NABARD

DEAR
ECO WATCH
Issue No. 94/ 06 Mar–12 Mar 2023

Global Economic Outlook

- **Silicon Valley Bank (SVB) crashes**
  The fall of SVB (rated as the 16th largest bank in the US, SVB is a regional bank in the US, headquartered in Santa Clara, California) is a case of asset liability management mismatch concerns which manifested into solvency issues for the bank. Incorporated in 1983, it was among the early banks to set focus on start-ups and venture capitalists.
  From the end of 2019 till March 2022, the bank's deposits tripled to $198 billion; growth outstripped the industry average of 37%. But COVID led to limited opportunities for deployment of funds. Hence, deposits were channelized towards investments for shorter duration (AFS) and longer duration (HTM).
  Due to rise in the cost of deposits of SVB by 1.19%, the bank chose to have a higher portion of HTM vis-à-vis AFS to manage yields. Much of the HTM was deployed into mortgage-backed securities and when interest rates started increasing the yield got affected and the unrealised losses shot to $16 billion by Sept 2022 thus driving the bank into insolvency.

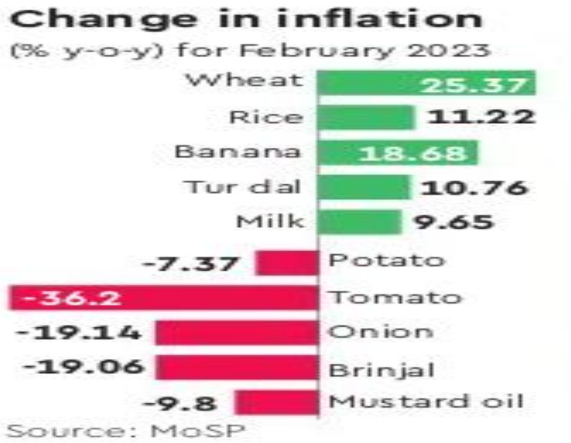
  However, as per analysts SVB crisis unlikely to affect Indian Banks as they have minimal exposure. Moreover it has a very little impact as far as Indian start-ups are concerned.

Domestic Outlook

- **India's retail inflation slows to 6.4%**
  India's retail inflation declined marginally to 6.44% y-o-y in February 2023 as against 6.52% in January 2023 thus remaining above RBI's tolerance band of 2-6% for the second straight month. The high inflation level can be attributed to rising food prices (accounting 40% of CPI). Food inflation stood at 5.95% in February *(Inflation rate for vegetables contracted marginally by 11.6% while that of fuel & light declined to 9.90%).*

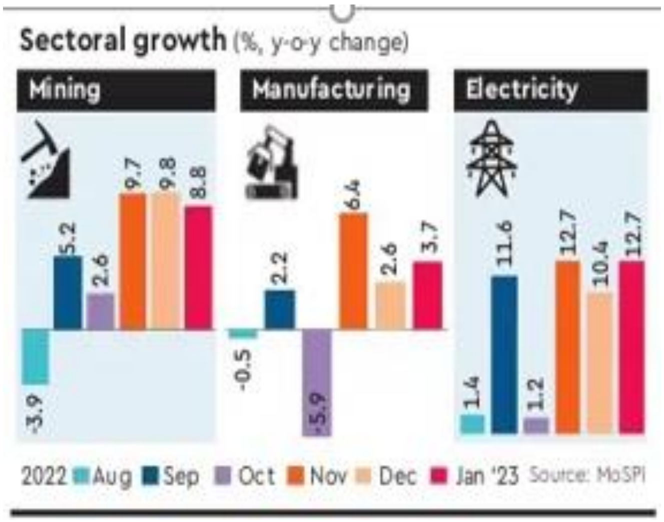
The uncertain nature of Russia-Ukraine war compounded supply-side disruptions thus resulting in higher inflation across the world. Core inflation at 6.1% remains elevated and sticky with relatively high inflation across clothing and footwear, health, household goods/ services thus expecting a 25 bps repo rate hike in April.

Food inflation eases marginally



- **India's WPI inflation eases to 3.85%**
  India's WPI based inflation eased to 3.85% in February from 4.73% in January. The decline is primarily contributed by fall in prices of crude petroleum & natural gas, non-food articles, food products, minerals, computer, electronic and optical products, chemical products, etc. The month-on-month change in WPI index for February saw an increase of 0.20% as against 0.13% in the preceding month.

- **Industrial Growth improves to 5.2%**
  The Index of Industrial Production (IIP) grew by 5.2% in Jan 2023 due to incredible performance by the mining, electricity and capital goods sector. While Jan growth was the 2nd highest since July 2022, analysts anticipate the IIP to reflect the slowing pace of the economy in the coming months.



