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**BWR द्रिश्टिकोण**

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# Economy's slow start needs to accelerate

August 2019

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## World Bank solidly backs India's growth, though at a slower pace

In the July 2019 edition of Global Economic Prospects, World Bank cited that India's growth remains solid, supported by improved confidence, slowing inflation and still robust investment. The report suggests the economy to grow a slower pace than in 2018, although investment growth is expected to remain robust as benefits of recent policy reforms further materialize. Further, the report also projects the growth to accelerate to 7.5% in FY 2019-20, on the back of support from monetary and fiscal policies.

The Union Budget and the Economic Survey projects the government's vision towards a USD 5 trillion economy by next few years. But, it needs sustained real GDP growth rate of 8% to reach that. It expects creation of virtuous cycle of savings, investment, exports and employment for the medium term towards achieving the targeted levels. However, recent data on most of the high frequency indicators point to slowdown in investment activity and moderate private consumption growth.

Industrial growth, measured by the Index of Industrial Production (IIP), moderated in May 2019, pulled down by manufacturing and mining even as electricity generation picked up on strong demand. Automobile sales continue to be under pressure owing to weak consumer sentiment from rising cost of ownership in terms of higher insurance and registration costs. Government's emphasis on electric vehicles is putting further pressure on the industry. Declining auto sales also hamper demand for steel. In telecom industry, Jio overtook Airtel to become the second largest carrier in June 2019 in terms of subscribers. Power supply position improved in June 2019; but, the country is still not in a power surplus position with continuing stress on discoms' financials. Cement demand expected to pick up due to increased government spending on infrastructure upgrade. Airline passenger growth revived with capacity additions and other airlines redeploying grounded aircraft of Jet Airways.

Despite the consecutive policy rate cuts by MPC, the transmission of rate cuts remains elusive. The headline inflation trajectory remains within control. Bond markets have witnessed positive sentiments with steady rupee followed by fall in crude prices. Looking ahead, bond markets is likely to mirror the rupee and oil trajectory, the fiscal target & borrowing plan and the US Federal Reserve's policy regime.

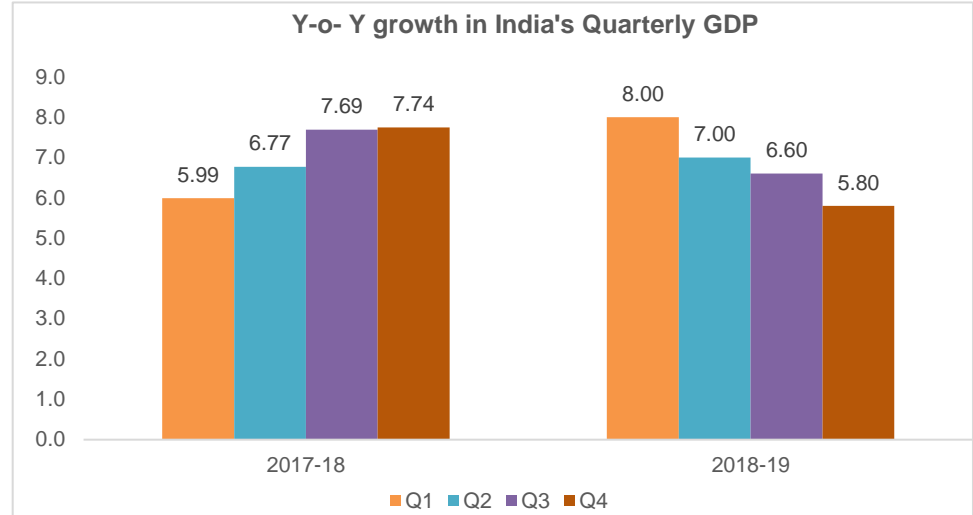
## MACRO-ECONOMIC INDICATORS

### Economy trends

#### BWR Views

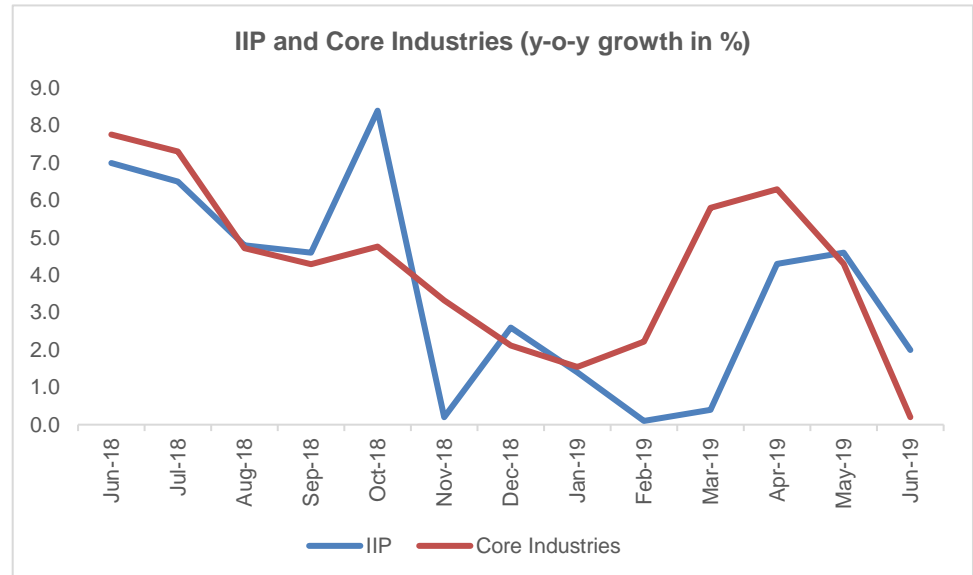
The economy is expected to improve in the current fiscal and grow at a rate of 7.0% taking support from monetary and fiscal policies. Slowdown in economic activity, characterized by muted performances in both IIP and Core sector growth signal need for immediate policy measures to revive growth.

