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WORLD TRADE ORGANIZATION

Committee on Balance-of-Payments Restrictions

1995 CONSULTATION WITH INDIA UNDER ARTICLE XVIII:12(b) OF THE GATT 1994 AND THE RELATED UNDERSTANDING

Background Paper by the Secretariat

1. This paper has been prepared in accordance with paragraph 12 of the Understanding on the Balance-of-Payments Provisions of GATT 1994. It describes the developments since the background paper prepared for the last consultation dated 28 October 1994 (BOP/W/159).

I. Previous Consultations with India

2. India has consulted regularly with the CONTRACTING PARTIES on its balance-of-payments restrictions, initially under Article XII, and, since 1960, under Article XVIII:B (see BISD 8S, page 74, paragraph 3). Full consultations have been held in 1960, 1962, 1964, 1967, 1969, 1973, 1978, 1987, 1989, and 1992. Simplified consultations have been held in 1975, 1977, 1980, 1982, 1984 , 1986 and 1994.

3. At the last simplified consultation under Article XVIII:12(b), held on 14 November 1994 the Committee appreciated the courage and sagacity with which India had carried out its economic reform programme and encouraged India to continue implementing its import liberalization programme. The Committee noted that, if the balance of payments showed sustained improvement, India's aim was to move to a régime by 1996/97, in which import licensing restrictions would only be maintained for environmental and safety reasons. Members of the Committee welcomed the significant improvement in India's balance-of-payments position since the last consultation, but recognized that it remained volatile. The Committee, therefore, determined that a full consultation was desirable in the second half of 1995.

II. Trading and Exchange System: Evolution since the last consultation

(i) Import restrictions

4. The Foreign Trade Development and Regulation Act of 1992, introducing the Export and Import Policy 1992-1997 from 1 April 1992, changed the basis of India's import licensing system. Export and import policy is revised every year in March. It set up consolidated Negative Import List to replace the large number of lists previously requiring all merchandise imports to be licensed. India's notification on its trade measures taken for balance-of payments purposes, dated 26 November 1991, contains Import Licensing Policy for April 1990- March 1993 on HS tariff line basis (L/6910). Export and Import Policy (1 April 1992 - 31 March 1997), aligned on HS Commodity Classification, incorporates the amendments up to 4 October 1995.[1] The current import policy, which is the First Schedule in this

[1]Copy available in TPR Division, office No. 1060.

document, covers the Negative List of imports as well as the Free List and the Special Import Licence List.

5. The Negative Import List classifies imports into prohibited items, restricted items and canalized items. All goods not on the Negative List are freely imported under Open General Licences (OGL).

(a) Prohibited items

6. Imports of tallow, fats and oils of animal origin, animal rennet, wild animals including their parts and products, and ivory are completely prohibited.

(b) Restricted items

7. The 1995/96 export-import policy statement pruned the Negative List by an additional 32 items, and placed mainly consumer goods including personal computers, CD-rom, diskettes, coffee, fish, paper and paper products, camera, sports goods and some baby products, pulses, sugar, edible oil, butter oil and skimmed milk powder, on the free import list. Items subject to licensing under the Negative List are: (i) Several broad product groups classified as consumer goods including some electronic goods, equipments and systems; telecommunications equipment, namely telephone and electronic PABX; watches, watch cases and dials; fabrics of cotton, wool, silk, man-made and blended fabrics including cotton terry towel fabrics; concentrates of alcoholic beverages, wines; saffron and cloves, cinnamon and cassis. Most consumer goods are restricted by these licensing arrangements. (ii) Other restricted items include pesticides and insecticides and formulations thereof; some drugs and pharmaceuticals; chemicals and allied items; some seeds, plants and animals; precious, semi-precious and other stones; several items reserved for production by the small-scale sector and; several miscellaneous items such as natural rubber, coir, raw silk and silk cocoons; cinematographic feature films, and video films; batteries and tyres of motor vehicles except buses and lorries. (iii) Certain goods such as firearms, ammunition, explosives and chloro-fluoro-hydrocarbons restricted for safety, security and related reasons.

(c) Canalized items

8. Imports of the following key products contained in the Negative List remain canalized i.e. exclusively importable by designated state trading entities: petroleum products (by the Indian Oil Corporation), nitrogenous phosphatic, potassic and complex chemical fertilizers (by the Minerals and Metals Trading Corporation), edible vegetable oils (by the State Trading Corporation and the Hindustan Vegetable Oils), cereals (by the Food Corporation of India) and vitamin-A drugs (by the State Trading Corporation). In setting import levels of canalized products, the state-trading agency takes into account the availability of foreign exchange.

9. In addition, under Special Import License (SIL) scheme introduced in 1992/93, import licences are granted to certain category of exporters in proportion of their export earnings. SIL also enables importers of consumer goods to purchase import licences from exporters for specified items on the Negative List including communication equipment, healthcare goods, office equipment, and a variety of durable and nondurable consumer goods. The list was expanded to 1487 HS lines, covering 75 items in textiles and garments, computer systems, TV tubes, commercial refrigeration equipment, battery and electrically-operated vehicles, refrigerated trucks, cash registers and sewing machines, etc..

10. Import licenses are issued with a validity of 12 months; in the case of capital goods imports, they are valid for 24 months. Advance licenses are granted for duty-free imports of raw materials,

intermediates, components, consumables, parts, accessories, packing materials, and computer software required for direct use in the product to be exported.

(ii) Tariffs

11. Progressive tariff reforms introduced in successive budgets reduced average import-weighted tariffs from 87 per cent in 1990/91 to 33 per cent in 1994/95 and eliminated virtually all specific duties. However, rates of 100 per cent and above apply to 28 per cent of industrial tariff lines in 1994 which accounted for 4.4 per cent of 1988 industrial imports. The maximum tariff rate was lowered from 400 per cent in 1990/91 to 65 per cent in 1994/95[2] and to 50 per cent in 1995/96.

