Economy Watch

Monitoring India's macro-fiscal performance

December 2020

EY

Building a better working world

Contents

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Highlights

1. Real GDP contracted at a slower pace of (-)7.5% in 2QFY21 as compared to (-)23.9% in 1QFY21.

2. At 3.6% in October 2020, IIP growth was the highest since February 2020.

3. In November 2020, PMI manufacturing was at 56.3 and PMI services at 53.7. These levels are slightly lower than 58.9 and 54.1 respectively in October 2020.

4. At 6.9% in November 2020, CPI inflation continued to breach the 6% upper tolerance limit of the RBI's inflation target range for the eighth successive month.

5. The RBI retained the repo rate at 4.0% in its December 2020 monetary policy review as CPI inflation remained elevated.

6. As per the CGA, center's gross taxes contracted by (-)16.8% during April-October FY21 as compared to a growth of 1.2% in the corresponding period of FY20.

7. During April-October FY21, center's capital expenditure contracted by (-)1.9% while revenue expenditure showed a subdued growth of 0.7%.

8. During April-October FY21, center's fiscal deficit stood at 119.7% of the annual budgeted target while the corresponding number for revenue deficit was 126.8%.

9. Contraction in merchandise exports and imports was at (-)8.7% and (-)13.3%, respectively, in November 2020.

10. The OECD projected a global contraction of (-)4.2% in 2020, with a contraction of (-)9.9% forecasted for India.

Foreword

Revenue constraints may limit Center's FY22 budget's growth thrust

The CSO released 2QFY21 national income aggregates on 27 November 2020 indicating that although the GDP contraction continued into 2QFY21, it was relatively moderate at (-)7.5% compared to the sharp fall of (-)23.9% in 1QFY21. The Monetary Policy Statement issued on 4 December 2020 by the RBI assesses mild positive GDP growth rates of 0.1% and 0.7% in 3Q and 4QFY21 respectively. Taking these together with the CSO's real GDP growth estimates of 1Q and 2QFY21, the RBI estimates real GDP to contract by (-)7.5% in FY21. This may improve further if there is a faster recovery at least in 4QFY21, the likelihood of which is quite high as high frequency indicators have started signaling a strong momentum towards recovery.

The high frequency indicators have been showing a slow but sustained turnaround. PMI manufacturing reached an unprecedented level of 58.9 in October 2020 and remained high at 56.3 in November 2020. PMI services recovered in October 2020 reaching a level of 54.1. In November 2020, it was at 53.7. In October 2020, growth in IIP increased to 3.6%, the highest since February 2020. By 11 December 2020, India's foreign exchange reserves were at a historic-high of US$578.5 billion which is US$100.8 billion more than the level in end-March 2020. Monthly GST collections crossed the threshold of INR1 lakh crore for the second consecutive month in November 2020. Passenger vehicle sales have shown a consistent increase since June 2020. In November 2020, the sale was about 8.3 lakh units as compared to 9 lakh units in November 2019. Growth in power consumption remained positive at 2.8% in November 2020. Contraction in merchandise exports and imports increased to (-)8.7% and (-)13.3%, respectively, in November 2020 as compared to (-)5.1% and (-)11.5% respectively in October 2020. Since the fall in imports is sharper than that in exports, the contribution of net exports to GDP growth is expected to remain positive as was the case in 1HFY21.

With CPI inflation remaining well above the upper threshold of the monetary policy target of 6%, the monetary authorities may not be inclined to reduce further the policy rate from the current level of 4%. As such, in the near future, the policy thrust to support growth may have to come almost entirely from fiscal policy initiatives of which the FY22 union budget may be a key instrument.

The fiscal policy options, however, are likely to be significantly constrained due to the weakness of center's gross tax revenues. This aspect has been discussed at length in the in-focus write-up of this month's Economy Watch. The Ministry of Finance has to assess the base magnitude in FY21 and the growth rate that can be applied on it in order to project center's gross tax revenues for FY22. There was a contraction in center's gross tax revenues even before the COVID shock hit the Indian economy. In FY20, center's gross tax revenues fell by (-)3.4%. In FY21, the contraction is expected to be sharper. We estimate it to be about (-)14.5%. This implies that in absolute numbers, the base figure for gross tax revenues estimated at INR17.2 lakh crore in FY21 may be below the actual gross tax revenues of INR20.1 lakh crore in FY20. In fact, center's gross tax revenues were at INR17.2 lakh crore in FY17. Given the structural changes in GST and CIT in the recent years, nominal tax revenue growth rate may be expected to be less than the nominal GDP growth rate implying a buoyancy of less than 1. The buoyancy of center's gross tax revenues was 0.8 and (-)0.5 in FY19 and FY20 respectively. With India's FY22 nominal GDP growth projected at 12% by the IMF, it would be unrealistic if the Ministry of Finance considers a growth in center's gross tax revenues at any rate higher than 10%. Accordingly, center's gross tax revenues may be estimated for FY22 at INR18.9 lakh crores. In FY21, center's total expenditure in the first seven months amounted to only 54.6% of the budgeted amount of INR30.4 lakh crore. Even if the center undertakes a fiscal deficit of 6.9% of the estimated GDP in FY21, it may be able to finance a total expenditure of only INR26.9 lakh crore, which is exactly equal to the actual expenditure in FY20. This may serve as the base figure for the FY22 budget. Even at this relatively lower level, if a growth of 10% is targeted in FY22, its financing will call for a high level of fiscal deficit at close to 6.8% of the estimated GDP. This large financing gap highlights a growing gap between total expenditures and non-debt receipts, consisting of center's revenue receipts and non-debt capital receipts. This gap, estimated at INR14.5 lakh crore for FY22 as compared to INR9.4 lakh crore and INR13.1 lakh crore in FY20 and FY21 (estimated) respectively, is to be financed by the fiscal deficit. This implies that even to finance a modest increase of about 10% in total expenditure in FY22, the central government may have to deviate from the FRBM norm of 3% of fiscal deficit to GDP ratio by a margin of 3-4% points. Given the need for continued reliance on a high level of fiscal deficit, an effort may be made to improve the quality of expenditure by focusing relatively more on capital expenditure which is associated with high income and employment multipliers.

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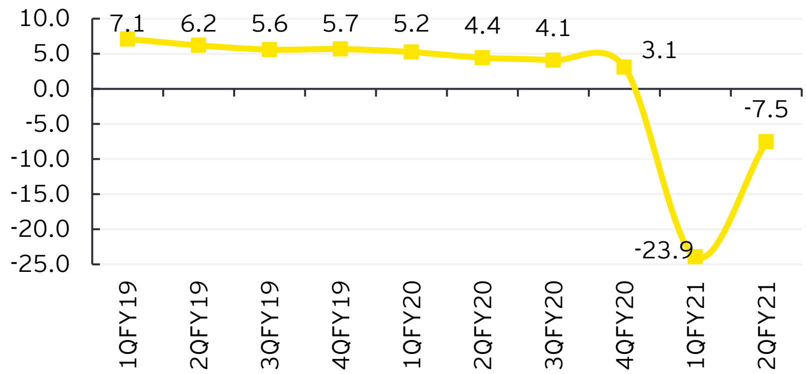
1. Growth: real GDP contracted at a slower pace of (-)7.5% in 2QFY21

A. Real GDP contracted for the second successive quarter in 2QFY21 implying that the economy has entered into a technical recession

- As per data released by the Ministry of Statistics and Programme Implementation (MoSPI) on 27 November 2020, real GDP contracted at a slower pace of (-)7.5% in 2QFY21 as compared to (-)23.9% in 1QFY21 (**Chart 1**) due to phased relaxation of COVID-19 related restrictions leading to a gradual resumption of economic activities.

Chart 1: real GDP growth (y-o-y, %)



- On the demand side, all the three components of domestic demand, namely, private final consumption expenditure (PFCE), government final consumption expenditure (GFCE) and gross fixed capital formation (GFCF) contracted in 2QFY21.
- Both PFCE and GFCF contracted at a slower pace of (-)11.3% and (-)7.3% respectively in 2QFY21 (**Table 1**).
- GFCE which posted a growth of 16.4% in 1QFY21, contracted sharply by (-)22.2% in 2QFY21.
- In 2QFY21, both exports and imports contracted at a slower pace relative to that in 1QFY21. However, imports contracted at a sharper rate of (-)17.2% as compared to the contraction of (-)1.5% in exports in 2QFY21.
- On the output side, contraction in real GVA was lower at (-)7.0% in 2QFY21 as compared to (-)22.8% in 1QFY21.
- Three GVA sectors namely agriculture, manufacturing and electricity et.al., together accounting for about 36%[1] of the overall output, showed a positive growth in 2QFY21. While the agricultural GVA grew by 3.4% in 2QFY21, the GVA in manufacturing and electricity grew by 0.6% and 4.4% respectively in 2QFY21 as compared to a sharp contraction in 1QFY21 (**Table 1**).
- Contraction in construction and trade, hotels, transport, communication and services related to broadcasting was lower at (-)8.6% and (-)15.6% respectively in 2QFY21.
- Growth in public administration, defence and other services, and financial, real estate and professional services contracted at a higher pace of (-)12.2% and (-)8.1% respectively in 2QFY21 as compared to (-)10.3% and (-)5.3% respectively in 1QFY21.
- Nominal GDP contracted by (-)4.0% in 2QFY21, significantly improving from (-)22.6% in 1QFY21.

Table 1: real GDP and GVA growth (%)

Agg. demand	2Q FY19	3Q FY19	4Q FY19	1Q FY20	2Q FY20	3Q FY20	4Q FY20	1Q FY21	2Q FY21
PFCE	8.8	7.0	6.2	5.5	6.4	6.6	2.7	-26.7	-11.3
GFCE	10.8	7.0	14.4	6.2	14.2	13.4	13.6	16.4	-22.2
GFCF	11.5	11.4	4.4	4.6	-3.9	-5.2	-6.5	-47.1	-7.3
EXP	12.5	15.8	11.6	3.2	-2.2	-6.1	-8.5	-19.8	-1.5
IMP	18.7	10.0	0.8	2.1	-9.4	-12.4	-7.0	-40.4	-17.2
GDP	**6.2**	**5.6**	**5.7**	**5.2**	**4.4**	**4.1**	**3.1**	**-23.9**	**-7.5**
Output: major sectors									
Agr.	2.5	2.0	1.6	3.0	3.5	3.6	5.9	3.4	3.4
Ming.	-7.0	-4.4	-4.8	4.7	-1.1	2.2	5.2	-23.3	-9.1
Mfg.	5.6	5.2	2.1	3.0	-0.6	-0.8	-1.4	-39.3	0.6
Elec.	9.9	9.5	5.5	8.8	3.9	-0.7	4.5	-7.0	4.4
Cons.	5.2	6.6	6.0	5.2	2.6	0.0	-2.2	-50.3	-8.6
Trans.	7.8	7.8	6.9	3.5	4.1	4.3	2.6	-47.0	-15.6
Fin.	6.5	6.5	8.7	6.0	6.0	3.3	2.4	-5.3	-8.1
Publ.	8.9	8.1	11.6	7.7	10.9	10.9	10.1	-10.3	-12.2
GVA	**6.1**	**5.6**	**5.6**	**4.8**	**4.3**	**3.5**	**3.0**	**-22.8**	**-7.0**

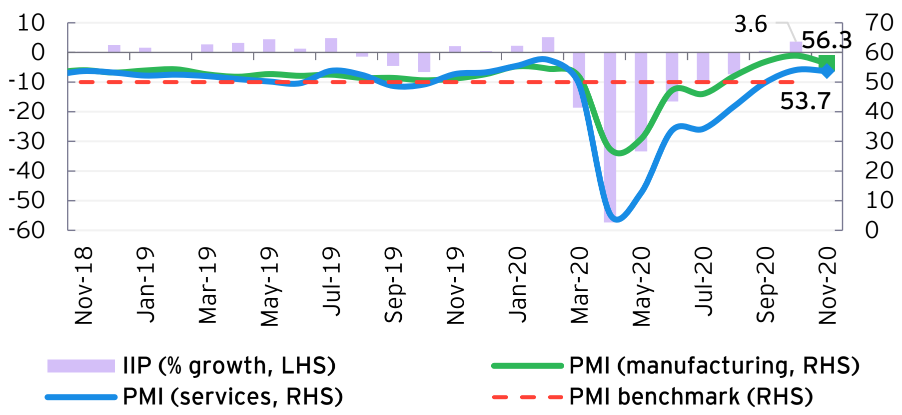
Source: MoSPI, GoI

[1] Share in FY20 nominal GVA

B. IIP: growth in IIP increased to 3.6% in October 2020

- As per the quick estimates of IIP for October 2020, released by the MoSPI on 11 December 2020[2], IIP grew by 3.6% in October 2020 as compared to 0.5% (revised) in September 2020 (**Chart 2**). This was led by a further improvement in the output of manufacturing and electricity (Table A1 in data appendix).
- After contracting for seven consecutive months, the output of manufacturing grew by 3.5% in October 2020. Growth in the output of electricity accelerated to 11.2% in October 2020 as compared to 4.9% in September 2020, partly aided by a favorable base effect. Output of mining however contracted by (-)1.5% in October 2020 as compared to a growth of 1.4% in September 2020.
- Output of capital goods, an indicator of investment, grew by 3.3% in October 2020 after contracting for 22 consecutive months. Growth in the output of consumer durables accelerated to 17.6% in October 2020 from 3.4% in September 2020. Output of both infrastructure/construction goods and consumer non-durables posted a robust growth of 7.8% and 7.5% respectively in October 2020 as compared to 2.5% and 2.8% respectively in September 2020.
- Output of eight core infrastructure industries (core IIP) however, contracted at a faster pace of (-)2.5% in October 2020 as compared to (-)0.1% in September 2020. This was led by a contraction in the output of petroleum refinery products ((-)17.0%), natural gas ((-)8.6%), crude oil ((-)6.2%) and steel ((-)2.7%). On the other hand, output of electricity (10.5%), coal (11.6%) and cement (2.8%) posted a positive growth during the month.

