DELHI POLICY GROUP

INDIA'S MACRO TRENDS

Advancing India's Rise as a Leading Power

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India's Macro Trends

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India's Macro Trends is produced by the Delhi Policy Group, an independent and autonomous, not for profit think tank which focuses primarily on strategic issues of critical national interest.

In keeping with the growing dynamism of India's foreign and security policy, the DPG is expanding its focus areas to include India's broader regional and global role and the strategic partnerships that advance India's rise as a leading power. To support that goal, the DPG undertakes research and organizes policy interactions across a wide canvas, including strategic and geo-political issues, geo-economic issues and defence and security issues.

DPG does not take specific policy positions; accordingly, all views, positions, and conclusions expressed in this publication should be understood to be solely those of the author(s).

Ambassador Hemant Krishan Singh
Director General

SECTION 1: MACRO CURRENTS

1. Cabinet Reshuffle

Prime Minister Narendra Modi carried out a major Cabinet reshuffle on September 3, 2017, inducting nine new Ministers. Highlights included the appointment of Nirmala Sitharaman as the first dedicated woman Defence Minister to hold that office in India's 70-year history, and the appointment of four former bureaucrats to serve in the Cabinet. The Cabinet changes saw rewards for high performers and prioritised efficiency of governance ahead of the 2019 general elections. With its statutory maximum strength of 81 members, the Cabinet still has room for inducting leaders from new and potential BJP allies among regional parties.

2. GST: Introduction and Impact

Following the passage of the GST Act on March 29, 2017, the nationwide Goods and Services Tax (GST) came into effect from July 1, 2017. As a comprehensive, multi-stage, destination based tax, GST is expected to eventually create positive socio-economic outcomes, reduce inflation and yield higher revenue collection. Despite initial technical glitches and new compliance burdens on businesses, the transition to GST was relatively smooth. On September 28, 2017 Prime Minister Modi urged the bureaucracy to handhold small businesses and traders to resolve their compliance problems and help bring them into the GST Network.[1]

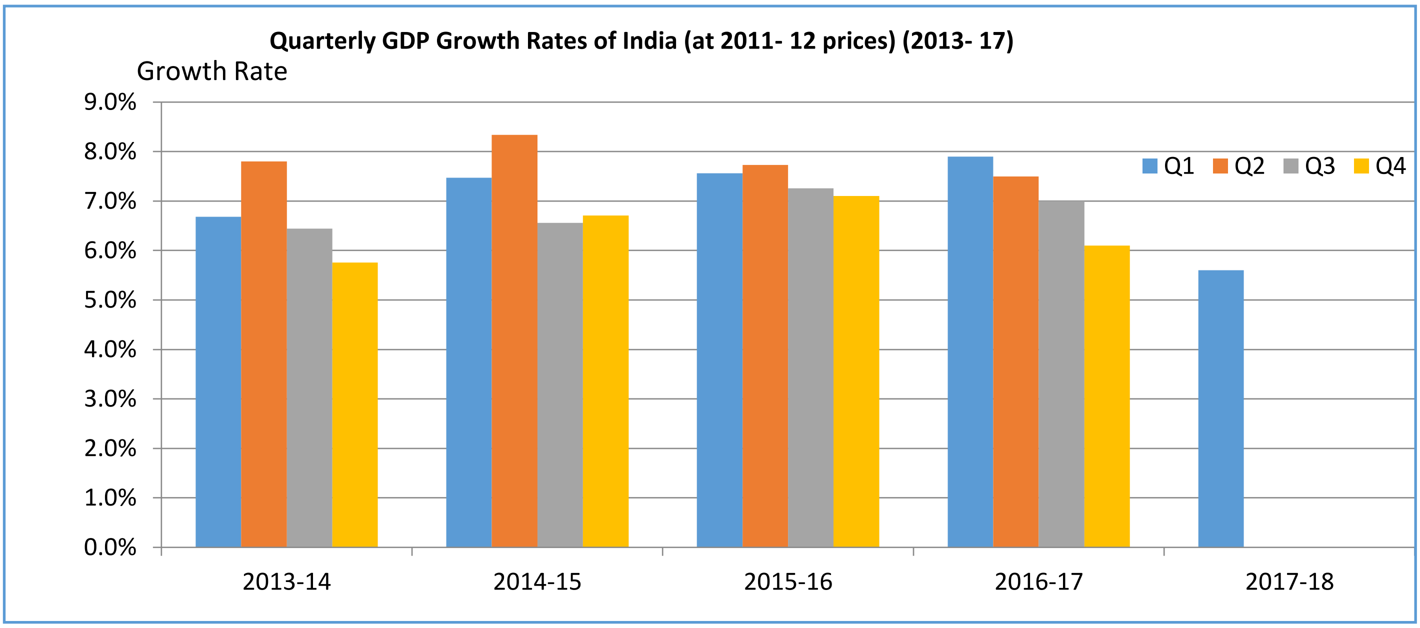
3. Economy

After a fairly robust 7.1% GDP growth in 2016-17, the gradual decline of GDP over the past five quarters to 5.7% in Q1 (April-June) of 2017-18 is being widely debated on partisan lines. Both the lingering effects of demonetisation (November 9, 2016) and transitory challenges following the introduction of GST (July 1, 2017) are seen to be impacting adversely on the economy, but the larger cause for concern is that growth engines are subdued. The Index of Industrial

Production (IIP) expanded by a modest 1.2% in July, 2017 with only mining and electricity growing by 4.8% and 6.5% respectively.

