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Economic Recovery is Gaining Pace

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Chief Economic Adviser's Views

Economic Recovery and Growth Acceleration: Searching for Fiscal Space

At last, there is some encouraging news on the economic front. Although the credit rating and multilateral lending agencies have been revising the growth rate downwards and inflation continues to rage above the upper tolerance limit, some high-frequency economic indicators are showing signs of continued recovery. Of course, it is still unclear whether this recovery will sustain, but it provides an encouraging possibility. Equally important is the fact that the fiscal implementation in the first half of the year has not been a matter of concern, but there could be challenges in ensuring adequate fiscal space to assist continued recovery while containing the deficits and debt at the budgeted level. It is important to take note of the challenges and ensure adequate fiscal space for continued recovery.

The recent high-frequency indicators show that the economy is on a recovery path, though it remains to be seen whether it will be sustained. The core sector growth, after slowing to 3.3% in August, recovered to a three-month high of 7.9% in September and the growth was particularly impressive in coal (12.1%), cement (12.1%), electricity (11%), and fertilizer (11.8%) sectors. The manufacturing PMI increased to 55.3 in October as against 55.1 in the previous month and the services PMI increased to 55.1 in October from 54.3 in the previous month. The GST collection in October was the second highest in the year at Rs. 1.51 trillion (in April it was Rs. 1.67 trillion). More importantly, the RBI data shows that the bank credit growth has risen to 17.94% in early October, as compared to 6.5% last year and corporate lending increased by 12.6% and lending to SMEs increased by 27%. The passenger car sales in October 2022 at 3.36 lakhs were 29% higher than October last year. These clearly point out some green shoots, but how they can be nursed to take deeper roots to achieve sustained recovery remains to be seen.

Despite these developments, there are areas of concern that need to be addressed to sustain the recovery process. The impact of the Russia -Ukraine conflict and the accompanying sanctions have continued to keep commodity prices, particularly in crude oil, at elevated levels. The persisting lockdown in China has continued to disrupt supply chains. The resulting high inflationary conditions in developed western economies have led to sharp increases in interest rates, particularly in the US, UK, and the Euro area. This has created instability in international financial markets and forced capital flows out of emerging markets, putting pressure on their exchange rates. With the US raising interest rates six times this year and four times in a row by 75 basis points and the UK and the Eurozone having similar increases and indicating further increases, India will have to continue with the cycle of rate increases. Although the economy has recovered to the pre-pandemic level and is projected to grow at 6.5 to 7% in the current year, inflation and high interest rates are likely to dampen the animal spirits, and maintaining high growth next year will require significant policy interventions. There is very little space for the monetary policy committee to keep up the growth momentum and the job of the heavy lifting falls mainly on fiscal policy. The high level of fiscal deficit and debt in the country has very little space for using fiscal space to boost the private investment cycle, and the country is faced with the challenge of expanding public sector investment while continuing the plan of fiscal consolidation.

The fiscal development in the first half of the current fiscal (H1FY23) for the central government shows a mixed picture. The actual fiscal deficit in H1FY23 is 37% of the budget estimate as compared to 35% H1FY22. Note that the budget this year has placed heavy emphasis on capital expenditure, and it is budgeted to increase by 24.5% of the revised estimate of last year. In H1FY23, the implementation capital spending works out to 45.7% as compared to 41.4% in H1FY22. It remains to be seen whether the government will be able to maintain the tempo of increasing capital expenditure in H2FY23.

The ability to maintain the tempo depends on the progress in containing the revenue deficit at the budgeted level. The government has stated that it will borrow about Rs. 100 billion less than the budgeted amount and still hopes to contain the fiscal deficit at the budgeted level of 6.4% of GDP. The overall tax revenue collection has been healthy so far and in spite of the cuts in excise and customs duties on petroleum products and edible oil to rein in the prices, the aggregate tax revenue is expected to be higher by about Rs. two trillion. However, there would be a significant shortfall in non-tax revenues and disinvestment receipts. The dividend from the RBI could be significantly lower than the budgeted, and there has not been much progress in disinvestment even as the budget estimate at Rs. 65000 crore is substantially lower than that of last year. Besides, additional subsidy bills on food and fertilizers and outgo in terms of dearness allowance payments could run into Rs. 2.5 trillion. Unless substantial pruning is done on other items of revenue expenditure, the revenue deficit may overshoot the budgeted sum and that could mean the axe may fall on capital expenditure if the estimated fiscal deficit has to be complied with. Thus, arresting the slowdown in the economy in the wake of international slowdown poses hard choices and these challenges have to be met effectively if the slowdown has to be avoided.

