II. AGGREGATE DEMAND*

Aggregate demand, as reflected on the expenditure side of GDP, remained sluggish during Q4 of 2012-13. Apart from investment, private consumption decelerated, adding to the drag on demand during 2012-13. Depressed private consumption, to a large part, has been the result of high consumer price inflation. Corporate investment intentions also remained languid, reflecting the overall negative business sentiment arising from slack cyclical conditions and structural factors. Corporate sales decelerated during Q4 of 2012-13, while earnings contracted. This, in turn, may have an adverse impact on new investment. In this situation, the key to turning around the economy will be re-balancing government spending from current to capital expenditures with a view to 'crowding-in' private investment.

Aggregate demand continued to remain weak

II.1 The expenditure-side GDP indicates that the aggregate demand of the Indian economy during Q4 of 2012-13 remained slack (Table II.1). Private final consumption expenditure, which is the principal component of GDP at market prices, continued to decelerate during the quarter on the back of weak agricultural production and persistent high consumer price inflation. Even so, it remains the largest contributor to growth in aggregate demand (Table II.2). The growth rate of government final consumption expenditure also moderated during Q4, reflecting fiscal consolidation efforts. Even though the growth rate of fixed investment

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

(Per cent)

Item	2011-12@	2012-13#	2011-12				2012-13			
			Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
1	2	3	4	5	6	7	8	9	10	11
Growth Rates										
GDP at market prices	6.3	3.2	8.3	6.4	5.8	5.2	3.4	2.5	4.1	3.0
Total Consumption Expenditure	8.1	3.9	6.9	7.0	9.0	9.3	4.7	4.0	3.8	3.3
(i) Private	8.0	4.0	6.6	6.3	9.2	9.7	4.3	3.5	4.2	3.8
(ii) Government	8.6	3.9	8.4	10.7	8.1	7.6	7.2	6.9	2.2	0.6
Gross Fixed Capital Formation	4.4	1.7	13.9	3.8	-1.7	2.6	-2.2	1.1	4.5	3.4
Change in Stocks	-30.6	73.4	-27.5	-30.4	-32.0	-32.4	69.8	71.7	75.8	76.0
Valuables	6.6	-12.0	16.1	-13.3	8.4	16.0	-20.9	4.3	-6.9	-20.2
Net Exports	-42.5	-17.3	-14.8	-17.7	-82.1	-83.3	-6.7	-21.4	-23.7	-16.4
Relative shares										
Total Consumption Expenditure	70.5	71.0	71.2	71.8	73.7	65.7	72.1	72.8	73.5	65.9
(i) Private	59.2	59.6	60.6	61.2	61.4	54.3	61.1	61.8	61.4	54.7
(ii) Government	11.3	11.3	10.6	10.5	12.3	11.5	11.0	11.0	12.1	11.2
Gross Fixed Capital Formation	33.7	33.2	35.7	35.1	31.8	32.5	33.8	34.6	32.0	32.6
Change in Stocks	2.3	3.8	2.4	2.4	2.2	2.2	3.9	4.0	3.7	3.8
Valuables	2.4	2.0	2.8	2.1	2.2	2.3	2.1	2.2	2.0	1.8
Net Exports	-8.8	-10.0	-9.3	-9.3	-9.5	-7.4	-9.6	-11.0	-11.3	-8.4
Memo:										
GDP at market prices (₹ billion)	56314	58137	13252	13207	14473	15382	13702	13536	15062	15836

@: First Revised Estimates. #: Provisional Estimates.
Source: Central Statistics Office.

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

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

(Per cent)

Item	2011-12				2012-13			
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
1	2	3	4	5	6	7	8	9
1. Private Final Consumption Expenditure	4.1	3.9	5.4	5.0	2.6	2.2	2.6	2.1
2. Government Final Consumption Expenditure	0.9	1.1	1.0	0.9	0.8	0.7	0.3	0.1
3. Gross Fixed Capital Formation	4.7	1.4	-0.6	0.9	-0.8	0.4	1.4	1.1
4. Change in Stocks	-1.0	-1.1	-1.1	-1.1	1.7	1.7	1.7	1.7
5. Valuables	0.4	-0.3	0.2	0.3	-0.6	0.1	-0.2	-0.5
6. Net Exports	-1.3	-1.5	-4.6	-3.6	-0.6	-2.0	-2.3	-1.2
(i) Exports	4.3	4.3	2.4	3.1	3.0	1.2	-0.9	-0.2
(ii) Imports	5.6	5.8	6.9	6.6	3.6	3.2	1.4	1.1
7. Sum (1 to 6)	7.8	3.4	0.4	2.4	3.0	3.1	3.5	3.2
8. Discrepancies	0.5	3.0	5.4	2.7	0.4	-0.6	0.6	-0.3
9. GDP at Market Prices	8.3	6.4	5.8	5.2	3.4	2.5	4.1	3.0

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

Source: Central Statistics Office.

during Q4 of 2012-13 was slightly higher than in the corresponding quarter of the previous year, aggregate fixed investment in the full year decelerated further.