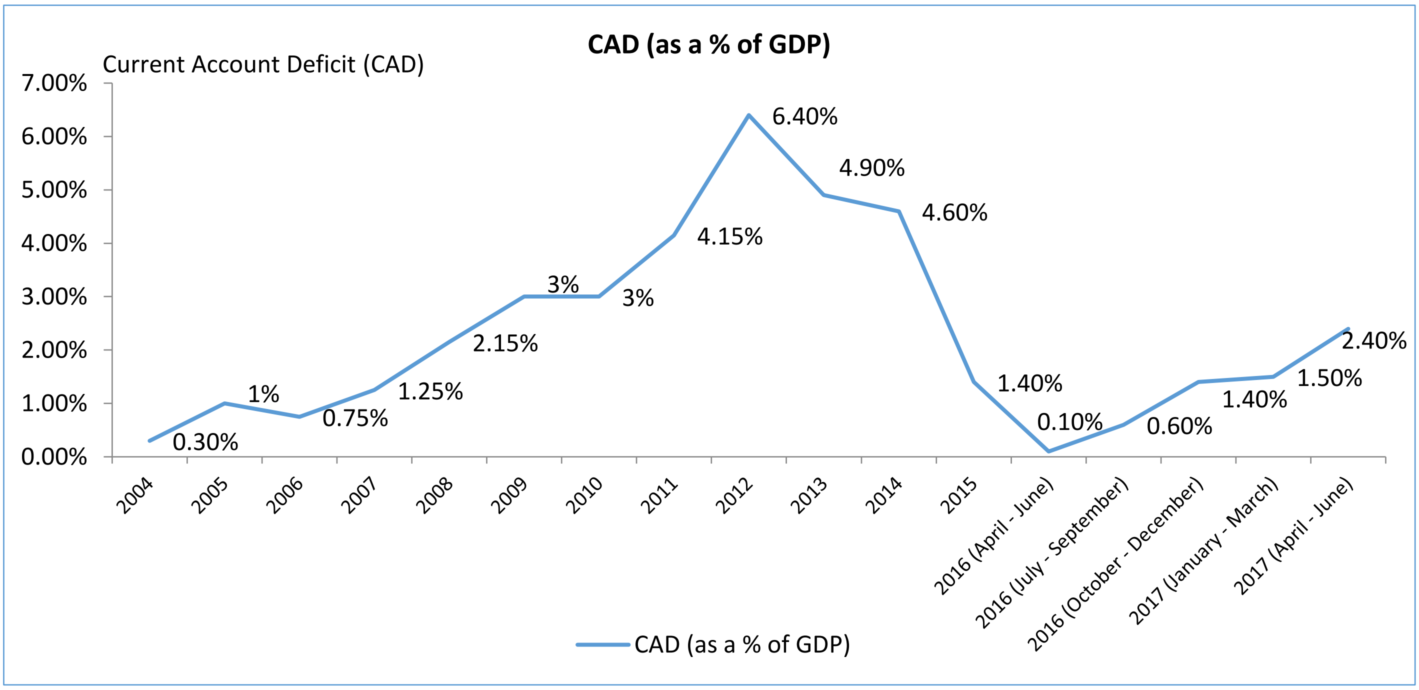
Sajjid Z. Chinoy, chief India economist at J.P. Morgan, explains that after March 2016, the Indian economy began slowing down as a natural consequence of the oil price windfall rolling off and the economy embarking on deleveraging. After demonetisation, the slowdown has been compounded by a negative supply shock as domestic supply chains were disrupted, temporarily inducing a 13% spurt in mainly manufacturing imports and quadrupling the current account deficit from 0.6% to 2.4% of GDP (Figures 1 and 2). This will self-correct over time, but the government can help by improving the regulatory and business environment for SMEs to resolve their teething problems with GST and ease their burdens on entering the formal sector. As the entire purpose of demonetisation and GST is to formalise the Indian economy, none of these temporary trends are surprising and there is no reason for government policy makers to abandon fiscal restraint by trading off macroeconomic stability for growth.[2]

Figure 1: Quarterly GDP Growth Rate of India



Source: *CSO | Graphics: DPG*

Figure 2: Current Account Deficit Pattern, 2004-2017



Source: *DGCIS, Kolkata |Graphics: DPG*

In its latest update on the Asian Development Outlook 2017 released by the ADB on September 26, 2017, the ADB now forecasts India's growth in FY 2017-18 to reach 7%, a 0.4% decline from earlier estimates in April this year. The ADB's outlook for FY 2018-19 projects a 7.4% GDP growth, down from the previous projection of 7.6%. At the same time, the ADB believes that despite short-term hiccups, the government's ambitious reform agenda will lead to higher long-term growth. The ADB also expects India to remain one of the world's most dynamic emerging economies.[3]

Prime Minister Narendra Modi appointed a new five-member Economic Advisory Council (PMEAC) on September 25, 2017, headed by Niti Aayog member Bibek Debroy and including economists Surjit Bhalla, Rathin Roy and Ashima Goyal. Niti Aayog Principal Adviser and former Finance Secretary Ratan Watal is the Member-Secretary of the PMEAC.

