panorama

October 2023

Key Insights:

Net Financial Savings of households dip on increase in financial liabilities

- Deposits continue to account for an outsize 37% share in financial assets, followed by 22% share of provident and pension funds, and 18% share of life insurance funds. MF, shares & debentures account for only 7%
- Housing, business, and agri account for two-thirds of incremental HH credit, one-third is consumption oriented
- Share of deposits in financial savings may remain high in the near term on attractive term deposit rates
- Quality of HH credit off-take has improved in Q1FY24 with decline in consumption-oriented credit

Expect RBI to intervene in both FX and G-sec market to maintain macro-stability

- Following the initial boost from index inclusion, debt flows are expected to be subdued due to the decreasing interest rate differential between India and developed markets
- RBI to intervene in the foreign exchange markets to prevent INR volatility
- RBI to carry out OMO sales to absorb the surplus banking system liquidity

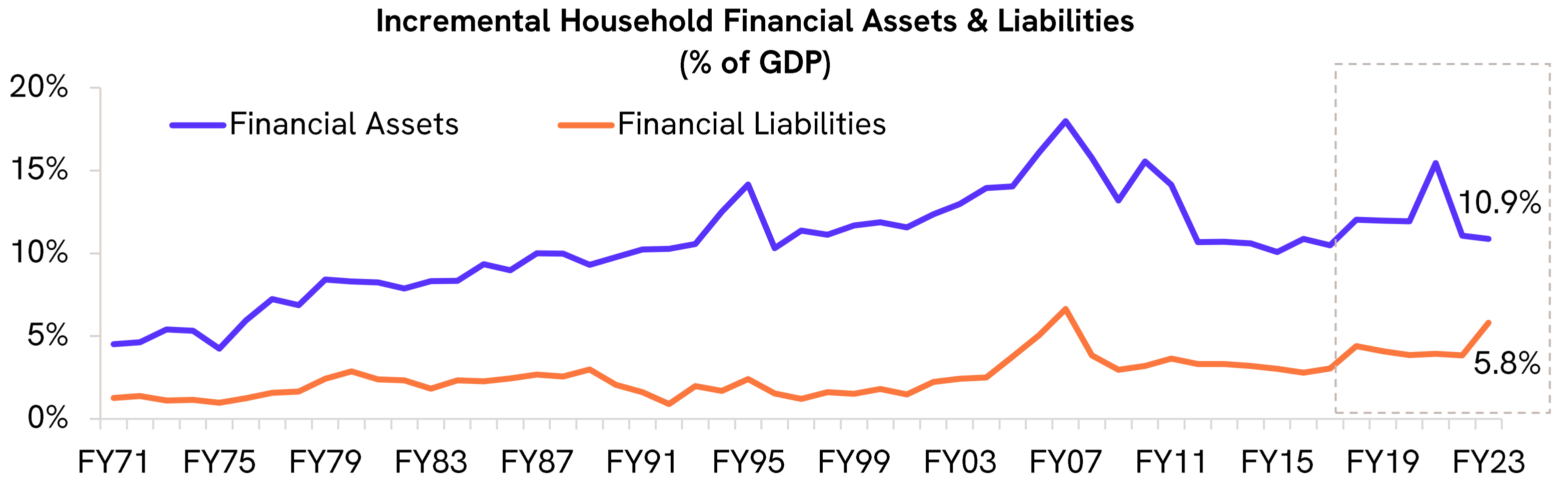
Crude oil to remain range-bound as tight supplies intersect with proactive central banks

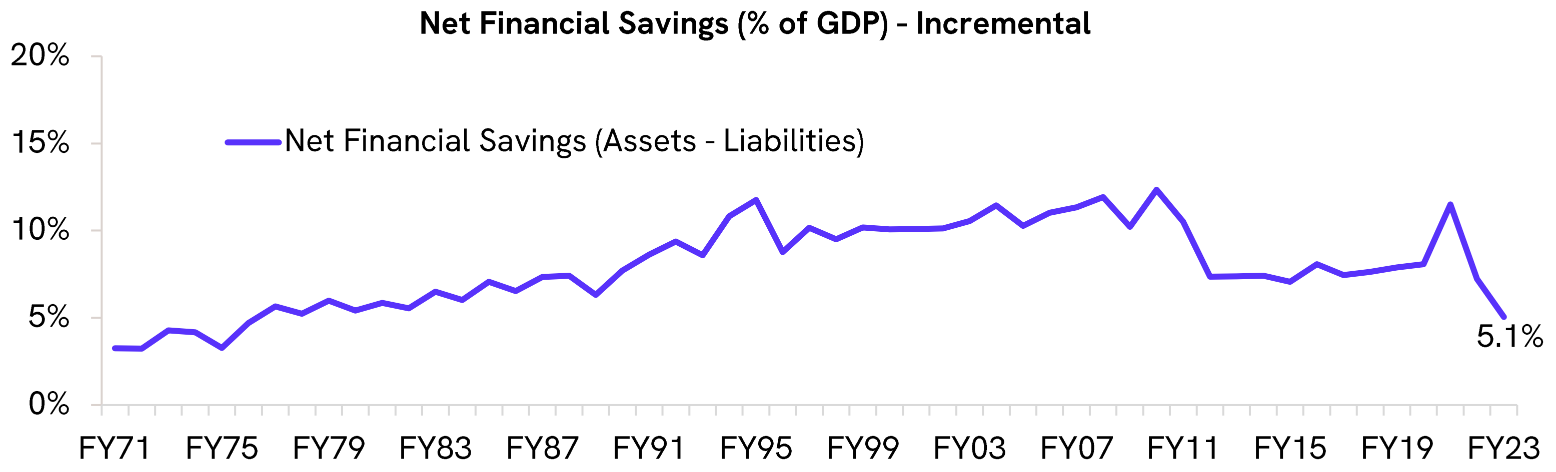
- Crude prices rose due to OPEC+ supply reductions and voluntary cuts by Saudi Arabia and Russia
- Rising oil prices could un-anchor inflation expectations, compelling central banks to act
- Oil Marketing Companies' marketing margins have declined on rise in crude prices
- Strong growth in government receipts opens the possibility of reduction in excise duty on fuel

Household Financial Savings

Net financial savings of households dip on increase in liabilities

The rise in household financial liabilities, totaling 5.8% of GDP, is the second highest since the 1970s





Source: RBI, MOSPI, 360 ONE Asset Research

Incremental household (HH) financial assets in FY23 are only marginally lower at 10.9% of GDP compared to 11.1% in FY22

Overall, HH financial assets remain consistent with the levels observed over the past decade

Incremental financial liabilities (% of GDP), however, are at their highest since FY07 and the second highest since the 1970s