Chart 2: IIP growth and PMI



Source: Office of the Economic Adviser, Ministry of Commerce and Industry and IHS Markit

At 3.6% in October 2020, IIP growth was the highest since February 2020.

C. PMI: signaled a slower expansion in manufacturing and services in November 2020

- Headline manufacturing PMI (seasonally adjusted (sa)) at 56.3 in November 2020 continued to expand for the fourth successive month. However, its level fell from 58.9 in October 2020 to a three-month low in November 2020 (**Chart 2**). Among the three sub-segments of manufacturing, consumer goods was the only one to witness a stronger pace of expansion in November 2020 compared to the previous month.
- PMI services expanded for the second successive month in November 2020 although falling to 53.7 from 54.1 in October 2020. Expansion in new work orders was driven by the domestic market with new export orders decreasing sharply again in November 2020.
- Reflecting a slower expansion in both manufacturing and service sectors activity, the composite PMI Output Index (sa) fell to 56.3 in November 2020 from 58.0 in October 2020.

In November 2020, both PMI manufacturing and services continued to expand although at a slower pace relative to that in October 2020. PMI manufacturing was at 56.3 and PMI services was at 53.7 in November 2020.

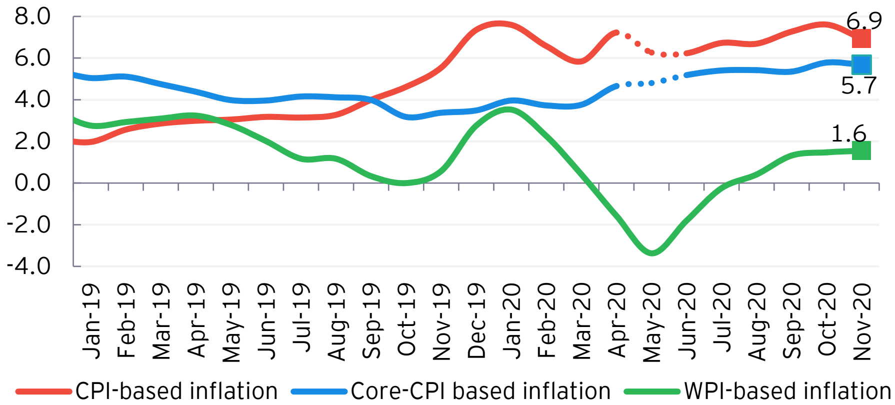
[2] Quick estimates of IIP and use-based index for the month of October 2020: http://mospi.nic.in/sites/default/files/iip/iipoct20.pdf

2. Inflation: CPI inflation remained elevated at 6.9% in November 2020

CPI inflation remained elevated at 6.9% in November 2020, although declining from a 77-month high of 7.6% in October 2020, due to lower inflation in vegetables.

- Inflation in vegetables fell to a three-month low of 15.6% in November 2020 from 22.1% in October 2020 led by a fall in inflation in onions to (-)0.6% from 9.8% over the same period.
- Consumer food inflation moderated to 9.4% in November 2020 from 11.0% in October 2020.
- Core CPI inflation[3] remained elevated, falling marginally to 5.7% in November 2020 as compared to a 24-month high of 5.8% in October 2020 **(Chart 3)**.
- Housing-based inflation eased marginally to 3.2% in November 2020 from 3.3% in October 2020.
- Inflation in transportation and communication services remained elevated at 11.1% in November 2020, as compared to 11.2% in October 2020, mainly due to higher taxation of fuel used for transportation. Health services inflation increased to a 13-month high of 5.5% in November 2020 from 5.2% in October 2020.
- Inflation in fuel and light eased to a five-month low of 1.9% in November 2020.

Chart 3: inflation (y-o-y, in %)



At 6.9% in November 2020, CPI inflation continued to breach the 6% upper tolerance limit of the RBI's inflation target range for the eighth successive month.

Source: MoSPI, Office of the Economic Adviser, Government of India (GoI)
Note: Headline CPI inflation and inflation in certain groups for the month of April 2020 and May 2020 have been imputed by the MoSPI[4]; Core CPI inflation has been estimated for April 2020 and May 2020 using this imputed data

WPI inflation increased to a nine-month high of 1.6% in November 2020 from 1.5% in October 2020, largely due to higher inflation in manufactured products.

- Core WPI inflation increased to a 22-month high of 2.6% in November 2020 led by rising inflation in manufactured basic metals.
- The level of inflation in 16 of the 22 manufactured products increased in November 2020 when compared to their respective levels in October 2020. Inflation in manufactured basic metals rose to a 23-month high of 7.2% in November 2020.
- WPI food index-based inflation fell to a five-month low of 4.3% in November 2020 from 5.8% in October 2020 as inflation in vegetables eased to 12.2% from 25.2% over the same period.
- The pace of contraction in prices of crude and natural gas increased to a six-month high of (-)25.6% in November 2020.
- Fuel and power-based inflation was at (-)9.9% in November 2020, as compared to (-)10.9% in October 2020 as inflation in furnace oil turned positive at 4.4% after 17 successive months of contraction.

[3] Core CPI inflation is measured in different ways by different organizations/agencies. Here, it has been calculated by excluding food, and fuel and light from the overall index.
[4] http://www.mospi.gov.in/sites/default/files/press_release/CPI%20Technical%20Note%20on%20Imputation.pdf

3. Fiscal performance: center's gross tax revenues during Apr-Oct FY21 contracted by (-)16.8%

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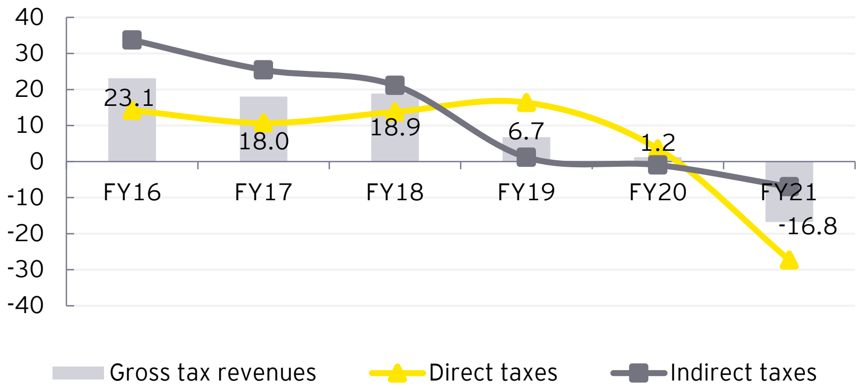
A. Tax and non-tax revenues

- As per the Comptroller General of Accounts (CGA)[5], gross central taxes during April-October FY21 contracted by (-)16.8% as compared to a growth of 1.2% during April-October FY20 (**Chart 4**). Both direct and indirect taxes contracted on a y-o-y basis during the first seven months of FY21.
- As a proportion of the annual budgeted target, gross taxes during April-October FY21 stood at 36.1%, the lowest since at least FY01. The corresponding ratio for FY20 stood at 42.7%.
- Direct tax revenues contracted by (-)27.3% during April-October FY21 as compared to a growth of 3.5% in the corresponding period of FY20.
- Corporate income tax (CIT) revenues contracted by (-)36.7% during April-October FY21 as compared to a growth of 0.9% in the corresponding period of FY20.
- There was a contraction of (-)16.9% in personal income tax (PIT) revenues during April-October FY21 as compared to a growth of 6.7% during the corresponding period of the previous year.
- Indirect taxes (comprising union excise duties, service tax, customs duty, CGST, UTGST, IGST[6] and GST compensation cess) showed a contraction of (-)7.0% during April-October FY21 as compared to (-)1.0% during the corresponding period of the previous year.
- Center's gross tax to GDP ratio stood at 8.5% in 1HFY21 as compared to a three-year corresponding average of 9.8%.

Chart 4: growth in central gross tax revenues during April-October (y-o-y, in %)



As per the CGA, center's gross taxes contracted by (-)16.8% during April-October FY21 as compared to a growth of 1.2% in the corresponding period of FY20.

Source: Monthly Accounts, Controller General of Accounts (CGA), Government of India
Notes: (a) Direct taxes include personal income tax and corporation tax, and indirect taxes include union excise duties, service tax, customs duty, CGST, UTGST, IGST and GST compensation cess; (b) Other taxes (securities transaction tax, wealth tax, fringe benefit tax, banking cash transaction tax, etc.) are included in the center's gross tax revenues along with direct and indirect taxes.

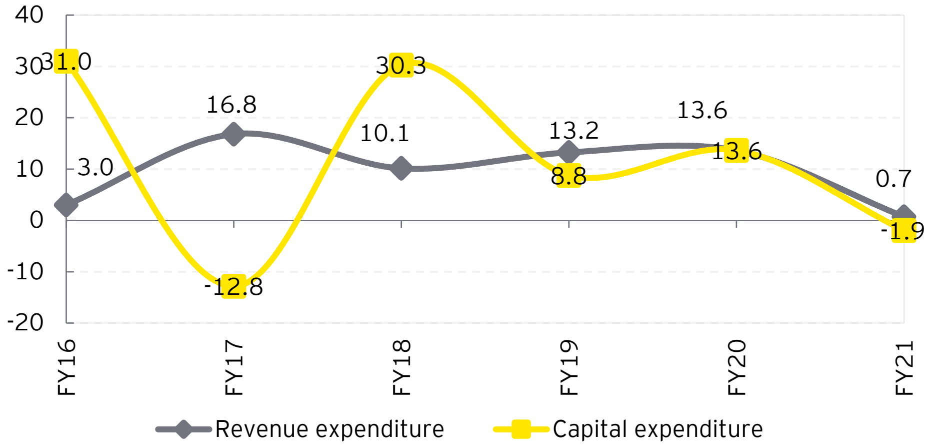
- Center's non-tax revenues showed a contraction of (-)48.2% during the first seven months of FY21 as compared to a growth of 75.5% during the corresponding period of FY20.
- As a proportion of the annual budgeted target, non-tax revenues during April-October FY21 stood at 30.2% as compared to 71.6% during April-October FY20.
- As per information sourced from the Department of Investment and Public Asset Management[7] on 22 December 2020, disinvestment receipts stood at INR12,380.28 crores, that is, 5.9% of the annual budgeted target of INR2,10,000 crores.

[5] Monthly accounts for September 2020 released on 27 November 2020
[6] IGST revenues are subject to final settlement
[7] https://www.dipam.gov.in/dipam/home

B. Expenditures: revenue and capital

- Center's total expenditure during April-October FY21 grew by only 0.4% as compared to a growth of 13.6% during the corresponding period of FY20.
- Revenue expenditure grew by a meagre 0.7% during April-October FY21 as compared to 13.6% during the corresponding period of FY20 (**Chart 5**).
- Center's capital expenditure showed a contraction of (-)1.9% during April-October FY21 as compared to a growth of 13.6% in the corresponding period of previous year.

