Ecowrap

'Be the Bank of Choice for a Transforming India'

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ARE WE IN A STATE OF QUASI GROWTH SLOWDOWN?

Are we currently facing a quasi growth slowdown? The apparent nervousness is clearly reflected in the trends exhibited in key stock indices. Initial trends in Q4FY19 exhibit overall decline in sectors such as Telecom Equipment & Infra Services; Agro Chemicals; Petrochemicals; Infrastructure Developers & Castings, Forgings & Fasteners. Pharmaceutical companies dependent on exports are likely to report poor growth numbers. In Q4FY19, of 384 companies more than 330 companies exhibited negative growth in mid-line and bottom-line. Perhaps, significantly depressed rural prices is disturbing rural income and weak demand is affecting the FMCG sector.

Behind the veil of corporate results, one issue that is engaging attention of the market is the recent data issues. For example, the existence of shell companies in MCA 21 has reinvigorated the debate of the veracity of GDP numbers. However, we would like to draw a similar analogy with the fact that all transactions, whether legitimate or illegitimate, form a part of GDP estimates and hence shell companies will not change GDP numbers, purely going by definition. Additionally, we would also like to point out the significant data difference between estimates given out by independent agencies in public domain, like say CMIE and Projects Today. For example, Government investment estimates by CMIE is lower by a staggering Rs 7 trillion compared to Projects Today! Let these numbers be also a part of a comprehensive data debate!

Leaving aside this debate, consumption demand is also showing signs of moderation as revealed by various leading indicators. Automobile sector has also shown lackluster performance with domestic sales, production and export all witnessing deceleration in growth. Also, percentage of leading indicators of both urban as well as rural demand showing acceleration has significantly reduced in recent months. Moreover, our Composite Leading Indicator (CLI) which has a one-quarter lead over non-agricultural GDP growth, is signaling a contraction in GVA for Q4 FY19 towards 6%. Interestingly, food inflation and retail inflation in general have not picked-up despite increase in MSP. For NBFCs, relying more on borrowed funds with limited capital, there seems to be more of solvency issue rather than a liquidity crisis being faced by the sector. Even the mutual fund industry is witnessing decline in investment flows. Though credit growth has picked-up after dipping in FY17, but it has not been broad based with credit offtake seen mostly in Government and high rated customers.

Overall, we still believe the current slowdown could be transitory, if proper policies are adopted in interregnum. For example, the current high real interest rates are severely acting as an impediment to investment. We are thus penciling a larger rate cut (in excess of 25 bps) by RBI in the forthcoming policy. However even such larger rate cuts will not help fully, but its transmission will. To this end, the RBI should now ensure that asset and liability side of the Banks move in tandem and ensure repo rate is directly benchmarked to non volatile bank liabilities /CASA that are mostly used for transaction purposes! Otherwise, we would continue to be constrained by lack of transmission.

GROWTH SLOWDOWN

- Recent data of IIP has disappointed with production data contracting in Mar'19 after a gap of 21 months. This shows declining momentum of both investment and consumption. Even core industries productions of steel, electricity, coal and cement are falling or have been stagnant in recent quarters.

INVESTMENT SCENARIO

- New Investment projects announcements have declined continuously in last four years to Rs 9.76 lakh crore in FY19 from Rs 20.86 lakh crore in FY15. It is pertinent to mention that share of private sector investment has increased to 66% in FY19 from 44% in FY15.
- Interestingly, data from *Projects Today* reflects increase in projects announcement in FY19 to Rs 17.25 lakh crore from Rs 12.16 lakh crore in FY18. However, the moot point is that the number of investment projects announced has slowed down during last couple of years. Further, majority of new investment announcement is in the areas such as Transport Services which includes Road, Railways etc., mainly driven by the Government.
- Investment intention, as measured by IEM filed, reported negative growth thrice during the last five-year period. Though it has improved by 16% in CY18 to Rs 4.58 lakh crore as compared to CY17, the same is still below CY13 level of Rs 5.29 lakh crore.

