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GENERAL REVIEW

The Year in Review

Macroeconomic Overview

1. The year 1994-95 saw the fastest growth of the Indian economy in the last four years. After the crisis induced low growth of 0.9 per cent in 1991-92, the economy had already responded smartly to wide-ranging reform measures to record growth of 4.3 per cent in each of the years 1992-93 and 1993-94. The current year has seen an acceleration of growth to 5.3 per cent led by strong, broad-based industrial growth of around 8 per cent and supported by a robust agricultural performance. The performance of the external sector continued to be strong with exports growing by more than 17 per cent in dollar terms in the first ten months of the year, the balance on invisibles climbing to over a billion dollars in the first six months of the year and foreign investment (direct plus portfolio) of $3.9 billion in April-December, 1994. Despite a surge in non-oil imports reflecting the strong industrial recovery, the current account deficit in the balance of payments is unlikely to exceed half a per cent of GDP in 1994-95 and foreign currency reserves have risen by over $4.5 billion since the beginning of the financial year as of February 13, 1995.

2. The remarkable progress made by the Indian economy since the difficult days of the 1991 economic crisis can be gauged by a few simple comparisons. Compared to overall economic growth of 0.9 per cent in 1991-92, the rate in 1994-95 is expected to be 5.3 per cent (Table 1.1). Industrial production, which virtually stagnated in 1991-92, is expected to grow by 8 per cent in 1994-95. Food-grain production had declined to 168 million tonnes in 1991-92; it is expected to attain a record high of 185 million tonnes in 1994-95. Public stocks of foodgrains with the Central Pool stood at 30 million tonnes, as of January 1, 1995, compared to 13.9 million tonnes three years earlier. Compared to an actual decline in 1991-92, the dollar value of exports has increased by more than 17 per cent in the first ten months of 1994-95, on top of a 20 per cent increase in 1993-94. In the year ended 31st March, 1991 India had added $8 billion to her stock of external debt; in the first half of 1994-95 the level of external debt actually declined by almost $300 million. From a level of hardly one billion dollars in June 1991, foreign currency reserves had climbed to over $19.5 billion by mid-February 1995. Whereas the increase in total economy-wide employment is estimated to have been only about 3 million in 1991-92, an expansion of about 6 million is estimated for each of the years 1992-93 and 1993-94, with prospects for a larger rise in the present year.

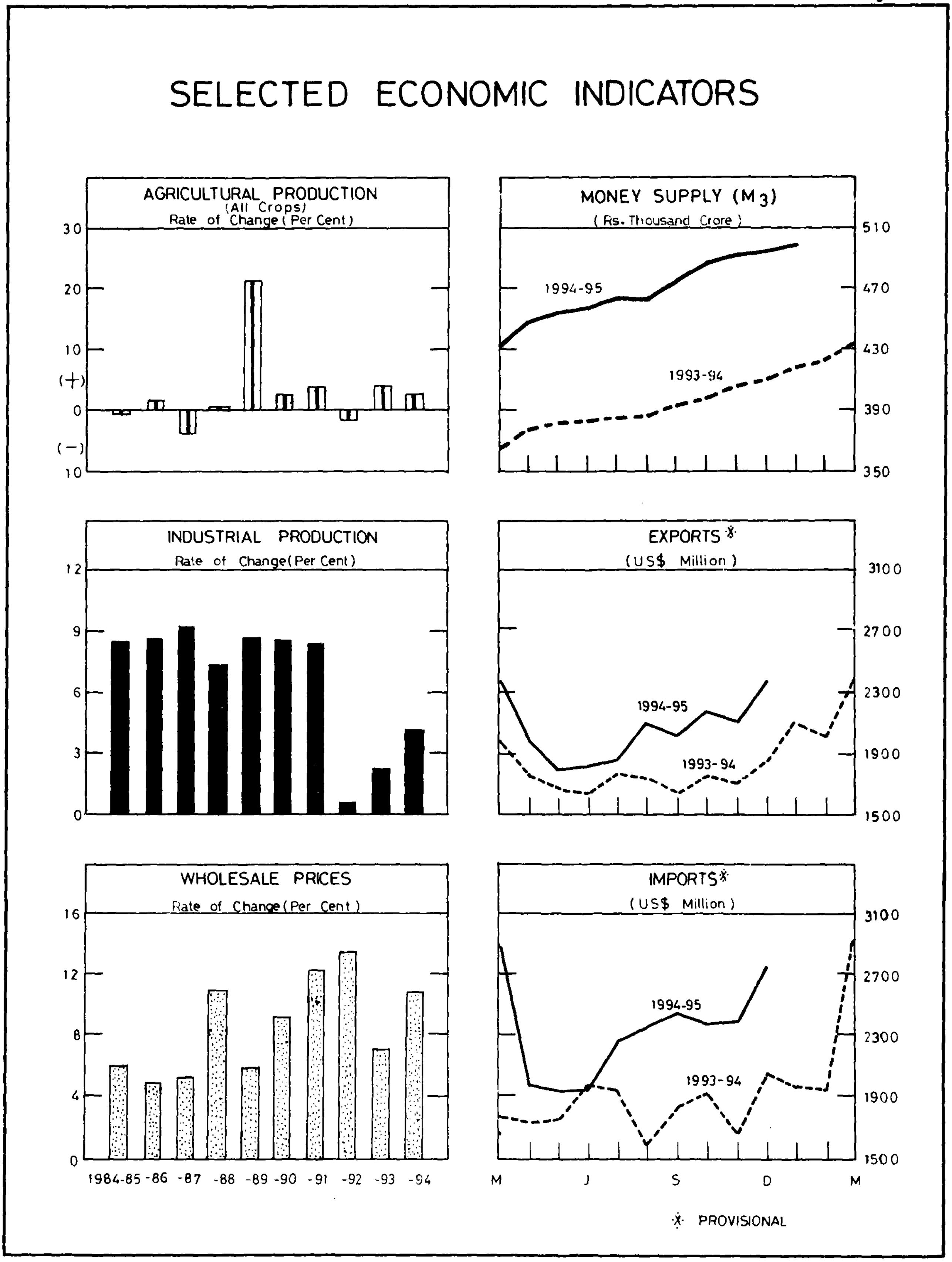
3. Compared to other countries coping with crisis and adjustment, the restoration of macroeconomic stability and revival of growth in output and employment has been exceptionally smooth. But these undeniable achievements are not free from threat. The Central Government fiscal deficit continues to be high and this is reflected in continuing inflationary pressure. The borrowing requirements of a high fiscal deficit are a source of pressure on interest rates and adversely affect the availability of resources for productive investment, especially at a time when a strong industrial recovery has resuscitated private sector demand for investible funds. Inadequate supply of quality infrastructure, especially power, is also an important constraint which could prevent the economy from achieving its full growth potential. Nor is the hard-won relaxation of the foreign exchange constraint immune from reversal. Unless fiscal restraint is observed and reforms in tax and trade policies continued, the recent improvements in international competitiveness and export growth could falter and thus bring the balance of payments under renewed stress. Moreover, in today's increasingly open and competitive international environment, perceptions of weakness in macroeconomic policy or economic reforms could easily affect adversely the flow of foreign savings.

