# 2023: India Macro Outlook

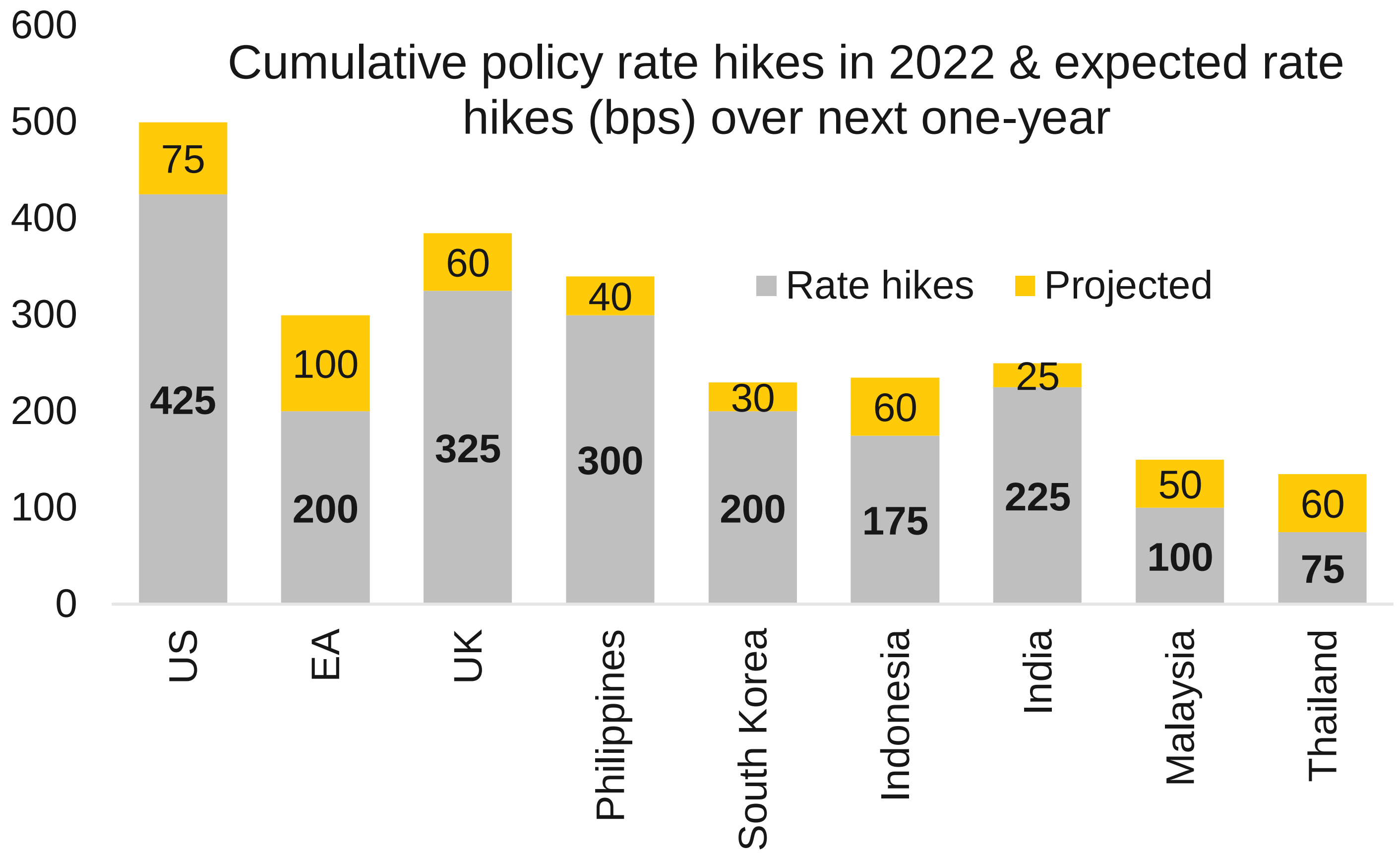
IDFC FIRST Bank

Gaura Sen Gupta
gaura.sengupta@idfcfirstbank.com
+91-22-7132 5562

Reports available on Bloomberg: NH DFC

# Global outlook

# Moving towards the end of rate hiking cycle

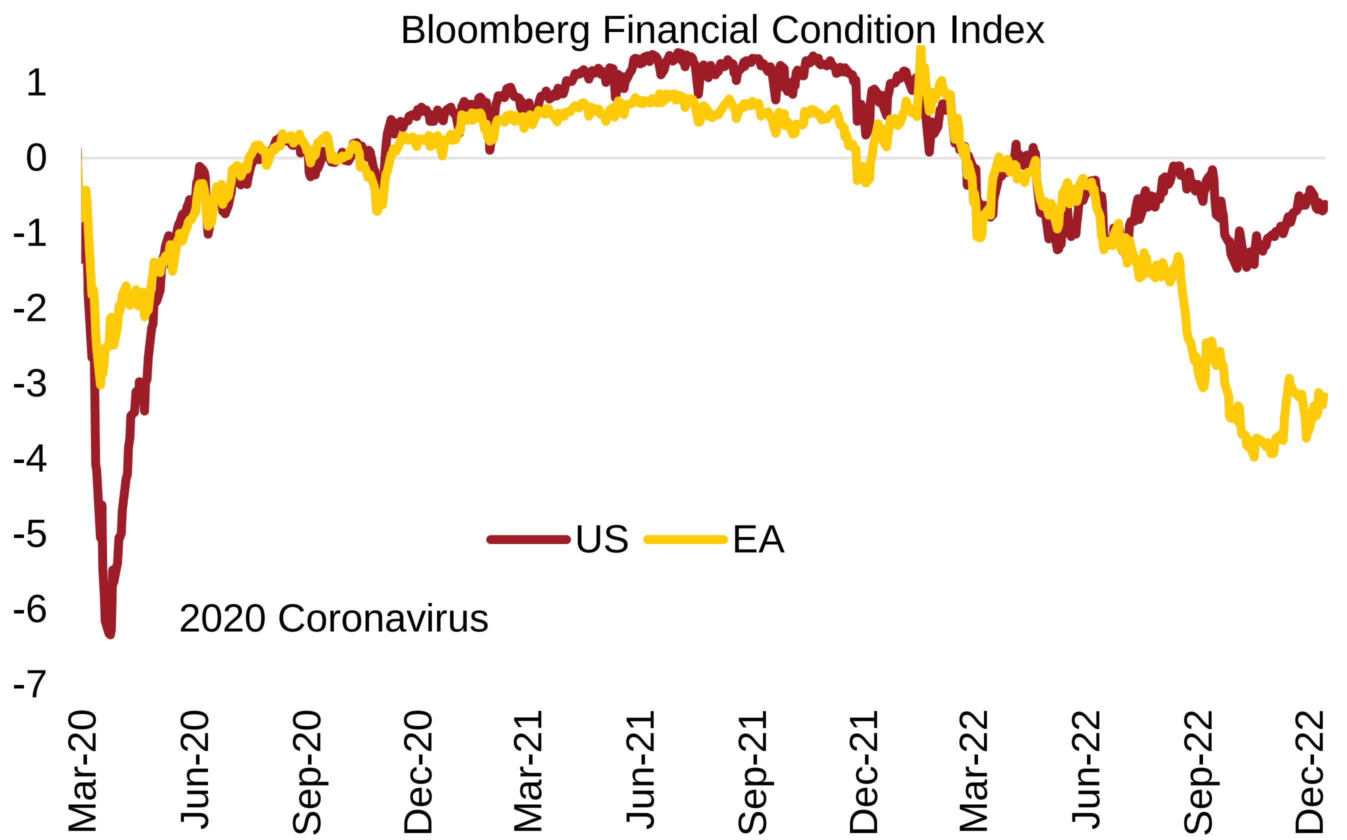



- US Fed: projections from Dot Plot and India RBI : IDFC FIRST Bank Estimate and rest from Bloomberg consensus

