

GENERAL AGREEMENT ON TARIFFS AND TRADE

RESTRICTED

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Committee on Balance-of-Payments Restrictions

REPORT ON THE CONSULTATION WITH INDIA

1. In accordance with its terms of reference the Committee has conducted a consultation with India under Article XVIII:12(b). The Committee noted that the previous consultation with India under the same provisions had been held in July 1967 (cf. BOP/R/13 and BOP/69). In conducting the present consultation the Committee had before it a basic document transmitted by the Government of India (BOP/99), a decision of the Executive Board of the International Monetary Fund dated 17 February 1969 (Annex I) and two papers dated 28 January and 22 October 1969 respectively, containing background material supplied by the Fund.

2. The Committee generally followed the plan for such consultations recommended by the CONTRACTING PARTIES (BISD, Seventh Supplement, pages 97-98). The consultation took place on 20 November 1969. The present report summarizes the main points of discussion.

Consultation with the International Monetary Fund

3. Pursuant to the provisions of Article XV of the General Agreement, the International Monetary Fund had been invited to consult with the CONTRACTING PARTIES in connexion with this consultation with India. In accordance with the agreed procedures the representative of the Fund was invited to make a statement supplementing the Fund's documentation concerning the position of India. The statement made was as follows:

"The Fund invites the attention of the CONTRACTING PARTIES to the Executive Board decision of February 17, 1969 taken at the conclusion of its most recent Article XIV consultation with India and particularly to paragraphs 4 and 5 which read as follows:

4. The sharp rise in exports and the reduction in imports that occurred in 1968 have done much to ease pressures on the balance of payments. It is essential, however, that continued emphasis be placed on export promotion. A rapid growth in exports will contribute to efficiency in the economy and permit the increased imports that a growing economy will need. The Fund believes that the liberalization of the restrictive system introduced in 1966 has benefited the economy and should be continued.

15. The Fund notes that India continues to maintain bilateral payments arrangements and believes that steps should be taken to reduce or eliminate the arrangements with member countries at an early date.'

"At the present time the general level of restrictions of India which are under reference does not go beyond the extent necessary to achieve a reasonable rate of increase in its reserves."

Opening statement by the representative of India

4. In his opening statement, the full text of which is reproduced in Annex II, the representative of India outlined the present balance-of-payments situation, the prospects for the near future, the current import control policy and relevant developments in the internal economic situation. It was stated that in the past year there had been a substantial improvement in the balance of payments. Exports had increased by a comfortable margin and imports had been reduced mainly owing to increased domestic production. The price rises which had beset the Indian economy in recent years had definitely abated, thanks to increased food production and increases in industrial output, and a better balance between overall supply and demand. Fiscal policy had also helped to keep inflationary pressures under check and the overall budgetary deficit was greatly reduced partly through increases in taxation. The rise in agricultural output was attributable to technical innovations such as the introduction of high yield seeds, greater use of fertilizers and pesticides, and better irrigation. The improvement in industrial production was reflected both in substantially increased output and in a more diversified and better balanced composition. Output of newer industries, particularly base metals and engineering goods, had considerably increased, although there was a decline in cotton textiles and jute manufactures. The improvements in agriculture as well as in industrial production had been greatly helped also by monetary policy, involving the provision of the required credit facilities for priority sectors. These developments had made possible a reduction in imports of foodstuffs, so as to enable greater import facilities to be provided for the purchase of essential inputs for development, priority being given to capital equipment required by exporting producers. A new feature in the current import policy was to require certain industries to export a specified proportion of their output and this had helped to bring about increased cost consciousness in industry as well as improved efficiency of labour and of management, and greater care in making purchases in the light of economy and efficiency.

5. The representative of India, in conclusion, observed that, while the overall trade and payments outlook was encouraging, careful use of the existing foreign exchange resources was still called for and the need for external financial help was still urgent, especially having regard to the mounting debt servicing obligations. There was need for increasing amounts of untied aid, untied both with regard to the types of imports that might be financed and the sources from which imports might be made. Furthermore, in spite of the results of the Kennedy Round, some of the major items of India's exports continued to face high tariffs in the major developed countries, as well as quantitative restrictions and other non-tariff barriers. In short, the situation called for a combination of appropriate trade and aid policies in developed countries without which India would find it difficult to attain the export targets which it had set for itself, and to obtain the increased imports necessary for the sustained development of the Indian economy.

Balance-of-payments position and prospects

6. Members of the Committee expressed appreciation for the very comprehensive and lucid statement by the Indian representative and expressed satisfaction over the remarkable progress that India had made in regaining stability and accelerating economic growth. It was observed that the Indian economic situation was better than it had been at any time in recent years. The fundamental change that had been brought about in agriculture had largely removed the severe strain on the economy, and had made self-sufficiency in food an objective attainable in a few years. Some members added that the Indian achievement provided a heartening example for other developing countries grappling with the same kind of problems faced by India which until now had been considered insoluble.

