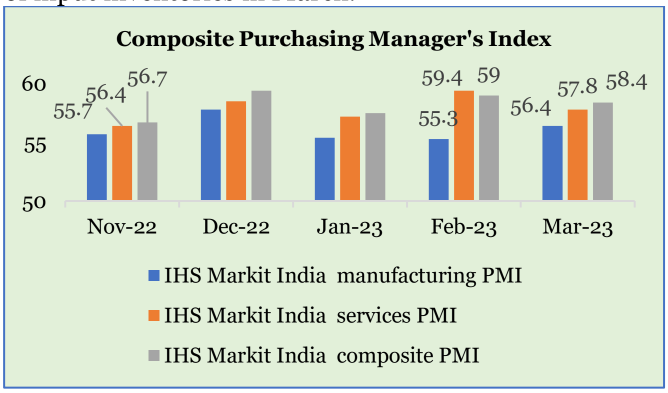
DEAR
ECO THINK
Issue No.67/ April 2023

ECONOMY

India's Manufacturing PMI rises

The seasonally adjusted S&P Global India Manufacturing PMI rose to 56.4 points in March from 55.3 points in February (India Purchasing Managers Index (PMI) tracks the prevailing direction of economic trends in the manufacturing and service sectors) signaling the strongest improvement at the end of the last quarter, as growth of the factory orders and production quickened to the strongest in three months. With pressure on supply chains subsiding and raw material availability improving, input cost inflation retreated to its second-lowest mark in 2 ½ years. Subsequently, goods producers concentrated on rebuilding their stocks. Robust increase in buying levels in recent months supported a near record accumulation of input inventories in March.



Source: CMIE, Economic Outlook

Service providers in India welcomed another upturn at the end of last fiscal quarter. Posting 57.8 points in March, the seasonally adjusted S&P Global India Services PMI Business Activity Index was in growth territory (above 50.0) for the twentieth successive month. Despite falling from 59.4 in February, indicating a slower rate of expansion, the latest figure was consistent with a substantial uptick in output. Favourable demand conditions and new business gains were among the reasons for the latest rise.

IMF lowers India's growth forecast to 5.9%

The IMF lowered its growth forecast for India for the current financial year and the next by 20 bps and 50 bps, to 5.9% and 6.3%, respectively citing lesser scope of pent-up demand due to historical revisions to data. Maintaining that India remains one of the bright spots in the global economy, i.e India did not weather the global turmoil as it was expected to in 2020 and 2021, the forecast was done as there is less to catch up. This will be followed by a very strong economic growth (higher living standards and creation of jobs that are necessary) in next financial year as indicated by IMF.

Growth: RBI MPC, April 2023
The RBI expects rural demand to improve on account of robust Rabi output. On the urban side, the central bank expects demand to hold up with sustained rebound in contact intensive services sector. While the RBI highlighted risks to external demand due to global slowdown, it expects above trend capacity utilisation, government capital spending and easing commodity prices to support investment and manufacturing. The RBI revised up FY24 GDP estimate by 10 bps to 6.5%. On a quarterly basis, while growth projections for Q1 and Q2 were left unchanged, estimates for Q3 and Q4 were revised up marginally (10 bps).

Milk products to be imported after a decade

India's milk production remained stagnant in 2022-23 due to lumpy skin disease in cattle across several states and the lagged effect of Covid-19 in the form of stunting of animals. Despite India being the largest milk producer since 1998 (India contributed 24% of global milk output in 2021-22), the country's milk inflation has been the second biggest element after the high prices of cereals that drove up retail inflation in January and February (9.65%) 2023.

Milk production has been annually growing at 6% since last many years while domestic demand for milk grew by 8-10% last fiscal because of the rebound in post pandemic demand. Mother Dairy and Amul hiked milk prices multiple times in the last one year citing higher fodder cost, robust demand and some impact due to reports of lumpy skin disease.