IDFC FIRST Bank

*Source: Bloomberg, IDFC FIRST Bank Economics Research.*

# Why the Fed will need to remain hawkish

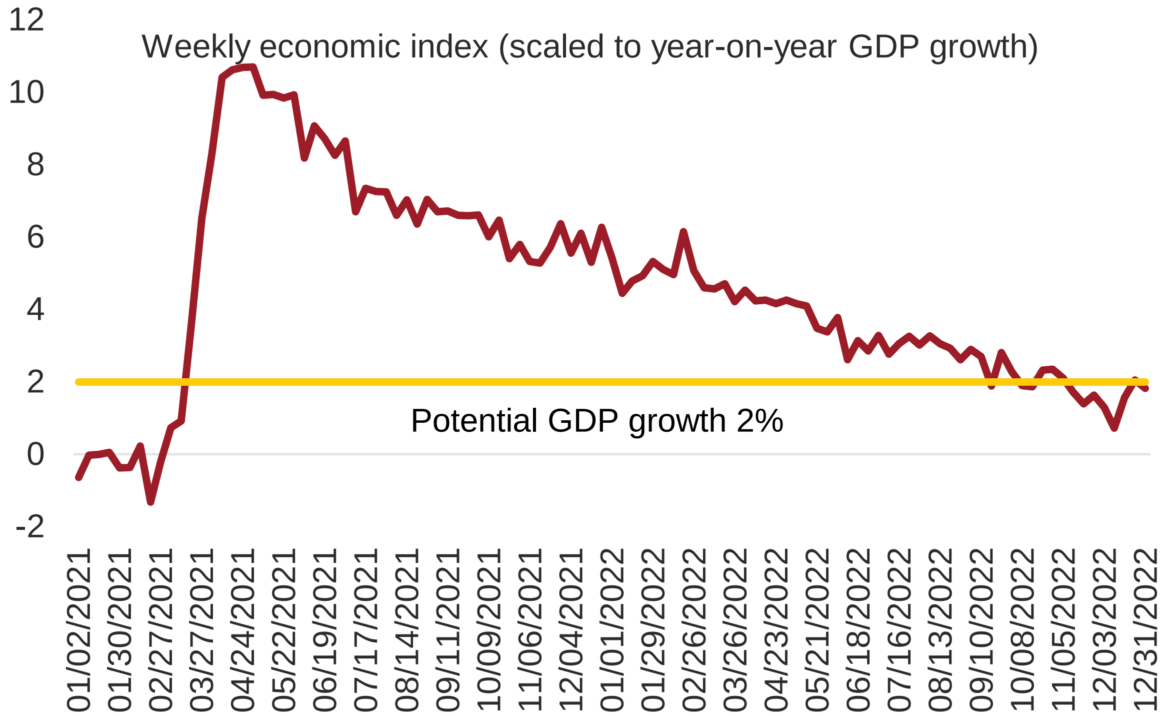


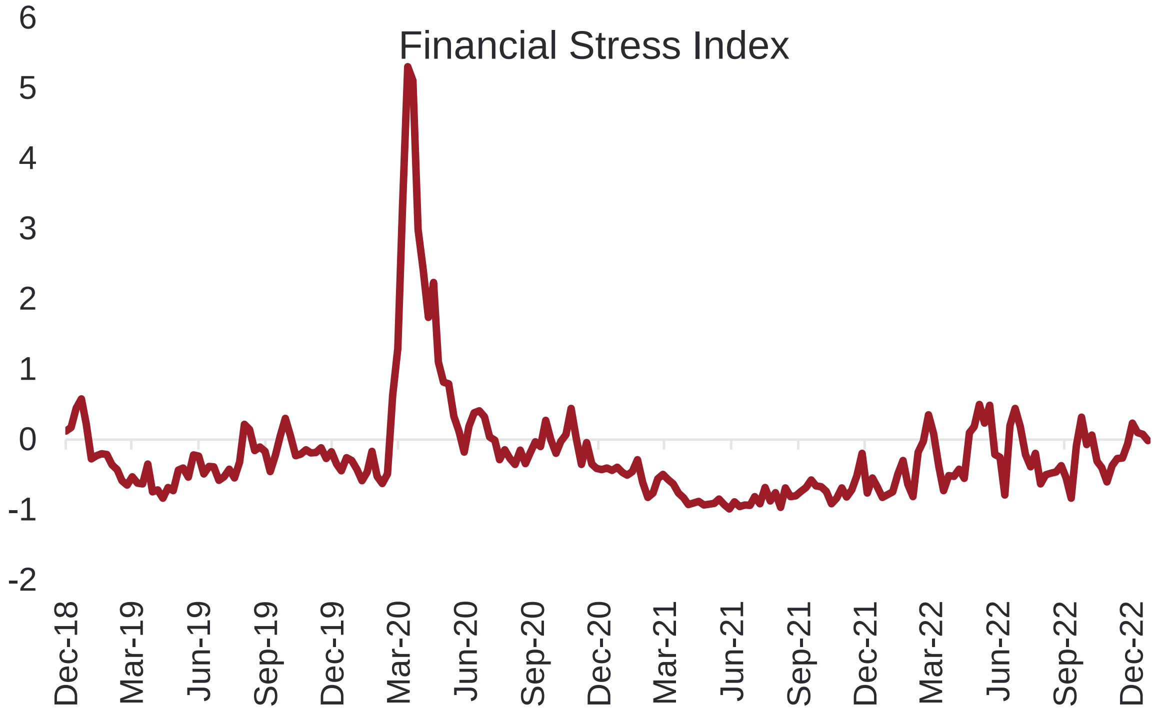

- To keep financial conditions tight as inflation is still elevated

IDFC FIRST Bank

*Source: IMF, IDFC FIRST Bank Economics Research.*

# US growth resilience: Led by strong balance sheets



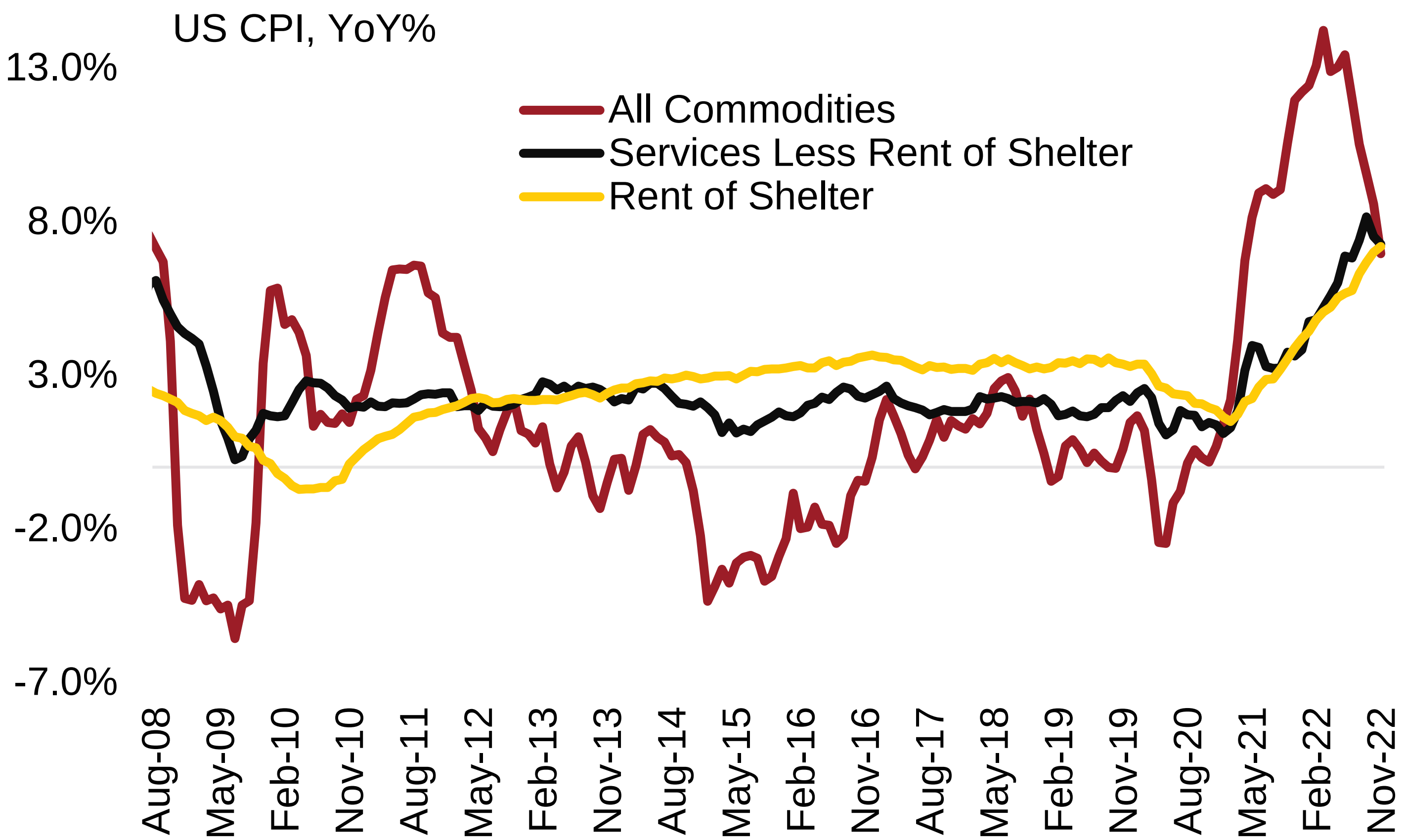

- **Household and corporate balance sheets in much better shape**
    - Household net worth has reduced from pandemic peak, but it remains well above pre-pandemic levels
- Weekly economic index – series covering consumer behavior, the labor market, and production.
- Financial Stress index - constructed from 18 weekly data series: seven interest rate series, six yield spreads and five other indicators.

IDFC FIRST Bank

*Source: CEIC, IDFC FIRST Bank Economics Research.*

# US: Inflation pressures are easing but the journey is long

Services inflation likely to remain strong

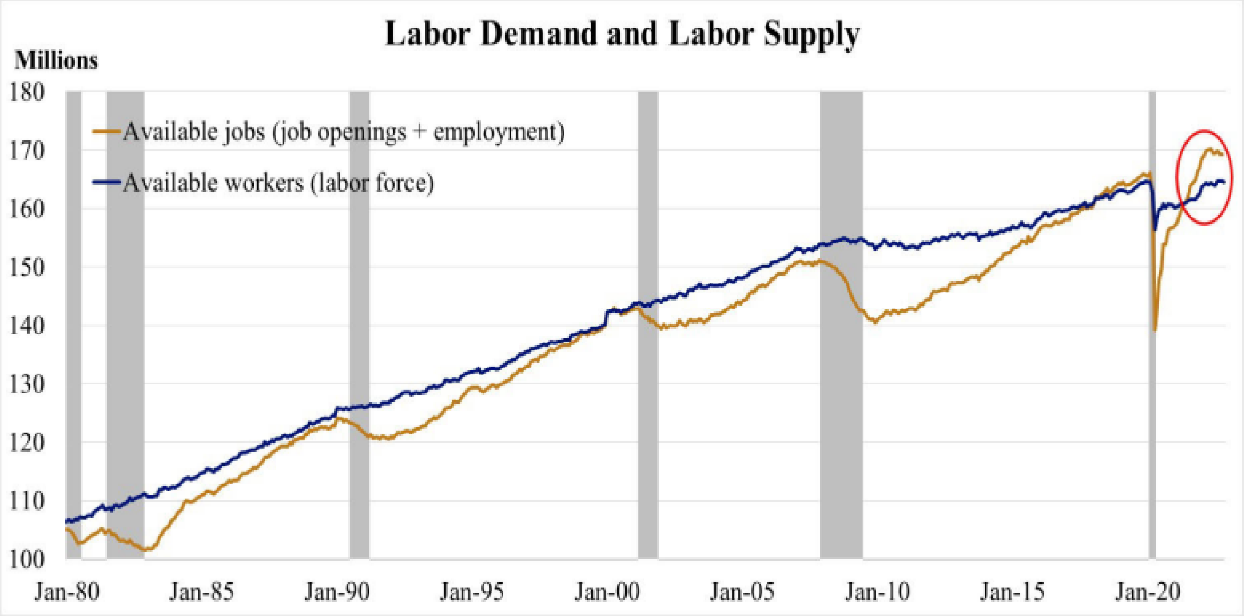



- Core services inflation to take time to decline as labour market remains strong
- The fall in house prices take time to reflect in CPI

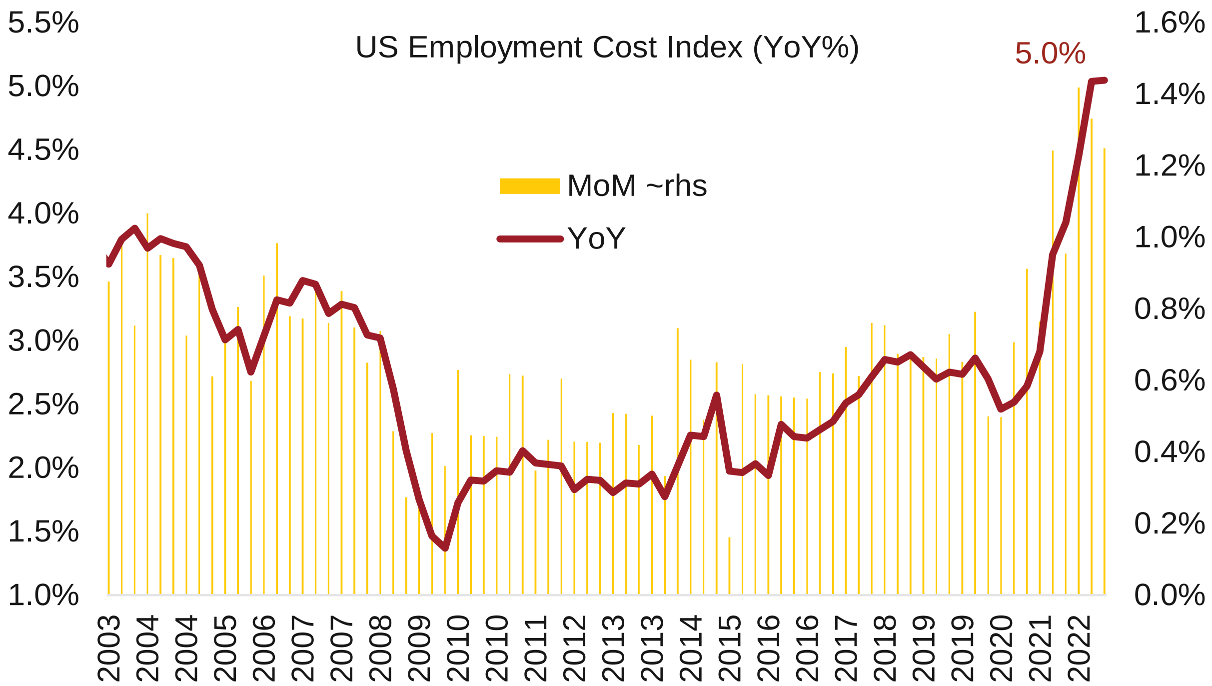
*Source: CEIC, IDFC FIRST Bank Economics Research.*

# US: Labour market remains exceptionally tight

Number of job openings > number of unemployed




*Sources: Bureau of Labor Statistics; R. Barnichon, "Building a composite Help-Wanted Index," Economics Letters, December 2010, 109, pp. 175-178; and author's calculations. Last observation: November 2022.*




- Labour market remains exceptionally strong, with more job openings than unemployed people
- Wage growth remains elevated
- Monetary policy focus on reducing demand and bring it alignment with supply

