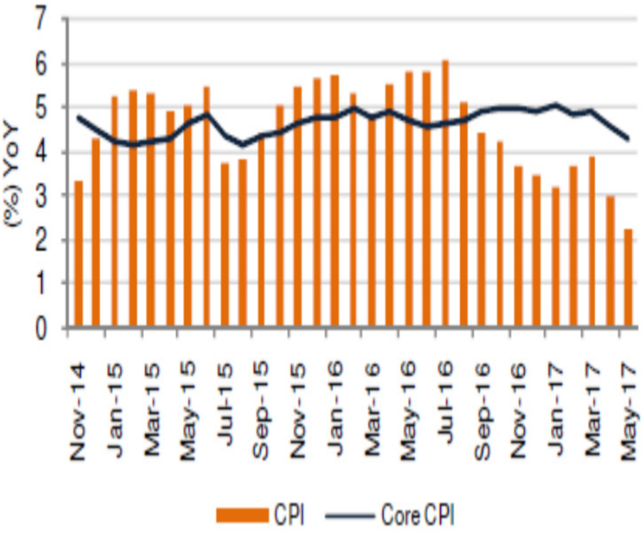
Monthly Political & Economic Updates

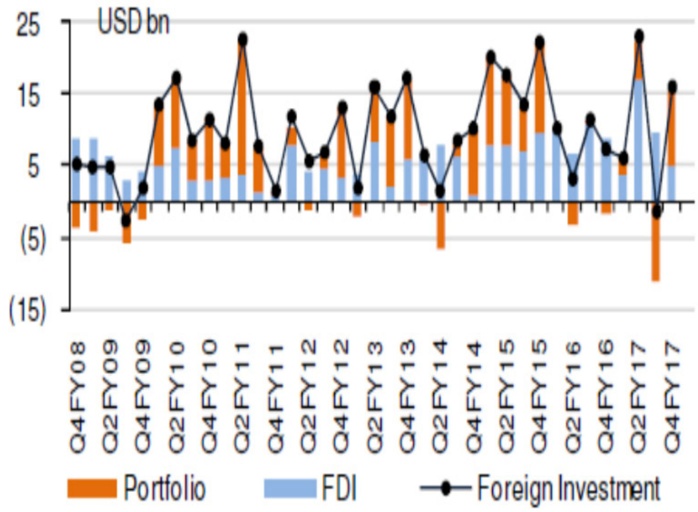
June 2017

Indian CPI & Core CPI Inflation (% yoy)



Source: MOSPI, UTI MF

Foreign Investment into India - portfolio flows turns positive again



Source: CSO, UTI MF Research

1. Inflation hits a series low in May's reading, consumer price index softens further

At 2.2% year-on-year (yoy) the CPI came in significantly close to the lower end of the Reserve Bank of India's (RBI) comfort band. This is compared to just under 3.0% a month ago. Continued softening in price pressures was attributed to subdued food price inflation and low crude oil prices. Core inflation also moderated to 4.3% from 4.5% in April.

2. Current account deficit continues to narrow further in the fiscal year ending March 2017

On a cumulative basis for FY17 India's CAD came in lower at 0.7% of GDP versus 1.1% in FY16 on the back of a lower trade deficit (yoy contraction recorded in imports versus a 5.0% growth in exports). Foreign Direct Investment (FDI) remained steady at $35.6 bn, and foreign institutional investor (FII) inflows were higher at $7.5 bn reversing the outflows in FY16. For the quarter specifically (Q4FY17), India's CAD was wider than a year ago. However strong portfolio flows led to a significantly higher accretion to FX reserves ($21.5 bn in FY17 versus $17.9 bn in FY16).

3. RBI holds rates in its June 7th monetary policy review, lowers inflation forecast

The Monetary Policy Committee (MPC) left the benchmark Repo rate unchanged at 6.25%. CPI projections were lowered to 2.0-3.5% in the first half FY18 and 3.5-4.5% in second half FY18. It also lowered the FY18 Gross Value Add (GVA) growth forecast by 10bps to 7.3%. Whilst a lower inflation trajectory was recognised, the RBI stuck to its neutral policy stance and implied it would monitor the sustainability of these lower inflation numbers before lowering rates further. Nonetheless the more dovish tone in policy language resulted in both equity and bond markets rallying.

4. RBI continues to ensure ample liquidity in the financial system

The RBI lowered the Statutory Liquidity Ratio (SLR) by 50bps to 20% of NDTL (with effect from the fortnight beginning June 24). The SLR is the portion of bank deposits that have to be invested in government bonds. This move ensures banks have enough flexibility to meet the minimum Liquidity Coverage Ratio (LCR) requirement of 100% by January 1st 2019 in an efficient manner.

5. State-run Chinese companies seek investments in India via stakes in power and construction sector

Chinese firms such as China Harbour Engineering Co. Ltd and China Datang Corp are reported to be looking to buy stakes in Indian companies on the back of India's infrastructure development programme. Meanwhile China Southern Power Grid may be bidding for power transmission projects in India. With plans to invest as much as $59bn (3.96 trn rupees) in the current fiscal year in integrated infrastructure projects such as roads and railways, foreign firms have shown interest in India infrastructure investments.

6. US plane maker Lockheed Martin Corp ties with India's Tata Advanced Systems Ltd. to manufacture F-16 fighter jets in India

This agreement was struck under India's "strategic partnership model" - which allows local private sector companies to form JVs with foreign defence equipment makers. India is in need of 200 more fighter planes. The agreement with Lockheed Martin, the biggest defence contractor globally, now enables jet manufacturing in India. Such partnerships are deemed positive for generating employment and for growing India's manufacturing base. Boeing, BAE systems, Airbus and Saab are also reported to be eyeing the Indian market.