



## Economy of India

The economy of India is the twelfth largest economy in the world by market exchange rates and the fourth largest by purchasing power parity (PPP) basis.

India was under socialist-based policies for an entire generation from the 1950s until the 1980s. The economy was characterised by extensive regulation, protectionism, and public ownership, leading to pervasive corruption and slow growth. Since 1991, continuing economic liberalisation has moved the economy towards a market-based system.

India's large service industry accounts for 54% of the country's GDP while the industrial and agricultural sector contribute 29% and 17% respectively. Agriculture is the predominant occupation in India, accounting for about 60% of employment. The service sector makes up a further 28% and industrial sector around 12%. The labor force totals half a billion workers. Major agricultural products include rice, wheat, oilseed, cotton, jute, tea, sugarcane, potatoes, cattle, water buffalo, sheep, goats, poultry and fish. Major industries include textiles, chemicals, food processing, steel, transportation equipment, cement, mining, petroleum, machinery, information technology enabled services and software.

India's per capita income (nominal) is \$1016, ranked 142<sup>nd</sup> in the world, while its per capita (PPP) of US\$2762 is ranked 129<sup>th</sup>. Previously a closed economy, India's trade has grown fast. India currently accounts for 1.5% of World trade as of 2007 according to the WTO. According to the World Trade Statistics of the WTO in 2006, India's total merchandise trade (counting exports and imports) was valued at \$294 billion in 2006 and India's services trade inclusive of export and import was \$143 billion. Thus, India's global economic engagement in 2006 covering both merchandise and services trade was of the order of \$437 billion, up by a record 72% from a level of \$253 billion in 2004. India's trade has reached a still relatively moderate share 24% of GDP in 2006, up from 6% in 1985.

Despite robust economic growth, India continues to face several major problems. The recent economic development has widened the economic inequality across the country. Despite sustained high economic growth rate, approximately 80% of its population lives on less than \$2 a day (PPP), more

than double the same poverty rate in China. Even though the arrival of Green Revolution brought end to famines in India, 40% of children under the age of three are underweight and a third of all men and women suffer from chronic energy deficiency

While the credit rating of India was hit by its nuclear tests in 1998, it has been raised to investment level in 2007 by S&P and Moody's. In 2003, Goldman Sachs predicted that India's GDP in current prices will overtake France and Italy by 2020, Germany, UK and Russia by 2025 and Japan by 2035. By 2035, it was projected to be the third largest economy of the world, behind US and China.

## **Sectors**

India ranks second worldwide in farm output. Agriculture and allied sectors like forestry, logging and fishing accounted for 16.6% of the GDP in 2007, employed 60% of the total workforce and despite a steady decline of its share in the GDP, is still the largest economic sector and plays a significant role in the overall socio-economic development of India. Yields per unit area of all crops have grown since 1950, due to the special emphasis placed on agriculture in the five-year plans and steady improvements in irrigation, technology, application of modern agricultural practices and provision of agricultural credit and subsidies since Green revolution in India. However, international comparisons reveal that the average yield in India is generally 30% to 50% of the highest average yield in the world.

India is the largest producer in the world of milk, cashew nuts, coconuts, tea, ginger, turmeric and black pepper. It also has the world's largest cattle population (193 million). It is the second largest producer of wheat, rice, sugar, groundnut and inland fish. It is the third largest producer of tobacco. India accounts for 10% of the world fruit production with first rank in the production of bananas, sapotas and mangoes.

## **Industry and services**

Industry accounts for 27.6% of the GDP and employ 17% of the total workforce. However, about one-third of the industrial labour force is engaged in simple household manufacturing only. In absolute terms, India is 16<sup>th</sup> in the world in terms of nominal factory output. India's small industry makes up 5% of carbon dioxide emissions in the world.

