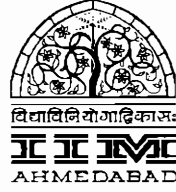

Working Paper

INDIAN ECONOMIC FORECAST
MARCH 1993

By

A.B. Rastogi

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INDIAN ECONOMIC FORECAST : MARCH 1993

by

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ABSTRACT

Although not spelt out by the Finance Minister as preparing ground for the EFF/ESAF loan from the IMF, it is a path-breaking budget with a strong emphasis on restructuring the economy and the augmenting supply side of the economy. The medium-term funding facility from the IMF/WB with concessional loan would act as an insurance and paper over the ripples generated in the goods market and financial assets market due to restructuring of the economy. To ameliorate short term consequences on labour, the labour market reforms are being handled in a politically deft manner. The economic strategy in the medium term is quite clear; go for growth and supply side incentives and push for structural reform. Monetary policy of the government is quite tight and as inflation falls rapidly the government should bring down interest rates quickly to maintain the momentum of private sector investment to enhance productive capacity of the economy. The success of the reform programmes hinges on sustained growth of agricultural and non-agricultural sectors which is inexorably linked to productive investment in these sectors.

Indian Economic Forecast : March 1993

by
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1. Overview

Behind the headline grabbing numbers of the 1993-94 budget lie the hard facts of fiscal compression, extremely tight monetary policy stance and supply-side economics *à la* the World Bank and the IMF style and the emphasis is on the rate of growth of national output, allocation and efficient use of resources. This should result in squeezing the inflation out of the system if the two assumptions underlying the budget come true, namely, an average agricultural production and stable crude oil prices this year. There are good reasons to believe that both assumptions would stick.

From the Economic Survey 1992-93 and the Budget documents of 1993-94 we piece together a Medium Term Financial Strategy (MTFS) of the government which will be the backbone of Policy Framework Paper (PFP) going to be submitted by the Finance Minister to the IMF for the Enhanced Fund Facility/Enhanced Structural Adjustment Facility (EFF/ESAF). In line with the PFP, submitted by the government, further restructuring of the economy would take place in the medium term.

Despite world-wide recession, India has been managing its economy reasonably well in the short-run due to its inherent strength. The unfulfilled potential for development is so vast that with appropriate policies, India can emerge as a major growth centre in the world economy. A dash to growth will prepare strong grounds to push reforms in the labour sector and financial sector. In the present macroeconomic disinflationary environment, it seems that the RBI would be able to cut interest rates at least by two percentage points or more in this year itself. The long shadow of security scam is slowly fading and a strong middle class is emerging in Indian market towns which is almost at par with their urban brethren. A booming demand for durable goods from this section is palpable in these towns.

The 1993-94 budget has laid foundation for supply-side reforms with 'human face' and as MTFS is followed it is more than likely that we may see real GDP doubling in next ten years and real per capita income doubling by the year 2005.

2. Political Economy of Structural Reforms

When the economic failure of a government manifests itself in macroeconomic imbalances, an unhealthy cosy relationship between national bureaucracy, politicians and protected industry gets developed. It interferes with the development of a competitive climate which is a vital stimulant for efficiency and productivity. Structural reforms are intended to bring about efficiency gains in the long run. The question commonly posed is not whether to reform or not to reform but rather how best to implement these reforms. For this, one has to understand not only basic economics but the political analysis of the reform process as well. It is better to think of a set of economic ministries, each having its own agenda and timetable. Macrostability -- a low rate of inflation and a manageable

balance of payment position -- should be emphasised at the outset, because this is a necessary precondition for the successful development of a market economy. A country should align quickly to internal relative prices for tradable goods and services with external relative prices, because appropriate relative prices are critical for obtaining the appropriate allocation of resources in the economy. In an economy where large stocks of productive assets are held by the government and a substantial part of investment is done by the government, the transformation effort lies in knowing what to do with large state enterprises which require a great deal of time to resolve and ultimately the social acceptability of the process. To do so, in a country like India, a comprehensive national poverty alleviation strategy is required which can address the transitional costs of reform.

The Fund/Bank emphasises not only stabilisation but also restructuring of such economies in medium term so that the economies are able to stand on their own feet. Hence, there is a strong undercurrent in the Fund/Bank supported restructure programme that social infrastructure should be enhanced and not allowed to deteriorate. In a democracy it makes immense sense because if large number of people can enjoy the fruits of restructuring, the government is in less trouble. The chances of food riots erupting or strikes being held reduce substantially. In case of India particularly, this means that International Development Agencies (IDA) loans, which are soft loans, could be utilised to improve the social infrastructure of the country. This is the underlying reason for emphasis on rural development programme in the budget.

It is generally known that policy prescription for stabilisation suggested by the Fund is based on a simple monetary model, where emphasis is to reduce government expenditure and curtail credit in the economy to bring inflation under control and to improve the balance of payment position. Therefore, stabilisation implies cut, in real terms, on social expenditure etc. which is painful to common man and in the past has created disenchantment in some countries. The common man does not see the future benefit of reduction in inflation. He is more concerned about health facility, employment opportunities etc. which take a severe beating during the stabilisation phase. If this is taken care of there are few in the dissatisfied lot and the government remains stable. On the other hand the Fund can ask for deeper cuts which affect 'rent seeking' behaviour or inefficient allocation in the economy. The big and 'prestigious' projects which increase public expenditure are forced to be put on back burner.

Therefore, in India, challenge to the reform process is there not only from the opposition but also from the ruling party as well as from bureaucracy. Some politicians interested in retaining patronage are opposed to the more 'market friendly' liberalisation. They would like Dr. Singh to follow and pursue a more lobby-friendly variant instead, the kind that many Indian businessmen would also be very comfortable with. In his pep-talk to senior civil servants in Delhi, the Prime Minister raised the growing concern of inertia with officers not willing to stick their necks out and implement decisions.

In the spirited defence of the restructuring process, Lord Professor Meghnad Desai of the London School of Economics -- a working peer of Labour Party and a die-hard critique of market economy -- said that the reform programme is anti-poor. Further, he said that by no stretch of imagination could the policies of the 1947-1991 period be called 'pro-poor'. His challenge to his audience, consisting of top bureaucrats and technocrats in Delhi, to provide instances of how the poor had benefited in the mixed economic model since independence got no convincing answer. According to his estimates, India in the name of socialism wastes as much as 15% of its GDP.

In fact, it is widely accepted now that inaction and postponement have their costs like pushing the country into a poor, inflationary, low growth economy. If India is to be an economic power, it has to gamble on growth. That is why there is no ideological risk to the reform process in India. This is evident from the alternate budget proposals of the opposition party. With the sole exception of its relative emphasis on domestic liberalisation, the BJP's macro-economic policy is not fundamentally different from that of the Congress party. However, economics of construction can not follow politics of destruction. This point is yet to be appreciated by some political parties.

Nevertheless, the political parties in India are redefining the role of government in the country's economic activities. The government should certainly intervene at a time of crisis, but under ordinary circumstances it must allow market forces to operate.

