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The Indian Economy

By

Sukumar Muralidharan
BACKGROUND PAPER ON THE INDIAN ECONOMY
PREPARED FOR THE CONFERENCE ON
"ECONOMIC PERSPECTIVES FOR SAARC"

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When embarking upon her planning exercise in the early 1950s, India was a predominantly agrarian economy. The changes in the sectoral composition of the gross domestic product (GDP) since then are illustrated in figure 1. It is obvious that there has been a secular decline in the contribution of the primary sector to GDP. (This sector is shown as "agriculture" in the figure, but covers the Central Statistical Organisation's categories of agriculture, forestry and fishing, and mining and quarrying.) Correspondingly, there has been a sustained increase in the contribution of manufacturing, construction, electricity, gas and water supply (shown as "manufacturing" in the figure); and transport, communication and trade (shown as "transport" in the figure). Similarly, the contribution of the services (or tertiary) sector, has also shown a trend increase. (This sector is depicted in terms of two sub-sectors: banking and insurance, real estate, and the ownership of dwellings with business services is shown as "banking" in the figure; and public administration, defence, and other services is shown as "administration".)

Classifying the sectors in another manner, it is apparent that the share of commodity production in GDP (i.e., the total contribution of the primary and secondary sectors) has been declining. Commodity production accounted for over 75 per cent of GDP in the early 1950s; its share today is just over 60 per cent.

At first sight, there is little that is exceptional about these trends. Diversification from primary to secondary production, and at a later stage towards tertiary processes, is a natural concomitant of economic growth. A vast increase in material output from the primary sector has often been followed by its decreasing share in GDP, because of the price-depressing effects of technological advancement. At the same time, economic diversification has necessitated the emergence of a large tertiary sector.
to fulfil the complex service needs of a modernising economy.

However, the difference in the case of India is that the structural shifts in the composition of output have not been accompanied by any corresponding shift in the composition of the work-force. The 1951 Census reported (Volume I, Part IIB, Economic Tables; General Population) that 69.84 per cent of the population was dependent on agriculture — 46.92 per cent being "cultivators of land wholly or mainly owned, and their dependents". Similarly, the 1981 Census (Series I, Part IIIA, General Economic Tables) reported that of the total number of "main workers" in the population, 66.52 per cent were dependent on agriculture — 41.58 per cent of them being cultivators, and the rest, agricultural labourers. Another 2.26 per cent were dependent on "livestock, forestry, fishing, hunting and plantations", and 0.57 per cent on "mining and quarrying". Though changes in concepts and definitions have undoubtedly rendered the task of comparison between the two points of time difficult, the overall message of these figures is fairly clear.

In these circumstances, the growth of the tertiary sector would require a tremendous increase in productivity in the primary and secondary sectors — not only would these sectors have to meet their own requirements, but they would also have to generate an adequate surplus to finance the growth of the services sector.

However, the picture that emerges in this respect in India is at best equivocal. In per capita terms, the availability of cereals has increased at the rather marginal trend annual rate of 0.33 per cent since 1960, while that of pulses has fallen at a trend annual rate of 1.77 per cent. The per capita availability of edible oils has increased at a trend annual rate of 2.60 per cent, but this has only been on account of large-scale imports from the mid-1970s onwards. And the per capita availability of cotton cloth has been declining at a trend annual rate of 1.82 per cent. Taking clothing
as a whole, i.e., by including synthetics, which are largely a middle and upper-income group commodity, the per capita availability has done no better than stagnate since 1960.

To narrow the focus to the agricultural sector: the per capita output of essential agricultural commodities has virtually stagnated over the last three decades. At the same time, the demand from the secondary and tertiary sectors has increased—both absolutely and relatively—since larger proportions of the national product have been originating in these sectors. In the circumstances, one would expect the terms of trade between the agricultural sector and the rest of the economy to move sharply in favour of the former. In other words, the secondary and tertiary sectors would have to sell increasing quantities of their output to the agricultural sector, to get constant (or more gradually increasing) quantities of the latter's output for their own use. However, here again, the experience in India has been somewhat contrary.

Between the years 1951-52 and 1963-64, there was no significant shift in the net barter terms of trade between agriculture and industry. There was a sustained movement in favour of agriculture between 1964-65 and 1973-74, after which there was a sharp reversal. This relative worsening of the agricultural sector's terms of trade is perhaps the single largest contributor to the ongoing peasant movements which seek to ensure a higher price for agricultural produce, cheaper inputs, and the writing off of agricultural loans. On the resolution of this issue will depend a great deal of the future growth prospects of the Indian economy.
HE RURAL SECTOR

The Indian countryside, which continues to be home for three-quarters of the nation's population, offers a study in contrasts. The "green revolution" strategy, which sought to increase agricultural yields through concentrating modern inputs in a few selected regions, has brought prosperity to the agricultural tracts of north-western India. Today, the states of Punjab, Haryana, and Uttar Pradesh contribute virtually all of the wheat and rice that goes into the central food buffer stock. Cropping intensity has increased in these areas because of the intensive application of irrigation, and the diffusion of shorter duration grain varieties. Some of these areas have a low land-man ratio, and higher cropping intensity has meant some tightness in the labour market. Hence, there have been periodic large-scale migrations of labour from less prosperous regions.