Initiatives have started addressing infrastructure bottlenecks, although progress is slow

II.2 Infrastructure bottlenecks have been a major factor in India's low growth. Project implementations are getting delayed due to delays in land acquisition, forest/environment clearances, insurgency problems in mining belts, geological surprises, contractual issues, etc. As on May 1, 2013, nearly half of 566 central sector projects (of ₹1.5 billion and above) got delayed due to these problems, for which cost overruns are estimated to be around 18.2 per cent.

II.3 To address these issues, the government has taken several initiatives. For speedy clearance of projects, in addition to the Cabinet Committee on Infrastructure (CCI), a Project Monitoring Group (PMG) has been set up by the Prime Minister's Office (PMO) with the objective of resolving hurdles facing mega projects (above ₹10 billion).

II.4 In the power sector, the government has initiated several measures, such as renovation and modernisation of old power plants, improvement of coal and gas supplies, and greater emphasis on power generation from renewable sources. The government has also set up a committee (under the chairmanship of Dr. Vijay Kelkar) to prepare a road map to enhance domestic production of oil & gas.

II.5 With regard to road projects, the response to the PPP mode of road building remained poor. Several projects have not elicited bids. The developers have been facing a severe shortage of equity and, consequently, are unable to raise the required debt. The government has decided to adopt the Engineering, Procurement and Construction (EPC) mode for national highways which are not viable on a PPP basis. However, the Cabinet Committee on Economic Affair's (CCEA) decisions in June 2013 to facilitate harmonious substitution of concessionaire in ongoing and completed National Highway projects and insulating the National Highway Authority of India (NHAI) from heavy financial claims and unnecessary disputes are likely to expedite the implementation of road projects.

II.6 With the cancellation of 2G licences in February 2012, the telecommunications sector has been struggling, with a noticeable decline in investor interest. However, investor interest is expected to improve once the recent decision by the Telecom Commission approving 100 per cent FDI in the sector gets ratified.

Corporate investment intentions remain subdued

II.7 Corporate investment intentions remain subdued. Additionally, some of the institutionally assisted projects which received sanction in 2010-11 and 2011-12 have been cancelled. The aggregate project cost envisaged from new projects for which assistance was sanctioned by major banks/FIs, aggregated ₹2.0 trillion in 2012-13 and remained almost at the same level as that of the previous year (₹1.9 trillion) but significantly below that in 2010-11 (₹3.8 trillion) (Table II.3). An industry-wise analysis revealed that during Q4 of 2012-13, the share of envisaged expenditure on new projects is the highest in the metal & metal products sector (56.0 per cent), followed by the power industry (30.0 per cent) (Chart II.1).

Sales growth remained sluggish during Q4 of 2012-13

II.8 Sales growth for listed Non-Government Non-Financial (NGNF) companies decelerated further in Q4 of 2012-13 to 4.1 per cent (Table II.4). The decline in sales was more distinct in the case of motor vehicles, electricity

Table II.3: Institutionally Assisted Projects and their Envisaged Cost (Quarter-wise)*

Financial Year		No. of Projects	Project Expenditure (₹ billion)
1		2	3
2010-11	Q1	178	1,139
	Q2	196	1,043
	Q3	157	752
	Q4	166	818
2011-12	Q1	147	749
	Q2	184	452
	Q3	137	462
	Q4	168	253
2012-13	Q1	110	413
	Q2	132	666
	Q3	89	256
	Q4	94	629

Note: Based on data reported by 39 banks/FIs.
*: Data are provisional. Past data has been revised due to subsequent reporting, including the cancellation of projects.

