

Trade balance slips into deficit again

India's merchandise trade balance slipped into deficit of US\$4.8bn in July 2020 after turning into a modest surplus of US\$793mn in June 2020. While imports saw some revival on a MoM basis, their general trend of contraction continues to be higher than that of exports, weighed down by falling aggregate demand.

India's import bill declined by a much lower 28.4% YoY in July following a 52.6% YoY contraction in 1Q FY21, led by a significant recovery in imports of vegetable oils, gold (largely reflecting higher gold prices), electronic goods and chemicals (pharmaceuticals and fertilizers). Oil imports, however, declined by a huge 32% YoY in July despite a favourable base, reflecting a consequence of weak demand and benign crude oil prices. Exports on the other hand continued to improve, falling by a much lower 10.2% YoY in July, largely led by engineering goods and pharmaceuticals, partly offset by a huge drop in exports of petroleum products, gems & jewellery, readymade textiles and electronic goods.

Exports are expected to continue to do better than imports as implementation of localised lockdowns by states in the wake of rising COVID-19 cases is expected to continue to weigh on domestic consumption demand, with low crude oil prices putting additional pressure on imports. Moreover, the second-order impact of the lock-down in the form of job losses and decline in disposable incomes may keep discretionary demand weak for an extended period. That said, a low base is likely to provide some support to imports over the next few months. This is likely to result in a significant contraction in trade deficit in FY21 (-77.7% YoY in 4MFY21), thereby translating into a current account surplus of ~0.5% of GDP—the first surplus in 17 years. This, along with a surge in foreign exchange reserves to all-time high levels (US\$538bn as on August 7th, +US\$81bn YTD), bodes well for the INR.

- Pace of contraction in exports dropped further in July: Exports recovered further in July, falling by 10.2% YoY to US\$23.6bn but growing at 7.9% on a sequential basis (MoM). This was led by a continued recovery in exports of engineering goods (+8.5% YoY) and a strong growth in exports of essential goods for yet another month, viz. agricultural commodities (rice), ores and pharmaceuticals. Exports of consumption-related items such as gems & jewellery, readymade garments and electronic goods remained weak for yet another month, falling by 49.6%, 22.1% and 17.4% YoY respectively, indicating weak global discretionary demand as well as reduced production levels in the wake of continued labour availability issues and social distancing norms. Exports of petroleum products also declined by a huge 51.5% YoY in July, reflecting low crude oil prices as compared to the same period last year. Excluding, petroleum products and gems & jewellery, exports actually registered a modest growth of 3.4% YoY in July.
- Imports recovers sharply on a sequential basis, but YoY contraction remains significant: **India's import bill** declined by a much lower 28.4% YoY in July following a 52.6% YoY contraction in 1Q FY21. On a sequential basis, the improvement was quite stark, with imports rising by a huge 34.8% MoM as economic activity picked up amid continued easing of restrictions. The improvement was largely led by a significant recovery in imports of vegetable oils, gold (largely reflecting higher gold prices), electronic goods and chemicals (pharmaceuticals and fertilizers). Oil imports, however, declined by a huge 32% YoY in July despite a favourable base, reflecting a consequence of weak demand and benign crude oil prices. Excluding oil and gold, imports fell by 29.1% YoY in July, much lower than 44% drop in 1Q FY21. A recovery in imports led to trade balance slipping back to deficit of US\$4.8bn in July after registering a modest surplus of US\$793mn in June—the first since Jan'02.

Exports recovered further in June, falling by 10.2% YoY vs. 36.6% YoY drop in 1Q FY21.

Imports declined by 28.4% YoY in July vs. 52.6% YoY contraction in 1Q FY21.

Trade balance slipped into deficit again of US\$4.8bn in July.

