

WEEKLY WRAP

01 July 2019

Budget to drive Indian yields

Weaker than anticipated US economic data led to further decline in global yields despite oil prices increasing by 2.1% in the week. Fed Chairman suggested Fed will be conservative in its approach to reducing rates. With President Trump indicating a temporary truce on trade war with China, yields are likely to inch up. In India's case trajectory of yields will depend upon Centre's borrowing programme which will be announced on Friday in the Budget. We expect government to maintain targets set out in Interim Budget.

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Markets

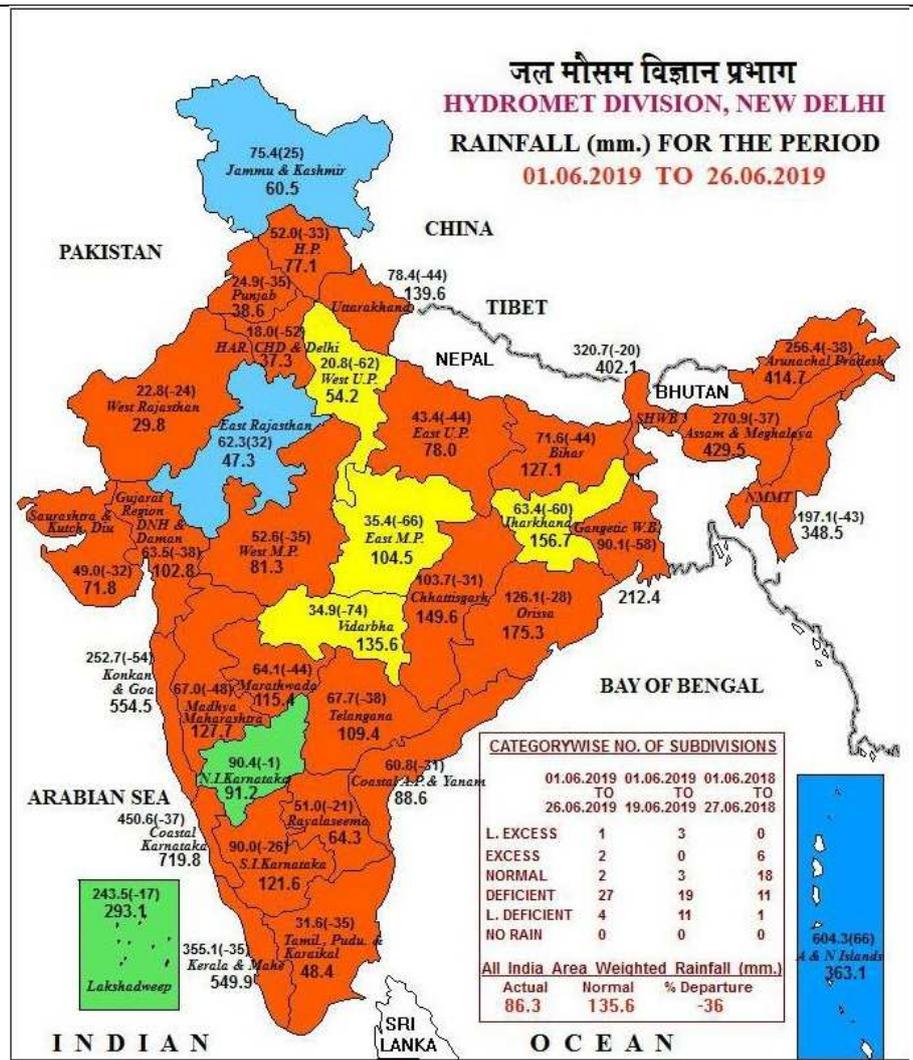
- **Bonds:** Global yields closed lower as US consumer confidence, new home sales, and durable goods orders were below estimate. Fed Chairman Powell expressed a conservative approach to rate cuts. Crude prices inched up by 2.1% in the week due to US-Iran tensions. The trajectory of oil prices will also depend upon OPEC's decision on output cuts later today. As a result, Indian 10Y yield rose by 2bps to 6.88%. System liquidity was in surplus of Rs 403bn as on 28 Jun 2019 vs Rs 165bn in the previous week.
- **Currency:** Global currencies closed mixed ahead of the meeting between US President Trump and his Chinese counterpart at the G-20 summit. DXY, CNY and EUR closed unchanged. GBP depreciated by (-) 0.3% in the week on Brexit uncertainty. INR appreciated by 0.8% in the week even as oil prices rose. FII inflows were also muted at US\$ 74mn.
- **Equity:** Barring Down and Shanghai Comp, global indices ended the week higher led by hopes of positive outcome from the US-China trade talks. However, weak macro prints from US & China dampened the mood. Shanghai Comp fell by (-) 0.8% followed by Dow (-0.4%). Tracking global cues, Sensex rose by 0.5% in the week.
- **Upcoming key events:** In the current week markets will closely watch global manufacturing and services PMIs. Apart from that US factory orders and non-farm payrolls will guide the market movement. On the domestic front, Economic Survey will be presented on 4 Jul and Union budget on 5 Jul.