4. Inauguration of the Sardar Sarovar Dam

Prime Minister Narendra Modi inaugurated the Sardar Sarovar Dam, built on the Narmada River, on September 17, 2017. This 1.20 km long, 138.68 metre high mega dam with the provision of 4.73 million acre feet of water storage, is the world's second largest dam in terms of volume. Apart from hydro-power generating units with installed capacity of 1,200 MW and 250 MW, Sardar Sarovar is expected to irrigate a massive 1.8 million hectares of land, covering 9,000 villages in the state of Gujarat through a vast network of canals. The project had been controversial because of environmental concerns but is widely expected to benefit the economy of Gujarat and neighbouring states.[4]

SECTION 2: MACRO FLOWS

1. New FDI Policy

On August 28, 2017, the Department of Industrial Policy and Promotion (DIPP), Government of India, launched a revised Foreign Direct Investment Policy, 2017-2018 (FDI Policy 2017). The revised policy aims to bring in large scale reforms in FDI inflows through the following set of measures[5]:

- Introduction of the 'Foreign Investment Facilitation Portal' (FIFP), an administrative body to facilitate FDI applicants, post the winding up of the Foreign Investment Promotion Board.

- Inclusion of sector-specific administrative ministry/department 'Competent Authorities', empowered to facilitate government approval for FDI. Authorities mentioned in the FDI Policy 2017 include the DIPP for applications of FDI in the Single Brand, Multi Brand and Food Product retail trading. The Department of Economic Affairs has been empowered to handle FDI in the financial services sector.

- Introduction of a 'Standard Operating Procedure' (SOP) to process FDI proposals.

- An LLP, operating in sectors/activities where 100% FDI is allowed under the automatic route (without FDI-linked performance conditions), is now permitted to convert into a company. Similarly, conversion of a company into an LLP is also now permitted under the automatic route.

- Issue of Convertible Notes by Start-ups.

- To further liberalise the manufacturing sector (which allows 100% FDI under the automatic route), 100% FDI under the government approval route has been allowed for retail trading, including through e-commerce, in respect of food products manufactured and/or produced in India.

- The threshold for FDI in existing projects under the automatic route was increased from 74% to 100% for civil aviation.

- In single brand retailing sourcing norms applicable for FDI were relaxed and will not be applicable up to three years from commencement of the business.

- In other financial services, the previously applicable capitalisation norms for non-banking financial services companies were struck off, and all financial sector activities by entities already regulated by financial sector regulators will fall under the 100% automatic route of investment, with applicability of sectoral laws.

SECTION 3: MACRO NEWS

An "India Innovation Index" has been developed by the World Economic Forum, NITI Aayog, the World Intellectual Property Organization and Cornell University. The index has been measuring innovation performance of all Indian states with the aim of taking India towards an innovation-driven economy. The index is based on key pillars of innovation and sub-indices facilitating policies that promote inclusive growth. The pillars of the index include the strength of institutions, capacity of human capital and research, supporting infrastructure and the level of business sophistication, among others.[6]

Globally, India continues to rise in the Global Innovation Index (GII) rankings[7] for the second year in succession. In this year's rankings, India improved its position from 66 to 60. Last year, India's ranking had improved from 81 to 66. This improvement is in line with trends among various Asian and middle-income countries.

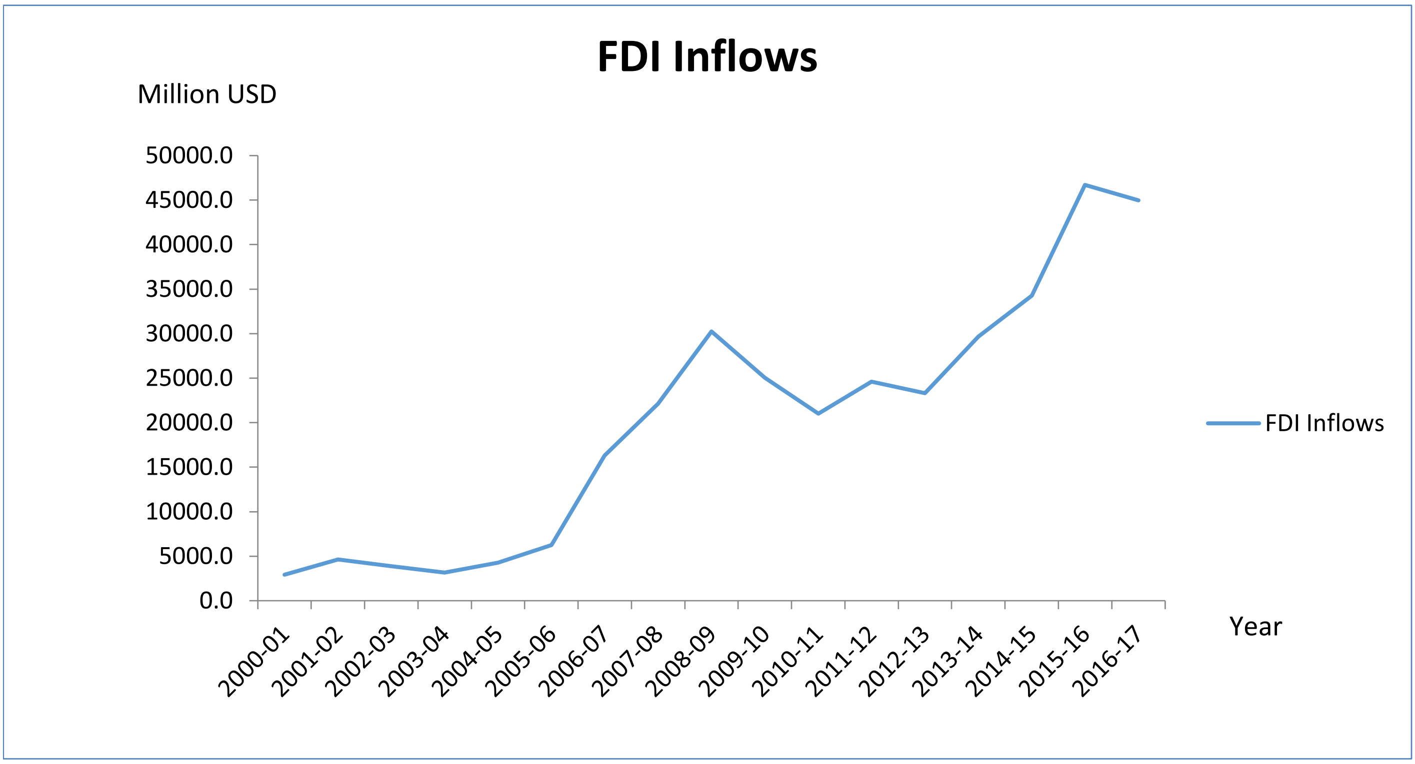
India's NITI Aayog will host the eighth annual Global Entrepreneurship Summit (GES), in partnership with the US Administration, in Hyderabad from November 28-30, 2017. The four primary focus areas of GES 2017 will be healthcare, financial technology, energy and infrastructure, and media and entertainment.[8]