Table 1
Tariff structure, 1990-96[1]
(percentage)

	Simple average					Import weighted average					
	1990-91	1992-93	1993-94	1994-95	1995-96	1990-91	1992-93	1993-94	1994-95	1995-96	No. of items
Whole economy	128(41)	94(34)	71(30)	55(25)	42(21)	87	64	47	33	27	5,040
Agri. products	106(48)	59(49)	39(39)	31(30)	26(21)	70	30	25	17	15	268
Mining	n.a.	n.a.	71(24)	48(25)	37(18)	n.a.	n.a.	33	31	30	100
Consumer goods	142(33)	92(42)	76(36)	59(33)	43(21)	164	144	33	48	39	1,347
Intermediates	133(42)	104(25)	77(22)	59(17)	45(15)	117	55	40	31	24	2,337
Capital goods	109(32)	86(26)	58(24)	42(20)	35(13)	97	76	50	38	30	988

n.a. Not applicable.
1 Standard deviations are in parentheses. In 1990-91 and 1992-93, mining is included in intermediates

Source: IBRD, Country Economic Memorandum, India, 30 May 1995; based on Ministry of Finance and Bank Staff estimates.

12. Further reductions introduced in the 1995/96 budget are expected to reduce the simple average tariff to about 21 per cent and import weighted average to 27 per cent.[3] The dispersion of import duties was also narrowed in 1995/96, with the peak rate lowered from 65 to 50 per cent and a reduction in duties on a broad range of industrial inputs and raw materials (metal based industries including sponge iron, ferrous and non-ferrous metals, aluminium articles, chemicals, electronics, computers, textiles and plastic) (Table 1 and Chart 1). Duties on general machinery, machine tools and instruments and their parts have been unified at 25 per cent.[4]

13. In its Schedule XII attached to the Marrakesh Protocol, India bound 67 per cent of its tariff lines (59 per cent at existing duty levels and at 7 per cent at ceiling duties) representing 73 per cent of 1988 imports. The great majority of tariff lines in industry are bound at 40 per cent . With few exceptions, tariff lines in agriculture are bound at 100 and 150 per cent . Prior to the Uruguay Round, 6 per cent of India's total tariff lines representing 15 per cent of 1988 imports were bound.

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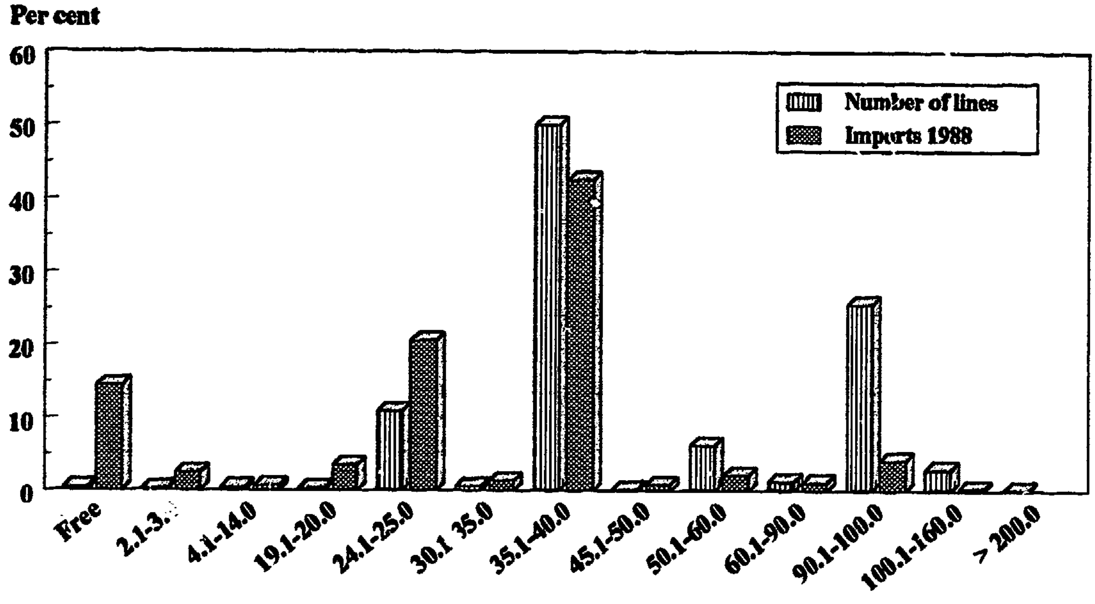
[2]Country Economic Memorandum, India; IBRD; 30 May 1995.

[3]58.5 per cent for industrial products in 1994 (WTO secretariat)

[4]Country Economic Memorandum, India; IBRD; 30 May 1995.

Chart 1
Tariff and trade profiles on individual products (excluding petroleum) in 1994



Source: WTO Secretariat.

(iii) Export policy

14. In the recent Exim Policy, Export Promotion Capital Goods (EPCG) scheme is extended to allow exporters to import capital goods at a concessional tariff rate of 15 per cent , subject to an export obligation of four times the c.i.f. value of imports to be fulfilled within a period of five years from the date of issue of the import license. The extension allows duty-free imports of capital goods against export obligation in cases where the c.i.f. value is over Rs 200 million. The export obligation is six times the c.i.f. value of imports in eight years. The scheme is extended to both goods exporters as well as to the service sector like tourism. In addition, supplies to all EPCG licence holders and projects in the power, oil and gas sectors will be regarded as indirect exporters and will be eligible for a number of benefits including duty drawbacks[5].

15. The current trade regime allows the free exportation of all goods excluding for 48 items that are subject to certain restrictions. Of these, 32 are permitted for export under a licence, 6 are canalised and 10 are banned for export.