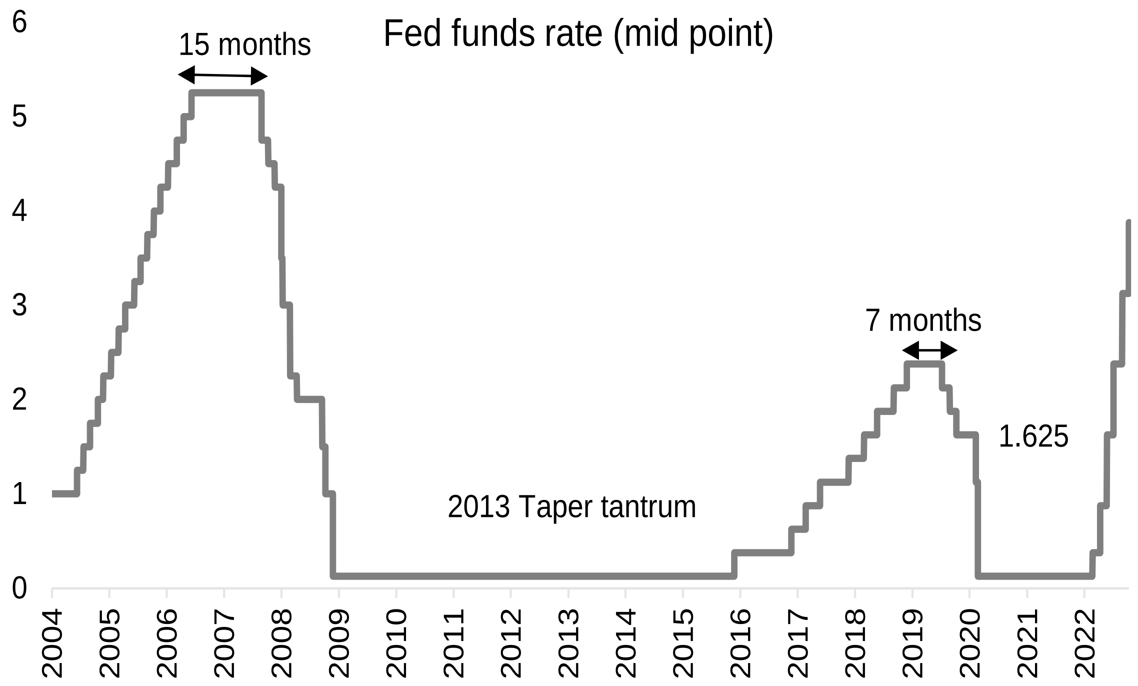
IDFC FIRST Bank

*Source: CEIC, IDFC FIRST Bank Economics Research.*

# US Fed: More rate hikes to come

FOMC indicates peak Fed Funds rate could be at 5.1% in 2023

| Year | Meeting | Real GDP | Unemployment rate | PCE inflation | Core PCE inflation | Fed funds rate |
|---|---|---|---|---|---|---|
| 2022 | Dec-22 | 0.5 | 3.7 | 5.6 | 4.8 | 4.4 |
| | Sep-22 | 0.2 | 3.8 | 5.4 | 4.5 | 4.4 |
| 2023 | Dec-22 | 0.5 | 4.6 | 3.1 | 3.5 | 5.1 |
| | Sep-22 | 1.2 | 4.4 | 2.8 | 3.1 | 4.6 |
| 2024 | Dec-22 | 1.6 | 4.6 | 2.5 | 2.5 | 4.1 |
| | Sep-22 | 1.7 | 4.4 | 2.3 | 2.3 | 3.9 |
| LR | Dec-22 | 1.8 | 4.0 | 2.0 | 0.0 | 2.5 |
| LR | Sep-22 | 1.8 | 4.0 | 2.0 | | 2.5 |

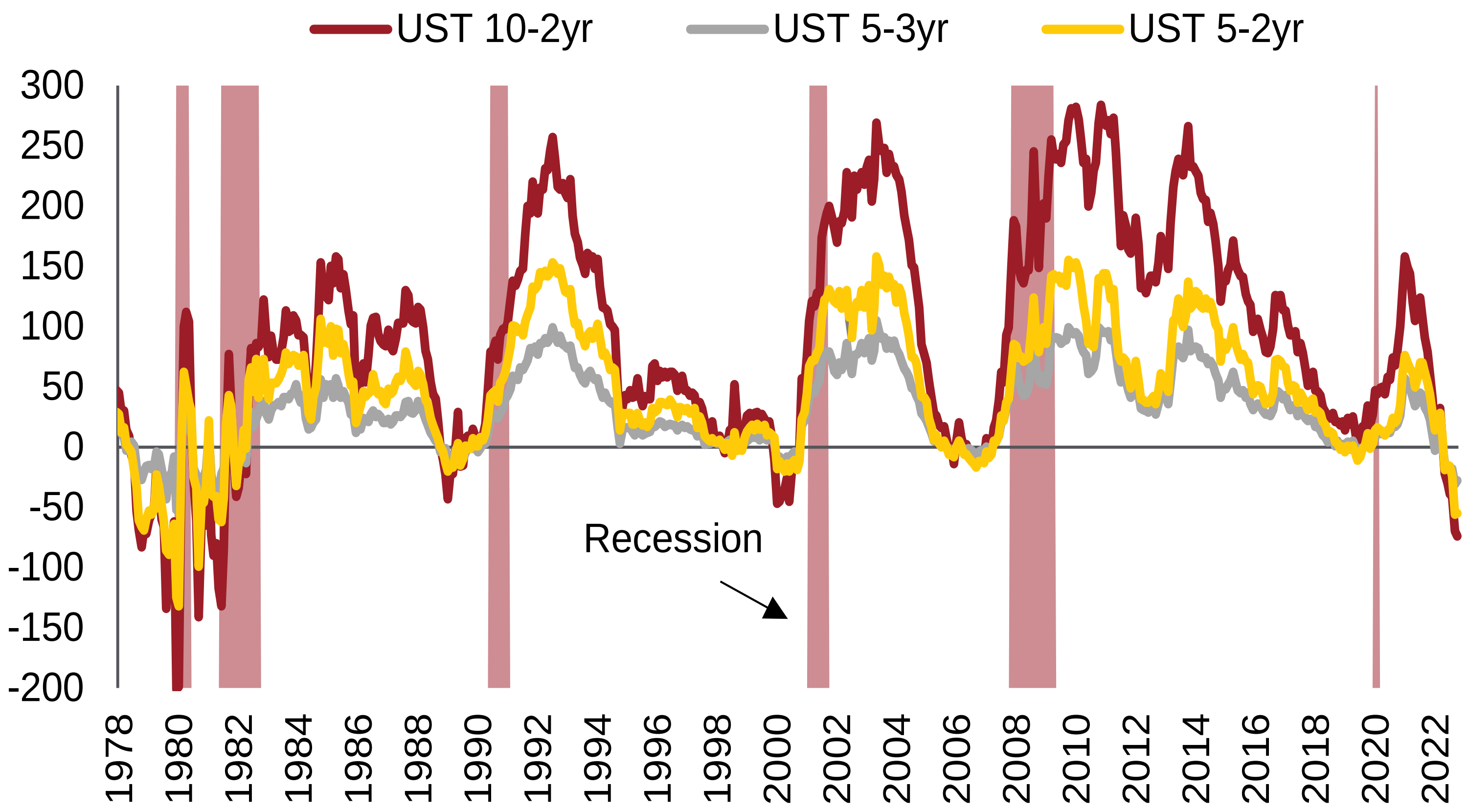



- **Implies another 75bps hike in 2023**
  - Latest FOMC dot plot shows willingness to maintain below trend growth till 2023
  - Given the strength of the US labour market and elevated inflation the Fed will need to maintain peak rate for majority of 2023

IDFC FIRST Bank

*Source: Bloomberg, IDFC FIRST Bank Economics Research.*

# US yield curve has been an accurate predictor of recession

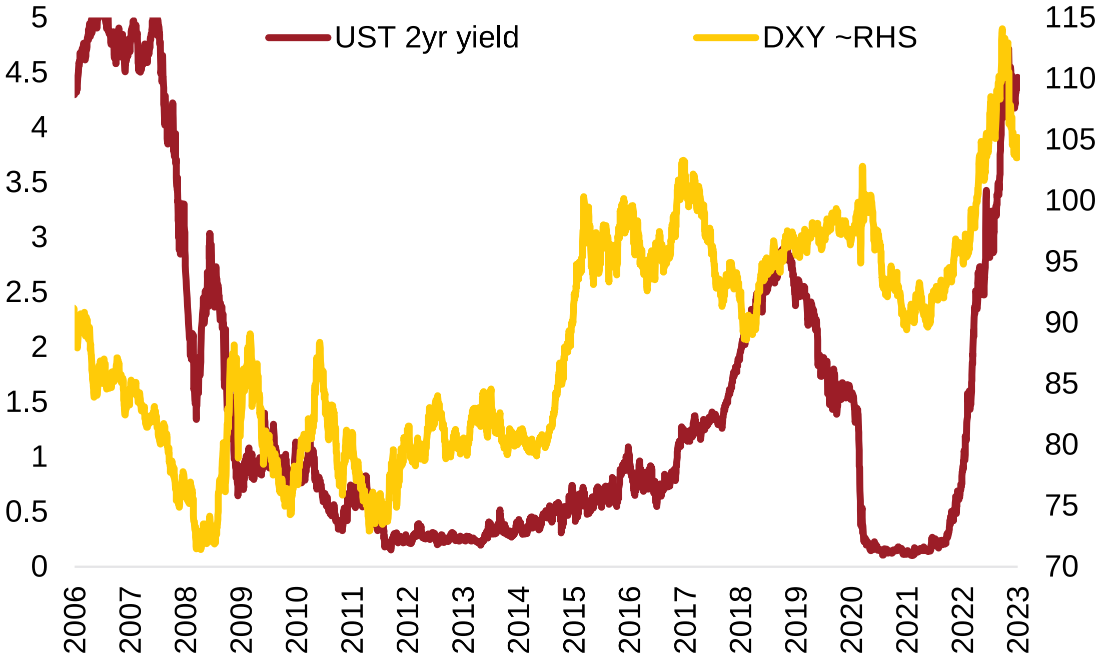


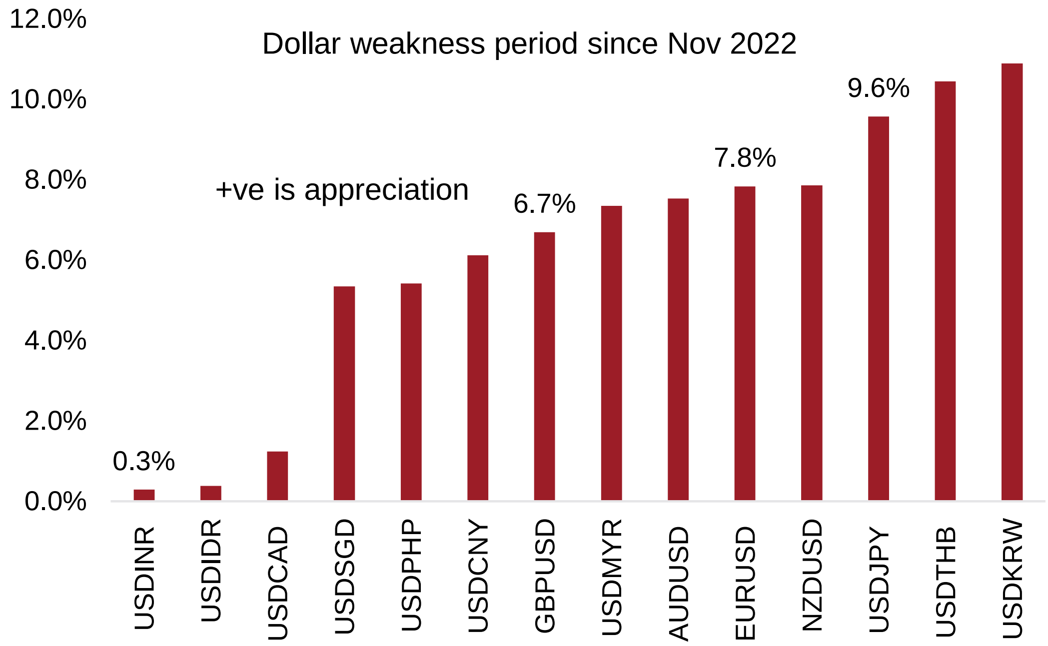

- **Yield curve inverted since July 2022**
- **Historically the yield curve inversion has a lead-time of up to 18 month**

*Source: Bloomberg, IDFC FIRST Bank Economics Research.*

# Dollar strength isn't over

Positioning adjustment overdone




- Positioning data indicates that net dollar longs have reduced by more than 60% from June 2022 peak levels
- USD strength to be supported by Fed remaining more hawkish than other Central banks and relatively better growth fundamentals than other DMs. Financial conditions in the US to tighten further next year as impact of QT is felt

