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June 24, 1983

To: Members of the Executive Board

From: The Secretary

Subject: India - Extended Arrangement - Program for 1983/84

Attached for consideration by the Executive Directors is a paper on the program for 1983/84 presented by India under its extended arrangement. A draft decision appears on pages 44, 45, and 46.

This subject has been tentatively scheduled for discussion on Friday, July 22, 1983.

If Executive Directors have technical or factual questions relating to this paper prior to the Board discussion, they should contact Mr. Bruce Smith (ext. (5)7301) or Mr. Ulrich Baumgartner (ext. (5)7307).

Att: (1)

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INTERNATIONAL MONETARY FUND

INDIA

Extended Arrangement--Program for 1983/84

Prepared by the Asian, Exchange and Trade Relations and Fiscal Affairs Departments

(In consultation with the Legal and Treasurer's Departments)

Approved by Tun Thin and Donald K. Palmer

June 21, 1983

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I. Introduction

Attached is a letter from the Minister of Finance, together with a memorandum entitled Statement of Policies, which give details of the policies to be followed and measures taken in 1983/84 (fiscal year ending March 31) in implementing the medium-term balance of payments adjustment program supported by the extended arrangement. The extended arrangement, in an amount of SDR 5,000 million (291 per cent of quota) and for a period of three years, was approved by the Fund on November 9, 1981 (EBS/81/198). The program for 1982/83, the second year covered by the arrangement, was approved on July 9, 1982 (EBS/82/102). To date all performance criteria have been observed and purchases of SDR 2,700 million have been made. As discussed below, it is proposed to provide for additional purchases during the coming year in an amount up to SDR 1,200 million. Executive Directors last discussed the program for India on February 18, 1983 when they considered the staff reports for the 1983 Article IV consultation with India and the mid-year review of the program for 1982/83 (EBS/83/16 and SM/83/28). The program for 1983/84 was discussed during a visit to Bombay and New Delhi of a staff team during April 6-22, 1983. The staff team comprised Messrs. Tun Thin (Head), Smith, Baumgartner, Ms. Schadler, Mr. Burton (all ASD), Messrs. Hino (ETR), Heller (FAD) and Harrison (IBRD) and Ms. Pugh (ASD, Secretary); Mr. Grawe of the World Bank's New Delhi office was also attached to the mission.

II. Recent Economic Developments and Performance Under the Program for 1982/83

In 1981/82 India's economy closely followed the path envisaged for the first year of the adjustment program. However, in 1982/83 the economy deviated considerably from the path foreseen a year ago upon which the program for 1982/83 was based. Most importantly, severe drought was experienced over large areas, especially in the South and East, and the kharif (autumn) food harvest was sharply reduced. Weather was more favorable for the subsequent rabi (spring) harvest and, with intensive efforts to maximize rabi production, a part of the earlier loss to food production has been recouped. Nevertheless, agricultural income is estimated to have fallen by about 2 per cent in 1982/83 compared with an increase of 4 per cent in the previous year.

At the same time, there was a marked slowdown in the industrial sector. This was due to a combination of factors, including the impact of the world recession, both through weak demand abroad and, in conjunction with continued liberal import policies, increased competition in the domestic market; tight credit conditions early in the year; and a major strike in the textile industry which cut aggregate industrial growth by as much as 1.5 percentage points. However, performance in key basic industries and infrastructure continued to improve, with sizable increases in the output of coal (5 per cent), electric power (7 per cent), cement (9 per cent), oil (31 per cent), and fertilizer (9 per cent), although sluggish demand reduced growth in rail freight and steel production. In total, industrial production rose by 4 per cent in 1982/83, compared with 8 per cent in 1981/82.

Reflecting these developments, real GDP is estimated to have grown by no more than 2 per cent in 1982/83, considerably less than the target of 5 per cent (Table 1). Gross domestic capital formation is estimated to have been reduced from 25.3 per cent of GDP to 24.7 per cent and total domestic savings declined by a similar amount. It is estimated that per capita real private consumption was broadly unchanged.

These developments had an adverse impact on public finances. 1/ Budget revenues rose by 16 per cent, slightly faster than the program estimate of 13 per cent, although tax revenues fell somewhat short of the program projections; nontax revenues were higher than anticipated because of higher interest income and larger foreign grants. The tax shortfall was due mainly to lower excise duties, reflecting sluggish economic activity. The shortfall would have been larger except for additional revenue measures, including the 5 percentage point increase in auxiliary import duties introduced in December 1982. In contrast, revised estimates prepared in February 1983 indicate an increase in budget expenditure of 19 per cent, compared with the program estimate of 12 per cent. The unplanned increase in expenditure of Rs 17 billion, equivalent to about 1 per cent of GDP, included additional amounts for drought and flood relief, fertilizer subsidies, and financing under bilateral payments agreements. However, subsequent to the preparation of these revised estimates, the authorities took steps to contain the budget deficit. It is tentatively estimated that efforts to contain expenditures, especially capital expenditures, reduced expenditures as identified in the revised estimates by about Rs 10 billion.

The revised budget estimates indicate that the overall budget deficit in 1982/83 amounted to 6.9 per cent of GDP. However, as a result of the measures to contain the deficit, the staff estimates the deficit would be lower at about 6.3 per cent of GDP, but still higher than estimated in the program. Bank financing of the Central budget deficit is estimated to be 2.4 per cent of GDP, less than the 2.8 per cent estimated in the program and the 2.7 per cent realized in 1981/82. *Public savings increased to 4.8 per cent of GDP from 4.3 per cent in the* previous year, although they fell short of the program target of 5.0 per cent. Central public savings rose to 3.2 per cent of GDP from 2.8 per cent as a result of strong resource mobilization efforts and despite the impact of additional spending on account of flood relief and subsidies; State public savings recorded a smaller increase.

1/ Discussion is confined to the Central Government budget; consolidated budgets for the Centre, States and Union Territories are not available subsequent to the original budget estimates of 1982/83.

Table 1. India: Selected Economic and Financial Indicators, 1981/82-1983/84

	1981/82		1982/83		1983/84	
	Program	Actual	Program	Revised estimate	Program	Revised projection
			(Annual per cent changes)			
National income and prices						
GDP at constant prices	4.8	5.2	5.0	2.0	4.8 1/	6.0-6.5
GDP deflator	9.0	8.7	8.5	3.5	8.0 1/	7.0
Wholesale prices 2/	11.0	2.4	8.0	6.5	8.0 1/	7.0
Consumer prices 3/	...	12.5	...	7.8	...	7.0
External sector (on the basis of SDRs)						
Exports, f.o.b.	16.2	13.9	11.9	3.3	15.0 4/	7.2
Imports, c.i.f.	12.4	5.6	3.9	--	11.8 4/	3.8
Non-oil imports, c.i.f.	29.8	14.4	11.2	6.8	15.2 4/	14.2
Export volume	5	7	7	1	8 4/	5
Import volume	3	-1	-1	-3	7 4/	4
Terms of trade (deterioration -)	--	-4.4	--	-1.7	-0.7 4/	3.2
Nominal effective exchange rate (depreciation -) 2/	...	-2.9	...	-3.6	...	...
Real effective exchange rate (depreciation -) 2/	...	-4.8	...	0.8	...	...
Central Government budget						
Revenue and grants	16.8	21.4	13.0	16.4	...	15.5
Total expenditure and net lending	15.5	14.2	12.0	19.2	...	13.0
Money and credit 5/						
Domestic credit	19.4	18.9	18.6	17.4	17.4 1/	17.8
Government	20.1	19.1	17.9	14.9	16.3 1/	17.3
Commercial sector	18.9	18.7	19.0	19.3	18.1 1/	18.1
Money and quasi-money (M3)	15.7	12.7	15.9	15.8	14.0 1/	15.0
Narrow money	...	6.8	13.8	14.6	11.0 1/	12.0
Interest rate (annual rate,five-year savings deposit)	10.0	10.0	10.0	11.0	...	11.0
			(In per cent of GDP)			
Public sector savings	4.4	4.3	5.0	4.8	5.2 6/	5.4
Central public sector savings	2.9	2.8	3.3	3.2	3.5 6/	3.5
Central Government budget deficit	6.4	5.8	5.6	6.3 7/	6.8 1/	6.5
Domestic bank financing	3.1	2.7	2.8	2.4 7/	2.9 1/	2.9
Foreign financing	0.9	0.7	0.7	0.9	...	0.9
Gross capital formation	25.7	25.3	25.5	24.7	26.5 1/	26.4
Gross domestic savings	23.7	23.2	23.4	22.6	24.3 1/	24.3
Current account deficit	2.0	2.1	2.1	2.1	2.1 4/	2.1
External debt 5/ (inclusive of use of Fund credit)	11.2	11.6	12.0	14.0	13.0 4/	14.4
Debt service ratio 8/9/	8.5	8.2	11.0	10.5	12.8 4/	13.8
Interest payments 8/9/	3.1	3.1	4.3	4.9	5.8 4/	7.1
Overall balance of payments (SDRs mn.)	-1,683	-2,175	-1,683	-1,280	-1,610 4/	-1,497
Gross official reserves (months of imports)	5	4	4	4	3 4/	4
External payments arrears	--	--	--	--	--	--

1/ Original program projections (November 1981).
2/ End-year percentage change.
3/ Annual average percentage change.
4/ Projections made at the time of the 1982/83 program (May 1982).
5/ End of period.
6/ Original program projections (November 1981) including subsequent minor refinements to the statistical definition of savings.
7/ Staff estimate.
8/ In per cent of current receipts.
9/ Including IMF.

The phased ceilings on total domestic credit and the subceilings on net credit to Government were observed during 1982/83 (Table 2). Reflecting the measures taken toward the end of the year to increase Central budget revenues and contain expenditures, the increase in net credit to Government during the year amounted to Rs 46.1 billion, well below the ceiling increase of Rs 55.5 billion under the financial program, and less than the increase of Rs 49.6 billion in 1981/82. Following extremely tight commercial credit conditions during the early months of 1982/83, credit policy was eased, largely by providing assurance of adequate resources to the banks and increased support to selected industries. Nevertheless, the overall stance of monetary policy remained cautious during 1982/83 in view of the inflationary potential of the supply shortfall. Commercial credit growth was subdued early in the year, but accelerated as business conditions became more buoyant. Commercial credit rose by 19 per cent in 1982/83, in line with the program projection, and total credit by 17 per cent, somewhat less than the ceiling increase. Money supply rose by 14.6 per cent, slightly faster than the program target of 13.8 per cent, while the increase in broad money of 15.8 per cent was closely in line with the program target. However, the end-year rate of increase in the money supply is heavily influenced by the tight liquidity position ruling at the end of 1981/82; the average increase in the money supply in 1982/83 was 11 per cent.

Wholesale price inflation remained low during most of 1982/83. Twelve-monthly rates of inflation of 2-3 per cent during much of the year reflect an unusual price decline toward the end of 1981/82 and understate the underlying inflation rate. The 12-monthly rate of inflation rose to 6.5 per cent at the end of 1982/83, more closely in line with the underlying rate, but below the program target of 8 per cent; the average wholesale price inflation rate for the year was lower at 3 per cent and consumer price inflation slowed considerably. The main factors behind the better than expected price performance were continued liberal availability of important commodities, including food items where timely steps were taken to supplement domestic supplies by imports, and the continuation of subdued aggregate demand.

Overall balance of payments pressures eased in 1982/83. While the current account deficit was unchanged at 2.1 per cent of GDP, in line with the program target, the overall deficit fell sharply to SDR 1.3 billion, SDR 0.4 billion less than projected in the program, and considerably less than the deficit of SDR 2.2 billion in 1981/82.

Export performance weakened considerably, especially during the second half of the year. Export earnings (in terms of SDRs) rose by about 8 per cent in the first half of 1982/83, but for the year as a whole the increase is estimated to have been no more than about 3 per cent. This suggests that the increase in export volume was small--about 1 per cent--and well below the target of 7 per cent. As for most countries, the world trade recession had a major, if delayed, impact on India's exports. Exports to developing countries where India has established a considerable presence, especially in Africa, were particularly

Table 2. India: Performance Under the 1982/83 Program and Performance Criteria for the 1983/84 Program 1/

	1982/83						1983/84		
	September 24		December 30		March 31		Program		
	Program	Actual	Program	Actual	Program	Actual	Sept.30	Dec. 30	Mar. 30
	(In billions of rupees)								
Domestic credit	807.29	788.30	856.59	837.76	876.79	868.56	937.00	991.06	1,013.21
	(21.5)	(18.6)	(21.6)	(18.9)	(18.6)	(17.4)	(20.0)2/	(19.4)2/	(17.8)2/
Net credit to Government	339.53	336.30	350.63	345.75	364.53	355.21	385.89	398.09	413.34
	(22.8)	(21.6)	(23.0)	(21.3)	(17.9)	(14.9)	(15.4)2/	(15.4)2/	(17.3)2/
	(In millions of SDRs)								
Nonconcessional external debt:									
1-12 years	1,400	235	1,400	531	1,400	1,269 3/	1,500	1,500	1,500
1-5 years	200	19	200	103	200	120	200	200	200

Sources: Data provided by the Indian authorities and EBS/82/102.

1/ Figures in parentheses are per cent changes over 12 months.

2/ Per cent changes over 12 months based on unadjusted 1982/83 data (for adjustments, see "India--Recent Economic Developments", SM/83/28, 2/7/83, Table 18).

3/ Includes borrowing of $400 million by ONGC which was understood to have been completed in 1982/83 but for which, because of procedural delays, contracting was formally completed only in April 1983. This loan would not be counted against the ceiling for 1983/84 which was established on the understanding that the formal contracting was completed before end-March 1983.

affected by adverse circumstances in these countries. Weak world demand especially affected exports of jute manufactures, textiles, leather and leather goods, iron ore, and iron and steel. Engineering goods, the largest export category, also faced increased competition from producers in industrial countries. In addition, export supplies of rice and tea were reduced by the drought, and exports of cotton textiles and garments suffered as a result of the prolonged textile strike. Importantly, exports to Eastern Europe under bilateral payments arrangements, which had contributed substantially to export growth in the preceding two years, slowed markedly in the latter part of 1982/83.

Lower than projected exports in 1982/83 were matched by a similar reduction in imports which were unchanged from 1981/82. Within the total, the oil import bill fell by 12 per cent because of a 16 per cent decline in import volume, and imports of other bulk items, including fertilizer and iron and steel, also declined; in most cases lower imports were made possible by increased domestic production. In contrast, imports of other than bulk items rose by 20 per cent, as liberal import policies allowed sizable increases in imports of producer materials and capital goods. Net invisible earnings fell by 12 per cent reflecting a deterioration on investment income account; remittances from Indian workers abroad were unchanged at SDR 1.5 billion.

Net nonmonetary capital inflows (including net errors and omissions) rose from SDR 0.8 billion in 1981/82 to SDR 1.8 billion in 1982/83. Net aid inflows rose to SDR 1.5 billion, and net commercial loan disbursements increased to SDR 0.3 billion. In addition, a short-term bridging loan of SDR 0.4 billion was arranged for oil sector financing, which will be repaid in 1983/84. Commitments of nonconcessional external loans subject to the ceiling of SDR 1.4 billion amounted to SDR 1.3 billion in 1982/83, excluding SDR 0.5 billion for a loan for a thermal power plant for which the ceiling is automatically adjusted upward; those subject to the subceiling of SDR 200 million amounted to SDR 120 million. Net capital outflows under bilateral payments arrangements amounted to SDR 0.4 billion, considerably higher than had been expected; the increase was due partly to import delays in the latter part of the year. After taking account of Fund purchases, and including valuation gains, international reserves rose by SDR 0.6 billion in 1982/83. At end-March 1983 international reserves amounted to SDR 4.9 billion (including SDR 0.3 billion of gold valued at SDR 35 per ounce), equivalent to four months of 1983/84 imports.

III. The Program and Prospects for 1983/84

1. Introduction

a. An outline of the 1983/84 program

The extended arrangement envisages that adjustment of India's balance of payments position will be achieved in line with the medium-term strategy described in detail in EBS/81/198. Briefly, a gradual improvement in the balance of payments is to be achieved through a strengthening of export performance and the replacement of imports where India is an efficient producer. To promote this, substantial investments in basic industry and infrastructure are required to overcome and prevent the recurrence of bottlenecks which have been a perennial constraint on growth and the external sector. To provide resources for the large investments and contribute to adjustment, domestic savings are to increase, including, in particular, a substantial increase in public savings. Economic efficiency and the adjustment process are to be promoted by reducing regulatory and pricing constraints in industry and by liberalizing imports. Financial policies are to aim at ensuring the stable environment necessary for adjustment and strengthening the efficiency of resource allocation.

The policy program for 1983/84 is framed to overcome the delayed effects of adverse developments in 1982/83 and assist in the transition to economic recovery, while continuing progress toward the medium-term goals of the adjustment program. A summary of the program is contained in Supplement 1. In brief, monetary and financial policies are designed to contain latent inflationary pressures and encourage savings. Budgetary policy will contain budget recourse to the banking system within limits which avoid crowding out commercial borrowers, and public savings are targeted to rise substantially. The public investment program is increased and efforts are made to ensure that, as far as possible, adequate funding is provided in areas important to external adjustment. The program also includes steps to reduce controls on private industry and to reduce import restrictions; the latter also include measures designed to encourage export development.

The program for 1983/84 includes the following performance criteria:

(1) A phased ceiling on total domestic credit and a phased subceiling on net credit to the Government.

(2) A ceiling on the official contracting or guaranteeing of nonconcessional external debt with original maturities between 1 and 12 years, with a subceiling for maturities between 1 and 5 years.

(3) A review before January 30, 1984 of progress made in implementing the program, including in particular policies relating to the resource position of the Central and State Governments and their enterprises in light of the public finance targets for 1983/84; all aspects of export development; and progress in implementing import liberalization.

(4) The usual understanding relating to exchange restrictions, multiple currency practices, bilateral payments agreements, and import restrictions for balance of payments reasons.

b. The amount and phasing of purchases

The decision granting the extended arrangement for India (EBS/81/198, Supplement 3, November 13, 1981) as amended, (EBS/81/198, Supplement 4, February 24, 1982 and EBS/82/102, June 11, 1982) provides for purchases of SDR 900 million in support of the program for 1981/82 and SDR 1,800 million for the program for 1982/83. The Executive Board has not yet taken a decision regarding the amount of purchases to be made in support of the program for 1983/84, although Executive Directors were provided an indication of the level of purchases envisaged in 1983/84 and 1984/85 to the end of the arrangement at the time the program for 1982/83 was presented to the Board in July 1982 (EBS/82/102). It was envisaged that, based on then current projections, purchases against the 1983/84 program would be SDR 1.5 billion, with SDR 0.8 billion being provided for the remaining seven months of the arrangement.

At the time (late 1981) when India's request for an extended arrangement was being considered, the staff and Executive Directors examined the issues of balance of payments need and of the mix of various forms of balance of payments financing. It was explained that the proposed amount of Fund financing had been established so as to contribute a balanced share of a mix of financing, which included also increased reliance on borrowing on international capital markets and a considerable drawdown in international reserves. It was also recognized that purchases under the arrangement would be subject to the requirement of balance of payments need.

During the intervening period, balance of payments pressures have eased perceptibly. Both the current and overall deficits in 1982/83 were lower than originally expected, and balance of payments prospects for the remainder of the program period are more favorable than earlier projected. The cumulative current account deficit during the four years 1981/82 to 1984/85 within which the extended arrangement falls is now estimated to be SDR 12.7 billion, SDR 1.9 billion less than originally projected. Similarly, the cumulative overall deficit during the same period is now estimated to be SDR 5.8 billion, compared with the original projection of SDR 7.2 billion. As a result, India's own contribution to financing the deficits through the drawdown in international reserves, which was projected to total SDR 2.4 billion, would be reduced to SDR 1 billion were the level and phasing of Fund financing unchanged.

As discussed below, the overall balance of payments deficit in 1983/84 is now estimated to be SDR 1.5 billion, considerably less than the original projection of SDR 2.7 billion. It is proposed that the Fund financing under the extended arrangement for 1983/84 be provided in an amount of SDR 1.2 billion. This amount could be increased to up to SDR 1.5 billion if the Fund decides that unforeseen balance of payments developments warranted such an increase. This could be done in the context of the mid-term review.

