CAD may fall in Q3 as net exports ease

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India's current account deficit (CAD) may reduce in the December quarter as pressure from negative net exports eased during the period to $35.5 billion from $50.3 billion between July and September.

India's high merchandise trade deficit cancels out the services trade surplus to generate a negative overall trade balance known as net exports. A high negative net exports becomes a drag on economic growth, apart from leading to higher current account deficit. CAD factors in remittances by Indians employed overseas, along with net exports.

In the September quarter, CAD touched a nine-year high at 4.4 per cent from 2.2 per cent in the June quarter as the negative net exports shot up to $50.3 billion from $36.3 billion.

RBI Governor Shaktikanta Das in his latest policy statement said the CAD situation remained "eminently manageable" as imports moderated in the wake of lower commodity prices, resulting in narrowing of the merchandise trade deficit.

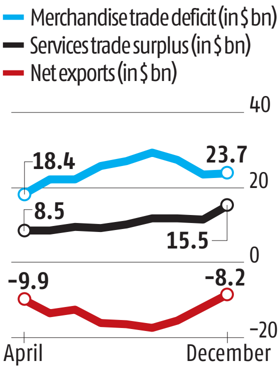
Merchandise trade deficit reduced to $74.5 billion in the December quarter from $81.8 per cent in the July-September period while services trade surplus rose to $39 billion from $31.5 billion during the same period.

Das said services exports rose by 24.9 per cent in the December quarter, driven by software, business, and travel services.

"Global software and information technology services spending is expected to remain strong in 2023. Remittance growth for India in H1 (April-September) of 2022-23 was around 26 per cent — more than twice the World Bank's projection for the year. This is likely to remain robust owing to better growth prospects of the Gulf countries. The net balance under services and remittances are expected to remain in large surplus, partly offsetting the trade deficit," he added.

While Rajani Sinha, chief economist at Care Ratings, is optimistic about the net services receipts and remittances, she feels slowing momentum in merchandise exports could continue to weigh on the CAD. "Given this background, we project CAD at 3.6 per cent of GDP in FY23, followed by a projected improvement to 2.2 per cent in FY24. On the financing front, foreign direct investment inflows have remained largely stable, while foreign portfolio investment inflows continued to exhibit volatility," she added.

UNEVEN PATH

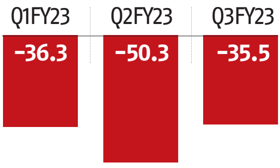


Source: Commerce Ministry, RBI

CAD (AS A % OF GDP)

Q1FY23	−2.2
Q2FY23	−4.4
Q3FY23	Not available

NET EXPORTS (IN $BN)



Source: RBI, BS calculations

Last month, Citigroup lowered its projection for India's CAD to 2.9 per cent of GDP for FY23 from 3.9 per cent estimated earlier, citing the growth in the country's service exports and a lower oil price forecast. Citi also revised India's CAD forecast for FY24 to 2.2 per cent of GDP, from 2.4 per cent earlier.

"The key surprise came from the phenomenal growth in services exports in the first half of the current fiscal year, which goes beyond just software services," Samiran Chakraborty, chief economist for India at Citi, said in a note.

India's high CAD has put pressure on its already weakening rupee due to global tightening of monetary policy.

Nomura on Friday said rupee was likely to underperform due to balance of payments pressures from India's wide CAD. "China's rapid reopening could precipitate higher commodity prices, which will drag on India's CAD. These factors will keep India's trade deficit wide, and lend support to Nomura Economics' CAD forecast of -$95.4 billion in 2023 (-2.6 per cent of GDP)," it added.