



# Macroeconomic Overview of India: Recent Trends and Developments

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# Structure



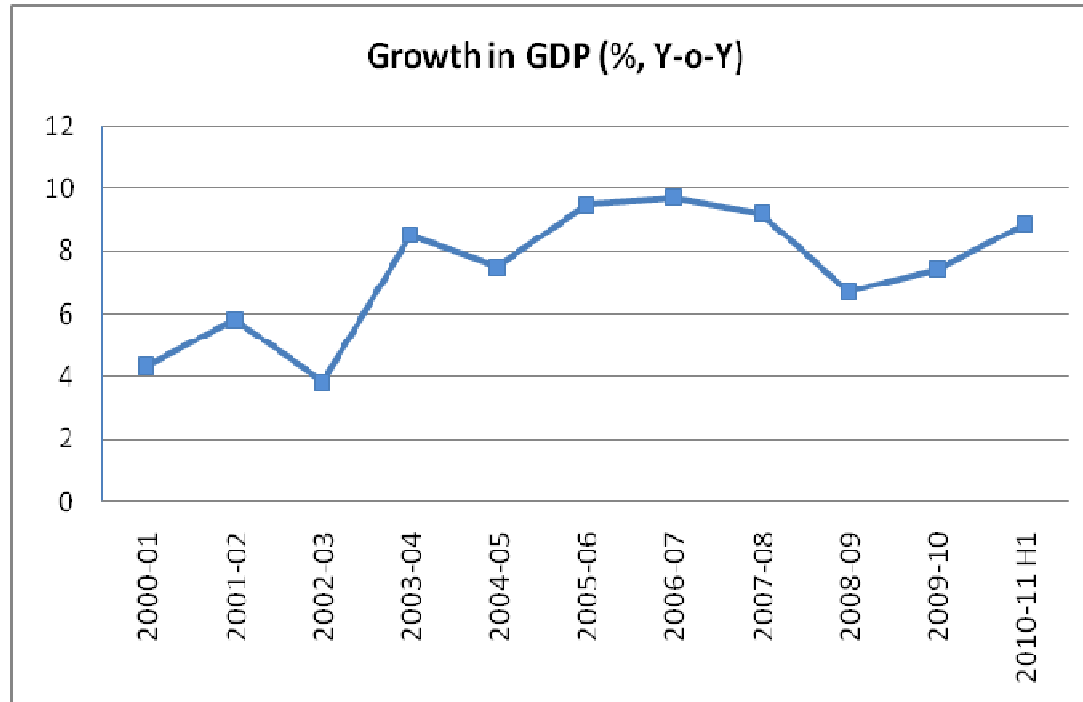
1. An overview
2. India's recovery from global crisis
3. India back to pre-crisis growth trajectory?
4. Twin risks in the economy
  - Inflation
  - Balance of payments
5. The next reform agenda

