India: Rural demand recovery in sight while urban demand slows

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Low consumption growth has been a concern for the Indian economy in recent years

Although Indian economic growth has been robust post-Covid and has emerged as the fastest growing economy in the world, weakness in private consumption demand has been a cause of concern (Fig 1 & Fig 2). Consumption demand recovery was lagging post-Covid. This was attributed to weak rural demand yet urban demand was a source of support on recovery in income levels. Data shows a moderation in private final consumption expenditure (PFCE), which serves as a proxy for consumer demand within the economy. In FY23, the PFCE growth clocked 6.8% which slipped to a dismal 4% levels in FY24. In our view, a pickup in household savings in FY24 from multiyear lows in FY23 (latest year for which data is available) weighed on consumption dynamics last year. After lagging in FY24, a pickup up in consumption growth was witnessed in Q1FY25 GDP. More importantly, various lead indicators and FMCG results signal rural demand recovery in the coming quarters especially H2.

Good news is that rural recovery is underway and likely to gain momentum in H2:FY25

As stated above, the trends in rural demand have turned favourable in the current financial year. This was also reflected in the Q1FY25 GDP data which showed a spike in PFCE growth to 7.4% YoY vs a weak 4% in FY24. Agriculture GVA growth came at 2% in Q1FY25, higher than 0.6% in Q4FY24. Additionally, the movements in high frequency indicators are signaling that a rural recovery is underway (Fig 3). Under rural indicators, pick up is seen in two-wheeler sales, three-wheeler sales, tractor sales, etc. which is a reversal from the negative growth seen last year. There is also a fall in demand for jobs under the rural employment guarantee programme (MGNREGA) in the current fiscal which may be due to labour demand for kharif sowing and migration of labour to urban areas. Under urban indicators, pick up is seen in domestic air passenger traffic which is however, lower than the double digit growth seen post-Covid. Although personal loans continue to grow in double digits, its moderating compared to last year. Passenger vehicle (PV) sales is trending lower this fiscal and showed negative growth during Jul-Sep'24.

As per NielsenIQ's latest FMCG Quarterly Snapshot data for Q3 2024, large FMCG companies grew slowest in terms of value growth and saw a decline in volumes in the July-September quarter. Growth has been largely led by small and mid-sized manufacturers. FMCG sector registered a growth of 5.7% for Q3 2024 and recorded a volume growth of 4.1% as against value growth of 3.5% and volume growth of 3.2% in the previous quarter. While rural areas saw a growth of 6% (vs 6.1% in Q3 2023), up from 5.2% in the last quarter, urban areas saw a marginal growth of 2.8% (vs 11% in Q3 2023) compared to 2.1% in the previous quarter.

The NIQ report affirmed that "the Indian FMCG industry shows resilience with steady value growth and marginal price increase. Rural volume growth at 6% continues to surpass urban markets, despite softer consumption in both regions this quarter." Going forward, expectations of a good sowing and Kharif crops as well as higher budgetary allocations for the rural economy would push up volume growth.

The latest RBI Bulletin for Nov'24 also asserts that **rural India is emerging as a gold mine for e-commerce companies in this festival season**; this is expected to gather further momentum with the sharp increase in kharif output and optimism around rabi production in 2024-25.

Recovery in rural wage growth likely to support demand

The pickup in real rural wage growth rates in recent months is a key positive with downward pressure on inflation in rural areas also helping to improve their real purchasing power. Also, higher demand for rural labour either for kharif sowing or in urban areas (primarily for construction work) is being reflected in a decline in household's demand for work under the Mahatma Gandhi National Rural Employment Guarantee Act (MGNREGA) by 9.2% (y-o-y) in Oct'24 and the same has been consistently negative since Nov'23. Moderating food inflation going forward is also expected to bring some respite from low real wages in rural areas.

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Urban incomes have been relatively steady

Urban areas, post-Covid, were less affected, on account of pickup in income levels apart from probably some impact of wealth effect from asset classes like equity, gold, real estate, etc. **Meanwhile our analysis of high frequency indicators shows some flattening out in urban consumption growth in recent months.** While personal loans have been consistently growing at double digits, it has shown some moderation from over 20% last year to around 16% in the first half of 2024. Besides, PV sales YoY growth was negative during Jul-Sep'24 and air traffic growth is also showing a slow pickup.

