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 27, 2006

In a robust demonstration of its nascent strengths, the Indian economy, after growing at 8.5 per cent and 7.5 per cent in the two previous years, is projected to grow at 8.1 per cent in the current year 2005-06. Growth of Gross Domestic Product (GDP) at constant prices in excess of 8.0 per cent has been achieved by the economy in only five years of recorded history, and two out of these five are in the last three years. After dipping below 1.0 per cent in 2004-05, mostly on account of erratic rainfall, agricultural and allied sector's growth in 2005-06 is projected at 2.3 per cent. With a good kharif and bright rabi prospects, foodgrain production is expected to increase by 5 million tonnes (MT) in 2005-06. Some significant dimensions of the dynamic growth in recent years are: a new industrial resurgence; a pick up in investment; modest inflation in spite of spiraling global crude prices; rapid growth in exports and imports with a widening of the current account deficit; laying of some institutional foundations for faster development of physical infrastructure; progress in fiscal consolidation; and the launching of the National Rural Employment Guarantee (NREG) Scheme for inclusive growth and social security.

According to the national income data released by the Central Statistical Organisation (CSO) on February 7, 2006, the advance estimate (AE) for growth of GDP at factor cost at constant (1999-2000) prices in 2005-06 at 8.1 per cent was up 0.6 percentage points over the 7.5 per cent growth recorded in 2004-05. The CSO has changed the base year for calculation of national income aggregates at constant prices from 1993-94 to 1999-2000. The revised growth rate with base 1999-2000 is the same as or less than the rate with base 1993-94 for each of the four earlier years ending in 2003-04. For 2004-05, with the availability of detailed data at the sectoral level rather than some indicators that were available at the time when the advance estimate was made, growth of GDP at factor cost at 1999-2000 prices is 7.5 per cent (according to the quick estimate), up from the 6.9 per cent for GDP at factor cost estimated on February 7, and June 30, 2005.

Against the annual average growth rate of 8.0 per cent envisaged in the Tenth Five Year Plan (2002-03 to 2006-07), the aver-

DOUBLE DIGIT GROWTH RATE: IT services play a key role

age rate is estimated to have been 7.0 per cent in the first four years ending in 2005-06. Excluding the first year of the Plan (with a much lower growth of 3.8 per cent) results in an average growth rate of 8.0 per cent in the remaining three of the first four years. Maintenance of growth at or above 8 per cent in 2006-07 will yield a plan period annual average growth rate of at least 7.2 per cent.

The growth trend for the last three years appears to indicate the beginning of a new phase of cyclical upswing in the economy from 2003-04. The initial momentum to this new phase of expansion, in 2003-04, was provided by agriculture. After a somewhat subdued impetus from the farm sector in 2004-05, there is a moderate recovery in agricultural growth in 2005-06. This is partly because of a change in the rainfall pattern from erratic to a near-normal distribution.

In contrast to the sharp fluctuations in agriculture, industry and services have continued to expand steadily. Indeed, since the beginning of the Tenth Plan in 2002-03, with annual growth of 7.0 per cent or more, industry and services have acted as the twin engines propelling overall growth of the economy. Over a somewhat longer horizon, in the six years between 2000-01 and 2005-06 (AE), on average, services with a share of 52.0 per cent of GDP, contributed 65.0 per cent of GDP growth, and increased its share in GDP from 49.8 per cent to 54.1 per cent. During the same reference period, on average, with a share of 25.8 per cent of GDP, industry, by contributing 28.0 per cent of GDP growth, increased its share in GDP from 25.9 per cent to 26.2 per cent.