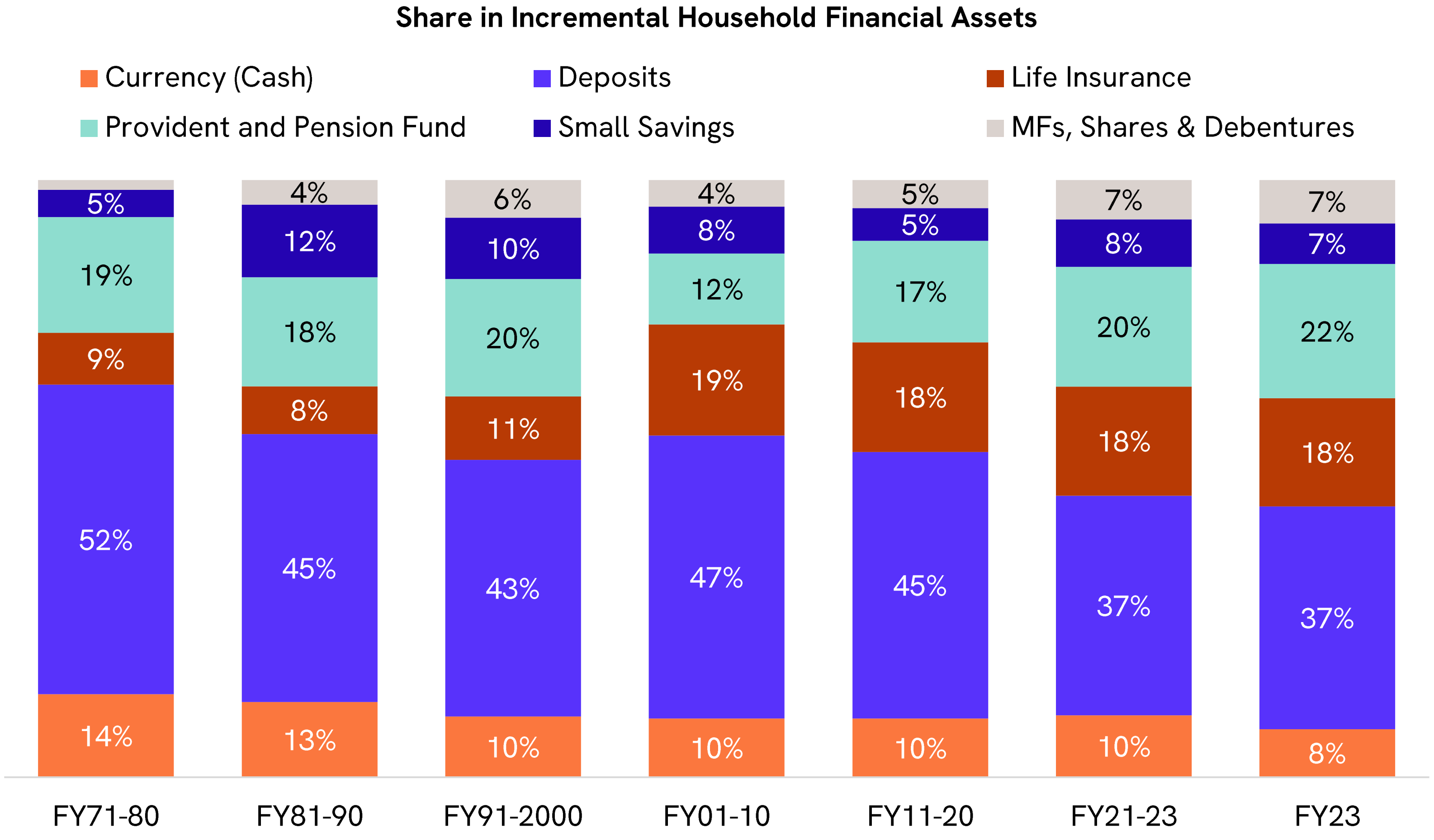
Net financial savings of households is the difference between gross financial assets and financial liabilities

The net financial savings of households as a percentage of GDP, standing at 5.1%, are the lowest observed since 1976

As shown in the above chart, the fall in net financial savings is driven by the rise in HH financial liabilities

Deposits continue to account for an outsize share in financial assets

Share of Life Insurance Funds has doubled from 9% in the 1970s to 18% in the current decade



Deposits account for a 37% share of incremental households (HH) financial assets in FY23, while Provident and Pension Funds account for the second-highest share at 22%

The share of Life Insurance Funds has doubled from 9% in the 1970s to 18% in FY23

The share of MFs, Shares & Debentures remains muted at 7%, although it has increased from almost negligible levels in the 1970s

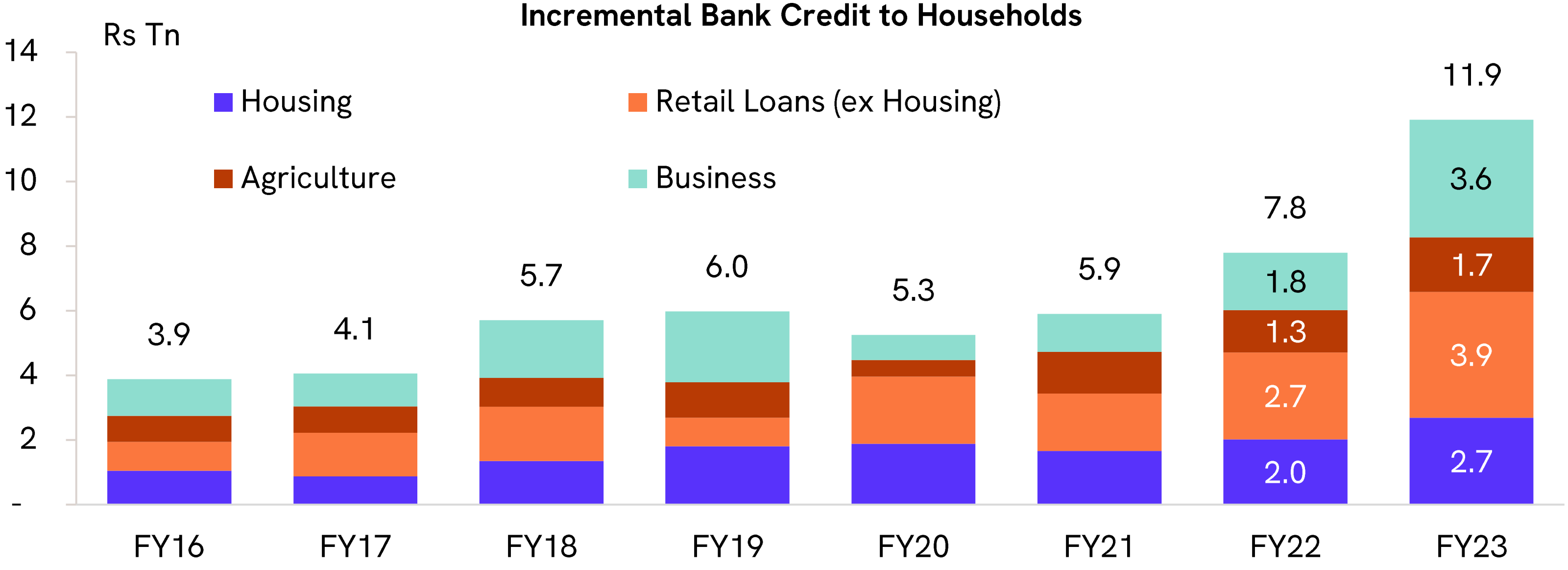
Currency's (cash) share in assets has decreased from 14% in the 1970s to 8% in FY23

