India Viewpoint

Year Ahead 2024: Slower growth, inflation and cuts

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GEM Economics
Asia | India

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Glossary

RBI: Reserve Bank of India
CPI: Consumer Price Index
GDP: Gross Domestic Product
MPC: Monetary Policy Committee
GVA: Gross Value Add
FD: Fiscal deficit
CAD: Current Account deficit
BoP: Balance of payments

Stable growth, steady disinflation and slow rate easing

As the world grows apart, with heterogenous and fragile growth trajectories across countries, India continues to deliver stable growth. We see growth rate in India stay stable at a 5.8% yoy (though down from FY24's 6.5% yoy), but adjusting for base effects, growth looks robust. Amidst resilient recovery, inflation is expected to soften further to 4.6% yoy on lower food inflation, deriving strength from prudent supply side measures of the government. Despite continued disinflation, CPI still has some room to achieve the 4% target and would keep deep and immediate rate cuts by the RBI at bay. We thus see slow and shallow rate easing by the RBI, only as 4% target comes in sight. Of the 22 countries that have major elections in 2024, India is an important one. While fiscal profligacy in the run up to elections is not unheard of, we believe the current government would continue to focus on further consolidation and despite some additional expenditure, meet the current year's fiscal deficit target. On the current account front, the deficit looks manageable, especially as FII debt flows come in, post the global bond index inclusion. This should allow INR to reluctantly appreciate.

Key forecasts

Real GDP growth: We expect real GDP growth to soften to 5.8% yoy in FY25 from an estimated 6.5% yoy in FY24. Sequential growth to remain strong. Agriculture & Industry to drive growth, service sector growth to fizzle.

CPI inflation: Expect CPI inflation to moderate to 4.6% yoy in FY25 from an estimated 5.4% yoy in FY24 on lower food inflation.

Fiscal Deficit: Despite poll pressures, expect fiscal consolidation to continue in FY25. See Centre's fiscal deficit narrow to 5.3% of GDP in FY25 from an estimated 5.9% of GDP in FY24.

Current Account Deficit: See CAD widen modestly to US$65bn (1.6% of GDP) in FY25 from an expected US$40bn (1.2% of GDP) in FY24. Bond index inclusion led flows to support capital account.

RBI monetary policy: See RBI MPC easing rates by 50bp in FY25 in 2HFY25.

Key risks: Polls and higher for longer rates globally

The most important event in 2024 is the national elections scheduled to take place in May'24. Currently, Mr. Modi's BJP is set to be re-elected for a third consecutive term. However, the strength of majority and vote share are important parameters to ascertain how smoothly can future reforms be undertaken. The other key risk is the higher for longer rates globally that could weigh in on the potential easing cycle by the RBI, which anyway is expected to be slow and shallow.

Global macro backdrop: Growing apart, cutting together

Our global economics team is calling for a soft landing. The US economy sees a significant soft patch but avoids a hard landing. The Euro Area continues to stagnate until the real income squeeze starts to fade in late 2024. China improves on the back of concerted stimulus action. The BoJ is able to make progress on exiting unconventional policies. All in, a very benign backdrop. As a base case this will deliver lower rates and lower rate vol. An end to US growth exceptionalism should also allow the dollar to give up its overvaluation.

That said, we find it much easier to come up with downside risks than upside risks, particularly in China and Japan. Japan needs to extricate itself from unconventional policy without destabilizing its own, let alone the global bond market. China needs to avoid Japanification to not become a drag on the world economy.

While the growth story is heterogenous, disinflation narrative is rather homogenous. We see global CPI inflation soften from 4.2% in 2023 to 3.1% in 2024. This paves the way for coordinated cuts by central banks. We expect the US Fed to start cutting rates from Jun'24 by 25bp each quarter. ECB is seen to be cutting rates from 2QCY24 by 75bp, taking end-2024 policy rate to 3.25%. BoJ is expected to end NIRP+ YCC by Apr'24.

As for FX, our strategists expect the USD to broadly weaken by 5-10% next year. But should the US economy see a hard landing, the USD could also weaken by more than our baseline. It will be hard for fiscal policy to loosen further, and the Fed could cut rates earlier and faster. For now, we believe any USD depreciation in 2024 is likely more cyclical than structural.

For the CNY, our base line forecast is for USDCNY to reach at a peak of 7.55 in 1Q24, because of wide interest rate differentials against the US and the artificial support the PBoC has provided the RMB in 2H23 which we think will be unwound. Regardless of the geopolitical situation, we think the RMB can weaken on a trade-weighted basis.

Our global team expects improving geopolitical backdrop vs seen in CY22/23 (conflicts across two resource rich subcontinents, Hamas/Israel & Russia/Ukraine), as 36 nations, representing 63% of GDP, are likely to head into elections over the next 15 months. Incumbent govts globally are likely to improve geopolitics near term to focus on domestic issues. We believe CY24 could see reduced geopolitical tensions between US & China, contained Middle East as well as the Russia-Ukraine conflicts. This could be positive for global economy as well as markets.

Our commodities analyst expects Brent to average US$90/bbl for CY24 (see note), up 8.4% YoY, above CY23 average of US$83. Expect a more manageable crude vs the risk that even a modest military escalation in the Middle East could rattle the oil markets and Brent could jump to US$130/bbl. Energy prices are a channel for geopolitics to manifest in macro data, with Europe's gas crisis serving as a recent example.

While the relationship between gold and wars has not always been straightforward, we would caution against discounting the turmoil in the Middle East entirely. Indeed, the concept of "energy fragility" has again reared its head. We recently outlined four scenarios for the oil market, expecting prices to hit $150/bbl or higher if a broadening regional conflict resulted in damage to Middle East energy infrastructure. All else equal, gold could rally to $2,400/oz if this known unknown came to pass. Of course, beyond higher oil prices, the yellow metal would also be impacted by rates, which would in all likelihood fall initially on a flight to quality.

