BANKING MONTHLY

SEPTEMBER 2022

PROGRESSIVE®
Your Progress Our Priority...

Prevailing Rates

I. Policy Rates

Repo Rate	5.90%
Reverse Repo Rate	3.35%
Standing Deposit Facility Rate	5.65%
Marginal Standing Facility Rate	6.15%
Bank Rate	6.15%

II. Lending/Deposit Rates

Base Rate	7.75% -8.80%
MCLR Rate (Overnight)	6.85% -7.75%
Savings Deposit Rate	2.70% -3.00%
Term Deposit Rate > 1 Year	5.30% -6.10%

III. Reserve Ratio

CRR	4.50%
SLR	18.00%

Global Banking:

Economic growth could grind to a halt and spark global recession next year, OECD says

Several of the world's largest economies face heightened recession risks as the pandemic's aftershocks and the Ukraine War slow growth worldwide. During the first half of 2022, inflation in many countries skyrocketed to levels unseen since the 1980s, the Organization for Economic Co-operation and Development (OECD) said in its latest economic outlook report. Fixing the problem might require engineering a dramatic economic slowdown in many countries. The two drivers behind the expected slowdown are the costs associated with the Ukraine War which the OECD said will lead to USD2.8tn drop in global GDP next year and central banks worldwide tightening their monetary policies in an effort to reduce inflation, measures that could tip several major economies into prolonged recession.

Our Comments:

Global economic activity will remain subdued for the rest of the year before declining in 2023, according to the OECD. As a result, the organization downgraded its global economic growth forecast for next year to 2.2% from the 2.8% it had predicted in its previous forecast in June.

China growth to fall behind rest of Asia for first time since 1990

China's economic output will lag behind the rest of Asia for the first time since 1990, according to new World Bank forecasts that highlight the damage wrought by President Xi Jinping's zero-Covid policies and the meltdown of the world's biggest property market. The World Bank has revised down its forecast for gross domestic product growth in the world's second-largest economy to 2.8%, compared with 8.1% last year, and from its prediction in April of between 4 and 5% for this year. China had set a GDP target of about 5.5% this year, which would have been a three-decade low. But the outlook has deteriorated markedly over the past six months.

Our Comments:

China, which was leading the recovery from the pandemic, and largely shrugged off the Delta (Covid variant) difficulties, is now paying the economic cost of containing the disease in its most infectious manifestation.

US' reckless rate hikes causing world economic earthquake

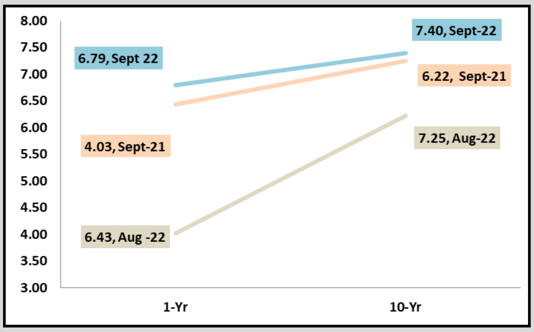
As predicted, the US Federal Reserve made another large interest rate hike adding further pressure to global equities markets. To make things worse, the US central bank remains stubbornly aggressive and hawkish, indicating more rate hikes are likely before the end of this year. The Fed is now raising rates at one of the fastest paces in its modern history. The 75bps rate hike, the fifth in a row lifts the rate the Fed charges banks to borrow from near zero at the beginning of 2022 to a current minimum of 3%.

Our Comments:

By 2023, the Fed could raise rates to as high as 4.5%, according to the US central bank's announced plan, which will undoubtedly take the wind of the sails of the world's largest economy, if not sending it into negative growth. The Fed predicts the US economy will crawl along at 0.2% this year. And in 2023 it seems that the US economy can hardly escape recession. The Fed is determined to quash elevated inflation that is seeping through the country's economy. As a matter of fact, the Federal Reserve's commitment to tamp down inflation to reach the bank's stated 2% target through drastically raising interest rates in a short span of 12 months is too radical, if not unrealistic.

