

Trade deficit shrinks on a strong revival in exports

India's merchandise trade deficit contracted to a three-month low of US\$2.7bn in September from US\$6.8bn in August—better than expectations (Consensus est.: US\$3.3bn; source: Reuters)—and led by a strong rebound in exports and a sustained double-digit decline in imports. Merchandise exports grew by an 18-month high of 6% YoY in September, marking the first expansion in last seven months on a YoY basis, supported by exports of petroleum products, engineering goods and readymade textiles. On the other hand, imports recorded a 19.6% YoY drop, led by a steep contraction in oil and gold imports; excluding these, the drop was relatively lower at 12.6% YoY. A strong 23% rise vs. August imports signals a pick-up in consumption demand ahead of the festive season. The monthly run-rate of merchandise trade points to a current account surplus of 2%+ of GDP in Q2FY21, marking the third quarter in a row to report a surplus.

A faster global recovery, thanks to relatively less stringent lockdown restrictions and aggressive policy responses, **has supported India's export activity**. This has been primarily led by economies which have been successful in checking COVID spread, such as China, Malaysia, Bangladesh, Vietnam, South Korea and Australia. **For instance, India's exports to China has** shot up by 27% YoY during Apr-Aug 2020, taking its share in India's overall export bill to 9.2% during this period vs. 5.3% in the same period last year. Weak domestic aggregate demand, however, has translated into a much slower recovery in imports, with lockdown-induced job losses and decline in disposable incomes adding to the woes. That said, a festive-led demand is expected to lead to some recovery in imports over the coming months. Consequently, we expect a significant contraction in trade deficit in FY21 (-73% YoY in H1FY21), translating into a current account surplus of 1.1% of GDP—the first surplus in last 17 years. Along with a surge in foreign exchange reserves to all-time high levels (US\$546bn as on October 2nd, +US\$88bn YTD), the comfort on CAD bodes well for the INR (+2.8% YTD).

- Exports growth turns positive after six months of contraction...: After a weak August, exports witnessed a significant recovery in September, rising by a 18-month high of 6.0% YoY, marking the first expansion in last seven months on an YoY basis. This was primarily led by a strong growth in exports of petroleum products (+5.1% YoY; +88% MoM), engineering goods (+5.4% YoY; +21% MoM) and readymade textiles (+10.2% YoY; 10% MoM). After improving over the previous three months, exports declined by a steep 12.7% YoY in August (-4% MoM). Excluding gems & jewellery, which continued to report a strong double-digit contraction for the ninth month in a row, growth in exports was much better at 10.9% YoY. On a cumulative basis, exports fell by 21.3% YoY in H1FY21.
- ...facilitated by a faster global recovery: Relatively less stringent lockdowns and aggressive policy responses have helped global economies recover faster from the COVID-19-induced slowdown. This, in turn, has supported India's export activity, with the pick-up largely led by economies which were successful in checking COVID spread. For instance, India's exports to China has shot up by 27% YoY during Apr-Aug 2020, taking its share in India's overall export bill to 9.2% during this period vs. 5.3% in the same period last year. In fact, China's share of India's exports is the highest in the last three decades.
- Imports recover at a slower pace: India's import bill sustained a double-digit drop for the seventh month in a row, falling by 19.6% YoY in September, following a 26% YoY contraction in the previous month, reflecting persistence of a weak domestic aggregate demand. This translates into a drop of 39.7% in the first half of the fiscal. Oil imports declined by a huge 35.9% on a YoY basis, contrary to a robust growth in exports of petroleum products, leading to oil trade deficit contracting to half of the previous month's figure. Gold imports also fell by 52.9% YoY and 84% MoM to

Exports grew by a robust 6% YoY in September—the highest in last 18 months.

China's share in India's export bill this fiscal has risen to three-decadal highs.

Imports fell by ~20% YoY in September led by oil and gold; excluding these, drop in imports was much lower at 12.6% YoY.

US\$601mn—the lowest in last four months in absolute terms, following a sharp surge in the previous month. Excluding oil and gold, India's import bill fell by a relatively lower 12.6% YoY but rose by a strong 23% on a MoM basis, signalling a pick-up in consumption demand ahead of the festive season.

