

WEEKLY WRAP

17 June 2019

Fed policy to drive markets

Oil prices fell by 2% in the week after EIA lowered its demand forecast for CY19 and Chinese imports, industrial production and investment remain under pressure. However, global equity markets went up ahead of US Fed's meeting. US yields were flat ahead of the meeting but DXY appreciated as US retail sales and production surprised positively. A weak global backdrop helped India's WPI to fall to a 22-month low of 2.45%. This along with RBI's OMO purchase of Rs 125bn despite surplus liquidity led to 5bps decline in 10Y yield.

Sameer Narang

+91 22 6698 5713

chief.economist@bankofbaroda.com

Sonal Badhan

sonal.badhan@bankofbaroda.com

Markets

- Bonds:** Global yields closed mixed amidst trade war concerns, volatility in oil prices and downbeat outlook on growth. US 10Y yield closed stable at 2.08% ahead of Fed's June policy meeting. Crude prices fell by 2% as US inventories increased and EIA lowered its forecast for oil demand in CY19. India's 10Y yield fell by 5bps (6.92%) supported by lower than anticipated WPI inflation and RBI's OMO purchase of Rs 125bn this week despite liquidity being in surplus of Rs 495bn vs Rs 676bn in the previous week.
- Currency:** Global currencies closed lower against the dollar. DXY rose by 1.1% in the week on upbeat US retail sales data. Upcoming Fed meet, US-China trade developments and weak Chinese industrial production and fixed asset investment data also supported USD. EUR depreciated by (-) 1.2% on disappointing industrial production data. INR fell by (-) 0.5% in the week as flaring geo-political tensions in Iran led to volatility in oil prices. FII inflows were at US\$ 321mn.
- Equity:** Barring Sensex, global indices ended the week higher on expectation of rate cut by Fed in its upcoming policy meet. Shanghai Comp gained by 1.9% followed by Nikkei at 1.1%. Sensex on the other hand ended the week in red falling by (-) 0.4% led by auto and banking stocks.
- Upcoming key events:** In the current week all eyes will be on the rate decision by US Fed, BoE and BoJ. Asian central banks in Indonesia, Philippines and Taiwan will also announce policy rates. Indonesia has held rates steady since Nov'18. On domestic front, progress of monsoon will be monitored closely.



India macro developments

- As per news reports, government is planning to privatise profit making state-run companies from its earlier policy of only disinvesting in loss making CPSEs. The disinvestment target for FY20 has been kept at Rs 900bn. However, government has been unable to sell any CPSEs to the private sector despite having approval for 24 firms including Air India.
- RBI made net purchase of US\$ 4.9bn in the spot market in Apr'19 vs US\$ 9.4bn in Mar'19. In the forward market, RBI sold US\$ 4.7bn in Apr'19, compared with sale of US\$ 9.4bn in Mar'19. RBI's net outstanding forward sales widened to US\$ 18.5bn from US\$ 13.8bn in Mar'19.
- India's CPI inflation rose to a 7-month high of 3.05% in May'19 led by higher food inflation. IIP growth also recovered to a 6-month high at 3.4% in Apr'19. Core inflation eased to 4.2% driven by across the board decline. While CPI has risen for 4-months now, it is still below RBI's target. With oil prices currently at US\$ 60/bbl, RBI has room to cut rates further. Progress of monsoon and Budget will however dictate the timing of the rate cut.
- UNCTAD's latest report highlighted that investment climate remained gloomier with global FDI flows falling for the 3rd consecutive year by 13% to US\$ 1.3tn in CY18. India received higher FDI (US\$ 42bn in CY18 vs US\$ 40bn in CY17) and ranked 10th among major economies, on account of robust inflows in manufacturing, communication and financial services.
- As per news reports, government may rollover Rs 626bn in subsidies payment to FY21, in order to stick to the 3.4% fiscal deficit target in FY20. In FY20 interim budget, fertilizer subsidy was kept at Rs 750bn and fuel subsidy at Rs 375bn. However, fertilizer companies have reported Rs 1.1tn payment dues from the government, while fuel companies (IOC, BP & HP) report Rs 631bn is pending in dues, together implying a gap of Rs 626bn.
- India has imposed higher tariffs on 28 US imports (over US\$ 200mn) from 16 Jun. These include important US export items to India such as apples, almonds and walnuts. On 5 Jun, US withdrew tariff concessions to India under the GSP scheme which allowed duty-free exports of up to US\$ 5.6bn to the US. India's imports from US were US\$ 35bn in FY19.
- India's forex reserves rose for the third straight week to its highest in over 14-months at US\$ 423.6bn in the week ending 7 Jun 2019. On a weekly basis, forex reserves rose by US\$ 1.7bn compared with an increase of US\$ 1.9bn last week. In CY19, forex reserves have increased by US\$ 30.1bn vs an increase of US\$ 3.7bn last year, supported by RBI's dollar-rupee swap as well as strong FII inflows.

