

WEEKLY WRAP

11 March 2019

Yields decline as growth falters

China's trade data suggests world's second largest economy is slowing faster than anticipated. Even Europe is likely to slow down this year and ECB reduced the region's growth estimate by 60bps for CY19. Global yields fell and equity markets braced for a slowing global economy. Indian yields fell as well. However, equity markets responded positively as manufacturing and services PMI inched up in Feb'19 and FII inflows resumed. INR also appreciated as a result. The global backdrop is positive for India.

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Markets

- Bonds:** Global yields fell after ECB reduced its growth and inflation projections and announced liquidity support well into 2021. Global growth concerns came to the fore after China's trade data surprised negatively. US 10Y yield declined by 12bps (2.63%). Crude prices inched up by 1% (US\$ 66/bbl) amid OPEC production cut and fall in US drilling activity. India's 7.17GS2028 yield declined by 3bps (7.53%). System liquidity deficit was reduced to Rs 25bn as on 8 Mar 2019 vs Rs 215bn in the previous week.
- Currency:** Barring JPY and INR, other global currencies closed lower this week as DXY index rose by 0.8%. While US macro data such as payroll was disappointing, a higher chance of US-China trade deal and under-performance of EUR drove US currency higher. INR ended the week higher by 1.1% supported by FII inflows (US\$ 89.3mn). Global backdrop is favourable for INR.
- Equity:** Barring Sensex, all other global indices ended lower led by renewed concerns of slowdown in global economy. Nikkei tumbled by (-) 2.7% followed by Dow (- 2.2%) and Dax (-1.2%). However, Sensex ended the week in green, posting its biggest weekly gain since Nov'18 on the back of FII inflows.
- Upcoming key events:** In the current week, investors await couple of data releases from US (CPI, retail sales, durable goods orders and new home sales) to project the trajectory of US Fed funds rate. Markets will also keep an eye on developments over US-China trade deal and Brexit. On the domestic front, inflation, trade and BoP data will guide markets.



India macro developments

- India's services PMI rose for the 9th straight month to 52.5 in Feb'19 from 52.2 in Jan'19. This was attributable to faster expansion in new orders signalling stronger demand conditions. It was further supported by higher job creation and improvement in output levels. This in turn resulted in composite PMI accelerating to a three-month high of 53.8 in Feb'19 from 53.6 in Jan'19, led by uptick in both manufacturing and services PMI.
- RBI reported that currency in circulation declined by Rs 14bn (on a weekly basis) and stood at Rs 21tn as on 1 Mar 2019. Overall reserve money grew by only 15% on a YoY basis compared to 37% a year ago. On FYTD basis, reserve money is growing at a slower pace of 10% against 21% in the previous year.
- RBI notified the interest subvention scheme for short term crop loans for the years 2018-19 and 2019-20. Under the scheme, farmers will get loan up to Rs 3lakh at an interest of 7% per annum with subvention of 2% to the lending institutions. In addition, further 2% interest subvention would also be given for early and timely repayments, thereby making effective interest to 4% p.a for these loans.
- As per news reports, finance ministry is expected to borrow around 60% of the budgeted estimate of Rs 7.1tn in H1FY20. This will be on the back of higher redemption (Rs 2.37tn in FY20) and financing of its required expenditure. In H1FY19, gross borrowing was far lower at 48%. Government is also likely to conduct more switches of around Rs 700bn to manage the rising redemption pressure.
- In order to address the woes faced by sugarcane industry, the government has approved a soft loan of Rs 150bn. Along with this, the loan amount will also enable the producers to diversify into ethanol production that will reduce the excess production of sugar to 1.5-2mn tonne form next year.
- The US government has announced terminating the benefits awarded to India under the Generalised System of Preferences (GSP). Under GSP, several Indian exports enjoy zero or very low tariffs in the US market. As per the US, a number of trade barriers implemented by India has prevented equitable access to US goods in India. As per reports, in FY18 goods worth US\$ 5.6bn out of a total of US\$ 48bn to the US were exported under this scheme.

