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FIRST LIGHT

01 October 2020

RESEARCH

BOB Economics Research | Balance of Payments

Current account surplus expands

BOB Economics Research | Interest Rate Outlook

Centre sticks to its borrowing calendar

Banking

Lending rates dip in August

SUMMARY

India Economics: Balance of Payments

After reporting a current account surplus of US$ 0.6bn in Q4, India reported a surplus of US$ 19.8bn (3.9% of GDP) in Q1FY21 as imports fell more sharply than exports. Services income led by software services was relatively stable. However, capital account saw a sharp reduction to US$ 0.6bn as FDI and ECB inflows dropped even as FPI inflows resumed and external assistance inflows increased. For FY21, we expect a current account surplus of 1.1% of GDP and a BoP surplus of US$ 82.6bn. This should support INR in the near-term.

Click here for the full report.

India Economics: Interest Rate Outlook

Centre has maintained its borrowing plan of Rs 12tn implying gross and net borrowing of Rs 4.25tn and Rs 3.37tn in H2. Issuance pattern remains skewed towards 10Y and above (55% of issuances) which to some extent justifies term premium/steep yield curve. State borrowings will also pick-up pace in Q3 and Q4. In addition, Centre may look at issuing longer dated securities to refinance some of the T-Bills outstanding. The above backdrop suggests gross borrowing of dated securities will be higher thus implying 10Y in the range of 6-6.25%.

Click here for the full report.

TOP PICKS

LARGE-CAP IDEAS

Company	Rating	Target
Bajaj Finance	Buy	4,000
Cipla	Buy	850
GAIL	Buy	155
Petronet LNG	Buy	310
Tech Mahindra	Buy	910

MID-CAP IDEAS

Company	Rating	Target
Alkem Labs	Buy	3,600
Chola Investment	Buy	280
Laurus Labs	Buy	1,200
Transport Corp	Buy	270
Mahanagar Gas	Sell	750

Source: BOBCAPS Research

DAILY MACRO INDICATORS

Indicator	Current	2D (%)	1M (%)	12M (%)
US 10Y yield (%)	0.65	0bps	(7bps)	(99bps)
India 10Y yield (%)	6.04	(2bps)	(11bps)	(63bps)
USD/INR	73.86	(0.1)	(0.6)	(3.9)
Brent Crude (US$/bbl)	41.03	(3.3)	(8.9)	(30.3)
Dow	27,453	(0.5)	(4.2)	3.3
Shanghai	3,224	0.2	(5.3)	11.0
Sensex	37,973	0	(3.8)	(0.9)
India FII (US$ mn)	**28 Sep**	**MTD**	**CYTD**	**FYTD**
FII-D	40.9	584.1	(14,505.9)	(4,746.4)
FII-E	71.3	(587.0)	4,220.3	10,823.3

Source: Bank of Baroda Economics Research

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Banking

As per latest RBI data, the weighted average lending rate (WALR) on fresh rupee loans sanctioned by scheduled commercial banks (SCB) declined 18bps MoM to ~8.4% in August, driven by a ~30bps fall in rates at private banks. Public sector (PSB) and private banks have reduced fresh lending rates by ~60bps and ~50bps respectively since Mar'20. Banks have been cutting MCLR on the back of lower policy rates, which has translated into lower fresh rates.

Click here for the full report.

BALANCE OF PAYMENTS

30 September 2020

Current account surplus expands

After reporting a current account surplus of US$ 0.6bn in Q4, India reported a surplus of US$ 19.8bn (3.9% of GDP) in Q1FY21 as imports fell more sharply than exports. Services income led by software services was relatively stable. However, capital account saw a sharp reduction to US$ 0.6bn as FDI and ECB inflows dropped even as FPI inflows resumed and external assistance inflows increased. For FY21, we expect a current account surplus of 1.1% of GDP and a BoP surplus of US$ 82.6bn. This should support INR in the near-term.

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Record current account surplus in Q1: India's current account registered a record surplus of US$ 19.8bn in Q1FY21, compared with a surplus of US$ 0.6bn in Q4FY20. Sharp reduction in imports relative to exports in Q1 contributed to the current account surplus. The invisible balance was lower on account of 7.7% QoQ decline in transfers and higher investment income outflows of US$ 8.4bn in Q1 compared with US$ 5.6bn in Q4. Income from software services was marginally lower at US$ 20.8bn, (-) 1.7% QoQ.

