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India's Economic Performance Review for February 2022

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Executive Summary

Amidst the softening third wave of COVID, India's business activity growth accelerated in February 2022, mainly due to the increased demand, a relatively higher output and impressive export sales; however, the monthly retail inflation surpassed the target ceiling of 6% for the second month in a row since June 2021. The prevailing hike in oil prices due to the Russia-Ukraine conflict has overwhelmed the Reserve Bank of India (RBI) for managing inflation under the target ceiling. While the third COVID wave has now receded, India, like other oil-importing countries, faces economic challenges caused by the Russia-Ukraine crisis.

Consumption sentiment was better in February compared to January, with a reducing number of COVID cases and easing of restrictions on mobility and markets. On the supply side, the Markit Purchasing Managers' Indices (PMI) for both Manufacturing and Services were up from their January levels. The Compositive PMI continued to grow at above 50 points, indicating expansion of business transactions during February 2022. Despite a positive business sentiment, the overall unemployment rate went up to 8.3% in February from the previous month's 6.6%, mainly due to a rise in rural unemployment.

Goods and Services Tax (GST) collections were down 5% in dollar terms in February compared with the January revenues, despite an upsurge in business transactions in February. Rail freight volume continued on an upward trajectory until January 2022, but it fell 7% to about 120 million tons in February, reflecting the impact of COVID restrictions.

India's foreign trade continues to expand, and the country seems well-set to achieve its goods export targets of $400 billion by the end of the fiscal year. However, in the near term, the geopolitical situation arising out of the Russia-Ukraine crisis may impact India's current account deficit, putting pressure on its currency.

The monthly downward trend continued in FDI inflows, reaching only $625 million in December 2021 (the latest available data), down from a peak of $5.01 billion in August 2021.

The consumer price index (CPI) was 6.07% in February, rising from the previous month's 6.01% and remaining above the Reserve Bank of India (RBI) target ceiling of 6.00% due to higher food prices and fuel prices. The wholesale price index (WPI) also surged to 13.11% in February from 12.96% recorded in January, indicating lifting input costs for manufacturers due to higher fuel prices.

The changing geopolitical situation arising from the Russia-Ukraine war may impact the implementation of government spending announced in the Union Budget for Fiscal Year 2022-23. The Budget significantly increased plans for public expenditure on infrastructure and provided impetus to private investments and financial inclusion through increased digitization efforts while continuing support to vulnerable sectors, such as hospitality and travel.

On the back of a lower-than-expected growth in the third quarter of the current fiscal year and in view of inflationary pressures arising out of the Russia-Ukraine crisis, the Government of India (GoI) has revised its GDP growth rate forecast downward, to 8.9% from the previous 9.2%. The economic growth outlook for India appears relatively softer in the near term and its revival may depend upon how soon the international fuel prices stabilize.

Economic Activities in India

Indicator	Jun-21	Jul-21	Aug-21	Sep-21	Oct-21	Nov-21	Dec-21	Jan-21	Feb-21
PMI*									
— Compositive	43.0	49.2	54.8	55.3	58.7	58.3	56.4	53.0	53.5
— Manufacturing	48.1	55.3	52.3	53.7	55.9	57.6	55.5	54.0	54.9
— Services	41.2	45.1	56.3	55.2	58.4	58.1	55.5	51.5	51.8
Industrial output (y-o-y % change)	13.6	11.5	12.0	3.3	4.0	1.4	0.7	1.4	n.a.
— Manufacturing	13.0	10.5	9.9	3.0	3.1	0.9	0.2	1.1	n.a.
Passenger Vehicles sold ('000)	235	264.4	232.2	160.1	260.1	245.3	254.5	254.3	262.5
Rail Freight (Million Tons)	114.9	112.7	110.7	105.8	117.3	116.8	126.8	129.1	119.8
Inflation									
— Consumer Price inflation (%)	6.3	5.6	5.3	4.4	4.5	4.9	5.7	6.0	6.1
— Wholesale Price inflation (%)	12.1	11.2	11.4	10.7	12.5	14.2	13.6	13.0	13.1
Unemployment Rate (%)	9.2	7.0	8.3	6.9	7.8	7.0	7.9	6.6	8.3
GST Collection ($ Billion)	12.5	15.6	15.2	15.9	17.5	17.4	17.2	18.6	17.7
Capital Expenditure ($ Billion)	6.5	2.3	5.9	7.7	3.2	2.7	15.9	6.7	n.a.
Exports ($ Billion)	32.5	35.2	33.3	33.8	35.5	29.9	37.3	34.5	34.5
Imports ($ Billion)	41.9	46.4	47.1	56.4	55.4	53.2	59.3	51.9	55.5
FDI Inflows ($ Billion)	-0.7	2.3	5.0	2.9	1.9	1.6	0.6	NA	n.a.
Exchange Rate (INR/USD)	74.4	74.5	74.2	73.6	74.3	75.2	75.4	74.5	75.0