Global macro developments

- OECD in its interim economic outlook has cut the global growth forecast to 3.3% and 3.4% in CY19 and CY20 respectively from 3.5% earlier. This was on the back of slowdown in China and EU as well as worsening global trade momentum. For CY19, while China's growth forecast was lowered to 6.2% (6.6% earlier), UK's and Germany's growth estimate was cut sharply to 0.8% (1.4% earlier) and 0.7% (from 1.6%) respectively
- US unemployment rate declined to 3.8% in Feb'19 from 4% in Jan'19. However, total nonfarm payroll employment remained broadly unchanged at 20,000 in Feb'19 (est.185,000), the weakest since Sep'17, signalling that the economy is losing steam. Average hourly earnings rose by 3.4% in Feb'19 from 3.1% in Jan'19, on a YoY basis
- Trade deficit in the US widened to a 10-year high of US\$ 621bn in CY18 vs US\$ 552bn in CY17. This was driven by a faster pace of growth in imports (7.5% in CY18 vs 6.8% in CY17) than exports (6.3% in CY18 vs 6.1% in CY17). Country wise, China still has the largest trade surplus with US followed by EU and Mexico. This data has come in the backdrop of global slowdown and heightened trade related uncertainty.
- ECB has kept its policy rates unchanged. It has significantly revised its growth & inflation projections downward by 60bps & 40bps respectively to 1.1% & 1.2% in 2019. In an effort to maintain favourable credit conditions in the economy, ECB has also launched a new series of quarterly targeted longer-term refinancing operations (TLTRO-III), which in turn might lend support to the muted demand conditions of the economy.
- On the back of global slowdown and tensions concerning trade deal, China has lowered its growth target for 2019 to 6-6.5% from the previous target of 6.5%. The annual meeting of China's parliament also highlighted that fiscal policy will be more expansionary. Budget deficit target of the government has been set at 2.8% of GDP as against 2.6% in 2018.
- China's export growth slumped by (-) 20.7% in Feb'19—lowest since Feb'16 (where Lunar New Year also fell earlier in the month, distorting Jan data). Even if the data is ironed out for this, the average Jan-Feb'19 exports growth shows a drop of (-) 5%, implying weakening global economy. China's exports to US fell by (-) 14.1% in Feb'19. Overall imports too declined in Feb'19 (-5.2% vs est.: -0.6%). Trade surplus thus declined to only US\$ 4.1bn in Feb'19 vs US\$ 39.2bn in Jan'19 and est.: US\$ 26.2bn.

