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January 25, 1985

To: Members of the Executive Board

From: The Secretary

Subject: India - Staff Report for the 1985 Article IV Consultation

Attached for consideration by the Executive Directors is the staff report for the 1985 Article IV consultation with India. A draft decision appears on page 32.

It should be noted that Executive Board consideration of this item has been shifted from Wednesday, February 20 to Friday, February 22, 1985.

If Executive Directors have technical or factual questions relating to this paper prior to the Board discussion, they should contact Mr. Scott (ext. 7607) or Ms. Ripley (ext. 6531).

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INTERNATIONAL MONETARY FUND

INDIA

Staff Report for the 1985 Article IV Consultation 1/

Prepared by the Staff Representatives for the 1985 Article IV Consultation with India

Approved by Tun Thin and Eduard H. Brau

January 24, 1985

Contents | Page

1/ Under normal practice, this would be considered as the 1984 Article IV consultation. It is attributed to 1985 in this case because the last Article IV consultation discussions were held in October-November 1983 and the Board concluded the 1984 Article IV consultation on January 27, 1984.

Contents | Page

I. Introduction

A staff mission visited New Delhi and Bombay during the period November 2-17, 1984 to hold the 1985 Article IV consultation discussions and in this connection to review developments under the extended arrangement. The principal Indian officials participating in the discussions were Messrs. P.K. Kaul, Finance Secretary, Bimal Jalan, Special Secretary and Chief Economic Advisor, Montek Singh Ahluwalia, Economic Advisor, all of the Department of Economic Affairs; and Manmohan Singh, Governor, Reserve Bank of India. Meetings were held in New Delhi with officials from the Ministries of Finance, Agriculture, Commerce, Industry, Petroleum, and from the Planning Commission; and in Bombay with the Reserve Bank of India and specialized development finance institutions. The staff representatives were Mr. Scott (Head, ASD), Ms. Ripley (ASD), Ms. Kelly (ETR), Messrs. Choudhry and Hides (ASD) and Ms. Job (ASD). Messrs. Grawe and Hansen (IBRD, New Delhi) participated in some of the discussions. Mr. Malhotra, Executive Director for India, attended the meetings as an observer.

The Executive Board approved an extended arrangement for India (EBS/81/198) on November 9, 1981 in an amount of SDR 5 billion (291 percent of old quota). Programs were negotiated covering the three fiscal years (ending March 31) 1981/82 to 1983/84. All performance criteria were observed and scheduled purchases, totaling SDR 3.9 billion, were made. In January 1984, the Indian authorities announced their intention to cancel the extended arrangement, effective May 1, 1984. This released committed resources amounting to SDR 1.1 billion.

India continues to avail itself of transitional arrangements under provisions of Article XIV and maintains a bilateral payments agreement with a Fund member (Romania) that is subject to approval under Article VIII.

II. A Retrospective and Economic Background to the Extended Arrangement

Indian economic performance during the 1970s was characterized by modest economic growth, moderate inflation, and a sustainable external position. Development plans aimed at a reduction in the number of families below the poverty level, but performance in this regard was disappointing. Between 1970/71 and 1980/81, real GDP rose at an annual rate of 3.2 percent; in per capita terms the increase was only 1 percent (Chart 1). 1/ Despite the rise in gross domestic savings from 17 to 23 percent of GDP, with a commensurate rise in gross investment, there

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1/ All macroeconomic statistics are reported on a fiscal-year basis (April-March) unless otherwise noted.

was no ascertainable increase in the trend rate of growth over the period. This may be attributed to both a high rate of capital consumption--about one third of gross fixed investment--and inefficiencies in the use of resources (Chart 2). 1/ In most key industries there was a marked fall in capacity utilization.

Exports grew rapidly in real terms in relation to GDP growth. Nonetheless, with export growth of 6 percent per annum, there was a continuing loss in India's market shares (Chart 3). The relative profitability of exports continued to deteriorate in relation to domestic sales. Imports rose, in real terms by 6 percent annually, with wide annual variations reflecting the availability of foreign exchange and also the developments in import prices. The approach of the authorities toward commercial borrowing and reserves management was extremely cautious; reserves came under pressure during 1974-75, but were restored to relatively high levels during the second half of the decade.

Developments in the external balance during the 1970s were marked by the two oil shocks. The first was followed by an increase in the value of merchandise imports (in terms of SDRs), which, despite a marked increase in the value of exports, caused the trade balance to move into a deficit equivalent to about 2 percent of GDP in 1974/75 and 1975/76. The current account deficits that emerged in these two years were more than offset by concessional inflows and net drawings from the Fund, including a first credit tranche purchase and drawings under the compensatory financing and oil facilities. The current account was brought into surplus in 1976/77 and 1977/78 with the elimination of the trade deficit through substantial export growth, cautious import management, and a significant strengthening on invisibles. Gross reserves rose to SDR 4.7 billion at end-1977/78, equivalent to 9 months of imports.

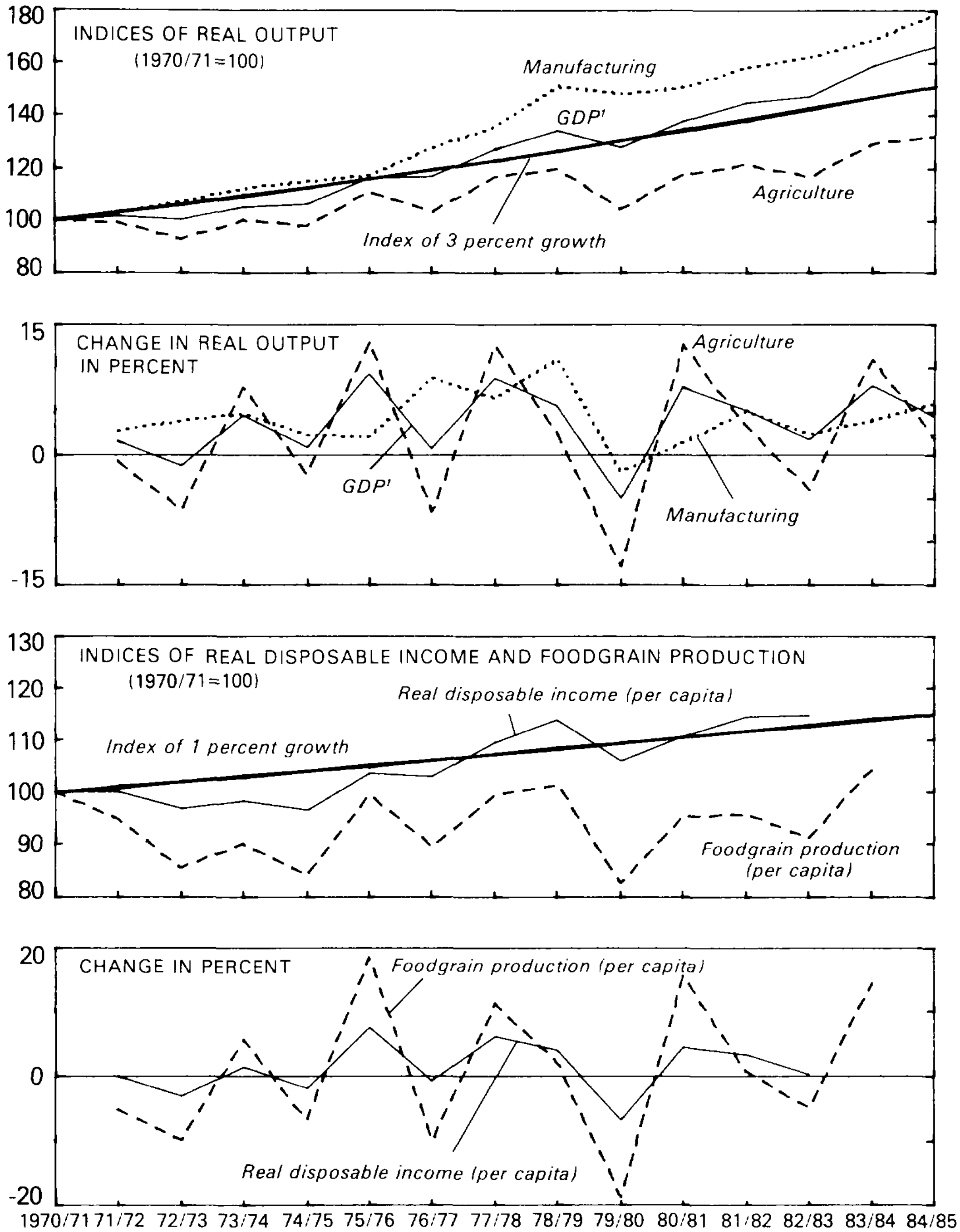
The rise in oil prices and associated deterioration in the terms of trade caused the current account to shift from near balance in 1978/79 to a deficit equivalent to 1.6 percent of GDP in 1980/81. The shift in the trade balance over this period was almost 3 percent of GDP. Two thirds of the increase in the import bill in these years was accounted for by crude oil and oil products. Capital inflows more than offset the modest current account deficit in 1979/80, but fell far short in the subsequent year, despite disbursements from the Trust Fund of SDR 525 million. This period was associated with a reorientation of policy toward a longer-term strategy to strengthen economic efficiency and growth, and particularly export growth, rather than to sharply curtail imports for purposes of external adjustment.

1/ Net investment as a proportion of net domestic product rose from 12 percent to 18 percent over the same period. About one third of the increase reflected higher annual inventory accumulation.

CHART 1

INDIA

SELECTED INDICATORS OF GROWTH



Sources: Central Statistical Organization, *National Accounts Statistics, 1970/71-1981/82*, Quick estimates, 1982/83, and data provided by the Indian Authorities.

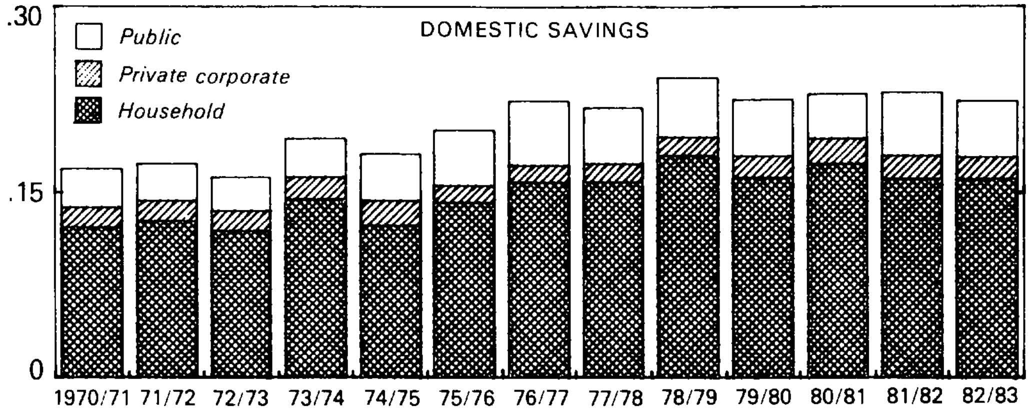
[1] At factor cost

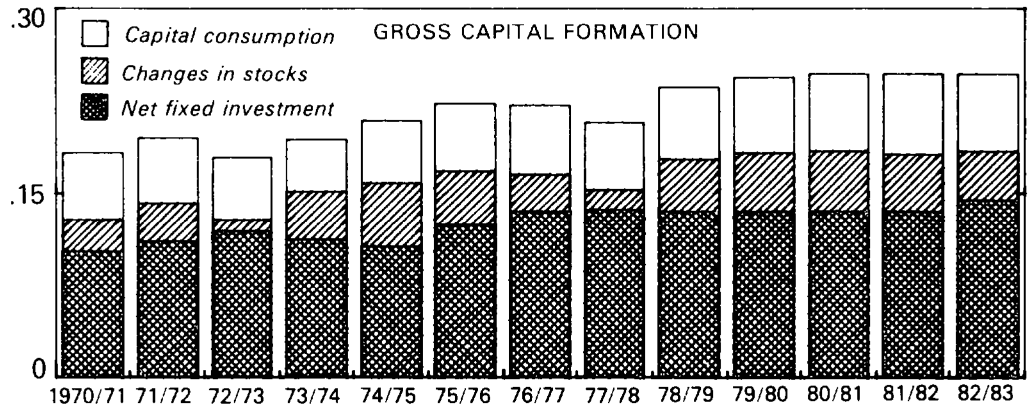
CHART 2

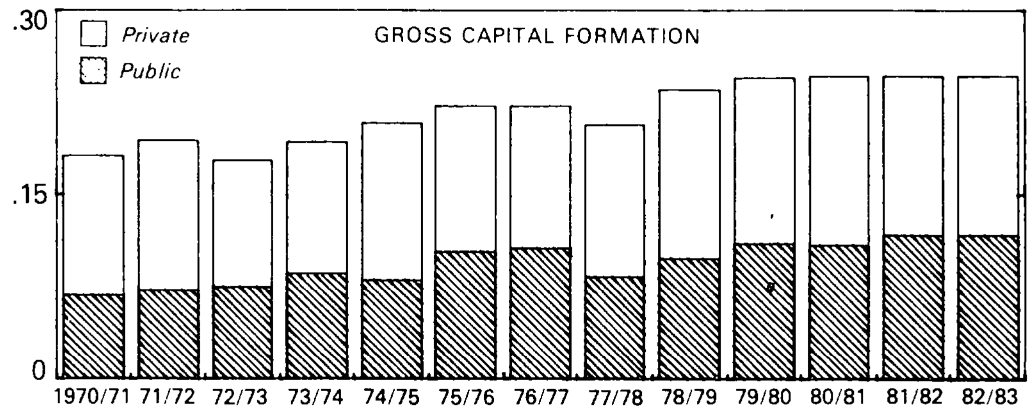
INDIA

SAVINGS AND INVESTMENT

(As percent of GDP)







