INDIA'S ECONOMY AT A GLANCE

SEPTEMBER 2019

National Australia Bank

CONTENTS

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KEY POINTS

India's economy needs a stimulatory kick start, with no guarantees of recovery

- India's economic growth continued to slow in the June quarter – down to 5.0% yoy (compared with a relatively weak 5.8% in Q1). This was the slowest rate of growth since March 2013, with weakness in both private consumption and investment persisting from the previous quarter. We have lowered our forecast for Indian growth, given the weaker than expected outcome in Q2, with growth at 5.7% in 2019, 6.8% in 2020 and 7.1% in 2021. Easing monetary policy is expected to support a modest recovery in the short term (led by investment), however downside risks (particularly around consumption) persist.

- A key uncertainty is the Government's commitment to its fiscal deficit target (3.3% of GDP) this financial year. Estimates from the Controller General of Accounts suggest that around 78% of this target was used in the first four months of the year (ending July). Despite a record transfer from the Reserve Bank of India – equivalent to around 0.9% of GDP – the Government will have to substantially curtail spending in coming months to meet this target – particularly following corporate tax cuts announced in September that could be around 0.7% of GDP (according to some estimates).

- Following a weak period at the start of 2019, India's industrial production recovered in the middle of the year – with growth stabilising in July at around 3.3% yoy (on a three month moving average basis). It is worth noting that this increase is well below the trend between Q4 2017 and Q4 2018. Conditions are mixed across the industrial sector, with automotive manufacturing particularly struggling.

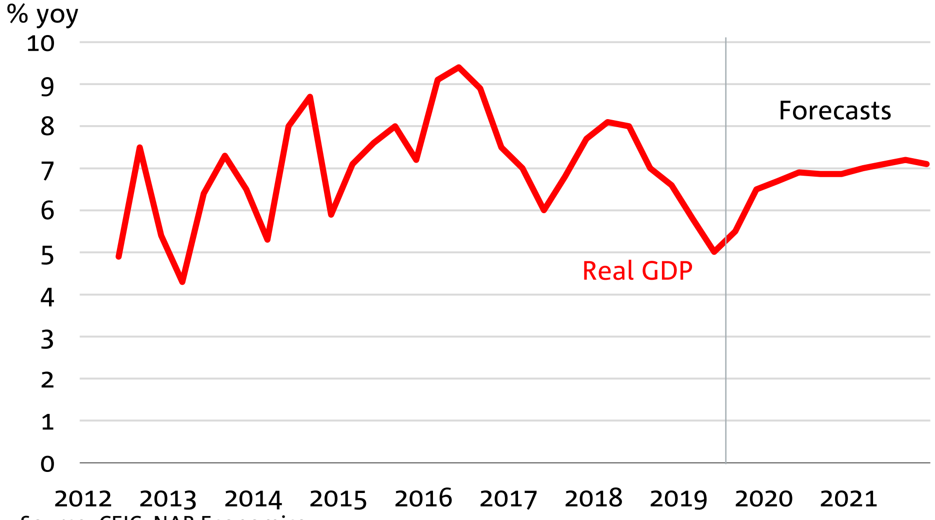
- The Reserve Bank of India has continued to ease monetary policy, cutting the Repurchase Rate by 35bps in June to a 9 year low of 5.4%. The 35bps cut was larger than expected and was the fourth straight rate cut in 2019. At the time of writing, markets have priced in cuts at the October 2019, December 2019 and February 2020 meetings, totalling around 50 basis points. Such moves would bring rates close to the lows implemented following the GFC.

- Access to credit remains an issue for many borrowers. The collapse of a high profile non-bank lender in late 2018 has led to a liquidity crisis in the shadow banking sector – with banks and other funding sources pulling back as risk concerns became elevated. So far there is little sign of improvement, largely cutting off finance to portions of the economy.

