

Economic Round-up: June 2024

Markit global manufacturing PMI eased slightly to 50.9 in Jun'24 from 51 in Apr'24. The index stood in the expansionary zone for the 5th consecutive month in a row, and was supported by rise in output, new orders, employment, and supplier delivery times. Worryingly, new export orders continued to decline, and input prices rose at the fastest pace in 16 months, with pressure visible more in case of developed nations, than emerging nations. Country-wise, Asian economies held ground, while activity weakened in Eurozone, and US (ISM index). In both US and China, there appears to be divergence in growth trends. In the US, while manufacturing sector and consumer confidence has taken a hit, labour market still remains relatively tight. In case of China, non-manufacturing sector and export and consumer related small and mid-size manufacturing are doing better than larger state owned manufacturing companies, which are more impacted by investment demand. In India, earlier than expected arrival of monsoon in the country, has narrowed the deficit as of 2 July (at 95% of its LPA), and this trend is expected to be positive for food prices. Markets now await announcement of full budget, most likely in the third week of July.

Global growth: Unevenness in global growth was visible in May/Jun'24. In the US, manufacturing activity continues to decline, and consumer confidence has also taken a beating. Labour market remains relatively steady, with initial jobless claims declining, job openings increasing. But job to unemployed person ratio still remains unchanged at its lowest level since 2021. In China, while consumer related sectors are performing well (small/mid-size manufacturing firms, retail sales), investment demand remains weak, due to moderation in FAI growth, thus impacting larger state owned manufacturing firms. In Eurozone, manufacturing activity is contracting at faster pace. Germany's Ifo business climate index also shows drop in sentiment in case of manufacturing and trade.

Global Central Banks: In Jun'24, US Fed and BoE, kept their respective rates on hold. Fed officials are increasingly sounding dovish, led by remarks of Fed Chair Powell. The Chair stated that central bank is likely to cut rates sometime later this year. As a result, probability of a rate cut by Fed in Sep'24 has increased. In case of BoE, markets are pricing in a rate cut in Sep/Nov'24, tracking trend in services inflation and wage growth. ECB announced 25bps rate cut in Jun'24, but is expected to remain on pause in its Jul'24 meeting. In contrast, uncertainty around the timing of rate hike by BoJ has increased as growth falters. However it is expected to announce ~\$100bn cut in its bond purchase program in the Jul'24 meeting.

Key macro data releases: INR appreciated marginally in Jun'24, after touching a fresh record-low during the month. Domestic conditions remain more or less the same for INR and suggest an appreciating bias for the currency. **We expect INR to trade in the range of 83.25-83.75/\$. We expect India's 10Y yield to trade in the range of 6.95%-7.05% in Jul'24**, with risk evenly balanced. **Core sector growth** for May'24 came in at a steady 6.3% as against 5.2% last year. The base effect did provide a prop to segments which did well. Power sector growth of 12.8% was mainly due to the heatwave which led to higher demand. **CPI inflation** came in at 4.75% in May'24, on YoY basis, marginally lower than our estimate of 4.9%. **Food inflation** remained sticky at 8.7% in May'24. **Core CPI (excl. food and fuel)** softened to 3.1%, on YoY basis. Apart from personal care and effects, sub-categories of core showed moderation across the board.

Global developments

Global growth: Remains in peril

Final estimates for US GDP growth in Q1CY24 showed that GDP rose by 3.4%. Upward revision was led by higher than previously estimated growth in non-residential fixed investment, government spending and lower imports. On the other hand, consumer spending was revised further lower (1.5% versus 2% as per 2nd estimates). High frequency data shows divergence in growth of different sectors. For instance, US ISM manufacturing index fell for the 3rd consecutive month in Jun'24, with index at 48.5 versus 48.7 in May'24. It was dragged lower by production, employment and new export index. Conference Board consumer confidence index slipped to 100.4 in Jun'24 from 101.3 in May'24. As per the survey results, the present situation index improved (141.5 versus 140.8), while the expectations index dropped (73 versus 74.9). Present situation optimism was driven by relative tightness in the labour market. Initial jobless claims fell by 6k in the week ending 22 Jun'24 to 233k. However, 4-week moving average of continued claims has risen by 12,250 to reach 1.82mn—highest level since Dec'21 (1.86mn). In contrast, retail sales rose by 0.1% in May'24, rebounding from (-) 0.2% decline in Apr'24. Core retail sales (excluding gasoline and motor vehicle & parts) also bounced back (0.1% versus -0.3%), helped by sales of sporting goods/hobby/musical instruments, and building material and gardening equipment.

In Eurozone, manufacturing activity weakened further towards the end of second quarter. The Markit PMI index eased to 45.8 in Jun'24 (2-month low) from 47.3 in May'24, dragged by fall in output, new orders, purchasing activity. Country-wise, only Italy noted improvement, while activity in other economies faltered. In case of major economies like Germany and France weakening of activity remains a significant cause of concern. France's manufacturing index fell to 45.4 in Jun'24 from 46.4 in May'24. In Germany, overall PMI index dropped to 43.5 in Jun'24 from 45.4 May'24. In both cases, new orders, purchasing activity and output volumes were dented by weak demand. Germany's Ifo business climate index also reports similar trend. The headline index fell to 88.6 in Jun'24 from 89.3 in May'24, with current situation index remaining unchanged at 88.3 and expectations index dropping to 89 from 90.3 in May'24. Sector-wise, participants from manufacturing and trade sectors noted worsening expectations in the coming months. In the construction sector, participants were less pessimistic but muted orders remains a key problem. Only participants from services expect situation to improve in the coming months.