3. Medium Term Financial Strategy

The stabilisation programme has been almost successful. At present, inflation is under control and the external sector imbalances are manageable, albeit with borrowed funds, as the decision to go for restructuring was taken as soon as the stand-by loan was taken from the IMF. Some of the government actions, especially in opening up of the economy, seem to contradict the objective of the stabilisation programme in the short run. However, these policies must be seen in the light of restructuring of the economy. The idea of supporting these programmes by the multilateral agencies is that in transition there are some economic costs involved and hence the restructuring programme should be supported by providing loans on easy terms but with tough conditions. Restructuring of the economy calls for reforms in trade sector, financial sector, agricultural sector, labour sector and public sector. Reforms in the public sector are interwoven with the labour sector reforms. For these sectors government is seeking soft loans from the Asian Development Bank (ADB), the IMF and the World Bank. Some of these loans which are meant to enhance the productive capacity of the economy have already been granted and others are being negotiated. The extended fund facility (EFF)/extended structural adjustment facility (ESAF) of the Fund, on the other hand, is to tie over the external sector imbalances which may arise due to reform process and repayments of past loans like stand-by loans and roll over of short-term commercial loans etc. Moreover, an IMF loan gives a clear signal to the international financial community that restructuring process is on course and productive capacity of the economy shall improve in future. There is no other comparable mechanism by which the international community can be convinced to invest in the country.

The EFF/ESAF programme may commence from June 1993 or November 1993 and will be a three year programme. Over the period 1993-96 the IMF expects to offer at least $7 billion support to India. The range of fund available is $6 billion to $9 billion and the exact amount will depend on the PFP agreed upon between India and the Fund. The EFF talks are to be held in the third week of March for two weeks. The EFF loan is expected to flow in after the current 20-month stand-by loan of $ 2.2 billion comes to an end by June 1993.

The Fund would undertake the third review of the $2.2 billion stand-by loan in March. The two week long review will evaluate whether the government will be in a position to meet March end targets. On the basis of the review report to the IMF executive board the decision would be taken whether the last instalment of the stand-by loan should be released in May 1993. Along with the

third review discussion on the EFF including soft loan under ESAF will also be discussed. The Finance Ministry is working towards finalising the PFP that will guide the IMF and World Bank's three-year support programme for India. The final decision on both -- the last instalment of the stand-by loan and the EFF/ESAF loan -- will be taken by the IMF board some time in April 1993.

The 1993-94 budget has been used by the government to send the necessary signals to the Fund/Bank for its readiness to restructure the economy. The draft PFP is expected to emphasise two areas of economic reforms which the IMF views as a priority area for the first year of the three year programme. These are tax policy reforms and public enterprise reforms.

Controversy is raging on the amount and the timing of the EFF/ESAF loan. The IMF, in the past, has preferred a gap between a stand-by loan and an EFF arrangement. The argument has been to borrow only when there is a clear need. The estimates of external exceptional finance gap has declined from $3 billion to $2.6 billion now as official reserves of the country have gone up. The current debate is whether to go for EFF now or after six months. The $1 billion soft loan component in the overall EFF facility to India will expire in November 1993. But the ESAF may be extended beyond November if required. The Finance Minister wants to have an inflow of $3 billion annually for the next 2-3 years as an insurance against the rainy day -- or shall we say, against a wide spread drought -- and therefore, the bigger the loan the better. It is better to have such a safety valve. The loan sanctioned by the Fund under the EFF depends on their *Weltanschung* - view of the world and availability of funds with them.

However, as far as timing is concerned, it has to do with the credibility of the restructuring programme. In fact, if the IMF board refuses to release the third instalment of the stand-by loan in March 1993, it will send strong signals to the international financial community that the stabilization targets have not been met and probably they will not be met. Fortunately for India, had this been the case or the political will to restructure the economy were lacking, the budget would not have sent the strong signal of restructuring to world community at large. Similarly, a delay in agreement on the EFF also would downgrade the credibility of the restructuring programme as rational agents would perceive it as the likelihood of failure of the programme targets coming from future policies. Not only that, the whole timetable, if postponed by another six months, may interfere with the state assembly election timetable due this year.

The Fund expects all the recommendations of the Raja Chelliah Committee's two reports to be implemented in 3-4 years' time and internal revenue mobilisation be given top priority. This is being emphasised by the Fund partly because it would like to see a further lowering of tariffs, which will imply loss of revenue for the Central government and therefore the need to compensate for this through higher direct and indirect tax collections; and partly because it would like the government to tap the huge reservoir of undeclared incomes in the country better.

The broad contours of the Chelliah Committee's final report on customs duty make eminent sense. Input tariffs today are quite high and almost all economists would like them to be brought down. But, they differ on the pace. Therefore, the real issue here is not economic but political. Many times reform movements have run out of steam when stretched over a period of time and so, it is better if the reforms are implemented quickly. Over-hasty reforms can often be corrected later. But if reforms are too leisurely, the chances are that they will be abandoned half way. In these circumstances, it is better to risk doing too much than too little.

As suggested earlier, from the IMF's point of view main issues, facing Indian economy, in medium-term are privatisation of PSUs and exit policy. There are other important issues in different sectors of the economy as well and what is being done in the medium term (see table 1). We analyse here the expected reforms, funding agencies of sectoral adjustment loans and government's acceptance as can be inferred from its actions.

As part of the public sector reforms the Finance Minister is reported to have said that public sector role would be drastically curtailed and no budgetary support would be available to chronically sick PSUs except in the areas of energy and transport, in three years time. He said that BIFR would ensure the sick companies are taken care of. Commenting on the allegations of large scale unemployment of workers as a result of restructuring, the Finance Minister said these fears are unfounded and once the National Renewal Fund is operational, workers would be convinced of the credible social safety net.

The World Bank sanctioned $1.6 billion loan to the power sector in January 1993 following the finalisation of a detailed package including the Bank condition that private sector - both foreign and domestic - should be allowed to invest in the power industry. The 1993-94 budget has gone a step further by providing five years tax holiday for generation and distribution of power.

In the financial sector the programme aims to improve access by the private sectors to financial savings and reduce intermediation costs and distortions in the banking system. While negotiating the Asian Development Bank loan for the financial sector the usefulness of the asset reconstruction fund, rationalisation of interest rates, prudential norms to capital adequacy, priority sector lending, computerisation, self-regulation and bank supervision were all discussed.

The ADB granted a loan of $ 300 million for financial sector restructuring. The loan implies that the government is now committed to promote competition by creating a more level playing field and freer entry and exit in the banking and development finance institutions. The ADB loan has two tranches - one has been given and the second tranche would be given by June 1994 after the conditions provided by the government are fulfilled and the ADB Board takes a fresh view on it. This means the government may well have to implement many of these decisions on restructuring the banking and financial sector before June 1994.

