Macroeconomics | First cut

Growth momentum losing steam

March 2023

GDP growth slows on domestic and external factors

- India's real gross domestic product (GDP) grew 4.4% on-year in the third quarter this fiscal, slower than 6.3% previous quarter and 5.2% in the same quarter last fiscal.
- Nominal GDP growth stood at 11% (due to slower inflation and real GDP growth), returning to its long-term trend.
- All demand segments saw slower growth, with private consumption, government consumption expenditure, and imports recording the sharpest fall. On the supply side, growth in the manufacturing and services sectors slid, while growth in the agriculture, construction, mining and electricity sectors accelerated.
- Private final consumption expenditure (PFCE) growth slowed to 2.1%, from 8.8% previous quarter, suggesting faltering domestic demand. This resonates with import growth plummeting to 10.9% from 25.9%.
- While export growth also decelerated to 11.3% from 12.3%, the extent of slowdown was less than that of imports. Exports began slowing down quicker than imports in the second quarter, as external demand started weakening earlier than domestic demand.
- Government final consumption expenditure (GFCE) growth decelerated for the second consecutive quarter (-0.8% vs -4.1%), reflecting normalisation of pandemic spend.
- Investment, or gross fixed capital formation (GFCF), growth performed relatively well, albeit slowing to 8.3% from 9.7%. While the centre's capital expenditure moderated, it picked up for major states.
- On the production side, gross value added (GVA) grew 4.6%, compared with 5.5% previous quarter. Manufacturing growth saw the sharpest fall (-1.1% vs -3.6%), reflecting the hit from exports and waning domestic demand.
- Services growth also slowed from the base effect-driven high growth, but was notably higher than manufacturing growth. Trade, hotels, transport and communication services (THTC) grew 9.7%, compared with 15.6% previous quarter, as they continued the catch-up with the pre-pandemic trend. The share of THTC in GVA stood at 19.3%, compared with 18.4% in the third quarter last fiscal and 20.1% in the same quarter in fiscal 2020 (the corresponding quarter before the pandemic struck).
- Agriculture GVA growth improved to 3.7% from 2.4%, reflecting improving farm prospects.
- Construction GVA growth accelerated to 8.4% from 5.8%, indicating support from the government's infrastructure push and healthy investment growth.

Growth estimates revised up for pandemic years, retained for this fiscal

- Alongside quarterly estimates, the National Statistics Office (NSO) released revised estimates until last fiscal and second advance estimates for this fiscal.
- The second advance estimates maintained the GDP growth estimate for this fiscal at 7.0%, same as the previous estimate.
- Growth estimates were revised up for the previous 3 years — 9.1% (compared with 8.7% previously) for fiscal 2022, -5.8% (-6.6) for fiscal 2021, and 3.9% (3.7%) for fiscal 2020. This suggests that the impact of Covid-19

waves (in fiscals 2021 and 2022) was not as severe as thought previously.

Our view

The quarterly growth trends indicate that the slowdown is intensifying and becoming more widespread in the economy. However, the data is subject to revisions, with the next update due in May.

India's export and industrial growth was hit in the second quarter this fiscal by a global demand slowdown (particularly for goods), and this continued into the third quarter.

The global slowdown is in early stages. The United States and Europe performed reasonably well in the December quarter, but that was driven by less import-intensive sectors. The slowdown in exports is also because the pattern of consumption in the West after opening up has become skewed towards services, which are not import-intensive.

The third quarter reflected waning momentum in domestic consumption. Demand for goods weakened more than for services. Given that services are yet to materially catch-up with pre-pandemic trends, they are registering robust growth rates relative to goods. Demand for goods had picked up before that for services, and the recent weakness reflects bigger pinch from inflation and rising interest rates. The good news has come from healthy agriculture growth, which is improving rural prospects.

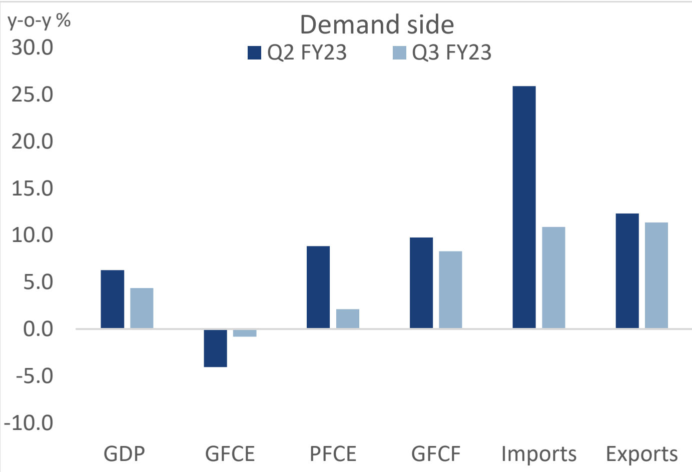
Demand momentum is expected to slow further, both at the domestic and global levels. Domestically, the transmission of the Reserve Bank of India's rate hikes has picked up since December, and key rates have either surpassed or reached close to the pre-pandemic 5-year average. The transmission is yet to be completed, which is likely to lead to a further rise in borrowing costs. This could take some steam off domestic demand next fiscal.

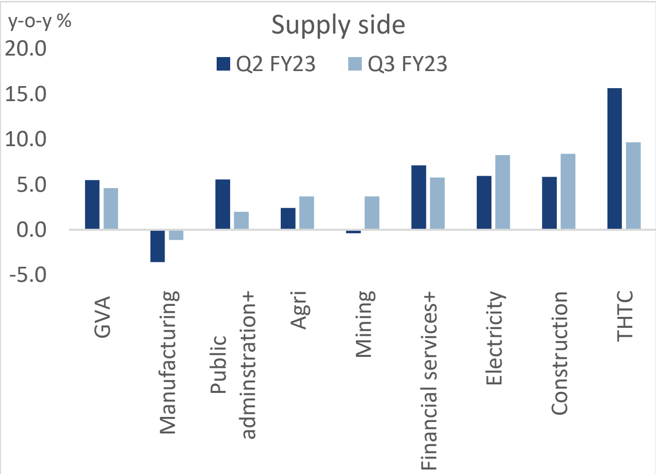
The advanced economies will inevitably face slower growth in 2023 as their interest rates are already at decadal highs. They account for 45% of India's exports, which will bear the brunt of weaker demand.

Besides the global slowdown, a forecast of El Nino, which disturbs Indian monsoons, is another risk to monitor — it could hit rural incomes.

The above-mentioned factors are expected to slow India's GDP growth to 6.0% next fiscal from 7.0% this fiscal.

Tracing growth slowdown in third quarter across major demand- and supply-side segments





Source: NSO, CEIC, CRISIL

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