

GDP: CSO estimates higher FY16 growth

GVA growth for Q3FY16 came in at 7.3% (7.1% in Q2) largely on expected lines however; GDP growth came in higher at 7.6% YoY. The CSO revised the previous quarter numbers significantly upwards with Q1 and Q2 numbers now estimated at 7.6 & 7.7% respectively (vs 7 & 7.4% earlier). Importantly, the CSO's advance estimate pegged FY16 GDP growth at 7.6% and GVA at 7.3%. This implies Q4 GDP growth rate of 7.7%.

Policy implication

The 7.6% estimated growth number is higher than that forecast by the CEA, RBI and multilateral as well as private forecasters and pencils in a higher PFCE growth of 7.6% (6.2% in FY15) and GFCF growth rate of 5.3% (4.9% in FY15). This could narrow the window for future Repo rate cuts to just 25 bps or even close it completely as rate cuts seem counterintuitive in an economy growing at ~8% led by consumption.

FY16: Consumption growth to the fore

Contribution to GDP growth (%)	FY15	FY16E	chg in bps
GDP by exp (Real)	7.2	7.6	33
PFCE	3.5	4.2	73
GFCE	1.3	0.3	(93)
GCF	2.2	2.0	(15)
Net exports	0.2	0.1	(12)
Discrepancies	0.1	0.9	80

Source: CSO, Axis Capital

Key takeaways

- ◆ **Debate over growth rate far from over and unlikely to end in a hurry:** Contrary to expectations even the third quarter data has added to the confusion and the debate over the new numbers (based on a revised, more recent base-year and new methodology), is unlikely to come to an end! Manufacturing growth at 12.6% in Q3 (9% in Q2) is confounding in light of IIP growth (avg 3.9%) and impact of Chennai floods on manufacturing. Moreover, even from a value added perspective it is at odds with our and consensus Q3 earnings estimates which are expected to remain flattish along with tepid topline and EBITDA margins.
- ◆ **Recovery gaining momentum?** With weakness in Agriculture and Services, the interpretation of recovery gaining momentum remains suspect if it is based entirely on the premise of manufacturing clocking near 10% growth for FY16. Readings from high frequency data on manufacturing as well as services remain mixed at best and do not offer an unambiguous picture of rapid recovery. Clearly, the favourable base is also at play. **We believe that the overall GDP growth number will likely be scaled down given that some of the implied growth rates (ie PFCE and agri growth rates for Q4) seem quite high.**
- ◆ **Gap between GVA & GDP:** The divergence between GDP (output) and GVA (value added) remains amplified due to declining input prices. Moreover difference between IIP & GVA base years also magnifies this difference. Higher indirect tax growth & lower growth in subsidies led to GDP growing higher than GVA in nominal terms.
- ◆ **Nom vs real:** Real GVA at 7.3% YoY is forecast to be higher than nominal GVA growth of 6.8% despite WPI deflation having moderated sharply. GVA deflator inflation was expected to have turned positive, given WPI rising to -2.1% in Q3 from -4.5% in Q2 and CPI rising to 5.3% in Q3 from 3.9% in Q2. However, nominal GDP growth pegged at 8.6% is a tad higher than expected by the CEA and will ease the pressure on budgetary numbers.
- ◆ **GDP growth recovery to remain moderate in FY17:** Global headwinds will continue to weigh on exports and manufacturing and hence the onus of growth will remain on domestic demand and public investments. Private consumption is likely to drive growth on the expenditure side. Seventh Pay Commission led stimulus, falling inflation and continuing subsidy to urban consumers from online retailers etc will prop urban consumption. However, rural consumption will remain weak given the lagged effect of 3 consecutive cash-negative crops, lower rural public spends and shrinking subsidies. Investment activity will remain muted due to low capacity utilization and highly leveraged balance sheets. Importantly, from GVA perspective, services such as trade, hotel, transport, communication and financial services and real estate will drive growth in FY17. We maintain our FY17 GDP growth estimate at ~ 7.7% YoY.