- Trade deficit shrinks to three-month lows: A strong rebound in exports, coupled with a sustained double-digit contraction in imports, led to trade deficit shrinking to a three-month low of US\$2.7bn in September vs. a deficit of US\$6.8bn in the previous month. On a cumulative basis, trade deficit in the first half of this fiscal has fallen by ~73% YoY to US\$24.3bn—the lowest half-yearly figure in last 15 years. The monthly run-rate of merchandise trade points to a current account surplus of 2%+ of GDP in Q2FY21, marking the third quarter in a row to report a surplus.
- Expect a current account surplus of 1.1% of GDP in FY21: Recovery in imports is expected to lag the recovery in exports as lockdown-induced job losses and decline in disposable incomes as well as change in consumer behaviour is likely to weigh on domestic demand, notwithstanding some pick-up expected in an ensuing festive season. That said, a festive-led demand is expected to lead to some recovery in imports over the coming months. Consequently, we expect a significant contraction in trade deficit in FY21 (-73% YoY in H1FY21), translating into a current account surplus of 1.1% of GDP—the first surplus in last 17 years. Along with a surge in foreign exchange reserves to all-time high levels (US\$546bn as on October 2nd, +US\$88bn YTD), the comfort on CAD bodes well for the INR (+2.8% YTD).

Trade deficit declined to three-month low of US\$2.7bn in September.

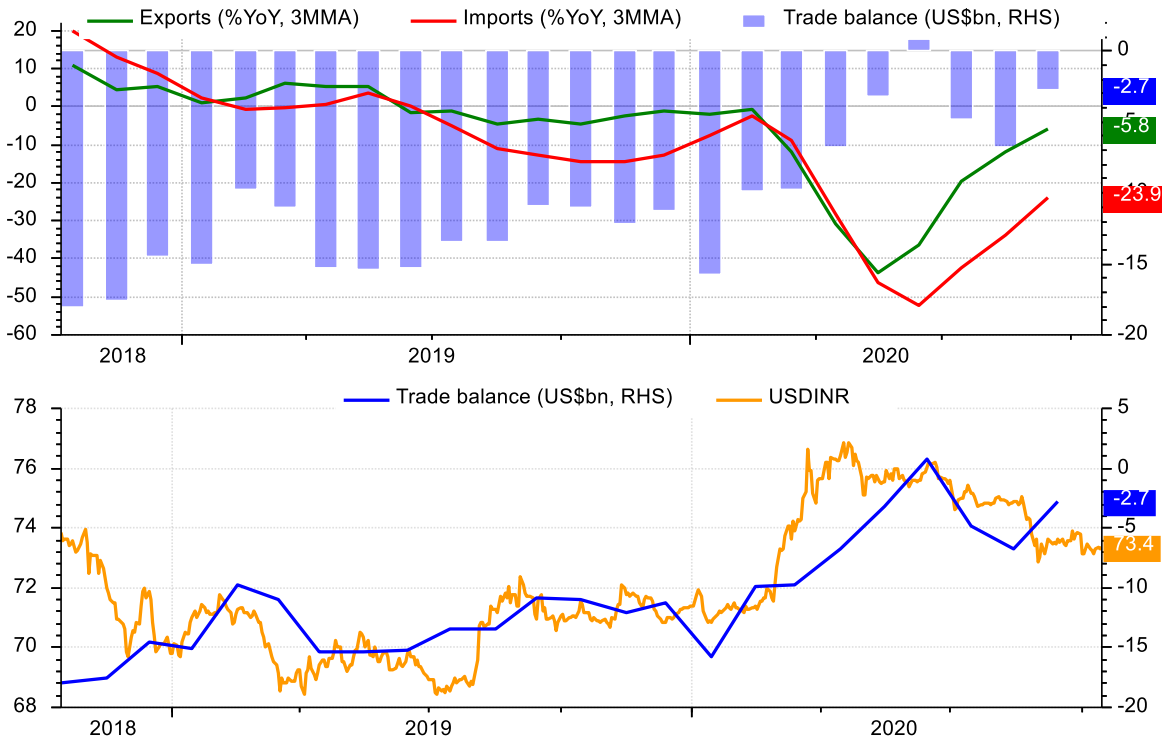
An expected current account surplus of 1.1% of GDP, coupled with record-high FX reserves, bodes well for the INR.

Figure 1: India monthly trade balance for September 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 |
| Sep-20 | 27.6 | 6.0 | 30.3 | -19.6 | 5.8 | -35.9 | 24.5 | -14.4 | 0.6 | -52.9 | -2.7 |
| Aug-20 | 22.7 | -12.6 | 29.5 | -26.0 | 6.4 | -41.6 | 23.1 | -20.1 | 3.7 | 171.3 | -6.8 |
| Sep-19 | 26.0 | -6.6 | 37.7 | -12.0 | 9.1 | -17.3 | 28.6 | -10.1 | 1.3 | -50.8 | -11.7 |
| FY21TD | 125.2 | -21.3 | 149.5 | -39.7 | 32.0 | -51.0 | 117.5 | -35.7 | 6.8 | -57.1 | -24.3 |

Source: Ministry of Commerce, CMIE Economic Outlook.

