India economy update: April 2024

Industrial production: Growth accelerates to 4-month high; FMCG remains muted

- Industrial production accelerated by 5.7% YoY in February 2024 compared with 4.1% in January 2024. On a MoM basis, index is declined by -4.1%

- Mining and electricity drove industrial activity higher followed by manufacturing. Manufacturing sector output was impacted by muted exports as well as lower FMCG output.

- Consumer durables along with infra and construction goods expanded by 12.3% YoY (11.9% in January) and 8.5% YoY (5.5% in January). Consumer non-durables output contracted by 3.8% YoY (-0.2% in January). Capital goods output is also muted at 1.2% YoY. A normal monsoon should drive consumption demand higher and thus outlook for FMCG sector is positive.

- Industrial output during April-February 2024 has increased by 5.9% compared with an increase of 5.6% in same period last year. High frequency indicators show India's growth is holding up led by uptick in investment cycle and recovery in rural demand as seen in two-wheelers.

Retail inflation: Core moves even lower, food is sticky

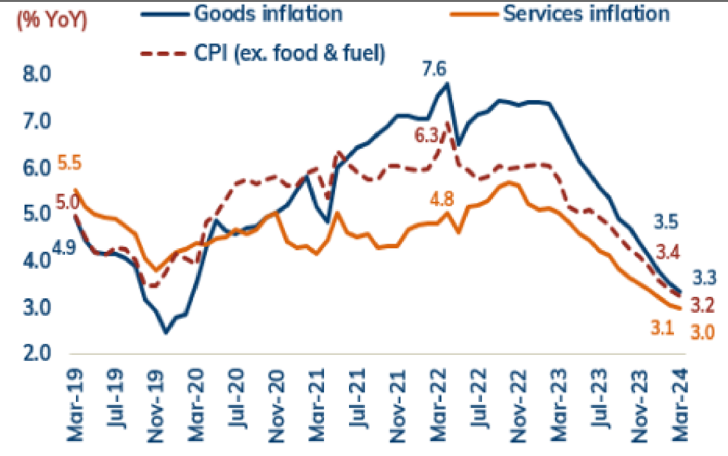
- CPI inflation eased to 4.85% YoY in March vs. 5.09% in February. Core inflation continues to move lower (3.2% YoY) even as food and beverages is still elevated at 7.7% YoY

- Food inflation has moderated on a sequential basis, but on a YoY basis it is still elevated led by vegetables, pulses and cereals along with meat and eggs. Notably, spices and pulses inflation is easing

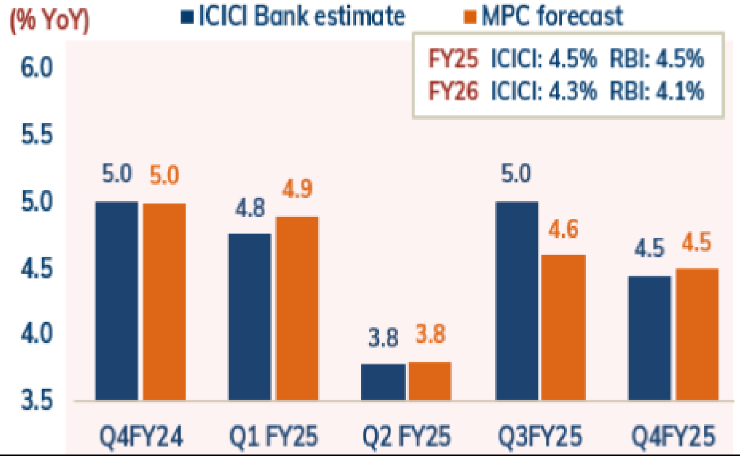
- Core inflation is moved even lower to 3.2% YoY with broad-based decline seen across categories except personal care and effects because of higher gold prices and recreation and amusement. With rising global commodity prices, core goods inflation should increase. Globally, too core goods inflation has bottomed out. However, In India's case services inflation has been well contained.

