



STUDY NOTE - 4

INDIAN SCENARIO – ECONOMIC SURVEY

This Study Note includes:

- **Government policies**
- **Government finances**
- **Public – Private sector investments**
- **Balance of payments**
- **Outlook**

INDIAN SCENARIO – ECONOMIC SURVEY

For four years in succession global economic activity has been buoyant and it is reasonable to believe that the current year 2007-2008 will also continue to maintain the growth momentum. The global economic growth accelerated from 4.9% during 2005 to 5.5% in 2006 and average 4.9% per annum during the four year period 2003-2006. In this environment of strong global growth the real GDP growth in India is increased to 9.4% in 2006-2007 from 9.0% in 2005-2006. The real GDP growth averaged at 7.6% per annum during the 10th five-year plan period (2002-2003 to 2006-2007). Growth in per- capita income increased from 7.4% in 2005-2006 to 8.4% during 2006-2007. Per-capita income growth averaged at 6.1% per annum during the tenth plan period and 7.1% per annum during the last four years. Domestic savings, investments and productivity gains, are amply supporting this robust economic activity. This sustained growth has been possible due to proactive policy measures taken by the government of India to improve the productivity and competitiveness of the Indian economy. The policies enunciated in the various sectors of the economy - real, fiscal, external, monetary and financial.

1. Real sector policies

a. Agriculture and allied activities

Agriculture sector has remained a problem area and there has been a deceleration in its growth. To arrest this trend and reverse the deceleration number of policy inputs has been made. A National Rain fed Area Authority (NRAA) has been created in November 2006 to support up gradation and management of dry land and rain fed agriculture. The authority would coordinate all schemes relating to watershed development and other aspects of land use. The accelerated irrigation benefit programme is also being revamped to repair, renovate and restore water bodies in various states. For improved productivity in the agricultural sector an action plan has been formulated product specific. Like the green revolution of 1960's another revolution is on the



threshold. The 11th plan will give special emphasis to agriculture to reorient and rejuvenate this sector to meet the needs of the farmers. The credit flow to the agricultural sector has exceeded the target for the third consecutive year. However, doubts are being expressed about the efficacy of the delivery systems and the improvement of this system is the urgent need. The National Agricultural Insurance Scheme (NAIS) and the National Rural Employment Guarantee Scheme (NREGS) are two important schemes, which have been implemented recently. These have been extended to more number of villages, so that the under employment in agriculture sector is mitigated and business risk in agricultural farming due to natural calamities are also taken care of.

b. Manufacturing and infrastructure policies

If the increased activity in the manufacturing sector since 2003- 2004 has to be sustained focus on upgrading the infrastructure facilities in the country is the need of the hour. Up gradation of human skills, work on golden quadrilateral, introduction of public-private partnership model, increase in the power production capacity, etc, have already been identified as the areas which need robust growth in the immediate future. Spiraling of crude oil prices has had a deleterious impact on production and logistics costs through higher fuel costs. Alternatives to fossil fuel are being looked into. Wind energy is being harnessed increasingly apart from utilizing the large coal reserves available in our country. The credible alternative of producing nuclear power is one of the salient government policy. In regard to the industrial policy, the micro, small and medium enterprises development act 2006 has modified the previous act to increase the threshold investment. Micro, small and medium enterprises have now being defined as those in which investment in plant and machinery does not exceed Rs. 25 lakhs, Rs. 5 crores and Rs. 10 crores respectively. For the service sector this classification has been defined as Rs.10 lakhs, Rs. 2 crores and Rs. 5 crores respectively. A new national pharmaceutical policy has also been announced during the year 2006 to strengthen drug regulatory system and patent office.

The public-private partnership model has enabled greater private sector participation in the creation and maintenance of infrastructure. Concepts of special economic zone are under introduction and there have been a lot of hiccups in this area. New modifications are on the anvil to take care of the displaced landowners as also protection of the fertile lands.

The information technology amendment bill 2006 will put in place technology applications, security practices and procedures relating to such applications.

2. Fiscal policy

While preparing a policy to take care of the robust growth of the economy it has also been necessary to introduce fiscal corrections to reduce the fiscal deficit. Government of India subjected itself to a fiscal discipline for reducing deficits in the key areas viz, revenue, fiscal and primary. The tax base is being broadened to include more and more new services in the tax net. Personal taxation is being reduced so that the disposable incomes are bigger and savings grow. Introduction of value added tax (VAT) in various



states has been a significant success and is expected to usher price stability as well as improved earnings to the various states through higher volumes.

