



Infomerics Ratings

Infomerics Valuation And Rating Pvt. Ltd.

SEBI REGISTERED / RBI ACCREDITED / NSIC EMPANELLED
CREDIT RATING AGENCY

Mr. Vipin Malik,
(Chairman, Infomerics Ratings)

Mr. Sankhanath Bandyopadhyay
(Economist)

ECONOMIC DIGEST

GLOBAL AND INDIAN ECONOMIC DEVELOPMENTS

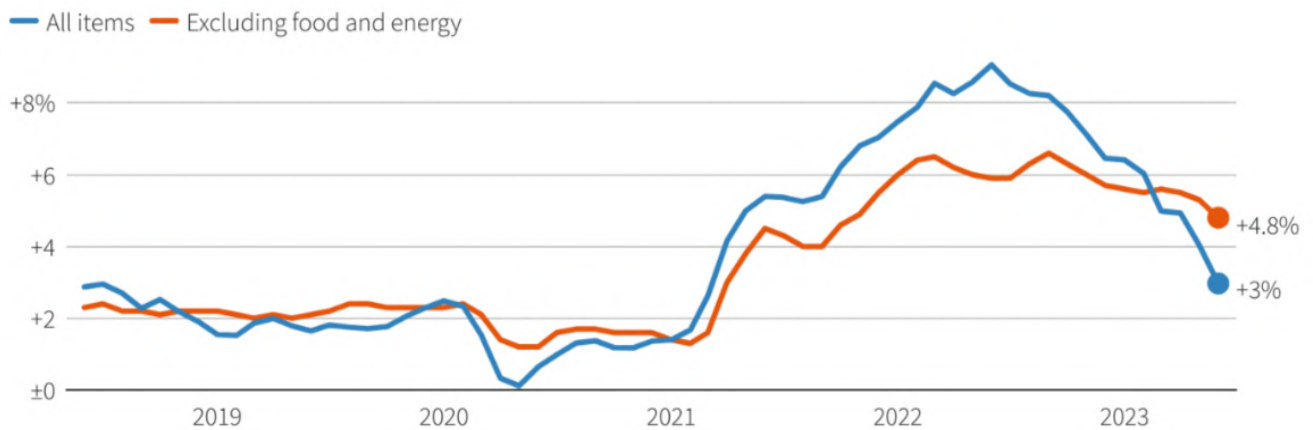
24 July 2023

Introduction

With a positive note, the US headline inflation eased to 3.0% from 4.0% in May'23, while core inflation moderated to 4.8% in June (vs. 5.3%). The DXY Index fell near a one-year low of 100.5 after US CPI shows comfortably downward trend.

Annual change in U.S. Consumer Price Index

In June inflation for all items fell to 3.0%. The 'core' rate that omits products expected to have volatile prices fell to 4.8%.



Published July 12, 2023 at 12:33 PM GMT
Sources: Bureau of Labor Statistics, Refinitiv

Core services CPI slowed from 6.6% year-on-year (YoY) in May'23 to 6.2% year-on-year (YoY) in June'23 while the shelter CPI inflation slowed from 8.0% YoY to 7.8% YoY. Therefore, core services CPI inflation excluding rents, declined from 4.6% YoY to 4.0% YoY.

According to the US Bureau of Labour Statistics (7 July 2023), total nonfarm payroll employment increased by 209,000 in June'23, and the unemployment rate changed little at 3.6 percent. Employment continued to trend up in government, health care, social assistance, and construction. The jobless rates for adult men (3.4 percent), adult women (3.1 percent), teenagers (11.0 percent), Blacks (6.0 percent), Asians (3.2 percent), and Hispanics (4.3 percent) showed little change over the month. In June'23, the labor force participation rate was 62.6 percent for the fourth consecutive month, and the employment-population ratio, at 60.3 percent, was unchanged over the month.