Since 1970-71, only five states of the union - Punjab, Haryana, Uttar Pradesh, Maharashtra, and Andhra Pradesh - have shown increases in food grain output that are in excess of increases in population. Most states have just been struggling to maintain grains output marginally ahead of population growth. This speaks of a growing degree of regional specialisation in Indian agriculture. However, whether regional specialisation should be encouraged in an economy where three-fourths of the population depends on agriculture, is an issue still to be satisfactorily resolved.

Fertiliser use has increased from 5.26 million tonnes (nitrogen, phosphorus and potassium) in 1979-80 to an estimated 9.11 million tonnes in 1987-88. The consumption of fertilisers is promoted through a subsidy handed out by the Government of India (GOI) to the manufacturers. The fertiliser subsidy, Rs 20,500 million in 1987-88, amounted to about 5 per cent of the GOI's total non-plan expenditure. One-third of the country's cropped area...
accounts for all the fertiliser use in the country, and the usage of fertiliser in Punjab, Haryana, and the western parts of Uttar Pradesh, is five times the national average. It follows that the beneficiaries of the fertiliser subsidies are also highly concentrated in these regions.

Irrigation potential in the country has increased from 22.6 million hectares in 1951, to about 74 million hectares today. The initial emphasis was on "major and medium" irrigation projects, such as large dams and canals. Since the 1970s however, "minor" irrigation projects - such as tubewells, and dug-wells, particularly the former - have begun to enjoy greater favour, because of their intrinsic economies, and amenability to private ownership.

A major issue confronting the agricultural sector today is that of optimising the utilisation of irrigation potential. This is a problem that pertains mostly to the major irrigation projects. The main reasons for sub-optimal utilisation are various infirmities in the planning of irrigation projects. Planners have for long been exclusively preoccupied with merely the building of centralised facilities like dams and canals, without paying sufficient attention to the various subsidiary activities needed in the command area of the irrigation project. Land-development, land-levelling, and the development of field channels have been left to local, initiative.

In areas where irrigation facilities have recently been introduced, local level co-operative institutions are not strong enough to work out an optimal pattern of water utilisation. In most instances, farmers at the head reaches exercise a pre-emptive claim on irrigation water, cultivating crops such as sugar-cane and paddy, in violation of the cropping pattern suggested in the course of project planning.

A recent policy initiative taken by the Government seeks to redress the situation through the creation of a Command Area Development Authority at the sites of major irrigation projects. However, it is not yet clear...
whether bureaucratic control can really substitute for local-level cooperative institutions in the management of irrigation facilities.

The concessional disbursement of credit has also been a major plank of the agricultural strategy of the GOI. Organised sector credit, i.e., institutional credit, has been progressively tending to outweigh non-institutional credit over the last two decades. According to the last All-India Debt and Investment Survey, conducted in 1981, the proportion of non-institutional credit was 36.8 per cent for cultivators, and 63.3 per cent for non-cultivators. In 1961, the figure for cultivators was 81.8 per cent, and for non-cultivators, 89.5 per cent. Hence the cultivators, i.e., those who own some land, have been preferential beneficiaries of the spread of institutional credit, as is only to be expected. Credits taken by non-cultivators would largely be consumption loans, for which institutional sources would not be forthcoming. The problem of indebtedness continues to be severe for the property-less rural population.

District-level co-operative institutions, and their apex state-level bodies, have been playing a major role in the disbursement of agricultural credit. The disbursement of agricultural credit went up from Rs 27,590 million in 1979-80, to Rs 96,450 million in 1987-88. Co-operative institutions, which accounted for almost 70 per cent of total agricultural credit in 1979-80, now account for just 45 per cent. Commercial banks controlled by the central Government, and "Regional Rural Banks", set up by consortia of commercial banks, have steadily been increasing their concessional disbursements to the agricultural sector.

The large volume of bad debts and overdues in agricultural credit payments could be the source of a potential crisis for the banking sector. The problem of overdues is particularly severe for co-operative institutions. According to latest available figures, the percentage of
overdues at the primary agricultural credit society and primary land
development bank levels is about 42 per cent. The Central Government has
been pressuring state governments to formulate time-bound programmes for
the recovery of outstanding loans from agriculturists. But any such
programme is likely to encounter stiff resistance from agriculturists' associations, which have been making the waiver of agricultural loans one of their central demands in recent times.

