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FICCI Economic Outlook Survey

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About the Survey

The Economic Outlook Survey was conducted during the period January 1 to January 15, 2010. As part of the survey, a structured questionnaire was drawn up and sent to key economists for their inputs and views. 12 economists of repute participated in the survey. These economists largely come from the banking and financial sector. The sample however also includes economists from industry and research institutions.

The economists were asked to provide their **forecast for key macro economic variables for the year 2009-10** as well as for **Quarter 3 and Quarter 4** of the **current financial year**.

In addition to these, FICCI sought the views of economists on five topical economic issues – **sustainability of growth**, **continuation of fiscal stimulus in 2010-11**, **expected monetary policy action by RBI in the light of rising inflation**, **reasons for lackluster credit growth** and **factors responsible for rising food prices**.

The feedback received from the participating economists was aggregated and analyzed. The results obtained are presented in the following pages.

The findings of the survey represents the views of the leading economists and do not reflect the views of FICCI.

Executive Summary

Annual Forecasts for 2009-10

- GDP growth – 6.9 percent
- Agriculture and allied activities growth – (-) 1.0 percent
- Industry growth – 8.5 percent
- Services growth – 9.0 percent
- Fiscal Deficit – 7.0 percent of GDP
- IIP – 8.3 percent
- WPI inflation rate (End March 2010) – 8.1 percent
- USD / INR exchange rate (End March 2010) – Rs. 45 / USD
- Bank credit growth – 15.0 percent

Quarterly Forecasts for Q3 and Q4 of 2009-10

- GDP growth – 6.8 percent (Q3) and 7.5 percent (Q4)
- Agriculture and allied activities growth – (-) 2.0 percent (Q3) and 0 percent (Q4)
- Industry growth – 10.3 percent (Q3) and 10.0 percent (Q4)
- Services growth – 8.8 percent (Q3) and 9.0 percent (Q4)
- IIP – 10.8 percent (Q3) and 10.7 percent (Q4)
- WPI inflation rate – 7.5 percent (Q4)
- USD / INR exchange rate – Rs. 45.5 / USD (Q4)
- Bank credit growth – 15.0 percent (Q4)

Economists' views on

- **Sustainability of growth in the near term** – **No consensus amongst economists**. **Factors considered positive for growth** – rising consumption and investment levels, exports moving to positive territory , reasonable rabi output, uptick in credit growth, comfortable liquidity position domestic and external. **Factors that could moderate growth** – Sizable decline in agri GDP in Q3 and lingering impact in Q4, weakening impact of stimulus measures on manufacturing sector, consumers continue to remain risk averse, capital flows may not pick up quickly enough.
- **Continuation of fiscal stimulus in 2010-11 – Broad consensus on continuation of fiscal stimulus**. Sudden withdrawal of stimulus would adversely affect growth trajectory. Government may look at withdrawal of stimulus in sectors which are showing good performance. Exports must continue to get support as outlook for global economy is still uncertain. Programs like NREGA, JNNURM constitute a form of fiscal stimulus and must get adequate emphasis.
- **Expected monetary policy action by RBI – Majority expects RBI to tighten monetary policy with a 50 bps hike in CRR looking imminent.** Tight monetary policy will have no impact on inflation as it is largely a supply side driven phenomenon. Repo and reverse repo rate should not be hiked. Instead reverse repo could be lowered to disincentivise banks from parking funds at the RBI window and lend for productive purposes.
- **Lackluster credit growth** – **Companies are using non-banking sources for raising funds**. IPOs and QIPs are seeing good activity. Commercial paper and NCDs are being increasingly used. ECB is an important source though recent move by RBI could cut down flows on this account. **Credit growth picks up with a lag following recovery**. Any interest rate hike by banks now would impact growth and corporate profitability. Input costs already on the rise and any increase in interest rates would further dent the profit margins. Even a slight increase in interest rates can impact large infrastructure projects which operate on competitive IRRs.
- **Food inflation** – Larger issue is high growth and rising incomes (NREGA) leading to more demand for food items while supplies languish. More recently, supply shortages on account of drought / floods, continuous increase in MSPs, delayed response with regard to imports, poor PDS management and speculation have aggravated inflation. Rabi output and recent administrative measures of government will help in cooling prices.