Real GDP growth to slow to 5.8% yoy in FY25

We forecast India's real GDP growth to moderate further to 5.8% yoy in FY25 (Apr'24 to Mar'25, Exhibit 2) from an estimated 6.5% yoy in FY24. This is below trend in year-on-year terms due to base effect normalization. Sequentially, we expect recovery to stay strong. That said, slower global growth in 2024 vs 2023 (Exhibit 1) is expected to weigh on India's growth trajectory too. As for drivers, agriculture and manufacturing growth are expected to drive overall GDP growth in FY25 even as services growth slows at margin. Agriculture growth is estimated to go back to trend in FY25, given favorable base and expectation of a normal monsoon. Easy monetary policy and conducive investment environment created by government's capex push should crowd in private investment and that is expected to drive growth in manufacturing GVA. Services sector growth is expected to slow as latent demand diminishes and construction activity moderates in an election year.

Real GDP surprised on the upside, growing by 7.6% yoy in Sep'23. This reversed the big miss vs estimate that we saw in Jun'23 quarter. Despite slower agriculture growth, sharp increase in manufacturing GVA and robust services sector growth (led by construction) drove the higher-than-expected GVA outcome in 2QFY24. We see FY24 real GDP growth to average at 6.5% yoy (vs 7% yoy, RBIe). For 1HFY24, private consumption, public expenditure and capital formation have grown by 4.5%, 5.1% and 9.5% yoy respectively. In FY25, we see private consumption growth soften at margin, capital formation to stay strong but moderate in yoy terms and growth in public expenditure to improve vs FY24.

Exhibit 1: Global growth: Heterogenous and weak

Soft landing is the theme, but situation remains fragile

Real GDP growth yoy	2022E	2023E	2024E
Global	3.6	3.0	2.8
US	1.9	2.4	1.4
Euro Area	3.4	0.5	0.5
China	3.0	5.3	4.8
Japan	1.5	1.2	0.8
India*	7.2	6.5	5.8

Source: BofA Global Research, India are FY numbers

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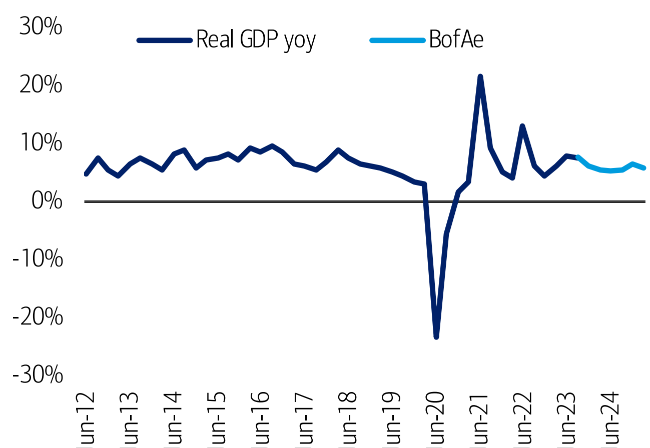
Exhibit 2: Real GDP growth to soften as base effects fade

Expect real GDP growth to soften to 5.8% yoy yin FY25 from 6.5% yoy in FY24



Source: MOSPI

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Exhibit 3: We see real GDP growth slow to 5.8% yoy in FY25 from an estimated 6.5% in FY24 as services growth fizzles out

While agriculture & manufacturing growth are expected to stay robust in FY25, services sector growth is expected to moderate

	Wts.	FY22	Sep'22	Dec'22	Mar'23	FY23	Jun'23	Sep'23	FY24 BofAe	FY25 BofAe
Real GVA		8.8%	5.4%	4.7%	6.5%	7.%	7.8%	7.4%	6.5%	5.9%
Agriculture, forestry & fishing	16%	3.5%	2.5%	4.7%	5.5%	4.%	3.5%	1.2%	2.5%	3.0%
Industry	23%	1.5%	-2.5%	.1%	4.7%	2.4%	4.6%	13.2%	7.0%	6.0%
Mining & Quarrying	*3%*	*7.1%*	*-.1%*	*4.1%*	*4.3%*	*4.6%*	*5.8%*	*1.%*	*6.5%*	*7.0%*
Manufacturing	*18%*	*11.1%*	*-3.8%*	*-1.4%*	*4.5%*	*1.3%*	*4.7%*	*13.9%*	*7.0%*	*6.5%*
Electricity, Gas, Water Supply	*2%*	*9.9%*	*6.%*	*8.2%*	*6.9%*	*9.%*	*2.9%*	*1.1%*	*8.0%*	*7.5%*
Services	61%	9.6%	8.9%	6.4%	7.4%	9.5%	1.%	6.7%	7.5%	6.5%
Construction	*8%*	*14.8%*	*5.7%*	*8.3%*	*1.4%*	*1.%*	*7.9%*	*13.3%*	*5.0%*	*7.0%*
Trade, Hotels, Transport, Communication serv	*19%*	*13.8%*	*15.6%*	*9.6%*	*9.1%*	*14.%*	*9.2%*	*4.3%*	*6.5%*	*6.0%*
Financial, Real Estate and Professional Serv	*22%*	*4.7%*	*7.1%*	*5.7%*	*7.1%*	*7.1%*	*12.2%*	*6.%*	*8.5%*	*5.5%*
Public Administration, Defense & Other Services	*13%*	*9.7%*	*5.6%*	*2.%*	*3.1%*	*7.2%*	*7.9%*	*7.6%*	*8.%*	*8.0%*