Q3FY16 data takeaways

GVA by activity:

- ◆ **Agriculture growth** turned negative with -1% YoY growth (2% in Q2). As per Agriculture department estimates Food grain output is expected to decline 0.5% (vs -5% in previous agri year) and Oilseeds are expected to decline by -4% (vs -16%) Horticultural crops will grow by 0.6%. Livestock, forestry and fisheries will grow at 5.5%. **Importantly, CSO numbers imply that Q4 growth rate is likely to jump to 2.6% which seems a tough ask in light of higher winter temperature and lower Rabi sowing.**
- ◆ **Industry grew at 9% YoY** owing to a huge spurt of 12.6% in manufacturing growth. Mining and construction grew at 6.5% (5% in Q2) and 4% (vs 1.2% in Q2) respectively.
- ◆ **Services sector growth** came in at a flattish 9.4% (vs 9.4% in Q2). Trade, hotels, transport & Communication segment grew at 10% (8% in Q2) whereas Financing, insurance, real estate registered slower growth rate of 9.9% (11.6% in Q2) with tepid bank credit and deposit growth backdrop. Public administration defence and other services grew at ~7.5% (vs 7.1% in Q2). **Services growth is likely to slow to ~9% in Q4 based on CSO numbers.**

GVA by expenditure:

- ◆ **Private consumption grew at 6.4% YoY** (vs 5.6% in Q2) and contributed ~3.5% to overall growth. The CSO numbers imply a near doubling to 11.7% in Q4 which seems unlikely. However, PFCE growth should remain buoyant from hereon with rising real incomes, pay commission awards and lagged effect of interest rates.
- ◆ **Gross Capital formation growth halved at 4.1%** (8.2% in Q2). Business sentiments have taken a knock with Chinese growth and currency woes impeding any incremental improvement in capex.
- ◆ **Govt Final Consumption Expenditure** remained rather flat at 4.7% (4.3% in Q2) due to moderate government spending.

Exhibit 1: GDP growth rate comparison

(YoY%)	Jun-14	Sep-14	Dec-14	Mar-15	Jun-15	Sep-15	Dec-15	Mar-16E
Economic activity								
Agriculture	2.3	2.8	(2.4)	(1.7)	1.6	2.0	(1.0)	2.6
Industry	8.0	5.9	3.8	5.7	6.8	6.4	9.0	7.3
Services	8.6	10.7	12.9	9.3	9.0	9.4	9.4	9.0
Expenditure								
PFCE	8.2	9.2	1.5	6.6	6.4	5.6	6.4	11.7
GFCE	9.0	15.4	33.2	(3.3)	1.0	4.3	4.7	3.0
GFCF	8.3	2.2	3.7	5.4	5.2	7.6	2.8	5.5
Overall GDP	7.4	8.1	6.7	6.2	7.2	7.5	7.1	7.4

Source: CSO, Axis Capital

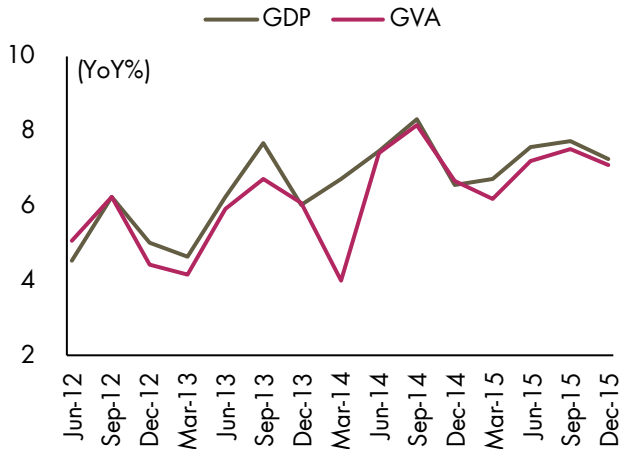
Exhibit 2: GDP Contribution to growth (%)

(%)	Jun-14	Sep-14	Dec-14	Mar-15	Jun-15	Sep-15	Dec-15	Mar-16E
Economic activity								
Agriculture	0.4	0.4	(0.6)	(0.3)	0.2	0.3	(0.2)	0.4
Industry	2.6	1.9	1.2	1.8	2.2	2.0	2.6	2.4
Services	4.5	5.9	6.1	4.7	4.7	5.3	4.6	4.6
Expenditure								
PFCE	4.5	5.1	0.9	3.6	3.6	3.1	3.6	6.5
GFCE	1.0	1.8	2.6	(0.3)	0.1	0.5	0.5	0.2
GFCF	2.7	0.8	1.2	1.8	1.7	2.4	0.9	1.8
Overall GDP	7.4	8.1	6.7	6.2	7.2	7.5	7.1	7.4

