Chapter 1

The State of the Economy

In 2014-15, the Indian economy is poised to overcome the sub-5 per cent growth of gross domestic product (GDP) witnessed over the last two years. The growth slowdown in the last two years was broad based, affecting in particular the industry sector. Inflation too declined during this period, but continued to be above the comfort zone, owing primarily to the elevated level of food inflation. Yet, the developments on the macro stabilization front, particularly the dramatic improvement in the external economic situation with the current account deficit (CAD) declining to manageable levels after two years of worryingly high levels was the redeeming feature of 2013-14. The fiscal deficit of the Centre as a proportion of GDP also declined for the second year in a row as per the announced medium term policy stance. Reflecting the above and the expectations of a change for the better, financial markets have surged. Moderation in inflation would help ease the monetary policy stance and revive the confidence of investors, and with the global economy expected to recover moderately, particularly on account of performance in some advanced economies, the economy can look forward to better growth prospects in 2014-15 and beyond.

1.2 After achieving unprecedented growth of over 9 per cent for three successive years between 2005-06 and 2007-08 and recovering swiftly from the global financial crisis of 2008-09, the Indian economy has been going through challenging times that culminated in lower than 5 per cent growth of GDP at factor cost at constant prices for two consecutive years, i.e. 2012-13 and 2013-14. Sub-5 per cent GDP growth for two years in succession was last witnessed a quarter of a century ago in 1986-87 and 1987-88 (Figure 1.1). Persistent uncertainty in the global outlook, caused by the

Economic growth has slowed due to domestic structural and external factors. Two successive years of sub-5 per cent growth is witnessed for the first time in 25 years.

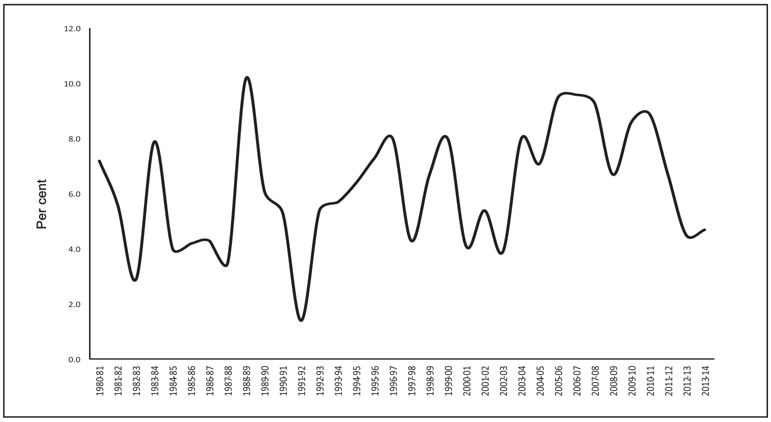


Figure 1.1 : Growth in Real GDP (per cent)

Source: Central Statistics Office (CSO)

Table 0.1 : Key Indicators

Data categories	Unit	2009-10	2010-11	2011-12	2012-13	2013-14
1. GDP and Related Indicators						
GDP (current market prices)	₹ Crore	6477827	7784115	9009722[2R]	10113281[1R]	11355073[PE]
Growth Rate	%	15.1	20.2	15.7	12.2	12.3
GDP (factor cost 2004-05 prices)	₹ Crore	4516071	4918533	5247530[2R]	5482111[1R]	5741791[PE]
Growth Rate	%	8.6	8.9	6.7	4.5	4.7
Savings Rate	% of GDP	33.7	33.7	31.3	30.1	na
Capital Formation Rate	% of GDP	36.5	36.5	35.5	34.8	na
Per Capita Net National Income (factor cost at current prices)	₹	46249	54021	61855	67839	74380
2. Production						
Food grains	Million tonnes	218.1	244.5	259.3	257.1	264.4[a]
Index of Industrial Production [b] (growth)	%	5.3	8.2	2.9	1.1	-0.1
Electricity Generation (growth)	%	6.1	5.5	8.2	4.0	6.1
3. Prices						
Inflation (WPI) (average)	%	3.8	9.6	8.9	7.4	6.0
Inflation CPI (IW) (average)	%	12.4	10.4	8.4	10.4	9.7
4. External Sector						
Export (in US$ terms)	% change	-3.5	40.5	21.8	-1.8	4.1
Import (in US$ terms)	% change	-5.0	28.2	32.3	0.3	-8.3
Current Account Balance (CAB/GDP)	%	-2.8	-2.8	-4.2	-4.7	-1.7
Foreign Exchange Reserves[c]	US$ Billion	279.1	304.8	294.4	292.0	304.2
Average Exchange Rate[d]	₹/US$	47.44	45.56	47.92	54.41	60.5
5. Money and Credit						
Broad Money (M3) (annual)	% change	16.9	16.1	13.2	13.6	13.3
Scheduled Commercial Bank Credit	% change	16.9	21.5	17	14.1	13.9
6. Fiscal Indicators (Centre)						
Gross Fiscal Deficit	% of GDP	6.5	4.8	5.7	4.9	4.5[e]
Revenue Deficit	% of GDP	5.2	3.2	4.4	3.6	3.2[e]
Primary Deficit	% of GDP	3.2	1.8	2.7	1.8	1.2[e]
7. Population	Million	n.a.	1210[f]	n.a.	n.a.	n.a.

Note: na: not available. 1R: 1st Revised Estimates, 2R: 2nd Revised Estimates, PE: Provisional Estimates.

a Third advance estimates.

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

c At end March.

d Average exchange rate (RBI's reference rate).

e Fiscal indicators for 2013-14 are based on the provisional actuals.

f Census 2011.

crisis in the Euro area and general slowdown in the global economy, compounded by domestic structural constraints and inflationary pressures, resulted in a protracted slowdown. The slowdown is broadly in sync with trends in other emerging economies, but relatively deeper. India's growth declined from an average of 8.3 per cent per annum during 2004-05 to 2011-12 to an average of 4.6 per cent in 2012-13 and 2013-14. Average growth in the emerging markets and developing economies including China declined from 6.8 per cent to 4.9 per cent in this period (calendar-year basis). What is particularly worrisome is the slowdown in manufacturing growth that averaged 0.2 per cent per annum in 2012-13 and 2013-14.

1.3 In addition to the growth slowdown, inflation continued to pose significant challenges. Although average wholesale price index (WPI) inflation declined in 2013-14 to 6.0 per cent vis-à-vis 8.9 per cent in 2011-12 and 7.4 per cent in 2012-13, it is still above comfort levels. Moreover, WPI inflation in food articles that averaged 12.2 per cent annually in the five years ending 2013-14, was significantly higher than non-food inflation. Fortunately, the upward trend of inflation that played a part in slowdown in growth, savings, investment, and consumption, appears to have subsided.

Inflation has eased but is still above comfort levels.

1.4 The external sector witnessed a remarkable turnaround after the first quarter of 2013-14, and the year ended with a CAD of 1.7 per cent of GDP as against 4.7 per cent in 2012-13. After plummeting to ₹ 68.36 to a US dollar on 28 August 2013, triggered by the expected taper of quantitative easing in the United States, the rupee gradually strengthened and the year ended with the exchange rate averaging ₹ 61 per US dollar in March 2014, owing to measures taken by the government and the Reserve Bank of India (RBI). Foreign exchange reserves increased by nearly US$ 40 billion from US$ 275 billion in early September 2013 to US$ 314.9 billion on 20 June 2014. These developments on external account have generated some optimism that the Indian economy is better prepared to confront the challenges of global policy reversals, including tapering of quantitative easing in the US. Improvement is also observed on the fiscal front, with the fiscal deficit declining from 5.7 per cent of GDP in 2011-12 to 4.9 per cent in 2012-13 and 4.5 per cent in 2013-14. Much of this improvement has been achieved by reduction in expenditure rather than from increased revenue. Nevertheless, the corrections in fiscal and current account deficits augur well for macroeconomic stabilization.

Improvements are visible on the fiscal front and in the current account balance.

1.5 The improvements in the twin deficits would, no doubt, feed into a higher growth in 2014-15, but the pace of recovery may be gradual. After reaching a low of 4.4 per cent during the last two quarters (Q3 and Q4) of 2012-13, growth inched up to 4.7 per cent in Q1 of 2013-14 and further to 5.2 per cent in Q2 of 2013-14, only to decline to 4.6 per cent in the next two quarters. The fact that this happened despite a gradual recovery in the global economy indicates the importance of addressing the domestic structural constraints that have engendered an undulating and gradual recovery (Box 1.1).

Sustenance of early signs of growth pick-up depends on amelioration of structural constraints.

Box 1.1 : What are structural constraints?

The impact of domestic structural factors on the current economic slowdown in India is often explained in terms of the irreconcilability of rate of fixed investment of around 30 per cent of GDP and sub-5 per cent growth, given India's demand conditions and long-term incremental capital-output ratio. Application of time series techniques that attempt to decompose the slowdown into structural and cyclical components, have acknowledged the presence of both, though the assignment of proportions differs (Chinoy and Aziz [2013]; IMF, WEO [2014]; Mishra [2013], among others). The accentuation of structural constraints has been one of the factors contributing to sub-5 per cent growth without a commensurate large decline in investment rate.

What are these structural factors? Salient among them as indicated by some studies are the following:

- Difficulties in taking quick decisions on project proposals have affected the ease of doing business. This has resulted in considerable project delays and insufficient complementary investments.
- Ill-targeted subsidies cramp the fiscal space for public investment and distort allocation of resources.
- Low manufacturing base, especially of capital goods, and low value addition in manufacturing. Manufacturing growth and exports could be facilitated with simplified procedures, easy credit, and reduced transaction cost.
- Presence of a large informal sector and inadequate labour absorption in the formal sector. Absence of required skills is considered an important reason.
- Sustaining high economic growth is difficult without robust agricultural growth. Low agricultural productivity is hampering this.
- Structural factors engendering continued high food inflation need to be tackled. Issues related to significant presence of intermediaries in the different tiers of marketing, shortage of storage and processing infrastructure, inter-state movement of agricultural produce, etc. need to be addressed.

