Macro Review

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Trade deficit narrows to three-month lows in February

India's merchandise trade deficit contracted further to a three-month low of US$12.6bn in Feb'21 from US$14.5bn in the previous month, primarily led by sequential tapering of imports accompanied with a mild uptick in exports. Thanks to a strong 7% growth in imports, however—attributed to a sharp surge in gold and core (non-oil, non-gold) imports—the deficit was meaningfully higher than Feb'20's US$10.2bn. Export growth on the other hand moderated from a 22-month high of 6.2% YoY in Jan'21 to a modest 0.7% in Feb, largely because of container shortages across the country.

Steady consumption demand as reflected through the core import group (three-month avg. of 7.6%YoY), coupled with the regained momentum in non-oil exporting activity (three-month avg. of 7.1%YoY), augers well for the overall economic recovery. That said, the sequential tapering of growth momentum seen in several high-frequency indicators including core imports, auto sales, cargo port/rail freight traffic, and petrol consumption warrants caution ahead, with the recent COVID-19 surge adding to the woes. An effective implementation of COVID vaccination drives is therefore crucial for a sustainable global trade recovery. We maintain expectations of a current account surplus of 1.1% of GDP in FY21, attributed to a sharply lower trade deficit (-42% YoY in Apr-Feb'21) and steady services exports. In FY22, we expect current account to slip into deficit again (est.: 0.7% of GDP), even as global risk-on sentiments are likely to keep the BoP in a comfortably surplus position.

Emerging market (EM) currencies have lately come under pressure in the wake of hardening oil prices, escalating US bond yields and a stronger US macroeconomic landscape translating into dollar rally. The INR is no different, having witnessed a significant volatility over the last few weeks, but has outperformed the broader EM pack. Going ahead, while the INR is likely to move in tandem with global cues, it should exhibit greater resilience relative to its peers due to the war chest of forex reserves (US$580bn as of March 5th, +109bn FYTD), favorable capital flows, healthy pace of inoculations and expectations of continued economic recovery.

- Exports grew sequentially but lost momentum on a YoY basis: After growing at a 22-month high of 6.2% YoY in Jan'21, exports witnessed a moderation in annual growth momentum in Feb'21, up 0.7% YoY, but expanded sequentially (+1.8% MoM). This is primarily attributed to container shortages across the country and supply disruptions in the last week of Feb'21 due to rising COVID-19 cases. The moderating pace of YoY drop in exports of petroleum products (-21%YoY in Feb'21 vs. 32%YoY in Jan'21) was outweighed by a marked slowdown in performance of non-oil export segment—up by 3.7%YoY in Feb vs. +11.5% YoY in Jan'21. While essential items such as other cereals (546.5%), oil meals (245.5%), iron ore (167.8%) and drugs (14.7%) continued to show stellar growth, non-essential items such as leather (-21.6%), gems & jewellery (-11.2%), ready-made garments (-8.5%), electronic goods (-5.8%) and engineering goods (-2.4%) continued to falter. Export growth in FY21 thus far (Apr'20-Feb'21) stood at -12.5% YoY.

Exports continued to show uptick on sequential basis, but moderated on a YoY basis from 22 month high of 6.2%YoY in Jan to 0.7%YoY in Feb.

- Import growth fell sequentially but remained healthy on a YoY basis: Import growth picked up meaningfully to 7% YoY in Feb from +2% YoY in the previous month, primarily led a sharp surge in gold imports (+124% YoY)—a consequence of price moderation and healthy wedding demand, as well as robust growth in non-oil non-gold imports (+6% YoY). Alongside, the YoY contraction in oil imports came off from 28%YoY to 17%YoY in Feb. Within the core import group, import growth of electronic goods remained quite resilient, registering 38% YoY print—indicating a steady recovery in consumption demand. Growth in inbound shipments for wood (19%YoY), iron and steel (23% YoY), pharma (15.4%YoY), chemicals (45%YoY) and metallic ferrous ores (30% YoY) continued to exhibit signs of industrial demand recovery. Imports, however, lost momentum on a sequential basis and declined by 3% MoM, thanks to an 8% MoM contraction in non-oil non-gold imports, thereby

Imports rose by a 7% YoY in Feb'21 vs. +2% in Jan'21 led by robust gold/non-oil non-gold imports that continue to point to strong industrial/ consumption demand.

giving us reasons to be cautious ahead particularly in the wake of resurgence of COVID-19 infections. Imports on a cumulative basis (Apr'20-Feb'21) are down 23% as compared to the same period in the previous year.