TABLE 1.1
Key Indicators

	1991-92	1992-93P	1993-94P	1994-95P	1991-92	1992-93P	1993-94P	1994-95P
	ABSOLUTE VALUES				PER CENT CHANGE OVER PREVIOUS YEAR			
1	2	3	4	5	6	7	8	9
Gross national product (Rs.thousand crore)								
At current prices	542.0	615.8	695.3 Q		15.2	13.6	12.9 Q	
At 1980-81 prices	209.8	218.7	228.7 Q	240.9 E	0.6	4.2	4.6 Q	5.4 E
Gross domestic product (Rs.thousand crore)								
At current prices	552.0	627.6	707.1 Q		15.5	13.7	12.7 Q	
At 1980-81 prices	214.2	223.4	233.0 Q	245.3 E	0.9	4.3	4.3 Q	5.3 E
Agricultural production(1)	145.5	151.5	154.8	158.2 A	-2.0	4.1	2.2	2.2 A
Foodgrain production (million tonnes)	168.4	179.5	182.1	185.0 A	-4.5	6.6	1.4	1.6 A
Industrial production(2)	213.9	218.9	227.8	232.8(3)	0.6	2.3	4.1	8.0 (3)
Electricity generated (Billion KWH)	287.0	301.1	323.5	257.9(8)	8.6	4.9	7.5	8.4 (8)
Wholesale price index(4)	217.8	233.1	258.3	284.3(5)	13.6	7.0	10.8	11.5 (5)
Consumer price index for industrial workers(6)	229.0	243.0	267.0	289.0(7)	13.9	6.1	9.9	9.5 (7)
Money supply (M3) (12) (Rs.thousand crore)	317.0	366.8	433.6	498.4(10)	19.4	15.7	18.2	18.6 (11)
Imports at current prices								
(Rs. crore)	47851	63375	72806	71248(8)	10.8	32.4	14.9	23.6 (8)
(US $ million)	19411	21882	23213	22708(8)	-19.4	12.7	6.1	23.6 (8)
Exports at current prices								
(Rs. crore)	44041	53688	69547	65483(8)	35.3	21.9	29.5	17.3 (8)
(US $ million)	17865	18537	22174	20871(8)	-1.5	3.8	19.6	17.3 (8)
Foreign currency assets								
(Rs. crore)	14578	20140	47287	61651(9)	232.2	38.2	134.8	30.4 (9)
(US $ million)	5631	6434	15068	19651(9)	151.8	14.3	134.2	30.4 (9)
Exchange rate (Rs/US $)[a,b]	24.65	28.96	31.37	31.38(8)	27.2	14.9	7.7	0.1 (8)

Note:Gross national product and Gross domestic product figures are at factor cost.
A-Anticipated; P-Provisional; Q-Quick estimates; E-Advance estimates
[a] Per cent change indicates the rate of depreciation of the Rupee.
[b] Composite rate from March 1992 to February 1993.
1. Index of agricultural production (principal crops) with base triennium ending 1981-82=100.
2. Index of industrial production 1980-81=100.
3. Average index for April-October,1994.
4. Index with base 1981-82=100. Percentages relate to point-to-point changes in the index over the year.
5. As on February 18, 1995 for 1994-95 and for the last week of March for the earlier years.
6. Index with base 1982=100. Percentages relate to point-to-point changes in the index over the year.
7. As in December,1994 and in March for the earlier years.
8. April-January, 1994-95.
9. As on February 13,1995 for 1994-95 and at the end of March for previous years.
10. As on January 20,1995.
11. April 1,1994-January 20,1995.
12. Percentages relate to point-to-point changes over the year.

Figure 1·1


SELECTED ECONOMIC INDICATORS
AGRICULTURAL PRODUCTION
(All Crops)
Rate of Change (Per Cent)
30
20
10
(+)
0
(−)
10
MONEY SUPPLY (M3)
(Rs. Thousand Crore)
510
470
430
390
350
1994-95
1993-94
INDUSTRIAL PRODUCTION
Rate of Change (Per Cent)
12
9
6
3
0
EXPORTS*
(US$ Million)
3100
2700
2300
1900
1500
1994-95
1993-94
WHOLESALE PRICES
Rate of Change (Per Cent)
16
12
8
4
0
IMPORTS*
(US$ Million)
3100
2700
2300
1900
1500
1994-95
1993-94
1984-85 -86 -87 -88 -89 -90 -91 -92 -93 -94
M J S D M
* PROVISIONAL

4. According to the latest estimates of the Central Statistical Organization (CSO), GDP at factor cost grew by 4.3 per cent in 1993-94, the same rate as in 1992-93. The sectoral composition of growth, however, became more broad-based. Agricultural growth predictably declined from the high of 5.3 per cent in 1992-93, while modern services such as banking and insurance showed faster growth. GDP from manufacturing continued its recovery, with the growth rate increasing from 3.1 per cent in 1992-93 to 3.6 per cent in 1993-94. The real surge in the manufacturing sector occurred this year, with the CSO's Advance Estimates for 1994-95 indicating growth of 8.7 per cent in manufacturing value added. Together with growth of 2.4 per cent in agricultural and allied value added and 5.6 per çent in services, overall GDP growth at factor cost in 1994-95 is estimated to be 5.3 per cent.

5. International experience indicates that real investment in the private sector often declines substantially and remains low during the initial phase of structural reform and adjustment. In India, private investment appears to have responded much more positively to reform policies. Real private gross fixed capital formation, which had fallen to 11.6 per cent of GDP (at 1980-81 prices) in 1991-92, recovered next year and has averaged over 12 per cent of GDP in 1992-93 and 1993-94 (Table 1.2). The prospects for continued growth in private investment in 1994-95 are favourable. The growth rate of sanctions by Development Finance Institutions accelerated from 29.8 per cent in 1992-93 to 44.4 per cent in 1993-94 and surged to 82 per cent in April 1994 to January 1995. Disbursements have shown a more gradual rise, by 28.6 per cent in 1993-94 and by 39.5 per cent in April 1994 to January 1995. The exceptional turnaround in the growth of capital goods production from a decline of 8.7 per cent in April-October 1993 to an increase of 21.7 per cent in the same period of 1994 provides a strong indication of the rising demand for investment goods this year.

6. The recovery in the private gross domestic savings rate has been slower than for investment. The recovery started in 1993-94 with a rise of 1.4 percentage points in the private savings rate to 19.9 per cent of GDP (Table 1.3). But because of the sharp increase in the Central Government revenue deficit in that year, the total domestic savings rate increased only marginally by 0.2 per cent of GDP to 20.2 per cent in 1993-94. An important reason for this lagged recovery in private savings is the decline in the absolute amount of household savings in 1992-93 as estimated by the CSO. Since this decline is observed for a year in which the GDP growth rate rises from 0.9 per cent to 4.3 per cent and GDP growth from agriculture shows a sharp turnaround from minus 2.5 per cent to plus 5.3 per cent, there appear to be grounds for reviewing the methodology for estimating saving and capital formation in the economy.

TABLE 1.2
Trends in Real GFCF as Percentage of GDP (at 1980-81 prices)

	1988-89	1989-90	1990-91	1991-92	1992-93P	1993-94Q
1	2	3	4	5	6	7
GFCF	20.1	20.5	21.3	20.3	19.7	19.8
Public	9.2	8.6	8.6	8.7	7.7	7.8
Private	10.9	11.8	12.7	11.6	12.1	12.0

Note : See Table 1.3 for acronyms and source.

