Economic Alert | 10 February 2014

India – FY14 GDP estimate shows sluggish growth

- **4.9% advance GDP growth estimate is better than FY13's 4.5% on statistical factors, government spending**
- **The economy remains trapped in slow-growth mode, with weak investment growth and consumption**
- **Positive election outcome is necessary for a sustained rebound in growth**

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Summary

India's official advance GDP growth estimate of 4.9% for FY14 (year ending 31 March 2014) beat expectations, including our 4.7% estimate. It is higher than FY13 GDP growth of 4.5%. However, we think this improvement is illusory, as FY14 growth was pushed up by data revisions to FY12 and FY13 GDP. Normalising the data for all years for statistical anomalies (explained in detail below) is likely to confirm that growth lost momentum in FY14 relative to FY13.

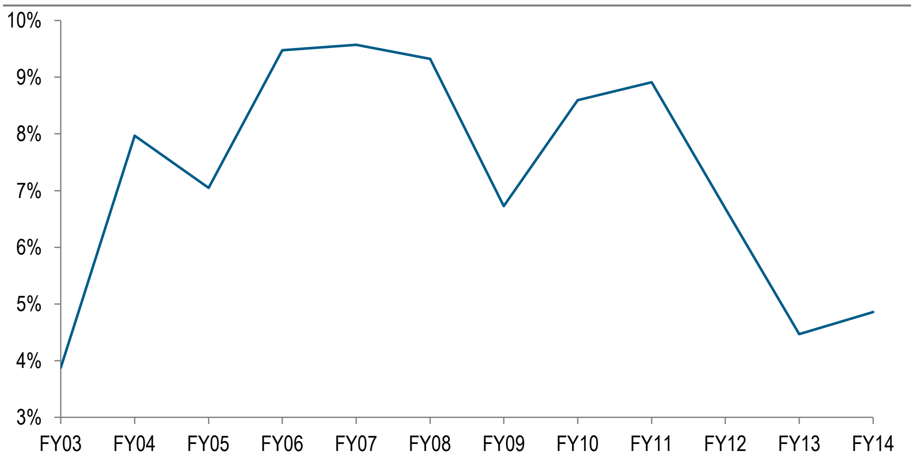
Even without these statistical adjustments, the GDP breakdown offers little reason for cheer. Consumption and investment, which contribute more than 90% of GDP, slowed markedly, according to advance estimates from the Central Statistical Organisation (CSO). Non-agricultural GDP excluding government expenditure also reveals sluggish private-sector activity. Our view that India's growth remains trapped in a low range remains intact.

We maintain our FY14 GDP growth forecast of 4.7% for now. The government spending cuts that are required to meet the FY14 fiscal deficit target of 4.8% of GDP have yet to hit real-sector activity. The CSO's advance GDP estimate is extrapolated from available economic data for the first eight to nine months of the fiscal year. The first estimate based on data for the full 12 months will be released in May 2014. Government expenditure was not cut in the first nine months of the fiscal year, so the adverse impact of cuts is likely to be concentrated in the final quarter of FY14.

The outcome of the May 2014 elections will hold the key to a sustained growth revival. While we expect FY15 GDP growth to improve marginally to 5.3% from 4.7% in FY14, an unexpected election outcome poses risks to our forecast on both sides.

Figure 1: Growth gains lost over a decade

GDP, % y/y



Source: CEIC, Standard Chartered Research

Highlights of the GDP release

Non-agriculture GDP excluding government expenditure slowed further, highlighting growth pains in the private sector

The statistical pull

The FY14 estimate received a statistical boost from data revisions to FY12 and FY13 GDP. On 30 January 2014, the CSO released its first revised estimate for FY13 and its second revised estimate of FY12 GDP. FY12 GDP growth was revised up to 6.7% from 6.2% due to the incorporation of more comprehensive data on the industrial sector (the Annual Survey of Industries, or ASI). The ASI data is not yet reflected in the FY13 growth figure, as it is available only with a two-year lag. As a result, FY13 GDP growth appeared weak.

Uninspiring GDP details

- Better growth in the agriculture sector was an important driver of the growth improvement in FY14 over FY13. This was in line with expectations, as monsoon rains were better this year. Industrial growth remained a drag on the overall number, slipping further to 0.2% from 0.9% in FY13.

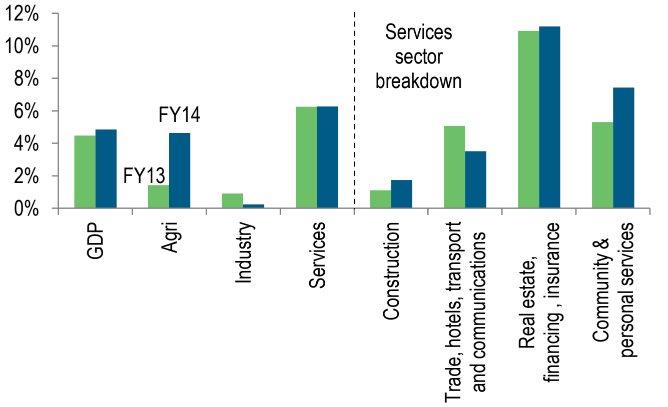
- Sluggish growth in private-sector activity is evident in non-agriculture GDP excluding government expenditure, which slowed to 4.5% in FY14 from 4.9% in FY13.

