सत्यमेव जयते

Economic Diplomacy Division

Ministry of External Affairs

MONTHLY ECONOMIC REPORT

MAY 2023

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Introduction

The provisional GDP estimates for FY23, released in May, exceeded expectations. The strong performance in the final quarter led to a GDP growth of 7.2%, surpassing the earlier estimated 7%. This positive momentum continues into the current fiscal year, with various forecasting agencies revising their growth projections for FY24. India's impressive growth in FY23, amidst global inflation and monetary tightening, demonstrates the effectiveness of its economic strategies.

The strength of India's domestic demand is a crucial driver of its economy. Despite the pandemic-induced contraction in FY21, domestic demand recovered and showed significant growth in FY23. The quarterly growth trajectories of consumption and investment have nearly converged with the pre-pandemic period, reflecting the economy's progress towards normalcy. However, external demand needs improvement, as it could have performed better in the second half of FY23 than the first.

Employment levels have risen, contributing to inclusivity, and bolstering domestic demand. India's labour force participation rate (LFPR) has increased, and the unemployment rate reached a five-year low of 4.1% in FY22. In FY23, urban unemployment rates declined steadily, indicating steady employment growth. Various policy measures implemented over the years, focusing on strengthening the corporate sector, supporting small enterprises, improving the ease of doing business, and attracting foreign capital, have played a role in generating employment opportunities and facilitating economic recovery.

Inflation emerged as a significant challenge in FY23 for India, as it did globally, due to geopolitical conflicts and the impact of El Nino. India's inflation, however, remained relatively lower compared to other emerging market economies (EMEs) and advanced economies (AEs), potentially due to adequate supply easing measures. The Reserve Bank of India (RBI) did not need to raise policy rates as much as other central banks. Towards the end of the year, declining international commodity prices led to a significant drop in India's wholesale price inflation, and headline inflation entered the target range.

India's GDP Growth in FY23

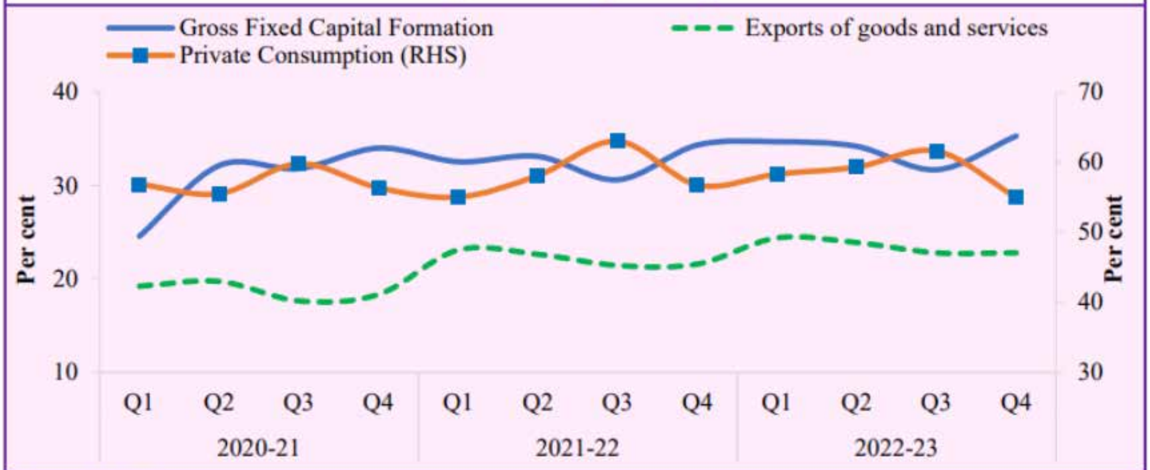
- International Monetary Fund's (IMF) April 2023 update of the World Economic Outlook (WEO) forecasts a slowdown in world output growth from 3.4% in 2022 to 2.8% in 2023.

- Growth is expected to marginally improve to 3.0% in 2024 but still lower than that of 2022 and significantly below the 6.4% in 2021.

Source: Bloomberg, MoSPI.
Note: 2022 is FY23 in India's case

- Q4 of FY23 showed outstanding performance of India's real GDP compared to other countries.
- Year-on-year growth in real GDP in Q4 of FY23 was estimated at 6.1%, surpassing the 4% growth in Q4 of FY22 and 4.5% growth in Q3 of FY23.
- On a sequential basis, Q4 of FY23 witnessed a growth rate of 8.4%, higher than the 3.7% growth in the previous quarter.
- The sustained growth momentum in Q4 highlights the strong performance of India's economy.

Share of demand-side components in quarterly GDP at Constant Prices



Source: MoSPI

- Private consumption (PFCE) as a proportion of GDP reached the highest in 17 years for FY23.
- Gross fixed capital formation (GFCF) recorded the highest proportion of GDP in 10 years for FY23, reaching a 10-year high of 35.3%.
- The increase in GFCF was supported by increased public sector investment, which attracted private sector investment.
- The share of total exports in GDP declined to 22.8% in Q4 of FY23, compared to 24.4% in Q1 of FY23.
- This decline was influenced by synchronized monetary tightening in major economies, resulting in reduced consumer spending and moderation in international trade.

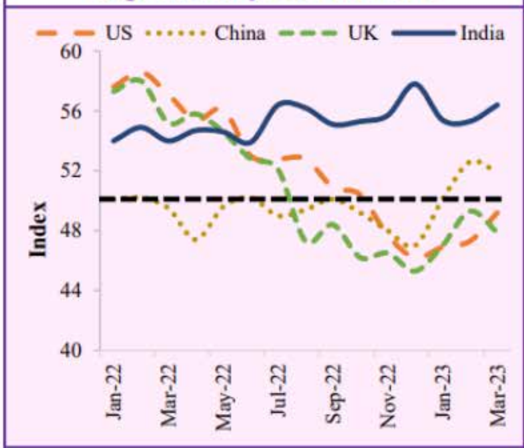
Sustained performance of the Industrial Sector

- PMI Manufacturing remained in an expansionary zone throughout FY23, supported by new orders and output expansion in the manufacturing sector.
- However, the growth in the manufacturing sector's GVA experienced a temporary moderation in Q2 and Q3 of FY23 due to elevated input costs.
- The Index of Industrial Production (IIP) expanded in Q4 of FY23, following modest growth in Q2 and Q3 as capital goods and infrastructure/construction goods witnessed a notable increase in production.