Overall industrial recovery that commenced from the second quarter of 2002-03 continues. After an acceleration of growth of industrial GDP at factor cost at constant 1999-2000 prices from 7.0 per cent in 2002-03 to 7.6 per cent and 8.6 per cent in the next two years, the industrial resurgence is manifest in the projected step up in its growth to 9.0 per cent in the current year. In the current year, industrial growth is driven by robust performances from manufacturing and construction sectors. Within industry, while manufacturing growth has accelerated steadily from 7.1 per cent in 2003-04 to 9.4 per cent in 2005-06, construction growth has been in double digits in each of the last

SOME KEY INDICATORS OF THE INDIAN ECONOMY

	2002-03	2003-04	2004-05	2005-06	2002-03	2003-04	2004-05	2005-06
	Absolute values				percentage change over previous period			
Gross national product at factor cost (Rs.thousand crore)								
At current prices	2238.9	2525.1 P	2826.0 Q	3178.8 A	7.8	12.8 P	11.9 Q	12.5 A
At 1999-2000 prices	2033.8	2208.2 P	2376.7 Q	2566.8 A	3.9	8.6 P	7.6 Q	8.0 A
Gross domestic product at factor cost (Rs. thousand crore)								
At current prices	2255.6	2543.4 P	2843.9 Q	3200.6 A	7.5	12.8 P	11.8 Q	12.5 A
At 1999-2000 prices	2052.6	2226.0 P	2393.7 Q	2586.6 A	3.8	8.5 P	7.5 Q	8.1 A
Agriculture and allied sectors (Rs. thousand crore) (at 1999-2000 prices)	448.7	493.7 P	497.4 Q	508.6 A	-6.9	10.0 P	0.7 Q	2.3 A
Foodgrains production (million tonnes)	174.8	213.5	204.6 +	209.3 + +	-17.9	22.1	-4.2 P	2.3+ +
Index of industrial production(2)	176.6	189.0	204.8	215.4 ^	5.8	7.0	8.4	7.8 ^
Electricity generated (in billion kwh)	531.6	558.3	587.4	458.6 ^	3.2	5.0	5.2	4.7 ^
Wholesale price index(3)	172.3	180.3	189.5	196.2 #	6.5	4.6	5.1	4.1 #
Imports at current prices (in US $ million)	61,412	78,149	1,09,173	1,08,803***	19.4	27.3	39.7	26.7***
Exports at current prices (in US $ million)	52,719	63,843	80,540	74,978***	20.3	21.1	26.2	18.9***
Foreign currency assets (7) (in US $ million)	71,890	1,07,448	1,35,571	1,33,770 *	40.8	49.5	26.2	8.2 *

Note : Gross national product and Gross domestic product figures are at factor cost (new series base 1999-2000).
Q-Quick estimates; A-Advance estimates; P-Provisional; @ Average exchange rate for April-January, 2005-06.
* At the end of January, 2006 *** April-January, 2005-06 # As on February 4, 2006. + 4th advance estimates 2004-05 + + 2nd Advance estimates 2005-06
^ April-December, 2005
1. Index of industrial production; (base 1993-94 = 100).
2. Index (with base 1982 = 100) at the end of fiscal year. 3. Index (with base 1993-94 = 100) at the end of fiscal year.
7. 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.

three years. Substantive commercial bank credit flows to the housing and real estate and retail sectors continue to provide support to the boom in construction and consumer durables. On the negative side, a deceleration in the growth of mining and quarrying, partly due to a fall in the levels of crude oil production as a result of a fire accident in July 2005 at Mumbai High North Platform, has had a dampening impact on overall industrial growth.

Services sector growth continued to be broad-based. Among the three sub-sectors of services, 'trade, hotels, transport and communication services' continued to lead by growing at double-digit rates for the third successive year. Impressive progress in expanding railway passenger network and production of commercial vehicles, and fast addition to existing stock of telephone connections, particularly mobiles, played key roles in such growth. Growth in financial services (comprising banking, insurance and real estate services), which after dipping in 2003-04 had bounced back in the following year, maintained the momentum with progressive maturing of Indian financial markets and the ongoing construction boom. However, community, social and personal services, which include public administration and defence, reflecting the process of fiscal consolidation and increasing efficiency of fiscal expenditure management, experienced a growth deceleration of more than a percentage point.