Source: MOSPI

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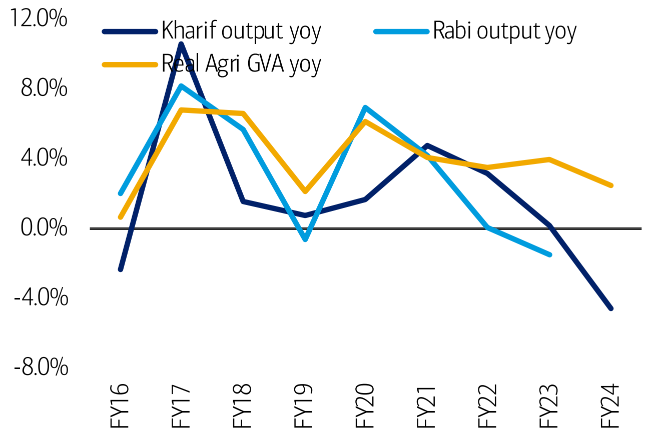
In Exhibits 4-6 we take stock of components of GVA growth. Advance estimates of kharif production suggest lower output this year vs last, rabi sowing so far is not encouraging either. We accordingly see agriculture growth slowing sizably in FY24 but expect it to go back to trend in FY25 (Exhibits 3, 4).

An interesting divergence between Industry GVA growth and IIP growth was the key driver of higher-than-expected GVA growth outcome in Sep'23 quarter. Exhibit 5 shows that this divergence is rare, and we expect it to mean revert soon. Accordingly, we have a lower than consensus FY24 real GDP/GVA growth estimate. As for FY25, we see Industry GVA grow by 6% yoy (slower vs FY24, but still strong).

Exhibit 4: Impact of rabi & kharif harvest on Agriculture GVA growth
Decline in kharif output and underwhelming rabi sowing to exert pressure on agri growth in FY24, expected to improve closer to trend in FY25



Source: Ministry of Agriculture, MOSPI

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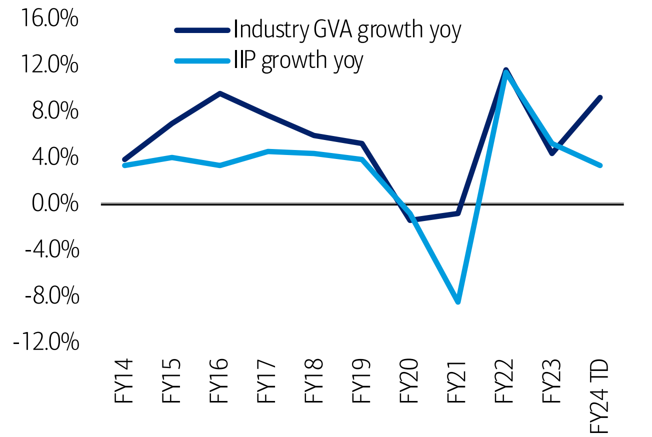
Exhibit 5: Strong correlation b/w IIP growth & Industry GVA growth
Typically, IIP growth & Industry GVA growth move in tandem, FY24 TD this changed adding gains to headline GVA growth, which we opine is a one-off



Source: MOSPI

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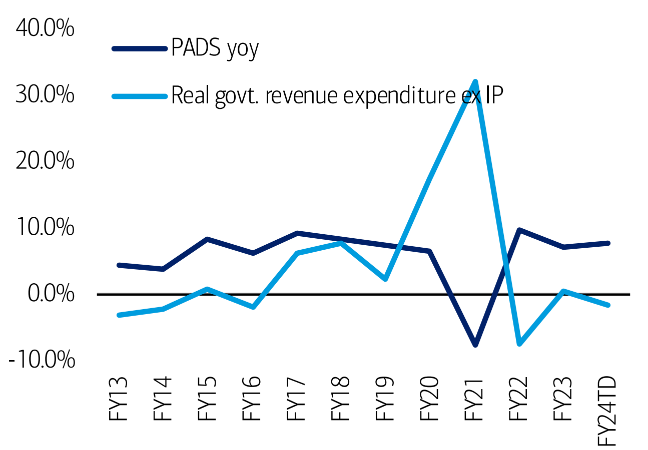
Exhibit 6: The weakening correlation b/w PADS & govt. expenditure
Pre-pandemic, govt revenue expenditure net of interest payments used to be a good proxy for public administration & defense services (PADS) component of GVA. But this correlation seems to have weakened now



Source: MOSPI, CGA

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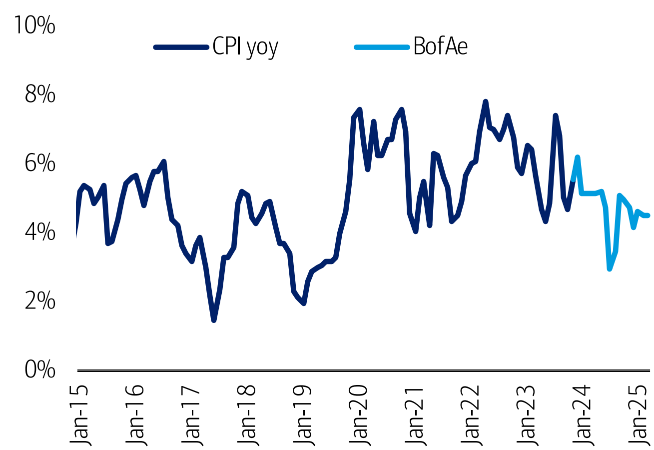
Exhibit 7: CPI inflation yoy: Path ahead (%, monthly)
We except headline inflation to moderate to 4.6% yoy in FY25 from an estimated 5.4% yoy in FY24, still higher than RBI's 4% target



Source: MOSPI

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Until the pandemic, there was directional correlation between public administration & defense services component of services VA and government revenue expenditure net of interest payments (deflated by headline CPI) as explained by MOSPI's methodology. This correlation weekend significantly post Covid (Exhibit 6), making estimation rather confusing. While we do see public expenditure growth to stay strong in FY25, it may not necessarily translate into higher PADS growth, rendering weakness to services sector.