It is proposed that, subject to the possibility of amendment, purchases for 1983/84 be phased as follows: SDR 400 million following the reaching of understandings between the Fund and India on the program for 1983/84; a further SDR 200 million after October 29, 1983 upon the observance of the ceilings for September 1983 and other performance criteria; a further SDR 400 million after January 29, 1984 upon the observance of the ceilings for December 30, 1983 and other performance criteria, and the completion of the mid-term review of policies; and a further SDR 200 million after April 29, 1984 upon observance of the ceilings for March 31, 1984 and other performance criteria (Table 3). This pattern of purchases within the year is similar to that established for 1982/83.

2. Output and demand management

a. Growth and inflation, savings, and investment

The economy is poised for recovery. Assuming that weather during the coming monsoon season is average, the prospects for 1983/84 are for real growth of 6.0-6.5 per cent (Table 4 and Chart 1). Based on this projection, average growth in the first four years of the Sixth Plan would be slightly above the Plan target of 5.2 per cent established for the five years to 1984/85. Given average weather, value-added in agriculture is projected to increase by 5 per cent which, following the setback in 1982/83, would represent a return to the path of production originally envisaged. With appropriate policies, industry is expected to emerge from the mild recession in 1982/83, and manufacturing growth is projected to be 7 per cent, in line with the original program projection.

With the recovery in growth and supportive policies, gross domestic savings are projected to rebound from the setback in 1982/83 and reach the original program projection of 24.3 per cent of GDP in 1983/84. Gross capital formation is expected to amount to 26.4 per cent of GDP in 1983/84, close to the original program target and substantially higher than in 1982/83. This investment projection reflects the continuing efforts to improve the environment for private investment and a further increase in the ratio of public Plan outlays to GDP.

In the absence of external price shocks, both wholesale and consumer prices are projected to increase by about 7 per cent in 1983/84, somewhat less than the original program target and broadly in line with the recent underlying rate of inflation. Price pressures would strengthen somewhat as a result of the lagged effects of last year's drought and recent increases in key administered prices and indirect taxes. Furthermore, it is expected that some sections of industry will attempt to restore profit margins which were eroded during 1982/83. However, continued cautious demand management and policies to import liberally to maintain adequate supplies are expected to contain inflationary pressures and further consolidate the progress made in controlling inflation since the beginning of the adjustment program.

Table 3. India: IMF Position, November 1981-April 1984

(In millions of SDRs)

	Actual							Proposed			
	Nov.30 1981	Jan.15 1982	Apr.21 1982	July 14 1982	Nov.4 1982	Feb.24 1983	May 16 1983	July 30 1983	Oct.30 1983	Jan.30 1984	Apr.30 1984
Purchases	300	300	300	600	300	600	300	400	200	400	200
Extended Fund Facility	300	300	300	600	300	600	300	400	200	400	200
Ordinary resources	(150)	(150)	(150)	(300)	(150)	(300)	(150)	(200)	(100)	(200)	(100)
SFF	(--)	(--)	(--)	(300)	(150)	(300)	(150)	(200)	(100)	(200)	(100)
EAR	(150)	(150)	(150)	(--)	(--)	(--)	(--)				
Repurchases	--	--	--	--	--	--	--	--	--	33	33
Net purchases	300	300	300	600	300	600	300	400	200	367	167
Fund holdings 1/											
Total (cumulative)	1,954	2,254	2,519	3,119	3,419	4,019	4,319	4,719	4,919	5,286	5,453
Holdings in per cent of quota 2/	113.8	131.2	146.7	181.6	199.1	234.0	251.5	274.8	286.4	307.8	317.5

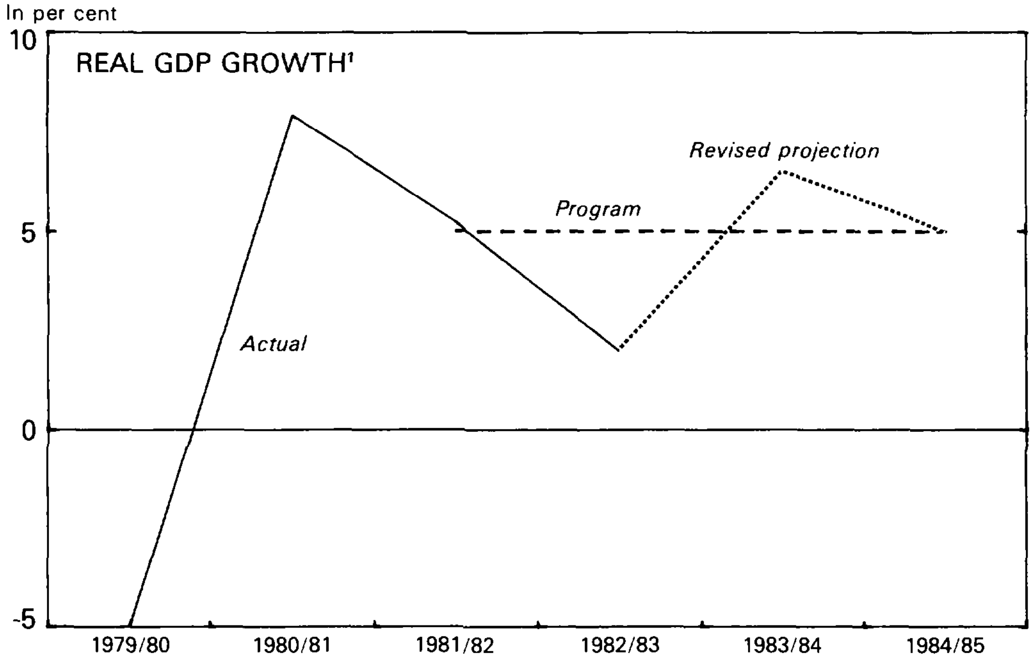
Source: Staff projections.

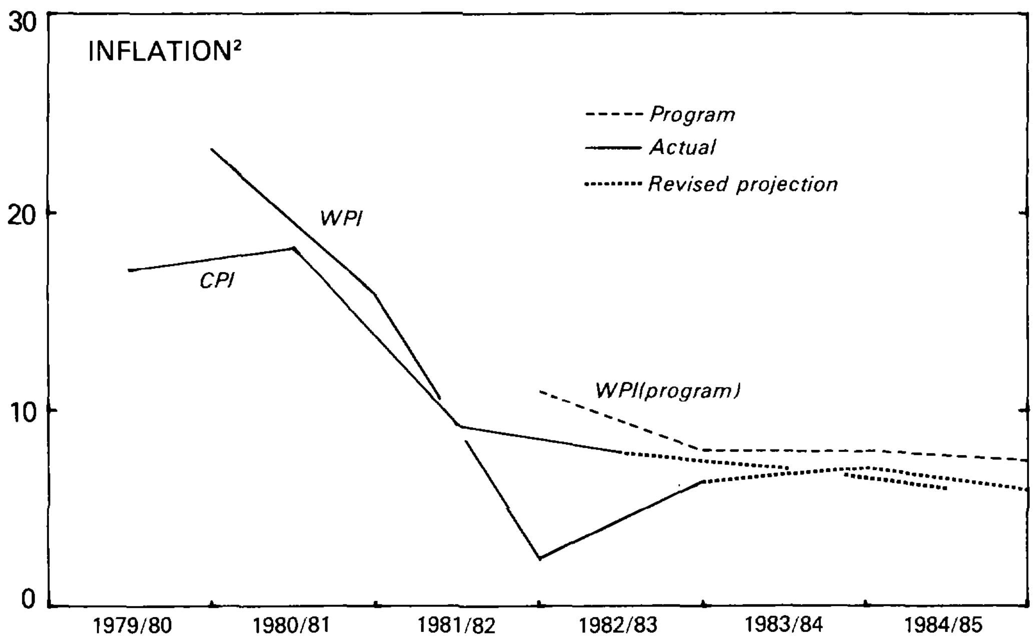
1/ At end-period and based on India's present quota of SDR 1,717.5 million.
2/ Purchases under the extended arrangement float above the reserve and first credit tranches.

CHART 1

INDIA

REAL GDP GROWTH AND INFLATION, 1979/80-1984/85





Sources: EBS/81/198, data provided by the Indian authorities, and staff projections.
[1]GDP at factor cost (at constant prices).
[2]WPI (end of fiscal year), CPI (fiscal year average).

Table 4. India: Growth, Prices, Savings and Investment, 1980/81-1983/84

(In per cent)

		1981/82		1982/83		1983/84	
	1980/81	Program	Actual	Program	Revised estimate	Original program	Revised estimate
Real growth rates							
GDP at factor cost	7.9	4.8	5.2	5.0	2.0	4.8	6.0-6.5
Agriculture	12.9	1.4	3.5	1.7	-2.0	1.4	5.0
Manufacturing	2.9	7.3	5.8	7.0	3.5	7.3	7.0
Prices							
GDP deflator	12.0	9.0	8.7	8.5	3.5	8.0	7.0
Wholesale prices 1/	15.8	11.0	2.4	8.0	6.5	8.0	7.0
Consumer prices 2/	11.4	...	12.5	...	7.8	...	7.0
Savings							
Gross domestic savings/GDP	22.2	23.7	23.2	23.4	22.6	24.3	24.3
Public savings/GDP	3.7	4.4	4.3	5.0	4.8	5.2	5.4
Central Government savings/GDP	2.3	2.9	2.8	3.3	3.2	3.5	3.5
Investment							
Gross capital formation/GDP	23.8	25.7	25.3	25.5	24.7	26.5	26.4
Public Plan outlays/GDP	11.7	11.8	12.3	12.5	13.9 3/	14.1	14.3
Foreign capital inflow/GDP	1.6	2.0	2.1	2.1	2.1	2.2	2.1

Sources: Data provided by the Indian authorities and staff estimates.

1/ End-year percentage change.
2/ Annual average percentage change.
3/ Based on revised estimates. Subsequent expenditure reduction measures would reduce this figure.

Agricultural policies in 1983/84 will continue to be aimed at increasing production of foodgrains and other crops which have important implications for the balance of payments, as well as ensuring adequate stocks of foodgrains. A central element of efforts to promote modern production techniques is the program to expand the area under irrigation. The area under irrigation increased by 2.4 million hectares in 1982/83, slightly less than the program target, and a further increase of 2.5 million hectares is targeted for 1983/84. With the expansion in irrigation and normal weather, fertilizer consumption is projected to increase by up to 12 per cent, following a 5 per cent increase in 1982/83, and the use of high-yielding seed varieties is projected to expand further. The authorities have recently introduced programs to encourage the cultivation of oilseeds on irrigated land and marginal foodgrain land, promote more intensive cultivation of pulses, and improve the productivity of small and marginal farmers. Foodgrain production is targeted to increase to a record 142 million tons from 125-128 million tons in 1982/83, and that of oilseeds is expected to rise to 12.5 million tons, up from 11 million tons in 1982/83. Nevertheless, some precautionary foodgrain imports may be necessary to augment stocks. Production of export crops such as tea, coffee and jute is expected to increase significantly in 1983/84. Sugarcane production reached a high in 1981/82 and fell slightly to 177 million tons in 1982/83; a further small cyclical decline is likely in 1983/84. The Government is making efforts to reduce the cyclical swings in sugar production and prices by adjusting sugar releases, and by introducing a buffer stock scheme. Agricultural pricing policies continue to aim at providing adequate producer incentives and ensuring sufficient supplies for the official foodgrain distribution system, where stocks are projected to rise moderately over the course of 1983/84. The procurement price of wheat was recently raised to offset cost increases and enable a buildup of stocks, and a support price for barley was also announced; procurement prices for the coming kharif season will be determined according to the same policy.

Industrial activity is likely to accelerate in 1983/84. The process of inventory adjustment induced by continued high interest rates in the face of declining inflation is running its course. Tight credit conditions which affected some industries in 1982/83 have also eased, partly as a result of selective credit measures. The drought-induced decline in agricultural incomes would be expected to continue to depress demand for industrial goods in the first part of 1983/84, although a good rabi harvest and the projected recovery in agricultural production in 1983/84 would strengthen demand in due course. A further sizable increase in public investment expenditure will also provide a boost to industry. The expected recovery in the world economy would have beneficial effects, both through increased external demand and reduced import competition in some sectors. The recent resumption of normal activity in most textile plants, following the virtual conclusion of the strike, will result in a noticeable increase in industrial activity as a whole. Supplies of basic goods and infrastructure appear likely to be adequate to support the more rapid industrial growth projected for 1983/84.

b. The financial program for 1983/84

Following the tight liquidity position ruling during early 1982/83, money and credit growth began to pick up toward the middle of the year. At about the same time, it became clear that the effect of the drought on agricultural output would reduce real growth to well below the forecast of 5 per cent made when the financial program was formulated. Nevertheless, a downward revision in the original money and credit targets for the year was judged unnecessary because it was expected that the reduction in agricultural income would affect the demand for money with a lag. An immediate tightening of monetary policy could have intensified recessionary conditions experienced in some sections of industry. In the event there is no evidence to indicate that monetary developments in 1982/83, which were broadly in line with the financial program, resulted in a discernible buildup in inflationary pressure during the second half of the year.

The financial program for 1983/84 takes into account the expected impact of the decline in agricultural income in 1982/83 on the demand for money in 1983/84. The staff expects that marketed output, which includes agricultural output with a lag, will rise by only 5 per cent in 1983/84, less than the projected growth in aggregate GDP of 6-6.5 per cent. The increase in marketed output, together with projected inflation of 7 per cent, will influence the demand for narrow money in its primary role as a medium for transactions. These factors, together with deposit interest rates (the maximum rate among which was raised by 1 percentage point in October 1982) will also influence growth in time deposits, which are a major repository for savings. On this basis, narrow money is projected to increase by 12 per cent in 1983/84, somewhat less than in 1982/83. 1/ Time deposits are projected to increase by 16.9 per cent, closely in line with the increase in 1982/83. As a result, the projected increase in broad money is 15 per cent, somewhat below the rate of 15.8 per cent in 1982/83.

Allowing for the expected contractionary influence of foreign transactions, and a normal increase in net other liabilities of the banking system, total domestic credit is targeted to increase by 17.8 per cent in 1983/84 (Table 5 and Chart 2). This is somewhat less than the increase of 18.6 per cent provided for in the program for 1982/83 but slightly more than the actual increase in that year. Within the aggregate credit ceiling, the expansion in net credit to Government will be limited to 17.3 per cent, compared with an increase of 17.9 per cent provided for in the program for 1982/83; this subceiling is derived from the budgetary prospects and the target for public savings for 1983/84 which are discussed below. This would allow for an increase in credit to the commercial sector of 18.1 per cent, somewhat less than provided

1/ Income velocity of circulation is estimated to increase in 1983/84, mainly on account of the lagged impact of changes in agricultural output; if the estimated increase in marketed output is substituted for that in GDP, there would be virtually no increase in velocity.

Table 5. India: The 1983/84 Financial Program

(In billions of rupees)1/

	March 1982 Actual	March 1983 Program	March 1983 Actual 2/	Projections 3/ 1983 September 30	Projections 3/ 1983 December 30	Projections 3/ 1984 March 31
Domestic credit (ceiling)	739.58	876.79 (18.6)	868.56 (17.4)	937.00 (20.0)	991.06 (19.4)	1,013.21 (17.8)
Net credit to Government (subceiling)	309.11	364.53 (17.9)	355.21 (14.9)	385.89 (15.4)	398.09 (15.4)	413.34 (17.3)
Credit to commercial sector	430.47	512.26 (19.0)	513.35 (19.3)	551.11 (23.4)	592.97 (22.2)	599.87 (18.1)
Net foreign assets	26.61	9.01	15.22	7.99	3.64	0.74
Other liabilities (net)	-141.31	-161.66	-160.19	-161.70	-171.55	-181.81
Broad money	624.88	724.14 (15.9)	723.59 (15.8)	783.29 (17.5)	823.15 (15.3)	832.14 (15.0)
Narrow money	247.92	282.13 (13.8)	284.16 (14.6)	297.12 (15.5)	314.85 (12.6)	318.26 (12.0)
Time deposits	376.96	442.01 (17.3)	439.43 (16.6)	486.17 (18.8)	508.30 (17.0)	513.88 (16.9)

Source: Data provided by the Indian authorities.

1/ Figures in parentheses are per cent changes over 12 months.

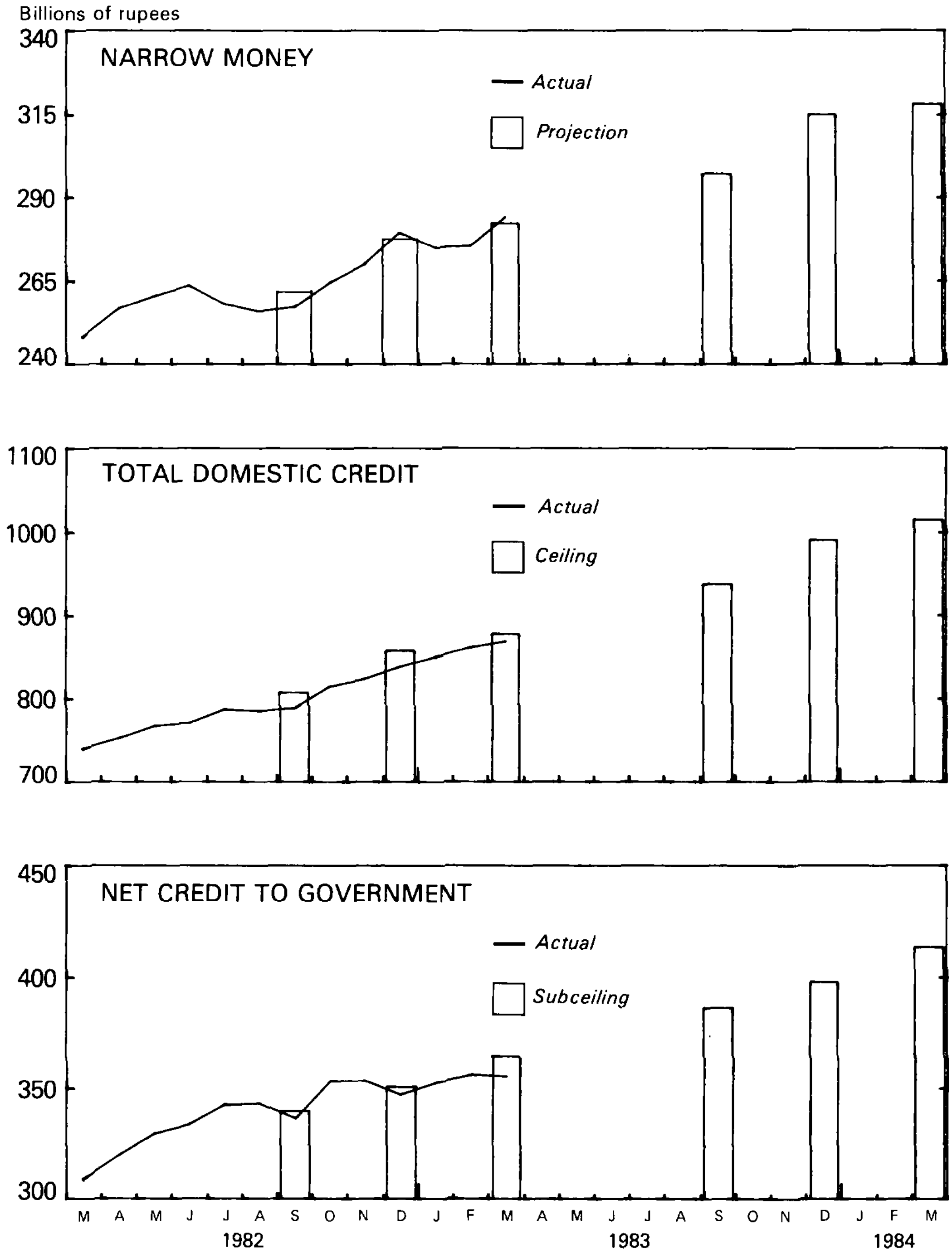
2/ Adjusted for the use of SDRs and other factors to maintain comparability with base data (for details of adjustments, see "India--Recent Economic Developments", SM/83/28, Table 18).

3/ Growth rates are over comparable unadjusted 1982/83 data.