References

1. Chinoy, Sajjid Z. and Jahangir Aziz (2013), 'Why is India's growth at a 10-year low?', available at www.jpmorganmarkets.com.
2. Mishra, Prachi (2013), 'Has India's Growth Story Withered?', *Economic and Political Weekly*, vol. XLVIII (15).
3. International Monetary Fund (IMF) (2014), World Economic Outlook (WEO), April.

Sectoral Growth Trends

1.6 Aided by a favourable monsoons, the agriculture and allied sectors achieved a growth of 4.7 per cent in 2013-14 (Table 1.1), compared to its long-run average of around 3 per cent (between 1999-2000 and 2012-13). However, in some other sectors, slowdown has been more pronounced and protracted. Mining and quarrying

Favourable monsoons helped agricultural growth and power generation. Slowdown in industry continued.

Table 1.1 : Growth in GDP at Factor Cost at Constant (2004-05) Prices (per cent)

Sector	2007-08	2008-09	2009-10	2010-11	2011-12 (2R)	2012-13 (1R)	2013-14 (PE)
Agriculture, forestry, & fishing	5.8	0.1	0.8	8.6	5.0	1.4	4.7
Mining & quarrying	3.7	2.1	5.9	6.5	0.1	-2.2	-1.4
Manufacturing	10.3	4.3	11.3	8.9	7.4	1.1	-0.7
Electricity, gas, & water supply	8.3	4.6	6.2	5.3	8.4	2.3	5.9
Construction	10.8	5.3	6.7	5.7	10.8	1.1	1.6
Trade, hotels, transport, storage, & communication	10.9	7.5	10.4	12.2	4.3	5.1	3.0
Financing, insurance, real estate, & business services	12.0	12.0	9.7	10.0	11.3	10.9	12.9
Community, social, & personal services	6.9	12.5	11.7	4.2	4.9	5.3	5.6
GDP at factor cost	9.3	6.7	8.6	8.9	6.7	4.5	4.7

Source: CSO.
Note: 2R: second revised, 1R: first revised, PE: provisional estimate.

activities have decelerated since 2011-12. Two prominent components of mining, coal and crude petroleum, have stagnated in the last three-four years. Subsequent to an average growth of 7.1 per cent in coal production during the four-year period 2006-07 to 2009-10, its growth declined to an average of 1.6 per cent during the next four years ending 2013-14. The slowdown in coal production partly owes to regulatory issues. The compound annual growth rate (CAGR) of crude petroleum was 1.2 per cent during 2004-05 to 2013-14. As coal and petroleum are universal intermediates, the slack in their production impacted the economy adversely.

1.7 The last two years were particularly disappointing for the manufacturing sector, with growth averaging 0.2 per cent per annum. The decline has been quite broad based, as per data from the index of industrial production (IIP). Decline in the growth rate for basic goods continued for the third year in succession in 2013-14. Output of capital goods declined for the third year in a row starting 2011-12. Contraction of 12.2 per cent in the consumer durables segment was observed in 2013-14. Only intermediate and non-durable consumer goods registered higher growth rate in 2013-14 vis-à-vis 2012-13. Following close to double-digit growth between

Box 1.2 : Trends in Employment

Slowdown in employment growth has been a serious concern in recent years. As per National Sample Survey Office data, the number of persons in the workforce (usual status) increased from 398 million in 1999-2000 to 458 million in 2004-05, an increase of nearly 60 million (nearly equally divided between the agriculture and non-agriculture sectors) or 15 per cent in five years. This increased further to 473 million in 2011-12, an increase of 15 million or 3.3 per cent over a span of seven years.

There was a decline in the workforce in the agriculture and allied sector by over 36 million between 2004-05 and 2011-12. On the other hand, the number of persons in the workforce in the non-agriculture sector increased by 51 million with industry and services contributing nearly 31 million and 20 million respectively. The table below gives the share of different sectors or the sectoral composition of the workforce (employed) by usual principal and subsidiary status (UPSS).

Share of Major Sectors in Total Employment (per cent)

	1999-2000	2004-05	2011-12
Agriculture & allied	59.9	58.5	48.9
Industry	16.4	18.2	24.3
Services	23.7	23.3	26.9

Source: Rangarajan, Seema, and Vibeesh (2014).

Decline in the share of employment in agriculture has been observed in most countries in their development process. Within industry, the bulk of the employment increase was accounted for by construction with an increase of nearly 25 million between 2004-05 and 2011-12. Employment increased by 6 million in the manufacturing sector. The around 20 million increase in employment in the services sector between 2004-05 and 2011-12 was more or less uniformly accounted for by an increase in the trade, hotels, and restaurants sector (4.7 million); transport, storage, and communications (5.4 million); financing, real estate, and business services (5.3 million); and community, social, and personal services (5 million) [Rangarajan, Seema, and Vibeesh (2014)].

In recent years there has also been a decline in the labour force and workforce participation rates of women. A large number of analysts have ascribed this to a rapid increase in female participation in education, both in the rural and urban areas.

Reference

Rangarajan, C., Seema, and E. M. Vibeesh (2014), 'Developments in the Workforce between 2009-10 and 2011-12', *Economic and Political Weekly*, vol. XLIX (23).

2004-05 and 2011-12, the construction sector (that was the major source of employment in this period, as can be seen from Box 1.2) lost momentum in the last two years. Taken together with the trends in capital goods, the slowdown in construction activity reflects subdued business sentiments.

1.8 The data on manufacturing growth during the last two years need to be interpreted with care, given the possibility of revisions by the CSO. The initial estimates of value added in manufacturing sector are based on the IIP, while the second and third revised estimates are based on more detailed data from the Annual Survey of Industries (ASI). For example, as per the National Accounts Statistics, the growth rate of manufacturing for 2011-12 was revised to 7.4 per cent in the second revised estimates (released in January 2014) from 2.7 per cent estimated earlier as ASI data for 2011-12 became available only in the second half of 2013.

1.9 The slowdown in services, in particular the internal trade, transport, and storage sectors, could be attributed to the loss of momentum in commodity-producing sectors. The moderate revival in the global economy may have helped the growth in business services. Bank credit grew by 14.3 per cent in 2013-14, indicating buoyant activity in financial services.

1.10 The disaggregated sectoral trends may be better understood in terms of movement in sectoral shares in GDP, as seen from Table 1.2. The share of the agriculture and allied sectors in GDP has been consistently declining. During the eight years between 1999-2000 and 2007-08, the share of agriculture and allied sectors in GDP declined by 6.4 percentage points, while that of industry and services increased by 1.9 and 4.4 percentage points respectively.

Table 1.2 : Sectoral Share in GDP (per cent)

Sector	1999-2000	2007-08	2012-13	2013-14(P)
Agriculture & allied	23.2	16.8	13.9	13.9
Industry	26.8	28.7	27.3	26.1
Mining & quarrying	3.0	2.5	2.0	1.9
Manufacturing	15.0	16.1	15.8	14.9
Registered manufacturing	9.2	10.7	11.2	NA
Unregistered manufacturing	5.8	5.4	4.5	NA
Services	50.0	54.4	58.8	59.9
Trade, hotels, transport, and communication	21.2	25.9	26.9	26.4
Financing, insurance, real estate, and business services	14.5	16.1	19.1	20.6
Community, social, and personal services	14.4	12.4	12.8	12.9

***Source*:** Calculated from National Accounts Statistics, CSO.
P: Provisional. NA: not available.
***Note*:** Industry includes electricity, gas & water supply and construction sectors that are not indicated in the table.

1.11 The mining and quarrying sector witnessed continuous decline in GDP share for several years, indicating its inability to cater to requirements of high growth, in the absence of comprehensive reforms.

1.12 In the case of manufacturing, most of the gain in share occurred during 2004-05 to 2007-08, when the sector was growing at an annual average rate exceeding 10 per cent, along with robust growth in corporate profits, savings, and investment. Activity was buoyant in registered manufacturing, while the share of unregistered manufacturing remained unchanged during the four years ending 2007-08. During 2008-09 to 2012-13, the share of manufacturing remained roughly constant despite an increase in share of the registered segment, as unregistered manufacturing recorded an average annual growth of only 3.4 per cent.

1.13 The share of services has been consistently rising; more so since 2004-05. However, the pace of expansion was not balanced. The biggest drivers of the service sector expansion since 2004-05 were communications and banking and insurance. Robust growth in these sectors primarily drove the expansion of the services sector even after 2010-11. Real estate and business services also gained share. The services that witnessed stagnation/decline in share after 2010-11 include domestic trade, hotels, and storage. The inability of some of these employment-intensive sectors to attain sustained momentum is one of the reasons for the less-than commensurate growth in employment in services.

Revival of growth in services depends on growth revival in commodity producing sectors. Industrial revival is central to sustained revival in overall growth.

1.14 In the absence of sufficiently high growth in agriculture and industry, services would be seriously constrained to sustain growth acceleration on auto-pilot mode since many of the services are dependent on buoyancy in the commodity-producing sectors, especially industry (Box 1.3).

Box 1.3 : Input flows in the economy

One of the ways to study inter-sectoral linkages is by examining the inter-industry input flow matrix. The table below has been constructed from the latest available input-output tables (2007-08) released by the CSO. The information, though slightly dated, could be indicative of the state of inter-sectoral linkages.