7. The fiscal deficit in 1993-94 was much larger than budgeted, but its monetary impact was contained through sizeable open market sales of Government securities by the Reserve Bank of India. Nevertheless, monetary growth accelerated to 18.2 per cent in 1993-94 from 15.7 percent in the previous year. This, together with the continuing substantial increases in procurement and issue prices of foodgrains, other administered price changes and production shortfalls in key commodities like cotton and sugar, led to a significant increase in the annual rate of inflation in the final quarter of 1993-94. These forces spilled into the first quarter of 1994-95 and took the annual rate of increase in the Wholesale Price Index to 12 per cent before subsiding to a range of 8 to 10 per cent in the middle two quarters of the year and then rising again to double digits in the final quarter.

8. As presaged in the last year's Economic Survey, the management of monetary and other effects of a sudden rise in foreign capital inflows proved to be an important challenge for macroeconomic policy making in 1994-95. To contain the monetary consequences of a rapid rise in foreign exchange reserves in the latter half of 1993-94, a phenomenon which persisted through the first half of 1994-95, a number of counter measures were taken. These included an increase in the general Cash Reserve Ratio (CRR) applicable to commercial banks in May 1994, the phasing out of new flows into the Foreign Currency Non-Resident (FCNRA) Scheme (under which Government bears the exchange guarantee), the imposition and increase in CRRs on various other categories of non-resident deposits held with banks in India, a reduction in the maximum interest allowable on deposits under Non-Resident External Rupee Accounts (NRERA), the tightening up of guidelines for Euro issues and continuation of open market sales of Government securities by the Reserve Bank of India to mop up excess liquidity. By November 1994, the effects of these measures were apparent in the slowing growth of money supply.

TABLE 1.3
Trends in Savings-Investment

	1988-89	1989-90	1990-91	1991-92	1992-93P	1993-94Q
1	2	3	4	5	6	7
	As percentage of GDP at current market prices					
Gross Domestic Savings	21.5	22.3	23.7	23.1	20.0	20.2
Public	2.0	1.6	1.0	2.1	1.5	0.2
Private	19.5	20.7	22.7	21.0	18.5	19.9
Gross Domestic Investment[1]	24.7	25.0	27.1	23.6	22.0	20.4
Public	9.9	10.0	9.7	9.2	8.9	8.9
Private	14.6	14.3	15.9	13.7	14.4	12.4
Gross Domestic Investment[1]	24.7	25.0	27.1	23.6	22.0	20.4
GFCF	21.6	22.5	23.2	22.2	21.5	20.9
Change in Stocks	2.9	1.8	2.5	0.7	1.8	0.4
Saving-Investment Gap[1]	-3.2	-2.7	-3.4	-0.5	-2.0	-0.2
Public	-7.9	-8.4	-8.7	-7.1	-7.4	-8.6
Private	4.9	6.4	6.8	7.3	4.1	7.5
	Growth Rate (%) in Capital Formation (at 1980-81 prices)					
GDCF[1]	17.8	4.7	16.3	-14.2	-1.2	-2.4
Public	8.8	7.0	4.6	-7.2	2.1	6.8
Private	27.7	-1.0	20.0	-15.4	11.9	-10.3
GFCF	7.1	8.7	9.9	-4.0	1.6	3.8
Public	4.7	0.6	4.8	2.0	-7.9	5.6
Private	9.2	15.5	13.6	-8.0	8.6	2.6

Note : *(i) Gross domestic investment means Gross Domestic Capital Formation (GDCF).*
(ii) Figures may not add up due to rounding off,
[1] *adjusted for errors and omissions;*
GFCF Gross Fixed Capital Formation;
P Provisional estimates; Q:Quick estimates
Source: Central Statistical Organisation

Production

9. The current year has been an excellent one for agriculture. This out turn has been shaped by a good monsoon in 1994, whose coverage across the country was the best since 1989. The rainfall during the period June to September 1994 was close to 110 per cent of its long run average. The likely output of foodgrains during 1994-95 at 185 million tonnes is the highest ever. Rice production, which has exceeded the target, constitutes 80 million tonnes and expected wheat production, 58.5 million tonnes. The rate of growth of foodgrains production for 1994-95 is therefore 1.6 per cent and for rice 1.3 per cent. Coarse cereal production, after suffering a setback in 1993-94, is expected to be around 32 million tonnes in 1994-95, with a growth of 3.6 per cent. Production of pulses is anticipated to grow by 10.7 per cent to 14.5 million tonnes. Aside from good weather, agricultural production has benefited from the cumulative effects of improved incentives engendered by higher support/procurement prices and lower protection to the industrial sector.

10. The picture regarding crops other than foodgrains is quite encouraging. Despite some setback in production of soyabean, total availability of edible oil from secondary as well as primary sources is likely to exceed last year's level of 61.7 lakh tonnes. Sugarcane output is expected to grow by 8.1 per cent to a production level of 245.6 million tonnes during 1994-95 (October-September), attributable to a large extent to higher cane availability in Maharashtra, Karnataka and Tamil Nadu. Cotton output is expected to be at 11.6 million bales, about 8.4 per cent higher than the preceding year. Among plantation crops, production of tea and natural rubber will be higher than last year.

11. The recovery in industrial growth, which was becoming apparent at the time of the last Economic Survey, gathered full force during 1994. Industrial production, as measured by the Index of Industrial Production (IIP), grew by 4.1 per cent in the second half of 1993-94. The momentum of growth accelerated substantially during 1994-95, with a growth rate of 8.0

per cent for April-October, 1994, over the corresponding period of last year. The acceleration in industrial growth during April-October 1994 has been primarily due to a robust growth of 8.3 per cent in the manufacturing sector, as measured by the IIP. The mining and quarrying sub-sector has also shown healthy recovery, with a growth of 6.2 per cent, while electricity generation growth has remained strong at 7.7 per cent during April-October 1994.

12. The IIP data by use based classification suggests that the acceleration in industrial growth has been led by a sharp recovery in investment, with the capital goods sector registering a growth rate of 21.7 per cent for April-October 1994, in contrast to a decline of 8.7 per cent for April-October 1993. The fears of domestic capital goods being swamped by imports have proved unfounded. The rate of growth of the IIP for consumer goods has recovered to 7.4 per cent in April-October 1994, with 8.6 per cent growth for durables and 7.1 per cent growth for non durables. This compares with significantly lower growth rates of 3.1 per cent for consumer goods and 0.7 per cent for non-durables in the corresponding period of 1993.

13. The industrial recovery was broad based with 13 of 17 manufacturing sub-sectors showing positive growth. The growth rate of five sectors, namely "other textile products", paper and paper products, metal products and parts, electrical machinery and transport equipment, exceeded 12 per cent. The four sectors which showed negative growth were cotton textiles, jute textiles, basic metals and miscellaneous manufactures. The decline in cotton textiles production was only marginal. Production data for April-October 1994 in respect of 172 selected industries, accounting for a weight of 88.1 per cent in the IIP, show that 121 industries with a weight of 74.2 per cent recorded positive growth rates and 51 industries with a weight of 13.9 per cent registered a decline.

