

FICCI

FICCI Economic Outlook Survey

July 2010

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FICCI Economic Outlook Survey – July 2010

About the Survey

FICCI's Economic Outlook Survey is a quarterly survey conducted amongst leading economists of the country with a view to gauge their perception and views on topical economic issues as well as seeks their outlook for key macro-economic variables. The economists who take part in this survey largely come from the banking and financial sector. The sample however also includes economists from industry and research institutions.

The first survey report was released in January 2010 and the second report was released in April 2010. This is the third report of the Economic Outlook Survey. The survey was conducted during the period June 24, 2010 and July 15, 2010. As part of the survey, a structured questionnaire was drawn up and sent to key economists for their inputs and views. This time 14 economists of repute participated in the survey.

The economists were asked to provide their **forecast for key macro economic variables for the year 2010-11** as well as for **Quarter 1 (Apr-June) and Quarter 2 (July- Sep) of 2010-11**.

In addition to these, FICCI sought the views of economists on some topical issues like **expected monetary policy action by RBI in the forthcoming monetary policy review; downside risks to growth during fiscal 2010-11; outlook for inflation of primary articles and manufactured products**.

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.

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Executive Summary

Annual Forecasts for 2010-11

- ♣ GDP growth – 8.5 percent
- ♣ Agriculture and allied activities growth – 3.5 percent
- ♣ Industry growth – 10.0 percent
- ♣ Services growth – 9.0 percent
- ♣ Fiscal Deficit – 5.1 percent of GDP
- ♣ IIP – 10.6 percent
- ♣ WPI inflation rate (End March 2011) – 6.5 percent
- ♣ Money Supply (M3) growth – 17.0 percent
- ♣ Trade Balance – (-) 8.2 percent
- ♣ USD / INR exchange rate (End March 2011) – Rs. 44.5/USD
- ♣ Bank credit growth – 20.0 percent

Quarterly Forecasts for Q1 (Apr- June) and Q2 (July- Sep) of 2010-11

- ♣ GDP growth – 8.7 percent (Q1, 2010-11) and 8.5 percent (Q2, 2010-11)
- ♣ Agriculture and allied activities growth – 2.6 percent (Q1, 2010-11) and 4.0 percent (Q2, 2010-11)
- ♣ Industry growth – 11.0 percent (Q1, 2010-11) and 10.0 percent (Q2, 2010-11)
- ♣ Services growth – 9.2 percent (Q1, 2010-11) and 9.1 percent (Q2, 2010-11)
- ♣ IIP – 13.1 percent (Q1, 2010-11) and 11.0 percent (Q2, 2010-11)
- ♣ WPI inflation rate – 10.0 percent (Q2, 2010-11)
- ♣ Money Supply (M3) growth – 15.8 percent (Q2, 2010-11)
- ♣ Trade Balance – (-) 8.0 percent (Q2, 2010-11)
- ♣ USD / INR exchange rate – Rs. 46.0/USD (Q2, 2010-11)
- ♣ Bank credit growth – 19.5 percent (Q2, 2010-11)

Economists' views on

- ♣ **Expected monetary policy action by the RBI.** Majority of economists feel RBI would continue to move ahead on the path of monetary tightening and **anticipate a hike of 25 basis points each in the repo rate and reverse repo rate in July 27, 2010.** Given the present liquidity situation, a hike in CRR on July 27, 2010 was however ruled out by the participating economists.

Surveyed economists feel non-food manufacturing inflation is now rising at a fast pace and this could be a source of worry for the RBI. Further, the full impact of the fuel price revision on inflation numbers is yet to be seen according to the economists. On the growth front, surveyed economists believe that while the recent IIP numbers may have shown a decline from 16.5 percent in April 2010 to 11.5 percent in May 2010, such a growth is still reasonable and may not dissuade RBI from restricting monetary policy action.

Though the above is the majority view, a few respondents opined that given the moderation in IIP growth and the expected slowdown of inflation in the coming months, a further rate hike by RBI during the policy review appears unlikely at this juncture. They also feel that such frequent rate hikes could derail the growth momentum the economy is witnessing presently.

