State of the Economy and Prospects

CHAPTER 1

While India's recent slowdown is partly rooted in external causes, domestic causes are also important. The strong post-financial-crisis stimulus led to stronger growth in 2009-10 and 2010-11. However, the boost to consumption, coupled with supply-side constraints, led to higher inflation. Monetary policy was tightened, even as external headwinds to growth increased. The consequent slowdown, especially in 2012-13, has been across the board, with no sector of the economy unaffected. Falling savings without a commensurate fall in aggregate investment have led to a widening current account deficit (CAD). Wholesale price index (WPI) inflation has been coming down in recent months. However, food inflation, after a brief slowdown, continues to be higher than overall inflation. Given the higher weightage to food in consumer price indices (CPI), CPI inflation has remained close to double digits. Another consequence of the slowdown has been lower-than-targeted tax and non-tax revenues. With the subsidies bill, particularly that of petroleum products, increasing, the danger that fiscal targets would be breached substantially became very real in the current year. The situation warranted urgent steps to reduce government spending so as to contain inflation. Also required were steps to facilitate corporate and infrastructure investment so as to ease supply. Several measures announced in recent months are aimed at restoring the fiscal health of the government and shrinking the CAD as also improving the growth rate. With the global economy also likely to recover somewhat in 2013, these measures should help in improving the Indian economy's outlook for 2013-14.

Growth of GDP and Other Macro Aggregates

1.2 Following the slowdown induced by the global financial crisis in 2008-09, the Indian economy responded strongly to fiscal and monetary stimulus and achieved a growth rate of 8.6 per cent and 9.3 per cent respectively in 2009-10 and 2010-11 (Table 1.1). However, with the economy exhibiting inflationary tendencies, the Reserve Bank of India (RBI) started raising policy rates in March 2010. High rates as well as policy constraints adversely impacted investment, and in the subsequent two years viz. 2011-12 and 2012-13, the growth rate slowed to 6.2 per cent and 5.0 per cent respectively. Nevertheless, despite this slowdown, the compound annual growth rate (CAGR) for gross domestic product (GDP) at factor cost, over the decade ending 2012-13 is 7.9 per cent.

1.3 The moderation in growth is primarily attributable to weakness in industry (comprising the mining and quarrying, manufacturing, electricity, gas and water supply, and construction sectors),

0.1 KEY INDICATORS

Data categories and components	Units	2007-08	2008-09	2009-10	2010-11	2011-12	2012-13
1. GDP and Related Indicators							
GDP (current market prices)	₹ Crore	4987090	5630063	6477827	7795313[2R]	8974947[1R]	100,28,118[AE]
Growth Rate	%	16.1	12.9	15.1	20.3	15.1	11.7
GDP (factor cost 2004-05 prices)	₹ Crore	3896636	4158676	4516071	4937006[2R]	5243582[1R]	5503476[AE]
Growth Rate	%	9.3	6.7	8.6	9.3	6.2	5.0
Savings Rate	% of GDP	36.8	32.0	33.7	34.0	30.8	na
Capital Formation (rate)	% of GDP	38.1	34.3	36.5	36.8	35.0	na
Per Capita Net National Income (factor cost at current prices)	₹	35825	40775	46249	54151	61564	68747
2. Production							
Food grains	Million tonnes	230.8	234.5	218.1	244.5	259.3	250.1[a]
Index of Industrial Production [b] (growth)	%	15.5	2.5	5.3	8.2	2.9	0.7[c]
Electricity Generation (growth)	%	6.3	2.7	6.6	5.5	8.1	4.6[c]
3. Prices							
Inflation (WPI) (average)	%change	4.7	8.1	3.8	9.6	8.9	7.6[d]
Inflation CPI (IW) (average)	%change	6.2	9.1	12.4	10.4	8.4	10.0[d]
4. External Sector							
Export Growth (US$)	%change	29.0	13.6	-3.5	40.5	21.3	-4.9[d]
Import Growth (US$)	%change	35.5	20.7	-5.0	28.2	32.3	-0.0[d]
Current Account Balance (CAB)/GDP	%	-1.3	-2.3	-2.8	-2.8	-4.2	-4.6[e]
Foreign Exchange Reserves	US$ Bn.	309.7	252.0	279.1	304.8	294.4	295.5[f]
Average Exchange Rate	₹ /US$	40.26	45.99	47.44	45.56	47.92	54.47[g]
5. Money and Credit							
Broad Money (M3) (annual)	%change	21.4	19.3	16.8	16.0	15.6	11.2[h]
Scheduled Commercial Bank Credit (growth)	%change	22.3	17.5	16.9	21.5	15.9	15.1[h]
6. Fiscal Indicators (Centre)							
Gross Fiscal Deficit	% of GDP	2.5	6.0	6.5	4.8	5.7[i]	5.1[j]
Revenue Deficit	% of GDP	1.1	4.5	5.2	3.2	4.3[i]	3.5[j]
Primary Deficit	% of GDP	-0.9	2.6	3.2	1.8	2.6[i]	1.9[j]
7. Population	Million	1138	1154	1170	1210[k]	na	na

na: not available.

1R: 1st Revised Estimates, 2R: 2nd Revised Estimates, AE: Advance Estimates.

[a] Second advance estimates.

[b] The Index of Industrial Production has been revised since 2005-06 on base (2004-05=100).

[c] April-December 2012.

[d] 2012-13 (April-January).

[e] CAB to GDP ratio for 2012-13 is for the period April-September 2012.

[f] At end January, 2013.

[g] Average exchange rate for 2012-13 (April 2012- January 2013).

[h] Provisional (up to December 28, 2012).

[i] Fiscal indicators for 2011-12 are based on the provisional actuals (unaudited).

[j] Budget estimates.

[k] Census 2011.

Table 1.1 : Growth in GDP at Factor Cost at 2004-5 prices (per cent)

	2005-06	2006-07	2007-08	2008-09	2009-10[3R]	2010-11[2R]	2011-12[1R]	2012-13[AE]
Agriculture, forestry & fishing	5.1	4.2	5.8	0.1	0.8	7.9	3.6	1.8
Mining & quarrying	1.3	7.5	3.7	2.1	5.9	4.9	-0.6	0.4
Manufacturing	10.1	14.3	10.3	4.3	11.3	9.7	2.7	1.9
Electricity, gas, & water supply	7.1	9.3	8.3	4.6	6.2	5.2	6.5	4.9
Construction	12.8	10.3	10.8	5.3	6.7	10.2	5.6	5.9
Trade, hotels, & restaurants, transport & communication	12.0	11.6	10.9	7.5	10.4	12.3	7.0	5.2
Financing, insurance, real estate & business services	12.6	14.0	12.0	12.0	9.7	10.1	11.7	8.6
Community, social & personal services	7.1	2.8	6.9	12.5	11.7	4.3	6.0	6.8
GDP at factor cost	**9.5**	**9.6**	**9.3**	**6.7**	**8.6**	**9.3**	**6.2**	**5.0**

Source **: Central Statistics Office (CSO).**
Notes**: 1R : First Revised Estimate, 2R: Second Revised Estimate, 3R: Third Revised Estimate, AE : Advance Estimate.**

which registered a growth rate of only 3.5 per cent and 3.1 per cent in 2011-12 and 2012-13 respectively. The rate of growth of the manufacturing sector was even lower at 2.7 per cent and 1.9 per cent for these two years respectively. Growth in agriculture has also been weak in 2012-13, following lower-than-normal rainfall, especially in the initial phases (months of June and July) of the south-west monsoon.

1.4 After achieving double-digit growth continuously for five years and narrowly missing double digits in the sixth (between 2005-06 and 2010-11), the growth rate of the services sector also declined to 8.2 per cent in 2011-12 and 6.6 per cent in 2012-13. In 2011-12 the sector that particularly slowed within the services sector was Trade, Hotels, and Restaurants, Transport and Communications, and its growth further declined in 2012-13. Activities in this sector, being forms of derived demand, tend to grow at a slower rate with the slowdown of economic activity in the industry and agriculture sectors.

1.5 Why has the economy slowed down so rapidly despite recovering strongly from the global financial crisis? A number of factors are responsible. *First*, the boost to demand given by monetary and fiscal stimulus following the crisis was large. Final consumption grew at an average of over 8 per cent annually between 2009-10 and 2011-12. The result was strong inflation and a powerful monetary response that also slowed consumption demand. *Second*, starting in 2011-12, corporate and infrastructure investment started slowing both as a result of investment bottlenecks as well as the tighter monetary policy. *Thirdly*, even as the economy slowed, it was hit by two additional shocks: a slowing global economy, weighed down by the crisis in the Euro area and uncertainties about fiscal policy in the United States, and a weak monsoon, at least in its initial phase.

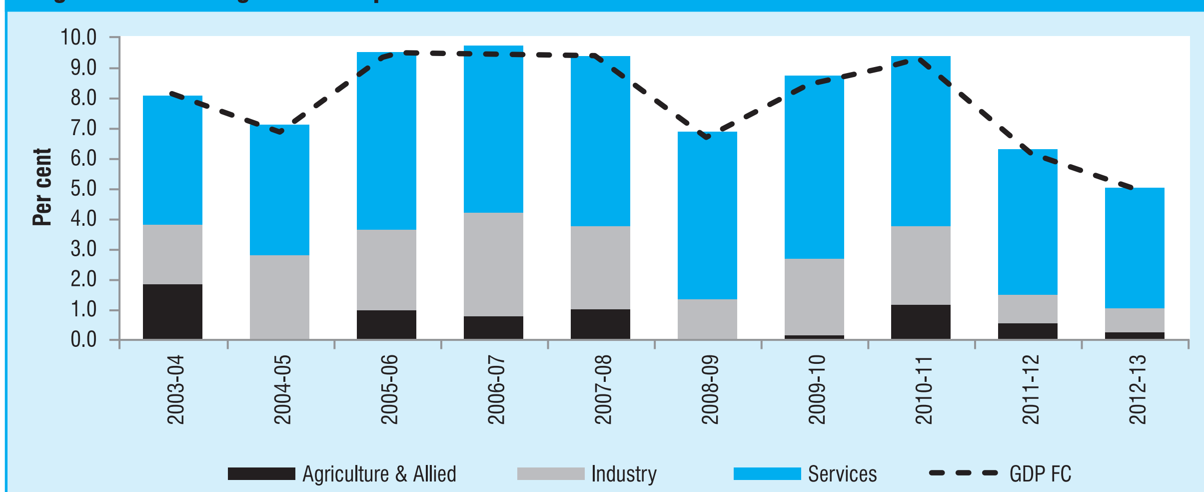
1.6 As growth slowed and government revenues did not keep pace with spending, the fiscal deficit threatened to breach the target. With government savings falling, and private savings also shrinking, the CAD--which is the investment that cannot be financed by domestic savings and has to be financed from abroad--also widened. In the rest of this chapter, the statistical underpinnings of the macroeconomy are analysed followed by the rationale behind the government's policy for macroeconomic stabilization and restoring growth, in addition to the macroeconomic outlook and possible risks to the outlook.

1.7 The Economic Survey does not just analyse the economy; it is also a detailed record of major developments in the economy. So the macroeconomic analysis will be followed by a summary tour of the other chapters in the Survey.

Aspects of Growth

1.8 In the last decade, growth has increasingly come from the services sector, whose contribution to overall growth of the economy has been 65 per cent, while that of the industry and agriculture sectors has been 27 per cent and 8 per cent respectively. Figure 1.1 shows the contributions of these sectors to the overall growth of the economy from 2003-04 to 2012-13.

Figure 1.1: GDP growth and point contribution of different sectors



Note : Data for 2012-13 is as per Advance Estimates released by CSO.

1.9 Figure 1.1 suggests that for achieving an annual growth rate of 9 per cent or higher, all the three major sectors of the economy have to perform well. Growth in agriculture, while small in overall contribution, does distinguish years of strong overall growth from years of more moderate growth. The two larger sectors are, of course, important to overall growth. In the high growth years of 2005-06 to 2007-08 as well as in 2009-10 and 2010-11, the rate of growth of both the industry and services sectors was over 9 per cent. Within the industry sector, the manufacturing sector in particular, outperformed most other sectors of the economy in these years. Its growth averaged 11.6 per cent between 2005-06 and 2007-08 and 10.5 per cent for the years 2009-10 and 2010-11. It is clear from the foregoing analysis that for growth to be strong, the contribution from the industry sector, and in particular from the manufacturing sector, has to increase in the years to come. This is also important from the point of view of absorbing surplus labour from the agriculture sector (see Chapter 2).

