Indian Economic Development-A Review

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Abstract

That India managed to achieve this high growth in the aftermath of demonetization and amidst the global slowdown, along with a macro-economic environment of relatively lower inflation (unlike a generally higher inflation in the previous episodes of high growth), moderate current account deficit coupled with broadly stable rupee-dollar exchange rate and the economy treading decisively on the fiscal consolidation path, makes it quite creditable. Most external debt indicators also point towards an improvement as at end September 2016.However, challenges abound. The objective of the study is to understand the To study the monetary management and financial intermediation of India in form of Liquidity situation, Yield on Government bills/ securities, Banking sector, Credit growth, Measures to strengthen corporate bond market. The study also aims to understand the India's merchandise trade in terms of export, import and trade deficit and Balance of payments which includes current account, capital account and exchange rate during the year 2015-2016. The study is purely secondary and which uses data from government websites, newspaper and journals.

Keywords:*Monetary Management, Financial Intermediation, Merchandise Trade, Balance Of Payments*

I. INTRODUCTION

The Economic Survey 2015-16 had predicted the Indian economy to register the GDP growth rate in the range of 7 to 7.75 per cent in the year 2016-17. The economy was indeed treading along that path and clocked 7.2 per cent in the first half of the current financial year, as per the estimates released by the Central Statistics Office (CSO). However, consequent upon the radical measures initiated in November 2016 in the form of demonetisation of Rs. 1000 and Rs. 500 currency notes, the Indian economy is likely to experience a slowdown in the growth rate that could be lower than the first advance estimates of CSO. The first advance estimates released in early January 2017 were arrived at mainly based on data prior to demonetisation and largely reflect the economic situation prevailing in the first seven to eight months of the financial year. Even the likely reduction in the rate of real GDP growth of 1/4 percentage points to 1/2 percentage points relative to the baseline of about 7 per cent still makes India's growth noteworthy given the weak and unsettled global economy which posted a growth rate of a little over 3 per cent in 2016. The investment to GDP ratio has not only been lower than the desirable levels but has been consistently declining over the last few years. This trend needs to be reversed at the earliest in order to realise higher and lasting economic growth. Similarly, the savings rate will have to be raised, so that investment can be financed without resorting to high dose of external financing. After remaining fairly stable for much of the last two years, international prices of crude oil have started to trend up. This along with rise in the prices of other commodities like coal, etc. could exert inflationary pressure and have the potential to adversely impact the trade and fiscal balances. The outlook for the next financial year suggests that growth is set to recover, as the currency in circulation returns to normal levels and taking into account the significant reform measures initiated by the government

A. Objectives of the study

- To study the monetary management and financial intermediation of India
- To understand the India's merchandise trade in terms of export, import and trade deficit and to study the Balance of payments of India

B. Research Methodology

The study is exploratory in nature. The data from government websites like economic survey, ministry of finance, economic review. In addition the study uses article, journals and newspaper for reference.

II. REVIEW OF ECONOMIC DEVELOPMENTS IN INDIA

A. Monetary Management And Financial Intermediation

The Government amended the Reserve Bank of India Act, 1934 during the current financial year. The amended Act provides for inflation target to be set by the Government, in consultation with the Reserve Bank, once in every five years and further provides for a statutory basis for the constitution of an empowered Monetary Policy Committee (MPC). As per the revised monetary policy framework, the Government has fixed the inflation target of 4 per cent with tolerance level of +/- 2 per cent for the period beginning from 5th August, 2016 to March 31, 2021. The Government has also notified the constitution of the Monetary Policy Committee on 29th September 2016. So far the Monetary Policy Committee has already held two meetings. The Monetary Policy Committee, in its latest meeting held on December 7, 2016, while maintaining accommodative policy stance did not change the policy rate. The policy rate was reduced by 25 basis points to 6.25 per cent in its first meeting held on October 4, 2016. Hence the reverse repo rate under the Liquidity Adjustment Facility (LAF) remains 5.75 per cent, and the Marginal Standing Facility (MSF) rate is 6.75 per cent.

The Reserve Bank of India (RBI) also refined its monetary policy framework in April 2016, with the objective of meeting short-term liquidity needs through regular facilities; frictional and seasonal mismatches through fine-tuning operations and more durable liquidity by modulating net foreign assets and net domestic assets in its balance sheet. The Monetary Policy Committee so far has gone by the script.