As per the latest Periodic Labour Force Survey (PLFS) Quarterly bulletin, the unemployment rate in urban areas among persons of age 15 years and above decreased from 6.6% during Jul– Sep'23 to 6.4% during Jul–Sep'24. The Labour Force Participation Rate (LFPR) in urban areas was 50.4% in Jul–Sep'24 (49.3% during Jul– Sep'23) for persons of age 15 years in above.

Post-Covid, the urban population have also been benefited by the better performance of alternative investment products including equity, gold and real estate with all three providing more than 20% average return during the last 3 years. These factors have supported urban income which in turn helped to keep consumption levels supported even as growth is flattening out.

FY25 GDP growth to be supported by revival in rural demand

Within GDP, we believe that consumption is expected to emerge as a key growth driver in FY25 especially with rural demand recovering from a low base. **During FY25, a shift is seen in growth drivers mix towards consumption in comparison to capex led growth pickup seen post-Covid, on expectation of a rise in real incomes amid easing inflation.** Agriculture GVA is expected to rebound to close to 4-5% growth in FY25 as against 1.4% in FY24. The revival in private consumption (56% share in GDP), the mainstay of aggregate demand, is likely to be strong underpinning forecast of 6.7% GDP growth this fiscal.

Interestingly, the stagnation in consumption was more pronounced in FY24 in rural areas on the back of ElNino effect on monsoon. The issue of rural distress was also echoed by fast moving consumer goods (FMCG) firms. As per NielsenIQ, the FMCG industry grew at 9.3% during 2023, with urban demand growth outpacing that in rural areas on a deficit in monsoon, which also weighed on agri GVA growth (1.4% YoY, lowest since FY16). That said, the gap between rural and urban consumption growth narrowed during the year and in FY25, a switch has been seen with rural demand growing at a faster pace vis-à-vis urban.

On balance, we believe that GDP growth in FY25 is likely to be supported by revival in household consumption demand, particularly rural demand. The positive outlook for agriculture and the resurgence of rural spending are likely to contribute to the growth momentum in H2- FY25. The above normal monsoon rains will support higher agriculture incomes amid contained food inflation. This could lead to a sustained rebound in overall household consumption spending in FY25.

Charts

Fig 1: Household consumption grew at half the pace of GDP in FY24… (% y/y)

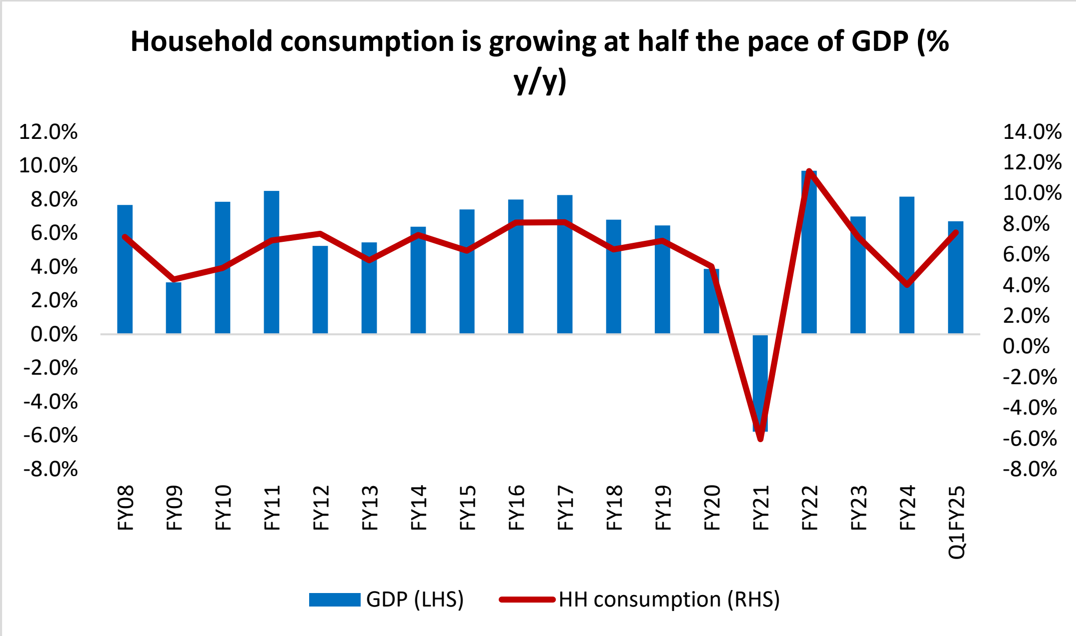


Fig 2: …slipping to weakest levels since the GFC (% y/y)

