GDP growth jumps to 6.1% in Q4 FY23; net exports and manufacturing surprised on the upside

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- Real GDP grew by 6.1% YoY in Q4 FY23, up from the revised estimate of 4.5% in the preceding quarter and reinforces the view that the economy continues to perform well both in absolute terms and relative to other economies around the world.
- From the policy standpoint, with the pace of economic growth staying solid plus recent signs of a moderation in price pressures, we retain our expectation of an extended pause in RBI monetary policy.
- Activity in Q4 was led by investment (owing to CAPEX push by the government), ongoing recovery in consumption demand and a turnaround of the net exports.
- On the supply side, gross value added grew by 6.5% YoY in Q4 FY23, accelerating from the 4.6% growth recorded in Q3 and way above the second advanced estimate, which implied growth of 5.1%.
- While growth in real GVA continued to be driven by the services sector, the positive surprise was the improvement in the industrial sector's performance driven by the manufacturing sector and construction. Meanwhile, the agriculture sector continued to punch above its weight on headline growth.
- For the full year FY23, although real GDP growth moderated to 7.2% from 9.1% in FY22, it is much more impressive given that it comes on top of a normal base, as opposed to last year when there was a very favourable base effect at play.
- Incoming high frequency indicators suggest a positive outlook for the Indian economy, however a possibility of adverse weather conditions, absence of sustained labour market improvement and external weakness could weigh on activity going forward.

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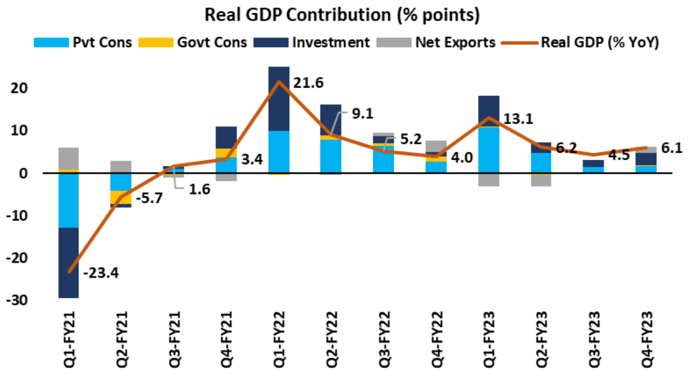
Real GDP growth supported by investment, continued recovery in private consumption; turnaround in net exports came as a surprise

The recent GDP report underscores the ongoing resilience in economic conditions. Real GDP grew by 6.1% YoY in Q4 FY23, up from the revised estimate of 4.5% in the preceding quarter and reinforces the view that the economy continues to perform well both in absolute terms and relative to other economies around the world. Resilient economic conditions persist despite continued global headwinds. With the pace of economic growth staying solid plus recent signs of a moderation in price pressures, we retain our expectation of an extended pause in RBI monetary policy.

Economic activity in the latest quarter was more broad-based than it has been of late, providing a favourable signal for economic health. Activity in Q4 was led by investment (owing to CAPEX push by the government), ongoing recovery in consumption demand and a turnaround of the net exports. Meanwhile, government consumption spending's contribution to overall real GDP growth rose compared to the previous quarter, as the government stepped up expenditure to meet budget targets. Nominal GDP growth slowed down to 10.4% from 11.4% in Q3 reflecting the impact of receding inflation.

Economic activity in the latest quarter was more broad-based



Source: MOSPI

The investment demand - gross fixed capital formation (GCF)- noted a robust growth of 8.9% YoY (v/s 8.0% in Q3) and contributed ~3.1 percentage points (pp) to the real GDP growth print. Even on a sequential basis, the investment activity noted a solid growth of 20.8% QoQ (vs 3.9% contraction in Q3) buoyed by the uptick in the pace of capital expenditure by the central government and the state government. Indeed, the central government's capital expenditure for FY23 stood 24.4% higher than last year. On the other hand, private investment has remained subdued as reflected in the declining share of the private sector (36%) in the total investment projects completed in FY23 compared to the pre-COVID three-year average of 50%. For the outlook ahead, we remain optimistic about a more broad-based recovery in the investment cycle due to the following reasons. First, with an ambitious CAPEX target for the third year in a row, the government is expected to remain steadfast in its plans to push infrastructure development in FY24. Second, the capex related indicators like steel and cement production are showing a steady recovery. And finally, the capacity utilization of manufacturing firms was above the long-term average in Q3, which bodes positively for the private sector investment.

