Economic Growth Registered Moderate Recovery in Q3; Need For Policy Support Continues

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- As expected, economic growth showed a moderate recovery in Q3 FY25, with real GDP expanding by 6.2%, up from 5.6% in the previous quarter but remained much lower compared to 9.5% growth in Q3 FY24.
- This was supported by higher government spending, a moderate pickup in private consumption, and better net export performance. Investment remained steady as higher government CAPEX offset the sluggish private investment.
- From the supply side, real Gross Value Added (GVA) grew by 6.2% in Q3 FY25, up from 5.8% in Q2. This growth was supported by strong performance in the agricultural sector, a moderate recovery in manufacturing activity, and a resilient services sector.
- The National Statistics Office (NSO) revised the FY24 real GDP growth estimate to 9.2%, up from the previous estimate of 8.2%. The revision was primarily driven by stronger private consumption and government spending.
- For FY23, real GDP growth was revised up to 7.6% from 7.0%, mainly due to upward revisions in private consumption and investment, though partially offset by a downward revision in government consumption.
- As per the second advance estimate for FY25, the NSO projects real GDP growth at 6.5%, up from the earlier estimate of 6.4%. However, the required growth rate of around 7.7% in Q4 FY25 to achieve the full year estimate seems overly optimistic due to expected lower government spending in the final quarter.
- We expect FY25 real GDP growth to be closer to 6.1% YoY, factoring in reduced fiscal support in Q4.
- We expect a moderate recovery in economic growth in FY26, with real GDP projected to increase to 6.4%, supported by policy measures such as the monetary policy easing and income tax reduction.
- The RBI is expected to cut the repo rate by 25-bps in April, following the rate cut in February. Combined with income tax reductions, these measures are anticipated to support economic recovery and aggregate demand in FY26. However, global trade tensions continue to pose downside risks.

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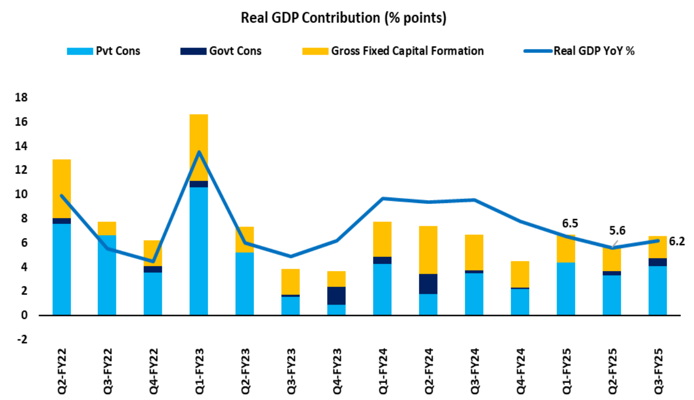
Economic growth recovers in Q3 FY25 from low of Q2

Economic growth showed a moderate recovery in Q3 FY25, aided by higher government spending, moderate pickup in private consumption, and better performance of net exports, while investment remained steady thanks to government CAPEX. From supply side, strong performance in the agricultural sector, a moderate recovery in manufacturing activity, and a resilient services sector supported the real GVA recovery. We project real GDP in FY25 at ~6.1% compared to 6.5% estimated by the NSO, as support from government spending in particular is expected to be lesser in Q4 than in Q3. In FY26, we project a moderate pickup in economic growth to 6.4%, factoring in policy support. However, the uncertain global economic landscape—particularly potential US trade actions—remains a significant headwind to the outlook.

Private consumption, government spending, and net exports help drive real GDP recovery in Q3

In Q3 FY25, real GDP grew by 6.2% YoY, exactly in line with our projection. This compares to a revised 5.6% (previously 5.4%) in Q2 and 6.5% (previously 6.7%) in Q1. As anticipated, economic growth was primarily driven by a recovery in government spending and private consumption, with rural demand likely playing a key role. Net exports also positively contributed to overall economic growth, led by services exports growth.