- ♣ **Potential downside risks to growth in 2010-11.** Downside risks to growth emanate from both domestic and global developments.

- ✚ **Domestic factors that could pull down growth include**

- ✂ **One, progress and spatial distribution of the monsoon.** Data shows that cumulative rainfall in the country between June 1 and July 14 was below normal by 13 percent. A less than optimum monsoon would adversely impact agricultural growth. Even if the rains were normal this year, overall agricultural performance may not be 'too strong' as overall soil productivity is now on the lower side. Further, if less rainfall can impact agricultural output, excessive rains and subsequent floods too will be a negative development. Some of the northern states are already seeing floods and this will have a bearing on agri output.
 - ✂ **Two, inflationary situation.** The headline inflation continues to remain stubbornly high. The recent fuel price revision will have an inflationary impact in the months ahead. Economists have pointed out that high prices are eating into the budget of the middle class population as far as their outlay for industrial produce is concerned. Thus if inflation persists at the current levels for a long time or if there is a sharper than anticipated pick-up in inflation then consumption demand could get dampened.
 - ✂ **Three, premature and aggressive monetary policy action.** While normalization of the monetary policy is expected and RBI would continue to tighten rates in the months ahead, premature and aggressive rollback of easy money policy can jeopardize growth. Rapid tightening of monetary policy will affect both consumption and investment demand and this could ease the growth impulses.
 - ✂ **Four, social unrest leading to output losses.** Given the recent pick up in naxal activities there is a fear that greater social unrest in times ahead may also lead to output losses and thus impact the growth trajectory.

- ✚ **External factors that could pull down growth include**

- ✂ **One, uncertainty regarding global recovery.** There are evident concerns with regard to developments taking place in the Euro Zone. Many believe that the next shock to the capital markets could come from evolving situation in the Euro area. This could increase volatility in capital flows and restrict availability of funds for supporting growth. Besides Euro area, economists are also skeptical about the direction of the US economy. There is a slight chance, some believe, of US economy getting into another recession. This, if it happens, will put a cap on our export growth (services sector like IT will get hit) and in turn affect GDP performance.
 - ✂ **Two, high commodity prices.** High commodity prices including crude prices is also being seen a risk to India's growth in 2010-11 by a small set of economists.

- ♣ **Inflation situation. Majority of the economists do not expect inflation rate to fall to the 5 percent mark by end December 2010 as estimated by the government.** The general view is that headline

inflation would continue to remain around the present levels for the next few months and then gradually trend downwards. There are three broad reasons which economists feel would prevent headline inflation from coming down at least in the next one or two months –

- ✚ **Impact of recent hike in the fuel prices** - Fuel price hike will add to the transportation cost for primary articles as well as increase the input costs for manufactured goods.
- ✚ **Sticky food inflation** - Spatial distribution of monsoon will be a key factor under watch here
- ✚ **Depreciation of INR** which is preventing any meaningful reflection of lower global prices in metals on inflation rate in India

Although inflation would after some time trend downwards, but **a good number of economists expect that by December 2010, headline inflation rate would continue to be in the range of 6 percent to 8 percent.**

Looking at the prognosis for the two key components – primary articles and manufactured articles – the trend is expected to be the same as for overall inflation. The only difference being that primary inflation will start to cool down from July / August 2010 onwards as the ‘negative base effect’ will come into play then and manufactured articles inflation would trend down from November 2010 onwards as it was in November 2009 when manufactured goods price index had shown a spike. Besides this base effect, some of the other factors that should help ease inflation later this year include –

- ✚ **Low probability of further high MSP hikes** (Primary articles inflation)
- ✚ **Slowdown in global growth which would keep a lid on commodity prices particularly those of industrial metals** (Manufactured articles inflation)

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♣ Annual Forecasts for 2010-11¹

