'FICCI's Economic Outlook Survey'

The slowdown in the economy due to demonetisation and the adjustment impact of GST implementation seems to be bottoming out

Government must take steps to strengthen consumption demand and continue with its focus on productive capital spending

High interest rates must be reviewed by RBI as these impact growth and Rupee value say Economists

GDP growth to improve to 6.2% in Q2, 2017-18; Fiscal Deficit to be at 3.3% in 2017-18

New Delhi, 27 November 2017: According to the results of FICCI's latest Economic Outlook Survey, GDP growth is expected to improve to 6.2% in Q2 of 2017-18 and further to 6.7% in Q3 of 2017-18. The slowdown in the economy due to demonetisation and the adjustment impact of GST implementation seems to be bottoming out and as the new indirect tax regime stabilizes, the economy would see an improvement in its performance. This view was expressed by the economists who participated in the latest economic outlook survey conducted by FICCI.

The steps taken by the government to reduce the compliance burden related to GST and make its implementation smoother, the comprehensive plan announced for recapitalisation of the banks and the thrust laid on the infrastructure sector have been acknowledged by the survey participants as an indication of government's clear resolve to address the key issues that are hobbling growth.

Even as these steps are taken by the government, the economists emphasised that reviving consumption particularly in the rural and semi-urban areas will be important to give a boost to overall demand in the economy. With the supply chains being impacted more in these areas compared to the urban areas, greater attention here was called for. In this context it was emphasised that projects such as 'housing for all' and 'electricity for all' should be expedited as these would improve employment prospects in the rural areas and thereby help improve demand. Strengthening of the agri-supply chains and diversification in the rural areas in terms of the economic activities pursued were also mentioned as steps to improve performance of the economy.

The participating economists also mentioned that government should continue with its emphasis on productive capital investments in the social and physical infrastructure space, even if this requires some calibration of the fiscal deficit target. The projected fiscal deficit number for the current year is likely to be slightly higher at 3.3% according to the economists polled by FICCI.

Additionally, there is a need to address the issues related to factors of production particularly land and labour. It was mentioned that unused surplus land along railway lines and stations,

major transport corridors and housing schemes can be utilized for undertaking commercial activities.

The participating economists also commended the role of the Reserve Bank of India in addressing the issue of stressed assets. It was however suggested that recapitalisation plan must be accompanied by reforms in the banking sector and support extended to banks should be linked to their performance.

As for the inflation outlook, the survey results show that WPI based inflation for the year 2017-18 is likely to be around 2.8% and CPI based inflation would be a bit higher at 3.4%. Given this outlook and the fact that supply side issues are largely responsible for the inflation movement in case of India, some of the economists mentioned that inflation targeting by the central bank may not be the correct approach. While asking for a review of the inflation targeting stance of the central bank and calibration of the policy rate giving equal importance to growth and inflation considerations, the participating economists also highlighted how a higher rate of interest leads to greater capital flows thereby putting pressure on the country's currency exchange rate. An overvalued exchange rate hurts exports and on this account too there is a case for the RBI to look at moderating rates.

Furthermore, it was suggested that RBI can undertake a reassessment of various loan rates and other ratios based on their historical trends and corresponding economic impact to identify a possible way of promoting credit take-off across various sectors. Some of the economists suggested the need to initiate targeted interventions like reducing standard asset provisions. For instance, while the RBI has already made a 0.25% cut on individual housing loans, a further cut may help in improving consumer demand for housing loans. The LTV (loan to value) ratios, risk weights and standard asset provisioning rate for individual housing loans are some of the targeted interventions that the RBI can include in its policy measures to push credit growth.

The surveyed economists were also asked to share their views on the pricing of loans by banks based on an external benchmark in place of MCLR as being currently examined by the RBI.

Most of the surveyed economists felt that linking the pricing of loans to an external benchmark will make the monetary transmission mechanism more effective. In the current MCLR regime, loan pricing decisions by banks are based on internal factors such as cost of funds which are not sensitive to changes in the policy rates. It was felt that the shift to an external benchmark will improve the response time and will bring greater flexibility in the lending rates of banks.

However, while the economists supported the idea, it was also felt that it may not be the right time to introduce this change in context of the underdeveloped money market in India. It was pointed out that while selection of an external benchmark (T-bill, CD or repo rate) could improve the transmission, the pricing of long tenure loans based on these short-term rates needs to be discussed thoroughly as this may not portray market dynamics clearly. Additionally, the current level of depth in T-bill and CD markets can potentially make such benchmarks susceptible to manipulation according to the surveyed economists.

Further, to enable banks to manage the pricing of their assets and liabilities in case of a move-over to an external benchmark, economists suggested that RBI should consider allowing deposit rates to be linked to such an external benchmark as well.

It was mentioned that loans of different tenors should be priced against appropriate tenor benchmarks. In other words, India needs to develop a genuine term money market that will also enable the proper pricing of the benchmark. The RBI could ask banks to price loans on market benchmark plus an appropriate spread rather than a bank specific benchmark.

Latest Projections* – FICCI's Economic Outlook Survey (November 2017)

Variable	**2017-18**
GDP growth rate at market prices (%)	6.7
GVA growth rate at basic prices (%)	6.5
Gross Domestic Savings (% of GDP at market prices)	30.8
Gross Fixed Capital Formation (% of GDP at market prices)	28.0
Fiscal Deficit (as % to GDP) Centre	3.3
WPI Inflation rate (%)	2.8
CPI combined new inflation rate (%)	3.4
Bank credit growth (%)	7.8
CAD as % of GDP at current price	- 1.7

*Median projections as per surveyed economists

Weblink: http://ficci.in/SEDocument/20418/FICCI-EOS-November-2017-Nov21.pdf

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