

II. AGGREGATE DEMAND*

Aggregate demand weakened further in Q1 of 2012-13, led by patchy investment demand. Corporate sales have moderated significantly. On the fiscal front, the deficit indicators have considerably widened. While the slowdown has had an impact on indirect taxes, both excise and customs, public expenditure remained high, particularly on subsidies. Recent initiatives taken by the government, especially those related to its expenditure on fuel subsidies are welcome but are less than adequate to avert fiscal slippage in 2012-13. Further steps will need to be taken soon.

Protracted slowdown in private consumption and investment

II.1 Expenditure side GDP growth moderated sharply to 3.9 per cent in Q1 of 2012-13 from 9.0 per cent in the corresponding quarter of previous year (Table II.1). Private final consumption expenditure and gross fixed capital

formation, which account for around 60 per cent and 30 per cent, respectively, of GDP and which had both decelerated in the previous year, slackened further in Q1 of 2012-13.

II.2 The downturn in investment, as explained in previous reports, was led by non-monetary factors, though interest rates also had a material

Table II.1: Expenditure Side GDP (2004-05 prices)

Item	2010-11	2011-12	2011-12					2012-13
			Q1		Q2	Q3	Q4	Q1
			4	5	6	7	8	
			Growth Rates					
Real GDP at market prices	9.6	6.9	9.0	6.9	6.2	5.6	3.9	
Total Consumption Expenditure	8.1	5.4	4.9	4.9	6.1	5.8	4.7	
(i) Private	8.1	5.5	4.9	4.6	6.4	6.1	4.0	
(ii) Government	7.8	5.1	4.9	7.2	4.7	4.1	9.0	
Gross Fixed Capital Formation	7.5	5.5	14.7	5.0	-0.3	3.6	0.7	
Change in Stocks	37.4	2.4	7.1	2.8	0.4	-0.4	-1.2	
Valuables	32.4	7.9	9.8	9.4	2.9	9.3	-55.4	
Net Exports	5.5	-30.7	-23.2	-46.7	-117.9	117.8	-2.1	
Discrepancies	38.9	-112.7	-51.8	-119.6	-152.0	-124.0	-123.7	
			Relative shares					
Total Consumption Expenditure	70.1	69.1	70.1	70.8	72.7	63.6	70.6	
(i) Private	58.7	57.9	59.5	60.3	60.4	52.2	59.5	
(ii) Government	11.4	11.2	10.6	10.5	12.5	11.4	11.1	
Gross Fixed Capital Formation	32.5	32.0	33.9	33.4	30.3	30.9	32.8	
Change in Stocks	3.7	3.5	3.7	3.6	3.4	3.4	3.5	
Valuables	2.4	2.4	2.6	2.7	2.1	2.2	1.1	
Net Exports	-6.0	-7.4	-8.6	-11.3	-11.1	0.6	-8.5	
Discrepancies	-2.5	0.3	-1.7	0.8	2.6	-0.6	0.4	
<i>Memo:</i>								
Real GDP at market prices (₹ billion)	52368	55959	13174	13111	14377	15296	13693	

* : Quick Estimates. # : Revised Estimates.

Note: As only major items are included in the table, data will not add up to 100.

Source: Central Statistics Office.

* Despite its well-known limitations, expenditure-side GDP data are being used as proxies for components of aggregate demand.

effect. At the same time, government final consumption expenditure (which excludes transfer payments such as subsidies), which accounts for around 11 per cent of GDP, picked up sharply in Q1 of 2012-13, partly reflecting a base effect.

II.3 The decline in the weighted contribution of net exports and valuables in Q1 of 2012-13 is in line with the balance of payments, in contrast to the data for the previous quarter (Table II.2). Significantly, discrepancies continue to vitiate expenditure data. The table shows that the sum of the contribution-weighted growth rates of the different expenditure components works out to only 1.9 per cent in Q1 of 2012-13, which is much lower than the growth rate of 3.9 per cent derived from the production approach GDP ('supply side') after adjusting for net indirect taxes. Since the production-approach GDP is considered as the firmer estimate in the National Accounts Statistics, the difference between the expenditure side GDP derived from the supply side and that obtained from the different components of

expenditure is reported as a statistical discrepancy. The discrepancy largely arises due to the lack of firm data on the expenditure components and the consequent use of indicator based approach by the CSO. Such large discrepancy complicates the assessment of aggregate demand in the economy for monetary policy.