The domestic economy seems to have slowed with the quarterly GDP growth coming down as can be seen in the charts with the full year GDP growth rate being revised downwards to 6.8%. The above growth trends were also reflected in the Eight Core Industries and IIP recent data releases which also point towards a slowdown.



Source: MOSPI, BWR Research

### Performance in Core Industries and IIP



Source: MOSPI, eaindustry.nic.in, BWR Research

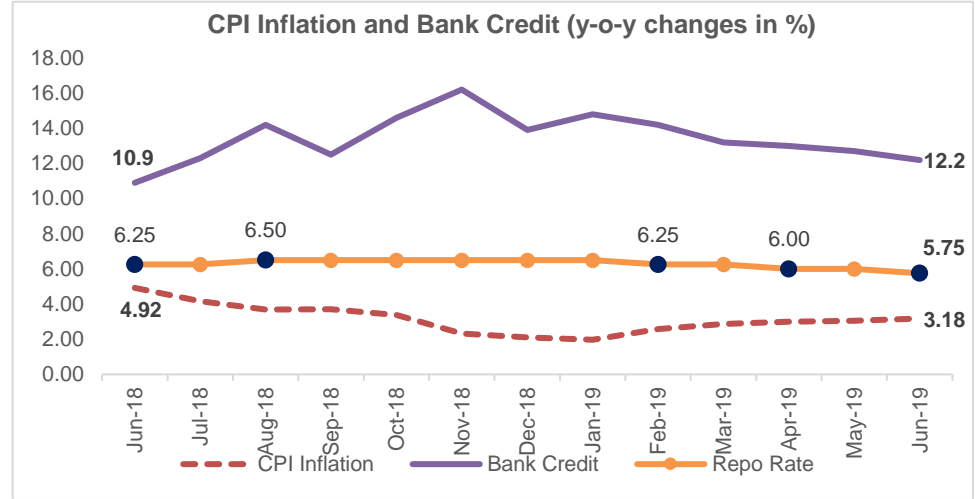


**BWR Views**

The decline in crude oil prices expected to keep the inflation benign in 2019-20 and RBI is likely to continue with accommodative stance. The monetary policy easing is expected to revive credit growth which has otherwise remained muted so far in 2019, witnessing poor transmission of rate cuts. So, the critical issue here is further transmission of the rate cuts down the line.

**Inflation and low bank credit growth**

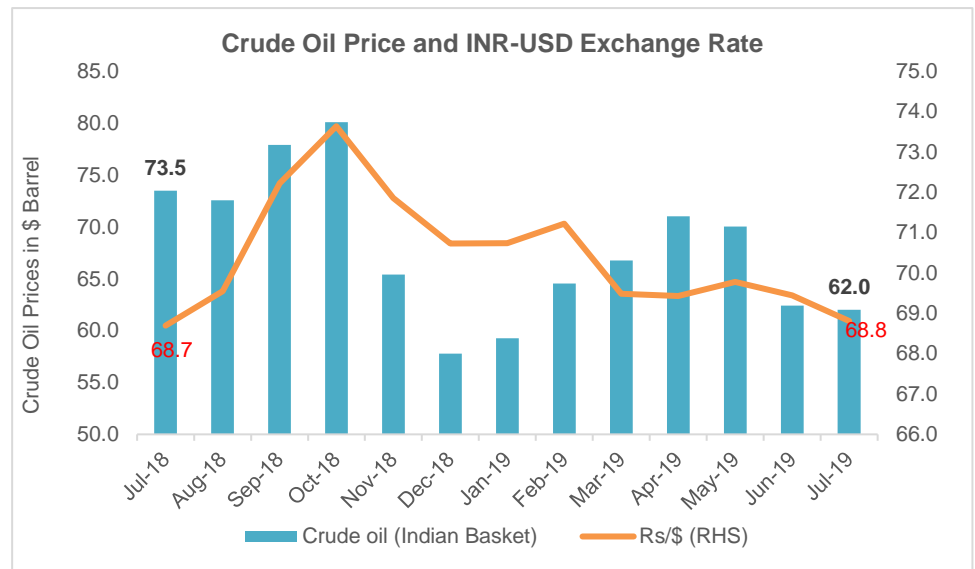
CPI inflation moderated to 3.18% in June well within the targeted level of RBI at 4% (+/-2%) providing support to an accommodative monetary policy. The credit growth, however, has not picked up speed and may do so in the latter quarters.



Source: MOSPI, RBI, BWR Research

**Crude oil Prices and stable INR/USD rates**

Rupee remained stable supported by falling crude oil prices in July 2019. The US -China trade woes and with a lower global economic growth, the demand for oil is expected to come down.



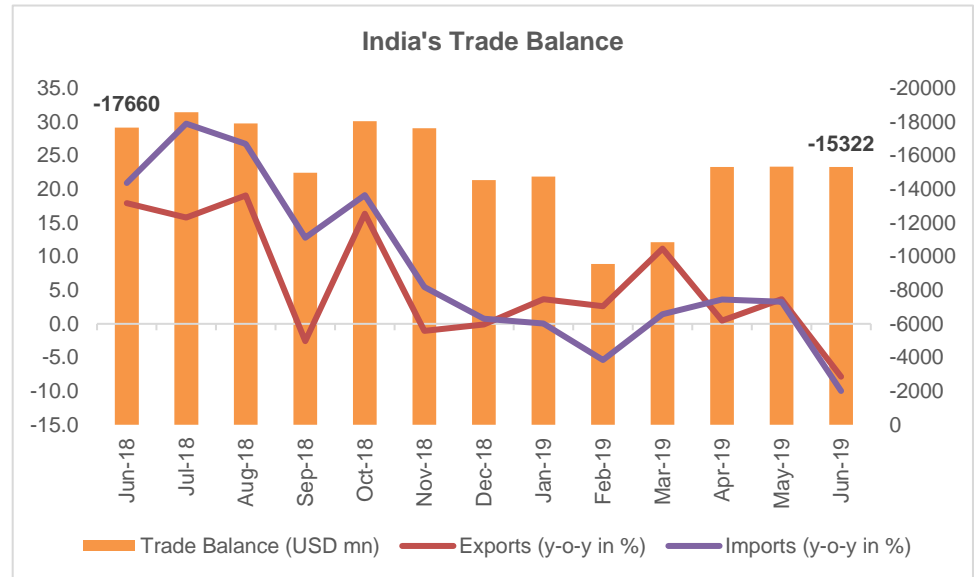
Source: Ministry of Petroleum & Natural Gas, FBIL, BWR Research

**BWR Views**

Stable rupee and crude oil prices helped a lower trade deficit at US\$ 15.3 billion in June 2019 as compared with US\$ 17.6 billion a year ago. If the trend continues this would help the economy to manage fiscal situation and current account deficit well in 2019-20.

