

WEEKLY WRAP

16 March 2020

RBI likely to ease by 50bps

In a surprise move, US Fed reduced policy rate by 1% and announced US\$ 700bn of bond purchases. US yields are likely to open lower. So is the case with equity markets. Data released from China shows retail sales falling by (-) 21%, industrial production by (-) 14% and fixed assets by (-) 25%. With most global economies now going into some form of quarantine, economic impact is likely to play out in Q2CY20. We see RBI cutting rates by 50bps in Apr'20 policy along with measures to boost durable liquidity.

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Markets

- **Bonds:** Asian yields have opened lower after a surprise 1% rate cut by US Fed. RBNZ too reduced rates by 50bps. US 10Y futures are trading lower at 0.67%. Among other central banks, BoE, ECB and PBOC too infused liquidity over the week. Oil prices fell sharply in the week by (-) 25% (US\$ 34/bbl) as Saudi Arabia and UAE exerted downward pressure on prices. India's 10Y yield is trading lower by 10bps today, following Fed action. System liquidity surplus was at Rs 2.7tn as on 13 Mar 2020 vs Rs 3tn in the previous week.
- **Currency:** DXY rose by 2.8% last week after falling to a 1-year low. Global currencies closed lower on the back of risk-off. AUD depreciated by (-) 6.5% in the week. INR also fell by (-) 0.2% on the back of FII outflows (US\$ 3bn). Despite US Fed cutting rates by 1%, Asian currencies are trading mixed today. JPY is trading higher today by 0.5%.
- **Equity:** Global equity indices fell last week as investors assess economic impact of COVID-19. Dax (-20%) slumped the most followed by FTSE (-17%) and Nikkei (-16%). Though US markets closed 9% up on Friday, US futures are trading at lower circuit even as Fed surprised with 1% rate cut on Sunday. Sensex fell by (-) 9.2% last week and is trading 5% lower today. Real estate and tech stocks were the worst affected.
- **Upcoming key events:** In the current week, markets will closely watch policy decisions by BoJ, Indonesia, Philippines, Taiwan and incoming data such as US existing home sales, advance retail sales and Germany's economic expectation survey.



India macro developments

- As per news reports, government may bring down the tax rate on dividend income for domestic investors from 43% to 20% in the highest tax bracket. Foreign investors on the other hand, are currently taxed between 5-15% on dividends depending on the tax treaty. The move is likely to create a level playing field for both domestic and foreign investors.
- RBI bought net US\$ 10.3bn in Jan'20 in the spot market (highest in 5 years) vs US\$ 4.4bn in Dec'19. In FYTD20, RBI has purchased US\$ 40bn in the spot market vs net sales of US\$ 25.6bn last year. In the forwards market, RBI purchased US\$ 0.7bn vs US\$ 4.3bn in Dec'19. RBI's net outstanding forward position is at (-) US\$ 1.2bn vs (-) 3bn in Jan'19.
- RBI reported that currency in circulation (CIC) declined by Rs 95bn and stood at Rs 23.5tn for the week ending 28 Feb 2020. Reserve money rose by 11.6% on a YoY basis, compared with 15.6% a year ago. On a FYTD basis, reserve money increased by 7.4% as against 10.2% last year.
- CPI inflation in India edged down to 6.6% in Feb'20 (7.6% in Jan'20) led by moderation in prices of vegetables and fruits. Core also fell by 10bps to 4.1% due to fall in retail fuel prices. While industrial output rebounded to 2% in Jan'20, we expect domestic economic activity to decelerate on the back of supply and demand disruption because of COVID-19. The current growth-inflation mix calls for 25-40bps cut in policy rate.
- India's CAD fell to US\$ 1.4bn (0.2% of GDP) in Q3FY20 from US\$ 6.5bn in Q2FY20 (0.9% of GDP) on the back of lower trade deficit. Sharp increase in FPI inflows in Q3 led to BoP surplus of US\$21.6bn vs US\$ 5.1bn in Q2. We expect CAD at 0.6% in FY21.
- GST council has hiked rates on mobile phones to 18% from 12%, in order to correct the inverted duty structure. To improve compliance burden and give relief to small businesses, deadline for GSTR-9C has been relaxed and late fee for delayed filing has been waived off (> turnover less than Rs 20mn). In addition, excise duty has been hiked by Rs 3/l on diesel and petrol. This is expected to bring an additional revenue of Rs 390bn for the government (0.2% of GDP).
- India's trade deficit narrowed to US\$ 9.9bn in Feb'20 from US\$ 15.2bn in Jan'20 as oil, electronic and capital goods imports came-off on MoM basis. Exports rose by 2.9% in Feb'20 versus (-) 1.7% decline in Jan'20 led by higher engineering goods and chemicals. Imports increased by 2.5% in Feb'20 vs (-) 0.7% in Jan'20. Oil imports rose by 14.3% in Feb'20 (15.3% in Jan'20). Non-oil-non-gold imports fell by (-) 0.9% in Feb'20 vs (-) 5.8% in FYTD20, indicating economic growth has bottomed out.