Moderation in sales growth coupled with decline in profits and contraction in margins reflect slack demand

II.4 The subdued demand is reflected in the dampened sales of non-government non-financial (NGNF) listed companies. Sales growth decelerated to a 10-quarter low of 13 per cent in Q1 of 2012-13 (Table II.3). Further, due to a higher rate of growth in expenditure compared to sales, net profits declined by 10.7 per cent. The decline in net profits on a q-o-q basis was even sharper at 18 per cent (Table II.4).

II.5 Lower growth in profits (EBITDA/EBIT/net profits) relative to sales led to a decline in profit margins (EBITDA/EBIT/net profits as

Table II.2: Contribution-Weighted Growth Rates of Expenditure-Side GDP (2004-05 Prices)*

Item	(Per cent)				
	2011-12				2012-13
	Q1	Q2	Q3	Q4	Q1
1	2	3	4	5	6
1. Private Final Consumption Expenditure	3.0	2.8	3.9	3.2	2.4
2. Government Final Consumption Expenditure	0.5	0.8	0.6	0.5	1.0
3. Gross Fixed Capital Formation	4.7	1.7	-0.1	1.1	0.2
4. Change in Stock	0.3	0.1	0.0	0.0	0.0
5. Valuables	0.3	0.2	0.1	0.2	-1.5
6. Net Exports (i-ii)	-1.8	-3.8	-6.4	4.0	-0.2
(i) Exports	3.9	4.4	1.5	4.6	2.4
(ii) Imports	5.7	8.2	7.9	0.6	2.6
7. Sum (1 to 6)	7.0	1.8	-2.0	9.0	1.9
8. Discrepancies	2.0	5.1	8.2	-3.4	2.1
9. GDP at Market Prices (7+8)	9.0	6.9	6.2	5.6	3.9

*: Contribution-weighted growth rate of a component of expenditure side GDP is obtained as follows:
 (Year-on-Year change in the component ÷ Year-on-Year change in GDP at constant market prices) × Year-on-Year growth rate of GDP at constant market prices.

Source: Central Statistics Office.

Table II.3: Corporate Sector- Financial Performance						
Item	2011-12		2011-12			2012-13
		Q1	Q2	Q3	Q4	Q1
1	2	3	4	5	6	7
No. of Companies	2308					
Growth Rates¹ (in Per cent)						
Sales	18.8	22.3	19.3	19.3	15.3	13.0
Expenditure, of which	21.4	22.8	22.7	24.9	16.4	15.3
Raw Material	22.6	28.0	23.1	25.0	16.1	13.0
Staff Cost	17.4	19.0	18.0	18.6	14.4	17.5
Power & fuel	28.2	31.1	26.2	30.4	25.4	17.7
Operating Profits (EBITDA)	1.1	12.6	-0.8	-5.5	-0.8	-4.1
Other Income*	49.3	63.5	25.6	69.9	47.5	29.4
Depreciation	10.6	11.4	9.8	10.3	10.7	9.5
Gross Profits (EBIT)	4.5	18.2	-0.1	-2.2	3.3	-3.0
Interest	40.3	34.1	47.4	43.6	36.7	36.3
Tax Provision	6.3	22.0	4.0	-2.6	2.9	-5.5
Net Profits	-11.9	7.1	-15.3	-30.5	-7.9	-10.7
Select Ratios						
Change in stock # to Sales	1.3	1.4	0.5	2.3	1.0	0.8
Interest Burden	26.7	23.4	28.5	28.5	26.8	32.9
Interest Coverage	3.7	4.3	3.5	3.5	3.7	3.0
EBITDA to Sales	13.4	15.0	12.9	12.6	13.1	12.7
EBIT to Sales	12.1	13.3	11.4	11.2	12.4	11.4
Net Profits to Sales	6.4	7.6	6.1	4.9	6.9	6.0

