



FICCI Economic Outlook Survey

January 2011

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FICCI Economic Outlook Survey – January 2011

About the Survey

The fifth round of FICCI's Economic Outlook Survey was conducted during December 29, 2010 to January 18, 2011. As part of the survey, a structured questionnaire was drawn up and sent to key economists with a view to gauge their perception and views on topical economic issues as well as to seek their outlook for key macro-economic variables. 11 economists of repute participated in the survey. These economists largely come from the banking and financial sector. The sample also includes economists from industry and research institutions.

The economists were asked to provide their **forecast for key macro economic variables for the year 2010-11** as well as for **Quarter 3 (Oct-Dec) of 2010-11 and Quarter 4 (Jan-Mar) of 2010-11**.

In addition to these, FICCI sought the views of economists on three topical issues – **outlook for inflation and corrective measures to curb inflation; expected monetary policy action by RBI in the forthcoming monetary policy review and fiscal situation of India**.

The feedback received from the participating economists was aggregated and analyzed. The results obtained are presented in the following pages.

The findings of the survey represents the views of the leading economists and do not reflect the views of FICCI.



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Executive Summary

Annual Forecasts for 2010-11

- ♣ GDP growth – 8.7 percent
- ♣ Agriculture and allied activities growth – 4.4 percent
- ♣ Industry growth – 8.6 percent
- ♣ Services growth – 9.6 percent
- ♣ Fiscal Deficit – 5.3 percent of GDP
- ♣ IIP – 8.7 percent
- ♣ WPI inflation rate (End March 2011) – 7.0 percent
- ♣ USD / INR exchange rate (End March 2011) – Rs. 44.5/USD
- ♣ Bank credit growth – 21.3 percent

Quarterly Forecasts for Q3 of 2010-11 and Q4 of 2010-11

- ♣ GDP growth – 8.7 percent (Q3, 2010-11) and 8.2 percent (Q4, 2010-11)
- ♣ Agriculture and allied activities growth – 5.4 percent (Q3, 2010-11) and 5.0 percent (Q4, 2010-11)
- ♣ Industry growth* – 7.3 percent (Q3, 2010-11) and 6.5 percent (Q4, 2010-11)
- ♣ Services growth – 9.9 percent (Q3, 2010-11) and 9.5 percent (Q4, 2010-11)
- ♣ IIP* – 6.5 percent (Q3, 2010-11) and 6.1 percent (Q4, 2010-11)
- ♣ WPI inflation rate – 7.0 percent (Q4, 2010-11)
- ♣ USD / INR exchange rate – Rs. 44.5 / USD (Q4, 2010-11)

* The downward revision in the quarterly forecasts of growth of Industry sector and IIP growth are a reflection of hardening raw material prices and rising cost of capital which are impacting the growth of industrial sector in India.

Executive Summary

Economists' views on

♣ Expected monetary policy action by RBI

- ✚ There was a consensus amongst all economists that RBI would continue to move ahead on its path of monetary tightening and would hike both the repo and the reverse repo rate in the forthcoming monetary policy review on January 25, 2011. Most of them expect RBI to hike both these rates by 25 basis points.
- ✚ The hike in policy rates (repo and reverse repo) is expected by all economists on the grounds that inflationary pressures are still looming large on the Indian economy and it is one of the key responsibilities of RBI to ensure price stability in the country. The upside risks to inflation such as rising global commodity prices and crude oil prices could pose a significant challenge. The robust GDP growth which can lead to a wage-price spiral and higher input costs could further add pressure on the inflation front. The economists feel that all these factors taken together would force RBI to hike the policy rates.
- ✚ However, given the present level of liquidity conditions, RBI is expected to maintain a status quo with regards to CRR.

♣ Outlook for inflation

- ✚ Majority of the economists expect inflation to remain a reason for concern throughout the calendar year 2011. The moderation in inflation indices is only seasonal in nature and there are many economists who expect the pressures on inflation front to continue through the current year.
- ✚ Headline inflation is not expected to come down significantly in the near future due to several reasons:
 - Global food supplies to India have been adversely affected due to natural calamities in some parts of the world.
 - The impact of the post harvest relief witnessed would fade away leading to a further rise in prices.
 - There is a risk of a possible spillover of higher international commodity prices as well as firmed up global food prices.
 - Rising global crude prices will be passed through to the consumers in India.



