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ECONOMY OBSERVER

JULY 2023

Monsoon may disrupt inflation calculations – Dun & Bradstreet

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> Irregular rainfall has disrupted the supply chain of cereals and vegetables and the consequent increase in prices is expected to further amplify inflationary pressures, thereby delaying the possibility of a rate cut in 2023. Lending rates are likely to remain elevated this year. Despite the rising lending rates, the overall bank credit is growing in double digits. This should not undermine the uneven pace of credit growth across different sectors which points to the underlying challenges faced by some of them. On the other hand, growth in personal loans, vehicle loans and credit card debt show the healthy consumer demand in the economy. Nonetheless, given the steep increase in the lending rates for personal loans, unsecured credit could see an increase in bad asset.

Real Economy

Dun & Bradstreet expects the Index of Industrial Production (IIP) to remain robust, supported by the improvement in overall consumer demand. Strong growth in infrastructure and construction goods since November 2022 reflects healthy investment activity in the economy and will continue to support industrial production even as exports remain weak. Nonetheless, the monsoon remains a major risk to industrial output. Dun & Bradstreet expects the Index of Industrial Production (IIP) to have grown by 8.0% - 8.50% during June 2023 partly due to the low base of the previous year.

Price Scenario

Dun & Bradstreet expects retail inflation to remain elevated given the food supply chain, especially cereals and vegetables, has been disrupted by an intense heatwave followed by heavy rainfall. The progression of the monsoon and the trend of Kharif sowing will play a crucial role in determining inflation in the coming months. The recent increase in food prices is expected to amplify inflationary pressures and may delay a policy rate cut in the short term. On the other hand, wholesale inflation is likely to remain negative due to the high base of the previous year and the decline in global commodity prices. Dun & Bradstreet expects the Consumer Price Inflation (CPI) to be in the range of 4.3% - 4.5% and Wholesale Price Inflation (WPI) to be around (-) 3.3% - (-) 3.2% in July 2023.

Money & Finance

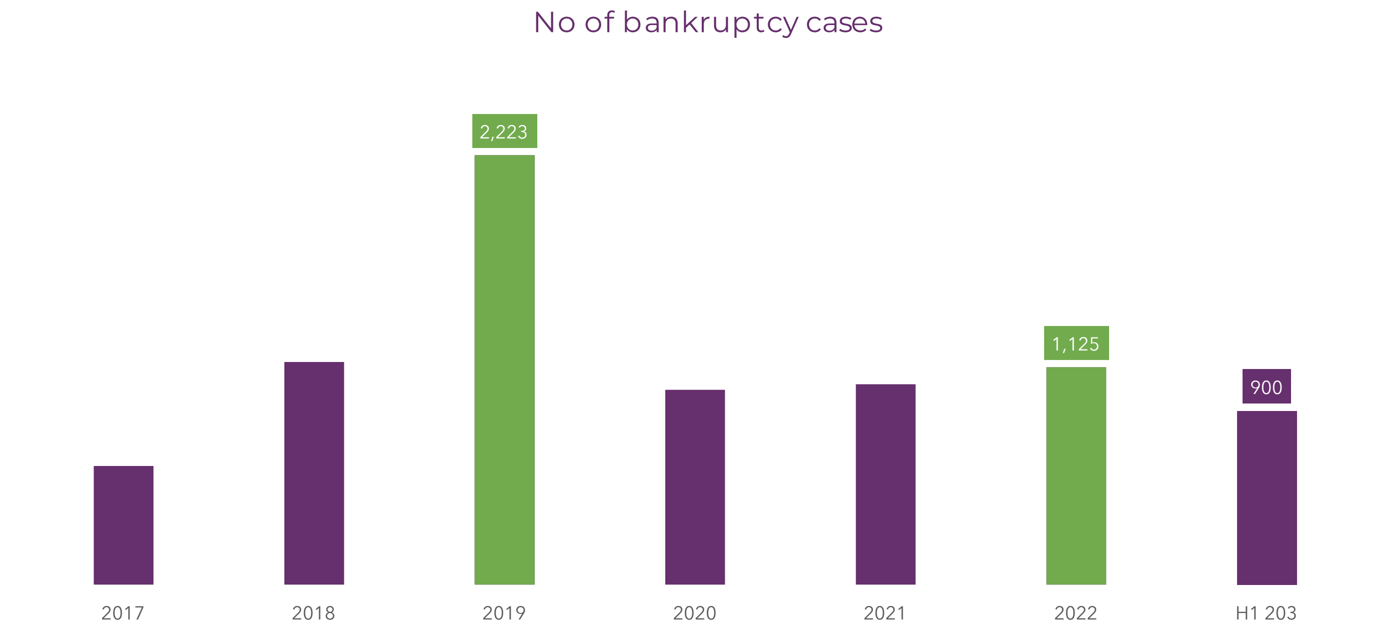
The impact of uneven rainfall and weather-related uncertainties followed by festival related demand from September 2023 is likely to keep inflation elevated, thereby pushing the possibility of a policy rate cut to early next year. This would keep bond yields elevated. Furthermore, the expected rate hike by the US FED and the consequent rise in US treasury yields will also prevent the yields from moderating. Dun & Bradstreet expects the 15-91-day Treasury Bills yield to remain at around 6.7%-6.72% and 10-year G-Sec yield to be 7.08%-7.10% for July 2023.

