

FIRST LIGHT

RESEARCH

BOB ECONOMICS RESEARCH | CURRENCY OUTLOOK

Where is INR headed in 2023?

BOB ECONOMICS RESEARCH | BONDS WRAP

Fortnightly review

DIVERSIFIED FINANCIALS | Q3FY23 PREVIEW

Healthy quarter likely for NBFCs and life insurers

SUMMARY

INDIA ECONOMICS: CURRENCY OUTLOOK

In 2022, INR depreciated by 10.1% led by a rally in dollar. DXY index gained by 8.2%. This is turn was due to Fed's aggressive monetary policy tightening. In 2022, Fed raised policy rates by a cumulative 425bps. While other global central banks also raised rates, they lagged the Fed and hence saw their currencies lose value against the dollar. India too did not remain immune. Further complicating the narrative was India's weakening domestic fundamentals such as high inflation, surging trade and CAD deficits as well as softening foreign inflows. However, we remain optimistic that the worst may be over for the INR and it may appreciate to 80-83/\$ in 2023. In saying so, risks do remain as a sharper than anticipated global slowdown may spur a fresh rally in the dollar.

[Click here for the full report.](#)

INDIA ECONOMICS: BONDS WRAP

In Dec'22, bond yields globally changed direction and went for an upswing as Federal Reserve now expects a higher terminal rate at 5.1%. Even ECB officials hinted at peak inflation might not be way past us. These moves impacted yield trajectory. On domestic front, RBI's policy remained in line with market expectation, thus 10Y yield did not exhibit much volatility. However, with ending of calendar year and a review of the yield situation compared to previous year, brings some interesting conclusion.

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Daily macro indicators

Indicator	29-Dec	30-Dec	Chg (%)
US 10Y yield (%)	3.81	3.87	6bps
India 10Y yield (%)	7.31	7.33	2bps
USD/INR	82.81	82.74	0.1
Brent Crude (US\$/bbl)	82.3	85.9	4.4
Dow	33,221	33,147	(0.2)
Hang Seng	19,741	19,781	0.2
Sensex	61,134	60,841	(0.5)
India FII (US\$ mn)	28-Dec	29-Dec	Chg (\$ mn)
FII-D	144.9	(52.0)	(196.9)
FII-E	(51.6)	56.6	108.2

Source: Bank of Baroda Economics Research

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DIVERSIFIED FINANCIALS: Q3FY23 PREVIEW

- IIFL Wealth projected to post Q3 AUM/PAT growth of 9%/12% YoY on higher operating leverage and strong recurring flows
- SBI Card's spends expected to grow 18% YoY with a 43% rise in PAT on higher income and lower credit costs
- SBI Life remains our top life insurance pick given its cost efficiency and high margins

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CURRENCY OUTLOOK

02 January 2023

Where is INR headed in 2023?

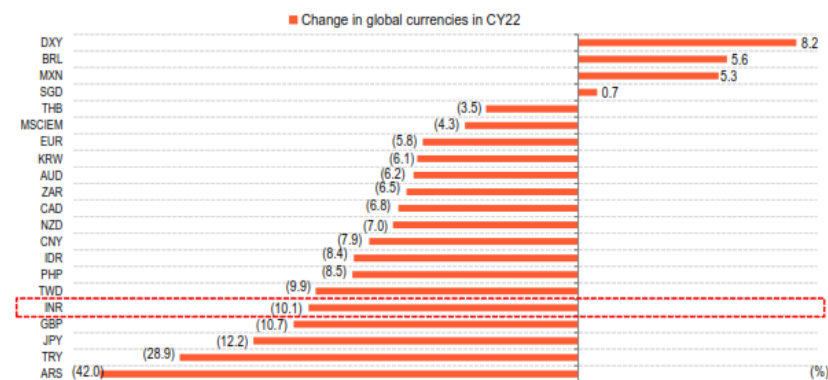
In 2022, INR depreciated by 10.1% led by a rally in dollar. DXY index gained by 8.2%. This in turn was due to Fed's aggressive monetary policy tightening. In 2022, Fed raised policy rates by a cumulative 425bps. While other global central banks also raised rates, they lagged the Fed and hence saw their currencies lose value against the dollar. India too did not remain immune. Further complicating the narrative was India's weakening domestic fundamentals such as high inflation, surging trade and CAD deficits as well as softening foreign inflows. However, we remain optimistic that the worst may be over for the INR and it may appreciate to 80-83/\$ in 2023. In saying so, risks do remain as a sharper than anticipated global slowdown may spur a fresh rally in the dollar.

Aditi Gupta
Economist

Global currencies in 2022

Bettered by a resurgent dollar, global currencies ended 2022 sharply lower. Almost all major currencies were under pressure for most part of the year as dollar continued to surge higher. However, with the dollar losing some of its sheen in the fag-end of the year, global currencies did find some breathing space. Amongst advanced economies, JPY was the worst performer, losing about 12.2% of its value over the course of the year. Growing divergence between Bank of Japan (BoJ), and its counterparts in US and Europe, was the prime reason behind this trend. However, the BoJ's decision to widen its ceiling for benchmark 10Y yield, led to expectations that the bank may relent further from its dovish stance. As a result, JPY rose by ~5% in Dec'22.

