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# GDP growth improves to 7.8% as services sector and private consumption drive growth; positive outlook is retained but risks remain

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- Real GDP grew by 7.8% YoY in Q1 FY24, up from 6.1% in the preceding quarter. The latest GDP data was slightly better than what was suggested by the RBI survey of professional forecasters as well as many independent market surveys.
- It underscores the importance of the country's domestic economy in driving growth, which continues to remain unperturbed by signs of economic slowdown elsewhere in the World.
- Growth in Q1 was led by strong private consumption and investment activity while government consumption and net exports exerted a drag on headline growth.
- As we have highlighted in our previous reports, consumption growth in Q1 was likely driven by a recovery in rural demand while urban demand likely slowed according to high frequency indicators. Investment activity remained strong owing to the government's strong push on CAPEX.
- On the production side of the economy, GVA growth was buoyed by the very strong performance of the services sector. Meanwhile the industrial and the agricultural sectors witnessed a slower growth.
- Within the service sector, the financial, real estate and professional services sub-sector witnessed the highest growth which was likely driven by revival of demand in the real estate sector. The contact intensive trade, transport, hotels, and communications sub-sector also grew handsomely.
- The pickup in growth in Q1 was partly due to a favourable base effect of last year when growth turned out to be much lower than expected. A waning favourable base effect is likely to moderate the pace of growth going forward.
- Looking ahead, activity in sectors like construction, real estate and manufacturing is likely to continue to hold up which will support investment activity. Early indicators of consumption and services sectors suggest some moderation in Q2.
- The top risk to near term outlook stems from lower-than-expected monsoon rainfall and slower progress of Kharif crops sowing. This could affect rural incomes and consequently demand in the upcoming festive season.
- Beyond the immediate near-term, we see a slowing global economy, which could slow capital flows and temper demand for Indian goods and services to be a continuing risk to the country's economic outlook.

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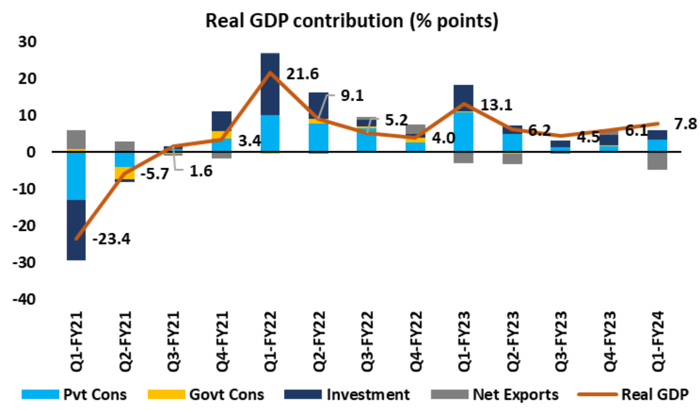
## A resilient domestic economy sustained growth in Q1 amid a morose global economic environment

The latest GDP data was slightly better than what was suggested by the RBI survey of professional forecasters as well as many independent market surveys. It underscores the importance of the country's domestic economy in driving growth, which continues to remain unperturbed by signs of economic slowdown elsewhere in the World.

## Private consumption rebounded; investment remained strong; net exports turned negative




*Source: MOSPI*

Real GDP growth accelerated to 7.8% YoY in Q1 FY24 (vs market consensus of 7.7% and the RBI survey's median expectation of 7.5%), up from 6.1% in the preceding quarter. Growth in Q1 was led by strong private consumption and investment activity while government consumption and net exports exerted a drag on headline growth.

## India's GDP estimates at a constant price

| (Constant Prices) | % YoY | | | | | |
|---|---|---|---|---|---|---|
| | FY 2023 | Q1-FY23 | Q2-FY23 | Q3-FY23 | Q4-FY23 | Q1-FY24 |
| **Private Consumption** | 7.5 | 19.8 | 8.3 | 2.2 | 2.8 | 6.0 |
| **Government Consumption** | 0.1 | 1.8 | -4.1 | -0.6 | 2.3 | -0.7 |
| **Gross Capital Formation** | 9.6 | 20.8 | 6.5 | 5.2 | 7.8 | 7.1 |
| Gross Fixed Capital Formation | 11.4 | 20.4 | 9.6 | 8.0 | 8.9 | 8.0 |
| Exports | 13.6 | 19.6 | 12.2 | 11.1 | 11.9 | -7.7 |
| Less Imports | 17.1 | 33.6 | 23.1 | 10.7 | 4.9 | 10.1 |
| **Real GDP** | 7.2 | 13.1 | 6.2 | 4.5 | 6.1 | 7.8 |
| **Real GDP Excluding Govt Exp** | 8.1 | 14.6 | 7.3 | 5.0 | 6.5 | 8.9 |