Sources: Society for Indian Auto Manufacturers, IHS Markit, Government of India Ministries, Reserve Bank of India, Controller General of Accounts
*Note: Purchase Manufacturers' Index (PMI) more than 50 indicates expansion and less than 50 denotes contraction

Demand Recovery Trends

A pick-up in private consumption was visible in February 2022. Vehicle sales were up about 3% from the January level despite the continuing chip shortages. The monthly survey by the Retailers Association of India (RAI) revealed 10% higher sales in February for almost all categories of consumer products, from electronics and apparels to food and groceries, consistent with the steady reduction in COVID cases. Sales automation firm Bizom, which transacts with 7.5 million retail stores across the country and tracks orders by Mom-and-Pop stores, also reported a 17% jump in the value of fast-moving consumer goods sales (mainly commodities and packaged food) in February, which may reflect a combination of both greater volume and higher prices due to inflation. The recovery signs in private consumption augur well for demand, but uncertainties due to the high inflation pressures and the unfolding Russia-Ukraine war will likely impact India's growth in the near-term.

Supply Side Dynamics

Input Purchases

The sustained momentum in economic activity since August 2021 has been reaffirmed by a steady Markit PMI Manufacturing Activity Index above 50, reflecting the optimistic mood of the businesses that have made bold input purchases in anticipation of increased demand (Figure 1). The Composite index in February 2022 improved marginally to 53.5 from the 53.0 recorded in January. The Services index showed an edged increase to 51.8 in February from 51.5 in January amidst a reduction in COVID cases. The Manufacturing index was also up, from 54.0 in January to 54.9 in February, indicating slight increase in production activities. According to the Markit index analysis, sustained sales growth supported the growth in manufacturing sector output in February and businesses also lifted production, input buying and stocks of input purchases. Although higher costs due to a rise in prices of chemicals, energy, food, labor, metals, plastics, and retail-related components impacted firms, the increase in input cost inflation was lower than January's level.

