L&T Financial Services

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1. Global economic briefs

- Several global analysts feel that expectations for tighter monetary policies across the globe have increased the risk of another major financial and economic shock. If monetary policies in advanced nations get tightened too soon or too fast – they risk choking off the synchronised global upturn currently under way.
- Jerome Powell will be making his first major public appearance as Fed chair when he gives the semiannual economic testimony before Congress on Feb 28th. This will be the next big catalyst markets would be watching, hoping the new central bank chair will be a referee in the tug-of-war between stocks and bonds.
- The CPB Global Trade Monitor data has shown global trade growth running at the strongest pace since the 2010, signaling a bounce back from the global financial crisis. Global import volumes were up 4.5% (y-o-y) in Dec-17 (vs. 2.6% in Dec-16 & 1.2% in Dec-15) reflecting a clear turnaround.
- On last Friday (Feb 23), the global rating agency S&P upgraded Russia and lifted its sovereign rating from BB+ to BBB-, with a stable outlook. According to the S&P press note, the upgrade reflects the track record of prudent policy response that has allowed the Russian economy to adjust to lower commodity prices and international sanctions. Fitch Ratings, which already has an investment-grade score for Russia, affirmed the rating at BBB- with a stable outlook on the same day.
- Euro zone consumer price growth slowed slightly in Jan-18 to 1.3% (y-o-y) but the core measure closely watched by the ECB edged higher to 1.2% (y-o-y) for the first time in months. On the other hand, Japan's core consumer inflation was steady at 0.9% (y-o-y) in Jan-18 in a sign a strengthening economy has yet to prompt companies to raise prices.
- Subdued inflation has forced the Bank of Japan to maintain ultra-loose policy even as the economic recovery gathers momentum, suggesting it will lag behind its global peers in normalising its monetary policy.
- The US will overtake Russia as the world's largest oil producer by 2019, according to the International Energy Agency (IEA). The US output would exceed 11 mln bpd by late 2018, as per the estimate of IEA.
- This week features wage and price growth data from the US, purchasing mangers' index prints from China, and a policy statement from South Korea's central bank following the country's quarter-on-quarter economic contraction at the end of 2017.

2. India: Agriculture and rural economic news

- India's rabi (winter) crop season has just concluded and as per the government data, total rabi sowing is marginally down by 0.8% (y-o-y) until Feb 9th. While sowing of oilseeds (-4.7%), wheat (-4.3%) & coarse cereals (-1.4%) witnessed a fall on year on year basis, sowing of rice (up 16.7%) and pulses (up 5.3%) showed a y-o-y increase.
- Rabi rice sowing has richly increased (y-o-y) in FY18, primarily on account of better water situation in Southern states this year, esp. in Tamil Nadu, Andhra Pradesh, Telangana & Kerala. Similarly, incentives provided through higher minimum support prices have increased the sowing of pulses in the states like Madhya Pradesh, Karnataka, Gujarat & Maharashtra.
- Top farm produce exporting countries - Canada, Australia, the EU and the US are irked with India's decision to raise the import duty on pulses and have questioned the government's move at the World Trade Organisation (WTO). India has clarified that the recent increase in tariff was based on the demand-supply equation and has not breached the WTO rules.

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3. India's overall economic & policy developments

- According to the US' Economic Report of the President (ERP), growth in India has slowed due to the effects of its structural economic reforms such as demonetisation and GST. The Report has also expressed concern over the risk posed by the increasing share of non-performing loan in India's banking sector. However, it believes that recently announced US$ 32.4 bln package to recapitalise publicly-owned banks will bring in some relief.
- In the recently released minutes of the RBI MPC's last policy meeting (held on Feb 7th), the MPC members expressed concern about continued inflationary risks, citing factors including high food and global crude prices and the government's decision to increase spending during FY19 (by postponing the fiscal consolidation roadmap) to support a struggling agricultural sector. But most also appeared mindful of wanting to see a stronger economic recovery, despite promising signs.
- According to the data by CMIE, India's investment climate during Apr-Dec, FY18 looks subdued with declining figures in announcements of new projects & the number of projects under execution.
- India's government is anticipating the GST portal to handle a load of up to 7.5 mln e-way bills in a day from 1st Apr, 2018, the likely date of e-way bill rollout for inter-state movement of goods, as per a report in the media.
- Majority of large investment firms have endorsed the RBI's new NPA Resolution Framework introduced on Feb 13, saying it ushered in transparent asset classification & disclosure standards and hence, should be viewed as structurally positive. However, they feel that the new framework could affect investor expectations negatively in the near term.
- According to the Rating Agency Fitch (which has a negative outlook on the Indian banking sector), India's new framework aimed at speeding up NPA resolution is likely to push up banks' credit costs and undermine earnings in the near term. Moreover, much of the recapitalisation amount will now be used up for resolution rather than growth.
- According to RBI, Indian banks loans and deposits rose at the pace of 11% and 5.7% on year respectively, as on Feb 2, 2018. While outstanding loans increased by Rs 939.7 bln to Rs 82.63 trln in the two weeks to Feb 2, aggregate deposits rose by Rs 131 trln to Rs 111.09 trln. The average Credit-Deposit ratio marginally dipped in the last reported fortnight to 74.39% as on Feb 2 from 74.42% as on Jan 19.
- India's Broad Money Supply, i.e., M3 growth continued to stay at a relatively higher 10.6% (y-o-y), as on Feb 2, 2018 (versus 6.2% a year ago) thanks to a noticeable pick up in bank credit to commercial sector in recent months and an increase in foreign exchange assets of the banking industry. But "cash withdrawals" from banks too have been increasing steadily. Between Mar 31st and Feb 2, "Currency with the Public" has grown from Rs 12.64 trln to Rs 16.68 trln reflecting an increase of Rs 4.04 trln. But during the past one year, term deposit growth has significantly decelerated from 11.5% to 5.2%.
- India's "foreign exchange reserves" reached the level of $421.72 bln as on Feb 16th on a healthy increase in the core currency assets and uptick in the gold stock. There has been a steady increase in India's foreign exchange reserves since the start of this year.