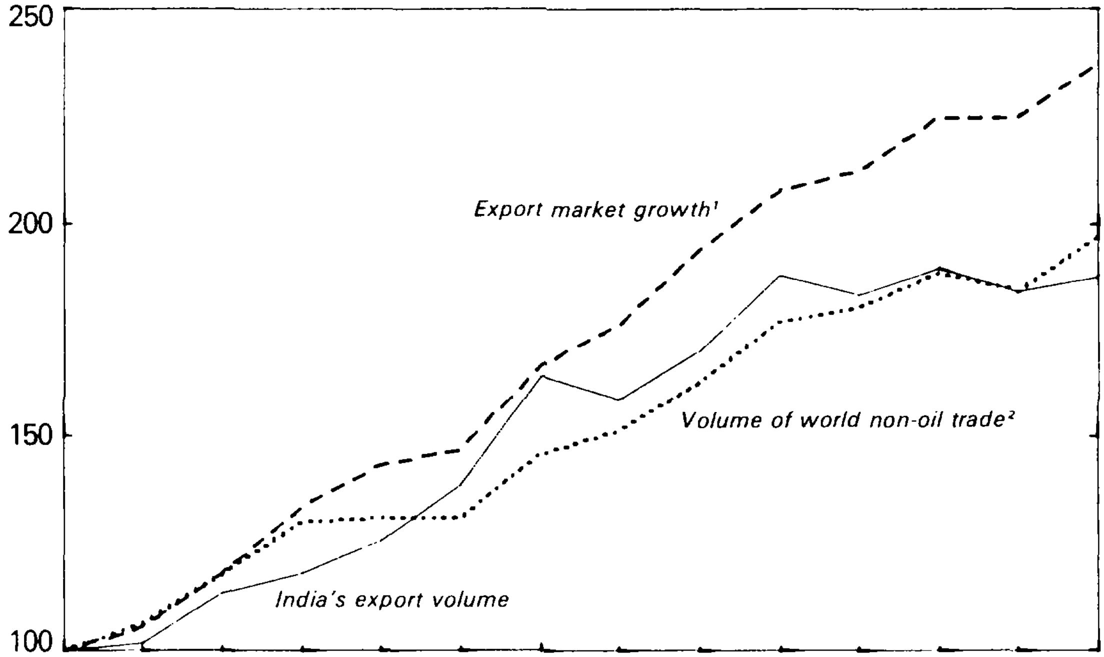
Sources: Central Statistical Organization, *National Accounts Statistics, 1970/71 1981/82;* Quick estimates 1982 83, and data provided by the Indian Authorities.

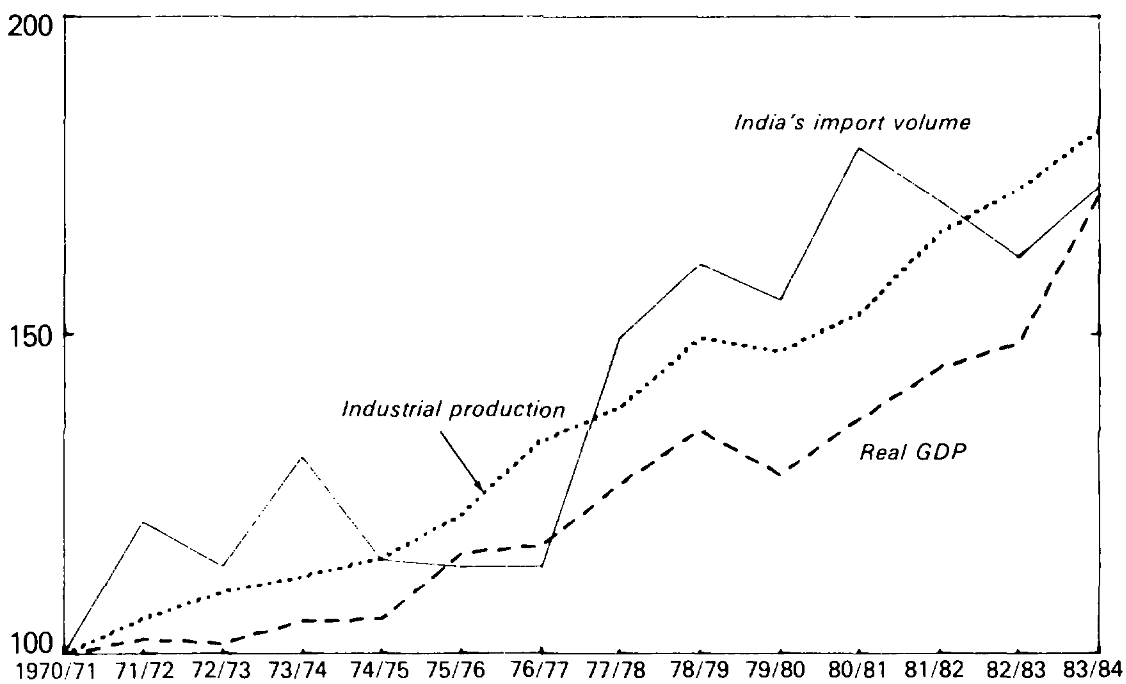
CHART 3

INDIA

TRADE VOLUMES, DOMESTIC AND FOREIGN DEMAND

(Indices: 1970/71 = 100)





Source: IMF, Datafund; Directorate General of Commercial Intelligence and Statistics, *Foreign Trade Statistics of India;* and staff estimates

[1] Partner countries' non-oil import volume weighted by the regional pattern of India's exports in 1980.

[2] Volume of world exports, excluding those of the oil exporting country group.

III. Adjustment Strategy, Instruments and Targets Under the Extended Arrangement

The adjustment strategy pursued under the extended arrangement was based on that of the Sixth Plan (1980/81-1984/85); the strengthening of the balance of payments was sought through measures to increase agricultural and industrial supplies and to make the domestic economy more efficient. Structural reforms were to be pursued particularly in the areas of industrial and trade policies in coordination with a careful policy of demand management. Because policies aimed at strengthening the structure of production were expected to have a long gestation period and because the external balance was still sustainable, the external adjustment path sought was a gradual one coupled with substantial domestic growth. The current account deficit was expected to remain broadly unchanged at about 2 percent of GDP until 1983/84 and to decline somewhat in 1984/85. 1/ Sizable overall balance of payments deficits were projected for the period of the arrangement (Table 1).

Real growth was targeted at 4.8 percent per annum, and the rate of wholesale price inflation was to be reduced from 15.4 percent in 1980/81 to 8 percent in 1983/84. High sectoral and overall rates of growth were to be achieved through an increase in the already high level of investment, particularly in the public sector, the alleviation of infrastructural bottlenecks, and generally improved efficiency of resource use. Particular stress was laid on the alleviation of shortages of coal, electric power, steel, cement, and railway transportation and on greater use of fertilizer and on the extension of the area under irrigation (Table 2). The accelerated schedule for crude oil production was expected to result in a decline in oil imports over the program as increases in domestic production were expected to exceed increases in consumption.

Improvements in efficiency were to be achieved by maximizing production from existing industrial capacity, and stimulating capacity expansion so as to (a) overcome bottlenecks; and (b) exploit economies of scale and areas of comparative advantage. Policies to achieve these objectives were to include improved access to imported inputs, including capital goods and foreign technology; the easing of regulatory restraints on capacity and production expansion; and heightened internal resource mobilization and production incentives through more flexible pricing policies.

Financial policies were designed to generate the increase in total domestic savings required to support the step-up in investment. Increased domestic savings were to result primarily from additional resource mobilization efforts by the public sector. Public sector savings targets (Table 1) were to be achieved mainly through a reduction

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1/ The current account deficit for 1980/81 initially was estimated at 2.1 percent of GDP. Subsequently, this was revised to 1.6 percent.

Table 1. Selected Economic and Financial Indicators, 1980/81-1983/84

	1980/81		1981/82		1982/83			1983/84		
	Program base 1/	Actual	Original program 1/	Actual	Original program 1/	Revised program (EBS/82/102)	Actual	Original program 1/	Revised program (EBS/83/130)	Actual/ prov.
					(Annual percent changes)					
National income and prices										
Real GDP at factor cost	7.0	7.8	4.8	5.3	4.8	5.0	1.8	4.8	6.0-6.5	8.0
Agriculture	14.0	12.8	1.4	3.3	1.4	1.7	-3.9	1.4	5.0	10.7
Manufacturing	4.1	1.7	7.3	5.1	7.3	7.0	2.4	7.3	7.0	4.0
GDP deflator	12.0	11.4	9.0	10.2	8.5	8.5	7.8	8.0	7.0	7.0
Wholesale prices 2/	15.4	16.7	11.0	2.4	9.0	8.0	6.6	8.0	7.0	9.1
Consumer prices 3/	...	11.4	...	12.5	...	...	7.8	...	7.0	12.6
External sector										
Exports, f.o.b.	13.3	7.1	16.2	11.8	16.1	11.9	0.4	16.6	7.2	6.4
Imports, c.i.f.	41.2	41.6	12.4	5.3	12.0	3.9	-2.8	15.8	3.8	4.7
Oil	85.1	66.0	-7.9	-6.5	0.6	-8.1	-10.4	14.3	-17.7	-23.9
Non-oil	17.2	28.0	29.8	13.8	19.0	11.2	1.7	16.5	14.2	19.7
Export volume	...	-0.8	5.0	3.5	7.0	7.0	-2.9	8.0	5.0	1.9
Import volume	...	15.8	1.6	-4.9	2.7	-1.0	-5.1	...	4.0	8.5
Terms of trade deterioration -)	...	-11.7	--	-2.4	-0.6	--	1.0	-0.6	3.2	8.2
Nominal effective exchange rate 2/	...	-3.9	...	-2.9	...	...	-3.6	...	...	-6.8
Real effective exchange rate 2/	...	-3.4	...	-4.8	...	...	-1.1	...	...	-0.7
Central government budget										
Revenue and grants	18.9	13.1	16.8	21.4	...	14.5	16.2	...	15.5	14.5
Total expenditure and net lending	18.9	19.3	15.5	14.7	...	11.6	26.2	...	13.0	14.1
Money and credit										
Domestic credit	24.6	25.0	19.4	18.9	18.3	18.6	17.4	17.4	17.8	15.5
Government	34.2	28.4	20.1	19.1	17.6	17.9	14.9	16.3	17.3	14.3
Commmercial sector	18.8	18.6	18.9	18.7	18.9	19.0	19.3	18.1	18.1	16.4
Money and quasi-money (M_3)	18.5	18.2	15.7	12.7	14.5	15.9	15.8	14.0	15.0	18.2
Narrow money	12.8	16.6	11.3	6.8	11.0	13.8	14.6	11.0	12.0	15.7
Interest rate (annual rate, five-year savings deposit)	10	10	10	10	...	10	11.0	..	11.0	11.0
					(In percent of GDP)					
Public plan outlays	11.6	11.7	11.8	12.3	12.9	12.5	13.2	14.1	14.3	13.4
Public sector savings	3.6	3.6	4.4	4.3	4.8	5.0	4.9	5.2	5.4	5.0
Central government savings	2.3	2.3	3.0	2.8	3.2	3.3	3.2	3.5	3.5	3.4
Central government budget deficit	6.2	6.5	6.4	5.8	6.4	5.6	7.5	6.8	6.5	7.1
Domestic bank financing	3.4	3.1	3.1	2.6	3.0	2.8	2.2	2.9	2.9	2.4
Foreign financing	...	1.1	0.9	0.7	1.0	0.7	0.8	...	0.9	0.9
Gross capital formation	23.7	24.6	25.7	24.7	26.1	25.5	24.1	26.5	26.4	25.0
Gross domestic savings	23.9	23.0	23.7	22.6	24.1	23.4	22.4	24.3	24.3	23.6
Current account deficit	-2.1	-1.6	-2.1	-1.8	-2.0	-2.1	-1.6	-2.3	-2.1	-1.5
Overall balance of payments (SDR mn.)	-712	-774	-1,683	-2,172	-2,024	-1,683	-1,143	-2,655	-1,497	-373
External debt (including IMF)	10.9	11.8	11.2	12.2	11.7	12.0	14.2	14.5	14.4	14.7
Debt service ratio 4/5/	8.3	8.5	8.5	9.3	9.2	11.0	11.3	9.9	13.8	14.0
Interest payments 4/5/	...	2.9	3.1	3.3	4.2	4.3	5.3	5.2	7.1	7.4
Gross official reserves (months of imports)	6	6	5	4	3	4	5	3	4	5
External payments arrears	--	--	--	--	--	--	--	--	--	--
Ceilings on nonconcessional loans (in millions of SDRs)										
1-12 years	--	--	1,400	363	--	1,400	1,269	--	1,500	751
1-5 years	--	--	400	44	--	200	120	--	200	30

1/ Original program projections (November 1981). Including subsequent refinements to the statistical definition of public savings.
2/ End-year percentage change.
3/ Annual average percentage change.
4/ In percent of total current receipts.
5/ Including IMF.