While the ISM services has increased in June'23, the ISM manufacturing has declined. In US equity, the S&P 500 index has recently (8/6/23) increased by more than 20% cumulatively from the low of October 12, 2022. The US 2- year bond yield posted one-month low (4.60%) after temporarily rising above 5% in the previous week, whereas the US 10-year bond yield moderated back below (3.76%) where it ended 2022 (3.87%) after the temporary spike above 4% in the previous week.¹

US Federal Open Market Committee (FOMC) held its target range of the federal funds rate steady (at 5.0 - 5.25 per cent) in its June 2023 meeting following a cumulative increase of 500 bps since March 2022. Australia, New Zealand and Israel also paused in their July meetings. The European Central Bank (ECB), Swiss National Bank and the Sveriges Riksbank raised their policy rates by 25 bps each in their June meetings, while Canada hiked further by 25 bps in its July meeting.

The UK and Norway, however, accelerated their pace of rate hikes in their latest meetings to 50 bps from 25 bps in the previous meeting. A positive development is that UK's inflation dropped to a 15-month low of 7.9% in June, compared to 8.7% in previous month.



Indian Economic Developments:

Economic Growth:

Amidst these global spillovers, India's economy has sustained its growth momentum in FY23 on account of its strong macroeconomic fundamentals and the prompt policy action by the Government and the RBI. India's real GP expanded by 7.2 per cent in FY23, the highest among major economies. The latest estimate of real GDP turned out to be higher than the second advance estimate released in February 2023. The higher annual growth was driven mainly by better-than-expected growth in the fourth quarter of the fiscal year.

¹ ALPHA BANK (14 July 2023).

The performance of India's real GDP in Q4 of FY23 stood out compared to other countries. The year-on-year (YoY) growth in real GDP in Q4 of FY23 is estimated at 6.1 per cent, compared to 4 per cent growth in Q4 of FY22 and 4.5 per cent growth in Q3 of FY23. On a sequential basis, the growth in Q4 of FY23 at 8.4 per cent is higher compared to 3.7 per cent in the previous quarter, reflecting the sustenance of growth momentum in Q4.

Inflation Trends:

The CPI inflation has increased to 4.81% in June'23 compared to 4.31% in May'23 primarily due to price pressures from tomatoes, pulses, spices. Uneven rainfalls among different states and recent upside pressure in tomato prices has posed challenges, though core inflation is range bound, but personal care segment has shown sticky prices, where still health, education, personal care segments have some stickiness in prices.² The increase is in line with the expectation due to recent upsurge in tomato prices, some segments in vegetable prices and due to uneven monsoon. The positive is that, it is still in the tolerable range of the RBI's inflation zone (4%+-2%). State wise Bihar, Haryana, Tamil Nādu, Uttarakhand have shown price pressures. Interestingly, West Bengal shows certain range bound inflation trend despite news of speculative hoarding due to upsurge in tomato prices.

A positive aspect on the industrial production is that the industrial production based on IIP registered a growth of 5.2% in May from 4.5% in April. For the first two months IIP registered a growth of 4.8%. The mining sector recorded a growth rate of 6.4% in May, manufacturing sector also witnessed growth, with a rate of 5.7%. Interestingly, seen from the use-based category, capital goods have shown remarkable growth (8.2%) possibly due to lag impact of government thrust on capex. Going forward, impact of EL Nino, monsoon, price movements of spices, pulses, vegetables would have impact on future inflation trends.

Gross Fixed Capital Formation:

Gross Fixed Capital Formation (GFCF) has been a major growth driver in Q4 of FY23, with its share in GDP at a 10-year high of 35.3 per cent. This has been propelled by the crowding-in of private sector investment by a significant ramp-up in public sector investment over the years. The share of total exports in GDP moderated to 22.8 per cent in Q4 of FY23, compared to 24.4 per cent in Q1 of FY23, as synchronised monetary tightening by major economies led to a decline in consumer spending in advanced nations and moderation in international trade.

