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RATINGS & RESEARCH

Macro Pulse Report

November 2023

From the desk of the Chief Economist

Dear Readers,

Hope you had an enjoyable festive month! Many of us have been disappointed that India team came close but couldn't get their hands on the ICC World Cup Trophy. It's an expectation that didn't come true, but it has surely done its bit to push up consumption demand in the months of Oct-Nov'23 along with the regular festivities. Urban demand has reportedly been strong as reflected by a step up in passenger vehicle sales, on-line food deliveries, airline traffic and hotel occupancies. The resilience in urban demand is clearly one of the primary drivers of the current momentum in the Indian economy albeit there may be some impact of the latest RBI circular which seeks to tighten the sharp growth in consumer lending. On the other hand, there are indications of a weaker rural demand in the second half of the fiscal due to the El Nino phenomenon and the estimated shortfall in the kharif crop along with the risk to the rabi crop.

From the growth perspective, India had a strong first half in FY24 with the growth print in Q1FY24 high at 7.8% YoY likely to be followed by a solid 6.8% YoY in the second quarter, going by the **Acuité Macroeconomic Performance index (AMEP)** which is based on a wide range of high frequency indicators. While economic activity in the core sector has continued to be propelled by public investments in the infrastructure sector, persistent headwinds on the export front, higher interest rates along with a tighter funding environment for consumer loans and weaker agricultural output due to the El Nino phenomenon can pose risks to the growth trajectory. We expect 5.0%-5.5% growth in H2FY24 and hold on to our base forecast of 6.0% for FY24.

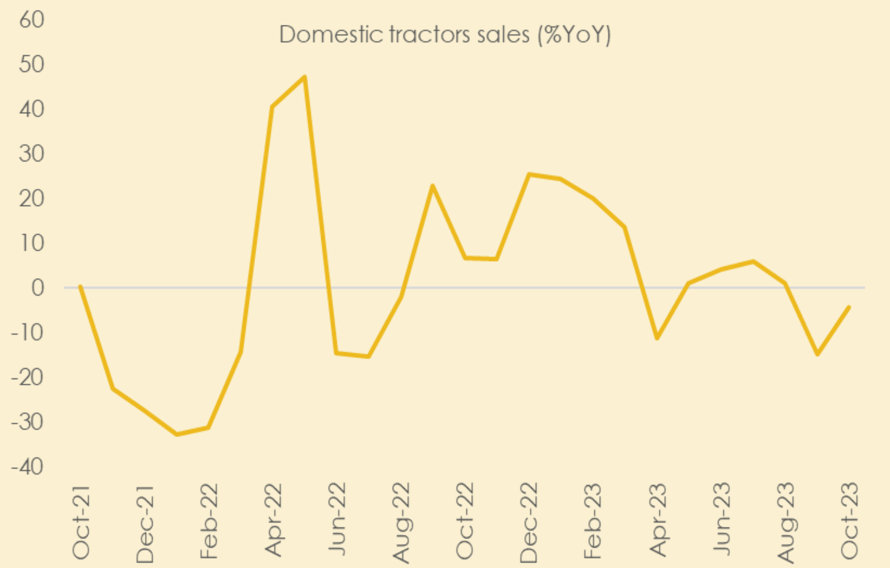
While downside risks will continue to linger be it on the food inflation side or on the global geo-political front in the near future, one thing that's is more likely than not is an end to the persistent rise in global interest rates that we have seen over the last 18-20 months. Core inflation has seen a softness in most economies and demand signals have got gradually weaker. Most of the major central banks in the world including the Fed and RBI are likely to be in a pause mode for the next six months to assess the growth-inflation dynamics closely before deciding on a pivot. This will help to normalize the capital flows to India, help the INR regain some strength and moderate the bond market yields. Hopefully, that will set the right platform for a favourable funding environment in the next fiscal. Cheers,

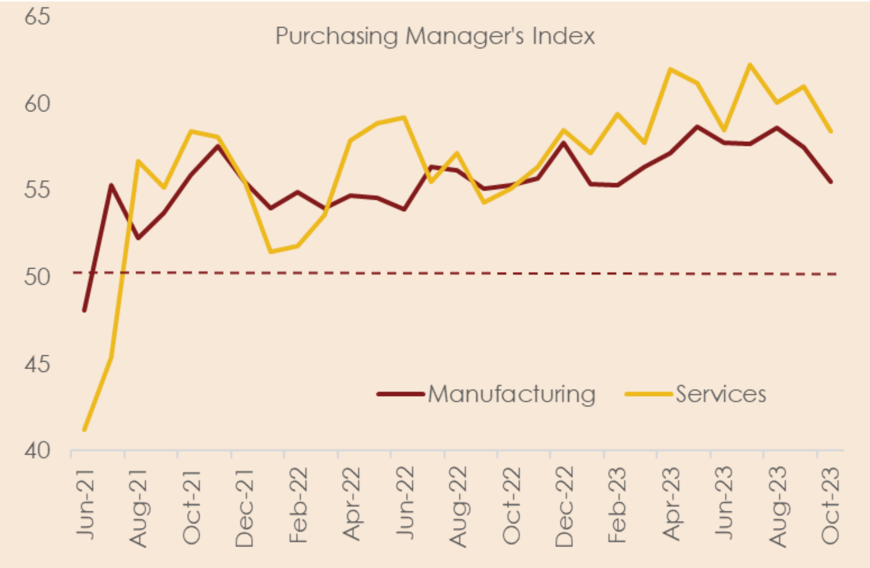
- Suman Chowdhury, Chief Economist and Head – Research

Rural demand slowdown in Q2 FY24

Rural demand witnessed some slowdown in Q2 FY24, amidst an adverse macroeconomic backdrop of elevated retail inflation and uneven/shortfall in monsoon. Key FMCG players with rural focus have seen a slowdown in volume growth in Q2 FY 24.

The downside in rural demand was more than offset by resilience in urban demand in Q2 FY24, as underscored by plethora of high frequency indicators such as PMI, air passenger traffic, record high PV sales, among others.

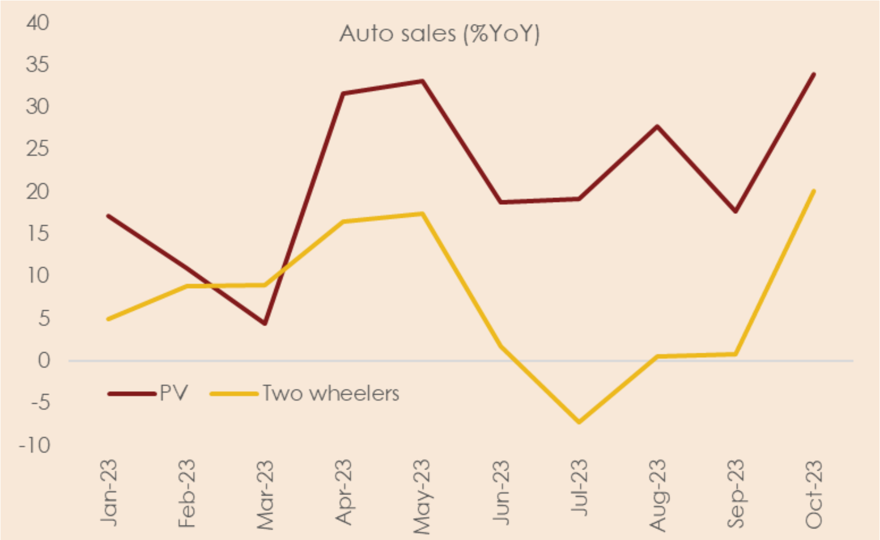




Festive season buoys Q3 FY24 consumption

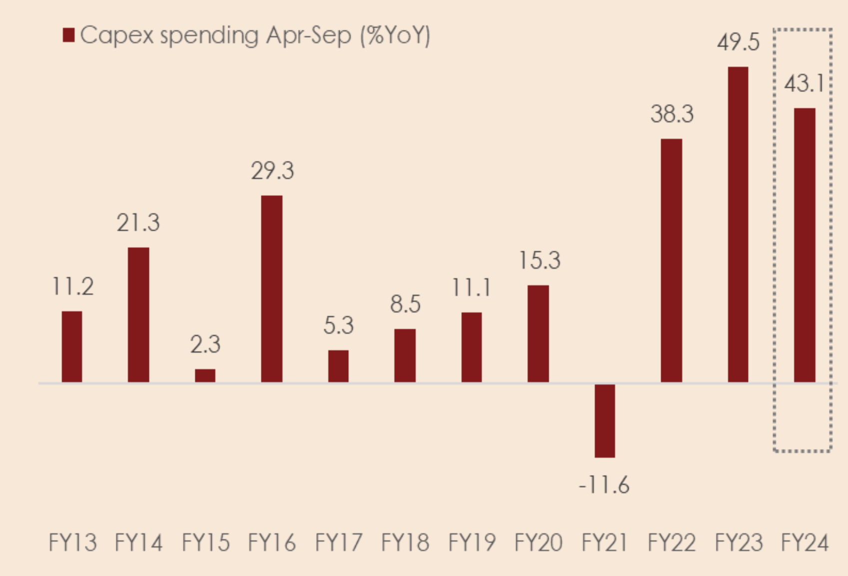
As per anecdotal evidence, festive season has augured well for consumption boost in sectors such as auto, electronics, appliances, real estate, among others. ICC Cricket World Cup season coinciding with festive season, likely further boosted consumption

With the onset of wedding and festive season, gems and jewellery imports soared to the second highest monthly pace of USD 10.5 bn in Oct-23, underscoring the resilience in demand for the sector



Fiscal support to growth continues

Government capex on a FYTD basis has expanded at a strong pace of 43.1%YoY on a sizeable base from last year. While adherence to BE would mean a lower annualised pace of capex growth in H2 FY24 vs. H1, overall, we expect fiscal support to growth to remain intact in the run up to the national elections