Trend of uneven recovery in China continues. On one hand, while the private survey of small and mid-size companies shows that manufacturing activity held ground in Jun'24 (Caixin PMI at 51.8 versus 51.7 in May'24), on the other hand, official survey (NBS) results for large state-owned manufacturing companies shows that activity remains in contraction with gauge unchanged at 49.5 in Jun'24. The difference in trends can be explained by better demand for consumer and export oriented goods, than for investment goods. Caixin survey mainly covers companies which are export oriented and consumer centric, while NBS survey covers companies in sectors like steel, cement, chemicals. These companies follow a trend visible in FAI growth. During Jan-May'24 period FAI slowed to 4% from 4.2% between Jan-Apr'24. Industrial production also missed expectations (6%), as it rose by 5.6% in May'24, slowing down from 6.7% growth in Apr'24. In contrast, retail sales got a boost due to holiday season and rose by 3.7% in May'24 (est.: 3%), up from 2.3% in Apr'24. Property sector continues to reel under pressure, as investment fell by (-) 10.1% during Jan-May'24 period, compared with (-) 9.8% decline between Jan-Apr'24. Thus there remains immense pressure on the government to announce stimulus measures to support growth.

RBI

MPC for the 8th consecutive time kept policy rates on hold, by keeping repo rate unchanged at 6.5%, SDF at 6.25% and MSF and bank rate at 6.75%. RBI also left its stance of “withdrawal of accommodation” unchanged. However these decisions were not unanimous, and were passed with the vote of 4-2, compared with a vote of 5-1 in Apr’24 policy. Dr Goyal joined Dr Varma in voting for 25bps cut and change in stance to neutral. However, Governor highlighted that interest rate transmissions are still not complete and inflation expectations still need to be anchored to targeted level. In this context, stance was left unchanged. RBI revised its GDP growth projections upward from 7% earlier to 7.2% now (closer to our estimates of 7.3-7.4%), supported by government capex, domestic consumption and corporate profits. Inflation projection was retained at 4.5% for FY25, awaiting more information on spatial distribution of rainfall in the coming months. We foresee no change in RBI’s position before Oct’24, that too if monsoon is normal and supportive of food inflation.

Global central bank decisions

US Fed kept its policy rates unchanged at 5.25-5.5% for the 7th consecutive time in Jun’24 meeting. However, slowing economic momentum along with PCE inflation cooling down, has raised hopes of a rate cut in Sep’24 (CME FedWatchTool is predicting ~60% chance of 25bps rate cut). Further, rise in continued jobless claims (currently highest since Dec’21) has also boosted prospects of a rate cut in Sep’24.

Bank of England (BoE) left its policy rate unchanged at 5.25%—at 16 year high, in its Jun’24 meet. The decision was not unanimous. 7 out of 9 members opted for a pause, while 2 members (Deputy Governor Dave and external member Dhingra) voted for a 25bps cut. This was despite inflation slipping to 2% mark in May’24 from 2.3% in Apr’24. Central Bank officials highlighted that they expect inflation go back up in H2CY24 (average at 2.5%) as effect of low energy prices fade. As a result, analysts are now pricing in a rate cut not before Sep’24 or Nov’24.

In line with expectations, **ECB** announced a 25bps rate cut in Jun’24, bringing down the policy rate to 3.75% now. This decision was driven sharp slowdown in inflation and economic activity. However, going forward, ECB President has signalled that the Central Bank will look at signals that inflation is firmly back in the targeted range before cutting any more rates. Currently, inflation in Eurozone is at 2.5% (Jun’24), compared with 2.6% in May’24. However, stickiness in core inflation (4.1% in Jun’24, unchanged from last month) is a cause of concern. Investors do not expect a cut before Sep’24, when ECB is also due to announce its revised projections.

BoJ in line with market expectation, kept its monetary policy rates unchanged in its Jun’24 meeting and reaffirmed that it will continue to maintain ultra-loose policy till inflation doesn’t rise to its targeted level on a durable basis. However, in the policy meeting at the end of this month, Central Bank is expected to announce plan for its ‘Quantitative Tightening’ program, by announcing ~\$100bn trim to its bond purchase program. Further, uncertainty still prevails around this timing of rate hike by the Central Bank, in the wake of weaker than expected GDP print for Q1CY24 and worsening economic outlook scenario for the services sector.

Special studies

Trends in remittance

Global picture of remittance inflows: Global remittance inflows have seen a steady increase in the last few years. From just US\$ 580.6bn in 2013, remittance inflows have risen to US\$ 857.3bn as per World Bank estimates. Country wise, India is the highest recipient of these inflows at US\$ 119.5bn in 2023, accounting for a share of 13.9% of total inflows. India's dominance in global remittance inflows can be gauged from the fact that inflows into Mexico, which is the second highest recipient of remittances, is almost half of the amount remitted into India. China received the third highest remittances in 2023 at US\$ 49.5bn, accounting for 5.8% of total global remittance inflows. Other South-Asian countries such as Pakistan and Bangladesh also feature in the list of the top 10 highest remittance receiving countries.

Remittance inflows into India: Remittance inflows into India have increased steadily over the years. In fact, India has retained its place at the top of the table with respect to remittance inflows in each of the last 10 years. From about US\$ 70bn in 2013, remittance inflows into India have increased to US\$ 119.5bn in 2023, at a CAGR of 5.5%. In comparison, global remittance inflows have increased by 4% in the same period. Within the top 10 remittance receiving countries, only Mexico registered a higher growth in remittances than India, at 10.7% in the last 10 years. On the other hand, there has been a decline of 1.8% in remittances to China. In fact, while Mexico ranked 5th amongst the top 10 in 2013, and gradually replaced China at the second place in 2023.

In terms of sources of remittance inflows, globally, the US is the largest source of remittance to the world and accounted for over 25% of total remittance inflows in the world in 2021. This was followed by the Gulf Cooperation Countries (GCC) which accounted for another 17%. Apart from these, Germany, the UK and Russia are also important contributor to global remittance flows.

For India, GCC countries accounted for over 40% of total remittance inflows in 2021, led by United Arab Emirates. USA with a share of close to 17% and UK with a share of 5% are other important contributors.

