ENTER

Economy Watch

Monitoring India's macro-fiscal performance

March 2022

Building a better working world

Contents

Prepared by Macro-fiscal Unit, Tax and Economic Policy Group, EY India

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Highlights

1. Real GDP growth fell from 20.3% in 1QFY22 to 5.4% in 3QFY22, indicating a normalization of growth and waning base effects. The implied 4QFY22 growth is estimated at 4.8%.

2. In February 2022, PMI indicated a modest improvement in both manufacturing and services with their levels at 54.9 and 51.8 respectively as compared to 54.0 and 51.5 in January 2022.

3. IIP growth improved to 1.3% in January 2022 from 0.7% in December 2021 partly owing to a favorable base effect.

4. CPI inflation increased for the fifth successive month to 6.1% in February 2022 from 6.0% in January 2022 led by higher inflation in food items.

5. WPI inflation remained high at 13.1% in February 2022 as compared to 13.0% in January 2022, led by inflationary pressures emanating from higher global crude and primary commodity prices.

6. According to the CGA, Center's gross tax revenues grew by 38.5% during April-January FY22 with growth in direct and indirect taxes at 56.1% and 24.1% respectively.

7. During April-January FY22, Center's total expenditure grew by 11.6% with a growth of 9.9% in revenue expenditure and 22.0% in capital expenditure.

8. During April-January FY22, Center's fiscal and revenue deficits stood at 58.9% and 48.6% of their respective FY22 RE.

9. In February 2022, merchandise imports growth surged to 36.1% while exports growth remained nearly stable at 25.1% leading to a widening of merchandise trade deficit at US$(-)20.9 billion.

10. Net FDI inflows surged to an eight-month high of US$5.9 billion while net FPI outflows were at a 22-month high of US$(-)4.9 billion in January 2022.

11. The OECD has estimated a reduction in global GDP growth by over 1% point and an increase in CPI inflation by 2.5% points over the one-year period beginning 24 February 2022, if the ongoing geopolitical uncertainty persists.

12. Global crude price at US$93.5/bbl. in February 2022 was at its highest level since September 2014. Global coal price also surged to a four-month high of US$196.4/mt. during the month.

Foreword

Rising crude prices and emerging policy challenges

Global crude prices averaged at a 16-year low of US$43.8/bbl. in FY21 due to a comprehensive demand slowdown in the wake of the pandemic. In FY22, prices increased, averaging close to US$75/bbl. during April-February FY22 with the overall global economic recovery. In FY23, crude prices are likely to come under pressure due to significant supply-side issues. Already, average brent crude price has increased to US$115.6/bbl. during the first three weeks of March 2022. In tandem, there are visible increasing trends in some critical input prices such as coal, iron ore, and potassium chloride. These are important commodities in the WPI basket which has a relatively larger weight in the implicit price deflator (IPD).

The FY23 budget estimates may have to be modified due to two main reasons: (a) likely upward revision of expenditures/ subsidies particularly those related to global crude prices and (b) likely additional fiscal capacity due to underassessment of some critical determinants of Center's gross tax revenues (GTR). These determinants relate to an underestimation of (1) base magnitude that is FY22 GTR, (2) FY23 assumed tax buoyancy and (3) FY23 assumed nominal GDP growth. The nominal GDP growth for FY23 was budgeted at 11.1%. However, assuming a revised real growth component of 6.3% and an IPD-based inflation component of 6.5%, we may estimate a revised nominal GDP growth close to 13.0% for FY23. This would also be the growth of Center's GTR if the tax buoyancy is 1. Using a modified FY22 GTR base magnitude and applying on this, a growth of 13%, the resultant Center's GTR for FY23 would be higher than the budgeted magnitude of INR27.6 lakh crore by a margin of about INR3.2 lakh crore. Alongside, there would be increases in some components of expenditures linked to global crude prices including petroleum and fertilizer subsidies which were budgeted at INR5,813 crore and INR1,05,222 crore respectively. Already in FY22, the third and last supplementary demand for grants has been presented involving an increase of INR14,902 crores in fertilizer subsidies when the original allocation as per the RE was INR1,40,122 crores. In FY23, the corresponding allocation being considerably lower, there is a strong likelihood of its upward revision.

Real GDP growth moderated from 20.3% in 1QFY22 to 5.4% in 3QFY22, indicating a normalization of growth with waning base effects. Similarly, real GVA growth also fell from 18.4% to 4.7% over this period. The implied 4Q GDP and GVA growth rates are estimated to be even lower at 4.8% and 4.1% respectively. Thus, without a base effect, quarterly GDP growth has averaged 5.1% in the last two quarters of FY22. Assuming some base effects to continue in the first two quarters of FY23, the annual growth may be close to 7%. The RBI, in its February 2022 monetary policy review, had projected a growth of 7.8% for FY23. However, their estimate had not accounted for the pressures emanating from the likely higher global crude prices.

High frequency indicators (HFIs) point to a gradual recovery in economic activity in the last few months of FY22. In February 2022, PMI manufacturing showed an improvement, increasing to 54.9 from 54.0 in January 2022. PMI services also showed a modest increase to 51.8 in February 2022 from 51.5 in January 2022. In February 2022, the contraction in total vehicle retail sales eased slightly to (-)9.2% as compared to (-)10.7% in January 2022. Growth in power consumption (y-o-y) increased to a six-month high of 4.0% in February 2022 as compared to 0.9% in January 2022. Overall IIP growth improved to 1.3% in January 2022 from 0.7% in December 2021. Growth in merchandise exports remained high at 25.1%. Imports growth increased significantly to 36.1% in February 2022 from 23.5% in January 2022, led by higher global commodity prices, particularly crude oil. Gross GST collections remained high at INR1.3 lakh crore in February 2022, although marginally falling from INR1.40 lakh crore in January 2022. Bank credit growth improved marginally to 7.9% in the week ended 25 February 2022 as compared to 6.6% in the week ended 26 February 2021.

The developed countries are uplifting their interest rates under inflationary pressures. The US Fed has raised its policy rate by 25 basis points on 16 March 2022[1]. This may be considered as the first tranche of the likely increases during the course of the year. In this context, the RBI may find it advisable to uplift the policy rate with a view to stemming inflationary pressures and outward flow of US dollar. In February 2022, both CPI and WPI inflation increased to 6.1% and 13.1%, rising from 6.0% and 13.0% respectively in January 2022. While CPI inflation was largely driven by higher food

[1] https://www.federalreserve.gov/newsevents/pressreleases/monetary20220316a.htm

inflation, WPI inflation was led by higher crude and commodity prices. With monetary policy options getting constrained by rising inflation, the main policy support to growth may have to come from the fiscal side.

In the context of the current pressures on global crude prices, policymakers may have to exercise a critical choice regarding who bears the burden of higher prices of petroleum products in India amongst consumers and industrial users, oil marketing companies (OMCs), and the government. If the OMCs are not allowed to raise the prices of petroleum products, the bill for oil sector linked subsidies would go up. If the central and state governments reduce excise duty and VAT on petroleum products, their tax revenues would be adversely affected. If, on the other hand, the burden of higher prices is largely passed on to the consumers and industrial users, the already weak investment and private consumption would suffer further. If growth is to be revived, maximum attention should be paid to supporting consumption growth and reducing cost of industrial inputs with a view to improving capacity utilization. One critical segment of demand pertains to private final consumption expenditure (PFCE). This would partly get supported by Center's current thrust on accelerating infrastructure investment which is expected to have strong positive multiplier effects. As investment side multipliers have a longer time lag, it would be advisable to also support demand through revenue expenditures by extending for example, the employment guarantee scheme to urban areas to complement the existing scheme for the rural areas. Some state-governments have taken an initiative on this account (e.g.- Rajasthan, Kerala, Odisha, Himachal Pradesh, Madhya Pradesh and Jharkhand). It is desirable to evolve a unified employment guarantee scheme covering both rural and urban areas.

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1. Growth: real GDP growth moderated to 5.4% in 3QFY22

A. GDP and GVA growth: show moderation in 3Q and 4Q of FY22

- According to the National Statistical Office (NSO)'s Second Advance Estimates (SAE) of national accounts for FY22 released on 28 February 2022[2], real GDP is estimated to grow by 8.9% in FY22. The quarterly GDP data show that real GDP growth moderated to 5.4% in 3QFY22 from 8.5% in 2QFY22. Using the FY22 annual GDP magnitude along with the magnitude for the first three quarters, the implied real growth is estimated to be lower at 4.8% in 4QFY22.
- A lower growth in all the domestic demand components namely private final consumption expenditure (PFCE), government final consumption expenditure (GFCE) and gross fixed capital formation (GFCF) has led to the fall in real GDP growth in 3QFY22 **(Table 1)**.
- At the end of 3QFY22, the magnitude of PFCE, GFCE and GFCF continued to remain below their corresponding magnitudes in 3QFY20 by INR(-)0.73 lakh crore, INR(-)0.23 lakh crore and INR(-)0.14 lakh crore respectively. This indicates that domestic demand is yet to recover to its pre-pandemic level.
- Despite a strong growth in exports of goods and services at 20.9% in 3QFY22, the net exports contribution was negative at (-)3.2% points. This was due to a relatively higher growth in imports of goods and services at 32.6%.
- On the output side, real GVA growth moderated to 4.7% in 3QFY22 from 8.4% in 2QFY22. The implied GVA growth in 4QFY22 is estimated to fall further to 4.1%.
- Growth in manufacturing GVA fell to 0.2% in 3QFY22 from 5.6% in 2QFY22. Implied estimates show that in 4QFY22, it is likely to remain subdued at 1.7%.
- GVA growth in four sectors namely, manufacturing, agriculture, financial, real estate et. al. and trade, hotel et. al. slowed in 3QFY22 **(Table 1)**. Construction GVA witnessed a contraction in 3QFY22.
- At the end of 3QFY22, that is, for the nine-month period April 2021 to December 2021, the magnitude of two GVA sectors namely, construction and trade, transport, hotel, et. al. continued to remain below their corresponding magnitudes in FY20. Although the magnitude of construction sector is expected to emerge on the positive side at the end of 4QFY22 relative to FY20 levels, that of trade, transport, hotel, et. al. sector is expected to remain below the corresponding levels in FY20 by INR(-)2.9 lakh crore.
- As per the SAE, the FY22 nominal GDP growth is estimated at an 11-year high of 19.4% with an implicit-price deflator (IPD)-based inflation of 9.6% (Table A6).

