

July 2022

Monthly Economic Review

Economic
Division



आर्थिक कार्य विभाग
DEPARTMENT OF
ECONOMIC AFFAIRS

सत्यमेव जयते

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Abstract

The global economic outlook remains challenging amid elevated inflationary pressures, monetary policy tightening, recession fears and financial markets uncertainties, although stock markets have staged a big recovery in the United States and elsewhere in the last two months. Despite softening of international commodity prices in July, inflationary pressures are expected to remain high in Advanced Economies (AEs) with rebalancing of demand towards services and pass-through of higher input costs along the value chain. Rising wages may also lead to a broadening of inflation beyond commodity prices. Further, the tightening of monetary policy by central banks has generated apprehensions of recessions in major economies. Global manufacturing PMI declined to a two-year low of 51.1 in July 2022. Apprehending slowing growth, the IMF in its latest World Economic Outlook Update of July 2022 entitled 'Gloomy and More Uncertain', has lowered the global growth forecasts for 2022 with a significant downgrade for AEs. In view of weakened global growth prospects, the market perceives peaking of policy rate hike as reflected in softening of global bond yields in July 2022.

Despite global headwinds, the IMF forecasts India's economy to grow at a robust rate of 7.4 per cent in 2022-23, the highest among major economies. The buoyant performance of some high frequency indicators during the first four months of 2022-23 is consistent with IMF's forecast. Index of Industrial production and 8 core industries points towards strengthening of industrial activity, while PMI Manufacturing touched an 8-month high in July with marked gains in growth of new business and output.

The services sector which was impacted the most by the COVID-19 pandemic, can emerge as a key growth driver, buoyed by the release of pent-up demand, easing of mobility restrictions and near universal coverage in vaccination. Amongst sub-sectors, a mixed trend in recovery is observed with Real Estate and Information Technology-Business Process Management (IT-BPM) completely recovering to the pre-pandemic levels of 2019-20. However, the logistics, tourism sector and hotel industry continue to be on the path of recovery having now come close to the pre-pandemic level. World services trade, as indicated by WTO's Services Trade Barometer index continued to grow, yet, some headwinds may be observed in the coming months with the slowing of output in AEs. Growth momentum in services sector activity, as measured by PMI services remained comfortably in the expansionary zone in July 2022. PMI services should continue to remain in expansive mode in the months ahead with the RBI's Services and Infrastructure Outlook Survey showing optimism of service-sector firms in

respect of demand conditions, overall business situation, employment and turnover in Q2 of 2022-23.

As India navigates the choppy waters of an uncertain global economic environment, the Indian banking system and the corporate sector are proving to be pillars of resilience. The Q1 data now available for 2022-23 confirms a secular decline in the Gross Non-Performing Assets (GNPA) ratio of Scheduled Commercial Banks (SCBs) for four successive quarters. The GNPA ratio has declined from 7.5 per cent in the June quarter of 2021 to 5.7 per cent in the June quarter of 2022. The balance sheets of the corporate sector have also been strengthening since May of 2020, and have continued to do so as the latest data available for June 2022 indicate, with robust metrics on net nominal and real sales, operating profit and interest coverage ratio staying above the pre-pandemic levels. Expectedly, the rising financial soundness of banks as well as that of the corporates have been boosting the YoY growth of non-food bank credit since the June quarter of 2021. The YoY growth in non-food bank credit stood at 14 per cent in June, 2022 driven by credit growth to both Industry and Services in the June quarter of 2022.

Domestic inflationary pressures have also moderated. Headline retail inflation eased to 6.7 per cent in July 2022 on the back of a decline in food inflation to 6.8 per cent, which to an extent has followed a decline in global food prices. The declining global prices of edible oils and the government's measures to reduce the domestic prices of these commodities have had a profound impact on tempering India's retail food inflation. Steps such as maintenance and calibrated releases of buffer stocks in the case of rice, pulses, and onions, and export restrictions in the case of wheat are expected to keep a check on food inflation. Softening of inflationary pressures in India is further on the anvil as the prices of important raw materials such as iron ore, copper, tin, etc. that feed into the domestic manufacturing process, globally trended downwards in July 2022. Lower global prices of minerals have contributed to bringing down input cost inflation in India. Inflation in the services sector has also decelerated as is evident in the softening of inflation in the services components of the CPI basket.

Household and business expectations have moderated over the last two months, indicating that the high inflation of the past few months has not entered the anchoring zone of inflation expectations. In the absence of any further shocks, the downward movement of global commodity prices along with the RBI's monetary measures and the government's fiscal policies are expected to cap inflationary pressures in the coming months.

On the external front, post the outbreak of the Russia-Ukraine conflict, an increase in uncertainty among investors has led to capital outflows, not just from India alone but from the group of emerging market economies (EMEs) as a whole. Thus, apart from India, the currencies of several EMEs also depreciated against the US dollar. Between January and July of 2022, foreign portfolio investors pulled out USD 48.0 billion from the group of EMEs as a whole. In the case of India, its relatively more liquid capital and foreign exchange markets as compared to those of Indonesia, South Africa, and Mexico were responsible for the net FPI outflows. Consequently, the INR depreciated as did the currencies of other EMEs. However, despite more liquid markets, 95 per cent of the Assets under Custody of FPI stayed on in India reflecting the confidence foreign portfolio investors have in India's economic strength. Further, if more liquid forex markets can facilitate capital outflow, they can enable in-bound flows as well when the tide turns. FPI in the month of July have been net purchasers to the extent of USD 458 million as global perception of monetary tightening having reached its peak gains ground. In August, until the 12th, FPI net inflows have been around USD 2.9 billion.

Global investor confidence in India's economic landscape is further endorsed by net foreign direct investment (FDI) inflows remaining robust at USD 13.6 billion in Q1 of 2022-23, as compared to USD 11.6 billion during the corresponding period of the last year¹. In sync, local investment activity has also picked up, as seen in the real sector where capital goods production and import of capital goods registered a robust double-digit growth during Q1 of 2022-23. Government also continues to support investment activity with capital expenditure reaching Rs. 1.75 lakh crore during Q1 of 2022-23, which is 23.4 per cent of the budget estimate and 57 per cent higher as compared to the corresponding period of last year.

Going forward, kharif sowing supported by southwest monsoon coupled with higher MSP for Kharif crops is likely to enhance rural demand. Urban consumption is expected to benefit from the demand for contact-intensive services, improving performance of corporates and growing optimism of consumers. The robust production of capital goods along with the government's capex push and large expansion in bank credit will uphold the investment activity. The manufacturing sector is expected to gain from easing of input prices and a rise in consumer demand during the festive season. As per RBI Survey, manufacturing firms expect sustained improvement in production volumes and new orders in Q2:2022-23.

¹ FDI data for Q1: 2022-23 is quoted from RBI Governor's Statement in August Bi-monthly Monetary Policy Statement, 2022-2023.

The sustained decline in the price of crude oil into August since June and the decline in the inflation rate in India below 7.0 per cent and the impressive growth in India's tax revenue collection in the current financial year have combined to contribute to a significant easing of concerns over growth and inflation in the current financial year.

Risks remain, however. The geopolitical environment remains tense and fraught. This could trigger fresh supply concerns in the winter for critical commodities such as crude oil and natural gas. The Chinese economy is struggling and the central bank has unexpectedly lowered its policy rate signalling serious worries about growth. That could trigger risk aversion in financial markets around the world that have begun celebrating, perhaps, prematurely, the easing of inflation pressures in the near-term in the developed world. Inflation rates are still stubbornly high. Without further considerable policy tightening, it is difficult to see the inflation rate in the advanced world drop to around 2 per cent to 3 per cent. Such tightening would almost guarantee a recession for economic growth and corporate profits. Hence, a reality check on the part of stock markets in the developed world could bring back growth chills everywhere.

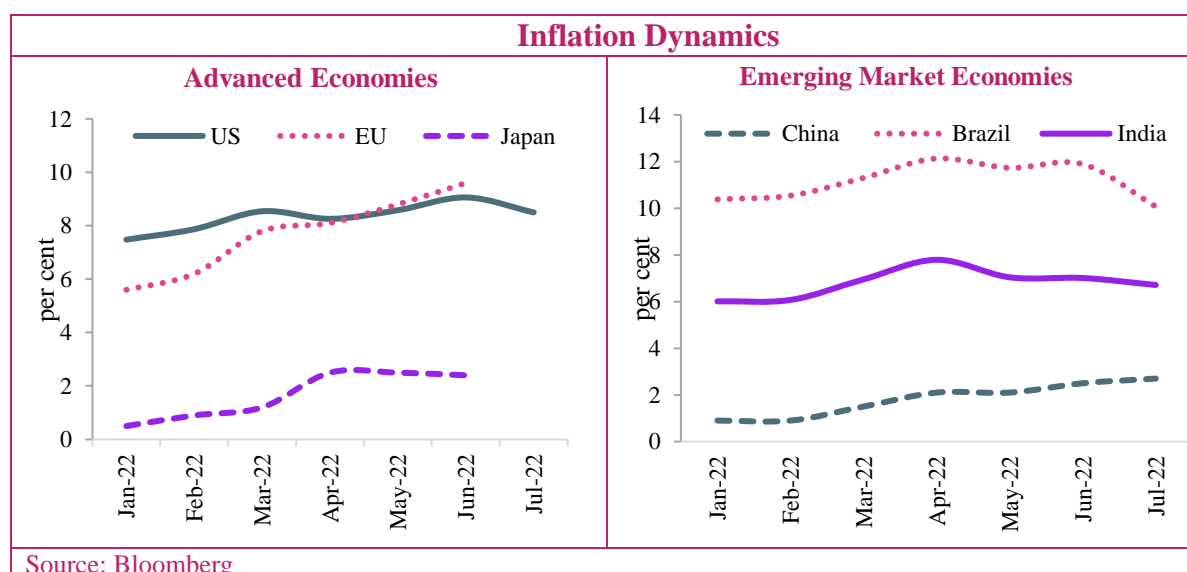
It is not necessarily the right thing to do to project either optimism or pessimism too far ahead in these uncertain times. For now, India looks better placed on the growth-inflation-external balance triangle for 2022-23 than it did two months ago. Such an improvement in the cyclical prospect is a reflection of the swift economic policy response by the government and the central bank. The economy's resilience, especially in the light of growth challenges elsewhere in the world, is due, in no small measure to the sustained efforts of the government and the central bank to regain and preserve the underlying macroeconomic and financial stability. Few countries around the world are better placed and can point to a recovery in their macroeconomic fortunes in the last few months as India is able to.

That is cause for cheer and gratefulness on the occasion of the celebration of the 75th anniversary of Indian independence.

