

ANNUAL ECONOMIC REVIEW 2022-23







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Abstract

The provisional GDP estimates for FY23 released in May were higher than the consensus estimate. A strong final quarter performance pushed the GDP growth for the full year to 7.2 per cent, higher than the 7 per cent estimated in February. This upside to the growth estimate takes the growth momentum deep into the current year. Several forecasting agencies also share optimism as they revise their growth estimates for FY24 upwards. The latest evidence also does not indicate any slowing of activity in the first two months of the current year. India is the fastest-growing major economy, is now no longer only a statistical fact. The country's impressive growth experience in FY23, when the world economy was rocked by inflation and restrained by monetary tightening, is a narrative on what works or does not work for the Indian economy.

What clearly works for India's economy is the strength of its domestic demand. The pandemic had struck at its roots to cause an unprecedented contraction of output in FY21. The domestic demand has, however, recovered since then and moved from strength to strength in FY23. In the process, it enabled a near convergence of the pre- and post-pandemic quarterly growth trajectories. Stated simply, FY23 has brought the economy to a touching distance of the quarterly output it would have otherwise achieved in the absence of the pandemic. Post-pandemic quarterly trajectories of consumption and investment have already crossed their pre-pandemic paths. Net exports, however, need to cover some more ground as external demand did not work for India's economy in the second half of FY23 as well as it did in the first half. When external demand starts to work, the pre-and post-pandemic trajectories of real GDP will also converge. The supply side served well the demand side in FY23. The agriculture sector registered a twelve-quarter record high growth rate in the last quarter. The industrial sector rebounded in Q4, driven by manufacturing. The year-end saw the contact-intensive services sector fully recovering to its pre-pandemic expanse and depth.

Rising employment levels further worked for India as it increased inclusivity and strengthened domestic demand. The labour force participation rate (LFPR) in India rose through the pandemic in line with the pre-pandemic trend. The overall unemployment rate declined to a five-year low of 4.1 per cent in FY22, raising with it the worker-population ratio. More recently, in FY23, the urban unemployment rate declined in each quarter, reflecting steady growth in employment levels in the country. Growing employment levels, in part, have been an outcome of several policy measures implemented over the last few years. These measures strengthened the corporate sector, supported small enterprises, improved the ease of doing business, and attracted foreign capital to increase the employment generation capacity of the economy. As these measures deepened after the outbreak of the pandemic, they reflected the now-vindicated understanding that only growth reforms would have worked for India in supporting economic recovery. Simply putting more cash in the hands of the people would not have worked.



Inflation emerged as the major challenge in FY23 for India as it did for the rest of the world following the emergence of the geopolitical conflict and the impact of El Nino. The world over, policy measures to mitigate inflation were broadly similar-monetary tightening by the central banks and supply easing by the governments. What, however, worked for India was the country's inflation breaching the target to a lesser extent as compared to the groups of emerging market economies (EMEs) and advanced economies (AEs). This happened as the average inflation in FY23 was lower in India than in the groups of EMEs and AEs, possibly owing to greater supply easing in the country. The RBI, thus, did not have to increase the policy rates as much as the central banks of other countries did. As the year-end approached, the declining international prices of commodities led to a steep decline in India's wholesale price inflation. The pass-through to the retail level took some time, but before the year-end, headline inflation in India entered the target range. Core inflation, however, remained sticky but started to decline from March 2023 onwards.

An increase in repo rates has worked for India, enabling a 40-45 per cent of transmission in lending and deposit rates by the end of FY23. This, coupled with fiscal and administrative measures by the Government, has been adequate to ease inflation down into the target range while ensuring that domestic demand is not crushed. Consequently, the growth of credit rose in FY23, feeding the elevated demand. High growth in credit contributed to increasing the profitability of banks whose bottom lines were already improving with the declining Gross Non-Performing Assets (GNPA) ratio. Clearly, the management of repo rate increases and the subsequent pauses in the latest two meetings of the MPC have worked for the Indian economy.

The external demand worked for the economy until the first quarter of FY23. Thereafter it fell under the influence of monetary tightening impacting merchandise exports. However, services exports continued to surge as apart from IT exports, India's skilled workforce provided professional services to multinational companies through global capability centres set up in the country. What also worked for India was the decline in global commodity prices, as it reduced the cost of imports, whose volume continued to be high through FY23 to sustain the growth of economic activity in the country. The developments in the merchandise and services trade helped the current account deficit (CAD) to narrow quickly towards the end of FY23, in part assisted by high levels of remittances. Reducing CAD worked for the economy as it saved resources for strengthening domestic demand. Besides a smaller CAD, net FDI inflows and smaller FPI outflows led to a year-end forex reserve worth ten months of imports. FY23 closed with India becoming the 5th largest forex reserve holder in the World, a cushion that contributed to orderly adjustment of the ₹ with lower volatility relative to many EMEs and AEs. Despite the impact of slowing external demand on merchandise exports, the external sector has also worked for the economy.

A critical cog in the wheel of economic growth in FY23 was the disciplined fiscal stance of the central government. The year ended with a lower fiscal deficit (as per cent of GDP) compared to the previous year. Yet, the government could cut duties and increase welfare spending to alleviate stress from inflation. The government could also maintain its enhanced provision for



capital expenditure, which is now leading to the crowding-in of private investment. Financial data for a consistent set of listed companies indicates broad-based private capex growth of 22 per cent in FY23. While revenue buoyancy helped in meeting the budgeted fiscal deficit ratio to GDP, rationalising revenue expenditure was key to maintaining a disciplined fiscal stance.

The Indian economy has carried the momentum from FY23 into the current fiscal year. High-frequency indicators paint a healthy picture of the state of the economy. Urban demand conditions remain resilient, with higher growth in auto sales, fuel consumption and UPI transactions. Rural demand is also on its path to recovery, with robust growth in two and three-wheelers sales. Goods and Services tax collection, Purchasing Managers' Index (PMI) for the manufacturing and services sector continues to expand. On the global front, the uptick in economic activity during the first quarter of 2023 has also continued in the second quarter, as evident in the expansion of the global Composite PMI. However, factors that can constrain the pace of growth include escalation of geopolitical stress, enhanced volatility in global financial systems, sharp price correction in global stock markets, a high magnitude of El-Nino impact, and modest trade activity and FDI inflows owing to frail global demand. Should these developments deepen and dampen growth in the subsequent quarters, the external sector may challenge India's growth outlook for FY24.

Despite unprecedented global challenges in the last few years coming on top of balance sheet troubles in Indian banking and non-financial corporate sectors, macroeconomic management has been stellar. It contributed significantly to enhancing India's macroeconomic stability and set India on a quicker recovery path than has been the case in other nations. Investments in supply-side infrastructure raise the possibility that India can enjoy sustained economic growth longer than it has been able to in several decades. Strong balance sheets and digital advancements could lead to better credit decisions allowing India's financial cycle to sustain for longer periods before encountering the challenge of bad debts. Thus, India appears poised to sustain its growth in a more durable way than before. Nonetheless, it is no time to rest on laurels nor risk diluting the painstakingly and consciously achieved economic stability. If we are patient, the rising tide will lift all boats as it has begun to.

India's GDP Growth in FY23

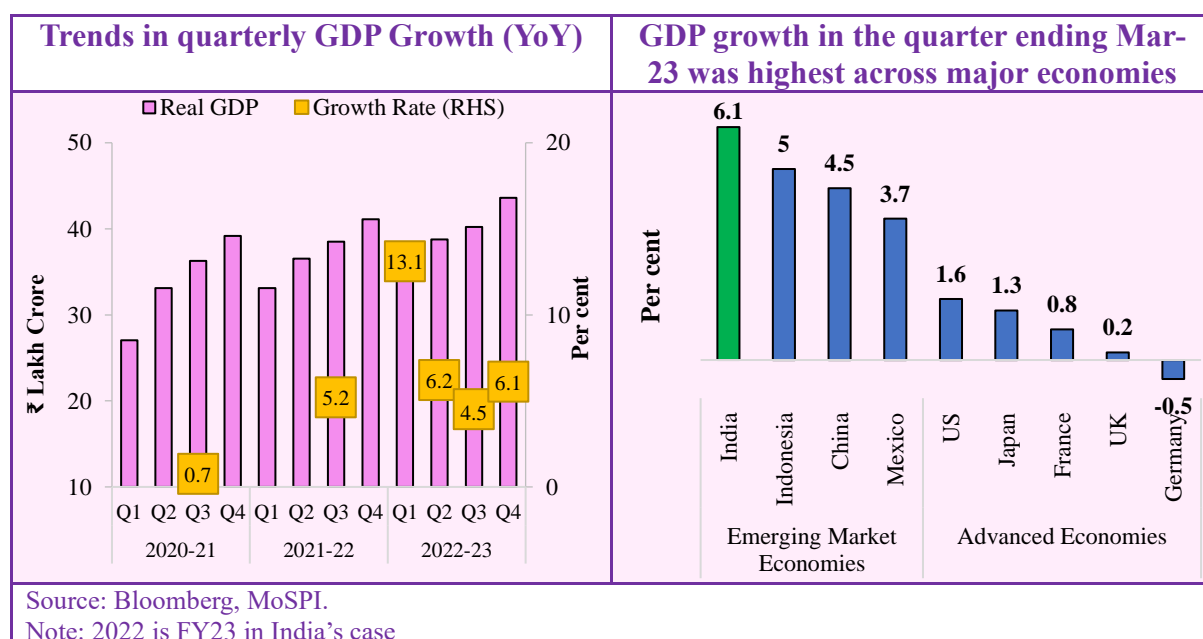
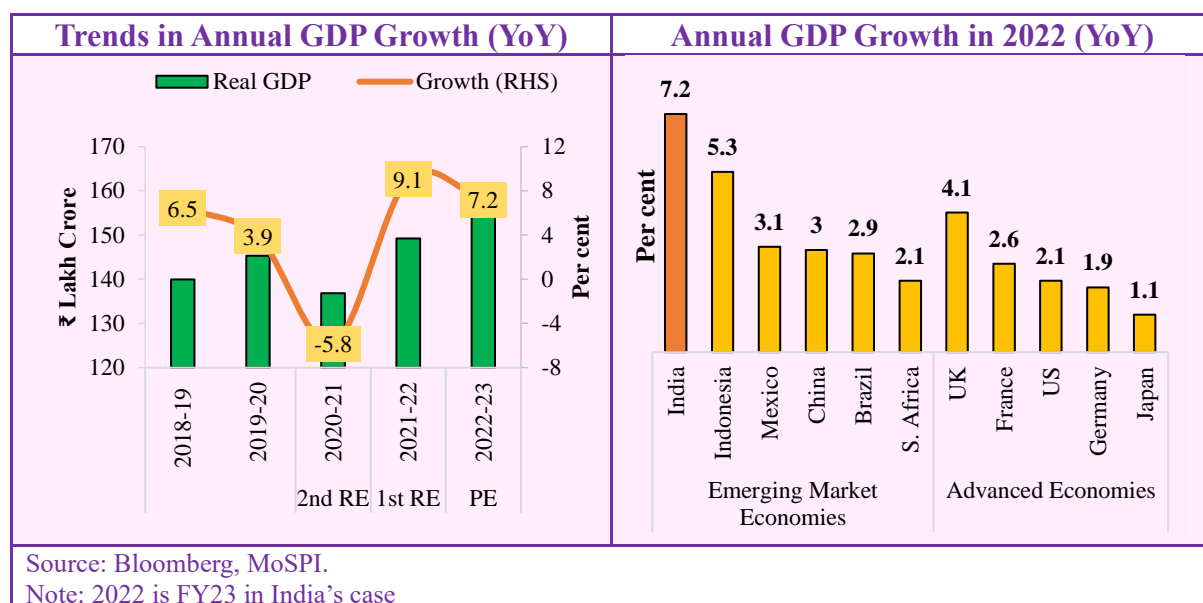
Resilient growth path amidst rising global uncertainties

1. The global economy was on the path of recovery after the waning of the COVID-19 pandemic until the Russia-Ukraine conflict broke out in February 2022. The conflict led to disruption in global supply chains, financial tightening, and a spike in the prices of critical commodities. The impact of these disruptions was witnessed in multiple leading indicators of global economic activity, such as global composite PMI entering the contractionary zone, capital outflow from most of the EMEs to traditionally safe havens, currency depreciation, and widening of current account deficit (CAD), among others. The global GDP projections for 2022 were revised downwards by the IMF. Though inflationary pressures have begun to ease, the impact of monetary tightening is slowing economic activity, especially in the advanced



economies. In its latest April update on World Economic Outlook (WEO), the IMF forecasted global growth to fall from 3.4 per cent in 2022 to 2.8 per cent in 2023, then rebound to 3 per cent in 2024.

2. Amidst these global spillovers, India's economy has sustained its growth momentum in FY23 on account of its strong macroeconomic fundamentals and the prompt policy action by the Government and the RBI. India's real GDP expanded by 7.2 per cent in FY23, the highest among major economies. The latest estimate of real GDP turned out to be higher than the second advance estimate released in February 2023. The higher annual growth was driven mainly by better-than-expected growth in the fourth quarter of the fiscal year.



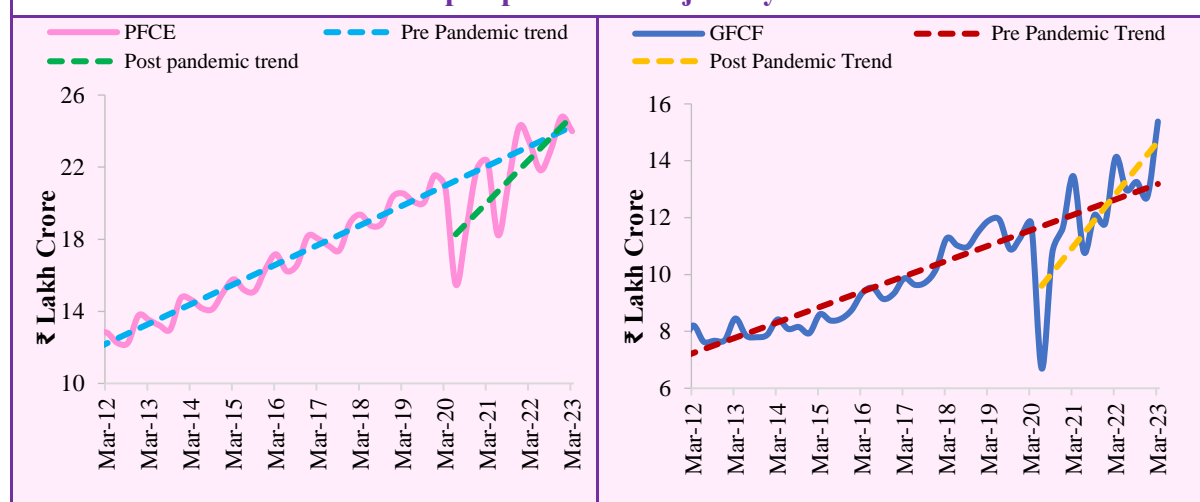
The performance of India's real GDP in Q4 of FY23 stood out compared to other countries. The year-on-year (YoY) growth in real GDP in Q4 of FY23 is estimated at 6.1 per cent, compared to 4 per cent



growth in Q4 of FY22 and 4.5 per cent growth in Q3 of FY23. On a sequential basis, the growth in Q4 of FY23 at 8.4 per cent is higher compared to 3.7 per cent in the previous quarter, reflecting the sustenance of growth momentum in Q4.

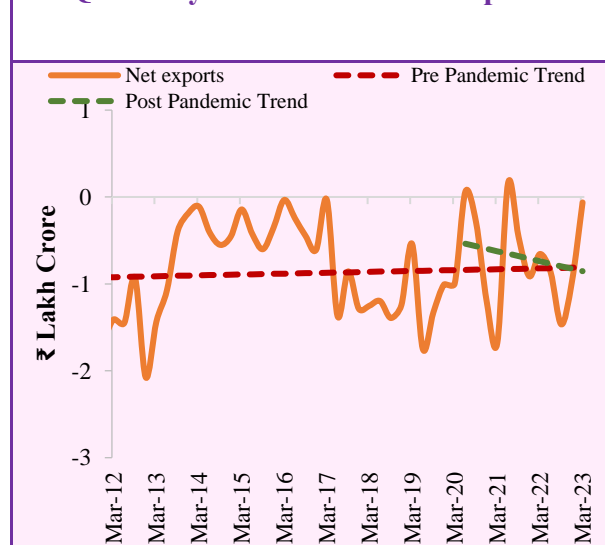
3. The performance of GDP growth in Q4 of FY23 was broad-based and addressed all concerns about the recovery of consumption and investment demand to the pre-pandemic growth trajectory. Enabled by the release of pent-up demand, real Private Final Consumption Expenditure (PFCE) has surpassed the pre-pandemic trend trajectory. Similarly, a large step-up in public sector capex over the last three years and a favourable credit situation in the country have contributed to real Gross Fixed Capital Formation (GFCF), also surpassing the pre-pandemic trend trajectory.