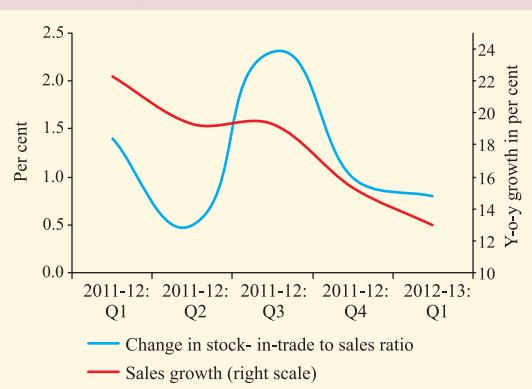
#: For companies reporting this item explicitly.
*: Other income excludes extraordinary income/expenditure if reported explicitly.
1. Growth rates are percentage changes in the level for the period under reference over the corresponding period of the previous year for common set of companies.

percentage of sales). A decline in change in stock-in-trade to sales ratio is in line with lower capacity utilisation as observed from OBICUS

and indicates a possible moderation in expectation on demand conditions, going forward (Chart II.1).

Table II.4: Corporate Sector Financial Performance (Sequential Growth)						
Indicator	Common Companies (Q-o-Q Growth in Per cent)					
	2011-12				2012-13	
	Q1	Q2	Q3	Q4	Q1	
1	2	3	4	5	6	
No. of Companies	2308					
Sales	-2.9	3.4	5.6	8.7	-4.8	
Expenditure, of which	-3.6	4.9	7.7	6.8	-4.5	
Raw Material	-3.3	1.1	8.3	9.7	-5.9	
Staff Cost	2.7	6.7	3.1	1.3	5.4	
Power & fuel	13.5	-3.0	7.9	5.5	6.6	
Operating Profits (EBITDA)	-4.9	-10.8	3.0	13.5	-8.1	
Other Income	-9.6	7.7	4.8	44.5	-20.7	
Depreciation	-1.9	0.6	3.7	8.2	-3.0	
Gross Profits (EBIT)	-6.3	-11.2	3.1	20.5	-12.1	
Interest*	8.4	8.0	3.1	13.3	8.0	
Tax Provision	5.0	-11.3	-4.5	15.6	-3.6	
Net Profits	-15.1	-16.3	-15.1	52.5	-17.7	

*: Some companies report interest on net basis.

Chart II.1: Movement in Sales Growth and Change in Stock in Trade to Sales

Table II.6: Institutionally-Assisted Projects and their Envisaged Cost (Quarter-wise)

Financial Year	No. of Projects	Project Expenditure # (₹ billion)
1	2	3
2011-12	Q1	154 (131) 787 (677)
	Q2	194 572
	Q3	151 506
	Q4	169 (153) 255 (226)
2012-13	Q1*	80 268

#: Based on data reported by 39 banks/FIs.

*: Data for Q1:2012-13 is provisional and is based on reported data from 32 banks/FIs. Corresponding data for Q1:2011-12 and Q4:2011-12 are given in parentheses.

II.6 Early results of 190 companies for Q2 of 2012-13 indicate that the sales growth continued to slowdown for these companies (Table II.5). There was a marked improvement in growth of

