MCB India Sovereign Bond ETF Report card for Quarter ending March 31, 2020

MCB India Sovereign Bond ETF Returns (USD)				
Security	**3 Months**	**6 Months**	**1 Year**	**Inception[1](Annualized Return)**
MCB India Sovereign Bond ETF	**-1.57%**	**-4.38%**	**-1.78%**	**-6.20%**

India Economic Outlook

The economic impact of the 2019–20 coronavirus pandemic in India has been hugely disruptive. Stock markets in India posted their worst loses in history on 23 March 2020. However, on 25 March, one day after a complete 21 day lockdown was announced by the Prime Minister, SENSEX and NIFTY posted their biggest gains in 11 years, adding a value of ₹4.7 lakh crore (US$66 billion) crore to investor wealth.

Disruption caused by ongoing coronavirus crisis and consequent expected slowdown in economic situation has resulted in huge FPI selling and redemptions in mutual funds leading to spike in bond yields. Across the globe, central bankers are reacting to this pandemic with massive rate cuts and liquidity injection to stabilize financial conditions.

RBI has also taken several measures including rate cut by 75 bps, CRR cut by 100 bps, rise in MSF, TLTRO, LTRO, Dollar sell/buy swaps and OMO purchase of government bonds which will help retaining some stability and optimism in debt markets and will help in easing any resultant financial dislocations as well as keep the funding channels working. RBI liquidity measures will inject liquidity of INR 3.74 lakh crore to the system. The liquidity measures are positive for the bond markets. We expect more actions from RBI incoming times including further rate cuts. In the present disruptive environment when the whole country and a large part of the world is under lockdown, relevance of fiscal deficit or inflation or such economic indicators is lost. It's a given that government will need massive fiscal measures which may not end up in range of normal fiscal deficit and inflation movements and therefore will need to be ignored for the time being. Savings from fall in oil prices will help in giving fiscal stimulus.

India Gross Domestic Product (GDP)

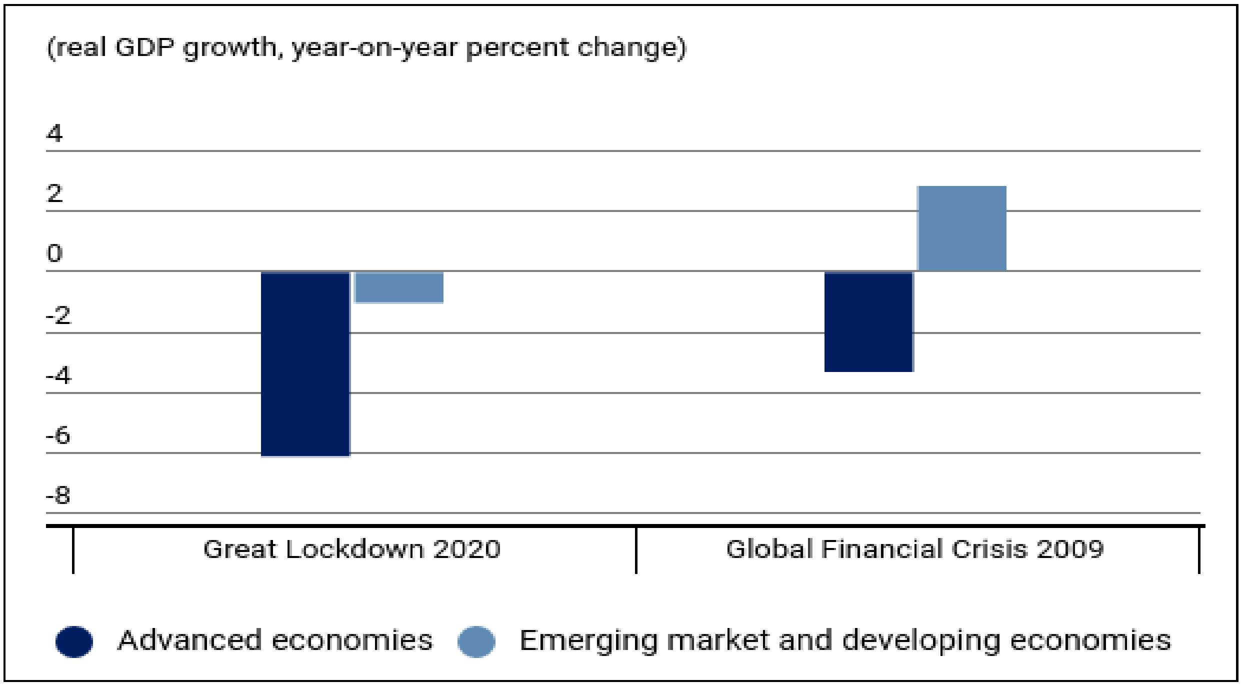
The International Monetary Fund (IMF) on Tuesday slashed its FY21 growth projection for India to 1.9% from 5.8% projected in January. The coronavirus pandemic came at a time when India's economy was already slowing, due to persistent financial sector weaknesses. The severe disruption of economic activities caused by covid-19, both through demand and supply shocks, has overtaken the incipient recovery in the Indian economy leading to massive job losses. IMF even expects FY20 growth at 4.2% as against 5% estimated by India's statistics department.