Chart II.1: Share of Envisaged Investment in Major Industries in Aggregate cost of Projects (per cent)

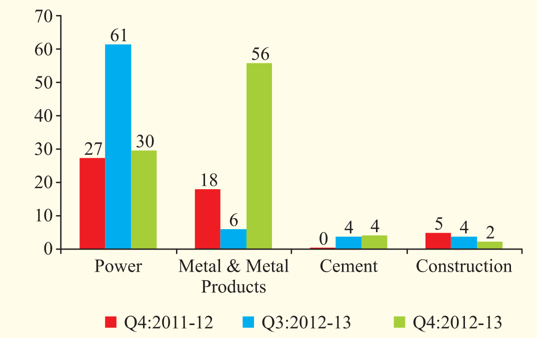


Table II.4: Performance of Non-Government Non-Financial Companies

(Per cent)

	Q4 of 2011-12	Q1 of 2012-13	Q2 of 2012-13	Q3 of 2012-13	Q4 of 2012-13
1	2	3	4	5	6
No. of Companies			**2,419**		
			Growth Rates (y-o-y)		
Sales	15.6	14.0	11.7	9.4	4.1
Value of Production	14.1	13.4	12.4	8.1	4.0
Expenditure, *of which*	16.7	16.4	12.6	8.2	4.7
Raw Materials	16.7	13.6	14.6	9.3	2.6
Staff Cost	14.3	17.7	15.3	13.1	13.5
Power & Fuel	30.6	26.2	20.9	11.0	3.5
Operating Profits (EBITDA)	-0.7	-3.4	11.3	7.9	-0.2
Other Income*	49.4	28.4	49.2	0.3	-1.4
Depreciation	10.7	10.4	10.1	10.3	8.4
Gross Profits (EBIT)	4.0	-2.5	18.9	5.6	-2.7
Interest	40.2	38.4	11.3	17.1	11.1
Tax Provision	1.2	-3.4	11.0	5.1	-2.7
Net Profits (without NOP)	-6.7	-18.5	26.2	-0.7	-9.2
Net Profits	-6.4	-9.7	23.1	24.3	-15.5
			Select Ratios		
Change in stock to Sales #	0.9	0.8	1.4	0.8	0.9
Interest Burden	26.6	32.5	27.2	33.1	30.5
EBITDA to Sales	13.3	12.9	13.2	12.6	12.7
EBIT to Sales	12.6	11.6	12.8	11.3	11.8
Net Profit to Sales	7.1	6.1	7.1	5.8	5.7

#: For companies reporting this item explicitly.
*: Other income excludes extraordinary income/expenditure if reported explicitly.

Table II.5: Performance of Non-Government Non-Financial Companies (Sequential Growth)

(Q-o-Q, per cent)

Indicator	Number of Companies: 2,419				
	2011-12	2012-13			
	Q4	Q1	Q2	Q3	Q4
1	2	3	4	5	6
Sales	9.5	-4.5	0.7	3.8	4.4
Value of Production	8.4	-4.6	1.2	3.2	4.4
Expenditure, *of which*	7.7	-4.2	0.9	3.9	4.4
Raw Materials	10.0	-6.1	1.9	3.8	3.0
Staff Cost	2.1	6.0	3.4	1.3	2.4
Power & fuel	3.4	9.7	-3.2	0.1	-2.4
Operating Profits (EBITDA)	13.7	-7.3	3.4	-0.9	4.9
Other Income**	30.3	-22.6	41.1	-27.9	23.2
Depreciation	6.2	-1.7	1.8	3.7	3.1
Gross Profits (EBIT)	19.2	-12.1	11.0	-8.7	9.0
Interest*	7.6	7.3	-7.1	10.9	0.7
Tax Provision	15.3	-0.9	3.4	-11.0	6.5
Net Profits	52.0	-17.8	17.0	-15.0	3.1

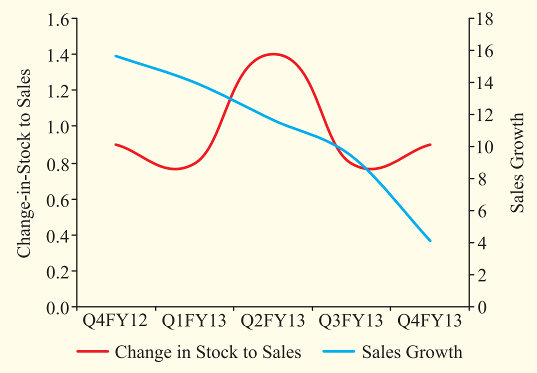
*: Some companies report interest on net basis.
**: Other income excludes extraordinary income/expenditure, if reported explicitly.

generation and supply, iron & steel and real estate. In tandem with the slow growth in sales, net profits went down in Q4 of 2012-13 due to higher employee expenses and lower support from other income. Sequentially (q-o-q), however, net profit recorded an improvement in Q4 (Table II.5). Further, profitability in terms of EBITDA and EBIT margins improved marginally in Q4 in comparison with the previous quarter. The net profit margin, however, recorded a marginal decline. Inventory accumulation (as reflected in change in stock-in-trade to sales ratio), which went up in Q2 of 2012-13, has reverted to earlier levels (Chart II.2). Early results for Q1 of 2013-14 suggest that sales growth has decelerated further.