Please Turn Over

Exhibit 1: 1 Year Yield v/s 10 Year Yield



Source: Investing.com, Progressive Research

Indian Banking:

India's retail inflation quickens to 7% in August; IIP growth eases to 2.4%

India's retail inflation as measured by the consumer price index (CPI) surged to 7% in August due to higher food prices, compared to 6.71% in July. The number has remained above the Reserve Bank of India's comfort zone of 2-6% for the eighth consecutive month. Meanwhile, industrial growth, as measured by the Index of Industrial Production (IIP), tumbled to 2.4% in July as compared to 12.3% in June.

Our Comments:

Analysts had predicted annual inflation of 6.9% in August, compared with 6.71% the previous month. The IIP growth plunged to a four month low of 2.4% in July 2022, trailing our expectation of 4%, unfortunate but expected fallout of the base normalisation, heavy rainfall in some areas, and the shift in discretionary consumption to contact-intensive services.

India’s bad bank aims to purchase 18 distressed accounts by the end of October

National Asset Reconstruction Company of India Ltd, the bad bank promoted by the Government, is preparing to acquire 18 distressed accounts totaling Rs39,921cr by October 31. This follows directions from Finance Ministry officials to government-owned banks. The government-owned firm has informed lenders that it has drawn up two lists. Phase one will consist of with eight accounts with Rs16,744cr debt and phase two will comprise 10 accounts with Rs18,177cr debt.

Our Comments:

The bad bank has failed to buy a single package of bad loans in a year of operation. The regulator’s rules stipulate that an asset reconstruction company must close at least one deal within a year of starting if it wants to retain its license. The haste is thereby justified.

Liquidity in India's banking system likely to remain in deficit in 2HFY23

The country's banking liquidity slipped into deficit for the first time in nearly 40 months: as per the central bank. The onset of the festive season and expectation of sequential improvement in economic growth would increase transactional demand for cash. Meanwhile, government spending, which boosts liquidity in the market, has been slower than expected despite robust tax collections. This combination of slow pick-up in government expenditure and buoyant tax collection is reflected in government cash balance.

Our Comments:

India's banking system liquidity is expected to remain in deficit in the second half of 2022-23 as credit growth has picked up and the volume of banknotes in circulation has increased.

India overtakes UK to become fifth biggest economy

Just a decade ago, Indian GDP was the eleventh largest in the world. Now, with 7% growth forecast for 2022, India's economy has overtaken the United Kingdom's in terms of size, making it the fifth biggest. That's according to the latest figures from the International Monetary Fund. India's growth is accompanied by a period of rapid inflation in the UK, creating a cost of living crisis and the risk of a recession which the Bank of England predicts could last into 2024. This situation, coupled with a turbulent political period and the continued hangover of Brexit, led to Indian output overtaking that of the UK in the final quarter of 2021, with the first of 2022 offering no change in the ranking.

Our Comments:

Looking ahead, the IMF forecasts this to become the new status quo, with India expected to leap further ahead of the UK up to 2027- making India the fourth largest economy by that time, too, and leaving the UK behind in sixth.

Monetary Policy: September 2022

The Reserve Bank of India's six-member Monetary Policy Committee (MPC) met from September 28-30th to decide on the fifth monetary policy for the fiscal. The RBI announced a 50bps increase in the repo rate to 5.9% amid rising concerns over surging inflation, global headwinds and a slump in rupee to its record lows. The MPC has increased the policy repo rate by 190bps since May to quell inflationary pressure (4% in April and 5.90% currently). The country is expected to have a real GDP of 7%, which has been lowered from 7.2% predicted earlier. The inflation target however has been unchanged at 6.7% for FY23. The rate setting panel has taken cues from its global counterparts, including the US Federal Reserve, to raise the key policy rate for the fourth time in a row.

