dun & bradstreet
GROWING RELATIONSHIPS THROUGH DATA

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Research Team
Dr. Arun Singh
Dipshikha Biswas
Raj Kiran

View from the top

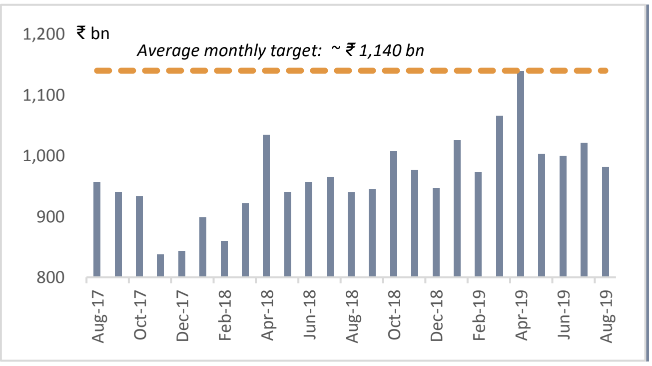
The slowdown is real and there is 'need' to be cautious, but it is 'too early' to press the panic button. Looking at the GDP data, we can infer that the magnitude of slowdown is not as deep as was witnessed during the global financial crisis in 2009 and the debt crisis in 2012. The apprehension to some extent emanates from the revision in forecast. India was forecasted to grow by around 7.8% in FY20 earlier by international agencies. Currently, GDP is now expected to grow by 6.6%-6.8% in FY20 and if we compare this to the 6.8% growth in FY18, it does not indicate a major slowdown from last year. Moreover, the real GDP growth of 5.0% in Q1 FY20 comes over the high base as GDP grew by 8% during Q1 FY19. Earlier, when GDP had recorded a high growth of 9.4% in Q1 FY17, it had slowed down to 6.0% in Q1 FY18.

Most worrying is that the Capital Goods (indicator for future investment) sector under Index of Industrial Production has declined by 4.5% during Nov 18 – Jul 19 as compared to 8.6% growth during Nov 17 – Oct 18. Concerns are more related to investment demand as Gross Fixed Capital Formation (GFCF) grew by just 3.8% during Jan 19 – Jun 19 (first six months of 2019) as compared to 12.5% during Jan 18 -Jun 18. Although, bank credit growth is picking up, it is not broad based. Micro and small segment remains at a disadvantage. Moreover, bank credit to exporters under priority sector recorded a negative growth consistently since Apr 17 to Jul 19 prompting the government to announce measures like revising the priority sector lending (PSL) norms for export credit which will lead to release of an additional funding of Rs 360 bn to Rs 680 bn. The issues at the sectoral level differ across sectors which makes the task of the government somewhat difficult.

Taking stock of the various ongoing and emerging challenges, globally and domestically, it is highly likely that the slowdown will last longer than anticipated. We expect the economy to start recovering from late FY20, as the funding constraints ease further with the RBI's recent measures to strengthen the transmission channels and the various measures taken by the government to address the issues from both short term and long-term perspective. The spate of measures taken by the government including reducing the corporate tax rates is expected to revive the corporate sentiment and provide an impetus to the corporate to kick-start their capex plans.

However, we expect the government to consider the following measures. Further rationalization of GST so that it does not block the capital. Imparting some degree of flexibility and time frame to the corporate sector to prepare and adopt the new rules and regulations and take stringent actions only when there is violation of law. Spending more on infrastructure and on increasing efficiency of capital utilization. The ICOR levels, i.e. investment efficiency after falling through the years since FY15 have inched close to 5% in FY19. Thrust in infrastructure and employment generating sectors and following through the measures outlined to increase farmer's income and agriculture exports. India will need to generate not only more jobs, but also high paying jobs.

