MACRO-ECONOMIC FRAMEWORK STATEMENT

The year 2008-09 saw a moderation in the growth of the Indian economy as compared to the previous years. The steep increases in prices of international crude oil and commodity prices in the beginning of the year followed by the global recession stemming from the global financial crisis, in the latter part of the year, resulted in the fall in the growth rate of the Gross Domestic Product. The impact of the global crisis was felt through the channels of capital flows, financial markets and trade. This resulted in growth of real Gross Domestic Product (at factor cost) falling to 6.7 per cent in 2008-09 as against a growth rate averaging 9.4 per cent per annum over the period 2005-06 to 2007-08. However India has been more resilient to the global crisis when compared to many other economies. The various measures taken by the government to mitigate the impact of the global crisis on the domestic economy aided by a savings rate of nearly 37.7 per cent and capital formation rate of 39.1 per cent in 2007-08, is expected to revive the growth of the economy towards its recent growth trajectory. With economic revival assuming greater importance, there has been a temporary deviation from the FRBM targets due to the various counter cyclical fiscal measures taken by Government to address the economic slowdown.

I. Economic Growth:

The Central Statistical Organization (CSO) has released the Revised Estimates for the 2008-09. The real Gross Domestic Product at factor cost is estimated at Rs.33.39 lakh crore during 2008-09, indicative of a growth of 6.7 per cent in 2008-09 as compared to the growth of 9 per cent in 2007-08. The moderation in growth for 2008-09 is mainly attributed to steep slowdown in growth in industry to 3.9 per cent from 8.1 per cent in 2007-08. Within industry, the manufacturing, electricity, gas and water supply and construction activities declined sharply, while growth in mining and quarrying sector showed a marginal growth. Growth in agriculture, forestry and fisheries declined from 4.9 per cent in 2007-08 to 1.6 per cent in 2008-09. The growth slowdown in services sector was moderate. It was estimated at 9.7 per cent in 2008-09 as compared to 10.9 per cent in 2007-08. Component wise analysis of the services sector indicates that there was a decline in growth in “trade, hotels, transport and communication” from 12.4 per cent in 2007-08 to 9 per cent in 2008-09, while in the case of “financing, insurance, real estate and business services” the growth dipped from 11.7 per cent in 2007-08 to 7.8 per cent in 2008-09. The impact of decline in these services was cushioned by the significant increase in growth in “community, social and personal services” from 6.8 per cent in 2007-08 to 13.1 per cent in 2008-09. This increased growth is attributed to increase in government expenditure in line with the fiscal policy to mitigate the impact of the global recession on economy.

Analysis of growth from the demand side indicates that private consumption growth declined from 8.5 per cent in 2007-08 to 2.9 per cent in 2008-09, while growth in fixed capital formation declined from 12.9 per cent in 2007-08 to 8.2 per cent in 2008-09, attributed largely to the negative impact of the global recession on the domestic economy. The fall in growth in private consumption and capital formation was partially offset by an increase in growth of government consumption which increased from 7.4 per cent in 2007-08 to 20.2 per cent in 2008-09. This resulted in growth in real gross domestic product at market prices at 6.1 per cent in 2008-09 as compared to 9.1 per cent in 2007-08.

(a) Agricultural Production

As per Third Advance Estimates of agricultural production released by the Directorate of Economics & Statistics, the total foodgrains production in 2008-09 has been estimated at 229.85 million tonnes as compared to 230.78 million tonnes in 2007-08 (final estimates). Area sown during Kharif (2008-09) was 1014.81 lakh hectares which is 2.3 per cent lower than the area sown in the previous year. An area of 641.07 lakh hectares was sown during rabi (2008-09) as reported on 1-5-2009, which is 2.9 per cent higher than the area sown in the previous year. As per the India Meteorological Department’s long range forecast for 2009, South west monsoon season rainfall (June to September) for the country as a whole is likely to be near normal. Accordingly, other things remaining the same, agricultural growth in the ensuing year is expected to be normal.

