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ECONOMY & GILT WATCH

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FY 2023-24 GDP FAE
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FY 2023-24 GDP FAE: Growth on Upswing

The first advance estimates (FAE) of GDP for FY 2023-24 foretell a rather robust show by the economy, with real GDP expected to grow by 7.3 per cent. This is above RBI's real GDP growth projection of 7 per cent for the financial year. The real GVA is projected to grow at 6.9 per cent y-o-y with manufacturing and services sector being the key growth boosters, while agriculture growth is projected at a tepid 1.8 per cent. Nominal GDP on the other hand, has been projected to grow by 8.9 per cent during the year compared with 16.1 per cent in FY 2022-23, with an implied deflator of 1.4 per cent. A lower nominal GDP growth is a bit concerning given that the estimate will be used for arriving at the current year's revised estimate of fiscal deficit to GDP ratio and will also form the base for next year's nominal GDP to be presented in the upcoming Union Budget for FY 2024-25. From monetary policy perspective, a robust real GDP growth of 7.3 per cent is likely to keep rate cut hopes rather modest, with a delayed and shallow rate cut cycle looking more probable given the underlying strength in the economy.

Implied H2 Growth Trajectory

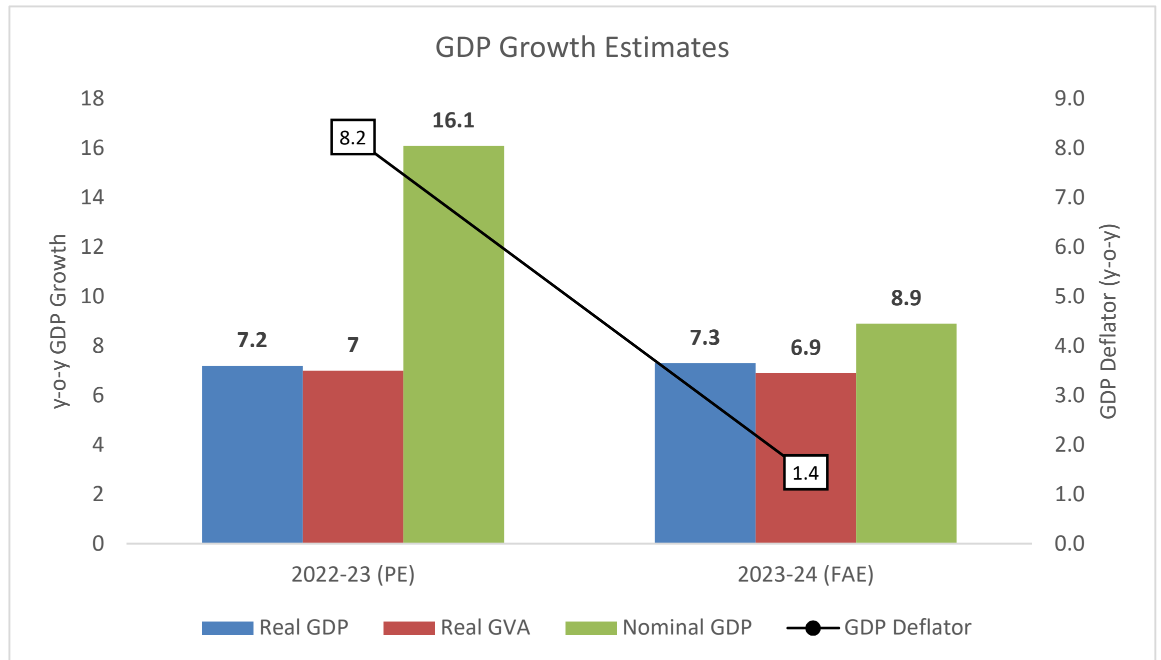
With the H1 GDP numbers already out, the implied real GDP growth for H2 based on full year FAE stands at 7 per cent, as against 7.7 per cent clocked in H1 of FY 2023-24. Sector wise expectations portend further deceleration in agriculture sector growth (~1.4 per cent in H2). This aligns with the lower than expected kharif harvest and slightly sluggish rabi crop sowing in the current season. As per the data available for week ended 5th Jan 2024, key rabi crop sowing is ~1.2 per cent lower than previous year's sowing level, with pulses sowing being significantly lower than previous year's levels. Manufacturing sector activity, which saw a spurt in Q2 of the current year, is expected to moderate in H2, with y-o-y growth projected at 3.9 per cent compared with 9.3 per cent in H1. The moderation in manufacturing sector is expected to be partially offset by higher growth in mining and electricity sector. However, given the larger contribution of manufacturing in overall GDP, the industrial sector growth is expected to be lower at 5 per cent in H2 as against 8.8 per cent in H1 of FY 2023-24. Services sector growth is projected to be mostly flat at 8 per cent in H2 as against 8.3 per cent in H1.