External Sector

While the net Foreign Institutional Investor (FII) inflows and the narrowing of the trade deficit will continue to support the rupee, it is expected to remain range bound given the interventions by the Reserve Bank of India. Dun & Bradstreet expects the rupee to remain at around 82.1 - 82.2 per US$ during July 2023.

D&B's Economy Observer Forecast			
Variables	Forecast	Latest Period	Previous period
IIP Growth	8.0% - 8.5% June-23	5.2% May-23	4.5% April-23
Inflation WPI	(-) 3.3% - (-) 3.2% July-23	-4.12% June-23	-3.48% May-23
CPI (Combined)	4.3% - 4.5% July-23	4.81% June-23	4.31% May-23
Exchange Rate (INR/US$)	82.1 - 82.2 July-23	82.23 June-23	82.34 May-23
15-91 day T-Bills	6.70% - 6.72% July-23	6.73% June-23	6.62% May-23
10 year G-Sec yield	7.08% - 7.1% July-23	7.05% June-23	7.01% May-23
Bank Credit	17.5% - 18.00% July-23	16.24% June-23	15.52% May-23

Bankruptcy levels in 2023 will remain below 2019



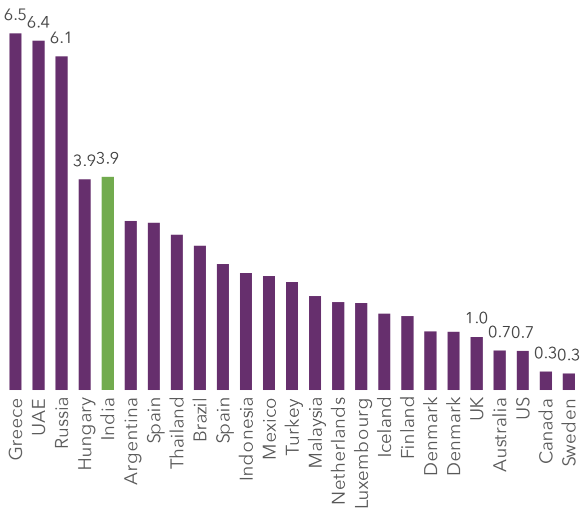
Source: RBI

Bankruptcy cases in India witnessed modest increase in 2022 from the previous two years but remained substantially lower than 2019. Despite international spillovers and a challenging global environment, sound macroeconomic fundamentals helped India navigate the difficult external environment.

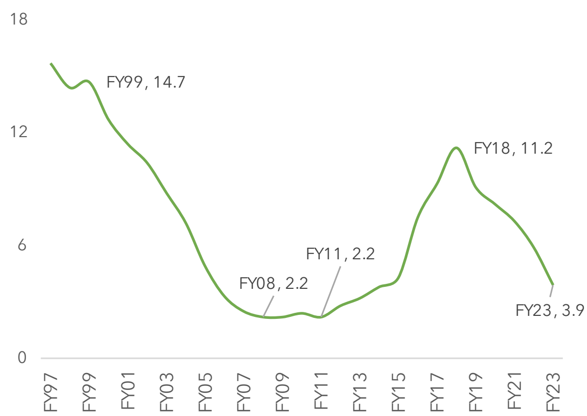
- As on 2022, of the total number of cases admitted under corporate insolvency resolution process (CIRP), 39% were from the manufacturing sector, followed by real estate (21%) and construction (11%). 57% cases were open at the end of 2022. The average time taken for closure of Corporate Insolvency Resolution Process (CIRP) yielding liquidation was 437 days. The goal of a time-bound liquidation process (180 days) as envisaged in the Bankruptcy Law Reforms Committee (BLRC) report is thus yet to be achieved.
- To strengthen its insolvency resolution process, India has proposed more than 40 amendments to its insolvency law, which could impact how recoveries are shared among creditors.
- In 2023, bankruptcy cases in India have edged up higher in H1 2023 as global economic conditions worsened; the global economy appears set to achieve lower growth than the recorded figures in 2022. Unfortunately, Asia Pacific's promising growth narrative has been overshadowed by a decrease in merchandise exports. The eurozone economies have slid into a recession. India’s exports were also impacted exports recorded a decline from October 2022 to June 2023 with the exception of January 2023.
- The multi-year low gross NPA level, decline in restructured assets in the banking system coupled with the resilient demand in the economy might lead to a moderation in the bankruptcy cases during the second half of 2023.

