The Indian economy grew by 13.5% in Q1 FY23 with the services sector showing a strong rebound. The GVA grew by 12.7%. Though GDP grew in double digits but still it came way below the market expectations. The primary culprit was the growth in manufacturing sector which grew by a measly 4.3% in Q1.

We strongly believe that the estimation of manufacturing sector growth needs serious introspection in the sense that IIP is still indexed at 2012 base. The CPI basket has also not changed since 2012 and this has also possibly resulted in overstating CPI inflation at multiple times. Take the example of manufacturing exports. Till pre pandemic, the IIP and manufacturing exports have moved in close tandem, but they have completely diverged post pandemic. This is because, with India announcing a lot of incentives under the PLI scheme, there has been an exponential jump in manufacturing exports from India, like handset exports that are not a part of IIP basket, for example Foxcon. Separately, the steel production by select companies has undergone locational shift which are not a part of the IIP sample. Nokia’s handset manufacturing facility at Chennai has closed down post 2014. There are many such examples. This has meant that the correlation between manufacturing exports and IIP growth post pandemic is weak. A logical corollary to all this is gross misappropriation (or underestimation) of manufacturing sector growth. We believe that the new base of IIP (on which the Government is currently working) will remove these glitches to have a fair representation.

Global tech major Apple’s recent decision to shift part production of its flagship iPhone 14 model for worldwide shipping from India, with a negligible time lag of a few weeks post its slated launch on September 7, bears testimony to further optimism! The move by Apple, the most recognisable face of tech infused innovation in the last two centuries, that captures aspirations of an upwardly mobile population should open the flood gates for other major conglomerates to follow suit.

The lower growth in manufacturing sector is also a reflection of pandemic induced uncertainties that seems to have impacted the margins.

On the expenditure side the picture has improved considerably. The private consumption has improved on the back of good urban demand with growth of 25.9%. Urban demand is getting support from contact-intensive services while rural demand has not responded to robust agriculture output growth. Gross fixed capital formation registered a growth of 20.1%. The new project announcements by the private sector in June 2022 as per Centre for Monitoring Indian economy (CMIE) data also rose to 117% of the pre-covid level (June 2019) suggesting healthy momentum.

Nominal GDP growth came at 26.7% yoy in Q1 FY23 compared to 32.4% in Q1 FY22 and 14.9% in Q4 FY22, with the share of private final consumption expenditure increasing in overall growth. Its weighted contribution has increased to 21.9% in Q1 FY23 from 7.5% in Q4 FY22 and 14.2% in Q1 FY22, thereby revealing its relative importance in GDP growth. Notably, private final consumption expenditure in real terms had improved to 10% above the pre-pandemic level in Q1 FY23.

Under alternative model specifications, we are now revising our annual GDP growth for FY23 to 6.8%, a large part of which is a statistical adjustment with growth momentum likely to show an increasing momentum in second half of current fiscal. The downward revision is mostly to do with our Q1 GDP estimate that was at 15.7%.

The lower growth in Q1 also compounds RBI’s job, with rate hike trajectory in next two MPC meets trying to find a neutral ground amidst growth and inflation. A lot should depend on emerging inflation prints locally, but if the message from Jackson Hole summit is a harbinger, US seems bracing for further hardening at elevated pace, with Fed chair also questioning the sustainability of growth and job markets going head, whose robustness has shielded the economy largely, of late. On the other hand, Eurozone seems to enter a conflict zone, accentuated by political melodrama in select jurisdictions, even as inflation promises to further spiral up with Russia likely to squeeze gas supply during ensuing winter to exert a tacit pressure on the block. Clearly, a fine balancing act by RBI would be on the anvil, keeping the rupee closer than ever to the centre.
GDP EXPANDS BY 13.5% IN Q1 FY23

- India’s economy grew by 13.5% in Q1 FY23 on the back of buoyant growth in services sector. The GVA grew by 12.7%. Though GDP grew in double digits but it was way below the market expectations. The main culprit is the manufacturing sector which grew by merely 4.8% in Q1.
- The lower growth in manufacturing sector is a reflection of pandemic induced uncertainties that seems to impacted the margins. Profit growth has also slowed down in Q1FY23. Corporate results, ex BFSI, for Q1FY23 shows lower EBIDTA growth of 7% yoy against significant EBIDTA growth in Q1 FY22 (which was mainly due to base effect). This shows the volatility in numbers when compared to post covid quarters on a yoy basis.
- Net sales grew by 51% in Q1FY23 while PAT grew by 11% on a yoy basis while on a sequential basis net sales grew by only 7% while PAT was down by 25%.
- Further, corporate margin seems to be under pressure, as reflected in results of around 3000 listed entities ex BFSI, on account of higher input costs with decreasing EBIDTA margin, on aggregate basis, from 17.65% in Q1FY22 to 12.51% in Q1FY23.
- Agriculture, the most consistent sector since pandemic, grew by 4.5% in Q1. Construction activity witnessed boom in Q1 and grew by 16.8%. Our assessment (based on new launches and sale) indicate that it will remain buoyant in the Q2 also.
- Services sector grew by 17.6% due to more than 25% growth in ‘Trade, hotels, transport, communication & services related to broadcasting’ and ‘Public administration, defence and Other Services’. ‘Financial, real estate & professional service’ is the only sector which grew by 9.2% despite very low base.

