

WEEKLY WRAP

05 August 2019

Fed cuts rate, RBI to follow

US-China trade war escalated as US announced additional tariffs on US\$ 300bn of Chinese imports. Global manufacturing remained muted in Jul'19. As a result, global yields, equities and oil prices fell. US 10Y yield fell by (-) 23bps. US Fed cut rates by 25bps. Other central banks such as BoE, BoJ, ECB and RBI will also ease. While India's manufacturing PMI improved slightly in Jul'19, the growth outlook remains weak. We thus expect RBI to cut rates by 50bps this week to support growth as inflation remains below RBI's target of 4%.

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Markets

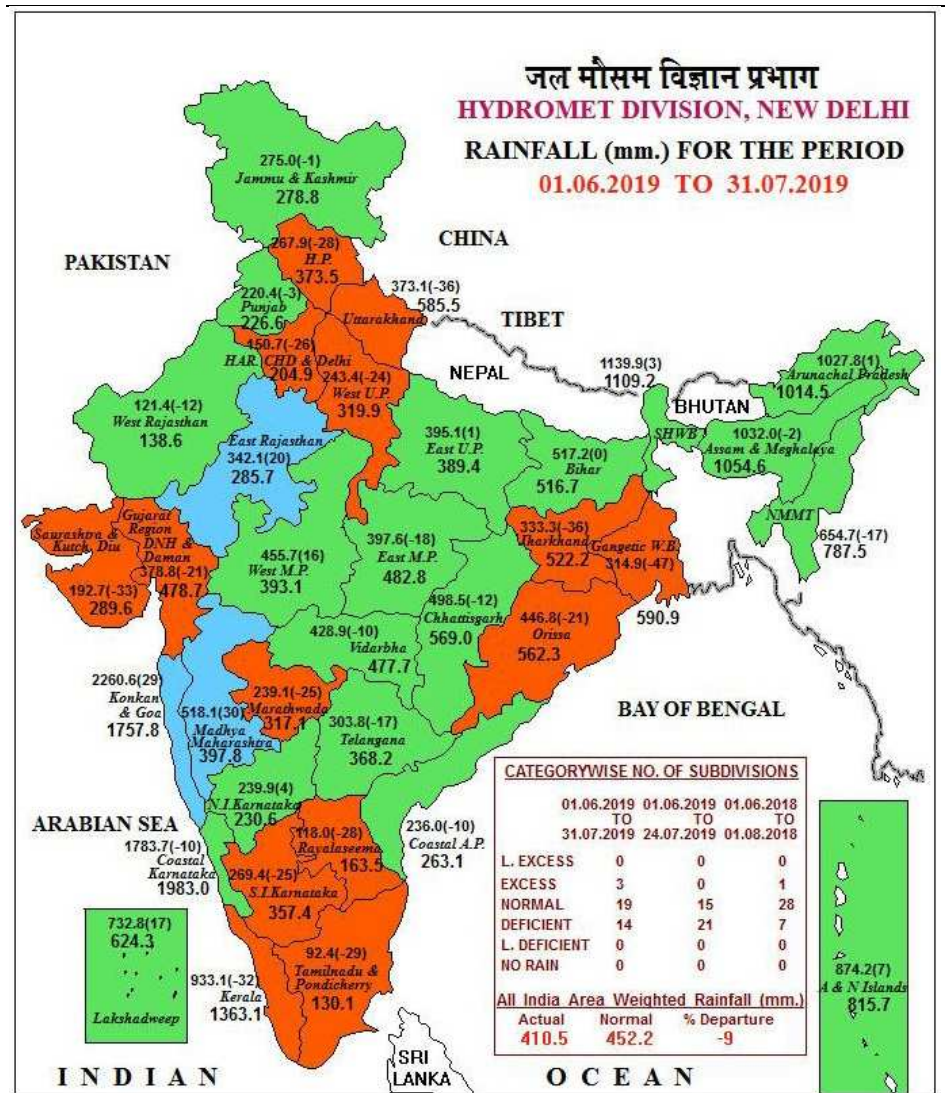
- Bonds:** Global yields closed lower led by US President's tweet on additional 10% tariff on China's imports of US\$ 300bn in addition to 25% tariff on US\$ 250bn of imports. US Fed which reduced policy rate by 25bps may cut further as economy slows. BoJ and BoE also hinted at lower rates. Crude prices declined by (-) 2.5% (US\$ 62/bbl). India's 10Y yield fell by (-) 17bps (6.35%). System liquidity surplus swelled to Rs 2.1tn as on 2 Aug 2019 vs Rs 1.3tn in the previous week.
- Currency:** Except JPY (up by 1.9% on safe haven demand), other global currencies closed lower against the dollar. DXY rose after US Fed signalled that it is unlikely to cut rates. However, with additional tariffs on China, world economy will slow down which may prompt Fed to change its stance later. GBP fell by (-) 1.8% on growing concerns over a no-deal Brexit. INR depreciated by (-) 1% in the week led by FII outflows of US\$ 550mn.
- Equity:** Global equity markets led by Dax and Nikkei, ended the week in red after US President announced 10% additional tariffs on Chinese imports worth US\$ 300bn. Apart from that, weak earnings and softer global manufacturing PMIs also impacted investor sentiments. Sensex fell by (-) 2% owing to muted corporate earnings and global cues.
- Upcoming key events:** Apart from developments on US-China trade war, markets await global services PMI data, China's trade data and Q2 GDP print for UK and Japan this week. Central banks of India, Australia, Thailand and Philippines will deliver their rate decisions. On the domestic front, IIP data is also scheduled to be released this week.