Noting that the stocks of products such as fats, butter and ghee, etc. lowered than previous year, the government may resort to import of these products.

South-West monsoon rainfall to be normal: IMD

As India is gearing up to tackle the heat wave and El Nino (*El Nino, a naturally occurring phenomenon characterised by the abnormal warming of sea surface temperature in the central and eastern equatorial Pacific Ocean. On average, it occurs every two to seven years and can last up to 18 months)* concerns as far as prospects of kharif crops is concerned, the Indian Meteorological Department (IMD) predicted that the

Prepared by Deblina Patra, AGM and Saad Bin Afroz, Mgr
Editorial team: Dr.K.C.Badatya, CGM, Dr. Vinod Kumar, GM and Dr. Ashutosh Kumar, DGM
Published by Department of Economic Analysis and Research, NABARD Head Office, Mumbai

DEAR
ECO THINK
Issue No.67/ April 2023

South-West monsoon rainfall during June-September is likely to be in the 'normal' range at 96% of the benchmark long-period average (LPA).

(*IMD classifies 'normal' rainfall between 96% and 104% of LPA. Rainfall between 90%-95% is considered 'below normal' and precipitation below 90% of LPA is termed 'deficient'. Rainfall received between 104%-110% of benchmark fall on 'above normal' category while volume of rainfall above 110% of LPA is refereed as 'excess'*).

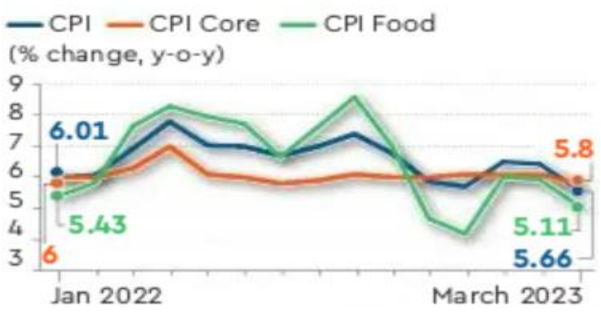
If the prediction of IMD holds true, the normal rainfall for five consecutive years will give boost to sowing of kharif crops (paddy, tur, soyabean, cotton) and also ensuring adequate soil moisture for rabi crops (wheat, mustard, chana). Though the central and eastern parts of the country are more dependent on monsoon for crop cultivation, some states are having a greater coverage under irrigation despite the El Nino conditions. As per the Director of IMD, of 15 El Nino years (1951-2022), six saw normal to above normal rainfall.

The IMD's forecast comes close on the heels of private weather forecasting agency Skymet's statement that monsoon precipitation this year could be 'below normal' at 94% of the LPA.

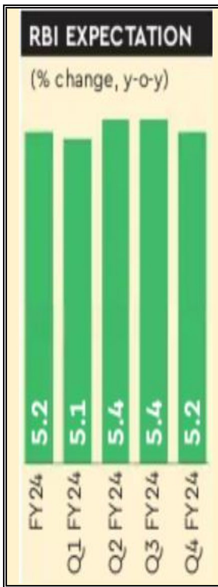
Inflation Outlook

Retail inflation moderates to 5.66% in March

India's retail inflation eased further to 5.66% in March 2023 on annual basis (6.95% in March 2022) as food inflation moderated on account of falling vegetable prices, offset in part by surging cereal prices. This reduction was a 15-month low slipping below the upper threshold of the RBI's medium-term 4+/-2% target after remaining above it for two months largely due to base effect and moderation in the prices of food basket.