**Improving Balance of trade**

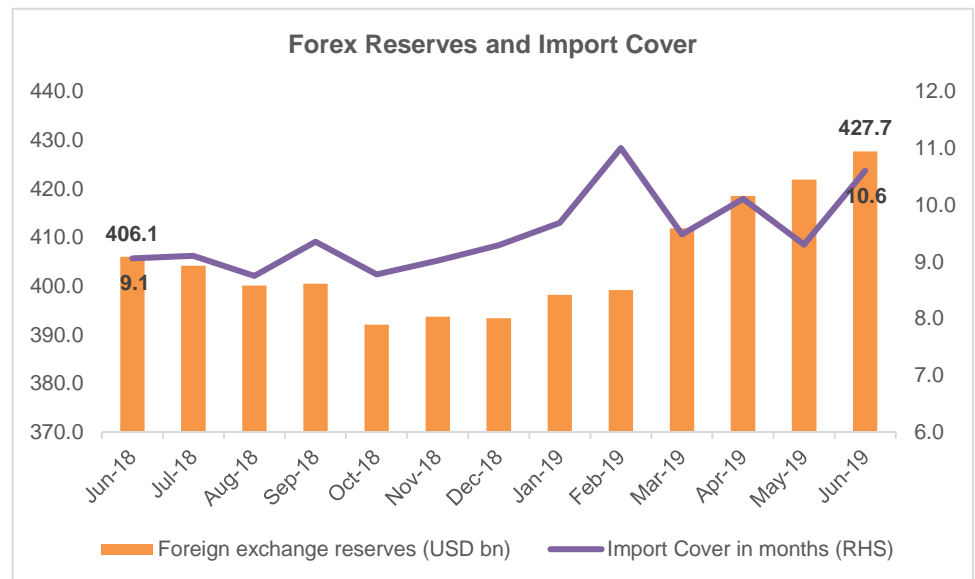
The trade deficit narrowed by 13% (y-o-y) during June 2019 helped by falling crude oil prices and a stable rupee. Exports of goods fell (7.9%) due to huge reduction in re-exports of petroleum products and non-petroleum products, while imports of goods fell (10%) with deceleration in gold imports and crude oil imports.



Source: Ministry of Commerce, BWR Research

**Forex Reserves and Import Cover**

Forex reserves increased by USD 5.8 billion to reach USD 427.7 billion in June 2019 sufficient to cover 10.6 months of imports.



Source: Ministry of Commerce, RBI, BWR Research

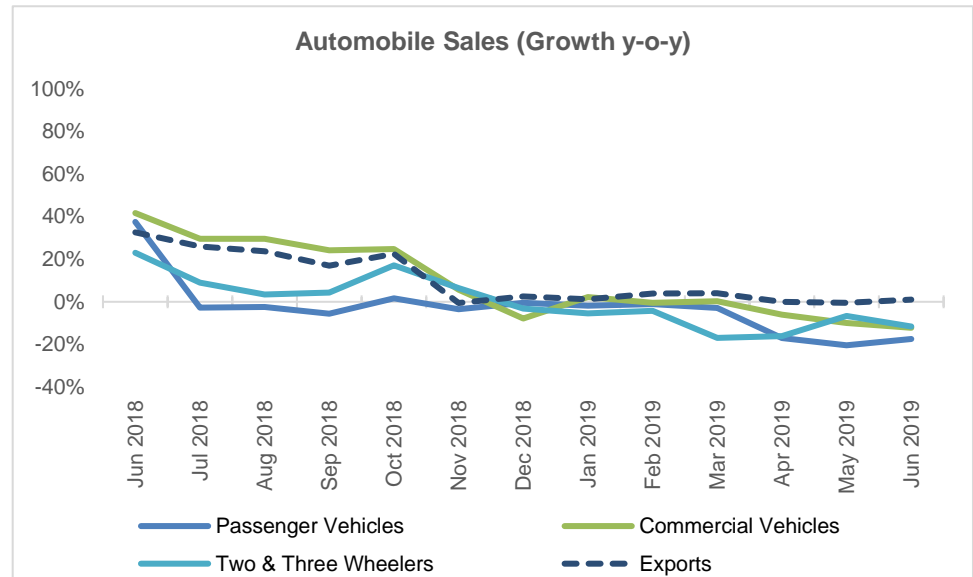
## SECTORAL INDICATORS

### Automobiles

Domestic automobile sales fell by 12% y-o-y in the month of June 2019 driven by weak sales of passenger vehicles. High cost of ownership due to increased insurance and registration cost has hampered the passenger vehicles and two-wheeler sales. Revised axle norms and financing issues due to NBFC crisis have hit the commercial vehicle sales.

#### BWR Views

Vehicle sales are expected to remain under pressure till H1 FY20, post which commercial vehicles might see an uptick due to pre-buying by fleet owners before the BS-VI norms kick in from FY21.



