GDP growth expected to moderate from 8.6% in 2010-11 to 8% in 2011-12

Inflationary Concerns to Continue Up to September This Year; Supply Side Rigidities Need to Be Addressed: Says FICCI Economic Outlook Survey

Economists cite governance, regulatory issues, global slowdown, expected domestic slowdown, emergence of other competent economies for recent dip in FDI inflows

NEW DELHI, May 30, 2011. FICCI's Economic Outlook Survey forecasts that the rate of inflation may further accelerate over the first half of the fiscal year (April-September 2011) because of the expected increase in diesel, LPG and kerosene prices and supply side constraints faced by commodities such as vegetables, fruits, pulses, milk and eggs.

The sixth round of the Survey was conducted during May 2, 2011 to May 26, 2011. Twelve leading economists from the banking and financial sector and those from industry and research institutions gave their forecast on key macro economic variables for the year 2010-11 and 2011-12 as well as for Quarter 1 (April-June) 2011-12.

The surveyed economists project the annual GDP rate to be at 8.6 per cent for 2010-11, with the fourth quarter (Q4) rate dipping to 8.2 per cent. For 2011-12, GDP growth is expected to decelerate to 8 per cent.

A majority of the economists felt that the RBI should stop its current anti- inflationary rate hikes when the inflation moderates to around 7 per cent to 7.5 per cent. They expect that the RBI will further increase the repo rate by another 50-75 basis points in this rate hike cycle.

The economists estimate that though the inflationary pressures are expected to persist in the near term, it is likely to moderate to the around 7 per cent by the end of fiscal year 2011-12 because of four reasons: One, the expected stability in the international crude oil price as the overreaction in oil prices to the problems in the Middle – East is calming down; two, the likely downward movement in the international commodity prices; three, the measures expected to be taken by the government to ease supply side bottlenecks; and four, the possible lagged impact of the successive policy rate hikes coming in to play and impinging on demand side pressure of the inflation.

Some of the economists strongly suggest that RBI should target only non-food inflation and not the food inflation. They recommended that a pure monetary approach to manage the inflation arising of supply side rigidities is a wrong approach and it is the duty of the government to make the effort to bring down the food inflation.

On the question of considering a 'new normal' range of 6 to 7 per cent for inflation, the Survey elicited a mixed reaction. While a majority of the economists agreed that Indian economy has to accept a new normal and agreed to a 6 per cent level as the new normal, a few economists said it could be even a 7 per cent mark considering the changing trend of inflation as well as the structural demand – supply mismatches.

A few economists opposed the consideration of a new normal level for WPI inflation because, setting a higher normal level will only prevent a push for structural reforms that are urgently needed to reduce the general level of inflation and also will exacerbate inflationary expectations.

They further suggested that government may continue to bring down the current inflation by debottlenecking the agriculture sector by taking urgent steps to increase productivity and improving supply side management of food products. Also, to tame the inflation in the manufactured products, steps must be taken to augment supplies of industrial inputs via greater investments in these sectors

Asked about the recent dip in Foreign Direct Investment (FDI) inflow and outlook for FDI inflows in 2011-12, the economists advanced the following reasons for the downtrend:

- Governance issues: Respondents feel that the factors that might have affected investors sentiments in the recent past could be the environment and land sensitive policies and spate of corruption scandals

- Regulatory uncertainties: Foreign investors planning to enter the retail space as well as banking in India or increasing their stake in insurance ventures have been awaiting the required policy changes for over a decade. This have vitiated the investment climate in the country

- General slowdown in the international market: Re- emergence of sovereign debt related issues in the Euro zone, weak recovery of the US economy and problems in Japan led to uncertainties in the global market

- Expected slowdown in the domestic market: India's macroeconomic stability coupled with the large potential of market was a big lead in attracting the FDI flows. However, RBI has echoed that growth may have to slowdown in order to tame the high inflation. This could have prompted the investors to wait and watch how the domestic situation spans out

- Emergence of other competent economies: India received a good FDI inflow during 2009-10, soon after the global melt down, as the country was seen as the brightest destination amongst the emerging markets. However, as the world economy recovers, funds are moving to other competent emerging economies as well, posing a reduction in FDI flow to India.

Against this back drop most of the surveyed economist expect that the FDI inflow to India during the fiscal year 2011-12 will remain subdued. However, economists are optimistic that fuller recovery in the mature economies, together with Indian Government's action on easing barriers and improving the ease of doing business could increase FDI inflows in the future.

Annual Forecasts of GDP at Factor Cost for 2010-11

- GDP growth – 8.6 per cent
- Agriculture and allied activities growth – 5.4 per cent
- Industry growth – 8.1 per cent
- Services growth – 9.6 per cent

Annual Forecasts for 2011-12

- GDP growth – 8.0 per cent
- Agriculture and allied activities growth – 3.7 per cent
- Industry growth – 8.0 per cent
- Services growth – 9.2 per cent
- Fiscal Deficit – 5 per cent of GDP
- Prime Lending Rate- 5.0 per cent
- WPI Inflation rate (end march 2011) –6.7 per cent
- IIP – 7.9 per cent
- Trade Balance – (-) 7.7 per cent
- Current Account Deficit – (-) 2.8 per cent of GDP
- USD/ INR exchange rate (end March 2012) – Rs. 43.7 /USD

Quarterly Forecasts for Q4 of 2010-11 and Q1 of 2011-12

- GDP growth – 8.2 per cent (Q4, 2010-11), 8.1 per cent (Q1, 2011-12)
- Agriculture and allied activities growth – 5.8 per cent (Q4, 2010-11), 4.0 per cent (Q1, 2011-12)
- Industry growth – 5.3 per cent (Q4, 2010-11), 6.5 per cent (Q1, 2011-12)
- Services growth –10.1 per cent (Q4, 2010-11), 9.3 per cent (Q1, 2011-12)

- Prime Lending Rate – 9.3 per cent (Q1, 2011-12)
- WPI inflation rate – 9.1 per cent (Q1, 2011-12)
- IIP – 6.8 per cent (Q1, 2011-12)
- Trade Balance- (-) 8.6 per cent (Q1, 2011-12)
- USD / INR exchange rate – Rs. 45 / USD (Q1, 2011-12)

Note: Detailed Survey

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