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

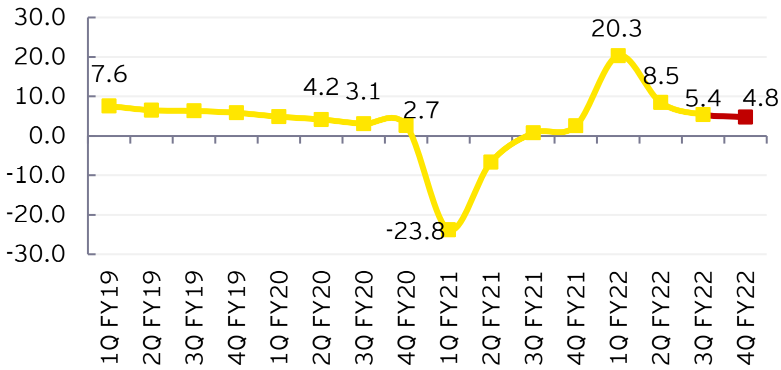


Table 1: Real GDP and GVA growth (%, annual)

Agg. demand	3Q FY21	4Q FY21	1Q FY22	2Q FY22	3Q FY22	4Q FY22*	FY21	FY22 (SAE)
PFCE	0.6	6.5	14.2	10.2	7.0	1.5	-6.0	7.6
GFCE	-0.3	29.0	-4.4	9.3	3.4	11.7	3.6	4.8
GFCF	-0.6	10.1	62.5	14.6	2.0	1.3	-10.4	14.6
EXP	-8.6	3.7	40.4	20.5	20.9	7.8	-9.2	21.1
IMP	-5.2	11.7	60.7	40.7	32.6	1.3	-13.8	29.9
GDP	**0.7**	**2.5**	**20.3**	**8.5**	**5.4**	**4.8**	**-6.6**	**8.9**
Output side								
Agr.	4.1	2.8	3.5	3.7	2.6	3.5	3.3	3.3
Ming.	-5.3	-3.9	17.6	14.2	8.8	10.7	-8.6	12.6
Mfg.	8.4	15.2	49.0	5.6	0.2	1.7	-0.6	10.5
Elec.	1.5	3.2	13.8	8.5	3.7	5.4	-3.6	7.8
Cons.	6.6	18.3	71.4	8.2	-2.8	-2.6	-7.3	10.0
Trade.	-10.1	-3.4	34.3	9.5	6.1	7.2	-20.2	11.6
Fin.	10.3	8.8	2.3	6.2	4.6	4.2	2.2	4.3
Publ.	-2.9	1.7	6.3	19.5	16.8	7.1	-5.5	12.5
GVA	**4.1**	**2.8**	**18.4**	**8.4**	**4.7**	**4.1**	**-4.8**	**8.3**

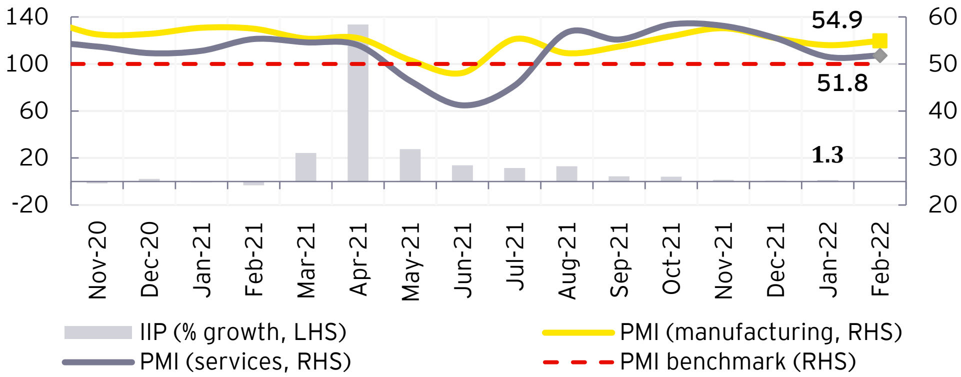
Source: MoSPI, GoI; * implied growth

[2] This release also contains the data for 3QFY22.

B. PMI: signaled a modest improvement in manufacturing and services in February 2022

- Recovering from the adverse impact of COVID's third wave, headline manufacturing PMI (seasonally adjusted (sa)) increased to 54.9 in February 2022 from 54.0 in January 2022 (**Chart 2**). February 2022 marked the eighth successive month for which manufacturing PMI has remained above its long-run average of 53.6.
- PMI services remained subdued at 51.8 in February 2022, although showing a modest improvement from a six-month low of 51.5 in January 2022. This was attributable to inflationary pressures, input shortages and state-level elections.
- Indicating a mild improvement in both manufacturing and services sector activity, composite PMI Output Index (sa) increased to 53.5 in February 2022 from 53.0 in January 2022. However, February 2022 level remained below its long-term average of 53.9.

Chart 2: PMI and IIP growth



In February 2022, PMI indicated a modest improvement in both manufacturing and services with their levels at 54.9 and 51.8 respectively.

Source: MoSPI and IHS Markit

C. IIP: grew by 1.3% in January 2022

- The quick estimates of IIP released by the MoSPI on 11 March 2022 showed that IIP grew by 1.3% in January 2022 as compared to 0.7% (revised) in December 2021 **(Chart 2)**. This improvement was partly owing to a favorable base effect.
- Manufacturing output continued to show a subdued growth at 1.1% in January 2022 as compared to 0.2% in December 2021. Growth in mining output, which is usually volatile, was at 2.8% in January 2022 as compared to 2.6% in December 2021. Growth in electricity output fell to 0.9% in January 2022 from 2.8% in December 2021.

IIP growth improved to 1.3% in January 2022 from 0.7% in December 2021 partly owing to favourable base effect.

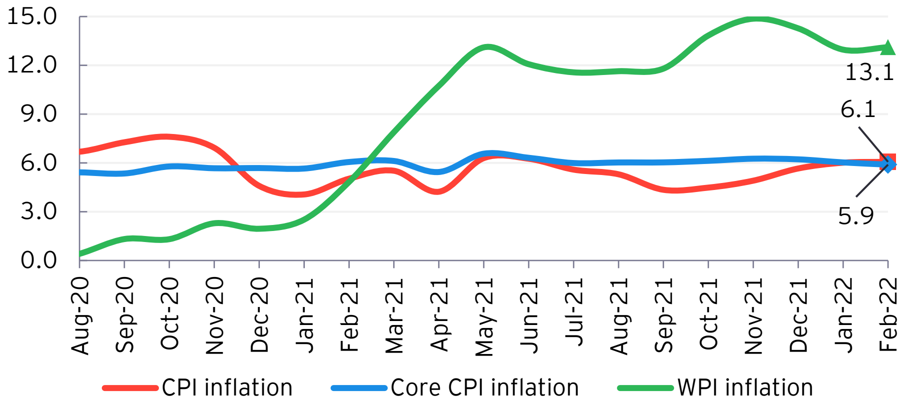
- As per the use-based classification of industries, output of consumer durables and capital goods showed a contraction for the fourth successive month at (-)3.3% and (-)1.4% respectively in January 2022. On the contrary, growth in the output of infrastructure and construction, and consumer non-durables improved to 5.4% and 2.1% respectively in January 2022 as compared to 2.1% and (-)0.1% respectively in December 2021.
- According to provisional estimates, growth in the output of eight core infrastructure industries (core IIP) moderated to 3.7% in January 2022 from 4.1% (revised) in December 2021. This slowdown may largely be attributed to a lower growth in the output of two key sub industries namely, petroleum refinery products (3.7%) and electricity (0.5%), having a combined weight of close to 47.9% in core IIP. In addition, a contraction in the output of crude oil ((-2.4%) and fertilizers ((-)2.0%), having a weight of 11.6% together in overall index, also acted as dampeners for core IIP growth.

2. Inflation: CPI inflation increased to an eight-month high of 6.1% in February 2022

CPI inflation increased for the fifth successive month to 6.1% in February 2022 from 6.0% in January 2022 led by higher inflation in food items (Chart 3).

- Consumer food inflation increased to a 15-month high of 5.9% in February 2022 from 5.4% in January 2022 due to higher inflation in meat and fish, vegetables, spices and cereals and cereal products. This increase was partly due to unfavorable base effects.
- Fuel and light-based inflation moderated to a 10-month low of 8.7% in February 2022 from 9.3% in January 2022.
- Core CPI inflation[3] marginally fell to 5.9% in February 2022 from 6.0% in January 2022 as inflation in transportation and communication services eased to 8.1% in February 2022. This was due to inflation in petrol and diesel used for transportation easing to 12.1% and 7.4% respectively in February 2022 from 16.7% and 12.6% respectively in January 2022 reflecting limited passthrough of rising global crude prices to retail fuel prices. The rise in retail fuel prices in March 2022 is likely to exert an upward pressure on inflation in this segment.
- Inflation in household goods and services increased to a 98-month high of 7.2% in February 2022.

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



Source: MoSPI, Office of the Economic Adviser, Government of India (GoI)

In February 2022, CPI inflation at 6.1% rose above the upper limit of RBI's tolerance range for the first time in eight months. Core CPI inflation remained elevated at 5.9%.

WPI inflation increased marginally to 13.1% in February 2022 from 13.0% in January 2022, led by inflationary pressures emanating from higher global crude and primary commodity prices.

- Inflation in manufactured basic metals increased to 19.8% in February 2022 from an 11-month low of 16.3% in January 2022.
- Inflation in crude surged to 55.2% in February 2022 from 39.4% in January 2022 reflecting higher global crude prices on account of geopolitical developments.
- Inflation in non-food articles increased to 24.2% in February 2022 from 19.7% in January 2022 led by higher inflation in fibres and floriculture. Inflation in fibres reached an all-time high (2011-12 series) of 45.7% in February 2022.
- Fuel and power inflation eased marginally to 31.5% in February 2022 from 32.3% in January 2022 as inflation in mineral oils (including petrol and diesel) moderated to 49.5% from 52.2% over the same period partly owing to a favorable base effect. Inflation in electricity was elevated at 15.1% in February 2022.
- WPI food index-based inflation eased to a four-month low of 8.5% in February 2022 from a 24-month high of 9.6% in January 2022 as inflation in vegetables moderated to 26.9% from 38.5% over the same period.
- Core WPI inflation rose to 10.0% in February 2022 from 9.7% in January 2022 led by higher inflation in global commodity prices.

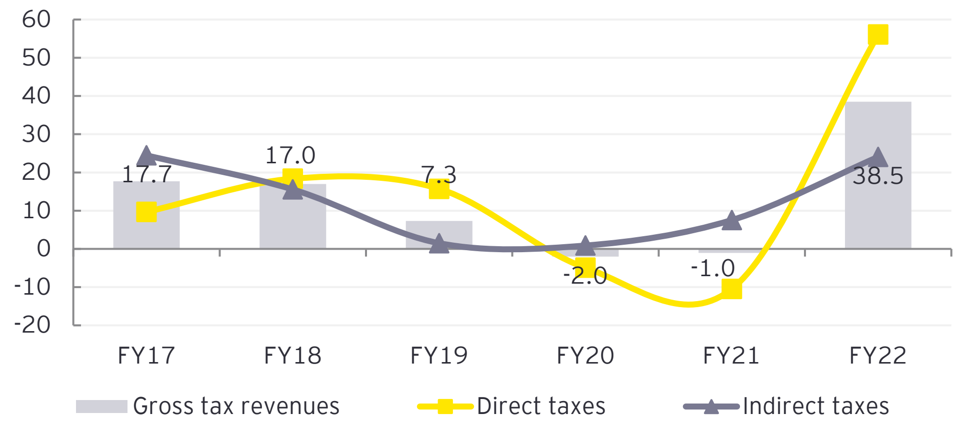
[3] Core CPI inflation is measured in different ways by different organizations/agencies. Here, it has been calculated by excluding food, and fuel and light from the overall index.