Economic reforms brought foreign competition, led to privatisation of certain public sector industries, opened up sectors hitherto reserved for the public sector and led to an expansion in the production of fast-moving consumer

goods. Post-liberalisation, the Indian private sector, which was usually run by oligopolies of old family firms and required political connections to prosper was faced with foreign competition, including the threat of cheaper Chinese imports. It has since handled the change by squeezing costs, revamping management, focusing on designing new products and relying on low labour costs and technology.

Textile manufacturing is the second largest source for employment after agriculture and accounts for 26% of manufacturing output. Tirupur has gained universal recognition as the leading source of hosiery, knitted garments, casual wear and sportswear. Dharavi slum in Mumbai has gained fame for leather products. Tata Motors' Nano attempts to be the world's cheapest car.

India is fifteenth in services output. It provides employment to 23% of work force, and it is growing fast, growth rate 7.5% in 1991–2000 up from 4.5% in 1951–80. It has the largest share in the GDP, accounting for 55% in 2007 up from 15% in 1950.

Business services (information technology, information technology enabled services, business process outsourcing) are among the fastest growing sectors contributing to one third of the total output of services in 2000. The growth in the IT sector is attributed to increased specialization, and an availability of a large pool of low cost, but highly skilled, educated and fluent English-speaking workers, on the supply side, matched on the demand side by an increased demand from foreign consumers interested in India's service exports, or those looking to outsource their operations. The share of India's IT industry to the country's GDP increased from 4.8% in 2005-06 to 7% in 2008. In 2009, seven Indian firms were listed among the top 15 technology outsourcing companies in the world. In March 2009, annual revenues from outsourcing operations in India amounted to US\$60 billion and this is expected to increase to US \$225 billion by 2020.

Most Indian shopping takes place in open markets and millions of independent grocery shops called kirana. Organized retail such supermarkets accounts for just 4% of the market as of 2008. Regulations prevent most foreign investment in retailing. Moreover, over thirty regulations such as "signboard licences" and "anti-hoarding measures" may have to be complied before a store can open doors. There are taxes for moving goods to states, from states, and even within states.

Tourism in India is relatively undeveloped, but growing at double digits. Some hospitals woo medical tourism.

## **Banking and finance**

The Indian money market is classified into: the organised sector (comprising private, public and foreign owned commercial banks and cooperative banks, together known as scheduled banks); and the unorganised sector (comprising individual or family owned indigenous bankers or money lenders and non-banking financial companies (NBFCs)). The unorganised sector and microcredit are still preferred over traditional banks in rural and sub-urban areas, especially for non-productive purposes, like ceremonies and short duration loans.

Prime Minister Indira Gandhi nationalised 14 banks in 1969, followed by six others in 1980, and made it mandatory for banks to provide 40% of their net credit to priority sectors like agriculture, small-scale industry, retail trade, small businesses, etc. to ensure that the banks fulfill their social and developmental goals. Since then, the number of bank branches has increased from 10120 in 1969 to 98910 in 2003 and the population covered by a branch decreased from 63800 to 15000 during the same period. The total deposits increased 32.6 times between 1971 to 1991 compared to 7 times between 1951 to 1971. Despite an increase of rural branches, from 1860 or 22% of the total number of branches in 1969 to 32,270 or 48%, only 32270 out of 5 lakh (500,000) villages are covered by a scheduled bank.

The public sector banks hold over 75% of total assets of the banking industry, with the private and foreign banks holding 18.2% and 6.5% respectively. Since liberalisation, the government has approved significant banking reforms. While some of these relate to nationalised banks (like encouraging mergers, reducing government interference and increasing profitability and competitiveness), other reforms have opened up the banking and insurance sectors to private and foreign players. Since liberalisation, the government has approved significant banking reforms. While some of these relate to nationalised banks (like encouraging mergers, reducing government interference and increasing profitability and competitiveness), other reforms have opened up the banking and insurance sectors to private and foreign players.

More than half of personal savings are invested in physical assets such as land, houses, cattle, and gold.

