

## RESEARCH

### BOB Economics Research | Weekly Wrap

India's economic recovery continues

### BOB Economics Research | CPI

CPI springs a negative surprise

### BOB Economics Research | WPI

Rising oil and commodity prices push WPI higher

### Banking

Framework to harmonise microfinance regulations

### Daily macro indicators

Indicator	Current	2D (%)	1M (%)	12M (%)
US 10Y yield (%)	1.45	2bps	(17bps)	78bps
India 10Y yield (%)	6.01	(1bps)	0bps	23bps
USD/INR	73.08	0.0	0.4	3.6
Brent Crude (US\$/bbl)	72.69	0.2	6.0	88.6
Dow	34,480	0.0	0.6	37.2
Shanghai	3,590	(0.6)	4.3	22.9
Sensex	52,475	0.3	6.7	56.5
India FII (US\$ mn)	10-Jun	MTD	CYTD	FYTD
FII-D	144.0	(245.7)	(2,826.3)	(799.1)
FII-E	197.6	1,419.5	8,005.6	679.2

Source: Bank of Baroda Economics Research

## SUMMARY

### India Economics | Weekly Wrap

Even with US inflation at 5%, US 10Y yield fell as surge is expected to be transitory. EUR fell by 0.5% after ECB reiterated its accommodative stance and Germany's economic sentiment and factory order dropped. Economic activity continues to rebound in India with receding cases and easing off restrictions. Our weekly economic tracker shows a pickup in economic activity (at 88 from 84 WoW). Easing US yields are a positive for Indian bonds where inflation concerns have been creeping in with double-digit WPI inflation.

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

### India Economics | CPI

CPI surprised negatively to 6.3% in May'21 led by higher food and core inflation. While food inflation increased to 5% (2% in Apr'21), core inflation went up to 6.6% (5.4% in Apr'21). The increase was broad based and likely to persist with pass-through of commodity, oil and precious metal prices. We now expect CPI inflation to average 5.5% in FY22 led by higher core inflation at 6.2%. While MPC is likely to focus on growth over inflation in the near-term, medium term policy normalisation will also be on the discussion agenda.

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

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### India Economics | WPI

WPI inflation rose by 12.9% in May'21, highest since Sep'91, from 10.5% in Apr'21 led by fuel and power index (37.6% in May'21 from 20.9% in Apr'21) and manufactured products (10.8% in May'21 from 9% in Apr'21) index. Food inflation rose from 7.6% in Apr'21 to 8.1% in May'21. International commodity prices and oil prices have seen a MoM increase even in Jun'21. This implies fuel and manufactured products inflation will remain elevated in coming months. A normal monsoon bodes well for outlook on food inflation.

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

### Banking

- RBI has released a consultative document on the regulation of microfinance that seeks feedback from stakeholders by Jul'21
- The proposed guidelines include withdrawal of the interest rate ceiling and relaxation of various regulatory restrictions on NBFC-MFIs
- We believe these norms would promote competition and encourage healthy lending practices without being disruptive as anticipated earlier

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

## WEEKLY WRAP

14 June 2021

### India's economic recovery continues

Even with US inflation at 5%, US 10Y yield fell as surge is expected to be transitory. EUR fell by 0.5% after ECB reiterated its accommodative stance and Germany's economic sentiment and factory order dropped. Economic activity continues to rebound in India with receding cases and easing off restrictions. Our weekly economic tracker shows a pickup in economic activity (at 88 from 84 WoW). Easing US yields are a positive for Indian bonds where inflation concerns have been creeping in with double-digit WPI inflation.

