FIRST LIGHT

03 September 2019

RESEARCH

BOB Economics Research | Q1FY20 GDP

Reforms and liquidity to drive recovery

Banking

Blockbuster merger - 10 PSBs fused into 4

SUMMARY

India Economics: Q1FY20 GDP

India's growth moderated to 5% in Q1FY20 on the back of a consumption and investment led slowdown. Exports too have moderated as global growth has fallen. The domestic slowdown has been accentuated by lack of liquidity with NBFCs and MSMEs. The recent reforms and measures announced by government such as pool buyouts from NBFCs, prompt payment and tax refunds to MSMEs, PSB recap, front loading of spending and liberalization of FDI norms have improved sentiment and will drive a cyclical recovery in H2.

Click here for the full report.

Banking

In a mega move towards consolidation, the Finance Minister has announced the merger of 10 PSBs into 4 new entities, albeit with no definite timelines or swap ratios. A further recap of Rs 553bn has also been mooted to fuel credit growth and meet regulatory/integration costs. In our view, merger will not materially benefit any of the four anchor banks, though integration will be a challenge. Also, synchronised, smooth mergers across multiple entities is a tall ask that can hurt credit growth, stall recoveries and gift market share to private banks in the short run.

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TOP PICKS

LARGE-CAP IDEAS

Company	Rating	Target
Cipla	Buy	595
GAIL	Buy	175
ONGC	Buy	175
TCS	Add	2,360
HPCL	Sell	200

MID-CAP IDEAS

Company	Rating	Target
Balkrishna Ind	Buy	1,290
Future Supply	Buy	715
Greenply Industries	Buy	195
Laurus Labs	Buy	480
PNC Infratech	Buy	250

Source: BOBCAPS Research

DAILY MACRO INDICATORS

Indicator	Current	2D (%)	1M (%)	12M (%)
US 10Y yield (%)	1.49	2bps	(57bps)	(136bps)
India 10Y yield (%)	6.55	(2bps)	14bps	(138bps)
USD/INR	71.79	0	(4.5)	(1.5)
Brent Crude (US$/bbl)	61.08	1.0	(4.1)	(21.5)
Dow	26,362	1.3	(3.2)	1.4
Shanghai	2,891	(0.1)	(1.7)	5.6
Sensex	37,069	(1.0)	(1.6)	(4.2)
India FII (US$ mn)	**28 Aug**	**MTD**	**CYTD**	**FYTD**
FII-D	15.8	1,408.4	4,062.4	3,517.7
FII-E	(176.4)	(2,191.5)	7,213.1	367.9

Source: Bank of Baroda Economics Research

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Bank of Baroda

Q1FY20 GDP

30 August 2019

Reforms and liquidity to drive recovery

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Q1FY20 growth slips to a 25-quarter low: Led by a sharp dip in consumption, India's Q1FY20 GDP growth fell to 5% compared with 5.8% in Q4FY19. While PFCE growth at 3.1% (7.2% in Q4) was at an 18-quarter low, investment growth too remained muted at 4% in Q1FY20 (3.6% in Q4). Declining auto sales and non-oil-non-gold imports suggest that domestic demand slowdown has continued even in Q2. Export growth too almost halved to 5.7% from 10.6% in Q4. Given the global backdrop, exports are unlikely to see a pickup. On the positive side, recap of banks, liquidity to NBFCs/ MSMEs and front-loaded government spending will drive a cyclical revival in H2.

Manufacturing dragged GVA lower: GVA growth fell to 4.9% in Q1FY20 (5.7% in Q4) led by sharp deceleration in manufacturing sector at 0.6% in Q1FY20 vs 3.1% in Q4. Mining too reported a dip at 2.7% (4.2% in Q4), construction decelerated to 5.7% (7.1% in Q4), financial services and real estate slowed down to 5.9% (9.5%in Q4) and public spending increased by only 8.5% (10.7% in Q4). However, agriculture reported an uptick at 2% (-0.1% in Q4). So was the case with electricity generation at 8.6% (4.3% in Q4).

PSB and liquidity to boost growth: The current slowdown can be attributed to liquidity issues with NBFCs and MSMEs. For the same, the government has announced a plan to infuse liquidity through pool buyouts from NBFCs and shorter payment cycle for MSMEs. In addition, the government today announced amalgamation of 10 PSBs into four anchor banks along with recapitalisation of Rs 525bn. This, in addition to reforms for attracting FDI announced earlier will help in reviving sentiment and growth (Page 2). We believe growth will bottom out at 6.4% in FY19 before recovering to 7% in FY21. A further slowdown in global growth remains a key risk to our estimates.

KEY HIGHLIGHTS

- GDP growth slips further to 5% in Q1FY20 from 5.8% in Q4FY19.
- GVA growth also dips to 4.9% compared with 5.7% in Q4FY19.
- Growth to recover to 7% in FY21 from 6.4% in FY20.

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BANKING

30 August 2019

Blockbuster merger – 10 PSBs fused into 4

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Big bang PSB consolidation: The government today has proposed the merger of 10 public sector banks (PSB) into 4, thereby reducing the number of PSBs to 12 from 27 (in 2017). Prima facie, it appears that banks which share a common CBS platform are being merged in order to minimise technology integration hurdles. Six PSBs have been left out of the consolidation process – we believe this was done to protect regional business interests or to avoid creating weaker entities.

Canara–Syndicate merger looks manageable: Apart from State Bank of India, Canara Bank (CBK) is the only anchor bank that we track in the public space. Post-merger with Syndicate Bank (SNDB), CBK will be the fourth largest PSB with a network of over 10,000 branches. Other synergies include a potential uplift in CASA, PCR and capital adequacy ratios (based on Mar'19 financials), besides cost reduction from network overlap. Its NNPA ratio, however, could deteriorate slightly by 25bps to 5.62%. In our view, a similar work culture could make SNDB's and CBK's consolidation journey more manageable.

Capital infusion the only silver lining: We see no material improvement in financials of the remaining anchor banks (Punjab National Bank, Union Bank, Indian Bank) post-merger. But as consolidation in the PSB space is the government's sole intention, additional capital infusion worth Rs 553bn makes the move less contentious.

Private banks to gain from protracted merger exercise: In our view, the inherently long-drawn merger process across multiple banks will divert management bandwidth away from credit growth and asset quality management in the short-run. As PSBs grapple with the mega consolidation exercise, private banks will be able to step in and augment their market share.

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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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