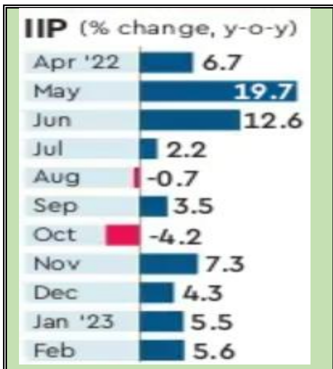
Both core and food inflation have eased to less than 6%. However, analysts are of the view that unfavourable weather conditions including the unseasonal rains and expected heat waves (El Nino effects) could push up the food prices again. Inflation in food and beverages eased to 5.11% in March 2023 from 6.19% in February 2023 followed by deflation in vegetables (8.11%), meat and fish (1.42%) and oils and fats (7.86%). Whereas, inflation in cereals and milk remained stubbornly high at 15.27% and 9.31% in March 2023. It is high in case of fruits (7.6%) and spices (18.2%) too. Two countervailing forces, inflation of cereals mainly wheat and milk have pushed inflation upwards on one hand while negative growth in case of vegetables and edible oils have brought it down. However, it is expected that increase in wheat prices due to shortage in wheat production will continue the current inflation trend.



Inflation: RBI MPC, April 2023

The RBI revised down FY24 inflation estimate by 10 bps to 5.2%, reflecting a downward revision in crude oil prices. On a quarterly basis, the central bank revised down Q4FY24 estimate to 5.2% from 5.6% and left estimates for Q2 and Q3 unchanged. As per the RBI, robust Kharif production and normal monsoon are likely to check food inflation. The central bank also emphasised that easing cost conditions could slow the pace of output price increase in manufacturing and services sector. On the risk front, the RBI sees imported inflation on account of uncertainty in the Global Financial Market, volatile oil prices and sticky core inflation (due to lagged pass-through of input costs) as key concerns.

Industrial Growth improves to 5.6%



India's industrial output as measured by the Index of Industrial Production (IIP) grew by 5.6% in February 2023 (5.2% in Jan 2023) due to incredible performance by the mining (4.6%), electricity (8.2%) and manufacturing (5.3%) sector showing a positive development.

Interest Rate Outlook

Against the backdrop of heightened global uncertainty (particularly after the SVB collapse), the RBI unanimously kept its rate unchanged at 6.5% while also keeping its stance unchanged at "withdrawal of accommodation", contrary to consensus expectations of

25bps rate hike. The tone of the policy was rather hawkish as the RBI highlighted inflationary risks and said it would not refrain from taking further action if required –thereby, becoming "data dependent" and keeping the "door open for future hikes".

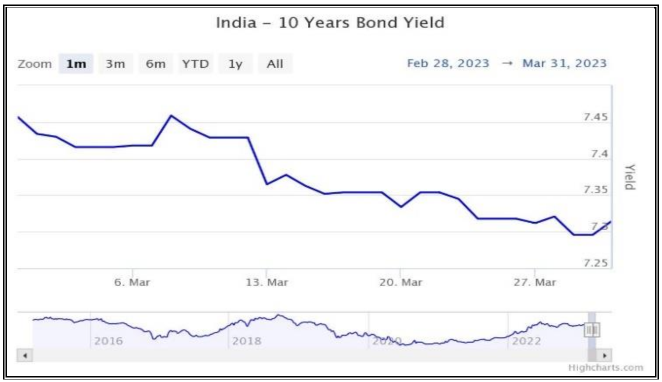
It is emphasised that the "pause" is limited to the current meeting and should not be viewed as a "pivot". However, for all practical purposes, macro conditions would have to change significantly from current levels to trigger further rate hikes by the RBI. The central bank can always choose to look through any volatile movements in food inflation (due to monsoon/ weather disruptions) or fuel prices (due to some increase in oil prices), till these pressures remain temporary. It is expected that no more rate hikes by the RBI going forward and see an "extended pause" as the most likely scenario. On the other hand, market chatter can start shifting towards timing of rate cuts, like in the US *(Source: Treasury, HDFC).*

Bond Yield: RBI MPC, April 2023

Tightening could continue in the form of normalising liquidity conditions which would imply that the yield curve could remain flat for some time and further transmission of past rate hikes could mean some more increase in money market rates. The 10-year bond yield dropped by 6 bps post the policy announcement to 7.21%. Some rise towards a 7.25-7.30% range in the coming weeks as the oil price risk remains, and the government's weekly bond supply could put pressure on yields.