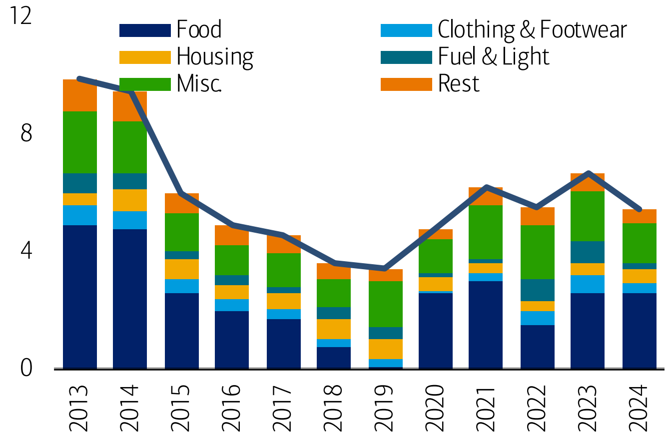
CPI inflation to soften to 4.6% yoy in FY25

We see CPI inflation softening further to 4.6% yoy in FY25 (Exhibit 7), largely driven by food disinflation and marginal moderation in core. Oil price spike amidst geo-political tensions is a well-known risk, however retail price of petrol and diesel in India are insulated by excise duty. The government still has sizable excise duty on pump of price petrol and diesel (20% and 17.6% respectively), and these can be reduced, should pressures from higher global crude price arise. Apart from oil, in case of food, India is mostly a price maker in the global markets and has shown resolve to keep domestic prices in check and rather export food inflation through protectionist measures such as export ban on rice, sugar etc.

For Apr-Nov FY24 headline CPI inflation has averaged at 5.4% yoy and core (headline minus food & fuel) averaged at 4.8% yoy. This is lower than the 6.7% yoy and 6.1% yoy respectively seen in FY23. Despite two almost consecutive food price shocks emanating from perishables, the outlook for FY24 CPI inflation is relatively benign at 5.4% yoy (same as RBIe). The highlight of inflation outcome in FY24 was the unexpected and steady softening of core CPI which arguably gave the RBI MPC the comfort to look through food price spikes. Exhibit 8 shows the share of non-food items in driving inflation slowed in FY24 TD vs FY23.

In Exhibit 9 we take stock of CPI goods vs services inflation. Up until the pandemic, services were a bigger driver of overall CPI inflation, but that reversed post Covid. Between FY20-FY24 TD, while services CPI inflation has averaged at 4.9% yoy, goods CPI inflation remained high at 6.4% yoy. Some welcome convergence between the two is visible in FY24, with softening of goods CPI. Some market observers opine that services CPI inflation could surprise on the higher side and services sector real GVA growth stays strong. As Exhibit 11 shows, there is hardly any correlation between the two. We look at headline minus food & fuel CPI inflation and core GVA (headline minus agriculture and public, administration & defense services) growth, even as core GVA growth swung between 6.3% yoy in FY19 to 10.8% yoy in FY24 (TD), core CPI inflation has remained range-bound between 4.5-5.5%. The reason behind this weak correlation is the composition of these two variables. While core CPI is dominated by services such as healthcare, education, housing, personal care etc., core GVA has construction, trade, hotels, transport, communication, industry as heavyweights. We expect services sector growth to moderate in FY25 vs FY24, but despite that we do not see core CPI inflation to soften further in a durable manner.

Exhibit 8: % point contribution to headline CPI
Food disinflation in FY25 is expected to drive overall softening, core CPI to remain closer to 4%



Source: MOSPI

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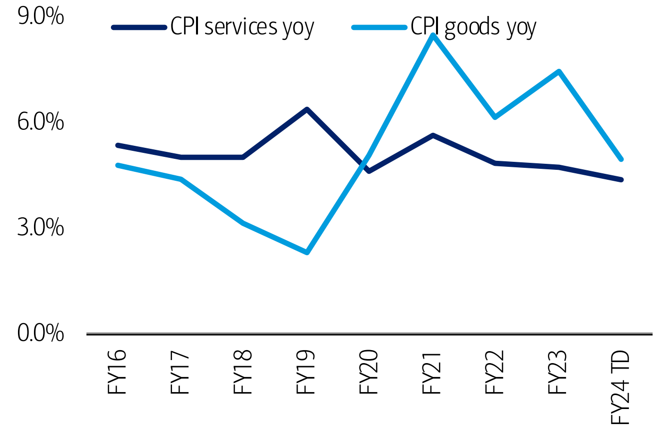
Exhibit 9: CPI inflation yoy: Goods vs Services (in %, annual)
CPI goods inflation has been higher than that for services since the pandemic, but slowly converging at palatable levels



Source: MOSPI

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Moving on to food inflation, barring shocks to perishables, which are fleeting and tend to correct over a relatively short time span, more structural drivers of food inflation are subject to pulls and pressures on both sides. Exhibit 10 shows that Rabi MSP increase is unlikely to be inflationary in nature as current mandi prices are trading higher than revised MSP, making that practically redundant for major crops. Rabi sowing on the other hand is underwhelming. As of Dec 7, 80% of normal area under rabi crop is sown already and that is down 2.7% yoy. While wheat acreage is down 0.9% yoy, pulses acreage down 8.4% yoy posing upside risks to already high pulses inflation. Despite potentially lower rice output and still low wheat sowing, cereal inflation may not rise much taking comfort from buffer stocks of rice and what which may be offloaded in the market, to contain domestic prices, should a supply shock arise.