Global Overview

Slow recovery clouded by inflationary pressures

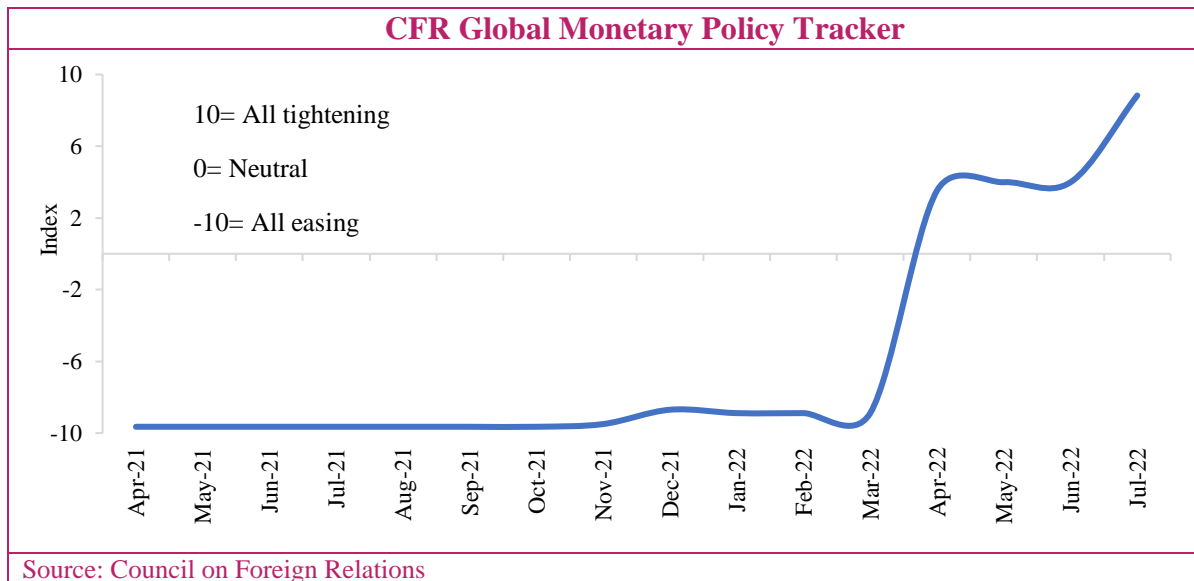
1. The global macroeconomic scenario continues to evolve with inflation driven to a new high in many Advanced Economies (AEs) as supply chain disruptions, coterminous with the Russia-Ukraine conflict and Chinese zero COVID policy, persist, and demand continues to revive with the waning of the pandemic. Inflationary pressures in specific food and energy items have however witnessed a slight moderation in July. Yet, a rebalancing of demand back towards services and a pick-up in pass-through of input costs along the value chain, may continue to drive up inflation in the coming months already ratcheted by tighter labour markets and anchoring of inflationary expectations in many AEs. Inflation rate in the USA reached 8.5 per cent in July 2022. Inflation in the EU also soared to record 9.6 per cent in June 2022. The tightening of monetary policy has been in overdrive with the Federal Reserve (Fed) effecting a second consecutive 75 basis points increase in benchmark rate taking it to the range of 2.25 - 2.50 per cent. The European Central Bank (ECB) also increased its benchmark rate up by 50 basis points for the first time in 11 years.



2. Monetary tightening by central banks is not limited to those in AEs alone. The central banks of emerging market economies (EMEs) have also been undertaking similar tightening to bring down inflation. As per the CFR Global Monetary Policy Tracker², most of the major economies were in the phase of quantitative easing until March, 2022. From April onwards

² CFR's Global Monetary Policy Tracker compiles data from 54 countries around the world to highlight significant global trends in monetary policy. In generating the index value at any point in time, each country's monetary policy stance is weighted by its currency's share of global foreign exchange reserves. (The United States, therefore, receives a 61 per cent weighting.) A country is said to be easing (tightening) policy if it has cut (raised) rates in the past three months, or is expected to do so in the next three months. A country is also said to be easing if it is engaged in QE.

however, the tightening of monetary policy was observed in several major economies. In July 2022, countries entered into another cycle of monetary tightening as EMEs face up to the dual challenge of rising inflation and capital outflows back to the AEs.

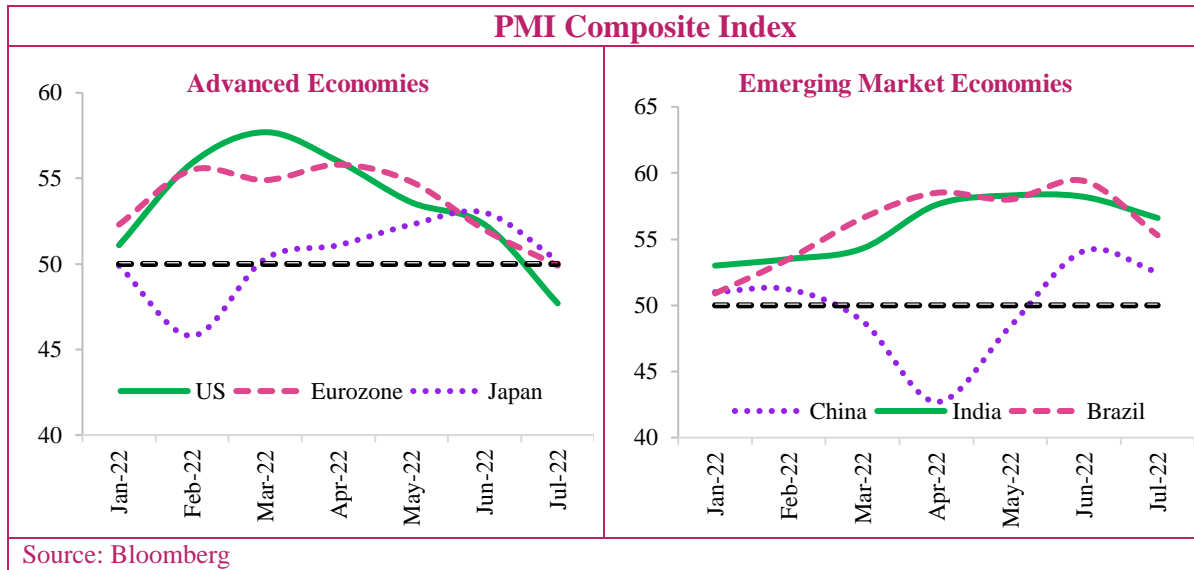


3. Monetary tightening in AE to rein in inflation has entailed the collateral damage of slower growth in world output already weakened by the pandemic. The first signs of slowdown have now surfaced with Global Manufacturing PMI falling from 52.2 in June to a two-year low of 51.1 in July, on the back of a decline in new orders and employment. Substantial downturn in output is witnessed in the United States, Eurozone, UK and Japan.

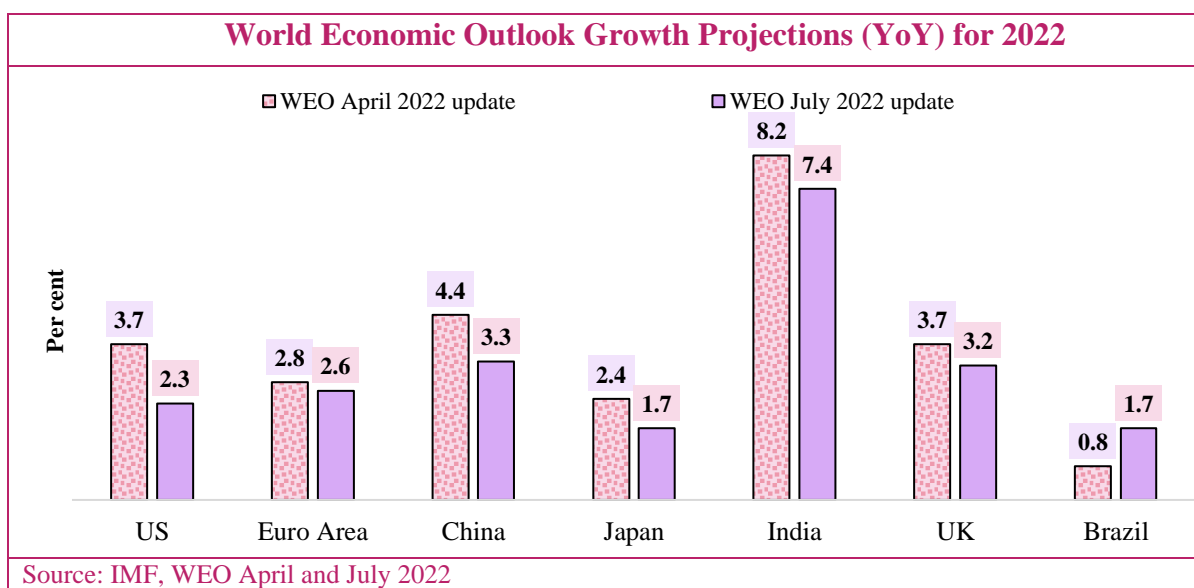
4. US Composite PMI fell into the contractionary zone in July, signalling a downturn in private sector business activity and softening momentum of exports order placed with trade partners. The real GDP numbers of the USA in Q2 of 2022 also signal a further weakening of economic activity with real GDP YoY declining 0.9 per cent in this second quarter having posted a 1.6 per cent decline in the first quarter. The consumer confidence index, a parameter to gauge private consumption, also declined in July 2022, in a further endorsement of an anticipated slowdown.

5. In the second quarter of 2022, EU real GDP recorded better than expected growth. Yet the fear of weakening growth persists with Eurozone PMI slipping into the contraction zone in July 2022 as manufacturing downturn was accompanied by a further slowdown in the service sector. The European Commission has now slashed GDP forecasts for 2022 and 2023 as a result of increased uncertainty, demand slowdown due to surging prices and possibility of winter energy shortages. Growth moderated in China as well as resurgence of COVID-19 cases and consequent re-imposition of restrictions have weakened production and slowed down manufacturing expansion in July. Indeed, growth forecasts for China for 2022, already

revised down by the IMF from 4.8 per cent in January 2022 to 3.3 per cent in July 2022 is at risk of being lowered further.