Inter-industry Input Flows in the Economy (in per cent)

	Agriculture and allied sector input	Industrial sector input	Service sector input
Agriculture & allied	55.3	7.7	7.5
Industry	21.4	68.2	45.1
Services	23.3	24.1	47.5

Contribution to Total Inputs in the Economy (in per cent)

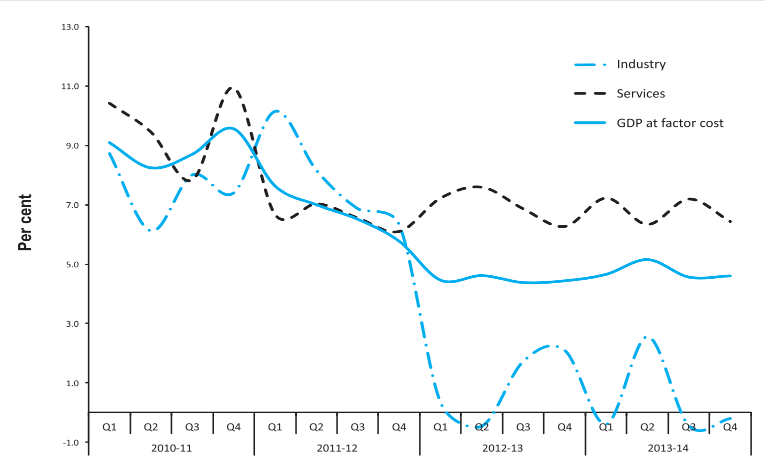
Agriculture & allied	11.8
Industry	59.6
Services	28.6

***Source*:** Internal calculations based on the CSO's input-output tables.

The upper panel of the table implies that out of the total input requirement of the agriculture and allied sector, 55.3 per cent was contributed by the sector itself, while industry and services accounted for 21.4 per cent and 23.3 per cent respectively. More than two-thirds of the total inputs required by industry came from industry itself, while nearly one-fourth were from the services sector. Over half the inputs for the services sector came from the industrial and agricultural sectors. The table highlights the importance of the industrial sector in sustaining economic activity in the services sector. As is evident from the lower panel of the table, the agricultural sector accounted for 11.8 per cent of the total inputs employed in the economy, while the industrial and services sectors accounted for 59.6 per cent and 28.6 per cent respectively. Hence a sustained recovery in the industrial sector is at the heart of a sustained growth recovery.

Quarterly trends

1.15 Quarterly GDP figures can be helpful in detecting inflexion points within the year (Figure 1.2). The current episode of a rather protracted growth deceleration commenced in Q1 2011-12, while the growth slowdown in manufacturing started in Q2 2011-12. The slowdown in mining and quarrying became evident in Q4 2010-11 and this trend continues. Electricity, gas, and water supply witnessed somewhat higher growth in 2013-14 vis-à-vis 2012-13, owing mainly to higher electricity generation from hydel sources on account of improved water availability in reservoirs.



Source: CSO

Figure 1.2 : Quarter-wise Growth in GDP at Factor Cost (2004-05 prices)

Aggregate Demand

Aggregate demand recovered mildly in 2013-14.

1.16 Aggregate demand of the economy comprises final consumption and investment along with net exports (exports minus imports) of merchandise and non-factor services. In national accounting identity, the current account balance maps the difference between domestic savings and domestic investment, which conveys the extent of this gap that needs to be bridged by foreign savings.

1.17 Aggregate demand, measured in terms of GDP at constant (2004-05) market prices, registered a growth of 5.0 per cent in the year 2013-14 as against 4.7 per cent in the previous year. The growth in private final consumption, which averaged 7.8 per cent during 2003-04 to 2011-12, declined to 5.0 per cent in 2012-13 and further to 4.8 per cent in 2013-14. In real terms, fixed investment hardly increased between 2011-12 and 2013-14. In terms of share of GDP, the most striking change on the demand side during 2012-13 and 2013-14 was the precipitous decline in the gross fixed capital formation to GDP ratio by 2.1 percentage points. Thus, the increase in the growth rate of aggregate demand in 2013-14 mainly owes to higher level of net exports (reflected by a reduction in the gap between exports and imports as can be seen in Table 1.3). The major components of aggregate demand are analysed in the sections that follow.

Item	2011-12 (2R)	2012-13 (1R)	2013-14 (PE)
(i) TFCE	68.5	68.8	68.9
Private	57.1	57.1	57.1
Government	11.4	11.8	11.8
(ii) GCF	35.5	34.8	NA
FCF	31.8	30.4	28.3
Change in stocks	1.9	1.7	1.6
Valuables	2.7	2.6	1.5
(iii) Exports	23.9	24.0	24.8
(iv) Less imports	30.2	30.7	28.4

Source: CSO.

Note: TFCE: Total final consumption expenditure, GCF: Gross capital formation, FCF: Fixed capital formation, 2R: second revised, 1R: first revised, PE: provisional estimate.

Sum of (i) to (iv) may not be 100 on account of discrepancies and rounding off.

Table 1.3 : Components of GDP at Current Market Prices and Share in GDP (per cent)

Consumption

1.18 Final consumption expenditure is estimated separately for government and private entities. The share of final consumption in GDP has been declining consistently since the 1950s, reflecting mainly the decline in share of private final consumption expenditure (PFCE). This is not surprising, as higher income levels have led to higher savings by households and reduced the share of consumption. This was also inevitable as higher investment required for raising growth had to come from higher domestic savings given the export pessimism that prevailed till the early 1980s. Despite high oscillations in annual growth, government consumption expenditure as a proportion of GDP has exhibited remarkable consistency since the 1980s (Table 1.4).

Share of private consumption in GDP has declined in recent years.

Table 1.4 : Share of Final Consumption in GDP at Current Market Prices (per cent)

Item	1980s	1990s	2000s	2010-11 to 2013-14
TFCE	85.8	77.5	71.6	68.4
PFCE	74.5	65.9	60.3	56.8
GFCE	11.3	11.6	11.3	11.6

Source: CSO.

Note: Data for 2013-14 is provisional. GFCE is government final consumption expenditure, PFCE is private final consumption expenditure and TFCE is total final consumption expenditure.

1.19 The share of the food items, beverages, and tobacco group in total final consumption in real terms declined by 9.5 percentage points of the GDP in the nine years from 2004-05 to 2012-13. However, in nominal terms (Table 1.5), this decline was only about half of the decline in real terms, reflecting higher inflation for these products during this period.

1.20 Apart from the food, beverages and tobacco group, there was a decline in the share of gross rent, fuel, and power, medical care and health services, and transport and communications, while the largest increase was registered in, other miscellaneous services comprising banking charges, legal services, business services, and life insurance. There has been a progressive inclination towards the consumption of services and a move away from non-durable goods, especially food items.

Table 1.5 : Share of Different Categories of Goods and Services in PFCE in the Domestic Market (per cent of total)

Item	Ratio at current prices 2004-05	2012-13
Food, beverages, & tobacco	40.0	35.2
Clothing & footwear	6.6	7.2
Gross rent, fuel, & power	13.8	13.1
Furniture, furnishing, appliances, & services	3.4	3.9
Medical care & health services	5.0	3.6
Transport & communication	19.3	17.4
Recreation, education, & cultural services	3.0	2.5
Personal care & effects	2.7	3.8
Personal goods n.e.c.	1.6	1.8
Other miscellaneous services	4.7	11.5

Source: CSO

Investment

1.21 Investment comprises fixed capital formation, acquisition of valuables, and changes in stock and inventories, adjusted for errors and omissions. The investment rate (investment to GDP ratio) averaged 24.5 per cent over the period 1990-91 to 2003-04 (Table 1.6). The year 2004-05 marked a break, with the rate of investment exceeding 30 per cent for the first time. Between 2004-05 and 2012-13, the rate of investment averaged 35.4 per cent, reaching the peak of 38.1 per cent in 2007-08. It averaged 35.3 per cent during the higher growth phase of 2004-05 to 2007-08 and 35.5 per cent between 2008-09 and 2012-13. The investment rate of 34.8 per cent in 2012-13 is lower than these two sub-period averages.

Fixed investment rate declined steeply in 2013-14.

1.22 The rate of gross fixed investment, which accounts for the bulk of total investment, increased significantly from 2004-05, peaked in 2007-08, and generally declined thereafter. As per the

Table 1.6 : Components of Investment as Ratios of GDP at Current Market Prices (per cent)

Item		1990-91 to 1999-2000	2000-01 to 2003-04	2004-05 to 2007-08	2008-09 to 2012-13	2012-13	2013-14
I.	Gross fixed capital formation	23.1	24.0	30.8	31.4	30.4	28.3
	Construction	12.1	14.2	16.9	17.7	17.5	NA
	Machinery & equipment	11.0	9.8	13.9	13.8	12.9	NA
(i)	Public sector	8.6	6.7	7.6	7.9	7.8	NA
	Construction	4.7	4.3	5.0	5.3	5.4	NA
	Machinery & equipment	3.9	2.4	2.6	2.7	2.4	NA
(ii)	Private corporate sector	6.7	5.5	11.9	9.8	8.5	NA
	Construction	1.0	1.3	3.5	2.5	2.4	NA
	Machinery & equipment	5.6	4.3	8.4	7.2	6.0	NA
(iii)	Household sector	7.9	11.8	11.3	13.7	14.1	NA
	Construction	6.4	8.6	8.4	9.9	9.7	NA
	Machinery & equipment	1.5	3.2	2.9	3.9	4.4	NA
II.	Change in stocks	0.7	0.5	3.2	2.4	1.7	1.6
III.	Valuables	—	0.7	1.2	2.1	2.6	1.5
IV.	Total investment*	24.3	25.0	35.3	35.5	34.8	NA

Source: Calculated from information contained in National Accounts Statistics, CSO.

Note: * Total investment may not be equal to the sum of the three components because of errors and omissions.

provisional estimates for 2013-14 released by the CSO, the ratio of fixed capital formation to GDP in 2013-14 was 2.1 percentage points lower than in 2012-13. The ratio of valuables to GDP generally increased, even in the period when fixed investment declined, thus keeping the overall rate of investment at around 35 per cent. Changes in stocks are generally subject to wide fluctuations.

1.23 Increase in investment by the private corporate sector explained the bulk of the increase in overall investment during the upswing phase between 2004-05 and 2007-08. The same sector contributed the most to the current decline in investment rate (Table 1.7). (Box 1.4 examines the proximate causes of decline in investment). The growth in investment by the private corporate sector was particularly sharp during 2004-05 to 2007-08, when it averaged 48.1 per cent annually at current prices. The rate of growth declined to 3.4 per cent during 2008-09 to 2012-13. Public-sector investment, which grew at an annual rate of 23.9 per cent in the former period, also slowed subsequently. Household investment growth, in contrast, increased from an annual average of 12.3 per cent during 2004-05 to 2007-08 to an average of 23.5 per cent in 2008-09 to 2012-2013. These patterns of investment by institutions are reflected in Table 1.7.

Reduced private corporate investment rate is the primary reason for decline in overall investment rate.