- Trade deficit narrowed to a three-month low: Trade deficit moderated further from US$14.5bn in Jan'21 to a three-month low US$12.6bn in Feb'21, primarily led by sequential tapering of imports accompanied with a mild uptick in exports. Trade deficit, however, was higher than the year-ago levels (US$10.2bn in Feb'20) due to a sharp increase in gold and core import group segment on a YoY basis. On a cumulative basis, trade deficit is down 42% YoY FYTD.

Trade deficit moderated to a three-month low of US$ 12.6bn in Feb'21 from US$14.5bn in Jan'21.

- External environment to remain conducive: Steady consumption demand as reflected through the core import group (three-month avg. of 7.6%YoY), coupled with the regained momentum in non-oil exporting activity (three-month avg. of 7.1%YoY), augers well for the overall economic recovery. That said, the sequential tapering of growth momentum seen in several high frequency indicators including core imports, auto sales, cargo port/rail freight traffic, and petrol consumption warrant caution ahead, with the recent resurgence in COVID cases adding to the woes. An effective implementation of COVID vaccination drives is therefore crucial for a sustainable global trade recovery.

  We maintain our expectations of a current account surplus of 1.1% of GDP in FY21, attributed to a sharply lower trade deficit (-42% YoY in Apr-Feb'21) and steady services exports. In FY22, we expect current account to slip into deficit again, with our estimate pegged at 0.7% of GDP, as import growth is expected to outpace export growth. While exports should benefit from a synchronized global recovery and the Government's PLI (Production-Linked Incentive) scheme, imports are expected to do better thanks to higher crude oil and commodity prices as well as recovery in consumption demand. Nevertheless, continued foreign capital flows amidst global risk-on environment is likely to keep the BoP (Balance of Payments) in a comfortably surplus position.

We estimate a current account surplus of 1.1% of GDP in FY21 but expect a deficit of 0.7% of GDP in FY22.

Sustenance of foreign capital inflows should keep the BoP in a comfortably surplus position.

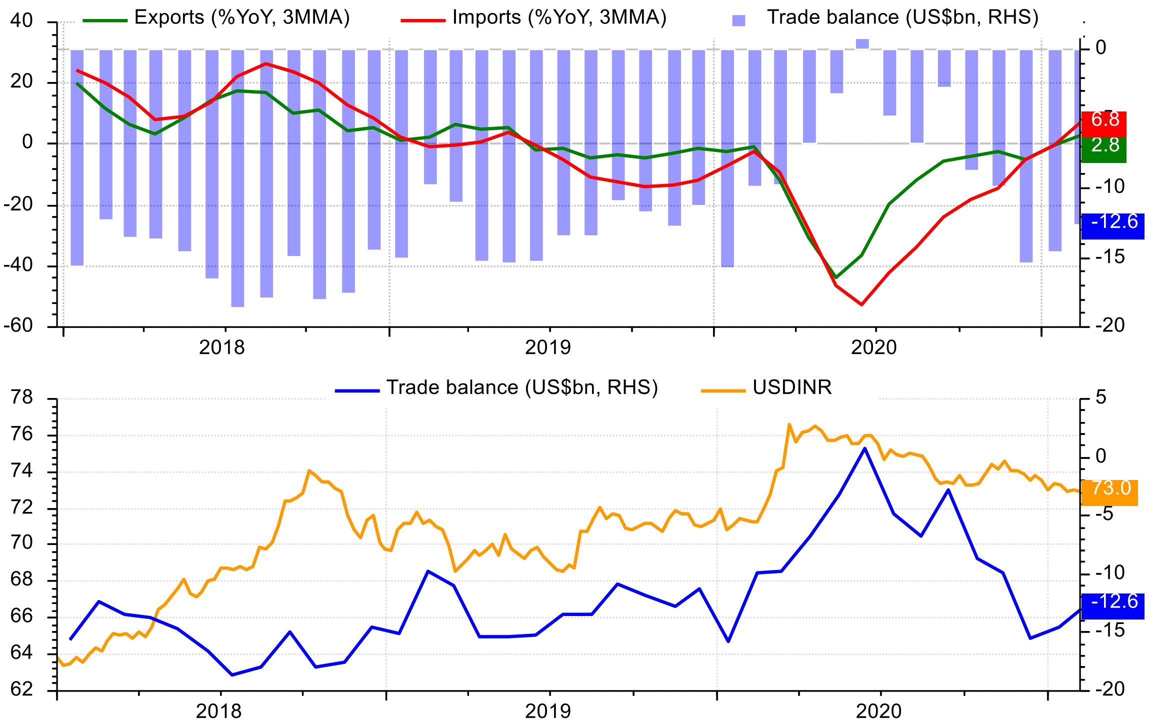
- INR likely to move in tandem with global cues: EM currencies have lately come under pressure in the wake of hardening oil prices, escalating US bond yields and a stronger US macroeconomic landscape translating into dollar rally. The INR is no different, having witnessed a significant volatility over the last few weeks, but has outperformed the broader EM pack. Going ahead, while the INR is likely to move in tandem with global cues, it should exhibit greater resilience relative to its peers due to the war chest of forex reserves (US$580bn as of March 5th, +109bn FYTD), favourable capital flows, healthy pace of inoculations and expectations of continued economic recovery.

