Speech of the Finance Minister at the Annual Economic Editors' Conference

November 12, 2007

I have always viewed the Annual Economic Editors' Conference as an important platform for interface between the Government and the Fourth Estate on the salient aspects of the economy, the current economic situation, the challenges and the policy responses of the Government. I understand that the participants of this Conference form a highly diverse cross section of informed economic editors from the length and breadth of the country. I extend a hearty welcome to all the participants and wish that over the next two days there will be meaningful discussions on the current state of the Indian economy and the Government's economic policies. Such discussion will generate useful feedback to the Government.

The United Progressive Alliance (UPA) Government assumed office in May 2004. It is with a high sense of achievement – and pardonable pride -- that we recapitulate the three and half years of the management of the economy. There has been a marked change in the way the Indian economy is viewed both within the country and in other countries of the world. This is largely due to the sustained, well-directed efforts of the Government that have resulted in globally acclaimed rates of economic growth, increased global competitiveness of Indian businesses, strong macro fundamentals, and above all, a highly favourable economic outlook.

Performance of Growth Variables

I am sure that you have carefully followed the developmental strategies followed by the Government, the travails in the growth process, the shift in the Government's approach to the goal of inclusive growth and restatement of its social and economic objectives. The command and control economy of India grew at a rate of 3.5 per cent per annum during 1950-51 to 1979-80. Growth, which hovered around a little above 5.5 per cent per annum during the 1980s and 1990s, increased to 5.8 per cent during 1998-99 to 2003-04 and further to 8.6 per cent since 2004-05. India, of late, has been globally acknowledged as a high growth economy. The rate of growth stood at 9.4 per cent during 2006-07. The growth rate during the first quarter of 2007-08 was an impressive 9.3 per cent over the corresponding quarter of the previous year. If we can sustain this rate of growth, per capita income can double in about 9 years. This high growth has been facilitated by an unprecedented increase in the rate of investment from 22.9 per cent in 2001-02 to an estimated 35.1 per cent in 2006-07.

According to Goldman Sachs, over the next 30-50 years, India is likely to grow fastest among the BRIC economies -- Brazil, Russia, China and India. McKinsey Global Institute has predicted that India will have the world's fifth-largest consumer market by 2025, with about 583 million people forming its middle class. This implies a huge opportunity for further investment and enterprise.

Structural shift and sectoral growth

The rapidly changing sectoral contributions to the GDP are an indication of the significant structural changes taking place in the economy. The share of industry in GDP has increased from 25.6 per cent in 2003-04 to 26.6 per cent in 2006-07, while there has been a decline in the share of agriculture and allied sectors from 21.7 per cent to 18.5 per cent during the same period. The decline in the share of agriculture in GDP has been mostly appropriated by the services sector, which increased its share from 52.7 per cent to 54.9 per cent.

Industry has, of late, been one of the major drivers of the growth of the Indian economy. The last four years have witnessed impressive rates of industrial growth, averaging around 10 per cent. In 2006-07, the industrial growth was a splendid 11.5 per cent, while the rate of growth of manufacturing was even higher at 12.5 percent. Though the growth of manufacturing has slightly decreased to 10.3 per cent during April-August 2007, the growth in capital goods at 21.3 per cent during the period is suggestive of significant addition to industrial capacity. The slackening has been mainly on account of the poor performance of the consumer durables sector.

The growing business optimism is manifest in the robust growth of bank credit to industry and large industrial investments in the pipeline. Outstanding credit to the industrial sector by the Scheduled Commercial Banks witnessed a growth of 30 per cent and 28.4 per cent in 2005-06 and 2006-07 respectively. Year on year growth of outstanding credit as on October 12 at 23.5 per cent has exhibited some moderation from the strong pace of the previous three years. However, we should note that industry is able to access funds from other sources as well. Preliminary assessment indicates that in the first quarter of 2007-08, access to resources by industry other than from bank credit, increased by over 30 per cent compared to the first quarter of 2006-07. Internal generation of funds continued to provide strong support to the funding requirements of the corporate sector. The CMIE data on investment in manufacturing in the pipeline for March 2007 showed a growth of around 50 per cent over March 2006. Besides, net FDI into India has grown from US$ 4.7 billion in 2005-06 to US$ 8.4 billion in 2006-07, an increase of around 79 per cent. FDI flows in the current year upto June 30, 2007 have been estimated at US$ 6.4 billion. Indian manufacturing has come of age and is highly competitive in the global market. The growing interest to invest in Indian industry is best embodied in the BSE Sensex that touched an all time high of 19,977 at closing on 29th October 2007. The business expectations index of the Federation of Indian Chamber of Commerce and Industry (FICCI) for July-December 2007 has also shown an improvement. Nearly 70 per cent of the respondents to the FICCI survey found the current overall economic conditions better than those in the preceding six months.

