EXTERNAL TRADE

Non-oil exports momentum soft

India Equity Research | Economy

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The trade deficit in May was at a four-month high of USD14.6bn, up USD1bn versus April. The key trends are: 1) non-oil exports grew 10% YoY–strongest in five months—entirely led by the base effect; sequential momentum was quite soft; 2) while chemical, auto and agriculture exports held steady, labour-intensive exports (gems/jewellery, fabric, etc) continued show persistent weakness, which is a cause for concern; and 3) imports too picked up to 15% YoY on a low base with electronics, oil and metals turning in strong growth and agri-imports slowing down.

We expect the trade deficit to remain elevated. This along with moderating FDI, tightening global liquidity, mounting trade war concerns, and slowing global growth make INR susceptible to further depreciation. Accordingly, we are revising the average USD/INR forecast to 68 for FY19 and 69 for FY20 from 66 earlier.

Trade deficit rise concerning

The trade deficit for May came in at USD14.6bn, higher than last three months' average of USD13bn. This widening was led by higher non-oil and gold imports as well as weak exports. In fact, despite the recent rise in oil prices, oil balance actually improved as exports growth was stronger (perhaps due to bunching up previous months' exports).

Labour-intensive exports remain weak; electronics imports surge

Overall, exports in April grew 20% YoY with non-oil exports growing only 10% YoY (versus 6% YoY in March). However, the momentum was subdued MoM. On a 3mma basis, non-oil export growth remained subdued at 6% YoY (14% YoY in January). What's particularly concerning is the persistent contraction in labour-intensive sectors—readymade garments, gems & jewellery, etc (which have been either flat or contracting for 11 months) despite a supportive base. This, perhaps, indicates that these sectors are yet to recover from the GST-induced disruption. Meanwhile, exports of a few capital-intensive sectors such as auto and chemicals remained relatively strong.

On the imports front, oil and gold posted higher sequential numbers; non-oil and non-gold imports grew by10% (vs. 0% in April) due to the base effect. Within that, electronics imports were up 20% YoY after slowing down for a couple of months. Furthermore, even metals and coal continue to show robust growth. Imports of agricultural commodities and precious stones were weak and in contraction zone.

Trade deficit to remain elevated and weigh on USDINR

We do not expect major acceleration in the exports momentum due to moderating global trade, although an improvement due to a low base is likely. This along with higher imports (especially oil) would keep the trade deficit elevated. Given FDI flows are now insufficient to fund the CAD and global liquidity is tightening, and INR has outperformed the EM peers so far, a depreciating bias on USDINR is likely. We revise our FY18/19 USDINR average to 68/69 (from 66/66 previously).

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Table 1: India's merchandise trade

					Apr-May	
(USD bn)	**May-18**	**Apr-18**	**Mar-18**	**Feb-18**	**FY19**	**FY18**
Imports	43.5	39.6	42.8	37.8	83.1	75.7
Oil imports	11.9	10.4	11.1	10.2	22.4	15.1
Gold imports	3.5	2.6	2.5	2.9	6.1	8.8
Non oil and gold imports	28.1	26.6	29.2	24.7	54.7	51.9
Exports	28.9	25.9	29.1	25.8	54.8	48.6
Trade balance	(14.6)	(13.7)	(13.7)	(12.0)	(28.3)	(27.1)