7. Invited to comment on the prospects of India's balance of payments in the current and coming years, the representative of India stated that India's total exchange reserves amounted to \$672 million at the end of October 1968. While this might appear comforting, account must be taken of the very sizable debt servicing payments that were due shortly, notably \$117 million of repayment to the IMF during 1969/70. During 1970/71 while exports were expected to rise by some \$100 million and total imports, owing to lower food grain imports, might decline by approximately another \$100 million, the gain would again be marginal if account was taken of debt servicing which in that fiscal year would amount to \$754 million, including a repayment to the IMF of \$205 million. The import control policy which, in respect of essential materials and components needed by the priority industries, permitted imports according to consumption during the past period, might have the effect of a generally even outlay of foreign exchange for imported raw materials. Basically, substantial amounts of foreign aid would continue to be needed to fill the foreign exchange gap.

8. In a discussion of India's recent success in expanding and diversifying exports, it was pointed out that the traditional items of Indian exports had generally not shared in the increase, and that the rise had occurred mainly in new lines such as iron and steel, machinery, transport equipment, etc. The suggestion was put forward that the expansion of exports might not be sustained as economic growth proceeded and domestic demand rose. Invited to assess India's export earning prospects the representative of India first commented on the factors responsible for the decline or stagnant pattern of some of the country's traditional exports. Tea, in spite of efforts at innovation in further processing and energetic marketing, had lost ground owing to a decline in demand in the major consuming countries with the result that the price had fallen markedly in recent years. Owing to changed methods of transport and packing of bulk commodities, demand for sacking and hessian had declined substantially over the years, and efforts at changing to new jute products such as carpet backing sometimes faced impediments in importing countries bent on protecting competing domestic products. Constant endeavours were made by the Indian authorities to improve the quality of Indian exports. Pre-shipment inspection had been introduced for a large variety of goods which had a salutary effect on the confidence of foreign buyers in Indian goods. Sustained efforts were made to make certain other products (such as iron ore, leather goods, handicraft products, etc.) more competitive, attractive and marketable. Jute manufactures situation would improve this year as raw jute had

again become available after a serious shortage and high prices had deprived the industry of its raw material during the past year. As regards future trends, the 13.5 per cent growth of exports in 1968/69 was unlikely to be repeated this year, the present rate being somewhat lower than the 7 per cent planned for the current and coming years.

9. A member of the Committee observed that there had been a decline in new foreign investment in India which appeared to have been partly caused by Government policy, and enquired whether there might be any change in that policy and whether any incentives might be provided to attract more foreign capital to meet the investment goals of the Fourth Five-Year Plan. In posing this question the member remarked that whereas a preliminary version of the Plan seemed to have over-estimated available investment resources from both domestic and foreign sources, the revised Plan's targets and resource estimates were much more realistic. The question would seem to be one of whether the planned investment outlay was sufficient to achieve the planned growth rate. The representative of India replied that the Indian Government had taken various steps to streamline decision-making procedures dealing with investment projects involving foreign capital and had recently set up a Foreign Investment Board on which all ministries concerned were represented so that decisions could be taken promptly and delays caused by the need for inter-ministerial consultations could be eliminated. In fact the Indian Government has been actively campaigning to get foreign investors to make direct investment in particular industrial sectors (such as fertilizers, tractors) to take part in the Indian economic growth, and the efforts had been fairly successful as might be seen from the number of foreign enterprises established in the country. An Indian Investment Centre had been operating in New York and a branch office had been set up in Düsseldorf. Similar branches at other foreign financial centres were not precluded.

10. In answer to a question on the recent nationalization of banks and any possible ramifications that this might have on capital inflow, the representative of India explained that the action had been taken for purely domestic reasons, and did not apply to foreign banking establishments in India. The main purposes of this action were to ensure that bank credit was available for the priority sectors in accordance with the basic Plan objectives, to ensure availability of working capital funds for the important sectors and to avoid the misuse of funds for purposes contrary to public interest, such as the use of bank resources for improper speculation in the equity market. There was no intention to affect the availability of credit for the private sector, or otherwise to alter the basic nature and functions of the banks.

