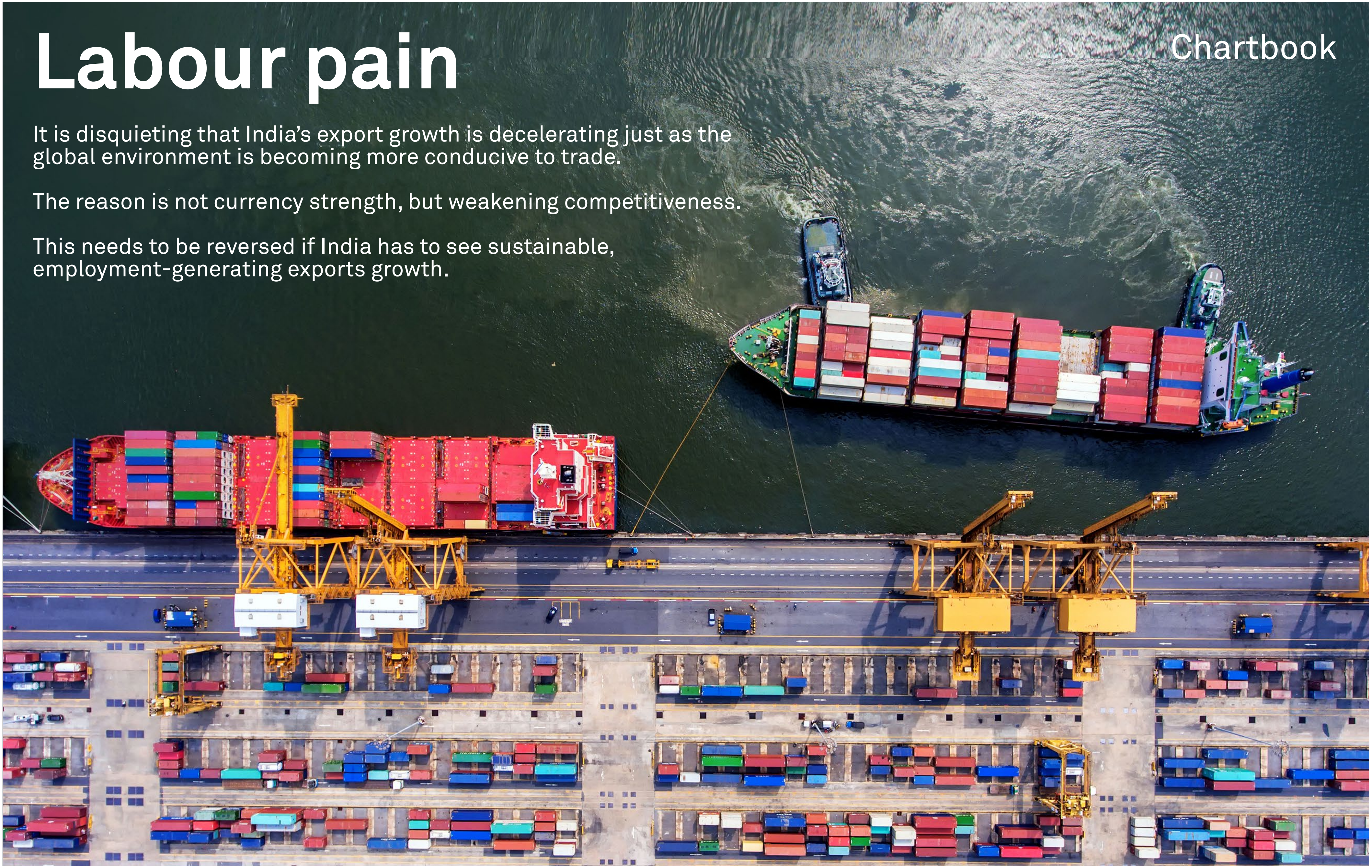
CRISIL
An S&P Global Company



Labour pain

Chartbook

It is disquieting that India's export growth is decelerating just as the global environment is becoming more conducive to trade.

The reason is not currency strength, but weakening competitiveness.

This needs to be reversed if India has to see sustainable, employment-generating exports growth.