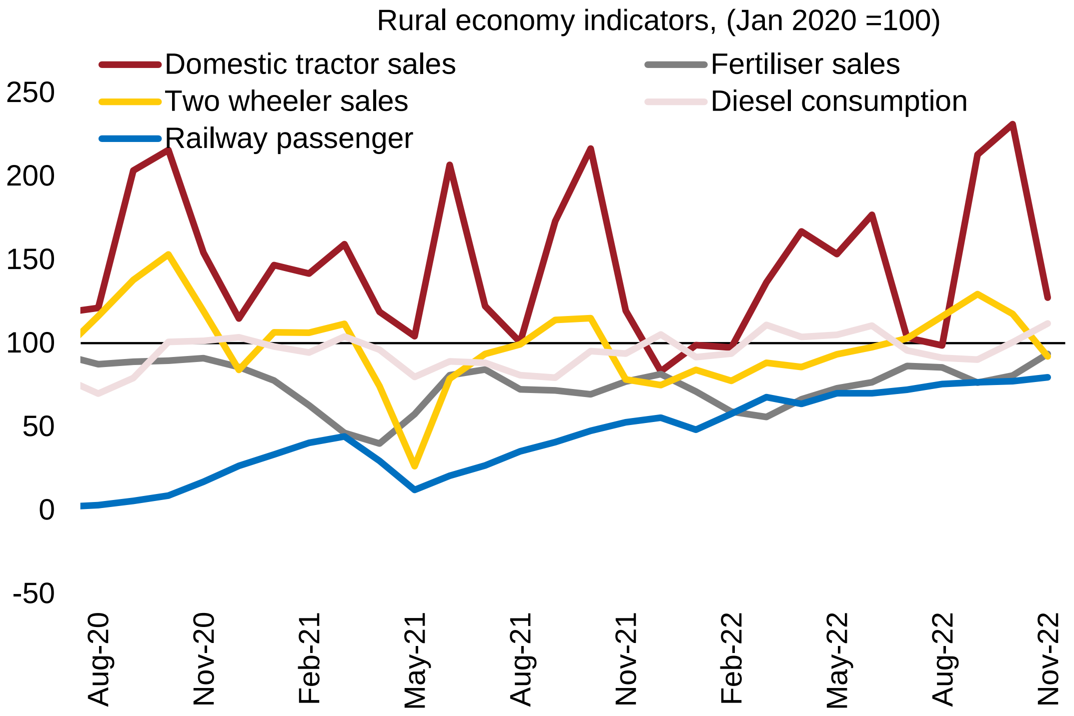
IDFC FIRST Bank

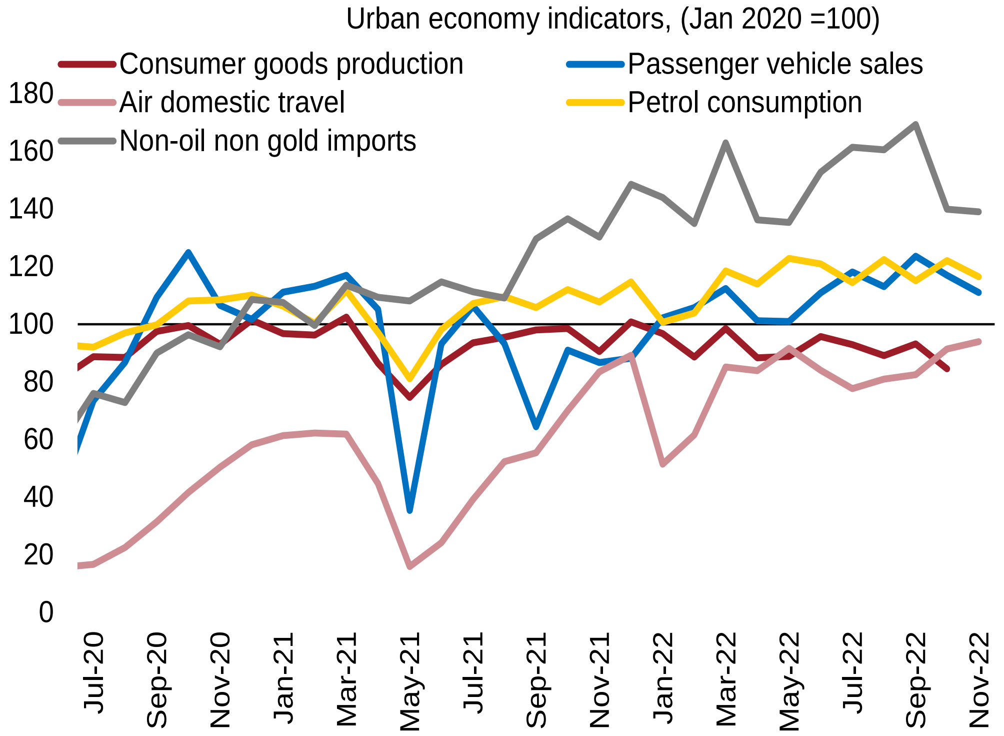
*Source: Bloomberg, IDFC FIRST Bank  Economics Research.*

# India outlook

# India growth momentum holds-up

Led by urban consumption




**FY23 GDP growth expected at 7.0%**

- Growth momentum has held-up with majority indicators above the pre-pandemic level; Impact of rate hikes yet to be felt
- Growth likely to be led by services and urban consumption

**FY24 GDP growth expected at 5.8%**

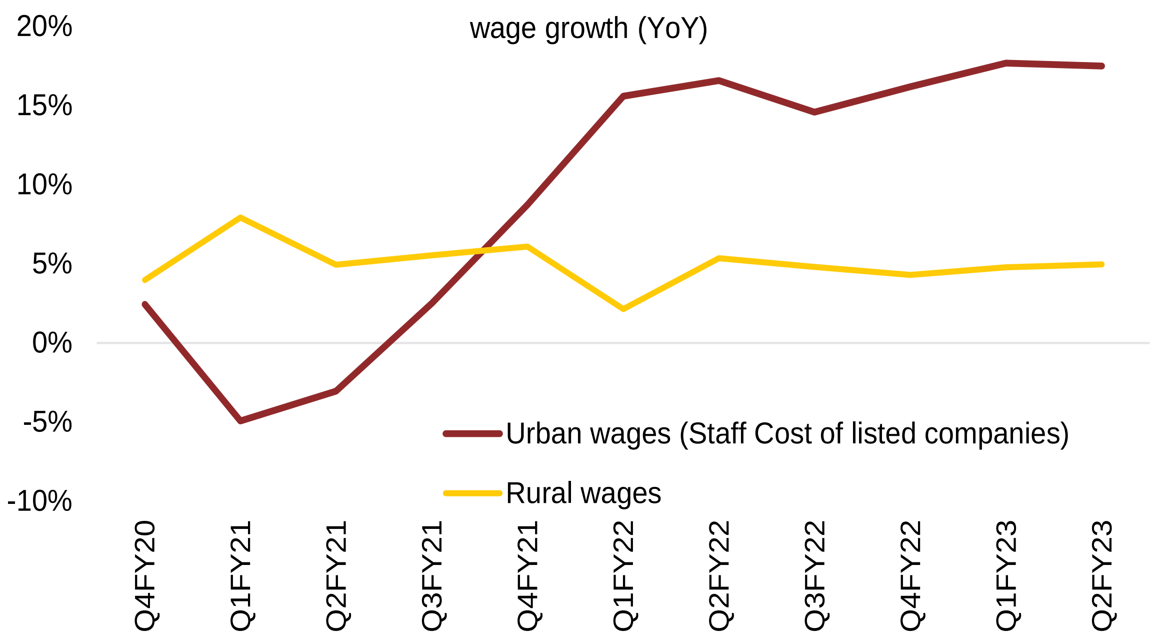
- Global growth slowdown which has impacted exports
- Transmission of rate hikes to rise as liquidity conditions tighten
- Waning support from base effects