The State and Central Governments' procurement operations play a major role in maintaining remunerative price levels in the rural primary markets during harvest seasons. Procurement prices are periodically fixed for major foodgrains, oilseeds, pulses, and other cash crops like sugarcane, by the GOI's Commission on Agricultural Costs and Prices. These prices are expected to guarantee a certain margin over costs of cultivation, and prevent a precipitous price decline in the harvest season. The stocks of food built up in this manner are used by the Central and State governments to sustain the public distribution system (PDS) for essential commodities, and certain poverty alleviation programmes in the rural areas.

Poverty alleviation programmes in the rural areas were introduced in the 1970s under several guises - the Integrated Rural Development Programme (IRDP), the Drought Prone Areas Programme (DPAP), the Rural Labour Employment Guarantee Programme (RLEGP), the National Rural Employment programme (NREP). These programmes aim to uplift standards of living in the rural areas by financing the creation of physical assets through the food surpluses held with the government. In practice, however, the outreach of these programmes has been limited because the agricultural sector is not capable of yielding the necessary surpluses.

Between April and October 1987, the distribution of foodgrains through the PDS was 8.52 million tonnes. In the same period, the volume of grains allocated for rural public works programmes was 1.6 million tonnes. The
coverage of the PDS is largely confined to the urban areas. The rural poverty alleviation programmes would therefore seem to be in direct conflict with urban areas for access to the central pool of foodgrains.
MANUFACTURING

Industrial policy in recent times has sought to provide the manufacturing sector with the growth impulse that it has lacked for long. Several sectors of manufacturing industry have been delicensed, and the procedures for foreign collaboration and the import of technology and equipment have been made less stringent.

Industrial output has shown some signs of raising itself out of the low-level equilibrium of the first three decades of planning in the country. Between 1980-81 and 1986-87, industrial production grew at a compound annual rate of 7.6 per cent, as against 4.2 per cent in the period between 1971-72 and 1979-80. The growth rate since 1980-81 is also significantly higher than the trend annual industrial growth rate of 6 per cent recorded in the first three decades of planning.

A feature of the recent phase of industrial growth in India is the changing sectoral composition of contributions to aggregate growth. Older industries now account for relatively less in the basket of industrial goods output. To reflect these structural changes in Indian industry, the Government recently introduced a new index of industrial production, which is reportedly based on "improved selection procedures and methodology for determining the weighting diagram (that determines the significance of each item in overall industrial production), exclusion of non-reporting items, inclusion of new industrial products and an appropriate representation of the small-scale sector".

Taking a more disaggregate picture, since 1981-82, the industries that have registered exceptionally high rates of growth include the manufacture of wood and wood products, the manufacture of leather and leather products, the manufacture of electrical machinery, and the residual category of "other manufacturing industries". The laggards have been manufacture of
food products; beverages; cotton textiles; textile products; jute, hemp and
esta textiles; basic metal and alloy products; metal products other than
achinery; machinery and machine tools (other than electrical machinery);
and transport equipment. The middling performers have included the
manufacture of paper and paper products; rubber, plastic, petroleum and
al products; chemicals and chemical products; and non-metallic mineral
products.

feature of the new phase of industrial growth is the rapid increase in
the import of capital goods. The imports of capital goods as a whole haveeen increasing at a compound annual rate of 19 per cent per annum since
1980-81. Imports of "non-electrical machinery" have increased at a rate of
23 per cent per annum, while those of electrical machinery and transport
equipment have increased at compound rates of 22 and 6 per cent per annum.

he annual compound growth rates of domestic production of these items are
a follows: machinery and machine tools (other than electrical machinery),
1 per cent; electrical machinery, 19 per cent; and transport equipment, 6
per cent. It is apparent that imports have been increasing much faster than
domestic production for the entire range of capital goods, and that the
differentials in growth rates are fairly large, except in the instance of
electrical machinery.

he argument behind liberalising the import of capital goods was that
indigenous industry did not have the capability to build many modern,
productivity-augmenting types of machinery, which were essential for
technological upgradation. But after a few years of liberal import, the
omestic capital goods sector began to display unmistakable signs of
ickness, in the form of declining capacity utilisation, and profitability
ates. The 1987 budget seemed to signal a reversal, with duty rates on
ital goods import being raised significantly across a wide range.
However, capital goods imports have continued to increase, and domestic producers today have begun to argue that quantitative restrictions on imports be put in place, and their inputs be made available at concessional rates of duty.

Another interesting characteristic of the industries that have shown high rates of growth in recent times is their large degree of import dependence. In the absence of adequate disaggregate data, it is difficult to arrive at a precise estimate of the degree of import dependence. But two industries—automobiles (two-wheelers and passenger cars) and electronics—best typify this problem of Indian industry.