*Source: MOSPI*

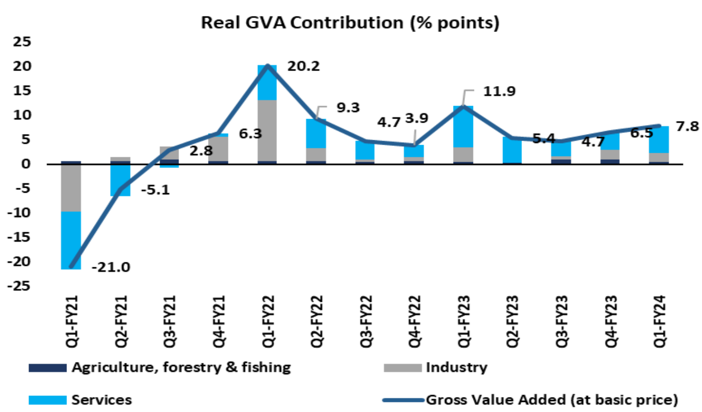
Acceleration of GDP growth in Q1 is mainly attributed to private consumption, which grew by 6% YoY, a sharp jump from the 2.8% growth seen in the previous quarter. It contributed the most to headline growth at ~3.5 pp. As we highlighted in our India Economic Monitor for August, consumption growth in Q1 was likely driven by a recovery in rural demand which was reflected in improvement in two-wheeler sales and consumer non-durables production. Higher Rabi season production likely supported rural incomes and consumption in Q1. Meanwhile indicators of urban demand like passenger vehicle sales and consumer durables production remained in the red in Q1.

Gross capital formation grew by a strong 7.1% in Q1 vs 7.8% in the previous quarter and contributed 2.6 pp to headline growth. To reiterate from our GDP preview in August, central and state governments' push on CAPEX is the main reason behind strong investment growth over the past few quarters. Additionally, a revival of demand in the housing/real estate sector has supported overall investment activity post-pandemic (this is reflected in strong growth in the services sector as well). Despite these positive factors supporting investment, the growth slightly moderated which probably is because of a lacklustre private sector investment. Indeed, according to CMIE, the share of private sector in investment projects completed in Q1 was merely 11% (down from a pre-COVID three-year average of 50%).

Government consumption contracted by 0.7% YoY which is not surprising given that revenue expenditure of the central government also contracted in Q1. For FY24, the government has budgeted a revenue expenditure growth of just 1.2% as it tries to consolidate its fiscal position while also focussing on capital expenditure to revive growth. However, given that general elections are due next year, spending may be increased which is typical of governments to do in the run up to elections. Still, we do not expect the scale of such spending to materially lift growth in FY24.

Meanwhile, net exports turned negative owing to a very strong 10.1% YoY growth in imports as exports fell by 7.7%. Overall, net exports sliced off a considerable 4.6pp from headline growth compared with a positive 1.4pp contribution in the previous quarter. Given the global economic environment, the external sector likely will be a source of volatility in India's GDP growth going forward.

## Services sector lifted GVA growth; industry and agriculture growth slowed slightly




*Source: MOSPI*

On the production side of the economy, GVA in Q1 FY24 grew by 7.8% YoY buoyed by the very strong performance of the services sector which grew at an astounding rate of 10.3% up from 6.9% in Q4 FY23. Meanwhile, the industrial sector growth slowed slightly to 5.5% from 6.3% previously and agricultural sector growth slowed to 3.5% from 5.5% in Q4.