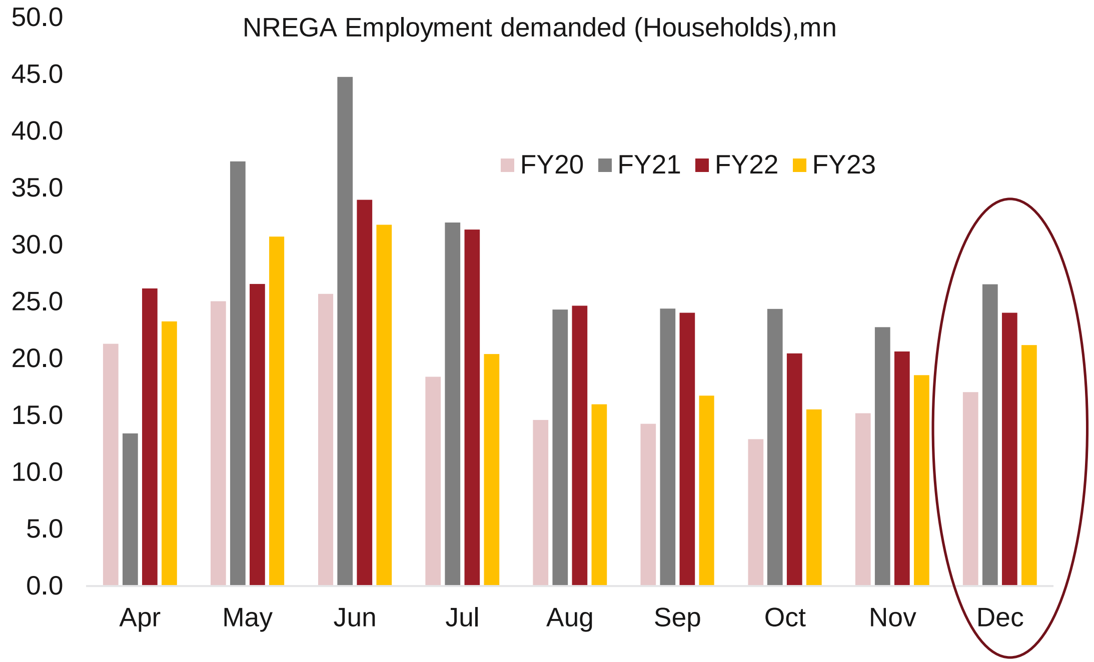
IDFC FIRST Bank

*Source: CEIC, IDFC FIRST Bank  Economics Research.*

# Differentiated pace of recovery continues

Rural wage growth remains on the weaker side



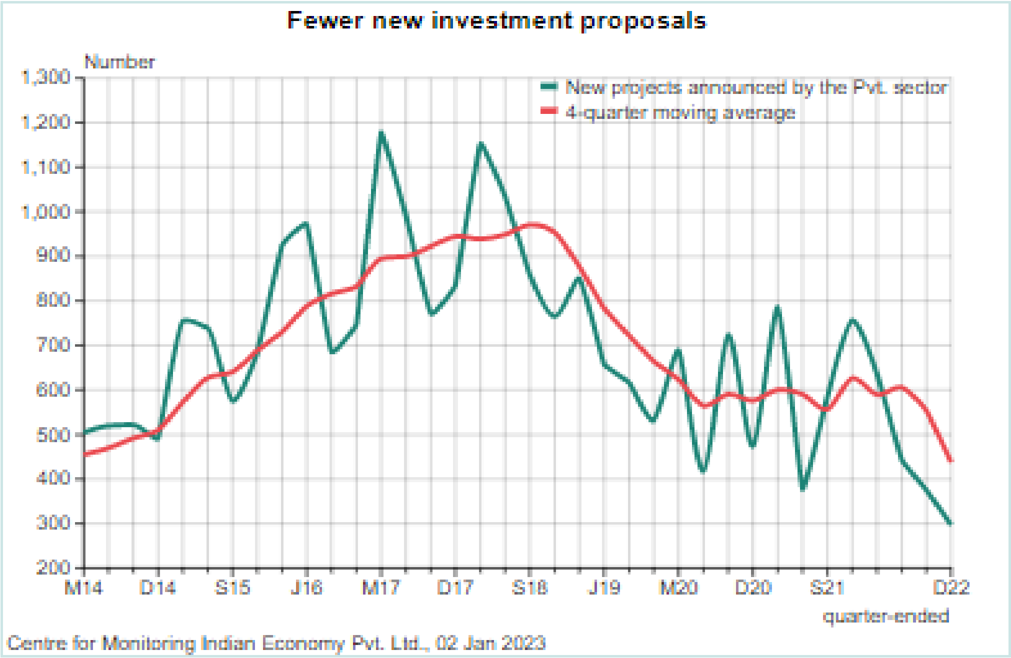



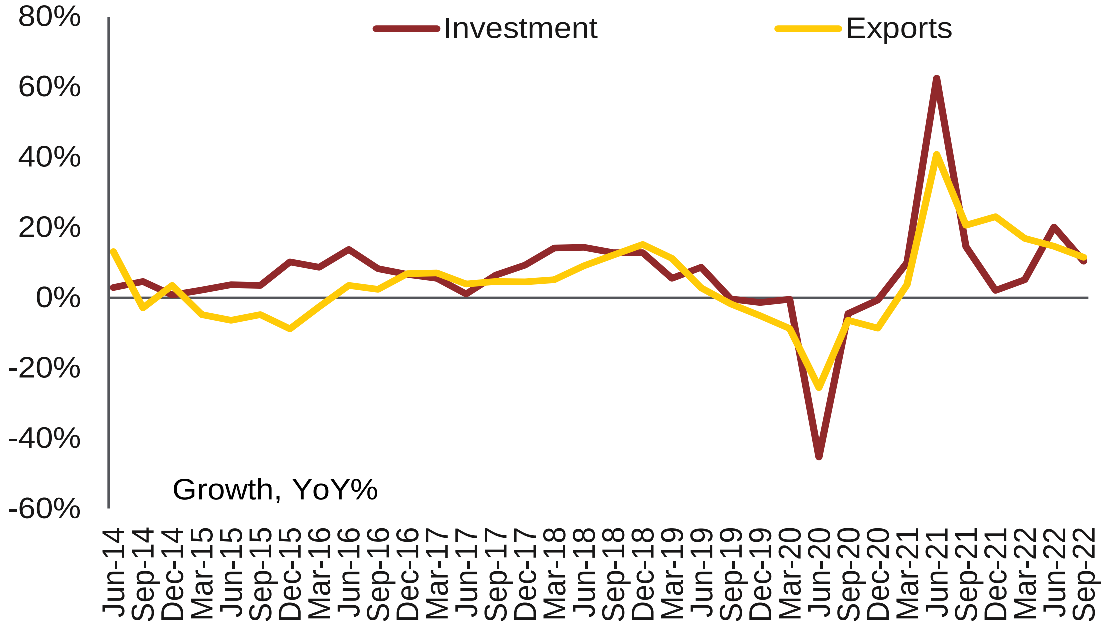

- NREGA shows demand for employment remains higher than pre-pandemic levels

IDFC FIRST Bank

*Source: CEIC, IDFC FIRST Bank Economics Research.*

# Risk from global growth slowdown in FY24

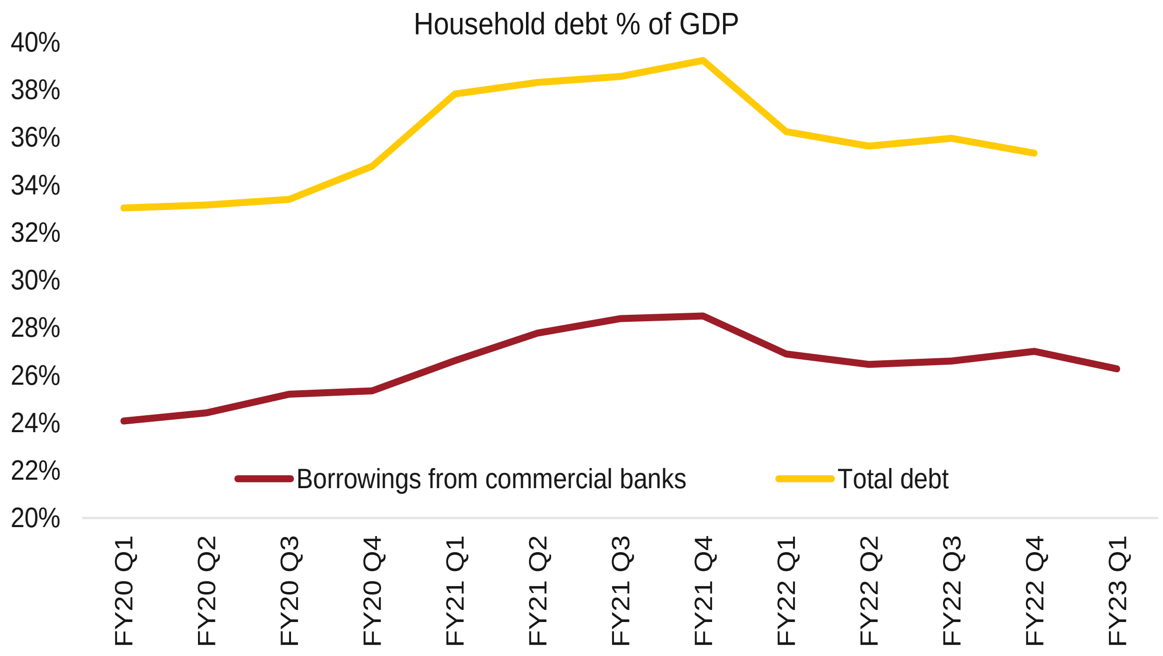


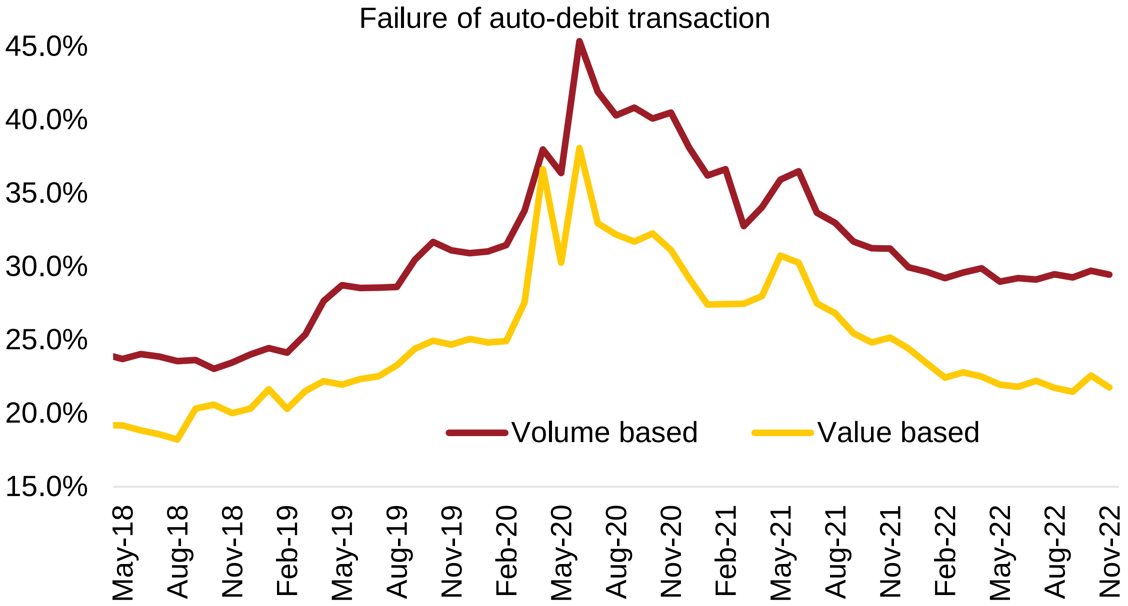




- Conditions supportive for capex cycle recovery with bank and corporate balance sheets in much better health. That said the expectation of global growth slowdown could delay recovery in private sector capex
- Support from government sector capex (Central government) is expected to continue in FY24

*Source: Bloomberg, RBI, IDFC FIRST Bank Economics Research*

# Moderate household leverage to limit impact of tighter financial conditions on consumption



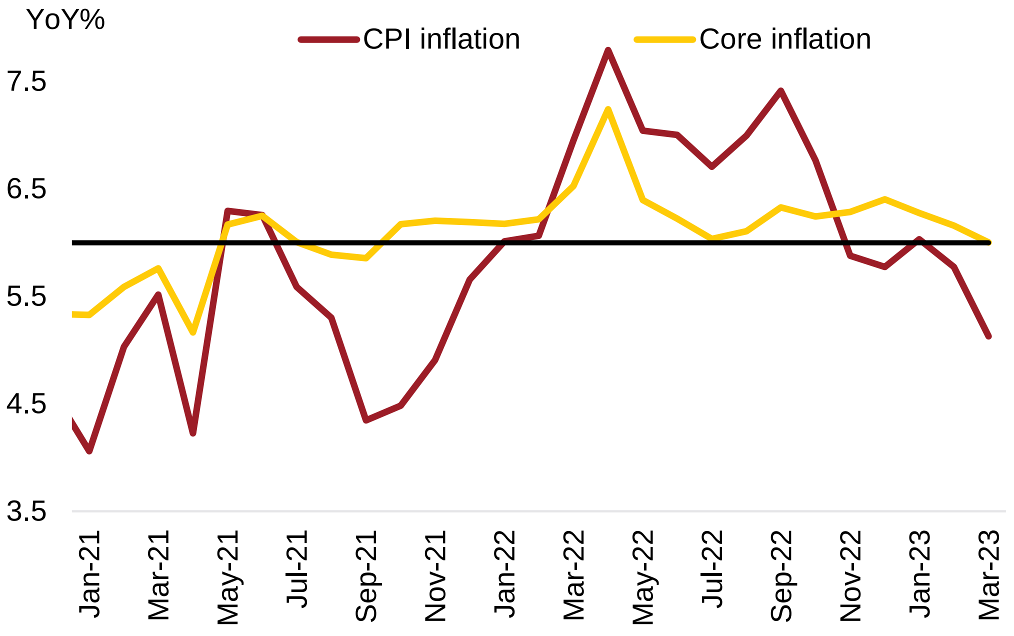

- Tighter financial conditions could dampen consumption demand but moderate leverage and credit quality holding-up will limit the impact