Annexure: Select Macro Economic and Sectoral Indicators

Indicators/Sectors		FY21	FY22	Sep-21	Oct-21	Nov-21	Dec-21	Jan-22	Feb-22	Mar-22	Apr-22	May-22	Jun-22	Jul-22	Aug-22	Sep-22	Oct-22
Economy				FY22Q1		FY22 Q3			FY22 Q4			FY23Q1			FY23Q2*		
GDP at 2011-12 Prices	Y-o-Y in %	**-6.60**	**8.68**	8.40		5.40			4.09			13.51			6.17		-
GVA at 2011-12 Prices	Y-o-Y in %	**-4.80**	**8.11**	8.30		4.71			3.89			12.75			5.77		-
Agriculture	Y-o-Y in %	**3.32**	**3.01**	3.16		2.54			4.13			4.46			2.50		-
Industry	Y-o-Y in %	**-3.26**	**10.27**	6.96		0.35			1.25			8.56			5.27		-
Services	Y-o-Y in %	**-7.82**	**8.44**	10.21		8.10			5.49			17.65			6.74		-
Banking																	
Gross Bank Credit	Y-o-Y in %	**5.00**	**9.60**	6.70	6.80	7.00	9.20	8.20	7.90	9.60	11.10	12.10	13.20	14.50	15.50	16.44	-
Bank Credit to Industries	Y-o-Y in %	**0.40**	**7.10**	2.50	4.10	3.80	7.60	6.40	6.50	7.10	8.10	8.70	9.50	10.50	11.40	12.56	-
Deposit	Y-o-Y in %	**11.40**	**8.90**	9.30	9.90	9.80	9.60	9.30	9.10	8.90	9.80	9.30	9.30	8.40	8.80	9.50	9.60
Industry																	
Composite PMI	Index	**44.70**	**53.47**	55.30	58.70	59.20	56.40	53.00	53.50	54.30	57.90	58.90	59.20	56.60	58.20	55.10	55.50
Manufacturing PMI	Index	**50.20**	**53.97**	53.70	55.90	57.60	55.50	54.00	54.90	54.00	54.70	54.60	53.90	56.40	56.20	55.10	55.30
IIP	Y-o-Y in %	**-8.40**	11.40	4.40	4.20	1.00	1.00	2.00	1.20	2.20	6.70	19.70	12.60	2.20	-0.70	3.10	-
Manufacturing in IIP	Y-o-Y in %	**-9.60**	11.80	4.30	3.30	0.30	0.60	1.90	0.20	1.40	5.60	20.70	7.80	-3.30	-3.90	4.60	-
Consumer Durables	Y-o-Y in %	**-15.00**	12.50	1.60	-3.20	-5.70	-1.90	-4.40	-9.70	-3.10	7.20	59.10	25.20	2.30	-2.50	-4.50	-
Consumer Non-Durables	Y-o-Y in %	**-2.20**	3.30	-0.10	0.70	-0.80	0.30	3.10	-6.80	-4.40	-0.80	1.40	2.90	-2.80	-9.50	-7.10	-
Eight Core Industries	Y-o-Y in %	**-6.39**	10.43	5.44	8.73	3.24	4.11	4.03	5.85	4.76	9.53	19.34	13.10	4.50	4.10	7.90	-
Auto Sales	Y-o-Y in %	**-14.64**	**-10.70**	-15.05	-20.69	-24.42	-8.04	-15.23	-17.75	-13.71	6.61	123.93	19.02	5.86	9.86	12.33	-
Passenger Vehicles	Y-o-Y in %	**-10.35**	**8.00**	-41.20	-27.10	-18.60	-13.30	-8.10	-6.50	-3.90	-3.80	185.14	19..06	11.13	21.00	92.03	-
Two & three Wheelers	Y-o-Y in %	**-15.06**	**-10.00**	-16.60	-24.40	-33.90	-10.10	-20.90	-26.80	-20.40	15.90	262.10	23.38	8.95	15.62	12.36	-
Power Generation	Y-o-Y in %	**-1.17**	**7.00**	-1.65	2.90	1.61	2.59	-0.18	2.85	2.55	9.88	20.60	17.12	2.95	0.67	10.87	-
Steel Consumption	Y-o-Y in %	**-6.42**	**11.00**	-3.19	-3.60	-6.73	-8.59	1.97	-4.38	4.47	6.59	21.19	6.16	14.48	17.91	14.85	11.42
Cement Consumption	Y-o-Y in %	**-13.00**	**22.00**	11.10	15.00	-3.30	-	14.10	11.60	15.70	-	-	20.29	0.48	-	-	-
Sugar Production	Y-o-Y in %	**15.59**	**4.00**	25.00	61.80	-4.90	-	-2.50	5.27	26.97	19.05	57.04	154.66	74.49	15.28		-
Domestic Passengers carried by Airlines	Y-o-Y in %	**-62.24**	**59.90**	79.20	70.46	65.50	52.89	-17.15	2.16	36.74	92.14	471.21	237.68	93.83	50.96	46.55	-
External Sector																	
Exports	USD Bn	**291.18**	**417.81**	33.80	35.65	30.04	37.81	34.50	33.81	40.38	38.19	37.29	37.94	35.24	33.00	35.45	29.78
Imports	USD Bn	**394.44**	**610.22**	56.39	55.37	52.95	59.49	51.93	55.01	59.07	58.26	60.62	63.58	66.26	61.68	61.16	56.69
Exchange Rate (Average)	INR/USD	**74.20**	**74.50**	73.56	74.93	74.50	75.37	74.44	75.03	76.29	76.12	77.32	78.07	79.60	79.56	80.23	82.34
Crude Oil (Average)	USD/barrel	**44.60**	**78.29**	73.13	82.11	80.64	73.30	84.67	94.07	112.87	102.97	109.51	116.01	105.49	97.40	90.71	91.70
Forex Reserves (As on date)	USD Bn	**579.29**	**617.65**	635.36	640.39	638.00	633.61	629.76	631.53	617.65	597.73	601.36	588.31	573.88	561.05	532.66	531.08
Net FPI Flows	USD Bn	**36.18**	**-19.40**	0.39	-1.66	-0.33	-3.94	-3.82	-5.07	-6.56	-2.96	-4.73	-6.59	0.24	7.11	-0.44	-0.38
Inflation																	
CPI	Y-o-Y in %	**6.16**	**5.51**	4.35	4.48	4.91	5.66	6.01	6.07	6.95	7.79	7.04	7.01	6.71	7.00	7.41	6.77
Food	Y-o-Y in %	**7.70**	**3.76**	0.68	0.85	1.87	4.05	5.43	5.85	7.68	8.31	7.97	7.75	6.69	7.62	8.60	7.01
Core	Y-o-Y in %	**5.51**	**5.98**	5.76	6.06	6.08	6.01	5.95	5.99	6.32	7.24	6.41	6.22	6.03	6.11	6.33	6.23
WPI	Y-o-Y in %	**1.20**	**12.97**	11.80	13.83	14.87	14.27	13.68	13.43	14.63	15.38	16.63	16.23	14.07	12.41	10.70	8.39
Food	Y-o-Y in %	**3.91**	**6.73**	2.59	4.25	6.83	9.37	9.55	8.67	9.29	9.13	10.58	11.78	9.28	9.93	8.08	6.48
Manufactured Products	Y-o-Y in %	**2.70**	**11.06**	11.57	12.87	12.34	10.71	9.50	10.24	11.26	11.39	10.27	9.35	8.24	7.51	6.34	4.42
Interest Rates (in %)																	
Repo	Effective	**4.00**	**4.00**	4.00	4.00	4.00	4.00	4.00	4.00	4.00	4.40	4.40	4.90	5.40	5.40	5.90	5.90
10-year Benchmark	Average	**6.40**	**6.51**	6.30	6.46	6.45	6.50	6.80	6.87	7.00	7.23	7.49	7.66	7.53	7.40	7.36	7.59
10- year AAA Corporate Bond	Average	**6.90**	**6.90**	6.80	6.86	6.90	6.90	7.00	7.00	7.00	7.27	7.67	7.84	7.76	7.70	7.89	8.04
5- year Benchmark	Average	**6.10**	**5.99**	5.80	5.96	5.96	5.96	6.30	6.30	6.40	6.79	7.24	7.42	7.28	7.12	7.31	7.54
5- year AAA Corporate Bond	Average	**6.10**	**6.01**	5.90	5.98	6.10	6.00	6.00	6.26	6.40	6.81	7.46	7.77	7.70	7.42	7.54	8.01
MCLR of SBI (1 year)	Average	**7.00**	**7.00**	7.00	7.00	7.00	7.00	7.00	7.00	7.00	7.10	7.20	7.40	7.50	7.70	7.95	7.95
Call Money	Average	**3.20**	**3.24**	3.20	3.20	3.17	3.30	3.50	3.27	3.27	3.64	4.11	4.67	5.16	5.13	5.12	5.99

Notes: The growth rates in 2021 and 2022 over corresponding period of previous year are to be interpreted considering the unusual circumstances on account of COVID 19 pandemic since March 2020. * BWR Estimates

Source: MOSPI, RBI, eaindustry.nic.in, IHSMarkits.com, SBI, CMIE, FIMMDA, NSDL, PPAC, PIB press releases, BWR Research

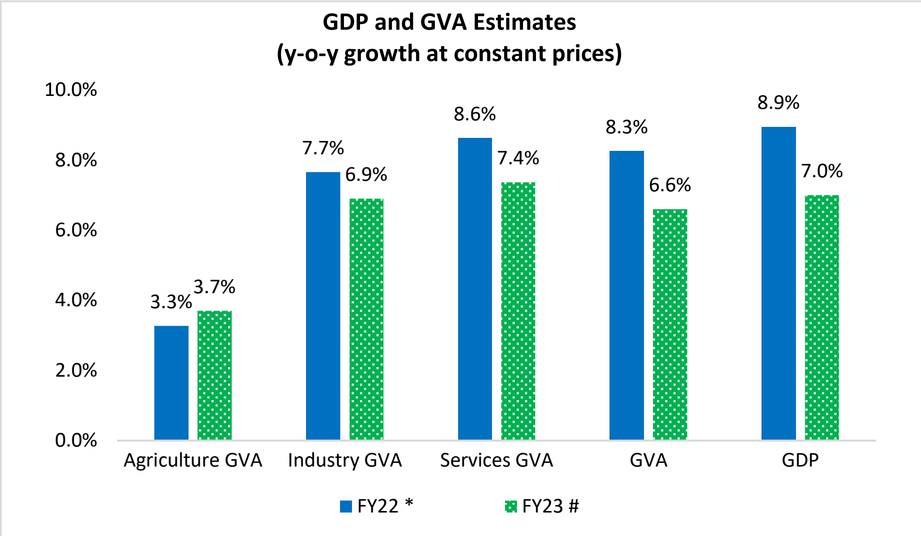
MACRO-ECONOMIC INDICATORS

BWR Views

Amid rising risks of a global recession, coupled with the tightening of financial conditions, the RBI in its latest monetary policy statement, revised India's FY23 GDP growth outlook downwards to 7.0% from its previous estimates of 7.2%. This is in line with BWR's expectations. The headwinds from extended geopolitical tensions, tightening global financial conditions and possible decline in the external component of aggregate demand can pose downside risks to these growth estimates. The H2FY23 and Q1FY24 growth outlook has been revised upwards by the RBI, but the waning monetary policy support poses a new challenge. Yet, the domestic economy is better positioned than that of many other emerging market economies, and the recovery process is likely to continue, albeit at a gradual pace. Despite inflation continues to rage above the upper tolerance limit, some high-frequency economic indicators are showing signs of continued recovery. We expect the economy to show moderate growth of 4% in H2FY23. While, in Q2FY23, the growth numbers are likely to be high at around 6.2%.