Capital account surplus shrinks: Capital account surplus narrowed to US$ 0.6bn in Q1FY21 from US$ 17.4bn in Q4FY20. The decline can be explained by net FDI outflow of US$ 0.4bn (inflow of US$ 12bn in Q4) and ECB outflow of US$ 1.6bn (inflow of US$ 10.3bn in Q4). On the other hand, FPI inflows turned positive at US$ 0.6bn in Q1FY21 compared with outflow of US$ 13.7bn in Q4. External assistance and banking capital inflows were at US$ 4.1bn and US$ 2.2bn respectively compared with US$ 0.6bn and (-) US$ 4.6bn respectively in Q4.

BoP surplus to expand further: India's current account surplus rose to a historic high of 3.9% of GDP in Q1FY21 as trade deficit narrowed. We expect a current account surplus even in Q2 and Q3 followed by a deficit in Q4. This coincides with India's economic recovery. For FY21, we expect trade deficit to narrow to US$ 98bn from US$ 158bn in FY20. At the same time, invisible receipts have held up, particularly for software services and are expected to remain so. Along with FPI inflows even FDI inflows will pick-up thus driving a BoP surplus of more than US$ 80bn in FY21 compared with US$ 59.6bn in FY20. This should support INR in the near-term.

KEY HIGHLIGHTS

- Current account surplus expands to US$ 19.8bn (3.9% of GDP) in Q1FY21.
- Trade deficit narrows sharply to US$ 10bn in Q1FY21 from US$ 35bn in Q4FY20.
- BoP surplus also increased to US$ 19.9bn versus US$ 18.8bn in Q4FY20.

30 September 2020

Centre sticks to its borrowing calendar

Centre has maintained its borrowing plan of Rs 12tn implying gross and net borrowing of Rs 4.25tn and Rs 3.37tn in H2. Issuance pattern remains skewed towards 10Y and above (55% of issuances) which to some extent justifies term premium/steep yield curve. State borrowings will also pick-up pace in Q3 and Q4. In addition, Centre may look at issuing longer dated securities to refinance some of the T-Bills outstanding. The above backdrop suggests gross borrowing of dated securities will be higher thus implying 10Y in the range of 6-6.25%.

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KEY HIGHLIGHTS

- Gross borrowing in FY21 unchanged at Rs 12tn, H2 borrowing at Rs4.34tn.
- States to borrow Rs 2.02tn in Q3 after issuing Rs 3.05tn SDLs in H1.
- Centre's fiscal deficit estimated at 7.5% (of GDP).

Centre's borrowing calendar unchanged at Rs 12tn: Centre has not changed its borrowing calendar for FY21. With Rs 7.66tn already borrowed in H1 (Rs 4.25tn in H1FY20), borrowing in H2 has been pegged at Rs 4.34tn (Rs 2.85tn last year). Net borrowing in H2 is estimated at Rs 3.37tn compared with Rs 1.33tn last year. Apart from dated securities, Centre has borrowed additional Rs 5.6tn by way of T-Bills in H1 compared with Rs 1.25tn last year. This has helped it to meet the gap between revenues and expenditure which increased to Rs 8.7tn during Apr-Aug compared with Rs 5.5tn last year.

Maturity pattern skewed towards long-end: Issuance pattern is skewed towards higher maturity bucket of 10-year and above at 55% in H2FY21 compared with 35% in H2FY20. This to some extent justifies the term premium between short-end and long-end bonds. Issuances in 1-5-year category is now kept at 23% in H2FY21 compared with 25% in H2FY20. FRB issuances are pegged at Rs 240bn (5.5% of overall issuance).

Consolidated deficit estimated at 12% of GDP: Driven by sharp decline in centre's net revenue receipts (40% in FYTD21) and steady growth in spending (6.2% in FYTD21) centre's fiscal deficit has already reached 6.5% of GDP in Aug'20 (12MMA basis). We expect the deficit to increase to 7.5% of GDP backed by the need to spend to support growth in H2. In addition, the Centre may issue dated securities to repay some of the outstanding T-Bills. The uncertainty over the extent of issuances implies term premium will remain elevated. In addition, fiscal deficit of states is estimated at 4.5% of GDP which implies borrowing of ~Rs 8tn by states in FY21 out of which states have already borrowed Rs 3.05tn in H1 and plan to issue another Rs 2.02tn in Q3. While banks have been large buyers of dated securities, MFs have bought T-Bills. We expect 10Y yield to remain in 6-6.25% range in the near-term.