- ✚ The economists who participated in the third round of FICCI's Economic Outlook Survey have estimated **annual GDP growth rate** (at factor cost) **for the fiscal year 2010-11** to be **8.5 percent**. The estimates from different participants for GDP growth rate range from a minimum of 7.8 percent to a maximum of 9.0 percent. The economists' forecast for annual GDP growth rate this time is very close to the 8.4 percent forecast made in the last survey (April 2010).
- ✚ The sector wise GDP forecast by the survey respondents shows that **agriculture and allied activities will grow by 3.5 percent during the year 2010-11**, which is lower than the forecast of 4.0 percent obtained in the earlier survey. Primary sector's growth forecast varied from 2.5 percent to 5.4 percent.
- ✚ **Forecasters have revised industry sector growth number upwards to 10.0 percent during 2010-11** from 9.2 percent in the last survey. At the same time, they foresee that **service sector will clock a growth rate of 9.0 percent in 2010-11**, which is a lower estimate from the 9.3 percent obtained in the previous survey for the same year. While the range for industry sector growth is 8.8 percent to 12.0 percent, the range for services sector growth is 8.1 percent to 10.0 percent.
- ✚ **Economists see central government fiscal deficit at 5.1 percent during 2010-11**, which is a downward revision from 5.8 percent obtained in the earlier survey. The estimate ranges between a minimum of 5.0 percent to a maximum of 6.0 percent.
- ✚ The respondents anticipate that **IIP would grow at a rate of 10.6 percent during 2010-11** against the earlier forecast of 10.0 percent.
- ✚ The surveyed participants adjusted both the WPI and the CPI (IW) against their earlier estimates. **The WPI inflation rate is revised by about 1 percentage points to be placed at 6.5 percent by end March 2011** against 5.5 percent in the earlier estimate. **The CPI (IW) inflation also is expected to settle at a higher rate of 8.0 percent**. This is however lower than the previous estimate of 8.5 percent. The range of both the WPI and the CPI (IW) varies between a minimum of 3.5 percent to a maximum of 9.1 percent and a minimum of 7.0 percent to a maximum of 11.4 percent respectively.
- ✚ **The money supply (M3) growth is projected to be 17.0 percent during 2010-11**. This was projected to be 19.6 percent in the previous survey.
- ✚ Economists have revised the export and import estimates upwards for 2010-11 from the earlier projections. While the **median forecast for export growth is 16.5 percent, the same for imports is 26.0 percent**. The earlier projections for export and import were 15.0 percent 12.0 percent respectively.
- ✚ In this round of survey, the economists revised the **trade balance slightly downwards to - 8.2 percent of the GDP during the current fiscal** against a - 8.3 percent of the GDP in the last survey.

¹ All forecast figures indicated are the median forecast of the sample

- ✚ Economists expect that **bank credit growth for the year 2010-11 would stand at 20.0 percent** against the earlier forecast of 19.0 percent.

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♣ **Quarterly Forecasts for Q1 (Apr-June) and Q2 (July- Sep) of 2010-11²**

