

CHAPTER 1

ECONOMIC SITUATION IN 1984-85

At the close of the year 1984-85, which is the last year of the Sixth Five Year Plan, the economy is in a reasonably strong position. However, there are also signs of strain in some areas which could present problems in the years ahead.

1.2 Agricultural production, which showed a strong performance in 1983-84, is likely to register a modest increase in 1984-85. Foodgrains production is likely to be around the record level achieved in the previous year. Industrial performance has improved and the growth rate in 1984-85 may rise to about 7 per cent compared with 5.5 per cent in the previous year. GNP growth is likely to be about 4 per cent, following upon the robust growth of 7.4 per cent in the previous

year. With this, the economy will have achieved an average growth rate of about 5.2 per cent in the Sixth Plan period which is equal to the Plan target.

1.3 Inflationary pressures were a cause of concern in the first half of the year but there was a marked improvement in the second half and the annual rate of inflation on February 9, 1985 was only 4.6 per cent, compared with an annual rate of 10.8 per cent at the same time last year. However, there is severe pressure upon resources which may have implications for the price situation. A marked improvement in the resource position would be required if we are to achieve the increases in development expenditure necessary in the Seventh Plan without jeopardising price stability.

TABLE 1.1
Selected Economic Indicators
(Percentage change over previous year)

	1975-76	1976-77	1977-78	1978-79	1979-80	1980-81	1981-82	1982-83	1983-84	1984-85
1	2	3	4	5	6	7	8	9	10	11
1. Gross National Product at 1970-71 prices	9.6	0.9	8.7	5.9	-4.8	7.7	4.6	1.7	7.4 [@]	4*
2. Agricultural production	15.2	-7.0	14.3	3.8	-15.2	15.6	5.6	-4.1	13.6	1*
3. Foodgrains production	21.2	-8.2	13.7	4.3	-16.8	18.1	2.9	-2.8	17.0	Neg.*
4. Industrial production	7.2	9.6	3.3	7.6	-1.4	4.0	8.6	3.9	5.5	7*
5. Electricity generated (utilities only)	12.9	11.5	3.4	12.2	2.1	5.9	10.1	6.6	7.6	13.5 ¹
6. Wholesale prices (on point to point basis)	-6.5	12.0	0.3	4.6	21.4	16.7	2.4	7.3	8.3	5.0 ²
7. Monetary resources (M3)	15.0	23.6	18.4	21.9	17.7	18.1	12.5	16.1	18.1	15.4 ³
8. Imports (at current prices)	16.5	-3.6	18.7	13.1	34.2	37.3	8.4	5.5	9.8	14.2 ⁴
9. Exports (at current prices)	21.3	27.4	5.2	5.9	12.1	4.6	16.3	14.1	10.8	22.9 ⁴
10. Foreign exchange reserves (excluding gold & SDRs, —end of period) Rs. crores	1492	2863	4500	5220	5164	4822	3354	4265	5498	6014 ⁵

[@]Quick estimates.

*Anticipated.

¹ April—December, 1984 over the same period in 1983.

² Between 31st March, 1984 and 9th February, 1985.

³ Between 31st March, 1984 and 25th January, 1985.

⁴ April—November, 1984 over the same period in 1983.

⁵ As on January 31, 1985.

1.4 The balance of payments position, which had improved in 1983-84, showed further improvement in 1984-85, but it will be necessary to exercise utmost vigilance in order to maintain viability in our payments situation over the medium term.

Gross National Product : Saving and Investment

1.5 The growth of GNP had accelerated to 7.4 per cent in 1983-84 reflecting the strong recovery in agriculture in that year from the depressed conditions prevailing in 1982-83. Value added in agriculture grew at 9.1 per cent in 1983-84 but growth in 1984-85 is likely to be modest because of the high base in the previous year, and also due to unfavourable weather conditions. However, industrial growth has accelerated somewhat in 1984-85 and, together with continued healthy growth in the tertiary sector, the growth of GNP in 1984-85 should be around 4 per cent. The average growth rate in the Sixth Plan period is likely to reach the Plan target of 5.2 per cent. Per capita income in the Sixth Plan period would have increased by about 3 per cent per year.

1.6 The rate of gross domestic capital formation in 1983-84 is provisionally estimated to be about 24 per cent of GDP as compared with 24.4 per cent in 1982-83. There was a decline in the net inflow of capital from abroad from 1.6 per cent of GDP in 1982-83 to 1.3 per cent in 1983-84. The rate of gross domestic savings is estimated at 22.6 per cent of GDP in 1983-84 which is slightly lower than 22.8 per cent in the previous year. It is possible that the method of estimating savings has not captured the large surpluses generated in 1983-84 in the oil sector, and when full account is taken of these surpluses the rate of gross domestic savings may be somewhat higher than in 1982-83.