GDP Trends: Nascent signs of economic recovery; Global cues continue to daunt outlook

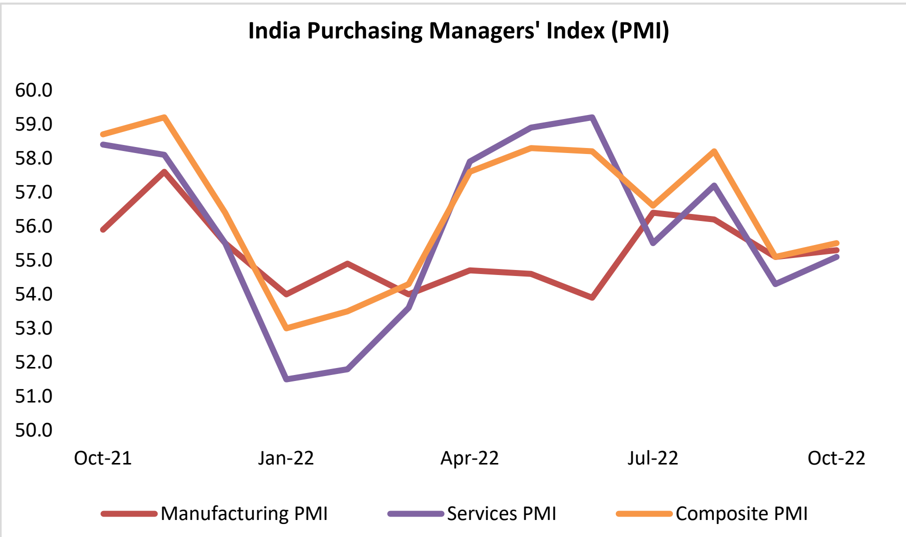
The domestic growth prospects have continued to be constrained by the ongoing geopolitical crisis, persistent supply-side bottlenecks and erratic monsoon behaviour. Yet, domestic high-frequency economic indicators are showing signs of continued recovery.



* Provisional Estimates, # BWR Estimates.
Source: Ministry of Statistics and Programme Implementation (MOSPI), BWR Research

Manufacturing and services sectors show signs of resilience

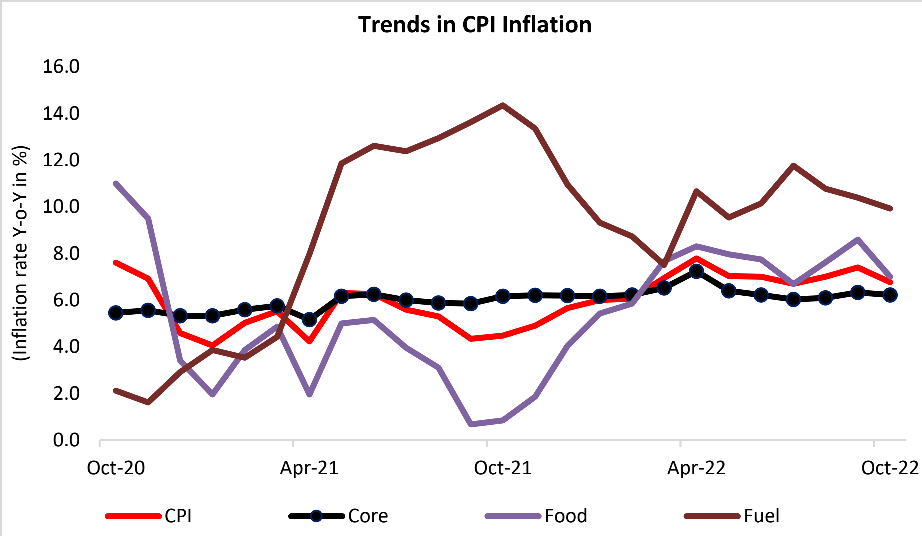
The manufacturing and services PMI, improved in October 2022, showing signs of resilience. Factory orders and production increased strongly despite losing growth momentum in the previous months while, the sector remained firmly inside expansion territory as business activity and payroll numbers were raised to support strengthening demand. The IIP and core sectors reflected revival in production with improved growth in September.



Source: www.pmi.spglobal.com, BWR Research

Inflation: Modest Moderation in inflation; food prices soften

After touching a five months' high of 7.41% in September 2022, CPI inflation eased to 6.77% in October due to softening food prices. Since January 2022, CPI inflation remained above the MPC's upper band target of 6%, as price levels remained sticky due to continued supply disruptions caused by ongoing geopolitical developments. Core inflation remained persistently lower than CPI inflation since March 2022, but remained above 6% and eased to 6.2% in October from 6.3% in September.



Note: Core inflation excluding food and fuel group
Source: MOSPI, BWR Research

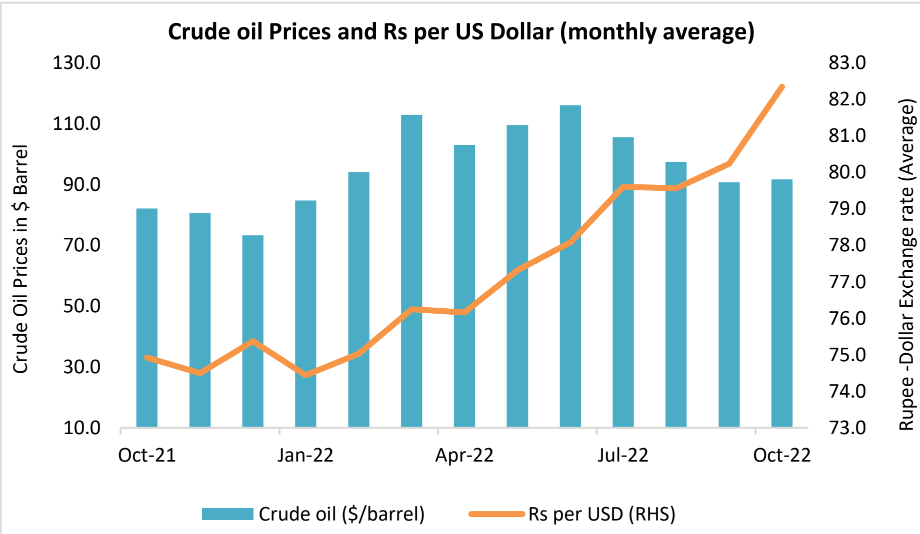
BWR Views

Due to higher food and fuel inflation, the inflation rate averaged 7.1% during H1FY23. The record-level inflation intensified significant downside risks to the growth momentum. With inflation remaining above the 6% mark for nine consecutive months, the RBI failed to meet its inflation target. The RBI continued with its rate hiking spree, and the key policy repo rate has been increased by 190 bps so far since 4 May 2022. The recent softening trend likely to ease some pressure on MPC to temper rate hikes.

Despite the increase in the rate cycle, we expect CPI inflation to remain above 6.5% in Q3FY23. With easing food prices and high base, inflation may ease below the 6.5% level in Q4.

Crude oil prices remained stable; rupee depreciated further

Crude oil prices remained relatively stable in October after easing since July due to slowing global demand. On the other hand, pressure on the Indian rupee has intensified, and the currency crossed Rs 83/USD on 20 October 2022, following the strengthening of USD, rising interest rates abroad coupled with FPI outflows from the domestic markets. Although, the RBI continue to intervene to prevent the Indian rupee from falling further, the rupee lost close to 8% against USD since March 2022.



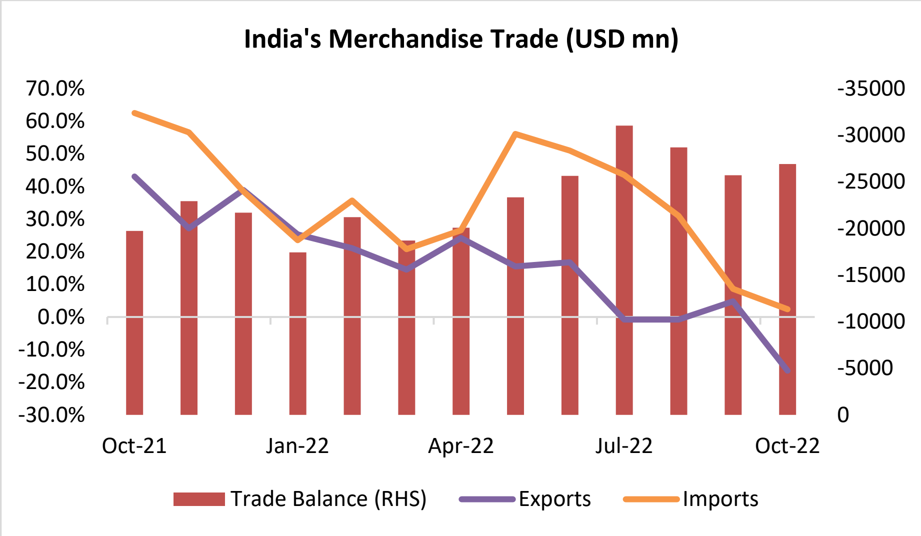
Source: www.ppac.gov.in, RBI, BWR Research

BWR Views

Moderate fall in crude oil prices provided some relief on imported inflation, but the decision of the OPEC to restrict oil production may result in higher crude oil prices in the coming months. Higher crude oil prices adversely impact India's current account, inflation and exchange rate stability. The depreciation of the rupee has already been discouraging imports because imported goods have become more expensive.

