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General Review

Review of developments

(a) Macroeconomic overview

According to data for 2001-02, released by the Central Statistical Organisation (CSO) on January 31, 2003, Gross Domestic Product (GDP) at factor cost at constant 1993-94 prices grew at 5.6 percent in 2001-02, as against 5.4 percent projected in February 2002. The higher growth estimate for 2001-02 is particularly significant as it comes against the backdrop of a revised estimate of a more moderate growth deceleration for 2000-01 than originally apprehended. In 2000-01, GDP at factor cost at constant 1993-94 prices grew at 4.4 percent, as against the previous estimate of 4.0 percent. The trends of key macro economic parameters are given in Table 1.1 and Figure 1.1.

1.2 The pick-up in growth of the Indian economy observed in 2001-02 was stronger than what had been initially anticipated. Data on quarterly GDP at factor cost at constant 1993-94 prices, available only for the first half of 2002-03, indicated that in the first and second quarters of the current year, year on year, GDP grew by 6 percent and 5.8 percent – rates that are markedly higher than 3.5 percent and 5.3 percent respectively, registered in the corresponding periods of the previous year. The monsoon failure, however, affected agriculture severely, with agriculture and allied GDP declining by 3.1 percent, as per the advance estimates released by the CSO on February 7, 2003. Overall GDP growth in the current year is likely to be only 4.4 percent. This agriculture-pulled deceleration in growth, in 2002-03, clouds an across-the-board improvement in the growth performance of industry and services from 3.3 percent to 6.1 percent, and from 6.8 percent to 7.1 percent, respectively, between 2001-02 and 2002-03. Indications are that, inspite of a severe monsoon deficiency, the rebound in growth observed since 2001-02 gained momentum in industry and services sectors in the current year.

1.3 The continued growth recovery in the first half of the current year is significant in view of the several downside risks prevailing in the international and domestic economy. The outlook of recovery in global economic activity and world trade has remained subdued. International financial flows have been affected by the unsettled conditions in Latin America and Turkey. Geo-political conditions have been highly volatile with the stand-off in Iraq. Moreover, the country has been affected by a most telling monsoon deficiency in two decades.

1.4 The growth recovery was accompanied by continued macroeconomic stability in terms of low inflation, orderly currency market conditions and comfortable reserves. In the past, droughts, with their impact on price and availability of foodgrains, have been particularly harsh on the poor. In the current year, notwithstanding the deficient monsoon, there were no shortages in availability of essential commodities, or flare-ups in their prices. The 52-week average inflation rate based on the Wholesale Price Index (WPI) was only 2.6 percent in mid January 2003. Prices of primary products remained below 4 percent for the larger part of the year, while inflation in manufactured products was

Table 1.1 : Key indicators

Items	1999-2000	2000-01	2001-02	2002-03	1999-2000	2000-01	2001-02	2002-03
	Absolute values				% change over previous period			
Gross national product (at factor cost) (Rs.thousand crore)								
At current prices	1746.5	1900.3 P	2081.4 Q	2217.8 A	10.3	8.8 P	9.5 Q	6.6 A
At 1993-94 prices	1136.8	1186.3 P	1257.0 Q	1309.9 A	6.2	4.3 P	6.0 Q	4.2 A
Gross domestic product (at factor cost) (Rs. thousand crore)								
At current prices	1761.9	1917.7 P	2094.0 Q	2236.1 A	10.2	8.8 P	9.2 Q	6.8 A
At 1993-94 prices	1148.4	1198.7 P	1265.4 Q	1320.7 A	6.1	4.4 P	5.6 Q	4.4 A
Agriculture and allied sectors (Rs. thousand crore) (at 1993-94 prices)	286.98	285.88	302.05 Q	292.63 A	0.3	-0.4	5.7 Q	-3.1 A
Index of agricultural production(1)	176.8	167.3 P	177.1 P	156.0 P	-0.6	-5.4 P	5.9 P	-11.9 P
Foodgrains production (million tonnes)	209.8	199.5	212.0 P	183.2 P	3.0	-4.9	6.3 P	-13.6 P
Index of industrial production(2)	154.9	162.6	167.0	170.5 **	6.7	5.0	2.7	5.3 #
Electricity generated (in billion kwh)	480.7	499.5	515.2	397.6 **	7.2	3.9	3.1	3.7 **
Wholesale price index(3)	150.9	159.2	161.8	167.9 *	6.5	4.9	1.6	4.4 *
Consumer price index for industrial workers(4)	434.0	445.0	468.0	484@	4.8	2.5	5.2	3.2@
Money supply (M3)(5) (Rs. thousand crore)	1,124.2	1,313.2	1,500.0	1689.1(6)	14.6	16.8	14.2	15.7(6)
Imports at current prices								
(in Rs. crore)	2,15,236	2,30,873	2,45,200	2,13,225 **	20.7	7.3	6.2	17.5 **
(in US $ million)	49,671	50,536	51,413	43,882 **	17.2	1.7	1.7	14.5 **
Exports at current prices								
(in Rs. crore)	1,59,561	2,03,571	2,09,018	1,85,211 **	14.2	27.6	2.7	23.4 **
(in US $ million)	36,822	44,560	43,827	38,115 **	10.8	21.0	-1.6	20.4 **
Foreign currency assets (7)								
(in Rs. crore)	1,52,924	1,84,482	2,49,118	3,34,065(8)	21.9	20.6	35.0	47.7(8)
(in US $ million)	35,058	39,554	510,49	69,888(8)	18.8	12.8	29.1	50.1(8)
Exchange rate (Re./US $) (9)	43.33	45.68	47.69	48.54(10)	-2.9	-5.1	-4.2	-2.16(10)

Note : Gross national product and Gross domestic product figures are at factor cost (new series; base = 1993-94).
Q-Quick estimates; A-Advance estimates; P-Provisional;
***: As on 18.01.2003 (provisional). @: December, 2002. **: April-December 2002. #: April-November 2002.**

1. **Index of agricultural production (of 46 crops, including plantations) with base triennium ending 1981-82=100 (revised).**
2. **Index of industrial production; (base 1993-94=100).**
3. **Index (with base 1993-94=100) at the end of fiscal year.**
4. **Index (with base 1982=100) at the end of fiscal year.**
5. **Outstanding at the end of financial year.**
6. **As on January 10, 2003, year-on-year growth.**
7. **Outstanding at the end of fiscal year.**
8. **At the end of January, 2003.**
9. **Percent change indicates the rate of appreciation (+)/depreciation (-) of the Rupee vis-á-vis the US Dollar.**
10. **Average for April-January, 2002-2003.**

around 3 percent. The transition to a market-based pricing regime for petroleum products was also devoid of disruptions, with fuel group inflation barely touching 5 percent for much of the year. However, the latest Gulf-related uncertainty has caused fuel price inflation to touch 6.4 percent in mid-January, 2003. Inflation, as measured by the Consumer Price Index for industrial workers (CPI-IW) declined from 4.7 percent at the beginning of 2002-03 to 3.2 percent in December 2002. The abundant stocks of wheat (28.8 million tonnes on January 1, 2003) and rice (19.4 million tonnes on January 1, 2003) held by the Food Corporation of India (FCI), while complicating the task of agricultural diversification and fiscal consolidation, did however, help to quell inflationary pulls.

1.5 In spite of volatility in global currency markets following the events of September 11, 2001, appropriate and timely policy interventions moderated the volatility in the exchange rate of the rupee, which moved in a range of Rs.46.56-48.85 per US dollar during 2001-02, with average depreciation against the US dollar amounting to 4.0 percent. During the current financial year, after reaching an all time high of Rs.49.06 per US dollar in May 2002, the rupee strengthened against the dollar and stood at Rs.47.80 per US dollar at the end of December 2002, thereby appreciating by 2.1 percent over the end-March 2002 level. The rupee, however, has depreciated against pound sterling, euro, and yen by 8.9 percent, 14.9 percent and 7.4 percent respectively between April 2002-January 2003, reflecting in part the weakening of the US dollar against these currencies.

1.6 Foreign currency assets at end-March 2002 amounted to US $51.05 billion, up by US $11.5 billion over US $39.5 billion at end-March 2001. Out of this increase, a large part (US $9.10 billion) was realized during the second half of 2001-02. Reserve accretion accelerated in the first three quarters of the current financial year, with foreign exchange reserves reaching a record high of US $73.58 billion at the end of January 2003, with an increase of US $19.47 billion over the level of end-March 2002. A recent Reserve Bank of India (RBI) study shows that the major sources of reserve accretion in the current fiscal till end-November 2002 have been a surplus in the current account, non-debt creating capital flows and valuation gains. In spite of the interest rate differential of 3-4 percent between the rates abroad and in India, there is no evidence to suggest that arbitrage through debt capital was substantial. Thus, at least upto November 2002, arbitrage may not have played a major role in accumulation of reserves. It is estimated that as much as two-thirds of the reserve accretion was on account of non-debt capital flows. Growth in foreign exchange reserves has facilitated a further relaxation of foreign exchange restrictions and a gradual move towards greater capital account convertibility.