Alternative measures to restore equilibrium

11. Some members of the Committee stressed the importance of monetary and fiscal policies in regulating the rhythm of growth, with reference to the greater degree of fiscal restraint that the Indian authorities seemed to have been exercising and to their success in keeping monetary expansion within the limits of increased output. In this connexion they asked what fiscal and monetary policies were intended to be applied in the coming years. The Indian representative stated that the budgetary provisions for the coming year included a slight increase in development outlays and a total deficit in consonance with the need for increased money supply to keep pace with the increase in national output. Such policies had indeed been successful in the past two years as might be witnessed by the stability of prices; the wholesale price index had fallen by a small margin. Monetary policy had been oriented to assisting the priority industries, and providing increased credit for agriculture and small-scale industries. To meet increasing investment needs, steps were taken to stimulate saving.

12. In confirming that the planned budgetary deficit for 1969/70 and 1970/71 were both about \$330 million the Indian representative pointed out that these figures, though slightly higher than the 1968/69 level were considerably lower than those in the preceding years. The Indian authorities considered that deficits of this magnitude would not be inconsistent with price stability, having regard to the increase in total national output. In fact, a judicious expansion of money supply was necessary in present circumstances when increased output was generating sufficient savings for investment; an inadequate money supply could exert an undesirably restrictive effect on industrial expansion and bring on a recession.

13. Noting that State Governments in India could have recourse to deficit financing, a member of the Committee asked what measures were available to limit the State Governments' ability to indulge in deficit financing to meet their deficits. The representative of India stated that the Central Government, as well as the Reserve Bank of India, had over the years been using their persuasive powers to discourage the State authorities from having undue recourse to deficit financing, and they had met with a certain measure of success, and such deficit financing had diminished. The States had been resorting to new ways of raising funds and the recent Finance Commission award provided that the States should have a greater share in the tax revenues of the Central Government.

14. In answer to questions concerning measures to stimulate investment the Indian representative referred to various tax exemptions applying to reinvested profits, generous depreciation allowance, etc., the tax policy being generally geared to encourage corporate reinvestment and self-sustained industrial expansion. The equity market in India was somewhat stagnant and less active than desired, partly owing to the unfortunate memories of the recession years. The means relied upon to activate personal savings included reasonably high interest rates for fixed-term savings accounts, which had led to a marked rise in time deposits.

15. The material before the Committee showed that Indian public revenue had not been responsive to the rise in national income in recent years, and that, in striking contrast to the highly taxed industrial sector, agriculture seemed to be virtually exempt from taxation. Interest was shown in the Committee in any measures, apart from the recently proposed wealth tax on agricultural assets, that the Indian authorities might have contemplated adopting to ensure that the agricultural sector, which accounted for an increasing proportion of Gross National Product, make a fuller contribution to revenue. In reply the Indian representative explained that one of the Government's basic policies being to encourage agricultural investment, the Government was reluctant to place any undue tax burden on rural income that might reduce the resources now devoted to the purchase of new farm implements, tractors, irrigation equipment and fertilizers. Furthermore, under the Indian constitution, the Central Government had no power to tax agricultural income. Reliance was placed on indirect taxes which could be so structured as to place an appropriate level of tax incidence on consumers and end-users in the agricultural sector.

16. A member of the Committee observed that while industrial output had shown a significant growth (by 6.4 per cent) and contributed substantially to the rise in exports in 1968/69, under-utilization of industrial capacity seemed to have persisted (the rate of utilization being: finished steel 66 per cent, aluminium 57 per cent, nitrogenous fertilizers 57 per cent and steel castings 37 per cent), and asked what the current situation was and whether special steps could be taken to raise the level of utilization of existing capacity. The representative of India explained that this "under-utilization" of industrial capacity reflected a number of situations. There had been, for example, a shift in the pattern of demand for various types of steel and some steel mills had met with certain technical difficulties in adjusting to new demand. Technical factors such as stoppage necessary for the relining of blast furnaces also tended to be reflected in a theoretical idle capacity, as could also be the time elapsing between the setting-up of plant and its effective operation. Some steel casting mills had been idle during periods of falling demand, but had recently been working to higher capacity, but a new problem had arisen as the country was now faced with an overall steel shortage. The Government had been endeavouring to ensure fuller utilization of industrial capacity and one of the solutions lay with the expansion of exports.

17. In response to a question concerning surplus manpower and unemployment, the Indian representative recalled that the problem of unemployment had been one of the main concerns of the Government ever since planning began in early 1951. The problem had of late become more acute owing to the pause in industrial growth which had lasted for several years during which the growing labour force outnumbered the increase in employment opportunities. The problem had to some extent been attenuated by recent developments in agriculture, as a result of which there had even been occasional labour shortages in rural areas in certain States during the sowing and harvest seasons. Policy measures included the promotion of small-scale industries and labour intensive industries such as hand-loom textile production which was particularly useful in solving the problems of under-employment in the countryside. (Small-scale local industries, incidentally, also served the useful purpose of mopping up surplus savings, which was likely to be squandered on consumption if productive outlets were not found to absorb such savings.)

