ECONOMIC DIGEST

(February 2020)

1. India: Understanding Economic Slowdown In India: What Steps Have Been Taken To Revive The Economy?- Ashima Obhan and Akanksha Dua

After years of outperforming its emerging market peers, the Indian economy has been running out of steam. Looking at five consecutive quarters of diminishing economic growth, followed by a very weak GDP print of 4.5 % for Q2 of FY 20, the Indian economy is going through one of its most serious crisis. The current economic slowdown in India dates back to the year 2000, and to an economic boom triggering a series of events resulting in today's crisis. A major global economic upswing in the year 2000 increased global demand, and India's exports reached an unprecedented high. India's GDP growth surged to 9-10% per annum. The economic boom triggered an increase in investment, particularly in the infrastructure sector. These infrastructure projects were largely financed by credit from within and from outside India.

The Global Financial Crisis ("GFC") of 2008 – The GFC of 2008 adversely impacted India's exports due to a slowdown in global trade growth. India's export growth rate fell from more than 15% before the GFC to 5% post the GFC. The GFC also triggered an increase in credit interest rates and depreciation of the Indian rupee. This, coupled with the general downturn of the market rendered companies' financial projections made during the economic boom, inaccurate. Various companies found it difficult to profit from ambitious investment projects entered into during the boom, which resulted in them being unable to service their debts. The depreciation of the Indian rupee also adversely affected companies that had made borrowings from outside the country.

The Twin Balance Sheet Crisis (**Banks and infrastructure companies**) -By the year 2015, stressed firms accounted for 40% of corporate debt. The rise in corporate debt meant a corresponding increase in the NPAs of banks, leading to a 'twin balance sheet' problem with 'NPAs or bad loans on one hand, and heavily indebted corporates on the other'. The gross NPAs of banks increased from 2.3% of total loans in 2008, reaching a peak of 11.5% in FY 2017/18, to 9.3% as of September, 2019. The Indian Central Government attempted to solve the twin balance sheet crisis by injecting capital amounting to over Rs. 2.8 lakh crore as of FY 2018/19 into PSBs. PSBs account for 70% of bank loans, and for 90% of total NPAs in India. These capital injections enabled banks to write off Rs. 7.2 lakh crore of their NPA burden, and to reduce their NPA to loan ratios by 2 points, from 11.5% in FY 2017/18, to 9.3% as of September, 2019.

Why did the Indian Economy Continue to Grow? -The demonetization initiative and the introduction of the GST regime have dragged growth down by "still-unknown extents over still-to-be-defined periods." In the long run, however, these negative shocks were offset by stimulus such as the post-GFC oil price decline. At the beginning the year 2014, international oil prices began to fall, and were at one-third of their earlier levels. This provided the Indian economy, with India being an importer of (crude) oil, a windfall, boosting GDP growth by 1.0 to 1.5% during the period of 2015-2017. This, coupled with an increase in world demand in 2017 and 2018, resulting in non-oil export growth, greatly benefitted India's economy.

These events made it appear as though India's GDP was steadily climbing, and concealed the negative effects of demonetization, the introduction of GST, and the twin balance sheet crisis. Another massive stimulus in this regard was the NBFC lending boom.

The NBFC Lending Boom and its Aftermath – The demonetization of high-value currency notes by the Indian Government in 2016 resulted in large amounts of cash being deposited with banks and mutual funds. A large amount of these funds were then on-lent to NBFCs, which subsequently lent them out, mostly to the real estate sector. ILFS accumulated a debt of Rs. 90,000 crore and defaulted on repayment of several of its obligations to its creditors. This jeopardized a large number of real estate and infrastructure projects, banks, mutual funds and other investors associated with IFLS. NBFCs' massive lending to the real estate and infrastructure sector, and subsequent debt accumulation was also affected by the fact that the ambitious projects of the post-2000 economic boom were difficult to complete post-GFC. Most NBFCs were caught in a funding squeeze forcing them to scale back their credit to the real economy. Provision of loans to small businesses, as well as to consumers for durable goods such as automobiles by NBFCs slowed, thus affecting investment in these sectors. The NBFC crisis also affected the lending capacity of public sector banks, some of whose lending to NBFCs amounted to 10% to 14% of loans they extended.