RBI hiked the repo rate by 50bps at 5.90% and continues to focus on withdrawal of Accommodative Stance; reverse repo rate remains unchanged at 3.35%.

Highlights of Monetary Policy:

- **Repo Rate:** 5.90% (5.40% in August 2022)
- **Reverse Repo Rate:** 3.35% (3.35% in August 2022)
- **Standing Deposit Facility:** Stands adjusted at 5.65%
- **Marginal Standing Facility:** 6.15% (5.65% in August 2022)
- **Bank Rate:** 6.15% (5.65% in August 2022)
- **GDP Projection**: Real GDP growth for FY23 projected at 7% from earlier 7.2%. Q2FY23 at 6.3%, Q3&Q4FY23 at 4.6% and Q1FY24 at 7.2%
- **CPI Inflation:** CPI forecast for FY23 maintained at 6.7%. Q2FY23 at 7.1%, Q3FY23 at 6.5%, Q4FY23 at 5.8% and Q1FY24 at 5%

Our View:

It was pretty expected that the sticky inflation and aggressive Fed coupled with no global economy hinting towards any kind of moderation would prompt the RBI to hike rates. Inflation continues to concern all the economies with India being no exception. And thereby the 50bps hike in the repo rate was very much expected. On the flip, there was reaffirmation of the India resilient theme alongwith CAD being financed comfortably which was taken as a positive. Furthermore, crude to be at $100 for rest of the year was also reassuring. Economic activity in India remains stable which gives the confidence to deal with aggressive policies of other central banks going forward as well. The MPC is expected to continue with the hikes going ahead too considering the adverse global backdrop and overall pressure on the rupee. However, inflation would be watched to assess the impact of the monetary tightening so far. So the reaction of the RBI will be a function of global disruption although the frontloading done consciously should give some breather for sure.

Non Coverage News:

HDFC Bank ties up with Refinitiv for digital transformation, cut costs

HDFC Bank has entered into a long-term partnership with London Stock Exchange group's Refinitiv for digital transformation, new customer acquisition and reduce costs. Refinitiv is one of the world's largest providers of financial markets data and infrastructure. Under the multi-year agreement, comprehensive access to Refinitiv's data and products will enable HDFC Bank to realise new customer opportunities and fast-track its innovation agenda while reducing total cost.

Our Comments:

The long-term strategic agreement with HDFC Bank will support digital transformation and innovation programmes across the whole business in India. It will foster innovation and boost cost savings across multiple bank divisions such as wealth management, capital markets and global markets, risk, compliance, and customer onboarding.

Non Coverage News:

Axis Bank to buy nearly 10% stake in Go Digit Life Insurance

Axis Bank has signed a non-binding term sheet to invest an amount between Rs49.9-69.9cr in Go Digit Life Insurance for 9.94% stake in two tranches, as the private lender seeks to tap a fast-growing insurance market subject to execution of definitive agreements whose terms and conditions are to be mutually agreed upon and fulfillment of other terms and conditions. The company proposes to carry out life insurance business in India, subject to grant of certificate of registration by Insurance Regulatory and Development Authority of India.

Our Comments:

Digit, which already has a presence in the general insurance business, is foraying into the life insurance segment with its Go Digit Life venture but has not yet received a licence for the unit.

Axis Bank to expand financing in EV sector

Keen to make the most of the current push for adoption of EVs, Axis Bank is looking to finance dealers as well as retail buyers of such vehicles. While the private lender has recently tied with Tata Motors for financing EVs, there are more in the offing and the bank sees significant potential in this space. Right now, everything is in short supply but hopefully, once the chip situation is sorted out and inventory levels come back to 30-45-day levels, there will be working capital demand for EVs.

Our Comments:

While the rate of interest is similar, they have a pricing benefit because a lot of states allow some incentives for EVs.