Chart 5: growth in central expenditures during April-October (y-o-y, in %)



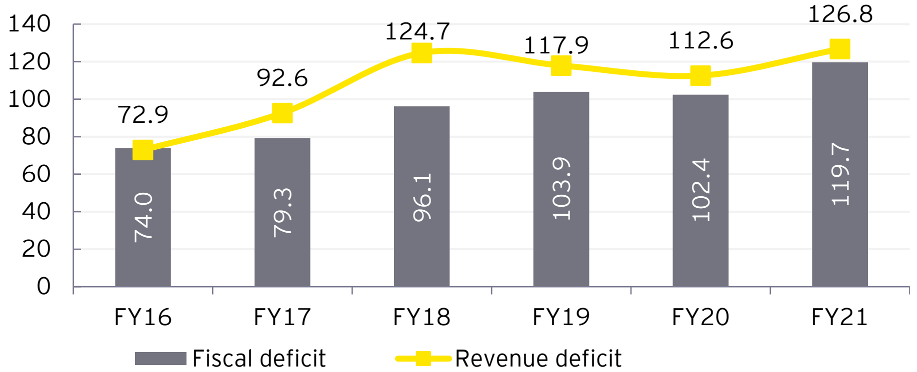
During April-October FY21, center's capital expenditure contracted by (-)1.9% while revenue expenditure showed a subdued growth of 0.7%.

Source (basic data): Monthly Accounts, Controller General of Accounts (CGA), Government of India

C. Fiscal imbalance

- Center's fiscal deficit during April-October FY21 stood at 119.7% of the annual budgeted target as compared to 102.4% during the corresponding period of FY20 (**Chart 6**).
- Center's revenue deficit during April-October FY21 stood at 126.8% of the annual budgeted target as compared to 112.6% in the corresponding period of FY20.
- In 1HFY21, center's fiscal and revenue deficits relative to GDP stood at 10.7% and 8.9% respectively.

Chart 6: fiscal and revenue deficit during April-October as percentage of annual budgeted target



During April-October FY21, center's fiscal deficit stood at 119.7% of the annual budgeted target while the corresponding number for revenue deficit was 126.8%.

Source: Monthly Accounts, Controller General of Accounts (CGA), Government of India.

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4. India in comparative perspective: GDP contraction of (-)10% and inflation of 6% projected in FY21

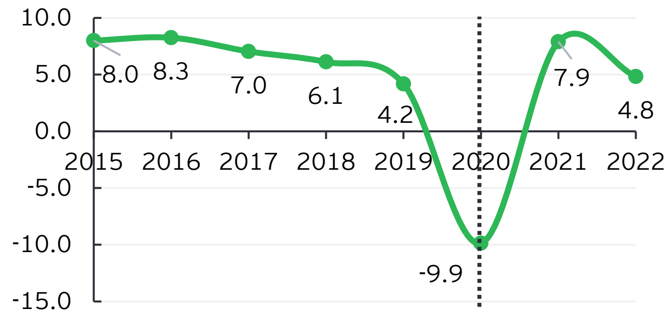
Real GDP growth

Table 2: real GDP growth (% annual)

	2019	2020	2021	2022
US	2.2	-3.7	3.2	3.5
UK	1.3	-11.2	4.2	4.1
Euro area	1.3	-7.5	3.6	3.3
Japan	0.7	-5.3	2.3	1.5
Brazil	1.1	-6.0	2.6	2.2
Russia	1.3	-4.3	2.8	2.2
India*	4.2	-9.9	7.9	4.8
China	6.1	1.8	8.0	4.9
S. Africa	0.2	-8.1	3.1	2.5
Global	**2.7**	**-4.2**	**4.2**	**3.7**

Source (basic data): OECD Economic Outlook, December 2020
*data pertains to fiscal year; actuals for 2019 and projections from 2020 onwards

Chart 7: India's real GDP growth (% annual)



- Global GDP is projected to contract by (-)4.2% in 2020 followed by a recovery thereafter (**Table 2**). By end-2021, the level of global output is projected to return to that at end-2019.
- Affected by the second wave of COVID-19, the UK and the Euro area are forecasted to contract sharply by (-)11.2% and (-)7.5% respectively in 2020. Recovery in the UK post 2020 is expected to be driven by a consumption rebound. In the Euro area, recovery post 2020 is projected to be milder with both private consumption and investment remaining affected by uncertainty and low confidence.
- In the US, after a contraction in 2020, growth is expected to increase to 3.2% in 2021 and further to 3.5% in 2022 helped by a substantial fiscal and monetary policy support.
- India's growth was slowing even before the Covid-19 shock. A sharp contraction of (-)9.9% is projected for India in 2020 followed by a growth of 7.9% in 2021 on a low base. Growth in 2022 is expected to remain below trend levels at 4.8% **(Chart 7)**. As per the OECD, GDP loss is expected to be substantial and it may take nearly two years for it to reach the pre-pandemic levels.
- China's growth is projected at 1.8% in 2020. Growth after 2020 at 8% in 2021 and 4.9% in 2022 is expected to be marginally higher than that in India.

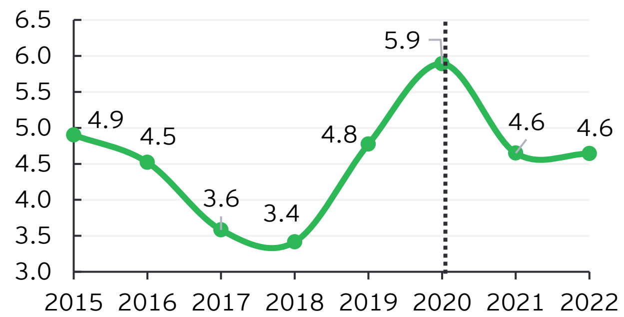
CPI inflation

Table 3: CPI inflation (% change)

	2019	2020	2021	2022
US	1.8	1.4	1.9	1.7
UK	1.8	0.8	0.7	1.5
Euro area	1.2	0.3	0.7	1.0
Japan	0.5	0.2	0.2	0.4
Brazil	3.7	2.7	2.5	3.2
Russia	4.5	3.3	4.1	4.1
India*	4.8	5.9	4.6	4.6
China	2.9	2.8	2.3	2.1
S. Africa	4.1	3.4	3.8	4.3

Source (basic data): OECD Economic Outlook, December 2020
*data pertains to fiscal year; actuals for 2019 and projections from 2020 onwards

Chart 8: India's CPI inflation (% change)



- In line with a slowdown in aggregate demand, CPI inflation is expected to fall in 2020 in all selected major economies except India. It is projected to converge to the pre-pandemic levels by end-2022 (**Table 3**).
- In selected AEs, CPI inflation in 2021 and 2022 is projected to remain well-below the respective central banks' target. In Japan, CPI inflation is projected to remain below 0.5% throughout the projection period.
- In the selected set of EMEs, CPI inflation is expected to remain below target during 2020 to 2022 with the exception of India. CPI inflation in India is projected at 5.9% in 2020 due to rising food prices and firming up of global crude prices **(Chart 8)**. Inflation in 2021 and 2022 is expected to continue to remain higher than the central bank's average target of 4%.

5. In focus: pursuing recovery - India's growth prospects in FY21 and beyond

Introduction

The release of 2QFY21 growth data by the CSO signals recovery of the Indian economy with a moderation of contraction in GDP in 2QFY21 as compared to 1QFY21. A key question now pertains to the extent of contraction that the Indian economy would end up with in FY21. The state of stimulus particularly fiscal stimulus remains inadequate. With CPI inflation running high, the monetary authorities have also indicated a preference for status quo. The Indian economy was facing significant challenges even prior to the onset of COVID. India should strategize emerging out not only from the impact of COVID but also reverse the adverse trends of investment and saving slowdown as well as a slowdown in the tax revenues relative to GDP over a longer period of time. In this write-up, we review demand and output trends and India's policy options faced with a significant erosion of government revenues.

Messages from 2QFY21 growth

The CSO released 2QFY21 national income aggregates on 27 November 2020 indicating that although the GDP contraction continued into 2QFY21, it was relatively moderate at (-)7.5% compared to the sharp fall of (-)23.9% in 1QFY21. The demand side of the GDP reflected continued weakness in both consumption and investment demand. Private final consumption expenditure (PFCE) which had contracted at an unprecedented rate of (-)26.7% in 1QFY21, recovered to some extent, showing a contraction of (-)11.3% in 2QFY21. The main disappointment came in the case of government final consumption expenditure (GFCE) where a deep contraction of (-)22.2% became visible in 2QFY21 from a positive growth of 16.4% in 1QFY21. Investment demand as measured by gross capital formation (GCF) showed a contraction of (-)8.9% in 2QFY21. We notice that investment demand has been in contraction for the last five quarters beginning 2QFY20. The maximum contraction was in 1QFY21 at (-)47.5% (**Table 4**).

In regard to the external sector, perhaps due to the implementation of Atmanirbhar Bharat, imports contracted faster than exports resulting into a positive contribution of net exports (NE) to GDP growth in both 1Q and 2Q of FY21 at 5.5% points and 3.4% points respectively.

Table 4: Real growth in output and aggregate demand components (%)

Agg. demand	*4Q FY18*	*4Q FY18*	*2Q FY19*	*3Q FY19*	*4Q FY19*	*1Q FY20*	*2Q FY20*	*3Q FY20*	*4Q FY20*	*1Q FY21*	*2Q FY21*
PFCE	8.1	6.7	8.8	7.0	6.2	5.5	6.4	6.6	2.7	-26.7	-11.3
GFCE	8.6	8.5	10.8	7.0	14.4	6.2	14.2	13.4	13.6	16.4	-22.2
GCF *of which*	15.2	10.8	11.4	11.5	5.0	5.3	-2.9	-4.3	-5.8	-47.5	-8.9
GFCF	*13.6*	*12.9*	*11.5*	*11.4*	*4.4*	*4.6*	*-3.9*	*-5.2*	*-6.5*	*-47.1*	*-7.3*
EXP	5.1	9.5	12.5	15.8	11.6	3.2	-2.2	-6.1	-8.5	-19.8	-1.5
IMP	23.6	5.9	18.7	10.0	0.8	2.1	-9.4	-12.4	-7.0	-40.4	-17.2
GDP	**8.2**	**7.1**	**6.2**	**5.6**	**5.7**	**5.2**	**4.4**	**4.1**	**3.1**	**-23.9**	**-7.5**
Output: major sectors											
Agr.	7.1	3.8	2.5	2.0	1.6	3.0	3.5	3.6	5.9	3.4	3.4
Ming.	3.3	-7.3	-7.0	-4.4	-4.8	4.7	-1.1	2.2	5.2	-23.3	-9.1
Mfg.	10.1	10.7	5.6	5.2	2.1	3.0	-0.6	-0.8	-1.4	-39.3	0.6
Elec.	11.8	7.9	9.9	9.5	5.5	8.8	3.9	-0.7	4.5	-7.0	4.4
Cons.	13.7	6.4	5.2	6.6	6.0	5.2	2.6	0.0	-2.2	-50.3	-8.6
Trans.	6.3	8.5	7.8	7.8	6.9	3.5	4.1	4.3	2.6	-47.0	-15.6
Fin.	4.4	6.0	6.5	6.5	8.7	6.0	6.0	3.3	2.4	-5.3	-8.1
Publ.	8.3	8.8	8.9	8.1	11.6	7.7	10.9	10.9	10.1	-10.3	-12.2
GVA	**7.6**	**6.9**	**6.1**	**5.6**	**5.6**	**4.8**	**4.3**	**3.5**	**3.0**	**-22.8**	**-7.0**

Source (basic data): MoSPI

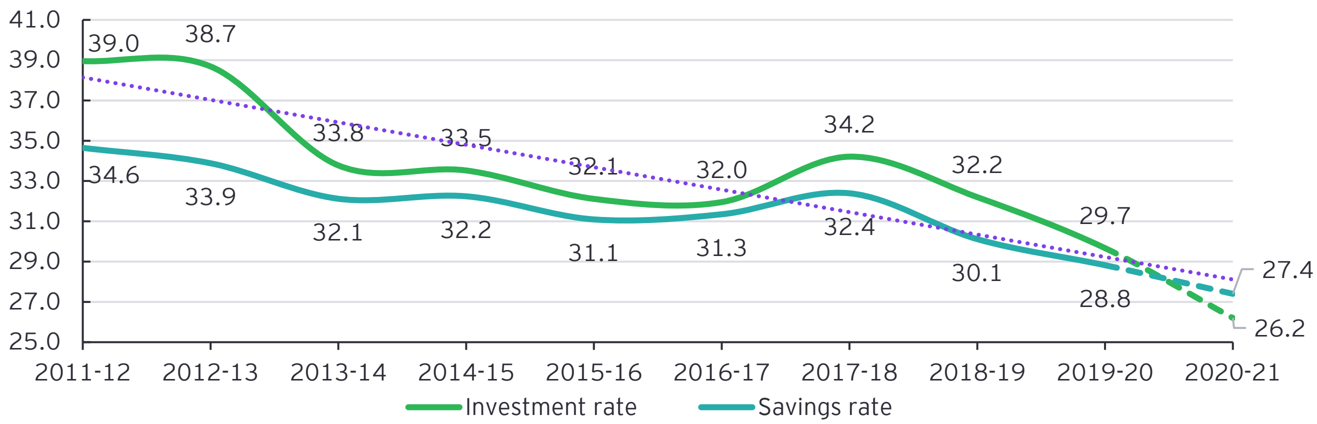
On the supply side, in 1QFY21, all output sectors except agriculture had contracted. The sharpest contraction was in construction ((-)50.3%), followed by trade, hotels, transport and communication services ((-)47.0%), and manufacturing ((-)39.3%). In 2QFY21, there was a welcome recovery in manufacturing and electricity, gas, and water supply that showed positive growth of 0.6% and 4.4% respectively, signaling the beginning of a V-shaped recovery. The main disappointment was the contraction in public administration, defence and other services. This contraction accentuated to (-)12.2% in 2QFY21 from (-)10.3% in 1QFY21, indicating weakness of fiscal stimulus.