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Table 1: Sectoral Adjustment Loans

Sector	Expected Reforms	Funding Agencies	Remarks
Trade Reforms	1. Reduction in tariff and excise taxes 2. Free floating rupee in medium-term	World Bank, Asian Devp.Bank	1. Chelliah Committee Report 2. Institute of Public Finance and Policy is asked to prepare an implementation report
Public Sector Reforms	1. Reduce number of industries reserved for public sector 2. Managerial freedom for existing PSUs 3. No budgetary support for sick units in 3 years time 4. Sick units to be allowed to close down	World Bank	1. Rangarajan Committee is set up for disinvestment of PSU shares
Financial Sector	1. Freer entry and exit in the banking and development financial institutions 2. Development of regulatory framework	Asian Devp. Bank World Bank	1. Reforms as suggested by the Narsimham Committee 2. Banking act to be amended 3. Asset reconstruction for public sector banks in the the 1993-94 budget
Labour Sector	1. Exit policy	World Bank	1. Amendment of Industrial Disputes act and Trade Union Act
Agricultural Sector	1. Liberalise trade in agricultural products 2. Removal of export restrictions 3. Removal of Essential Commodities Act 4. Targeting food subsidies	World Bank	1. National Agriculture Policy adopted by State Agriculture Ministers

The loan is from the ADB's ordinary capital resources which is repayable over 15 years with a 3-year grace period. The interest rate will be determined in accordance with ADB's pool-based variable lending rate system for US $ loans. The ADB lending to India will also be maintained at over $1 billion over the next few years. However, fast disbursing programme loans apart from ADB's current commitment here will be $250 million probably linked to India's trade policy adjustment programme.

India could not secure the $ 500 million financial sector adjustment loan from the World Bank in December 1992. This follows a categorical assertion from the World Bank that the reforms package finalised by the Indian government was not adequate to justify the release of such a loan as it did not contain the provision of privatisation of the existing banks.

In the 1993-94 budget session amendment to Section 3(iii) of the Banking Companies Acquisition and Transfer of Undertakings Act, which provides the entire share capital of the public sector banks to be held by the Union government, is expected to be carried out. In the budget the banks have been allowed to raise money from the private sector directly. To adopt internationally accepted norms of

capital adequacy the government has given budgetary support to the banks and this year we are going to see a more transparent balance sheet of the banks. Given all these changes and other procedural changes, it is likely that India shall approach for a sectoral adjustment loan for the financial sector to the World Bank and this time it may be successful.

The reforms in the labour sector is an emotive subject. There is a broad agreement among economists now that an effective exit policy is a must for the success of reforms, although a safety net should be devised to minimise hardship to workers.

The IMF is understood to have raised the issue of exit policy recently when its team had come to India in December 1992 for holding preliminary discussion for nearly $7 billion EFF/ESAF loan. Though it had welcomed amendment in the Sick Industrial Companies Act giving the BIFR powers to handle PSUs as well, it wanted more radical steps towards a more effective exit policy. And gradually but consistently India is moving towards an effective exit policy by convincing the organised labour's trade union leaders. Sheer weight of statistics is loaded against them -- Working population is roughly 325 million out of which 18 million are in organised sector. As restructuring takes place at the most 10% of the labour employed in the organised sector may be displaced and that too, mainly in coals and mines, steel and bureaucracy. This is a probable reason why the back of trade union resistance has softened as was indicated by the pre-budget meeting of the Finance Minister with the union representatives this year.

The labour Ministry is involved in the framing of the new Industrial Relations Bill which is likely to be piloted in the coming budget session along with the Trade Union Act. The bill shall rationalise Industrial Disputes Act and the Trade Unions Act. Changes in the labour laws are one of the main features of the government's economic reforms. The main feature of the amendment of the IR Bill (Industrial Dispute Act) is that industrial units employing less than 300 workers can close down the unit without seeking prior government approval. The main feature of the amendment of the Trade Union Act is that a Trade Union would not be allowed to resort to strike if less than fifty one percent of the workers support the move. Therefore, the IR bill along with the amended Trade Union Act will form a virtual exit policy. The Minister of State for labour Mr. P.S. Sangama has recently confirmed in a Confederation of Indian Industry seminar that the 'exit policy' is awaiting the Cabinet approval. The policy would not give employers' right to hire & fire workers, but shall provide adequate legal power to deal with undisciplined workers.

India has already received $500 million loan from the World Bank, a part of which would finance unemployment benefits for retrenched workers in the public sector through the NRF. Half of the disbursement India received in December 1992 and the other half would come in autumn 1993, provided certain activities and action for the second tranche are fulfilled. Needless to say that the IR Bill and the amended Trade Union Act would go a long way to satisfy many of the conditions set for the second tranche.

In case of agricultural sector reforms the question is if industrial sector wants a market-friendly economy, why not provide one for agriculture. At present, agriculture production is in private hands but government intervention in trade dealing with agricultural produce is comprehensive, which is hampering overall agricultural growth now. Agriculture can act as a drag on the economy and that must be looked at closely despite the fact that this year a bumper crop is expected. The input and output price rationalisation and other trade opportunities have the potential of unlocking substantial

demand for consumer durable and non-durable goods in market towns, as is witnessed in the late eighties. *It is reported that farmers and traders are calling for a long-term export strategy of agricultural products. The government too is receptive to their demand. It is encouraging that the* state agricultural ministers have agreed on a national agricultural policy. *It is reported that if the* Government of India is willing to liberalise trade in agriculture products, both internally and externally, eliminating zonal restrictions at home and export restriction, if it is willing to reduce the level of government intervention in agricultural commodities the Bank will come forward with a $500 million structural/sectoral (SAL/SECAL) adjustment loan for agriculture. In the present disinflationary environment opening up of trade in agricultural produce may provide incentive to emerging 'farmer-trader' class to produce more.

From the above explanation of the government action it can be surmised that the government is serious about the reform process and is working in that direction steadily. However, the situation is quite fluid at the moment and solidification of it will take some time.

4. World Economy

In the last seven consecutive quarters the US economy has shown positive growth. The faltering growth of the earlier quarters has gave way to robust growth rate in the later half of 1992. Japanese and German economies are in deep recession. Japan is considering a second fiscal package, in late spring, to bring forward public works expenditure and to make cuts in taxes to boost investment and consumer spending. Pressure is mounting to have mid-term elections, but it is unlikely that LDP will be unseated from power in Japan. Germany too has eased its monetary policy to fight off recession.

Japanese growth rate in fiscal year 1992-93 is expected to be 1.5% and for 1993-94 the outlook is even more depressing which confirms that the Japanese juggernaut is slowing down. Japan is facing one of the most comprehensive, complex and severe economic crisis since the end of the Second War due to fall in consumer spending. There is a silver lining in the clouds. With the economy close to the core of such crisis, anything can happen. Whether the response is another bout of feverish creativity or a lapse into complacency is anybody's guess. But, it is worth reminding ourselves that the creativity of the Japanese economy has been largely the product of crisis - from the occupation after the Second World War to the oil stocks of the 1970s and the high yen recession of the mid-1980s. In fact, in the mid 1980s Japanese industry had prepared itself to be competitive at 100¥/$. On the other hand, as the US economy is looking up, the chances are that the Japanese economy suffering from demand recession shall get a demand boost through exports.

