

DEBT MARKETS

GLOBAL

China cut interest rates for the first time in six years and allowed most banks to set aside smaller reserves as worsening credit-market turmoil and weakening export demand dim the outlook for economic growth. The People's Bank of China reduced the one-year lending rate to 7.20 percent from 7.47 percent, and lowered the reserve ratio at the nation's smaller banks by 1 percentage point.

The Fed kept the benchmark rate at 2 percent, citing risks to growth and inflation. Fed agreed to an \$85 billion loan for AIG, the insurer hit by billions of dollars of write downs on investments in securities tied to mortgages. The government will get a 79.9 percent equity interest in the company as a result. The Federal Reserve almost quadrupled the amount of dollars central banks can auction around the world to \$247 billion in a co-ordinated bid to ease the worst crisis facing financial markets since the 1920s. The Fed increased the amount of dollars that the European Central Bank, the Bank of Japan and other counterparts can offer from \$67 billion "to address the continued elevated pressures in U.S. dollar short-term funding markets". The Bank of England, the Bank of Canada and the Swiss National Bank also participated.

The Bank of Japan kept interest rates unchanged after pumping more than 5 trillion yen (\$47 billion) into money markets in the wake of Lehman Brothers Holdings Inc.'s collapse. The Bank of Japan pumped 3 trillion yen into the banking system on September 18, 2008 after the overnight call rate surged to 0.65 percent, higher than the bank's 0.5 percent target and a day before 2.5 trillion yen injection was the biggest since March 31.

- RBI Announces Market Measures to inject liquidity in the banking system. According to RBI "The recent extraordinary global developments triggered by the bankruptcy/sell-out/restructuring of

some of the world's largest financial institutions have resulted in severe disruptions of international money markets, sharp declines in stock markets across the globe and extreme investor aversion. Several central banks and financial regulators have responded with both unusual and unconventional measures to facilitate the orderly operation of financial markets and to ensure financial stability".

In order to alleviate these transient pressures which are related largely to external developments, RBI has decided to take the following measures:

- Reserve Bank will continue to sell foreign exchange (US dollar).
- Increase the interest rate ceiling on FCNR(B) deposits by 50 basis points, i.e. to Libor/Euribor/Swap rates minus 25 basis points.
- Increase in the interest rate ceiling on NR(E)RA deposits by 50 basis points, i.e. to Libor/Euribor/Swap rates plus 50 basis points.
- RBI has allowed scheduled banks to avail additional liquidity support under the LAF to the extent of up to 1% of their NDTL and seek waiver of penal interest.
- To conduct Second LAF on a daily basis.

RBI further states that "It may be recalled that, on earlier occasions of market stress also, the Reserve Bank had given market participants assurances of domestic as well as foreign currency liquidity to financial markets and had announced certain measures, which were ad hoc and temporary in nature".

CBLO

The CBLO rates moved up higher tracking huge liquidity crunch in the banking system due to advance tax outflow and global turmoil. CBLO rates ranged between 9.00%-14.50%. Liquidity situation in the system is expected to remain tight and overnight rates will remain at elevated levels.

Government Securities and Treasury Bills

WPI inflation for the week ended 6th September, 2008 came at 12.14% (YoY) which was slightly higher than market expectation of 12.03%.

In the twin auction of Treasury Bills on Wednesday the 182 day and 91 day T bill cut off came in line with market expectation. For the 182 day T-Bill cut off was at 8.77% as compared to the previous fortnight cut off of 9.07% while the 91 day T-Bill had a cut off of 8.65% which was lower than the previous week cut off of 8.73%.

10-year benchmark yields moved higher tracking the liquidity tightness and RBI measure to waived the SLR requirement to the extent of 1% and allow banks to borrow the same through LAF Repo. Yields rise was

also contributed by the rise in crude prices from \$ 91/bbl to \$104/bbl.

Further, RBI has announced 91 day T-Bill auction of Rs 1,000 crores and 364 day T-Bill auction of Rs 500 crores to be held on 24th September, 2008. Further, RBI announced the State Government security auction of four States/Union Territory of Rs 1,712 crores to be held on 25th September, 2008.

Corporate Bonds

The credit spreads Corporate Bonds remained moved higher by 40-50 bps across the curve in wake of tighter liquidity situation and comparatively lower level of investment confidence by investors of corporate bond.

SPREADS OF CORPORATE BONDS AS ON 15TH AUGUST 2008 OVER G-SECS

Tenure	Rating		
	AAA	AA +	AA
1 year	283.50	304.50	329.50
3 year	232.90	250.90	279.90
5 year	256.40	285.40	309.40
10 year	236.20	279.20	310.20

Rupee

After the measures taken by RBI to support the weakness of rupee against dollar, rupee appreciated considerably. USD/INR after reaching \$46.99 declined to as low as \$45.88 before closing at \$46.32 last week. Rupee appreciated against USD & GBP and depreciated marginally against EURO & YEN.

FUND MANAGER COMMENTS

The present liquidity tightness in all markets has created unprecedented risk aversion in the minds of the investors. While the corporate yields are moving higher the Government Securities yield has been moving in the other

direction. All the major Central Banks are providing liquidity to improve the market conditions. As has been pointed earlier RBI has also started providing liquidity support in the domestic market through a host of measures.

It is expected that due to overall uncertainty the yields would still remain under pressure at least for some more time. The pay commission payment is expected to be made in the current month which should reduce the liquidity pressures to some extent. However a higher borrowing in the second half of the financial year could lead to increase in yields. The Government Securities yield could range between 8.40-8.60% for the week.

EQUITY MARKETS

The week ended September 20, 2008 will be remembered in the history of the world capital market for its bitter reasons. The week has witnessed a very strange behaviour not only in India but global markets as well, which is very erratic. Number of large investment banks in U.S and U.K has tumbled down one after another which has its own ripple effects on the world economy. The week has also witnessed a steep fall in the crude price which came down below \$100 / barrel. Gold also declined and so the rupee has also depreciated and crossed a level of 46 / dollar during the week.

Though the U.S Government tried to salvage the position, the wounds are so deep that it would take long time to recover. The economic crisis is so severe that the Central Banks of many countries including RBI had to intervene and pump in more than \$300 bn to cool off the turmoil. Though desired cooling effect is being felt not only in the Indian market but the world markets also had recovered on the last trading day of week, however, more pains from the global front cannot be ruled out in the near future.

The Indian markets are quite sensitive and dominated by the FIIs' inflow/outflow, which is quite volatile and due to global liquidity crunch, the FIIs' flows to Indian market is continuously shrinking. Now second quarter results would be out from the second week of October and the Advance tax collection figures are indicating that results may not be as good as in the previous year. The market may start discounting these numbers from the coming week only and accordingly, stock specific actions based on expected financial results would be there in the market.

The market is unlikely to be cheered in the near future and is expected to be in the range of 12500 -14500. This range can be encashed for making investment / disinvestment in the market.

