Economic Outlook Survey

August 2018

HIGHLIGHTS

GDP growth estimated at 7.1 % for Q1 of 2018-19 and 7.4% in 2018-19: FICCI's Economic Outlook Survey

- The latest round of FICCI's Economic Outlook Survey puts forth an annual median GDP growth forecast for 2018-19 at 7.4%, with a minimum and maximum range of 7.1% and 7.5% respectively. The survey was conducted during July 2018 among economists belonging to the industry, banking and financial services sector.
- The median growth forecast for agriculture and allied activities has been put at 3.0% for 2018-19. Industry and services sector are expected to grow by 6.9% and 8.3% respectively in 2018-19.
- Further, the quarterly median forecasts indicate a GDP growth of 7.1% in the first quarter of 2018-19. The official growth numbers for the first quarter are expected to be released later this month (August 31, 2018).
- The median growth forecast for IIP has been put at 6.7% for the year 2018-19, with a minimum and maximum range of 5.2% and 7.5% respectively.
- The outlook of the participating economists on inflation remained moderate. The median forecast for Wholesale Price Index based inflation rate for 2018-19 has been put at 4.8%, with a minimum and maximum range of 4.1% and 5.0% respectively. The Consumer Price Index also has a median forecast of 4.8% for 2018-19, with a minimum and maximum range of 3.0% and 5.5% respectively.
- Concerns remain on external front with median current account deficit forecast pegged at 2.5% of GDP for 2018-19. Merchandise exports are expected to grow by 9.8% while imports are expected to grow by 14.2% during the year.

Views of economists on some key topical issues

Prognosis about Rupee over the near term

- Participating economists unanimously felt that the Rupee will continue to depreciate in 2018-19. It was felt that movement in oil prices and domestic as well as global economic developments will remain two key swing factors for the Rupee.
- While a rise in oil prices are already putting pressure on the current account, global uncertainties around trade and financial markets carry serious risks for the Rupee. Trade tensions between major economies is disturbing the global economic recovery.
- On the domestic front, it was suggested that as India approaches state elections in late 2018 and general elections in early 2019, markets will price in greater degree of political risk premium for the Indian Rupee.
- Even though economists universally believe that the Rupee will remain under strain, they remained divided on the argument on whether the Rupee/US Dollar exchange rate could breach the 70 mark. However, almost all economists believed that any sharp weakening of the Rupee (with or without breaching the 70 mark) is unlikely to sustain for long.
- Participating economists are optimistic about the overall sentiment regarding the Indian economy and feel that favourable investor confidence and a promising long-term growth story will work in favour of bringing stability to the Rupee, going forward.
- Majority of economists believed that the fair value of Indian Rupee vis-à-vis the US Dollar would be in the range of 65 to 66.

Thoughts on ways to strengthen the banking sector

- Most of the economists felt that while all the measures taken so far are well intentioned and mark a paradigm shift in resolving NPAs, the process is still new and will take time to show requisite results.
- Some of them indicated a timeline of about four to six quarters before witnessing a visible progress in resolution of the problem.
- Economists unanimously agreed that the government must work on bringing about reforms in the governance of public sector banks.

- It was also suggested that consolidation of banks along with privatizing some of them could instil better governance standards and should be seriously looked into.
- Economists believed that making banks accountable for their performance through a transparent framework is of utmost importance. For this, it was recommended that banks must be advised to implement separate credit channel with specialised staff to deal with all types of loans from beginning to end.
- In addition, majority of the respondents believed that a fresh round of capital infusion is needed to meet greater capital requirements following stricter norms for NPA recognition by the RBI.
- Lastly, quite a few participating economists felt that there was a need to bring in flexibility in hiring norms. Further, focus must be laid on improving compensation to attract talented individuals. It was suggested that linking recovery of bad loans with incentives could also bring a desirable outcome.

