

WEEKLY WRAP

21 January 2019

US-China trade talks to steer markets

Progress on US-China trade deal lifted global markets. Global equity markets and yields rallied and dollar rose for the first time in 4 weeks. However, growth concerns continue as China's exports fell and GDP moderated further in Q4. Indian yields also rose, even as retail inflation cooled-off in Dec'18 to 18-month low. Higher crude prices and anticipation of an expansionary budget drove yields higher. INR depreciated by (-) 1% amidst FII outflows (US\$ 256mn). As Budget draws nearer (1-Feb), noise on rural stimulus will increase further.

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Markets

- Bonds:** Except Japan and China, global yields closed higher. This was driven by 3.7% jump in crude prices (US\$ 63/bbl) as well as optimism over progress on US-China trade talks. US 10Y yield shot up by 8bps (2.78%). Economic data was also supportive with robust manufacturing production. Indian 10Y yield inched up by 10bps (7.60%) as fiscal concerns prevailed over anticipation of a large stimulus for the farm sector. System liquidity was in deficit of Rs 428bn vs Rs 108bn in the previous week.
- Currency:** Barring GBP, other global currencies closed lower as dollar rebounded to end the week higher by 0.7%. This was the first weekly gain after four weeks led by progress on US-China trade deal. GBP ended higher by 0.2% on hopes that a no-deal Brexit seemed like the most improbable scenario. INR depreciated by 1% in the week on the back of higher oil prices (3.7%) and FII outflows (US\$ 256mn).
- Equity:** Riding on the wave of optimism over the ongoing trade negotiations between US and China, global indices edged higher. Dow surged by 3% followed by Dax (2.9%) and Shanghai Comp (1.7%). European markets rose, despite uncertainty over Brexit. Sensex too gained by 1% on the back of stronger global cues.
- Upcoming key events:** Apart from monetary policy decision of BoJ and ECB, global manufacturing PMIs, US new home sales and trade balance data will be released. Apart from this, progress on US-China trade talks, China's retail sales, industrial production and GDP data will drive markets. Given the lukewarm growth in Europe, consumer confidence in Euro Area and Germany's PPI and ZEW survey will be closely monitored.



India macro developments

- Both CPI (2.19% vs 2.33% in Nov'18) and WPI inflation (3.8% vs 4.6% in Nov'18) cooled off further in Dec'18. While the drop in WPI inflation was led by lower fuel and power inflation (8.4% vs 16.3%), continued deflation in food prices (-2.5% in Dec'18) dragged CPI down. With CPI inflation significantly undershooting RBI's trajectory and inflationary pressures remaining muted, we believe RBI is likely to change its stance next month.
- India's trade deficit narrowed to US\$ 13.1bn in Dec'18 (US\$ 16.7bn in Nov'18) on account of decline in imports (-2.4%), a first in 27-months. The fall was led by (-) 24.3% decline in gold imports as well as non-oil-non-gold imports at (-) 1.9%. Exports too registered near flat growth of 0.4% with a broad-based slowdown. With a benign global outlook, exports are likely to remain muted. We expect CAD at 2.5% of GDP in FY19.
- RBI reported that currency in circulation (CIC) increased by Rs 255bn (on a weekly basis) and stood at Rs 21tn as on 11 Jan 2019. Overall reserve money grew by 16.8% on a YoY basis compared to 55.2% a year ago. On FYTD basis, reserve money is growing at a slower pace of 7.7% against 17.3% in the previous year.
- According to news reports, government is likely to allocate additional sum of Rs 60.8bn to MGNREGA, thereby taking the total allocation to Rs 610.8bn in FY19. Over 99% of the allocation has already been utilized and with Rs 904bn of pending liability from last year. Separately, India is also likely to overshoot its fertilizer subsidy bill in FY19 to Rs 1tn (vs BE Rs 700bn) owing to expensive imported fertilizers and previous unsettled dues.
- Number of beneficiaries under PM-Rashtriya Rozgar Prothshahan Yojna has crossed the 10mn mark. The scheme launched in 2016, aimed at providing new employment opportunities by incentivizing employers. This is done through government paying full contribution of 12% wages towards EPF. Over 1.24 lakh establishments have benefited from this scheme till date.
- India's FX reserves for the week ending 11 Jan 2019 rose to US\$ 397bn. On a weekly basis, forex reserves rose by US\$ 1.3bn, lower than an increase of US\$ 2.7bn last week. However, on FYTD basis, reserves are down by US\$ 27bn, compared with an accretion of US\$ 43.9bn in the same period last year.