Some of the fiscal measures that have been announced in recent weeks

Extension of free foodgrains scheme for next 5 years

- This could keep the food subsidy elevated

Reduction in LPG cylinder price by Rs 200

- Another Rs 100 reduction for Ujjwala beneficiaries

Hike in DA for government employees

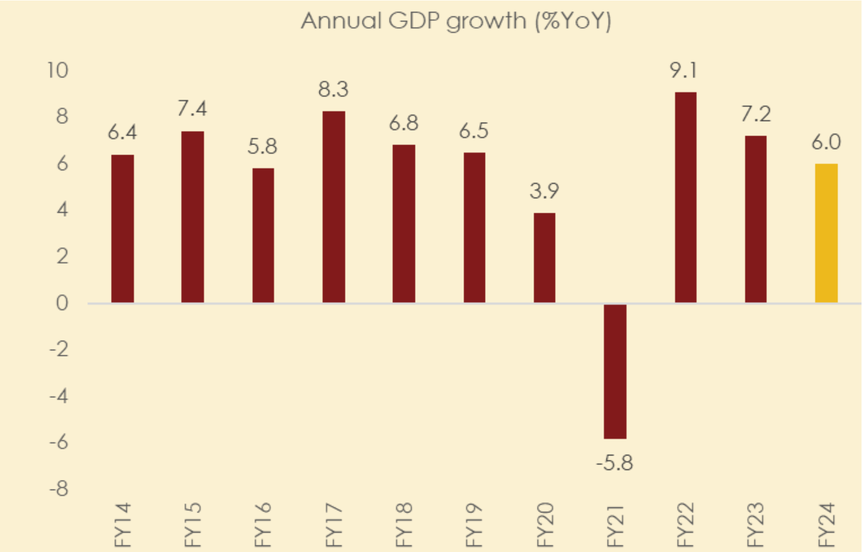
- By 4.0% for central govt. employees, also announced by select states including TN and UP

Wheat MSP hiked by 7.0%

- The highest increment in over a decade

But GDP growth to moderate in H2 FY24

On net basis, we continue to expect FY24 GDP growth to moderate to 6.0-6.2% from 7.2% in FY23.



There are four key factors that would weigh upon H2 FY24 GDP :

- Adverse spillover from the anticipated (albeit somewhat delayed) global slowdown.
- Dilution of pent-up demand (esp. in services)
- Lagged impact of domestic monetary tightening and of the latest RBI measures on uncollateralised retail lending will restrain leveraged urban demand
- Likelihood of some downside to Kharif crop yields post monsoon deficiency in 2023
- Elevated crude oil prices above USD 90 pb over H2 FY24, can shave off 10-15 bps from GDP growth

-1.6%

- Average annual change in Agriculture GVA during El Nino years*

315 bps

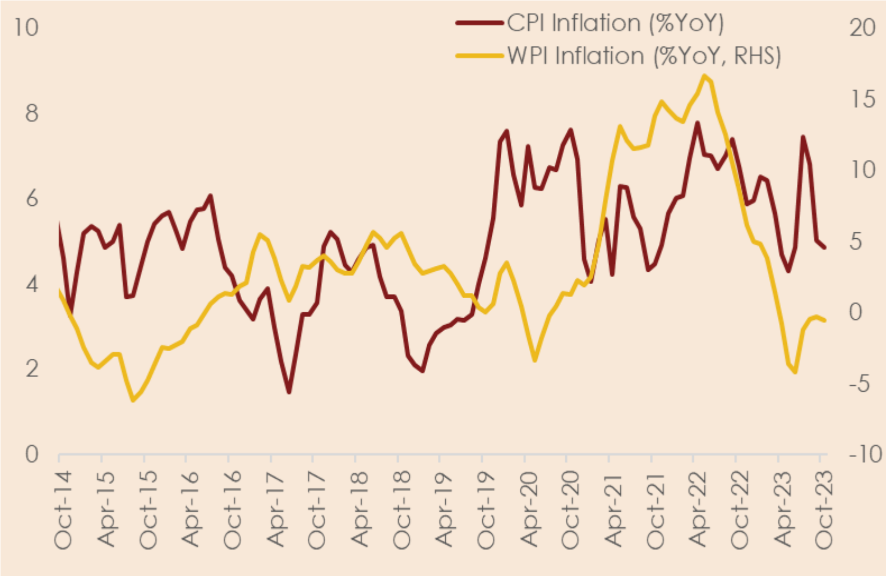
- Effective rate hike done by the RBI between Apr-22 and Feb-22

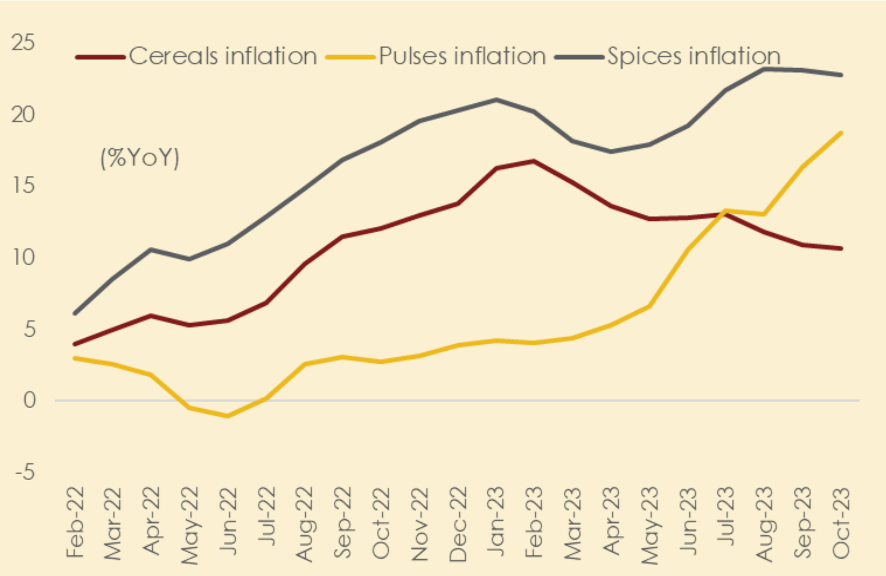
* Time period: 1995-2021

Oct-23 CPI slips below 5.0%

India's CPI inflation moderated further in Oct-23 to 4.87%YoY from 5.02% in Sep-23, though the pull back was marginally lower than consensus expectations pegged at 4.7-4.8%.

The moderation in headline as well as food inflation notwithstanding, some categories of food such as cereals, pulses and spices continued to see elevated price pressures in Oct-23.



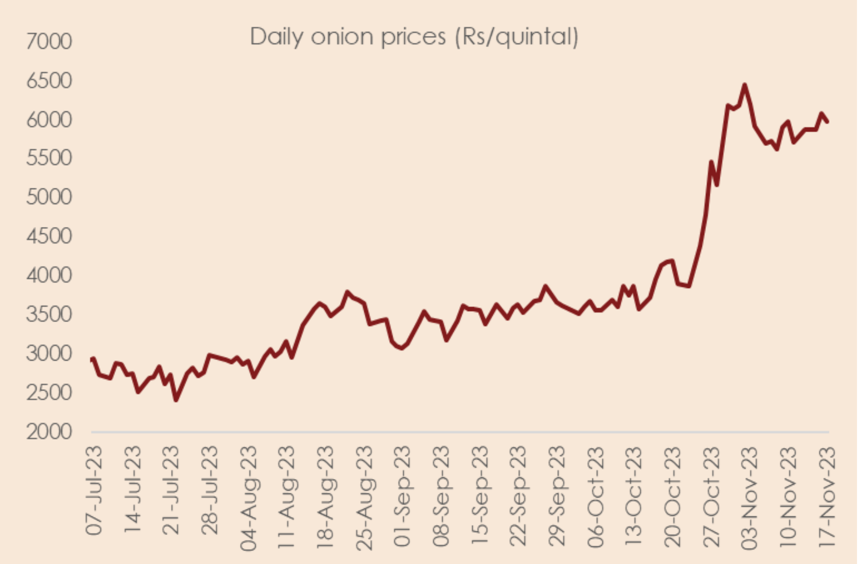


Food prices remain on watch

The outlook on food inflation remains somewhat clouded amidst the expected downside to Kharif yields, especially pulses and oilseeds as per Government's first advance estimates and the risks to the Rabi crop due to uncertain weather conditions.

Onion prices have seen a sizeable run-up in Nov-23. As per mandi data, onion prices have jumped up by ~42% sequentially in Nov-23, so far amidst supply shortages. This could add an upside to Nov-23 CPI inflation, though we expect prices to ease by Dec-23.