Monsoon Tracker

- For the week ending 26 June 2019, monsoon rains were (-) 24% below normal. However, for the period 1 June 2019 to 26 June 2019, monsoon was (-) 36% below LPA compared with (-) 10% last year. While large parts of India continue to receive deficit rains, parts of Eastern Rajasthan and J&K have fared much better. Going ahead, the conditions for Southwest Monsoon are likely to become more favourable for Uttarakhand, Gujarat and Maharashtra during the first week of Jul'19.
- Led by patchy monsoon, overall Kharif sowing as on 28 Jun 2019 is down by (-) 10% this year. This in turn resulted in lower sowing area for both pulses (-) 61% and cotton (-) 16% respectively. Sowing for rice fell only marginally by (-) 0.1%. Major decline was also visible in coarse cereals (-11%) and jute (-7%).

FIG 1 – DISTRIBUTION PATTERN OF SOUTH-WEST MONSOON



LEGEND: ■ L. EXCESS (+60% OR MORE) ■ EXCESS (+20% TO +59%) ■ NORMAL (+19% TO -19%)
 ■ DEFICIENT (-20% TO -59%) ■ L. DEFICIENT (-60% TO -99%) ■ NO RAIN (-100%) ■ NO DATA

Source: IMD, Bank of Baroda Research

India macro developments

- According to news reports, Bimal Jalan committee on the transfer of excess reserves of RBI will not be released before the budget on Jul 5. The delay is reportedly on account of dissent by finance secretary Garg on the matter of methodology and timeline of transfer. This dims the chances of central government making up for Rs 1.1tn shortfall in tax revenue in FY19RE. In FY19, RBI has transferred Rs 680bn as dividend to the centre vs Rs 749bn in FY19BE. In FY20BE, government has estimated Rs 548bn as dividend.
- As per news reports, ministry of petroleum and natural gas has requested for additional Rs 330bn in the budget to meet FY19 subsidy dues, over Rs 248bn allocated in FY19RE. As of Mar'19, dues of IOCL were Rs 190bn (vs Rs 9bn in Mar'18), while dues of HPCL and BPCL were around Rs 80bn each. If the subsidy payment gets rolled over to FY20, then the amount sanctioned in FY20IB (Rs 375bn) will only be enough to cover the arrears.
- RBI reported that currency in circulation decreased by Rs 139bn (on a weekly basis) and stood at Rs 22tn as on 21 Jun 2019. Overall reserve money grew by only 11.1% on a YoY basis compared to 24.1% a year ago. On FYTD basis, reserve money grew at a slower pace of 0.2% vs 3.3% last year.
- RBI's FSR highlighted capital adequacy of SCBs has improved after PSB recap, and a turnaround in the NPA cycle has also been seen. Provision coverage ratio of SCBs has improved from 48.3% in Mar'18 to 60.6% in Mar'19, signalling banking sector's resilience. Baseline scenario also projects that GNPA ratio would come down from 9.3% in Mar'19 to 9% in Mar'20. Higher surveillance of large HFC/NBFCs has also been highlighted.
- India's forex reserves rose to a lifetime high at US\$ 426.4bn in the week ending 21 Jun 2019. On a weekly basis, forex reserves rose by US\$ 4.2bn compared with a decline of (-) US\$ 1.4bn last week. In CY19, forex reserves have increased by US\$ 33bn vs an decline of (-) US\$ 1.6bn last year, supported by RBI's dollar-rupee swap as well as strong FII inflows.
- India's CAD narrowed sharply to US\$ 4.6bn (0.7% of GDP) in Q4FY19 from US\$ 17.7bn (2.7% of GDP) in Q3FY19 led by lower trade deficit. Higher FPI and ECB inflows helped increase BoP surplus in Q4 to US\$ 14.2bn. For FY19 however, CAD rose to 2.1% of GDP from 1.8% in FY18 due to higher oil imports. With muted non-oil-non-gold imports and oil prices below US\$ 70/bbl, CAD is expected to remain steady at 2.1% of GDP in FY20.