## **Natural resources**

India's total cultivable area is 1,269,219 km<sup>2</sup> (56.78% of total land area), which is decreasing due to constant pressure from an ever growing

population and increased urbanisation.

India has a total water surface area of 314,400 km<sup>2</sup> and receives an average annual rainfall of 1,100 mm. Irrigation accounts for 92% of the water utilisation, and comprised 380 km<sup>2</sup> in 1974, and is expected to rise to 1,050 km<sup>2</sup> by 2025, with the balance accounted for by industrial and domestic consumers. India's inland water resources comprising rivers, canals, ponds and lakes and marine resources comprising the east and west coasts of the Indian ocean and other gulfs and bays provide employment to nearly 6 million people in the fisheries sector. In 2008, India had the world's third largest fishing industry.

India's major mineral resources include coal, iron, manganese, mica, bauxite, titanium, chromite, limestone and thorium.

India meets most of its domestic energy demand through its 92 billion tonnes of coal reserves (about 10% of world's coal reserves). India's oil reserves, found in Bombay High off the coast of Maharashtra, Gujarat, Rajasthan and in eastern Assam meet 25% of the country's domestic oil demand. India's total proven oil reserves stand at 11 billion barrels, of which Bombay High is believed to hold 6.1 billion barrels and Mangala Area in Rajasthan, an additional 3.6 billion barrels. India's huge thorium reserves — about 25% of world's reserves — is expected to fuel the country's ambitious nuclear energy program in the long-run. India's dwindling uranium reserves stagnated the growth of nuclear energy in the country for many years. However, the Indo-US nuclear deal has paved the way for India to import uranium from other countries. India is also believed to be rich in certain renewable sources of energy with significant future potential such as solar, wind and biofuels (jatropha, sugarcane).

### **External trade and investment**

Until the liberalisation of 1991, India was largely and intentionally isolated from the world markets, to protect its fledging economy and to achieve self-reliance. Foreign trade was subject to import tariffs, export taxes and quantitative restrictions, while foreign direct investment was restricted by upper-limit equity participation, restrictions on technology transfer, export obligations and government approvals; these approvals were needed for nearly 60% of new FDI in the industrial sector.

In 2006-07, major export commodities included engineering goods, petroleum products, chemicals and pharmaceuticals, gems and jewellery, textiles and garments, agricultural products, iron ore and other minerals. Major import commodities included crude oil and related products,

machinery, electronic goods, gold and silver.

### **Global trade relations**

According to World Trade Organization (WTO), India accounted for 1.2% of the global trade in 2006. Until the liberalization of 1991, India was largely and intentionally isolated from the world markets, to protect its economy and to achieve self-reliance. Foreign trade was subject to import tariffs, export taxes and quantitative restrictions, while foreign direct investment (FDI) was restricted by upper-limit equity participation, restrictions on technology transfer, export obligations and government approvals; these approvals were needed for nearly 60% of new FDI in the industrial sector. The restrictions ensured that FDI averaged only around US\$200 million annually between 1985 and 1991; a large percentage of the capital flows consisted of foreign aid, commercial borrowing and deposits of non-resident Indians.

India's exports were stagnant for the first 15 years after independence, due to the predominance of tea, jute and cotton manufactures, demand for which was generally inelastic. Imports in the same period consisted predominantly of machinery, equipment and raw materials, due to nascent industrialization. Since liberalization, the value of India's international trade has become more broad-based and has risen to Rs. 63080109 crores in 2003–04 from Rs. 1250 crores in 1950–51. India's major trading partners are China, the US, the UAE, the UK, Japan and the EU. The exports during April 2007 were \$12.31 billion up by 16% and import were \$17.68 billion with an increase of 18.06% over the previous year.

India is a founding-member of General Agreement on Tariffs and Trade (GATT) since 1947 and its successor, the WTO. While participating actively in its general council meetings, India has been crucial in voicing the concerns of the developing world. For instance, India has continued its opposition to the inclusion of such matters as labour and environment issues and other non-tariff barriers into the WTO policies.

