6

EXTERNAL SECTOR

The global economic and financial situation that deteriorated following the crises in Asia and Russia, staged a rapid recovery in 1999 and continued to gain strength in 2000. Global output growth is now estimated at 4.7 per cent in 2000, up from 3.4 per cent in 1999 and 2.6 per cent in 1998 (Table 6.1). Undoubtedly, the global economic expansion has been led by the continued strength of the U.S. economy. The improvement is also due to a robust upswing in Europe, a consolidation of the recovery in Asia and a rebound in economic activity in emerging markets in Latin America, the Middle East and Europe. Growth of world trade volume in goods and services recovered slightly from 4.3 per cent in 1998 to 5.1 per cent in 1999 and it is estimated to have almost doubled to 10 per cent in 2000. World trade prices of manufactures in US Dollar value, which continued to be on the downslide for five years in succession since 1996, are expected to rise by 1.1 per cent in 2001. On the other hand, world trade prices of non-fuel primary commodities have, much to the respite of developing countries, been estimated to have increased by 3.2 per cent in 2000 with prospects for further increase in 2001, in contrast to significant declines in the previous four years. International prices of oil rose by 37.5 per cent in 1999 and strengthened further by 47.5 per cent in 2000. They are expected to show some softening (about 13 per cent) in 2001. Private

TABLE 6.1

External Environment

(Annual per cent change unless otherwise noted)

			Projections	
	1998	**1999**	**2000**	**2001**
World Output	**2.6**	**3.4**	**4.7**	**4.2**
Advanced Economies	2.4	3.2	4.2	3.2
United States	4.4	4.2	5.2	3.2
European Union	2.7	2.4	3.4	3.3
Japan	-2.5	0.2	1.4	1.8
Other Adv. Economies	1.0	5.5	5.8	4.4
Developing Countries	3.5	3.8	5.6	5.7
Asia	4.1	5.9	6.7	6.5
China	7.8	7.1	7.5	7.3
India	6.3	6.4	6.7	6.5
ASEAN-4*	-9.3	2.6	4.5	5.0
Countries in Transition	-0.8	2.4	4.9	4.1
Russia	-4.9	3.2	7.0	4.0
World Trade Volume (goods & services)	**4.3**	**5.1**	**10.0**	**7.8**
World Trade Prices (in US dollar terms)				
Manufactures	-1.2	-1.2	-5.3	1.1
Oil	-32.1	37.5	47.5	-13.3
Nonfuel primary commodities	-14.7	-7.1	3.2	4.5
Net private capital flows to emerging markets (US$bn)	**66.2**	**67.4**	**36.4**	**116.0**

*** Indonesia, Malaysia, the Philippines, and Thailand**
Source: World Economic Outlook - October 2000, IMF

BOX 6.1
External Sector Developments during the 1990s

There have been significant improvements in the structure of India's balance of payments and the strength of the external sector since the economic crisis of June 1991.

Selected Indicators of External Sector in 1980s and 1990s

Item	1980-81 to 1991-92 (Annual Average)	1992-93 to 1999-2000 (Annual Average)
Annual Average Growth Rates		**Percent Per Year**
1. Growth of Exports - BOP (%)	7.6	10.0
2. Growth of Imports - BOP (%)	8.5	13.4
Non-POL-DGCI&S (%)	6.6	13.2
Key Ratios		**Averages for the period**
3. Exports/Imports - BOP (%)	62.3	74.0
4. Import cover of FER (No. of months)	3.8	7.2
5. External assistance (net)/TC (%)	41.6	18.9
6. ECB (net)/TC (%)	25.1	22.7
7. NR deposits/TC (%)	23.2	23.2
8. Short-term debt / FER (%)	137.5*	23.8
9. Debt service payments as % of current receipts	31.8*	22.2
Selected Items in Balance of Payments		**Percent of GDP**
10. Exports	5.1	8.4
11. Imports	8.2	11.5
12. Trade balance	-3.1	-3.1
13. Invisibles balance	1.2	1.9
14. Current account balance	-1.9	-1.2
15. External Debt	31.4*	27.9
16. Debt Service Payments	2.8*	3.0

*** Data relate to the year 1989-90 to 1991-92. External debt and debt service payments data for the earlier years in the 1980s are not comparable with those for the latter years, because of incomplete coverage of data.**

Notes : For foot-notes, see Table 6.3.

- The export cover of imports rose sharply from an annual average of 62 per cent during 1980-81 to 1991-92 to 74 per cent during 1992-93 to 1999-2000.
- The reforms of the 1990s facilitated India to move away from a closed economy framework towards a more open and liberal economy.
- The ratio of exports and imports to GDP, rose from an annual average of 13.2 per cent during 1980-81 to 1991-92 to an average of 19.9 per cent during 1992-93 to 1999-2000.
- The current account deficit, as percentage of GDP, declined from an annual average of 1.9 per cent during 1980-81 to 1991-92 to a well manageable level of 1.2 per cent during 1992-93 to 1999-2000.
- The capital account of BOP has also undergone a major structural change in favour of non-debt creating foreign investment flows.
- Foreign exchange reserves were built to a very comfortable level of about 8 months of imports from a critical level of about two months of imports in June 1991.
- External debt and debt service indicators marked sustained improvements over the 1990s. External debt, as a per cent of GDP, declined gradually from 38.7 per cent at the end of March 1992 to 21.9 per cent at the end of March 2000.
- Similarly, debt service payments on external debt, as a per cent of current receipts, declined gradually from 35.3 per cent in 1990-91 to 16.0 per cent in 1999-2000.
- The strength of the external sector has enabled India to withstand fairly well the Asian financial crisis contagion and the related adverse spillovers.

capital flows to emerging market economies fell sharply between mid-1997 and end-1998, in the wake of financial crises that struck Asia and Russia. In net terms, private financing of capital to emerging markets fell from the peak of US $ 225 billion in 1996 to US $ 66 billion in 1998. After remaining subdued at US $ 67 billion in 1999, they rose sharply in the first quarter of 2000, before dropping again in the second quarter. For the whole of 2000, net private capital flows are estimated at only US $ 36.4 billion and they are projected to recover to US $ 116 billion in 2001.

6.2 There are, however, significant risks and uncertainties to the otherwise encouraging outlook in the external environment. They include the uneven pattern of growth of GDP and demand growth among the three major currency areas (U.S, Europe and Japan), and the associated imbalances in their external current accounts; the apparent misalignment among major currencies, particularly the Euro and the US dollar. The possibility that these imbalances may unwind in a disorderly fashion remains a risk to global expansion. Second, oil prices have been significantly higher than previously expected, due to both supply constraints in the producing countries and the continued strength of global demand. With many oil producers close to capacity and stocks relatively low, there may still be upside risks to oil prices, which will have direct impact on global activity and inflation. Estimates by IMF suggest that a US $ 5 per barrel increase in oil prices would reduce GDP growth in industrial countries by 0.2 per centage points in 2001, accompanied by higher inflation and interest rates. Besides, many individual developing countries, which are net oil importers, would be seriously affected with trade balances deteriorating to a large extent.