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### Markets

- Bonds:** Despite higher than estimated CPI inflation, US 10Y yield fell by 10bps (1.45%) during the week. Consensus expectation is that US Fed might follow ECB's tone regarding inflation spike being transient. Crude prices rose by 1.1% (US\$ 73/bbl) as global economy continued on the path to recovery. India's 10Y yield fell by 2bps (6.01%) supported by GSAP. System liquidity surplus rose to Rs 4.8tn as on 11 Jun 2020 from Rs 4.7tn in previous week.
- Currency:** Global currencies closed lower this week. EUR fell by 0.5% as ECB is expected to continue its stance on rates and liquidity. DXY rose by 0.5% with buoyant consumer sentiment. INR depreciated by 0.1% as oil prices rose to a more than 2-year high. FII inflows were US\$ 591mn.
- Equity:** Global indices closed mixed. While Dow and Shanghai Comp fell, FTSE and Sensex rose. Investors believe high US CPI print to be transitory and await Fed's policy decision this week. Sensex rose by 0.7% led by power, tech and metal stocks.
- Covid-19 tracker:** Global Covid-19 cases rose at a slower pace of 2.6mn this week versus 3mn last week led by India at 0.6mn (0.9mn last week). Our weekly economic activity tracker index rose to 88 (100=Feb'20) from 84 last week. Israel has fully vaccinated 59% of its population, US and UK at 43%. India still far lower at 3.4%.
- Upcoming key events:** Major events this week include policy decision at US Fed and BoJ, industrial production and retail sales data from US and China. On the domestic front, CPI and WPI prints are due later today.



## INFLATION

14 June 2021

### CPI springs a negative surprise

CPI surprised negatively to 6.3% in May'21 led by higher food and core inflation. While food inflation increased to 5% (2% in Apr'21), core inflation went up to 6.6% (5.4% in Apr'21). The increase was broad based and likely to persist with pass-through of commodity, oil and precious metal prices. We now expect CPI inflation to average 5.5% in FY22 led by higher core inflation at 6.2%. While MPC is likely to focus on growth over inflation in the near-term, medium term policy normalisation will also be on the discussion agenda.

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**CPI overshoots:** CPI inflation surprised negatively and rose to a 6-month high of 6.3% in May'21 (consensus estimate of 5.4%). At the same time, Apr'21 CPI inflation has been revised to 4.2% (earlier 4.3%).

**Food inflation accelerates:** Food inflation rose to 5% in May'21 from 2% in Apr'21. This was led by oils and fat (30.8% from 25.9%), eggs (15.2% from 10.6%), fruits (12% from 9.7%), and pulses (9.4% from 7.5%). Vegetable prices fell by -1.9% (-14.5% in Apr'21), sugar by -1.4% (-6%) and cereal by -1.4% (-3%). However, rate of price increase in meat and fish moderated to 9% (16.7%). While vegetable and cereal inflation is likely to remain moderate, edible oils, pulses, egg and meat and fish will remain elevated.

**Core inflation firms up:** CPI excluding food and fuel rose by 120bps to 6.6% in May'21 from 5.4% in Apr'21. The increase was broad based led by 260bps jump in personal care and effects (8% from 5.4%), 190bps jump in household goods and services (3.9% from 1.9%), 180bps jump in recreation and amusement (6.3% from 4.6%), 180bps jump in clothing and footwear (5.3% from 3.5%) and 160bps jump in transport and communication (12.4% from 10.8%). Despite weak demand, the broad based increase points to pass-through of higher commodity, oil and precious metal prices into consumer inflation.

**CPI Inflation now estimated at 5.5%:** We now expect CPI to overshoot RBI's estimate of 5.1% in FY22. This will be largely driven by higher core inflation (already at 6.6%) and likely to average 6.2% in FY22. Fuel and light inflation will also be on higher side. Food inflation will be relatively lower at less than 5%. While MPC will continue to focus on growth, an upward revision in inflation trajectory implies discussion on accommodative policy exit will also be on the table. Risk to our estimates is from cut in excise duties on petroleum products.

#### KEY HIGHLIGHTS

- CPI rose to a 6-month high of 6.3% in May'21 from 4.2% in Apr'21.
- Food inflation rose to 5% from 2% in Apr'21, core increased to 6.6% from 5.4% in Apr'21.
- Revised our forecast for FY22 CPI to 5.5% led by core elevated at 6.2%.