Further, results of RBI survey indicate that over 40% of remittances inflows into India in 2020-21 were for family maintenance, followed by deposits in banks which accounted for close to 35% of total inflows.

Outward remittances from India: There has also been a commensurate increase in India's outward remittance in the last 10 years. From just US\$ 1.1bn in FY14, remittance outflows increased to US\$ 31.7bn in FY24. This translates into a CAGR of over 40%, which is much higher than the CAGR of remittance inflows in the same period. Barring FY21, which was marked by the Covid-19 pandemic, remittance outflows from India have shown a clear upward trend.

Looking at the granular data, some interesting facts emerge. Over the last 10 years, there has been a significant change in the nature of outward remittances. Purpose wise, 'gifts' had the highest share in India's outward remittance in FY14, followed by 'others'. Maintenance of close relatives and investment in equity/debt were the other major heads. On the other hand, their share has declined significantly in subsequent years. Travel has emerged as the primary source of remittance outflow from India, accounting for 53.6% of total outflows in FY24

from just 1.5% share in FY14. An increase in disposable income and growth of aspirational middle class in the country, there has been an increase in foreign travel. This trend gained further traction after travel restrictions due to the Covid-19 pandemic were lifted. The share of maintenance of close relative has remained around 15% over the last 10 years. However, there has been a sharp decline in the share of gifts and education in this period.

Concluding remarks: Remittances play an important role in a country's balance of payment position. This is especially true for countries like India which consistently run a deficit on the current account due to an unfavorable trade balance position. In India, the current account deficit has averaged a little over 1% of GDP in the last 10 years, while the merchandise trade deficit has been much higher at over 6% of GDP. Support to the current account has stemmed from services and remittance receipts. At 3% of GDP in FY24, net remittances have helped ease the pressure on the current account and thus improve the country's external stability.

There has been a steady increase in both inward and outward remittance from India in the last decade. Inward remittance has benefitted from better growth outcomes in major source countries such as the US and GCC. At the same time, outward remittance from India have also shown traction, with most of it being directed toward travel and maintenance of close relatives. We expect this trend to continue.

Rise of an aspiring middle-class has ensured that discretionary spending of households has gone up, which is reflected in higher travel expenses to foreign countries. Global growth is expected to gradually improve, with USA expected to remain resilient. Labour markets in the USA, UK and Eurozone remain robust with unemployment rate near record lows. This bodes well for inward remittance. Further, while there seems to be some slowdown in remittance inflows from GCC countries, stable oil prices should help in reviving the inflows from the region. On balance, we expect net remittances into India to remain steady in FY25 and contribute positively to the current account balance which is expected in the range of 1-1.5% of GDP.

India's ongoing heatwave

Energy demand has increased sharply: Due to the severe heatwave in the country, power demand witnessed a sharp surge. There was a sharp pickup in electricity demand at 11.4% between Apr-Jun'24, compared with an increase of 1.1% in the same period last year. Region wise, electricity demand from the northern region rose steeply by 22.3% compared with a decline of 6.2% last year. Power demand in other regions also witnessed a significant uptick. In fact, barring the southern and north-eastern region, power demand in all other regions was higher compared to last year.

It must be noted that parts of northern and central India have been reeling under intense heatwave conditions. Both maximum and minimum temperature recorded in several parts of northern India remained 5-8°C and 4-7°C above normal temperature even in Jun'24.

Impact on production of certain items: Production of items such as ice cream, air conditioners and refrigerators has seen a pickup in Apr'24 due to the intense heatwave. Production of ice cream has jumped by over 26% in Apr'24, ACs by 16.2% and refrigerators by 2.7%. It is to be noted that production for these products was much lower last year in the same period as unseasonal rainfall in parts of the country had led to lower temperatures. It

must also be prudent to mention here that this is just preliminary data for Apr'24, and the full impact of heatwaves would be better reflected in production numbers for May-Jun'24.

Higher demand reflected in google trends: While we will have to wait for Q1FY25 interim results to assess the impact of heatwave on sales of related products, a few major players in the segment have signaled robust sales in Apr-Jun'24. Ice cream manufacturers are expecting sales to rise by over 40% in Q1, while demand for ACs is expected to increase by over 50-60% to touch a record high.

To assess this, we looked at the google trends data which helps to get an understanding of demand based on searches on the google search engine, on a real time basis. Based on popularity of searches, some interesting results emerge. The google trend for items such as battery-operated fans peaked towards end of May. For air coolers, the scale reached its peak towards end of Apr'24. For power inverter the scale peaked towards end of May'24. These trends though not conclusive, reflect that certain industries may witness transient momentum due to adverse weather conditions.

Do prices reflect any impact of heatwave?: With increased interest in these items, we next attempted to assess whether there has been an increase in the prices. For this, we studied the trend in inflation in some items of consumption and durable goods from the CPI basket. The caveat here is that supply side issues as well as input prices also have an impact on prices. However, for our analysis, we assume that the increase in prices is demand driven.

Among major FMCG items, cumulative inflation rate in items such as ice cream, fruit juices and shakes does not provide a conclusive picture. For ice cream, the inflation rate is impacted by an elevated base. However, the inflation in this category is still above 4%.

To better assess this, we used the seasonally adjusted series. For items such as ice cream generally the increased consumption during summer bumps up the prices. However, this year even adjusting for this seasonality, the sequential momentum is higher than last year, both in Apr'24 as well as May'24. A part of it can be attributed to rising milk prices, which in turn are impacted due to rising fodder prices on account of adverse weather conditions. Apart from ice cream, even the seasonally adjusted sequential momentum for fruit juices and shakes and refrigerators has seen a pickup, which was not visible in the cumulative data. However, prices of air conditioners/air coolers have shown momentum in terms of cumulative inflation, which is reflective of higher demand for these durable goods.