Table 1.7 : Investment by Type of Institution as a Ratio of GDP at Current Market Prices (per cent)

Sector	1990-91 to 1999-2000	2000-01 to 2003-04	2004-05 to 2007-08	2008-09 to 2012-13	2012-13
Public	8.8	6.8	8.1	8.6	8.1
Private Corporate	7.0	5.6	13.9	11.1	9.2
Household	8.0	12.1	11.9	14.1	14.8
Total investment*	24.3	25.0	35.3	35.5	34.8

Source: CSO.

Note: * Total investment will not be equal to the sum of the three components because of valuables and errors and omissions.

Box 1.4 : Investment Slowdown : Proximate Factors

Is it the nominal or real interest rate that explains the reduction in investment rate? A study entitled 'Real Interest Rate Impact on Investment and Growth- What the Empirical Evidence for India Suggests?', by the RBI, indicates that it is not so much the nominal but real interest rate that explains investment decisions. It is, however, argued by some that, in recent years, investment growth has weakened despite lower *real* interest rates. The study highlights that a lower real interest rate can stimulate investment and growth, provided it is not achieved via higher inflation. The study further suggests that nominal interest rate is, however, more important than real interest rate for investment planning at the firm level.

The RBI study also points to the role of leverage in explaining investment decisions: 'In a highly leveraged sector, such as infrastructure, the required rate of return on equity may remain high but the actual return on equity will be a function of interest costs and cash flows outlook. If interest costs rise and expected cash flow declines, arranging adequate equity capital flow could be difficult, which in turn may lead to shelving of some of planned investment projects.' The decline in cash flows of corporates could also be attributed to (a) sluggish demand conditions, (b) weak pricing power, (c) high input cost, and (d) delays in collection of receivables after delivery of orders.

Part of the slowdown in investment growth post 2007-08 can be attributed to policy uncertainty emanating from difficulties in land acquisition, delayed environmental clearances, infrastructure bottlenecks, problems in coal linkages, ban on mining in selected areas, etc. According to Tokuoka (2012), high and volatile inflation (partly caused by high fiscal deficit) along with heightened global uncertainty may have resulted in slowdown in corporate investment. Slowdown in investment could also be explained in terms of the subdued business environment and bleak business confidence.

Anand and Tulin (2014) suggest that while real interest rates explain aggregate investment activity better than nominal interest rates, they account for only one quarter of the explained investment downturn. They conclude that standard macro-financial variables do not fully explain the recent investment slump and increased uncertainty along with deteriorating business confidence have also played a key role. According to them, lowering nominal interest rates may provide short-term relief from interest burden but, in the medium term, lower rates with little slack in the economy will lead to further inflation, affecting investment adversely. Therefore structural reforms and resolving supply-side bottlenecks are the key to incentivizing investment.

References

1. RBI (2013), 'Real Interest Rate Impact on Investment and Growth — What the Empirical Evidence for India Suggests?' available at www.rbi.org.in.
2. Tokuoka, Kiichi (2012), 'Does the Business Environment Affect Corporate Investment in India?', IMF Working Paper, WP/12/70.
3. Anand, Rahul and V. Tulin (2014), 'Disentangling India's Investment Slowdown', IMF Working Paper, WP/14/47.

1.24 In the high growth phase between 2004-05 and 2007-08, the machinery and equipment segment of fixed investment of the private corporate sector as a ratio of GDP nearly doubled (Table 1.6). Similarly, the ratio of construction also registered a sharp increase.

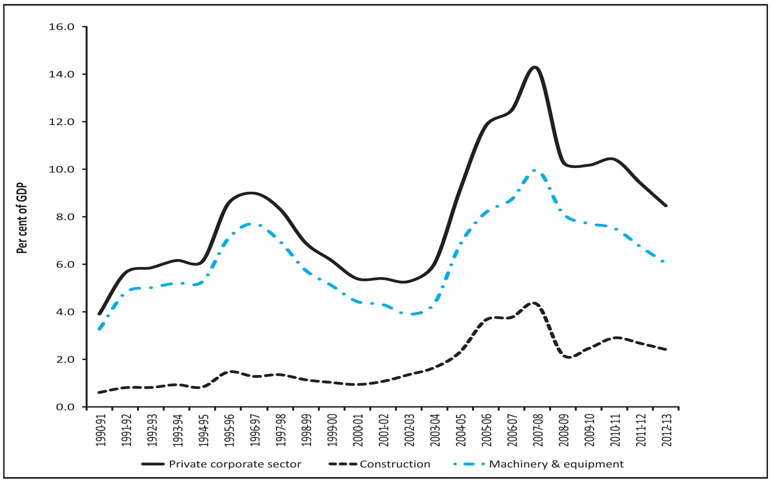


Figure 1.3 : Gross Fixed Investment in Private Corporate Sector and its Components as a Ratio of GDP

Source: CSO.

The decline in fixed investment rate in the last three-four years can be mainly attributed to decline in the share of the machinery and equipment segment of the private corporate sector (Figure 1.3).

1.25 The decline in the construction segment of fixed investment by the private corporate sector (as a ratio of GDP) has been relatively moderate, as against that in the machinery and equipment segment. This could be on account of the fact that the machinery and equipment segment of investment responds relatively more quickly to business sentiments than the construction segment. The long gestation period for construction implies that a project once started/shelved would take longer to stop/revive with change in business sentiments. Investing in machinery and equipment during slowdown may also lead to its underutilization, along with the usual wear and tear (obsolescence). Construction activity is less prone to these problems.

Valuables

1.26 Valuables include assets that are primarily held as store of value. Net acquisition of valuables covers precious articles, gems and stones, silver, gold, platinum, and gold and silver ornaments. Change in aggregate possession of valuables may not have any direct bearing on the productive capacity of the economy.

1.27 Acquisition of valuables has been subject to significant fluctuations in recent years. Their share in GDP increased from 1.2 per cent in 2006-07 to 2.6 per cent in 2012-13 and then declined to 1.5 per cent in 2013-14. The value of imports of gold and silver increased from US$ 42.6 billion in 2010-11 to US$ 55.8 billion in 2012-13. In order to restore stability in the foreign exchange market and reduce the CAD, several measures including hike in import duties on gold and silver were announced by the government in August 2013. These measures resulted in reduction in the combined value of import of gold and silver by about 40 per cent in US dollar terms, which is largely reflected in the decline in share of valuables in the GDP.

Net exports

1.28 Net exports in national accounts are defined as the difference between export of goods and non-factor services and import of goods and non-factor services. Although full-fledged recovery in the global economy is still distant, the early signs of global economic strengthening helped India achieve partial recovery in exports. On the other hand, measures taken by the government and the RBI to contain the CAD, primarily by disincentivizing the import of non-essential items, coupled with economic slowdown, helped in reducing imports. The share of exports in GDP increased from 24.0 per cent in 2012-13 to 24.8 per cent in 2013-14, while the share of imports declined from 30.7 per cent to 28.4 per cent, resulting in an improvement in net exports by 3.1 percentage points of GDP.

Moderate revival of exports, coupled with decline in imports, helped improve net exports.

Public Finance

1.29 In the aftermath of the adoption of the Fiscal Responsibility and Budget Management (FRBM) Act, the fiscal deficit of the centre was brought down to 2.5 per cent of GDP in 2007-08 that was below the threshold target of 3 per cent of GDP. Fiscal balances were deliberately expanded in the aftermath of the global financial crisis in 2008-09 to shore up aggregate demand and raise the growth rate. The gradual fiscal consolidation process was resumed in 2010-11. 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 by 2016-17.

Fiscal consolidation was achieved with lower-than budgeted expenditure in 2013-14.

1.30 The fiscal deficit of 4.5 per cent of GDP in 2013-14 as compared to the budgeted target of 4.8 per cent of GDP is indicative of continued focus on fiscal consolidation. With a shortfall in tax revenues and disinvestment receipts along with higher-than-budgeted subsidies and interest and pension payments, fiscal consolidation was mainly achieved through reduction in expenditure from the budgeted levels.

1.31 The outcome in terms of fiscal deficit of the Centre broadly indicates that despite the macroeconomic uncertainties and elevated global crude oil prices, fiscal targets were achieved. Raising the tax-GDP ratio above the currently prevailing levels is critical for sustaining the process of fiscal consolidation in the long run as compression of expenditure beyond a certain minimum can be counter-productive.

1.32 One of the major factors that has resulted in an increase in the Centre's fiscal deficit after 2008-09 has been the build-up in subsidies. As per the provisional actual figures of the Controller General of Accounts (CGA), major subsidies amounted to ₹ 2,47,596 crore in 2013-14. There has been a sharp increase in total subsidies from 1.42 per cent of GDP in 2007-08 to 2.56 per cent of GDP in 2012-13, and 2.26 per cent of GDP in 2013-14 (RE). Food subsidy has been increasing due to the widening gap between the economic cost of procurement by the Food Corporation of India and the central issue prices fixed for cereals under the public distribution system (PDS). While there has been partial decontrol of fertilizer subsidy, prices of urea are still sticky; similarly petrol prices have been decontrolled and diesel prices are subjected to monthly increases of ₹ 0.50 per litre. The cap set on the number of subsidized LPG cylinders per annum per family was increased from 9 to 12 from April 2014. In addition, leakages contribute substantially to the overall increase in subsidy burden. In the case of food subsidy, the Performance Evaluation Report of the Planning Commission on Targeted PDS (2005) states that for every kilogram of grains delivered to the poor, the GOI released 2.4 kg from the central pool. This has implications for the delivery cost of PDS foodgrains through the existing delivery mechanism.

Raising the tax-GDP ratio and furtherance of subsidy reforms are essential for fiscal consolidation.

1.33 Higher fiscal deficits usually lead to rising public debt. India's central government liabilities-GDP ratio declined from 61.6 per cent in 2002-03 to 49.4 per cent in 2013-14 (RE). The reduction in this ratio owes to higher nominal GDP growth rate vis-à-vis nominal interest rates. Of the total public debt, internal debt constitutes 95.5 per cent, whereas external debt (at book value) constitutes the remaining.

