ICRA

A MOODY'S INVESTORS SERVICE COMPANY

EXTERNAL SECTOR OUTLOOK

India's CAD rose to 36-quarter high US$23.0 billion in Q3 FY2022, mildly lower than our expectations

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HIGHLIGHTS

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India's CAD widened to 36-quarter quarter of US$23.0 billion in Q3 FY2022, albeit undershooting our expected range of US$24-28 billion

We expect CAD to recede somewhat US$17-21 billion in Q4 FY2022 from US$23.0 billion in Q3 FY2022, with the third wave temporarily curtailing certain imports

If the price of the Indian crude oil basket averages at ~US$105/bbl in FY2023, then the CAD is projected to widen to US$90-95 billion (2.6% of GDP) based on our latest forecasts of nominal GDP and the US$-INR cross rate

India's current account deficit (CAD) surged to a 36-quarter high of US$23.0 billion (-2.7% of GDP) in Q3 FY2022 from US$9.9 billion (-1.3% of GDP) in Q2 FY2022. However, the Q3 FY2022 deficit has undershot the lower end of our expectation band of US$24-28 billion, with a better than anticipated outcome for the balances of goods, services and secondary income. The sequential widening of the deficit was on account of the spike in merchandise trade deficit to US$60.4 billion in Q3 FY2022 from US$44.4 billion in Q2 FY2022. We expect the current account deficit to recede to around US$17-21 billion in Q4 FY2022, with the third wave temporarily curtailing certain imports. Accordingly, the CAD in FY2022 is projected at US$43-47 billion or 1.5% of GDP. For FY2023, if the ongoing geo-political tensions between Ukraine and Russia push up the average price of the Indian crude oil basket to ~US$105/bbl, then the CAD is projected to widen to US$90-95 billion (2.6% of GDP). Nevertheless, the merchandise trade and CAD projections for FY2023 will be contingent upon commodity price movements and the duration of the ongoing geopolitical conflict as well as supply chain implications amid lockdown in China.

- **India's CAD printed at a 36 quarter high in Q3 FY2022:** India's CAD surged to a 36-quarter high of US$23.0 billion (-2.7% of GDP) in Q3 FY2022 from US$9.9 billion (-1.3% of GDP) in Q2 FY2022. This was led by a widening of the merchandise trade deficit to US$60.4 billion in Q3 FY2022 from US$44.5 billion in Q2 FY2022, in conjunction with a rise in the net outflow of primary income to US$11.7 billion from US$10.0 billion. However, the services trade surplus (at US$27.8 billion in Q3 FY2022 from US$25.6 billion in Q2 FY2022) and the net inflow of secondary income (at US$21.3 billion from US$19.0 billion) improved in the quarter.
- **Larger CAD, lower capital flows temper reserve accretion to 12-quarter low in Q3 FY2022:** Net financial flows to India fell sharply to US$23.4 billion in Q3 FY2022 from US$40.4 billion in Q2 FY2022 and also trailed the levels seen in Q3 FY2021. Lower net FDI inflows (at US$5.1 billion in Q3 FY2022 as against US$9.6 billion in Q2 FY2022) and large FPI outflows (at US$5.8 billion vs. inflows of US$3.9 billion) led to the fall in financial flows. Owing to the sharp increase in the CAD and lower financial flows, the accretion to foreign exchange reserves dropped to a 12-quarter low of US$0.5 billion in Q3 FY2022 from an average of US$31.5 billion in Q1 FY2022 and Q2 FY2022.
- **CAD to recede modestly in Q4 FY2022 from Q3 FY2022 highs:** The average monthly merchandise trade deficit eased to US$19.2 billion in January-February 2022 from US$21.4 billion in Q3 FY2022. Consequently, we expect the Q4 FY2022 merchandise trade deficit to print at ~US$55-59 billion, modestly lower than the US$64.3 billion in Q3 FY2022. Based on this, we expect the current account deficit to recede somewhat US$17-21 billion in Q4 FY2022 from the multi-quarter high of US$23.0 billion in Q3 FY2022.
- **Average crude oil price of US$105/bbl could widen CAD to 2.6% of GDP in FY2023:** We expect the net oil imports to widen by ~US$14-15 billion (0.4% of GDP) for every US$10/bbl increase in the average price of the Indian crude oil basket. If the ongoing geo-political tensions between Ukraine and Russia push up the average price of the Indian crude oil basket in FY2023 to ~US$105/bbl, then the CAD is projected to widen to US$90-95 billion (2.6% of GDP, based on our latest forecasts of nominal GDP and the US$-INR cross rate). Regardless, the merchandise trade and CAD projections for FY2023 will be contingent upon commodity price movements and the duration of the ongoing geopolitical conflict as well as supply chain implications amid lockdown in China.