Global macro developments

- US Fed has slashed its interest rate to 0-0.25% from 1-1.25% earlier, due to expected disruption in financial and economic activity from COVID-19. Fed would also purchase US\$ 700bn treasury bonds and mortgage-backed securities. It also issued a coordinated statement along with Bank of Canada, BoE, BoJ, ECB and Swiss National Bank to enhance liquidity by lowering the pricing on US dollar liquidity swap arrangements by 25 bps.
- BoE has cut policy rate (Bank rate) by 50bps to 0.25%, on the back of downside risks to growth. It has also announced couple of measures to combat economic shock emanating from COVID-19. New term-funding scheme has been introduced to support SMEs. Further to boost lending by commercial banks, UK countercyclical capital buffer has been reduced to 0% for at least 12-months from the current requirement of 1%.
- Against consensus estimate of 10bps reduction in policy rate, ECB kept policy rate unchanged. However, it announced measures to support banks for lending and increase its asset purchase program by €120bn. To support lending, European banks will be able to borrow from ECB at (-) 0.75%, lower than (-) 0.5% deposit rate. With ECB's interest rates already in the negative territory, the scope for further lowering of rates is limited.
- PBOC has reduced the RRR by 50bps for 6 bigger banks and by 100bps for other banks. This will bring the RRR down to 12% for large banks and is expected pump in overall liquidity amounting to 550bn Yuan (US\$ 79bn). Of this, ~400bn Yuan is expected to be lent to smaller firms. In the coming days, analysts also expect cuts in 7D-reverse repo, MLF and LPR
- China's PPI fell by (-) 0.4% in Feb'20 vs est.: (-) 0.3% and 0.1% increase in Jan'20. Sharp decline in global commodity prices led by muted demand (COVID-19) was a drag. Headline CPI also eased marginally to 5.2% in Feb'20 from 5.4% in Jan'20. The elevated levels are mainly owing to higher food inflation, and hygiene materials. Core inflation is down to 10-year low of 1%, as demand cools off further.
- Euro Area's GDP slowed to 0.1% in Q4CY19 from 0.3% in Q3CY19. Household final consumption expenditure rose by 0.1% vs 0.5% and exports decelerated by 0.4% vs 0.6% for the same period. For CY19, seasonally adjusted GDP was up 1.2% compared with 1.9% growth seen in CY18. Employment levels also rose at a slow pace (1.2% vs 1.5%) in CY19.
- US CPI rose by 0.1% in Feb'20 (est.: 0%), unchanged from Jan'20. Downward pressure from falling energy prices (-2% vs -0.7%) was offset by higher prices of food (0.4% vs 0.2%) and autos (0.4% vs -1.2%). Core inflation remained unchanged in Feb'20 at 0.2%. On a YoY basis, it is up at 2.4% vs 2.3% in Jan'20, with pressures visible in goods more than services.