Table 2. India: Agriculture and Industry Targets and Achievement, 1980/81-1983/84

(In millions of tons)

	1980/81		1981/82		1982/83			1983/84		
	Program base	Actual	Original program	Actual	Original program	Revised program	Actual	Original program	Revised program	Actual 1/
Industry capacity										
Coal (production)	114	114	121	124.2	...	133	130.7	...	142	138.4
Electric power (installed capacity, '000 mw)	32.8	33.2	36.1	35.6	41.0	38.6	38.8	46.4	42.2	43.2
Nitrogenous fertilizer	4.6	4.6	5.3	4.7	5.3	5.3	5.1	5.4	5.3	5.2
Railway freight (bn. ton kilometers)	158	158	173	174	185	184	178	200	184	176
Steel	11.2	11.2	11.2	11.2	14.1	12.4	11.2	14.3	12.8	12.5
Cement	28.2	27.0	30.0	29.3	35.0	38.0	33.5	40.0	38.0	37.0
Crude oil	...	10.5	...	16.2	...	20.95	21.1	...	26.3	26.0
Agriculture										
Foodgrain (production)	133.0	129.9	138.5	133.3	143.3	141.5	129.5	148.4	142.0	151.5
Area under irrigation (mn. hectares)	55.1	54.1	57.6	56.0	60.1	60.1	58.1	62.6	61.07	60.5
Fertilizer consumption	5.6	5.5	6.6	6.1	7.5	7.2	6.4	8.5	7.2	7.8

Source: Data provided by the Indian authorities.

1/ Official estimates.

in subsidies and improved profitability of public enterprises. 1/ It was recognized that the targeted levels of public sector savings would be insufficient to finance the ambitious investment plan and that increased efforts would be required, particularly at the State level, for this purpose. However, if sufficient savings were not forthcoming, investment targets in key sectors for which the States had a major responsibility, notably electric power and irrigation, were to be safeguarded. Measures to encourage private savings included widening the range of attractive financial assets available to private savers and, if necessary, a more flexible interest rate policy.

The Central Government budget deficit was projected to remain at 6-7 percent of GDP. 2/ The annual rate of increase in bank credit to Government (including both the Central and State Governments) was targeted to decline from 34 percent in 1980/81 to 16 percent in 1983/84, thus leaving adequate room to meet the financing needs of the commercial sector. The projected increase in monetary aggregates during the program was consistent with a reduction in inflationary pressures.

External policies stressed the development of a dynamic export sector; this represented a major change from the earlier emphasis given to import substitution. Export policies were generally to focus on identifying and removing disincentives, e.g., from the tax system, from inadequate access to imported inputs, and from industrial and other regulatory constraints. In addition, special export incentives were to be provided to industries considered to have high export potential. The authorities recognized that their goal of increasing the volume of exports by 8 percent in 1983/84 (and by 9 percent in 1984/85) would depend in part on the adequacy of financial incentives. Exchange rate policy was to be consistent with achieving a strengthened export performance.

Import policies were to continue to provide protection to domestic producers, while at the same time carrying forward the policy on liberalizing access to imported inputs, including capital goods, established in the late-1970s. Imports of finished consumption goods, other than essential items, were not expected as part of the more liberal import policy. Rather, policies were to focus on enhancing the

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1/ Public savings under the program were defined as savings available for Plan expenditure. This definition differs from the national accounts concept, but historically there has been no large difference between these alternative measures. The program concept was adopted to facilitate monitoring on a timely basis.

2/ Explicit targets were not established for the consolidated deficit of the Central and State Governments or for the consolidated public sector. The implicit public sector deficit (defined as the difference between public plan outlays and public sector savings) was projected to increase from 8 percent of GDP in 1980/81 to almost 9 percent in 1983/84.

efficiency of resource use by overcoming supply-side weaknesses, thus helping to reduce production costs. Significant measures aimed at increasing access to imported inputs were to be implemented in the Import Policy Orders for 1982/83 and 1983/84. The authorities undertook to provide an assessment of the significance of these measures at the time they were introduced. Measures to be considered included greater access to restricted imports, a shift in some items from more restricted to less restricted import categories, and measures to simplify regulations and procedures governing import license approval. A more flexible implementation of policies governing imports of capital goods and technology and foreign collaboration agreements was also to be pursued.

IV. Recent Developments and Performance Under the Extended Arrangement, 1981/82-1983/84

1. Overview

The extended arrangement was predicated on the assumptions of normal weather, a buoyant world economy, buoyant commodity prices, and successful implementation of structural and demand management policies. International oil prices were expected to remain constant in real terms and India's terms of trade were to continue to decline, though only slightly. Oil imports were expected to decline in volume terms over the period of the arrangement, and in nominal terms for the first two years. A shift in the composition of imports toward more expensive refined products, as the limits of domestic refining capacity were reached, was expected to result in an increase in the oil bill in nominal terms in 1983/84. Non-oil imports were projected to increase substantially in volume terms both on account of more rapid growth and in response to a more liberal import policy. Notwithstanding a large increase in the total import bill and some weakening in invisibles on account of rising interest payments and slow growth of remittances, the rapid growth of exports was expected to keep the current account deficit roughly unchanged in relation to GDP.

Circumstances differed significantly from those assumed. The world recession lasted longer than expected: India experienced a major drought in 1982 followed by extremely favorable weather conditions in 1983 and 1984; oil prices declined in terms of the U.S. dollar; and world inflation was less than envisaged. Thus, after deteriorating in 1981/82, India's terms of trade improved in both 1982/83 and 1983/84. Also, the estimate of the current account deficit for 1980/81 subsequently was revised downward from 2.1 percent of GDP to 1.6 percent, both on account of revisions in the balance of payments figures and in nominal GDP.

Assessing performance under the extended arrangement in terms other than established performance criteria, which were consistently observed, is difficult. Apart from changes in underlying assumptions and base data, the data covering the period of the arrangement are, at best, highly tentative and will be subject to further revisions. In addition, the inadequacies or limited availability of data preclude assessment of the extent to which such underlying objectives as improvements in efficiency and competitiveness were achieved. However, the broad objectives of higher economic growth, lower inflation, and avoiding a deterioration in the external balance on current account, appear to have been achieved.

Reflecting the effects of weather and world demand, the growth path was different from that envisaged, with growth falling short of the program target in 1982/83 and exceeding it in 1983/84. Inflationary tendencies re-emerged toward the end of the second year of the program and continued into 1983/84, partly as a result of weather-related factors, but also as a result of higher than programmed monetary expansion. The outturn on both the current account and overall balance of payments was significantly better than expected, but at much lower levels of exports and imports (both in volume and value terms) than envisaged. Higher than projected domestic oil production and lower oil import prices were major contributing factors. Non-oil imports were also below projections.

While the stronger external performance and the attainment of growth objectives are to be welcomed, the reduced growth of non-oil imports and exports suggests that economic policies have had a smaller impact on external trade than expected, and that the looked-for strengthening of the export sector under the initial program has not been fully realized. Although this was due partly to slower growth in world trade, the original program anticipated that India's exports would rise more rapidly than import growth in its major markets. Available data indicate that India's export performance has continued to lag behind market growth (Chart 1).

2. Balance of payments and external debt

At the time the extended arrangement was negotiated, the current account deficit was projected to remain approximately unchanged in relation to GDP during the program period but to decline as a percent of GDP from 1984/85. Debt service payments (including those to the Fund, but excluding interest on nonresident deposits) were projected to rise from 8.3 percent of current receipts in 1980/81 to 10 percent in 1983/84 and to a peak of 16 percent in the late-1980s before receding. In the event, the current account deficit in relation to GDP has remained relatively stable around the actual base year value of 1.6 percent, a level considerably lower than envisaged. Reflecting this development and more buoyant capital inflows, the cumulative overall balance of payments deficit during the program was less than two thirds of that envisaged under the original program.

The more favorable outturn on the current account now provisionally estimated for 1983/84 reflects primarily the lower deficit at program inception, the greater strength of workers' remittances, and higher domestic oil production (Table 3). Notwithstanding policy initiatives to improve competitiveness and reduce domestic nonprice barriers to exports, export performance was disappointing over the program. Export volume increased on average at an estimated 0.8 percent per annum, compared to a program target of 5.7 percent (based on revised program estimates) and market growth for India of almost 4 percent. Measures to encourage exports, such as special tax benefits to 100 percent export-oriented units and units in free trade zones, revisions of cash compensation and duty drawback rates, and frequent adjustment to the nominal exchange rate so as to maintain the same real effective rate as in November 1981 were not sufficient. Export performance was also adversely affected in 1983/84 by a brief dock strike 1/ and by a decline in exports to bilateral areas (mainly the U.S.S.R.) to reduce surpluses in bilateral accounts.

The trade balance has been more in line with program expectations as import growth was also substantially less than foreseen. Both oil and non-oil imports fell well below the original program projection for 1983/84, due to lower price and volume increases and base period revisions. Accelerated domestic oil production and weaker than expected industrial growth and investment dampened import demand.

Higher commercial borrowing and substantially larger inflows of nonresident Indian deposits were the major sources of increased capital inflows. The latter reflected the maintenance of attractive interest rates. Government and government-guaranteed loans subject to program ceilings were held well within the limits. This financing was augmented by several public sector enterprises which increased their reliance on suppliers' credits and other loans that did not require a government guarantee (Table 1).

The lower cumulative current account deficit, coupled with more buoyant capital inflows, caused gross reserves to reach levels substantially above those anticipated in the program. However, largely because of the slower export volume growth and decline in global inflation, the burden of debt service payments for 1983/84 is estimated at 14 percent of current receipts, compared to the program forecast of 10 percent. Including interest on nonresident deposits, the ratio in 1983/84 was 15 percent.

3. Real sector and prices

For the period 1981/82-1983/84, real growth (at factor-cost) averaged 5 percent per annum, somewhat higher than the program target. The stronger overall performance mainly reflected favorable developments

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1/ If adjusted to exclude the effects of the dock strike of March-April 1984, the average annual rate of export volume growth would have been about 1.5 percent over the program period.

Table 3. India: Balance of Payments, Program Targets, and Outturn, 1980/81-1983/84

(In millions of SDRs)

	1980/81		1981/82		1982/83			1983/84		
	Original program	Actual	Original program	Actual	Original program	Revised program	Actual	Original program	Revised program	Prel. actual
Exports, f.o.b.	6,996	6,479	8,128	7,324	9,435	8,230	7,581	11,002	8,171	7,894
Imports, c.i.f.	-12,021	-12,359	-13,508	-13,271	-15,133	-13,876	-13,069	-17,519	-13,538	-13,265
Oil	-5,567	-5,188	-5,128	-4,840	-5,159	-4,640	-4,219	-5,895	-3,528	-3,306
Non-oil	-6,454	-7,171	-8,380	-8,431	-9,974	-9,236	-8,850	-11,624	-10,010	-9,959
Trade balance	-5,025	-5,880	-5,380	-5,947	-5,698	-5,646	-5,487	-6,517	-5,367	-5,371
Net invisibles	2,409	3,816	2,350	3,409	2,285	2,235	3,050	2,221	1,967	2,746
Nonfactor services	734	1,115	910	923	990	1,097	917	1,020	1,113	1,000
Investment income 1/	345	477	40	329	-180	-135	-268	-349	-512	-554
Private tranfers	1,330	2,224	1,400	2,157	1,475	1,273	2,401	1,550	1,346	2,300
Current account balance	-2,616	-2,064	-3,030	-2,538	-3,413	-3,411	-2,437	-4,296	-3,400	-2,625
Net aid	1,528	1,384	1,267	975	1,293	1,460	1,579	1,466	1,532	1,495
Disbursements	2,101 1/	2,060 2/	1,889	1,610	1,950	2,096	2,137	2,100	2,116	2,077
Repayments	-573	-676	-622	-635	-657	-636	-558	-634	-584	-582
Commercial borrowing	126	91	80	80	96	364	334	176	464	499
Bilateral arrangements		-73		-280		--	-333		139	183
Other capital 3/	250 4/	148 4/	--	-142	--	-96	914	--	-232	422
Errors and omissions (net)		-260		-267		--	-1,200		--	-347
Overall balance	-712	-774	-1,683	-2,172	-2,024	-1,683	-1,143	-2,655	-1,497	-373
Monetary movements	712	774	1,683	2,172	2,024	1,683	1,143	2,655	1,497	373
IMF (net)	320	266	900	600	1,800	1,800	1,800	2,344	1,233	1,234
Reserves (increase -)	392	508	781	1,572	224	-117	-657	421	254	-861
Exchange rate (Rs/SDR)	10.153	10.150	10.000	10.295	10.000	10.450	10.526	10.000	10.791	10.914
GDP (Rs billion)	1,294.5	1,274.9	1,478.0	1,486.8	1,681.0	1,681.4	1,644.1	1,902.0	1,780.5	1,900.0
Current account/GDP	2.1	1.6	2.1	1.8	2.0	2.1	1.6	2.3	2.1	1.5

1/ Excludes interest on nonresident deposits.
2/ Includes Trust Fund loans of SDR 525 million.
3/ Includes nonresident deposits.
4/ Includes SDR allocations of SDR 120 million.

in 1983/84, following a year of severe drought and accompanying a revival in economic activity abroad. Inflation was brought under control during the first two years of the program. However, wholesale prices began to accelerate at the end of 1982/83, a trend which continued into 1983/84. While initially this development reflected shortages of some items affected by drought and the impact of increases in administered prices, the continuation of these trends was associated with strong monetary expansion.

Agriculture registered an average growth rate of about 3.3 percent over the period, compared to the original program target of 1.4 percent. The severe drought in 1982/83 resulted in a decline in output, primarily of foodgrain, but the resilience of the agricultural system, together with substantial official stocks, obviated the need for heavy recourse to foodgrain imports. A combination of good weather and further productivity gains resulted in a record harvest of 152 million metric tons of foodgrains in 1983/84. Policy adjustments contributing to strong agricultural growth included increases in producer incentives resulting from increased procurement prices, a reduction in fertilizer prices in 1983, and the provision of adequate credit. Investments to extend the area under irrigation and field service support to further the use of fertilizer and high-yielding varieties of seeds were also pursued. However, the extension of area under irrigation fell somewhat short of program targets, partly reflecting financial constraints on the States. Production of oilseeds and pulses did not respond as had been hoped to the strengthening of procurement prices and substantial imports of edible oils and pulses were required.