# Indian economy: An Overview



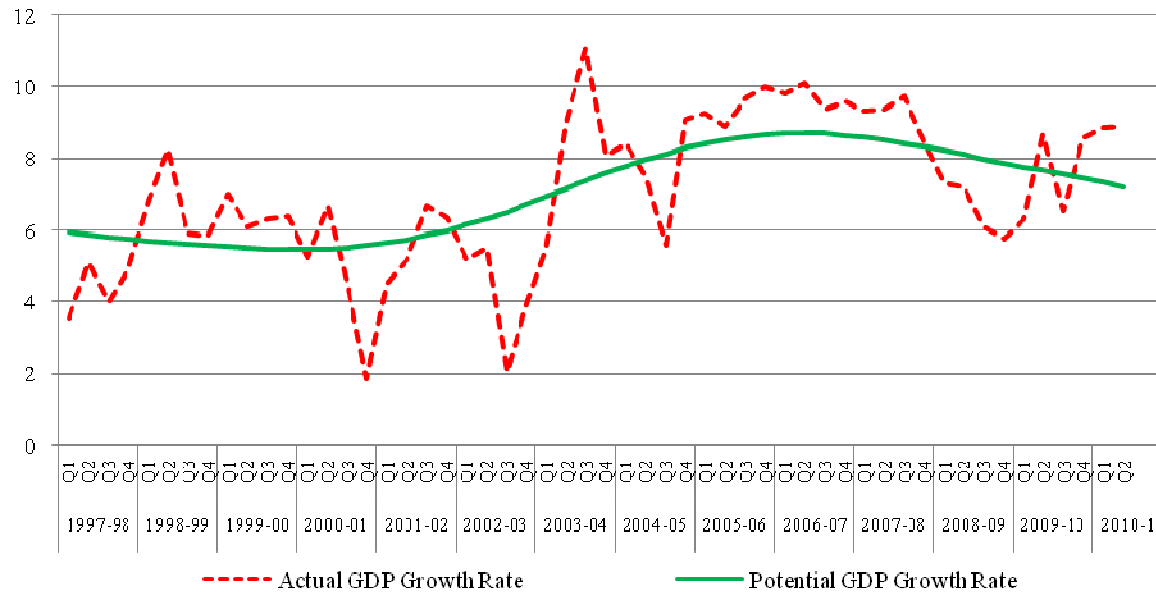
- **12<sup>th</sup>** in terms of GDP at market exchange rates (\$1.3 trillion) and **4<sup>th</sup>** in terms of GDP at purchasing power parity exchange rates (\$3.8 trillion) in 2009
- **2.3%** of global GDP at market exchange rates and **5.2%** of global GDP at purchasing power parity exchange rates
- Relatively a closed economy till 1991 and opened up after the external payments crisis of 1991
- Average growth rate about **4%** before 1991 and moved up to **6.5%** post reforms
- Growth rate rose to nearly **9%** in the pre-crisis 5-years, 2003-08
- Per capita GDP rose **3 times** from \$374 in 1990 to \$1134 in 2009

# Recovery from Global Crisis



- Growth fell to **6.7%** in 2008-09 from **9.2%** in 2007-08
- Smart recovery to **7.4 %** in 2009-10 and **8.9%** in H1 2010-11 (average growth rate, 2003-08 : 8.9%)
- India returning to **9%+ sustained growth trajectory?**

# Potential Growth Rate of Indian Economy



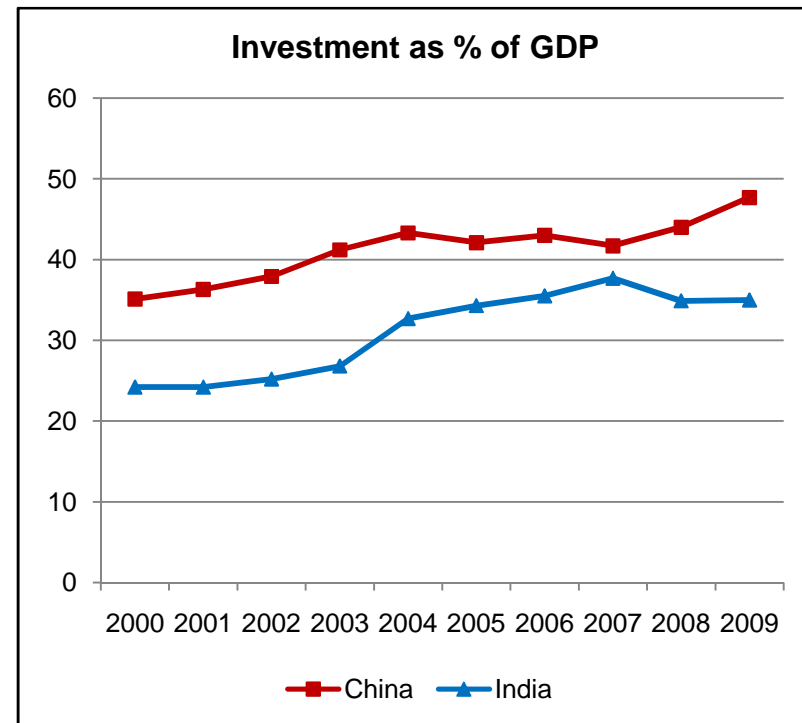
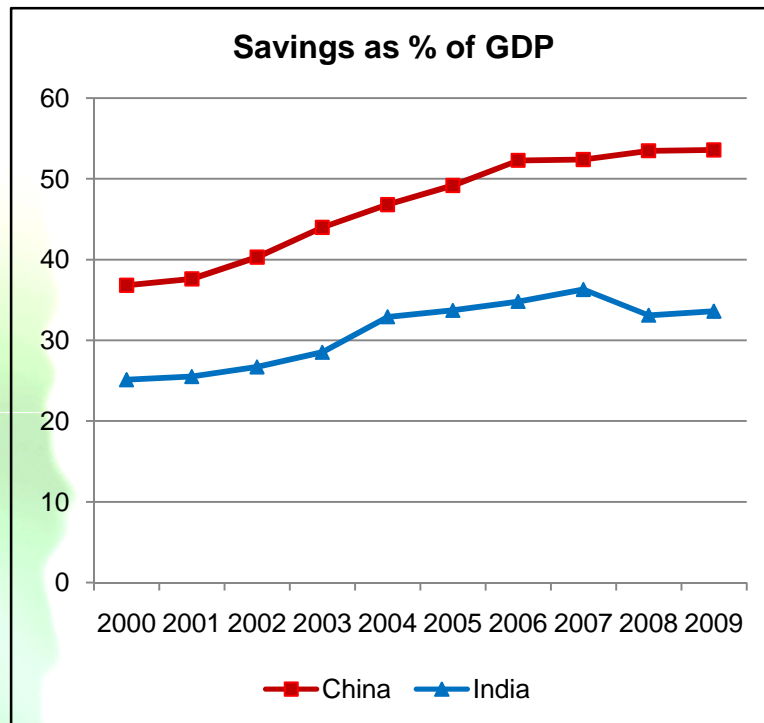
• **Potential growth rate:** the maximum sustainable rate at which an economy can grow without raising the rate of inflation

