

## **MACROECONOMIC FRAMEWORK STATEMENT**

### **OVERVIEW OF THE ECONOMY**

1. The economy has made significant strides over the last two decades with annual average growth rising from a low level of 2.9 per cent in the seventies to 5.8 per cent in the nineties. The improvement in growth has also been accompanied by structural change as, between the seventies and 2003-04, the share of agriculture and allied sectors in Gross Domestic Product (GDP) has declined from an average of 42.8 per cent to 22.1 per cent, the share of services has improved from an average of 34.5 per cent to 51.0 per cent, while the share of industry has improved marginally from an average of 22.8 per cent to 26.9 per cent. Inflation has remained in single digits in recent years in contrast to the double-digit inflation in the early seventies and the early nineties. Food-grain production increased from 108.4 million tonnes in 1970-71 to 210.8 million tonnes in 2003-04. The external sector witnessed a transformation with foreign exchange reserves touching US\$113 billion at the end of 2003-04 from less than US\$1 billion on July 12, 1991. The response of the economy to the East Asian crisis in 1997 and the drought in 2002, one of the severest in recent years, demonstrated its resilience.

### **ECONOMIC GROWTH**

2. The year 2003-04 began in the backdrop of a drought-induced deceleration in GDP growth to 4.0 per cent in 2002-03, mainly because of a sharp decline of 5.2 per cent in the agriculture and allied sector. The improvement in industrial sector growth from 3.4 per cent in 2001-02 to 6.4 per cent in 2002-03, and in services from 6.8 per cent to 7.1 per cent in the same period resulted in modest growth even in a year of severe drought.

3. Helped by an abundant monsoon, growth bounced back in 2003-04. Real GDP in 2003-04 is estimated to have grown by 8.2 per cent, supported by a growth of 9.1 in agriculture and allied sectors, 6.7 per cent in industry sector and 8.7 per cent in the services sector. A growth rate higher than 8 per cent was achieved in the past in only three years - 1967-68 (8.1 per cent), 1975-76 (9.0 per cent) and 1988-89 (10.5 per cent). Revival of industrial growth witnessed in 2002-03 continued in 2003-04 aided by significant improvements in the performance of manufacturing, and electricity, gas and water supply.

### **EXTERNAL SECTOR**

4. Foreign exchange reserves have been rising steadily in recent years. Significant changes observed in the pattern of reserve inflows between 2003-04 and 2002-03 are: (a) an increase in the current account surplus to US\$8.7 billion from US\$4.1 billion; (b) a significant rise in the net capital inflows to US\$22.7 billion from US\$12.8 billion; (c) increases in portfolio investment, non-resident deposits and short-term credit in the capital account; and (d) greater valuation changes, reflecting the appreciation of the euro, pound sterling and yen against the US dollar, to US\$5.4 billion from US\$4.4 billion.

5. Aided by a recovery in growth of world trade, exports in US dollar terms had witnessed a sharp increase to 20.3 per cent in 2002-03 from a decline of 1.6 per cent in 2001-02. In US dollar terms, exports grew by a further 17.1 per cent in 2003-04. Imports, after stagnating for two years, had grown by 19.4 per cent in 2002-03. The higher growth

was on account of enhanced volume as well as higher unit values. Reflecting the increase in international crude oil prices, Petroleum, oil and lubricants (POL) imports grew by 26.0 per cent in 2002-03, while non-POL imports grew by 17.0 per cent. The increase in imports accelerated further to 22.8 per cent in 2003-04. Consequently, the trade gap widened to US\$16.7 billion in 2003-04 from US\$12.8 billion in the previous year. Nevertheless, with a surplus of US\$25.4 billion under invisibles, the current account registered a surplus (US\$8.7 billion), for the third successive year. The surplus in the capital account of the balance of payments increased from US\$12.8 billion in 2002-03 to US\$22.7 billion in 2003-04. The joint operation of current and capital account surpluses since 2001-02 has resulted in sizeable overall surplus as well as accumulation of foreign exchange reserves.

6. External debt at the end of 2003-04 is estimated at US\$112.6 billion as against US\$104.9 billion at the end of the previous year. Over the same period, the respective shares of concessional debt and short-term debt as a proportion of total outstanding debt declined marginally from 36.8 per cent and 4.4 per cent to 35.8 per cent and 4.2 per cent, respectively. Total outstanding debt, as a proportion of GDP, declined from 20.2 per cent to 17.8 per cent. Over the years, external financing of fiscal deficit has not only been declining, but it has been negative in recent years. External debt position is relatively comfortable.

#### **MONEY, BANKING AND CAPITAL MARKETS**

7. In line with higher than anticipated real growth, year-on-year, broad money (M3) grew by 16.4 per cent in 2003-04 after a growth of 14.7 per cent in 2002-03. Reserve money grew sharply by 18.3 per cent in 2003-04 as compared with 9.2 per cent in the previous year, contributed entirely by an increase of 35.2 per cent in the net foreign exchange assets of the Reserve Bank of India (RBI) in 2003-04 on top of a 35.7 per cent increase in 2002-03. The year-on-year growth in M3, as on June 11, 2004, was 15.3 per cent as compared to 11.9 per cent on the corresponding date last year. The year-on-year growth in reserve money as on June 18, 2004 was 12.2 per cent as compared to 10.8 per cent on the corresponding date last year.