Yes Bank to sell its Rs48,000cr bad loans to JC Flowers ARC

Yes Bank's board has approved the transfer of stressed assets worth Rs48,000cr to private equity firm JC Flowers. Yes Bank will also pick up a 19.99% stake in the ARC. JC Flowers ARC won Yes Bank's non-performing loan portfolio for Rs11,183cr in a Swiss Challenge auction, after a consortium of Cerberus Capital and Asset Reconstruction Company of India (ARCIL) withdrew its bid. The ARC will have to pay Rs1,677cr within 60 days of Yes Bank formally approving the offer. It had paid an earnest money deposit of USD50mn at the time of submitting the bid.

Our Comments:

The bank had already provisioned for over 80% of the total loan value, which will now be transferred to JC Flowers.

SBI raises Rs4,000cr via Tier 2 bonds at coupon rate of 7.57%

State Bank of India has raised Rs4,000cr Basel III compliant Tier 2 bonds at a coupon rate of 7.57%. The public lender also said that the tier 2 bonds attracted overwhelming response from investors with bids of Rs9,647cr and was oversubscribed by about 5 times against the base issue size of Rs2,000cr. Following the response, the SBI has now decided to accept Rs4,000cr at a coupon rate of 7.57% payable annually for a tenor of 15 years.

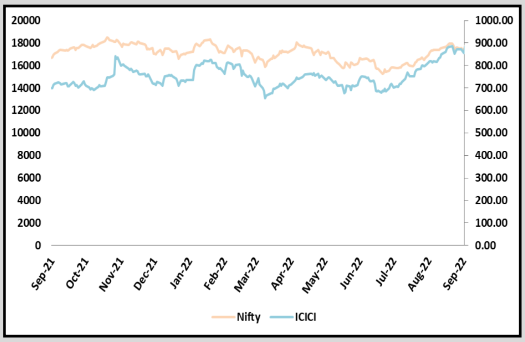
Our Comments:

SBI said that this issuance represents spread of 14bps over 10 year G-sec. The 10 year SDL cut off was at 7.69% annualized on September 20, 2022.

Coverage News:

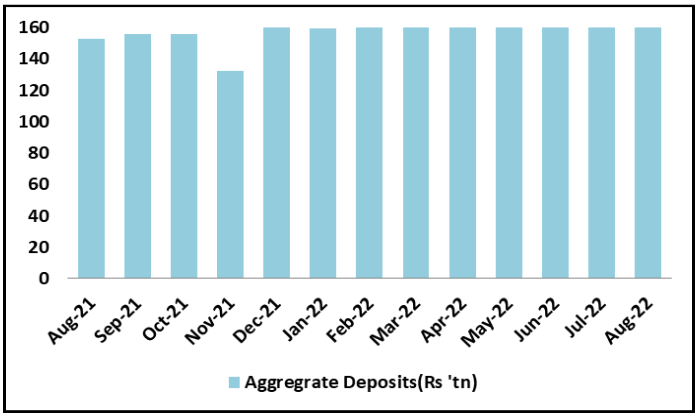
ICICI Bank Limited: The Bank has allotted 21,000 senior unsecured redeemable long term bonds in the nature of debentures aggregating to Rs2,100cr on private placement basis, the date of allotment being September 15, 2022. The bonds are redeemable at the end of 7 years. The bonds carry a coupon of 7.42% p.a. payable annually and were issued at par.