Domestic Savings

1.34 For estimation of gross domestic savings, the economy is classified into three broad institutional sectors, public, private

Table 1.8 : Gross Domestic Savings Rate and its Components as Percentage of GDP at Current Market Prices

Item	1990s	2000s	2007-08	2008-09	2009-10	2010-11	2011-12	2012-13	Historic high*
Gross domestic savings	23.0	30.6	36.8	32.0	33.7	33.7	31.3	30.1	36.8 (2007-08)
Household sector	17.7	23.1	22.4	23.6	25.2	23.1	22.8	21.9	25.2 (2009-10)
Financial	9.6	10.8	11.6	10.1	12.0	9.9	7.0	7.1	12.0 (2009-10)
Physical	8.0	12.3	10.8	13.5	13.2	13.2	15.8	14.8	15.8 (2011-12)
Private corporate sector	3.6	6.3	9.4	7.4	8.4	8.0	7.3	7.1	9.4 (2007-08)
Public sector	1.6	1.2	5.0	1.0	0.2	2.6	1.2	1.2	5.6 (1976-77)

Source: CSO.

Note: * The figure in brackets is the year in which the highest rate was recorded.

corporate, and households. The savings rate increased from 29.0 per cent in 2003-04, the highest achieved till then, to 36.8 per cent in 2007-08, which still remains the historic peak (Table 1.8).

Savings rate has declined significantly since 2007-08.

1.35 From a high of 36.8 per cent, the gross savings rate fell by 6.7 percentage points of the GDP in 2012-13. The bulk of the decline can be attributed to the private corporate and public sectors. While the decline in the former owes mainly to lower growth in the industry sector and lower profit margins, lower public savings to GDP ratio can be attributed to reduced savings of non-departmental public enterprises and greater dis-savings of public authorities. The savings of the household sector are the sum of financial savings and savings in physical assets. The household savings rate had stabilized around an average of 23 per cent of the GDP between 2000-01 and 2006-07 and started fluctuating thereafter. It witnessed strong compositional shifts from financial to physical savings during the period 2007-08 to 2011-12. Net addition to the physical assets of households including investment in construction, machinery and equipment and change in stocks constitutes the saving of households in physical assets. With a significant reduction in the growth of construction activity in 2012-13, physical savings rates by households also declined. The failure of the construction sector to pick up strongly in 2013-14, coupled with sluggishness in machinery and equipment segment indicates that the increase in physical savings of household in the year may have been muted.

In recent years, households tended to save more in physical than in financial assets.

1.36 Retained profits of the private corporate sector adjusted for non-operating surplus/ deficit plus depreciation constitutes its gross savings, which increased sharply after 2002-03 to reach over 9 per cent of the GDP by 2007-08. It was the significant and consistent improvement in corporate profitability that took the private corporate sector savings rate to above 9 per cent in 2007-08 from less than 2 per cent during the 1980s. A study by the RBI on the Performance of Non-Governmental, Non-financial Companies showed that their profit margins deteriorated in 2012-13. This would possibly have affected the savings of the private corporate sector. With negative growth in manufacturing in 2013-14, the savings rate of the private corporate sector is unlikely to have revived.

1.37 The trends in macroeconomic variables discussed above have implications for other variables too, viz. inflation, balance of payments, etc. These are discussed below.

Prices and Monetary Management

Inflation

1.38 The average headline WPI inflation moderated to a four-year low of around 6 per cent in 2013-14 after averaging 8.6 per cent in the previous three years, with the contribution of the non-food segment moderating significantly on the back of the fall in global commodity prices. However the pressure from domestic food items remained elevated. WPI inflation remained below 5 per cent in the first quarter of 2013-14. However, higher inflation in vegetables and cereals led to a spike, with headline inflation reaching 6.6 per cent and 7.1 per cent respectively in the second and third quarters. With some moderation in cereals inflation and correction in vegetable prices, headline inflation declined to 5.4 per cent in the last quarter of 2013-14. Inflation in non-food manufactured products (core inflation) remained benign throughout the year and moderated to a four-year low of 2.9 per cent in 2013-14. This indicates that the underlying pressures of broad-based inflation may have somewhat eased.

1.39 Inflation in terms of the new series of consumer price index (CPI) (combined) remained fairly sticky at around 9-10 per cent owing to higher food inflation in the last couple of years. However, the headline CPI inflation started moderating after December 2013 and declined to a 25-month low of 8.0 per cent in February 2014, following moderation in inflation for vegetables and egg, meat, and fish. On the other hand, CPI inflation excluding food and fuel, remained sticky due to higher inflation in services-led components such as medical, education, household requisites, etc.

Major contributors to headline WPI inflation

1.40 The level of inflation and its movement across major sub-groups varied significantly over the eight quarters up to Q4 of 2013-14. In 2013-14 inflation was chiefly confined to food and fuel, which contributed nearly two-thirds of overall inflation. High inflation in the last few years, particularly food inflation, has been the result of structural and seasonal factors. While inflation in food articles remained persistent, its drivers have been changing over time. For example, cereals and protein items were the main

Food inflation has been much higher than non-food inflation.

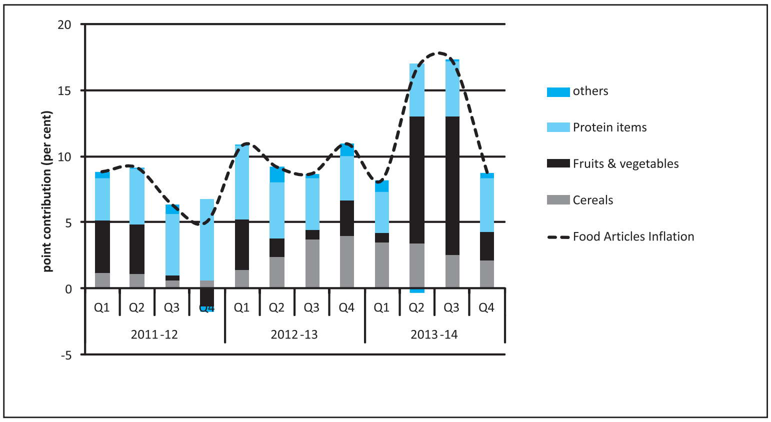


Figure 1.4 : Major Drivers of Food Articles Inflation

Source: Office of the Economic Adviser, DIPP.

contributors to food inflation in Q1 of 2013-14, while vegetables, especially onions, pushed up food inflation in Q2 and Q3 (Figure 1.4). Within the food group, the contribution of the commodity sub-groups, fruits and vegetables and egg, meat and fish has been high. Inflation in these protein-based items is on account of increase in share of consumption of these items arising from growing income levels.

1.41 Food inflation partly owes to large wastage of food articles in the supply chain owing to inefficiencies in distribution channels. The provisions of the State Agricultural Produce Marketing Committee (APMC) Acts have prevented creation of competitive conditions in the distribution of commodities and creation of a national market for agricultural commodities. Multiple layers of intermediation in the distribution of food articles have also pushed up prices for consumers. It is therefore necessary to focus on distribution channels and on reducing food wastage in the supply chain. Significant investment in marketing infrastructure, including modern warehouses, cold storages, reefer vans, scientific packaging, and handling would help strengthen distribution channels. State governments will have to play a vital role in removing restrictive provisions in the APMC Act and proactively promoting alternative trading options for farmers.

1.42 Fuel inflation remained in double digits in the last three quarters. A major reason for high inflation in fuel and power items was the rationalization of tariff for electricity in many states, in addition to the policy of allowing greater pass-through in diesel prices and depreciation of the Indian rupee against the US dollar.

Outlook for Inflation

1.43 Forecasts by the IMF expect international commodity prices to remain benign. This should help in moderation of WPI headline inflation. However, the major risk arises from sub-normal monsoons during 2014-15 on account of the El Nino effect and higher prices of oil due to the geo-political situation in the Middle East. The decisions of the government regarding subsidy on inputs for agriculture including fertilizer and increase in the minimum support prices (MSP) could also have an impact on food inflation.

Monetary Developments

1.44 Gradual monetary easing that had started alongside some moderation in inflationary pressures at the beginning of 2013-14 was disrupted by the need to stabilize the foreign exchange market. In May 2013, there were indications of tapering of quantitative easing by the US Federal Reserve. The surge in capital outflows that followed, resulted in sharp depreciation of the rupee. To restore stability in the foreign exchange market, the RBI hiked interest rates and compressed domestic money market liquidity.

1.45 Measures taken in mid-July 2013 included a 200 basis points (bps) hike in the marginal standing facility (MSF) rate to 10.25 per cent; cap on daily Liquidity Adjustment Fund (LAF) borrowing to 0.5 per cent of net demand and time liabilities (NDTL) of respective banks; and a hike in the minimum daily cash reserve ratio (CRR) requirement to 99 per cent from 70 per cent. Weekly auctions of cash management bills were also conducted to drain out liquidity. These measures raised the call rate to the level of the MSF rate, making the latter the effective policy rate.

1.46 Following the ebbing of volatility in the foreign exchange market, the RBI initiated normalization of the exceptional measures in a calibrated manner since the mid-quarter review of 20 September 2013. The interest rate corridor was realigned to normal monetary policy operations with the MSF rate being reduced in three steps to 8.75 per cent between 20 September 2013 and 29 October 2013 even as the repo rate was increased in two steps of 25 bps each to 7.75 per cent to contain inflation and inflation expectations. Minimum daily CRR balance maintained by banks was reduced to 95 per cent of the requirement from 99 per cent to provide banks with the flexibility to better manage liquidity. As an additional liquidity-enhancing measure and for developing the term money market, the RBI introduced weekly variable-rate term repos of 7-day and 14-day tenors for an amount equivalent to 0.25 per cent of the NDTL of the banking system.

1.47 The RBI in the Third Quarter Review of Monetary Policy on 28 January 2014 hiked the repo rate by 25 bps to 8 per cent on account of upside risks to inflation. The move was intended to set the economy securely on a disinflationary path. In the second bimonthly Monetary Policy Statement 2014-15, on 3 June 2014, the RBI kept the Policy Repo rate unchanged at 8 per cent and reduced the statutory liquidity ratio by 50 bps from 23 per cent to 22.5 per cent. The RBI thus expects banks to reduce their government securities holdings, allowing them to lend more to the private sector.

Tight monetary policy stance was followed by RBI for containing inflation and restoring stability in the foreign exchange market.