Small Savings' share stands at approximately 7% in FY23

Source: RBI, MOSPI, 360 ONE Asset Research

Housing, business, and agriculture account for two-thirds of HH credit

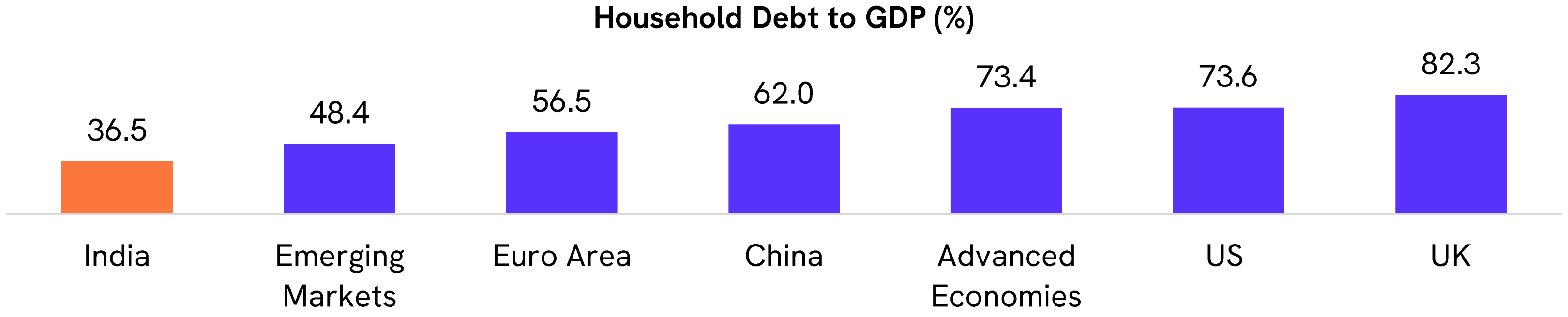
Only one-third of incremental household credit in FY23 was consumption-oriented and may require monitoring



Housing credit accounts for approximately a quarter of total household credit uptake, contributing to physical savings

Business credit accounts for roughly one-third of the share, primarily directed toward productive business investments

Retail loans, excluding housing, which account for 33% of the total incremental credit, have seen a substantial increase and are predominantly geared towards consumption



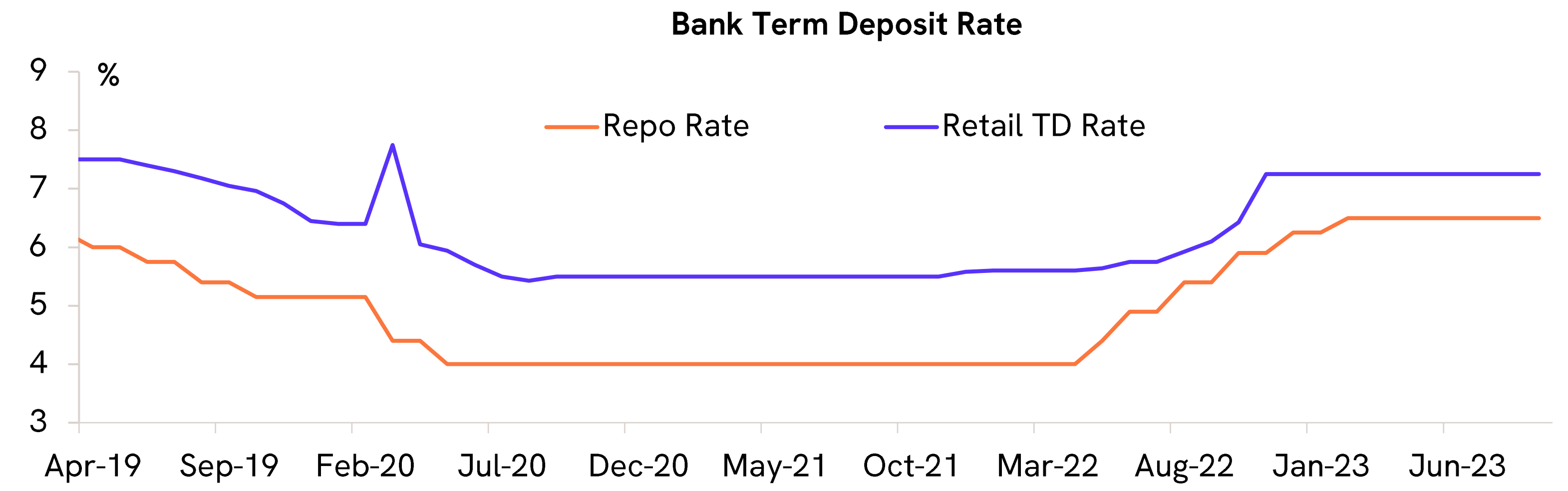
India's HH debt remains manageable and does not pose any systemic risks. However, non-mortgage retail loans may warrant monitoring for signs of potential stress, as highlighted by the RBI during the October 2023 policy meeting

Source: RBI, BIS, 360 ONE Asset Research

Note: Household Debt to GDP (%) as on March 2023

Deposits' share may stay high in HH savings due to attractive rates

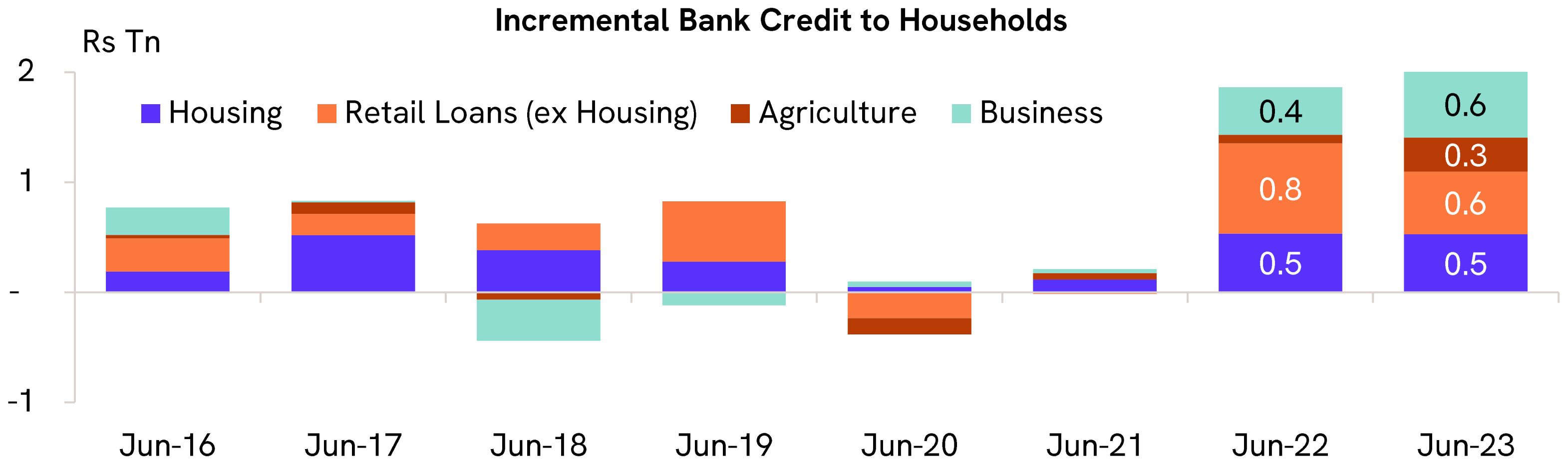
In Q1FY24, HH's non-mortgage retail credit off-take is relatively subdued, while business credit is more robust



Banks are competing for deposits as credit growth outpaces deposit growth

Rates offered on term deposits (TD) are the highest in the last four years. Hence, the share of deposits in HH savings may remain high in the near term

Withdrawal of Rs 2000 denomination notes to also shift savings from currency to deposits



There has been a decrease in non-mortgage retail credit off-take in Q1FY24 in comparison to same quarter last year

Business and agricultural credit off-take have seen an increase, while housing credit has remained at approximately the same levels as last year