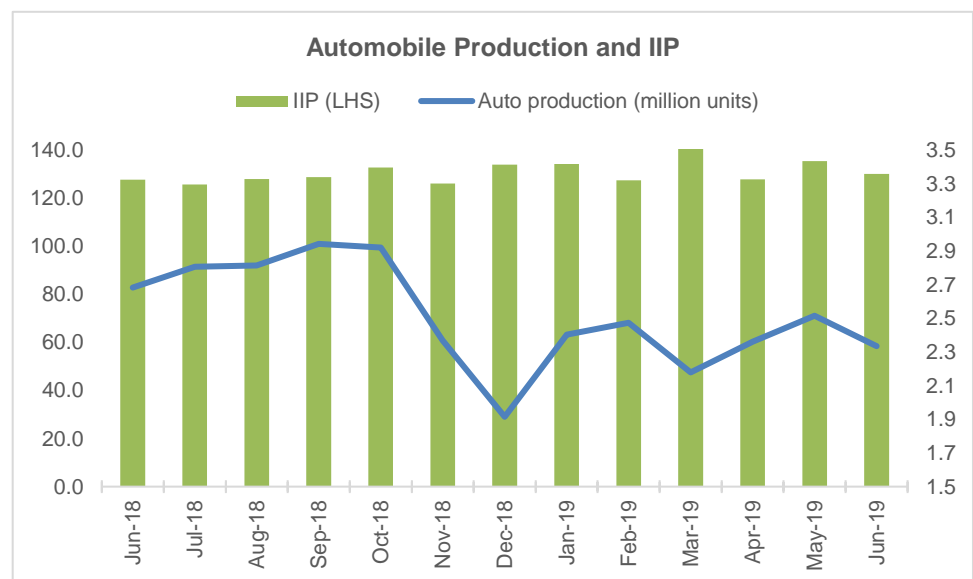
Source: CMIE, BWR Research

### IIP and Automobiles

Domestic automobiles production declined by 13% y-o-y in the month of June 2019 due to production cut downs by manufacturers on account of huge inventory build-up occurring from falling sales. Slowdown in auto production is in line with overall decline in IIP growth. This has also affected adversely the ancillaries and automobile dealers.

#### BWR Views

Slowdown in vehicle sales has resulted in huge inventory build-up. Therefore, production cut down is expected to continue in the coming months until inventory at the dealer level eases.



Source: MOSPI, CMIE, BWR Research

## Telecom

Consolidation of the market continues with Jio increasing its market share and driving the overall subscriber additions in the sector. As on May 31, 2019, the market share of Vodafone-Idea was 33.4% followed by Reliance Jio at 27.8% and Bharti Airtel at 27.6%. Reliance Jio overtook Airtel to become the second largest telecom carrier in India.

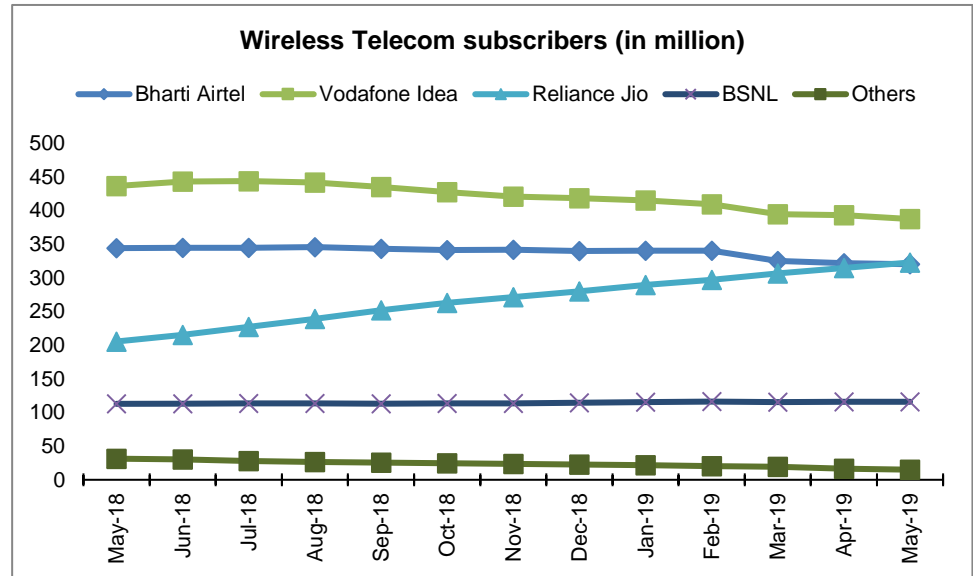
While, Reliance Jio has been substantially adding new subscribers, the same for Airtel has been very slow and in contrast Vodafone-Idea has been losing subscribers.

### BWR Views

Reliance Jio is expected to increase its market share going forward. Players to continue to feel pressure on their profitability.

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Source: TRAI, BWR Research

The sector currently has only three major players who have all recently declared their Q1 FY20 results which are not encouraging for the sector as a whole. While, Reliance Jio continues to be profitable, it has been reporting declining ARPU for the last 7-8 quarters.

On the other hand, Airtel and Vodafone are struggling with significant losses and falling subscriber base. All the players have adopted various loyalty measures to retain their subscribers and add new customers. However, unless the tariffs are increased, any improvement in the performance over the medium term is unlikely to happen.

## Power

### BWR Views

Power sector may continue to witness stress due to stalled projects.