3. External sector policies

Foreign trade policy of 2004-2009 was modified through an annual supplement in 2007 for deepening the incentives provided for focused products and markets. For simplifying and liberalizing the external payments regime and deepen the foreign exchange market the recommendations of the committee of Fuller Capital Account Convertibility have been considered by the Government of India and certain policy initiatives have been undertaken. They relate to increase in overseas investment limits for joint ventures / wholly owned subsidiaries abroad by Indian companies, higher portfolio investment limits for Indian companies / domestic mutual funds, higher ceilings for investments by foreign institutional investors in Government securities and enhanced repayment limits for external commercial borrowings.

4. Monetary policies

The necessity to balance the growth of economy with containing inflationary pressures has guided the monetary policy. The Reserve Bank of India (RBI) have taken its stance on the monetary policy to continue to reinforce the emphasis on price stability and well anchored inflation expectations and there by sustain the growth momentum contextually, financial stability may assume greater importance in the near future. RBI has been managing this area with the cash reserve ratio (CRR) on one-hand and Repo rates on the other. The interest rates are being modified whenever necessary on the basis of the monitoring exercise on rates of inflation.

5. Financial sector policies

In view of the critical role played by the financial sector in supporting the robust growth of economy, RBI have tightened provisioning norms and risk weights to ensure asset quality, strengthened the accounting and disclosure norms for greater transparency and discipline. Final guidelines for the implementation of the new capital adequacy framework have been issued. Alongside its initiatives to strengthen the financial sector the RBI continue to take measures for protecting customers' rights and enhancing the quality of customer service.

GOVERNMENT FINANCES

a. Pattern of receipts

The combined finances of central and state governments registered an impressive improvement during 2006-2007. The buoyancy in tax revenue was possible due to the growth economy as well as the changes effected in the taxation system through reduced tax rates and broadening tax base. As a result Government of India could increase the allocation for development expenditure. 21.4% of GDP represented revenue receipts and the total expenditure net off repayments was 28.2% of the GDP. Developmental expenditure accounted for 15.2 % of GDP against 14.5% earlier. Debt including the reserve funds and deposits and advances came down to 77% against 80.5% of the previous year. For the year 2007-2008 revenue receipts are expected to increase by



14.9% over the previous year. Tax to GDP ratio is expected to increase to 11.8% in 2007-2008 and the non-tax revenue increase to 6.7% in 2007-2008. In respect of non-debt capital receives the recoveries of loans and advances from the state governments and central public sector units are expected to decline due to debt consolidation.

b. Pattern of expenditure

Aggregate expenditure as percentage of GDP in 2007-2008 has been budgeted at 13.8% of GDP as against 14.1% of GDP in 2006-2007, reflecting reduction of non-planned expenditure particularly interest payments and subsidies. On the other hand the planned expenditure to GDP ratio is budgeted to increase on the back of higher budgetary support for the central plan at 22.5% against 20.9% during the previous year. Capital expenditure will remain unchanged at 1.8% of GDP in 2007-2008. Among the major developmental expenditure education and health as a proportion to total expenditure has increased to 4.1% and 2.1% respectively against 3.7% and 1.8% in the previous year. The share of agriculture and rural development has more or less maintained the same level at around 10%.

PUBLIC - PRIVATE SECTOR INVESTMENTS

a. Public sector investments

During 2005-2006 the public sector enterprises contributed to around 11.12% of GDP and supplied a wide range of products and services including basic goods like steel, cement and chemicals, capital goods and intermediate goods. They also rendered services like telecommunications, tourism and warehousing. The cumulative investment of all central public sector enterprises (CPSE) at end March 2006 was Rs. 3,93,057 crores. Manufacturing CPSEs contributed 51% followed by CPSEs for services at 40% and mining by CPSEs accounted for 9%. In terms of capacity utilization, major CPSEs operated at above 75%. CPSEs had near monopoly in the production of coal 85.5%, crude oil 85.87% and petroleum refining 74.5%. The accumulated losses of all CPSEs declined by Rs.10, 578 crores from Rs.83, 725 crores in 2004-2005 to 73,147 crores in 2005-2006 (12%). In net value addition of CPSEs at market prices, the share of taxes and duties was the highest at 46%. At end March 2006, 239 CPSEs employed over 16.49 lakh people excluding casual workers.

b. Private sector investments

Resource mobilization through primary market was Rs.1, 61,769 crores during 2006 as against Rs.69, 543 crores during 2003. Out of this, private placement accounted for 1,17, 40 crores. And equity through IPOs accounted for Rs.32, 672 crores during 2006. Mutual funds contributed to private sector to the extent of Rs.86, 295 crores in 2006 against 35,646 crores in 2003.

Foreign direct investment inflows net were of the order of USD 4.7 billion during 2005 – 2006 and continued to climb during 2007. Foreign institutional investors have shown a chequered movement depending on the variation of interest rates in various countries compared to India and also exchange parity. Indian rupee has been steadily strengthening against dollar and it had its own impact on foreign trade as well as investments.