System and methods of the restrictions

18. Members of the Committee presented questions on various aspects of the Indian import controls and restrictions. In the course of the discussion, they reviewed the evolution of the system especially since the new departure made at the time of the Indian devaluation in June 1966, in the direction of seeking external stability and increases in exchange reserve through export expansion and import liberalization. Since then India had taken several steps in the direction of liberalizing administrative controls on imports of industrial inputs, the most significant one being the designation of fifty-nine "priority industries" entitled to import licences to meet their total needs irrespective of previous base year imports. In the view of members of the Committee this progress towards simplification of the administrative controls were praiseworthy and should be welcomed by the contracting parties.

19. On the other hand, the Open General Licence was still confined to a limited number of raw materials; new items had recently been added to the already lengthy prohibited list, now including not only luxuries and non-essential consumer goods but chemicals, insecticides, pharmaceuticals, and even machine tools, on account of their being also available from domestic production.

20. Members of the Committee said that they recognized that India was entitled to maintain the import restrictions at a level necessary to safeguard its balance of payments and monetary reserves as provided for in Article XVIII:B. Some of the members wished to know, however, India's outlook for further liberalization, especially with respect to the underlying policy of maximizing import substitution through prohibiting imports; how India viewed the effects of past liberalization of administrative controls; what were the prospects of enlarging the Open General Licensing and shortening or abolishing the Prohibited List. Some members wished to know whether India would at least shorten the Prohibited List as soon as its balance-of-payments situation permitted such a move. Other members merely urged that India simplify its import control procedures and documentary requirements, having regard to the complexity of the present procedures which sometimes involved long delays in the issue of licences, required calls and waiting by applicants at a multitude of ministries and regulatory agencies or entailed prolonged withholding of foreign exchange transfers.

21. In discussing the State-trading operations of India and their possible discriminatory effects on imports from different sources, members of the Committee noted that the list of commodities which must be imported through State-trading corporations had recently been lengthened by the addition of seven industrial raw materials while four other products would henceforth "normally be arranged under the auspices of the State-trading corporation". This seemed to indicate that increasing reliance was being placed on this device. While they felt reassured by the Indian Government's statement that "an entirely non-discriminatory policy is followed, subject to the constraints imposed by the exchange availability and the conditions attached to external assistance" (BOP/99, paragraph 20), they were nevertheless anxious to be assured that the State-trading arrangement would not interrupt the traditional contact between foreign exporters and Indian end-users, and that exporters in Western countries would continue to have equal opportunities to compete with the State-trading countries on the Indian market for the products in question.

22. The representative of India stated that the State-trading agencies of India had been set up primarily because of the economic and practical advantages that could be derived from bulk buying, particularly for the small industrial end-users of imported raw materials, most of whom had neither the administrative set-up nor the necessary demand volume to be able economically to engage in direct importation. For such end-users the economy to be derived from bulk buying and bulk transportation could be considerable, and the multitude of small industrial producers in India had greatly benefited from imports by the State-Trading Corporation. Recently even large-scale industrial firms in the priority sectors had shown a willingness to entrust their requirements of non-ferrous metal imports to the State-owned corporation and to surrender their own import licences. The attitude of the end-users had conclusively proved that the rôle of the State-trading corporations in India was that of an expert trading agency, competently performing an essential service to the industrial community on the basis of commercial considerations at a minimum cost. Certain

products had recently been placed under the auspices of the State-trading corporations in order to ensure their proper utilization; that is, to ensure that the imported goods were used for the purposes for which their import had been facilitated and paid for with scarce foreign exchange. In short, the State-trading agencies' operation involved no discrimination against any particular countries, or in favour of any specific countries.

23. Some members of the Committee recalled that in the sixteen years since 1953 an increasing portion of India's trade had been carried out under bilateral trade agreements. They noted that while in the earlier years these agreements had been designed to help India to trade traditional exports for capital equipment and manufactured goods, they had increasingly served to market India's industrial products against imports of raw materials. One member expressed the view that some of these agreements were not in India's best interest in so far as they obliged India to purchase inferior products at excessively high prices or to supply Indian products at low prices which the bilateral partner could re-export to third markets at a profit - thereby depriving India of her traditional outlet. Apart from the damage that might be caused to the trading interest of other contracting parties by the discriminatory features of these agreements, India was likely to have suffered sizable loss from this rupee trade with the few bilateral trading countries. Recalling the advice repeatedly given by the IMF and the CONTRACTING PARTIES that India reduce her reliance on bilateral agreements, members of the Committee wished to know whether India had any plans to give effect to that entreatment by terminating or reducing the scope of its bilateral agreements. They would also like to be assured that the existing agreements were operated in such a way as to involve no discrimination against the exports of the contracting parties. In this connexion they noted that whereas an Indian statement asserted that most of India's bilateral agreements did not involve any obligation to import any goods (BOP/99, paragraph 17) it had been reported officially elsewhere that its agreements with certain trading partners entailed the purchase and sale of specified commodities.