4. India's industrial & services sectors scenario

- India's central government is in the process of identifying coal blocks that could be offered for commercial coal mining to private players. Around a dozen coal blocks are identified so far with each having at least 50 mln of coal reserves. The coal ministry is likely to announce the final list of mines to be put on offer and the auction timeline by the end of Mar-18. The auction process is expected to be wrapped up by Mar-19.

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- To offset the impact of increase in customs duty, India's television manufacturers are set to increase the prices of LED/ OLED sets by up to 7%, which may impact the TV sales in the short-term.
- India's cotton imports this season (Oct-17 to Sept-18) might surpass the official estimate of 1.7 mln bales as textile mills are increasing buying cotton from the US in larger quantities, according to trade and industry sources. Though imported cotton is of slightly lower micronaire compared with the widely used domestic cotton, mills are opting for US cotton as these were free of contamination and realisation will be better.
- According to Care Ratings, India's fertiliser production may increase by 4% to 42.7 mt in FY18. Since the start of FY18, fertiliser production was subdued due to clearing of the stockpile up of inventory, in anticipation of the introduction of GST. However, the production has started increasing from the third quarter due to a restocking and preparation of Rabi sowing.
- Another study by Care Ratings shows an improved earnings performance by Indian companies in Q3, FY18 led by higher growth in sales as compared to growth in expenses, which in turn, was due to lower interest outgo. Another favourable factor was a lower level of effective tax rate.
- National Highways Authority of India (NHAI) has secured permission to raise up to Rs 700 billion by way of stock market instruments, according to India's Union Minister for Road Transport & Highways. He further said that the ministry was keen on tapping salaried class, senior citizens and other middle class people in NHAI's fund raising through bonds and other instruments in order to fund India's highway expansion projects.

5. Indian money market review last week

- India's weighted average call money rate (WACR) averaged at 5.94% last week (Feb 20-23) versus 5.89% in the week earlier (Feb 12-16), as liquidity in the banking system turned tight on account of GST outflows.
- While 91-day T-bill rate moved in the band of 6.30% to 6.33% last week, 364-day T-bill rate moved in the range of 6.58%-6.65%. On an average, while the yield on 91-D TB fell by two bps, that on 364-D TB increased by five bps.
- Three-month CP rate averaged at 7.89% last week. The average yield on this instrument too hardened marginally by two bps last week.
- Currently, liquidity in the banking system is estimated to be in a deficit of around Rs 400 bln.

6. Indian government bonds under pressure

- The 10-year GOI benchmark yield surged by nine bps last week to 7.67% as a sharp fall in INR versus US dollar eroded risk appetite and intensified fears of overseas investors pulling out from the Indian debt instruments.
- Another dampener to the G-Sec sentiment last week was the release of MPC minutes that showed heightened concerns over inflation.
- Government bonds have continued to stay under pressure this week too because of a surge in global crude prices and as risk appetite is subdued in a truncated trading week (as Friday is a holiday) with key events lined up. Market participation has remained muted ahead of the release of India's GDP growth data tomorrow for the quarter Q3, FY18 (as higher growth prints are expected to make RBI more hawkish). Market participants are staying on the sidelines ahead of the US Fed Chair's testimony tomorrow.

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7. Near-term outlook negative for INR

- INR depreciated by 0.8% last week to 64.73 per US dollar, as relatively more hawkish FOMC minutes added to the dollar's strength.
- At present, it is hovering between 64.91-64.92 per US dollar. The dollar index has steadied above 89.50 levels ahead of the new Fed chief's first congressional testimony.
- According to Forex experts, worries of US rate hikes & consequent rally in US yields coupled with uncertainties due to the PNB episode have brought back pressure on the INR, which has now broken through crucial 64.80 levels seen earlier. According to the Bloomberg news, Deutsche Bank AG and Mizuho Bank Ltd. are forecasting more losses for INR, as a widening trade deficit and capital outflows amid a bank fraud sour the sentiment for the currency.

8. Indian equities to seek direction from macro data & global cues

- Global financial markets ended last week with modest gains. Back home, Indian indices too made modest gains of 0.4% on a spurt in metals and pharma stocks even as banking stocks continued to face selling pressure due to the fraud saga.
- This week, Indian equities are expected to seek direction from macro data (India's Q3 GDP release) and global cues (US Fed Chair's testimony), as the results (earnings) season is almost over. Losses in banking stocks and caution before GDP data continue to weigh on market sentiment. Also, the movement of funds and crude oil prices are expected to influence the market sentiment, going forward.

9. Brent crude at $67.18 per bbl today (Feb 27)

- Today, the price of Brent oil is at $67.18 and the US WTI crude is at $63.80 per barrel. Crude oil prices moved higher late last week after Libya declared force majeure over contracts at its Elephant, or El-Feel, oil field following labor strikes.
- The Organization of the Petroleum Exporting Countries (OPEC) has decided to extend cuts in oil output by nine months to March 2018. The cuts are likely to be shared again by a dozen non-OPEC members led by top oil producer Russia, which reduced output in tandem with OPEC from Jan-18.
- However, US shale output is also growing strongly and coming at a time when other major producers have been withholding output to prop up prices. Many global analysts expect energy supply growth to outpace demand growth and set a backdrop for well-supplied fossil fuel markets during 2018.

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