<u>Opinion on India's strategy to ensure energy security</u>

- Participating economists believed that formation of an Oil Buyers' Club would be a good move as it would substantially increase the countries' negotiating power.
- China and India together account for more than one-fifth of the total world imports of crude oil. A cooperative arrangement between the two or even more oil importing nations such as Japan and South Korea will lead to a reasonably negotiated price rather than a price dictated by the sellers.
- Further, since the two countries are likely to have a sustained demand for oil, it will be beneficial for all countries involved to enter into long term contracts to reduce the impact of volatility in crude oil prices. Economists suggested hedging of oil prices should be considered to limit the impact of volatility on the macroeconomic fundamentals of a country.
- It was also suggested that India can look at other oil exporting countries (like African and Latin American countries) to secure its supplies while simultaneously cutting OPEC's dominance in its energy basket.
- The government must incentivise and encourage more private investments in domestic exploration and production of oil to reduce dependence on imports.
- Economists recommended that India must simultaneously diversify its energy basket and shift to other cleaner/ renewable sources of energy like solar, wind, bio-gas etc as well as adopt alternate technologies to meet its requirement. India could develop closer ties with countries that pioneer in renewable energy technology (like Iceland, Israel etc.) to develop its own energy sector.

<u>Views on global trade prospects</u>

- A majority of participating economists believed that an extension of the trade war beyond the short term can significantly impact India.
- However, in the long run, as inflation levels rise in the US on the back of higher domestic prices of imported goods, it may lead to a further increase in interest rates causing even greater outflow of foreign capital from India. Furthermore, an increase in tariffs by the United States will make Indian goods un-competitive and more so if India also plans to increase import tariffs.
- Economists opined that Indian economy is facing three key external shocks viz.- rising oil prices, protectionist trade policies and asymmetry in monetary policy actions in the advanced economies which are already stressing some of the most crucial macroeconomic parameters.
- It was said that the baseline scenario, for now, is that the new tariff walls will continue between US, China and other advanced economies in the short term, however the resultant disturbance in the global value chains will force governments to reach a solution.
- Economists fear that if countries fail to reach a consensus, the world risks a breakdown of the rules based multilateral trade system which would greatly harm India's interests.
- Having said that, some of the economists felt that the US driven trade war is temporary. It was felt that that the US would reconsider the new tariff structure and might, in fact, revoke many of these new tariffs, in the medium term (by early 2020) before entering the general elections.

Survey Profile

The present round of FICCI's Economic Outlook Survey was conducted in the month of July 2018 and drew responses from leading economists representing industry, banking and financial services sector. The economists were asked to provide forecast for key macro-economic variables for the year 2018-19 as well as for Q1 (April-June) FY19 and Q2 (July-September) FY19.

In addition, economists were asked to share their views on certain contemporary themes. Economists were asked to share their prognosis about Rupee over the near term. Views of economists were also sought on ways - other than those already under consideration - to strengthen the banking sector. Further, opinion of economists was sought on India's strategy to ensure energy security. Finally, economists were asked to share their views on trade prospects amidst the current global scenario.

Survey Results: Part A
Projections – Key Economic Parameters

National Accounts

GDP growth at 2011-12 prices

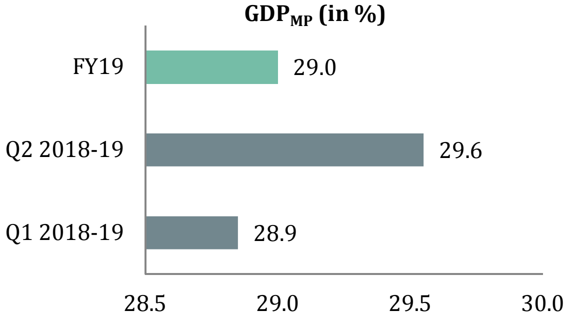
	Annual (2018-19)			Q12018-19			Q2 2018-19		
Growth (in %)	**Median**	**Min**	**Max**	**Median**	**Min**	**Max**	**Median**	**Min**	**Max**
GDP@ market prices	**7.4**	7.1	7.5	**7.1**	7.0	7.4	**7.1**	7.0	7.6
GVA@ basic prices	**7.2**	7.0	7.3	**6.9**	6.5	7.3	**7.0**	6.7	7.3
Agriculture & Allied activities	**3.0**	2.4	4.3	**3.3**	1.9	4.5	**3.0**	2.5	4.0
Industry	**6.9**	5.0	7.5	**6.7**	5.0	8.2	**6.6**	6.3	8.0
Services	**8.3**	7.8	9.4	**8.2**	7.4	8.3	**8.3**	7.8	8.8

The latest round of FICCI's Economic Outlook Survey puts forth an annual median GDP growth forecast for 2018-19 at 7.4% - which reflects no change from the estimate put out in the previous survey round.