• India's potential growth rate rose from about **5.5%** in late 1990s to above **8.5%** in mid-2000s

• Growth potential has fallen after crisis to about **7.5%** and below

• Current growth rate above potential and has **triggered inflationary pressures**

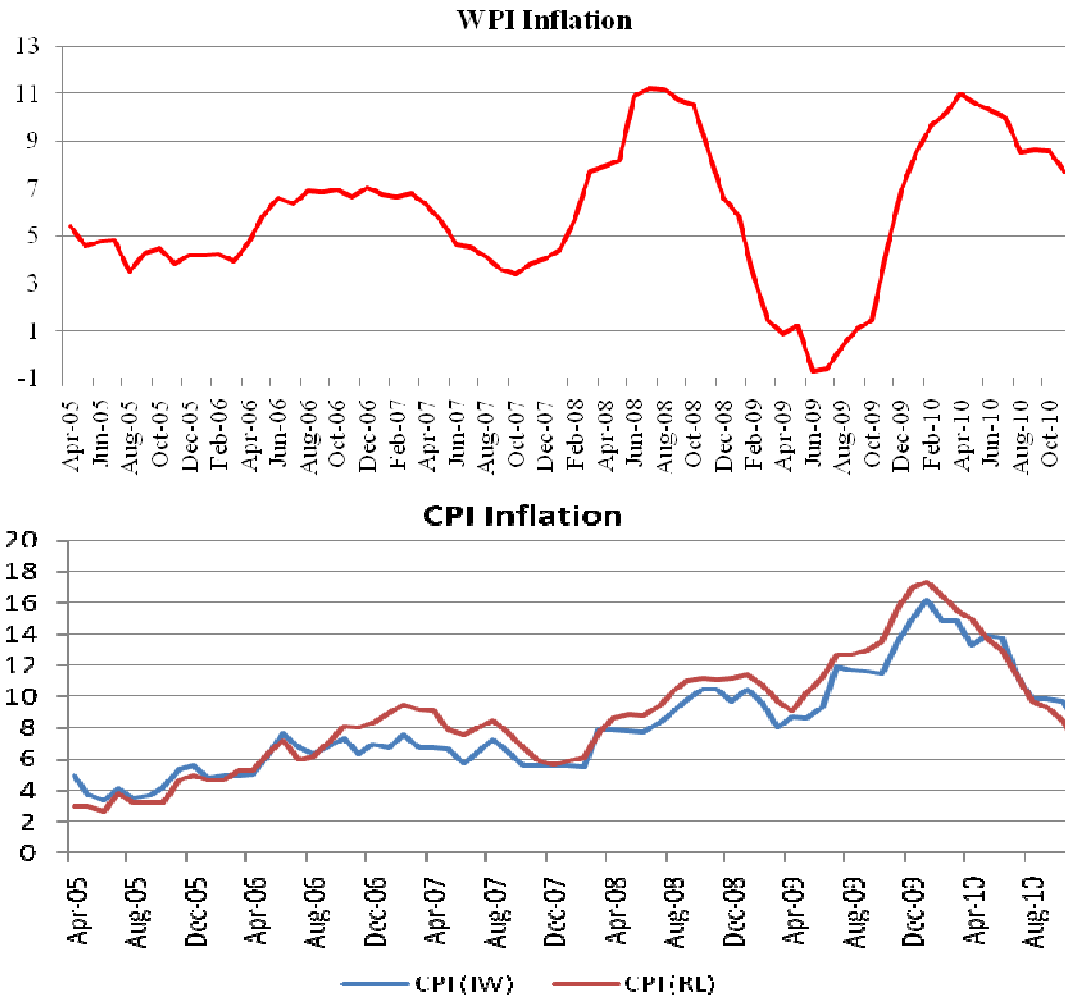
# Post-crisis Saving and Investment: India-China Contrast