CHART 2

INDIA

PERFORMANCE UNDER THE 1982/83 FINANCIAL PROGRAM AND PROJECTIONS FOR 1983/84



Sources: Data provided by the Indian authorities and EBS/82/102.

in the program for 1982/83 and the actual increase in that year. However, within the total increase in credit, the share provided for the commercial sector is the same as in the program for 1982/83 (60 per cent). The provision for 1983/84 is expected to be fully adequate to support the economy's recovery during the year, especially because some sectoral credit needs, e.g., food and sugar, may be lower than in 1982/83. Table 5 also provides details of the intermediate ceilings for total domestic credit and subceilings on net credit to Government for September and December 1983 which are derived on the same basis as those for 1982/83 and take account of expected seasonal credit needs.

The authorities recognize that continued caution in credit policies will be required to implement the financial program. Measures were recently announced to provide for an appropriate distribution of commercial credit throughout the year and avoid the need for stringent measures later should the recent tempo of credit expansion continue. On April 30, 1983 the Reserve Bank announced a two-stage increase in the cash reserve ratio, from 7 to 7.5 per cent effective May 27, 1983 and to 8 per cent effective July 29, 1983.

3. Fiscal policy, public savings and investment

a. The 1983/84 budget

The Central Government budget for 1983/84 provides for an increase in revenue and grants of 14 per cent over the revised 1982/83 estimates relative to a 9 per cent increase in expenditure and net lending, with an overall deficit of Rs 108 billion, equivalent to 6.1 per cent of GDP (Table 6). Official budget estimates do not provide an estimate of bank financing of the deficit. 1/ The growth in revenues envisaged in the 1983/84 budget is buoyed by steps taken since November 1982 and preceding the budget, which are projected to yield about Rs 10 billion in 1983/84. These measures included an increase in auxiliary import duties in December 1982 and a 17 per cent increase in the price of domestically produced crude oil introduced in February 1983. New measures in the 1983/84 budget were mainly in the areas of personal and corporation income tax, customs duties, and excises, and are expected to yield an additional Rs 6 billion (net) in 1983/84. 2/ On the expenditure side, the 1983/84

1/ Deficit financing, as officially defined, includes net Treasury bill issues and net changes in cash balances, but excludes bank subscriptions to market borrowings.

2/ The principal measures in the 1983/84 budget were an increase in the rate of the surcharge on the income tax on noncorporate income; an increase in the standard deduction and exemption; an increase in deductions for exporters; an increase in the general rate of depreciation for investments in plant and machinery; a halving of the interest tax; disallowal for income tax purposes of a portion of the entertainment and travel expenses of businesses; a further 5 percentage point increase in the auxiliary customs duties; increased tariffs on chemicals, zinc and lead; and a 52 per cent increase in the excise duty on cement.

Table 6. India: Summary of Central Government Budget, 1980/81-1983/84

(In billions of rupees)

	1980/81	1981/82	1982/83 Budget	1982/83 Program	1982/83 Revised est. 1/	1983/84 Budget	1983/84 Program
Total revenue and grants	128.3	155.7	175.9	176.0	181.2	206.3	209.3
Current revenue	124.6	152.5	173.7	173.8	178.0	202.8	205.8
Foreign grants	3.7	3.2	2.2	2.2	3.2	3.5	3.5
Total expenditure and net lending	211.5	241.6	265.5	270.6	287.9 2/	314.3	325.3
Current expenditure	136.0	158.7	182.3	184.8	194.2	224.2	227.2
Capital expenditure and net lending	75.5	82.9	83.2	85.8	93.7	90.1	98.1
Overall deficit	-83.2	-85.9	-89.6	-94.6	-106.7 2/	-108.0	-116.0
Net external financing	13.4	10.3	14.7	12.5	13.9	16.1	16.1
Gross	17.3	14.5	19.3	17.0	18.3	20.6	20.6
Repayment	3.9	4.2	4.5	4.5	4.4	4.5	4.5
Domestic borrowing	69.8	75.6	74.8	82.1	92.8	91.9	99.9
Net market borrowing	25.8	29.1	32.0	32.0	38.0	40.0	40.0
Nonmarket and miscellaneous financing	18.3	32.6	29.0	29.1	35.5	36.4	36.4
Official deficit financing	25.7	13.9	13.8	21.0	19.3	15.5	23.5
Memorandum items:							
Bank financing							
Central Government	50.6	39.2	...	47.0	37.1 3/	...	52.0
Central and State Governments	57.1	49.6	...	55.5	46.1 4/	...	61.0
				(In per cent of GDP)			
Overall deficit	6.6	5.8	5.3 5/	5.6 5/	6.3 6/	6.1	6.5
Bank financing							
Central Government	4.0	2.7	...	2.8 5/	2.4	...	2.9
Central and State Governments	4.5	3.4	...	3.3 5/	3.0	...	3.4

Sources: 1983/84 budget documents and data provided by the Indian authorities.

1/ Based on information available at the beginning of 1983 which is published in the 1983/84 budget.

2/ Expenditure reduction measures taken after the revised estimates were prepared are estimated to result in actual expenditures and the overall deficit being reduced by about Rs 10 billion from these amounts in the revised estimates.

3/ Estimated actual.

4/ Actual.

5/ Based on May 1982 estimate of GDP.

6/ Based on estimated overall deficit taking account of expenditure reduction measures.

budget projects an increase in the share of current expenditure in the total to 71 per cent from 69 per cent in the original budget for 1982/83. In part, this reflects a growth in subsidies (including those on food and fertilizers) and interest payments; total subsidies rose from Rs 19.9 billion (1.4 per cent of GDP) in 1981/82 to Rs 23.9 billion (1.5 per cent of GDP) in 1982/83 and are projected to rise further to Rs 26.5 billion (1.5 per cent of GDP) in 1983/84. The budget also continues the recent trend to reduce the share of Central Government budgetary financing of total Plan expenditures; Central budgetary financing is estimated to account for 50.4 per cent of Plan expenditure compared with 53.6 per cent in the 1982/83 budget.

As was the case last year, the authorities indicate that the budget represents an ambitious goal toward which they will aim, but the program, to be realistic, should make allowance for likely supplementary expenditures and other contingencies. The agreed program for 1983/84 provides for additional revenues of Rs 3 billion beyond those envisaged in the budget, and supplementary expenditures of Rs 11 billion. On the revenue side, economic recovery as now projected would be expected to yield greater revenue buoyancy, especially in corporation taxes and customs duties. Of the supplementary expenditures provided for in the program, Rs 3 billion would be for current expenditure to cover automatic cost of living adjustments beyond those provided for in the budget, and disaster relief. The remaining Rs 8 billion would be for additional budget support for the Plan. This is expected to be required to supplement investment provisions in the budget in key sectors; it is expected that a part of the total amount will be provided to the States to augment State Plan resources in such sectors.

Taking account of these adjustments, the overall deficit would rise to Rs 116 billion, equivalent to 6.5 per cent of GDP, which is somewhat higher than in 1982/83, but less than the 6.8 per cent envisaged in the original program (Chart 3). Consistent with this deficit, bank financing of the Central Government is estimated to be Rs 52 billion, or 2.9 per cent of GDP, which is in line with the original program target although higher than bank borrowing of 2.4 per cent of GDP realized in 1982/83. Allowing for bank financing of State deficits, including net bank subscriptions to State Government market loans of Rs 9 billion, which is the same as the estimate for 1982/83, total bank financing of the Government is programmed to be Rs 61 billion in 1983/84; this has been adopted as the subceiling on net credit to Government in the financial program. As a percentage of GDP, bank financing of the Government would amount to 3.4 per cent in 1983/84, which is somewhat larger than the program allowance in 1982/83 (3.3 per cent) and the actual recourse to bank financing (3.0 per cent).

b. Public savings, resource mobilization, and financing of the Annual Plan

A major element of the adjustment program is the policy to increase public savings. For 1983/84, public savings are estimated to rise by 26 per cent to Rs 96.2 billion (Table 7). As a percentage of GDP public savings would be 5.4 per cent, compared with the original program projection of 5.2 per cent. This would mark a continuation of the persistent increases in the public savings ratio during the program from 3.6 per cent in 1980/81. As a result, the share of total Plan expenditures financed by public savings, rather than from borrowing, has risen steadily from 30 per cent in 1980/81 to an estimated 38 per cent in 1983/84, while over the same period Plan expenditures have risen by as much as 70 per cent.

Central public sector savings are projected to increase by 26 per cent to Rs 63.1 billion (3.5 per cent of GDP) in 1983/84. Within this amount, budgetary savings (consistent with the program budgetary projections discussed above) are estimated to increase only slightly, mainly because of the sizable increase projected for current expenditures. The bulk of the increase in Central public sector savings is projected to derive from increased surpluses of Central public enterprises, which are estimated to rise by 38 per cent to Rs 45.5 billion. This program projection is 5 per cent below the estimate in the 1983/84 budget, the reduction being made to allow realistically for the impact on enterprise profits of higher petroleum prices, rail tariffs and wage costs and other changes in administered prices which have a pervasive impact on business costs. The authorities have indicated that cost increases in several public industries have eroded profitability and that in these areas consideration will be given to timely pricing adjustments and other steps to restore adequate profitability.

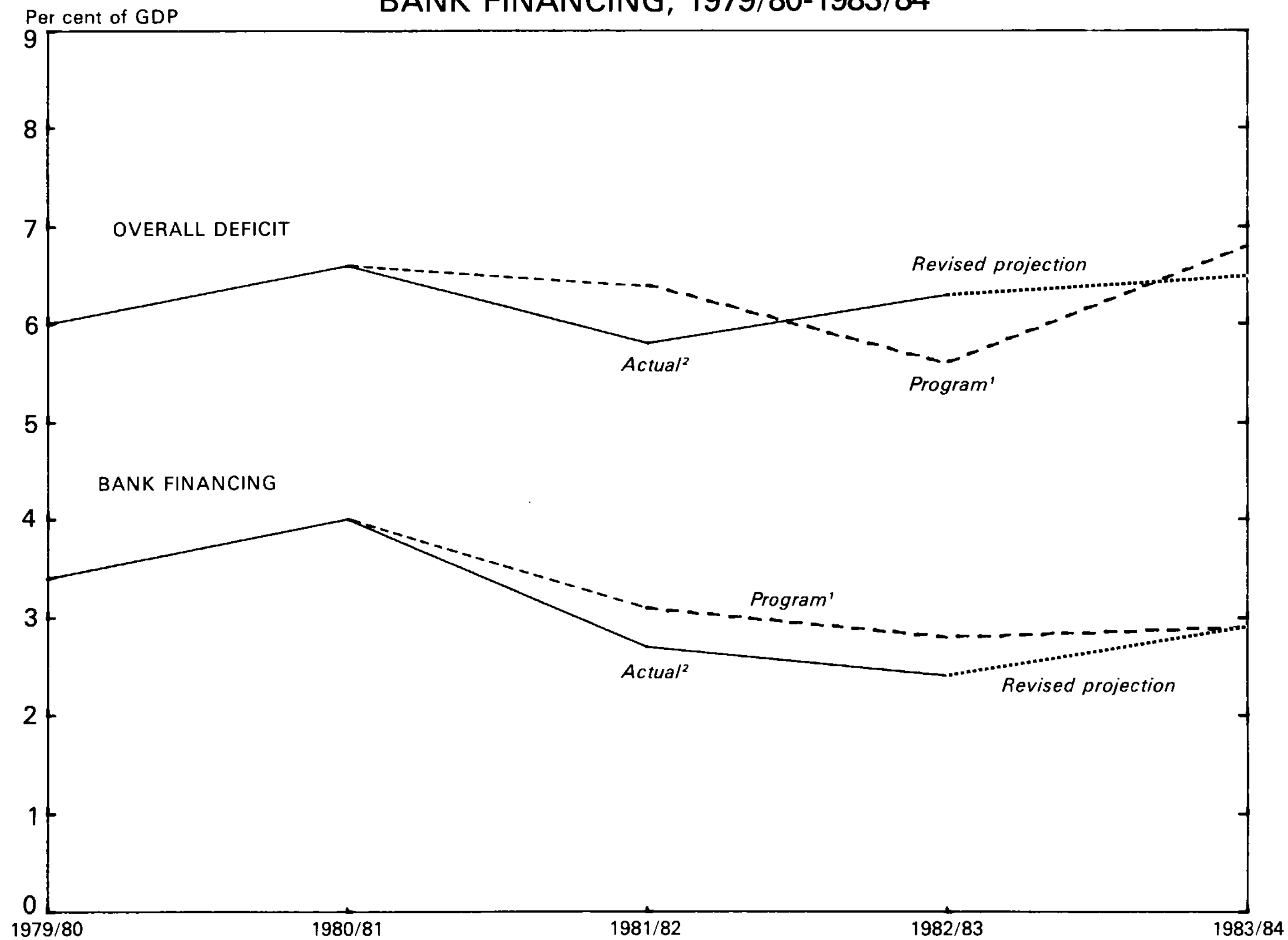
The large increase in the surpluses of public enterprises reflects the strength of the Government's resource mobilization effort. A major part of the increase is due to the full year effect of the increases in administered prices made during 1982/83, including in particular the increase in domestic petroleum prices in February 1983 (EBS/83/16, Supplement 1). Increases in railway and postal tariffs introduced broadly coincident with the 1983/84 budget will yield an additional Rs 4.4 billion in 1983/84. In total, resource mobilization measures undertaken by the Central Government and its enterprises since November 1982, including those contained in the 1983/84 budget, are projected to yield Rs 24 billion, equivalent to 1.3 per cent of GDP, during the current year.

State savings are expected to rise by 32 per cent to Rs 33.1 billion in 1983/84; as a proportion of GDP, State savings would be 1.9 per cent compared with 1.7 per cent in the original program and 1.6 per cent in 1982/83. State resources for Plan financing derive almost entirely from the budgetary savings of the State Governments. On balance, State nonfinancial enterprises generate negligible savings as a consequence of

CHART 3

INDIA

CENTRAL GOVERNMENT OVERALL DEFICIT AND BANK FINANCING, 1979/80-1983/84



Sources: EBS/81/198, EBS/82/102, data provided by the Indian authorities and staff estimates.
[1]Includes May 82 revisions.
[2]Staff estimates for 1982/83.

Table 7. India: Public Sector Savings for Plan Financing, 1980/81-1983/84

(In billions of rupees)

	1980/81	1981/82	1982/83 Program 1/	1982/83 Revised	1983/84 Original program 2/	1983/84 Budget	1983/84 Revised program
Central public sector resources	29.1	41.9	55.0	50.2	65.2	65.5	63.1
(Per cent of GDP)	(2.3)	(2.8)	(3.3)	(3.2)	(3.5)	(3.7)	(3.5)
Budgetary resources	12.7	19.0	21.1	17.2	29.1	17.6	17.6
Nonfinancial enterprises	16.4	22.9	33.9	33.0	36.1	47.9	45.5
State public sector resources	16.9	21.4	29.1	25.0	32.9	30.0	33.1
(Per cent of GDP)	(1.3)	(1.5)	(1.7)	(1.6)	(1.7)	(1.7)	(1.9)
Public savings available for Plan financing	46.0	63.3	84.1	75.2	98.1	95.5	96.2
(Per cent of GDP)	(3.6)	(4.3)	(5.0)	(4.8)	(5.2)	(5.4)	(5.4)

Sources: EBS/81/198; EBS/82/102; EBS/83/16; 1983/84 budget documents; and staff estimates based on discussions with the Indian authorities.

1/ From EBS/82/102, Table 10.
2/ Revised slightly from EBS/81/198, Table 10, mainly to exclude borrowing by public enterprises from the definition of savings.

persistent losses by some State Electricity Boards and State Road Transport Corporations. State Governments have agreed to raise an additional Rs 8.3 billion in revenues in 1983/84. Some of the States have already announced specific resource mobilization measures; these include increased electricity tariffs, revenues from the sale of State property, improved tax administration, additional sales and excise taxes, increased irrigation fees, and higher cesses on agricultural products. In addition, most State Electricity Boards have agreed to a program which will generate more resources while at the same time establishing a ceiling on rural electrification subsidies paid by State Governments.

The projected levels of public sector savings, together with estimated borrowing (including the ceiling amount of net bank credit to Government), will provide resources sufficient to finance Plan expenditures totaling Rs 254.8 billion, virtually the amount provided in the 1983/84 budget. However, these resources include Rs 8 billion of budgetary transfers which are expected to be required to finance priority investments in key sectors additional to those provided for in the budget. Based on current projections, financing for these additional investments will be feasible only if expenditures of a similar magnitude already budgeted do not take place. The authorities have indicated their intention to limit Plan expenditure within the amount of available resources and that, if necessary, steps will be taken to ensure that expenditures are allocated so as to ensure that essential investment needs in key sectors are met.

c. Public sector investment program

Public sector Plan expenditures are budgeted to rise by 21 per cent over the approved Plan outlay for 1982/83 (Table 8). Plan outlays have increased considerably so far during the program, rising from 11.7 per cent of GDP in 1980/81 to an estimated 14.3 per cent in 1983/84. On this basis, total real Plan expenditures in the first four years of the Sixth Plan will amount to some 73 per cent of the original Sixth Plan target for the five years ending in 1984/85. Within the total for 1983/84, increases in investment are planned in key sectors although, with the notable exception of the petroleum sector, the budgeted increases are smaller in percentage terms than for the Plan as a whole. However, as noted above, the authorities have indicated that, beyond the amounts provided in the budget, the Government is considering significant additional expenditures in 1983/84 to step up implementation of priority Plan projects in such key sectors as electric power, irrigation, coal, and the railways.

Expenditures on energy development are budgeted to increase by 24 per cent in 1983/84 with expenditures on petroleum exploration and development increasing by 39 per cent. In line with the accelerated production plan for the petroleum sector, total real expenditures on petroleum will be well above the original Sixth Plan target. Expenditures on power and coal are budgeted to rise by 19 per cent and 8 per cent, respectively, taking total real expenditures in these two sectors

Table 8. India: Sectoral Allocation of Plan Outlays, 1980/81-1983/84

(In billions of rupees)

	1980/81 Actual	1981/82 Actual	1982/83 Approved Plan outlay	1983/84 Budget	Total Real Plan Expenditures 1/ 1980/81 to 1983/84 as a proportion of Sixth Plan Target 2/ (In per cent)
Agriculture and rural development	20.2	22.3	24.0	26.7	76
Irrigation and flood control	17.8	19.5	22.0	25.2	63
Energy	38.3	50.6	68.4 3/	84.5	81
Power	(26.6)	(31.8)	(39.2)	(46.6)	67
Petroleum	(7.4)	(12.1)	(20.2) 3/	(28.1)	139
Coal	(4.3)	(6.6)	(8.8)	(9.5)	91
Industry and minerals	21.9	27.8	30.2	35.0	69
Fertilizer	(2.4)	(3.2)	(4.8)	(5.4)	59
Steel	(7.6)	(7.9)	(8.6)	(8.2)	73
Transport	21.6	25.8	25.3	30.6	75
Railways	(9.7)	(12.1)	(13.3) 3/	(13.4)	86
Other	28.5	35.9	40.8	52.9	70
Total	148.3	181.9	209.9 4/	254.9	73

Source: Data provided by the Indian authorities.

1/ In constant 1980/81 prices, deflated by GDP deflator.
2/ The Sixth Plan target covers the five years 1980/81 to 1984/85.
3/ Revised estimate.
4/ A revised estimate for total Plan outlays of Rs 215.6 billion was made in February 1983. However, subsequent expenditure reduction measures are estimated to have amounted to about Rs 10 billion, of which a large proportion is likely to have been Plan expenditure.

in the four years to 1983/84 to 67 per cent and 91 per cent of the corresponding Sixth Plan targets. Expenditure on irrigation and flood control is to rise by 15 per cent which raises total expenditures in this area to 63 per cent of the Sixth Plan target. In relation to the approved Plan outlay for 1982/83, expenditure on the railways has been increased by 18 per cent, although this represents virtually no increase over the estimated actual level of expenditure of Rs 13.3 billion in 1982/83; however, the authorities are again considering significant additional expenditures in 1983/84.

Considerable progress was made in expanding capacity in most key sectors of the economy in 1982/83. On the basis of the public sector investment program, supported by private investment in some sectors, the authorities envisage that further progress will be made in expanding capacity in these sectors in 1983/84. Details of capacity expansion in 1982/83 and the targets for 1983/84 are provided in Table 9. Chart 4 shows capacity expansion in key sectors during the first four years of the Sixth Plan as a percentage of the original Sixth Plan targets.