To take the instance of Maruti Udyog Ltd, a public sector company which has in recent times infused some dynamism into the Indian passenger car sector—the import value of components and raw materials as a proportion of the total value of components and raw materials consumed, was as high as 97.2 per cent in 1983-84. It has since declined, but rather slowly, from 85.3 per cent in 1984-85, to 80.8 per cent in 1985-86, and 72.3 per cent in 1986-87. Considering that Maruti Udyog produces over 100,000 vehicles per annum, and hence should enjoy the economies of scale necessary for the progressive indigenisation of components manufacture, this would seem a rather slow rate of progress. Other manufacturers in the passenger cars sector do not even have the benefit of scale, since they typically produce less than 30,000 cars per annum. Their progress in this respect, should therefore, be expected to be even slower.

electronics is an industry that has shown growth rates well in excess of the average for the manufacturing sector in recent times. The official economic Survey for 1986-87 had spoken of the electronics industry as one with a bright future and a special relevance to India. However, a recent Discussion paper put out by the GSI's Department of Electronics (DOE) explicitly concedes that the import-oriented growth path of the industry may
not be sustainable, considering its sluggish export performance.

The keystone of the GOI's approach to the problem of import dependence is the phased manufacturing programme (PMP). All the foreign collaboration and component import agreements that were approved in the liberal phase of the GOI's economic policy were subject to the stipulation of indigenising under the terms of a PMP drawn up in advance. However, the DOE has admitted in a recent paper that the results have not been quite as good as expected, at least in the case of electronics. Automobiles too have not done very much better, as is evidenced by the fact that the appreciation of the Japanese yen led to a steep escalation in import costs for most manufacturers — and in some cases, to their being priced out of the market.

The very utility of the PMP as a policy device in today's industrial environment has been questioned by the Bureau of Industrial Costs and Prices (BICP) — an advisory body under the aegis of the GOI's Ministry of Industry. In a recent paper, the BICP argued that the PMP was a "policy-induced source of higher costs", which had no place in a technological milieu dominated by specialisation in narrowly defined product ranges, and the use of bought-out components by "parent" assembly units. In such circumstances, the PMP for the single entrepreneur would be no more than a road for purposeless and expensive vertical integration — which would be quite contrary to world trends.

Thus, the problem of reconciling between the imperatives of modernisation, the conservation of foreign exchange in a context of stagnant export earnings, and maximising growth is yet to be satisfactorily resolved for the Indian manufacturing sector.
ENERGY

The underlying parameters of energy policy were radically changed in India, as in several other countries, by the oil price hikes of the 1970s. A Fuel Policy Committee appointed by the GOI in 1975 recommended a coal-based energy policy, on the presumption that existing reserves of coal could be optimally tapped with minimal additional investment. There has been some rethinking of this policy in recent times, mainly on account of large discoveries of hydrocarbons, especially natural gas. However, there has not yet been any official intimation of a change in the current emphases of energy policy.

Most of the coal mined in the country is within the aegis of the nationalised company—Coal India Ltd. The output of coal has shot up from 75 million tonnes in 1974-75, to about 170 million tonnes in 1987-88. But the quantitative expansion conceals a certain degree of qualitative deterioration. Today, most of the coal produced in the country falls in the inferior E, F, and G grades.

The power sector consumes well over half the coal produced in the country. In recent times, thermal power generation has suffered from the problem of low-quality coal. Steam generators are designed on the assumption that coal of a certain quality would be available. But these conditions are rarely ever fulfilled.

The power sector today accounts for between 25 and 30 per cent of the total capital outlay under the Five Year Plans. Power generation capacity has more than doubled between 1975-76 and 1987-88, from 20,100 megawatts (MW) to 51,900 MW. A feature of this phase of expansion is the increasing share of thermal generation capacity in the total. The share of thermal (i.e., mostly coal-based) generation in total capacity rose from 55 per cent in 1975-76 to 65 per cent in 1987-88. For optimal load-matching, power sector officials are committed to a thermal-hydro ratio of 60:40. This implies
that greater emphasis will have to be placed on developing hydroelectric sources of power in the next few years.

Most of the power generation capacity in the country is under the state-government owned electricity boards. These state electricity boards (SEBs), with only a few exceptions, have been large loss makers. In recent times, enterprises owned by the central government have been accounting for most of the fresh additions to capacity. This has raised issues about the equitable division between states of power generated in the central sector. Distribution continues to be handled by state government agencies. Some of the larger metropolitan towns have municipal agencies handling power distribution functions.

India has built up substantial capacity in the production of power generation equipment – mostly under the aegis of the public sector. The central government owned Bharat Heavy Electricals Ltd now has the capacity to manufacture 210 and 500 MW turbo-generator sets. There were initially some problems in arriving at the optimal capacity at which to standardise domestic manufacturing capabilities. The early factories set up went in for 60 and 110 MW generator sets – many of which entered service in the 1970s, never to perform at anywhere near design levels. Indian electrical equipment manufacturers have had rather more success with the 210 MW sets. Production of 500 MW thermal sets, and gas turbines has just begun in the country, under different collaboration agreements with international electrical equipment giants.

Private sector participation in power generation is possible only under a special dispensation of the Electricity (Supply) Act, which is very rarely invoked.

The petroleum sector in India has grown rapidly since the mid-1970s, when
the exploration effort was stepped up significantly following the first of the oil price shocks.