Services sector is projected to lead the economic growth H2, offsetting the moderation in agriculture and manufacturing sector activity

Largely, services sector is projected to lead the economic growth in the second half of the year, offsetting the moderation in agriculture and manufacturing sector activity. The optimism over services sector may have to be seen with some caution, as there may be some pull back in demand for services and tapering of construction activity in the second half of the year. On expenditure wise basis, capital formation (GFCF) is expected to grow at a brisk pace of 11 per cent in H2 as against 9.5 per cent in H1, leading overall economic growth. GFCE and PFCE are expected to moderate in H2, expected to grow at 3.1 per cent (5.1 per cent in H1) y-o-y and 4.4 per cent (4.5 per cent in H1) respectively.

Sharp decline in Deflator

The sharp decline in nominal growth in FY 2023-24 to 8.9 per cent as against 16.1 per cent in previous year is mainly attributed to a low deflator of 1.4 per cent for FY 2023-24 vis-à-vis 8.2 per cent for FY 2022-23. This is in line with average WPI inflation of -1.3 per cent in FY 2023-24 vis-à-vis average WPI of 9.6 per cent in FY 2022-23.



Outlook: The robust FY 2023-24 FAE of GDP growth at 7.3 per cent may be posed with some downside risks emanating from expected moderation in government expenditure ahead of general elections, tapering of global demand and subdued agriculture sector activity as well as continued softness in private consumption. Nonetheless, a robust growth trajectory is expected to keep the domestic rate cut cycle rather contained, unless new risks to growth re appear.

Macro Monitor

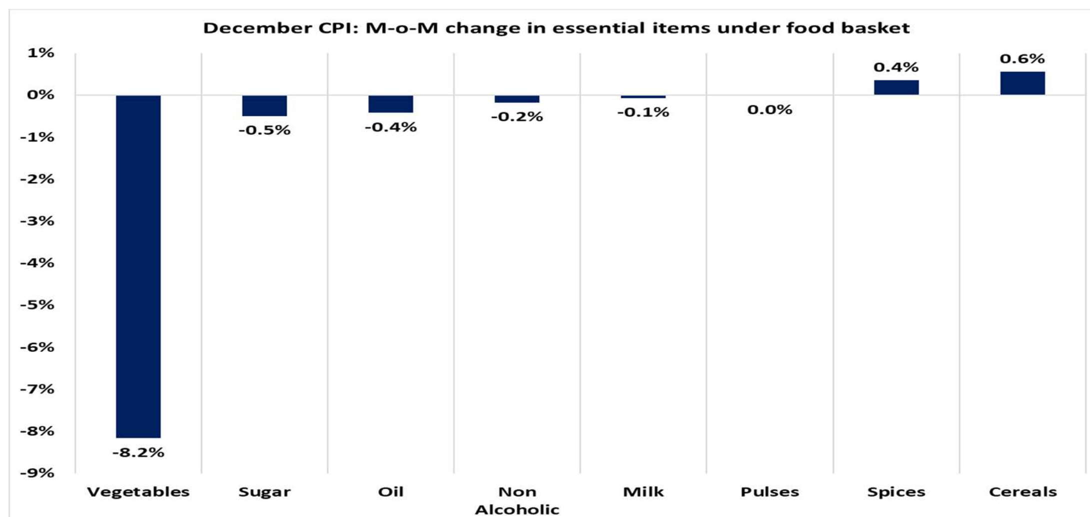
December CPI preview: Inflation is expected to surge

Despite some major vegetable price corrections witnessed during the past month, the headline inflation is expected to soar further for the month of December 2023, primarily on the back of a low base effect. The skyrocketing onion prices made headlines during the month of November 2023, followed by a surge in prices of tomatoes and garlic. Other subgroups including fruits, spices, cereals and pulses also jumped on the wagon and pulled the inflation print on the higher side to 5.55 per cent.