Industrial and manufacturing growth averaged 4.3 percent and 3.8 percent, respectively, over the period and fell well short of the program target (7.3 percent for manufacturing). Industrial growth slowed in 1982/83 and remained subdued in the early part of 1983/84, due to world recession, weak domestic demand, supply bottlenecks--particularly in the power sector--and a textile strike. A strengthening in foreign demand, and in domestic demand on account of the improved agricultural performance, contributed to a revival of industrial production in the second half of 1983/84 and into 1984/85.

Investment showed little increase in relation to GDP over the period. The shortfall relative to the program target was due, in part, to a shortfall in public plan outlays on account of financial difficulties at the State level and in a number of public sector enterprises. Investment and production in power, coal, railways, and irrigation were particularly affected. 1/ Inadequate capacity expansion in the power sector initially reflected difficulties in project implementation, but more recently has stemmed from financial constraints arising from the

1/ Details on developments in key sectors during the Sixth Plan are provided in EBS/83/276 (12/30/83) and in the forthcoming paper on recent economic developments.

poor financial performance of State Electricity Boards. The accelerated oil development program was more successful than envisaged and contributed importantly to the lower current account deficit.

Additional resource mobilization efforts by the public sector were an important element of the adjustment program. The targets specified at the outset of the program were met. Higher than specified savings by Central Government public enterprises were partially offset by shortfalls in Central Government budget and State savings. However, additional public savings did not generate an equivalent increase in total domestic savings as had been hoped. Further, while savings of Central Government public enterprises were in excess of that specified, this reflected to a large extent the profits of the oil sector. 1/ Indeed, data on non-oil public enterprises available through 1982/83 indicate a rate of return on total capital substantially below market rates of interest. Notwithstanding the increase in public savings, financial resources in real terms fell some 30 percent below what was necessary to finance all Plan expenditures included in the Sixth Plan. The shortfall was particularly acute at the State level, partly because increased costs resulting from Central Government price adjustments were not passed on fully into higher prices. This has contributed to important investment shortfalls in electric power, coal, transportation, and irrigation. The Bank staff shares this observation.

4. Financial policies

The Central Government deficit increased relative to GDP over the program period, exceeding program estimates in both 1982/83 and 1983/84 (Table 1). The deficits of the consolidated Central and State Governments and of the public sector also rose (Annex I). Despite these trends, bank credit to the Government (including the Central and State Governments) was well within the program ceilings in both years, as higher deficits were more than offset by higher nonbank financing, predominantly from small savings and borrowing from the oil sector.

The higher Central Government deficit in 1982/83 was due to higher expenditures which were only partly offset by higher revenues and grants; outlays were bolstered by demands for disaster relief related to the drought and a strong growth in fertilizer subsidies. Higher revenues reflected increases in auxiliary import duties in November 1982 imposed in an effort to contain the budget deficit. Factors contributing to the higher deficit in 1983/84 were a revenue shortfall on account

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1/ The larger than expected profits of the oil sector resulted from a softening of international oil prices which, even after allowing for the depreciation of the rupee, led to a margin between the domestic sales price of petroleum products and their average cost including domestic taxes (see also footnote 4 to Table 7).

of tax concessions offered to stimulate the lagging industrial sector, higher current expenditures for fertilizer subsidies and wage adjustments, and higher capital expenditures and net lending.

Throughout the program the authorities pursued a monetary policy aimed at containing inflationary pressures of monetary origin. Interest rate policy was used with some flexibility, primarily to enhance the attractiveness of financial savings. There was little change in nominal rates after 1981/82, and real rates varied with changes in price expectations. In 1981/82, credit policies toward the commercial sector were tightened to keep total credit in line with program targets. However, the growth of credit weakened toward the end of the year, which, with the larger than expected contraction from the external sector, resulted in a growth of monetary aggregates that was somewhat below the program targets (Table 4). Again in 1982/83, a combination of cautious credit policies, particularly toward the end of the year, kept the increase in monetary aggregates within the revised program targets, despite the smaller than expected reduction in liquidity on account of the development of net foreign assets. Throughout 1983/84, the balance of payments was stronger than anticipated. To limit its effect on liquidity growth, several policy changes were made, including a two-step increase in the cash reserve ratio (CRR) from 7 to 8 percent in May and July 1983, a further increase to 8.5 percent in August. In November, refinance facilities for food credit were reduced and a 10 percent incremental cash reserve requirement was introduced. These measures and greater than projected nonbank financing of the Government kept the increase in total credit well within program targets. However, they were insufficient to offset the smaller contraction emanating from the external sector and the development of nonmonetary liabilities (net). 1/

5. Measures to improve efficiency

Despite numerous measures to make resource utilization more efficient, the continuing infrastructure bottlenecks, the poor financial performance of State enterprises (especially in the power sector and non-oil Central Government enterprises), high and rising incremental capital output ratios, and low capacity utilization indicate that much remains to be done. The persistence of these problems is recognized by the authorities in the approach underlying the Seventh Plan which aims at improvements in productivity as one of its priority objectives.

1/ In 1983/84 these liabilities rose by 2.5 percent, against a projected rise of 13-14 percent. More generally, the absence of details underlying the strong trend of rising other liabilities (net) necessarily adds some uncertainty to interpretation of developments in credit and monetary aggregates.

Table 4. India: Monetary Survey--Programs and Actuals, 1981-84 1/

(In billions of rupees)

	1981 March	1982 March		1983 March			1984 March		
	Program base	Original program	Actual	Original program	Revised program	Actual 2/	Original program	Revised program	Actual 2/
Domestic credit	621.26	741.81	739.58	877.56	876.79	868.56	1,030.26	1,013.21	1,003.48
	(24.6)	(19.4)	(18.9)	(18.3)	(18.6)	(17.4)	(17.4)	(17.8)	(15.5)
Net credit to Government	258.06	309.81	309.11	364.34	364.53	355.21	423.72	413.34	405.84
	(34.2)	(20.1)	(19.1)	(17.6)	(17.9)	(14.9)	(16.3)	(17.3)	(14.3)
Credit to the commercial sector	363.20	432.00	430.47	513.65	512.26	513.35	606.62	599.87	597.64
	(18.80)	(18.9)	(18.7)	(18.9)	(19.0)	(19.3)	(18.1)	(18.1)	(16.4)
Net foreign assets	46.82	30.07	26.61	...	9.01	15.22	...	0.74	15.95
Other liabilities	-114.94	-131.94	-141.31	...	-161.66	-160.19	...	-181.81	-164.11
Broad money (M_3)	553.14	639.94	624.88	732.73	724.14	723.59	835.31	832.14	855.32
	(18.5)	(15.7)	(12.7)	(14.5)	(15.9)	(15.8)	(14.0)	(15.0)	(18.2)
Narrow money	232.70	259.02	247.92	287.49	282.13	284.16	319.11	318.26	328.69
	(16.6)	(11.3)	(6.8)	(11.0)	(13.8)	(14.6)	(11.0)	(12.0)	(15.7)
Time deposits	320.44	380.92	376.96	445.24	442.01	439.43	516.20	513.88	526.63
	(19.3)	(18.9)	(17.0)	(16.9)	(17.3)	(16.6)	(15.9)	(16.9)	(19.8)

Source: Data provided by the Indian authorities.

1/ Figures in parentheses are percentage changes over 12 months.

2/ Adjusted for 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).

a. Industrial licensing and pricing policies 1/

A complex network of industrial regulations exists to promote investment in priority sectors, disperse industry throughout the country (particularly directing it to backward areas), develop the small-scale sector, prevent the concentration of monopoly power, and avoid investment that could lead to excess capacity. As part of this system, industrial investments above a certain level require official approval through the issue of an industrial license. While the Government has maintained its industrial policy objectives, the regulatory instruments were revised during the program, with a view to eliminating unnecessary restrictions and delays and improving industrial efficiency. A more flexible use of industrial pricing policies was also implemented to the same ends.

Major changes in industrial licensing policies in recent years are detailed in EBS/81/198, EBS/82/44, and EBS/83/276. These included the recognition of capacity in excess of endorsed limits (1980); introduction of automatic growth provisions enabling units to expand licensed capacity by 25 percent over five years; and a further liberalization of capacity and production constraints (1982), whereby approved capacity could be increased without procedural difficulty to 125 percent of licensed capacity, or 133 percent of the highest annual production level during the most recent five-year period, whichever was higher. Actual production could be 25 percent higher than approved capacity. Other measures included increases in the investment limit above which an industrial license is required; measures to speed up the granting of licenses; exemption of a number of industries from restrictions arising under the Monopolies and Restrictive Trade Practices Act (MRTP), freer access to foreign technology, particularly in the vehicles, oil field services, and electronics industries; and a provision enabling 100 percent export-oriented units to sell up to 25 percent of their output in the domestic market, although only against valid import licenses (which are not obtainable for a number of items produced by these units).

Prior to approval of the arrangement, administered prices were increased for a number of important products, including petroleum, and flexible pricing policies were pursued during the arrangement. Official controls on iron and steel prices were eliminated and a free market was established for part of cement production in 1982, while coal prices were increased in May 1982 and again in January 1984. Tariffs for railways, post and telegraph, and electricity were also increased.

b. Import liberalization

Liberalization measures were introduced in the annual import policy during each year of the program. These measures aimed mainly at

1/ A description of the industrial licensing system is contained in SM/84/15 (1/18/84), pp. 41-58.

increasing competition and reducing costs by providing better access to needed inputs, capital goods, and technology. Improved access was achieved by placing items in less restricted licensing categories and by simplifying licensing procedures. Particular emphasis was placed on measures designed to improve access to imported inputs by exporters.

An economically weighted assessment of these measures was presented in EBS/82/102 and EBS/83/130. These concluded that access to imports in 1983/84 would be increased by 30 percent following an increase of 21 percent in 1982/83, with relatively large increases in access to capital goods and consumption goods imports (Table 5). 1/ Despite the introduction of some measures, which worked in the direction of increasing protection of domestic industry, these assessments concluded that, in 1983/84, the overall level of protection afforded domestic industry declined.

Data that would permit Table 5 to be updated on the basis of actual licenses used and imports under OGL and through baggage clearance procedures are not available. 2/ Data on actual licenses issued show a decline over the period of the arrangement (although an increase over 1980/81). However, this trend is indicative of a decline in the percentage of imports subject to licensing and not of a tightening of import restrictions. 3/ Licensing data do reveal increases in capital goods licenses and import replenishment licenses (REP) available to exporters over the period of the arrangement. The increase in capital goods imports would be higher than indicated by licensing data, as a number of capital goods were moved to OGL. Preliminary data on non-oil, non-bulk imports (the category targeted by import liberalization measures) indicate a growth in volume of about 10 percent on average per annum over the period.

6. Exchange and payments system

The exchange rate system remained unchanged during the arrangement, with the rupee pegged to a basket of currencies within margins of 5 percent. Exchange rate policy was guided by the need to strengthen the balance of payments and to avoid a deterioration in external competitiveness. Broadly, an index of the real effective exchange rate indicates only relatively small deviations around the November 1981

1/ Access was measured as the sum in rupees of import licenses permitted under the import policy, estimated imports under OGL, imports of canalizing agencies and goods brought in through personal baggage.

2/ Data on licenses utilized are not recorded. Also, actual imports by license category are not available and imports through personal baggage are unrecorded except for that part subject to duty.

3/ During the last few years importers have been permitted to use automatic and supplementary licenses issued in previous years on a "repeat" basis. Use of these licenses does not require approval by licensing authorities and is not recorded in licensing data.

Table 5. India: Various Licenses Issued, Imports under OGL, and Total Non-oil Imports, 1980/81-1983/84

(In millions of rupees)

	1980/81	1981/82		1982/83		1983/84	
		Estimate	Revised Est.	Program	Revised	Program	Revised
Automatic licenses	7,386	11,400	10,543	13,720	11,272	17,090 1/	9,445
Supplementary licenses	2,551	3,270	3,706	3,990	3,542	4,600	2,940
REP licenses 2/	14,220	18,000	17,629	20,000	19,635	23,900 1/	22,945
Capital goods licenses	11,273	16,750	17,599	19,000	13,197	24,000 3/	18,670
Imports under OGL	...	5,850	...	9,000	...	15,200	...
Canalized agencies 4/	690	7,500	8,400	10,700	10,961,	12,720	12,967
Baggage clearance	...	3,570	3,750	3,750	...	6,500	...
Special clearance procedures for consumption goods	...	497	497	550	500	600	600
Total	...	66,837	...	80,710	...	104,610	...
(Percentage increase)				(20.8)		(29.6)	
Memorandum items:							
1. Total imports (excluding oil)	72,830	...	84,180	...	87,620	...	108,770
2. Licenses issued	53,404	...	77,553	...	71,657	...	70,303
(as percent of (1))	(73.3)	...	(92.1)		(82.8)		(64.6)
3. Residual 5/	19,426	...	6,627		15,963	...	38,467
(percentage increase)					(141.0)		(141.0)

Sources: Table 3, EBS/83/130 (Supplement 1), page 12 (classified by category of license instead of type of import); and data provided by the Indian authorities.

1/ Includes increase in effective value of licenses for use of Indian vessels.

2/ Includes imports of canalized items against REP licenses.

3/ Includes Rs 3,000 million allowance for automatic clearance of capital goods imports by the Chief Controller of Imports and Exports (CCIE).

4/ Excludes imports of canalized items against REP licenses (assumed to be 30 percent or REP licenses issued in revised estimated for 1981/82-1983/84 revised estimates).