1.10 The general pattern over recent years has been that, in years of sharply higher growth, GDP growth at market prices exceeds GDP at factor cost and the reverse is true in years of slow growth (Figure 1.2).

1.11 GDP at factor cost is GDP at market prices less indirect taxes plus subsidies. Part of the reason for the differences in growth at factor costs and at market prices lies in the fact that the growth of indirect taxes tends to fall in a slowdown while the expenditure on subsidies often increases. This reduces the growth of net indirect taxes, which is the difference between the two items, in a slowdown. For example, the net indirect taxes to GDP ratio declined from an average of 8.1 per cent between 2003-04 and 2007-08 to an average of 5.7 per cent in 2008-09 and 2009-10, which is why GDP growth

Figure 1.2: A Comparison of growth rates of GDP at Factor Cost and GDP at Market Prices

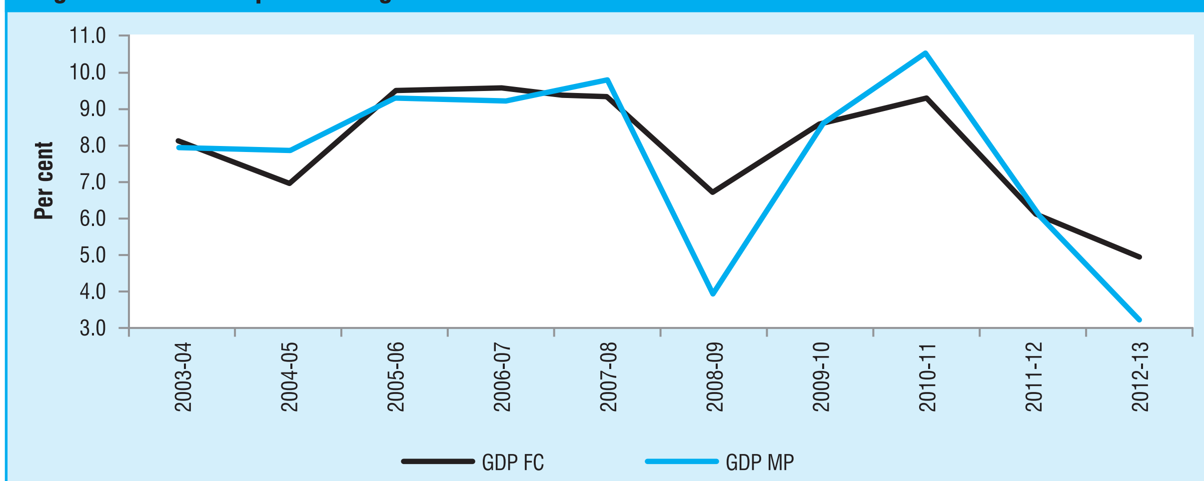


Table 1.2 : Growth in GDP at Constant Market Prices (per cent)

	2005-06	2006-07	2007-08	2008-09	2009-10	2010-11[2R]	2011-12[1R]	2012-13[AE]
1. Total final consumption expenditure	**8.7**	**7.7**	**9.4**	**7.7**	**8.4**	**8.1**	**8.1**	**4.1**
1.1 Private final consumption expenditure	8.6	8.5	9.4	7.2	7.4	8.6	8.0	4.1
1.2 Government final consumption expenditure	8.9	3.8	9.6	10.4	13.9	5.9	8.6	4.1
2. Gross capital formation	**16.2**	**13.4**	**18.1**	**-5.2**	**17.3**	**15.2**	**0.5**	**3.9**
2.1 Gross fixed capital formation	16.2	13.8	16.2	3.5	7.7	14.0	4.4	2.5
2.2 Changes in stocks	26.7	31.6	31.3	-51.4	67.7	29.7	-30.6	47.6
2.3 Valuables	-1.6	13.7	2.9	26.9	57.6	32.4	6.6	-18.1
3. Exports	**26.1**	**20.4**	**5.9**	**14.6**	**-4.7**	**19.7**	**15.3**	**5.1**
4. Less imports	**32.6**	**21.5**	**10.2**	**22.7**	**-2.1**	**15.8**	**21.5**	**5.7**
Growth in GDP at 2004-05 market prices	**9.3**	**9.3**	**9.8**	**3.9**	**8.5**	**10.5**	**6.3**	**3.3**

Source : CSO.
Notes: 1R: First Revised Estimate, 2R: Second Revised Estimate, AE: Advance Estimate. Totals may not tally due to adjustment for errors and omissions.

at factor cost was higher in 2008-09 than GDP growth at market prices.

1.12 As per the Advance Estimates released by the CSO, the rate of growth in terms of GDP at market prices (at 2004-05 prices) is expected to be 3.3 per cent for 2012-13 as against 6.3 per cent in 2011-12 (Table 1.2). The growth rate declined significantly on account of the reduction in investment rate and lower growth of exports vis-à-vis that of imports. The rate of growth of consumption expenditure and particularly that of private final consumption expenditure has generally been more stable than investment, except in 2012-13.

Quarterly Estimates of Growth of GDP

1.13 Table 1.3 gives the quarterly growth rates of GDP at factor cost (at constant 2004-05 prices) in major sectors of the economy for 2010-11, 2011-12, and the first two quarters of 2012-13. The slowdown was broad-based in 2011-12 and has become more so in the first half of 2012-13.

Table 1.3 : Quarterly Estimate of GDP Growth (year-on-year in per cent)

	2010-11				2011-12				2012-13	
Sector	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2
1. Agriculture, forestry & fishing	**3.1**	**4.9**	**11.0**	**7.5**	**3.7**	**3.1**	**2.8**	**1.7**	**2.9**	**1.2**
Industry	**8.3**	**5.7**	**7.6**	**7.0**	**5.6**	**3.7**	**2.5**	**1.9**	**3.6**	**2.8**
2. Mining & quarrying	6.9	7.3	6.1	0.6	-0.2	-5.4	-2.8	4.3	0.1	1.9
3. Manufacturing	9.1	6.1	7.8	7.3	7.3	2.9	0.6	-0.3	0.2	0.8
4. Electricity, gas & water supply	2.9	0.3	3.8	5.1	8.0	9.8	9.0	4.9	6.3	3.4
5. Construction	8.4	6.0	8.7	8.9	3.5	6.3	6.6	4.8	10.9	6.7
Services	**10.0**	**9.1**	**7.7**	**10.6**	**10.2**	**8.8**	**8.9**	**7.9**	**6.9**	**7.2**
6. Trade, hotels, transport & communication	12.6	10.6	9.7	11.6	13.8	9.5	10.0	7.0	4.0	5.5
7. Financing, insurance, real estate, business services	10.0	10.4	11.2	10.0	9.4	9.9	9.1	10.0	10.8	9.4
8. Community, social, & personal services	4.4	4.5	-0.8	9.5	3.2	6.1	6.4	7.1	7.9	7.5
9. GDP at factor cost (total 1 to 8)	**8.5**	**7.6**	**8.2**	**9.2**	**8.0**	**6.7**	**6.1**	**5.3**	**5.5**	**5.3**

Source : CSO.

1.14 Quarterly GDP growth rate in India declined in each of the successive quarters between the fourth quarter of 2010-11 and the fourth quarter of 2011-12. Growth in H1 of the current year works out to 5.4 per cent, while the CSO's Advance Estimate for growth for 2012-13 is 5.0 per cent. Let us now analyse some of the key elements of aggregate demand to see why the economy has slowed.

Private Final Consumption Expenditure

1.15 Private final consumption expenditure accounts for about three-fifths of GDP at market prices. An increase in people's disposable income tends to reduce the share of food in total consumption (the National Sample Survey Organization's [NSSO] Survey on Consumption Expenditure provides clear evidence of the downward trend in share of food in total consumption). Expectedly, therefore, the growth rate of expenditure on the food, beverages, and tobacco group is lower than that of total private final consumption expenditure, resulting in a reduction in its share from 40 per cent in 2004-05 to 31.2 per cent in 2011-12 (Table 1.4).

1.16 In the current year, private final consumption expenditure has slowed considerably, from 8 per cent in 2011-12 to 4.1 per cent in 2012-13 (Table 1.2). The rate of growth of production of a large number of consumer durables declined significantly, e.g. private vehicles from 23.2 per cent in April-November 2011 to - 5.6 per cent in April-November 2012. Similarly, the growth rate of production of consumer durables for mass consumption declined from 12.2 per cent in April-November 2011 to 3.3 per cent in April-November 2012.

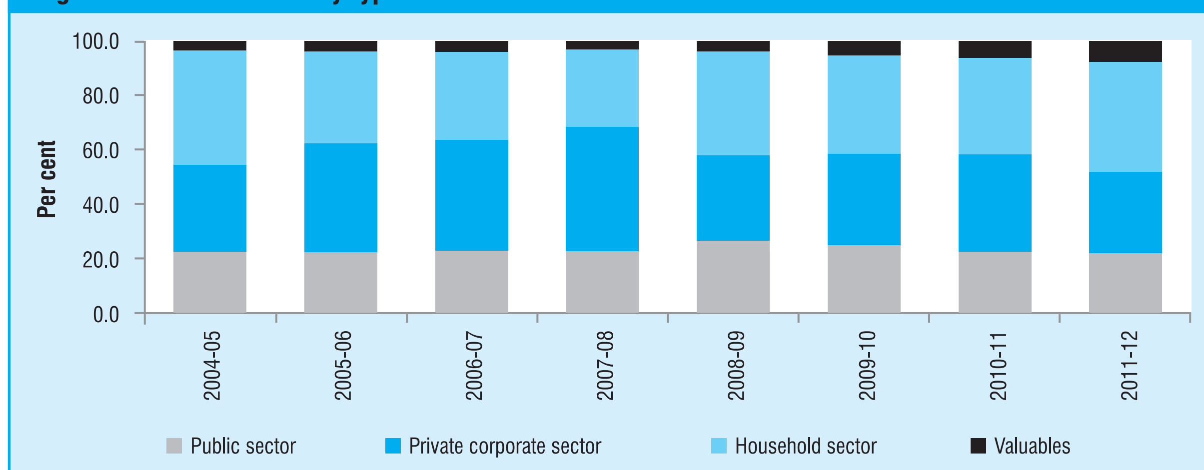
1.17 Part of the reason for the general slowdown in consumption could be that higher inflation tends to reduce real disposable incomes of households. Growth of durable goods consumption (under the assumption that growth of consumption for these items would not be significantly different from the growth in production) may have slowed even further recently, because high interest rates and resulting high monthly instalments restrained purchases. At the same time, the seasonally adjusted consumer non-durable index of industrial production (IIP), which is typically a smoother series than durable goods production, has been picking up since August 2012.

Table 1.4 : Private Final Consumption Expenditure : Annual Growth and Shares at 2004-05 prices

	2004-05	2006-07	2007-08	2008-09	2009-10	2010-11[1R]	2011-12[2R]
			Annual growth (per cent)				
Food, beverages, & tobacco		3.4	6.4	3.3	0.4	5.9	5.8
Clothing & footwear		23.3	5.0	5.0	14.9	20.2	-3.9
Gross Rent, fuel, & power		3.8	4.7	3.6	6.0	4.2	6.2
Furniture, furnishings, etc.		17.1	16.1	12.2	9.0	16.6	6.2
Medical care & health services		8.7	4.5	6.9	8.9	7.6	6.2
Transport & communication		9.1	7.9	7.7	12.1	10.0	9.8
Recreation, education, & cultural services		8.4	9.8	6.8	4.0	11.8	8.1
Miscellaneous goods & services		21.1	28.6	20.2	15.7	7.9	19.1
Total private consumption expenditure		8.7	9.2	7.1	7.5	8.7	7.9
			Share in total (per cent)				
Food, beverages, & tobacco	40.0	37.3	36.3	35.0	32.7	31.8	31.2
Clothing & footwear	6.6	8.3	8.0	7.8	8.4	9.3	8.2
Gross Rent, fuel, & power	13.8	12.6	12.1	11.7	11.5	11.1	10.9
Furniture, furnishings, etc.	3.4	3.9	4.1	4.3	4.4	4.7	4.6
Medical care & health services	5.0	5.0	4.8	4.8	4.8	4.8	4.7
Transport & communication	19.3	18.9	18.7	18.8	19.6	19.8	20.2
Recreation, education, & cultural services	3.0	3.0	3.0	3.0	2.9	3.0	3.0
Miscellaneous goods & services	8.9	11.0	13.0	14.6	15.7	15.6	17.2
Total private consumption expenditure	100.0	100.0	100.0	100.0	100.0	100.0	100.0

Source: **CSO.** ***Notes*****: 1R: First Revised Estimate, 2R: Second Revised Estimate.**

Figure 1.3: Investment by type of institutions



Investment

1.18 The growth rate of the economy since 2003-04 has been strongly correlated with investment rate. The investment rate averaged 34.5 per cent between 2003-04 and 2011-12, much higher rate than before. As can be seen from Tables 1.1 and 1.2, the real growth rate in the economy averaged 9.5 per cent per annum during 2005-06 to 2007-08, which were also the years when the growth rate of investment in real terms averaged around 16 per cent. Similarly, the average growth rate of the economy was close to 9 per cent per annum in 2009-10 and 2010-11, with the growth rate of investment averaging around 16.2 per cent in these two years. The rate of growth of GDP was lower in the years when growth rate of investment was low, as was the case in 2008-09 and 2011-12.