3. Fiscal performance: Center's fiscal deficit during Apr-Jan stood at 59% of the FY22 RE

A. Tax and non-tax revenues

- As per the Comptroller General of Accounts (CGA), Center's gross tax revenues (GTR) grew by 38.5% during April-January FY22 as compared to a contraction of (-)1.0% during the corresponding period of FY21 (**Chart 4**). As a proportion of the FY22 RE, Center's GTR during the first ten months of FY22 stood at 83.4%, higher than the corresponding average ratio of 73.6% during the five-year period from FY17 to FY21.
- With the base effects waning, the buoyancy of Center's GTR moderated to 1.3 in 3QFY22 from 2.3 in 2Q and 3.0 in 1Q of FY22.
- Direct and indirect tax revenues grew by 56.1% and 24.1% respectively during April-January FY22 as compared to (-)10.5% and 7.5% during April-January FY21.
- Among direct taxes, corporate income tax (CIT) showed a growth of 63.8% during April-January FY22 as compared to a contraction of (-)14.9% in the corresponding period of FY21.
- Personal income tax (PIT) grew by 48.3% during April-January FY22 as compared to a contraction of (-)5.5% in the corresponding period of FY21.
- Among indirect taxes, Center's GST revenues[a] grew by 26.1% during April-January FY22 as compared to a contraction of (-)8.6% during the corresponding period of FY21.
- Union excise duties (UED) showed a low growth of 9.5% during April-January FY22 due to unfavorable base effect as reflected in the high growth of 57.8% during the corresponding period of FY21.
- Center's customs duty revenues showed a strong growth of 56.5% during April-January FY22 as compared to only 1.8% during April-January FY21.

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



Center's GTR grew by 38.5% during April-January FY22 with growth in direct and indirect taxes at 56.1% and 24.1% respectively.

Source: Monthly Accounts, CGA, Government of India
Notes: (a) Direct taxes include personal income tax and corporation tax, and indirect taxes include union excise duties, arrears of service tax, customs duty, and GST (comprising 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 GTR along with direct and indirect taxes, (c) IGST revenues are subject to final settlement.

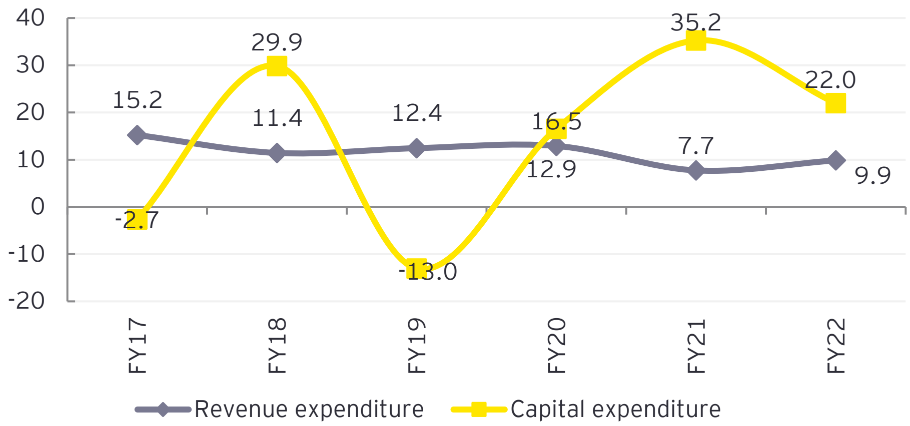
- Center's non-tax revenues grew by 106.6% during April-January FY22 as compared to a contraction of (-)44.0% during the corresponding period of FY21. Non-tax revenues during the first ten months of FY22 stood at 92.9% of the annual RE as compared to the corresponding ratio of 67.0% in FY21.
- Non-debt capital receipts showed a contraction of (-)19.2% during April-January FY22 as compared to a growth of 23.3% over the corresponding period of FY21. Non-debt capital receipts during April-January FY22 stood at 32.6% of the FY22 RE which had been lowered to INR99,975 crores from the BE of INR1.88 lakh crore.
- According to the Department of Investment and Public Asset Management[4], as on 24 March 2022, disinvestment receipts stood at INR12,423.67 crores, that is 15.9% of the FY22 RE.

[4] https://dipam.gov.in/

B. Expenditures: revenue and capital

- Center's total expenditure grew by 11.6% during April-January FY22 as compared to 11.0% during the corresponding period of FY21. Total expenditure during the first ten months of FY22 stood at 74.5% of the FY22 RE as compared to the corresponding ratio of 73.0% during FY21.
- Revenue expenditure showed a growth of 9.9% during April-January FY22 as compared to 7.7% during the corresponding period of FY21 (**Chart 5**). Revenue expenditure during April-January FY22 stood at 74.8% of the FY22 RE as compared to the corresponding ratio of 71.6% during FY21.
- Growth in Center's capital expenditure was at 22.0% during April-January FY22 as compared to 35.2% during the corresponding period of FY21. Capital expenditure during the first ten months of FY22 stood at 73.3% of the RE as compared to the corresponding ratio of 82.5% in FY21.

Chart 5: Growth in central expenditures during April-January (%, y-o-y)



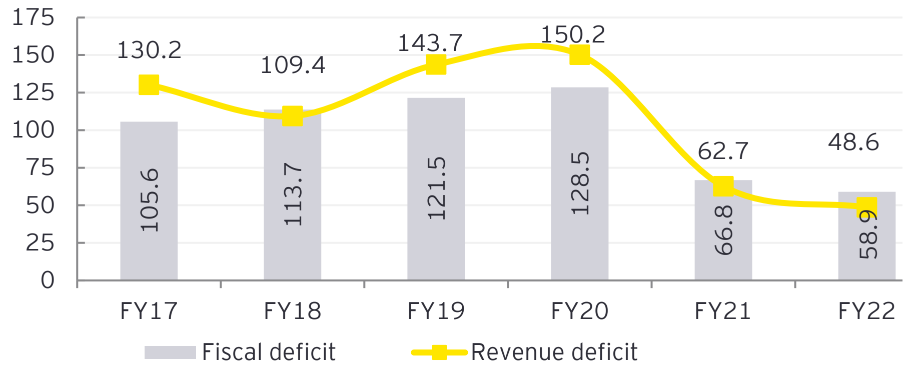
Source (basic data): Monthly Accounts, Controller General of Accounts (CGA), Government of India

During April-January FY22, Center's total expenditure grew by 11.6% with a growth of 9.9% in revenue expenditure and 22.0% in capital expenditure.

C. Fiscal imbalance

- Center's fiscal deficit during April-January FY22 stood at 58.9% of the RE as compared to the corresponding average ratio of 113.8% during the period FY16 to FY20 (**Chart 6**).
- Center's revenue deficit during April-January FY22 as a proportion of the RE stood at 48.6% as compared to the corresponding average level of 127.0% during FY16 to FY20.

Chart 6: Fiscal and revenue deficit during April-January as percentage of annual RE



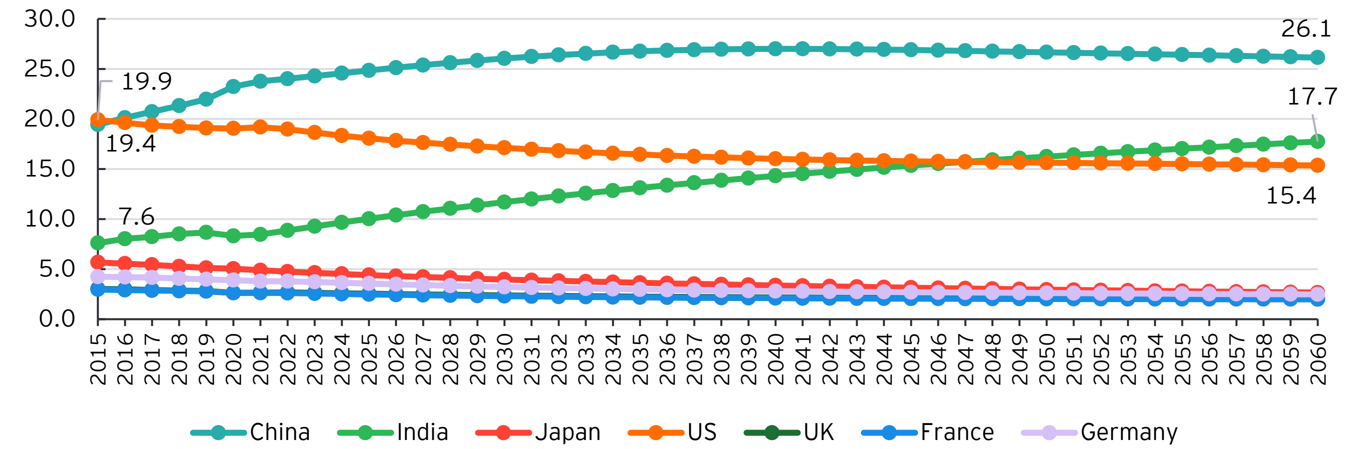
Source: Monthly Accounts, Controller General of Accounts (CGA), Government of India.

During April-January FY22, Center's fiscal and revenue deficits stood at 58.9% and 48.6% of their respective FY22 RE.

4. Comparative global perspective: India to overtake US in terms of PPP based GDP by 2047

- The OECD provides data for trend GDP including long-term baseline projections (up to 2060), in real terms. This is measured in US$ at 2010 Purchasing Power Parities (PPP). Using this data, the annual growth and shares in global GDP have been calculated for seven major economies namely, China, India, Japan, US, UK, France and Germany.
- The selected seven economies account for an average share of 67% in world trend GDP during 2015 to 2060.
- The share of both China and the US was close to 20% in 2015 while India accounted for 7.6% of global GDP. Japan's share was at 5.7% and Germany and France accounted for less than 5% of global GDP in 2015 **(Chart 7)**.
- There is a fall in the share of all selected AEs particularly the US, and an increase in the share of selected EMEs particularly India. China's share is expected to be the highest, stabilizing in the range of 26-27% during 2030 to 2060. India's share is expected to continuously increase, surpassing that of the US in 2047 and reaching 17.7% by 2060. The share of the US is forecasted to decline to 15.4% by 2060.
- The share of Japan, France and Germany is forecasted to fall to less than 3% by 2060.

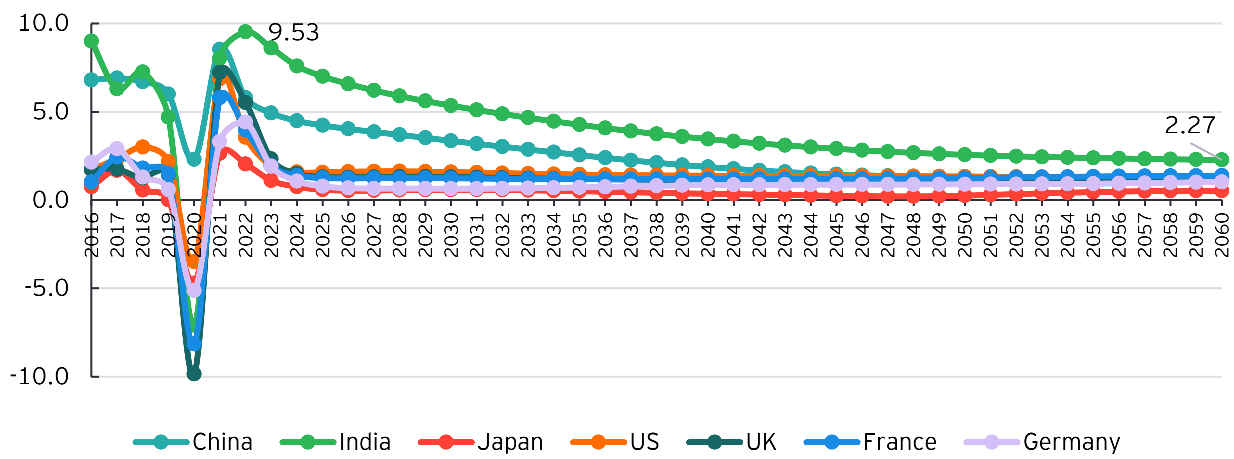
Chart 7: Share in trend global GDP (%)



Source: OECD

- Growth evaluated using trend GDP levels for all selected economies witnessed a sharp fall in 2020 indicating the adverse impact of the pandemic. The subsequent year of 2021 marked a strong recovery owing to base effects and there is normalization of trend growth after that **(Chart 8)**.
- Growth rates calculated using trend GDP levels for India and China indicate a noticeable decline, reaching 2.3% and 1.2% respectively by 2060 while that for the remaining countries show a near-stagnation. Nevertheless, India's growth is expected to remain higher than the selected set of countries during 2022 to 2060.