[5]Country Economic Memorandum, India; IBRD; 30 May 1995

(iv) Exchange regulations affecting import trade

16. The exchange value of the Indian Rupee is determined in the interbank market. The Reserve Bank of India intervenes in the foreign exchange market by buying or selling foreign currency to and from authorized dealers. Exchange control is administered by the Reserve Bank in accordance with the general policy laid down by the Government. Much of the exchange control is handled by the authorized dealers.

17. The required foreign exchange is released to holders of import licences by an authorized bank on the presentation of exchange control copy of the license and the shipping documents Licence holders may make payments by opening letters of credit or by remitting against sight drafts. The contracting of suppliers' credits exceeding 180 days and other long-term import credits is subject to prior approval. Advance payments in excess of $5,000 (up to 15 per cent in the case of capital goods) may be made by authorized dealers against guarantees from an international bank . However in special cases - for example, imports of machinery and capital goods for which deposits have to be made with overseas manufacturers - the Reserve Bank grants special authorization for advance payment for a part of the value of imports.[6]

III. Macroeconomic developments

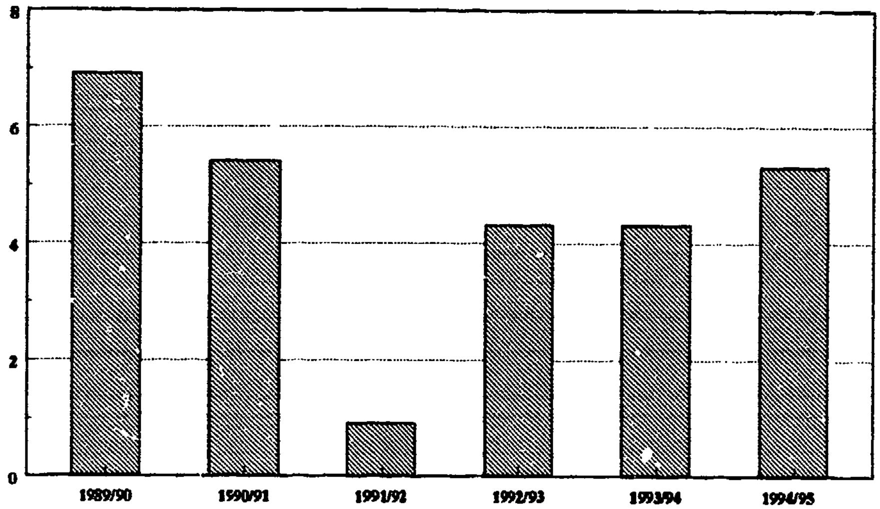
(1) Output and Expenditures

18. In fiscal years 1992/3 and 1993/4 India's real GDP increased by 4.3 per cent each year, following growth of below 1 per cent in 1991/92 (Chart 2). The recovery follows stabilization measures introduced by the Indian authorities. According to preliminary estimates by the IMF, the growth has continued over the last year, and has even slightly accelerated, with real GDP increasing by 5.3 per cent in 1994/95. The recovery was spurred by strong growth in agriculture and services since 1991/92, while industrial growth remained sluggish until 1994/95 when real growth accelerated to 7.8 per cent , compared to 3.5 per cent , in the previous year (Table 2). The recovery is expected to be strong in 1995/96.

19. The recovery was spurred by a turnaround in investment growth and by an acceleration in the growth of domestic consumption. Growth of Government consumption was particularly fast. It increased by 3.2 per cent in 1992/93 and by almost 8 per cent in 1993/94 in real terms. Gross fixed capital formation increased by almost 4 per cent in 1993/94, with investments into machinery and equipment expanding by 6.7 per cent (Table 2). There are strong indications that private investment began to recover in 1994/95, even though precise figures are not yet available.

[6]Exchange Arrangements and Exchange restrictions, IMF; Annual report 1995.

Chart 2 - India - Growth of GDP, 1989/90 - 1994/95 (Annual percentage change)



Source: IMF.
Note: GDP at factor costs. The data for 1992/93 are provisional and those for 1993/94 and 1994/95 are budget figures.

Table 2 - India - Selected Macroecononomic Indicators, 1989/90-1993/94
(Percentage change)

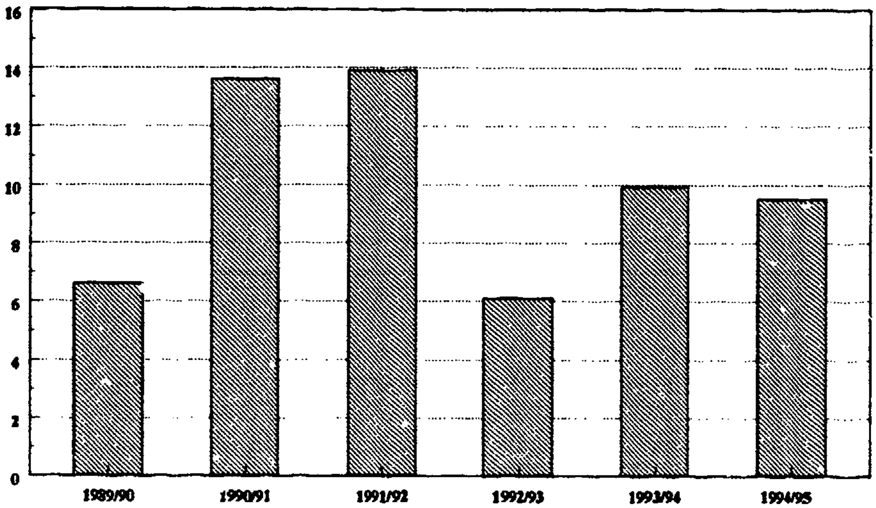
	1989/90	1990/91	1991/92	1992/93	1993/94
Output[1]					
GDP factor costs	6.9	5.4	0.9	4.3	4.3
Agriculture[2]	2.0	4.2	-1.8	4.8	3.1
Industry[3]	10.5	7.0	-1.2	3.1	3.4
Services	8.8	5.2	4.7	4.8	5.9
Expenditure[1]					
Consumption	4.5	3.7	1.4	1.6	4.5
Private	4.4	3.8	1.8	1.4	4.0
Government	5.6	3.4	-0.5	3.2	7.8
Gross fixed capital formation	8.7	9.9	-4.0	1.5	3.8
Construction	4.0	9.9	2.4	0.4	-0.9
Machinery and equipment	11.6	9.9	-7.8	2.3	6.7
Prices[4]					
Consumer prices	6.6	13.6	13.9	6.1	9.9
Wholesale prices	9.1	12.1	13.6	7.0	10.8

[1]In constant 1980/81 prices.
[2]Includes mining and quarrying.
[3]Includes manufacturing, electricity, gas and water supplies, and construction.
[4]End of period.