A pick-up in investment, reflecting the high business optimism, not only strengthened industrial performance but also reinforced the growth outlook itself. The rally in gross domestic capital formation (GDCF) that had commenced in 2002-03 continues. GDCF, as a proportion of GDP at cur-

POWER CONSTRAINT: The wind alternative

rent market prices, had declined from 26.0 per cent in 1999-2000 to 23.0 per cent in 2001-02 before the commencement of the industrial recovery in 2002-03. Climbing back to 25.3 per cent and 27.2 per cent in the two subsequent years, the ratio reached a high of 30.1 per cent in 2004-05.

Stock market index returns of 11 per cent in 2004 followed by 36 per cent in 2005 provide a good measure of investor sentiments. The bell-weather BSE Sensex crossed the 10,000 mark on February 6, 2006. In 2005, Rs30,325 crore ($6.7 billion) of resources were raised on the primary market for equity. The number of initial public offerings (IPOs) per year, on the rise since 2002, increased from 26 to 55 between 2004 and 2005. In line with the rally in investment, bank credit to the commercial sector increased by 22.8 per cent during 2004-05 and by a further 21.2 per cent between end-March 2005 and January 20, 2006.

Robust growth of the industrial sector and Government's conscious decision to increase credit to the agriculture sector led to rapid increases in bank credit. Non-food credit by Scheduled Commercial Banks (SCBs) expanded by Rs2,21,808 crore ($49.3 billion) in 2004-05, substantially up from the increase of Rs1,25,088 crore ($27.8 billion) in 2003-04. During the period (ending on January 20, 2006) of 2005-06, non-food credit expanded further by Rs2,66,857 crore ($59.3 billion), up 25.2 per cent from Rs1,68,188 crore ($37.4 billion) in the corresponding period of the previous year. Food credit by SCBs, after expanding by Rs5,159 crore ($1.1 billion) in 2004-05 compared to a decline of Rs13,517 crore ($3 billion) in the previous year, declined again by Rs2,778 crore ($617 million) during 2005-06 up to January 20, 2006 because of lower procurement and lower stocks of Food Corporation of India (FCI) after a lean agricultural year.

Bank credit disbursal during 2004-05 was well diversified across different sectors of the economy, with flows to housing and retail sector particularly strong and a substantial pick up in flows to agriculture. Strong industrial recovery was accompanied by much higher credit growth of 17.4 per cent to industry (medium and large) in 2004-05 compared to only 5.1 per cent in the previous year. During 2005-06, at end-October, 2005, the year-on-year growth (over end-October 2004) of credit to industry (medium and large) accelerated further by 45.7 per cent.

Inflation, in most parts of the world, showed a rising tendency on account of rising global crude oil prices. The sharp and spiraling increase in international oil prices from late 2003, combined with considerable week-to-week and even day-to-day volatility, posed considerable challenge in the maintenance of macroeconomic stability. Average headline world price of Indian basket of crude petroleum increased by 44.5 per cent, from US$37.3 per barrel in April-November 2004 to US$53.9 per barrel in April-November 2005, and was US$58.10 per barrel on February 13, 2005. Nevertheless, the virtuous expansion in the current phase of economic upturn has been maintained without an undue escalation of domestic prices. In India, inflation, measured by a point-to-point increase in the Wholesale Price Index (WPI) declined from 5.7 per cent on April 2, 2005, to a low of 3.3 per cent on August 27, 2005. Despite increasing thereafter, prices have remained at comfortable levels with the WPI-inflation at 4.1 per cent on February 4, 2006 vis-à-vis 5.0 per cent on February 5, 2005.

In a marked departure from the trend observed in recent years, the pace of accretion to foreign exchange reserves has slowed sharply during the current year so far. Following accretion of US$28.5 billion during 2004-05, in the current year until February 10, 2006, there was a reduction of US$1.1 billion from the end-March 2005 level of US$141.5 billion of foreign exchange reserves. Three key factors were instrumental behind this turnaround: an outgo of US$7.1 billion on IMD redemption; valuation losses from a weakened dollar vis-à-vis other major currencies; and a widening deficit in the current account of the balance of payments (BOP).