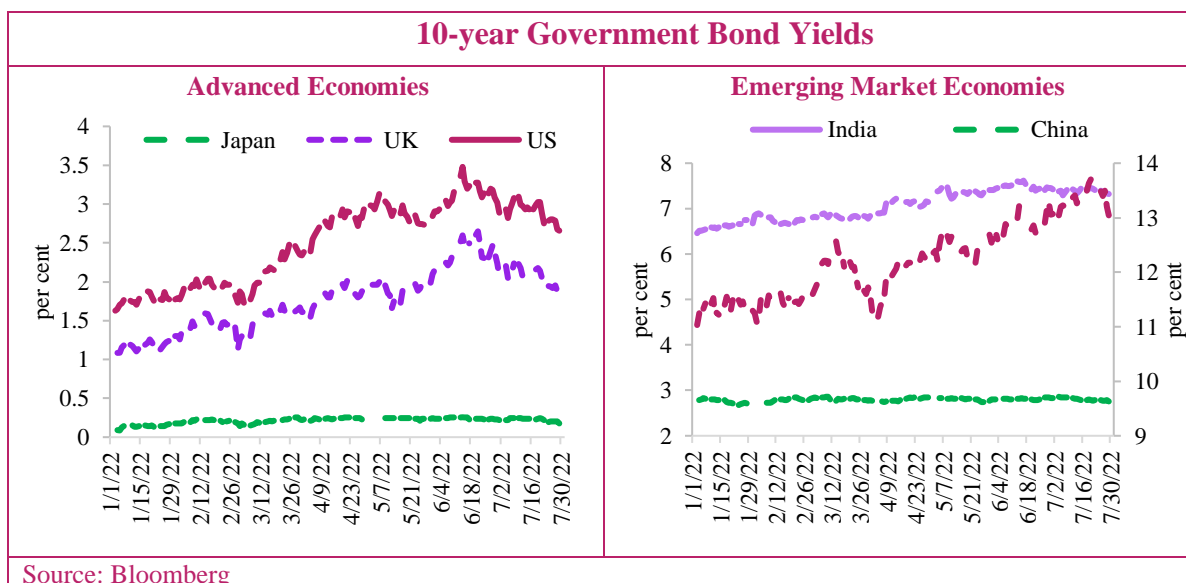


6. Capturing recent adverse global developments such as higher input costs and monetary tightening, the IMF’s World Economic Outlook Update of July 2022, has also lowered the global growth forecasts for 2022 to 3.2 per cent from 3.6 per cent in its April update. For the AE, the growth projection has been revised downward from 3.3 per cent in April update to 2.5 per cent in July update while for EMEs the downward revision has been from 3.8 per cent to 3.6 per cent. Across the two updates, the IMF has revised India’s real GDP growth projections for 2022 from 8.2 per cent to 7.4 per cent. The downward revisions of growth projections coexist with the upward revision of inflationary forecasts. The IMF has revised the inflation forecast for AE from 5.7 per cent to 6.6 per cent and for EMEs from 8.7 per cent to 9.5 per cent in 2022.



7. Unlike the IMF, the RBI in its August meeting of the Monetary Policy Committee (MPC) has retained the growth and inflation forecasts for 2022-23 made in the June meeting, at 7.2 per cent and 6.7 per cent respectively, after increasing the repo rate by another 50 basis points. An unchanged growth projection reflects the growth momentum in the Indian economy. However, the momentum may be challenged if merchandise exports, which have fallen to a five-month low in July, 2022, do not recover to their earlier high levels, as slowing growth in AE is set to weaken cross-border trade. An unchanged inflation forecast on the other hand, despite the raising of the repo rate, is consistent with the global view that global inflationary pressures may be slow to abate. We should note that the Indian central bank projects inflation to drop well below the upper end of its target inflation range of 2 per cent to 6 per cent by the first quarter of 2023-24. Inflation in Q1 2023-24 is projected at 5 per cent.

8. With inflationary pressures unabated and also not expected to soften in the near term, a further tightening of monetary policy across the central banks cannot be ruled out. However, market participants perceive that central banks are already near the peak of policy rate hikes in view of weakened growth of global output and therefore, going forward, may opt for only a mild tightening. Market perception is reflected in government bond yields, which have registered a sharp decline in July, 2022 after showing a rising trend since the outbreak of the Russia-Ukraine crisis when tightening of the monetary policy had just begun.

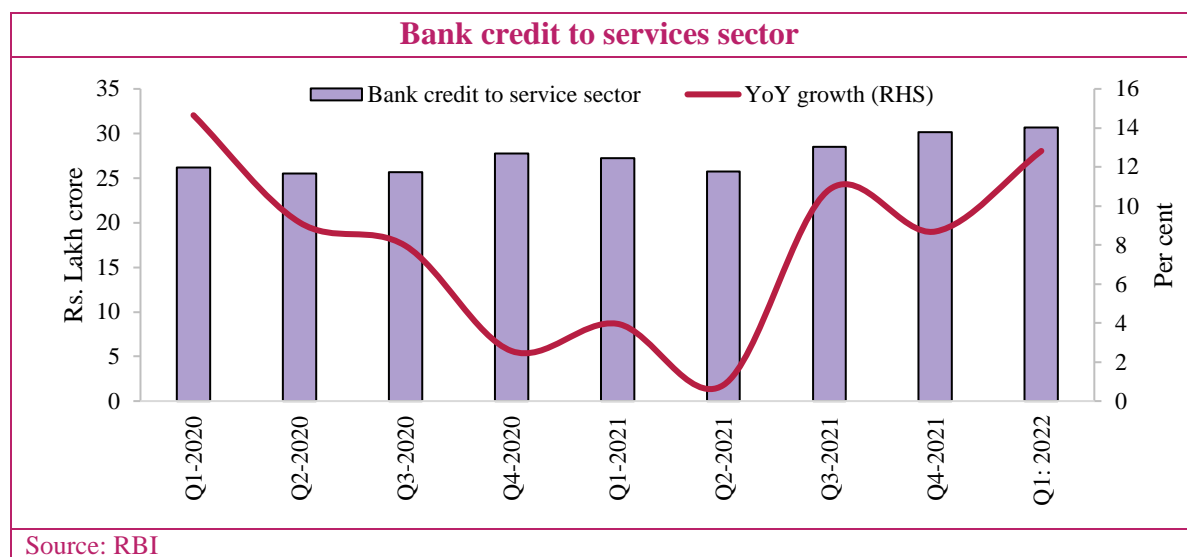


Services sector

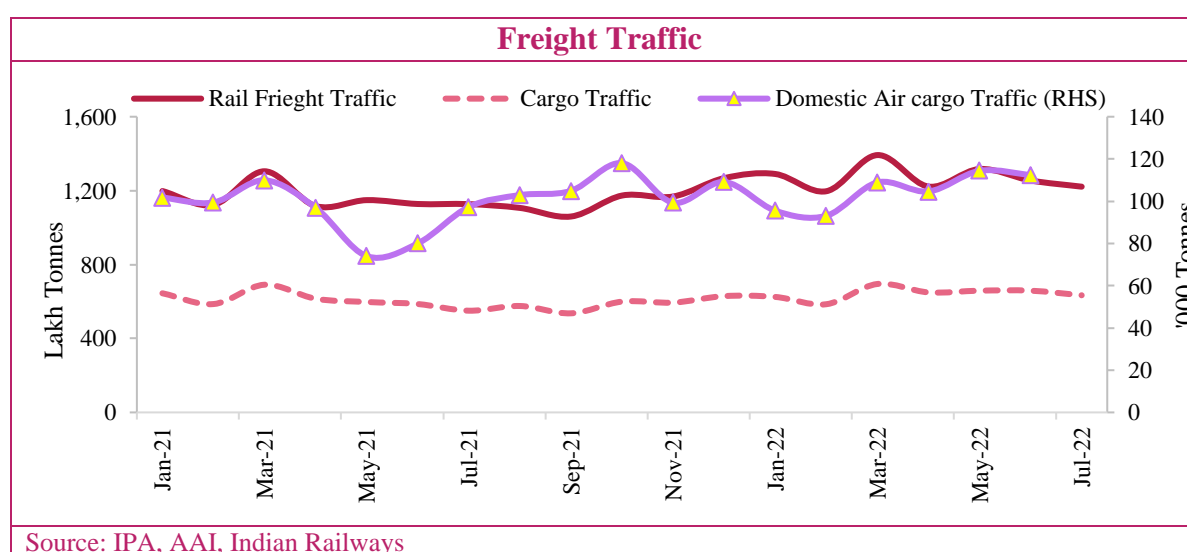
Service sector to drive growth enthused by release of pent-up demand, easing of mobility restrictions and near universal coverage in vaccination

9. Monetary tightening and elevated inflation in the country besides somewhat subdued export prospects consequent upon slowing growth in AEs may appear to pose some downside risks to India's growth. Yet mitigation of the threat is likely from the services sector, which is being driven by the release of pent-up demand, easing of mobility restrictions and near-

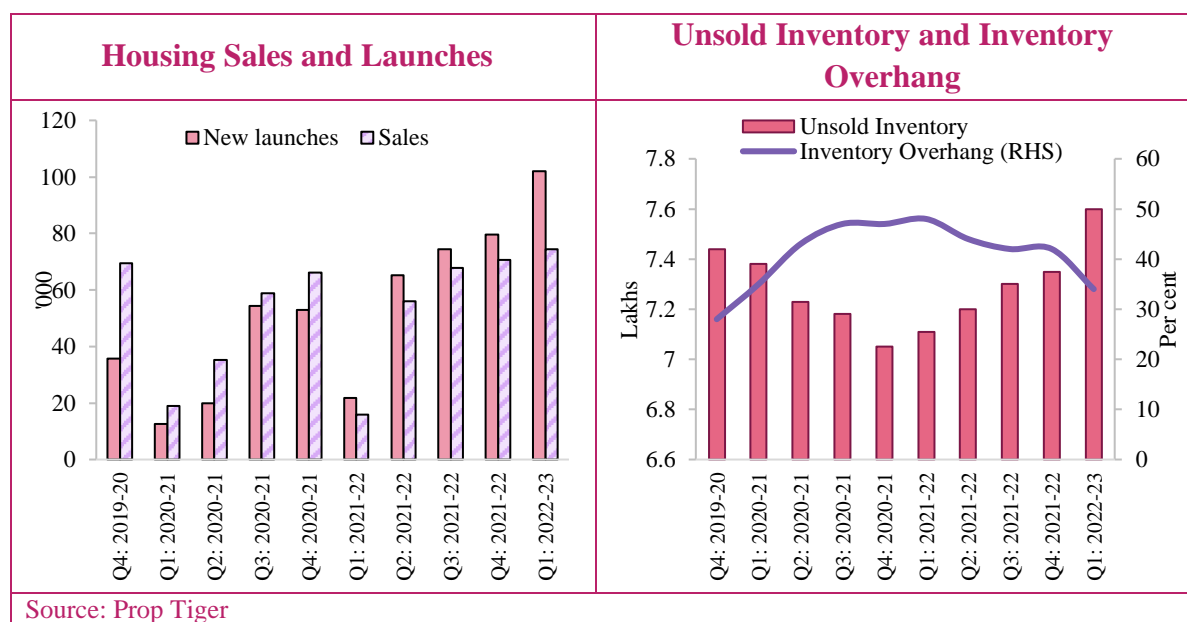
universal vaccination coverage. Evidence to this effect is seen in the bank-credit supply to the services sector, which has registered a YoY growth of 12.8 per cent in Q1 of FY 2022-23 as compared to 3.9 per cent in corresponding quarter of the previous year, mainly due to improved credit offtake by transport operators, professional services, retail trade and non-banking financial companies (NBFCs).