Figure 2: India monthly trade balance trend



Source: Refinitiv Datastream.

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

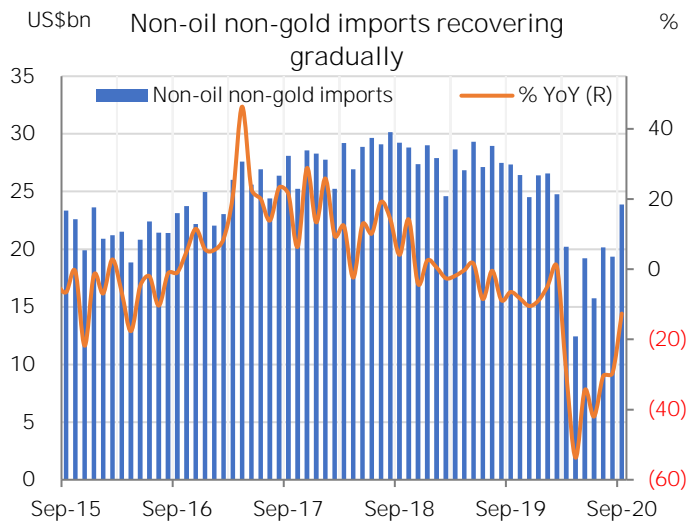
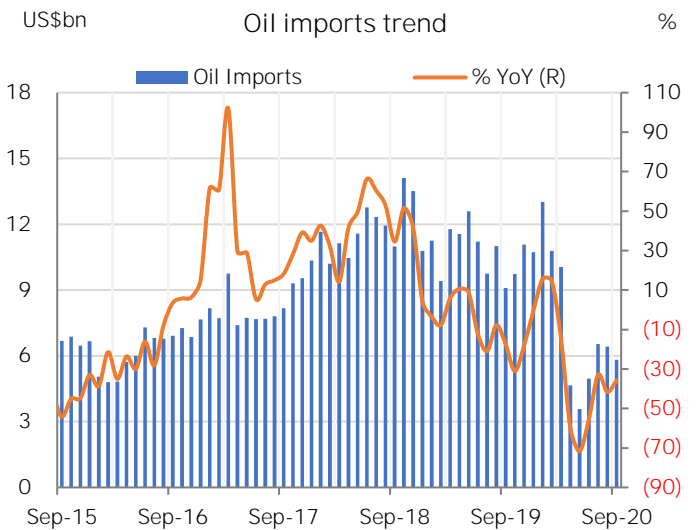


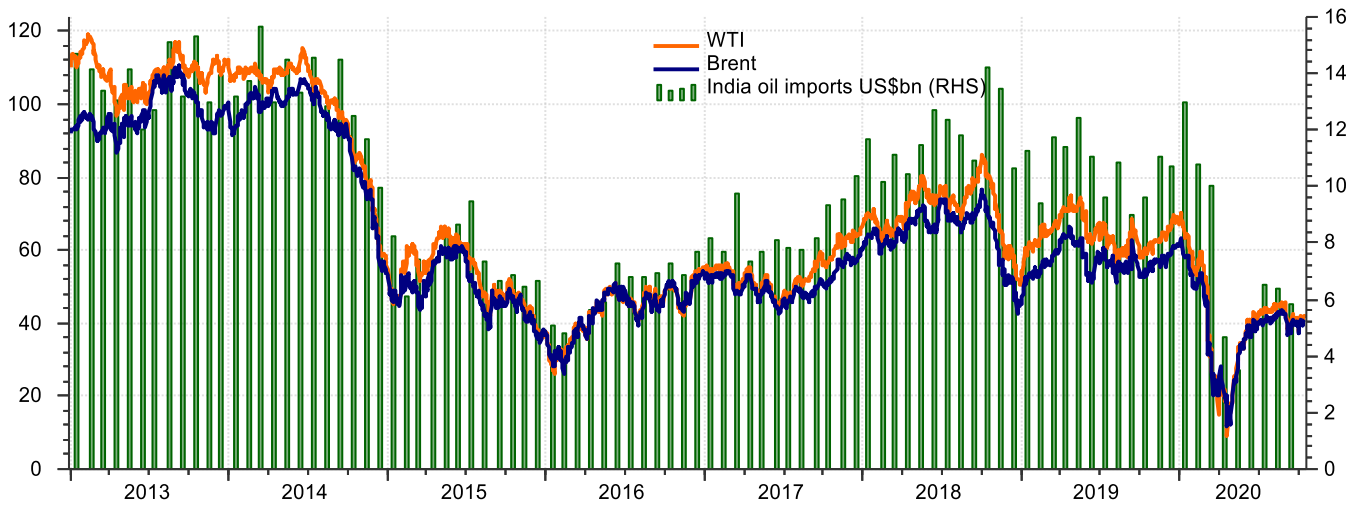
Figure 4: Oil imports trend



Source: Ministry of Commerce, CMIE Economic Outlook.

