

WEEKLY WRAP

17 August 2020

Global yields rise as recovery continues

Worst seems to be over for global economy with Euro Area, Singapore and UK reporting sharp contraction for Q2CY20. Recent data shows while manufacturing and services activity is rebounding, consumption is still weak. As a result, yields rose and gold prices fell. US 10Y yield rose by as much as 15bps. India's 10Y yield rose by 8bps as higher inflation rules out further rate cuts by RBI. In addition, dividend transfer by RBI is lower than last year. MPC minutes this week may shed light on growth inflation debate in RBI.

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Markets

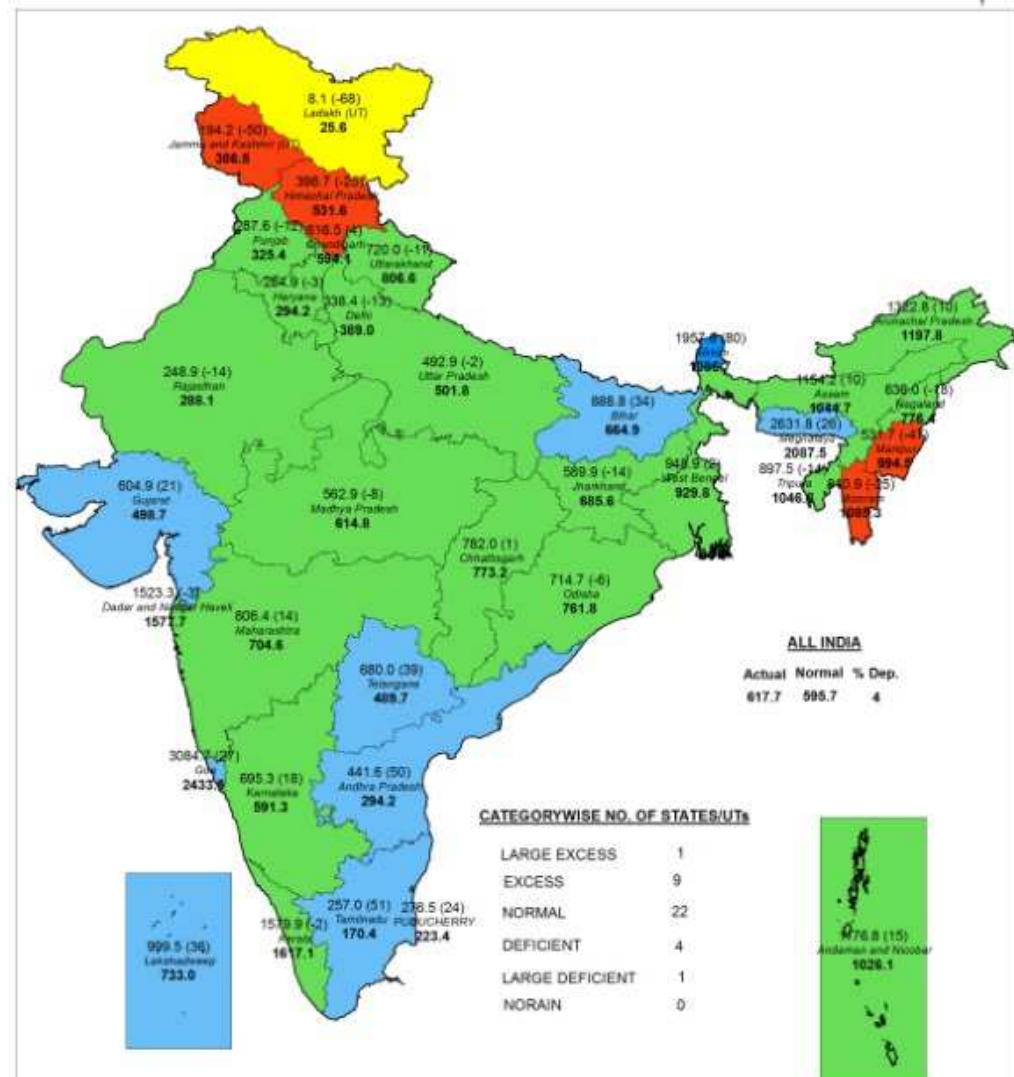
- Bonds:** Except China, global yields closed higher. US 10Y yield rose the most by 15bps (0.71%) supported by better CPI data and improvement in employment scenario. Oil prices rose by 0.9% (US\$ 45/bbl) due to unexpected drop in US inventory. India's 10Y yield rose by 8bps (5.97%) due to firming up of CPI, core print and also lower than expected surplus transfer by RBI to the government. System liquidity surplus fell to Rs 3.3tn as on 14 Aug 2020 compared with Rs 3.8tn in the previous week.
- Currency:** Except JPY, other global currencies closed higher this week on the back of dollar weakness. DXY fell by 0.4% in the week, as uncertainty remained over US fiscal stimulus. EUR rose by 0.5% supported by improvement in Germany's economic sentiment index in Aug'20. AUD also rose by 0.2% as Australia's unemployment rate rose less than expected in Jul'20. INR closed stable even as FII inflows surged to US\$ 2.2bn in the week.
- Equity:** Except Sensex, global equity indices rose on hopes of an economic recovery. Nikkei surged the most by 4.3%, to a 6-month high. Dow surged by 1.8% amidst improvement in US CPI print and jobless claims. Sensex fell by 0.4% weighed down by banking and technology stocks.
- Upcoming key events:** In current week, markets await global flash manufacturing PMIs and US FOMC meeting minutes. Apart from this, housing data and jobless claims print of the US will also shed some light on the underlying economic conditions. On the domestic front, minutes of RBI's August policy meeting are awaited.



