Report of the Central Board of Directors on the working of the Reserve Bank of India for the year ended June 30, 2004 submitted to the Central Government in terms of Section 53(2) of the Reserve Bank of India Act, 1934

RESERVE BANK OF INDIA ANNUAL REPORT 2003-04

CENTRAL BOARD / LOCAL BOARDS

GOVERNOR
Y.V. Reddy

DEPUTY GOVERNORS

Rakesh Mohan

K.J. Udeshi

DIRECTORS NOMINATED UNDER SECTION 8 (1) (b) OF THE RBI ACT, 1934

Y.H. Malegam

Mihir Rakshit

K. Madhava Rao

DIRECTORS NOMINATED UNDER SECTION 8 (1) (c) OF THE RBI ACT, 1934

Ratan N. Tata

Amrita Patel

K. P. Singh

V. S. Vyas

D. S. Brar

C.N. R. Rao

H. P. Ranina

N. R. Narayana Murthy

Suresh Krishna

Ashok S. Ganguly

DIRECTOR NOMINATED UNDER SECTION 8 (1) (d) OF THE RBI ACT, 1934

D.C. Gupta

MEMBERS OF LOCAL BOARDS

WESTERN AREA

Y.H. Malegam

K. Venkatesan

Dattaraj V. Salgaocar

Jayanti Lal Bavjibhai Patel

Mahendra Singh Sodha

EASTERN AREA

Mihir Rakshit

P. D. Chitlangia

A. K. Saikia

Sovan Kanungo

NORTHERN AREA

Mitha Lal Mehta

Ram Nath

Pritam Singh

SOUTHERN AREA

K. Madhava Rao

C. P. Nair

S. Ramachander

M. Govinda Rao

Devaki Jain

As on June 30, 2004

PRINCIPAL OFFICERS

(As on June 30, 2004)

EXECUTIVE DIRECTORS	R.B. Barman
	Smt. S. Gopinath
	P.K. Biswas
	Smt. Usha Thorat
	A.V. Sardesai
	P.V.Subba Rao
PRINCIPAL LEGAL ADVISER	N.V.Deshpande *
* With status equivalent to that of the Bank's ED	
PRINCIPAL MONETARY POLICY ADVISER	D. Anjaneyulu **
** With status equivalent to that of the Bank's ED	
CENTRAL OFFICE	
Department of Administration and Personnel Management	G. K. Sharma, Chief General Manager-in-Charge
Department of Banking Operations and Development	C.R. Muralidharan, Chief General Manager-in-Charge
Department of Banking Supervision	G. Gopalakrishna, Chief General Manager-in-Charge
Department of Currency Management	V.R. Gaikwad, Chief General Manager
Department of Economic Analysis and Policy	Narendra Jadhav, Principal Adviser
Department of Expenditure and Budgetary Control	A.N. Rao, Chief General Manager
Department of External Investments and Operations	T.C. Nair, Chief General Manager-in-Charge
Department of Government and Bank Accounts	V.S. Das, Chief General Manager-in-Charge
Department of Information Technology	R. Gandhi, Chief General Manager-in-Charge
Department of Non-Banking Supervision	O.P. Aggarwal, Chief General Manager-in-Charge
Department of Statistical Analysis and Computer Services	K.S.R. Rao, Officer-in-Charge
Foreign Exchange Department	Smt. G.E. Koshie, Chief General Manager-in-Charge
Financial Institutions Division	S.S. Gangopadhyay, Chief General Manager
Human Resources Development Department	Sandip Ghose, Chief General Manager
Industrial and Export Credit Department	Smt. R.K. Makhija, Chief General Manager
Inspection Department	H.V. Rane, Chief General Manager
Internal Debt Management Department	H.R. Khan, Chief General Manager-in-Charge
Legal Department	*
Monetary Policy Department	**
Premises Department	J.B. Bhoria, Chief General Manager
Rural Planning and Credit Department	C.S. Murthy, Chief General Manager-in-Charge
Secretary's Department	H.N. Prasad, Chief General Manager & Secretary
Urban Banks Department	S. Karuppasamy, Chief General Manager-in-Charge
COLLEGES	**PRINCIPALS**
Bankers Training College, Mumbai	Karuna Sagar
College of Agricultural Banking, Pune	Smt. Phulan Kumar
Reserve Bank Staff College, Chennai	Smt. C. Chandramouliswaran
OFFICES	**REGIONAL DIRECTORS**
Chennai	B. Ghosh
Kolkata	V.K. Sharma
Mumbai	M.P. Kothari
New Delhi	Ramesh Chander
BRANCHES	**REGIONAL DIRECTORS**
Ahmedabad	Smt. Vani J. Sharma
Bangalore	Smt. D. Muthukrishnan
Bhopal	K.V.Rajan
Bhubaneswar	G. Jaganmohan Rao (Gr.E)
Chandigarh	D.P.S. Rathore
Guwahati	Surindra Kumar
Hyderabad	G.Padmanabhan
Jaipur	Smt. Deepa Srivastava
Jammu	M.D.Dasari (Gr.E)
Kanpur	B. K. Vasdev
Nagpur	P. Aravind
Patna	S. Ganesh
Thiruvananthapuram	N. Krishna Mohan
	CHIEF GENERAL MANAGER
Lucknow	S.C. Agrawal
	GENERAL MANAGER (O-in-C)
Navi Mumbai, Belapur	Deepak Singhal
	GENERAL MANAGER (O-in-C)
Kochi	M.O. Sebastian