1) Liquidity Situation

The RBI has been managing liquidity following its liquidity management framework. In order to bring ex ante liquidity conditions close to neutrality it has pumped durable liquidity through open market operations (OMOs). Post the withdrawal of specified bank notes (SBNs), RBI has conducted exceptional operations to mop the large surplus liquidity through variable reverse repo rate. To complement the RBI's efforts, the Government also increased the limit on securities under market stabilisation scheme from Rs. 30,000 crore to Rs. 6 lakh crore. Liquidity conditions were generally tight during Q1 of 2016-17. The condition eased significantly in the subsequent months barring one or two exceptional episodes. The weighted average call money rate (WACR), on an average has been hovering around policy rate without crossing the upper and lower bounds of the corridor.

2) Yield on Government bills/ securities

There was a sharp fall in the 91 days t-bill rate in April 2016 owing to 25 bps cut in repo rate. Ten years government security (G-sec) yield however continued to tread high in spite of the rate cut and in fact increased marginally after the rate cut . However, yield on G-sec started softening since June 2016. As of 30th December 2016, 10-year G-sec yield stood at 6.63 per cent.

The transmission of the rate cuts, however, remained far from perfect. Base rate came down marginally from 9.30/9.70 in April 2016 to 9.30/9.65 as of 30th December 2016. Term deposit rates for greater than one-year maturity period declined from 7.00/7.50 to 6.50/7.00 in this period.

3) Banking Sector

The performance of the banking sector, public sector banks (PSBs) inparticular, continued to be subdued in the current financial year. The asset quality of banks deteriorated further. The gross non-performing assets (GNPA) to total advances ratio of scheduled commercial banks (SCBs) increased to 9.1 per cent from 7.8 per cent between March and September 2016. Profit after tax (PAT) contracted on year-on -year basis in the first half of 2016-17 due to higher growth in risk provisions, loan write-off and decline in net interest income.

4) Credit Growth

Non- food credit (NFC) outstanding grew at sub 10 per cent for all the months except for September 2016 . Credit growth to industrial sector remained persistently below 1 per cent during the current fiscal, with contraction in August, October and November. However, bank credit lending to agriculture and allied activities (A&A) and personal loans (PL) segments continue to be the major contributor to overall NFC growth.

5) Measures to Strengthen Corporate Bond Market

The RBI took a number of measures to strengthen the corporate bond market in india. It accepted many of therecommendations of the Khan Committee to boost investor participation and market liquidity in the corporate bond market. The new measures as announced by the RBI include:

a) Commercial banks are permitted to issue rupee-denominated bonds overseas (masala bonds) for their capital requirements and for financing infrastructure and affordable housing;
b) brokers registered with the Securities and Exchange Board of India (SEBI) and

authorized as market makers in corporate bond market permitted to undertake repo / reverse repo contracts in corporate debt securities. This move will make corporate bonds fungible and thus boost turnover in the secondary market;

c) banks allowed to increase the partial credit enhancement they provide for corporate bonds to 50 per cent from 20 per cent. This move will help lower-rated corporates to access the bond market;

d) permitting primary dealers to act as market makers forReserve government bonds, to give further boost to government securities by making them more accessible to retail investors; and

e) to ease access to the foreign exchange market for hedging in over the counter (OTC) and exchange-traded currency derivatives, the RBI has allowed entities exposed to exchange rate risk to undertake hedge transactions with simplified procedures, up to a limit of US$30 million at any given time.

6) Indian Markets Performance

Indian markets recorded modest growth of 1.95 – 3 per cent (Sensex was up by 1.95 per cent while Nifty was higher by per cent) for the calendar year 2016 as compared to losses registered in 2015. The upward momentum, visible in the Indian markets peaked around September 2016, lost steam thereafter particularly in the wake of foreign capital outflow from emerging markets. Global and domestic factors had a sizable impact on the performance of the Indian markets. Some of the closely watched developments were the Brexit, the US Presidential elections as well as policy announcements by the US Federal Reserve and the RBI. In addition, other factors which weighed on market sentiment included the policy decisions taken by the OPEC regarding oil production and the appointment of the new governor of the RBI

7) Foreign Portfolio Investments

For the first time since the meltdown of 2008, Net Foreign Portfolio Investments (FPI) have turned negative (implying that there was an outflow from the Indian markets to the tune of Rs. 23079 crore) (Table 1). The FPI outflow was not a phenomenon associated with Indian markets alone as FPIs pulled out of most EMEs in a big way due to higher returns in advanced economies.