SECTION 4: MACRO LINES

1. Foreign Direct Investment (FDI) Patterns

The long-term pattern of FDI inflows into India shows a steadily increasing trend, apart from a dip between 2008-2010 owing to the global financial crisis. FDI inflows have also slowed down post demonetisation (Figure 3).

Figure 3: Pattern of FDI Inflows

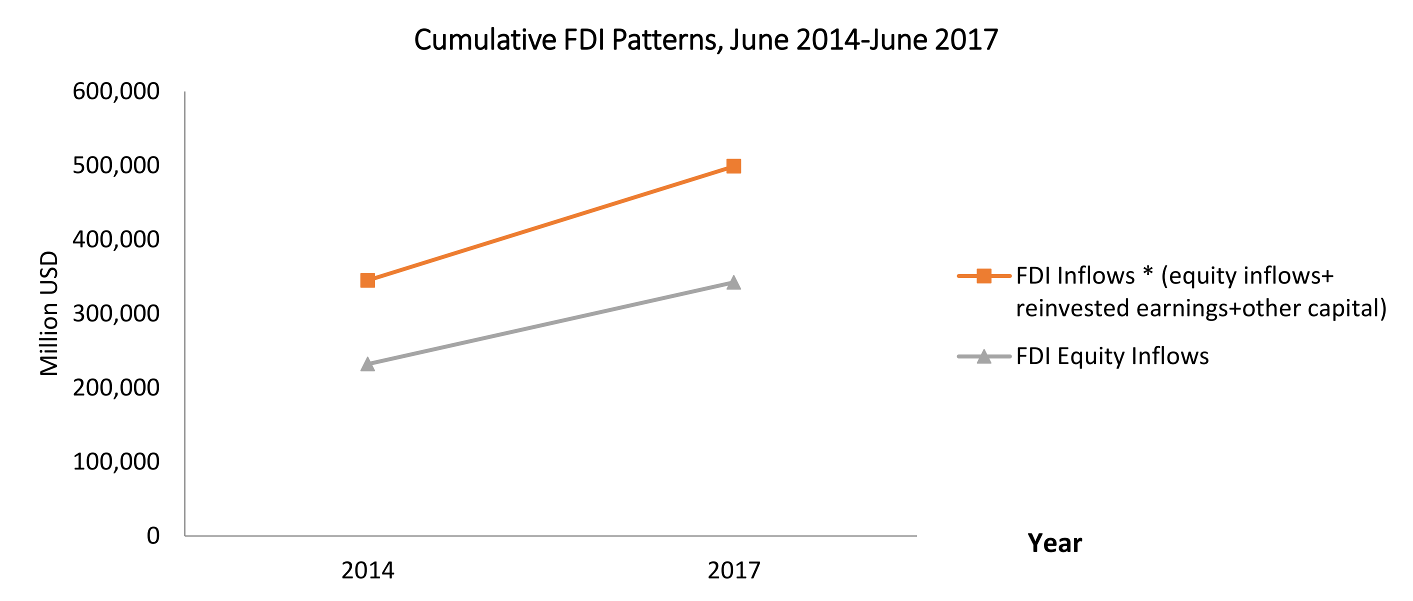


** Total FDI includes – direct, green field investments as well as portfolio investments

Source: RBI Statistics |Graphics: DPG

Cumulative FDI inflows (which include equity inflows + reinvested earnings + other capital) have increased from $34.50 billion in June 2014 to $49.89 billion in June, 2017. In the same period, cumulative FDI equity inflows (excluding amounts remitted through RBI's NRI schemes) have increased from $23.20 billion to $34.24 billion (Figure 4).

Figure 4: Cumulative FDI Patterns, June 2014-June 2017



Statistical Source: Department of Industrial Policy and Promotion, Government of India |Graphics: DPG

The countrywise ranking of leading contributors to FDI stock in India from 2000-2017 can be seen in Table 1.