- Rising domestic commodity prices and supply constraints in several sectors can drive up the non-food manufacturing inflation.
- Aggregate demand pressures due to rise in rural incomes, change in consumption patterns, supply bottlenecks and stagnant output and productivity levels in agriculture would continue to keep food articles inflation high and sticky.
- ✚ While this is the majority view, some economists do expect inflation to moderate in the coming months primarily due to a higher base effect along with the positive impact of the active intervention undertaken by both the government and RBI to combat the mounting inflationary expectations.
- ✚ The corrective steps suggested by the surveyed economists in order to bring down inflation covers both the short term and long term. The immediate/short term measures that need to be undertaken to bring down prices are:
 - Urgent need to take firm action against hoarding and black marketing as has been done in China.
 - Implementation of the amended APMC act so that farmers are permitted to sell their produce to private buyers as against only to the government.
 - Infrastructure for storage and transportation of food products should be put in place – refrigerated trucks/vans, food processing units, involvement of corporates in farming and marketing etc.
- ✚ The long term measures suggested to tame inflation have been given with a view that inflation has now become somewhat structural in nature and more so a supply side issue.
 - Removal of supply side bottlenecks to increase food supply and curb the persistent rise in food articles inflation. There is a need to open more procurement and distribution centers, thereby making food grains and horticultural products easily accessible to the masses. Also farmers should be encouraged to deal with these procurement centers directly.
 - Encourage more public private partnership to make investments in agriculture infrastructure especially in opening of more cold storages across country.
 - Every state of India must increase their spending on agriculture especially in areas like irrigation, power and rural connectivity to increase farm productivity in the medium run and to ensure that we have a higher quantum of production.
- ♣ Although a policy rate hike is anticipated by all economists, it has also been pointed out that to address the inflation issue in the long run, addressing the supply side problems are most essential. Taking note of this, it is important to highlight that successive monetary policy tightening would not help in cooling down inflation as it is a supply side phenomenon. It



would rather have a dampening effect on the industrial growth of the economy and may induce a slowdown in the manufacturing sector as the cost of capital further rises.

♣ Fiscal Situation of India

- ✚ Majority of the surveyed economists believe that India would be able to achieve its budgeted target of fiscal deficit in the year 2010-11. Most of them actually expect it to be slightly lower than the estimated level of 5.5 percent in the current fiscal.
- ✚ The fiscal deficit target for the year 2010-11 is attainable on account of the following factors-
 - A one-off hike in the revenue generation of the government through the 3G/BWA auctions. The highly successful auctioning of 3G and BWA auctions have ensured a total revenue of approximately Rs. 1,06,262 crore for the central government.
 - The government has also generated a large quantum of resources through disinvestments in PSUs. Dilution of stakes has already taken place in Satluj Jal Vidyut Nigam, Coal India, Power Grid and Engineers India in the current fiscal which has resulted in a mop up nearly Rs. 25,000 crore for the government. In its bid to achieve its target of Rs. 40,000 crore for the current year more disinvestment are lined up.
 - Overall economic activity has picked up and improved industrial activity has led to higher indirect tax collections. Indirect tax collections went up by 42.8 per cent to Rs 2,37,192 crore in April-December period this financial year, against Rs 1,66,133 crore in the corresponding months of 2009-10.
 - Control over expenditure by the government for example reduction in petroleum subsidy following the decontrol of petrol prices has also helped in curbing expenditure.
- ✚ While this year's fiscal situation is comfortable, the next year is what most economist are worried about. According to most of the surveyed respondents the fiscal consolidation in the next two years could come under pressure since government's expenditure is on the rise (rising subsidy bills: higher food subsidies under the Food Security Act and potentially higher oil subsidies if crude rises further).
- ✚ Though this is the majority view, a few respondents opined that given the proposed plans of disinvestments and current pace of GDP growth, the fiscal deficit targets for the years 2011-12 and 2012-13 are achievable.