Jobless rate in Japan fell to 2.3% from 2.4% in December 1992. The fall largely reflects a strong growth in employment in the construction sector which is enjoying a surge in orders from public works programmes. It is likely, however, that unemployment will grow over the next few months as manufacturers attack their costs by laying off workers.

European community is expecting a growth by 1% to 1.5% this year, a little higher than what it was last year of 0.8%. This seems to be bit optimistic. Hence, there is a lingering doubt that the community may slide into recession along with the German economy. The Europeans lay most of the blame on the sluggish German economy. Germany is expected to be in recession this year with

France and Spain reaching a meagre 0.5% growth and a polite hope for the UK growing at 0.5% from -0.5% growth last year.

British economy is looking up -- retail sales are on an upward trend and output and economy seems to be stabilising. Economic data coming in this quarter suggests that recovery is on the way. Some forecasters are expecting the UK economy to grow by 3% in 1994 despite some tightening of the policy.

The US GDP grew by a handsome 3.9% in the July to September period last year. Inflationary pressures in the US economy remained subdued and the Fed managed to keep interest rates around 3%. The low interest rates have helped both business and consumers to ease their debt burden. Consumer Confidence index soared nearly 11 points to 65.5 in November 1992 reinforcing the growing perception that consumers are beginning to feel appreciably more positive about the future prospects. This was just before X-Mas which provided the retail sector good news that it had been waiting for for some time. New home sales in the last quarter provided further evidence of an accelerating economic recovery in the US.

A battery of figures in early March has confirmed a steady expansion of the US economy but probably at a slower pace than the 4.1% annual rate of growth registered in the second half of last year. The purchasing managers' index -- a closely watched barometer of conditions in the manufacturing industry -- fell to 55.8% last month from 58.0% in January. The dip mainly reflected a slower rate of growth of new orders, which had soared to a nine-year high in January. However, the index remained well above the 50% level which is the threshold for growth of the manufacturing sector.

Industry, too, is confident of increasing its investment on equipment especially those which would enhance their productivity. The recent Commerce Department Survey of investment intention suggests this trend to continue, with business intending to increase spending on plant and equipment in 1993 by 7.6% in real terms. The investment tax credit, as outlined in the budget plan, will further boost spending. However, as real earnings continue to fall and employment gains remain modest, only a subdued rate of growth is likely in 1993.

The IMF is not optimistic on global recovery in 1993. It is forecasting a growth rate of 2.3% up from 0.8% for the US economy and for industrialised countries a growth rate of 2% only from 1.4% last year. However, the international trade is expected to grow at the rate of 5-6% this year from 4% of growth last year.

In regard to erstwhile USSR and East Europe, the interim assessment of the IMF is very bleak. In Russia economic contraction was over 9% in 1991 and this rate is estimated to have slide down to -18.6% in 1992. The current year also promises to be one of absolute decline in economic growth. In Eastern Europe, after the poor economic performance in 1991 and 1992 growth is likely to limp back to a modest but positive 2.1% in 1993 according to the IMF forecast.

5. Forecast

The present forecast takes into account the changes wrought in the Indian economy in the last quarter, namely, the new tax structure and the exchange rate regime brought about by the union budget 1993-94. The growth prospect for 1993-94 is only 4.5% and inflation rate (WPI) about 7%.

6. Exogenous variables

6.1 World Interest Rates

Japanese banks have cut lending rates to the lowest since 1989. The recent reduction in discount rate to 2.5% was a belated response by the Bank of Japan to prevent gloomy business sentiment from deteriorating even further. The German Bundesbank has come in the ring and is cutting interest rate quite severely. The US prime rates are one of the lowest in the recent memory and so is the case of the UK interest rates. Even though, there are firmer signs of recovery and lack of any inflationary pressures, there are no signs of further monetary easing in the US this year. These changes are reflected in our exogenous variables assumptions. A little bit hardening in the US rates may take place if inflation monster raises its ugly head in the near future.

6.2 World Trade

What worries most the 1,200 of the world's top industrialists, financiers and politicians attending World Economic Forum in Devos is the risk that America's new administration will be protectionist and that the emergence of regional trading blocks might heighten trade conflicts. These fears are emitting from the actions of the new administration like large anti-dumping duties on European steel and restrictions on the purchase of foreign equipment in public procurement decision. The fear that the US will close its borders to foreign trade is not well placed as Mr. Summer, currently Adviser to President Clinton, is a strong supporter of free trade. It is highly unlikely that America shall try to put clock back by ninety years. On the other hand a strict *quidpro quo* trade policy is expected to be followed in medium term by the Clinton administration. The US is expected to take stiff negotiating stance on GATT, which may conclude by December 1993, in the field of agricultural produce and trade in services.

Table 2: Exogenous Variables

	1991	1992	1993	1994	1995	1996
World						
Trade growth (%)	1.5	1.3	2.8	5.6	5.5	5.5
Real Short-term Interest Rate	3.1	2.0	2.0	2.8	3.0	3.2
Real Long-term Interest Rate	5.4	4.2	3.8	3.5	3.5	3.5
O.E.C.D. Inflation	4.3	3.0	2.8	2.9	2.9	3.0
Crude Oil($/barrel)	18.3	18.4	18.5	18.5	18.5	18.5
Domestic						
	91-92	92-93	93-94	94-95	95-96	96-97
Rainfall (% of normal rainfall)	92	92	90	90	90	90

Table 3: Forecast

	91-92	92-93	93-94	94-95	95-96	96-97
GDP growth (%)	1.2	3.1	4.5	6.0	6.1	6.5
WPI (%)	12.8	9.5	7.0	6.2	5.9	5.7
CPI (%)	13.9	12.5	8.1	7.0	6.5	6.1
Exports (%GDP)	7.2	8.2	8.6	8.9	9.1	9.5
Imports (%GDP)	7.8	10.0	10.2	10.3	10.2	10.0
Current a/c (%GDP)	-1.0	-2.5	-2.1	-1.8	-1.4	-1.2
Current a/c ($ bill)	-2.9	-6.9	-5.9	-4.9	-3.8	-3.2
Exchange Rate (Rs/$)	24.5	30.5	31.8	33.6	34.6	35.6
Production (growth p.a.):						
Agriculture	-2.8	3.6	2.1	2.2	2.2	2.0
Non-agriculture	2.8	3.0	5.8	8.0	8.2	8.5
Investment (% gdp):						
Private Sector	13.4	13.2	14.9	15.5	15.2	15.6
Public Sector	10.9	9.5	8.7	8.1	8.1	8.0
Govt. expdt. (%gdp) (Central + State + UTs)	30.3	30.2	29.7	29.5	29.0	28.4
Fiscal deficit (%gdp)	6.3	5.3	4.7	4.0	4.0	4.0

In France, it seems that the Centre-right will win the election with a large majority. Its leaders are publicly committed to the maintenance of current economic policy, but they may be more prepared to listen to business which is pro-devaluation in order to get the lower interest rate. Hence, the French franc could become increasingly vulnerable after the March election. How the European Community policy would change after the French election is anybody's guess. However, one thing is sure that the fortress Europe policy with one currency will not be on the agenda.