Table 1: Share of Countries in Cumulative FDI Stock in India, 2000-2017

Country (Rankwise)	Share	FDI stock ($ million)
Mauritius	34%	111638
Singapore	17%	54590
Japan	8%	25675
U.K.	7%	24591
The Netherlands	6%	20682
U.S.A	6%	20323
Germany	3%	9698
Cyprus	3%	9156
France	2%	5725
UAE	1%	4705

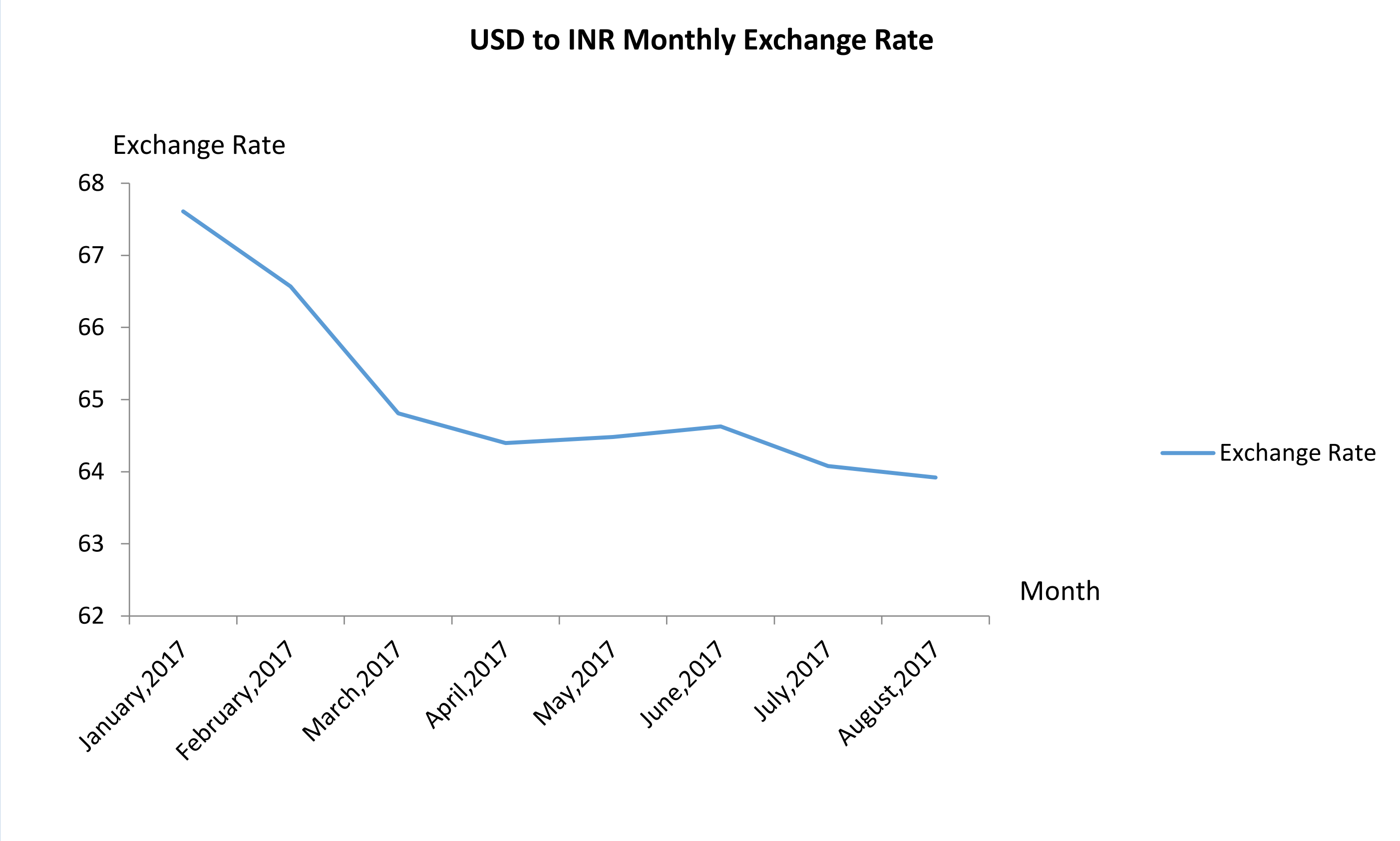
Source: Department of Industrial Policy and Promotion, Government of India | Table: DPG

3. Forex Reserves and Exchange Rate Patterns

India's foreign currency reserves reached an all-time high of $400.726 billion on September 8, 2017, the sixth highest in the world. Favourable inflows of foreign direct investment and portfolio investments in India's capital markets have contributed to this trend. Foreign exchange reserves had hit the $300 billion mark in March, 2008, and it has taken nine years to reach the new level.[9]