Figure 1: India monthly trade balance for February 2021

	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
Feb-21	27.9	0.7	40.5	7.0	9.0	-16.6	31.6	16.3	5.3	123.9	-12.6
Jan-21	27.4	6.2	42.0	2.0	9.4	-27.7	32.6	15.8	4.0	154.7	-14.5
Feb-20	27.7	3.3	37.9	3.6	10.8	14.5	27.1	-0.2	2.4	-8.5	-10.2
FY21TD	256.7	-12.0	345.1	-22.1	72.3	-40.0	272.8	-15.5	26.1	-3.3	-88.4

Source: Ministry of Commerce, CMIE Economic Outlook. FY21TD: Apr'20-Feb'21

Figure 2: India monthly trade balance trend



Source: Refinitiv Datastream.

Figure 3: Non-oil, non-gold imports trend

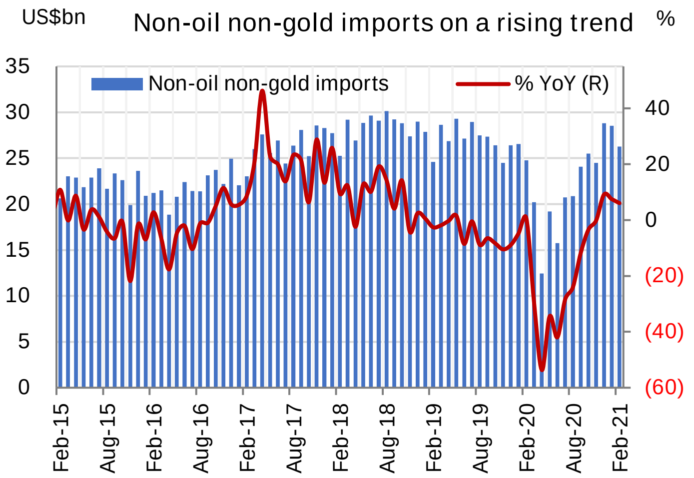
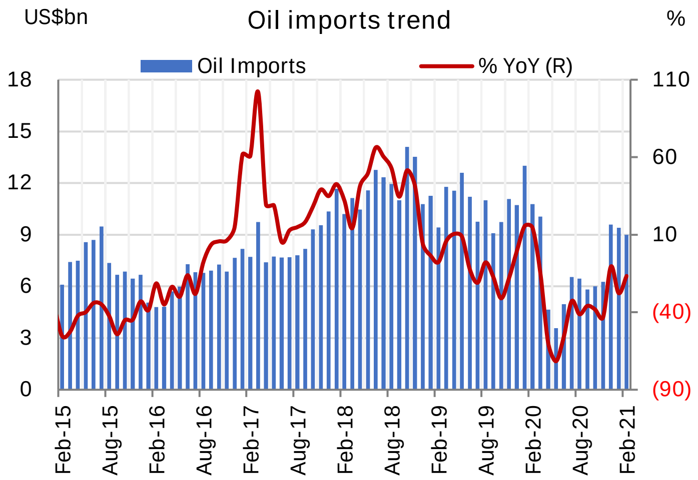
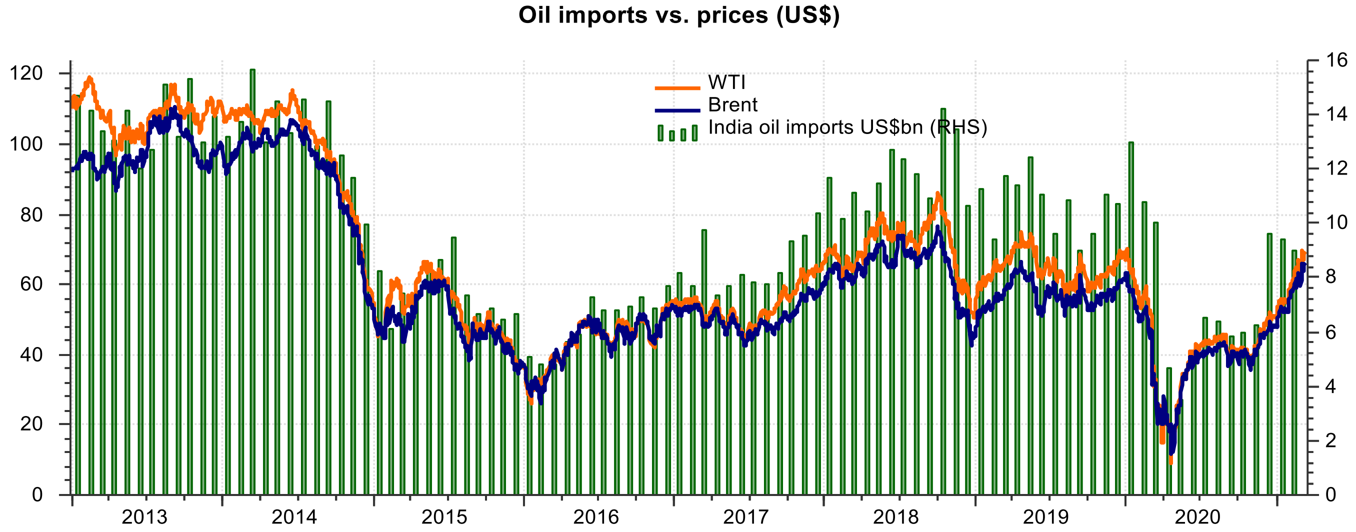


Figure 4: Oil imports trend



Source: Ministry of Commerce, CMIE Economic Outlook.

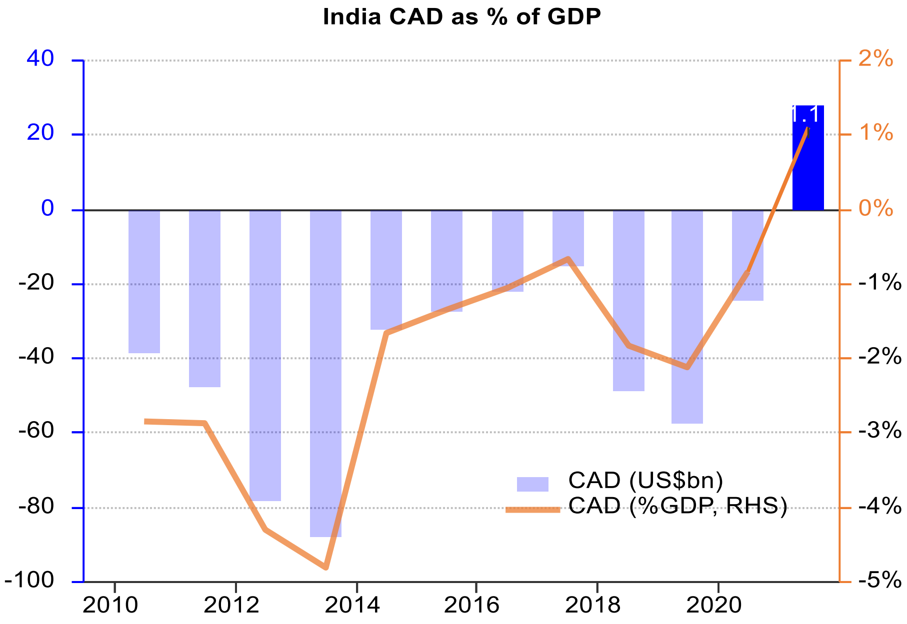
Figure 5: Oil imports vs. Brent crude oil prices trend