FIG 1 – MOVEMENT IN KEY GLOBAL ASSET CLASSES

Particulars	Current	1W	1M	3M	12M
10Y yields (Δ bps)					
US	0.96	20	(67)	(86)	(163)
UK	0.41	18	(20)	(38)	(80)
Japan	0.05	18	9	7	9
Germany	(0.54)	17	(17)	(26)	(63)
India	6.32	14	(15)	(46)	(102)
China	2.69	6	(15)	(51)	(46)
2Y yields (Δ bps)					
US	0.49	(2)	(95)	(111)	(195)
UK	0.29	19	(24)	(25)	(47)
Japan	(0.19)	9	(4)	(6)	(4)
Germany	(0.87)	(1)	(24)	(25)	(33)
India	5.51	17	(25)	(27)	(108)
China	1.96	(34)	(33)	(65)	(45)
Currencies (Δ %)					
EUR	1.1107	(1.6)	2.1	(0.1)	(1.9)
GBP	1.2278	(5.9)	(5.3)	(7.9)	(7.6)
JPY	107.62	(2.1)	2.2	1.6	3.5
AUD	0.6203	(6.5)	(7.9)	(9.8)	(12.4)
INR	73.90	(0.2)	(3.6)	(4.4)	(7.0)
CNY	7.0086	(1.1)	(0.5)	(0.5)	(4.4)
Equity & Other indices (Δ %)					
Dow	23,186	(10.4)	(21.5)	(17.6)	(10.3)
FTSE	5,366	(17.0)	(28.8)	(27.0)	(25.8)
DAX	9,232	(20.0)	(32.9)	(30.5)	(21.0)
NIKKEI	17,431	(16.0)	(26.9)	(27.4)	(18.7)
Shanghai Comp	2,887	(4.8)	(1.3)	(2.7)	(4.4)
SENSEX	34,103	(9.2)	(18.0)	(16.8)	(10.3)
Brent (US\$/bbl)	33.85	(25.2)	(39.3)	(48.1)	(49.6)
Gold (US\$/oz)	1,530	(8.6)	(2.3)	3.6	17.5
CRB Index	387.4	(2.8)	(3.7)	(2.2)	(7.7)
Rogers Agri Index	669.1	(4.5)	(9.6)	(9.5)	(11.6)
LIBOR (3M)*	0.84	(5)	(86)	(106)	(178)
INR 5Y Swap*	5.67	(7)	(86)	(93)	(100)
India FII data (US\$ mn)					
	12 Mar	WTD	MTD	CYTD	FYTD
FII-Debt	(403.0)	(1,355.8)	(1,602.4)	(3,169.5)	(225.4)
FII-Equity	(243.0)	(1,663.1)	(2,909.5)	(1,122.6)	6,266.6

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

FIG 2 – DATA RELEASE CALENDAR

Date	Event	Period	Estimate	Previous	Actual
16-Mar	Central Bank of New Zealand policy rate, %	16-Mar	--	1.0%	0.3%
	US Fed policy rate, %	15-Mar	--	1.0%	0.0%
	Japan core machine orders, % MoM	Jan	(1.0%)	(12.5%)	2.9%
	China new home prices, % MoM	Feb	--	0.3%	0.0%
	China retail sales YTD, % YoY	Feb	(4.0%)	--	(20.5%)
	China industrial production YTD, % YoY	Feb	(3.0%)	--	(13.5%)
	China fixed assets ex rural YTD, % YoY	Feb	(2.0%)	--	(24.5%)
	India WPI, % YoY	Feb	2.4%	3.1%	--
	Bank of Japan policy rate, %	16-Mar	(0.1%)	(0.1%)	--
17-Mar	Singapore non-oil domestic exports, % YoY	Feb	(6.9%)	(3.3%)	--
	RBA minutes of March policy meeting	--	--	--	--
	Japan industrial production, % MoM	Jan	--	0.8%	--
	UK jobless claims change	Feb	--	5,500	--
	Germany ZEW survey expectations	Mar	(27.2)	8.7	--
	US retail sales advance, % MoM	Feb	0.2%	0.3%	--
18-Mar	Japan exports, % YoY	Feb	(4.2%)	(2.6%)	--
	Euro Area CPI, % YoY	Feb	1.2%	1.2%	--
	US housing starts, in mn	Feb	1.5	1.6	--
19-Mar	New Zealand GDP SA, % QoQ	Q4CY19	0.5%	0.7%	--
	Japan CPI, % YoY	Feb	0.5%	0.7%	--
	Australia unemployment rate, %	Feb	5.30%	5.30%	--
	Central Bank of Indonesia policy rate, %	19-Mar	4.63%	4.75%	--
	Central Bank of Philippines policy rate, %	19-Mar	3.50%	3.75%	--
	US initial jobless claims	19-Mar	2,19,000	2,11,000	--
	Central Bank of Taiwan policy rate, %	19-Mar	1.4%	1.4%	--
20-Mar	South Korea PPI, % YoY	Feb	--	1.0%	--
	Germany PPI, % MoM	Feb	(0.2%)	0.8%	--
	Taiwan export orders, % YoY	Feb	0.7%	(12.8%)	--
	Euro Area current account SA, € bn	Jan	--	32.6	--
	US existing home sales, in mn	Feb	5.5	5.5	--

Source: Bloomberg, Bank of Baroda

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