I. ECONOMIC ENVIRONMENT

(1) OVERVIEW

1. During the period under review (2007 to end-April 2011), India continued to reap the benefits from the process of trade liberalization and structural reform initiated in the early 1990s. Annual real GDP growth averaged over 8.4% between 2006/07 and 2010/11, despite the effects of the global economic crisis, which only caused a mild slowdown. The Government conducted a very proactive policy to face the crisis, introducing a large stimulus package consisting of increased spending, lower excise and customs duties on some products, and subsidies. However, as the economy started to get back on track and as inflation started to accelerate, the Government reversed most of these stimulus measures. As has been the case for some years now, growth has been led by services and manufacturing, the two largest sectors, with agriculture growing much more slowly. India's growth prospects remain strong, as potential GDP growth has been estimated at between 8% and 8.5%. However, to achieve sustained growth at the potential rate, bottlenecks will need to be eliminated and investment will be needed in infrastructure and education. The business environment will also need to be simplified by streamlining the regulatory environment, and defining a more stable and transparent trade and investment policy.

2. India embarked on a process of fiscal consolidation in 2004. This has not resulted in the intended decrease in the fiscal deficit, partly due to the effects of the global crisis. Although progress has been made towards fiscal consolidation, achieving it remains a challenge for India, in particular considering its infrastructure needs and growth targets. Throughout the period under review, India continued to post sizeable public-sector deficits. India's public finances deteriorated partly as a result of lower revenue and the impact of the stimulus package in the wake of the global financial crisis; the consolidated fiscal deficit reached 9.5% of GDP in 2009/10. Although the consolidated deficit declined to some 7.3% of GDP, this reduction largely reflects the effect of one-off items, though revenue collection in general also increased. The focus of fiscal policy has been shifted back to achieving consolidation and tax rationalization. A new tax Code has been drafted to simplify the tax regime and increase reliance on direct rather than indirect taxes.

3. Strong domestic demand and rising oil prices have resulted in a widening of the trade deficit, leading to a current account deficit throughout the reviewed period. The deficit has been financed through large capital inflows, both foreign direct and portfolio investment, attracted by the expanding domestic demand and the good prospects of the economy. Capital inflows have been somewhat volatile and this volatility has been largely accommodated by letting the exchange rate adjust. Although the floating exchange rate regime has served India well in accommodating substantial capital inflows, policies need to be designed to attract more medium- and long-term capital, particularly given India's infrastructure and general investment needs. A step in this direction is the Government's recent decision to increase investor limits in the corporate bond and government bond markets.

(2) RECENT ECONOMIC DEVELOPMENTS

4. During the review period, the Indian economy continued to expand at a fast pace, despite the mild slowdown caused in 2008/09 by the global financial crisis. Annual real GDP growth averaged over 8.4% between 2006/07 and 2010/11, supported primarily by strong domestic demand. Growth was particularly strong in 2006/07 and 2007/08, exceeding 9% (Table I.1), driven mainly by private investment and, to a lesser extent, private consumption. In the wake of the global financial crisis, growth has been driven by government spending. Strong domestic demand led to a sharp increase in

imports, particularly in 2008/09, only partly offset by a rise in exports. Although both import and export levels declined slightly in 2009/10, they remained considerably above those of 2006/07 (see sections (5) and (6)). The Government estimates that GDP growth reached 8.6% in 2010/11.[1] GDP growth at 2004/05 market prices reached 10.1% at an annual rate in the April-December 2010 period.

Table I.1
Selected macroeconomic indicators, 2006-11

	2006/07	2007/08	2008/09	2009/10[a]	2010/11[a]
Real GDP at factor cost (Rs billion, 2004/05 prices)	35,660.1	38,989.6	41,625.1	44,937.4	..
Real GDP at factor cost (US$ billion, 2004/05 prices)	787.5	968.9	906.5	947.7	..
Real GDP at market prices (Rs billion, 2004/05 prices)	38,746.3	42,479.2	44,653.6	48,693.3	53,425.7
Real GDP at market prices (US$ billion, 2004/05 prices)	855.6	1,055.6	972.5	1,013.8	..
Current GDP at factor cost (Rs billion)	39,522.4	45,814.2	52,820.9	61,332.3	..
Current GDP at factor cost (US$ billion)	872.8	1,138.5	1,150.4	1,293.5	..
Current GDP at market price (Rs billion)	42,936.7	49,864.3	55,826.2	65,502.7	..
Current GDP at market price (US$ billion)	948.1	1,239.1	1,215.8	1,381.4	..
GDP per capita at current market price (Rs)	38,268.0	43,817.5	48,376.3	55,985.2	..
GDP per capita at current market price (US$)	845.1	1,088.9	1,053.6	1,180.7	..
Real GDP (at 2004/05 factor cost)	9.6	9.3	6.8	8.0	8.6
National accounts			(% change)		
Real GDP at market prices (2004/05 prices)	9.4	9.6	5.1	9.1	10.1
Consumption	7.5	9.8	8.3	8.7	7.7
Private consumption	8.2	9.8	6.8	7.3	8.3
Government consumption	3.8	9.7	16.7	16.4	4.7
Gross fixed capital formation	14.3	15.2	4.0	7.3	16.1
Exports of goods and non-factor services	24.5	26.6	15.0	5.8	..
Imports of goods and non-factor services	22.7	31.6	16.6	0.0	..
Unemployment rate (%)	7.3	..	..	..	..
Prices, interest rates and money			(%)		
Inflation (%age change)					
CPI - industrial workers	6.7	6.2	9.1	12.4	10.6[b]
WPI	6.5	4.8	8.0	3.6	9.0[c]
Deposit rate[d]	7.5-9.0	8.25-8.75	8.0-8.75	6.0-7.0	8.25-9.0
Prime lending rate[e]	12.25-12.5	12.25-12.75	11.5-12.5	11.0-12.0	8-25-9.50[f]
M3	21.7	21.4	19.3	16.8	15.9
Exchange rate					
Rs/US$ (financial year - annual average)	45.28	40.24	45.92	47.42	45.58
Real effective exchange rate (%age change)[g]	-1.6	8.2	-8.7	0.2	13.4
Nominal effective exchange rate (%age change)[g]	-3.9	7.6	-13.0	-3.4	5.7
			(% of GDP, unless otherwise indicated)		
Central Government balance					
Current (revenue) balance	-1.9	-1.1	-4.5	-5.2	-3.4
Current revenue (revenue receipts)	10.1	10.9	9.7	8.7	9.9
Tax revenue (net)	8.2	8.8	7.9	7.0	7.2
Current expenditure (revenue expenditure)	12.0	11.9	14.2	13.9	13.4
Capital receipts	3.5	3.4	6.2	6.9	5.5
Capital expenditure	1.6	2.4	1.6	1.7	2.1
Gross fiscal balance[h]	-3.3	-2.5	-6.0	-6.3	-5.1
Primary deficit	0.2	0.9	-2.6	-3.1	-2.0
Central Government total debt	59.1	56.9	56.6	53.7	49.9
Domestic debt	56.7	54.7	54.4	51.5	47.9
External debt	2.4	2.2	2.2	2.1	2.0

Table I.1 (cont'd)

[1] Ministry of Finance (2011a), Chapter 1: State of the Economy and Prospect.