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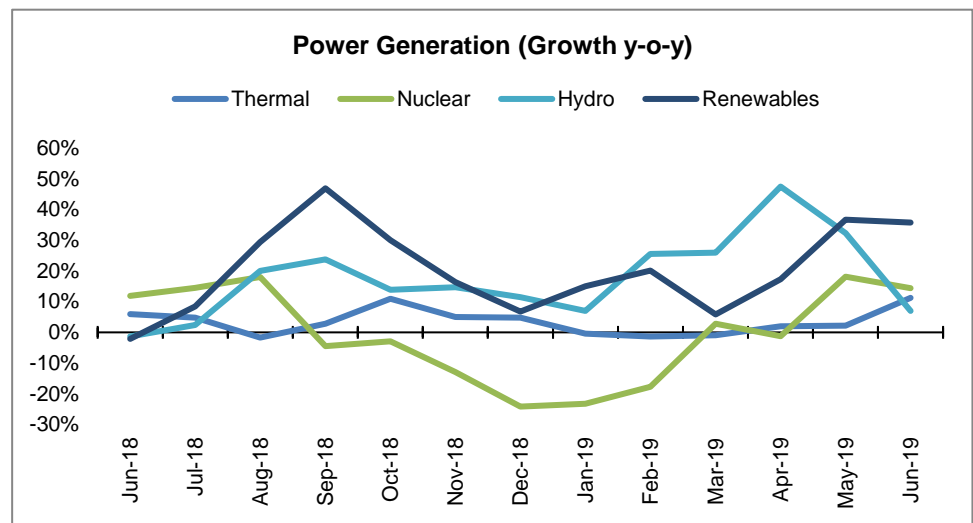
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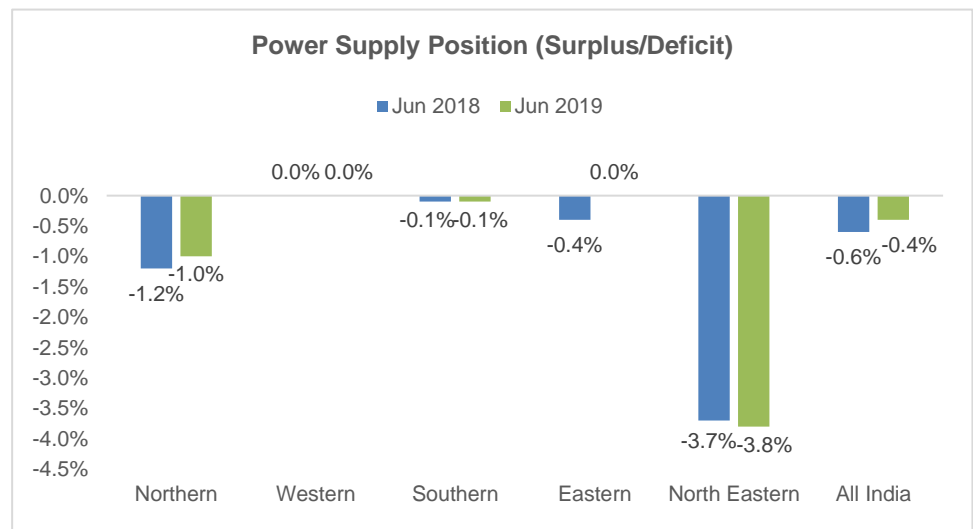
Power generation in hydro show a healthy growth this year compared to thermal in terms of conventional energy sources. Thermal power producers has been facing challenges in terms of coal availability. On the other hand, renewable sources continue to show strong growth. Although, the Government has been promoting and incentivizing setting up of renewable energy plants, the investor sentiment has been consistently declining.

The tariffs have already fallen considerably (with the introduction of auction system for both Solar and Wind); now Andhra Pradesh Government has also set up a committee to renegotiate Power Purchase Agreements (PPAs) in order to bring down the power purchase cost. While, this has its own set of legal challenges, it will further hurt the investor sentiment as these Independent Power Producers (IPPs) were promised certain return on their investment while setting up these plants and this move compromises the same. If the other states also follow suit, it will prove to be disastrous for the clean energy dream of the current Government.



Source: Central Electricity Authority, BWR Research

India's power supply position improved in June 2019, but country is still not a power-surplus nation. The deficit is primarily due to DISCOMS stressed financials on account of its mounting losses and huge debt burden.



Source: Central Electricity Authority, BWR Research



**BWR Views**

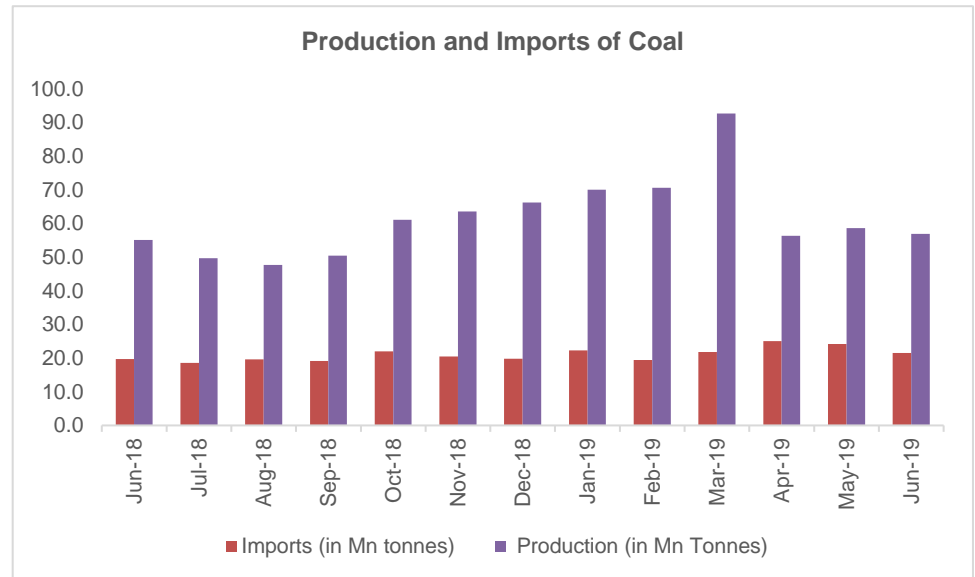
In the domestic market coal-fired power generation capacity is expected to rise due to increase in demand and lack of alternative fuels by power generation companies. The central government is planning to auction more than 41 new coal blocks soon to augment this demand.

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**Coal**

India imports nearly 20 million tonnes of coal compared to 60 million tonnes of domestic production on an average. During June 2019, domestic production of coal increased by 3.2% whereas imports have risen by 9% y-o-y. Globally, coal prices have been declining since July 2018, due to weak global growth and lower demand.