10. Indian Railways has been a critical driver in imparting impetus to the services sector. The railway freight traffic YoY growth of 8.4 per cent in July 2022 was fuelled by incremental loading of coal, cement & clinker and automobiles. The sustained efforts of Indian Railways to increase the supply of coal to power plants has been instrumental in delivering an improved freight performance and in ensuring that India saw through the summer months without significant power outages. Transportation of coal further contributed to growth in port traffic as also rising congestion and shortage of fuel in Sri Lanka that led to the diversion of shipments to ports in south India. Domestic Air cargo traffic registered double-digit growth in June 2022 however, moderating compared to the previous month due to a decline in passenger load factor and higher fuel prices.

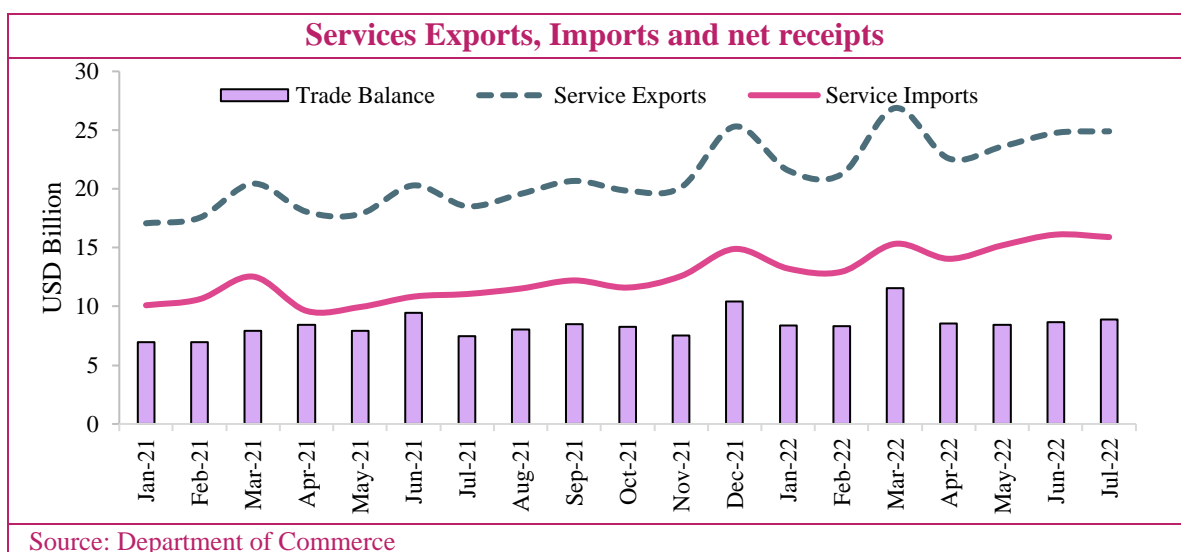


11. In the real estate sector, housing sales and the launch of new houses in the top 8 cities registered significant sequential growth in Q1 of FY 2022-23 despite an increase in the interest rate on home loans and a rise in property prices. Positive buyer sentiment has been instrumental in bringing down the inventory overhang³ to 34 months in Q1: 2022-23 from 42 months in the preceding quarter bodes well for disposing of growing volumes of unsold inventory. Sustained growth in housing will not only keep the economic growth at high levels but also provide livelihood to a large section of the workforce.



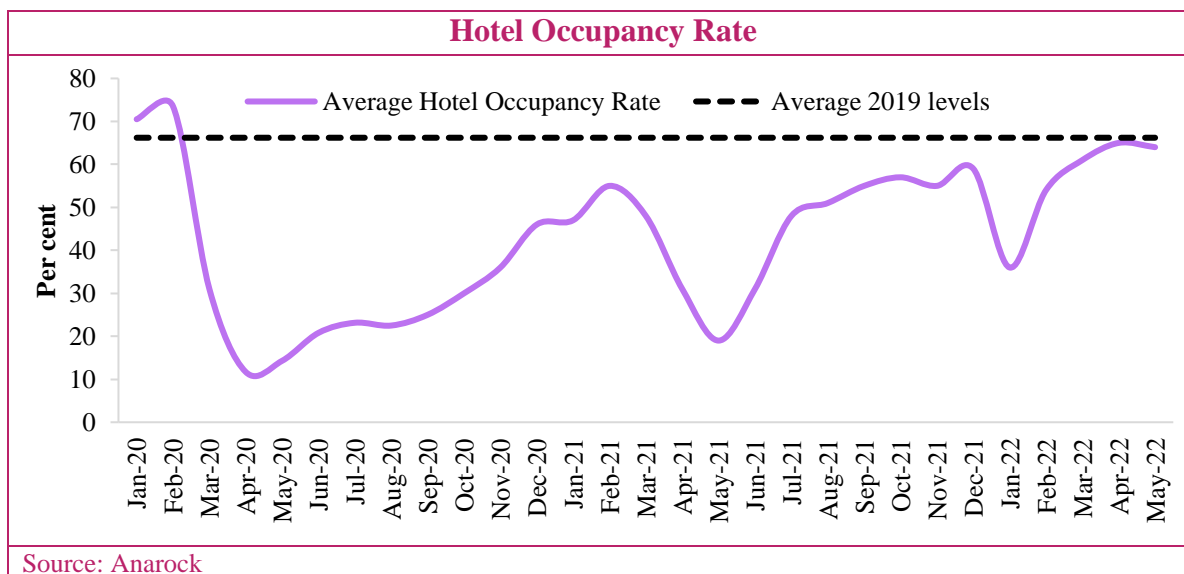
12. On the external front, world services trade continued to grow as indicated by WTO's Services Trade Barometer index which stood at 105.5 in June 2022 (above the baseline value of 100). Some headwinds may however be observed in the coming months on account of the slowing of output in AEs. Yet, given the dominant presence of India in global services exports, export volumes will continue to be large despite a weakening of global trade. India was among the top ten services exporter countries in 2021 having increased its share in world commercial services exports from 3.0 per cent in 2015 to 4.0 per cent in 2021. Seeing the strength and further potential of India's services sector, the highest ever annual foreign direct investment (FDI) inflows into India recorded in 2021-22, significantly comprised FDI equity inflows into the services sector including computer software and hardware. Share of the services sector in total FDI equity inflows increased from 8.5 per cent in FY 2020-21 to 12.1 per cent in FY 2021-22.

³ inventory overhang is estimated time period developers are likely to take to sell off the unsold inventory, based on the current sales velocity.



13. Going forward, the Information Technology–Business Process Management (IT-BPM) services is critical for propelling the Indian economy onto a higher growth path and to sustain it. So far during the post-pandemic recovery, the performance has been both encouraging and promising. According to NASSCOM's provisional estimates, the IT-BPM revenues registered YoY growth of 15.5 per cent during FY 2021-22, with all sub-sectors witnessing a double-digit revenue growth. Exports (including hardware) grew by 17.2 per cent, driven by cost transformation deals and core operations. Growth in exports was also seen across all major markets. NASSCOM has further indicated that many firms are now focusing on new markets, leading to market diversification which will increase the IT-BPM sector's resilience in the coming years. The industry recorded nearly 10 per cent estimated growth in the direct employee pool in FY 2021-22, with a highest-ever net addition to its employee base.

14. The post-pandemic scenario of global tourism is gradually converging to the pre-pandemic one. As per the World Tourism Barometer of the United Nations World Tourism Organization (August 2022), international tourism witnessed a strong rebound during January-May 2022, with international tourist arrivals registering YoY growth of 224.7 per cent, recovering almost half of pre-pandemic 2019 levels. Foreign tourist arrivals in India in 2022-23 have also been growing month-on-month with the resumption of scheduled international flights and easing of COVID-19 regulations. Yet the arrivals are still below the pre-pandemic level. Recovery in domestic tourism has however ensured improvement in average hotel occupancy rate, increase in the average room rate (ARR) and rise in revenue per available room (RevPAR) that are now much nearer to the pre-pandemic level of 2019-20. Sustained growth in both domestic and international tourism in India is contributing to India's better growth performance in 2022-23 compared to other nations.

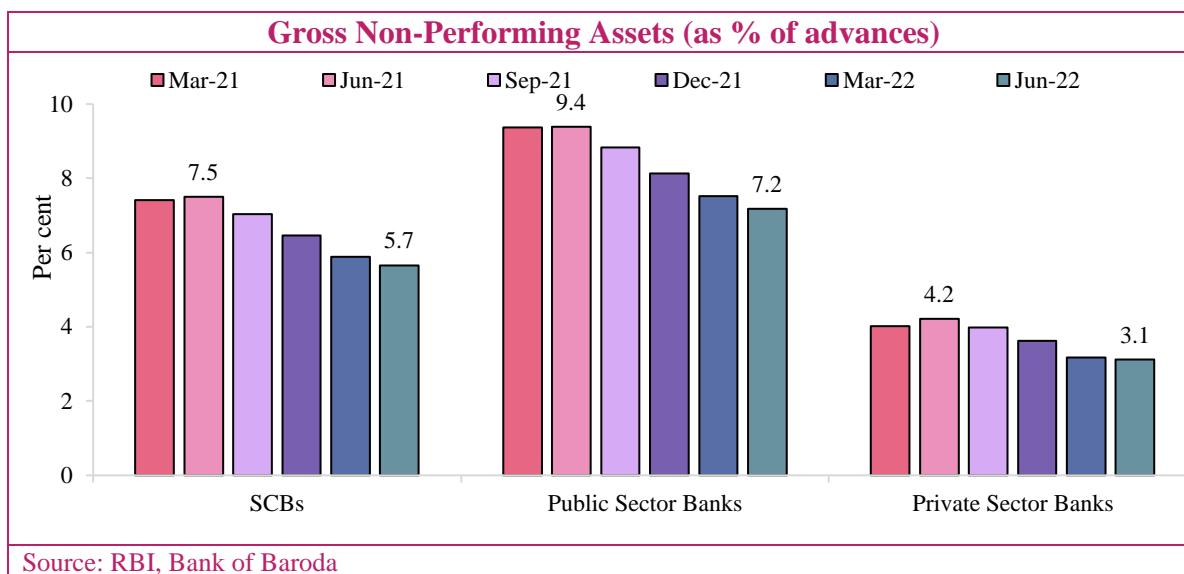


15. Growth momentum in services sector activity, as measured by PMI services, remained comfortably in the expansionary zone at 55.5 in July 2022, correcting for the exceedingly high level of 59.2 in June. The PMI services should continue to remain in the expansive mode in the months ahead as can be expected from the RBI Services and Infrastructure Outlook Survey that show optimism of service-sector firms in respect of demand conditions, overall business situation, employment and turnover in Q2 of FY 2022-23.