₹: RBI MPC, April 2023

The pause in the domestic rate hike cycle with some scope for further rate hikes in the US and the EU could put some pressure on the USD/INR in the near-term. However, this is unlikely to be sustained as the dollar index is expected to lose its shine over the coming months as the US economy could go into a recession and markets price in rate cuts by the Fed.



Source: CMIE, Economic Outlook, worldgovernmentbonds.com

RBI's Monetary Policy Committee Meeting held on 3,5,6 of April 2023 has come out with the following resolutions:

- ✓ Benchmark lending rate unchanged at 6.50 per cent
- ✓ RBI projects 6.5% economic growth for 2023-24, better than 6.4% projected in February
- ✓ Inflation to be 5.2% in 2023-24, against 5.3% estimated in February
- ✓ Fight against inflation far from over, inflation outlook dynamic amid sudden announcement of crude output cut by OPEC+
- ✓ War against inflation has to continue until RBI sees a durable decline in inflation closer to the target
- ✓ Expectation of a record Rabi harvest bodes well for easing of food price pressures, milk prices likely to remain firm going into the summer season due to tight demand-supply balance and fodder cost pressures
- ✓ Protracted geopolitical tensions and global financial market volatility pose downside risks to growth outlook
- ✓ Witnessing unprecedented uncertainties in geopolitics and economy
- ✓ Global economy confronted with serious financial stability challenges in wake of recent banking sector developments in advanced countries
- ✓ Regulators need to identify potential vulnerabilities and take proactive regulatory and supervisory measures
- ✓ Institutions should exercise due diligence in risk management, corporate governance practices; pay close attention to asset-liability mismatches, build up adequate capital buffers
- ✓ RBI keeping a close watch on the banking sector turmoil in some developed countries
- ✓ RBI to set up centralised portal for public to search unclaimed deposits in multiple banks
- ✓ Indian Rupee moved in an orderly manner in 2022 and continues to be so in 2023, RBI remains watchful on maintaining stability
- ✓ CAD to remain moderate in Q4:2022-23 and in the year 2023-24 at a level that is both viable, eminently manageable.

Dashboard on Agricultural Commodity: Wheat

India, in the year 1943, suffered from the world's worst recorded food crisis, the Bengal Famine which led to death of a large population in eastern India due to hunger. Growing population led to insufficiency of foodgrains, farmers became landless and landed in debt. During that time the Green Revolution was an endeavour which led to high productivity of crops through adapted measures like increased area under farming, double cropping, adoption of HYV seeds, increased use of fertilizers and pesticides, improved irrigation facilities, etc. The revolution helped the country to move from a state of importing grains to a state of self-sufficiency mainly in wheat and rice.

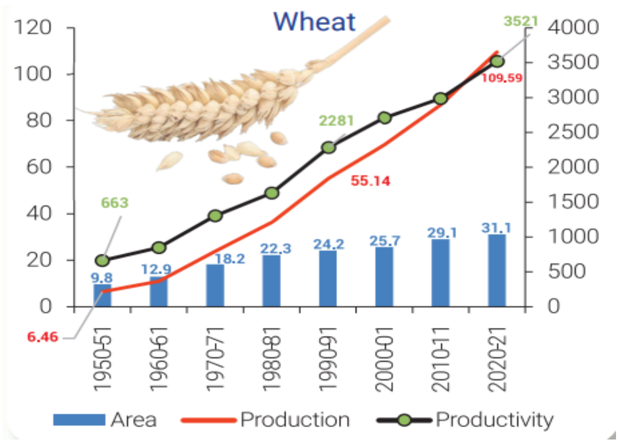
Wheat is a predominantly and widely cultivated food crop in India. India is the world's second largest producer. Area, Production and Productivity of wheat increased over the years. UP, MP and Punjab are the major producing states. Wheat has been in the news lately due to El Nino waves and thus procurement issues.