1.7 The rapid growth in reserves was partly the result of a strong current account. After twenty-three years, the current account of India's balance of payments recorded a surplus – equivalent to 0.3 percent of GDP – in 2001-02. Stagnant exports and falling imports brought down the trade deficit by 0.5 percentage points in 2001-02. The current account showed a surplus mainly because of buoyant net invisible inflows equivalent to 2.9 percent of GDP, which, at US $14.05 billion, were the highest in the last decade. Invisibles are doing well in the current year too, primarily on account of heavy inflow of remittances. This, coupled with a sharp rise in exports, considerably enhances the possibility of recording a surplus in the current account for the second successive year. According to DGCI&S data, exports in dollar terms are currently (April-December, 2002) growing at 20.4 percent. Year-on-year exports in dollar terms grew by 34.3 percent in December, 2002. The surge in exports has occurred in spite of the sluggish pace of global economic recovery, and the slight appreciation of the rupee vis-à-vis the dollar, and has contributed to domestic industrial growth.

1.8 While merchandise exports have grown well in 2002-03, services exports have also been an important area of success reflected in net invisible inflows of US $14 billion in 2001-02. India's share in world commercial services trade is larger than India's share in world merchandise trade. While software exports is a well-known success story, India is now an important venue for many tasks in services such as financial accounting, call centres, processing insurance claims, and medical transcription. The future potential for growth in these areas appears to be considerable.

1.9 The strengthening of the balance of payments has impacted on the monetary sector, with net foreign exchange assets (NFA) of RBI emerging as an important source of reserve money. From 9.1 percent as at end-March 1991, the share of net foreign exchange assets in reserve money, which had reached 78.1 percent by the end of 2001-02, became 100.7 percent on January 24, 2003, which is close to a currency board situation. Similarly, the NFA to currency ratio increased gradually from 14.4 percent as at end-March 1991, to 105.2 percent as on March 31, 2002, and further to 127.7 percent on January 24, 2003. For liquidity management, the substantial increase in foreign exchange assets was partly neutralised by the decline in RBI's net domestic credit. In the current financial year, RBI credit to the government remained negative, and reserve money grew by 2.9 percent up to January 24, 2003, as compared with 4.7 percent in the corresponding period of last year.

1.10 The money multiplier – the ratio of broad money (M_3) to reserve money – which had increased from 4.3 to 4.4 in the previous year, increased further to 4.8 as on January 10, 2003. In the current financial year up to January 10, 2003, broad money grew at 9.8 percent (net of merger of ICICI and ICICI Bank) as compared with 11.2 percent in the corresponding period of last year. The year-on-year growth in M_3, as on January 10, 2003, amounted to 12.8 percent (net of mergers) compared with 14.5 percent last year.

1.11 Inspite of the slower growth of money supply, the current year has been characterised by easy liquidity conditions. There are signs of a pick-up in non-food credit and a fall in interest rates, including in the yields on government securities. Upto January 10, 2003, non-food credit (net of mergers) increased by 11.4 percent, as compared with 9.1 percent in the corresponding period of last year. A revival in industrial activity may lead to a further increase in the off-take of non-food credit. Food credit declined by 7.1 percent in the current financial year as compared to an increase of 33.0 percent in the corresponding period of last year, mainly on account of the drought, and higher off-take of food-grains in the current year. Priority sector advances of public sector banks formed 43.1 percent of net bank credit at the end of March, 2002. The corresponding percentage for private banks was 40.9 percent, higher than the prescribed target of 40 percent. However, there were shortfalls under priority sector sub-targets set for the agricultural sector. A declining trend in sanctions and disbursements by All-India Financial Institutions was observed mainly on account of a reduction in the number of project proposals seeking financial assistance, the weak financial position of IDBI and IFCI, and the spread of universal banking.

1.12 Facilitated by relatively lower inflation, interest rates continued to soften during the year. The RBI reduced the bank rate by 25 basis points to 6.25 percent in October 2002. At its present level, the bank rate is the lowest since 1973. The cash reserve ratio (CRR) was reduced by 50 basis points to 5.0 percent from June 1, 2002, and further to 4.75 percent from the fortnight beginning November 16, 2002. The PLR of five major commercial banks declined from 11.00-12.00 percent to 10.75-11.50 percent in the current year. A noticeable development in the current year is sub-PLR lending by commercial banks. Yields on government securities continued to maintain their downward trend. The yield on 7.4 percent 12-year government paper reached a low of 6.13 percent on December 31, 2002.

1.13 Gross non-performing assets (NPAs) of scheduled commercial banks increased by

Rs. 7,164 crore to Rs. 70,905 crore, while net NPAs increased by Rs. 3,084 crore to Rs. 35,546 crore in 2000-01. The incremental gross NPAs in 2001-02, which is more than double the amount in 2000-01, is mainly on account of the inclusion of an amount of Rs. 4,512 crore in gross NPAs consequent on the merger of ICICI with ICICI Bank. There was an increase in NPAs of public sector banks, despite significant progress in recoveries. In the case of foreign banks, recoveries exceeded net accretion to NPAs. The ratios of gross and net NPAs of commercial banks to advances and total assets have been declining across all bank groups. Gross NPAs of public sector banks, at 11.1 percent of gross advances, and 4.9 percent of total assets, are higher than those of private sector and foreign banks. Advances to non-priority sectors accounted for the bulk of the outstanding NPAs in the case of both public sector banks (53.5 percent) and private banks (77.9 percent). At the end of March 2002, 25 out of 27 public sector banks (PSBs) had capital to risk-weighted asset ratio (CRAR) above the prescribed minimum level of 9 percent. Of these, as many as 23 banks had CRAR exceeding 10 percent. Two PSBs, two private sector banks, and one foreign bank, did not fulfill the minimum CRAR. The CRAR of scheduled commercial banks, as a whole, increased from 11.2 percent at end-March, 2001 to 11.8 percent at end-March, 2002.

1.14 Capital markets continued to be subdued. The NSE-50 index, which was at 1,087 in January 2002, was at 1,073 in January 2003, showing no significant change. This weakness in the secondary market led to a small volume of issuance on the primary market. However, the drop in the Indian equity market in the period after December 2001 is smaller than that in many other countries. Unlike the heavy inflows in the preceding years, there was a small outflow of foreign portfolio investment from India between April to November 2002.

1.15 The subdued conditions in domestic capital markets, however, conceal important structural reforms. The equity market has absorbed a new market design, with rolling settlement and equity derivatives trading. Liquidity, which was adversely affected in July 2001, has bounced back to strong levels from March 2002 onwards. In 2001, two Indian exchanges, National Stock Exchange (NSE) and Bombay Stock Exchange (BSE), ranked third and sixth among exchanges all over the world, sorted by the number of transactions.

1.16 Risk management functions performed by the Clearing Corporation of India Limited (CCIL) for bonds and foreign exchange transacted by telephone, has imparted a new level of safety with regard to settlement risk. In January 2003, government bonds started trading on stock exchanges, ushering in a new level of transparency and market access for the government bond market. This is a welcome move away from bilateral negotiation towards anonymous screen-based order matching.

1.17 Recent legislative amendments to the SEBI Act have put SEBI on a better footing in terms of enforcement of proper market conduct. This should help reduce the extent of market malpractice and improve market efficiency. The UTI Act was repealed to break UTI into UTI-1 and UTI-2, with UTI-2 handed over to a new set of owners.

1.18 Public finances, both at the Centre as well as the States, which have been under pressure since 1997-98 after the implementation of the Fifth Central Pay Commission's recommendations, deteriorated further in 2001-02. The fiscal deficit of the Central Government, as a proportion of GDP, which had increased continuously from 4.1 percent in 1996-97 to 5.6 percent in 2000-01, rose further to an estimated 5.9 percent in 2001-02. The primary deficit of the Central Government (excluding loans to States against small savings collections), after turning into a small surplus in 1996-97, started deteriorating thereafter, reaching a level of 1.4 percent of GDP in 2001-02. The lack of fiscal consolidation at the State level is revealed by a similar deterioration of their combined fiscal deficit, again as a proportion of GDP, from 2.7 percent in 1996-97 to 4.3

percent in 2000-01, and further to a revised estimate of 4.6 percent in 2001-02. The consolidated fiscal deficit of the Centre and the States was 10.0 percent of GDP, according to the revised estimates for 2001-02.

1.19 During the first nine months of the current year, central finances displayed considerable improvement with the fiscal deficit at Rs. 86,269 crore, slightly lower than the figure of Rs. 89,014 crore observed in April-December 2001. However, the remaining part of the year could see some pressures on both revenue and expenditure. Unanticipated weakening of the growth momentum may affect revenue collections. Expenditure management would also pose larger challenges because of enhanced food subsidies on account of higher farm support prices, higher fertilizer subsidy from augmented retention prices, larger subsidies resulting from distribution of liquefied petroleum gas (LPG) and kerosene at below market prices, and unanticipated expenditure on drought relief. The disinvestment programme is running behind schedule, and there is likely to be a shortfall in capital receipts under this head. During the year, the Central Government also had to provide Rs. 938 crore of budgetary resources for rehabilitation of the UTI.