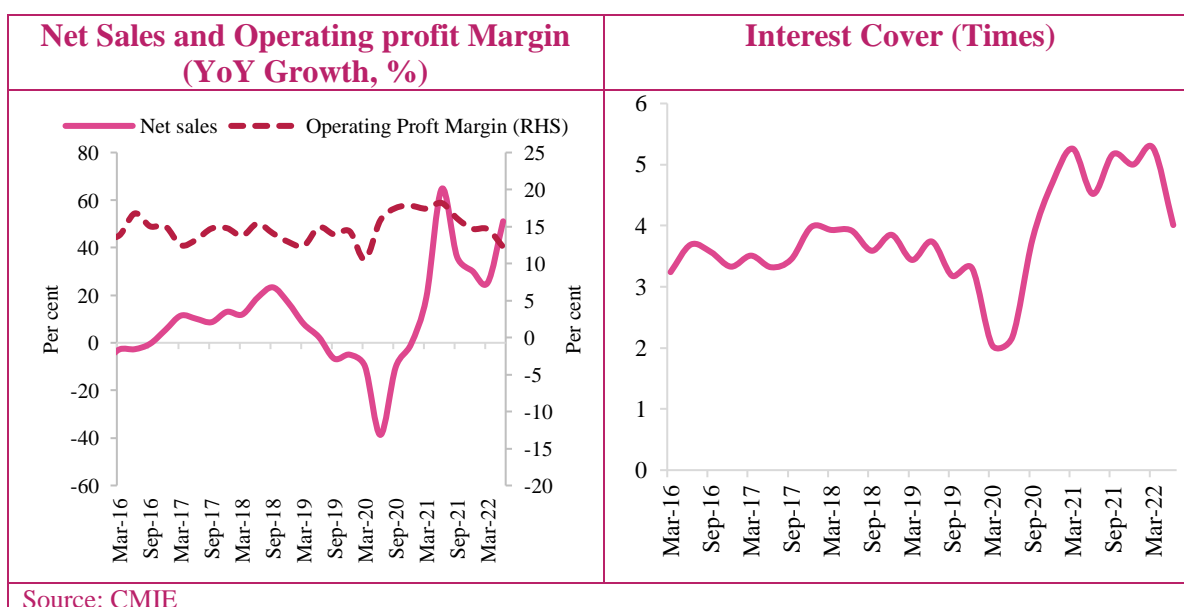
Financial and Corporate Sector

Strengthened banking system and strong corporate sector fundamentals will enhance the credit flow into productive investment opportunities

16. The Q1 data now available for 2022-23 confirms a secular decline in the Gross Non-Performing Assets (GNPA) ratio to outstanding advances of Scheduled Commercial Banks (SCBs) for four successive quarters. The GNPA ratio has declined from 7.5 per cent in the June quarter of 2021 to 5.7 per cent in the June quarter of 2022. Public Sector Banks (including IDBI) registered a larger decline of 221 bps to 7.2 per cent in June 2022 compared to Private Sector Banks which witnessed a reduction of 110 bps to 3.1 per cent in June 2022. The consequent strengthening of the balance sheets of the suppliers of credit has made them more responsive to the credit needs of small and corporate enterprises. This is evident from the outstanding bank credit to the Industry sector which expanded by 9.5 per cent year on year basis to ₹ 31.7 lakh crore as on 30th June 2022.



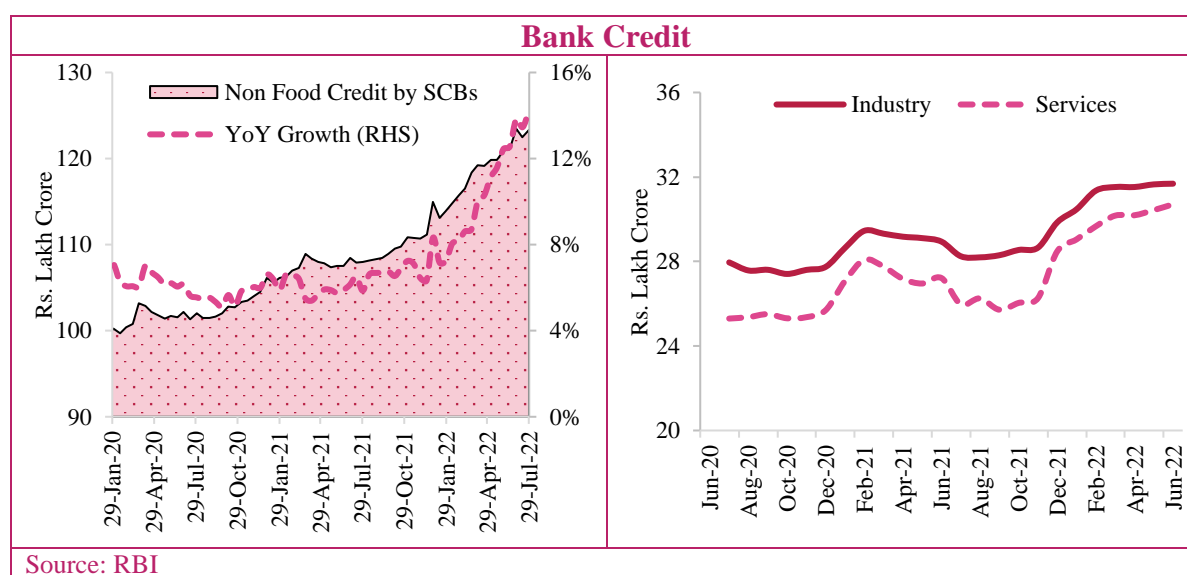
17. The balance sheets of the corporate sector has also been strengthening since May of 2020, and has continued to do so as the latest data available for June, 2022 indicate, with robust metrics on net nominal and real sales, operating profit and interest coverage ratio staying above the pre-pandemic levels. The performance has slightly dipped in the June quarter of 2022 owing to the war-induced global macroeconomic uncertainty and inflationary pressures. Yet the secular improvement in the corporate sector performance is unmistakable, contributing to an enhanced risk appetite to undertake long-term capital expenditure. India's much awaited capex cycle, while pushed back by successive one-off shocks of pestilence and war, may not be too far away.



18. Expectedly, the rising financial soundness of banks as well as the corporates has been boosting the YoY growth of non-food bank credit since the June quarter of 2021. The YoY growth in non-food bank credit stood at 14 per cent in July, 2022 driven by credit growth to

both Industry and Services in the June quarter of 2022. Credit growth to services has however been higher as lately this sector has been sustaining the growth momentum following the release of its pent-up demand. Strengthened asset quality of the banking system and stronger corporate sector fundamentals should continue to enhance the flow of bank credit into productive investment opportunities notwithstanding the rising interest rates.

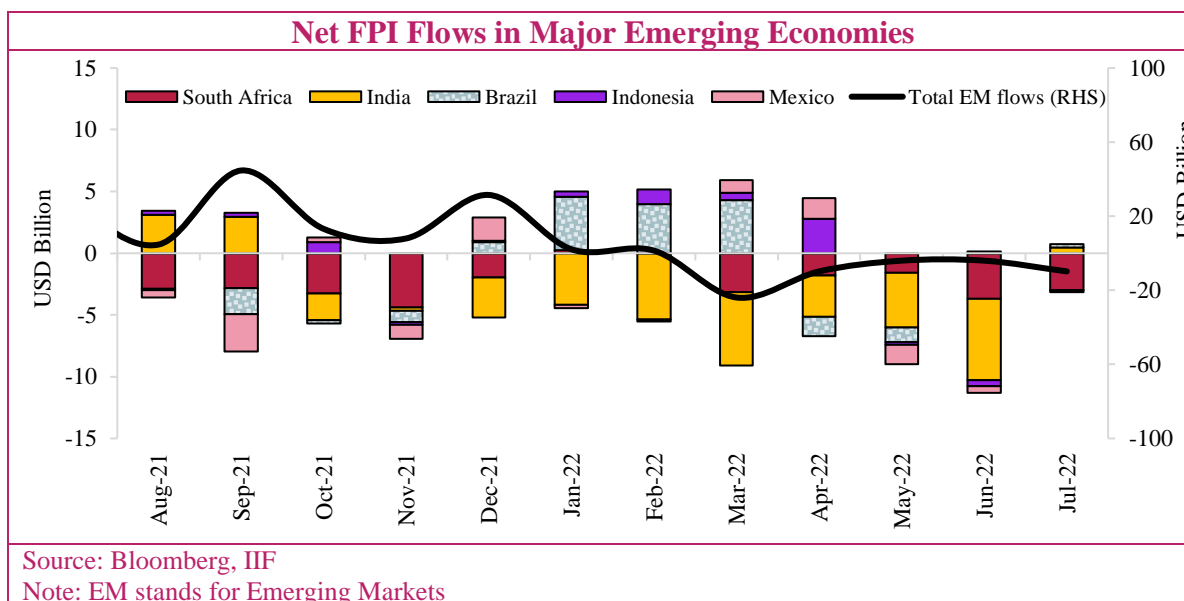
19. Swift action by the Reserve Bank of India in raising policy rates and government measures to control the rise in prices and ensuring supply of essential commodities, detailed later, have contributed to dampening the inflation rate staving off the risk of higher interest rates and higher cost of capital for the government and for the industry.