Table II.5: Corporate Sector- Early Results Q2 of 2012-13

Item	Growth Rates ¹ (in Per cent)		
	2011-12 Q2	2012-13 Q1 Q2	
1	2	3	4
Number of Companies		190	
Sales	28.9	16.1	13.5
Expenditure, of which	32.6	19.8	15.7
Raw Material	39.6	20.7	15.8
Staff Cost	22.0	23.1	23.0
Power & fuel	21.9	8.1	12.5
Operating Profits (EBITDA)	11.7	2.0	8.4
Other Income*	77.6	37.5	30.7
Depreciation	5.8	-2.6	-3.4
Gross Profits (EBIT)	21.6	8.6	15.4
Interest	57.6	33.0	-5.2
Tax Provision	24.7	6.8	12.0
Net Profits	15.9	7.9	21.6
Select ratios			
Change in stock [#] to Sales	1.2	1.2	2.3
Interest Burden	9.8	10.0	8.1
Interest Coverage	10.2	10.0	12.4
EBITDA to Sales	15.8	14.4	15.0
EBIT to Sales	15.1	14.2	15.4
Net Profits to Sales	10.3	9.8	11.0

#: For companies reporting this item explicitly.

*: Other income excludes extraordinary income/expenditure if reported explicitly.

1. Growth rates are percentage changes in the level for the period under reference over the corresponding period of the previous for common set of companies.

net profits. However, the early results are from a small set of companies which are not representative of the overall corporate sector.

Investment remained subdued in Q1 of 2012-13

II.7 Moderation in the cost of projects sanctioned by major banks/FIs for new corporate investment persisted during Q1 of 2012-13 (Table II.6). While the number of approvals declined sharply, there was a marginal increase in the envisaged cost of projects during the quarter. Industry-wise analysis of investment intentions reveals that the share of the power sector in the total planned investment was the highest (Chart II.2).

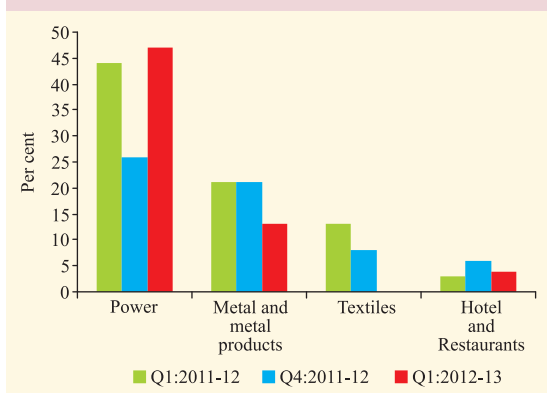
Chart II.2: Share of Industries in Planned Investment


Table II.7: Central Government Finances during April-August 2012

(₹ billion)								
Item	2011-12	2012-13	April-August		Percentage to		Growth Rate	
	(RE)	(BE)	Amount		Budget Estimates		(Per cent)	
	(Amount)		2011-12	2012-13	2011-12	2012-13	2011-12	2012-13
1	2	3	4	5	6	7	8	9
1. Revenue Receipts (i+ii)	7669.9	9356.9	1885.5	2227.3	23.9	23.8	-35.2	18.1
i) Tax Revenue (Net)	6422.5	7710.7	1449.0	1750.6	21.8	22.7	4.6	20.8
ii) Non-Tax Revenue	1247.4	1646.1	436.6	476.7	34.8	29.0	-71.3	9.2
2. Non-Debt Capital Receipts	297.5	416.5	101.4	50.8	18.4	12.2	85.1	-49.9
3. Non-Plan Expenditure	8921.2	9699.0	3402.2	4174.0	41.7	43.0	9.3	22.7
<i>of which</i>								
i) Interest Payments	2756.2	3197.6	1002.4	1137.7	37.4	35.6	17.1	13.5
ii) Food Subsidies	728.2	750.0	282.2	451.0	46.6	60.1	-11.7	59.8
iii) Fertiliser Subsidies	672.0	609.7	263.1	377.1	52.6	61.8	20.0	43.3
iv) Petroleum Subsidies	684.8	435.8	10.3	396.1	4.4	90.9	20.5	-
4. Plan Expenditure	4266.0	5210.3	1320.0	1479.5	29.9	28.4	-3.3	12.1
5. Revenue Expenditure	11619.4	12861.1	4185.5	5001.7	38.1	38.9	7.0	19.5
6. Capital Expenditure	1567.8	2048.2	536.7	651.9	33.4	31.8	-5.1	21.5
7. Total Expenditure	13187.2	14909.3	4722.2	5653.5	37.5	37.9	5.5	19.7
8. Revenue Deficit	3949.5	3504.2	2300.0	2774.4	74.9	79.2	129.2	20.6
9. Gross Fiscal Deficit	5219.8	5135.9	2735.2	3375.4	66.3	65.7	80.6	23.4
10. Gross Primary Deficit	2463.6	1938.3	1732.8	2237.7	119.6	115.4	163.3	29.1