Merchandise trade: External sector continue to remain under pressure

A weaker rupee, higher crude oil and other commodity prices have rendered imports expensive. In dollar terms, growth in merchandise imports decreased by 16% in October m-o-m, while imports too fell by 7%. Exports declined by 16.5% y-o-y, while imports registered a moderate of 2.4%. During H1FY23, exports improved by 17% over H1FY22, while imports risen by 38.6%.



Note: Data is provisional.
Source: Ministry of Commerce and Industry, BWR Research

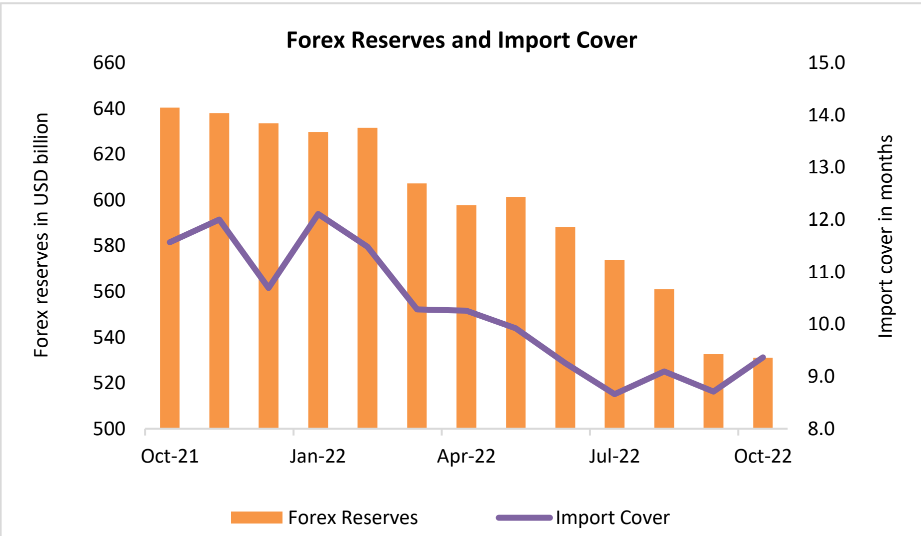
BWR Views

Geopolitical tensions continued to keep the external sector under stress, while recessionary expectations in the advanced economies may dampen demand for domestic exports. The recent fall in crude oil prices brings some respite on import bills, but a weak rupee is discouraging imports due to rising import costs.

The trade deficit narrowed to USD 25.71 bn in September 2022 from USD 28.68 bn in August 2022, but increased by USD 3.2 bn compared to September 2021. Due to the widening trade deficit, India's current account balance recorded a deficit of USD 23.9 bn (2.8% of GDP) in Q1FY23, up from USD 13.4 billion (1.5% of GDP) in Q4FY22.

Weak rupee continues to drain forex reserves

With the depreciation of the rupee leading to valuation loss, India's foreign exchange reserves have depleted sharply in the recent period. Forex reserves were reduced by about USD 109 bn in a year to nearly USD 531 bn as on 27 October 2022. The RBI has continued to use its foreign exchange reserves to curb volatility in the exchange rate, and FPIs have also started withdrawing from Indian markets since September 2022, after being net buyers in July and August 2022.



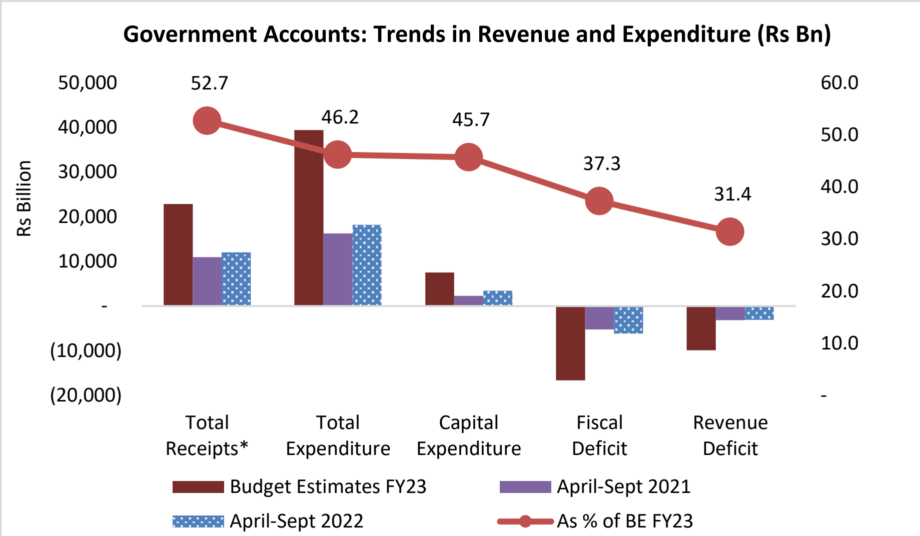
Source: Ministry of Commerce, RBI, BWR Research

BWR Views

Frequent intervention by the RBI kept the rupee from depreciating further. However, forex reserves depleted sharply, and the import cover of India's foreign exchange reserves fell to 8.7 months in September 2022 compared to 11.3 months in the year ago period.

Government Finances: Fiscal development shows a mixed picture

Provisional data released by the CGA for April-September 2022 (H1FY23) shows that the central government has spent 46.2% of the budget expenditure for FY23 with spending through capital expenditure reaching 45.7% of the Budget Estimates (BE), as compared to 41.4% of BE in H1FY22. Fiscal deficit touched 37.3% of the budget targets so far.



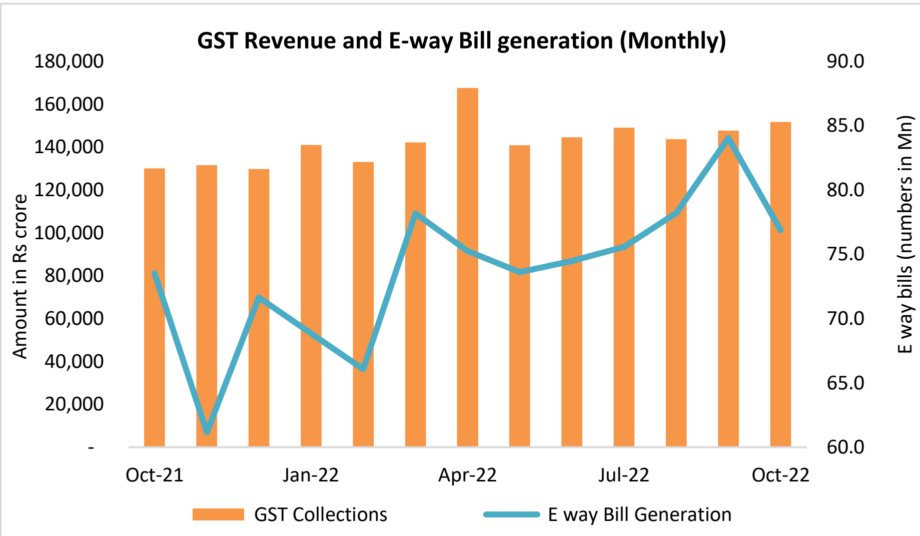
Note: Data is provisional, RBE: Revised Budget Estimates. * Excluding government borrowing.
Source: Controller General of Accounts (CGA), BWR Research

BWR Views

The overall tax revenue collection has been healthy so far and in spite of the cuts in excise and customs duties on petroleum products and edible oil to rein in the prices, the aggregate tax revenue is expected to be higher by about Rs. two trillion. However, the budget this year has placed heavy emphasis on capital expenditure, and it is budgeted to increase by 24.5% of the revised estimate of last year. With a fiscal deficit target of 6.4% of the GDP for FY23, higher crude oil prices impose a huge risk on fiscal management. It remains to be seen whether the government will be able to maintain the tempo of increasing capital expenditure in H2FY23.