The Monetary Policy Statement issued on 4 December 2020 by the RBI assesses mild positive GDP growth rates of 0.1% and 0.7% in 3Q and 4Q of FY21 respectively. These together with the CSO's real GDP growth estimates of 1Q and 2QFY21 at (-)23.9% and (-)7.5%, take the estimate of contraction in real GDP to (-)7.5% in FY21. This implies that the large contraction in 1QFY21 would be roughly neutralized by mild recovery in the 3Q and 4QFY21. With the likelihood of a strong base effect in 4QFY21, the recovery in this quarter may turn out to be higher than what is being expected by the RBI, particularly if fiscal support gathers momentum January 2021 onwards.

Erosion of long-term saving and investment rates

The Indian economy has been placed in a far more difficult situation than many other emerging market economies (EMEs) because economic crisis in India precedes the COVID shock. Its main long-term weakness is reflected in a fall in the investment and savings rate on trend basis. Investment rate has fallen from a peak of 39% in FY12 to 29.7% in FY20, its lowest level since FY12, and is projected to fall further to 26.2% in FY21 (median forecast from RBI's Professional Forecasters Survey - December 2020). Savings rate fell from 34.6% in FY12 to 28.8% in FY20, which is projected to fall further to 27.4% in FY21, assuming a current account surplus of 1.2% of GDP for FY21 **(Chart 9)**. In 1HFY21, real gross capital formation contracted by (-)29.0%. During this period, the investment rate (GCF relative to GDP) was at 25.2% and the savings rate is estimated at around 27.5%. Unless the savings and investment rates improve, India will continue to show GDP growth well below its potential. In fact, if investment rate is limited to about 26%, it will show up in a GDP growth of less than 6% whereas the potential growth is estimated at over 7.5%[8].

Chart 9: trends in savings and investment (as % of GDP)



Source (basic data): MoSPI
Note: Gross savings are estimated to rise above the investment rate to 27.4%, assuming a current account surplus of 1.2% for FY21 (projections for 2020-21 are median forecast from RBI's Professional Forecasters Survey - December 2020)

Fiscal policy constraints

Fiscal policy plays a key role both in terms of overcoming short-term crises and affecting the longer-term growth performance. This is so because fiscal stimulus enables coping with slowdowns and recessions whereas the level of fiscal deficit relative to GDP determines government savings and sustainable levels of debt-GDP ratio. India's fiscal stimulus in the face of the COVID crisis has proved to be quite inadequate. The main reason for this is the erosion in center's gross tax revenues, which contracted by (-)16.8% during the first seven months of FY21 **(Table 5)**. Center's non-tax revenues also showed a contraction of (-)48.2% during this period. In spite of increasing fiscal deficit relative to the FRBM norms to some extent, revenue and capital expenditures grew much below trend growth in the first seven months of FY21. Centre's revenue expenditure grew only by 0.7% in the

[8] Rangarajan, C., and D. K. Srivastava (2017). Underlying Drivers of India's Potential Growth. Economic & Political Weekly 52.25-26 (2017): 69-77.

first seven months of FY21 as compared to an average growth of 12.3% in the corresponding period of the last three years. In the case of capital expenditure, there was a contraction of (-)1.9% during this seven-month period as compared to an average growth of 17.6% in the corresponding period of last three years. Center's fiscal deficit during April-October FY21 was close to 120% of the annual budgeted target.

Table 5: center's fiscal position so far in FY21

Fiscal aggregate	Amount in 1HFY21 as a proportion of GDP (%)	Growth during Apr-Oct FY21 over Apr-Oct FY20 (%)	Amount in Apr-Oct FY21 as a proportion of FY21 budget target (%)
Receipts			
Centre's gross tax revenues *of which*	8.5	-16.8	36.1
Direct taxes	3.7	-27.3	28.5
Indirect taxes	4.6	-7.0	44.6
Non-tax revenues	1.1	-48.2	30.2
Non-debt capital receipts (including disinvestment)	0.2	-38.9	7.3
Expenditures			
Total expenditure *of which*	17.3	0.4	54.6
Revenue expenditure	15.4	0.7	55.7
Capital expenditure	1.9	-1.9	47.9
Deficits			
Fiscal deficit	10.7	32.3	119.7
Revenue deficit	8.9	41.4	126.8

Source (basic data): CGA, MoSPI

The fiscal position of states has been equally weak. In their case, considering available data for 20 states from the CAG, capital expenditure contracted sharply by (-)35.1% during 1HFY21 **(Table 6)**. Revenue expenditure of these states showed a subdued growth of 0.08% during this period. The fiscal deficit of these 20 states in 1HFY21 is estimated to be 4.5% of the sum of estimated GSDPs of these 20 states in the first half of the fiscal year[9]. This implies that these states have not fully used the flexibility in fiscal deficit which was provided to them by the central government to go up to 5% of their respective GSDPs subject to certain conditions. Had they been more proactive in supporting demand particularly through capital expenditure, they could have borrowed more in 1HFY21 during the unprecedented crisis.

Table 6: states' fiscal position so far in FY21

Fiscal aggregate	Growth in 1HFY20 over 1HFY19 (%)	Growth in 1HFY21 over 1HFY20 (%)	Amount in 1HFY20 as a proportion of FY20 budget target (%)	Amount in 1HFY21 as a proportion of FY21 budget target (%)
Receipts				
Tax revenues	3.0	**-21.4**	39.7	**30.7**
Own tax revenues	--	**-23.0**	44.0	**31.9**
Share in central taxes	--	**-17.7**	16.0	**12.9**
Non-tax revenues	-7.8	**-26.7**	9.5	**6.4**
Expenditures				
Total expenditure *of which*	7.1	**-3.9**	38.7	**35.6**
Revenue expenditure	8.2	**0.08**	40.4	**38.4**
Capital expenditure	-0.5	**-35.1**	29.4	**18.9**
Deficits as percent of estimated GSDP (1HFY21) of 20 states*				
Revenue deficit (20 states)	**3.2%**			
Fiscal deficit (20 states)	**4.5%**			

Source (basic data): CAG, MoSPI
Notes: *pertains to states for which CAG data on fiscal parameters was available. These states included most of the large states such as Andhra Pradesh, Haryana, Karnataka, Kerala, Madhya Pradesh, Tamil Nadu, Telangana, Uttar Pradesh and West Bengal.

[9] The sum of GSDPs of these 20 states accounted for about 77% of the national GDP in FY19.

Inflation experience: status quo in monetary policy

The monetary authorities, in the initial period of the crisis appeared to be more proactive in providing stimulus. They reduced the repo rate from 5.15% in February 2020 in two steps to 4.0% in May 2020. A variety of other liquidity enhancing measures were also undertaken. However, as CPI inflation started firming up, the monetary authorities became less active in further strengthening monetary stimulus.

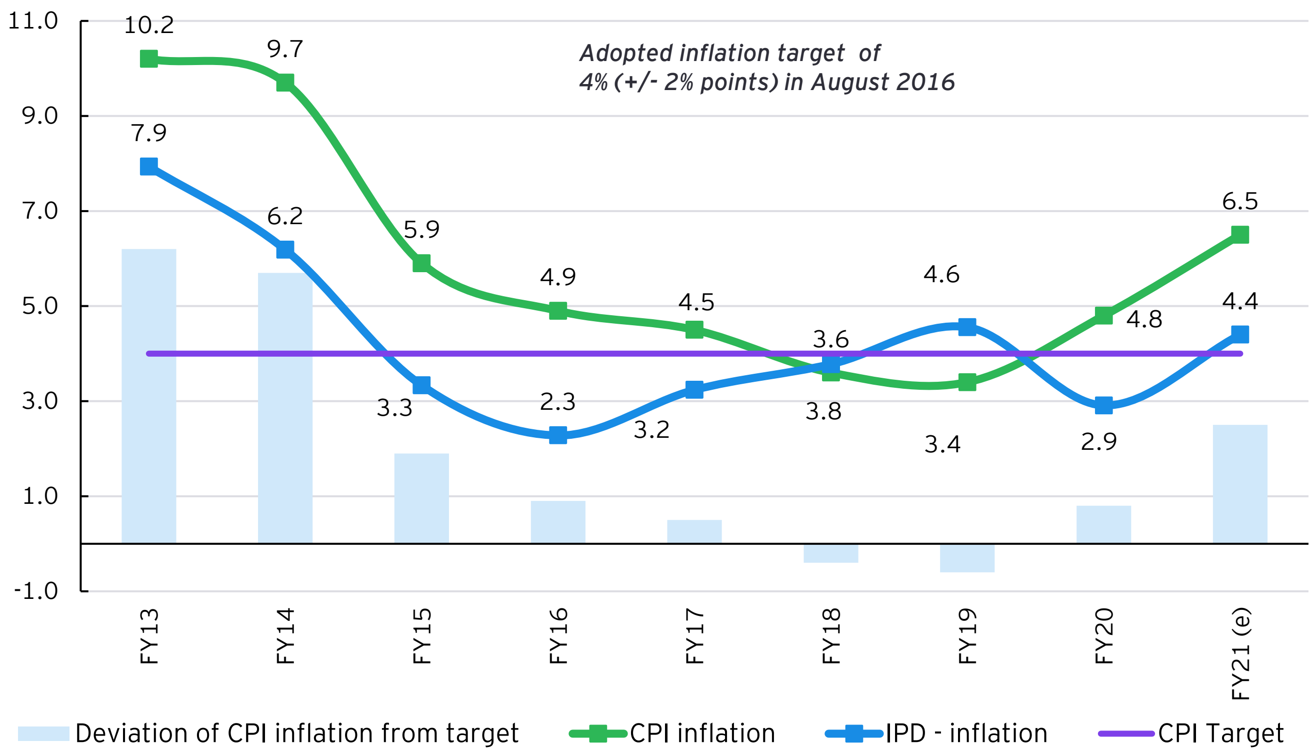
CPI inflation breached the upper tolerance limit of 6% of RBI's inflation target in 4QFY20, 1Q and 2Q of FY21. In October and November 2020, it has remained high at 7.6% and 6.9% respectively. With inflation expectations remaining well above 6% for FY21, the monetary authorities are firmly placed in a status quo mode for the rest of the year. The MPC in its meeting on 4 December 2020 has retained the repo rate at 4.0% with an accommodative policy stance. International crude prices have started firming up with global demand gaining strength and oil producers beginning to implement supply cuts.

In RBI's assessment, CPI inflation for FY21 as a whole is close to 6.5%. The upper ceiling of 6% has been breached in the first two quarters and is projected to be breached in the third quarter as well. In 4QFY21, RBI projects CPI inflation at 5.8%. This elevated level of inflation has been driven by cost push factors affecting food prices and lately prices of petroleum products. The RBI expects core inflation also to remain sticky. Given this sustained breach of the policy target, RBI is likely to maintain status quo, continuing to maintain the repo rate at 4% for the remaining part of the fiscal year although this situation may be reassessed in the next MPC meeting scheduled in February 2021 after the presentation of FY22 Union Budget.

Nominal GDP growth and tax buoyancy

Tax revenue growth and tax buoyancy is dependent upon both real GDP growth and GDP deflator-based inflation (IPD-based inflation). In recent years, a relationship between CPI inflation and the IPD-based inflation has been observed. CPI inflation exceeded the GDP deflator-based inflation by about 2.6% points on average during FY13 to FY21(e) excluding FY18 and FY19 **(Chart 10)**. The MPC has been tasked to maintain a CPI inflation in the range of 2-6% with a mean level of 4%. This implies that the IPD-based inflation may dip to about 2.5% or less thereby adversely affecting the nominal GDP growth. In fact, India's nominal GDP growth has fallen from 13.8% in FY13 to 7.2% in FY20. This has had a bearing on tax revenue growth as shown in **Chart 11**.