Crop	% Change vs. 2022	
	Area Sown	1st advance estimate : output
Rice	1.9	1.3
Maize	3.8	-2.7
Tur	-4.9	-12.1
Moong	-6.0	-19.7
Urad	-1.3	-18.2
Oilseeds	-1.6	-8.6
Groundnut	-3.6	-6.5
Soybean	0.7	-10.6
Sugarcane	7.6	-6.5



All eyes on Rabi season

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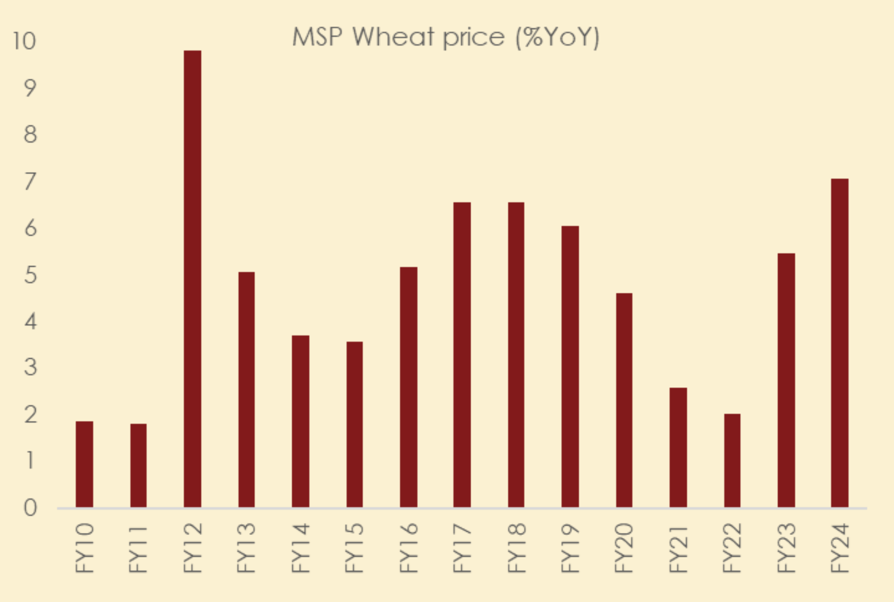
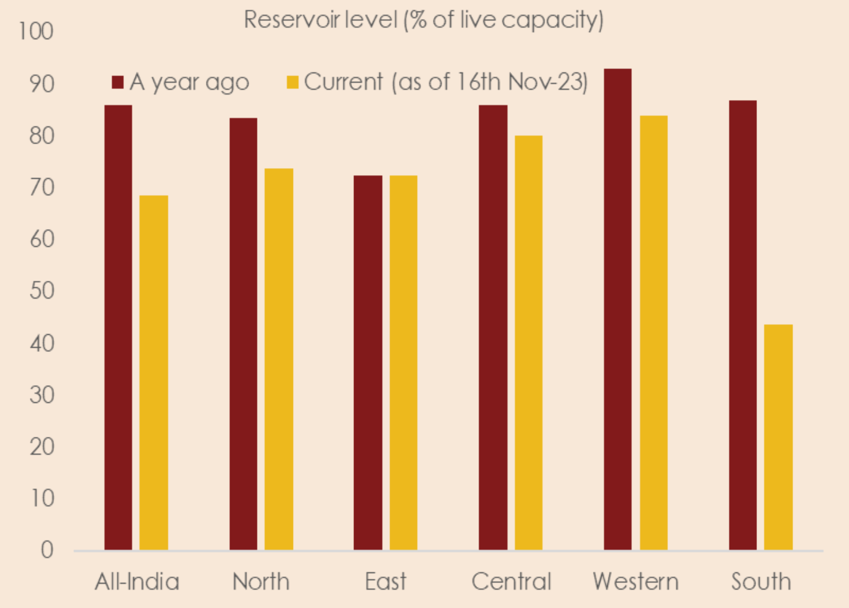
In a bid to boost Rabi sowing of wheat, Government has announced a 7.0% hike to MSP for the foodgrain this year – the sharpest increment in over a decade. Higher production will allow Government to push up its wheat procurement next year in a bid to replenish depleting wheat stocks

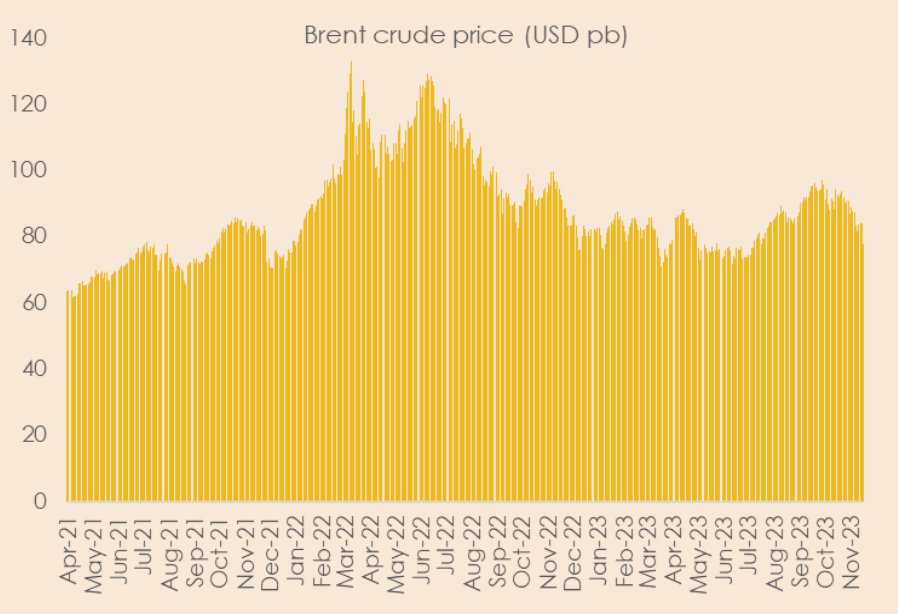
While rabi sowing has begun on a healthy note, a good production will be critical to counter the kharif downside. Having said so, reservoir levels remain unsupportive post SW monsoon deficiency and a poor start to NE monsoon in Oct-23.





Crude volatile, risks to inflation stacked on upside

Crude prices have behaved erratically over the last few weeks, to trade in a broad range of USD 77-97 pb; while extension of OPEC's production cuts and resilience in US economy offered support along with geopolitics, but elevated inventories as well concerns over Chinese demand have weighed lately on prices.

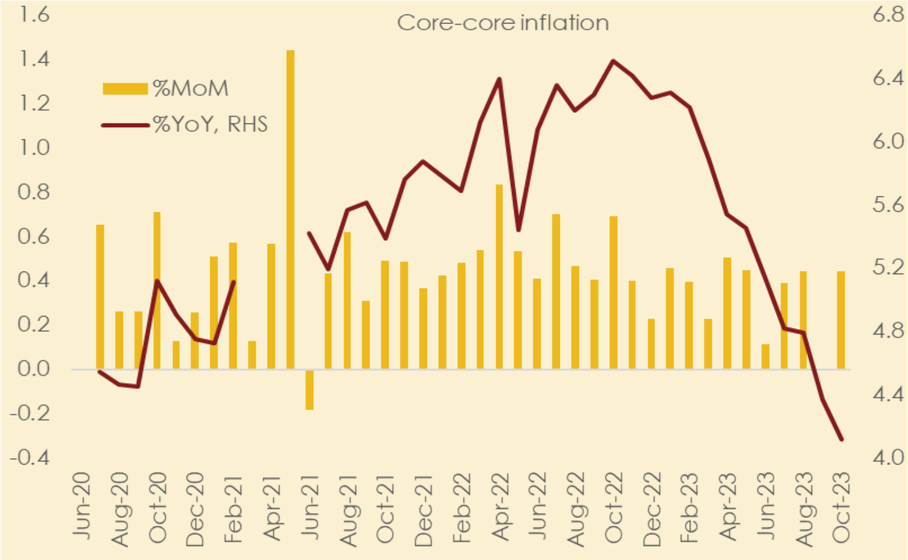


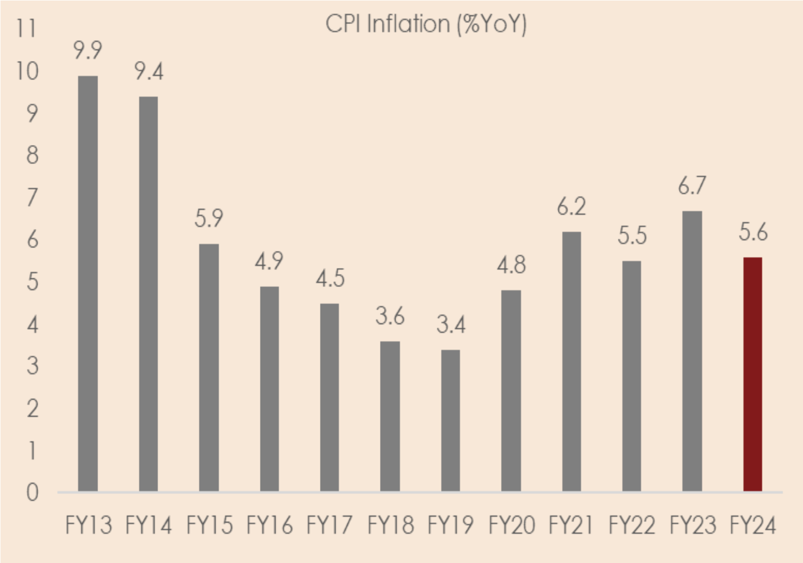
Upside risks to watch on inflation
Impact of Israel-Hamas tensions, OPEC+ decision to cut production on crude oil prices
Impact of El Nino on global food production in the coming months. Weather agencies expect El Nino to remain strong at least through spring of 2024
Durability of price pressures seen in cereals, pulses and spices, despite administrative measures
Impact of deficient monsoon on Kharif crop production

CPI inflation may average at 5.6% in FY24

Core inflation at 4.1%YoY in Oct-23 marks the lowest level of in the post pandemic phase, well below its LPA of 5.2%

We hold on to our FY24 average CPI inflation estimate of 5.6%, given the downside risks.





Snapshot of Apr-Sep FY24 fiscal performance

The FYTD (Apr-Sep) accretion to fiscal deficit stood at 39.3% of budget estimates (BE) for FY24, higher than 35.8% seen in the corresponding period in FY23. While both receipts and expenses have seen a quick pace of accrual/disbursal in FYTD24 vs. FYTD23, relatively faster pace of expenditure this year has driven the fiscal deficit moderately higher on FYTD basis.

Key Fiscal Variables (Cumulative position, Apr-Sep)

	% of FY Actual/Target		%YoY	
	FY23	FY24	FY23	FY24
Revenue Receipts	49.1	53.1	8.2	19.5
Net Tax	48.2	49.8	9.9	14.7
Non-Tax	55.1	78.5	-1.7	50.2
Non-Debt Capital Receipts	47.4	24.0	88.7	-41.0
Total Receipts	**49.0**	**52.2**	**9.5**	**17.7**
Revenue Expenditure	42.9	46.5	6.0	10.0
of which, Interest Payments	47.0	44.8	19.6	10.9
of which, Major Subsidies	38.1	55.1	9.9	3.8
Capital Expenditure	46.6	49.0	49.5	43.1
Total Expenditure	**43.5**	**47.1**	**12.2**	**16.2**
Fiscal Deficit	**35.8**	**39.3**	-	-

Revenues: Comfort remains

Gross tax collection momentum remains robust albeit marginally lower than in FY23. As of Sep, barring excise and GST, all other categories of taxes have maintained healthy momentum (GST could potentially find support in the upcoming festive season).

