External trade

1.53 India's greater integration with the world economy was reflected by the trade openness indicator, the trade to GDP ratio, which increased from 22.5 per cent of GDP in 2000-01 to 34.8 per cent of GDP in 2006-07. If services trade is included, the increase is higher at 48 per cent of GDP in 2006-07 from 29.2 per cent of GDP in 2000-01, reflecting greater degree of openness.

1.54 India's merchandise exports and imports (in US$, on customs basis) grew by 22.6 per cent and 24.5 per cent respectively in 2006-07, recording the lowest gap between growth rates after 2002-03. Petroleum products (59.3 per cent) and engineering goods (38.1 per cent) were the fastest growing exports. The perceptible increase in share of petroleum products in total exports reflected India's enhanced refining capacity and higher POL prices. The rising share of engineering goods reflected improved competitiveness. The value of POL imports increased by 30 per cent, with volume increasing by 13.8 per cent and prices by 12.1 per cent in 2006-07. Non-POL import growth at 22.2 per cent was due to the 29.4 per cent growth of gold and silver and 21.4 per cent growth of non-POL non-bullion imports needed to meet industrial demand.

1.55 In the first nine months of the current year, exports reached US$111 billion, nearly 70 per cent of the year's export target. During April-September 2007, the major drivers of export growth were petroleum products, engineering goods and gems and jewellery. Machinery and instruments, transport equipment and manufactures of metals have sustained the growth of engineering exports. There was a revival of the gems and jewellery sector with export growth at 20.4 per cent for April-September 2007, after a deceleration in 2006-07.

1.56 Imports grew by 25.9 per cent during April-December 2007 due to non-POL imports growth of 31.9 per cent, implying strong industrial demand by the manufacturing sector and for export activity. The merchandise trade deficit in April-December 2007 at US$ 57.8 billion was very close to the trade deficit of US$ 59.4 billion for 2006-07 (full year). Despite the large overall trade deficit, there was a large (but declining) trade surplus with the United States and UAE, and a small surplus with the United Kingdom and Singapore (till 2006-07). The surplus with the first three has continued in 2007-08. The largest trade deficits are with Saudi Arabia, China and Switzerland. The trade deficit with China has increased further in April-September 2007.

1.57 A comparison of the commodity-wise growth of major exports to the United States, European Union and rest of the world provides a better idea of the impact of economic slowdown and rupee appreciation. Manufactured exports to the United States decelerated sharply in 2006-07 because of demand slowdown while dollar depreciation was an additional factor in 2007-08. The slowdown of exports to the European Union was marginal because both factors were absent. In contrast, there was a marginal acceleration in manufactured exports to the rest of the world in the first half of 2007-08. India's exports of textiles, leather & manufactures and handicrafts to US performed poorly in 2006-07, even though the rupee depreciated marginally. However, exports of all subcategories, including engineering goods and chemicals, have decelerated in the first half of 2007-08. In the case of EU, the sharp deceleration in textiles and poor performance in handicrafts were substantially offset by reasonable growth in other manufactures in 2006-07 and the first half of 2007-08. Leather and leather manufactures exports have performed well overall and to EU and other countries, while showing a decline in the case of United States. Thus, there seems to be a greater corelation between the demand in partner country and the bilateral exchange rate, on the one hand, and India's bilateral exports at a disaggregated level, on the other, than is visible for total Indian exports to the world.

1.58 Trade with the top 12 trading partners increased by over 11.2 percentage points since 2001-02 to 53.8 per cent of total in 2006-07. The share of the United States, the largest trading partner, declined by 2.5 per cent points to 9.8 per cent in 2006-07 while China became the second largest partner in 2006-07 with its share increasing by 5.2 percentage points over the decade. China's trade share during April-October 2007 is even higher than that of the United States by Rs. 600 crore.

1.59 India's export of services grew by 32.1 per cent to US$ 76.2 billion in 2006-07. Software services, business services, financial services and communication services were the main drivers of growth. Commercial services exports were almost 60 per cent of merchandise exports in 2006-07. However, services exports grew by a disappointing 8.6 per cent in April-September 2007, due to a decline in value of non-software services, particularly business and communication services.

1.60 India has continued to favour multilateral trading arrangements which are both transparent and fair to the developing economies. After the suspension of negotiations in July 2006 due to differences in perceptions, safeguarding the interests of low income and resources poor agricultural producers along with making real gains in services negotiations and addressing growth and development concerns in industrial tariff negotiations.

Rupee appreciation

1.61 With the demand for foreign exchange (debit side of BOP) not keeping pace with the supply of foreign exchange (credit side of BOP), the rupee appreciated by 8.9 per cent against the US dollar during the current financial year between April 3, 2007, and February 6, 2008. The rupee appreciation against the US dollar over the past 12 months on year-on-year basis (December 2007 over December 2006) at 13.2 per cent was even higher. While the rupee appreciated against other major currencies as well for most parts of the year, it was modest as compared to the rise against the US dollar. It even depreciated marginally against the Euro during the financial year (till February 6, 2008).

1.62 The appreciation of the rupee against the US dollar could be attributed to the effect of depreciation of the US dollar against all the major currencies and the surge in capital flows. The REER (6 currency, trade- based weights) that indicates the real competitiveness by factoring the relative price levels, after depreciating in 2006-07, appreciated by 7.8 per cent in April-January 2007-08. The appreciation of the rupee vis-à-vis the dollar, the main invoicing currency of exports, compared to the lower appreciation of competing countries coupled with the slow growth in imports of major trading partners like the United States, affected exports of some sectors with low import intensity. To mitigate the effect and facilitate adjustment, the government announced relief measures to selected sectors.

Stock markets

1.63 Stock markets are an important instrument of financial intermediation. They saw increased activity in 2007-08. Primary market issue of debt and equity increased along with private placement. The secondary market too showed a rising trend, notwithstanding intermittent ups and downs in the stock prices responding mainly to global developments. The Bombay Stock Exchange (BSE) Sensex rose from 13,072 at end-March 2007 to 18,048 as on February 18, 2008, while the National Stock Exchange (NSE) index Nifty 50 rose from 3,822 to 5,277 during the same period. Both the indices gave a return of around 38 per cent during this period. The higher net mobilization of resources by mutual funds showed that investors were realising the importance of using intermediaries in risky markets. All the other indicators of capital market such as market capitalization, turnover and price-earning ratio remained strong. The commodity market also showed signs of expansion in terms of turnover and number of transactions during the year.