24. The representative of India, in reply to these questions, stated that the trade agreement with Fund members merely served the useful purpose of ensuring supplies of certain products and that the proportion of trade covered by them was an insignificant portion of India's total trade. As far as the rupee payments countries were concerned, the change in the composition of products covered by India's agreements merely reflected the general change in India's industrial horizon and the widening of the range of her production. The agreements with non-members of the Fund had inter alia provided for continued supplies of components and spare parts for equipment originally bought from the partner country. The Indian authorities were not aware of any cases in which inferior goods were forced on India at prices higher than world market prices. India's bilateral agreements contained a provision forbidding the diversion to third markets of goods traded under the agreement. If, on rare occasions, a product of Indian origin found its way to third markets a representation was made to the bilateral partner and an appropriate adjustment made in the plans for the supply of the product to that country to ensure that only its own requirements were obtained from India.

25. Some members of the Committee mentioned in this context the question of preferential and discriminatory effects of the Tripartite Agreement between India, the United Arab Republic and Yugoslavia and enquired whether any information was

available on its balance-of-payments implications or on specific industries which had benefited. It was generally agreed, as pointed out by the India representative, that since the Tripartite Agreement was under examination in a forum specially appointed for that purpose, it was not necessary to consider it in this Committee. The Indian representative added that considering the small size of trade that was involved under the Agreement it could not have any significant influence on the overall balance of payments of India.

26. The representative of India reiterated his conviction that India's balance-of-payments position, in spite of the apparent increase in reserves in the past year, remained precarious, especially having regard to the debt repayments falling due in the near future which called for vigilant husbandry of the limited resources. It would not be prudent for India to take any precipitate action now and court the danger of having to take retrogressive steps at a later stage. Within permissible limits, however, the Government of India would be willing, as it had always been, to explore all the possibilities of simplifying the procedures. The need-based licensing of essential supplies for priority industries had been evolved precisely to that end. As a large part of India's foreign exchange resources consisted of tied aid funds the limited availability of individual currencies entailed the scrutiny of applications for import licences with reference to the availability of tied aid funds and this might cause some delay in licensing. Slowness of exchange transfer might similarly be caused by the task of weighing the availability of, and estimating the likely calls on individual currencies.

27. In response to a question regarding the prospects for further liberalization, particularly the possibility of eliminating or reducing the list of banned items, the Indian representative stated that in India, with increasing requirements of imported raw materials to meet the need of increased industrial production, the success of the liberalization policies adopted by the Government depended partly on export promotion efforts and partly on the success of the policy of import substitution. As far as banned items were concerned, it was explained that actual users and manufacturers in the fifty-nine priority industries were permitted to import even banned items up to certain specified amounts where these items were required in the manufacturing process. The Indian representative further noted that there was a procedure whereby a Special Committee headed by the Chief Controller of Imports and Exports (on which private interests were also represented) reviewed the list of banned items from time to time and whenever deemed desirable, articles were removed from that list. As a result of such a review, a number of items initially banned had been removed from the banned list during the current year. It was, however, not possible at the present stage to indicate any definite date for enlarging the scope of Open General Licensing. In general the Indian policy was oriented towards export expansion and import substitution. It should be noted that if the import of some items was severely restricted it simply meant that foreign exchange was being saved for use in payment for other, more urgently needed, imports.

28. In reply to a question as to whether the requirements of spare parts were being adequately met the representative of India stated that imports of spare parts generally enjoyed high priority and, in so far as they were needed for a priority industry, were licensed up to the full requirement expressed as a percentage of the imported capital equipment. As for earth-moving equipment, the Indian representative indicated that considerable volume of import licences was being issued to trade to ensure availability of spare parts.

29. In response to a representation concerning transit trade through India the Indian representative explained that trade across the Eastern border had been interrupted owing to certain political difficulties, and that India earnestly hoped that the situation would be normalized. As to transit trade facilities for other neighbouring countries these matters were dealt with amicably to mutual satisfaction. In this regard it had, however, to be ensured that the effectiveness of India's import control system was not reduced. The Indian representative added that if any specific complaints were brought to the notice of the Indian authorities they would be looked into.