**c. Public-Private partnership**

The growth in the economy either in the industrial or services sector has put an inordinate pressure on the infrastructure like power, ports, highways, airports, tourism and urban infrastructure. The growth of infrastructure has lagged behind and may assume serious proportions. So, the government has been actively pursuing public private partnership (PPP) to bridge the deficit in the infrastructure. Under the overall guidance of the committee of infrastructure headed by the Prime Minister, the PPP programme formulation and implementation are being closely monitored by the relevant ministry / departments. An appraisal mechanism has been laid down and PPP appraisal committee has been given a mandate and guidelines for drawing up time frame for according approvals to proposals in a speedy manner. About 15 proposals valued at Rs. 2,480 crores have been already approved. PPP projects normally involve long term contracts between the government and private parties detailing the rights and obligations of both the contracting parties. Government has decided to develop standardized frameworks based on due diligence and agreements will follow international practices. They will also create a framework with a right matrix of risk allocation, obligations and returns. Planning commission has also issued model concession agreement (MCA) for ports, state highways and operation maintenance agreements for highways. PPP is still a nascent concept in India and the expertise for handling PPP is still under evolution. To promote PPP programme all state governments and central ministries are setting up PPP cell with a senior level officer as a nodal officer. Technical assistance has been obtained from Asian Development Bank (ADB) including hiring of consultants and training of personnel. A database on PPP projects in India is also under preparation.

BALANCE OF PAYMENTS

The strengthening of Rupee against USD started from a low of Rupees 46.5 to Rs. 39.50 in October 2007. Robust capital inflows are expected in the near future also and as such the pressure on the rupee is expected to continue. Net foreign institutional investment (FII) peaked at 4.7 billion USD in July 2007. FDI during April – July 2007 nearly doubled to USD 4.4 billion compared to USD 2.3 billion in the corresponding period in the previous year. RBI may tighten the external commercial borrowing norms further. India's export growth in terms of USD continued to show an impressive performance in spite of the strengthening rupee. Exports have grown cumulatively at a satisfactory level of 18.5% for the period April – September 2007 but still it was lower than the corresponding period of previous year at 27%. Various exports like leather, textile, and readymade garments were affected by the strengthening of the rupee. During April – May 2007 total imports were higher by 37.7%. POL and gold silver imports recorded an increase of 38.6% and growth in capital goods imports increased by 35%.

The world trade growth is expected to slow down during the year 2007-2008 according to world economic outlook; growth in world trade goods and services in volume terms is expected to be lower at 6.6% compared to 9.2% of last year. During January 2007, world exports in USD increased by 13.3% as compared to 13.5% to the corresponding period in 2006. Growth was



higher due to exports from industrialized countries. In the case of developing countries, the growth was lower at 15.1% during January –July 2007, against 18.1% in the corresponding period previous year.

OUTLOOK

The Indian economy has grown by 8.58% in the quarter ended September 2007. While the industrial sector grew by 8.7%, the services and agriculture sector are expected to grow at 10.3% and 3.2% respectively. For the year 2007-2008 GDP growth is forecasted at 9.1%. Interest rates continue to shown a lower trend. But this trend is expected to be arrested with the latest announcement by RBI of CRR hike of 50 basis points. Inflation has been under control with the lowest level at 3.02% during October 2007.

The national development council (NDC), the country's highest policy-making body recently endorsed the draft for 11th five-year plan for the country. This draft assumes an average 9% growth in GDP for the first four years and 10% growth during the final year 2011-2012. The overall investment Rs. 36,00,000 crores out of which Rs.10, 00, 000 crores will be from gross budgetary support to assist the states for introducing inclusive growth through the development of social infrastructure such as health, education and eradication of poverty by generating more jobs. The target for reduction in incidence of poverty by 10% of points would mean generating 7 crores new jobs and ensuring electricity connection for all the villages in the country. After serious discussion on the draft it has been decided to institute a task force in the planning commission to examine the resource needs for expanding irrigation and chalking out a new approach to implementation there of. In regard to agricultural indebtedness a scheme is under formulation on the basis of the recommendations of Radha Krishna committee. The discussions on the 11th five-year plan also brought into focus the problem of food security. The plan recognizes the necessity for enhancing stocks of food grains and considering buffer stocks for pulses and edible oils. To take care of the regional disparity and increasing rural-urban divide, the 11th plan has allocated more than 50% of the gross budgetary support to the key sectors of agriculture, health and education. Power sector however was expected to be major area of concern and the necessity to build enough power capacity to keep abreast of the growing industrial sector has been given high priority by the Government of India.