Monsoon Tracker

- For the period 1 Jun 2019 to 4 Aug 2019, monsoon was (-) 7% below LPA same as last year. Till Jul'19, parts of Central India, Eastern region, and J&K have received normal rainfall. Some regions such as Karnataka, Tamil Nadu, parts of North India and Odisha continue to witness deficient rains. However, Eastern Rajasthan and Madhya Maharashtra have been experiencing excess rainfall.
- Overall Kharif sowing dropped by (-) 6.6% as on 2 Aug 2019 compared with last year led by lower sown area of rice (-) 12.5% and cereals (10.2%). Major decline was also visible in pulses (-7.6%) and sugarcane (-5.7%). However, sown area of cotton has improved by 4.9%.

FIG 1 – DISTRIBUTION PATTERN OF SOUTH-WEST MONSOON



LEGEND: ■ L. EXCESS (+60% OR MORE) ■ EXCESS (+20% TO +59%) ■ NORMAL (+19% TO -19%)
 ■ DEFICIENT (-20% TO -59%) ■ L. DEFICIENT (-60% TO -99%) ■ NO RAIN [-100%] ■ NO DATA

Source: IMD, Bank of Baroda Research

India macro developments

- According to data released by DIPAM, in FYTD20 the government has so far collected Rs 124bn through disinvestment vs the budgetary target of Rs 1.05tn. This has been achieved via IPO of Rail Vikas Nigam Ltd. (Rs 5bn), CPSE-ETF (Rs 100bn) and enemy share sale (Rs 19bn). To meet the rest of disinvestment target (Rs 926bn), government is betting on privatisation of Air India, ETFs and strategic sale of almost 59 CPSEs.
- Government has passed the Code on Wages Bill which is expected to benefit over 500mn workers. The bill subsumes 4 labour laws including minimum wages act and equal remuneration act. Through the bill, the tripartite committee including trade unions, employers and state government will decide floor wages for workers across the country. The bill will also universalise provisions of minimum wages and timely payment to all employees, irrespective of wage ceiling and sector.
- Central government's fiscal data shows that it lowered its spending in Q1FY20 to 2% vs 8.7% in Q1FY19. This was led by a sharp contraction in capex growth (-27.6% vs +27.3% in Q1FY19). Centre's net revenue receipts growth also eased to 6.4% in Q1FY20 vs 34.4% last year. Indirect tax collections remain a worry (4% vs 8.5% last year), while direct tax collections are holding ground (9.7% vs 6.2% in Q1FY19).
- Total GST collections for Jun'19 reached Rs 1tn vs Rs 999bn in May'19. This was driven by 14.4% jump in CGST on a YoY basis and 15.2% increase in SGST. However IGST collections fell by (-) 60.4% while cess collections rose by only 0.1%. In Q1FY20, total collections are at Rs 3tn vs Rs 2.9tn in the same period last year (+5.7%). This run rate is however much lower than government's targeted rate of 13.6% for FY20.
- RBI reported that currency in circulation declined by Rs 120bn (on a weekly basis) and stood at Rs 21.7tn as on 26 Jul 2019. Overall reserve money grew by 12.9% on a YoY basis compared to 20.6% a year ago. On FYTD basis, reserve money dropped by (-) 0.1% against (-) 19.9% in the previous year.
- India's core sector growth slumped to 0.2% in Jun'19 from 4.3% in May'19. This was on the back of contraction in petroleum refinery (-9.3% vs -1.5% in May'19), crude oil (-6.8% vs -7% in May'19) and cement output (-1.5% vs 2.8% in May'19). Against this backdrop, IIP growth is expected to be muted for Jun'19.

