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GDP GROWTH RECOVERS SIGNIFICANTLY

As expected, Gross Value Added accelerated to 6.7% in Q3 FY18 as against 6.2% in Q2. GDP growth printed at 7.2% as against revised 6.5% in Q2. Nominal GDP expanded by 11.9% (10% in Q2).

The good thing is that in the last couple of quarters the GVA had increased due to lower GVA deflator but in Q3, deflator and GDP both have accelerated indicating that economy is firmly on the mend. However, the surprising part is the decline in deflator estimates in Q4 in all sectors. This may impart an element of downward bias in Q4 estimates.

CSO has revised upwards FY17 GVA numbers by 46 bps (average) to 7.1% with Q1 revised upwards by 71 bps and Q2 by 47 bps. Interestingly, while Q3 FY17 GVA was revised upwards, the concomitant GDP numbers were revised downwards. This may be one of the reasons for strong GDP numbers in Q3. Nevertheless, growth seems to have now reached the levels of Q1FY17, the break point from when growth had dipped.

There were 2 numbers that surprised in the GDP narrative.

First, Agriculture and Allied Activities grew at 4.1% in Q3 (7.5%). For FY18 also, Agriculture is likely to show a growth rate of 3.0% in its GVA in FY18, as against the previous year's growth rate of 6.3%, largely reflecting a robust performance of non-foodgrain component.

Second, the growth in construction sector in Q3 has now touched a 24 quarter high. This will augur well for job creation as it shows that the Government efforts in heavy lifting in investment activities in rural areas and the push to affordable housing is finally bearing fruit.

The narrative of decline in overall investment due to decline in capex may not be fully correct. The data for previous years show share of household sector in GFCF has declined to 31.8% in FY17 compared to 40.1% in FY15 and 32.1% in FY16. In general some revival in capital formation that was visible in January press release appears to be continuing, but at a slightly moderate rate. This is primarily in unorganized manufacturing. However, household capital formation in dwellings has not recovered even in FY18 thus limiting a full scale revival in capital formation.

The Q4 GVA growth derived from annual and three quarters comes out to be 6.9%. We believe this will largely depend upon few factors. Now the GST has stablised and this will have positive impact on trade, hotel, transport, communication sector.

GDP GROWTH ACCLERATES

- As expected, Gross Value Added accelerated to 6.7% in Q3 FY18 as against 6.2% in Q2, owing to smart growth in Manufacturing (8.1%) and Trade, Hotel, Transport, Communication sub segment (9.0%). GDP growth increased to 7.2% in Q3 from 6.5% in Q2 FY17, while the nominal GDP grew by 11.9% (Q2: 10.0%). In the last couple of quarters the GVA had increased due to lower GVA deflator but in Q3 deflator and GDP both have accelerated indicating that economy is on the mend.
- For FY18, CSO anticipated GVA growth at 6.4% in FY18 compared to 7.1% growth in FY17. Real GDP is estimated at 6.6% as compared to the growth rate of 7.1% in FY17.
- CSO has revised upwards FY17 GVA numbers by 46 bps (average) to 7.1% with Q1 revised upwards by 71 bps and Q2 by 47 bps. Interestingly, while Q3 FY17 GVA was revised upwards, the concomitant GDP numbers were revised downwards. This may be one of the reasons for strong GDP numbers in Q3. Nevertheless, growth is firmly on the mend.
- Agriculture and Allied Activities grew at 4.1% in Q3, compared to last year's growth of 7.5%. For FY18 also, Agriculture is likely to show a growth rate of 3.0% in its GVA in FY18, as against the previous year's growth rate of 6.3%, largely reflecting a robust performance of non-foodgrain component.
- Industry sector growth accelerated sharply to 6.8% in Q3 from 5.9% in Q2, due to higher growth in all sub-sectors barring mining. The 8.1% growth in Manufacturing GVA in Q3 is quite consistent with the smart growth in Corporate GVA (defined as sum of PBIDT and Wages/Salaries) as both of these are strongly positively correlated. The Corporate GVA which decelerated since Q3 FY17 rebounded in Q2 FY18 and exhibited positive growth of 11.3% in Q3 (based on the data of 3423 non-financial companies).