5/ Includes imports under OGL, imports against automatic and supplementary licenses issued in previous years used on a repeat basis without need for further endorsements by the licensing authority, and other imports not requiring licenses.

level (Chart 4). India continued to avail itself of transitional arrangements under Article XIV, and bilateral payments arrangements with a Fund member (Romania) and four non-Fund members remained in effect. An expert committee on exchange control procedures was established in December 1982 and issued its report in December 1983. A number of its recommendations, including a simplification of procedures applicable to imports and exports and the delegation of certain powers previously held by the Reserve Bank to Authorized Dealers, have been adopted and others are under consideration. Steps also were taken to liberalize investment facilities and repatriation benefits for investments by nonresident Indians.

7. Cooperation with the World Bank

The World Bank staff collaborated closely with the staff in its work on the extended arrangement program. Bank staff participated in discussions with the authorities and their views were taken into account in formulating each of the three annual programs.

V. 1984/85: Prospects and Policies as Seen at Mid-Year

1. Prospects

The outlook for 1984/85 at mid-year is promising, though the rate of growth of real GDP will decline to some 4-5 percent, following the strong growth in output during 1983/84 (Annex I). Agricultural production is expected to rise by 2 percent, both on account of continued good weather and measures to increase productivity, including expanded use of fertilizer. Industrial output is expected to increase by 8 percent, with production up some 7 percent in the first four months over a year earlier; this rapid growth is made possible by the strong growth in demand stemming from the rise in agricultural incomes, but also by temporary alleviation of important bottlenecks in key sectors. Generation of electricity in the first six months rose by 14 percent because of especially satisfactory rainfalls which have increased the generation from hydroelectric plants, the coming on stream of new capacities, and improved maintenance. The coal supply situation has improved although quality continues to be a problem.

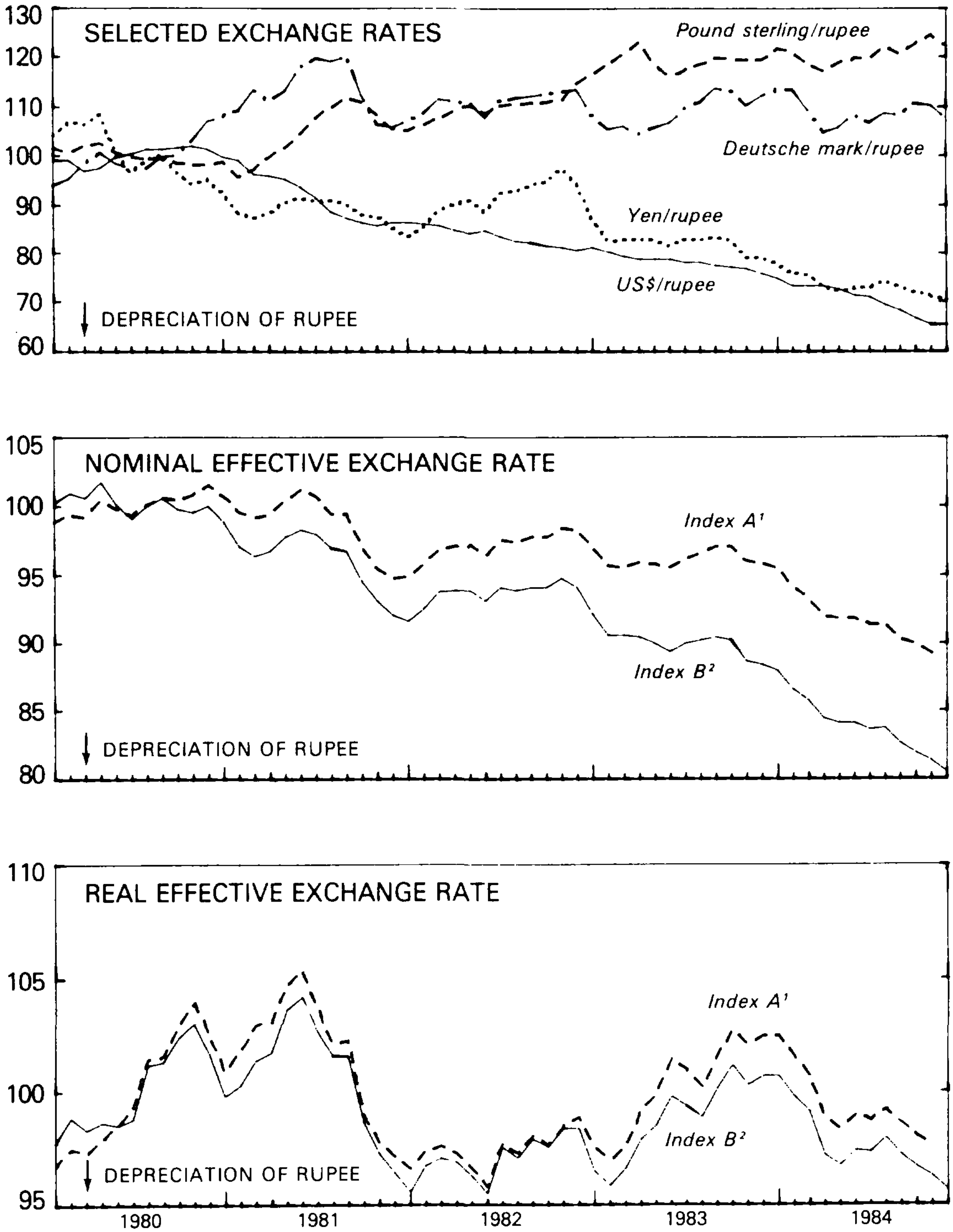
Price developments, of concern to the Executive Board at the time of the last consultation, have been varied during the first half of the year. Inflation, as measured by wholesale prices, decelerated to some 6-7 percent in May, but by mid-August had returned to year-on-year rates of 9 percent, notwithstanding a decline in foodgrain prices: major goods contributing to rising prices included sugar, tea, edible oils, and also manufactured goods. Following measures by the Government to increase the supply of key commodities--including the reintroduction of restrictions on tea exports--and to reduce certain administered prices,

CHART 4

INDIA

EXCHANGE RATE INDICATORS

(Indices: 1980 = 100)



Source: IMF, *IFS*; and staff calculations.

[1] The nominal effective exchange rate index is an export weighted index with weights for 33 of India's major trading partners; the real effective exchange rate index is the nominal effective exchange rate index adjusted for relative wholesale prices.

[2] The nominal effective exchange rate index is an export weighted index with weights for 4 of India's major trading partners. the real effective exchange rate index is the nominal effective exchange rate index adjusted for relative wholesale prices.

the rate of wholesale price increase has slowed to the 6-7 percent range.

The current account deficit is expected to remain constant in 1984/85 in percent of GDP: a stronger export performance--reflecting more buoyant growth in foreign markets and a carryover of exports from 1983/84 related to a port strike--will be largely offset by the upswing in non-oil imports associated with the growth in industrial production (Table 6). Workers' remittances are likely to weaken somewhat, offsetting further modest gains on the oil balance. The overall balance for the first six months was in small deficit but was expected by the authorities to shift into small surplus for the year as a whole. The staff projection for the year is for approximate overall balance, reflecting partly a somewhat less buoyant view regarding workers' remittances. Gross reserves rose during the first six months of 1984/85 to SDR 6.2 billion or 5 months of imports. 1/

2. Policies

Policy discussions focused on short-term issues relating to price developments, prospects for the fiscal balance, and liquidity growth. Longer-term issues included those of a structural nature affecting the efficiency of resource use in the economy and the rising trend of the government deficit. The need to pursue policies to strengthen public finances, adjust administered prices, provide adequate incentives for production, and strengthen general export incentives, continued to be of primary concern. The authorities restated their commitment to financial stability and were closely monitoring developments in the fiscal and monetary aggregates that could give rise to an untoward rate of inflation. For the longer term, the continued pursuit of adjustment policies was reaffirmed. Accelerated export growth was seen as essential to the maintenance of an adequate rate of overall growth and avoidance of excessive external borrowing. The authorities stated that increased domestic competition would be necessary if exports were to be competitive in world markets but stressed that, in designing policies, the small share of exports in GDP had to be taken into account.

In a speech following the recent elections, the Prime Minister has indicated that a major review of policies is being undertaken. Improvements in productivity, absorption of modern technology and fuller utilization of capacity are to be major objectives. A review of foreign trade policies is underway; the objective is to give a fresh impetus to exports. Reforestation and diminished water and air pollution were also identified as areas commanding priority for early action.

1/ India has gold holdings of 8.594 million fine troy ounces, which are valued in Fund calculations at SDR 35 per ounce.

Table 6. India: Balance of Payments, 1980/81-1984/85 1/

(In millions of SDRs)

	1980/81	1981/82	1982/83	1983/84 Prov.	1984/85 Staff Forecast
Exports, f.o.b.	6,479	7,324	7,581	7,894	8,965
Imports, c.i.f.	-12,359	-13,271	-13,069	-13,265	-14,244
Oil	-5,188	-4,840	-4,219	-3,306	-3,240
Non-oil	-7,171	-8,431	-8,850	-9,959	-11,004
Trade balance	-5,880	-5,947	-5,487	-5,371	-5,279
Net invisibles	3,750	3,321	2,931	2,571	2,400
Nonfactor services	1,115	923	917	1,000	1,050
Investment income 2/	411	241	-387	-729	-850
Private transfers	2,224	2,157	2,401	2,300	2,200
Current account balance	-2,130	-2,626	-2,556	-2,800	-2,879
(in percent of GDP)	(1.7)	(1.8)	(1.6)	(1.6)	(1.6)
Net aid	1,384	975	1,579	1,495	1,717
Loans	952	689	1,257	1,217	1,470
Grants	432	286	322	278	247
Commercial borrowing	91	80	334	499	859
bilateral arrangements	-73	-280	-333	183	214
Nonresident deposits	113	155	542	792	683
Other capital	-35 3/	-297	370 4/	-370 4/	--
Errors and omissions	-194	-179	-1,200	-347	-594
Overall balance	-774	-2,172	-1,143	-373	--
Monetary movements	774	2,172	1,143	373	--
Net use of Fund credit	266	600	1,800	1,234	67
Reserves (increase -)5/	508	1,572	-657	-861	-67
Conversion rate: rupees/SDR	10.150	10.295	10.526	10.914	11.660

Sources: Reserve Bank of India, Bulletin; data provided by the Indian authorities; and staff estimates.

1/ Current account data for 1980/81-1982/83 are official balance of payments estimates, based on exchange record data, published by the Reserve Bank of India; capital account data for these years have been provided separately by the Indian authorities. Data for 1983/84 are staff estimates based on provisional data provided by the Indian authorities; estimates for exports and imports are based on provisional trade statistics and are therefore not strictly comparable to the exchange record data for earlier years.

2/ Includes staff estimates of interest on nonresident deposits.

3/ Includes SDR allocation of SDR 120 million.

4/ Short-term bridging loan.

5/ Excluding changes in reserves due currency revaluations.

a. Fiscal policy

The budget document for 1984/85 foresaw a deceleration in the growth of revenues by 3 percentage points, and of expenditures and net lending by 6.5 percentage points. Thus, the budget deficit of the Central Government was expected to decline from 7.5 percent in 1983/84 to 6.9 percent of GDP (Table 7). The consolidated deficit of the Central and State Governments was to decline from 11 percent of GDP to 10 percent (Annex I). The main revenue features of the Central Government budget were the further increase by 5 percentage points of the auxiliary import surcharge (bringing the total increase in these duties to 20 percent over the last three years) and an assumption of greater compliance with tax regulations associated with a reduction in personal income tax rates. The share of tax revenues collected by the Central Government and allocated to States was to increase, reflecting in part the difficult financial situation faced by many States. Plan expenditures were to rise by 17 percent, against a rise in non-Plan expenditures of 5-6 percent.

At the time of the consultation discussions, the authorities were in the process of reviewing budgetary developments during 1984/85 and were not in a position to provide the staff with comprehensive revised estimates. However, they noted a number of factors that would increase the Central Government budget deficit by Rs 6 billion (or from 6.9 percent to 7.2 percent of GDP). These included lower than projected tax revenues, higher expenditures on account of the fertilizer subsidy, cost of living increases not provided for in the budget, supplementary provisions for Plan expenditures as well as additional loans to States (representing their mandated share of higher than budgeted small savings receipts).

Bank financing of the Central and State Governments during the first half of 1984/85 suggested that the increase in the consolidated deficit could be substantially larger than initially projected; by end-September, credit to Government had risen by Rs 48 billion against an unofficial target increase for the year as a whole only somewhat larger than the increase of Rs 58 billion during 1983/84. The authorities were concerned at the sharp increase in credit to Government although they stressed that it was subject to important short-term fluctuations and that Reserve Bank credit to Government showed a more moderate increase. Nevertheless, ministries and States had been cautioned by the Minister of Finance to adhere to the expenditure limits laid out in the 1984/85 budget. The budget review underway would identify whether expenditures were out of line. The authorities indicated that restraining measures would be implemented, if necessary, so that the demand for credit by the Government would not jeopardize monetary and price objectives.