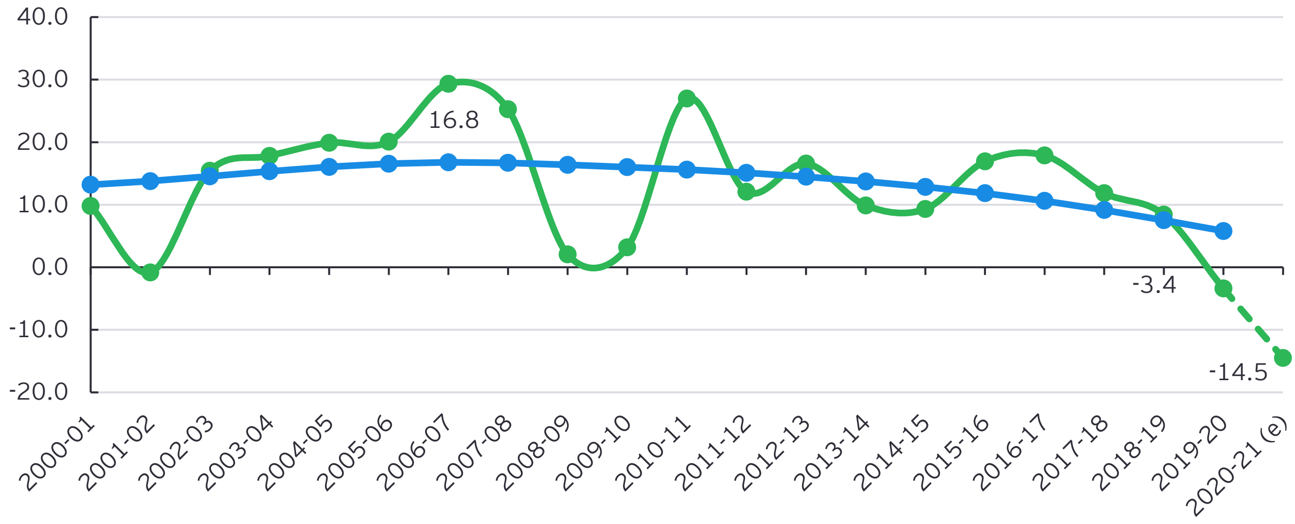
Chart 10: CPI inflation and IPD-based inflation (%)



Source (basic data): MoSPI, IMF, RBI
Note: FY21 CPI inflation estimate is as per the December Monetary Policy Statement and FY21 IPD based inflation is as per IMF's projection; (e) represents RBI's estimates

Trend growth rate in center's gross tax revenues has fallen from a peak of 16.8% in FY07 to 5.8% in FY20. Actual growth rate became negative at (-)3.4% in FY20. It has fallen to (-)16.7% in the first seven months of FY21. Fall in the trend growth of center's gross tax revenues is due to a fall in nominal GDP growth and a fall in buoyancy. This has led to a systematic erosion of fiscal space for the center.

Chart 11: center's gross tax revenues: actual and trend growth (%)

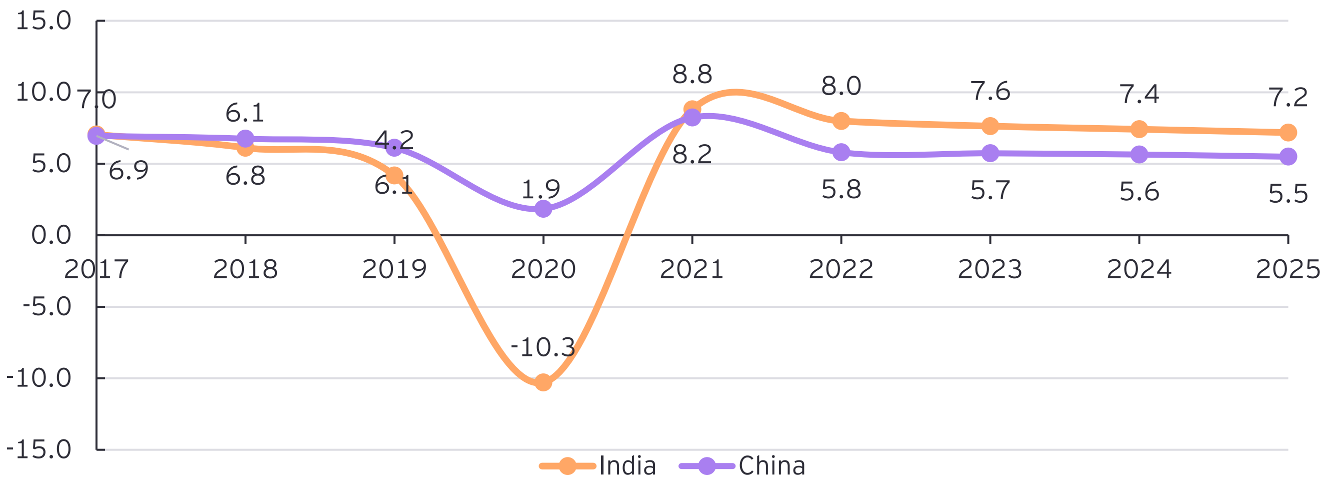


Source (basic data): CGA; (e) EY estimates

Analyzing short- and medium-term growth prospects

There is much discussion whether in the short-term, India's recovery would be V-shaped or it will assume some other known or unknown shape. Going by the IMF's projection, the recovery in 2021 (FY22) is clearly V-shaped with its trough in 2020 (FY21) estimated at real GDP growth of (-)10.3% **(Chart 12)**. These projections are from the IMF's World Economic Outlook released in October 2020. After the release of the 2QFY21 GDP data by the CSO, many analysts assess India's recovery to be better than IMF's assessment. For example, Rangarajan and Srivastava (2020)[10] assess the FY21 full year GDP growth to be in the range of (-)6.0 to (-)7.0%. Although China's recovery is also V-shaped, its trough is quite mild. In the medium-term, India is slated to overtake China in terms of growth performance exceeding China's GDP growth by an average margin of about 1.9% points.

Chart 12: real GDP growth projection (%): FY21 to FY26: India and China

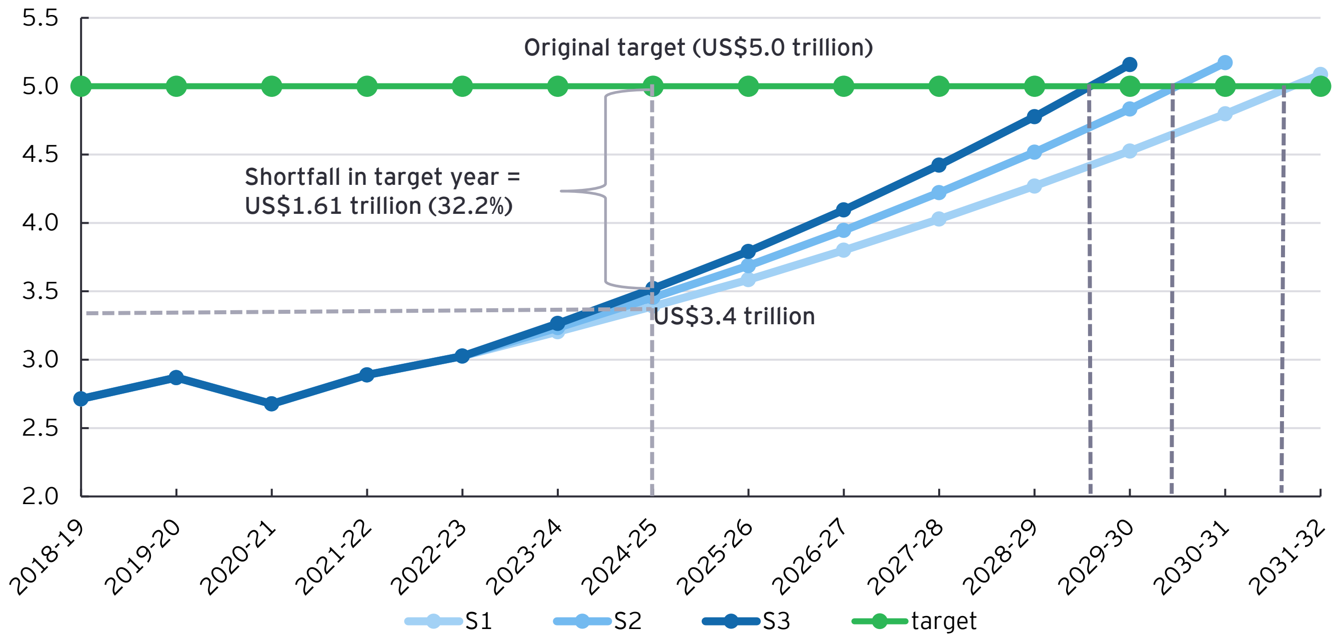


Source: WEO, IMF (October 2020)

[10] https://www.thehindubusinessline.com/opinion/fiscal-support-can-contain-gdp-contraction/article33233731.ece#:~:text=In%20order%20to%20ensure%20positive,may%20play%20a%20crucial%20role.&text=This%20amount%20is%20equal%20to,21%20as%20per%20the%20IMF

It is important to recognize that fiscal policy will play a key role if India is to uplift its growth to close to 8%. In particular, significant support to capital expenditure in line with the National Infrastructure Pipeline (NIP) may need to be provided where the central as well as the state governments, their public sector enterprises (PSEs) and the private sector may have to play a key role. We may also recognize that even if India achieves a real GDP growth rate in the range of 7 to 8% in the medium-term, we will experience delay in achieving the US$5 trillion target, which may be considered largely an outcome of the COVID shock. In **Chart 13**, we consider three simulations namely, S1, S2, and S3 corresponding with real GDP growth rates of 6%, 7%, and 8% respectively. These are applied from FY24 onwards. FY21 reflects the COVID shock, FY22, a very strong base effect and FY23 indicates a normalization of growth which is the base year. These three years are independently projected using the OECD projections (December 2020) as a reference point.

Chart 13: Expected slippage from the US$5 trillion target: simulations



Source (basic data): IMF, MoSPI, RBI, and EY estimates

The original year for reaching the US$5 trillion target was FY25 but by this time, the Indian economy would reach a size of US$3.4 trillion, missing the US$5 trillion target by US$1.6 trillion (S1). Taking a real growth rate of 7%, this target would be achieved in FY31 (S2). This is to say that the COVID shock, largely if not entirely, would have effectively delayed reaching the US$5 trillion target by six years (**Table 7**).

Table 7: India's nominal GDP levels (US$ trillion) under alternative simulations

Fiscal year	S1	S2	S3
Real GDP growth assumption	6%	7%	8%
FY20	2.9	2.9	2.9
FY21	2.7	2.7	2.7
FY22	2.9	2.9	2.9
FY23	3.0	3.0	3.0
FY24	3.2	3.2	3.3
FY25	3.4	3.5	3.5
FY26	3.6	3.7	3.8
FY27	3.8	3.9	4.1
FY28	4.0	4.2	4.4
FY29	4.3	4.5	4.8
FY30	4.5	4.8	5.2
FY31	4.8	5.2	5.6
FY32	5.1	5.5	6.0

Source: EY estimates
Note: FY23 indicates the base year on which the real GDP growth assumption is applied

Concluding observations

There is now a need to give a fresh start to India's growth momentum once the COVID shock subsides. A strong growth-supporting policy framework requires to be put in place, in which fiscal and monetary policies should play a critical role. In the August 2020 issue of Economy Watch, in the In-focus section entitled *"Is it time to recast India's fiscal and monetary policy frameworks?"*[11], we had argued that there may be a case for modifying India's FRBMA as well as the Monetary Policy Framework. In particular, there is a need to increase the combined government debt-GDP target to 70% from the current level of 60%. Further, the center may have to play a more active role both for supporting growth and for macro-stabilization, for which it may be given a higher limit of 4% of fiscal deficit relative to GDP, and a higher limit of 40% for debt relative to GDP. States may be allowed to continue at the present FRBM levels of 3% of fiscal deficit and 30% of debt relative to GDP. It was shown that these are internally consistent targets. This reform should be accompanied by a significant improvement in the tax-GDP ratio.