1.20 At the level of the States, while a large number of initiatives like Fiscal Responsibility legislations, and medium-term fiscal reform programmes, have been undertaken, pressure on the fiscal front continues. While the expenditure composition, both for the Centre and the States continues to reflect a preponderance of wages, salaries, interest payments, and subsidies, there has been some welcome relief on the interest payments front with the softening of interest rates in recent months. The high fiscal deficit continues to complicate the task of conducting counter-cyclical fiscal policies and augmenting outlays on the much needed social and physical infrastructure, and poverty alleviation programmes.

1.21 A significant reform in the current year was the dismantling of the administered price mechanism for petroleum products from April 1, 2002, exactly as per the schedule announced in 1997. Reforms picked up speed in the third quarter of the current year. The winter session of Parliament saw the passage of several important Bills, including Securitisation and Reconstruction of Financial Assets and Securities Bill, 2002, the Securities and Exchange Board of India (Amendment) Bill, 2002, the Unit Trust Of India (Transfer of Undertaking and Repeal) Bill, 2002, Prevention of Money Laundering Bill, 2002, the Companies (Amendment) Bill, 2002, the Companies (Second Amendment) Bill, 2002 and the Competition Bill, 2001. The announcement about the disinvestment strategy for Bharat Petroleum Corporation Limited (BPCL) and Hindustan Petroleum Corporation Limited (HPCL), in December 2002, cleared the uncertainty over privatisation.

(b) Consumption, savings and investment

1.22 With a faltering global recovery, private final consumption expenditure has been the major factor sustaining growth in the Indian economy. Private final consumption expenditure, at constant 1993-94 prices, increased by Rs. 48,275 crore or 5.9 percent in 2001-02, compared to a rise of only 5.6 percent in GDP at factor cost at constant prices (Table 1.2). Private final consumption expenditure as a proportion of GDP at market prices – both at constant prices – increased from 62.2 percent in 2000-01 to 62.5 percent in 2001-02.

1.23 The composition of private final consumption expenditure in 2001-02 displayed a change in trends observed for a number of years. The share of food, beverage and tobacco in overall consumption at constant prices, which had steadily declined from 54.8 percent in 1993-94 to just about 48.1 percent in 2000-01, improved to 48.8 percent in 2001-02. The increase was largely due to a more than one percentage point increase in the share of expenditure on cereals. Cereal expenditure rose, presumably on account of pressures on open market

Table 1.2 : Disposition of gross domestic product (GDP)										
	Percentage change over the previous year									
	(at current prices)					(at 1993-94 prices)				
Component	1997-98	1998-99	1999-2000	2000-01P	2001-02Q	1997-98	1998-99	1999-2000	2000-01P	2001-02Q
Total final consumption expenditure	**10.0**	**17.3**	**12.5**	**6.6**	**10.1**	**3.8**	**7.4**	**7.1**	**2.3**	**6.1**
Govt. final consumption expenditure	18.2	24.3	17.3	5.4	11.5	11.1	12.9	13.2	0.6	7.2
Pvt. final consumption expenditure	8.6	16.1	11.6	6.9	9.8	2.6	6.4	6.0	2.6	5.9
Gross domestic capital formation, of which :	11.8	5.0	24.3	3.3	8.0	7.7	0.7	20.3	-1.4	3.0
Gross fixed capital formation	6.0	13.3	11.4	9.6	9.6	2.1	8.7	9.3	3.8	3.2
Exports of goods and services	14.0	18.2	16.6	27.4	4.9	—	—	—	—	—
Less Imports of goods and services	14.5	21.9	18.2	15.2	4.6	—	—	—	—	—

Q : Quick Estimates P : Provisional
Source : Central Statistical Organisation.

prices of foodgrains, whose supply reduced because of heavy procurement under the central pool. Among other major categories of consumption, expenditure on medical and health care services rose by 0.3 percentage points. The share of clothing and footwear, gross rent, fuel & power, and furniture, furnishings, appliances and services declined, while that of transport & communication, and recreation, education and cultural services remained unchanged.

1.24 In 2001-02, gross and net domestic savings at current prices, grew by 11.8 percent and 13.3 percent respectively, to increase their share in GDP at market prices. Gross (net) domestic savings, as a

Table 1.3 : Savings and investment							
	1995-96	1996-97	1997-98	1998-99	1999-2000	2000-01 (P)	2001-02 (Q)
	(As percent of GDP at current market prices)						
Gross domestic savings	**25.1**	**23.2**	**23.1**	**21.5**	**24.1**	**23.4**	**24.0**
Public	2.0	1.7	1.3	-1.0	-1.0	-2.3	-2.5
Private	23.1	21.5	21.8	22.5	25.1	25.7	26.5
Household	18.2	17.0	17.6	18.8	20.8	21.6	22.5
Financial	8.9	10.4	9.6	10.5	10.7	10.4	11.2
Physical	9.3	6.7	8.0	8.4	9.6	11.2	11.3
Private corporate	4.9	4.5	4.2	3.7	4.4	4.1	4.0
Gross domestic investment*	**26.9**	**24.5**	**24.6**	**22.6**	**25.2**	**24.0**	**23.7**
Public	7.7	7.0	6.6	6.6	6.9	6.4	6.3
Private	18.9	14.7	16.0	14.8	16.7	16.1	16.1
Gross domestic investment*	**26.9**	**24.5**	**24.6**	**22.6**	**25.2**	**24.0**	**23.7**
GFCF	24.4	22.8	21.7	21.5	21.8	21.8	21.7
Change in stocks	2.2	-1.0	0.9	-0.1	1.9	0.7	0.8
Saving-investment gap@	**-1.7**	**-1.3**	**-1.5**	**-1.0**	**-1.1**	**-0.6**	**0.2**
Public	-5.6	-5.4	-5.3	-7.6	-8.0	-8.7	-8.8
Private	4.2	6.8	5.8	7.7	8.4	9.5	10.3

Note : (i) Gross domestic investment denotes gross domestic capital formation (GDCF).
(ii) Figures may not add up due to rounding off.
*** : adjusted for errors and omissions;**
@ : refers to the difference between the rates of savings and investment.
GFCF : Gross fixed capital formation.
P : Provisional estimates; Q : Quick estimates;
Source : Central Statistical Organisation.

proportion of GDP (NNP) at market prices, improved to 24.0 (16.0) percent in 2001-02, from 23.4 (15.4) percent in 2000-01 (Table 1.3). The household sector was once again the best performer, with the increase in its gross savings exceeding the total increase in gross domestic savings. Households increased the share of financial savings in their total savings from 48.0 percent in 2000-01 to 49.8 percent in 2001-02. Private corporate savings increased roughly at half the rate of increase of household savings. The public sector not only continued to be a net dis-saver, but it increased its dissavings by nearly Rs 10,000 crore. The departmental enterprises became net dissavers in 2001-02. The increased savings by non-departmental enterprises were more than neutralized by the increased net dissavings of government administration.

1.25 Gross domestic capital formation at constant prices grew at 3.0 percent in 2001-02, which was considerably lower than the growth of GDP (Table 1.4). At current prices, gross capital formation constituted 23.7 percent of GDP in 2001-02, which was slightly lower than the share of 24.0 percent observed in 2000-01, and 25.2 percent observed in 1999-2000. Among components of gross capital formation, in 2001-02, it appears that changes in stocks grew at a much faster rate than gross fixed capital formation. Within fixed capital formation, however, construction grew relatively faster than gross investment in machinery and equipment. In the public sector, there was a sharp increase of 7.2 percent in capital formation in construction.