With regard to the size of the public sector and the overall public sector deficit, the staff noted that not only did there seem to be a

Table 7. India: Summary Operations of the Central Government, 1980/81-1984/85

	1980/81	1981/82	1982/83	1983/84 Budget estimates	1983/84 Estimated outturn	1984/85 Budget estimates
			(In billions of rupees)			
1. Total revenue and grants	128.3	155.7	180.9	206.3	207.1	240.2
1.1. Tax revenue	93.9	115.7	130.6	154.9	154.5	175.3
1.2. Nontax revenue	30.7	36.8	47.4	47.8	49.5	61.6
1.3. Foreign grants	3.7	3.2	3.0	3.5	3.1	3.3
2. Total expenditure and net lending	211.5	242.5	306.0	315.7	349.0	386.3
2.1. Current expenditure	136.0	158.7	193.5	224.2	232.4	263.4
a. Plan	(27.4)	(30.0)	(37.9)	(45.1)	(47.0)	(56.7)
b. Non-Plan	(108.6)	(128.7)	(155.6)	(179.1)	(185.4)	(206.7)
2.2. Capital expenditure and gross lending	90.7	104.6	146.3	124.2	155.3	162.0
a. Plan	(63.3)	(72.5)	(81.2)	(83.5)	(94.0)	(108.0)
b. Non-Plan	(27.4)	(32.1)	(65.1) 1/	(40.7)	(61.3) 2/	(54.0)
2.3. Less: Loan repayments	-15.2	-21.7	-33.7	-32.7	-38.7	-39.1
3. Overall deficit	-83.2	-86.8	-125.1	-109.4	-141.9	-146.1
4. Net external financing	13.4	10.3	13.5	16.1	16.3	17.9
Gross	17.3	14.5	17.9	20.6	20.9	22.6
Repayments	3.9	4.2	4.4	4.5	4.6	4.7
5. Net domestic borrowing	69.8	76.5	111.6	93.3	125.6	128.2
5.1. Net market borrowing	25.8	29.1	37.7	40.0	40.0	41.0
5.2. Small savings and provident funds (net) 3/	20.0	24.7	31.4	28.8	36.5	38.5
5.3. Special bearer bonds	0.9	8.8	--	--	--	--
5.4. Capital investment bonds	--	--	0.8	2.0	0.6	0.6
5.5. Miscellaneous deposits (net) 4/	-2.6	--	7.7	5.6	30.0	30.5
5.6. Official deficit financing 5/	25.7	13.9	34.0 1/	15.5	18.5 2/	17.6
Of which: State investment in Treasury bills	(-4.0)	(-3.3)	(1.9)	(...)	(...)	(...)
6. Memorandum items:						
6.1. Defense capital expenditure	3.3	4.8	5.3	6.1	6.0	7.2
6.2. Budgetary savings excluding foreign grants (1.1+1.2-2.1b-6.1)	12.7	19.0	17.1	17.5	12.6	23.0
6.3. Bank financing	50.6	39.2	35.7	...	45.8	...
			(In percent of GDP)			
Overall deficit	6.5	5.8	7.6	6.1	7.5	6.9
Bank financing	4.0	2.6	2.2	...	2.4	...

Sources: Budget at a Glance and Explanatory Memorandum on the Budget of the Central Government for 1984/85; Budget of the Central Government for 1984/85; and data provided by the Indian authorities.

1/ Includes Rs 17.4 billion in loans to the States to absorb their outstanding overdrafts with the Reserve Bank of India as of March 31, 1982.

2/ Includes Rs 4.0 billion in loans to the States to absorb outstanding overdrafts with the Reserve Bank of India as of March 31, 1983.

3/ Includes small savings funds on-lent to the States.

4/ Includes lending by the oil sector through deposits of surplus funds with the Government; the amounts involved are Rs 3 billion in 1982/83, Rs 11 billion in the Revised Estimates for 1983/84, Rs 12 billion in the Estimated Outturn for 1983/84, and Rs 10 billion in the Budget Estimates for 1984/85.

5/ Deficit financing as officially defined includes net issues of Treasury bills and use of cash balances.

rising trend of expenditure and deficit relative to GDP, but that the size of the deficit indicated that the public sector was absorbing a large share of the savings available to the economy (Chart 5). It was imperative that these savings be efficiently used, and also that adequate allowance be made for the credit needs of the private sector. The authorities did not think that the size of the public sector should give rise to concern in the Indian context, where responsibility for more than three fourths of the nonhousehold investment was with the public sector and social objectives played an important role in economic decision making. Also, a part of public expenditure reflected transfers to financial institutions to support private investment. In their view, the size of the overall deficit was not excessive and the savings and financial resources available to the private sector were adequate. It was agreed, however, that the efficient use of resources in the public sector and throughout the economy was of crucial importance for sustaining higher growth and enhancing competitiveness. Strategies to increase efficiency were under intensive review in preparation for the Seventh Plan. The authorities also indicated that greater attention would be given in the next Plan to financial returns achieved by public enterprises. In this regard, the staff noted that inadequate cost recovery or financial returns from public investments could place an undue burden on the tax system to attain public sector resource mobilization requirements.

b. Credit and monetary policies

The growth of liquidity in 1983/84 substantially exceeded the targets established under the program, though the limits on credit to the Government and on total bank credit were observed. The credit policy announcement for May-October 1984 noted the need to reduce the growth of overall liquidity to dampen inflationary expectations while providing adequate credit for the support of productive activities. To these ends the statutory liquidity ratio was increased from 35 to 35.5 percent effective July 28, 1984 and to 36 percent on September 1, 1984. The impact of these measures on bank liquidity was to have been moderated at the beginning of the busy season by the phased release of certain impounded cash balances held by the banks with the Reserve Bank of India (RBI). In the event, liquidity growth continued to be strong at 16-17 percent, and it was decided in September to postpone the release of the cash balances by a month.

The busy season credit policy, announced in late-October 1984, for the following six months again noted the objectives of reducing liquidity growth while at the same time providing the credit necessary for productive activities. Measures were announced at that time to reduce bank liquidity by an estimated Rs 5 billion (about 0.5 percent of broad money). The ceiling above which 100 percent refinancing was available to banks was raised by Rs 3 billion to Rs 43 billion for food credits, while refinancing of export credits was limited to 100 percent of the increase over the monthly average for 1983. It was hoped that the demand for credit from the government sector would moderate, and that liquidity growth would be brought down to 15 percent by March 1985.

Shortly after the announcement of the credit policy for the busy season, the interest rate banks were permitted to charge for food credits was raised from 12.5 percent to 14 percent, effective retroactively to the first of October, while the interest rate received on holdings of cash reserve requirements with the RBI in excess of the initial 3 percentage points of required reserves was raised by 1 percentage point to 10 percent. These measures will strengthen somewhat the financial position of banks which has been adversely affected by high operating costs, prescribed lending at preferential rates, and nonperforming loans. Measures are also under consideration to make operation of the banking system more efficient, including introduction of computers for selected operations and record keeping.

c. Trade and industrial policies

The authorities indicated that their major objectives in the Seventh Plan were to increase food supplies and employment and improve productivity. Given the rising effective cost of foreign savings and the limited opportunities to increase the already high domestic savings ratio, the need to increase efficiency took on additional urgency. Increased efficiency and domestic competitiveness were also seen by the authorities as prerequisites for achieving a marked improvement in export performance. A number of expert committees had been established to examine ways of increasing efficiency. One committee, in particular, was focusing on possibilities for increasing reliance on financial/fiscal instruments in lieu of physical controls on trade and industry, but its report was not expected to be ready until early 1985/86. Recommendations were also expected on measures to increase the financial responsibility of public sector undertakings.

The authorities explained that the industrial licensing system increasingly had been managed in a manner to strengthen competition between domestic units of production. They expected the recent merger between the Department of Company Affairs and the Ministry of Industry to reduce licensing delays, notwithstanding a recent amendment to the MRTP Act which would subject a larger number of firms to more time-consuming and restrictive licensing procedures. Special one-window clearance facilities had been set up for specific sectors, particularly to facilitate licensing in cases where foreign collaboration was being sought. So far, however, this facility had not been used extensively. Directives had been issued denoting the maximum acceptable delay in the processing of applications for industrial licenses. This had been followed by a significant reduction in the time taken to obtain a license.

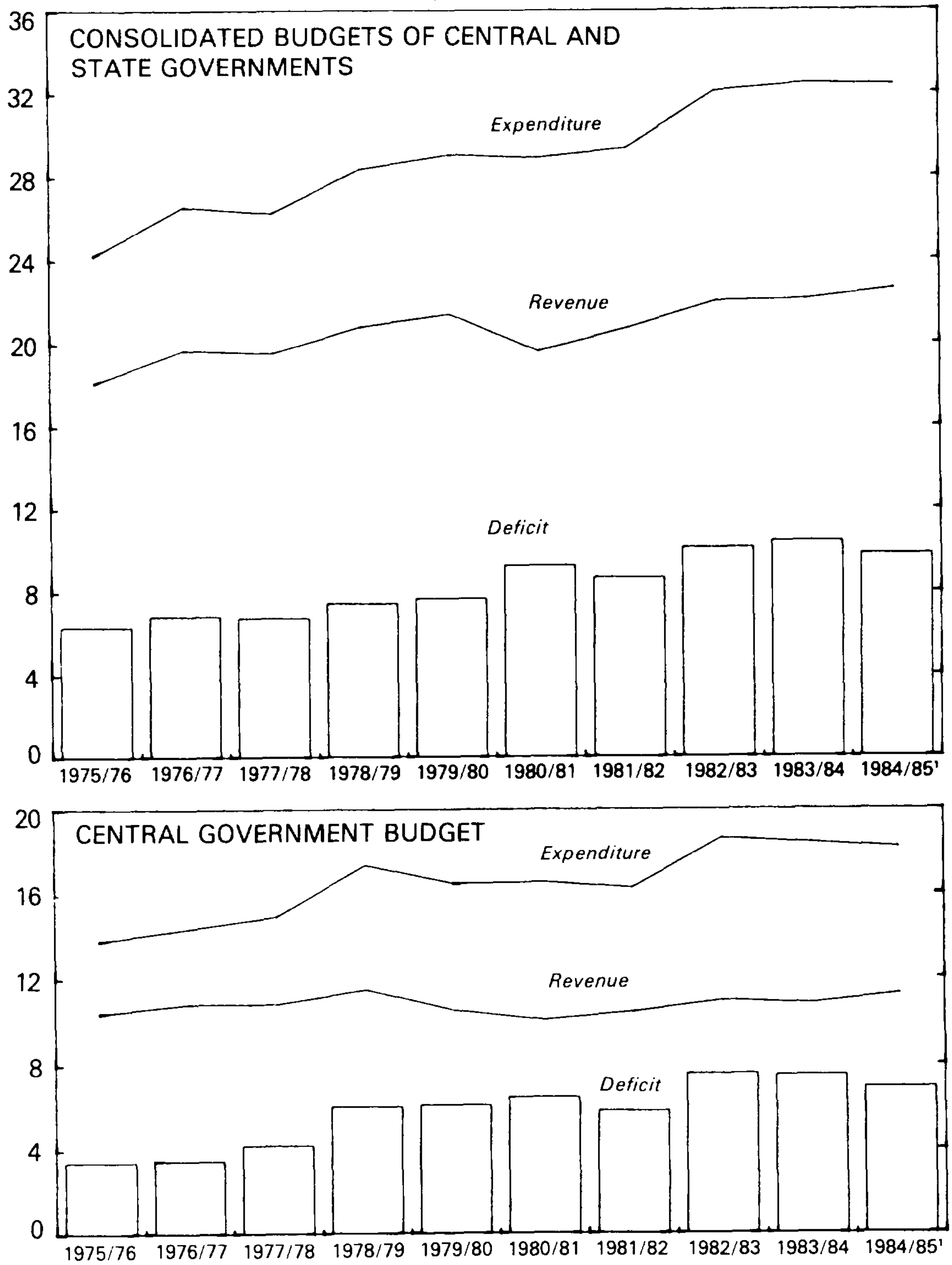
Decisions had recently been taken to allow private investment in areas formerly reserved for the public sector, and even to eliminate

CHART 5

INDIA

BUDGETARY DEVELOPMENTS

(In percent of GDP)



Sources: *Budget of the Central Government*, and data provided by the Indian authorities.

[1] Budget estimates.

licensing for firms, irrespective of size, for production of specific products (e.g., micro and mini computers). The electronics and computer industries had also recently been given special incentives to expand production by a very substantial reduction in customs duties for imported inputs, irrespective of whether the end-products were exported or sold domestically. The small-scale reservation list was reviewed from time to time to ensure that the costs in terms of foregone economies of scale were not excessive. However, there had been no change in the capacity limit (Rs 200 million) above which industrial licensing procedures applied.

The Import/Export Policy for 1984/85 announced in April basically represented a continuation of the previous policy. Some further simplification in procedures was introduced and access by exporters to imported inputs further increased. Special incentives are to be given to promote exports of products with high domestic value added, as well as exports of new products and the development of new markets. Changes were also made in the licensing classification of items, with a number of raw materials and components being moved off OGL on to more restricted lists and a larger number of capital goods being made available on OGL. In response to the staff's observation that the 1984/85 policy did not constitute a further significant move toward liberalization, the authorities stressed that substantial efforts had been required to withstand protectionist pressures from domestic industries. With regard to auxiliary import duties, which were increased again in the 1984/85 budget, it was indicated that these were largely a revenue device, although such increases did assist in withstanding pressures to further restrict imports through licensing.

The authorities stated that India's trade framework, with a large portion of exports being sold by exporters or trading houses and a large portion of imports being obtained through distinct canalization agencies, did not lend itself to countertrade. Regarding bilateral trade and payments arrangements, the authorities were not in a position to indicate any time frame for the elimination of the bilateral payments agreement with Romania. The present agreement is due to lapse in December 1985.

d. Balance of payments financing and exchange rate policy

The authorities continued to feel that foreign commercial borrowing should be approached cautiously; it should be project-related and not undertaken for general balance of payments support. Debt servicing in excess of 20 percent of current receipts was considered excessive, and cautious import management would be pursued, if necessary, to avoid an undue buildup of external liabilities that could give rise to such a burden.

The role foreseen by the authorities for the use of exchange rate policy in the Indian context was limited. Exchange rate policy was only one of the instruments that could be used to strengthen the external balance and should be used in a coordinated approach as other nonprice barriers to competitiveness were reduced. The staff noted the recent depreciation of the rupee in real effective terms. By October 1984 the real appreciation that had taken place in early 1983/84 had been offset, restoring the real rate to its level of November 1981. The staff noted that exchange rate policy and import liberalization should play a more central role in fostering a competitive domestic economy, a development that was seen as necessary to achieve the needed strengthening of export performance.