1.19 As can be seen from Table 1.5, the private sector is the major source of investment in the country. Within the private sector there are two categories of investors, viz. the private corporate sector and household sector. Figure 1.3 gives the share of these sectors, along with the investment of the public sector and valuables, in total investment.

1.20 Since 2004-05, the year when the overall investment rate in the economy first exceeded 30 per cent, the share of public investment in total investment (excluding valuables) has remained fairly stable at around 24 per cent for all the years, except in 2008-09 and 2009-10 when it was 27.6 per cent and 26.5 per cent respectively. The increase in these years could be attributed to the fiscal stimulus provided by the government in order to overcome the slowdown in the economy in 2008-09 following the global slowdown.

Table 1.5 : Ratio of Investment to GDP (at current market prices per cent)

		2004-05	2006-07	2007-08	2008-09	2009-10	2010-11 2R	2011-12 1R
1.	**Gross capital formation (investment)**	**32.8**	**35.7**	**38.1**	**34.3**	**36.5**	**36.8**	**35.0**
	Public sector	7.4	8.3	8.9	9.4	9.2	8.4	7.9
	Private sector	23.8	26.4	28.1	24.8	25.4	26.5	24.9
	Corporate sector	10.3	14.5	17.3	11.3	12.1	13.4	10.6
	Household sector	13.4	11.9	10.8	13.5	13.2	13.1	14.3
2.	**Gross fixed capital formation**	**28.7**	**31.3**	**32.9**	**32.3**	**31.7**	**31.7**	**30.6**
	Stocks	2.5	3.4	4.0	1.9	2.8	3.1	2.1
	Valuables	1.3	1.2	1.1	1.3	1.8	2.1	2.7
3.	**Gross domestic savings**	**32.4**	**34.6**	**36.8**	**32.0**	**33.7**	**34.0**	**30.8**
4.	**Saving-investment gap (3-1)**	**-0.4**	**-1.1**	**-1.3**	**-2.3**	**-2.8**	**-2.8**	**-4.2**

Source: **CSO.** ***Notes*** **: 1R: First Revised Estimate, 2R: Second Revised Estimate. Totals may not tally due to adjustment for errors and omissions.**

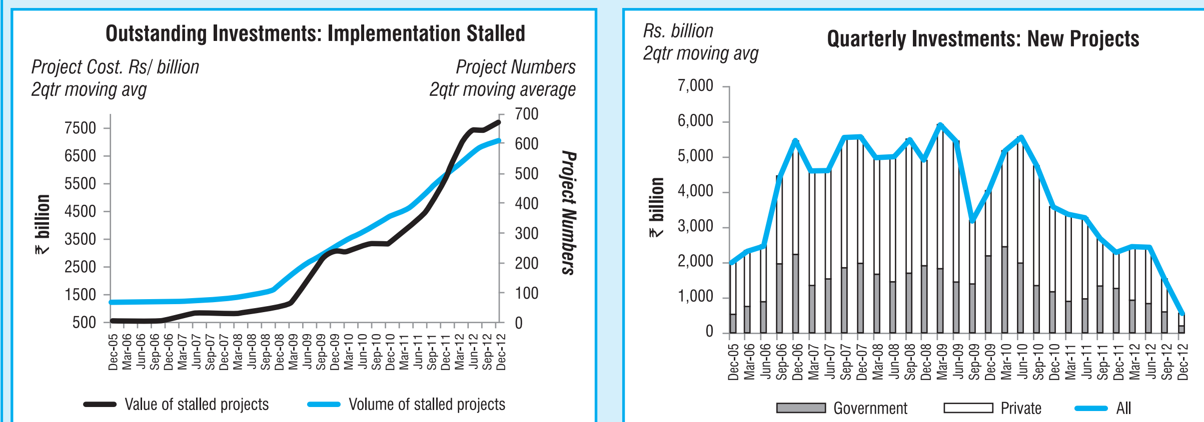
1.21 As per the First Revised Estimates released by the CSO in January 2013, gross domestic capital formation as a ratio of GDP at current market prices (investment rate) is estimated to be 35.0 per cent in 2011-12 as against 36.8 per cent in 2010-11. Both public and private investment declined as a share of GDP. Within private investment, investment by the private corporate sector registered a sharper decline.

1.22 The reduction in private investment could be attributed to a number of factors. First is the increase in policy rates (to combat inflation and inflationary expectations). Between March 2010 and October 2011, the RBI raised the repo rate by 375 basis points (bps), thus raising the cost of borrowings in a bid to reduce demand. Another reason for lower private investment could be lower demand for Indian exports

Box 1.1 : Recent Investment Trends: A Case of Rising Stalled Projects and Falling Project Starts

Two trends in investments stand out--rising stalled projects and falling project starts. To study these, we use data from the Capex database of the Centre for Monitoring Indian Economy (CMIE), which tracks investments at a project-specific level.

Rising Stalled Projects: There has been a surge in projects where implementation has stalled. Both in value and volume terms, stalled projects have been rising since early 2009. As of December 2012, six sectors accounted for about 80 per cent of all stalled projects--electricity, roads, telecommunication services, steel, real estate, and mining.



Source: CMIE CapEx.

Falling Project Starts: New investment projects have been drying up across sectors, partly as a consequence of rising stalled projects which reduce the ability of firms to start new ones. New projects of both private sector and government have been falling. Government projects peaked in March 2010 and private-sector projects peaked two quarters later. Ever since, private-sector investment levels have been lagging government investments by about six months.

Causes of slowdown: Several factors are believed to have caused the stalling of investments and drying up of new investment. A CMIE study[1] shows that in 2011-12, 20 projects accounted for almost 70 per cent of total cost of shelved projects. An analysis of these 20 individual projects suggests difficulties in land acquisition, coal linkages, and mining bans as major causes. Analysis of other stalled projects suggests that policy issues such as in telecom spectrum allocations have also played a role. Several sectors such as consumer non-durables, which are less subject to the type of permissions described above and are more driven by demand conditions and GDP growth, are also seeing a slowdown in new investments. For example, there is a slowdown in new investments in manufacturing food and agro-based products. Lack of growth and slowdown in investment are feeding into each other, with causation flowing both ways. High interest rates have contributed to the depressed investment climate as well. However, given the stability in the repo rate between April and December 2012, the latest quarterly data suggest that interest costs of companies have moderated slightly.

Way forward: The government has taken some steps to kick-start investments. The Cabinet Committee on Investments (CCI) has been set up to fast-track projects more than ₹ 1,000 crore. The Land Acquisition and Rehabilitation and Resettlement (LARR) Bill, which has been cleared by the Cabinet, could bring greater clarity, reduce uncertainty, and thereby aid investments. Investments by cash-rich public-sector units (PSU) have the potential of crowding-in the private sector. Progress on the Delhi-Mumbai Industrial Corridor has the potential of providing a fillip to the investment climate of the country. Policy rate cuts by the RBI and improving business sentiments could also support a revival in investments.

[1] **"Sharp Increase in Projects Shelved", CMIE, May 2012.**

from the rest of the world, particularly the advanced countries. A third possible reason for lower corporate investment is policy bottlenecks (such as obtaining environmental permissions, fuel linkages, or carrying out land acquisition, see Box 1.1), which led to a number of large projects becoming stalled, which may in turn have discouraged new investment. In what follows, the recent trends in various components of investment are discussed to understand the decline in overall investment rate.

1.23 Between 2004-05 and 2011-12, on an average, the share of the household sector and the private corporate sector in total private investment has been more or less equal. However, there are large fluctuations from year to year, with the share of the private corporate sector being significantly higher in the high growth years of 2005-06 to 2007-08 and much lower in the years when growth was lower, particularly in 2008-09 and 2011-12. Investment by the private corporate sector, at current prices, was lower by nearly ₹ 90,000 crore in 2011-12 as compared to 2010-11. Consequently, the share of private corporate investment in total investment declined to 29.8 per cent in 2011-12 as against 36.1 per cent in 2010-11. Parenthetically, the magnitude of decline was much larger in 2008-09, when private corporate investment declined by nearly ₹ 2,25,000 crore as compared to 2007-08.

1.24 Further analysis of the data reveals that the reduction in investment by the private corporate sector in 2011-12 was on account of a drawdown of the stocks. Unlike in 2008-09, when the gross fixed investment in the private corporate sector declined by nearly ₹ 1,30,000 crore vis-à-vis 2007-08, the gross fixed capital formation by the private corporate sector registered a marginal increase in 2011-12 vis-à-vis 2010-11. Of course, in real terms as well as in terms of percentage of total investment, gross fixed investment of the private corporate sector also declined in 2011-12 as against 2010-11. Given that consumption grew strongly in 2009-12 even while productive investment slowed, it is not surprising that the economy has become increasingly supply constrained.

1.25 Investment in the form of valuables increased by nearly ₹ 80,000 crore in 2011-12 vis-à-vis that in 2010-11. Valuables include works of art, precious metals, and jewellery carved out of such metals and stones. At current prices, investment in the form of valuables registered a nearly 4.5-fold increase between 2007-08 and 2011-12 and their share in total investment increased from 2.8 per cent in 2007-08 to 7.6 per cent in 2011-12. A part of the increase in this share can be explained by the surge in the prices of gold and other valuables. However, even at constant prices, the share of valuables increased from 2.9 per cent in 2007-08 to 6.2 per cent in 2011-12, thereby pointing to larger acquisition of valuables, including gold. Advance Estimates of CSO for 2012-13 suggest that acquisition of valuables may have declined in real terms.

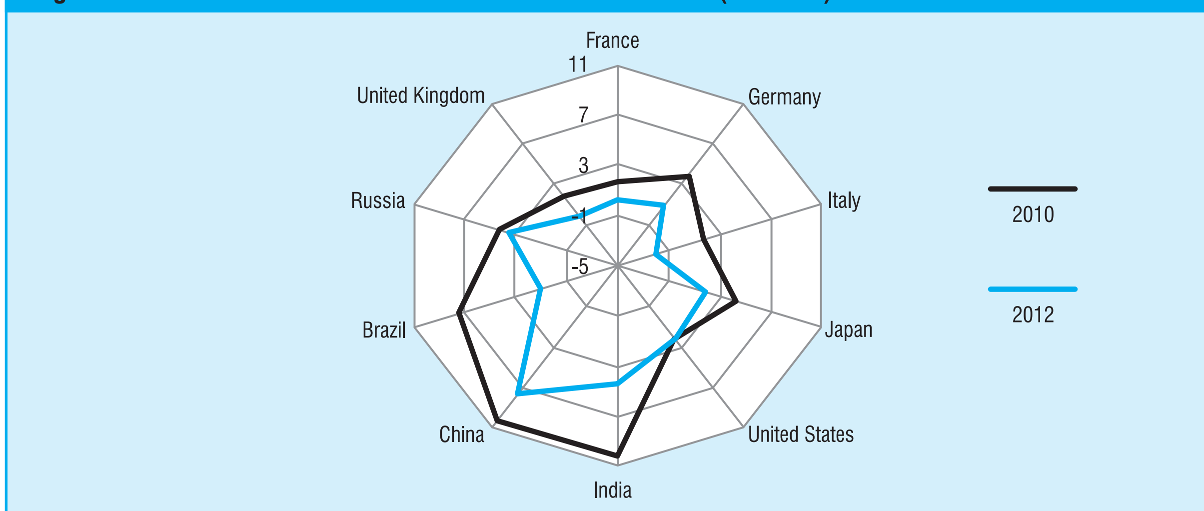
1.26 To summarize, overall investment would have slowed further were it not for non-productive investment such as in valuables. Particularly worrisome is the sharp slowing of corporate investment, which is the source of future supply (needed to quell inflation) and of future growth potential. Policies to remove investment bottlenecks as well as structural reforms to encourage productive investment and its financing are essential, as is more accommodative monetary policy, as inflation abates.