Steps Taken by the Indian Government

Introduction of the Insolvency and Bankruptcy Code, 2016 – The IBC was introduced in December, 2016. The Code aims to complete the insolvency resolution process in a time bound and efficient manner. An important aspect of the Code is the way in which it deals with the issue of NPAs. The Code enables all classes of creditors to file an application for initiation of the corporate insolvency resolution process. The creditors may apply to the relevant authority under Code for the appointment of a resolution professional, who will take over the management of a defaulting debtor. The Code provides for an Insolvency Resolution Plan ("**Resolution Plan**"), and procedure for application thereof, as an alternative to liquidation of the debtor concern/company. The Resolution Plan is to be approved by a creditor committee with a 75% majority. The time period for completion of the Corporate Insolvency Resolution Process ("**CIRP**") is specified under the Code as 180 days, which can be extended by the relevant Adjudicating Authority by a maximum of 90 days. The time limit is an attempt to ensure, *inter alia,* that NPAs are recovered in a time-bound manner so as to reduce stress on banks and other financial institutions. The gross NPA to loan ratio of the banking sector is estimated to have declined from 11% in Q2 of FY, to 9.3% as of September, 2019, a drop which has be attributed, in some part to the CIRP under the Code.

Taxation Reforms – The Taxation Laws (Amendment) Act, 2019 amending the Income Tax Act, 1961 and the Finance Act, 2019 came into force on September 20, 2019. The Amendment Act has introduced certain measures for the benefit of companies. Domestic companies will have the option to pay tax at a rate of 25.17%, as opposed to the 30% rate prior to the Amendment Act. Such companies will also be exempt from minimum alternate tax. Domestic companies incorporated on or after 1st October, 2019 making a fresh investment in manufacturing have an option to pay income-tax at the rate of 15%. This tax rate is contingent upon such companies commencing their production on or before

31st March, 2023. This provision has been put in place in order to boost the 'Make in India' initiative, and to attract fresh investment in manufacturing.

Companies which continue to avail exemptions or concessions under the Act shall continue to pay tax at the pre-amended rate of 30%. However, such companies are allowed to opt for the aforementioned concessional tax regime after the expiry of their tax exemption/holiday period. The Amendment Act has also reduced the rate of Minimum Alternate Tax to 15% from the pre-amended rate of 18.5%.

The Amendment Act provides that the enhanced surcharge under the Finance Act shall not apply on capital gains arising on sale of any security including derivatives in the hands of Foreign Portfolio Investors, or on the sale of equity share(s) in a company, unit of an equity oriented fund, unit of a business trust liable for securities transaction tax, in the hands of an individual, HUF, AOP, BOI and AJP. This provision has been introduced with the intention of stabilizing the flow of funds into the capital market. The Amendment Act also provides that tax will not be charged on the buy-back of shares in case of companies which have already made a public announcement of such buy-back before July 5, 2019.

Environmental Impact Assessment Waived for Oil and Gas Exploratory Drilling – The Ministry of Environment, Forests and Climate Change vide a notification dated Jan. 18, 2020, has waived the requirement of environmental clearance for oil and gas firms conducting exploratory drilling. Promoters of exploratory projects prior to the Notification had to mandatorily prepare an Environment Impact Assessment plan, scrutinized by a committee of experts appointed by the Centre.

2. Will Modi's $5 trillion economy goal be reality by 2025? -FE

Even as BJP government has set itself an ambitious target of achieving a $5 trillion economy by 2024-25, the target can only be achieved by 2032-33, Kaushik Basu wrote. "Compute the size of the GDP and it becomes clear that the target of $5 trillion will be reached not in 2024-25, but in 2032-33," he wrote. India's GDP is growing at a rate of 4.5% and in 2018-19, its GDP stood at $2.75 trillion. "Clearly, in 2019-20, the GDP will rise to $2.87 trillion, which is $2.75 trillion plus 4.5% of 2.75".

Amid India's current economic slowdown, business-as-usual is unlikely to fulfil the $5 trillion economy dream. The government can look into doing "reverse arithmetic" and calculate the growth rate required to reach a $5 trillion economy. "We have to get the nation growing faster than the abysmal performance seen in recent times… Compute the implicit growth rate that will get us there. This turns out to be 10.5%," Kaushik Basu wrote. However, even this turns out to be an ambitious target with only one example of China when the nation grew for six consecutive years at an average annual rate of over 10.5% from 2003 to 2009.
Further, the government also needs a clear roadmap. "For international observers and particularly investors, not to see these creates doubts about professionalism," Kaushik Basu said. More information is also needed as to what $5 trillion economy will mean for granular indicators such as annual growth and inflation.