Global macro developments

- US CPI eased to 1.8% in May'19 vs est.: 1.9% and 2% in Apr'19. Core CPI too fell (2% vs 2.1% in Apr'19) indicating muted inflationary pressures. This was mainly on account of softening prices of apparels, new vehicles and services. While this points towards weak domestic demand and calls for a rate cut by Fed, analysts believe that the Jun'19 meeting will be too soon for any decision.
- Retail sales in the US rose by 0.5% (est. 0.6%) in May'19 vs 0.3% in Apr'19 on MoM basis. This was driven by pickup in motor vehicle sales reflecting signs of improvement in consumption demand amidst a muted backdrop. In a separate print, US industrial production also rebounded by 0.4% in May'19 vs (-) 0.4% in Apr'19 driven by broad-based pickup in all sectors except mining. Capacity utilization also inched up 0.2% to 78.1% in May'19.
- Producer prices in the US moderated and rose by 0.1% in May'19 vs 0.2% in Apr'19, on MoM basis. On a YoY basis as well, PPI edged down to 1.8% in May'19 vs 2.2% in Apr'19 led by falling energy prices. Muted inflation print in the past few months have refrained Fed from taking any call on interest rates.
- China's PPI eased from 0.9% in Apr'19 to 0.6% in May'19, on the back of declining price gains in oil, natural gas extraction, coal processing, and construction material. This trend is also confirmed by softening non-food retail inflation (1.6% in May'19 vs 1.7% in Apr'19). Despite this headline CPI rose to 2.7% from 2.5% in Apr'19 on account of higher prices (7.7% in May'19 vs 6.1% in Apr'19), led by supply side distortions.
- China's export growth surprised positively as it rose by 1.1% in May'19 on a YoY basis, vs est.: (-) 3.8% and (-) 2.7% in Apr'19. Front loading of exports and weakening Yuan (-7.2% YoY in May'19) may have helped export growth. Import growth on the other hand fell to the lowest in 3 years (-8.5% in May'19 vs est. -3.8%) pointing towards weak domestic demand conditions.
- China's industrial production growth eased to 5% in May'19 (lowest in 17 years), and down from est.: 5.5% and 5.4% in Apr'19. This was in line with FAI growth slipping to 5.6% between Jan-May'19 vs 6.1% in Jan-Apr'19. Only retail sales, mainly owing to seasonality, rose marginally from 7.2% in Apr'19 (lowest since May'03) to 8.6% in May'19. As a result, to boost growth government has recently announced 300bn Yuan support for smaller banks and analysts expect a 100bps cut in RRR in CY19.
- Industrial production in the Euro Area fell for the 2nd straight month in Apr'19 by (-) 0.5% vs (-) 0.4% in Mar'19, on a MoM basis. This was led by consumer durables (-1.7%) and capital goods (-1.4%). Germany saw the largest decline (-2.3%). Separately, Germany's economy ministry predicted that growth in Q2CY19 is likely to be subdued as the manufacturing sector reels under the effect of US trade war against China and EU.

