

## POSITIVE EVENTS IMPROVE INDIA'S Q2 GDP PROJECTIONS: LOSSES REDUCED BUT REASONS TO REMAIN CAUTIOUS REMAIN

Issue No. 62, FY21

Date: 20 November 2020

There is a flurry of revisions in India's GDP estimates which remind us of the famous quote "When the events change, I change my mind. What do you do, sir?" There is ambiguity regarding the famous person who stated these wise words. Some attribute it to John Maynard Keynes and some to Paul Samuelson, both noted economists. Regardless of the source, continuous revisions in GDP estimates have become the norm now.

**We are also revising our Q2 GDP growth to -10.7% (earlier: -12.5%) with positive bias**, based on our nowcasting model with 41 high frequency indicators, associated with industry activity, service activity, and global economy. Our estimate of Q2 FY21 (or Q32020) is aligned with the economic growth seen by various economies in Q3 2020. The GDP contraction halved in Q32020 compared to Q22020 for select 18 economies.

The upward revisions reflect faster recovery and these estimates would have been even better if July and August would have shown even a little bit of traction. The SBI business activity index shows that there is continuous improvement and Q3 numbers could be even better. However, the extent of recovery in subsequent quarters can only be gauged after the actual Q2 numbers are published.

There is no doubt that the economy has suffered and scarring remains. The MSME sector has borne the brunt of the COVID pandemic and the ECLGS scheme was a shot in the arm. As on March'20 around Rs 14 lakh crore was outstanding to MSME sector. As per data uploaded by Member Lending Institutions on the ECLGS portal, an amount of Rs. 2.05 lakh crore has been sanctioned under the Scheme to 61 lakh borrowers so far, while an amount of Rs 1.52 lakh has been disbursed with it states like AP, MP, Telangana and Odisha benefitting more. However, if the overall corpus of the ECLGS scheme stays at Rs 3 lakh crore it could be a constraining factor.

Corporate results remain good and growth in corporate GVA of 3640 listed entities is at 22.06% y-o-y- for Q2FY21 and size wise analysis based on turnover shows resilience in small and medium enterprises. For example, entities with turnover up to Rs 50 crore reported only 4% dip in top line and reported reduction in loss as compared to Q2FY20. Similarly, entities with turnover between Rs 100 crore and Rs 250 crore, reported 7% degrowth in revenue while recorded growth of 12% and 8% in EBIDTA and PAT respectively. The good performance in the listed space shows that the dichotomy between the formal and informal sectors has become more pronounced with formal sector doing better than informal sector and the recovery in the small and medium firms in listed space does not translate to overall better situation in the MSME space.

We also need to reiterate that although the GST numbers provide cheer as in Oct'20 they showed 10% y-o-y growth and are expected to be healthy in Oct'20, the true picture will emerge when GDP data comes. Overall, in May-Sep'20 the retail to wholesale passenger vehicle sales %, which was 99.5% in May-Oct'19, has come down to 83.8% in in May-Oct'20. There are concerns that excess inventory due to tepid sales might raise more problems for dealers. The rising dealer inventory is visible in the outstanding advances availed by them. Also, our conversations with car dealers highlighted that there is more demand for vehicles up to Rs 8 lakh and the vehicles in the range of Rs 8-12 lakh are not seeing traction. This segment could be a gauge of the discretionary spend, and its subdued performance could be a cause of concern.

Future prognosis will depend on two things- the shape of the recovery from COVID infections and how fast the vaccine is rolled out. The current trends of COVID-19 infection show that COVID cases in India peaked in September. With Unlock 5.0 and festival season till December end, the chances of possible second wave will increase. The fortnight after Diwali will be crucial and we need to carefully monitor the situation. With domestic vaccine entering Phase III and one more phase to go, COVID-19 recovery will be contingent on how fast the vaccine is rolled out and consumer confidence is restored. The best estimate of full recovery in consumer confidence can be placed in Q3 FY22.