### **Balance of payments**

Cumulative Current Account Balance 1980-2008 based on the IMF data since independence, India's balance of payments on its current account has been negative. Since liberalisation in the 1990s (precipitated by a balance of payment crisis), India's exports have been consistently rising, covering 80.3% of its imports in 2002–03, up from 66.2% in 1990–91. India's growing oil import bill is seen as the main driver behind the large current account deficit. In 2007-08, India imported 120.1 million tonnes of crude oil, more than 3/4th of the domestic demand, at a cost of \$61.72 billion.

Although India is still a net importer, since 1996–97, its overall balance of payments (i.e., including the capital account balance), has been positive, largely on account of increased foreign direct investment and deposits from non-resident Indians; until this time, the overall balance was only occasionally positive on account of external assistance and commercial borrowings. As a result, India's foreign currency reserves stood at \$285 billion in 2008, which could be used in infrastructural development of the country if used effectively.

Due to the global late-2000s recession, both Indian exports and imports declined by 29.2% and 39.2% respectively in June 2009. Since the decline in imports was much sharper compared to the decline in exports, India's trade deficit reduced to \$252.5 billion.

India's reliance on external assistance and commercial borrowings has decreased since 1991–92, and since 2002–03, it has gradually been repaying these debts. Declining interest rates and reduced borrowings decreased India's debt service ratio to 4.5% in 2007. In India, External Commercial Borrowings (ECBs) are being permitted by the Government for providing an additional source of funds to Indian corporates. The Ministry of Finance monitors and regulates these borrowings (ECBs) through ECB policy guidelines.

### **Foreign direct investment in India**

As the fourth-largest economy in the world in PPP terms, India is a preferred destination for foreign direct investments (FDI); India has strengths in information technology and other significant areas such as auto components, chemicals, apparels, pharmaceuticals, and jewellery. Despite a surge in foreign investments, rigid FDI policies resulted in a significant hindrance. However, due to some positive economic reforms aimed at deregulating the economy and stimulating foreign investment, India has positioned itself as one of the front-runners of the rapidly growing Asia Pacific Region. India has a large pool of skilled managerial and technical expertise. The size of the middle-class population stands at 50 million and represents a growing consumer market.

Share of top five investing countries in FDI inflows. (2000–2007)			
Rank	Country	Inflows (Million USD)	Inflows (%)
1	<u>Mauritius</u>	85,178	44.24%
2	<u>United States</u>	18,040	9.37%
3	<u>United Kingdom</u>	15,363	7.98%
4	<u>Netherlands</u>	11,177	5.81%
5	<u>Singapore</u>	9,742	5.06%

India's recently liberalized FDI policy (2005) allows up to a 100% FDI stake in ventures. Industrial policy reforms have substantially reduced industrial licensing requirements, removed restrictions on expansion and facilitated easy access to foreign technology and foreign direct investment FDI. The upward moving growth curve of the real-estate sector owes some credit to a booming economy and liberalized FDI regime. In March 2005, the government amended the rules to allow 100 per cent FDI in the construction business. This automatic route has been permitted in townships, housing, built-up infrastructure and construction development projects including housing, commercial premises, hotels, resorts, hospitals, educational institutions, recreational facilities, and city- and regional-level infrastructure.

While market observers lament the arrival of the global recession on India's doorsteps, the obverse has also been true. Business magnates such as the expatriate Indian NRI's including Lakshmi Mittal of UK - Chairman ArcelorMittal and Arvind Sanmugam of Canada- Chairman World Police Academy, Chairman and CEO of Chez Leeloo Canada, Chairman of Chez Leeloo India, Director of Chez Leeloo Philippines, President of Canadian Peacemakers Corporation and Director of Tan Theta Entertainment and others have been building and interweaving their corporations with local business and government. Thus the NRI created employment opportunities are creating their own revenue source and revenue distribution within the nation.

