FIRST LIGHT

09 February 2022

RESEARCH

BOB Economics Research | Monthly Chartbook

RBI to raise reverse repo rate

SUMMARY

India Economics: Monthly Chartbook

India's recovery has gained momentum with a steady moderation in Covid-19 cases recently. While there was some moderation in services and manufacturing PMI in Jan'22 due to Omicron induced restrictions, things have started looking up. Consumption demand is showing continued improvement. Economic Survey empahsised on the role of investment to support growth. This was followed by the Union Budget which focussed on investment while also sticking to the fiscal consolidation path. However, government's large borrowing programme of Rs 14.95tn remains a cause of concern, and is likely to push yields higher. All eyes are on the RBI policy meet scheduled this week. We expect RBI to hike reverse repo rate by 25bps.

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Daily macro indicators

Indicator	04-Feb	07-Feb	Chg (%)
US 10Y yield (%)	1.91	1.92	1
India 10Y yield (%)	6.89	6.87	(2)
USD/INR	74.86	74.70	0.2
Brent Crude (US$/bbl)	93.3	92.7	(0.6)
Dow	35,090	35,091	0.0
Hang Seng	24,573	24,580	0.0
Sensex	58,645	57,621	(1.7)
India FII (US$ mn)	**03-Feb**	**04-Feb**	**Chg ($ mn)**
FII-D	7.8	(75.7)	(83.5)
FII-E	(280.1)	(689.6)	(409.5)

Source: Bank of Baroda Economics Research

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Revival on cards: The spread of Omicron has gradually receded with cases slowly dipping down across the country. With this, the government has also started reopening the economy. Notably, digital payments and electronic imports have improved in Jan'22 giving early signals of revival in consumption demand. On a monthly basis, passenger vehicle sales has also shown some improvement. Further, slower pace of contraction in tractor sales and uptick in agriculture credit reflect strength in rural demand. Moreover, rabi sowing has grown at a robust pace with sown area up by 1.2% compared with last year. Budget announcements towards agriculture were fairly positive focusing on self dependency and use of digital channels to support agri value chains.

Investment centric budget: The FM presented the budget for FY23 on 1 Feb 2022, wherein government decided to stick to the path of fiscal consolidation, without compromising on the quality of expenditure. Government has set fiscal deficit (% of GDP) target of 6.4% for FY23 compared to the upwardly revised estimte of 6.9% in FY22. The revision is mainly on account of higher spending (both revenue and capital), despite better than projected tax and non-tax revenue collections. Disinvestment receipts are expected to remain muted both this year and next year. Notably, next year, capex will see a huge jump with target set at Rs 7.5tn versus Rs 6tn in FY22. Also, market borrowing program has been pushed higher to Rs 14.95tn in FY23 versus Rs 10.47tn in FY22.

Yields inching up: India's 10Y yield shot up by 19bps in Feb'22. Government's borrowing plan of Rs 14.95tn in FY23, elevated energy prices, inflationary risks globally and central banks' adopting hawkish policy approach worldwide, have impacted yields. All eyes will be on the upcoming credit policy of RBI where we expect a 25bps hike in reverse repo rate. Even weighted average call rate is inching up towards the repo rate. Thus, pressure on yields is expected to continue and is likely to touch the 7% mark.

INR depreciates: INR depreciated by 0.4% in Jan'22, after appreciating by 1.1% in Dec'21. This was due to FII outflows (US$ 4.2bn) and higher oil prices (up by 17.3% MoM). Fed's hawkish tilt also drove dollar higher. Trade deficit eased in Jan'22 as imports moderated more sharply than exports. We expect trade deficit to remain elevated on the back of higher oil prices and economic recovery. FPI inflows too may remain weak as global central banks begin hiking rates. However, depreciation pressure on INR is likely to remain muted. We expect INR to trade in the range of 74.5-75.5/$ in the near term.

Note: The source for all exhibits is 'CEIC and Bank of Baroda' unless otherwise specified

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BUY – Expected return >+15%

HOLD – Expected return from -6% to +15%

SELL – Expected return <-6%

Note: Recommendation structure changed with effect from 21 June 2021

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