### Q2FY21 GDP GROWTH WOULD BE AROUND -10.7%

- ◆ The estimates of GDP contraction for Q2 FY21 by various economists is in the range of 8-16%, big improvement from the Q1 FY20 decline of 23.9%. It is true that economic activities gained momentum in Q2 as compared to Q1. Despite this, we still believe that Q2 GDP contraction will be in double digits as recovery was patchy in sectors like mining, manufacturing, construction and services related to trade, hotels and transport.
- ◆ However, the sectors like, 'Electricity, gas, water supply & other utility services', 'Financing, insurance, real estate & bus. Services' and 'Public administration, defence and Other Services' will reverse their negative growth of Q1 to positive growth in Q2. Agriculture will keep its momentum of positive growth in Q2 also, as this was the least affected sector due to Covid-19 pandemic.
- ◆ Based on the above trends we believe that **Q2 FY21 real GDP growth would be around -10.7%**. Nominal GDP contraction would be around 8.4%.

SBI Projections for Q2 FY21		
Sectors	FY21 (% YoY)	
	Q1 (Actual)	Q2 (SBI Projections)
Agriculture, forestry & fishing	5.7	9.0
Mining & quarrying	-41.3	-26.5
Manufacturing	-39.3	-21.3
Electricity, gas, water supply & other utility services	-5.3	6.0
Construction	-51.4	-29.0
Trade, hotels, transport, communication & services related to broadcasting	-47.4	-29.2
Financing, insurance, real estate & bus. Services	-4.3	3.6
Public administration, defence and Other Services	-5.0	11.2
<b>Nominal GVA</b>	<b>-20.6</b>	<b>-6.8</b>
<b>Nominal GDP</b>	<b>-22.6</b>	<b>-8.4</b>
GDP Deflator	1.3	2.3
<b>Real GDP</b>	<b>-23.9</b>	<b>-10.7</b>

Source: SBI Research

SBI Composite Leading Index vs GDP Growth



Source: SBI Research

**GDP GROWTH ESTIMATE BASED ON “NOWCASTING”**

- ◆ **GVA Growth as per our composite leading indicator (CLI):** The CLI Index (a basket of 41 leading indicators which includes parameters from almost all the sectors) based on monthly data shows early signals of turning-points in economic activity. Out of the 41 high frequency leading indicators, 26% are showing acceleration. Two wheeler & passenger vehicle sales, domestic Tractor Sales, Bitumen Consumption and ASCBs bank deposits are showing acceleration in Q2.
- ◆ To estimate GDP statistically, we have built a ‘Nowcasting Model’ with 41 high frequency indicators associated with industry activity, service activity, and global economy. The model is developed in collaboration with *State Bank Institute of Leadership (SBIL), Kolkata by Mallick, J. & Parida, T. K.* We have used the dynamic factor model to estimate the common or representative or latent factor of all the 41 high frequency indicators from Q4 of 2012 to Q1 of 2020. These indicators are associated with industry activity, service activity, and global economy. The result could be different from RBI estimates due to capturing more indicators than the RBI model.
- ◆ The variables are used in the form of standardized year to year growth. The dynamic factor model is estimated with one lag. The estimated common factor (FACTOR) is converted to quarterly. The following structural equation is estimated to forecast the quarterly growth of GDP.

$$GDP_t = a_t + b * FACTOR_t + e_t \quad [1]$$

- ◆ Where  $e_t$  follows AR1 error structure or the serial correlation at lag one. That means,

$$e_t = c_t + r * e_{t-1} + \vartheta_t$$

- ◆ The GDP and FACTOR are transferred to  $V_t$  and  $U_t$  to adjust the AR1 error structure. Hence, the induced regression estimation is

$$EV_t = 3.31 + 43.88 * U_t \quad [2]$$

$EV_t$  is the estimated transferred GDP

- ◆ Therefore, with auto-regression coefficient “r” the estimated  $GDP_t = EV_t + r * GDP_{t-1}$  [3]
- ◆ We have data on actual GDP until Q1 of 2020 and actual FACTOR until Q2 of 2020. **The forecasted GDP growth for Q2 is -10.7%.**

**Q3 2020 GDP GROWTH OF SELECT ECONOMIES**

- ◆ Our estimate of Q2 FY21 (or Q3 2020) is aligned with the economic growth seen by various economies in Q3 2020. Almost all economies have shown significant improvement in Q3 compared to Q2. The GDP contraction halved in Q3 2020 compared to Q2 2020 for a sample of our selected 18 economies.

