II. Aggregate Demand

Drivers of growth from the expenditure side in the first quarter of 2010-11 suggest continued predominance of both private consumption and investment expenditures. Recent trends in capital goods production, capital expenditure plans of corporates, non-oil imports, growth in credit and financing from non-banking sources point to strengthening of drivers of investment expenditure. Expenditure side GDP data as well as trends in corporate sales and production of consumer durables indicate pick-up in private consumption expenditure. Despite the policy emphasis on fiscal consolidation and the observed improvement in revenue deficit, Government's expenditures have shown stronger growth than last year. The turnaround in agricultural production during kharif 2010-11 is expected to stimulate private expenditure.

Domestic Demand

II.1 India's growth drivers continue to be domestic. This has helped not only in limiting the impact of global recession on domestic growth but also in ensuring a fast and durable recovery. The key factors driving growth and their sustainability over the medium-term could be seen from the expenditure side of GDP. Real GDP at market prices grew by 10 per cent in the first quarter of 2010-11, higher than 8.8 per cent growth recorded in respect of real GDP at factor cost. The higher growth in real GDP at market prices is a reflection of higher net indirect taxes.

II.2 At a disaggregated level, the growth of private final consumption expenditure

(PFCE) picked up moderately during the first quarter of 2010-11. With turnaround in agriculture production during the *kharif* season 2010-11, it is expected that rural demand and private consumption expenditure could gather momentum, going forward. The Government final consumption expenditure (GFCE) after remaining subdued for two quarters, accelerated sharply during the first quarter of 2010-11. The acceleration in GFCE during the first quarter of 2010-11 is in tandem with the growth in revenue expenditure of the Central Government (Chart II.1 and Table II.1).

II.3 Investment growth in the form of gross fixed capital formation (GFCF), which had picked up in the third quarter of 2009-10 and then accelerated sharply in the last quarter, witnessed moderation during the first quarter of 2010-11. Reflecting this, the share of gross fixed capital formation in GDP declined, with an offsetting increase in the share of private consumption expenditure. Private consumption expenditure and gross fixed capital formation, nevertheless, were the major drivers of growth in real GDP at market prices (Chart II.2).

II.4 The slack in gross fixed capital formation during the first quarter of 2010-11, however, appears to be somewhat contrary to the buoyant trends witnessed in respect of capital goods segment in the IIP.

Demand Management through Fiscal Policy

Central Government Finances

II.5 Reflecting the impact of economic recovery, partial rollback of fiscal stimulus measures and receipts from 3G spectrum and broadband wireless access (BWA) auctions, the position of Central Government finances improved significantly with revenue deficit (RD) and gross fiscal deficit (GFD) during April-August 2010-11 turning out to be substantially lower, both in absolute terms and as a proportion of budget estimates,

Chart II.1: Growth in Major Components of Expenditure Side GDP

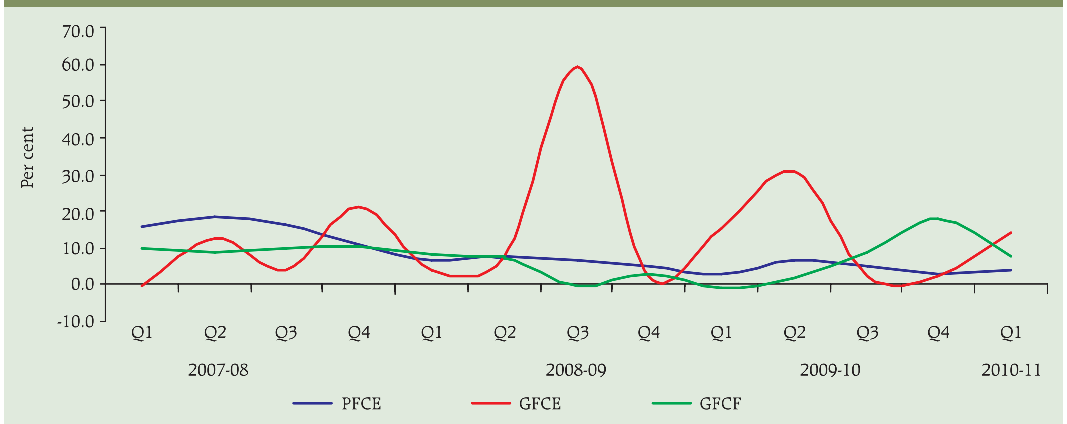


Table II.1: Expenditure Side GDP (2004-05 Prices)