External Sector

India's external sector continued to be robust and reflected the strength of the economy during 2006-07. Preliminary **Balance of Payment** estimates released by the RBI for the first quarter of the current year (i.e. April – June 2007-08) point to a continuation and, in fact, strengthening of the broad trends observed in 2006-07. The current account shows a deficit of US$ 4.7 billion primarily due to the relatively higher growth of imports vis-à-vis exports. Net invisibles, despite recording a robust level of US$ 16.9 billion, fell short of the trade deficit of US$ 21.6 billion, leading to the current account deficit. The capital account, however, had a surplus of US$ 15.9 billion during the period. Foreign investment (net) inflows were particularly buoyant on account of robust portfolio investment inflows.

The **exchange rate** of the Rupee against the US dollar had displayed reasonable stability during 2005-06 and 2006-07. However, the Rupee showed a mixed trend against other major global currencies like the Euro, Yen and Pound Sterling. During the first half of the current year, the exchange rate of the Rupee against the US dollar has appreciated sharply reflecting mostly the copious capital inflows, the strong fundamentals, higher returns on equity and even higher expectations. This surge in capital flows, apart from causing volatility in the forex market, has led to an accumulation of reserves. The **foreign exchange reserves** increased to US$ 199 billion at end-March 2007 and further bourgeoned to US$ 262 billion on October 26, 2007. In response to the widespread concern about the possible adverse effect of Rupee appreciation on exports, the Government announced three packages for exporters that included enhancement of 3 per cent of the DEPB rates for 9 sectors, reduction in ECGC premium by 10 per cent, release of around Rs. 600 corers to clear all arrears of terminal excise duties and CST reimbursement, enhancement of the rate of duty drawback by around 10 per cent to 40 per cent, reduction in the rate of interest on pre and post shipment credit by 2 per cent and refund of service tax to exporters for use of services not in the nature of 'input services'. The total value of these packages is estimated at Rs.5,200 crore.

In 2006-07, the **net capital inflows** almost doubled from the level of the previous year to touch US$ 46.2 billion. External commercial borrowings (ECBs) alone accounted for about 35 per cent of total capital flows, enabled by ample liquidity and favourable interest rates in the global markets on the one hand and rising financing requirements for capacity expansion domestically on the other.

Prudent policies on **external debt management**, inter alia, the emphasis on raising funds with longer maturities on concessional terms from less expensive sources, monitoring of short-term debt, prepayment of high-cost loans and encouragement to non-debt creating capital flows have helped contain the growth in the accumulation of external debt. The ratio of external debt to GDP came down from 38.7 per cent in 1991-92 to 21.1 per cent in 2001-02 and further to 16.6 per cent in 2006-07 (revised). By end-June 2007, the ratio of foreign exchange reserves to total external debt stood at a comfortable 129 per cent.

Inflation

In our open economy framework, we attach the highest importance to inflation monitoring so that effective corrective action can be taken when required. High inflation in 2006-07 was triggered by shortfalls in the domestic supply of some agricultural commodities and hardening of international prices on the supply side and high growth in money supply and credit on the demand side. Thanks to a rise in per capita income, consumption also increased. Prudent measures adopted by the Government, including monetary measures that impacted the availability and cost of credit, selective reduction in import duties of supply-constrained items, measures for augmenting domestic availability, and other administrative measures have helped the Government to gain command over inflation.

Inflation, measured by variation in the wholesale price index (WPI) on a year-on-year basis, declined from 5.94 per cent at end-March 2007 to 2.97 per cent as on 27th October 2007. Inflation in the primary articles index came down from 10.72 per cent to 5.10 per cent during the same period while that of manufactured products declined from 6.11 percent to 3.88 percent. Headline inflation in major advanced economies, however, has generally edged up towards the end of the second quarter of 2007-08, mainly reflecting hardening of food and fuel prices. Hence, there are still some pressures on inflation measured in terms of the consumer price indices, but we expect these to get moderated.

