

India: Downgrade of growth forecast

We cut our GDP growth forecast for FY18-19 from 7.2% to 6.7%. Yet elevated inflation supports our forecast for two more central bank policy rate hikes this year



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The message from the latest activity from India was that the economy slowed coming into the beginning of the financial year 2018-19 (runs from April to March). This prompts a downgrade of our GDP forecast for this year. But the balance of economic risks remains tilted toward inflation rather than growth, keeping the Reserve Bank of India (RBI) on track for a second rate hike of the year at the August meeting. There may be one more hike in October.

\$16.6bn

Trade deficit in June

Higher than expected

Widening trade deficit

The trade deficit increased by \$2bn to \$16.6bn in June from May, as export growth slowed by 18% year-on-year and imports rose faster by 21% compared with 20.2% and 15% growth rates, respectively, in the previous month. This resulted in a cumulative deficit in the first three months of FY18-19 (financial year runs from April to March) at \$44.8bn, or \$4.8bn wider on the year. About a 50% YoY surge in imports of oil accounted for almost half of the total trade deficit year-to-date.

A wider trade deficit tells us that net exports possibly contributed negatively to India's GDP growth in the first quarter of the current financial year. We expect the widening to continue ahead as the trade war will hurt exports and the high global oil price buoys imports. These trends will be associated with the continued weakening pressure on the Indian rupee.

Elevated inflation, slower manufacturing

Consumer prices rose by only 5% in June, lower than the consensus of 5.3%. It's still higher than the 4.9% in the previous month, and above the RBI's 4.8% to 4.9% forecast range for the first quarter of the current financial year.

Food prices were a source of downside inflation surprise in June. This is the month when food prices typically rise more than most other months in the year. This June's 1% month-on-month rise was the smallest in more than a decade. But most other CPI components rose during the month, pushing headline inflation higher. Average inflation in 1Q FY18-19 quickened to 4.8%, and this was the fastest in the last seven quarters. Our full-year inflation forecast is 4.7%.

The 3.2% industrial production (IP) growth in May was much weaker than the consensus of 4.4%. A sharp slowdown from 4.9% growth in April was at odds with a sharp acceleration in exports growth. We see 1Q FY18-19 average IP growth at 4.6%, a slowdown from 6.3% in the previous quarter. Such a pace is consistent with about 7% GDP growth.

6.7% ING forecast for FY18-19 GDP growth
Revised down from 7.2%

We downgrade our GDP forecast

We revise our 1Q FY18-19 forecast for GDP growth to 7.0% from 7.5%, a significant dip from the 7.7% growth in the previous quarter. That's not it. We now see growth slipping below 7% in the forthcoming quarters as the global trade war takes its toll. This leads us to cut our full-year growth forecast from 7.2% to 6.7%. At least this is an unchanged pace from the last year, if not worse.