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ECONOMY OBSERVER

NOVEMBER 2023

Central Bank's Stricter Rules Signal an Era of Increased Borrowing Costs for Consumers on Unsecured Loans – Dun & Bradstreet

"Expect a potential uptick in GDP growth this December quarter driven by strong festive demand, increased government spending, and expanding private investment. Despite these positive factors, challenges persist due to high food inflation. It's unlikely that retail inflation will quickly fall below 4%, mainly due to uncertainties in global crude oil prices. As a result of incomplete transmission from previous rate hikes, lending rates are set to keep rising. Consumers should brace for higher borrowing expenses due to stricter capital regulations for unsecured loans.

> Anticipating a surge in GDP growth this December quarter due to robust festive demand, government spending, and growing private investment. However, challenges persist with elevated food inflation and an unlikely quick return of retail inflation to below 4%, given global crude oil price uncertainties. Lending rates to continue rising as the transmission of previous rate hikes remains incomplete. Consumers can expect higher borrowing costs following tightened capital norms for unsecured loans.

Real Economy

Festive demand, pre general election expenditure boost, government spends on infrastructure, and uptick in private capex to have uplifted industrial activity in October 2023. Dun & Bradstreet expects the Index of Industrial Production (IIP) to have grown by 9.5% in October 2023.

Price Scenario

Global food and crude oil prices continue to keep inflation elevated. Food inflation remain above the ‘comfort’ level and some of the food articles continue to witness uptick. Global oil prices have rallied on geo-political concerns (Israel Hamas conflict), risk of the additional sanctions on Russia and supply cuts from OPEC. Dun & Bradstreet expects the Consumer Price Inflation (CPI) to be 5.4% and WPI to be around 0.5% for November 2023.

Money & Finance

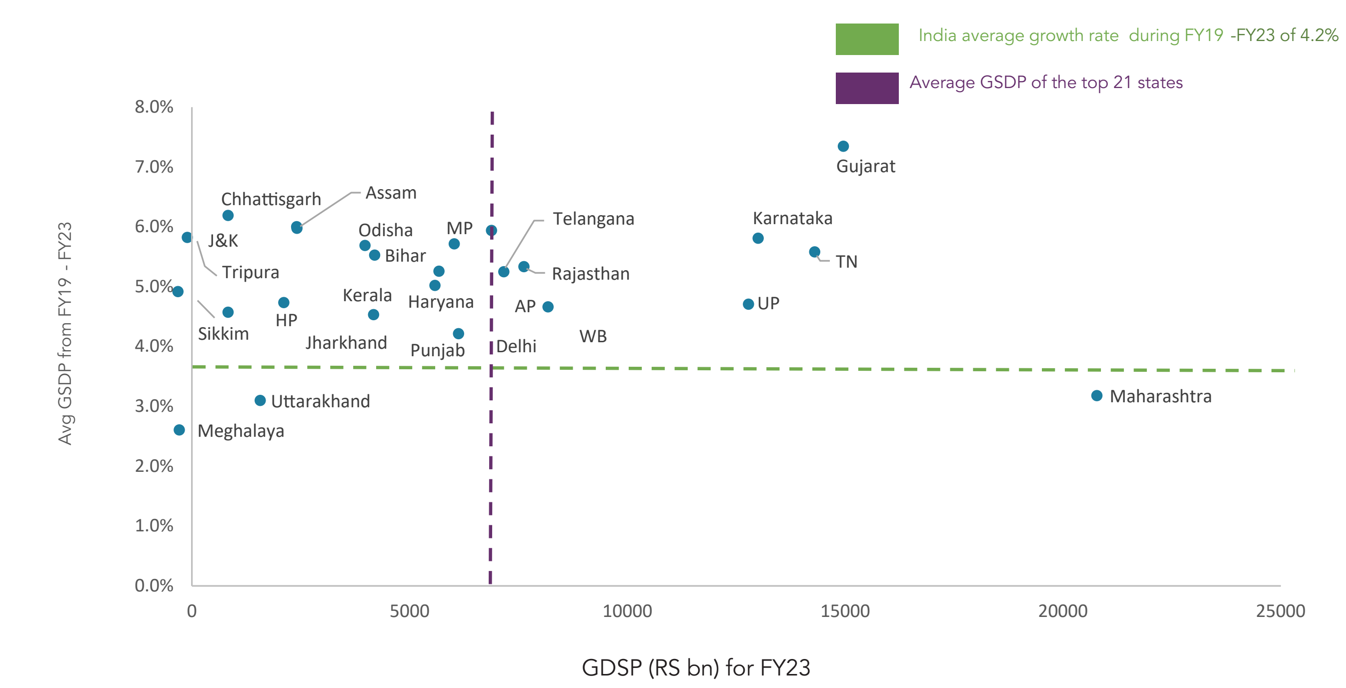
Inflationary pressures along with higher US Treasury yields and the dollar strength to keep yields elevated. Dun & Bradstreet expects the 15-91-day Treasury Bills yield at 6.7% and 10-year G-Sec yield to be 7.45% for November 2023.