GROSS DOMESTIC PRODUCT

INDIA'S ECONOMIC GROWTH SLOWED FURTHER IN Q2

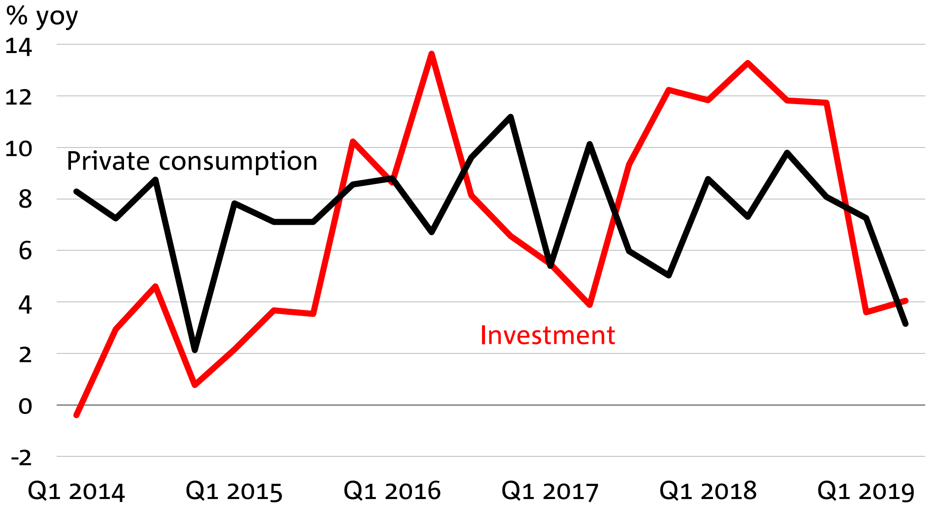
Slowest rate of growth in 5 years



Source: CEIC, NAB Economics

ECONOMIC GROWTH BY CATEGORY

Key expenditure components have grown more slowly



Source: Refinitiv, NAB Economics

- India's economic growth continued to slow in the June quarter – down to 5.0% yoy (compared with a relatively weak 5.8% in Q1). This was the slowest rate of growth since March 2013, with weakness in both private consumption and investment persisting from the previous quarter.
- Growth in private consumption plunged in Q2 – increasing by just 3.1% yoy, compared with 7.2% in the March quarter. Key indicators – such as auto sales – have been particularly weak, while unofficial measures of unemployment have been trending higher.
- Political uncertainty ahead of the General Election (held between mid-April and mid-May) had been blamed for the weakness in investment in Q1 and there was little improvement in Q2 (investment up by 4.0% yoy from 3.6% previously). This was despite a strengthening in opinion polls for the ruling BJP-led alliance from January through the election – which was won with an increased majority.
- A key uncertainty is the Government's commitment to its fiscal deficit target (3.3% of GDP) this financial year. Estimates from the Controller General of Accounts suggest that around 78% of this target was used in the first four months of the year (ending July). Despite a record transfer from the Reserve Bank of India – equivalent to around 0.9% of GDP – the Government will have to substantially curtail spending in coming months to meet this target – particularly following corporate tax cuts announced in September that could be around 0.7% of GDP (according to some estimates).
- We have lowered our forecast for Indian growth, given the weaker than expected outcome in Q2. Easing monetary policy is expected to support a modest recovery in the short term (led by investment), however downside risks (particularly around consumption) persist.

NAB INDIA GDP FORECASTS

%	2019	2020	2021
GDP	5.7	6.8	7.1

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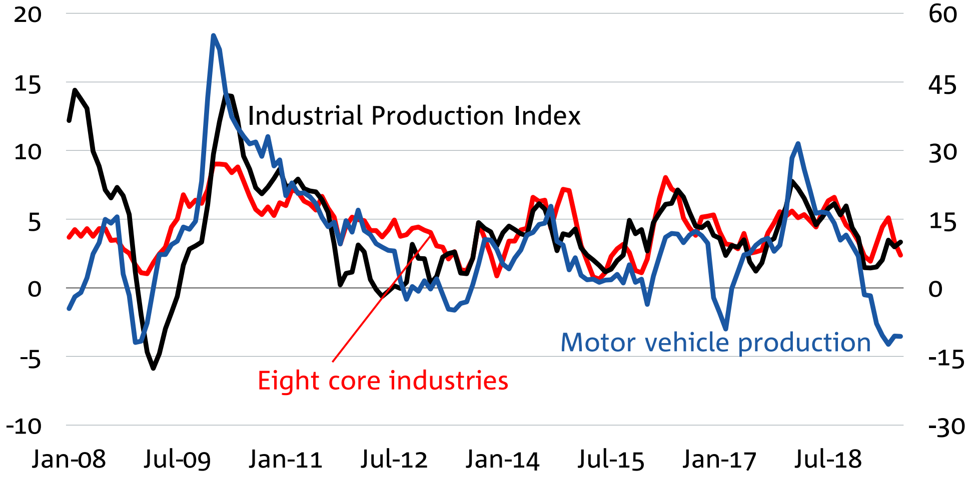
INDUSTRIAL PRODUCTION