Heatwaves and vegetable price spiral: Vegetable price spiral is a seasonal thing during summer months, when harvesting period nears its end. However, this year particularly, the TOP items which are tomato, onion, potato (TOP) have exhibited significant volatility, and the steepening of its trajectory intensified during Apr-Jun period which coincided with heatwave alerts issued by IMD. Interestingly, arrival of TOP has been impacted which is also reflected in their rising Mandi prices. State wise arrival picture also corroborated with heatwave conditions. For example, States where heatwave conditions prevailed in pockets also witnessed sharp deceleration in arrival of these vegetables.

The arrival data shows that both in the harvesting period and during the period of Apr-Jun when heatwave conditions aggravated, the arrival quantity of TOP has been impacted, showing significant decline. The moderation in quantity was reflected in rising prices. For Potato and Onion, prices have risen considerably during Apr-Jun period by over 80%. For Potato most of the increase in prices was witnessed after the harvesting period when the arrival of fresh crops stopped.

State wise arrivals picture:

- For tomato, arrivals in States such as Karnataka, Andhra Pradesh and Gujarat, have fallen considerably. Other States such as MP and Odisha have also seen far lower arrivals during Apr-Jun'24 period compared to the same period of previous year. A part of it may be attributable to heatwaves or unseasonal rains.
- For Onion, arrivals in major producing states such as Madhya Pradesh have been disrupted due to heatwave conditions in some pockets of the region. For Karnataka and Maharashtra, unseasonal rains might have had an impact on arrivals.
- For potato, Uttar Pradesh, the largest potato producing State has noticed significant drop in production Apr-Jun'24 period. The northern-state has also experienced heatwave conditions during the same period.

Impact on Inflation: Heatwave in the country seems to be persisting longer than usual with IMD alerts for certain northern States and Eastern part of India still continuing. These are also the major TOP producing States. Further, harvesting period is also nearing its end, so there will be a lag in fresh arrivals. We expect pressure on headline CPI to continue and do not foresee food inflation to dip below 7.5-8% in the next two-three months. Thus, weather vagaries may lead to CPI overshooting RBI's projection both in Q1 as well as Q2FY25.

Impact on travel and tourism: With the ongoing heatwave conditions in the country, the travel and tourism industry too has been impacted. It must be mentioned here that due to the heat spell; travelers tend to prefer cooler destinations both domestically and abroad. The figure below shows that there has been a moderation in air passenger traffic for both domestic as well as international travel in FY25. However, it must be noted that there is a negative base effect as travel picked up sharply in the period after the pandemic amidst emergence of "revenge tourism". Also, there might be a decline in interest in travel to destinations which are reeling under the impact of the heatwave, which can also explain some part of the deceleration. On the other hand, there has been a surge in tourists in hill stations closer to metro cities such as Delhi. To gauge this, we have looked at the fuel consumption data. While there has been an increase in petrol consumption this year, diesel consumption has moderated. It must be mentioned here that this data is only indicative, and that it will also include essential travel for business etc.

Conclusion:

- Heatwave conditions continued in northern, central and eastern parts of India.
- Impact was visible in terms of lower arrivals of crops in states impacted by severe heatwave conditions.
- This is likely to keep food inflation elevated for longer.
- Transient bump in demand for products such as AC, air cooler, refrigerator will be visible, whose Q1 results is expected to reflect the same.
- Other sectors such as travel witnessed some lethargy due to conscious effort of staying indoors to avoid heat.

Corporate Investment in FY24

A subject that merits debate is corporate investment. It is generally argued that the government has been doing the heavy lifting when it comes to investment, which is mainly in infrastructure. Companies base their investment decisions on a variety of factors such as spare capacity, demand, existing capacity utilization rates, and cost of capital, among others. When the PLI scheme was announced there was a lot of enthusiasm by industry participants in terms of application for the same. Further, the new investment announcements made by companies in the last few quarters have been impressive. These reflect a lot investment intentions. How far have these materialized?

One way of getting a hold on actual investment undertaken by companies is to look at their balance sheets and analyse trends in GFA, i.e. gross fixed assets (including capital work in progress) over the last three years. The study here looks at a sample of 4,418 companies and analyses the progress made in terms of growth in GFA. The last three years are considered here; and hence starts from FY22, which was also a biased year as Covid-19 was rampant and came in the way of economic activity due to the lockdowns.

GFA of the sample companies increased by 4.8% in FY24 which is lower than 7.6% witnessed in FY23. In absolute terms GFA of these companies increased from Rs 37.33 lakh crore in FY22 to Rs 40.17 lakh crore in FY23 to Rs 42.09 lakh crore in FY24. The companies are clubbed under 38 industry groups. Interestingly as of FY24, crude oil and power sectors accounted for 40% of total assets of the sample companies. These 17 industries accounted for 92% of total assets. As can be seen in the Chart, besides crude oil and power, telecom, iron and steel, auto and banks are the main drivers of investment in physical assets. This is followed by construction materials, chemicals, FMCG, healthcare and non-ferrous metals.

Due to the peculiar nature of the last few years which overlap with the Covid-19 syndrome, we have grouped industries under 4 headings in terms of improvement in growth in assets in FY24.

- a) **Industries which have witnessed higher growth in Assets in FY24:** The industries in this group witnessed higher growth in GFA in FY24 relative to FY23 as well as higher growth than the sample average in FY24 which was 4.8%. The positive feature here is that investment is taking place in the capital goods segment as well as FMCG sector. Growth for the hospitality sector is also encouraging though a higher number would have been expected given the revival of pent-up demand in the last few years. But when data on investment announcements are looked at, there is a lot of interest for expansion here. Higher investment in mining can be linked to the coal sector which has also performed very well in terms of production growth in the last two years.
- b) **Industries which have maintained growth momentum of FY23:** In here, we looked at those companies that had more or less maintained growth of FY23. Here, the essential condition was that the growth in FY24 is close to 4.8%, while the secondary condition was that growth in FY24 was lower or at a similar level as in FY23.
- c) **Industries affected by high base effect of FY23 and shown slowdown in FY24:** The industries in this group are those that have witnessed lower growth in FY24 which was also associated with a high base effect. Here telecom, media and realty have witnessed sharp decline in growth in assets.
- d) **Industries that witnessed slowdown in growth in assets:** These are the clear laggards where limited investment has taken place. In this set of industries, the continued decline in assets for the power sector

is indicative of there being excess capacity with the generating firms which has obviated the need for fresh investment. This also falls in line with the observation that the thrust is more on renewable energy (which may have less representation in this sample). A similar trend is also seen for the IT sector where it appears that there is slower growth. In case of logistics, there is a recovery though it may be expected that there should be acceleration in future given the growth in the economy. The textiles and agriculture related sectors have witnessed slowdown in growth rate which may be attributed to lower demand conditions, especially on the exports side for the former.