India's GDP estimates at a constant price

(Constant Prices)	% YoY						Q3 FY23 v/s	Q4 FY23 v/s
	FY 2022	FY 2023	Q1-FY23	Q2-FY23	Q3-FY23	Q4-FY24	Q3 FY20	Q4 FY20
Private Consumption	11.2	7.5	19.8	8.3	2.2	2.8	15.0	14.9
Government Consumption	6.6	0.1	1.8	-4.1	-0.6	2.3	0.2	41.1
Gross Capital Formation	17.9	9.6	20.8	6.5	5.2	7.8	13.0	29.1
Gross Fixed Capital Formation	14.6	11.4	20.4	9.6	8.0	8.9	12.6	30.3
Exports	29.3	13.6	19.6	12.2	11.1	11.9	29.8	42.3
Less Imports	21.8	17.1	33.6	23.1	10.7	4.9	25.7	25.3
Real GDP	9.1	7.2	13.1	6.2	4.5	6.1	11.6	14.0
Real GDP Excluding Govt Exp	9.4	8.1	14.6	7.3	5.0	6.5	12.9	11.3

Source: MOSPI

Private consumption expenditure growth increased from 2.2% YoY in Q3 to 2.8% in Q4 and contributed 1.6 pp to the real GDP growth. The growth is aided by the base effect as sequentially private consumption contracted by 3.2% QoQ potentially due to the waning of the festive-led demand. Growth in this component was likely supported by the steady recovery in urban demand till now. Meanwhile, the nascent signs of recovery were also noted for the proxies of rural demand indicators including two-wheeler registrations, consumer non-durables, and rural wages which augur well for the outlook ahead for rural consumption. But the outlook for the rural demand remains two-sided with the El Nino conditions (uneven monsoon) predicted for FY24. Further, the growth trajectory for both urban and rural demand will depend crucially on the labour market recovery which shows only marginal signs of improvement hitherto (Refer to our monthly for more details).

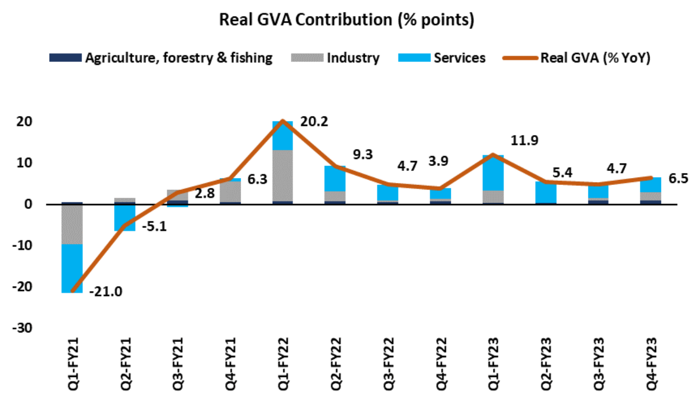
On the external front – the net exports noted a turnaround as they contributed 1.4 pp positively to the real GDP growth after three consecutive quarters of drag. Overall, the trade deficit in the final quarter of FY23 narrowed led by a combination of a decline in the merchandise trade deficit and a continued increase in the services surplus on the back of robust exports. On the merchandise front, the drop in the trade deficit is being led by the decline in imports outpacing the decline in exports potentially due to a softening of the domestic demand and moderation in global commodity prices. Going ahead, external demand, especially for services, is likely to weaken owing to the global growth slowdown which could impact the services sector which has been relatively unaffected until now.

Lastly, the government consumption expenditure noted improvement with a growth of 2.3% YoY in Q4 after two consecutive quarters of contraction and contributed 0.3 pp to the real GDP growth. This was despite the unfavourable base effect of the last year. With the government accelerating its expenditure in the final quarter of FY24, government consumption noted a massive increase of 39.3% QoQ in Q4 compared to 4.8% in the previous quarter, reaching 141% of its pre-pandemic levels. In FY24, other demand indicators will have to pick up pace as economic recovery reliance on government consumption spending will have to go down in view of the modest revenue growth budgeted at 1.2%.

Services sector remains strong; industry surprises on the upside; agriculture a bonus

Gross value added grew by 6.5% YoY in Q4 FY23, accelerating from the 4.6% growth recorded in Q3 and way above the second advanced estimate, which implied growth of 5.1%. While growth continued to be driven by the services sector, the positive surprise was the improvement in the industrial sector's performance, especially when compared to the dismal growth in that sector in the prior six months. The agriculture sector remained resilient and continued to punch above its weight on headline growth. Sequential GVA growth in Q4 at 6.9% was much higher than the pre-COVID five-year average for this quarter, which points to good momentum in overall economic activity.

A resurgent industrial sector lifted headline growth



Source: MOSPI

The services sector remains a bright spot with growth in this sector outpacing that in others. Growth in services accelerated to 6.9% YoY in the quarter ending in March from 6.1% in the December quarter. A delayed recovery of the contact intensive services from COVID-19, and shift of consumer demand towards services (during the first two years of COVID-19 goods demand had shot up due to mobility restrictions) and a strong financial and real estate sector continues to drive services growth. As was the case in the previous two quarters, the trade, transportation, hotels, communication, and broadcasting services sub-sector contributed the highest to services growth followed by the financial, real estate and professional services sub-sector. Public administration, defence and other services' performance was slightly better compared to Q3, which is in line with an improvement in the government's revenue expenditure growth (ex. interest payments and subsidies) in Q4.

