Issues and Priorities

62. The sharp slow down in GDP and export growth following three years of high growth in each case, are two central areas of concern. Export growth decelerated sharply in 1996-97 and 1997-98, accompanied by a marked deceleration in industrial growth. The level of concern regarding the fiscal deficit and infrastructure problems continues to rise with each passing year. Higher growth is the best antidote for removing mass poverty and unemployment, and for generating revenues needed to supply public goods and other vital government services. Therefore, it is imperative to put back the economy on a higher growth path of the order 7 to 8 per cent per annum. This would necessitate raising of our savings rate to about 30 per cent of GDP through a reduction of government dissavings, an improvement in the performance of non-traded infrastructure (energy, transport and communications) and restoration of export growth to respectable levels.

63. The slippage on the fiscal front during 1997-98 is a cause of concern. Continuing high deficits have a number of adverse consequences. Lack of fiscal flexibility complicates the task of preserving macroeconomic stability, as it puts a heavy burden on monetary policy. Pre-emption of credit by the government is likely to crowd out credit to private sector and raise interest rates. This in turn would dampen the recovery of private production and investment. It could also constrain the pace of financial liberalisation.

64. Our earlier experience shows that high levels of government expenditure and fiscal deficits can also put pressure on the current account deficit in the balance of payments. This is particularly important at a time when export growth has slowed. Among the reasons for the slow down in export growth is the slower growth of world trade, the real appreciation of the rupee vis-à-vis our trading partners, and the very sharp depreciation of the currencies of some of our potential competitors in Asia. It is therefore essential to maintain a market-responsive exchange rate determined by fundamental demand-supply factors, while containing any excessive short-term volatility. Further, as FDI is the most stable form of capital flow, the share of FDI in total capital flows must be raised progressively. FDI also has the additional benefit of introducing new technology, techniques and practices into the economy. ECB, FII and FDI norms and procedures have been substantially liberalised in past years to facilitate the flow of funds for production and investment. Greater procedural simplifications are however still necessary in the area of FDI.

65. States have also to share the responsibility of fiscal consolidation and prudence in a federal polity. State finances need to be strengthened, for both macroeconomic and structural reasons. An expansion in revenue expenditure by states raises the revenue deficit while leaving little funds for developmental expenditures, especially for the key area of human resource development. Inadequate infrastructure (irrigation, electricity, roads etc) and human capital formation (expenditures on education, basic health etc.) where states shoulder major responsibilities have large costs not only to the states concerned but beyond their borders. Similarly, inefficient state taxes can limit the benefits accruing from the reform of central taxes.

66. Though the rate of growth in non-food credit of 14.2 per cent in 1997-98 was higher then that in 1996-97 (10.9 per cent), it was much lower than that in 1995-96 (22.5 per cent). The slow growth in non-food credit remained a source of concern in view of deceleration in industrial production. However, the significant expansion in bank investment commercial papers and other debt instruments like bonds and debentures of both PSUs and private corporates has complemented non-food credit. Nevertheless, measures need to be taken to induce banks to step up delivery of non-food credit to medium and small industrial units. At the same time, considering the prevailing low rate of inflation, real interest rates are high, making the cost of institutional funds expensive. The banking system has to be reformed so that interest rates come done due to competitive pressures, greater efficiency and lower implicit taxation of the banking sector. Access of companies to debt markets also needs to be improved by deepening and widening these markets.

67. Despite several policy initiatives taken by the SEBI, the primary market remained subdued in 1997-98. Resource mobilisation through public issues from the primary market in 1997-98 is estimated to have slowed down to one-third of the amount mobilised in 1996-97. The depressed situation prevailing in the capital markets may be at least partially responsible for low investment. Corporations found it difficult

to mobilise resources for industrial investment. It is necessary to address this issue and make the capital market a stronger instrument for mobilising funds. Confidence seems to be returning gradually to the market in 1998-99. Further measures are needed to bring back small investors to the capital market by raising the transparency and accountability of listed companies as well as that of capital market intermediaries. Efforts must also continue to modernise and improve our regulatory and payments systems to get them on par with developed countries.

68. As world inflation rates are currently of the order of 0 to 3 per cent, 4 to 6 per cent inflation rate could be regarded as an acceptable level for India at present. In 1997-98 the annual rate of increase in prices was confined to this range. Inflationary pressures tend to build up either on account of supply side shortfalls in primary products, which later get reflected in the manufacturing sector or due to pressures on the demand side. Where as the former is dealt with through timely and judicious supply management policies often involving government market intervention through liberal trade policy, the latter is dealt with through appropriate macro-economic policies involving control of money supply and fiscal deficit. The year 1998-99 may require special efforts at supply management in order to offset the possible shortfall in food-grains, sugar and cotton production.