- ✚ The surveyed economists estimate that the **GDP growth (at factor cost) for Q1 (Apr- June) 2010-11 to be 8.7 percent and then move down to 8.5 percent during Q2 (July- Sep) of 2010-11.**
- ✚ Looking at a sector wise growth projections the economists foresee a lower growth for agriculture and allied activities during the first quarter of 2010-11. **Agri and allied activities are estimated to grow at 2.6 percent during Apr-June. The sector however is expected to register a robust growth of 4.0 percent during the second quarter of the current fiscal** as per the projections made by the respondents.
- ✚ Both the secondary and the tertiary sector are projected to have a lower growth in the second quarter compared to the first quarter. Economists foresee that the **industrial sector will clock a robust growth of 11.0 percent during Q1 and the slide down by about one percentage point to 10.0 percent during Q2 of 2010-11. The service sector is projected to grow at 9.2 percent in the first quarter and then fall marginally to grow at 9.1 percent during the second quarter.**
- ✚ Economists expect that **IIP would clock a growth rate of 13.1 percent and 11.0 percent in the first and second quarter of 2010-11 respectively.**
- ✚ Economists anticipate that **the WPI inflation rate will be 10 percent in the second quarter of 2010-11.** They also expect the CPI (IW) to reduce to 11.0 percent in the second quarter from the projected figure of 13.7 percent in the first quarter.
- ✚ Economists foresee **money supply growth at 15.8 percent during Q2 of the current fiscal year.**
- ✚ The survey respondents feel that **the export growth will fall from 32.1 percent in the first quarter of 2010-11 to 27.3 percent in the second quarter of 2010-11. Imports are expected to see their growth going a notch down to 36.3 percent in the second quarter from a 38.8 percent in the first quarter of 2010-11.**
- ✚ The economists feel that the country's trade balance will be in a negative zone in both the first and second quarter of 2010-11 and also expects the trade balance to widen in the second quarter. **The trade balance is projected at (-) 7.0 percent of GDP for Q1 of 2010-11 and at (-) 8.0 percent of GDP in Q2 of 2010-11.**
- ✚ The forecasters feel that **exchange rate of Rupee would be around 46 per USD in Q2 of 2010-11.**
- ✚ Economists have projected **bank credit to grow by 19 percent in the first quarter of 2010-11 and then slightly increase to reach 19.5 percent during the second quarter of 2010-11.**

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

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

On July 2, 2010, the central bank announced a hike of 25 basis points in both repo and reverse repo rates. This intra policy date hike came as a surprise to many of the market participants who were expecting RBI to stay on status quo mode till July 27, 2010 when the quarterly review is due. Most of the economists who participated in the FICCI Economic Outlook Survey said that they were expecting RBI to tighten rates while announcing the monetary / credit policy review on July 27, 2010. A similar view was obtained when FICCI had interacted with the economists last month on the Greece Debt Crisis and how RBI would react keeping in mind developments in the Euro Zone. Given this and RBI's pre-emptive move, we asked the survey participants on what they thought RBI would now do at the forthcoming monetary policy review.

The responses received show that an **overwhelming majority of economists feel that RBI would continue to move ahead on the path of monetary tightening and that we should be prepared for another hike of 25 basis points each in the repo rate and reverse repo rate in July 27, 2010**. Given the present liquidity situation, a hike in CRR on July 27, 2010 was however ruled out by the participating economists.

Economists have pointed out that non-food manufacturing inflation is now rising at a fast pace and this could be a source of worry for the RBI. Further, the full impact of the fuel price revision on inflation numbers is yet to be seen according to the economists. They feel that this second point also gives RBI reason to continue with its policy tightening drive. On the growth front, surveyed economists believe that while the recent IIP numbers may have shown a decline from 16.5 percent in April 2010 to 11.5 percent in May 2010, such a growth is still sizable and may not dissuade RBI from restricting monetary policy action.

Though the above is the majority view, a few respondents opined that given the moderation in IIP growth and the expected slowdown of inflation in the coming months, a further rate hike by RBI during the policy review appears unlikely at this juncture. They also feel that such frequent rate hikes could derail the growth momentum the economy is witnessing at this point.

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♣ Economists' views on potential downside risks to growth in 2010-11

According to CSO, Indian economy registered a growth of 7.4 percent in 2009-10. This improvement in performance over the previous year (6.7 percent), and the continued momentum being seen both in consumption and in investment demand in the economy raised expectation about growth performance in the fiscal 2010-11. Both government and RBI have pegged GDP growth for 2010-11 at the level of 8 percent plus. More recent estimates coming from the IMF show that India may well clock a growth of 9.5 percent in 2010. While such forecasts are certainly encouraging and underline the steady growth being witnessed in the economy, there are at the same time a few factors that can pull down these favourable estimates for growth in 2010-11. In course of our discussion and interaction with the participating economists, FICCI requested them to list out the downside risks to growth they see in fiscal 2010-11. Feedback received shows that the downside risks to growth emanate from both domestic and global developments.