Non-Performing Assets declined to 9-year low

Non-performing assets (NPA) of emerging and developed countries in 2022



NPAs over the years



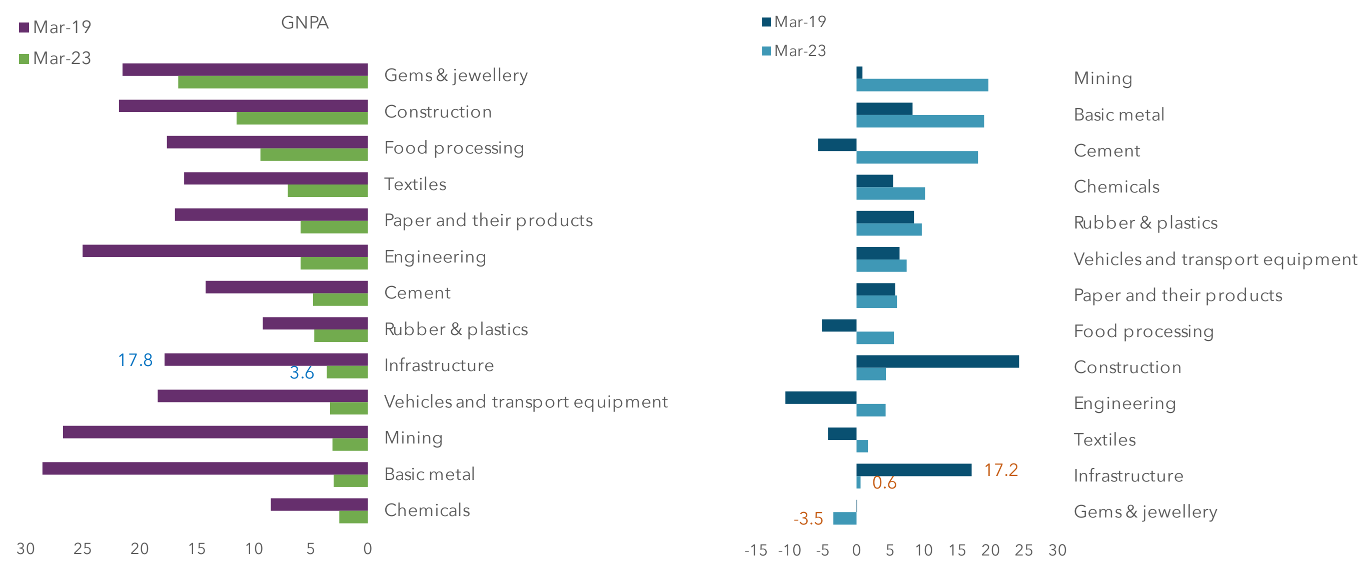
Source: Reserve Bank of India (RBI) and Haver Analytics

Gross non-performing assets (GNPA) ratio in the banking sector steadily decreases to a 9-year low of 3.9% in March 2023; NNPA drops to 1%, lowest in 15 years.

- Indian banks' NPA ratio, was once the worst among emerging economies; almost one in 10 loans had turned bad in 2019.
- NPA levels have continued to decline after that. The decline in gross NPAs in 2023 can be attributed to post-Covid economic recovery besides the expansive Asset Quality Review conducted by the RBI in 2016 which was followed by years of provisioning and insolvency proceedings, strengthened risk management and underwritings.
- The asset quality of MSME portfolio in SCBs significantly improved during FY23; GNPA ratio dropped from 9.3% in March 2022 to 6.8% in March 2023.
- Notably, there has a substantial annual write-off of NPAs by banks, totaling around Rs 10 trillion since FY17 during FY23, which also contributed to decline in NPA levels.
- After write-off, banks have been able to recover about Rs 6.5 trillion, resulting in a recovery rate of only 13%.