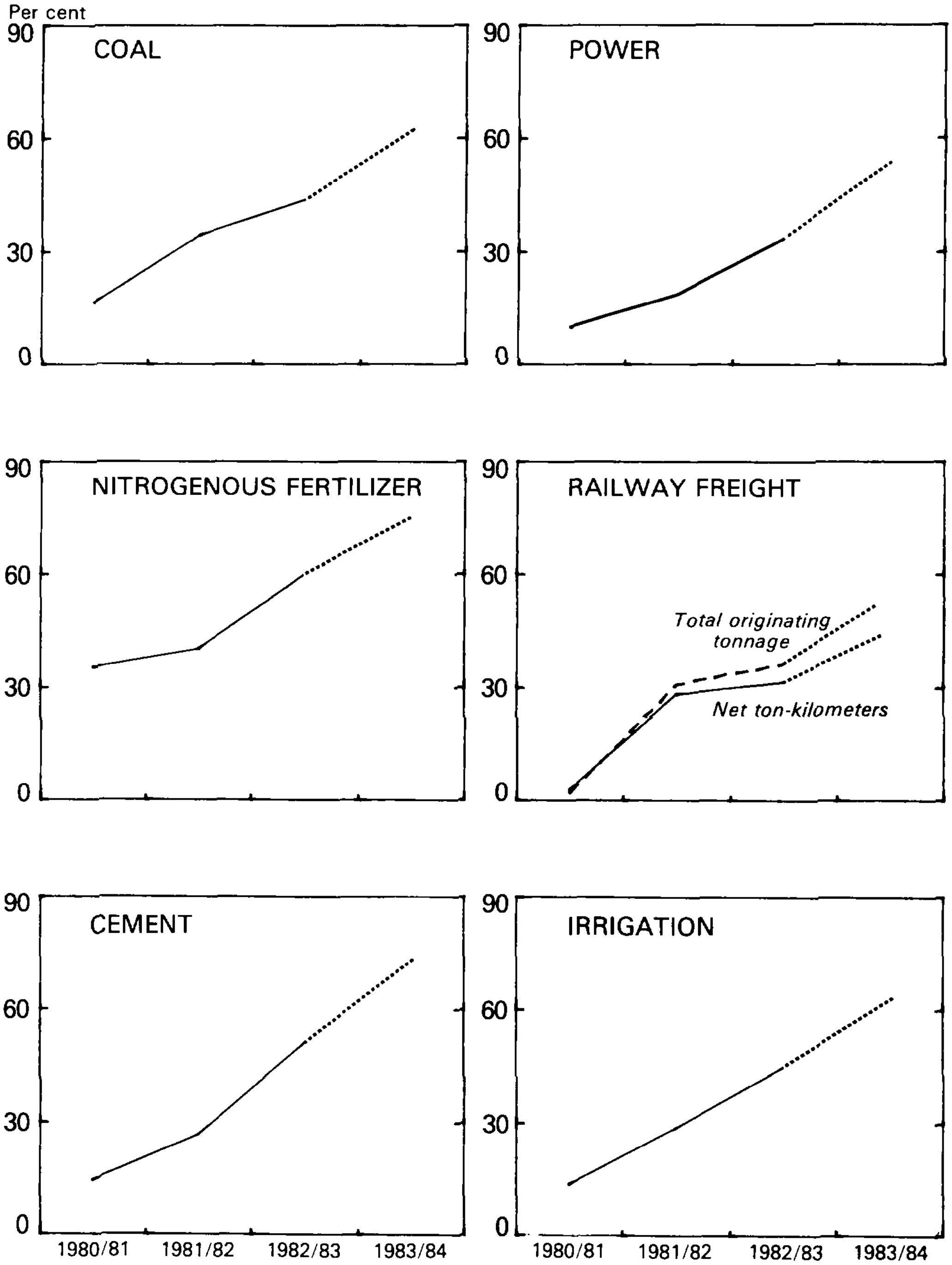
Following two years of strong growth, coal production increased by 5 per cent to 130.7 million tons in 1982/83. The increase fell somewhat short of the target for the year mainly because of power shortages in the Eastern coal fields. Nevertheless, production was more than adequate to meet demand which was lower than expected. An increase in production of 9 per cent to 142 million tons is planned for 1983/84. Electric power generating capacity increased by 3,060 MW in 1982/83. While this was less than the targeted increase of 3,500 MW, it was 41 per cent greater and considerably closer to the program target than in 1981/82. The authorities believe that their efforts to overcome the problems which slowed implementation in the past have been largely successful, especially at the Central level, while similar progress has been achieved in increasing the average plant load factor from existing capacity. For 1983/84, the target for additional generating capacity is 4,100 MW. Reflecting the priority attached to petroleum development, oil production increased by 31 per cent to 21.2 million tons in 1982/83, following a 54 per cent increase in the previous year. Production is targeted to rise to 26.3 million tons in 1983/84, well in excess of the original Sixth Plan target of 21.6 million tons. The degree of self-sufficiency in petroleum is now projected to reach about 75 per cent by 1984/85, substantially higher than originally targeted in the program.

Capacity in the cement industry rose by 16 per cent to 34 million tons in 1982/83, broadly in line with the program. In view of the buoyant investment climate in the industry, an increase to 38 million tons is projected for 1983/84, and it is expected that the original Plan target for capacity in 1984/85 will be reached. Nitrogenous fertilizer capacity increased from 4.7 to 5.1 million tons, somewhat below the target of 5.3 million tons because of delays in one project. For 1983/84 the target has again been set at 5.3 million tons, and the authorities expect that the Plan capacity target for 1984/85 of 5.9 million tons will be met. There was no expansion in capacity in the

CHART 4

INDIA

ACCUMULATED INCREASES IN CAPACITY IN KEY SECTORS AS PERCENTAGES OF SIXTH PLAN TARGET INCREASE



Source: Data provided by the Indian authorities.

Table 9. India: Agriculture and Industry Projections, 1981/82-1983/84

(In millions of metric tons)

	1981/82	1982/83		1983/84		1984/85
	Actual	Program	Estimate	Original program 1/	Revised	Original Sixth Plan target
Industry capacity targets						
Coal (production)	124.9	133.0	130.7	...	142.0	165.0
Electric power (end-year installed capacity, '000 MW)	35.0	38.5 2/	38.1	46.4	42.2	51.2
Nitrogenous fertilizer	4.7	5.3	5.1	5.4	5.3	5.9
Railway freight (bn. ton-kms.)	174	183 2/	176	200	184	220
Steel	11.7	12.4	11.7	14.3	12.8	14.3
Cement	29.3	38.0	34.0	40.0	38.0	43.0
Crude oil (production)	16.2	21.0	21.2	...	26.3	21.6
Agriculture						
Foodgrain production	133.1	141.5	125-128	148.4	142.0	153.6
Area under irrigation (mn. hectares)	56.17	58.70 2/	58.54	62.60	61.07	66.24
Fertilizer consumption	6.1	7.2	6.4	8.5	7.2	9.7

Source: Data provided by the Indian authorities.

1/ The original program projections for industrial capacities in 1983/84 were tentative estimates, and the program envisaged that official targets for 1983/84 would take into account achievements in the first two years of the program.
2/ Revised downward to allow for a revision in the 1981/82 base figure.

steel industry in 1982/83 because of delays in major steel projects. An increase in capacity of 1.1 million tons in 1983/84 is expected by the authorities.

Railway freight movement showed only a modest increase in 1982/83, because of lower than expected demand. Freight movement in 1983/84 is projected to increase by 4.5 per cent in terms of net ton-kilometers, the relatively small projected increase partly reflecting an expected further decline in the average haulage distance. The authorities indicate that additional investment beyond the amount currently envisaged will be required to avoid transportation bottlenecks again emerging as a constraint on growth. The utilized area under irrigation increased by 2.4 million hectares in 1982/83, slightly less than the target. An increase of 2.5 million hectares is projected for 1983/84; despite financial constraints, the authorities believe that by concentrating expenditures on ongoing projects this target is feasible.

4. Structural policies

a. Interest rate policy, private savings, and capital markets

Measures to strengthen private savings and to increase the share of financial savings are an important part of the adjustment program. Efforts to stimulate private savings are being undertaken against the background of the major public sector resource mobilization effort, a setback to growth in 1982/83, and less favorable developments with respect to the terms of trade and workers' remittances than in the past; these factors would all tend to dampen private savings. Nevertheless, private savings have responded favorably to the measures introduced so far, which included increases in interest rates on bank deposits and company debentures, special interest rate incentives for nonresident Indians, tax incentives, and the introduction of attractive new long-term financial assets. 1/

Interest rate policy has continued to be deployed flexibly with a view to increasing efficiency. In October 1982, the maximum deposit interest rate was raised from 10 to 11 per cent when a category of time deposits with maturity of five years or longer with an interest rate of 11 per cent was reintroduced. In March 1983, the interest rate on five-year Post Office deposits was increased from 10.5 to 11.5 per cent, and interest rates on deposits with various provident, gratuity and superannuation funds were increased by 1 percentage point. These steps were taken in view of the evidence that savers respond strongly to interest rate incentives and are not discouraged by long maturity.

1/ For an analysis of private saving behavior, see Annex III of "India--Recent Economic Developments" (SM/83/28, February 7, 1983).

Following the sustained decline in inflation, the ceiling interest rate for general bank lending was reduced from 19.5 to 18.0 per cent in March 1983 and preferential bank lending rates were lowered by 0.5 to 1.0 percentage points. To compensate banks for the loss in interest earnings, the tax on interest income was halved to 3.5 per cent. These adjustments further reduced the average differential between general and preferential lending rates, and the Government intends to keep under review measures to promote efficiency in the allocation of credit. At present levels of inflation, interest rates on most deposits and all lending are positive in real terms. Also, the authorities have been gradually increasing interest rates on government securities to levels closer to market rates. The Government intends to maintain a flexible interest rate policy, keeping in view developments in inflation. The Reserve Bank is currently reviewing the effectiveness of the credit authorization scheme with a view to rationalization and simplification.

The 1983/84 budget contains a number of tax incentives designed to promote private savings. These include an increase in deductions for savings through contributions to life insurance and provident funds; a merging of exemptions from income tax for investment income from a number of financial assets, accompanied by an increase in the overall exemption limit; and an improvement in tax arrangements for nonresident Indians investing in India. To strengthen corporate savings, the general rate of depreciation for plant and machinery was increased from 10 to 15 per cent. Furthermore, subscriptions to the Public Provident Fund were liberalized and an interest premium of 1 per cent was introduced on subscriptions in foreign exchange to six-year National Savings Certificates by nonresidents.

As part of efforts to promote private savings and encourage the corporate sector to cover an increasing share of investment financing from outside the banking system, efforts are being made to strengthen capital markets. As a result, there has been a sharp increase in capital market activity over the last two years. Approvals of new capital issues rose steeply to Rs 5.3 billion in 1981/82 and increased further to Rs 7.9 billion in 1982/83. Recently, the Government has introduced a scheme to develop a secondary market for nonconvertible debentures. With the expected rebound in industrial activity and the continued favorable policy environment, capital market activity is expected to continue to be buoyant in 1983/84.

b. Industrial policy

The Government regulates private industrial investment through a complex regulatory policy. Industrial policy aims to promote investment in priority sectors, the development of small-scale industry, and the regional dispersal of industry, while avoiding the spread of monopolies and the concentration of industry in large-scale firms. The main features of the network of industrial regulations are the requirement to obtain an industrial licence for all investments exceeding a minimum amount; the reservation of a large number of industries for small-scale producers; and extensive scrutiny and control of investment by large and dominant firms, which is also restricted to certain specified areas. The adjustment strategy envisages a gradual reduction in the constraints on private industry emanating from industrial regulations. The programs for 1981/82 and 1982/83 contained a number of steps in this direction which would increase economic efficiency and encourage private industrial activity.

The authorities recognize the need, consistent with national priorities, to harness potential economies of scale effectively in order to raise industrial productivity. Accordingly, the list of industries reserved for the small-scale sector has been adjusted from time to time to exclude more sophisticated industries. Also, in May 1983 a list of eight nationally important industries in which large firms can invest without restrictions arising because of their size under the Monopolies and Restrictive Trade Practices (MRTP) Act was announced. In April 1983, the limit on investment below which an industrial license is not required was raised from Rs 30 million to Rs 50 million. This increase more than compensates for cost escalation since the last adjustment in 1979, and frees a large number of investments from licensing formalities.

Foreign technology collaboration is approved on a case-by-case basis depending on the terms of royalty payments or purchase. Policy has been flexibly implemented over recent years with the aim of updating technology and modernizing industry while, at the same time, promoting indigenous research and development activity. The established policy norm has been to limit royalty payments to 8 per cent of turnover and to a period of five years; however recently royalties in excess of these norms have been approved in a number of cases. Partly as a result of such flexibility, the number of foreign collaboration agreements approved has risen sharply over recent years and in 1982 reached a record 590. The authorities indicate that the flexible and pragmatic policy will continue in the period ahead. Foreign direct investment, while remaining small, rose from Rs 109 million in 1981 to Rs 628 million in 1982. This reflected the relaxation of restrictions on investments by nonresident Indians and the more liberal approval of other direct investment.

c. Public sector pricing

The program envisages that public pricing policies will be applied flexibly to mobilize resources for investment, contain subsidies, and promote efficient resource allocation. A number of public pricing measures have been taken recently with these objectives in view. In February 1983, prices were increased for a broad range of petroleum products by an average of 6 per cent. Coming at a time of falling world prices, this lifted average domestic petroleum prices considerably above import cost. Besides mobilizing substantial resources for investment, this measure will contribute to restraining domestic petroleum consumption and reducing reliance on imported energy. To mobilize resources, the rail freight tariff was adjusted on several occasions during 1982/83 and the 1983/84 railways budget provided for an average increase in passenger and freight tariffs of 9 per cent. Post and telecommunications charges have also been increased in 1983. Following the recently announced 6.3 per cent increase in the procurement price for wheat from the current rabi harvest, the issue prices of wheat to the public and to mills have been raised by 7.5 and 12.4 per cent, respectively, in order to contain the food subsidy.

Although electricity tariffs were raised in several States in 1982/83, average tariffs remain well below long-run marginal costs and a number of State Electricity Boards (SEBs) continue to face losses. Most SEBs have recently agreed to a World Bank program under which they will contribute from internal resource generation 20 per cent of their investment needs, while limiting rural electrification subsidies paid by State Governments. The authorities have indicated that efforts are being made to implement this program effectively, which will require increases in power tariffs in a number of States. Coal prices were raised by 14 per cent in May 1982 with the aim of achieving a 10 per cent return on equity capital employed. However, subsequent cost increases have prevented this objective from being achieved, and a wage settlement is pending. It is estimated that for tradeable qualities of coal, prices are well below opportunity costs as reflected by the appropriate border prices. The Government is currently reviewing coal prices. The authorities reaffirmed that in 1983/84 coal and electricity pricing policies will be implemented in accordance with their policy objective that prices should reflect economic cost and generate internal resources.

Retail fertilizer prices were raised substantially in 1980 and 1981. Since then, international fertilizer prices have declined to a level broadly in line with domestic retail prices. Nevertheless, the fertilizer subsidy has doubled from Rs 3.9 billion in 1981/82 to an estimated Rs 8 billion in 1983/84. The increase in the subsidy mainly reflects increased domestic production, and higher average prices paid to producers (which are based on cost of production including a 12 per cent return on capital) because of increases in feedstock costs and the completion of new plants with high capital costs. The authorities are currently undertaking a detailed investigation of fertilizer pricing in its entirety. Fertilizer pricing policy aims to avoid an undue fiscal burden and to ensure that prices broadly reflect economic cost. At the same time, the authorities emphasize the need for pricing policy to continue to encourage the expanding use of fertilizer and for careful timing of necessary price adjustments.

5. Balance of payments adjustment

a. The 1983/84 balance of payments and medium-term prospects

The authorities and the staff have again reviewed the balance of payments projections for 1983/84 and 1984/85 taking account of the current outlook for the domestic economy, world trade, international prices, and aid. Balance of payments projections for 1985/86, the first post-program year, have also been added. The revised estimates show that, barring unforeseen adverse developments, balance of payments prospects are generally more favorable than projected earlier. This is largely due to an improvement in the terms of trade, and reduced imports of bulk items, including oil. Details of the new projections are provided in Table 10.

Exports (in terms of SDRs) are projected to increase by 7 per cent in 1983/84, compared with the growth of 12 per cent expected earlier. The lower growth is due both to volume and prices. Volume growth in 1983/84 is now projected to be 5 per cent, less than the target of 8 per cent. While India's recent export performance has been less favorable than projected in the program, it has been in line with that of other similar developing countries and world trade (Chart 5). In light of current projections for world trade in 1983, the export volume target for 1983/84 appears feasible, although the authorities emphasize the uncertainty of the world trade outlook and the potentially adverse impact of protectionist measures abroad.

Export performance is expected to improve over the course of 1983/84 in response to the expected gradual recovery of world demand and international trade. A strengthening of demand from industrial countries would benefit a broad range of exports including iron ore, textile products, jute manufactures, leather and leather products, engineering goods, and gems and jewelry. In contrast, exports to Eastern Europe are likely to grow more slowly, partly because of the need to redress the sizable imbalance in bilateral trade. This would tend to depress exports of cashew kernels, spices, tobacco, some textile products, and chemical and pharmaceutical products. Also, economic conditions in some of the oil exporting countries where India has a strong market presence are likely to be less buoyant than earlier expected. On the supply side, the expected recovery in agricultural production should result in increased exportable surpluses of agricultural commodities including, in particular, rice. The resumption of normal activity in the textile sector is expected to remove supply constraints on textile exports. Export unit prices are projected to increase by about 2 per cent in SDR terms 1/ in 1983/84, the same rate of increase as in 1982/83 and considerably less than projected earlier (6.5 per cent).

Total imports in 1983/84 are now projected to be SDR 2 billion lower than estimated in May 1982 and only about SDR 0.5 billion higher than in 1982/83. This reflects both the lower 1982/83 estimate and reduced growth (4 per cent) compared with last year's projection (12 per cent). Oil imports (net of exports) in 1983/84 are projected to be as much as 28 per cent less than projected earlier, on account of both lower volume and prices. The volume of oil imports is expected to be 25 per cent

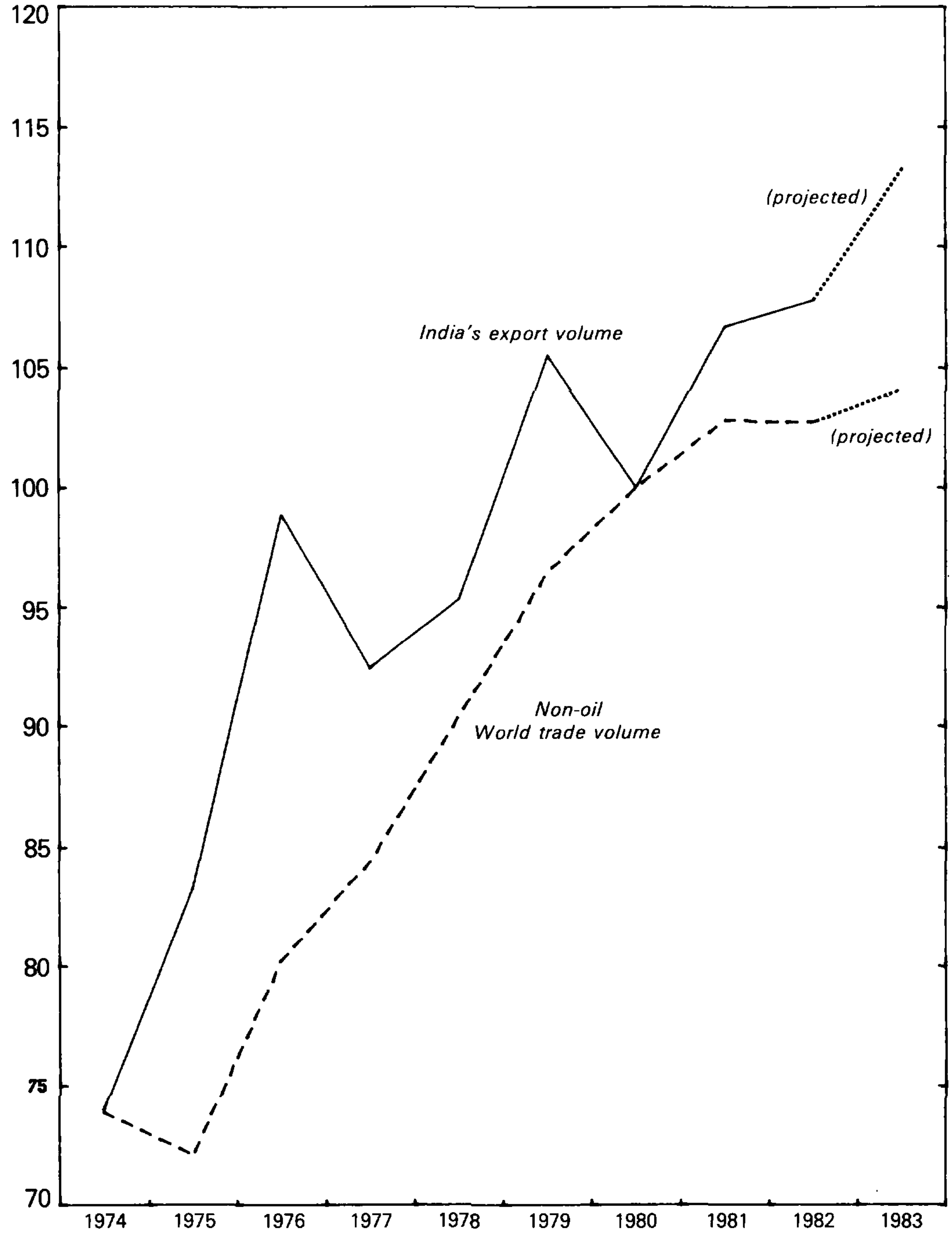
1/ In U.S. dollar terms this would also represent an increase of 2 per cent, compared with a 3 per cent decline in 1982/83.