Taking the **domestic factors** first, the following points were raised by the surveyed economists.

One, progress and spatial distribution of the monsoon. It was pointed out that although the monsoon has gathered pace in recent days, we are still in the 'deficiency zone'. Data shows that cumulative rainfall in the country between June 1 and July 14 was below normal by 13 percent. According to most economists, a less than optimum monsoon would adversely impact agricultural growth which in turn will have a bearing on overall GDP performance. It was also pointed out that even if the rains were normal this year, overall agricultural performance may not be 'too strong' as overall soil productivity is now on the lower side. Further, if less rainfall can impact agricultural output, excessive rains and subsequent floods too will be a negative development. Some of the northern states are already seeing floods and this will have a bearing on agri output.

Two, inflationary situation. The headline inflation continues to remain stubbornly high. What is more worrisome is that inflation is now spreading from primary articles to fuel and manufactured goods. The recent fuel price revision will have an inflationary impact in the months ahead. Although the inflation situation is expected to ease by the close of 2010, there is still a lot of concern that is seen with regard to movement of this variable in the days ahead. Economists have pointed out that high prices are eating into the budget of the middle class population as far as their outlay for industrial produce is concerned. Thus if inflation persists at the current levels for a long time or if there is a sharper than anticipated pick-up in inflation then consumption demand could get dampened.

Three, premature and aggressive monetary policy action. In the recent past we have seen that RBI has not hesitated from announcing an intra policy rate hike in key policy rates. While normalization of the monetary policy is expected and RBI would continue to tighten rates in the months ahead, premature and aggressive rollback of easy money policy can jeopardize growth. Rapid tightening of monetary policy will affect both consumption and investment demand and this could ease the growth impulses.

Four, social unrest leading to output losses. Besides macro issues highlighted above, a small set of economists FICCI spoke to have also raised the issue of naxal problem that afflicts some of the major states in the country. Given the recent pick up in naxal activities there is a fear that greater social unrest in times ahead may also lead to output losses and thus impact the growth trajectory.

Coming now to the **external factors**, the surveyed economists drew attention to the following points.

One, uncertainty regarding global recovery. Most of the economists have highlighted state of the global economy as a key factor that will impact India's growth performance in 2010-11 and beyond. There are evident concerns with regard to developments taking place in the Euro Zone. Many believe that the next shock to the capital markets could come from evolving situation in the Euro area. This could increase volatility in capital flows and restrict availability of funds for supporting growth. Besides Euro area, economists are also skeptical about the direction of the US economy. There is a slight chance, some believe, of US economy getting into another recession. This, if it happens, will put a cap on our export growth (services sector like IT will get hit) and in turn affect GDP performance.

Two, high commodity prices. High commodity prices including crude prices is also being seen a risk to India's growth in 2010-11 by a small set of economists.

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♣ Economists' views on inflation situation

In May 2010, headline inflation touched 10.16 percent. In June 2010, the figure went up further to 10.55 percent. According to the Planning Commission there could be some further increase in inflation rate in July 2010 when the full impact of fuel price revision will come into effect. However, after that inflation rate is expected to trend down slowly and be around 5 percent by the close of this year. We asked the participating economists on how they viewed the inflation situation and are there an upside risk to inflation from here on.

The survey results show that majority of the economist do not expect inflation rate to fall to the 5 percent mark by the end December 2010. The general view amongst economists is that headline inflation would continue to remain around the present levels for the next few months and then gradually trend downwards. There are three broad reasons which economists feel would prevent headline inflation from coming down at least in the next one or two months –

- ✚ **Impact of recent hike in the fuel prices** - Fuel price hike will add to the transportation cost for primary articles as well as increase the input costs for manufactured goods. Further, with diesel prices too on the anvil of being deregulated there could be further pressure on price line in the days ahead
- ✚ **Sticky food inflation** - Spatial distribution of monsoon will be a key factor under watch here
- ✚ **Depreciation of INR** which is preventing any meaningful reflection of lower global prices in metals on inflation rate in India