From 1947 till now, India's economy registered over 10% growth only twice. The first instance occurred because in the previous year, the economy had grown very slowly, by 3.5%; meaning a large part of the subsequent growth was catch-up. Another example of remarkable growth was in 2007-8, which also brought massive FDI's in the country. For now, the two best shots for India are — "a huge policy initiative to boost real growth or the luck of a dollar depreciation".

3. Liquidity crunch continues to hurt NBFCs, GDP growth – Fitch

Operating conditions for Indian non-banking financial companies/institutions (NBFCs or NBFIs) have improved slightly in the first two months of 2020, however, uncertainty levels continue to be high for certain segments within the sector such as housing finance and wholesale lending. "The recent fundraising by a number of NBFIs during the first two months of 2020 points to a slightly improved funding environment. Fitch expects NBFIs to continue to tap the offshore market, but access is likely to remain uneven and limited largely to retail-focused NBFIs and those backed by large corporate groups. "Wholesale and housing finance companies are the most at risk as they will continue to find it difficult to raise funds – given their greater exposure to the real-estate sector where we expect further pressure on cash flows and collateral values." NBFCs play a crucial role in the Indian economy due to a failure by the banks to address the needs of the majority of the people and small businesses.

Due to high levels of red-tape, getting a loan from a bank is nearly impossible for those without a predictable and demonstrable levels of income. The excluded segments typically include those who work in the informal sector as well as small businesses, which are considered too risky. As such, various types of non-banking finance companies, including those specializing in small and medium enterprises, micro-finance companies, gold loan providers and housing loan providers, accounted for the majority of the loans provided in India. They, in turn, used to get their funds from banks and debt mutual funds. However, due to a crackdown on bad loans, nepotism and cronyism in the banking sector, fund flow from banks have dwindled over the last several months, affecting NBFCs' ability to operate. The situation was complicated by revelations of corruption at IL&FS and defaults by Dewan Housing Finance Ltd.

The liquidity crunch continues to have an economy-wide impact. "Fitch expects India's real GDP growth to slow to 4.6% in FY 20 from 6.8% in FY19, led by a squeeze in credit availability from non-bank financial institutions (NBFI) and deterioration in business and consumer confidence, with a modest rebound to 5.6% for FY21. Funding conditions are therefore likely to remain weak and Indian FIs risk-averse in the year ahead – in line with Fitch's negative sector outlook for both banks and NBFIs." Concerns around asset-quality are likely to intensify even more if the stress on non-banks, real estate and SMEs remain unresolved. "The support measures from the authorities have had a mixed effect, with the onus largely on banks' weak balance sheets through higher lending and regulatory forbearance."

4. Coronavirus outbreak To Impact Global Economic Growth, India Needs to Remain Watchful-RBI Chief

The death toll from the Coronavirus epidemic in China crossed the 2,000 mark, while the overall number of confirmed cases climbed to 74,185. India needs to "keep a very close watch" on the impact of the Coronavirus outbreak in China… segments of Indian industry including pharmaceuticals, mobile handsets and electronic manufacturers are dependent on China for the import of raw materials, while also insisting that the Indian pharmaceutical sector's raw material supply will be "maintained". "Most of the large pharma companies always keep stock for three-four months. So, they should be able to manage, and the virus outbreak has not impacted those provinces from where these pharma intermediates are sourced. Therefore, there is an expectation that the supply of raw pharma- materials will be maintained," Das said.

Indian drug makers import almost 65-70 % of their Active Pharmaceutical Ingredients (API) - the basic building blocks of drugs - from China. Even though the current stocks should last until April, the Indian government held a high-level meeting on domestic manufacturing of API… the Indian government will soon come up with a comprehensive API manufacturing policy. Makers of mobile handsets, TV sets and certain other electronic products in India are also dependent on China. "There again our manufacturers must be able to develop alternative places of sourcing these raw materials," the RBI chief maintained.

China accounts for 45 % of India's total electronics imports. One-third of machinery and almost two-fifths of organic chemicals that India purchases from the world comes from China. ″Automotive parts and fertilisers are other items where China's share in India's import is more than 25%. India sources about 65-70% of active pharmaceutical ingredients and close to 90% of certain mobile phone parts from China," the FICCI said.

5. Modi government does not acknowledge word 'slowdown' - India Blooms Service

Former PM Manmohan Singh said the Modi government does not acknowledge the word "slowdown"… The government's economic policy came under the scanner over the falling of GDP, which recorded 4.5% in the immediate last quarter, over the last several quarters…the IMF in its WEO said the domestic demand in India reduced "more sharply than expected" apart from the stress in "non-bank financial sector" and a "decline in credit growth". IMF chief economist Gita Gopinath had said the slowdown in the Indian economy is expected to impact the growth of the world economy.