Analytical contacts

Dharmakirti Joshi
Chief Economist
dharmakirti.joshi@crisil.com

Adhish Verma
Economist
adhish.verma@crisil.com

Pankhuri Tandon
Economic Analyst
pankhuri.tandon@crisil.com

Media contacts

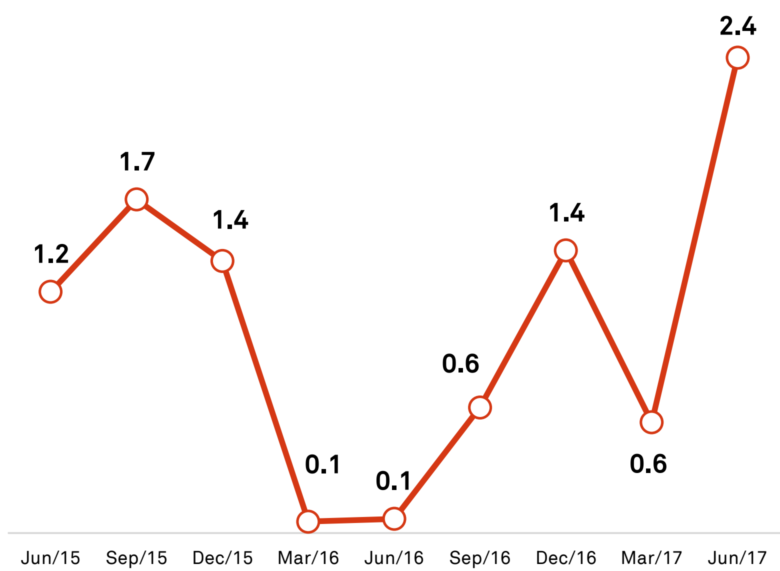
Saman Khan
Media Relations
D: +91 22 3342 3895
M: +91 95940 60612
B: +91 22 3342 3000
saman.khan@crisil.com

Khushboo Bhadani
Media Relations
D: +91 22 3342 1812
M: +91 72081 85374
B: +91 22 3342 3000
khushboo.bhadani@crisil.com

Shruti Muddup
Media Relations
D: +91 22 3342 5916
M: +91 98206 51056
B: +91 22 3342 3000
shruti.muddup@crisil.com

India's current account deficit (CAD) climbed to a four-year high of $14.3 billion in the first quarter of this fiscal, or 2.4% of gross domestic product (GDP). That compares with $0.4 billion, or 0.1% of GDP, in the same period last fiscal.

CAD at a four-year high in Q1 % of GDP



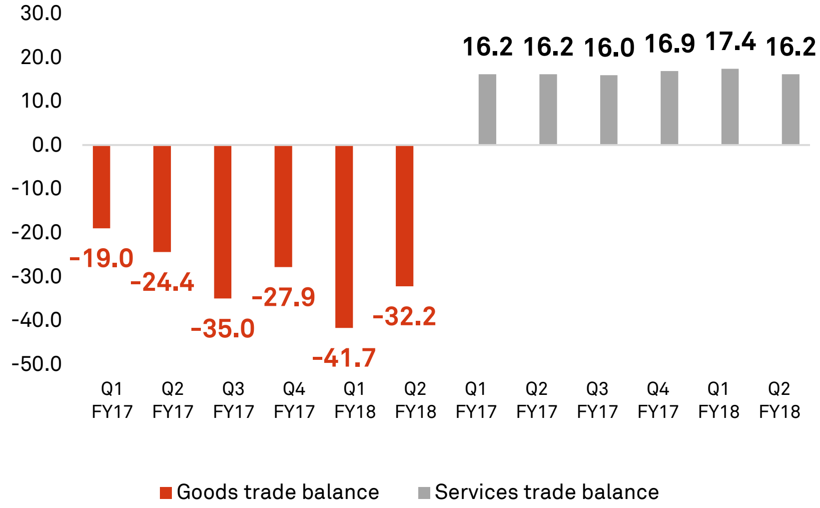
Source: Reserve Bank of India

The main reason for this is merchandise trade deficit ballooning to a four-year high of $41.7 billion compared with $19 billion in the corresponding quarter of fiscal 2017. While export growth was 9.1%, import growth was way faster at 34.6%.