- ✚ Steps that need to be taken by the government to focus on fiscal consolidation and achieving the FRBM targets are:
 - A revamp of the subsidy bill especially the food and fuel so that the benefits reach the intended beneficiaries only. A cut back on the oil subsidy bill through diesel price deregulation would also benefit immensely.
 - Tax reforms need to be introduced which would be vital for further progress on the path of fiscal consolidation.
 - Need to follow an approach of targeted spending and cutting down wasteful expenditure.



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✿ Annual Forecasts for 2010-11¹

- ✚ The economists who participated in the fifth round of FICCI's Economic Outlook Survey have revised upwards their forecast for **GDP growth rate (at factor cost) for the fiscal year 2010-11 to 8.7 percent** from 8.5 percent made in the last survey (October 2010). The range of the forecast for GDP growth lies between a minimum of 8.4 percent and a maximum of 8.9 percent.
- ✚ The sector wise division of GDP growth estimate for the year 2010-11 shows that **agriculture and allied activities will grow at rate of 4.4 percent**, which is the same as forecasted in the previous survey. The primary sector's growth forecast varied from 3.5 percent to 5.6 percent.
- ✚ The surveyed economists expect the **industry sector to grow at the rate of 8.6 percent during 2010-11**. It is interesting to note that the economists have been revising downwards their estimates for industry sector growth since the last two surveys. The estimates have been lowered from 10 percent in July 2010 survey to 9.1 in October 2010 survey to the present level of 8.6 percent in the current survey. The range for industry sector growth is 7.1 percent to 9.4 percent.
- ✚ The **services sector growth is pegged at 9.6 percent in 2010-11** by the survey respondents. The service sector growth estimates lie between a minimum of 9.4 percent and a maximum of 10.1 percent.
- ✚ The projected **fiscal deficit of the centre for fiscal year 2010-11 is 5.3 percent** which is marginally lower than the last survey's projection of 5.5 percent. The projections lie between the range of 5 percent and 5.8 percent.
- ✚ The participating economists anticipate that **IIP would mark a growth of 8.7 percent during 2010-11** as against the previous survey forecast of 9 percent. Similar to the trend seen in industry sector growth, forecasts of IIP growth have also seen a downward revision since the past two surveys.

¹ All forecast figures indicated are the median forecast of the sample



- ✚ The forecast for **WPI inflation has been revised upwards to 7 percent by end March 2011** from 6.3 percent in the earlier survey. The **CPI (IW) inflation is pegged at a higher rate of 8.1 percent**. The estimates of WPI inflation rate vary between 6 percent and 8 percent while that for CPI (IW) inflation rate vary between 7.6 percent and 10.5 percent.
- ✚ The surveyed economists see **money supply (M3) growth to be around 16.9 percent during 2010-11**. The range for M3 growth has narrowed down to lie between 15 percent and 18.5 percent.
- ✚ The median forecast for **merchandise export growth and merchandise import growth** for the year **2010-11 is 21.3 percent and 19 percent** respectively.
- ✚ **For 2010-11, the trade balance** is perceived to stand at **-8.8 percent of the GDP** by the respondent economists. The projection is a downward revision from last survey's figure of 9.6 percent.
- ✚ The economists expect that **bank credit would grow by 21.3 percent** in the current fiscal as against 19.0 percent in the previous forecast.



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♣ Quarterly Forecasts for Q3 (Oct-Dec) of 2010-11² and Q3 (Jan-Mar) of 2010-11³