Source: WDI Database, World Bank 2010.

- Both savings and investment rates declined in India following the crisis; in China both rose
- In India consumption ratio rose following crisis, both for households and government; China the opposite

# Inflation

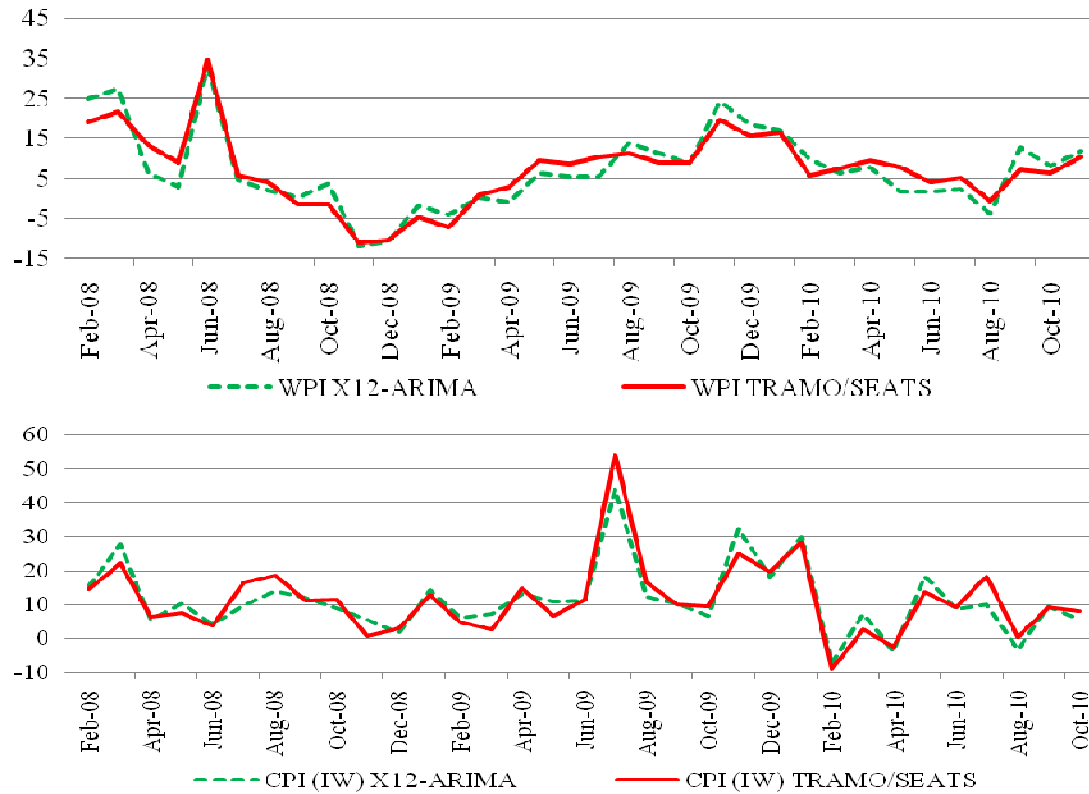


- CPI inflation above 5% right back from April 2006
- Though falling , rate remain at 7.5-8.5%