Infrastructure

Different constituents of infrastructure have shown improvement in the current financial year. In the power sector, power generation and plant load factor are on course to achieve their annual targets. In the transport sector, the total earnings of the railways have shown an increase close to 11 per cent during April-September 2007, while passenger traffic handled at domestic air terminals grew by about 28 per cent during April-August 2007. An ambitious National Highway Development Programme (NHDP), involving a total investment of Rs.220,000 crore upto 2012, has been established. In telecommunications, telephone connections have increased by 65 per cent while cell phone connections have grown by 53 per cent during April-August 2007. India Post launched its first aircraft, with a 15 tonne load capacity, in August 2007.

Needless to say, India must make enormous investments in its social and economic infrastructure in the near future. The Planning Commission has estimated that the total investment in infrastructure in the 11^{th} Five Year Plan must increase from 4.5% to around 8% of the GDP. Under the governing rules of fiscal management in the FRBM regime, budgetary deficits are being strictly monitored, restricting the scope for unlimited fiscal expansion. Hence, the solution to the challenge of infrastructure is partly located in public-private partnerships, which not only bridge the gap in resources but also bring in private sector expertise and efficiency in the operation and maintenance of assets. During a decade of experience with PPPs in India, some sectors like ports and roads have shown greater progress than others. The Government of India has taken several initiatives like viability gap funding, Public Private Partnership Appraisal Committee (PPPAC) and India Infrastructure Finance Company Ltd. (IIFCL) to promote PPPs.

Fiscal scenario

The financial year 2007-08 has so far shown the expected revenue buoyancy. 40.7 per cent of the budgeted revenue receipts have been realized by September 2007, as against 40.0 per cent during April-September 2006-07 and 35 per cent during April-September 2005-06. Revenue receipts and capital receipts, especially non-debt capital receipts, have shown improvement. On the revenue side, the gross tax collection has shown a 25 per cent growth during April-September 2007. Customs duty has increased by 16 per cent, taxes on income by 38.9 per cent, corporation tax by 41 per cent, service tax by 36.3 per cent and union excise duty by 6.5 per cent. Non-tax revenue went up by 19 per cent during the period.

On the expenditure front, 42.3 per cent of the budgeted plan expenditure has been realized by September 2007, as against 39.9 per cent during April-September 2006-07. Notably, a greater increase is seen in the plan capital expenditure (49.4 per cent as against 38.4 per cent) than in the plan revenue expenditure (41.0 per cent as against 40.2 per cent). Ministry-wise performance presents a mixed picture; yet, a majority of them have surpassed the levels achieved by September of the previous year. We have already reached 48.6 per cent of the budgeted non-plan expenditure too, as against only 46.8 per cent by September 2006. Revenue buoyancy coupled with the expenditure trends are reflected in the fiscal deficit, which stands at 53.8 per cent of the budgeted figure by September 2007 as against 58.2 per cent for the corresponding period last year. Indications are that we are well on course to achieving the fiscal consolidation mandated by the FRBM Act.

Social sector

The Central Statistical Organisation has reported that the poverty ratio has fallen from 36% in 1993-94 to 27.5% in 2004-05 (both following data collected employing Uniform Recall Period). Statistically, unemployment rate (usual principal status) seems higher at 3.06% of the labour force in 2004-05 as compared to 2.78% in 1999-2000. However, one should remember that the growth in labour force has been higher. The growth of labour force increased from 1.60 to 2.54 per cent during the period while the growth in the workforce (i.e. people actually employed) has increased from 1.57 per cent to 2.48 per cent. Accelerated growth in the work force is a sign of development and creation of more jobs.

Government has diligently adhered to the mandate of the National Common Minimum Programme. Social sector programmes, in general, have received an increased outlay during 2007-08. The eight flagship programmes have continued to receive high priority. Bharat Nirman, which is an important edifice of Government's policy, received a budgetary outlay of Rs. 24,603 crore in 2007-08 as against Rs. 18,696 crore (including NER component) in 2006-07. Under Bharat Nirman, 60 lakh houses are envisaged to be constructed during a period of four years from 2005-06 to 2008-09. 30.50 lakh houses have been constructed during the first two years of this programme. The National Rural Health Mission was allocated Rs. 9,947 crore in 2007-08 as against 8,207 crore in 2006-07. In order to expand the Integrated Child Development Scheme(ICDS) to cover all habitations and settlements during the 11th Plan and reach out to all children below the age of six as well as expecting and lactating mothers, the allocation to ICDS was increased from Rs. 4,087 crore in 2006-07 to Rs. 4,761 crore in 2007-08.