The positive surprise in yesterday's data release was the industrial sector performance. Not only did the industrial sector production improve, but it also improved to the highest level in the post-COVID period, exceeding Q4 FY20 by almost 27%. The progress was led by the manufacturing sector, which recorded respectable growth after two consecutive quarters of being in the red. In H2 CY22, the manufacturing sector was hurt due to high commodity and industrial raw materials prices, a sharp increase in interest rates (cost of finance) and slowing global economic growth. Meanwhile manufacturing PMI had remained consistently in the expansionary territory for the past one year, suggesting in hindsight that an upside surprise in manufacturing GVA should have been expected. Momentum in the manufacturing sector was very strong given that sequential growth for the sector was much stronger than the pre-COVID trend for the March quarter.

India's GVA estimates at constant price

(Constant Prices)	% YoY						Q3 FY23 v/s	Q4 FY23 v/s
	FY 2022	FY 2023	Q1-FY23	Q2-FY23	Q3-FY23	Q4-FY23	Q3 FY20	Q4 FY20
Agriculture, Forestry & Fishing	**3.5**	**4.0**	**2.4**	**2.5**	**4.7**	**5.5**	**12.3**	**13.5**
Industry	**11.6**	**4.4**	**9.4**	**-0.5**	**2.3**	**6.3**	**13.5**	**26.5**
Mining & Quarrying	7.1	4.6	9.5	-0.1	4.1	4.3	3.8	2.7
Manufacturing	11.1	1.3	6.1	-3.8	-1.4	4.5	12.7	25.6
Electricity and Other Utility Services	9.9	9.0	14.9	6.0	8.2	6.9	15.5	16.9
Construction	14.8	10.0	16.0	5.7	8.3	10.4	17.7	39.1
Services	**8.8**	**9.5**	**16.3**	**9.4**	**6.1**	**6.9**	**12.5**	**13.8**
Trade, Hotels, Transport, Communication etc	13.8	14.0	25.7	15.6	9.6	9.1	8.3	11.0
Financial, Real Estate & Professional Services	4.7	7.1	8.5	7.1	5.7	7.1	20.9	21.3
Public Administration, Defence and Other Services	9.7	7.2	21.3	5.6	2.0	3.1	7.2	7.8
Gross Value Added (at Basic Price)	**8.8**	**7.0**	**11.9**	**5.4**	**4.7**	**6.5**	**12.7**	**17.6**
Core GVA	**9.9**	**7.6**	**12.5**	**5.9**	**5.3**	**7.3**	**14.0**	**20.4**

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

While the turnaround in the manufacturing sector primarily contributed to a higher industrial growth in Q4, it was the construction sector with the highest contribution to growth within industry, showing effects of the government push on CAPEX. Sequential growth in the construction sector was about six times higher than the pre-COVID trend growth for this sector for the quarter ending in March.

Agriculture, forestry, and fishing sector production was expected to remain strong as well given that sowing in the Rabi season was strong, weather conditions were favourable and high frequency indicators like tractor and fertilizer sales growth had increased in Q3-Q4 FY23, however actual growth in Q4 surpassed those optimistic estimates as well.

Given the positive feedback from high frequency indicators we judge the immediate near-term outlook for both industrial and services sectors to be bright. Both manufacturing and services PMIs remained near historically high levels in April. Looking further ahead, in FY24 sectors such as manufacturing and construction are likely to be supported by government schemes and policies like the Production-Linked Incentives, Gati Shakti and National Logistics Policy. As such we remain optimistic about these. However, we are cautious about the outlook for the services sector. As the push from the release of pent-up demand fades, momentum in the services sector is likely to slow in the absence of sustained improvement in the labour market conditions. Furthermore, there are downside risks to services exports due to the bleak economic outlook for advanced economies in CY23.

Annual real GDP forecast revised upwards to 7.2%

The National Statistical Office (NSO) also released the provisional estimates for the real GDP and GVA for FY23. The real GDP grew by 7.2% in FY23 surpassing the market expectations on the back of faster than anticipated improvement in the external sector. On the supply side, the real GVA growth in FY23 came in much higher at 7.0% YoY than the second advanced estimate of 6.6%, mostly on the back of better-than-expected industrial sector performance in Q4. Although the growth moderated on both expenditure and supply front in FY23 from FY22 levels, it is much more impressive given that it comes on top of a normal base, as opposed to last year when there was a very favourable base effect at play.

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