- Expect current account surplus in FY21: Exports are expected to fare better than imports in FY21, benefiting from an aggressive global policy response and relatively lenient lockdown restrictions. India, on the other hand, has seen one of the most stringent and extended lockdowns which has adversely impacted consumption as well as investment demand. Rising number of COVID-19 cases in India has now led to states resorting to localised lockdowns, which in turn is expected to continue to weigh on domestic demand. In fact, discretionary demand is expected to remain weak in India for an extended period in the wake of falling disposable incomes and changing consumer behaviour. This, along with lower crude oil prices, is expected to result in a significant contraction in trade deficit in FY21, translating into a current account surplus of 0.5% of GDP in FY21—the first surplus in 17 years, vs. a deficit of 0.9% of GDP in FY20. This coupled with a surge in foreign exchange reserves to all-time high levels (US\$538bn as of August 7th, +US\$81bn YTD) bodes well for the INR.

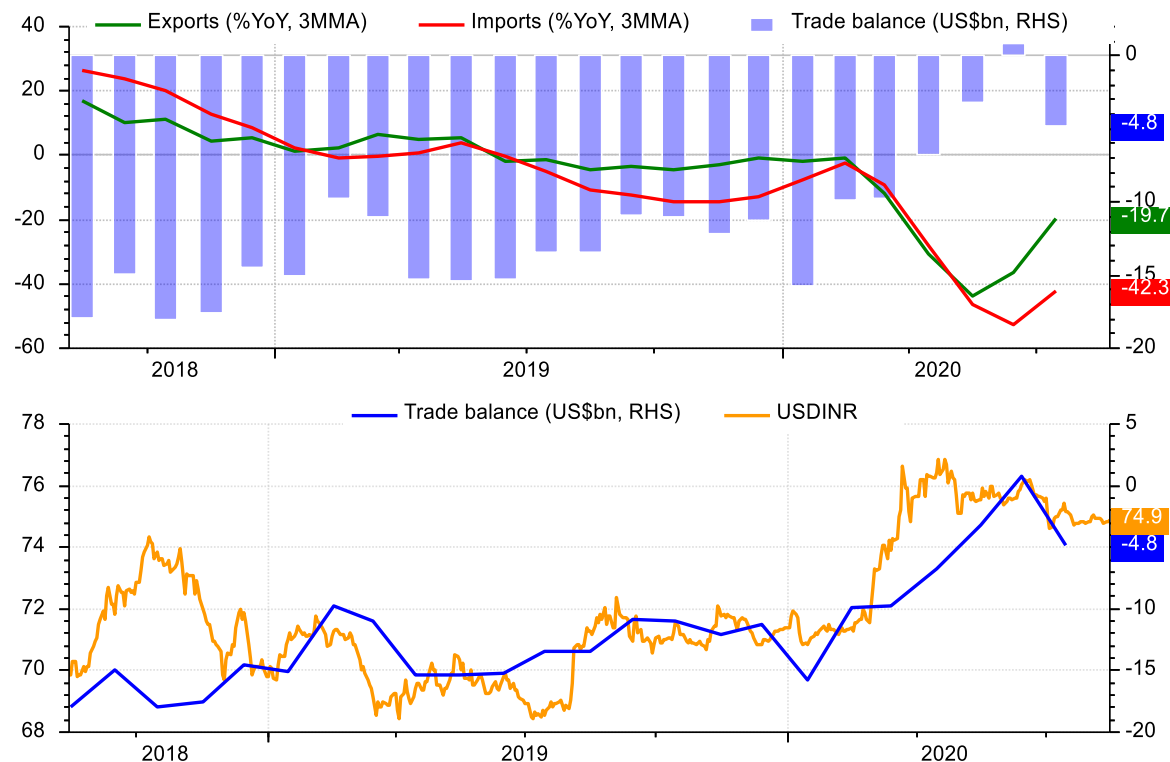
A significant deterioration in trade deficit is likely to translate into a current account surplus of 0.5% of GDP in FY21 vs. a deficit of 0.9% of GDP in FY20.