Figure 1: Global currencies were mostly lower in 2022



Source: Bloomberg, Bank of Baroda Research, Data as of 30 Dec 2022 | Note: Figures in bracket denote depreciation against USD

GBP too depreciated by more than 10% against the dollar, led by growth concerns amidst a worsening cost-of-living crisis which was in turn brought about by record-high inflation. CNY depreciated by 7.9% as the economic outlook remained marred by an ongoing property crisis as well as surging Covid-19 infections. This also put pressure on commodity currencies such as AUD and NZD. EUR ended the year on a relatively stronger footing, depreciating by only 5.8%. It must be noted that it slipped below the dollar-parity level during the year, due in part to the energy crisis from the fallout of the Russia-Ukraine conflict.



BONDS WRAP

02 January 2023

Fortnightly review

In Dec'22, bond yields globally changed direction and went for an upswing as Federal Reserve now expects a higher terminal rate at 5.1%. Even ECB officials hinted at peak inflation might not be way past us. These moves impacted yield trajectory. On domestic front, RBI's policy remained in line with market expectation, thus 10Y yield did not exhibit much volatility. However, with ending of calendar year and a review of the yield situation compared to previous year, brings some interesting conclusion.

Dipanwita Mazumdar
Economist

In CY22, sovereign 10Y yield globally as well as in India noticed considerable upward movement. Tightening policy environment amidst inflation, resulted in the same. For India, what has been a stark contrast compared to CY21 is that there has been a significant flattening of the yield curve, with rise in yield of short term papers. The short term papers were indeed more responsive to policy rate change by RBI. The gap between short and long end paper fell to 74bps in Dec'22 compared to 298bps in Dec'21.

The liquidity dynamics also changed considerably. On an average, liquidity surplus fell to Rs 3.1lakh crore in CY22 compared to Rs 6.3lakh crore in CY21. Even the drivers of liquidity noticed a shift. With rising credit deposit gap, forex depletion and constrained space for OMO (on account of rising rate cycle), liquidity surplus in the system went down. Going forward, we expect slight deficit in liquidity is going to be the new normal. The outlook for yields remain heavily contingent on the upcoming borrowing calendar of FY24. No additional borrowing in Q4 has comforted domestic yield in Dec'22. We expect fiscal deficit ratio to come down slightly to 5.5-6 % in FY24. This would support the yield. Our outlook for the next 30days is at 7.3-7.4%.

Global yields started inching up in Dec'22:

- Sovereign 10Y yields again reversed its direction in Dec'22. In comparison to Nov'22, where global yields broadly fell following the 44bps drop in US 10Y yields, the situation was quite the opposite in Dec'22. 10Y yields of major economies have risen with Germany, UK and US rising as much as 64bps, 51bps and 27bps respectively.
- So what has been the reason behind this upswing? 1) Major central banks such as US Fed, ECB and BoE went for an expected 50bps rate hike, yet yields firmed up. This was driven by US FOMC's upward revision in its terminal federal fund rate forecast. It now projects terminal rate to reach 5.1% against its earlier forecast of 4.6%. Current US OIS 1Y rate is at 4.9%. 2) ECB President also hinted that inflation peak may not be way past us on account of wage growth spiral due to government stimulus. Notably, recently, Head of Dutch Central Bank Klaas Knot remained thoroughly hawkish and hinted at "quite a decent pace of tightening".



Healthy quarter likely for NBFCs and life insurers

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- **SBI Card's spends expected to grow 18% YoY with a 43% rise in PAT on higher income and lower credit costs**
- **SBI Life remains our top life insurance pick given its cost efficiency and high margins**

Mohit Mangal

research@bobcaps.in

Wealth management: We expect IIFL Wealth to post 9% YoY AUM growth in Q3FY23 boosted by fresh fund flows and mark-to-market gains despite high volatility in equity markets. Recurring AUM is forecast to constitute 59% of the mix (53% in the year-ago quarter). Revenue could be flattish as an estimated 12% YoY increase in recurring revenue is likely to be offset by a decline in transactional revenue and other income.

We expect the company to have a cost-to-income ratio of 45% and deliver PAT growth of 12% YoY. Key monitorables include AUM growth and commentary on recurring business, especially IIFL One, as well as management's insights into new market forays planned for FY24.

Credit cards: Sectoral credit card spends continued to gain traction in October and November, crossing the Rs 1tn mark in each of these months. SBI Card saw market share gains in November, and we estimate 18% YoY growth in its spends for Q3, which will be reflected in income from fees and services.

The company continues to maintain ~19% market share in credit cards outstanding at the end of November. Net receivables is forecast to grow 35% YoY. We believe NIM would take time to return to pre-Covid levels. Provisions are expected to be lower and we place credit cost at 5.7%, down 370bps YoY and 70bps QoQ, which should boost PAT. Data on revolvers and credit cost would be key to watch.

Insurance: We maintain our positive stance on the life insurance industry and believe that the ongoing focus on profitable products would aid sustained margin gains for our coverage stocks (SBI Life, HDFC Life, IPRU) in Q3FY23. Our gross premium growth projections for covered companies ranges from 5-21% YoY in Q3FY23.

Cost ratios for HDFC Life and IPRU are likely to decline sequentially. Solvency ratios should hold in line with regulatory requirements. Market leader **SBI Life** (BUY, TP Rs 1,512) remains our top pick.

Recommendation snapshot

Ticker	Price	Target	Rating
HDFCLIFE IN	566	691	BUY
IIFLWAM IN	1,777	2,206	BUY
IPRU IN	451	645	BUY
SBICARD IN	796	1,139	BUY
SBILIFE IN	1,231	1,512	BUY

Price & Target in Rupees | Price as of 30 Dec 2022



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Recommendation scale: Recommendations and Absolute returns (%) over 12 months

BUY – Expected return >+15%

HOLD – Expected return from -6% to +15%

SELL – Expected return <-6%

Note: Recommendation structure changed with effect from 21 June 2021

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