- ✚ Economists estimate the **GDP growth (at factor cost) for the third quarter (Q3) of 2010-11 to be 8.7 percent** and then move down to **8.2 percent during the fourth quarter (Q4) of 2010-11.**
- ✚ The sectoral break-up of GDP growth projections indicate that **agriculture and allied activities expected to grow robustly at 5.4 percent and 5 percent respectively during Q3 and Q4 of 2010-11.**
- ✚ The participating economists foresee a lower growth for the industry sector. **The industry sector is estimated to mark a growth of 7.3 percent in quarter 3 of 2010-11** and then further slow down to **6.5 percent in quarter 4 of 2010-11.**
- ✚ The **services sector is projected to grow at 9.9 percent during Oct- Dec 2010-11** and then slide down to **9.5 percent in quarter 4 of 2010-11.** It is important to note that the survey respondents feel that all the three sectors as well as overall GDP growth will grow slower in Q4 of 2010-11 vis-à-vis Q3 of 2010-11.
- ✚ The economists expect the **IIP to clock a growth rate of only 6.5 percent during Q3, 2010-11** and then fall further to **6.1 percent in Q4, 2010-11.**
- ✚ The surveyed economists expect **WPI inflation rate to be 7 percent in Q4 of the current fiscal year 2010-11.** They also anticipate a fall in the **CPI (IW) inflation rate from 9 percent in the third quarter to 8.3 percent in fourth quarter of 2010-11.**
- ✚ The survey respondents foresee **export growth at 19 percent during Q3 of 2010-11** and marginally lower at **18 percent during Q4 of 2010-11.** **Import growth** is projected to see a steep decline from **21 percent in Q3 of 2010-11 to 14 percent in Q4 of 2010-11.**
- ✚ The forecasters predict that **exchange rate** of Rupee would be around **44.5 per USD in Q4 of 2010-11.**

² All forecast figures indicated are the median forecast of the sample. Sample size varies as not all participants provided quarterly projections and for all variables

³ All forecast figures indicated are the median forecast of the sample. Sample size varies as not all participants provided quarterly projections and for all variables

♣ Economists' views on expected monetary policy action by RBI on January 25, 2011

With an aim to tame inflation, the Reserve bank of India has been actively tightening its monetary policy throughout the whole of last year. Even though the latest numbers on WPI inflation show some relief from the double digit inflation levels experienced in the start of the fiscal year, it is still significantly higher than the comfort zone of the RBI. Due to successive hikes in policy rates, liquidity management is also emerging as a key challenge. In this backdrop, FICCI asked the survey participants on what they thought RBI would do in the forthcoming monetary policy review on January 25, 2011.

The responses received show that there is consensus amongst all the economists that RBI would undertake another round of monetary tightening in the upcoming policy review. The majority of them expect the central bank to hike the repo rate and the reverse repo rate by 25 basis points each. Given the present level of liquidity conditions, RBI is expected to maintain a status quo with regards to CRR.

The moderate hike in policy rates (repo and reverse repo) has been expected by all the participating economists on the grounds that inflationary pressures are still looming large on the Indian economy and it is one of the key responsibilities of RBI to ensure price stability in the country. There are upside risks to inflation both from the global front as well domestic front. Rising commodity and crude oil prices could pose a significant challenge in the medium to long term. Further with the Indian economy growing at 8.9 percent in the first half of 2010-11, GDP growth is expected to remain robust. This could further add pressure on the inflation situation as it could lead to a wage-price spiral and a rise input costs. With the core inflation remaining sticky at around 5-5.4 percent, the demand side pressures are well indicated. The economists feel that all these factors taken together would force RBI to hike the policy rates.

There are a few economists who expect that RBI will continue on its path of monetary policy tightening throughout the calendar year of 2011 given the not so benign outlook for inflation in the months ahead.

❁ Economists' views on outlook for inflation

The Indian economy reached its pre-crisis growth trajectory much ahead of the other economies of the world. However it has been facing increasing inflationary pressure ever since. A mix of administrative measures and withdrawal of accommodative monetary policy stance has been used to curb inflation. After remaining in the double digits for the first 4 months of the current fiscal year it showed some signs of moderation before rising again to 8.43 percent in December 2010. The sustained increase in prices of food articles is the most important concern for all stakeholders. The latest available weekly data shows that food inflation in India has moderated for the second week in a row in January after spiking to nearly a two-year peak in end of December. FICCI asked the participating economists whether they expect this moderation in inflation to last and if not then what corrective steps do they suggest to tame inflation.