Source: IMF.

20. After a sharp acceleration between 1990 - 1992, inflation was also brought under control in 1992/93. The rate of inflation accelerated in each of the years 1990/91 and 1991/1992 to almost 14 per cent, measured by the consumer price index. Stabilization measures that were adopted in 1991/92 resulted in a significant reduction in the rate of inflation in 1992/93 when consumer prices increased by 6.1 per cent. However, inflation began to pick up again in mid-1993. By the end of fiscal year 1993/94, the consumer price index had increased by almost 10 per cent in comparison to the previous year and, according to provisional data, inflation continued at about the same rate in 1994/95 (Chart 3). The strengthening of domestic demand, loose monetary conditions associated with a surge of capital inflows, and supply bottlenecks all contributed to price pressures. The tightening of financial conditions since October 1994 and selective import liberalization measures, that relieved some product markets with an excess demand, has helped bring down the inflation rate somewhat by the end of May 1995, and the rate remained around 9 per cent through October 1995.

Chart 3 - India - Inflation*, 1989/90 - 1994/95**
(Annual percentage change)



Source: IMF.
*Inflation is measured by the consumer price index.
**Including data until December 1994.

(ii) <u>Investment - Saving Balances</u>

21. The stabilization program of 1991/92 was also associated with a dramatic adjustment of the main macroeconomic variables. The share of aggregate investment in GDP has declined sharply, and this reduction has been instrumental in alleviating balance of payments pressures. The rate declined from more than 27 per cent in 1990/91 to 23.6 per cent in the crisis year of 1991/92, and it continued to slide in the following years. It is estimated that the rate stood at 20.4 per cent in 1993/94 (Table 3). The decline reflected a sharp fall in the rate of private investments - from 17.4 per cent in 1990/91 to an estimated rate of 11.5 per cent in 1993/94. The rate of public investment also declined but relatively much less. Domestic savings rates also declined with the delay of one year in comparison to the adjustment of aggregate investments but they began to recover again in 1993/94. There was

a sharp decline in both private and public savings in 1992/93. However, while the rate of public savings continued to fall the following year, private savings quickly recovered and, according to preliminary indications, they continued to rise in 1994/95, accompanying a surge in private investments.

Table 3 - India - Savings and Investment, 1989/90-1993/94
(In percent of GDP at market prices)

	1989/90	1990/91	1991/92	Prov. 1992/93	Est. 1993/94
Gross domestic savings	22.3	23.7	23.1	20.0	20.2
Private sector	20.7	22.7	21.0	[illegible]	19.9
Public sector	1.6	1.0	2.1	1.5	0.3
Gross capital formation	25.0	27.1	23.6	22.0	20.4
Private sector[1]	15.0	17.4	14.4	13.1	11.5
Public sector	10.0	9.7	9.2	8.9	8.9
Savings-investment gap	-2.7	-3.4	-0.5	-2.0	-0.2
Private sector	5.7	5.3	6.5	5.4	8.4
Public sector	-8.4	-8.7	-7.1	-7.4	-8.6

[1]Includes errors and omissions.

Source: IMF.

(iii) Fiscal Developments

22. The decline of public savings noted above has been primarily due to the performance of the Central and State Governments. Reversing the marked improvement in the previous two years, the Central Government's deficit increased by 2 percentage points in 1993/4 to 7.7 per cent of GDP (Table 4 and Chart 4). This reflected both shortfalls in revenue and expenditure overruns. The Central Government's budget for 1994/95 called for a reduction in the budget deficit to 6 per cent of GDP but in the event the actual deficit was 6.7 per cent of GDP. The budget included measures to rationalize and streamline customs and excise taxes. The number of excise rates was halved and many concessions and end-use exemptions were eliminated. The tax base has also been expanded as several services have been brought into the tax net. The higher-than-budgeted deficit was mainly due to higher net lending to the States, while revenues were buoyant. The State budgets have also been under a severe strain. The overall balance of the State budgets was in deficit, amounting to 3 per cent of GDP in 1991/92. The deficit as a percentage of GDP was marginally reduced in the following two years but a further increase to 3.5 per cent of GDP was budgeted in 1994/95, as a result of an increase of non-development expenditures. The overall budget of central public enterprises has also been in deficit amounting to approximately 3 per cent of GDP and showing only a small declining trend.