69. Barring 1996-97, when food-grains output peaked at 199.3 million tonnes, the growth in food-grains output during nineties has been just about 1.73 per cent per annum. The yield rates appear to have reached a plateau in major wheat and rice growing areas. Hence attention would have to shift to those regions where productivity is well below the national average. Eastern U.P., Bihar and Orissa could be target areas where higher investment in rural infrastructure by way of improved water conservation and delivery system, fertiliser use and credit availability should receive special focus.

70. The pace of industrial growth and investment has slackened markedly since the middle of 1996-97 for a variety of reasons. Some of the factors are cyclical and can be expected to correct themselves. Others are the result of some of the policies followed in the past. On the policy side, therefore, measures should embrace a broad array and include: steps to boost export growth, to revive the primary capital market, to encourage higher private and public investment to relieve infrastructure bottlenecks and boost demand for core industrial sectors, and fiscal and monetary policies aimed at moderating real rates of interest and ensuring adequate availability of productive capital to industry. The climate for industrial investment and growth can also be greatly enhanced through bold economic policy initiatives. Economic reforms play a vital role not only by directly stimulating higher productivity and efficiency, but also by keeping confidence high and boosting investment intentions of entrepreneurs. Reform of inappropriate policies, unproductive government programmes and inefficient public organisations and projects can generate hope and confidence in a more productive future.

71. Almost twenty years ago a High Level Government Committee made wide ranging recommendations for replacement of controls and licenses by fiscal and other indirect policy instruments. While there has been substantial progress with delicencing industry and foreign trade, the “controls mind-set” remains influential and the “inspector raj” continues to flourish. Fresh initiatives are necessary to reduce the role of these factors in industry, agriculture, trade, infrastructure, finance and social services in order to unleash the productive energies and capacities of economic agents in all these areas. At the same time, new emphasis must be accorded to improve rating and certification systems, self-regulatory organisations and (in areas of natural monopoly such as some infrastructure services) independent regulatory authorities.

72. With the revival of economic growth, the demand for key infrastructure services such as power, telecom, railways, roads and ports, will press harder against existing supply constraints. The strategy to relieve infrastructure bottlenecks must encompass both the creation of additional capacity in various sectors as well as initiatives to induce much better capacity utilisation. The strategy must also encourage both private and public provision of infrastructure services in a competitive environment and with an appropriate and transparent regulatory framework. This broad approach calls for an acceleration of sector-specific reforms to tackle existing lacunae in the design and implementation of policies.

73. To illustrate, low capacity utilisation and high

transmission and distribution losses, unrealistic tariff policies and non-commercial approaches of SEBs constrain both the levels of generation and distribution from the existing power network as well as the flow of fresh investment into this sector. The railways and postal services continue to suffer from substantial operational losses in their provision of subsidised service. In the case of railways, the heavy cross-subsidy of passenger traffic by freight traffic has led to a situation where India's comparative advantage in key sectors such as coal and steel has been severely eroded. Indian ports suffer from problems of outdated organisational modes and low productivity of labour and equipment in comparison to many other Asian ports. The level of investment in new roads and the quality of maintenance of existing networks is far below requirement. All these issues and problems need to be tackled urgently.

74. As we approach the beginning of the twenty first century, the shortcomings in our social sectors — such as education, health, water supply and sanitation, housing — in relation to both our own aspirations as well as performance levels achieved by other Asian countries becomes increasingly stark and unacceptable. The constitutional provision of making primary education free and compulsory up to fifth standard should be implemented as soon as feasible. The provision of free education for girls will not only empower women but also help in controlling population growth and improving the quality of life of our children. The achievement of health for all requires greater focus on epidemic diseases and better water supply, sewage and sanitation systems. In the social sectors, Central and State Governments must clearly play a leading role in ensuring universal provision of basic minimum services. However, policies should be designed to encourage private provision of services as well. It is noteworthy that Kerala's oft-commended achievements in the fields of education and literacy are substantially dependent on a long history of private schools at all levels.

75. The ongoing economic reform process should be re-appraised and revitalised to give the entire national development effort a more humane face. The eradication of poverty and unemployment must be the abiding goal of our development policies and programmes. The achievement of this goal will require sustained and rapid economic growth combined with well functioning public programmes for social services, rural development and employment generation to provide an effective safety net for all those millions at the margins of the growth process.

Postscript : Following the testing of nuclear devices by India in the second week of May 1998, some industrialised countries have reacted negatively in the field of economic relations. As of mid-May (when this document goes for printing), it is too early to assess the implications of these reactions for the short and medium-term development prospects of the Indian economy. One thing however is clear : to the extent to which these reactions render the external economic environment less friendly, to that extent, it becomes more urgent to implement the policy decisions necessary to ensure macroeconomic stability and rapid and sustainable economic growth.