6.3 Oil Prices

One of the assumptions in the present budget is that crude oil prices are not going to rise sharply. It seems that this assumption will hold true not only in short term but in medium term too. At present, global demand for crude oil due to recession in industrialised countries is quite low. OPEC members have to cut their production target again and again to support oil prices. Iraqi oil has been shut in by a UN embargo since it invaded Kuwait in 1990. Resumption of Iraqi exports may create a messy situation for OPEC. A gradual easing of the embargo cannot be ruled out. Crude oil export from the country might add a substantial 1.5 to 2.0 million barrels per day (mbpd) to world supply. It has been reported that the amount of oil that the market will require will be even less if inventories are drawn down. Therefore, crude oil prices are unlikely to increase.

Actual production remained consistently above the ceiling last year. In September 1992, OPEC crude oil output rose to 24.75 mbpd from 24.57 mbpd in the previous month. In October 1992 output was still higher at 25.2 mbpd as compared to 23.9 mbpd in the corresponding month of 1991.

In the Vienna meeting the OPEC producers have agreed to hold output at a level 23.6 million barrels per day after four days of tough negotiations. For the first time Kuwait has agreed to restrict its

output within its quota. Saudi Arabia favours a one mbpd reduction in OPEC oil production which will help to support oil prices, at least partially offsetting a fundamentally bearish outlook.

The price situation is worrying the OPEC members can be gauged by the fact that in April 1993 the members will meet independent oil producers in Oman to stabilise oil prices. OPEC seeks close links with CIS to monitor supplies of crude oil in the world market.

Oil import bill for 1992-93 earlier forecast to be at $5.5 billion, will be around $6.5 billion. The government saves if the present price is below $18 per barrel. According to government estimate, crude import is expected to be 29.5 million tonnes in 1992-93 from previous 26.66 million tonnes because indigenous production has fallen by 2 million tonnes as a result of declining output from the off-shore Bombay high wells. In 1993-94, crude oil import is expected to be about 29 million tonnes and increase in indigenous crude oil production is expected. General fear of increase in hike in prices of petro-products, in our opinion, is not well founded. Only in exceptional circumstances like rupee depreciating by more than 10% and stabilising at that level, it may become necessary to raise prices of petro-products.

Indigenous crude oil output is expected to double in three years time. At present, only half of the consumption is produced domestically. India produces 30 million metric tonnes of crude oil which is likely to go up to 60 million metric tonnes in three years' time. We have not taken this into account as extracting oil from the proven reserves is a risky business.

For India the weak trend in crude oil price is quite a welcome. The IMF Petroleum crude prices are forecast at $18 a barrel in the current year and inflation in industrialised countries is expected to be 3.1% this year.

In our forecast we have assumed an average rate of crude oil to be $18.5 per barrel as some hardening of oil prices is expected as Anglo-Saxon economies are emerging out of recession and their stocks of oil have been run down in the last one year.

6.4 Domestic Rainfall

A little precipitation during winter months has been beneficial to the Rabi crop and as the moisture content of the earth is normal, it will be helpful for the Kharif crop as well. Early sign are signalling to an average monsoon this year. In our forecast we have assumed only 90% of the average rainfall for this year as well as in the medium term. Some commentators are pessimistic about monsoon precipitation this year as it would be sixth year in a row that monsoon rainfall may be average. But, this they have been saying for the last three years. One has to realise that Indian agriculture production is slowly becoming drought resistant as a result of new varieties of seeds and developments in irrigation system at micro level.

7. Output

Is the economy bolting ahead? If one is to believe the Central Statistical Office (CSO) forecast for 1992-93 the answer must be yes. Exports have grown by 2.9% in April 1992-January 1993 over the corresponding period in dollar terms and major industries are in recession. Economy, in general, is

facing demand recession. Even then 'advanced estimates' of CSO of growth rate of 4.2% for the economy in our opinion is too optimistic. Our estimate for 1992-93 is 3.1%, same as the last forecast. However, 1991-92 growth has been aligned with the CSO data, according to which economy grew only by 1.2%.

For the fiscal year 1993-94, we are talking about a hike in growth rate by 1.4 percentage points if this year's growth rate is 3.1%. By increasing allocations for the infrastructure sectors the budget has attempted to stimulate the supply side in the medium term. By cutting excise and import duties it has endeavoured to stimulate the demand in the current year. The Finance Minister could achieve investment injection along with demand stimulation by a mixture of luck and good management. Not forgetting that a favourable agricultural output growth has kept the economy ticking in 1992-93.

7.1 Agricultural Output

The country is set to harvest 177 million tonnes of foodgrains in 1992-93 against only 167 million tonnes in 1991-92. Similarly the oilseeds production is expected to take a quantum jump from 19.5 million tonne in 1991-92 to 22 million tonnes in 1992-93. The farmers are, dissimilar to the last year, unlikely to withhold the stock *en masse* as it will be a loosing proposition. Similarly the traders who financed the withholding of the stock last year may not do so in the changed circumstances. The government continues to have the Essential Commodity Act in its armory to discipline the traders. But how long it would like to hold it is a moot question. The storage control and the restrictions in inter-state movements have wrought havoc in some states. Rajkot marketing yard had to ban entry of the new arrivals of wheat, chilli and cotton from Saurashtra for some time, in the beginning of March, due to lack of space and trade restrictions. Soon we may see these restrictions too melting away. The increase in levy sugar price suggests that complete decontrol of sugar industry is in store this year. Thereafter, the government will rely on open market operation to keep prices stable.

The revised procurement price for wheat is fair and provides good returns to farmers. They may, therefore, not hesitate in parting with their produce. The procurement agencies are unlikely to experience any difficulty in procuring required quantity. Therefore, the procurement of wheat during the marketing year 1993-94 is likely to be very high. Certain amount of wheat will be withheld by farmer-trader type operators. That is good for the economy as it would maintain a downward pressure on open-market wheat prices in the lean period of October, November and December when they like to sell their produce. The prices of rapseed mustard, safflower, as also those of gram and barley are expected to be more stable.

The increase in phosphatic fertiliser price, on average, is only Rs.12/Kg. but since the government wants farmers to pay the full price for their inputs they must be allowed to get the full prices for their produce. By rough estimate, the consumption of phosphatic fertilisers has reduced by 25%-30% during rabi crop, but this is due to government's delay in announcing procurement prices for the wheat. As farmers were uncertain about procurement prices, they tried to save on costly inputs. Urea consumption is expected to be at 15.2 million tonnes in 1992-93 against 14 million tonnes in the previous year. This mis-match in usage is a result of the farmer trying to substitute muriate of potash and di-ammonium fertilisers with nutrients like Calcium Ammonium Nitrate. If the trend continues in the long run, foodgrain output is likely to be adversely affected.