Table 4 - India - Consolidated Public Sector Operations, 1990/91-1994/95[1]

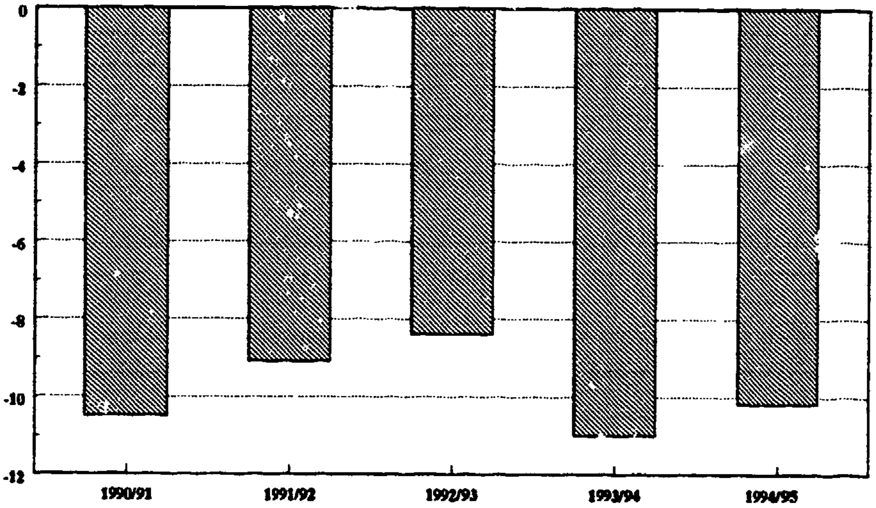
	1990/91	1991/92	1992/93	Est. 1993/94	Budget 1994/5
			(In billions of rupees)		
Total revenue and grants[2]	1,108.3	1,412.8	1,613.3	1,707.3	2,010.8
Tax revenue	863.8	1,031.2	1,145.1	1,208.3	1,405.3
Non-tax revenue[2]	238.7	372.2	459.0	489.1	591.9
Grants	5.9	9.5	9.2	9.9	13.7
Total expenditure and net lending[3]	1669.1	1972.4	2205.7	2571.8	2938.7
Overall deficit (-)	-560.8	-559.6	-592.4	-864.5	-950.9
			(In percent of GDP)		
Total revenue and grants[2]	20.7	22.9	23.0	21.7	22.1
Total expenditure and net lending[3]	31.2	32.0	31.4	32.7	32.3
Overall deficit	-10.5	-9.1	-8.4	-11.0	-10.2
Memorandum items:					
Central Government (CG)	-8.6	-6.4	-5.7	-7.7	-6.0
States	-2.6	-3.0	-2.9	-2.9	-3.5
Central public enterprises	-3.2	-2.8	-2.5	-3.2	-3.0
Net loans to states by Central Government	1.6	1.3	1.3	1.3	1.1
Budgetary support of public sector enterprises	1.4	1.1	0.9	0.9	0.8
Central Government's non-plan loans to public sector enterprises	0.2	0.1	0.1	--	0.1

[1]The consolidation covers budgetary transactions at the levels of the Central and State Gvernments, the departmental undertakings of both levels of Government, the balance of the Oil Coordination Committee and the central public enterprises.
[2]Including internal resources of public enterprises indicated in footnote 1.
[3]Including investment expenditure by public enterprises indicated in footnote 1.

Source: IMF.

23. As a result, the consolidated public sector deficit remains large. The deficit increased to 11 per cent in 1993/94 after two years of fairly successful attempts by the authorities to reduce it, especially the Central Government deficit. The budget for 1994/95 called for a small reduction in the deficit, down to 10.2 per cent of GDP but the actual deficit is now estimated by the IMF to be 10.5 per cent of GDP. The overruns have mainly been due to the overrun in the Central Government deficit, as noted above, as well as to overruns in the State budgets. The actual deficit of the central public enterprises was slightly lower than the corresponding budget figure.

Chart 4 - India - Consolidated Public Sector Deficit, 1990/91 - 1994/95*
(As percentage of GDP)



Source: IMF.
*The consolidation covers budgetary transactions at the levels of the Central and State Governments, the departmental undertakings of both levels of Governments, the balance of the Oil Coordination Committee, and the central public enterprises. The figures for 1994/95 are budget data.

24. In addition, the government has recently taken further steps to rationalize and liberalize tax and trade policies; further progress was taken towards simplifying and lowering excise tax rates and the policy of reducing import duty rates. Exemptions for personal income tax and for investment income have been increased. At the same time, the authorities propose to restrain the growth of expenditures by reducing spending on defence, subsidies and grants to the States, amounting to almost 1 per cent of GDP. The consolidated public sector deficit for 1995/96 should decline by 0.6 per cent of GDP in comparison to the 1994/95 outcome.

IV. Monetary Developments

25. Monetary developments have been characterized by a sharp increase of liquidity in 1993/94, contributing to the increase in inflationary pressures noted above. Following a reduction in the rate of growth of liquidity in 1992/93, the rate of growth of reserve money doubled and reached 25.1 per cent in 1993/94 (Table 5). Broad money increased rapidly as well, in spite of a fairly small increase in net credit to the Government. The growth of M3 would have been even faster were it not for a rise in public holdings of cash and the slow expansion of bank credit. The sharp increase in liquidity primarily reflected a surge in foreign private capital inflows and heavy market interventions by the Reserve Bank of India in the market to prevent an appreciation of the rupee.

Table 5 - India - Monetary Developments, 1991/92-1994/95

	1991/92	1992/93	1993/94	Est. 1993/94
		(Percentage change)		
Reserve money	13.4	11.3	25.1	21.0
Broad money	19.3	15.7	18.2	21.4
Currency	15.2	11.7	20.4	22.7
Deposits	20.3	16.5	17.4	21.0
Credit to commercial sector	9.4	17.1	7.8	21.4
		(In units indicated at end-period)		
Memorandum items:				
Domestic liquidity (percent change)[1]	17.20	15.20	20.10	25.50
Money multiplier	3.19	3.31	3.13	3.12
Average money multiplier[2]	3.05	3.45	3.14	3.11
Velocity of broad money	1.94	1.92	1.81	1.73
Minimum bank lending rate (percent)[3]	20.00	17.00	15.00	--
Maximum bank deposit rate (percent)	13.00	11.00	11.00	11.00

[1]Broad money minus NRI deposits and India development bonds.
[2]Ratio of broad money to four-week average reserve money (at end-year).
[3]On loans in excess of Rs 200,000 (about 60 percent of the total). The minimum lending rate was abolished on October 18, 1994.