New Investment Projects Announcements

Year	Amount (Rs Trillion)		Growth Rate (%)	
	CMIE	Projects Today	CMIE	Projects Today
FY15	20.86	15.26		
FY16	19.97	14.61	-4.3	-4.2
FY17	16.30	14.25	-18.4	-2.5
FY18	11.65	12.16	-28.5	-14.7
FY19	9.76	17.25	-16.2	41.9

Source: CMIE; Projects Today; SBI Research

CMIE & Projects Today Difference: New Investment Projects Announcements (Rs Trillion)

Year	A. CMIE		B. Projects Today		GAP (A-B)	
	Govt.	Private	Govt.	Private	Govt.	Private
FY15	11.62	9.24	9.61	5.65	2.01	3.60
FY16	10.08	9.89	9.68	4.93	0.40	4.96
FY17	8.31	7.99	10.17	4.08	(1.86)	3.90
FY18	5.44	6.21	8.23	3.92	(2.79)	2.29
FY19	3.33	6.44	10.24	7.01	(6.91)	(0.57)

Source: CMIE; Projects Today; SBI Research

CONSUMPTION DEMAND SCENARIO

- Not only is the investment demand slowing down but consumption demand is also showing signs of moderation as revealed by various leading indicators.
- The automobile sector is witnessing a decline in growth. SIAM data for domestic sales, production and export growth all indicate a slowdown. For passenger vehicles, domestic sales growth has declined to a mere 2.7% in FY19 compared to 7.9% in the previous fiscal. Meanwhile, their production growth eased to 0.1% from 5.8% in FY18. In case of commercial vehicles, production growth has increased to 24.2% in FY19 from 10.2% in FY18, however, sales growth has declined to 17.6% from 20% in FY18. Export growth of automobiles has also witnessed declining growth momentum from the past two years.
- FMCG sector is also showing lacklustre performance in recent quarters with deceleration in demand for consumer staples, such as biscuits, soaps, oil.
- The leading indicators, when grouped into rural and urban consumption, reveal a serious slowdown in both areas. Percentage of indicators of rural and urban consumption showing acceleration has fallen in recent months (50 in Jan'19 to 30 in Feb'19 in case of rural and 38 to 25 in case of urban consumption demand).
- Moreover, our Composite Leading Indicator (CLI) which has a one-quarter lead over non-agricultural GDP growth, is signaling a contraction in economic activity for Q4 FY19. The CLI Index (a basket of 32 leading indicators) is based on monthly data which shows the early signals of turning-points in economic activity.
- Based on the leading indicators yoy performance, we are expecting the GDP growth to be around 6.1%-6.2% in Q4 FY19. Among the Leading Indicators, the growth of Passenger Vehicle, Railway Traffic, Cargo traffic, Electricity Generation and Manufacture of Capital Goods are showing declining trend during the Q4 FY19.

TRANSMISSION OF MSP ON FOOD INFLATION

- Post Announcement of MSP, prices of almost all crops, except Mustard and Nigerseed, have shown a sign of price increase (min of 3.6% to max of 37.7%) but its impact on food inflation is very minimal.
- Decline in retail inflation in the past few months suggest that rural demand is not picking up despite efforts by the Government to increase farmer income through higher MSP. Procurement data published by NAFED suggests that procurement agencies could not procure even half of the quantity sanctioned by Centre's Department of Agriculture, Cooperation and Farmers Welfare (DAC&FW) at MSP, thereby the impact on food prices and rural demand remain low in many States.

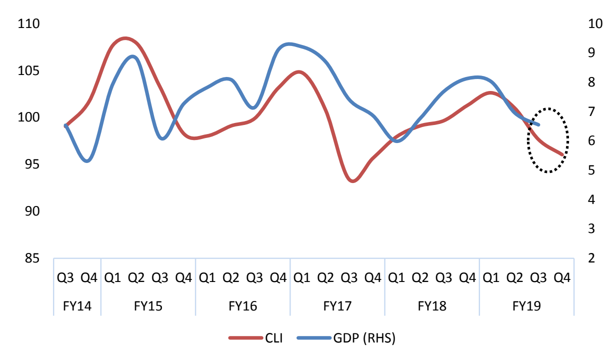
NBFC FACING SOLVENCY ISSUES

- NBFC sector is facing liquidity squeeze since second half of FY19 after a few of the big NBFCs defaulted on their obligations. For NBFCs relying more on borrowed funds with limited capital this seems to be more of solvency issue rather than a liquidity crisis.
- In H2FY19, share of Investment by Mutual Funds in NBFCs CPs has also declined from 11.31 % in Jul'18 to 7.70% in Feb'19. However, it has increased marginally in Mar'19 to 8.13% (i.e. Rs 1.06 lakh crore).