Exhibit 2: ICICI v/s Nifty



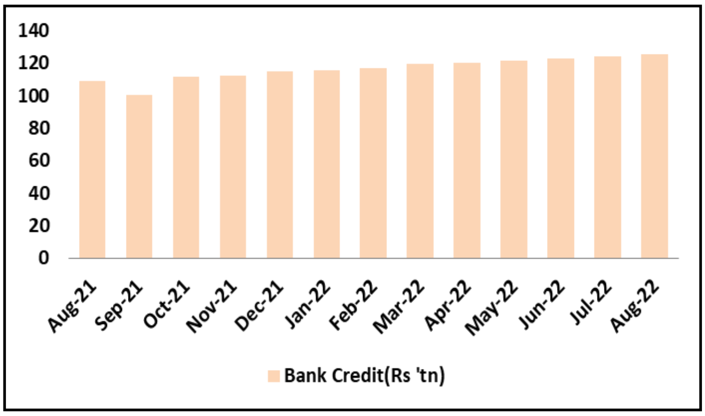
Source: Ace Equity, Progressive Research

Exhibit 03: Trend of Aggregate Deposits of SCBs



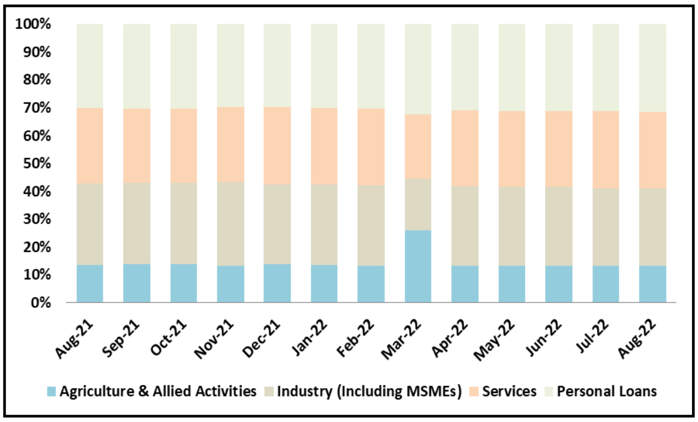
Source: RBI, Progressive Research

Exhibit 04: Trend of Bank Credit of SCBs



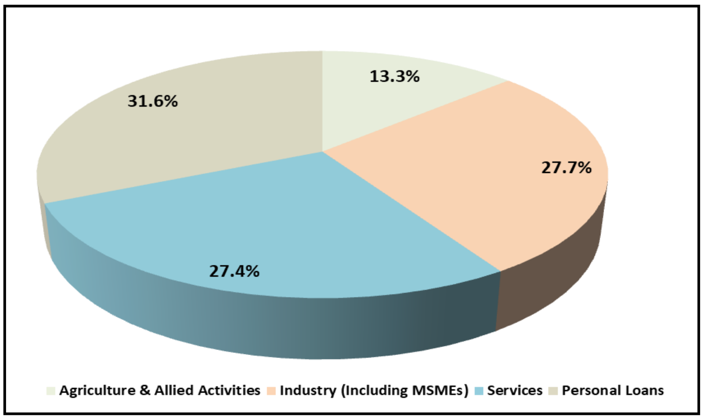
Source: RBI, Progressive Research

Exhibit 05: Deployment of Gross Bank Credit by major sectors



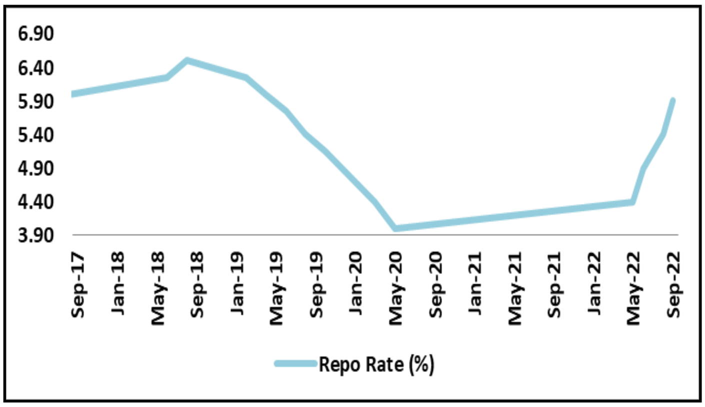
Source: RBI, Progressive Research