Sector-wise data shows bank credit in the infrastructure sector did not pick up in FY23 even as NPAs dopped significantly

A glance at the NPA ratio and bank credit in major sectors



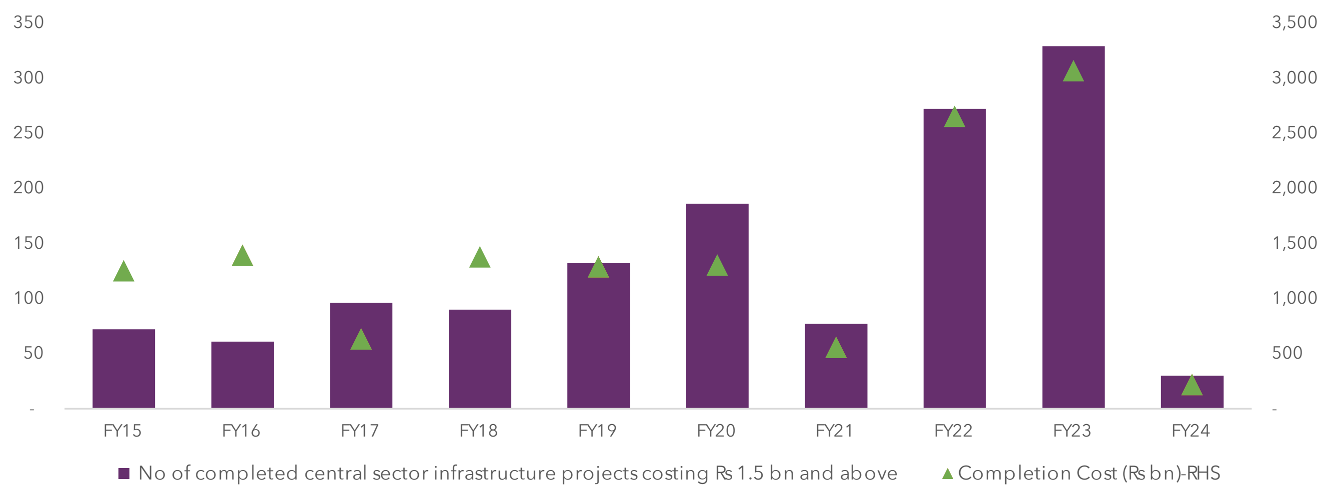
Source: RBI

In FY23, the gems & jewellery and construction sectors experienced elevated GNPA ratios, although they were lower than the levels before the pandemic. Meanwhile, bank credit to these sectors remained subdued when comparing 2023 to FY19. It is noteworthy that despite significant improvement in the GNPA ratio within the infrastructure sector since the pandemic, bank credit remains notably limited, suggesting, investment to have been largely shouldered by the government

- Across major sectors, there has been a widespread enhancement in asset quality for SCBs, as indicated by a consistent reduction in the ratio of stressed advances over the years.
- The twin balance sheet issue (corporates and banks) largely resolved, have triggered significant credit growth and healthier balance sheets contributing to the decline the GNPA ratios.
- Nevertheless, even with the recent expansion of credit, India's credit-to-GDP gap has stayed negative since March 2013, indicating subdued credit utilization in comparison to its counterparts.

Expenditure in high value (Rs 1.5 bn and above) government infrastructure projects rose in FY22 and FY23