Global macro developments

- Amidst concerns of slowing global economy, Germany's IFO business climate index dropped to a 5-year low of 97.4 in Jun'19 from 97.9 in May'19. Trade disputes and uncertainties over Brexit have hurt Germany's economic prospects. Bundesbank expects GDP to contract in Q2CY19 and has thus revised its growth forecast to 0.5% in CY19 from 1.5% in CY18.
- Euro Area inflation held steady at 1.2% in Jun'19 on a YoY basis, as increase in prices of food items and services was offset by a decline in energy prices. Core inflation excl. food and energy prices rose to 1.2% in Jun'19 from 1% in May'19. Despite this, inflation has remained lower than ECB's target of 2% suggesting that it might look at monetary easing to support growth and inflation.
- US new home sales fell by (-) 7.8% on a MoM basis in May'19 vs (-) 3.7% in Apr'19, led shortage of land and labour. Sales declined the most in West and Northeast regions. However, existing home sales (accounting for 90% of residential investment) rose in May'19 (2.5%) suggesting lower mortgage rates may help real estate sector recover to high of Nov'17. Separately, US consumer confidence dipped to 121.5 in Jun'19 vs 131.3 in May'19, signalling consumers are less optimistic about economic outlook in the near-term.
- US durable goods orders fell by (-) 1.3% in May'19 vs (-) 2.8% in Apr'19 on a MoM basis. The decline was led by transport equipment (-4.6% in May'19 vs -7.6% in Apr'19). Orders for non-defence capital goods excl. aircraft, a proxy for business spending plans, however rose by 0.4% in May'19 after dropping by (-) 1% in Apr'19. This was on the back of increased demand for machinery, computers and electronic products.
- Central Banks of Thailand and New Zealand held their respective policy rates unchanged at 1.75% and 1.5% in the latest meeting. BoT in addition lowered its growth forecast for CY19 to 3.3% from 3.8% in Mar'19. Export growth in CY19 is expected to remain flat (0%) vs 3% projected in Mar'19. It also conveyed that future course of decision will depend upon fund inflows into the country, strength of Baht and weakness in GDP. RBNZ on other hand has expressed a need to cut more rates in the near-term.
- China's industrial profits rose by 1.1% in May'19 vs (-) 3.7% in Apr'19. This uptick was driven by high-tech manufacturing and emerging industries, signalling that impact of cuts in VAT, is taking effect. Government's fiscal stimulus also seems to be a key driver of growth. On CYTD basis profits continue to decline in May'19 by (-) 2.3% vs (-) 3.4% in Jan-Apr'19, led by automobile and computer and telecom equipment producers.

