

**WEEKLY WRAP**

10 December 2018

**State poll results to drive markets**

Disappointing macro data from both US and China fuelled concerns over global economic outlook leading to a decline in global yields. US markets fell on uncertainty over future pace of rate hikes and lower than expected job additions. Indian yields fell by 14bps as RBI indicated its willingness to change its stance to neutral if inflation remains subdued. INR depreciated by 1.8% as oil prices rose, especially in the last trading day as OPEC announced a production cut. Equity markets also ended lower. With key state elections results due this week, markets are likely to be volatile.

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**Markets**

- **Bonds:** Global yields closed lower driven by fall in US 10Y yields by 14bps (2.85%) on the back of softer economic data (decline in factory orders, slower pace of hiring). Crude prices jumped up by 5% driven by OPEC's and non-OPEC members' decision of production cut (1.2mbpd). Indian 10Y yields plunged by 14bps (7.46%) as RBI revised inflation projections downward for H2FY19. System liquidity was in deficit of Rs 583bn as on 7 Dec 2018 compared to Rs 714bn in the previous week.
- **Currency:** Weaker economic data from the US, along with declining US10Y yield led to DXY declining by 0.8% in the week. While a temporary trade truce between US & China helped Yuan and Japanese yen (ending the week higher by 1.2% and 0.8% respectively), INR (down 1.8% in the week) was impacted by rising Brent (+5%).
- **Equity:** Barring Shanghai Comp, global indices closed lower on the back of worries over global growth outlook and worries over whether US and China will be able to negotiate a deal in 90 days. Slowdown in global growth may drive a dovish stance by Fed in the upcoming meet which may give a boost to equity markets. Sensex too ended lower as investors remained cautious ahead of state poll results.
- **Upcoming key events:** Investors will closely watch China's industrial production and US CPI data. ECB's policy is also likely to drive the markets this week. Further, focus will also be on the upcoming Brexit vote. On the domestic front, state election results will drive markets this week. Apart from this India's retail & wholesale inflation print, trade and industrial production data also awaited.



## India macro developments

- India's manufacturing PMI rose to 54 in Nov'18, an 11-month high from 53.1 in Oct'18. This was attributed to robust demand conditions resulting from stronger inflow of new orders and jump in sales. On the price front, cost inflation moderated due to weaker supply chain pressures. Job creation on the other hand, continued to improve sharply as it rose at its fastest pace in over six years.
- According to news reports, Power Finance Corporation is expected to buy government's stake in Rural Electrification Corporation (58%) for almost Rs 140bn. This will be a part of government's Rs 800bn disinvestment program for FY19, of which Rs 192bn has been collected till Oct'18. The deal between the 2 NBFCs will require RBI's approval. Apart from this, a similar deal is being planned for NTPC and Satluj Jal Vidyut Nigam.
- RBI held rates and its calibrated tightening stance unchanged in its latest policy meet. However, inflation forecast was revised downward to 3% in H2FY19 from 4.2% and 4% in H1FY20 (earlier Q1 at 4.8%) on the back of muted food inflation and significant decline in oil prices. Notably, RBI indicated its willingness to take appropriate policy action if inflation prints remain subdued.
- India's services activity rebounded sharply as PMI rose to a 4-month high of 53.7 in Nov'18 vs 52.2 in Oct'18. Composite PMI also jumped to 54.5 in Nov'18, supported by higher inflows of new orders, strengthening business sentiment and accelerated pace of job creation. Input price pressure moderated and stronger demand conditions enabled manufacturers to improve their margins.
- Indian government has approved Agriculture Export Policy, 2018 to double farm exports to US\$ 60bn by 2022 from US\$ 30bn last year. It has also been proposed to keep outbound shipment of processed and organic items free of any restriction. Agriculture & allied products exports is at US\$ 18bn in FYTD19 vs US\$ 33bn in FY18.
- India's CAD jumped to US\$ 19.1bn in Q2FY19 (2.9% of GDP) from US\$ 15.8bn in Q1FY19 (2.4% of GDP), led by higher trade deficit at US\$ 50bn in Q2 vs US\$ 46bn in Q1. Inflows on account of remittances and services exports accelerated in Q2. FII outflows and muted FDI inflows drove US\$ 13.2bn decline in FX reserves in H1FY19. We estimate CAD to moderate to 2.5% of GDP in FY19 from 2.7% in H1FY19 on the back of lower oil prices.
- RBI reported that currency in circulation (CIC) declined by Rs 149bn (on a weekly basis) and stood at Rs 20tn as on 30 Nov 2018. Overall reserve money grew by 17% on a YoY basis compared to 10% a year ago. On FYTD basis, reserve money is growing at a slower pace of 5.7% against 15% in the previous year.