In the case of Real PFCE and GFCF, the post-pandemic trend line has surpassed the pre-pandemic trajectory



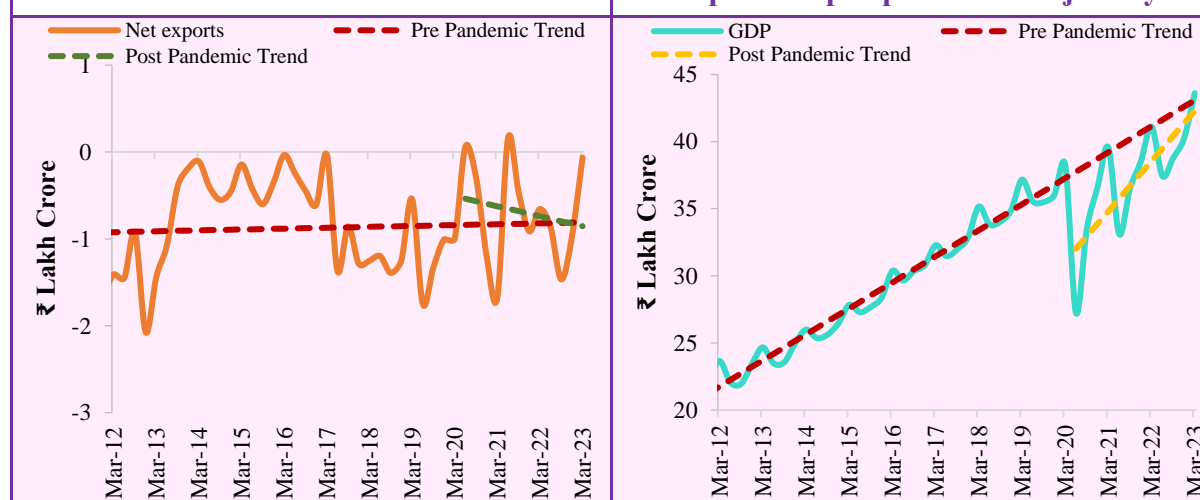
Source: MoSPI

Quarterly trends in real net exports



Source: MoSPI

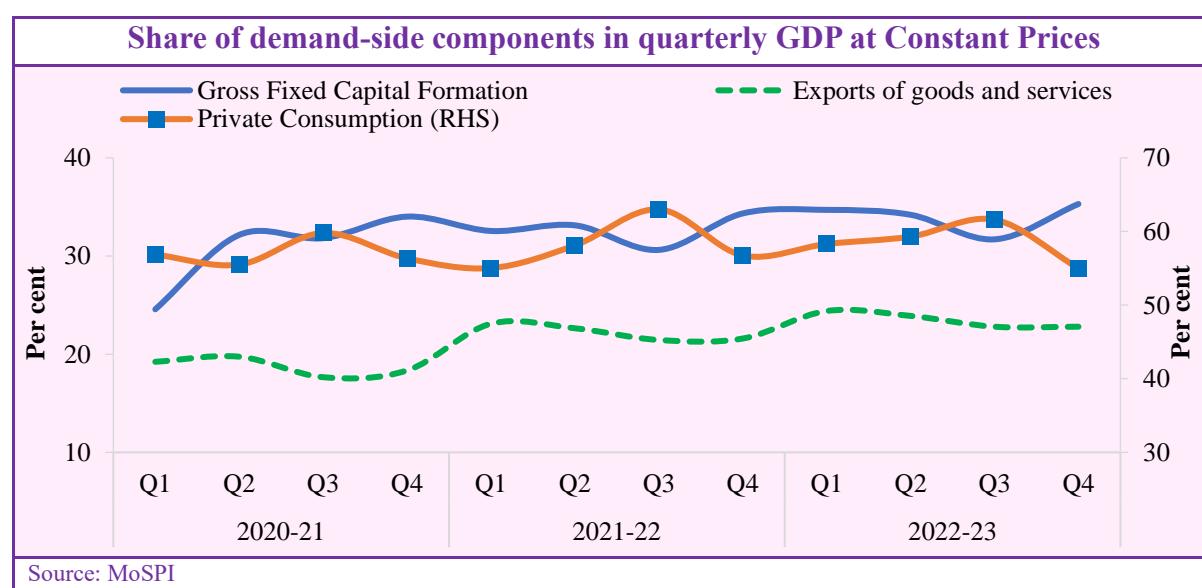
Real GDP Post Pandemic trend line yet to surpass the pre-pandemic trajectory





4. However, the faster growth in post-pandemic economic activity in the Indian economy and high import prices have kept the import demand elevated. As a result, the negative net exports in real terms have shown a sharp post-pandemic downward trend trajectory as compared to a slightly upward pre-pandemic trend trajectory. This has prevented the post-pandemic real GDP trend line from crossing the pre-pandemic trend trajectory, although it is very near to doing so. Given the decline in prices of India's import basket and a sustained surge in service exports, the net exports gap is expected to become smaller sooner than earlier expected. This will enable real GDP to surpass its pre-pandemic trend trajectory in the near future.

On an annual basis, private consumption (PFCE) as a proportion of GDP (at Constant Prices) for FY23 reached the highest in 17 years, and the gross fixed capital formation (GFCF) (at Constant Prices) recorded the highest proportion of GDP in 10 years. However, the quarterly data shows a moderation in the share of private consumption in GDP for Q4 of FY23. Its share in GDP declined from 61.6 per cent in Q3 of FY23 to 55 per cent in Q4 of FY23, partly because capital formation growth spurred in the fourth quarter.



Gross Fixed Capital Formation (GFCF) has been a major growth driver in Q4 of FY23, with its share in GDP at a 10-year high of 35.3 per cent. This has been propelled by the crowding-in of private sector investment by a significant ramp-up in public sector investment over the years. The share of total exports in GDP moderated to 22.8 per cent in Q4 of FY23, compared to 24.4 per cent in Q1 of FY23, as synchronised monetary tightening by major economies led to a decline in consumer spending in advanced nations and moderation in international trade.

On its own, privation consumption is showing strong enough growth, as evidenced by several high-frequency indicators. Some of these HFIs include personal loan growth, which continues to be impressive, notwithstanding the environment of higher interest rates. Increased spending by credit cards in Q4 of FY23 can be attributed to a surge in e-commerce and point-of-sale transactions. The outlook

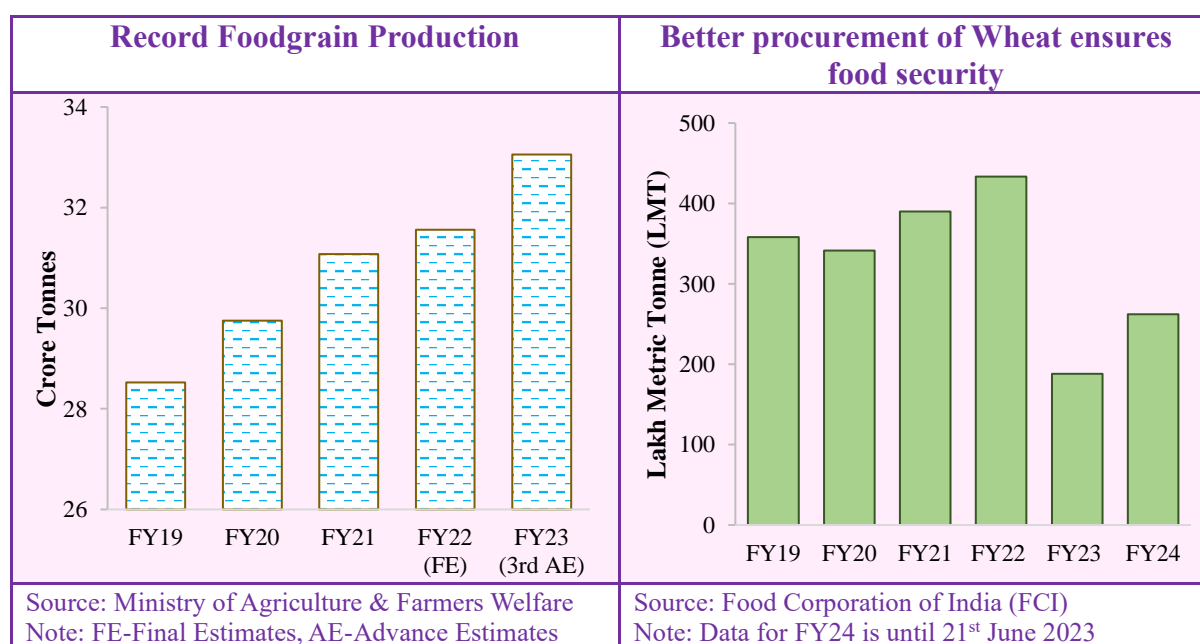


for consumption growth remains positive, with the Current Situation Index and Future Expectations Index of the RBI undergoing substantial improvement.

Bright kharif prospects, with adequate availability of inputs

5. The supply-side components of GDP exhibit strengthening of the economy across all sectors. Following a growth moderation in the first two quarters and a revival of growth in the third, the agriculture sector registered a twelve-quarter record high growth rate in Q4 of FY23. This is partly due to an upward revision in the estimates of rabi production as per the third advance estimates. The forecast of a normal monsoon despite the prevalence of El Nino, adequate availability of seeds and fertilisers and sufficient storage capacity in reservoirs augur well for healthy kharif sowing in FY24.

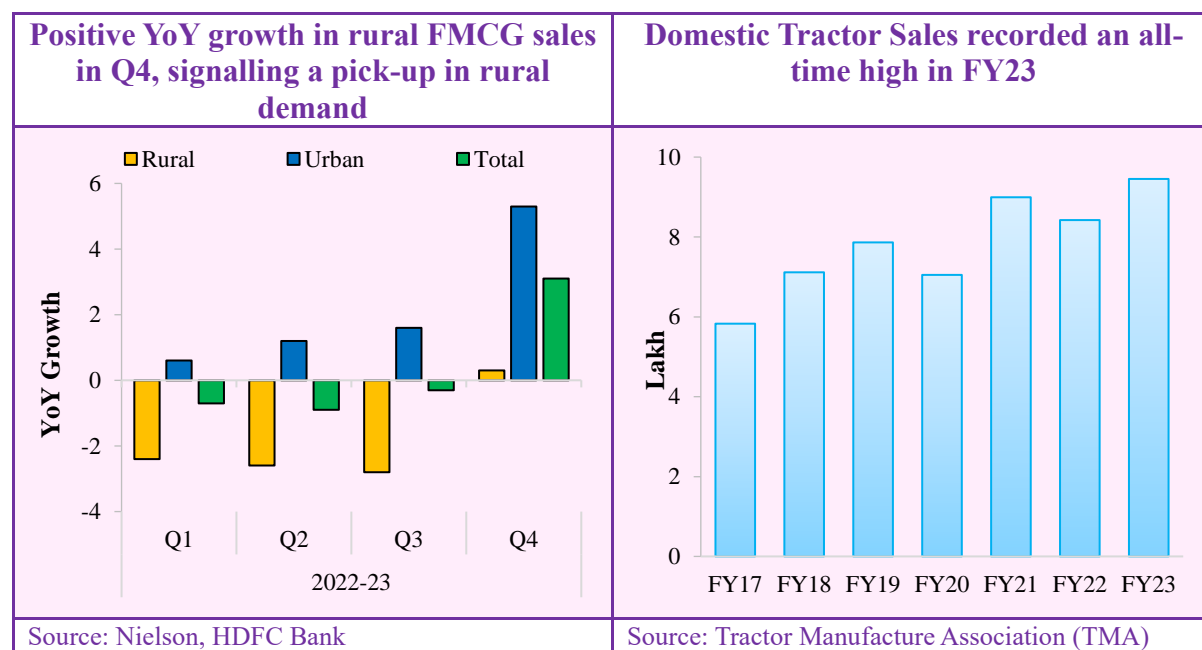
Comfortable wheat procurement provides a buffer to the agri-economy. Nearly 2.6 crore Metric Tonne of wheat has been procured until 21st June 2023, benefitting 21.3 lakh farmers. As against the buffer norm of 2.1 crore Metric Tonnes for the April-June period of 2023, the combined stock position of wheat and rice in the central pool has reached 7.3 crore Metric Tonnes, placing India in a comfortable position to meet its domestic foodgrain requirements.



6. Increase in foodgrain production accompanied by rising rural wages (agricultural and non-agricultural sectors) have spurred rural demand. Year-on-year (YoY) growth in Fast Moving Consumer Goods (FMCG) volume sales in rural areas turned positive in Q4 of FY23, signalling a pick-up in rural demand. Buoyed by an increase in Minimum Support Price (MSP) that boosted farm income, easy availability of finance, and favourable monsoon, domestic tractor sales recorded an all-time high in FY23. Going forward, an increase in MSP for rabi and kharif crops, a hike in Fair and Remunerative Price (FRP) for Sugarcane and a rise in the



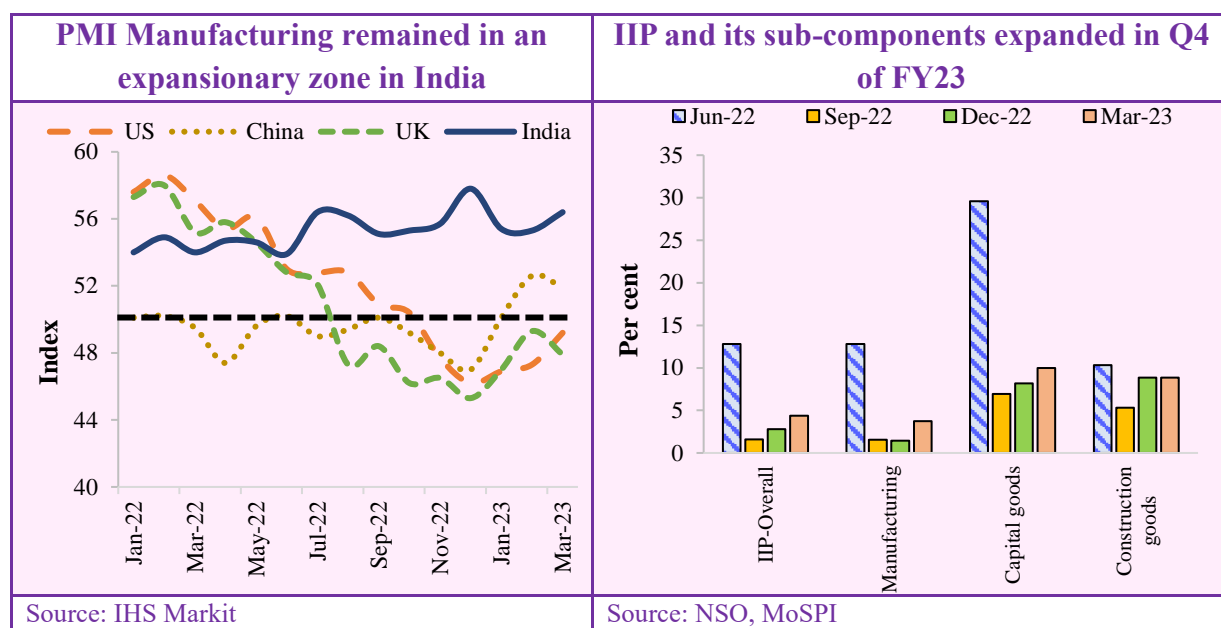
Mahatma Gandhi National Rural Employment Guarantee Scheme (MGNREGS) wage rate are expected to improve the financial security of rural households further and boost rural demand.



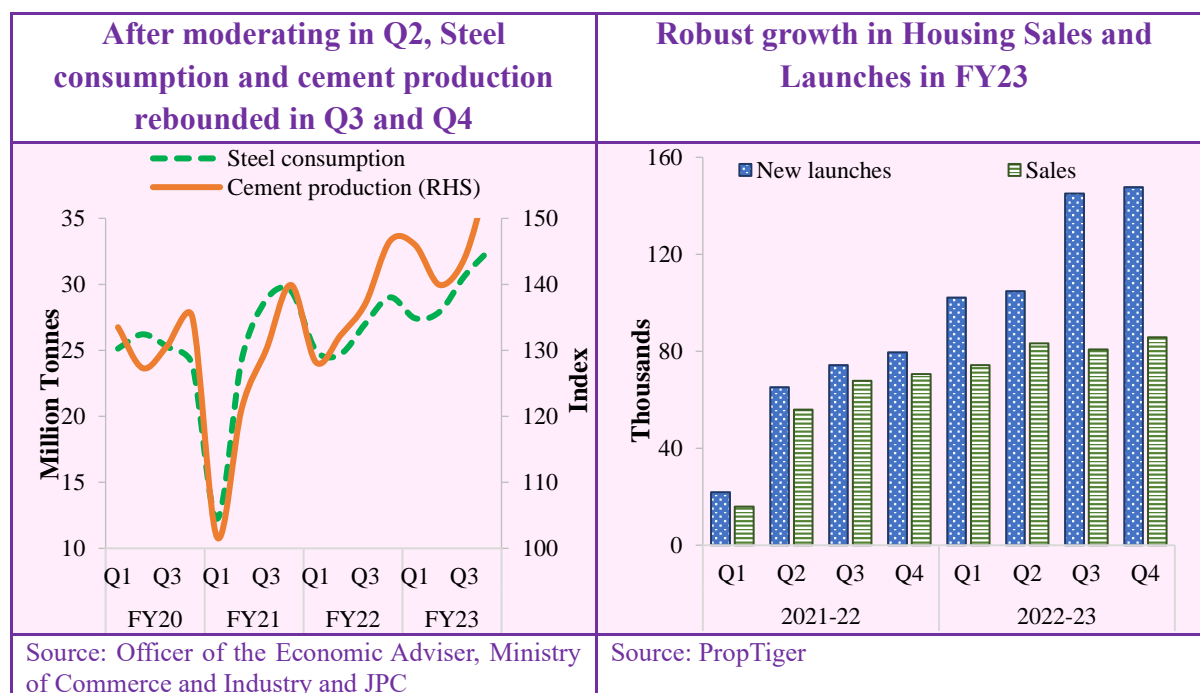
Sustained performance of the Industrial Sector

7. The industry sector the world over was adversely impacted during FY23 owing to supply chain disruptions and high raw material costs. Major economies witnessed PMI Manufacturing entering the contractionary zone post-August 2022. However, in the case of India, PMI Manufacturing remained in an expansionary zone throughout the year, supported by new orders and output expansion. Yet the growth in the manufacturing sector's GVA witnessed a temporary moderation in Q2 and Q3 of FY23 owing to elevated input costs. However, with the decline in input costs, rising demand and increased capacity utilisation, the manufacturing sector's GVA revived in Q4 of FY23. The growth in the manufacturing sector's GVA, which constitutes around three-fourths of the industrial Gross Value Added (GVA), led to a rebound in the industrial sector in Q4 of FY23. This was also supported by growth in Q4 of the other major component of the industries, i.e., the construction sector.

Several high-frequency indicators also point towards a strong rebound in the industry sector. After growing at a modest pace in Q2 and Q3, the Index of Industrial Production (IIP) expanded in Q4 of FY23, with a notable increase in the production of capital goods and infrastructure/construction goods. This signifies a pick-up in capital formation in the economy. The construction sector (IIP) registered double-digit growth in Q4 of FY23 after slowing in Q2 on account of heavy monsoons. Other construction sector indicators, such as cement production and steel consumption, also rose in Q4 of FY23. The growth in the sector has been supported by Government's emphasis on infrastructure and increased housing demand. The Indian housing market has witnessed significant growth in sales and new house launches in FY23, despite increasing home prices and a rise in interest rates on home loans.



Among the other segments of IIP, the electricity sector witnessed a notable increase in production in FY23, as intense summer heatwaves and economic recovery required a rise in electricity production.



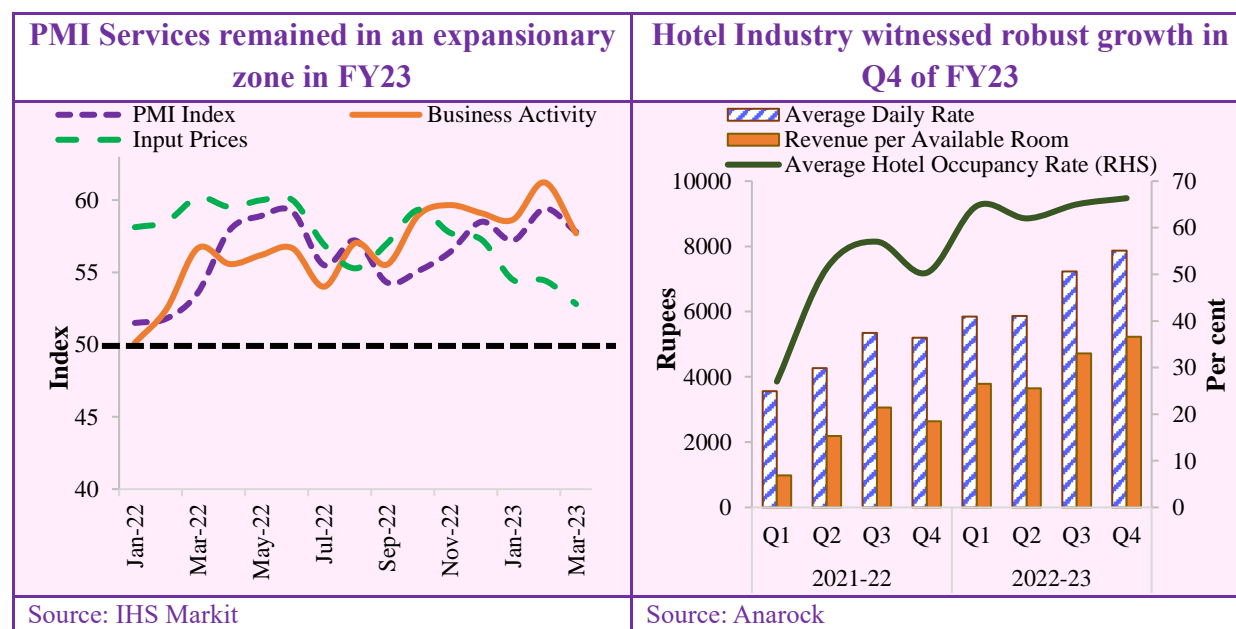
6. Going forward, the expansion of reforms such as the National Logistics Policy, the Production Linked Incentive (PLI) scheme, and PM GatiShakti, among others, are likely to boost manufacturing output in the coming months.