Figure 1: Index of Input Purchases

Data Source: IHS Markit

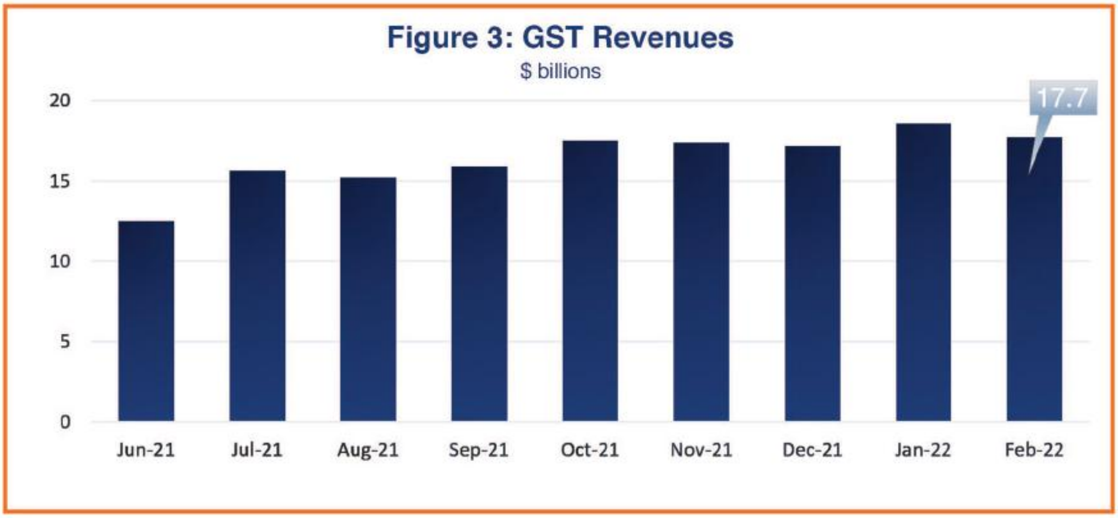
Industrial Production

Growth in industrial production rose to 1.3% in January 2022 from 0.7% (revised upwardly) year-on-year growth recorded in December 2021 (Figure 2), short of market expectations of 1.5% growth. Manufacturing, accounting for 77% of total industrial production, grew 1.1% in January, faring better than the previous month's 0.2%. While performance in the mining sector, which comprises 14% of total industrial output, improved slightly in January 2022, to 2.8% from 2.6% in December 2021, electricity production (8% of total industrial production) slipped to 0.9% from 2.8% for the same period. It is noted that the third wave of COVID had impacted economic activity in January 2022 after several states had imposed restrictions to control the number of cases.

Source: GoI, Ministry of Statistics and Program Implementation

GST Revenues

Changes in value of Goods and Services Tax (GST) collection is considered an indicator of business transactions. The GST revenue collections for February 2022 were slightly down from January, to nearly $17.7 billion (Figure 3), probably due to the weakening of the Indian Rupee by about 2.2% against the US$ over the last month due to the unfolding of Russia-Ukraine war, which reduced the GST collected on imported goods. More broadly, GST collections are now on a stable trajectory and the current fiscal year's targets may well be surpassed; despite the short-term decline GST collections are reflecting an upward trend, in tandem with the restored economic activity, and the tightening of compliances. Downside risks stem from inflation pressures and the Russia-Ukraine conflict, which may have negative impacts on economic activities and GST collections.



Data Source: GoI, Ministry of Finance

Trade

India's monthly goods exports reached a record $37.29 billion in December 2021, following recovery in economic activities and increased global demand post second wave of the pandemic, but exports declined 8.7% on a month-on-month basis to $34.06 billion in January 2022, and moderated to $34.5 billion in February (Figure 4). During FY 2021-22 to date (April 2021-February 2022), exports have grossed more than $374 billion, on track to meet India's target of $400 billion by March 31, 2022.

India's merchandise imports were $55.5 billion in February, up almost 7% from $52 billion the previous month, reflecting partially the relative upward movement in industrial activity along with rising global oil prices caused by geopolitical crisis situations. India's services exports for April-January 2021-22 are estimated at $210 billion, and the Services Export Promotion Council expects it to reach $250 billion by the end of this fiscal year.

Trade analysists have voiced concerns regarding the expected widening of India's current account deficit owing to the skyrocketing global oil prices. The Government of India (GoI) Finance Ministry has said it believes current global oil prices are 'unsustainable' and likely to ease soon, while also asserting that India's record foreign exchange reserves can absorb the increased import costs. That said, India being a major crude oil importer, its current account deficit ratio to the GDP will depend on how long the Russia-Ukraine tension borne hike in international fuel prices persists.