INDUSTRIAL PRODUCTION

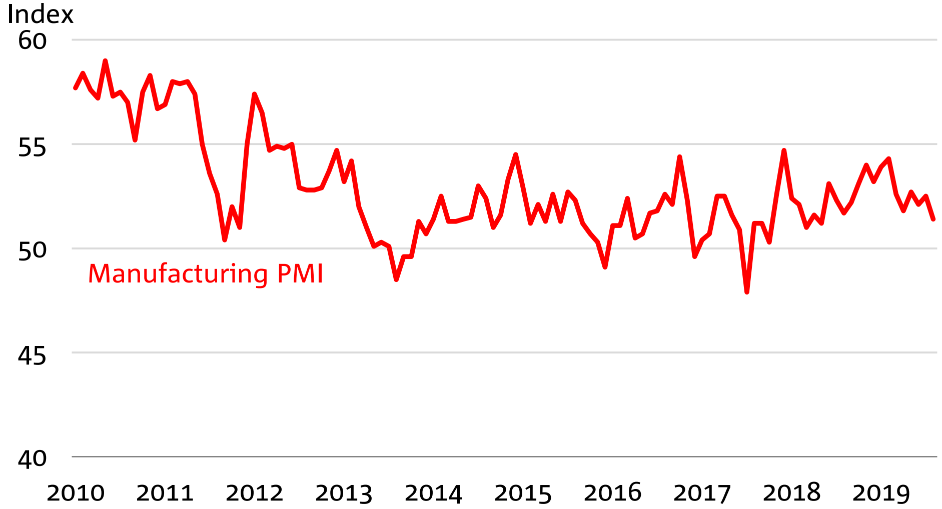
Slowing trend in growth, led by core industries



Source: CEIC, NAB Economics

PMI SURVEYS IMPROVE

PMI increases driven by improved output



Source: CEIC, NAB Economics

- Following a weak period at the start of 2019, India's industrial production recovered in the middle of the year – with growth stabilising in July at around 3.3% yoy (on a three month moving average basis). It is worth noting that this increase is well below the trend between Q4 2017 and Q4 2018 (around 5.5% yoy).

- This slower trend rate of growth is evident in the aggregate eight core industries index (coal, crude oil, natural gas, refinery products, fertiliser, steel, cement and electricity) that account for around 40% of the total industrial production index – with growth easing to 2.4% yoy (3mma) in July.

- That said, there are some divergent trends among individual industry sectors. There has been strong growth in steel production – up 10.1% yoy (3mma) in July – and electricity, increasing by 6.6% yoy (3mma). In contrast, crude oil and refinery products growth contracted – down 6.1% yoy (3mma) and 3.9% yoy (3mma) respectively.

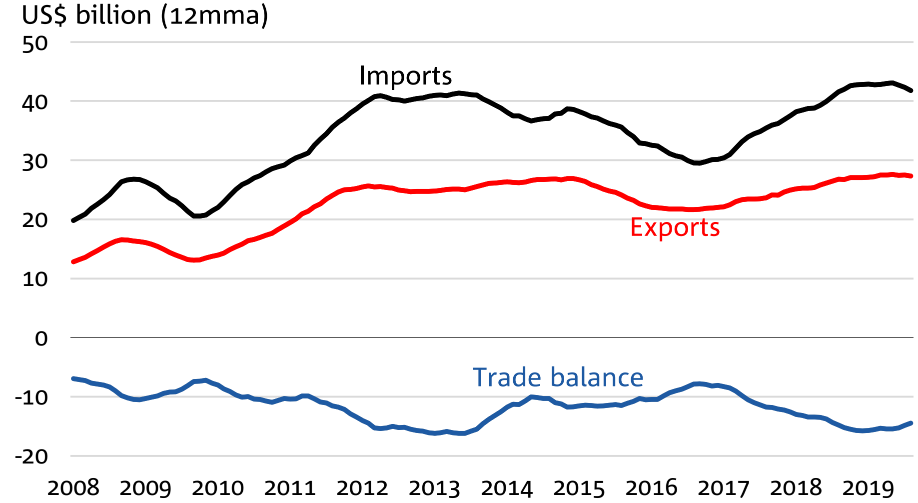
- Outside the core industries, automotive manufacturing is suffering – due to a sharp drop off in auto sales. A range of factors have been attributed to this decline, including slower economic growth, weaker consumer confidence and the collapse of non-bank finance firms that had been heavily involved in auto loans. Automotive manufacturing directly accounts for around 5% of the industrial production index, but the Automotive Component Manufacturers Association of India suggest that the sector accounts for around a quarter of manufacturing output when inputs from other manufacturing are factored in. Total motor vehicle production fell by almost 11% in the first eight months of 2019.