1.48 Liquidity conditions remained tight during the first half of 2013-14, mainly reflecting policy intent to stabilize the foreign exchange market. Money markets remained in orderly condition during Q1 of 2013-14 with the call rate hovering within the corridor set by the reverse repo and MSF rates and remaining close to the policy (repo) rate. However the exceptional measures taken by the RBI during July and August 2013 to contain exchange rate volatility impacted the money market, and consequently the money market rates exceeded the corridor.

International Trade, Balance of Payments, and External Debt

International Trade

1.49 India's share in world exports and imports increased from 0.7 per cent and 0.8 per cent respectively in 2000 to 1.7 per cent and 2.5 per cent respectively in 2013. There has also been marked improvement in India's total merchandise trade to GDP ratio from 21.8 per cent in 2000-01 to 44.1 per cent in 2013-14.

1.50 India's merchandise exports reached US$ 312.6 billion (on customs basis) in 2013-14, registering a growth of 4.1 per cent as compared to a contraction of 1.8 per cent during the previous year. In April-May 2014, exports registered a growth of 8.9 per cent over the corresponding period of 2013. Exports of petroleum products, engineering goods, chemicals and related products accounted for more than half of total exports in 2013-14. The value of imports declined by 8.3 per cent in 2013-14 as compared to 2012-13, owing to a 12.8 per cent fall in non-oil imports. The value of imports of petroleum, oil, and lubricants (POL) increased by 0.7 per cent in 2013-14. Imports of gold declined from 1078 tonnes in 2011-12 to 1037 tonnes in 2012-13 and further to 664 tonnes in 2013-14, on account of several measures taken by the government. In value terms, gold and silver imports fell by 40.1 per cent to US$ 33.4 billion in 2013-14. The sharp decline in imports and a moderate growth in exports in 2013-14 resulted in a decline in India's trade deficit to US$ 137.5 billion from US$ 190.3 billion during 2012-13, contributing to a lower CAD.

Services Trade

1.51 Services exports registered a growth of 4 per cent in 2013-14 as against 2.4 per cent in 2012-13. Surplus in services trade (net services) has been a major source of financing India's growing merchandise trade deficit in recent years. During 2006-07 to 2012-13, this surplus on an average financed around 38 per cent of merchandise trade deficit. While in 2012-13, net services financed 33.2 per cent of the merchandise trade deficit, during 2013-14, with moderate growth in services exports and fall in their imports, net services financed nearly half of merchandise trade deficit.

Balance of Payments

1.52 India's Balance of Payments (BoP) position improved significantly in 2013-14, particularly in the last three quarters. The stress on BoP observed during 2011-12 as a fallout of the crisis in the Euro area and inelastic domestic demand for certain key imports continued through 2012-13 and the first quarter of 2013-14. The CAD rose sharply to a high of US$ 88.2 billion (4.7 per cent of GDP) in 2012-13, surpassing the 2011-12 level of US$ 78.2 billion. After being at perilously unsustainable levels in 2011-12 and 2012-13, the improvement in BoP position in 2013-14 is a relief. However, the outcome in 2013-14 was mixed: high levels of CAD in the first quarter followed by gradual correction thereafter; broadly adequate financing through capital flows till May 2013; a sharp correction in June-August 2013 followed by a surge in September-November 2013. The correction in June-August 2013 was on account of market fears of an imminent tapering of asset purchases by the US Fed. The subsequent surge in flows owed to the special swap windows incentivized by the RBI for non-resident deposits and the overseas borrowing programme of banks.

Demand slowdown and restrictions on non-essential imports resulted in reduced trade deficit and lower CAD.

1.53 Widening of the CAD in 2012-13 could largely be attributed to rise in trade deficit arising from weaker exports and relatively stable imports. The latter owed to India's dependence on crude petroleum imports and elevated level of gold imports since the onset of the global financial crisis. While the financing of the high CAD was adequate and in line with the general trend prior to the 2008 crisis, the inadequacy during 2011-12 and since May 2013 indicated that beyond the threshold level of CAD, financing could be a problem. This is because the post-2008 crisis period is characterized by excessive risk aversion, that has implications for capital flows and the exchange rate of the rupee.

1.54 The government moved swiftly to correct the situation through restrictions in non-essential imports like gold; custom duty hike in gold and silver to a peak of 10 per cent; and measures to augment capital flows through quasi-sovereign bonds and liberalization of external commercial borrowings. The RBI also put in place a special swap window for foreign currency non-resident deposit (banks) and banks' overseas borrowings, through which US$ 34 billion was mobilized. These measures led to a turnaround in the BoP position in the latter three quarters and for the full fiscal 2013-14. With higher exports and lower imports, there was a reduction in trade deficit to 7.9 per cent of GDP in 2013-14 from 10.5 per cent in 2012-13.

1.55 Out of the total reduction of US$ 48.0 billion in trade deficit on BoP basis in 2013-14, reduction in import of gold and silver contributed approximately 47 per cent, reduction of non-POL and non-gold imports constituted 40 per cent, and higher exports constituted 25 per cent. Higher POL and non-DGCI&S (Directorate General of Commercial Intelligence and Statistics) imports contributed negatively to the reduction to the extent of 12 per cent in 2013-14 over 2012-13.

1.56 Net invisibles' surplus remained stable at US$ 28-29 billion per quarter resulting in overall net surplus of US$ 115.2 billion for 2013-14. Software services improved modestly from of US$ 63.5 billion in 2012-13 to US$ 67.0 billion in 2013-14. Non-factor services increased from US$ 64.9 billion in 2012-13 to US$ 73.0 billion. This was partly on account of business services turning positive with net inflows of US$ 1.3 billion in 2013-14 as against an outflow of US$ 1.9 billion in 2012-13. Thus the CAD moderated to US$ 32.4 billion in 2013-14 as against US$ 88.2 billion in 2012-13. The CAD at 1.7 per cent of GDP in 2013-14, compares favourably with the levels in the pre-2008 crisis years.

Capital flows moderated, but foreign exchange reserves increased in 2013-14.

1.57 Capital flows (net) moderated sharply from US$ 92.0 billion in 2012-13 to US$ 47.9 billion in 2013-14. This decline essentially reflects slowdown in portfolio investment and net outflow in 'short-term credit' and 'other capital'. However, there were large variations within quarters partly due to domestic and partly to external factors. The move to augment capital inflows through special swap windows resulted in copious inflows of about US$ 34 billion.

1.58 These inflows in tandem with the lower level of CAD led to reserve accretion in 2013-14. Foreign exchange reserves were placed at US$ 304.2 billion at end march 2014 as against US$ 292.0 billion at end March 2013. Thus foreign exchange reserves in nominal terms increased by US$ 12.2 billion as against a reserve accretion of US$ 15.5 billion on BoP basis at end March 2014. The difference owed to valuation loss in the non-US dollar assets held due to cross-currency movements and the decline in gold prices. On June 20, 2014, foreign exchange reserves stood at US$ 314.9 billion.

1.59 In 2013-14, the rupee started to depreciate in May 2013. Depreciation was more pronounced in June and August 2013—in excess of 5 per cent on a month-on-month basis. The average exchange rate declined to a level of ₹ 63.75 per US dollar in September 2013. Thereafter, owing to the measures taken to reduce CAD and boost capital flows, the rupee rebounded to reach an average level of ₹ 61.62 per US dollar in October 2013. Subsequently, the rupee was range bound and stable in 2013-14. The exchange rate thus far in 2014-15 reflects similar pattern as in the latter half of 2013-14, with the surge in foreign institutional investment (FII) flows impacting the foreign exchange and equity markets favourably; but the rupee appreciation has been limited relative to the rise in equity indices.

External Debt

1.60 The one-off mobilization of deposits by the RBI had implications for India's external debt. India's external debt stock at end March 2013 stood at US$ 404.9 billion as against US$ 360.8 billion at end March 2012. This increased further to US$ 426.0 billion at end December 2013. India's external debt consists predominantly of long-term borrowings and has remained within manageable limits owing to prudential restrictions on debt varieties of capital inflows given large interest differentials.

Priorities for Reviving Growth

Priorities for growth revival include: investment revival, strengthening of macro-economic stability, creation of non-agricultural jobs, strengthening of infrastructure, and boost to agricultural development.

1.61 With the twin deficits reasonably under check, the macroeconomic outcomes of slow growth and inflationary pressures require immediate attention. Short-term stabilization apart, the focus of policy should be on wide-ranging structural reforms to ease supply-side constraints and sector-specific incentives to boost demand. Some specific priorities, with the objective of restoring growth, are outlined.

- Revival of investment is crucial for raising the growth rate. This requires acceleration in project clearances and streamlining of implementation procedures, apart from sector-specific investment policies.
- Over the medium term, structural reforms that boost productivity are crucial for sustaining higher growth.
- Linked to efforts at investment revival are policies needed for rejuvenating growth in manufacturing, which has significant backward and forward linkages. Simplification of tax policy and administration, repeal of archaic laws that govern market access, expansion and entry/exit of firms, revamp of the dispute resolution mechanism for commercial disputes, etc. would lend greater predictability to policy. An environment of policy certainty, continuity, and transparency, will help boost business sentiments further.
- Strengthening macroeconomic stability, a non-negotiable instrument for stable and faster growth, is predicated on fiscal discipline, manageable current account balance, and price stability. Policy challenges include:
    - keeping fiscal deficit in check without compromising on capital expenditure;

- maintaining the CAD in the range of 2-2.5 per cent of GDP. This may turn out to be challenging if non-oil imports revive upon growth revival and oil prices harden. Therefore, policies that help in sustained export growth remain relevant.
- stepping up efforts to further reduce inflation not only to counter the direct macroeconomic consequences but to provide leeway to the RBI for monetary easing and to counter external challenges more effectively.

- To harness the demographic dividend, the non-agrarian sector must generate employment. With the agrarian sector still employing the bulk of the workforce, policy attention needs to be focused on the rural non-farm sector, manufacturing sector, and labour-intensive segments of services.
- Physical and social infrastructure, both urban and rural, that can accommodate and fuel robust growth, is central to regaining and sustaining economic momentum.
- Sustained and high overall economic growth is possible with the farming sector growing at around 4 per cent per annum. This requires a boost to investment and productivity in the sector, crop protection and insurance, and a fresh look at policies towards procurement, marketing, transport, storage, and processing.