Overview

Current account deficit widened in Q3 FY2022, on account of higher merchandise trade deficit

India's current account deficit widened to a 36-quarter high of US$23.0 billion in Q3 FY2022 from US$9.9 billion in Q2 FY2022, led by the widening in merchandise trade deficit and larger net primary income outflows

India's current account deficit widened to a 36-quarter high of US$23.0 billion in Q3 FY2022 (-2.7% of GDP) from US$9.9 billion (-1.3% of GDP) in Q2 FY2022 and US$2.2 billion in Q3 FY2021 (-0.3% of GDP; refer Exhibit 1 and 7). However, the Q3 FY2022 deficit printed lower than our expectations, with a better than anticipated outcome for the balances of goods, services and secondary income. The sequential widening of the deficit in Q3 FY2022 was on account of the increase in the merchandise trade deficit (to US$60.4 billion in Q3 FY2022 from US$44.5 billion in Q2 FY2022). Moreover, primary income outflows rose to US$11.7 billion in Q3 FY2022 from US$10.0 billion in Q2 FY2022. In contrast, the size of the services trade surplus and secondary income inflows picked up to US$27.8 billion and US$21.3 billion, respectively, in Q3 FY2022 from US$25.6 billion and US$19.0 billion in the previous quarter.

On a YoY basis, the merchandise trade deficit expanded to US$60.4 billion in Q3 FY2022 from US$34.6 billion in Q3 FY2021, with the growth in merchandise imports (+51.5%) outpacing that in merchandise exports (+41.1%) in the quarter. As per the preliminary data released by the Ministry of Commerce and Industry, non-oil non-gold imports increased by 39.7% to US$108.5 billion in Q3 FY2022 from US$77.6 billion in Q3 FY2021, with a strengthening domestic demand, as well as elevated commodity prices. Additionally, gold imports surged to US$14.1 billion in Q3 FY2022 from US$10.0 billion in Q3 FY2021, attributable to the healthy wedding and festive season demand, with a modest 4.2% fall in prices during this period. On a BoP basis, net oil imports rose to US$26.0 billion in Q3 FY2022 from US$16.4 billion in Q3 FY2021.

Net financial flows to India nearly halved to US$23.2 billion in Q3 FY2022 from US$40.4 billion in Q2 FY2022

Net outflows of primary income deepened modestly to US$11.7 billion in Q3 FY2022 from US$10.1 billion in Q3 FY2021, on account of higher outflows in net overseas investment income (to US$13.7 billion from US$11.6 billion, led by higher net FDI outflows). On the contrary, the services trade surplus rose in Q3 FY2022 (in YoY terms; to US$27.8 billion from US$23.2 billion in Q3 FY2021), driven by the healthy increase in the net earnings related to telecom, communication and information (to US$28.8 billion from US$23.8 billion) and other business services (to US$1.6 billion from US$0.1 billion). Besides, the net inflows of secondary income increased to US$21.3 billion in Q3 FY2022 from US$19.3 billion in Q3 FY2021, was led by personal transfers (to US$21.1 billion from US$19.1 billion, partly stemming from higher workers' remittances).

There was a mild accretion to foreign exchange reserves of US$0.5 billion in Q3 FY2022

Net financial flows to India nearly halved to US$23.2 billion in Q3 FY2022 from US$40.4 billion in Q2 FY2022, and also trailed the US$34.1 billion seen in Q3 FY2021 (refer Exhibit 2). FPIs pulled out US$5.8 billion from the country in Q3 FY2022, in contrast to the net inflows of US$3.9 billion and US$21.2 billion, respectively, in Q2 FY2022 and Q3 FY2021. Moreover, there was a marginal net outflow in external commercial borrowings of US$0.2 billion in Q3 FY2022 (-US$1.6 billion in Q3 FY2021), as opposed to inflows of US$4.3 billion in Q2 FY2022. In addition, net FDI inflows moderated to three-quarter low of US$5.1 billion in Q3 FY2022 (+US$9.6 billion in Q2 FY2022; +US$17.4 billion in Q3 FY2021).

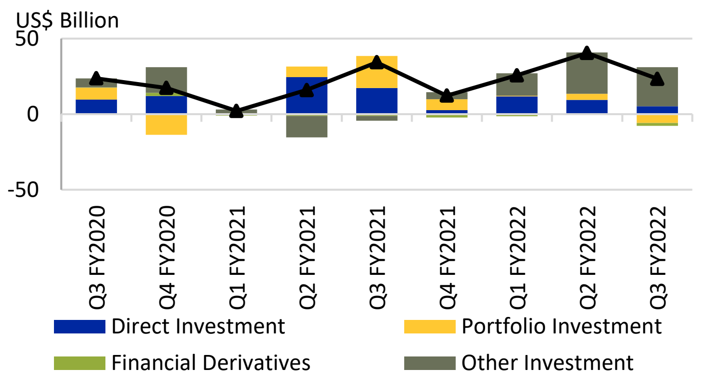
Overall, net financial inflows managed to fully finance the CAD in Q3 FY2022, leading to a mild accretion to foreign exchange reserves of US$0.5 billion in that quarter (refer Exhibit 3). However, this was much lower than the robust accretion of US$31.2 billion seen in Q2 FY2022.