Net Exports

1.27 Growth in net exports can be an important source of demand. Unfortunately for India, net exports growth has been low because of global weakness. The World Economic Outlook (WEO) Update released by the IMF in January 2013 put the rate of growth of world output at 3.9 per cent in 2011 and 3.2 per cent in 2012, down from 5.1 per cent in 2010. For the advanced economies, the growth rate was much lower at 3 per cent, 1.6 per cent, and 1.3 per cent for 2010, 2011 and 2012 respectively. The growth rate in the faster growing emerging economies also fell over this period. Figure 1.4 gives growth rates for select advanced and emerging economies for 2010 and 2012 (based on information available from the WEO).

1.28 As a result of weak growth in trading partner countries, Indian exports also declined (see Box 7.1 in Chapter 7). In the first half of FY 2012-13 (April-September 2012), there was a steep decline in exports (Table 1.6). Imports did not decline as much in percentage point terms. Inelastic oil imports were the primary reason for the relatively smaller decline of imports. But gold imports, which have surged in recent years on the back of higher perceived returns on gold holdings, contributed significantly to imports, even though they declined in value over the previous year (Box 1.2). The net result was an increase in

Figure 1.4: Growth Rate of Real GDP of Select Economies (Per cent)



the trade deficit to 10.8 per cent of GDP in H1 of 2012-13 vis-à-vis 9.9 per cent of GDP in H1 of 2011-12.

1.29 The net invisibles balance (in which net service exports and remittances are prominent) usually offsets the trade deficit. However, it also declined in dollar terms in H1 of 2012-13 relative to H1 of 2011-12. The increased outflow of investment income to foreigners has also played a part in reducing net invisibles. As a result of the widening of the trade deficit and moderation in net invisibles surplus, the CAD worsened to 4.6 per cent of GDP during H1 of 2012-13 as compared to 4.0 per cent of GDP in H1 of 2011-12.

1.30 With investment, consumption, and net exports all slowing in 2012-13, only an increase in government spending could hold up economic growth. But the government deficit had already shot up as a result of past expansionary policy to pull India out of the post global financial crisis slump. And it increased further as slow growth diminished revenues.

Table 1.6 : Current Account Balance

Items	2011-12 H1(April-September 2011)	2012-13 H1(April-September 2012)
	US$ billion	
Exports	158.2	146.5
Imports	247.7	237.2
Trade deficit	89.5	90.7
Net invisibles	53.1	51.7
CAD	36.4	39.0
	Memo items as per cent of GDP	
Trade deficit	9.9	10.8
Net invisibles	5.9	6.2
CAD	4.0	4.6

Public Finance

1.31 Following the global financial crisis and the slowdown in aggregate demand that followed, fiscal stimulus was injected in 2008-09 and 2009-10 and the fiscal deficit of the centre increased to 6.0 per cent and 6.5 per cent of GDP respectively. Fiscal consolidation resumed in 2010-11 with a partial withdrawal of the fiscal stimulus. With growth in GDP recovering sharply in 2010-11, the fiscal deficit of the centre declined to 4.8 per cent of GDP. A large part of this was on account of the growth in nominal GDP in excess of 20 per cent.

1.32 This momentum could not be sustained in 2011-12 as growth faltered. The fiscal deficit of the centre widened to 5.7 per cent of GDP in 2011-12 (as per the Provisional Actuals). The dynamic nature of the relationship between macroeconomic outcome and the fiscal outcome was manifest thus: the sharp slowdown in industrial output led to a slowdown in overall GDP growth affecting tax revenues, particularly corporate income tax--the hitherto most buoyant source; the persistence of inflation that necessitated a tight monetary policy stance to rein in demand also dampened investment; subdued financial markets that hampered the planned disinvestment programme, resulting in slippage over Budget Estimates (BE); and continued high levels of global prices of crude oil and fertilizers with

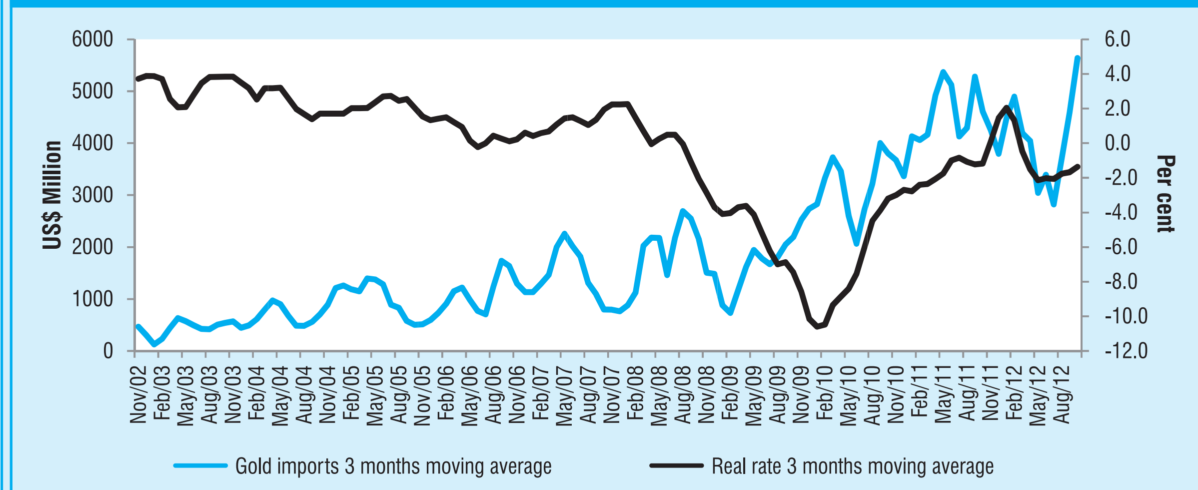
Box 1.2 : The Gold Rush[1]

1. **Demand for gold has been rising worldwide :** The global financial crisis, turned debt crisis, has seen a steep rise in commodity prices, especially gold. This, now in hindsight, rather unsurprising fact, has mostly been driven by the meteorically increasing demand for safe havens to park the world's savings. Global gold prices, as denominated in US$, have doubled since 2008, and increased three times as denominated in Indian rupees.

2. **India has traditionally been a major absorber of world gold :** The last three years have seen a substantial rise in gold imports (the value of gold imports increased nine times between January 2008 and October 2012), contributing significantly to the current account deficit along with oil (Figure 2).

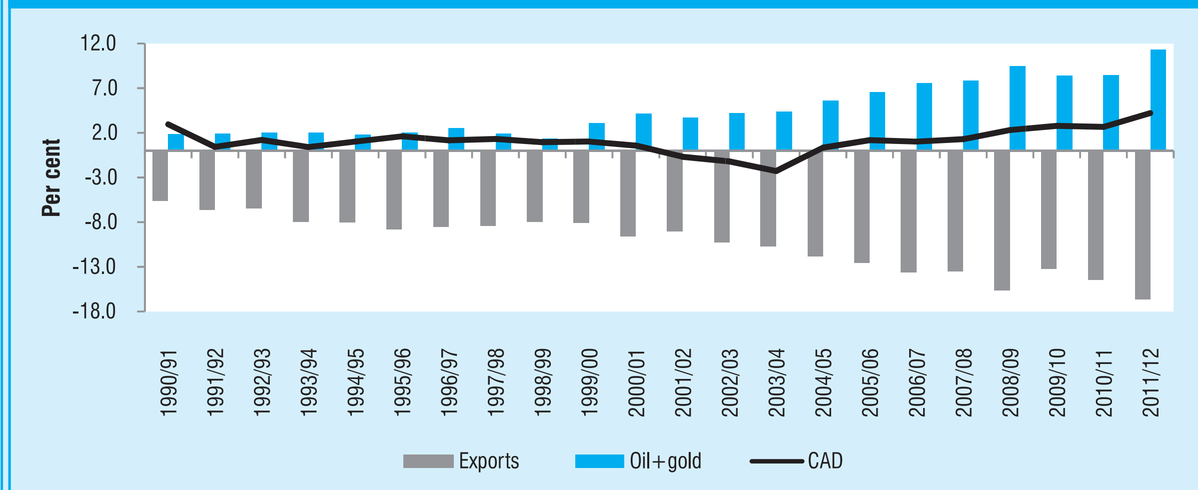
3. **Gold imports are positively correlated with inflation :** High inflation reduces the return on other financial instruments. This is reflected in the negative correlation between rising imports and falling real rates (Figure 1). Even though real rates have started rising, they are barely in the positive territory.

Figure 1: Gold imports (US$ million) and Real interest rate (repo rate-CPI inflation)



Source : CEIC Data Company.

Figure 2: Components of Current Account as per cent of GDP



Source : CEIC Data Company.

(Contd...)

Box 1.2 : The Gold Rush[1] (Contd...)

4. **Reduce Gold Purchases to curb CAD :** Given soaring energy and transportation needs, since there seems to be little we can do to temper oil imports, gold is the component that needs to be contained to bring the CAD back to a comfort zone.

5. **The demand for gold as an investment tool has been increasing over time :** Gold has been a combination of investment tool and status symbol in India. With limited access to financial instruments, especially in the rural areas, gold and silver are popular savings instruments. The recent economic uncertainty has seen people across the board buy gold. Almost all of India's demand for raw gold is met through imports[2]. Figure 3 shows that the composition of gold has seen a steady movement towards non jewellery items. Anecdotally, this can be construed as a rising demand for pure investment, predominantly in the urban and semi-urban areas. In the last quarter, non-jewellery constituted 40 per cent of the total demand. This observation, in line with global trends, is easily explained by the declining real returns on the gamut of financial instruments available to the investor and soaring ones on gold (23.7 per cent annual average return between April 07 and March 2012 versus 7.3 per cent return on Nifty and 8.2 per cent on savings deposits, Sehgal et. al., 2012).

Figure 3: Composition of Gold Demand - Jewellery Vs Other

Source : World Gold Council.

6. **The longer term way to address the rising demand for gold** : The overarching motive underlying the gold rush is high inflation and the lack of financial instruments available to the average citizen, especially in the rural areas. The rising demand for gold is only a "symptom" of more fundamental problems in the economy. Curbing inflation, expanding financial inclusion, offering new products such as inflation indexed bonds, and improving saver access to financial products are all of paramount importance.

1. Prepared by Mr. Rohit Lamba and Dr. Prachi Mishra. We would like to thank Amresh Acharya at the World Gold Council, Suresh Phadnis at PMEAC, Sneha Arora and Arun Narendhranath at ISB for many discussions.

2. There are three active gold mines, which meet less than 1 per cent of domestic demand.

References

Sehgal, Sanjay Muneesh Kumar, Wasim Ahmad and Priyanshi Gupta, 2012, "The gold rush and policy options: An empirical study", Department of Financial Studies, University of Delhi.

inadequate pass through to domestic consumption led to higher-than-budgeted subsidy outgo. Thus, the slippage in fiscal deficit in 2011-12 resulted from slippage of 35 per cent in revenue receipts, 23 per cent in disinvestment receipts and recovery of loans, and 42 per cent in expenditure outgo.

1.33 These macroeconomic developments broadly continued through the first half of the current fiscal. Concerns were raised in many quarters about the deterioration in the fiscal position for a second year in a row and the credibility of the fiscal policy stance. Recognizing that some of the assumptions made at the time of budget formulation needed to be reviewed and corrective policy measures put in place, the government appointed a committee headed by Dr Vijay Kelkar to chalk out a roadmap for fiscal consolidation.

1.34 Following its recommendations, the government unveiled a revised fiscal consolidation roadmap in October 2012. It targeted a fiscal deficit of 4.8 per cent of GDP for 2013-14 and through a correction of 0.6 percentage point each year thereafter, a fiscal deficit of 3.0 per cent of GDP in 2016-17. Controlling the expenditure on subsidies will be crucial. Domestic prices of petroleum products, particularly diesel and liquefied petroleum gas (LPG) need to be raised in line with the prices prevailing in international markets. A beginning has already been made with the decision in September 2012 to raise the price of diesel and again in January 2013 to allow oil marketing companies to increase prices in small increments at regular intervals. The number of subsidized gas cylinders has also been capped at nine. Efforts will also have to be made to contain subsidies through better targeting (see Box 1.3 on the rationale for capping gas cylinders), limit other expenditures, and raise revenues over time so as to take the revenue to GDP ratio to 2007-08 levels. The disinvestment process has also been speeded up. Taking all these measures into account, the Mid-Year Economic Analysis 2012-13 indicated a likely slippage in the fiscal deficit for the current fiscal by only 0.2 percentage point.