Source: CSO, Axis Capital

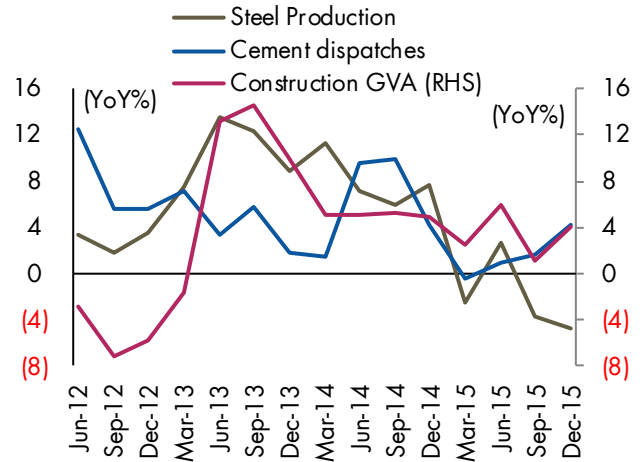
Key indicators

Exhibit 3: Gap between GVA & GDP owed to higher indirect taxes and lower subsidies



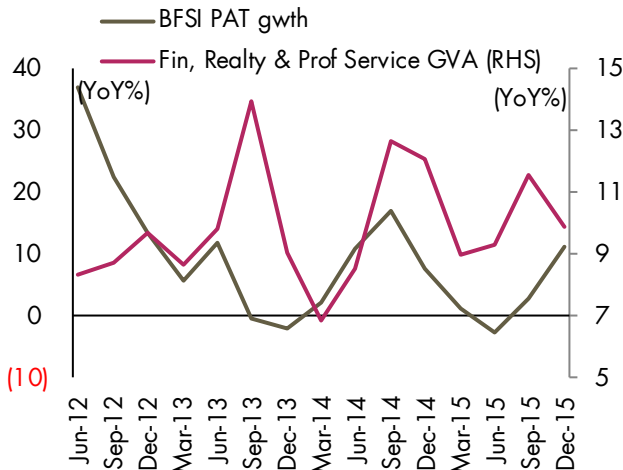
Source: CSO

Exhibit 4: Construction GVA in sync with cement



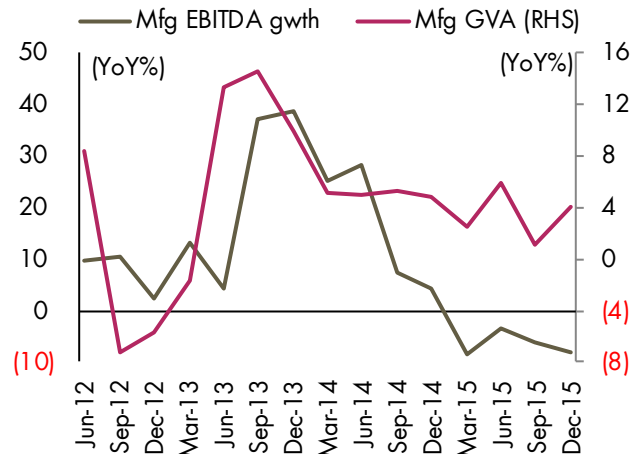
Source: EA Industry; CSO

Exhibit 5: Weak credit & deposit growth weigh on Fin segment



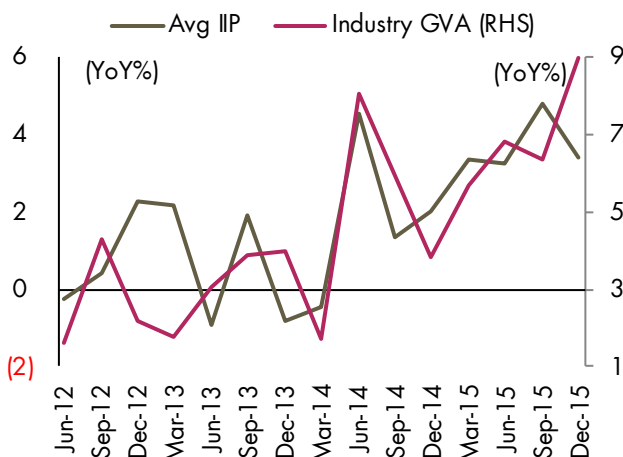
Source: Axis Capital; CSO

Exhibit 6: Huge divergence in Manufacturing



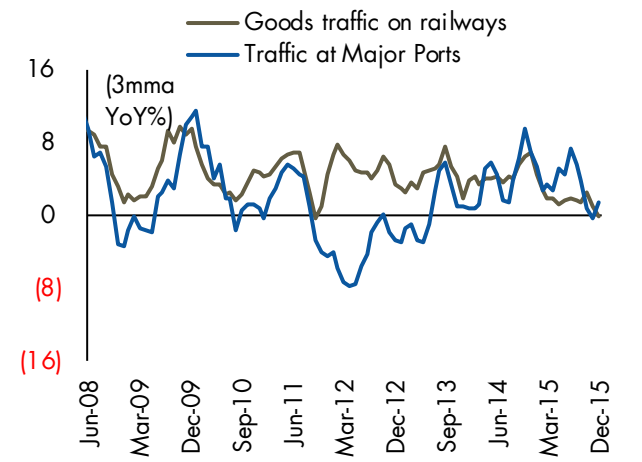
Source: Axis Capital; CSO

Exhibit 7: IIP & Industry growth rates in variance too