8. During the year 2003-04, demand deposits with Scheduled Commercial Banks (SCBs) increased by 30.3 per cent compared to 11.3 per cent in the previous year. In 2003-04, growth in time deposits decelerated to 15.3 per cent from 16.9 per cent in the previous year, while the growth in aggregate deposits of SCBs accelerated to 17.3 per cent from 16.1 per cent in the previous year.

9. Aggregate credit (food and non-food) by SCBs grew by 14.6 per cent in 2003-04 compared to 16.1 per cent (net of mergers) in the previous year. After a decline of 8.3 per cent in 2002-03, mainly on account of higher off-take of foodgrains from the public distribution system and lower procurement, food credit declined by a further 27.3 per cent in 2003-04. Non-food credit grew by 17.6 per cent in 2003-04 as compared to 18.6 per cent (net of mergers) in the previous year. A sharp increase in the off-take of non-food credit was discernible from the third quarter of 2003-04.

10. The capital market has made rapid strides with the implementation of a state-of-the-art trading system and a sound clearing mechanism. New highs were recorded in trading volumes, prices and liquidity during 2003-04. The equity market capitalisation

grew from Rs.7.2 trillion in March 2003 to Rs.13.7 trillion in March 2004. The equity market capitalisation was about 49 per cent of GDP in 2003-04. There were 33 initial public issues and 19 rights issues in 2003-04 compared with 14 initial public issues and 12 rights issues in 2002-03. Amount raised through public and rights issues in 2003-04 was Rs.20,059 crore compared to Rs.4,070 crore in 2002-03.

#### **CENTRAL GOVERNMENT FINANCES**

11. After some improvement in the early nineties, the fiscal situation started worsening from 1997-98 with the pay revision of Government employees and the economic slowdown. Fiscal deficit of the Central Government after declining from 6.6 per cent of GDP in 1990-91 to 4.1 per cent of GDP in 1996-97 started rising from 1997-98 to reach 6.2 per cent of GDP in 2001-02. The deterioration in revenue deficit of the Central Government was sharper. The cumulative effect of high fiscal deficits has been an increase in the debt-GDP ratio. Outstanding liabilities of the Central Government, after declining from 55.3 per cent of GDP in 1990-91 to 51.2 per cent of GDP in 1998-99, started rising to reach 62.1 per cent of GDP in 2002-03.

12. The fiscal situation improved in 2003-04. The fiscal deficit in the Revised Estimates (RE) came down to Rs 1,32,103 crore (4.8 per cent of GDP) from the Budget Estimates (BE) of Rs.1,53,637 crore (5.6 per cent of GDP). The revenue deficit declined to Rs.98,308 crore (3.6 per cent of GDP) compared with the BE of Rs.1,12,229 crore (4.1 per cent of GDP). Revenue expenditure was lower than the BE mainly on account of savings under interest payments (Rs. 2,748 crore), defence (Rs.5,000 crore), and food subsidy (Rs. 2,600 crore), while additional expenditure of Rs. 4,080 crore was incurred on account of premium for the prepayment/buy back of high-cost public debt. Net tax revenue exceeded the BE by Rs.3,370 crore, mainly on account of higher collections from corporation tax (Rs. 11,487 crore) which more than neutralized the shortfalls in Union Excise Duties (Rs. 4,412 crore) and income tax ( Rs. 3,801 crore). Non-tax revenues also exceeded the BE by Rs.5,722 crore, mainly on account of higher-than-budgeted dividends from public sector enterprises.

#### **PROSPECTS**

13. The RBI in its annual policy statement (May 18, 2004) has put the growth prospect in 2004-05 at 6.5 per cent with 3 per cent growth in agriculture, and industry and services maintaining their growth momentum. The RBI has indicated that growth could be higher at 7 per cent, if the acceleration noticed in the third quarter of 2003-04 is sustained. Other projections of GDP growth in 2004-05 vary from 6.0 to 7.4 per cent.

14. The pre-monsoon rainfall (March to May), has been estimated at 25 per cent above normal. The Indian Meteorological Department has forecast a normal and evenly distributed rainfall for 2004-05. This augurs well for agricultural production. The industry and service sectors are also expected to maintain their growth momentum observed in recent years. Industrial sector growth has gathered pace in recent years with growth accelerating from 3.4 per cent in 2001-02 to 6.4 per cent in 2002-03 and further to 6.7 per cent in 2003-04. There has also been a pick-up in growth of the services sector from 6.8 per cent in 2001-02 to 7.1 per cent in 2002-03 and further to 8.7 per cent in 2003-04. The revenue balance of the Central government is likely to show continued improvement

in 2004-05, aided amongst others by a moderation in the weighted average interest rate on its debt, buoyancy in taxes and expenditure management. The fiscal deficit is also likely to improve, but not by as much as the revenue deficit because of a deliberate attempt to speed up public investment in aid of the growth recovery.

