FIRST LIGHT

04 April 2022

RESEARCH

BOB Economics Research | Monthly Economic Buffet

Economic Wrap – March 2022

BOB Economics Research | Industry Report

Which industries are vulnerable in terms of fuel cost

BOB Economics Research | Currency Outlook

INR to stabilise at 75.5-76.5/$

Daily macro indicators

Indicator	30-Mar	31-Mar	Chg (%)
US 10Y yield (%)	2.35	2.34	(1bps)
India 10Y yield (%)	6.78	6.84	5bps
USD/INR	75.91	75.79	0.2
Brent Crude (US$/bbl)	113.5	107.9	(4.9)
Dow	35,229	34,678	(1.6)
Hang Seng	22,232	21,997	(1.1)
Sensex	58,684	58,569	(0.2)
India FII (US$ mn)	**29-Mar**	**30-Mar**	**Chg ($ mn)**
FII-D	(90.0)	10.3	100.4
FII-E	(23.3)	314.6	337.8

Source: Bank of Baroda Economics Research

SUMMARY

India Economics: Monthly Economic Buffet

With continuing war between Russia and Ukraine, commodity prices remain elevated. Global markets are analysing the impact of this on global inflation and trajectory of growth. Rise in Covid-19 cases in China have posed another downside risk to economic recovery. On the domestic front, Rs 6.4/lt rise in retail fuel prices this month added to inflation burden on consumers. We expect RBI to take note of this and consider changing its accommodative stance in the upcoming Apr'22 meet.

Click here **for the full report.**

India Economics: Industry Report

RBI in a recent report has highlighted three industries-electricity, chemicals and automobiles, as being the most vulnerable sectors in terms of fossil fuel intensity. As a corollary banks need to keep this in mind when lending. This study looks at the energy intensity of various industries and also juxtaposes the same with the banking system's exposure to them.

Click here **for the full report.**

India Economics: Currency Outlook

After depreciating to a record-low of 76.97/$, INR has stabilised in the last few days. This has coincided with easing concerns over Russia-Ukraine war and moderation in oil prices. FPI outflows too have receded as risk-sentiment has improved. We expect INR to trade in the range of 75.5-76.5/$ in the next fortnight. Sharp jump in oil prices remains a key risk. However, over the medium and long term, Fed tightening might put downward pressure on INR. For FY23, we expect INR to trade in the range of 76-77/$.

Click here **for the full report.**

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MONTHLY ECONOMIC BUFFET

01 April 2022

Economic Wrap: March 2022

Sonal Badhan
Economist

With continuing war between Russia and Ukraine, commodity prices remain elevated. Global markets are analysing the impact of this on global inflation and trajectory of growth. Rise in Covid-19 cases in China have posed another downside risk to economic recovery. On the domestic front, Rs 6.4/lt rise in retail fuel prices this month added to inflation burden on consumers. We expect RBI to take note of this and consider changing its accommodative stance in the upcoming Apr'22 meet.

War continues: Full scale war between Russia and Ukraine continues to dominate global markets. As a result of the war and stiff economic sanctions imposed on Russia, global commodity prices have increased hsarply. In particular, international crude price is hovering above US$ 110/bbl with 9% (MoM) increase since the war started. Gold is also up by 2%. Prices of food commodities too remain elevated. The impact of this is also visible in domestic fuel prices, which have gone up by Rs 6.4/lt since 22 Mar 2022. However, with rise in new Covid-19 cases in China and announcement of stringent lockdown restrictions, pose downside risk to oil and other commodity prices. It also poses downside risk to global economic recovery.

Global Central Banks on the move: US Fed has begun its rate hike cycle with 25bps increase in its Mar'22 policy meeting. More aggressive rate hikes (~50bps) are expected in the upcoming meetings to tame rising inflation. BoE has also hiked rate (by 25bps) for the third consecutive time now On the other hand, BoJ remains on hold and continues to keep its policy accommodative to support 10Y yield.

Key macro data releases: Latest data shows that India's eight core industries continued its upward momentum as it rose to a 4-month high of 5.8% in Feb'22 compared with a growth of 4% in Jan'22. Separately, India's current account deficit (CAD) widened to a 13-quarter high of 2.7% in Q3FY22 (US$ 23bn) compared with 1.3% of GDP in Q2FY22 (US$ 9.9bn). Trade deficit rose by US$ 16bn led by sharp jump in both oil and non-oil imports.

Centre has also announced its borrowing calendar for H1FY23, pegging borrowing at Rs 8.45tn (59% of total). Net borrowing in H1 is estimated at Rs 6.18tn (Rs 5.35tn last year). However, borrowing through T-bills will be slightly lower in H1 at Rs 4.32tn compared with Rs 4.68tn last year.

CPI inflation rose to 6.1% in Feb'22 against market consensus of 6%. Notably, inflation surpassed its Jan'22 level which was supposed to be the peak as said in the RBI's policy statement. Going forward, we expect CPI to be ~5.5-6% in FY23. Upside risks persist and all eyes are now on RBI's policy decision due next week.