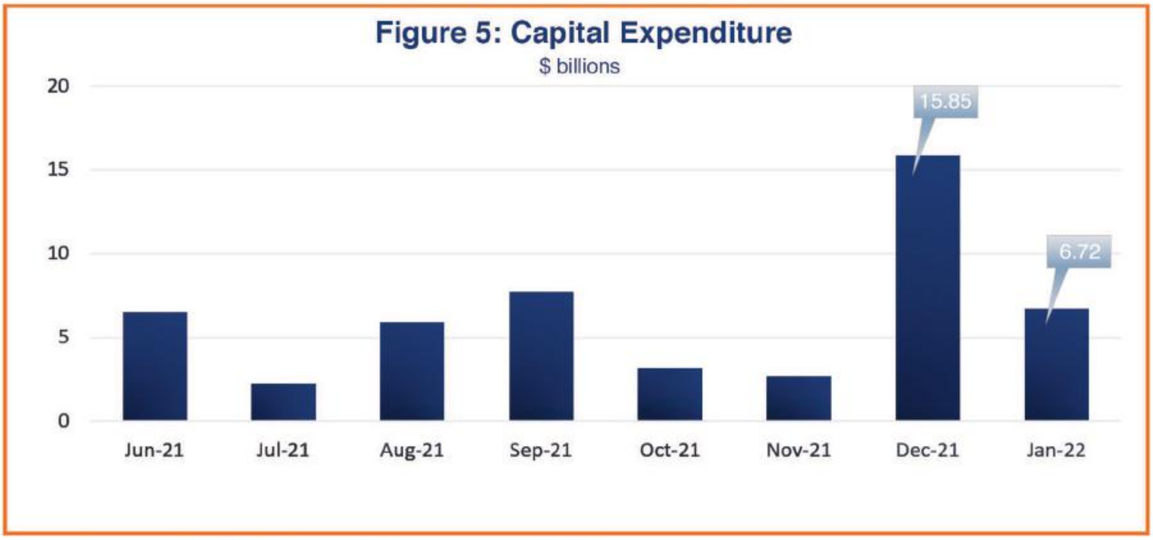
Exporters of tea, coffee and seafood have also flagged disruptions arising out of Russia-Ukraine war. Russia is a major export destination for Indian tea and instant coffee, Ukraine is a growing export market for Indian coffee, and India has emerged as a new source of seafood to the region in recent years. Industry is still assessing the impact of the war on its exports, which were still recovering from the pandemic disruptions. While India's exports to Russia were more than $2.5 billion out of a total bilateral trade of $8 billion in IFY2020-21, its exports to Ukraine are on a smaller scale. India's other export products to Russia include textiles and apparels, plastics, electronics, and pharmaceuticals, all of which may be adversely affected by the war. While Russia-Ukraine disruptions have caused losses in certain exports sectors, they have resulted in

opportunities of diversification in specific sectors, such as wheat, steel, and engineering items. Russia and Ukraine are collectively account for about 10% of the world's steel trade; with supply disruptions and sanctions imposed on Russian exports, Indian steel and engineering goods exporters will likely have new opportunities in the European markets. Likewise, Indian exporters of wheat may benefit from a reduction in exports from Russia and Ukraine, which are major suppliers of wheat in the global market.

Data Source: GoI, Ministry of Commerce & Industry

Government Spending

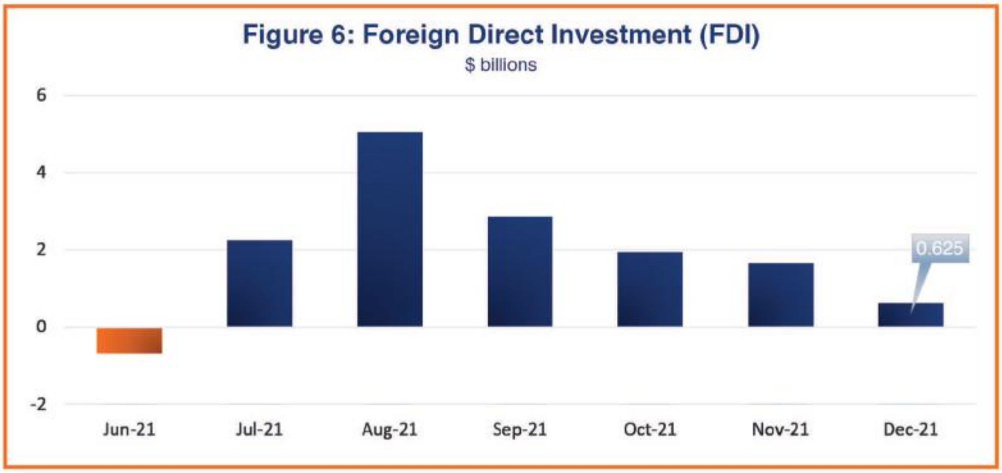
The combination of the government's $26 billion production-linked incentive (PLI) scheme (for automobiles, drones, consumer goods, solar modules, and semiconductors), various export promotion schemes, and reduced corporate tax rates for new entities will likely increase private investment and strengthen India's manufacturing and export sectors. The budget for the IFY2022-23 augments public capital expenditure by more than 34%, to nearly $101 billion, reflecting the government's focus on building public infrastructure. According to the latest Controller General of Accounts (CGA) Monthly Report, the monthly capital expenditure was highest in December 2021 at $15.85 billion, likely due to the equity infusion planned for Air India, but it was down more than half to $6.72 billion in January 2022 (Figure 5). The GoI, in February, has initiated action for selling its 5% stake in the country's biggest public sector insurance giant through an initial public offering (IPO).