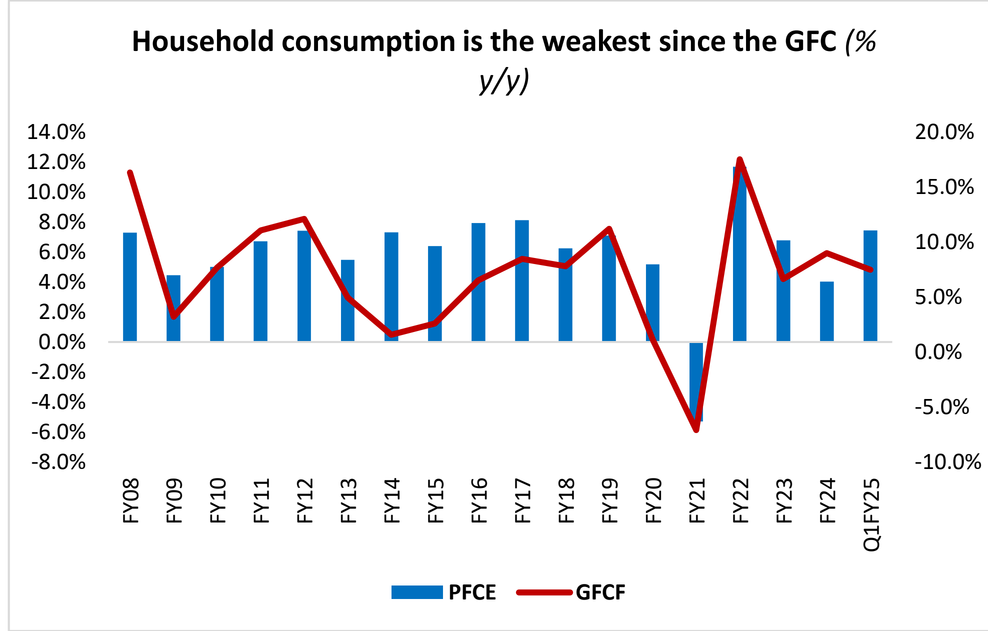


Fig 3: Rural demand is showing initial signs of recovery (YoY %)

Initial signs of recovery seen in Rural demand																	
	May'23	Jun'23	Jul'23	Aug'23	Sep'23	Oct'23	Nov'23	Dec'23	Jan-24	Feb-24	Mar-24	Apr-24	May-24	Jun-24	Jul-24	Aug'24	Sep'24	Oct'24
Urban indicators																		
IIP: Consumer durables	1.5	-6.8	-3.6	6.0	1.0	15.9	-4.8	5.2	11.6	12.6	9.5	10.5	12.6	8.8	8.3	5.3	6.5	
Domestic Air passenger traffic	15.7	19.2	26.3	23.6	19.3	10.7	8.7	8.1	5.0	5.8	4.7	3.8	5.9	6.9	7.6	6.7	7.4	10.0
Personal loans	19.0	21.0	18.4	18.3	18.2	18.0	19.0	18.0	18.0	18.0	18.0	17.0	18.0	16.6	17.8	16.9	16.4	
PV sales	14.9	1.6	2.9	11.6	3.1	17.3	4.3	3.2	13.9	5.7	8.9	1.2	4.3	4.9	-2.0	-1.8	-1.4	0.9
Rural indicators																		
Rural wages	6.7	7.0	6.8	6.5	6.5	6.1	6.0	6.2	6.2	6.0	5.6	5.9	5.8	5.6	5.4	6.1	6.3	
2-wheeler sales	17.4	1.7	-7.2	0.6	0.8	20.1	31.3	16.0	26.2	34.6	15.3	30.8	10.1	21.3	12.5	9.3	15.8	14.2
3-wheeler sales	70.4	98.6	78.9	68.8	47.0	42.1	30.8	30.6	9.5	8.3	4.3	14.5	14.4	12.3	5.1	8.0	7.1	-0.2
Tractor sales	1.0	4.0	6.0	1.0	-15.0	-4.3	6.4	-19.8	-15.3	-30.6	-23.1	-3.0	0.0	3.6	1.6	-5.8	3.7	22.4
IIP consumer non-durable	8.9	0.5	8.3	9.9	2.7	9.3	-3.4	3.0	0.3	-3.2	5.2	-2.5	2.8	-1.0	-4.3	-4.5	2.0	
MGNREGA (person days)	9.0	10.0	16.0	32.0	9.0	20.0	-8.0	-10.9	-0.4	9.6	-17.6	-3.7	-19.4	-32.5	-26.1	-23.2	-18.7	-8.8

