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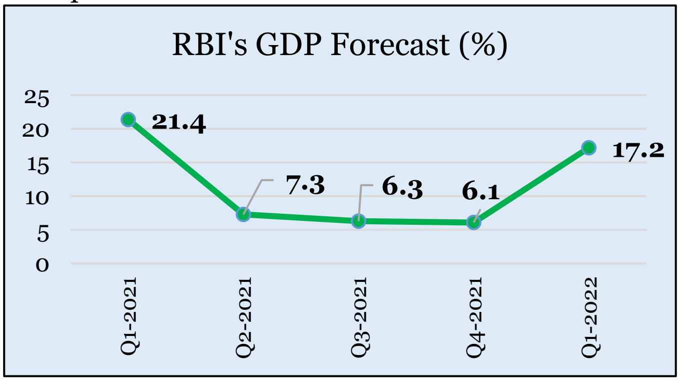
DEAR
ECO WATCH
Issue 11/ 02-08 Aug 2021

Global Economic Outlook

- The findings of the latest World Economic Forum (WEF)/Ipsos market survey of around 22,000 people across 29 countries reveal that an average of three in four adults believe that it will take **at least two more years for their country's economy to recover** from the Covid-19 pandemic.
- As expected, Bank of England decided **not to change Bank's main lending rate** which is at a historic low of 0.1% since March 2020, and voted 7-1 to maintain the quantitative easing program at $ 1.25 trillion.
- The bank also raised its inflation forecasts, and now expects inflation to rise further in the near term, temporarily reaching 4% in Q4-2021 and Q1-2022, 1.5% higher than the projection done in May-21.
- **Oil prices fell** about 1% lower on 6th August 21, posting to their steepest weekly losses in months, after weak economic data from China and United states (the world's top oil consumer), higher crude output from OPEC+ countries. Travel restrictions to curb the spread of the Delta variant of COVID-19 in countries like China, US may further derail the global recovery in energy demand.
- Though **China's factory activity** expanded in July 2021, as pointed out in official manufacturing PMI which stood at 50.4, the pace of growth was lowest since the index slumped to 35.7 in February 2020, as higher raw material costs, equipment maintenance and extreme weather weighed heavily on business activity, adding to concerns about a slowdown in the world's second-biggest economy.
- U.S. **manufacturing activity** also showed signs of **slowing** (July manufacturing PMI registered 59.5 per cent, a decrease of 1.1 percentage points from the June 2021 reading of 60.6 per cent.). The pace of growth slowed for the second straight month as spending rotates back to services (July 2021 service PMI, came at 64.1, a 4.0 percentage point gain over June's 2021 60.1, and growing, at a faster rate, for the 14th consecutive month) from goods and shortages of raw materials persist, according to data from the Institute for Supply Management (ISM).

Domestic Outlook

- The Reserve Bank of India (RBI) **retained its GDP growth forecast** for 2021-22 at 9.5 per cent in its third monetary policy review on 6th August 2021. It expects GDP to grow Y-o-Y by 21.4% in the Q1 of 2021-22, by 7.3% in Q2, by 6.3% in Q3 and by 6.1 % in the last quarter of 2021-22. It has projected the GDP growth for the first quarter of 2022-23 at 17.2%.
- The RBI expects agricultural production and rural demand to remain resilient this year, but urban demand to revive with a lag when pace of vaccination accelerates and the release of pent-up demand acquires a durable character.



- While Economist and Nobel laureate Shri Abhijit Banerjee is of the view that a third Covid-19 wave might adversely impact India's GDP growth, pulling it down to 7% in 2021-22.
- He further stated that the Centre should be more into free-spending policies like economies of Europe and the United States rather than being more concerned about balancing fiscal deficit and the budget.
- The Reserve Bank of India **(RBI) revised** its retail price (CPI) **inflation projection** for 2021-22 upwards to 5.7 per cent from 5.1 per cent earlier.
- It expects inflation of 5.9 per cent in the September 2021 quarter and further down to 5.3 per cent in the December 2021 quarter, before surging again to 5.8 per cent in the final quarter of 2021-22
- The central government expects the **total debt as percentage of GDP to increase** to 61.7 per cent (provisional) in 2021-22 from 60.5 per cent (provisional) in the previous fiscal. Further the Minister of State for Finance commented that government's amendment of the FRBM Act will target a path of fiscal consolidation aimed towards reaching a level of fiscal deficit below 4.5 per cent of GDP by 2025-26.
- The gross GST revenue collected in the month of **July 2021 is ₹ 1,16,393 crore, 33% higher** than the GST revenues in the same month last year. During the month, revenues from import of goods was 36% higher and the revenues from domestic transaction are 32% higher than the revenues from these sources during the same month last year.
- IHS Markit India **Manufacturing (PMI) rose to 55.3** in July 2021, recovering from the 11-month low of 48.1 in June 2021. The Index reported an all-round improvement in July 2021, with output, new orders, exports, quantity of purchases and input stocks all returning to the expansionary territory.