The survey results show that the majority of the economists expect inflation to remain a concern throughout the calendar year 2011. Moderation in inflation indices is only seasonal in nature and there are many economists who expect the pressures on inflation front to continue through the current year. The broad reasons which the economists feel are likely to prevent the headline inflation from coming down significantly in the near future are:

- ❁ Global food supplies to India have been adversely affected due to natural calamities in some parts of the world.
- ❁ The impact of the post harvest relief witnessed would fade away leading to a further rise in prices.
- ❁ There is a risk of a possible spillover of higher international commodity prices as well as firmed up global food prices.
- ❁ Rising global crude prices will be passed through to the consumers in India.
- ❁ Rising domestic commodity prices and supply constraints in several sectors can drive up the non-food manufacturing inflation
- ❁ Aggregate demand pressures due to rise in rural incomes, change in consumption patterns, supply bottleneck and stagnant output and productivity in agriculture would continue to keep the primary food inflation high and sticky.

While this is the majority view, some economists do expect that inflation would moderate in the coming months primarily due to a higher base effect along with the positive impact of the



active intervention undertaken by both the government and RBI to combat the mounting inflationary expectations.

The corrective steps suggested by the surveyed economists in order to bring down inflation covers both the short term and long term. The immediate/short term measures that need to be undertaken to bring down prices are:

- ✚ Urgent need to take firm action against hoarding and black marketing as has been done in China.
- ✚ Implementation of the amended APMC act so that farmers are permitted to sell their produce to private buyers as against only to the government.
- ✚ Infrastructure for storage and transportation of food products should be put in place – refrigerated trucks/vans, food processing units, involvement of corporates in farming and marketing etc.

The long term measures that have been suggested by the participating economists have been given with a view that inflation has now become somewhat structural in nature and more so a supply side issue. The following steps have been recommended:

- ✚ Removal of supply side bottlenecks to increase food supply and curb the persistent rise in food articles inflation. There is a need to open more procurement and distribution centers, thereby making food grains and horticultural products easily accessible to the masses. Also farmers should be encouraged to deal with these procurement centers directly.
- ✚ Encourage more public private partnership to make investments in agriculture infrastructure especially in opening of more cold storages across country.
- ✚ Every state of India must increase their spending on agriculture especially in areas like irrigation, power and rural connectivity to increase farm productivity in the medium run and to ensure that we have a higher quantum of production.

In short the need of the hour to combat high inflation is to launch a second green revolution to increase agricultural production and productivity in the country.

♣ **Economists' views on fiscal situation of India**

The Indian economy embarked upon the path of fiscal consolidation with the enactment of the FRBM act in 2003. However, amidst the global economic meltdown of 2008, the government introduced a fiscal stimulus package to support its economy, which led to a deviation from the FRBM targets. In 2009-10, the central government's fiscal deficit touched a high of 6.9 percent. The Union Budget of 2010-11, put in place some targets to bring down the fiscal deficit in the next 3 years. The fiscal deficit for the current fiscal has been pegged at 5.5 percent while it is projected to go down to 4.8 percent and 4.1 percent in 2011-12 and 2012-13 respectively. In light of this, we asked the survey participants to share their views on the fiscal situation of India and whether the projected fiscal deficit targets are achievable.

The feedback received shows that majority of the surveyed economists believe that India would be able to achieve its budgeted target of fiscal deficit in the year 2010-11. Most of them actually expect it to be slightly lower than the estimated level of 5.5 percent in the current fiscal. According to the set of survey participants, the fiscal deficit target for the year 2010-11 is attainable on account of the following factors-

- ♣ A one-off hike in revenue generation for the government through the 3G/BWA auctions. The highly successful auctioning of 3G and BWA auctions have ensured a total revenue of approximately Rs. 1,06,262 crore for the central government.
- ♣ The government has also been able to generate large quantum of resources through disinvestments in PSUs. The government has already undertaken dilution of its stakes in Satluj Jal Vidyut Nigam, Coal India, Power Grid and Engineers India in the current fiscal mopping up nearly Rs. 25,000 crore. In its bid to achieve its target of Rs. 40,000 crore for the current year more disinvestment are lined up.
- ♣ Overall economic activity has picked up and improved industrial activity has led to higher indirect tax collections. Indirect tax collections went up by 42.8 per cent to Rs 2,37,192 crore in April-December period this financial year, against Rs 1,66,133 crore in the corresponding months of 2009-10.
- ♣ Control over expenditure by the government for example reduction in petroleum subsidy following the decontrol of petrol prices has also helped in curbing expenditure.