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

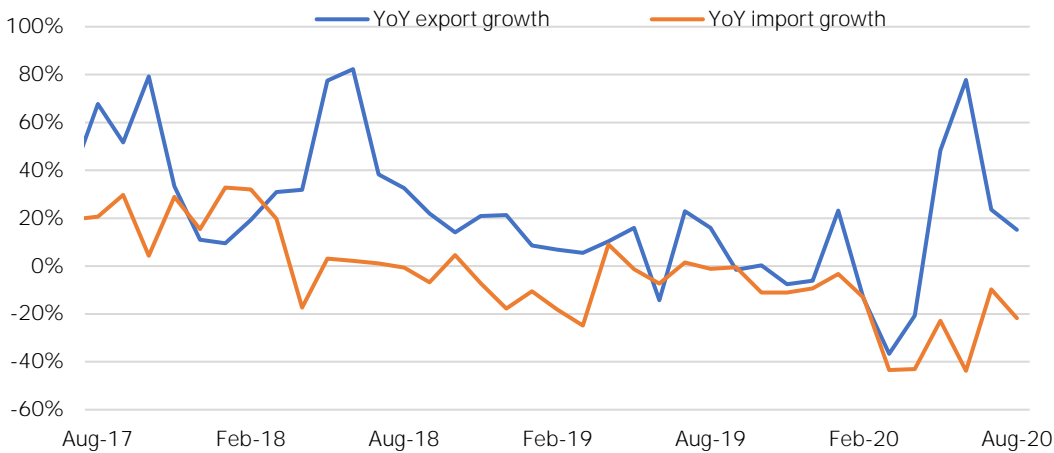
Oil imports vs. prices (US\$)



Source: Refinitiv Datastream.

Figure 6: **India's trade with China**

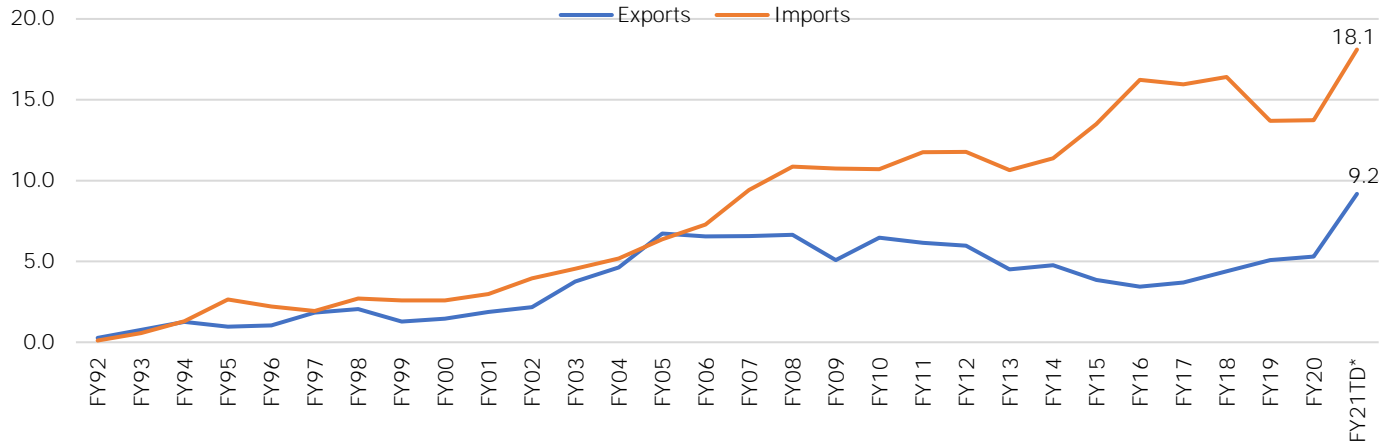
India's trade with China



Source: CMIE Economic Outlook.

