

## VII. MACROECONOMIC OUTLOOK

*Various forward looking surveys conducted in the recent period suggest an overall improvement in business sentiments as also the possibility of further acceleration of growth in 2010-11. The Professional Forecasters' Survey of the Reserve Bank also shows upward revision in the median growth projections for 2010-11. With stronger growth outlook, high generalised inflation has emerged as the key macroeconomic concern. The anti-inflationary monetary policy measures taken so far by the Reserve Bank, coupled with an improved supply position that may result from better performance of kharif relative to last year, could be expected to help in arresting inflation by firmly anchoring inflationary expectations in the coming months.*

VII.1 The Indian economy witnessed robust recovery in growth in the last quarter of 2009-10. Most of the business expectations surveys suggest continuation of the growth momentum in 2010-11. The Industrial Outlook Survey of the Reserve Bank indicates further improvement in several parameters of the business environment for the July-September 2010 quarter. The Professional Forecasters' Survey conducted by the Reserve Bank in June 2010 places overall (median) GDP growth rate for 2010-11 at 8.4 per cent, higher than 8.2 per cent reported in the previous round of the survey.

### Business Expectations Surveys

VII.2 The forward looking surveys conducted by various agencies generally

convey an optimistic picture about the economy. In continuation of the trend observed in recent rounds of surveys, the latest round of most of the surveys also shows strong y-o-y as well as q-o-q improvement. (Table VII.1).

VII.3 NCAER-MasterCard Worldwide Index of Business Confidence points to continuation of high level of optimism notwithstanding a marginal decline in the index. The optimism is led by sustained recovery in the industrial activity and improvement in merchandise export during April-May 2010, which contributed to the expectation that the overall GDP growth in the first quarter of 2010-11 may exceed 8.5 per cent. At the same time, there are concerns that persistence of double digit inflation may affect consumption and

**Table VII.1: Business Expectations Surveys**

Period/Index	NCAER-MasterCard Worldwide Index of Business Confidence June 2010	FICCI Q4:2009-10 Overall Business Confidence Index	Dun & Bradstreet Q3: 2010 Business Optimism Index	CII Apr.-September 2010-11 Business Confidence Index
1	2	3	4	5
Current level of the Index	155.9	74.8	150.0	67.6
Index as per previous survey	156.8	70.0	142.8	66.1
Index levels one year back	118.6	64.1	132.1	58.7
% change (q-o-q) sequential	-0.6	6.9	5.0	2.3
% change (y-o-y)	31.5	16.7	13.6	15.2

investment demand and also lead to policy response that could increase the cost of credit and funds.

VII.4 The latest round of Business Confidence Survey of the FICCI suggests that 87 per cent of the companies view the overall economic conditions as “moderately to substantially better”. Going ahead, around 82 per cent of the companies foresee an improvement in overall economic conditions in the coming six months. The outlook for jobs has been somewhat subdued, with about two-thirds of the participants anticipating no change in employment levels in the coming six months, even though about 30 per cent firms expect an increase in their employee strength in the coming six months.

VII.5 The Dun and Bradstreet Business Optimism Survey recorded sustained improvement, which at a two year high, is reflective of the continuous strengthening of confidence amongst corporates. Robust growth in industrial production, stabilising domestic consumption demand, rapidly growing investment demand coupled with increase in imports and exports seem to have supported the growing business confidence. Five out of the six optimism indices, *viz.*, volume of sales, net profits, new orders, inventory levels and employee levels have registered an increase as compared to the previous quarter. However, selling prices recorded a decline as compared to the previous quarter. Demand conditions are expected to witness significant improvement in the medium to long-term and employment scenario is expected to improve in the July-September 2010 quarter.

VII.6 The CII Business Confidence Survey for April-September 2010-11

suggested growing confidence of respondents about expansion of exports over the next six months. Headline inflation touching double digits emerged as a major concern, while the respondents felt that procedural delays need to be addressed urgently.