Source : Controller General of Accounts, Ministry of Finance.

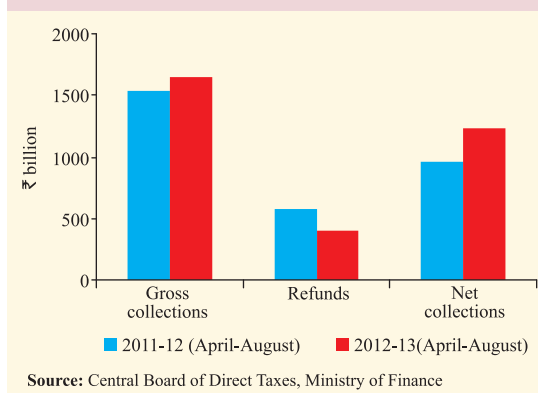
Fiscal slippage likely in 2012-13, in spite of recent measures

II.8 The deficit indicators of the central government widened during 2012-13 (April-August) compared with the corresponding period of the previous year (Table II.7). There is a deviation from the projected fiscal consolidation path as the fiscal deficit during the first five months of 2012-13 comprised nearly two-thirds of the budget estimate for the year as a whole. On the current reckoning, the centre's gross fiscal deficit (GFD/GDP) ratio in 2012-13 is unlikely to see a significant improvement from that in the previous year. This underscores the need for taking further steps soon, in addition to the measures taken since mid-September 2012.

II.9 On the revenue side, the net collections under direct taxes improved during April-August 2012, with a growth rate higher than budgeted for the year, mainly reflecting lower

refunds than a year ago (Chart II.3). The growth in indirect tax collections, however, has moderated during the period. Deceleration in industrial growth and foreign trade has affected collections under union excise duties and customs duties, respectively. Service tax revenue increased sharply over the period due to an increase in the service tax rates as well as the widening of the services tax base since

Chart II.3: Direct Tax Collections of Central Government



July 2012. For the year as a whole, the gross tax-GDP ratio, is likely to be much lower than the budget estimates, reflecting the impact of slowdown in economic growth on tax collections.

II.10 Overall, there could be some shortfall in centre's revenue receipts. With regard to non-debt capital receipts, the government recently approved partial disinvestment of its equity holding in four public sector enterprises. Given the recent buoyancy witnessed in the stock markets, it may be possible to meet the budgetary target for disinvestment proceeds.

II.11 Total expenditure growth during 2012-13 (April-August) was higher than in the corresponding period of 2011-12 and the budgeted growth for 2012-13. The expenditure on subsidies was more than two-thirds of the budget estimates. For the year as a whole, a significant slippage in all three major subsidies – food, fertilisers and petroleum – is likely, resulting in higher than budgeted non-plan expenditure. Consequently, a cut-back in plan expenditure is envisaged to restrict the fiscal slippage.

II.12 The recent measures such as upward revision in diesel prices, restriction on subsidised LPG and levy of service tax on railway freight and passenger fares are steps in the right direction but further corrective measures are required to contain the fiscal deficit within sustainable limit. In this regard, the Committee on Roadmap for Fiscal Consolidation (Chairman: Dr. Vijay Kelkar) has made recommendations for policy interventions. The report set out the targets as well as the steps for course correction that need to be adhered to. In accordance with the stipulations of the amended Fiscal Responsibility and Budget Management Act, 2003, the government has placed before the Parliament in September 2012, the Medium Term Expenditure Framework Statement which sets out a three-year rolling target for the

expenditure indicators, specifying the underlying assumptions and risks involved.