Monsoon tracker

- For the period 1 Jun 2020 to 16 Aug 2020, monsoon is 4% above LPA compared with 1% last year. While large parts of central and north eastern region of the country continue to receive normal rainfall, states like Bihar, Gujarat, Telangana and Tamil Nadu have been receiving heavy rainfall. On the other hand, parts of J&K, Himachal Pradesh and Manipur have received deficient rainfall.
- Overall Kharif sowing is higher by 8.5% compared with last year. The improvement is led by higher sown area for rice (14.1%), cereals (10.4%) and foodgrains (8.7%). Sowing area of oilseeds and cotton rose sharply by 14.4% and 3.2% respectively.

FIG 1 – DISTRIBUTION PATTERN OF SOUTH-WEST MONSOON



Source: IMD, Bank of Baroda Research | Note: Cumulative Data for 1 Jun-16 Aug 2020

India macro developments

- As per CMIE data, India's unemployment rate for the week ending 9 Aug 2020 rose considerably to 8.7% from 7.2% in the previous week. This was on account of significant jump in the rural unemployment rate (8.4% against 6.5%). Urban unemployment rate also went up to 9.3% from 8.7% in the previous week, indicating strain in the employment scenario.
- India's auto sales showed improvement as the pace of contraction eased significantly in Jul'20 to 18.6% from 43% in Jun'20. Most recovery was visible in passenger vehicle sales which fell by 3.9% compared with 49.6% last month. Two-wheeler sales were also better with decline of only 15.2% versus 38.6% in Jun'20.
- RBI reported that currency in circulation (CIC) increased by Rs 136.2bn and stood at Rs 26.8tn for the week ended 7 Aug 2020. Reserve money rose by 15% on a YoY basis, versus 12.5% a year ago. On a FYTD basis, reserve money increased by 5.2% as against an increase of 0.1% last year.
- RBI purchased net US\$ 9.8bn in Jun'20 in the spot market versus net purchase of US\$ 4.4bn in May'20. In Q1FY21, RBI purchased US\$ 13bn in spot market versus purchase of US\$ 9.9bn in Q1FY20. In the forwards market as well, RBI purchased US\$ 4.4bn versus sale of US\$ 0.2bn in May'20. RBI's net outstanding forward position is at US\$ 2.5bn.
- RBI approved a transfer of Rs 571.3bn for the accounting year 2019-20 to the government, while maintaining the contingency risk buffer at 5.5%. Last year, RBI had transferred Rs 1.76tn inclusive of Rs 1.23tn as dividend and Rs 526bn from surplus capital to the government. This comes in the wake of the economy struggling with record fiscal deficit on account of revenue shortage due to imposition of lockdown.
- CPI inflation rose to 6.9% in Jul'20 (6.2% in Jun'20) led by higher food and core inflation. Only 3 food items have reported an inflation level below 4%. The drivers of core are: personal care at 13.6% and transport and communication at 10%. Core tends to be sticky and supply bottlenecks are impacting food. Thus, CPI inflation is likely to remain above RBI's target of 4% making further rate cuts difficult for now.
- India's trade deficit increased to US\$ 4.8bn in Jul'20 versus a surplus of US\$ 0.8bn in Jun'20 as imports picked up faster than exports. Exports contracted by 10.2% in Jul'20 versus 12.4% drop in Jun'20. Imports contracted by only 28.4% in Jul'20, after falling steeply by 47.6% in Jun'20 led by an increase in gold imports. Electronic imports are also showing some revival as demand stabilizes after unlocking of the economy.