Outlook for 2014-15

1.62 The descent into the present phase of sub-5 per cent growth has been rather sharp. The interplay of structural constraints alongside delays in project implementation, subdued domestic sentiments, and an uncertain global milieu led to general growth slowdown while rendering macroeconomic stabilization particularly challenging. Inflation also remained at elevated levels. These factors triggered risk-aversion and injected considerable uncertainty in investment activity. The current macroeconomic situation precludes fiscal stimulus to kick-start activity. Similarly, the task of monetary policy calibration for growth revival has been made difficult by persistent inflation and further complicated by uncertainty in international financial conditions and, until recently, by rupee depreciation. Targeted measures by the government and RBI have improved the external economic situation significantly, even as India remains exposed to risk on/off sentiments of investors and to policy shifts in advanced economies. Regaining growth momentum requires restoration of domestic macroeconomic balance and enhancing efficiency. To this end, the emphasis of policy would have to remain on fiscal consolidation and removal of structural constraints. Though some measures have been initiated to this end, reversion to a growth rate of around 7-8 per cent can only occur beyond the ongoing and the next fiscal.

> Despite some measures undertaken to address structural constraints, reversion to a growth rate of around 7–8 per cent can only occur beyond the ongoing and the next fiscal.

1.63 Global economic activity is expected to strengthen in 2014-15 on the back of some recovery in advanced economies. The Euro area is also expected to register a growth rate of above 1 per cent as against contraction witnessed in 2012 and 2013 (IMF, WEO, April 2014). The European Central Bank's monetary policy measures, most significantly introduction of the negative deposit facility interest rate are expected to boost economic activity in Europe. In addition, the performance of the real sector in the US (that is likely affect the pace of taper) is a major factor that would impact the global economic situation in 2014-15. The growth outlook for emerging Asian economies is generally benign with some grappling with inflation, structural bottlenecks, and external imbalances. The slowdown in emerging economies comes at an inopportune juncture.

1.64 Downward movement along with heightened volatility, witnessed, for example, in fixed investment post 2008-09 in India, often tends to magnify the impact and transmission channels of shocks (e.g. below-normal monsoons and/or upshot in oil prices) and hampers build-up of positive expectations. Under such circumstances, the Indian economy can recover only gradually with the GDP at factor cost at constant prices expected to grow in the range of 5.4 – 5.9 per cent in 2014-15. This assumes the revival of growth in the industrial sector witnessed in April 2014 to continue for the rest of the year, the generally benign outlook on oil prices (notwithstanding the uncertainty on account of recent developments in the Middle East), and the absence of pronounced destabilizing shocks (including below-normal monsoons). Growth in the above range implies a pick-up, aided by an improved external economic situation characterized by a stable current account and steady capital inflows, improved fiscal situation and, on the supply side, robust electricity generation and some recovery in manufacturing and non-government services.

With expectation of better performance in manufacturing, improved balance of payments situation and modest global growth revival, the economy is expected to grow in the range of 5.4-5.9 per cent in 2014-15.

1.65 Growth in 2014-15 is expected to remain more on the lower side of the range given above, for the following reasons: (i) steps undertaken to restart the investment cycle (including project clearances and incentives given to industry) are perceived to be playing out only gradually; (ii) the benign growth outlook in some Asian economies, particularly China; (iii) still elevated levels of inflation that limit the scope of the RBI to reduce policy rates; and (iv) expectation of below-normal monsoons. Downside risk also emerges from prolonging of the geo-political tensions. On the upside, such factors as institutional reform to quicken implementation of large projects and a stronger-than-expected recovery in major advanced economies would help the Indian economy clock a higher rate of growth.

Sectoral Developments

1.66 In what follows, major sectoral issues and developments are outlined. These developments have fed into the macroeconomic scenario that has been presented in the previous sections.

Agriculture and Food Management

1.67 Substantial strides in agricultural production have been made in the last few years. There was an increase of around 40 lakh ha in overall area coverage under foodgrains in 2013-14 as compared to 2012-13. A record foodgrains production of 264.4 million tonnes is estimated in 2013-14, as per the third Advance Estimates, indicating

The year 2013-14 witnessed record foodgrains production.

an increase of more than 20 million tonnes over the average production during the previous five years. Horticulture production is estimated at 265 million tonnes in 2012-13 and for the first time has exceeded the production of foodgrains and oilseeds.

1.68 The robustness of the agriculture and allied sector can be attributed to the steady increase in gross capital formation (GCF) in this sector (both public and private) as a percentage of its GDP, from 14.9 per cent in 2006-07 to 21.2 per cent in 2012-13 (2004-05 prices). However, the share of public expenditure (comprising public investments and input subsidies) in total GCF of the agriculture and allied sector declined from 25 per cent in 2006-07 to 14.7 per cent in 2012-13. Private investment as a proportion of agri-allied GDP increased from 12.6 per cent in 2007-08 to 18.1 per cent in 2012-13.

1.69 In the monsoons for 2014-15, there are concerns about the likely occurrence of the El Niño, when surface temperatures in the Pacific Ocean continuously rise above average for several months which adversely affects weather in many regions. This is likely to have an impact on India's agriculture and consequently on food prices. With 60 per cent of the total foodgrains and oilseeds produced being grown in the kharif season, and with just about 35 per cent of arable area being irrigated, Indian agriculture is still largely dependent on rainfall. The south-west monsoon (from June to September) accounts for nearly 75 per cent of total annual rainfall in India. The forecast released in June 2014 by the IMD indicates that there is a 71 per cent probability of a sub-normal / deficient south-west monsoon with a 70 per cent probability of occurrence of El Niño. However, the extent of impact of El Niño depends on temporal and spatial distribution of rainfall. A comparison of the rainfall distribution across 36 meteorological subdivisions and districts upto 11 June in the last five years shows that rainfall distribution is the worst this year. However, storage position of water reservoirs is better than the last year and the average of the last ten years.

1.70 Expansion in area and increase in MSPs of select agricultural crops, inter alia, have resulted in higher foodgrains production. Owing to higher procurement, there are huge stocks of foodgrains in the central pool, which as on 1 June 2014, was 77.7 million tonnes. The per capita net availability of foodgrains increased to 186.5 kg per year in 2013 from 162.1 kg per year in 2009 and the net availability of edible oils from 12.7 kg per year to 15.8 kg per year.

1.71 While the production estimates highlight the continued robustness of Indian agriculture, some concerns remain. Productivity levels in Indian agriculture are still much lower than global standards. Productivity levels of rice and wheat have not risen significantly after the 1980s. While cotton yields have shown tremendous leap over the last decade, largely due to the adoption of Bt cotton; some increase is also seen in coarse cereals and pulses. Without new technology and quality inputs, desired productivity levels would be difficult to achieve. Soil degradation owing to declining efficiency of fertilizer use and alarming reduction in the water table, especially in Punjab and Haryana due to their cropping pattern, are other major concerns. There is a need to review the

Productivity levels of rice and wheat have not increased significantly after the 1980s.

nutrient based subsidy (NBS) policy, which does not have urea under its purview.

1.72 The pricing of subsidized fertilizers has resulted in their higher usage. The recommendation of the Task Force for Direct Transfer of Subsidy to shift to a system of direct transfer of fertilizer subsidy to farmers in a phased manner needs to be considered. The Crop Diversification Scheme has been introduced in the Punjab and Haryana region and is expected to promote technological innovations and encourage farmers to choose crop alternatives. The predominance of small and marginal farms in India's agriculture, with limited capital availability, hampers progress of farm mechanization.

1.73 Domestic and international marketing of agricultural commodities needs immediate attention. A plethora of government interventions for building marketing set up has in fact created barriers to trade. There is need to facilitate a National Common Market for agricultural commodities with uniform taxes in the domestic market, and to foster a long-term stable trade policy for agricultural products.

1.74 There is need to expand the adoption of the decentralized system of procurement for the PDS from 11 states and union territories (UT) at present to all states. This would help save transport costs, reduce transit losses and other leakages, increase food availability, reduce food prices in the open market and ultimately rein in food subsidy.

Industry and infrastructure

1.75 As per the latest GDP data, the industry sector registered a growth of 1.0 per cent in 2012-13 that slowed further to 0.4 per cent in 2013-14. The key reason for poor performance was contraction in mining and deceleration in manufacturing. Manufacturing- and mining-sector GDP declined by 0.7 per cent and 1.4 per cent respectively in 2013-14. The underlying cause for this has been the deceleration in investment particularly by the private corporate sector during 2011-12 and 2012-13.

Mining output contracted for the third successive year in 2013-14.

1.76 As per IIP data, mining output contracted for the third successive year in 2013-14, declining by 0.6 per cent. Natural gas production plummeted mainly owing to declining production from the KG-6 basin. Electricity generation increased by 6.1 per cent in 2013-14 as compared to 4.0 per cent in the previous year, mainly on account of significant capacity addition in recent years.

1.77 Slowdown in construction resulted in capacity under-utilization in the steel and cement sectors. Steel and cement consumption increased by 0.6 per cent and 3.0 per cent respectively in 2013-14. The capital goods segment has been among the weakest performers in the manufacturing sector. Its index declined by 6.0 per cent in 2012-13 and further by 3.6 per cent in 2013-14.

1.78 For eight 'core' industries—coal, fertilizer, electricity, crude oil, natural gas, refinery products, steel, and cement—the average growth rate declined from 6.5 per cent during 2012-13 to 2.7 per cent during in 2013-14. The moderation in growth occurred mainly on account of contraction in natural gas and crude oil, and subdued growth in coal, fertilizers, and refinery products.

1.79 Continuing slowdown has impacted the performance of the corporate sector. Growth of sales, particularly of the listed private manufacturing companies, declined from 24.9 per cent in Q1 2011-12 to 4.5 per cent in Q3 2013-14. Capacity utilization (CU) remained largely flat in Q3 of 2013-14. Thus, the finished goods inventory to sales ratio also declined in Q3 of 2013-14 over the previous quarter.

Slowdown in industry was reflected in lower sales growth in the corporate sector.

1.80 Of the total 239 central infrastructure projects costing ₹ 1000 crore and above, 99 are delayed with respect to the latest schedule and 11 have reported additional delays vis-à-vis the date of completion reported in the previous month (Flash Report for February 2014, Ministry of Statistics and Programme Implementation [MOSPI]). The additional delays are in the range of 1 to 26 months in projects relating to the petroleum, power, steel and coal sectors.