Source: FE

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DEAR ECO WATCH

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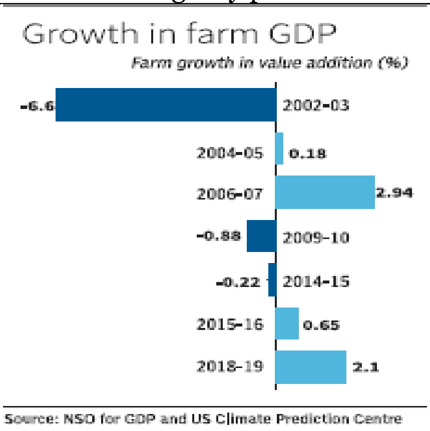
- **Export to cross $750 bn this Fiscal**

  The country's goods and services exports are marching ahead to cross $750 bn in the current FY *(last year's exports reached an all-time high to $676 bn)* as indicated by the Commerce and Industry Minister. India's merchandise exports during April-Jan has increased to $369.25 bn this fiscal *(as against $340.28 bn last year)*. Services exports during the 10-months period are estimated at $272 bn. Addressing tariff and non-tariff barriers, collaboration with trade and technology were recommended by the ministry for global trade.

- **Shadow of El Nino Overgrowth**

  The immediate issue of concern is the prospects of the kharif crop during an El Nino event. This is so because on an average around 60% of the crop is rainfall dependent, and hence any deviation can harm prospects. This tends to be more significant for crops like pulses and oilseeds besides cotton where prices too tend to add to the vulnerability. Rice could still be managed as the northern States of Haryana, Punjab and UP do have access to irrigation which is not the case with other states. The graph below shows how agricultural production (as per GDP data) has moved when there were El Nino, 2015-16 being the larger one.

  The kharif (kharif crop total 50% of agricultural output) season attains more prominence as the timing coincides with the festival season when typically there is higher spending on consumer products. Therefore, close monitoring of El Nino is important and the government should be prepared with a contingency plan.



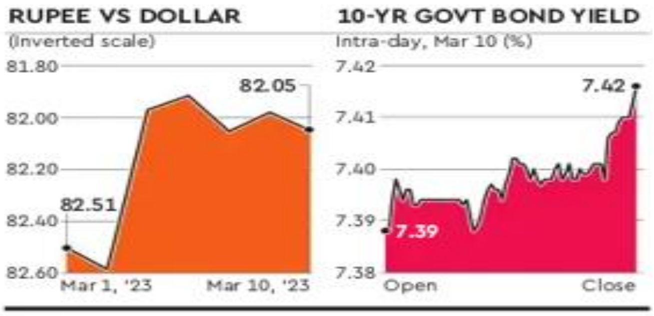
El Nino, a naturally occurring phenomenon characterised by the abnormal warming of sea surface temperature in the central and eastern equatorial Pacific Ocean. On average, it occurs every two to seven years and can last up to 18 months.

Source: Business Line

Today, inflation is a tough nut to crack with core inflation being high. Food inflation has come down due to prices of horticulture products and edible oils easing significantly even while cereals have registered high inflation numbers. This trend can get exacerbated in the event of a subnormal monsoon with pulses and oilseeds crops being affected. Further, concerns on the prospects of the wheat crop remain at this point of time, even though there has been a spell of rain in north India.

Interest Rate Outlook

- Rupee pared its initial gains to settle 17 paise down at 82.23 as against US dollar tracking losses in the domestic equity market and unabated foreign fund outflow. However, till 10 March 2023, Rupee held up well to dollar's rally, almost unchanged week-on-week.



  Fall in crude oil price and a weaker dollar against major currencies restricted the fall of the Indian currency.

- **1-yr, 10-yr yield curve inverts for first time in 8 years**

India's 1-yr Govt debt yield rose higher than that of 10-yr last week following higher than expected cut-offs of RBI's Treasury bill sale *(An inverted yield curve indicates that long term interest rates are less than short term interest rates)*. The Reserve Bank of India sold 364day notes at a 7.48% yield, the highest since October 2018. An inverted curve has proven to be a reliable indicator of recession in the past which may not be the case here but a slowdown in growth is imminent.

Govt bond yields fell on 13 March 2023 tracking a plunge in US yields, as investors scaled back expectations of an aggressive rate hike by the Federal Reserve. The 10-yr benchmark 7.26% 2032 bond yield ended at 7.35% *(lowest since Feb 16)*, after closing at 7.43% on last Friday *(biggest single-session drop since Oct 4)*.

Weekly Benchmark Bond Yield Movement (%)

Date	06-Mar	07-Mar	08-Mar	09-Mar	10-Mar
USA 10 years	3.97	3.97	3.98	3.91	3.68
India 10 years	7.41	7.41	7.45	7.44	7.42
India 5 years	7.38	7.38	7.43	7.41	7.40
India 3 months	6.92	6.92	6.95	6.97	6.90

Source: CMIE, worldgovernmentbonds.com

We expect benchmark 10-Yr bond to trade in the range of 7.35%-7.42% during the week (13 March 2023-17 March 2023).