Although inflation would after some time trend downwards, but **a good number of economists expect that by December 2010, headline inflation rate would continue to be in the range of 6 percent to 8 percent.**

Looking at the prognosis for the two key components – primary articles and manufactured articles – the trend is expected to be the same as for overall inflation. The only difference being that primary inflation will start to cool down from July / August 2010 onwards as the 'negative base affect' will come into play then and manufactured articles inflation would trend down from November 2010 onwards as it was in November 2009 when manufactured goods price index had shown a spike. Besides this base effect, some of the other factors that should help ease inflation later this year include –

- ✚ Low probability of further high MSP hikes (Primary articles inflation)
- ✚ Slowdown in global growth which would keep a lid on commodity prices particularly those of industrial metals (Manufactured articles inflation)

♣ Annual Forecasts for 2010-11

Key Macroeconomic Variables	Annual Forecast 2010-11			
	Mean	Median	Max	Min
1 GDP growth rate at factor cost (%)	8.4	8.5	9.0	7.8
<i>Agriculture & Allied</i>	3.7	3.5	5.4	2.5
<i>Industry</i>	9.9	10.0	12.0	8.8
<i>Services</i>	9.1	9.0	10.0	8.1
2 Fiscal Deficit (as % to GDP) Centre	5.3	5.1	6.0	5.0
3 Growth in IIP (%)	10.8	10.6	13.0	8.0
4 WPI Inflation rate (%) (End March 2011)	6.6	6.5	9.1	3.5
5 CPI-IW Inflation rate (%) (End March 2011)	8.6	8.0	11.4	7.0
6 Money Supply (M3) growth (%)	17.3	17.0	18.5	15.5
7 Merchandise Export growth (%)	18.5	16.5	40.0	8.0
8 Merchandise Import growth (%)	25.8	26.0	50.0	12.0
9 Trade Balance (% to GDP)	-8.4	-8.2	-7.7	-9.4
10 US\$ / INR exchange rate (End March 2011)	44.7	44.5	46.5	44.0
11 Bank credit growth (%)	20.5	20.0	23.0	17.0

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♣ **Quarterly Forecasts for Q1 (Apr- June) and Q2 (July- Sep) of 2010-11**

	Key Macroeconomic Variables	Quarterly Forecasts							
		Apr-June (Q1 2010-11)				Jul-Sep (Q2 2010-11)			
		Mean	Median	Max	Min	Mean	Median	Max	Min
1	GDP growth rate at factor cost (%)	8.6	8.7	9.5	7.9	8.4	8.5	9.1	7.8
	<i>Agriculture & Allied</i>	2.6	2.6	4.0	1.5	3.5	4.0	5.0	1.0
	<i>Industry</i>	11.3	11.0	13.8	8.5	10.1	10.0	12.0	8.6
	<i>Services</i>	9.1	9.2	10.0	8.0	9.0	9.1	10.7	7.6
2	Growth in IIP (%)	13.1	13.1	16.0	9.0	11.3	11.0	13.5	8.6
3	WPI Inflation rate (%)	10.5	10.5	11.0	10.0	10.1	10.0	11.6	9.0
5	CPI-IW Inflation rate (%)	13.5	13.7	14.7	12.0	11.2	11.0	14.5	8.9
6	Money Supply (M3) growth (%)	17.0	17.0	17.0	17.0	16.0	15.8	19.0	14.0
7	Merchandise Export growth (%)	31.9	32.1	35.0	30.0	27.5	27.3	40.0	17.3
8	Merchandise Import growth (%)	37.1	38.8	45.0	23.0	35.9	36.3	50.0	23.0
9	Trade Balance (% to GDP)	-8.1	-7.0	-7.0	-10.4	-8.7	-8.0	-7.5	-10.5
10	US\$ / INR exchange rate	46.3	46.4	46.6	46.0	45.8	46.0	46.5	45.0
11	Bank credit growth (%)	19.0	19.0	19.0	19.0	19.5	19.5	22.0	16.8