- The electricity sector also experienced a significant increase in production in FY23, driven by intense summer heatwaves and economic recovery.

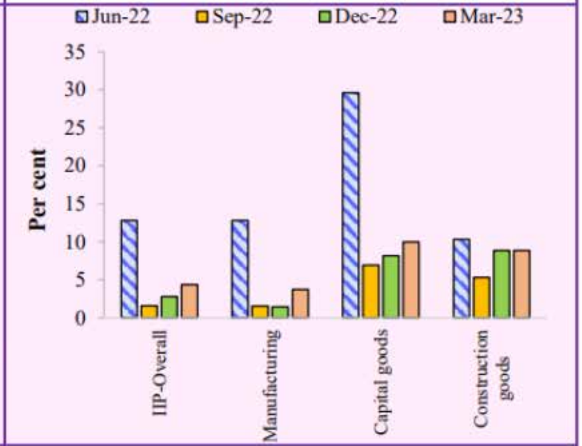
- Reforms such as the National Logistics Policy, the Production Linked Incentive (PLI) scheme, and PM GatiShakti are expected to boost manufacturing output further.

PMI Manufacturing remained in an expansionary zone in India



Source: IHS Markit

IIP and its sub-components expanded in Q4 of FY23



Source: NSO, MoSPI

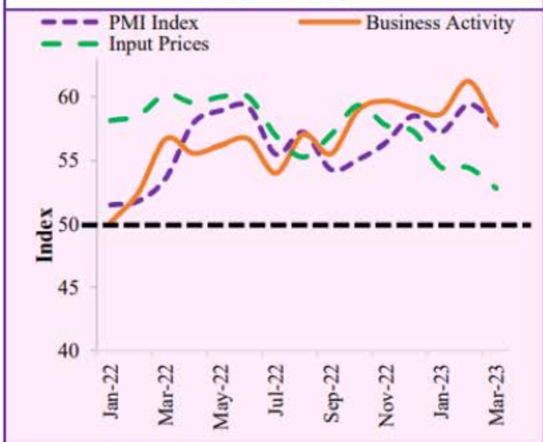
Strong Services sector performance

- PMI Services remained in the expansionary zone throughout FY23, supported by improvements in new business intakes and increased orders.

- The tourism sector showed signs of revival, with Foreign Tourist Arrivals (FTA) in India reaching close to pre-pandemic levels in Q4 of FY23.

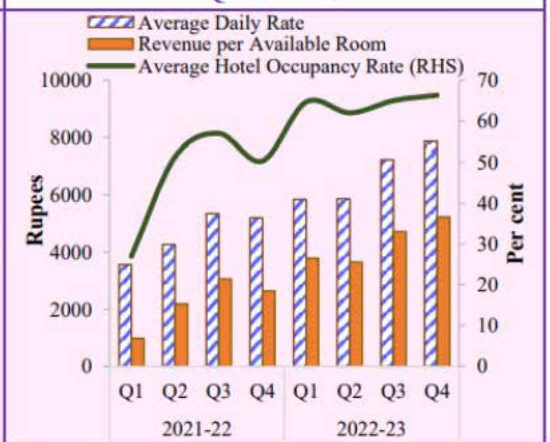
- Domestic air passenger traffic surpassed pre-pandemic levels in Q4 of FY23, driven by a surge in corporate travel, a rebound in MICE tourism, and leisure travel.

PMI Services remained in an expansionary zone in FY23



Source: IHS Markit

Hotel Industry witnessed robust growth in Q4 of FY23



Source: Anarock

Growth momentum build-up in FY23 will likely be sustained in Q1 of FY24.

- High-Frequency Indicators (HFIs) for April/May 2023 indicate a pick-up in economic activity and sustained growth momentum in Q1 of FY24.

- Gross GST collection rose by 12% year-on-year to ₹1.57 lakh crore in May 2023, surpassing the ₹1.5 lakh crore benchmark for the fifth time.

- E-Way bills grew in April and May 2023, indicating solid prospects for GST collection in the coming months.

- PMI manufacturing reached a 31-month high of 58.7 in May 2023, driven by record expansion in input stocks, new orders, and inputs.

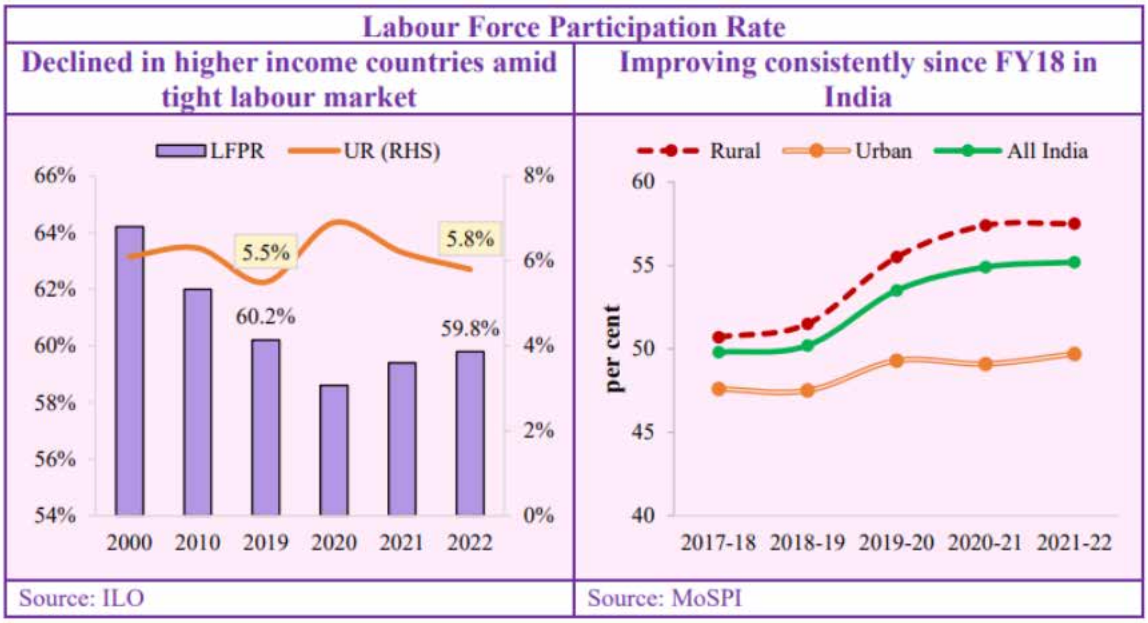
- PMI services expanded with a reading of 61.2 in May 2023, indicating further output expansion across sectors at the second-quickest pace since July 2010.