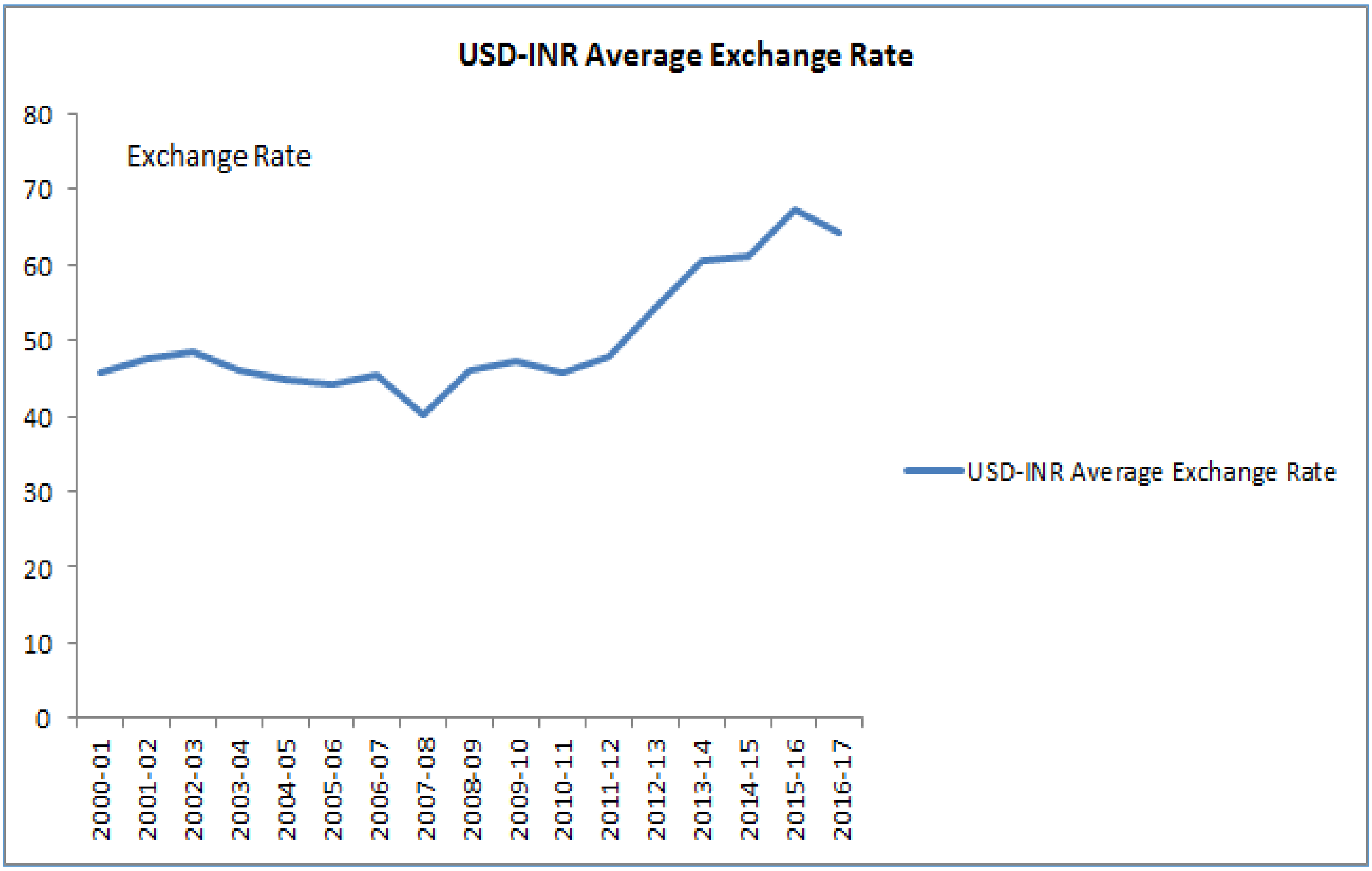
The exchange rate of the Indian rupee has been appreciating in 2017 (Figure 5). This has provided impetus to FII capital inflows, but has also contributed to rising imports and an increase in the current account deficit (Figure 2). However, the long-term trend of the Rupee-Dollar exchange rate is fairly stable, a reflection of the stable macroeconomic and foreign exchange fundamentals of the Indian economy (Figure 6).