Table 1. Net FPI/FII Investment in India in 2010-2016 (in Rs. Crore)

Segments	2010	2011	2012	2013	2014	2015	2016
Equity	133266	-2714.3	128360	113136	97054	17808	20568
Debt	46408	42067	34988	-50849	159156	45857	-43647
Total	**179674**	**39352.9**	**163348**	**62286**	**256213**	**63663**	**-23079**

Source: NSDL

B. India's Merchandise Trade

1) Exports

In line with subdued global growth and trade, India's exports declined by 1.3 per cent and 15.5 per cent in 2014-15 and 2015-16 respectively. The trend of negative growth was reversed somewhat during 2016-17 (April-December), with exports registering a growth of 0.7 per cent to US$ 198.8 billion from US$ 197.3 billion in 2015-16 (April-December). During 2016-17 (April-December) Petroleum, oil and lubricants (POL) exports constituting 11.1 per cent of total exports declined by 9.8 per cent to US$ 22.0 billion over corresponding previous period, while non POL exports grew by2.2 per cent to US $ 176.8 billion. A large number of export sectors have moved to positive growth territory in April-November 2016-17 as compared to 2015-16 (Table 2).

Region-wise, India's exports to Europe, Africa, America, Asia and CIS and Baltics declined in 2015-16. However, India's exports to Europe, America and Asia increased by 2.6 per cent, 2.4 per cent and 1.1 per cent respectively in 2016-17 (April-November), while exports to Africa declined by 13.5 per cent. USA followed by UAE and Hong Kong were the top export destinations.

Table 2. Export Performance of some important sectors

	2015-16	**2016 (Apr-Nov) (P)**
Positive Growth	Chemicals and related* products {0.6}	• Ores and minerals { 35.3 } • Marine products { 20.6} • Gems and Jewellery {11.6} • Electronic goods {3.0 } • Engineering goods {0.9}
Negative Growth	• Textiles {-3.2} • Gems and Jewellery {-4.8} • Electronic goods {-5.3} • Leather {-10.3} • Marine products {-13.5} • Ores and minerals {-16.4} • Engineering goods {-17.0} • Agriculture and allied products {-17.6} • Petroleum products {-46.2}	• Chemicals and related products* { -0.5 } • Agriculture and allied products { -3.0} • Leather { -4.8} • Textiles { -5.2} • Petroleum products { -9.8}

Source: Department of Commerce

***Note:* Figures in bracket { } indicates growth rate y-o-y. *: including plastic & plastic products.P: Provisional as per quick estimates**

2) *Imports*

Value of imports declined from US$ 448 billion in 2014-15 to US$ 381 billion in 2015-16, mainly on account of decline in crude oil prices resulting in lower levels of POL imports. During 2016-17 (April-December) imports declined by 7.4 per cent to US$ 275.4 billion compared to the corresponding period of previous year. POL imports declined by 10.8 per cent. Gold and silver imports declined by 35.9 per cent and non-POL and non-gold & silver imports by per cent. Positive growth was registered in pearls and semi-precious stones (19.0 per cent) and Food and allied products (1.3 per cent). Imports of capital goods declined by per cent. India's imports from Europe, Africa, America, Asia and CIS & Baltics regions declined in 2015-16. However, in 2016-17 (April-November), imports from CIS & Baltics region increased by 10.3 per cent while other four regions witnessed decline. Top three import destinations of India were China followed by UAE and USA in 2016-17 (April-November).

3) *Trade deficit*

8.33 In 2015-16, India's trade deficit declined by 13.8 per cent (vis-à-vis 2014-15) to US$ 118.7 billion. Furthermore, it declined by 23.5 per cent to US$ 76.5 billion in 2016-17 (April-December) as compared to US$ 100.1 billion in the corresponding period of previous year.

C. *Balance Of Payments*

1) *Current account*

Despite moderation in India's exports, India's external sector position has been comfortable, with the current account deficit (CAD) progressively contracting from US$ 88.2 billion (4.8 per cent of GDP) in 2012-13 to US$ 22.2 billion (1.1 per cent of GDP) in 2015-16. The CAD further narrowed in 2016-17 (H1) to 0.3 per cent of GDP. In 2016-17 (H1), sharp contraction in trade deficit outweighed the decline in net invisible earnings. The downward spiral in international crude oil prices resulted in a decline in oil import bill by around 18 per cent which together with a sharp decline in gold imports led to a reduction in India's overall imports (on BoP basis). Net services receipts declined by 10 per cent in H1 of 2016-17 despite increase in services receipts (4.0 per cent) as growth in services payments was higher (16 per cent). However, growth of receipts of software was marginal and financial services receipts declined. Subdued income conditions in source countries, particularly in the gulf region due to downward spiral in oil prices continued to weigh down on remittances by Indians employed overseas as private transfers moderated to US$ 28.2 billion in H1 of 2016-17 from US$ 32.7 billion in H1 of 2015-16.