6. India Becomes 5th Largest Economy Overtaking UK And France - Brinkwire

India overtook France and the U.K. to become the fifth-largest economy in 2019, a U.S. think tank has said. India with a nominal GDP, of $2.94 trillion is narrowing the gap with Germany, which is now in the fourth place with a GDP of $3.86 trillion. The nominal GDP is the total value of all goods produced and services provided within a specified geographical unit at current prices, as opposed to real GDP estimated at constant prices…India's real GDP growth, however, is expected to weaken for the third year straight from 7.5% to 5%,

according to the report. RBI lowered its estimate of GDP growth for the 2019-20 to 5% in December from the estimate of 6.1% made in October. India's economic liberalization that began in the early 1990s including industrial deregulation, opening up of the economy to foreign trade and investment, and privatization of state-owned enterprises, has helped meet growth targets. "These measures have helped India accelerate economic growth," it said. India's services sector is among the world's fast-growing ones, accounting for about 60% of the economy and 28% of employment. Manufacturing and agriculture are two other significant sectors that have received special government attention… launched the Make-in-India initiative for revitalizing the manufacturing sector… the Modi administration initiated direct payment into farmers' bank accounts to boost the economy's liquidity. The national budget has given a further push to various programs including privatization and economic liberalization to make India a $5 trillion economy by 2025.

7. When will India's economic slowdown end?-IT

During the Budget Session, FM said that "green shoots were visible" indicating that the economic slowdown might be over. Recovery was on the cards. But Moody's thinks otherwise. It has revised its estimate about GDP growth rate of India for calendar years 2020 and 2021. There is marked decline in growth projections for Indian economy compared to Moody's forecast made in November 2019. In four months' time, Moody's slashed growth forecast for Indian economy to 5.4 % from 6.6 %for 2020 -- a difference of over one percentage point. The updated GDP growth estimate for 2021 is 5.8 %, down from 6.7 %.
Moody's estimated that Indian economy grew by 5 % in 2019- the estimate that Sitharaman projected for GDP growth for 2019-20 financial year. This comes on the back of a rather distressing quarterly GDP growth rate figure of 4.5 %for July-September 2019 -- the slowest in more than six years. At 5 %, the GDP growth rate for 2019-20 is the lowest in 11 years.
Moody's prediction of GDP growth rate staying at around 5.4 per cent this year is much lower than the government's estimate. The Economic Survey estimated that Indian economy would grow by 6-6.5 % in 2020-21.
CEA KV Subramanian asserted earlier that economic slowdown has bottomed out. But Moody's downward revision of the growth figures raises a doubt on assertion of economic slowdown having bottomed out. The Moody's pins its hope on the easing of key rates by the RBI, which has been cautious in the wake of rising retail inflation. The RBI, however, slashed repo rate by a cumulative 135 bps through 2019. But further easing of the rates would depend on how inflation stays.
Retail inflation hit a 68-month high (5 years 8 months) of 7.59 % in January this year. The RBI aims to cap inflation at 4 % over the medium term. Its mandate for retail inflation is in the target range of 2-6 %. High inflation dictates what the RBI does with the key banking rates. In the absence of credit impetus from the banks, early revival of credit to industry, services and even agriculture appears difficult. But further easing of rates may push inflation further up. This is a catch-22 situation for the RBI, which earlier this month revised India's GDP growth forecast downward for first six months of the next fiscal. It slashed growth rate for April-September 2020 to 5.5-6.0 % from its earlier prediction of 5.9-6.3 %. However, politically, India and the government may take comfort from the fact that the Moody's has kept China's GDP growth rate forecasts lower than India's -- 5.2 % to 5.4 % for 2020, and 5.7

% to 5.8 % for 2021. But is that enough to meet much publicised target of making India a $5 trillion economy by 2024-25?

8. India needs a ground-up growth model for an inclusive economy-Mint

One group of economists is fixated on interest rates and fiscal deficits as the levers to improve the health of the economy. They debate the impact on economic growth of decimal point differences in interest rates and ratios of fiscal deficit to gross domestic product. All this, even though they do not have a good model of the role of money in an economy, as Robert Skidelsky explains in *"Money And Government: A Challenge To Mainstream Economics"*. Another group of "trade economists" sees opportunities for India in greater integration with global trade. These economists are alarmed by the weakening of the spirit of the 1991 reforms and the return of protection of domestic industries. But as economists like Dani Rodrik, Ha-Joon Chang and others have pointed out, countries that now promote free trade, like the US, had achieved growth by protecting their own infant industries.