Global macro developments

- BoJ kept policy rate unchanged with a 7-2 vote, but signalled monetary easing in its statement on the back of downside risks to growth and for maintaining price stability. In a separate print, Japan's industrial output tanked to nearly 1.5 year low of (-) 3.6% in Jun'19 (est.: -1.8%) vs 2% in May'19 on MoM basis, confirming slowdown in line with other economies.
- Consumer confidence in the US rebounded to its 8-month high of 135.7 in Jul'19 (est.: 125) vs 124.3 in Jun'19. Both the current situation and expectation index showed improvement as consumers are optimistic about business and labour market conditions in the near term. However, economic sentiment index in the Euro Area declined by 0.6 points to 102.7 in Jul'19.
- China's official manufacturing PMI indicates that activity contracted for the 3rd month in Jul'19 (49.7 vs 49.4 in Jun'19). This was led by continuous decline in new orders, in particular new export orders (46.9 vs 46.3 in Jun'19), thereby adding pressure on employment as well. Weak domestic demand also led to easing of non-manufacturing activity in Jul'19 (53.7 vs 54.2 in Jun'19).
- US Fed reduced its policy rates by 25bps for the first time since Dec'08 on the back of muted inflation print, weak business spending and concerns of slowdown in global economy. Notably, Fed may not reduce rates any further in CY19 as initially anticipated, since it referred to the rate cut to 'mid-cycle adjustment'. It has also decided to reduce its bonds holding programme, two months ahead of the scheduled date.
- Bank of England (BoE) kept policy rate unchanged at 0.75% in its latest meeting. However, growth forecast has been slashed to 1.3% for both CY19 and CY20 as against 1.5% and 1.6% projected earlier. This has been on the back of muted global growth. Newspaper reports also quoted that BoE sees 33% risk of recession due to Brexit uncertainty.
- Global manufacturing activity contracted further in Jul'19 (49.3 vs 49.4 in Jun'19). Faster contraction was visible across regions-Eurozone (in particular Germany & France), UK and Japan, led by declining new orders. US ISM index too eased marginally in Jul'19 (51.2 vs 51.7 in Jun'19). India however remains a bright spot with PMI at 52.5 vs 52.1 in Jun'19, led by revival in factory orders, raw material purchases and job creation.
- US unemployment data showed non-farm payroll increased by 164,000 in Jul'19 (est.: 164,000) vs 224,000 in Jun'19. Average hourly earnings rose by 0.3% in Jul'19 on MoM basis vs 0.2% in Jun'19. Labour force participation rate increased to 63% and unemployment rate was at 3.7% in Jul'19. In a separate print, US factory orders rose by 0.6% in Jun'19 vs (-) 1.3% in May'19 boosted by demand for machinery and transportation equipment.