CHART 5

INDIA

WORLD TRADE GROWTH AND INDIA'S EXPORTS, 1974-83[1]

(1980 = 100)



Source: Staff estimates and projections.

[1]World trade is measured as worldwide non-oil imports. World trade is measured on a calendar year basis while the volume of India's exports is measured on a fiscal year basis(e.g. fiscal year 1974/75 is 1974 in the chart).

Table 10. India: Balance of Payments, 1981/82-1985/86

(In millions of SDRs)

	1981/82	1982/83		1983/84		1984/85		1985/86
	Revised Est.	Program May '82	Revised Apr.'83	Program May '82	Revised Apr.'83	Program May '82	Revised Apr.'83	Estimate Apr.'83
Exports, f.o.b.1/	7,379	8,230	7,619	9,464	8,171	10,981	9,285	10,678
Imports, c.i.f.	-13,049	-13,876	-13,048	-15,512	-13,538	-17,150	-14,485	-15,785
Oil (net)	(-4,844)	(-4,640)	(-4,286)	(-4,873)	(-3,528)	(-5,111)	(-3,630)	(-4,062)
Non-oil	(-8,205)	(-9,236)	(-8,762)	(-10,639)	(-10,010)	(-12,039)	(-10,855)	(-11,723)
Trade balance	-5,670	-5,646	-5,429	-6,048	-5,367	-6,169	-5,200	-5,107
Net invisibles	2,718	2,235	2,381	2,220	1,967	2,438	1,857	1,764
Nonfactor income	(1,087)	(1,097)	(1,090)	(1,244)	(1,133)	(1,488)	(1,270)	(1,413)
Investment income	(160)	(-135)	(-152)	(-412)	(-512)	(-581)	(-705)	(-900)
Private transfers	(1,471)	(1,273)	(1,443)	(1,388)	(1,346)	(1,531)	(1,292)	(1,251)
Current account	-2,951	-3,411	-3,048	-3,828	-3,400	-3,731	-3,343	-3,343
Concessional loans and grants 2/	1,339	1,460	1,462	1,759	1,532	1,954	1,718	1,857
Disbursements	(1,850)	(2,096)	(2,016)	(2,412)	(2,116)	(2,603)	(2,292)	(2,477)
Repayments	(-511)	(-636)	(-554)	(-653)	(-584)	(-649)	(-574)	(-620)
Net commercial borrowing	173	364	272	574	464	861	789	929
Bilateral accounts	-283	--	-383	--	139	--)		
Short-term bridging loan	--	--	367	--	-367)	)	--	--
Other capital (net)	24	-96	95	-115	135)	-143)		
Errors and omissions	-477	--	-45	--	--)	)		
Overall balance	-2,175	-1,683	-1,280	-1,610	-1,497	-1,059	-836	-557
Fund (net)	600	1,800	1,800	1,483	1,233	...	...	...
Purchases	(600)	(1,800)	(1,800)	(1,500)	(1,300)	(...)	(...)	(...)
Repurchases	(--)	(--)	(--)	(-67)	(-67)	(...)	(...)	(...)
Reserves	1,575	-117	-520	127	264	...	...	...
Exchange rate Rs/SDR	10.295	10.450	10.526	10.450	10.791	10.450	10.791	10.791

Source: Data provided by the Indian authorities.
1/ Excludes oil.
2/ Includes IBRD loans.

less than estimated a year ago. This reflects the success of the accelerated oil production program and substantially slower growth in oil consumption than previously envisaged. The projected increase in non-oil imports (14 per cent) is broadly in line with earlier estimates. Continuing the developments in 1982/83, imports of bulk items such as fertilizer, iron and steel, and nonferrous metals are estimated to be lower than previously expected. However, imports of capital goods by the Oil and Natural Gas Commission (ONGC) for oil exploration and production are projected to rise sharply and offset this saving. The import estimates include an allowance of SDR 0.5 billion to cover possible imports of foodgrains. Imports of other than bulk items are projected to rise by more than 20 per cent, in line with earlier projections, with a strong increase in volume reflecting increased industrial activity and more liberal access to imports.

While export prices (in SDR terms) are now expected to increase much less in 1983/84 than projected earlier, import prices are expected to decline slightly in contrast to the marked rise earlier anticipated. As a result, India's terms of trade are now expected to improve by about 3 per cent in 1983/84, whereas a small deterioration was projected earlier (Chart 6). The trade deficit is estimated at SDR 5.4 billion, SDR 0.7 billion less than the May 1982 projection. Invisibles items have been revised to take account of recent developments in nonfactor income, revised estimates of investment income and less favorable prospects for remittances from oil producing countries. Net receipts are now estimated at SDR 2.0 billion compared with SDR 2.2 billion in the projections prepared in May 1982. The current account deficit is estimated to amount to SDR 3.4 billion, SDR 0.4 billion less than projected in May 1982 and SDR 0.9 billion below the original estimate. In terms of GDP, the current account deficit is estimated to be 2.1 per cent, unchanged from 1982/83 but somewhat below the original program target of 2.2 per cent (Chart 7).

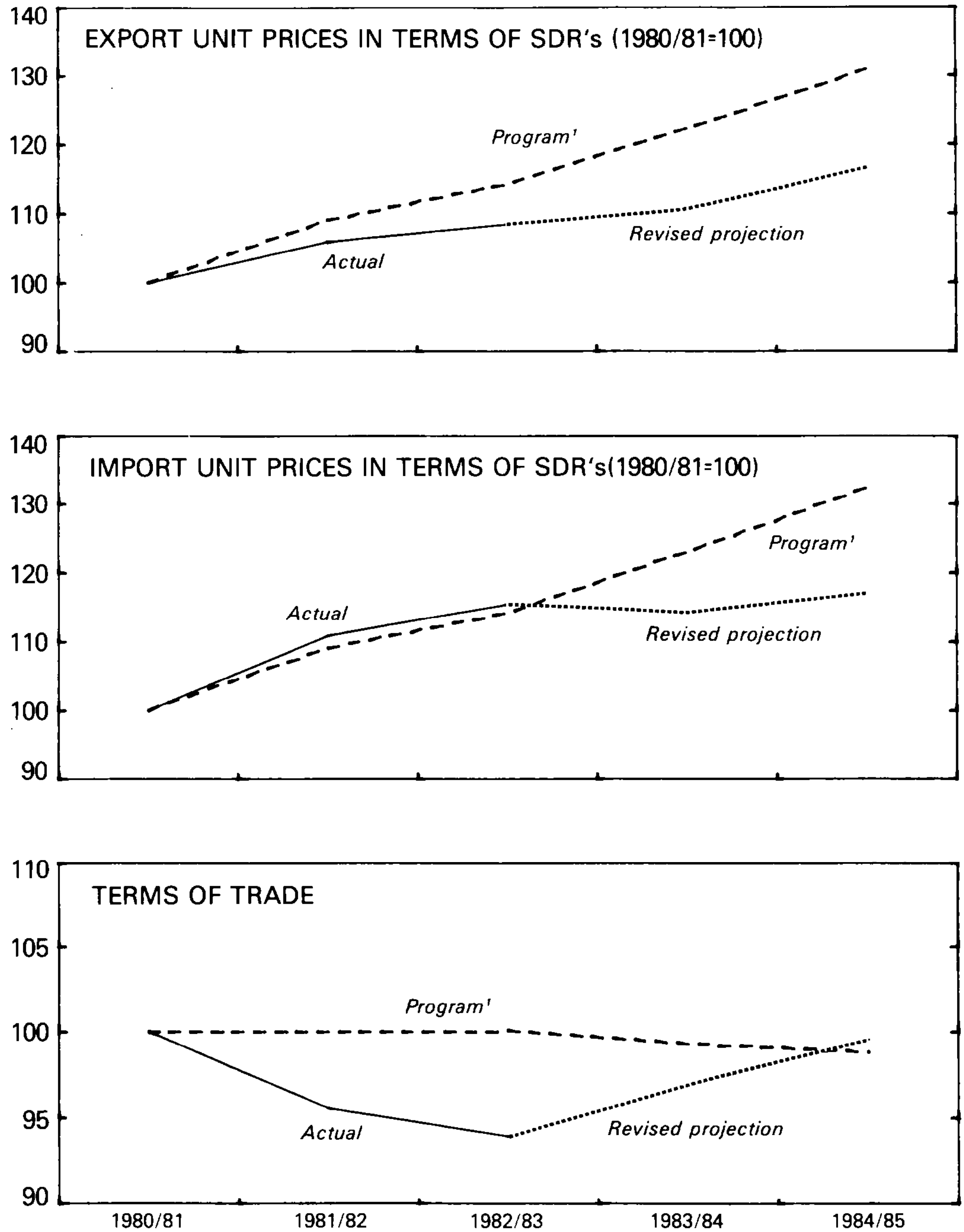
Net receipts of concessional loans and grants are expected to amount to SDR 1.5 billion, some SDR 0.2 billion less than projected a year ago. Net disbursements of commercial loans are estimated to amount to SDR 0.5 billion, somewhat less than projected earlier but 70 per cent more than in 1982/83. Gross disbursements are projected to reach SDR 0.7 billion, up from SDR 0.5 billion in 1982/83. This includes medium-term borrowing by ONGC, part of which will be used to repay short-term bridging finance arranged in 1982/83. India's net creditor position on bilateral account is projected to be reduced by some SDR 140 million in 1983/84.

These estimates imply an overall balance of payments deficit of SDR 1.5 billion, SDR 0.2 billion higher than in 1982/83 but SDR 0.1 billion below the projection made a year ago and substantially less than the original program projection of SDR 2.7 billion.

CHART 6

INDIA

EXPORT AND IMPORT UNIT PRICES AND TERMS OF TRADE, 1980/81-1984/85

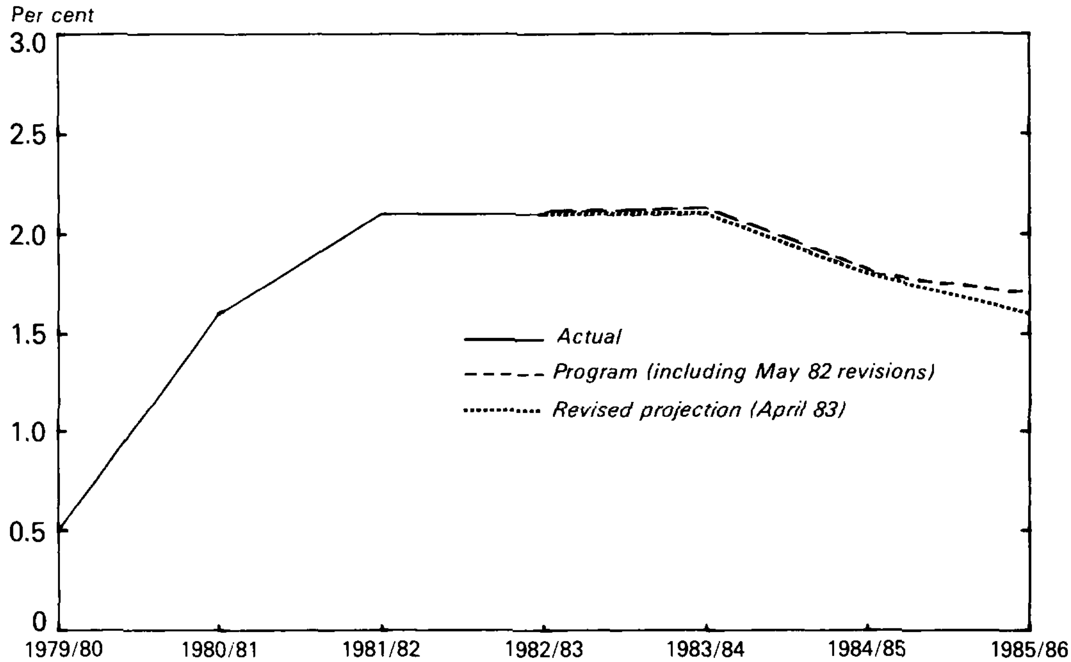


Sources: EBS/81/198, EBS/82/102, data provided by the Indian authorities and staff estimates.
[1] Including May 82 revisions.

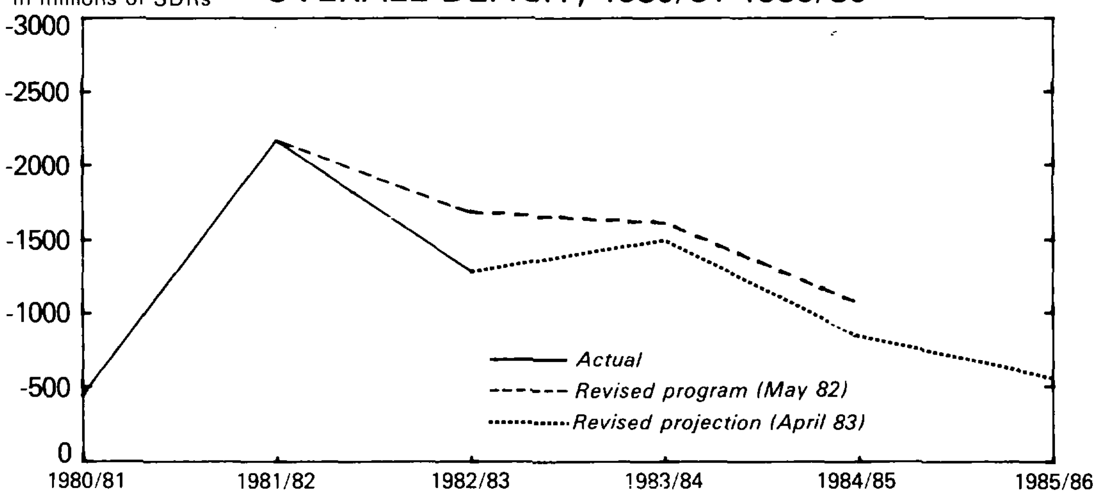
CHART 7

INDIA

CURRENT ACCOUNT DEFICIT/GDP RATIO, 1979/80-1985/86



OVERALL DEFICIT, 1980/81-1985/86



Sources: Data provided by the Indian authorities and staff projections.

Against this background and based on present policies in India and the outlook for the world economy, a continued gradual improvement in the balance of payments situation can be expected over the medium term. Aided by a progressive strengthening of world demand, export volume growth is projected to increase progressively. Export performance would be supported by further improvements in infrastructure and policies to increase efficiency. On the import side, lower prices than expected earlier and continued progress in replacing imports where India is an efficient producer should limit annual import growth to about 8 per cent, even with liberal import policies. In contrast with earlier projections, which indicated a deterioration, India's terms of trade are expected to improve slightly further in 1984/85. However, the outlook for invisibles is less favorable and, net receipts are expected to continue to decline because of higher interest payments and lower remittance receipts.

On this basis, the current account deficit would amount to SDR 3.3 billion in 1984/85, SDR 0.4 billion less than projected in May 1982 and SDR 0.6 billion below the original estimate, and to remain at that level in 1985/86. In terms of GDP, the current account deficit would decline to 1.8 per cent in 1984/85, in line with the original program target, and further to 1.6 per cent in 1985/86. Based on current aid prospects--total new aid commitments declined from SDR 3.0 billion in 1981/82 to about SDR 2.0 billion in 1982/83 because of much lower commitments of IDA funds--net disbursements of aid in 1984/85 and beyond are likely to be lower than expected earlier. In the light of recent commitment levels, net disbursements of commercial loans are projected to reach SDR 0.8 billion in 1984/85 and SDR 0.9 billion in 1985/86. On this basis, the overall deficit is projected to decline to about SDR 0.8 billion in 1984/85, broadly in line with the original projection. The overall deficit is projected to decline further to some SDR 0.6 billion in 1985/86.

b. Export policy

Efforts are being made under the program to improve the structure and performance of the export sector. These include measures to increase the productive efficiency of exporters, improve export incentives, and enhance the competitive position of exporters, as well as effective exchange rate management. A number of measures to strengthen the productive efficiency of exporters have been taken since 1980. While these have already improved export performance, in many cases they have not yet had their full effects on export growth. The main thrust has been to relax industrial regulations applying to exporters and to liberalize import policy to meet the needs of exporters. As a result, exporters benefit from improved access to imports, simpler procedures for importing, and a wider scope of customs duty exemptions on imports. A program providing tax and other concessions to 100 per cent export-oriented units is expected to result in a rapid growth in the number and output of these units; although only 26 units had begun operation by March 1983, 285 units have been approved and the number in operation is expected to expand considerably during 1983/84. Programs have also been initiated for the formation and development of large trading houses, with the aim of developing the considerable export potential of the small-scale sector.

Export-oriented measures included in the 1983/84 Import Policy further enhance exporters' access to imports while, in many respects, increasing incentives for export growth. Exporters of new export products and to new markets will receive increased import replenishment (REP) licenses. The scope for using REP and other licenses also has been increased. Duty-free imports of raw materials will be available to a wider range of exporters, while more duty-free imports of intermediate goods will be permitted. For small-scale producers meeting specified export performance criteria, procedures for access to certain types of import licenses have been simplified and amounts of such licenses increased. The 100 per cent export-oriented units, which already import most requirements under OGL, will now have access to used capital goods under OGL. Although the allocation of additional import licenses to large trading houses has been reduced, the flexibility in using additional licenses has been increased.

In October 1982, a new schedule of Cash Compensation Support (CCS) for exports for the next three years was announced. The CCS scheme, together with duty drawbacks, is designed to compensate exporters for indirect tax payments. The amount and coverage of duty drawbacks and duty exemptions was increased in 1981 and the new schedule of CCS included a range of increases and decreases in rates of support, but the average rate declined slightly. The 1983/84 budget includes several measures designed to encourage exports. The income tax relief scheme initiated in 1982/83 has been extended to allow income tax deductions equal to 1 per cent of export turnover in addition to 5 per cent of incremental export turnover relative to the preceding year.