During December, the spiked vegetable prices underwent some corrections, in addition to moderating prices of oil and fruits. However, the spices and cereals category continued on the track of sequential price elevation, with pulses prices expected to stay flat this month. Eggs are also expected to record a single-digit inflation during the month owing to an increased winter demand amid production shortfall. Price movement in other groups including Clothing and Footwear, Fuel and Light and Miscellaneous category also witnessed an uptrend. While the yellow metal started the month on subdued levels, it eked out towards the end of the month following an indication of rate cuts in the next year by the US Federal Reserve.

We expect the December 2023 headline inflation to edge up to ~5.83 per cent and stay within the MPC's projection of 5.6 per cent for the third quarter

Basing the above analysis, we expect the December 2023 headline inflation to edge up to ~5.83 per cent and stay within the MPC's projection of 5.6 per cent for the third quarter. Further, we do not expect upside risks to the forth coming CPI prints as the base effect will turn favourable from January onwards, also continued arrival of winter supplies will keep the vegetable prices under check.



Source: Dept. of Consumer Affairs

Fixed Income Outlook

Fundamental View

The term structure witnessed steepening during the previous fortnight, with short term yields cooling off as rate cut expectations continued to keep sentiments supported, however longer end of the curve witnessed firming on supply concerns as SDL borrowing calendar surprised on the upside. The news of inclusion of Bloomberg Index Services proposing to include eligible Indian bonds in its emerging market local currency index from September 2024, bought some cheer to the market. After hovering close to 7.25 per cent mark in the new calendar year, the 10-yr yield softened to fall below 7.20 per cent as of today's closing. In the current fortnight, market will keenly watch for US CPI and domestic CPI inflation prints for the month of December. The US CPI is expected to be a key driver especially after US non-farm pay roll exhibited resilience in December beating market expectations, which may jeopardise expectations of an early Fed pivot. On the domestic front, the Indian CPI is expected to peak out in December remain within the RBI's tolerance band going into the next quarter. Given the above, we expect bond yields to trade range bound with a softening bias riding on optimism over another index inclusion.

US and domestic CPI prints for December will be keenly watched in the current fortnight

SDL Outlook

During the last fortnight, 10 Yr. State Loans traded in the broad range of 7.550%-7.770%, whereas the 10 Yr. CG benchmark, remained in the range of 7.168%-7.238%. The spread between yields on the 10-year state bonds and the benchmark 10-year widened to a two-year-high amid concerns of higher supply of state bonds during the last quarter of the current financial year. The last time the yield spread widened above 50 bps was in Jan 2022.

The states plan to borrow Rs 4.13 lakh cr vs market expectations of Rs 3.5 lakh cr in the fourth quarter of fiscal 2023-2024. We expect the yield spread between the 10-year state governments' loans and the benchmark 10-year G-sec to widen further and trade in the range of 55-60 bps in the coming weeks, and most movement will depend on the actual issuance.

Going forward, we may see 10 yr to trade in the range of 7.16%-7.23%. However, any sustainability below 7.16% will open the gate for 7.08%-7.04% levels.

Technical View

Technical Synopsis 7.18% GS 2033 Yield:

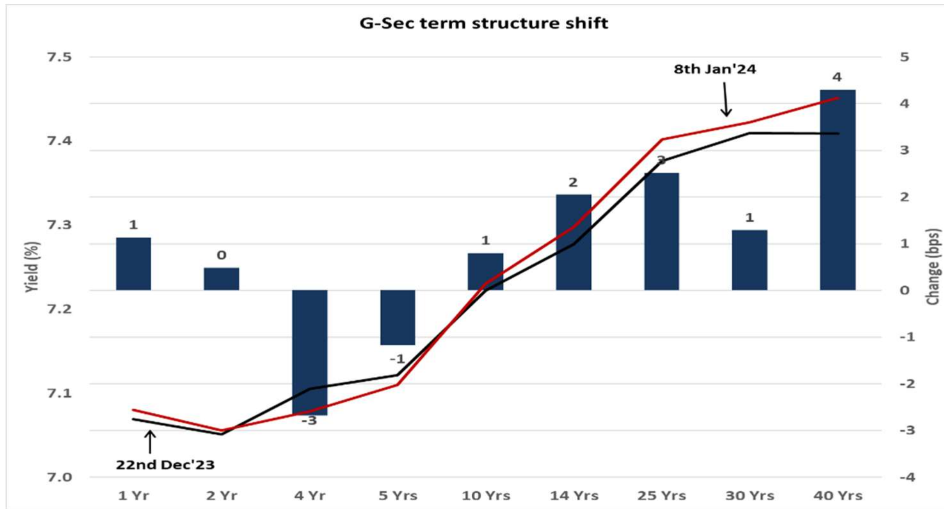
7.18% G Sec 2033 paper settled at 7.1884% on Tuesday's session. Passing fortnight Benchmark traded between 7.24%-7.15% zone and settled in the middle of the range.