Exhibit 10: Minimum support price for rabi crops, 223-24
MSP increases for rabi marketing season were quite modest, hardly any impact on CPI as mandi prices already trading higher than MSP in many cases

in Rs/qntl	222-23	223-24	Current mandi/wholesale price	MSP yoy	Mandi price vs MSP
Wheat	2125	2275	2505	7.1%	230
Barley	1735	1850	2136	6.6%	286
Gram	5335	5440	6258	2.0%	818
Masur	6000	6425	7100	7.1%	675
Rapeseed/Mustard	5450	5650	5400	3.7%	-250
Safflower	5650	5800	4145	2.7%	-1655
Jute	4750	5050	5050	6.3%	0
Sugarcane	305	315	310	3.3%	-5

Source: CACP

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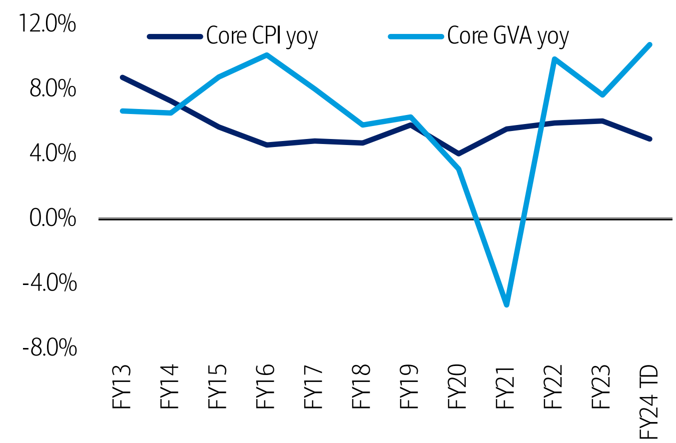
Exhibit 11: Does lower growth aid core CPI disinflation?
Core CPI inflation has softened despite improved growth in core GVA. Difference in composition of the 2 partly explains this divergent behavior



Source: MOSPI , CGVA minus agriculture & PADS

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RBI MPC to cut rates in FY25, albeit slowly

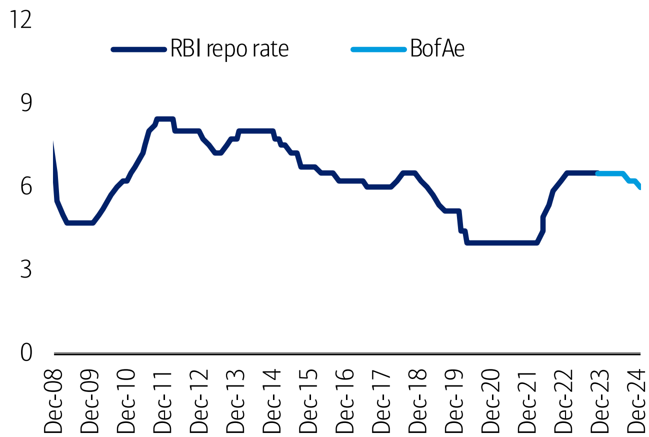
While we were expecting the RBI MPC to deliver one last hike on Dec 8 to seal the deal on 4% inflation target and turn neutral alongside, the outcome differed. RBI MPC unanimously chose to stay on hold, keeping repo rate unchanged at 6.5%. Stance was retained as withdrawal of accommodation in a 5 to 6 vote. After two reasonably hawkish monetary policies in Aug and Oct, the Dec MPC meeting was seen to be moving away from hawkishness. That said, we do not see RBI MPC cutting rates anytime soon.

RBI MPC sees CPI inflation averaging at 4.6% yoy between Apr-Dec 2024 (higher than the 4% target) and despite that persisted with a pause, possibly indicating that further tightening is not needed to bring down CPI inflation closer to target. The stance as withdrawal of accommodation signifies that inflation at 5.4% (Apr-Oct 2023) is still higher than the 4% target, so monetary policy is still accommodative and would turn neutral once the target is secured. In the post policy conference call, the RBI cautioned about the risk of over-tightening but was quick to clarify that they will follow a balanced approach and not get carried away by last few months of data (where CPI fell from 7.4% to 4.9%) and thus loosening of monetary policy is not round the corner as there is still room to achieve the 4% CPI target.

We had highlighted that financial conditions in India despite 250bp of tightening are still below mean and four consecutive pauses have led to further softening of the financial conditions index (FCI). RBI is concerned about incomplete policy rate transmission and tightening financial conditions could potentially accelerate that process. As CPI inflation softens further in FY25, we see the RBI MPC take some comfort and start cutting rates in 2HFY25 (Sep'24 to Mar'25). We do not see the RBI MPC tracking the Fed one to one in this easing cycle and expect 50bp policy repo rate cut in FY25 (Exhibit 12). In Exhibit 13, we plot change RBI repo rate vs Fed funds rate, annually- as can be seen, RBI has seldom traced the Fed in magnitude of rate cuts and is mostly guided by domestic growth-inflation conditions while deciding monetary policy.