The embryonic deficit in the current account of the BOP, which emerged in 2004-05 after three consecutive years of surpluses, has assumed much larger dimensions during the current year. During April-September 2005-06, the current account deficit enlarged to around $13.0 billion, which was more than twice the deficit ($5.4 billion) in the whole of 2004-

MODERATE GROWTH: The grain basket

05. While net invisibles continued to rise, it was not enough to neutralize the rapidly expanding trade deficit, which at $31.6 billion during April-September 2005-06 was only around $5.0 billion less than that recorded in twelve months of 2004-05.

The sharp rise in current account deficit reflects the burgeoning trade deficit during the current year so far. Net invisibles increased, but was not enough to neutralize the expanding trade deficit. While the surge ahead in merchandise exports observed since 2002-03 continued, such growth was surpassed by an even faster rise in merchandise imports. Merchandise imports have been rising more rapidly than exports since 2003-04, reflecting perhaps the overall industrial recovery that commenced from the second quarter of 2002-03. Growth of GDP at factor cost at constant prices crossed 7.0 per cent in 2003-04 and has remained in excess of that rate ever since. The heavy demand for imports arising from increasing buoyancy and robustness of Indian industry may have led to a sustained rise in growth of merchandise imports.

India's merchandise exports (in US dollar terms and customs basis) have been recording annual growth rates of more than 20 per cent since 2002-03. In 2004-05, such exports grew by 26.2 per cent — the highest annual growth rate in the last three decades — to cross $80 billion. Five major sectors — gems & jewellery, engineering goods, petroleum products, ores & minerals, and chemicals and related products - were the key drivers. Despite recording a somewhat lower rate of growth of 18.9 per cent, exports during April-January 2005-06 have already reached $74.9 billion and are well on their way to achieve the $92 billion target set for 2005-06.

After growing by $10.8 billion to $27.8 billion in 2003-04, the increase in net invisibles, was limited to only $3.4 billion in 2004-05, primarily on account of a drop of $1.4 billion in private transfers. However, services exports - captured by net non-factor services, and including software and IT-enabled services - have continued to perform satisfactorily with unfailing regularity. Such exports (in US dollar terms), after growing by 71.3 per cent in 2004-05, increased further by 75.3 per cent in the first half of 2005-06. In addition to software and IT-enabled services, of late, business services, including professional services, have come to play a key role in enlarging services exports.

With robust inflows, during 2004-05, the surplus of $31.6 billion recorded in the capital account more than compensated the current account deficit and resulted in an addition of more than $26 billion, on BOP basis, to the existing stock of foreign exchange reserves. In April-September 2005, while the capital account surplus at $19.5 billion remained higher than the current account deficit of $13.0 billion, there was a slowdown in reserve accretion on BOP basis. The dominance of non-debt cre-

ating flows in the capital account continued. During April-September 2005, foreign investment flows at $7.4 billion were nearly $5.0 billion higher than such flows of $2.5 billion in the first half of 2004-05. Within foreign investment, portfolio flows, comprising mainly foreign institutional investor (FII) investment, were the dominant variety. At $4.2 billion during April-September 2005, FII flows (net) were higher than not only the FDI flows of $2.3 billion, but also the FII flows of $339 million in April-September 2004. FDI flows (net) during April-September 2005 were $2.3 billion - up by only $0.3 billion from such flows of $2.0 billion in the first half of 2004-05.