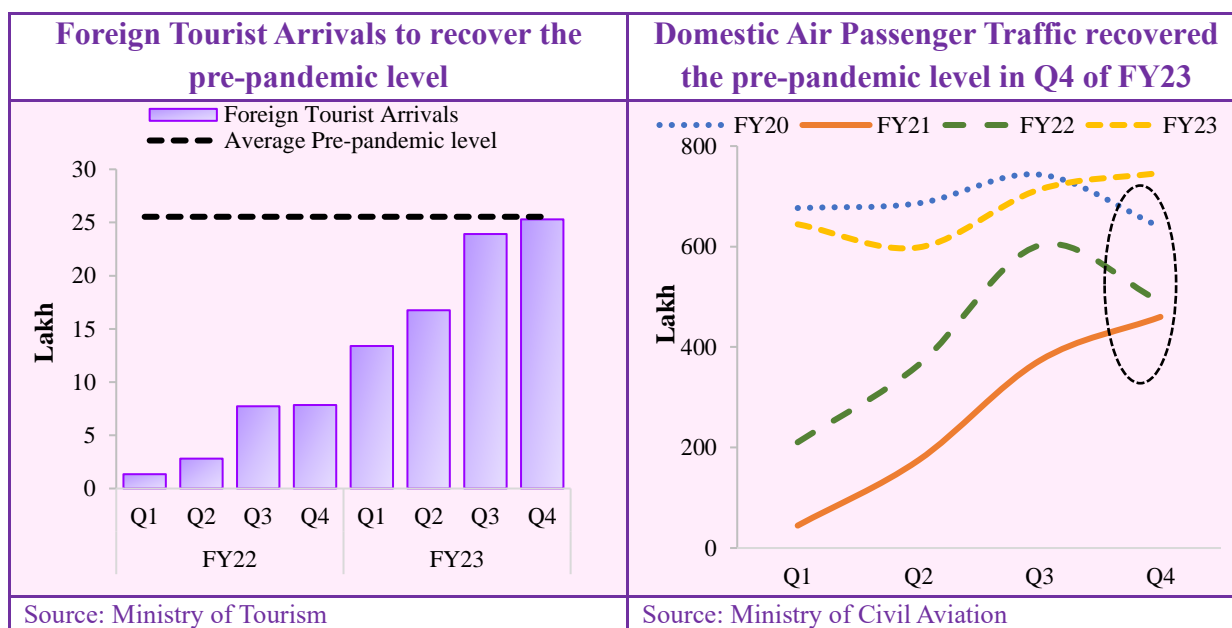
Strong Services sector performance

7. The growth in the services sector also remained strong in FY23, largely driven by the contact-intensive services sectors. This sector completely recovered to the pre-pandemic level in FY23, driven by the removal of mobility restrictions, the release of pent-up demand, and near-universal vaccination coverage. PMI Services remained in the expansionary zone throughout the year, supported by improvement in new business intakes, increased orders placed, and flagged price pressures of inputs and raw materials post-October 2022. Trade, Hotels, Transport, Communication and Services related to Broadcasting and Financial Real Estate & Professional Services are major drivers of the growth in this sector.

The Hotel Industry began a strong recovery in FY23, with the hotel occupancy rate surpassing the average pre-pandemic level of FY20 in Q4, accompanied by a rise in Average Daily Rate (ADR) and Revenue per Available Room (RPAR). The growth in the hospitality sector was driven by domestic leisure travel growth, the resumption of business travel in the country, as well as wedding and social events. Small-to-medium-sized domestic MICE (Meetings, Incentives, Conference, Exhibitions) events also made a comeback, fuelling demand for hotels. The tourism sector also showed signs of revival, with Foreign Tourist Arrivals (FTA) in India close to the average pre-pandemic level in Q4 of FY23, supported by the resumption of scheduled international flights. With the removal of pandemic-related restrictions, a surge in corporate travel and a rebound in MICE tourism and Bleisure¹ travel, domestic air passenger traffic surpassed the pre-pandemic level in Q4 of FY23.



¹Bleisure is a term used to describe travel that combines both business and leisure



Growth momentum build-up in FY23 is likely to be sustained in Q1 of FY24.

8. High-Frequency Indicators (HFIs) for April/May 2023 reflect a pick-up in economic activity in Q1 of FY24 and sustenance of growth momentum. Gross GST collection rose by 12 per cent over the last year to ₹1.57 lakh crore in May 2023, crossing ₹1.5 lakh crore benchmark for the fifth time since its inception. E-Way bills showed positive growth in April and May 2023, suggesting prospects of strong growth in GST collection in the upcoming months. Increasing electronic toll collection levels reaffirm rising commercial activity. PMI manufacturing increased to a 31-month high of 58.7 in May, driven by record expansion in input stocks and a strong rise in new orders and inputs. Growth momentum in the Services sector continued with expansion in PMI services, which stood at 61.2 in May 2023, highlighting a further expansion in output across sectors, which rose at the second quickest pace since July 2010.

9. The outlook for the manufacturing sector is positive, as highlighted in RBI's Industrial Outlook Survey. Most of the respondents were positive on demand conditions in terms of improved assessment for the overall business situation, production, order books and capacity utilisation in the next two-quarters of FY24 as well. The outlook for the services sectors also remains bright, as indicated in the RBI's Services and Infrastructure Outlook Survey. The survey respondents were upbeat about the overall business situation and the turnover during Q1 of FY24. They expect favourable employment conditions for both full-time and part-time employees. The survey expects that demand for services is likely to grow sequentially till the third quarter of FY24.



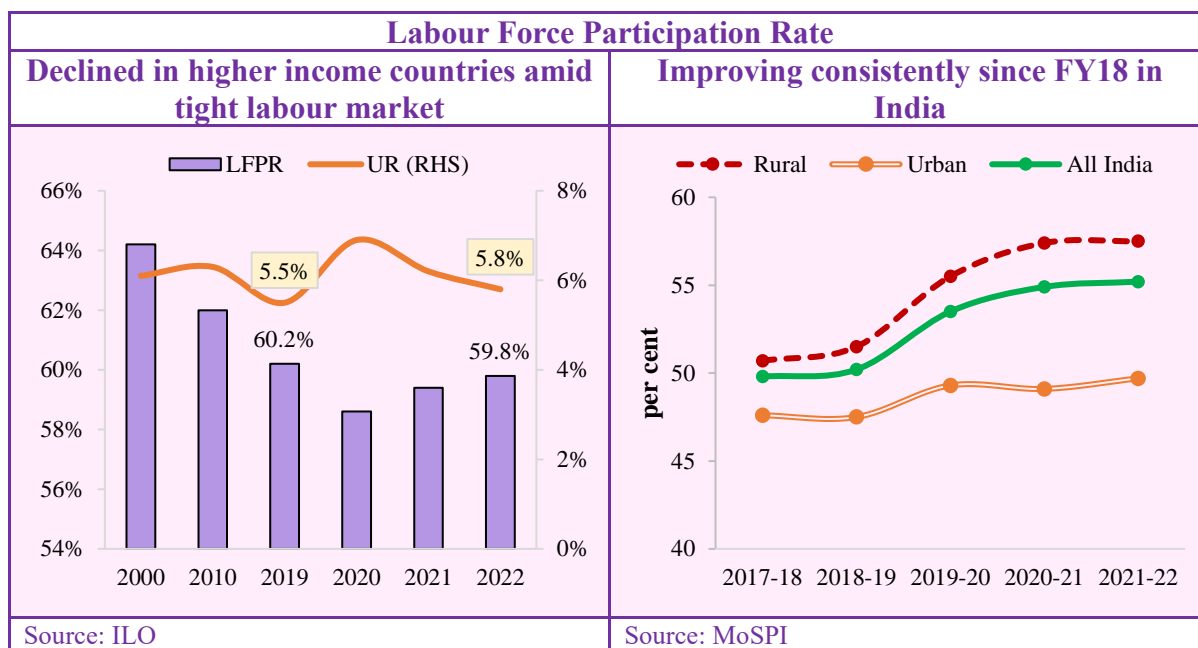
Ascending Employment Levels

10. The year 2021 saw a resumption of economic growth in several countries even as the pandemic manifested itself in several variants. The demand boost financed by massive fiscal stimulus increased growth in advanced economies. It also increased the demand for labour. The supply of output, however, did not respond in equal measure as the scarring inflicted by the pandemic reduced the size as well as the participation rate of the labour force. Consequently, the wage rate rose, setting in motion the wage-price spiral even before the onset of the war in Ukraine. The supply of labour has been gradually recovering in the advanced economies.

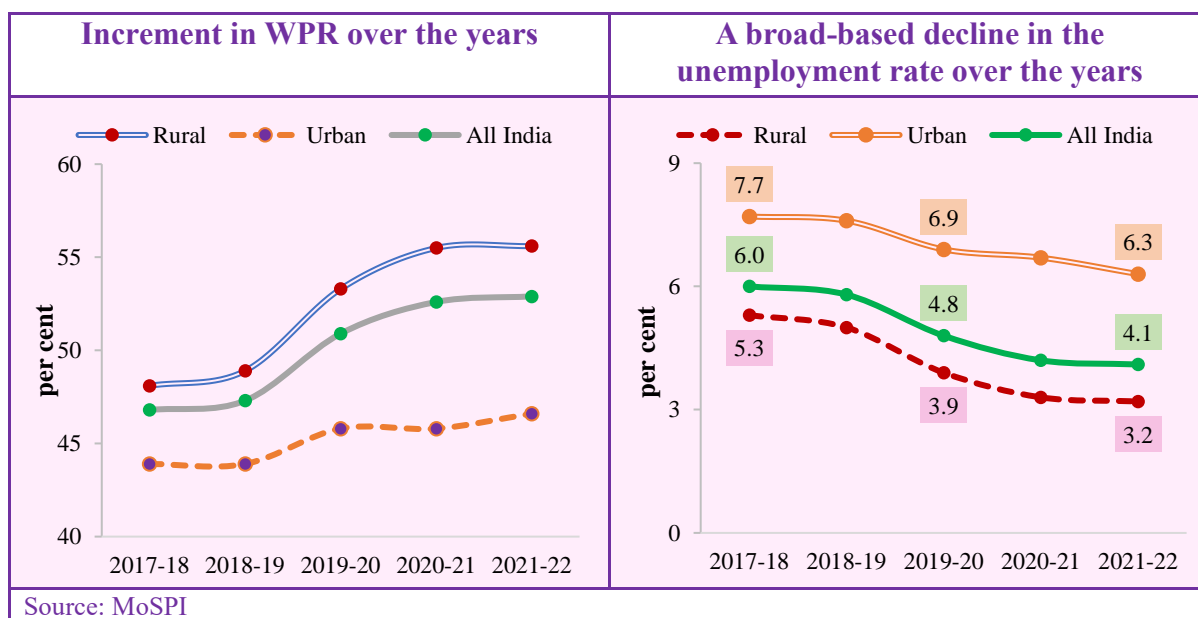
Complete Recovery of Labour Market in 2021-22

11. The ILO, in its World Employment and Social Outlook 2023, has stated that the recovery of global labour markets is not yet complete. This may be particularly true for the advanced economies. In so far as India is concerned, its labour force, as well as the labour force participation rate (LFPR), has risen through the pandemic, broadly in tandem with the pre-pandemic trend. The presence of a large unorganised sector that sustains on daily wages and income overcame the scarring effects of the pandemic to register a continuous increase in Worker Population Ratio (WPR) as well. Consequently, the annual rural-urban combined unemployment rate (UR) declined from 2017-18 to 2021-22 despite a brief period in 2020-21 when the pandemic-induced lockdowns temporarily increased the urban UR. In 2022-23, the urban UR declined in each quarter, reflecting steady growth in employment levels in the country. A declining urban UR has also subsumed growth in employment in the construction sector, as its strong revival has paved the way for rural migrants to find job opportunities in urban areas.

Labour markets in most advanced economies are tighter than they were prior to COVID-19, which is partly reflected in reduced labour force participation. The LFPR in high-income countries remained lower in 2022 at 59.8 per cent compared to 60.2 per cent in 2019. On the other hand, in FY22, India's LFPR was 55.2 per cent, higher than 54.9 per cent in FY21 and 53.5 per cent in FY20. Worker-population ratio also increased from 50.9 per cent in FY20 to 52.6 per cent in FY21 and 52.9 per cent in FY22. Strong economic growth, in part aided by calibrated fiscal policy and expansion of public capex, raised the worker-population ratio as the UR declined to a five-year low of 4.1 per cent FY 22, with a secular decline observed in both the rural and urban areas.



The declining trend in UR has been complemented by an across-the-board rise in the earnings of workers by around 4.7 per cent in both urban and rural areas, especially in the case of casual labourers, which are mostly employed in the construction sector. The construction sector expanded at a double-digit pace in FY22, contributing as the second largest employer after agriculture. Around 12.4 per cent of total workers were in the construction sector in FY22, up from 11.6 per cent in FY20.



Apart from sectoral growth, various government interventions also created employment opportunities. Aatmanirbhar Bharat Rojgar Yojana incentivised employers to create new employment along with social security benefits that led to the restoration of loss of employment during the pandemic. Garib Kalyan Rojgar Abhiyaan boosted employment and livelihood opportunities for returnee migrant workers. The availability of collateral-free loans with a 100 per cent credit guarantee for MSMEs also created employment in the small enterprises sector. Mahatma Gandhi National Rural Employment

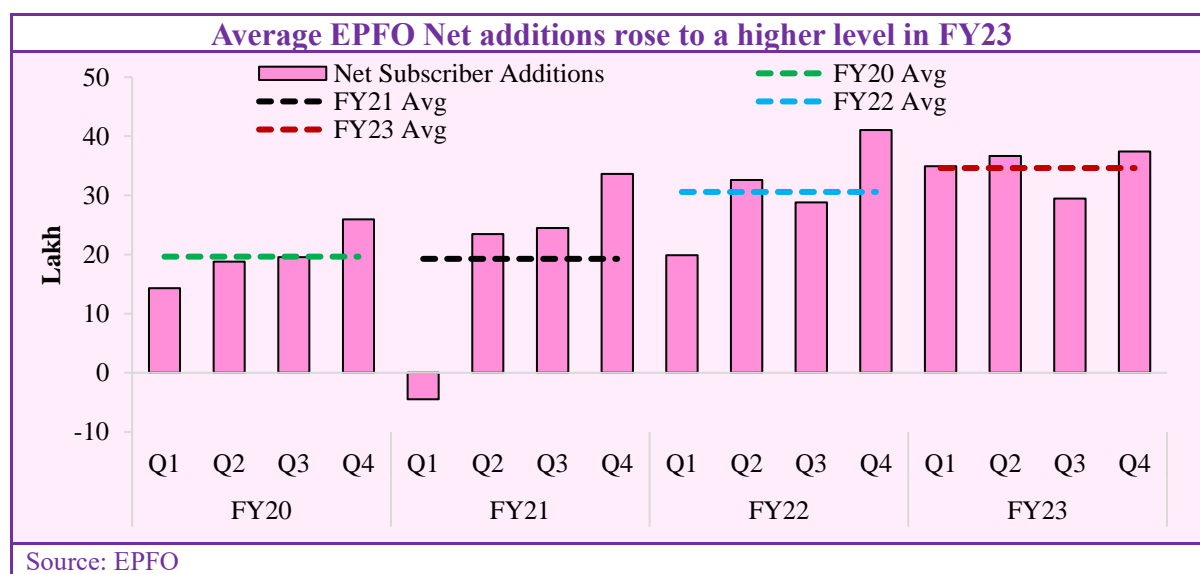


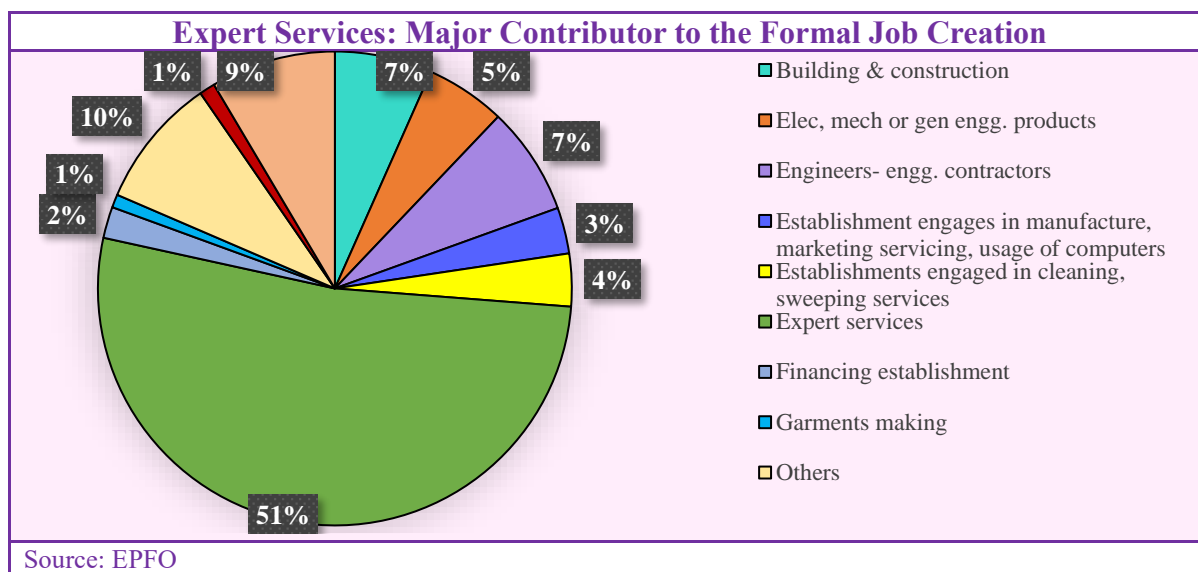
Guarantee Scheme (MGNREGS) enhanced livelihood security in rural areas by providing guaranteed wage employment. Under MGNREGS, “Works on individual’s land” significantly created assets to help households to diversify their sources of income and lift their supplementary incomes.

Growth with rising inclusivity

12. The rising employment levels, along with calibrated fiscal stimulus and a significant upscaling of public capex, created a demand boost in the Indian economy to accelerate growth from FY21 to FY23. As job creation played a critical role in boosting demand, it bespeaks the rising inclusivity in the growth of the Indian economy. Rising inclusivity is neither temporary nor transitional. It is now becoming deep-rooted with increasing job creation in the formal sector as the latter continues to expand on the back of Aadhaar, the e-shram portal for registration of unorganised workers, registration of MSMEs on the Udyam Portal and the implementation of GST, among others.