14. Infrastructure sectors have performed much better this year. Electricity, coal, steel, cement, crude oil and petroleum products with a combined weight of 28.8 per cent in the IIP show a growth rate of 8.0 per cent for April-December, 1994 compared with 5.0 per cent for April-December 1993. Electricity generation grew by 8.4 per cent, saleable steel by 8.9 per cent, cement by 8.6 per cent, and crude oil by 19.4 per cent. Coal was the only sector showing a deterioration, with a growth of 3.2 per cent compared with 4.8 per cent for the same period in 1993-94. Infrastructure sectors not included in the IIP, also show good growth for April - December, 1994. New telephone connections grew by 81.3 per cent, cargo handled at major ports by 8.4 per cent and revenue generating traffic of the railways by 2.5 per cent.

15. On industrial policy reforms, a new Drug Policy, consistent with the liberalised industrial policy, was announced. Industrial licensing was abolished for all bulk drugs and their formulations and intermediates except in a few cases. Most basic drugs and formulations were also brought under the automatic approval policy for 51 per cent foreign equity holding. The number of drugs under price control was reduced from 142 to 73 by defining transparent criteria for identifying drugs whose prices need to be controlled.

16. A number of measures have been announced to facilitate private entry into areas of infrastructure which were formerly the preserve of the public sector, with a view to freeing scarce public resources for social sectors. These include natural resource sectors and non-tradeable infrastructure services such as electricity, internal transport and telecommunications. Among important developments are :

- The National Mineral Policy was revised and the Mines and Mineral Development Act amended, to open up this sector to private and foreign investment. Thirteen minerals were dereserved for exploitation by the private sector.
- The RBI based automatic approval policy for foreign investment was made applicable to mining (except for atomic minerals and mineral fuels), subject to a limit of 50 per cent on foreign equity.
- The power sector policy framework attracted 138 private proposals for creating 58,745 mega watts of capacity with an investment of Rs.2,19,927 crore. Of these, 41 proposals are from foreign investors or are joint ventures with foreign partners, of which thirteen have already been cleared by the Government.
- The National Telecom Policy, 1994 allows private provision of basic telecom services. Implementation has begun after announcement of rules and procedures.
- The new Air Corporation Act 1994 enables private Air Taxi companies to operate as regular domestic airlines. Nine Air Taxi operators, complying with Air Craft rules, have been granted "scheduled airline" status.
- Areas like development and maintenance of airport infrastructure and material handling at major airports have been opened up for private participation.
- The National Highway Act has been amended to enable levy of tolls on national highway users. Government intends further amendment of the Act to allow private participation in construction,

maintenance and operation of roads on Build-Operate-Transfer (BOT) basis.

Private participation has been invited in leasing of port equipment, operation and maintenance of container terminals, cargo landling terminals, creating warehouse and storage facilities, transportation within ports, setting up of private berths by coast based industries, ship repairs and maintenance.

Money and Prices

17. Monetary trends observed in the second half of 1993-94, have continued through most of the current year. The rate of growth of money supply, M_3 (currency plus all bank deposits), displayed a gradual but sustained uptrend till November 1994. There was an even stronger acceleration in the annual rate of growth of narrow money, M_1 (currency plus demand deposits of banks). The annual growth rate of M_3, which peaked at 22 per cent in November 1994, has subsequently declined to 18.6 per cent as of January 20, 1995. The reason for the uptrend in monetary growth through most of 1994-95 was a sharp rise in the growth of reserve money, which followed a similar pattern to that of money supply.

18. Reserve money is the sum of many variables such as RBI credit to government, RBI credit to banks and the commercial sector, and RBI's net foreign exchange assets. The growth rate of two of its important sources have moved in opposite directions. RBI credit to government has shown a decline in growth, while growth of RBI's net foreign exchange assets has accelerated. The net result has been an acceleration in the annual rate of growth of reserve money since the middle of 1993-94. Reserve money growth peaked in February 1994, and, after fluctuating at fairly high levels, it has declined to an annual rate of 21.2 per cent on January 20, 1995. Annual growth of net foreign exchange assets of RBI similarly peaked in March 1994, and was down to 93 per cent by January 20, 1995. The large accretion of net foreign exchange assets, which has propelled the growth of reserve money, is a reflection of the strong build-up of foreign exchange reserves, arising from improvements in the current and capital accounts of the balance of payments.

19. What is more remarkable about the growth of reserve money in 1994-95 compared to 1993-94, is the dramatic fall in the contribution of the monetised deficit of the Central Government. Accumulation of net foreign exchange assets by RBI up to January 20, 1995 constituted 88.7 per cent of the total increase in reserve money during the financial year. Net RBI credit to government made a negative contribution (- 20.2 per cent) to the growth of reserve money in 1994-95, because of a decline of Rs.3983 crore. In the corresponding period of 1993-94, the increase in net RBI credit to government constituted 36.4 per cent of the increase in reserve money, while increase in net RBI foreign exchange assets constituted 65.6 per cent of the increase. This very different pattern of reserve money growth has been made possible by the behaviour of the Central budget deficit (total expenditures minus total receipts - both revenue and capital) which has been negative for almost six consecutive months of 1994-95 from July 29, 1994 to January 20, 1995. A decline in net RBI credit to Government has been accompanied by a reduction in the growth of "Other banks' credit to Government" from 27.1 per cent in 1993-94 (till January 21, 1994) to 15 per cent in 1994-95 (till January 20, 1995). The slowing down of the growth of Government borrowing is due to a reduction in the fiscal deficit in 1994-95 from the previous year.

20. Bank credit to the commercial sector has been much more buoyant in the current financial year. By January 20, 1995, it had grown by 13.6 per cent, which is more than double the growth of 6.3 per cent in the comparable period of 1993-94. Unlike last year, when most of bank credit by commercial banks went into food credit, the acceleration in growth of non-food credit by scheduled commercial banks is dramatic. In the financial year up to January 20, 1995 this has grown by 17 per cent compared to only 4.4 per cent in the corresponding period of last year. The strong recovery of industrial production has been the principal reason for this growth. Food credit growth of 26.2 per cent, though slower than the 58.8 per cent growth in the corresponding period of 1993-94, is still substantial.

21. Two major initiatives were taken to improve the working of the monetary system. One was to initiate a process which will break the link between the Central Government fiscal deficit and reserve money growth. A historic agreement was signed in September 1994 between RBI and the Ministry of Finance to phase out by end 1996-97, Central Government borrowing from RBI through ad hoc Treasury Bills. The agreement also specifies the budget estimate of Rs.6000 crore as ceiling for the year 1994-95. Further, such borrowing will not be allowed to exceed Rs.9000 crore for more than ten consecutive working days during the year. Traditionally, an increase in the fiscal deficit above the availability of conventional sources of borrowing, automatically resulted in an increase in the budget deficit and RBI credit to Government. This in turn increased reserve money and led to higher monetary growth. The agreement between the Reserve Bank and the Central Government will sever this direct link between the fiscal deficit and monetary growth, and to that extent make monetary policy independent of the Central budget.

22. Second, a key psychological barrier to a flexible and market responsive financial system was also

crossed in 1994-95, with the abolition of the minimum lending rate on bank loans above Rs.2 lakhs. Each bank will now have to set its own prime rate on which the structure of loan rates will rest. This, along with the entry of six new private banks during the financial year, is expected to spur competition and cost consciousness in the banking sector. The cooperative banking sector saw similar changes, with complete decontrol of deposit rates and deregulation of lending rates subject to a minimum lending rate of 12 per cent.