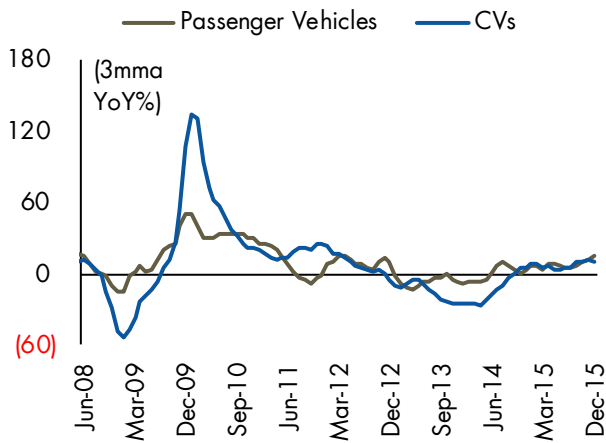
Source: CSO, Axis Capital

Exhibit 8: Port Traffic activity slows



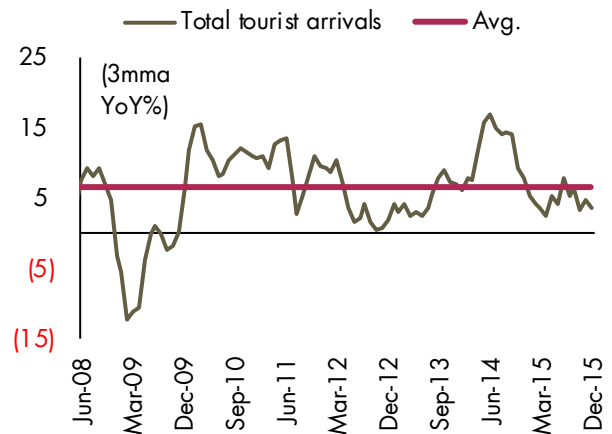
Source: CMIE; Axis Capital

Exhibit 9: CV & car sales uptick visible



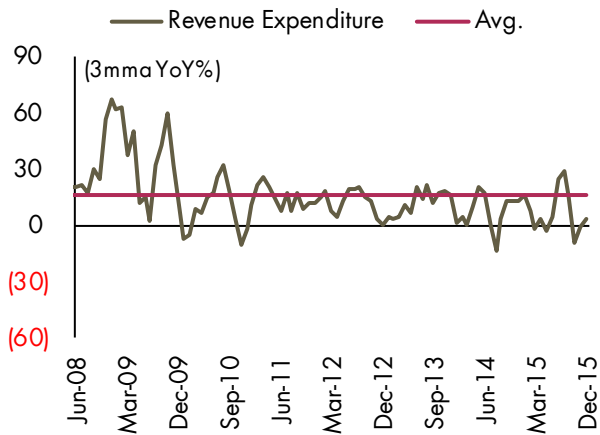
Source: SIAM, Axis Capital

Exhibit 10: Tourist arrivals deceleration



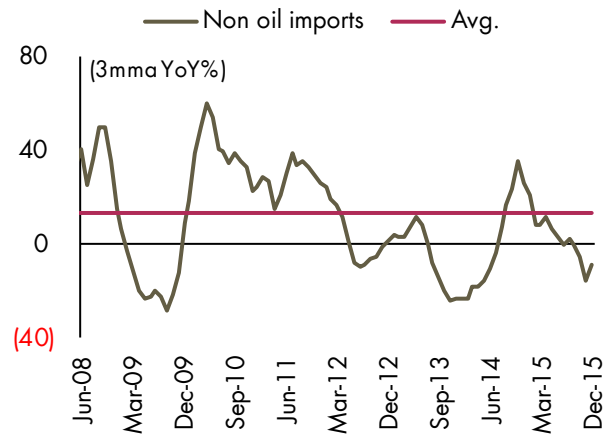
Source: CMIE; Axis Capital

Exhibit 11: Govt expenditure



Source: CMIE; Axis Capital

Exhibit 12: Weak non-oil imports hint at lackluster growth



Source: Bloomberg; Axis Capital

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