	2006/07	2007/08	2008/09	2009/10[a]	2010/11[a]
Saving and investment					
Gross domestic savings	34.6	36.9	32.2	33.7	..
Public sector	3.6	5.0	0.5	2.1	..
Gross domestic investment	35.9	38.0	35.4	35.8	..
Public sector	8.3	8.9	9.5	9.2	..
External sector					
Current account balance	-1.0	-1.3	-2.3	-2.8	-3.1[i]
Net merchandise trade	-6.5	-7.4	-9.8	-8.6	-8.3[i]
Merchandise exports	13.6	13.4	15.4	13.2	13.9[i]
Merchandise imports	20.1	20.8	25.2	21.7	22.2[i]
Services balance	3.1	3.1	4.4	2.6	2.9[i]
Capital account	4.7	8.6	0.5	3.8	4.3[i]
Direct investment	0.8	1.3	1.6	1.4	0.6[i]
Balance of payments	3.8	7.4	-1.7	1.0	0.9[i]
Terms of trade, (1978/79=100)	76.7	79.0	81.2	91.2	..
Merchandise exports (%age change)[j]	25.1	14.6	28.4	0.5	27.0[i]
Growth rate based in US$	22.6	28.9	13.7	-3.6	33.3[i]
Merchandise imports (%age change)[j]	24.1	20.0	35.7	1.3	21.1[i]
Growth rate based in US$	21.4	35.1	19.8	-2.6	27.1[i]
Service exports (%age change)[j]	30.3	9.0	34.4	-7.1	34.5[i]
Growth rate based in US$	28.0	22.4	17.3	-9.6	41.2[i]
Service imports (%age change)[j]	30.7	3.4	15.9	18.3	44.6[i]
Growth rate based in US$	28.5	16.2	1.1	15.3	51.7[i]
Foreign exchange reserves[k] (US$ billion, end-period)	191.9	299.2	241.4	254.7	304.8[i]
In months of imports	12.5	14.4	9.8	11.1	..
Total external debt (US$ billion, as at end-March)	172.4	224.4	224.5	261.2	279.5[l]
Debt service ratio[m]	4.7	4.8	4.4	5.5	3.9 [l]

.. Not available.

a Provisional.
b April 2010 to February 2011
c March 2010/March 2011.
d Refers to the deposit rates of five major public sector banks of maturity of one to three years, as at end-March.
e Benchmark prime lending rate of five major public sector banks (period average).
f Base rate
g Six-currency trade based weight (including the euro, Japanese yen, U.S. dollar, U.K. pound, Chinese renminbi, and H.K dollar).
h Revenue receipts plus capital receipts (not including borrowing and other liabilities) minus total expenditure.
i April to December 2010.
j Growth rates are based on national currency.
k Excluding gold, SDRs (Special Drawing Rights), and Reserve Tranche Position in IMF.
l As at end-December 2010.
m Including debt-servicing on non-civilian credits.

Sources: Ministry of Finance (2011), *Economic Survey 2010-11*. Viewed at: http://indiabudget.nic.in/; Reserve Bank of India (2010), *Handbook of Statistics of the Indian Economy*, 15 September. Viewed at: http://www.rbi.org.in/scripts/AnnualPublications.aspx?head=Handbook of Statistics on Indian Economy; Reserve Bank of India (2011), *Macroeconomic and Monetary Developments in 2010-11*, 2 May; and information provided by the Reserve Bank of India.

5. The IMF estimates India's GDP growth potential to be some 8.5% per year; the authorities consider the post-global-crisis growth potential to be of some 8%.[2] Achieving this in a context of a lesser reliance on public consumption and investment will imply boosting private investment, which, over the medium run will require a simplification of the business and regulatory environment, as well as facing the challenges of improving infrastructure to overcome the current shortcomings.

[2] Reserve Bank of India (2010a), p. 17.

6. Services continued to be the most dynamic sector during the period under review, expanding at an average annual rate of around or over 10%, thus exceeding GDP growth, and exhibiting resilience to the negative effects of the global crisis. Growth in services continued to be led by the financial sector, and the trade, hotel, transport, and communications subsectors. Manufacturing showed robust growth over 2006/07 and 2007/08, but was subsequently affected by the global economic crisis, which led to a decline in foreign demand, particularly in areas such as textiles and clothing. There was a resurgence of growth, however, in 2009/10, triggered mainly by stronger domestic demand, particularly for consumer durables, capital goods, and industrial inputs; the production of non-durable goods showed only a modest increase.[3] Growth in agriculture remained weak throughout most of the review period due to a prolonged drought, excessive reliance on monsoon-related crops, and low productivity.

7. The services sector is the largest contributor to GDP; its share of GDP increased from 53% in 2006/07 to 56% in 2009/10 (Table I.2), while the share of manufacturing declined somewhat, from 16.1% to 15.5% and the share of agriculture fell from 18.1% to 16.6%. The authorities have noted that, despite the decline in its relative share, agriculture continues to be the mainstay of the majority of the population, occupying some 52% of the total workforce (including non-organized labour); the sector is also critical for achieving the Government's objectives of food security and price stability.[4]

Table I.2
Basic economic and social indicators, 2006-11

	2006/07	2007/08	2008/09	2009/10	2010/11[a]
			Annual % change		
GDP by economic activity at constant 2004/05 prices					
Agriculture, forestry, and fishing	4.2	5.8	0.1	0.4	5.4
Mining and quarrying	7.5	3.7	1.3	6.9	6.2
Manufacturing	14.3	10.3	4.2	8.8	8.8
Electricity, gas, and water	9.3	8.3	4.9	6.4	5.1
Construction	10.3	10.0	5.5	6.7	8.0
Services	10.1	10.3	10.1	10.1	9.4
Trade, hotels, transport, and communication	11.6	11.0	7.5	9.7	11.0
Financing, insurance, real estate, and business services	14.0	11.9	12.5	9.2	10.6
Community, social, and personal services	2.9	6.9	12.7	11.8	5.7
			%		
Share of main sectors in current GDP at factor cost					
Agriculture, forestry, and fishing	18.3	18.3	17.6	17.8	..
Mining and quarrying	2.7	2.7	2.6	2.5	..
Manufacturing	16.1	16.0	15.5	14.8	..
Electricity, gas, and water	1.9	1.8	1.6	1.5	..
Construction	8.2	8.5	8.6	8.1	..
Services	53.0	53.1	54.6	56.0	..
Trade, hotels, transport, and communication	25.3	25.3	24.9	24.4	..
Financing, insurance, real estate, and business services	14.9	15.2	16.2	17.0	..
Community, social, and personal services	12.8	12.6	13.4	14.6	..

Table I.2 (cont'd)

[3] Reserve Bank of India (2010a), p. 23.

[4] Reserve Bank of India (2010a), p. 16. Most of the people employed in agriculture do not fall under the category of organized employment, which explains why the share of agriculture in total organized employment (shown in Table I.2) is so low.

	2006/07	2007/08	2008/09	2009/10	2010/11[a]
Share of sector in total employment[b]					
Agriculture, forestry, and fishery	5.3	5.4	..	..	..
Mining and quarrying	4.6	4.5	..	..	..
Manufacturing	21.7	22.2	..	..	..
Electricity, gas, and water	3.3	3.1	..	..	..
Construction	3.5	3.4	..	..	..
Services	61.7	61.4	..	..	..
Wholesale and retail trade	2.2	1.6	..	..	..
Transport, storage, and communication	10.2	10.1	..	..	..
Financing, insurance, real estate, etc.	8.3	9.0	..	..	..
Public administration and defence, and other services	41.0	40.7	..	..	..

.. Not available.

a Advance estimate.
b Organized sector employment only.

Source: Ministry of Finance (2011), *Economic Survey 2010-11*. Viewed at: http://indiabudget.nic.in/; Reserve Bank of India (2010), *Handbook of Statistics of the Indian Economy*, 15 September. Viewed at: http://www.rbi.org.in/scripts/AnnualPublications.aspx?head=Handbook of Statistics on Indian Economy; and Reserve Bank online information. Viewed at: http://www.rbi.org.in/home.aspx.