TABLES

Annual Forecasts for 2009-10[1]

- The economists participating in the Economic Outlook Survey have forecasted **annual GDP growth rate** (at factor cost) **for the year 2009-10** to be **6.9 percent**. The forecast for GDP growth rate ranged between a minimum of 6.5 percent to a maximum of 7.4 percent.

- The sectoral GDP forecast for the year 2009-10 shows that **agriculture will show a negative growth of 1 percent**. Agriculture sector's growth rate forecast ranged between -3.3 percent and 1.8 percent. The economists expect the **industry sector to grow at 8.5 percent** and the **services sector to mark a growth of 9 percent in 2009-10**. While the range for industry sector growth is 6 percent to 9 percent, the range for services sector growth is 7.8 percent to 12 percent.

- The economists have projected that the **fiscal deficit of the centre for the year 2009-10 would be 7 percent of GDP** which is above the budget estimate of 6.8 percent. The range for the projections for fiscal deficit varies from 6 percent to 7.5 percent.

- The surveyed economists anticipate that **IIP would grow by 8.3 percent during the fiscal 2009-10**.

- The surveyed economists have estimated that while **WPI inflation will go up to 8.1 percent by end March 2010**, the **CPI (IW) inflation would be further high at 11.1 percent by end March 2010**.

- The **money supply (M3) growth is projected to be 17.5 percent during 2009-10**.

- The economists have forecasted the growth rate of exports and imports for the financial 2009-10 to be in a negative territory. While the **median forecast for export growth is -8.9 percent, the same for imports is -12.0 percent**. Even the **trade balance** is expected to be in the negative territory at -**8.0 percent of the GDP** during the current fiscal.

- The **Rupee exchange rate** is estimated to be **Rs. 45 per USD by end March 2010**. The responses varied between a high of Rs. 43.5 per USD and a low of Rs. 46.2 per USD.

- When asked about the **average PLR of the PSU banks** by **end March 2010**, majority of the economists have reported that it will lie **between 11.0 percent and 12.0 percent**.

- Though the **bank credit growth** is sluggish now, the economists feel that it will pick up gradually and will hit **15 percent growth during 2009-10**.

[1] **All forecast figures indicated are the median forecast of the sample**

Quarterly Forecasts for Q3 (Oct-Dec) and Q4 (Jan-Mar) of 2009-10[2]

- The economists have projected **GDP growth** (at factor cost) for the **third quarter (Q3) of 2009-10 to be 6.8 percent** and then rise during the **fourth quarter (Q4) to 7.5 percent**.

- Looking at a sector wise growth projections for Q3 and Q4, economist's feel that **there will be a dip in the agricultural sector growth while industry and services sector will show a consistent growth performance.** The industrial sector is estimated to grow at a relatively faster rate among the three sectors.

- The economists feel that there will be a dip in the growth rate of **agriculture and allied activities** in Q3 and that agri GDP will be in the negative zone - the **agri sector is estimated to decline by 2 percent in Q3**, **2009-10**. Although the sector will move away from the negative growth trend during the following quarter, in **Q4 2009-10 growth will be flat**.

- The industry sector is expected to show a consistent growth over Q3 and Q4 of 2009-10 as projected by the survey participants. The surveyed economists feel that the **industry sector** will show a GDP growth rate of **10.3 percent and 10.0 percent in Q3 and Q4** of the current financial year respectively. The same trend is seen in the **services sector,** which is expected to grow by **8.8 percent during Q3 and 9.0 percent during Q4, 2009-10**.

- The economists believe that growth in **IIP** is sustainable and in **Q4 of 2009-10** will show a growth rate to the tune of **10.7 percent**.

- Economists anticipate **WPI inflation rate** to be at **7.5 percent for Q4, 2009-10**, while **CPI (IW)** is **projected at 11.2 percent** during the same period.

- Economists foresee **money supply growth** at **17.5 percent during Q3** and at **18.0 percent during Q4** of 2009-10.

- The survey respondents are optimistic about **export performance** with the growth **projected at 11 percent during Q3 and 17 percent during the last quarter** of current fiscal. On the other hand, **imports** are **expected to show a negative growth of 0.5 percent in Q3** but will recover to a **high growth rate of 20 percent in Q4**.

- The economists feel that the country's **trade balance** will be in a negative zone in both the third and the fourth quarter of 2009-10. The trade balance is projected at -8.2% of GDP for Q3 and at -7.1% of GDP in Q4 of 2009-10.