(Per cent)

Item	2008-09*	2009-10#	2009-10 Q1	2009-10 Q2	2009-10 Q3	2009-10 Q4	2010-11 Q1
1	2	3	4	5	6	7	8
	Growth Rates						
Real GDP at market prices	5.1	7.7	5.2	6.4	7.3	11.2	10.0
Total Consumption Expenditure	8.3	5.3	4.7	9.6	4.8	2.6	5.5
(i) Private	6.8	4.3	2.9	6.4	5.3	2.6	3.8
(ii) Government	16.7	10.5	15.3	30.5	2.5	2.1	14.2
Gross Fixed Capital Formation	4.0	7.2	-0.7	1.6	8.8	17.7	7.6
Change in Stocks	-61.2	5.9	-0.9	4.2	8.7	11.1	7.0
Net Exports	40.2	-9.7	-27.4	6.1	-0.3	-113.4	20.5
	Relative shares						
Total Consumption Expenditure	70.9	69.4	71.4	71.5	73.4	62.3	68.4
(i) Private	59.5	57.6	59.9	60.1	60.4	51.1	56.5
(ii) Government	11.5	11.8	11.5	11.3	13.1	11.2	11.9
Gross Fixed Capital Formation	32.9	32.8	31.2	33.2	31.9	34.6	30.5
Change in Stocks	1.3	1.3	1.3	1.4	1.3	1.3	1.3
Net Exports	-6.1	-5.1	-4.8	-8.7	-6.7	0.4	-5.2
Memo:							(₹ crore)
Real GDP at market prices	4,465,360	4,807,222	1,099,653	1,125,257	1,242,858	1,339,454	1,209,888

* : Quick Estimates. # : Revised Estimates.

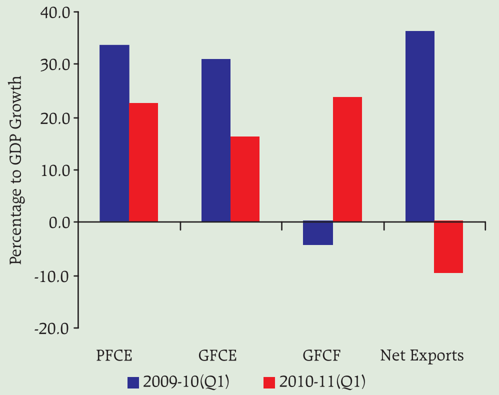
Note: As only major items are included in the table, data will not add up to 100.

Source: Central Statistics Office.

over the corresponding period of the previous year (Chart II.3 and Table II.2).

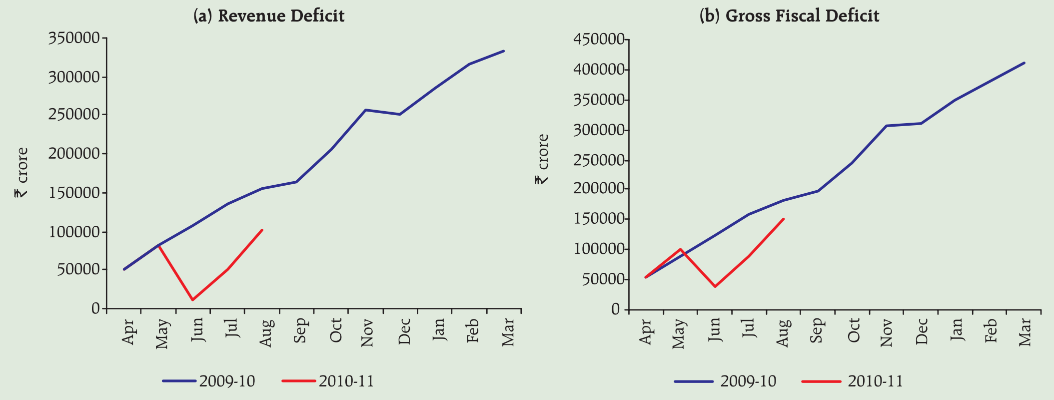
II.6 Improvement in finances of the Central Government during 2010-11 so far (April-August) was evident from substantial increase in revenue receipts (85.0 per cent), supported by tax and non-tax revenues. The gross tax revenue increased significantly (27.3 per cent) in contrast to the sharp decline (11.6 per cent) recorded during 2009-10 (April-August), mirroring the underlying economic recovery and the partial rollback of indirect tax cuts.