Source: IMF

26. In 1994/95, the monetary authorities took various steps to slow down the growth of liquidity. The measures included an increase in cash reserve requirements, increasing restrictions on global depositary receipts, tighter conditions on nonresident deposits in order to slow the growth of capital inflows, raising in stages the ceilings on deposit interest rates as well as some other measures. In addition, the net RBI credit to the government expanded well below the limit set in the budget. At the same time, demand for credit in the commercial sector increased sharply, resulting in the growth of bank credit to this sector by 21.4 per cent compared to a 7.8 per cent increase in the previous year. The inflow was also adversely affected by the developments after the Mexico crisis. Moreover, a number of further steps was taken to improve the system of financial intermediation. The most significant measures were the deregulation of interest rates on loans greater than Rs 200 000 (equivalent to about US$ 6400), the reduction in the statutory liquidity ratio on aggregate deposits, and a dilution of the existing system of priority credit allocation by the broadening of eligibility criteria. Significant changes were also introduced to the capital market.

27. As a result of all these factors, the growth of reserve money slightly slowed down in 1994/95 but the growth of broad money slightly accelerated. The combination of tighter liquidity and strong demand for credit has also led to a significant rise in interest rates. This, in turn, has induced the Government authorities in 1995/96 to increasingly seek the RBI financing out of concern that heavy market borrowing might further contribute to the sharp increase in interest rates. However, the increased reliance of the Government on the RBI financing is leading to rising tensions between fiscal and monetary policies. For 1995/96 the RBI is targeting a significant slowdown in the growth of broad money from 21.4 per cent in 1994/95 to 15.5 per cent . A further acceleration in the growth of net RBI credit to the Government might jeopardize the target in spite of the fact that bank credit to the commercial sector is expected to slow down.

V. External Developments

28. India's current account deficit was reduced from 3.4 per cent of GDP in 1990/91 to 0.3 per cent in 1993/94, rising slightly to 0.5 per cent in 1994/95; however it is projected to increase to 1.2 per cent in 1995/96. Foreign exchange reserves increased from US$ 2.2 billion at the end of March 1991, or the equivalent of one month of imports of goods and services, to US$ 20.8 billion by the end of March 1995, or the equivalent of 8 months of imports. Major factors in the build-up of international reserves

had been growth of private transfers and a surge in direct and portfolio investment (Table 6). Most recently, the level of international reserves dropped to US$17.5 billion at the end of October 1995 as a result of continued rapid growth of imports and the slowdown of capital inflows.

Table 6 - India - Balance of Payments, 1990/91-1995/96
(In US$ million)

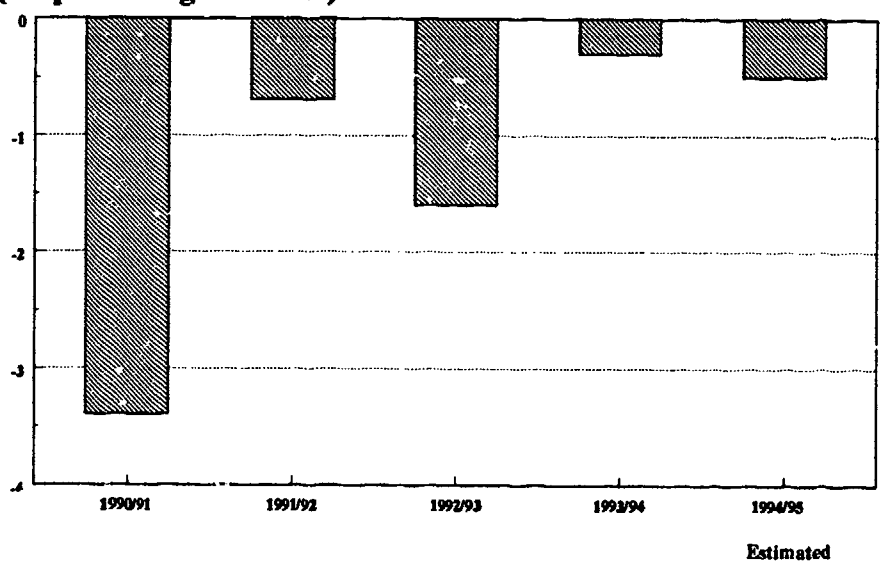
	1990/91	1991/92	1992/93	1993/94	Prel. Est. 1994/95
Trade balance	-9,437	-2,798	-4,368	-1,285	-2,870
Exports, f.o.b.	18,477	18,266	18,869	22,700	26,658
Imports, c.i.f.[1]	-27,914	-21,064	-23,237	-23,985	-29,528
Of which: oil	6,028	5,001	6,100	5,653	5,800
Invisible balance (net)	-703	1,160	480	600	1,482
Non-factor services	980	1,207	1,129	782	496
Net investment income[2]	-3,752	-3,830	-3,423	-4,007	-3,999
Private transfers	2,069	3,783	2,774	3,825	4,985
Current account balance	-10,140	-1638	-3,888	-635	-1,388
Capital account	7,644	3,420	2,785	8,506	7,767
Direct investment	68	154	344	620	1,000
Portfoliio investment	--	--	241	3,490	3,500
Net aid	2,666	2,489	1,454	1,344	1,533
Loans	2,205	2,029	1,091	974	1,183
Commercial borrowing[3]	2,019	1,417	-392	790	127
Medium- and long-term	2,102	2,816	867	2,572	2,466
Short-term/other (net)	882	-582	-1,173	-800	-250
Amortization	965	817	86	982	2,089
Private non-guaranteed[4]	230	39	34	49	55
Non-resident deposits	1,536	290	2,001	940	1,000
Bilateral arrangements[5]	-1193	-1,240	-878	-745	-1,200
Other capital (including errors and omissions)[6]	2,318	271	-19	2,018	1,752
Overall balance	-2,496	1,782	-1,103	7,821	6,379
Increase in gross reserves	-1,282	3,521	1,041	8,815	5,773
Fund repurchases	-648	-459	-334	-134	-1134
Total exceptional financing	1,862	2,198	2,478	1,128	528
Fund purchases	1,862	1,240	1,623	322	--
World Bank	--	455	444	556	260
Bilateral and other multilateral[7]	--	503	411	250	268
Memorandum items:					
Current account /GDP (in percent)	-3.4	-0.7	-1.6	-0.3	-0.5
Export volume growth (in percent)	3.7	-2.0	3.8	23.4	14.2
Import volume growth (in percent)	6.5	-20.2	8.8	8.7	21.4
Terms of trade (in percent)	-2.1	6.8	-1.1	2.7	0.5
External debt/GDP (in percent)[8]	28.3	34.0	36.9	35.8	31.2
Debt service ratio (in percent)[8]	31.8	31.6	30.4	25.4	27.3
Foreign exchange reserves					
(in US$ billions)	2.2	5.6	6.4	15.1	20.8
(in months of imports)	1.0	3.2	3.3	7.6	8.5