# Month-on-Month Inflation



Annualised Month-on-Month Seasonally Adjusted Rate of WPI and CPI (IW) Inflation



*Month-on-month inflation indicates persistence of inflationary pressures at annualized 8-10%*



# Inflation and Agriculture

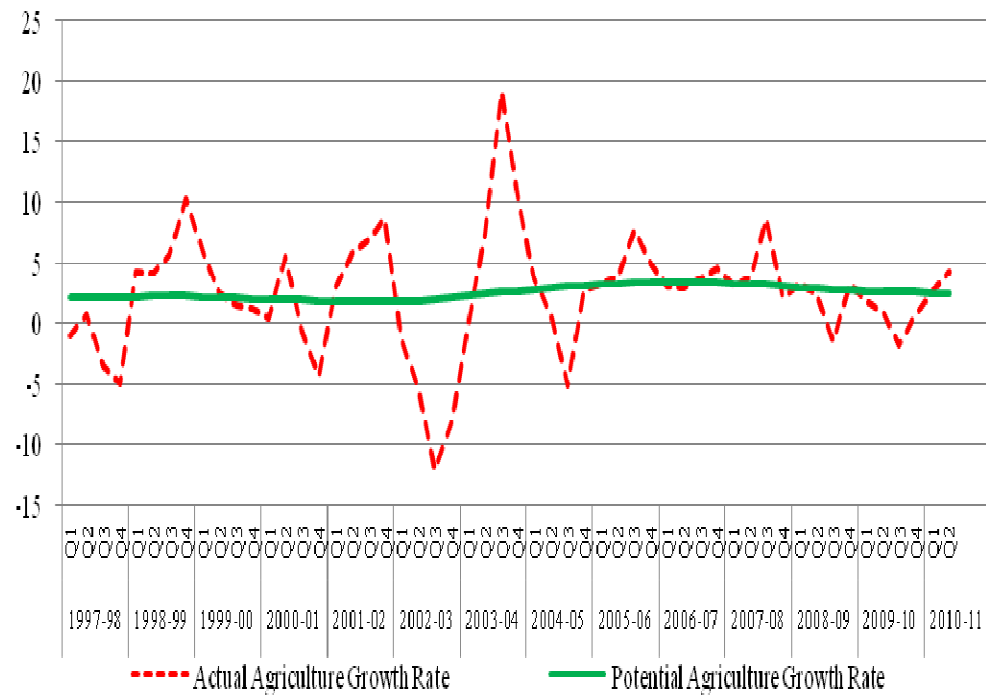


	<b>WPI Inflation</b>	<b>CPI-IW Inflation</b>	<b>WPI Food Inflation</b>
2000-06	5.1	4.0	2.9
<b>2006-10</b>	<b>5.7</b>	<b>8.6</b>	<b>10.2</b>
2006-07	6.5	6.8	9.6
2007-08	4.8	6.2	7.0
2008-09	8.0	9.1	9.1
2009-10	3.6	12.4	15.3
2010-11 (Apr-Nov)	9.4	11.2	16.8

Source: Office of the Economic Adviser, Ministry of Commerce & Industry; Labour Bureau, Ministry of Labour and Employment.

