MACRO-ECONOMIC FRAMEWORK STATEMENT

The Indian economy entered the financial year 2008-09 with a buoyant growth rate. The average growth rate during the recent four years namely 2004-05 to 2007-08 has been at record level close to 9 per cent when compared to the average growth rate of 5.6 per cent recorded during the preceding four years. There has been a moderation in the growth in the current year due to the fallout of the global crisis. The progress made on the fiscal consolidation has been satisfactory in the post-FRBM period till 2007-08. The Budget Estimates for 2008-09 was envisaged keeping fiscal deficits below that set under the FRBM Act, 2003. However, the recent global meltdown and its ramifications on the domestic economy have necessitated counter-cyclical fiscal measures that may enhance the expenditure outflow leading towards temporary deviation from the FRBM targets. Compared to other emerging economies, India has several strengths that can help mitigate the adverse effects of global financial crisis. The Government has taken several measures in this direction and the economy is expected to return to the high growth trajectory.

ECONOMIC GROWTH

2. For the H1 2008-09, the growth rate at 7.8 per cent is lower than 9.3 per cent recorded in the H1 2007-08. At the sectoral level, growth in H1 2008-09 is higher in mining and quarrying (4.4), construction (10.5) and in community, social and personal services (8.0), but substantively lower in agriculture, manufacturing and electricity, gas & water supply vis-a-vis the corresponding period in 2007-08. There has been some slowdown in the growth rate of Gross Fixed Capital Formation from an average of 15.0 per cent per annum over the last three years (2005-2008) to 11.4 per cent for H1 2008-09, though its growth rate in 2008-09 Q2 at 13.8 per cent was higher than 9.0 per cent in Q1. There has also been some slackening in the growth rate of Private Final Consumption Expenditure from an average of 7.1 per cent per annum in the last three years (2005-08) to 6.5 per cent in for H1 2008-09. Its growth in 2008-09 Q2 at 5 per cent dropped from 8 per cent in Q1.

3. The Central Statistical Organisation (CSO) has released the Advance Estimates for 2008-09. The Gross Domestic Product at factor cost is placed at Rs.33.52 lakh crore during 2008-09, indicative of a growth of 7.1 per cent in 2008-09 as compared to the growth of 9 per cent in 2007-08. The moderation in growth for 2008-09 is mainly attributed to sharp slowdown in growth in industry to 4.8 per cent from 8.1 per cent in 2007-08. Within industry, the manufacturing and construction activity are expected to moderate sharply. However the decline in these sectors is expected to be offset partially by an increase in growth in the Mining and Quarrying sector. Growth in agriculture, forestry and fisheries is estimated to decline to 2.6 per cent in 2008-09 as against a growth of 4.9 per cent in 2007-08. Services is slated to grow at 9.6 per cent in 2008-09 as compared to a growth of 10.9 per cent in 2007-08, with growth in 'Financing, Real estate, Insurance and Business services declining, and growth in community, social and personnel services increasing. Viewed from the demand side, the growth in Gross Domestic Product at market prices is expected to grow at 7.1 per cent. Private Final Consumption expenditure growth is expected to decline from 8.1 per cent in 2007-08 to 6.7 per cent in 2008-09, while Government Final Consumption Expenditure is expected to increase sharply from 7.4 per cent to 16.8 per cent during the same period. Growth in Gross Fixed Capital Formation is projected to decline from 12.9 per cent in 2007-08 to 8.9 per cent in 2008-09.

4. As per the Fourth Advance Estimates of agricultural production released by the Directorate of Economics & Statistics, the total foodgrains production in 2007-08 has been estimated at 230.7 million tonnes, 13 million tonnes higher than the 217.3 million tonnes in 2006-07 (final estimate). For three consecutive years, foodgrains production has recorded an average annual increase of over 10 million tonnes. The cumulative South West monsoon season rainfall was marginally lower than the long period average with special and regional disparities. During 2008-09 the area sown under Kharif was 2.3 per cent less than the normal area sown of 1018.83 lakh hectares. In the first advance estimates of kharif production for 2008-09, production of foodgrains, oilseeds, cotton and sugarcane is estimated at 115.3 million tonnes, 17.9 million tonnes, 23.9 million bales and 294.7 million tonnes, respectively. While compared to the First Advance Estimates of 2007-08, this represents an increase of 2.8 per cent in foodgrains production. The encouraging news for Rabi 2008-09 is the area sown of all crops is estimated to increase by 3.8 per cent.