Subsidies remain high and likely to overshoot budget estimates

II.13 Notwithstanding the recent price revisions and quantitative restrictions in administered petroleum products, the required compensation for under-recoveries of OMCs is estimated to be higher than budget estimates. Though the government had budgeted for an absolute decline in the amount of fertiliser subsidy in 2012-13, these have already crossed the budget estimate for the year as a whole. The food subsidy in 2012-13, as per official sources, is estimated to be ₹924.9 billion, an increase of around 24 per cent over the budget estimates.

II.14 Rationalisation and reprioritisation of government expenditure is imperative for fiscal consolidation. Strategically, overall expenditure on subsidies needs to be restricted, and complemented with better targeting and distribution in accordance with policy priorities. Direct cash transfer of subsidies in food, fertilisers and petroleum will help towards subsidy reduction.

Financial restructuring of state distribution companies may have medium to long-term implications for state finances

II.15 The consolidated key deficit indicators of states are budgeted to improve in 2012-13 over 2011-12 (RE), reflecting the intent to carry forward fiscal consolidation in line with the recommendations of the Thirteenth Finance Commission (Table II.8). The consolidated revenue surplus for states is budgeted to increase in 2012-13, primarily through an increase in revenue receipts. The improvement in the revenue account is expected to reduce the fiscal deficit and primary deficit by 0.2 percentage points of GDP each and would also provide resources for higher capital outlay. The

Table II.8: Key deficit Indicators				
(As per cent of GDP)				
Year	Primary Deficit	Revenue Deficit	Gross Fiscal deficit	Outstanding Liabilities
1	2	3	4	5
Centre				
2010-11	1.8	3.3	4.9	52.8
2011-12 RE	2.8 (2.7)	4.5 (4.3)	5.9 (5.8)	51.9
2012-13 BE	1.9	3.4	5.1	-
States				
2010-11	0.5	-0.1	2.1	23.4
2011-12 RE	0.8	-0.1	2.3	22.5
2012-13 BE	0.6	-0.4	2.1	21.8
Combined				
2010-11	2.4	3.2	6.9	66.0
2011-12 RE	3.6	4.4	8.2	65.6
2012-13 BE	2.6	3.0	7.1	-

RE: Revised Estimates. BE: Budget Estimates.
Note: 1. Minus (-) sign indicates surplus.
 2. Outstanding liabilities of centre and combined includes external liabilities of the centre calculated at current exchange rates.
 3. Figures in parentheses are provisional accounts.
Source: Budget documents of the Central and State governments.

revenue expenditure-GDP ratio is expected to decline by 0.1 percentage point in 2012-13. This will, however, be on account of lower growth in the development component, both social and economic services.

II.16 The recently announced scheme for financial restructuring of state distribution companies (discoms) proposes a strategy for their financial turnaround. As per the announced scheme, 50 per cent of the outstanding short-

term liabilities of the discoms to lending institutions would be converted into bonds issued by the former, backed by state government guarantees. These bonds are to be taken over within 2-5 years and converted into special securities by the state governments. The restructuring/ rescheduling will be subject to state governments and discoms taking certain prior steps to improve the operational performance of the discoms. The financial restructuring plan will hence not have any immediate implications for state finances as there is a moratorium on repayment of the principal for three to five years and even the interest payment would be due only in the next fiscal. This will, however, have a medium- to long-term impact on the state finances.

Fiscal consolidation and boost to investment is key to growth revival

II.17 High fiscal deficit has impacted the macroeconomic climate and contributed to the investment downturn. A credible fiscal consolidation strategy is now on the anvil but needs to be backed by further measures. Overall demand conditions during 2012-13 have stayed depressed, due mainly to slack in investment. With a number of initiatives to address structural impediments and augment FDI, the investment climate should start improving. As the structural constraints facing investment get removed, there could be some revival in investment demand going forward.