8. During the period under review, increasing commodity and oil prices and supply-side constraints, together with fast economic growth, in particular strong domestic demand, resulted in an acceleration of headline inflation as measured by the new wholesale price index (WPI) during most of the period under review (with the exception of FY 2008/09).[5] The WPI increased by 9% in the 12-month period ending in March 2011 (8.3% in the 12 months to February 2011).[6] The Government's headline inflation estimate for 2011 was increased from 7% to 8% in early 2011.[7] Core inflation (excluding food and energy) has proceeded at a similar pace than headline inflation, increasing also by 9% in the twelve months till March 2011. Although administered prices (fuels and fertilizers) were adjusted during the period under review and steps taken to deregulate fuel prices (see below), inflation figures may be underestimated due to the subsidization of some fuel prices, certain basic food prices, and electric power rates.

9. The Government has undertaken a number of measures to fight inflation, including monetary, fiscal, and administrative actions; the last two include measures that have an effect on trade. With respect to monetary measures, the RBI has tightened monetary policy by raising its policy rates several times since early 2010 (see below), and narrowing the liquidity adjustment facility (LAF) corridor to reduce rate volatility. Fiscal measures have included customs duty reductions, e.g. a reduction to zero of import duties on rice, wheat, pulses, onions and shallots, edible oils (crude), and ghee, and to 7.5% on refined and hydrogenated oils and vegetable oils; also imports of raw sugar at zero duty have been allowed under a licensing system.[8]

10. Trade-related administrative measures have also been used, such as export prohibitions (e.g. on non-basmati rice, onions, and edible oils (see Chapter IV(2)) and minimum export prices (onions and basmati rice). The authorities have indicated that these measures were taken in view of

[5] A new WPI series with a 2004-05 basis was released in September 2010. The new series has a commodity basket comprising 676 items with different weights and more price quotations than the previous one.

[6] This average is considerably higher than the ten-year average of headline WPI inflation from 2000-01 to 2009-10, which was of some 5.3%. See Ministry of Finance (2011a), Chapter 4: Prices and Monetary Management.

[7] Reserve Bank of India (2011b).

[8] Ministry of Finance (2011a), Chapter 4: Prices and Monetary Management.

the emerging scenario of scarcity and the consequent rise in prices of essential commodities. An Inter-Ministerial group was set up in early 2011 under the Ministry of Finance, to review the overall inflation situation, with particular reference to primary food articles. The group may recommend action on fiscal, monetary, production, marketing, distribution, and infrastructure matters to prevent price increases, but its recommendations are not binding.

11. India does not publish official unemployment figures. The latest available information points to an unemployment rate of 7.3% in 2006/07. Since then, the Government has conducted surveys to assess the conditions of the labour market; no complete employment figures are available. The authorities have indicated that this is due to the relatively large segment of non-organized (not formally employed) workers, and that only figures for organized employment are available. Total organized employment in 2008 was 275.5 million, of which 176.7 million were employed by the public sector and 98.8 million by the private sector.[9] The Ninth Quarterly Quick Employment Survey, conducted by the Labour Bureau, shows that, during 2010, organized employment increased by 870,000 persons; some 60% of this increase was in information technology and business process outsourcing. With respect to the sectoral distribution of employment, it is estimated that some 22% of organized labour is employed in the manufacturing sector. Agriculture accounts for just over 5% of total organized employment but this figure is misleading, as most agriculture labourers are not unionized or otherwise organized. It is estimated that over 50% of India's workforce is employed in the agricultural sector. Services accounts for over 60% of organized employment.

12. High economic growth has translated into rising per capita incomes. GDP per capita at current market prices reached US$1,180.7 in 2009/10, some 40% higher than in 2006/07. Growth has also improved social and poverty indicators, with infant mortality declining from 68 per 1,000 in the mid 1990s to 52 per 1,000 in 2008, and literacy levels reaching 66% of people over 15 in 2008, up from 49% in 1990.[10] Despite high growth, however, poverty alleviation remains a challenge. There are no recent statistics, but data from the Planning Commission show that 27.5% of the population lived under the poverty line in 2004/05, down from 36% in 1993/94.[11] However, a 2009 study by an expert group, found a 37.2% poverty ratio for 2004/05.[12] Although these levels are considerably below those of a decade ago, there is still a large number of poor, especially in the rural areas.

(3) FISCAL POLICY

13. India's public finances deteriorated in the wake of the global financial crisis. The 2009/10 consolidated fiscal deficit reached 9.5% of GDP, up from 8.5% in 2008/09, with the Central Government deficit at 6.4% of GDP, and state government deficits of 3.3% of GDP. After two years of increasing deficits, the consolidated deficit declined to some 7.3% of GDP in 2010/11, as both central and state government deficits fell, to 5.5% and 2.5% of GDP, respectively. This reduction in the deficit largely reflects the effect of one-off items (e.g. telecommunications licences), although an increase in general revenue also played a role. While progress has been made towards fiscal consolidation, achieving it remains a challenge for India, in particular considering its infrastructure needs and growth targets. Fiscal consolidation would also be an important step to prevent an excessive real exchange rate appreciation, which would lead to further deterioration of the current account of the balance of payments.

[9] Planning Commission of India (2011).
[10] World Bank (2011).
[11] The poverty level in India is defined on the basis of calorie intake of 2,100 kilocalories in urban areas and 2,400 kilocalories in rural areas.
[12] Planning Commission of India (2011).

14. For part of the period under review, fiscal policy has been conducted within the framework of the Fiscal Responsibility and Budget Management Act (FRBMA), notified in 2004, which calls for the Central Government to take measures to reduce the revenue (current) and overall fiscal deficits with a view to eventually eliminating them. Tax revenue growth was instrumental in allowing progress toward fiscal consolidation prior to the global financial crisis. Gross tax revenue rose as a proportion of GDP, from 9.2% in 2003/04 to a peak of 12% in 2007/08, before falling to 10.9% and 9.5% in 2008/09 and 2009/10, respectively. Tax revenue net of states' shares was only 7% of GDP in 2009/10, down from a pre-crisis level of 8.8%, partly on account of lower excise and customs duty collection (Table I.3). Tax revenue/GDP was expected to recover to 10.8% in 2010/11, but advance estimates point to a 10% ratio. This is of concern since tax revenue continues to be insufficient to finance India's infrastructural and developmental needs.

Table I.3
Central Government's tax revenue, 2006-11
(Rs billion and %)

	2006/07	2007/08	2008/09	2009/10	2010/11[a]
Total tax revenue, net of states' share (Rs billion)	3,511.8	4,395.5	4,433.2	4,651.0	5,340.94
(% of GDP)	8.2	8.8	7.9	7.0	7.2
			(% of total tax revenue)		
Direct taxes	48.6	52.6	55.2	60.5	56.7
Corporation taxes	30.5	32.5	32.5	39.2	37.7
Personal income taxes	18.1	20.0	20.0	21.2	18.9
Wealth taxes	0.1	0.1	0.1	0.1	0.1
Indirect taxes	51.4	47.4	44.8	39.5	43.3
Customs	18.2	17.6	16.5	13.3	16.7
Union excise duties	24.8	20.8	17.9	16.5	17.4
Service taxes	7.9	8.6	10.1	9.4	8.8

a Estimates.

Source: Reserve Bank of India (2010), *Handbook of Statistics of the Indian Economy*, 15 September. Viewed at: http://www.rbi.org.in/scripts/AnnualPublications.aspx?head=Handbook of Statistics on Indian Economy; and information provided by the Indian authorities.