Global macro developments

- Singapore's GDP contracted by 13.2% in Q2CY20 on a YoY basis, lower compared with an initial estimate of 12.6% decline. This is the largest decline on record and follows a 0.3% contraction in Q1, pushing the economy into a technical recession. With this, the government now expects GDP to contract by 5%-7% (4%-7% earlier).
- China's PPI fell by 2.4% in Jul'20 versus est.: 2.5% decline and 3% drop in Jun'20. The easing was driven by higher prices of oil and other major raw materials, as signs of recovery were visible across regions. CPI inched up to 2.7% in Jul'20 from 2.5% in Jun'20, as supply disruptions due to floods impacted food prices. Core inflation however eased to 0.5% from 0.9% in Jun'20, as prices of services continue to fall, as demand still remains weak.
- Germany's ZEW economic expectation index jumped 12.2 points to 71.5 in Aug'20. However the current situation index remained weak at (-) 81.3 versus (-) 80.9 in Jul'20, as the pace of current recovery is estimated to be slow. While the domestic economy is expected to recover fast, key concerns over poor earnings for banks and insurers over the next 6 months remain.
- US consumer prices inched up by 0.6% in Jul'20 on MoM basis, same as in Jun'20 and higher than expectation of 0.3%. This was led by surge in gasoline prices (5.6%). CPI excluding food and energy registered its highest monthly gain since Jan'91 at 0.6% versus 0.2% in Jun'20. On an annualised basis, CPI and core CPI rose by 1% and 1.6% respectively.
- UK GDP contracted by record 20.4% in Q2CY20 on a QoQ basis, versus 2.2% decline in Q1, thus entering a technical recession. This was driven by 23.1% drop in household consumption versus 2.9% decline in Q1 and 25.5% contraction in GFCF versus 1.1% dip in Q1. Services sector activity fell by 19.2% in Q2 from 2.3% drop in Q1.
- China's industrial production rose by 4.8% in Jul'20, same as Jun'20 and tad lower than estimate of 5.1% increase. This was driven by 6% jump in manufacturing output, while mining output fell by 2.6%. Supply chains seem to be recovering with investment also picking up, but consumer spending remains weak. Dip in FAI on CYTD basis eased to 1.6% in Jan-Jul'20 versus 3.1% in H1. Retail sales showed slower recovery as it declined by 1.1% versus 1.8% in Jun'20 and est.: 0.1% increase.
- US industrial production rose by 3% in Jul'20 on a MoM basis versus 5.7% rise in Jun'20, with growth in manufacturing sector easing (3.4% from 7.4%). Separately, retail sales in Jul'20 rose by 1.2% versus 8.4% in Jun'20. While headline print was dragged down by motor vehicles, building material and clothing, spending on electronic items and health care items remained steady.