The median growth forecast for agriculture and allied activities has been put at 3.0% for 2018-19, with a minimum and maximum growth estimate of 2.4% and 4.3% respectively. Industry and services sector are expected to grow by 6.9% and 8.3% respectively during the year.

The quarterly median forecasts indicate a GDP growth of 7.1% in the first quarter of 2018-19 as well as in the second quarter.

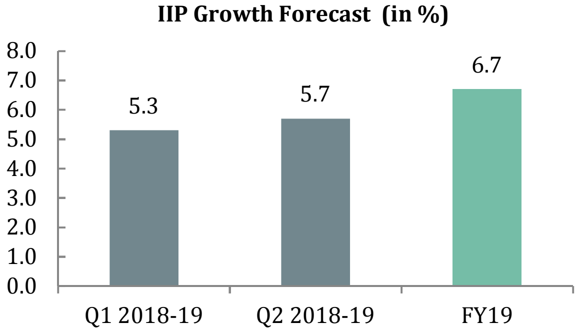
Gross Fixed Capital Formation as % of GDP_{MP} (in %)



The ratio of Gross Fixed Capital Formation to GDP for 2018-19 has been estimated at 29.0%. As per actual data, the corresponding number in 2017-18 was 31.4%.

The median growth projection for Q1 2018-19 is put at 28.9%.

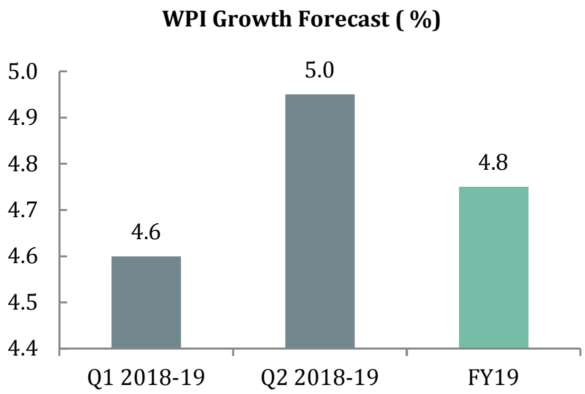
Index of Industrial Production (IIP)

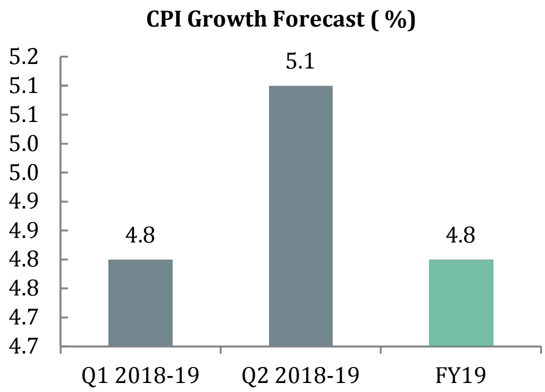


The economist put median growth forecast for IIP at 6.7% for 2018-19, with a minimum and maximum range of 5.2% and 7.5% respectively.

The latest data, however, reported some moderation in the index of industrial production. The index grew by 3.2% in the month of May 2018 vis-à-vis 4.8% growth witnessed in the month of April. Cumulative growth in the first two months of Q1 2018-19 is reported at 3.9%.