23. During the current financial year up to February 4, 1995 the general price level rose by 9.6 per cent compared to 9.1 per cent in the same period last year. The annual growth rate for February 1995, was however, closer to 11 per cent. Aggregate inflation has therefore followed a pattern broadly similar to that of monetary variables since the middle of 1993-94. Throughout the second half of 1993-94, inflation was on a rising trend, which continued in 1994-95 to reach a peak of 12 per cent in May.

24. Primary articles continue to contribute disproportionately to the total inflation, with an increase in their contribution from 35 per cent in 1993-94 (till February) to 46 per cent in 1994-95 (till February). The pattern of price increases within this group is, however, significantly different this year. The contribution of food articles has more than doubled from 12 per cent to 29 per cent, even though the contribution of cereals has declined because of stable wheat prices. The inflation in primary non-food articles has been somewhat lower this year.

25. Both supply and demand factors contributed to high inflation. Among supply side factors were the cumulative effect of large increases in minimum support prices, production shortages in key commodities and the spill-over effect of administered price increases. On the demand side, the continued high fiscal deficit in 1994-95, though lower than the 7.3 per cent of GDP in 1993-94, contributed to inflation. High growth of monetary aggregates was one of the more important factors in the high level of inflation in 1994-95.

26. A number of measures were therefore taken to control money growth. The cash reserve ratio (CRR) was raised from 14 per cent to 15 per cent to moderate monetary growth. The agreement to limit access of the Central Government to RBI borrowing through ad hoc Treasury Bills limits monetisation of the fiscal deficit. Cash reserve ratios were also imposed on the Foreign Currency Non Resident (Banks) Accounts scheme and on the Non-Resident Non-Repatriable Rupee Deposit (NRNRRD) scheme (15 and 7.5 per cent respectively). The FCNRA scheme (in which the Government bears the exchange guarantee) was eliminated in a phased manner, and the interest rates on NR(E) RA deposits brought down, with a view to moderating inflows. The RBI also undertook open market sales of Government securities to mop up excess liquidity.

27. On the supply side a number of measures were taken since March 1994, to moderate prices of primary articles:

- Sugar was put on OGL in April 1994 with zero duty (leading to estimated imports of about 9 lakh tonnes in 1994-95) and 10 lakh tonnes were imported on Government account for supply through PDS.
- Open market sales of wheat from record high public stocks continued with sale of 3.4 million tonnes in 1994-95 (till January 1995), on top of 2.8 million tonnes sold in 1993-94.
- 2.8 lakh tonnes of rice were also sold from stocks up to January 1995. FCI was advised to reduce the price sharply from January 1995 to increase the pace of open market sales.
- Palmolein imports were placed on OGL with 65 per cent duty in April 1994. In March 1995, a number of other edible vegetable oils (except coconut oil) were also placed on OGL and the customs duty lowered to 30 per cent.
- Imports of 1.5 lakh tonnes of edible oils for the PDS in April 1994 and additional 1.5 lakh tonnes by NDDB were authorised at a concessional duty by August 1994.
- Imports of cotton were placed on OGL in April 1994 with zero duty, and sizeable import of viscose staple fibre allowed at concessional duty.

Fiscal and Financial Developments

28. The slippage seen in 1993-94 in the programme for restoring fiscal balance, has been checked in the year 1994-95. The fiscal deficit is expected to go down from 7.3 per cent of GDP in 1993-94 (RE) to 6 per cent of GDP in 1994-95 (BE). The Central Government's fiscal deficit has therefore declined by 2.4 per cent of GDP since the start of the programme of fiscal correction in 1991-92. The gross primary deficit has shown an even greater decline of 3.4 per cent of GDP, resulting largely from successful containment of growth in non-Plan expenditures. There has also been a qualitative change in the expenditure of the Government. The share of Plan expenditure in relation to the non-Plan expenditure has been on the increase. This is despite the fact that interest payments, which form a major component of the non-Plan expenditure, continue to rise.

29. The 1994-95 Budget undertook a major reform of indirect taxes. The peak rate of customs duty was further reduced from 85 per cent to 65 per cent. In an important exercise to remove anomalies, the very high

duties on steel and steel products were substantially reduced. Customs duties on project imports were reduced from 35 per cent to 25 per cent and on machine tools from 40, 60 and 80 per cent to 35 or 45 per cent, to give a boost to investment. This was combined with the imposition of a countervailing duty (CVD) on capital goods imports, and extension of MODVAT to capital goods to boost domestic production. The structure of import duties on non-ferrous metals and their minerals, coal, petroleum products and medical equipment was rationalised. The number of end use notifications and rate categories was sharply reduced for both custom and excise duties. Within excise, a significant switch over was effected from specific to ad-valorem duties to strengthen built-in revenue elasticity. The number of rates of excise duty was reduced by half. MODVAT was extended to cover petroleum and capital goods.

30. Reform of income taxes through simplification, reduction in marginal rates, rationalisation and administrative reforms also continued. As the 1994-95 Budget indicated, all these tax reforms will entail a loss of Rs.3604 crore for the Centre, if estimated by conventional methods. However, it was felt that the comprehensive tax reform undertaken would induce greater tax compliance, leading to larger revenue increases, which would wholly offset the conventionally estimated "revenue losses". Preliminary data through October 1994 showing an increase of 53.5 per cent in receipts from personal and corporate income taxes and 18 per cent in customs and excise taxes suggest that revenue collections in 1994-95 have vindicated the tax reform strategy pursued.

31. The cumulative effect of the decline in marginal income tax rates in the past four years has not reduced tax revenue as feared by some. On the contrary, the overall effect of the reforms has been to raise the buoyancy (measured as percentage change in revenue divided by percentage change in nominal GDP at factor cost) of both personal and corporate income tax revenues. The personal income tax buoyancy has averaged about 1.4 during 1991-92 to 1994-95 (BE) as against 1 during the previous four years. The corporate tax buoyancy has similarly risen from 0.8 during 1987-88 to 1990-91 to around 1.7 during 1991-92 to 1994-95 (BE). The share of direct taxes in the Centre's gross revenue has consequently increased from 19.1 per cent in 1990-91 to 28.4 per cent in 1994-95 (BE).

32. In the financial sector, reforms continued to strengthen the banking system and promote competition. Six new private sector banks were established. The complete decontrol of interest rates on large loans expanded the arena for competitive forces to work. Public sector banks completed provisioning for substandard assets and attained 4 per cent capital to risk weighted assets ratio (CRAR) in 1993-94. Though most banks made larger profits before provisioning than in 1992-93, higher provisioning resulted in a net loss, the State Bank of India was the main exception to this trend. The Banking Companies (Acquisition and Transfer of Undertakings) Act was amended to enable public sector banks to access the capital market, and one of them has already raised about Rs.360 crore through equity issues. For the weaker banks who are not yet in a position to access the capital market, a provision of Rs.5600 was made for Government support for recapitalization.