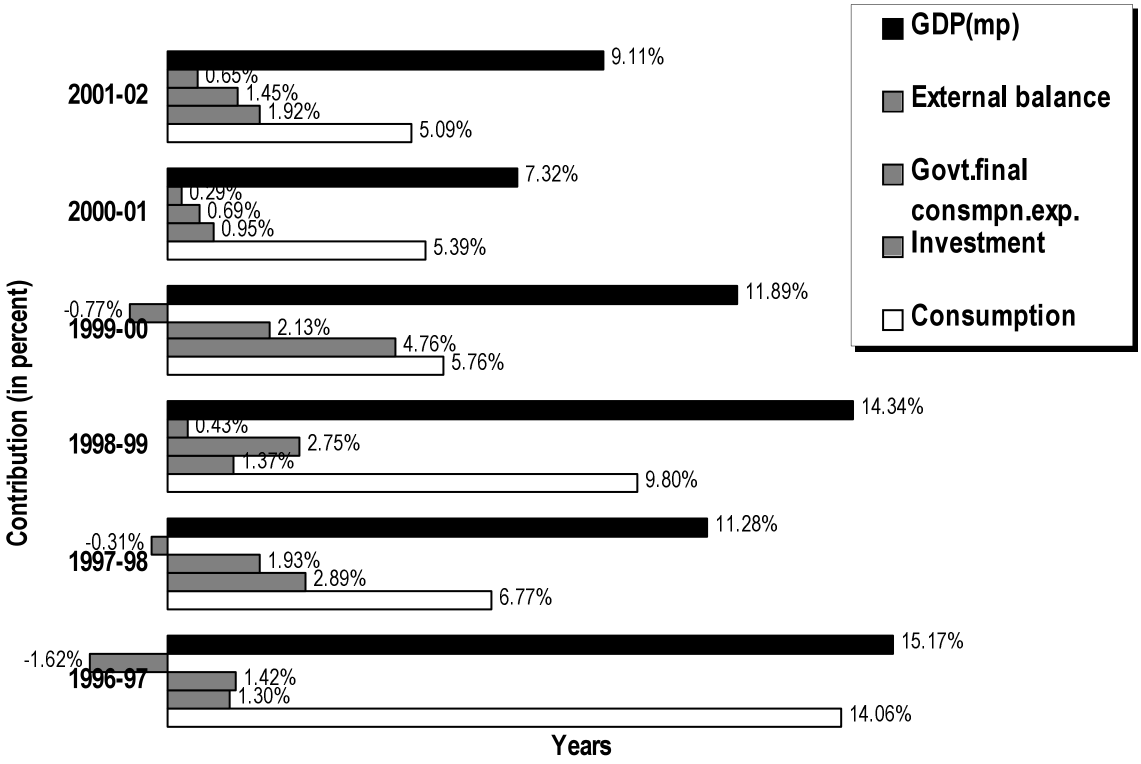
1.26 Domestic demand, and particularly, private final consumption expenditure, has been fuelling growth in recent years (Figure 1.2). In 2000-01, private final consumption expenditure contributed as much as 73.6 percent of the growth in GDP at current market prices, which was considerably higher than not only the corresponding contribution of 48.4 percent in 1999-2000, but also the average contribution of private final consumption expenditure to growth of 58.9 percent in the previous three years (1997-98

Table 1.4 : Real gross domestic capital formation

	1995-96	1996-97	1997-98	1998-99	1999-2000	2000-01 (P)	2001-02 (Q)
	(As percent of GDP at market prices, 1993-94 prices)						
GDCF*	**27.3**	**25.1**	**25.9**	**24.6**	**27.7**	**26.2**	**25.6**
Public	7.6	6.8	6.5	6.6	7.0	6.4	6.2
Private	19.3	15.5	17.3	16.7	19.0	18.3	18.0
Pvt. corporate sector	9.9	8.7	9.0	7.6	7.7	5.8	5.7
Household sector	9.4	6.9	8.3	9.1	11.3	12.4	12.3
GFCF	**24.7**	**23.4**	**22.9**	**23.4**	**23.9**	**23.9**	**23.4**
Public	7.6	6.7	6.2	6.4	6.2	6.0	5.8
Private	17.1	16.7	16.6	17.0	17.7	17.8	17.6
Change in stocks	**2.2**	**-1.0**	**0.9**	**-0.1**	**2.0**	**0.7**	**0.8**
Public	-0.0	0.2	0.3	0.1	0.8	0.3	0.4
Private	2.2	-1.2	0.7	-0.3	1.2	0.4	0.4
	Growth rate in percent						
GDCF*	**11.1**	**-1.0**	**7.7**	**0.7**	**20.3**	**-1.4**	**3.0**
Public	-6.5	-3.1	-0.8	7.3	13.3	-5.0	2.7
Private	38.5	-13.7	16.4	2.6	21.5	0.0	4.2
GFCF	**19.3**	**1.5**	**2.1**	**8.7**	**9.3**	**3.8**	**3.2**
Public	-6.5	-5.9	-2.8	9.4	2.7	2.0	0.7
Private	36.1	4.8	4.1	8.4	11.8	4.5	4.1

Note : GDCF : Gross domestic capital formation; GFCF : Gross fixed capital formation;
Figures may not add up due to rounding off.
*** : adjusted for errors and omissions; P : Provisional estimates; Q : Quick estimates;**
Source : Central Statistical Organisation

Fig. 1.2 Contribution to GDP growth at current market prices (1996-97 - 2001-02)



to 1999-00). The contribution of investment to growth has been following an uneven pattern, with a year of reasonably high contribution followed by a year of low contribution. The same erratic behaviour was observed again in 2001-02, when investment accounted for around 21 percent of the increase in GDP. Investment made up for the decline in the share of contribution by consumption expenditure, which, nevertheless, remained the largest single contributor by accounting for more than fifty percent of the increase in GDP growth.

1.27 Public investment has been partly constrained by increasing government consumption expenditure, which includes expenditure on wages and salaries, commodities, and services for current use. As a proportion of total expenditure of the Central Government, it increased from 22.8 percent in 1990-91 to 23.6 percent in 1997-98, in the aftermath of the increase in wages and salaries following the recommendations of the Fifth Central Pay Commission. Although the share of wages and salaries in total expenditure declined from 11.1 percent in 1998-99 to 10.1 percent in 2001-02 (RE), the share of consumption expenditure in total expenditure again shows a rising trend from 2000-01. The share of consumption expenditure in total central expenditure rose from 21.9 percent in 2000-01 to 22.9 percent in 2001-02, and is budgeted to increase further to 23.2 percent in 2002-03. This is primarily due to a rise in the expenditure on commodities and services for current use.

1.28 Information on consumption expenditure of State Governments as compiled by the CSO is available only till 1999-2000. The share of consumption expenditure in total expenditure of State Governments increased from 38.0 percent in 1997-98 to 39.6 percent in 1998-99 and remained at almost that level in 1999-2000. The share of wages and salaries in total expenditure increased from 30.0 percent in 1997-98 to 32.1 percent in 1999-2000.

1.29 Apart from government consumption expenditure, public investment has also been squeezed by increases in the proportion of current transfers to total expenditure. Such transfers include interest payments, subsidies, pensions, and grants, among others. Current transfers as a proportion of total Central Government expenditure increased steadily through the 1990s. As a result, the share of current expenditure in Central Government expenditure, which is consumptive and current in nature, in total expenditure, increased from 68.9 percent in 1990-91 to 79.4 percent in 2001-02 (RE), and is budgeted to decline marginally to 79.3 percent in 2002-03. The share of interest in current transfers, which constituted 53.2 percent in 2000-01, gradually declined to 51.5 percent in 2001-02, and is budgeted at 49.5 percent in 2002-03. There is, however, an increase in the share of subsidies in current transfers from 15.9 percent in 2000-01 to 16.2 percent in 2001-02, and is budgeted to increase to 18.4 percent in 2002-03. The softening of interest rates in recent years has provided some relief to the exchequer by way of reduced share of interest payments in total expenditure. Current transfers, as a proportion of total State Government expenditure, declined from 42.5 percent in 1997-98 to 39.8 percent in 1999-2000.

1.30 As a result of the softening of nominal interest rates, the real PLR of five major commercial banks, based on a 52-week average of the WPI general index, has come down marginally from 9.6 percent in 1997 to 9.0 percent by January 2003. While softer rates of interest have opened up some fiscal space for fiscal consolidation and enhanced public investment, and given a boost to housing activity, the benefits of such rates may be expected to fully accrue in terms of higher private investment over time with an improvement in investor sentiment. Investor sentiment has been constrained by poor infrastructure facilities. The leap forward in infrastructure investment, particularly in roads and telecommunications, with the National Highway Authority of India (NHAI) providing the lead in the road sector with the Golden Quadrilateral, has been a significant development in the current year.

1.31 The external current account has been strengthening over the years to provide additional demand for domestic goods and services. A surplus in the current account, observed in 2001-02 after a gap of twenty-three years, indicates, in value terms, an excess of goods and services supplied by India to the rest of the world, relative to such goods and services supplied to India by the rest of the world. While the country's traditional export drivers – gems and jewellery, textiles, engineering goods, chemicals, and ores and minerals have recovered strongly, services exports have imparted the fastest thrust to overall export growth. The surge in exports relative to imports has provided a strong stimulus to domestic industrial growth.

1.32 The net terms of trade, which measure the relative change in export and import prices, have been fluctuating with an average annual increase of 1.5 percent during the 1990s. However, with depressed prices for exports and high prices of oil, it has been deteriorating since 1999-2000; it worsened by 4.5 percent in 2000-01, and further by 2.4 percent in 2001-02. Inspite of the deterioration in the price terms of trade, the income terms of trade measuring the import-purchasing power of exports have consistently improved every year during the 1990s, except in 1996-97. On an average, the annual growth in income terms of trade has been 11.7 percent, partly fueled by strong export growth in volume terms. With exports volume growing by 23.9 percent and 3.8 percent in 2000-01 and 2001-02, the import-purchasing power of exports increased by 18.3 percent and 1.5 percent respectively, in these two years.

(c) Production

1.33 The share of services in GDP has gone up by 12.8 percentage points from 36 percent in 1980 to 48.8 percent in 2001. This increase in the share of services is strikingly similar to the corresponding rise in services' share in GDP in many other Asian courntries (Table 1.5) between 1980 and 2001. Among some selected countries given in Table 1.5, except for Indonesia and Malaysia, there is an increasing trend in the share of services, to a large extent matched by a corresponding decline in the share of agriculture. However, the industrial share of GDP appears particularly low in India. It is likely that with accelerated growth and development, there will be a rise in the share of industry in GDP. A disaggregated profile of the sectoral real growth rates in GDP for India, since 1994-95, is given in Table 1.6.