Wholesale Price Index (WPI)& Consumer Price Index (CPI)



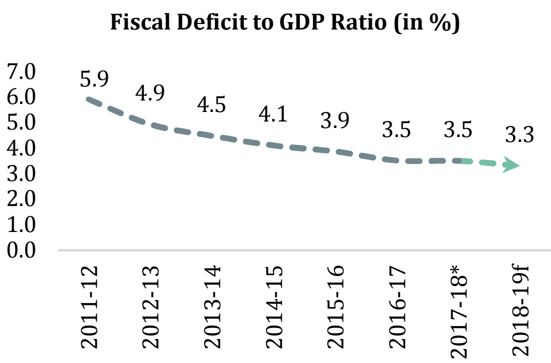


Wholesale Price Index based inflation rate is projected at 4.8% in 2018-19, with a minimum and maximum range of 4.1% and 5.0% respectively. WPI based inflation stood at 2.9% for the entire fiscal year 2017-18. The increase in price levels in 2018-19 comes on back of surging crude oil prices. The latest data on WPI based inflation puts across an inflation rate of 4.6% over the cumulative period April-June 2018.

Consumer Price Index has a median forecast of 4.8% for 2018-19, with a minimum and maximum range of 3.0% and 5.5% respectively. CPI based inflation was reported at 3.6% in 2017-18 vis-à-vis 4.5% inflation noted in 2016-17.CPI forecast for Q2 2018-19 has been put at 5.1% according to our survey results.

Fiscal Deficit

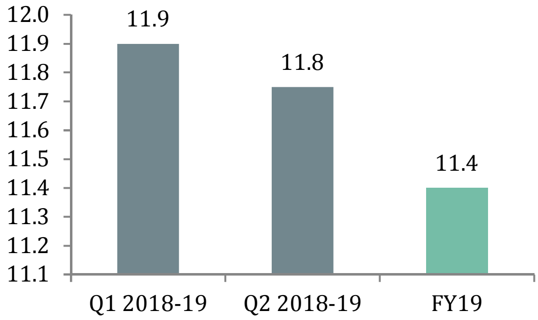
The median fiscal deficit to GDP ratio was put at 3.3% for the fiscal year 2018-19 with a minimum and maximum range of 3.2% and 3.6% respectively.



2017-18* Government Projection
2018-19# Budgeted

Money and Banking

Bank Credit: Growth (in %)



	End of Q2 2018-19	End of 2018-19
Repo Rate	**6.5%**	**6.5%**

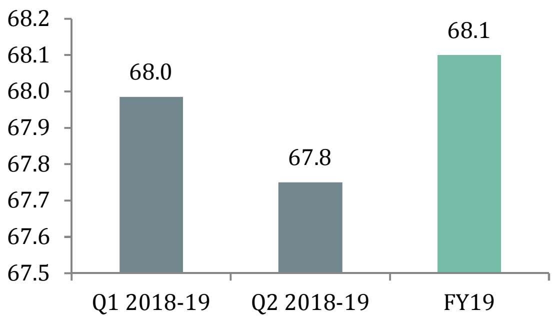
External Sector

2018-19	Export	Import
USD billion	337	537
Growth (in %)	9.8	14.2

Based on the responses of the participating economists, the median growth forecast for exports has been put at 13.0% and for imports at 17.0% for Q2 2018-19.

	End of Q2 2018-19	End of 2018-19
CAD as % of GDP	**2.0%**	**2.5%**

USD/INR Exchange Rate



Survey Results: Part B
Views of the Economists

PROGNOSIS ABOUT RUPEE OVER NEAR TERM

Rupee has been facing several headwinds recently. The Rupee Dollar exchange rate depreciated to an all-time low of 68.94 on June 28, 2018 which is reminiscent of the sharp drop witnessed in August 2013. Economists were asked to share their prognosis about the movement of Rupee over near term and the likelihood of Rupee Dollar exchange rate breaching the 70 mark. Economists were also asked to share their thoughts on the fair value of Indian Rupee.

Participating economists unanimously felt that the Rupee will continue to depreciate in 2018-19. It was felt that movement in oil prices and domestic as well as global economic developments will remain the two key swing factors for the Rupee value. Widening current account deficit and higher inflationary pressures arising out of increasing international crude oil prices are already pulling the currency down. Therefore, any further rise in oil prices poses significant risks to the fair value of currency.