VI. Medium-Term Prospects and Projections

Three medium-term scenarios are presented in Table 8. These indicate the challenge facing Indian policymakers over the coming years in sustaining the satisfactory economic growth recently attained, holding debt service to below 20 percent of current receipts, and maintaining reserves at about four months of imports.

Scenario A is based on the assumption of a 2 percent per annum gain in export market shares. Thus, exports in real terms are projected to increase by 7 percent in relationship to the growth of foreign markets of 5 percent--a strengthening in the export elasticity with respect to market growth from appreciably less than 1 over the last five years to 1.4. Such an achievement is seen by the authorities as requiring a very substantial effort and is difficult to anticipate on the basis of disaggregated commodity projections. Imports in real terms are projected to grow at 6 percent per annum, one percentage point faster than the projected rate of growth of real GDP. The authorities stated that this would imply some reduction in the historical elasticity between imports and GDP. Under this scenario, with commercial borrowing determined endogenously to close the financing gap, the debt service ratio would increase to 20 percent (including servicing on nonresident Indian accounts) by 1988/89 and reserves would decline to less than 4 months of imports.

Scenario B is based on the observed historical relationship between exports and market growth, with all other assumptions the same as in scenario A. Commercial borrowing is also determined endogenously to close the financing gap. Under this scenario, gross commercial borrowing would rise to almost $8 billion by 1989/90, and the debt service ratio, including interest paid on nonresident Indian deposits, to 24 percent. Finally, scenario C is constructed so as to keep the debt service ratio from exceeding 20 percent. Import volume growth is determined endogenously and is limited to 3 percent per annum. This rate of growth is likely to prove insufficient to attain the authorities' growth objectives, unless a further reduction in oil imports could be achieved or non-oil imports could be replaced by efficiently produced domestic goods on a larger scale than in the past.

Table 8. India: Medium-Term Debt Projections

	1985/86	1986/87	1987/88	1988/89	1989/90
	(In millions of U.S. dollars)				
Exogenous inputs: 1/					
Balance on					
Services	1,130	2,294	1,238	2,547	1,384
Transfers	2,115	2,235	2,446	2,671	2,912
Concessional loans, net	1,682	1,900	2,091	2,192	2,234
IMF transactions	-198	-43	-727	-860	-753
	(In percent)				
Export market growth	5.0	5.0	5.0	5.0	5.0
Increase in export unit values	1.4	4.9	7.5	7.5	7.5
Increase in import unit values	1.2	3.8	7.5	7.5	7.5
Scenario A:					
Export volume growth	7.0	7.0	7.0	7.0	7.0
Import volume growth	6.0	6.0	6.0	6.0	6.0
Debt service burden, including nonresident accounts	16.6	18.2	19.3	20.2	20.0
Debt service burden, excluding nonresident accounts	14.8	16.5	17.8	18.9	18.9
Reserves in months of imports	4.7	4.3	3.8	3.3	2.9
Gross borrowing on commercial terms ($ bn.)	1.4	2.2	2.9	3.9	5.0
Total external debt ($ bn.) 2/	30.8	33.9	37.7	42.3	47.8
Scenario B:					
Export volume growth	4.0	4.0	4.0	4.0	4.0
Import volume growth	6.0	6.0	6.0	6.0	6.0
Debt service ratio, including nonresident accounts	17.0	19.2	21.0	23.1	24.3
Debt service ratio, excluding nonresident accounts	15.1	17.4	19.5	21.7	23.1
Reserves in months of imports	4.7	4.3	3.8	3.3	2.9
Gross borrowing on commercial terms ($ bn.)	1.7	2.8	4.1	5.8	7.8
Total external debt ($ bn.) 2/	31.1	34.9	39.9	46.3	54.5
Scenario C:					
Export volume growth	4.0	4.0	4.0	4.0	4.0
Import volume growth	3.0	3.0	3.0	3.0	3.0
Debt service ratio, including nonresident accounts	16.9	18.8	20.0	21.1	20.8
Debt service ratio, excluding nonresident accounts	15.04	17.04	18.5	19.7	19.5
Reserves in months of imports	4.8	4.5	4.1	3.7	3.3
Gross borrowing on commercial terms ($ bn.)	1.4	1.8	2.3	3.0	3.6
Total external debt ($ bn.) 2/	30.7	33.5	36.7	40.4	44.5

Source: Staff estimates.

1/ Entries for non-interest services, transfers and concessional aid flows are invariant across the scenarios, as are the terms for commercial borrowing, and price assumptions for exports and imports. Market growth for India is based on WEO assumptions and is projected at 5 percent per annum. The interest rate for new dollar borrowings declines from 10 percent in 1985 to 8.5 percent in 1990, with a grace period of three years followed by a repayment period of seven years.

2/ Excluding nonresident deposits, which are estimated to total approximately $3.1 billion at end-March 1985; the projections allow for only a small increase in such liabilities.

It must be emphasized that these scenarios are illustrative. They are dependent on base period values that are surrounded by considerable uncertainties and are extremely sensitive to assumptions about elasticities, developments in world inflation, and the terms and conditions of credit. However, they do illustrate the importance of putting in place as soon as possible policies to enhance the competitiveness of domestic products and to achieve a more dynamic export performance. The alternatives would lie in the direction of reverting to intensified import restraint (with attendant implications for economic growth) or potentially excessive accumulation of external debt. The authorities indicated their firm determination to avoid the latter course of developments. With regard to the role of foreign direct investment, the authorities indicated that it should be viewed primarily as an important means to facilitate the transfer to technology. It was not seen as an important source of financing the current account deficit.

VII. Staff Appraisal

The policy program supported by the extended arrangement was aimed at establishing the medium-term viability of the balance of payments while also increasing the rate of economic growth and reducing inflation. A principal focus was to achieve a broad measure of structural adjustment in the wake of the second oil shock and the sharp deterioration in the terms of trade. Investment programs, within the framework of the Sixth Plan, were oriented toward alleviating infrastructural bottlenecks, especially in core sectors, and intensifying domestic resource mobilization efforts to provide a higher degree of internal financing. The need to improve the efficiency of resource use was recognized; pricing, import, and industrial policies were oriented to support this objective. Exchange rate policy was to be implemented consistent with these objectives, as well as to strengthen export performance, shifting the relative profitability of production for home and export markets in favor of the latter. Financial support from the Fund augmented continuing strong official capital flows and enabled the adjustment process to move forward deliberately, but without requiring the speed of adjustment to be disruptive.

The important objectives relating to higher economic growth, reducing inflation, and avoiding a deterioration in the balance of payments on current account in relation to GDP appear to have been substantially achieved. The larger than expected amelioration of the burden of net imports of petroleum through intensified exploration and development of domestic petroleum resources was particularly notable. All performance criteria were observed throughout the program period. In these respects, the program can be judged to have been successful. This assessment must be tempered by recognition that export performance was much weaker than expected; this partly reflected weakness in the world economy, but the longer-term relation between export volume and market growth has continued to decline.

Somewhat stronger capital inflows and diminished pressure on the current account obviated the need for use of SDR 1.1 billion of resources available under the extended arrangement while maintaining adequate gross reserves. However, by the end of 1983/84, the burden of external debt service had risen considerably above the program forecast of 14 percent of current account receipts. This reflects a combination of factors including the weaker export performance and somewhat larger capital inflows on less concessional terms. The issues underlying the unexpectedly rapid rise in the debt service burden remain to be addressed more vigorously during the remainder of the decade if India is to sustain the momentum of economic growth recently achieved.

The strong recovery of agricultural production in 1983/84 and of industrial output during the latter part of that year has contributed to sustaining momentum in the economy in 1984/85. Foodgrain production is expected to surpass the record 152 million-ton crop of 1983/84 and industrial production is rising at about 8 percent. Strong growth in electricity generation has facilitated economic growth in 1984/85. Price pressures which re-emerged in 1983/84 have abated somewhat. Nevertheless, the increase in wholesale prices is expected to be about 8 percent in the current year, a rate of increase considerably above that prevailing in India's major trading partners. Inflationary pressures pose particular problems in the Indian economy: in adjusting administered prices to maintain production incentives and profitability; in preventing industrial licensing from becoming more restrictive where size limits are expressed in nominal value terms; and in achieving the necessary strengthening of incentives for exports.

The fiscal outlook during the current year could only be assessed through developments in net bank credit to the State and Central Governments. From this perspective, the degree of expansion during the first half of 1984/85 indicates that budgetary implementation is substantially more expansionary than anticipated when the budget was approved. The staff attaches considerable importance to the fiscal review initiated in November and to the authorities' continuing commitment to cautious financial policies. In this regard, the notices to spending ministries should signal the need for avoiding excessive expenditure growth until a more comprehensive assessment of current fiscal developments is possible and appropriate supplementary measures put in place to arrest the untoward growth in bank credit to the Government.

Recent adjustments in monetary policy reflect the authorities' aim to reduce the rate of growth of monetary expansion to 15 percent by March 1985. The staff attaches considerable importance to achieving such a slowing of growth in total liquidity. The expansionary pressures emanating from fiscal operations of the States and Central Government pose the most important challenge for reducing monetary expansion. The staff notes the special role played by the banking system in mobilizing financial resources and, through the statutory liquidity ratio, allocating a large part to the Government. However, India's industrial and export growth prospects depend importantly on the performance of the private sector. Adequate access to the savings of the economy will be important for sustained growth in the private sector.

Sustaining the rate of economic growth recently achieved will require strengthening key elements of the adjustment strategy pursued in recent years. The staff believes that policies to enhance competition in the domestic economy and to raise the productivity of investment must be strengthened. This is recognized in the strategy being defined for the Seventh Plan. Further liberalization of import and industrial policy, within the framework of shifting policy instruments away from administrative controls toward macroeconomic management and financial incentives, would be appropriate.

The present medium-term outlook for the balance of payments, including developments in the capital account, the growth of external debt, and the burden of debt servicing is not to be viewed with equanimity. Export performance must be improved considerably. Resource use in the Indian economy must become more efficient. In the view of the staff, this latter goal could best be pursued through a reduction in the role of direct interventions through administrative procedures and an appropriate stance of macroeconomic policies; and much greater emphasis should be given to strengthening financial performance of public enterprises. Recognizing the important role that further import liberalization must play, a more active use of exchange rate policy for the rupee would be appropriate. Such a policy should be aimed at shifting relative prices in favor of exports and efficient import substitution so as to avoid undue pressure on the balance of payments over the medium term.

The present burden of external debt service is not excessive. However, the sharp rise in the debt service ratio since 1980/81 must be moderated. Although interest rate developments may prove more favorable in the period ahead, the effective cost to India of external resources will increase as greater recourse to foreign savings on commercial or semi-commercial terms becomes necessary. Thus, the prognosis for sustaining higher rates of economic growth will only become favorable if India's export performance is strengthened. Import substitution will also have a role to play, but historic trends do not suggest that it would be a sufficient strategy to realize higher rates of economic growth with sustained external stability.

The timeliness, and for some series, the quality of the statistical base makes it difficult to monitor current economic developments in any but the narrowest terms, namely, in terms of movements in prices, credit to the Government, and foreign exchange reserves. The strong growth in unspecified monetary liabilities creates uncertainties for interpretation of movements in key monetary and credit aggregates. Were there to be a move toward greater reliance on financial incentives and on macroeconomic policy instruments, a broader and more current overview of developments would be imperative. The staff was informed of and welcomes the move toward the computerization of selected operations in the banking system, with implications for ultimately strengthening certain aspects of banking statistics.

In the close-to-four-decade period since independence, India has made remarkable economic progress in several respects. The achievement of self-sufficiency in foodgrains, the rapid development of petroleum production in recent years, the development of a diversified industrial sector and of the relevant infrastructure, and the spread of technical education are among the creditable achievements. Yet there is no gainsaying that the rich resource potential of the Indian economy could be more fully and vigorously tapped than has been done so far. The staff and authorities are in agreement on the importance of achieving higher economic growth with a sustainable balance of payments. What needs to be done in various sectors of production and distribution to achieve these goals may be diverse in detail but there is an underlying common theme: the promotion of efficiency and international competitiveness. The present affords a unique opportunity to make a new beginning in this respect. The objectives outlined in the recent statement by the Prime Minister indicate also a convergence of views around this theme.

It is recommended that the next Article IV consultation with India be held on the standard 12-month consultation cycle.

VIII. Proposed Decision

The following draft decision concluding the 1985 Article IV consultation with India is proposed for adoption by the Executive Board:

1. The Fund takes this decision relating to India's exchange measures subject to Article VIII, Section 2, and in concluding the 1985 Article XIV consultation with India, in the light of the 1985 Article IV consultation with India conducted under Decision No. 5392-(77/63), adopted April 29, 1977 (Surveillance Over Exchange Rate Policies).

2. The restrictions on the making of payments and transfers for current international transactions described in SM/85/... are maintained by India in accordance with Article XIV, except that the restriction arising under the remaining bilateral payments agreement with a Fund member is subject to approval under Article VIII, Section 2. The Fund encourages the authorities to terminate the bilateral payments agreement with a Fund member as soon as possible and to further simplify the exchange system.

