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FIRST LIGHT

01 April 2021

RESEARCH

BOB Economics Research | Balance of Payments

Rising imports drive current account to deficit

BOB Economics Research | Interest Rate Outlook

Government borrowing skewed towards long-end

SUMMARY

India Economics: Balance of Payments

India's current account went back into deficit of US$ 1.7bn (-0.2% of GDP) from surplus of US$ 15.1bn (2.4% of GDP) in Q2. Non-oil imports increased to US$ 111.8bn in Q3 from US$ 90.4bn in Q2. Software exports (+ 9% YoY) rose. Still, BoP surplus increased to US$ 32.5bn (from US$ 31.6bn in Q2) due to FPI inflows of US$ 21.2bn in Q3. Normalisation of domestic economic activity and rising oil prices imply current account deficit will increase to 1.5% of GDP in FY22. This along with stronger US$ implies depreciation bias for INR.

Click here **for the full report.**

India Economics: Interest Rate Outlook

Centre's borrowing in H1FY22 is pegged at Rs 7.2tn compared with Rs 7.4tn in H1FY21. The share of greater than 30 year maturity has increased to 27% from 22% last year. Share of 10 year and 14 year maturity has declined to 41% from 47%. Government has also reduced interest rates on small saving schemes of different maturities ranging from 0.4% to 0.9% from 1 April 2021. This is positive for interest rate transmission and sentiment. But rising global yields, inflation and issuance pattern suggests upward momentum in yields to sustain.

Click here **for the full report.**

TOP PICKS

LARGE-CAP IDEAS

Company	Rating	Target
Cipla	Buy	1,000
GAIL	Buy	160
Petronet LNG	Buy	330
TCS	Buy	3,710
Tech Mahindra	Buy	1,130

MID-CAP IDEAS

Company	Rating	Target
Alkem Labs	Buy	3,750
Greenply Industries	Buy	195
Laurus Labs	Buy	480
Transport Corp	Buy	330
Mahanagar Gas	Sell	750

Source: BOBCAPS Research

DAILY MACRO INDICATORS

Indicator	Current	2D (%)	1M (%)	12M (%)
US 10Y yield (%)	1.70	(1bps)	30bps	103bps
India 10Y yield (%)	6.15	2bps	(9bps)	1bps
USD/INR	73.39	(1.2)	0.1	2.9
Brent Crude (US$/bbl)	64.14	(1.3)	(3.0)	182.1
Dow	33,067	(0.3)	6.9	50.9
Shanghai	3,457	0.6	(1.5)	25.7
Sensex	50,137	2.3	2.1	70.1
India FII (US$ mn)	**26 Mar**	**MTD**	**CYTD**	**FYTD**
FII-D	118.9	(756.0)	(2,240.2)	(6,333.8)
FII-E	54.6	2,627.4	7,621.2	37,596.9

Source: Bank of Baroda Economics Research

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BALANCE OF PAYMENTS

31 March 2021

Rising imports drive current account to deficit

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India's current account went back into deficit of US$ 1.7bn (-0.2% of GDP) from surplus of US$ 15.1bn (2.4% of GDP) in Q2. Non-oil imports increased to US$ 111.8bn in Q3 from US$ 90.4bn in Q2. Software exports (+ 9% YoY) rose. Still, BoP surplus increased to US$ 32.5bn (from US$ 31.6bn in Q2) due to FPI inflows of US$ 21.2bn in Q3. Normalisation of domestic economic activity and rising oil prices imply current account deficit will increase to 1.5% of GDP in FY22. This along with stronger US$ implies depreciation bias for INR.

KEY HIGHLIGHTS

- Current account deficit at US$ 1.7bn (0.2% of GDP) in Q3FY21 from surplus of US$ 15.1bn (2.4% of GDP).
- Trade deficit widens to US$ 34.5bn in Q3FY21 from US$ 14.8bn in Q2FY21.
- BoP surplus increased to US$ 32.5bn from US$ 31.6bn in Q2FY21 led by FPI inflows.

