# ECOWRAP

भारतीय स्टेट बैंक
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'Be the Bank of Choice for a Transforming India'

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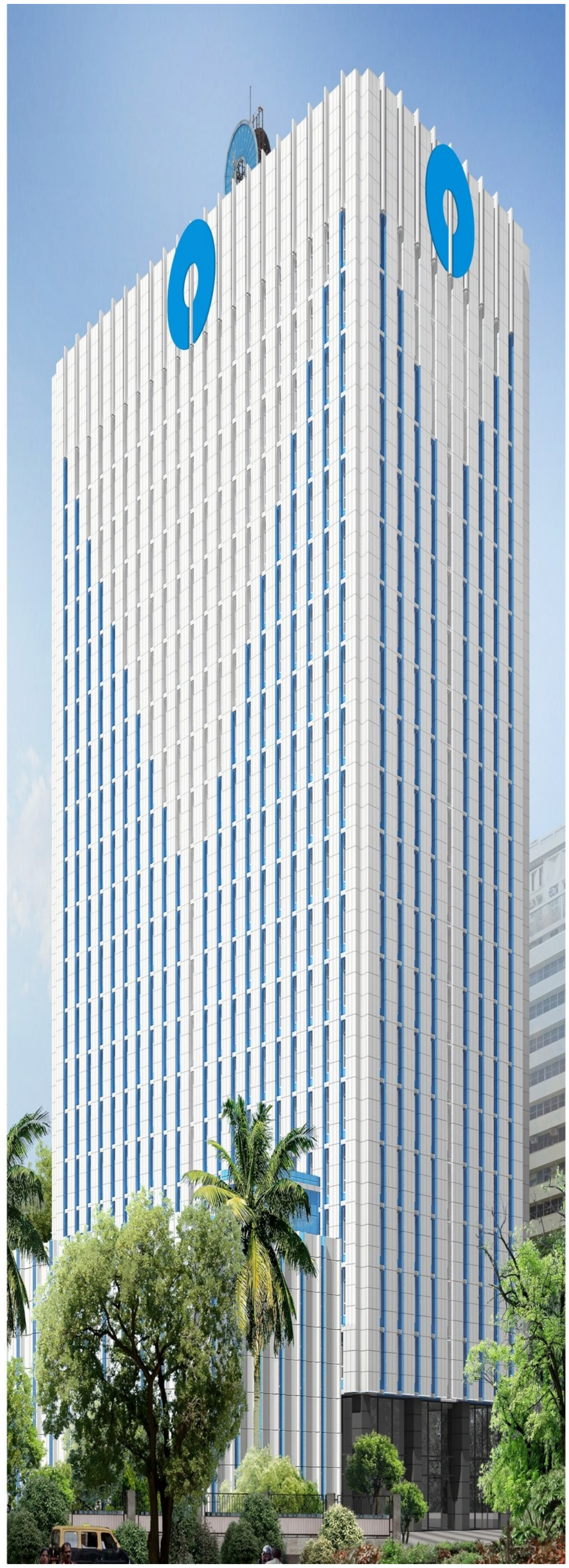


## A RATE PAUSE MOST LIKELY FROM RBI BUT DON'T RULE OUT A SURPRISE ON FEB 7

We now expect RBI to change stance in February, but it is likely to remain on a pause mode. The first cut might happen in April 2019, but we believe it will be shallow rate cut cycle. However, we will not be overtly surprised if the RBI delivers a 25bp rate cut on February 7 itself.

There are indeed reasons to believe why RBI might just prefer to cut in February rather than / in addition to in April annual policy.

*First,* headline inflation still remains significantly benign (to remain likely so till Aug'19) and growth has hit a soft patch. Sharp revisions in GDP growth in FY17 and FY18 imply a sub 7% figure in FY19, clearly implying that we are currently in a slowdown mode. Also, inflation might have just bottomed out in December. *Second,* credit growth has declined for the second fortnight in January, implying that incremental credit growth data available till December is showing significant decline, which might have continued in January. This is not encouraging and is evident for Services, despite improvement in credit to NBFCs in December. However, most encouraging is Credit to MSE sector, which has seen good growth in December due to Government recently launching an MSME Outreach Programme. NBFCs primary issuance of corporate bond for the 3 month ended December has declined by Rs 25,168 crore. This rapid decline in 3-months may have shifted to banks credit portfolio. Bank credit to industry has jumped by Rs 47,700 crore during the same period. But bank results have been a turning point!