Global macro developments

- China's Q4CY18 GDP growth eased to 6.4% vs 6.5% in Q3, taking the CY18 growth down to 6.6% (lowest since CY90) from a downwardly revised 6.8% in CY17. In the wake of lower growth, industrial production (IP) and retail sales data for Dec'18 surprised positively, indicating support from front-loading of exports. IP rose by 5.7% in Dec'18 vs 5.4%, while retail sales rose by 8.2% in Dec'18 vs 8.1% in Nov'18. Overall, the data represents a soft landing for China's economic growth rather than a hard landing.
- Industrial production in both the Euro Area and EU28 declined by (-) 1.7% & (-) 1.3% respectively in Nov'18 vs 0.1% increase seen in Oct'18. There was broad based decline in all categories such as capital and consumer goods, yet again confirming that global growth picture is showing signs of stress. Within EA, Ireland, Portugal and Germany registered the largest decline.
- US industrial production rose by 0.3% in Dec'18 on a MoM basis, vs 0.4% in Nov'18. The increase in mining and manufacturing production offset the fall in utilities, resulting in higher industrial production. Within this, manufacturing production rose to 10-month high of 1.1%, biggest gain since Feb'18. This was led by jump in production of motor vehicles as it surged by 4.7% in Dec'18 from 0.2% in Nov'18.
- China's exports in Dec'18 fell by (-) 4.4%, vs est.: 2% and 5.4% in Nov'18. Its imports also contracted more than expected (-7.6% in Dec'18 vs 3% in Nov'18). As a result, while its trade surplus rose to US\$ 57.1bn in Dec'18 (US\$ 44.8bn in Nov'18), for CY18 total surplus declined to US\$ 357bn, the lowest since CY13. Despite fears of slowing economy, China continued to attract FDI in CY18 (+3%, US\$135bn).
- Germany's GDP in CY18 rose by 1.5% vs 2.2% in the previous 2 years. This is slowest rate of growth since CY13 (0.5%). This was led by slowdown in exports & consumption demand. With these numbers, it is now assumed that German economy recorded near flat growth (0%) in Q4CY18. Led by recent trade wars and slowdown in China, German corporates' profits have taken a serious hit, thus putting the economy on a weaker footing in CY19.
- New home sale prices in China recorded weakest MoM gain in 8 months in Dec'18 (0.8% vs 0.9% in Nov'18). This was led by lower prices in tier-3 cities. Number of cities reporting rise in prices also fell, from 63 in Nov'18 to 59 in Dec'18, out of a total of 70 cities surveyed. On YoY basis, real estate price growth was robust at 9.7% in Dec'18 vs 5.4% in Dec'17.

FIG 1 – MOVEMENT IN KEY GLOBAL ASSET CLASSES

| Particulars | Current | 1W | 1M | 3M | 12M |
|---|---------------|------------|------------|-------------|-------------|
| 10Y yields (Δ bps) | | | | | |
| US | 2.78 | 8 | 3 | (41) | 13 |
| UK | 1.35 | 6 | 8 | (22) | 2 |
| Japan | 0.02 | 0 | (2) | (13) | (7) |
| Germany | 0.26 | 2 | 2 | (20) | (31) |
| India | 7.60 | 10 | 38 | (32) | 31 |
| China | 3.11 | (2) | (26) | (47) | (87) |
| 2Y yields (Δ bps) | | | | | |
| US | 2.61 | 7 | (3) | (29) | 55 |
| UK | 0.81 | 0 | 8 | 1 | 25 |
| Japan | (0.17) | (2) | (2) | (5) | (4) |
| Germany | (0.58) | 1 | 2 | 0 | 2 |
| India | 7.03 | 3 | 15 | (60) | 18 |
| China | 2.60 | (3) | (13) | (54) | (98) |
| Currencies (Δ %) | | | | | |
| EUR | 1.1363 | (0.9) | (0.1) | (1.3) | (7.0) |
| GBP | 1.2872 | 0.2 | 2.1 | (1.6) | (7.1) |
| JPY | 109.78 | (1.2) | 2.4 | 2.5 | 0.9 |
| AUD | 0.7168 | (0.7) | 0.8 | 0.7 | (10.3) |
| INR | 71.19 | (1.0) | (1.1) | 2.9 | (11.5) |
| CNY | 6.7778 | (0.2) | 1.6 | 2.2 | (5.8) |
| Equity & Other indices (Δ %) | | | | | |
| Dow | 24,706 | 3.0 | 5.9 | (2.9) | (5.2) |
| FTSE | 6,968 | 0.7 | 3.0 | (1.2) | (9.9) |
| DAX | 11,206 | 2.9 | 4.1 | (3.0) | (16.6) |
| NIKKEI | 20,666 | 1.5 | (1.5) | (8.3) | (13.2) |
| Shanghai Comp | 2,596 | 1.7 | 1.8 | 1.8 | (25.6) |
| SENSEX | 36,387 | 1.0 | (0.3) | 6.0 | 2.5 |
| Brent (US\$/bbl) | 62.70 | 3.7 | 9.5 | (21.4) | (8.6) |
| Gold (US\$/oz) | 1,282 | (0.6) | 3.1 | 4.5 | (3.7) |
| CRB Index | 414.0 | 0.7 | 0.3 | (0.6) | (5.3) |
| Rogers Agri Index | 776.4 | 0.6 | 0.5 | (1) | (4.6) |
| LIBOR (3M)* | 2.78 | (2) | (1) | 30 | 103 |
| INR 5Y Swap* | 7.21 | 1 | 7 | (49) | 40 |
| India FII data (US\$ mn) | | | | | |
| | 17 Jan | WTD | MTD | CYTD | FYTD |
| FII-Debt | (39.8) | (299.8) | (347.9) | (347.9) | (7,338.5) |
| FII-Equity | 125.0 | 43.4 | (283.5) | (283.5) | (6,966.3) |