1.35 The Budget for 2012-13 estimated a fiscal deficit of ₹ 5,13,590 crore. As per the data on union government finances made available by the Controller General of Accounts, the fiscal deficit is placed at 78.8 per cent of BE, significantly below the five-year average of 85.9 per cent and last year's level of 92.3 per cent. Revenue deficit at the same time is placed at 85.1 per cent of BE, well below the level achieved in the recent past. This has largely been made possible by a moderation in growth of total expenditure in April-December 2012 to 10.6 per cent as against BE of 14.8 per cent for 2012-13 (over provisional actuals of 2011-12). This moderation in growth is in spite of the fact that subsidies have burgeoned in April-December 2012 to reach a figure of ₹ 1,66,824 crore (92.9 per cent of BE). The restraint in expenditure could largely offset the lower levels of non-debt receipts in April-December 2012.

1.36 Gross tax revenue was budgeted at ₹ 10,77,612 crore for 2012-13. As a proportion of BE, gross tax revenue in April-December 2012 was 63.2 per cent, lower than the last five-years' average of 69.0 per cent. The growth in gross tax revenue in April-December 2012 was 15.0 per cent, comprising a growth of 17.4 per cent in union excise duties; 6 per cent in customs; 22.5 per cent in personal income tax; 33 per cent in service tax; and 10.6 per cent in corporate income tax.

1.37 In terms of the implied year-on-year growth envisaged by BE 2012-13 over provisional actuals of 2011-12, there is slippage in the first nine months of the current fiscal in corporate income tax by 4.9 percentage points, customs by 18.9 percentage points, and central excise by 16 percentage points. There is overperformance in service tax collection by 5.9 percentage points and personal income tax by 7.6 percentage points. In terms of overall gross tax revenue there is slippage of 6 percentage points in April-December 2012. Going forward, the realization in the fourth quarter will determine the extent of shortfall for the year over BE.

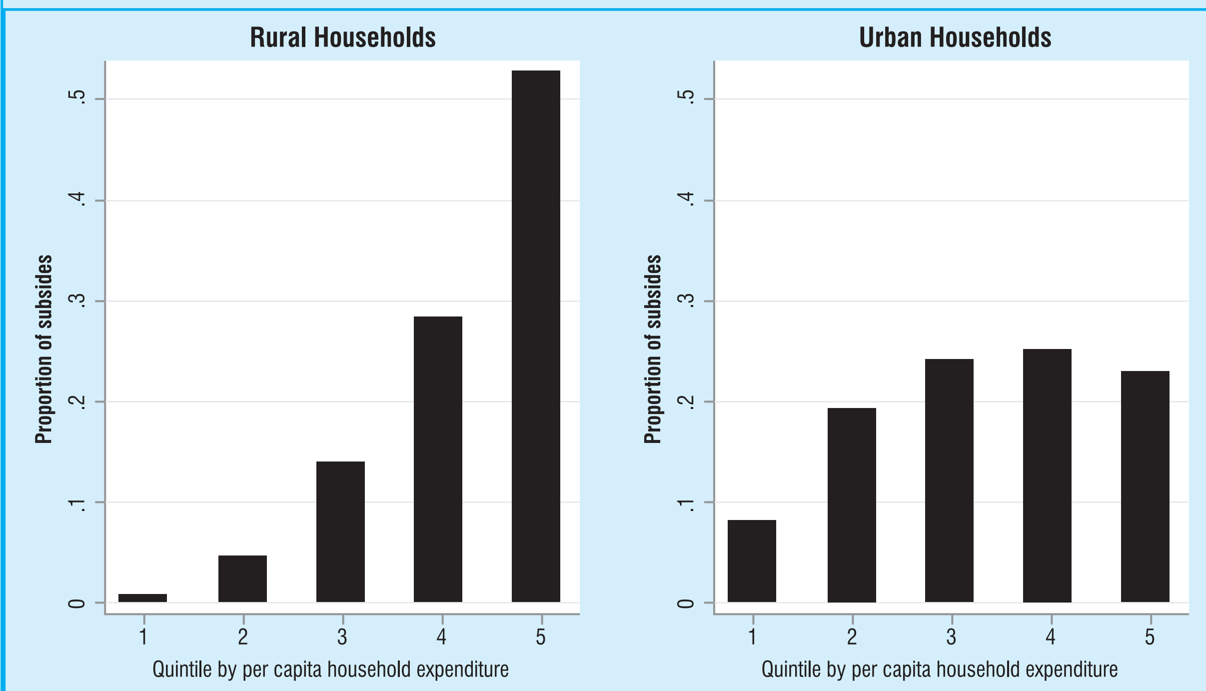
1.38 The outcome in terms of the fiscal deficit of the centre broadly indicates that the slippage will be limited to 0.2 percentage point on account of the expenditure measures that could help offset the shortfall in non-debt receipts. The crucial lesson that emerges from the fiscal outcome in 2011-12 and 2012-13 is that in times of heightened uncertainties, there is need for continued risk assessment through close monitoring and for taking appropriate measures for achieving better fiscal marksmanship. Open-ended commitments such as uncapped subsidies are particularly problematic for fiscal credibility because they expose fiscal marksmanship to the vagaries of prices.

1.39 It is better to achive fiscal consolidation partly through a higher tax-GDP ratio than merely through reduction in the expenditure to GDP ratio, in view of large unmet development needs. After reaching a peak of 11.9 per cent in 2007-08, the tax-GDP ratio had declined to 9.6 per cent in 2009-10 and was placed at 9.9 per cent in 2011-12. Therefore, raising the tax-GDP ratio to above the 11 per cent level is critical for sustaining the process of fiscal consolidation in the long run. Of course, it is much better to achieve a higher tax-GDP ratio by broadening the base which is taxed rather than increasing marginal tax rates significantly--higher and higher tax rates impinge more and more on incentives to undertake taxable activity, while encouraging tax evasion.

1.40 Finally, higher fiscal deficits usually lead to rising public debt. India's central government liabilities-GDP ratio has in fact come down since 2002-03 because high nominal GDP growth has

Box 1.3 : Who Gets LPG Subsidies?*

Subsidies should be well targeted at the poor. The reach of subsidies on LPG is highly unequal amongst the poor and rich in rural and urban areas. While there is a significant inequality in the proportion of subsidies received by the poorest and richest households in rural areas, the distribution is more equitable across urban households. However, in both cases, the proportion of subsidies that go to the poor is low.



The proportion of LPG subsidies received by each quintile across rural and urban households

To calculate the distribution of subsidies across households, we use the 64th Round of NSS data and categorize all rural (and urban) households into quintiles based on their per capita household expenditure. Furthermore, we use the reported household expenditure on LPG to calculate the share of each quintile in the total expenditure on LPG. The share in expenditure on LPG for any quintile therefore reflects the proportion of subsidies received by that quintile.

From the above graph, we see a highly unequal distribution of subsidies across rural households. The proportion of subsidies that go to the poorest quintile is only 0.07 per cent as compared to 52.6 per cent for the richest quintile. In urban areas, though the proportion of subsidies that go to the poor is still low (around 8.2 per cent), there is a more equitable distribution across the remaining quintiles (19 per cent, 24 per cent, 25 per cent and 23 per cent respectively).

*Prepared by Abhijit Banerjee and Gaurav Chiplunkar.

offset both the new borrowing as well as the nominal interest payments creditors have demanded. Put differently, India has been able to borrow at low real interest rates even while the government has run fiscal deficits. Such a sequence of events cannot be relied upon, which is yet another reason for bringing down the fiscal deficit.

1.41 Another way of looking at the slippage in public finances is to see it in the context of domestic savings, which is the safest way of financing investment. Large fiscal deficits may imply lower public savings, lower domestic savings, and given a level of investment, larger CADs. Of course, private savings can increase to make up the shortfall in public savings. Unfortunately, after moving up in 2008-09 and 2009-10, private savings have declined sharply, compounding the decline in public savings.

Domestic Savings

1.42 The volume and composition of domestic savings in India have undergone significant changes over the years. The savings rate (gross domestic savings as percentage of gross domestic product at market prices) averaged 18.6 per cent in the 1980s and 23 per cent in the 1990s. The savings rate exceeded 30 per cent for the first time in 2004-05

and has remained above that level ever since. It peaked in 2007-08 at 36.8 per cent and reached an eight-year low of 30.8 per cent in 2011-12 (the latest period for which we have complete figures) (Table 1.7).

1.43 Savings come from three sources, viz. households, the private corporate sector, and the public sector. On average, households accounted for nearly three-fourths of gross domestic savings during the period 1980-81 to 2011-12. The share declined somewhat in recent years, and in the period from 2004-05 to 2011-12, it averaged 70.1 per cent of total savings. Savings of the private corporate sector accounted for 15 per cent of total savings on an average between 1980-81 and 2011-12. However, during the years 2004-05 to 2011-12, their share increased to 23.2 per cent. The public sector accounted for 10 per cent of total savings on average between 1980-81 and 2011-12. It has been progressively declining and during 2004-05 to 2011-12, public savings as a ratio of total savings averaged 6.7 per cent. Figure 1.5 shows the trends in contribution of the household, private corporate, and public sectors to total savings since 1980-81.

1.44 Within households, the share of financial savings vis-à-vis physical savings has been declining in recent years. Financial savings take the form of bank deposits, life insurance funds, pension and provident funds, shares and debentures, etc. Financial savings accounted for around 55 per cent of total household savings during the 1990s. Their share declined to 47 per cent in the 2000-10 decade and it was 36 per cent in 2011-12. In fact, household financial savings were lower by nearly ₹ 90,000 crore in 2011-12 vis-à-vis 2010-11. Some possible explanations for the reduction in the share of financial savings are discussed in Box 1.4.

Figure 1.5: Share of type of institutions in total savings

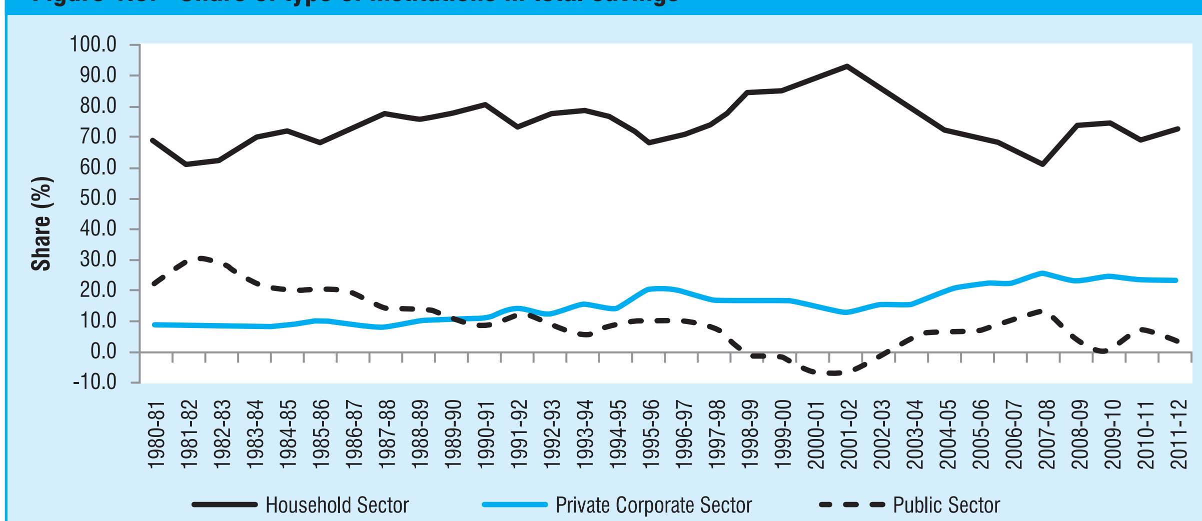


Table 1.7 : Ratio of Savings to GDP (at current market prices per cent)

	2004-05	2006-07	2007-08	2008-09	2009-10	2010-11 2R	2011-12 1R
Gross domestic saving	**32.4**	**34.6**	**36.8**	**32.0**	**33.7**	**34.0**	**30.8**
Public sector	2.3	3.6	5.0	1.0	0.2	2.6	1.3
Private sector	30.1	31.0	31.8	31.1	33.5	31.5	29.5
Household sector	23.6	23.2	22.4	23.6	25.2	23.5	22.3
Financial saving	10.1	11.3	11.6	10.1	12.0	10.4	8.0
Saving in physical assets	13.4	11.9	10.8	13.5	13.2	13.1	14.3
Private corporate sector	6.6	7.9	9.4	7.4	8.4	7.9	7.2

Source : **CSO.**

Notes **: 1R : First Revised Estimate, 2R : Second Revised Estimate.**

Box 1. 4 : Reduction in Financial Savings

Much of the financial savings of the household sector are in the form of bank deposits (around 30 per cent in the 2000s), life insurance funds (22 per cent in the 2000s as against 9.6 per cent in the 1980s), and pension and provident funds (16.5 per cent in the 2000s as against 23.6 per cent in the 1980s). There has been a decline in the proportion of pension and provident funds, particularly since the late 1990s. This trend continued till 2007-8. These were also the years when the real rate of interest was generally declining. There has been some upward movement in the share of pension and provident funds during 2008-9 and 2009-10, partly due to the increase in disposable income of government servants who are significant contributors to these funds, on account of higher pay and arrears arising from the implementation of the recommendations of the Sixth Pay Commission.