Food subsidy (RE) was Rs.2,800 crore and this year it may be Rs.3,000 crore. Subsidy going to be provided on the import of two million tonnes Nitrogenous fertiliser (Urea) in 1993-94 is Rs.2,000 crore. Improving growth rates in Punjab and Haryana are good but the efforts should also be made to step up the productivity in MP, Rajasthan and Bihar which account for 25% of total food-grain production. The increase in food-grain procurement prices offers good scope for a substantial increase in productivity in these regions.

Our model predicts a growth rate in the agricultural production in line with long-term growth rate for agricultural production for this year and in medium term too. If substantial structural changes in the agricultural sector, as noted earlier, are brought about we may see trend growth in agricultural production increasing to about 3% a year from the present rate of about 2.2% now.

7.2 Non-Agricultural Output

The recession in the industrial sector, especially in the manufacturing sector, as a consequence of demand recession was further compounded by adverse global developments. The upturn in the manufacturing sector in 1993-94 is approaching but the real substantive growth is not round the corner. It is probably, at least, a year away in fiscal year 1994-95, the reason being that for the moment, industry is down in the grip of recession, and it is readjusting to new business environment.

Breath has gone out of domestic businesses as it reads through the second volume of the Raja Chelliah Committee's report on tax reforms. Diehard trade liberalisers are now cautioning the government from going too fast with customs duty reduction. How can you kill domestic enterprise, they ask! All of a sudden the virtue of anti-dumping laws are being discovered and the threatened species are running for cover. The reduction in import duty from 110% to 80% on average meant that blanket protection through import ban is over. On the other hand the government is removing non-tax barriers as well, so that small domestic producers can get on with production. In a significant move to end the 'Inspector Raj' the government has banned visit of inspectors of the Employees State Insurance Corporation to visit a unit employing less than 50 workers.

Though the budget is considered industry friendly, the benefits are expected to accrue only after a few months. The budget is expected to revive the industrial growth in 1993-94. The major beneficiaries of the budget are the electronics industry, the automobile industry, refrigeration & air-conditioning and the textile industry. The Bombay Sensex index is sliding downwards because of overbought position and corporate results to be announced next month are expected to be poor due to disruptions in the economy in December and January. Absence of corporate tax relief and investment allowance has fanned bearish sentiments in bourses.

8. Interest Rates and Credit

The monetary policy, so far, was used to finance the fiscal deficit and administered interest rates to minimise the cost to the government. As the swelling fiscal deficit was financed by printing money, inflationary pressure forced the government to raise interest rate to the productive sector. The rolling back of fiscal deficit in the last medium term and bond financing of the government deficit is freeing the monetary policy from the clutches of government profligacy. This is the intrinsic cause in the

medium term for disinflationary stance in the economy and monetary policy will be used, as elsewhere in the world, to maintain price stability in future.

In 1991-92 government was pre-empting 61.5% of incremental deposits which reduced to 45% in the first half and 25% in the second half of 1992-93. It has been stated in the budget that statutory liquidity ratio (SLR) is going to be brought down to 25% level of total deposits in three years' time and cash reserve ratio (CRR) will be reduced to 10% level in four years' time. Actual modalities are going to be announced by the RBI. This shall increase the supply of loanable funds with the banking sector. One percentage point cut in SLR releases roughly Rs.600 crore of funds. On the other hand public sector demand for funds is going to increase. In the disinflationary setting, at present, there are good chances of a further reduction in lending rates. This year we should see a further reduction in interest rates by 2 to 3 percentage points. The reduction in interest rates shall go a long way in laying strong foundation for a competitive economy through increased investment.

The reduction in SLR and CRR is interlinked with the growth in demand & time liabilities (DTL) of the banking industry. A reduction in reserve requirements has to be in line with the growth in DTL. A deeper cut in SLR would leave a surplus of government securities with banks and the market value of these securities could slump. Not only this, a cushion has to be kept for absorbing a part of Rs 700 crore worth of new securities, other than roll over of the past stock, government is going to issue in the fiscal year 1993-94. The budget support of Rs 5700 crore this year to banking industry would also form a part of SLR requirements. Hence, not more than a couple of percentage points reduction in SLR is expected in the forthcoming credit policy in April. Anyway, the banking sector would be flushed with loanable funds as budgetary support given to the banking sector, to reconstruct their assets, in the form of government securities, would form part of their SLR requirements. Of course, the demand for funds would also be there, especially from the public sector enterprises who are expected to raise funds for their planned investment through internal & extra-budgetary resources.

The Idea of BIBOR, mothballed by RBI last year may revive this year as RBI is talking about a Reference Rate and when it evolves, these rates as also the deposit rates, will adjust to that.

The credit situation is extremely tight as can be seen from M1 growth rate which is likely to be 5.5% and M3 growth rate is likely to be about 15% for 1992-93. Besides this, one of the reasons for recession was that the traders were starved of working capital. Therefore, despite good monsoon there was demand recession in the last quarter of the fiscal year 1992-93. The whole situation is interlinked with the non-payment of the bills by the government in order to meet the IMF quarterly targets. We expect that this informal rationing shall ameliorate in the coming year starting with the payments of bills by the government.

9. Inflation

The effects of asset price deflation are still being felt whether the assets are financial assets with town people or food-grain stocks with farmers in market-towns. Coupled with the fiscal austerity of the government last year, the liquidity in the system has dried up. The situation in 1993-94 is unlikely to be as tight as it was in 1992-93. Only cost push factors like administered prices of petroleum products, support/issue prices of agricultural products, wages in the private & public

sector may push the price level upwards. However, many of these must be seen as structural adjustment. Nevertheless, disinflationary environment is likely to continue at least this year due to external settings and good domestic agricultural output.

The government no doubt anticipated the opposition party reaction. That is why it has decoupled the unpopular price hikes from the presentation of the budget itself. The hike in prices of coal and railway fares will no doubt push the price level up. But not increasing prices in the face of rising costs would only have meant a larger budget deficit. The government has correctly chosen to bring hidden or suppressed inflation out in the open so that it may be controlled more easily. The objective of price hikes has not been to reduce subsidies only but several of the reforms that have accompanied the price hikes, suggest that the government is going for a far-reaching decontrol of prices and a withdrawal from the market. Coal prices have been hiked by 12% before the budget. According to present reckoning the present increases in coal prices and railway fares have increased the annual inflation rate by 0.7 percentage point.

The decision to decanalise the import of kerosene, liquefied petroleum gas (LPG) and low sulphur high stock (LSHS) fuel for sale to the private sector, will relieve Indian Oil of having to buy upto 8.5 million tonnes of kerosene, a million tonne of LPG and anything upto six million tonnes of fuel oil. These goods will be imported and sold by private dealers, on the basis of what the market will bear. Considering that indentor is paying upto Rs.100/cylinder of LPG, there are obviously handsome pickings to be made here. The duel market in LPG is going to increase the supply of the gas in the economy and also lessen the burden of subsidy on the government budget.