A large group of economists is concerned that governments are interfering with the "magic" of the market. Their political heroes are Margaret Thatcher and Ronald Reagan, who promoted the thesis of Milton Friedman and the Chicago school of economics that governments are the problem and not the solution. The market is poisoned by a concentration of market power. In economies where the "business of business must be only business" and where private participants are expected to pursue their self-interest, self-regulation is an oxymoron. They reluctantly accept that governments must shape the rules of the game for the market to work its magic.

The dominant school of economics for the past 40 years has concentrated on framing regulations (and their reduction) to make economies attractive for investors. It measures an economy's health by the size and growth of GDP. Countries, including India, have seen their GDP grow by adopting this ideology and the rules that flow from it. At the same time, the wealth of investors at the very top has grown much faster than the incomes and wealth of citizens in the lower half of the pyramid. This has fuelled the rise of anti-establishment, "anti-expert" populist movements around the world. Citizens are asking whose interests these economists, or the policymakers who accept their advice, serve.

Some economists question the dominant paradigm. They view economies "bottom-up" and "inside out" from the perspective of people at the bottom. Unlike the dominant school which takes a "top-down" and "outside in" view from investors' perspectives. The ruling school derides them as "socialists" and "anti-growth". First grow the pie, before you redistribute it. Whereas the bottom-up, people-first school's view is that to grow the pie, there must be human development alongside, with significant public investment in education and health.

Economists now agree that structural reforms are necessary to revive the Indian economy…

Gandhi (and J.C. Kumarappa, his long-time adviser in economics) differed with Jawaharlal Nehru (and his advisers) on the best economic model for inclusive growth. Gandhi envisaged a model in which producers would be owners of their tiny enterprises. The charkha was a symbol. He wanted constructive workers to create wealth for themselves, and not be mere wage earners enriching remote owners.

Gandhi advocated policies that would support the growth of wealth in tiny enterprises, in which people would work and take risks to generate incomes and wealth for themselves. Nehru chose the other path of promoting large enterprises. And since private capital was not

sufficient then, these were state-owned. In both—state owned enterprises and capitalist enterprises owned by remote investors—humans are merely workers and wage earners. The wealth created by their efforts accumulates with remote owners who decide what it will be used for. The State takes some for its maintenance and is expected to spend the rest for the benefit of people. Investors spend on their own welfare and may use what's left to "give back" to society through philanthropy and corporate social responsibility activities (or taxes).
Some Nobel laureates in economics recommend a new paradigm for inclusive growth. Joseph Stiglitz, Jean-Paul Fitoussi, and Martine Durand, in their book Measuring What Counts, suggest a model driven by the well-being of citizens, rather than an obsession with GDP. So do Abhijit Banerjee and Esther Duflo in *Good Economics For Hard Times*.
Economists must evolve new ideas. India's economy is often compared with an elephant: large and plodding, and difficult to turn. The insufficient increase in employment and incomes at the bottom and the slow pace of human development while GDP grows and millionaires multiply causes concern.

9. Money flow from banks to NBFCs picks up in Oct-Dec-ET

Mortgage lenders, viz., Tata Capital Housing Finance, Piramal Capital & Housing Finance, Housing Finance and L&T Housing Finance have raised nearly 80 % of the Rs 15,000 crore secured loans sanctioned by banks to HFCs in the December quarter. While PNB raised the most at Rs 5,250 crore, Piramal was a close second with Rs 3,650 crore followed by Tata and L&T. Almost 90% of this funding was contributed by PSBs. "Borrowing activity among non-bank lenders and housing finance companies has been largely slow. Even the December quarter showed that banks leaned towards the best-rated companies and this largely seems to be driven by the partial credit guarantee scheme," said Sandeep Reddy, Propstack. While PSBs are slowly opening their purse strings, risk aversion towards shadow banking and mortgage lending space still remains. Smaller and mid-sized housing finance companies like Magma and Repco managed to raise a part of the Rs 3,000 crore distributed among such firms. SBI, PNB, Union Bank of India, Corporation Bank, Bank of India, Central Bank of India, United Bank of India, Karnataka Bank and Indian Bank were the major lenders. Three private banks - Yes Bank, Standard Chartered Bank and Axis Bank - sanctioned loans to this sector in the December quarter. "Asset quality trends remain weak, given stress mainly from developer financing portfolio and some pockets of stress even in vehicle finance for select players," Emkay Global said. "However, money supply for the sector witnessed some improvement with NBFCs continuing to diversify their borrowing sources toward banks, international and retail markets instead of the traditional capital markets, while securitisation market too is opening up."