In conclusion, it may be said that with 4 infra industries dominating 60% of total assets of the sample, a low performance by telecom and power has slowed down overall growth in FY24. On the positive side, 23 of the 27 industries have witnessed higher or stable growth. More importantly this growth pattern is randomly distributed across sectors which is comforting as it is not confined to just the infra based industries.

How have NRI deposits moved?

The movement of NRI deposits is interesting. During Covid-19 period, it has picked up sharply to US\$ 142bn from US\$ 131bn despite a softer interest rate regime globally. Bank deposits probably have been the preferred choice of savings during that uncertain environment where other asset classes exhibited considerable volatility. Apart from this, increase in precautionary savings globally (Gross savings rate to GDP of world rose to 27.1% from 25.8% in the same period, as per World Bank data), has also led to repatriation of savings in terms of bank deposits. However, with normalisation of economic activity, some correction was witnessed in NRI deposits in FY22 and FY23. Again, in FY24 (provisional figures), considerable momentum was visible. A possible explanation could be a more calibrated approach of domestic central bank compared to global central banks, where the rhetoric of interest rates has been far more volatile.

NRI deposits vis a vis aggregate deposits: NRI deposits in rupee terms have grown at a CAGR of 7.2% in the past 10-Year while aggregate deposits have grown at a much sharper pace of 10.2% during the same period supplemented by higher domestic resources. The rupee had depreciated by 3.2% during this period.

The last 5-Year CAGR of NRI deposits has been 6.6% while for deposits again it recorded a double-digit growth of 10.1%. Notably, Non-Resident Ordinary Rupee Accounts (NRO accounts) have grown at a far sharper pace. The 10-Year CAGR for the same stood at 15.2% higher than the 10-Year CAGR of aggregate deposits. There may be several reasons of the same ranging from ease of liquidity, interest rate differential and repatriation issues. On the other hand, Foreign Currency Non-Resident Accounts-FCNR(B) has witnessed volatility.

Thus, on account of faster pace of increase in aggregate deposits (as seen in the CAGR data as well), the shares of NRI deposits have flattened at 6.2%. However, with start of the rate cut cycle by Fed and hence a favourable interest rate differential for India, there is scope for the share to further increase.

How shares of different components of NRI deposits have evolved?: Some shift in shares is witnessed in the past few years. Share of NRO deposits has consistently risen, especially post Covid-19 period. NRO account basically handles domestic revenue. Thus, an insulated domestic economy compared to global counterparts in

terms of growth and policy dynamics could explain this rise. FCNR (B) deposits have picked up considerably since FY22. Higher remittance flows could be a possible explanation of the same. (Note: Here the higher share of FCNR (B) in NRI deposits seen during FY15 and FY16, is a one-off event, on account of Central Bank's measure to support domestic currency). However, the share of FCNR (B) deposits is still lower than seen during pre-Covid-19 period. NR(E)RA have exhibited some volatility. This is basically used by non-residents for transferring foreign profits to India. Muted growth in the global space, stickier inflation and an elevated borrowing cost might have impacted profitability of companies which is reflected in the falling share of these deposits.

NRI deposits are useful both from the point of view of augmenting aggregate deposits of banks as well as bringing in foreign exchange. The flow of funds will depend a lot on interest rate differentials and remittances into the country. Based on the trends witnessed in the last decade, a growth rate of 9-10% in NRI deposits could be expected in the next five years or so which will keep it aligned with growth in overall deposits which would be in the region of 12-13% and rupee depreciation of 2-3% per annum.

Trends in FDI

FDI has been a major support for India's capital account which in turn has steadied the balance of payments even under trying conditions. There has been a substantial increase in these flows over the years. They are determined by two sets of factors. The first is the quantum of investible funds where investors from different countries look at opportunities in different countries including emerging markets. The second is the business opportunity presented in countries in terms of scope for investment and doing business environment. Being the fastest growing economy, India has the scope; and an enabling environment has facilitated an increase in flows.

According to UNCTAD, in 2022 out of a total of \$ 1295 bn of FDI inflows, India ranked eight with a sum of \$ 49 bn. Countries ahead of India were Canada (\$ 53 bn), Australia (\$ 62 bn), Brazil (\$ 86 bn). The top four were USA (\$ 285 bn), China (\$ 189 bn), Singapore (\$141 bn) and Hong Kong (\$ 118 bn). Below India were Sweden, Mexico, France, Spain and Japan which had between \$ 30-45 bn. This gives an idea of the countries that India would be competing with when it comes to attracting such investment. For India, however, according to UNCTAD, FDI in 2022 was 5.1% of gross fixed capital formation, which shows less dependence on these flows with domestic resources dominating. This can be contrasted with almost 28% for Brazil and 16% for Australia. China had a similar ratio of 5.8%.

After peaking at nearly \$ 60 bn in FY21, there was a decline to \$ 44.4 bn in FY24. This slowdown can be explained by both the lower quantum of investable funds due to quantitative tightening pursued by the west post pandemic as well as more countries being open to such investment as part of the reconstruction process of their economies.