Global uncertainties around trade and financial markets also carry serious risks to the Rupee. Trade tensions between major economies are disturbing the global economic recovery and might put the global economic order in danger. Additionally, a tighter monetary policy stance of Federal Reserve, volatile global financial markets and increasing geo-political uncertainties are contributing to higher foreign capital outflows, thereby putting a downward pressure on the Rupee exchange rate.

On the domestic front, it was suggested that as India approaches state elections in late 2018 and general elections in early 2019, markets will price in greater degree of political risk premium for the Indian Rupee.

Even though economists universally believe that the Rupee will remain under strain, they were divided on the argument on whether the Rupee/US Dollar exchange rate could breach the 70 mark. Approximately, half of the respondents felt that it was a highly probable scenario. However, they also agreed that the slip would be temporary in nature as historical evidence suggests that the Rupee tends to recover and move to its baseline trend. Almost all economists believe that any sharp weakening of the Rupee (with or without breaching the 70 mark) is unlikely to sustain for long. Economists are optimistic about the overall sentiment regarding the Indian economy and feel that favourable investor confidence and a promising long-term growth story will work in favour of bringing stability to the Rupee, going forward.

On being asked about the fair value of the currency, majority of the economists believed that the fair value of Indian Rupee vis-à-vis the US Dollar would be in the range of 65 to 66.

THOUGHTS ON WAYS TO STRENGTHEN THE BANKING SECTOR

Reserve Bank of India released the Financial Stability Report in June 2018. The report signalled continuing stress in the Indian banking system and cited a further increase in gross non-performing assets (GNPA) ratio from 11.6% in March 2018 to 12.2% by March 2019. Furthermore, public sector banks that are already under the prompt corrective action framework indicate worsening of their GNPA ratio by March 2019, with six of them experiencing capital shortfall. To redress this stress in the banking sector, the government and the central bank have been proactively taking several measures. The most recent one includes announcement of Project Sashakt- a five point plan to help resolution of stressed assets. Besides the steps already taken, participating economists were asked to recommend alternate/additional ways which could strengthen the banking sector in the country.

Most of the economists felt that while all the measures taken so far are well intentioned and mark a paradigm shift in resolving NPAs, the process is still new and will take time to show requisite results. Some of them indicated a timeline of about four to six quarters before witnessing a visible progress in resolution of the problem. This comes despite various attempts being made to reduce ambiguity and expedite the resolution process, including the recent amendments made to the Insolvency and Bankruptcy Code.

In the meantime, economists unanimously agreed that the government must work on bringing about reforms in the governance of public sector banks. In this regard, it was suggested that implementing the Nayak Committee recommendations could help in improving the functioning of the banks and create a more empowered board. This would also reduce interference in credit decisions, which has been a major contributing factor for the current NPA mess. It was also suggested that consolidation of banks along with privatizing some of them could instil better governance standards amongst them and should be seriously looked into.

Further, it was opined that all banks must be advised to implement separate credit channel with specialised staff to deal with all types of loans from beginning to end. Making banks accountable for their performance through a transparent framework is of utmost importance.

In addition, majority of the respondents believed that a fresh round of capital infusion is needed to meet greater capital requirements following stricter norms for NPA recognition by the RBI. This will also enable banks to grow their lending operations at a healthy rate. There is a need for banks to rework their business strategies and focus on improving efficiency in the delivery centric financial services to regain their role as principal financial intermediaries. It was indicated that innovating customer specific products to meet their financial needs could be one such strategy.

Lastly, many economists felt that there was a need to bring in flexibility in hiring norms. Focus must be laid on improving compensation to attract talented individuals. It was suggested that linking recovery of bad loans with incentives could also bring a desirable outcomes.

OPINION ON INDIA'S STRATEGY TO ENSURE ENERGY SECURITY

The recent volatility in crude oil prices has posed a significant risk to India's macroeconomic fundamentals. Given that India is highly dependent on imports for its crude oil requirement, such episodes of uncertainty have severe repercussions for the economy. Recent developments in the oil market have brought China and India together and two countries are contemplating to constitute an 'Oil Buyers' Club' to counter dominance of OPEC in oil pricing. Given this backdrop, economists were asked to share their thoughts on whether the possible cooperation strategy between China and India bring in greater energy security and recommend other solutions for achieving the same.