Exhibit 06: Sectoral breakup of Gross Bank Credit of the major sectors in Aug



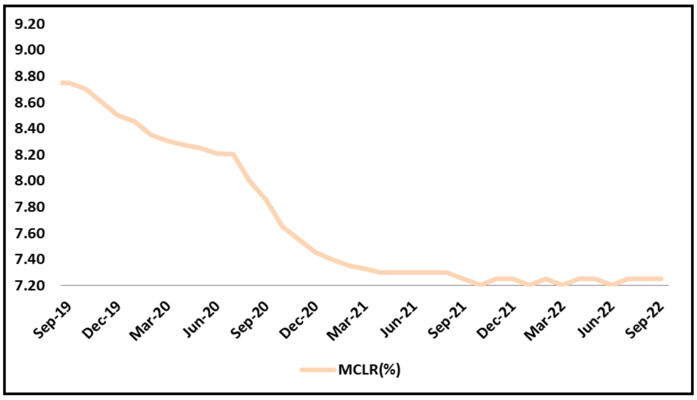
Source: RBI, Progressive Research

Exhibit 07: Repo Rate Trend



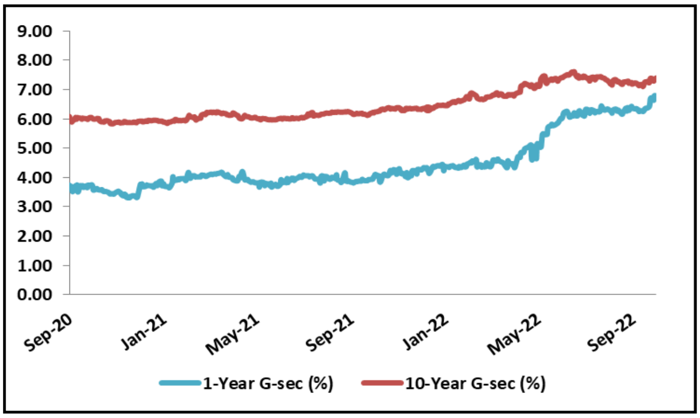
Source: RBI, Progressive Research

Exhibit 08: MCLR trend in the last 3 years



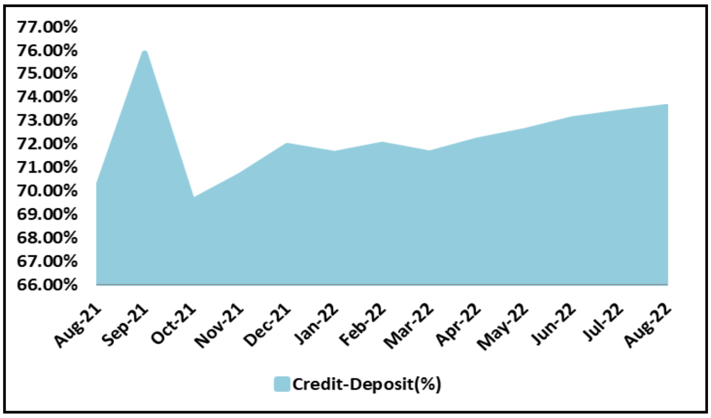
Source: RBI, Progressive Research

Exhibit 09: RBI trying to keep the gap between short and long term bond in check



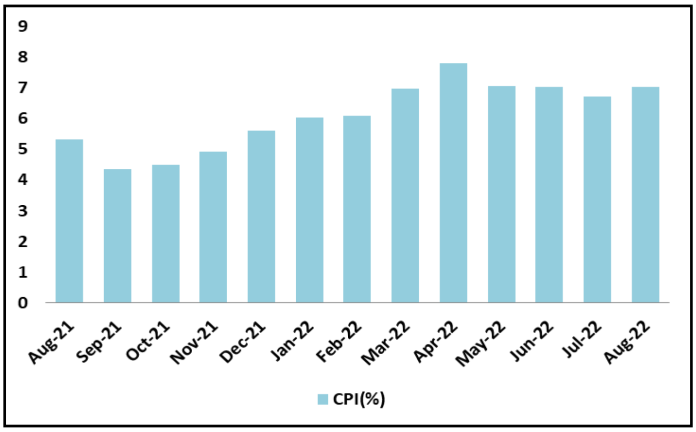
Source: Investing.com, Progressive Research