Fig 4: Demand for jobs has slowed under the employment guarantee scheme *(% y/y)*

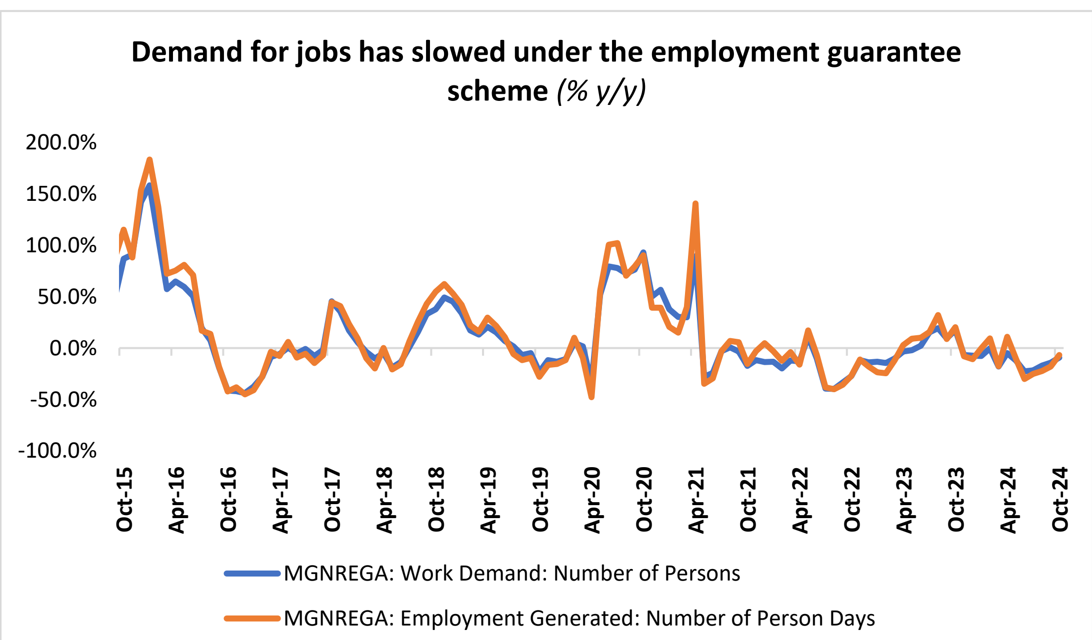


Fig 5: Rural wage growth on a recovery trend (% y/y)