Source: Ministry of Commerce, Edelweiss research

Chart 1: India's exports growth remains subdued on trend basis

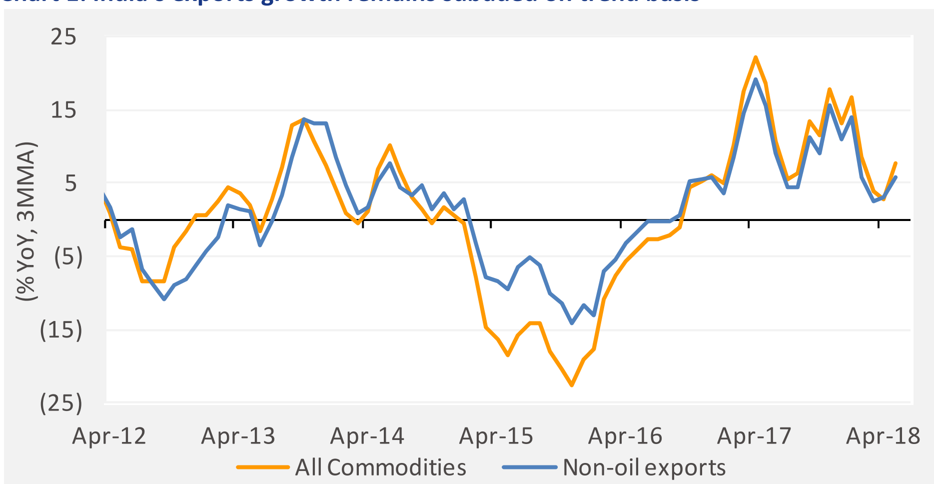
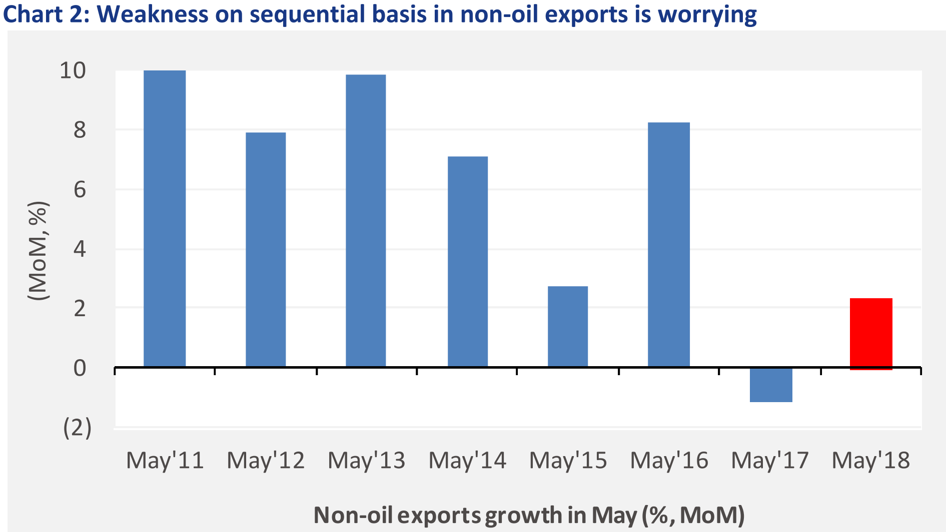