10. Coop. sector can generate large number of jobs: Satish Marathe-Hindu

RBI Director Satish Marathe said that thousands of jobs can be created by increasing the quantum of food processing through the cooperation sector as India's food processing achievement is just 20 % as against 70 % in developed countries... there were over 65,000 cooperatives in the country that were running profitably. Profit can be earned through extension and proper planning in cooperative mode.

10. Market asking if the next interest rate move depends on GoI's finances-ET

Much of the equity market's budget disappointment was that the budget, which aims to cut the headline deficit from 3.8% of GDP last year to 3.5%, was devoid of any material tax cuts or increased spending when GDP growth has dropped to its lowest since the 2008-09 global crisis. The reality is, however, different. Most countries do not count privatisation as revenue, but as a source of financing fiscal deficit since it's just a redistribution of savings from the private sector to the government. It does not change overall demand in the economy. Excluding privatisation from revenue, as it should be, a very different picture of the fiscal stance emerges. The underlying deficit in 2018-19 at 3.9% (headline deficit 3.4%) widened to 4.1% (headline 3.8%) in 2019-20, providing 0.2% in fiscal support. For 2020-21, the underlying budgeted deficit is 4.5%, excluding the outsized 0.9% of planned privatisation. This implies a doubling of fiscal support of 0.4%. Of course, it is uncertain whether privatisation and tax collection targets will be achieved and modest fiscal changes are sufficient to put India back on its winning way. But, GoI intends to provide substantial fiscal support this year. While the MPC held rates citing high inflation, RBI announced new liquidity measures, including one and three-year repos with banks. .. they raise questions about India's monetary policy framework. The shift to a formal inflation-targeting framework in 2015, and the delegation of all authority regarding interest rate policy to MPC for the first time, separated monetary policy from RBI's many other functions, including managing GoI's debt This, by far, has been one of GoI's most effective and far-reaching structural reforms.

There's a rate cut, there's not

What happened on February 6? MPC revised higher its inflation forecast for the year on the back of the recent rise in food prices and kept policy rates on hold. At the same time, RBI announced the new long-term repo operations (LTROs) that effectively cut yields on medium-term government paper by about 25 bps. Thus, while MPC found the rise in inflation sufficiently disconcerting to keep policy rates on hold, RBI found it benign enough to effect a cut in interest rates…puzzled by MPC's inability to look past the transient rise in food inflation as implied by its own 2020 forecast and continue to cut rates. India's real lending rates (deflated with core inflation) have risen relentlessly over the past 12 months. The hoped-for domestic recovery is likely to be delayed by the outbreak of coronavirus, substantially damaging near-term global demand and intensifying global disinflation. Instead, my question is whether this is the new de facto monetary policy framework, whereby MPC decides the overnight rate and RBI the rest of the yield curve. Many will argue that the reduction in medium-term rates is an unintended consequence of LTROs, which aim to provide liquidity to improve monetary transmission and boost credit.
First, policymakers need to be wary of inadvertent spillovers from their policy choices. Second, with excess interbank liquidity at 1.5% of GDP, it is doubtful whether further injection of liquidity will boost credit. On the one hand, demand for credit is low because of weak growth. On the other, banks have appropriately tightened lending standards after the painful restructuring of bad loans over the last 18 months.
There is nothing wrong with a central bank controlling the yield curve. After all, don't all the G3 (US, EU, Japan) central banks effectively do the same? True, for the most part. But there

is a difference. These central banks resorted to unconventional monetary policy only after policy rates had hit zero, not when they were above 500 bps as in India. In addition, economic efficiency demands that the central bank influence the interest rate structure with minimal control and allow the market to determine the price and allocation of credit. This implies controlling rates at the shortest horizon, not the entire term structure.

Separation of church & state

Separately, even if not intended, LTROs could well be misconstrued as ways to reduce government borrowing costs. For years, GoI has been urged to relieve RBI of debt-management responsibilities and entrust these to an independent agency, as in most developed and advanced emerging market economies. This is because the two objectives — monetary policy and debt management — can lead to contradictory choices about interest policy, as is the case now. If the market starts to ask whether growth-inflation dynamics, or the state of government finances, will decide the next interest rate move. While governments, both past and present, have shown little urgency in establishing an independent debt management agency, the formation of MPC and the formalisation of RBI's monetary policy objective since 2015 had been providing some degree of separation between RBI's two roles. This had helped to greatly clarify RBI's communications and, in turn, deepen credibility. Alas, these old disconnects have now resurfaced.