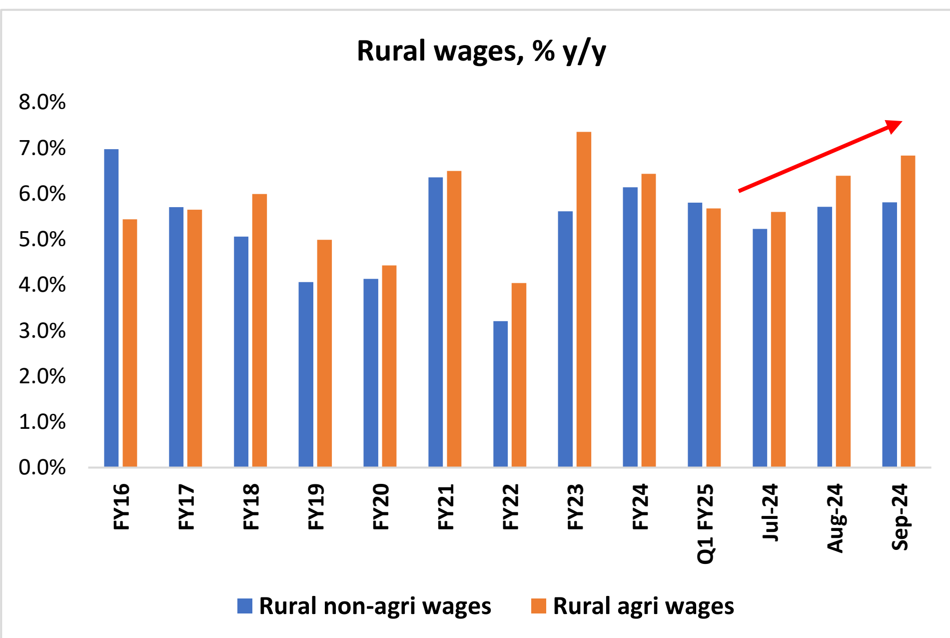


Fig 6: Urban wage growth have held relatively steady *(% y/y)*

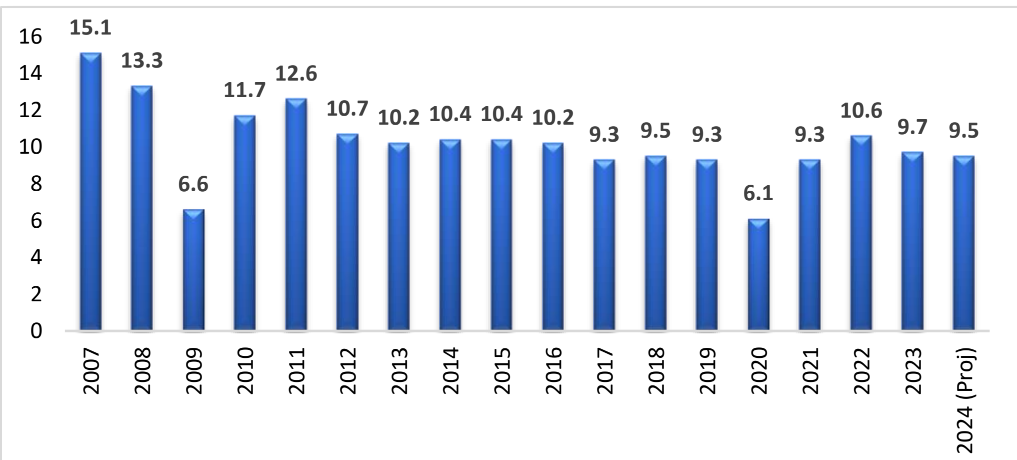
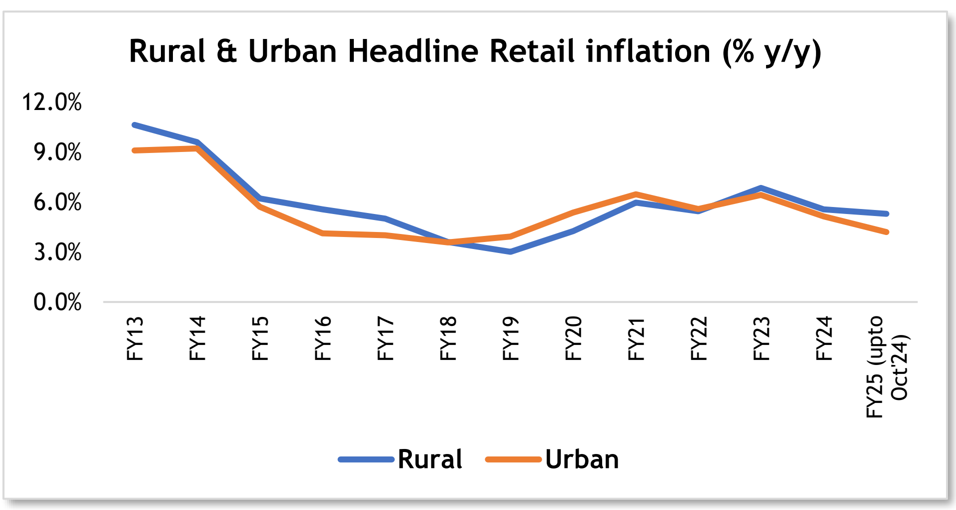


Fig 7: Slowdown in inflation in FY25 to support real purchasing power



Source: CEIC, RBI, Aon Survey

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