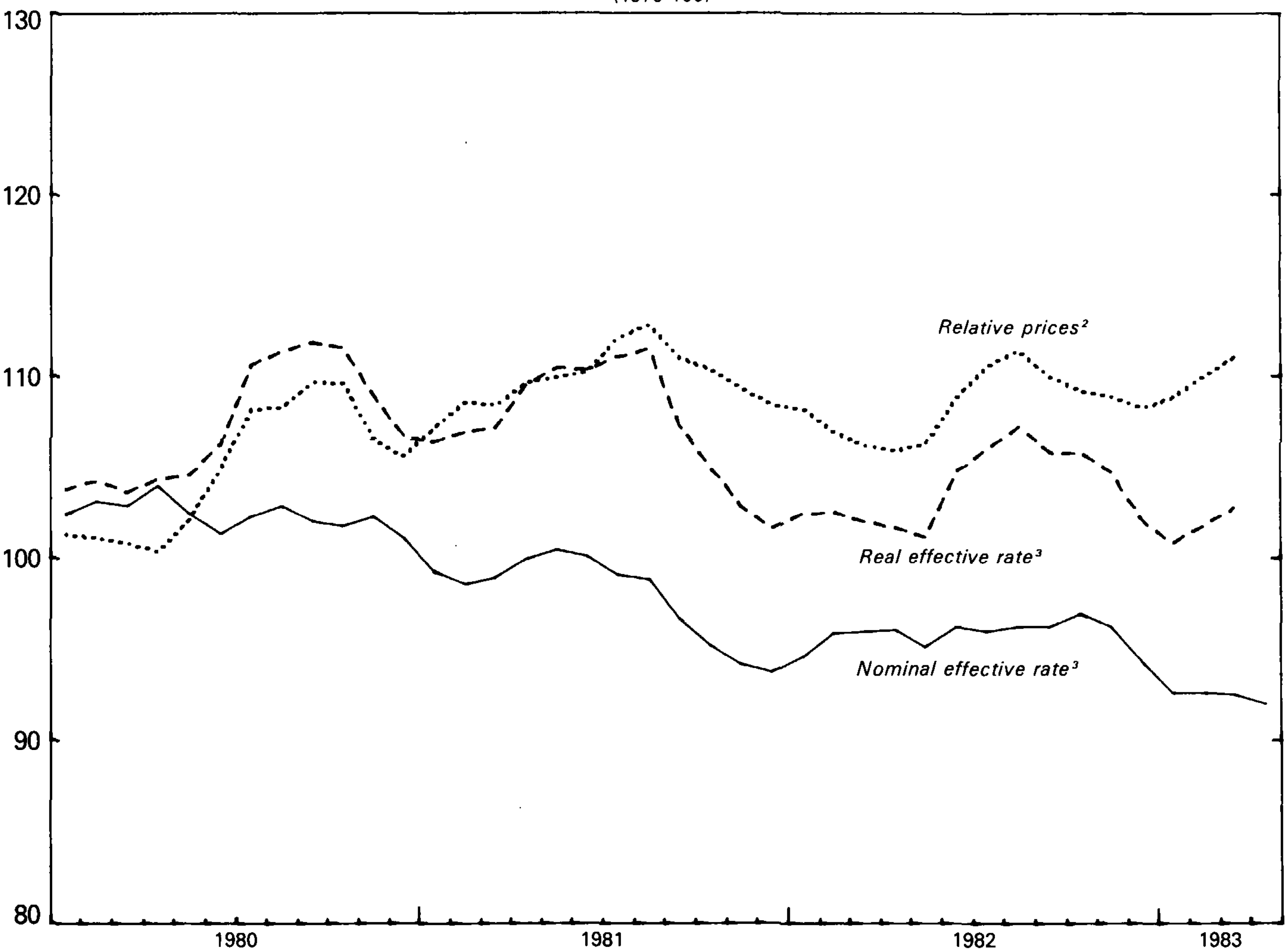
Since September 1975, India has linked the value of the rupee to a basket of currencies of India's trading partners. The margin of variability is 5 per cent on either side of the peg. The pound sterling is the intervention currency. Despite large changes in exchange rates among currencies of India's major trading partners, the nominal effective value of the rupee remained virtually unchanged during the first half of 1982/83 (Chart 8). An increase in prices in India relative to those in trading partners, which mainly reflected seasonal factors, produced a 5 per cent appreciation of the real effective exchange rate between April and August 1982. This appreciation was subsequently reversed as a result of both a gradual reversal of the shift in relative prices and a 4 per cent depreciation in the nominal effective exchange rate in the latter half of 1982/83. The real effective rate appreciated slightly during the first three months of 1983, despite a small depreciation of the nominal effective rate, reflecting an increase in relative prices. The authorities recognize the critical role of exchange rate policy in export development through export profitability and competitiveness.

CHART 8

INDIA

EFFECTIVE EXCHANGE RATES, 1980-1983[1]

(1979=100)



Source: IMF, *International Financial Statistics.*

[1]Export weighted

[2]Upward movement indicates higher inflation in India.

[3]Upward movement indicates appreciation of the rupee.

They indicate that their exchange rate management so far during the program period has been a positive factor affecting export performance and they intend to continue to implement a realistic exchange rate policy during 1983/84.

c. Import liberalization

Import liberalization is a key element of the adjustment effort. The program for 1982/83 contained significant measures in this direction, and these were implemented as envisaged. The program for 1983/84 includes significant additional liberalization measures which, taken overall, will increase access to restricted items substantially, particularly for capital goods and technology which have been widely restricted, and increase the competitiveness of domestic industry. The aim of the measures is to facilitate the modernization of the Indian industry, with emphasis particularly on manufacturers exporting a sizable proportion of their production. Flexibility in the choice of raw materials and components imported by exporters is also increased.

Supplement 1 includes an economically weighted analysis of the effects of the new measures on the access to imports in 1983/84 and the extent of protection of domestic industry. In brief, overall access to imports is raised by 12.5 per cent as a result of the new measures. Taking account also of the built-in mechanisms for growth in the licensing system, access to imports is estimated to rise by as much as 30 per cent in 1983/84, following an estimated 21 per cent increase last year. Substantial increases in access to imports in the least restrictive licensing category (automatic permissible items which account for about 20 per cent of imports covered by the policy) have now reached such a magnitude that licensing generally no longer imposes an effective restriction. However, licensing continues to impose an effective constraint on imports under more restricted import categories, principally as a means of providing protection to domestic producers.

For the four fifths of domestic industry which enjoys protection through the restrictive system, measures to increase access to imports of restricted items will reduce the level of protection in 1983/84. However, for the remaining one fifth of domestic industry, the level of protection has risen as a result of the increases in the auxiliary import duties introduced in the 1983/84 budget for revenue reasons. Taken overall, it appears that the net impact of these recent changes would be to reduce the level of protection afforded to domestic industry.

A number of measures have been introduced which tend to increase import restrictions and reduce competitive pressures. However, the aggregate impact of these changes does not appear to be large. International prices of several important imported items fell sharply in 1982/83 as a result of the recession in the world economy. Customs duties were raised by 10-20 per cent for some of these products in the 1983/84 budget, but despite calls for the imposition of direct controls, imports continued to be allowed under OGL. The steel industry was also affected adversely by increased imports. In response, the Government has decided to restrict imports of three important steel products, on the condition that the domestic producers supply the goods at international prices within a period specified by the customers. Although the 1983/84 import policy also includes several voluntary provisions which tend to encourage industry to procure from domestic sources rather than from imports, financial incentives given for domestic procurement generally appear to be smaller than necessary to divert procurement from imports.

There have been other liberalization policies which are of potential importance, but whose significance is not fully captured by their quantitative impact in 1983/84. First, manufacturers are allowed to undertake import-intensive production with low value-added, subject to a commitment to reduce the import component gradually under a Phased Manufacturing Program. This program is being widely and effectively implemented and is facilitating the modernization of the consumption goods industry where imports have generally been prohibited. In addition, the scope for direct imports of manufactured consumption goods has increased as a result of the substantial relaxation of baggage allowances included in the 1983/84 budget. Second, access to imports of capital goods, which has been widely restricted, has now been eased by measures which substantially widen access to capital goods imports for units exporting at least 25 per cent of production. Also units in Free Trade Zones (which have free access to capital goods imports) will be allowed to sell in the domestic market up to 25 per cent of their production against import licenses.

6. External borrowing and debt service

India's external capital needs have been met mainly through bilateral and multilateral concessional financing but, beginning in 1980/81, increasing recourse has been had to international capital markets for project financing. Total commitments of commercial loans rose from SDR 0.9 billion in 1981/82 to SDR 2.1 billion in 1982/83; the latter amount includes SDR 0.5 billion for a single power project. In 1983/84 total new commitments of loans on commercial terms are projected to amount to about SDR 1.7 billion. This amount includes official and officially guaranteed loans for projects in the petroleum, power, engineering, steel and mining sectors, loans to financial institutions for onlending to the private sector, and suppliers' credits contracted by the private sector. During 1983/84, the Government intends to limit the official contracting and guaranteeing of nonconcessional loans with a maturity of between 1 and 12 years to no more than SDR 1.5 billion; within this ceiling, loans in the 1 to 5-year maturity range will be limited to SDR 200 million. External borrowing by the private sector continues to be permitted, subject to government approval, on the basis of the creditworthiness of the companies and the viability of their projects. Short-term debt is small and short-term borrowing is generally avoided. The Government's policy is to prevent an excessive debt servicing burden while utilizing more fully its access to international capital markets.

India's outstanding external debt, of which less than 1 per cent is owed by the private sector, amounted to about SDR 21.5 billion at the end of 1982/83 (Table 11). The bulk of external debt (about 80 per cent) relates to loans provided through the India Aid Consortium. Outstanding loans on commercial terms amounted to about SDR 1.1 billion, up from SDR 0.8 billion at the end of 1981/82. Commercial borrowing is projected to continue to increase in coming years and, as a result, India's external debt profile is expected to change in the course of the 1980s with the share of commercial debt rising (Chart 9). Total external debt service is estimated to be SDR 1.2 billion in 1982/83, equivalent to 10.5 per cent of current receipts. Debt service projections have been revised taking account of new current account projections and the less favorable outlook for aid, especially disbursements from IDA. Debt service is projected to rise to SDR 2.3 billion in 1985/86, about the same level as projected in May 1982, but the ratio of debt service to current receipts is expected to increase to 15.2 per cent, about 2 percentage points higher than projected earlier, mainly because of the impact of reduced inflation on current receipts. Debt service is now forecast to be somewhat higher in the second half of the 1980s than projected a year ago, reflecting harder terms of borrowing because of less favorable aid prospects. As a result of this factor, and with export prices increasing more slowly than previously projected, the debt service ratio is now expected to rise more steeply in the second half of the 1980s than earlier expected, reaching a peak of 22 per cent of current receipts in 1987/88. However, parallel with earlier projections, the debt service ratio is expected to decline toward the end of the decade and interest payments are projected to remain well below 1 per cent of GDP throughout the period.

IV. World Bank Staff Views Related to the Program

The World Bank staff has continued to collaborate closely in the staff's work on the extended arrangement. The Bank staff again participated in the discussions with the authorities and their views have been taken into account in the formulation of the program for 1983/84 as presented by the authorities. As in the past, the Bank staff has provided an assessment of policies and developments in areas of Bank concern.

The Bank staff believes that the crude oil production program continues to be the most crucial and, at the same time, the best implemented component of the investment program. Appropriate pricing policies and supporting foreign commercial borrowing have ensured the resources needed to finance the accelerated oil production program. Rapid increases in

Table 11. India: External Debt and Debt Service, 1981/82-1985/86

(In millions of SDRs)

	1981/82	1982/83	1983/84	1984/85	1985/86
Outstanding external debt (public and private)					
Concessional loans 1/	15,465	17,070	18,040	19,346	20,777
Medium- and long-term commercial loans	820	1,121	1,574	2,363	3,293
IMF 2/	866	2,666	4,149	5,066	4,868
Short-term debt	325	692 3/	350	...	...
Total	17,476	21,549	24,113	26,775	28,938
Debt service					
Concessional loans	814	911	973	993	1,089
Interest payments	(304)	(358)	(389)	(418)	(469)
Amortization	(510)	(553)	(584)	(575)	(620)
Medium- and long-term commercial loans	102	216	356	412	567
Interest payments	(30)	(121)	(195)	(248)	(288)
Amortization	(72)	(95)	(161)	(164)	(279)
IMF 4/	19	98	358	555	639
Interest payments	(19)	(98)	(291)	(422)	(441)
Amortization	(--)	(--)	(67)	(133)	(198)
Total	935	1,225	1,687	1,960	2,295
Interest payments	(353)	(577)	(875)	(1,088)	(1,198)
Amortization	(582)	(648)	(812)	(872)	(1,097)
			(In per cent)		
Debt and debt service ratios					
Debt service/current receipts					
Including IMF	8.2	10.5	13.8	14.4	15.2
Excluding IMF	8.2	9.7	10.9	10.3	11.0
Commercial debt service/current receipts	0.9	1.9	2.9	3.0	3.8
Total debt/GDP	11.6	14.0	14.4	14.5	14.0
Interest payments/GDP	0.2	0.4	0.5	0.6	0.6
Assumptions					
GDP (in billions of SDRs)	143.1	147.8	165.0	185.4	206.4
Current receipts (in millions of SDRs)	11,349	11,652	12,244	13,594	15,094
Current account deficit/GDP	2.1	2.1	2.1	1.8	1.6
Export volume growth	7	1	5	8	9
Import volume growth	-1	-3	4	5	4
Increase in export unit prices (in terms of SDRs)	5.9	2.3	2.2	5.2	5.5
Increase in import unit prices (in terms of SDRs)	10.8	4.1	-1.0	2.5	5.5
Interest rate on new concessional loans	3.4	5.0	5.0	5.0	5.0
Interest on new commercial loans	15.8	11.9	10.0	10.0	10.0

Sources: Data provided by the Indian authorities; World Bank Debt Reporting System; and staff estimates.

1/ Includes Trust Fund.

2/ Excludes Trust Fund.

3/ Includes short-term bridging loan of $400 million to be repaid in 1983/84.

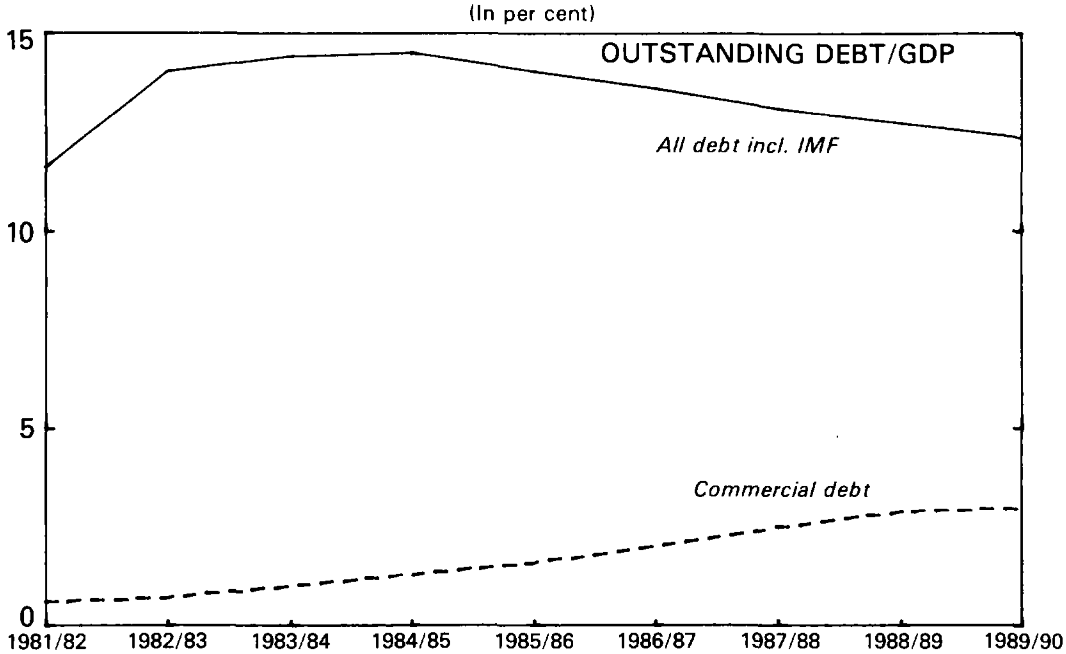
4/ Based on present charges.

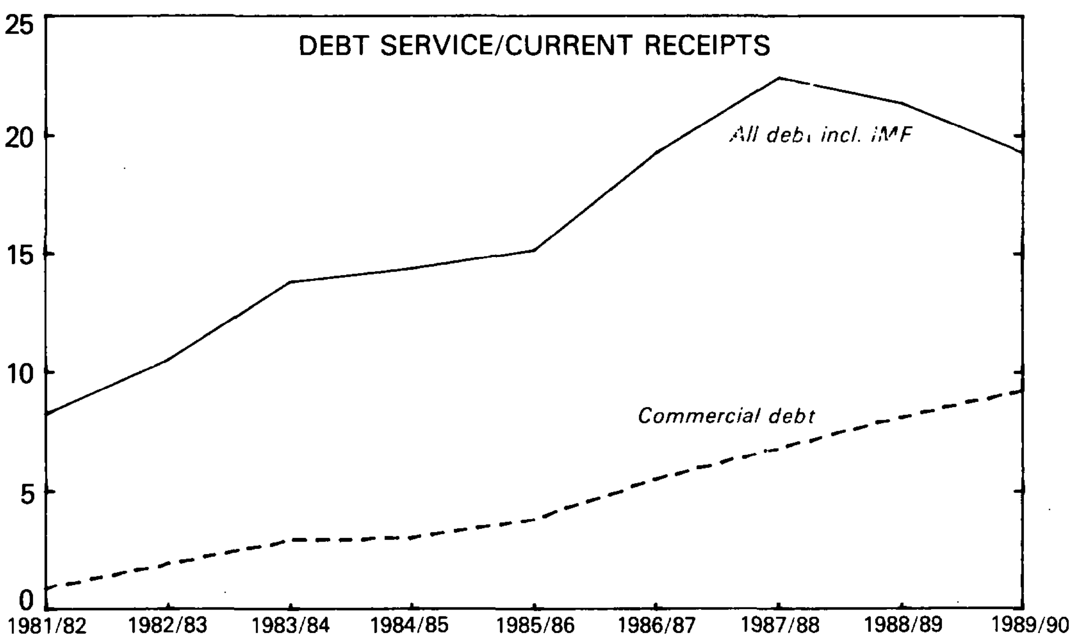
CHART 9

INDIA

EXTERNAL DEBT PROFILE, 1981/82-1989/90[1]

(In per cent)





Sources: Data provided by the Indian authorities, World Bank debt reporting system and staff projections.

[1] Includes estimated future borrowing.

production yielded a reduction in the oil import bill in 1982/83 and contributed substantially to improving the external position. The sizable increase in Plan outlays projected for 1983/84 appears consistent with the investment needs and priority of this sector.

In recent years, investment in the coal industry has increased substantially. This has been reflected in an improvement in labor productivity and rapid growth in production. The proposed increase in Plan outlays of 8 per cent for 1983/84, however, marks a distinct slowdown in the growth of investment. The Government is giving careful consideration to the adequacy of this level of investment. The Bank staff believes this is important in view of the need to maintain the momentum of the investment program if future production targets are to be met. Improvements in operating efficiency and coal pricing policy have resulted in a strengthened financial performance of the coal industry. Nevertheless, increases in costs reduced profits below their expected level in 1982/83 and a new wage contract is likely to be concluded shortly which would increase operating costs significantly. Domestic prices for tradeable qualities of coal are also still well below border prices. In view of these factors, particular importance attaches to a detailed study of coal pricing which is expected to be completed soon.

The Bank staff believes that the planned increase of in electric power generating capacity in 1983/84 is realistic, even though it is sharply higher than the achievement in 1982/83. Even if the target is met, installed capacity at the end of the Plan will inevitably be substantially less than originally projected. However, the possible adverse impact on the economy would be mitigated by lower than expected demand and higher capacity utilization. While technical and organizational problems explain part of the shortfall in capacity additions during the Plan to date, outlays have also been much less than original Plan projections. The Bank staff is concerned that, while the 19 per cent increase in Plan outlays for power in 1983/84 may be adequate to meet the current year's capacity target, it could result in a reduction in the project pipeline and create problems in future years. Investment in transmission lines, which is already behind schedule, may suffer further. At the State level where resource constraints have been most pressing, States have agreed, in the context of the World Bank-assisted Third Rural Electrification Project, to several measures to improve their financial position and increase the resources available for investment. The Government has also turned to external commercial borrowing to finance several new Central sector superthermal plants; agreement was reached on one such project in 1982/83 and others are under consideration.

Virtually no increase in expenditure on the railways is budgeted in 1983/84 over the actual level of expenditure in 1982/83. While railway efficiency has increased markedly in recent years, the scope for further increases without sizable complementary investments appears to be limited.

The Bank staff believes that a substantial supplemental appropriation will be necessary if the railways are to meet the transportation needs of a more rapidly growing economy.