12. MSMEs bank loans: access to money easier- Zee Business

Over the last few years, India's economic growth has been bolstered by MSMEs. Contributing a whopping 30 % to the country's GDP, the 63 million MSMEs in India also attribute to 45 % of the manufacturing output and is home to livelihood for over 110 million Indians. Despite challenges such as lack of adequate credit, infrastructure, technology, remote and inaccessible markets, the sector has held strong and is touted to be the torchbearers of India's vision of becoming a $5 trillion economy by 2024-25. Mehernosh Tata, Head, Edelweiss SME Lending said, "the Indian government foresees the MSME sector contributing up to $2 trillion as India eyes becoming a $5 trillion economy by 2024. However, the major impediment to this is that access to low-cost credit for working capital requirements remains the primary challenge for the sector. Despite the contribution they make to the country's economy, MSMEs are deterred by a lack of access to a quality credit line for investing in business and expansion plans, often, derailing the entrepreneurs from their vision. Industry estimates indicate that the current credit flow to this sector is approximately Rs 13 trillion." In continued alignment with the formalisation of the MSMEs, there will be a need for increased transparency in accounts reporting, requisite collateral for access to credit and support from financial players and fintech, would be needed for the sector to relentlessly tap demand in domestic and international markets.

An IFC-Intellecap report indicates that only 16 % of MSMEs are being financed by formal banking; more than 80 % of the MSMEs have no form of financing from the formal system. Financial institutions are unable to adequately lend to MSMEs given challenges in credit risk

assessment owing to lack of financial information, historical cash flow data etc. On MSMEs credit flow Tata, said, "For this to be addressed and increase flow of credit, MSMEs need to ensure adherence to accounting standards with updated bank statements. This helps financial institutions effectively judge creditworthiness and repayment capacity. It is a key parameter used to offer to lend. Additionally, MSMEs must focus on moving from cash transactions into bank transactions that can accurately reflect the turnover of the entity for the purpose of disbursal assessment."

Digitally available data is eliminating uncertainty in acquiring and underwriting SMEs and customers. The Government of India has made consistent efforts through targeted policy interventions to address credit issues, e.g., the Udyog Aadhaar scheme is a 12-digit government registration that is provided along with a recognition certificate and a unique number in order to certify MSMEs. A registered MSME will be eligible for benefits under government schemes such as guarantee free loans, easy loans, low-interest loans, government subsidies, etc. Having a Udyog Aadhar number is now imperative for MSMEs. Other schemes introduced by the Government include:

1) Zero Defect Zero Effect – concessions on goods manufactured for export;
2) Quality Management Standards & Quality technology Tools – activities conducted to sensitise businesses about new technology;
3) Grievance Monitoring System – to address complaints of business owners;
4) Incubation – Financial support to promote new ideas, designs, products, etc;
5) Credit Linked Capital Subsidy Scheme – capital subsidy provided to the business owners to replace their old and obsolete technology; and
6) Women Entrepreneurship – capital, counseling, training for women entrepreneurs.

13. RBI remains focused on growth, says governor Shaktikanta Das-Mint

The RBI remains focused on boosting economic growth but decided to pause on rate cuts following a spike in inflation. “On the whole, inflation has remained under control during the last three-and-half years but for the recent spike on account of spike in vegetable prices, of which onion was the major factor… Going forward, we do expect it to moderate. With this temporary spike in inflation, we have not shifted our attention from growth. We are still focussed on growth. Because of the spike in inflation, we have decided to take a pause," Das said. RBI has also started reviewing the monetary policy framework, and expects to hold a roundtable with various experts “sometime in June 2020." “…The legal provision in the RBI Act says that price stability should be the prime objective keeping in mind the objective of growth. So, the prime target is price stability 4% +/- 2%. But keeping that as the prime target, the aspect of growth has to be taken into consideration. Internally, we have already started a review of the working of the monetary policy framework in the last three-and-half years. And going. Once our review is over, then we will place the outcome of our review before stakeholders. Based on that, we will take it forward. If there is a requirement, we will also take it up with the government," the Governor said.