1.81 Among infrastructure services, growth in freight traffic by railways, cargo handled by major ports, and the civil aviation sector (except import cargo) has been comparatively higher during 2013-14. In the road sector, construction of national highways by the National Highways Authority of India (NHAI) posted negative growth of 33 per cent during 2013-14 vis-a-vis a growth of 26.5 per cent during 2012-13.

1.82 Gross bank credit flow to industry increased by 14.9 per cent in 2013-14 as against 17.8 per cent in 2012-13. Credit flow to mining remained nearly stagnant with 0.05 per cent growth during 2013-14. In keeping with the performance of the power sector during 2013-14, credit flow to the sector increased by 24.9 per cent. Petroleum, chemicals and chemical products, basic metals, transport, and all engineering sectors registered lower growth in gross bank credit flow during 2013-14 compared to the previous year. The rate of growth of bank credit to major infrastructure sectors moderated from an average of 44.8 per cent in 2011-12 to 17.7 per cent in 2013-14. The telecom sector witnessed consecutive decline in the last three years.

Growth of credit flow to industry was lower in 2013-14.

1.83 Total foreign direct investment (FDI) inflows into major infrastructure sectors registered a growth of 22.8 per cent in 2013-14 as compared to the contraction of 60.9 per cent during 2012-13. In recent years, services, construction, telecommunications, computer software and hardware, drugs and pharmaceuticals, automobile industry, power, metallurgical industries, and hotels and tourism sectors have attracted maximum FDI inflows.

Services Sector

1.84 The services sector has emerged as the fastest growing sector of the economy and the second fastest growing in the world, with a CAGR of 9 per cent, behind China with a CAGR of 10.9 per cent during the period from 2001 to 2012. Services have also contributed substantially to foreign investment flows, exports, and employment. The share of the services sector in employment increased from 19.7 per cent in 1993-94 to 26.9 per cent in 2011-12.

1.85 Like industry, services also slowed during the last two years. The deceleration in growth was particularly sharp in the combined category of trade, hotels & restaurants and transport, storage, and communications. However, robust growth continued in financing, insurance, real estate, and business services.

Financial Intermediation

1.86 Financial reforms are critical to the emergence of India as a strong market economy. A well-functioning financial system will support growth, financial inclusion and stability. The passage of the Pension Fund Regulatory and Development Authority (PFRDA) Act, the shift of regulatory supervision of commodity futures trading to the Ministry of Finance, and the presentation of the Financial Sector Legislative Reforms Commission (FSLRC) report, are some of the major developments in 2013-14.

1.87 The Indian banking sector, which exhibited considerable resilience in the immediate aftermath of the global financial crisis, has been impacted by the global and domestic economic slowdown over the last two years. During 2012-13, the deteriorating asset quality of the banking sector emerged as a major concern, with gross non-performing assets (NPAs) of banks registering a sharp increase. Overall NPAs of the banking sector increased from 2.36 per cent of total credit advanced in March 2011 to 3.90 per cent of total credit advanced in March 2014 (provisional). As a consequence of the slowdown and high levels of leverage, some industry and infrastructure sectors, namely textiles, chemicals, iron and steel, food processing, construction, and telecommunications, are experiencing a rise in NPAs. The RBI in the Financial Stability Report (December 2013) identified five sectors—infrastructure, iron and steel, textiles, aviation and mining—as stressed sectors. Public sector banks (PSBs) have high exposures to the 'industry' sector in general and to such 'stressed' sectors in particular.

1.88 The New Pension System (NPS), now National Pension System, was introduced for the new recruits joining government service on or after January 2004. It represents a major reform of Indian pension arrangements, and lays the foundation for a sustainable solution to ageing in India by shifting to an individual account, defined-contribution system. Till 7 May 2014, a total of 67.41 lakh members have been enrolled under the NPS with a corpus of ₹ 51,147 crore. From 1st May 2009, the NPS was opened up for all citizens in India to join on a voluntary basis. The Swavalamban Scheme for workers in the unorganized sector launched in 2010, initially for three years for the beneficiaries who enrolled themselves in 2010-11, has now been extended to five years for the beneficiaries enrolled in 2010-11, 2011-12, and 2012-13 and thus the benefits of co-contribution under the Scheme would be available till 2016-17.

1.89 With a view to revamping financial-sector laws to bring them in tune with current requirements, the government set up the FSLRC on 24 March 2011. The Commission in its Report has given wide-ranging recommendations, both legislative and non-legislative, on the institutional, legal, and regulatory framework and operational changes in the Indian financial sector. The draft Indian Financial Code (IFC) that has been proposed by the FSLRC has provisions that aim at replacing a large numers of existing financial laws. The FSLRC has designed a modified financial regulatory architecture, which would increase accountability by achieving clarity of purpose for each organization and avoid conflicts of interest. The modified arrangements also facilitate achieving economies of scope and scale of related activities, for the private sector and for the government.

1.90 In the 8th meeting of the Financial Stability and Development Council (FSDC), held on 24 October 2013, the Council decided that Regulators would voluntarily adopt governance-enhancing recommendations that do not require legislative changes. This initiative has translated into a handbook on voluntary adoption of non-legislative governance-enhancing aspects of the draft Indian Financial Code, and a MIS statement which tracks compliance.

1.91 Implementing the IFC will also require establishing many new organisations. The FSDC decided to initiate institution-building for four new organizations: the Resolution Corporation (RC) which will detect and deal with distressed financial firms; the Public Debt Management Agency which will manage the domestic and overseas borrowing for the government; the Financial Sector Appellate Tribunal which will hear appeals against financial agencies; and the Financial Data Management Centre which will be a database within the FSDC. These are likely to enable a holistic view of the Indian financial system.

Human Development

1.92 India with a large and young population has a great demographic advantage. The proportion of working-age population is likely to increase from approximately 58 per cent in 2001 to more than 64 per cent by 2021. While this provides opportunities, it also poses challenges. Policymakers have to design and execute development strategies that target this large young population. Demographic advantage is unlikely to last indefinitely. Therefore timely action to make people healthy, educated, and adequately skilled is of paramount importance.

1.93 According to the United Nations Human Development Report (HDR) 2013, India with a human development index (HDI) of 0.554 in 2012 slipped down the global ranking to 136 from 134 as per HDR 2012. India is in the medium human development category with countries including China, Egypt, Indonesia, South Africa, and Vietnam having better overall HDI ranking within the same category. The existing gap in health and education indicators in India as compared to developed countries and many developing countries calls for much faster spread of basic health and education. Life expectancy at birth in India was 65.8 years in 2012, compared to 75.1 years in Sri Lanka and 73.7 years in China. The expenditure on social services by the government as a percentage of GDP has increased from 6.8 per cent in 2008-09 to 7.2 per cent in 2013-14 (BE) with expenditure on education increasing from 2.9 per cent to 3.3 per cent and on health from 1.3 per cent to 1.4 per cent.

Unless timely action is taken, the potential for reaping the demographic dividend is unlikely to last indefinitely.

1.94 The poverty ratio declined from 37.2 per cent in 2004-05 to 21.9 per cent in 2011-12. In absolute terms, the number of poor declined from 407.1 million in 2004-05 to 269.3 million in 2011-12. During 2004-05 to 2011-12, employment growth (CAGR) was only 0.5 per cent, compared to 2.8 per cent during 1999-2000 to 2004-05 as per usual status. However the unemployment rate continued to hover around 2 per cent under usual status (principal+subsidiary).

Sustainable Development and Climate Change

1.95 Sustainable development is an imperative for achieving inter-generational equity. The business-as-usual approach to development has entailed unsustainable consumption patterns, which is essentially attributable to the developed countries. Anthropogenic activities are the dominant cause for climate change. GHG emissions grew on an average by 2.2 per cent per year between 2000 and 2010, as compared to 1.3 per cent per year between 1970 and 2000. India's per capita carbon emissions were 1.7 metric tons in 2010, well below the world average of 4.9 metric tonnes.

1.96 Governments are currently working on two new agreements on climate change and sustainable development, both of which will be new global frameworks for action to be finalized next year. Following the Rio +20 mandate, the global community is working to develop a set of Sustainable Development Goals (SDGs), possibly to be integrated with Millennium Development Goals (MDGs) when they end in 2015. Work is already under way and a number of thematic focus areas for the SDGs have been identified.

1.97 How developed and developing countries will be treated in the new aggrements is the most crucial aspect of the global pact. Any future agreement should fully take into account India's concerns and developmental requirements. There is need to ensure that the principles of equity and common but differentiated responsibilities remain firmly embedded in the new deals. Historical responsibility of developed countries and 'equity' in access to global atmospheric resources should define commitments under the international arrangements. The deals must ensure that developing countries are given the required 'carbon space' and 'development space'. The issue of the means of implementation is also important. Lack of adequate resources for SDGs and non-capitalization of the Green Climate Fund may threaten the credibility of global negotiations.

1.98 Sustainability has acquired prominent focus in India's Twelfth Five Year Plan. India reduced CO_2 emissions per unit of GDP by 20 per cent between 1990 and 2011. India's renewable power capacity reached 23 GW in January 2012, equivalent to nearly 12 per cent of total power capacity. Considerable progress has been made in implementing the National Action Plan on Climate Change and also on the State Action Plans on Climate Change (SAPCCs.) The SAPCCs of nine states have already been endorsed.

1.99 The cumulative costs of India's low carbon strategies have recently been estimated by an Expert Group at around US$ 834 billion at 2011 prices, between 2010 and 2030. This could constrain India's efforts, as the magnitude of resources required is very large. Global negotiations provide an opportunity to ensure a fair division of the earth's resources, cooperation between rich and poor nations, curbing wasteful consumption, switching to cleaner technologies, and improving efficiency in resource use. At the heart of all of this lies a fair division of both global rights and responsibilities.

Significant reduction was noticed in the number and proportion of persons below the poverty line in 2011-12.

India's per capita carbon emissions were 1.7 metric tons in 2010, well below the world average of 4.9 metric tonnes.

New climate deals must ensure that developing countries are granted the required 'carbon space' and 'development space'.