15. India classifies its expenditure into revenue (current) and capital, and Plan and non-Plan (interest payments, subsidies, defence expenditure, payrolls, and pensions). The thrust of public expenditure management policies has been on containing non-Plan revenue expenditure and raising the levels of Plan expenditure, preferably capital expenditure. Defence expenditure and interest payments have been relatively stable during the period under review (at some 1.8%-2.2% of GDP and 3.1%-3.4%, respectively), and budgets have focused on streamlining expenditure on subsidies. However, due to the increase in subsidies to crude oil and fertilizers, and other subsidies to consumers during the global slowdown, their proportion of GDP rose from 1.3% in 2006/07 to 2.3% in 2008/09, before declining slightly to 2.2% in 2009/10, and to an estimated 2.1% of GDP in 2010/11. This recent improvement followed policy steps to deregulate the price of gasoline and increase, albeit modestly, the regulated prices of kerosene and LPG (liquefied petroleum gas) (Chapter III).

16. To counter the effects of the global financial crisis, India engaged in a policy of fiscal expansion, which was one of the largest among emerging economies, estimated at about 10% of GDP in both 2009 and 2010. As growth resumed at a faster pace than expected, the authorities, following the recommendations of the Thirteenth Finance Commission, changed policy course and returned to focusing on fiscal consolidation in the 2010/11 Budget, including through a partial withdrawal of the stimulus measures put in place during the crisis. The policy stance was shifted to addressing long-run sustainability concerns, while continuing to support growth in the short run. For example, the 2010/11 Budget recommended bringing expenditure down through a proper targeting of subsidies and

announced that new policies to reduce subsidies on fertilizers and petroleum products would be implemented.

17. The 2010/11 Budget reversed some of the measures adopted to face the crisis. The standard rate of excise duty (CENVAT), which had been lowered to 8% by two successive reductions, in December 2008 and February 2009, was raised to 10%. Excise duty on petrol and diesel was increased by Rs 1 per litre so as to restore the pre-June 2008 levels, while excise duty on cigarettes and other tobacco products, as well as of the *ad valorem* component of the excise duty on certain vehicles, was raised from 20% to 22%. Full or partial excise duty exemptions/concessions available on some items were withdrawn and duty imposed on them at the rates of 4% or 10%. The customs duties on crude petroleum and diesel were increased, and eight new services were brought under the service tax. On the other hand, the 2011/12 Budget seems to have placed more emphasis on growth; it contains provisions to lower customs duty rates, for example on imports of certain inputs and of agricultural machinery, to promote the development of agricultural and manufacturing production, and of exports.

18. The 2010/11 fiscal results were better than expected. While the Budget for 2010/11 had estimated the fiscal and revenue deficits at 5.5% and 4% of GDP, respectively, they were 5.1% and 3.4% of GDP, respectively. The lower deficits were partly due to higher-than-expected tax revenue due to economic growth and the termination of excise and customs duties reduction, but also to the substantial increase in non-tax revenues arising from telecom 3G/BWA (third generation/broadband wireless access) licence auctions, a one-time event (see Chapter IV(3)(iii)).

19. When India embarked on the path of economic reform in 1991/92, the ratios of direct and indirect taxes to gross tax revenue were 22.6% and 77.4%, respectively; in 2009/10 these ratios were of 60.5% and 39.5%, respectively (Table I.3). This was partly a result of the gradual reform of the tax structure to reduce customs and excise duties and rely more on direct taxes, particularly corporate income tax, and on service tax revenues. Union excise duties were the single largest revenue earner until 2006/07, when they were replaced by corporate income tax. The Government aims to improve direct tax collection through rationalization of the tax structure: to this end, the 2010/11 Budget reduced the surcharge on corporate income tax from 10% to 7.5%. The authorities are confident that tax rationalization will allow corporate and personal income tax collection to continue growing rapidly and help improve the prospects of revenue-led medium-term consolidation. However, indirect taxes, including taxes that fall solely or mainly on imports, continue to be an important source of revenue, and changes in their levels are a much used policy tool.

20. For several years the Government has been intent on introducing a goods and services tax (GST) and on consolidating the Income Tax Act 1961 and the Wealth Tax Act 1957 in a single law. In March 2011, a Constitutional Amendment Bill was introduced in Parliament for the implementation of the GST. The authorities indicated that, as at May 2011, progress has been made in creating the information technology infrastructure required for the implementation of the GST, including with respect to the creation of a GST network. They also indicated that work was under way on drafting model legislation for the implementation of the GST at the Central Government and State levels. With respect to the consolidation of the two tax acts, a Direct Taxes Code Bill was introduced in Parliament in August 2010, envisaged to be effective from 1 April 2012. The Direct Taxes Code Bill seeks to establish a more effective and equitable direct tax system and help increase the tax to GDP ratio. The proposed Code would do away with the current system of determining tax rates every year through an approved Finance Act, even if no tax changes take place, and replacing it by fixed Schedules (to the Code) containing the relevant tax rates. New legislation would only be

required when a change of rates is decided, thus enhancing the stability and predictability of the tax system.

21. The proposed Code also seeks to improve predictability with respect to the taxation of international transactions. It contains provisions to eliminate the differences in taxation on profits between foreign companies, currently taxed at 42.2% (inclusive of surcharge and cess) and domestic companies, taxed at 33.2% (inclusive of surcharge and cess). It is proposed to set both rates at 30%, and to levy a branch profit tax of 15% to replace the current dividend distribution tax of 16.6%. There are also provisions to enhance transfer-pricing stability in international transactions by introducing five-year advance pricing agreements.

22. The Code also modifies the current system of incentives, by phasing out profit-linked tax incentives, replacing them with investment-linked incentives. This is a very important step, since the persistence of the different incentives schemes has been costly for the Indian economy. It has resulted in forgone excise and customs duties revenue of Rs 4 trillion (US$88.9 billion), some 6.1% of GDP, in 2009/10. Revenue forgone due to corporate income tax exemptions was estimated at Rs 72.8 billion in 2009/10 (some US$1.61 billion), or 0.11% of GDP, while personal tax exemptions totalled Rs 45 billion (some US$995 billion, or 0.07% of GDP). Revenue forgone on account of various export promotion schemes was estimated at Rs 381 billion (US$8.5 billion, or 0.6% of GDP) in 2009/10.

23. The Government's debt-management policy objectives are to meet the Central Government's financing needs at the lowest possible long-term borrowing costs and to keep the total debt within sustainable limits, while reinforcing the development of a domestic bond market.[13] There are no explicit debt caps or limits. Reflecting the general fiscal consolidation policy thrust, the ratio of Central Government debt to GDP declined during the period under review, from 61.2% of GDP in 2005/06 to 53.7% in 2009/10, and is estimated at 49.9% in 2010/11. Some 92% of India's (Central Government) debt is domestic, most of it medium- to long-term, with a weighted average maturity period of ten years. Some 97% of the Central Government's debt is at fixed rates; the average interest rate is 7.8% per year.[14]

24. The net outstanding debt of state governments is estimated at 25% of GDP for 2009/10. The consolidated debt of the Government declined from 78.6% of GDP in 2004/05 to 71.4% in 2007/08, and 69.1% in 2009/10. Total debt was well below the 74% of GDP target recommended by the 12th Finance Commission.

25. FRBM Rules limited Central Government annual indebtedness to a maximum of 9% of GDP for 2004/05 to be reduced progressively by at least one percentage point of GDP in each subsequent financial year. Although there is no explicit public debt target, the Thirteenth Finance Commission recommended that action be taken to reduce the combined public debt to GDP ratio to 68% by 2014/15. A status paper with a roadmap for debt reduction was presented to Parliament in November 2010. The paper estimated that, at current GDP growth rates, the Central Government's debt as a proportion of GDP would decline to 43% in 2014/15, while the state governments' debt would fall more moderately, to 23.1% of GDP in the same fiscal year; the consolidated Government debt would decline from 73% of GDP in 2009/10 to 64.9% in 2014/15.

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[13] Ministry of Finance (2011a), Chapter 3: Fiscal Developments and Public Finance.
[14] Ministry of Finance (2011a), Chapter 3: Fiscal Developments and Public Finance.