Chart II.2: Weighted Contribution to GDP Growth from Expenditure Side



II.7 Direct tax collections showed significant improvement during April-August 2010-11, recording a growth of 13.8 per cent over April-August 2009-10. While corporate tax collections grew by 18.4 per cent, collections under personal income tax increased by 14.0 per cent. In addition, the mobilisation of revenues from 3G/BWA spectrum auctions in June 2010 helped to ease the pressure on Government finances.

Chart II.3: Key Deficit Indicators



II.8 During April-August 2010-11, growth in revenue as well as capital expenditure was higher than in the corresponding period of 2009-10. The escalation in aggregate expenditure emanated from accelerated growth (39.2 per cent) in plan expenditure. During 2010-11 so far (April-August), Centre has already incurred 40.4 per cent of aggregate expenditure budgeted for 2010-11 (Chart II.4).

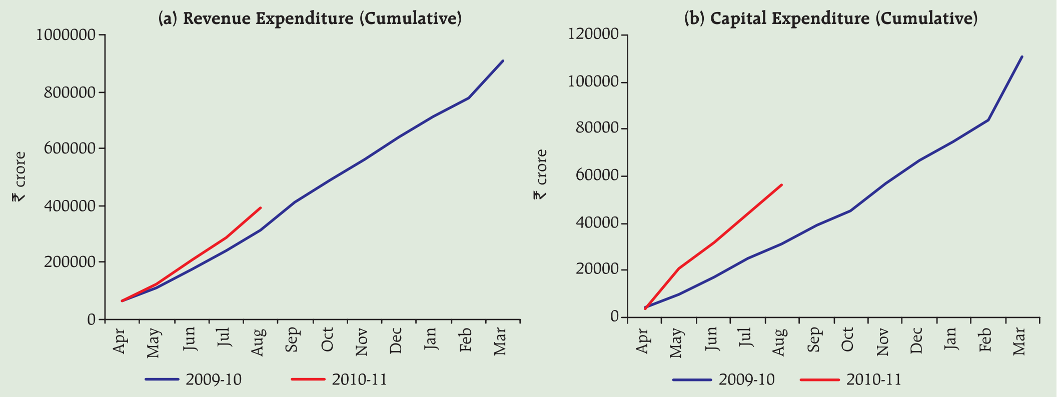
II.9 The fiscal stimulus measures initiated by the Government achieved the objective of containing the duration and extent of economic slowdown in India. Taking cognisance of the improved growth

Table II.2 : Central Government Finances: April-August 2010-11

Item	April-August (₹ crore)		Percentage to Budget Estimates for		Growth Rate (Per cent)	
	2009	2010	2009-10	2010-11	2009-10	2010-11
1	2	3	4	5	6	7
1. Revenue receipts	1,57,198	2,90,799	25.6	42.6	-2.7	85.0
i) Tax revenue (Net)	1,06,837	1,38,500	22.5	25.9	-14.8	29.6
ii) Non-tax revenue	50,361	1,52,299	35.9	102.8	39.6	202.4
2. Non-debt capital receipts	3,835	5,479	71.7	12.1	218.8	42.9
3. Non-plan expenditure	2,45,275	3,11,249	35.3	42.3	27.1	26.9
of which:						
i) Interest payments	72,133	85,621	32.0	34.4	9.6	18.7
ii) Defence	41,129	45,395	29.0	30.8	65.8	10.4
iii) Major subsidies	54,193	54,738	51.1	50.2	4.7	1.0
4. Plan expenditure	98,048	1,36,454	30.2	36.6	13.2	39.2
5. Revenue expenditure	3,12,283	3,91,151	34.8	40.8	20.4	25.3
6. Capital expenditure	31,040	56,552	25.1	37.7	53.6	82.2
7. Total expenditure	3,43,323	4,47,703	33.6	40.4	22.8	30.4
8. Revenue deficit	1,55,085	1,00,352	54.9	36.3	58.4	-35.3
9. Gross fiscal deficit	1,82,290	1,51,425	45.5	39.7	56.0	-16.9
10. Gross primary deficit	1,10,157	65,804	62.8	49.6	115.8	-40.3

