The Economic Survey

Every year, in end-February, the Indian Government publishes the economic survey. It is the state-of-the-economy report and suggests the broad contours for the government's policy during the ensuing year. We reproduce excerpts from the latest survey which was released on February 25, 2005.

THE PERFORMANCE OF THE INDIAN ECONOMY in 2004-05 (April 2004 - March 2005) so far has exceeded expectations formed at the beginning of the year. Buoyed by a rebound in the agriculture and allied sector, and strongly helped by improved performance in industry and services, the economy had registered a growth rate of 8.5 per cent in 2003-04, the highest ever except in 1975-76 and 1988-89. Normally, strong growth is expected after anaemic growth, and vice versa. Following the 'bumper' growth in 2003-04, initial growth projections for 2004-05 were placed in the range of 6.2 per cent to 7.4 per cent. Modest expectations were further pared down to around 6.1 per cent when rainfall, after remaining normal in June, 2004, became deficient in the crucial sowing month of July and the shortfall in the south-west monsoon turned out to be 13 per cent. Deterioration in the benign world inflation environment, particularly of petroleum, coal and steel, led to further apprehensions about growth and inflation.

In the event, according to the advance estimate of the Central Statistical Organisation released on February 7, 2005, the economy is likely to grow by 6.9 per cent in 2004-05. Year-on-year wholesale price index-based inflation was 5 per cent on February 5, 2005. The economy has managed to maintain the growth momentum in spite of a deficient south-west monsoon, hardening international prices of oil and steel and, last but not the least, its first recorded experience of tsunami which caused extensive damage to life and property in Andaman & Nicobar islands, and 2,260 km of coastline in Tamil Nadu, Kerala, Andhra Pradesh and Pondicherry.

After a drought-induced decline of 7.0 per cent in 2002-03, the growth rate in the agriculture and allied sector bounced back to 9.6 per cent in 2003-04. While industry maintained the higher growth of 6.6 per cent observed in 2002-03, the services sector improved its performance significantly from 7.9 per cent in 2002-03 to 9.1 per cent in 2003-04. Growth in the industry and services sectors in 2003-04 was broad-based with manufacturing, public utilities, the trade, hotels, transport and communication group, and community, social and personal services recording higher growth than that in the previous year.

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THERE WAS A SUDDEN BOUT OF INFLATION in the first half of 2004-05, caused by a combination of factors, some exogenous, like the sharp rise in global petroleum prices, deficient rainfall-induced inflationary expectations and monetary overhang from accretion of foreign exchange reserves. The year 2004-05, after starting with a point-to-point, annual inflation rate of 4.5 per cent on April 3, 2004 witnessed a peak level of inflation at 8.7 per cent on August 28, 2004, the highest in the last four years. However, as a result of the quick monetary and fiscal measures taken by the Reserve Bank of India and Government, coupled with a slight easing of global petroleum prices, inflation has been on a declining trend and stood at 5 per cent on February 5, 2005 compared to 6.1 per cent a year ago.

The 52-week average inflation rate at 6.4 per cent on February 5, 2005 was, however, higher than the 5.5 per cent registered last year. In the current year up to February 5, 2005, both manufactured products and primary articles recorded lower year-on-year inflation rates at 4.5 per cent and 1.6 per cent, respectively, compared to 6.7 per cent and 3.4 per cent, respectively, last year. But there was acceleration in the inflation rate of the fuel, power, light and lubricant group from 7.6 per cent last year to 10.0 per cent this year due to a hardening of international prices of oil and minerals.

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THE RISING TREND IN INDIA'S foreign exchange reserves continued with such reserves (including gold, SDRs and reserve position in IMF) reaching an estimated level of $128.91 billion on February 4, 2005 in excess of India's total external debt of $114 billion at end-September, 2004. However, the accretion to reserves so far in this year at just over $15.9 billion is small compared to that of more than $31 billion during the corresponding period of the previous year, and an unprecedented $36.9 billion in the full year 2003-04.

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THE CAPITAL ACCOUNT SURPLUS in April-September 2004 was also down by around $1.5 billion from April-September 2003. Buoyant foreign investment inflows along with robust inflows of commercial borrowings sustained the capital account. The balance of payments surplus was around $7 billion in the first half of 2004-05, roughly half of what it was in April-September 2003.