FIG 2 – MOVEMENT IN KEY GLOBAL ASSET CLASSES

Particulars	Current	1W	1M	3M	12M
10Y yields (Δ bps)					
US	2.01	(5)	(26)	(40)	(86)
UK	0.83	(1)	(8)	(17)	(45)
Japan	(0.16)	0	(9)	(8)	(19)
Germany	(0.33)	(4)	(17)	(26)	(63)
India	6.88	2	(27)	(47)	(102)
China	3.24	(1)	(9)	17	(24)
2Y yields (Δ bps)					
US	1.75	(1)	(37)	(51)	(77)
UK	0.62	1	2	(2)	(10)
Japan	(0.22)	1	(6)	(5)	(10)
Germany	(0.75)	(1)	(11)	(15)	(9)
India	6.30	8	(25)	(25)	(125)
China**	2.63	(2)	3	26	(53)
Currencies (Δ %)					
EUR	1.1373	0	1.9	1.4	(2.7)
GBP	1.2696	(0.3)	0.3	(2.6)	(3.9)
JPY	107.85	(0.5)	1.4	2.7	2.6
AUD	0.7020	1.4	1.4	(1.1)	(5.2)
INR	69.03	0.8	0.9	0.2	(0.8)
CNY	6.8668	0	0.6	(2.3)	(3.7)
Equity & Other indices (Δ %)					
Dow	26,600	(0.4)	4.9	2.6	9.6
FTSE	7,426	0.2	2.2	2.0	(2.8)
DAX	12,399	0.5	3.1	7.6	0.8
NIKKEI	21,276	0.1	0.1	0.3	(4.6)
Shanghai Comp	2,979	(0.8)	2.4	(3.6)	4.6
SENSEX	39,395	0.5	(0.9)	1.9	11.2
Brent (US\$/bbl)	66.55	2.1	(5.1)	(2.7)	(16.2)
Gold (US\$/oz)	1,410	0.7	10.2	9.1	12.5
CRB Index	408.7	(0.6)	(2.1)	(4.2)	(6.9)
Rogers Agri Index	751.4	(0.8)	0.7	1.0	(6.1)
LIBOR (3M)*	2.32	(3)	(20)	(28)	(2)
INR 5Y Swap*	6.74	22	(4)	27	(87)
India FII data (US\$ mn)					
	27 Jun	WTD	MTD	CYTD	FYTD
FII-Debt	(190.4)	(319.1)	921.9	1,157.6	612.9
FII-Equity	6.6	392.6	231.5	11,421.4	4,576.2

Source: Bloomberg, Bank of Baroda Research | *Indicates change in bps, **1Y yield.

FIG 3 – DATA RELEASE CALENDAR

Date	Event	Period	Estimate	Previous	Actual
1-Jul	China manufacturing PMI	Jun	49.5	49.4	--
	China non-manufacturing PMI	Jun	54.2	54.3	--
	South Korea exports, % YoY	Jun	(13.5%)	(9.4%)	--
	Caixin China manufacturing PMI	Jun	50.1	50.2	--
	Markit India manufacturing PMI	Jun	--	52.7	--
	Markit France manufacturing PMI	Jun	52.0	52.0	--
	Markit Germany manufacturing PMI	Jun	45.4	45.4	--
	Markit Eurozone manufacturing PMI	Jun	47.8	47.8	--
	Markit UK PMI manufacturing SA	Jun	49.5	49.4	--
	Euro Area unemployment rate, %	May	7.6%	7.6%	--
	Markit US manufacturing PMI	Jun	50.1	50.1	--
	US ISM manufacturing PMI	Jun	51.0	52.1	--
2-Jul	South Korea CPI, % YoY	Jun	0.8%	0.7%	--
	Germany retail sales, % MoM	May	0.5%	(2.0%)	--
	Euro Area PPI, % YoY	May	1.8%	2.6%	--
3-Jul	Markit Japan services PMI	Jun	--	51.7	--
	Caixin China services PMI	Jun	52.6	52.7	--
	Markit India services PMI	Jun	--	50.2	--
	Markit Italy services PMI	Jun	50.0	50.0	--
	Markit France services PMI	Jun	53.1	53.1	--
	Markit Germany services PMI	Jun	55.6	55.6	--
	Markit Eurozone services PMI	Jun	53.4	53.4	--
	Markit/CIPS UK services PMI	Jun	51.0	51.0	--
	US trade balance, US\$ bn	May	(53.5)	(50.8)	--
	US initial jobless claims	29-Jun	221,000	227,000	--
	Markit US services PMI	Jun	50.7	50.7	--
	US factory orders, % MoM	May	(0.5%)	(0.8%)	--
4-Jul	South Korea current account balance, US\$ mn	May	--	(664.8)	--
	Australia retail sales, % MoM	May	0.2%	(0.1%)	--
	India economic survey				
	Euro Area retail sales, % MoM	May	0.4%	(0.4%)	--
5-Jul	India FY20 budget presentation				
	Germany factory orders, % MoM	May	(0.2%)	0.3%	--
	France trade balance, € bn	May	(4.9)	(5.0)	--
	Taiwan CPI, % YoY	Jun	0.9%	0.9%	--
	US change in nonfarm payrolls	Jun	160,000	75,000	--
US unemployment rate, %	Jun	3.6%	3.6%	--	

Source: Bloomberg, Bank of Baroda Research

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