The slippage in capacity creation in steel does not appear critical. In the view of the Bank staff, projected capacity levels appear satisfactory to meet the expected increase in demand for steel from the depressed 1982/83 level. The fertilizer investment program is progressing well in terms of capacity expansion and production. However, the Bank staff is concerned about the rise in the fertilizer subsidy and welcomes the detailed study of all aspects of fertilizer pricing initiated by the Government. The partial decontrol of cement prices seems to have had the desired effect of encouraging a more rapid expansion of capacity and higher levels of production.

Despite its priority, the investment program in irrigation appears to be falling short of its targets. This applies particularly to major and medium projects which absorbs the bulk of public investment in irrigation. With Plan expenditure projected to rise by only 15 per cent in 1983/84, the Bank staff expects that about one half of the Sixth Plan target for the increase in area under major and medium projects will remain uncompleted by the end of 1983/84.

The Bank staff also has made some more general comments on the investment program. Overall, substantial progress has been made and continues to be made in expanding productive capacity in key sectors, and real investment levels in these sectors are significantly higher than in past Plans. At the same time, gaps have emerged in some sectors between actual and projected real expenditure levels and these gaps are reflected in shortfalls of physical achievements from Plan targets. This is of most concern in the cases of power and irrigation. A shortfall in investment in irrigation would be reflected in slower growth of agricultural production over the medium term and increased vulnerability to weather. With continued large shortfalls in power generation capacity, critical power shortages could arise which would seriously impede progress toward sustained higher growth and adjustment. While outlays in the first four Plan years in two other sectors--coal and railways--were broadly in line with original Plan allocations, allocations for 1983/84 appear low in relation to need.

To assess the impact of expected shortfalls in Plan resources and implementation of the investment program, the Government is undertaking a mid-term review of the Plan. However, there has been a delay in completing this review and the Government has now only limited time in which to make appropriate adjustments. Without prejudging the outcome of the review, the Bank staff believes that a two-pronged approach could help minimize the effect of Plan shortfalls. First, continuing resource mobilization efforts would appear essential, especially at the State level where the resource shortfall is largest. Second, there appears to be scope to strengthen the pattern of resource allocation so as to more effectively protect investment levels in the most important areas. The Bank staff also attaches particular importance to the indication included in the program that the Government is considering allocating significant additional funds during 1983/84 for key sectors, particularly irrigation, power, coal, and railways.

V. Staff Appraisal

Following the favorable results of 1981/82, India's economy experienced more difficult circumstances in 1982/83. Severe drought cut agricultural incomes, while industrial growth was reduced. Real economic expansion in 1982/83 is unlikely to have been more than 2 per cent, with incomes unchanged in per capita terms. However, the authorities were able to contain the adverse impact of a lower growth rate and to avoid major adverse effects in other economic areas. In particular, demand management was disciplined and inflationary pressures were contained. Although export growth lagged, the overall balance of payments deficit was considerably less than expected under the program.

The program for 1983/84 presented by the authorities is designed to continue and strengthen the broad thrust of balance of payments adjustment policies followed over the past two years, while supporting the economy's transition to more normal and satisfactory growth. The annual program has been framed in light of the potential for above average real growth which can be reasonably expected given normal weather conditions and some improvement in the world economy. Against this, demand management policies are to remain cautious in view of the lingering threat to price stability emanating from last year's drought. Budgetary recourse to the banking system will be limited and public savings will be increased to support a further sizable growth in public investment. The program includes a range of measures in the fields of industrial regulations and pricing, and a further liberalization of import restrictions, both aimed at improving economic efficiency and international competitiveness.

Assuming that weather is normal, agricultural production should rebound strongly from the setback suffered last year, especially in view of the continuing efforts being made to promote modern agricultural methods and to exploit more fully the potential for growth in this vital sector. Industry is likely to emerge from the sluggish conditions which ruled during much of 1982/83. The recovery would gain much of its impetus from improved international trading conditions and a return to normal in the strike-affected textile sector, while the expected agricultural recovery would strengthen industrial demand as the year progresses. At the same time, pressures for price increases could well become a factor in the period ahead as a result of the lagged impact of last year's supply shortfall and increases in administered prices and indirect taxes. Demand management policies must be alive to this possibility, and for this reason there is little room for expansionary financial policies. In this context, the proposed stance of budgetary and monetary policies is appropriate. The projected increases for money and credit in the financial program for 1983/84 are less than those allowed for in the program for last year and, while they should be adequate to accommodate industrial recovery, they appear unlikely to aggravate inflationary pressures. The share of total credit absorbed by budgetary financing, after providing realistically for contingencies, is contained to the same level as last year; this should provide adequate room to finance commercial sector expansion. The recent steps taken by the Reserve Bank to reinforce the cautious stance of commercial credit policies are appropriate and should allow for smoother implementation of credit policy over the course of the year. Additional steps have been taken to contribute to improving the efficiency of the credit system.

Following the measures adopted in the first two years, the program for 1983/84 continues the emphasis on policies to encourage savings in both the public and private sectors. The reduction in the tax on bank interest earnings is welcome because it has allowed the authorities to increase some interest rates on deposits while reducing general lending rates. Together with other initiatives, including tax incentives, the continuation of an appropriate interest rate policy will encourage an increase in the already high private savings rate. The program provides for a significant increase in public savings, following upon sizable increases in the first two years. At the Central level, the projected increase in savings is expected to derive almost entirely from higher surpluses of public enterprises resulting from the flexible implementation of pricing policies. In contrast, budgetary savings are expected to increase only slightly and remain below the 1981/82 level. The weak performance in budgetary savings reflects, among other factors, a sharp increase in the subsidy bill over the last two years. While subsidies are not so large as to have an important adverse impact on the overall economic situation, the authorities would be well advised to ensure that the subsidy bill is at least contained. Progress was achieved in the past year in enforcing greater discipline in State finances and mobilizing State resources, but State finances remain a problem area. In the aggregate, State public enterprises contribute little to investment resources, in part because of widespread losses by some State Electricity Boards. Despite the Government's program which should, in time, reduce these losses, progress is likely to be slow in improving the resource position of the States and perseverance will be required.

The World Bank staff have collaborated with the Fund staff in presenting an assessment of policies related to the investment program. Although implementation of the public investment program has been satisfactory in several key sectors, the difficulties experienced in others have become more pronounced. Investment programs in sectors where the

States have a major responsibility are suffering from an inadequacy of resources because of the continuing weakness of State finances. In particular, funding of investment in irrigation and electric power has fallen considerably short of the path originally envisaged. While the impact of the resource shortfall has been partly masked by investments in privately financed irrigation and greater efficiency in the electricity sector, the threat posed over the longer term were this situation to persist, can hardly be overemphasized. The Bank staff is also concerned that in 1983/84 investment shortfalls have spread to include other key sectors not directly affected by State resource constraints. In particular, investment allocations for the coal and railways sectors in the 1983/84 budget appear inadequate to meet minimum investment needs. It is to be hoped that during the course of the year the authorities will be successful in providing additional resources in these sectors so that the pattern of investment allocations will more accurately reflect the priorities for external adjustment. Needless to say, the authorities' efforts to ensure that investment needs in critical sectors are adequate would be greatly facilitated by the additional resource mobilization associated in particular with realistic and flexible public pricing policies.

Recent pricing adjustments in several important areas, most notably for petroleum, will both promote resource mobilization and greater efficiency in resource allocation. The authorities are currently reviewing pricing policies for coal and fertilizer. The staff believes that appropriate adjustments in coal prices should not be long delayed. While recognizing the importance of timing in the case of fertilizer, the study being undertaken by the authorities should be completed as quickly as possible and be followed by an appropriate policy response. Several useful steps have also been taken to reduce restrictive regulations on private industry, although perseverance is called for to promote efficiency and ensure that the full benefit is gained from the more open trading policies.

New import liberalization measures constitute an important element of the program for 1983/84. Measures recently introduced should considerably increase access to imports. As a result of successive large increases in access, the licensing system appears to no longer be an effective constraint on imports falling within the least restrictive licensing category. The increased availability of imports of restricted items would increase competitive forces on domestic industry enjoying protection through the system of licensing, although higher auxiliary import duties introduced for revenue reasons, would increase protection through the tariff. Also, small, but potentially important, facilities have widened access to imports of finished consumer goods which are largely prohibited. While pressures for protection were accommodated in some cases, the authorities were able to maintain exposure to competition in most areas. The staff believes that, while the liberalization measures are not as wide-reaching as those introduced last year, nevertheless they are significant overall and are consistent with the authorities' intention as indicated in the original program statement. The significance of the measures is enhanced when viewed against the difficult international and domestic circumstances in which they have been taken. While there remains much more to be done to develop a truly open trading environment, the authorities' consistency and determination provides an important signal of continuity in these efforts.

The world trade recession had a major, if somewhat delayed, impact on the demand for India's exports in 1982/83, while export supplies of some agricultural items were reduced by the drought. Despite the shortfall in export volume growth, the overall balance of payments position improved. The import bill was unchanged, despite unexpected food imports, thanks to reductions in imports of bulk items made possible by higher domestic production. Also, commercial capital inflows increased as the external borrowing program gained momentum. These two developments are likely to continue in the period ahead. An improvement in export growth as projected appears feasible if the world economy recovers as expected. It is essential that the policy basis be established to support achievement of the 1983/84 export volume target and considerably higher growth by 1984/85. Exchange rate policy should be flexibly applied so as to fully capture the potential benefit from a resumption in growth in world trade. The authorities should be alert to quickly take additional measures if the expected pickup in exports is delayed. In 1983/84, which was originally projected to be the year of greatest balance of payments difficulty, the external position is now projected to stabilize, and looking further ahead, a persistent strengthening of the balance of payments is projected over the subsequent few years.

The authorities' borrowing program will facilitate a gradual increase in loan disbursements to support the balance of payments in the period after the end of the extended arrangement. Current projections indicate that the debt service ratio will rise further and more sharply than earlier expected, because of a lower path of exchange earnings and the reduced prospects for concessional assistance. Nevertheless, the debt servicing burden is expected to remain manageable during the remainder of the decade.

India came early to the Fund; the fundamental objective of the program supported by the EFF was not to achieve an immediate reduction in external deficits but rather to carry out a comprehensive policy effort to strengthen the balance of payments position over the medium term. Several policy changes are contributing to the achievement of significant underlying progress on external account: the growth of public savings is financing higher levels of investment in areas essential for balance of payments adjustment, without leading to larger current account deficits; more realistic pricing (with some exceptions) of key products is contributing to an improved allocation of scarce resources and lower imports; the liberalizing of access to imports is leading to some strengthening of competitive forces; India's export effort has been enhanced although continued emphasis needs to be given to this key policy area. The program presented by the authorities for 1983/84 includes policies and measures which will support the momentum of the medium-term balance of payments adjustment process. Accordingly, the staff believes that the proposed program continues to merit the Fund's strong support.

VI. Proposed Decision

The following draft decision is proposed for adoption by the Executive Board:

1. India has consulted with the Fund in accordance with paragraph 4(d) of the extended arrangement for India (EBS/81/198, Supplement 3, November 13, 1981), as amended (EBS/81/198, Supplement 4, February 24, 1982 and EBS/82/102, June 11, 1982), in order to reach understandings with the Fund regarding policies and measures that India will pursue through March 31, 1984.

2. The letter dated June 8, 1983 from the Minister of Finance of India, together with the annexed Statement of Policies shall be attached to the extended arrangement for India, as amended, and the letters dated September 28, 1981 and June 8, 1982, together with the annexed Statements of Policies, shall be read as supplemented by the letter dated June 8, 1983.

3. Accordingly, India will not make purchases under the extended arrangement from July ..., 1983:

(a) during any period in which the data at the end of the preceding period indicate that:

(i) the ceiling on total domestic credit as specified in paragraph 5 of the Statement of Policies annexed to the letter dated June 8, 1983; or

(ii) the ceiling on the net credit to the Government as specified in paragraph 5 of the Statement of Policies and annexed to the letter dated June 8, 1983 is not observed; or

(b) if India fails to observe the limits on official contracting and guaranteeing of nonconcessional loans as specified in paragraph 16 of the Statement of Policies annexed to the letter dated June 8, 1983; or

(c) during any period after January 29, 1984, until the review with the Fund contemplated in paragraph 3 of the letter dated June 8, 1983 has been completed, or if following that review, any performance criteria established by the Fund pursuant to the review are not observed.

4. Paragraph 4(d) of the extended arrangement for India shall be amended to read as follows:

"(d) for the period from April 1, 1984 to the end of the extended arrangement, if before June 30, 1984, suitable performance clauses for this period have not been established in consultation with the Fund or if such clauses, having been established, are not observed; or ....."

5. Purchases under the extended arrangement for India shall not, without the consent of the Fund, exceed the equivalent of SDR 3,900 million until June 30, 1984, provided that

purchases shall not exceed the equivalent of SDR 3,100 million until October 30, 1983; the equivalent of SDR 3,300 million until January 30, 1984; and the equivalent of SDR 3,700 million until April 30, 1984.

ATTACHMENT

Minister of Finance
India
New Delhi - 110001

June 8, 1983

Dear Mr. de Larosière,

India's economy which had made significant progress in 1980/81 and 1981/82, suffered a setback in 1982/83 because of a severe drought. Real economic growth was reduced to about 2 per cent with a reduction in incomes in the agricultural sector and a slowdown in industrial growth. As a result of the reduction in incomes and additional expenditure related to drought relief, the budgetary position came under strain. However, steps were taken during the year to contain the budgetary deficit, including sizeable resource measures, and a cautious credit policy was continued. As a result of demand management policies and steps to ensure adequate supplies of essential commodities, inflationary pressures were contained; wholesale prices rose 6.5 per cent over the course of the year. Also, balance of payments pressures were reduced, largely because of increased domestic production of such important items as oil and fertilizer. The current account deficit was reduced to 2.1 per cent of GDP and the overall deficit was also reduced. As a result of our policies, we expect the current account deficit in the balance of payments to remain at 2.1 per cent of GDP in 1983/84 while the overall deficit would be SDR 1.5 billion. This would represent progress, as envisaged in the program, toward overcoming the balance of payments problem, and the Government of India remains fully committed to this objective.

2. Details of the policies to be followed by the Government of India in 1983/84 in implementing the medium-term balance of payments adjustment programme supported by the extended arrangement with the Fund are contained in the attached memorandum.

3. With respect to the programme for 1983/84, the Government will consult with the Fund on the adoption of any appropriate measures, consistent with the national policies accepted by our Parliament, in accordance with the Fund's policies on such consultations. The Government will review with the Fund before January 30, 1984, the progress made in implementing the programme and in particular the policies and measures relating to public finance, imports and exports in view of

paragraphs 4, 14 and 15 of the attached memorandum, and reach such understandings with the Fund as are necessary for the purposes of achieving the objectives of the programme. Earlier understandings pertaining to consultations with the Fund continue to apply during 1983/84.

With regards,

Yours sincerely,

/s/

Pranab Mukherjee
Finance Minister

Encl.

Mr. J. de Larosière
Managing Director
International Monetary Fund
Washington, D.C. 20431

Statement of Policies

Considerable progress has been made during 1981/82 and 1982/83, the first two years of the adjustment programme covered by the extended arrangement with the Fund. The performance of India's economy was generally favourable in 1981/82, but drought caused severe setback in 1982/83. Real economic growth was reduced to about 2 per cent, with a reduction in incomes in the agricultural sector and a slowdown in industrial growth. The adverse weather imposed pressures on public finances; the Central Government's net borrowing was larger than projected and public savings, although increased from the previous year, were somewhat below the programme targets. Also, precautionary food imports to support the public food distribution system involved a cost to the balance of payments equivalent to 0.4 per cent of GDP. However, in most other respects, economic performance was favourable, and continued the progress toward adjustment achieved in 1981/82. Steps were taken during the year to strengthen public finances, including the raising of a significant volume of additional resources, and a cautious policy with regard to total credit was maintained. As a result, the increases of 13.4 and 15.4 per cent in narrow and broad money respectively in 1982/83 were broadly in line with the financial programme. Careful overall demand management policies, supported by efforts to ensure adequate supplies of key items, consolidated control over inflation; wholesale prices rose by 6.5 per cent over the course of 1982/83, below the programme projection of 8 per cent, and the rise in consumer prices was considerably reduced. Of particular note, balance of payments pressures eased significantly. Policies to encourage exports were continued, but largely because of the adverse world trading environment export volume fell below the programme target. However, the growth in the import bill was contained as investments in the oil and fertilizer sectors yielded substantial increases in domestic production; this more than offset the effects of a liberalised import regime aimed at promoting growth, and significant food imports. The current account deficit was 2.1 per cent of GDP, in line with the programme target, and the overall deficit declined sharply to SDR 1.1 billion, considerably less than envisaged in the programme.

2. The Government's economic policy programme for 1983/84 is outlined in the following paragraphs. The objective of the programme is to overcome the difficulties experienced in 1982/83 and achieve further economic progress in line with the original medium-term balance of payments adjustment programme. The programme is aimed at supporting a recovery in real economic growth to 6-6.5 per cent in 1983/84, which is a feasible objective if weather is normal, while limiting the increase in wholesale prices to 7 per cent. To this end, overall financial policies will continue to be cautious and budgetary policy will be directed toward containing deficit financing from the banking system and leaving ample scope for credit to the commercial sector. Policies will aim to promote increased savings in both the private and public sectors to finance increased investment. In line with the targets of the Sixth Plan, large investments will be made in key sectors to expand

productive capacity in areas important to external adjustment. Policies will be directed toward increasing efficiency and productivity and protecting international competitiveness. In particular, the programme will aim at promoting the expansion of exports while reducing import restrictions in some important areas. With these policies it is envisaged that further progress toward external adjustment will be achieved. The current account deficit in the balance of payments is projected to be SDR 3.5 billion, equivalent to 2.1 per cent of GDP. With a further increase in disbursements of commercial loans in line with cautious but expanded borrowing programme, the overall deficit is expected to be reduced to SDR 1.5 billion in 1983/84.

3. The Central Government's budget for 1983/84 has been framed to continue to promote production, savings, investments and exports while maintaining a tight rein on inflation and making special efforts to improve the welfare of weaker sections of the community. Compared with the 1982/83 budget, Plan outlays of the Centre and States are budgeted to rise by 26 and 16 per cent, respectively, yielding an increase in total Plan outlays of 21 per cent. The financing of this Plan has required a major resource mobilization effort at all levels of government. At the Central Government level, sizeable steps in this direction were taken in November and December 1982. New measures introduced in the 1983/84 budget, including an increase in the excise duty on cement, further increases in auxiliary and individual customs duties and in direct taxes will yield an additional Rs 7.2 billion. Increased railway and postal tariffs will yield Rs 4.4 billion in additional revenues in 1983/84. The budget provides for an increase in total expenditures of 9.2 per cent. The share of Plan outlays financed from the Central Government budget is to be reduced from 56 per cent in 1982/83 to 50 per cent. Central public sector enterprises are budgeted to finance 35 per cent of Central Plan outlays from internally generated resources compared with 29 per cent in 1982/83, reflecting steps being taken to increase the efficiency of public enterprises and signficant price adjustments. In addition domestic petroleum prices have already been increased by an average of 6 per cent in February 1983 which is expected to yield Rs 8 billion in 1983/84 (Rs 5.2 billion, of which accrues to the budget). The share of State Plans to be financed from State resources has increased to 64 per cent from 58 per cent in 1982/83. The States and their enterprises have agreed to mobilize additional resources yielding Rs 8.3 billion in 1983/84.

4. It is likely that additional expenditures beyond those provided for in the budget will be required in 1983/84. These would include increases in non-Plan expenditures on account of public sector wages and other contingencies, and increases in Plan outlays in some key sectors. Taking these factors into account, the Government projects that public savings will rise to 5.4 per cent of GDP in 1983/84. This would represent a continuation of the significant increases in this ratio achieved during the programme period (over 50 per cent since 1980/81); public savings rose from 3.5 per cent of GDP in 1980/81 to 4.2 per cent in 1981/82 and 4.8 per cent in 1982/83. Within the total, Central public

sector savings are projected to increase to 3.5 per cent of GDP in 1983/84 from 3.2 per cent in 1982/83. These increases reflect the strength of the Government's efforts to increase its resource mobilization to finance increased Plan investments. The resource position of both the Central and State Governments and their enterprises will be reviewed and measures taken as needed to ensure that the public finance targets for 1983/84, including those for public savings, are achieved.