GST: Tax collections remain buoyant; second highest ever

There has been a steady increase in the revenue collections, and the total GST collection in October amounted to Rs 1.5 trillion, which was 17% higher than the collection for the same month last year. GST collections have been higher than Rs 1.4 trillion in eight months in a row. State-wise, Maharashtra, Uttar Pradesh, Gujarat and Karnataka have reported double-digit growth in GST revenue receipts in October 2022 compared to a year ago period.



Source: PIB press releases, GSTN, BWR Research

BWR Views

Buoyant GST collections actually indicate the stabilisation of the technology platform. Due to improved tax compliance and better tax administration by both the central and state tax authorities, coupled with a more stable technology platform in place, GST collections may continue to be higher in the coming months. The generation of E-way bills has led to a significant improvement in compliance. However, in October 2022, the pace of growth in E-way bill generation declined, recording just 5% increase over the corresponding month last year.

SECTORAL INDICATORS

Banking

BWR Views

The Net Interest Income and Net Interest Margin improvement was supported by revision in lending rates and growth in overall advances. The asset quality of the public sector banks also improved and BWR believes that the same shall continue to improve in the remaining part of FY23 due to level playing by NARCL for the resolution of high-value Non-Performing Assets (NPAs).

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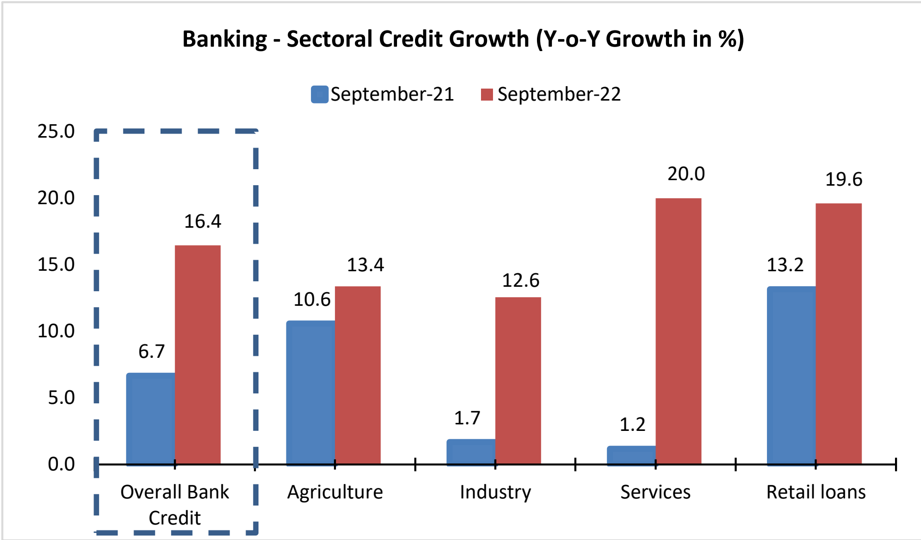
Koppula Shyam Sundar
(Rating Analyst)

Improvement in asset quality of public sector banks is expected to continue

The public sector banks continued to show better performance as of 30 September 2022, on a y-o-y as well as on a q-o-q basis. There has been a healthy growth in both deposits and advances. Further, there was an increase in earnings reflected through improved net profits, supported by an increase in Net Interest Income (NII) and other income, especially the fee-based income for the half year ended 30 September 2022. Though, CPI inflation softened to 6.73% in October 2022, the inflation concern remains, as it is still on the upper side of RBI's tolerance level.



Source: RBI, BWR Research

National Asset Reconstruction Company Limited (NARCL), India's Bad Bank incorporated on 7 July 2021 has commenced operations and has submitted bids for two assets. The lenders are likely to call for the Swiss Challenge Auction soon. Another important development is that RBI has taken the state-owned lender Central Bank of India (CBI) out of the Prompt Corrective Action (PCA) subject to certain conditions and continuous monitoring. CBI was the only bank under PCA.

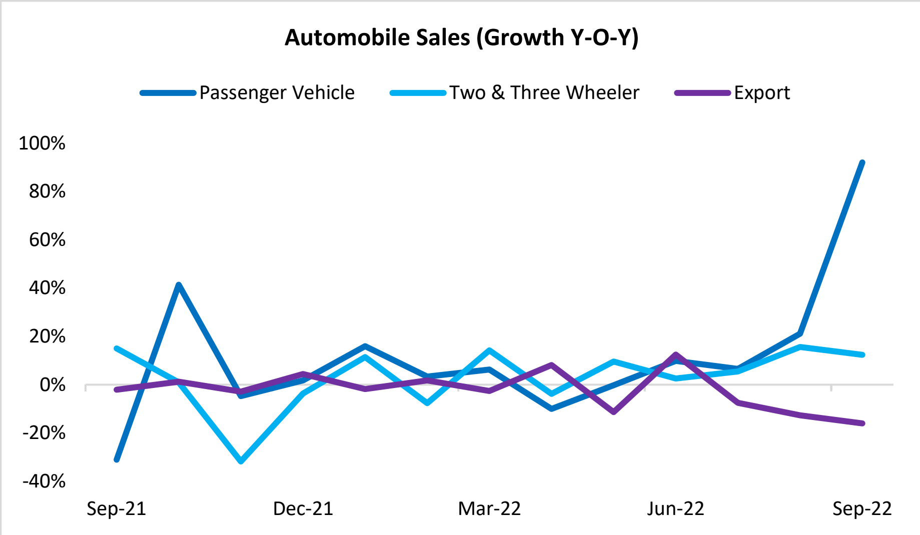
As per the RBI data on sectoral deployment of credit, the non-food credit growth on a y-o-y basis stood at 16.4% in September 2022 compared to 6.7% in September 2021. Since March 2022, the bank credit grew by 6.2%, as compared to 0.1% in the corresponding period previous year.

The overall credit growth was led by the personal loans sector followed by services sector and industry. The growth in the personal loans segment was largely driven by the growth in the housing and vehicle loans segments. Credit to agriculture and allied activities continued to show an accelerated growth of 13.4% in September 2022 compared to 10.6% in September 2021. On the whole, the outlook for the banking industry appears to be bright for FY23.

Automobiles

Festive season uptick demand in automobile industry

Sales of passenger cars in India, which had declined over the last two years, have now resumed to the pre-pandemic levels. Domestic Passenger Vehicles (PVs) industry witnessed a robust demand during Q2FY23, fuelled by the festive season and new launches. Sales in September 2022, almost doubled to 3,07,389 units and established a new monthly record. There has been a 92% growth y-o-y in sales and approximately 10% growth on m-o-m basis (281,210 units were sold in August 2022).



Source- CMIE, BWR Research

Easing of semiconductor supply chain issues and strong customer demand in the first normal festive season post Covid-19 have resulted in the ramp up of production and sales of vehicles. The Two and Three-wheeler vehicle segments also witnessed good demand and manufacturers posted an uptick in domestic sales. The two and three-wheeler segment reported a growth of 12% y-o-y to 17,50,109 units in September 2022. However, total exports have declined by 16% to 3,78,926 units due to economic slowdown and higher inflation in the importing countries.

BWR Views

With the excellent resilience shown by the Indian economy over the last few quarters, the festive season has further fuelled the demand momentum. Halfway through the current financial year, the automobile sales improved notably owing to the low base, easing of semiconductor shortage challenges, narrowing supply-demand gap, new launches and renewed consumer enthusiasm following a COVID-free festive season after a gap of two years. Passenger vehicle sales saw a robust growth in September, with mid-segment cars and SUVs grabbing the festive demand which also lifted the entry-level category. However, the two-wheeler sales remained subdued. BWR expects the market momentum to remain strong in the second half of FY23 as demand for PVs is expected to increase, especially in the SUV category. Commercial vehicle and tractor segments are also on a positive trajectory and are anticipated to see continued demand due to rising infra projects and government spending. Concern still remains in two wheelers, especially in the entry level category.

Saurabh Agarwal
(Manager - Ratings)

Akanksha Maindiratta
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Telecom

Introduction of 5G services will provide impetus to the growth of telecom infrastructure development

Chintan D Lakhani
(Director - Ratings)

Ronojyoti Deb
(Senior Manager- Ratings)

Telecom companies are vying to get an early start in the launch of 5G services. In this regard, Reliance Jio has recently announced that it has completed 5G service in the top-1000 cities, while Airtel has stated that it has network roll out plans in 5,000 towns. The government is taking steps to scale up infrastructure deployments in the 5G network roll outs. It has recently announced certain amendments to the Indian Telegraph Right of Way rules 2016 to expedite the upgradation of the telecom network and bring down the time and cost of telecom infrastructure deployment.