India: Basic Data 1/

Area: 3.27 million sq. kms.
Population/population growth: 738 million (September 1983 estimate)/2.2 percent
Nominal GDP (1983/84) SDR 173.0 billion; (SDR 234.5 per capita)
Exchange rate: rupees per SDR: Rs 12.205 per SDR (on December 31, 1984)

	1980/81	1981/82	1982/83	1983/84 Prel. actual	1984/85 Staff forecast 2/
	(Annual percent change, unless otherwise specified)				
National income and price					
Real GDP at market prices	6.8	5.9	2.6	8.0	4.5
GDP deflator	11.4	10.2	7.8	7.0	7.0
Consumer prices (period average)	11.4	12.5	7.8	12.6	8.0
Wholesale prices (period average)	18.2	9.3	2.6	9.5	8.0
Industrial production	4.0	8.6	3.9	5.5	8.0
External sector (on the basis of SDRs)					
Exports, f.o.b.	7.1	11.8	0.4	6.4	13.6
Imports, c.i.f.	41.6	5.3	-2.8	4.7	7.4
Non-oil imports, c.i.f.	28.0	13.8	1.7	19.7	10.5
Export volume	-0.8	3.5	-2.9	1.9	7.0
Export market growth	2.2	5.9	0	5.5	8.6
Import volume	15.8	-4.9	-5.1	8.5	5.3
Terms of trade (deterioration, -)	-11.7	-2.4	1.0	8.2	4.1
Nominal effective exchange rate (depreciation, -) (period average)	0.2	-4.3	-2.0	-4.8	... 3/
Real effective exchange rate (depreciation, -) (period average)	5.6	-1.4	-2.2	2.6	-2.9 4/
Central Government budget					
Revenue and grants	13.1	21.4	16.2	14.5	16.0
Total expenditure	19.3	14.7	26.2	14.1	10.7
Current expenditure	13.1	16.7	21.9	20.1	13.3
Capital expenditure and net lending	32.5	9.8	35.8	3.6	5.4
Money and credit (end-period)					
Domestic credit	22.3	19.8	17.6	16.3	17.7 5/
Government	28.6	21.9	15.3	16.6	19.6 5/
Private sector	18.3	18.4	19.2	16.1	16.3 5/
Money and quasi-money	18.3	12.8	16.7	17.5	16.2 5/
Velocity (GDP relative to M_3) average	2.3	2.4	2.3	2.2	2.2
Interest rate (annual rate, three-year savings deposit)	8.5	10.0	11.0	11.0	11.0

India: Basic Data (Concluded)

	1980/81	1981/82	1982/83	1983/84 Prel. actual	1984/85 Staff forecast 2/
			(In percent of GDP)		
Gross domestic investment	24.6	24.7	24.1	25.0	25.0
Gross domestic savings	23.0	22.6	22.4	23.6	23.8
Consolidated deficit of State and Central Governments	9.3	9.0	10.3	10.6	10.0
Central Government budget deficit	6.5	5.8	7.6	7.5	6.9
Foreign financing	1.1	0.7	0.8	0.9	0.8
Tax revenue	7.4	7.8	7.9	8.3	8.2
Central Government expenditure	16.6	16.3	18.6	18.6	18.0
External current account deficit 6/					
Excluding grants	1.7	1.8	1.6	1.6	1.6
Including grants	1.4	1.6	1.4	1.5	1.5
External debt (including IMF)	11.8	12.2	14.2	14.7	15.8
Debt service ratio (in percent of current receipts) 6/	9.0	9.9	12.1	15.3	15.6
Interest payments (in percent of current receipts) 6/	3.4	3.9	6.1	8.7	8.8
	(In millions of SDR, unless otherwise specified)				
Exports	6,479	7,324	7,581	7,894	8,965
Imports	12,359	13,271	13,069	13,265	14,244
Oil imports	5,188	4,840	4,219	3,306	3,240
Current account balance	-2,130	-2,626	-2,556	-2,800	-2,879
Overall balance of payments 6/	-774	-2,172	-1,143	-373	--
Gross official reserves (weeks of imports)	25	17	19	23	24
External payments arrears	--	--	--	--	--
External debt outstanding	14,980	17,497	21,737	24,563	28,000

1/ Data relate to fiscal year, April -March 31.

2/ Staff forecasts, except for Government budget; the latter are budget estimates. The export estimate for 1983/84 and forecast for 1984/85 reflect a substantial shortfall and subsequent catch-up following the end 1983/84 dock strike.

3/ As of October 1984, the nominal effective exchange rate was 8 percent depreciated relative to the average for 1983/84.

4/ Assuming the rate in October 1984 remains unchanged throughout the remainder of 1984/85.

5/ Percentage change over 12 months ending September 28, 1984.

6/ Including payments of interest on nonresident deposits; the figures shown in Table 1 exclude these amounts.

India: Fund Relations
(As of End-December 1984)

(Amounts in millions of SDRs, unless otherwise indicated).

I. Membership Status

a.	Date of membership:	December 27, 1945
b.	Status:	Article XIV

A. FINANCIAL RELATIONS

II. General Department

a.	Quota:	2,207.7
b.	Fund holdings of rupees:	5,720.5 (259.1 percent of quota).
c.	Fund credit:	3,999.5 (181.2 percent of quota).
	Compensatory financing:	99.8 (4.5 percent of quota).
	EFF:	1,950.0 (88.3 percent of quota).
	Supplementary financing under EFF:	1,200.0 (54.4 percent of quota).
	Enlarged access under EFF:	750.0 (34.0 percent of quota).
d.	Reserve tranche position:	487
e.	Remuneration positon	252
f.	Current operational budget:	Not included.
g.	Lending to the Fund:	None.

III. Stand-By Or Extended Arrangement and Special Facilities

a.	Current stand-by or extended arrangement:	None.
b.	Previous stand-by or extended arrangements:	The three-year extended arrange ment for SDR 5,000 million (291 percent of old quota) approved on November 9, 1981 was cancelled by the authorities, effective May 1, 1984. Purchases under the

India: Fund Relations (cont'd)

b.	Previous stand-by or extended arrangements:	arrangement totaled SDR 3,900 million, including SDR 1,467 million drawn in 1983 and SDR 567 million drawn in 1984. There were no other arrangements with the Fund during the last ten years.
c.	Special facilities:	India last used the Fund's special facilities in 1980 when there was a compensatory financing purchase of SDR 266 million.

IV. SDR Department

a.	Net cumulative allocation:	681.2
b.	Holdings:	137.6 (20.2 percent of net cumulative allocation).
c.	Current Designation Plan:	Not included.

V. Administered Accounts

a.	Trust Fund loans	
	(i) Disbursed:	529.01
	(ii) Outstanding:	529.01
b.	SFF Subsidy Account	
	(i) Donations and loans to Fund:	None.
	(ii) Payments by Fund:	48.37

VI. Overdue Obligations to the Fund

None.

B. NONFINANCIAL RELATIONS

VII. Exchange Rate Arrangements

The Indian rupee is linked to a basket of currencies with 5 percent margins. The intervention currency is the pound sterling. India maintains extensive exchange restrictions which are subject to Article XIV. India has one restriction on the making of payments and transfers for current international transactions--a bilateral payments arrangement with a Fund member (Romania)--which is subject to approval under Article VIII, Section 2.

India: Fund Relations (concluded)

VIII. Last Article IV Consultation

Article IV consultation and EFF review discussions were held on the standard 12-month cycle during October 20-November 4, 1983. The staff report (EBS/83/276, 12/30/83) was discussed by the Board on January 27, 1984, and the following decision No. 7615-(84/17) was adopted:

1. The Fund takes this decision relating to India's exchange measures subject to Article VIII, Section 2, and in concluding the 1984 Article XIV consultation with India, in light of the 1984 Article IV consultation with India conducted under Decision No. 5392-(77/63), adopted April 29, 1977 (Surveillance Over Exchange Rate Policies).

2. The restrictions on the making of payments and transfers for current international transactions described in SM/84/15 are maintained by India in accordance with Article XIV, except that the restriction arising under the remaining bilateral payments agreement with a Fund member is subject to approval under Article VIII, Section 2. The Fund encourages the authorities to terminate the bilateral payments arrangement with a Fund member as soon as possible and to further simplify the exchange system.

IX. Technical Assistance

None has been provided by the Fund during the last three years.

X. Resident Representative/Advisors

None.

India: Relations with the World Bank Group
(As of October 31, 1984)

The Fund staff has maintained a close and effective working relationship with the staff of the World Bank on matters related to India for many years. Collaboration was particularly intense during the period of the extended arrangement (1981-84) when there was a regular exchange of views on program issues and a section was included in program papers presenting Bank views. Contact was facilitated by the participation of two Bank staff members--one from headquarters and one from the New Delhi office--in all Fund program missions. Fund staff members also took part in World Bank missions during the early stages of the extended arrangement discussions.

During the period of the extended arrangement, the work of the Fund has benefited from the Bank's expertise in the areas of appraisal of the investment program, export and import policies, and the regulation of industry. The Bank's assessments of public investment programs were included in all extended arrangement program papers.

As background for the 1985 Article IV consultations, the IBRD staff provided a series of indepth briefings on sectoral issues relating to agriculture, energy, and industry and also macroeconomic developments and issues. Bank staff from the resident mission in Delhi attended most meetings with the Indian authorities. The Bank staff has reviewed a draft of the staff report and has expressed concurrence with the importance of the macroeconomic issues identified and with the thrust of the staff appraisal.

The Bank's financial relations with India are summarized in the attached table.

India: Financial Relations with the World Bank Group
(As of October 31, 1984)

	IBRD	IDA	Total
Loans/credits fully disbursed	2,164.0	5,535.2	7,699.2
Present commitments 1/			
Agriculture	493.2	3,398.0	3,891.2
Power	1,785.2	1,813.0	3,598.2
Energy	547.3	--	547.3
Industry	929.6	400.0	1,329.6
Transportation	730.7	425.0	1,155.7
Telecommunications	120.0	314.0	434.0
Urban	49.1	270.0	319.1
Water supply and sewerage	--	507.0	507.0
Population/nutrition	--	148.0	148.0
Sub-total	4,655.1	7,275.0	11,930.1
Total fully disbursed and present commitments	6,819.1	12,810.2	19,629.3
Repayments	1,354.6	174.2	1,528.8
Total now held by Bank	5,464.5	12,636.0	18,100.5
Total disbursed and outstanding	1,894.1	8,125.7	10,019.8
Total undisbursed	3,570.4	3,950.6	7,521.0
IFC investment now held	--	--	97.1

India--Statistical Issues

The main sources of the statistics used in the report are the Central Statistical Office, the Reserve Bank of India, and the Ministry of Finance. A major problem is the delay in compiling many of the figures, so that for recent periods it has been necessary to make estimates. The reliability of these estimates varies according to the lag in availability of data; in some cases--e.g., the national accounts--the lag is as much as two years. Apart from delays in compilation, the financial data base is generally comprehensive, although there are a few areas where no official statistics are compiled in particular for employment and earnings. There are the following specific problems with the data:

1. National accounts

Official estimates are only available with a two-year lag, so that the data in the report for 1982/83 are "quick estimates", and those for 1983/84 are unofficial guideline estimates with only limited direct statistical foundation. Further, official estimates of private investment are subject to wide variation and are of uncertain reliability.

2. Prices and production

The consumer price index (CPI), (1960 = 100) is based on a household expenditure survey conducted in 1958/59, which is now outdated. A new household survey was conducted for the period March 1981-February 1982 by the Labor Bureau with a view to updating the weighting pattern for the index. Plans for the revision of the CPI are presently under consideration by the Government. The authorities are also planning to revise the base years for the current series on the wholesale price index (WPI, 1970/71 = 100) and the industrial production index (1970 = 100).

3. Monetary accounts

The data are monthly and current but are subject to sizeable revisions due to late reporting by some commercial banks. All data relate to the last Friday of the period, except for March where Reserve Bank data relate to March 31 after the close of the government accounts. As a result, it should be noted that transactions between the Reserve Bank and the commercial banks between the last Friday of March and March 31 can influence the reported credit data significantly.

There is a difference between the Monetary Survey data in this report and those published in IFS due to the fact that the latter do not include data for the nonscheduled commercial banks; this omission is in the process of being rectified so that the two series will in future be identical.

4. Merchandise trade

There is at least a six-month lag in the production of aggregate data on import and export values and even these data are subject to constant upward revision during the ensuing 18 months, as late returns are received. Efforts are made to estimate the missing returns, but variability in data reporting lags makes the estimates of trade growth subject to considerable uncertainty.

Official data on export and import prices and volumes are available only with a four-year lag and are of doubtful reliability. Furthermore, there are discrepancies between the monthly index series and the annual series compiled on a fiscal year basis due to differences in coverage. Data in the report are staff estimates with limited direct statistical foundation.

5. Balance of payments

The primary source of balance of payments data is the exchange record, but no official data were available to the mission beyond 1982/83. Therefore, unofficial estimates were prepared by the authorities for subsequent years based on partial or aggregate data, which are not comparable with the official series. Data are reported for IFS on a quarterly basis, so that the annual figures appearing there are on a calendar year basis (instead of the end-March year basis used in the report); however, the lag in the data is over 18 months.

6. Coverage, currentness, and reporting of Data in IFS

The table below shows the currentness and coverage of data published in the country page for India in the January 1985 issue of IFS. The data are based on reports sent to the Fund's Bureau of Statistics by the Reserve Bank of India, which during the past year have been provided on a timely basis, although there is an urgent need for reducing the lag in the availability of data on trade prices and the balance of payments.

Status of Data in January 1985 IFS

		Latest Data Published
Real sector	- National accounts	1982/83 1/ (partial)
	- Prices: Consumer	August 1984
	Wholesale	October 1984
	- Production: Industrial	August 1984
	- Employment	n.a.
	- Earnings	n.a.
Government finance	- Deficit/surplus	1983/84 1/
	- Financing	1983/84 1/
	- Debt	1983/84 1/
Monetary accounts	- Central Bank	October 1984
	- Deposit money banks	August 1984
	- Other financial institutions	Q3 1983
External sector	- Merchandise trade: Values	June 1984
	- Merchandise trade: Prices	Q1 1981
	- Balance of payments	Q1 1983
	- International reserves	August 1984
	- Exchange rates	November 1984

1/ Fiscal year ending March 31.