FIG 1 – MOVEMENT IN KEY GLOBAL ASSET CLASSES

Particulars	Current	1W	1M	3M	12M
10Y yields (Δ bps)					
US	2.63	(12)	(7)	(22)	(27)
UK	1.19	(11)	(3)	(8)	(30)
Japan	(0.03)	(3)	(2)	(9)	(9)
Germany	0.07	(11)	(9)	(18)	(58)
India#	7.53	(3)	(4)	7	(14)
China	3.15	(6)	4	(16)	(70)
2Y yields (Δ bps)					
US	2.46	(9)	(6)	(25)	20
UK	0.75	(5)	1	1	(8)
Japan	(0.15)	(0)	1	(1)	1
Germany	(0.53)	(3)	2	7	2
India	6.66	(4)	(27)	(46)	(32)
China^	2.41	(3)	2	(9)	(85)
Currencies (Δ %)					
EUR	1.1235	(1.1)	(1.1)	(1.3)	(8.7)
GBP	1.3015	(1.4)	0.6	2.3	(6.0)
JPY	111.17	0.6	(1.1)	1.3	(4.1)
AUD	0.7045	(0.5)	(0.8)	(2.3)	(10.2)
INR	70.15	1.1	2.0	0.9	(7.6)
CNY	6.7214	(0.2)	0.4	2.2	(6.1)
Equity & Other indices (Δ %)					
Dow	25,450	(2.2)	0.2	4.4	0.5
FTSE	7,104	(0.0)	(1.0)	4.8	(1.7)
DAX	11,458	(1.2)	1.2	6.2	(7.2)
NIKKEI	21,026	(2.7)	0.7	(3.0)	(2.1)
Shanghai Comp	2,970	(0.8)	13.4	14.0	(10.2)
SENSEX	36,671	1.7	(0.8)	2.8	10.1
Brent (US\$/bbl)	65.74	1.0	4.9	6.6	0.4
Gold (US\$/oz)	1,298	0.4	(0.6)	3.9	(1.9)
CRB Index	413.6	(0.0)	0.0	(1.0)	(7.1)
Rogers Agri Index	741.5	(1.2)	(5.0)	(5.4)	(12.6)
LIBOR (3M)*	2.60	(0)	(14)	(17)	51
INR 5Y Swap*	6.97	(4)	(24)	(36)	5
India FII data (US\$ mn)					
	7 Mar	WTD	Feb'19	CYTD	FYTD
FII-Debt	(101.3)	3.6	65.5	(1,587.1)	(8,577.7)
FII-Equity	153.4	85.7	672.6	2,968.0	(3,714.9)

Source: Bloomberg, Bank of Baroda Research | *Indicates change in level | #7.17GS2028 | ^1Yr yield is taken

FIG 2 – DATA RELEASE CALENDAR

Date	Event	Period	Estimate	Previous	Actual
11-Mar	Japan machine tool orders, % YoY	Feb	--	(18.8%)	--
	Germany industrial production SA, % MoM	Jan	0.4%	(0.4%)	--
	Germany trade balance, € bn	Jan	13.5b	13.9b	--
	US retail sales advance, % MoM	Jan	0.0%	(1.2%)	--
	China FDI (CNY), % YoY	Feb	--	4.8%	--
12-Mar	Philippines exports, % YoY	Jan	(5.0%)	(12.3%)	--
	Thailand consumer confidence	Feb	--	80.7	--
	UK industrial production, % MoM	Jan	0.1%	(0.5%)	--
	India CPI, % YoY	Feb	2.4%	2.1%	--
	India industrial production, % YoY	Jan	2.0%	2.4%	--
	US CPI, % MoM	Feb	0.2%	0.0%	--
13-Mar	South Korea unemployment rate SA, %	Feb	4.2%	4.4%	--
	Japan PPI, % YoY	Feb	0.7%	0.6%	--
	Japan core machine orders, % MoM	Jan	(1.5%)	(0.1%)	--
	Euro Area industrial production SA, % MoM	Jan	0.5%	(0.9%)	--
	US PPI final demand, % MoM	Feb	0.2%	(0.1%)	--
	US durable goods orders, % MoM	Jan	(0.8%)	--	--
14-Mar	China fixed assets ex rural YTD, % YoY	Feb	6.0%	5.9%	--
	China industrial production YTD, % YoY	Feb	5.5%	6.2%	--
	China retail sales YTD, % YoY	Feb	8.1%	9.0%	--
	India WPI, % YoY	Feb	2.8%	2.8%	--
	Germany CPI, % MoM	Feb	0.5%	0.5%	--
	France CPI, % YoY	Feb	1.3%	1.3%	--
	US initial jobless claims	09-Mar	--	2,23,000	--
	US new home sales	Jan	6,28,000	6,21,000	--
15-Mar	China new home prices, % MoM	Feb	--	0.6%	--
	Indonesia exports, % YoY	Feb	--	(4.7%)	--
	Euro Area CPI, % YoY	Feb	1.5%	1.4%	--
	US industrial production, % MoM	Feb	0.6%	(0.6%)	--
	BOJ policy balance rate	15-Mar	--	(0.1%)	--
	India exports, % YoY	Feb	--	3.7%	--

Source: Bloomberg, Bank of Baroda Research

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