Rural Consumption							
% y-o-y	2018				2019		
	Q1	Q2	Q3	Q4	Jan	Feb	Mar
Consumption							
Consumption: Diesel	9.6	3.6	2.8	1.9	6.3	2.7	1.4
Consumer Non Durables	10.7	2.0	6.1	4.7	3.3	4.3	
Currency in Circulation	56.5	30.1	23.0	20.2	19.1	18.5	16.8
Rural wages	3.3	3.3	3.4	3.8	3.7	3.7	
Two Wheelers	25.2	16.1	5.1	7.4	-5.2	-4.2	-17.3
Tractor sales	43.0	25.2	5.5	21.1	2.4	-0.5	-15.0
% of indicators showing acceleration	83	67	33	50	50	33	
Urban Consumption							
% y-o-y	2018				2019		
	Q1	Q2	Q3	Q4	Jan	Feb	Mar
Passenger Vehicle	13.2	21.6	-3.6	-0.8	-1.9	-1.1	-3.0
Consumer Durables	7.1	8.1	8.3	6.1	2.3	1.2	
Petroleum: Consumption:Petrol	13.5	8.7	6.6	7.8	13.3	8.1	7.2
Telecom Service: # of Subscribers	0.1	-4.0	-1.9	0.2	2.4	2.2	
Passenger Traffic: All Airports	20.3	17.2	16.1	10.6	8.4	4.5	-1.1
Credit Card transaction	30.5	32.2	31.9	31.5	32.5	28.6	29.9
Urban wages (construction workers)	3.5	3.0	2.3	3.3	3.4	3.8	
Consumer credit	19.4	18.5	16.7	17.0	16.9	16.7	16.4
% of indicators showing acceleration	75	63	50	38	38	25	

Source: SBI Research, Green shading suggests the fastest growth since 2014, while Red suggests the slowest growth since 2014

Graph: CLI vis a-vis GDP



Source: SBI Research

Movement of Crop Prices Post MSP Announcement			
Crops		Apr'19 Mandi Prices over MSP (%)	Mandi Prices (Apr'19 over Jul'18, %)
Cereals	Wheat	10	6.4
	Paddy	16	3.6
Coarse Cereals	Barley	18	14.9
	Jowar	-8	10.9
	Bajra	3	32.3
	Maize	16	32.2
	Ragi	-6	37.7
Pulses	Gram	7	18.7
	Masur	27	12.1
	Arhar	-9	25.6
	Moong	-15	15.6
	Urad	-5	22.3
Oilseeds	Mustard	-10	-3.6
	Soyabean	10	11.0
	Groundnut	2	24.9
	Seasamum	60	26.5
	Nigerseed	-26	-2.7
	Cotton	15	11.4

Source: AGMARKET, SBI Research Note: *: MSP for 2019-20

MATURITY PROFILE AND WIDENING SPREAD

- ♦ Maturity profile of mutual fund holdings in NBFCs paper, as on Mar'19, shows more than 50% of the same (Rs 1.08 lakh crore) is going to mature in Q1FY20.
- ♦ The average spread between the sovereign 10-year paper and AAA rated corporate bonds has started widening since Sep'18. It has gone up from 76 bps in Aug'18 to 133 bps in Feb'19. The spread, when calculated against 3-year paper, has shot up from 73 bps in Aug'18 to 177 bps in Mar'19. Though the same has started softening since Apr'19, with the maturity of NBFC papers of more than Rs 1 lakh crore in the Q1 FY19, it will be important to see how the same are being rolled over and at what cost.

GROWTH IN AUM SLOWING DOWN

- ♦ The growth in investment flows to mutual funds is declining. The quarterly growth in Asset under Management (AUM) which was as high as 35% in Jun'17 has come down to 3.2% in Mar'19. Month-wise data on Net inflows to Mutual fund also shows there is larger outflow than inflow during Feb'19 and Mar'19. However, in Apr'19 the net inflows have become positive and we believe this positive inflows may continue in coming months.