In this context it is interesting to see the sectors that have been attracting FDI and whether there is any pattern followed. We note the following trends:

- The share of manufacturing has shown a volatile trend. It was at 33% when FDI was at \$ 36 bn. However, subsequently there has been a decline. It rose again in FY22 to 27.7%, but has come down to 21% by FY24. Within manufacturing the leading sectors have been automobiles, drugs and pharmaceuticals, chemicals and metals.

- This also means that 70-80% of FDI has been going to the services sectors.
- Power has witnessed a continuous increase in share post pandemic to reach 12.4%.
- The IT sector showed a smart increasing trend till FY21 where share peaked at close to 40% (mainly due to single large deals), and then had tapered downwards to 11% by FY24.
- The financial services sector has also averaged around 11% for the 8-years period.
- The transport sector has witnessed increase in share in FY21 and then in FY24 which is mainly due to the airlines industry.
- The share of trade has been steady and averaged almost 10% with some high investment being witnessed in the e-commerce and retailing segments.

But the crux here is that there are fewer flows to the manufacturing sector relative to services.

Source-wise, Singapore, Mauritius and USA continue to be the three major sources of FDI for India accounting for around 55% of total in FY24. This share however has come down from over 60%. Netherlands has become progressively an important source with share of 11% in FY24. One of the factors making these countries popular pertain to tax laws which are more favourable.

There is evidently potential to increase the FDI flows in the next few years in a more diverse manner across sectors. Doing business conditions are important from the FDI perspective and efforts must be on even at the regional level to attract FDI. For the period 2000-2024, five states have accounted for 87% of total FDI. Maharashtra leads with 30% followed by Karnataka with 22%. The next three are Gujarat, Delhi and Tamil Nadu. Signing more FTAs which include investment terms would be an aggressive way of enhancing these inflows on a bilateral basis.

Corporate performance: Q4-FY24

Financial performance of India Inc. continued to be marked by a moderation in sales growth, even as profit growth picked up when compared with last year. Banks and the auto sector remained the outperformers and contributed to most of the growth in both sales and profits. This was similar to the trend witnessed in the last 3 quarters of the year. FMCG sector still awaits a meaningful recovery in demand, with many companies resorting to a volume-led approach by undertaking price cuts.

Financial performance of corporates in Q4 FY24: Financial performance of 2537 companies suggests that Q4-FY24 was marked by a slowdown in net sales, even as profit growth exhibited an uptick on a YoY basis. Sales growth moderated from 10.2% in Q4 FY23 to 7.8% in Q4 FY24. Expenditure growth remained stable at 7.5%. This was also reflected in a significant improvement in profitability. All major profit indicators witnessed an improvement led by lower input prices as global commodity prices were elevated in Q4 FY23.

There was improvement in sales growth on a sequential basis. On the other hand, profit growth saw a marked slowdown as commodity prices stabilized and as such the tailwinds from the correction in global commodity prices have largely been utilized. For a comprehensive analysis of financial performance of India Inc in Q3 FY24, please refer to our earlier report.

To get a better picture of the financial performance of India Inc. it is essential to analyze the sample after excluding the BFSI sector, which tends to lend a considerable degree of bias to the total picture as banks have been riding on a sustained business upcycle amidst buoyant credit growth in the economy.

Sales growth for the non-BFSI sector is much more somber at just 4.4% compared with 8.3% in the last quarter of FY23. Lower growth in expenditure and interest costs have contributed positively to profit growth. It must however be noted that the growth in profits for the non-BFSI sector is lower than the overall growth in profits.

Aided by both lower interest costs as well as an improvement in profitability, the interest coverage ratio (ICR) of the companies has shown an improvement. It must be noted that the ICR indicates the debt servicing capability of a company as it shows whether the company is making enough profits to meet its interest liabilities. The ICR is calculated as a ratio of profit before interest and tax (PBIT) and the interest cost. In Q4FY24, the ICR has increased to 5.89 from 5.5 in Q4 FY23. The improvement in ICR must be viewed against the backdrop of higher interest rates and muted sales growth.

Sector-wise movement in interest cover: There are marked differences between sectors with respect to interest cover ratio which can be seen in Table 3. Despite an increase in weighted average lending rates (WALR) by banks in Q4 FY24, most sectors have seen an improvement in ICR compared with Q4 FY23. This is because a large part of the increase in interest costs has been offset by an improvement in profit growth. Sector wise ICR shows the following important facts:

- Out of a total of 33 sectors, only 12 witnessed a moderation in ICR in Q4 FY24 compared with the same period last year.
- There is an improvement in ICR for the top 3 highly indebted sectors, namely power, telecom and crude oil. It must be mentioned here that the ICR for the telecom sector at 0.71, is less than ideal. The sector continues to see high debt levels due to several factors such as AGR dues and spectrum auction as well as high capex requirements, thus contributing to a much higher interest rate burden. For both crude oil and power, while there has been an improvement in ICR in Q4 FY24, it still trails behind Q4 FY23.
- Sectors which saw the maximum improvement in ICR vis-à-vis Q4 FY23 are healthcare, gas transmission, industrial gases and fuels and automobiles and ancillaries.
- On the other hand, sectors which saw a significant deterioration in ICR include Non-ferrous metals, FMCG, paper and electricals.

It is interesting to note that while the ICR has shown an improvement vis-à-vis last year, it is still lower than Q4 FY22. This is because interest rates were significantly lower in FY22 as the repo rate was reduced to just 4% to stimulate growth. With a subsequent increase in interest rates, the ICR too inched up but is now showing signs of improvement, led by an uptick in corporate profitability. In this context, it is important to note that the RBI has kept the repo rate unchanged at 6.5% since Feb'23.