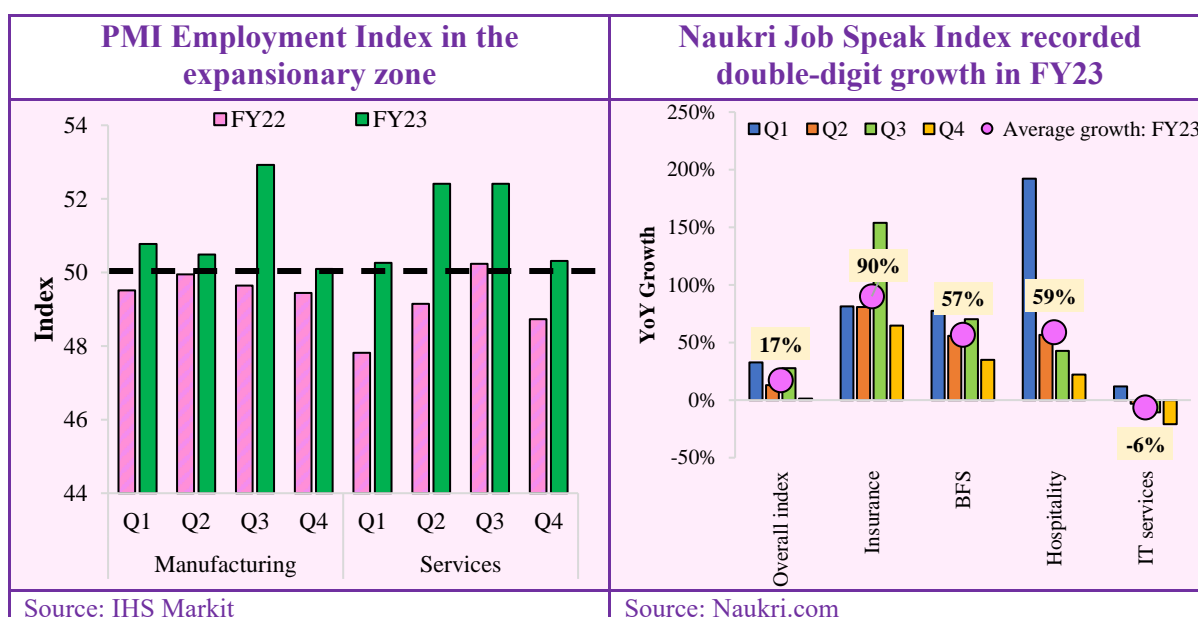
Job creation in the formal sector has been accelerating over the years, as reflected in a level shift of net monthly payroll additions under the Employees Provident Fund Organisation (EPFO), signalling increased formalisation of the economy. In FY23, net members added by EPFO reached a four-year high, growing by double-digits over the previous year. The annual trend across sectors reveals that the expert service sector (consisting of manpower suppliers, normal contractors, and security services, among others) contributed 51 per cent to formal job creation. Schools and financing establishments have also significantly increased their contribution to formal employment generation in FY23. On a YoY basis, however, net additions grew significantly in the first three quarters before moderating in Q4 of FY23. The moderation, in part, is explained by the slowing of employment generation in the Information Technology (IT) sector. This mirrors the global slowdown in IT hiring activity following the exuberant hiring during the pandemic period.





13. At a broader level of the manufacturing and services sector as well, rising job creation is evident. Growth in new business is seen to be behind job creation, particularly in the manufacturing sub-sectors of electronics, auto and auto ancillary and chemicals and the services sector of insurance, hospitality and banking. In the services sector, particularly, increased public awareness of health insurance products post-pandemic, rising business and leisure travel, and rapid expansion of digital banking services were the major factors contributing to new job creation.

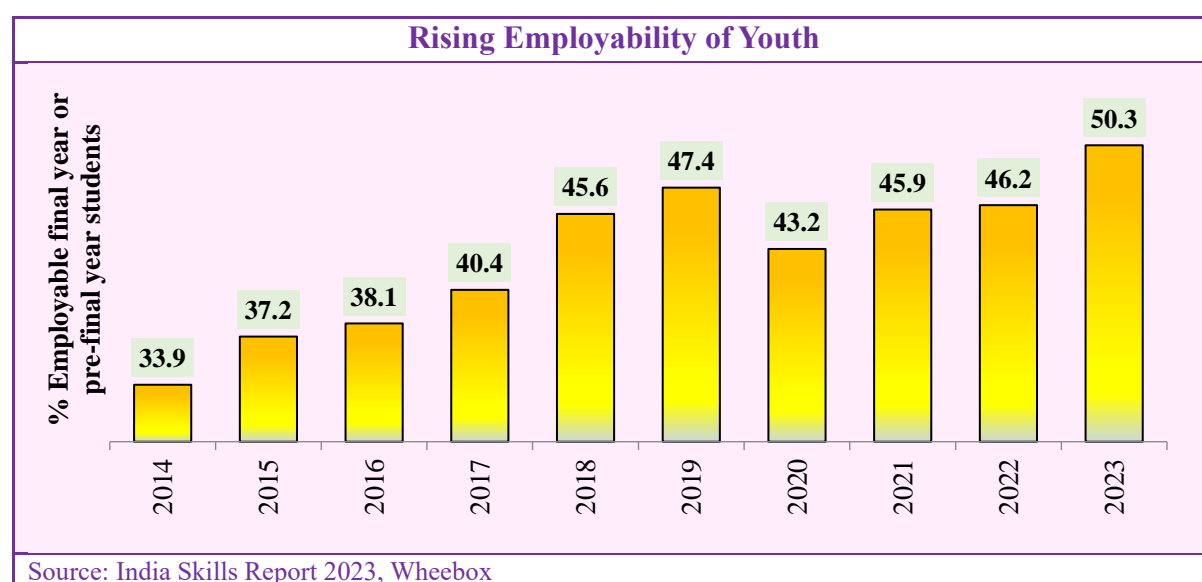
PMI sub-indices for employment in manufacturing and services moved into the expansionary zone in FY23. Average PMI sub-indices for Manufacturing and Services sector employment were higher in all four quarters of FY23 compared to FY22 values. A similar trend is observable in Naukri Job Speak Index, which doubled in FY23. The overall Naukri Job Speak Index increased across all four quarters of FY23, reflecting resilience in the overall hiring activity.





14. Rising employment levels in the formal sector have also been supported by improved education infrastructure and enhanced quality of education, which has increased the employability of the young labour force. According to India Skills Report 2023, the employable percentage of final-year and pre-final-year students increased from 33.9 per cent in 2014 to 50.3 per cent in 2023.

Wheebox (an online skill assessment venture run by Integrated Learning Solution Pvt Ltd) has been preparing the India Skills report since 2014 in partnership with CII, Taggd, AICTE, AIU, Sunstone, Pearson, AWS, and Economic Times. The Wheebox Employability Test assesses students' work readiness for India's changing employment market online, including technical and psychometric evaluation. In 2022, Over 3.75 lakh students were surveyed from various domains and educational backgrounds for WNET. Survey results were analysed based on educational domain, specific skill-oriented employability, state-specific employability, etc., to arrive at the national figure.



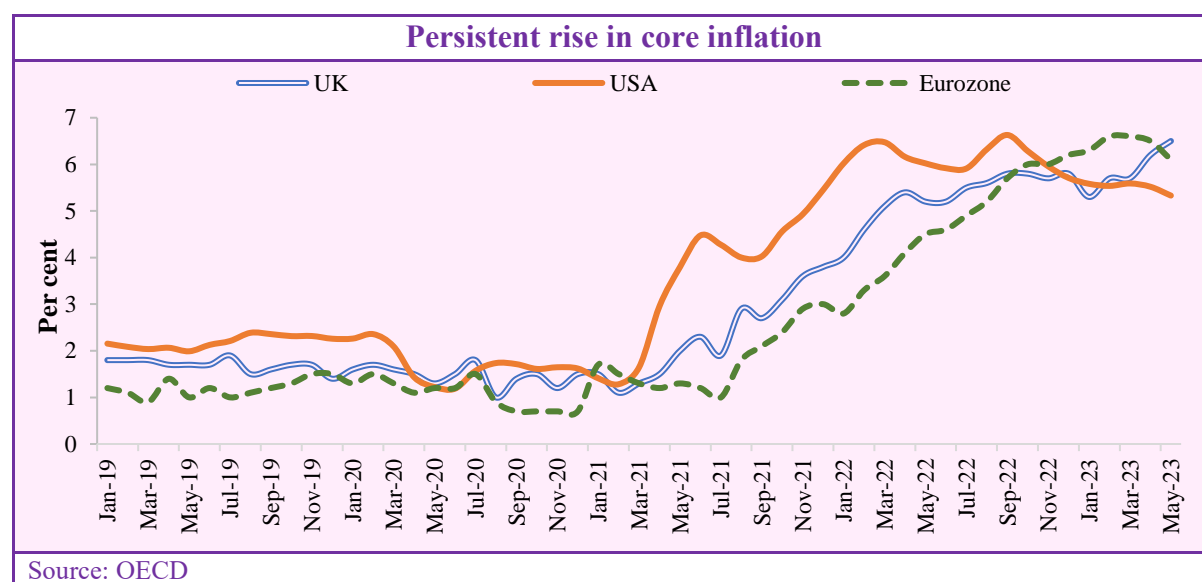
15. Going forward, employment levels are expected to remain buoyant, mainly driven by rapid digitalisation, technological advancement, and the expanding implementation of the PLI scheme, thereby creating employment avenues for both semi-skilled and skilled workers.

Rise and Fall of Inflation in India

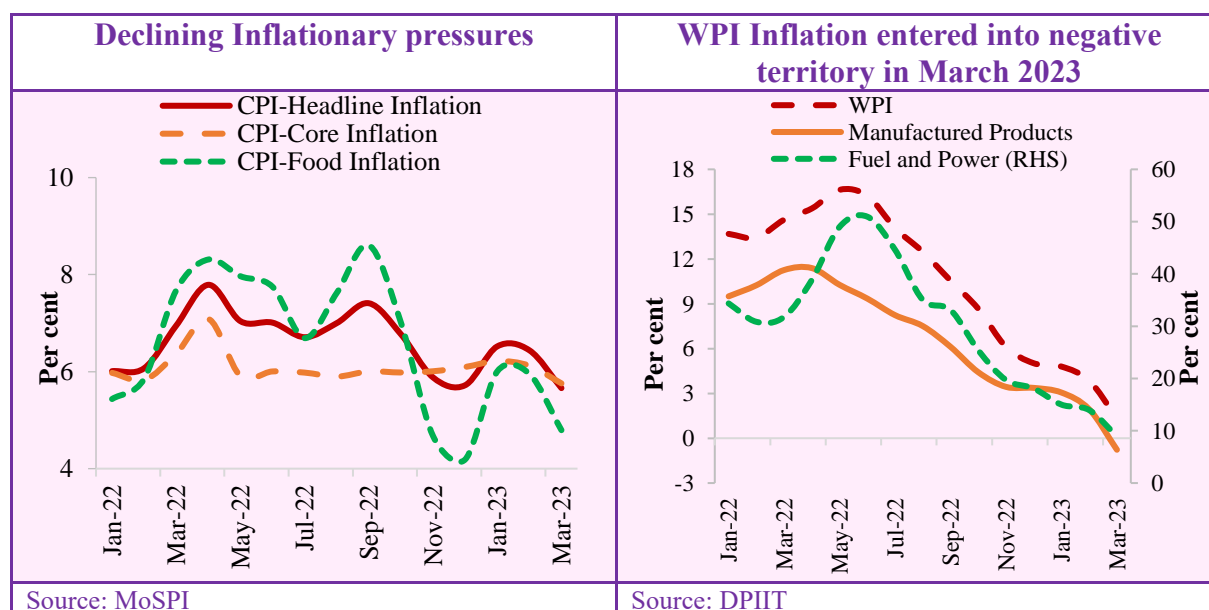
16. The year 2022 will be remembered for the high inflation afflicting most of the economies, advanced as well as emerging markets, soon after the relenting pandemic had allowed growth to resume. A localised geopolitical conflict assumed the proportions of a mighty global headwind disrupting supply chains the world over, causing an indiscriminate spike in commodity prices. And as a result, inflation soared to decadal highs and, for some nations, higher than the levels attained in the new millennium. Efforts to rein in inflation immediately commenced with the national governments implementing specific supply-side measures while their central banks undertook monetary tightening to restrain demand. These



efforts have started to bear fruits. With the softening of commodity prices, the headline inflation weakened in most of the economies in the early months of 2023. Encouraged by this development, the IMF, in its April update of the World Economic Outlook, projected global inflation to decline in 2023. Core inflation, however, is still persistent as some input costs remain high owing to local reasons, while those that have declined have more ground to cover.



17. The inflation narrative in India is broadly similar. In the first half of FY23, it reflected high imported inflation. Subsequently, the easing of global supply chains, specific government interventions, and monetary tightening have led to softening of headline inflation in the second half. A few domestic factors, like unseasonal rainfall, continue to keep upward pressure on the prices of some vegetables, such as tomatoes. However, these are more than counterbalanced by declining inflation in other food items leading to a moderation in food inflation in the second half of FY23. CPI-Core inflation remained downward sticky before it started to decline from March 2023.





CPI-Core inflation in India hovered around 6 per cent from May 2022 to February 2023 before declining to a 23-month low of 5.7 per cent in March 2023. This was driven by a decline in the ‘transport and communication’ component of miscellaneous inflation and the pass-through of rapidly declining inputs costs associated with the drastic fall of wholesale inflation. Wholesale price inflation started declining in June 2022 and kept falling steeply enough to a low of 1.3 per cent in March 2023. The decline has been very prominent since October 2022, with inflation in manufactured products shrinking steadily and fuel & power inflation also declining at a much faster pace. Even as core-inflation somewhat relented, food inflation also started to come down significantly from the third quarter of FY23. A perceptible decline in food inflation overbore the sticky core inflation and brought about a 100 basis points (bps) decline in headline inflation in Q4 of FY23 compared to Q1.

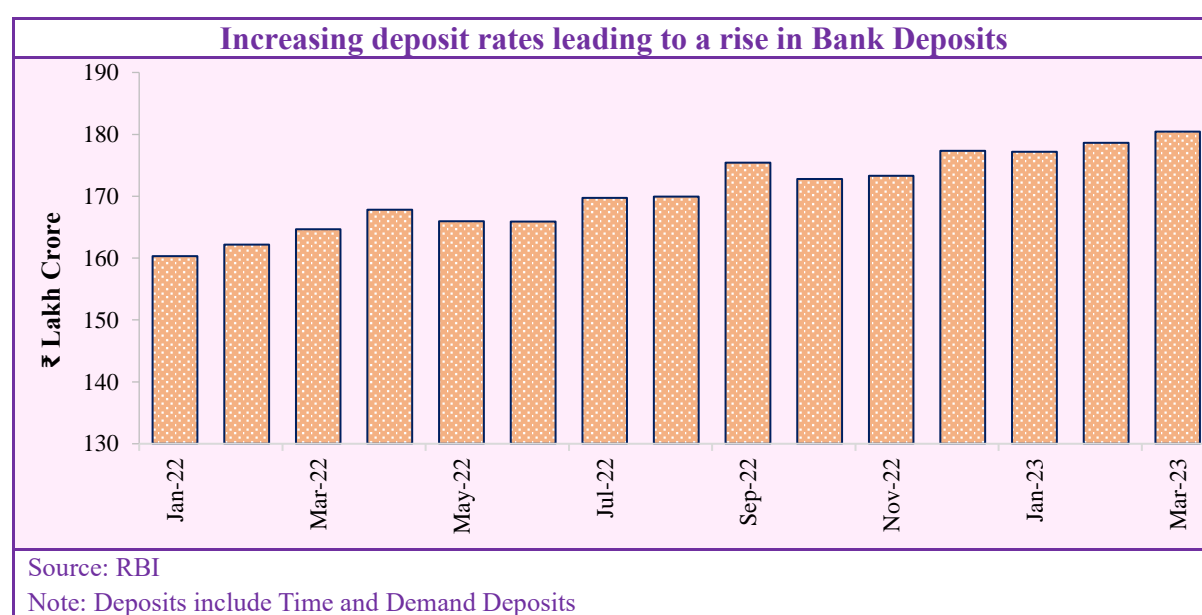
Government interventions to control inflation post Russia-Ukraine conflict

- **Fuel:** Excise duty on diesel and petrol was cut in May 2022 to bring down their retail prices. Additionally, over 90 million beneficiaries of the Pradhan Mantri Ujjwala Yojana were covered by a subsidy of Rs 200 per LPG cylinder for up to 12 refills in a year. The price for a commercial LPG cylinder was also reduced with effect from 1st June 2022.
- **Rice:** With effect from 9th September 2022, an export duty of 20 per cent was imposed on rice, brown rice, and semi-milled as well as wholly milled rice, except parboiled rice.
- **Onion:** A buffer stock of 2.5 lakh metric tonnes of onion was built in FY23 for calibrated release during the lean season. This helped to keep a check on onion prices, with onion inflation remaining in the negative range throughout FY23.
- **Oilseeds:** Custom duty and Agriculture Infrastructure and Development Cess (AIDC) were exempted on yearly import of 20 lakh metric tonnes in respect of crude soya bean and sunflower oil. Stock limits on all edible oils and oilseeds were imposed to prevent hoarding. Leading Edible Oil Associations were directed to ensure a reduction in the maximum retail price of edible oils to pass on the benefits of a fall in global edible oil prices to consumers. Owing to these measures, inflation in oils & fats declined from 8.6 per cent in H1:FY23 to (-)1.6 per cent in H2:FY23.
- **Pulses:** A buffer stock of pulses has been maintained for price stabilisation, and its calibrated release in the market helped restrain its inflation rate to 5.3 per cent in FY23. Also, measures like provisions to procure chana by States at discounted prices, the import of tur and urad under the free category, and zero per cent AIDC on masur contributed to keeping pulses price under control.
- **Wheat:** The lower production of wheat in FY22 led to reduced availability in the market, which resulted in its double-digit inflation since June 2022. To check the inflationary trend, the government decided to sell wheat in the open market. About 34 lakh MT of wheat was sold in the open market between February and March 2023. As a result, retail inflation in wheat slowed down from a peak of 25.4 per cent in February 2023 to 15.5 per cent in April 2023.



Monetary Policy Tightening

18. In FY23, the RBI kept up the pressure on monetary tightening, whose transmission was first seen in the lending rates. However, as the lower rate in most savings avenues amidst the low-interest rate regime from 2020 to H1:2022 incentivised individuals to move their financial savings into stock markets, banks faced competitive pressures and were forced to raise deposit rates. The increase in deposit rates thus went past the increase in lending rates from December 2022, about seven months after the initial increase in the repo rate. A simultaneous increase in the lending and deposit rates makes the monetary policy doubly effective. On the one hand, it restrains growth in spending by increasing the lending rate, and on the other, it curtails spending by attracting savings induced by an increase in the deposit rates.