*Third,* general elections in April may perforce a rate cut earlier than April.

*Fourth,* global growth is slowing down across continents. For example, correction in property prices in Canada and Australia is the latest indicator of such, though there is still not a consensus on US!

However, the factors that militate against a rate cut could be the high rural core that has still not found entirely convincing explanations. We expect RBI to clearly state in policy that it intends to look through such high core just as it did for the Housing component when Pay Commission recommendations were announced.

The other factor is obviously an expansionary budget. Apart from the FY19 numbers being overtly ambitious, and hence FY20 numbers more of a ritual, an additional amount of Rs 79,604 crore will have to be raised in the remaining four months of this fiscal from small savings, apart from Rs 19,000 through dated borrowings! Clearly, the last word has not been said on the fiscal front yet!

## OUR BASE CASE IS HOLD, BUT RATE CUT NOT RULED OUT IN ENTIRETY

- The forthcoming review of monetary policy will happen in interesting times. The Interim Budget 2019-20 has set the tone for general election and fiscal arithmetic of the budget is quite puzzling. Growth is expected to gather momentum and inflation trajectory will remain on the higher side in Q4 compared to Q3/Q2 FY19.

## INFLATION

- CPI inflation eased to almost 18-month low to 2.19% in Dec'18 mostly by deflation in Pulses and products (-7.1%) and Vegetables (-16.1%), Sugar and Confectionery (-9.2%) and Eggs (-4.3%) but strangely, Core CPI inflation increased to 5.73% in Dec18 due to huge jump in health (9.0%) and education (8.4%) inflation. The most puzzling aspect of the inflation data is the increase in rural health and education inflation at the time when rural demand is collapsing. Urban core CPI has declined to 5.26% during Dec'18. Such contrarian movement in urban core and rural core is bemusing as over a 7-year period, correlation between the rural and urban core was at 0.85. In the past Rural and Urban Core have moved in opposite directions on only two occasions and such period of recurrence was 4-5 months.
- A deep analysis of this completely contrarian behavior shows that it could be due to change in methodology from Sep'18 in terms of data collection in rural areas where, as against the earlier practice of collecting data through Post Offices, the NSSO is now collecting data itself. There may also be changes in the specifications of a product, which might be causing changes in numbers.
- However, the new data collection methodology adopted by CSO might also be resulting in better price discovery that was hitherto absent. This contradictory behaviour needs explanations. RBI would do well to take cognizance of the situation and look deeper into CPI numbers. Looking at Headline numbers is not always a preferred strategy since sometimes headline numbers are largely impacted by other components.
- We are now concerned that this data aberration could obfuscate policy choices. **Even though we expect a hold in February policy, but RBI may surprise the market with a rate cut that may not be negated .**

## GOVERNMENT BORROWING & FISCAL MATH

- Deviating from fiscal consolidation path, fiscal deficit for FY19 and FY20 is pegged at 3.4% of GDP. The Budget estimates 11.5% nominal GDP growth rate for FY20 (same as the previous year). Assuming a 7.5% real GDP growth rate, this translates into an inflation of around 4.0%. This seems to be quite realistic.
- However, the tax revenue projections do not seem to be realistic despite their downward revision. The tax revenue projections have been revised downward by Rs 23067 crore, due to reduction in CGST collection by Rs 1.00 lakh crore. Though some compensation in tax revenue shortfall is sought from increased projection of Corporation and Customs Tax, the data from CGA shows even the revised projections seem to be bordering on the aggressive side.
- For example, Corporation tax actual collection till Nov'18 is around 43% of the revised annual estimates. This translates into an average monthly collection of Rs 36,407 crore. However, the Government is expecting that in the Dec-Mar period, the average monthly collections will be Rs 94937 crore. The Corporation Tax growth rate has been projected at a reasonable 13% for FY20. However, the inflated revised estimates for FY19 cast a shadow on next year's estimates.
- For GST also the, despite the reduced estimates, the target appears optimistic (60% of the revised estimates achieved till Nov'18). How much IGST has the Centre kept and how much it is going to allocate to states will only be clear after March.
- Fiscal arithmetic of FY20 is largely dependent upon FY19 numbers. Since FY19 numbers are optimistic given the trends in revenue and expenditure so far, the FY20 numbers look reasonable. However, once the numbers for FY19 are revised downward, the FY20 projections will swell.
- As far as market borrowings are concerned, Government has increased the projected gross borrowing figure by an effective Rs 19,000 crore. The FY20 estimates are also on the higher side with Rs 7.1 lakh crore gross and Rs 4.73 lakh crore net borrowing. Moreover, the issuance of securities against small savings has been increased to Rs 1.25 lakh crore for FY19 as against the budgeted Rs 75,000 crore (FY20 at Rs 1.30 lakh crore).