Figure 5: Monthly Exchange Rate Patterns in 2017



Source: www.poundsterlinglive.com | Graphics: DPG

Figure 6: USD-Rupee Exchange Rate Patterns



Source: RBI Statistics | Graphics: DPG

SECTION 5: TRADE PATTERNS

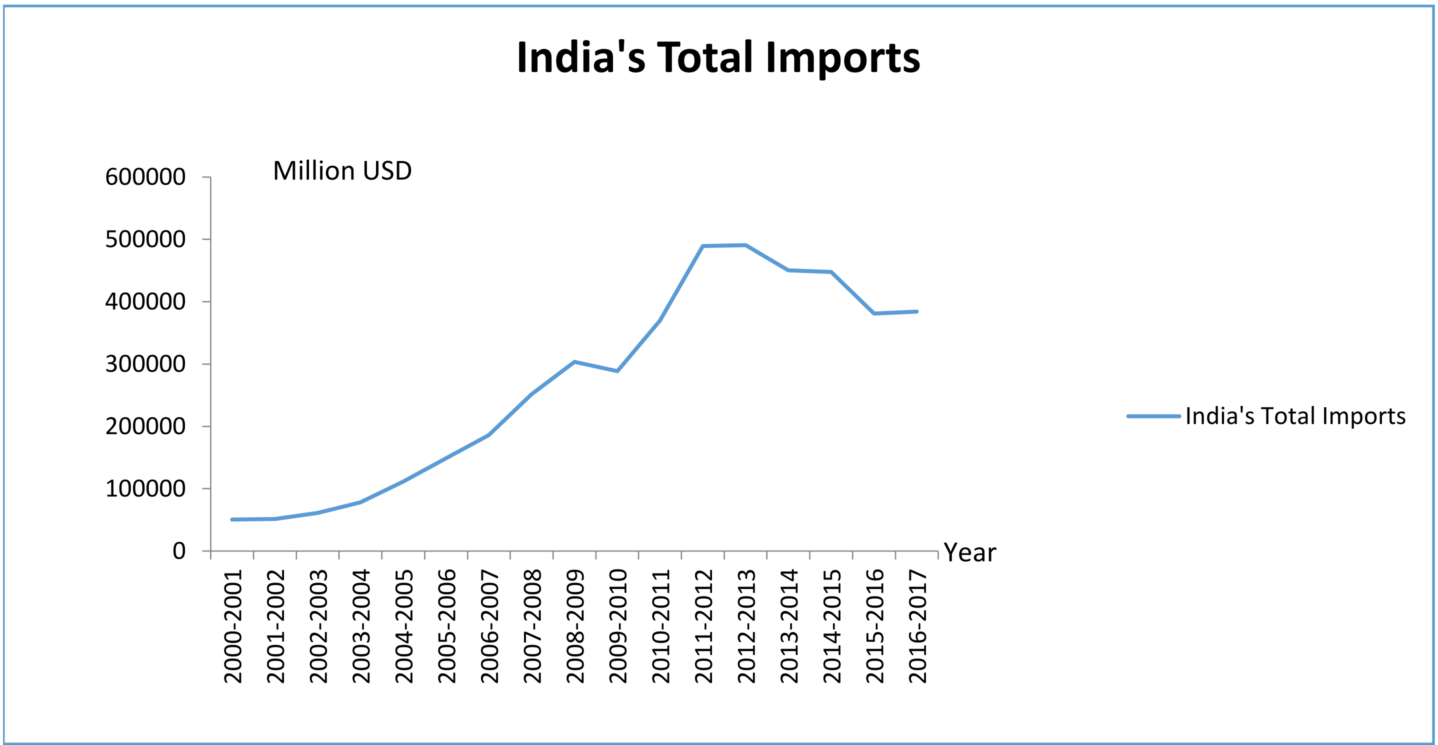
India's total exports, imports and trade balance can be seen in Figures 7, 8 and 9 respectively.

After peaking at $791 billion in 2012-13, India's total merchandise trade has progressively declined to $660 billion in 2016 – 17.

Figure 7: India's Total Exports to Destination over the years

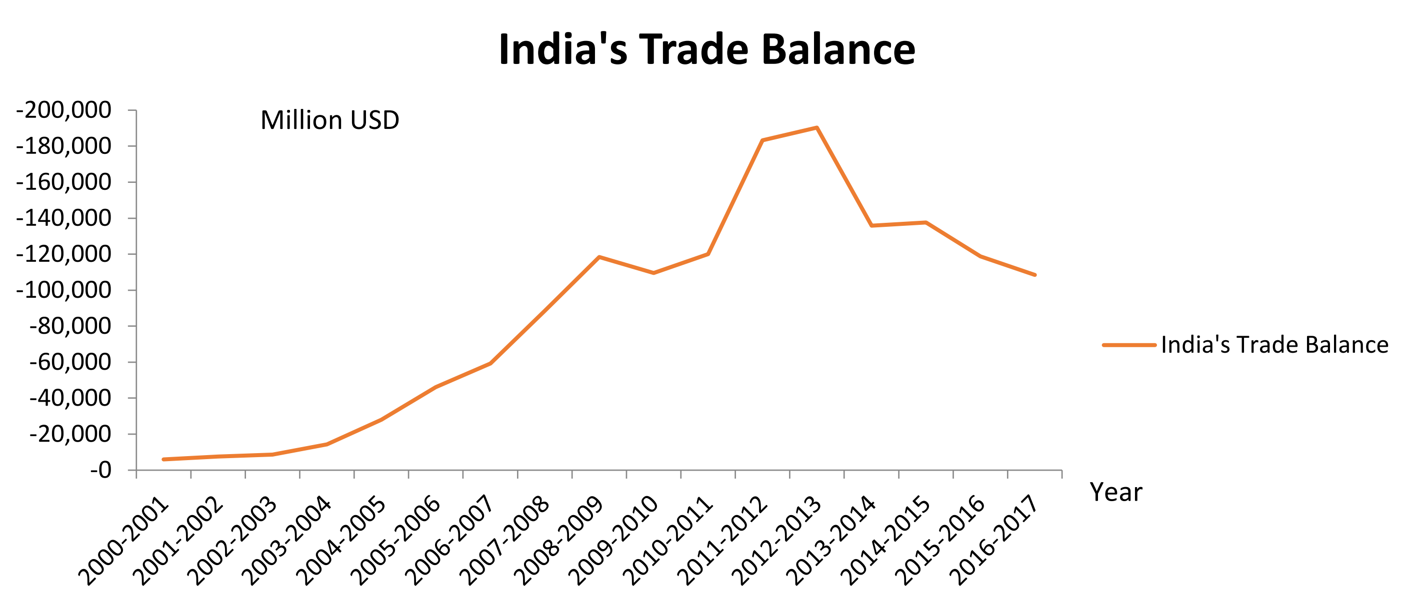
Data Source: - Ministry of Commerce and Industry, Department of Commerce | Graphics: DPG

Figure 8: India's Total Imports from source over the years



Data Source: - Ministry of Commerce and Industry, Department of Commerce | Graphics: DPG

Figure 9: India's Trade Balance over the years



Data Source: - Ministry of Commerce and Industry, Department of Commerce | Graphics: DPG

India's major trading relationships with the various regions of the world can be seen in Table 2.