5. As per the index of industrial production (IIP) data released by CSO, the overall growth in April- November 2008 is estimated at 3.9 per cent year-on-year basis compared to a growth of 9.2 per cent in April-November 2007. The decelerating growth phase which kicked in the second half of 2007-08 has been continuing in the 2008-09 H2. Deceleration in growth was significant for manufacturing and electricity sectors, and somewhat moderate for the mining sector. The Index of six core-infrastructure industries having a combined weight of 26.7 per cent in the IIP registered a drop in growth to 2.2 per cent (provisional) in November 2008, compared to a growth of 5.1 per cent in November 2007. During April-November 2008-09, six core-infrastructure industries registered a growth of 3.6 per cent (provisional) as against 6.4 per cent during the corresponding period of the previous year. In terms of use based classification, while basic goods, capital goods and intermediate goods registered a sharp decline in growth during 2008-09 (April- November) as compared to corresponding period of previous year, consumer goods registered an increase in growth. The growth in consumer goods was led by growth in consumer non-durables.

FISCAL CONSOLIDATION

6. Progress on the fiscal consolidation front has been satisfactory in the post-FRBM period till 2007-08. The Budget estimates for 2008-09 envisaged keeping fiscal deficit well below that set under FRBM Act, 2003. However, due to increase in global oil prices, additional commitments owing to conscious shift in expenditure in favour of health, education, the social sector and the fiscal stimulus to overcome the impact of global financial crisis on the real economy, it was felt that it might be difficult to adhere to the targets envisaged earlier. A fiscal stimulus in a year of stress on the macro-economy is in line with international best practices. The gross tax-GDP ratio for the centre, which stagnated at around 8-10 per cent range in the pre-FRBM period, increased to 11.4 per cent in 2006-07 and further to 12.5 per cent of GDP in 2007-08 (Provisional Actual). The 2008-09 Budget placed this at 13.0 per cent of GDP. In the first nine months of 2008-09, gross tax receipts of the Centre increased by 9.6 per cent over corresponding period of the previous year. Revenue expenditure increased by 39.2 per cent in the first nine months (April-December 2008-09). The apparent decline in capital expenditure by 40.2 per cent during the period owes to the transaction relating to acquisition of equity of the State Bank of India during the previous year (2007-08), which provides for a higher base. In the first nine months of the current year (April-December 2008), the total expenditure was 79.5 per cent of Budget Estimates (BE). Non-debt receipts during the same period in the current year was 61.4 per cent of BE. The receipts were sufficient to cover only 63.5 per cent of the expenditure leaving a fiscal deficit of Rs.2,18,262 crore. This is higher as compared with the fiscal deficit of Rs.77,578 crore reported last year during the same period. The revenue deficit up to December 2008 was Rs.1,73,830 crore. This is also higher as compared to the figure of Rs.39,210 crore reported up to December, 2007. The non-debt receipts (excluding acquisition of RBI stake in SBI) increased by 4.9 per cent over the corresponding period last year. The total Expenditure growth was 36.1 per cent, if the one time expenditure of Rs.35,531 crore on acquisition of RBI stake in SBI is adjusted. As per present reckoning, the fiscal consolidation process would resume once the impact of global financial crisis is overcome, which is likely in the second half of next fiscal.

MONETARY DEVELOPMENTS

7. The surge in capital inflows in 2007-08 of the order of 9.2 per cent of GDP led to a growth of 30.9 per cent in Reserve Money (M_0) much higher than the level envisaged for the year in the Annual Policy Statement of the RBI. Broad Money (M_3) in 2007-08 grew by 20.8 per cent against a level of 17.0-17.5 per cent projected by the RBI. As against a projection of 16.5-17.0 per cent for 2008-09, revised to 19.0 per cent in the third quarter review of Monetary policy by RBI, M_3 recorded a growth rate of 19.6 per cent as of January 2, 2009. In the first quarter 2008-09, Reserve Money (M_0) grew by 29.3 per cent and Broad Money (M_3) grew by 20.8 per cent. By Mid-June 2008, WPI based inflation, driven by exogenous factors (such as global commodity price rise particularly crude oil), had reached double digits. Thus, the RBI had to tighten the monetary policy stance to prevent engendering of inflationary expectations. In a series of policy announcements, the RBI raised: CRR to a level of 9 per cent as on August 30, 2008; and repo rate to 9.0 per cent on August 30, 2008.