Recovery of Labour Markets

- India's labour force and labour force participation rate (LFPR) have risen through the pandemic, broadly in tandem with the pre-pandemic trend. In FY22, India's LFPR was 55.2%, higher than 54.9% in FY21 and 53.5% in FY20.

- Strong economic growth, supported by calibrated fiscal policy and expansion of public capital expenditure, contributed to the rise in the worker-population ratio.

- The unemployment rate (UR) declined to a five-year low of 4.1% in FY22, with a consistent decrease observed in rural and urban areas.



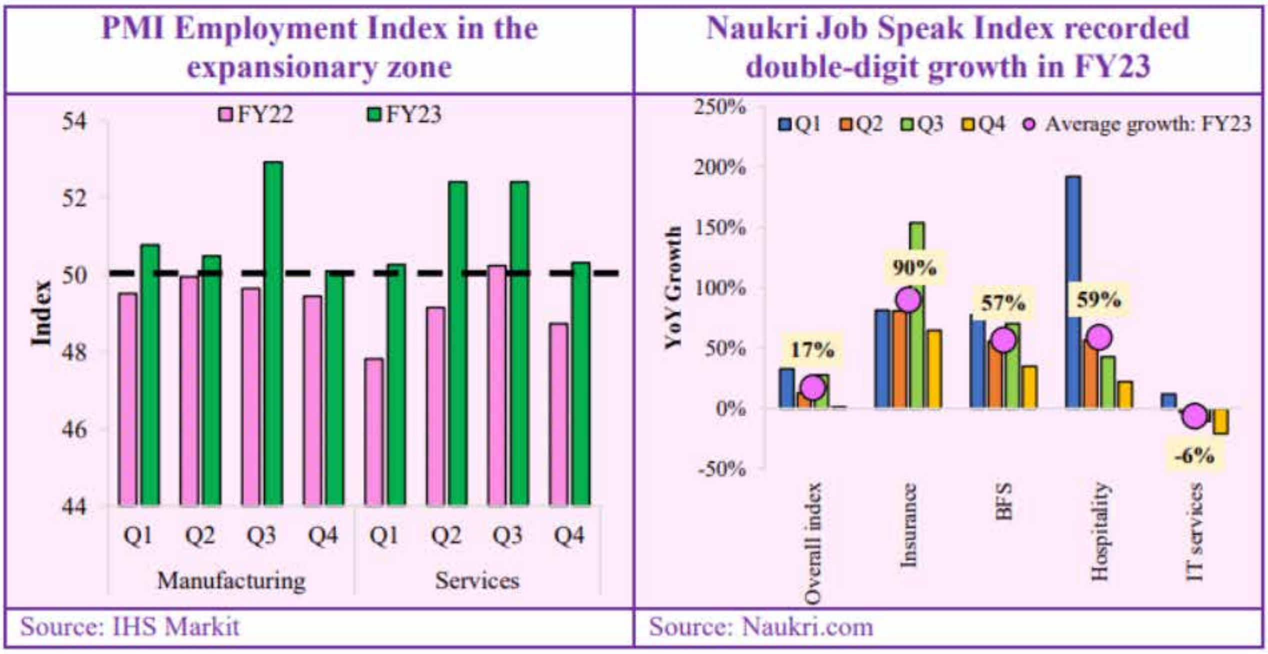
Growth with rising inclusivity

- Job creation in the formal sector has been accelerating, as seen in the increased net monthly payroll additions under the Employees Provident Fund Organisation (EPFO). Net members added under EPFO reached a four-year high, growing by double-digits compared to the previous year.

- The expert service sector accounted for 51% of formal job creation, including manpower suppliers, normal contractors, and security services.

- PMI sub-indices for employment in manufacturing and services entered the expansionary zone in FY23.

- The Naukri Job Speak Index also doubled in FY23, reflecting increased hiring activity.