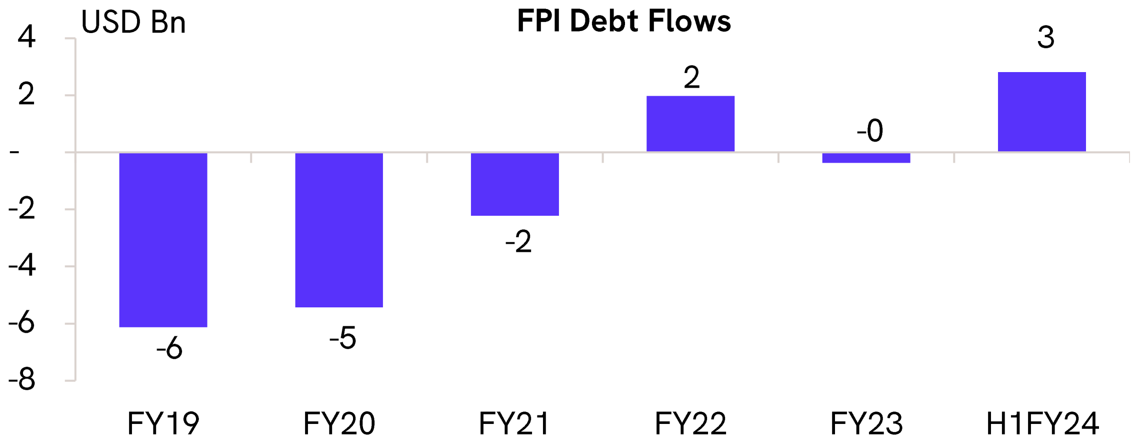
Thus, the quality of household credit demand (consumption vs investment oriented) has improved in Q1FY24

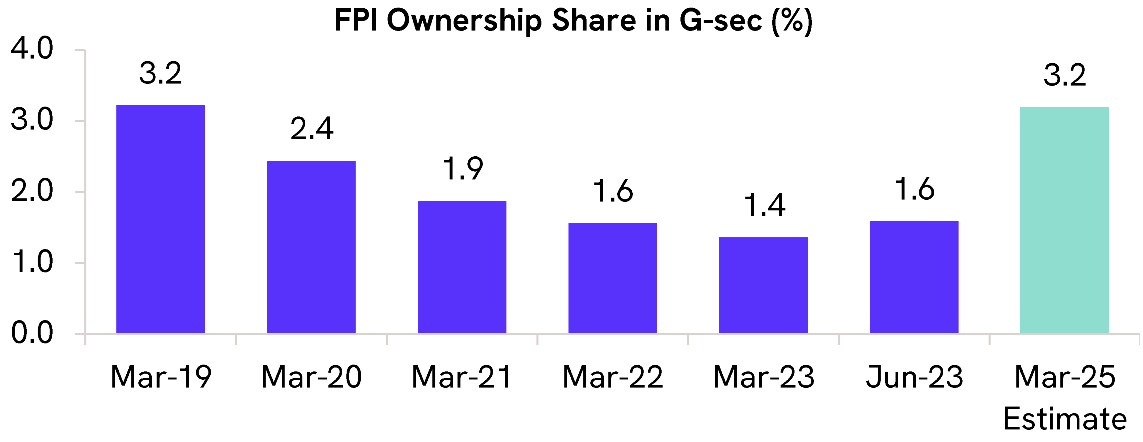
Source: RBI, 360 ONE Asset Research

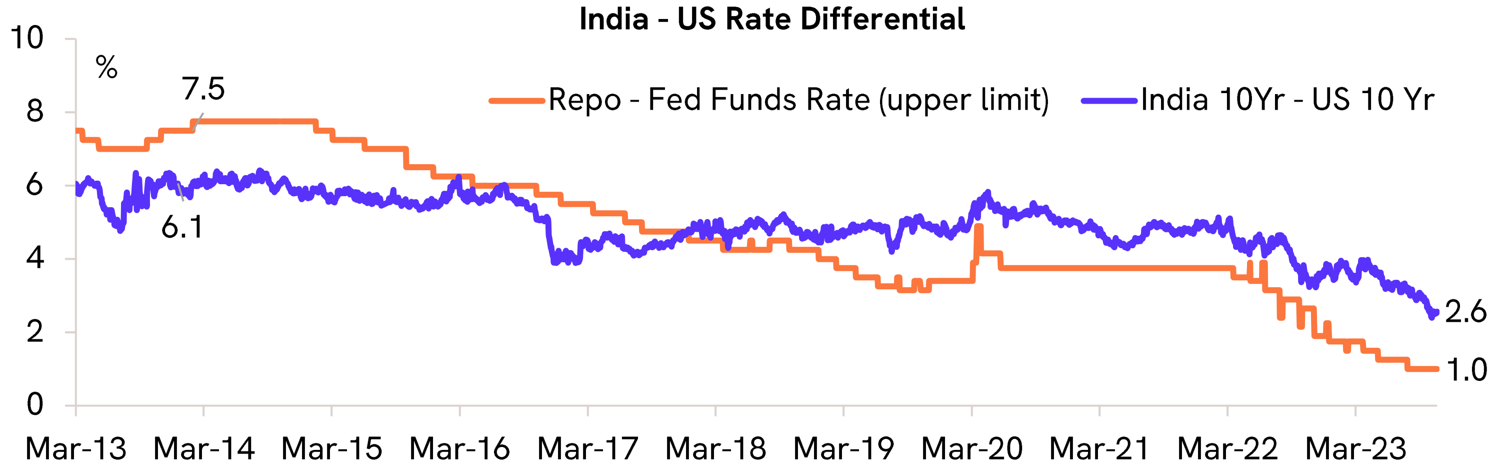
Rates & Flows

FPI debt flows in India have been muted over the past 5 years

Lower interest rate differential b/w India and developed markets could limit flows after the initial boost from index inclusion







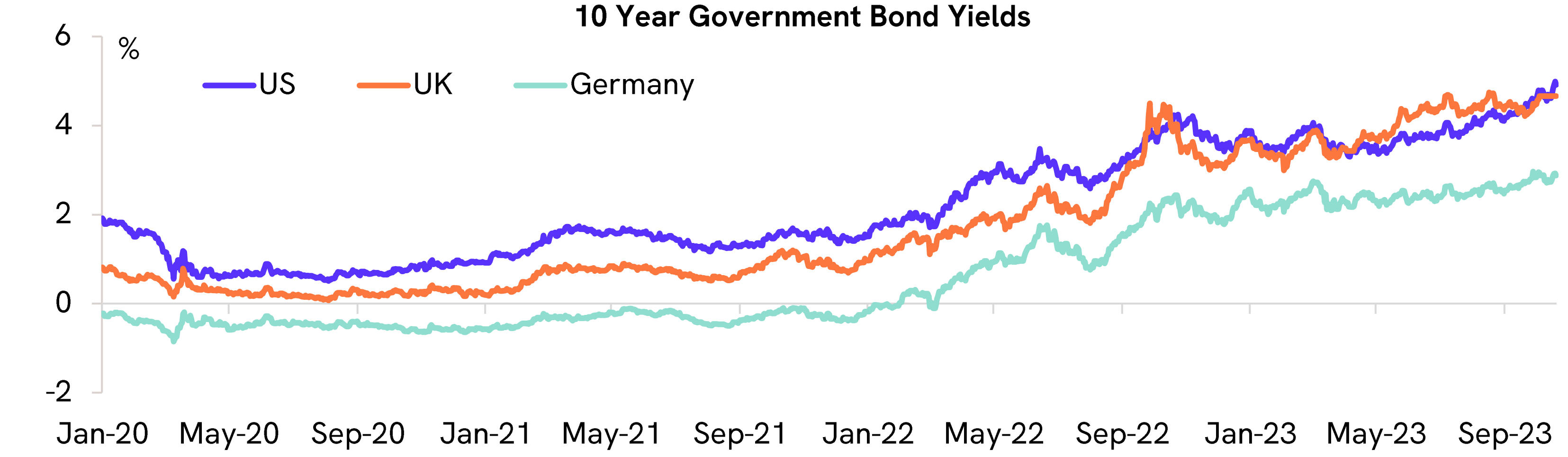
The market consensus expects a significant $30 billion in debt inflows by March 2025 due to index inclusion. In comparison, there have been total outflows of $20 billion over the last 5 years