VII.7 The seasonally adjusted HSBC Markit Manufacturing Purchasing Managers’ Index (PMI), which had recorded a twenty-seven month high in May 2010, witnessed a marginal fall in June 2010, mainly reflecting slower growth in output and new orders, even though the pace of new export orders accelerated. On the downside, the employment levels remained stagnant. Notwithstanding the recent fall, the index has remained in the above neutral territory (*i.e.*, above 50) in each of the past fifteen months.

VII.8 The HSBC Markit Services PMI accelerated sharply to reach a two year high in June 2010, indicating optimism and continuation of higher levels of activity in the services sector. India is one of the few countries that showed an improvement in the services PMI in June 2010. The employment scenario also improved and the output prices continued to rise at accelerated pace, thus suggesting continuation of pricing pressures. The growth in services sector offset the weakness in manufacturing sector and, as a result, the composite output index registered the sharpest rise in almost two years.

#### **Reserve Bank’s Industrial Outlook Survey**

VII.9 The 50<sup>th</sup> round of the Industrial Outlook Survey of the Reserve Bank conducted during April-June 2010, based

on a sample of 1,092 companies, suggested a moderate slowdown in the index, both for the assessment quarter (April-June 2010) as well as expectations for the July-September 2010 quarter. However, both indices (*i.e.*, assessment about the current quarter and expectations about the next quarter) remained in the growth terrain (*i.e.*, above 100, which is the threshold that separates contraction from expansion) (Chart VII.1a). Most of the parameters of

the survey indicate buoyancy in business environment (Table VII.2). The findings of the survey are in line with the forward looking manufacturing PMI survey (Chart VII.1b).

### Survey of Professional Forecasters

VII.10 The results of the twelfth round of “Survey of Professional Forecasters” conducted by the Reserve Bank in June 2010 shows overall (median) GDP growth rate

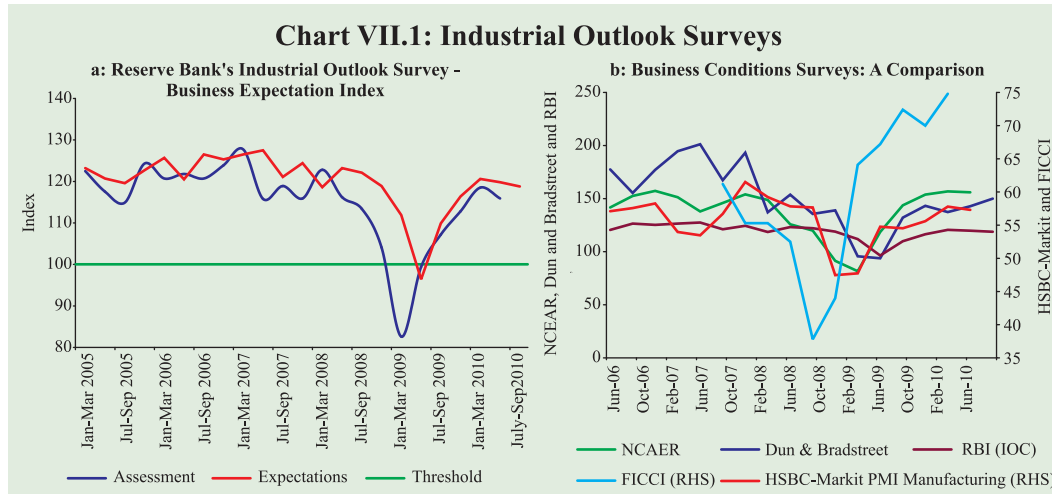
**Table VII.2: Reserve Bank's Survey -Net Response on Expectations and Assessment about the Industrial Performance**