Contribution to real GDP growth



Source: MOSPI, CMIE

In real terms, private consumption growth showed moderate recovery, rising to 6.9% YoY in Q3 FY25, up from 5.9% (revised from 6%) in Q2 but still lower compared to 7.7% (revised from 7.4%) in Q1. This recovery contributed positively to real GDP, increasing private consumption's contribution from 3.3 percentage points (pp) in Q2 to 4.1 pp in Q3.

The recovery in private consumption during Q3 was supported by festive demand, with rural consumption likely leading the charge. In Q3, rural demand indicators showed acceleration, while urban demand demonstrated a more modest and uneven recovery. This trend is expected to persist, supported by agricultural growth and easing inflationary pressures. We anticipate rural demand to continue driving private consumption recovery, underpinned by a favourable outlook for the farm sector.

Regarding the urban demand outlook, we expect a continued, though moderate and uneven, recovery. Retail loans and urban real salary/wage growth (as reflected in corporate employee costs) have shown signs of slowing. However, easing inflationary pressures may offer some relief. Moving into FY26, the pass-through effects of policy rate cut and the reduction in income tax rates in the budget could provide additional support for urban consumption.

As anticipated, government final consumption expenditure accelerated to 8.3% YoY in Q3 FY25, the highest in five quarters. This aligns with expectations, as the central government's revenue expenditure (excluding interest and subsidies) picked up in the December quarter, following slower spending in H1 FY25 due to elections. The figures for the previous two quarters were also revised. Government consumption spending in Q2 FY25 is now estimated at 3.8%, down from the earlier estimate of 4.4%, and -0.5% in Q1 FY25, revised from an earlier estimate of -0.2%.

We expect relatively less support from government consumption in the final quarter of FY25. The government has revised its FY25 revenue expenditure growth target downward to 5.8%, compared to the initially budgeted estimate of 6.2%. This implies a modest 3.4% growth in the central government's revenue expenditure in Q4 FY25.

India's GDP estimates at a constant price

(GDP Constant Prices)	% YoY							
	FY24	Q1-FY24	Q2-FY24	Q3-FY24	Q1-FY25	Q2-FY25	Q3-FY25	FY25
Private Consumption	**5.6**	**7.4**	**3.0**	**5.7**	**7.7**	**5.9**	**6.9**	**7.6**
Government Consumption	**8.1**	**5.3**	**20.1**	**2.3**	**-0.5**	**3.8**	**8.3**	**3.8**
Gross Capital Formation	**10.5**	**8.9**	**11.9**	**12.4**	**6.4**	**6.1**	**5.0**	**5.8**
Gross Fixed Capital Formation	8.8	8.4	11.7	9.3	6.7	5.8	5.7	6.1
Exports	2.2	-7.0	4.6	3.0	8.1	2.5	10.4	7.1
Less Imports	13.8	18.0	14.3	11.3	-0.7	-2.5	-1.1	-1.1
Real GDP	**9.2**	**9.7**	**9.3**	**9.5**	**6.5**	**5.6**	**6.2**	**6.5**
Real GDP Excluding Govt Exp	**9.3**	**10.2**	**8.4**	**10.2**	**7.3**	**5.8**	**6.0**	**6.8**

Source: MOSPI, CMIE

Government spending has also influenced investment growth. Gross Fixed Capital Formation (GFCF) growth remained steady at 5.7% YoY in Q3 FY25, compared to 5.8% in Q2. Given that private investment growth has likely remained sluggish, as reflected in mixed high-frequency data and a contraction in new project announcements, much of the GFCF growth is likely driven by government CAPEX. According to fiscal data, central government expenditure increased by 47.7% YoY in Q3, up from 10.3% in Q2. State government capital expenditure also rose to approximately 7% (based on data from 17 states) in Q3, compared to a contraction of 4% in Q2. Central government CAPEX is expected to continue supporting economic growth in Q4, with an implied growth rate of 21% for FY25. However, fiscal support for CAPEX is expected to be weaker than previously anticipated in Q4 FY25.