15. Global recovery has strengthened and broadened in 2003-04. As per the World Economic Outlook brought out by the International Monetary Fund in April 2004, global GDP growth averaged nearly 6 per cent at an annualized rate in the second half of 2003, the highest since 1999. The prospects for Indian exports look bright in 2004-05. India has already emerged as a hub for exports of auto components. Exports of textiles may get a boost with the phasing out of the Agreement on Textiles and Clothing from January 1, 2005. The large foreign exchange reserves provide an opportunity towards deepening trade reforms. With global recovery, prospects for growth in output and trade have brightened. There are, however, downside risks in terms of high international oil prices, volatility in cross-currency rates, and a rally in world inflation; and these require a dynamic and calibrated response.

16. In a nutshell, we may characterize the present macroeconomic environment as a challenge and an opportunity. It is a challenge in terms of the uncertainties in the international capital and commodity markets and rising inflationary pressures. It is an opportunity for policies to enhance infrastructure facilities, both physical and social, pursue reforms with a human face, and effect rapid fiscal consolidation.

17. The Budget estimates for 2004-05, particularly gross tax revenues, is predicated upon the robust macroeconomic environment. The fiscal adjustment proposed in the budget, in terms of reductions in non-plan revenue expenditure growth, is anchored on a sustained benign interest rate regime and stability in prices. Budget 2004-05, through enhancements in public investment in infrastructure, physical and social, seeks to reinforce the dynamic growth momentum and macroeconomic stability.

**MACROECONOMIC FRAMEWORK STATEMENT  
(ECONOMIC PERFORMANCE AT A GLANCE)**

S.No	Item	Absolute value			Percentage change	
		April - May			April-May	
		2003-04	2003-04	2004-05	2003-04	2004
<b>Real Sector</b>						
1.	GDP at factor cost (Rs.thousand crore)					
	(a) at current prices	2523.9 (R)	-	-	12.2 (R)	-
	(b) at 1993-94 prices	1426.7 (R)	-	-	8.2 (R)	-
2.	Index of Industrial production (1)	188.8	174.0	190.3	6.9	9.4 *
3.	Wholesale price index (2) (point to point)	180.3	173.8	184.0	4.6	5.9 **
4.	Consumer price index (3)	504	493	504	3.5	2.2
5.	Money Supply (M3)(Rs. Thousand crore)	2000.3	1796.7	2070.8	16.4	15.3 \$
6.	Imports at current prices ***					
	(a) In Rs. Crore	346474	54840	65192	16.6	18.9
	(b) In US \$ million	75400	11613	14607	22.8	25.8
7.	Exports at current prices					
	(a) In Rs. Crore	283604	40933	48315	11.2	18
	(b) In US \$ million	61718	8668	10823	17.1	24.9
8.	Trade Balance(in US\$ million)	-13682	-2945	-3784	57.4	28.5
9.	Foreign currency assets					
	(a) In Rs. Crore	466215	366516	519847	36.5	41.8
	(b) In US \$ million	107448	77932	114102	49.5	46.4
10.	Current Account Balance (In US\$million)	3226 @	-	-	10.4 @@	-

	2002-03	RE		BE	
		2003-04	2004-05	2003-04	2004-05
				over	over
				2002-03	2003-04
(Rs crore)					
<b>Government Finances#</b>					
1.	231748	263027	309322	13.50	17.60
2.	159425	187539	233906	17.63	24.72
3.	72323	75488	75416	4.38	-0.10
4.	182414	211228	168507	15.80	-20.23
5.	34191	64625	27100	89.01	-58.07
6.	3151	14500	4000	360.17	-72.41
7.	145072	132103	137407	-8.94	4.02
8.	414162	474255	477829	14.51	0.75
9.	302708	352748	332239	16.53	-5.81
10.	268074	284801	293650	6.24	3.11
<i>Of which:</i>					
11.	117804	124555	129500	5.73	3.97
12.	34634	67947	38589	96.19	-43.21
13.	111455	121507	145590	9.02	19.82
14.	71554	78086	91843	9.13	17.62
15.	39901	43421	53747	8.82	23.78
16.	414162	474255	477829	14.51	0.75
17.	339628	362887	385493	6.85	6.23
18.	74535	111368	92336	49.42	-17.09
19.	107880	99860	76171	-7.43	-23.72
20.	145072	132103	137407	-8.94	4.02
21.	27268	7548	7907	-72.32	4.76

**Note :** The figures of Railways have been netted as in Budget.

\* Relates to April

\*\* As on June 19

\$ As on June 11

\*\*\* Imports on the basis of Customs data.

@ April-Dec.2003.

@ @ April-Dec.2003 over "-" 2002

# Controller General of Accounts

R - Revised estimates.

1. Base:1993-94=100

2. Base:1993-94, end of the year.

3. Base:1982, relates to the month of May.