Meanwhile, non-tax revenue (NTR) has not just gained from the higher than budgeted surplus transfer from the RBI but continues to find support from strong dividend payout from PSUs and spectrum income. However, divestment activity is slow (Rs 69 bn until Sep-23 vs. Rs 246 bn until Sep-22) and likely to face a shortfall.

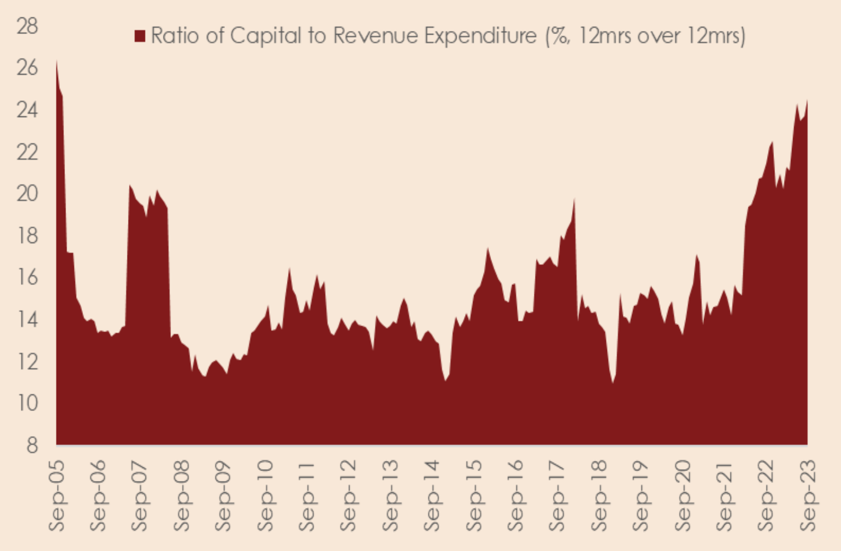
Growth in key tax categories	Apr-Sep FY23 (% YoY)	Apr-Sep FY24 (% YoY)	FY24 BE (% change*)
Gross Tax	**17.6**	**16.3**	**10.1**
Corporate Tax	21.6	**20.2**	11.7
Income Tax	25.7	**31.1**	11.4
Customs	-6.9	**23.1**	9.2
Excise	-18.5	**-10.8**	6.3
GST	33.4	**8.7**	12.1

* Implied growth over FY23 actuals

FYTD performance of non-tax revenue collection	
Total NTR: Apr-Sep FY23 (Rs bn)	1576
Total NTR: Apr-Sep FY24 (Rs bn)	2368
Total NTR: Apr-Sep (% of FY23)	55.1
Total NTR: Apr-Sep (% of FY24)	78.5
Growth in Total NTR: Apr-Sep FY23 over Apr-Sep FY22 (% YoY)	-1.7
Growth in Total NTR: Apr-Sep FY24 over Apr-Sep FY23 (% YoY)	78.5

Focus on superior expenditure quality; Slight slippage risks, a monitorable

Capex continues to receive priority over revex; upcoming elections might be driving the front-loaded disbursals



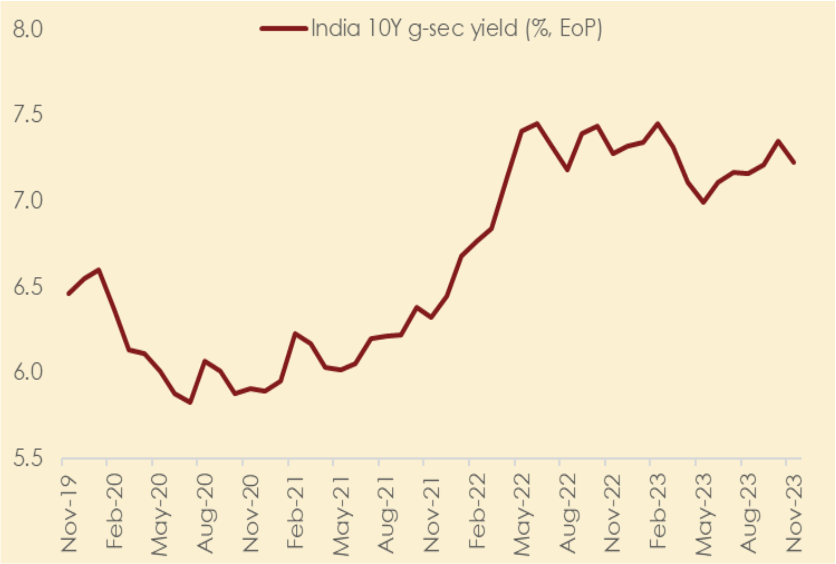
Upcoming elections could weigh upon government's appetite for disinvestments, even as developmental expenditure finds a boost. This would require reallocation of spending commitments.

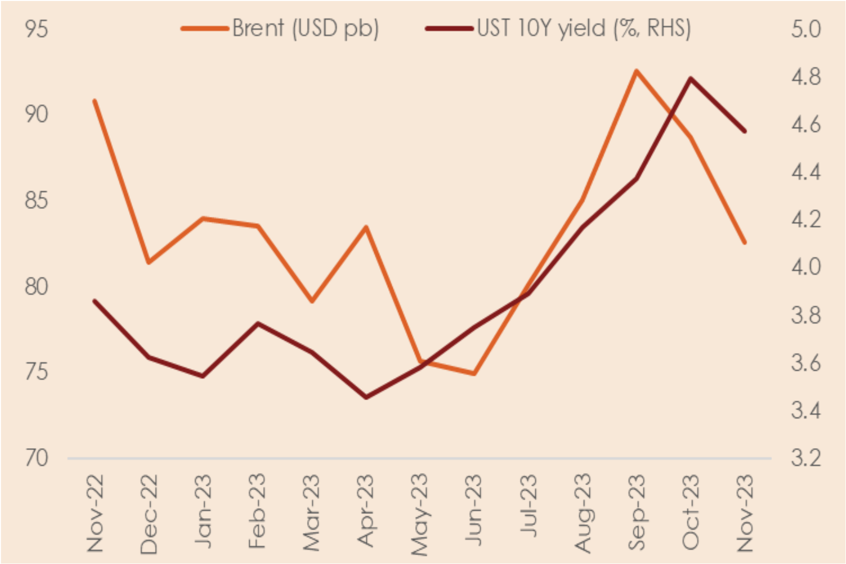
We continue to expect FY24 fiscal deficit target of 5.9% of GDP to be largely met (with expenditure compression in Q4 and some cushion from non-tax revenues) but there may be some slight slippages of 10-20 bps.

Slight moderation in g-sec yields…

From its recent monthly high of 7.35% in Oct-23, India's 10Y g-sec yield has moderated MoM, and is currently trading around 7.22% levels.

Over the last few weeks, there has been a respite from both crude oil prices as well as US rates.

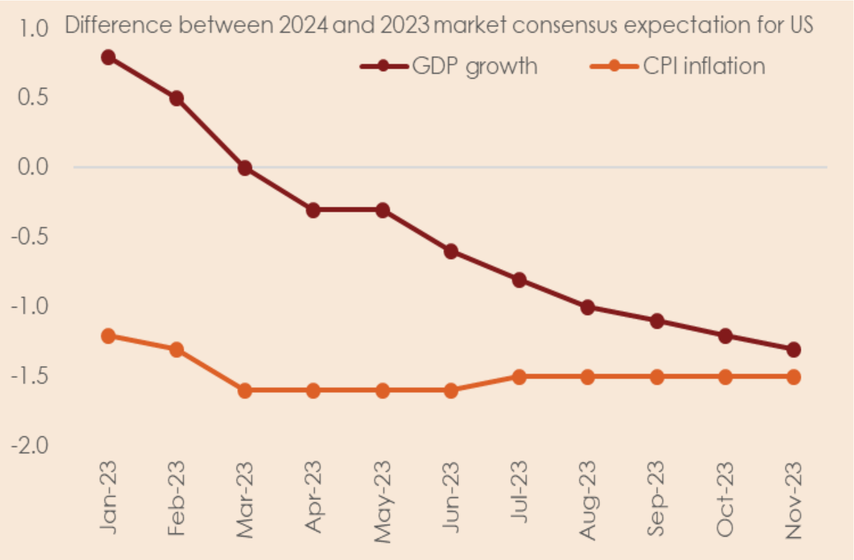


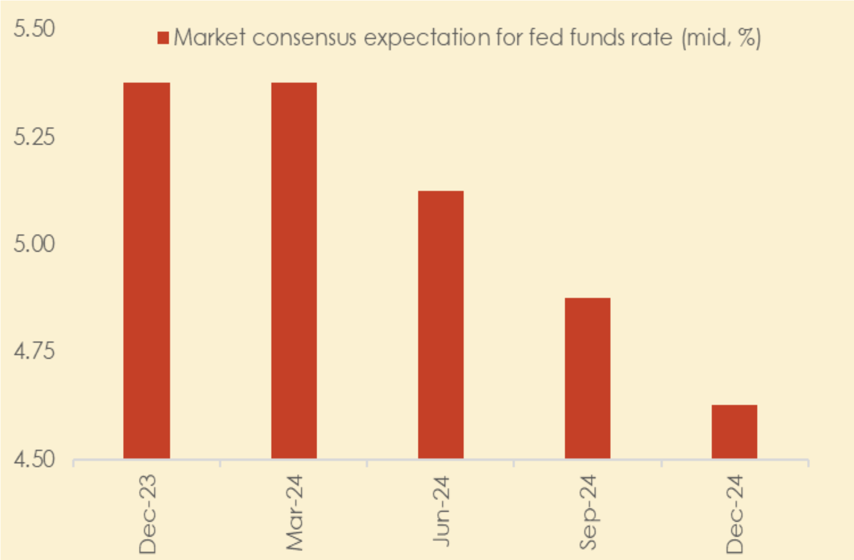


…with global factors turning favorable on the margin

Although US economic resilience is now completely priced in for 2023, market participants expect a significant slowdown in 2024, even though expectations with respect to inflation have remained relatively stable.