- *Rising inflation from 2006-07*
- *Inflation linked with food inflation and in turn, the state of agricultural output vis-à-vis consumer demand*

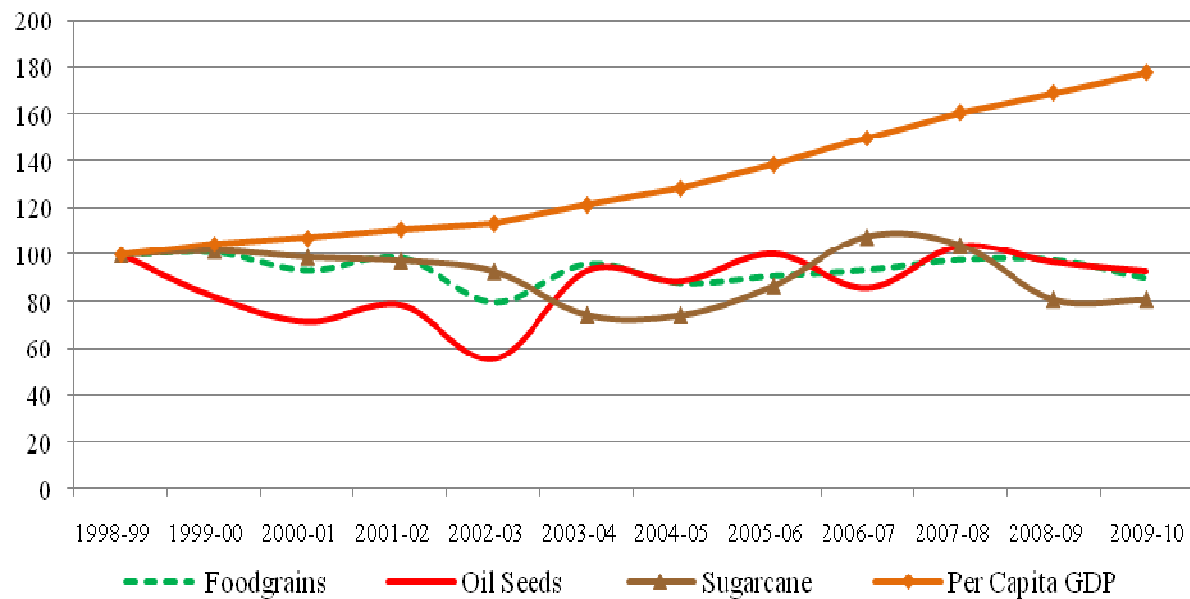
# Declining Agricultural Potential Growth Rate



- *Inflationary surge in 2008-09 and 2008-10 due to agricultural supply shocks, but gradually rising inflation from 2006 due to falling agricultural potential growth rate*
- *Potential growth rate in agriculture declined from **3.5%** in 2006-07 to **2.5%** in 2009-10*



## Index of Per Capita Availability of Major Agricultural Food Products



Source: Computed based on data from Department of Agriculture and Co-operation; CSO.

• Per capita income rising by 5.5% per annum but per capita food availability either stagnant or falling

# Investment in Agriculture

(Average Annual Growth in Per cent)