8. Capital flows moderated in the first quarter of the current financial year itself and coupled with the tight monetary policy stance led to a situation of liquidity crunch. This crunch was accentuated by the global financial crisis in September 2008 with the collapse of some major global financial institutions. A decline in the global commodity prices, particularly petroleum crude helped ease the monetary policy stance, which was unwound in a series of policy measures in October 2008 through to January 2009. These, inter alia, included: reduction in CRR to a level of 5.0 per cent effective January 17, 2009, reduction in repo rate to a level of 5.5 per cent on January 2, 2009; reduction in reverse repo rate to a level of 4.0 per cent on January 2, 2009; reduction in the Statutory Liquidity Ratio by one percentage point to a level of 24 per cent of NDTL (Net Demand and

Time Liability) w.e.f. November 8, 2008. Following these measures, liquidity position has eased considerably. The Yield-to-Maturity on 91 day Treasury bills which had increased to 7.23 per cent on March 26, 2008 decreased to 4.79 per cent on January 28, 2009.

9. In the first nine months of the current financial year (April-December 19, 2008), Reserve Money decreased by (-) 4.5 per cent against increase of 14.0 per cent in corresponding period of fiscal 2007-08; Broad money grew by 10.6 per cent (April-December 19, 2008) against 11.7 per cent in corresponding period of last year; bank credit grew by 12.0 per cent (April-December 19, 2008) against 10.0 per cent in corresponding period of last year. The moderation in the growth in the monetary aggregates has been more pronounced since the second quarter. Non-food credit by scheduled commercial banks (SCBs) expanded by 23.9 per cent on y-o-y basis as on January 2, 2009, higher than 22.0 per cent a year ago. For the same period, real credit growth increased from 17 per cent in January 2008 to 18 per cent in January 2009. The higher expansion in credit growth relative to the expansion in deposit growth was reflected in the credit-deposit ratio on y-o-y of SCBs at 73.48 per cent as on January 2, 2009 compared to 71.83 per cent recorded a year ago.

INFLATION

10. Headline inflation measured in terms of the WPI, were in the range of 3.8-6.9 per cent in 2003-04, 4.3-8.7 per cent in 2004-05, 3.3-5.7 per cent in 2005-06, 3.7-6.7 per cent in 2006-07 and 3.1-8.0 per cent during April-March 2007-08. The current fiscal year started with inflation at close to 8 per cent and reached double digits in the first week of June. It rose to a high of 12.9 per cent in the first week of August and continued to be over 12 per cent in September. In October 2008 it came down to below 12 per cent and subsequently witnessed a sharp fall into single digit in the first week of November 2008. It has continued to decline since then except for a brief upswing in mid January 2009 and as of the week ending January 31, 2009 was 4.39 per cent. Cumulative increase in first 43 weeks of the current fiscal year at 1.5 per cent is significantly lower than the build up of 4.1 per cent in the first 43 weeks of 2007-08.

11. Annual (year-on-year) WPI inflation rate stood at 4.39 per cent on January 31, 2009 compared to 9.1 per cent for primary articles, (-)3.5 per cent in fuel group and 5.5 per cent in Manufactured products. Inflation for the three broad groups of commodities indicate hardening of prices for all the three major groups over the previous year, but some deceleration in inflation for fuel and power and manufactured products continued since first week of November, 2008. The continued rise in the inflation for primary articles has its implications for the food, non food and minerals index as well as the index for some essential commodities.

12. Average annual WPI inflation decelerated from 6.5 per cent in 2004-05 to 4.4 per cent in 2005-06, 5.4 per cent in 2006-07 and 4.7 per cent in 2007-08. Inflationary pressures got exacerbated during 2008-09 by hardening of international prices of crude oil, minerals and metal related products. With prices of these items shooting up in world markets, imported inflation played a crucial role in domestic inflation in 2008-09. However, because of the higher inflation in the early part of the year, the average inflation of 52 weeks reached at 9.2 per cent on January 24, 2009 was considerably higher than 52-weeks average of 4.6 per cent in the corresponding period of the previous year. In respect of primary articles, the average 52-weeks inflation at 10.6 per cent as on January 24, 2009 was higher than the average 52-weeks inflation of 8.0 per cent in the previous year.

