

Recovery, with a changed mix

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Economic growth has weighed in at a five-quarter high in the quarter ended December.

The Central Statistical Office (CSO) released the gross domestic product (GDP) data for Q3 fiscal 2018 and second advance estimates for full fiscal 2018 on February 28, 2018. To recall, the CSO had also released revised GDP estimates of fiscal 2017 on January 31, 2018, and in which some of the sectoral growth numbers had undergone substantial revision.

Quarterly growth trend

- Real GDP growth continued the upward trend and jumped to a five-quarter high of 7.2% in Q3 from 6.5% in Q2, suggesting the economy was steadily recovering from the twin shocks of demonetisation and a bumpy transition to the Goods and Services Tax (GST) regime. The jump was largely on the back of fixed investments, which grew 12% on-year, almost double the pace of 6.9% in Q2. Private consumption growth, on the other hand, slowed to 5.6% from 6.6%. Government consumption supported the overall consumption by growing at 6.1%, up from 2.9% in Q2.
- The external sector was a big drag on GDP with imports rising at 8.7% compared with a muted 2.5% growth in exports in Q3.
- On the supply side, gross value added (GVA) growth improved to 6.7% in Q3 from 6.2% in Q2, with a broad-based improvement in all sectors – agriculture (to 4.1% from 2.7%), industry (to 6.8% from 5.9%) and services (to 7.7% from 7.1%). Improvement in industrial growth in Q3 over Q2 was supported by a pick-up in manufacturing growth (to 8.1% from 6.9%) and a sharp upward movement in construction activity (to 6.8% from 2.8%). However, mining growth at -0.1% was a drag.

Changed growth mix

While the improvement in GDP growth is heartening, it is important to take cognisance of the fact that the revised annual estimates throw up a different growth mix. Broadly, industrial and agriculture sectors grew faster than estimated earlier. On the demand side, consumption grew at a slower pace, while investment growth was higher. Key takeaways from the recent GDP revisions are:

- Real economic activity in recent two fiscals was higher than estimated earlier. Looking from the supply or the production side, real GVA growth has been revised upwards – by 50 and 30 bps in fiscal 2017 and 2018, respectively (see tables at the end of the section). A sharp rise in mining and agricultural growth estimates helped push up fiscal 2017 GVA growth, whereas upward revision in construction and agriculture growth pushed up fiscal 2018 growth estimates. Since supply-side growth estimates are generally the more robust measures of economic activity, such sharp movement in these numbers is a bit startling.
- Demand-side estimates of GDP, too, saw large revisions. The biggest surprise element here has been that gross fixed capital formation (GFCF) – or fresh investments – grew much faster than anticipated earlier. Real GFCF growth for fiscal 2017 was revised to 10.1% from 2.4% earlier. This implies the share of investment in GDP – which was declining earlier – now shows a pick-up starting fiscal 2017, or in other words, the slowdown in investments, which we believed would bottom out in fiscal 2019, actually did in fiscal 2017.
- Another important observation is the slower consumption growth in the recent two fiscals. Private final consumption expenditure (PFCE), the biggest contributor to the demand-side GDP, grew at a slower pace than estimated earlier, both in fiscal 2017 and fiscal 2018. Government final consumption expenditure (GFCE) growth, which spurted to 20.8% in fiscal 2017, largely as a result of implementation of the 7th Pay Commission recommendations, has been revised down to 12.2%. In fiscal 2018, though, GFCE growth has been revised

marginally upwards. On the external front, CSO has estimated a slowdown in export growth and a rise in import growth in fiscal 2018, suggesting a drag from net trade on GDP growth. This is particularly disturbing at a time when world exports have rebounded and indicates India hasn't been able to take advantage of that due to GST-related hiccups.

Outlook

We expect the real GDP growth to rebound to 7.5% in fiscal 2019 from 6.6% this fiscal as the transitory disruption from GST implementation would wane and a low base would help. While growth would continue to be driven by consumption – with interest rates expected to remain soft, inflation under control, and implementation of 7th Pay Commission hikes at the state level. Investments, fired largely by public sector investment in infrastructure, too, would start lending a helping hand to growth. Growth would also be mildly supported by public spending (with a rural focus) in infrastructure, especially roads. The government's Rs 2.11 lakh crore bank recapitalisation plan would mean the banks would be sufficiently funded to support growth. On the external front, too, synchronised global recovery is expected to gather pace, which should help Indian exports that were held back to some extent on account of GST-related glitches.