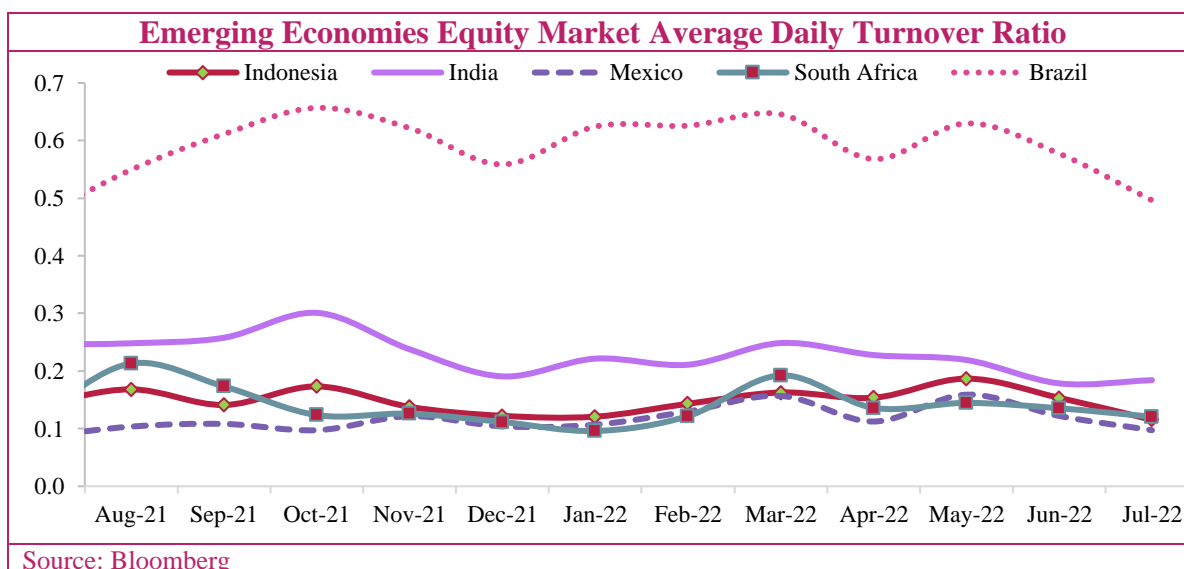
Investment

Confidence of foreign investors remains intact in Indian economy, FPIs turns net buyers in July

20. The INR recently breached the mark of 80:1 USD depreciating close to 7 per cent in the first seven months of 2022. Rapid currency movements in the short-term are generally the outcome of short-term developments themselves but there was no such development unique to India alone. The impact of the Russian-Ukraine conflict on global commodity prices, monetary tightening by central banks across countries and increase in uncertainty among investors led to capital outflows, not just from India alone but from the group of EMEs as a whole. Thus, apart from India, the currencies of several EMEs also underwent depreciation. Currencies of some AEs were not spared either. To be specific, incipient outflows of FPI from EMEs and the resulting pressure on their currency had become evident in January itself as investors had begun pulling out funds in anticipation of policy rates increasing in AEs to mitigate inflationary pressures arising from a liquidity glut therein. Between January and July of 2022, foreign portfolio investors pulled out USD 48 billion out of the EMEs.

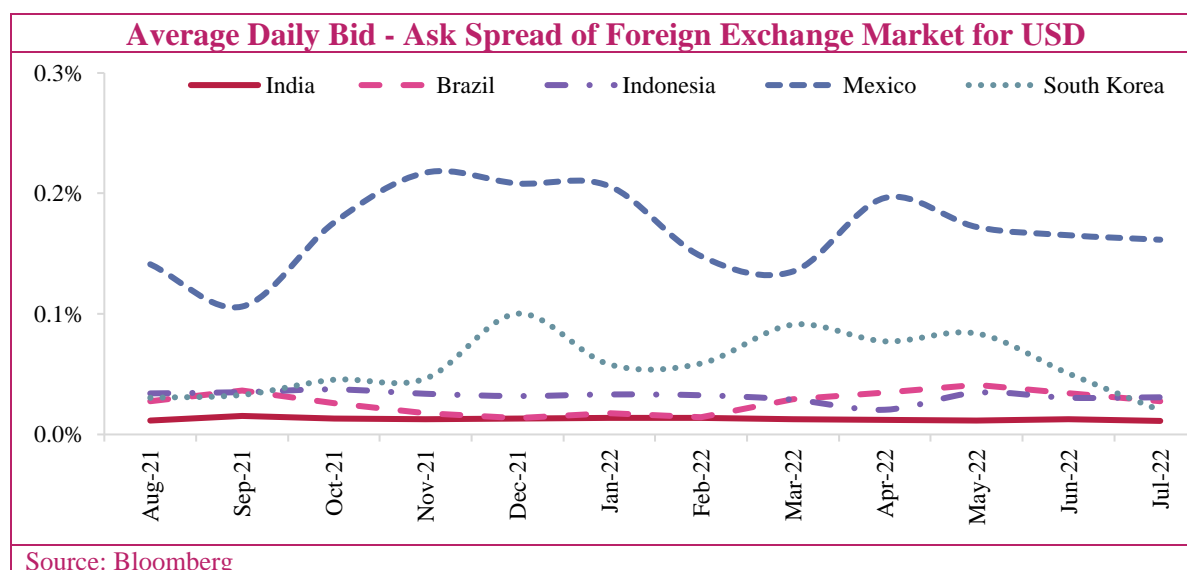


21. Discussions with the Industry have revealed that FPI outflows from India happened because India's capital market is relatively more liquid. Some granular assessment shows that this indeed is the case. The turnover ratio of equity markets, a measure of liquidity computed as the ratio of value of shares traded to market capitalisation, shows that the Indian equity market has a higher ratio and is thus relatively more liquid as compared to Indonesia, South Africa and Mexico.

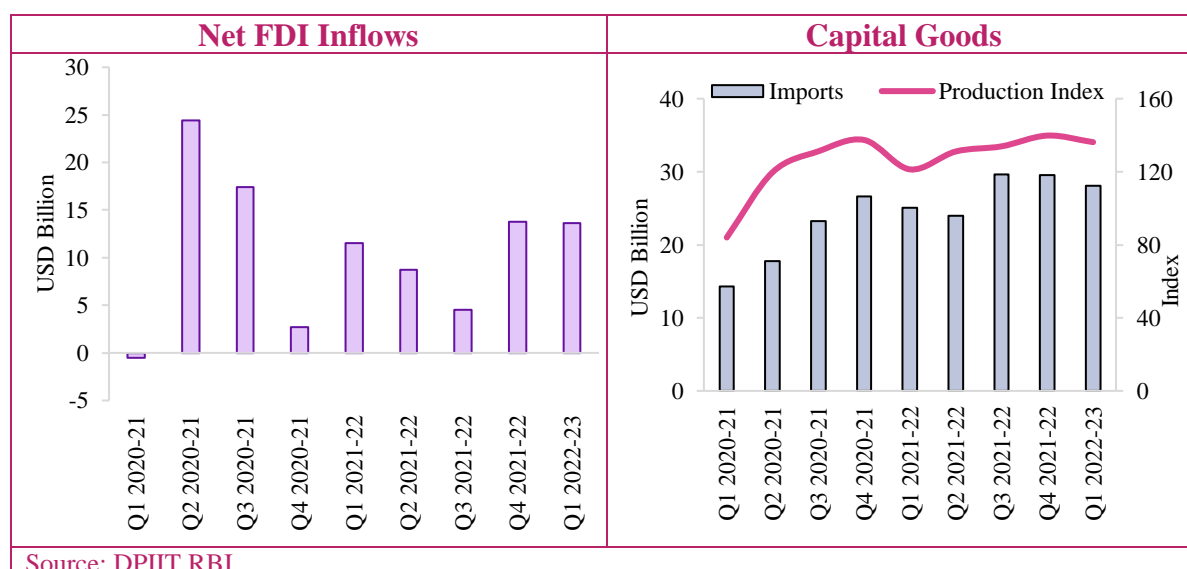


22. The bid-ask spread in the foreign exchange market is another indicator of liquidity. The lower the spread, the greater the liquidity in the market. During the period of January-July, 2022, India's forex market was the most liquid with an average daily bid-ask spread of 0.01 per cent, as compared to 0.32 per cent in South Africa, 0.17 per cent in Mexico and 0.03 per cent in Indonesia and Brazil respectively, implying that it is easier to trade USD in the

Indian forex market as compared to the other stated markets. High liquidity in the equity and forex market led to FPI outflows from India and depreciation of INR, just like in the case of other EMEs.



23. In August until 12th, FPIs had bought Indian financial assets worth USD 2.9 billion, net. The value of FPI’s Assets Under Custody (AUC) stood at USD 575 billion as of June end, 2022 indicating that over a period of 6 months, only 5 per cent of the AUC departed the country’s shores. 95 per cent of the AUC stayed on despite high market liquidity reflecting the confidence FPI have in India’s economic strength. Further, if more liquid forex markets can facilitate capital outflow, they can enable in-bound flows as well when the tide turns. It may well have, as mentioned earlier.



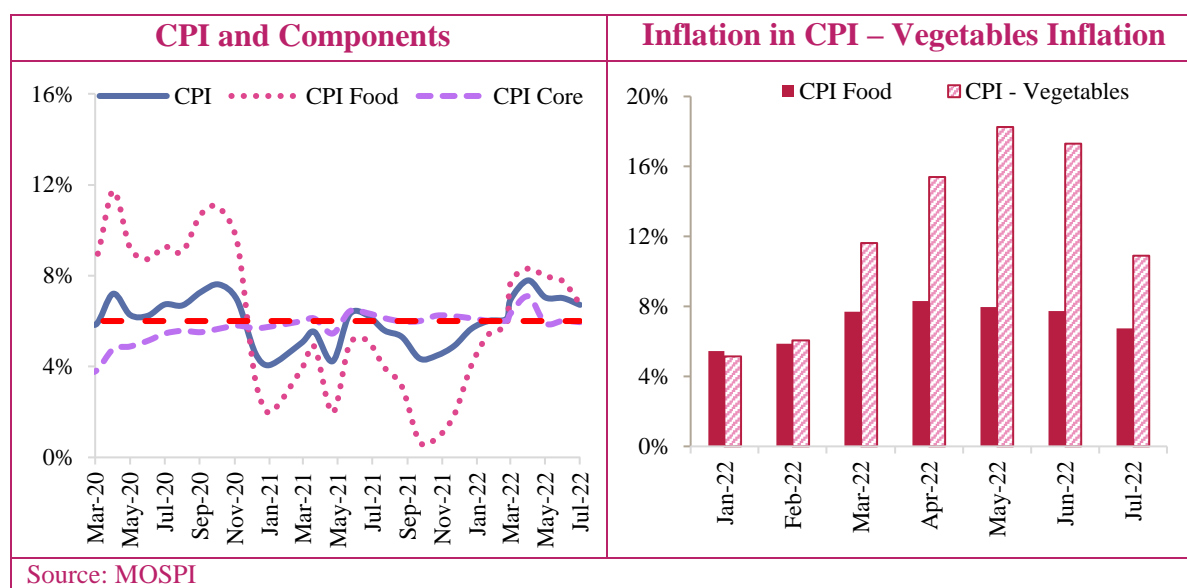
24. Global investor confidence in India’s economic landscape is further endorsed by net FDI inflows remaining robust at USD 13.6 billion in Q1 of 2022-23, as compared to USD 11.6 billion during the corresponding period of the last year. In sync, local investment activity

has also picked up, as is seen in the real sector where capital goods production and import of capital goods registered a robust double-digit growth during Q1 of 2022-23. Further, bank credit to infrastructure projects grew by 9.5 per cent to Rs. 12.1 lakh crore as of June 2022, and other crucial sectors such as engineering goods sector saw a double-digit credit growth. Government also continues to support investment activity with capital expenditure reaching Rs. 1.75 lakh crore during Q1 of 2022-23, which is 23.4 per cent of the budget estimate and 57 per cent higher as compared to the corresponding period of last year.