(4) MONETARY AND EXCHANGE RATE POLICY

26. The Reserve Bank of India (RBI) formulates, implements, and monitors monetary policy. The RBI's objective to maintain price and financial stability and ensure an adequate flow of credit.[15] However, the RBI does not resort to inflation targeting. The RBI's Monetary Policy Department (MPD) formulates monetary policy, while the Financial Markets Department (FMD) handles day-to-day liquidity management operations. The Technical Advisory Committee (TAC) on Monetary Policy, created in July 2005, provides advice on monetary policy formulation. The RBI also acts as the Central Government's banker and debt manager, and acts as banker for the states that require it do so.

27. The RBI implements monetary policy through the use of several direct and indirect instruments based on an assessment made that takes into account indicators such as interest rates, the inflation rate, money supply and credit levels, exchange rate fluctuations, trade and capital flows, output trends, and the fiscal position.[16] The RBI's monetary policy operational target is the weighted average overnight money rate. The main direct instrument used to conduct monetary policy is the cash reserve ratio (CRR), followed by the statutory liquidity ratio (SLR) and refinance facilities.[17] The RBI uses the liquidity adjustment facility (LAF), as its main indirect instrument which enables it to adjust short-term liquidity through repo and reverse repo auctions.[18] The RBI also makes use of open market operations, and the Market Stabilization Scheme (MSS) to sterilize foreign inflows. Under the MSS, the RBI auctions government securities and keeps the equivalent cash balance in a special account. Since mid 2010, the RBI has not made much use of the MSS, opting for letting the exchange rate adjust.

28. Until May 2011, the RBI fixed three policy interest rates: the repo and reverse repo rates, and the Bank rate, which is the rate at which the RBI will buy or rediscount bills of exchange or other commercial papers. The first two rates signalled the short-term monetary policy stance, while the Bank rate signalled the medium-term stance. As of 3 May 2011, the repo rate is the only independently varying policy rate; the RBI expects that a single independently varying policy rate will more accurately signal the monetary policy stance.[19] The reverse repo was pegged to the repo rate at a rate fixed at 100 basis points below it, and a new Marginal Standing Facility (MSF) rate was created. The MSF is to be at 100 points above the repo rate (8.25% as at May 2011), and will enter into effect once the MSF becomes operational.[20]

29. In response to the global financial crisis, the RBI adopted an accommodative monetary policy stance in September 2008 to boost confidence and prompt economic growth.[21] As economic growth

[15] Reserve Bank of India online information, "About us". Viewed at: http://www.rbi.org.in/scripts/AboutusDisplay.aspx.

[16] Reserve Bank of India (2010b).

[17] The CRR is the share of net demand and time liabilities (NDTL) that banks must maintain as cash balance with the RBI; the SLR is the share of NDTL that banks must maintain in safe and liquid assets such as government securities, cash, and gold.

[18] The repo rate is the rate at which the RBI lends money to banks under the LAF; the reverse repo rate is the return earned by banks on funds deposited with the RBI.

[19] Reserve Bank of India (2011c).

[20] The new Marginal Standing Facility (MSF) will allow scheduled commercial banks to borrow overnight up to 1% of their respective NDTL.

[21] The measures the RBI took as a response to the global financial crisis, included: reductions in interest rates; loosened restrictions on access to foreign currency; the creation of a rupee-dollar swap facility to manage short-term funding requirements; the establishment of a refinancing window and special-purpose

accelerated in 2009/10 and headline inflation increased, the RBI partly shifted policy stance, restoring the statutory liquidity ratio (SLR) of scheduled commercial banks to its pre-crisis level. During 2010/11, the RBI continued to gradually abandon the accommodative policy stance and refocused monetary policy on containing inflation and inflationary expectations.[22] The RBI raised its policy rates seven times until April 2011, with the repo rate cumulatively rising by 200 basis points (bps) to 6.75% and the reverse repo rate by 250 bps to 5.75%. The CRR was kept at 6%, at which it stood in May 2011. In May 2011, following the change in policy stance to fix only one rate, the repo rate was increased to 7.25%, while the reverse repo was adjusted automatically to 6.25%.

30. The persistent liquidity pressure led the RBI to provide additional liquidity support to scheduled commercial banks in November 2010.[23] Subsequently, in December 2010, the RBI reduced the SLR of scheduled commercial banks from 25% to 24%. As at April 2011, growth remained strong and inflation was still significantly above the comfort level of the RBI, with risks on the upside, both from domestic demand and higher global commodity prices. One of the RBI's major challenges continues to be to supply the liquidity required while containing inflation and anchoring inflationary expectations.

31. India has had a managed float since 1993, with the exchange rate determined in the interbank market. The degree of intervention of the RBI to stabilize the market has varied over time; the RBI does not have a fixed or pre-announced target or band, and has intervened in the market when deemed necessary in accordance with its general monetary policy stance. The exchange rate policy in recent years has approached more a pure float, with the RBI intervening very little in the market. Maintaining a floating exchange rate helps India absorb external shocks and large inflows of capital.

32. After appreciating sharply in FY 2007/08 as a result of large capital inflows, the nominal effective exchange rate (NEER) depreciated in the aftermath of the global financial crisis. During the crisis and in its aftermath, the RBI focused less on the exchange rate, allowing for wider flotation and higher volatility. Since 2010, the nominal effective exchange rate has been appreciating.[24] The real effective exchange rate (REER) depreciated in 2008/09, but started appreciating in 2009/10; this appreciation has been modest even though inflation in India has been considerably higher than in countries whose currencies comprise its REER basket.[25]

33. Further currency appreciation is likely in the absence of fiscal tightening, particularly given the increasingly floating nature of the exchange rate regime. Estimating a real appreciation of the rupee of some 6% (as at December 2010) from its ten-year historical average, the IMF considers that further moderate REER appreciation would not have a significant negative impact on growth.[26] Moderate appreciation could be beneficial, particularly as it would make imports cheaper and help rein-in inflation, and it could lead to some self-correction, as it would reduce the attraction for

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vehicle for non-banking financial companies; and the expansion of funding sources for financial institutions to keep credit flowing to small and export businesses and for housing (Ministry of Finance, 2011a).

[22] Reserve Bank of India (2010e).

[23] The RBI has fixed a liquidity comfort level of +/- 1% of net demand and term liabilities. When liquidity departs too much from this range, the RBI intervenes through open-market operations or the MSS. The liquidity pressure observed in 2010 stemmed from a large build-up of Government cash balances, accompanied by a strong demand for credit.

[24] The NEER and REER baskets comprise: U.S. dollar, euro, yen, pound sterling, HK$, and the renminbi.

[25] Initially the rupee appreciated against the U.S. dollar, however this did not offset its depreciation against other currencies in its NEER basket resulting in the NEER depreciating.

[26] IMF (2011).

additional inflows. However, over the medium run, further appreciation would result in a worsening of the current account deficit, requiring further inflows of capital and or debt to finance it (see below).

(5) BALANCE OF PAYMENTS

34. India posts a structural trade deficit, partly explained by its large population and development needs. During the period under review, strong domestic demand and rising oil and food prices resulted in a widening of the trade deficit, leading to a current account deficit throughout the reviewed period. The trade deficit peaked at US$119.5 billion in 2008/09 (some 10% of GDP) (Table I.4), before declining somewhat in 2009/10. Partial data for 2010/11 shows an increase in the deficit, linked to higher growth rates and hence increased absorption, which translated into a substantial increase in imports, which more than offset the expansion in exports.