- The IHS Manufacturing PMI eased in August – down to a still positive 51.4 points, but well off the peaks of early 2019 (above 54 points in February). This was the weakest result for 15 months. Commentary within the PMI survey noted negative trends on both the demand and supply side – given the softness in the economy, along with rising input costs.

INTERNATIONAL TRADE

TRADE DEFICIT STARTING TO NARROW

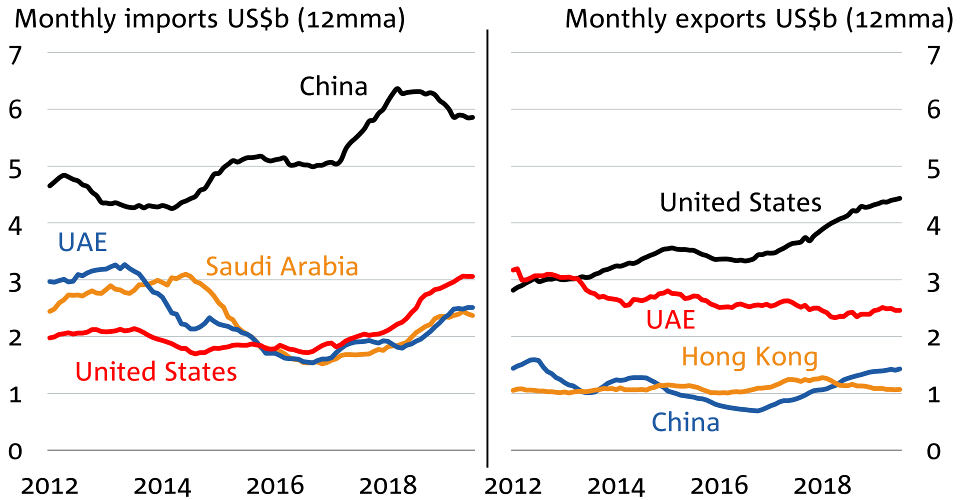
Value of imports has slowed since mid-2019



Source: CEIC, NAB Economics

TRADE BY MARKET

Trade with the United States has strengthened



Source: CEIC, NAB Economics

- At a high level, India is not particularly trade dependent for its stage of development. According to World Bank data, India remains below its income peers (Lower Middle Income economies) for both goods and services trade as a share of GDP. Overall, India has been a net importer of goods and services since the late 1970s.

- India's trade deficit increased significantly between late 2016 and late 2018 – essentially doubling in size – in part reflecting the strength of economic growth over this period. The rolling twelve month average value of imports plateaued in late 2018 and has declined slightly since June 2019, while exports remained relatively stable. The trade deficit has narrowed from a recent peak of US$15.8 billion (12mma) in December 2018 to US$14.5 billion (12mma) in August 2019.

- In US dollar terms, imports rose only modestly in the twelve months to August 2019 – up around 0.5% yoy. This increase was driven by imports of crude oil and petroleum products – which rose by around 6.0% yoy over this period. In contrast, imports of non-oil products fell by around 1.9% yoy. It is worth noting the negative impact of exchange rate movements over this period, with the Rupee down around 7.2% on average.