Inflation in India

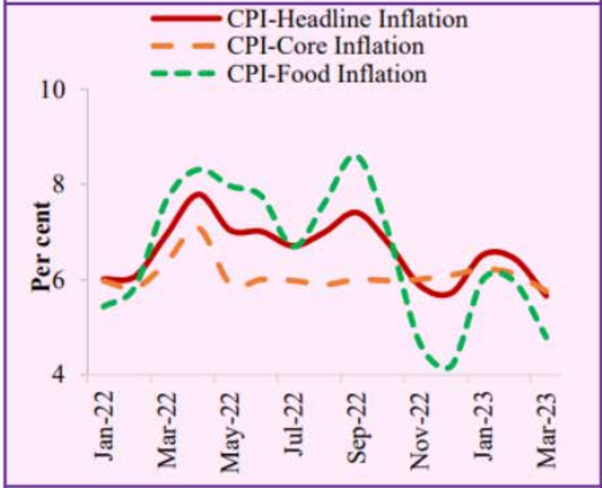
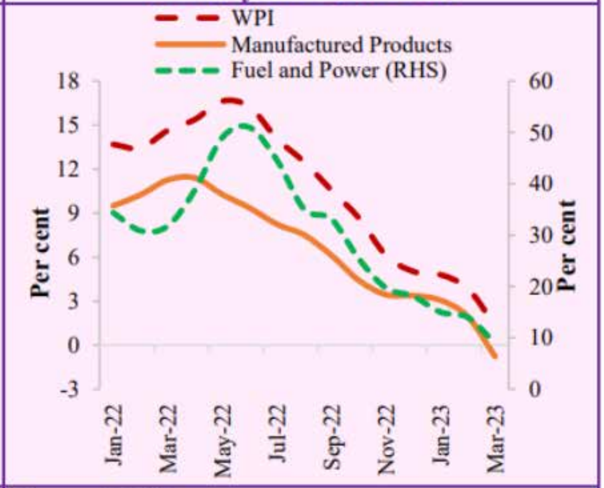
- CPI-Core inflation in India remained around 6% from May 2022 to February 2023.

- Wholesale price inflation started declining in June 2022 and reached a low of 1.3% in March 2023.

- The decline in inflation was particularly noticeable since October 2022, with a steady shrinkage in manufactured products inflation and a faster decline in fuel & power inflation.

- While core inflation somewhat eased, food inflation significantly decreased from the third quarter of FY23.

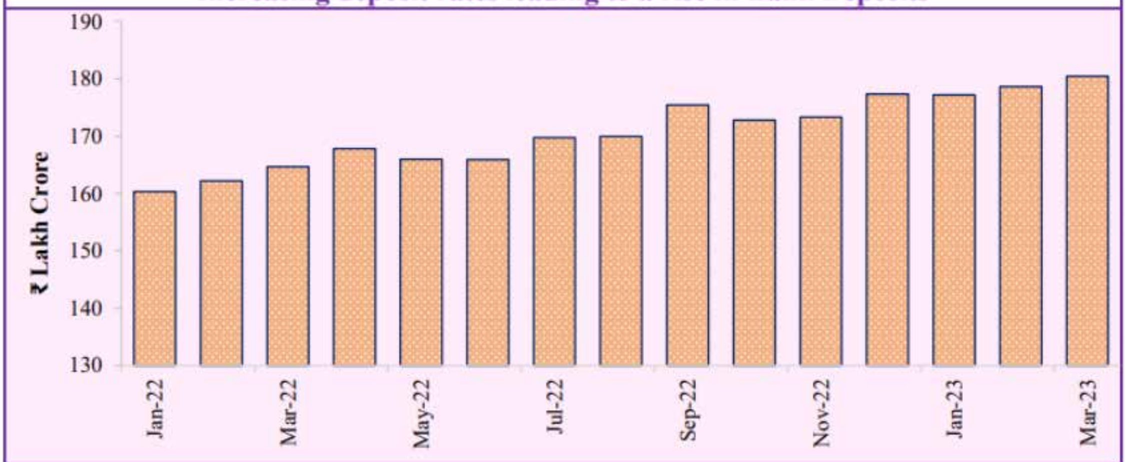
The notable decline in food inflation, combined with sticky core inflation, led to a 100 basis points (bps) reduction in headline inflation in Q4 of FY23 compared to Q1.

Declining Inflationary pressures	WPI Inflation entered into negative territory in March 2023
	
Source: MoSPI	Source: DPIIT

Monetary Policy Tightening

- In FY23, the RBI continued its monetary tightening measures, which initially affected lending rates.
- Due to the low-interest rate regime from 2020 to H1:2022, many individuals shifted their financial savings from savings avenues to stock markets. As a result, banks faced competitive pressures and were compelled to raise deposit rates to attract deposits.
- The increase in deposit rates exceeded the rise in lending rates, which occurred approximately seven months after the initial repo rate hike in December 2022.
- Between May 2022 and February 2023, the Reserve Bank of India (RBI) increased the repo rate six times.
- The repo rate was raised from 4% in April 2022 to 6.5% in February 2023.

Increasing deposit rates leading to a rise in Bank Deposits



Source: RBI
Note: Deposits include Time and Demand Deposits

Impact of FPI on Monetary Policy

- Despite relatively lower hikes in policy rates, India's inflation rate remained close to its target range. This can be attributed to the calibrated fiscal stimulus provided by India during the pandemic, in contrast to major fiscal expansions undertaken by other countries.

- The Reserve Bank of India (RBI) has also paused to increase the policy rate in its recent Monetary Policy Committee (MPC) meetings, as retail and core inflation has declined.

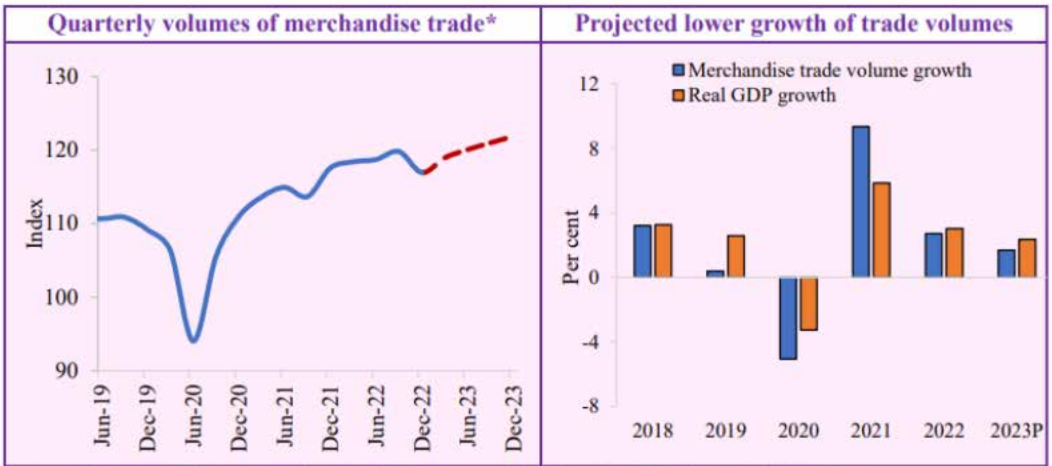
- The monetary stance is expected to remain stable in the foreseeable future. However, the impact of El Nino on domestic food prices and the potential delay in the pass-through of the Wholesale Price Index (WPI) into retail output may lead to a rise in inflationary pressures.