Table I.4
Balance of payments, 2006-11
(US$ million)

	2006/07	2007/08	2008/09	2009/10	2010/11[a]
Current account	-9,565	-15,737	-27,915	-38,383	-38,940
Goods and services balance	-32,313	-52,615	-65,604	-82,648	-82,648
Goods balance	-61,782	-91,467	-119,520	-118,374	-102,124
Exports f.o.b.	128,888	166,162	189,001	182,235	173,004
Imports c.i.f.	190,670	257,629	308,521	300,609	275,128
Services balance	29,469	38,852	53,916	35,726	34,246
Receipts	73,780	90,342	105,963	95,759	95,920
Transportation	7,974	10,014	11,310	11,177	10,133
Travel	9,123	11,349	10,894	11,859	10,757
Insurance	1,195	1,639	1,422	1,603	1,359
Software[b]	31,300	40,300	46,300	49,705	41,812
Business	14,544	16,772	18,603	11,368	17,846
Finance	3,106	3,217	4,428	3,736	4,900
Communication	2,262	2,408	2,298	1,229	1,166
Government n.e.s.	253	331	389	440	369
Other	4,023	4,313	10,319	4,642	7,578
Payments	44,311	51,490	52,047	60,033	61,674
Transportation	8,068	11,514	12,820	11,934	10,642
Travel	6,684	9,258	9,425	9,342	7,990
Insurance	642	1,044	1,130	1,286	1,099
Software[b]	2,267	3,358	2,564	1,469	1,869
Business	15,866	16,553	15,317	18,049	20,913
Finance	2,991	3,133	2,958	4,643	5,270
Communication	796	860	1,087	1,355	811
Government n.e.s.	403	376	793	526	543
Other	6,594	5,394	5,952	11,429	12,573
Income balance	-7,331	-5,068	-7,110	-8,040	-10.645
Credit	9,308	14,272	14,309	13,022	6,925
Debit	16,639	19,339	21,418	21,062	17,570
Current transfers	30,079	41,945	44,798	52,305	39,583
Credit	31,470	44,261	47,547	54,623	41,830
Debit	1,391	2,316	2,749	2,318	2,247
Capital account	46,171	107,901	7,835	51,824	49,959
Direct investment	7,693	15,893	19,816	18,771	7,606
Foreign direct investment in India	22,739	34,728	37,672	33,124	18,033
India's direct investment abroad	-15,046	-18,835	-17,855	-14,353	-10,427
Portfolio investment	7,060	27,433	-14,031	32,396	30,095
Loans, net	24,490	40,652	8,318	13,259	22,006
External assistance	1,775	2,114	2,441	2,893	4,190
Commercial borrowings[c]	22,715	38,538	5,877	10,366	17,816

Table I.4 (cont'd)

	2006/07	2007/08	2008/09	2009/10	2010/11[a]
Banking, net	1,913	11,759	-3,246	2,084	5,741
Rupee debt service	-162	-122	-100	-97	-17
Other capital, net	4,209	10,968	-3,990	-13,016	-12,699
Errors and omissions	968	1,316	1,067	-1,573	-2,773
Reserve assets (a minus sign denotes an increase)	-36,606	-92,164	20,080	-13,441	-11,019

a April to December 2010.
b Software services include computer services and information technology enabled services (ITES)/business process outsourcing (BPO).
c Includes short-term credit.

Source: Reserve Bank of India online information, "RBI Bulletin". Viewed at: http://rbi.org.in/scripts/BS_ViewBulletin.aspx.

35. While posting a structural trade deficit, India has a sizeable surplus in the services balance. Until the global financial crisis this surplus increased substantially, on account mainly of higher exports; in FY 2009/10, in the aftermath of the crisis, the surplus dropped by a third, partly due to lower exports but also to an increase in imports, in particular of financial and business services.

36. India's increasing current account deficit is a reflection of the extent by which gross domestic investment needs in India exceed gross domestic saving. During the review period, public investment was consistently greater than public sector savings, partly due to the high growth rates, but also reflecting the deterioration of the fiscal accounts and the resulting increase in the public deficit.

37. The financing of the current account deficit has not been a problem: although unevenly spread across the period, there have been large capital inflows, both as foreign direct investment (FDI) and as portfolio investment, attracted by the expanding domestic demand and the good prospects of the economy.[27] Foreign institutional investor (FII) investment, external commercial borrowing (ECBs), and trade credit account for most capital flows, with FII flows being the largest.[28] Foreign convertible currency bonds (FCCBs), which can be converted into equity at maturity, constituted a significant part of the ECBs raised in 2007/08 and 2009/10.[29]

38. Despite their general upward trend, capital inflows have been highly volatile during the period under review, due to the heavy reliance on portfolio capital and to the global financial crisis: FIIs have accounted for some 47% of flows, compared to just 9% represented by FDI inflows. Volatility has been largely accommodated by exchange rate fluctuations, without the need for massive

[27] Net capital inflows (excluding errors and omissions) totalled US$106.6 billion, or 8.7% of GDP in 2007/08; they plummeted to 0.5% of GDP during 2008/09, but rose to 4.1% during 2009/10. During the first three quarters of 2010/11 (April-December 2010), net capital flows were US$52.7 billion, almost 40% higher than during the same period of the previous year.

[28] Foreign institutional investors (FIIs), non-resident Indians (NRIs), and persons of Indian origin (PIOs) are allowed to invest in the primary and secondary capital markets in India through the portfolio investment scheme (PIS). Under this scheme, FIIs/NRIs can acquire shares/debentures of Indian companies through the stock exchanges in India. The ceiling for overall investment for FIIs is 24%t of the paid-up capital of the Indian company and 10% for NRIs/PIOs. The limit is 20% of the paid-up capital in the case of public-sector banks. The ceiling of 24% for FII investment can be raised up to the sectoral cap/statutory ceiling, and the ceiling of 10% for NRIs/PIOs to 24%, subject to the approval of the general body of the company. The ceiling for FIIs is independent of the ceiling of 10/24% for NRIs/PIOs. Repatriation by any single NRI/PIO must not exceed 5% of the paid up equity capital of the company.

[29] FCCBs are issued outside of India and give the investor the option to convert the bond into equity at a fixed conversion price or as per a pre-determined pricing formula.

open market interventions on the part of the RBI. The policy approach towards capital inflows has been to aim at the broader objective of financial and macroeconomic stability and let the exchange rate adjust. To this end, the authorities seek to encourage non-debt-creating and long-term capital inflows and to discourage short-term debt flows, except for trade transactions. The authorities expect to achieve this through the use of multiple instruments, including quantitative limits, price-based measures, and administrative measures, particularly to limit corporate foreign currency borrowing.[30] In particular, the Government has undertaken measures to attract capital that may be converted into equity, for example, through the use FCCBs. Also, private investor limits in the corporate bond market have been increased to US$40 million per investor, and to US$10 million per investor in the case of government bonds. Moreover, foreign investors may now invest in corporate bonds issued by non-listed companies.

39. As a result of strong capital inflows, and despite the rising current account deficit, foreign exchange reserves continued to show robust growth overall through the period, increasing by almost US$50 billion between 2006/07 and 2010/11. India's foreign exchange reserves were at US$309.7 billion in late-April 2011, equivalent to some 9.9 months of imports. Reflecting the mostly short-term nature of capital inflows, India's external liabilities have been increasing. The debt/service ratio was at 5.5% of exports at the end of 2009/10, up from 4.7% in 2006/07, while the ratio of external debt to foreign exchange reserves increased from 89.1% of GDP in 2008/09 to 99.9% at end-December 2010, and the ratio of short-term debt to reserves increased from 17.2% to 21.0%. Although pressures for repayment of FCCBs could start building up in the near future, the authorities consider that the issue is not to limit capital flows but to be able to manage the capital account to respond to the needs of the real economy while maintaining financial stability.[31]

(6) DEVELOPMENTS IN TRADE

(i) Composition of trade in goods

40. Merchandise trade as a percentage of GDP continued to increase during the review period, to 40.3% of GDP in 2009/10 up from 30.1% in 2005/06. This was despite the negative effects on trade of the global economic crisis. Imports continued to grow faster than exports, leading to a widening of the trade deficit.