Exhibit 10: Credit-Deposit ratio of the SCBs in Aug-22



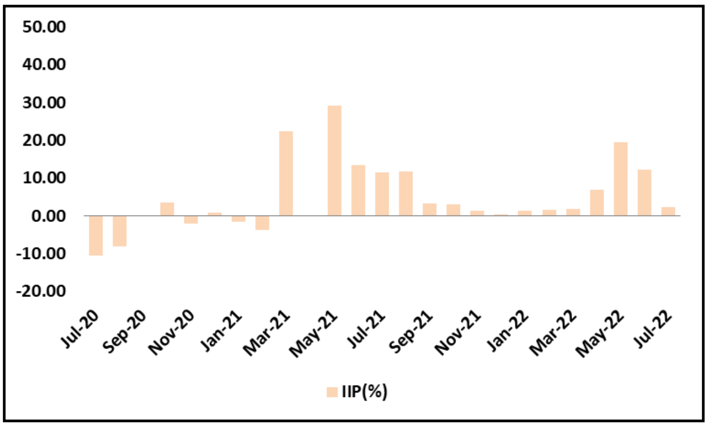
Source: RBI, Progressive Research

Exhibit 11: Retail Inflation Range Bound



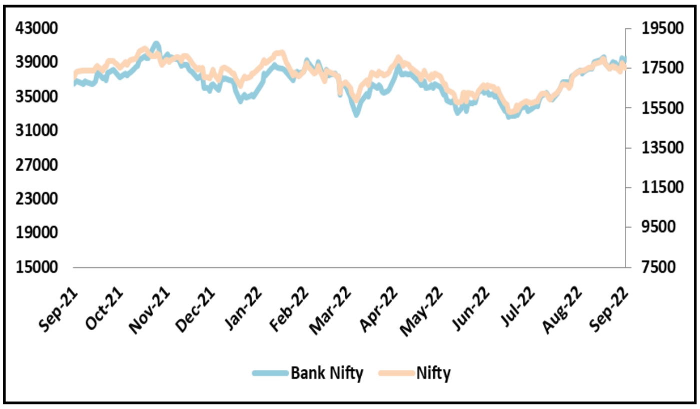
Source: RBI, Progressive Research

Exhibit 12: Change in Y-o-Y IIP data



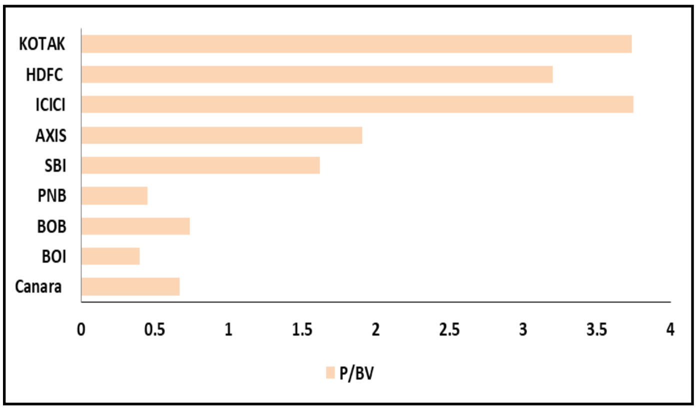
Source: RBI, Progressive Research

Exhibit 13: Bank Index v/s Nifty Index



Source: NSE, Progressive Research

Exhibit 14: Major Banks' Valuation as on 30th September, 2022



Source: Ace Equity, Progressive Research

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