(b) Industrial Production

The overall index of industrial production for the year 2008-09 (provisional) shows a sharp slowdown in the growth of the industrial sector to 2.4 per cent compared to 8.5 per cent during 2007-08. Manufacturing growth during 2008-09 was only 2.3 per cent as compared to 9.0 per cent in 2007-08. Mining grew at 2.3 per cent during 2008-09 as compared to 5.1 per cent during 2007-08. Electricity recorded a 2.8 per cent growth during 2008-09 as compared to 6.4 per cent during 2007-08. For 2008-09 as a whole, the growth in the index of 6 core industries was 2.7 per cent compared to 5.9 per cent in 2007-08. The growth rate of Coal and Cement was 8.1 per cent and 7.5 per cent respectively. Finished carbon steel grew at only 0.4 per cent during the year and petroleum products at 3.0 per cent; both lower than their growth in 2007-08. Crude oil production declined by 1.8 per cent during 2008-09.

(c) Inflation

Inflation, measured by variations in the wholesale price index (WPI) on a year-on-year basis, eased sharply from its intra-year peak of 12.9 per cent on August 2, 2008 to 0.8 per cent by March 28, 2009. Average annual inflation is assessed at 8.4 per cent in 2008-09 versus 4.7 per cent in 2007-08. The current financial year (2009-10) started with an inflation rate of 0.8 per cent as on 1st week of April 2009 and remained below 1 per cent till end May 2009. For the week ended 20th June, 2009, the year-on-year inflation was (-) 1.3 per cent as against 11.91 per cent last year during the corresponding week. Inflation based on the consumer price index (CPI) for industrial workers showed an increase to 8 per cent on a year-on-year basis in March 2009 from 7.9 per cent a year ago.

II. External Sector

For the year 2008-09, an export target of US$ 200 billion was set initially which was later revised to US$ 175 billion. In 2008-09, the value of merchandise exports reached US$ 168.7 billion with a growth of 3.6 per cent despite global recession, thus achieving 96.4 per cent of the revised export target. While export growth was robust till August 2008, it became low in September and became negative from October 2008 to March 2009 due to the global recession. The negative trend continued in April 2009 with export growth at (-) 33.2 per cent. The main drivers of exports growth during 2008-09 (April-February) are engineering goods and chemicals and related products. Petroleum and textiles exports witnessed a positive but low growth, while handicrafts, primary products and gems and jewellery exports registered negative growth. During 2008-09 import growth was subdued at 14.4 per cent with growth in both POL and non-POL imports moderating to 16.9 per cent and 13.2 per cent respectively. Gold and silver imports registered negative growth of (-) 7 per cent and non-POL non-bullion imports grew by 15 per cent. This was due to the global recession resulting in lower fuel prices with the Brent price rising by only 1.9 per cent, and the price of the Indian crude import basket rising by 4 per cent; slow down in industrial activity and lower demand for exports resulting in lower demand for imports needed for exports and industrial activity. Import growth started declining from October 2008, with a one month lag from export growth and even turned negative from January to March 2009. The negative trend continued in April 2009 with import growth at (-) 36.6 per cent. While oil import growth was lower at 58.5 per cent, non-oil import growth was lower at 24.6 per cent over April 2008. Trade deficit increased from US$ 88.5 billion (as per customs data) in 2007-08 to US$ 119.1 billion in 2008-09.

(a) Services Export

The impact of global recession was relatively less on India’s services exports till December 2008 although the services export growth rate during April-December 2008-09, moderated to 16.3 per cent. A negative growth rate of (-) 8.2 per cent in insurance and sharp fall in growth rate to 6.2 per cent in travel services was registered during this period. Even transport services and miscellaneous services registered lower growth. Software services grew at 26 per cent, while financial services registered a robust growth of 45.7 per cent despite the global financial crisis and fall in growth rate in world financial services exports. Business services growth was however at a lower rate of 3.9 per cent.