Data Source: GoI, Ministry of Commerce & Industry

Foreign Direct Investment (FDI)

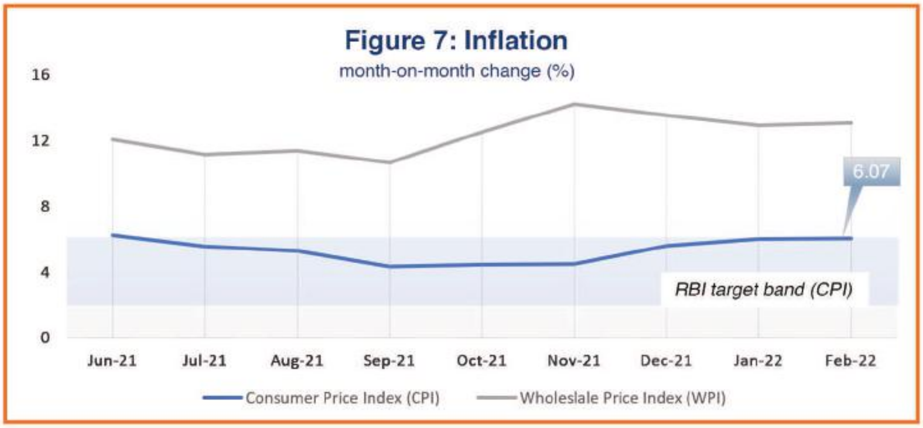
Monthly FDI inflows peaked in August 2021 at $5.04 billion, after which the inflows have been on the downtrend, sliding to merely $625 million in December (Figure 5). The GoI has reported that India has attracted more than $60 billion in FDI so far in the current fiscal year (Apr–Dec 2021). According to the UNCTAD Annual Investment Trend Monitor's latest release, FDI inflows in India were 26% lower in 2021 despite a 77% rebound in global foreign direct investment flows, mainly because large M&A deals in India recorded in 2020 were not repeated in 2021.



Data Source: GoI, RBI

Inflation

After hovering in the 4-5% range between July and December 2021, the consumer price index (CPI) remained above the target ceiling of 6% for the second month in a row. The retail inflation in February 2022, at 6.07% was even higher than the 6.01% recorded in January, mainly due to soaring prices of staples and crude oil (Figure 6). The RBI has maintained an accommodative Monetary Policy so far, but it may soon respond to the recent hike in global oil prices. The central bank anticipated inflation to remain around the upper limit of 6% for February and March on the back of rising crude oil prices and global supply disruptions.



Data Source: : GoI, Ministry of Finance

Digital Payments

The RBI Digital Payments Index (RBI-DPI) measures the extent of digitization of payments in India across four main variables: payment enablers, infrastructure, performance, and consumer engagement. The index has doubled since the start of the pandemic, rising from 153 in March 2019 to 304 in September 2021 (latest available), demonstrating a consistent growth in the adoption and deepening of digital payments across the country (Figure 7).

The RBI has increased the limit for IMPS transactions that should catalyze digital transfers of funds within the banking system, and it has launched a Universal Payment Interface (UPI)-based payments product on feature phone in March 2022, that allows users to make offline digital payments through feature phones.