FIG 2 – MOVEMENT IN KEY GLOBAL ASSET CLASSES

Particulars	Current	1W	1M	3M	12M
10Y yields (Δ bps)					
US	1.85	(23)	(13)	(68)	(110)
UK	0.55	(14)	(17)	(67)	(78)
Japan	(0.16)	(2)	(2)	(12)	(27)
Germany	(0.50)	(12)	(13)	(52)	(90)
India	6.35	(17)	(49)	(104)	(141)
China	3.10	(7)	(7)	(30)	(36)
2Y yields (Δ bps)					
US	1.71	(14)	(5)	(62)	(93)
UK	0.44	(5)	(9)	(36)	(31)
Japan	(0.20)	1	1	(5)	(9)
Germany	(0.79)	(4)	(3)	(20)	(20)
India	5.95	(14)	(30)	(82)	(154)
China	2.55	(4)	(5)	(12)	(22)
Currencies (Δ %)					
EUR	1.108	(0.2)	(1.6)	(0.8)	(4.0)
GBP	1.2162	(1.8)	(3.4)	(7.7)	(6.5)
JPY	106.59	1.9	1.2	4.1	4.2
AUD	0.6801	(1.6)	(2.8)	(3.1)	(8.1)
INR	69.61	(1.0)	(1.0)	(0.6)	(1.5)
CNY	6.9405	(0.9)	(1.0)	(3.1)	(1.7)
Equity & Other indices (Δ %)					
Dow	26,485	(2.6)	(1.1)	(0.1)	4.0
FTSE	7,407	(1.9)	(2.0)	0.4	(3.3)
DAX	11,872	(4.4)	(5.2)	(4.4)	(5.9)
NIKKEI	21,087	(2.6)	(3.1)	(5.3)	(6.4)
Shanghai Comp	2,868	(2.6)	(5.8)	(6.8)	4.6
SENSEX	37,118	(2.0)	(6.8)	(4.7)	(1.2)
Brent (US\$/bbl)	61.89	(2.5)	(0.8)	(12.6)	(15.5)
Gold (US\$/oz)	1,441	1.5	1.6	12.6	18.6
CRB Index	400.4	(1.4)	(0.8)	(4.4)	(6.3)
Rogers Agri Index	710.7	(3.2)	(4.2)	(1.4)	(13.0)
LIBOR (3M)*	2.29	2	(3)	(27)	(6)
INR 5Y Swap*	6.56	(6)	(18)	(68)	(108)
India FII data (US\$ mn)					
	1 Aug	WTD	MTD	CYTD	FYTD
FII-Debt	(159.2)	(16.1)	(159.2)	2,494.8	1,950.2
FII-Equity	(169.0)	(534.3)	(169.0)	9,235.7	2,390.5

Source: Bloomberg, Bank of Baroda Research | *Indicates change in bps

FIG 3 – DATA RELEASE CALENDAR

Date	Event	Period	Estimate	Previous	Actual
5-Aug	Jibun Bank Japan services PMI	Jul	--	52.3	--
	Caixin China services PMI	Jul	52.0	52.0	--
	Markit India services PMI	Jul	--	49.6	--
	Markit Spain services PMI	Jul	53.6	53.6	--
	Markit Italy services PMI	Jul	50.6	50.5	--
	Markit France services PMI	Jul	52.2	52.2	--
	Markit Germany services PMI	Jul	55.4	55.4	--
	Markit Eurozone services PMI	Jul	53.3	53.3	--
	Markit/CIPS UK services PMI	Jul	50.3	50.2	--
	Markit US services PMI	Jul	52.2	52.2	--
	ISM non-manufacturing index	Jul	55.5	55.1	--
6-Aug	S. Korea BoP current account balance, US\$ bn	Jun	--	4.9	--
	Australia trade balance, AUD bn	Jun	6.0	5.7	--
	Reserve Bank of Australia monetary policy rate, %	6-Aug	1.0%	1.0%	--
	Germany factory orders, % MoM	Jun	0.5%	(2.2%)	--
	Taiwan CPI, % YoY	Jul	0.9%	0.9%	--
7-Aug	Germany industrial production, SA, % MoM	Jun	(0.5%)	0.3%	--
	RBI policy rate, %	7-Aug	5.50%	5.75%	--
	France trade Balance, EUR bn	Jun	(4.1)	(3.3)	--
	Bank of Thailand benchmark interest rate, %	7-Aug	1.75%	1.75%	--
	Taiwan exports, % YoY	Jul	1.0%	0.5%	--
8-Aug	Japan BoP current account balance, ¥ tn	Jun	1.2	1.6	--
	Philippines GDP, % YoY	Q2CY19	5.9%	5.6%	--
	Bank of France industrial sentiment index	Jul	96.0	95.0	--
	Bank of Philippines (BSP) overnight borrowing rate, %	8-Aug	4.25%	4.50%	--
	US initial jobless claims	3-Aug	215,000	215,000	--
	US wholesale inventories, % MoM	Jun	0.2%	0.2%	--
	China exports, % YoY	Jul	(0.2%)	(1.3%)	--
9-Aug	Japan GDP, annualized SA, % QoQ	Q2CY19	0.6%	2.2%	--
	China CPI, % YoY	Jul	2.7%	2.7%	--
	China PPI, % YoY	Jul	0.0%	0.0%	--
	Germany exports, SA, % MoM	Jun	0.0%	1.1%	--
	France industrial production, % MoM	Jun	(1.2%)	2.1%	--
	UK GDP, % QoQ	Q2CY19	0.0%	0.5%	--
	UK industrial production, % MoM	Jun	(0.2%)	1.4%	--
	India industrial production, % YoY	Jun	--	3.1%	--
	US PPI final demand, % MoM	Jul	0.2%	0.1%	--

Source: Bloomberg, Bank of Baroda Research

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