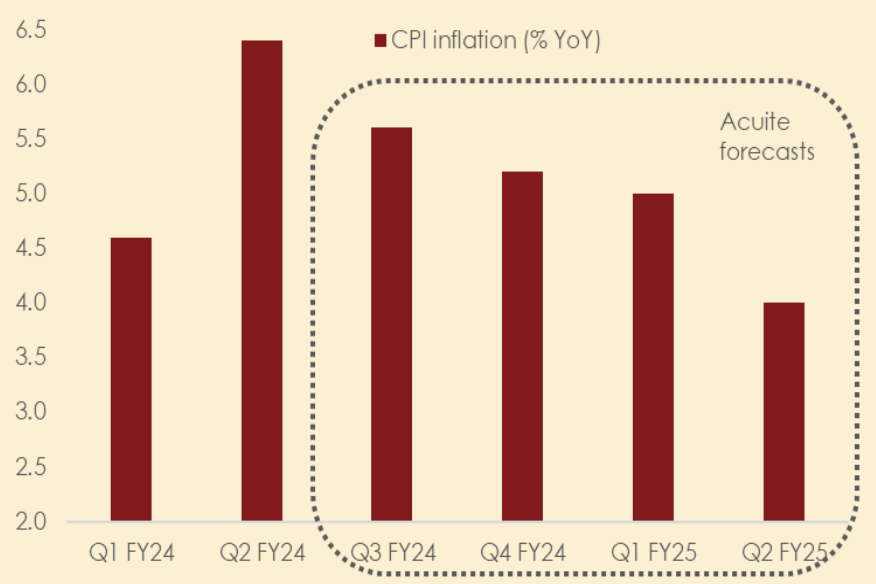
Currently, market participants expect 75 bps cumulative rate cut from the US Fed, which is broadly in line with the latest FOMC dot plot projection.



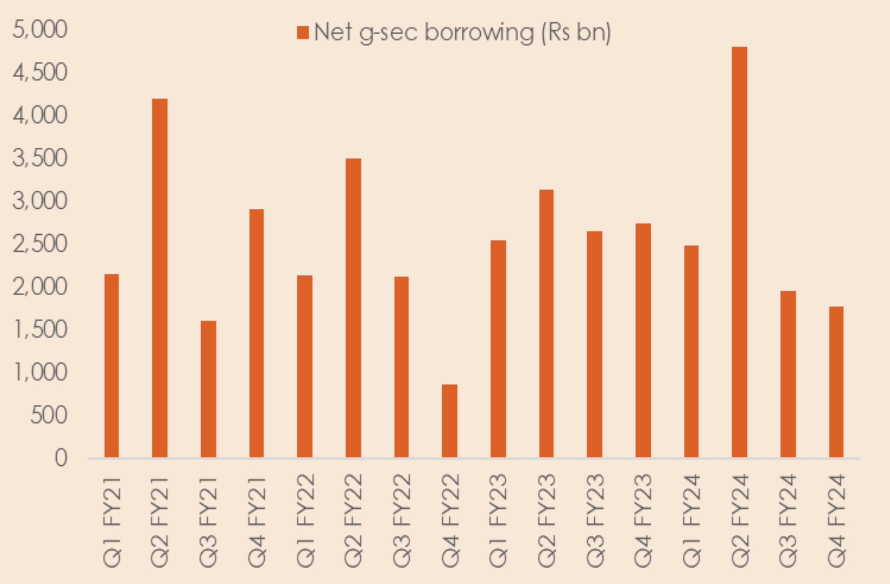


Domestic factors remains supportive for now…

After peaking at 6.4% in Q2 FY24, CPI inflation is projected to moderate to 5.2% in Q4 FY24, and further towards 4.0% in Q2 FY25.



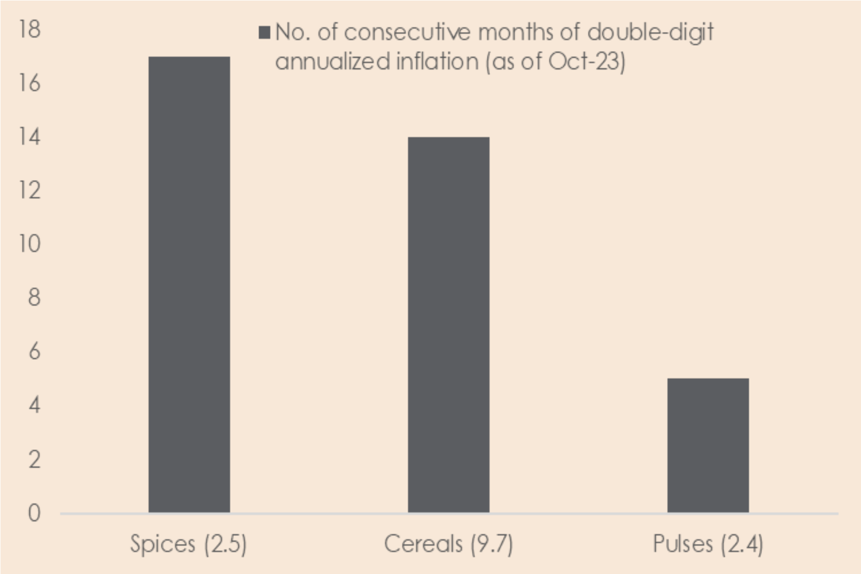
Although net g-sec borrowing is at its post Covid high in Q2 FY24, it is scheduled to decline considerably in H2 FY24.



…however, MPC needs to maintain caution

Below normal and erratic monsoon has kept key staple (within staples) at elevated levels. This can provide downward rigidity to food inflation in coming months despite favorable seasonality.

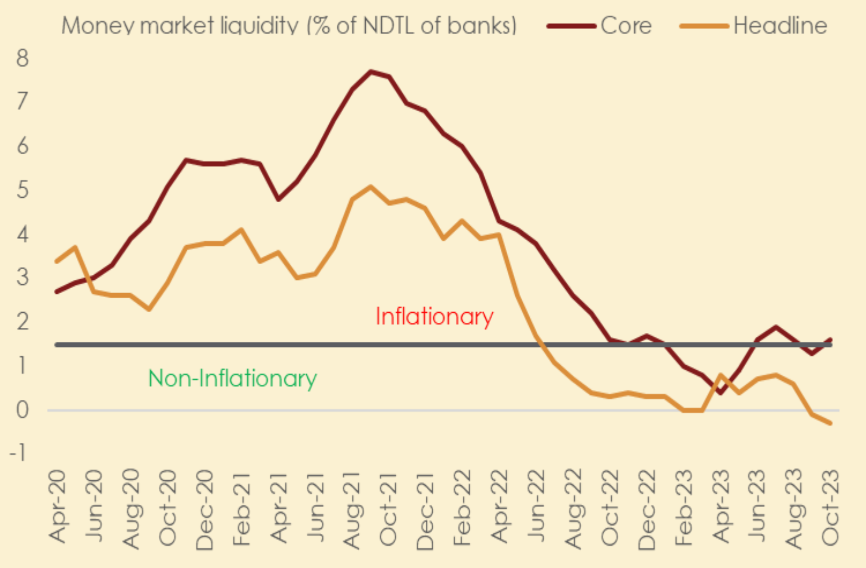
Long term inflation expectation of professional forecasters is yet to find its anchor despite record pace of monetary tightening by the MPC.



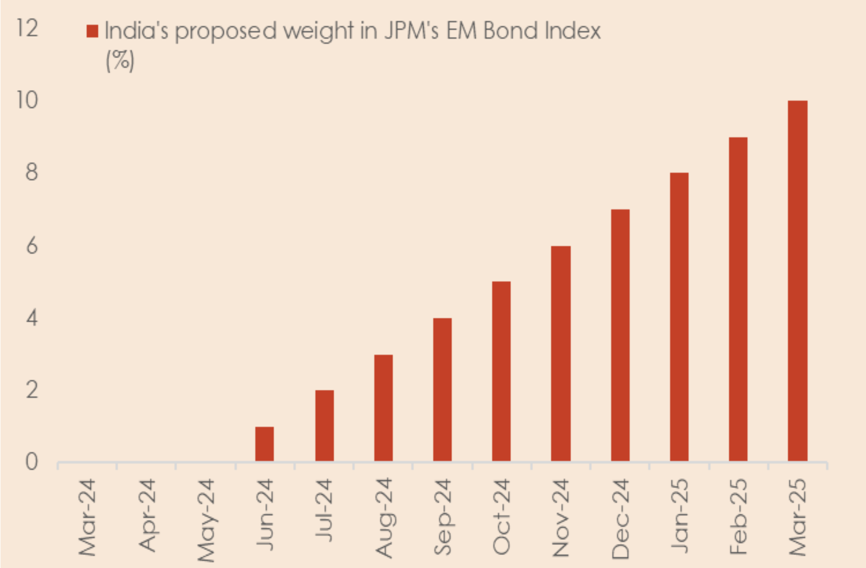
Note: Figures in parenthesis indicates the weight in CPI

Moderately benign outlook on rates

We expect RBI to moderate core liquidity surplus from Rs 2.9 tn as of end Q2 FY24 towards Rs 1.7 tn by end Q4 FY24 to boost policy transmission.