With the advent of 5G services, it is expected to account for 40% of all subscriptions in India by 2027. Further, it is expected 56% of the total mobile data traffic in the country will be carried by the 5G network in 2027.

Power

Proposed monetization of power transmission assets expected to generate moderate grant support for future capacity additions in the power sector

Resembling other brownfield asset monetization models such as the Toll-Operate-Transfer (TOT) model for highways and the Operations, Management and Development Agreement (OMDA) for airports, the Ministry of Power introduced a model in October 2022 for monetizing power transmission assets in the public sector. It has termed it as 'the Acquire, Operate, Maintain and Transfer (AOMT)' model. The model basically entails ownership transfer of power transmission assets for limited periods to private entities selected through competitive bidding. The entities would be required to transfer these assets back to the government upon completion of their period of operations.

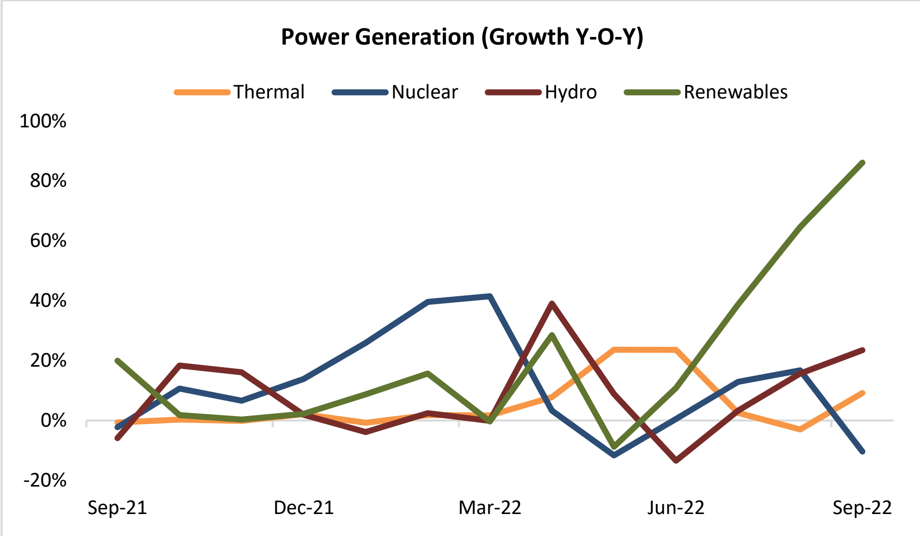
The introduction of the new AOMT model has relevance in light of Central Electricity Authority (CEA's) recent fund requirement estimates of ~Rs. 14.3 lakh crore during 2022-27 and ~Rs. 17.2 lakh crore during 2027-32 for power generation projects in the country, as mentioned in its Draft National Electricity Plan released in September 2022. The proposed AOMT led monetisation of transmission assets would fetch some near-term cash for the government, which may be channelled as grant support for power capacity additions envisaged in the said plan. However, the plan notes that ~75% of the said funding requirements for power generation projects would need to be raised as debt.

BWR Views

The government is expected to extend its asset monetization practices earlier adopted in other infrastructure sectors to the power transmission sector, through a newly introduced PPP model termed as the AOMT model. Yields from deployment of this model are expected to be applied in greenfield power projects, to meet capacity targets envisaged in the Draft National Electricity Plan. However, given the primacy accorded to debt funding in the said plan, rigorous due diligence would be key to circumvent the emergence of stressed power assets as seen in the past decade.

Chintan D Lakhani
(Director - Ratings)

Sourav Sen
(Rating Analyst)



Source- Central Electricity Authority, BWR Research

A key consideration which the Draft National Electricity Plan addresses is the need for energy storage systems in the power sector in future, with more emphasis on renewables and less on coal. Given the inherent intermittency characterizing solar and wind power generation, energy storage systems can serve as buffers during potential phases of power demand exceeding supply. The two main energy storage systems identified for development are Pumped Storage Plants (PSP) which basically harness level differentials between adjoining artificial reservoirs and Battery Energy Storage Systems (BESS) systems. The plan estimates that a PSP based power capacity of ~6.8 GW would be required to meet a peak projected power demand of ~272 GW in 2026-27 whereas a PSP capacity of ~18.8 GW together with a BESS capacity of ~51.6 GW would be required for a peak projected power demand of ~363 GW in 2031-32.

Steel

Lower steel prices are expected in the short to medium term

BWR Views

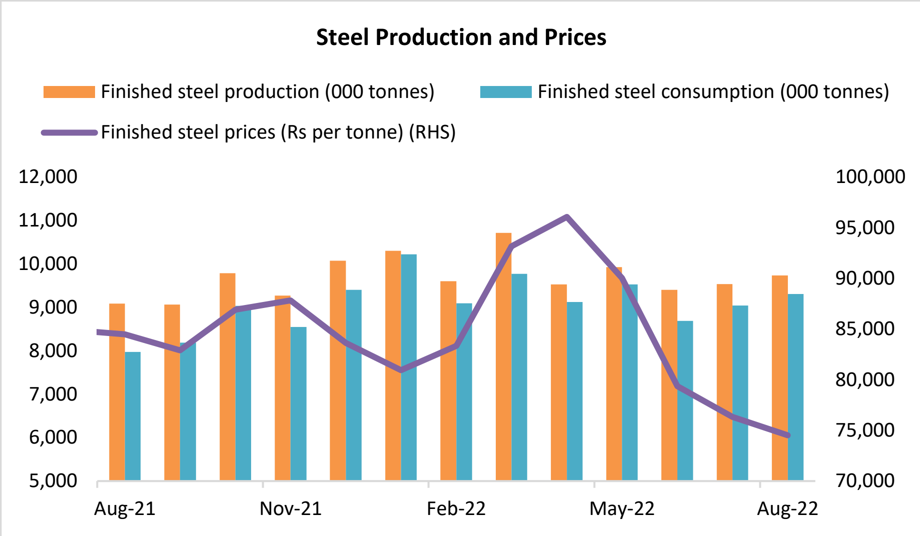
Indian steel consumption is growing at around 7-8% globally, however, the steel demand is under pressure which has resulted in a check on local steel pricing. The near-term outlook for the prices would continue to remain negative, while demand continues to remain stable.

Iron ore prices continued to fall and reached 2020 levels amid limited demand from steelmakers globally. Coking coal and natural gas prices, although continue to remain fluctuating, are on a downtrend. Steel prices will eventually follow a similar direction and are expected to remain under pressure in the short to medium term.

The continued war between Russia and Ukraine, in addition to international tensions across geographies like China and Taiwan, is not aiding in any better price outlook in the near term. Prevailing uncertainty about the demand in winter from the Eurozone, expectation of lower production due to higher gas prices and subdued demand from China have resulted in lower global steel demand. Steel consumption is expected to grow at 1-2% for the remaining part of FY23.

Bal Krishna Piparaiya
(Principal Director - Ratings)

Forum Parekh
(Senior Manager- Ratings)



Source: CMIE, BWR Research

With domestic steel prices more or less reaching the level of global prices, the government is considering removing the export duty that was levied to curb the price rise in the domestic market. Given the fall in steel prices and stable demand at the local market, the steel ministry is also in favour of phase-wise removal of the export duty.

