

Budget 2008-09: A Macroeconomic Perspective

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Context

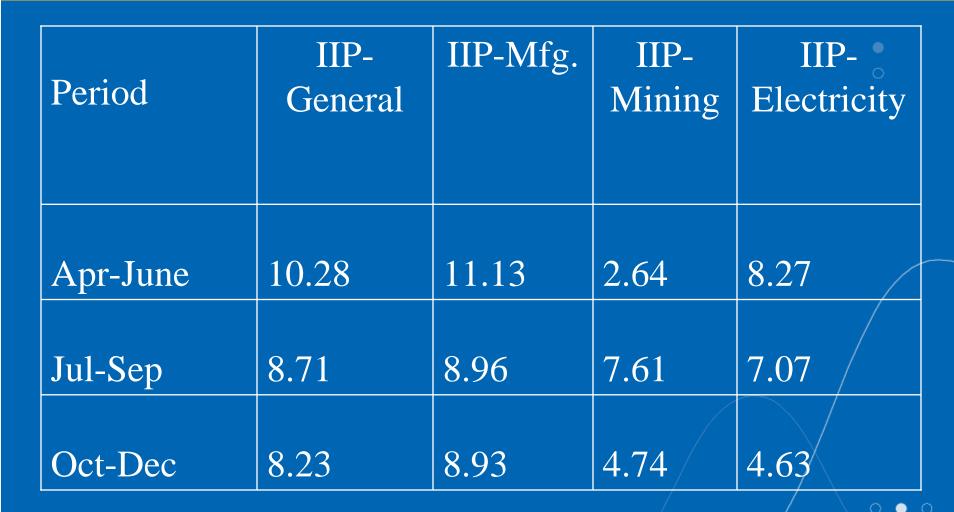
- Remarkable performance by economy over Tenth Plan (Economic Survey; EAC Report)^a
 - Growth acceleration
 - Sharp rise in corporate saving and Investment; improved investment climate
 - Well-behaved balance of payments
 - Significant adjustment in public savings

Growth Expectations 2007-08: Under 9% but still strong

Period	< 8.5	8.5-9.0	>9.0
Upto April 2007	ADB, Indicus NCAER (8.3)	Merrill Lynch	Citigroup
May-September 2007	RBI (around 8.5%), JP Morgan	IMF, ASSOCHAM, ICRA, NCAER (8.5), UNCTAD	
October-December 2007	Crisil	NCAER (8.9%) CEA (9%)	CMIE, Citigroup, FM
January 2008	RBI (Around 8.5%)	CEA (8.9%)	NCAER (9.1%)
Feb 2008		CSO (8.6)	

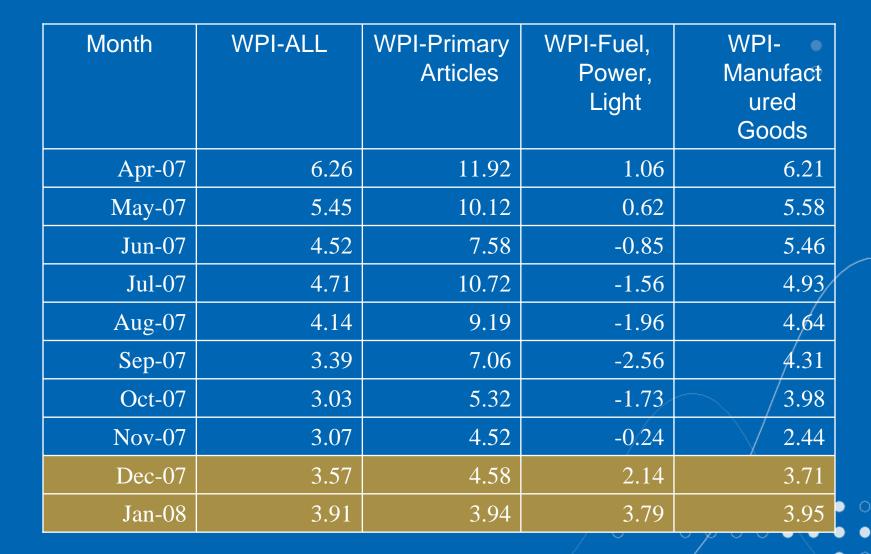
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Deceleration in industrial growth: IIP % YOY 2007



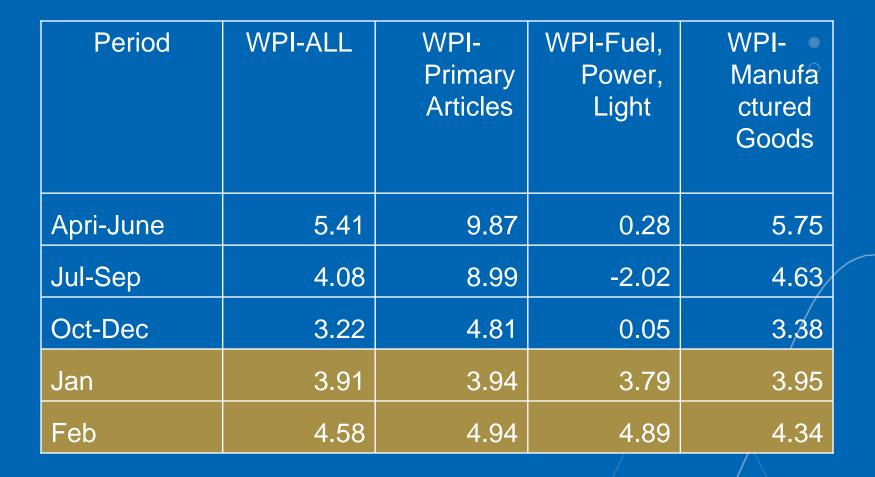
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Inflationary pressures raise head: WPI % YOY



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Primary articles drive inflation: • • • • WPI % YOY



Squeeze on commercial credit: % YOY

Period	M3	Reserve Money	Bank Credit to Comm.
April-June	20.4	23.7	23.8
Jul-Sep	21.2	28.6	21.6
Oct-Dec	22.7	29.2	21.1

Goals of Policy

To sustain high growth through <u>efficient</u> investment

 Requires ability to direct domestic, foreign capital into productive uses.

Role of financial sector critical

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Complications

 No "political consensus" on how to manage "trilemma" (exchange rate, monetary autonomy, capital opening)

 International, domestic rigidities generating supply, demand shocks

High political sensitivity to price changes

Issues and Choices

 Is there a domestic/international cyclical case for stimulus?

If so, should it be fiscal or monetary?

Does the budget facilitate monetary easing?

 What is the appropriate response to supply shocks?

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Political Economy of Policy Mix

 Pure inflation targeting requires both fiscal restraint and a floating exchange rate.

Indian circumstances currently permit neither.

As EAC notes, probably at limit of nominal appreciation of the rupee

Assessment

 See powerful underlying forces demanding a real appreciation.

Inflation likely to be part of adjustment mechanism

Fiscal policy needs to be tighter to permit monetary easing

But inconsistent with political imperatives.