[1]Includes interst on trade finance. Excludes personal imports of gold and silver.
[2]Includes interest on NRI deposits. Excludes interest on NR (NR) deposits.
[3]Includes Foreign Currency Convertible Bonds (FCCBs) and other Euro bond issues.
[4]Medium- and long-term.
[5]Including interest payments under Russian debt agreement.
[6]Also includes valuation adjustment on non-U.S. dollar reserves.
[7]Includes AsDB.
[8]Includes military debt. Excludes NR deposits which totalled US$1.8 billion at end-1993/94.

Source: IMF.

29. The current account deficit has been crucially dependent on the performance of merchandise trade. In 1990/91, the current account deficit of about US$10 billion, or 3.4 per cent of GDP, almost entirely reflected the deficit on merchandise trade, which amounted to almost US$9.5 billion. The crisis of 1991/92 resulted in a significant reduction in the trade deficit (down to US$2.8 billion) due to a sharp reduction of imports which declined by more than 20 per cent in real terms. In the following year both the trade and current account deficits again increased mainly as a result of the faster recovery of imports compared to exports. However, the subsequent years saw a major improvement in the trade and current account position due to a sharp improvement in export performance (Chart 5 and Table 5). Export volumes increased by more than 23 per cent in 1993/94, and a further rapid growth was registered in 1994/95 (more than 14 per cent). The increase in the deficit expected by the Indian authorities in 1995/96 is ascribed mainly to import growth (WT/BOP/9), paragraph 14).

Chart 5 - India - Current Account Deficit, 1990/91 - 1994/95
(As percentage of GDP)



Source: IMF.

30. In addition to several exogenous events, the major factor of the improved current account position was the positive impact of various policy measures on the competitiveness of the Indian economy. The real exchange rate was depreciated, and the process of trade liberalization deepened. A series of tariff reductions was introduced in successive budgets. Specific import duties were virtually eliminated. Duties on most capital goods and their parts have been unified at 25 per cent . The list of imports of consumer goods subject to quantitative restrictions has been reduced. Foreign exchange restrictions have also been further liberalized, leading in August 1994 to the adoption of Article VIII of the IMF's

Articles of Agreement.[7] In addition, trade under the special bilateral agreements with the former centrally-planned economies has collapsed (Table 7).

31. The continuation of soft international oil prices combined with the slow industrial recovery has been the other main reason for the improvement. The stronger industrial recovery in 1994/95 stimulated a surge in imports of investment goods and manufacturing imports, leading to growth of total merchandise imports at more than 21 per cent in real terms. The rapid growth of exports was mainly due to strong growth of traditional exports of textiles, chemicals and related products. The main markets have been the United States and oil-exporting countries, but also various non-traditional markets (Table 8).

Table 7 - India - Trade and Balances Under Bilateral Arrangements, 1989/90-1993/94
(In US$ million)

	1989/90	1990/91	1991/92	1992/93	1993/94
Exports					
Czech and Slovak Republics	143	81	143	91	94
German Democratic Republic	125	..	..	..	..
Poland	73	96	80	64	52
Romania	71	53	12	8	26
U.S.S.R./C.I.S.	2,682	2,929	2,132	607	763
Total	3,094	3,159	2,367	770	935
Imports					
Czech and Slovak Republics	113	149	46	59	30
German Democratic Republic	114	..	..	..	..
Poland	83	81	79	81	39
Romania	62	28	25	55	25
U.S.S.R./C.I.S.	1,225	1,420	729	255	374
Total	1,597	1,678	879	450	468

Source: IMF.

[7]The restrictions on current account transactions have been virtually all eliminated. The exceptions include arrangements concerning (i) the Indo-Russian debt agreement, (ii) existing balances under bilateral agreements and (iii) the repatriation of dividend income on foreign investment in consumer goods industries that restrict the outflow of dividend payments to the amount of export earnings over a specified period.

Table 8 - India - Direction of Trade, 1989/90-1993/94[1]
(In US$ million)

	1989/90		1990/91		1991/92		1992/93		1993/94 (Prov.)	
	Exports	Imports	Exports	Imports	Exports	Imports	Exports	Imports	Exports	Imports
United States	2,686	2,559	2,673	2,923	2,921	1,995	3,516	2,147	4,006	2,718
European Community	4,148	7,049	4,388	7,067	4,827	5,665	5,247	6,603	5,786	6,982
Of which:										
France	383	968	427	727	425	615	472	595	504	595
Germany, (formerly Federal Republic of)	1,068	1,652	1421	1,936	1,270	1,559	1,427	1,657	1,541	1,791
United Kingdom	961	1,786	1,186	1,613	1,133	1,202	1,213	1,417	1,373	1,528
Japan	1,639	1,694	1,694	1,808	1,651	1,369	1,436	1,428	1,732	1,527
Oil exporting countries[2]	1,106	3,048	1,020	3,924	1,563	3,853	1,789	4,727	2,372	5,217
Of which:										
Iran, Islamic Republic of	79	234	79	567	123	582	114	398	159	380
Iraq	75	277	24	276	--	2	6	--	4	0
Saudi Arabia	258	870	233	1,616	351	1,443	407	1,495	510	1,551
Eastern Europe	3,205	1,796	3,243	1,882	1,953	992	780	554	835	404
Of which: FSU	2,681	1,224	2,929	1,420	1,640	729	607	255	639	319
Other countries	3,828	5,073	5,125	6,471	4,950	5,537	5,769	5,823	7,508	6,459
Total	16,612	21,219	18,143	24,075	17,865	19,411	18,537	21,282	22,239	23,307

[1]Customs basis
[2]UNCTAD classification of major petroleum exporters.