EXHIBIT 1: Trends in India's Current Account

Figures in US$ billion	Q3 FY2021	Q4 FY2021	Q1 FY2022	Q2 FY2022	Q3 FY2022	FY2021	*FY2022 ICRA exp.*	*FY2023 ICRA exp.*
Merchandise Exports	77.2	91.3	97.4	104.8	109.0	296.3	*418-422*	*440 to 445*
Merchandise Imports	111.8	133.0	128.2	149.3	169.4	398.5	*615 to 617*	*685 to 695*
Merchandise Trade Balance	**-34.6**	**-41.7**	**-30.7**	**-44.5**	**-60.4**	**-102.2**	***-194 to -196***	***-245 to -250***
Net Services	23.2	23.5	25.8	25.6	27.8	88.6	*106 to 108*	*108 to 112*
Primary Income	-10.1	-8.7	-7.7	-10.0	-11.7	-36.0	*-38 to -40*	*-38 to -42*
Secondary Income	19.3	18.9	19.0	19.0	21.3	73.6	*79 to 81*	*81 to 85*
Current Account Balance	**-2.2**	**-8.1**	**+6.4**	**-9.9**	**-23.0**	**+24.0**	***-43 to -47***	***-90 to -95***
Percentage of GDP	*-0.3%*	*-1.0%*	*+0.9%*	*-1.3%*	*-2.7%*	*+0.9%*	*-1.5%*	*-2.6%*

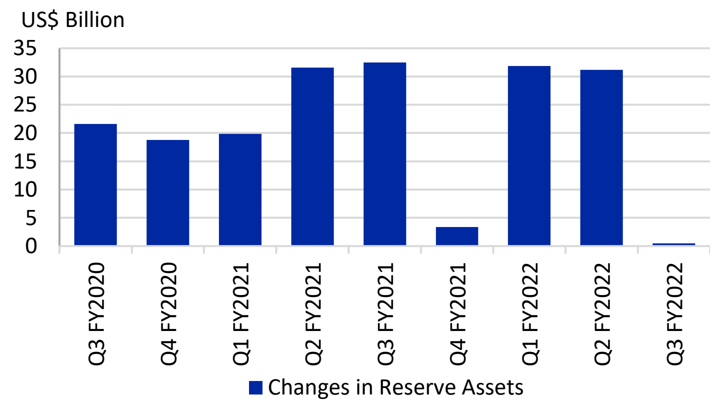
*Surplus (+)/Deficit (-); **Source**: RBI; CEIC; ICRA Research*

EXHIBIT 2: Trends in Financial flows to India



*"-" denotes outflows and vice versa; **Source**: RBI; CEIC; ICRA Research*

EXHIBIT 3: Trends in changes in India's reserve assets



*Change in Reserve Asset [Increase (+)/Decrease (-)]; **Source:** ICRA Research*

Merchandise exports expanded by 25.2% YoY in Jan-Feb FY2022; however, the pace was much lower than 37% uptick seen in Q3 FY2022

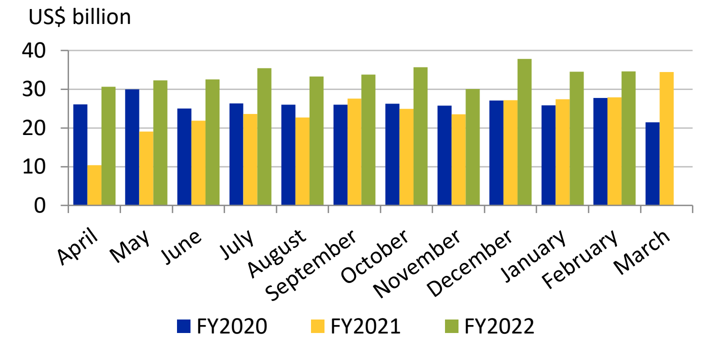
In monthly terms, exports dipped from the record high of US$37.8 billion in Dec 2021 to US$34.5 billion in Jan 2022, and remained steady in Feb 2022 (US$34.6 billion)

The healthy YoY growth in merchandise exports during Jan-Feb FY2022 benefitted from the doubling of oil exports, given the surge in prices following the abatement of the Omicron variant led Covid-19 wave across the world