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[11] https://assets.ey.com/content/dam/ey-sites/ey-com/en_in/topics/tax/economy-watch/2020/08/economy-watch-august-2020.pdf

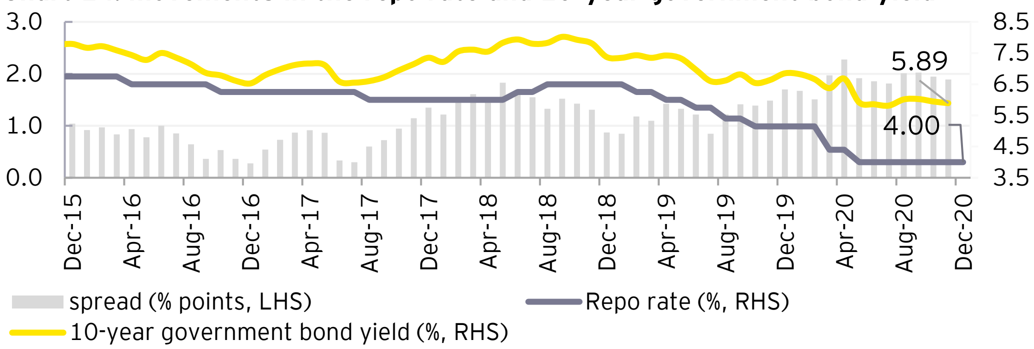
6. Money and finance: repo rate retained at 4.0% in the RBI's December 2020 monetary policy review

A. Monetary sector

Monetary policy

- The Monetary Policy Committee unanimously voted to retain the repo rate at 4.0% in its monetary policy review on 4 December 2020 as CPI inflation continued to remain at elevated levels **(Chart 14).** The RBI cited that a sustained surge in CPI inflation has limited the ability of monetary policy to support growth.
- The Monetary Policy Statement[12] observed that a substantial wedge between CPI and WPI inflation pointed to the presence of supply side bottlenecks and higher retailers' margins. In the RBI's assessment, CPI inflation outlook worsened in recent months. Although, prices of cereals and vegetables are likely to ease, prices of other food items may remain elevated. With regard to international crude oil prices, the RBI anticipates volatility in the near-term led by some recovery in demand and production cuts. Core inflation is also likely to remain elevated due to cost push pressures.

Chart 14: movements in the repo rate and 10-year government bond yield



Source: Database on Indian Economy, RBI

The RBI retained the repo rate at 4.0% in its December 2020 monetary policy review as CPI inflation remained elevated.

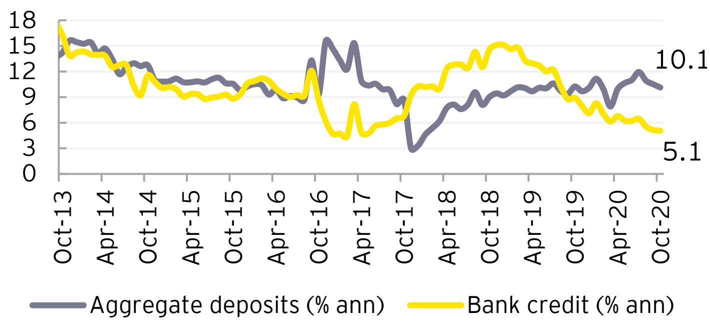
Money stock

- Growth in broad money stock (M3) increased to 12.5% in November 2020 from 11.6% in October 2020. This was due to a higher growth in narrow money (M1) and a marginal improvement in the growth of time deposits. Growth in time deposits was at 10.5% in November 2020 as compared to 10.0% in October 2020.
- Growth in narrow money (M1) increased to 19.0% in November 2020 from 16.8% in October 2020 due to increase in the growth of currency in circulation and demand deposits. Currency in circulation and demand deposits grew by 22.2% and 12.8% respectively in November 2020 as compared to 20.3% and 10.0% respectively in October 2020.

Aggregate credit and deposits

- Growth in bank credit continued to remain subdued at 5.1% in October 2020, similar to the level in September 2020 (**Chart 15**).
- Growth in non-food credit at 5.6% in October 2020 was the lowest since September 2017.
- Among the sectoral deployment of bank credit[13], outstanding credit to industry contracted by (-)1.7% in October 2020 as compared to zero growth in September 2020. Within the industrial sector, credit to infrastructure contracted by (-)2.0% in

Chart 15: growth in credit and deposits



Source: Database on Indian Economy, RBI

[12] Monetary Policy Statement, 2020-21 Resolution of the Monetary Policy Committee (MPC) December 2-4, 2020 dated 04 December 2020; https://www.rbi.org.in/Scripts/BS_PressReleaseDisplay.aspx?prid=50747

[13] As per RBI, data on sectoral deployment of bank credit collected from select 33 scheduled commercial banks accounts for about 90 per cent of the total non-food credit deployed by all scheduled commercial banks

October 2020 as compared to a growth of 1.1% in September 2020. Credit to iron and steel contracted for the fourth consecutive month by (-)7.8% in October 2020 as compared to (-)6.4% in September 2020. Credit to cement sector contracted for the third consecutive month by (-)4.6% in October 2020 as compared to (-)4.1% in September 2020.

- Credit growth to the services and agricultural sectors increased to 9.5% and 7.4% respectively in October 2020 from 9.1% and 5.9% in September 2020.
- Growth in personal loans, a key driver of retail loans, marginally increased to 9.3% in October 2020 from 9.2% in September 2020.
- Growth in aggregate bank deposits moderated to 10.1% in October 2020 as compared to 10.5% in September 2020.

B. Financial sector

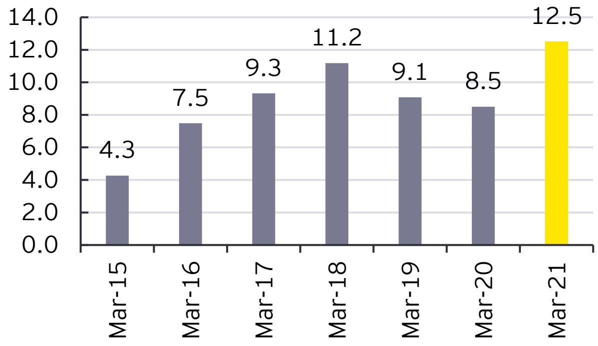
Interest rates

- As per the data released by the RBI on 15 December 2020, interest rates offered by commercial banks on term deposits with a maturity of more than one year averaged 5.20% in November 2020 (ranging from 4.90% to 5.50%) falling from 6.43% (ranging from 6.16% to 6.70%) in October 2020.
- The MCLR has fallen gradually from 7.74% in January 2020 to 6.86% in November 2020, a fall of only 88 basis points. On the contrary, interest rate on term deposits with a maturity of more than one year fell by 233 basis points during the same period.
- The average yield on 10-year government bond fell marginally to 5.89% in November 2020 from 5.95% in October 2020. In spite of RBI's continued interventions, the spread between benchmark bond yield and the repo rate continues to be sticky at around 200 basis points on average during April 2020 to November 2020 as compared to an average of 130 basis points during the corresponding period of previous year **(Chart 14)**.
- WALR on fresh rupee loans by SCBs increased to 8.38% in October 2020 from 8.29% in September 2020, despite RBI's decision to retain the repo rate at 4% in its October 2020 monetary policy review.

Gross non-performing assets ratio

- The RBI's July 2020 Financial Stability Report[14] estimates the scheduled commercial banks' (SCBs) gross non-performing assets (GNPA) ratio to increase to 12.5% by March 2021 under the baseline scenario (14.7% in a very severe stress scenario) from 8.5% in March 2020 **(Chart 16)**.
- GNPA ratio was earlier at 9.3% in September 2019.
- GNPA ratio of public sector banks continued to be the highest at 11.3% in March 2020, but lower than that in September 2019. In the case of private banks, this ratio was at 4.2% in March 2020, higher than its level of 3.9% in September 2019. For foreign banks, GNPA ratio was lower at 2.3% in March 2020 as compared to 2.9% in September 2019.
- Among major sectors, GNPA ratio in industries was the highest at 17.1% in March 2020, although marginally lower than 17.3% in September 2019. Among major sub-sectors within industry, GNPA ratios in construction and gems and jewelry sectors increased sharply to 24.8% and 24.3% respectively in March 2020. On the other hand, the infrastructure sector (13.1%), basic metals (16.2%) and electricity (13.5%) have shown a decline in their GNPA ratios in March 2020.
- In the case of services, GNPA ratio increased to 7.2% in March 2020 from 6.3% in September 2019 while in agriculture, it remained at 10.1% in March 2020, similar to the level in September 2019.

Chart 16: GNPA ratios of SCBs



Source: Database on Indian Economy, RBI

14 https://rbidocs.rbi.org.in/rdocs//PublicationReport/Pdfs/0FSRJULY2020C084CED43CD1447D80B4789F7E49E499.PDF

7. Trade and CAB: merchandise exports contracted by (-)8.7% in November 2020

A. CAB: current account posted a surplus of 3.9% of GDP in 1QFY21

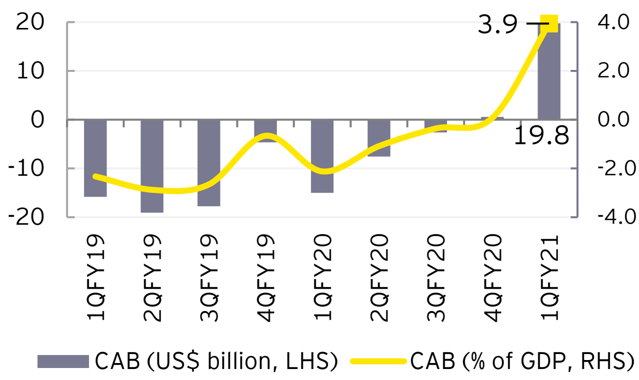
- Current account recorded a surplus of 3.9% of GDP in 1QFY21, the highest in 65 quarters **(Chart 17)** aided by lower merchandise trade deficit and higher net invisible receipts (**Table 8**). Merchandise imports relative to GDP fell to a 73-quarter low of 12.4% in 1QFY21 while merchandise exports were at 10.4%, the same level as it was in 4QFY20. Net invisible receipts improved significantly to 5.9% of GDP in 1QFY21 from 4.8% in 4QFY20. The improvement in CAB relative to GDP is partly attributable to a fall in the denominator arising from a sharp contraction in GDP in 1QFY21.

Table 8: components of CAB in US$ billion

Fiscal year	CAB as % of nominal GDP	CAB	Goods account net	Invisibles* net
FY17	-0.7	-15.3	-112.4	67.5
FY18	-1.8	-48.7	-160.0	77.6
FY19	-2.1	-57.3	-180.3	81.9
FY20	-0.9	-24.7	-157.5	84.9
2QFY20	-1.1	-7.6	-39.6	20.9
3QFY20	-0.4	-2.6	-36.0	21.9
4QFY20	0.1	0.6	-35.0	22.0
1QFY21	3.9	19.8	-10.0	20.5

Source: Database on Indian Economy, RBI
Note: (-) deficit; (+) surplus; *invisibles include services, current transfers and income components

Chart 17: CAB



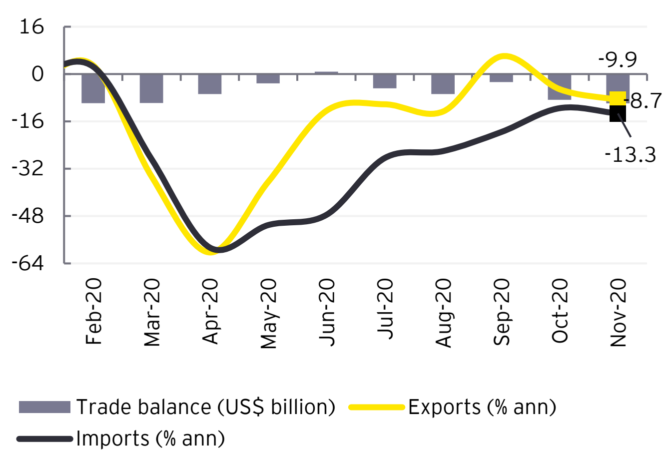
Source: Database on Indian Economy, RBI

B. Merchandise trade and exchange rate

Contraction in merchandise exports and imports increased to (-)8.7% and (-)13.3%, respectively, in November 2020.

- Merchandise exports contracted by (-)8.7% in November 2020 as compared to (-)5.1% in October 2020, led by an increase in contraction in oil and engineering goods exports **(Chart 18)**.