Big ticket government infrastructure projects

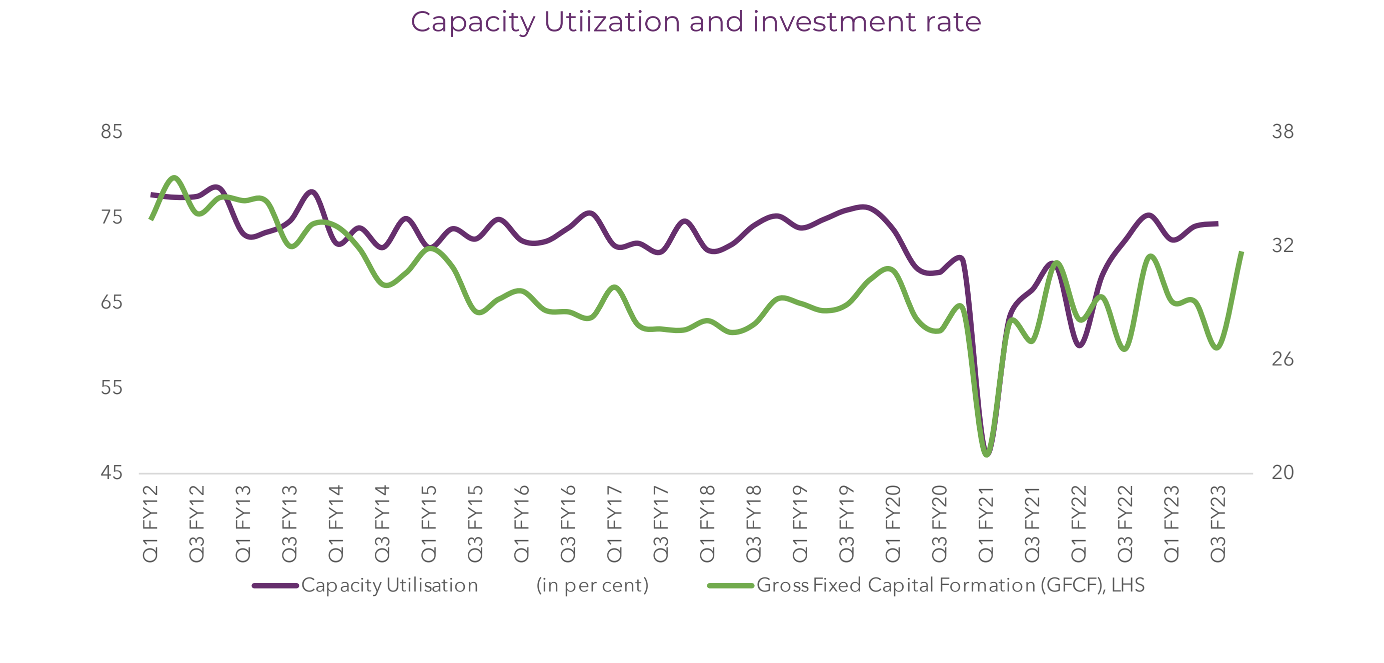


Source: Ministry of Statistics and Programme Implementation Infrastructure and Project Monitoring Division

The number of high ticket infrastructure projects executed by the Central Government has increased five-fold and doubled in value terms during FY15 to FY23. The cost and time overrun is also at a multiyear high

- Based on information available on the Online Computerised Monitoring System (OCMS) for the central sector infrastructure projects with a cost of Rs 150 crore and above, demonstrate that the road transport sector had the highest number of projects (52%), followed by railways (12%), petroleum (10%), coal (8%), power (5%), and a solitary project each in renewable energy, shipping and ports, and defense, among others at end Match 2023.
- As of March 2032, a significant 56.3% of high ticket Union Government projects experienced delays, marking the highest rate within the last decade (FY14-FY23). In 2018, the proportion of delayed central government projects had reached a nadir at 19.3%. On an average, the time overrun is over three years (37.79 months). Sector-wise civil aviation (96%), higher education (71%), and power (69%) witnessed a higher share of delayed projects.
- The infrastructure projects are now expected to incur costs of 22.02% higher than their initial estimates, which translates to an additional expenditure of Rs 4.6 trillion.
- The time overrun can be attributed to various reasons, including delays in land acquisition, obtaining forest/environment clearances, infrastructure support, and linkages, project financing tie-ups, finalization of detailed engineering, scope changes, tendering delays, equipment supply setbacks, law and order issues, unexpected geological challenges, delays in obtaining clearance from local authorities besides others.