Shares and debentures accounted for 8.3 per cent of total financial savings in the1980s; their share increased to nearly 13 per cent in the 1990s before declining to 4.8 per cent in the 2000s. The reasons for such a trend could be the behaviour of share prices, as reflected by the Bombay Stock Exchange (BSE) Sensex, and depicted in the following Table.

	1980s	1990s	2000s
Average of BSE Sensex	448	3120	8612
Return on BSE Sensex (%) CAGR	-	21.4	10.7
Coefficient of Variation	42.3	33.2	60.1

***Note* : These have been calculated from the information available in the RBI's *Handbook of Statistics on Indian Economy*.**

The increase in the proportion of shares and debentures in total financial savings in the 1990s could be ascribed to higher returns (21.4 per cent per annum on an average for the decade) along with lower volatility as reflected by a lower coefficient of variation that declined from 42.3 in 1980s to 33.2 in the 1990s. The returns on the BSE Sensex halved to 10.7 per cent in the 2000s and volatility increased as can be seen from the higher value of the coefficient of variation at 60.1. Thus a combination of lower returns and higher volatility in the 2000s vis-à-vis the 1990s could have contributed to the reduced share of shares and debentures in total financial savings. This, coupled with high inflation, could also be one of the reasons why gold has become a 'safe haven' investment in recent times (see boxes 1.2 and 7.2). Acquisition of gold by the households in the country tends to have a negative impact on savings and on household financial investments.

1.45 One of the reasons for the increasing share of the private corporate sector in total savings could be that there has been an increase in the total profit to output ratio from 3.5 per cent for the 1980s to 5.4 per cent in the 1990s and further to 7.7 per cent in the 2000s in the factories sector (estimated from the information available from the Annual Survey of Industries). There has also been a reduction in certain costs, that is emoluments, interest payments, and fuels as a ratio of total value of output, as can be seen from Table 1.8. This reduction has contributed to profits and consequently higher savings of the corporate sector.

1.46 A slowdown in the industrial sector has an impact on private corporate savings, as was the case in 2008-09 and again in 2011-12, and the revival of this form of savings depends on how fast industry recovers.

1.47 Public-sector savings include savings by (a) public authorities comprising government administration and quasi-government bodies and departmental commercial enterprises and (b) non-departmental commercial enterprises. The share of public savings in total savings progressively declined from over 20 per cent in the 1980s to 7.3 per cent in the 1990s and further to 3.3 per cent in the 2000s. Within public savings, the share of non-departmental PSUs on an average remained in the range of 12-13 per cent during each of the three sub-periods. The share of public authorities in total savings declined by nearly 16 percentage points from a positive contribution of 7.4 per cent in the 1980s to a negative contribution of 8.7 per cent in the 2000s. Public authorities have generally been dis-savers since 1987-88, with large dis-savings since 1998-99.

1.48 Despite a long-term trend decline in savings by public authorities, there have been periods of improvement. On the back of strong growth in revenues and the Fiscal Responsibility and Budget Management Act of 2003, the combined fiscal deficit of both the central and state governments declined from 9.6 per cent of GDP in 2002-03 to 4 per cent of GDP in 2007-08. Public-sector savings as a ratio of GDP increased from - 0.3 per cent of GDP in 2002-03

Table 1.8 : Cost of certain inputs as a Ratio of Value of Output (per cent)

	1980s	1990s	2000s
Total emoluments	9.2	6.7	4.3
Fuel cost	8.3	7.4	6.7
Interest paid	5.1	5.5	2.6
Material consumed	60.8	59.4	62.2

Source **: Based on Annual Survey of Industries, Factory Sector.**

to 5 per cent in 2007-08, before declining following the fiscal stimulus in 2008-09. The significant improvement in domestic savings rate between 2003-04 and 2007-08 owed to a great extent to the increased public savings, stemming from fiscal consolidation.

1.49 As Table 1.5 suggests, gross fixed capital formation has fallen by over 2 percentage points between pre-crisis 2007-08 and 2011-12. However, gross domestic savings have fallen by about 6 percentage points over the same period. So even as we have to raise investment, especially corporate investment, raising domestic savings is the safest way of financing the increase without putting pressure on the current account balance. A large part of the future increase in savings will have to come from increased public savings. This will entail gradually reducing the central government's fiscal deficit from 5.8 per cent in 2011-12 to the 3 per cent projected for 2016-17 as per the fiscal roadmap (see previous section for details).

1.50 Household savings will also have to be raised. The financial savings of the household sector are likely to improve with lower inflation, especially as the real rate of return on financial savings rises. A greater variety of reliable financial savings opportunities (such as inflation-indexed bonds) and relative ease of access to them could also help in raising the share of financial savings in total savings, reducing the attractiveness of alternatives like gold.

1.51 Let us now turn to two important consequences of macroeconomic imbalances--prices and the balance of payments or external position.

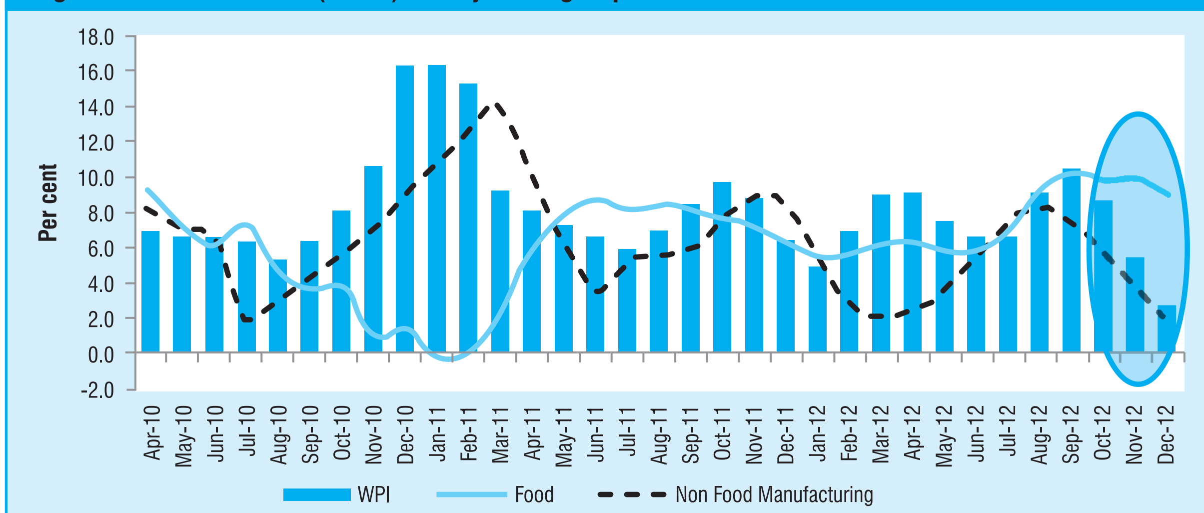
Prices and Monetary Management

1.52 Headline WPI inflation remained relatively sticky around 7 to 8 per cent in the current financial year and moderated to a three-year low of 7.18 per cent in December 2012. Average headline WPI inflation in 2012 (April-December) moderated to 7.55 per cent from 9.35 per cent in the corresponding period of the previous year. The momentum based on seasonally adjusted annualized rate (SAAR) has also been showing a declining trend in the last couple of months for major subgroups of the WPI (Figure 1.6). The decline is mainly due to moderation in non-food manufacturing inflation (core as defined by the RBI). Core inflation remains muted and declined to 4.24 per cent in December 2012 from its peak of 8.35 per cent in November 2011. Apart from monetary measures taken by the RBI, softening of international and domestic prices of metals, chemicals, and textiles products also contributed to the moderation of core inflation.

1.53 Elevated food inflation, however, remains an area of concern with inflation gradually inching upwards to double digits in December 2012. Unlike the previous year, when food inflation was mainly driven by higher protein food prices, this year the pressure has been coming mainly from cereals. Inflation in cereals has increased to 17.05 per cent in the third quarter of 2012-13 from 6.36 per cent in the first quarter mainly on account of an increase in prices of wheat, rice, and maize. Besides an increase in the minimum support price (MSP) for wheat and rice, inadequate open market availability relative to demand, particularly for wheat, has also resulted in a build-up of price pressure and hardening of inflation for cereals. The recent increase in onion prices in December 2012- January 2013 may also put some pressure on primary food articles inflation. However, milk and other protein items witnessed moderation in inflation in the second and third quarters of 2012-13.

1.54 Rising food inflation has also widened the gap between inflation measured in terms of CPIs and WPI to 3.91 percentage points in December 2012 from 1.55 percentage points in May 2012. However, global commodity prices have remained relatively benign with both energy and non-energy prices registering a decline until recently. As per the World Bank's Global Economic Prospects, except for metals, most global commodity prices are expected to decline further in 2013 and 2014, a silver lining in the tepid global recovery. The impact of benign inflationary expectations internationally will have a moderating impact on domestic prices.

Figure 1.6: Momentum (SAAR) in major sub groups of WPI



1.55 In the meantime though, the RBI has to weigh the costs of rapidly slowing growth against persistent CPI inflation. To the extent that the primary component of CPI inflation is food prices, elevated because of supply constraints, the textbook prescription is for the RBI to look through higher food prices even while setting rates to ensure that the 'second round effects' as reflected in core inflation are contained--in other words, set monetary policy based on the behaviour of core inflation. One worry with this more accommodative approach is that CPI inflation, which is what the public sees, is becoming entrenched in the public's expectations. A second worry is that high inflation may be causing anxious investors to shun fixed income investments such as deposits and even turn to gold as an inflation hedge, thus contributing to the CAD. Nevertheless, to the extent that monetary policy has limited influence over certain aspects of inflation such as food prices, it may be appropriate for monetary policy to set rates based on what it can influence, while keeping in mind that nominal interest rates affect many aspects of the economy other than growth and inflation.

1.56 From the government's perspective, a major contribution to the fight against inflation will be to reduce the fiscal impetus to demand. Also a focus on incentivizing food production through measures other than price supports, while facilitating storage and distribution, can help contain food inflation, which is hard for the RBI to control. Policy on price and procurement supports should be calibrated so as to not encourage more production of crops that are already abundantly supplied. Other measures to increase investment more broadly, and therefore supply, can also help over the medium term.

The Balance of Payments and External Position

1.57 The CAD in the first half of 2012-13 has been 4.6 per cent of GDP. Available indications do not seem to suggest any improvement in the current account balance in the second half. There is a case for discouraging imports of commodities like gold and making efforts to raise exports. While the government has 'thrown sand in the wheels' by raising the tariff on gold from 4 per cent to 6 per cent in order to discourage imports and tried to unlock passive gold holdings through gold loans, gold purchases are likely to come down primarily when households see attractive alternative investment avenues. Lower inflation will be the key. In the meantime, increasing exports at the present juncture is proving to be a more difficult task, given the slow global recovery. Greater competitiveness of exports through greater corporate productivity as well as better logistics infrastructure will help, as will diversification towards fast growing emerging and frontier markets--which is under way. But a return to strong export growth will depend on the revival of growth in industrial countries.