- The forecasters feel that **exchange rate** of Rupee would be around **45.5 per USD in Q4 of 2009-10.**

- Economists have projected **bank credit to grow by 15 percent in the fourth quarter of 2009-10**.

[2] **All forecast figures indicated are the median forecast of the sample. Sample size varies as not all participants provided quarterly projections and for all variables**

Economists' views on sustainability of growth in the near term

Indian economy grew by a robust 7.9 percent in the second quarter of fiscal 2009-10. The surveyed economists were requested to provide their feedback and views on the sustainability of this growth in the near term. And the responses received from the survey participants clearly shows that ***there is no consensus on this issue. In fact the number of economists who feel that the Indian economy would see a sustainable high growth in the near term evenly matches those who feel the situation would not be all that good***.

According to those who hold the view that the high growth seen in the second quarter is sustainable in the near term, the factors that would aid the growth process as we go ahead include:

- Private consumption and investment level in the economy have started moving up and would now complement government consumption in driving overall growth. Capital expenditure cycle is expected to move up particularly on the back of rising infrastructure investments which in turn is the result of stimulus measures announced by government.
- Exports have turned positive after thirteen straight months of decline. With the global economy showing signs of stabilization, India's exports would further pick up in the coming months.
- Manufacturing sector and services sector would negate the adverse impact agriculture sector would have on GDP in the third and fourth quarters of current fiscal. In fact, with the rabi output projected to be reasonable, agricultural GDP in the last quarter would also contribute to overall GDP growth.
- Credit growth is now showing a gradual pick up and is expected to continue in the weeks / months ahead. This should be a further stimulant for overall economic activity.
- The liquidity situation – domestic and global – is comfortable and should keep the growth momentum going.
- GDP growth in the fourth quarter of 2008-09 was particularly weak at 5.5 percent. Due to this low base, GDP growth in the last quarter of this fiscal would be comparatively higher.

On the other hand, the reasons cited by those who feel that the GDP growth would moderate in the near term include:

- Agriculture sector GDP would see a sizable decline in the third quarter of current fiscal. The impact of poor kharif output would be reflected in the Oct-Dec quarter of 2009-10.
- It is unlikely that the momentum in the manufacturing sector would be maintained in the last two quarters of this fiscal. Growth in manufacturing sector in the second quarter was largely stimulus driven and was higher than expected.
- The manufacturing sector has built up the inventory levels. This was a one-time event and will not be repeated any time soon.
- Investment activity in the economy is still sluggish. Private consumption too has not revived significantly and consumers continue to remain risk averse.
- Capital flows though rising may not pick up quickly enough and to that extent limit the funds availability for economic activities.
- High growth seen in the first and second quarter of current fiscal was driven by a significant drop in imports, particularly oil imports. With imports positioned to move up, the positive addition to GDP may be negated.

♣ Economists' views on continuation of fiscal stimulus in the year 2010-11

Continuation on fiscal stimulus in the next financial year is turning out to be a major debatable issue. While it is true that the package of fiscal measures that the government came out with in the wake of slowing down of the economy was largely responsible for arresting the economy's slide last year, it is equally important to note that fiscal deficit has reached a fairly high level. It is concerns relating to high fiscal deficit that are leading to certain sections in the policy circles to suggest withdrawal of fiscal stimulus measures in the forthcoming budget. FICCI put across this issue to the surveyed economists and the responses received show that there is a ***broad consensus on continuation of fiscal stimulus in the next budget***.

Majority of the survey respondents have said that a sudden and complete withdrawal of the stimulus measures in the next budget would adversely affect the growth trajectory of the economy. The government may instead look at gradual rolling back of the stimulus and in those segments that are showing improvement in their performance. This would also aid in the fiscal consolidation process. Moreover, growth and fiscal consolidation are complementary as higher growth would lead to higher revenues for the government.

According to some of the surveyed economists, the global economic recovery is being led by the emerging market economies, particularly from the Asian region. How conditions in the western economies would shape up is still unclear. Hence, it would be appropriate if the government continues with the fiscal support especially for the export sector.

Economists have also pointed out that government programmes such as NREGA, JNNURM etc entail huge expenditure and these too constitute a form of fiscal stimulus. Given the far reaching impact which these programs have, government must continue with its emphasis on these and other similar programmes.