Exhibit 12: RBI policy repo rate: Path ahead

RBI MPC delivered a dovish hold today; we no longer see any hike in this cycle. See cuts beginning 2HFY25



Source - RBI

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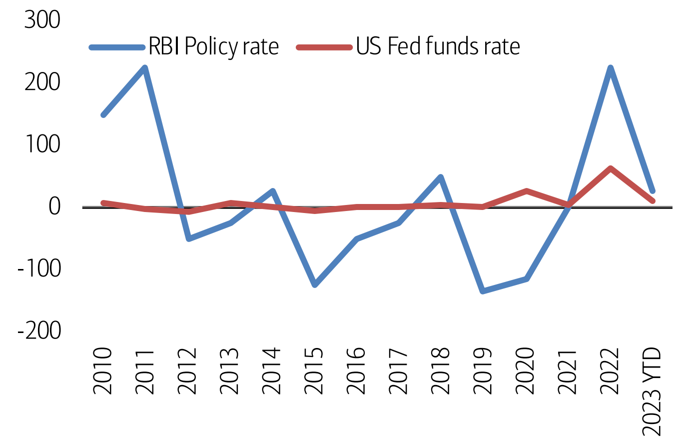
Exhibit 13: Change in RBI repo rate & US Fed funds rate (in bp, annual)

RBI has seldom traced the Fed moves in magnitude, we see that continue in 2024



Source: RBI, Bloomberg

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Fiscal consolidation to continue, despite poll pressures

Concerns surrounding fiscal slippage in an election year are understandable. However, we expect the Centre to meet their fiscal deficit target of 5.9% of GDP in FY24, despite slippage concerns brewing. For FY25, we see Centre's fiscal deficit to consolidate further to 5.3% of GDP in FY25, despite poll pressure. We have previously argued that the current government's intent is to consolidate fiscal deficit through capital expenditure driven growth instead of expenditure compression. Digitization led formalization of the economy is a blessing in disguise aiding tax buoyancy on one side and reducing wasteful expenditure on the other (such as subsidy leakages).

Exhibit 14: Despite poll pressure we see the central govt. meeting FY24's target of 5.9% of GDP & consolidate further to 5.3% of GDP in FY25
Higher than budgeted revenue receipts to pave way for additional expenditure that may be required in the run up to general elections

in INR bn	FY23 Actuals	FY24 BE	FY24 (Apr-Oct)	FY24 (Apr-Oct) as % of full year BE
1.Revenue receipts	2383519	2632281	1567722	60%
Tax revenue	2097368	2330631	1301957	56%
Non-tax revenue	286151	301650	265765	88%
2. Non Debt Capital receipts	72187	84000	22990	27%
2.1 Recovery of loans	26152	23000	14990	65%
2.2 Other receipts	46035	61000	8000	13%
3. Total receipts (1+2)	2455706	2716281	1590712	59%
4. Revenue expenditure	3452518	3502724	1847488	53%
of which, interest payments	928424	1079971	545086	51%
of which, subsidy	530959	374707	231694	62%
& residual				
5. Capital expenditure	736319	1000373	546924	55%
of which, loans & advances	115268	163834	77842	48%
6. Total expenditure (4+5)	4188837	4503097	2394412	53%
Fiscal deficit	1733131	1786816	803700	45%
as % of GDP	6.4	5.9		

Source: CGA, FinMin

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Between Apr-Oct 2023, the government used up 45% of full year's fiscal deficit target. This compares better than 45.6% seen during same period last year and much lower than 62.9% which is typical of this period. Revenue receipts have shown sharp outperformance vs median run rate, paving way for higher than usual capital outlay, without disturbing the fiscal math. Accordingly, even as total expenditure run rate between Apr-Oct FY24 is a shade higher than median, overall fiscal deficit looks comfortably placed.

Current account deficit to modestly widen to 1.6% of GDP

Current account deficit is expected to widen modestly to 1.6% of GDP in FY25 from an estimated 1.2% of GDP in FY24 (Exhibit 15). Merchandise trade deficit is expected to stay elevated on account of oil imports. As western world sees a soft landing, services net exports may find it difficult to rise further and that may limit its offsetting role in overall current account dynamics.

Below are our key assumptions:

Net oil imports: Net oil import bill is set to rise further in FY25 basis both volume growth (4% yoy) and price increase (7%). Our commodity strategist sees Brent crude averaging at US$90/bbl in 2024, up 8% from CY23. Volume growth in FY24 so far is at a healthy 4.5% yoy. We see it soften a shade in FY25 amidst overall slower growth.

Gold imports: Gold prices are expected to rise by 3% yoy to US$1975/oz in 2024. Even though volume wise gold imports are set to fall in 2023, we expect it to go back to 2022 levels of 775 MT and accordingly see a modest increase in gold import bill in FY25.

Non-oil, non-gold imports: Slow domestic growth is expected to keep a lid on NONG import growth too. We see NONG imports rise by 2% yoy in FY25.

Non-oil exports: Despite slower global growth estimates (which we see impacting services net exports more), we expect non-oil exports to grow by 4% yoy in FY25.

Services net exports: Slower growth especially in the developed world is expected to take a toll on services net exports, we thus see a US$10bn fall in services net exports in FY25 vs FY24.

On capital account, the key thing to watch is FII debt inflows. Post India's inclusion in the JP Morgan Emerging Market bond index (to start from Jun'24) we see US$20-25bn of FII debt inflows in FY25 on account of this. Overall, we see a capital account surplus of US$105bn, yielding a BoP surplus of US$40bn in FY25. This should pave way for reluctant appreciation of INR. Our FX strategists see INR at 82/USD by Dec'24.