CURRENT ACCOUNT DEFICIT TO RECEDE MODESTLY IN Q4 FY2022 IN SEQUENTIAL TERMS

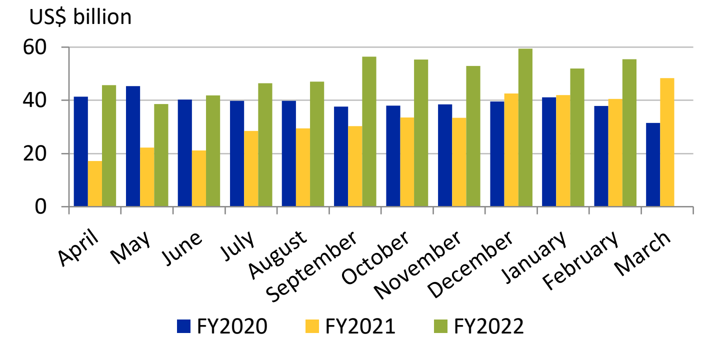
Trends in merchandise trade for January-February FY2022: The initial data released by the Ministry of Commerce and Industry indicates that merchandise exports in January-February FY2022 expanded by 25.2% YoY to US$69.1 billion from US$55.2 billion in January-February FY2021 (refer Exhibit 4) and were a robust 28.9% higher than the pre-Covid level of January-February FY2020 (US$53.6 billion). This reflects a combination of the elevated commodity prices and continued demand from major export destinations. However, the pace of YoY expansion in January-February FY2022 moderated from the robust 37.0% recorded in Q3 FY2022. In monthly terms, exports dipped from the record high of US$37.8 billion in December 2021 to US$34.5 billion in January 2022, and remained steady in February 2022 (US$34.6 billion).

EXHIBIT 4: Monthly Trends in Merchandise Exports



*Surplus (+)/Deficit (-); **Source:** RBI, Ministry of Commerce and Industry, GoI; ICRA Research*

EXHIBIT 5: Monthly Trends in Merchandise Imports

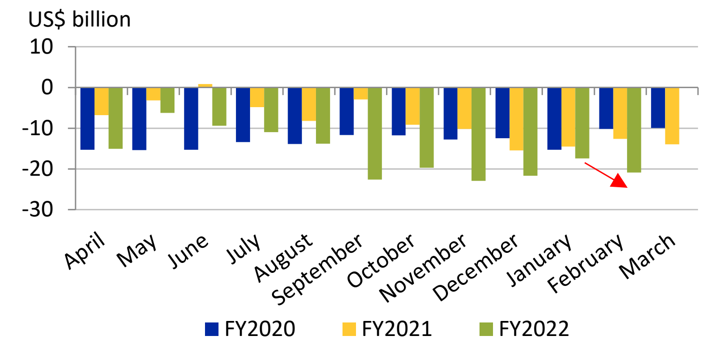


*Surplus (+)/Deficit (-); **Source:** ICRA Research*

The YoY uptick in merchandise exports during January-February FY2022 benefitted from the doubling of the oil exports to US$8.8 billion in that period (+91.4%), from US$4.6 billion in January-February FY2021 (-30.5%). This was chiefly driven the surge in crude oil prices (+53.0%), on account of the healthy demand prospects following the abatement of the Omicron variant led Covid-19 wave across the world. Moreover, oil exports in January-February FY2022 exceeded the pre-Covid level of January-February FY2020 by a healthy 33.1%. In addition, non-oil exports grew by 19.2% YoY to US$60.3 billion from US$50.6 billion, respectively, and were also 28.3% higher than the pre-Covid level (US$47.0 billion). Notably, four items, engineering goods (absolute increase: US$4.0 bn; YoY growth: +28%; share of total rise in non-oil exports: +42%), organic and inorganic chemicals (+US$1.0 bn; +26%; +10%), gems and jewellery (+US$0.9 bn; +16%; +9%) and cotton yarn/fabrics, handloom products (+US$0.7 bn; +38%; +7%) accounted for nearly 70% of the total YoY increase of US$9.7 billion recorded in non-oil exports during January-February FY2022. Compared to the pre-Covid levels, exports of as many as 27 of the 29 non-oil commodities were higher in January-February FY2022.