A number of changes were approved on the FDI policy to remove the caps in most sectors. Fields which require relaxation in FDI restrictions include civil aviation, construction development, industrial parks, petroleum and natural gas, commodity exchanges, credit-information services and mining. But this still leaves an unfinished agenda of permitting greater foreign investment in politically sensitive areas such as insurance and retailing. FDI inflows into India reached a record US\$19.5 bn in fiscal year 2006/07 (April-March), according to the government's Secretariat for Industrial Assistance. This was more than double the total of US\$7.8 bn in the previous fiscal year. The FDI inflow for 2007-08 has been reported as \$24 bn and for 2008-09; it is expected to be above \$35 billion. A critical factor in determining India's continued economic growth and realizing the potential to be an economic superpower is going to depend on how the government can create incentives for FDI flow across a large number of sectors in India.

## **Infrastructure**

Development of infrastructure was completely in the hands of the public sector and was plagued by corruption, bureaucratic inefficiencies, urban-bias and an inability to scale investment. India's low spending on power, construction, transportation, telecommunications and real estate, at \$31 billion or 6% of GDP in 2002 had prevented India from sustaining higher growth rates. This has prompted the government to partially open up infrastructure to the private sector allowing foreign investment which has helped in a sustained growth rate of close to 9% for the past six quarters.

Some 600 million Indians have no mains electricity at all. While 80% of Indian villages have at least an electricity line, just 44% of rural households have access to electricity. According to a sample of 97,882 households in 2002, electricity was the main source of lighting for 53% of rural households compared to 36% in 1993. Some half of the electricity is stolen, compared with 3% in China. The stolen electricity amounts to 1.5% of GDP. Almost all of the electricity in India is produced by the public sector. Power outages are common. Many buy their own power generators to ensure electricity supply. As of 2005 the electricity production was at 661.6 billion kWh with oil production standing at 785,000 bbl/day. In 2007, electricity demand exceeded supply by 15%. Multi Commodity Exchange has tried to get a permit to offer electricity future markets.

Indian Road Network is developing. Trucking goods from Gurgaon to the port in Mumbai can take up to 10 days. India has the world's second largest road network. Container traffic is growing at 15% a year. Some 60% of India's container traffic is handled by the Jawaharlal Nehru Port Trust in Mumbai.

Internet use is rare; there were only 2.1 million broadband lines in India in January 2007.

Most urban cities have good water supply water 24 hours a day, while some smaller cities face water shortages in summer season. A World Bank report says it is an institutional problem in water agencies, or "how the agency is embedded in the relationships between politics and the citizens who are the consumers."

### **Economic disparities**

One of the critical problems facing India's economy is the sharp and growing regional variations among India's different states and territories in terms of per capita income, poverty, availability of infrastructure and socio-economic development. Seven low-income states - Bihar, Chhattisgarh, Jharkhand, Madhya Pradesh, Orissa, Rajasthan, and Uttar Pradesh - are home to more than half of India's population.

Between 1999 and 2008, the annualized growth rates for Gujarat (8.8%), Haryana (8.7%), or Delhi (7.4%) were much higher than for Bihar (5.1%), Uttar Pradesh (4.4%), or Madhya Pradesh (3.5%).

Poverty rates in rural Orissa (43%) and rural Bihar (40%) are some of the worst in the world. On the other hand, rural Haryana (5.7%) and rural Punjab (2.4%) compare well with middle-income countries.

The five-year plans have attempted to reduce regional disparities by encouraging industrial development in the interior regions, but industries still tend to concentrate around urban areas and port cities. After liberalization, the more advanced states are better placed to benefit from them, with infrastructure like well developed ports, urbanisation and an educated and skilled workforce which attract manufacturing and service sectors. The union and state governments of backward regions are trying to reduce the disparities by offering tax holidays, cheap land, etc., and focusing more on sectors like tourism, which although being geographically and historically determined, can become a source of growth and is faster to develop than other sectors.