On the other side, services trade surplus has remained stable.

Goods trade deficit moderated to $32.2 billion[1], but remained higher than the $24.4 billion in the same quarter last fiscal.

Trade balance $ billion



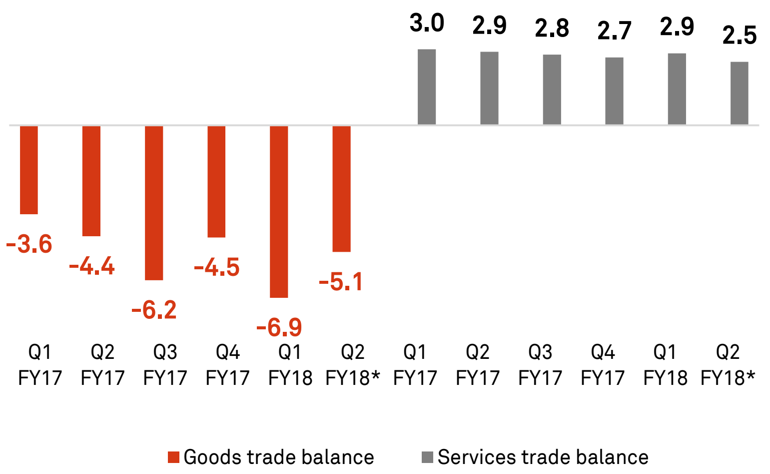
Source: Ministry of Commerce, Reserve Bank of India

[1]Based on Commerce Ministry's estimates

Merchandise trade deficit has been widening because exports growth has fallen way short of imports growth.

In this fiscal so far[2], imports have grown 23.8% on average, compared with 9.5% growth in exports.

Goods trade deficit narrowed sequentially, but not on-year % of GDP

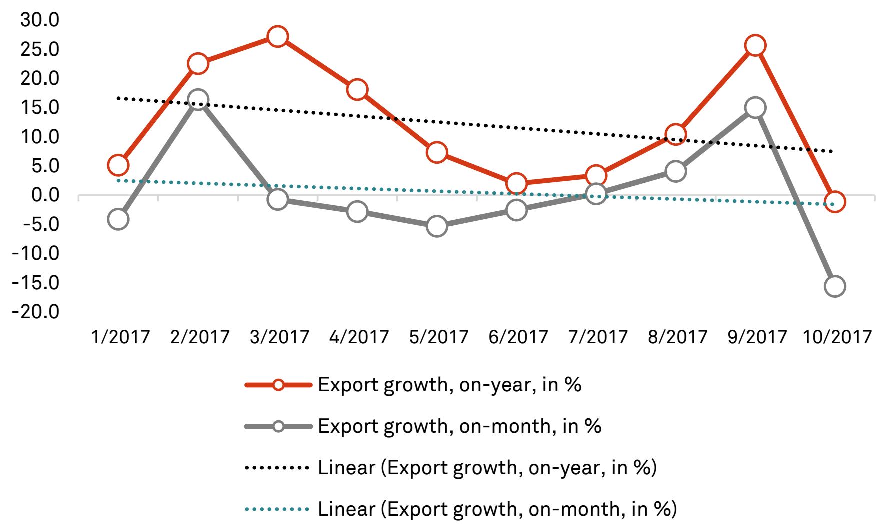


**Q2 FY18 estimates are based on CRISIL GDP forecasts*
Source: Ministry of Commerce, RBI

Though higher than the previous fiscal, exports growth has been on a decelerating trend, and declined 1.1% in October.

Import growth has also moderated in recent months, though it remains stronger than export growth.

Exports growth on a slippery slope



Note: On-month export growth is deseasonalised series
Source: Ministry of Commerce

[2] April-October 2017

It is disquieting that India's export growth is decelerating at a time when the global environment is becoming more conducive for trade.

The International Monetary Fund (IMF) expects global growth to rise to 3.6% in 2017 from 3.2% in 2016.