1.34 The relative performance of agriculture and industry and their contributions to growth are likely to be quite different in 2001-02 and the current year. A robust performance by agriculture (5.7 percent) was instrumental in the acceleration of GDP growth by more than one percentage point in 2001-02. Industry, by

Table 1.5: Movement in sectoral shares in GDP at current market prices in some select Asian countries

(In percent)

Country	Agriculture			Industry			Services		
	1980	1990	2001	1980	1990	2001	1980	1990	2001
China	30.1	27.0	15.2	48.5	41.6	51.1	21.4	31.3	33.6
India #	38.1	31.0	24.7	25.9	29.3	26.4	36.0	39.7	48.8
Indonesia	24.8	19.4	16.4	43.4	39.1	46.5	31.8	41.5	37.1
Korea	14.9	8.5	4.4	41.3	43.1	41.4	43.7	48.4	54.1
Malaysia	…	15.2	8.4	…	42.2	49.6	…	42.6	41.9
Pakistan#	29.6	26.0	25.0	25.0	25.2	23.0	45.5	48.8	52.0
Philippines	25.1	21.9	15.1	38.8	34.5	31.6	36.1	43.6	53.3
Thailand	23.2	12.5	8.6	28.7	37.2	42.1	48.1	50.3	49.3

 # For India and Pakistan, data are based on GDP at current factor cost.

Source : Asian Development Bank (ADB), Key Indicators 2002.

Table 1.6 : Sectoral real growth rates in GDP (at factor cost)

Item	Percentage change over the previous year							
	1995-96	1996-97	1997-98	1998-99	1999-2000	2000-2001 (P)	2001-2002 (Q)	2002-2003 (A)
I. Agriculture and allied	**-0.9**	**9.6**	**-2.4**	**6.2**	**0.3**	**–0.4**	**5.7**	**-3.1**
II. Industry	**11.6**	**7.1**	**4.3**	**3.7**	**4.8**	**6.6**	**3.3**	**6.1**
1. Mining and quarrying	5.9	0.5	9.8	2.8	3.3	2.4	1.0	4.8
2. Manufacturing	14.9	9.7	1.5	2.7	4.0	7.3	3.4	6.1
3. Electricity, gas & water supply	6.8	5.4	7.9	7.0	5.2	5.0	4.3	5.2
4. Construction	6.2	2.1	10.2	6.2	8.0	6.9	3.7	7.1
III. Services	**10.5**	**7.2**	**9.8**	**8.4**	**10.1**	**5.6**	**6.8**	**7.1**
5. Trade, hotels, transport and communications	13.3	7.8	7.8	7.7	8.5	6.9	8.7	7.8
6. Financial, real estate & business services	8.2	7.0	11.6	7.4	10.6	3.5	4.5	6.5
7. Community, social and personal services	7.9	6.3	11.7	10.4	12.2	5.6	5.6	6.4
IV. Total GDP at factor cost	**7.3**	**7.8**	**4.8**	**6.5**	**6.1**	**4.4**	**5.6**	**4.4**

A : Advance estimates; Q : Quick estimates; P: Provisional estimates

Source : Central Statistical Organisation.

contrast, had a relatively disappointing record in 2001-02, with lower growth being registered by all industry groups compared with the preceding year.

1.35 Industry has experienced a significant revival, with IIP growth of 5.3 percent in April-November 2002-03. This has been a broad-based recovery, comprising of 5.7 percent in mining and quarrying, 5.4 percent in manufacturing and 4 percent in electricity. The two key elements which led this growth were capital goods, which grew by 9.9 percent, and consumer non-durables, which had growth of 12.7 percent.

1.36 The revival of industrial growth is also reflected in freight traffic movements. Cargo handled at major ports grew by 8 percent during the current year (April-November) compared with 2.4 percent during the same period of the previous year. Over the same period, railway freight traffic grew by 6.2 percent as against 2.6 percent in the previous year. Import and export cargo handled at airports grew remarkably well during the year, while growth in volume of passengers also reversed the declining trends of the previous year.

1.37 The growth in capital goods production, as well as imports, suggests a revival of investment demand. It is corroborated by the Department of Industrial Policy and Promotion (DIPP) data for foreign direct investment (FDI), where inflows in 2002 rose to Rs.21,286 crore, as against Rs.19,265 crore in the previous year.

1.38 Two industries, which have experienced striking revivals in the current year, are steel and cement. World steel prices rose from December 2001 onwards. Domestic demand for steel and cement was supported by the highway construction taking place under the aegis of NHAI, and housing sector growth spurred by easy access to housing finance and a favourable tax regime. Improvements in technology and cost reductions have made India more competitive in exporting steel and cement. For these reasons, steel output grew by 19.8 percent in 2001-02, and a further 24.5 percent in April-November 2002. In the first half of 2002-03, cement production grew strongly by 9.5 percent.

1.39 The textile industry is a key area where India has an opportunity for labour-intensive exports. Textile products showed a strong growth of 14.8 percent in April-November 2002. A key element of this growth was an increase of 11.6 percent in exports of readymade garments in dollar terms. The powerloom segment accounted for most of the growth in fabrics.

1.40 Tourism is an environment-friendly, labour-intensive, export-oriented sector. Tourist arrivals into India fell sharply in the wake of the September 11, 2001 attack in the US and other developments. There were travel advisories by many foreign governments advising their nationals against travel to India. This resulted in group cancellations and limited future bookings. There are signs of a subsequent revival since October 2002.

1.41 Assisted by low interest rates, growth in consumer finance, and strong export demand, the automobile industry is experiencing sound growth. The number of vehicles exported during April-December, 2002, was 2,15,318, compared with 1,28,119 in the corresponding previous period, thereby registering a bouyant growth of 68 percent. Most major international companies in this industry now have operations in India, and are increasingly using India as a platform for export-oriented production. All elements of the automobile industry are functioning soundly in India, ranging from components to various kinds of vehicles, sophisticated inputs of design, research and consulting.

1.42 Gems and jewellery, which since 1998-99 has had a share of 16-20 percent in the total exports of the country, registered a buoyant growth of 28.6 percent in April-October 2002, relative to a decline of 12.2 percent in April-October, 2001. The rise in exports mainly reflects a spurt in sales to the United States, the largest importer of India's gems and jewellery. This has been assisted by policy initiatives of the government, such as delicensing of the import of rough diamonds. There are fresh efforts underway in prospecting for precious gems in the country.

1.43 In the oil and gas industry, a significant development is gas discovery in new blocks. Preliminary estimates of the in-place reserves from the recent discoveries in the Krishna-Godavari offshore, and in the Rajasthan block, are about 220 million metric tonne (MMT) of oil and oil equivalent gas. In late 2000-01, there was enough refining capacity in India relative to domestic demand, to result in India exporting petroleum products in net terms of 3.08 million tonnes in 2001-02, and 2.08 million tonnes in April-October 2002. In addition, three new refineries, adding up to a capacity of 24 million tonnes, are under construction. Natural gas production rose to 20.61 billion cubic metres (BCM) during the current year (April-November 2002), which was 4.2 percent higher than that in the corresponding period of last year. To enhance the natural gas availability in the country, eight coal bed methane (CBM) blocks have been awarded in the first round under the National CBM Policy.

1.44 India continues to make progress on export-oriented production in electronics and computer technology. Software exports have grown at a compound growth rate of over 50 percent per year for the last five years. There are now signs of headway being made in the field of hardware exports as well. Hardware exports grew sharply in 2000-01 and 2001-02, reaching a level of Rs.5,871 crore in 2001-02, with growth of 22.6 percent over the previous year. Many top information technology (IT) firms from across the world have started utilising India in their global production chains, and in high-end functions such as research and development.

1.45 One important area of policy focus has been the resolution of failure, or the creation of swift and efficient mechanisms through which labour and capital in failed firms can be reutilised as efficiently as possible. This is closely related to the problem of creditors rights. Initiatives like the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Bill, 2002, giving creditors the ability to seize collateral when a loan becomes delinquent, and amendments made to the Companies Act, which are likely to improve the working of the BIFR, can significantly reduce the loss of output associated with failed firms. In December 2002, the Competition Bill 2001 was passed in Parliament. This seeks to establish a pro-competitive legal framework, contain anti-competitive practices and abuses of dominance and yield better regulation of markets.

1.46 The government has been following a policy of privatisation of non-core enterprises, in the quest for greater productivity. There has been a steady stream of transactions where PSUs, or productive assets such as hotels, have been sold through strategic sales. Contrary to fears expressed earlier, these transactions have not had any harmful effects upon employment.