India's Resilient External Sector

- India's merchandise exports followed the global trend, experiencing peak growth in Q1 of FY23 (April-June 2022). However, the impact of the European war began to set in, leading to a moderation in export growth.

- Despite the moderation, exports remained resilient in FY23 and surpassed the levels of FY22. The volume growth of India's imports remained high throughout FY23, supporting the country's sustained economic activity growth.

- The trade deficit, however, improved in the second half of FY23 due to lower international commodity prices, which lowered the cost of imports.

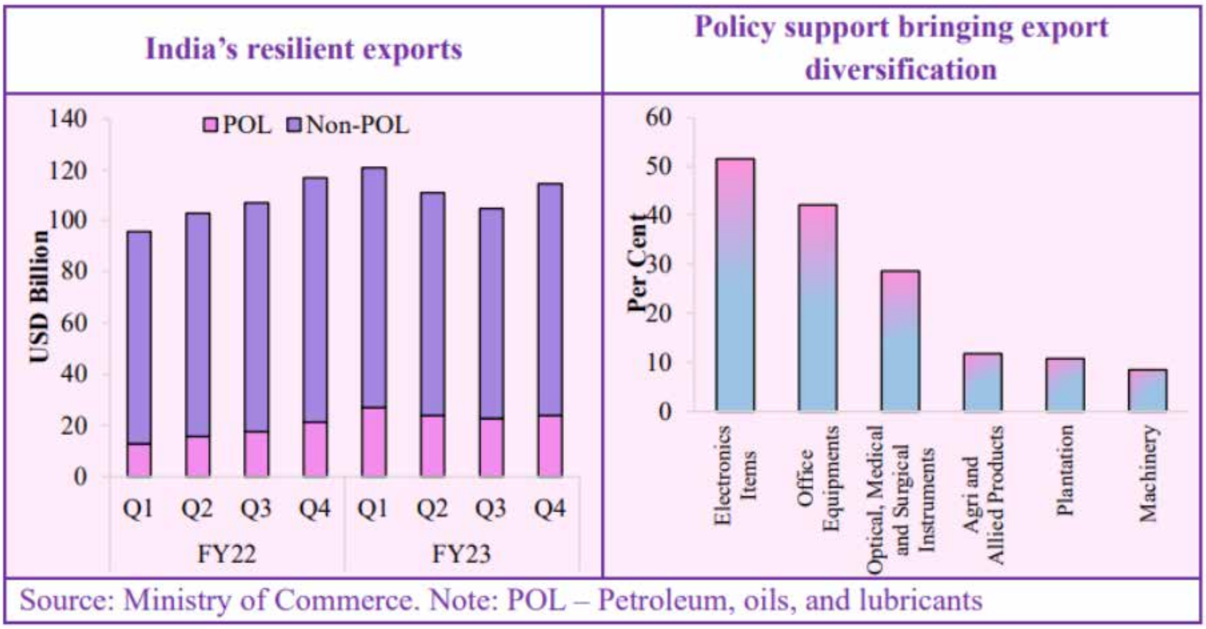


Source: World Trade Organisation; *Index is seasonally adjusted and chained to 2015 prices.
Note: Dotted line implies a forecast starting from the quarter ending March 2023.
P stands for Projected.

- The recovery of industrial activity in FY23 in India led to increased imports. This is reflected in the higher share of energy products, such as crude petroleum and coal, in total imports in FY23 compared to FY22.

- However, the higher energy imports in Q1 and Q2 of FY23 were also influenced by elevated energy prices in the global energy markets.

- In the last two-quarters of FY23, energy prices started trending downwards, resulting in a decline in energy imports.



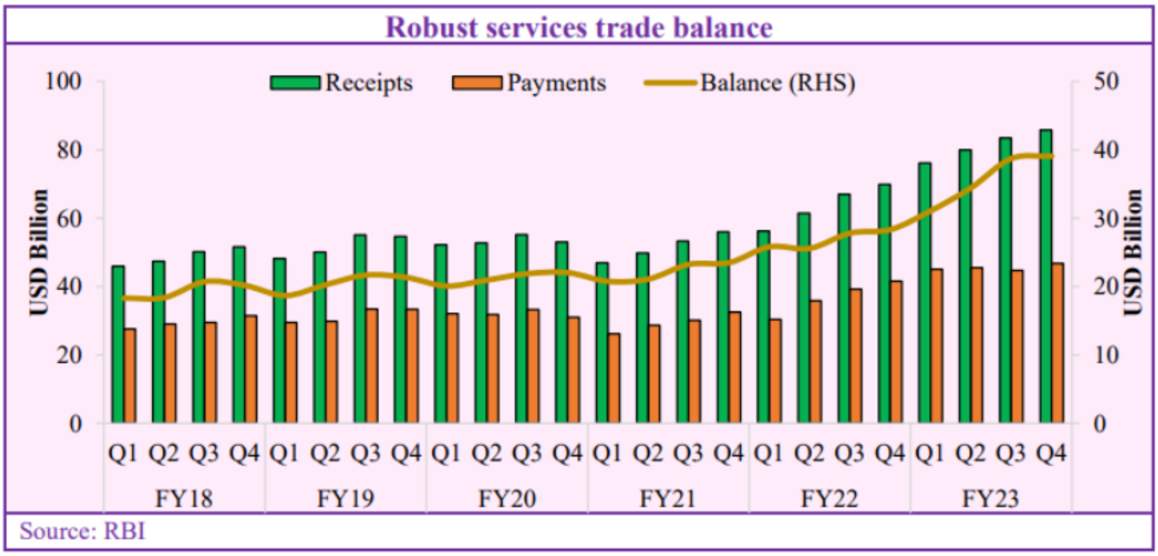
India's resilient exports | Policy support bringing export diversification

Source: Ministry of Commerce. Note: POL – Petroleum, oils, and lubricants

- Unlike the moderation in merchandise exports, services exports experienced a surge in FY23. The strong performance of services exports is attributed to India's quick adaptation to a contactless world, particularly in the IT sector.