2) ***Capital/finance account***

Despite higher net repayments on overseas borrowings and fall in banking capital (net) with building up of foreign currency assets by banks &decline in NRI deposits (net), robust inflow of foreigndirect investment (FDI) and net positive inflow of foreign portfolio investment (FPI) were sufficient to finance CAD leading to an accretion in foreign exchange reserves in H1 of 2016-17. The net FDI flows of US$ 21.3 billion recorded a growth of about 29 per cent over the corresponding period of last year. There was net inflow of portfolio investment amounting to US$ 8.2 billion in H1 of 2016-17 as against outflow of US$ 3.5 billion in H1 of 2015-16. Banking capital recorded net outflow of US$ 6.8 billion, primarily on account of acquisition of foreign currency assets by banks, while net repayment of external commercial borrowings resulted in an outflow of US$ 4.6 billion in H1 of 2016-17. With net capital flows remaining higher than the CAD, there was net accretion to India's foreign exchange reserves (on BoP Basis) (Table 3).

Table 3. Summary of Balance of Payments (US $ billion)

	2013-14	2014-15	2015-16	2015-16	2016-17
	(April-March)			H1	H1
Trade balance	-147.6	-144.9	-130.1	-71.3	-49.5
Net services	73.1	76.5	69.7	35.6	32.0
Invisibles (net)	115.2	118.1	107.9	56.7	45.7
Current Account Balance	-32.4	-26.9	-22.2	-14.7	-3.7
Total Capital/ Finance A/C (Net)	47.9	88.3	40.1	25.3	19.2
Reserve Movement (- increase) and (+ decrease)	-15.5	-61.4	-17.9	-10.6	-15.5
Trade balance/GDP(per cent)	-7.9	-7.1	-6.3	-7.1	-4.6
Invisible Balance/GDP (per cent)	6.2	5.8	5.2	5.7	4.3
Current Account Balance/GDP (per cent)	-1.7	-1.3	-1.1	-1.5	-0.3
Net Capital Flows/GDP (per cent)	2.6	4.3	1.9	2.5	1.8

***Source:* RBI**

3) ***Foreign Exchange Reserves***

In H1 of 2016-17, India's foreign exchange reserves increased by US$ 15.5 billion on BoP basis (*i.e.*, excluding valuation effects), while in nominal terms (*i.e.*, including valuation effect) the increase was to the tune of US$ 11.8 billion. The loss due to valuation changes of US$ 3.7 billion mainly reflects the appreciation of the US dollar against major currencies.

4) ***Exchange rate***

Inflows on account of FIIs, particularly into the equity segment, and positive sentiments generated by a narrower CAD in H1 of 2016-17 helped the rupee to move in a narrow range. The subsequent depreciation of the rupee could be attributed largely to the strengthening of the US dollar globally following the US presidential election results and tightening of monetary policy by the Federal Reserve. Nevertheless, in 2016-17 so far, the rupee has performed better than most of other emerging market economies (EMEs). During 2016-17 (April-December), on y-o-y basis, the rupee depreciated by 3.4 per cent against US dollar as compared to the depreciation of Mexican peso (14.4 per cent), South African Rand (8.6 per cent) and Chinese renminbi (6.3 per cent). The rupee depreciated in terms of nominal effective exchange rate (NEER) against a basket of 6 and 36 currencies during April-December 2016. However, the 6-currrency and 36-currency REER (Trade-based; Base year: 2004-05=100) appreciated by 6.1 per cent and 5.6 per cent, respectively as at end-December 2016 over end-March 2016.

III. CONCLUSION

The investment to GDP ratio has not only been lower than the desirable levels but has been consistently declining over the last few years. This trend needs to be reversed at the earliest in order to realise higher and lasting economic growth. Similarly, the savings rate will have to be raised, so that investment can be financed without resorting to high dose of external financing. After remaining fairly stable for much of the last two years, international prices of crude oil have started to trend up. This along with rise in the prices of other commodities like coal, etc. could exert inflationary pressure and have the potential to adversely impact the trade and fiscal balances. The outlook for the next financial year suggests that growth is set to recover, as the currency in circulation returns to normal levels and taking into account the significant reform measures initiated by the government. Thus the aim of the study is to understand the monetary management and financial intermediation of India and to understand the India's merchandise trade in terms of export, import and trade deficit and to study the Balance of payments of India

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