With RBI likely to wait until it gets more clarity on the progress of monsoon, we do not anticipate a rate cut before Oct'24. Further, with transmission of earlier repo rates majorly completed, the interest costs for India Inc. are likely to remain stable in H1FY25. Hence, corporate profits will be the most significant driver of debt serviceability going. Companies might face headwinds on this front as the benefits from lower input prices have largely been utilized

leading to a negative base effect. This is already manifesting in higher WPI inflation in recent months. Hence, we may see some moderation in ICR going forward. On the positive side, the corporate sector has been diversifying its debt portfolio through alternate channels such as corporate bonds and external commercial borrowings (ECBs) etc. based on relative cost advantage, which might keep interest costs contained to an extent.

Sector-wise performance

In terms of sector-wise performance, out of the 33 sectors, 17 recorded sales growth higher than the aggregate level of 7.8%. Further, while on an aggregate basis there has been a slowdown in sales growth, a total of 17 sectors have witnessed an improvement in Q4 FY24. These include consumer durables, insurance, textiles and plastic products amongst others.

For net profits, a total of 16 sectors showed higher growth than the average of 17.1%. In comparison to last year, 22 sectors show higher growth than Q4-FY23.

Looking at growth in sales and net profits of various sectors in Q4-FY24 on a YoY basis, divided into different ranges, the following points stand out:

- The performance of the chemicals sector was weak on both sales as well as profit parameters. However, even within chemicals there was a mixed performance.
- Similarly, even the iron and steel industry witnessed a decline in both sales and PAT. Sales growth was dampened by imports as well as destocking ahead of elections. On the other hand, profit growth was impacted by higher prices of key inputs such as coking coal and iron ore.
- There was moderation in sales for the crude oil sector. PAT was severely impacted due to a decline in gross refining margins as well as a reduction in fuel prices announced by the government in Mar'24.
- The performance was FMCG sector less than satisfactory as sales continued to remain muted, while PAT growth turned negative. Urban and premium focused products continued to drive demand.
- For Indian IT companies, performance in Q4 remained almost steady. Demand continued to remain weak even as major players announced an uptick in new deals. Discretionary demand conditions remained constrained amidst a continued focus on cost efficiency.
- The real estate sector continued to witness an upswing with major market players reporting a strong interest among homebuyers. There was some moderation in sales growth due to base effect but the outlook for the sector is positive, led by expectations of a rate cut and the emergence of a growing middle-income class.
- For the cement sector, sales growth showed moderation due to base effect. Demand during the quarter was strong, led by front loading of government expenditure ahead of elections as well as continued demand from the real estate sector.
- Hospitality segment continued to witness a strong demand momentum, major companies remained upbeat on the outlook of the sector.
- After remaining an underperformer for the last few quarters, the textiles sector exhibited signs of a recovery in Q4 FY24. Despite weak external demand, sales growth picked up led by increased demand for home textiles.

- The consumer durables industry benefitted from the earlier than expected onset of summer and extreme heatwaves in some parts of the country, especially the southern parts. There was increased demand from households for cooling products.
- The performance of the auto sector remained impressive, despite a negative base effect. Sales growth continued to be in double digits led by sustained demand momentum, particularly in the passenger vehicle (PV) segment.
- However, demand for tractors was downbeat due mainly to an erratic monsoon and lower reservoir levels which had a negative impact on sowing and output.
- The capital goods sector and infrastructure related industries replicated their strong performance even in Q4 FY24 with both sales and profit growth posting double-digit growth.
- The diamonds and jewellery sector saw a steady growth in sales despite higher gold prices as companies resorted to new products and offers to attract customers. PAT saw a moderate dip due to higher prices of gold.
- For the pharmaceuticals sector, there was significant improvement in both sales and PAT. Improvement in demand, both domestic and external, especially in the US, led to better volume growth. On the other hand, soft input prices as well as price hikes translated into better profit growth.
- The performance of banks continued to be impressive. The quarter was marked by healthy growth in business and stable asset quality. Credit growth continued to be driven by retail. Deposit growth also picked up pace.
- Retailing sector performed reasonably well on both the sales and PAT matrix led by improved demand led by new product launches and increased penetration into newer markets.

Concluding remarks: Corporate performance of India Inc. in Q4FY24 was marked by an improvement in profits matrix, even as sales growth was largely muted on a YoY basis. Banks and financial companies as well as the auto sector continued to outperform and did most of the heavy lifting. On the other hand, FMCG companies continued to report a dismal performance with the rural demand picture still fuzzy. Capex announcements by companies have shown a pickup which should be positive for growth. However, our analysis shows that there are only a few industries which are investing, suggesting that the investment picture remains lop-sided. Further, companies are increasingly looking at alternate sources of funds with both corporate bonds issuances and ECBs approvals surging in FY24.

The outlook is heavily contingent on the monsoon trajectory, with both timing and distribution of rainfall likely to play an important part in the revival of the FMCG sector. Export oriented sectors also await a recovery in demand, even as some pockets such as textiles witnessing early green shoots. IT sector growth is also impaired muted discretionary demand, which is expected to see a revival in FY25.

Overall, we believe that the corporate sector is likely to see a more volume-led growth in FY25. Headwinds are likely to emerge in FY25 with the positive base effect from lower commodity prices waning. This may impact profitability going ahead.

Data Releases

Currency outlook

INR appreciated marginally in Jun'24, after touching a fresh record-low during the month. In H1 2024, INR has depreciated by 0.2%, even as the dollar strengthened by over 4.5%. RBI's effective management as well as India's strong macro fundamentals have underlined the strength in the domestic currency. The trajectory of INR will be determined by the movement in dollar. While US inflation and growth is showing signs of a moderation, the possibility of monetary easing will face hurdles due to the evolving political landscape in the country. As of now, a rate cut is priced in for Sep'24, however, the path forward will be contingent on the election results in Nov'24. Till then, we can expect some volatility in the global markets and DXY. This will also have an impact on INR. On the positive side, domestic conditions have remained more or less the same for INR and suggest an appreciating bias for the currency. We expect INR to trade in the range of 83.25-83.75/\$.