BANKING

30 September 2020

Lending rates dip in August

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Fresh lending rate of SCBs declines to 8.4%: As per latest RBI data, the weighted average lending rate (WALR) on fresh rupee loans sanctioned by scheduled commercial banks (SCB) declined 18bps MoM to ~8.4% in August, driven by a ~30bps fall in rates at private banks. Public sector (PSB) and private banks have reduced fresh lending rates by ~60bps and ~50bps respectively since Mar'20. Banks have been cutting MCLR on the back of lower policy rates, which has translated into lower fresh rates. The WALR on outstanding loans remained largely stable at 9.7%.

Term deposit rate down 10bps MoM to ~5.9%: The weighted average domestic term deposit rate of SCBs declined 10bps MoM to 5.9% in August. PSBs saw a fall of ~9bps MoM to ~6%. For private banks, rates dropped 11bps to ~5.9%, coming in below that of PSBs for the first time since Jul'17.

Spreads largely stable: Spreads for private banks and PSBs remained largely stable in August at 4.7% and 3.1% respectively as the reduction in outstanding lending rates was compensated for by lower term deposit rates. Spreads for private players are currently ~160bps higher than that of PSBs.

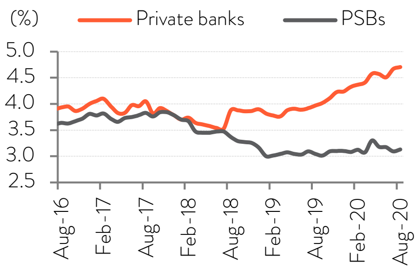
NIMs likely to remain steady for now: The median MCLR of SCBs remained largely stable at 7.4% in Aug'20. A bulk of the banking sector's loan portfolio is still linked to MCLR where both large/mid-sized private banks and PSBs have cut rates by 35-95bps since Jan'20. We believe that surplus liquidity coupled with tepid disbursements would translate into lower lending rates. This apart, banks would also begin to register the impact of repo-linked loans. While multiple negative variables are currently at play, we believe that banks are likely to mitigate pressure on NIMs by reducing deposit rates.

FIG 1 – MCLR OF BANKS DOWN >40BPS SINCE MAR'20

Banks	1-year MCLR (%)							Change (bps)
	Mar-20	Apr-20	May-20	Jun-20	Jul-20	Aug-20	Sep-20	Sep-20 over Mar-20
AXSB IN	8.1	8.0	7.8	7.8	7.7	7.6	7.5	(60)
HDFCB IN	8.2	8.0	8.0	7.7	7.5	7.4	7.3	(85)
ICICIBC IN	8.2	8.0	7.8	7.7	7.6	7.5	7.4	(75)
IIB IN	9.3	9.3	9.3	9.2	9.1	9.0	8.9	(40)
KMB IN	8.4	8.1	7.9	7.8	7.6	7.5	7.5	(85)
CBK IN	8.2	7.9	7.9	7.7	7.6	7.5	7.4	(80)
SBIN IN	7.8	7.4	7.3	7.0	7.0	7.0	7.0	(75)

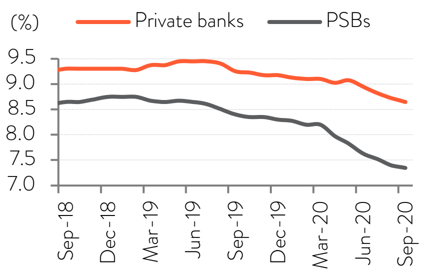
Source: RBI, BOBCAPS Research

LENDING SPREADS OF PRIVATE BANKS DECLINED IN AUG'20



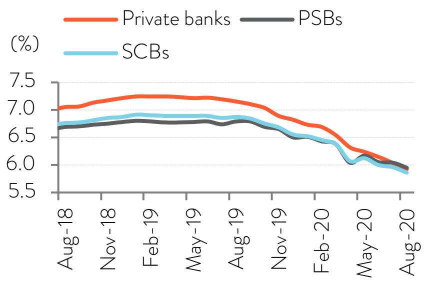
Source: RBI, BOBCAPS Research

MEDIAN MCLR STABLE



Source: RBI, BOBCAPS Research

TERM DEPOSIT RATES FOR SCBs DECLINED IN AUG'20



Source: RBI, BOBCAPS Research

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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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