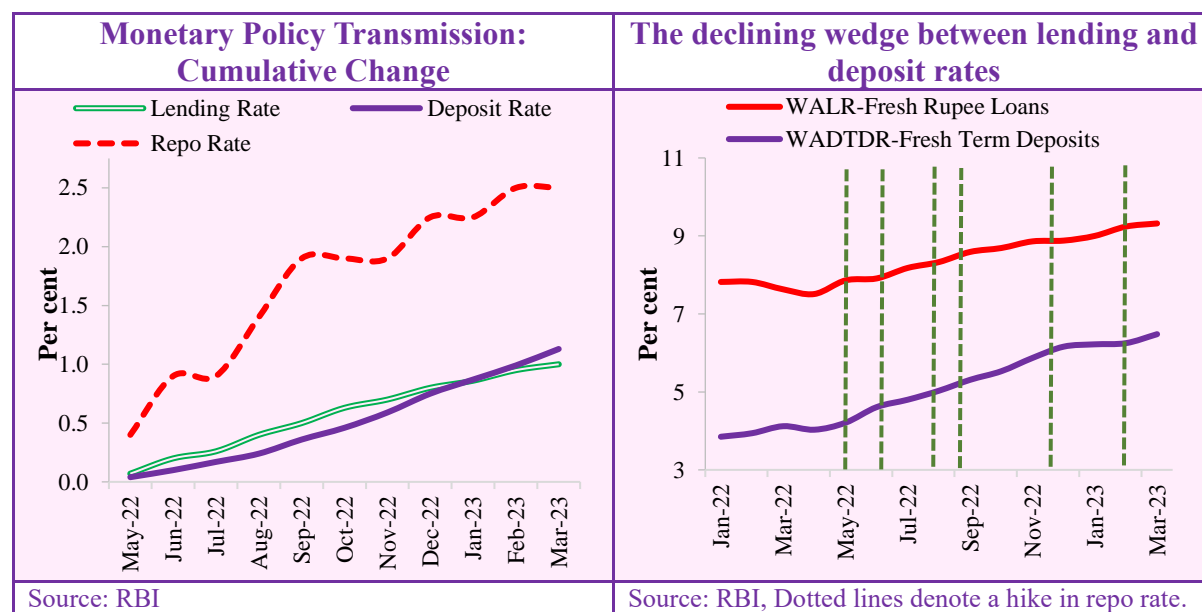


Various monetary policy measures were undertaken by RBI to contain inflation post the Russia-Ukraine conflict. Between May 2022 and February 2023, RBI hiked the repo rate six times, taking the policy rate from 4 per cent in April 2022 to 6.5 per cent in February 2023. RBI also introduced Standing Deposit Facility in April 2022 at 25 basis points (bps) below the repo rate as the new floor of the liquidity adjustment facility (LAF) corridor, thereby allowing effective liquidity management in a collateral-free manner. The width of the corridor was thus restored to its pre-pandemic configuration of 50 bps. In May 2022, the RBI also increased the cash reserve ratio (CRR) by 50 bps to 4.5 per cent, withdrawing excess liquidity from the banking system. Acknowledging the same, in June 2022 meeting, Monetary Policy Committee (MPC) dropped the word “accommodative” from the forward guidance, signalling the start of the monetary tightening cycle.

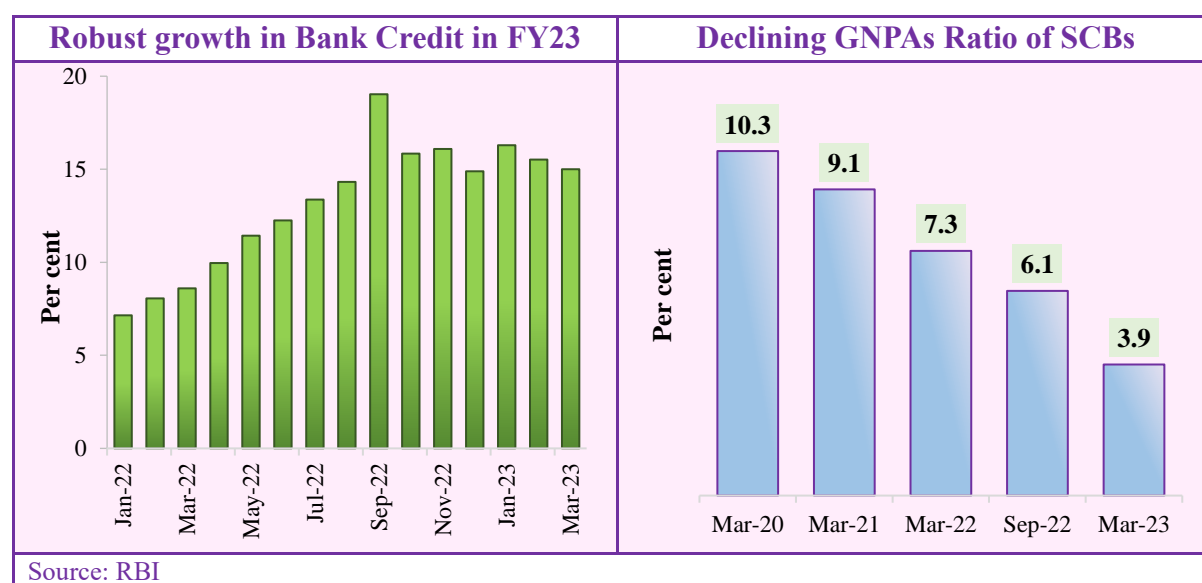
Lending and deposit rates of Scheduled Commercial Banks (SCBs) have increased in consonance with policy rate changes, reflecting moderation in surplus liquidity in the banking system and improved transmission of the monetary policy. During FY23, the Weighted Average Domestic Term Deposit Rate (WADTDR) of SCBs on Outstanding Rupee Term Deposits increased by 113 bps compared to a 100 bps rise in Weighted Average Lending Rate (WALR) on Outstanding Rupee Loans. This means that for



every percentage increase in repo rate, deposit rates have increased by 45 bps, more than the 40 bps increase in lending rates. Until December 2022, the transmission of a hike in the policy rate to lending rates exceeded the transmission to deposit rates. Post that, the trajectory changed, and deposit rates started increasing at a faster pace.



19. Despite the repo rate transmission of about 40-45 per cent, credit disbursement grew significantly in FY23 as elevated consumption demand and the induced investment demand on account of a favourable outlook kept the credit demand high. This contributed to increasing the profitability of banks whose bottom lines have already been improving with the declining Gross Non-Performing Assets (GNPA) ratio.



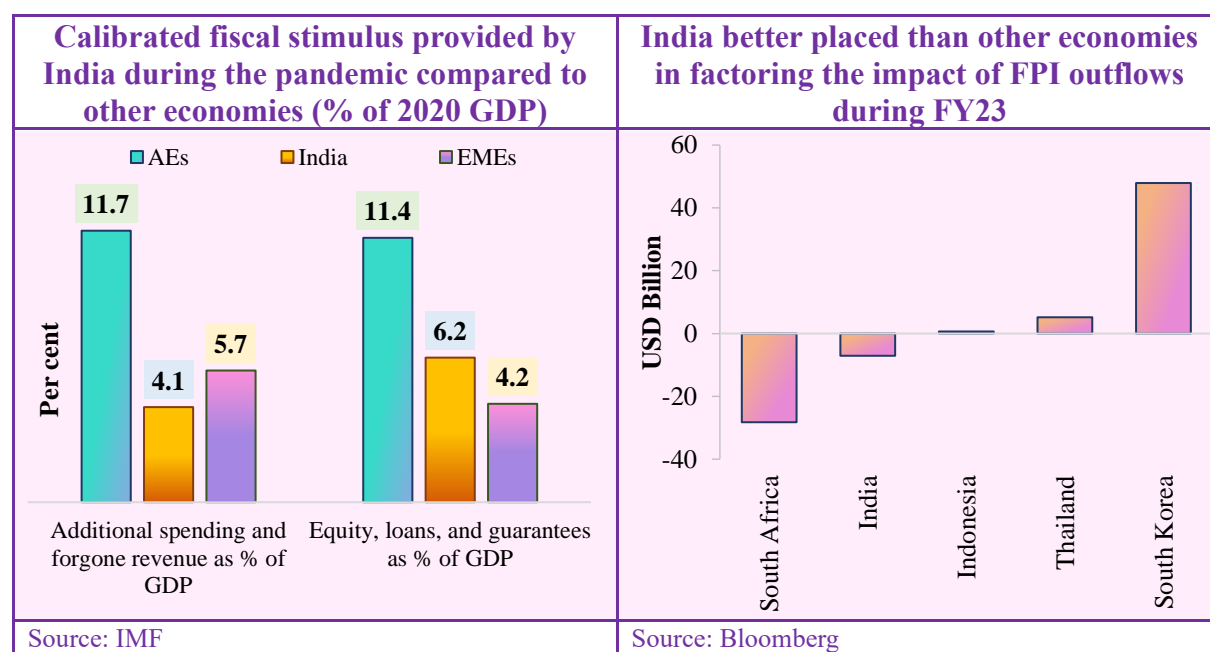
The Net Interest Margin, the difference between the interest rates bank charges and the interest rate it pays, an indicator of a bank's profitability, expanded until December 2022, and subsequently, though



remaining high, it started declining as banks were forced to raise deposit rates at a faster pace to mobilise deposits for credit creation. Other parameters of the bank's profitability also indicate significant improvement, as seen in their balance sheets in FY23, partly attributed to continued recovery in economic activities despite high inflation. Return on Equity (RoE) and Return on Assets (RoA) for SCBs posted notable increases during the year. Further, overall bank credit grew by 15 per cent in FY23 on an annual basis, with non-food credit growing at 15.4 per cent. At the same time, GNPA as a proportion of advances witnessed a declining trend and stood at 3.9 per cent in March 2023, down from 7.3 per cent in March 2022, mainly supported by various macroprudential policy measures, lower slippage ratio and swift recovery of bad loans under the Insolvency and Bankruptcy Code (IBC).

Unpredictable Impact of FPI on Monetary Policy

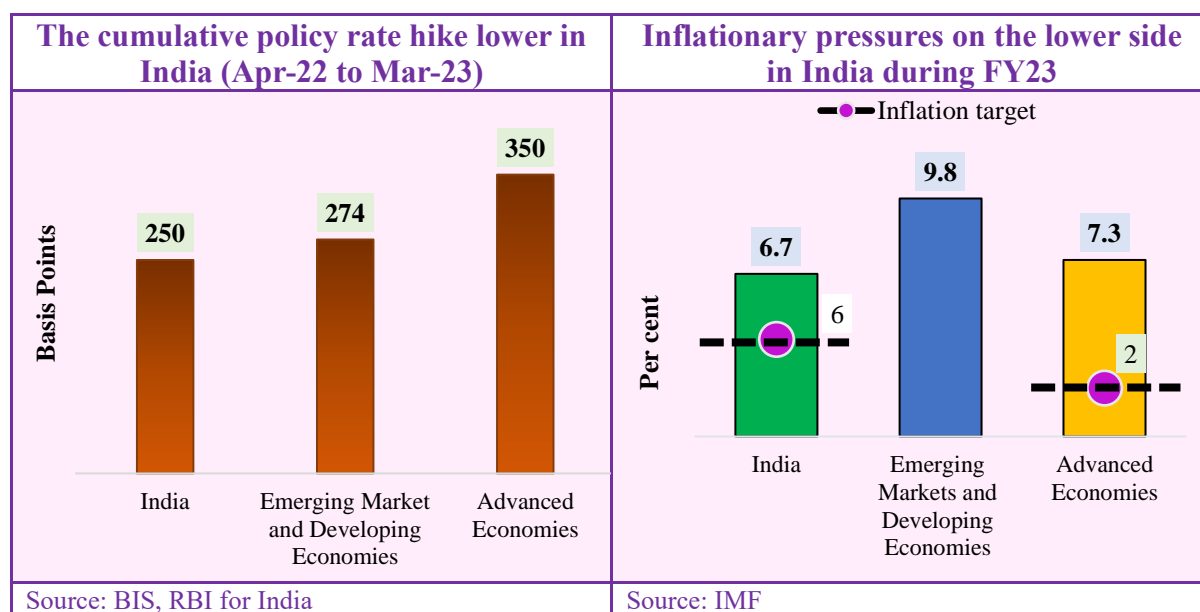
20. The movement of FPI in India's equity and debt markets has been volatile. The volatility had much to do with the increase in Fed rates. With an increase in Fed rates, FPI flows out, squeezing rupee liquidity in the economy, which in turn reinforces monetary tightening. When Fed pauses the increase in rates, FPI flows back, increasing rupee liquidity, thereby easing monetary tightening. The calibrated increase in the repo rates by RBI, however, absorbed the tightening impact of outflowing FPI on rupee liquidity. Expectedly, the increase in the repo rate by RBI since the outbreak of the pandemic is less than the repo rate hikes of the US Fed, as also the average hike for the advanced economies. It is even lesser than the average hike of emerging market economies, which indicates that India was able to better handle the impact of FPI outflows this time.



21. The impact of repo rate hikes, among others, on inflation has also been satisfactory for India. Despite the lower hikes in policy rates, India's inflation rate remained close to its target range, while those of EMEs and AEs remained far above their acceptable range even as the hike in policy rates in these countries was sharper. This has much to do with calibrated fiscal



stimulus provided by India during the pandemic as compared to major fiscal expansions undertaken by other countries.



22. Going forward, FPI flows are expected to become less volatile as Fed has indicated a prolonged pause in rate hikes. The RBI has also paused on increasing the policy rate in its last two MPC meets as retail inflation, along with core inflation, has started to decline. The monetary stance is thus likely to remain stable in the foreseeable future. The impact of El Nino on domestic food prices, and the possible stalling of pass-through of WPI into retail output, may, however, cause inflationary pressures to rise. However, the lagged impact of monetary policy on credit demand may dampen the incipient rekindling of inflation.

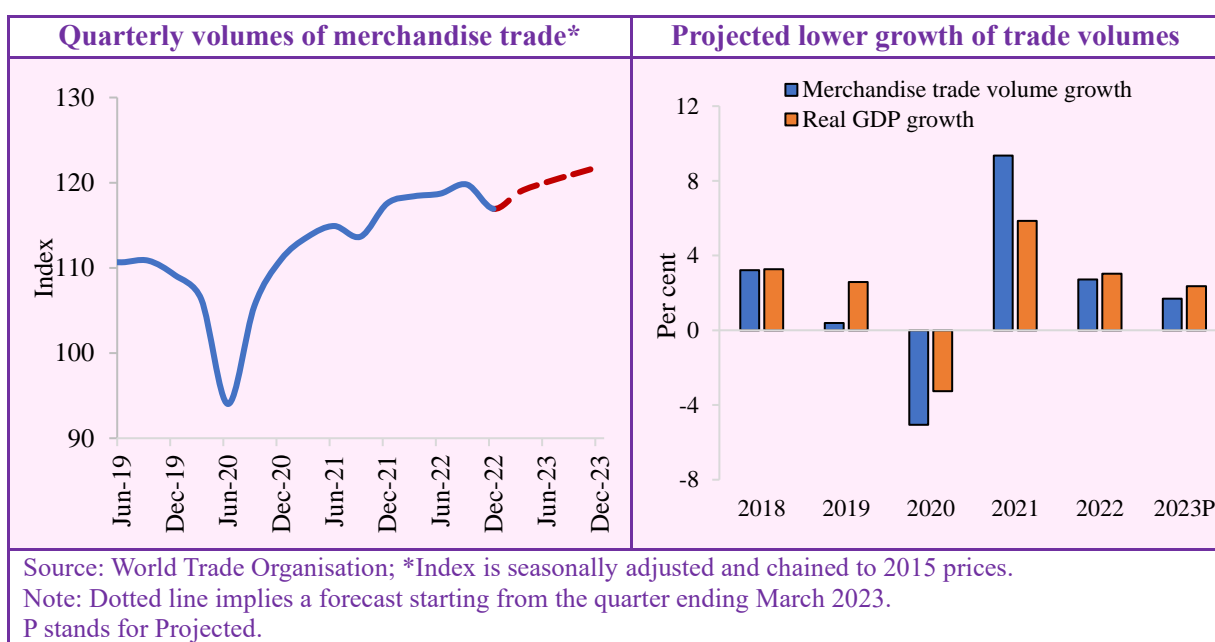
India's Resilient External Sector

23. Global merchandise trade in 2021 grew 9.4 per cent on the back of global growth of 5.9 per cent as the world economy recovered from the pandemic shock of 2020. The year 2022 was expected to take this process forward, but the fledgling growth recovery was thwarted by the outbreak of the Russian-Ukraine war. The war disrupted the global supply chains and sharply drove up commodity prices to stoke inflation. Growth suffered, and so did trade and even more so when central banks undertook significant monetary tightening to rein in inflation. Considering these developments, the WTO, in October 2022, projected a global trade volume growth of 3.5 per cent for the year 2022. The latest data, however, shows that trade volumes grew even slower at 2.7 per cent. The lower-than-expected growth was on account of a slump in trade following global demand showing the first signs of tepidness in the quarter ending December 2022. In this quarter, monetary tightening began to depress demand and is likely to continue doing so in subsequent quarters as further hikes in the policy rates are expected to bring down still high global inflation. Consequently, the growth in trade volumes may be even slower in 2023 and is projected at 1.7 per cent by the WTO.



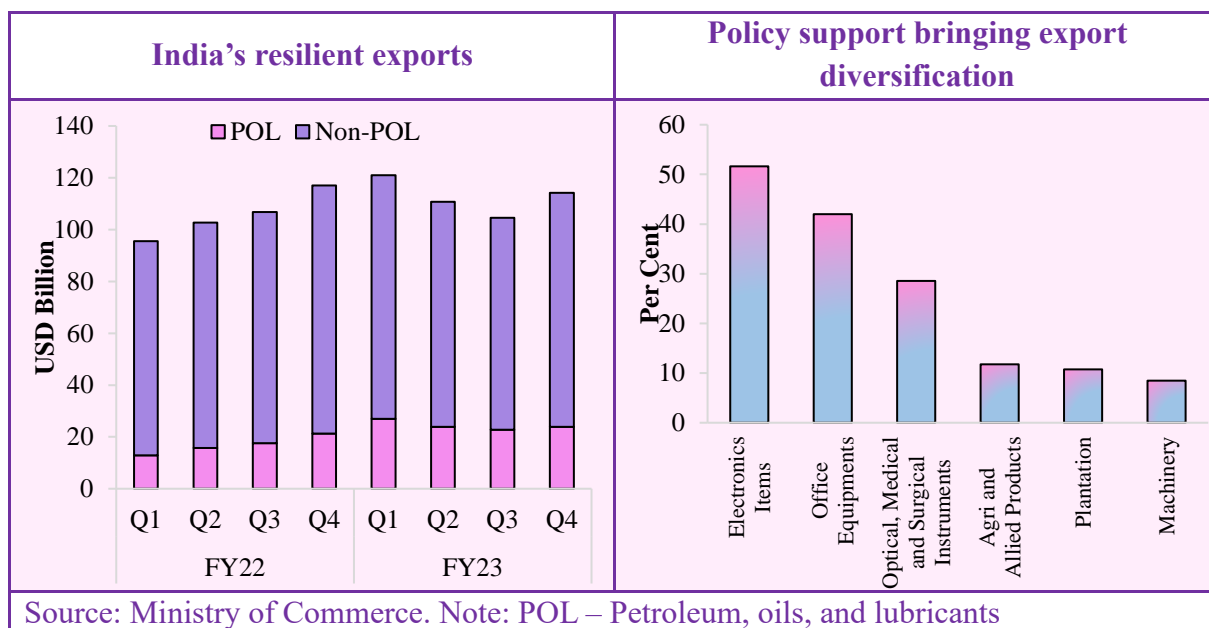
Robust services export and higher remittances narrow current account deficit

24. India's merchandise exports also aligned with the global trend. Its growth peaked in the April-June quarter of 2022 (Q1 of FY23) before the impact of the European war began to set in. Thereafter it moderated but was still resilient in FY23 to surpass the FY22 level. The volume growth of India's imports, on the other hand, continued to be high through FY23 to support the sustained growth of economic activity in the country. Yet the trade deficit improved in the second half of FY23 as international commodity prices fell to lower the cost of imports.