Debt flows post the full index inclusion are expected to be subdued because of the decreasing interest rate differential between India and developed markets

Source: CMIE, FRED, 360 ONE Asset Research

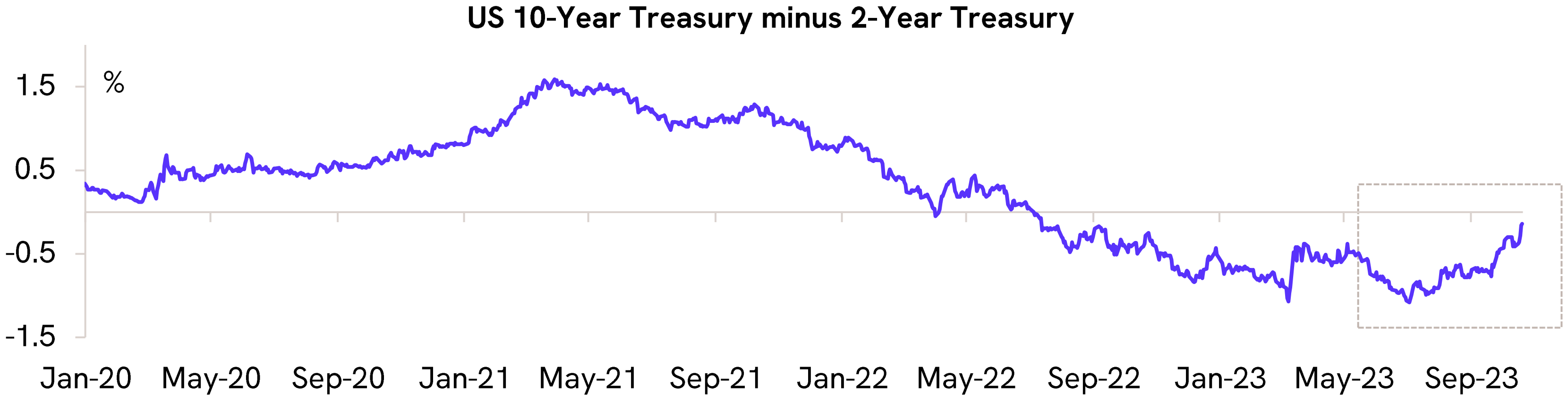
Long-end yields rise globally on expectations of higher rates for longer

Decent US economic data and high volume of bond issuances also contribute to the steepening of the US yield curve



Ten-year yields have risen across developed markets as the Fed continues to signal that rates are likely to stay elevated for an extended period

The ECB has also indicated that maintaining key interest rates for a prolonged duration will significantly contribute to achieving the target inflation rate



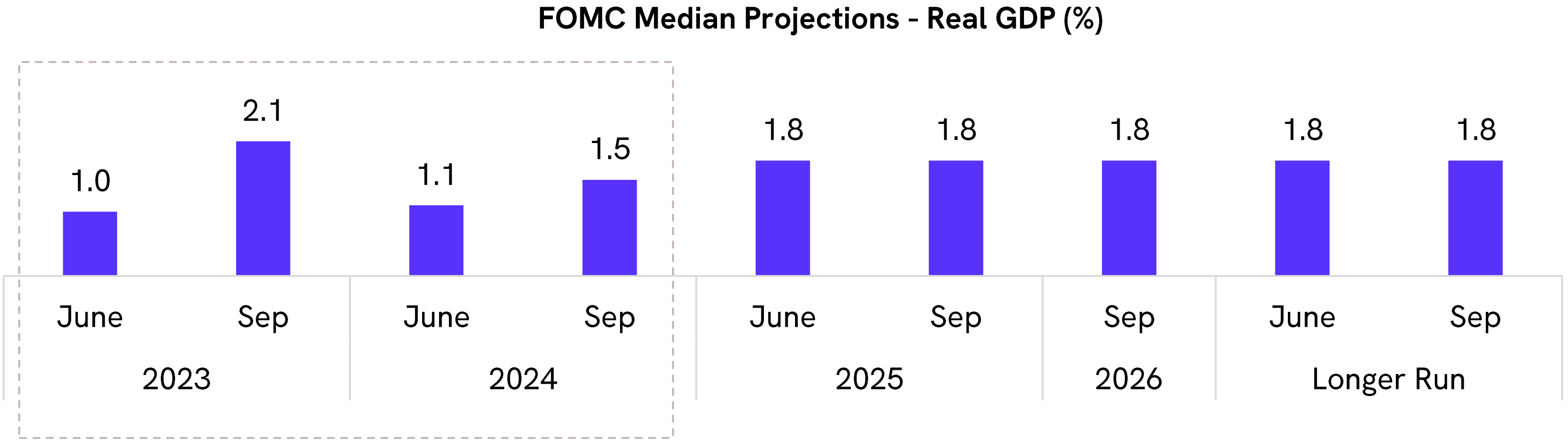
The US yield curve is experiencing 'bear steepening,' which means that the yields of longer-dated bonds are rising more rapidly than those of short-dated sovereign debt

Decent US economic data and high volume of bond issuances contribute to the steepening of the yield curve

Source: Bloomberg, FRED, 360 ONE Asset Research

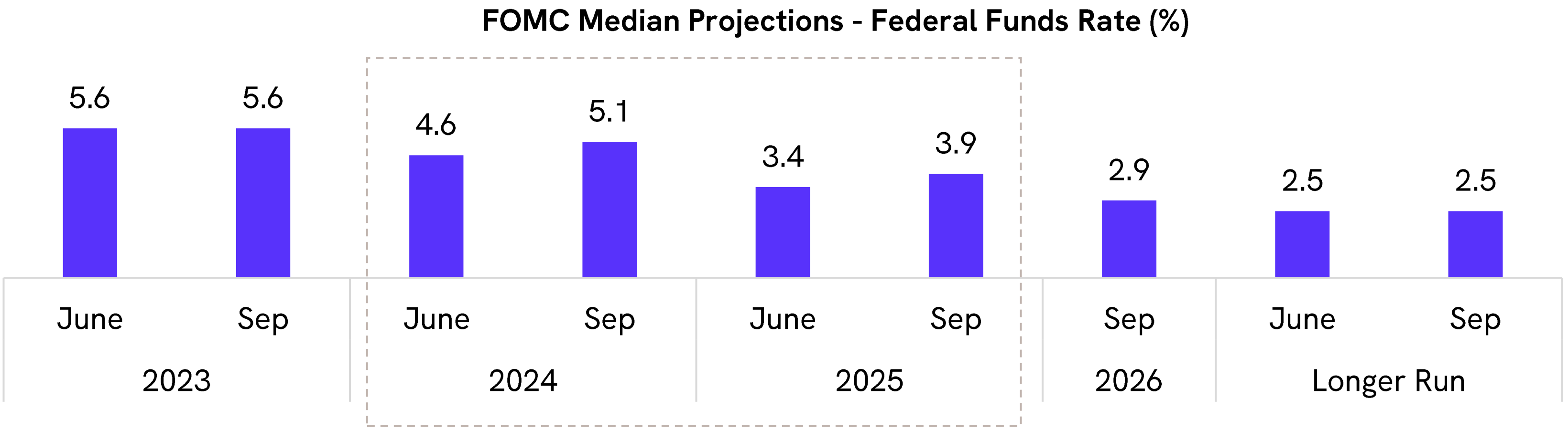
FOMC GDP projections revised significantly upwards for 2023 and 2024