- This adaptation allowed highly skilled professionals in India to offer services online to clients worldwide.

- The vital services trade surplus and moderating merchandise trade deficit reduced India's overall trade deficit in FY23.



Robust services trade balance

Source: RBI

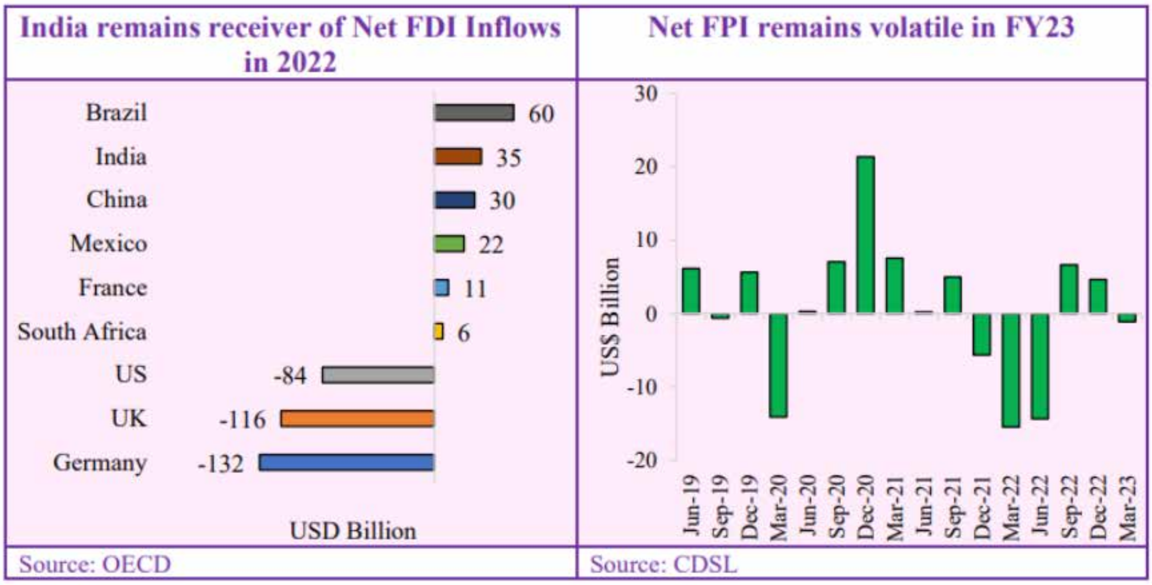
Capital flows remained volatile, with FDI inflows higher than peer EMEs

- FDI flows to India were impacted by inflationary pressures and tighter monetary policies abroad.

- Gross FDI reached a record high of US$ 84.8 billion in FY22 but moderated by 16% on a YoY basis in FY23.

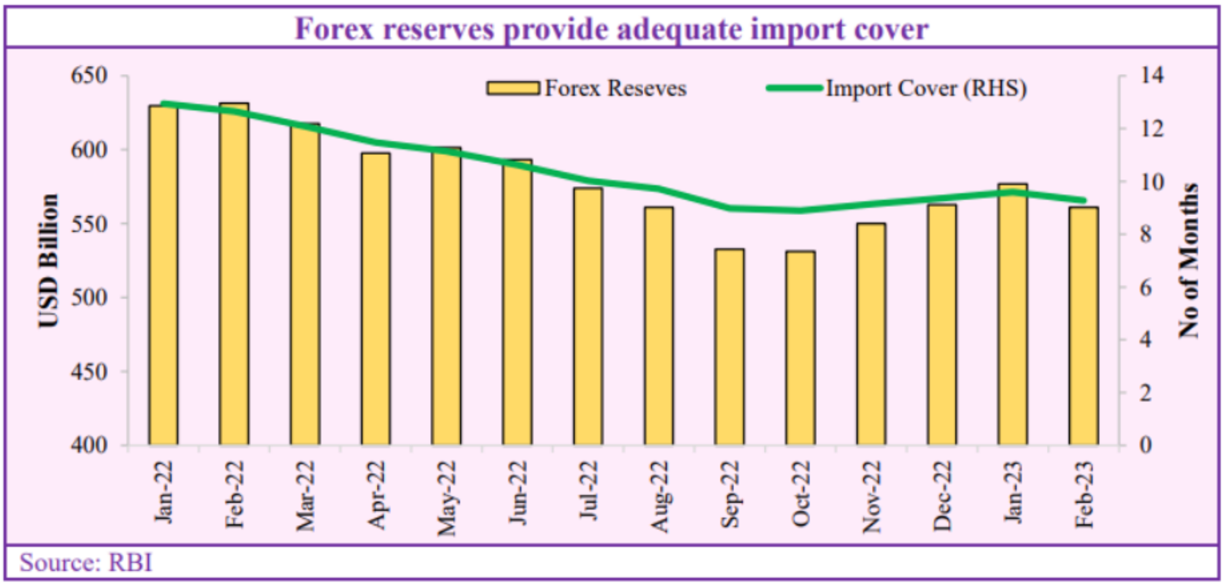
- Net FDI declined by 27.4% in FY23 on a YoY basis.

- According to OECD statistics, this trend is not unique to India, as net FDI inflows to emerging market economies (EMEs) declined by 36% in 2022.



