores in August, Overnight TREPs rate had remained almost stable in the range of ~ 3.15% - 3.25%. Accordingly, we don't expect much disruption on short end rates with more quantum of VRRR.

Liquidity measures extended and G-SAP 2.0 to continue

The liquidity window under on Tap targeted long-term repo operation (TLTRO) and Marginal Standing Facility (MSF) is extended till December 31, 2021 and is conducive for overall benign liquidity conditions. Additionally, the bond buying under the GSAP 2.0, usage of Open Market Purchase Operations (OMOs) & Operating Twists is in line of RBI's endeavor to ensure orderly evolution of the yield curve.

Market reaction post policy announcement

Segment	Broad movement of yields today in bps	
	G-Sec	AAA Corporates
3 Months	+2	Flat
6 Months	+2	+2
1 year	Flat	+1 to 2
2 -3 years	+4 to 5	+6 to 7
4 - 5 years	+5 to 6	+5 to 6
10 years	+3	+5 to 6

Data source: Bloomberg.

Fund Positioning

Status quo on policy rates and accommodative stance has reconfirmed our expectation that RBI will give precedence to durable economic recovery, despite the elevated inflationary risks. We continue to believe that RBI will hold the policy rates steady for the rest of the year and will continue to use all the possible tools to revive & support the growth.

We also expect RBI to maintain ample liquidity and conducive financial conditions with gradual approach towards normalization of policy rates, initially beginning with calibrated approach on liquidity withdrawal measures.

We feel that 6-9 months segment of the yield curve provides opportunity to risk-averse investors amid expectations of gradual normalization of policy rates with a possibility of reverse repo rate hike in beginning next calendar year or so. **Our funds like Invesco India Ultra Short Term Fund, Invesco India Money Market Fund and Invesco India Treasury Advantage Fund are apt for such risk-averse investors looking for short term investment horizon.**

The 2-5 years segment of the yield curve remains attractively placed from carry perspective given the current steepness of the curve. Additionally, benign liquidity conditions and favorable demand- supply dynamics also augers well for this segment. **Our funds such as Invesco India Corporate Bond Fund, Invesco India Short Term Fund and Invesco India Medium Duration Fund largely positioned in 2-5 years space provide attractive investment opportunity amid RBI's continued accommodative policy and liquidity stance.**

Investors with long term horizon and ability to absorb short term volatility may consider Invesco India Banking & PSU Debt Fund which is positioned at longer-end of the curve and finds merit on the back of conviction that RBI will manage the yield curve and may support the long-term yields through the tools like G-SAP and regular Open Market Purchase Operations / Operation Twist and secondary market intervention. While the credit environment is expected to improve over the medium term, we believe credit dispersion will continue as of now, with very high-quality credits benefitting from RBI's benign liquidity policy but the lower quality credits continuing to be avoided for the time being. At the same time, very selective AA+/ AA credits backed by strong internal credit assessment can also be considered.

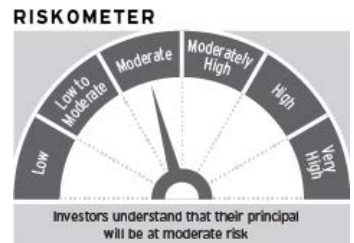
Invesco India Banking & PSU Debt Fund

(An open-ended debt scheme predominantly investing in Debt instruments of banks, Public Sector Undertakings, Public Financial Institutions and Municipal Bonds)

Suitable for investors who are seeking*:

- Returns over short to medium term
- Investments primarily in debt & money market instruments issued by Banks, PFIs, PSUs and Municipal Bonds

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



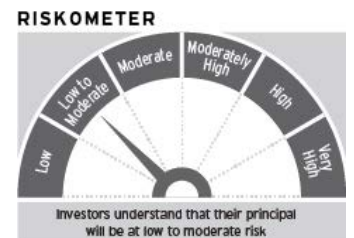
Invesco India Short Term Fund

(An open ended short term debt scheme investing in instruments such that the Macaulay duration[^] of the portfolio is between 1 year to 3 years)

Suitable for investors who are seeking*:

- Income over short to medium term
- Investments in short term debt and money market instruments

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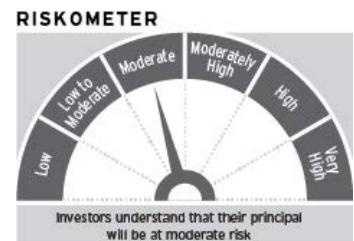
Invesco India Corporate Bond Fund

(An open ended debt scheme predominantly investing in AA+ and above rated corporate bonds)

Suitable for investors who are seeking*:

- Income over medium to long term
- Investments in AA+ and above rated corporate bonds

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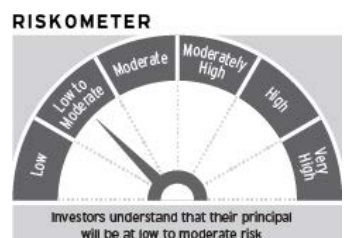
Invesco India Treasury Advantage Fund

(An open ended low duration debt scheme investing in instruments such that the Macaulay duration[^] of the portfolio is between 6 months to 12 months)

Suitable for investors who are seeking*:

- Income over short term
- Investment in debt and money market instruments

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



[^]Please refer to the heading 'C. Asset Allocation Pattern' under Section 'II. Information about the Scheme' of Scheme Information Document where the concept of Macaulay duration has been explained.

Note - Macaulay duration of a bond is the number of years taken to recover the initial investment of a bond. It is calculated as the weighted average number of years to receive the cash flow wherein the present value of respective cash flows is multiplied with the time to that respective cash flows. The total of such values is divided by the price of the security to arrive at the duration.

Invesco India Medium Duration Fund

(An open ended medium term debt scheme investing in instruments such that the Macaulay duration[^] of the portfolio is between 3 years and 4 years)

Suitable for investors who are seeking*:

- Income over medium term
- Investments predominantly in debt and money market instruments with portfolio Macaulay Duration of 3 – 4 years

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



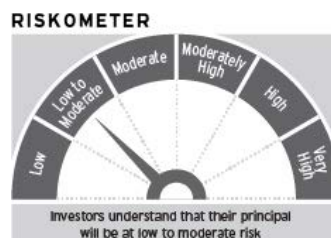
Invesco India Ultra Short Term Fund

(An open ended ultra-short term debt scheme investing in instruments such that the Macaulay duration[^] of the portfolio is between 3 months to 6 months))

Suitable for investors who are seeking*:

- Income over short term
- Investments in a portfolio of short term money market and debt instruments

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



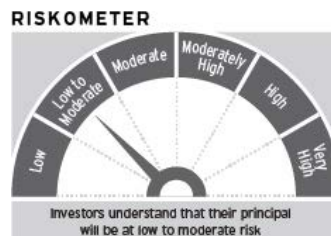
Invesco India Money Market Fund

(An open ended debt scheme investing in money market instruments)

Suitable for investors who are seeking*:

- Income over short term
- Investment in money market instruments

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



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