Chart 8: GDP growth (%, annual)



Source: OECD

5. In focus: Growth and fiscal prospects – policy options for post-COVID recovery

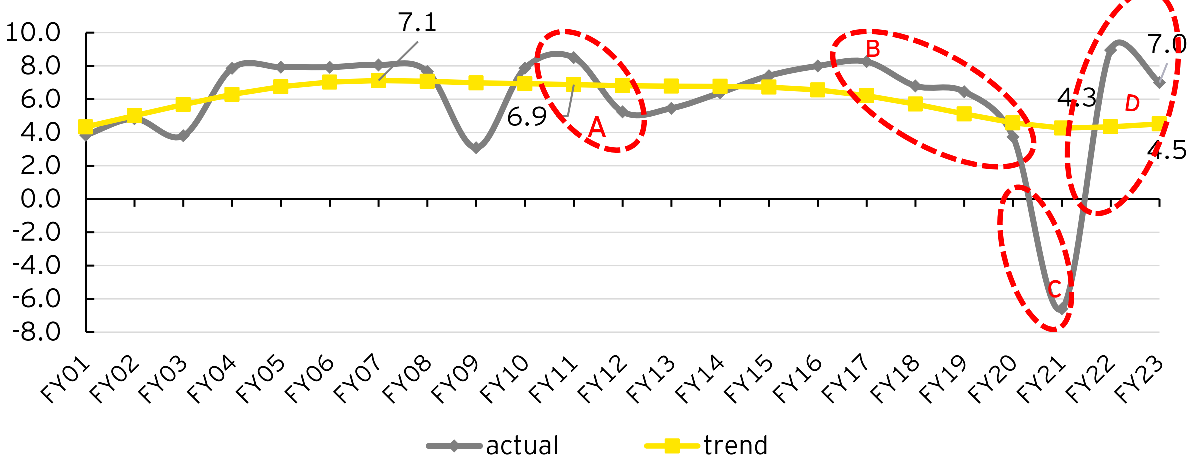
1. Introduction

In FY23, the Indian economy is expected to normalize once again after overcoming COVID's sharp adverse shock. This process consumed two years: FY21 which suffered a major contraction and FY22 which allowed enough recovery to enable the economy to reach back to a real GDP magnitude only marginally above its pre-pandemic FY20 level. Even as policymakers have been looking forward to the prospects of a normalized Indian economy, another layer of challenges has gathered momentum in the form of surging prices of global crude and primary products along with an accentuation of supply-side bottlenecks. These issues in fact, pre-date the recent geopolitical developments.

2. India's growth performance: phases of slowdowns coincided with upsurges in crude prices

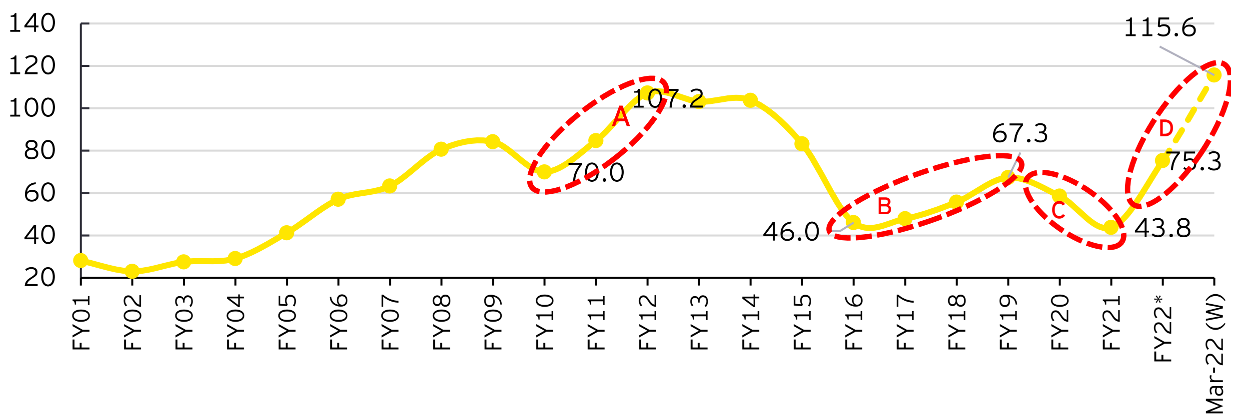
Chart 9 shows the four recent distinct phases of growth in India namely, (1) Phase A, spanning from FY11 to FY13, (2) Phase B, from FY17 to FY20, (3) Phase C comprising the COVID-affected year of FY21, and (4) Phase D comprising FY22 and FY23. There was a fall of (-)3.0% points and (-)3.1% points in real GDP growth respectively during phases A and B. In FY21, real GDP contracted by (-)6.6% from a growth of 3.7% in FY20, a fall of (-)10.3% points. Phase D shows a recovery in FY22 enabling a normalization of the growth process in FY23. While the first two phases were characterized by global crude price upsurges, in phase C, there was a fall in crude prices due to a comprehensive demand slowdown. In phase D, particularly in FY22, there has been a release of pent-up demand and significant supply rigidities leading to an increase in global crude prices. In FY23, due to the recent geopolitical uncertainty, crude prices are expected to increase sharply. **Chart 10** shows that the average brent crude price has already surged to US$123.21/bbl. (week ending 7 March 2022[5]).

Chart 9: Real GDP growth (%, annual): actual and trend



Source (basic data): MoSPI
Note: Real GDP growth for FY23 is taken at 7%

Chart 10: Global crude prices (US$/bbl.) – annual trends



Source (basic data): World Bank and https://oilprice.com/
*Averaged for the period April 2021 to February 2022; (w) for the period 1 March to 21 March 2022

[5] https://www.statista.com/statistics/326017/weekly-crude-oil-prices/

In FY22, on a quarterly basis, both GDP and GVA show normalizing growth with waning base effects. Real GDP growth moderated from 20.3% in 1Q to 5.4% in 3Q of FY22. Similarly, real GVA growth also fell from 18.4% to 4.7% over this period. The implied 4Q GDP and GVA growth rates are estimated to be even lower at 4.8% and 4.1% respectively. Thus, without a base effect, quarterly GDP growth has averaged 5.1% in the last two quarters of FY22. Assuming some base effects to continue in the first two quarters of FY23, the annual growth is likely to be lower than 7% if we factor in the continuing pressures on prices of global crude and primary products.

In tandem, there are visible increasing trends in some critical input prices such as coal, iron ore, sunflower oil and potassium chloride **(Charts 11 and 12)**. Potassium chloride is a key input for potassium fertilizers. These are important commodities in WPI which has a relatively larger weight in the implicit price deflator (IPD).

Chart 11: Global coal and iron ore prices

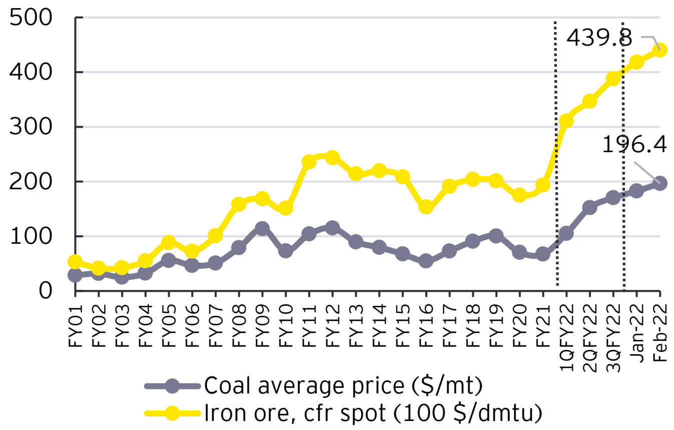
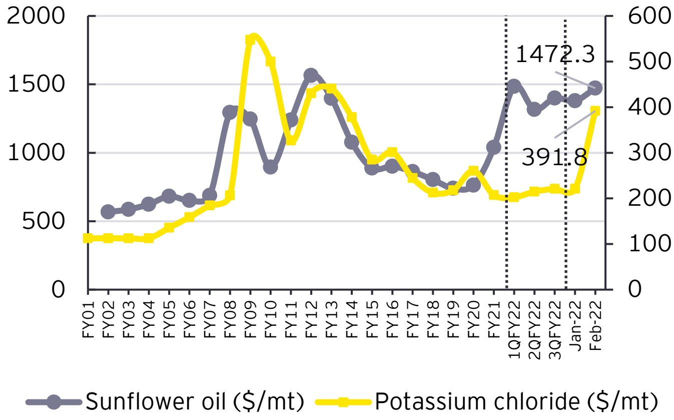


Chart 12: Global sunflower oil and potassium chloride prices



Source (basic data): World Bank

3. Macro implications of crude shock: *ceteris paribus* assumptions

It is difficult to arrive at precise estimates of the impact of the increase in global crude prices, but some idea can be provided using RBI's recent estimates (2021) of the effects of an increase of US$10/bbl., *ceteris paribus* on some critical macroeconomic parameters including growth and inflation. **Table 2** shows that the estimated impact of a US$10/bbl. increase in the price of Indian crude basket is a reduction in real GDP growth by 27 basis points and an increase in CPI inflation by 40 basis points. An earlier RBI (2019) study had estimated the impact on current account deficit and Center's fiscal deficit relative to GDP of a US$10/bbl. increase in the Indian crude basket. The adverse impact for both cases is of the order of 43 basis points of GDP. For Center's fiscal deficit, it is assumed that the burden of increased price is not passed on to the consumers.

Table 2: Impact of a US$10/bbl. increase in price of Indian crude basket on India's key macro parameters

Impacted parameter	RBI (2021) - in % points
Real GDP growth (reduction)	0.27
CPI inflation (increase)	0.40
CAD as % of GDP (deterioration)	0.43*
Centre's fiscal deficit to GDP ratio (widening)#	0.43*

Notes: (1) For RBI (2021), source is Monetary Policy Report, October 2021 - In the original study, a baseline assumption for Indian crude basket at US$75/bbl. for 2HFY22 is considered. RBI estimates the impact of a 10% increase in Indian crude basket at (-)0.2% points for growth and (+)0.3% points for CPI inflation.
*https://www.rbi.org.in/Scripts/MSM_Mintstreetmemos17.aspx (RBI, 2019); # For Centre's fiscal deficit, the assumption is that the burden of increased price is not passed on to the consumers

The RBI (2021) study had assumed a baseline price of Indian crude basket at US$75/bbl. Using this as the baseline, we may consider two benchmarks relating to the average price of the Indian crude basket in FY23 at US$100/bbl. (scenario 1) and at US$125/bbl. (scenario 2). Thus, the increase from the baseline price would be US$25/bbl. (scenario 1) and US$50/bbl. (scenario 2). **Table 3** summarizes the estimated impact in these two scenarios.

