

RESEARCH

BOB Economics Research | Balance of Payments

CAD expands in Q1, but will moderate

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Adherence to borrowing glide path implies lower yields

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RBI policy and H2 borrowing to drive yields

SUMMARY

India Economics: Balance of Payments

Despite an increase in CAD to US\$ 14.3bn in Q1 from US\$ 4.6bn in Q4, India's BoP surplus remained stable at US\$ 14bn. Higher FDI inflows and reduction in banking capital outflows explains this. Going ahead, we expect FDI inflows to remain resilient and trade deficit to moderate as domestic demand is subdued. Lower oil prices will also ensure decline in trade deficit in FY20 to US\$ 170bn from US\$ 180bn in FY19. The above backdrop is positive for INR and we expect it to remain in 70-72/\$ range with an appreciation bias.

[Click here for the full report.](#)

India Economics: Interest Rate Outlook

Centre has maintained its guidance of gross borrowings at Rs 7.1tn in FY20. Net borrowing in H2 is estimated at Rs 1.33tn. Notably, >10 year issuances in H2 are at 75.4% (42% outstanding) thus implying continuous bias for a steeper yield curve. The government today announced disinvestment including 100% stake sale in certain CPSEs. This will meet any revenue shortfall. For driving growth higher, we expect fiscal deficit at 3.5% of GDP in FY20 and inflows from small savings schemes to support the same.

[Click here for the full report.](#)

TOP PICKS

LARGE-CAP IDEAS

Company	Rating	Target
Cipla	Buy	555
GAIL	Buy	200
ONGC	Buy	200
TCS	Add	2,360
HPCL	Sell	200

MID-CAP IDEAS

Company	Rating	Target
Alkem Labs	Buy	2,230
Future Supply	Buy	730
Greenply Industries	Buy	200
Laurus Labs	Buy	480
PNC Infratech	Buy	250

Source: BOBCAPS Research

DAILY MACRO INDICATORS

Indicator	Current	2D (%)	1M (%)	12M (%)
US 10Y yield (%)	1.68	(1bps)	19bps	(137bps)
India 10Y yield (%)	6.74	2bps	18bps	(129bps)
USD/INR	70.56	0.4	1.7	2.8
Brent Crude (US\$/bbl)	61.91	(1.3)	1.4	(24.2)
Dow	26,820	(0.3)	1.7	1.4
Shanghai	2,932	0.1	1.4	5.0
Sensex	38,823	(0.4)	4.7	6.9
India FII (US\$ mn)	26 Sep	MTD	CYTD	FYTD
FII-D	(205.7)	(106.6)	4,140.6	3,596.0
FII-E	1,569.8	1,039.6	8,245.6	1,400.4

Source: Bank of Baroda Economics Research

BOBCAPS Research

research@bobcaps.in



India Economics: Weekly Wrap

Global manufacturing activity weakened further in Sep'19, especially in the Eurozone. In addition, US consumer confidence fell. With Mexico and Philippines reducing rates, global yields closed lower in the week. Oil prices fell by (-) 3.7% as Saudi output resumed. This supported Indian yields. Announcement of corporate tax cut helped lift Sensex and robust FII inflows supported INR. Government's H2 borrowing calendar and RBI policy meet will set the tone for the markets this week. We expect 25bps rate cut.

[Click here](#) for the full report.

BALANCE OF PAYMENTS

30 September 2019

CAD expands in Q1, but will moderate

Despite an increase in CAD to US\$ 14.3bn in Q1 from US\$ 4.6bn in Q4, India's BoP surplus remained stable at US\$ 14bn. Higher FDI inflows and reduction in banking capital outflows explains this. Going ahead, we expect FDI inflows to remain resilient and trade deficit to moderate as domestic demand is subdued. Lower oil prices will also ensure decline in trade deficit in FY20 to US\$ 170bn from US\$ 180bn in FY19. The above backdrop is positive for INR and we expect it to remain in 70-72/\$ range with an appreciation bias.

