BBVA RESEARCH

India Flash

Q1 2013 GDP meets subdued expectations, making another 25 bps rate cut more likely

As expected, India's 1Q13 GDP growth inched up to 4.8% y/y (BBVA: 4.7%, Consensus: 4.8%) from an upwardly revised 4.7% (4.5% previously) in 4Q12 on favorable base effects and a modest pick up in industrial activity, which offset sluggish services and agriculture growth. While weak final demand and limited fiscal spending weighed on services output, recent investment reforms alongside aggressive monetary easing (cumulative 75 bps rate cuts since January) helped improve the business environment for manufacturing and construction firms. Looking ahead, gradually improving global demand, combined with softening domestic inflation (WPI inflation of 4.9% in April) and higher capital spending ahead of the national elections in 2014 bodes well for growth prospects. Delays in policy execution and weak business confidence, however, present near term risks. Sub-par growth is likely to prompt the RBI to implement another 25 bps rate cut on June 17, probably the last for the year. With growth expected to rise in the coming quarters, we maintain our full-year GDP projection of 5.7% y/y in 2013, up from the 2012 outturn of 5.1%.

- **With fiscal consolidation on track, there is room for higher government spending to support growth in the coming months.** Limited fiscal spending amid concerns over the high fiscal deficit has weighed on growth. Reassuringly, fair progress on fiscal reforms in recent months, particularly on diesel prices, leaves scope for a ramp up in capital spending, which in turn should support final demand going ahead.

- **A renewed push to reform momentum is needed to support growth:** The pace of India's investment reforms has slowed with key legislative reforms, including the land acquisition bill and insurance bill yet to be passed and limited progress in addressing India's energy shortage. Mining sector growth fell 3.1% y/y in 1Q13, its second successive contraction, highlighting the need to resolve environmental issues and expedite investment project approvals.

- **An improving global growth outlook bodes well for the trade balance.** The pace of contraction in export growth eased in 1Q13 (-0.6% y/y vs -3.5% y/y in 4Q12), even as imports slowed further. Better growth prospects in advanced economies, particularly for the US, bodes well for India's current account balance going forward, which we expect to improve from 5.0% of GDP in 2012 to a still high level of 4.1% in 2013. This should help stabilize the weakening rupee, which at 56.7 per USD has depreciated by 5.3% since the beginning of May.

Chart 1
India's 1Q13 GDP growth remains subdued at 4.8% y/y

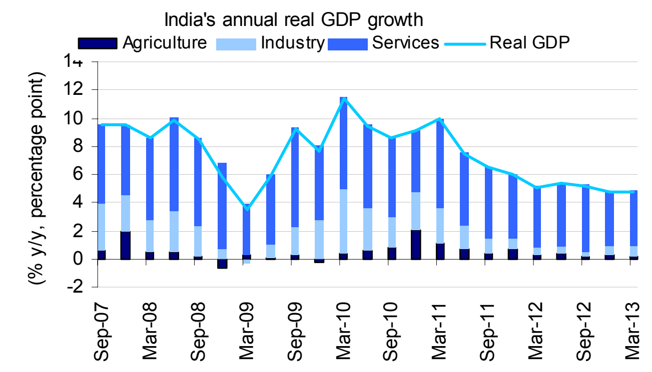
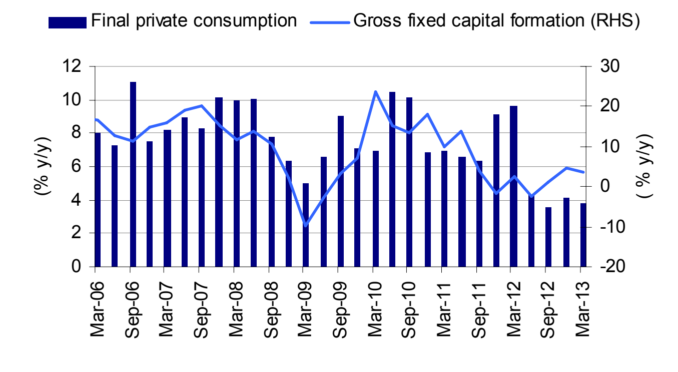


Chart 2
Slowing investment and consumption growth have weighed on GDP



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