While this year's fiscal situation is comfortable due to a surge in revenues because of the windfall gains, the next years are what most economist are worried about. According to most of the economists the fiscal consolidation in the next two years could come under pressure since



government's expenditure is on the rise (rising subsidy bills: higher food subsidies under the Food Security Act and potentially higher oil subsidies if crude rises further) and there would not be an adequate cushioning for the government's expenditure. If the government wants to achieve the FD targets it would need to be extremely stringent with respect to its expenditure since incomes can vary according to the state of the economy (especially the PSU disinvestments which depends on general market and global conditions).

Though the above is the majority view, a few respondents opined that given the proposed disinvestment plan and current pace of GDP growth, the fiscal deficit targets for the fiscal year 2011-12 and 2012-13 are achievable.

The following suggestions have been made by the participating economists on the steps that need to be taken by the government to focus on fiscal consolidation and achieve the FRBM targets:

- ✚ A revamp of the subsidy mechanism especially the food and fuel subsidy that would ensure the benefits reach the intended beneficiaries only. A cut back on the oil subsidy bill through diesel price deregulation would also benefit immensely.
- ✚ Tax reforms need to be introduced which would be vital for further progress on the path of fiscal consolidation.
- ✚ Need to follow an approach of targeted spending and cutting down wasteful expenditure.

♣ **Annual Forecasts for 2010-11**

Key Macroeconomic Variables	Annual Forecast 2010-11			
	Mean	Median	Max	Min
1 GDP growth rate at factor cost (%)	8.7	8.7	8.9	8.4
<i>Agriculture & Allied</i>	4.5	4.4	5.6	3.5
<i>Industry</i>	8.4	8.6	9.4	7.1
<i>Services</i>	9.7	9.6	10.1	9.4
2 Fiscal Deficit (as % to GDP) Centre	5.4	5.3	5.8	5.0
3 Growth in IIP (%)	8.8	8.7	10.0	7.8
4 WPI Inflation rate (%) (End March 2011)	7.0	7.0	8.0	6.0
5 CPI-IW Inflation rate (%) (End March 2011)	8.4	8.1	10.5	7.6
6 Money Supply (M3) growth (%)	16.9	16.9	18.5	15.0
7 Merchandise Export growth (%)	20.9	21.3	26.0	12.0
8 Merchandise Import growth (%)	20.3	19.0	27.4	14.0
9 Trade Balance (% to GDP)	9.4	8.8	14.0	7.8
10 US\$ / INR exchange rate (End March 2011)	44.5	44.5	45.5	43.5
11 Bank credit growth (%)	20.9	21.3	24.0	18.0

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♣ Quarterly Forecasts for Q3 (Oct-Dec) of 2010-11 and Q4 (Jan-Mar) of 2010-11

Key Macroeconomic Variables		Quarterly Forecasts							
		2010-11 Q3 (Oct-Dec)				2010-11 Q4 (Jan-Mar)			
		Mean	Median	Max	Min	Mean	Median	Max	Min
1	GDP growth rate at factor cost (%)	8.6	8.7	9.1	8.0	8.3	8.2	9.2	7.8
	<i>Agriculture & Allied</i>	5.6	5.4	7.5	3.8	5.2	5.0	8.3	3.3
	<i>Industry</i>	7.3	7.3	9.0	5.3	6.5	6.5	8.5	4.2
	<i>Services</i>	10.0	9.9	11.2	9.4	9.7	9.5	10.6	8.8
2	Growth in IIP (%)	6.7	6.5	9.5	3.7	5.6	6.1	10.5	-1.6
3	WPI Inflation rate (%)	8.2	8.2	9.0	7.8	7.0	7.0	8.0	5.2
4	CPI-IW Inflation rate (%)	9.0	9.0	9.5	8.6	8.2	8.3	9.2	7.4
5	Merchandise Export growth (%)	21.6	19.0	31.4	12.0	15.7	18.0	22.0	4.0
6	Merchandise Import growth (%)	19.0	21.0	38.6	5.0	16.4	14.0	33.3	7.0
7	US\$ / INR exchange rate					44.4	44.5	44.5	44.0

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