

## India Outlook

Victory in UP sets the tone

**A**fter a landslide win in state elections for Uttar Pradesh (UP), India's most populous state, PM Narendra Modi and his BJP-led government are well positioned to win a second five-year term in the 2019 federal election. The UP win also signalled the collapse of Congress Party and its Nehru/Gandhi dynasty, which together had led India for most of the 70 years since independence. The win should help Mr Modi push reform legislation through the parliament's upper house, where his bills have been frustrated by a lack of support. The BJP will not gain an immediate upper house majority (UP sends 31 MPs to the 245-seat upper house, but they are appointed for 6-year terms with one third retiring every two years). However, it should help Mr Modi win over smaller parties that have sided with Congress in blocking legislation.

All five of the enabling bills for the GST have been approved by the joint federal-state GST Council and will be put into the current parliamentary session attached to "money bills", which cannot be rejected by the upper house. Finance Minister Arun Jaitley hopes the new tax system will start in July and it must start before October, when

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the states will lose many existing taxes under laws already passed. Most clients we have spoken to are preparing for considerable turmoil that may affect consumer sentiment and corporate cash flow, during the implementation phase.

India's new GDP series says that consumer demand surged by 10 per cent yoy in October-December 2016, when the cash crunch created by demonetisation was in full effect. Vehicle sales (by volume) show who suffered most. Hardest hit were 3-wheeler sales, which saw an 8 per cent ytd fall to last October turn into a 30 per cent yoy plunge in the final two months of 2016 and a 25 per cent yoy fall

for the first two months of 2017. Two-wheeler sales (a guide for low-income households) swung from 11 per cent ytd growth by last October to a 12 per cent yoy fall for the final two months of 2016, followed by a milder 3 per cent yoy fall for Jan-Feb 2017. Passenger vehicle sales were least affected, with growth easing from 10 per cent ytd by October to 5 per cent yoy growth for Nov-Dec 2016 and then a rebound to 12 per cent yoy growth for Jan-Feb 2017. Commercial vehicle sales, which rose 11 per cent ytd by October, fell 7 per cent yoy in the final two months of 2016, but recovered to 2 per cent yoy growth for Jan-Feb 2017. Poor households and small businesses were hit hardest, with less impact for middle-income households and larger firms. Apart from small businesses, the hit to demand is fading in the current quarter.

India exhibited 7 per cent growth in calendar 2016 with the help of a 20 per cent yoy surge in public consumption in Q4'16 and a 10 per cent jump in consumer demand. The jump in government consumption started earlier in 2016, with the phase in of a 14.3 per cent pay hike (plus an array of allowances) under India's once-in-a-decade pay rise for civil servants. That undoubtedly supported recent passenger vehicle sales and should continue to lift consumer demand in 2017. A good monsoon in 2016, after two poor ones, appears to have produced good (possibly record) wheat, rice, and pulse production. Both developments should help sustain real growth in consumer spending near 7 per cent this year. The main weakness in domestic demand lies in fixed investment, which fell 1.5 per cent last year, as bank credit growth slowed to 6.5 per cent under a mountain of non-performing loans. India has no quick fix for this, so fixed investment growth is likely to be limited to 3-5 per cent this year and next. This sets India up for GDP growth to continue at around 7 per cent, mostly thanks to its consumers. ■

Fiscal year starting 1 April	2013-14	2014-15	2015-16	2016-17	2017-18
GDP mp (2011-12 base year), real growth, %	6.6	7.2	7.9	6.5	7.0
Inflation - WPI, year average, %	6.5	2.1	-2.5	3.5	3.8
Inflation - CPI, yragv, %	9.0	6.0	4.9	4.5	5.0
RBI lending (repo) rate, year end, %	8.0	7.5	6.75	6.25	6.00
Rupee to US\$, RBI Ref Rate, yr end	60.1	62.5	66.2	65.0	67.5

Sources: 2013-2015 data from the government (NCI, RBI) and CEIC.