

## WEEKLY WRAP

12 October 2020

**RBI's moves drive Indian yields lower**

Global yields and equities went up with hopes of fresh US fiscal stimulus gaining ground. Global currencies gained against US\$ led by CNY and AUD. India's 10Y yield fell by 6bps after RBI announced accommodative stance well into next financial year, and on tap TLTRO of Rs 1tn, OMOs for SDLs and extension of HTM limits for banks. RBI projected India's growth at (-) 9.5% in FY21 before rebounding to 20.6% in Q1FY22. With inflation projected above 4% in FY22, we see limited room for further rate cuts.

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**Markets**

- **Bonds:** US 10Y yield rose by 7bps as investors pinned their hopes on US fiscal stimulus and potential win for Democrats in the upcoming presidential elections. Oil prices shot up by 9.1% (US\$ 42.9/bbl) as hurricane Delta in the Gulf of Mexico impacted output. However, India's 10Y yield fell by 6bps (5.94%) following RBI's guidance of an accommodative stance well into next year and additional liquidity support for corporates and state borrowings. System liquidity surplus was at Rs 3.9tn as on 9 Oct 2020 compared with Rs 3.7tn in the previous week.
- **Currency:** Safe-haven JPY (lower by 0.3%) and DXY (down by 0.8%) fell as risk sentiment improved on hopes of US fiscal stimulus. GBP rose by 0.8% to a 1-month high on hopes of Brexit trade deal. CNY also rose sharply to its highest level since Apr'19 as early indicators point towards a win for the Democrats in the upcoming US elections. INR closed flat as higher oil prices (up by 9.1% in the week) were offset by FII inflows (US\$ 277mn) and RBI's liquidity infusion measures.
- **Equity:** Global indices ended the week higher on hopes of US stimulus plan and expectations of Democratic win in the US presidential elections. Sensex (4.7%) surged for 7th straight session on the back of reopening of the economy, green shoots and liquidity measures announced by RBI. This was followed by gains in Dow (3.3%) and FTSE (2.9%).
- **Upcoming key events:** In the current week, US (CPI, jobless claims, retail sales, industrial production) and China (Exports, CPI, PPI) data will be in focus. In addition, Indonesia and S. Korea will announce rate decisions. On the domestic front, CPI, WPI and trade data are scheduled for release.



## India macro developments

- Government of India has appointed 3 external members to the Monetary Policy Committee of RBI. These members will have a 4-year term and will not be eligible for re-appointment, as per the RBI act. The new members are Prof Ashima Goyal from IGIDR, Prof Jayanth R Varma from IIM Ahmedabad and Dr Shashanka Bhide from NCAER. RBI had postponed its last policy meet as the appointment of external members was delayed.
- In the recent GST council meeting, deadlock on compensation cess remained unresolved. While 19 states have agreed for borrowing Rs 1.1tn from the RBI, the remaining 10 states have proposed that the Centre should borrow to meet the compensation cess gap, as it can borrow at lower rates. It was agreed that the decision will be taken in the next GST Council meet on 12 Oct 2020.
- India's services PMI improved substantially to 49.8 in Sep'20 from 41.8 in Aug'20. The jump was driven by loosening of lockdown restrictions and re-opening of business units in most states. New business orders fell at the slowest pace since Mar'20, supported by new export orders. Business outlook for the year ahead turned positive for the first time since Apr'20.
- RBI reported that currency in circulation (CIC) declined by Rs 29bn and stood at Rs 26.8tn for the week ending 2 Oct 2020. Reserve money rose by 13.5% on a YoY basis, compared with 14.3% a year ago. On a FYTD basis, reserve money increased by 6.1% as against 2.3% last year.
- World Bank has slashed India's growth forecast for FY21, estimating a contraction of 9.6% versus 4.5% decline estimated in Jun'20. The sharp cut was attributed to strict lockdown restrictions and slump in incomes of small households and businesses. Growth is expected at 5.4% in FY22, only if lockdown restrictions are fully lifted.
- MPC members unanimously voted to keep the policy rate unchanged and maintain the accommodative stance into the current and next financial year. It expects GDP to contract by 9.5% in FY21 with positive growth in Q4. Inflation too is likely to ease in the range of 4.1-4.4% in FY22 which is higher than target of 4%. RBI announced on tap TLTROs, SDL OMOs, extension of HTM limits and lower risk weight for housing.
- India's forex reserves rose by US\$ 3.6bn to a record high of US\$ 545.6bn in the week ended 2 Oct 2020. Last week, forex reserves had declined by US\$ 3bn. In FYTD21, forex reserves have increased by US\$ 70bn compared with an accretion of US\$ 25.9bn in the same period last year.