Agricultural Production

1.7 Agricultural production in 1984-85 is likely to show a modest increase over the record production achieved in 1983-84. The weather conditions during the current year were far from satisfactory. The South-West monsoon has been erratic and winter rains have been inadequate. Even so, foodgrains production is likely to be around the same level as in 1983-84. Some decline is anticipated in kharif foodgrains but this is expected to be made up by rabi output, which may exceed last year's level of 62.4 million tonnes. The predominant rabi crop, wheat, is now insulated to a significant extent from inadequate rainfall because of

irrigation. Cotton production is likely to show a strong increase from the depressed level of 1983-84. Overall agricultural production may increase by a modest 1 per cent.

1.8 Maintenance of the exceptionally strong performance of the previous year, in the face of unfavourable weather conditions, highlights the strengthening of the production base in Indian agriculture. This has been achieved by the strategy of increasing the supply of critical inputs such as irrigation, fertilisers, high yielding varieties, etc. Fertiliser consumption increased from 63.9 lakh tonnes in 1982-83 to 77.2 lakh tonnes in 1983-84. The target for the current year was a further increase to 84 lakh tonnes and preliminary indications are that this target will be exceeded. Thus, over the Sixth Plan period fertiliser consumption will have increased by more than 60 per cent from 52.6 lakh tonnes in 1979-80 to over 84 lakh tonnes in 1984-85. Area under irrigation (potential) was of the order of 56.5 million hectares in 1979-80. It is expected to increase from 65.6 million hectares at the end of 1983-84 to around 68 million hectares at the end of 1984-85. Over the Sixth Plan period, irrigation potential registered an average increase of about 2.3 million hectares per year. This is twice the annual rate of increase achieved prior to the Sixth Plan. The area covered under the high yielding varieties (HYV) programme is also projected to increase from 52.5 million hectares in 1983-84 to 56 million hectares in 1984-85. The distribution of certified seeds is expected to show a significant increase from 57.7 lakh quintals in 1983-84 to 70.4 lakh quintals in 1984-85. At this level, certified seed distribution will have increased five-fold over the Sixth Plan period.

Infrastructure

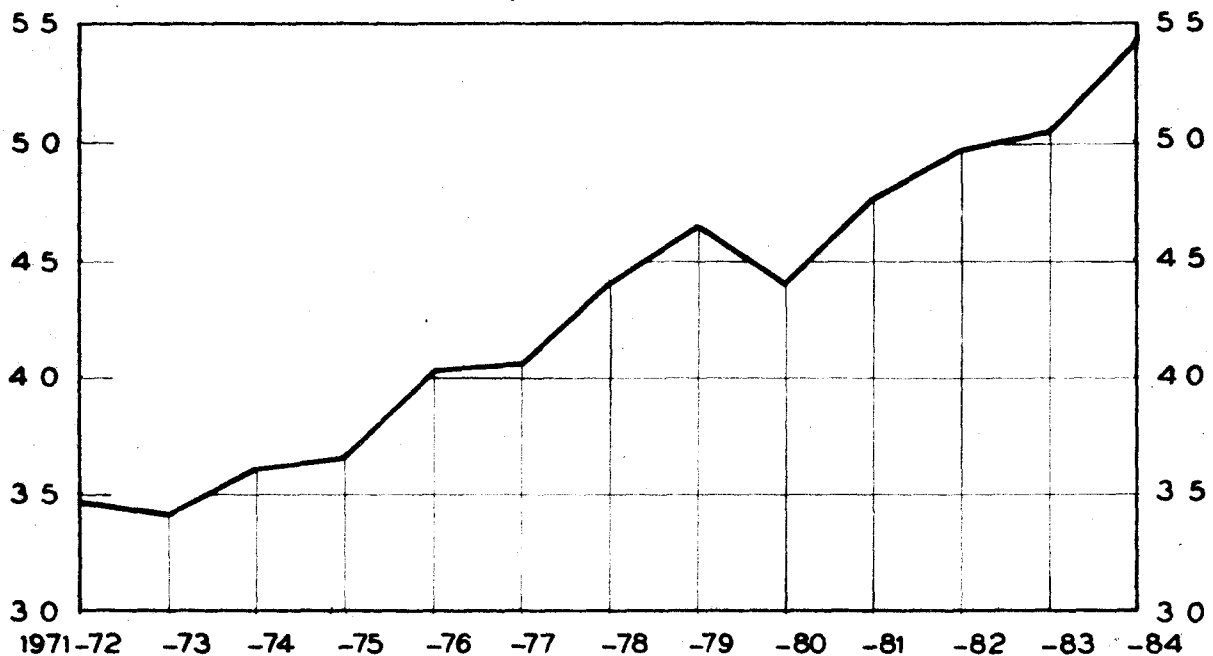
1.9 The major infrastructure sectors, comprising energy and transport, showed a generally strong performance in 1984-85 and were broadly supportive of an accelerated industrial growth. The growth rate of power generation, which had decelerated to 6.6 per cent in 1982-83 and recovered only modestly to 7.6 per cent in 1983-84, has performed especially well in the current year with both hydel and thermal generation showing high rates of growth. Total power generated in the period April—December, 1984 was 13.5 per cent higher than in the same period in the previous year. However, one disquieting feature of performance

