

WEEKLY WRAP

15 June 2020

Risk-off drives markets lower

Global yields closed lower after US FOMC painted a dismal picture of recovery for the US economy in CY20. Risk-off sentiment resulted in 2% gain for JPY in the week. Equity markets were also lower in the week led by Dax, FTSE and Dow. Lockdown resulted in India's Industrial production declining by 55% in Apr'20. However, as restrictions were eased in May'20, food inflation did start to inch lower. We believe the sharp reduction in growth implies RBI will follow up with another rate cut in next policy meeting.

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Markets

- **Bonds:** Global long-end yields closed lower led by US as markets fear second wave after most world economies have opened up. FOMC also painted a dismal growth picture for US in CY20 with sharp contraction of 6.5%. Oil prices too fell by 8.4% (US\$ 39/bbl). India's 10Y yield fell by 3bps (6.01%) in-line with global yields. System liquidity surplus was higher at Rs 4tn as on 12 June 2020 compared with Rs 3.8tn in the previous week.
- **Currency:** Risk-off was visible in global markets with JPY and DXY gaining 2% and 0.4% respectively. Fears of a second wave led to decline in EM currencies. AUD fell by 1.5% on the back of rising tensions with China. GBP too depreciated by 1% as UK's GDP growth contracted by most on record. INR too closed lower by 0.4% despite FPI inflow of US\$ 200mn.
- **Equity:** Global indices ended the week sharply lower as US Fed painted a grim picture on US economic outlook. Markets also fear second wave which will delay economic recovery further. The fall was led by Dax (7%) followed by FTSE (5.8%) and Dow (5.6%). Sensex (1.5%) too ended lower led by subdued global cues.
- **Upcoming key events:** In current week, markets will track US industrial production, housing starts and retail sales. Germany's Zew expectation index will also be released. Central bank decisions are awaited for UK, Japan and Taiwan. India's trade data will be released. But markets will also look at spread of COVID-19 in the country.



India macro developments

- World Bank expects India's GDP growth to contract by 3.2% in FY21 as lockdown measures to curtail COVID-19 derail economic activity. Further, weakness in global economy and stress in the financial sector will also have a dampening effect on growth with a possible recovery in FY22 (3.1%). It also expects global GDP to contract by 5.2% in CY20 - the deepest contraction since WWII. Further, almost 90% of the world economies are expected to experience a recession.
- OECD in its latest economic outlook has projected India's GDP to contract sharply by 3.7% in FY21. However, the decline will be more pronounced at 7.3%, if second wave of infection prevails. The report highlighted an inclusive growth strategy with focus on social investment, income support and curtailing unwarranted revenue spending as possible solutions for recovery in the near term.
- According to news reports, GST collections have steadily declined in Mar and Apr'20, showing the impact of nationwide lockdown. While in Mar'20 collections dropped to Rs 615bn from Rs 976bn in Feb'20, they eased further in Apr'20 to Rs 495bn. On a YoY basis, Mar'20 saw a 46% decline while Apr'20 has seen 51% decline in GST collections.
- RBI sold net US\$ 1.1bn in the spot market in Apr'20 compared with US\$ 4.1bn in FX sales in Mar'20. In the forwards market, RBI purchased US\$ 3.2bn in Apr'20 versus net sales of US\$ 2.6bn in Mar'20. RBI's net outstanding forward sales position is US\$ 1.7bn versus US\$ 4.9bn in Mar'20.
- India's forex reserves rose by US\$ 8.2bn to a record-high at US\$ 501.7bn in the week ended 5 Jun 2020 compared with an increase of US\$ 3.4bn last week. This was the largest weekly increase since Sep'07. In CYTD20, forex reserves have risen by US\$ 44.2bn, higher compared with an accretion of US\$ 28.8bn last year.
- India's industrial production contracted by 55.5% in Apr'20 on the back of a nationwide lockdown led by 95.7% and 92% reduction in consumer durables and capital goods respectively. As supply side restrictions eased in May'20, food inflation fell to 9.3% from 10.5% in Apr'20. However, core inflation data was not available apart from housing and health. Notably, health inflation did inch up. We do believe sharp contraction in growth warrants another rate cut by RBI to mitigate the impact on the economy.

Global macro developments

- UNCTAD estimates world trade to contract by 27% in Q2CY20 in value terms, versus a decline of 5% in Q1CY20 due to the COVID-19 pandemic. The decline is more pronounced in Apr'20 with trade nose-diving sharply in developing countries. Trade in energy and auto products is estimated to have fallen by 40% and 50% respectively in Apr'20. For CY20, global trade is expected to contract by 20%.
- US PPI rose by 0.4% on MoM basis in May'20 versus 1.3% decline in Apr'20, driven by higher prices of final goods (1.6% versus 3.3% decline in Apr'20). Within goods, prices of both food and energy rose. Prices of services continued to decline by 0.2% in May'20. Separately, initial jobless claims for the week ending 6 Jun eased to 1.5mn from 1.9mn the previous week. The 4W-moving average also eased to 2mn (previously 2.3mn).
- Fed in its recent policy highlighted that policy rate is expected to be at its ultra-low level (0-0.25%) till CY22. Further, US GDP is estimated to fall sharply by 6.5% in CY20 (2% growth projected earlier) due to COVID-19. Unemployment is also expected to be higher at 9.3% and inflation lower at 0.8%. Fed will continue its pace of asset purchase to support the economy. However, revival is expected from CY21 onwards.
- Growth in the Euro Area and EU fell sharply by 3.6% and 3.2% respectively in Q1CY20, on a QoQ basis against 0.1% growth in Q4CY19. This was the steepest decline since CY95. Sharp contraction in household consumption spending and exports amidst COVID-19 crisis contributed to this decline. Employment in both the Euro area and EU is down by 0.2% and 0.1% respectively in Q1CY20- first time since Q2CY13.
- UK GDP contracted by 20.4% in Apr'20 against 5.8% decline in Mar'20. The econtraction was led by sharp fall in construction (40% decline against 5.9% fall in Mar'20) and manufacturing (24.3% decline against 4.6% fall in Mar'20) activities. In a separate print UK's industrial production also fell by a record 20.3% in Apr'20.
- Japan's GDP in Q1CY20 contracted by 2.2%, less than previously estimated (3.4%) and up from 7.2% dip in Q4CY19. The upward revision was driven by private non-residential investment, revised from a decline of 2.1% to increase of 8%. Private consumption, and exports continued to contribute negatively. In Q2CY20, GDP is estimated to contract by over 20% led by private investment and consumption.