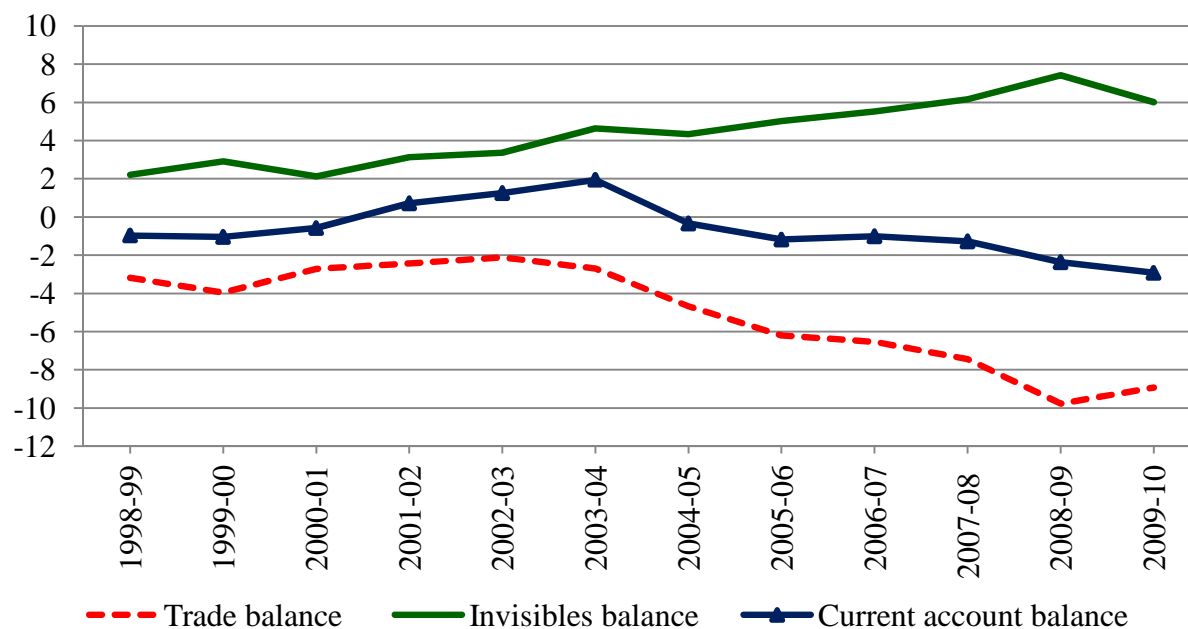


	Total	Agriculture
1970-80	5.0	7.3
<b>1980-90</b>	<b>5.4</b>	<b>-2.6</b>
1990-00	7.9	9.3
<b>2000-05</b>	<b>9.0</b>	<b>3.2</b>
2005-09	11.2	16.1

Source: CSO.

- *Huge underinvestment in agriculture in 1980s and early 2000s*
- *Government support to agriculture through input subsidies (water, electricity, urea fertilizers, etc)*
- *Government investment in irrigation has declined sharply*
- *Agriculture subject to huge restrictions with regard to pricing, movement and sale of products*
- *“Subsidy-control regime” not congenial to a breakthrough in production*

# Rising Current Account Deficits (% of GDP)



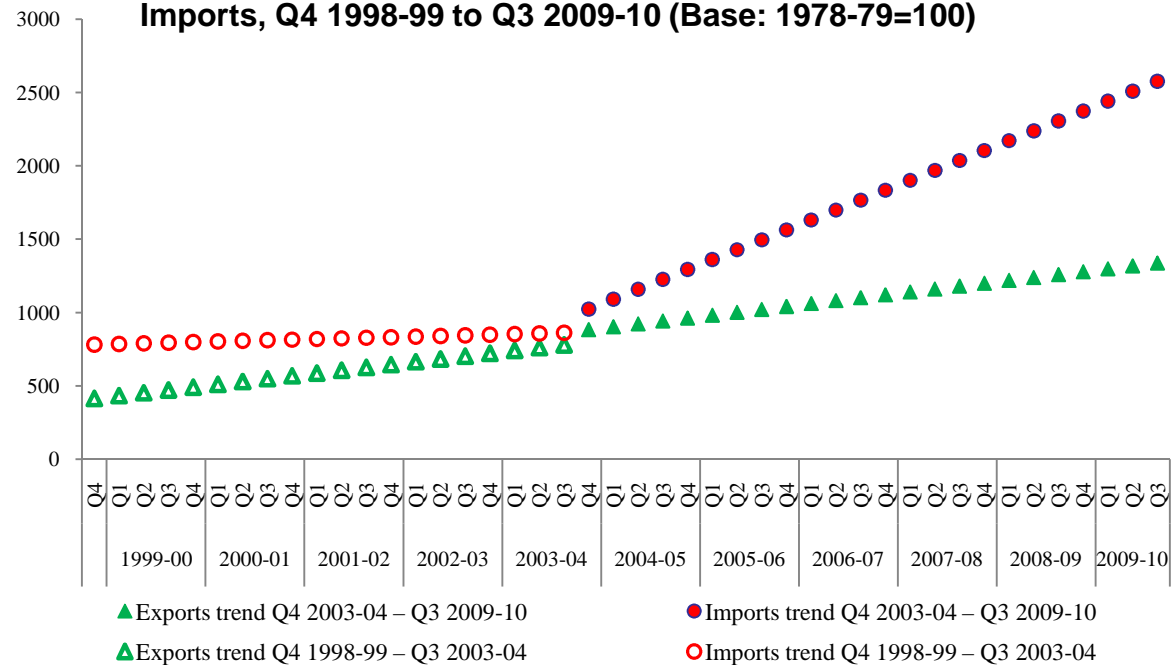
- Progressive deterioration in trade balance since 2003-04, from **2.3%** to **9.0%** in 2009-10