In 2008-09 April-December, there was a sharp fall in the growth rate of business services imports (as in the case of business services exports) mainly due to the fall in imports of architectural, engineering and other technical services and relatively low growth in imports of business and management consultancy services. Import growth of travel services fell sharply to 5.9 per cent, while transportation import growth registered good growth though it moderated to 26.5 per cent.

(b) Balance of Payment (BoP) and Trade Deficit

The global financial crisis, which had set in around August 2007, impacted the emerging economies including India through the slowdown in capital flows. The impact became pronounced particularly from September 2008 with the heightened uncertainties in international financial markets triggered by the collapse of the Lehman Brothers. The turbulence in international financial markets and the slowdown in real economic activity in advanced countries of the world manifested in reversal of capital flows to emerging economies and decline in demand for exports from these economies. India's external sector was also affected through the trade and financial channels and the impact was clearly visible during the second half of the financial year. Notwithstanding the impact of global developments in terms of reversal of portfolio investment by foreign institutional investors (FIIs) and deceleration in export growth during the year 2008-09, the external sector of the country exhibited resilience as the FDI flows remained higher during April-December 2008 and the higher invisibles receipts by way of remittances and software exports counterbalanced the impact of higher trade deficit. The decline in oil prices from September 2008 also contributed to lower oil import growth rates during 2008-09. The comfortable foreign exchange reserves position also helped to mitigate the impact of adverse external sector developments on liquidity in domestic foreign exchange markets, and the consequent movements in exchange rate of the Indian rupee.

During April-December 2008, trade deficit widened to US$ 105.3 billion (12 per cent of GDP) from US$ 69.3 billion (8.2 per cent of GDP) during the corresponding period last year. Invisibles (net) during April-December 2008 were higher by 28 per cent at US$ 68.9 billion (7.8 per cent of GDP) as against US$ 53.8 billion (6.4 per cent of GDP) during the corresponding period of 2007-08. The current account deficit was significantly higher at US$ 36.5 billion (4.1 per cent of GDP) during April-December 2008 compared to US$ 15.5 billion (1.8 per cent of GDP) during April-December 2007.

In the capital account of BoP, net capital flows amounted to US$ 15.3 billion during April-December 2008 as compared with US$ 82.0 billion during April-December 2007. While the net inward FDI into India at US$27.4 billion during April-December 2008 remained higher than its previous year's level of US$ 20.0 billion, the portfolio investment (net) recorded a net outflow of US$ 11.3 billion during the same period (net inflow of US$ 33.3 billion during April-December 2007). In fact, net outflow in respect of investment by FIIs was even higher at US$ 12.4 billion during April-December 2008 as compared with a net inflow of US$ 24.5 billion during April-December 2007. NRI deposits (net) also showed a turnaround, reflecting the impact of upwards revisions in interest rates on non-resident Indian deposits. External commercial borrowings and short-term trade credit (net) flows mirrored the impact of global financial crisis on international capital markets, the consequent liquidity constraints and the reduced availability of finance to the private sector. During October-December 2008, the capital account balance was negative at –US$ 3.7 billion as compared with US$ 31.0 billion surplus in the capital account during October-December 2007.

The external sector developments in the financial year 2009-10 so far indicate an improvement in terms of capital flows from FIIs which reflects revival of market sentiment and increased investor confidence in the Indian economy. As per Securities & Exchange Board of India (SEBI) data, FIIs have invested US$ 5.4 billion in equity and debt instruments taken together during April-May 2009. Foreign exchange reserves have also increased from end-March 2009 level of US$ 252.0 billion to US$ 262.3 billion as on May 29, 2009.

