IMF raises India's FY25 GDP growth forecast to 6.5%

But estimate falls below FinMin's 7% projection

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The International Monetary Fund (IMF) raised India's growth projection for 2024-25 (FY25) by 20 basis points (bps) to 6.5 per cent in its World Economic Outlook (WEO) update on Tuesday, citing buoyant domestic spending and improved global growth prospects. The estimate, however, falls below the 7 per cent growth projection by the Ministry of Finance (FinMin).

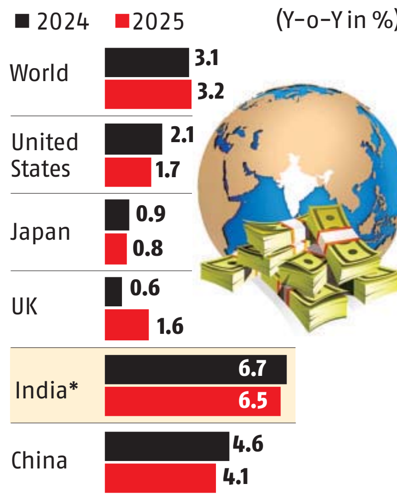
For FY24, the IMF raised India's growth estimate by 40 bps to 6.7 per cent compared to its October report, which is still lower than the 7.3 per cent growth projected by the National Statistical Office earlier this month.

Fund cites India's resilient domestic demand, says global 'soft landing' in sight

"Growth in India is projected to remain strong at 6.5 percent in both 2024 (FY25) and 2025 (FY26), with an upgrade from October of 0.2 percentage point for both years, reflecting resilience in domestic demand," the IMF said in its report.

The FinMin, in its review released on Monday, said the economy is likely to grow at or over 7 per cent for the fourth consecutive year in FY25. Turn to Page 6

GROWTH PREDICTIONS



*Figures for India are for FY24 and FY25, respectively
Source: IMF

FY24 DIRECT TAX-GDP RATIO TO BE HIGHEST SINCE FY01

On the back of robust tax collection, the ratio of direct taxes to gross domestic product (GDP) this financial year is likely to be the highest in this century so far. This, along with strong GST collection, may drive up receipts from central taxes as a proportion of GDP to the highest level since FY09. 4

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"That would be an impressive achievement, testifying to the resilience and potential of the Indian economy. It augurs well for the future," it added.

RBI Governor Shaktikanta Das, in a speech at the World Economic Forum in Davos earlier this month, had said he expected India's GDP growth would reach 7 per cent in FY25. "Our research teams are in the process of making a comprehensive assessment for our forthcoming February 2024 monetary policy. I am saying this on the basis of the strong momentum of economic activity seen in India," he said.

The IMF raised its global growth projection for 2024 by 20 bps to 3.1 per cent, compared to its October report, citing greater-than-expected resilience in the United States and several large emerging market and developing economies, as well as fiscal support in China.

However, this is still below the historical (2000–19) average global growth of 3.8 per cent, with elevated central bank policy rates to fight inflation, withdrawal of fiscal support amid high debt weighing on economic activity, and low underlying productivity growth.

For China, the IMF increased its growth forecast for 2024 by 40 bps to 4.6 per cent. "The upgrade reflects carryover from stronger-than-expected growth in 2023 and increased government spending on capacity building against natural disasters," it reasoned.

IMF Chief Economist Pierre-Olivier Gourinchas said Brazil, India, and Southeast Asia's major economies continue to show great resilience, with accelerating growth.

"The global economy begins the final descent toward a soft landing, with inflation declining steadily and growth holding up. But the pace of expansion remains slow, and turbulence may lie ahead. New commodity and supply disruptions could occur, following renewed geopolitical tensions, especially in the Middle East. Shipping costs between Asia and Europe have increased markedly, as Red Sea attacks reroute cargoes around Africa," he cautioned.

Banks' valuation discount to Sensex hits 10-year high

Analysts at Kotak Institutional Equity, in their recent report on the earnings outlook for the banks, wrote: "Banks' operating profit growth is weak because the contraction cycle in the net interest margins (NIMs) is underway. We expect banks to report a 15-20 basis point decline in NIMs. While loan yields have limited room for expansion, we see deposit costs likely to reprice higher."

Others blame HDFC Bank for the relatively poor showing of the banking index. The bank's stock declined nearly 20 per cent after its Q3FY24 earnings. Relatively poor earnings in Q3FY24 also triggered a selloff in Axis Bank, IndusInd Bank, and AU Small Finance Bank.

"HDFC Bank is the single-biggest culprit in relative under-performance and the valuation discount of the banking index. At one time, it used to trade at a P/E of nearly 30X, which is now down to 20X, while its P/B ratio has shrunk to 2.7x from close to 5 at the peak," said G Chokkalingam, founder and chief executive officer, Equinomics Research Pvt Ltd.

Banks remain the biggest component of the benchmark index with a weighting of 32.1 per cent in it. There are five banks, led by HDFC Bank, which has a weighting of 13 per cent. In comparison, there are 10 banks in the BSE Bankex index. Banks are followed by information-technology services companies such as Tata Consultancy Services and Infosys with a combined weighting of 15.3 per cent in the index.

At its current valuation, the banking index is trading at a discount to its average valuation the last 10 years while the benchmark index is at a premium to its average valuation in the last decade.

In the past 10 years, the BSE Bankex P/E multiple has been 24.2X, on average, nearly 50 per cent higher than its current P/E multiple. Similarly, the Bankex P/B ratio has been 2.3X on average in the past 10 years, 4 per cent higher than its current P/B ratio.

In contrast, the current Sensex P/E multiple is 5 per cent higher than its 10-year average P/E multiple of 23.5X while its current P/B ratio is nearly 20 per cent higher than its 10-year average P/B ratio of around 3X.

In the past 12 months, the BSE Bankex P/E multiple has declined by 90 basis points from 16.2X at the end of January 2023 to 15.3X on Monday.

In the same period, the Sensex P/E multiple expanded by 230 basis points from 22.3X at the end of January 2023 to 24.6X on Monday. The banking index price to book value has also declined by nearly 10 basis points in the last 12 months compared to an expansion of 36 basis points in the Sensex P/B ratio during the period.

One basis point is one-hundredth of 1 per cent.

This is a trend reversal for the banking index, which traded at a premium to the broader market during the pre-pandemic period.

For more than three and a half years -- between August 2016 and February 2020 -- the BSE Bankex trailing P/E multiple was higher than the benchmark index.

Analysts say poor showing by banks is weighing on the broader market, given its still large weighting in the benchmark indices.