1.58 With net exports declining, India's balance of payments (BoP) has come under pressure. So far the CAD has been financed without drawing on reserves. Net capital flows declined to US$ 40.0 billion (4.8 per cent of GDP) in H1 of 2012-13 as against

Table 1.9 : Performance of BoP

Items	2011-12 H1(April-Sept 2011)	2012-13 H1(April-Sept 2012)
	US$ billion	
CAD	36.4	39.0
Capital account	43.5	40.0
Net FDI	15.7	12.8
Net portfolio(including FIIs)	1.3	5.8
NRI deposits	3.9	9.4
ECB	8.4	1.7
Trade credit	5.9	9.5
Memo items as per cent of GDP		
CAD	4.0	4.6
Net capital flows	4.8	4.8

Note **: ECB is external commercial borrowings.**

US$ 43.5 billion (4.8 per cent of GDP) in H1 of 2011-12 (Table 1.9). Net foreign direct investment (FDI) to India decreased but net portfolio flows including foreign institutional investments (FII) increased, with early estimates suggesting an even larger inflow of US$ 9.9 billion in the third quarter as compared to US$ 5.8 billion in the second quarter. Non-resident Indian (NRI) deposits remained robust as did net flows of trade credit. Despite the large CAD, therefore, there was net accretion to reserves (on BoP basis) during H1 of 2012-13 at US$ 0.4 billion. This was, however, lower than the US$ 5.7 billion accretion in H1 of the previous year.

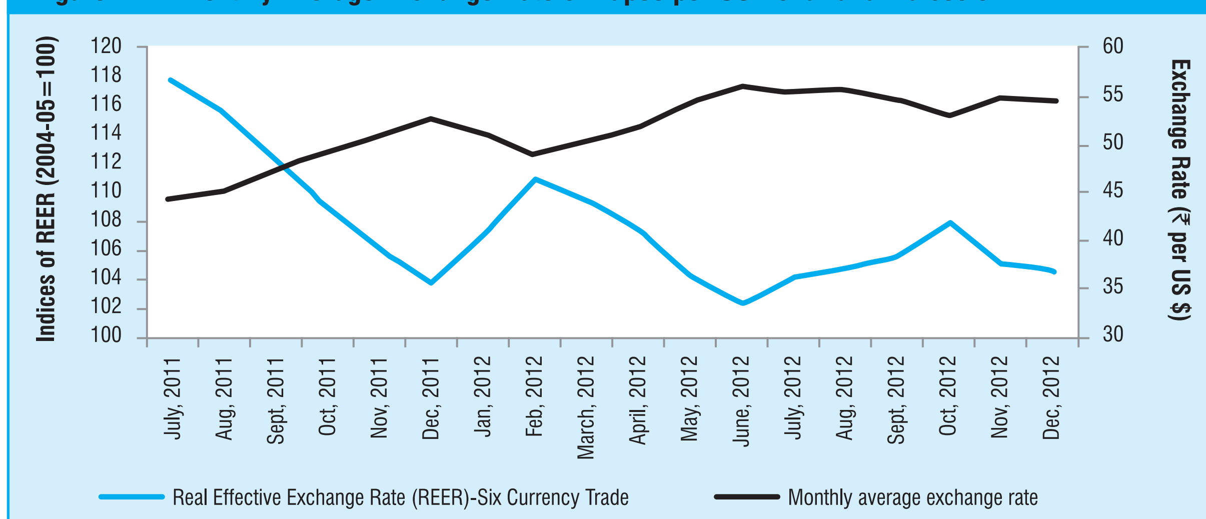
1.59 In the current fiscal, foreign exchange reserves have fluctuated between US$ 286.0 billion and US$ 295.6 billion. At end January 2013, reserves stood at US$ 295.5 billion, indicating a marginal increase from US$ 294.4 billion at end March 2012. The rupee, however, has been more volatile. Between April 2012 and January 2013, the monthly average value of the rupee per US dollar fluctuated significantly, touching an all-time low of ₹ 57.22 per US dollar on 27 June 2012, thus depreciating by 10.6 per cent from ₹ 51.16 per US dollar on 30 March 2012. In the subsequent months of July to September 2012, the rupee appreciated, touching ₹ 51.62 per US dollar on 5 October 2012. It began depreciating again thereafter and the monthly average exchange rate has since been in the range of ₹ 53.02 to ₹ 54.78 per US dollar during October 2012 to January 2013 (Figure 1.7).

1.60 The real effective exchange rate, which takes into account domestic inflation in India, and is an important determinant of the competitiveness of Indian exports, has depreciated by about 11 per cent since mid - 2011.

1.61 India's external debt stock stood at US$ 365.3 billion at end-September 2012, recording an increase of about US$ 20.0 billion (5.8 per cent) over the end-March 2012 level. This increase has been primarily on account of higher NRI deposits, short-term debt, and ECBs. These three components together contributed 94.7 per cent of the total increase in the country's external debt.

1.62 The maturity profile of India's external debt continues to be dominated by long-term loans. At end-September 2012, long-term external debt at US$ 280.8 billion, accounted for 76.9 per cent of total external debt, while the remaining 23.1 per cent was short-term debt. Government (sovereign) external debt stood at US$ 81.5 billion, while non-government

Figure 1.7: Monthly Average Exchange Rate of Rupee per US Dollar and indices of REER



debt amounted to US$ 283.9 billion at end-September 2012. India's external debt has remained within manageable limits as indicated by the external debt-GDP ratio of 19.7 per cent and debt service ratio of 6.0 per cent in 2011-12. But the trends in size, source, maturity, and hedging of external debt bear careful monitoring. In particular, regulators will have to be careful about the tendency of some Indian corporations or entities without substantial foreign exchange earnings to leave foreign exchange borrowings un-hedged so as to get 'cheap' foreign financing. Low un-hedged foreign interest rates can be deceptively enticing, leaving the borrower exposed to significantly higher repayments if the rupee depreciates unexpectedly.

1.63 In this context, regulators have to maintain a balance between what is of public importance and what is prudential. Areas of public importance, such as infrastructure, do deserve substantial support. However, these areas of activity may also be risky. Support should be given by de-risking the areas (policy to speed up infrastructure projects and ease their completion), through financial development (creating new financing institutions, attracting new investors), or fiscal means (interest subventions, tax breaks) but not by relaxing prudential norms (lower capital requirements, allowing un-hedged foreign borrowing) or riskier capital structures (allowing greater debt ratios). Ultimately, riskier financing for projects of public importance builds up greater risk for the country because if these projects fail to take off, they impinge on both growth and the financial system at the same time, at a time when the government has fewer resources to cope.

Assessment and Policy Measures

1.64 The strong post-financial-crisis fiscal and monetary stimulus in India led to spectacular growth in the immediate aftermath of the crisis. But with corporate and infrastructural investment not keeping pace, and food production constrained, the boost to consumption eventually led to higher inflation. And falling savings, partly as a result of government spending and partly as a result of high inflation, have led to a widening CAD. Monetary policy has been tightened, even as global headwinds to growth have increased. India has been caught in a vicious circle of falling growth and stimulus withdrawal that could well exacerbate the decline. Of some concern is India's increased dependence on foreign borrowing even as growth has slowed.

1.65 Because of the slowdown and high levels of leverage, some industry and infrastructure sectors are experiencing an increase in non-performing assets (NPAs). Overall gross NPAs of the banking sector increased from 2.36 per cent of total credit advanced in March 2011 to 3.57 per cent of total credit advanced in September 2012. The increase is particularly sharp for the industry and infrastructure sectors. Sub-sectors particularly under stress include textiles, chemicals, iron and steel, food processing, construction, and telecommunications. The increase in gross NPAs is also significantly higher for public-sector banks, which are typically more exposed to the distressed sectors.

1.66 Some of the reasons for the increase in NPAs are technical (a switch to system-based identification by public-sector banks), but stress also stems from slow growth and project delays. A revival of growth will help contain NPAs, but going forward, more attention will have to be paid to whether projects are adequately capitalized up front given the risks, and to whether distress resolution systems work effectively in recapitalizing distressed assets and putting them back to work, while excising ineffective promoters from management and imposing losses on those who contracted to take the risk.

1.67 The way out, and the hope for starting a virtuous circle, lies in shifting national spending from consumption to investment, removing the bottlenecks to investment, growth, and job creation, in part through structural reforms, combating inflation both through monetary and supply-side measures, reducing the costs for borrowers of raising financing, and increasing the opportunities for savers to get strong real investment returns.

1.68 In practical terms for government policy, this translates into containing the fiscal deficit especially by shrinking wasteful and distortionary subsidies. It means working on reducing the impediments to investment such as delays in getting permissions, clarifying difficult and non-transparent processes for land acquisition, and increasing access to good infrastructure such as power and roads. It warrants reworking the regulatory and incentive structure that keeps small businesses tiny and prevents them from creating good productive jobs. It calls for reducing the barriers to entry in various areas of business and allowing FDI, even while ensuring domestic companies are not disadvantaged. It entails providing the incentives and means for the farmer to increase

production, even while improving the management and the logistics of food procurement and distribution. And it necessitates continuing financial-sector reform to increase the entry of new institutions, reduce transactions costs for investors, increase access for borrowers and savers to one another, and improve the quality of regulation.

1.69 The government has already taken some important steps in this direction, some of which we have already alluded to. In addition, two helpful potential developments are in sight, one on the revenue side and the other on the expenditure side. The goods and services tax (GST), if approved, would replace a number of state and central taxes, make India more of a national integrated market, and bring more producers into the tax net. By improving efficiency as well as revenues, it can add substantially to growth as well as helping government finances. On the expenditure side, the direct benefit transfer scheme that will allow the transfer of government benefits directly to targeted recipient bank accounts can help reduce transactions costs, prevent duplication, leakage, and fraud, and improve choices for the poor. By translating a number of subsidies into equivalent cash transfers, it can avoid price distortions and can target subsidies better to the truly deserving. This will help contain expenditure.

1.70 The government has also taken a number of steps to revive investment and growth. These comprise setting up the CCI headed by the Prime Minister to fast-track mega projects of over ₹ 1,000 crore; a scheme for restructuring the debts of state power distribution companies, which includes incentives for them to charge reasonable tariffs so that they do not get over-indebted again; movement towards a land acquisition bill that will clarify and make the process of land acquisition fairer; permitting FDI in a number of areas including multibrand retail, power exchanges, and civil aviation; increasing investment in irrigation, storage and cold storage networks; and undertaking programmes to improve the production of protein foods.

1.71 Steps have also been taken on financial-sector reform. The Banking Laws (Amendment) Act 2012 strengthens the regulatory powers of the RBI and paves the way for grant of new bank licences by the RBI. The Financial Sector Legislative Reforms Commission is examining the laws governing the financial sector with a remit to suggest ways of modernizing them. A number of steps have been taken by the government, together with the financial-sector regulators, for easing savings and investment in the country, both for domestic and foreign investors. These are detailed in Chapter 5.

1.72 More generally, India's situation is difficult but steps have been taken to bring the macroeconomy back into balance and growth on track. What is important is to recognize that a lot needs to be done and the slowdown is a wake-up call for increasing the pace of actions and reforms.

Prospects, Short Term and Medium Term

1.73 The revival of growth in the advanced countries is expected to be slow and uncertain at least in the near future, despite the measures being taken on monetary and fiscal fronts. In Europe, in particular, this is also being accompanied by changes in the institutional framework. With the ongoing private-sector deleveraging and government fiscal consolidation, most analysts have projected only a very moderate global recovery in 2013, which could gather steam in 2014. At the same time, if the United States can deal with its fiscal overhang, the potential upside to global growth could be substantial, given the health of US corporations, continuing innovation, low energy costs, and the improving finances of households. Emerging markets can also compensate a little for tepid growth in industrial economies, and the changing direction of Indian exports towards emerging markets (see Chapter 7) can help their revival.

1.74 Nevertheless, it is unlikely that the support to Indian growth from the global economy will be significant. Indeed, there are two sources of downside risk. First, India is exposed to shifts in the risk tolerance of international investors. Second, India's import bill is strongly tied to the price of oil. Of course, one reason for rising oil prices would be improvements in the global economy, which would mean stronger exports. The more worrisome situation would be if the oil prices rise because of geopolitical risks, which would mean increasing investor anxiety and slow world growth.

1.75 The bottomline is that India cannot take the external environment for granted, and has to move quickly to restore domestic balance. The government is committed to fiscal consolidation. This along with demand compression and augmented agricultural production should lead to lower inflation, giving the RBI the requisite flexibility to reduce policy rates.

Lower interest rates could provide an additional fillip to investment activity for the industry and services sectors, especially if some of the regulatory, bureaucratic, and financial impediments to investment are eased.