Federal Funds Rate expectations revised upward by 50 bps for both 2024 and 2025 in the September FOMC



FOMC's median Real GDP forecasts for 2023 were significantly revised upwards to 2.1% YoY in September 2023, up from 1% in the June projections. The projection for 2024 was also revised higher by 40 bps

The revisions indicate that US economic growth continues to outperform expectations



Federal Fund Rate (FFR) projections indicate another rate hike in 2023

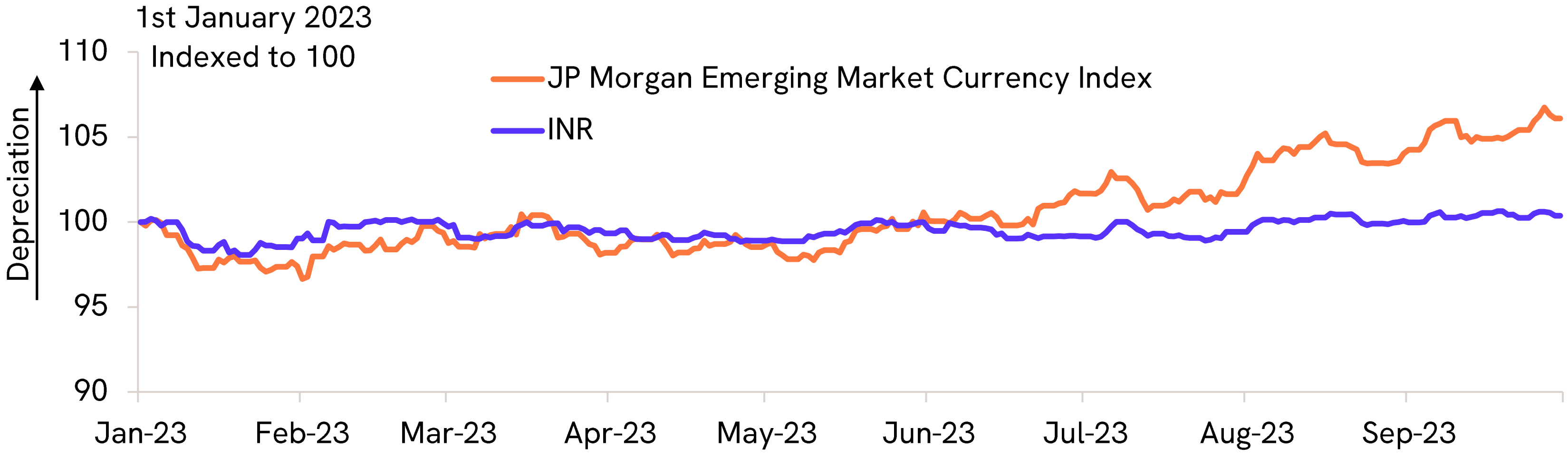
The Fed's dot plot suggests 50 basis points of rate cuts in 2024, a reduction from the 100 basis points of cuts anticipated in the June policy

FFR projections for 2025 were also adjusted upwards by 50 basis points in the September FOMC meeting

Source: FED, 360 ONE Asset Research

Anticipate RBI intervention to stabilize INR and curb excessive volatility

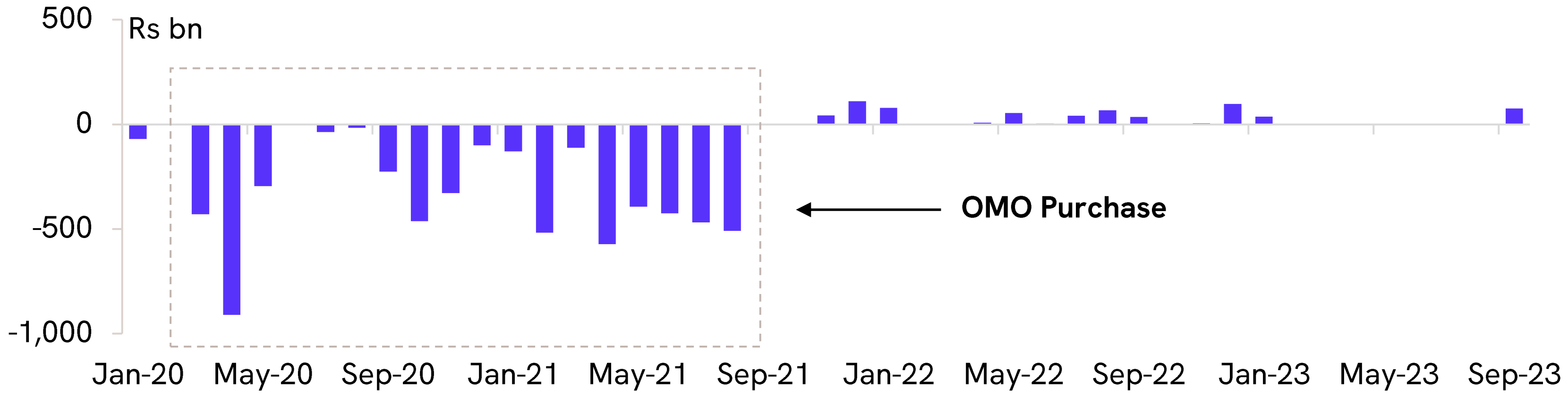
RBI expected to carry out OMO sales to absorb the surplus banking system liquidity in the system



The RBI has repeatedly intervened in the FX market to control INR volatility, resulting in the INR being much more stable when compared to a basket of emerging market currencies

RBI is anticipated to intervene in the foreign exchange markets (by purchasing dollars in spot along with carrying out FX swaps) to prevent INR volatility during the index inclusion-related debt flows

Net Open Market Operation (OMO) Sales by RBI



RBI's foreign exchange spot buy intervention will bolster banking system liquidity

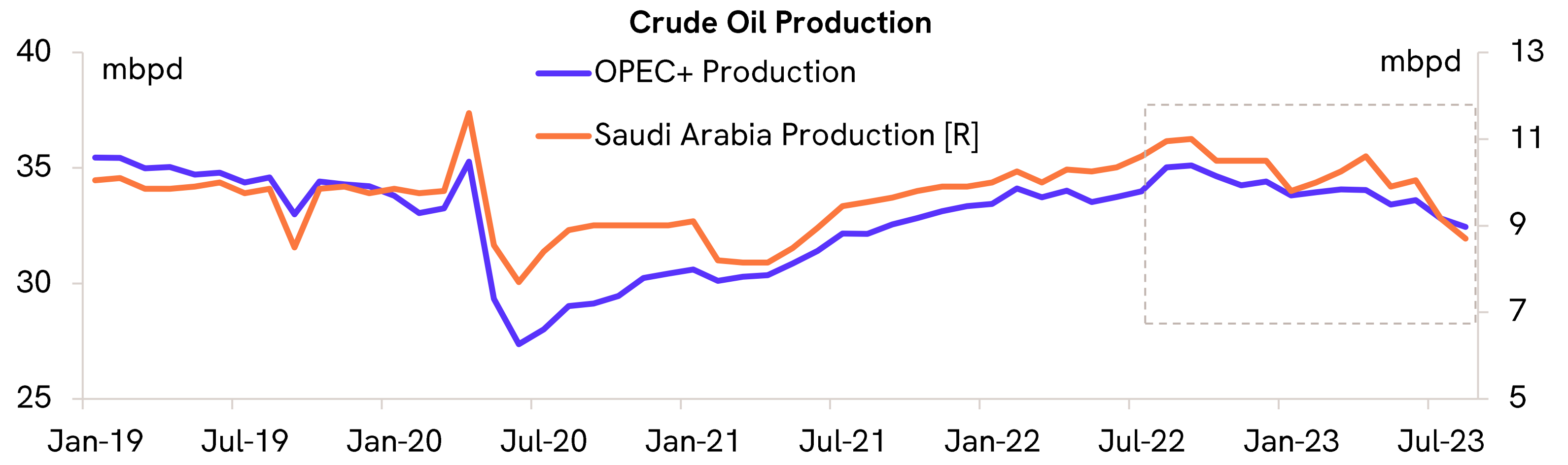
However, given the concerns around inflation and financial stability risks stemming from excessive system liquidity, the RBI is likely to carry out OMO sales to absorb the surplus liquidity