Table 3: Estimated impact of increase in price of Indian crude basket on key macro parameters

Impacted parameter	Margin of increase from baseline price of US$75/bbl. (% points)	
	Scenario 1 (US$25/bbl.)	Scenario 2 (US$50/bbl.)
Real GDP growth (reduction)	0.7	1.35
CPI inflation (increase)	1.0	2.0
CAD as % of GDP (deterioration)	1.07	2.15
Centre's fiscal deficit to GDP ratio (widening)	1.07	2.15

Source: EY estimates

With reference to baseline FY23 real GDP growth at 7% and CPI inflation at 5%, the revised levels of these variables may be put at 6.3% and 6% respectively after taking into account, the impact of crude price increase by a margin of US$25/bbl. as per scenario 1 **(Table 4).** The impact would be larger if other factors are also taken into account, or if the margin of increase is enhanced.

Table 4: Revision in selected FY23 estimates due to the impact of an increase in the price of Indian crude basket

Variable	Baseline estimates (FY23)	Revised estimates incorporating crude price effects	
		Scenario 1 (US$25/bbl.)	Scenario 2 (US$50/bbl.)
Real GDP growth (%)	7.0 *(7.8 - RBI#)*	6.3 *(7.1)*	5.6 *(6.5)*
CPI inflation (%)	5.0 *(4.5 - RBI#)*	6.0 *(5.5)*	7.0 *(6.5)*
Current Account Deficit (% to GDP)	1.9*	3.0	4.1
Centre's fiscal deficit (% to GDP)	6.4**	7.5	8.6

Source: EY estimates
* RBI Professional Forecaster's Survey, Feb 2022; ** FY23 Union Budget; # as per RBI's February 2022 Monetary Policy Statement

There may also be some sectoral supply-side bottlenecks and cost escalation. Sectors that draw heavily on petroleum products such as fertilizers, iron and steel foundries, transportation, construction and coal would be adversely affected. Some adverse effects in regard to financial flows have also become noticeable. Net FPI outflows during October 2021 to January 2022 increased to US$11.2 billion. Net FDI inflows, although positive, have also been falling during this period as compared to the corresponding period of the previous year.

4. Center's FY23 budget: unanticipated fiscal capacity and compulsions

In this section, we examine the main contours of Center's FY23 budget (as discussed in detail in the February 2022 issue of the EY Economy Watch[6]), with reference to the emerging challenges emanating from the global crude price upsurge and related developments.

I. Budget estimates prior to crude shock

Table 5 summarizes the major fiscal aggregates of Center's FY23 budget in terms of the relevant magnitudes. The estimated impact on some of the macro-fiscal parameters due to the upward pressure on global crude price are highlighted in **Table 4**.

Table 5: Major fiscal aggregates (magnitudes in INR lakh crore)

Item	FY21	FY22 (RE)	FY23 (BE)
Gross tax revenues	20.27	25.16	27.58
Net tax revenues	14.26	17.65	19.35
Non-tax revenues	2.08	3.14	2.70
Non-debt capital receipts	0.58	1.00	0.79
Fiscal deficit	18.18	15.91	16.61
Total expenditure *of which*	35.10	37.70	39.45
Revenue exp.	30.84	31.67	31.95
Capital exp.	4.26	6.03	7.50

Source (basic data): FY23 Union Budget

[6] https://assets.ey.com/content/dam/ey-sites/ey-com/en_in/topics/tax/economy-watch/2022/02/ey-economy-watch-february-2022.pdf

II. Broad contours of revised estimates

The FY23 budget estimates may have to be modified due to two main reasons: (a) likely additional fiscal capacity due to underestimation of some critical determinants of Center's GTR and (b) likely upward revision of expenditures/ subsidies particularly those related to global crude prices.

In regard to the estimation of additional fiscal capacity, reference may be made to the budgeted nominal GDP growth forecast for FY23 at 11.1%. Assuming a revised real growth component of 6.3% and an IPD-based inflation component of 6.5%, which may be slightly higher than the corresponding CPI inflation **(Table 4)**, we may have a revised nominal GDP growth close to 13.0%. Applying on this, a tax buoyancy of 1, the resultant Center's GTR would be higher than the budgeted magnitude of INR27.6 lakh crore by a margin of about INR3.2 lakh crore **(Table 6).** Alongside, there would be increases in some components of expenditures linked to prices of petroleum products including petroleum and fertilizer subsidies which were budgeted at INR5,813 crore and INR1,05,222 crore respectively. Already in FY22, the third and last supplementary demand for grants[7] has been presented involving an increase of INR14,902 crore in fertilizer subsidies when the original allocation as per the RE was INR1,40,122 crore. In FY23, the corresponding allocation being considerably lower, there is a strong likelihood of its upward revision.

Table 6: Estimation of additional fiscal capacity in FY23 relative to BE

No.	Items	Gross tax revenues	Net tax revenues
		INR lakh crore	
1	FY22 RE	25.2	17.7
2	Modified FY22	27.3	19.2
3	FY23 BE	27.6	19.3
4	Modified FY23	30.8#	21.7
5=4-3	Additional fiscal space in FY23	3.2	2.3
Memo item: Nominal GDP (INR lakh crore)			
FY22 (NSO)			*236.4*
FY23 Estimated			*267.2**

Source (basic data): Union budget and EY estimates
*Estimated by assuming 13% growth over FY22 nominal GDP
Assuming a buoyancy of 1

5. Policy options

Policymakers may have to exercise a critical choice regarding who bears the burden of higher prices of petroleum products in India amongst consumers and industrial users, oil marketing companies (OMCs), and the government. If the OMCs are not allowed to raise the prices of petroleum products, the bill for oil sector linked subsidies would go up. If the central and state governments reduce excise duty and VAT on petroleum products, their tax revenues would be adversely affected. If, on the other hand, the burden of higher prices is largely passed on to the consumers and industrial users, the already weak investment and private consumption would suffer further. If growth is to be revived, maximum attention should be paid to supporting consumption growth and reducing cost of industrial inputs with a view to improving capacity utilization. The government may have to strike an appropriate balance amongst these options.

The developed countries are uplifting their interest rates under inflationary pressures. The US Fed has raised its policy rate by 25 basis points on 16 March 2022. This may be considered as the first tranche of the likely increases during the course of the year. In this context, the RBI may find it advisable to uplift the policy rate with a view to stemming inflationary pressures and outward flow of US dollar. In February 2022, both CPI and WPI inflation increased to 6.1% and 13.1%, rising from 6.0% and 13.0% respectively in January 2022. With monetary policy options getting constrained by rising inflation, the main policy support to growth may have to come from the fiscal side.

Post COVID, as the Indian economy has started to normalize, focus may be on some of the immediate compulsions emanating from the current pressures on prices of global crude and primary products. Other things remaining the same, this may have an adverse impact on real growth and CPI inflation. There would also be some slippage in fiscal and current account deficits relative to GDP. The magnitude of such an adverse impact will depend on the extent to which crude prices increase in FY23 on average. However, some of these effects can be mitigated by undertaking

[7] https://dea.gov.in/sites/default/files/FINAL%20Supp.pdf

policy initiatives that would support demand and growth. One critical segment of demand pertains to private final consumption expenditure (PFCE). This would partly get supported by Center's current thrust on accelerating infrastructure investment which is expected to have strong positive multiplier effects. As investment side multipliers have a longer time lag, it may be advisable to also support demand through revenue expenditures by extending for example, the employment guarantee scheme to urban areas to complement the existing scheme for the rural areas. Some state-governments have taken an initiative on this account (Rajasthan, Kerala, Odisha, Himachal Pradesh, Madhya Pradesh and Jharkhand)[8]. It may be useful to evolve a unified employment guarantee scheme covering both rural and urban areas.

6. Time for recasting FRBM

Since the enactment of Center's FRBMA in 2003 and subsequently, state-level Fiscal Responsibility Legislations, two major global crises in FY09 and in FY21 upset India's fiscal consolidation efforts. In both cases, the slippage was largely on account of the central government and comparatively much less on account of the state governments. This may be considered justifiable since the central government, in theory and practice, has had to play a proactive role in achieving macro-stabilization. The more recent COVID crisis forced the combined government debt-GDP ratio to sharply increase by a margin of 14.9% points to an estimated 89.4% at the end of FY21, largely because of the contraction in both real and nominal GDP growth.

In the emerging post-COVID global economic scenario, India has to attempt uplifting its growth rate closer to its potential while restoring fiscal consolidation so that sustained growth and stability in government finances can be achieved. For this purpose, Center's FRBMA requires to be recast. Moving towards sustainable levels of debt and deficit would usher India as a global growth leader quickly and help sustain this position over a long period. As shown in **Table 7**, the central government may be given a higher fiscal deficit target at 4.0% instead of the current target of 3.0% of GDP in view of its macro-stabilization role. The corresponding debt-GDP target for the central government would be 40%. For states, the consistent debt and deficit targets could be kept at 30% and 3% of GDP respectively. However, states could be provided a complementary role in macro-stabilization by using instruments other than flexibility in fiscal deficit, such as a 'Stabilization Fund'. Stabilization Funds have been used in other countries also as a countercyclical instrument[9]. The combined debt would stabilize at 70% of GDP with a general government fiscal deficit to GDP ratio of 7%. These combinations are consistent with a nominal GDP growth of 11%. If India manages to uplift its nominal growth to say, 12%, then the combined debt-GDP ratio could be stabilized at nearly 65.3% (may be rounded down to 65%) of GDP with central debt at 37.3% (may be rounded down to 37%) and state debt at 28% of GDP with their corresponding fiscal deficit to GDP ratios at 4% and 3%.

Table 7: Proposed debt and deficit targets for Center and states (consistent with nominal growth of 11%)

relative to GDP at current market prices

Tier of government	Existing FRBM			Proposed FRBM		
	Debt	Fiscal deficit	Revenue deficit	Debt	Fiscal deficit	Revenue deficit
Centre	40%	3%	Not specified	40%	4%	Balance or surplus
State	20%	3%	Balance or surplus	30%	3%	Balance or surplus
Combined	60%	6%	Not specified	70%	7%	Balance or surplus

Source: Srivastava, D.K., Bharadwaj, M., Kapur, T., & Trehan, R. (2021). Covid's Economic Impact: Should India Recast its Fiscal and Monetary Policy Frameworks?: Journal of International Economics and Finance. 1(1), 63-81.

7. Conclusions

Post COVID, as the Indian economy has started to normalize, focus may be on some of the immediate compulsions emanating from the current pressures on prices of global crude and primary products. Other things remaining the same, this may have an adverse impact on real growth and CPI inflation. There would also be some slippage in fiscal and current account deficits relative to GDP. The magnitude of such an adverse impact will depend on the extent to which crude prices increase in FY23 on average. Policymakers may have to exercise a critical choice regarding who

[8] https://indianexpress.com/article/explained/explainspeaking-urban-employment-guarantee-schemes-rajasthan-budget-7794046/
Kerala (Ayyankali Urban Employment Guarantee Scheme), Odisha (Unnati or Urban Wage Employment Initiative), Himachal Pradesh (Mukhya Mantri Shahri Ajeevika Guarantee Yojna or MMSAGY), Madhya Pradesh (Mukhyamantri Yuva Swabhiman Yojana) and Jharkhand (Mukhyamantri Shramik Yojana)
[9] Report of Committee on 'State FRL: The next phase', 2009 (constituted by the RBI)

bears the burden of higher prices of petroleum products in India amongst consumers and industrial users, oil marketing companies (OMCs), and the government. The government may have to strike an appropriate balance amongst these options.