Source: Refinitiv Datastream.

Figure 6: Current account surplus pegged at 1.1% of GDP in FY21; expect deficit of 0.7% of GDP in FY22

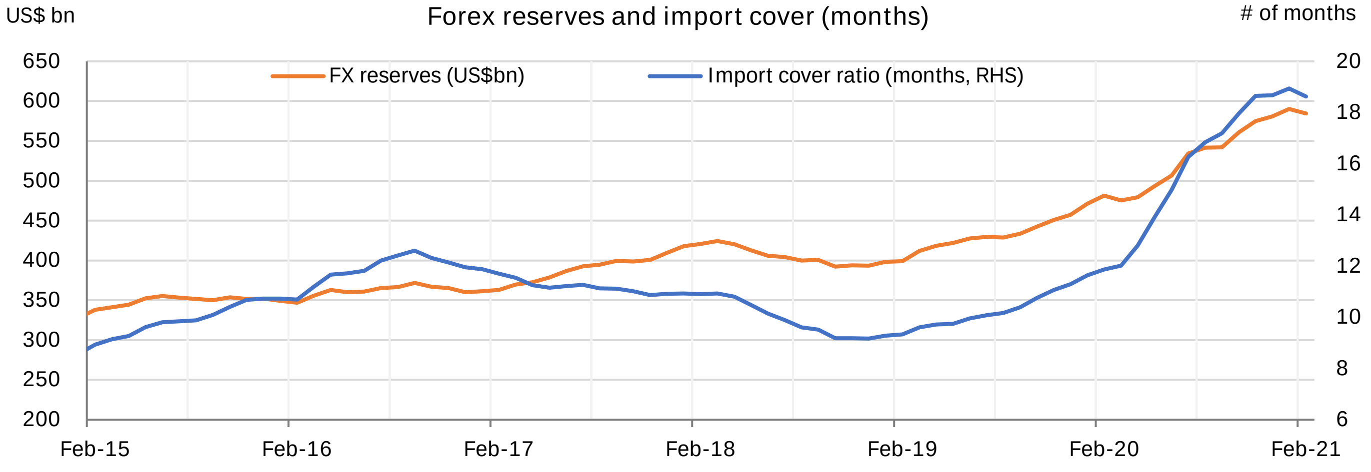
A significant contraction in trade deficit in FY21 is expected to translate into a current account surplus of 1.1% of GDP in FY21—the first surplus in 17 years, vs. a deficit of 0.9% of GDP in FY20. In FY22, we expect current account to slip into deficit again, with our estimate pegged at 0.7% of GDP, even as expectations of sustenance of foreign investments is likely to keep BoP in a comfortable surplus position for the third year in a row.