A comfortable level of forex reserves

- Forex reserve holdings in India declined in the first half of FY23, as they were used to finance a widening Current Account Deficit (CAD) and capital outflows.
- However, the subsequent narrowing of CAD and Foreign Portfolio Investments (FPI) inflows contributed to rebuilding the forex reserves.
- By the end of FY23, India became the world's 5th largest holder of forex reserves.
- The forex levels are considered adequate, providing an import cover of ten months and a comfortable cushion against external shocks.
- Looking ahead, the continued narrowing of CAD and increasing FPI inflows, supported by the non-aggressive posturing of the Federal Reserve, will further strengthen the forex reserves.



Outlook for the external sector

- Downside risks to India's exports include the implementation of the Carbon Border Adjustment Mechanism (CBAM) by the European Union, uncertainty surrounding the Russia-Ukraine conflict, and the potential adoption of trade-restrictive measures due to geopolitical tensions.

- Supply chain disruptions are easing, as indicated by the upward trend in globalized container trade measured by the Kiel Trade Indicator. Moderating inflation across countries may provide some leeway for policymakers to halt or slow the pace of monetary policy tightening.

- Ongoing trade agreements with advanced economies, the new foreign trade policy, the digital revolution in payments and trade facilitation, trade promotion activities, improved trade credit, and the promotion of districts as export hubs are expected to boost India's global export market share.

- Prices of commodities, particularly energy commodities, are anticipated to remain relatively lower, helping to narrow India's merchandise trade deficit.

- While the effects of recessionary tendencies on services trade and remittance growth are uncertain, their levels are expected to remain broadly stable. As a result, India's current account deficit is projected to stay narrow throughout FY24.

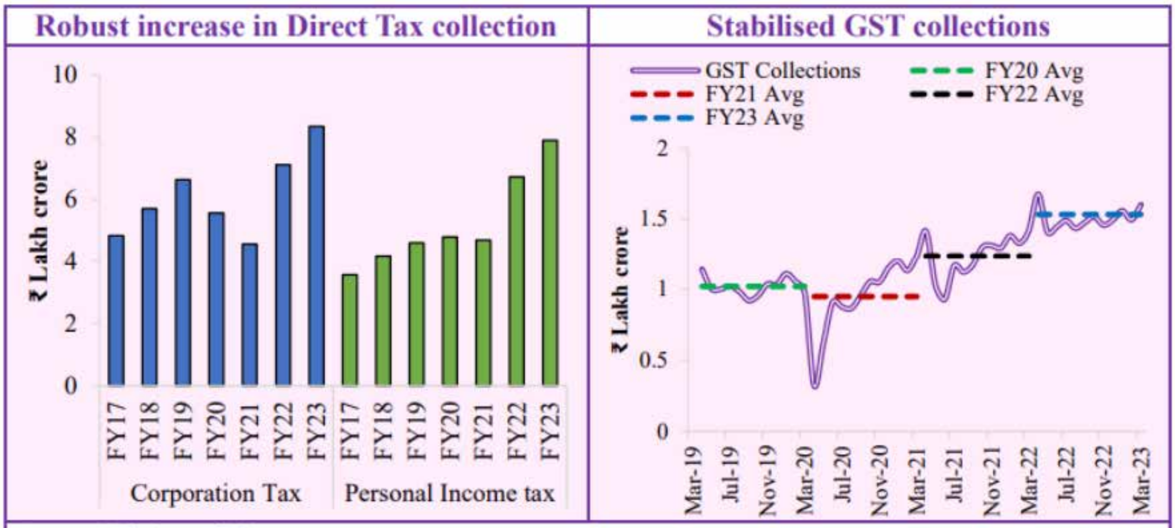
Buoyant revenue helped Govt to achieve Fiscal targets.

- The gross tax revenue in FY23 experienced a year-on-year growth of 12.7%. This growth was primarily driven by strong performance in direct taxes (income and corporate tax) and Goods and Services Tax (GST).

- Direct taxes increased by 20%, while corporate taxes grew by 16% in FY23.

- Gross GST collections also recorded significant growth of 21.4%.

- Average monthly GST collections rose from ₹ 1.2 lakh crore in FY22 to ₹ 1.5 lakh crore in FY23.



Source: Ministry of Finance

- In FY23, the total subsidy expenditure increased to 15.4% of the revenue, surpassing the previous year's figure of 13.9%. However, according to budget estimates, subsidy expenditure will decline to 10.7% in FY24.

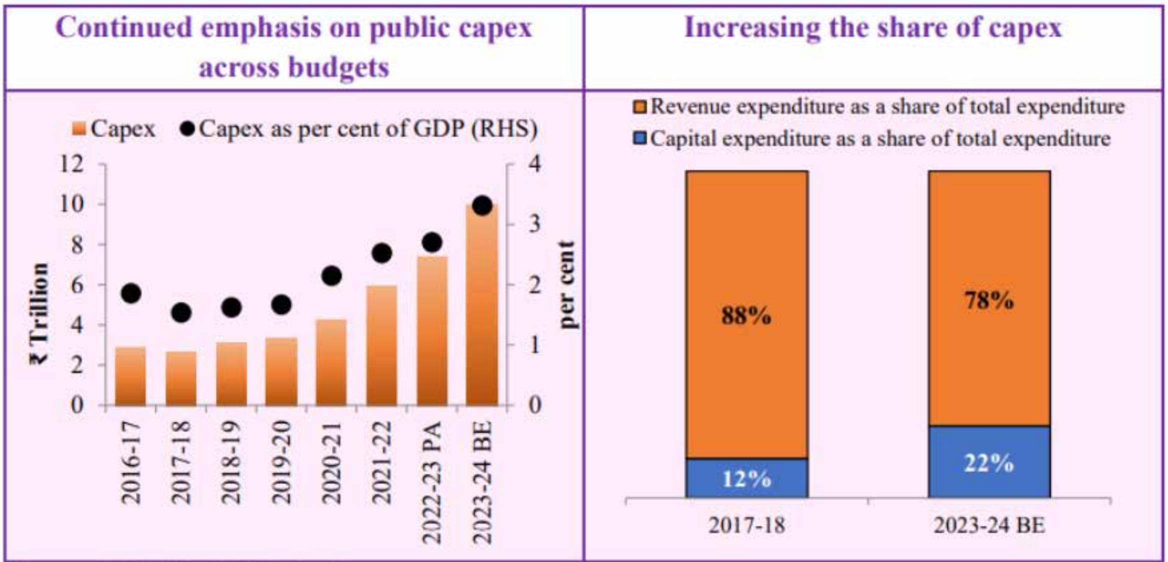
- This projection is based on the expected decrease in international prices of food, fertilizers, and fuel. The decline in subsidy expenditure in FY24 is anticipated due to the lower costs of these essential commodities.