The point-to-point inflation rate which is hovering around 7% may harden a little in short-term but a substantial increase in the supplies arising from a buffer production of foodgrains and oilseeds will maintain downward pressure on prices. Coupled with adequate growth rate in agricultural sector and competition in the manufacturing sector the downward pressure on prices is likely to be maintained throughout the coming year. Our model predicts a WPI of 7% for this year and about 6% in the medium term. As a result of increase in foodgrain issue prices and further removal of subsidies from petroleum based products may push CPI around 8% in 1993-94.

10. Exchange Rate

The unified exchange rate has surprised many including the Finance Ministry officials to give strong signals to the structural adjustment side to compensate for the gradualism on the fiscal side.

NRIs have welcomed the rupee convertibility. Additional pressure on the US dollar may prompt non-resident Indians to remit large sums of money to India which shall make rupee to appreciate further. However, unfavourable trade figures of November 92 - February 93 in the next quarter may weaken rupee a little in short term. We expect rupee value in terms of $ to stabilise near about Rs 31.8/$. In the second and third quarter of the fiscal year 1993-94, if the IMF loan is sanctioned, there is unlikely to be any pressure on the rupee. In the medium term rupee is likely to depreciate only as much as the differential between the rate of inflation and productivity in the two economies.

According to the Institute for Financial Management and Research study rupee depreciated to the extent of 70% in nominal terms and 47% in real terms in the eighties. As the productivity of the

economy rises in couple of years, we may not see as much depreciation in the rupee value, thus preparing grounds for full convertibility of the rupee by March 1996.

Critiques of floating exchange rates have argued that now India has convertible currency the rupee will face choppy weather in the midst of a whirlpool of speculation. The incentive given to exporters is illusory as exchange rate will slide down as trade deficit reaches the level of 3% of GDP. As India's main imports are essential to oil the wheels of the economy, the sliding rupee shall contribute further to inflation and trade deficit. India cannot afford to cut down on its essential imports the domestic increase in the prices of petroleum products would give rise to cost-push inflation. Other inflationary pressure may come from the increase in money supply as exports would become competitive if rupee depreciates. Of course, these pressures will remain and a floating exchange rate system is expected to adjust the value of domestic currency in such a way that trade gap narrows. The economy has to get used to short-term strains if rupee value does not adjust quickly or the government tries to lean against the wind. But experience of other economies suggests that a economy with floating exchange rate system tend to weather external shocks better than a economy with fixed exchange rate system.

In the opinion of some critiques without the support of IMF loan this situation is untenable in the long run. Would they continue to support forever? Past experiences suggest otherwise. The appreciation of the rupee in the last few days and the RBI's intervention in the market to keep the value of rupee down has put those people in a tight corner who thought that India cannot afford full convertibility. These scare mongers further give the example of the Bank of England which spent $2 billion overnight to protect pound sterling. They should realise that gyrations in sterling pound is linked with the fact that London is a major financial centre for euro-dollar market.

Normally, a unified exchange rate should have meant an increase of 20% in the rupee price of petroleum products and defence imports. However, the fall in the world price of oil will provide a cushion of perhaps Rs.3,500 crore to the oil pool this year. The renegotiation of the rupee-ruble rate has cut the defence repayments bill by over Rs.1,000 crore, and the fall in global interest rates has cut the debt service bill significantly. External circumstances have thus been favourable to Indian economy.

11. Trade Balance

A major cause for concern in the past 18 months of reform has been the lack-lustre performance of exports. The unified exchange rate offers an excellent change of putting a shine on that performance. During April-October 1992 exports have risen. The manufacturing exports have gone upto $10,093 million during April-October 1992-93 against $9,517 million in April-October 1991-92. Exports have achieved a 5.9% growth from April-November which went down to 3.4% in December. A fall of 9% in dollar terms in the exports of engineering goods in November for the second consecutive month appears to present a gloomy picture for this sector's overall export performance in 1992-93. Current account deficit of approximately $7 billion is a reflection of increased imports and the revival of the economy. As a percentage of GDP, the current account deficit should begin declining from the financial year 1993-94 according to our model.

Government expects exports profitability to increase by 5% to 6% as a result of the unified exchange rate system. Exports growth in dollar terms too is expected to be around 15-16% during 1993-94. To improve export profitability, the budget has provided a further reduction by one percentage point on rupee export credit. The financial companies too are exempted from the levy of interest-tax on export credit provided by them to make sure that exports do not get scuttled due to lack of credit. Other concessions given to export oriented industries like textiles, leather, marine products, gems & jewellery, in terms of reduction in import duty on some capital goods used in these industries, would go a long way in increasing exports from India.

The official import bill is $1.5 billion per annum, largely consisting of defence related goods. The burden of the additional cost, due to convertible rupee, has to be provided in the budget for defence imports. As regards other imports -- petroleum products and fertilisers are likely to go up slightly in line with the rate of inflation. The Government has signed trade and economic cooperation agreements with major republics of the erstwhile Soviet Union, and put in place banking arrangements and a liberal counter-trade mechanism in view of the shortage of hard currency resources in these countries. However, as noted earlier, the slow growth in these economies, the trade with the CIS countries, other than military spares etc., may not improve substantially:

In the current year exports are expected to be $20.5 billion. As a result of the hikes in retail prices of petroleum products last year the Oil Co-ordination Committee Pool is expected to benefit by about Rs.3500 crore in 1993-94 provided the price of imported crude does not rise beyond $18.5 per barrel.

12. Public Finance

Some of the major expectations, which have not materialised are the removal of surcharge on income-tax, reduction in corporate tax, introduction of investment allowance and some relaxation on dividend tax.

The steep import tariff cuts have given unalloyed signal to domestic manufacturers to be not only competitive in the domestic market but also in the global market. The National Renewal Fund (NRF) signals New Delhi's commitment to protect the most vulnerable sections of Indian society against the vagaries of structural adjustment programme. As indicated earlier, it has been a virtual condition from the World Bank and the IMF to fund the reform programme. The bank gave $ 500 million for NRF. In the past, these agencies have spoken out against rise in Military expenditure. But the nearly 10% increase in the defence budget may escape criticism from them because the real increase in military spending may be marginal taking inflation into account. The average growth of customs and excise revenue in the past years has been about 14%. The introduction of unified exchange rate will itself result in enhancement of customs revenue to the extent of 4 to 5%.

The cuts in customs and excise duties have been a pro-reform exercise and appropriate reduction in the fiscal deficit has shown the government's resolve towards fiscal consolidation. Major subsidies on food, fertilisers, and export promotion have been reduced by roughly Rs 2500 crore from the present estimates of Rs 9,480 crore for 1992-93. The promise of introduction of VAT and further cut in corporation tax next year are also good signs.