GST Revenue collection trailing target for FY20

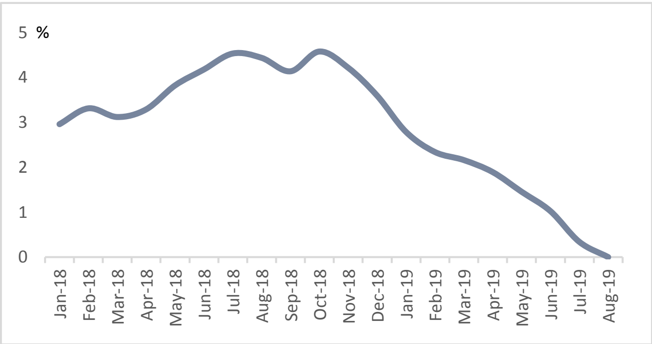


Source: PIB

Real Sector

- Growth in Gross Domestic Product (GDP) moderated to 5.0% during Q1 FY20, lowest in 25 quarters. Private Final Consumption Expenditure grew by 3.1%, slowest in 18 quarters.
- Growth in Gross Value Added (GVA) moderated to 4.9% during Q1 FY20, lowest in 21 quarters. Barring Q4 FY19, growth in agricultural value added is the lowest since Q1 FY17. The services sector grew by 6.9%, slowest in 7 quarters.
- During Q1 FY19, growth in Industrial value added moderated to 2.7% while manufacturing sector grew by 0.6% - both lowest in 8 quarters.
- The Index of Industrial Production (IIP) increased by 4.3% in Jul 19, compared to 3.0% in Q1 FY20. Manufacturing output increased by 4.2% in Jul 19 compared to 2.4% in Q1 FY20.
- Output in the capital goods sector declined for the 7th consecutive month. Infrastructure/ construction goods sector grew by 2.1% in Jul 19 compared to -0.3% in Q1 FY20.

Moderating manufacturing inflation signals weak pricing power

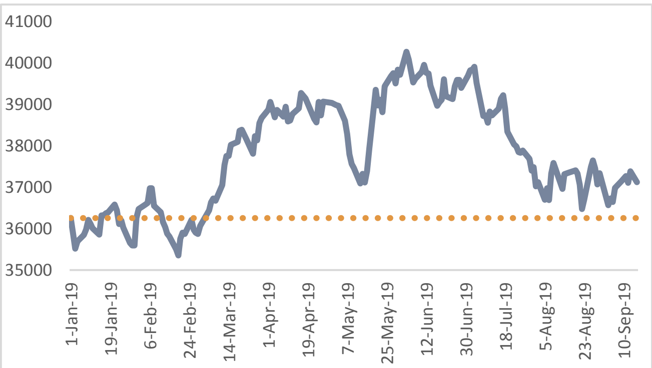


Source: Ministry of Commerce & Industry

Price Scenario

- WPI inflation remain unchanged at 1.1% in Aug 19 compared to Jul 19. Build-up inflation rate in the financial year so far was 1.3% compared to a build-up rate of 3.3% in the corresponding period of the previous year.
- Food inflation increased to 7.7% in Aug 19, highest since Aug 16, due to an increase in prices of eggs, meat & fish. Inflation in fruits increased to 19.7%, highest since Sep 14.
- Inflation in the fuel & power segment contracted by 4.0% in Aug 19, lowest since Sep 16. Crude petroleum inflation contracted for the 4th consecutive month.
- Manufacturing inflation showed nil growth. Core WPI inflation contracted by 0.6% in Aug 19, lowest since Sep 16.
- Retail inflation increased marginally to 3.2% in Aug 19 from 3.1% in Jul 19. Inflation in vegetables increased sharply to 6.9% from 2.8% during the same period.
- Rural inflation in both health and education remain elevated at 9.5% and 8.7% respectively.

Sensex erases nearly all gains since Jan 1, 2019

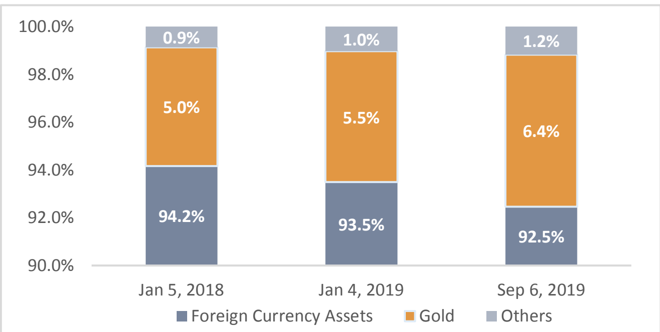


Source: BSE

Money & Finance

- Bank credit grew by 10.2% during Aug 19 compared to 14.2% in Aug 18. Aggregate deposits grew by 9.7% compared to 9.9% during the same period. Bank credit-to-deposit ratio stood at 75.7% in Aug 19, lowest since Sep 18.
- Bank credit to iron & steel industry and textile industry continued to contract for the 15th and 8th consecutive month, respectively. Bank credit to construction industry moderated to 5.8% in Aug 19, lowest since Mar 18.
- Growth in bank credit to micro & small sector moderated for the 3rd consecutive month and stood at 7.8% in Jul 19. Bank credit to export sector continued to contract for the 28th consecutive month.
- Net investments in mutual funds stood at Rs 677.2 bn in Aug 19. The equities segment witnessed net inflows of Rs 174.1 bn, highest since Nov 18.
- The RBI in its liquidity operations absorbed Rs 29.1 tn in Aug 19, highest since Apr 17.
- Weighted average call money rate stood at 5.38% in Aug 19, lowest since Sep 10.