In 2003-04, capital account surplus doubled to over $20 billion. There was a rise of 255 per cent in net foreign investment flows, mainly of the portfolio variety driven by the heavily bullish sentiments in the Indian stock markets. NRI deposits increased by $3.6 billion in 2003-04, compared to the previous year's increase of $3.0 billion. The capital account remained in surplus during the first half of the current year, but at a reduced level compared to April-September 2003, reflecting a sharp fall in portfolio and banking capital inflows. Portfolio flows declined by about $3 billion from the corresponding period of the previous year to $512 million. With a decline in the premium on their interest rates, NRI deposits—the dominant component of banking capital—declined by $1.2 billion in April-September 2004, compared to an increase of $2.2 billion in the corresponding period of the previous year. With a more liberalised regime and an improvement in the country's foreign currency ratings, there was a large increase of about $2 billion in external commercial borrowings in the first half of 2004-05 over the corresponding period of the previous year; but this increase was not sufficient to offset the decline in portfolio flows and banking capital.

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....**THERE ARE FIVE ISSUES** that need to be addressed to step up investment. First is the issue of investment in agriculture and allied activities, a sector that produces only 21 per cent of GDP, but supports nearly 57 per cent of the population. While there has been some diversification from foodgrains into areas such as fruits and vegetables, floriculture, dairy and poultry, much more needs to be done to encourage such diversification. There is a colossal loss of output due to inadequate storage and transport facilities and lack of sufficient food processing capacities. More public and private investment on these post-harvest facilities is required not only to increase value addition in agriculture but also to improve the link between agriculture and rural industrialisation...

Second is the issue of simplifying procedures and relaxing entry-exit barriers. The ease with which firms are able to enter into and exit from business activities is an important determinant of the investment climate. For business start ups, a large number of clearances have to be taken, both at the Central and State level. Such a system introduces delays and creates avenues for corruption... The recently constituted Investment Commission, with a mandate to interact with industry groups/houses and large companies abroad, secure investments, and also advise the Government on procedures and policies, should help. Similarly, the National Manufacturing Competitiveness Council will also help in focussing attention on the policies and procedures needed to tap the vast potential of manufacturing.

Third is the issue of finance. The incipient investment boom in infrastructure, industry (including housing), and services will yield best results only if the enormous resource flows are successfully intermediated at a low cost. It will depend on the ability of the financial sector to process information properly, and convert domestic and foreign savings into optimal investment by specific firms and sectors.

Fourth is infrastructure. Infrastructural inadequacy constrains economic growth, particularly in the backward States and in the agriculture sector. For example, fruits and vegetables will perish before reaching

> The National Electricity Policy announced recently envisages access to electricity for all households in the next five years.

SOME KEY INDICATORS OF THE INDIAN ECONOMY

	2001-02	2002-03	2003-04	2004-05	2001-02	2002-03	2003-04	2004-05
	Absolute values				percentage change over previous period			
Gross national product at factor cost (Rs.thousand crore)								
At current prices	2065.9	2241.7 P	2505.7 Q	2820.1 A	9.6	8.5 P	11.8 Q	12.5 A
At 1993-94 prices	1257.6	1310.5 P	1422.5 Q	1519.5 A	6.0	4.2 P	8.5 Q	6.8 A
Gross domestic product at factor cost (Rs. thousand crore)								
At current prices	2081.5	2254.9 P	2519.8 Q	2838.1 A	9.4	8.3 P	11.7 Q	12.6 A
At 1993-94 prices	1267.9	1318.4 P	1430.5 Q 1	529.4 A	5.8	4.0 P	8.5 Q	6.9 A
Agriculture and allied sectors (Rs. thousand crore) (at 1993-94 prices)	304.7	283.4 P	310.6 Q	313.9 A	6.3	-7.0 P	9.6 Q	1.1 A
Foodgrains production (million tonnes)	212.9	179.4	212.4 P	206.4 P	8.1	-15.7	18.4 P	-2.8 P
Index of industrial production(1)	167.0	176.6	189.0	199.4 ^	2.7	5.8	7.0	8.4 ^
Electricity generated (in billion kwh)	515.3	531.6	558.3	437.9 ^	3.1	3.2	5.0	6.5 ^
Wholesale price index(2)	161.8	172.3	180.3	188.6 #	1.6	6.5	4.6	5.0 #
Imports at current prices (in US $ million)	51,413	61,412	78,149	83,442***	1.7	19.4	27.3	34.7***
Exports at current prices (in US $ million)	43,827	52,719	63,843	60,754***	-1.6	20.3	21.1	25.6***
Foreign currency assets (3) (in US $ million)	510,49	71,890	1,07,448	123654 *	29.1	40.8	49.5	22.7 *