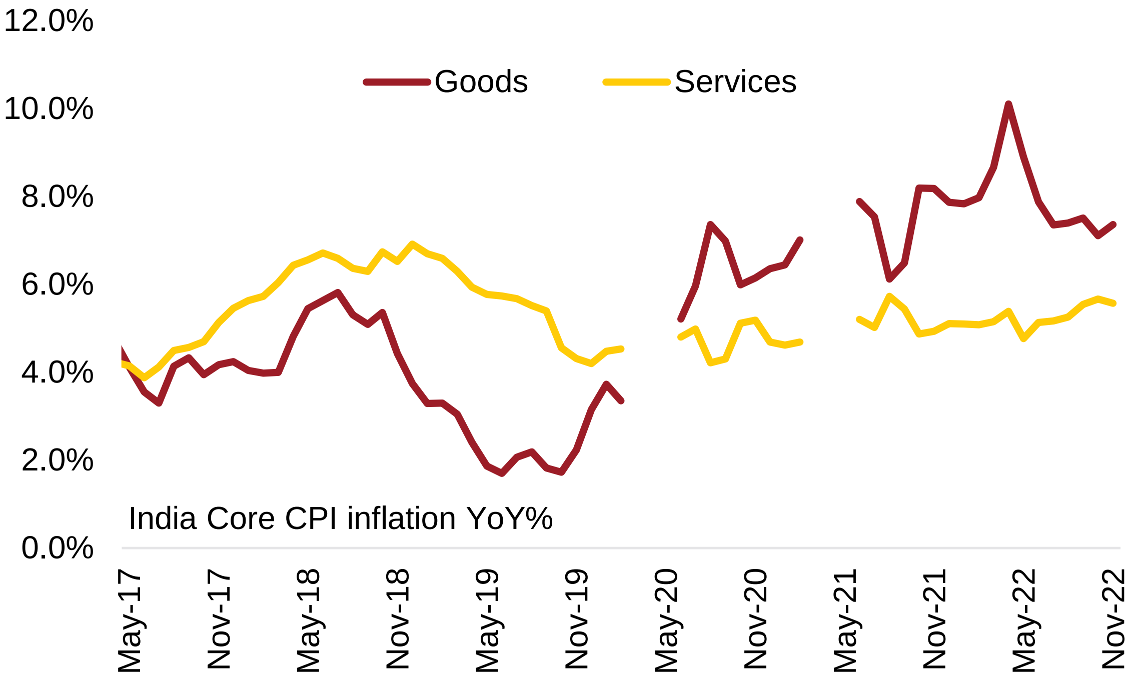
IDFC FIRST Bank

*Source: Bloomberg, RBI, IDFC FIRST Bank Economics Research*

# RBI: Terminal repo rate expected at 6.50%

25bps hike in February 2023




**One more rate hike supported by elevated core inflation and Fed**

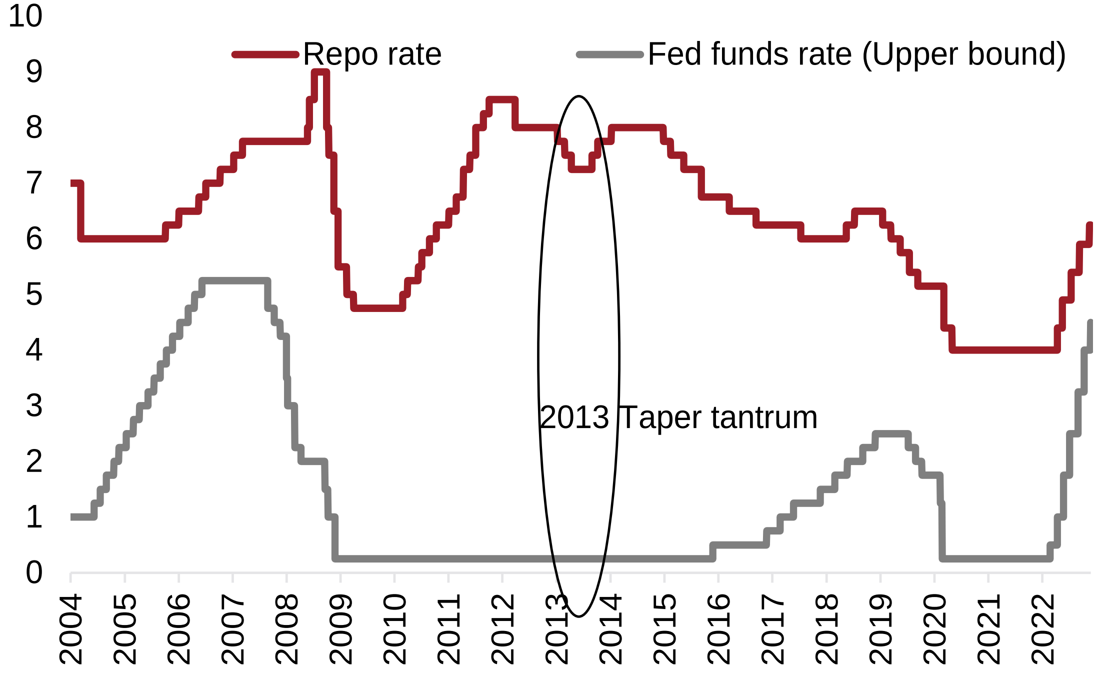
- Focus has shifted towards elevated core inflation, which could stay elevated as services sector recovery gains momentum
- External factors also support another rate hikes given Fed is likely to remain hawkish
- 25bps hike in February with stance maintained as withdrawal of accommodation

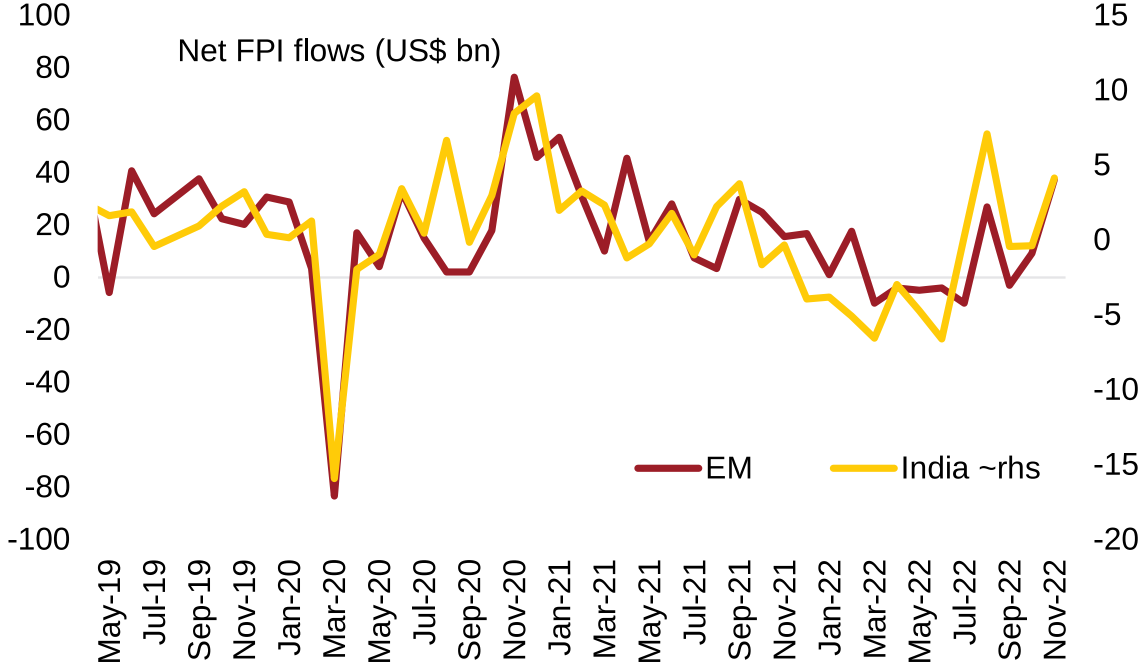


*Source: Bloomberg, RBI, IDFC FIRST Bank Economics Research*

# Depreciation pressures on INR to persist as interest rate differentials narrow

USDINR expected to trade between 81 to 83.50 till March 2023 ; Between 83.50 to 85 post March 2023



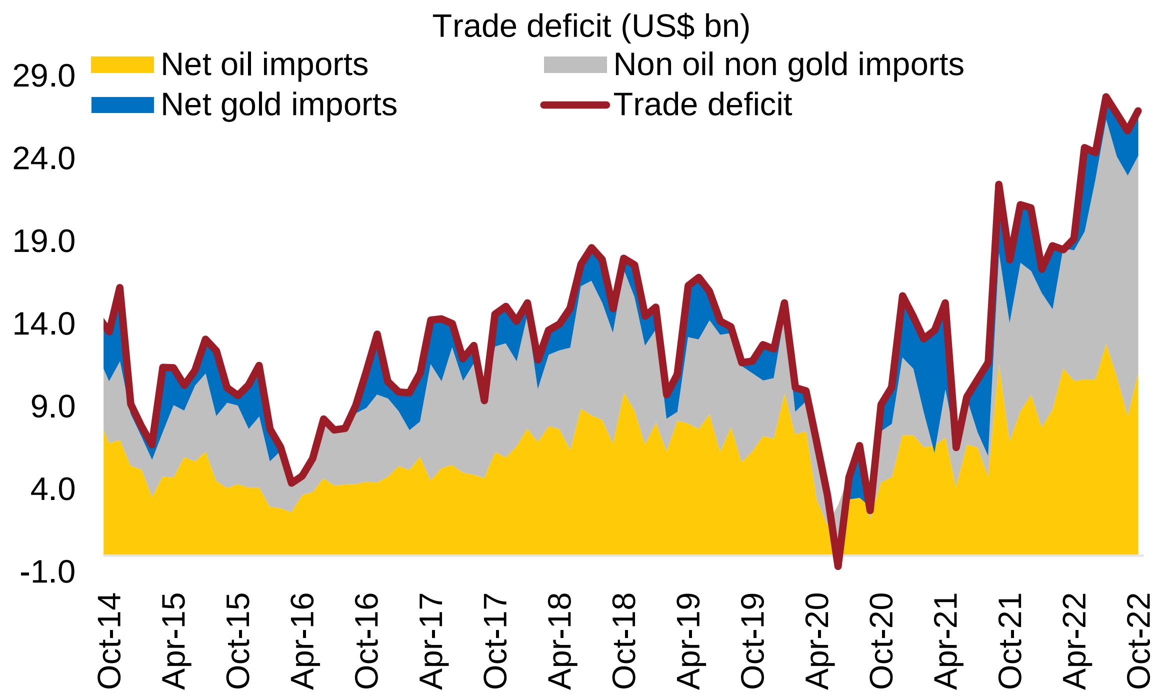

**Depreciation supported by**

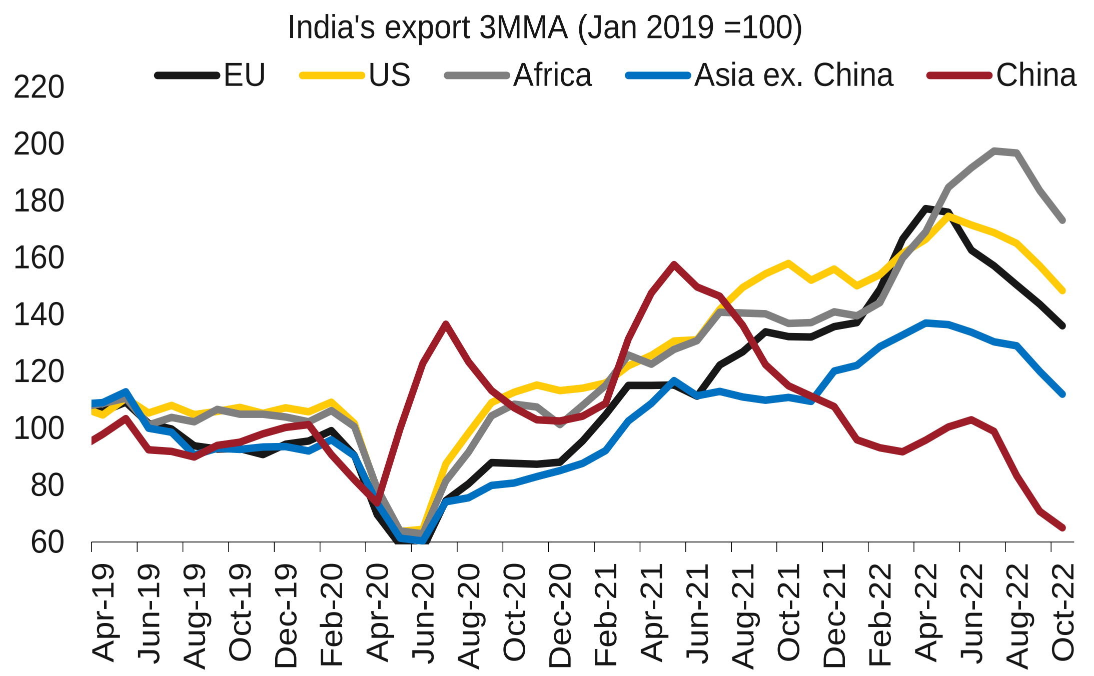
- Peak Fed funds rate of 5.1% and RBI repo rate of 6.50%, implied interest rate differentials to narrow to fresh historical lows
- Current account deficit to narrow as crude oil prices likely to remain ~US$80pb in FY24. However, weakness in exports to limit improvement.
- India to start FY24 with lower FX reserve cover
- Risk-off sentiment to keep portfolio flows volatile