Q3 GDP Growth of Select Economies (% YoY)		
Country	Q2 2020	Q3 2020
China	3.2	4.9
Norway	-4.6	-0.1
Israel	-8.2	-1.4
Lithuania	-4.6	-1.7
Poland	-8.0	-2.0
US	-9.0	-2.9
Latvia	-8.6	-3.1
Denmark	-7.7	-3.4
Indonesia	-5.4	-3.6
Sweden	-7.7	-4.1
France	-18.9	-4.3
Euro area	-14.8	-4.4
Hungary	-13.5	-4.7
Italy	-17.9	-4.7
Austria	-14.5	-5.3
Czech Republic	-10.9	-5.8
Japan	-10.3	-5.9
UK	-21.5	-9.6
<b>Average of Above Economies</b>	<b>-10.2</b>	<b>-3.4</b>

Source: OECD; SBI Research

**COVID-19 RECOVERY CONTINGENT ON VACCINE**

- ◆ The COVID-19 outbreak impacted those activities where direct human to human contact is inevitable. This includes services such as tourism and hotels and trading in unorganised sector. Thus a sustainable recovery will require large scale immunisation of population so that consumer confidence pick up.
- ◆ The current trends of COVID-19 infection show that COVID cases in India peaked in September. With Unlock 5.0 and festival season till December end, the chances of possible second wave will increase. However there is also a growing confidence that even if there is a second wave, the precipitous plunges of Q1:2020-21 may not recur because the brunt of the impact on contact-dependent industries and services has happened, and they are quickly adapting to a virtual normal.
- ◆ With domestic vaccine entering Phase III and one more phase to go, COVID-19 recovery will be contingent on how fast the vaccine is rolled out and consumer confidence is restored. The best estimate of full recovery in consumer confidence can be placed in Q3 FY22.

**CORPORATE RESULTS**

- ◆ Corporate, in the listed space, reported improved earnings in Q2 after a dip of around 30% in the top line and more than 75% in bottom line in Q1FY21.
- ◆ In Q2FY21, we observed sectors sector such as FMCG, Edible Oil, Pharma, Cement, Packaging, Consumer Durable etc. reported better number across key parameters. Around 3000 listed entities, excluding BFSI and telecom reported around 11% de-growth in top line and around 7% growth in EBIDTA. PAT too grew by around 6% in Q2FY21 as compared to Q2FY20. Size wise analysis based on turnover shows resilience in small and medium enterprises.
- ◆ For example, entities with turnover up to Rs 50 crore reported only 4% dip in top line and reported reduction in loss as compared Q2FY20. Similarly, entities with turnover between Rs 100 crore and Rs 250 crore, reported 7% de-growth in revenue while recorded growth of 12% and 8% in EBIDTA and PAT respectively.
- ◆ Earlier in Q4FY17 & Q1FY18, destocking had happened in both consumer and investment intensive sectors which led to slowdown in GDP in these quarters. On similar logic, we believe the growth of manufacturing may turn out weak in Q2 & Q3 as the destocking activity has well continued in Q3 at least till November.

**GST COLLECTIONS DO NOT SHOW THE COMPLETE PICTURE**

- ◆ Meanwhile, Oct'20 GST revenue is 10% higher than the GST revenues in the same month last year. The positive trend which started from Sep'20 has sustained. Although GST collections look promising, the taxes are paid both by wholesalers and retailers. When the GDP data comes, the extent of recovery can be gauged looking at the inventory figures.
- ◆ Case in point is the auto sector sales. As per the wholesale sales data, passenger vehicle sales have registered positive growth rate of 14%, 26% and 14% y-o-y in Aug'20, Sep'20 and Oct'20 respectively. However, the retail sales data shows fluctuations with Aug'20 sales de-growing at 7%, Sep'20 sales increasing at 10% and Oct'20 sales again declining at -9% y-o-y. Overall, in May-Sep'20 the retail to wholesale % which was 99.5% in May-Oct'19, has come down to 83.8% in in May-Oct'20. There are concerns that excess inventory due to tepid sales might raise more problems for dealers.