- Government expenditure growth, as captured in the 'community, social and personal services' category, improved to 7.4% in FY14 from 5.3% in FY13, according to the advance estimate. Although we expect nominal government expenditure to grow 12-13% in FY14, versus 8% in FY13, real GDP growth for this category might be below 7.4%. Government expenditure grew 17.4% in the first nine months of FY14, and the advance estimate is likely to have extrapolated a similar trend for Q4-FY14. However, with the government likely to cut spending in Q4 (by INR 700-800bn, we project), the advance estimate might overestimate growth in the 'community and personal' services category. Also, the advance numbers do not capture the adverse impact of these cuts on the rest of the economy. This impact will be more pronounced on the private sector, and may lead to a downward revision when the first estimate of FY14 GDP is released in May 2014, based on data for the full 12 months.

- Both investment and household consumption lost further momentum in FY14. Investment barely grew. The CSO estimates gross fixed capital formation (GFCF) growth at 0.2%, down from 0.8% in FY13. This is a far cry from the

Figure 2: Not much joy in the details

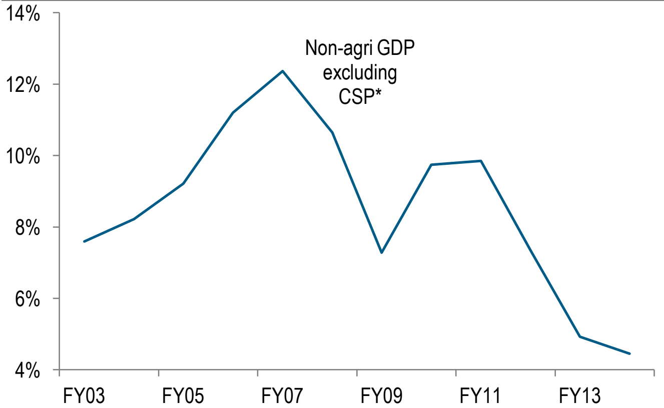
% y/y



Source: CEIC, Standard Chartered Research

Figure 3: Private-sector activity remains low

% y/y



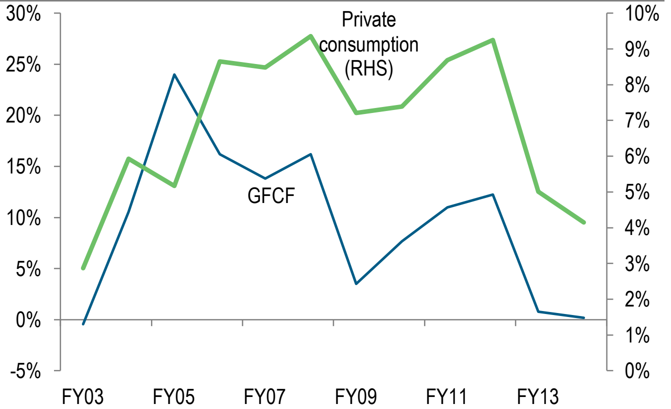
* Community, social & personal services; Source: CEIC, Standard Chartered Research

strong-double-digit growth seen in the pre-crisis period. GFCF growth at nominal current prices slipped below 30% for the first time since FY05. Unless the investment environment improves, gains in GDP growth look unlikely. The seeds of India's current slowdown were sown in mid-2010, when a lack of policy clarity and the slow pace of project approvals curbed investment activity and eventually overshadowed household consumption. Growth in household consumption – which contributes c. 60% of GDP – dropped by more than half to 4.1% in FY14 from 9.3% in FY12. While the government has recently taken steps to improve the investment climate, the positive impact of these measures is unlikely to be felt until election-related political uncertainty is over.

- Better global growth, and thus a narrower trade deficit, provided support, with the trade deficit shaving fewer percentage points from headline GDP growth. India has always been a net importer. However, in FY14 better exports – driven by improved global growth and slower imports as a result of lacklustre domestic activity – reduced the trade deficit and provided support to headline GDP.

Figure 4: Slow investment takes a toll on consumption

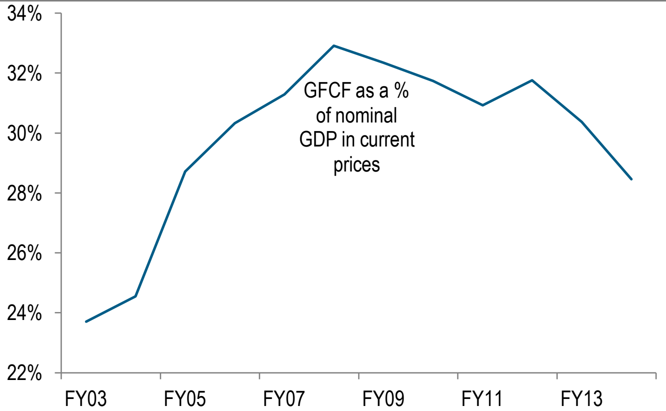
% y/y



Source: CEIC, Standard Chartered Research

Figure 5: Investment revival is needed

% of nominal GDP



Source: CEIC, Standard Chartered Research

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