In 1970-71, India's balance of trade deficit stood at Rs 990.4 million, and petroleum, oil and lubricants (POL) accounted for a mere 8.56 per cent by value of her imports. In 1975-76, when the economy was beginning to digest the effects of the first oil shock, the balance of trade deficit was Rs 12,285.4 million, with POL's share in total imports having grown to 23.86 per cent. In 1980-81—the first full accounting year following the second oil shock—the balance of trade deficit was Rs 58,385 million, and the share of POL in India's import basket was a record figure of 41.97 per cent.

If the trade deficit has remained within controllable limits since then, a large part of the credit lies with the performance of the petroleum sector. In 1970-71, India was able to meet just 36.76 per cent of her total domestic demand for crude oil indigenously. The extent of self-sufficiency had not increased very much till as late as 1980-81, standing at 39.33 per cent. The subsequent year saw the big breakthrough, with domestic production topping the 50 per cent mark in relation to total consumption. Since then, the story has been one of almost uninterrupted increase in the degree of self-sufficiency, with over two-thirds of demand now being met through indigenous production.

Together with increasing self-sufficiency, there has also been a rapid rise in the proportion of domestic crude output from offshore oil fields. Offshore oil production began as late as 1975-76, when it accounted for just 4.49 per cent of total output. It has increased steadily over the years, and today stands at over 68 per cent of the total. The entire offshore production is accounted for by the Bombay High oilfield.

This provides an index of the dependence of the Indian petroleum sector.
and with it of the entire economy, on one source of crude oil. But the Bombay High oilfield has long since reached its highest level of sustainable yield. This is reflected in the fact that the production of crude oil increased threefold between 1980-81 and 1984-85, after which the rate of growth has been relatively moderate. The reserves-production ratio, which is a measure of the rapidity of depletion of petroleum resources, stood at 18.77 in 1970-71. Following the discovery of Bombay High, it shot up, to a figure of 34.82 in 1980-81. But once large-scale exploitation began from this oilfield, the ratio began to decline, to finally touch the current level of 16.58. This is the highest feasible level of exploitation that the national petroleum policy envisages.

Exploration efforts have again to be mounted on a large-scale. A redeeming feature in this respect is that the potential hydrocarbon-bearing sedimentary basins in the country are so far grossly under-explored. Only 4 of the 27 basins in the country have been explored so far. However, the other side of the coin is that the drilling effort will progressively be moving into geologically more complex and logistically hostile environments. The finding costs of oil would be higher in these areas, and the world-wide softening of oil prices would act as a disincentive.

There has been a great deal of emphasis in recent times on the containment of demand for petroleum products. The pattern of demand in India exhibits a heavy preponderance of the petroleum middle-distillates – mainly diesel and kerosene. The share of middle-distillates in the total consumption of petroleum products stood at 50.47 per cent in 1970-71. In 1980-81, it stood at 55.20 per cent, and in 1987-88, at almost 60 per cent. Oil refineries in India have had to do a considerable amount of revamping to keep their output mix in consonance with this pattern of demand. The fluid catalytic cracking (FCC) process was initially adapted to boost the yield of middle distillates. This has succeeded in increasing the share of middle
distillates in the output basket from 50.04 per cent in 1970-71 to almost 55 per cent in 1987-88. But this still falls below the requirements at the consumption end.

By the turn of the century, it is expected that middle-distillates will account for 66 per cent of the total consumption of petroleum products in the country. Indian refineries are now going in for the newly developed "hydro-cracking" process to augment their yield of middle-distillates.

Critics point out that the growth in demand for middle-distillates is largely in consequence of a system of cross-subsidisation followed by the petroleum companies, wherein most of the cost of processing is put on the heavy- and top-ends. But there is unlikely to be any change in this price system, because of the repercussions it would have in terms of diesel users like the transportation sector, and kerosene users, like the household sector.

Natural gas has now emerged as a major potential fuel in the country, following the discovery of large deposits of associated gas in Bombay High, and free gas in the adjacent South Bassein fields. The initial policy emphasis was to use natural gas preferentially as a feedstock in fertilisers and petrochemicals, rather than as a fuel. But in recent times, there has been a rethinking of this strategy, and greater acceptance of the utility of natural gas in power generation.
SERVICES

As seen from figure 1, services have been a relatively fast growing sector of the Indian economy, in terms of contribution to GDP. However, the share of this sector in employment has not increased in any significant measure. This is an important respect in which the Indian service sector is different from that in the advanced countries, like the US.

The transport, communication, and trade sector has grown at a compound annual rate of 6 per cent since 1980-81. Banking, insurance, and real estate has grown at 6.1 per cent, and public administration, defence, and other services has grown at 6.2 per cent. All these rates of growth are significantly in excess of the aggregate growth rate of 4.8 per cent in the Indian economy.