With India's inclusion in JP Morgan's EM Bond Index, there is a possibility of USD 20 bn passive inflows by Mar-25.

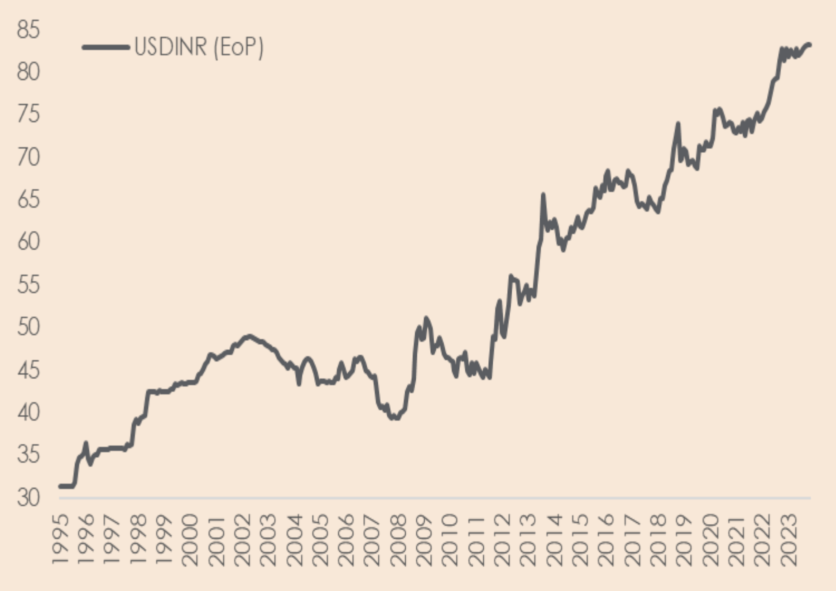


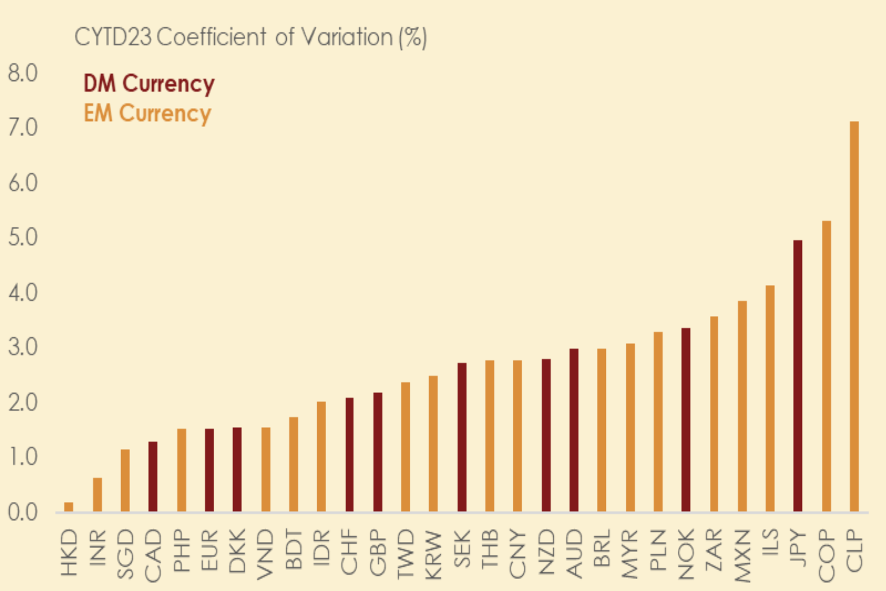
With domestic inflation projected to moderate and index inclusion becoming a reality we **expect 10Y g-sec yield to moderate towards 7.00% by Mar-24**. However, El Nino and geopolitical factors could potentially provide an upside risk.

INR touched a new record low in Nov-23

USDINR is currently trading close to 83.3-83.4 levels, the weakest in history.

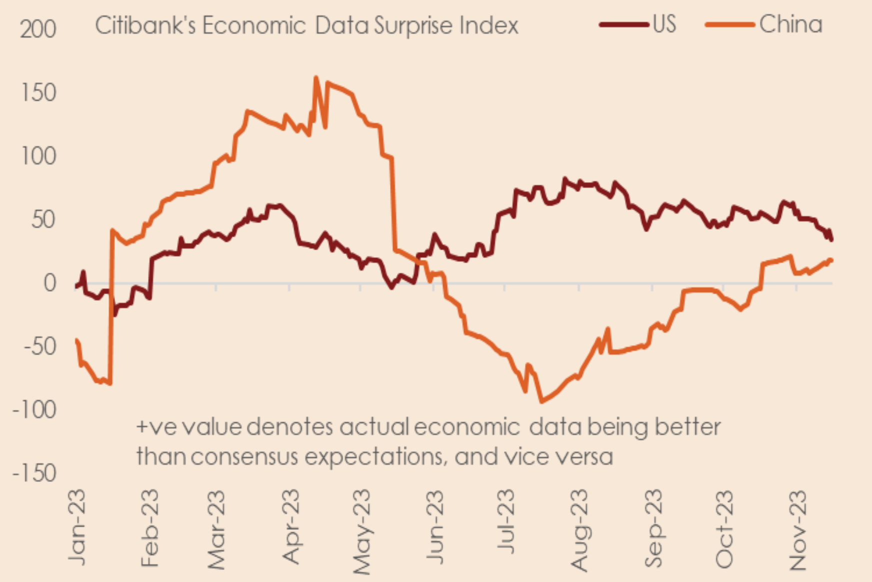
However, record low weakness in INR has not resulted in excessive volatility; in fact, INR has been one among the least volatile major currency.



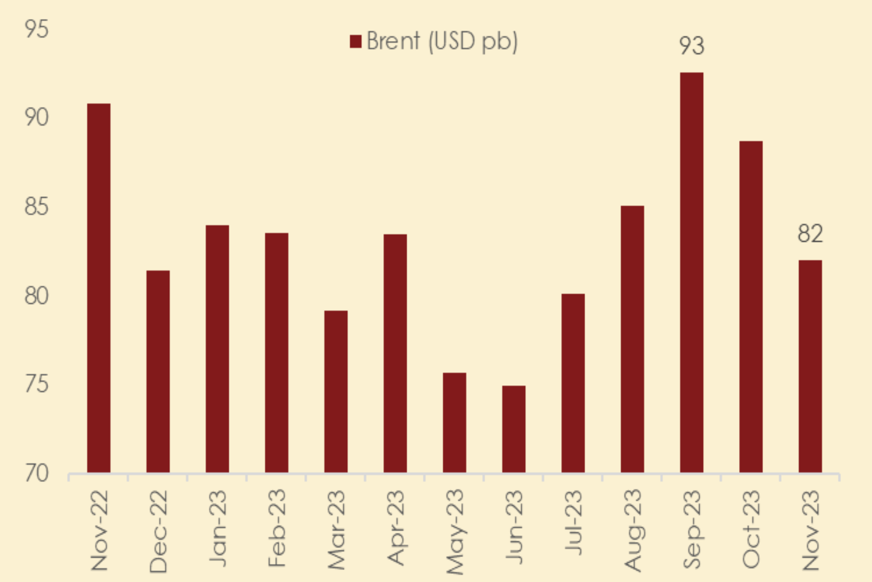


Adversity of global factors has reduced

Over last 1-month, the momentum of positive data surprises in US has waned and in case of China, string of negative data surprises have reversed. Both these developments are supportive of EM currencies.



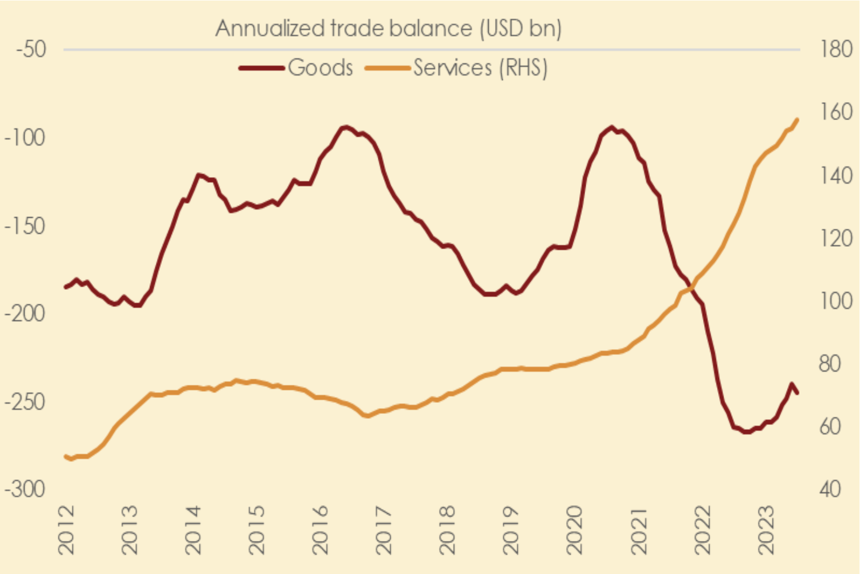
International commodity prices have softened in last 1-month. Brent crude has fallen from its recent high of USD 93 pb levels in Sep-23 to USD 80 pb levels in Nov-23 so far (despite the ongoing Israel-Hamas war).