Sameer Narang

Aditi Gupta | Jahnvi

chief.economist@bankofbaroda.com

CAD expands to 2% of GDP in Q1FY20: Led by a higher trade deficit, India's CAD expanded to US\$ 14.3bn in Q1FY20 from US\$ 4.6bn in Q4FY19. Trade deficit in Q1FY20 increased to US\$ 46.2bn (6.6% of GDP) from US\$ 35.2bn (4.9% of GDP) in Q4FY19 led by higher oil and gold imports. Merchandise exports too declined. Services receipts moderated from US\$ 21.3bn in Q4FY19 to US\$ 20bn in Q1FY20 even as software services receipts were higher. Remittances too rose to US\$ 18bn compared with US\$ 16.2bn in Q4.

BoP surplus at US\$ 14.0bn in Q1FY20: BoP surplus remained stable at US\$ 14bn in Q1FY20 versus US\$ 14.2bn in Q4FY19. While trade deficit increased by US\$ 11bn on a QoQ basis, sharp increase in FDI inflows at US\$ 13.9bn (US\$ 6.4bn in Q4) helped contain a depletion in FX reserves. Outflows on account of banking capital also moderated to US\$ 3.9bn compared with US\$ 8.1bn in Q4. On the other hand, FII and ECB inflows moderated. After touching an 8-quarter high at US\$ 9.4bn in Q4, FII inflows slowed to US\$ 4.8bn in Q1FY20, particularly in the equity segment. ECB inflows too rose by only US\$ 6.4bn compared with US\$ 7.5bn in Q4FY19.

BoP surplus US\$ 33bn in FY20, CAD at 1.5% of GDP: Notwithstanding, the increase in CAD to 2% of GDP in Q1 from 0.7% of GDP in Q4, we expect CAD in FY20 to decrease to 1.5% of GDP in FY20 from 2.1% in FY19. This will be led by 1) lower oil prices (US\$ 65/bbl in FY20 versus US\$ 70 in FY19), 2) subdued domestic demand, 3) resilient services exports and 4) stable remittances. India may see a large increase in FDI inflows as visible in Q1. FII inflows have moderated in Q2 but given the spate of reforms announced by government, overall inflows are expected at US\$ 10bn in FY20. The above backdrop implies INR is likely to remain in the range of 70-72 to the US\$ with an appreciation bias. The key risk to our call remains 1) sharp increase in international oil prices and 2) Yuan depreciation.

KEY HIGHLIGHTS

- CAD widens to 2% of GDP in Q1FY20 from 0.7% of GDP in Q4FY19.
- BoP surplus at US\$14bn in Q1FY20 led by FDI inflows.
- CAD to narrow to 1.5% of GDP in FY20. BoP surplus at US\$ 33bn.



INTEREST RATE OUTLOOK

30 September 2019

Adherence to borrowing glide path implies lower yields

Centre has maintained its guidance of gross borrowings at Rs 7.1tn in FY20. Net borrowing in H2 is estimated at Rs 1.33tn. Notably, >10 year issuances in H2 are at 75.4% (42% outstanding) thus implying continuous bias for a steeper yield curve. The government today announced disinvestment including 100% stake sale in certain CPSEs. This will meet any revenue shortfall. For driving growth higher, we expect fiscal deficit at 3.5% of GDP in FY20 and inflows from small savings schemes to support the same.

Sameer Narang

Dipanwita Mazumdar | Jahnavi

chief.economist@bankofbaroda.com

H2FY20 gross borrowing at Rs 2.68tn: Despite lower than Budgeted collections (4.2% in FYTD20 versus FY20BE of 9.5%) along with recently announced reduction in peak corporate tax rates (estimated impact at Rs 1.45tn), the government has announced gross borrowing of Rs 2.68tn, in-line with BE. With H1 borrowing at Rs 4.42tn, overall borrowing in FY20 is Rs 7.1tn. The government today also announced stake sale in 5 CPSEs to ensure it not only meets but exceeds its disinvestment target of Rs 1.05tn in FY20.