India's foreign exchange reserves comprising Foreign Currency Assets (FCA), Gold, Special Drawing Rights (SDRs) and Reserve Tranche Position (RTP) reached its peak at US$ 314.6 billion at end-May 2008. The reserves declined thereafter to US$ 247.7 billion at the end of November 2008 and were at US$ 252.0 billion at the end of March 2009. However, in the current fiscal 2009-10, it has increased to US$ 262.3 billion as on May 29, 2009.

Foreign currency assets declined by US$ 57.8 billion from US$ 299.2 billion on 31.3.2008 to US$ 241.4 billion on 31.3.2009; a large part of the decline was on account of valuation change, reflecting the impact of strengthening of the US dollar vis-à-vis other international currencies. The foreign currency assets of the country have, however, increased to US$ 251.5 billion as on May 29, 2009.

The fiscal 2008-09 was witness to sharp decline in rupee exchange rate and currency volatility. The exchange rate of rupee per US dollar which was at Rs.39.99 per US dollar at end March 2008 exhibited both way movements during April-August 2008 but depreciated from September 2008 to Rs.52.09 per US dollar on March 5, 2009. However, it recovered to Rs.50.95 per US dollar at end March 2009. The rupee per US dollar exchange rate depreciated by 21.5 per cent during 2008-09 over its level on March 31, 2008. In the current year 2009-10, however, rupee exchange rate has appreciated by 7.8 per cent from Rs.50.95 per US dollar as on March 31, 2009 to Rs.47.27 per US dollar as on June 10, 2009.

III. Monetary Developments

The monetary policy stance in 2008-09, presented a contrast between the first and second half of the year, as it had to adapt itself to the emerging situation.

The first six months of the financial year 2008-09, witnessed a situation in which RBI addressed the need to control monetary expansion resulting from increased capital inflows; there were increases in the Cash Reserve Ratio (CRR) and the Repo Rate. While the CRR was increased from 7.75 per cent as of April 26, 2008 to 9.0 per cent with effect from August 30, 2008, the repo rate was also increased from 7.75 per cent as on April 1, 2008 to 9.0 per cent with effect from July 30, 2008. The reverse repo rate was, however, left unchanged at 6.0 per cent.

During the subsequent months, due to a decline in Foreign Institutional Investor (FII) inflows, capital inflows were reduced thereby reversing the uptrend. The months of September/October 2008 marked the contrasting situation. Co-terminus with the unfolding turbulence in the Global Financial Markets, the liquidity crunch in the Indian money market manifested. To address the situation, the RBI initiated various measures such as decreases in the CRR, Repo Rate, Reverse repo rate and the Statutory Liquidity Ratio (SLR). The CRR was lowered from 9.0 per cent as of August 30, 2008 to 5.0 per cent with effect from January 17, 2009. The repo rate was reduced in the wake of emerging liquidity crunch from 9.0 per cent in early October 2008 to 4.75 per cent with effect from April 21, 2009, while the reverse repo rate was also lowered from 6.0 per cent (as it was prevalent in November 2008) to 3.25 per cent with effect from April 21, 2009. The SLR was also cut by 100 basis points from 25 per cent of Net Demand & Time Liabilities (NDTL) to 24 per cent with effect from fortnight beginning November 8, 2008. This led to an improvement in the situation. The position changed to one of surplus liquidity with large amounts of money being parked in the Reverse Repo facility of RBI by the money market players towards the end of the year.

Having regard to the emerging trends, the growth in Reserve Money (M_0) for the full year 2008-09 was 6.4 per cent as against an increase of 31.0 per cent during 2007-08. Expansion of an important source of M_0, viz. the Net Foreign Exchange Assets (NFA) of RBI recorded a subdued growth of 3.6 per cent during 2008-09 compared to an expansion of 42.7 per cent in the preceding year. During the current financial year (April-May 22, 2009), M_0 has recorded a decline of 3.1 per cent as against a decline of 1.8 per cent in the corresponding period of the last year. Broad money (M_3) increased by 18.4 per cent during 2008-09 as against an increase of 21.2 per cent in 2007-08. During the current financial year 2009-10 so far (April – May 22, 2009) M_3 has recorded an increase of 3.6 per cent as against an increase of 1.8 per cent in the corresponding period of last year.