1.76 Given such a scenario, where all the three major sectors of the economy perform better in 2013-14 as compared to 2012-13, the overall economy is expected to grow in the range of 6.1 to 6.7 per cent in 2013-14. Of course, these projections assume a normal monsoon, further moderation in inflation as expected (to induce further relaxation of the tight monetary stance), and mild recovery of global growth as anticipated. Forecasting at potential turning points is difficult, hence the relatively wide range this time.

1.77 While the current environment is difficult, the future holds promise, provided we can answer the question that is probably foremost in the minds of India's young population: 'Where will my job come from?' In Chapter 2, we look at this question in some depth. India is creating jobs in industry but mainly in low productivity construction and not enough formal jobs in manufacturing, which typically are higher productivity. The high productivity service sector is also not creating enough jobs. As the number of people looking for jobs rises, both because of the population 'dividend' and because share of agriculture shrinks, these vulnerabilities will become important. Because good jobs are both the pathway to growth as well as the best form of inclusion, we have to think of ways of enabling their creation. Chapter 2 examines possible avenues.

1.78 Let us now turn to summary outlines of the chapters in the survey that focus on different sectors and aspects of the complex economy that India is.

Agriculture and Food Management

1.79 Indian agriculture has performed remarkably well in terms of output growth, despite weather and price shocks in the past few years. Although agriculture, including allied activities, accounted for only 14.1 per cent of the GDP in 2011-12, its role in the country's economy is much bigger with its share in total employment as high as 58.2 per cent according to the 2001 census. The declining share of the agriculture and allied sector in the country's GDP is consistent with the normal development trajectory of any fast growing economy (see Chapter 2), but fast agricultural growth remains vital for jobs, incomes, and food security.

1.80 Average annual growth of the agriculture and allied sector during the Eleventh Five Year Plan at 3.6 per cent fell short of the target of 4 per cent but was higher than the average annual growth of 2.5 and 2.4 per cent achieved during the Ninth and Tenth Plans respectively. An important reason for the dynamism of the agriculture sector has been a step-up in the gross capital formation (GCF) relative to GDP of this sector. Overall GCF in agriculture (including the allied sector), more than doubled in the last 10 years and registered an average annual growth of 8.1 per cent. During the Eleventh Plan period, foodgrains production witnessed an increasing trend, except in 2009-10. During 2011-12, total foodgrains production reached a record of 259.3 million tonnes. Better agricultural performance in the Eleventh Plan is a result of: a) farmers' response to better prices; b) continued technology gains; and c) appropriate and timely policies coming together, e.g. increased credit at concessional rates. However, the production of 2012-13 kharif crops is likely to be adversely affected by deficiency in the south-west monsoon and resultant acreage losses. The output for all the major crops is expected to decline.

1.81 Owing to good production of foodgrains in recent years and remunerative MSPs, even states that were traditionally not procuring sufficient foodgrains, e.g. Bihar, Madhya Pradesh, Bihar, Chhattisgarh, and West Bengal showed significant increase. In recent years, the policy impetus provided by the government has also provided much required stability to agricultural exports.

1.82 India does not fare well, however, in terms of agricultural yields or productivity. Improvement in yields holds the key for India to remain self-sufficient in foodgrains. Another challenge is how to maximize agricultural income while adopting a more sustainable agricultural strategy. The concerns here are land and water degradation due to soil erosion, soil salinity, waterlogging, excessive application of nutrients, and overexploitation of water resources in some parts of the country. Better management practices for rehabilitation of degraded land and water resources hold the key. Expenditure on agricultural research also needs to be raised in the Twelfth Five Year Plan.

1.83 A notable feature of the Indian agricultural sector is the domination of small farmers with small landholdings. This poses a challenge for the adoption of farm mechanization and generating productive incomes from farm operations. Land-related issues and implementation of land reforms require to be attended to on priority basis to revitalize the agriculture sector. Declining per capita availability of foodgrains is another major concern in India. For ensuring nutritional security, it is not only important to increase per capita availability of foodgrains but also to ensure the right amounts of food items in the food basket of the common man. A thrust on horticulture products and protein-rich items is required for ensuring nutritional security.

1.84 Another critical issue is supply-chain management in agricultural marketing in India. It is necessary to evolve mechanisms for linking wholesale processing, logistics, and retailing with farm-production activities so as to generate enhanced efficiency, better farm prices, etc. Recently the government allowed FDI in retail, which can pave the way for investment in new technology and marketing of agricultural produce in India.

1.85 There is need for stable and consistent policies where markets play an appropriate role, private investment in infrastructure is stepped up, the public distribution system (PDS) is revamped, food price and food stock management improves, and a predictable trade policy is adopted for agriculture. These initiatives need to be coupled with skill development and better research and development (R&D) along with improved delivery of credit, seeds, etc.

Industry and Infrastructure

1.86 The capital goods sector remained weak for the second consecutive year. Negative growth was not only experienced across the sub-sectors of the capital goods segment but was also more persistent with only two months in the last twelve months recording positive growth. The production of key capital goods such as machinery and equipment , electrical machinery, and transport segments contracted owing to deceleration in investment, a decline in new projects, and import competition. High interest rates and slower growth in household or retail credit resulted in slower growth in consumer durables.

1.87 Sluggish industrial performance also affected corporate performance. The rate of growth of sales of the listed manufacturing companies in the private sector declined from an average of 28.8 per cent in the first quarter of 2010-11 to 11.4 per cent in the second quarter of 2012-13. Interest expenditure increased significantly. Together with a deceleration in the rate of growth of sales, the ratio of net profit to sales also declined.

1.88 The aggregate resource flow to industry, including credit disbursed by the banks and money raised in domestic and overseas market through other instruments, however, has been showing some signs for optimism. The total flow of financial resources to the commercial sector in the current financial year so far (up to 11 January 2013) has been higher compared to the corresponding period of the previous year.

1.89 The eight core infrastructure industries registered a growth of 3.3 per cent during April-December 2012 compared to 4.8 per cent during the same period of the previous year. The decline in growth in the current year so far is mainly on account of negative growth witnessed in the production of coal, natural gas, and fertilizers. Among infrastructure services, freight traffic by railways has been comparatively higher during the first eight months of the current year. In the road sector the National Highways Authority of India (NHAI) achieved 17.3 per cent growth in widening and strengthening of highways during April-November 2012.

1.90 A large number of major central-sector projects costing ₹ 150 crore and more are delayed with respect to their latest scheduled dates of completion. Delays in land acquisition, municipal permission, supply of materials, award of work, operational issues, etc. continue to bog down project implementation.

Services Sector

1.91 The services sector is the dominant sector in most developed economies of the world and in some developing economies such as India. The CAGR of the services sector GDP was 10 per cent for the period 2004-05 to 2011-12. It has clearly outgrown both the industry and agriculture sectors. In 2011-12 and 2012-13, in tune with the general moderation in the economy, the growth rate of the services sector also declined. The services sector is providing

employment to more people, but employment growth is probably below the desired pace, given how productive service jobs are (see Chapter 2).

1.92 The slowdown in the rate of growth of services in 2011-12, and particularly in 2012-13, from the double-digit growth of the previous six years, contributed significantly to slowdown in the overall growth of the economy. While some slowdown could be attributed to the lower growth in agriculture and industrial activities, given the backward and forward linkages with services, lower demand from the rest of the world could also have played a part.

Financial Intermediation

1.93 The existence of well-developed and efficient financial markets is critical for achieving real economic growth. The country now has a vibrant and transparent financial market in terms of market efficiency, transparency, and price discovery process.

1.94 As far as the banking sector is concerned, the focus continues to be on reform initiatives which will facilitate the flow of credit to critical sectors of the economy including agriculture, infrastructure, micro, small and medium enterprises, housing, and export. Financial inclusion and improved accessibility of banking infrastructure remain high on the list of priorities of the government. The performance of Indian banks during 2011-12 was conditioned to a large extent by the fragile recovery of the global financial markets as well as a challenging operational environment on the domestic front, with persistent high inflation and muted growth performance. Net profit growth of banks slowed down. Though Indian banks remained well-capitalized, concerns regarding growing NPAs persisted.

1.95 In the overall context of the evolving macroeconomic situation in the country and global financial developments, the government in close collaboration with the RBI and Securities and Exchange Board of India (SEBI) has recently taken a number of initiatives to meet the growing capital needs of the Indian economy. Some of the initiatives taken in this regard are launching of the Rajiv Gandhi Equity Savings Scheme (RGESS) and SME exchange / platform, expansion of the Qualified Foreign Investors (QFIs) Scheme to facilitate their access to the Indian capital market, progressive enhancement in the quantitative limits for FIIs' investments in various debt categories, allowing refinancing rupee loans through ECB route for Indian companies in the power sector, reduction in the withholding tax on interest payments on ECBs, and introducing a new ECB scheme for companies in the manufacturing and infrastructure sector.

1.96 Investment sentiment started improving in the last few months with foreign investors reposing more confidence in the Indian economy in general and markets in particular. During the current financial year (up to 31 December 2012), the rise in the indices stood at 11.62 per cent for the Sensex and 11.51 per cent for Nifty. The economic and political developments in the Euro-zone area and United States had an impact on markets around the world including India. The temporary resolution of the 'fiscal cliff' in the US had a positive impact on the markets. Further, the reform measures initiated by the government recently have been received well by the markets.

Human Development

1.97 Economic growth though important cannot be an end in itself. The Twelfth Five Year Plan, with its focus on 'Faster, More Inclusive and Sustainable Growth', puts the growth debate in the right perspective. The government's targeted policies for the poor, with the prospect of fewer leakages, can help better translate outlays into outcomes.

1.98 Expenditure on social services by the general government (centre and states combined) has increased in recent years reflecting the higher priority given to this sector. Expenditure on social services increased considerably in the Twelfth Plan, with the education sector accounting for the largest share, followed by health. As a proportion of GDP, expenditure on social services increased from 5.9 per cent in 2007-08 to 6.8 per cent in 2010-11 and further to 7.1 per cent in 2012-13(BE). Nevertheless, India's expenditure on health as a per cent of GDP is lower than in many other emerging and developed countries and the share of the public sector still lower.

1.99 Poverty has declined in the country, though precisely how poverty is measured is currently being examined. Based on the methodology suggested by the Tendulkar Committee, the percentage of people living below the poverty line in the country declined from 37.2 per cent in 2004-

05 to 29.8 per cent in 2009-10. Even in absolute terms, the number of poor people declined by 52.4 million during this period. Of this, 48.1 million are rural poor and 4.3 million urban poor. Thus poverty has declined on an average by 1.5 percentage points per year between 2004-05 and 2009-10. The annual average rate of decline during the period 2004-05 to 2009-10 is twice the rate of decline during the period 1993-94 to 2004-05.

1.100 In the last few years public expenditure on social programmes increased dramatically. In the Eleventh Plan period nearly ₹ 7 lakh crore has been spent on the 15 major flagship programmes. A number of legislative steps have also been taken to secure the rights of people, like the Right to Information Act, the Mahatma Gandhi National Rural Employment Guarantee Act (MGNREGA), the Forest Rights Act, and the Right to Education (RTE). However, there are also pressing governance issues like programme leakages and funds not reaching the targeted beneficiaries that need to be addressed. Direct benefit transfer (DBT) with the help of the Unique Identification (UID) number can help plug some of these leakages.

Sustainable Development and Climate Change

1.101 Though multilateral efforts on sustainable development and climate change have led to several positive outcomes, there are still areas of concern where further work is needed to safeguard the interests of developing countries. The key question to be addressed is equity in the evolving arrangements. It has to be ensured that domestic goals continue to be nationally determined even as we contribute to the global efforts according to the principle of common but differentiated responsibilities (CBDR). More importantly, equity, fair burden sharing, and equitable access to global atmospheric resources have to be protected and addressed more adequately.

1.102 With the Twelfth Plan's focus on 'environmental sustainability', India is on the right track. However, the challenge for India is to make the key drivers and enablers of growth – be it infrastructure, the transportation sector, housing, or sustainable agriculture – grow sustainably. This leads us to the most vital issue: of raising additional resources for meeting the need for economic growth with greater environmental sustainability. More often, it is the resource crunch which is the stumbling block for developing countries like India. While it makes efforts to efficiently and expeditiously bring price signals and other policy instruments into play, India could do much more if new and additional finance and technology were made available through the multilateral processes. There is a case for greater cooperation, action, and innovation, provision of finance and technology for developing countries, and institutions and mechanisms for capacity building.