Source: CMIE, BWR Research

**BWR Views**

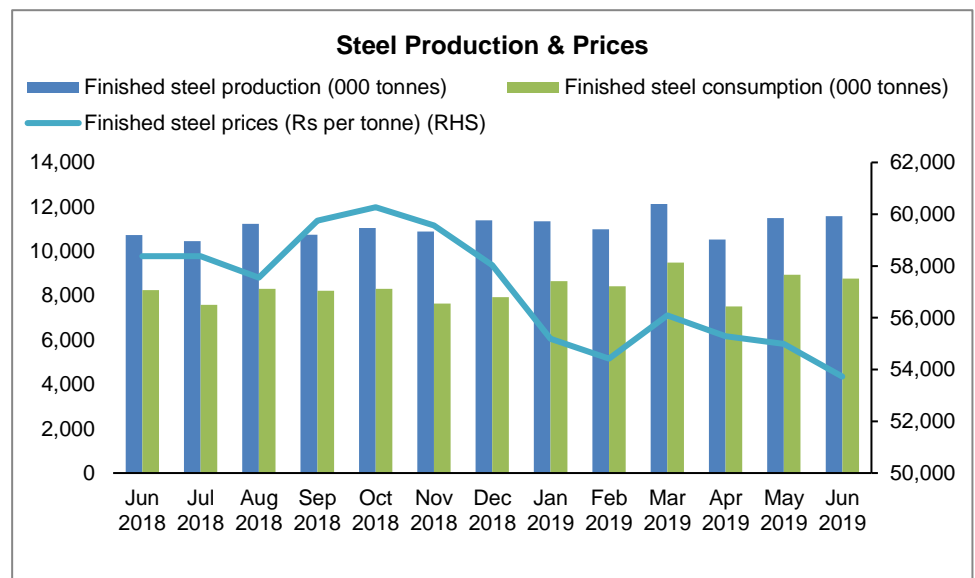
Steel prices are expected to remain muted in H1 FY20 owing to continued slowdown in the automobile, housing and infrastructure sectors. In addition to this trade tensions between China and US may further put pressure on prices.

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**Steel**

Steel prices are on a declining trend after October 2018, owing to subdued industrial activity in the country visible in declining infrastructure & construction activity and lower automobile sales.



Source: CMIE, BWR Research

**BWR Views**

Going forward cement prices may find support from governments' focus on infrastructure segments such as road and railways and rural & affordable housing. Pradhan Mantri Awas Yojana – Gramin (PMAY-G) aims to achieve the objective of “Housing for All” by 2022. Pradhan Mantri Gram Sadak Yojana (PMGSY-III) is envisaged to upgrade 1,25,000 kms of road length over the next five years, with an estimated cost of Rs. 80,250 crore.

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**BWR Views**

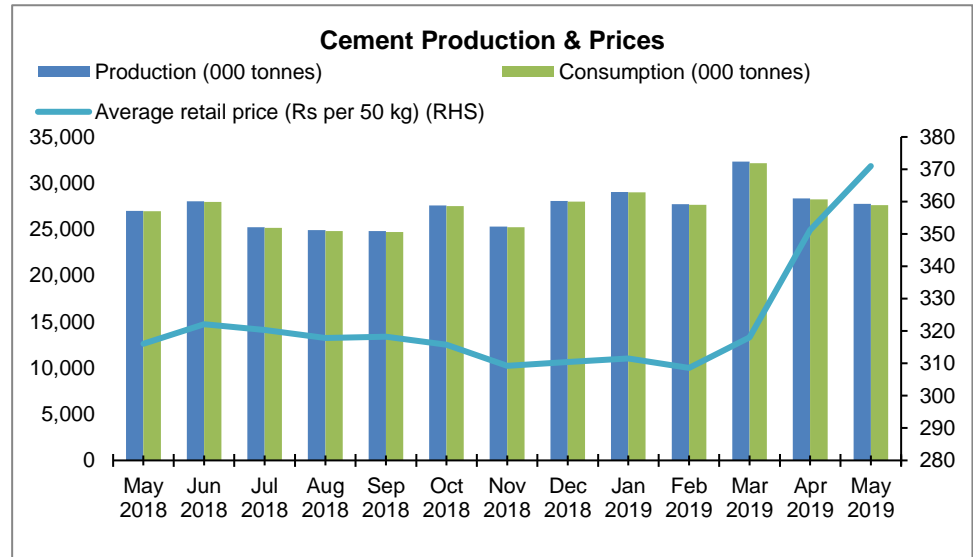
Domestic air passenger traffic in India is expected to grow in the single digits this fiscal, mainly because of a capacity shortage caused by the grounding of Jet Airways.

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**Cement**

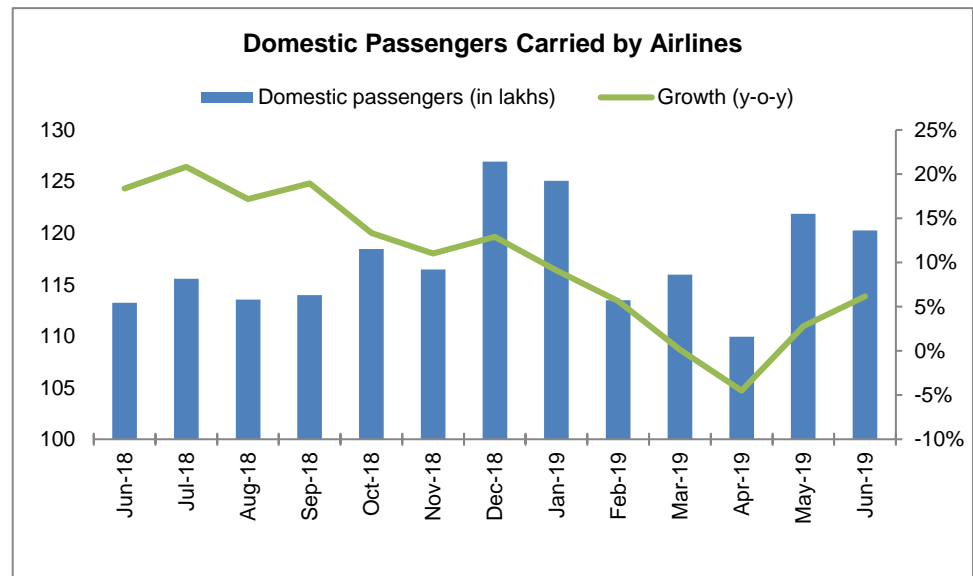
Cement prices have remained range bound in 2018-19. From March 2019, dealers have raised the prices in anticipation of healthy demand going forward. However, the price may not be sustainable due to weak seasonal demand.