- The central government's capital expenditure in FY23 experienced a year-on-year growth of 24.3%. This growth rate surpassed the average growth of 7.8% observed during the pre-pandemic years from FY17 to FY20.

- The Union Government's capital expenditure as a percentage of GDP stood at 2.7% in FY23, compared to 1.7% in FY20.

- It also accounted for 21.3% of the revenue expenditure in FY23, in contrast to 14.3% in FY20.

- In the Union Budget for FY24, the capital investment outlay increased by 33%. The increased outlay in FY24 is nearly three times that in FY20, indicating a significant boost to capital investment.



Source: CGA, MoSPI, Budget Documents

- The Central Government incentivized states to encourage them to take complementary policy actions to boost infrastructure investment. Grants for capital works and interest-free capex loans with a 50-year tenure were available to state governments in FY23.

- The government's focus on capital expenditure also motivated its departmental arms and Central Public Sector Enterprises (CPSEs) to expedite their expenditure.

- CPSEs surpassed their full-year revised target of Rs 6.5 lakh crore for capital expenditure in FY23, achieving more than 100% of the target.

Increased focus on public capex aiding crowding in of private capex

- According to the CMIE Capex Database, new private investment proposals in FY23 showed significant growth of 78% compared to the previous year.

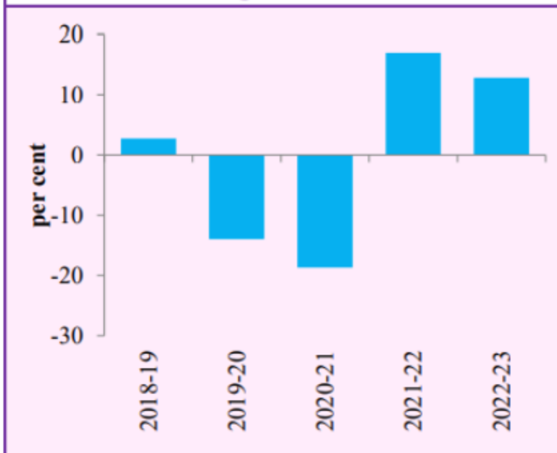
- Real sector indicators of investment activity, such as capital goods production (IIP - capital goods) and import of capital goods, also experienced robust double-digit year-on-year growth during FY23.

- Financial data from a consistent set of listed companies indicate a broad-based private capital expenditure growth of 22% in FY23, as reported by Axis Bank Research.

- The RBI's Order Books, Inventories, and Capacity Utilization Survey revealed that capacity utilization in the manufacturing sector increased to 74.3% in Q3:2022-23, compared to 74.0% in Q2:2022-23.

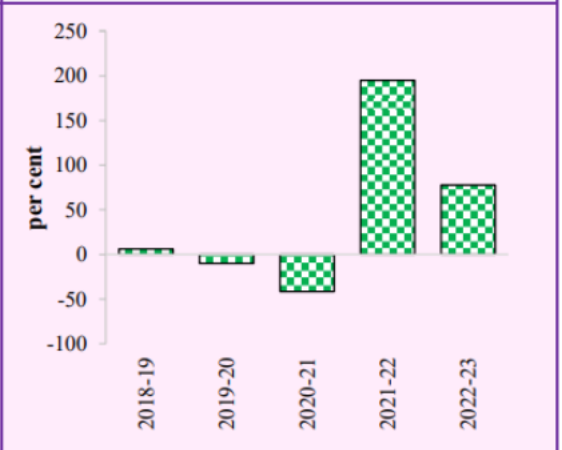
- The combination of higher capacity utilization and double-digit growth in non-food bank credit in FY23 indicates a positive intent from the private sector to undertake fresh investments in the near future.

Double-digit Capital goods production growth



Source: MoSPI

Growth in private investment in FY23



Source: CMIE Capex Database

Growth Outlook for FY24

The Indian economy has continued its momentum from FY23 into the current fiscal year, with high-frequency indicators reflecting a healthy state of the economy. Urban demand remains resilient, as seen in higher auto sales, fuel consumption, and UPI transactions. Rural demand is also recovering, with solid growth in two and three-wheeler sales. GST collections and the Purchasing Managers' Index for the manufacturing and services sector show ongoing expansion. Globally, economic activity has improved in the second quarter, as indicated by the development of the global Composite PMI. However, factors like geopolitical stress, financial system volatility, stock market corrections, El-Nino impact, modest trade activity, and FDI inflows due to weak global demand could constrain growth and challenge India's outlook for FY24.

India's macroeconomic management has been commendable Despite unprecedented global challenges and domestic balance sheet issues in the banking and corporate sectors. It has significantly contributed to enhancing macroeconomic stability and enabling a faster recovery compared to other countries. Investments in supply-side infrastructure have the potential to sustain long-term economic growth. Strong balance sheets and digital advancements can improve credit decisions, making the financial cycle longer without encountering significant dire debt challenges. India is well-positioned for sustainable growth.

For more information:
Ministry of Finance, Department of Economic Affairs
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