♣ Economists' views on expected monetary policy action by the RBI

Headline inflation based on WPI has moved up from 4.78 percent in November 2009 to 7.31 percent in December 2009. Figures at the disaggregated level show that inflation is being driven largely by rise in prices of primary articles. This rise in inflation numbers is a matter of concern. The participating economists were asked to give their views on what monetary policy action they were expecting from the RBI in the forthcoming third quarter review later this month. Inputs received by FICCI show that the ***majority of the surveyed economists expect RBI to tighten the monetary policy with a hike in CRR of up to 50 basis points looking imminent***.

According to many participating economists, while **a hike in CRR and other monetary policy variables will have no impact on inflation**, **as this is being driven largely by supply side factors** that are at work, RBI may still want to indicate its seriousness about this issue though a symbolic move in the forthcoming monetary policy. A hike in CRR at this point in time may tone down the inflationary expectations that are building in the economy but would fail to arrest inflation as it is not a monetary phenomenon.

Majority of the surveyed economists have reported that the central bank should desist from raising the repo and the reverse repo rate at this point in time. Some have even suggested that instead of tightening, the reverse repo rate should be lowered as this would disincentive banks to park money at the RBI window and instead lend it for productive purposes. A hike in rates could lead banks to up their PLRs and thereby reduce credit off-take while also increasing the possibility of delinquent assets.

Economists' views on lackluster credit growth and impact of a possible interest rate hike on growth and corporate profit

Although recent numbers on industrial production show that industrial growth is gathering momentum, this up-tick in economic activity is not getting reflected in the credit growth figures. Statistics show that credit growth continues to remain close to the 12-13 percent mark and is much lower as compared to the RBI target for the year. It is only in December 2009 (fortnight ending January 1, 2010) that we saw credit off take showing signs of improvement. FICCI asked the participating economists on what factors they feel were responsible for this trend and what would the impact of a hike in interest rates by banks at this juncture on overall growth and corporate profits.

Feedback received from economists shows that there are a ***variety of reasons that can be ascribed for this slow pace of credit expansion***. The reasons mentioned include –

- Companies are relying more on equity financing given the attractive valuations. Initial Public Offers and Qualified Institutional Placement windows are seeing good activity.
- Commercial paper and non-convertible debentures are also being increasingly used by the corportaes for raising resources.
- Companies are also utilizing internal resources that were built up over the last two years.
- Access to external sources of finance has improved. However, the recent changes introduced in the ECB guidelines would force some companies to look at the domestic banking sector for meeting financing requirements.
- Due to a fall in oil prices, oil companies have cut down on their borrowings from the banking sector.
- Mutual funds have been active in meeting the working capital requirement of companies. With the RBI taking note of this phenomenon, it is likely that companies will have to go back to the banks for their working capital requirements.
- Overall working capital requirement of corporates has been down due to lower commodity prices and de-stocking.
- Investment activity is still to gather full momentum and banks are still plagued by risk aversion towards lending largely to the SME sector.

While alternate non-banking sources are gaining in importance as a source of funds for companies, it is equally important to note that credit growth generally picks up with a lag following industrial recovery. During the initial phase of recovery, companies generally tend to use limited leverage and focus more on productivity increases to support volume growth. Many of the surveyed economists feel that as we move ahead in time (in 2010) credit growth will pick up.

On the issue of a possible ***rise in interest rates by the banking sector*** and it impact on growth and corporate profits, the ***majority view*** is that this ***would have a deleterious effect on economic growth and corporate profitability***. The surveyed economists have opined that with input costs already on the rise, any increase in interest rates would further dent the profit margins of corporates. Further, even a slight increase in interest rates can impact large infrastructure projects which operate on competitive IRRs.

Economists' views on food inflation

Food inflation has been a cause for concern for some time now. Numbers indicate that prices of several agricultural commodities have been rising at a fast pace and contributing to the overall increase in the inflation level in the country. This issue has taken centre stage with both the central bank and the government indicating that strong measures would be taken to address the inflation problem lest inflationary expectations gather steam and become a self fulfilling prophecy. In the FICCI Economic Outlook Survey, the participating economists were asked to comment on the food inflation scenario and indicate when they see prices cooling down.

The inputs received show that there are ***two sets of reasons that can be attributed to the rise in the prices of food / agri commodities in the country***.