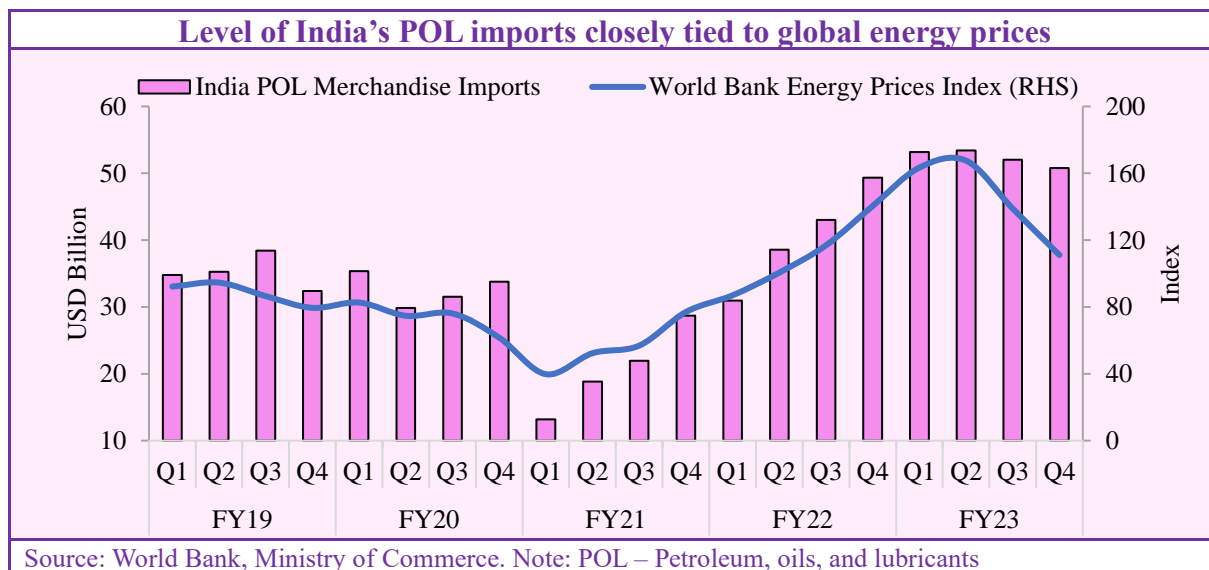


Merchandise exports posted double-digit growth in Q1 FY23. The global economic slowdown took its toll on exports in the second and third quarters. However, in the quarter ending March 2023, global economic activity accelerated, driven by growth in the global service sector². This provided positive momentum to India's merchandise exports in Q4 FY23. On an annual basis, merchandise exports grew by 6 per cent. A disaggregated analysis of the export data for FY23 suggests that significant strides have been registered in exports of electronic items, petroleum products, optical and medical surgical instruments, agriculture and allied products, leather and leather manufactured products, machinery, and transport equipment. The impressive growth of emerging commodity classes can be attributed to the policy support provided by the government to diversify the export basket. At the same time, India's food diplomacy following the Russia-Ukraine conflict resulted in increased demand for India's agricultural commodities in food-importing countries.

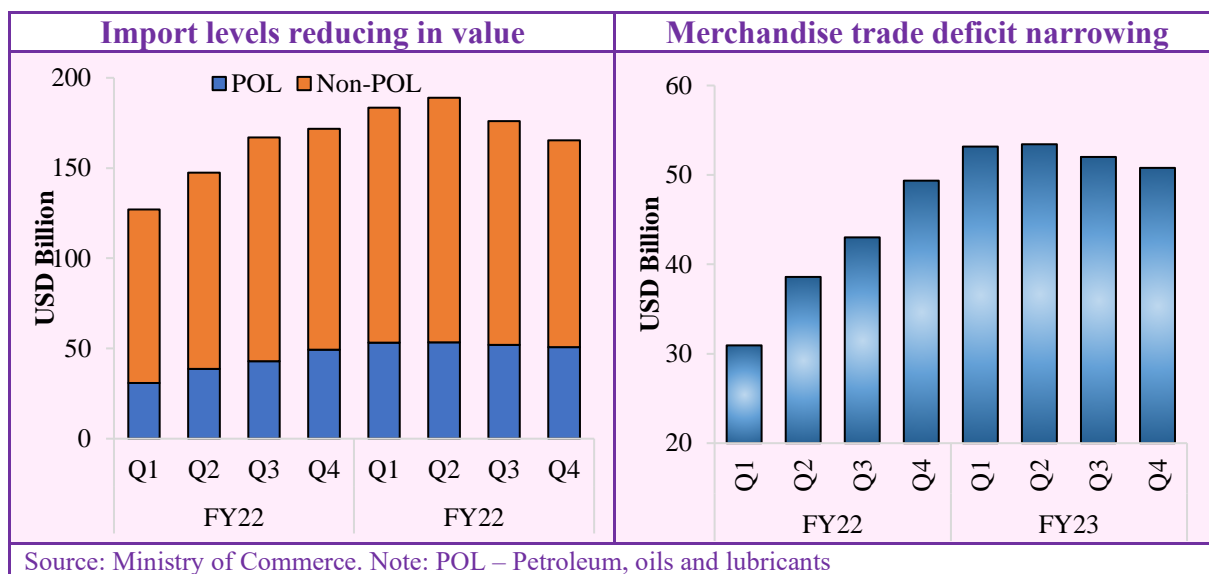
² https://cdn.ihsmarkit.com/www/pdf/4703914_4703896_0.1.pdf



Recovery in India's industrial activity in FY23 gave impetus to India's imports. This is evident in the increased share of energy products such as crude petroleum and coal in total imports in FY23 compared to FY22. However, higher energy imports in Q1 and Q2 of FY23 were also on account of elevated energy prices that characterised global energy markets. The last two quarters of FY23 saw energy prices trending downwards, leading to a decline in energy imports.

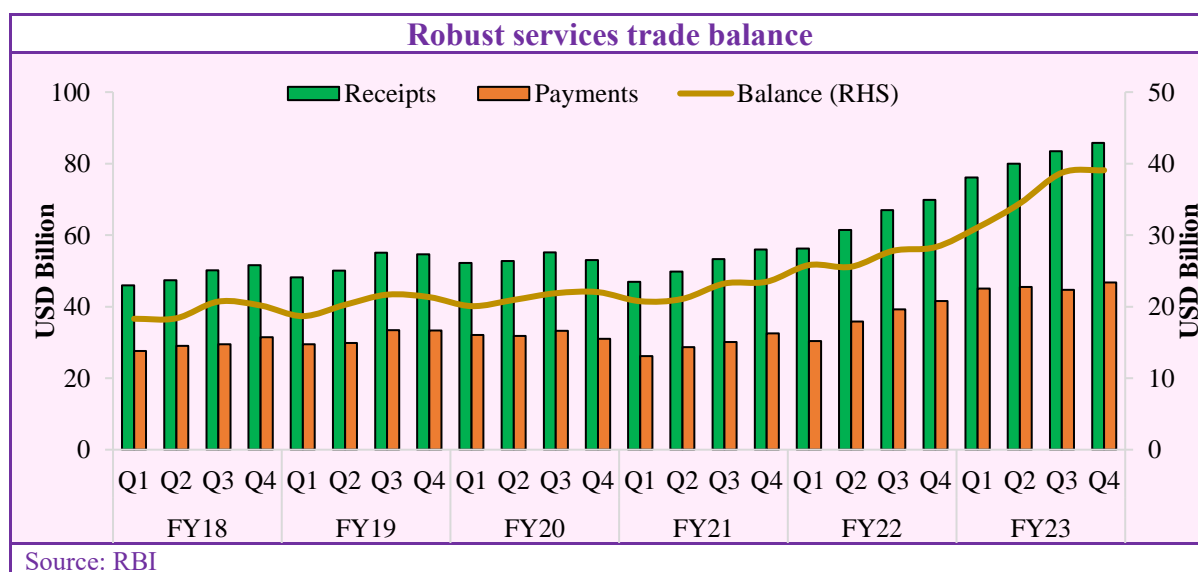


India's robust recovery amid elevated energy prices in the first two quarters of FY23 is evidenced by non-oil, non-gold, and silver imports growing YoY by 15.4 per cent while imports of crude oil and petroleum products grew at a much faster pace of 29.1 per cent, reflecting both the volume growth and rising energy costs. Owing to these developments, India's merchandise trade deficit widened to 8.5 per cent of GDP in H1 of FY23 before moderating to 7.5 per cent in H2.



25. Unlike the moderation in merchandise exports, services exports surged in FY23. The robust performance of services exports is also a reflection of how quickly India, through IT, adapted to a contactless world, enabling the country's highly skilled professionals to offer services online to the rest of the world. A strong services trade surplus and a moderating merchandise trade deficit combined to bring down the overall trade deficit of India in FY23.

The services trade balance improved over the year primarily on account of an improvement in services exports. Net services trade grew by a robust 33.3 per cent on a YoY basis in FY23. Unbundling of services, advances in technology, and rising demand for digitally deliverable services have allowed service importers across the globe and especially the developed countries, to take advantage of the growing Indian services sector. This is evident from the emergence of Global Capability Centres (GCC) in large numbers in India, through which the country's highly skilled workforce provides back-end support to multinational companies. In addition to this, India benefitted from the rising demand for digitally deliverable services. The services trade surplus was 4.2 per cent of GDP in FY23 as compared to 3.4 per cent in FY22.

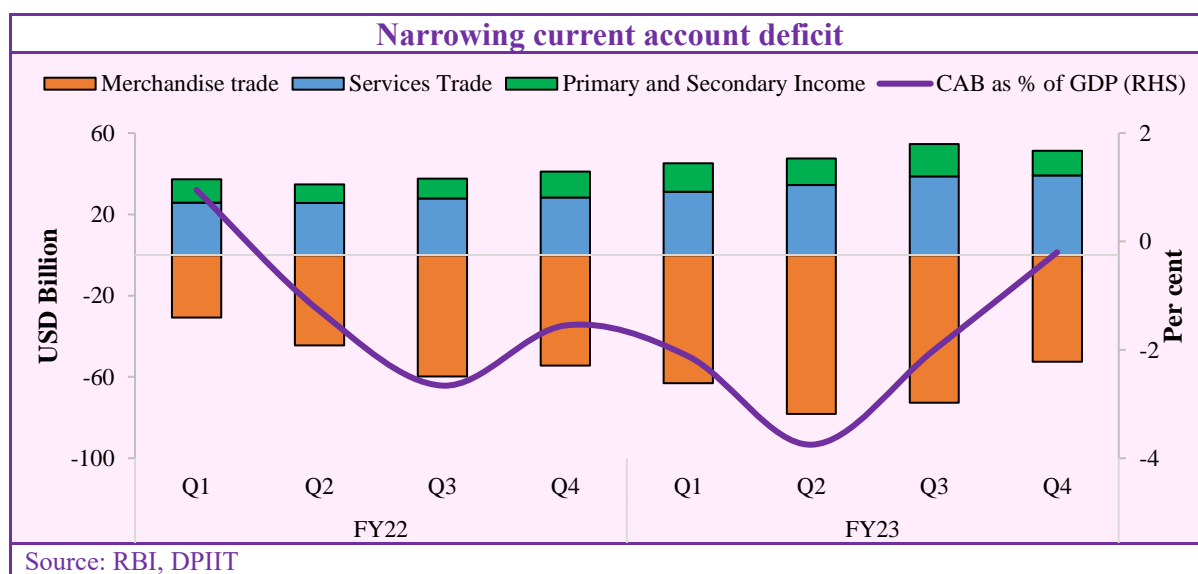




26. The developments in the merchandise and services trade helped the current account deficit (CAD) to narrow quickly towards the end of FY23, thereby strengthening the macroeconomic balance. Remittances played a key role in limiting the downside to the CAD in FY23. However, given the slowing global growth in the current fiscal, the growth of remittances may taper. Yet, the continued decline in global energy prices and sustained performance of services exports may further narrow CAD in FY24.

The second half of FY23 witnessed a narrowing of the merchandise trade deficit and the continuation of strong services export performance. This led to a decline in the CAD from 3.6 per cent of GDP in Q2 FY23 to 0.2 per cent in Q4 of FY23. Overall, CAD stood at 2.0 per cent in FY23, higher than 1.2 per cent in the previous year due to elevated commodity prices in the first half of the year.

Significant growth of remittances has also contributed to the narrowing of CAD. The RBI has pegged India's remittances at US\$ 97.8 billion in CY2022, a YoY growth of 25.7 per cent. The World Bank's Migration and Development Brief, June 2023, estimates this to represent about 63 per cent of South Asia's total remittance flows. Two factors contributed to this unprecedented level. Almost 36 per cent of India's remittances are sourced from highly skilled and largely high-tech Indian migrants in three high-income destinations (United States, United Kingdom, and Singapore), where the post-pandemic recovery led to tight labour markets and the consequent wage hikes boosted remittances. In addition, other high-income destinations of India's skilled migrant workforce also enjoyed favourable economic conditions. At the same time, high energy prices favored the employment and incomes of the low-skilled Indian migrants to the Gulf Cooperation Council (GCC) countries. The GCC governments' special measures to curb food price inflation also shielded migrants' remitting potential leading to further remittance inflows. The remittance inflows from the GCC countries thus also soared in 2022, accounting for about 28 per cent of India's total remittance inflows.



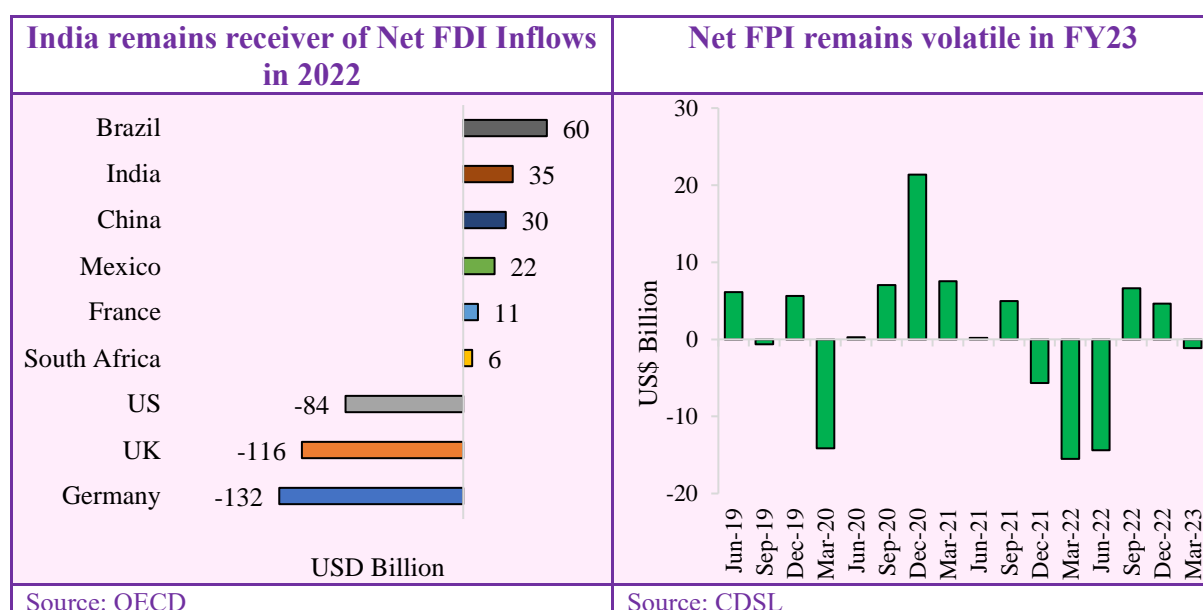


Capital flows remained volatile, with FDI inflows higher than peer EMEs.

27. The CAD is sustainable if it is financed by normal capital inflows. However, in 2022, capital flows to the EMEs remained subdued and volatile as geopolitical uncertainties rose and global economic activity weakened. Yet India continued to be comforted by a net FDI inflow even as most of the EMEs and AEs were challenged by net FDI outflows. The contrasting capital flows can be attributed to strong macroeconomic fundamentals and the supportive FDI policy of India, which have characterised the country as an attractive and investor-friendly destination. A global slowdown in investment flows to EMEs led to India's net FDI inflows dipping in FY23.

28. Global uncertainties also made foreign portfolio investors (FPI) pull out capital from EMEs, including India. However, FPI outflows from India in the first quarter of FY23 turned into inflows from the second quarter onwards before adverse developments in the banking sectors of the US and Europe again led to a mild FPI outflow in the fourth quarter. Overall, the quantum of FPI outflow narrowed in FY23 compared to FY22, reflecting a strengthening of faith in India's impressive economic credentials.

FDI flows to India bore the brunt of inflationary pressures and tighter monetary policy abroad. While Gross FDI, which reached a record high of US\$ 84.8 billion in FY22, moderated in FY23 by 16 per cent on a YoY basis, net FDI declined by 27.4 per cent in FY23 on a YoY basis. However, this phenomenon is not unique to India, as net FDI inflows to EMEs declined by 36 per cent in 2022, as per OECD statistics. Also, geopolitics has dominated geography, with investors "friend shoring" the FDI by increasing investments in countries which are geopolitically aligned to each other, thereby leading to fragmentation in FDI flows across the globe indicated in IMF's World Economic Outlook (April 2023). Hence, India needs to watch FDI data closely and continue to take measures to facilitate FDI inflows. Last-mile infrastructure issues, labour availability and measures to facilitate large capacity creation will be needed. This policy space may need India's increasing attention in the coming months and years.



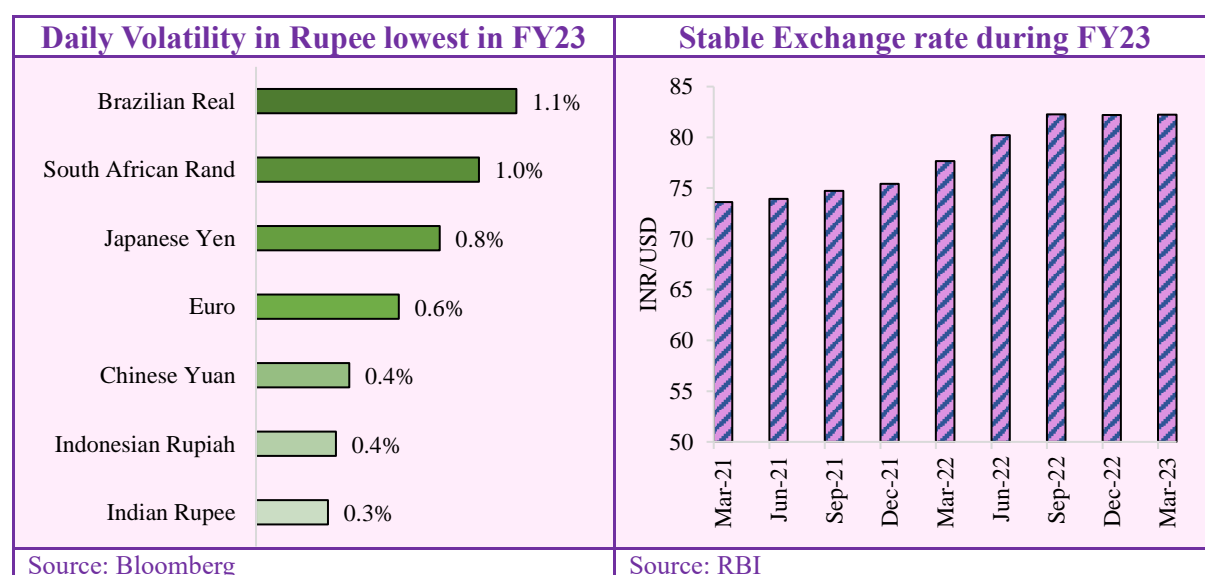


FPI became net sellers in the Q1 of FY23 with an outflow of US\$ 14.3 billion. However, the second and third quarters of FY23 witnessed an inflow of US\$ 11.2 billion, with Q4 observing a smaller quantum of outflow of US\$ 1.2 billion. On an annual basis, net FPI outflows moderated from US\$ 16 billion in FY22 to US\$ 5.5 billion in FY23. The trend until mid-June 2023 indicates that FPIs find Indian markets attractive despite globally tighter financial conditions.