The developed countries are uplifting their interest rates under inflationary pressures. In this context, the RBI may find it advisable to uplift the policy rate with a view to stemming inflationary pressures and outward flow of US dollar. With monetary policy options getting constrained by the rising inflation, the main policy support to growth may have to come from the fiscal side. One critical segment of demand pertains to private final consumption expenditure (PFCE). This would partly get supported by Center's current thrust on accelerating infrastructure investment which is expected to have strong positive multiplier effects. As investment side multipliers have a longer time lag, it would be advisable to also support demand through revenue expenditures by extending for example, the employment guarantee scheme to urban areas to complement the existing scheme for the rural areas. Some state-governments have taken an initiative on this account (Rajasthan, Kerala, Odisha, Himachal Pradesh, Madhya Pradesh and Jharkhand). It is desirable to evolve a unified employment guarantee scheme covering both rural and urban areas.

Moving beyond these immediate concerns, laying a solid foundation for achieving a high and stable medium-term growth consistent with India's potential in the range of 7-7.5% is called for. For this purpose, Center's FRBM in which critical state-level debt and deficit targets are also embedded, may require to be recast. We consider that in view of Center's larger responsibility with respect to macro stabilization, it may be given a higher fiscal deficit benchmark of 4% of GDP while states may continue with the target of 3% of GDP. Both tiers of government should be made to achieve revenue account balance so that the combined fiscal deficit can be devoted to financing capital expenditures which will support infrastructure expansion at an adequate pace.

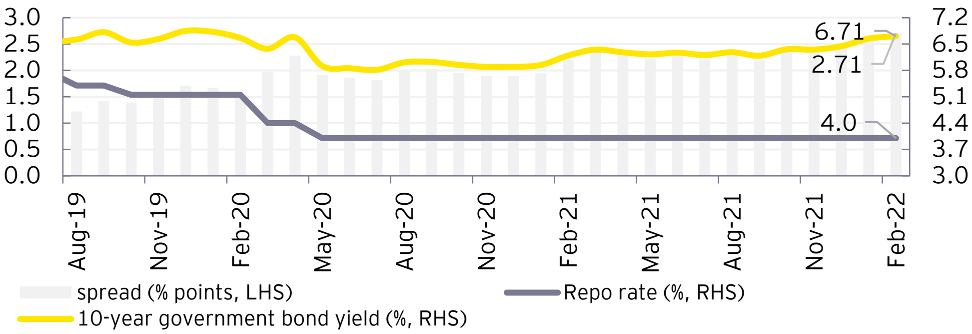
6. Money and finance: growth in bank credit slowed to 8.2% in January 2022

A. Monetary sector

Monetary policy

- The Monetary Policy Committee (MPC) unanimously voted to retain the repo rate at 4.0% in its February 2022 monetary policy review as CPI inflation was expected to remain within the RBI's inflation tolerance range in the last quarter of FY22 **(Chart 13).** However, CPI inflation touched 6.0% in January 2022 and increased further to 6.1% in February 2022.
- The MPC had assessed that in the coming months, two divergent inflation trends may be visible for food vis-à-vis non-food items. Vegetable prices are expected to ease due to the arrival of winter crops and an expected robust Rabi harvest is likely to lower the pressure on food prices. Similarly, strong supply side interventions by the government and higher domestic production are expected to ease the prices of edible oil and pulses. However, the outlook on crude oil prices is expected to remain uncertain owing to geopolitical developments while cost push pressures on core inflation are likely to persist in the near-term.

Chart 13: Movements in the repo rate and 10-year government bond yield



Source: Database on Indian Economy, RBI

Growth in bank credit moderated to 8.2% in January 2022 from 9.2% in December 2021. It has remained below the 10% mark since August 2019.

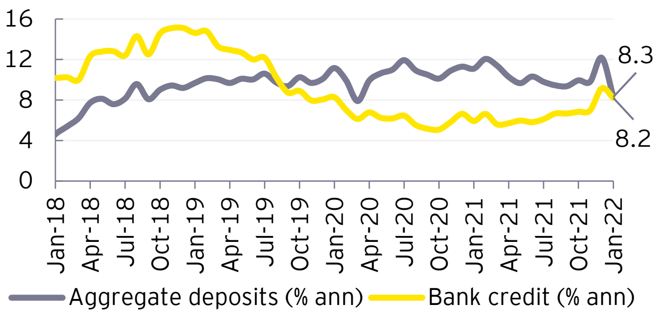
Money stock

- Growth in broad money stock (M3) increased marginally to 8.7% in February 2022 as compared to 8.4% in January 2022. This pickup was due to a higher growth in narrow money (M1).
- Growth in M1 increased to 11.6% in February 2022 from 10.1% in January 2022 due to a strong growth in demand deposits as also a recovery in the growth of currency with the public. Growth in demand deposits increased to 15.3% in February 2022 from 12.6% in January 2022. Growth in currency with the public increased to 9.0% in February 2022 from 8.3% in January 2022.
- Time deposits, accounting for about 76% of M3 on average (last three years), showed a growth of 7.8% in February 2022, similar to its level in January 2022.

Aggregate credit and deposits

- Outstanding bank credit by scheduled commercial banks (SCBs) moderated to 8.2% in January 2022 from 9.2% in December 2021 **(Chart 14)**.
- Growth in non-food credit slowed to 8.3% in January 2022 from 9.3% in December 2021 due to a broad-based slowdown in credit offtake across all sectors.
- Sectoral deployment of bank credit[10] showed that growth in outstanding credit to industries fell to 6.4% in January 2022 from 7.6% in December 2021.

Chart 14: Growth in credit and deposits



Source: Database on Indian Economy, RBI

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

- Within the industrial sector, growth in credit to textiles, chemicals, and drugs and pharmaceuticals moderated to 1.9%, 4.1% and 9.0% respectively in January 2022 from 11.8%, 12.7% and 11.0% respectively in December 2021. Even though growth in credit to infrastructure sector improved to 12.0% in January 2022 from 10.9% in December 2021, this may largely be attributed to a favorable base effect.
- Growth in credit to services sector at 7.3% in January 2022 was lower than 10.8% in December 2021.
- Growth in credit to agricultural sector was also lower at 10.4% in January 2022, falling from 14.5% in December 2021. Similarly, personal loans, accounting for about 30% of total non-food credit also showed a lower growth of 11.6% in January 2022 as compared to 14.3% in December 2021.
- Growth in aggregate bank deposits moderated to 8.3% in January 2022 from 12.2% in December 2021.

B. Financial sector

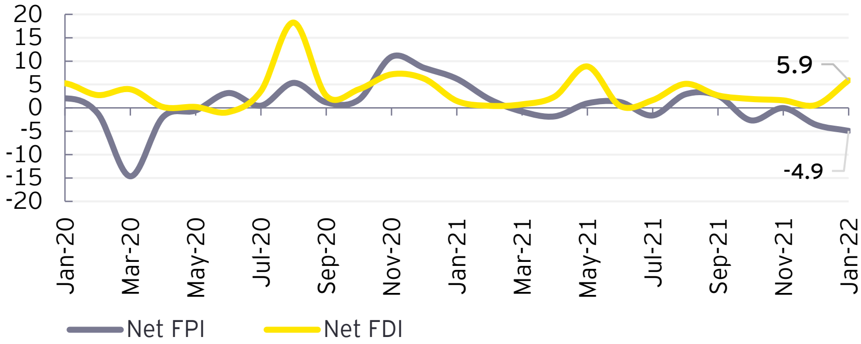
Interest rates

- As per the data released by the RBI on 4 March 2022, the average interest rate on term deposits with a maturity of more than one year was increased marginally from 5.28% in January 2022 to 5.30% in February 2022 with the actual rate ranging from 5.00% to 5.60%.
- The MCLR remained stable at 6.73% for the second successive month in February 2022 with the actual rate ranging between 6.45% and 7.00%.
- The average yield on 10-year government bonds increased to a 22-month high of 6.71% in February 2022 from 6.69% in January 2022 **(Chart 13)**. Bond yields were largely influenced by (a) the Union Budget announcement of an unprecedented gross borrowing target of INR14.95 trillion in FY23[11] and (b) the perceived adverse impact of the geopolitical developments on India's inflation and growth.
- WALR on fresh rupee loans by SCBs increased by 10 basis points to 7.82% in January 2022 from 7.72% in December 2021.

FDI and FPI

- As per the provisional data released by the RBI on 17 March 2022, overall foreign investment[12] (FI) inflows were at US$1.0 billion in January 2022 as compared to outflows amounting to US$(-)2.7 billion (revised) in December 2021. This was largely on account of a sharp surge in net FDI inflows.

Chart 15: Net FDI and FPI inflows (US$ billion)



Net FDI inflows surged to an eight-month high of US$5.9 billion while net FPI outflows were at a 22-month high of US$(-)4.9 billion in January 2022.

Source: Database on Indian Economy, RBI

- Net FDI inflows rose to an eight-month high of US$5.9 billion in January 2022 from US$0.9 billion (revised) in December 2021 **(Chart 12)**. Gross FDI inflows were higher at US$8.9 billion in January 2022 as compared to US$6.7 billion in December 2021.
- Net FPI outflows reached a four-month high of US$(-)4.9 billion in January 2022 from US$(-)3.6 billion in December 2021.

[11] https://www.indiabudget.gov.in/doc/rec/ctr.pdf
[12] Foreign Investment (FI) = net FDI plus net FPI

7. Trade and CAB: merchandise trade deficit widened to US$(-) 20.9 billion in February 2022

A. CAB: after a surplus of 0.9% of GDP in 1QFY22, current account posted a deficit of (-)1.3% of GDP in 2QFY22

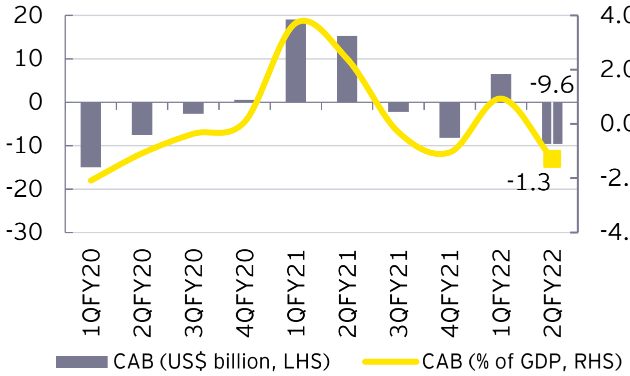
Current account recorded a deficit at (-)1.3% of GDP in 2QFY22 as compared to a surplus of 0.9% of GDP in 1QFY22 **(Chart 16, Table 8).** Net merchandise trade deficit deteriorated to a nine-quarter high of (-)5.9% of GDP in 2QFY22 from (-)4.4% in 1QFY22 as merchandise imports rose to a 12-quarter high of 19.9% of GDP in 2QFY22 from 18.5% in 1QFY22. Merchandise exports relative to GDP were at a 27-quarter high of 14.0% in 2QFY22, the same level as seen in 1QFY22. Net service receipts and net transfer receipts relative to GDP weakened to 3.4% and 2.5% respectively in 2QFY22 from 3.7% and 2.7% respectively in 1QFY22.