FIG 2 – MOVEMENT IN KEY GLOBAL ASSET CLASSES

Particulars	Current	1W	1M	3M	12M
10Y yields (Δ bps)					
US	2.08	0	(33)	(51)	(84)
UK	0.85	3	(26)	(36)	(48)
Japan	(0.13)	(1)	(8)	(10)	(17)
Germany	(0.26)	0	(19)	(34)	(66)
India	6.92	(5)	(46)	(42)	(97)
China	3.27	2	(2)	12	(35)
2Y yields (Δ bps)					
US	1.84	(1)	(36)	(60)	(71)
UK	0.61	8	(11)	(16)	(12)
Japan	(0.20)	0	(5)	(5)	(7)
Germany	(0.69)	(2)	(6)	(15)	(8)
India	6.22	(5)	(47)	(37)	(132)
China**	2.53	(6)	(13)	8	(64)
Currencies (Δ %)					
EUR	1.1208	(1.1)	0	(1.0)	(3.5)
GBP	1.2589	(1.2)	(2.4)	(5.3)	(5.2)
JPY	108.56	(0.3)	1.0	2.6	1.9
AUD	0.6872	(1.8)	(1.0)	(3.0)	(7.7)
INR	69.80	(0.5)	0.9	(1.0)	(2.6)
CNY	6.9255	(0.2)	(0.7)	(3.2)	(7.6)
Equity & Other indices (Δ %)					
Dow	26,090	0.4	2.2	0.9	4.0
FTSE	7,346	0.2	1.4	1.6	(3.8)
DAX	12,096	0.4	0.9	3.5	(7.0)
NIKKEI	21,117	1.1	0.2	(1.6)	(7.6)
Shanghai Comp	2,882	1.9	(0.1)	(4.6)	(4.6)
SENSEX	39,452	(0.4)	5.7	3.8	10.8
Brent (US\$/bbl)	62.01	(2.0)	(13.0)	(7.7)	(15.6)
Gold (US\$/oz)	1,342	0.1	3.5	3.0	4.9
CRB Index	412.1	0.6	0.4	(1.8)	(8.4)
Rogers Agri Index	764.1	2.6	7.8	1.0	(6.5)
LIBOR (3M)*	2.41	(4)	(11)	(22)	8
INR 5Y Swap*	6.79	17	(21)	13	(71)
India FII data (US\$ mn)					
	13 Jun	WTD	MTD	CYTD	FYTD
FII-Debt	5.2	322.8	1,109.5	1,345.2	800.6
FII-Equity	(92.7)	(1.9)	74.9	11,264.8	4,419.6

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

FIG 3 – DATA RELEASE CALENDAR

Date	Event	Period	Estimate	Previous	Actual
17-Jun	Italy general government debt, € bn	Apr	--	2.4	--
	China new home prices, % MoM	May	--	0.6%	--
18-Jun	RBA minutes of June policy meeting	4-Jun	--	--	--
	Euro Area trade balance SA, € bn	Apr	16.3	17.9	--
	Euro Area CPI, % YoY	May	1.2%	--	--
	Germany ZEW survey expectations	Jun	(5.8)	(2.1)	--
	US housing starts	May	1,235	1,235	--
	Japan trade balance, ¥ bn	May	(1,207)	60.4	--
19-Jun	Germany PPI, % YoY	May	2.2%	2.5%	--
	UK CPI, % YoY	May	2.0%	2.1%	--
	US FOMC policy rate, %	19-Jun	2.50%	2.50%	--
	South Korea PPI, % YoY	May	--	0.6%	--
20-Jun	Japan machine tool orders, % YoY	May	--	(27.3%)	--
	Taiwan benchmark interest rate, %	20-Jun	1.38%	1.38%	--
	Philippines policy rate, %	20-Jun	4.25%	4.50%	--
	UK retail sales ex auto fuel, % MoM	May	(0.5%)	(0.2%)	--
	Bank of England bank rate, %	20-Jun	0.75%	0.75%	--
	US current account balance, US\$ bn	Q1CY19	(125.0)	(134.4)	--
	US initial jobless claims, thousands	15-Jun	220	222	--
	Euro Area consumer confidence	Jun	(6.5)	(6.5)	--
	BOJ policy rate, %	20-Jun	--	(0.10%)	--
	Bank of Indonesia policy rate, %	20-Jun	6.00%	6.00%	--
	Japan CPI, % YoY	May	0.7%	0.9%	--
	21-Jun	Markit France manufacturing PMI	Jun	50.9	50.6
Markit France services PMI		Jun	51.6	51.5	--
Markit/BME Germany manufacturing PMI		Jun	44.6	44.3	--
Markit Germany services PMI		Jun	55.3	55.4	--
Markit Eurozone manufacturing PMI		Jun	48.0	47.7	--
Markit Eurozone services PMI		Jun	53.0	52.9	--
Markit US manufacturing PMI		Jun	50.5	50.5	--
Markit US services PMI		Jun	51.0	50.9	--
US existing home sales, mn		May	5.25	5.19	--

Source: Bloomberg, Bank of Baroda Research

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For further details about this publication, please contact:

Economics Research Department

Bank of Baroda

+91 22 6698 5713

chief.economist@bankofbaroda.com