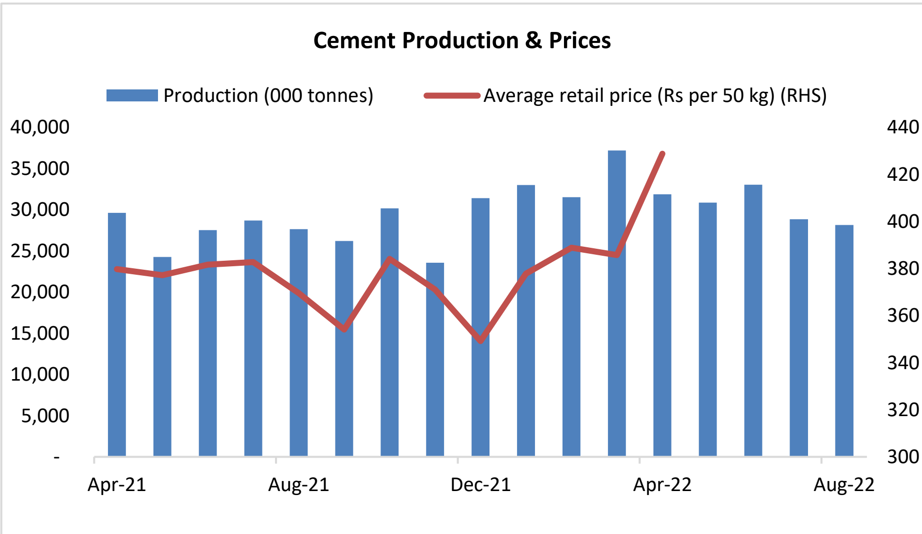
Cement

Cement industry expected to pick up pace in FY23

BWR Views

Higher government spending on infrastructure, increased focus by the government on low cost and affordable housing, and pick up in real estate demand in the backdrop of the general elections in 2024, continue to be the key drivers of demand for cement industry.

The cement sector has witnessed a decline in demand in the recent months on account of the extended monsoons and labour shortage due to the festive season across the country. However, the situation is expected to improve going forward. Going by the post monsoon historical trend, there is likely to be an increase in cement prices in the short-term. However, the manufacturers are expected to keep the prices at a moderate level to maintain the demand.



Source: CMIE, BWR Research

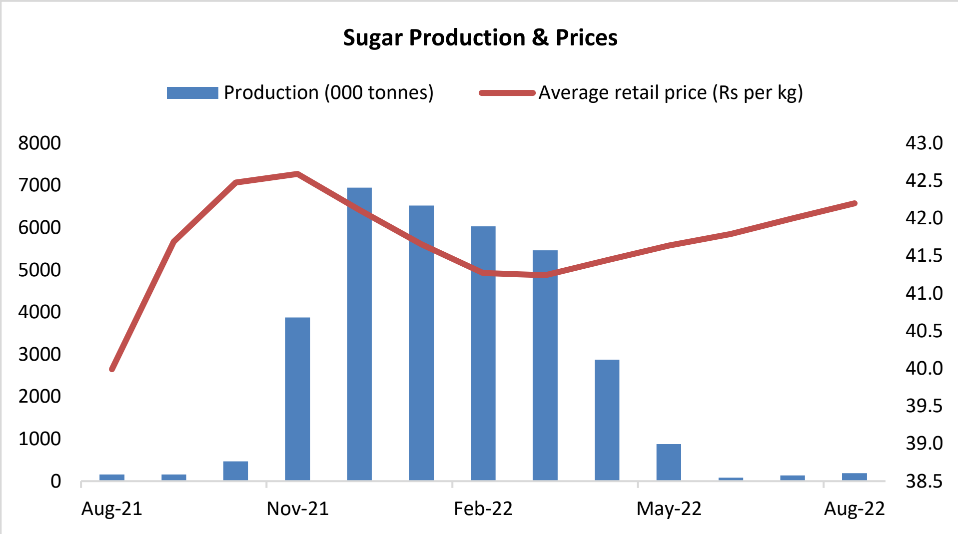
Saakshi Kanwar
(Associate Director - Ratings)

Vineetha Ann Varughese
(Sr Rating Analyst)

Sugar

Reduction in sugar export quote expected to lead increased supply in domestic market

The sugar production at 365 lakh tons for sugar supply (SS) 2022-23 is expected to grow by ~2% after accounting for diversion of 45 lakh tons for ethanol production (34 lakh tons in SS 2021-22). As per the advance estimate released by Indian Sugar Mills Association (ISMA) an increase of ~6% in acreage has been envisaged. The Government of India has capped the sugar exports at 60 lakh tons for the period between 1 November 2022 and 31 October 2023 to ensure sufficient availability of sugar for domestic consumption at a reasonable price. This is a considerable decline from ~110 lakh tons exported during 2021-22 SS which had resulted in substantial foreign currency inflows.



Source: CMIE, ISMA, BWR Research

BWR Views

On 2 November 2022, Cabinet Committee on Economic Affairs (CCEA) has approved, an increase in ethanol prices for Ethanol Supply Year (ESY) 2022-23, from 1 December 2022 to 30 November 2023 which is expected to aid increased levels of ethanol production. During the ESY 2022-23, a total of about 545 crore litres of ethanol would be required and supplied to achieve the target of 12% blending. The government has advanced the target of 20% ethanol blending in petrol to ESY 2025-26 from 2030.

Saakshi Kanwar
(Associate Director - Ratings)

Swarn Saurabh
(Assistant Manager- Ratings)

DEBT MARKET INDICATORS

Movements in Bond Yields

Bond yields continue northwards on global cues.

BWR Views

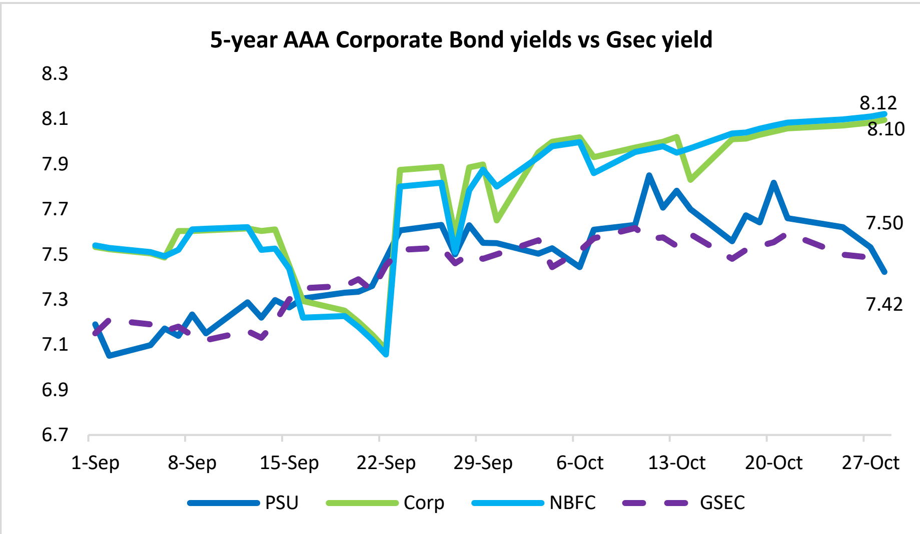
The successive hikes in the policy repo rates by RBI has led to hikes in the benchmark lending rates/ Repo Linked Lending Rates (RLLR) for retail and corporate loans in BFSI segments, however the deposit rates have not risen much at the back of a good growth. The fixed income securities have depreciated and the banks' treasury profits have shown a hit as forecasted by BWR in its earlier publications. The long-term bond yields have shown a volatile trend on account of global uncertainties and the short-term yields, a hardening trend. In BWRs opinion, in the near-term, the bond yields are expected to remain elevated and volatile.

Bal Krishna Piparaiya
(Principal Director - Ratings)

Fuelled by rise in global crude oil prices and interest rates, continued global inflationary trends, augmented government domestic borrowings and weakening rupee, the bond yields continue to rise. At the back of rise in repo rate by 190 bps by RBI in about last 6 months and global issues including hike in interest rates by the Federal Reserve Bank (FED) and European banks, the Gilt bond yields in India have continued to spike at the short end of the yield curve, while the rise is relatively lower at the longer end. Non-inclusion of the Indian debt in the global bond index has added fuel to the fire. Over a period of 6 months, the short and mid-term yields have risen substantially whereby the 3 months T-bill yield has risen by 169 bps, 6 months by 147 bps, 1 year by 146 bps and 3 years by 46 bps. As against this, the longer-term yields have bounced back to similar levels of 6 months ago and the 5- and 10-year yields show a rise of only 8 bps and 30-year declined by 10 bps as on 10 November 2022, indicating tapered rise as the tenure increases and expectations of higher interest rates in short to medium term. However, the longer-term yields have been volatile on account of uncertainties in the global scenario and volatility in rupee-dollar exchange rate.