Global merchandise trade[3] is seen growing stronger at 4.2%, boosting trade intensity of growth[4] for the first time in six years.

Global exports recovering...

Note: 2017F is IMF's forecast for 2017
Source: IMF

India has not been able to take as much advantage of stronger trade growth as many of its Asian peers.

While India's export growth is 9.5% in this fiscal so far, for Vietnam, South Korea, and Indonesia it was way higher at 23.8%, 18.4% and 17.8%, respectively.

...but India's exports are trailing

**Average export growth for April-September 2017*
Source: World Trade Organisation

[3]As measured by global volume of goods exports
[4]Ratio of world trade to GDP growth

The subdued export performance in recent months cannot be attributed to unfavourable currency competitiveness.

After appreciating significantly up to March 2017, the rupee has been stable against the dollar.

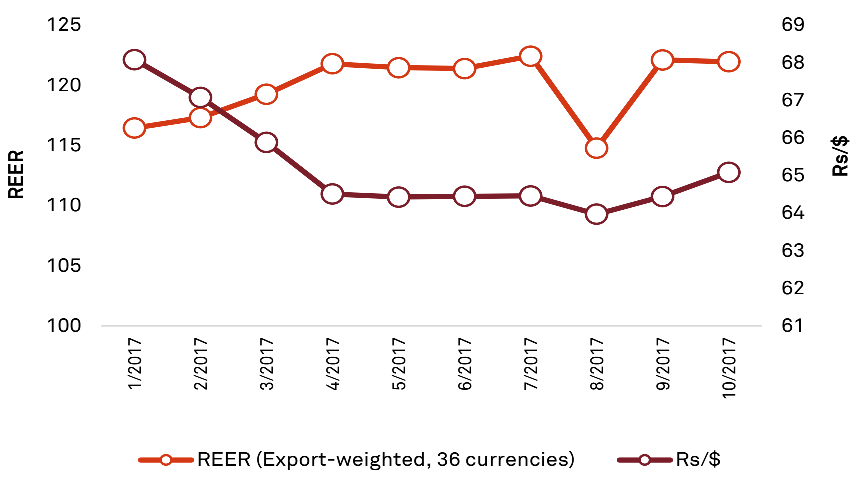
A better indicator of India's export competitiveness is the real effective exchange rate[5] (REER), which has also remained stable since the beginning of this fiscal. In fact, it fell a touch in August 2017.

Improving global growth and stable rupee suggest that domestic developments might have had a greater role to play in the current export growth slowdown.

The implementation of the Goods and Services Tax (GST) and associated glitches have had an impact, particularly on small and medium enterprises -- evident in low export growth in gems and jewellery, textiles, and leather sectors.

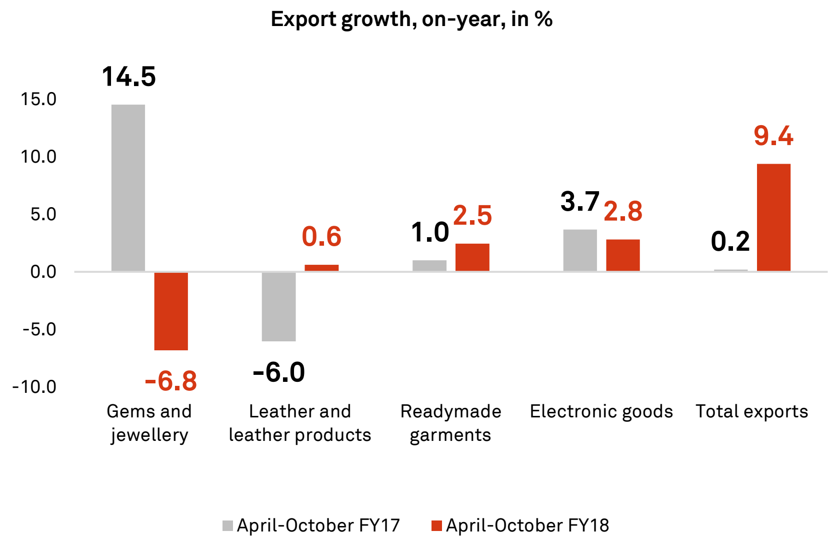
Incidentally these sectors are the most labour-intensive among the major export sectors. Significantly, export growth in labour-intensive sectors has been much lower than the overall export growth in this fiscal.