Note : Gross national product and Gross domestic product figures are at factor cost (new series base 1993-94).
Q-Quick estimates; A-Advance estimates; P-Provisional; @ Average exchange rate for April-January, 2004-05.
* At the end of January, 2005 *** April-January, 2004-05 # As on February 5, 2005. $ As on December, 2004. + 2nd Advance estimates 2004-05
^ April-December, 2004
1. Index of industrial production; (base 1993-94=100).
2. Index (with base 1993-94 = 100) at the end of fiscal year.
3. Outstanding at the end of financial year.

Editor's notes: ❖ currently $1 = Rs 45 approximately. ❖ A crore equals ten million. ❖ India's fiscal year is from April - March.

the household kitchen, if there are no good roads and no cold-chains. And cold-storages will not work if there is no reliable and adequate power supply... The decline in public spending in the infrastructure sector has not been adequately compensated by the private sector mainly due to difficulties in the regulatory environment. Therefore, there is a need to find an appropriate policy framework enabling public-private participation in the infrastructure sector.

Initiatives taken in a number of sectors like telecom, roads, ports and civil aviation have started yielding results. The National Electricity Policy announced recently envisages access to electricity for all house-holds in the next five years and fully meeting power demand by 2012. The structure and composition of the telecom sector has undergone a substantial change with mobile telephones accounting for 50 per cent of the total phones and the private sector accounting for 44 per cent of the total phones. Expansion of the broadband telecom sector will also impact economic growth considerably. In the area of roads, there is a need to shift the focus from construction to corridor management and road safety. Ports need to have an adequate policy framework to promote inter-port and intra-port competition. Provision of port connectivity through rail and road, and international benchmarking of performance parameters and prices, are very important factors in determining the growth of the port sector. In the civil aviation sector, there is an immediate need

On the Web
The complete Economic Survey is available on the Government of India's Press Information Bureau website pib.nic.in.

to improve regulation and competition in the airline industry, and to build better airports. Given the volatility observed in recent years in international petroleum, oil and lubricant prices and the import dependency of the country for crude petroleum, efforts need to continue to enhance energy security by augmenting the infrastructure of trans-border gas pipelines.

Fifth is the need for higher foreign investment, in the form of foreign direct investment and foreign institutional investment. Such investment triggers technology spillovers, assists human capital formation, contributes to international trade integration and particularly exports, helps create a more competitive business environment, enhances enterprise development, increases total factor productivity and, more generally, improves the efficiency of resource use. Progressive global integration of the Indian economy has resulted in successful assimilation of many domestic industries in global production chains. Automobiles, software and electronics are important examples. Entry of foreign investment has helped these industries in achieving technological upgradation and higher value addition.

While trade liberalisation, introduction of greater competition and liberal foreign investment policies have succeeded in transforming several segments of Indian manufacturing into globally competitive entities, there exists a strong case for revisiting the issue of caps in sectors such as coal mining, insurance, real estate and retail trade. Foreign direct investment in retail can not only organise a significant part of the largely unorganised domestic retailing, but can also invite established global retail brands into the Indian market, thereby creating greater outlets for sourcing and marketing Indian products. Organised retail formats will also help in upgrading the quality of products, establishing efficient supply chains from farm to market and generating greater employment.

The macroeconomic stability observed in recent years needs to be sustained. The benefits of such stability for investment, protecting the poor and furthering growth are well-known. Growth in the post-reform period has avoided the pitfalls of earlier decades, when the economy suffered from balance of payments problems. There is a need to build on the growing external strength of the economy, and foster improvements in institutions and infrastructure, which will accelerate the current export momentum.

Growth in India so far, from the demand side, has been mostly driven by private final consumption, with investment and exports playing a minor role, unlike in China and East Asia. The recent buoyancy of investment and exports needs to be enhanced to leverage growth in the Indian economy. Success in this regard will depend on how vigorously reforms are pursued to improve the investment climate and augment infrastructure.

> More investment on post-harvest facilities is required to improve the link between agriculture and rural industrialisation.