Corporate leverage has increased gradually

II.9 The leverage of the corporate sector at the aggregate level, as measured by the total borrowing to equity ratio, increased in 2011-12, reversing a gradual and declining trend

Chart II.2: Movement in Sales Growth and Stock-in-Trade to Sales (per cent)



in the previous two years (Table II.6). Based on the available annual results of 621 non-government non-financial public limited companies, leverage is observed to have increased further in 2012-13.

Table II.6: Total borrowing to Equity: 2009-10 to 2011-12

	2009-10	2010-11	2011-12
1	2	3	4
Manufacturing	72.0	68.1	71.7
Of which			
Food products and beverages	112.8	116.4	114.7
Textiles	187.2	191.9	208.2
Coke and refined petroleum	46.2	44.8	46.4
Chemicals and chemical products	61.7	60.4	69.4
Cement and cement products	73.4	45.0	52.5
Iron and steel	112.6	106.7	115.3
Electrical equipment	50.5	48.4	38.9
Machinery	36.5	39.8	53.1
Motor vehicles and accessories	66.5	53.3	52.4
Electricity, gas, steam and air conditioning supply	61.6	70.6	114.6
Construction	89.0	95.5	80.8
Services	62.3	65.7	68.6
Of which			
Transportation and storage	121.3	241.5	338.9
Telecommunications	61.8	87.7	78.9
Computers and related activities	20.8	18.6	19.8
Real estate	70.1	76.1	62.0
All companies	**69.7**	**69.0**	**72.3**
Size by sales			
Large	66.6	65.2	71.5
Medium	79.9	82.4	85.2

Note: Large companies – annual sales above ₹10 billion; Medium companies – annual sales between ₹1 billion and ₹10 billion.

Fiscal consolidation resumed during 2012-13 mainly through expenditure cutbacks

II.10 The central government restricted its gross fiscal deficit (GFD) to 4.9 per cent of GDP during 2012-13, less than the budget estimate of 5.1 per cent (Table II.7). The containment in GFD, despite lower tax and non-tax revenues, was achieved mainly through a cutback in plan expenditure. Non-plan expenditure, on the other hand, was higher due to a sharp increase in expenditure on the revenue account. Subsidies on food, fertilisers and petroleum accounted for 2.5 per cent of GDP as against the 1.8 per cent that had been budgeted for the year. Overall, the revenue expenditure as a proportion of GDP was lower than the budget estimate by 0.3 percentage points, although it could not offset the shortfall in revenue receipts, which resulted in a higher revenue deficit.

Table II.7: Key Fiscal Indicators

(Per cent to GDP)

Year	Primary Deficit	Revenue Deficit	Gross Fiscal Deficit	Outstanding Liabilities @
1	2	3	4	5
		Centre		
2011-12	2.7	4.4	5.7	51.9
2012-13 PA	1.8 (1.9)	3.6 (3.4)	4.9 (5.1)	51.9#
2013-14 BE	1.5	3.3	4.8	51.1
		States*		
2011-12	0.4	-0.1	1.9	22.3
2012-13 RE	0.8	-0.2	2.3	22.0
2013-14 BE	0.6	-0.4	2.1	21.6
		Combined*		
2011-12	3.3	4.3	7.7	65.5
2012-13 RE	2.9	3.7	7.5	65.8
2013-14 BE	2.2	2.9	6.9	66.1

@: Includes external debt at current exchange rates.
#: Pertains to revised estimates.
*: Data in respect of states pertains to 26 state governments, of which one is Vote on Account.
PA: Provisional Accounts. BE: Budget Estimates.
RE: Revised Estimates.
Note: 1. Figures in parentheses are budget estimates.
2. Combined liabilities of 2013-14 are adjusted for states' investment in Treasury Bills as on July 19, 2013.
Source: Budget documents of central and state governments.

Tax collection remains weak during 2013-14 so far

II.11 During April-May 2013, key deficits of the Centre as percentages to budget estimates were higher than in the corresponding period of last year. The widening of the revenue deficit and higher capital expenditure resulted in a higher gross fiscal deficit during April-May 2013 than a year ago.