External Sector

The hawkish stance by the US FED, elevated US Treasury yields, strength of the US dollar amid high crude prices would lead to further depreciation of rupee. Despite RBI's interventions, drawing down foreign currency reserves from USD 603 billion in July to USD 586 billion in October 2023, the rupee depreciated to its lifetime low in the month of November. Dun & Bradstreet expects the rupee to remain at 83.3 per US$ in November 2023 and 83.5 per US$ in December 2023.

D&B's Economy Observer Forecast			
Variables	Forecast	Latest Period	Previous period
IIP Growth	9.5% October-23	5.8% September-23	10.3% August-23
WPI Inflation	0.5% November-23	(-)0.52% October-23	(-)0.26% September-23
CPI (Combined) Inflation	5.4% November-23	4.87% October-23	5.02% September-23
Exchange Rate (INR/US$)	83.5 December-23	83.3 November-23 (est)	83.24 October-23
15-91 day T-Bills	6.7% November-23	6.89% October-23	6.6% September-23
10 year G-Sec yield	7.45% November-23	7.35'% October-23	7.17% September-23
Bank Credit	20.5% November-23	19.7% October-23	20.0% September-23

Economic performance and growth opportunity in states

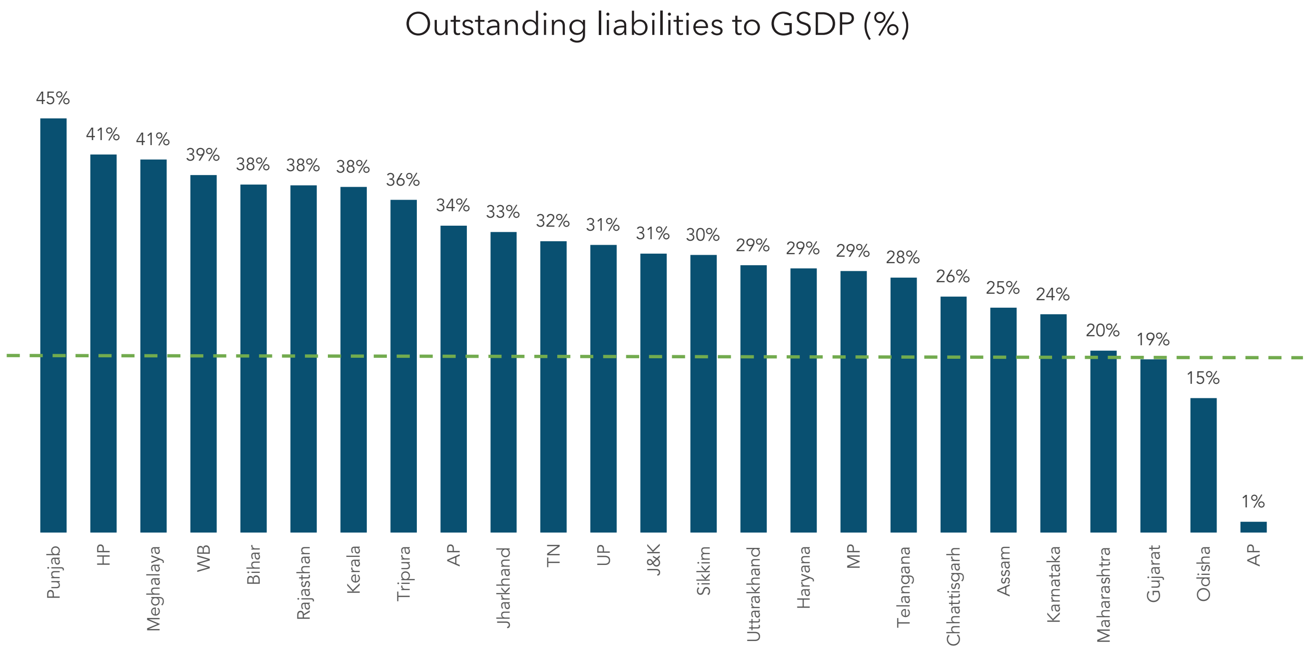


Source: RBI

21 of 25 large states recorded above national average State Gross Domestic Product (SGDP) growth during the last five years.