Chart 2: Weakness on sequential basis in non-oil exports is worrying



Source: Ministry of Commerce, Edelweiss research

Chart 3: Persistent weakness in labour-intensive exports is also very concerning

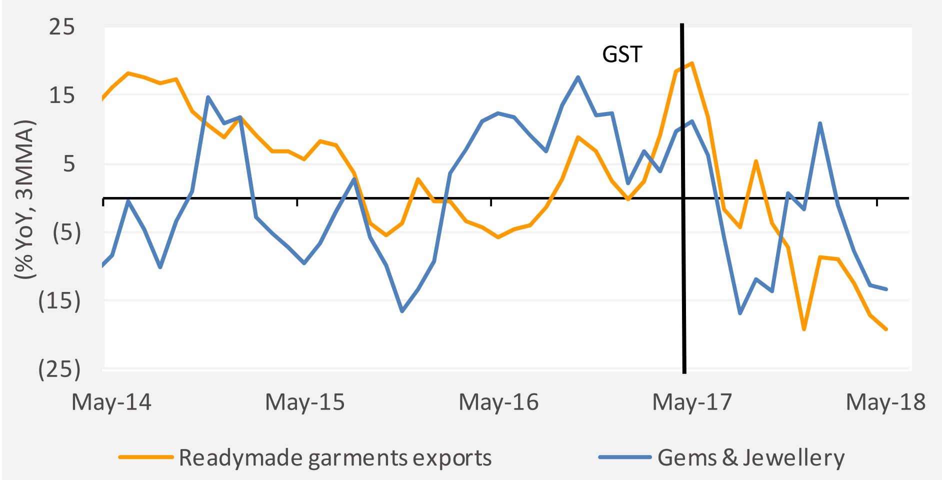


Chart 4: Non-oil & non-gold imports growth slowdown owing to high base

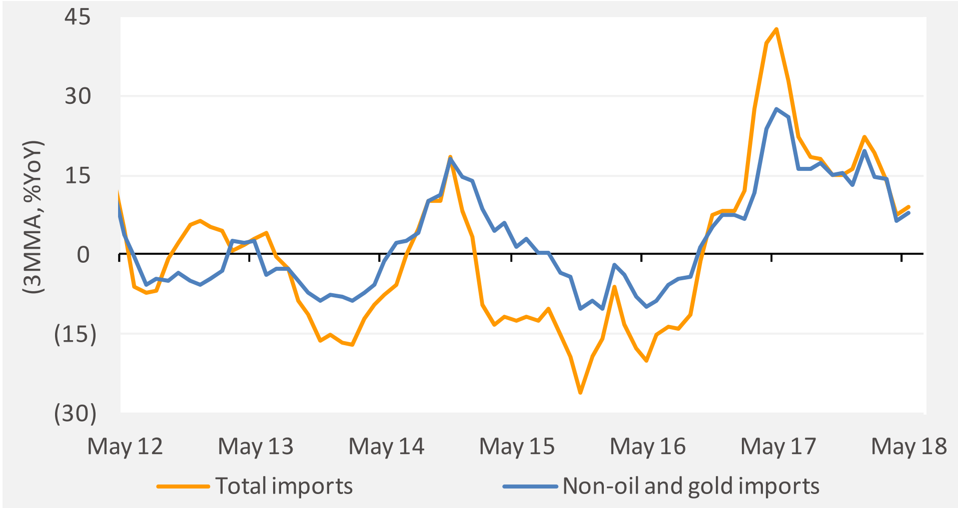
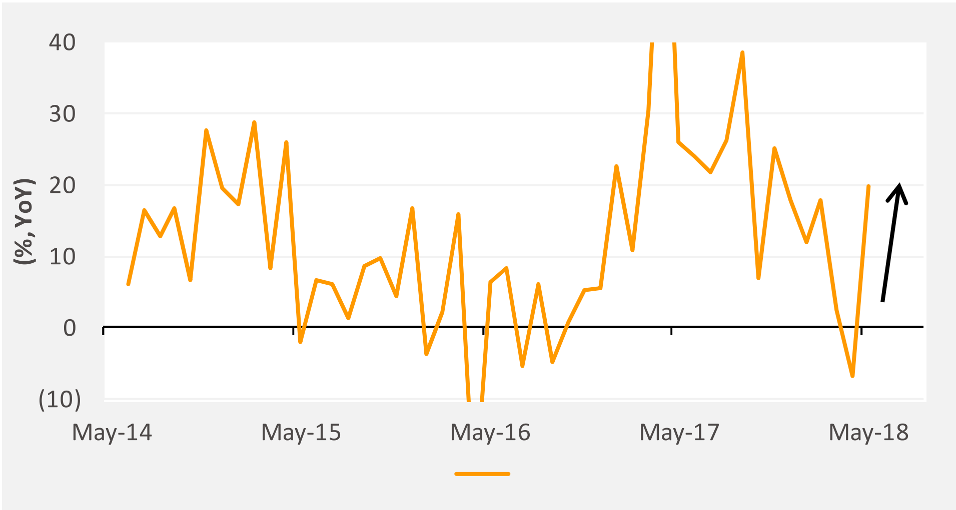


Chart 5: Electronic goods imports remain elevated



Source: Ministry of Commerce, Edelweiss research

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