Stable Rupee with lower volatility relative to EMEs and AEs

29. The trajectory of the ₹ in FY23 was influenced by factors such as elevated Brent oil prices, high import dependence and capital outflows driven by tightened global financial conditions. Yet, the performance of the ₹ has been resilient, exhibiting orderly adjustment with lower volatility relative to many other EMEs and AEs. During the first half of the year, the ₹ was under pressure before it rebounded later in the second half and remained stable within a narrow range. The recovery of the ₹, among other reasons, was supported by the softening of Brent oil prices and improvement in the current account balance.

The Indian rupee depreciated by 8.5 per cent in FY23. However, the daily volatility in INR stood at 0.3 per cent, much lower compared to other currencies of EMEs and AEs, such as the Brazilian Real (1.1 per cent) and South African Rand (1.0 per cent), Japanese Yen (0.8 per cent), Euro (0.6 per cent), Chinese Yuan (0.4 per cent), Indonesian Rupiah (0.4 per cent). Following the movements in the nominal exchange rate, the 40-currency real effective exchange rate (REER) also depreciated during the year. On a quarterly basis, after depreciating for three quarters, the rupee has recovered and appreciated by 0.7 per cent in Q4 of FY23.

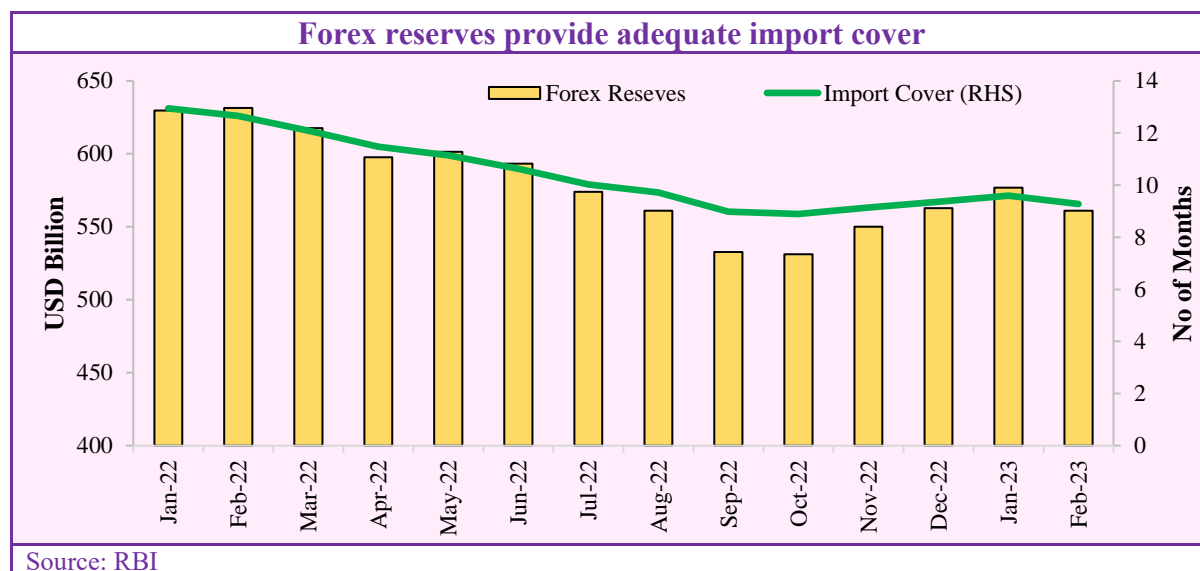


Comfortable level of forex reserves

30. Forex reserve holdings declined in the first half of FY23, going into the financing of a widening CAD and rising capital outflows. The subsequent narrowing of CAD and FPI inflows led to the rebuilding of the reserves. The FY23 closed with India becoming the 5th largest



forex reserve holder in the World. Forex levels are adequate to provide an import cover of ten months, which is a comfortable cushion against external shocks. Going forward, continued narrowing of CAD and rising FPI inflows enabled by non-aggressive posturing by the Federal Reserve will further build the forex reserves.



Outlook for the external sector

31. The impending downside risks to India's exports include the European Union's introduction of the Carbon Border Adjustment Mechanism (CBAM), for which reporting of carbon content in exports to the EU would be required beginning 1st October 2023; continued uncertainty about the Russia-Ukraine conflict; and polarisation risks arising out of the prevailing geopolitical situation reflected in the possible adoption of trade-restrictive measures. Further, foreign direct investment flows may also be impacted by political distance more than geographical distance, as IMF research points out.

32. Counterbalancing the downside risk is the easing of supply chain disruptions, as seen in the upward trend in globalised container trade monitored by the Kiel Trade Indicator. Further, moderating inflation across countries is expected to provide some room for policymakers to halt their monetary policy tightening or slow the pace and magnitude of tightening.

33. Trade agreements presently under negotiation with the advanced economies, the new foreign trade policy, the digital revolution in payments and trade facilitation, trade promotion activities, improved trade credit, and the promotion of districts as export hubs are expected to increase the global market share of India's exports.

34. Prices of commodities, particularly those of energy commodities, are expected to remain at their relatively lower levels in the remaining months of 2023. This will aid in keeping India's merchandise trade deficit narrow. While the effects of an exacerbation of recessionary tendencies on services trade and remittance growth are yet to be seen, their levels are expected



to hold broadly steady. In this context, India's current account deficit is expected to remain narrow through FY24.

Fiscal policy closely aligned to delivering macroeconomic stability in an environment of geopolitical uncertainty

35. Fiscal policy across economies has undergone major swings in the recent past, with the governments addressing the growth and price outcomes of the pandemic and geopolitical shocks. The pandemic, in general, had caused the fiscal deficits to expand as governments, attempting to recover the lost output, reinforced the spending power in the economy to give growth a demand push. As the pandemic waned in 2021 enabling the recovery of the global economy, governments, particularly those constrained for fiscal room, took steps towards fiscal consolidation. The consolidation efforts, however paused no sooner than they had started as the new challenge of price spirals following the outbreak of the Russian-Ukraine conflict necessitated additional spending on welfare measures and cuts in the tax rates. These measures constricted the fiscal room even further than caused by the pandemic as several economies were yet to fully complete the recovery process, further challenged by monetary tightening undertaken by central banks to rein in inflationary pressures.

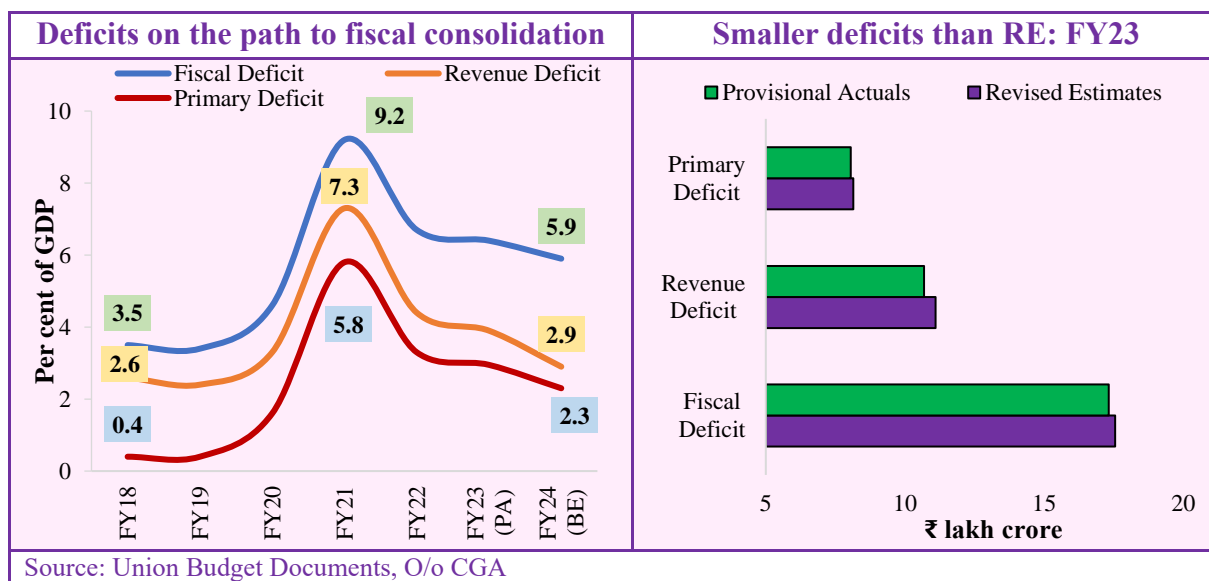
Union Government closer to the glide path of reaching fiscal deficit target

36. To mitigate the inflationary impact of the geopolitical shocks, the government of India implemented several measures ranging from duty cuts to enhancing the outlays on subsidies. The objective was to minimise the pass-through of high prices on vulnerable groups and businesses with a view to providing them with a safety net. While doing so, the government ensured that its enhanced outlay on capital expenditure was not compromised, which was needed to give an investment thrust to the economy. The capital outlay was protected in FY23 by rationalising revenue expenditure. This contributed to bringing down the fiscal deficit of the Union Government from 6.7 per cent in FY22 to 6.4 per cent in FY23. The fiscal consolidation has brought the Union Government closer to the glide path of reaching the fiscal deficit target of 4.5 per cent by 2025-26.

The government implemented multiple fiscal measures to soften the impact of inflationary pressures. It reduced the excise duties on petrol and diesel in two phases – a ₹5 cut on petrol and a ₹10 cut on diesel in November 2021, and a ₹8 reduction on petrol and a ₹6 reduction on diesel in May 2022. The duties on naphtha, propylene oxide and polymers of vinyl chloride have been reduced from 2.5 per cent to 1 per cent, 5 per cent to 2.5 per cent and from 10 per cent to 7.5 per cent, respectively, on 21 May 2022. In the same month, duties on major inputs, ferronickel, coking coal, PCI coal, coke and semi-coke, were reduced to zero per cent. Similarly, it waived the customs duty on imported cotton in April 2023, while the customs duty on certain critical chemicals such as methanol, acetic acid and heavy feedstocks for petroleum refining was reduced in Union Budget 2022-23. To counter the rising prices of fertiliser prices, the government enhanced the outlay on the fertiliser subsidy. Data from the CGA reveals



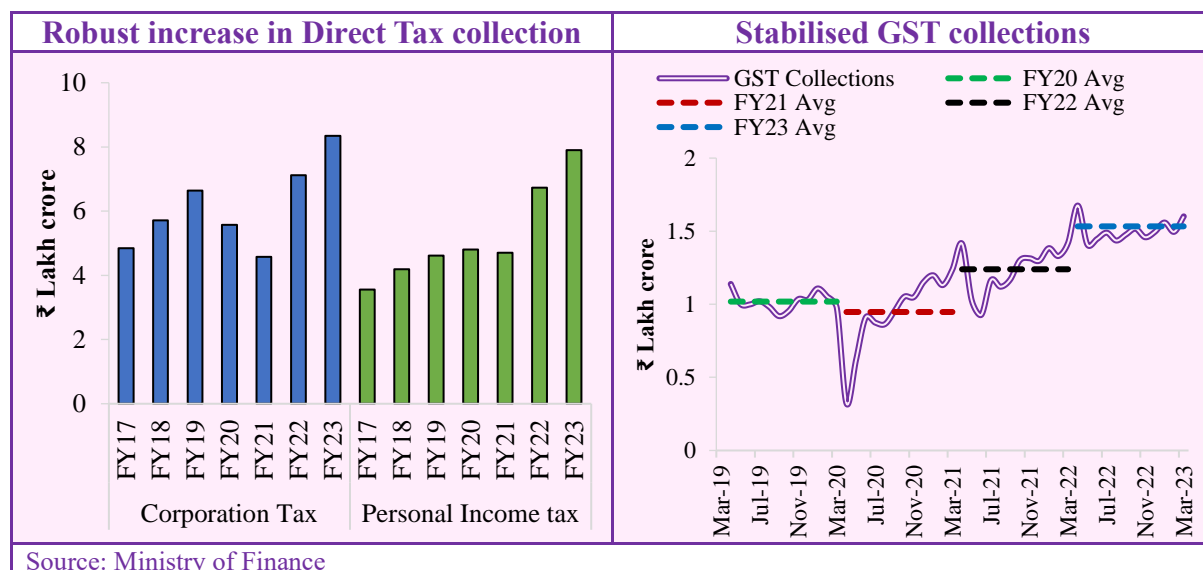
estimates that the Urea subsidy and the nutrient-based fertiliser subsidy were 7 per cent and 21 per cent higher, respectively than the revised estimates stated in the Budget 2023-24.



Buoyant revenue helped Govt to achieve Fiscal Target

37. The consistent buoyancy in revenues has supported the Government in achieving its fiscal targets. The robust revenue receipts in FY23 were facilitated by better-than-anticipated economic performance and high buoyancy in direct taxes and goods and services Tax (GST). Higher growth in direct taxes and GST collections relative to the growth in GDP is a testimony to the effectiveness of efforts taken by the government over the years to expand the tax base and enhance tax compliance. Despite a reduction in corporate tax rates, corporation tax collection in the past two years has been strong, driven by higher profits and healthy growth in economic activity. At the same time, the GST system has stabilised over the last six years, thereby becoming a pivotal source of revenue for central and state governments. The custom duty collections have also shown decent growth despite a cut in the duties to control the inflation impact on edible oils, pulses, cotton, steel, etc. Additionally, the non-tax revenue receipts for FY23 have also exceeded the revised estimates, driven by higher interest receipts and better performance of public sector enterprises leading to higher distribution of dividends and profits.

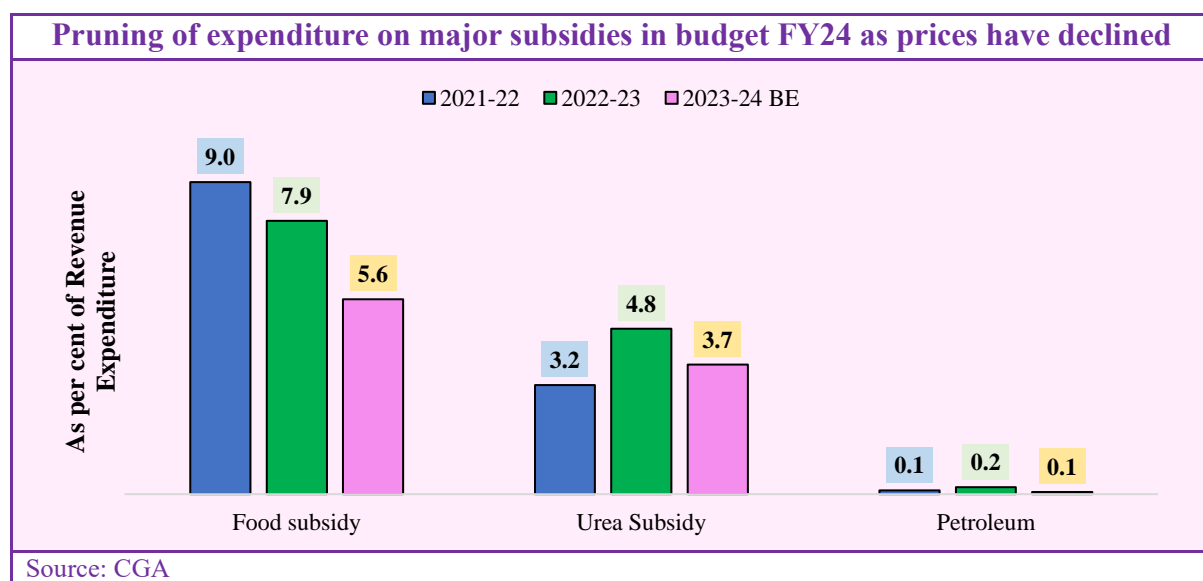
The gross tax revenue registered a YoY growth of 12.7 per cent in FY23, driven by robust growth in the direct taxes and GST. Direct taxes, including income and corporate tax, increased by 20 per cent and 16 per cent, respectively. At the same time, the gross GST collections grew by 21.4 per cent. Average monthly collections have also risen from ₹1.2 lakh crore in FY22 to ₹1.5 lakh crore in FY23.



Increased revenue expenditure to cushion impact on vulnerable sections arising from external exogenous shocks

38. On the expenditure side, geopolitical shocks stretched the revenue expenditure requirements of the government in FY23, mainly led by the jump in the subsidy expenditure as international prices of food, fertilisers and fuel shot up. However, as supply chain disruptions are expected to ease, the government has budgeted lower subsidy expenditure for FY24.

The total subsidy expenditure shot up to 15.4 per cent of revenue expenditure in FY23, higher than 13.9 per cent registered in the previous year. However, as per budget estimates, subsidy expenditure is projected to decline to 10.7 per cent in FY24 on the back of an expected decline in the international prices of food, fertilisers and fuel.