Source: IMF.

32. The capital account developments have been dominated by a surge of inward foreign investments. The inflow has taken mainly the form of direct foreign investments and portfolio investments. Deposits of non-residents have also increased significantly. Between November 1993 and October 1994 alone, direct and portfolio foreign investments increased by US$10 billion. The inflows reflected the significant measures taken by the authorities to liberalize acquisitions by foreigners of equity and convertible bond issues and the local stock exchanges. Inflows have slowed down sharply since November 1994, however, reflecting rising international interest rates, the effects of international investors' assessment of emerging markets following the Mexico crisis, and the decline of domestic stock market prices. As a result of the massive capital inflows and the improved current account position, gross international reserves increased sharply in 1993/94 - and in 1994/95 by almost US$9 billion and US$6 billion respectively.

33. The improved balance of payments position together with the domestic recovery has reduced the foreign debt burden as a percentage of GDP. The percentage declined from almost 37 per cent in 1992/93 to about 31 per cent in 1994/95 (Table 6). The actual increase in external debt reflected an increase in multilateral and bilateral borrowing between the beginning of 1990 and the end of 1994 while commercial borrowing remained stagnant during that period (Table 9). Moreover, the stock of short-term debt declined significantly since 1991. The debt service ratio is expected by the authorities to increase slightly in 1994-95 (WT/BOP/9, paragraph 10).

Table 9 - India - External Debt, 1990-94
(In US$ billion : end of period)

	March 1990	March 1991	March 1992	March 1993	March 1994	Sept. 1994
Convertible currency debt						
Medium- and long-term						
Multilateral	19.2	20.9	23.1	25.0	26.3	26.9
Government borrowing	18.4	19.9	21.7	23.2	24.2	24.7
Concessional	12.7	13.4	14.3	15.5	16.0	16.8
Of which: IDA	(12.3)	(13.1)	(13.9)	(15.2)	(15.7)	(16.4)
Nonconcessional	5.7	6.5	7.3	7.7	8.1	8.0
Of which: IBRD	(5.7)	(6.3)	(6.8)	(6.9)	(7.2)	(7.0)
Nongovernment borrowing	0.8	1.0	1.4	1.8	2.1	2.1
Bilateral	13.6	14.2	15.5	16.2	17.1	18.0
Government borrowing (concessional)	11.5	11.9	13.1	13.6	14.5	15.3
Nongovernment borrowing	2.1	2.2	2.4	2.6	2.6	2.7
IMF	1.5	2.6	3.5	4.8	5.0	4.1
Export credit	4.7	4.3	4.0	4.3	4.4	4.1
Commercial borrowing	9.3	10.2	11.7	11.6	11.5	11.8
Of which: Commercial bank loans	(6.7)	(6.8)	(6.7)	(6.5)	(5.7)	(5.8)
Nonresident Indian deposits[1]	9.2	10.4	10.1	11.1	12.7	13.4
Total medium- and long-term	57.5	62.6	67.9	73.0	77.0	78.3
Short-term	7.5	8.5	7.1	6.3	3.6	2.8
Of which: NRI deposits[2]	(3.2)	(3.6)	(2.5)	(2.6)	(1.3)	(1.5)
Total debt	65.0	71.1	75.0	79.3	80.6	81.1
(in percent of GDP)	(24.3)	(25.8)	(35.9)	(35.2)	(32.1)	(27.7)
Nonconvertible currency debt	11.0	12.8	10.4	10.6	10.1	9.4
Total External debt	75.9	84.0	85.3	90.0	90.7	90.5
(in percent of GDP)	(28.5)	(30.5)	(41.1)	(39.9)	(36.1)	(30.9)

[1]Deposits of one or more years' maturity. Excludes nonrepatriable, nonresident rupee deposits, which totalled US$ 0.6 billion at end-1992/93 and US$ 1.8 billion at end-1993/94.
[2]Deposits of up to one year's maturity.

Source: IMF.

VI. Sectoral Policies

34. The post-1991/92 economic reform measures have included a number of important structural policy changes. A major aim of these changes has been the opening of most sectors of the economy to the private sector. In addition to the trade policy reforms and the reforms of the financial sector noted above, the changes also included significant steps in deregulating the telecommunication sector. Under the new policy, licences will be issued to private operators for a period of 15 years, and foreign partnerships in joint ventures will be permitted up to 49 per cent equity participation. Private sector participation in value added services has also been allowed. In the power generating sector, private sector investments have also been permitted since 1991. However, projects in this sector have taken off rather slowly so far in view of lack of access to the financial market and poor financial health of the State Electricity Boards. The Government also announced in 1994 a National Highway Policy that will permit private participation in the construction, maintenance, and operation of roads on a build-operate-transfer basis. The development and maintenance of airport infrastructure and material handling has also been opened to private participation. Moreover, private air taxis can now operate as regular domestic airlines. Under the revised National Mineral Policy private and foreign investments will now be allowed in the exploitation of 13 minerals. In September 1994, a new pharmaceutical policy was introduced that abolished industrial licensing on most bulk drugs. The pricing policy has also been significantly liberalized and the number of drugs under price controls has been halved.