Source: Controller General of Accounts, Ministry of Finance.

Chart II.4: Trends in Central Government Expenditure



prospects and the need for fiscal consolidation for sustaining the growth momentum, Central government has embarked on gradual fiscal exit plan as announced in the Budget 2010-11. The robust growth in revenue receipts in 2010-11 is premised on partial rollback of indirect tax rate reduction and revenue from 3G/BWA spectrum auctions. Given the one-off nature of auction proceeds, the priority of consolidation should continue in terms of quantity and quality. In order to achieve a sustainable progress on fiscal consolidation path, it would be desirable to adopt measures designed to augment revenue collection on a sustainable basis and rationalisation of recurring expenditure, with a focus, particularly on curtailing non-plan revenue expenditure.

State Finances

II.10 State Governments undertook various measures in terms of additional spending and tax cuts in 2009-10 with a view to boost domestic economic activities. As a result, revenue deficit re-emerged in 2009-10, after a gap of three years. Recognising the need for fiscal discipline, States have embarked upon the process of fiscal consolidation in 2010-11. Revenue expenditure, as a ratio to GDP, is budgeted to be lower at 13.4 per cent in 2010-11 (BE) as against 13.6 per cent in 2009-10 (RE). States expect to witness higher revenue buoyancy in 2010-11 (BE) on account of higher own tax revenue and share in Central taxes. Accordingly, revenue deficit and gross fiscal deficit of State governments are budgeted to be lower in 2010-11.

Combined Fiscal Position

II.11 An overview of the combined finances of the Central and State Governments budgeted for 2010-11 indicates that the key deficit indicators as per cent of GDP would moderate compared to the elevated levels in 2009-10 (Table II.3). The envisaged fiscal consolidation is to be driven by significant increase in revenue receipts, while curtailing the growth of expenditure. Total expenditure in terms of both growth and as a percentage of GDP

Table II.3: Key Fiscal Indicators

(Per cent to GDP)

Year	Primary Deficit	Revenue Deficit	Gross Fiscal Deficit	Outstanding Liabilities*
1	2	3	4	5
Centre				
2008-09	2.6	4.5	6.0	56.7
2009-10 RE	3.2	5.3	6.7	56.4
2010-11 BE	1.9	4.0	5.5	56.9
States #				
2008-09	0.6	-0.2	2.4	26.2
2009-10 RE	1.6	0.8	3.4	26.2
2010-11 BE	1.0	0.4	2.9	26.1
Combined				
2008-09	3.4	4.3	8.5	72.0
2009-10 RE	4.8	6.0	10.0	72.5
2010-11 BE	3.0	4.4	8.3	73.6

RE : Revised Estimates. BE : Budget Estimates.
* : Includes external liabilities at historical exchange rates.
# : Data pertain to 27 State Governments.
Note: Negative sign indicates surplus.

would moderate somewhat from the previous year. Growth in tax collections is expected to improve on account of reversal of tax cuts and the acceleration in economic growth.