Deceleration, during the current financial year came as a surprise to almost everybody but the RBI was "not so surprised as most others." "Right from the February 2019 monetary policy, when we started cutting rates, the market was surprised. We started cutting rates from February 2019 because the slowdown in the growth momentum was very clearly visible from the incoming data. And we do nowcasting internally. So RBI decided to act proactively and cut rates five times after February. By the third cut, all analysts agreed that RBI had acted proactively. Many central banks also initially expressed surprise at our decision to cut rates as early as February 2019," he said. Amid growing concerns over the economic fallout of the novel coronavirus outbreak, Moody's slashed its 2020 growth projection for India from 6.6% earlier to 5.4%. The agency expects a shallower recovery, considering that global growth will likely take a hit following the virus outbreak in China. The Indian economy is expected to grow at its slowest pace in 11 years at 5% in 2019-20. The Economic Survey has pegged GDP growth at 6-6.5% for 2020-21.

14. India Gilts Review: End up as RBI steps continue to support appetite-Cogencis

Government bonds ended slightly up because the appetite for dated securities remained robust after the steps taken by the RBI to boost liquidity in the banking system on Feb 6. Today, the 10-year benchmark 6.45%, 2029 bond closed at 100.44 rupees or 6.3864% yield as against 100.42 rupees or 6.3895% yield on Monday. RBI revised its liquidity management framework which removed quantitative ceilings on surplus liquidity in the banking system. The RBI also introduced long-term repo operations up to 1 trln rupees at the repo rate for tenors of one-year and three-year.

Yield on short term bonds have fallen sharply over the past few days as market participants expect part of the additional liquidity to be used to purchase bonds yields of which are at a spread of around 50-70 bps. Yield on the five-year 7.32%, 2024 bond has fallen by close to 30 basis points and that on the 10-year benchmark 6.45%, 2029 bond has fallen by 12 basis points, since Feb 5.

Most traders expect bond yields to continue to fall with yield on the 10-year benchmark 6.45%, 2029 paper seen declining to 6.25% in the coming weeks. Investors have perceived the central bank's comfort on surplus liquidity in the banking system and the intent to add to this liquidity through long term repo operations as a sign that interest rates may remain "lower for longer" until green shoots of economic growth take firm root. India's industrial output for December contracted by 0.3% far below the consensus estimate. A contraction in industrial output indicates investment and consumption demand in the economy still remains sluggish. Industrial output grew 1.8% in November. The RBI cut the repo rate cumulatively by 135 bps last calendar year in order to boost economic growth. When retail inflation showed signs of a sharp rise, the central bank shifted its focus on expediting the transmission of interest rates. In the monetary policy meeting earlier this month, RBI said it had launched Operation Twist with an aim to improve transmission in corporate bond market and yield on government securities had just been in line of transmission. The revisions announced on liquidity management and additional liquidity through long term operations may not be rolled back soon because the economic slowdown remains largely a demand-based problem. "Right

now the liquidity is here to stay and for much longer time than before because you have problems in demand within the economy," a dealer with a private bank said. "There has been a focus on deleveraging in some sectors and so there is no question of demand rising suddenly because of a large liquidity. Whatever problems we are having on inflation side continue to remain a supply side problem."

Earlier few bond traders chose to book profits after the recent surge in prices. Some traders were also cautious over which securities may be offered in the switch operation which will be conducted on Monday. In a switch operation, the government offers to switch security of a shorter tenure with a longer term paper in order to smoothen its own maturity profile by delaying the repayment. However, since yield on the 10-year benchmark 6.45%, 2029 bond is not expected to rise above 6.40%, traders bought the paper at those levels.

Trade volumes remained muted today because some market participants avoided large bets ahead of holidays. Marketwide turnover fell to 457.80 bln rupees from 455.70 bln rupees on Monday, according to the RBI's Negotiated Dealing System – Order Matching platform.

Bonds in the 10-14 year maturity bucket may be weighed by expectations of a rise in supply of such bonds through switches. Bonds in the 1-5 year maturity bucket may remain supported by RBI's steps on liquidity management and long term repo operations. Yield on the 10-year benchmark 6.45%, 2029 bond is seen in a band of 6.35-6.40%.

	TODAY		MONDAY	
	Price	Yield	Price	Yield
7.32%, 2024	104.8550	5.9185%	104.7900	5.9385%
7.27%, 2026	105.2000	6.2346%	105.1500	6.2449%
7.26%, 2029	104.5350	6.5773%	104.5900	6.5697%
6.45%, 2029	100.4425	6.3864%	100.4200	6.3895%
7.57%, 2033	107.8400	6.6711%	107.9000	6.6648%

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