Parameter	Optimistic Response	Jul-Sept 2009		Oct-Dec 2009		Jan-Mar 2010		Apr-Jun 2010		July-Sep 2010
		E	A	E	A	E	A	E	A	E
1	2	3	4	5	6	7	8	9	10	11
1 Overall business situation	Better	24.2	26.3	39.8	36.0	44.9	43.1	41.2	40.7	41.5
2 Financial situation	Better	20.0	21.8	33.5	29.5	39.3	35.8	36.3	32.2	34.1
3 Working capital finance requirement	Increase	26.3	23.8	30.4	28.8	32.7	30.5	27.7	29.9	31.1
4 Availability of Finance	Improve	16.6	19.2	26.1	23.0	29.2	25.7	26.8	26.4	28.5
5 Cost of external finance	Decrease				-14.7	-18.3	-15.9	-20.6	-21.9	-23.3
6 Production	Increase	22.4	22.6	35.0	28.9	40.0	36.5	35.9	35.4	40.2
7 Order books	Increase	16.8	20.5	32.3	25.9	35.8	31.9	33.4	31.3	36.3
8 Pending orders, if applicable	Below normal	19.1	17.4	11.0	11.6	5.7	8.8	6.4	6.9	4.2
9 Cost of raw material	Decrease	-27.1	-41.7	-38.4	-47.1	-44.3	-60.2	-48.6	-62.7	-49.3
10 Inventory of raw material	Below average	-0.5	-2.1	-1.2	-4.2	-3.6	-5.8	-2.6	-5.0	-5.1
11 Inventory of finished goods	Below average	-1.8	-4.3	-3.7	-4.3	-1.9	-4.3	-2.6	-4.1	-5.0
12 Capacity utilisation (main product)	Increase	10.7	10.1	22.0	16.5	25.4	21.7	19.7	21.1	26.5
13 Level of capacity utilisation (compared to the average in the preceding four quarters)	Above normal	-12.1	-11.2	-3.8	-3.9	1.3	3.0	1.6	2.5	5.8
14 Assessment of the production capacity (with regard to expected demand in the next six months)	More than adequate	5.5	5.8	6.5	5.3	5.0	6.4	7.1	3.1	4.1
15 Employment in the company	Increase	1.5	4.1	8.8	10.3	12.1	13.7	13.6	14.7	16.8
16 Exports, if applicable	Increase	0.1	-2.9	12.5	9.2	20.2	12.7	18.5	15.3	20.7
17 Imports, if any	Increase	4.6	7.8	11.5	13.0	16.9	17.1	17.1	20.9	21.7
18 Selling prices are expected to	Increase	0.0	0.2	6.0	2.6	9.8	12.4	13.3	17.3	15.2
19 Increase in selling prices, if any, is expected	Increase at lower rate	-100.0	23.2	19.4	19.3	16.8	21.6	19.7	17.4	14.3
20 Profit margin	Increase	-13.4	-15.1	-2.8	-9.9	1.1	-2.9	3.2	-4.8	3.1

**Note:** 1. ‘Net response’ is measured as the percentage share differential between the companies reporting ‘optimistic’ (positive) and ‘pessimistic’ (negative) responses; responses indicating *status quo* (no change) are not reckoned. Higher ‘net response’ indicates higher level of confidence and *vice versa*.

2. E: Expectations and A: Assessment.

3. ‘Cost of external finance’ is a newly added question from the 48<sup>th</sup> (October – December 2009) survey round.



for 2010-11 at 8.4 per cent, as against 8.2 per cent reported in the previous survey (Table VII.3). The sectoral growth rate

forecast for the agriculture sector was revised marginally upwards from 4.0 per cent to 4.1 per cent. For the services sector also