Momentum oscillator RSI is hovering around 45 level. We are witnessing a Symmetrical triangle formation in 10yr, with falling upper trend line indicating stiff resistance around 7.23% level and on lower side rising trend line hinting 7.16% to act as crucial support for coming fortnight. Going forward, we may see 10 yr to trade in the mentioned range of 7.16%-7.23%. However, any sustainability below 7.16% will open the gate for 7.08%-7.04% levels.

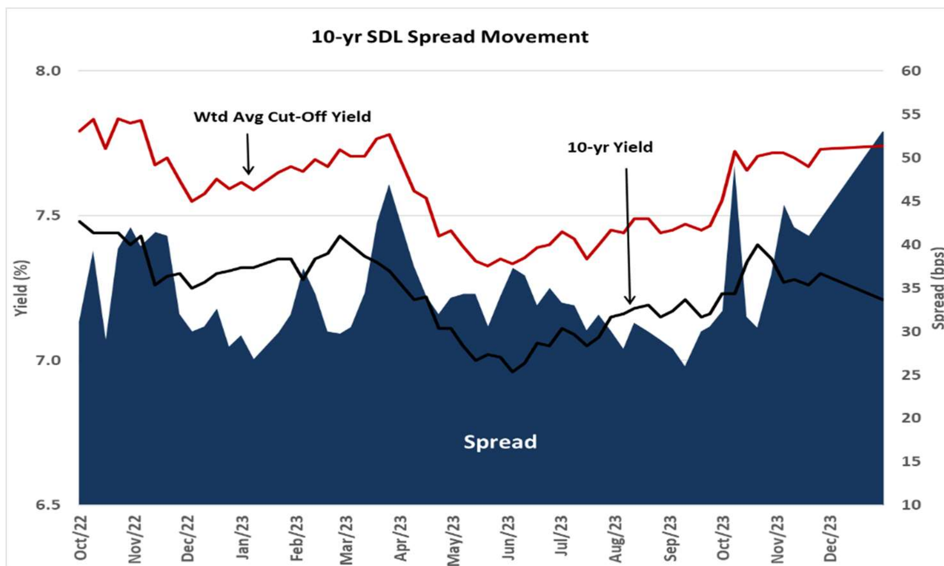
Running Chart GOI 10yr Daily.

Source: Cogencis

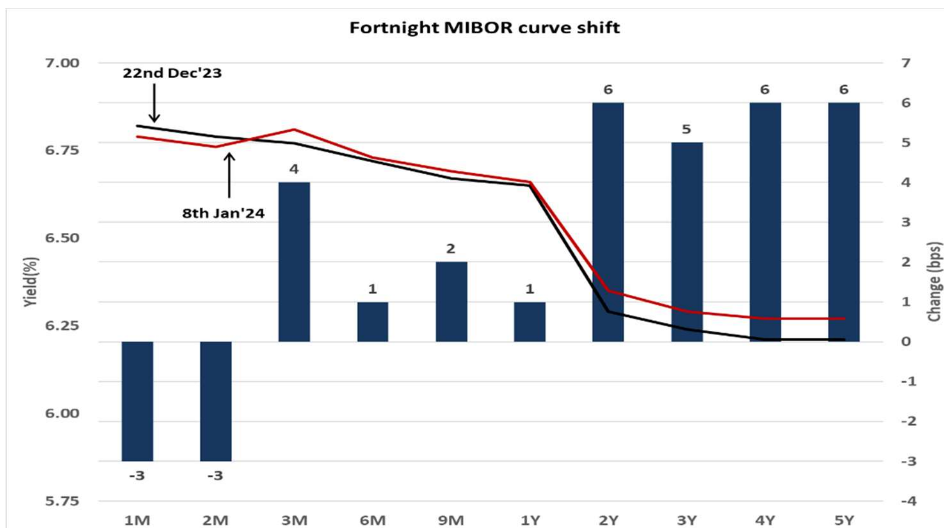
In Graphs



G-sec term structure steepened during the fortnight



The spread between 10 Yr SGS and CG is expected to widen further and trade in the range of 55-60 bps in the coming weeks



Overnight indexed swap rates firmed up due to rise in US yields

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