Figure 1: India monthly trade balance for July 2020

	Exports		Imports								Trade balance
	US\$ bn	%YoY	Total (US\$ bn)	%YoY	Oil imports (US\$ bn)	%YoY	Non-oil imports (US\$ bn)	%YoY	Gold Import (US\$ bn)	%YoY	US\$ bn
Jul-20	23.6	-10.2	28.5	-28.4	6.5	-32.0	21.9	-27.3	1.8	4.2	-4.8
Jun-20	21.9	-12.5	21.1	-48.5	4.9	-56.0	16.2	-45.7	0.6	-77.4	0.8
Jul-19	26.3	2.2	39.8	-10.4	9.6	-22.2	30.2	-5.9	1.7	-42.2	-13.4
FY21TD	74.9	-30.1	88.9	-47.7	19.6	-56.3	69.3	-44.5	2.5	-81.2	-14.0

Source: Ministry of Commerce, CMIE Economic Outlook, NSE

Figure 2: India monthly trade balance trend



Source: Refinitiv Datastream, NSE

Figure 3: Non-oil, non-gold imports trend
 Non-oil non-gold imports recovered in July, falling by 29.1% YoY vs. 44% YoY drop in 1Q FY21.

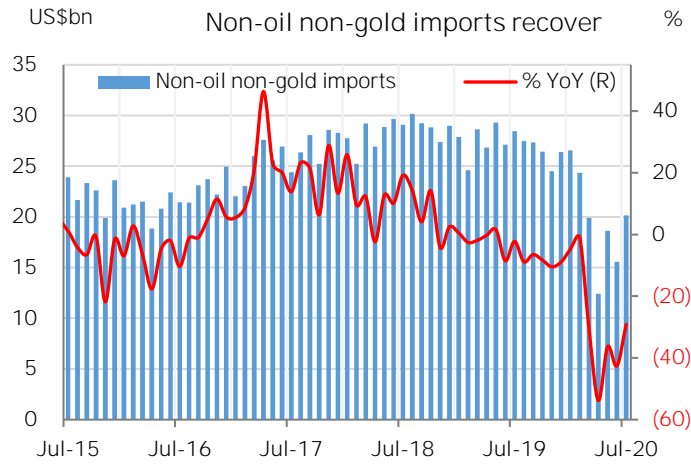
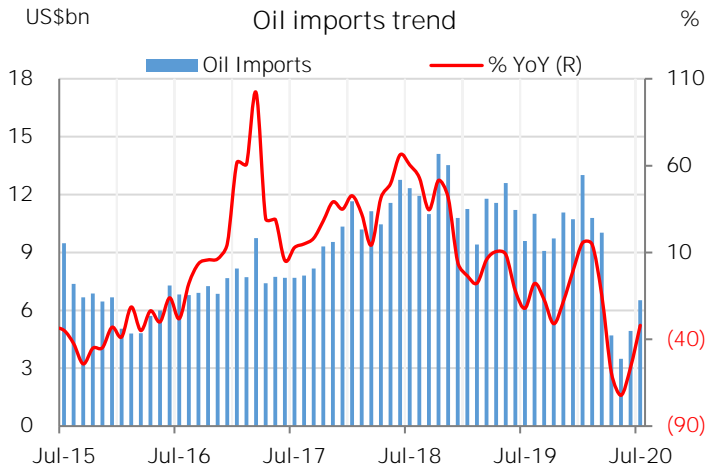


Figure 4: Oil imports trend
 Oil imports fell by a 32% YoY in July, reflecting low crude oil prices, translating into a drop of 56.3% YoY in FY21 TD.