Exhibit 15: Expect CAD to modestly widen to US$65bn in FY25 (1.6% of GDP) from an estimated US$4bn (1.2% of GDP) in FY23

Despite higher oil & gold imports, see well managed current account deficit in FY25, focus on FPI debt inflows as bond index inclusion materializes

	FY2	FY21	FY22	FY23	FY24BofAe	FY25 BofAe
Current Account Balance (CAB)	**-24656**	**23912**	**-38766**	**-66,984**	**-45000**	**-65000**
% of GDP	**-0.9**	**0.9**	**-1.2**	**-2**	**-1.2**	**-1.6**
Trade balance	-157506	-102152	-189459	-265,291	-250000	-260000
Exports	313296	291619	422004	450963	400000	445000
Imports	474702	392013	613052	714041	650000	705000
Net oil imports	101123	101262	94339	112004	105000	110000
Gold & silver Imports	30956	35394	49442	40307	55000	59000
Invisibles balance	132850	126065	150694	198,236	205000	195000
Services	84922	88565	107516	143,283	155000	145000
Transfers	75208	73460	80447	100,877	95000	100000
Income balance	-27281	-35960	-37269	-45,923	-45000	-50000
Capital Account	**83180**	**63721**	**85807**	**58,943**	**80000**	**105000**
Foreign Investment	44417	80092	21809	22,834	45000	60000
Net FDI	43013	43955	38587	27,986	15000	20000
Net FPI	1403	36137	-16777	-5,152	30000	40000
Loans	25686	6903	33605	8,269	10000	35000
External assistance	3751	11167	5366	5,521	5000	10000
ECBs	22960	-134	8135	-3,790	9000	10000
Short term credit	-1026	-4130	20105	6,539	1000	15000
Banking capital	-5315	-21067	6669	20,980	20000	10000
Rupee debt service	-69	-64	-71	-68	-75	
Other capital*	18462	-2143	23794	6,928	-4925	
Errors & omission	974	-347	459	-1,024		
Overall balance	**59498**	**87286**	**47501**	**-9,135**	**30000**	**40000**

Source: RBI, CEIC, Bloomberg

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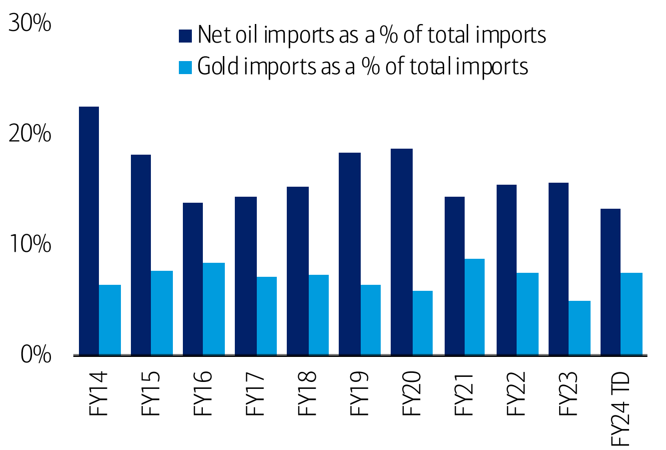
Exhibit 16: Sticky imports: Share of oil & gold in total import bill

Share of net oil imports in total imports has fallen steadily from 23% in FY14 to 13% in FY24 TD. Gold imports on the other hand have been sticky at 8%



Source: Ministry of Commerce, CEIC

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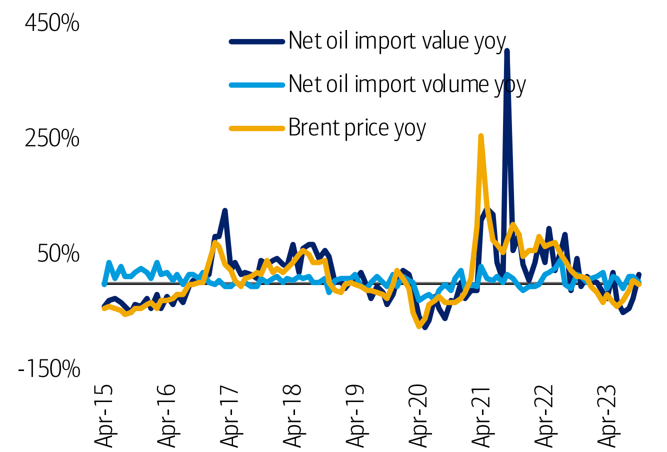
Exhibit 17: Net oil imports: Volume vs Price effect

Net oil imports in FY24 TD have fallen by 20% yoy, owing to a 19% decline in Brent price, even as volume growth stood at 4.2% yoy During Apr-Oct 2023



Source: PPAC, CEIC, Bloomberg

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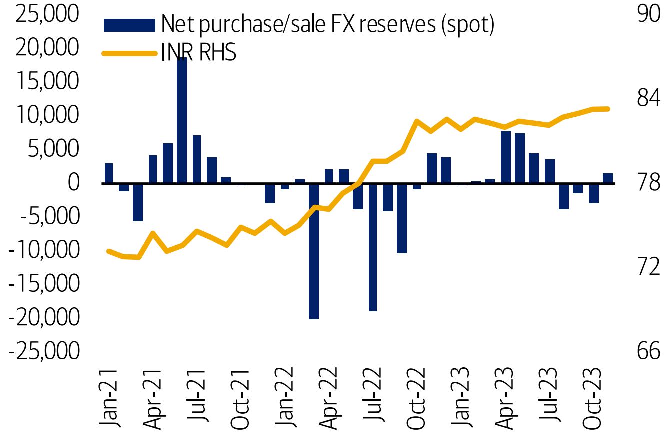
Oil and gold together account for 21% of total import bill. While the share of oil in total imports has fallen steadily from 23% in FY14 to 13% in FY24 TD, gold imports have been relatively sticky at 7% of total imports (Exhibit 16). Together these 2 components are expected to keep import bill elevated in FY25 too. A welcome development is the rise of oil exports (exports of refined products) which now make for 42% of total oil imports vs long period average of 33%. In Exhibit 17, we try to isolate the price vs volume effect in net oil imports. In FY24 TD, net oil imports have de-grown by 20.2% yoy despite a 4.2% yoy increase in volume growth, during the same period. An 18.9% yoy decline in oil prices has been the driver of falling net oil imports, which has been the prime reason for keeping current account deficit in check.