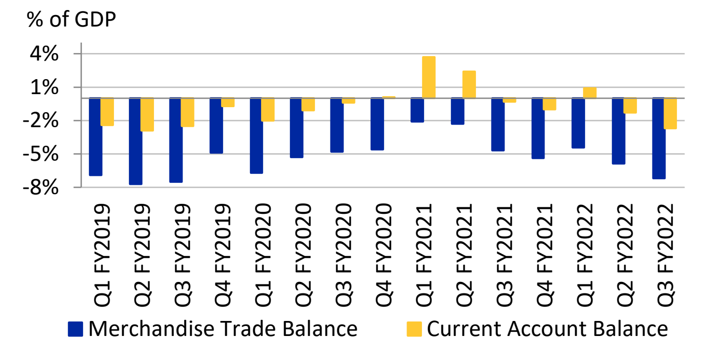
Merchandise imports expanded by 29.7% YoY in Jan-Feb FY2022, aided by higher commodity prices, even though the momentum was interrupted in Jan 2022, owing to the impact of the third wave on mobility, and hence demand for oil and gold

EXHIBIT 6: Monthly Trends in Merchandise Trade Balance



Source: *Ministry of Commerce and Industry, GoI; ICRA Research*

EXHIBIT 7: Trends in Merchandise Trade Balance and Current Account Balance



Source: *Ministry of Commerce and Industry, GoI; ICRA Research*

With lifting of restrictions, oil and gold imports improved in Feb 2022, and accordingly the trade deficit widened compared to Jan 2022

Merchandise imports grew sharply by 29.7% YoY to US$107.4 billion in January-February FY2022 from US$82.8 billion in January-February FY2021 (refer Exhibit 5), boosted by higher commodity prices. On a monthly basis, the momentum was interrupted in January 2022, with imports falling to a five-month low of US$51.9 billion, owing to the impact of the third wave on mobility, and accordingly, the demand for oil, as well as gold. Subsequently, aggregate imports rebounded by 6.8% MoM to US$ 55.4 billion in February 2022, led by oil and gold, following the lifting of state-wise restrictions with the rapid decline in Covid-19 cases. Overall, the YoY growth in merchandise imports during January-February FY2022 was led by the imports of petroleum, crude and products (+47.6%; to US$27.2 bn in Jan-Feb FY2022 from US$18.5 bn in Jan-Feb FY2021) and non-oil non-gold items (+32.6%; to US$73.0 bn from US$55.0 bn). In contrast, gold imports contracted by 23.0% YoY to US$7.2 trillion from US$9.3 trillion, respectively, owing to the impact of the third wave, as well as the high base (YoY: +136.3%) related to the inventory build-up around the presentation of the Union Budget FY2022, amidst steady prices, on an average, in January-February FY2022. Nevertheless, relative to pre-Covid levels of January-February FY2020, gold imports were a sizeable ~82% higher in January-February FY2022.

Nevertheless, gold imports contracted by 23% YoY in Jan-Feb FY2022, owing to the dip in Jan 2022, coupled with a high base, amidst steady price levels

The YoY spike of US$17.9 billion in non-oil non-gold imports during January-February FY2022 was driven by electronic goods (absolute increase: US$3.8 bn; YoY growth: +38%), fertilisers, crude and manufactured (+US$2.4 bn; +298% on a low base), coal, coke and briquettes (+US$2.3 billion; +72%), vegetable oil (+US$1.2 bn; +59%), and machinery, electrical and non-electrical goods (+US$1.1 bn; +17%). Compared to the pre-Covid levels of January-February FY2020, imports of as many as 23 of the 28 non-oil non-gold items expanded in January-February FY2022, except for leather and leather products, transport equipment, project goods, newsprint, and fruits and vegetables.

While higher commodity prices will inflame imports in March 2022, the volume of oil imports will partly determine the size of the trade deficit. We expect the trade deficit to remain higher than US$20 billion in March 2022

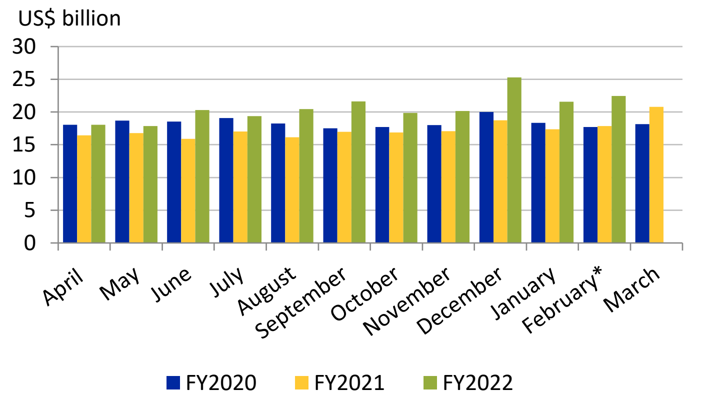
Merchandise trade deficit in January-February FY2022: With a higher YoY growth in merchandise imports (+29.7%) compared to exports (+25.2%) during January-February FY2022, the merchandise trade deficit widened to US$38.3 billion in that period from US$27.6 billion in January-February FY2021 (US$25.5 billion in January-February FY2020). **However, the monthly average deficit of US$19.2 billion recorded in January-February FY2022 was narrower than the US$21.4 billion seen in Q3 FY2022. This indicates that the current account deficit in Q4 FY2022 may recede to around US$17-21 billion from the considerable US$23.0 billion seen in Q3 FY2022, with the third wave temporarily curtailing certain imports.** ~71% of the absolute YoY widening in the trade deficit of US$10.7 billion in January-February FY2022 was driven by oil (US$4.6 bn; +43% share) and gold (US$3.0 billion; +28%). Moreover, the trade deficit of non-oil non-gold items widened by US$3.1 billion in January-February FY2022, relative to the year-ago level. In monthly terms, the deficit moderated sharply from US$21.7 billion in December 2021 to US$17.4 billion in January 2022, led by the third wave-related fallout on the demand for oil and gold (refer Exhibit 6). Subsequently, the deficit scaled back to US$20.9 billion in February 2022, led by these two items, following the easing of restrictions, and the resultant improvement in mobility.