33. Prudential and capital adequacy norms were announced for the five All India development finance institutions namely, Industrial Development Bank of India, Industrial Credit and Investment Corporation of India, Industrial Finance Corporation of India, Industrial Reconstruction Bank of India and Export Import Bank. All must attain 4 per cent capital adequacy norm by March 1995 and 8 per cent by March 1996, though institutions operating abroad have to achieve 8 per cent by March, 1995. Prudential norms were also announced for Non-banking financial companies. Companies with net owned funds of Rs.50 lakhs and over will have to register with RBI and meet a capital adequacy norm of 6 per cent by March 1995 and 8 per cent by March 1996.

34. Institutional reforms for strengthening financial systems also continued. Four Special Debt Recovery Tribunals were set up along with an Appellate Tribunal to expedite the recovery of bank loan arrears. For an integrated and efficient supervision of the financial sector as a whole, a Board for Financial Supervision has been set up with the Governor of RBI as its Chairman. An Advisory Council (to the Board) including a former Chief Justice of the Supreme Court, has also been set up. RBI's new Department of Supervision established in December 1993 will service the Board.

35. The process of capital market reforms was deepened, with SEBI continuing its efforts to introduce greater transparency, participant responsibility and efficiency into primary and secondary markets. Rules have been announced for private placement and for allotment of shares to promoters. A comprehensive new takeover code has been announced. The National Stock Exchange of India commenced operation in June 1994 with the wholesale debt market segment. This covers public sector bonds, Government dated securities and Treasury Bills, certificates of deposits, commercial paper and corporate-debentures. It started equity market trading from November, 1994. The NSE's screen-based, scripless trading system and VSAT satellite links

provide an important element in the journey towards an integrated national debt and equity market. During 1994-95, the number of foreign institutional investors (FIIs) rose from 158 to 286, while their stock of investment increased from $1.66 billion to $3.1 billion (till end January). Indian companies have raised $1.74 billion through GDRs during 1994-95 (inflows till January).

Balance of Payments

36. The balance of payments position has shown steady improvement since 1991-92 with exports covering a larger proportion of imports than in the earlier years. The export-import ratio has averaged nearly 90 per cent during 1991-92 to 1993-94, compared to an average of about 65 per cent for the preceding three years. The current account deficit has also declined, averaging about 0.7 per cent of GDP for these three years, compared to an average of about 2.6 per cent of GDP in the preceding three years. Even though the export-import ratio for 1994-95 is expected to decline from the high of 94.6 per cent in 1993-94, and the current account deficit rise from the low of 1993-94, the four year average is unlikely to be much different from the three year average.

37. The improvement in India's balance of payments during 1993-94 which resulted in an unprecedented build up of foreign currency reserves, continued in 1994-95. These assets rose further from $15.1 billion at the end of March 1994 to $19.8 billion by October 1994, and have since stabilised at around this level. This improvement enabled India to complete the country's phased transition to current account convertibility and to assume the obligations under Article VIII of the IMF, including avoidance of unilateral restrictions on current account transactions in future.

38. The reserve build-up, as the net result of all external transactions, reflects the effect of improvements on the current and capital accounts. During the first half of 1994-95, the current account deficit was only $436 million as compared to $938 million in the first half of 1993-94. The surplus on invisibles account for the first half of 1994-95 improved sharply to $1096 million, compared to a small deficit in the first half of 1993-94. This improvement was, however, partially offset by a widening of the trade deficit to $1.5 billion in the first half of 1994-95 from about $850 million in the first half of 1993-94. This has been due mainly to a 28 per cent growth in non-oil imports, fuelled by the upsurge in industrial growth. These developments are expected to yield a higher trade deficit for 1994-95 than during the previous year. Despite this, the trade deficit as a proportion of GDP will be less than in 1992-93.

39. Net capital inflows from abroad have risen sharply from $2.1 billion in April-September 1993 to $3.8 billion in April-September 1994. The composition of these flows has also changed towards equity and away from debt. External assistance, external commercial borrowing, IMF loans, and non-resident deposits, have declined progressively from 85.8 per cent of net capital inflows in 1990-91 to 40 per cent in 1993-94. The average maturity of NRI deposits is now much higher, and they constitute only 10.2 per cent of current inflows. In contrast, direct foreign investment quadrupled from $150 million in 1991-92 to $620 million in 1993-94. In the first half of 1994-95, it has been 50 per cent higher than in the first half of 1993-94. Foreign equity inflows in the form of GDRs and FII inflows, which surged in 1993-94, are likely to stabilise in 1994-95 at levels moderately higher than last year.

40. The Government has continued to follow a prudent course with regard to external debt. As a result, the annual increase in the stock of external debt outstanding declined from a high of $8.1 billion in 1990-91 to $0.7 billion in 1993-94. Indeed, in the first half of 1994-95 the stock of external debt actually fell, by $270 million, for the first time in recent history. Government has also successfully striven to bring down the proportion of short-term debt in total external debt from 10.2 per cent at the end of 1990-91 to 4.0 per cent at the end of 1993-94, with a further decline to 3.1 per cent by end-September, 1994. Furthermore, the proportion of concessional debt in total debt remains unusually high at 47 per cent compared to other developing countries with large debt stocks, such as Brazil (2%), China (16%), Indonesia (28%), Mexico (1%) and the Russian Federation (5%).

Social Sectors and the Poor

41. The development of our vast human resources is essential for both equity and sustained growth. Despite substantial accomplishments, the size of our population makes the remaining task quite daunting. As the economy emerges from the crisis and the stabilisation measures needed to get us out of it, special care must be taken to protect the weakest and poorest segments of society. Recognizing these imperatives, Government has substantially stepped up Central Plan allocations for social sectors and poverty alleviation programmes in the last two budgets.

42. The Central Plan allocation for Education has been increased by 62 per cent over the last two years, with outlays for elementary and adult education growing by 84 and 78 per cent respectively. The outlay for health was increased by 91 per cent. The Central Plan outlay for rural development, including anti-poverty programs, was increased by 126 per cent over

the past two years to a level exceeding Rs.7000 crore in 1994-95 (BE). Two new schemes, the Employment Assurance Scheme and Prime Minister's Rozgar Yojana, were launched in 1993-94 and are being strengthened and expanded. Central Plan expenditure on education, health, family welfare, women and children and rural development as a per cent of GDP increased from 0.9 per cent in 1991-92 to 1.2 per cent in 1993-94 (RE). This has helped protect disadvantaged groups from the adverse effects of the reforms.

43. Government has accorded the highest priority to promotion of sustainable employment generating growth in its economic reforms. As a result, employment growth is estimated to have doubled to 6 million per annum in 1992-93 and 1993-94 from 3 million in the crisis year of 1991-92. With growth accelerating this year, employment generation is expected to increase commensurately.

44. One indicator of trends in rural poverty is real wage rates for agricultural labour. Although there are differences across States, average agricultural real wages show a drop in the crisis year of 1991-92 and increases in 1992-93 and 1993-94. The increases more than neutralised the drop in 1991-92.

45. Annual data on vital statistics reveal some interesting trends in recent years. Though too much should not be read into annual variations, it is nevertheless interesting, that the trend decline in the Crude Death Rate (per thousand), halted and even reversed slightly in 1991 and 1992 before resuming a downward trend in 1993. Similarly, the trend decline in the Infant Mortality Rate also paused in 1991 and 1992 before continuing downwards in 1993. These preliminary data are consistent with the view that the economic crisis of 1991-92 adversely affected general living standards in both 1991 and 1992, while the reform induced recovery led to an improvement in general living standards in 1993.

