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Economics Group

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India Releases Disappointing GDP Data for Q2-2016

GDP growth in India continued to clip along in excess of 7 percent in Q2. However, the underlying details of the GDP release were disappointing.

Domestic Economy Shows Signs of Deceleration in Q2

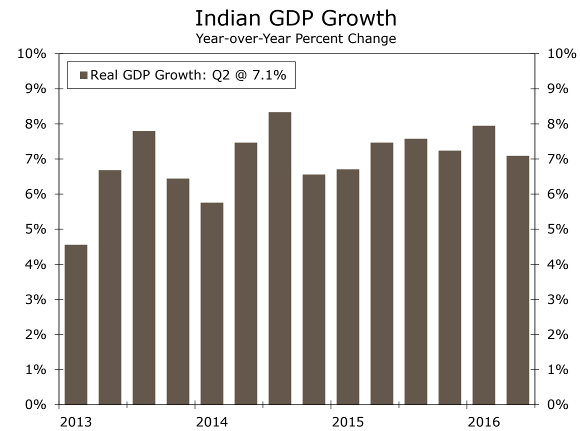
Data released this morning showed that real GDP in India rose 7.1 percent on a year-ago basis in Q2-2016 (top chart). Not only did the outturn represent a step-down from the 7.9 percent rate that was registered in the first quarter, but it was significantly below the 7.6 percent rate that the consensus forecast had anticipated. Moreover, the underlying details were weaker than the headline growth figure implied.

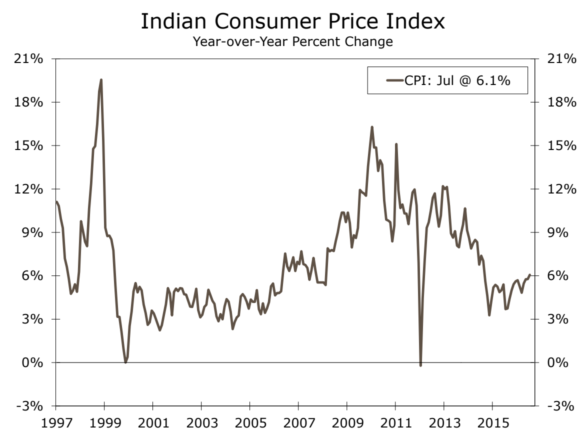
In that regard, growth in personal consumption expenditures downshifted markedly to 6.7 percent in Q2 from 8.3 percent in Q1, and investment spending fell 3.1 percent on a year-ago basis. This deceleration in domestic demand showed up in the import component, which sank 5.8 percent. On a positive note, exports rose 3.2 percent, the first positive growth rate in five quarters. Consequently, net exports, which are the difference between exports and imports, boosted the overall GDP growth rate by 2.1 percentage points. But this large contribution to GDP growth from the external sector was due, at least in part, to weakness in imports. (Recall that imports reduce GDP, so a decline in imports actually raises the level of GDP.) Likewise, weakness in imports reflects deceleration in domestic demand. In other words, the underlying details of the GDP release show that the Indian economy is not quite as strong as many market participants had thought.

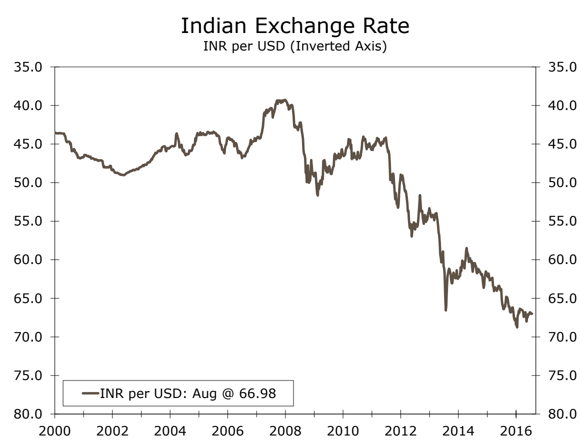
Inflation Has Trended Higher This Year

Not only was the growth performance in Q2 weaker than expected, but recent inflation indicators have been disappointing as well. After trending markedly lower between 2013 and 2015, CPI inflation has edged higher again this year (middle chart). Much of the increase in the overall inflation rate this year reflects acceleration in food and beverage prices, which account for nearly one-half of India's consumer price index. The good news is that the country has enjoyed a good monsoon this year, which should help stabilize food prices. Consequently, CPI inflation should recede again later this year. Until the central bank sees the inflation fever actually break, however, it may be slow to ease policy further. Lower interest rates would help to support growth in economic activity. But if the central bank is slow to ease policy further, then growth may weaken a bit more in coming quarters.

Similar to many other emerging market currencies, the Indian rupee has depreciated markedly against the U.S. dollar over the past few years (bottom chart). Our currency strategy team does not look for much further depreciation of the rupee from current levels, although they also do not expect the Indian currency to stage a sharp comeback vis-à-vis the greenback anytime soon.







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