With a lower monthly average trade deficit in Jan-Feb FY2022 compared to Q3 FY2022, CAD in Q4 FY2022 may recede to US$17-21 billion from the considerable US$23.0 billion in Q3 FY2022

Early data for March 2022 for merchandise exports: As per the early estimates shared by the Ministry of Commerce and Industry, India's merchandise exports as on March 23, 2022 reached the FY2022 target of US$400 billion. This implies that exports during March 1-23, 2022 stood at US$29.5 billion, which is equivalent to 85-86% of levels seen in the prior as well as the year-ago month. Moreover, in anticipation of fulfilling the fiscal year-end orders, we expect merchandise exports to rise sequentially in March 2022. **While higher commodity prices will inflame imports in March 2022, the volume of oil imports will play a key role in determining the size of the trade deficit. We expect the trade deficit to remain higher than US$20 billion in March 2022.**

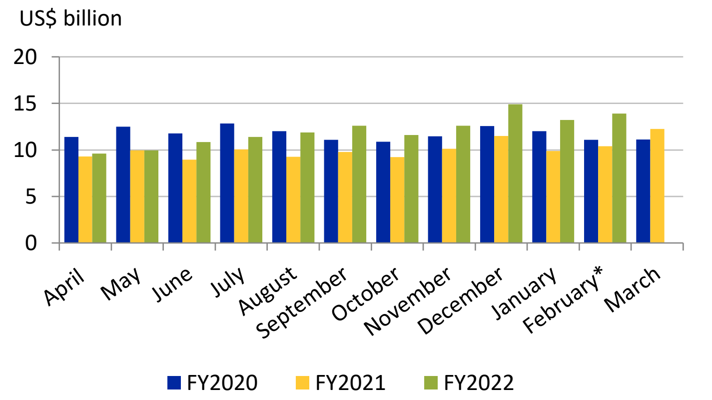
Merchandise exports are likely to print at US$418-422 billion in FY2022, indicating a YoY expansion of ~42%, benefitting from higher commodity prices, bouts of global optimism as well as the low base

EXHIBIT 8: Monthly Trends in Services Exports



Data for Feb 2022 are based on initial estimates by the Ministry of Commerce and Industry; **Source: RBI; Ministry of Commerce and Industry; ICRA Research*

EXHIBIT 9: Monthly Trends in Services Imports



*Data for Feb 2022 are based on initial estimates by the Ministry of Commerce and Industry; **Source:** RBI; Ministry of Commerce and Industry; ICRA Research*

Merchandise imports are expected to expand by 55% YoY in FY2022, boosted by higher commodity prices and a turnaround in domestic demand

ICRA expects India to record a current account deficit of ~US$43-47 billion or ~1.5% of GDP in FY2022

The escalation of Russia-Ukraine conflict and renewed lockdowns in China following the surge in Covid-19 cases, pose downside risks to the world output as well as the trade volume projections of the IMF, released in Jan 2022 for CY2022

Trend for January 2022 for services trade: As per the data released by the RBI, services exports and imports witnessed a YoY growth of 24.2% and 33.8%, respectively, in January 2022 (-8.5% and -17.7%, respectively, in January 2021), and exceeded the respective pre-Covid levels of January 2020 by 13.6% and 10.2%, respectively (refer Exhibit 8 and 9). Accordingly, the services trade surplus rose by 11.5% YoY to US$8.4 billion in January 2022 and was a robust 19.6% higher than the January 2020 level. The initial estimates provided by the Ministry, which will be revised based on RBI's subsequent release, indicated a mild uptick in the YoY growth of services exports and imports to 25.9% and 34.0%, respectively, in February 2022, compared to January 2022, with a marginal improvement in the trade surplus to US$8.6 billion from US$8.4 billion, respectively.