1.47 In 2002-03, with seasonal rainfall falling short of its normal volume by 19 percent, the country experienced the most deficient monsoon after 1987-88. Seventeen states of the country experienced moderate to severe drought conditions. Kharif foodgrain output (rice, coarse cereals and pulses) declined by 19 percent compared to the previous year. Among commercial crops, oilseeds were the worst hit, followed by cotton and sugarcane. While a strong rabi harvest in April 2002 had led to a four percent growth for agriculture in the first quarter of the current year, the subsequent poor monsoon has cast its shadow on the outcome of this year's rabi crops, even though the late January rainfall may imply normal wheat harvest in Punjab and Haryana.

1.48 The decline in this year's projected foodgrain production to 183.2 million tonnes compared to last year's output of 212 million tonnes, (13.6 percent fall) is large. Fortunately, though, the accumulated public stock of foodgrains provide a cushion to more than compensate for this shortfall, the most important effect of which is the absence of an inflationary undercurrent amongst primary product prices.

1.49 The services sector, the most consistent performer in recent times, maintained its growth momentum in 2001-02, as well as in the first half of the current year. Trade, hotels, transport & communications, and financing, real estate & business services, improved their performance in 2001-02 over 2000-01. In the current year, on a year-on-year basis, in terms of GDP, the services sector registered a growth of 7.6 percent in the first and second quarters, respectively. According to advance estimates released by the CSO, services sector GDP is estimated to grow by 7.1 percent in 2002-03, a rate higher than the 6.8 percent observed in 2001-02.

1.50 The demand generated by enhanced public investment in physical infrastructure has been a key stimulant behind industrial recovery. The impressive progress of the National Highway Development Project (NHDP), one of the most ambitious highway projects in the world, has provided strong backward linkages for the steel and cement industries. Major gains have also been achieved in telecommunications in the current year. New telephone connections during the current year (April-December) have shot up by 17 percent compared to the corresponding period of the previous year. Out of these, 63 percent are attributable to cellular phones, underlining the growing preference of new consumers towards mobile services. Progressively falling tariffs have expanded the cellular subscriber base in the country to 10.4 million from just 0.3 million within a little over five years.

1.51 Despite a disappointing performance by hydroelectric power owing to scanty rainfall, overall power generation has improved during the current year, due to good growth in thermal and nuclear generation. Rural electrification has been proceeding fast, with ten states having achieved 100 percent village electrification. The country is slated to electrify all villages by 2007. Apart from electrification, rural infrastructure is being strengthened through the Pradhan Mantri Gram Sadak Yojana (PMGSY), under which more than 10,000 rural roads have already been constructed.

(d) Employment and poverty

1.52 No official poverty estimates are available beyond 1999-2000, the year of the 55th round of the National Sample Survey (NSS). However, the NSS 56th round (July 2000-June 2001) report on household consumer expenditure and employment-unemployment situation in India, for 2000-01, albeit on a thin sample, provides some insights into developments in labour markets and monthly per capita consumption expenditure.

1.53 The work force participation rate (WFPR) – which is the number of persons employed per 1,000 persons – for rural (urban) males according to 'usual status' went up from 522 (513) in the 55th round (July 1999 – June 2000) to 532 (525) in the 56th round when only "principal status" is considered, and from 531 (518) to 544 (531) when principal plus subsidiary status (all) are taken into account. The corresponding increase for rural (urban) males according to the current weekly status is from 510 (509) to 525 (519). However, there is a decline in WFPR for rural (urban) females from 231 (117) in the 55th round (July 1999 – June 2000) to 221 (116) in the 56th round, when only principal status is considered. When principal plus subsidiary status are both taken into account, female WFPR, between the two rounds, shows a decline from 299 to 287 in rural areas, but a marginal increase from 139 to 140 in urban areas. According to the current weekly status, WFPR for females declined from 253 to 217 in rural areas and from 128 to 117 in urban areas.

1.54 WFPR for rural males (usual status-all) in the age group of 15-59 years was 87 percent in the 55th and 56th rounds. For rural females, WFPR declined from 48 percent in the 55th round to 46 percent in the 56th round. For urban males, WFPR during this period increased from 78 percent to 79 percent. However, for urban females, WFPR was about 21 percent in both rounds. During the period 1998 to 2001, for the age group 15-59 years, the WFPR has tended to increase for three categories, namely, rural males, urban males, and urban females. In urban areas, the increase was larger for females than for males.

1.55 In rural India, according to the 'usual status', about 69 percent of the male workers and 82 percent of the female workers are engaged in agricultural activities. In urban India, about 58 percent of the male workers and about 48 percent of the female workers are engaged in tertiary sector activities.

1.56 Between the 55th round and the 56th round, the all-India average for monthly per-capita consumption expenditure went up from Rs. 486.16 to Rs. 494.90 for rural areas, and from Rs. 854.92 to Rs. 914.57 for urban areas.

1.57 Organised sector employment has witnessed some positive trend in the private sector, which, in the current state of buoyancy of the industrial sector, should further accelerate if some of the rigidities in the labour laws are removed. The Industrial Disputes Act, 1947, Contract Labour Act, 1970, and Payment of Wages Act, 1936, are some of the legislative instruments that the government is considering for amendment. Simultaneously, the government is also proposing to bring forth a comprehensive legislation for the welfare of workers in the unorganised sector. Under the Minimum Wages Act, in January 2002, wages were raised for workers of mining and construction sectors in respect of scheduled employment in the Central sphere.

1.58 According to the data from the NSS rounds, between July 1999-June 2000, and July 2000-June 2001, the number of 'chronically hungry' households (not getting enough food everyday during even some months of the year) per thousand households, declined from 12 to 6 in the rural areas, and 7 to 2 in the urban areas. The decrease in the number of 'seasonally hungry' (getting enough to eat everyday in only some months of the year) per thousand households, fell from 26 to 19 in rural areas and from 6 to 4 in urban areas. Against this evidence of continued 'seasonal hunger', this year's drought has caused enhanced distress in a number of chronically deficit areas. With the drought affecting large parts of the country, the pursuit of active food management policy helped in containing the incidence of poverty and deprivation. The off-take of foodgrains under various welfare schemes such as Annapurna, World Food Programme, Sampoorna Grameen Rozgar Yojana, indigent people, nutrition programme, hostel for scheduled caste/scheduled tribe/other backward castes, food for work, and mid-day meal, at 5.48 million tonnes during April-October, 2002, was considerably higher than 3.15 million tonnes during the same period of the previous year. The stability in prices of essential items, including food, through the management of the adequate buffer stock has helped in protecting the poor from some of the suffering that is traditionally associated with droughts in the country.

1.59 Apart from drought relief, the Government has taken a few other measures for improving living conditions in both rural and urban areas. Central allocation has been stepped up under the Accelerated Rural Water Supply Programme (ARWSP). The corpus of the Rural Infrastructure Development Fund (RIDF) has been enhanced in the current year along with a reduction in the rate of interest on loans from the Fund. The rural housing initiative is being carried forward through the ongoing Indira Awaas Yojana (IAY) scheme. Housing activity in the country, on the whole, has shown distinct signs of pick-up, as reflected in the higher outflow of credit to housing during the current year, primarily on account of encouraging fiscal incentives for housing finance. The Housing and Urban Development Corporation (HUDCO) has been the key player in stepping up housing finance. HUDCO has also been instrumental in implementing the low cost sanitation scheme in urban areas, which intends to eliminate manual scavenging, and under which 860 schemes have been sanctioned in almost 1,500 towns till the end of December 2002.

Issues and priorities

1.60 The current year is the first year of the Tenth Five Year Plan (2002-07), which envisages an average annual growth rate of 8 percent. While the growth performance in recent years has been lower than this target, international evidence, as well as India's own experience, demonstrate that the target is indeed feasible. Malaysia, Republic of Korea, and Thailand, among other East Asian countries, sustained annual growth rates at levels equal to, or higher than what India is seeking to achieve in the Tenth Plan, for several years, before the outbreak of the East Asian crisis. The People's Republic of China, a large country like India in terms of both area and population, has been one of the best performers among the major economies of the world during the 1980s and 1990s, and has been maintaining high growth (7 percent plus) despite the recent slowdown in global economic activity. Furthermore, the acceleration in growth in these countries from fairly modest initial levels took place rapidly, almost in the manner of a jump-start.

1.61 The experience of India in terms of growth acceleration is also similar to that of countries in East Asia and China. The decadal average annual growth rate of the Indian economy, after fluctuating around 3½ percent for the decade of the 1950s, 1960s and 1970s, took a quantum leap to 5.65 percent in the decade of the 1980s (Figure 1.3). Similarly, after hitting a low of 1.3 percent in 1991-92 in the aftermath of the balance of payments crisis, the annual rate of growth rapidly accelerated to around 7½ percent during 1994-95 to 1996-97 (Figure 1.4).

1.62 The drivers of change and rapid growth acceleration have to be technology and competition, together with benchmarking to the best international practices. India is now taking advantage of all three factors. Technology is getting upgraded rapidly and competition in the market place has become fierce. The IT revolution, and the vibrant IT industry in the country, have been critical factors in making information available about state of the art technology and in bridging the technological divide in some sectors. With quantitative restrictions on imports a thing of the past, customs duties progressively coming down, and foreign investment – both direct and portfolio – liberalized, integration of India into the global economy is also progressing. Buoyant export performance, a surplus in the current account, and the strong balance of payments position demonstrate the success of the country in this integration process.