Participating economists universally believed that formation of an Oil Buyers' Club would be a good move as it would substantially increase the countries' negotiating power. China and India together account for more than one-fifth of the total world imports of crude oil. A cooperative arrangement between the two or even more oil importing nations such as Japan and South Korea will lead to a reasonably negotiated price rather than a price dictated by the sellers.

It was felt that since the two countries are likely to have a sustained demand for oil; it will be beneficial for all countries involved to enter into long term contracts to reduce the impact of volatility in crude oil prices. Further, economists' proposed that oil prices should be hedged to limit the impact of volatility on the macroeconomic fundamentals of a country. This, they believed, will ensure energy security and reduce import bills apart from avoiding sudden shocks to the economies of the countries involved.

Alongside, India can look at other oil exporting countries (like African and Latin American countries) to secure its supplies while simultaneously cutting OPEC's dominance in its energy basket.

Additionally, the government must incentivise and encourage more private investments in domestic exploration and production of oil to reduce dependence on imports.

Majority of the respondents also felt that while the above-mentioned measures are necessary, India must simultaneously diversify its energy basket and shift to other cleaner/ renewable sources of energy like solar, wind, bio-gas etc as well as adopt alternate technologies to meet its requirement. Transport sector, for instance, could highly benefit from this as it continues to be one of the major guzzlers of crude oil. In this regard, economists felt that moving towards electric vehicles could contribute to management of a ballooning oil import bill. This must be combined with ongoing power distribution reforms in order to improve efficiency of distribution to ensure sustained supply of power.

In addition, India must develop closer ties with countries that pioneer in renewable energy technology (like Iceland, Israel etc.) in order to develop its own energy sector. Focussing on accelerated use of renewable energy will balance India's energy needs and dependence on imports for meeting the same.

VIEWS ON GLOBAL TRADE PROSPECTS

The Federal Reserve is on a tightening spree with the central bank raising the interest rates by 25 basis points in the month of June, while indicating two more increases in 2018. This is likely to result in capital outflow from EMEs. Furthermore, there are a fresh round of tariffs and retaliatory tariffs being imposed by countries around the world. Of late, the US has announced 25% tariff on USD 50 billion worth of Chinese goods in the first round and on USD 35 billion worth of Chinese imports in the second round. China, too, has retaliated in equal measure to both instances of tariff imposition. Even though there were growing indications of a looming trade war since February this year, actual implementation came as a surprise as the move came after both, US and China, reached an agreement on reducing the trade gap.

Given these latest developments, economists were asked to share their views on the evolution of global trade architecture in the short to medium term and the impact it will have on India.

A majority of the participating economists believed that an extension of the trade war beyond the short term can significantly impact India. The Indian economy can cash in on the opportunities being opened by the trade war, in the short term, which could result in new tie-ups and trade agreements among nations.

However, in the long run, as inflation levels rise in the US on the back of higher domestic prices of imported goods, it may lead to a further increase in interest rates causing even greater outflow of foreign capital from India. Furthermore, an increase in tariffs by the United States will make Indian goods un-competitive and more so if India also plans to increase import tariffs. This would specially be true for products which utilize an import dependant input.

Economists opined that India's economy will be impacted by three key external shocks viz.- rising oil prices, protectionist trade policies and asymmetry in monetary policy actions in the advanced economies which are already stressing some of the most crucial macroeconomic parameters. The most prominent and inevitable risk lies in the widening imbalance being seen in the current account. This along with foreign capital outflows is pressurising the Rupee with the currency hitting an all-time low in June 2018. It was indicated that impact on India is more sentiment driven which was witnessed in the recent rally as well where in risk aversion fuelled by elevation in trade tensions sent the Rupee and bond markets into a tizzy.

While the baseline scenario, for now, is that the new tariff walls will continue between US, China and other advanced economies over the short term, the resultant disturbance in the global value chains will force governments to reach a solution. Economists fear that if countries fail to reach a consensus, the world risks a breakdown of the rule based multilateral trade system. This would greatly harm India's interests as it could reduce external demand due to weaker global growth and cause delays in investment decisions.