Steady accretion of Gold in Forex Reserves



Source: RBI

External Sector

- Merchandise exports declined by 6.0% to US$ 26.1 bn in Aug 19, while imports declined by 13.4% to US$ 39.6 bn. The pace of decline in imports in the highest in 3 years.
- Oil imports declined by 8.9% to US$ 10.9 bn in Aug 19 from US$ 11.9 bn in Aug 18.
- Brent crude oil price rose sharply to US$ 68.42 on Sep 16, 2019 from US$ 61.25 on Sep 13, 2019, caused by supply disruptions in Saudi Arabia following the drone strikes.
- The average exchange rate of the rupee stood at 71.15 per US$ in Aug 19, highest in 6 months.
- Average inter-bank forward premia stood at 3.95% in Aug 19, lowest since Sep 11.
- There was a net outflow of US$ 0.85 bn in Foreign Institutional Investments during Aug 19, highest in 10 months. Equities segment witnessed outflows of around US$ 2.5 bn while the debt segment witnessed inflows of around US$ 1.6 bn.

Dun & Bradstreet's Macro Economic Forecasts

Variables	Forecast	Latest Period	D&B's Comments
I.I.P Growth	4.0% -4.5% Aug-19	4.30% Jul-19	The initiatives taken by the RBI for policy rate transmission and the various measures announced by the government is expected to boost the corporate sentiment and ease some of the issues faced by the various sectors. With floods affecting many states, rural demand is likely to remain impacted in the near term. However, a pick-up in the industrial production will only be gradual and an uptick is expected to be visible during the festive months of Sept and Oct 2019. D&B expects Index of Industrial Production (IIP) to have grown by 4.0-4.5% during Aug-19.
Real GVA Growth	Q2 FY20(F) 5.9%	Q1 FY20(P) 4.9%	
Inflation W.P.I	0.8% - 1.0% Sep-19	1.08% Aug-19	As expected, food prices have started edging up with inflation in vegetables and pulses inching close to 7%. The sudden spike in oil prices will now impart upward inflationary pressures. However, low commodity prices globally, weak demand and subdued economic activity will help in keeping the inflation rate within the RBI's target range. D&B expects the CPI inflation to remain at 3.7%-3.9% and WPI inflation to be in the range of 0.8% - 1.0% during Sep 19, respectively.
Inflation C.P.I (Combined)	3.7% - 3.9% Sep-19	3.21% Aug-19	
15-91 days T-Bills	5.2% - 5.4% Sep-19	5.36% Aug-19	RBI's initiative to link the bank lending rates to external benchmark rates such as repo rate, treasury bills etc. is expected to improve the monetary transmission and keep interest rates low. The monetary easing taking place globally with the Fed reducing the rates for the 2nd time in 2019 will keep the bond yields low. Out of the budgeted Rs 7.1 tn, the government has already borrowed Rs 5.4 tn putting less pressures on borrowing during the H2 FY20. This along with more than expected transfer of funds by the RBI is expected to lower concerns on fiscal stimulus spending and keep the yields benign. D&B expects 15-91-day T-Bill yield to average at around 5.2%-5.4% and 10-year G-sec yield at around 6.4%-6.6% during Sep-19.
10-year G-Sec Yield	6.4% - 6.6% Sep-19	6.62% Aug-19	
Bank Credit*	9.5%-10.0% Sep-19	10.25% Aug-19	
Exchange Rate INR v/s US$	71.6 - 71.8 Sep-19	71.15 Aug-19	Rupee is likely to remain under pressure amidst trade tensions, geopolitical risks including the current oil price hike, risks of no-deal Brexit, strengthening of dollar and FII outflows. Domestically, dismal corporate earnings and weak domestic growth would also weigh upon rupee. D&B expects the rupee to depreciate further from the previous month to 71.6-71.8 per US$ during Sep-19.

All figures are monthly average

* Refers to End Period

Towards an investment led growth phase

The Indian economy is currently undergoing a downturn. How long the slowdown will last will depend on the underlying trends i.e. the slowdown in consumption since 2019 which started recently and the long-term slowdown in the investment rate. During the different phases of growth, an economy is either driven by consumption or led by investment. Mapping the GDP growth with the different phases of consumption and investment growth, it is evident that the Indian economy in the past few years has been driven by consumption. The resiliency in the consumption demand had helped the economy withstand the impact of the global shocks. However, more worrying is the long-term slowdown in the investment rate which has added to the growing concerns about the pace of revival in the economy. An understanding of the factors which is driving the consumption and investment growth cycle will help in deciphering the extent and pace of revival in the growth momentum and the extent to which the current measures taken by the government will support the economy.