Source: CMIE, BWR Research

**Airlines**

Domestic air passengers grew by 6% y-o-y in the month of June 2019. This is a revival in growth after a decline in April 2019 and a slowdown since the start of the year. This revival in growth was aided by capacity additions by the players and also due to other airlines redeploying grounded aircraft of Jet Airways.



Source: DGCA, BWR Research

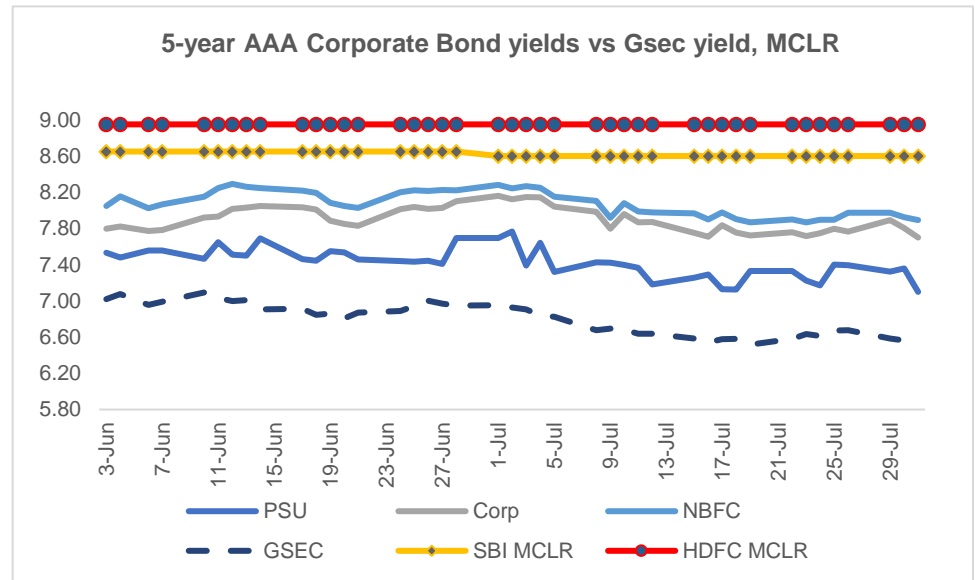
## DEBT MARKET INDICATORS

### Movements in Bond Yields

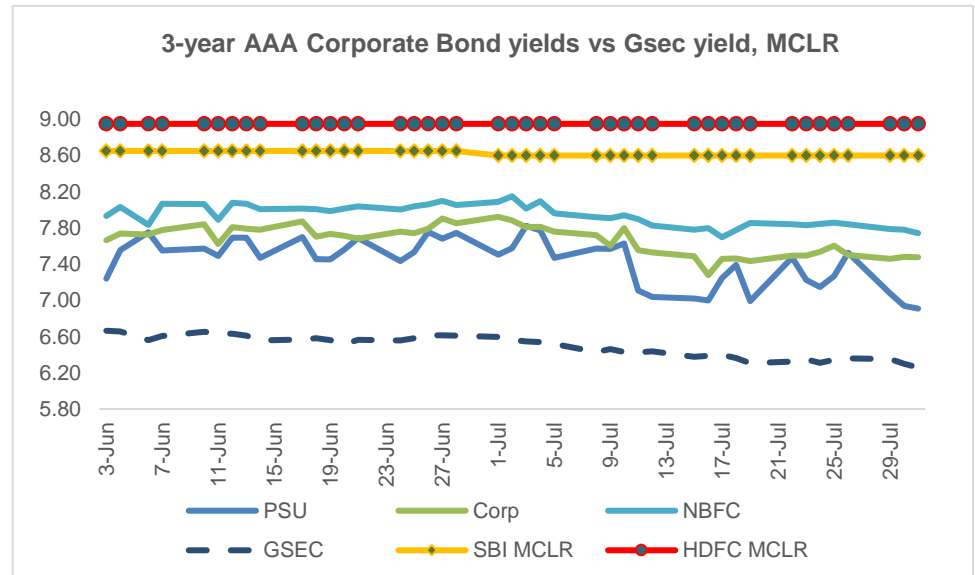
#### BWR Views

Yields of shorter tenor corporate bond have eased due to moderation in crude oil prices amid expectation of RBI's easing rate cycle to continue.

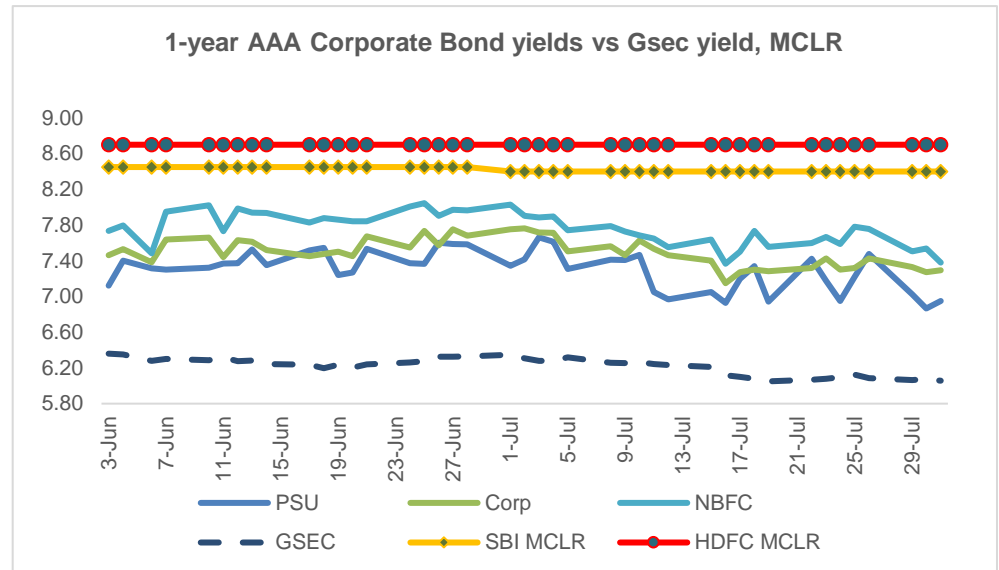
Bond yields (annualised) of Public Sector Units (PSUs), Corporates and Non-Banking Finance Companies (NBFCs) maturing in 1-year, 3-year and 5-year period with corresponding Government Securities and Bank Marginal Cost of funds based Lending Rate (MCLR) are provided below.