## Global macro developments

- Services sector activity globally remained weak in Sep'20. Services PMI in Euro Zone and UK edged down to 50.4 (versus 51.9) and 56.1 (versus 58.8) as new restrictions were imposed to curb the spread of COVID-19. However, separate data showed that US ISM services index rose close to the pre-pandemic level at 57.8 in Sep'20 versus 57.3 in Aug'20. The rise was led by new orders and a rebound in employment.
- Factory orders in Germany rose strongly by 4.5% in Aug'20 on a MoM basis versus 3.3% in Jul'20 and estimate of a 2.9% increase. This was led by 14.6% increase in new orders from rest of Euro Zone. Domestic orders rose by 1.7%. Sector wise, while orders for capital goods rose by 4.7%, orders for intermediate goods were also up by 4.5%.
- Reserve Bank of Australia kept its official cash rate (0.25%) and target yield for the 3-year government bonds unchanged. This was largely led by recovery cycle that is underway. However, the Governor pointed out that both unemployment and under-employment are expected to remain high for extended period. It was also hinted that low rate and stimulus measures will continue 'as long as is required' to support the economy.
- Germany's industrial production contracted by 0.2% in Aug'20 on a MoM basis, (est.: 1.7% increase) and increase of 1.4% in Jul'20. This was led by a sharp decline of 12.5% in auto production versus 8.9% increase in Jul'20. Production of capital goods and consumer goods was also down by 3.6% and 1.3% respectively in Aug'20. Industrial output in Aug'20 is estimated to be 10.8% lower compared to pre-pandemic levels.
- US FOMC minutes reinforced that while economy recovery was on track for now, it could be dented if additional fiscal stimulus is not announced in time. In addition the members also suggested that in the upcoming meetings, future course of Fed's asset management program should also be reassessed. It also reaffirmed that the current policy will be maintained till inflation and maximum employment targets are reached (~CY23/24).
- UK's industrial production rose by 0.3% in Aug'20 (MoM) versus est.: 2.5% and 5.2% increase in Jul'20. Manufacturing output slowed to 0.7% from 6.9% in Jul'20 with 8 of 13 sub-sectors reporting growth. Other manufacturing and repair were the key drivers in Aug'20. In addition, while utilities (1.6%) output contributed positively, mining and quarrying fell by 4.1%. Production in Aug'20 was 6% lower than Feb'20 levels.