Issues and Priorities

46. Last year's Economic Survey outlined the principal issues and priorities for the Indian economy in the medium term. In broad terms the diagnosis remains unchanged. However, it does no harm to remind ourselves of the most pressing issues. Above all, it is salutary to reassert the basic goals of growth, equity, self-reliance and modernization. We must never forget that the fundamental objective of economic reforms, and indeed of all economic policies of Government, should be to bring about a sustained improvement in the living standard of the people of India, especially the poor. Rapid and sustained growth of output and employment opportunities is the surest antidote to our daunting problem of poverty.

47. In the immediate future, an important factor determining the quality of life of India's people, is the quality of public goods and services provided by all levels of government. This includes services such as police, legal systems, education, health, the work of revenue officers, roads, sanitation, electricity, water supply, irrigation water, post, telecommunications and banking. The importance of this interface between the government and the public cannot be exaggerated. It can have a profound impact on the level of satisfaction of the vast majority of the public, which has neither the influence nor the resources to improve public service provision nor the wherewithal to have recourse to costly private options.

Fiscal Policy

48. The most important lesson on fiscal policy comes from our own past, though it is confirmed by the experience of a wide variety of countries. The crisis of 1991 showed clearly that fiscal excess, political instability and governmental inaction can combine to have serious consequences. As the lag between fiscal imbalance and its effects is not precisely predictable, there is always the temptation of fiscal laxity for short-term gains. But history teaches that the costs of fiscal populism can be extraordinarily high and long-lasting. If the basic goal of sustained, employment-intensive growth is to be achieved, we have no alternative to fiscal prudence.

49. As the momentum of growth accelerates, the competition for investible resources will increase. If fiscal deficits continue to be high, the growth in private investment can be throttled by rising interest rates. In theory, foreign inflows, by augmenting domestic savings, can reduce or eliminate crowding out of private investment by government borrowing. In practice, such inflows are dependent on fiscal trends, progress with economic reform and perceptions regarding political stability. Thus, in practice, the sustainability of growth hinges on securing a measured and sustainable reduction in the fiscal deficit.

50. The second fiscal lesson is that reasonable, broad based taxes are more likely to produce a sustained rise in revenues and improvement in equity than high rates which spawn strong incentives for evasion and avoidance and lead to shrinkage of the tax base. Income tax rates were raised progressively during the early seventies, to reach marginal tax rates inclusive of wealth tax, of over 100 per cent. This produced an illusion of better equity and temporarily higher revenues, but led to an increase in tax evasion and corruption. In contrast, the reduction in marginal rates, coupled with other tax reforms and administrative measures to improve compliance, has raised the buoyancy of these direct taxes.

51. Reform of the structure of Central excise and customs duties must be persevered with till completion. For customs duties, this means that duty rates must become comparable with those in other parts of Asia. Though substantial progress has been made in eliminating exemptions based on user, usage and source, which give rise to many anomalies, the task is by no means complete.

52. MODVAT should be transformed into a genuine Central VAT, within the current constitutional parameters. Though a number of steps have been taken in this direction, there is still a gap between theory and practice. The MODVAT principle must be applied comprehensively and uniformly. Ideally, with the exception of final consumer goods, all other manufactured goods used as inputs in production, should have a single uniform excise rate. Once VAT credit is available, this simplifies the system enormously and eliminates most anomalies and much harassment potential. There can be three to five rates on final consumer goods based on a broad classification into categories such as necessities, normal goods and luxuries. Simplified self-assessment procedures, backed by computerized checking, are a must if the system is to be effectively broad based to encompass the entire manufacturing and modern service sectors.

53. Identification and reduction of wasteful expenditure in government organizations and programmes remain both essential and difficult. By its very nature, members of every organization have a vested interest in preserving expenditures and support staff, the source of power and prestige. Consensus on what precisely constitutes waste is therefore very difficult. When we add to this the host of special interests who have become dependent on the system, the task becomes stupendous. Nevertheless we must continue to strive towards the goal of ensuring that expenditures, subsidies and transfers reach the intended beneficiaries, by : targeting subsidies to the poor and making the rest pay the cost of public services; cutting leakages and reducing administrative overheads; and phasing out programmes, departments and organizations which benefit only those who work in them.

Monetary Policy

54. With this year's historic accord between the Government and the Reserve Bank of India limiting the former's unilateral access to the latter for borrowing through ad hoc Treasury Bills, the linkage between fiscal and monetary policy has been sharply weakened, restoring much more autonomy to monetary policy. With greater autonomy comes more responsibility. The RBI is now both more able and more responsible for controlling the overall growth of money and credit in a manner best suited for moderating inflation, while meeting the genuine credit needs of the economy. The capacity for effective monetary management and inflation control needs to be further strengthened through rapid deepening and broadening of primary and secondary markets for Government securities.

Industry and Trade

55. An important element of trade and industrial policy reforms is to promote both domestic and foreign competition and thus foster greater productivity, lower costs, better quality and more innovation. Competition is the best antidote to monopolistic practices: it ensures that businesses earn their profits and wealth through enterprise and skills rather than "monopoly rents", which are an inequitable form of hidden taxation. The resurgence in output, quality and product range in the machine tools industry provides an illustration of the benefits of industrial deregulation and reduction in controls and duties on imports. Continued dismantling of barriers to competition must be a key element of further reforms.

56. The process of eliminating licensing as a method of controlling imports needs to be extended further. Substitution of tariffs for quantitative import restrictions (including in the area of consumer goods), as indicated in the Eighth Plan, will improve efficiency and check smuggling. This is especially so since import policy has been liberalised in our neighbouring countries and there is an encouragement to smuggle goods which are banned for import into India. Capital and intermediate good industries have responded well to the transition from licensing to tariff based controls and there is little reason to believe that other industries will not be able to do so. The fear that there will be an unsustainable upsurge in consumer goods imports is unwarranted, since tariffs and exchange rate management should prevent such an outcome.

57. An important second theme of industrial and trade policies is to phase out unnecessary legal and bureaucratic impediments which impose time delays and costs on producers, without contributing to economic efficiency. Among others, the Urban Land Ceiling Act, the Companies Act and the Sick Industrial Companies Act need to be reformed. Speedy restructuring, acquisitions and mergers are among the tools needed for meeting the challenge of competition. Removal of investment licensing of electronic and agro industries, and distribution and price controls on petroleum products and coal, are also part of the unfinished agenda. The consumer electronic industry can benefit greatly from competition. Last year's delicensing of the automobile industry has led to a boom in investment in automobile components and plans for producing new cars. Delicensing of consumer electronics can have more beneficial results, as

segments of the consumer electronic industry are extremely labour intensive. The time taken to reach the sale volumes needed to attract high technology segments of this industry will also be reduced.

58. The third element of the policy is to improve the ability of industry to compete, by developing and increasing the efficiency and transparency of factor markets. Convenient access to capital, technology and skills at competitive costs is essential for the economy to grow. Reform and improved regulation of equity markets, banks, insurance, debt markets and labour laws, are necessary to accelerate the growth of output and employment to levels seen in other parts of Asia. Improving the education and industrial skills of the population is also essential for sustaining equitable growth in the long term.