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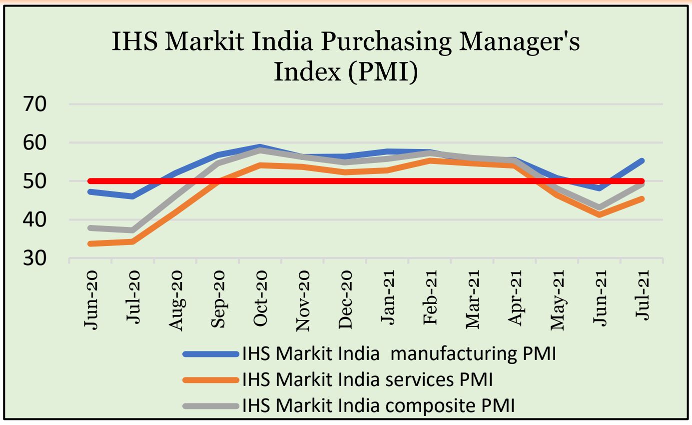

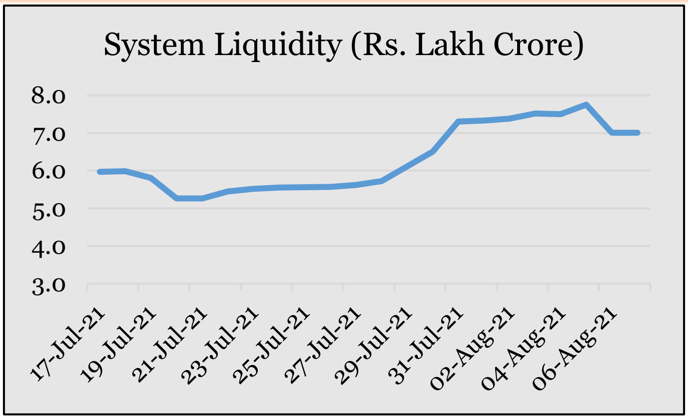

Source: CMIE

Interest Rate Outlook

- The week started with US benchmark 10-year yield falling and touching to 1.15% on 2nd August 2021, after data showed the U.S. manufacturing sector expanded at a slower pace in July 2021 than in the previous month.
- On 6th August 2021 yield on the benchmark 10-year bond added 8 basis points, rising to 1.305% after labour department's highly anticipated jobs report (Bureau of Labour Statistics reported that economy added 943,000 nonfarm payrolls and the unemployment rate dropped to 5.4%) came out better than expected.
- For the first half of the week the new benchmark 6.10%- 2031 bond ended almost flat due to lack of fresh triggers as traders were waiting for the guidance of the RBI in the monetary policy which was scheduled to be released on 6th August 2021.
- On 5th August 2021, the yield marginally rose on supply concerns, but any further rise was capped due to easing oil prices and fall of US treasury yields.
- The Reserve Bank of India (RBI), in its **third Monetary Policy** statement for 2021-22 announced to keep the policy **repo rate** under the liquidity adjustment facility (LAF) **unchanged at 4.0** per cent, to keep the **reverse repo rate unchanged** at **3.35 per cent**. Consequently, the bank rate and the marginal standing facility (MSF) rate, both remain unchanged at 4.25 per cent.
- The Monetary Policy Committee (MPC) decided to continue with its 'accommodative' policy stance as long as necessary to revive and sustain growth on a durable basis and continue to mitigate the impact of Covid-19 on the economy, while ensuring that inflation remains within the medium-term target for consumer price index (CPI) inflation of 4 per cent with a band of +/- 2 per cent.
- To absorb surplus liquidity (Rs.7 lakh crore), RBI plans to conduct Variable Rate Reverse Repo (VRRR) auction worth Rs 4 lakh crore by September end. Expert's hint that this may be a start of reversal of easy monetary policy.
- RBI increased its CPI forecast by 60 basis points more than the experts' expectation of 40 basis points.
- The benchmark yield rose three basis points to close at 6.237% on 6th August, mainly because of announcement of (VRRR) auction and 60 basis point increase in CPI inflation projection.
- In the weekly bond auction held on 6th August, RBI sold bonds worth Rs 3,750 cr and Rs 11,250 cr through sale of 4.26%-2023 and 6.76% 2061 bonds respectively. On both the bonds RBI accepted green shoe option (selling excess than the notified amount). However, 10-year benchmark bond bids were rejected by the central bank as investors were looking for better yields and total amount of Rs 14000 cr was accepted by primary dealers.
- The Reserve Bank of India (RBI) has announced third and fourth tranche of **G-sec Acquisition Programme** (G-SAP 2.0) i.e., open market purchase of government securities worth Rs.25,000 crore each, to be conducted on 12th and 26th August 2021. These open market operations are intended to anchor the yields on few papers and to keep all segments of the yield curve liquid.
- Inclusion of 5 year bechmark bond in the GSAP third tranche to be conducted on 12th August will provide cushion to this bond

Weekly Benchmark Bond Yield Movement (%)					
Date →	**02/8**	**03/8**	**04/8**	**05/8**	**06/8**
India 10 year	6.20	6.20	6.20	6.21	6.23
India 5 year	5.72	5.73	5.71	5.72	5.78
USA 10 year	1.179	1.17	1.18	1.23	1.305

- Bond yield for government benchmark 10 year is expected to remain in range of 6.20-6.30. This is mainly on account of higher CPI forecast and announcement of VRRR. It will also weigh on release of CPI inflation data this week.