GDP Growth Rate (yoy %) at Constant Prices (Base: 2011-12)

Particulars	FY18					FY17					Deflator (FY18)			
	Annual	Q4 (P)	Q3	Q2	Q1	Annual	Q4 (P)	Q3	Q2	Q1	Q1	Q2	Q3	Q4 (P)
1. Agriculture, forestry & fishing	**3.0**	**1.9**	**4.1**	**2.7**	**2.7**	**6.3**	**7.1**	**7.5**	**5.5**	**4.3**	-2.3	1.6	3.6	1.0
2. Industry	4.8	6.6	6.8	5.9	0.1	6.8	5.0	7.1	6.8	8.3	3.2	2.6	3.5	3.0
2.1 Mining & quarrying	3.0	3.9	-0.1	7.1	1.8	13.0	18.8	12.1	9.1	10.5	11.4	7.7	11.9	8.9
2.2 Manufacturing	5.1	7.2	8.1	6.9	-1.8	7.9	6.1	8.1	7.7	9.9	2.7	2.5	2.6	2.6
2.3 Electricity, gas, water supply & other utility services	7.3	8.4	6.1	7.7	7.1	9.2	8.1	9.5	7.1	12.4	0.7	-0.3	-0.4	-2.1
2.4 Construction	4.3	6.1	6.8	2.8	1.5	1.3	-3.9	2.8	3.8	3.0	2.3	2.7	3.7	2.9
3. Services	**8.3**	**8.7**	**7.7**	**7.1**	**9.6**	**7.5**	**6.3**	**6.5**	**7.9**	**9.4**	3.2	3.4	4.3	3.8
3.1. Trade, hotels, transport, communication & services related to broadcasting	8.3	6.7	9.0	9.3	8.4	7.2	5.5	7.5	7.2	8.9	2.9	3.1	4.1	3.3
3.2. Financing, insurance, real estate & bus. Services	7.2	6.6	6.7	6.4	8.9	6.0	1.0	2.8	8.3	10.5	3.1	3.6	4.5	3.6
3.3. Public administration, defence & other services	10.1	15.0	7.2	5.6	13.2	10.7	16.4	10.6	8.0	7.7	3.3	3.6	4.4	4.1
Total GVA at Basic Prices	**6.4**	**6.9**	**6.7**	**6.2**	**5.6**	**7.1**	**6.0**	**6.9**	**7.2**	**8.3**	2.3	2.8	3.8	3.0
GDP	**6.6**	7.1	7.2	6.5	5.7	**7.1**	**6.1**	**6.8**	**7.6**	**8.1**	3.3	3.4	4.4	1.0

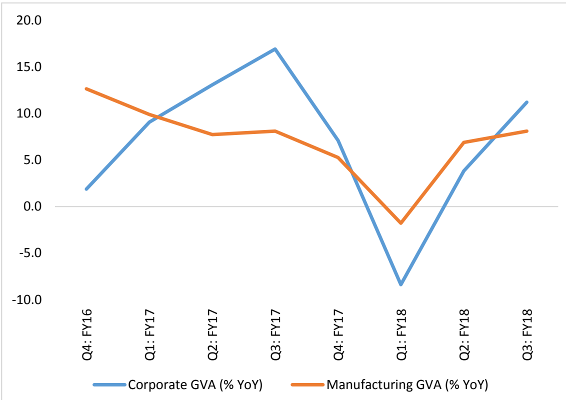
Source: CSO & SBI Research

Economic Growth: New vs. Old (%)

Quarter		GVA			GDP		
		Old	New	Change in bps	Old	New	Change in bps
FY16	Q1	7.6	7.8	0.21	7.6	7.8	0.25
	Q2	8.2	8.4	0.22	8.0	8.1	0.08
	Q3	7.3	7.3	0.03	7.2	7.1	-0.10
	Q4	8.7	8.7	0.08	9.1	9.1	-0.02
FY17	Q1	7.6	8.3	0.71	7.9	8.1	0.18
	Q2	6.8	7.2	0.47	7.5	7.6	0.09
	Q3	6.7	6.9	0.24	7.0	6.8	-0.20
	Q4	5.6	6.0	0.44	6.1	6.1	-0.03
FY18	Q1	5.6	5.6	0.02	5.7	5.7	-0.05
	Q2	6.1	6.2	0.16	6.3	6.5	0.19
	Q3	…	6.7	…	…	7.2	…
	Q4	…	6.9	…	…	7.1	…