NET NATIONAL PRODUCT

(AT 1970-71 PRICES)

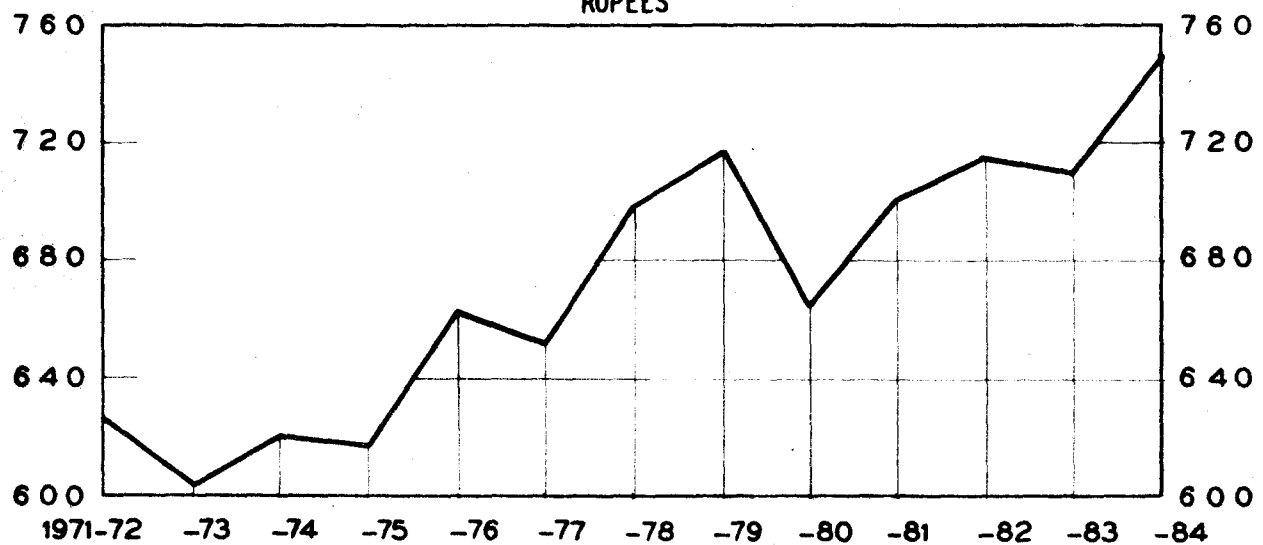
NATIONAL INCOME

RS. IN '000 CRORES



PER CAPITA INCOME

RUPEES



MINISTRY OF FINANCE, ECONOMIC DIVISION

in this sector is that the pace of addition to new capacity in 1984-85 has slowed down and is much below the target.

1.10 Coal production which increased by 5.8 per cent in 1983-84 showed an acceleration in 1984-85 with production over the period April—December, 1984 showing an increase of 6.9 per cent over the same period in the previous year. Although this is below the target of 10 per cent, there has been no serious shortage of coal, except coking coal, where domestic production is inadequate and needs to be supplemented by imports. There was some improvement in the performance of railways in moving freight in 1984-85, although performance was below expectations. Freight movement by rail had stagnated in 1983-84 but it has picked up in the current year with a modest growth of 3.2 per cent in the first nine months. The capacity of major ports has expanded substantially in 1984-85 with total freight traffic expected to increase from 100 million tonnes in 1983-84 to about 106 million tonnes.