Source: FIMMDA, SBI, HDFC, Brickwork Research



Source: FIMMDA, SBI, HDFC, Brickwork Research



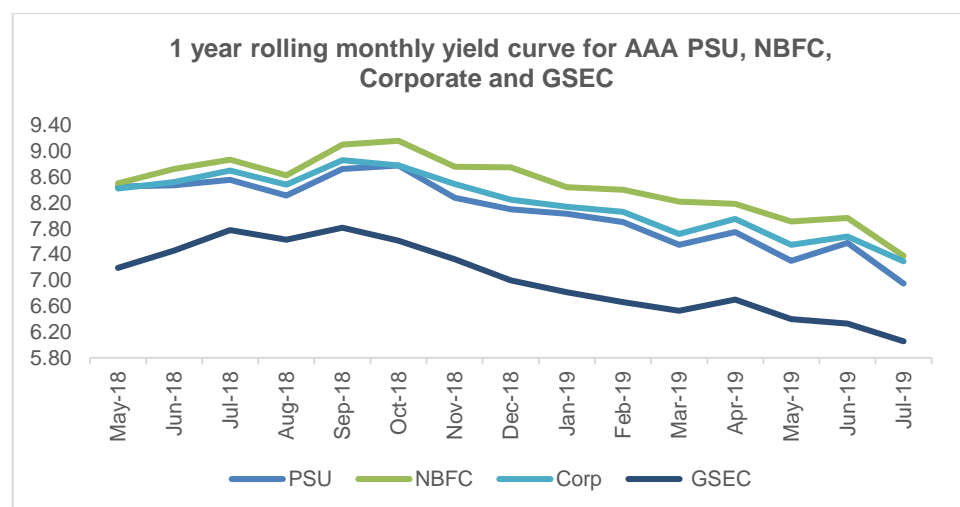
Source: FIMMDA, BWR Research, SBI, HDFC

The yields of AAA rated corporate bonds maturing in 1-year, 3-year and 5-year have eased by 12-21, 13-26 and 7-17 basis points respectively in the month of July compared to June due to better liquidity in the bond market amid infusions by Reserve Bank of India. Infusion of huge liquidity by Central Bank through Open Market Operations (OMOs) as and when required also supported this easing trend and could result in increasing supply of new bond issuances

The bonds across the said categories witnessed improving investor sentiments on the back of anticipation of easing policy rates to continue and falling crude oil prices.

### Monthly yield curve of AAA PSUs, NBFCs, Corporates and Gsec

The monthly yields of Government Security maturing in 1 year compared with Corporate bonds yields of PSUs, NBFCs and Corporates with similar maturity time buckets have witnessed downward trend due to softening of interest rates post RBI-MPC repo rate cuts. This is expected to lower the cost of borrowing for Issuers.



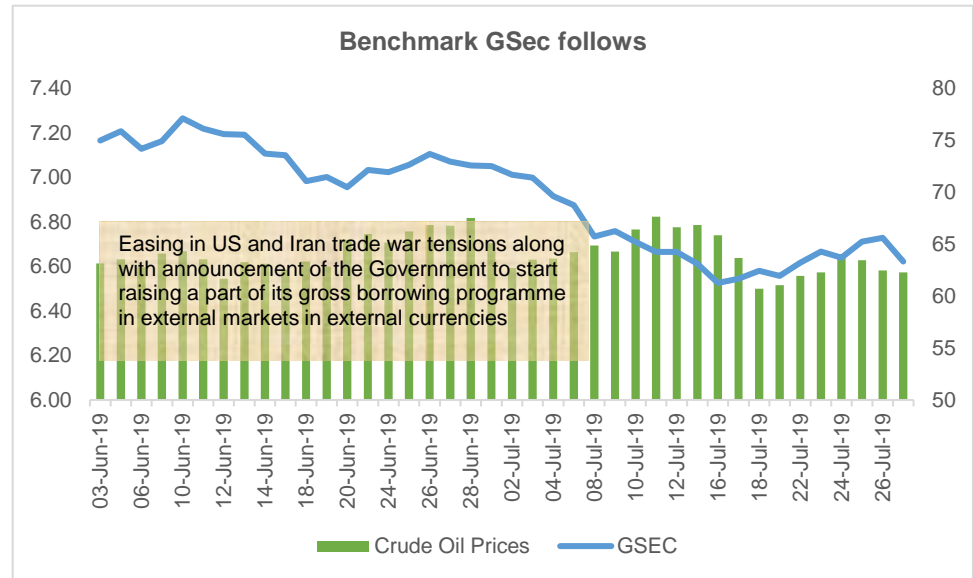
Source: FIMMDA, BWR Research

## Lower Brent Crude Oil directs the Indian Government Securities

The recent fall in Brent Crude oil prices has reflected in the easing of yields, thereby, boosting positivity in the bond market. The average crude oil prices saw a sharp fall in the month of July to USD 63.98/ barrel as against previous month's average of USD 64.33/barrel.

### BWR Views

Recent sharp fall in the crude oil prices helped easing domestic yields. Global cues continue to influence the Indian bond market.



Source: U.S Energy Information Administration, BWR Research



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