

EMERGING ASIA DATA RESPONSE



29th May 2009

India GDP (Q1)

Recovery already begun

- **India's economy outperformed in the first quarter, and revised data cast new light on the shape of its slowdown last year.** We are revising up our forecast for growth in 2009 to reflect the stronger starting point and recent signs of recovery.
- India's economy expanded by 5.8% y/y in Q1, which was well above our own and consensus expectations. Growth in the previous quarter was revised up, from 5.3% to 5.8%, which makes the upside surprise less dramatic. Nonetheless, today's data are strong evidence that India's economic recovery has already begun. Admittedly, manufacturing posted a 1.4% y/y decline, the first in 11 years. But strength in construction and resilience in services, allied with a bounce-back in agricultural output growth, lifted the broader economy. (See Chart.)
- Perhaps just as important as the Q1 figures, revisions to earlier data show the slowdown to have had a different shape than previously thought. The Indian economy was growing faster than initially reported when the slowdown began. But downward revisions to growth in the first half of last year coupled with the upward revision in Q4 suggest that the slowdown started earlier (growth peaked in Q4 2007) and was subsequently less abrupt.
- This is not entirely good news. In percentage point terms, the decline in India's growth from peak to trough is unchanged, but **the latest data suggest that less of the weakness can be attributed to a sharp correction in inventories and global trade flows that could rapidly be reversed.**
- There are significant discrepancies in the published breakdown of GDP by expenditure. But at face value it confirms that **government spending was the main driver of growth in the first quarter, as it had been in Q4.** The government will not be able to continue boosting growth in this way for long. Its spending power has been boosted in real terms by falling energy prices, which has allowed it to redeploy spending from subsidies. However, with oil prices now well above their trough, these gains will soon peter out.
- The new government has nonetheless pledged to carry on using fiscal policy to provide support. However, strains are already showing – the combined government deficit in the fiscal year just ended reached 10% of GDP. **Accordingly, we expect government support for the economy to ease in the second half of the year. With industry showing no sign of a rapid return to health, this will put a brake on India's recovery. We now expect GDP to expand by 6.0% this year, up from an earlier forecast of 4.0%.**

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