## Global macro developments

- Manufacturing activity in US continued to expand at a robust pace as reflected in the ISM PMI data (59.3% in Nov'18 vs 57.7% in Oct'18). In Eurozone, the pace of expansion of manufacturing activity was at its weakest since Aug'16 (51.8 in Nov'18 vs 52 in Oct'18) driven by faltering demand conditions and deterioration in new orders. In Japan as well, manufacturing PMI dropped to more than 1-year low in Nov'18.
- South Korea's real GDP rose by 0.6% on a seasonally adjusted QoQ basis in Q3CY18, unchanged from Q2CY18. While private consumption rose at a slower pace (0.5% vs 0.3% in Q2), GFCF acted as a drag on the overall growth (-4.6% vs 2.9% in Q2). Government consumption on the other hand helped keep the economy afloat (1.5% vs 0.3% in Q2).
- Services activity in Europe slowed down in Nov'18 (53.4 vs 53.7 in Oct'18), led by easing pace of growth in Germany. On the other hand, services activity in Japan continues to hold ground (Services PMI 52.3 vs 52.4 in Oct'18). While output and new orders are under strain in the Eurozone, Japan has seen steady rise in both. Input price pressures remain elevated across countries.
- US factory orders fell by (-) 2.1% on a MoM basis in Oct'18 vs 0.2% in Sep'18, the largest drop since Jul'17. This was led by decline in orders for transport equipment (-12% vs 0.9% in Sep'18). Separately, jobless claims as of week ending 1 Dec 2018 fell less than estimated to 231,000. The 4-week moving average rose to 228,000-highest since mid Apr'18. In addition, US trade deficit rose to a 10-year high at US\$ 55.5bn in Oct'18 vs US\$ 54.6bn in Sep'18.
- Factory orders in Germany rose for the third straight month by 0.3% in Oct'18 from 0.1% in Sep'18 (est., -0.4%). The rise was led by foreign orders which rose by 2.9%, even as domestic orders declined by 3.2%. Further, apart from consumer goods which fell by 1.7%, new orders in intermediate goods and capital goods increased by 0.8% and 0.4% respectively.
- Data released by Labour Department showed that the pace of hiring in US slowed down moderately. Total nonfarm employment increased by 155,000 in Nov'18 against expectation of 199,000. Unemployment rate however remained stable at 3.7% for 3rd month in a row. Average hourly earnings on a YoY basis grew by 3.1% in Nov'18 vs 2.3% in Nov'17.
- China's trade data for Nov'18 fell short of expectation as its exports rose by 5.4% vs est.: 10% and 15.6% in Oct'18. Export growth to US, Europe and S. Korea slowed significantly, indicating that front-loading of exports is now losing momentum. Depreciating Yuan also led to weaker import demand, as imports rose by only 3% in Nov'18 vs est.: 14.5% and 21.4% in Oct'18.