Monsoon Trends:

The South-west monsoon (SWM) covered the entire country on July 02, 2023 six days before the normal date, even though its onset was delayed by eight days – SWM touched the Kerala coast on June 08 as against June 04 predicted by the India Meteorological Department (IMD). The progress of SWM has, however, been uneven partly on account of the impact of cyclone Biparjoy. Precipitation picked up in recent weeks and as per the latest data as of July 14, 2023 the cumulative monsoon was one per cent above the long period average (LPA). As on July 09, 2023 the total kharif sown area was 5.4 per cent lower than the previous year's level across all major crop categories, except sugarcane and coarse

² Core inflation declined marginally to 5.1 per cent in June from 5.2 per cent in May. While inflation in most of the constituents of the core group softened, it remained steady for health and increased in the case of transport and communication, and education.

cereals. The current reservoir storage levels are much above long period averages, which augurs well for ongoing sowing activity.

Major Crop Production & Procurement Trends:

The horticulture sector, accounting for about 33 per cent of total agriculture gross value added (GVA) in India, continued to register record production as per the first advance estimates (1st AE) for 2022-23. Total horticultural production surpassed last year's final production estimate by 1.1 per cent, driven by vegetables. Rice procurement in the Kharif Marketing Season (KMS) 2022-23 and wheat procurement in the Rabi Marketing Season (RMS) 2023-24 touched 56.8 million tonnes and 26.2 million tonnes, respectively on July 11, 2023. In order to alleviate retail price pressures, the Food Corporation of India (FCI) has been conducting e-auctions for rice and wheat under the Open Market Sale Scheme (Domestic); and the third weekly e-auctions for rice and wheat commenced on July 12, 2023.³ Comfortable wheat procurement provides a buffer to the agri-economy. Nearly 2.6 crore Metric Tonne of wheat has been procured until 21st June 2023, benefitting 21.3 lakh farmers. As against the buffer norm of 2.1 crore Metric Tonnes for the April-June period of 2023, the combined stock position of wheat and rice in the central pool has reached 7.3 crore Metric Tonnes, placing India in a comfortable position to meet its domestic foodgrain requirements.

High Frequency Indicators (HFIs) show strong rebound:

Several high-frequency indicators also point towards a strong rebound in the industry sector. After growing at a modest pace in Q2 and Q3, the Index of Industrial Production (IIP) expanded in Q4 of FY23, with a notable increase in the production of capital goods and infrastructure/construction goods. This signifies a pick-up in capital formation in the economy. The construction sector (IIP) registered double-digit growth in Q4 of FY23 after slowing in Q2 on account of heavy monsoons. Other construction sector indicators, such as cement production and steel consumption, also rose in Q4 of FY23. The growth in the sector has been supported by Government's emphasis on infrastructure and increased housing demand. The Indian housing market has witnessed significant growth in sales and new house launches in FY23, despite increasing home prices and a rise in interest rates on home loans.

The Hotel Industry began a strong recovery in FY23, with the hotel occupancy rate surpassing the average pre-pandemic level of FY20 in Q4, accompanied by a rise in Average Daily Rate (ADR) and Revenue per Available Room (RPAR). The growth in the hospitality sector was driven by domestic leisure travel growth, the resumption of business travel in the country, as well as wedding and social events. Small-to-medium-sized domestic MICE (Meetings, Incentives, Conference, Exhibitions) events also made a comeback, fuelling demand for hotels. The tourism sector also showed signs of revival, with Foreign Tourist Arrivals (FTA) in India close to the average pre-pandemic level in Q4 of FY23, supported by the resumption of scheduled international flights. With the removal of pandemic-related restrictions, a surge in corporate travel and a rebound in MICE tourism and Bleisure¹ travel, domestic air passenger traffic surpassed the pre-pandemic level in Q4 of FY23.

³ RBI Bulletin (June 2023).