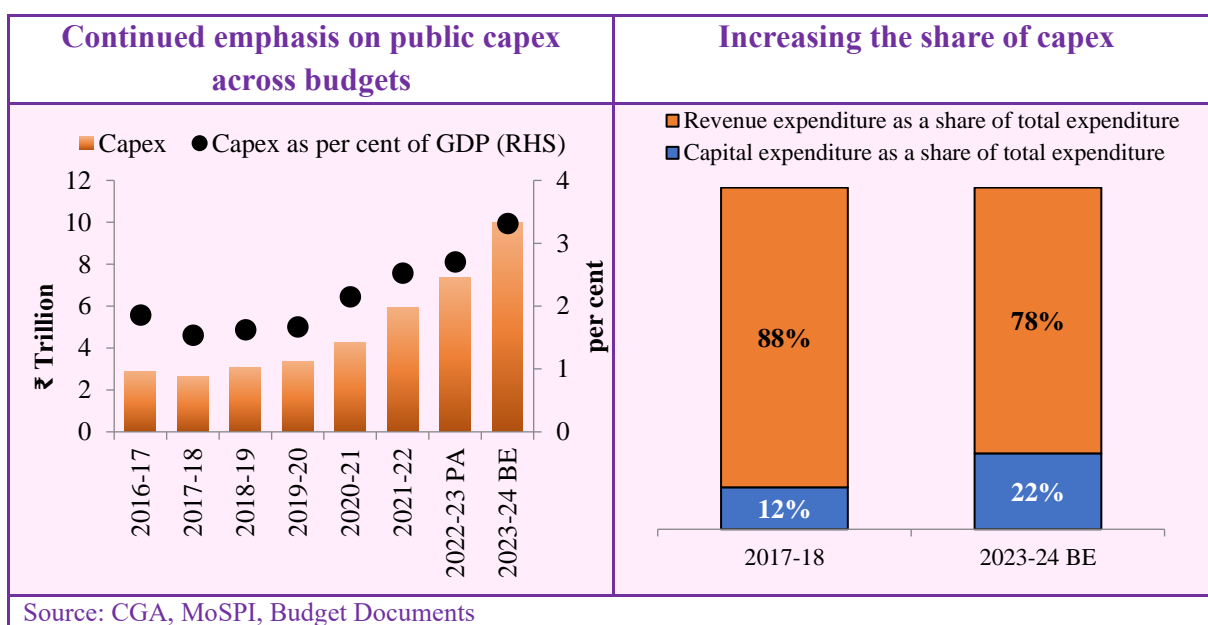


39. Despite the higher subsidy requirements in FY23, the Central Government continued its thrust on capex during the year, achieving 98 per cent of the budgeted target. While revenue



buoyancy assisted in supporting capital outlay, rationalisation of revenue expenditure also helped in protecting the capital outlay within the budgeted fiscal deficit.

Capital expenditure of the central government registered a YoY growth of 24.3 per cent in FY23, higher than the average growth of 7.8 per cent during pre-pandemic years from FY17 to FY20. Union Government Capex as a per cent of GDP stood at 2.7 per cent of GDP and 21.3 per cent of revenue expenditure in FY23 as compared to 1.7 per cent and 14.3 per cent in FY20. In Union Budget FY24, **capital investment outlay has been further increased by 33 per cent to reach** almost three times the outlay in FY20.



40. The Central Government also continued to incentivise states for complementary policy actions to spur investment in infrastructure. The grants for capital works and 50-year interest-free capex loans were made available to the state governments in FY23. The focus of the government on capex also pushed its departmental arms and Central Public Sector Enterprises to accelerate their capital expenditure. CPSEs were able to achieve more than 100 per cent of their full-year revised target of Rs 6.5 lakh crore for capex in FY23.

To incentivise states to increase capex, the union government has provided 50-year interest-free loans to state governments under the 'Scheme for Special Assistance to States for Capital Investment'. During the year FY24, the allocation under the Scheme has been raised to ₹1.3 lakh crore to give further impetus to State Capex plans. This amount includes an unconditional component and smaller components linked to specific reforms/initiatives.

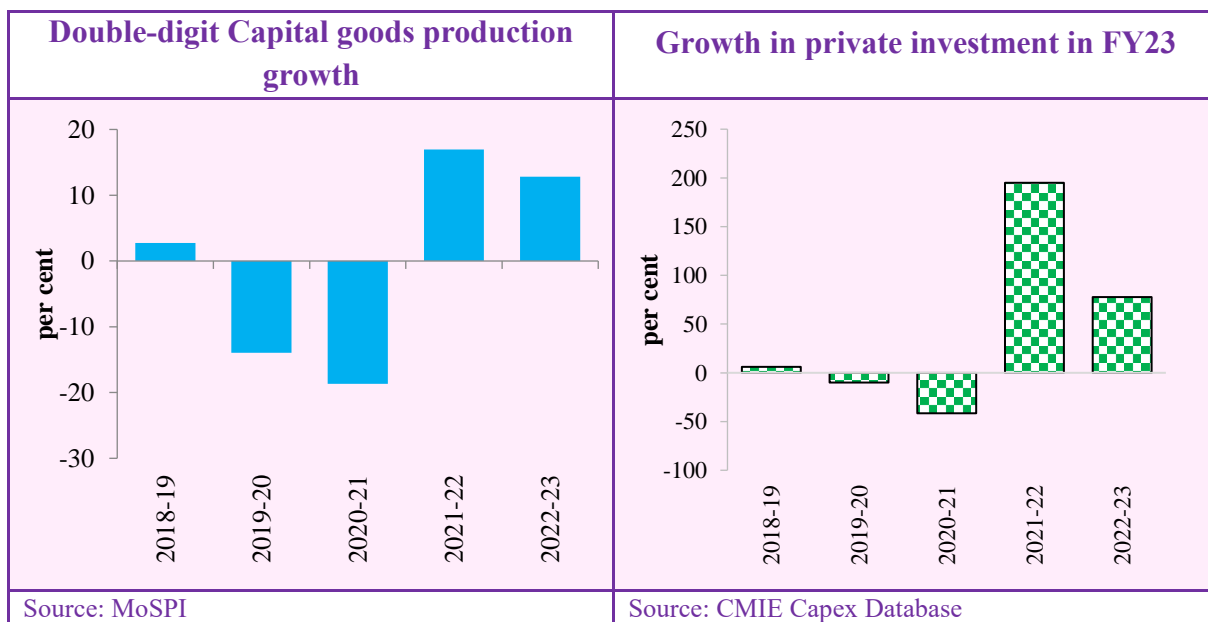
Increased focus on public capex aiding crowding in of private capex

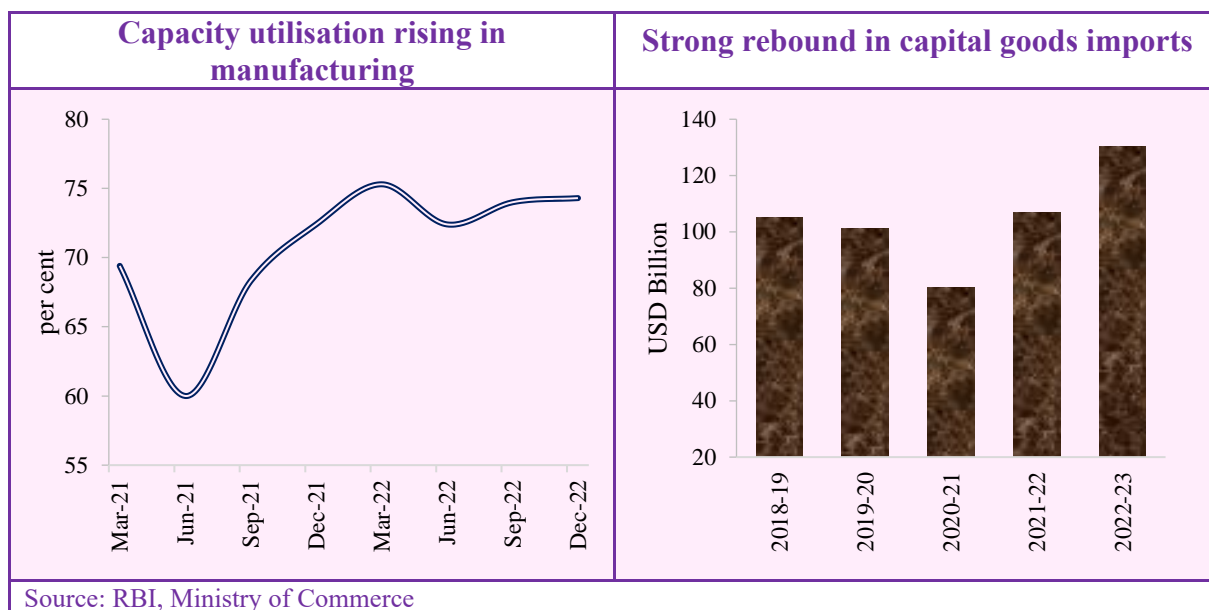
41. The Government's emphasis on capital expenditure was critical in the past few years since the private sector showed risk averseness to undertaking investments due to its own balance sheet issues. However, the latest evidence shows a pickup in private sector investments



induced, among other factors, by the significant upscaling of the government capex. The government's National Infrastructure Pipeline of Projects, Bharatmala, and Sagarmala, among others, have also been important platforms to on board major private sector infrastructure players. Initiatives like PM GatiShakti have also helped and encouraged private sector participation in creating new infrastructure. Increased focus on renewable energy and digitalisation have also opened up new avenues and opportunities for the private sector. Signs of a rebound in private capex are already visible in various proxy indicators. It is expected that the positive trend in private investments will further strengthen in the current year. This is particularly so as capacity utilisation in the manufacturing sector is now above its long-run average, signalling the need for additional capacity creation as demand sustains in the domestic economy.

As per CMIE Capex Database, new private investment proposals registered a strong growth of 78 per cent in FY23 compared to the corresponding period last year. Further, real sector indicators of investment activity, such as capital goods production (IIP – capital goods) and import of capital goods, have registered robust double-digit YoY growth during FY23 as well. Additionally, as per Axis Bank Research, financial data for a consistent set of listed companies indicates broad-based private capex growth of 22 per cent in FY23. As per RBI's Order Books, Inventories and Capacity Utilisation Survey, capacity utilisation for the manufacturing sector increased to 74.3 per cent in Q3:2022-23 from 74.0 per cent in Q2:2022-23. Higher capacity utilisation along with double-digit growth in non-food bank credit in FY23 signals positive intent of the private sector to undertake fresh investment soon.





42. Different ministries in the union government have undertaken infrastructure development in innovative ways. The Ministry of Railways and the Ministry of Road Transport & Highways are developing projects of road connectivity to link 2000 goods sheds. Similarly, 156 critical infrastructure gaps in sectors such as coal, steel, fertiliser, ports and food and public distribution have also been identified for quick action. For the rollout of the cutting-edge 5G network, the Department of Telecom and State Governments are using National Master Plan to identify suitable street furniture for the installation of 5G cells. Significant progress has also been achieved in social sector planning, with 14 social sector ministries/departments having been onboarded under the scheme.

Debt leverage on a glide path

43. The public debt of the union government as at the end of Q3 FY23 was 50.6 per cent of GDP, still higher than the FY20 burden of 42.8 per cent but significantly lower than the peak of 52.6 per cent attained in Q1 FY22 when the pandemic left a debilitating impact on the economy. Similarly, general government debt as a per cent of GDP has also moderated from 89.4 per cent as at the end of FY21 to 82.6 per cent in the quarter ending December 2022. The debt leverage is now on a glide path which will become more pronounced as the economy continues to defy global headwinds and grow above the pre-pandemic rate. The ability of the government to contain its fiscal deficit/GDP ratio within the budgeted target will further contribute to a quicker decline of its debt ratio, strengthening its case for a better credit rating and also lowering interest rates. Given India's general government debt and deficit, fiscal prudence can be fiscal stimulus through its impact on credit rating and lower cost of borrowing.



Growth Outlook for FY24

44. The Indian economy has carried the momentum from FY23 into the current fiscal year. High-frequency indicators paint a healthy picture of the state of the economy. Urban demand conditions remain resilient, with higher growth in auto sales, fuel consumption and UPI transactions. Rural demand is also on its path to recovery with robust growth in two and three-wheelers sales. GST collections and Purchasing Managers' Index for the manufacturing and services sector continue to expand. On the global front, the uptick in economic activity during the first quarter of 2023 has continued in the second quarter as well, as evident in the expansion of the global Composite PMI. However, factors that can constrain the pace of growth include escalation of geopolitical stress, enhanced volatility in global financial systems, sharp price correction in global stock markets, high magnitude of El-Nino impact, and modest trade activity and FDI inflows owing to frail global demand. Should these developments deepen and dampen growth in the subsequent quarters, the external sector may challenge India's growth outlook for FY24.

45. Despite unprecedented global challenges in the last few years coming on top of balance sheet troubles in Indian banking and non-financial corporate sectors, macroeconomic management has been stellar. It contributed significantly to enhancing India's macroeconomic stability and set India on a quicker recovery path than has been the case in other nations. Investments in supply-side infrastructure raise the possibility that India can enjoy sustained economic growth longer than it has been able to in several decades. Strong balance sheets and digital advancements could lead to better credit decisions allowing India's financial cycle to sustain for longer periods before encountering the challenge of bad debts. Thus, India appears poised to sustain its growth in a more durable way than before. Nonetheless, it is no time to rest on laurels nor risk diluting the painstakingly and consciously achieved economic stability. If we are patient, the rising tide will lift all boats as it has begun to.

For feedback and queries, one may write to: mer-dea@gov.in



Performance of High-Frequency Indicators

Data Title	Unit	YTD Period/As at the end of	Year			YoY Growth (per cent)		
			2019-20	2021-22	2022-23	2019-20	2021-22	2022-23
Agriculture								
Fertiliser Sales	Mn Tonnes	Apr-Mar	60.2	59.2	68.1	4.1	-10.6	15.2
Domestic Tractor Sales	Lakhs	Apr-Mar	7.1	8.4	9.5	-10.3	-6.4	12.2
Rabi Production	Mn Tonnes	3rd AE	151.7	159.6	175.4	7.9	1.6	9.9
Kharif Production	Mn Tonnes	3rd AE	144.0	154.9	155.1	0.8	4.4	0.1
Reservoir Level	Bn Cu. Metres	13-Apr	46.5	72.8	69.8	13.7	14.1	-4.1
Wheat Procurement (RMS)	LMT	Apr-Mar	341.3	433.4	187.9	-4.6	11.2	-56.6
Rice Procurement (KMS)	LMT	21 st June	NA	NA	561.0	NA	NA	NA
Rainfall	Millimetres	June-Sep	968	874.6	925	20.4	-8.7	5.8
Industry								
8-Core Industries	Index	Apr-Mar	131.7	136.1	146.6	0.4	10.4	7.7
IIP	Index	Apr-Mar	129.0	131.6	138.4	-0.8	11.4	5.3
Domestic Auto sales	Lakh	Apr-Mar	207.1	164.2	196.8	-26.5	-7.9	19.8
PMI Manufacturing	Index	Apr-Mar	52.3	54.0	55.6	-0.8	7.5	3.0
Power consumption	Billion kWh	Apr-Mar	1,290.3	1,380.1	1,506.5	1.2	8.2	9.2
Natural gas production	Bn Cu. Metres	Apr-Mar	31.2	34.0	34.4	-5.1	18.7	1.2
Cement production	Index	Apr-Mar	145.7	157.0	170.6	-0.9	20.8	8.7
Steel consumption	Mn Tonnes	Apr-Mar	100.5	105.8	118.2	11.7	5.2	11.8



Data Title		YTD Period/As at the end of	Year			YoY Growth (per cent)		
			2019-20	2021-22	2022-23	2019-20	2021-22	2022-23
Inflation								
CPI-C	Index	Apr-Mar	146.3	163.8	174.7	4.8	5.5	6.7
WPI	Index	Apr-Mar	121.8	139.4	152.5	1.7	13.0	9.4
CFPI	Index	Apr-Mar	146.5	163.7	174.6	6.7	3.8	6.6
CPI-Core	Index	Apr-Mar	145.7	162.9	172.8	4.0	6.0	6.1
Services								
Average Daily ETC Collection	₹ Crore	Apr-Mar	NA	104.5	148.4	NA	64.2	42.0
Domestic Air Passenger Traffic	Lakh	Apr-Mar	2745.1	1668.0	2703.4	-0.3	58.5	62.1
Port Cargo Traffic	Million tonnes	Apr-Mar	704.9	720.1	783.5	0.8	7.0	8.8
Rail Freight Traffic	Million tonnes	Apr-Mar	1210.2	1418.1	1512.1	-1.06	15.0	6.6
PMI Services	Index	Apr-Mar	51.9	52.3	57.3	-0.4	25.5	9.5
Fuel consumption	Million tonnes	Apr-Mar	214.1	201.7	222.3	0.4	3.8	10.2
UPI (Value)	₹ Lakh crore	Apr-Mar	21.3	84.2	139.2	143.1	105.1	65.4
UPI (Volume)	Crore	Apr-Mar	1251.9	4596.8	8375.3	132.2	105.8	82.2
E-way Bill Volume	Crore	Apr-Mar	62.9	77.4	96.1	12.8	25.5	24.2
Fiscal Indicators								
Gross tax revenue (Central Govt)	₹ Lakh crore	Apr-Mar	20.1	27.1	30.5	-3.4	33.7	12.7
Revenue Expenditure	₹ Lakh crore	Apr-Mar	23.5	32	34.5	17.1	3.8	7.8
Capital Expenditure	₹ Lakh crore	Apr-Mar	3.4	5.9	7.4	9.3	39.1	24.4
Total Expenditure	₹ Lakh crore	Apr-Mar	26.9	37.9	41.9	16.1	8.1	10.4
Fiscal Deficit	₹ Lakh crore	Apr-Mar	9.3	15.8	17.3	43.9	-12.9	9.4
Revenue Deficit	₹ Lakh crore	Apr-Mar	6.7	10.3	10.7	46.6	-28.9	3.6
Primary Deficit	₹ Lakh crore	Apr-Mar	3.2	7.8	8.0	382.4	-31.6	3.3
GST Collection	₹ Lakh crore	Apr-Mar	12.2	14.8	18.1	3.8	30.4	21.9



Data Title		YTD Period/As at the end of	Year			YoY Growth (per cent)		
			2019-20	2021-22	2022-23	2019-20	2021-22	2022-23
External Sector								
Merchandise exports	USD Billion	Apr-Mar	313.2	422.3	446.9	-5.2	45.1	5.8
Non-oil exports	USD Billion	Apr-Mar	271.9	354.7	352.5	-4.1	33.7	-0.6
Merchandise imports	USD Billion	Apr-Mar	474.2	613.6	713.5	-7.8	56.2	16.3
Non-oil non-gold imports	USD Billion	Apr-Mar	312.8	402.1	463.9	-7.1	45.9	15.4
Net FDI	USD Billion	Apr-Mar	43.0	38.6	28.6	40.0	-12.2	-25.9
Net FPI	USD Billion	Apr-Mar	-3.0	-16.0	-5.5	-	-	-
Exchange Rate	INR/USD	Mar	74.4	76.2	82.3	7.1	4.7	8.0
Foreign Exchange Reserves	USD Billion	07th Apr	476.5	604.0	584.8	15.2	3.9	-3.2
Import Cover	Months	31st Mar	12.0	11.9	9.7	-	-	-
Monetary and Financial								
Total Bank Credit	₹ Lakh crore	Mar	97.7	109.5	136.8	6.1	8.6	15.0
Non-Food Credit	₹ Lakh crore	Mar	97.3	108.9	136.6	6.1	8.7	15.4
10-Year Bond Yields	Per cent	Mar	6.70	6.33	7.33	-12.7	5.5	15.8
Repo Rate	Per cent	Mar	4.4	4	6.5	-29.6	0.0	62.5
Currency in Circulation	₹ Lakh crore	Mar	3.3	4.07	4.31	9.40	13.0	6.0
M0	₹ Lakh crore	Mar	2.45	3.13	3.38	14.5	9.8	7.9
Employment								
Net payroll additions under EPFO	Lakh	Apr-Mar	78.6	122.3	138.5	28.6	58.7	13.2
Number of persons demanded employment under MGNREGA	Crore	Apr-Mar	30.1	40.2	33.2	-0.6	-10.0	-17.4
Urban Unemployment Rate	Per cent	Mar	7.9	8.8	7.2	-	14.6	-18.2
Subscriber Additions: National Pension Scheme	Lakh	Apr-Mar	7.6	8.8	8.2	0.9	39.9	-6.3