As per the Chief Economist at Nomura, El Nino is equal to high inflation and bad production thus affecting rural demand. A Committee constituted by the DA&FW to monitor the situation of wheat crop assessed that as on date, wheat crop condition is normal in all major wheat growing states. A large number of terminal heat and stress-tolerant varieties developed by the efforts of ICAR and SAUs are now under cultivation in an estimated area of more than 50% particularly in North Western plain zone. Since 75% of the area is under early and timely sowing conditions, the Government is optimistic that it will not be affected by heat conditions in March.

Indian Institute of Wheat and Barley Research provides the necessary crop-specific advisories to the famers through mobile apps. The Central Government has issued instructions that all extension agencies from Central and State governments along with ICAR/SAUs should visit the farmers' fields regularly providing timely advisories to the farmers during heat stress.

Measures to be taken by the Indian Government during heat stress

Ensure the availability of ample food stocks in its granaries. As per the 2nd AE for 2022-23, the total foodgrain production in the country is estimated at 323.55 MT (production of wheat is estimated at 112.18 MT, which is higher by 4.44 MT than the previous year's production). Though production has been high compared to last year, the Government could only procure 18.8 MT (requirement was 19.2 MT) during sudden rise in temperature in March 2022 as ample stock was not there. An article suggests that at least 25 MT must be procured in the Rabi marketing season of 2023-24 to meet the requirements of the PDS and thus ensuring food security (the central pool stock on 1st April this year may be only about 9.5 MT while the buffer norm is 7.4 MT).



(Units for Area-Million Hectare, Production-Million Tonnes, Productivity-Kg/Hectare)

Centre could resort to export curbs to ensure adequate domestic supplies. To reduce market price, the Government has increased the sale under Open Market Sale Scheme (OMSS) from 3-5 MT (under OMSS, the Government allows FCI to sell wheat to bulk users. The reserve price is fixed by the Government. The bidders cannot quote less than the reserve price if the tenders are floated by FCI.)

OMSS has been one of the major instruments for reducing the market price of wheat, resulting in wheat farmers being the losers. The Government's decision to sell wheat under OMSS was meant to more or less douse the inflationary fires, but it came rather late (the reserve price for bulk users came down from ₹2,600 per quintal to ₹2,150 per quintal). However, procuring much more than its requirement resulted in fall in wheat prices below MSP and farmers did not get the price they were hoping for. This phenomenon is expected in case of Punjab and Haryana. As private traders does not buy its requirement due to high market fees and other charges.

The biggest weapon to discourage private trade from stocking too much wheat in the open market is the threat of imposition of the Essential Commodities Act 1955 (one of the farm laws amended by the Government through an ordinance in 2020). However, a ban on export of wheat and wheat products during Russia-Ukraine war was a little possibility of relaxation. Large corporates will not be interested in buying and storing wheat from open markets thus hurting the farmers again.

Madhya Pradesh has emerged as an important wheat procurement state where procurement has increased from 6.7 MT in 2019-20 to 13 MT in the next two years. The market fee and other charges are also less. The success of wheat procurement for the central pool will depend on what happens in the state.

Report📖THINK

India Development Update (IDU)-This publication by World Bank reports on recent developments in India's economy and places these in a global context. Based on these developments and on policy changes over the period, the IDU updates the outlook for India's economy.

The key takeaways from the report are as follows:

1. India's growth continued to be resilient, despite some signs of a moderation in the second half of FY22/23

- India was one of the fastest growing economies in the world with real GDP growing 7.7 percent year-on-year during Q1-Q3 fiscal year 2022/23 (April-March, FY22/23).
- Growth was underpinned by robust domestic demand – strong investment activity bolstered by the government's capex push and buoyant private consumption, particularly among higher income earners.
- While the overall growth momentum remains robust and real GDP growth for FY22/23 is estimated to be 6.9 percent, there were signs of moderation in Q3 as growth slowed to 4.4 percent year-on-year (y-o-y). There was also a change in the composition of domestic demand in Q3 FY22/23 with a lower share from government consumption as fiscal consolidation efforts continued.