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

FIG 2 – DATA RELEASE CALENDAR

| Date | Event | Period | Estimate | Previous | Actual |
|------------------------------|--|--|-----------|-----------|--------|
| 21-Jan | China retail sales, % YoY | Dec | 8.1% | 8.1% | 8.2% |
| | China industrial production, % YoY | Dec | 5.3% | 5.4% | 5.7% |
| | China fixed assets ex rural YTD, % YoY | Dec | 6.0% | 5.9% | 5.9% |
| | China GDP, % YoY | Q4CY18 | 6.4% | 6.5% | 6.4% |
| | Germany PPI, % YoY | Dec | 2.9% | 3.3% | -- |
| 22-Jan | South Korea GDP, % YoY | Q4CY18 | 2.3% | 2.0% | -- |
| | Germany ZEW survey current situation | Jan | 43.3 | 45.3 | -- |
| | Euro area ZEW survey expectations | Jan | -- | (21.0) | -- |
| | US existing home sales, mn | Dec | 5.2 | 5.3 | -- |
| 23-Jan | Japan trade balance, ¥ bn | Dec | (35.3) | (737.3) | -- |
| | Japan machine tool orders, % YoY | Dec | -- | (18.3%) | -- |
| | France manufacturing confidence | Jan | 103.0 | 104.0 | -- |
| | Euro area consumer confidence | Jan | (6.5) | (6.2) | -- |
| | BOJ Policy Balance Rate | Jan | -- | (0.1%) | -- |
| | US new home sales | Nov | 567,000 | 544,000 | -- |
| | US factory orders | Nov | 0.3% | (2.1%) | -- |
| | US trade balance, US\$ bn | Nov | (54.0) | (55.5) | -- |
| | US retail sales advance, % MoM | Dec | 0.1% | 0.2% | -- |
| | US housing starts | Dec | 1,253,000 | 1,256,000 | -- |
| 24-Jan | Nikkei Japan manufacturing PMI | Jan | -- | 52.6 | -- |
| | Philippines GDP, % YoY | Q4CY18 | 6.2% | 6.1% | -- |
| | Markit France manufacturing PMI | Jan | 50.0 | 49.7 | -- |
| | Markit France services PMI | Jan | 50.5 | 49.0 | -- |
| | Markit Germany manufacturing PMI | Jan | 51.5 | 51.5 | -- |
| | Markit Germany services PMI | Jan | 52.2 | 51.8 | -- |
| | Markit Eurozone manufacturing PMI | Jan | 51.3 | 51.4 | -- |
| | Markit Eurozone services PMI | Jan | 51.5 | 51.2 | -- |
| | ECB Main Refinancing Rate | Jan | 0.0% | 0.0% | -- |
| | US initial jobless claims | 19-Jan | 219,000 | 213,000 | -- |
| | Markit US manufacturing PMI | Jan | 53.5 | 53.8 | -- |
| | Markit US services PMI | Jan | 53.9 | 54.4 | -- |
| | BoK 7-Day Repo Rate | Jan | 1.8% | 1.8% | -- |
| | 25-Jan | Singapore industrial production, % YoY | Dec | 4.4% | 7.6% |
| Germany IFO business climate | | Jan | 100.6 | 101.0 | -- |
| US durable goods orders | | Dec | 1.5% | -- | -- |
| US new home sales | | Dec | 563,000 | -- | -- |

Source: Bloomberg, Bank of Baroda Research

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