Chart 18: developments in merchandise trade



Source: Ministry of Commerce and Industry, GoI

- Exports of oil and engineering goods contracted by (-)59.7% and (-)8.1% respectively in November 2020 as compared to (-)52.0% and (-)3.7% respectively in October 2020.
- Non-oil non-gold exports contracted by (-)0.4% in November 2020 as compared to a growth of 6.5% in October 2020.
- The pace of contraction in merchandise imports increased to (-)13.3% in November 2020 from (-)11.5% in October 2020.
- Contraction in oil imports increased to (-)43.4% in November 2020 from (-)38.5% in October 2020.
- Imports excluding oil, gold and jewelry contracted for the sixteenth successive month, although at a slower pace of (-)1.2%, in November 2020.
- Out of the 30 sectors for which exports and imports data is provided, 11 and 19 sectors, respectively, experienced a contraction in November 2020 as compared to 10 and 19 sectors, respectively, in October 2020.
- Merchandise trade deficit rose to an eight-month high of US$9.9 billion in November 2020.
- The rupee depreciated to an average level of INR74.2 per US$ in November 2020 from INR73.5 per US$ in October 2020.

8. Global growth: OECD projected a global contraction of (-)4.2% in 2020

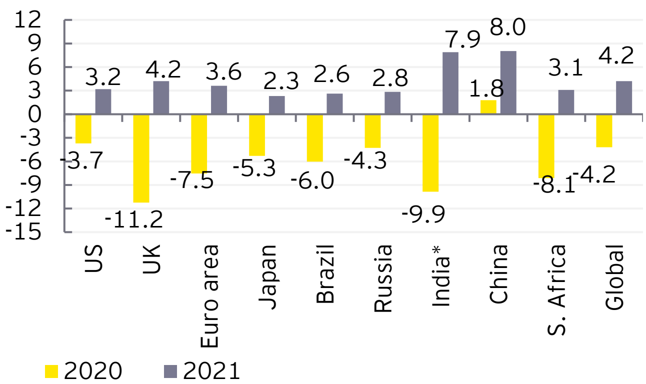
A. Global growth outlook

- The OECD (Economic Outlook, December 2020) has projected a global contraction of (-)4.2% in 2020 and a recovery of 4.2% in 2021 based on a) the assumption that the second COVID outbreak would remain contained and b) the prospect of a widely available vaccine towards end-2021 that would help support confidence (**Chart 19**).
- The OECD assessed that by end-2021, the magnitude of global GDP would reach the pre-crisis levels, helped by a strong recovery in China, but growth prospects differ significantly across major economies.
- In the US, a contraction of (-)3.7% is projected for 2020 followed by a growth of 3.2% in 2021 helped by an expected additional fiscal package in early 2021 and an accommodative monetary policy that would support activity particularly in the housing market.
- Severely impacted by the second wave of COVID-19, a sharp contraction of (-)11.2% is projected for the UK in 2020. Growth is projected to improve to 4.2% in 2021 driven by a consumption rebound while investment is expected to remain weak.
- A contraction of (-)7.5% in 2020 is forecasted for the Euro area reflecting the impact of a reintroduction of containment measures in most countries. Recovery is expected to remain moderate in 2021 and 2022.

The OECD projected a global contraction of (-)4.2% in 2020, with a contraction of (-)9.9% forecasted for India.

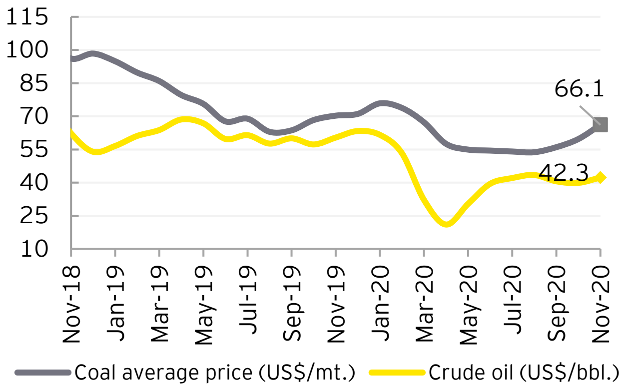
- Among selected EMEs, the sharpest contraction in 2020 is projected for India at (-)9.9%. The OECD assesses that there would be limited scope for additional fiscal measures and further reductions in policy interest rates would remain contingent on the inflation outlook. Growth is projected to increase to 7.9% in 2021 on a low base.
- China is projected to grow by 1.8% in 2020 and by 8.0% in 2021 led by strong investment in real estate and infrastructure, helped by policy stimulus and stronger credit growth, and improved export performance.

Chart 19: global growth projections (%)



Source: OECD Economic Outlook, December 2020
*data for India pertains to fiscal year

Chart 20: global crude and coal prices



Source (basic data): World Bank, Pink Sheet, December 2020

B. Global energy prices: global crude oil price increased in November 2020 as OPEC+ countries extended supply cuts

- Average global crude price[15] increased to US$42.3/bbl. in November 2020 from US$39.9/bbl. in October 2020 (**Chart 20**) due to the OPEC+ agreement on supply cuts. Beginning January 2021, these countries have decided to reduce production by 0.5 mb/d to 7.2 mb/d[16]. However, subdued demand particularly in Europe and America may put downward pressure on crude prices.
- Average global coal price[17] continued to increase, reaching an eight-month high of US$66.1/mt. in November 2020 from US$59.7/mt. in October 2020. As per the World Bank[15], coal production is expected to remain subdued and global coal price is projected at US$57.2/mt. in 2020 and at US$57.8/mt. in 2021.

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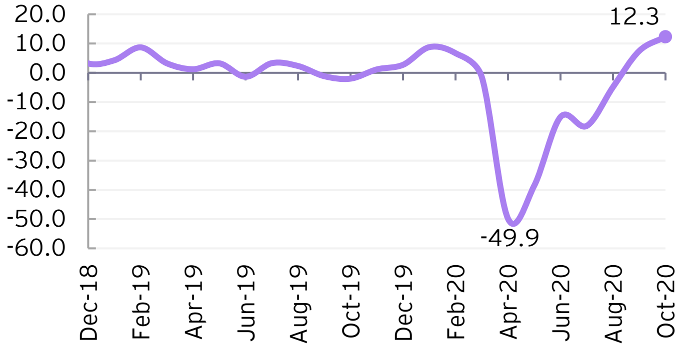
[15] Simple average of three spot prices, namely, Dated Brent, West Texas Intermediate and Dubai Fateh
[16] https://www.opec.org/opec_web/en/press_room/6257.htm
[17] Simple average of Australian and South African coal prices

9. Index of Aggregate demand (IAD): grew at a faster pace of 12.3% in October 2020

IAD grew by 12.3% in October 2020 as compared to 7.5% in September 2020

- EY developed an IAD to reflect the monthly combined demand conditions in the agriculture, manufacturing and services sectors. It considers the movements in PMI for manufacturing and services, both measured in non-seasonally adjusted terms, tracing the demand conditions in these sectors. Demand conditions in the agricultural sector have been captured by movements in monthly agricultural credit off-take.
- IAD posted a growth of 12.3% for the second consecutive month in October 2020 as compared to 7.5% in September 2020 (**Chart 21**). This pickup may be attributable partly to the festive demand and partly to a favorable base effect.
- All the key sectors of the economy namely agriculture, industry and services witnessed an improvement in demand conditions during October 2020 **(Table 9).**

Chart 21: growth in IAD (y-o-y)



Source (Basic data): IHS Markit PMI, RBI and EY estimates

Table 9: IAD

Month	Feb-20	Mar-20	Apr-20	May-20	Jun-20	Jul-20	Aug-20	Sep-20	Oct-20
IAD	137.9	126.2	63.5	77.5	107.9	106.2	118.5	133.4	141.7
Growth (% y-o-y)	6.7	-1.4	-49.9	-38.5	-15.1	-18.2	-4.9	7.5	12.3
Growth in agr. credit	5.8	4.2	3.9	3.5	2.4	5.4	4.9	5.9	7.4
Mfg. PMI**	4.7	1.7	-23.9	-16.5	-3.2	-4.9	2.1	8.0	9.4
Ser. PMI**	9.0	-1.1	-48.0	-38.4	-16.4	-17.7	-9.7	0.5	7.2

**Values here indicate deviation from the benchmark value of 50. A positive value indicates expansion in demand while a negative value implies contraction in demand; PMI for Mfg. and Serv. are non-seasonally adjusted.
Source (basic data): IHS Markit PMI, RBI and EY estimates

10. Capturing macro-fiscal trends: data appendix

Table A1: industrial growth indicators (annual, quarterly and monthly growth rates, y-o-y)

Fiscal year/ quarter/ month	IIP	Mining	Manufacturing	Electricity	Core IIP	Fiscal year/ quarter /month	PMI mfg.	PMI ser.
	% change y-o-y							
FY17	4.6	5.3	4.3	5.8	4.8	FY17	51.6	51.0
FY18	4.4	2.3	4.7	5.3	4.3	FY18	51.5	50.0
FY19	3.8	2.8	3.8	5.2	4.4	FY19	52.8	52.2
FY20	-0.8	1.6	-1.4	0.9	0.4	FY20	52.3	51.9
3QFY20	-1.4	0.0	-1.1	-6.0	-0.6	3QFY20	51.5	51.7
4QFY20	-4.3	3.9	-6.3	1.6	-0.4	4QFY20	53.9	54.1
1QFY21	-35.6	-22.3	-40.3	-15.8	-23.8	1QFY21	35.1	17.2
2QFY21	-5.9	-7.1	-6.6	0.1	-5.2	2QFY21	51.6	41.9
Jul-20	-10.5	-12.7	-11.4	-2.5	-7.6	Aug-20	52.0	41.8
Aug-20	-7.4	-9.0	-7.9	-1.8	-7.3	Sep-20	56.8	49.8
Sep-20	0.5	1.4	-0.2	4.9	-0.1	Oct-20	58.9	54.1
Oct-20	3.6	-1.5	3.5	11.2	-2.5	Nov-20	56.3	53.7

Source: Office of the Economic Adviser, Ministry of Commerce and Industry and IHS Markit Economics

Table A2: inflation indicators (annual, quarterly and monthly growth rates, y-o-y)

Fiscal year/ quarter/ month	CPI	Food Price Index	Fuel and light	Core CPI	WPI	Food Price Index	Mfg. products	Fuel and power	Core WPI
	% change y-o-y				% change y-o-y				
FY17	4.5	4.2	3.3	4.9	1.7	5.9	1.3	-0.3	-0.1
FY18	3.6	1.8	6.2	4.6	2.9	1.9	2.7	8.2	3.0
FY19	3.4	0.1	5.7	5.5	4.3	0.6	3.7	11.5	4.2
FY20	4.8	6.7	1.3	3.8	1.7	6.9	0.3	-1.8	-0.4
3QFY20	5.8	10.7	-1.1	3.3	1.1	9.3	-0.7	-5.1	-1.8
4QFY20	6.7	11.1	5.5	3.8	2.1	7.5	0.5	1.8	-0.7
1QFY21	6.6	9.9	1.7	4.9	-2.3	3.4	0.0	-17.4	-1.0
2QFY21	6.9	9.7	2.9	5.4	0.5	5.5	1.3	-9.2	0.5
Aug-20	6.7	9.1	3.2	5.4	0.4	4.8	1.4	-9.1	0.6
Sep-20	7.3	10.7	2.8	5.3	1.3	7.2	1.9	-8.6	1.3
Oct-20	7.6	11.0	2.1	5.8	1.5	5.8	2.1	-10.9	1.7
Nov-20	6.9	9.4	1.9	5.7	1.6	4.3	3.0	-9.9	2.6

Source: Office of the Economic Adviser, Ministry of Commerce and Industry and MoSPI
* The CPI for April and May 2020 has been imputed

Table A3: fiscal indicators (annual growth rates, cumulated monthly growth rates, y-o-y)

Fiscal year/month	Gross tax revenue	Corporate tax	Income tax	Direct taxes*	Indirect taxes**	Fiscal deficit % of GDP	Revenue deficit % of GDP
FY17 (CGA)	17.9	6.7	21.5	12.3	21.6	3.5	2.1
FY 18 (CGA)	11.8	17.8	19.9	18.6	6.0	3.5	2.6
FY 19 (CGA)	8.4	16.2	13.1	14.9	2.9	3.4	2.4
FY20 (CGA)	-3.4	-16.1	4.0	-7.8	1.7	4.6	3.3
FY 21 (BE over FY 20 RE)	12.0	11.5	14.0	12.7	11.1	3.5	2.7
	Cumulated growth (%, y-o-y)					% of budgeted target	
Mar-20	-3.4	-16.1	4.0	-7.8	1.7	122.0	133.6
Apr-20	-44.3	57.7	-32.1	-10.8	-69.9	35.1	41.3
May-20	-41.2	1408.1	-41.0	-14.6	-52.5	58.6	67.6
Jun-20	-32.6	-23.3	-35.9	-30.6	-34.5	83.2	94.8
Jul-20	-29.5	-39.2	-29.1	-33.2	-27.5	103.1	117.4
Aug-20	-23.7	-41.8	-28.9	-34.1	-16.5	109.3	121.9
Sep-20	-21.6	-39.7	-21.8	-31.4	-12.0	114.8	125.2
Oct-20	-16.8	-36.7	-16.9	-27.3	-7.0	119.7	126.8

Source: Monthly Accounts, Controller General of Accounts, Government of India, Union Budget documents
* Includes corporation tax and income tax
** Includes customs duty, excise duty, service tax, CGST, UTGST, IGST and GST compensation cess.
#: as % of revised targets for FY20.