Fig. 1.3 **India : Decadal growth rates (1951-52 — 1990-91)**

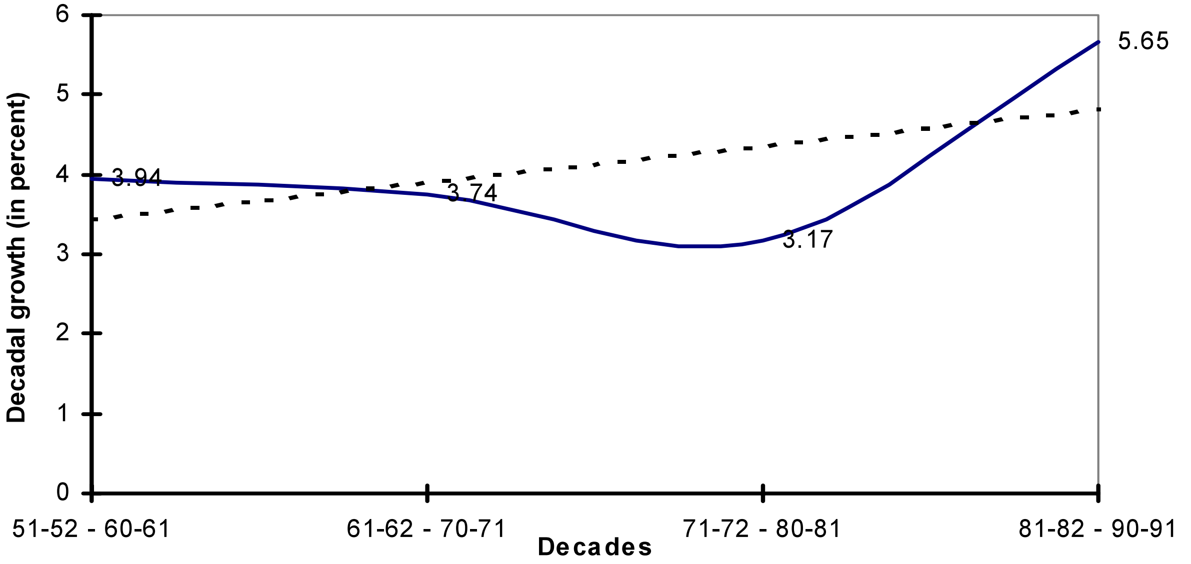
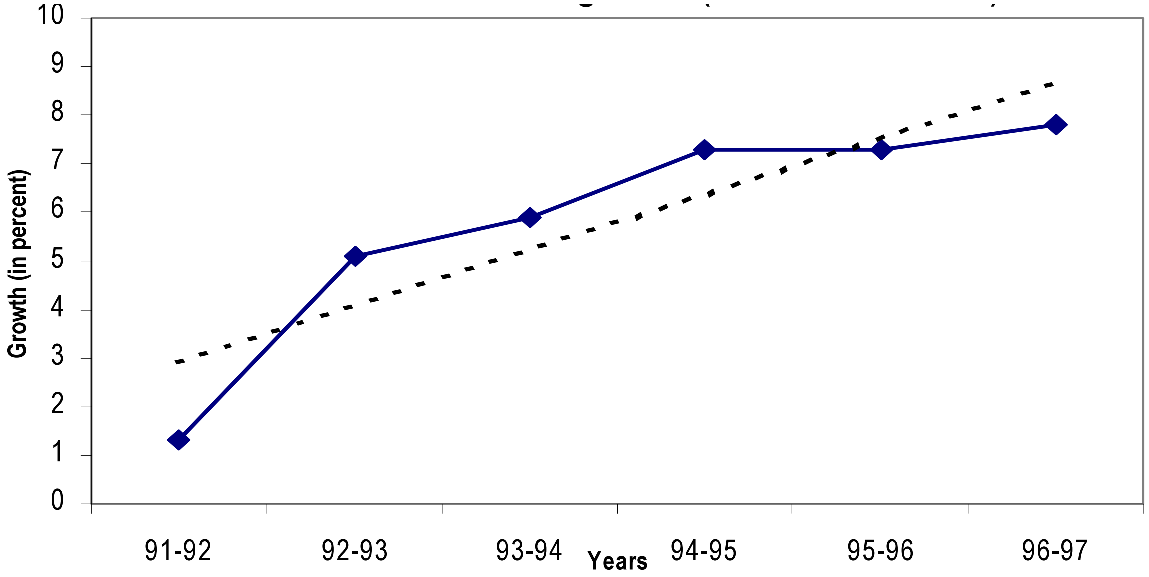


Fig. 1.4 India : Annual GDP growth (1991-92 — 1996-97)



1.63 There is an intimate and virtuous interaction among the drivers of change mentioned earlier. This is best illustrated by the consumer goods, automobiles and telecommunications industries in the country. Previously under quantitative restrictions, consumer goods can now be imported freely upon payment of customs duty. While some foreign consumer products have appeared in shops, particularly in up-market segments, their presence is limited. However, there has been a remarkable improvement in the quality of domestic consumer products, with convergence towards the best international practices.

1.64 The automobile sector, previously under a strict licensing regime, has been a direct beneficiary of competition and technology in the new liberal regime. Not only has automobile output grown at double digit compound rates, but the sector has become a sizeable exporter. Major international auto-companies now have operations in India, and are increasingly using the country as a platform for export-oriented production. There is also a strong set of upstream firms, producing ancillaries for, and providing design consultancy to the automobile industry. The telecommunications sector provides another illustration of a virtuous interaction between technology and competition. While mobile telephony is rapidly raising teledensity, price competition between two technologies, namely Global System for Mobile (GSM) and Code Division Multiple Access (CDMA), has yielded price benefits to the consumer.

1.65 It is vital that this virtuous interaction among technology, competition, and benchmarking to the best international practices is extended to agriculture. While the spectacular growth in production of cereals has been instrumental in ensuring the country's food security, there is a need to accelerate the trend towards growing diversification in agriculture.

1.66 The principal focus in the past five decades was to maintain foodgrains growth abreast of population growth. India has been successful in this regard. All the facets of agriculture policy so far have been guided for meeting shortages as it was considered risky for a country of India's size to depend on imports for meeting critical shortages in essential commodities like foodgrains and sugar. However, there remain vital areas, which in the process have remained rather neglected. India's advantage lies in owning the asset of the largest arable land area next only to U.S.A., and ranking first in irrigated area in the world. Most importantly, the country is characterised by a variety of agro-climatic regions that enables production of all possible kinds of tropical, semi-tropical and temperate agriculture products. The focus, therefore, has to shift towards improving productivity in horticultural products that encompass a variety of fruits and vegetables, which would have a global market if only these products are properly graded, processed, packaged and transported under fast and modern transit systems. Value addition in horticulture, floriculture, and sericulture, as well as in food processing can yield rich dividends to farmers and expand the scope for quality employment. Whereas success stories have been reported in competing in the global market for export of flowers and fruits from Maharashtra, Andhra Pradesh, and even Uttar Pradesh, the vast potential for exports of value added horticultural products can be realised only when there is appropriate infrastructure specific to processed agri-product exports available in the country. There are many ports which do not have mechanical loading facilties for fast moving products. India currently produces 145 million tonnes of fruits and vegetables, of which less than 2 percent follow the processing route thus depriving Indian producers of the benefits of value addition, and access to global markets.

1.67 What is needed in addition is not only improved seed technology and modern irrigation systems, but also processing industries specific for various agriculture products. Unlike cereals and oilseeds, fruits and vegetables are perishable. Cold storage is essential for their preservation. There is some acceleration noticed in expanding cold storages in the current year. But irregular and poor quality of power supply has been acting as a serious barrier to growth in cold storages. The key to value addition in agriculture, and consequent income and employment growth in rural areas, lies in building up the required infrastructure. Public-private partnership can play a vital role in promoting this infrastructure. The earlier emphasis on raising irrigation potential has to be renewed with greater vigour, especially through watershed development. Access to water – potable drinking water, and ordinary water for irrigation – is an absolute necessity and should constitute an integral part of the strategy for rural infrastructure development.

1.68 Water will increasingly emerge as a scarce resource. The vulnerability of Indian agriculture to monsoon failures has focused renewed attention on how best to utilise this scarce resource. It is also time to rethink whether the country can afford the practice of irrigation through field flooding, which is basically wasteful, and evaluate more economic methods of irrigation. The Accelerated Irrigation Benefits Programme (AIBP), aiming to help states in establishing irrigation facilities through Central Loan Assistance (CLA), has assured full central assistance to approved major and medium irrigation projects being completed within a year, under its fast track programme from February 1, 2002. A new initiative, 'Hariyali', intending to strengthen the technical capabilities of panchayati raj institutions (PRIs) for implementing the existing watershed development programmes like Integrated Wasteland Development Programme (IWDP), and Drought Prone Area Programme (DPAP) — has been launched on January 27, 2003. What is important, however, is a mechanism for more efficient cost recovery to not only ensure adequate funds for operation and maintenance, but also to promote a sense of user participation and water conservation.