- So far only Rs 45,396 crore has been raised through small savings during Apr'18-Nov'18. Thus the additional amount of Rs 79,604 crore will have to be raised in the remaining four months of this fiscal. Coupled with Rs 19,000 crore additional market borrowing, the yields may see an uptick. Thus the fiscal situation is likely to remain under pressure going forward.
- The subsidy trends are also not encouraging. Given the current rate of expenditure on various subsidies, the revised numbers for FY19 look conservative. For example the food subsidy rate per month is Rs 17807 crore. This translates to additional expenditure of Rs 71229 crore, in next 4 months. However, going by the revised estimates, only Rs 28,840 crore are required to be spent. This means that if the current pace of food subsidies is maintained, a significant amount may be rolled over to next year.

## BANK RESULTS & FUTURE INSIGHTS

- Loan loss provisioning rose sharply in 2017-18 due to elevated levels of GNPAs and time-bound referrals of large delinquent accounts to the National Company Law Tribunals (NCLTs) under the IBC. The provision coverage ratio (PCR) accordingly showed improvement across bank groups and crossed 52% for ASCBs in H1FY19. As a result of higher provisioning, PSBs has incurred net losses to the tune of Rs 854 billion, while PVBs and FBs continued to report net profits. Since 2015-16, provisioning by PSBs has consistently exceeded their operating profit or earnings before provisions and taxes (EBPT), resulting in net losses.

**Performance of Selected Banks: Net Profit & Gross NPA**

| Banks | Net Profit (Rs Crore) | | | Gross NPA (%) | | |
|---|---|---|---|---|---|---|
| | Q1 | Q2 | Q3 | Q1 | Q2 | Q3 |
| HDFC Bank | 4601 | 5006 | 5586 | 1.33 | 1.33 | 1.38 |
| Yes Bank | 1260 | 965 | 1002 | 1.31 | 1.6 | 0.78 |
| Axis Bank | 701 | 790 | 1681 | 6.52 | 5.96 | 5.75 |
| Indusind Bank | 1036 | 920 | 985 | 1.15 | 1.09 | 1.13 |
| ICICI Bank | 67 | 909 | 1605 | 8.81 | 8.54 | 7.75 |
| SBI | -4876 | 945 | 3955 | 10.69 | 9.95 | 8.71 |
| Bank of India | 95 | -1156 | -4738 | 16.66 | 16.36 | 16.31 |
| PNB | -940 | -4532 | - | 18.26 | 17.16 | - |
| Bank of Baroda | 528 | 425 | 471 | 12.46 | 11.78 | 11.01 |

Source: SBI Research

- However, in the Q3 FY19 banks, especially PSBs, has come up with a pleasant numbers who have so far declared their results. There are only a few PSBs, which on account of making one time huge provisions, could not show positive net profit numbers.

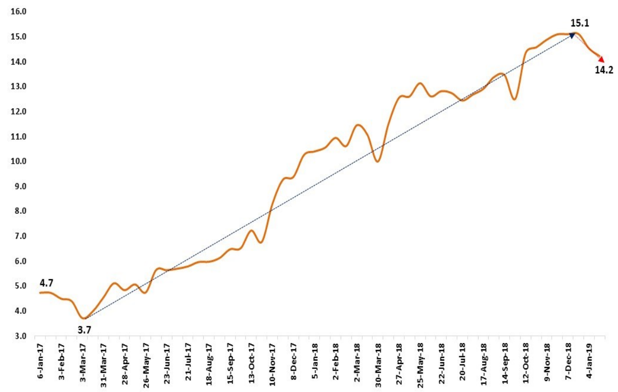
## ELECTIONS COULD PREPONE THE RATE CUT

- Apart from the high Government borrowing estimates for FY20, the schedule of General Election in Apr/May is the another factor that may also be looked at by RBI for any policy decision.