EXTERNAL SECTOR

13. The trade to GDP ratio, an indicator of trade openness, increased from 22.5 per cent of GDP in 2000-01 to 36.2 per cent of GDP in 2007-08 (on BOP basis). If services are included, this ratio increases further to 48.3 per cent of GDP in 2007-08. India's merchandise exports and imports (in US$, on customs basis) grew by 28.9 per cent and 35.4 per cent respectively in 2007-08. Despite the global recession, the first nine months of the current year witnessed a export growth of 17.1 per cent and reached US $ 132 billion, which constitutes nearly 66 per cent of the year's export target. Major drivers of export growth during April-September 2008 were petroleum products, engineering goods, agricultural and allied products and chemicals & related products.

14. During 2008-09 (April-December), total imports grew by 31.5 per cent in US $ terms. POL and Non POL imports grew by 44.8 and 25.3 per cent respectively. The merchandise trade deficit in April-December 2008 was at US$ 94 billion which was 59 per cent higher than the trade deficit of corresponding period of the previous year. India's export of services grew by 22.1 per cent to US$90 billion in 2007-08 mainly due to software services. Services exports were almost 54 per cent of merchandise exports in 2007-08. During 2008-09 (April-September), services exports grew by 21.5 per cent mainly due to software and financial

services which grew by 22 per cent. However, business services with a share of 18 per cent witnessed a lower growth of 13.7 per cent in April-September 2008 over the corresponding period of the previous year.

15. The signs of global financial crisis were evident in India's Balance of Payment (BOP) position in the first half of 2008-09. During the first half of the year (April –September 2008), trade deficit increased to US $ 69.2 billion (11.8 per cent of GDP) as compared to US $ 43.2 billion (8.2 per cent of GDP) during the same period last year. Similarly, Goods and Services deficit widened to US$ 46.3 billion (7.9% of GDP) as compared to US$ 25.2 billion (4.8% of GDP) last year. Invisible balances however showed an upward trend, increasing from US$ 32.3 billion (6.2% of GDP) in 2007-08 (April- September 2007) to US$ 46.8 billion (8% of GDP) during 2008-09, partly negating the effect of higher Trade Deficit. The Current Account Deficit (CAD), as a result, was US $ 22.3 billion (3.8% of GDP) in the first half of 2008-09 as against US $ 11 billion in 2007-08 (2.1% of GDP).

16. There has been portfolio net outflows to the extent of US $ 5.5 billion during April-September 2008 as a fallout of the global crisis, vis-a-vis inflow of US $ 18.4 billion in April-September 2007. The silver lining, however, has been a step up in foreign direct investment (FDI) to US $ 14.6 billion as against US$ 4.9 billion during the corresponding period last year showing an increase of 198 per cent. In 2007-08, India's trade deficit had widened to US $ 91.6 billion (7.8 per cent of GDP) from US $ 61.8 billion (6.7 per cent of GDP) in 2006-07. The CAD, however, was at US $ 17 billion, which was 1.5 per cent of GDP as against US $ 9.6 billion (1 per cent of GDP) in 2006-07. This was largely on account of surplus of US $ 74.6 billion in invisible account, which was 6.4% of GDP in 2007-08. Net capital flows, as a percentage of GDP has increased from 4.9% in 2006-07 to 9.2 % in 2007-08 due to increase in FDI, Portfolio, ECB, Short Term Credit.

17. The composition of capital flows has been changing. The salient feature was the 55.9 per cent increase in foreign direct investment inflows to US$ 36.8 billion in 2007-08 from US$ 23.6 billion in 2006-07. The trend continued in the current fiscal with gross FDI flows reaching US$ 14.6 billion during the first half of 2008-09 as compared to US$ 4.9 billion during corresponding period in 2007-08. FDI inflows were broad based and spread across a range of economic activities like financial services, manufacturing, banking services, information technology services and construction. Net direct investment abroad shot up to US$18.84 billion in 2007-08 from around US$ 15.0 billion in 2006-07. It has, however, declined to US$ 6.1 billion in the current year (April – September 2008).

18. With the demand – supply imbalances in domestic foreign exchange market, due to repatriation of portfolio investment by Foreign Institutional Investors to replenish US $ balances abroad, there has been sharp decline in Rupee exchange rates and the currency depreciated by 17.7 per cent against the US dollar during current fiscal between April – December 2008. The Rupee depreciation against the US dollar over the past twelve months on a year-on-year basis (December 2008 over December 2007) at 18.9 per cent was even higher. This rupee volatility has consequent implications for exporters, importers and debt service payments.