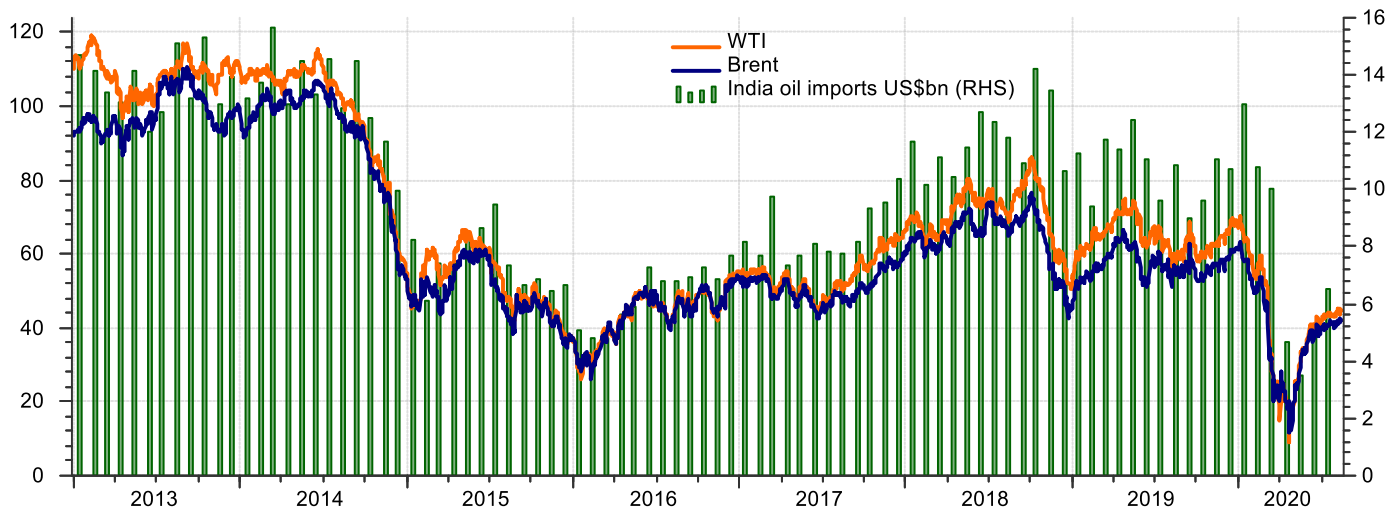


Source: Ministry of Commerce, CMIE Economic Outlook, NSE

Figure 5: Oil imports vs. Brent crude oil prices trend

An increase in crude oil prices over the last couple of months, coupled with continued lifting of mobility restrictions, has translated into a pick-up in oil imports on a sequential basis.

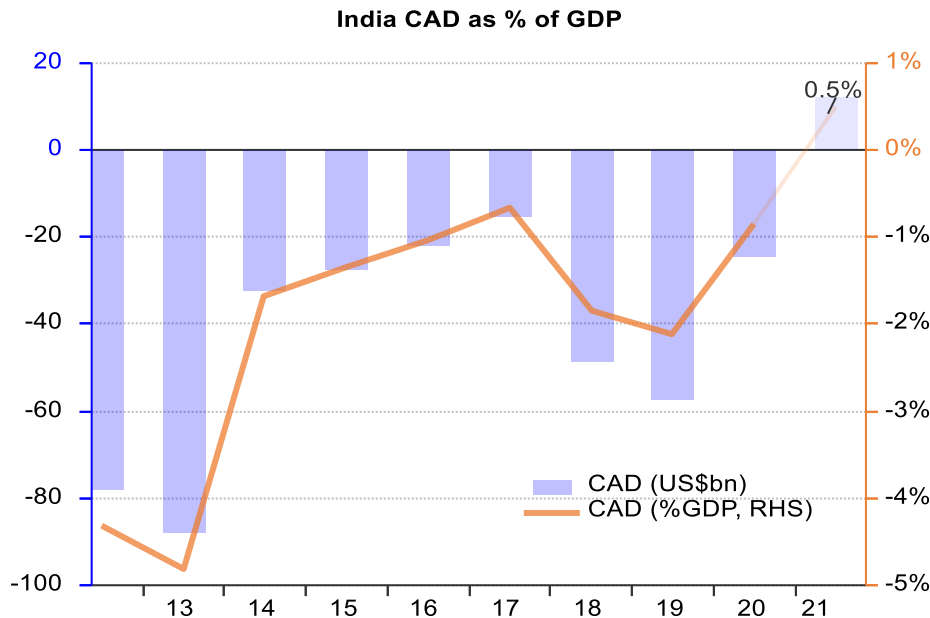
Oil imports vs. prices (US\$)