The continued boom in the economic activities, which, for the third year (2007-08) in succession had led to significant expansion of credit by the scheduled commercial banks (SCBs), moderated during 2008-09. Though bank credit to commercial sector witnessed strong growth in the first half of the year, it decelerated particularly in the second half of the year. While during 2007-08, bank credit expanded by 22.3 per cent, the increase was only 17.3 per cent during 2008-09. Food credit recorded an increase of 4.1 per cent during 2008-09 as against a decline of 4.6 per cent in 2007-08. Non food credit recorded an increase of 17.5 per cent in 2008-09, as against an increase of 23.0 per cent in 2007-08. During the current financial year so far (April – May 22, 2009), bank credit has recorded a decline of 1.4 per cent, while it had recorded no growth in the corresponding period of the last year. Non food credit recorded a decline of 1.9 per cent in April-May 22, 2009, as against a growth of 0.5 per cent in the corresponding period of 2008-09. Investment by Scheduled Commercial Banks (SCBs) in Statutory Liquidity Ratio (SLR) securities as per cent of their net demand and time liabilities (NDTL) continued to be higher than the stipulated level of 24 per cent. As compared to the level of 27.8 per cent at end March 2008, it increased to a level of 28.1 per cent at end March 2009. Non-SLR investment by SCBs during 2008-09 posted an increase of 9.0 per cent, compared to an increase of 14.3 per cent during 2007-08. Taking into account the need for monetary policy to respond to slackening economic growth witnessed lately, RBI's Annual Policy Statement for 2009-10 aims to minimise the impact of the global financial crisis on the domestic economy and facilitate restoration of the economy to a high growth path consistent with price and financial stability.

IV. Central Government Finances

Progress on the fiscal consolidation front has been satisfactory in the post-FRBM period till 2007-08. The Budget estimates for 2008-09 envisaged keeping fiscal deficits well below that set under FRBM Act, 2003. However, due to increase in global commodity (particularly crude petroleum) prices, additional commitments owing to conscious shift in expenditure in favour of health, education, the social sector and the fiscal stimulus to overcome the impact of global financial crisis on the real economy, it was felt that it might be difficult to adhere to the targets envisaged earlier. A fiscal stimulus in a year of stress on the macro-economy is in line with international best practices.

The gross tax-GDP ratio for the centre, which stagnated at around 8-10 per cent range in the pre-FRBM period, increased to 11.5 per cent in 2006-07 and further to 12.6 per cent of GDP in 2007-08. The Budget for 2008-09 estimated this at 13.0 per cent of GDP assuming a continuation of the trend. Union Government Accounts released by Controller General of Accounts (Provisional Actual) for 2008-09 placed the growth in gross tax receipts of the Centre at 2.8 per cent over the level in 2007-08. Revenue expenditure increased by 33.2 per cent during the same period (April-March 2008-09). The apparent decline in capital expenditure by 24.1 per cent during the period owes to the transaction relating to acquisition of equity of the State Bank of India during the previous year (2007-08), which provides for a higher base. In 2008-09 (Provisional Actual), the total expenditure was 117.4 per cent of Budget Estimates (BE). Non-debt receipts during the same period was 89.3 per cent of BE. The receipts were sufficient to cover only 62.5 per cent of the expenditure leaving a fiscal deficit of Rs.3,30,114 crore. This is much higher as compared to the fiscal deficit of Rs.1,26,912 crore in 2007-08. The revenue deficit for 2008-09 was Rs.2,47,046 crore. This is also much higher as compared to the figure of Rs.52,569 crore in 2007-08. Non-debt receipts during 2008-09 reduced by 0.03 per cent over 2007-08 after excluding acquisition of RBI stake in SBI. Growth in total expenditure in 2008-09 was 29.9 per cent, if the one time expenditure of Rs.34,308 crore on acquisition of RBI stake in SBI is adjusted. The reduction in taxes and enhanced expenditure as part of the fiscal stimulus also impacted on the fiscal position and contributed to the worsening of the fiscal situation in 2008-09 with fiscal deficit rising to a level of 6.2 per cent of GDP (Prov. Actuals). As per the present reckoning, the fiscal consolidation process could be resumed once the impact of global financial crisis is overcome, in the near term.