Source: CSO, SBI Research

Graph 1: Corporate GVA & Manufacturing GVA (% YoY)



Source: CSO, SBI Research

- The negative growth (0.1%) in Mining & Quarrying during Q3 (compared to 7.1% in Q2 FY18 and 12.1% in Q3 FY17) is primarily due to base effect. Construction sector grew by 6.8% in Q3 FY18 (highest in the new series) compared to Q1 as consumption of finished steel registered growth rates of 5.2%.
- Service sector grew at a better pace of 8.3% in FY18 compared to 7.5% in FY17, driven by growth in 'Trade, hotels, Transport, Communication and Services' at 8.3% (7.2%) and 'Financial, Real estate & Professional Services' at 7.2% (6.0%). Despite a pick-up in credit growth during Non-Dec'17, the growth in 'Financial, Real estate & professional services' has declined significantly to 6.7% in Q3, compared to 8.9% in Q1. This may be due to the larger share (72%) of real estate and professional services in the 'Financial, Real estate & Professional services' sector. The real estate and professional services sector may have declined due to the implementation of GST and RERA, but this may be a short term phenomenon.
- On the expenditure side, GFCF has registered 12.0% yoy growth in Q3FY18 compared to 6.9% yoy growth in the previous quarter. For FY18 GFCF is however expected to register a growth rate of 9.7% at current prices and 7.6% at constant prices during FY18. this indicates investment revival will take some more time.
- The narrative of decline in overall investment due to decline in capex may not be fully correct. The data for previous years show that the share of private non-financial corporate sector in GFCF has increased to 42.2% in FY17 compared to 35.9% in FY15 and 41.1% in FY16. Meanwhile, share of household sector in GFCF has declined to 31.8% in FY17 compared to 40.1% in FY15 and 32.1% in FY16. Household investment in dwellings and real estate has declined while that in machinery and equipment has increased from the past few years.

GOING FORWARD

- The annual GDP estimates in the latest CSO data show that overall growth has/will moderate by 50 bps in FY18. Reasons for the moderation include slowdown in growth across all sectors except transport services and construction which have increased, possibly due to the impact of GST transition. Another reason which has caused moderation in the growth rate is the steep rise in imports at current prices by 13% owing to rise in crude oil prices but not matched by corresponding increase in export growth rates.
- The private final consumption expenditure has also moderated, indicating buildup of inflation pressure and if the trends continue there will be pressure on the GST revenue collections. In general some revival in capital formation that was visible in January press release appears to be continuing, but at a slightly moderate rate. This is primarily in unorganized manufacturing. However, household capital formation in dwellings has not recovered even in FY18 thus limiting a full scale revival in capital formation.
- The Q4 GVA growth derived from annual and three quarters comes out to be 6.9%. We believe that this will largely depend upon few factors. Now the GST has stablised and this will have positive impact on trade, hotel, transport, communication sector.
- Based on the 2nd AE numbers of FY18, it is estimated that the services will grow by 8.7%, with highest contribution from 'public administration & defence' sector.

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ABOUT US

The Economic Research Department (ERD) in SBI Corporate Centre is the successor to the Economic and Statistical Research Department (E&SRD). The latter came into being in 1956, immediately after the State Bank of India was formed, with the objective of "tendering technical advice to the management on economic and financial problems in which the Bank has interest and which required expert analysis".

After the first reorganization of the Bank, when specialized departments like Management Science, Management Information Systems, Planning and Market Segment Departments took over the statistical work of E&SRD, the Department was renamed as ERD.

However, with the ERD team now taking on multidimensional functionalities in the area of risk management , corporate analytics, strategy and so on, who knows, the time may have come to rename it again!

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