Rupee has been stable in recent months



Source: RBI

Exports from labour-intensive sectors have suffered the most



Source: Ministry of Commerce

[5]REER measures rupee's real value (inflation-adjusted) against currencies of its 36 major export destinations

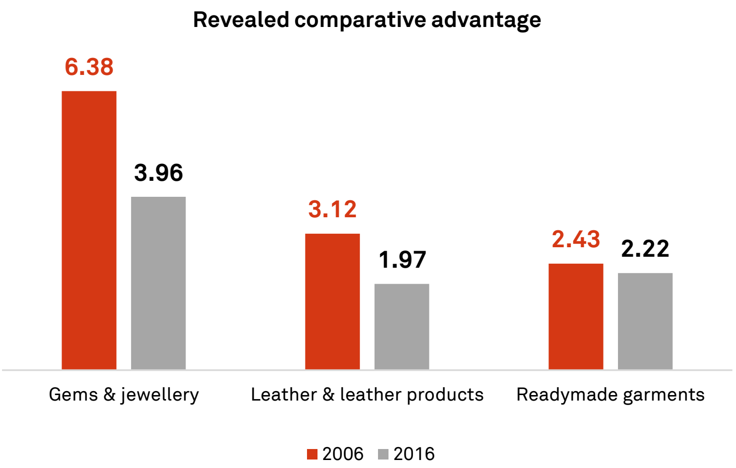
Disruptions due to GST are transitory but there are other structural issues that need to be addressed. The revealed comparative advantage (RCA), or generally speaking, competitiveness of these labour intensive sectors, was already on the decline.

The 2006-2016 decade saw RCA markedly diminish for three of these sectors, with demonetisation and GST impacting further.

So while policy disruptions have been transitory, there are structural issues dogging India's export competitiveness.

High exports growth, particularly in the labour-intensive sectors, is vital to sustaining employment-generating growth.

Labour-intensive sectors have been losing their competitive edge



Source: ITC database

About CRISIL Limited

CRISIL is an agile and innovative, global analytics company driven by its mission of making markets function better. We are India's foremost provider of ratings, data, research, analytics and solutions. A strong track record of growth, culture of innovation and global footprint sets us apart. We have delivered independent opinions, actionable insights, and efficient solutions to over 100,000 customers.

We are majority owned by S&P Global Inc., a leading provider of transparent and independent ratings, benchmarks, analytics and data to the capital and commodity markets worldwide.

About CRISIL Research

CRISIL Research is India's largest independent integrated research house. We provide insights, opinion and analysis on the Indian economy, industry, capital markets and companies. We also conduct training programs to financial sector professionals on a wide array of technical issues. We are India's most credible provider of economy and industry research. Our industry research covers 86 sectors and is known for its rich insights and perspectives. Our analysis is supported by inputs from our large network sources, including industry experts, industry associations and trade channels. We play a key role in India's fixed income markets. We are the largest provider of valuation of fixed income securities to the mutual fund, insurance and banking industries in the country. We are also the sole provider of debt and hybrid indices to India's mutual fund and life insurance industries. We pioneered independent equity research in India, and are today the country's largest independent equity research house. Our defining trait is the ability to convert information and data into expert judgments and forecasts with complete objectivity. We leverage our deep understanding of the macro-economy and our extensive sector coverage to provide unique insights on micro-macro and cross-sectoral linkages. Our talent pool comprises economists, sector experts, company analysts and information management specialists.

Argentina | China | Hong Kong | **India** | Poland | Singapore | UK | USA
CRISIL Limited: CRISIL House, Central Avenue, Hiranandani Business Park, Powai, Mumbai – 400076. India
Phone: + 91 22 3342 3000 | Fax: + 91 22 3342 3001 | www.crisil.com
/company/crisil @CRISILLimited /CRISILLimited /user/CRISILLimited

CRISIL
An S&P Global Company