FIG 1 – MOVEMENT IN KEY GLOBAL ASSET CLASSES

Particulars	Current	1W	1M	3M	12M
<b>10Y yields (Δ bps)</b>					
US	0.77	7	10	13	(96)
UK	0.28	3	5	13	(43)
Japan	0.04	1	1	1	22
Germany	(0.53)	1	(9)	(6)	(9)
India	5.94	(6)	(12)	18	(57)
China	3.19	6	9	16	3
<b>2Y yields (Δ bps)</b>					
US	0.15	2	1	0	(144)
UK	(0.02)	2	9	9	(57)
Japan	(0.12)	1	(0)	(0)	17
Germany	(0.71)	(1)	(5)	(3)	1
India	4.27	(9)	(22)	16	(140)
China**	2.62	2	5	49	4
<b>Currencies (Δ %)</b>					
EUR	1.1826	0.9	0.1	4.7	7.1
GBP	1.3036	0.8	1.8	3.3	2.9
JPY	105.62	(0.3)	0.5	1.2	2.5
AUD	0.7240	1.1	(0.2)	4.2	6.6
INR	73.13	0.0	0.4	2.8	(3.0)
CNY	6.6947	1.9	2.0	4.4	5.6
<b>Equity &amp; Other indices (Δ %)</b>					
Dow	28,587	3.3	3.8	9.6	6.6
FTSE	6,017	1.9	0.2	(1.3)	(17.0)
DAX	13,051	2.9	(1.2)	3.3	4.3
NIKKEI	23,620	2.6	1.7	6.0	8.4
Shanghai Comp	3,272	1.6	1.2	(3.3)	10.0
SENSEX	40,509	4.7	4.3	10.7	6.2
Brent (US\$/bbl)	42.85	9.1	7.0	(0.9)	(29.2)
Gold (US\$/oz)	1,930	1.6	(0.8)	7.3	29.6
CRB Index	410.3	1.7	2.8	12.9	4.9
Rogers Agri Index	772.3	2.8	4.7	11.7	6.4
LIBOR (3M)*	0.22	(1)	(3)	(4)	(178)
INR 5Y Swap*	5.33	(9)	(28)	6	(107)
<b>India FII data (US\$ mn)</b>					
	<b>8 Oct</b>	<b>WTD</b>	<b>MTD</b>	<b>CYTD</b>	<b>FYTD</b>
FII-Debt	(35.2)	(219.8)	(462.6)	(15,142.3)	(5,382.8)
FII-Equity	167.3	497.5	751.2	4,791.3	11,394.3

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

FIG 2 – DATA RELEASE CALENDAR

Date	Event	Period	Estimate	Previous	Actual
12-Oct	Japan PPI, % YoY	Sep	(0.5%)	(0.6%)	(0.8%)
	Japan core machine orders, % MoM	Aug	(1.0%)	6.3%	0.2%
	Malaysia industrial production, % YoY	Aug	0.5%	1.2%	--
	Germany producer price index, % MoM	Sep	--	(0.4%)	--
	India CPI, % YoY	Sep	6.9%	6.7%	--
	India industrial production, % YoY	Aug	(7.8%)	(10.4%)	--
13-Oct	UK ILO unemployment rate, %, 3 months	Aug	4.3%	4.1%	--
	Germany CPI, % MoM	Sep	(0.2%)	(0.2%)	--
	Bank of Indonesia 7D reverse repo	13-Oct	4.0%	4.0%	--
	Germany ZEW survey expectations	Oct	72.00	77.40	--
	US CPI, % MoM	Sep	0.2%	0.4%	--
	China exports, % YoY	Sep	10.0%	9.5%	--
14-Oct	Japan industrial production, % MoM	Aug	--	1.7%	--
	India wholesale prices, % YoY	Sep	0.9%	0.2%	--
	Euro Area industrial production, SA, % MoM	Aug	0.7%	4.1%	--
	US MBA mortgage applications	14-Oct	--	4.6%	--
	US PPI final demand, % MoM	Sep	0.2%	0.3%	--
	Bank of Korea, 7-Day repo rate	14-Oct	0.5%	0.5%	--
15-Oct	Australia unemployment rate	Sep	7.0%	6.8%	--
	China PPI, % YoY	Sep	(1.8%)	(2.0%)	--
	China CPI, % YoY	Sep	1.9%	2.4%	--
	Indonesia exports, % YoY	Sep	(7.5%)	(8.4%)	--
	France CPI, % YoY	Sep	0.1%	0.1%	--
	US initial jobless claims, in thousands	10-Oct	825	840	--
	India exports, % YoY	Sep	--	(12.7%)	--
16-Oct	Euro Area CPI, % YoY	Sep	(0.3%)	(0.3%)	--
	US retail sales advance, % MoM	Sep	0.8%	0.6%	--
	US industrial production, % MoM	Sep	0.6%	0.4%	--
	US University of Mich. sentiment	Oct	80.5	80.4	--

Source: Bloomberg, Bank of Baroda

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