Effects of the restrictions

30. A member of the Committee referred to the protective effects of the restrictions which, by fostering uneconomic and inefficient production, placed a burden on the consumer and might, in some cases, necessitate governmental financial incentives to encourage exports. He asked what consideration was being given to allowing some of these imports in the interest of the consumer, and how the Indian Government evaluated the added cost of protectionism in regard to exports. The representative of India stated that in order to provide local producers with stimulative competition and to instill cost consciousness in domestic production the present system allowed importation of products, including those which were on the Banned List. Cash compensation was paid to some exporters of some products, but this was intended partially to offset the burden of a multiplicity of taxes that manufacturers had to pay at different stages of production. Indian manufacturers and exporting firms had to pay a number of taxes at various stages on the raw materials, components, etc. used by them in the process of manufacture; owing to the federal structure of government, there was in India a large number of indirect taxes ranging from octroi levied by municipalities and local authorities to sales taxes and other duties levied by the State Governments and excise duties levied by the Centre on raw materials, components and other items going into the manufacturing process. While there was a system of refund of excise duty on a finished product meant for export, there was no way to refund to exporters the multiplicity of such indirect taxes. The cash compensation paid by the Government was calculated partially to offset the disadvantage to exporters by way of these taxes and in order to ensure that the consumer in the importing country did not bear the full burden of such indirect taxes in India.

Conclusions

31. Members of the Committee commended the Government of India for the substantial improvement in the balance of payments, and especially for the increase in exports and the rise in food production which contributed substantially to the progress towards solution of the most fundamental problem of the country. They expressed appreciation for the prudent yet flexible fiscal and monetary policies which India had relied upon for restoring the balance between supply and demand. They recognized that under the present circumstances India needed to maintain its restrictions on imports the general level of which had been referred to in

paragraph 3 of this report. They expressed the hope that further improvements in the balance of payments would be made in the near future so as to enable India to take new steps of import liberalization. In the meantime, they urged that India examine the possibility, within the limits set by the balance-of-payments considerations, of simplifying its import control procedures.

32. The representative of India expressed appreciation for the sympathetic attitude of the members of the Committee in considering the problems faced by his country, and assured the Committee that he would take up with the other competent authorities in New Delhi the various questions and representations put forward by members of the Committee during this consultation.

ANNEX I

International Monetary Fund Executive Board Decision
Taken at the Conclusion of the Fund's Consultation
with India on 17 February 1969

1. This decision is taken by the Executive Directors in concluding the 1968 consultation with India pursuant to Article XIV, Section 4, of the Articles of Agreement.
2. Owing to a sharp increase in agricultural production and greater restraint in fiscal policy, there has been a marked improvement in the financial situation during 1968. The Fund welcomes the return to price stability after several years of inflation and believes this should lay the basis for a faster growth rate to be achieved by extension of the new agricultural techniques and more rapid growth in industry.
3. The period of the next Five-Year Plan will pose difficult problems in the mobilization of resources both at home and abroad. The Fund hopes that the Government will give high priority to improving the tax system and to working out effective means of stimulating savings in both the public and the private sectors. Success in these efforts, coupled with an adequate inflow of resources from abroad, should foster a more satisfactory growth rate than in prospect for 1968/69.
4. The sharp rise in exports and the reduction in imports that occurred in 1968 have done much to ease pressures on the balance of payments. It is essential, however, that continued emphasis be placed on export promotion. A rapid growth in exports will contribute to efficiency in the economy and permit the increased imports that a growing economy will need. The Fund believes that the liberalization of the restrictive system introduced in 1966 has benefited the economy and should be continued.
5. The Fund notes that India continues to maintain bilateral payments arrangements and believes that steps should be taken to reduce or eliminate the arrangements with member countries at an early date.

ANNEX II

Opening Statement by the Representative of India

1. The Government of India is glad to have this opportunity of reviewing with the contracting parties the recent developments in the Indian balance of payments. The very useful paper prepared by the International Monetary Fund in connexion with the 1968 Article XIV consultations has already been circulated to members.
2. There has been a distinct and considerable improvement in the balance of payments of India in the past year. Indian exports increased during 1968-69 by 13.5 per cent over exports during the previous year. In the first six months of 1969-70, namely over April-September 1969, exports have continued to increase although the rate of increase has lately been somewhat lower than anticipated at the beginning of the year. As a result of the increase in exports, and a reduction in imports brought about largely by improved production of foodgrains and successful import substitution within the country, the foreign exchange reserves position has also improved. The price increase observed until 1967-68 has been definitely arrested, the index of wholesale prices at the end of October 1969 being marginally lower than the index of wholesale prices a year ago. This has been possible due to combination of increased food production within the country, increased industrial output, and a better balance between overall demand and supply. There was a record harvest in 1967-68 and in 1968-69, the economy consolidated this position. Industrial production which had been facing a recession in the two previous years increased by over 6 per cent in 1968-69. On the whole the economy has recovered from the traumatic experience of two successive years of drought and is ready to resume the trend of growth. The outlook today calls for a step up in the rate of investment in the economy in order to stimulate a high rate of long-term growth of the economy.
3. The immediate objective of budgetary policy is to resume growth which had been interrupted by the emergence of recession in the past few years. The budget for the current year therefore provides for various measures to stimulate savings and investment and encourage larger exports. The developmental outlays provided