Exhibit 18: RBI's FX purchase/sale & INR

RBI has bought US$100bn of FX in FY24 TD but run down their forward book from US$20bn in Apr'23 to US$4.5bn by Sep'23



Source: RBI, Bloomberg

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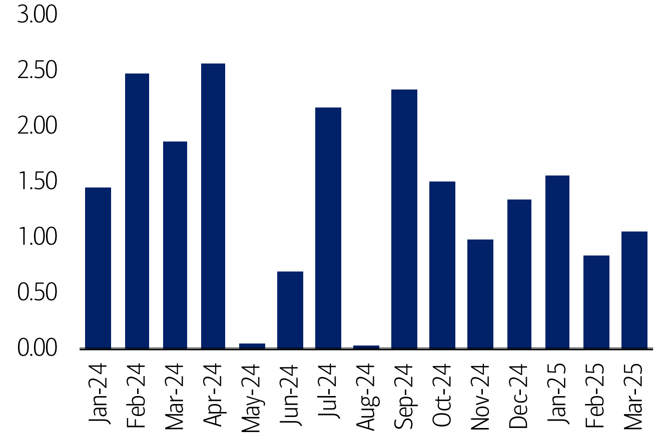
Exhibit 19: Maturity profile of external commercial borrowing (in US$ bn)

We see US$21bn worth of ECB maturities between Jan'24 to Mar'25. Mostly bunched up in 1QCY24



Source: Bloomberg

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A key reason that INR has been one of the least volatile currencies globally in 2023 was the active intervention by the RBI in FX market. Between Apr-Nov 2023, RBI is estimated to have bought US$16.2bn of FX reserves on one hand and rolled down their forward book from US$20bn in Apr'23 to US$4.5bn in Sep'23 on the other. This has allowed INR to stay in a close range between 81.76 to 83.40 during Apr-Nov FY24.

In Exhibit 19, we look at external commercial borrowings maturing between Jan 2024 to Mar 2025. The total number at US$21bn looks manageable. Jan-Mar 24024 will see some bunching up of maturities.

Bracing up for national elections: Looking for continuity

The results for five states which held elections in Nov'23 indicated a thumping victory for Mr. Modi's BJP. PM Modi's Bharatiya Janata party won 3/5 states, namely, Rajasthan, Madhya Pradesh and contrary to exit polls, even Chhattisgarh. Congress won in Telangana, taking the state away from a regional party. The margin of victory for BJP in these 3 states was quite encouraging, especially the performance in Chhattisgarh. Congress on the other hand saw further fall in political footprint. Meanwhile, In Mizoram, regional party Zoram People's Movement (ZPM) won, unseating the Mizo National Front. Better than expected outcome for BJP in these state polls reinforces policy continuity at the Centre in 2024.

While the government has announced a few populist measures- LPG (liquefied petroleum gas) cylinder price cut (costing ~INR185 bn), extension of free food grain program for five years (costing ~INR250bn) and potentially some more could follow in the run up to May, we don't see it impacting fiscal consolidation. Better than expected tax revenues are expected to offer additional resources, allowing fiscal deficit to stay on course to achieve the targeted 5.9% of GDP in FY24.

In Exhibit 20, we look at how macro variables behave in the run up to general elections, in the year of election and one year post that. Contrary to popular belief, inflation doesn't generally fall in a pre-election year, fiscal deficit doesn't always rise (vs election year), RBI has raised rates in the run-up to general elections and INR has moved both ways.

Exhibit 20: Macro variables in pre-election, election and post-election year

No solid conclusions, contrary to popular belief

	CPI yoy	GDP yoy	CAD as a % of GDP	Centre's FD as a % of GDP	INR	RBI policy rate
1998	13.17	4.0%	-1.4%	5.8%	37.30	
1999	4.84	6.2%	-0.9%	6.4%	42.19	
2000	4.02	8.8%	-1.0%	5.3%	43.39	
2003	3.81	3.8%	1.2%	5.8%	48.34	7.00
2004	3.77	7.9%	2.3%	4.4%	45.79	6.00
2005	4.25	7.9%	-0.4%	3.9%	44.95	6.00
2008	8.32	7.7%	-1.3%	2.6%	40.12	7.80
2009	10.83	3.1%	-2.3%	6.1%	46.55	4.90
2010	12.11	7.9%	-2.8%	6.6%	47.26	5.00
2013	10.01	5.5%	-4.8%	4.9%	54.45	7.52
2014	6.73	6.4%	-1.7%	4.5%	60.70	8.00
2015	4.91	7.4%	-1.3%	4.1%	61.26	7.50
2018	3.96	6.8%	-1.8%	3.5%	64.48	6.00
2019	3.72	6.5%	-2.1%	3.4%	69.90	6.30
2020	6.63	3.9%	-0.9%	4.6%	71.04	4.40
2023 TD	5.45	7.7%	-1.1%	5.9%	82.67	6.50

Source: RBI, Bloomberg

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Key risks: National elections, higher for longer global rates

The most important event in 2024 is the national elections scheduled to take place in May'24. Currently, Mr. Modi's BJP looks set to be re-elected for a third consecutive term. However, the strength of majority and vote share are important parameters to ascertain how smoothly can future reforms be undertaken. The other key risk is the higher for longer rates globally that could weigh in on the potential easing cycle by the RBI, which anyway is expected to be slow and shallow.

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