One important reason cited by some of the respondents relates to the high growth seen in the Indian economy over the last few years and the related development of increasing incomes. According to the participating economists, with high growth and rising incomes the demand for food products has been going up over time. Government programmes like NREGA have also contributed to increasing purchasing power amongst people living in the rural areas. While overall demand for food items has been going up, the supplies have not risen to the extent needed and this mismatch is leading to higher prices.

While the above is a long term phenomenon, there are several other factors that have / are contributing to a rise in prices of food items. And these include –

- Supply shortages due to drought and floods seen in different parts of the country last year.
- Continuous increase in the Minimum Support Prices of various food items by the government.
- Delayed response on part of the government in terms of importing the required food items and making the same available throughout the country.
- Poor management and distribution of food stocks through the PDS.
- Speculation and hoarding of food items.

The participating economists are of the opinion that the Indian agriculture sector suffers from structural problems which need to be addressed on a mission mode basis or else inflation will become a chronic problem capable of derailing the India growth story. It is only by addressing issues of low productivity, food wastage, weak farm to market linkages due to dilapidated infrastructure that we can expect to raise food production levels in the country and address the inflation problems on a sustainable basis.

With regard to food price inflation in the near term, the majority of the economists expect that with the rabi output coming into the market soon food prices would see a downward movement. Further, steps taken by the government to ease imports of certain items and drawdown from the food stocks would also help in easing the inflationary pressure in the near term.

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♣ Annual Forecasts for 2009-10

	Key Macroeconomic Variables	Annual Forecast 2009-10			
		Mean	Median	Max	Min
1	GDP growth rate at factor cost (%)	6.9	6.9	7.4	6.5
	Agriculture & Allied	-1.0	-1.0	1.8	-3.3
	Industry	8.2	8.5	9.0	6.0
	Services	9.1	9.0	12.0	7.8
2	Fiscal Deficit (as % to GDP) Centre	6.9	7.0	7.5	6.0
3	Growth in IIP (%)	8.2	8.3	9.5	6.0
4	WPI Inflation rate (%) (End March 2010)	7.7	8.1	9.0	4.5
5	CPI-IW Inflation rate (%) (End March 2010)	11.6	11.1	15.0	9.0
6	Money Supply (M3) growth (%)	17.3	17.5	19.6	12.0
7	Merchandise Export growth (%)	-5.0	-8.9	13.0	-15.0
8	Merchandise Import growth (%)	-9.8	-12.0	10.0	-19.0
9	Trade Balance (% to GDP)	-8.2	-8.0	-5.0	-12.0
10	US$ / INR exchange rate (End March 2010)	45.0	45.0	46.2	43.5
11	Bank credit growth (%)	14.7	15.0	16.0	12.0

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♣ Quarterly Forecasts for Q3 (Oct-Dec) and Q4 (Jan-Mar) of 2009-10

	Key Macroeconomic Variables	Quarterly Forecasts							
		2009-10 Q3 (Oct-Dec)				2009-10 Q4 (Jan -Mar)			
		Mean	Median	Max	Min	Mean	Median	Max	Min
1	GDP growth rate at factor cost (%)	6.9	6.8	8.0	6.0	7.3	7.5	8.5	6.0
	Agriculture & Allied	-2.8	-2.0	-1.0	-5.5	-0.2	0.0	2.5	-3.0
	Industry	9.8	10.3	11.5	6.8	9.6	10.0	13.0	6.8
	Services	9.3	8.8	13.5	8.0	9.3	9.0	13.5	7.9
2	Growth in IIP (%)	10.6	10.8	13.3	7.5	10.3	10.7	12.8	7.5
3	WPI Inflation rate (%)					7.1	7.5	8.8	5.0
4	CPI-IW Inflation rate (%)	11.9	12.5	13.5	8.0	11.5	11.2	15.0	8.0
5	Money Supply (M3) growth (%)					17.6	18.0	18.5	16.0
6	Merchandise Export growth (%)	13.6	11.0	26.0	7.9	18.6	17.0	25.0	13.5
7	Merchandise Import growth (%)	-1.8	-0.5	5.0	-10.0	17.5	20.0	40.1	-8.5
8	Trade Balance (% to GDP)	-3.9	-8.2	8.0	-11.5	-2.9	-7.1	9.0	-10.5
9	US$ / INR exchange rate					45.4	45.5	46.3	44.5
10	Bank credit growth (%)					14.5	15.0	16.0	12.5

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