in the central budget have been stepped up from \$3.3 billion in 1968-69 to \$3.5 billion in 1969-70. To keep inflationary pressures under check, reliance on deficit financing is, however, sought to be kept at a level which is consistent with the requirements of monetary stability. The overall budgetary deficit of the Central Government declined from \$400 million in 1966-67 to \$266 million in 1967-68. The estimates for 1968-69 as well as for 1969-70 indicate an overall budgetary deficit of the Government of India by some \$330 million each year. Substantial additional taxes have been imposed by the Government of India and every effort made to curtail non-developmental expenditures.

4. The agricultural situation in the country has definitely improved. Food production, which increased to 95 million tons in 1967-68 due partly to the adoption of the new agricultural strategy remained more or less at the same level in 1968-69 because of failure of rain in many parts of the country. The prospects this year are much better and, according to current forecasts, food output will increase to 100 million tons in 1969-70. Although the cotton, jute and oilseeds crops had suffered a setback during 1968-69, there are indications of a substantial improvement in the production of commercial crops like cotton, jute and sugar during 1969-70.

5. The new agricultural strategy consists of the introduction of high-yielding varieties of seeds and the increased use of inputs like fertilizers, pesticides and water, and improved agricultural practices. The input of both fertilizers and pesticides has increased substantially. The consumption of nitrogenous fertilizers has risen from 840,000 tons (nitrogen) in 1966-67 to 1.2 million tons in 1968-69. Plant protection measures covered 54 million hectares in 1968-69 as compared to 24 million hectares in 1966-67. There has been increased emphasis on minor irrigation works and the additional irrigation potential created from major and medium irrigation projects was 0.8 million hectares and from minor irrigation works 1.45 million hectares. Government have been endeavouring to increase the production of agricultural machinery, particularly tractors within the country. There has been a marked improvement in yields of a number of crops as a result of the introduction of the new high-yielding varieties of seed. During 1968-69, 8.5 million hectares of land were under high-yielding varieties of seed as compared to 1.9 million hectares in 1966-67.

6. Industrial production also has shown definite signs of revival from the earlier period of stagnation. During 1968-69, the overall index of industrial production showed an increase of some 6.4 per cent as compared to a mere 1 per cent in the two years 1966-67 and 1967-68 taken together. Preliminary figures indicate that industrial output may increase by some 7 to 8 per cent this year. This increase in industrial production has been achieved in spite of a stagnation in the production of cotton textiles, and to an extent also of jute manufactures, and has been brought about by a significant rise in the output of newer industries, particularly of base metals and engineering industries. The sluggishness in the cotton textiles output has been due partly to a faltering domestic demand caused by a shift to synthetics and partly to the financial difficulties of some of the textile mills, which had been hit adversely during the recessionary years. There has also been a relatively slow rate of recovery in some of the machinery manufacturing industries like machine tools and electrical equipment, although there has been a steady growth in the production of a number of industrial machinery items including cement, sugar, paper and chemical machinery.

7. The accent of monetary policy has also been on aiding economic recovery, particularly in sectors affected by recession. During the last two years or so, the Reserve Bank has been according preferential credit treatment to the priority sectors, viz agriculture, exports and small-scale industries. This policy of concessional refinance to the priority sectors is being continued in the current busy season (November 1969 to April 1970). The commercial banks were particularly directed to earmark funds out of additional deposits for agriculture and small-scale industry. The process of channelling credit to priority sectors in conformity with social and economic commitments has received further impetus with the nationalization of fourteen major banks.
8. The resurgence of industrial production has led to a sharp increase in import licensing during the current year. During the six months of April-September 1969 the total value of import licences issued, at \$770 million was 34 per cent higher than the level of licensing (\$573 million) during the corresponding six months of 1968. Understandably, however, there has been a major shift in the pattern of imports, which in 1968-69 and also over the first few months of the current year reflects the success of the policies adopted by the Government over the past few years. During 1968-69, there was a sharp drop in food imports by \$242 million.
9. While the decline in imports has been due mainly to a decline in requirements of food imports, the improvement in exports observed during 1968-69 as also during the current year have been largely the result of an improvement in exports of non-traditional items. Iron ore, iron and steel, engineering goods, leather manufactures, handicrafts, etc., have figured in the major increases, and although during the current year, exports of both iron ore and steel have declined, the improved performance of exports of engineering goods has continued.
10. During the past few years, Government policy on import has been geared to the need to provide the essential inputs for the development not only of agriculture but also of industry so that the momentum of growth can be continued. During the last consultation, reference was made by the Indian representative to the liberalization of import licensing policy, particularly for priority industries, adopted in 1966. This liberal licensing policy for the fifty-nine priority industries accounting for three quarters of industrial output has been continued on a need-based basis. Actual users in these industries are entitled to apply for replenishment of import licences on the basis of consumption during the previous period. Selective liberalization has also been introduced in regard to the requirements of small scale-industry for which some of the difficult items are now sought to be bulked for imports, so as to reduce both the import costs and transportation charges. A number of policy measures which had been taken to promote exports have been continued, provision being made for exporters to secure their full raw material import requirements from