According to finance ministry the fiscal squeeze of the last two years meant that even if the Finance Minister did nothing at all on the tax side, the fiscal deficit would have fallen to around 3.5% of GDP from 5.3% in 1992-93 and 8.3% in 1990-91. This left room for Dr Singh to cut taxes and yet cut the fiscal deficit to approximately 4.7% of GDP. It is noteworthy that he has not cut the ratio to 4% (as the IMF originally wanted) leaving him with an extra Rs.5,000 crore for Plan spending. This shows that the IMF is, very sensibly, interested in the general direction of reform rather than every decimal point in the targets!!

13. Public Debt

What is disturbing to some of the critics is the fact that debt, both internal and external, continues to be an important source of finance for the Union Government. But this is not the right way of looking at public debt. What one has to understand is the maturity structure and composition of public debt -- both external and internal.

The government's own borrowing (excluding recourse of loan) is expected to grow by nearly 15% (BE/BE) with 182 and 364 days treasury bills, bearing a 11.5% rate of interest, becoming a major source of income (Rs.6000 crore in 1993-94 compared to Rs.5300 crore last year). Interest payment on 182/364 days treasury bills has gone up by 53% in 1993-94 budget from Rs 1170 crore in the revised estimates for 1992-93. One way of reducing this ballooning interest burden is by reducing interest rates as inflation falls. According to finance ministry estimates interest expenditures would start decelerating sharply from 1995-96, pointing towards a tight fiscal-stance lower fiscal deficit in the years to come.

Public sector enterprises (PSES) are expected to borrow an additional Rs.7,676.04 crore in 1993-94 over their total borrowing of Rs.3,956.69 crore in 1992-93 implying a growth rate of 55% (BE/RE). The inability of the PSES including the Railways to loan what they had planned to in 1992-93 suggests that this is a rather optimistic answer. More so when in 1992-93 the revised estimate for the PSU's borrowing (through bonds and debentures, external commercial borrowing and suppliers credit and other sources) fell short of the budget estimate by over Rs.850 crore. The internal and extra-budgetary resources (IEBR) of PSUs are to grow in tandem with the Central Plan, and out of these internal sources are expected to grow by almost 26% (BE/BE). The fact that interest payments have ballooned to 42% of total non-plan expenditure is a reminder of past sins. But this does not appear to have discouraged the Finance Minister from continuing to depend on borrowing, and newer sources at that, in 1993-94.

Dr Singh has failed dismally in one respect. The revenue deficit is going to balloon to Rs.17,630 crore next year, against the budgeted Rs.13,882 crore for 1992-93. Dr Singh can argue that the primary deficit -- that is the budgetary deficit minus interest payment -- has turned into a surplus for the first time in years, suggesting that the interest burden is not allowing revenue deficit to fall.

The short-term external debt ceiling was prescribed by the IMF at $2.5 billion, but the government had run up a short term debt of only about $1.5 billion until end-December 1992. The ceiling on new non-concessional external borrowing with a maturity of one to five years which was $1.6 billion

and with a maturity of one to twelve months, which was $1.9 billion also has not exceeded. In fact the actual level was $1 billion less than the ceiling.

14. Investment

There is a 29% step up in the outlay for public sector enterprises from Rs 36,661 crore in 1992-93 to Rs 47,234 crore in 1993-94. But as noted earlier budgetary support in nominal terms has declined from Rs 6,576 crore in 1992-93 to Rs 6,540 crore in 1993-94. The enterprises are expected to raise as much as 86% of their resources from internal & extra-budgetary sources in 1993-94.

One must not underestimate NRI investment in India as nearly 25 companies in east Germany have already been acquired by Indians and negotiations are under way for taking over at least another 20 companies.

The reduction in import duty should also spur investment, both by Indians and foreigners, after an interregnum in which many investors were waiting for duty cuts before ordering new plants. Through the budget India has taken an important step forward towards globalisation. It does much for exports as a unified exchange rate, abolition of export duties and cuts in import duty mean low costs of production and therefore, improvement in profitability.

We should also see a boom in investment as the availability of credit would improve and cost of credit is likely to decline because of the cut in the lending rate as well as the reduction in the SLR of banks very soon. The fall in the cost of capital goods should reinforce the trend in investment.

Dr Rangarajan while addressing Indian Chambers of Commerce said,

> "If we can show the world that we can maintain law and order, foreign investors will not be deterred. Much worse had happened in China but this did not hamper investments. All I can say at that juncture is that we will keep interest rates under continuous review. It is not our intention to keep real lending rates at very high levels over a long period."

15. Consumption

The major reason why India may become a powerhouse of world economy in the next century is the growing domestic demand. The steady increase in personal income manifests in rising expectations. In the eighties all, who were able sought to acquire the three treasures: refrigerator, scooter and colour television. In the nineties it is likely to be: car, cooler and Karaoke music system. Who knows that at the beginning of the next century it may be: villa, visa and visit. Though our savings of 21% of national income is not negligible, a comparison with the super-performing nations of Asia, which saves 30% of their national income, suggests that India can do better. But question is that should we? No doubt that tax incentive on savings would increase volume of savings. But policies to promote savings and discourage consumption. Such policies reduce today's living standards in order to raise tomorrows. What Indian economy suffers from the past regulatory regime is not blatant consumerism but a high cost economy which is a 'tax' on consumption.

The Finance Minister has reduced excise duties in sectors which are facing demand recession. By reducing excise duties he has reduced cost of production, but by reducing import duties he has given the injection of import competition to domestic producers. For consumers it is a good news, for the first time they have a real choice.

Consumer temptations may grow with the likely reductions in prices of consumer durables. In a rush to pocket a large number of consumers, companies are vying with each other to announce a price cut in their products. It is happening for the first time in long years, and the consumer is being wooed like never before. Private sector consumption grew by 4.5% in real terms in 1992-93 and expected to grow by 5.5%-6% in 1993-94.

16. Summary

Although not spelt out by the Finance Minister as preparing ground for the EFF/ESAF loan from the IMF, it is a path-breaking budget with a strong emphasis on restructuring the economy and the augmenting supply side of the economy. The medium-term funding facility from the IMF/WB with concessional loan would act as an insurance and paper over the ripples generated in the goods market and financial assets market due to restructuring of the economy. To ameliorate short term consequences on labour, the labour market reforms are being handled in a politically deft manner. Bolstered by good economic performance in the next eight months the country *may* be slapped a mid-term poll after the festival season. For the sake of political stability, which shall embolden the government to legislate unpleasant decisions, this is a burden worth carrying.

The economic strategy in the medium term is quite clear; go for growth and supply side incentives (both in direct and indirect taxes) and push for structural reform. Monetary policy of the government is quite tight and as inflation falls rapidly the government should bring down interest rates quickly to maintain the momentum of private sector investment to enhance productive capacity of the economy. This shall help the government as the interest burden would come down rapidly. The success of the reform programmes hinges on sustained growth of agricultural and non-agricultural sectors which is inexorably linked to productive investment in these sectors.

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