**Table VII.3: Median Forecasts of Select Macroeconomic Indicators by Professional Forecasters 2010-11**

	Actual 2009-10	Annual Forecasts				Quarterly Forecasts									
		2010-11		2011-12		2010-11								2011-12	
		E	L	E	L	Q1		Q2		Q3		Q4		Q1	
1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	16
1. Real GDP growth rate at factor cost (in per cent)	7.4 R	8.2	8.4	-	8.5	8.1	8.7	8.3	8.2	8.4	8.5	8.5	8.4	-	8.3
a. Agriculture and Allied Activities	0.2 R	4.0	4.1	-	3.0	2.9	2.7	3.8	4.0	5.7	6.0	4.3	3.9	-	3.0
b. Industry	10.4 R	9.0	9.0	-	9.1	10.6	11.6	9.3	9.3	9.0	8.7	8.5	8.4	-	8.7
c. Services	8.3 R	9.0	9.1	-	9.5	8.9	9.1	8.8	8.9	9.7	9.3	9.9	9.2	-	9.5
2. Gross Domestic Saving (per cent of GDP at current market price)	-	35.3	34.7	-	35.9	-	-	-	-	-	-	-	-	-	-
3. Gross Domestic Capital Formation (per cent of GDP at current market price)	-	38.0	36.0	-	37.8	37.0	36.8	38.0	36.8	38.7	36.3	38.8	36.1	-	37.3
4. Corporate profit after tax (growth rate in per cent)*	28.8	20.0	22.5	-	21.0	18.5	20.0	18.8	18.0	18.4	18.9	26.1	25.0	-	25.0
5. Inflation WPI	3.8	7.0	8.6	-	6.0	9.5	10.4	8.0	9.5	6.7	8.1	5.7	7.0	-	6.4
6. Exchange Rate (INR/US\$ end period)	45.1	44.0	44.5	-	43.5	45.0	46.3	44.8	45.5	44.6	44.8	44.1	44.5	-	43.8
7. T-Bill 91 days Yield (per cent-end period)	4.4	5.3	5.2	-	5.0	-	-	-	-	-	-	-	-	-	-
8. 10-year Govt. Securities Yield (per cent-end period)	7.2	8.0	7.8	-	7.5	-	-	-	-	-	-	-	-	-	-
9. Export (growth rate in per cent)!	-4.7 P	15.0	15.0	-	16.0	-	-	-	-	-	-	-	-	-	-
10. Import (growth rate in per cent)!	-8.2 P	18.0	17.9	-	15.0	-	-	-	-	-	-	-	-	-	-
11. Trade Balance (US\$ billion)	-102.1 P	-	-	-	-	-32.7	-32.8	-34.6	-34.5	-35.5	-36.5	-32.1	-33.0	-	-35.9

E: Previous Round Projection. L: Latest Round Projection. R: Revised Estimate. P: Preliminary Estimate.  
 -: Not Available. \*: BSE listed companies. !: US\$ on BoP basis.  
**Note:** The latest round refers to twelfth round for the quarter ended June 2010, while previous round refers to eleventh round for the quarter ended March 2010.  
**Source:** Survey of Professional Forecasters, First Quarter 2010-11.

**Table VII.4: Agencies' Forecast for 2010-11**

Agency	Latest Projection		Earlier Projection	
	Real GDP Growth (Per cent)	Month	Real GDP Growth (Per cent)	Month
1	2	3	4	5
Economic Advisory Council to the PM	8.5	July-10	8.2	Feb-10
Ministry of Finance	8.5 (+/-0.25)	Feb-10	..	..
IMF (calendar year)	9.4	July-10	8.8	April-10
ADB	8.2	July-10	8.2	April-10
NCAER	8.1	April-10	..	..
OECD	8.3	May-10	7.3	Nov-09
.. : Not available.				

the assessment was revised marginally upwards from 9.0 per cent to 9.1 per cent. For industry, the forecast remained unchanged at 9.0 per cent.

#### **Growth Projections of Different Agencies**

VII.11 All available projections of real GDP growth for 2010-11 are higher than 8 per cent. The IMF's projected growth figure for India may seem to be on the higher side but it is not so as it is at constant market prices. (Table VII.4 and Box VII.1).

#### **Factors Influencing the Current Growth and Inflation Outlook**

VII.12 The economic recovery witnessed in 2009-10 after the slowdown in 2008-09 was mainly driven by a turnaround in the industrial output, with continued resilience of the services sector. The leading indicators point to the prospect of robust growth in the coming quarters and fast closing of the output gap. An uncertain external environment, however, is a major risk to growth in the near term.