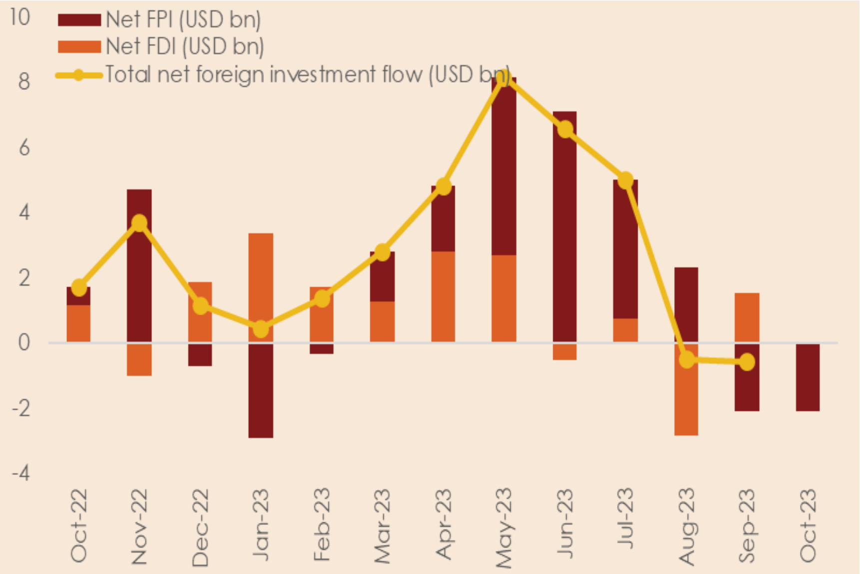


But trade balance and BoP position weaker

Although merchandise and services trade balance provided comfort in H1 FY24, we could see some deterioration in H2 on account of jump in commodity prices (on average), global slowdown, and spike in geopolitical risk.

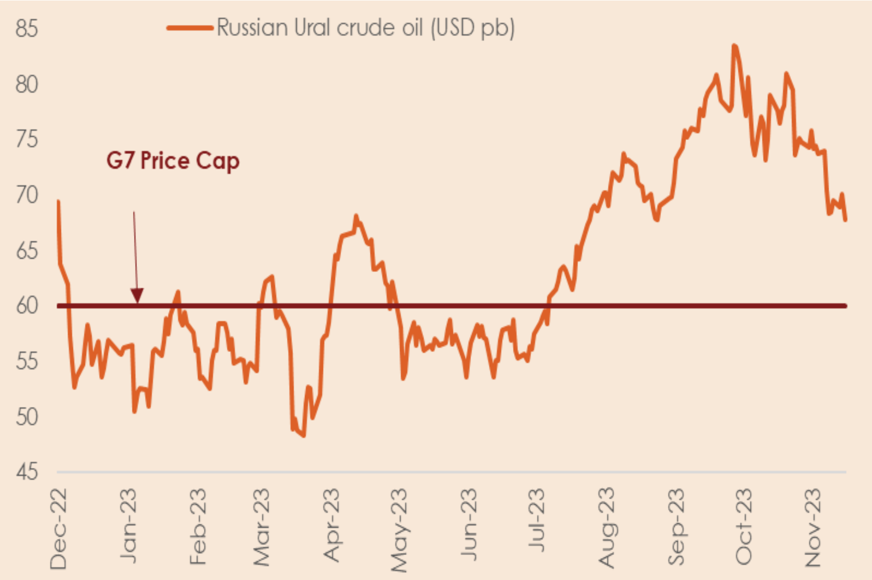
Narrative of 'higher for longer' rates in the US and spike in geopolitical risk premium (with adverse impact on energy prices) has weighed upon direct investment and portfolio investment flows.



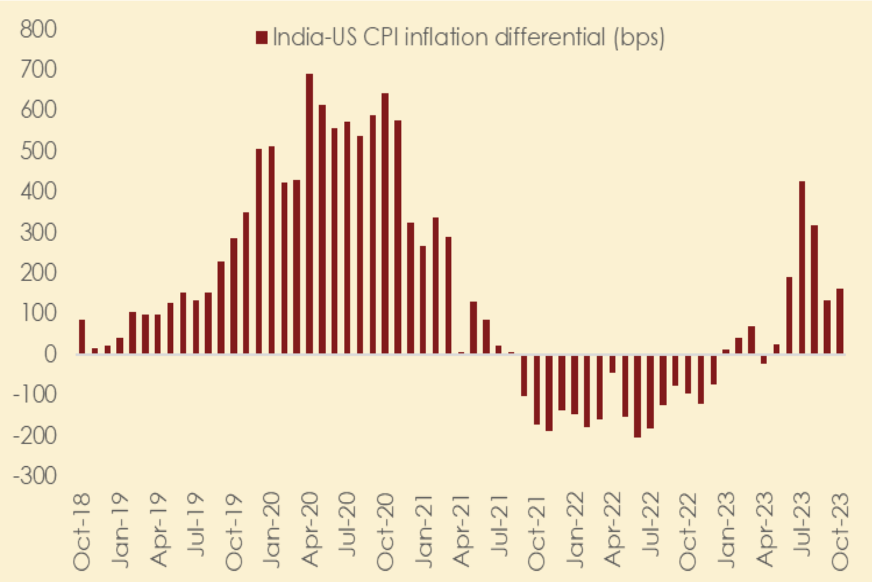


Swing factors no longer in favor

Notwithstanding the recent drop in crude oil prices, Russian Urals continue to stay above the G7 implied price cap.

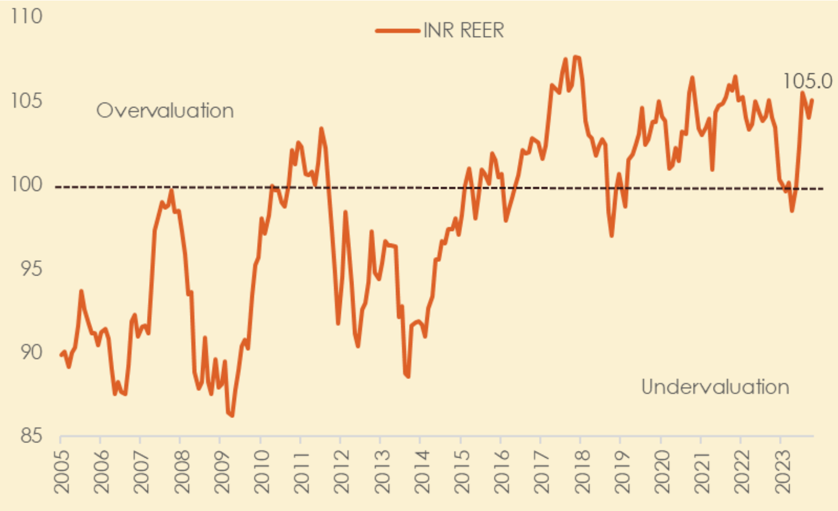


With inflation differential with the US remaining against India in recent months, INR could continue to face some pressure in the near-term.

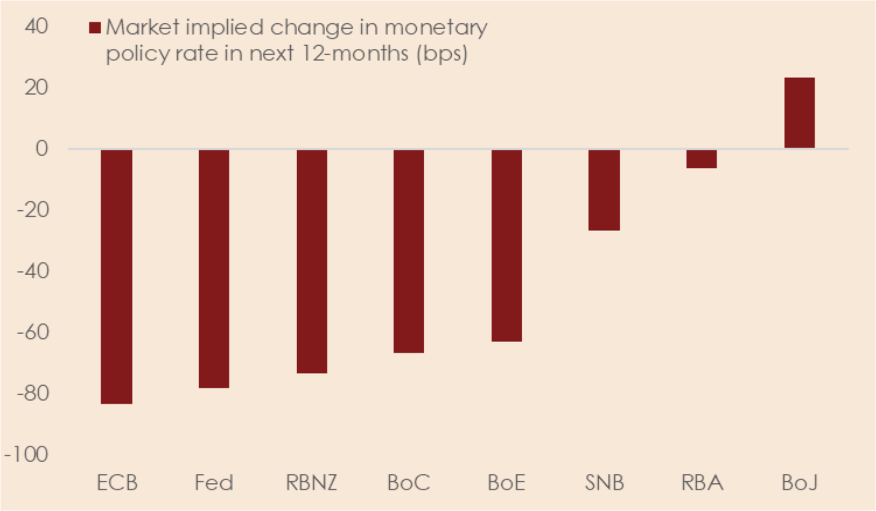


Rupee – short term pressures, regain strength next year

Since Jun-23, while INR has been stable, the EM currency pool has weakened vs. the USD, thereby resulting in increase in INR's overvaluation. This could make RBI somewhat tolerant of near-term adjustment.



Markets now expect Fed and the ECB to deliver identical quantum of rate cuts in next 1Y.

