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Chart A: GDP growth

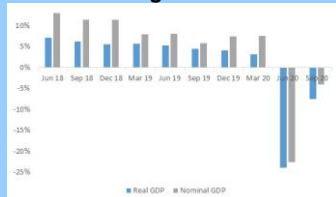


Chart B: Core GVA growth



Chart C: Sectoral contribution to real GVA growth



Chart D: Investment Rate (% of GDP)



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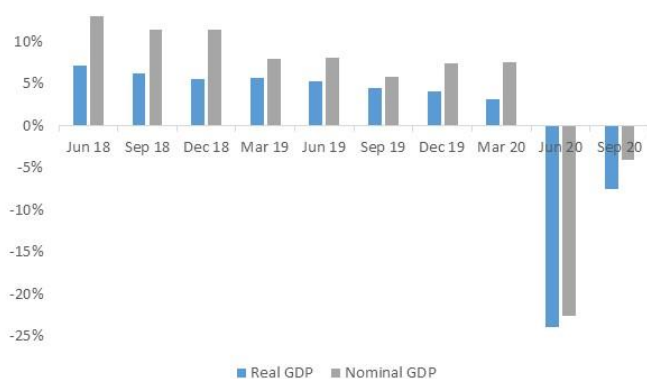


Economy

Q2 growth surprises on the upside

- **Q2FY21 growth surprises on the positive side:** The growth numbers published today showed that in the second quarter of FY21 the economy contracted at a much slower pace than expected. Real GDP contracted 7.5% y/y in Q2FY21, sharply up from the 23.9% contraction recorded in the preceding quarter. The contraction in Q2FY21 was much lower than consensus (street estimate: -8.9%, RBI SPF: -10%, RBI Nowcasting model: -8.6%). Despite better-than-expected performance in Q2, India slipped into 'technical recession' i.e. contraction in real GDP in two consecutive quarters. Nominal GDP in Q2FY21 contracted by just 4%, indicating high inflation during the quarter. Real and nominal GVA contracted by 7% and 4.2% respectively. Core GVA (excluding agriculture and public admin) contracted 7.2% during Q2FY21, up from 24.6% contraction in Q1.
- **Manufacturing, trade, construction lend support to growth:** Positive growth in agriculture and electricity was along expected lines. However, better than expected performance by manufacturing, trade and construction sectors provided the biggest support to growth. Manufacturing grew 0.6% in Q2FY21 (-0.6% in Q2FY20 and -39.3% in Q1FY21). Manufacturing activity is less contact-intensive compared to other sectors of the economy and hence it rebounded more quickly when lockdowns were lifted. PMI data corroborates this – manufacturing PMI rebounded much faster than services. Moreover, low base provided further support to manufacturing growth in Q2FY21. Quick resumption in construction and trade activities also aided growth. Construction sector contracted 8.6% in Q2FY21 (-50.3% in Q1FY21, 2.6% in Q2FY20), while trade sector contracted -15.6% (-47% in Q1FY21 and 4.1% in Q2FY20). The sequential improvement in construction growth possibly reflects resumption in construction activity following monsoon season and gradual return of migrant labourers. On the other hand, sequential improvement in 'trade, hotels and transportation' could be due to pent-up demand entering the market and consumer spending ahead of the festive season.
- **Lower government spending plays a drag on growth:** The government continued belt-tightening to limit fiscal slippage. A separate data release showed that during Apr-Oct '20 the central government spent 54.6% of its budget estimate for FY21, down from 59.4% during Apr-Oct '19. Public admin, which is the expenditure-side proxy for government spending, contracted 12.2% in Q2FY21 on the back of a 10.3% contraction in Q1FY21. According to our estimates, lower government spending shaved off 160bps and 150bps from headline growth in Q2 and Q1FY21 respectively.
- **Private consumption gets a boost from pent-up demand, festivals:** Private consumption contracted 11.3% y/y in Q2FY21, halving from 26.7% contraction recorded in Q1. Good monsoon, pent-up demand and consumer spending ahead of the festive season is likely to have aided private consumption. Government consumption, on the other hand, declined 22.2%. Out of the 13.3% contraction recorded in consumption, private and government consumption accounted for 9.4% and 3.7% respectively.
- **Investment rate increases to 29%:** In Q1FY21, the contraction in capital formation was twice as sharp as contraction in headline growth, leading to a fall in investment rate to 22.3% of GDP. In Q2, the contraction in capital formation was in line with contraction in headline growth. Hence, investment rate increased to 29% of GDP which is broadly in line with its long-term trend.
- **Virus trajectory to determine growth in H2FY21:** The resurgence in Covid-19 infections in many geographies and possibility of a stronger second wave pose risks to growth in H2FY21. Based on the current information, we expect growth to pick up even further in Q3FY21 (albeit still remain negative) and print a small positive number in Q4. However, the unfolding of second wave needs to be watched carefully.

Chart 1: Real and nominal GDP



Source: MOSPI, I-Sec Research

Chart 2: Real and nominal GVA



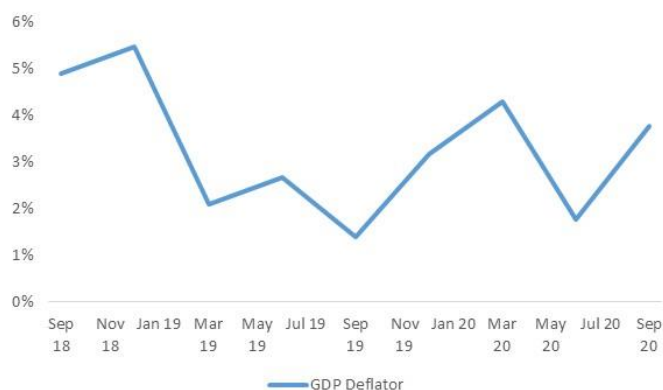
Source: MOSPI, I-Sec Research

Chart 3: Investment rate (% of GDP)



Source: MOSPI, I-Sec Research

Chart 4: GDP deflator



Source: MOSPI, I-Sec Research

Chart 5: Sectoral contribution to core GVA



Source: MOSPI, I-Sec Research

Chart 6: Sectoral contribution to GVA



Source: MOSPI, I-Sec Research

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