TRADE, HOTEL, TRANSPORT STILL NEED TO SURPASS THE PRE-PANDEMIC LEVEL

- The ‘Trade, Hotels, Transport, Communication & Services related to broadcasting’ is the only sector still 15% lower than the pre-pandemic level (i.e. Q1 FY20). Despite expanding by whopping 25.7% it is still Rs 1.0 lakh crore less than the FY20 levels. On the expenditure side, both the Private and Government Final Consumption Expenditure crossed the pre-pandemic level by Rs 2.0 lakh crore and 0.36 lakh crore, respectively.
SEASONALLY ADJUSTED SERIES SHOWS IMPROVING SEQUENTIAL MOMENTUM

- Real GDP growth has declined by 9.6% qoq in Q1 FY23. However, the seasonally adjusted real GDP growth series shows pick up in economic momentum, with higher growth at 5.6% qoq in Q1 FY23 compared to -4.1% qoq in Q1 FY22 and 1.9% qoq in Q4 FY22.

- Notably, this is higher than SA qoq growth achieved in all Q1s since FY13. Also, the sequential seasonally adjusted GDP growth is higher than the non-seasonally adjusted GDP growth for Q1 over the past, indicating higher seasonal component in the first quarter of a fiscal year.

NOMINAL GDP GROWTH AT 26.7%

- Nominal GDP growth came at 26.7% yoy in Q1 FY23 compared to 32.4% in Q1 FY22 and 14.9% in Q4 FY22, with the share of private final consumption expenditure increasing in overall growth. Its weighted contribution has increased to 21.9% in Q1 FY23 from 7.5% in Q4 FY22 and 14.2% in Q1 FY22, thereby revealing its relative importance in GDP growth. Notably, private final consumption expenditure in real terms had improved to 10% above the pre-pandemic level in Q1FY22.

- The gap between the nominal GDP growth and the real GDP growth has increased between Q2 FY20 and Q1 FY22 owing to higher inflation. It moderated in Q2 and Q3 FY22 but increased again in the last two quarters.

- The growth in deflator has increased modestly to 11.6% yoy in Q1 FY23 compared to 10.4% in the last quarter of FY22. Growth in GDP deflator for agriculture has increased further to 12.4% yoy compared to 10.7% yoy in Q4 FY22, indicating the persistent impact of higher food prices. For industry growth in deflator has increased mainly on account of mining & quarrying and electricity, gas, water supply & other utility services. Meanwhile for services, GDP deflator declined only in case of public administration, defence and other services.
EXPENDITURE SIDE GDP

- On the expenditure side the picture has improved considerably. The private consumption has improved on the back of good urban demand with growth of 25.9%. Urban demand is getting support from contact-intensive services while rural demand has not responded to robust agriculture output growth.
- Gross fixed capital formation registering a growth of 20.1 percent. The new project announcements by the private sector in June 2022 as per Centre for monitoring Indian economy (CMIE) data also rose to 117% of the pre-covid level (June 2019) suggesting healthy momentum.
- On the external front the outlook is tilted towards the negative side. The real exports growth was 14.7% and the corresponding imports growth was 37.2%. The sharp jump in the imports and corresponding depreciation of rupee has take the net real exports to 8.1% of the GDP. This factor is serious drag on the future outlook and with falling demand in key exports regions, the GDP growth is expected to slow further.

LOW RURAL DEMAND

- FMCG results show tepid demand as rising retail inflation exerted pressure on share of wallet for FMCG. It is natural for consumers, in such inflationary scenarios, to feel the pinch of increased pressure on their wallets and they adjust volumes and prioritize essentials over discretionary spend to manage the household budgets.
- Furthermore, rural growth continues to lag growth in urban markets. Companies are cautiously optimistic that the trends will improve in the coming quarters as the current quarter was impacted by overall rural slowdown and inflationary pressures. We believe, in near term, growth to be price led, inflation to continue impacting consumption till it starts to decline meaningfully.

GDP ESTIMATE FOR FY23

- Our economic activity index that employs a dynamic factor model (DFM) with 41 high frequency indicators is showing a marginal moderation in July. The yearly SBI Composite Index declined and is at 55.1 (High Growth) in August 2022, compared to 56.1 (High Growth) in July 2022. While, the monthly index also declined marginally to 55.5 (High Growth) in August from 55.9 (High Growth) in July 2022.
The banking and financial sector also fared well amidst a pickup in credit growth, lower provisioning costs and improvement in asset quality. Credit growth continues to remain strong and has been consistently rising since February 2022, grew at 15.3% y-o-y as on J12 Aug, 2022 (6.5% a year ago). The incremental growth (YTD) in credit is Rs 5.39 lakh crore (4.5%) till date (degrowth of Rs 0.6 lakh crore last year or −0.6%). It’s clearly evident that the demand for credit is still continuing and may end with more than 12% (YoY) growth in FY23.

The sector-wise credit data for the month of July 2022 indicates that there is a substantial improvement in incremental credit to each and every sector. Specifically, credit growth to MSME sector has expanded by Rs 64,334 crores in current fiscal as against a de-growth of Rs 67,889 crore in similar period previous fiscal. Retail loans expanded by Rs 2.0 lakh crores against Rs 16,768 crore last year. Credit to services sector rebounded and grew by Rs 1.5 lakh crore during Apr-Jul’22.

Under alternative model specifications, GDP growth for Q2:2022-23 would be around 6.2%, supported by a favourable base effect and bumper credit growth but may decline thereafter. With this, we are revising our annual GDP growth for FY23 to 6.8%, a large part of which is a statistical adjustment with growth momentum likely to show an uptick in Q2.
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