Source: Refinitiv Datastream, NSE

Figure 7: Forex reserves are all all-time high levels, leading to a sharp rise in import cover

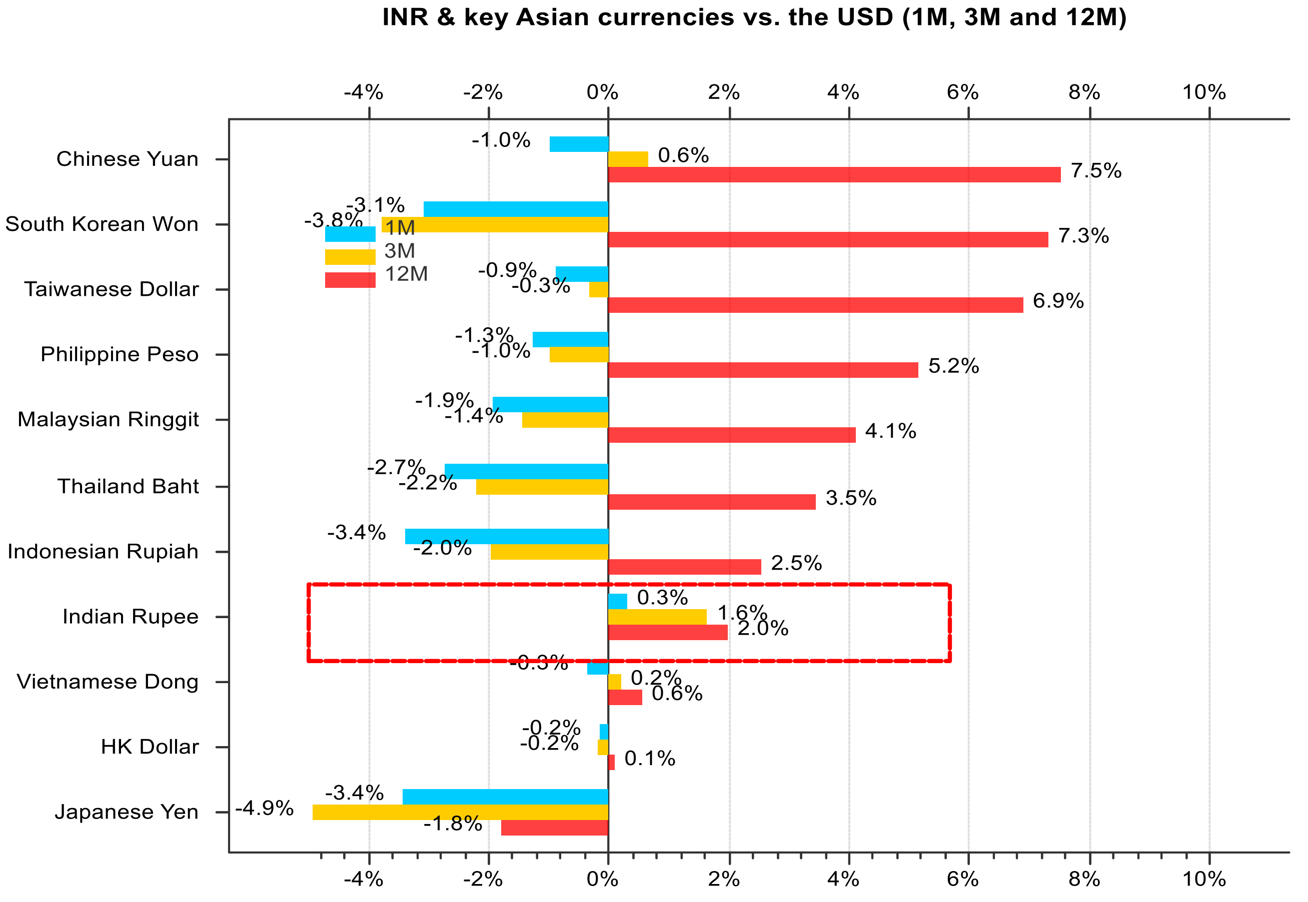
A significant accretion to forex reserves over the years, and particularly this fiscal year (+US$ 109bn in FY21 till date, as on March 5th), has resulted in a significant improvement in import cover.



Source: CMIE Economic Outlook, NSE.

Figure 8: INR vs. other key Asian market currencies

EM currencies have lately come under pressure in the wake of hardening oil prices, escalating US bond yields and a stronger US macroeconomic landscape translating into dollar rally. The INR is no different, having witnessed a significant volatility over the last few weeks, but has outperformed the broader EM pack.



Source: Refinitiv Datastream.

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