41. Exports increased from US$126.4 billion in 2005/06 to US$178.8 billion in 2009/10, growing at an average annual rate of 15.4% during the period. However, in 2009/10, they decreased by 3.5% over 2008/09, reflecting the effects of the global economic crisis. Over the review period, the share of manufactures in India's exports remained stable while the share of primary products decreased slightly from 33.9% to 33%. Fuel products and machinery and transport equipment are the main components of Indian exports, followed by chemicals (Table AI.1 and Chart I.1). Food products, clothing, and textiles remain among the main exported commodities. Diamonds and, in particular, jewellery products have emerged as significant exports.

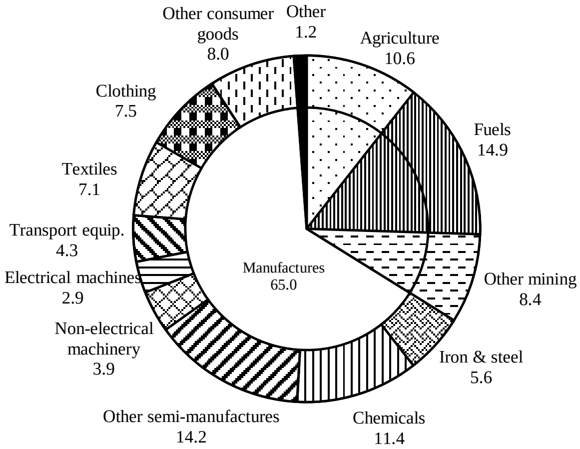
[30] Reserve Bank of India (2011d).
[31] Reserve Bank of India (2011d).

Chart I.1
Product composition of merchandise trade, 2006/07 and 2009/10

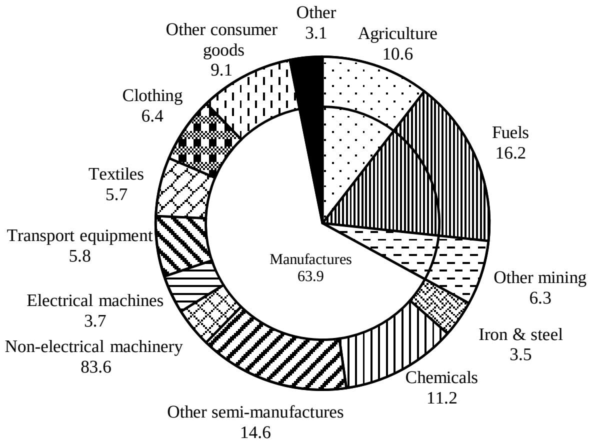
Per cent

2006/07 **2009/10**

(a) Exports (f.o.b.)

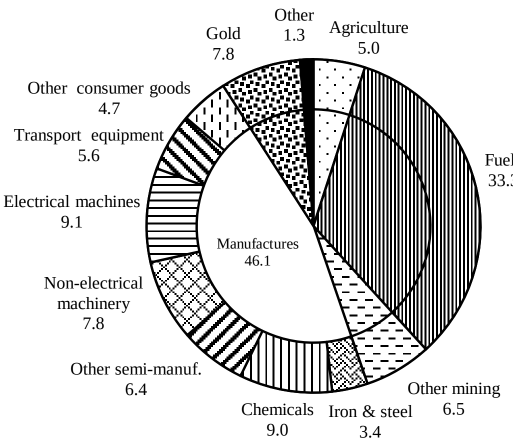


Total: US$126.4 billion

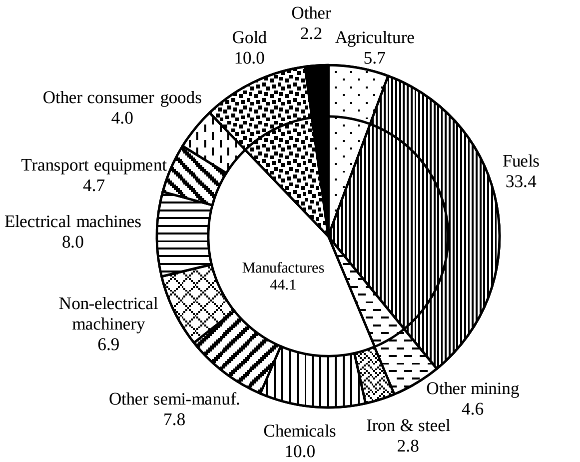


Total: US$178.8 billion

(b) Imports (c.i.f.)



Total: US$185.7 billion



Total: US$288.4 billion

***Source*: WTO calculations, based on Department of Commerce online information, "Export Import Data Bank". Viewed at: http://commerce.nic.in/eidb/default.asp [24/02/2011].**

42. In 2009/10, imports totalled US$288.4 billion, up from US$185.7 billion in 2006/07, expanding at an annual average rate of 18.9% during the period. However, there was a decline in imports in 2009/10 over 2008/09 (-5.1%) as domestic demand slowed down under the effects of the global crisis. Over the review period, crude oil represented around one quarter of India's total imports, followed by machinery and transport equipment, chemicals, and gold (Table AI.2). In 2008, the share of primary products in India's total imports exceeded the share of manufactures.

43. India is intent in promoting export growth. In February 2011, the Ministry of Commerce and Industry released a "Strategy for doubling exports in the next three years", aimed at increasing merchandise exports from an estimated US$225 billion in 2010/11 to US$450 billion in 2013/14. To achieve this, the Government intends to intensify initiatives to diversify products and markets, particularly diversifying towards emerging economies. The base of the strategy is to promote aggressively export growth of high value products that have a strong domestic manufacturing base, such as engineering, including machinery and transport equipment, and chemicals.[32]

(ii) Direction of trade in goods

44. Over the review period, India's main export markets were the EU 27 (20.5% of total exports in 2009/10), followed by the United Arab Emirates (13.4%), the United States (11.0%), and China (6.5%) (Table AI.3 and Chart I.2). India's main sources of imports were the EU 27, China, and the United Arab Emirates (Table AI.4). During the period under review, exports continued to shift away in relative terms from Europe and the United States (22.5% and 16.9%, respectively, of total exports in 2005/06), while the share of the U.A.E. and Asia continued to increase. The same trend is witnessed with respect to the origin of imports; although the EU 27 (13.3% of the total) and the United States (5.9%) are still major exporters to India, the shares of Asia (32.6%) and the Middle East (26.5%) have been increasing and they are now the main origins of imports (Chart I.2 and Table AI.5). The diversification reflects the changing composition of India's trade.

(iii) Trade in services

45. India is a net exporter of services. The services trade surplus as a percentage of GDP increased from US$29.5 billion or 3.1% in 2006/07 to US$54 billion or 4.7% in 2008/09 (Table I.4) as software and IT exports, as well as transportation, travel and business services grew considerably. After peaking in 2008/09, however, exports of services declined, as they were strongly affected by the global financial crisis, while imports continued to increase. This led to a substantial reduction in the surplus, to US$35.7 billion, or 2.8% of GDP in 2009/10; the surplus for 2010/11 is also estimated to be significantly lower than in 2008/09. Most affected by the global crisis were business services and communications, while exports of software services continued to grow.

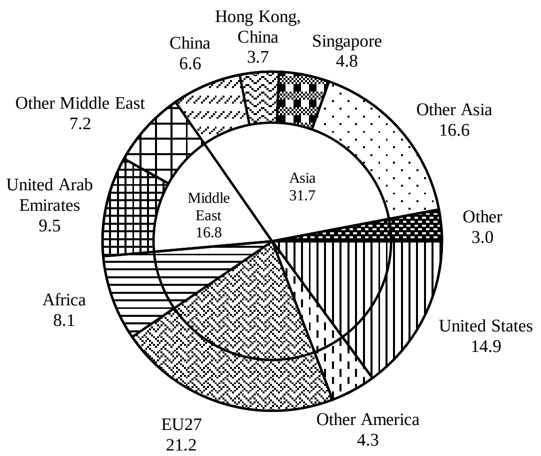
[32] Department of Commerce (2011).