Figure 8: RBI - Digital Payment Index
March 2018 = 100

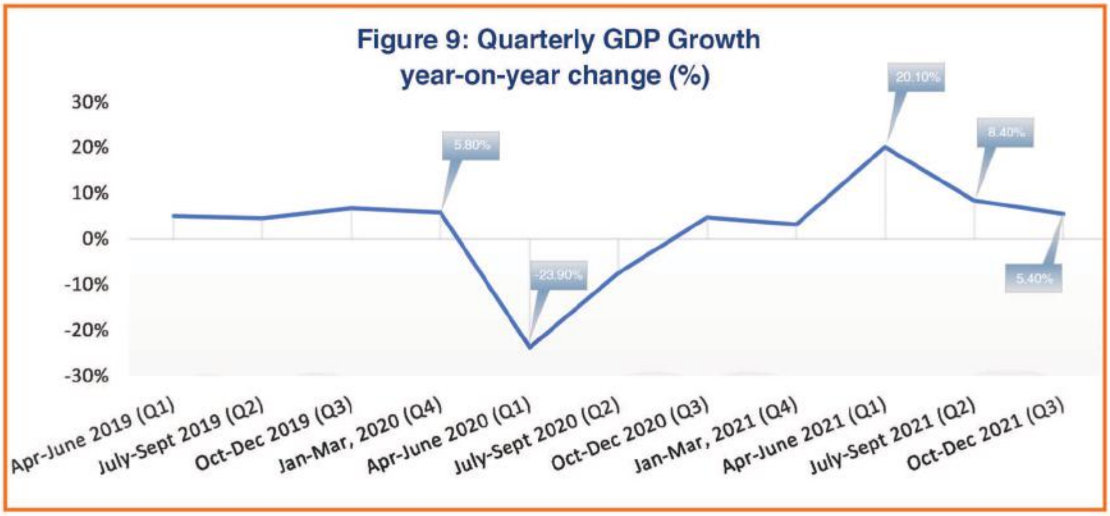
Data Source: Reserve Bank of India

Economic Outlook

The Government of India's fast track measures to vaccinate the public, and the increase in trade activity, and industrial production, led to a remarkable rebound in GDP growth in the first half of FY 2021-22. Year-on-year, real GDP grew by 20.1% in the first quarter of FY 2021-22 (Apr-Jun 2021), despite partial lockdown conditions in several states, followed by an 8.4% year-on-year growth in the second quarter (Jul-Sep 2021), and a slower 5.4% growth in third quarter (October-December 2021; Figure 8) that is below the expectations of most economists. Subsequently, the GoI has scaled down the overall growth forecast for IFY 2021-22 to 8.9% per cent from 9.2% estimated earlier.

India's economy is growing slower than expected, even with a milder third wave of COVID cases, as fears mount up from inflation amid Russia-Ukraine tension. The upsurge in demand with ebbing COVID cases has been coupled with supply shortages in domestic production and imports due to the Russia-Ukraine war, effectively reducing the growth prospects in the near term. The slower pace of growth recorded in the third quarter of the IFY 2021-22 appeared even before the onset of the geopolitical risks from the prevailing higher energy prices. Experts say that the adverse impact of the third wave of the pandemic on services sectors will seep into the fourth quarter also, and the rising commodity prices may further depress the GDP growth in IFY 2021-22. Many economists expect India's GDP growth at less than 8% in FY23, as they suggest a cut in excise duties on oil to cushion the impact on inflation. The GoI has, however, shown optimism on the back of its strong foreign exchange reserves. The Economic Survey in January 2022 had forecast 8-8.5% growth in IFY2022-23 and the International Monetary Fund (IMF) had measured India's GDP growth at 7.1% for IFY2022-23.

The economic growth outlook for India appears relatively softer in the near term and its revival may depend upon how soon the international energy and commodity prices stabilize. India procures more than 80% of its oil supplies from imports. With the current high cost of crude oil at $100+/barrel, India's oil import bill is likely to bloat, resulting in higher current account deficit, consuming higher foreign exchange reserves, and weakening the Indian Rupee (INR).



Data Source: GoI, MoSPI