Table 8: Components of CAB in US$ billion

Fiscal year	CAB as % of nominal GDP	CAB	Goods account net	Invisibles* net
FY18	-48.7	-1.8	-160.0	111.3
FY19	-57.3	-2.1	-180.3	123.0
FY20	-24.7	-0.8	-157.5	132.8
FY21	32.1	0.9	-60.4	92.5
3QFY21	-0.3	-2.2	-34.6	32.4
4QFY21	-1.0	-8.2	-41.7	33.6
1QFY22	0.9	6.5	-30.7	37.2
2QFY22	-1.3	-9.6	-44.4	34.8

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

Chart 16: CAB



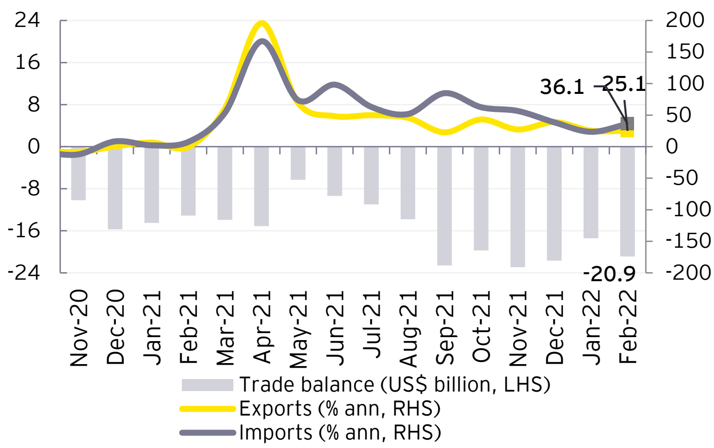
Source: Database on Indian Economy, RBI

B. Merchandise trade and exchange rate

Merchandise imports growth surged to 36.1% in February 2022 from 23.5% in January 2022 even as exports growth remained nearly stable at 25.1% in February 2022 resulting in widening of merchandise trade deficit to US$(-)20.9 billion.

- Merchandise exports growth was driven primarily by exports of oil, engineering goods and organic and inorganic chemicals. While growth in exports of engineering goods increased to 32.0% in February 2022 from 24.1% in January 2022, growth in oil and organic and inorganic chemicals exports marginally eased to 88.1% and 25.4% respectively from 95.2% and 25.8% over the same period.
- The surge in growth of merchandise imports in February 2022 reflected the rising global crude and commodity prices. Growth in imports of oil, coal, fertilizers and pearls and precious stones accelerated to 69.2%, 117.0%, 643.7% and 32.9% respectively in February 2022 from 26.9%, 39.5%, 167.4% and 6.0% in January 2022.
- Y-o-y growth in exports excluding oil, gold and jewelry moderated to 19.0% in February 2022 from 20.1% in January 2022 whereas growth in imports of this segment at 34.0% in February 2022 was close to its level at 33.6% in January 2022.
- Merchandise trade deficit widened to US$(-)20.9 billion in February 2022 from US$(-)17.4 billion in January 2022, due to the relatively higher growth in imports vis-à-vis exports.
- Services trade surplus fell to US$8.6 billion in February 2022 from US$11.1 billion in January 2022.
- The rupee depreciated to INR75.0 per US$ (average) in February 2022 from INR74.4 per US$ (average) in January 2022 partly due to pressures stemming from higher imports and net foreign investment outflows.

Chart 17: Developments in merchandise trade



Source: Ministry of Commerce and Industry, GoI

8. Global growth: OECD estimated worsening global growth and inflation due to geopolitical developments

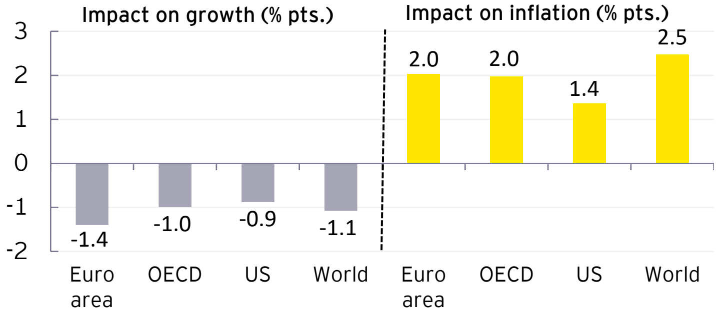
A. Global growth outlook by OECD

- As per the OECD (Interim Economic Outlook, March 2022), prior to the recent geopolitical developments, most key global macroeconomic variables such as growth and inflation were expected to normalize over 2023 following the COVID-19 pandemic.
- In OECD's assessment, if the recent trends in commodity prices and financial markets are sustained, global GDP growth could reduce by over 1% point and global CPI inflation could be pushed up by approximately 2.5% points over the one-year period beginning 24 February 2022 **(Chart 18)**.

The OECD has estimated a reduction in global GDP growth by over 1% point and an increase in CPI inflation by 2.5% points over the one-year period beginning 24 February 2022, if the ongoing geopolitical uncertainty persists.

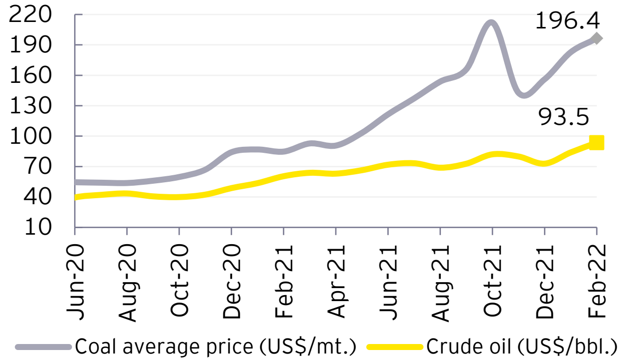
- The impact of the geopolitical uncertainty is expected to differ across regions. European economies are likely to be the worst hit with a fall of (-)1.4% points in growth and an increase of nearly 2% points in CPI inflation.
- The adverse impact on the growth in advanced economies (AEs) in the Asia-Pacific region and the Americas is expected to be comparatively less although weaker global demand and higher crude and commodity prices would have a dampening effect on household incomes and spending. Growth in the US is expected to be reduced by (-)0.9% points and inflation is expected to increase by 1.4% points.
- Growth outcomes in the emerging market economies (EMEs) reflect a balance between stronger output in some commodity-producing economies and deeper declines in the major commodity-importing economies. Higher food and energy prices are expected to push up inflation in EMEs by more than that in the AEs.
- Monetary policy has responded to the upturn in inflation across the world, with policy interest rates raised by a little over 1% point on average in major AEs and by 1.5% points in major EMEs.
- As per OECD's simulations, a well-targeted rise in final government spending of 0.5% of GDP for one year in all OECD economies could offset around half of the estimated decline in output without adding significantly to inflation.

Chart 18: OECD's simulated impact on growth and inflation*



Source: OECD Economic Outlook, Interim Report (March 2022)
*simulated impact on GDP (% change) and inflation (% points) over the 1-year period beginning 24 February 2022.

Chart 19: Global crude and coal prices



Source (basic data): World Bank, Pink Sheet, March 2022

B. Global energy prices: global crude price at US$93.5/bbl. in February 2022 was at its highest level since September 2014

- Average global crude price[13] at US$93.5/bbl. in February 2022 was at its highest level since September 2014 **(Chart 19)**. This was driven by supply disruptions caused by recent geopolitical developments. According to available information[14], Brent crude price is forecasted at US$135/bbl. in 2022 and at US$115/bbl. in 2023.
- Average global coal price[15] increased to a four-month high of US$196.4/mt. in February 2022 from US$182.7/mt. in January 2022 due to supply disruptions emanating from the geopolitical uncertainty[16].

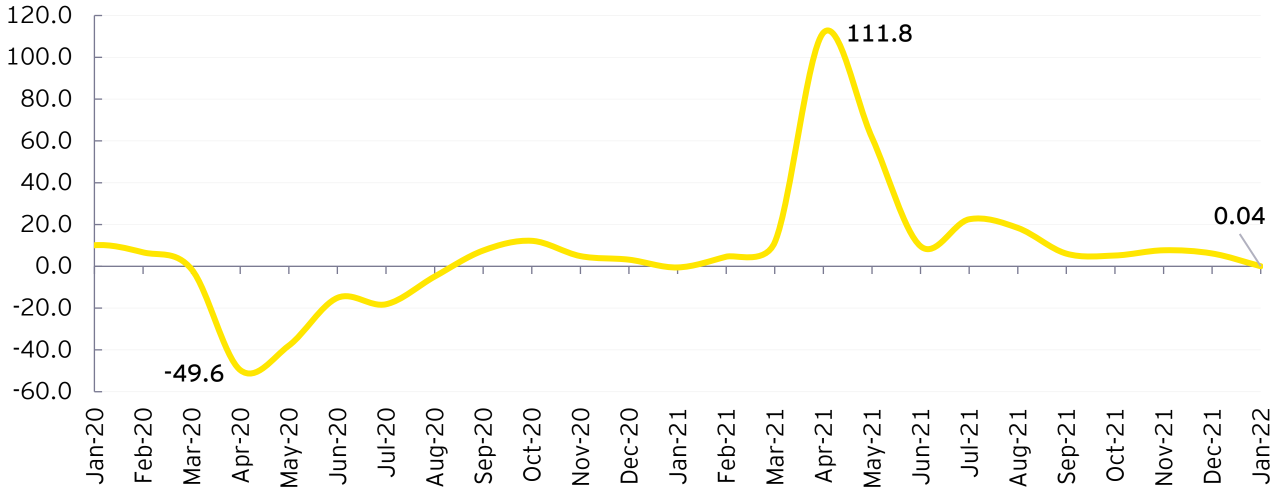
[13] Simple average of three spot prices, namely, Dated Brent, West Texas Intermediate and Dubai Fateh
[14] https://www.reuters.com/markets/europe/goldman-raises-oil-price-forecasts-russia-supply-shock-2022-03-08/
[15] Simple average of Australian and South African coal prices
[16] https://www.business-standard.com/article/economy-policy/global-coal-prices-at-record-high-to-increase-india-s-import-bill-122030701189_1.html

9. Index of Aggregate Demand (IAD): reflected sustained weakness in demand in January 2022

IAD showed a near zero growth in January 2022

- EY has 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 showed a muted growth of 0.04% in January 2022 as compared to 6.1% in December 2021, indicating continued weakness in demand conditions **(Chart 20** and **Table 9).**
- Demand conditions deteriorated across all the three key sectors in January 2022. In particular, demand conditions in the services sector deteriorated sharply in January 2022 as indicated by the services PMI. The deterioration in demand was relatively mild in the industrial sector during the month. Demand conditions in the agricultural sector, as measured by growth in agricultural credit off take, also moderated in January 2022.