Chart I.2
Direction of merchandise trade, 2006/07 and 2009/10

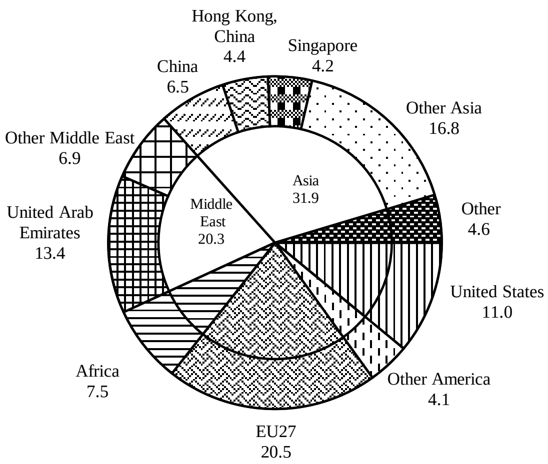
Per cent

2006/07 **2009/10**

(a) Exports (f.o.b.)

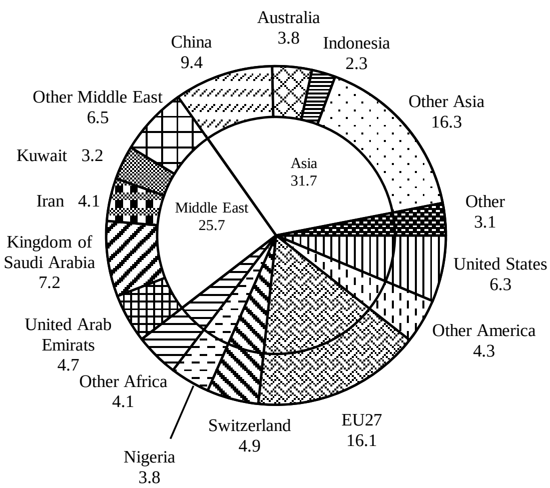


Total: US$126.4 billion

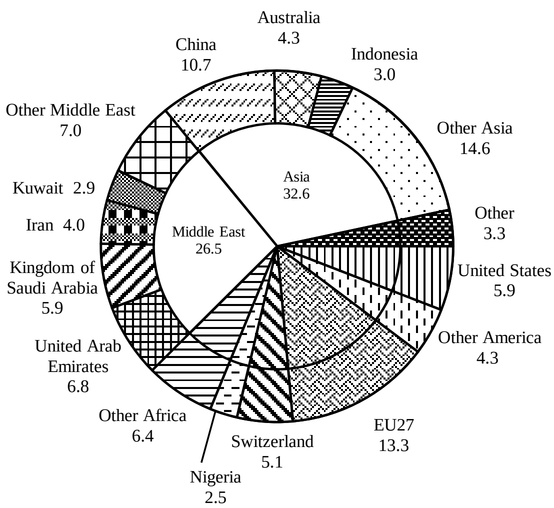


Total: US$178.8 billion

(b) Imports (c.i.f.)



Total: US$185.7 billion



Total: US$288.4 billion

Source: **WTO calculations, based on Department of Commerce online information, "Export Import Data Bank". Viewed at: http://commerce.nic.in/eidb/default.asp [24/02/2011].**

(7) DEVELOPMENTS IN FOREIGN DIRECT INVESTMENT

46. India has benefited from large inflows of capital during the period under review, both in the form of portfolio investment and as foreign direct investment (FDI). Annual FDI inflows grew from US$22.86 billion in 2006/07 to US$37.76 billion in 2009/10.

47. FDI inflows have been strong in telecommunications (reflecting partly large auctions of licences) and in other services. Inflows have also been robust in housing and real estate, and construction, as well as power-related activities and the automobile sector (Table I.5). Increased FDI inflows during the period reflect to a large extent the increase in FDI limits in various sectors (Chapter II(4)(ii)), but also the attractiveness of India's large domestic market and solid economic growth.

Table I.5
Foreign direct investment inflows/outflows, by economic activity, 2006-11[a]
(US$ million)

	2006/07	2007/08	2008/09	2009/10	2010/11[b]
Total inflows, net	22,826	34,835	37,838	37,763	25,949
Total inflows, based only on equity capital components	12,492	24,575	27,330	25,834	18,355
Services, other than telecommunications	4,698	6,614	6,150	4,324	3,274
Computer software and hardware	2,618	1,425	1,724	919	766
Telecommunications	478	1,261	2,558	2,554	1,410
Housing and real estate	467	2,233	2,801	2,939	1,109
Construction	985	1,743	2,028	2,862	1,072
Automobile industry	276	675	1,152	1,208	1,320
Power	157	974	999	1,437	1,237
Metallurgical industries	173	1,177	961	407	1,044
Petroleum and natural gas	89	1,405	350	271	562
Chemicals (other than fertilizers)	205	229	749	362	384
Other	2,346	6,842	7,858	8,551	6,177
Total outflows, net	10,447	18,442	16,325	12,270	14,246

a Financial years.
b Data until February 2011.

Source: RBI monthly data (February 2011); and Ministry of Finance (2011), *Economic Survey 2010-11*. Viewed at: http://indiabudget.nic.in/. Data based only on equity capital components are taken from the Department of Industrial Policy and Promotion online information, "FDI in India: Statistics". Viewed at: http://www.dipp.nic.in/fdi_statistics/india_fdi_index.htm; and information provided by the Indian authorities.

48. Mauritius remains the largest source of FDI, accounting for approximately 40.2% of inward FDI flows in 2009/10 (Table I.6). Part of these large flows may result from the advantages of the tax treaty between Mauritius and India, which may make it attractive for investors to route their investment through Mauritius to take advantage of the preferential provisions, which include exemption from the capital gains tax. Other major sources during the period under review were Singapore, the United States, Cyprus, and Japan.

Table I.6
Foreign direct investment inflows/outflows, by origin, 2006-11[a]
(US$ million)

	2006/07	2007/08	2008/09	2009/10	2010/11[b]
Total inflows, net	22,826	34,835	37,838	37,763	25,949
Total inflows, based only on equity capital components	12,492	24,575	27,330	25,834	18,355
Mauritius	6,363	11,096	11,229	10,376	5,746
Singapore	578	3,073	3,454	2,379	1,449
United States	856	1,089	1,802	1,943	1,055

Table I.6 (cont'd)

	2006/07	2007/08	2008/09	2009/10	2010/11[b]
United Kingdom	1,878	1,177	864	657	475
Netherlands	644	695	883	899	1,016
Japan	85	815	405	1,183	1,192
Cyprus	58	834	1,287	1,627	633
Germany	120	514	629	626	111
France	117	145	467	303	685
United Arab Emirates	260	258	257	629	321
Other	1,533	4,879	6,053	5,212	5,672
Total outflows, net	10,447	18,442	16,325	12,270	14,246

a Financial years.
b Data until February 2011.

Source: RBI monthly data (February 2011); and Ministry of Finance (2011), *Economic Survey 2010-11*. Viewed at: http://indiabudget.nic.in/. Data based only on equity capital components are taken from the Department of Industrial Policy and Promotion online information, "FDI in India: Statistics". Viewed at: http://www.dipp.nic.in/fdi_statistics/india_fdi_index.htm; and information provided by the Indian authorities.

49. India's total FDI outflows increased from US$10,447 million in 2006/07 to a peak of US$18,442 million in 2007/08. Outflows began to rise again in 2010/11.