FIG 1 – MOVEMENT IN KEY GLOBAL ASSET CLASSES

Particulars	Current	1W	1M	3M	12M
<b>10Y yields (Δ bps)</b>					
US	2.85	(14)	(39)	(9)	48
UK	1.27	(10)	(27)	(19)	1
Japan	0.06	(3)	(6)	(5)	0
Germany	0.25	(6)	(20)	(14)	(4)
India	7.46	(14)	(34)	(57)	41
China	3.31	(7)	(19)	(33)	(59)
<b>2Y yields (Δ bps)</b>					
US	2.71	(8)	(25)	1	91
UK	0.74	(4)	(8)	(3)	23
Japan	(0.14)	(1)	(1)	(4)	0
Germany	(0.60)	0	(1)	(5)	16
India	7.12	(11)	(41)	(74)	76
China	2.50	(5)	(39)	(35)	(126)
<b>Currencies (Δ %)</b>					
EUR	1.1379	0.5	(0.4)	(1.5)	(3.3)
GBP	1.2726	(0.2)	(3.0)	(1.5)	(5.6)
JPY	112.69	0.8	0.7	(1.5)	0.4
AUD	0.7208	(1.3)	(0.9)	1.4	(4.0)
INR	70.81	(1.8)	3.2	1.3	(9.7)
CNY	6.8743	1.2	0.7	(0.4)	(3.9)
<b>Equity &amp; Other indices (Δ %)</b>					
Dow	24,389	(4.5)	(6.8)	(5.9)	0.7
FTSE	6,778	(2.9)	(4.8)	(6.9)	(7.4)
DAX	10,788	(4.2)	(6.8)	(9.8)	(17.3)
NIKKEI	21,679	(3.0)	(1.8)	(2.8)	(3.6)
Shanghai Comp	2,606	0.7	(1.3)	(3.6)	(20.4)
SENSEX	35,673	(1.4)	1.2	(7.1)	8.3
Brent (US\$/bbl)	61.67	5.0	(14.4)	(19.7)	(0.9)
Gold (US\$/oz)	1,249	2.4	1.9	4.4	0.2
CRB Index	417.7	0.4	0.1	1.4	(2.2)
Rogers Agri Index	783.8	1.3	0.2	1	(2.0)
LIBOR (3M)*	2.77	3	17	44	124
INR 5Y Swap*	7.35	(18)	(44)	(20)	81
<b>India FII data (US\$ mn)</b>					
	<b>6 Dec</b>	<b>WTD</b>	<b>MTD</b>	<b>CYTD</b>	<b>FYTD</b>
FII-Debt	363.0	364.1	364.1	(7,208.0)	(7,454.0)
FII-Equity	(7.5)	(31.7)	(31.7)	(4,921.5)	(7,046.9)

Source: Bloomberg, Bank of Baroda Research | \*Indicates change in level

FIG 2 – DATA RELEASE CALENDAR

Date	Event	Period	Estimate	Previous	Actual
10-Dec	Japan GDP SA, % QoQ	Q3CY18	(0.5%)	(0.3%)	--
	Japan Current Account Balance, ¥ bn	Oct	1,410	1,822	--
	India CAD, US\$ bn	Q2FY19	(19.9)	(15.8)	--
	Germany trade balance, € bn	Oct	--	18.4	--
	Italy industrial production, % MoM	Oct	--	(0.2%)	--
	UK trade balance, £ mn	Oct	(1,100)	(27)	--
	UK industrial production, % MoM	Oct	0.2%	0.0%	--
11-Dec	Japan machine tool orders, % YoY	Nov	--	(0.7%)	--
	Germany ZEW survey current situation	Dec	55.6	58.2	--
	US PPI final demand, % MoM	Nov	0.0%	0.6%	--
12-Dec	Japan PPI, % YoY	Nov	2.4%	2.9%	--
	Japan core machine orders, % MoM	Oct	10.1%	(18.3%)	--
	Euro Area industrial production SA, % MoM	Oct	0.5%	(0.3%)	--
	India CPI, % YoY	Nov	--	3.3%	--
	India industrial production, % YoY	Oct	--	4.5%	--
	US CPI, % MoM	Nov	0.0%	0.3%	--
13-Dec	US monthly budget statement, US\$ bn	Nov	--	(100.5)	--
	Germany CPI, % YoY	Nov	2.3%	2.3%	--
	France CPI, % YoY	Nov	--	1.9%	--
	ECB policy meet	13-Dec	0.0%	0.0%	--
	US initial jobless claims	8-Dec	--	231,000	--
14-Dec	Japan manufacturing PMI	Dec	--	52.2	--
	China retail sales, % YoY	Nov	8.80%	8.60%	--
	China industrial production, % YoY	Nov	5.90%	5.90%	--
	China fixed assets ex rural YTD, % YoY	Nov	5.90%	5.70%	--
	Japan industrial production, % MoM	Oct	--	2.90%	--
	India WPI, % YoY	Nov	--	5.28%	--
	Germany manufacturing PMI	Dec	52.0	51.8	--
	Eurozone manufacturing PMI	Dec	52.0	51.8	--
	Eurozone services PMI	Dec	53.5	53.4	--
	Germany services PMI	Dec	53.5	53.3	--
	India trade balance, US\$ bn	Nov	--	(17.1)	--
	US retail sales advance, % MoM	Nov	0.20%	0.80%	--
	US industrial production, % MoM	Nov	0.30%	0.10%	--
	US manufacturing PMI	Dec	--	55.3	--
US services PMI	Dec	--	54.7	--	

Source: Bloomberg, Bank of Baroda Research

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