OVERALL, INDIA'S CURRENT ACCOUNT DEFICIT IS FORECAST AT US$43-47 BILLION OR 1.5% OF GDP IN FY2022

Given the January-February 2022 merchandise trade deficit and our expectations for March 2022, we expect the Q4 FY2022 merchandise trade deficit to print at US$55-59 billion, modestly lower than the US$64.3 billion in Q3 FY2022. Based on this, we expect the current account deficit to recede somewhat US$17-21 billion in Q4 FY2022 from the 36-quarter high of US$23.0 billion in Q3 FY2022.

Overall, ICRA expects merchandise exports and imports to increase significantly by ~42% and ~55%, respectively, in FY2022 to ~US$418-422 billion, and US$615-617 billion, respectively. As a result, the merchandise trade deficit is projected to nearly double to ~US$194-196 billion in FY2022 from US$102.2 billion in FY2021. The services trade surplus is likely to rise by ~18% to US$106-108 billion in FY2022, whereas the outflow of primary income may rise by 9-10% relative to FY2021 levels. The global economic recovery is anticipated to boost secondary income by 8-9% in FY2022 relative to FY2021. Overall, ICRA expects India to record a current account deficit of ~US$43-47 billion or ~1.5% of GDP in FY2022 (refer Exhibit 10), in contrast to the surplus of US$24.0 billion or 0.9% of GDP in FY2021.

AVERAGE CRUDE OIL PRICE OF US$105/BARREL COULD WIDEN CAD TO 2.6% OF GDP IN FY2023

In its World Economic Outlook (WEO) report released in January 2022, the IMF projected the growth in the global economy to moderate from 5.9% in CY2021 (in line with October 2021 forecast) to 4.4% in CY2022 (lower than October 2021 forecast of 4.9%) and further to 3.8% in CY2023, amidst the withdrawal of monetary accommodation, and continued supply chain disruptions. Moreover, the growth in trade volumes is expected to ease from 9.3% in CY2021 to 6.0% in CY2022, and further to 4.9% in CY2023, while remaining higher than the projected broader global recovery. **However, the rapid escalation of Russia-Ukraine conflict and renewed lockdowns in China following the surge in Covid-19 cases pose downside risks to the world output as well as the trade volume projections of the IMF for CY2022.**

We believe that exports of some items from India, such as steel, inorganic chemicals, jewellery, plastics, etc. will rise to meet the shortfall caused by disruptions amid the Russia-Ukraine conflict

With rising global prices of commodities such as crude oil, edible oils, fertilisers, etc. the import bill is expected to increase in the near term

We believe that exports of some items from India, such as steel, inorganic chemicals, jewellery, plastics, etc. will rise to meet the shortfall caused by disruptions amid the Russia-Ukraine conflict. On the contrary, with rising global prices of commodities such as crude oil, edible oils, fertilisers, etc. the import bill is expected to rise considerably in the near term, given the country's large dependence on importing such items, unless the geopolitical tensions subside rapidly. Moreover, the geopolitical conflict as well as supply-chain implications in China will weigh on the sectors such as automobiles, which are partly dependent on key raw materials provided by Russia, Ukraine or China, in the absence of any other alternatives.

The cargo handled at major ports posted a YoY contraction for the fourth consecutive month in February 2022, and the pace of the same worsened to 4.5% in that month from 2.8% in January 2022, led by containers, given the surge in freight rates. **The increase in key commodity prices amid Russia-Ukraine conflict, elevated freight costs, persistent shortage of containers, as well as the supply chain implications of the renewed lockdowns in China following the outbreak of a fresh Covid-19 wave in the country, do not augur well for the performance of inbound/outbound cargo shipments at ports.** Nevertheless, the recent extension of Interest Equalization Scheme for Pre and Post Shipment Rupee Export Credit Scheme up to March 31, 2024 for MSME exporters by the Central Bank is a positive move to support outbound shipments.

The outlook for tourism-dependent economies and cross-border services, is expected to improve somewhat. **We expect the IT sector to continue to boost services exports. Over the medium term, we anticipate that the government's PLI schemes will help in enhancing overall India's competitiveness of manufacturing exports.**

The average international price of crude oil, in Indian basket terms, jumped to US$114/bbl during March 1-30, 2022, a steep ~22.2% higher than US$93.3/bbl in February 2022, in light of the ongoing Russia-Ukraine conflict and widening sanctions on Russia, including the import ban of oil, natural gas and coal by the US. **We expect the net oil imports to widen by ~US$14-15 billion (0.4% of GDP) for every US$10/bbl increase in the average price of the Indian crude oil basket. However, the volume of other imports is likely to be constrained in this scenario, reducing the deterioration in the CAD. With the assumption that oil averages US$105/bbl (up from ~US$79/bbl in FY2022), the net oil imports may shoot up to ~US$145-150 billion in FY2023 from US$104.3 billion expected in FY2022.**

With some satiation of pent-up demand, we expect the value of gold imports to decline to ~US$35 billion in FY2023 from ~US$46-47 billion in FY2022.