Source: Bloomberg, CMIE, 360 ONE Asset Research

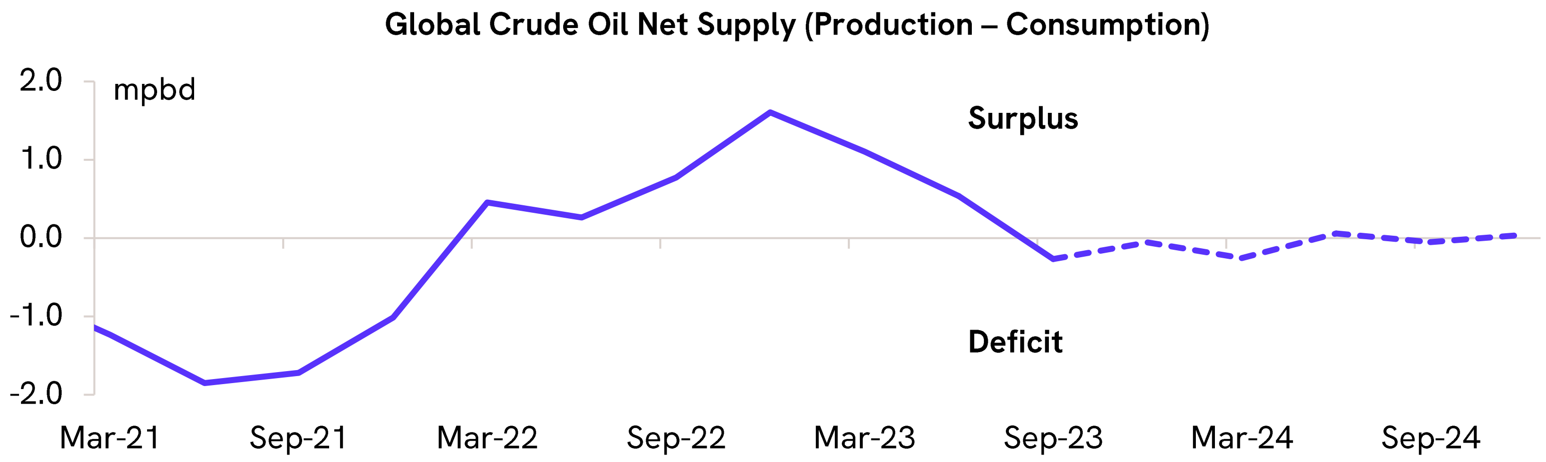
Oil Outlook

Crude oil prices spike due to OPEC+ supply reductions

Crude oil prices expected to remain range-bound as tight supplies intersect with proactive central banks



Saudi Arabia announced extension of production cuts of 1 mpbd until the end of 2023. Russia also announced that it would continue current export cuts of 300 thousand bpd for the rest of the year



Crude oil market expected to remain tight till Mar-24 and broadly balanced from June-24 onwards

The expected increase in supply from non-OPEC producers by 2024 is barely enough to cover the increase in demand

Crude oil prices are expected to remain rangebound (85-95 $/Bbl), with geopolitical conflicts posing a risk to the outlook

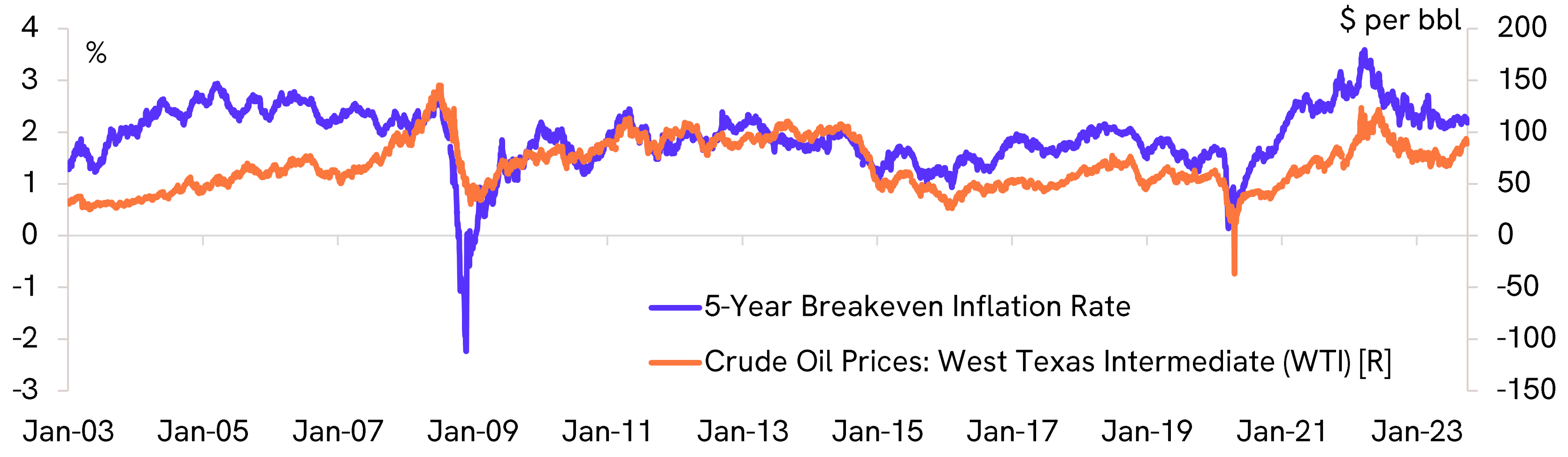
Central banks could consider resuming rate hikes if high prices begin to exert upward pressure on inflation

Source: EIA- STEO, 360 ONE Asset Research

Note: mpbd - million barrels per day

Rising oil prices could un-anchor inflation expectations

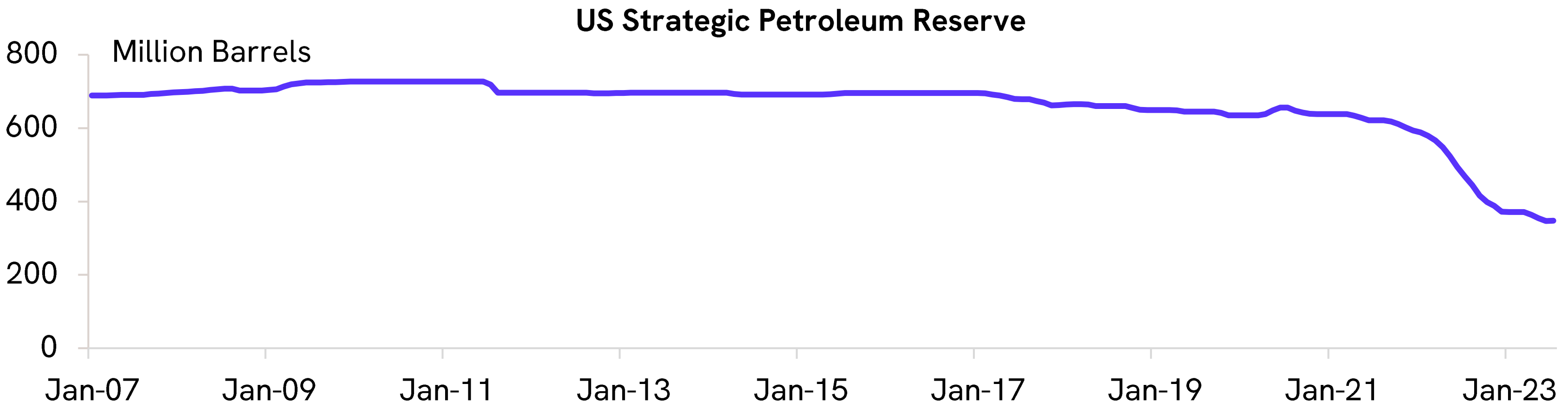
US Strategic Petroleum Reserve drained by ~44% over the last 2 years, limiting scope for further intervention