2. Inflation moderated in the second half of 2022 but remains above the upper threshold of RBI.

- Headline inflation averaged around 6.6 percent in FY22/23. Average inflation in H2 FY22/23 was almost 1 percentage point lower than the first half as inflationary pressures began to taper and the combination of supply side measures (such as export restrictions) and monetary policy tightening began to take effect.
- The gradual moderation in price pressures was led by a decline in food inflation (the single largest component of headline inflation) and easing fuel prices on the back of softening in global oil prices.
- However, the core inflation remained elevated in FY22/23, averaging around 6.1 percent over the fiscal year. While there was some tapering in domestic demand growth in Q3, it remained the main reason for the stickiness in core inflation. An improving traditional market services sector (trade, hospitality, transport and storage and, communication) also played a role in propping up core inflation.

3. The current account deficit narrowed in Q3 FY22/23 as commodity prices ease

- The current account deficit narrowed from 3.3 percent of GDP in H1 FY22/23 to 2.2 percent in Q3 FY22/23. While service exports remained robust, softening global demand weighed particularly on merchandise goods exports, which limited overall export growth.
- The current account balance remains adequately financed by robust net capital inflows and foreign direct investment inflows. The rupee has depreciated by 9.1 percent since April 2022, but the pace of depreciation showed signs of slowing in H2.

4. The government remains on track to meet its fiscal deficit target for FY22/23

- Robust nominal GDP growth bolstered revenue collection during Q1-Q3 FY22/23. The highlight continued to be the performance of the Goods and Services Tax (GST) with average growth of over 20 percent year-on-year. According to the government's revised estimates, tax revenues were about 8 percent higher than budgeted and 15.6 percent higher than the previous year.
- Overall, the central government is likely to meet its fiscal deficit target of 6.4 percent in FY22/23. The general government fiscal deficit – the combined deficit of the Centre and States – is estimated to have declined further to 9.4 percent in FY22/23 from 13.3 percent of GDP in FY20/21. Public debt is also estimated to decline to 84.3 percent of GDP in FY22/23, from a peak of 87.6 percent in FY20/21.

5. Growth is projected to moderate to 6.3 percent in FY23/24

- Constrained by slower consumption growth, fiscal consolidation and challenging external conditions Although India's economy has been relatively resilient to challenging external conditions, real GDP growth is likely to moderate to 6.3 percent in FY23/24 from the estimated 6.9 percent in FY22/23.
- Moderating consumption growth, easing global commodity prices and the lagged effect of monetary policy tightening is expected to bring headline inflation within the RBI's target range despite core inflation remaining elevated.
- On the external front, the negative contribution of net exports will be smaller due to the strong performance of service exports and a gradual decline in the import bill.
- The narrowing trade deficit will contribute to the current account deficit reducing to 2.1 percent from around 3 percent in FY 22/23. The general government deficit will likely consolidate by 0.7 percentage points to 8.7 percent in FY23/24 due to continued, albeit slower, revenue growth and lower current spending, reflecting the withdrawal of pandemic-related support programs. The lower projected fiscal deficit will stabilize the debt-to-GDP ratio at around 83 percent.

6. There are some downside risks to India's growth in FY23/24

- Despite resilience amid slowing global growth, there are headwinds to India's growth in FY23/24. Recent financial sector turmoil in the US and Europe could reduce appetite for emerging market assets, trigger another bout of capital flight and put pressure on the Indian rupee.
- Tighter global financial conditions could also weigh on the risk appetite for private investment in India. Moreover, faster-than expected inflation due to higher food or fuel prices may also weigh on domestic demand. These downside risks to growth could affect fiscal consolidation plans.

Click here for [Full Report]