- India grew at an average rate of 4.2% during the last five years i.e., FY19 to FY23 (lower than expected, mainly due covid impact in FY21).
- While Gujarat, J&K, Chhattisgarh, Assam, Telangana, Tripura, and Karnataka recorded higher growth rate (above 5.5%), registering consistent high growth post pandemic, Maharashtra and Uttarakhand and Meghalaya were an outlier, growing by only around 3%.
- Gujarat, Karnataka, and Tamil Nadu outshine their peers, in terms of growth despite their size.

Outstanding liabilities of states

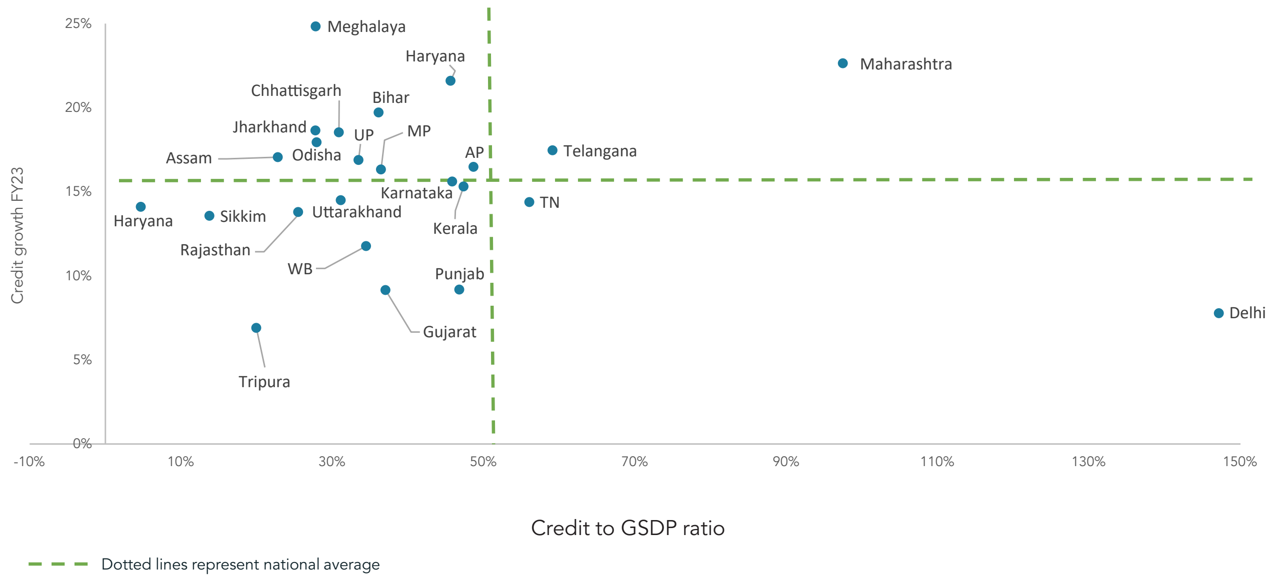


Source: RBI

In FY23, 21 of 24 states is estimated to have breached the 20% threshold limit of debt-to-SGDP ratio.

- Tamil Nadu, Uttar Pradesh, Maharashtra, West Bengal, Rajasthan, Karnataka are the top 6 states with hight debt burden in absolute terms accounting for 50% of all the total debt of 31 states and Union territories.
- The debt-to-GDP ratio of Indian states influences credit ratings, budgetary decision and fiscal strategies.
- The FRBM Acts of states usually specify limits on the outstanding liabilities as a percentage of GSDP. Typically, these limits were set at 25% of their GSDP. In 2017, the FRBM Review Committee recommended a limit of 20% of GDP on aggregate for states.
- Total outstanding liabilities of states is estimated to have increased by 12% in FY23. In recent years, outstanding liabilities of states have increased partly due to large one-time expenditure debt takeover under the UDAY scheme, and increased dependence on borrowing to fund expenditure since FY20.