*Source: CEIC, IDFC FIRST Bank  Economics Research*

# FY24 current account deficit to narrow as oil prices remain ranged

Export weakness to limit improvement



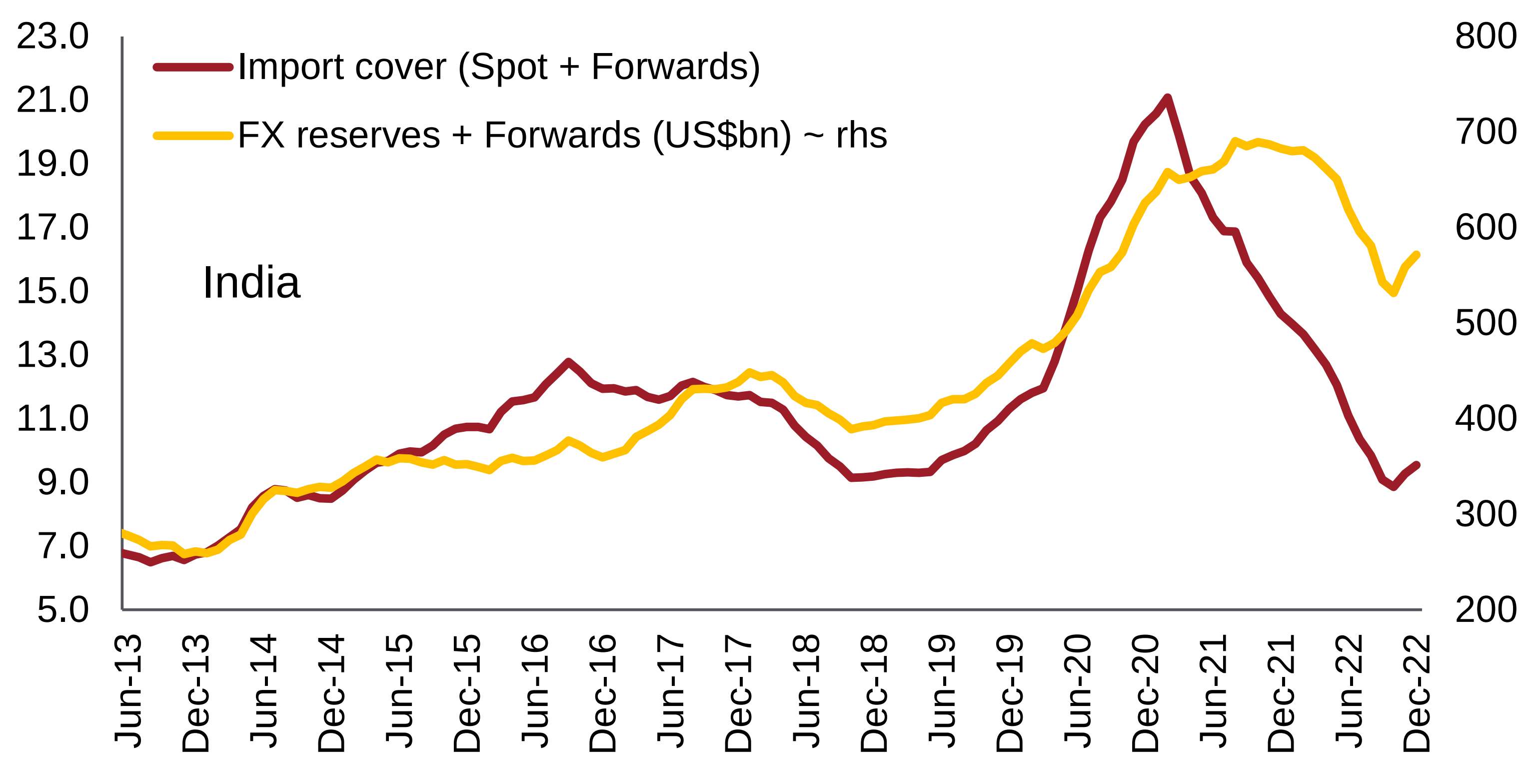

**FY24 current account deficit expected at 2.8% of GDP v/s 3.0% in FY23**

- Crude oil prices expected to average at US$80bp in FY24; Domestic demand slowdown to moderate non-oil imports
- Export weakness to intensify with global growth slowdown

IDFC FIRST Bank

*Source: CEIC, IDFC FIRST Bank Economics Research*

# FX reserve cover lower in FY24



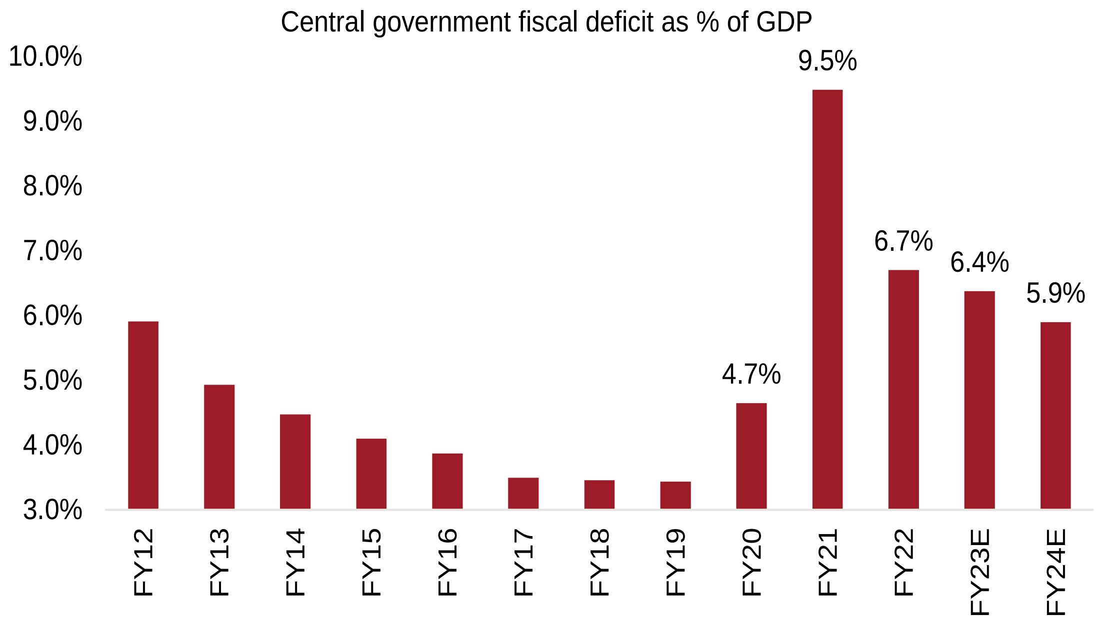

**FX cover (spot + forward book) has reduced to 9.5 months as of December 2022 v/s 14 months December 2021**

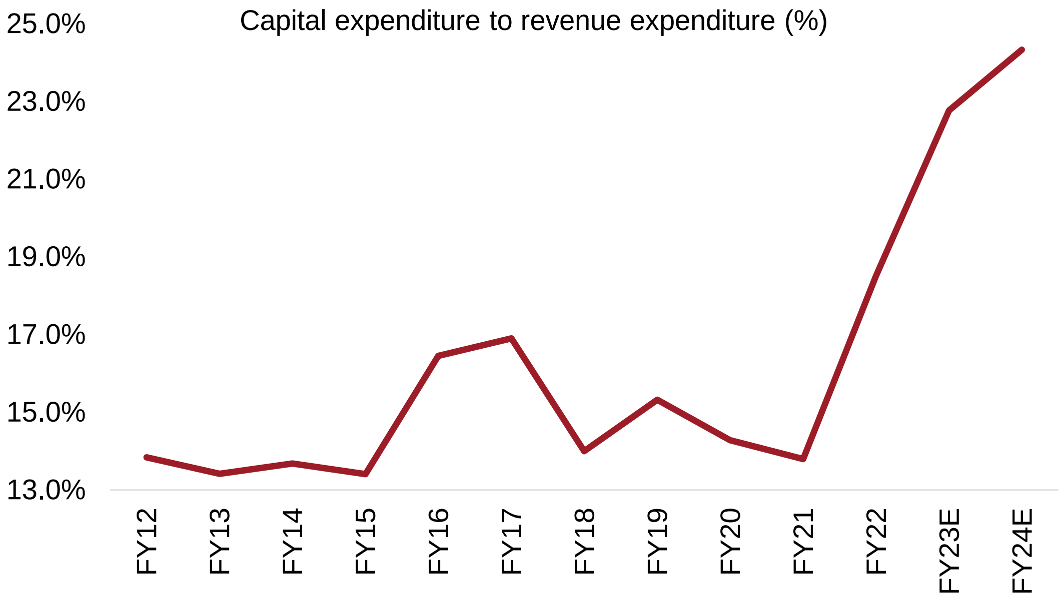
- Will limit RBI's ability to counter INR depreciation

*Source: CEIC, IDFC FIRST Bank Economics Research. * Capital Flows at Risk: India's Experience, June RBI monthly bulletin*

# FY24 fiscal deficit expected at 5.9% of GDP v/s 6.4% in FY23

Expenditure saving from lower subsidy expenditure; focus to remain on capex




**Fiscal slippage in FY23 estimated at INR800bn; no extra-borrowing expected in FY23**

- Led by rising subsidy expenditure – fertilizer, food, LPG
- Strong tax collections to limit slippage with both direct and indirect tax collection exceeding Budget Estimate

**FY24 fiscal deficit estimated at 5.9% of GDP**

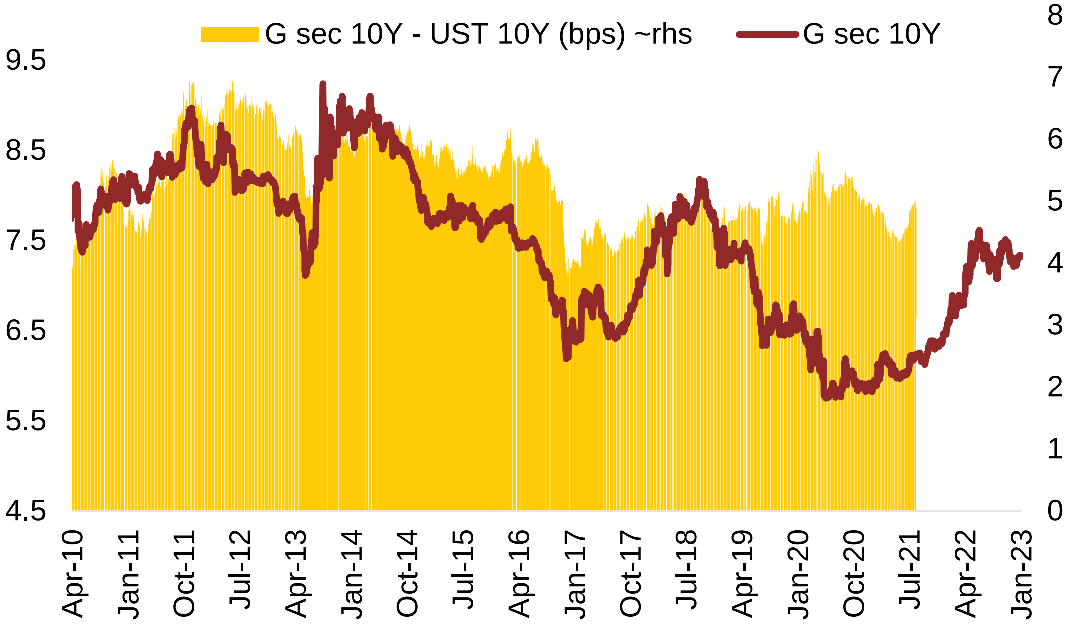
- Savings from subsidy payments estimated at INR1.6tn (fertilizer, food and LPG)
- Tax collection growth expected to slow to ~8% in FY24 from 14.5% in FY23, based on expectation of moderation in nominal GDP growth to 10.6% (v/s 15.4% in FY23) and lower fuel excise collections

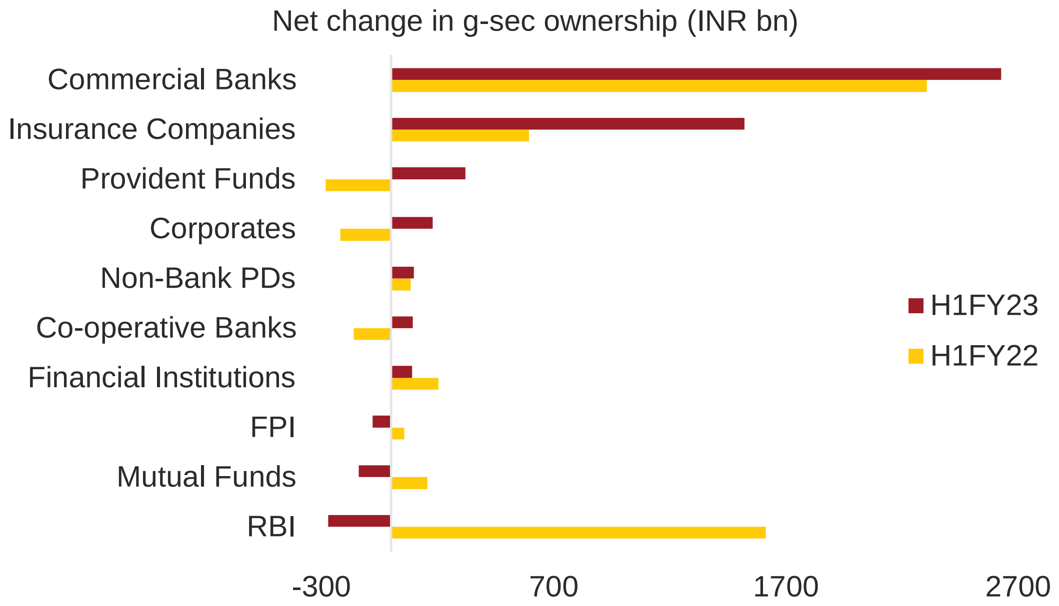
IDFC FIRST Bank

*Source: Bloomberg, RBI, IDFC FIRST Bank Economics Research*

# Investor demand for g-secs stronger than expected

10-yr yield not expected to exceed 7.5% in FY23; expected to be ranged in FY24




**In FY23 Demand supported by:**

- Net issuance of SDL lower by 10.9%YoY in FYTD23 (till December)
- Corporate bond net issuances in H1FY23 were lower by 68.6%
- Strong demand from banks, insurance companies and provident funds
- Surplus liquidity conditions persist on an average basis in FY23