FIG 2 – MOVEMENT IN KEY GLOBAL ASSET CLASSES

Particulars	Current	1W	1M	3M	12M
10Y yields (Δ bps)					
US	0.71	15	8	7	(84)
UK	0.24	10	8	1	(22)
Japan	0.05	4	2	5	28
Germany	(0.42)	9	2	11	26
India	5.97	8	16	19	(58)
China	2.94	(4)	(1)	29	(8)
2Y yields (Δ bps)					
US	0.15	2	(1)	0	(133)
UK	(0.02)	1	7	(1)	(54)
Japan	(0.11)	1	2	4	16
Germany	(0.65)	4	2	8	26
India	4.25	3	9	(25)	(162)
China**	2.26	2	12	105	(26)
Currencies (Δ %)					
EUR	1.1842	0.5	3.8	9.4	6.8
GBP	1.3086	0.3	4.0	8.0	7.7
JPY	106.60	(0.6)	0.3	0.4	(0.2)
AUD	0.7171	0.2	2.3	11.8	5.8
INR	74.90	0	0.3	0.9	(5.3)
CNY	6.9503	0.3	0.6	2.1	1.3
Equity & Other indices (Δ %)					
Dow	27,931	1.8	3.9	17.9	7.9
FTSE	6,090	1.0	(3.2)	5.0	(14.4)
DAX	12,901	1.8	(0.2)	23.3	11.6
NIKKEI	23,289	4.3	1.5	16.2	14.1
Shanghai Comp	3,360	0.2	0	17.1	19.0
SENSEX	37,877	(0.4)	5.1	21.8	1.4
Brent (US\$/bbl)	44.80	0.9	2.3	37.8	(23.6)
Gold (US\$/oz)	1,945	(4.4)	7.4	11.6	28.5
CRB Index	380.4	0.5	4.0	4.8	(4.5)
Rogers Agri Index	708.7	2.6	2.9	7.8	2.1
LIBOR (3M)*	0.27	2	0	(11)	(187)
INR 5Y Swap*	5.34	11	8	16	(95)
India FII data (US\$ mn)					
	13 Aug	WTD	MTD	CYTD	FYTD
FII-Debt	78.9	33.3	36.8	(14,490.8)	(4,731.3)
FII-Equity	66.4	2,271.3	3,613.4	2,325.2	8,928.2

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

FIG 3 – DATA RELEASE CALENDAR

Date	Event	Period	Estimate	Previous	Actual	
17-Aug	Japan GDP, SA, % QoQ	Q2CY20	(7.5%)	(0.6%)	(7.8%)	
	Thailand GDP, % YoY	Q2CY20	(13.0%)	(2.0%)	(12.2%)	
	Japan industrial production, % MoM	Jun	--	2.7%	--	
18-Aug	Minutes of RBA Aug policy meeting		--	--	--	
	Indonesia exports, % YoY	Jul	(14.3%)	2.3%	--	
	US housing starts, in thousands	Jul	1,240	1,186	--	
19-Aug	Japan trade balance, ₹bn	Jul	(85)	(269)	(269)	
	Japan core machine orders, % MoM	Jun	2.0%	1.7%	--	
	UK CPI, % YoY	Jul	0.6%	0.6%	--	
	UK PPI Output, NSA, % MoM	Jul	0.2%	0.3%	--	
	Bank of Indonesia 7D reverse repo	19-Aug	4.0%	4.0%	--	
	Eurozone current account, SA, EURbn	Jun	--	8.0	--	
	Hong Kong unemployment rate, SA	Jul	6.4%	6.2%	--	
	Euro Area CPI, % YoY	Jul	0.4%	0.3%	0.3%	
	US MBA mortgage applications	14-Aug	--	6.8%	--	
	US FOMC meeting minutes	29-Jul	--	--	--	
	Philippines BoP, \$mn	Jul	--	80.0	--	
	20-Aug	Germany PPI, % MoM	Jul	0.1%	0.0%	--
		BSP overnight borrowing rate	20-Aug	2.3%	2.3%	--
		Taiwan export orders, % YoY	Jul	3.1%	6.5%	--
		Minutes of RBI Aug policy meeting		--	--	--
Hong Kong CPI, % YoY		Jul	0.5%	0.7%	--	
US initial jobless claims, in thousands		15-Aug	920	963	--	
21-Aug	Japan CPI, % YoY	Jul	0.3%	0.1%	--	
	S. Korea exports, 20 Days, % YoY	Aug	--	(12.8%)	--	
	Jibun Bank Japan manufacturing PMI	Aug	--	45.2	--	
	Jibun Bank Japan services PMI	Aug	--	45.4	--	
	UK retail sales (inc auto fuel), % MoM	Jul	2.0%	13.9%	--	
	Markit France manufacturing PMI	Aug	53.0	52.4	--	
	Markit France services PMI	Aug	56.0	57.3	--	
	Markit/BME Germany manufacturing PMI	Aug	52.3	51.0	--	
	Markit Germany services PMI	Aug	55.1	55.6	--	
	Markit Eurozone manufacturing PMI	Aug	52.7	51.8	--	
	Markit Eurozone services PMI	Aug	54.6	54.7	--	
	Markit UK PMI manufacturing SA	Aug	54.0	53.3	--	
	Markit/CIPS UK services PMI	Aug	57.0	56.5	--	
	Markit US manufacturing PMI	Aug	51.5	50.9	--	
	US existing home sales, in mn	Jul	5.40	4.72	--	

Source: Bloomberg, Bank of Baroda

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