India's External Balance and Trading Relations:

India's merchandise exports registered contraction for the fifth consecutive month in June 2023, declining by 22.0 per cent (y-o-y) as a sharp negative momentum of -) 5.8 per cent interacted with an adverse base. The contraction in exports was broad-based, with 77.5 per cent of the export basket (21 out of 30 major commodities) registering a decline on a y-o-y basis. The largest drag on growth was from petroleum products, followed by gems and jewellery.

Amidst the overall decline, electronic goods, which account for 7.4 per cent of total merchandise exports, remained positive contributors to export growth.⁴

One of the reasons for moderating pace of growth in merchandise exports significantly in 2023 has been because of persistent geopolitical tensions, disruption in global supply chain due to Russia-Ukraine war, monetary tightening and recessionary fears, which has continuously led to a fall in consumer spendings across the globe especially in advanced economies. Though the decline in imports is a good sign for the country, however, that has also led to de-growth in India's major export sectors like petroleum products, gems & jewellery, organic & inorganic chemicals etc. Some policies have been suggested as follows:⁵

- ✓ Easy and low cost of credit to the MSMEs.
- ✓ Marketing support for further promoting Brand India products and services globally.
- ✓ GST exemption on Freight on exports.

Indonesia has emerged as India's largest trading partner in the ASEAN region, with trade seeing an eightfold increase since 2005, reaching an impressive USD 38 billion in FY 2022-23. The evolution of India's 'Look East Policy' in 1991, followed by the 'Act East Policy', has facilitated a rapid development in India's bilateral relations with Indonesia. Areas of cooperation inter-alia, include macroeconomic challenges and global economic prospects, bilateral investment relations, and cooperation in G20 and ASEAN matters.⁶ Indian authorities are also in conversations with their Indonesian counterparts to settle cross-border transactions in local currencies.

Further, RBI and the United Arab Emirates (UAE) Central Bank Sign MoUs for Cross-Border Transactions. These agreements focus on promoting the use of local currencies for cross-border transactions and integrating their payment systems, specifically the Unified Payments Interface (UPI) with the Instant Payment Platform (IPP) of UAE.

The India-UAE Comprehensive Economic Partnership Agreement (CEPA) came into effect on May 1, 2022. In the year since the agreement came into force (between May 2022 and April 2023), the bilateral trade in goods between the two countries increased to US\$ 82.6 billion from US\$ 75.2 billion in the corresponding period a year ago. Exports to the UAE increased by 6.5 per cent during this period, as against India's overall merchandise export growth of 3.5 per cent. Imports from the UAE, however, grew by 12.2 per cent, lower than India's overall merchandise import growth of 13.0 per cent.

⁴ RBI Bulletin (June 2023).

⁵ Federation of Indian Export Organisations, Press Release; FIEO/MC/PR/11/2023-24 (July 14, 2023).

⁶ BUSINESSWORLD (17 July 2023).

Fiscal Deficit Trends

As highlighted by the RBI June'23 Bulletin, according to the latest data released by the Controller General of Accounts (CGA), the gross fiscal deficit (GFD) of the central government during April-May 2023 stood at 11.8 per cent of the budget estimates (BE) for 2023-24, which was lower than in the corresponding period of the previous year. This improvement is attributable to higher collections under non-tax receipts. On the other hand, the total expenditure of the central government increased by 6.9 per cent on a y-o-y basis. A noteworthy feature is the continued thrust on capital outlay with a y-o-y growth of 58.8 per cent. The revenue expenditure contracted by 4.3 per cent, which led to improvement in the quality of spending of the central government.

On the receipts side, direct tax collections contracted by 5.0 per cent, owing to a decline in corporate tax receipts by 28 per cent. Indirect taxes recorded a moderation in growth to 1.6 per cent, attributable to a reduction in excise duty collections by 16.3 per cent.⁷ Net tax collections contracted by 9.6 per cent over their level a year ago. Non-tax revenue collections of the central government recorded a y-o-y growth of 173.4 per cent on the back of higher surplus transfer by the Reserve Bank. Non-debt capital receipts contracted by 88.0 per cent vis-à-vis the corresponding period of the previous year on account of slower pace of disinvestment.