Bond Market Round-up

Global yields continued their downward trajectory. US 10Y yield declined as renewed bets of rate cut by Fed resurfaced. This was attributable to softer PCE price index which came in line with expectations. With the cooling off price pressure, the rate cut is expected by the market to begin as early as Sep'24. ECB on the other hand, has already begun the rate cut cycle and is expected to trim rates further as they deem it reasonable which could bring the borrowing cost lower. On the domestic front, India's 10Y yield inched up. Going forward, it is expected to trade in the range of 6.95%-7.05% in Jul'24, with risk evenly balanced. The inclusion in the global bond yield index and the expectation of fiscally prudent Budget remains a key positive for the government bonds.

Core sector growth

Core sector growth for May'24 came in at a steady 6.3% as against 5.2% last year. The base effect did provide a prop to segments which did well. Power sector growth of 12.8% was mainly due to the heatwave which led to higher demand. Higher power generation also led to higher growth in mining as coal production increased. Steel growth at 7.6% was propped up by both government spending as well as auto sectors. Cement production fell by -0.8% due to strong double digit base effect of last year. A slowdown in apex in May of government affected some projects involving cement. Fertilizers production was down by 1.7% which can be attributed more to adequate stocks for sale during Kharif season. Crude oil and refinery products witnessed low and negative growth mainly due to lower demand for diesel.

Fiscal update

The fiscal deficit for the first two months came in at just 3% of the budgeted amount compared with 11.8% last year. For these two months the growth in tax and non-tax revenue was very buoyant and while the revenue expenditure was on par with last year, there was some slowdown in capex at 12.9% of target as against 16.8% which helped to compress the fiscal deficit. The higher RBI transfer was also useful in increasing overall revenue.

WPI inflation accelerating

Headline WPI inflation inched up to 2.6% in May'24 from 1.3% in Apr'24, marginally lower than our estimate of a 2.7% increase. The increase was driven by higher **food inflation** which accelerated to a 10-month high of 7.2% compared with 5% in Apr'24. Vegetable inflation picked up to 32.4% versus 23.6% in Apr'24. It must be noted that vegetable inflation has continued to grow in double-digits since the last 7-months. Within vegetables, prices of tomato showed a significant uptick and increased by 64.5% in May'24 versus 40.6% in Apr'24. On the other hand, despite some moderation, inflation in potato and onion remained elevated at 32.4% and 64.1% respectively in May'24.

Fuel and power inflation decelerated to 1.3% in May'24 from 1.4% in Apr'24, led by a contraction in electricity price index. After increasing by 6.3% in Apr'24, index for electricity prices declined by 0.4% in Apr'24. However, other categories within the fuel and power index showed acceleration. Coal inflation accelerated to 1.2% in May'24 versus 0.2% in Apr'24. Notably, global coal prices have inched up in recent months amidst an increase in demand. Mineral oil index marked its first increase in 14- months and rose by 2% in May'24, after declining by 0.2% in Apr'24.

Core inflation snapped a 14-month deflation streak and increased by 0.4% in May'24 after declining by 0.7% in Apr'24. Deflation in manufactured products also ended in May'24 as the index inched up by 0.8% after contracting by 0.4% in Apr'24. Out of the 22 sub-indices, acceleration was visible in 17 categories. Within this, categories such as basic metals, food, paper and paper products and textiles witnessed maximum acceleration.

CPI inflation

CPI inflation came in at 4.75% in May'24, on YoY basis, marginally lower than our estimate of 4.9%. Food inflation remained sticky at 8.7% in May'24. Within food, 6 out of 12 broad categories have remained above 6%, with inflation remaining elevated for vegetables (27.3%, YoY), pulses (17.1%), cereals (8.7%) and eggs (7.6%). Considerable upside pressure was also visible in the case of oils and fats and fruits. The sequential picture gives a better picture of the evolution of food inflation. Food inflation has risen by 0.7% in May'24 (MoM). On a seasonally adjusted basis, however, food inflation fell by 0.3%, so some of the upside rise was attributable to seasonal phenomenon.

Core CPI (excl. food and fuel) softened to 3.1%, on YoY basis. Apart from personal care and effects, sub-categories of core showed moderation across the board. The sharpest pace of moderation was visible for household goods and services. Sequentially, the fall in core was led by housing (seasonal phenomenon), personal care and effects (due to moderation in gold prices), household goods and services and clothing and footwear. Demand conditions are still patchy, so core is likely to be range bound between 3.5-4% in the near term.

Growth in Industrial Production

IIP growth moderated to 5% in Apr'24 compared with a growth of 5.4% in Mar'24 (revised). This was marginally lower than our estimate of 5.5%. The slowdown was led by manufacturing output which decelerated to 3-month low of 3.9% in Apr'24 from 5.8% in Mar'24. On the other hand, both mining and electricity output witnessed an improvement in Apr'24. Mining output rose by 6.7% compared with a growth of 1.3% in Mar'24. Electricity output clocked double digit growth of 10.2% from 8.6% in Mar'24, on account of higher seasonal demand.

Within use-based, output of primary goods improved to 5-month high to 7% in Apr'24 from 3% in Mar'24. Output of infra and construction goods recorded a much higher growth of 8% in Apr'24 (7.4% in Mar'24). Consumer durables output also inched up further to 9.8% in Apr'24, supported by base effect. However, output of intermediate goods witnessed slowdown, falling to 1- year low of 3.2% in Apr'24 from 5.5% in Mar'24. Even capital goods output registered deceleration at 3.1% against a growth of 6.6% in Mar'24. FMCG output registered a contraction at (-) 2.4% after increasing by 5.3% in Mar'24.

Way forward: India's growth has remained stable. Recently, World Bank has also revised the growth forecast for the country upwards on the back of sustained domestic demand, buoyant services sector and improvement in investment. We expect the economy to fare better than its global counterparts aided by rebound in agriculture sector, given the expectation of above normal monsoon, pick up in investment activity with thrust on capex and policy continuity, overall. The focus will now shift towards budget.

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