Non-oil non-gold imports have expanded to US$360.4 billion in Apr-Feb FY2022 from US$245.7 billion in the year-ago period, with a broad-based uptick across various commodity groups reflecting rising commodity prices, and a turnaround in domestic economic activity.

If the ongoing geo-political tensions between Ukraine and Russia push up the average price of the Indian crude oil basket in FY2023 to ~US$105/bbl, then the CAD is projected to widen to US$90-95 billion (2.6% of GDP)

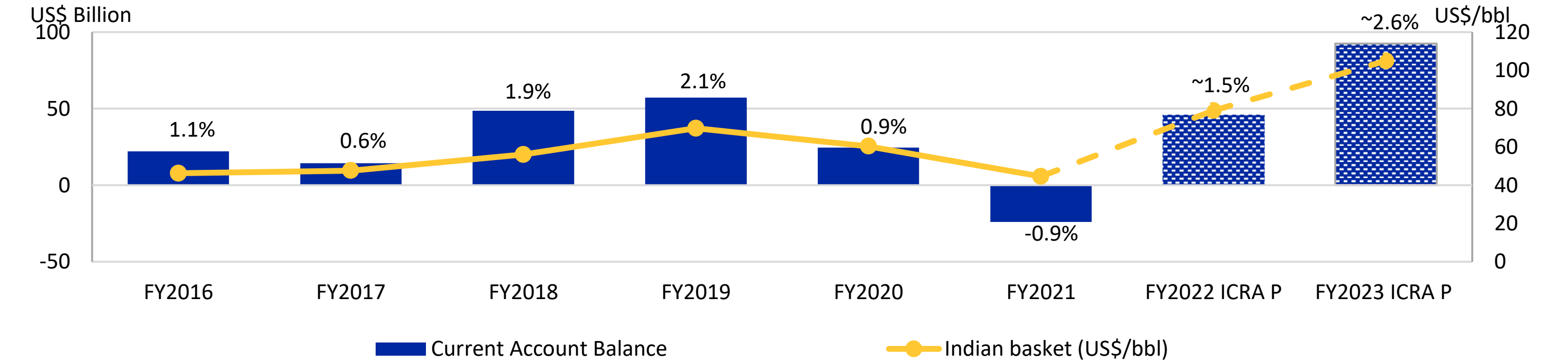
The trade projections for FY2023 will be contingent upon commodity price movement, as well as the duration of the ongoing geopolitical conflict

ICRA expects non-oil non-gold imports to increase by ~5% to ~US$420 billion in FY2023 from ~US$400 billion expected in FY2022. Overall, we expect merchandise imports to rise by ~12% to US$685-695 billion in FY2023 from US$615-617 billion in FY2022. Merchandise exports, on the other hand, are expected to rise by ~5% to US$440-445 billion in FY2023 from US$418-422 billion in FY2022.

Given ICRA's projections for merchandise exports and imports, the merchandise trade deficit is expected to rise considerably to ~US$245-250 billion in FY2023, from ~US$194-196 billion expected in FY2022. The global economic recovery is expected to boost the services trade surplus by ~3-4% in FY2023 and secondary income by ~4-5%, while the outflow of primary income may increase by ~2% in FY2023 relative to FY2022. Given our assumption of the average price of the Indian crude oil basket in FY2023 at ~US$105/bbl, the CAD is projected to widen to an all-time high of US$90-95 billion (2.6% of GDP) from the ~US$43-47 billion (1.5% of GDP) expected in FY2022. Nevertheless, as a proportion of GDP, CAD is projected to be much lower than the levels seen in FY2013 (4.8% of GDP).

The trade projections for FY2023 will be contingent upon commodity price movements and the duration of the ongoing geopolitical conflict as well as supply chain implications amid lockdown in China. While elevated crude oil and commodity prices, the ongoing geo-political tensions between Russia and Ukraine and an expectedly steeper rate hike cycle by the US Fed are likely to impart a depreciating bias to the INR, India's large forex reserves are likely to prevent a disorderly depreciation in the currency. Overall, we expect the US$-INR cross rate to trade in a range of 74.0-78.0/US$ in H1 FY2023.

EXHIBIT 10: Current Account Balance, Crude oil Price, and ICRA's expectations for FY2022 and FY2023



Labels indicate current account balance as a % of GDP; Deficit (-)/Surplus (+); P: Projected; ***Source:*** *RBI; ICRA Research*

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