On external trade, the contribution of net exports to real GDP more than doubled to 2.5 pp in Q3 FY25, compared to 1.2 pp in Q2. According to the GDP data release, real export growth surged to 10.4% YoY in Q3, up from 2.5% in the previous quarter. This improvement is likely driven by strong growth in services exports, while growth in goods exports remained muted. Additionally, goods imports had risen sharply in Q3. Looking ahead, services exports are expected to continue supporting economic growth, while goods exports are likely to experience a more moderate recovery. However, risks to external trade remain tilted to the downside, particularly due to the heightened uncertainty around US trade policies.

Lastly, discrepancies shaved off ~2.8 pp from the real GDP growth, reflecting the data quality issues on the expenditure side. The following section from the production side gives a more accurate picture of the underlying growth.

Real GVA growth improved to 6.2% in Q3 FY25

From the supply side, real GVA grew by 6.2% in Q3 FY25, up from the revised estimate of 5.8% (previously 5.6%) in Q2. This growth was driven by a strong performance in the agricultural sector and a moderate recovery in manufacturing activity. The services sector also continued to show resilience. Notably, the improvement is observed despite the upward revision in the base year, with Q3 FY24 real GVA growth revised upward to 8.0%, compared to the earlier estimate of 6.8%. GVA growth for Q1 and Q2 FY25 has been revised to 6.5% (down from 6.8%) and 5.8% (up from 5.6%), respectively.

Activity in the agricultural sector accelerated sharply by 5.6% in Q3 FY25, up from 4.1% in Q2, reflecting a strong Kharif output supported by favourable monsoon conditions. We remain optimistic about the sector's outlook for the remainder of the fiscal year, driven by healthy Rabi sowing.

Industrial sector GVA grew by 4.5%, up from 3.8% in Q2, led by broad-based improvements across most components, except for construction. The recovery in the manufacturing sector was moderate, with real GVA increasing by only 3.5% (up from 2.1% in Q2). According to the RBI's performance data for private sector listed companies, manufacturing profits (operating profits) recovered modestly in Q3, despite rising sales.

On the other hand, construction sector GVA moderated from 8.7% in Q2 to 7.0% in Q3. This suggests continued muted private investments as the government capital expenditure has risen sharply in the quarter. The outlook for the manufacturing sector remains mixed. While companies report better demand conditions ahead (based on the RBI's Industrial Outlook Survey), softer domestic consumption and uncertainty on the external front could weigh on the sector.

India's GVA estimates at a constant price

(GVA Constant Prices)	% YoY							
	FY24	Q1-FY24	Q2-FY24	Q3-FY24	Q1-FY25	Q2-FY25	Q3-FY25	FY25
Agriculture, Forestry & Fishing	2.7	5.7	3.7	1.5	1.7	4.1	5.6	4.6
Industry	10.8	7.3	15.1	11.8	8.4	3.8	4.5	5.6
Mining & Quarrying	3.2	4.1	4.1	4.7	6.8	-0.3	1.4	2.8
Manufacturing	12.3	7.3	17.0	14.0	7.5	2.1	3.5	4.3
Electricity and Other Utility Services	8.6	4.1	11.7	10.1	10.2	3.0	5.1	6.0
Construction	10.4	9.2	14.6	10.0	10.1	8.7	7.0	8.6
Services	9.0	12.5	7.5	8.3	6.8	7.2	7.4	7.3
Trade, Hotels, Transport, Communication etc	7.5	11.0	5.4	8.0	5.4	6.1	6.7	6.4
Financial, Real Estate & Professional Services	10.3	15.0	8.3	8.4	6.6	7.2	7.2	7.2
Public Administration, Defence and Other Service	8.8	9.3	8.9	8.4	9.0	8.8	8.8	8.8
Gross Value Added (at Basic Price)	8.6	9.9	9.2	8.0	6.5	5.8	6.2	6.4
Core GVA	9.8	10.9	10.2	9.7	7.1	5.6	5.9	6.3