II.12 The revenue deficit as a percentage to budget estimate during April-May 2013 was higher due to both higher revenue expenditure and lower tax revenues. Gross tax revenue in absolute terms declined mainly due to a decline in revenues from corporation tax and union excise duties. The collection of income tax and service tax as percentages to budget estimates were also lower than a year ago.

II.13 Total expenditure, as a percentage of the budget estimate in the first two months (April-May) of 2013-14, was higher than a year ago, mainly due to higher plan and capital expenditure, which registered growth rates of 52.6 per cent and 48.9 per cent, respectively, over April-May 2012. On the other hand, despite higher payments of subsidies, non-plan expenditure in the revenue account, was lower than in the corresponding period of the previous year.

II.14 If the government's revenues fall short of the target due to slowdown in growth, a cutback in expenditure will be required to achieve the budgeted fiscal deficit. It is, therefore, important to contain subsidies and re-prioritise expenditure towards plan and capital expenditures, thereby enhancing the growth prospects of the economy.

State finances expected to remain on the consolidation track

II.15 Despite an increase in the consolidated GFD-GDP ratio in 2012-13 (RE), over the previous year, the GFD-GDP ratio was within the target set by the Thirteenth Finance Commission. The revenue account at the consolidated level recorded a surplus in 2012-13 (RE), *albeit* lower than budgeted.

II.16 The consolidated position of the state governments for 2013-14[1] is budgeted to show an increase in the revenue surplus-GDP ratio and a marginal improvement in the GFD-GDP ratio. The surplus in revenue account would be achieved by a reduction in the revenue expenditure-GDP ratio, while the revenue receipts-GDP ratio is budgeted to remain unchanged from the previous year's level. The expenditure pattern of the states shows that while the development expenditure-GDP ratio is budgeted to decline, the non-development expenditure-GDP ratio is budgeted to increase marginally during 2013-14. However, the capital outlay-GDP ratio is budgeted to be higher in 2013-14 than in 2012-13 (RE).

Table II.8: Combined Finances of Central and State Governments*

Item	Per cent to GDP		
	2011-12	2012-13 RE	2013-14 BE
1	2	3	4
1. Total Expenditure	26.4	27.9	27.9
2. Revenue Expenditure	22.5	23.8	23.4
3. Capital Expenditure	3.9	4.2	4.5
Of which: Capital Outlay	3.4	3.7	4.2
4. Non-development Expenditure	10.8	11.0	11.3
5. Development Expenditure	15.3	16.6	16.1
6. Revenue Receipts	18.3	20.0	20.4
i) Tax Revenue (net)	16.0	16.9	17.5
ii) Non-tax Revenue	2.2	3.1	3.0

*: Data in respect of states pertains to 26 state governments.
RE: Revised Estimates. BE: Budget Estimates.
Source: Budget documents of central and state governments.

Combined government finances budgeted to improve in 2013-14

II.17 Data on combined finances show that the revenue deficit and fiscal deficit as ratios to GDP in 2012-13 (RE) were lower by 0.6 percentage points and 0.2 percentage points, respectively, over the previous year. The decline in the combined GFD-GDP ratio was entirely on account of the lower fiscal deficit of the Centre (Table II.7). In 2013-14, the combined fiscal position is budgeted to improve further on account of fiscal plans of both the Centre and the states (Table II.8).

Need to keep the momentum of the fiscal consolidation and increase government investment in productive sectors

II.18 The government's fiscal consolidation process has contributed to improving the state of public finances in India at a critical juncture. The low collection of both tax and non-tax revenue during 2012-13 complicated the task of reducing fiscal imbalances. Thus, the containment of GFD in 2012-13 was brought about by expenditure compression on plan revenue account and also plan and non-plan capital account. The cuts in union government's capital expenditure were undertaken at a time when private investment had already decelerated. This raised concerns about the quality of fiscal consolidation. It is, therefore, important for the Centre to take steps to contain its non-plan revenue expenditure within the limit set in the Union Budget 2013-14 through subsidy reforms. Staying on the path of fiscal consolidation in the current year, however, remains challenging. Moderation in aggregate demand poses risks to budgetary projections for revenue. The recent exchange rate depreciation has compounded the problems in restraining subsidies. At the present juncture, it is important that the government restrains its subsidy commitments, strikes a judicious balance under its various budgetary heads by increasing investment in the productive sectors so as to crowd-in private investments. Tax reforms also need to be expedited to improve the tax/GDP ratio.

[1] Based on budget documents of 26 state government for 2013-14 of which one is Vote on Account.