Looking at the contribution of services to employment – according to a study done by the Centre for Monitoring Indian Economy, the share of the agricultural sector in employment in terms of standard person years fell only marginally to 51.5 per cent from 53.1 per cent, between 1979-80 and 1984-85. Concurrently, the share of the manufacturing sector went up fractionally, from 14.6 to 14.9 per cent. Hence, the share of the service sector could not have increased very much in this period. This becomes even more clear when we look at figures for the organised sector. The share of services in organised sector employment increased only rather marginally, from 54.7 per cent, to 56.7 per cent, between 1971 and 1984. In the same period of time, the contribution of services to GDP at factor cost increased by almost 8 percentage points. It follows that the per capita income in services has been going up.

The growth in service incomes – particularly under the government head – has had repercussions on public finances. The trend in savings of Government (i.e., surplus on revenue account of administrative departments and departmental enterprises) are shown in figure 2. As a recent document
2: TRENDS IN GOVT SAVING

(AS PERCENTAGE OF TOTAL EXPENDITURE)
prepared by the Planning Commission has mentioned: "savings of Government administration have become wages and salaries. Between 1980-81 and 1985-86, the wage bills in public administration and publicly provided services has doubled. If the average compensation per employee in these sectors had increased only as much as the consumer price index, and if the total number of employees had remained constant, the total wage bill for these employees would have been lower by Rs 4,500 crore (i.e., Rs 45,000 million)". Because of the runaway increase in incomes, the Government sector is now borrowing to pay wages and salaries. As the Planning Commission has observed later in the document cited above, this could well limit the country's ability to "maintain a more broad-based programme for employment generation and poverty alleviation".

The banking sector has played a major role in national economic planning since the nationalisation of large commercial banks began in 1969. The objective of nationalisation was to enforce greater social accountability in the disbursement of credit. Since nationalisation, many of the regional disparities in banking, such as the preferential location of branches in urban areas and well-developed centres of commerce, and the large advantage of metropolitan centres by way of access to credit, have been ironed out. To take a commonly used measure, the credit-deposit ratios for the prosperous states such as Maharashtra, Tamil Nadu, and Punjab; prior to nationalisation, used to be well in excess of those for the poorer states like Orissa, Bihar and Madhya Pradesh. The figures now are less divergent.

Nationalised banks are obliged under a Government directive, to reserve a certain portion of their advances for priority sector lending. Small-scale industry, agriculture, rural artisans, and government food procurement operations are some of the earmarked areas for priority application of bank credit. The national target for priority sector lending is 40 per cent of total bank credit. The figure in recent times has moved up from 40.8 per
cent in 1985-86, to 42.2 per cent in 1986-87, and 44.0 per cent as on September 30, 1988.

The increase in the proportion of lending going to the low-yielding priority sector advances could well be a result of a declining demand for prime lending from the corporate sector. In the 1980s, the direct mobilisation of resources through the stock-markets has become a major avenue for corporate sector financing in India. The demand for bank funds from the high-yielding segments has hence been declining. National Accounts Statistics show that the household sector's holdings of corporate shares, debentures, and units of the Unit Trust of India, have increased from 3.4 per cent of their total savings in 1981-82 to 6.9 per cent in 1985-86. In the same period, the consents granted for the issue of shares and debentures have increased from Rs 6,223 million to Rs 30,553 million. Small savers are increasingly putting their money into the relatively high-yielding corporate shares and debentures, rather than low-yielding bank deposits.

This points to the fact that the commercial banks' efforts to offset the costs of priority sector lending through prime lending to the corporate sector, may be less successful in future. Though the nationalised banks as a whole have continued to show increasing profits over the years, the number of loss-making branches has been increasing. The rural sector accounts for most of the loss-making branches, but urban branches contribute over 70 per cent of the losses. There may be a relative overcrowding of bank branches in the urban areas. The pace of expansion in future may hence be reduced, and productivity augmenting measures may be instituted to cut down manpower and establishment costs. Another emerging response of the banking sector to the crisis of profitability is diversification into new lines, such as mutual funds which exploit the stock-market boom, merchant banking, and consumer credit.
The telecommunications sector has in recent times been elevated to a high-priority status. A series of organisational changes have been instituted in recent times, beginning with the bifurcation of posts and telecommunications, and the formation of an autonomous public sector corporation to manage the telecom networks in the two main metropolitan centres. The newly formed corporation has been able to overcome the resource constraints faced by the departmental enterprises by tapping the capital markets directly for funds. However, critics of the current policy question the wisdom of administratively separating the high-revenue earning segments from the national telecommunications network. They argue that this could retard the development of telecommunications in the rural sector by disrupting the traditional systems of cross-subsidisation between high-density and low-density areas.