FIG 1 – MOVEMENT IN KEY GLOBAL ASSET CLASSES

Particulars	Current	1W	1M	3M	12M
10Y yields (Δ bps)					
US	0.71	(19)	(4)	(14)	(143)
UK	0.21	(15)	(7)	(7)	(64)
Japan	0.01	(4)	0	7	12
Germany	(0.44)	(16)	10	33	(17)
India	5.99	(3)	(18)	(25)	(102)
China	2.79	(6)	13	14	(50)
2Y yields (Δ bps)					
US	0.19	(2)	2	(28)	(164)
UK	(0.05)	(6)	(6)	(25)	(64)
Japan	(0.17)	(5)	(1)	8	6
Germany	(0.69)	(9)	10	28	3
India	4.42	(3)	1	(97)	(184)
China**	1.99	0	75	3	(54)
Currencies (Δ %)					
EUR	1.1256	(0.3)	4.6	1.0	0.2
GBP	1.2540	(1.0)	2.2	0.2	(0.6)
JPY	107.38	2.0	0.7	(2.1)	1.4
AUD	0.6866	(1.5)	5.6	9.9	(0.9)
INR	75.85	(0.4)	(0.1)	(2.1)	(9.0)
CNY	7.0835	0	0.5	(0.5)	(2.1)
Equity & Other indices (Δ %)					
Dow	25,606	(5.6)	3.7	18.5	(3.7)
FTSE	6,105	(5.8)	2.3	16.0	(17.5)
DAX	11,949	(7.0)	10.6	30.7	(1.6)
NIKKEI	22,184	(3.0)	10.2	21.1	6.9
Shanghai Comp	2,920	(0.4)	0.9	(0.1)	0.3
SENSEX	33,781	(1.5)	6.3	2.3	(15.6)
Brent (US\$/bbl)	38.73	(8.4)	30.1	16.0	(37.1)
Gold (US\$/oz)	1,728	2.7	1.8	9.6	28.7
CRB Index	366.6	(0.5)	1.3	(7.4)	(11.3)
Rogers Agri Index	676.4	(0.7)	2.9	0.5	(11.3)
LIBOR (3M)*	0.32	0	(12)	(42)	(209)
INR 5Y Swap*	5.22	6	(9)	(39)	(156)
India FII data (US\$ mn)					
	11 Jun	WTD	MTD	CYTD	FY20
FII-Debt	15.7	(65.2)	(290.9)	(14,346.2)	(4,586.7)
FII-Equity	113.2	266.4	2,864.5	(2,050.0)	4,553.0

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

FIG 2 – DATA RELEASE CALENDAR

Date	Event	Period	Estimate	Previous	Actual
15-Jun	China new home prices, % MoM	May	--	0.4%	0.5%
	China industrial production, % YoY	May	5.0%	3.9%	4.4%
	China retail sales, % YoY	May	(2.3%)	(7.5%)	(2.8%)
	China property investment YTD, % YoY	May	(0.8%)	(3.3%)	(0.3%)
	China fixed assets ex rural YTD, % YoY	May	(6.0%)	(10.3%)	(6.3%)
	India WPI, % YoY	May	(1.2%)	--	--
	Italy CPI, % YoY	May	(0.2%)	(0.2%)	--
	India exports, % YoY	May	--	(60.3%)	--
16-Jun	RBA minutes of Jun. policy meeting				
	UK ILO unemployment rate 3mths, %	Apr	4.7%	3.9%	--
	Germany CPI, % YoY	May	0.6%	0.6%	--
	Germany ZEW survey expectations	Jun	60.0	51.0	--
	US retail sales advance, % MoM	May	8.0%	(16.4%)	--
	US industrial production, % MoM	May	3.0%	(11.2%)	--
	BOJ policy balance rate, %	16-Jun	(0.1%)	(0.1%)	--
17-Jun	Japan exports, % YoY	May	(26.1%)	(21.9%)	--
	UK CPI, % YoY	May	0.5%	0.8%	--
	Euro Area CPI, % MoM	May F	(0.1%)	(0.1%)	--
	US housing starts, in mn	May	1.1	0.9	--
18-Jun	Australia unemployment rate, %	May	6.9%	6.2%	--
	Bank of England bank rate, %	18-Jun	0.10%	0.10%	--
	US initial jobless claims, in mn	13-Jun	1.3	1.5	--
	Taiwan CBC benchmark interest rate, %	18-Jun	1.0%	1.1%	--
19-Jun	Japan CPI, % YoY	May	0.2%	0.1%	--
	Germany PPI, % MoM	May	(0.3%)	(0.7%)	--
	Euro Area current account SA, € bn	Apr	--	27.4	--
	US current account balance, US\$ bn	1Q	(103.0)	(109.8)	--

Source: Bloomberg, Bank of Baroda

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