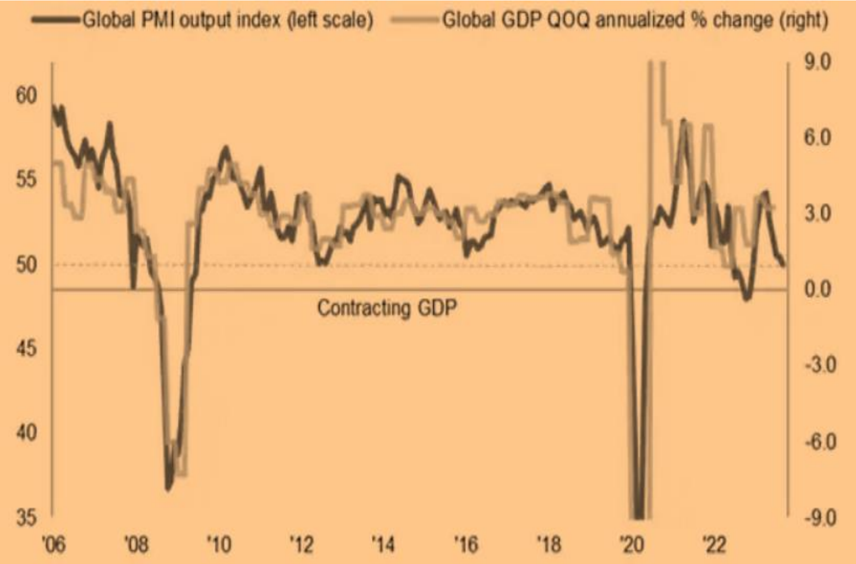


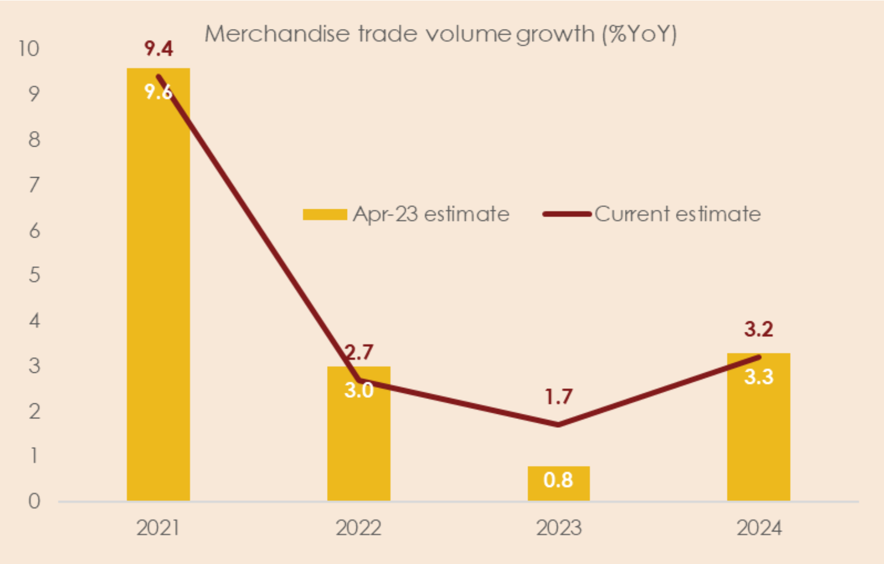
A BoP surplus and a backloaded dollar negative backdrop would support INR in the medium term. However, near-term pressure points in the form of higher trade deficit and lower capital inflow could weigh on INR. As such, we expect INR to weaken towards 84 levels by Dec-23. We maintain our moderately constructive view on INR, with a move towards 82 by Mar-24. Uncertainty on Fed rate trajectory and geopolitical factors could provide some risk to our forecasts.

Global economic activity remains largely weak

Global economic expansion stalled at the start of the fourth quarter, as new orders recorded a second consecutive, and sharper, fall in Oct-23. The JP Morgan Global PMI Composite Output Index fell to the neutral mark of 50.0 in October, down from 50.5 in Sep-23.

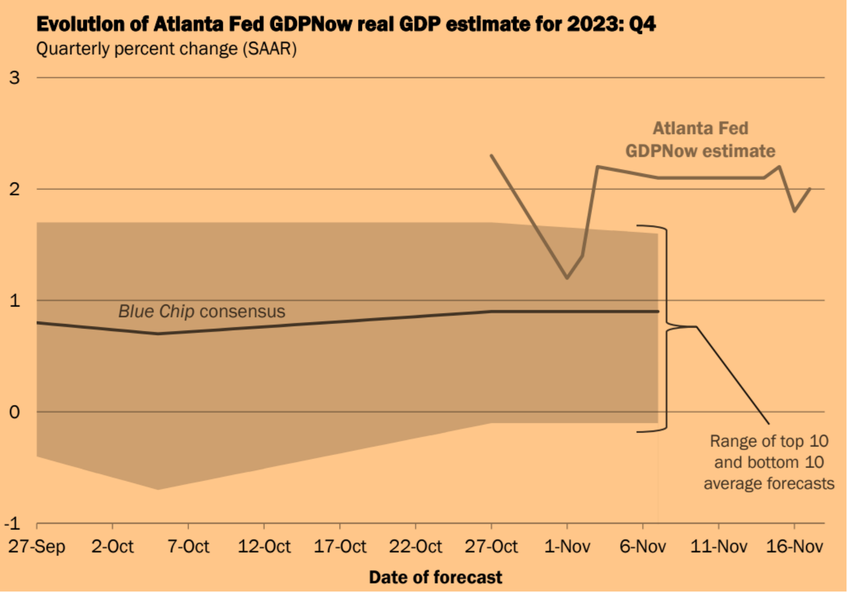
As per WTO, the volume of world merchandise trade is now expected to grow by 0.8% this year, less than half the 1.7% increase forecasted in Apr-23. The 3.2% growth projected for 2024 remains nearly unchanged from the previous estimate.



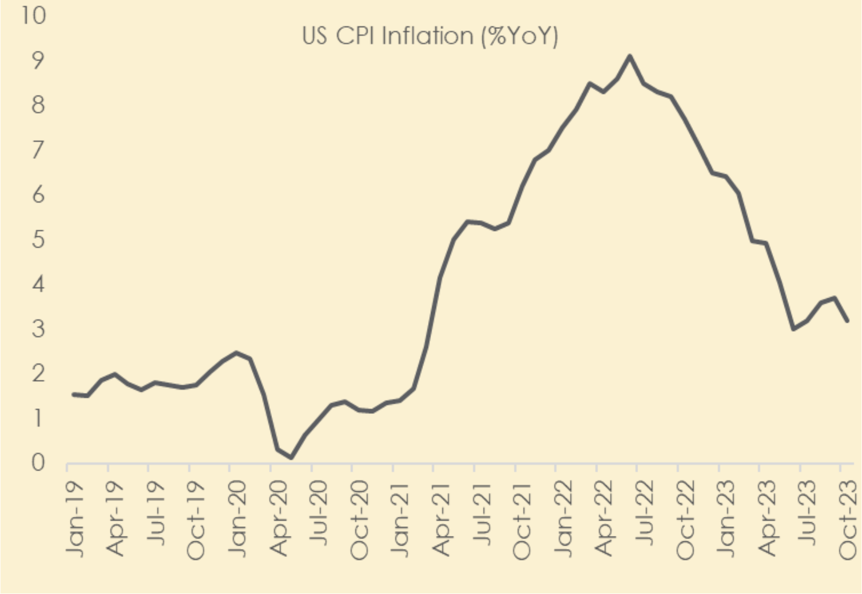


US growth and inflation both on a softening path

As per Atlanta Fed's GDP Nowcast, US economy's real GDP growth (seasonally adjusted annual rate) in Q4-23 is currently tracking 2.0%, much lower than 4.9% clocked in Q3



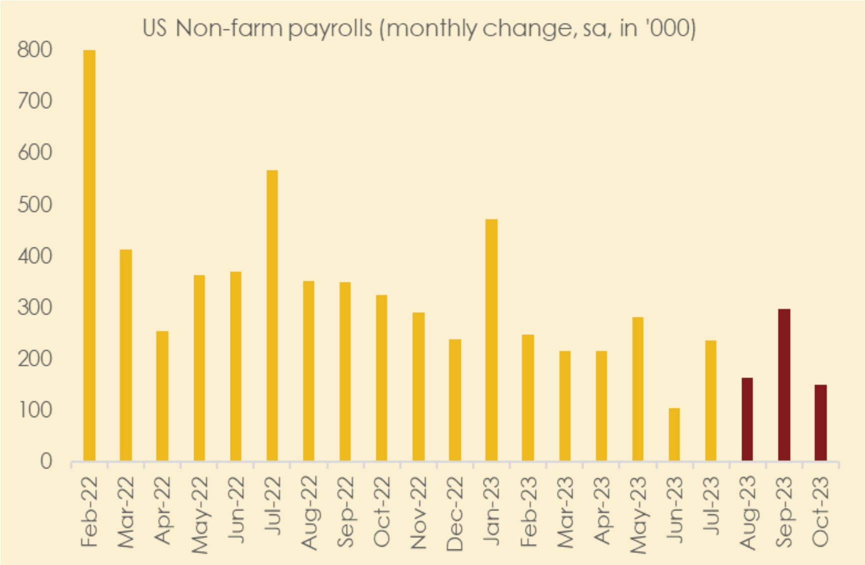
US CPI inflation eased to 3.2%YoY in Oct-23 from 3.7% in Sep-23, owing to a favorable base and the index remained unchanged sequentially

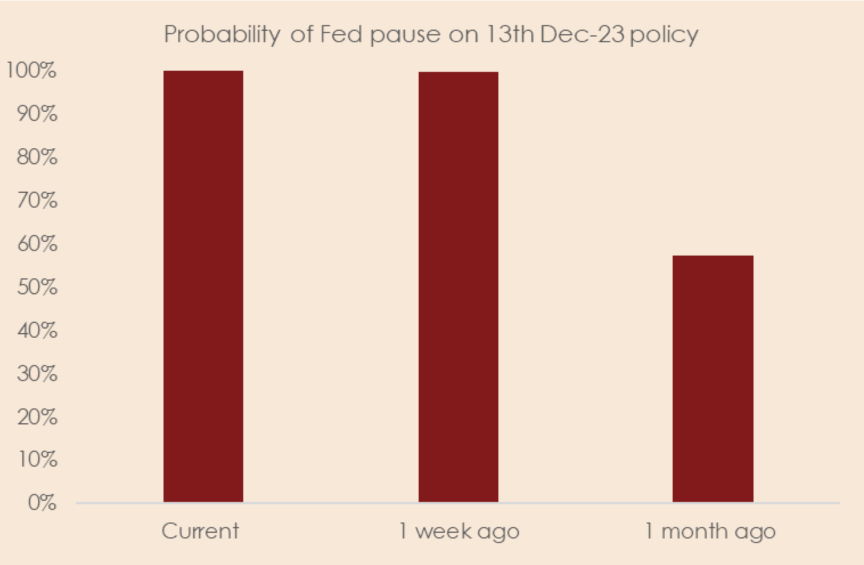


Fed done with rate hikes

US Non-farm payrolls slowed in October to 150k, while the unemployment rate ticked higher to 3.9%, in yet another sign that the US economy is now starting to slow

Market participants are now expecting Fed to pause in its Dec-23 policy, compared to a near 50% probability of a hike a month ago. The cool down in inflation has cemented the view of no further hikes with market pricing in interest rate cuts beginning May-24.





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