**In FY24 g-sec yield to remain range-bound around 7.5%**

- Gross g-sec supply estimated at INR15.7tn (v/s INR14.2tn in FY22) and net issuance of INR11.2tn (v/s INR11.08tn in FY22)
- Gross SDL issuance in FY24 estimated at INR8.7tn (v/s INR7tn in FY23) and net issuance of INR5.86tn (v/s INR4.6tn in FY22)
- Liquidity expected to be in mild deficit
- Rate hiking cycle behind us with CPI inflation expected to average at 5% to 5.5% in FY24 v/s 6.5% in FY23

IDFC FIRST Bank

*Source: CEIC, IDFC FIRST Bank Economics Research. BE- Budget Estimate, E- IDFC FIRST Bank Estimate*

# Annex: FY24 Current account deficit expected at 2.8% of GDP

| USD bn | FY21 | FY22 | FY23E | FY24E |
|---|---|---|---|---|
| **A. CURRENT ACCOUNT (I+II)** | **23.9** | **-38.8** | **-100.4** | **-99.2** |
| AS % of GDP | 0.9 | -1.2 | -3.0 | -2.8 |
| **I. MERCHANDISE** | **-102.2** | **-189.5** | **-283.3** | **-269.5** |
| AS % of GDP | -3.8 | -6.0 | -8.3 | -7.5 |
| Total exports | 296.3 | 429.2 | 422.3 | 379.0 |
| Total imports | 398.5 | 618.6 | 705.6 | 648.5 |
| **II. INVISIBLES (a+b+c)** | **126.1** | **150.7** | **183.0** | **170.3** |
| a) Services | 88.6 | 107.5 | 139.1 | 132.3 |
| b) Transfers | 73.5 | 80.4 | 88.0 | 75.2 |
| c) Income | -36.0 | -37.3 | -44.2 | -37.3 |
| | | | | |
| **B Total Capital Account (1 to 5)** | **63.7** | **85.8** | **56.0** | **72.8** |
| As % of GDP | 2.4 | 2.7 | 1.6 | |
| a) Foreign Direct Investment (i+ii) | 44.0 | 38.6 | 38.1 | 38.3 |
| b) Portfolio Investment | 36.1 | -16.8 | -1.2 | 7.6 |
| 2.Loans (a+b+c) | 6.9 | 33.6 | 18.6 | 20.0 |
| 3. Banking Capital (a+b) | -21.1 | 6.7 | 0.6 | 7.0 |
| **D. Overall Balance (A+B+C)** | **87.3** | **47.5** | **-44.4** | **-26.4** |

IDFC FIRST Bank

*Source: CEIC, IDFC FIRST Bank Economics Research*

# Annex: FY24 fiscal deficit expected at 5.9% of GDP

| | Rs bn | | | | % GDP | | | |
|---|---|---|---|---|---|---|---|---|
| | FY22 | FY23BE | FY23E | FY24E | FY22A | FY23BE | FY23E | FY24E |
| **Revenue Receipts** | **21684** | **22044** | **24088** | **25521** | **9.2%** | **8.5%** | **8.8%** | **8.5%** |
| **Gross tax revenue** | **27083** | **27578** | **31011** | **33449** | **11.4%** | **10.7%** | **11.4%** | **11.1%** |
| Corporate tax | 7120 | 7200 | 8623 | 9087 | 3.0% | 2.8% | 3.2% | 3.0% |
| Income tax | 6734 | 7000 | 8535 | 9665 | 2.8% | 2.7% | 3.1% | 3.2% |
| CGST | 5912 | 6600 | 6966 | 7961 | 2.5% | 2.6% | 2.6% | 2.6% |
| Compensation cess | 1046 | 1200 | 1255 | 1292 | 0.4% | 0.5% | 0.5% | 0.4% |
| Customs | 1991 | 2130 | 2048 | 1963 | 0.8% | 0.8% | 0.8% | 0.7% |
| Excise | 3908 | 3350 | 3202 | 3039 | 1.7% | 1.3% | 1.2% | 1.0% |
| **Tax Revenue (Net)** | **18204** | **19348** | **21610** | **23100** | **7.7%** | **7.5%** | **7.9%** | **7.6%** |
| **Non-Tax Revenue** | **3480** | **2697** | **2479** | **2421** | **1.5%** | **1.0%** | **0.9%** | **0.8%** |
| --Dividend RBI & PSB | 1071 | 739 | 343 | 760 | 0.5% | 0.3% | 0.1% | 0.3% |
| **Non-Debt Capital Receipts** | **392** | **793** | **600** | **800** | **0.2%** | **0.3%** | **0.2%** | **0.3%** |
| -Disinvestment | 146 | 650 | 450 | 650 | 0.1% | 0.3% | 0.2% | 0.2% |
| **Total Receipts** | **22076** | **22837** | **24688** | **26321** | **9.3%** | **8.9%** | **9.0%** | **8.7%** |
| **Revenue Expenditure** | **32014** | **31947** | **34294** | **35460** | **13.5%** | **12.4%** | **12.6%** | **11.7%** |
| -Interest Payments | 8054 | 9407 | 9407 | 10327 | 3.4% | 3.6% | 3.4% | 3.4% |
| -Subsidy | 5008 | 3556 | 5702 | 4131 | 2.1% | 1.4% | 2.1% | 1.4% |
| --Food subsidy | 2890 | 2068 | 2872 | 2642 | 1.2% | 0.8% | 1.1% | 0.9% |
| --Fertilizer subsidy | 1537 | 1052 | 2145 | 1052 | 0.6% | 0.4% | 0.8% | 0.3% |
| Capital Expenditure | 5928 | 7502 | 7813 | 8641 | 2.5% | 2.9% | 2.9% | 2.9% |
| **Total Expenditure** | **37942** | **39449** | **42107** | **44101** | **16.0%** | **15.3%** | **15.4%** | **14.6%** |
| **Fiscal Deficit** | **15865** | **16612** | **17418** | **17780** | **6.7%** | **6.4%** | **6.4%** | **5.9%** |
| | | | | | | | | |
| Nominal GDP | 236646 | 258000 | 273078 | 302024 | | | | |
| Nominal GDP - growth | 19.5% | 9.0% | 15.4% | 10.6% | | | | |

IDFC FIRST Bank

*Source: CEIC, IDFC FIRST Bank  Economics Research*

# Annex: FX reserve adequacy

| | FX reserves (US$ bn) | Volatile capital flows (as % of FX reserves) | Short-term external debt % of FX reserves (original maturity) | Short-term debt % of FX reserves (residual maturity) | Import cover (Spot + Forwards) | FPI holdings of government debt (as % of FX reserves) | Net FPI holdings of equity (as % of FX reserves) | Net FPI holdings of debt (as % of FX reserves) |
|---|---|---|---|---|---|---|---|---|
| FY14 | 304 | 96% | 30% | 57.4% | 7.0 | 1.9% | 47.0% | 19.0% |
| FY22 | 606 | 63% | 20% | 44.1% | 13.0 | 3.4% | 25.6% | 17.2% |
| FY23E | 542 | 69% | 24% | 50.7% | 9.4 | 3.4% | 24.1% | 19.2% |
| FY24E | 516 | 74% | 26% | 53.3% | 9.5 | 3.5% | 25.3% | 20.2% |

IDFC FIRST Bank

*Source: CEIC, IDFC FIRST Bank  Economics Research*

# Disclaimer

- Disclaimer: This Report is published by the Financial Markets Group of IDFC FIRST Bank Ltd. for purpose of information dissemination and is meant for private circulation only. This document does not constitute an offer or solicitation for the purchase or sale of any financial instrument or as an official confirmation of any transaction.
- The information contained herein is from publicly available data or other sources believed to be reliable. While we would endeavor to update the information herein on reasonable basis, the opinions and information in this report are subject to change without notice and IDFC FIRST Bank, its subsidiaries and associated companies, their directors and employees (“IDFC FIRST Bank and affiliates”) are under no obligation to update or keep the information current. Also, there may be regulatory, compliance, or other reasons that may prevent IDFC FIRST Bank and affiliates from doing so. Thus, the opinions expressed herein should be considered those of IDFC FIRST Bank as of the date on this document only. We do not make any representation either express or implied that information contained herein is accurate or complete and it should not be relied upon as such. The information contained in this document has no regard to the specific investment objectives, financial situation or particular needs of any specific recipient. This document is prepared for assistance only and is not intended to be and must not alone be taken as the basis for an investment decision. The investment discussed or views expressed in the document may not be suitable for all investors. Investors should make their own investigations as they deem necessary to arrive at an independent evaluation of an investment in the securities referred to in this document (including the merits and risks involved) and investment decisions based upon their own financial objectives and financial resources. Investors assume the entire risk of any use made of the information contained in the document. Investments in general involve some degree of risk, including the risk of capital loss. Past performance is not necessarily a guide to future performance and an investor may not get back the amount originally invested.
- Foreign currency-denominated securities are subject to fluctuations in exchange rates that could have an adverse effect on the value or the price of, or income derived from, the investment. In addition, investors in securities, the values of which are influenced by foreign currencies, effectively assume currency risk.
- Affiliates of IDFC FIRST Bank may have issued other reports that are inconsistent with and reach different conclusions from, the information presented in this report. This report is not directed or intended for distribution to, or use by, any person or entity who is a citizen or resident of or located in any locality, state, country or other jurisdiction, where such distribution, publication, availability or use would be contrary to law, regulation or which would subject IDFC FIRST Bank and affiliates to any registration or licensing requirement within such jurisdiction. The securities described herein may or may not be eligible for sale in all jurisdictions or to a certain category of investors. Persons in whose possession this document may come are required to inform them of, and to observe, such applicable restrictions.
- Reports based on technical analysis centers on studying charts of a stock's price movement and trading volume, as opposed to focusing on a company's fundamentals and, as such, may not match with a report on a company's fundamentals.
- IDFC FIRST Bank and affiliates, their directors, officers, and employees may from time to time have positions in, purchase or sell, or be materially interested in any of the securities mentioned or related securities. IDFC FIRST Bank and affiliates may from time to time solicit from, or perform investment banking, or other services for, any company mentioned herein. Without limiting any of the foregoing, in no event shall IDFC FIRST Bank, any of its affiliates or any third party involved in, or related to, computing or compiling the information have any liability for any damages of any kind including but not limited to any direct or consequential loss or damage, however arising, from the use of this document. Any comments or statements made herein are those of the analyst and do not necessarily reflect those of IDFC FIRST Bank and affiliates.
- This document is subject to changes without prior notice and is intended only for the person or entity to which it is addressed and may contain confidential and/or privileged material and is not for any type of circulation. Any review, retransmission, or any other use is prohibited.
- Though disseminated to all the customers simultaneously, not all customers may receive this report at the same time. IDFC FIRST Bank will not treat recipients as customers by virtue of their receiving this report.
- IDFC FIRST Bank and its affiliates (i) may have received compensation from the company covered herein in the past twelve months for investment banking services; or (ii) may expect to receive or intends to seek compensation for investment-banking or any other such services from the subject company in the next three months from publication of the research report.
- Affiliates of IDFC FIRST Bank may have managed or co-managed in the previous twelve months a private or public offering of securities for the subject company.
- IDFC FIRST Bank and affiliates collectively do not hold more than 1% of the equity of the company that is the subject of the report as of the end of the month preceding the distribution of the research report.
- IDFC FIRST Bank and affiliates are not acting as a market maker in the securities of the subject company.
- 