Under the assumption that the pandemic and required containment peaks in the second quarter for most countries in the world, and recedes in the second half of this year, *World Economic*

[1] Inception Date: June 06, 2016

Outlook projected global growth in 2020 to fall to -3 percent. This makes the Great Lockdown the worst recession since the Great Depression, and far worse than the Global Financial Crisis.
For the first time since the Great Depression both advanced economies and emerging market and developing economies are in recession. For this year, growth in advanced economies is projected at -6.1 percent. Emerging market and developing economies with normal growth levels well above advanced economies are also projected to have negative growth rates of -1.0 percent in 2020, and -2.2 percent. Income per capita is projected to shrink for over 170 countries. Both advanced economies and emerging market and developing economies are expected to partially recover in 2021

Comparison of Recession due to pandemic with Global Financial Crisis



Source: IMF, World Economic Outlook

There are some hopeful signs that this health crisis will end. Countries are succeeding in containing the virus using social-distancing practices, testing, and contact tracing, at least for now, and treatments and vaccines may develop sooner than expected.

As per the data below from IMF India will perform better in terms of GDP from rest of the world in the year 2020 at 1.9% and 7.4% in the year 2021 excluding China in the year 2021 wherein China's GDP growth is projected at 9.2%.

The COVID-19 pandemic will severely impact growth across all regions.

(real GDP, annual percent change)	2019	PROJECTIONS 2020	2021
World Output	**2.9**	**-3.0**	**5.8**
Advanced Economies	**1.7**	**-6.1**	**4.5**
United States	2.3	-5.9	4.7
Euro Area	1.2	-7.5	4.7
Germany	0.6	-7.0	5.2
France	1.3	-7.2	4.5
Italy	0.3	-9.1	4.8
Spain	2.0	-8.0	4.3
Japan	0.7	-5.2	3.0
United Kingdom	1.4	-6.5	4.0
Canada	1.6	-6.2	4.2
Other Advanced Economies	1.7	-4.6	4.5
Emerging Markets and Developing Economies	**3.7**	**-1.0**	**6.6**
Emerging and Developing Asia	5.5	1.0	8.5
China	6.1	1.2	9.2
India	4.2	1.9	7.4
ASEAN-5	4.8	-0.6	7.8
Emerging and Developing Europe	2.1	-5.2	4.2
Russia	1.3	-5.5	3.5
Latin America and the Caribbean	0.1	-5.2	3.4
Brazil	1.1	-5.3	2.9
Mexico	-0.1	-6.6	3.0
Middle East and Central Asia	1.2	-2.8	4.0
Saudi Arabia	0.3	-2.3	2.9
Sub-Saharan Africa	3.1	-1.6	4.1
Nigeria	2.2	-3.4	2.4
South Africa	0.2	-5.8	4.0
Low-Income Developing Countries	5.1	0.4	5.6

Source: IMF, World Economic Outlook

RBI Monetary Policy Highlights – March 2020

- Amidst unfolding effects of the pandemic and the urgent need to support the frail economic conditions, RBI conducted the seventh bi-monthly monetary policy prior to the scheduled meeting of April 3, 2020, advancing it by a week.

- In view of the current and evolving macroeconomic situation, MPC voted to reduce the policy repo rate by 75 bps.

- RBI also decided to widen the LAF corridor from 50 bps to 65 bps in view of persistent excess liquidity. Therefore, key policy rates stand as follows: Repo Rate at 4.40%, Reverse Repo Rate at 4.0% and Marginal Standing Facility Rate at 4.65%.

- All the members of the committee decided to maintain the accommodative stance as long as it is necessary for the revival of the growth and to diminish the impact of COVID-19 while ensuring that inflation remains within the target.

- RBI aims at injecting a massive liquidity of Rs 3.74 Lakh Cr through three major development and regulatory policies including TLTROs, CRR and MSF.

- Announced Targeted Long-Term Repo Operations (TLTROs) up to three years of maturity for a total amount up to Rs 1 Lakh Cr at floating rate linked to policy repo rate.

- Cash Reserve Ratio reduced to 3% of NDTL down from 4% of NDTL. The reduced rate would be applicable for one year.