1.69 The flow of institutional credit to agriculture has witnessed a sharp increase of 21 percent in 2001-02 compared with 14 percent in 2000-01. This seems to have had a positive impact on capital formation in agriculture in 2001-02. Under the Kisan Credit Card (KCC) scheme, more than Rs 64,000 crore has been sanctioned till September 2002. The scheme intends to cover all eligible farmers by March 31, 2004, and is also extending personal insurance cover (for accidental death, permanent disability etc.) to its beneficiaries. The National Agricultural Insurance Scheme (NAIS), which extends to all food crops, had covered more than 20 million farmers till rabi 2001-02. Implementation of NAIS will soon be taken over by the Agriculture Insurance Company of India Ltd., which is now awaiting registration with the Insurance Regulatory and Development Authority (IRDA). This new corporation, set up with an authorised capital of Rs 1,500 crore by the General Insurance Corporation (GIC), NABARD, and four public sector general insurance companies, also aims to cover other rural/agricultural risks in addition to crop insurance. There is a strong case for utilizing the services of self-help groups and other micro-credit institutions and, with proper regulatory systems, enlisting the support of local persons with knowledge of local conditions to efficiently lend money from banks to farmers, while reducing transactions costs and minimizing the risk of default. Participation of private insurers in agricultural insurance will also provide the benefits of a competitive market.

1.70 Despite the vast variety of agro-products produced, the country's annual agro-exports are valued at less than US $ 6 billion with marine products alone accounting for 20 percent. Exploiting the country's untapped export potential in agriculture requires removal of regulatory inefficiencies like prohibitive food standards laid down by the Prevention of Food Adulteration Act, the Food Products Order, the Meat Products Order and the Bureau of Indian Standards. During the current year, the number of commodities under the Essential Commodities Act have been reduced to eighteen. The restrictions on movement and stocking of six agricultural products have also been removed with the objective of establishing a common market in the country. Futures trading in agriculture has been extended to 42 commodities including sugar and tea. However, in order to promote diversification in agriculture by enabling producers to directly access new markets, it is essential to amend the Agricultural Produce Marketing Committee (APMC) Act. This would, however, require urgent action on part of States since agriculture is a State subject. The reform measures adopted in the current year are likely to create new avenues for private investment in agriculture and lay the foundation for value addition besides improving quality of agro-products for global markets.

1.71 The virtuous interaction among technology and competition in India, while benchmarking to the best international practices, will need an enabling environment and will need to be facilitated by three factors: appropriate social and physical infrastructure, a suitable regulatory framework and an efficient tax system, and macro-economic stability.

1.72 Amongst the priority areas requiring focussed attention are the elimination of illiteracy, reduction in infant and maternal mortality rates, eradication of diseases such as malaria and polio, provision of quality transportation facilities in the form of roads, railroads, ports and airports, reliable and reasonably priced power supply, and safe drinking water and sanitation. There is a need to encourage public-private partnership in promoting infrastructure to leverage public funds, improve quality of service delivery and ensure better value for money. The success achieved under the NHDP launched by the Prime Minister in October 1998 indicates that there is considerable scope for new methods of financing and public-private partnerships in this area. It is essential to build on the limited success achieved in promoting public-private partnerships in the field of power generation, transmission and distribution, and accelerate reforms to remove an important bottleneck on the country's development. There is considerable scope for improving the delivery of social services, such as health care, by promoting community and private sector participation. What is required is a change in the paradigm of the public sector to 'providing' public goods and services, without necessarily "producing" them itself.

1.73 Considerable progress has been made in the area of regulatory framework and a suitable tax system. For example, the Telecom Regulatory Authority of India (TRAI), State Electricity Regulatory Commissions (SERCs), Insurance Regulatory and Development Authority (IRDA), Securities and Exchange Board of India (SEBI), have been functional for some time. The Competition Bill, 2001 has also been passed by the Parliament. However, what is needed is an overhaul of the regulatory regime in agriculture. A closely related issue is the question of labour market reforms and small-scale industry (SSI) reservation. The country should seek to sell to the global market consumer goods of quality, at competitive prices, produced in large-scale establishments operating under flexible labour-markets. Furthermore, it is essential to restructure the tax system with a move to an impersonal and efficient tax administration with a minimum interface between the assessee and the tax official, and a system with minimum of exemptions in the field of central excise and States sales tax, and a move to a value added tax (VAT). The proposed move to VAT by the States from April 1, 2003 will be an important landmark in establishing an efficient and self-enforcing domestic tax system with minimal cascading effects. A reduction in the rate of Central Sales Tax (CST), and its elimination over time will be important steps towards the establishment of a unified Indian common market.

1.74 India is moving towards macro-economic stability through the pursuit of a suitable combination of fiscal and monetary policies. While sluggish growth suggests counter-cyclical policies, there is a need to step up progress in the field of fiscal consolidation. The fiscal deficit, as a proportion of GDP, has gone up from 4.1 percent in 1996-97 to 5.9 percent in 2001-02 for the Central Government, and from 9.5 percent in 1999-2000 to 10.0 percent in 2001-02 for the general government (i.e. consolidated Centre and States). While the rate of interest continues to be below the rate of growth of the economy, high primary deficits (fiscal deficit less interest payments) have led to progressive increases in both the deficit to GDP and debt to GDP ratios. Increases in debt, with the associated high interest payments, have resulted in pre-emption of a very large proportion of revenue receipts, both of the Centre as well as of the States, by interest payments, wages and salaries, and pensions. Given the indices of growth recovery already visible, without fiscal consolidation, there is a risk that the preemption of resources by the general government will crowd out the nascent recovery in private investment.

1.75 Fiscal consolidation requires a two-pronged strategy of augmenting revenues and restraining expenditure. An efficient, computerized, and impersonal tax system is critical for increasing the tax-GDP ratio. In non-tax revenue, there is a clear need for better cost recovery through appropriate user charges. On the expenditure front, it is critical to contain the growth of wages, salaries and pensions. There is a need to revise the rate of interest on small savings mobilised by the government in line with movements in market related interest rates. Any successful expenditure rationalization and reprioritization programme must address the issue of subsidies, through a rationalization of the prices of food, fertilizers, LPG and kerosene. There is a need to look into the whole issue of federal fiscal transfers, including the role of the plans, gross budgetary support for the plans, and why plan expenditure affects the path of fiscal deficit and debt adversely, and how.

1.76 With India emerging as a surplus producer of a number of exportable agricultural products, including foodgrains, in recent years, efficient management of the country's food economy has become a major policy issue. The comparative and regional advantage of some crops, has, however, been distorted by minimum support prices (MSP) for rice and wheat, thus generating both surpluses (sugar, rice, wheat) and shortages (oilseeds, pulses and fibres). Accumulation of large food stocks has posed serious issues with regard to the effect of current food management policy, not only on agricultural growth and diversification, but also on the fiscal deficit. The merits of the MSP in achieving the objective of food security is established. So is the general consensus that some food subsidy is absolutely essential for providing income support to the country's poor and vulnerable. Apart from providing subsidised foodgrains to the Below Poverty Line (BPL) population (over 30 crore), a most significant and innovative measure to address abject poverty is the Antyodaya Anna Yojana, which enables a section of the poorest (about 6 crore) to obtain 35 kg foodgrains per month at the low price of Rs.2/- per kg for wheat and Rs. 3/-per kg. for rice. It is important, however, to recognize that our procurement methods have begun to seriously distort, and also eliminate the role of private trade in foodgrains, thus aggravating the subsidy commitment of the Central Government. There is a need to economise on buffer carrying costs, as also procurement costs, which may be possible by involving state participation in procurement. FCI is faced with serious diseconomies of scale, since it is now procuring and stocking almost three times the normal volume of grains.

1.77 The last quarter of the current financial year has seen rapid escalation of tensions in the Persian Gulf. The possibility of hostilities breaking out in the Middle East has cast doubts over the pace of global recovery in 2003. With global crude oil prices rising, there are serious concerns regarding the growth prospects of emerging market economies, particularly those in developing Asia, in the coming months. Apart from large food stocks held in the central pool, the huge volume of foreign exchange reserves held by the country provide comfort in an uncertain global situation. With reserves rising to more than US$73 billion, India is now one of the top reserve-holding, emerging market economies. The country is capable of financing higher import bills in the event of steep escalation in global oil prices or other exogenous developments. However, a prolonged conflict in the Middle East is likely to affect the export prospects of several economies of developing Asia, due to their heavy dependence on the US economy. Notwithstanding a marginal compression in export prospects, the overall growth performance of the Indian economy in the coming months is unlikely to be seriously affected by the developments in the Gulf, due to the clear signs of revival in domestic demand, and the resultant buoyancy imparted to domestic economic activity. Nevertheless, there is an imperative need to address the three issues of infrastructure, regulatory and tax reform, and fiscal consolidation, to establish the foundations of robust growth on a sustained basis.