Financial and Liquidity Conditions:

The RBI conducted one variable rate repo (VRR) fine tuning operation on 19th June 2023 to inject liquidity amounting to ₹ 75,004 crore to the banking system (offers received were ₹ 75,695 crore). Afterwards, Government spending in the beginning of July'23 augmented surplus liquidity in the banking system. Volatile liquidity conditions have induced some aversion among banks to park surplus funds for longer tenors. Illustratively, while the response to the 14-day variable rate reverse repo (VRRR) (main operation) conducted on June 30 was tepid, with offers received amounting to a mere ₹ 11,789 crore (notified amount of ₹ 1.0 lakh crore), six-fine tuning VRRR operations of 1-4 days maturity conducted in July'23 evoked more interest.

The liquidity absorbed through these operations amounted to ₹63,843 crore (July 3), ₹67,295 crore (July 4), ₹87,870 crore (July 5), ₹39,000 crore (July 6), ₹1.06 lakh crore (July 7) and ₹40,291 crore (July 11). Overall, the average total absorption under the liquidity adjustment facility (LAF) narrowed to ₹1.6 lakh crore during June 16-July 12 (from ₹1.8 lakh crore during May 16 to June 15).⁸

Of the total average surplus liquidity, placement of funds under the standing deposit facility (SDF) averaged ₹1.1 lakh crore during June 16 to July 12, 2023, down from ₹1.4 lakh crore during the previous period (May 16 to June 15, 2023). Amidst tapering of surplus liquidity and its skewed distribution, recourse to the marginal standing facility (MSF) averaged ₹17000 crore during 16th June to 12th July 2023 (₹2000 crore during the previous period) and the daily MSF reached ₹85,821 crore on 29th June 2023 (the highest since 1st April 2019). Accordingly, net absorptions under the LAF declined to ₹1.19 lakh crore during 16th June'23 to 12th July'23 as compared with ₹1.45 lakh crore during 16th May'23 to 15th June 2023.

⁷ GST collections (Centre plus States) stood at Rs.1.6 lakh crore in June 2023, registering a year-on-year growth of 11.7 per cent.

⁸ RBI Bulletin (June 2023).

The weighted average call rate (WACR) gradually trended towards the upper band of the LAF corridor during the second half of June before easing sharply in the first week of July. On an average basis, the WACR traded 6 bps above the policy repo rate while the triparty repo rate and the market repo rate traded 2 bps and 5 bps, respectively, below the policy repo rate during June 16 to July 12, 2023.

Domestic bond yields traded with a hardening bias and the yield on the 10-year benchmark Government securities (G-sec) (7.26 per cent GS 2033) closed at 7.12 per cent on 12th July, 2023 as compared with 7.04 per cent on 15th June 2023. Stronger than expected US GDP data and a sharp rise in US treasury yields imparted pressure on domestic bond yields across the term structure.

The withdrawal of ₹2000 banknotes from circulation announced on May 19, 2023 (20th week) resulted in a decline in CiC between 20th (May 19) and 26th week (June 30) in 2023 when compared with the corresponding period of previous years. About 87 per cent of the notes received back from circulation as on June 30 has been deposited with the banks.

Bank Credit Growth

Bank credit growth remain steady and undergoing a sustained growth with healthy credit growth of 15.4% YoY in Jun'23, driven by continued traction in the Retail and SME segments. The Credit card business is seeing strong momentum, with robust growth in both spends and the number of cards. In FY23, most Tier 1 and Tier 2 banks were able to improve their NIMs and some banks got distinguished from others through add on of generating higher levels of NII which increased their net profit to all-time highs. The rapid pace of personal loan growth (both housing and non-housing) has been supporting overall credit expansion. Accordingly, the share of personal loans in total bank credit has surged to 28 per cent in 2022-23 from 21 per cent in 2017-18.