Overall, the ASEAN+5 (RCEP) grouping is India's largest trade partner, followed by the European Union, ASEAN, China, USA, Africa and Latin America. However, among individual countries, the US is the largest destination of India's exports (15.3%), while China is the largest source of India's imports (15.94%).

Between 2015-2016 and 2016-2017, India's trade with ASEAN showed the greatest buoyancy, increasing by 10.01%. In the same period, India's exports to ASEAN grew by 23.09%.

Table 2: India's Major Trading Relationships with various regions (in Million USD)

Indicators (in USD Million)	Region	2014-2015	2015-2016	2016-2017	%Growth (Year on year growth, 2015-16 to 2016-17)
Exports	**ASEAN + 5 (RCEP countries)**	310338.48	262290.13	275851.71	5.17%
	Share in Total Exports (%)	18.32	17.51	19.03	
	European Union	49315.35	44461.24	47167.92	6.09%
	Share in Total Exports (%)	15.89	16.95	17.09	
	USA	42448.66	40335.82	42212.27	4.65%
	Share in Total Exports (%)	13.68	15.38	15.3	
	ASEAN	31812.58	25154.5	30961.62	23.09%
	Share in Total Exports (%)	10.25	9.59	11.22	
	Africa	25,167.48	19,714.95	18,256.05	-7.40%
	Share in Total Exports (%)	8.11	7.52	6.62	
	CHINA	11934.25	9010.35	10171.18	12.88%
	Share in Total Exports (%)	3.85	3.44	3.69	
	Latin America	11,528.41	7,530.80	7,230.94	-3.98%
	Share in Total Exports (%)	1.52	1.17	1.10	

Indicators (in USD Million)	Region	2014-2015	2015-2016	2016-2017	%Growth (Year on year growth, 2015-16 to 2016-17)
Imports	**ASEAN + 5 (RCEP)**	448033.41	381006.63	384355.56	0.88%
	Share in Total Imports (%)	31.16	35.16	35.36	
	CHINA	60413.17	61706.83	61281.57	-0.69%
	Share in Total Imports (%)	13.48	16.2	15.94	
	European Union	49207.74	43898.1	42359.23	-3.51%
	Share in Total Imports (%)	10.98	11.52	11.02	
	ASEAN	44714.77	39909.6	40617.31	1.77%
	Share in Total Imports (%)	9.98	10.47	10.57	
	Africa	33,375.43	28,037.74	24,897.59	-11.20%
	Share in Total Imports (%)	7.45	7.36	6.48	
	USA	21814.6	21781.39	22307.44	2.42%
	Share in Total Imports (%)	4.87	5.72	5.8	
	Latin America	26,951.76	17,691.79	17,290.63	-2.27%
	Share in Total Imports (%)	6.02	4.64	4.50	
Total Trade	**ASEAN + 5 (RCEP)**	196466.64	179881.49	188385.2	4.73%
	Share of RCEP Trade Basket (%)	25.91	27.96	28.53	
	European Union	94831	88943.55	94136.77	5.84%
	Share of European Union Trade Basket (%)	12.5	13.83	14.26	
	ASEAN	76527.36	65064.11	71578.93	10.01%
	Share of ASEAN Trade Basket (%)	10.09	10.11	10.84	
	CHINA	72347.42	70717.18	71452.75	1.04%
	Share of Chinese Trade Basket (%)	9.54	10.99	10.82	
	USA	64263.26	62117.21	64519.71	3.87%
	Share of USA Trade Basket (%)	8.47	9.66	9.77	
	Africa	58,542.91	47,752.69	43,153.64	-9.63%
	Share in Total Imports (%)	7.72	7.42	6.54	
	Latin America	38,480.17	25,222.59	24,521.57	-2.78%
	Share in Total Imports (%)	5.07	3.92	3.71	
	India's Total Trade Basket	758371.89	643296.75	660207.28	2.63%

Data Source: - Ministry of Commerce and Industry, Department of Commerce | Table: DPG

***

Endnotes:

[1] Source: TNN, September 28, 2017

[2] Chinoy, S, 2017, September 30, "Pause before you leap", *The Indian Express* URL*: http://indianexpress.com/article/opinion/columns/pause-before-you-leap-gdp-taxation-4867578/*

[3] https://www.pressreader.com/india/business-standard/20170927/281552291050214

[4] http://www.indiatimes.com/news/india/sardar-sarovar-narmada-dam-all-the-facts-about-the-world-s-2nd-largest-dam-why-it-matters-329907.html

[5] http://dipp.nic.in/sites/default/files/CFPC_2017_FINAL_RELEASED_28.8.17.pdf

[6] Source: http://pib.nic.in/newsite/PrintRelease.aspx?relid=157941

[7] Source: https://www.globalinnovationindex.org/gii-2017-report

[8] Source: http://economictimes.indiatimes.com/news/economy/policy/niti-aayog-set-to-organise-global-entrepreneurship-summit-in-november/articleshow/60883272.cms

[9] Source: http://indianexpress.com/article/business/banking-and-finance/forex-reserves-cross-400-bn-for-the-1st-time-on-asset-surge/

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