Corporate Performance

II.12 The turnaround in overall economic activity was reflected in the corporate sector performance. Sales of private corporate business sector witnessed significant improvement, recording a growth of 24.2 per cent (y-o-y) during the first quarter of 2010-11 (Table II.4). The high growth in sales partly reflects the low base effect, as the economic activity in the first quarter of the previous year had remained subdued with an almost flat sales and moderate profit

Table II.4: Corporate Sector Financial Performance

(Growth rates/ratios in per cent)

Item	2008-09				2009-10				2010-11
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1
1	2	3	4	5	6	7	8	9	10
No. of companies	2500	2386	2486	2561	2530	2531	2562	2565	2546
Sales	29.3	31.8	9.5	1.9	-0.9	0.1	22.5	29.1	24.2
Other income*	-8.4	-0.6	-4.8	39.4	50.2	6.0	7.4	10.3	-21.2
Expenditure	33.5	37.5	12.6	-0.5	-4.4	-2.5	20.6	30.7	29.0
Depreciation provision	15.3	16.5	16.8	19.6	21.5	20.7	21.6	20.1	19.9
Gross profits	11.9	8.7	-26.7	-8.8	5.8	10.9	60.0	36.7	8.2
Interest payments	58.1	85.3	62.9	36.5	3.7	-1.0	-12.3	-2.9	26.9
Profits after tax	6.9	-2.6	-53.4	-19.9	5.5	12.0	99.3	44.0	2.4
Select Ratios									
Change in stock-in-trade to sales #	2.9	2.2	-1.7	-1.8	0.6	2.3	0.8	1.1	2.9
Gross profits to sales	14.5	13.5	11.0	13.7	15.7	14.9	14.3	14.6	13.9
Profits after tax to sales	9.7	8.6	5.3	8.1	10.2	9.4	8.8	9.0	8.6
Interest to sales	2.4	2.9	3.8	3.2	2.8	3.1	2.7	2.4	2.9
Interest to gross profits	16.8	21.5	34.6	23.3	18.0	20.5	19.1	16.6	21.1
Interest coverage (times)	6.0	4.6	2.9	4.3	5.6	4.9	5.2	6.0	4.7

* : Other income excludes extraordinary income/expenditure, if reported explicitly.
# : For companies reporting change in stock-in-trade explicitly.
Note: 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.
2. The quarterly data may not add up to annual data due to differences in the number and composition of companies covered, in each period.

growth. Sequentially, sales growth during the first quarter of 2010-11 witnessed moderation over the fourth quarter of 2009-10, though seasonally adjusted sales increased by 1.9 per cent over the fourth quarter of 2009-10.

II.13 Change in stock-in-trade, which remains generally around the peak in the first quarter of each financial year, formed 2.9 per cent of sales during the first quarter of 2010-11 (Chart II.5). A rise in change in stock-in-trade to sales ratio suggests that corporates are building up their inventories in anticipation of higher demand. Accumulation of stocks increased to 3.3 per cent of sales excluding sugar industry during the quarter. Given the strong growth in sales, increase in change in stock to sales ratio suggests significant addition to stocks during the quarter, which could have been a factor to support the robust overall GDP and industrial growth in that quarter.

II.14 Strong investment intentions were evident as reflected in higher envisaged capital expenditure of companies, which approached banks/FIs for financial assistance during April-June 2010. In the first quarter of 2010-11, 87 projects were sanctioned assistance by banks/FIs of ₹99,998 crore as against 35 projects of ₹30,116 crore sanctioned during corresponding period of the previous year.

External Demand

II.15 Unlike in the fourth quarter of 2009-10, when net exports had contributed positively to real GDP growth on the expenditure side, the contribution of net exports during the first quarter of 2010-11 became negative, as growth in imports remained ahead of growth in exports. (see Chart II.2). While the growth in exports was impacted by the weak and uncertain global economic environment, that of imports reflected the increasing momentum of domestic economic activity.

II.16 To sum up, private consumption expenditure has picked up, but needs to gain further momentum to support a self-sustaining robust growth in GDP. Notwithstanding the process of fiscal consolidation that is underway,

Chart II.5: Movement in Sales Growth & Change in Stock-in-Trade to Sales Ratio

Government spending continues to support growth, reflecting higher growth in both revenue and capital expenditures. Available data relating to production of capital goods, notwithstanding volatility, and capital expenditure plans of the corporates point to a strong momentum in investment expenditure during the current fiscal year. Reflecting the high growth in India relative to hesitant recovery in the advanced economies, the contribution of net exports to aggregate demand could be expected to remain negative during the year. Overall, although aggregate demand trends point to continuation of the momentum, investment demand needs to emerge as the key driver for sustainable robust growth.