Source: Refinitiv Datastream, NSE

Figure 6: Current account balance expected to turn surplus in FY21

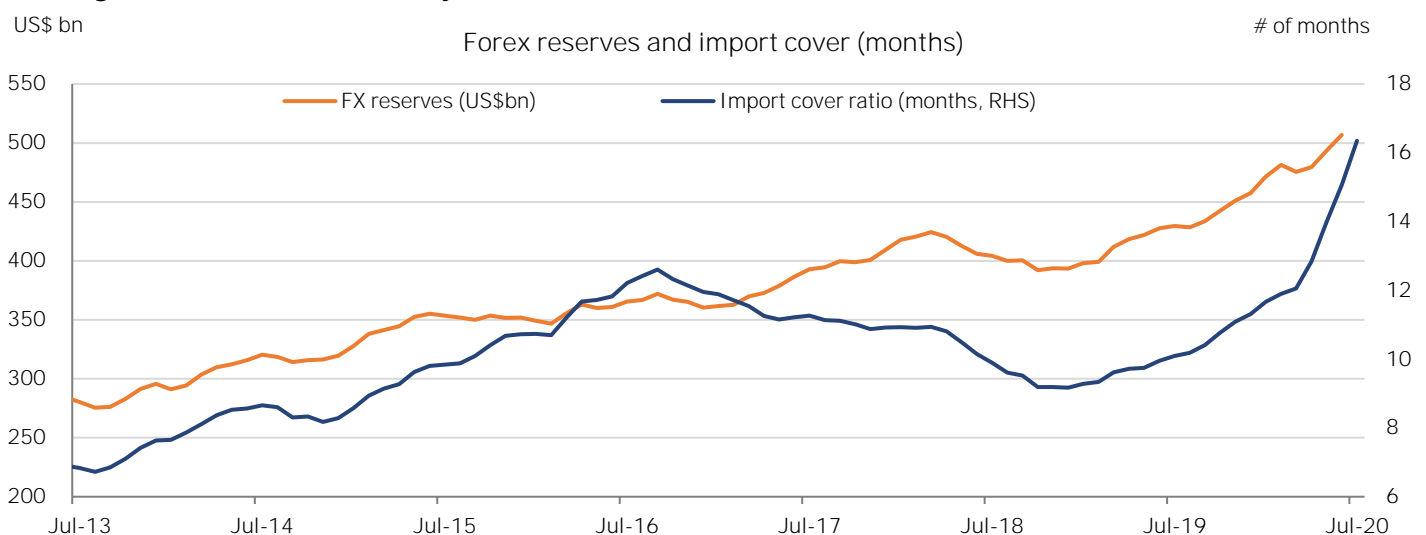
A significant contraction in trade deficit in FY21 is expected to translate into a current account surplus of 0.5% of GDP in FY21—the first surplus in 17 years, vs. a deficit of 0.9% of GDP in FY20.



Source: Refinitiv Datastream, NSE

Figure 7: **India's foreign exchange reserves and import cover**

A significant accretion to forex reserves over the years, and particularly this year (+US\$ 81bn in 2020 till date), has resulted in a significant improvement in import cover, further supported by moderation in domestic demand. After falling to eight months in 2014, India's import cover has improved sharply to nearly 16 months now, thereby significantly reducing India's external vulnerability.



Source: CMIE Economic Outlook, NSE. Import cover is calculated as the ratio of forex reserves at the end of the period to average monthly imports over the last 12 months

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