Figure 7: **China's share in India's export and import bill**

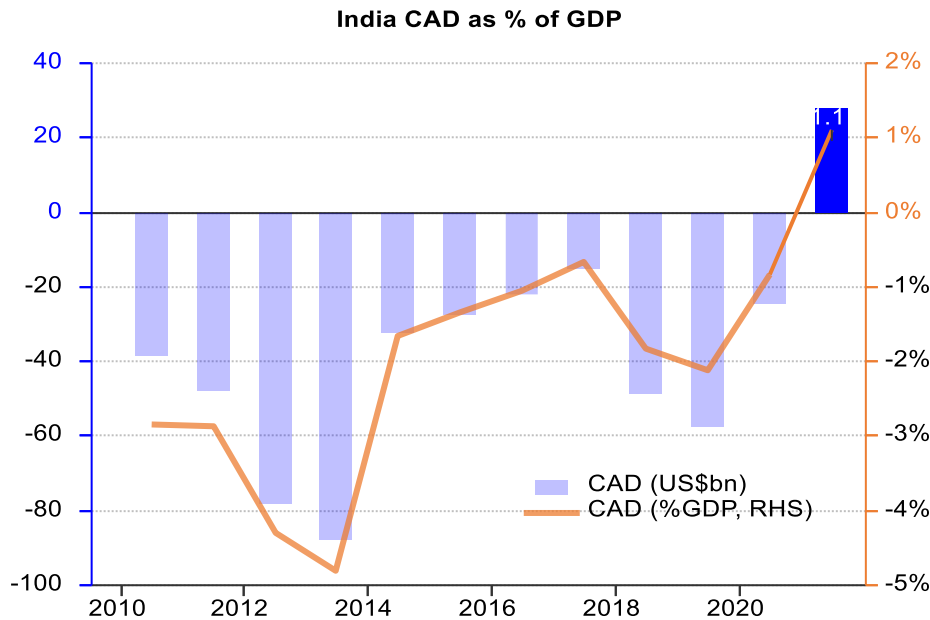
China's share in India's trade



Source: CMIE Economic Outlook.

Figure 8: Current account balance expected to turn surplus in FY21

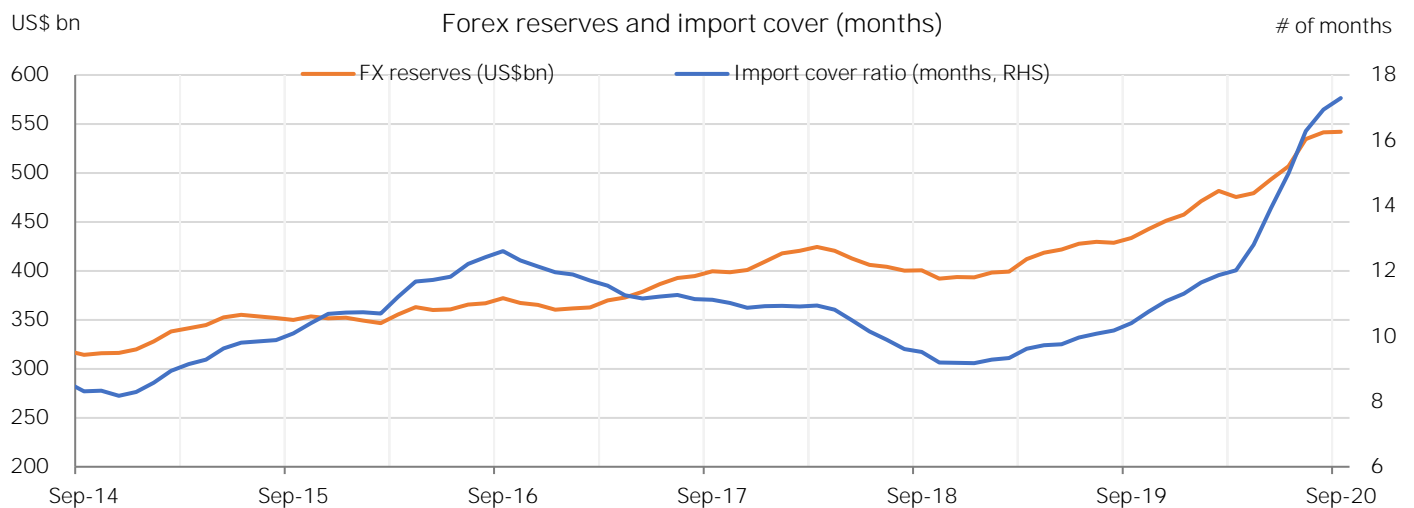
A significant contraction in trade deficit in FY21 is expected to translate into a current account surplus of 1.1% of GDP in FY21—the first surplus in 17 years, vs. a deficit of 0.9% of GDP in FY20.



Source: Refinitiv Datastream, NSE.

Figure 9: **India's foreign exchange reserves and import cover**

A significant accretion to forex reserves over the years, and particularly this year (+US\$ 88bn 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 17 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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