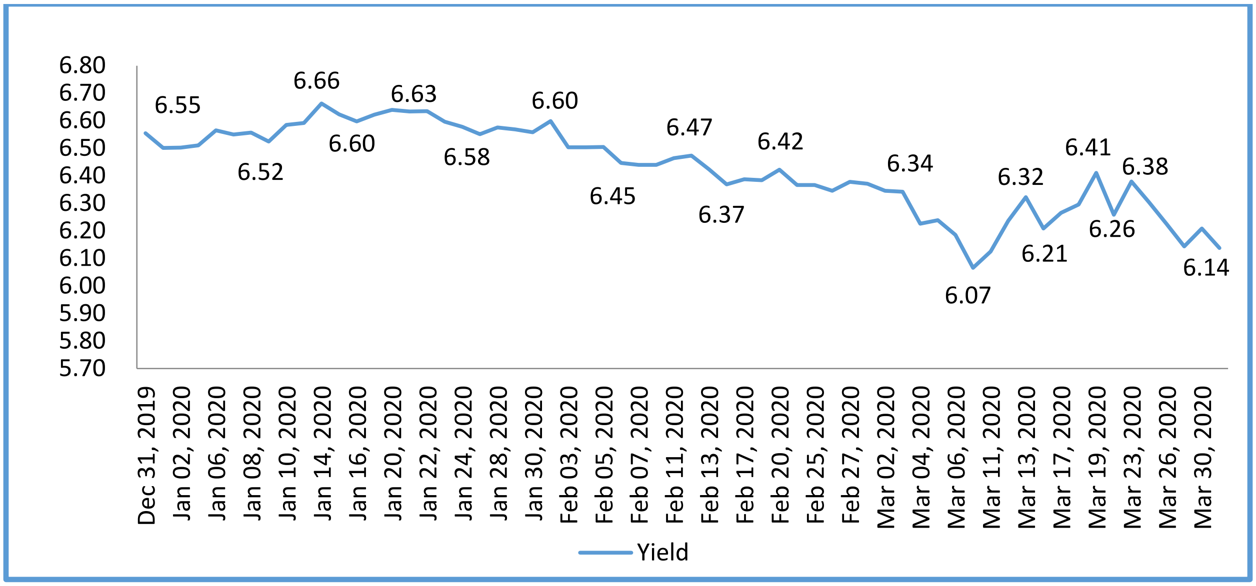
- Percentage of SLR that can be used under overnight borrowing in Marginal Standing Facility increased from 2% to 3%.

- Moratorium on instalments on all term loans outstanding as on March 01, 2020 for a period of three months. Further, interest on working capital facilities in the form of cash credit/overdraft to be deferred for a period of three months.

Indian Debt Market Review

The union budget has paved way for inclusion of its sovereign bonds in Global Emerging Markets bond indices. This will be a huge positive for long bonds. Liquidity is in huge surplus but market is yet to price this. LTRO will bring downcast of funds for the banks and the chase of assets will lead to transmission which is RBI’s aim. RBI announced LTRO worth INR 1 Lakh crore, a much potent tool than rate cut. RBI also announced OMO worth INR 300 billion.

India 10-Year G-Sec Yield Movement



Source: Investing.com

The falling commodity prices and bond rally globally will help Indian rates lower. This may reduce trade deficit. However due to equity sell off INR will remain under pressure against USD which is manageable as RBI has enough reserves to fight the same. Slump in US Treasury yields may prompt foreign portfolio investors (FPI) to step up their purchase of Indian dated securities.

Indian Indicators	31-March-19	31-December-19
10 Year Benchmark	6.14%	6.55%
USD / INR	75.55	71.32
FPI DEBT (INR Cr.)	-60,376	-4,616
Current Account Deficit	-0.2% (December 2019)	-2.0%(September 2019)
CPI Inflation	5.90%	7.35%
IIP	4.50%	2.10% (Revised)
Forex Reserves (USD Million)	475,561	457,468
Gross Domestic Product (GDP) (Annual YoY %)	4.70%	4.50%

Source: RBI, NSDL, Trading Economics, investing.com

Consumer price inflation rose to 7.59% in January but eased at 6.58% in February and 5.91% in March. The decline in CPI was driven by decline in food inflation. The inflation in food basket slipped to 8.76% in March 2020. This is the first time since November last year that retail inflation based on Consumer Price Index (CPI) has fallen below the Reserve Bank of India Monetary Policy Committee's targeted upper band of 6%.

RBI has opened a new window “Fully Accessible Route” wherein specified government securities shall be eligible for investments by foreign investors. This will ease foreign investors to the Indian Bond Market and facilitate inclusion in global bond indices. Indian central bank has also increased FPI limits for corporate bonds to 15% from 9% for 2020-21. These moves by the central bank will have huge scope of incremental flows by FPI’s. This will have a downward pressure on interest rates.

Economist expects the central bank to announce another rate cut of 50 bps due to an unexpected plunge in economic activity. RBI policy measures were a reasonably strong boost in terms of action across market.

Positives for India

- Lower Oil Prices
- Lower trade deficit with China
- RBI rate cut – credit floe to economy will begin
- Government fiscal stimulus
- Lower Global Interest Rates & Higher Liquidity can bring more capital allocation to India.
- Supply chain disruption companies coming from China to India.
- Potential higher FPI capital allocation post medical solutions emerge for COVID-19.