Fiscal year/month	CGST	UTGST	IGST	GST compensation cess	Total GST (center)
	INR crore				
FY 2020 (RE)	5,14,000	-	-	98,327	6,12,327
FY 2021 (BE)	5,80,000	-	-	1,10,500	6,90,500
Monthly tax collection (INR crore)					
Mar-20	40,159	447	2,373	8,089	51,068
Apr-20	5,934	34	9,749	990	16,707
May-20	18,961	107	9,643	6,020	34,731
Jun-20	30,152	154	9,672	7,472	47,450
Jul-20	37,902	224	-6,026	6,816	38,916
Aug-20	32,359	191	5,198	6,856	44,604
Sep-20	37,171	243	-290	6,810	43,934
Oct-20	42,901	136	192	7,840	51,069

Source: Monthly Accounts, Controller General of Accounts, Government of India, Union Budget documents
Note: IGST revenues are subject to final settlement.

Table A4: monetary and financial indicators (annual, quarterly and monthly growth rates, y-o-y)

Fiscal year/ month	Repo rate (end of period)	Fiscal year/ quarter/ month	Bank credit	Agg. deposits	Net FDI	Net FPI	Fiscal year/ quarter/ month	M1	M3	10-year govt. bond yield	FX reserves
	%		% change y-o-y		US$ billion			% change y-o-y		%	US$ billion
Jan-20	5.15	FY17	7.9	11.6	35.6	7.6	FY17	3.1	10.1	7.03	370.0
Feb-20	5.15	FY18	7.5	7.5	30.3	22.1	FY18	21.8	9.2	7.05	424.4
Mar-20	4.40	FY19	13.7	8.9	30.7	-0.6	FY19	13.6	10.5	7.68	411.9
Apr-20	4.40	FY20	9.4	9.9	43.0	1.4	FY20	11.2	8.9	6.80	475.6
May-20	4.00	3QFY20	8.0	10.0	9.7	7.8	3QFY20	12.5	10.4	6.68	457.5
Jun-20	4.00	4QFY20	7.1	9.6	12.0	-13.7	4QFY20	11.2	8.9	6.62	475.6
Jul-20	4.00	1QFY20	6.4	10.5	3.6	1.4	1QFY21	17.7	12.3	6.15	506.8
Aug-20	4.00	2QFY20	5.7	11.1	23.3	7.3	2QFY21	18.6	12.2	5.95	542.0
Sep-20	4.00	Jul-20	6.5	11.9	3.2	1.2	Aug-20	19.2	12.6	6.01	541.4
Oct-20	4.00	Aug-20	5.5	10.9	17.7	6.8	Sep-20	18.6	12.2	6.03	542.0
Nov-20	4.00	Sep-20	5.1	10.5	2.4	-0.7	Oct-20	16.8	11.6	5.95	560.7
Dec-20	4.00	Oct-20	5.1	10.1	4.6	2.9	Nov-20	19.0	12.5	5.89	574.8

Source: Database on Indian Economy - RBI

Table A5: external trade and global growth

External trade indicators (annual, quarterly and monthly growth rates)							Global growth (annual)			
Fiscal year/ quarter/ month	Exports	Imports	Trade balance	Ex. rate (avg.)	Crude prices (avg.)	Coal prices (avg.)	Calendar year	World GDP	Adv. econ.	Emer. econ.
	% change y-o-y		US$ billion	INR/US$	US$/bbl.	US$/mt		% change y-o-y		
FY17	5.1	0.9	-108.2	67.1	47.9	73.0	2010	5.4	3.1	7.4
FY18	10.6	20.9	-159.0	64.5	55.7	90.8	2011	4.3	1.8	6.4
FY19	8.6	10.6	-182.3	69.9	67.3	100.4	2012	3.5	1.2	5.4
FY20	-5.0	-8.5	-155.5	70.9	58.5	70.4	2013	3.5	1.4	5.1
3QFY20	-1.5	-11.9	-35.8	71.2	60.3	69.9	2014	3.5	2.1	4.7
4QFY20	-12.8	-9.8	-34.8	72.4	49.1	72.3	2015	3.4	2.4	4.3
1QFY21	-36.7	-52.4	-9.1	75.9	30.3	55.7	2016	3.3	1.8	4.5
2QFY21	-5.6	-24.8	-14.3	74.4	42.0	54.6	2017	3.8	2.5	4.8
Aug-20	-12.7	-26.0	-6.8	74.7	43.4	53.8	2018	3.5	2.2	4.5
Sep-20	6.0	-19.6	-2.7	73.5	40.6	56.0	2019	2.8	1.7	3.7
Oct-20	-5.1	-11.5	-8.7	73.5	39.9	59.7	2020*	-4.4	-5.8	-3.3
Nov-20	-8.7	-13.3	-9.9	74.2	42.3	66.1	2021*	5.2	3.9	6.0

Source: Database on Indian Economy - RBI, Pink Sheet - World Bank and IMF World Economic Outlook, October 2020.
* Indicates projections.

Table A6: macroeconomic aggregates (annual and quarterly real growth rates, % change y-o-y)

Fiscal year/quarter	Output: Major sectors									IPD inflation
	GVA	Agr.	Ming.	Mfg.	Elec.	Cons.	Trans.	Fin.	Publ.	GVA
FY17 (3rd RE)	8.0	6.8	9.8	7.9	10.0	5.9	7.7	8.6	9.3	2.9
FY18 (2nd RE)	6.6	5.9	4.9	6.6	11.2	5.0	7.6	4.7	9.9	4.2
FY19 (1st RE)	6.0	2.4	-5.8	5.7	8.2	6.1	7.7	6.8	9.4	4.2
FY20 (PE)$	3.9	4.0	3.1	0.0	4.1	1.3	3.6	4.6	10.0	3.0
2QFY19	6.1	2.5	-7.0	5.6	9.9	5.2	7.8	6.5	8.9	4.7
3QFY19	5.6	2.0	-4.4	5.2	9.5	6.6	7.8	6.5	8.1	3.8
4QFY19	5.6	1.6	-4.8	2.1	5.5	6.0	6.9	8.7	11.6	3.7
1QFY20	4.8	3.0	4.7	3.0	8.8	5.2	3.5	6.0	7.7	3.1
2QFY20	4.3	3.5	-1.1	-0.6	3.9	2.6	4.1	6.0	10.9	1.8
3QFY20	3.5	3.6	2.2	-0.8	-0.7	0.0	4.3	3.3	10.9	3.4
4QFY20	3.0	5.9	5.2	-1.4	4.5	-2.2	2.6	2.4	10.1	3.7
1QFY21	-22.8	3.4	-23.3	-39.3	-7.0	-50.3	-47.0	-5.3	-10.3	2.9
2QFY21	-7.0	3.4	-9.1	0.6	4.4	-8.6	-15.6	-8.1	-12.2	3.1

Source: National Accounts Statistics, MoSPI
$ Growth numbers for FY20 are based on the provisional estimates of NAS released by the MoSPI on 29 May 2020 over the first revised estimates (RE) of NAS for FY19 released by the MoSPI on 31 January 2020.

Fiscal year/quarter	Expenditure components						IPD inflation
	GDP	PFCE	GFCE	GFCF	EX	IM	GDP
FY17 (3rd RE)	8.3	8.1	6.1	8.5	5.0	4.4	3.2
FY18 (2nd RE)	7.0	7.0	11.8	7.2	4.6	17.4	3.8
FY19 (1st RE)	6.1	7.2	10.1	9.8	12.3	8.6	4.6
FY20 (PE)$	4.2	5.3	11.8	-2.8	-3.6	-6.8	2.9
2QFY19	6.2	8.8	10.8	11.5	12.5	18.7	4.9
3QFY19	5.6	7.0	7.0	11.4	15.8	10.0	5.5
4QFY19	5.7	6.2	14.4	4.4	11.6	0.8	2.1
1QFY20	5.2	5.5	6.2	4.6	3.2	2.1	2.7
2QFY20	4.4	6.4	14.2	-3.9	-2.2	-9.4	1.4
3QFY20	4.1	6.6	13.4	-5.2	-6.1	-12.4	3.2
4QFY20	3.1	2.7	13.6	-6.5	-8.5	-7.0	4.3
1QFY21	-23.9	-26.7	16.4	-47.1	-19.8	-40.4	1.8
2QFY21	-7.5	-11.3	-22.2	-7.3	-1.5	-17.2	3.8

Source: National Accounts Statistics, MoSPI
$Growth numbers for FY20 are based on the provisional estimates of NAS released by **the** MoSPI on 29 May 2020 over the first revised estimates (RE) of NAS for FY19 released by the MoSPI on 31 January 2020

List of abbreviations

Sr. no.	Abbreviations	Description
1	AD	aggregate demand
2	AEs	advanced economies
3	Agr.	agriculture, forestry and fishing
4	AY	assessment year
5	Bcm	billion cubic meters
6	bbl.	barrel
7	BE	budget estimate
8	CAB	current account balance
9	CGA	Comptroller General of Accounts
10	CGST	Central Goods and Services Tax
11	CIT	corporate income tax
12	Cons.	construction
13	CPI	Consumer Price Index
14	Covid-19	Coronavirus disease 2019
15	CPSE	central public-sector enterprise
16	CRAR	Credit to Risk- weighted Assets Ratio
17	CSO	Central Statistical Organization
18	Disc.	discrepancies
19	ECBs	external commercial borrowings
20	EIA	US Energy Information Administration
21	Elec.	electricity, gas, water supply and other utility services
22	EMDEs	Emerging Market and Developing Economies
23	EXP	exports
24	FAE	first advanced estimates
25	FC	Finance Commission
26	FII	foreign investment inflows
27	Fin.	financial, real estate and professional services
28	FPI	foreign portfolio investment
29	FRBMA	Fiscal Responsibility and Budget Management Act
30	FY	fiscal year (April–March)
31	GDP	Gross Domestic Product
32	GFCE	government final consumption expenditure
33	GFCF	gross fixed capital formation
34	GoI	Government of India
35	G-secs	government securities
36	GST	Goods and Services Tax
37	GVA	gross value added

Sr. no.	Abbreviations	Description
38	IAD	Index of Aggregate Demand
39	IBE	interim budget estimates
40	ICRIER	Indian Council for Research on International Economic Relations
41	IEA	International Energy Agency
42	IGST	Integrated Goods and Services Tax
43	IIP	Index of Industrial Production
44	IMF	International Monetary Fund
45	IMI	Index of Macro Imbalance
46	IMP	imports
47	INR	Indian Rupee
48	IPD	implicit price deflator
49	J&K	Jammu and Kashmir
50	MCLR	marginal cost of funds-based lending rate
51	Ming.	mining and quarrying
52	Mfg.	manufacturing
53	m-o-m	month-on-month
54	Mt	metric ton
55	MoSPI	Ministry of Statistics and Programme Implementation
56	MPC	Monetary Policy Committee
57	NEXP	net exports (exports minus imports of goods and services)
58	NPA	non-performing assets
59	NCLT	National Company Law Tribunal
60	OECD	Organization for Economic Co-operation and Development
61	OPEC	Organization of the Petroleum Exporting Countries
62	PFCE	private final consumption expenditure
63	PIT	personal income tax
64	PMI	Purchasing Managers' Index (reference value = 50)
65	PoL	petroleum oil and lubricants
66	PSBR	public sector borrowing requirement
67	RE	revised estimates
68	PSU/PSE	public sector undertaking/public sector enterprises
69	RBI	Reserve Bank of India
70	SLR	Statutory Liquidity Ratio
71	Trans.	trade, hotels, transport, communication and services related to broadcasting
72	US$	US Dollar
73	UTGST	Union Territory Goods and Services Tax
74	WALR	weighted average lending rate
75	WPI	Wholesale Price Index
76	y-o-y	year-on-year
77	1HFY20	first half of fiscal year 2019-20, i.e., April 2019-September 2019

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