Annex - I

MACROECONOMIC FRAMEWORK STATEMENT
(ECONOMIC PERFORMANCE AT A GLANCE)

Sl.	Item	Absolute value		Percentage change	
		2007-08	2008-09	2007-08	2008-09
	Real Sector				
1	GDP at factor cost (Rs. thousand crore)				
	a) at current prices	4320.8 Q	4933.2 R	14.3 Q	14.2 R
	b) at 1999-2000 prices	3129.7 Q	3339.4 R	9.0 Q	6.7 R
2	Index of Industrial Production (1993-94=100)	268.0	274.3	8.5	2.4
3	Wholesale Price Index (1993-94=100)[a]	226.7	228.6	7.8	0.8
4	Consumer Price Index: Industrial Workers (2001=100)	137	148	7.9	8.0
5	Money Supply (M3)(Rs. thousand crore)	4017.6	4758.5	21.2	18.4
6	Imports at current prices [b]				
	a) In Rs. crore	1012312	1305503	20.4	29.0
	b) In US $ million	251439	287759	35.4	14.4
7	Exports at current prices				
	a) In Rs. crore	655864	766935	14.7	16.9
	b) In US $ million	162904	168704	28.9	3.6
8	Trade Deficit(in US$ million)	-88535	-119055	...	...
9	Foreign Currency Assets				
	a) In Rs. crore	1196023	1230066	43.0	2.8
	b) In US$ million	299230	241426	55.9	-19.3
10	Current Account Balance (In US$ million) (Apr- Dec)	-15508	-36469	...	...
	Government Finances [c]				
1	Revenue receipts	541864	544651	24.8	0.5
2	Tax revenue (Net)	439547	447726	25.2	1.9
3	Non-tax revenue	102317	96925	23	-5.3
4	Capital receipts (5+6+7)	170807	336818	14.6	97.2
5	Recovery of loans	5100	6158	-13.5	20.7
6	Other receipts	38795	546	7165	-98.6
7	Borrowings and other liabilities	126912	330114	-11	160.1
8	Total receipts (1 +4)	712671	881469	22.2	23.7
9	Non-Plan expenditure (10+12)	507589	606019	22.8	19.4
	Of which:				
10	Revenue Account	420861	556521	13.1	32.2
	Of which:				
11	Interest payments	171030	190485	13.8	11.4
12	Capital Account	86728	49498	109.8	-42.9
13	Plan expenditure (14 +15)	205082	275450	20.7	34.3
	Of which:				
14	Revenue Account	173572	235176	21.9	35.5
15	Capital Account	31510	40274	14.8	27.8
16	Total expenditure (9+13)	712671	881469	22.2	23.7
17	Revenue expenditure (10+14)	594433	791697	15.5	33.2
18	Capital expenditure (12+ 15)	118238	89772	71.9	-24.1
19	Revenue deficit (17-1)	52569	247046	-34.5	369.9
20	Fiscal deficit (l6-(1 +5+6))	126912	330114	-11	160.1
21	Primary deficit (20-11)	-44118	139629	473	-416.5

[Q] Quick Estimates; [R] Revised Estimates.

[a] as on end March (point to point)
[b] On Customs basis; comparison for current year is on provisional over revised basis.
[c] Figures as reported by Controller General of Accounts, Department of Expenditure, Ministry of Finance