- Outlook on CPI inflation is contingent on normal monsoon and trajectory of global commodity prices. As of now, we expect CPI inflation to average 4.5% for the year though upside risks are building up. With CPI inflation expected to be below 4% in Q2, backdrop is favourable from a domestic standpoint. However, rising US yields putting pressure on EM currencies along with INR which is inflationary. Overall, domestic monetary cycle could also get delayed from our base case of October cut

Goods and services inflation continue to ease

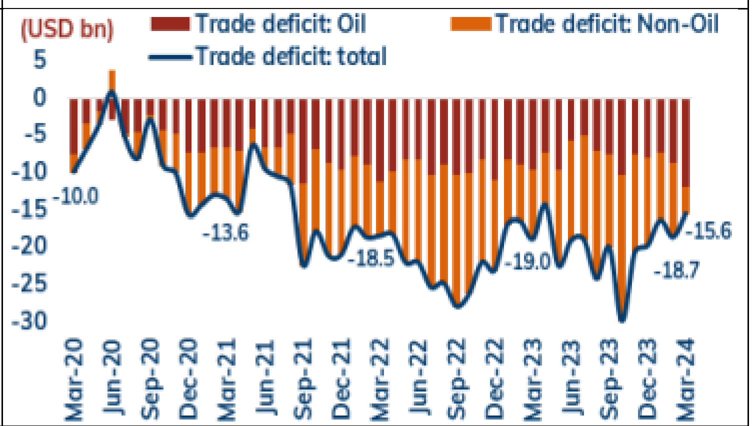


CPI seen at 4.5% in FY25 (RBI: 4.5%)



Merchandise trade: Trade deficit narrows, but rising oil prices a concern

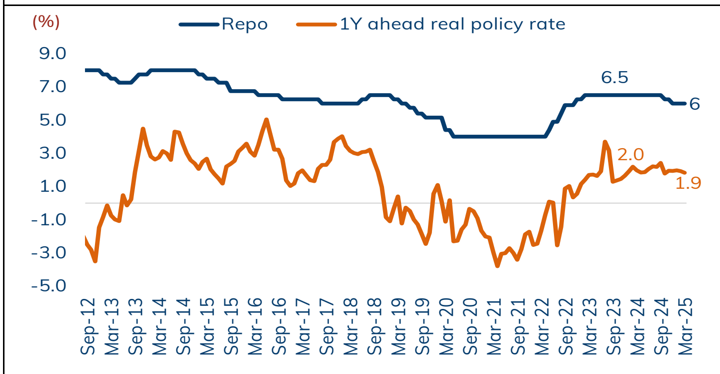
- Merchandise exports fell by 0.7% YoY at USD 41.7bn in March (+0.7% MoM), led by lower oil exports (-35% YoY) despite higher non-oil exports (+8.0% YoY).
- Imports fell by 6.0% YoY at USD 57.3bn, mainly due to lower gold imports (-54% YoY). Oil imports and non-oil non-gold imports picked up sequentially, but remain lower on YoY basis
- Trade deficit narrowed to 11-month low of USD 15.6bn in March from USD 18.7bn in Feb, mainly due to lower gold imports. Non-oil non-gold deficit narrowed due to higher non-oil exports. If oil prices remain in USD 80-90/bbl. range, trade deficit should be USD 266bn for FY25 which could go up to USD 276bn if oil prices move up by another USD 10/bbl. With rising oil prices and stronger dollar, outlook for INR is not as positive as few weeks back. Even net services exports have seen downward momentum in last two months
- Services exports were weaker in March and fell by 6.2% YoY at USD 28.5bn. On a MoM basis, services exports saw a mild pick-up (+0.7%). Service imports fell by 6.6% YoY at USD 15.8bn in March. On a MoM basis, it rose by +3.9% MoM. Net services exports fell by 6.2% YoY at USD 12.7bn (USD 13.1bn last month).

Services exports fell by 6.2% YoY at USD 28.5bn	Trade deficit narrowed to USD 15.6bn in March
	

MPC keeps status-quo on rate and stance, optimistic on growth

- MPC voted to keep repo rate unchanged at 6.5% and retained stance of 'withdrawal of accommodation' with 5:1 vote each. Growth and inflation forecasts for FY25 were retained at 7% and 4.5% respectively. Notably, while CPI forecast was kept unchanged, inflation estimate for all quarters other than Q3 was revised lower
- Liquidity conditions eased in March on the back of pick-up in government spending. Liquidity situation should remain benign given expected FX inflows next year and build-up of reserves which have already crossed USD 645bn
- A normal monsoon should not only drive an uptick in rural consumption but also ensure lower food inflation. This gives MPC room to change stance in August when it can see how rains have played out. MPC to ease policy rates and lower real rates, which are likely to peak in Q2 at 2.7%. We expect 50bps reduction in policy rate in FY25 starting October, depending upon domestic and global factors

Real rates are comfortably above the 1% mark



Interest rate differential between the MPC and the FOMC stands at 1%