Chart 20: Growth in IAD (y-o-y)



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

Table 9: IAD

Month	May-21	Jun-21	Jul-21	Aug-21	Sep-21	Oct-21	Nov-21	Dec-21	Jan-22
IAD	126.5	118.3	130.2	140.5	141.8	149.1	146.7	144.3	139.0
Growth (% y-o-y)	61.6	9.6	22.5	18.4	6.1	5.2	7.7	6.1	0.0
Growth in agr. credit	10.3	11.4	12.4	11.3	9.9	10.2	10.4	14.5	10.4
Mfg. PMI**	-0.9	-3.5	5.5	2.3	6.0	7.4	7.6	5.1	3.3
Ser. PMI**	-4.1	-10.7	-5.9	7.4	5.5	11.2	8.6	4.9	0.1

**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							
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
FY21	-8.6	-7.8	-9.8	-0.5	-7.0	FY21	50.2	41.7
4QFY21	6.0	-0.1	6.8	9.2	3.5	4QFY21	56.9	54.2
1QFY22	44.4	27.5	53.0	16.8	26.0	1QFY22	51.5	47.2
2QFY22	9.5	17.1	8.6	9.3	9.2	2QFY22	53.8	52.4
3QFY22	2.1	6.0	1.4	2.7	5.4	3QFY22	56.3	57.3
Oct-21	4.2	11.5	3.3	3.1	8.7	Nov-21	57.6	58.1
Nov-21	1.3	4.9	0.8	2.1	3.4	Dec-21	55.5	55.5
Dec-21	0.7	2.6	0.2	2.8	4.1	Jan-22	54.0	51.5
Jan-22	1.3	2.8	1.1	0.9	3.7	Feb-22	54.9	51.8

Source: MoSPI, 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				
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
FY21	6.2	7.7	2.7	5.5	1.3	4.0	2.8	-8.0	2.2
4QFY21	4.9	3.5	3.9	5.9	5.1	2.9	6.5	2.5	6.3
1QFY22	5.6	4.0	10.8	6.1	12.0	7.5	10.5	28.8	9.9
2QFY22	5.1	2.6	13.0	6.0	11.7	3.6	11.5	28.2	11.3
3QFY22	5.0	2.2	12.9	6.2	14.3	6.8	12.0	40.4	12.2
Nov-21	4.9	1.9	13.3	6.3	14.9	6.8	12.3	44.4	12.7
Dec-21	5.7	4.0	11.0	6.2	14.3	9.4	10.7	38.1	11.1
Jan-22	6.0	5.4	9.3	6.0	13.0	9.6	9.4	32.3	9.7
Feb-22	6.1	5.9	8.7	5.9	13.1	8.5	9.8	31.5	10.0

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
FY 19 (CGA)	8.4	16.2	13.1	14.9	3.0	3.4	2.4
FY20 (CGA)	-3.4	-16.1	4.0	-7.8	1.7	4.7	3.3
FY21 (CGA)	0.7	-17.9	-2.3	-10.7	12.7	9.2	7.3
FY22 (RE over budget actuals)	24.1	38.7	26.2	32.3	17.0	6.9	4.7
FY 23 (BE over FY 22 RE)	9.6	13.4	13.8	13.6	5.7	6.4	3.8
	Cumulated growth (%, y-o-y)					% of budgeted target	
Jun-21	97.1	128.2	97.5	111.8	85.2	18.2	14.9
Jul-21	83.1	171.5	76.7	111.8	64.8	21.3	18.1
Aug-21	70.5	159.7	69.3	101.4	52.1	31.1	27.3
Sep-21	64.2	105.1	64.7	83.9	48.1	35.0	27.7
Oct-21	55.8	91.6	53.3	70.9	44.0	36.3	27.5
Nov-21	50.3	90.4	47.2	66.3	38.6	46.2	38.8
Dec-21	44.2	66.5	50.5	58.7	31.5	47.7$	36.4$
Jan-22	38.5	63.8	48.3	56.1	24.1	58.9$	48.6$

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 a proportion of revised estimate

Fiscal year/month	CGST	UTGST	IGST	GST compensation cess	Total GST (Center)
	INR crore				
FY 2022 (RE)	5,70,000	-	-	1,05,000	6,75,000
FY 2023 (BE)	6,60,000	-	-	1,20,000	7,80,000
Monthly tax collection (INR crore)					
Jun-21	33,696	170	6,377	6,565	46,808
Jul-21	47,901	254	-3,733	7,530	51,952
Aug-21	53,326	289	-16,195	8,474	45,894
Sep-21	47,379	222	-634	8,489	55,456
Oct-21	48,546	140	8,970	8,221	65,877
Nov-21	49,238	118	7,238	9,442	66,036
Dec-21	46,227	254	14,635	9,141	70,257
Jan-22	69,662	432	-27,918	9,456	51,632

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
Mar-21	4.00	FY18	7.5	7.5	30.3	22.1	FY18	21.8	9.2	7.05	424.4
Apr-21	4.00	FY19	13.7	8.9	30.7	-0.6	FY19	13.6	10.5	7.69	411.9
May-21	4.00	FY20	9.4	9.9	43.0	1.4	FY20	11.2	8.9	6.83	475.6
Jun-21	4.00	FY21	6.1	11.0	44.0	36.1	FY21	16.2	12.2	6.05	579.3
Jul-21	4.00	4QFY21	6.0	11.5	2.7	7.3	4QFY21	16.2	12.2	6.16	579.3
Aug-21	4.00	1QFY22	5.8	10.1	11.7	0.4	1QFY22	15.4	10.7	6.26	609.0
Sep-21	4.00	2QFY22	6.5	9.5	9.5	3.9	2QFY22	11.4	9.3	6.23	638.6
Oct-21	4.00	3QFY22	7.7	10.6	4.4	-6.3	3QFY22	11.5	9.3	6.38	633.6
Nov-21	4.00	Oct-21	6.8	9.9	1.9	-2.7	Nov-21	12.3	9.5	6.35	637.7
Dec-21	4.00	Nov-21	7.0	9.8	1.6	-0.04	Dec-21	11.5	9.3	6.44	633.6
Jan-22	4.00	Dec-21	9.2	12.2	0.9	-3.6	Jan-22	10.1	8.4	6.69	629.8
Feb-22	4.00	Jan-22	8.2	8.3	5.9	-4.9	Feb-22	11.6	8.7	6.71	631.5

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		
FY18	10.6	20.9	-159.0	64.5	55.7	90.8	2012	3.5	1.2	5.4
FY19	8.6	10.6	-182.3	69.9	67.3	100.4	2013	3.5	1.4	5.1
FY20	-5.1	-8.2	-157.4	70.9	58.5	70.4	2014	3.5	2.1	4.7
FY21	-7.2	-16.7	-101.2	74.2	43.8	67.2	2015	3.4	2.4	4.3
4QFY21	19.4	18.7	-41.5	72.9	59.3	88.1	2016	3.3	1.8	4.5
1QFY22	85.9	108.7	-30.8	73.8	67.1	105.1	2017	3.8	2.5	4.8
2QFY22	38.5	66.5	-47.4	74.1	71.7	152.3	2018	3.5	2.2	4.5
3QFY22	36.6	51.4	-64.3	74.9	78.3	170.3	2019	2.8	1.6	3.7
Nov-21	27.2	56.6	-22.9	74.5	79.9	142.7	2020	-3.1	-4.5	-2.0
Dec-21	38.9	38.5	-21.7	75.4	72.9	156.1	2021	5.9	5.0	6.5
Jan-22	25.3	23.5	-17.4	74.4	83.9	182.7	2022*	4.4	3.9	4.8
Feb-22	25.1	36.1	-20.9	75.0	93.5	196.4	2023*	3.8	2.6	4.7

Source: Database on Indian Economy - RBI, Pink Sheet - World Bank and IMF World Economic Outlook October 2021 and January 2022.
* forecasts for 2022 and 2023 are sourced from the WEO Update released in January 2022.

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
FY19 (3rd RE)	5.8	2.1	-0.8	5.4	7.9	6.5	7.2	7.0	7.5	4.7
FY20 (2nd RE) $	3.8	5.5	-1.5	-2.9	2.2	1.2	5.9	6.7	6.3	2.9
FY21(1st RE) $	-4.8	3.3	-8.6	-0.6	-3.6	-7.3	-20.2	2.2	-5.5	3.3
FY22(SAE)*	8.3	3.3	12.6	10.5	7.8	10.0	11.6	4.3	12.5	9.2
3QFY20	3.2	4.9	-3.5	-3.3	-3.1	-1.1	6.6	4.8	6.9	3.0
4QFY20	3.3	7.5	-1.3	-4.6	2.7	1.8	5.1	4.2	7.6	3.0
1QFY21	-21.4	3.0	-17.8	-31.5	-14.8	-49.4	-49.9	-1.1	-11.4	2.3
2QFY21	-5.9	3.2	-7.9	5.2	-3.2	-6.6	-18.8	-5.2	-10.2	1.7
3QFY21	2.1	4.1	-5.3	8.4	1.5	6.6	-10.1	10.3	-2.9	3.4
4QFY21	5.7	2.8	-3.9	15.2	3.2	18.3	-3.4	8.8	1.7	5.2
1QFY22	18.4	3.5	17.6	49.0	13.8	71.4	34.3	2.3	6.3	7.3
2QFY22	8.4	3.7	14.2	5.6	8.5	8.2	9.5	6.2	19.5	9.1
3QFY22	4.7	2.6	8.8	0.2	3.7	-2.8	6.1	4.6	16.8	10.4

Source: National Accounts Statistics, MoSPI
$ Growth numbers for FY21 are based on the first revised estimates (RE) of NAS released by the MoSPI on 31 January 2022 over the second RE of NAS for FY20, *FY22 growth numbers are based on the SAE released on 28 February 2022 over the first revised estimates for 2021 released on 31 January 2022.

Fiscal year/quarter	Expenditure components						IPD inflation
	GDP	PFCE	GFCE	GFCF	EX	IM	GDP
FY19 (3rd RE)	6.5	7.1	6.7	11.2	11.9	8.8	3.9
FY20 (2nd RE) $	3.7	5.2	3.4	1.6	-3.4	-0.8	2.4
FY21(1st RE) $	-6.6	-6.0	3.6	-10.4	-9.2	-13.8	5.6
FY22(FAE)*	8.8	4.1	11.0	17.4	23.0	29.5	7.7
3QFY20	3.1	5.6	4.8	-0.1	-5.5	-7.0	2.3
4QFY20	2.7	1.2	8.0	0.6	-9.1	-2.4	4.3
1QFY21	-23.8	-23.7	13.6	-45.3	-25.5	-41.1	2.9
2QFY21	-6.6	-8.3	-22.9	-4.5	-6.4	-17.9	4.0
3QFY21	0.7	0.6	-0.3	-0.6	-8.6	-5.2	5.4
4QFY21	2.5	6.5	29.0	10.1	3.7	11.7	9.2
1QFY22	20.3	14.2	-4.4	62.5	40.4	60.7	10.5
2QFY22	8.5	10.2	9.3	14.6	20.5	40.7	10.0
3QFY22	5.4	7.0	3.4	2.0	20.9	32.6	9.8

Source: National Accounts Statistics, MoSPI
$ Growth numbers for FY21 are based on the first revised estimates (RE) of NAS released by the MoSPI on 31 January 2022 over the second RE of NAS for FY20, *FY22 growth numbers are based on the SAE released on 28 February 2022 over the first revised estimates for 2021 released on 31 January 2022.

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 advance 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	FRL	Fiscal Responsibility Legislation
31	FY	fiscal year (April–March)
32	GDP	Gross Domestic Product
33	GFCE	government final consumption expenditure
34	GFCF	gross fixed capital formation
35	GoI	Government of India
36	G-secs	government securities
37	GST	Goods and Services Tax
38	GVA	gross value added
39	IAD	Index of Aggregate Demand

Sr. no.	Abbreviations	Description
40	IBE	interim budget estimates
41	ICRIER	Indian Council for Research on International Economic Relations
42	IEA	International Energy Agency
43	IGST	Integrated Goods and Services Tax
44	IIP	Index of Industrial Production
45	IMF	International Monetary Fund
46	IMI	Index of Macro Imbalance
47	IMP	imports
48	INR	Indian Rupee
49	IPD	implicit price deflator
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	WHO	World Health Organization
76	WPI	Wholesale Price Index
77	y-o-y	year-on-year
78	1HFY20	first half of fiscal year 2019-20, i.e., April 2019-September 2019

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