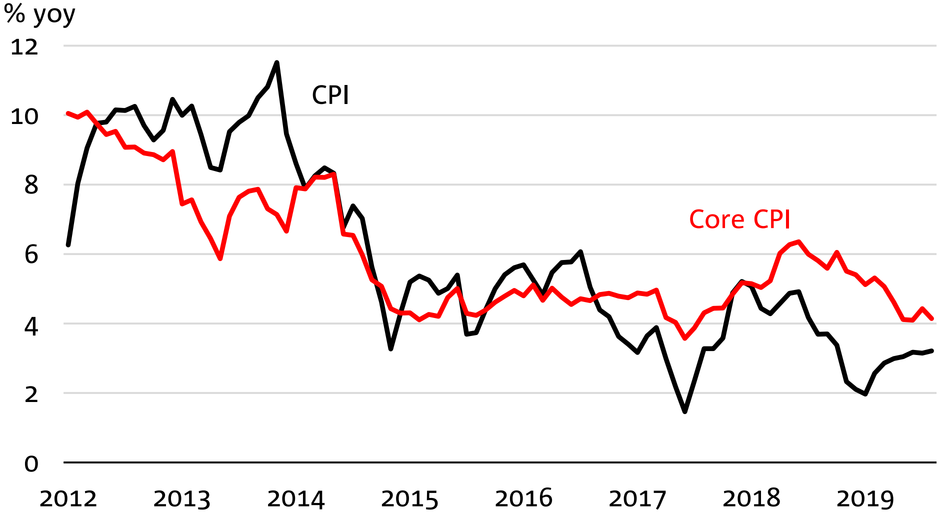
- China remains the largest source of India's imports – despite a 7.2% yoy fall in imports over the twelve months to July. In contrast, imports from the United States (the second largest source) rose by 22% over this period, along with a 31% yoy and 14% yoy increase from the UAE and Saudi Arabia.

- Exports rose modestly in the twelve months to August – up by almost 2.0% yoy in US dollar terms. The United States is by far the largest export market, with exports growing by 7.1% yoy in the twelve months to July, while there was also strong growth in exports to China.

INFLATION AND MONETARY POLICY

INFLATION

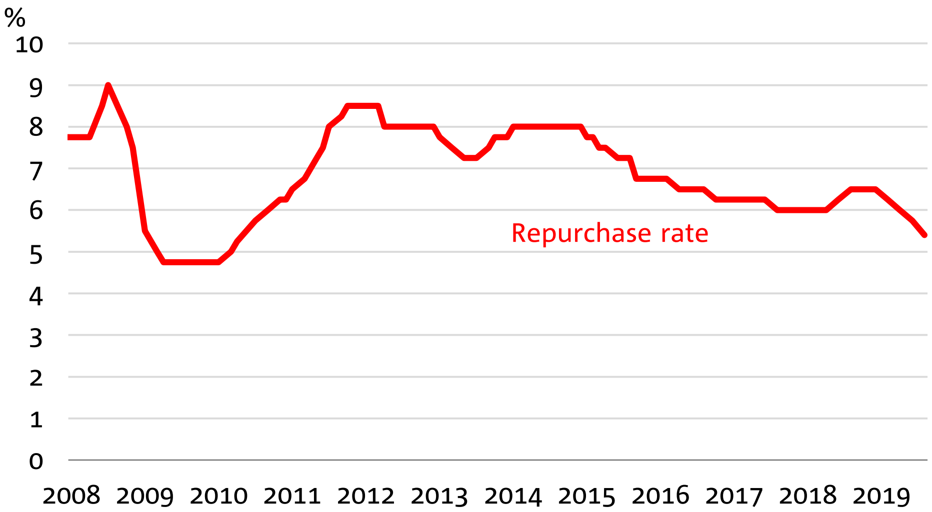
Headline inflation remains near historically low levels



Source: CEIC, NAB Economics

RBI REPURCHASE RATE

Monetary policy is easing



Source: CEIC, NAB Economics

- India's headline inflation has trended higher in recent months – with the Consumer Price Index increasing from around 2.0% yoy in January to around 3.2% yoy in August. This rate of inflation is historically low for India and sits below the mid-point of the Reserve Bank of India's inflation target (4%).

- Core inflation – removing generally more volatile fuel and food prices – edged slightly lower in August to 4.1% yoy (from 4.4% previously), a rate that was below the peaks of early 2018 and the typical rates of the post-GFC period. A range of economic reforms, including addressing external vulnerabilities, have contributed to this trend.

- The Reserve Bank of India has continued to ease monetary policy, cutting the Repurchase Rate by 35bps in June to a 9 year low of 5.4%. The 35bps cut was larger than expected and was the fourth straight rate cut in 2019.

- With inflation in the lower part of the target range, economic growth slowing and an easing bias for major central banks globally, the RBI has further scope for rate cuts. At the time of writing, markets have priced in cuts at the October 2019, December 2019 and February 2020 meetings, totalling around 50 basis points. Such moves would bring rates close to the lows implemented following the GFC.

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