**Key Financials of listed entities Q2FY21 vis-à-vis Q2FY20 (sizewise)**

Turnover	No of Companies	Revenue	EBIDTA	PAT
up to Rs 50 crore	1803	-4%	LTP	Loss
above Rs 50 crore to Rs 100 crore	320	-9%	91%	LTP
above Rs 100 crore to Rs 250 crore	349	-7%	12%	8%
above Rs 250 crore to Rs 500 crore	213	-6%	48%	251%
above Rs 500 crore to Rs 1000 crore	172	-10%	3%	24%
above Rs 1000 crore	179	-12%	7%	0.03%
<b>Overall</b>	<b>3036</b>	<b>-11%</b>	<b>7%</b>	<b>6%</b>

Source: SBI Research; Cline; Turnover based on Q2FY20; results ex BFSI and telecom; LTP = loss to profit

**Growth in Corporate GVA**

Quarter	No of Companies	Growth
Q2FY20	3715	-10.69%
Q3FY20	3732	-0.16%
Q4FY20	3699	-18.94%
Q1FY21	3708	-18.48%
Q2FY21	3640	22.06%

Source: SBI Research; Cline; listed entities; Corporate GVA as represent by EBIDTA + Employee cost

**ECLGS STATE-WISE SHARE: ESTIMATES BY SBI**

- ◆ In May'2020 Government announced ECLGS to mitigate the distress caused by coronavirus pandemic-induced lockdown, by providing credit to different sectors, especially micro, small and medium enterprises (MSMEs) with Rs 3 lakh crore Collateral free Automatic Loan for Businesses including MSMEs. Borrowers with upto Rs 25 crore outstanding and Rs 100 crore turnover were eligible for 20% of outstanding credit as on 29.02.2020. The scheme is now extended till 31st March,2021 with additional credit up to 20% of outstanding loans as on 29.2.2020 for entities with outstanding credit up to Rs 50 crore as on 29.2.2020 and annual turnover up to Rs 250 crore, which were up to 60 days past due as on 29.2.2020.
- ◆ As on March'20 around Rs 14 lakh crore is outstanding to MSME sector. As per data uploaded by Member Lending Institutions on the ECLGS portal, an amount of Rs. 2.05 lakh crore has been sanctioned under the Scheme to 61 lakh borrowers so far, while an amount of Rs 1.52 lakh has been disbursed. Based on share of SBI share, we have calculated the state-wise share in ECLGS disbursement and found that it benefits more to the states like AP, MP, Telangana and Odisha .
- ◆ We believe the ECLGS 2.0 can provide much needed relief to stressed sectors including Auto Component, Constructions, Gems & Jewellery, Hotel and Restaurants, Iron & Steel, Real Estate, Textile etc. by helping entities sustain employment and meet liabilities. We believe potentially around 40,000 entities can benefit from the scheme. However, if the overall amount stays at Rs 3 lakh crore, the overall corpus of ECLGS 2.0 could be a constraining factor.

**% Share in ECLGS Disbursement**

Name of the State/UT	Sanctioned Amount (%)	Disbursed Amount (%)	Number of Accounts (%)
ANDHRA PRADESH	7.25	7.29	11.86
MADHYA PRADESH	4.64	3.96	8.68
TELANGANA	5.65	5.59	8.00
ODISHA	3.40	3.29	7.40
WEST BENGAL	4.08	4.08	6.42
MAHARASHTRA	9.50	9.33	6.21
TAMILNADU	9.22	9.40	6.01
UTTAR PRADESH	7.97	7.85	5.80
GUJRAT	11.68	11.00	5.20
RAJASTHAN	5.45	5.62	5.10
KERALA	4.66	5.08	4.28
KARNATAKA	5.51	6.01	3.18
BIHAR	2.41	2.39	2.78
JHARKHAND	1.69	1.76	2.54
CHATTISGARH	2.21	2.16	2.44
UTTARAKHAND	1.47	1.47	2.39
PUNJAB	2.33	2.38	2.01
ASSAM	1.63	1.65	1.90
HARYANA	2.84	3.10	1.60
HIMACHAL PRADESH	1.29	1.48	1.48
NEW DELHI	2.50	2.53	1.07
OTHER STATES & Uts	2.65	2.59	3.65
All India	100	100	100

Source: PIB, SBI Research, State amounts are estimated

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