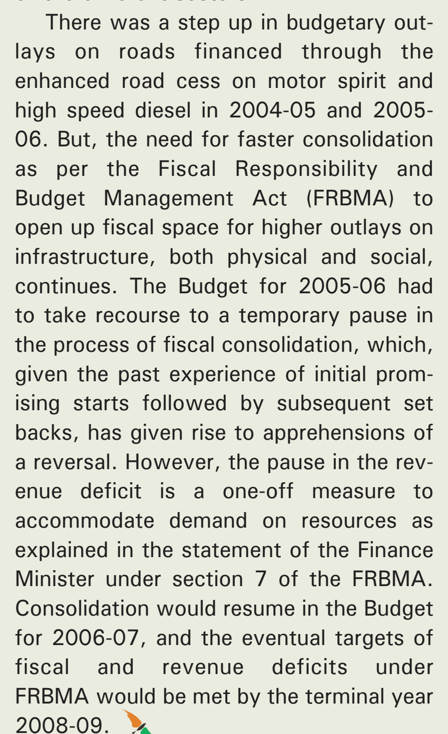
Infrastructural inadequacies continued to constrain the full potential for industrial resurgence, pick up in investment and buoyant exports. The growth of power generation in April-December 2005 at 4.7 per cent, for example, was lower than not only the annual target but also the 6.5 per cent achieved in the same period of the previous year. In the first three quarters of the current financial year, the overall index of six core industries - coal, electricity, crude petroleum, refinery throughput, steel, and cement — having a direct bearing on infrastructure, registered a growth of 4.5 per cent, which was lower than the 6.4 per cent registered during April-December, 2004. In the first half of 2005-06, crude oil production registered a decline, and there was deceleration in growth of coal, electricity and steel sectors. Growth of cement production, however, accelerated during this period.

While progress continued in attracting private investment into the infrastructure sectors of telecommunications, ports, and airports, there was a step up in budgetary outlays on roads financed through the enhanced road cess on motor spirit and high speed diesel. Nevertheless, overall investment in infrastructure continued to remain far below the requirement, and net capital stock, for example, in electricity, gas and water supply grew at a compound annual rate of 3.7 per cent between 1993-94 and 2003-04. The recently introduced public-private partnership (PPP) model had limited success in the area of electricity and mining, and the dominance of the public sector continued.

The total investment required in infrastructure is enormous. The Committee on Infrastructure, headed by the Prime Minister, has estimated the investment requirements as: Rs1,72,000 crore ($38.2 billion) in the National Highways sector by 2012; Rs40,000 crore ($8.9 billion) for Airports by 2010; and Rs50,000 crore ($11.1 billion) for Ports by 2012. A substantial share of this investment is expected to come from the private sector. India has an estimated potential to absorb $150 billion of FDI in the next five years in the infrastructure sector alone. It is important that the India Infrastructure Finance Company Limited (IIFCL), incorporated on January 5, 2006, not only becomes operational but starts lending funds, especially debt of longer term maturity, directly to the eligible projects to supplement other resources from banks and financial institutions from an early date.

Policies and institutions need to be geared up to meet the specific requirements of the infrastructure sectors in India. A well-defined regulatory architecture has to be in place, to increase the comfort level of the different players in the market. Issues of span of control, and conflicting domains need to be delineated and fleshed out. For example, an energy regulator, cutting across line ministries, needs to be in harness to tap the synergy of the different sectors.

There was a step up in budgetary outlays on roads financed through the enhanced road cess on motor spirit and high speed diesel in 2004-05 and 2005-06. But, the need for faster consolidation as per the Fiscal Responsibility and Budget Management Act (FRBMA) to open up fiscal space for higher outlays on infrastructure, both physical and social, continues. The Budget for 2005-06 had to take recourse to a temporary pause in the process of fiscal consolidation, which, given the past experience of initial promising starts followed by subsequent set backs, has given rise to apprehensions of a reversal. However, the pause in the revenue deficit is a one-off measure to accommodate demand on resources as explained in the statement of the Finance Minister under section 7 of the FRBMA. Consolidation would resume in the Budget for 2006-07, and the eventual targets of fiscal and revenue deficits under FRBMA would be met by the terminal year 2008-09.



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