CORPORATE RESULTS – EARLY TRENDS

- ♦ Of 384 companies, only 46 companies exhibited topline growth. More than 330 companies reported negative growth in top, mid and bottom-line. Going forward, initial trends suggest most of the companies may exhibit negative growth trends. Sectors such as Telecom Service, Pharma, Automobiles, Mining are likely to be affected.

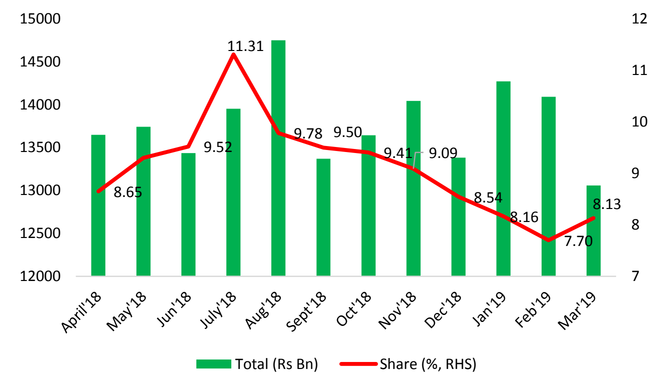
ISSUES IN DATA DISCREPANCY

- ♦ The latest debate on using the MCA-21 database thus overstating the GDP numbers may find some resonance in the slowing investment, IIP, falling core inflation numbers, however, the fact that all companies registered under MCA-21 contribute to GDP growth has to be taken into account.
- ♦ The existence of shell companies in MCA 21 has reinvigorated the debate of the veracity of GDP numbers. However, we would like to draw a similar analogy with the fact that all transactions, whether legitimate or illegitimate form a part of GDP estimates and hence shell companies will not change GDP numbers, purely going by definition. Additionally, we would also like to point out the significant data difference between estimates given out by independent agencies in public domain, like say CMIE and Projects Today. For example, Government investment estimates by CMIE is lower by a staggering Rs 7 trillion compared to Projects Today! Let these numbers be also a part of larger data debate!

WAY FORWARD

- ♦ Overall, we still believe the current slowdown could still be transitory, if proper policies are adopted in interregnum. For example, the high real interest rates are severely acting as a impediment to investment. To this end, we are thus penciling a larger rate cut (in excess of 25 bps) by RBI in the forthcoming policy. However such larger rate cuts will still not help fully but transmission will. To this end, the RBI should now ensure that asset and liability side of banks move in tandem and ensure repo rate is directly benchmarked to non-volatile bank liabilities /CASA that are mostly used for transaction purposes! Otherwise, we would continue to be constrained by lack of transmission.

Graph: Deployment of Debt MF in CPs of NBFC

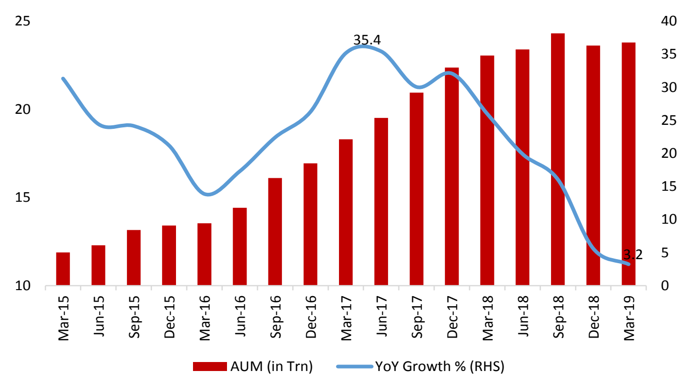


Source: SBI Research

Mutual Fund Holdings in NBFC papers - Maturity Profile as on Mar'19					
Description	Less than 90 days	90 days to 182 days	182 days to 1 year	1 year and above	Total
CP	95,709	4,231	6,191	-	1,06,131
Bond	13,034	13,778	17,433	66,264	1,10,509
Total	1,08,743	18,010	23,623	66,264	2,16,639
Share	**50.20**	**8.31**	**10.90**	**30.59**	**100**

Source: SEBI; SBI Research

Graph: Quarterly Trend in AUM (Rs trillion & % Growth)



Source: SBI Research

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