5. For the year ahead, credit policy will remain committed to the objective of consolidating control over inflation while providing adequate support for a recovery in growth. The financial programme for 1983/84 is designed to be consistent with a recovery in real growth to 6-6.5 per cent, and an average increase in the general price level of 7 per cent. The programme takes into account the lagged effect of the decline in agricultural output and lower consumer price inflation which would offset the effects on the growth in the demand for money of the recovery in real growth and the consolidation of public confidence in price stability. The financial programme provides for an increase in narrow money of 12.0 per cent in 1983/84. Time deposits are projected to continue to increase strongly (16.9 per cent), reflecting in part an increase in the maximum interest rate payable on time deposits, introduced in October 1982. As a result, the growth in broad money is estimated to be 15.0 per cent in 1983/84. Allowing for the estimated deficit on external transactions, total domestic credit expansion is to be limited to 17.8 per cent. Within the total, the increase in net credit to Government is to be no more than Rs 61 billion; this increase takes into account the 1983/84 government budget and the additional factors indicated in paragraph 4. Taking account of seasonal factors, the Government intends to limit net credit to the Government and total domestic credit within the ceilings in the following table. Corrective measures will be taken promptly if developments indicate that the ceilings may be exceeded.

India: Ceilings on Net Credit to Government and Total Domestic Credit

(In billions of rupees)

	Amount Outstanding on March 31, 1983	Ceiling Amounts Outstanding on Sept. 30 1983	Dec. 30 1983	Mar. 31 1984
Net credit to Government	352.34	385.89	398.09	413.34
Total domestic credit	860.21	937.00	991.06	1,013.21

6. In March 1983, the ceiling interest rate for general bank lending was reduced from 19.5 to 18.0 per cent, and preferential bank lending rates were lowered by 0.5-1.0 percentage points. Deposit rates have been left unchanged, and the spread between deposit and lending rates reduced by halving the 7 per cent tax on banks' interest income. The adjustment of lending rates was appropriate because of the sustained decline in inflation; lending rates, including preferential lending rates, continue to be positive in real terms. The differential between general and preferential lending rates has been narrowed as a result of the recent interest rate adjustment. The structure of preferential lending is related to government socio-economic objectives, Plan priorities and imperatives of export promotion. The Government will continue to keep under review measures to increase the efficiency with which credit resources are allocated. The Reserve Bank of India is also reviewing the effectiveness of the credit authorization scheme with a view to rationalising and simplifying it. The Government has followed a policy of gradually increasing interest rates on government securities and in this connection policy will continue to be guided, inter alia, by the need to enhance the efficiency of the financial system.

7. Parallel with the Government's efforts to increase public savings, policies to encourage private savings, which account for about 80 per cent of total domestic savings, are being strengthened further. The objective is not only to increase private savings in aggregate, but also to raise the share of financial assets (currently about half). Following increases in deposit interest rates in March 1981 and 1982, a category of time deposits with maturity of five years or longer was introduced in October 1982 and the maximum bank deposit rate was increased from 10 to 11 per cent. In addition, the interest rate on five-year Post Office time deposits was increased from 10.5 to 11.5 per cent in March 1983. The Government will continue to deploy interest rate policy flexibly keeping in view developments in inflation. The 1983/84 budget includes additional measures to promote personal and corporate savings. With respect to deductions for savings through contributions to life insurance and provident funds, the previous ceilings on such deductions of 30 per cent of gross total income has been removed and the scope of eligible investments for this purpose widened, although the absolute monetary ceilings have been retained. At the corporate level, the general rate of depreciation in respect of plant and machinery has been increased from 10 to 15 per cent. Subscribers to the Public Provident Fund will be able to continue beyond 15 years, and the limit for annual subscription was raised from Rs 30,000 to Rs 40,000. The interest rate on special deposits of Employees' Provident Fund and other non-Government provident, gratuity and superannuation funds has been increased by 1 percentage point to 11 per cent; this will benefit workers and small savers. The exemption from income tax of investment income from a large number of financial assets, which had been Rs 4,000, and the additional exemption of Rs 2,000 for interest on securities and bank deposits with a maturity exceeding one year, have been merged and the total exemption limit has been raised to Rs 7,000; the existing separate exemption of Rs 3,000 in respect of income from units of the Unit Trust of India is

unchanged. Tax incentives in respect of nonresident Indians investing in India have also been liberalized. Henceforth, a flat rate of tax of 20 per cent (plus surcharge) will be levied on incomes derived from investments including shares and debentures of Indian companies, units of the Unit Trust of India, and government securities. Furthermore, the interest rate on six-year National Savings Certificates, which is normally 12 per cent per annum, has been raised to 13 per cent for subscriptions in foreign exchange by nonresidents.

8. The Government is continuing its efforts to strengthen domestic capital markets so as to encourage private savings and reduce reliance on bank financing for investment needs of the stronger corporate enterprises. Measures introduced so far during the programme period, include increases in the interest rates on convertible and nonconvertible company debentures and preference shares; larger tax exemptions, including a doubling of the amount of equity investment qualifying for tax-exempt status; and a liberalisation of the permissible debt/equity ratios. These measures contributed to a quantum jump in capital raisings by companies in 1981/82 to Rs 5.29 billion. The buoyancy in new issues continued in 1982/83 when 287 companies raised capital totalling Rs 7.85 billion. To strengthen further the capital market, the Government has taken steps to encourage the development of a broader secondary market for nonconvertible debentures. Companies issuing nonconvertible debentures undertake to repurchase debentures at par from debenture holders, subject to certain limits and to a minimum holding period of one year, and institutional investers in turn, enter into agreements with the companies concerned to repurchase from them, at par, debentures so acquired. As a result of Government encouragement and the favourable investment climate, the prospect is for a further increase in capital market activity in 1983/84.

9. Agricultural policies in 1983/84 have been designed to stimulate a strong recovery in agricultural production following the setback caused by the severe drought in 1982/83. Emphasis continues to be placed on the medium-term goals of increasing foodgrain output and improving production of crops which have important implications for the balance of payments. In this, great importance continues to be attached to the expansion in the area under irrigation. Following an increase of 2.4 million hectares in irrigated area in 1982/83, a further expansion of 2.5 million hectares is planned for 1983/84. The considerable improvements made in the fertilizer distribution system in 1982/83 will be consolidated in 1983/84 and a 12.5 per cent increase in fertilizer consumption is projected. A further expansion in the area under high-yielding varieties is also expected. Programmes are being introduced to encourage the cultivation of oilseeds on irrigated land, promote more intensive cultivation of pulses, and increase production on rainfed land. The 1983/84 budget includes a special allocation of Rs 1.25 billion for a programme to improve the productivity of small and marginal farmers. Agricultural procurement and support prices will continue to be actively deployed to support agricultural expansion. Foodgrain procurement prices for 1983/84 will be established with a view both to providing adequate production incentives and strengthen official grain procurement in line with the

objective of rebuilding foodgrain stocks. To this end, the wheat procurement price for the current rabi harvest was raised by 6.3 per cent, and a support price for barley was also announced. At the same time, the issue prices of wheat for distribution to the public and to the mills were both raised, in line with the Government's objective to contain the subsidy bill. The Government remains firmly committed to development programmes aimed at the upliftment of the weaker sections of society, especially in rural areas.

10. Plan expenditures allocated to the petroleum sector were increased by 51 per cent in 1981/82 and by a further 68 per cent in 1982/83. The decision to devote an increasing proportion of Plan outlay to expanding domestic petroleum production has been more than justified by the impressive growth in oil production, which increased to 21.2 million tons in 1982/83 from 10.5 million tons in 1980/81. This increase in production over two years enabled net imports of oil to be reduced by 33 per cent to 16 million tons in 1982/83. A further increase in expenditure of 39 per cent is budgeted for 1983/84, when production is projected to rise to 26.3 million tons, which will result in a further decline in imports. The degree of self-sufficiency in petroleum, which amounted to 31 per cent in 1980/81, increased to 57 per cent in 1982/83 and is now expected to reach about 75 per cent by 1984/85. As noted above, the prices of a broad range of petroleum products were increased by an average of 6 per cent in February 1983. The Government's petroleum pricing policy is making a substantial contribution to resource mobilization and is designed also to restrain consumption of petroleum products and reduce reliance on imported energy.

11. The considerable progress achieved in 1981/82 in strengthening the performance of the infrastructural sectors of the economy was sustained in 1982/83. Power production increased by 7 per cent, despite the effects of the drought on hydrogeneration, and the addition to generating capacity of 3,060 MW was 41 per cent greater, and considerably closer to the higher programme target, than in 1981/82. As a result of measures taken by the Government, the plant-load factor of thermal power stations improved significantly and thermal power generation increased by 13.4 per cent in 1982/83. Coal production increased by 5 per cent in 1982/83 and railway freight movement showed some further improvement; in both sectors, the economy's needs in 1982/83 were effectively met. Substantial increases were recorded in the production of nitrogenous fertilizer (8.8 per cent) and cement (8.5 per cent), with capacity also expanding substantially in these two industries. There was, however, only a modest increase in steel production in 1982/83 because of weak demand. The Government remains firmly committed to ensuring adequate expansion in capacity in these key sectors. In conjunction with capacity increases, concerted efforts are being continued to strengthen management of public enterprises and increase capacity utilization and economic efficiency. Productive capacity in six key sectors is estimated to expand in 1983/84 in line with the following schedule:

	1982/83 Estimated	1983/84 Projected	1984/85 Sixth Plan (Original target)
Coal (production mn. tons)	130.7	142.0	165.0
Electric power (end-year installed capacity in '000 MW)	38.1	42.2	51.2
Nitrogenous fertilizer (mn. tons)	5.1	5.3	5.9
Railway freight traffic (bn. ton-km.)	176	184	220
Steel (mn. tons)	11.7	12.8	14.3
Cement (mn. tons)	34.0	38.0	43.0

Public sector Plan outlays amounted to Rs 215.9 billion in 1982/83 and are budgeted to rise to Rs 254.9 billion in 1983/84. The Government is considering significant additional Plan expenditures in 1983/84 to step up implementation of priority Plan projects in such key sectors as electric power, irrigation, coal and the railways. The Government intends to limit Plan expenditure within the amount of available resources, including the allowance for bank financing indicated in paragraph 5, and, if necessary, steps will be taken to ensure that expenditures are allocated so as to ensure that the essential investment needs in these sectors are met.

12. The Government recognizes the important role of public sector pricing, both in order to mobilize resources for investment and to promote an efficient use of resources. Together with steps to streamline efficiency, public pricing policies have been effectively implemented over the past year to increase the net profits of Central public enterprises from Rs 4.85 billion to Rs 6.0 billion in 1982/83. Coal prices were raised by 14 per cent in May 1982. Coal pricing policy is being reviewed by Government, taking into account the Government's objective that the coal industry should earn a return on equity capital of 10 per cent. Electricity tariffs have been raised in several States in 1982. However, a number of State Electricity Boards (SEBs) continue to face losses. Recently, most SEBs have agreed to a programme to set tariffs at levels which generate more resources while establishing ceilings on rural electrification subsidies paid by State Governments. Efforts are being made to effectively implement this programme in 1983/84. In 1983/84, as indicated in the original Statement of Policies (dated September 28, 1981) coal and electricity pricing policies will continue to be in accordance with the Government's policy objective that these prices should reflect economic cost and generate internal resources for investment. Fertilizer prices were raised by 38 per cent in 1980 and by a further 17.5 per cent

in 1981 following increases in costs and international prices. Since then there has been a reduction in international prices because of recession, but the domestic costs have increased on account of high capital costs, particularly of imported equipment, and domestic prices of feedstocks. As a result, the fertilizer subsidy has risen from Rs 3.9 billion in 1981/82 to an estimated Rs 8.0 billion in 1983/84. The increase in the subsidy also reflects higher carrying costs of fertilizer stocks because of lower growth in consumption of fertilizers due to farmer resistance to the increase in prices. The Government has initiated a detailed analysis of fertilizer pricing in its entirety in view of the Government's objectives of avoiding an undue fiscal burden and ensuring that domestic fertilizer prices be broadly in line with economic costs, while taking account of the need to provide due encouragement to increasing the use of fertilizers, particularly in areas where fertilizer use is very low.

13. Industrial policy is guided by the objectives of achieving higher productivity and encouraging private investment, while avoiding concentration of economic power, encouraging regional dispersal and providing adequate protection to small-scale producers. During recent years investment licences have been granted liberally, exemptions from licensing requirements have been expanded, and the scope of allowable activity of large and foreign investment firms has been increased consistent with national priorities. Steps have been taken to ensure that this thrust of policy will be carried forward in 1983/84. The value limit below which an investment licence is not required has been raised from Rs 30 million to Rs 50 million. This increase would more than offset the cost escalation since the last adjustment in 1978. In accordance with the provisions of the Monopolies and Restrictive Trade Practices (MRTP) Act, as amended in August 1982, the Government has announced a list of nationally important industries in which large companies will be allowed to operate without being subject to restrictions under the MRTP Act on setting up new capacity or expanding existing capacity. The procedure for MRTP units to obtain endorsement for higher capacity, based on past actual production, has also been simplified. A number of industries are exclusively reserved for small-scale producers in accordance with the Government's social objectives. The Government is cognizant of the need to avoid the limit on size from preventing potential economies of scale from being exploited in such industries, and this list has been adjusted from time to time. Parallel with the promotion of indigenous research and technology, the Government has over recent years adopted a flexible and pragmatic policy toward the import of foreign technology, with a view to upgrading technology and modernising Indian industry, thus improving efficiency. The limits on royalty payments and on the terms of outright purchases have been flexibly administered and approval has been granted where the value and the duration of royalty payments exceeded the normal limits in justified cases. Due in part to more liberal administration, the number of new foreign collaboration agreements reached a record high last year. In 1983/84, the Government intends to continue and strengthen the access of domestic industry to foreign technology, within the framework of its Technology Policy.

14. Despite recessionary conditions and decline in world trade in the year 1982/83, the policy of providing liberal access to imports of raw materials, intermediates and capital goods is being maintained and where appropriate strengthened in 1983/84. Accordingly, significant steps have been taken in the import policy for 1983/84 to further liberalise access to imports for exporters and for small-scale industry, and the policy was further strengthened in May by additional measures. The measures included: (i) expanding substantially the coverage of Open General Licence (OGL) imports; (ii) establishing new OGL facilities for units exporting 100 per cent of production and for nonresident Indians returning home; (iii) raising the effective value of REP and automatic licences by 20 per cent, when imports are carried by Indian vessels; (iv) raising the entitlement for REP licences by 10 per cent for exports to new markets or of new products and for those shipped by Indian vessels; (v) establishing a one-window clearance for automatic imports of capital goods and technology without indigenous angle clearance; (vi) increasing the flexibility in the use of REP licences by expanding the facilities of free choice in the limited permissible and canalised lists; and (vii) raising the limits on free imports of capital goods and technology against REP licences and allowing importers to use REP licences transferred to them for this purpose. Furthermore, the "baggage" allowance for Indians returning from abroad has been liberalised and this will have the effect of significantly increasing imports of certain categories of restricted items. Thus, although some measures were taken to reduce imports partly to prevent speculative purchases, the overall access to imports was raised substantially with most of the increases occurring for restricted categories of imports. Last year, international prices of a number of manufactured products declined sharply as the world economy continued to stagnate; as a result, imports of some of these products increased rapidly, adversely affecting several important industries. It was necessary to provide adequate protection, temporarily, to the industries which have a good long-term potential, from short-run adversity in the world economy. Thus, some products were shifted to a more restrictive import licensing category and some customs duties were raised. Also, there was a 5 per cent increase in the auxiliary import duty for most products. While this raises protection for products for which tariffs determine the effective level of protection, for a much wider range of products where licensing constitutes the effective instrument for providing protection, the level of protection was lowered as imports of restricted products were raised substantially. The import policy for 1983/84 thus preserves the structure of liberal access to imports and strengthens it in important areas. It gives an important signal of continuity in spite of highly adverse conditions in the world economy and is conducive to expanding production and efficiency in Indian industry, particularly in export sectors. As in the past, adjustments may be made in the import policy during the course of the year as necessary in the light of the emerging situation, including, inter alia, reclassification of the licensing category for some products. Measures in the direction of liberal access will be greater in impact than any adjustments to tighten restrictions. Changes will be in line with the broad objectives of the Government's policy, and the Government intends to review the

implementation of import policy in the light of its policy objectives before the end of 1983.

15. The programme envisages that, over the medium term, exports must accelerate from past trends. Export volume growth reached 7 per cent in 1981/82, 2 percentage points higher than the programme target, and was projected to rise to 9 per cent by 1984/85. The sizeable increase in export volume in 1981/82, arising from improved domestic supplies and encouraged by strengthened international competitiveness was maintained during early 1982/83. It is estimated that during the first half of 1982/83 export volume rose by 5 per cent. However, there was a sharp slowdown in export growth during the second half of 1982/83. This slowdown reflected mainly the impact of recessionary conditions in the world economy which affected India's exports with a lag and a slowdown in exports under bilateral payments arrangements, which had risen sharply in the previous two years. As a result, the growth in export volume in 1982/83 is now estimated to be 2 to 3 per cent, considerably less than the target of 7 per cent, which was established when world trading conditions were expected to be more buoyant. Within the framework of an expected upturn in world demand, the Government is determined to reverse the slowdown in export volume growth. Export volume growth is a key objective of the adjustment programme. In this connection, the Government will take the necessary measures to ensure a strong balance of payments in the medium term. However, it will take time to lift export performance, especially in view of the current position of the world economy and uncertainty concerning the pace with which the projected revival in world demand will occur and its impact on export markets. With this in view, the volume of exports is now targeted to expand by 5 per cent in 1983/84. This target is feasible in the light of present prospects for world trade, providing that protectionist measures are not intensified. While this target is below the original target of 8 per cent, it is envisaged that performance will improve over the course of the year and that at year end volume growth will be near the original target rate. To assist in achieving this, policies have been strengthened substantially. As noted above, the import policy for 1983/84 contains a number of measures which strengthen incentives for exporters by (a) increasing effective access to imports of restricted items of intermediates, capital goods and of technology through REP licences; (b) increasing the flexibility with which REP licences (including transferred licences) can be freely used for this purpose; and (c) providing special facilities for access and flexibility for units exporting 25 per cent of production, especially for those exporting 50 per cent or more. The increased flexibility in the use of acquired REP licences increases the premium on these licences when transferred and this strengthens incentives to exporters across the board. Units in the Free Trade Zone have been allowed to sell up to 25 per cent of their production in the domestic market against import licences. The scope of duty-free imports for exports has been expanded and some exports decanalised. The Government's policy of promoting 100 per cent export-oriented units is being effectively implemented. At the end of 1982/83, approval has been granted for the establishment of 285 units and 26 units have begun

operation; a considerable expansion in the number of units in operation is expected in 1983/84. Exports by 100 per cent export-oriented units are projected to contribute importantly to the export effort over the coming five years. There has been a substantial increase in exports under bilateral payments agreements over the past two years. The Government is conscious of the need to balance bilateral trade and has budgeted for a reduction of Rs 2 billion in its outstanding net credit in 1983/84. The Government is keenly aware of the need to ensure adequate export profitability and external competitiveness. The Government intends to review all relevant policies bearing on export development before the end of 1983 and if necessary will strengthen its policies.

16. The existing framework of policies concerning external borrowing will be continued in 1983/84. Parallel with efforts to maximise access to multilateral and other concessional sources of financing, the commercial borrowing programme is intended to ensure an adequate flow of project financing, especially after the period of the extended arrangement. It is expected that the debt servicing burden will increase over coming years, but will remain manageable. It remains the Government's policy not to increase the future debt service burden beyond prudent levels. The short-term debt is very small. As in the past, private companies are permitted subject to government approval, to raise funds abroad on their own account and without government guarantee. The Government continues to monitor closely the country's external borrowing commitments. During 1983/84, the Government will limit the official contracting and guaranteeing of nonconcessional loans with original maturity of between 1 and 12 years to no more than SDR 1.5 billion; within this ceiling, the official contracting and guaranteeing of loans with original maturity of between 1 and 5 years will be limited to SDR 200 million.

17. The Government recognizes that exchange rate policy has an important bearing on export growth. The rupee has been pegged to a basket of currencies of India's trading partners since September 1975. Exchange rate management followed this policy in 1981/82 and it was a factor in improved export performance. This policy was continued in 1982/83. The Government will continue to pursue a realistic policy in regard to exchange rates keeping in mind, inter alia, their objectives with regard to the overall balance of payments and export promotion.