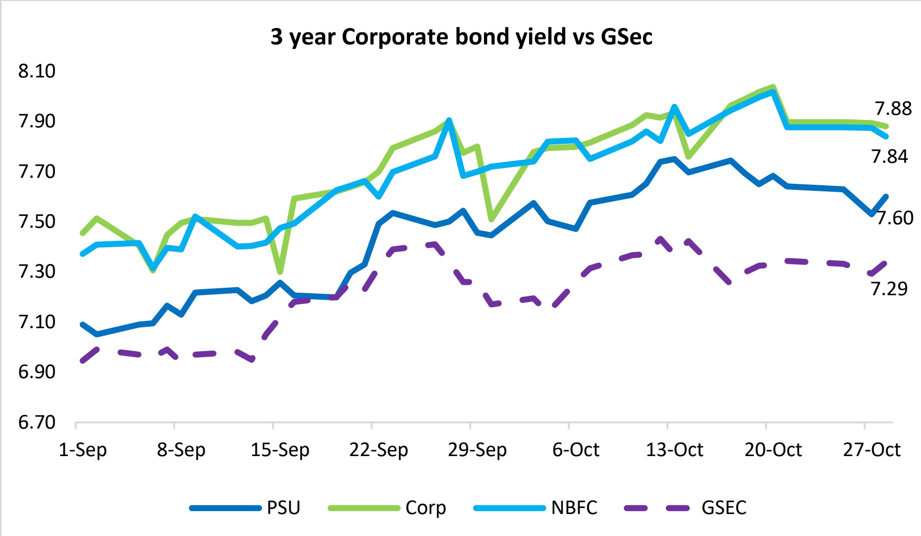
The Gilt yields were ruling at the following levels on 10 November 2022 (as against 8 September 2022): 10-year 7.29% (7.142 %), 3-year at 7.19 % (6.97 %), 5-year at 7.18 % (6.97 %) and 30-year at 7.52% (7.38%); 3-month at 6.44 % (5.66 %), 6-month at 6.75% (6.11%), 1-year at 6.94 % (6.34 %). The Corporate bond yields moved in tandem.

The bond yield (annualised) issued by Public Sector Units (PSUs), corporates and Non-Banking Finance Companies (NBFCs) maturing in 5-, 3- and 1-year tenures with the corresponding government securities are provided below.

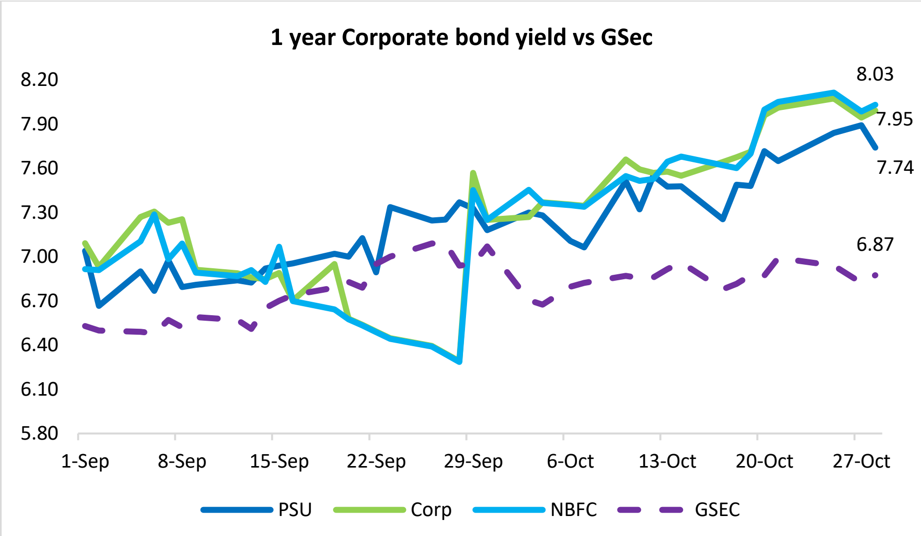


Source: FIMMDA, SBI, HDFC, BWR Research

The yield of AAA-rated corporate bonds maturing in 5-, 3- and 1-year tenures has remained stable to volatile due to timely strategic market operations and liquidity injection by the RBI and regulators.



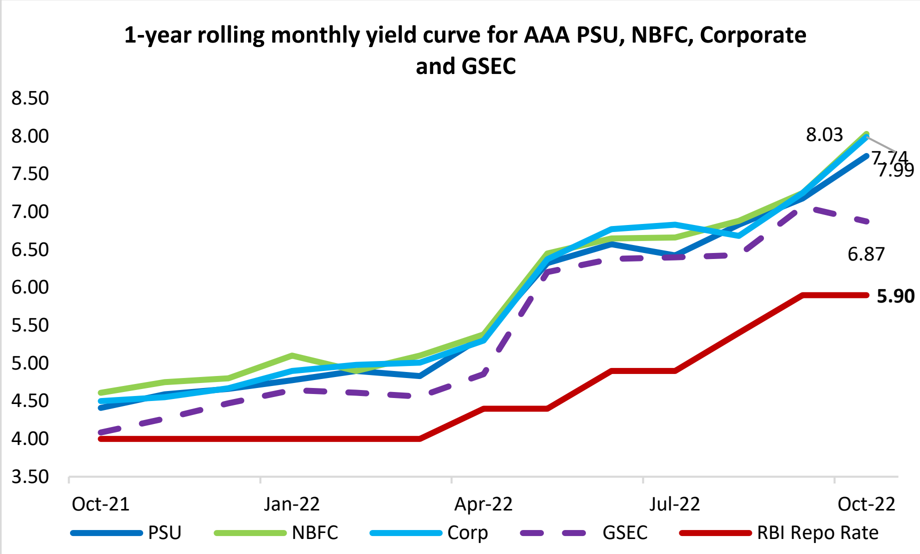
Source: FIMMDA, SBI, HDFC, BWR Research



Source: FIMMDA, SBI, HDFC, BWR Research

Yield curve of AAA PSUs, NBFCs, Corporates and G-Sec

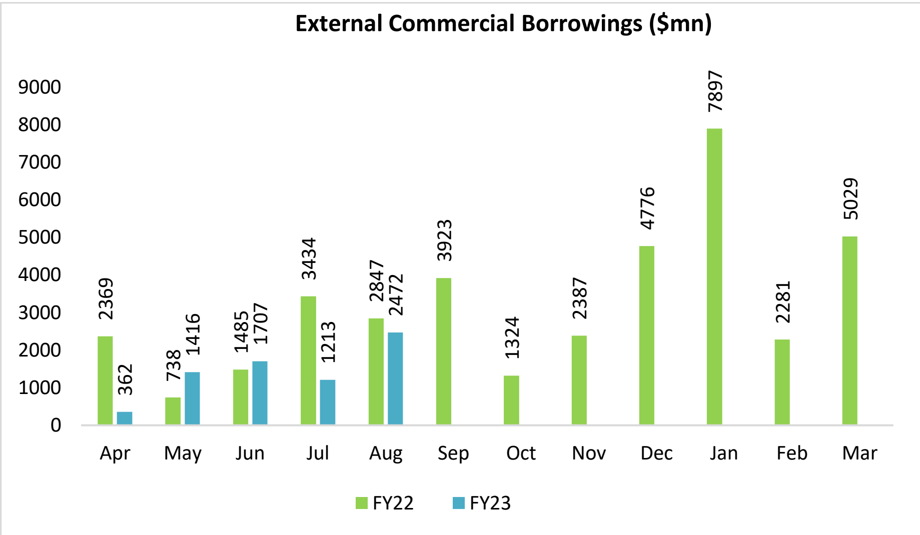
The borrowing costs for bonds maturing in 1 year issued by PSUs, NBFCs and corporates witnessed some escalation in the range by 271-349 bps in October in line with the G-Sec yields (279bps) against the corresponding period last year. The key policy rate (repo rate) was increased by 190 bps so far since May 2022.



Source: FIMMDA, BWR Research

External Commercial Borrowings

According to RBI data, Indian corporates' borrowings were at USD2.5 billion from offshore markets in the form of External Commercial Borrowings (ECBs) during August 2022 compared to USD2.8 billion during the same period last year, recording a slight fall in the trend.



Source: RBI, BWR Research

BWR Views

Indian companies' ECBs which declined in April 2022 y-o-y, reversed the trend and showed a rise in May and June 2022. However, again showed a declining trend in July and August 2022 (y-o-y) on account of continuing uncertainties in the global market.

In BWR's opinion, in spite of the global rise in interest rates, the demand for ECBs is expected to rise on account of interest rates differentials, however the overall borrowings are expected to remain in the same range y-o-y.

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