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INDIAN ECONOMY

CRISIL Insights

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Through the monthly CRISIL Insights Indian Economy series, we offer incisive analysis of macroeconomic parameters of the country. In this issue, we give an outlook on GDP growth in fiscal 2020 and outline key drivers

Home, quite alone

The global growth momentum is expected to soften in 2019, with growth slowing in major advanced economies including the United States (US), Europe and China. Moreover, risks are tilted to the downside. With weak global environment, India will have to lean on domestic factors. And consequent to the government pursuing a fiscal consolidation path, the pickup in growth is expected to be only gradual. A change in the growth mix is on cards, with the private sector likely to take over the baton from the government.

In fiscal 2020, CRISIL expects gross domestic product (GDP) to grow 7.3%, compared with 7.2% in fiscal 2019, under the assumptions of normal rains, lower crude oil prices than in 2018 and a stable political outcome. Private consumption and investment are expected to be the key drivers of India's growth in fiscal 2020. Private consumption growth is likely to find support from softer interest rates and improvement in farm realization, as food inflation moves up. Plus, the lower base effect will help. Investment, especially from the private corporate, will improve, given the continuously improving capacity utilization and the end of the de-leveraging phase for corporates.

However, the risks to our growth forecast are tilted to the downside: (a) monsoon risk – if 2019 happens to witness El Nino, as forecasted by the National Oceanic and Atmospheric Administration of US, the agriculture GDP could erode and rural distress could accentuate; (b) political risk - if the general elections this year were to yield a fractured mandate and derail/delay the reforms process, the implications on sentiments, investments and growth could be adverse; (c) oil price risk – if crude oil prices were to spike and stay high through the fiscal, India's manufacturers could face input price pressures; (d) weaker global outlook – if the global slowdown is more than expected, then global demand and trade growth could severely slowdown, creating adverse consequences for India's exports.

As for the other key macros, we expect the Consumer Price Index (CPI)-based inflation to pick up to 4.5% in fiscal 2020, compared with an estimated 3.7% in fiscal 2019. While fuel inflation will be benign, pressure from food and core inflation is expected to weigh on the headline inflation. Current account deficit (CAD) is expected to reduce to 2.4% of GDP in fiscal 2020 from 2.6% in fiscal 2019, supported by lower crude oil prices.

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Money and Banking	Industrial Production	Inflation
Softer rates	IIP growth slumps	Inflation downtrend

MONEY AND BANKING

- Despite slowing inflation, the Reserve Bank of India's (RBI) Monetary Policy Committee (MPC) held the policy rate and stance in its latest policy meet. The MPC's decision was based on the need to monitor the evolving situation on the inflation front and support liquidity in the system, which has come under pressure in past few months
- Even as the MPC kept policy rates on hold, both long- and short-term interest rates softened
- Systemic liquidity however, tightened further. The RBI continued open market operations to address tighter systemic liquidity
- Banking credit continued to register double-digit growth, increasing 15.1% on-year as on December 21, 2018, at the same pace as on November 30, 2018. However, with industrial credit growth marginal, the banking credit growth is not broad-based
- CRISIL Research expects banking credit to clock upwards of 11% on-year growth this fiscal, compared with 7.4% in fiscal 2018, driven by strong retail credit growth, higher disbursement to non-banks, and resolution of big-ticket stressed assets

INDUSTRIAL PRODUCTION

- Index of Industrial Production (IIP) growth fell to 0.5% in November, down from 8.4% in October, primarily due to high-base effect. The plunge was driven by manufacturing, where growth turned negative to -0.4% from 8.2%, while electricity growth halved over October
- Within manufacturing, there was a near across-the-board de-growth in capital, intermediate and consumer goods segments
- Despite the big decline, industrial production has fared much better this fiscal, Apr-Nov, (5% average growth) compared with last (3.2%)
- November growth is a blip and IIP growth should improve in the coming months with GDP growth estimates for fiscal 2019 forecast showing industry growing robustly, led by manufacturing and construction

INFLATION

- Consumer Price Index (CPI)-based inflation fell to an 18-month low of 2.19% in December on negative food inflation and softening fuel inflation, besides a high base of the previous year
- Food inflation has been negative since October and has been the major factor behind the decline in headline inflation. Sans food, inflation continues to remain above 5.0%
- Fuel inflation also moved down sharply, given a significant downward movement in domestic petrol and diesel prices
- Wholesale Price Index (WPI)-based inflation too slowed down in December, recording 3.8% in December, down from 4.6% in November
- For fiscal 2019, CRISIL forecast CPI inflation at 3.7%, compared with 3.6% in fiscal 2018, given the continuous and sharp decline in food prices and slowdown in international crude oil prices
- In fiscal 2020, however, inflation may see some upside as food inflation might move up if the monsoons this year are inadequate, some global indicators are already pointing to higher food inflation in 2019 and core inflation moves up on factors such as implementation of Pay Commission hikes by more states and populist measures such as farm loan waivers. Accordingly, CRISIL pegs fiscal 2020 CPI inflation at 4.5%

Interest Rate	Rupee	Trade
End of tumult	Rupee firm as 2018 ends	Trade deficit relief

INTEREST RATE

- Yield on the 10-year government security (G-sec) averaged 7.4% in December, 34 bps lower on-month, but 22 bps higher on-year
- Even as large-scale open market purchases by the RBI are shoring up demand for G-secs, the macroeconomic environment is lending the bond market a helping hand
- Falling oil prices and US Treasury yields on the external front and a stable repo rate and low inflation on the domestic front are supporting yields
- After a tumultuous year for the Indian debt market, the 10-year G-sec yields ended 2018 at the level where they started. They were on a rising trend for most of the year, and even crossed 8%, a level not seen in the past four years
- CRISIL expects the 10-year G-sec yield to settle at 7.5% by fiscal 2020-end compared with 7.7% in fiscal 2019-end

RUPEE

- Rupee continued to recover in December for the second straight month, gaining 1.6% on-month to average 70.7/$, buoyed by falling crude oil prices and modest net foreign portfolio investment
- The sharp fall in crude prices boosted inflows by foreign portfolio investors (FPIs). FPIs net-invested a modest $1.1 billion, mostly in the debt market. In addition, the US Federal Reserve lowering the federal funds rate hike projection to two (from three) and improved risk appetite for emerging market currencies, supported the rupee
- CRISIL believes the rupee will settle at ~71/$ by fiscal-end, compared with 65/$ in March 2018, supported by easing crude prices and slower-than-expected pace of future rate hikes by the US Fed. However, there is downside risk from widening CAD – 2.6% of GDP this fiscal compared with 1.9% in fiscal 2018 – and tighter global monetary conditions, have been partially offset by the steep fall in crude prices in recent months
- For fiscal 2020, low oil prices, which keep external vulnerability at check, and slowing pace of policy normalization in the US, which would mean lesser interest rate arbitrage, are expected to keep rupee depreciation in check. Therefore, CRISIL expects the rupee to average at 72/$ by March 2020

TRADE

- Merchandise export growth slowed to 0.4% on-year in December from 0.8% the previous month, led by a slowdown in global growth
- Imports contracted 2.4%, compared with 4.3% growth, dragged down by gold
- Consequently, trade deficit narrowed in December by $3.6 billion on-month to $13.1 billion as both oil and non-oil deficit eased
- In Q3 of fiscal 2019, exports grew 5.7% on-year, slower than 10% the previous quarter. Import growth, too, was lower at 6.1% compared with 21.1%
- Services export growth slowed to 8.3% on-year in November compared with 18.8% in October, while import growth slowed to 4.8% from 16.1%

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