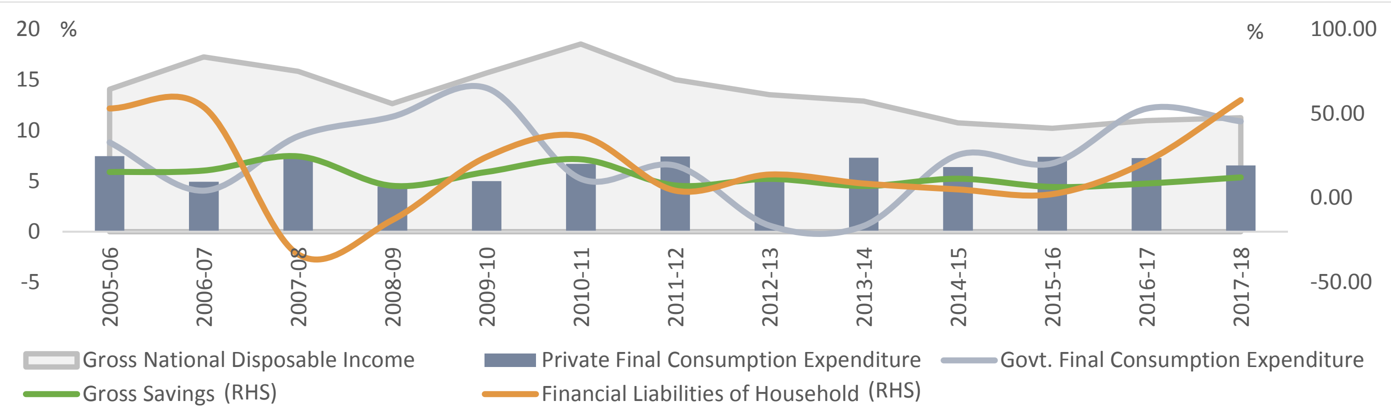
The current consumption growth phase during FY13 to FY17 has been accompanied by dip in savings, rise in household borrowings, low inflation and limited capacity creation. This was different from the previous growth phase of FY07 to FY12, where consumption grew at a lower rate, savings rate was higher, inflation rate was high and investment rate also remained high.

Per capita consumption grew at an average rate of 5.7% during the phase FY13-FY17, higher than the average growth of 4.5% during FY07-FY12. Average WPI inflation stood at 2.3% between FY13-FY17 compared to 6.9% during FY07-12. Gross savings rate grew at an average of 9.0% during FY13-FY17, a marked slowdown from the average growth of 15.6% during FY07 to FY12. During FY13 to FY17, the increase in household debt/liabilities pose concerns. During FY17, household liabilities were 1.4 the level in FY13, whereas household disposable income in FY17 was 1.5 times the level in FY13. During FY18, household liabilities/borrowings as a percentage to disposable income were a 11-year high of 4.3%. The increase in household borrowings without an adequate increase in income and a dip in savings indicated that expenditure was increasingly funded by savings.

In terms of Investment, capacity creation also slowed down; average Gross Fixed Capital Formation (GFCF) grew by 4.9% between FY13-17, much lower than the growth of 10.7% during FY07 to FY12. Research shows that consumption led growth tends to be followed by weaker growth if it is accompanied by limited capacity creation and borrowed consumption. In fact, consumption led growth has a negative impact on gross value-added growth one-year ahead by 1.39 percentage points. After reaching a peak during FY17 consumption slowed down and led to the slowdown in the growth momentum. Data shows that GVA growth fell by around 1.3 percentage points to 6.6% in FY19 from 7.9% in FY17.

The long-term slowdown in the investment rate has added to the growing concerns about the current slowdown. Investment rate has been slowing down since FY13. The slowdown in investment is accompanied not just by the cyclical component of the investment growth cycle, but the trend component of the cycle has been slowing down since FY12 and more significantly since FY15. Uncertain global environment, highly leveraged corporate sector and sluggish credit offtake from the banking system had impacted the investment activity. Further, the low business optimism, low returns on investment by the corporate and increase in inefficiency in capital employed, as indicated by increasing incremental capital output (ICOR) ratio, raises concerns over pace of revival in the investment activity. We need not only an increase in the investment momentum but also an upturn in the trend component as that would ensure a sustainable and a higher GDP growth rate. The recent slew of proactive measures taken by the government and the RBI to address the slowdown in consumption and investment from the short term and long-term perspective is expected revive the corporate sentiment and provide an impetus to the corporate to kick-start their capex plans. Moreover, the government's plan to spend US$ 100 tn in infrastructure over the next five years is expected to push the investment trend upwards and drive the transition from consumption led to investment led growth over the few years.

Increase in financial liabilities of household and fall in savings indicate that expenditure is increasingly funded by borrowings



Source: MOSPI, RBI

Please send your feedback to Dr Arun Singh, Chief Economist.
Dun & Bradstreet Information Services India Pvt. Ltd., ICC Chambers, Saki Vihar Road, Powai, Mumbai 400 072. CIN - U74140MH1997PTC107813
Tel: 91-22-4941 6666 | Email: SinghArun@DNB.com | www.dnb.co.in