Inflation Dynamics

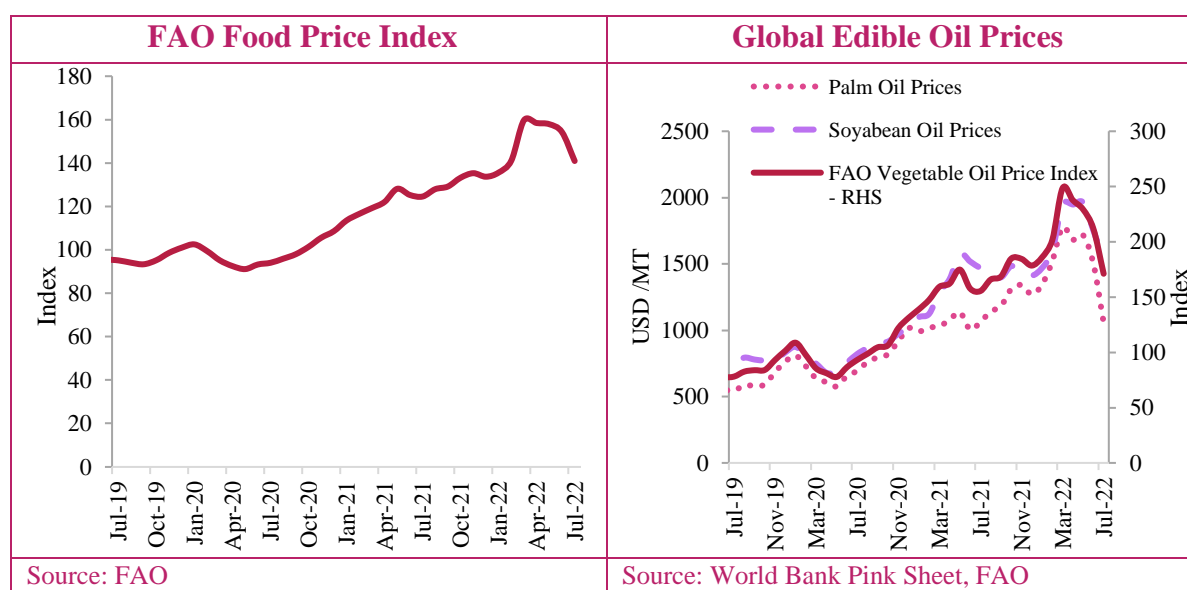
Softening of inflation broad-based in July, RBI's policy measures kept inflation expectations moderated

25. After a high of 7.8 per cent in April, 2022, retail inflation has been declining in India with the latest print of 6.7 per cent in July. The decline in inflation has been driven by retail food inflation, which to an extent has followed the decline in global food inflation as seen in FAO price index falling for four consecutive months to 140.9 points in July, 2022. An important component of the declining FAO price index has been the price of edible oil whose impact on bringing down retail food inflation in India has been profound.



26. The prices of edible oils, an important food commodity in India's import basket, declined with the easing of supply concerns in the exporting countries. The concerns had started to ease by the beginning of May itself with Indonesia lifting its exports ban within three weeks of imposing it and recovery in supplies of sunflower oil improving from Ukraine. Consequently, and on government's directions, branded edible oil makers slashed prices of palm oil, sunflower oil and soybean oil by up to Rs.15 per litre. The government subsequently went on to exempt customs duty and Agriculture Infrastructure Development Cess (AIDC) on yearly import of 20 lakh metric tonnes each of crude soya bean and sunflower oil for the year

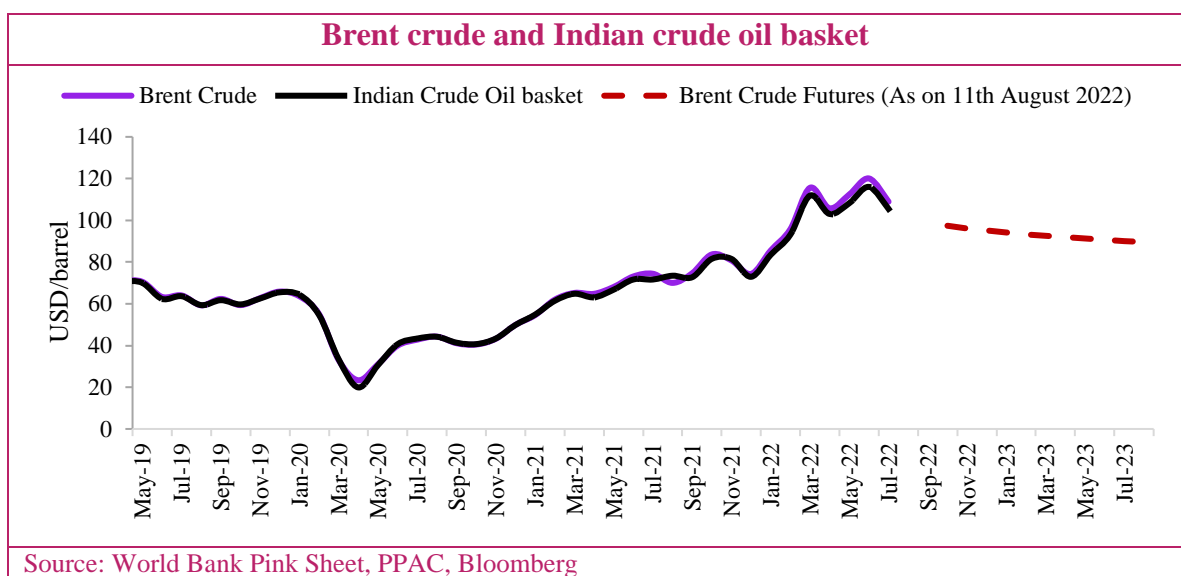
2022-23 and 2023-24. Stock limits imposed on all edible oils and oilseeds were next extended up to December 31, 2022 to curtail any unfair practices like hoarding, black marketing etc.



27. The steps taken by the government on other food products are now also beginning to bear down on their prices. The Government regulated the export of wheat and its products which helped in curbing the speculative activities in wheat trading and prevented the substantial increase in domestic prices of wheat and its products. The buffer stock of pulses maintained for price stabilization has been further moderating prices with calibrated release of pulses in the market. To address the downward rigidity in price of masur, import duty in July, 2021 and AIDC in February, 2022 were brought down to zero. Later in March, import of Tur and Urad under Free Category was extended till March 31, 2023.

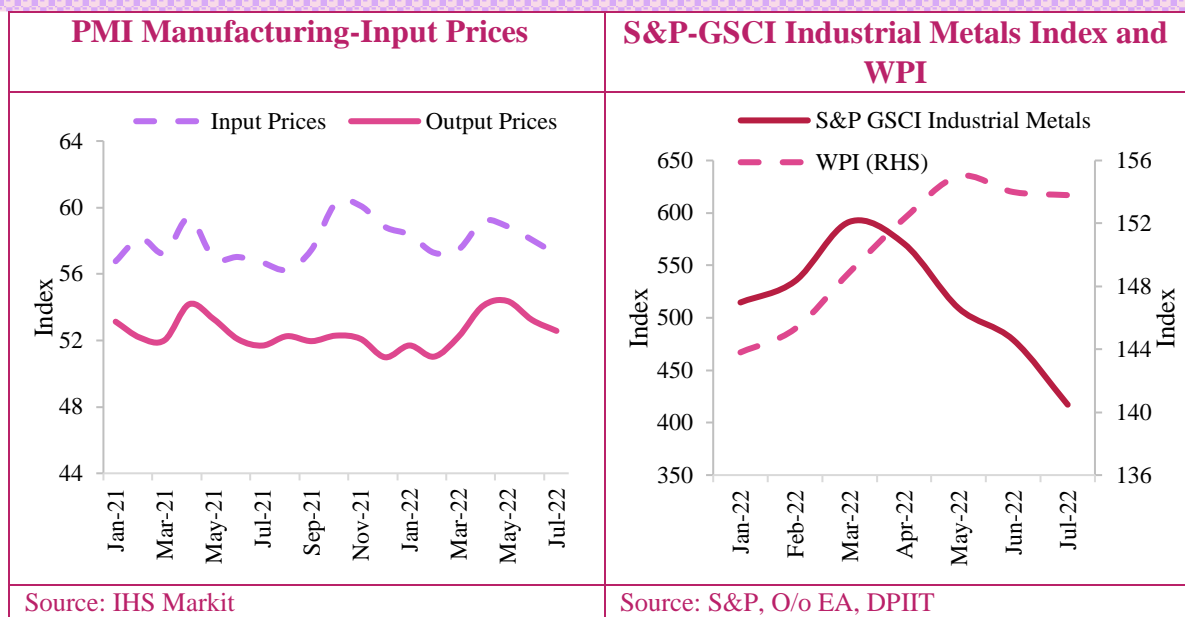
28. Vegetable price inflation, which was 18.3 per cent in May and 17.4 per in June, declined to 10.9 per cent in July contributing to overall decline in retail inflation. Price variations in vegetables are often on account of uncertain weather conditions but these can be mitigated by maintaining buffer stocks. To this end a buffer stock of 2.5 LMT of onion is being built in 2022-23 by procuring rabi-2022 harvest. The procurement till 13.07.2022 was 2.5 LMT. The stocks from the buffer will be released in a targeted and calibrated manner during lean season (Aug - Dec) to contain price rise. Going forward, a normal second half of the south-west monsoon is expected to narrow the deficit in rice and other kharif crop sowing activity, thereby ensuring adequate rice output. Additionally, the FCI has ample stock of rice grain which as of July 2022 is 3.5 times the buffer stock norm. Supplies of food are thus steadily being augmented to keep a check on food inflation.

29. Among non-food components, fuel and light inflation continues to increase. This could still be an outcome of supply chain issues although likely to be a temporary one, as declining global crude prices should eventually lower the inflation of fuel and light category as well.