## BANK CREDIT GROWTH INDICATING A DECLINING TREND IN JAN'19

- The ASCB data for the fortnight ended 18 Jan'2019 indicates that on YTD basis, Aggregate deposits grew by 4.9% or Rs 5604 billion (2.1% or Rs 2203 bn last year) and advances by 8.2% or Rs 7062 billion (4.2% or Rs 3279 billion). On YoY basis, Aggregate deposits grew by 9.2% or Rs 10,084 billion (5.1% or Rs 5328 billion) and Advances grew by 14.2% or Rs 11623 billion (10.6% or Rs 7798 billion). **This is the second consecutive fortnight when the credit growth has declined.**

**ASCBs Credit Growth (YoY %) Trend**




Source: RBI, SBI Research

- A deeper analysis of sectoral data indicates that there was not much credit off-take happening till mid-Aug 2018, but since then there has been a substantial amount of credit off-take beginning September and continuing till December. Of total incremental credit expansion of Rs 5.1 lakh crores in current fiscal, Rs 4.2 lakh crores is accounted for in 4-months ended December.

- Incremental credit growth that had slowed down in October (0.2 times of September indicating churn in demand) has again picked up robust pace in November (3.3 times of October) but declined significantly in December (0.7 times of November). This is not encouraging and is clearly evident for Services, despite marginal improvement in credit to NBFCs in December.
- Credit to Industry has continued to accelerate in November and December after a lackluster October, with 'infrastructure', 'chemical and chemical products', 'all engineering', 'vehicles' and 'petroleum, coal products & nuclear fuels' accelerating. However, credit growth to 'basic metal & metal product', 'textiles', 'food processing' and 'gems & jewellery' decelerated/contracted.
- Despite marginal improvement in credit to NBFCs in December, credit to services sector has declined significantly. Credit to MSE sector has seen good growth in December due to Government's recently launched MSME Support and Outreach Programme, which will run for 100 days covering 100 Districts throughout the country.

**Sector-Wise Credit Flow (Rs bn)**

| Sectors | Loan Outstanding | | | | | | Growth | | | | | | Growth in Sep, Oct, Nov & Dec (Rs bn) |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | Mar-18 | Aug-18 | Sep-18 | Oct-18 | Nov-18 | Dec-18 | April1-Aug (Rs bn) | Apr1-Sep(Rs bn) | Apr1-Oct(Rs bn) | Apr1-Nov(Rs bn) | Apr1-Dec (Rs bn) | % YTD | |
| **Agri. & Allied** | **10302** | **10419** | **10544** | **10597** | **10648** | **10821** | **117** | **242** | **295** | **345** | **519** | **5.0** | **402** |
| **Industry** | **26993** | **26621** | **27016** | **26962** | **27084** | **27494** | **-372** | **24** | **-31** | **91** | **501** | **1.9** | **873** |
| MSE (Priority) | 9964 | 9881 | 9945 | 9961 | 9957 | 10047 | -83 | -19 | 64 | -7 | 84 | 0.8 | **166** |
| **Services** | **20505** | **20740** | **22014** | **22081** | **22538** | **22330** | **235** | **1509** | **1576** | **2033** | 1825 | **8.9** | **1590** |
| NBFCs | 4964 | 4902 | 5467 | 5626 | 5663 | 5709 | -62 | 503 | 662 | 699 | 746 | 15.0 | 808 |
| **Personal Loans** | **19085** | **19924** | **20200** | **20386** | **20662** | **20997** | **840** | **1115** | **1301** | **1577** | 1912 | **10.0** | **1073** |
| Housing (Including Priority) | 9746 | 10419 | 10502 | 10623 | 10774 | 10966 | 673 | 757 | 878 | 1029 | 1220 | 12.5 | 548 |
| Other Personal Loans | 5080 | 5309 | 5431 | 5480 | 5582 | 5714 | 229 | 351 | 400 | 502 | 634 | 12.5 | 405 |
| **Gross Bank Credit** | **77303** | **78191** | **80250** | **80574** | **81652** | **82413** | **888** | **2947** | **3272** | **4349** | 5110 | **6.6** | **4221** |

Source: SBI Research

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## ABOUT US

The Economic Research Department (ERD) in SBI Corporate Centre is the successor to the Economic and Statistical Research Department (E&SRD). The latter came into being in 1956, immediately after the State Bank of India was formed, with the objective of "tendering technical advice to the management on economic and financial problems in which the Bank has interest and which required expert analysis".

After the first reorganization of the Bank, when specialized departments like Management Science, Management Information Systems, Planning and Market Segment Departments took over the statistical work of E&SRD, the Department was renamed as ERD.

However, with the ERD team now taking on multidimensional functionalities in the area of risk management , corporate analytics, strategy and so on, who knows, the time may have come to rename it again!

## DISCLAIMER



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