Having said that, some economists felt that the US driven trade war is temporary. It was felt that that the US would reconsider the new tariff structure and might, in fact, revoke many of these new tariffs, in the medium term (by early 2020) before entering the general elections. They argued that the ongoing trade war would severely impact supply channels of US manufactures as well which would soon be visible in the GDP estimates for the country, forcing the country to reconsider its decision. It was felt that normalcy would start getting restored starting May 2019 once the US mid-term elections in November 2018 pass and the impact of protectionism on US GDP start becoming clearer.

Appendix

	Outlook 2018-19				Outlook Q1 2018-19				Outlook Q22018-19			
Key Macroeconomic variables	**Mean**	**Median**	**Min**	**Max**	**Mean**	**Median**	**Min**	**Max**	**Mean**	**Median**	**Min**	**Max**
GDP growth rate at market prices (%)	7.3	7.4	7.1	7.5	7.2	7.1	7.0	7.4	7.2	7.0	7.0	7.6
GVA growth rate at basic prices(%)	7.1	7.2	7.0	7.3	6.9	6.9	6.5	7.3	7.0	7.0	6.7	7.3
Agriculture & Allied	3.2	3.0	2.4	4.3	3.3	3.3	1.9	4.5	3.2	3.0	2.5	4.0
Industry	6.8	6.9	5.0	7.5	6.6	6.7	5.0	8.2	6.8	6.6	6.3	8.0
Services	8.3	8.3	7.8	9.4	8.0	8.2	7.4	8.3	8.3	8.3	7.8	8.8
Gross Domestic Savings (% of GDP at market prices)	30.1	30.0	29.5	30.5	29.6	29.9	28.0	30.5	29.8	29.9	29.0	30.5
Gross Fixed Capital Formation (% of GDP at market prices)	29.0	29.0	28.2	29.5	28.8	28.9	28.5	29.0	29.7	29.6	28.7	31.0
Fiscal Deficit (as % to GDP) Centre	3.3	3.3	3.2	3.6	-	-	-	-	-	-	-	-
Growth in IIP (%)	6.4	6.7	5.2	7.5	5.5	5.3	4.8	6.5	5.9	5.7	5.5	6.8
WPI Inflation rate (%)	4.6	4.8	4.1	5.0	4.5	4.6	4.3	4.8	5.0	5.0	4.7	5.4
CPI combined new inflation rate (%)	4.7	4.8	3.0	5.5	4.8	4.8	4.7	5.0	5.2	5.1	4.8	6.0
Money supply growth M3 (%) (end period)	9.8	10.7	8.0	11.2	10.0	9.8	9.8	10.5	10.2	9.9	9.8	11.0
Bank credit growth (%)	11.2	11.4	8.0	13.5	11.4	11.9	9.0	12.8	11.8	11.8	11.0	12.5

Repo Rate (end period)	6.5	6.5	6.5	6.75	6.25	6.25	6.25	6.25	6.5	6.5	6.25	6.5
Merchandise Export												
Value in USD billion	338.9	336.9	320.0	362.4	82.2	82.7	78.5	85.0	85.4	85.2	81.4	90.0
Growth (%)	11.1	9.8	8.0	17.3	14.1	14.0	14.0	14.2	13.8	13.0	12.5	16.0
Merchandise Import												
Value in USD billion	529.5	536.7	462.5	566.2	125.7	126.5	120.0	130.0	126.6	127.2	122.0	130.0
Growth (%)	15.4	14.2	12.0	20.7	14.5	13.5	13.0	17.0	16.7	17.0	14.0	19.0
Trade Balance (% to GDP)	-6.7	-6.9	-5.2	-7.3	-5.8	-5.8	-5.0	-6.5	-5.8	-5.8	-5.5	-6.1
CAD as % of GDP at current price	2.4	2.5	2.0	2.6	2.0	1.9	1.6	2.5	1.8	2.0	1.5	2.0
US$ / INR exchange rate (end period)	68.2	68.1	64.5	71.0	67.9	68.0	67.0	68.6	67.6	67.8	65.5	69.3

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