5-Year Breakeven Inflation rate implies what market participants expect inflation to be in the next 5 years, on average

There is a strong correlation between inflation expectations and crude oil prices in the US. Therefore, an increase in crude oil prices could drive expectations higher

A rise in inflation expectations would, in turn, compel the FOMC to take action to prevent these expectations from feeding into headline inflation

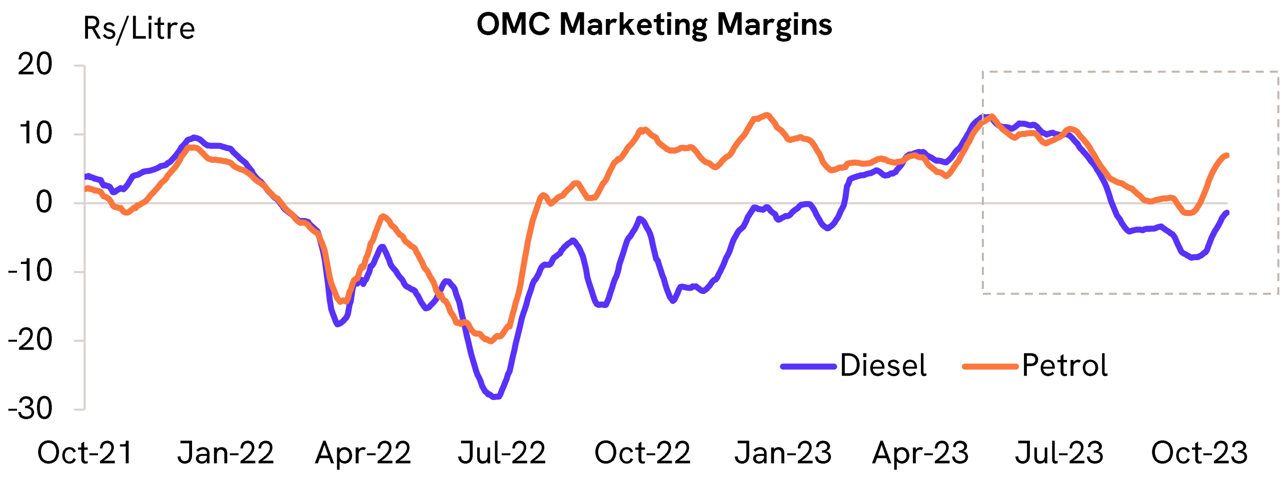


The US Strategic Petroleum Reserve (SPR) has already been significantly depleted, reducing the potential for additional interventions to control fuel price increases. The SPR is now 44% lower in July 2023 compared to July 2021 levels

Source: FRED, EIA, 360 ONE Asset Research

OMC's marketing margins decline on rise in crude prices

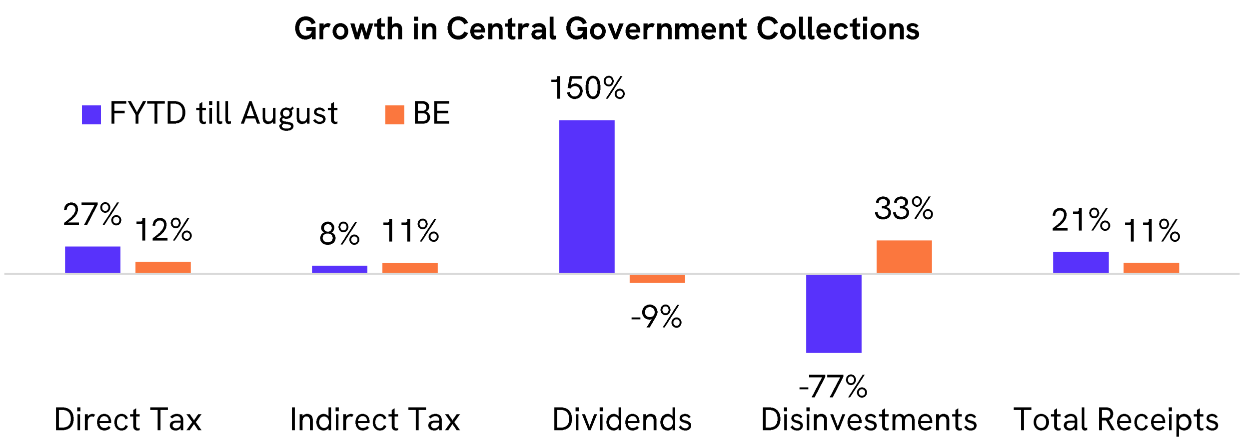
Strong growth in government receipts opens the possibility of reduction in excise duty on fuel

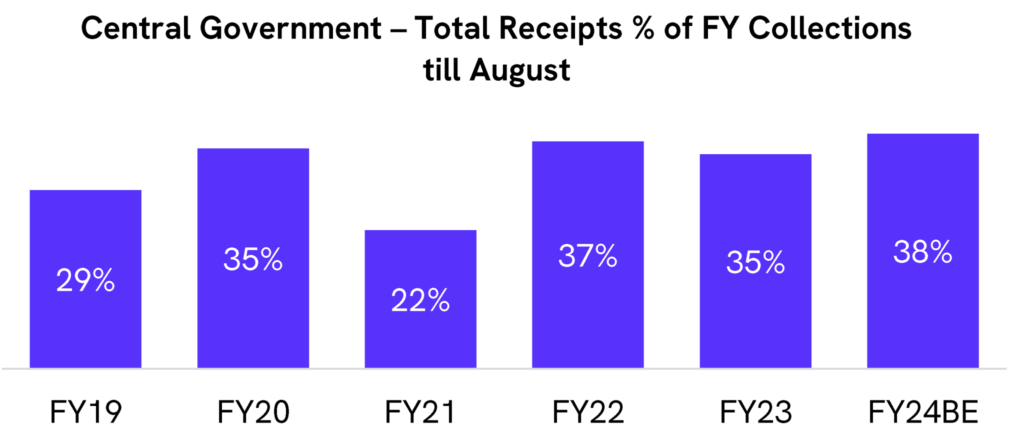


Marketing margins for Oil Marketing Companies (OMCs) have decreased due to the surge in oil prices. This reduction has restricted the potential for lowering pump prices

However, there is a possibility of a reduction in pump prices if the government opts to reduce excise duties on petrol and diesel. Government tax collections have exhibited strong performance, exceeding the budgeted growth through August

However, sticking to the fiscal deficit target of 5.9% should be the top priority





Source: Kotak Institutional Equities, CGA, Budget Documents, 360 ONE Asset Research

Note: BE – Budget Estimates

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