India’s efforts to be a major player in the world trade in services are yet to pay off. Exports of computer software have increased rapidly over the years, from Rs 170.23 million in 1983 to Rs 580.01 million in 1987. Close to 80 per cent of the software export from the country is accounted for by two firms in the private sector. Analysis of their performance shows that the value addition in software export is around 40 per cent. Besides this, the kind of software export operation mounted by these firms is highly manpower intensive. It is doubtful if India has the manpower training resources to achieve the target of Rs 3,000 million in net software export by 1990, on the basis of a quantitative expansion of the existing kind of operation. A qualitative change towards high value-addition software would be necessary if the manpower resources available in the country are to be leveraged to maximise the export earnings.

Exports of technical consultancy services are not very significant. Some breakthroughs have been reported in railway construction, power plant and oil refinery engineering, and fertiliser plant erection.
INTERNATIONAL TRADE AND RELATIONS WITH SAARC

Since 1980-81, India’s exports in rupee terms have increased at a trend annual rate of 11 per cent, while her imports have increased at 7.8 per cent. However, since imports started off from a larger base, the trade deficit has widened from Rs 58,390 million to Rs 70,911 million.

The major contributors to the export basket in 1987 (April to December) were cotton fabrics, 6.29 per cent; ready-made garments, 10.52 per cent; gems and jewellery, 16.88 per cent; and leather and associated goods, 6.62 per cent. The rather heterogeneous category of "engineering goods", which includes machinery, transport equipment, and metal manufactures excluding iron and steel, accounted for 5.43 per cent of the export earnings in the period under review. However, this component of the export basket has been fairly stagnant over the years, having registered only an annual compound growth rate of 1.2 per cent since 1980-81. In comparison, exports of gems and jewellery have grown by 22.3 per cent; of cotton fabrics by 5.5 per cent; of readymade garments by 14.2 per cent; and of leather and associated goods, by 12.4 per cent. The fast growing export sectors are thus the traditional industries, where the value addition is not very high. Even in gems and jewellery, as we shall see below, the value addition and the net foreign exchange benefit to the economy is much below the export value.

The large contributors to the import bill in 1987 (April to December) were petroleum and petroleum products, 18 per cent; capital goods, 27.68 per cent; pearls, precious and semi-precious stones, 9.10 per cent; iron and steel, 5.37 per cent; chemicals, 4.4 per cent; and edible oils, 3.21 per cent.

Imports of petroleum and petroleum products, and capital goods have been dealt with elsewhere. Pearls and precious stones are imported as raw material for the gems and jewellery industry, which as shown above, is one
of the fastest growing export sectors. In a typical year, imports of pearls and precious stones amount to between 60 and 70 per cent of the export value of gems and jewellery. The export growth in this segment has thus been highly import-intensive.

Receipts on invisibles account have played a role in partly bridging the wide payments imbalance caused by the trade gap. As seen from figure 3, the major head for receipts have been transfer payments under the private account from Indian nationals abroad. Receipts from "foreign travel", i.e., from tourism, have fallen in importance since the early 1980s. Investment income, after briefly contributing positively towards net receipts, turned negative in subsequent years, indicating either that Indian investments abroad have been falling off in productivity, or that profit repatriations from India have been increasing at the faster rate.

Remittances from Indian workers abroad, particularly in the oil-exporting nations of the Gulf, have played an indubitably critical role in stabilising the economy on the external payments front. In this connection, the recently manifest tendency for Gulf remittances to taper off has created some concern in official circles. Schemes are now being worked out which make it more attractive for nationals abroad to deposit foreign currency in Indian bank accounts.

Between 1980-81 and 1984-85, drawals from the International Monetary Fund (IMF) played a major role in financing the balance of payments deficit of the Indian economy. (Figure 4.) In some of those years, there was a tendency to build up on the foreign exchange reserves. However, once the drawals from the IMF ceased, there has been a tendency to draw down foreign exchange reserves to finance the BOP deficit. Grants peaked briefly in importance in 1984-85, but then have tended to taper off. Loans have emerged as the single largest means of financing the payments gap. The debt servicing ratio of the Indian economy, i.e., interest and amortisation on
3: INVISIBLES ON CURRENT ACCOUNT

(PERCENTAGE COMPOSITION)

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4: FINANCING OF BOP DEFICIT

(PERCENTAGE CONTRIBUTION)
external loans as a proportion of current receipts, today stands at 28 per cent. This is a distinctly uncomfortable figure, and policy makers are today greatly concerned with initiating corrective measures, such as boosting exports, and restraining imports growth. The objective is to emphasise the former as far as possible, without necessarily resorting to the latter, since in the current thinking, a certain degree of import liberalisation is essential for modernisation and export growth in the long-run.

Japan has increased its share in India's imports rather rapidly, from 7.2 per cent in 1984-85, to 9 per cent in 1985-86, and 12.7 per cent in 1986-87. It is today the largest source of imports into India. The US was second with 9.8 per cent, down from 10.5 per cent the previous year; while the Federal Republic of Germany and the UK had shares of 9.6 and 8.1 per cent respectively. The USSR had a share of 5.3 per cent, while other East European countries together accounted for another 2.2 per cent. The oil-exporting nations of OPEC had a modest 8.8 per cent share, down from 19.4 per cent in 1984-85 and 17.4 per cent in the subsequent year - mainly because of the steep decline in oil prices in 1986-87. The share of non-OPEC developing countries was 18.7 per cent. There has been no significant change in this figure in recent times.

