India Flash

Weakening investment and subdued exports drag on 4Q11 GDP

India's growth momentum slowed markedly in 4Q11, as real GDP registered 6.1% y/y from 6.9% in 3Q11, its slowest year-on-year growth rate since the first quarter of 2009. The outturn was below expectations (BBVA: 6.6%; consensus: 6.3%), dragged down by a further contraction in investment and sluggish export growth. This brings the full year 2011 GDP growth to 7.1% y/y from 8.7% in 2010 (slightly below our previous estimate of 7.2%) On a sequential basis, we estimate real GDP to have gained 0.8% q/q, seasonally adjusted in 4Q11 from 1.2% in 3Q11. The outturn is likely to reinforce growth concerns, and with inflation moderating, we expect a 25bp rate cut by the RBI at its policy meeting on March 15. We also anticipate another 50 bps cut in the CRR amid tight liquidity conditions.

- **Industrial production and weak exports drag growth lower.** Industrial activity in 4Q11 grew by just 2.6% y/y from 3.2% in 3Q11, its slowest pace in 11 quarters. Further contraction in mining (-3.1% y/y vs -2.9% in 3Q) and a sharper than expected decline in manufacturing growth largely offset high growth in the construction and electricity sectors. The slowdown was exacerbated by weakening exports growth (13.1% y/y vs 23.3% in 3Q11) amid slowing global demand, while imports gained at a fast clip.

- **Little signs of a meaningful revival in investment.** Gross fixed capital formation contracted for a second consecutive quarter by -1.2% y/y in 4Q11 compared to -4.0% in 3Q11, due to rising interest rates, global uncertainty, and sluggish policy reforms. In this context, policy announcements with the upcoming union budget will be closely watched by investors for visible steps to revive the investment climate.

- **Consumption and the services sector remain broadly supportive thanks to fiscal accommodation.** GDP growth was largely supported by a 5.9% y/y gain in total consumption (3.4% in 3Q11) as government subsidies contributed to strong gains in private consumption, especially in rural areas. As anticipated, the services sector remained the main growth driver from the income side, driven by government spending. On a cautious note, with fiscal consolidation in store over 2012, support from services and consumption sector is expected to fade.

- **Risks to the 2012 growth outlook are to the downside.** We maintain our GDP growth projection for 2012 of 7.0% y/y but highlight downside risks amid the weak investment cycle and absence of effective policy reforms.

Chart 1
India's GDP growth momentum slows markedly in 4Q11

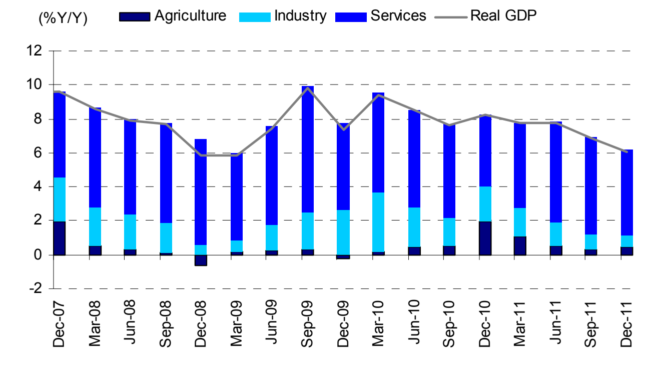
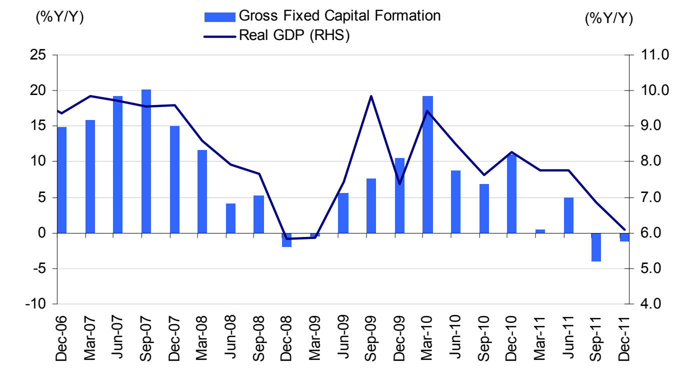


Chart 2
Investment activity contracts further



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