INDUSTRY REPORT

31 March 2022

Which industries are vulnerable in terms of fuel cost

Dipanwita Mazumdar
Economist

RBI in a recent report has highlighted three industries-electricity, chemicals and automobiles, as being the most vulnerable sectors in terms of fossil fuel intensity. As a corollary banks need to keep this in mind when lending. This study looks at the energy intensity of various industries and also juxtaposes the same with the banking system's exposure to them.

Global backdrop: In Glasgow COP26 (2021), India has pledged to reduce its net emission to 0 by 2070 (3rd largest emitter) and increase its share of renewables in the energy mix to 50% by 2030. As we move towards the attainment of this goal, companies will face challenges in terms of compliance and banks will have to keep this in mind when lending as financial performance can be impacted.

RBI's recent research report flagged three industries -*electricity, chemical and chemical products and automobiles* - as having high fossil fuel intensity. Their data has been taken from the Annual Survey of Industries, 2016-17.

Our study looks at the share of power and fuel to total expenditure to analyse energy intensity of industries. Admittedly the energy component includes all sources and not just fossil fuels. *We have taken an aggregate of 2648 companies and evaluated their Power and fuel cost as share of total expenditure*.

What our study says: Our study shows that the energy intensity for the aggregate sample has remained by and large stable in the range of 9.4% to 10.2% in the last 6 years ending 2020-21. There has been a marginal decline in 2020-21 which can be attributed more to the decline in overall production. The leading sectors in terms of energy intensity are communications, glass and glassware, paper and paper products, metals and products and transport besides electricity which inherently is fuel intensive. If we exclude electricity (as it is an outlier), the average of the past 6 years (since Mar-16) stands at 6%.

Limitation of our study: We have taken the power and fuel cost in the Income Expenditure Statement, so it incorporates both renewable and non-renewables. The share of non-conventional energy is limited (as 80% of India's energy needs are met by coal, oil and solid biomass-IEA report on India Energy Outlook, 2021).

CURRENCY OUTLOOK

01 April 2022

INR to stabilise at 75.5-76.5/$

After depreciating to a record-low of 76.97/$, INR has stabilised in the last few days. This has coincided with easing concerns over Russia-Ukraine war and moderation in oil prices. FPI outflows too have receded as risk-sentiment has improved. We expect INR to trade in the range of 75.5-76.5/$ in the next fortnight. Sharp jump in oil prices remains a key risk. However, over the medium and long term, Fed tightening might put downward pressure on INR. For FY23, we expect INR to trade in the range of 76-77/$.

Aditi Gupta
Economist

Currency movement: Most global currencies rallied in the second-half of Mar'22 (18-31 Mar'22), as concerns over Russia-Ukraine war stabilised. This led to a risk-on sentiment in the global forex markets. While DXY had strengthened by 2.5% between 1-15 Mar'22, it fell by 0.8% in the latter period. This was notwithstanding Fed's first rate-hike since Dec'18 and rising US 10Y yields. Amongst other advanced economies, EUR rose by 1% after falling by 2.3% between 1-15-Mar'22 as higher than expected inflation in the Eurozone has raised expectations of rate hikes by ECB. On the other hand, JPY has depreciated sharply in both the periods and continues to trade near a 6-year low. JPY's relative underperformance can be attributed to BoJ's dovish commentary and rising yield differential with the US. Further, higher oil prices have raised concerns over external stability and hence weighed on the JPY. However, EM currencies rallied between (18-31 Mar'22), led by Brazilian Real. Higher commodity prices are supporting the rally in most EM currencies.

INR too has moved in tandem with other EM currencies. After depreciating by 1.7% between 1-15 Mar'22, it appreciated by 1.1% in the latter half of the month. This was supported by some correction in oil prices as well as weakness in dollar. Further, while FPI's continued to remain net sellers in the domestic market even in the second half of Mar'22, there was some moderation. FPI outflows totalled US$ 5.6bn between 1-15 Mar'22, compared with outflows of US$ 0.3bn in the second-half. This too supported INR.

Outlook: While, dollar has weakened recently, it is likely to recoup its losses. This is because, Fed is turning increasingly hawkish. The median rate projection for Fed's funds rate of 1.9% for CY22 (in Mar'22 policy meet), was much higher than 0.9% estimated in its Dec'21 meeting. This implies rate hikes in each of the six remaining meetings in CY22. Even in CY23, three more rate hikes are expected, bringing the Fed funds rate to 2.8% (1.6% expected in Dec'21 meeting). This will support DXY. While other global central banks are also likely to embark on the policy tightening cycle, Fed is likely to remain ahead of the curve. This should keep the yield differential in favour of the dollar. US Jobs report due later in the evening will also have a bearing on the outlook for DXY.

INR to remain range-bound: After depreciating to a record-low of 76.97 on 7 Mar 200, INR has consolidated its losses. In fact, while INR closed at a ~1-month high of 75.79/$ in the last trading session. Notably, India's current account deficit (CAD) expanded to a 13-quarter high of 2.7% in Q3FY22. This is likely to surge further to 3.5% in Q4 led by higher oil prices (brent oil prices averaged US$ 97.9/bbl in Q4 versus US$ 79.7/bbl in Q3). However, the recent correction seen in oil prices will lent support to INR. We expect INR to trade in the range of 75.5-76.5/$ in the next two-weeks. Escalation in tensions between Russia and Ukraine and the resulting increase in oil prices remains a key risk.

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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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