## WHOLESALE INFLATION

14 June 2021

### Rising oil and commodity prices push WPI higher

**WPI inflation rose by 12.9% in May'21, highest since Sep'91, from 10.5% in Apr'21 led by fuel and power index (37.6% in May'21 from 20.9% in Apr'21) and manufactured products (10.8% in May'21 from 9% in Apr'21) index. Food inflation rose from 7.6% in Apr'21 to 8.1% in May'21. International commodity prices and oil prices have seen a MoM increase even in Jun'21. This implies fuel and manufactured products inflation will remain elevated in coming months. A normal monsoon bodes well for outlook on food inflation.**

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**Food inflation continues to rise:** Food inflation accelerated for the 4th straight month in May'21 to 8.1% (16-month high) from 7.6% in Apr'21 led by pulses and edible oils. While pulses index increased by 12.1% in May'21 from 10.7% in Apr'21, vegetable (edible) oils index rose by 51.7%. Deflation in cereals moderated to 2.5% from 3.3% in Apr'21. However, fruit prices rose at a slower pace of 20.2% versus 27.4% in Apr'21. Price rise in egg, meat and fish items was stable at 10.7% in May'21. Prices of vegetables contracted at 9% in May'21, same as Apr'21. A normal monsoon bodes well for food inflation. Edible oils too may see some dip as the Centre is considering reducing customs duty.

**Fuel and power inflation remains elevated:** Fuel and power inflation rose further to 37.6% in May'21 from 20.9% in Apr'21. A low base, index dropped by 23.1% May'20 compared with fall of only 12.6% in Apr'20, and rising oil prices explain this. Mineral oil index rose the most by 81.2% in May'21 (45.3% in Apr'21) with a broad based increase. On a YoY basis, Kerosene index moved up by 217.7% (42.7% in Apr'21), ATF by 234.4% (96.4%) and Naphtha by 241.1% (154.3%). Rising oil prices (Brent now at US\$ 72/bbl versus US\$ 68.3/bbl in May'21) imply upward bias in fuel and power inflation will remain.

**Core inflation inches further up:** Core inflation rose to its new high (2011-12 series) of 10% in May'21 from 8.4% in Apr'21. Manufactured products inflation also rose to 10.8% from 9% in Apr'21. Of the 22 commodities indices, as many as 13 commodities indices rose at a faster pace in May'21 than Apr'21 led by basic metals, fabricated metals, furniture and 'other manufacturing'. With a low base and international commodity prices firming up by 2.7% (MoM) in Jun'21, core and manufactured inflation is likely to remain elevated in coming months.



## BANKING

14 June 2021

### Framework to harmonise microfinance regulations

- RBI has released a consultative document on the regulation of microfinance that seeks feedback from stakeholders by Jul'21
- The proposed guidelines include withdrawal of the interest rate ceiling and relaxation of various regulatory restrictions on NBFC-MFIs
- We believe these norms would promote competition and encourage healthy lending practices without being disruptive as anticipated earlier

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**Interest rate cap abolished:** Under the proposed guidelines, the RBI will allow the board of directors of NBFC-MFIs to determine the interest rates to be charged for loans as against present rules where the regulator dictates the maximum rates these institutions can charge.

**Select restrictions eased:** The central bank has retained the overall income cap of Rs 125k/Rs 200k for rural/semi urban borrowers and capped the EMI at 50% of household income. Moreover, a limit for maximum permissible level of indebtedness for microfinance borrowers shall be made applicable to all lenders. However, the RBI has withdrawn most regulatory restrictions around (1) loan limit of Rs 75k in the first cycle and Rs 125k in subsequent cycles, (2) loan tenure, (3) 50% lending towards income generation activity, and (4) the two-lender limit.

**Guidelines not as disruptive as anticipated:** We believe these guidelines encourage competition and aim to build healthy lending practices by providing autonomy to NBFC-MFIs to set interest rates based on their board-approved policies. Moreover, the proposals are not as disruptive as anticipated earlier. However, we remain cautious on the microfinance sector as its collection efficiency is expected to decline in Q1FY22 owing to protracted Covid-19 curbs amid the second wave that will intensify pressure on asset quality.

### Recommendation snapshot

Ticker	Price	Target	Rating
AUBANK IN	1,070	1,300	BUY
BANDHAN IN	317	335	ADD
CBK IN	155	165	ADD
HDFCB IN	1,479	1,800	BUY
KMB IN	1,768	2,100	BUY
SBIN IN	430	515	BUY

Price &amp; Target in Rupees | Price as of 14 June 2021

### NBFC-MFIs' 30+ PAR trend



Source: Crisil Ratings



## Disclaimer

### Recommendation scale: 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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