Credit growth of states

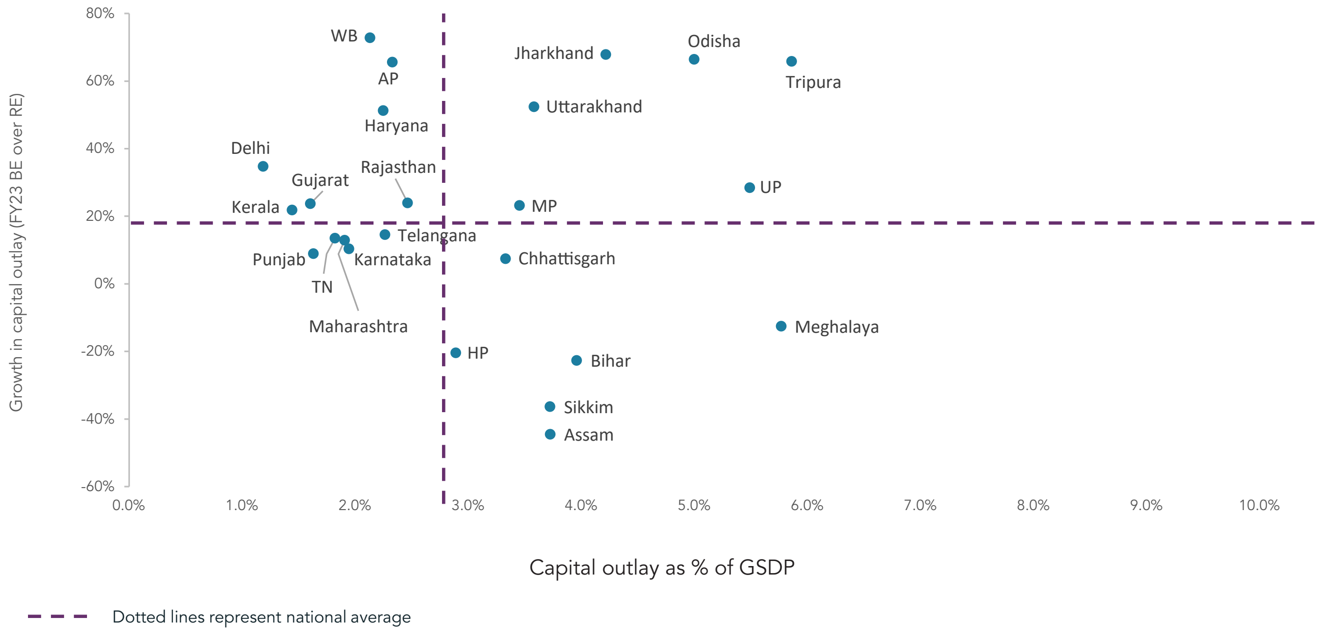


Source: RBI

While India's credit growth remains robust, credit penetration i.e., credit to GDP ratio at 52% is remarkably below the world average (148%), and lowest among its Asian peers — China (185%), South Korea (175%), and Vietnam (126%).

- State-wise penetration of bank credit remains quite low and uneven. Bank credit to GSDP ratio for most of the states remains below the national average.
- States like Gujarat, Rajasthan, West Bengal, Uttar Pradesh, Madhya Pradesh and Meghalaya have credit to GSDP ratio below 40% even as credit growth remains high at double digits.
- States with low outstanding total debt (as % of GSDP) have higher penetration of bank credit (credit to GDP ratio) for example Maharashtra and Telangana.
- Concomitantly, states such as Punjab, West Bengal, Himachal Pradesh and Uttarakhand has higher debt and low credit penetration underlying the crowding out effect of the public debt.
- There is still an unmet need for formal enterprise credit in India beyond those currently served by the corporate bond market and banks indicated by the low bank credit penetration.
- Low bank credit penetration also reflects the high cost of credit that firms, especially MSMEs, face to source credit from non-banking sources.
- The corporate bond market is an opportunity that remains sub-optimally utilized in India (14% of GDP 2022) as compared to its Asian peers like South Korea, Malaysia, Hong Kong, Singapore, China etc.