As far as exports go, the largest buyers from India in 1986-87 were the US, with 18.8 per cent of the total, and the USSR, with 14.9 per cent. Japan took 10.7 per cent, while the FRG and the UK had 5.9 per cent each. The share of the non-OPEC developing countries was 15.3 per cent.

It is apparent that the developing world does not play a very major role in India's international trade. The role of the SAARC economies is also rather marginal. The main obstacle to expanding trade, it appears, would be non-complementarities in economic structure, and payment difficulties on account of hard currency shortages.
A feature of India's economic relations is its rupee trade with the Soviet Union and other nations of the eastern bloc. According to a recent analysis by the Reserve Bank of India, 40 per cent of India's exports in 1984-85 were invoiced in rupees, while only 12.6 per cent of her imports were so invoiced. This is in consequence of the large rupee-balances that were built up with the eastern-bloc economies when India was a heavy purchaser of defence equipment, petroleum, and certain kinds of capital goods from them. In some instances, as in the Kandla Free Trade Zone, India has been known to act as a conduit for goods to the eastern bloc. This trade route helps to minimise the eastern bloc's outflow of hard currency, and in the liquidation of its rupee balances. But the gains for India are not as unambiguous, since she has to pay out hard currency to buy these goods, and receives only rupees in exchange.

Most of India's imports are invoiced in dollars. As of 1984-85, the figure was 65.1 per cent of the total import basket — up from 60 per cent in 1979-80. The share of the pound sterling had fallen steadily from 11 per cent to 5.2 per cent between these two years; that of the Deutsch mark had held steady at around 6 per cent; and that of the Japanese yen increased gradually from 2.3 per cent to about 5 per cent.

Since the rupee has a very large proportion of the export invoicing from the country, and a relatively small role in import invoicing, the borrowing requirements for bridging the trade gap would be even higher than indicated by the excess of imports over exports.

Export promotion is one of the priority areas in economic policy today. There is no gainsaying that the depreciation of the rupee in the 1980s has had a role in the relatively rapid rate of export growth in this period. But currency depreciation implies that the import capacity of a certain
quantum of export growth would be relatively lower, and the debt-servicing too. In the years to come, the economy may have to keep running faster to merely remain in the same place with respect to the rest of the world.
INTERNATIONAL FINANCIAL INSTITUTIONS

India's policy of extreme prudence through the years of the successive oil shocks led to her stock going up with international financial institutions. However, the environment of stringent economic controls within the country was an impediment to integration with the international financial system.

The negotiation of the large SDR loan under the IMF's Extended Fund Facility in 1980-81 coincided with a move to liberalise economic controls. Liberalisation has continued apace ever since, and the pace of borrowings from the international financial system has increased. However, India's credit rating continues to be good, and the last meet of the Aid India Consortium in Paris authorised a record level of disbursements, apart from congratulating the national government for tiding over a period of drought and adversity with considerable panache.

The current conjuncture is nevertheless a difficult one for India, as far as external payments are concerned. Repayments to the IMF have risen steadily from SDR 131.25 million in 1985-86, and 431.25 million in 1986-87, to 704.17 million in 1987-88. The peak value will be touched in 1988-89, when SDR 804.13 million is due for repayment. Then the repayments will fall off, though gradually, to 681.21 million in 1989-90, and 468.71 million in the subsequent year. Repayments amounting to SDR 3900 million in all are scheduled to continue, though in steadily diminishing quanta, up to 1994-95. Together with these repayments, the total debt servicing liability will also rise rapidly between now and 1991-92. Official sources anticipate a decline thereafter.

India's borrowing from the World Bank has been increasing over the years. These borrowings are mostly project-related, and are used to finance either power projects in the central public sector, oil exploration activities, urban improvement projects, water supply and sanitation schemes, or
irrigation projects. World Bank group lending to India increased from US$ 368 million in the Bank's financial year 1985-86 (July to June) to Rs 860 million in the financial year 1986-87. The proportion of total World Bank disbursements coming under concessional terms from the International Development Association (IDA) declined from 26.4 per cent in 1985-86 to 12 per cent in the following year. India's share in total IDA credits has been falling after the arrival of China as a big borrower. Of IDA's total credit disbursements, India got 19.4 per cent in 1986-87, compared to 19.9 per cent the earlier year. Thus the relative terms of India's borrowing from the World Bank have been hardening over the years.

Profile of India's borrowings in the last decade shows a steadily growing share of private credits of shorter maturities. This too may have adverse implications for the country's debt servicing burden in the 1990s. The declining world value of the rupee would place a further burden on the export sector to earn the foreign exchange resources necessary to service the debt burden.