Industrial Production

1.11 Industrial production had begun to recover in 1983-84 from the setback in the previous year and the recovery gained strength in 1984-85, with an acceleration in growth. The index of industrial production showed a growth of over 6.6 per cent in the first eight months of the year compared with the same period in the previous year. The growth rate for the year as a whole is likely to be about 7 per cent. The modest growth in industrial production in 1984-85 reflects an acceleration in both electricity and manufacturing offsetting a slight deceleration in mining. However, the growth rate of manufacturing, which accounts for a weight of 81.08 per cent in the index of industrial production, remains low at 5.3 per cent in April—November, 1984 compared with 3.6 per cent in the same period of the previous year. The average growth rate of industry in the Sixth Plan period amounts to nearly 6 per cent, which is a small improvement over the average of about 5.3 per cent in the preceding five years.

1.12 In each of the last three Plans industrial growth has been lower than the targets. This is a matter of concern. Industrial growth needs to be stepped up to about 8 per cent per year in the Seventh Plan period if the economy is to continue to grow at 5 per cent and if adequate employment is to be provided to the ever-growing labour force. The industrial sector

has expanded and matured considerably in many ways but it remains burdened by a high cost structure and growing technological obsolescence, which underline the lack of dynamism. It will be necessary to restructure industrial policy to overcome these constraints in the years ahead.

1.13 The past few years have seen a number of initiatives by the Government to streamline procedures and to liberalise industrial policy so as to provide incentives to industry to improve efficiency and to expand production. In continuation of this thrust, a new computer policy was also announced in November, 1984 under which licensing procedures for manufacturers of computers have been considerably liberalised.

Price Behaviour

1.14 Prices had come under pressure in 1983-84 because of the lagged effect of the drought in the previous year, and the pressure on prices continued into the early part of 1984-85. The wholesale price index moved up by 7.4 per cent between 31st March and 25th August, 1984. However, there was a marked improvement in the later part of the year, reflecting higher production and effective supply management. There was a normal seasonal decline in prices after August, 1984. By 9th February, 1985, the annual rate of inflation in wholesale prices, had declined to 4.6 per cent. The annual rate of inflation as measured by the Consumer Price Index in December, 1984 was also low at 5.2 per cent.

1.15 The major factor accounting for the moderation in inflationary pressure in the current year is clearly the maintenance of the high levels of foodgrains production in 1984-85, following upon the bumper harvest of 1983-84. Total foodgrains stocks at the end of December, 1984 had increased to 22.5 million tonnes, compared with only 16 million tonnes a year earlier. Prices of cereals, which had declined by 5 per cent in 1983-84, showed a further decline of 2 per cent upto end December, 1984. However, the prices of pulses, which had increased by 26 per cent in 1983-84, increased further by 24 per cent upto end December, 1984. Prices of the sugar, khand-sari and gur group also came under pressure in the first part of the year, as also of edible oils and tea. The public distribution system was actively and successfully used to combat these price pressures. Imports of sugar and edible oils were arranged to augment domestic supplies. Releases of sugar (levy, plus free sale re-

lease) in 1984-85 were raised to a level of 82 lakh tonnes which was 16 per cent higher than in the previous year. Edible oils releases during 1984-85 were nearly 33 per cent higher than in the previous year and this helped to stabilise edible oil prices in 1984-85. Exports of tea were restrained in the course of the current year to increase domestic availability and counter the pressure on prices.

1.16 On the whole, economic management in the Sixth Plan period has succeeded in keeping the rate of inflation to a reasonable level. The rate of inflation in the first year of the Plan was 16.7 per cent, mainly a spillover of the inflation which began in 1979-80. Thereafter, the annual rate declined sharply to 2.4 per cent in 1981-82. Despite a bad monsoon in 1982-83, the rate of inflation was kept at the single digit level thereafter.

Fiscal and Monetary Policy

1.17 Fiscal policy in 1984-85 strove to maintain the difficult balance between the need for large provisions for Plan expenditure to meet the targets set in the Sixth Plan, and the need to contain total demand in the face of inflationary pressures, which appeared especially strong in the first half of the year. The budget for 1984-85 had proposed an increase of 25 per cent in the Central Plan outlay over the budget estimates for the previous year. While customs duties were raised, substantial relief was provided for income tax payers by an across the board reduction in tax rates. Incentives for savings and investment were further strengthened, in continuation of the initiatives along the same line in the previous two years. The textile and paper industries received special relief in indirect taxation.

1.18 The pressure on the Centre's budget continued in 1984-85. Non-Plan expenditure is likely to be higher than anticipated, partly on account of dearness allowance (DA) payments and higher subsidies. The States have also experienced severe pressures on their budgetary position in the course of the year. These developments highlight the growing stringency of the resource position. Unless overcome, these trends could severely constrain the Seventh Plan.