High-capacity utilization signals investment revival in FY24



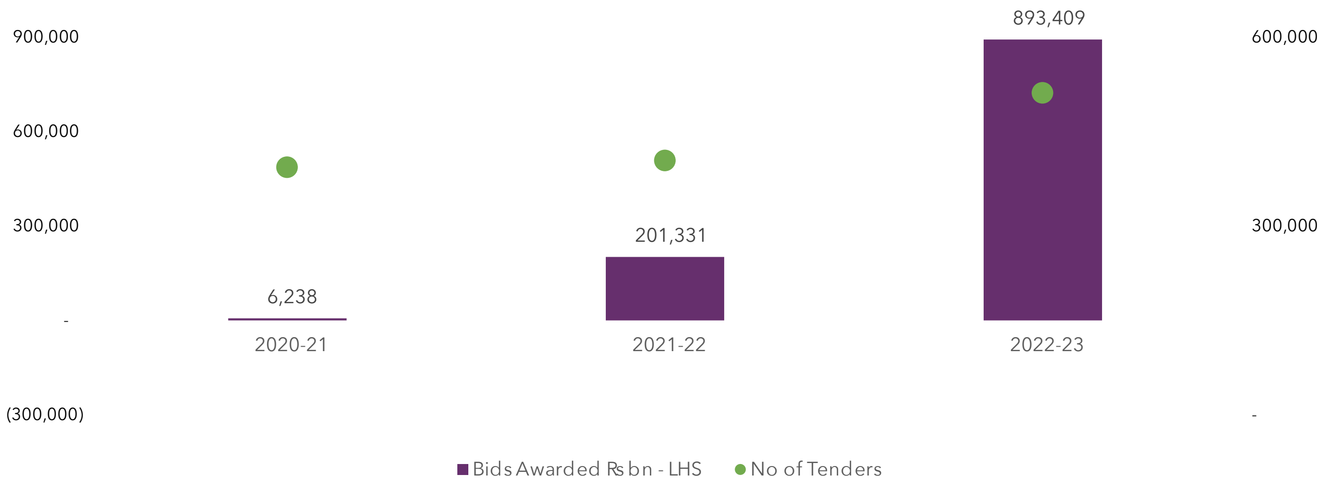
Source: Reserve Bank of India, MOSPI

Despite global headwinds, India's manufacturing sector has remained positive during the first quarter of 2023-24 (April-June) and has found its existing average capacity utilization at a robust 74.3% in Q3 FY23, up from pre-pandemic level (Q1 FY20) of 73.6%.

- Capacity utilisation has held above the 72-per-cent mark since Q3 FY22, indicating that the manufacturing activity is taking place at a brisk pace. This has brightened the prospects for fresh investments by companies. High capacity utilization levels also mean that companies will have to go for capital investments to increase capacities if demand increases further. Capacity utilisation is the ratio of actual output to the potential output that can be produced under normal conditions.
- India's overall domestic demand is expected to remain resilient. Urban demand remains robust while rural demand will lag behind owing to the impact of the uneven monsoon in the short term and then pick up sequentially.
- Continued improvement in consumer confidence also points to uptick in demand going ahead, according to surveys conducted by the Reserve Bank of India. This will be aided by the moderation in the inflationary situation in India.
- Since the second surge of the Covid-19 pandemic, consumer confidence in the present period has consistently increased compared to a year ago. Notably, the Current Situation Index (CSI) has recently advanced by 1.5 points in the latest May 2023 round of the bi-monthly survey.
- This can be attributed to improvement for economic situation, employment, price and income, except for essential spending.
- Additionally, outlook of households for the upcoming year has also shown a growth, despite a slight decline in March 2023.

Promising investment growth is also indicated by India's procurement data for Central Government

Central government bids awarded (works, services and goods)



Source: https://eprocure.gov.in/

FY24 is expected to be a strong year for investments in India, as indicated by data from the Government's eProcurement System.

- It appears that FY24 will continue to be a strong year with regard to infrastructure investments, indicated by the aggregate contract value for the three main types of bids awarded (works, services and goods) in FY23. This value surged four-fold, reaching Rs 893 trillion in FY23 from FY22 and an astonishing 143-fold rise since FY21, the year marked by the pandemic.
- Furthermore, the tally of awarded tenders in FY23 saw a notable 30% surge compared to the preceding year.
- These trends serve to underscore the government's dedication to leveraging capital expenditure as a pivotal catalyst for propelling economic growth. Such a strategy aligns with the Keynesian doctrine of spurring infrastructure to create jobs and channelise multiplier cycles.
- Demonstrating a consistent upward trajectory since the low point of 2021, the gross fixed capital formation's proportion to the GDP has exhibited steady growth. By Q1 2023, this figure had reached 31.7%, marking a considerable increase from the 21.0% recorded in Q1 2021.

WATCH OUT IN NOVEMBER 2022

The Reserve Bank of India's Bi-Monthly Monetary Policy

Watch out for Reserve Bank of India's Bi-monthly policy expected to release in August given the uncertain global conditions and central bank's focus on keeping interest rate within 4% amidst threat of inflation

Consumer Confidence Survey

RBI will publish its bi-monthly Consumer Confidence survey in August 2023, which gauges consumers' outlook on the present economic situation and their expectations for the future economy regarding aspects like price trends, employment, and spending willingness.

Quarterly Estimates of GDP for Q1 2023

National Statistical Office is expected to release Quarterly Estimates of National Income by 31 Aug that will offer more concrete data on the trajectory of the Indian economy in Q1 FY24

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