Current account moves to deficit: Led by wider trade deficit of US$ 34.5bn in Q3FY21 (US$ 14.8bn in Q2), India's current account slipped back to deficit of US$ 1.7bn in Q3FY21 (surplus of US$ 15.1bn in Q2FY21). Imports jumped to US$ 111.8bn (US$ 90.4bn in Q2FY21) led by sharp increase in non-oil imports as economic activity normalised. Exports too inched up, marginal increase of US$ 1.6bn (QoQ), to US$ 77.2bn in Q3. Net invisible receipts increased to US$ 32.8bn in Q3 from US$ 29.9bn in Q2 led by higher transfers (US$ 19.3 bn in Q3 from US$ 18.4bn in Q2) and income from services—software exports—US$ 23.4bn from US$ 22bn. Investment outflows on income side increased to US$ 10.1bn in Q3 from US$ 9.4bn in Q2.

Capital account surplus rises: Capital account surplus improved to US$ 33.5bn in Q3 from US$ 16.1bn in Q2. This was led by pick up in FPI inflows which rose to US$ 21.2 in Q3 from US$ 7bn in Q2. Equity inflows increased to US$19.8bn in Q3 compared with US$ 6.8bn in Q2. Banking capital outflows eased to US$ 7.6bn in Q3 from US$11.2bn outflows in Q2. The same was the case with ECB outflows which fell to US$ 1.2bn from US$ 3.9bn in Q2. Short-term credit picked up to US$ 0.2bn against outflow of US$ 1.8bn. Overall, BoP surplus expanded to US$ 32.5bn in Q3 compared with US$ 31.6bn in Q2.

Current account deficit at 1.5% in FY22: India's current account slipped in to deficit mode at 0.2% of GDP in Q3 as trade deficit widened. This trend is likely to continue as domestic economic activity is normalizing. Higher oil prices too will put upward pressure on imports. We estimate a current account surplus of 0.9% of GDP in FY21 and a deficit of 1.5% of GDP in FY22 (Oil at 65/bbl). Accordingly, BoP surplus will be much lower. This along with a strong dollar outlook implies mild depreciation on INR. Inclusion of India into global bond index may reverse the sentiment.

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Bank of Baroda

INTEREST RATE OUTLOOK

31 March 2021

Government borrowing skewed towards long-end

Centre's borrowing in H1FY22 is pegged at Rs 7.2tn compared with Rs 7.4tn in H1FY21. The share of greater than 30 year maturity has increased to 27% from 22% last year. Share of 10 year and 14 year maturity has declined to 41% from 47%. Government has also reduced interest rates on small saving schemes of different maturities ranging from 0.4% to 0.9% from 1 April 2021. This is positive for interest rate transmission and sentiment. But rising global yields, inflation and issuance pattern suggests upward momentum in yields to sustain.

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KEY HIGHLIGHTS

- Gross borrowing in H1FY22 at Rs 7.24tn.
- Issuance calendar skewed towards long-end with more than 30 year maturity at 27% of issuances.
- Long-end yields likely to see upward pressure in the year.

Centre's borrowing for H1 at Rs 7.2tn: Gross borrowing for H1FY22 has been kept at Rs 7.2tn as against Rs 7.4tn in H1FY21. Net borrowing is estimated at Rs 5.9tn in H1FY22 compared with Rs 6tn in H1FY21. Given the overall borrowing of Rs 12.05tn in FY22, H1 borrowing works out to be 60% of annual borrowing. This implies gross borrowing will be sharply lower in H2FY22 at Rs 4.8tn. However, state government borrowings are likely to remain elevated in FY22. In FY21, states have borrowed Rs 7.8tn. Out of this, 57% was borrowed in H2.

Maturity pattern skewed towards long-end: Out of the total issuance, 7% is through FRBs (6% in H1FY21). The 2-year and 5-year buckets account for 25% of total issuance in H1FY22 (25% in H1FY21). While 10 and 14 year issuance is at 41% of H1 borrowing (47% in H1FY21), greater than 30 year bucket stands at 27%, much higher than last year's 22%. The overwhelming presence of such high dated maturities should put upward pressure on yields at the longer end of the curve.

Outlook on interest rates: Global yields have been increasing this year with 10 year yield in US rising by 79bps followed by UK at 62bps and Germany by 28bps in CYTD21. Compared to this, India's 10 year yield has increased by 28bps. EM bond yields are up by 51bps. After the announcement of borrowing calendar, the government also announced sharp reduction in small saving rates ranging from 0.4% to 0.9% across different maturities. While this bodes well for decline in domestic interest rates, the size of Centre and State gross borrowing of Rs 20tn in FY22 along with upward pressure on inflation on account of rising commodity prices implies 10Y yields is likely to be in the range of 6.2-6.5% in most of FY22.

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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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