1.19 Monetary policy in 1984-85 was formulated against a background of a high rate of growth of both money supply (M3) and reserve money in the previous year. Efforts were made to reduce the rate of expansion in these monetary aggregates to more

acceptable levels, consistent with the objectives of reducing the rate of inflation in the economy. The statutory liquidity ratio (SLR) was raised from 35 per cent to 36 per cent in a two-phased adjustment completed during the first half of 1984-85. The incremental cash reserve ratio of 10 per cent on the addition to deposits which was imposed in November, 1983 was maintained during 1984-85 and this helped to dampen the monetary consequence of reserve money expansion. The cut-off point for food credit beyond which 100 per cent refinance is made available was increased in two stages, from Rs. 3300 crores to Rs. 4300 crores, to further tighten liquidity in the banking system. However, these measures were not able to reduce the rate of growth of M3 below the level observed in the previous year. M3 growth in 1984-85 upto 25th January, 1985 was 15.4 per cent compared with 14.6 per cent in the corresponding period of the previous year. M1 growth was also higher at 12.2 per cent compared with 9.6 per cent in the same period in the previous year.

1.20 The relatively high rate of monetary expansion in the current year was partly due to the larger than expected expansion in net bank credit to Government. Another factor contributing to expansionary stimulus was the improvement in the external payments position, with net foreign assets of the banking system showing an increase of Rs. 422 crores upto January 25, 1985 compared with a decline of Rs. 533 crores in the same period of the previous year.

Balance of Payments

1.21 The balance of payments position had improved considerably in 1983-84. There was a further improvement in the current year. The government voluntarily terminated the IMF arrangement effective May 1, 1984 after having drawn only SDR 3.9 billion out of the SDR 5 billion available under the three year arrangement. Despite the cessation of IMF drawings in the current year, foreign exchange reserves (including gold and SDRs) in 1984-85 increased by about Rs. 547 crores upto end-January, 1985. Part of the increase in rupee terms is because of the strengthening of the US dollar in world currency markets and the consequent increase in the rupee value of dollar holdings.

1.22 Export performance, which was relatively weak in 1983-84, has shown a welcome improvement in the current year. The rupee value of exports

showed a growth of 23 per cent in the first eight months compared with a growth of only 7 per cent in the corresponding period of 1983-84. However, imports increased by about 14 per cent in this period compared with a decline of 4 per cent in the same period of the preceding year. The trade deficit in the first eight months of 1984-85 is estimated at Rs. 3017 crores, which is slightly lower than the deficit of Rs. 3080 crores in the same period of the previous year. The deficit had declined from 4.6 per cent of GDP in 1980-81 to 3 per cent in 1983-84. It is likely to decline further in 1984-85.

1.23 The balance of payments position continues to be strengthened by net inflows on other accounts, though there are a number of uncertainties affecting these flows. Partial data available indicate that although the inflow of remittances from Indian workers abroad continues at a relatively high level, the earlier growth in these inflows has decelerated considerably and prospects are necessarily uncertain. Inflows from non-residents in the form of deposits with Indian banks had increased to Rs. 961 crores in 1983-84 but declined in 1984-85 because of higher interest rates abroad. The inflow was, nevertheless, substantial with an accretion of Rs. 619 crores (including accrued interest) upto end-December 1984, compared with Rs. 750 crores in the same period for previous year. In addition to these sources of funds the volume of commercial borrowings has also increased in the past few years and has supplemented the normal inflow of external assistance as a means of import financing. While recourse to commercial borrowings has provided

additional financing, it has also added to the country's debt service obligations. Future recourse to commercial borrowings will have to be kept under strict control in order to keep the debt service ratio within manageable limits.

1.24 To summarise, the Sixth Plan period is closing with a highly satisfactory performance of the economy. The agricultural sector has performed well and has encouraged expectations of steady growth in the coming years. Industrial performance has improved, though the scope for further improvements remains considerable. The annual growth rate of GDP over the Sixth Plan period is likely to equal the Plan target of 5.2 per cent. At the same time inflationary pressures have been contained and significant adjustments have been attained in the country's external account. These very considerable achievements have been secured in the face of unfavourable developments in world trade and payments.

1.25 Nevertheless, some areas of weak economic performance combined with prospects of a less favourable external environment caution against any complacency. Industrial performance remains below expectations and fresh initiatives are clearly necessary to spur dynamism in this sector. The growing scarcity of public sector resources underlines the necessity for stringent review of expenditure priorities in the Seventh Plan. The medium-term outlook for the balance of payments also underscores the need for efficient import substitution together with a substantial acceleration in export performance.