#### **Box VII.1: GDP Growth at Factor Cost and Market Prices**

The growth projections generated by different agencies, both in India and outside reflect the divergence in their assessments. The difference in growth estimates across agencies provides a broader perspective to the market, though at times they may not be exactly comparable. While most of the projected growth numbers, including those released by the Reserve Bank are at factor cost, the IMF's recent projection for India's growth in 2010 is at market prices and also relates to the calendar year. GDP growth at market prices may differ significantly from GDP growth at factor cost depending on the trend in "indirect

taxes net of subsidies". For example, GDP growth at factor cost in 2008-09 at 6.7 per cent was higher than GDP growth at market prices (5.1 per cent). In contrast, GDP growth at factor cost in 2009-10 was lower at 7.4 per cent as compared with 7.7 per cent at market prices. During the fourth quarter of 2009-10, the difference was particularly high with GDP at market prices growing at 11.2 per cent as against the growth of 8.6 per cent at factor cost. The IMF's 9.4 per cent projected growth for the calendar year 2010 factors in the turnaround in taxes in January-March 2010.

VII.13 The growth outlook for the Indian economy for 2010-11 remains positive on account of the following factors: (a) prospect of better *kharif* output than last year, (b) buoyancy in the industrial sector, notwithstanding the moderation in May 2010, (c) stronger growth in corporate sales with higher profitability, (d) improving business environment as per optimism expressed in different surveys, (e) strong growth in exports, notwithstanding weakness in global conditions, (f) indications of pick-up in private consumption demand, as evident from trends in production of consumer durables and non-durables as also auto sales, (g) significant pick-up in investment demand, (h) stronger growth in lead indicators of services sector like tourist arrivals, commercial vehicles production and railway freight traffic, (i) a potentially lower fiscal deficit due to the favourable outcome of the 3G/ BWA spectrum auctions, which could create greater space for private sector investment, and (j) significant acceleration in credit demand from the private sector.

VII.14 Notwithstanding the upside prospects, certain downside risks remain: (a) as the export growth hinges on external demand conditions, given the asymmetry in growth outlook for advanced economies and EMEs, sustaining high export growth would be challenging, (b) real appreciation of the exchange rate could also weaken external price competitiveness of Indian exports, (c) even though investment demand accelerated sharply in Q4 of 2009-10, it needs to be sustained to return to the pre-global crisis trajectory, (d) while private consumption demand has shown signs of revival, sustenance of the trend is

crucial, given the gradual phasing out of the fiscal stimulus and the monetary exit, and (e) the inflationary pressures, besides affecting the cost structure through demands for higher wages and increase in input costs, could also depress demand.

VII.15 Headline inflation, which reached 10.6 per cent in June 2010, has been in double digits for last five months and is also increasingly getting generalised. Even though recent upward revisions in administered prices have added to inflation, demand side pressures are also building up. Going forward, factors which may exert further upward pressure on inflation are: (a) return of pricing power in step with the pick-up in private demand and faster closing of capacity utilisation gap may add further pressure on investment demand, (b) recent measures to align domestic fuel prices with the international prices; while the first round impact of the rise in fuel prices is presently becoming evident, the indirect impact would be felt with a lag, (c) possible wage pressures, and (d) recent increase in minimum support prices.

VII.16 Given these risks, the factors that may help in restraining the inflationary pressures include: (a) better *kharif* production, thereby easing the supply side constraints in agricultural production, (b) indications of stable global commodity prices, especially that of oil and food, and (c) the impact of monetary policy actions already initiated by the Reserve Bank to contain inflation and anchor inflationary expectations.

VII.17 An overall assessment suggests that the GDP growth will be higher than 8 per cent projected in the April 2010 Monetary

Policy Statement, as the upside bias has materialised. The major policy concern, therefore, would be to contain the inflationary pressures and anchor inflationary expectations. The acceleration in growth seen so far needs to become self-sustaining, with durable pick-up in both private consumption and investment demand. Moreover, uncertainties in the

external environment cannot be overlooked. Hence, the calibrated approach to normalisation of monetary policy continues to be appropriate. Given the risk to inclusive growth from high inflation, the monetary unwinding that started in October 2009 should continue till inflation expectations are firmly anchored and inflation is brought down.