19. The Reserve Bank of India has intervened in the foreign exchange market to stabilize the currency. The foreign exchange reserves, therefore, declined from the peak of US $ 314.6 billion in May 2008 to US $ 255 billion as on 9th January, 2009. Since foreign exchange reserves are denominated in US dollars, the changes in inter se exchange rates affect the reserve levels through the valuation route.

20. The financial crisis in the US and other developed countries that took the full blown form from September 2008 has had a worldwide impact including India. Estimates of growth for the world economy for 2009 have been successively lowered by multilateral institutions. In view of the magnitude of the crisis, the Government initiated pro-active measures that included a fiscal stimulus, along with the Reserve Bank of India that initiated appropriate monetary measures. The overriding policy objective has been to minimize the impact of global financial crisis on the Indian economy. The policy stance at this juncture needs to be flexible, so that the growth momentum is restored. At the same time, it is envisaged that the process of fiscal consolidation will be resumed from the ensuing fiscal year.

Annex - I

MACROECONOMIC FRAMEWORK STATEMENT
(ECONOMIC PERFORMANCE AT A GLANCE)

Sl. No.	Item	Absolute value April - December 2007-08	Absolute value April - December 2008-09	Percentage change April - December 2007-08	Percentage change April - December 2008-09
	Real Sector				
1	GDP at factor cost (Rs. thousand crore)[F]				
	a) at current prices	4320.8 [QE]	4989.8 [AE]	14.3	15.5
	b) at 1999-2000 prices	3129.7 [QE]	3351.6 [AE]	9.0	7.1
2	Index of industrial production [(1)]	258.6	268.7	9.2	3.9
3	Wholesale price index (Base 1993-94=100)[(2)]	219.0	230.1	4.8	5.1
4	Consumer price index (2001=100)[(3)]	134.0	147	5.5	9.7
5	Money Supply (M3)(Rs. hundred crore)[(4)]	3892.7	4235.1	11.7	10.6
6	Imports at current prices*				
	a) In Rs. crore	693445	1003947	13.0	44.8
	b) In US $ million	171718	225809	27.8	31.5
7	Exports at current prices*				
	a) In Rs. crore	454997	585594	9.2	28.7
	b) In US $ million	112737	131990	23.5	17.1
8	Trade Deficit(in US$ million)*	-58981	-93819	…	…
9	Foreign currency assets				
	a) In Rs. crore	1050485	1194790	39.6	13.7
	b) In US $ million	266553	246603	56.6	-7.5
10	Current Account Balance (In US$ million)[@]	-17034	-22332		
	Government Finances (in Rs. crore) [#]				
1	Revenue receipts	355,646	375,937	26.6	5.7
2	Tax revenue (Net)	295,994	309,927	27.5	4.7
3	Non-tax revenue	59,652	66,010	22.4	10.7
4	Capital receipts (5+6+7)	118,607	221,279	15.4	86.6
5	Recovery of loans	3,304	2,974	-58.5	-10
6	Other receipts	37,725	43		
7	Borrowings and other liabilities	77,578	218,262	-18.2	181.3
8	Total receipts (1+4)	474,253	597,216	23.6	25.9
9	Non-Plan expenditure	337,090	426,419	23.8	26.5
10	Revenue Account	280,050	403,758	10.3	44.2
	Of which:				
11	Interest payments	111,764	123,735	20.7	10.7
12	Capital Account	57,040	22,661	209.8	-60.3
13	Plan expenditure	137,163	170,797	23.0	24.5
14	Revenue Account	114,806	146,009	22.3	27.2
15	Capital Account	22,357	24,788	26.9	10.9
16	Total expenditure (9+13)	474,253	597,216	23.6	25.9
17	Revenue expenditure (10+14)	394,856	549,767	13.6	39.2
18	Capital expenditure (12+15)	79,397	47,449	120.4	-40.2
19	Revenue deficit (17-1)	39,210	173,830	-41.3	343.3
20	Fiscal deficit {16-(1+5+6)}	77,578	218,262	-18.2	181.3
21	Primary deficit (20-11)	-34,186	94,527	-1639.9	-376.5

[QE] Quick Estimates [AE] Advance Estimates

F Period relates to April-March ;
** on Customs basis; comparison for current year is on provisional over revised basis.*
(1) Base:1993-94=100 Period relates to April-November;
(2) as on 24th January(Point to point)
(3) End of December (Point to point)
(4) variation during financial year(upto 19th December)
 # Figures as reported by Controller General of Accounts, Ministry of Finance.
@ for 2007-08 the period relates to April-March and for 2008-09 the period relates to April-September.