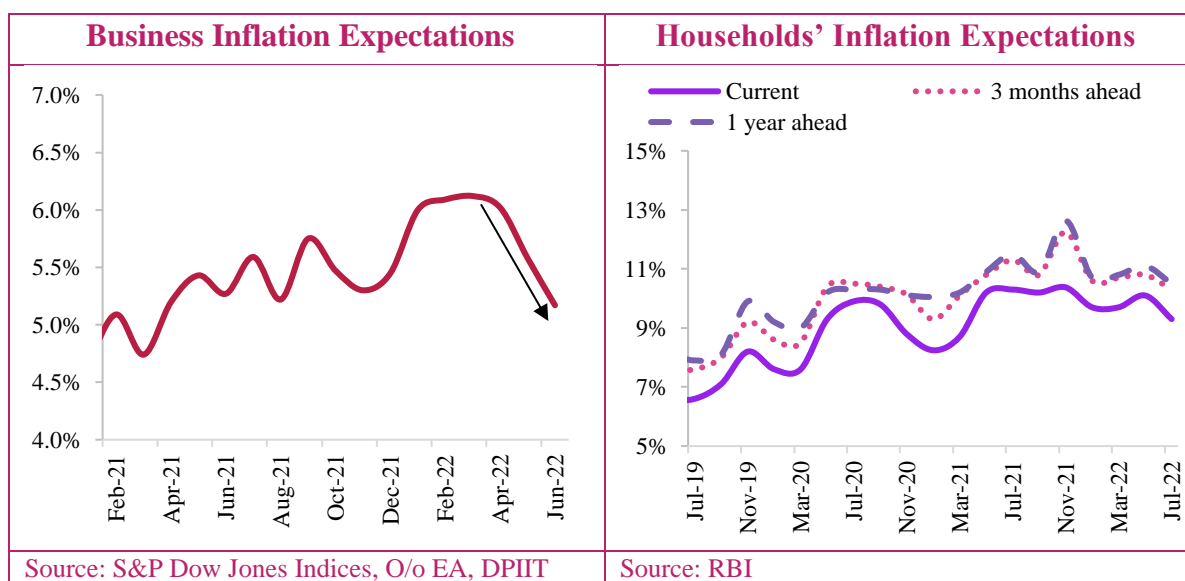


30. International prices of crude oil, derivatives of which feed into input prices across sectors, declined in July 2022 as the dampening of the global growth outlook combined with risks of recession in AEs weighed heavily on the demand for crude oil. The Organisation of Petroleum Exporting Countries (OPEC) has also revised downward its forecasts for global oil demand. The average price of Brent crude declined from USD 122.7/barrel in June 2022 to USD 111.9/barrel in July 2022. Consequently, the price of the Indian basket of crude declined from USD 116.0/barrel to USD 105.5/barrel. A part of the difference between the prices of Brent crude and the Indian basket of crude may be attributed to Indian refiners procuring discounted Russian crude in an attempt to diversify India’s import sources of crude oil.

31. Softening of inflationary pressures in India is further on the anvil with the prices of raw materials such as copper, tin, aluminium, iron ore, and zinc all having declined in July 2022. The S&P-GSCI Industrial Metals index continued its downward trend in July. As these raw materials feed into the manufacturing process, the decline in their prices is expected to soften the cost-push component of inflation, and consequently temper price pressures in the manufacturing sector. This is evident in the PMI Manufacturing report for July 2022 which stated that the rates of input cost inflation subsided to an eleven-month low as incidences of shortages diminished. The receding rates of input price inflation are subsequently moderating the inflation in output prices of manufacturing goods which was the weakest in four months. WPI Inflation too eased from 15.2 per cent in June to 13.9 per cent in July, marking the second successive month of moderation. The index declined sequentially as well, indicating slowing momentum in wholesale inflation.



32. Inflation in the services sector is also slowing down. Data from the PMI Services report for July 2022 indicates that input costs increased at the slowest rate since February 2022 which has consequently contributed to a softer rise in prices charged. Inflation in the services subcomponents of the CPI basket such as ‘health’, ‘transport and communication’, and ‘education’ has moderated.



33. The continued decline in commodity prices combined with the government’s fiscal measures and the RBI’s monetary measures have helped in lowering household inflation expectations. The July 2022 round of the RBI’s Households’ Inflation Expectation Survey (HIES) reveals that households’ median inflation perception for the current period moderated by 80 basis points. Furthermore, results from the June round of the IIM Ahmedabad’s Business Inflation Expectations Survey (BIES) have also shown that the one-year ahead business inflation expectations have further moderated to 5.17 per cent compared to 5.58 per

in the May round. The softening of inflationary expectations indicates that high inflation over the past few months has not entered the anchoring zone. Thus, as global price pressures ease, domestic inflation is expected to decline as well.

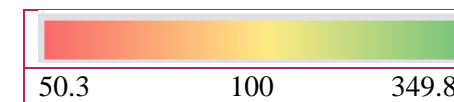
34. The RBI stayed on course in its efforts toward containing inflation. In its August meeting the RBI's MPC raised the policy repo rate, the standing deposit facility (SDF), and the marginal standing facility (MSF) by 50 basis points to 5.4 per cent, 5.15 per cent and 5.65 per cent. The committee maintained its inflation projection for FY 2022-23 at 6.7 per cent and has projected Q2, Q3, and Q4 inflation rates to be 7.1 per cent, 6.4 per cent and 5.8 per cent. In the absence of any further shocks to global commodity prices, particularly crude oil, India's inflation rate may well have peaked already for this cycle, thanks to RBI's monetary tightening and the government's policy measures.

Outlook

35. Going forward, kharif sowing supported by southwest monsoon coupled with higher MSP for Kharif crops is likely to enhance rural demand. Urban consumption is expected to benefit from the demand for contact-intensive services, improving performance of corporates and growing optimism of consumers. The robust production of capital goods along with the government's capex push and large expansion in bank credit will uphold the investment activity. The manufacturing sector is expected to gain from easing of input prices and a rise in consumer demand during the festive season. As per RBI Survey, manufacturing firms expect sustained improvement in production volumes and new orders in Q2:2022-23.

36. India's growth outlook for 2022-23, though lower than projections made before the outbreak of the conflict in Europe which resulted in sharply higher price for crude oil and other essential commodities, is still comfortably high and confirms the recovery of animal spirits and economic growth from the pandemic-induced contraction in 2021-22. Private sector and banking sector balance sheets are healthy and there is appetite to borrow and to lend respectively. Therefore, barring further adverse shocks to commodity prices and, thus, India's terms of trade, economic growth will consolidate and retain its momentum into 2023-24. Conservative estimates of medium-term potential growth for India may be missing a trick as they overweight the decline and subsequent stagnation in capital formation in the country in the second decade of the millennium. That was due to the stress in the financial system. As and when the Indian private sector embarks on the long-awaited capital expenditure cycle, building on the government's capital expenditure of recent years, India's potential and estimated economic growth performance in the rest of the decade will inevitably be revised higher.

With an aim to track the progress of the Indian economy since the outbreak of the Russia-Ukraine conflict, the HFI table has been rebased to January 2022.



Performance of High Frequency Indicators
Base Month Jan 2022= 100

Indicator	Feb-22	Mar-22	Apr-22	May-22	Jun-22	Jul-22
Agriculture						
Tractor sales	98.5	138.1	169.0	155.3	179.0	104.6
Fertilisers sales	84.8	80.4	91.2	102.4	110.5	
Industry						
8-Core Industries	94.8	109.3	99.7	103.2	99.0	
IIP-Consumer Durable goods	95.3	108.8	93.6	95.7	104.6	
IIP-Consumer Non-Durable goods	89.1	97.3	90.2	88.7	94.5	
Domestic Auto sales (Excluding Commercial vehicles)	94.4	106.3	101.0	108.8	114.5	121.6
Domestic Passenger vehicles sales	103.4	109.9	98.9	98.3	106.2	114.0
PMI Manufacturing	101.7	100.0	101.3	101.1	99.8	104.4
Power consumption	97.1	115.6	118.0	120.7	119.0	114.0
Natural gas production	91.0	100.9	98.8	101.8	98.3	
Cement production	95.1	112.7	96.9	93.8	100.2	
Steel consumption	89.0	95.6	89.2	93.3	84.7	89.7

Indicator	Feb-22	Mar-22	Apr-22	May-22	Jun-22	Jul-22
Services						
Electronic Toll Collection	111.5	113.5	120.4	120.9	123.3	115.4
Domestic Air Passenger Traffic	119.7	165.5	163.2	178.3	163.4	
Port Cargo Traffic	93.7	111.2	103.9	105.4	105.4	101.4
Rail Freight Traffic	92.8	107.9	94.7	102.1	97.3	94.7
PMI Services	100.6	104.1	112.4	114.4	115.0	107.8
Fuel Consumption	99.8	110.2	103.2	103.6	106.0	100.0
UPI (Value)	99.4	115.5	116.6	125.0	121.9	127.6
UPI (Volume)	98.1	117.1	116.8	128.8	127.0	136.2
Inflation						
WPI	101.7	104.2	106.3	107.8	107.8	107.6
CPI	100.2	101.2	102.7	103.6	104.2	104.6
CPI food	99.8	101.2	102.7	104.4	105.4	105.5
Crude price (Average of Brent, Dubai, WTI)	111.4	134.0	123.2	131.2	139.2	125.3
Crude Oil Indian basket	110.8	135.0	122.2	129.8	136.9	125.7
External Sector						
Merch Exports	105.5	126.2	113.0	111.0	120.4	103.1
Non-Oil Exports	98.7	113.4	103.9	99.7	103.6	97.7

Indicator	Feb-22	Mar-22	Apr-22	May-22	Jun-22	Jul-22
Non-Oil & Non-Gold Imports	93.8	109.7	103.2	101.2	111.9	103.8
Baltic Dry Index	104.2	139.9	126.1	167.1	135.7	
Exchange Rate	100.7	102.4	102.3	103.9	104.9	106.9
NEER	99.2	98.9	98.5	99.8	99.8	99.2
Net FDI	76.8	50.3	81.8	81.1	61.3	
Fiscal						
Gross Tax Revenue (Central Govt)	104.4	256.2	137.3	101.2	145.9	
Capital Expenditure	86.9	215.1	157.7	214.0	349.8	
GST	94.4	100.7	119.2	100.0	102.1	105.7
E-way Bill Volume	100.5	113.7	109.0	107.0	108.3	110.5
Monetary and Financial Markets						
M3	101.2	102.7	103.8	103.7	103.6	104.8
Non-Food credit	101.7	103.9	104.6	105.1	105.5	108.3
Sensex	97.0	101.0	98.4	95.8	91.4	99.2
Nifty	96.9	100.7	98.6	95.6	91.0	99.0

Note: Scale is reverse for inflation indicators.

For feedback, contact:

1. Mr. Rajiv Mishra, Economic Adviser (r.mishra67@nic.in)
2. Ms. Shreya Bajaj, Deputy Director (shreya.bajaj@gov.in)
3. Ms. Megha Arora, Deputy Director (megha.arora1506@gov.in)
4. Ms. Sonali Chowdhry, Consultant (sonali.chowdhry@nic.in)
5. Mr. Bharadwaja Sastry Adiraju, Young Professional (bharadwaj.adiraju@govcontractor.in)