59. Policy reforms are beginning to percolate down to the level of State governments and State capitals. The actual benefits of new industrial investment can only accrue if investment approvals and intentions are translated into real investment, employment and production. The role of State governments is critical because land use, water, power generation and distribution and roads come under the purview of State governments. Radical changes in policy, rules and procedures will be necessary for translating the new potential into a reality that the voting public can perceive.

External Sector

60. Sustained growth of exports and direct foreign investment are the keys to sustained viability of the balance of payments. The exchange rate changes in 1991-92 and the subsequent reforms have made Indian manufacturing competitive. The inflow of foreign capital and consequent increase in inflation, which led to an appreciation of the real exchange rate over the past two years, has not changed this fact. Nevertheless, there are still too many policy constraints on exports compared to our competitors. The labour policy for exporters is much more adverse than in competitor countries, inhibiting flexibility and responsiveness to world markets. Many exportable goods are still subject to small industry reservations, inhibiting growth of volumes and the build-up of a base for quality exports. The foreign investment policy has not yet attracted the wave of labour intensive consumer goods producers which generated high growth of exports and employment in South-East Asia and China. These policies need to be liberalised to encourage formation of export linkages.

61. It is essential for a sustained high growth of exports that administrative procedures and practice accord genuine fast-track priority to exporters. Administrative procedures relating to import licensing, customs and duty drawback need to be radically reformed. For instance, if export-import documentation was fully computerized, all recording, checking and approval could be done instantaneously at the customs house. A genuine pass-book system could be operated, with no need for individual "licensing" and duty drawback procedures for each export order.

62. The overall management of the balance of payments, foreign exchange reserves, external debt and the exchange rate will continue to demand vigilance and capacity for flexible response as the integration of India's foreign trade and payments with the world economy deepens progressively. Recent events in the international arena have vindicated India's balance of payments strategy of pursuing a low current account deficit, a cautious approach towards full capital account convertibility, strong foreign exchange reserves, effective controls on external debt (including discouragement of short-term liabilities), a flexible market-determined exchange rate, encouragement of foreign direct investment and, above all, strong export growth. In an inherently uncertain world environment, management of India's balance of payments will need unceasing vigilance, mature judgement, prudent anticipatory action and timely response to unpredictable developments.

Agriculture

63. With two-thirds of our work force deriving their livelihood from agriculture and allied activities, the performance of this sector still holds the key to improvements in real incomes and living standards of the bulk of India's population. Economic reforms over the past three and half years have gone a long way towards improving the relative profitability of agriculture as compared to industry. The reduction in controls on domestic and foreign trade in agricultural commodities has substantially expanded the opportunities for income gains. But much more needs to be done to broaden the pattern of agricultural development, eliminate remaining biases against this sector and improve the availability of key inputs, credit and extension services on a sustainable basis.

64. The decline in public investment in agriculture (mainly undertaken by States) is a major source of concern. Realistically, resources for higher public investment can only become available if the current large subsidies on agricultural inputs can be scaled down. To take one example, it is vital to improve cost recovery in irrigation to cover operation and maintenance costs and a substantial part of capital costs. One way that the irrigation subsidy could be phased down is by decentralising the distribution of irrigation water. A hierarchy of irrigation cooperatives could be formed at different levels who would also be responsible for maintenance of channels. State

irrigation departments could be converted into public sector units to impart greater commercial orientation to their functioning. Such a re-orientation would have a dual impact, directly on productivity, and by fostering rural private investment. The imbalance in the primary plant nutrients - Nitrogen (N), Phosphate (P) and Potash (K) consumption, is also a cause for concern. The actual NPK consumption ratio was 9.3:3.1:1 in 1993-94 for India as a whole as against the ideal average ratio of 4:2:1. This imbalance is a reflection of distortions in relative prices. If not corrected, it is likely to damage the environment and harm productivity.

65. Large increases in procurement and minimum support prices of foodgrains have undoubtedly strengthened production incentives for these crops. But they have also contributed to general inflation through large increases in the prices of wage goods and diversion of food stocks from private trade to the Food Corporation of India, with its attendant high unit costs of storage, handling and distribution. Rising prices for foodgrains particularly have adverse consequences for the poorest segments of the rural population, most of whom have very limited access to the Public Distribution System. There is urgent need to revamp the Public Distribution System to meet more effectively the needs of more vulnerable sections of society.

66. As pointed out in last year's Economic Survey, there is a large unfinished agenda of agrarian reform, special support programmes for small farmers, strengthening of rural credit, revival of agricultural cooperatives, revitalization of Panchayats and other grass-roots bodies in the enormous task of agricultural development. That agenda remains as demanding and urgent as ever before. The tasks of delicensing agro-industries, like sugar, and eliminating restrictions on agro exports and domestic trade also remain unfinished. The Uruguay Round of multilateral trade agreements has opened up vast new opportunities in world trade in agriculture. Indian agriculture cannot afford to lag behind in availing these opportunities.

Infrastructure

67. The single most important constraint on India's economic development in the next few years is likely to be the availability of good quality infrastructure, especially power, roads, water and telecommunications. The availability of these non-tradeable services is also essential for international competitiveness and export dynamism. In the past, infrastructure services were largely a monopoly of Central and State governments. They are now being opened up to private investment and, in some cases, to private management and operation. This process needs to be widened, deepened and accelerated and the modalities of the transition made as transparent as possible. However, because of gestation lags, the bulk of overall supply will remain dependent on the performance of public entities for quite a few years.

68. Most infrastructure sectors call for a two-pronged approach: measures to improve current levels of operational efficiency and productivity and steps to ensure adequate investment for the future. To use the power sector as an illustration, a one percentage point improvement in the average plant load factor of thermal plants would effectively add 390 megawatts of power supply each year, which could cost about Rs.1250 crore in terms of new capacity. While there is substantial scope for productivity improvements in generation, transmission and distribution, there is no escape from ensuring adequate investment in future capacity. Investment requires resources, which either have to be generated from current operations or attracted through an acceptable policy framework. In either case, this will entail substantial revision of electricity tariffs and drastic reduction in subsidies. The brute fact is that for power sector investments to be viable, the user of electricity must pay for its cost. Guarantees and counter-guarantees can, at best, provide a temporary breathing space for carrying out radical reform of institutional arrangements, operating practices and tariffs in State Electricity Boards. They cannot substitute for the necessary reforms.

Social Sectors and the Poor

69. The Government has been following a three-pronged strategy for poverty alleviation:

(i) the overall programme of economic reform is designed to promote rapid, broad-based, employment-intensive economic growth;

(ii) Spending on direct anti-poverty programmes has been greatly increased and new programmes have been launched;

(iii) Spending on social sectors, such as education and health, has also been stepped up by the Central government.

70. But simply increasing budgetary allocations for social sectors and poverty programmes is not enough. The emphasis must now shift to revamping delivery systems and administrative structures for all these programmes to make them much more accountable and responsive to the beneficiaries they are intended to serve. Leakages and malpractices must be curbed. The focus of public sector activity and attention must shift decisively towards these areas. It is easy to state these goals; much harder to implement them. But if the scourge of poverty is to be effectively lifted, we must be steadfast in our efforts.