- Invisibles surplus declining since 2008-09

# Structural Break in India's Merchandise Imports

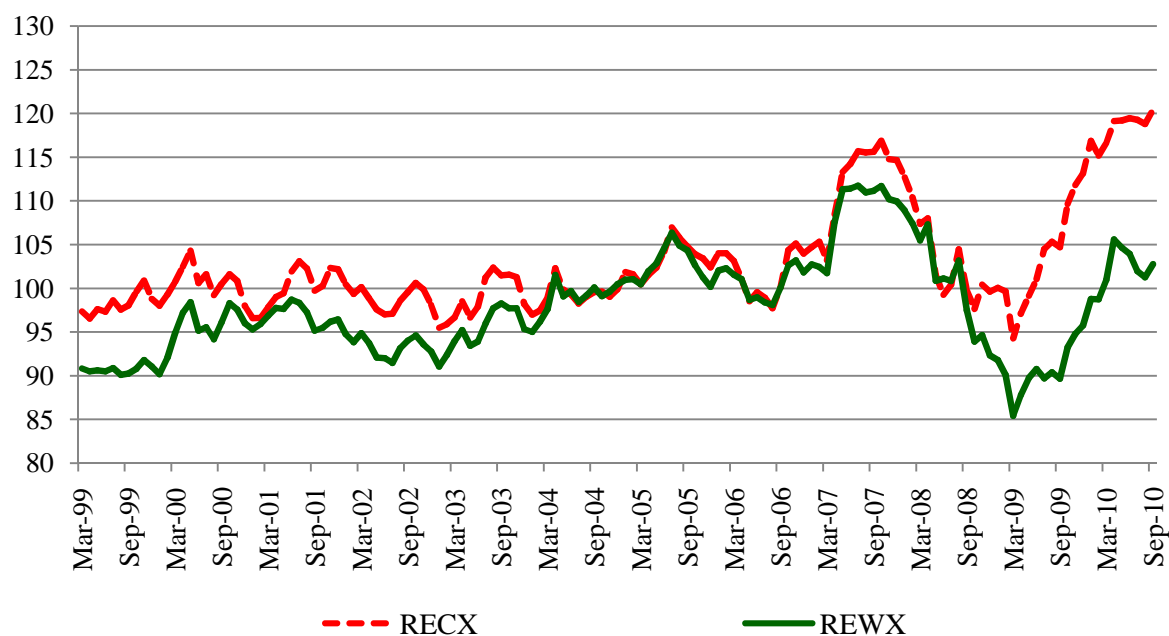


The Trend in the Quantum Indices of Merchandise Exports and Imports, Q4 1998-99 to Q3 2009-10 (Base: 1978-79=100)



*While high domestic growth sucks in huge imports, India lags behind in export competitiveness*

## Index of Real Effective Exchange Rate (REER) for the Rupee (36-Currency Export Weighted, Base: 2004-05=100)



Source: Constructed based on data from IFS, IMF, Labour Bureau (Ministry of Labour and Employment), and Office of the Economic Adviser (Ministry of Commerce and Industry)

- Substantial real appreciation of the rupee from both nominal appreciation and high inflation (more in terms of consumer price index than wholesale price index)
- Huge inflow of portfolio capital putting upward pressure on rupee despite rising current account deficits

# Risks to Growth



- Inflation and rising current account deficits
  - Structural and not cyclical
- Central bank raised policy rates six times since February 2010 and likely to raise again
- Rising global commodity prices and rising interest rates to hurt corporate profits
- Structural reforms necessary to raise the potential growth rate beyond 7-8 per cent



# “The Second Generation Reforms”



- To policy and procedural reforms to pave the way for **speedy infrastructure building**
- **Agricultural reforms** to liberate the farmer for enhanced food production and its better distribution
- **Educational reform** at school, vocational and college levels to raise the labour productivity and remove skill shortages
- **Regulatory reforms** for vastly improving the ease of doing business
- **Raising government efficiency** in the delivery of public services



*Thank You.*