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

The services sector continued to show resilience, with Q3 real GVA growth for the sector at 7.4%, up slightly from 7.2% in Q2. Growth in the 'trade, hotels, transport, and communication' segment outpaced the previous quarter, in line with high-frequency indicators such as rising air passenger traffic. Meanwhile, growth in real estate and financial services remained stable at 7.2%. According to the RBI's performance data for private sector listed companies, operating profit growth in the services sector (excluding IT) showed some improvement, aided by a softer rise in input prices. Growth in public administration, defence, and other services also remained steady at 8.8%. We expect the services sector to remain resilient, supported by robust external demand. However, signs of softer urban consumption could weigh on activity going forward.

Revision in FY23 and FY24 numbers

	FY23		FY24		FY25	
	Old	Revised	Old	Revised	Old	Revised
Real GDP	7.0	7.6	8.2	9.2	6.4	6.5
Private Consumption	6.8	7.5	4.0	5.6	7.3	7.6
Government Consumption	9.0	4.3	2.5	8.1	4.1	3.8
Gross Fixed Capital Formation	6.6	8.4	9.0	8.8	6.4	6.1
Exports	13.4	10.3	2.6	2.2	5.9	7.1
Less Imports	10.6	8.9	10.9	13.8	-1.3	-1.1
Real GVA	6.7	7.2	7.2	8.6	6.4	6.4
Agriculture, forestry & fishing	4.7	6.3	1.4	2.7	3.8	4.6
Industry	2.1	2.5	9.5	10.8	6.2	5.6
Mining & quarrying	1.9	3.4	7.1	3.2	2.9	2.8
Manufacturing	-2.2	-1.7	9.9	12.3	5.3	4.3
Electricity and other utility services	9.4	10.8	7.5	8.6	6.8	6.0
Construction	9.4	9.1	9.9	10.4	8.6	8.6
Services	10.0	10.3	7.6	9.0	7.2	7.3
Trade, hotels, transport, communication etc	12.0	12.3	6.4	7.5	5.8	6.4
Financial, real estate & professional services	9.1	10.8	8.4	10.3	7.3	7.2
Public administration, defence and other services	8.9	6.7	7.8	8.8	9.1	8.8

Source: CMIE, Note: Green shows an upward revision in number, orange shows a downward revision, and blue shows no change from previous estimates

Growth numbers for FY23 and FY24 revised upwards

The government has revised the real GDP numbers for FY23 and FY24. The updated figures show higher economic growth, with FY24 now recorded at 9.2%, up from the previous estimate of 8.2%, and FY23 at 7.6%, compared to the earlier estimate of 7%. The upward revisions for FY24 were primarily driven by stronger private consumption and government spending. For FY23, the revisions were largely due to increased private consumption and investment, partially offset by a downward revision in government consumption.

From the supply side also, data for previous years has been revised, with FY24 real GVA now estimated at 8.6%, up from 7.2%, and FY23 growth revised to 7.2% up from the previous estimate of 6.7%, due to broad-based upward revisions across all three major sectors.

FY26 outlook: moderate recovery expected supported by policy actions

According to the second advance estimate, the NSO now projects FY25 real GDP growth at 6.5%, up from 6.4% in the first advance estimate. This implies a required real GDP growth rate of ~7.7% in Q4 FY25, which we consider overly optimistic, given the reduced support from government consumption and CAPEX in Q4 due to the revised expenditure targets. We expect real GDP growth to be closer to 6.1% in FY25. From the supply side, the full-year FY25 GVA growth estimate remains unchanged at 6.4% (as per the first advance estimates released in January).

We expect policy support to continue in order to revive growth impulse. We anticipate the RBI will cut the repo rate by 25 basis points in April, following the rate cut in February. Combined with income tax cuts, these policy measures should help support aggregate demand and ensure that the economic recovery continues into FY26. Accordingly, we project a moderate pickup in economic growth to 6.4%, factoring in policy support. However, the uncertain global economic landscape—particularly potential US trade actions—remains a significant headwind to the outlook.

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