sources of supply of their choice. The requirements of exporting units for imported capital equipment are given the highest priority. Marketing and other promotional efforts have been intensified and as a measure of introducing greater cost-consciousness as well as awareness of the export opportunities and avenues abroad, a number of industries have been required to export between 5 to 10 per cent of their output. This special feature of import policy for the current year, namely 1969-70, has helped to bring about increased cost-consciousness in industry, forcing entrepreneurs to pare down inventories, bring about improved efficiency of labour as well as of management, and to seek to shape their purchase policies with a view to securing maximum economy and efficiency. Fiscal policies have been geared to assist exporters, and export promotion schemes for reducing some of the disadvantages arising out of a multiplicity of indirect taxes that industry has to bear have been adopted. The 1969-70 budget provided for a reduction in the export duty on jute, tea and mica, resulting in a loss of \$31 million to the exchequer.

11. While the overall trade and payments outlook as a result of the various fiscal and import liberalization measures has thus definitely improved, the outlook for the coming years continues to be one which calls for careful budgeting of resources and also highlights the need for continued assistance from friendly countries in order to help sustain the policies already adopted and to stimulate the rate of investment and growth of the economy in the coming years. Repayments of short-term borrowings from the International Monetary Fund due in 1970-71 amount to as much as \$205 million. Other debt repayment liabilities over the coming year would be as much as \$549 million. The aid for non-project imports promised at the Consortium meeting during the current year has yet to be translated into aid agreements and it seems that the total availability of resources may be less than anticipated. There has also been a noticeable slowing down of project aid, which has resulted in a slowing down of capital investments and to a decline in imports of capital goods. The greatest need of the economy is to raise the level of investments so that the growth of industrial production and of employment can be stepped up.

12. In the above context, the need is for increasing quantities of untied aid both in relation to the types of imports to be financed and to the sources from which the imports can be obtained. The effect of the total tied aid is to reduce significantly the extent to which Indian importers can be given flexibility in taking decisions regarding imports on purely commercial grounds. Relaxation of the restrictions on use of such assistance would promote the emergence of competitive conditions and would help the Government of India to improve the competitive position of Indian industries.

13. While the tariff obstacles to India's exports have been reduced somewhat as a result of concessions negotiated in the Kennedy Round, some of the major items of India's exports continue to suffer from high tariffs in important developed countries. There has also been little progress in regard to relaxation or removal of quota restrictions on certain products of substantial export interest to India. Early removal of these restrictions would enable India to augment her foreign exchange earnings and this would ease the continued balance-of-payments difficulties which stand in the way of further liberalization. The Government of India, therefore, hope that on these matters early and favourable action would be taken by the developed countries.

14. To sum up, while the past two years have seen a distinct improvement in the Indian economy, the overall situation and the balance-of-payments prospects continue to be such as to call for careful planning of import and export policies. The requirements of long-term growth can no longer be ignored. A better balance has been brought about in the economy partly through an improvement in output but also largely through a very sharp paring down of inventories, and if there is not to be a hiatus in the development of the economy in the future, a significant increase in investment outlays would be necessary during the coming year. The trend of import licensing during the first half of the current fiscal year, to which reference has already been made, together with the debt repayments due, highlight the generally difficult foreign exchange position over the coming year. The situation, therefore, calls for a combination of trade and aid policies which may help the Government of India to overcome the balance-of-payments difficulties in the longer run. The Fourth Plan Draft has set a target for export by 1973-74 which is crucial for achieving the longer-term viability and growth of the Indian economy, and which is also necessary for sustaining the level of imports estimated for 1973-74. Brief reference has already been made to some of the restrictions imposed by some of the major trading partners on India's exports. While this is an issue which is essentially suitable for bilateral discussions, the Government of India would hope for the continued interest and assistance of friendly countries in a combination of trade and aid policies which may help India achieve the export targets envisaged, and also pay for the imports necessary for the sustained development of the Indian economy.