

## Outlook

6.76 With the strengthening of global recovery, prospects for growth in global output and trade in 2004 have brightened. The expected robust pick up in global trade is likely to contribute to the overall growth of Indian economy. However, significant downside risks to this growth persist. These include continuing firmness of global oil prices, volatility among major currencies and the danger of interest rate hikes in developed countries. Efficacy of macro policies in carefully managing the impact of a potential global transition from low interest rate and currency imbalances to a more sustainable regime, therefore, gains relevance.

6.77 External sector continues to be a source of strength, providing comfort to the conduct of such public policies. The sector has strengthened over the years with fragility of balance of payments being no longer a policy concern. While trade deficit has increased, the current account has been in surplus for the last three years, largely because of remittances from non-resident Indians. The large capital flows in 2003-04 have resulted in a further accumulation of reserves, rendering reserve position comfortable as per various indicators of reserve adequacy. These reserves provide an opportunity towards deepening of trade reforms and other administrative measures. India is already being seen as a new hub for exports of auto parts and other engineering goods and opportunities are expected to open in the textile sector after the phasing out of ATC next year. Micro strategies for export growth based on various policy pronouncements need to be designed to put export growth on a higher and sustainable growth trajectory. A reduction in tariffs towards the already announced alignment of tariff structure with ASEAN countries is likely to have beneficial effect on the competitiveness of the economy. Export promotion policies also need to utilize the natural complementarity of FDI with export activity, as the global

reach and marketing ability of FDI could be effectively utilized to provide a cutting edge to the export effort. The impressive increase in imports of capital goods bolsters the hope of accelerated investment activity in 2004-05. Efforts towards strengthening of the services sector to promote services exports, in which India has a competitive advantage, need to be sustained and intensified. A further simplification of the domestic policy regime, rules and procedures is likely to attract higher foreign investment, thus supporting the investment needs of the economy for higher growth.

6.78 Trade liberalization is likely to counter some of the upward pressure on the exchange rate of the rupee. Current exchange rate policy of focusing on managing volatility with no fixed rate target, while allowing the underlying demand and supply conditions to determine the exchange rate movements in an orderly way, has stood the test of time. This broad approach of watchfulness, caution and flexibility in the foreign exchange market needs to be continued. Exchange rate management policy needs to balance build up of reserves and domestic liquidity on the one hand and maintaining external competitiveness with low inflation and interest rates on the other. This may entail some moderation in the exchange rate appreciation on account of concerns about the competitiveness of exports and maintaining a stimulative macroeconomic environment. Hence, the policy of flexibility in exchange rate together with ability to intervene, if and when necessary, needs to be continued.

6.79 Prudent reserve management has emerged as an important macroeconomic policy challenge. Suitable policy measures to facilitate greater productive absorption of capital flows for growth promoting purposes are likely to facilitate higher investment in the economy. The improvement in external debt position has been consolidated through recourse to pre-payment by Government as well as the corporates. The debt

management policy should continue with its focus on concessional and less expensive sources of funds, preference for longer maturity profiles, a constant vigil on build up of short term debt, focus on non debt creating capital flows and prepayment of high cost external loans.

6.80 An immediate challenge for the global community is to achieve further multilateral trade liberalization under the Doha round of trade negotiations. Given need for such liberalization, recent protectionist measures

by some countries against BPO misses out not only the efficiency gains from such outsourcing but also the employment gains from the resources saved in the process and deployed in other employment generating sectors. There is, thus, an urgent need to revive the trade negotiations under the WTO, as a successful conclusion to the Doha Development Agenda could contribute to a stronger and more even expansion of world trade and sustained global economic growth.