Capital outlay by states

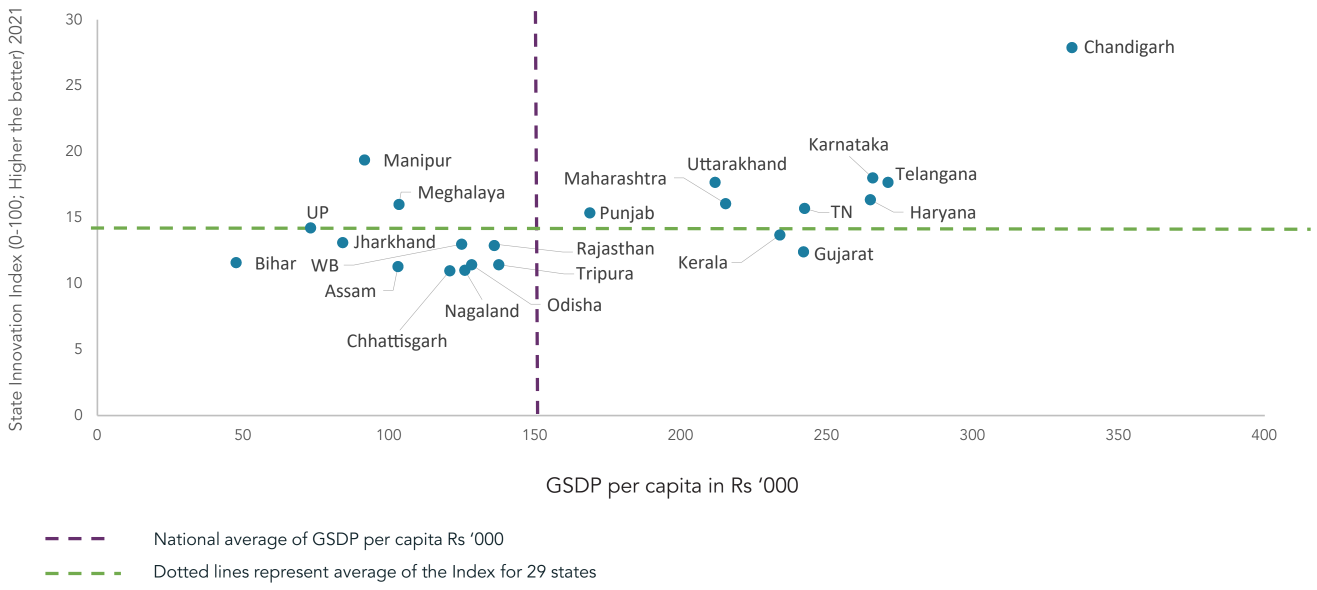


Source: RBI

In tandem with the Central Government, States have planned a higher capital spending, however, it remains low as a % of GSDP.

- Of the top 21 states, in terms of GSDP, only a few states have increased their capital outlay and allocated a higher share of capital in terms of their total income i.e. gross domestic product.
- States such as Maharashtra, Gujarat, Tamil Nadu, and Karnataka, which collectively contribute 40% to India's GDP, allocate a mere 2% of their GSDP towards capital outlay.
- On the contrary, Gujarat has both higher allocation and growth in capital outlay.
- The low state government capex indicates a reduced focus on infrastructural development.
- To boost the long-term growth prospects of various regions, the capital expenditure should increase.

State innovation index



Source: NITI Aayog, RBI

States which have a greater contribution to India's growth have shown lower innovative abilities and ecosystems.

- States like Maharashtra, Gujarat and Tamil Nadu rank far below Karnataka.
- States like Telangana and Haryana with a similar per capita income like Maharashtra or Tamil Nadu have higher innovative ability.
- Relationship between innovation and growth has a positive correlation: higher investments in innovation activities cause development and higher productivity.

PERFORMANCE OF CORPORATE BUSINESS SECTOR

Watch out for the release of the data on the financial performance of the corporate sector during the second quarter of 2023-24 drawn from abridged quarterly financial results of selected listed non-government non-financial companies by the Reserve Bank of India.

EXTERNAL DEBT

Watch out for the Quarterly External Debt Report of India for the quarter ending September 2022. Placed at US$ 624.7 billion as at end-March 2023, external debt of the country grew marginally by 0.9% (US $ 5.6 billion) over the previous year. External debt as a ratio to GDP declined to 18.9% as at end-March 2023 from 20.0% at end-March 2022. Foreign exchange reserves covered 92.6% of the external debt at end-March 2023.

STATE LEVEL ELECTIONS

Watch out for state election results. Five states will conduct elections I the month of November; Mizoram to vote on Nov 7, Madhya Pradesh on Nov 17, Chhattisgarh on Nov 7 and 17 in two phases, Rajasthan on Nov 23 and Telangana on Nov 30. Counting of votes to be held on December 3 for all five States.

Research Team

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