Launched on February 2, 2006 in the 200 most backward districts in the first phase, the National Rural Employment Guarantee Scheme (NREGS) has been expanded to 330 districts in the second phase. The remaining 266 districts have been notified on 28^{th} September, 2007 where the scheme will come into effect from 1^{st} April, 2008. As against the total budget allocation of Rs. 12,000 crore, an amount of Rs. 7,763.74 crore has been released till 26^{th} October, 2007.

A new scheme called 'Aam Admi Bima Yojana' (AABY) was launched on 2^{nd} October, 2007. Under the scheme, the head of the family of rural landless households in the country will be provided insurance cover against natural and accidental deaths and partial/permanent disability. The Rashtriya Swasthya Bima Yojana was also formally launched in October, 2007, under which all BPL families in the unorganized sector will be provided health cover, in a phased manner over the next 5 years. The scheme has a provision of a smart card to be issued to the beneficiaries to enable cashless transaction for health care upto Rs. 30,000 per family per annum. All pre-existing diseases will be covered under the scheme.

Challenges

Given the numerous challenges that confounded the growth process in India, the history of its development planning has been marked by both success and failure. Yet, in the first three decades of planning, India certainly recorded major achievements in establishing a deep-rooted, pluralistic democratic system of administration and development; in attaining food security, thanks mainly to the Green Revolution; in preparing a diversified industrial base; and in alleviating the incidence of the multiple deprivations that the majority of its population faced. Yet, less than optimal growth rates and persistence of poverty in many parts of the country spurred the Government to make a paradigm shift and launch the economic reforms in 1991. The reform process has been sustained for 16 years through six governments. The country has reaped rich dividends. Now that we have identified a successful growth model, the biggest challenge faced by the economy is one of managing growth in a turbulent world. Managing growth has manifold dimensions, both short-term and long-term.

The short-term challenges on the external front are posed by the need to effectively manage an unprecedented influx of capital inflows and burgeoning foreign exchange reserves and to contain the adverse effects of appreciation of the rupee on Indian exports. These inflows are a test of the absorptive capacity of the economy. Further, domestic prices may also be impacted by international hardening of food grain, commodity and energy prices. The economy must also be insulated to the extent possible from the potentially adverse effects of the economic slowdown occurring in some of its major trading partners. Given the general optimism prevalent in the economy and the strength of the economic fundamentals, I am certain that the nation will be able to overcome these challenges.

In the medium and long term, one of the biggest challenges is to effectively sustain the high pace of growth witnessed in recent years. This requires development of diverse, regionally balanced, physical and social infrastructure. The investment requirements for infrastructure are humungous and we must find ways and means to mobilise these resources and complete the infrastructure projects without cost or time overruns. Further, issues of inter-temporal equity must be kept in mind while utilizing the natural resources for current growth and managing the growth induced stress on environment. India has to play a mature and responsible role in matters relating to environmental conservation and climate change.

Another cause of concern is the slow-growing farm sector that still supports the livelihood of a majority of the population. Issues like stagnant yield rates in many important crops, declining per capita availability of food grains and need for additional public investment call for urgent policy attention. The Eleventh Five Year Plan targets a four per cent growth in agriculture. Action points for the Centre and the States for achieving a four per cent growth rate have been drawn up. I refer to the path-breaking resolution on agriculture adopted by the NDC on May 29, 2007. However, even if all these tasks are completed, average per capita increase in income in the agriculture sector will still be about two thirds of the overall increase. These issues are high on the agenda of the Government and it has taken many initiatives on this count; much more needs to be done.

Rapid economic development is a huge opportunity for fulfilling many national objectives. It is important that we seize the opportunity. There is an urgent need for improving the education and skills of the labour force, especially of those belonging to the lower strata of the society, in a planned and structured manner.

The Government is alive to these challenges and the hard work that is required to achieve our objectives. The Government once again rededicates itself to take appropriate policy, legislative and administrative measures in order to achieve these objectives.

Thank you.