Changes in India's growth trajectory

Earlier estimates

Supply side

Real growth (%)	FY 13	FY 14	FY 15	FY 16	FY 17	FY 18
Agriculture	1.5	5.6	-0.2	0.7	4.9	2.1
Industry	3.3	3.8	7.5	8.8	5.6	4.4
<i>o/w Manufacturing</i>	5.5	5	8.3	10.8	7.9	4.6
<i>Construction</i>	0.3	2.7	4.7	5.0	1.7	3.6
<i>Mining</i>	0.6	0.2	11.7	10.5	1.8	2.9
Services	8.3	7.7	9.7	9.7	7.7	8.3
GVA	5.4	6.1	7.2	7.9	6.6	6.1

Revised estimates

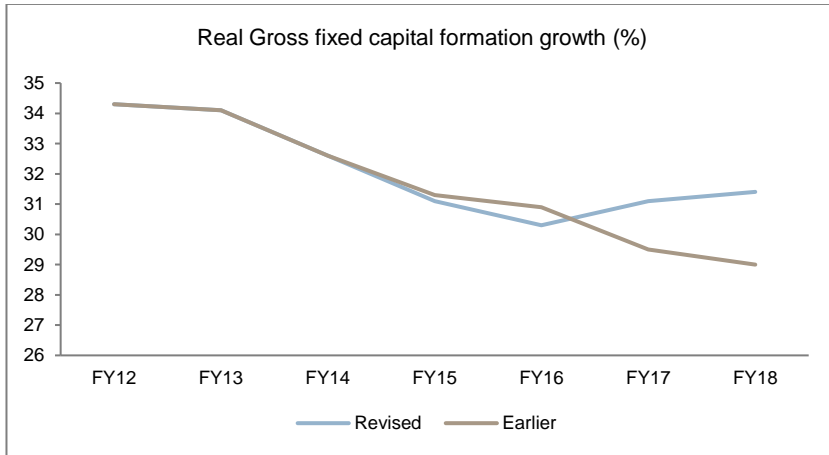
Real growth (%)	FY 13	FY 14	FY 15	FY 16	FY 17	FY 18
Agriculture	1.5	5.6	0.2	0.6	6.3	3
Industry	3.3	3.8	7.0	9.8	6.8	4.8
<i>o/w Manufacturing</i>	5.5	5	7.9	12.8	7.9	5.1
<i>Construction</i>	0.3	2.7	4.3	3.7	1.3	4.3
<i>Mining</i>	0.6	0.2	9.7	13.8	13	3
Services	8.3	7.7	9.8	9.6	7.5	8.3
GVA	5.4	6.1	7.2	8.1	7.1	6.4

Demand side

Real growth (%)	FY 13	FY 14	FY 15	FY 16	FY 17	FY 18
PFCE	5.5	7.3	6.2	6.1	8.7	6.3
GFCE	0.6	0.6	9.6	3.3	20.8	8.5
GFCF	4.9	1.6	3.4	6.5	2.4	4.5
Exports	6.8	7.8	1.8	-5.3	4.5	4.5
Imports	6.0	-8.1	0.9	-5.9	2.3	10.0
GDP	5.5	6.4	7.5	8	7.1	6.5
Nominal GDP growth (%)	13.8	13.0	10.8	9.9	11.0	9.5

Real growth (%)	FY 13	FY 14	FY 15	FY 16	FY 17	FY 18
PFCE	5.5	7.3	6.4	7.4	7.3	6.1
GFCE	0.6	0.6	7.6	6.8	12.2	10.9
GFCF	4.9	1.6	2.6	5.2	10.1	7.6
Exports	6.8	7.8	1.8	-5.6	5.0	4.4
Imports	6.0	-8.1	0.9	-5.9	4.0	9.9
GDP	5.5	6.4	7.4	8.2	7.1	6.6
Nominal GDP growth (%)	13.8	13.0	11.0	10.4	10.8	9.8

Investments bottomed out in fiscal 2016



Source: CSO

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