### India's GVA estimates at constant price

| (Constant Prices) | % YoY | | | | | |
|---|---|---|---|---|---|---|
| | FY 2023 | Q1-FY23 | Q2-FY23 | Q3-FY23 | Q4-FY23 | Q1-FY24 |
| **Agriculture, Forestry & Fishing** | **4.0** | **2.4** | **2.5** | **4.7** | **5.5** | **3.5** |
| **Industry** | **4.4** | **9.4** | **-0.5** | **2.3** | **6.3** | **5.5** |
| Mining & Quarrying | 4.6 | 9.5 | -0.1 | 4.1 | 4.3 | 5.8 |
| Manufacturing | 1.3 | 6.1 | -3.8 | -1.4 | 4.5 | 4.7 |
| Electricity and Other Utility Services | 9.0 | 14.9 | 6.0 | 8.2 | 6.9 | 2.9 |
| Construction | 10.0 | 16.0 | 5.7 | 8.3 | 10.4 | 7.9 |
| **Services** | **9.5** | **16.3** | **9.4** | **6.1** | **6.9** | **10.3** |
| Trade, Hotels, Transport, Communication etc | 14.0 | 25.7 | 15.6 | 9.6 | 9.1 | 9.2 |
| Financial, Real Estate & Professional Services | 7.1 | 8.5 | 7.1 | 5.7 | 7.1 | 12.2 |
| Public Administration, Defence and Other Services | 7.2 | 21.3 | 5.6 | 2.0 | 3.1 | 7.9 |
| **Gross Value Added (at Basic Price)** | **7.0** | **11.9** | **5.4** | **4.7** | **6.5** | **7.8** |
| **Core GVA** | **7.6** | **12.5** | **5.9** | **5.3** | **7.3** | **8.7** |

***Source: MOSPI; Note – Core GVA is GVA excluding agriculture, forestry & fishing and public administration, defence, and other services***

The services sector was the largest contributor to GVA growth in Q1 at 5.6pp. Within this sector, financial, real estate and professional services sub-sector showed the most impressive growth at 12.2% YoY, accelerating from 7.1% in Q4. Growth in this sub-sector was likely lifted by robust activity in the real estate sector, which we have highlighted in our previous reports. The contact intensive trade, transport, hotels, and communications sub-sector also performed well with the second highest contribution of any sub-sector, albeit slightly moderating from the previous quarter. Growth in public administration, defence and other services also improved.

Industrial sector contribution to GVA growth fell slightly to 1.7pp from 2.1pp previously. Within industry, activity momentum in the manufacturing sector was maintained as was suggested by high frequency indicators like the IIP and core industry data. Sectors that led manufacturing growth in Q1 include pharmaceuticals, metals, electrical equipment, automobiles, machinery, and transport equipment (according to the breakdown of IIP data). The construction sector remained the second largest contributor to GVA growth within industry although its contribution shrunk as growth moderated from 10.4% YoY in Q4 to 7.9%. Mining growth improved while electricity and other utilities slowed but each of these have very small contributions to overall growth.

Lastly, the agriculture sector experienced some bit of slowdown although growth in this sector remained respectable at 3.5% (vs 5.5% in Q4 FY23). The slowdown can be attributed to the delay in monsoon which affected progress of sowing of the Kharif crops as well as extreme weather events which likely affected non-farming and other agriculture-allied activities.

### We retain a positive outlook; but risks remain

The pickup in growth in Q1 was partly due to the favourable base effect of last year when growth turned out to be much lower than expected. A waning favourable base effect is likely to moderate the pace of growth going forward. Still, India is likely to be the fastest growing major economy in 2023.

We remain confident on prospects of certain sectors like construction and real estate. Furthermore, outlook for the manufacturing sector remains positive as is evidenced by the latest industrial outlook survey according to which demand conditions – both domestic and foreign are expected to remain conducive to growth. Accordingly, we expect the outlook for investment to remain favourable. Public sector push to CAPEX, positive sentiment in the real estate sector, increasing capacity utilisation of manufacturing companies, and robust twin balance sheets of banks and corporates, are likely to keep conditions favourable on that front.

We are less confident about the prospects of the following sectors. Early indicators for the contact intensive trade, transport, hotels, and communications sector suggest some moderation in Q2, however these could receive a boost as the festive season demand kicks in. Narrowing of the banking sector spread is likely to affect profitability in that sector as well. In the insurance sector, premium collection slowed significantly in July.

The top concern surrounding India's growth is linked with sub-par monsoon conditions. This has led to lower-than-normal sowing activity to date. The disappointing progress of monsoon rains is likely to impact late sowing of the Kharif crops and ultimately affect production. If rainfall and sowing fail to pick up in September, it could lead to a disappointing Kharif crops harvest. Additionally, this would lead to a dampening of rural incomes, which have only started recovering recently. Consequently, rural demand could turn out to be disappointing in the upcoming festive season. Furthermore, urban consumption indicators like auto sales, petroleum consumption, and employment suggest some signs of a slowdown in Q2. Higher inflation in July-August is also likely to have some detrimental effect on overall consumer demand. Trade is likely to remain a drag on growth given weak external demand while domestic consumption and investment continue to keep the import bill high.

Beyond the immediate near-term risk to agriculture and the rural economy, we continue to see a slowing global economy, which could lead to a moderation of capital flows into the country and temper demand for Indian goods and services, to be the central risk to the country's economic outlook.

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