KEY HIGHLIGHTS

- Gross borrowing in H2FY20 maintained at Rs 2.68tn.
- Disinvestment roadmap key to meet fiscal glide path.

Bias continues towards longer-end maturity: In comparison with FY19 (35% of issuances > 10years), there has been a significant increase in the issuance of long-end dated securities in FY20. For instance, in H1FY20 as much as 67.6% of issuances were in the greater than 10 year bucket. This has now increased to 75.4%. As on Sep'19, only 42% of outstanding stock of government securities has a maturity of greater than 10 years. Thus steepening bias of the yield curve is likely to persist. At present difference between 10Y yield and 1Y T-Bill is 110bps in Sep'19 vs 78bps in Aug'19.

RBI to remain accommodative, yields to decline: H2FY20 borrowing will support 10Y yield which has inched up by 20bps in Sep'19 after announcement of reduction in corporate tax rate. The fiscal data released today shows that the government has reduced its fiscal deficit to Rs 5.5tn in Apr-Aug'19 compared with Rs 5.9tn in the same period last year. The government is looking at meeting revenue shortfall from 1) higher dividend transfer from RBI (Rs 1.48tn in FY20 versus BE of Rs 900bn), 2) disinvestment in CPSEs and 3) expenditure management. With a thrust on reviving growth, we believe government may look at increasing the fiscal deficit to 3.5% of GDP. Government may rely on small saving schemes to meet the gap as sovereign issuance is unlikely in the near-term.



WEEKLY WRAP

30 September 2019

RBI policy and H2 borrowing to drive yields

Global manufacturing activity weakened further in Sep'19, especially in the Eurozone. In addition, US consumer confidence fell. With Mexico and Philippines reducing rates, global yields closed lower in the week. Oil prices fell by (-) 3.7% as Saudi output resumed. This supported Indian yields. Announcement of corporate tax cut helped lift Sensex and robust FII inflows supported INR. Government's H2 borrowing calendar and RBI policy meet will set the tone for the markets this week. We expect 25bps rate cut.

Sameer Narang | Aditi Gupta

chief.economist@bankofbaroda.com

Markets

- **Bonds:** Except China, global yields closed lower amidst weaker than expected data in Eurozone, Japan and falling consumer confidence in the US. Central Banks of Mexico and Philippines did reduce policy rate. US 10Y yield fell by 4bps (1.68%). Crude prices declined by (-) 3.7% (US\$ 62/bbl) over demand concerns. India's 10Y yield also fell by 5bps (6.74%). All eyes will be on H2 borrowing calendar and RBI policy. System liquidity surplus was at Rs 1.6tn as on 27 Sep 2019 vs Rs 324bn in the previous week.
- **Currency:** Barring AUD (flat) and INR, other global currencies closed lower. DXY rose by 0.6% in the week on the back of progress in US-China trade talks. Led by weak macro data in the EU (economic sentiment, manufacturing PMI), EUR depreciated by (-) 0.7%. GBP also fell by (-) 1.5% as uncertainty over Brexit intensified. INR rose by 0.5% in the week supported by FII inflows (US\$ 1.5bn) and lower oil prices.
- **Equity:** FTSE and Sensex bucked the trend as global equity markets ended the week lower led by growth concerns. Shanghai Comp (-2.5%) declined the most, followed by Nikkei (-0.9%) and Dax (-0.7%). However Sensex (2.1%) ended in green, supported by announcement of corporate tax cuts by government in order to boost growth.
- **Upcoming key events:** In the current week, PMIs of major economies (Germany, France, US and Japan) are due to be released. Unemployment data of US will also be watched. On the domestic front, all eyes will be on H2 borrowing calendar and RBI policy meet. BoP data is also scheduled to be released.



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Recommendations and Absolute returns (%) over 12 months

BUY – Expected return >+15%

ADD – Expected return from >+5% to +15%

REDUCE – Expected return from -5% to +5%

SELL – Expected return <-5%

Note: Recommendation structure changed with effect from 1 January 2018 (Hold rating discontinued and replaced by Add / Reduce)

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