*For the Year July 1, 2003 to June 30, 2004**

PART ONE : THE ECONOMY : REVIEW AND PROSPECTS

I MACROECONOMIC POLICY ENVIRONMENT*

INTRODUCTION

1.1 Global recovery, which was somewhat hesitant earlier, firmed up and spread across various parts of the world in 2003 and continued through the first quarter of 2004 in an environment marked by heightened uncertainty. World merchandise trade accelerated in the second half of 2003 and financial flows to developing countries rebounded from subdued levels witnessed in the post-Asian crisis years. Persisting excess capacity and unemployment moderated potential inflationary pressures emanating from rising commodity prices. Consequently, inflation remained largely benign worldwide. Given the virtual absence of inflationary fears and prevalence of abundant liquidity conditions, an accommodative monetary policy stance was generally pursued in support of the recovery except in a few countries where rising asset prices prompted pre-emptive tightening. Financial markets experienced a broad-based strengthening, aided by the orderly depreciation of the US dollar. Improvements in corporate profitability and credit quality balanced the appetite for risk, enabling some consolidation of gains towards the close of 2003. These developments markedly improved the near-term outlook for the global economy, despite the risks from persistent US macro imbalances and rising oil prices weighing upon the transition to a higher interest rate regime in the emerging phase of the global business cycle.

1.2 India surged ahead of the global recovery on the back of a sharp turnaround in agriculture in 2003-04, aided by a normal monsoon (Appendix Table I.1). Industrial and services sector activities strengthened significantly, reinforced by higher rural consumption demand and a robust growth in merchandise exports for the second consecutive year. Consequently, India's real GDP grew at an impressive 8.2 per cent during 2003-04. In the post-Independence history, India's real GDP grew by over 8.0 per cent only on three occasions [*i.e.,* 1967-68 (8.1 per cent), 1975-76 (9.0 per cent) and 1988-89 (10.5 per cent)]. On these three occasions, however, the share of agriculture in GDP was much higher than in 2003-04. In 2003-04, while the rebound in agriculture was a significant driving force, the overall growth acceleration was widespread, drawing from industry, services and exports.

1.3 Growth prospects during the year were aided by a generally stable inflation situation. With orderly and easy conditions in the financial markets engendered by domestic and international sources of liquidity, interest rates continued to rule at low levels (Appendix Tables I.2 and I.3). This favourable environment, combined with restructuring by the industrial sector under competitive pressures, provided a significant boost to the profitability of the corporate sector. Unprecedented portfolio flows led to a strong rally in the stock markets with share prices touching new highs.

1.4 A resurgent industrial sector, improved corporate sector profitability and record resource mobilisation by way of divestment helped in fiscal consolidation with the revised fiscal deficit for the year turning out to be lower by 0.8 per cent of GDP than the budget estimates. Buoyant software exports and record workers' remittances led to a current account surplus for the third year in succession even as the merchandise trade deficit expanded due to the strong industrial recovery underway. The sustained buoyancy in merchandise exports was led by manufactures, reflecting structural changes and the growing competitiveness of the industrial sector. The overall strengthening of the balance of payments was reflected in an unprecedented accretion to India's foreign exchange reserves, which by March 2004, touched US $ 113 billion, the sixth highest in the world.

1.5 Achieving high growth rates on a sustainable basis requires further improvements in productivity

* While the Reserve Bank of India's accounting year is July-June, data on a number of variables are available on a financial year basis, *i.e.*, April-March and hence, data in this Report are analysed on the basis of the financial year. Where available, data have been updated beyond March 2004. For the purpose of analysis and for providing proper perspectives on policies, reference to past years as also prospective periods, wherever necessary, has been made in this Report.

and a step-up in investment as envisaged in the Tenth Five Year Plan. Key policy initiatives, thus, need to focus on augmenting the flow of resources to the productive sectors of the economy. In this regard, a number of initiatives have been undertaken recently by the Reserve Bank.

1.6 This Section reviews macroeconomic policy settings in 2003-04 against the backdrop of the foregoing developments. The assessment indicates that in the context of the significant turnaround in agricultural production, building the rural infrastructure and credit delivery conduits emerge as the key priorities in the formulation of real sector policies. In the external sector, capital account and foreign exchange transactions were further liberalised in view of the strong balance of payments position. Access to imported inputs was significantly liberalised for accelerating the growth of exports. The review of fiscal policy underscores the need for fiscal consolidation to be carried forward to preserve the benefits in terms of macroeconomic stability and sustained growth. The evaluation of monetary policy reveals the dominant concern associated with managing capital flows, *i.e.*, the recourse to large-scale sterilisation operations in the pursuit of price stability even while ensuring adequate resources for supporting credit demand for investment activity. Going forward, the dilemma posed by these conflicting pulls would become sharper. The Section concludes with a review of financial sector policies and the progress in building the appropriate legal architecture.

REAL SECTOR POLICIES

1.7 Policy initiatives for nurturing growth impulses were framed in the context of the strong recovery in agricultural production and the brightening of the investment climate in manufacturing and services. Several measures were initiated for improving agricultural productivity. Industrial policy initiatives were designed in the context of the multi-faceted globalisation of production systems, especially in terms of technology transfers and development of the physical infrastructure for higher growth.

Agriculture and Allied Activities

1.8 The Government stepped up efforts to improve agricultural productivity through regionally differentiated strategies under the macro management mode of planning and implementation, introduced in October 2000, subsuming all earlier Centrally Sponsored Schemes. In order to mitigate both the yield and price risks, a Farm Insurance Income Scheme (FIIS) was launched on a pilot basis during the *rabi* season 2003-04 in 19 districts across 12 States for wheat and rice, which was subsequently extended to 100 districts during *kharif* 2004. The scheme envisages a minimum guaranteed income computed on the basis of (i) average yield over the last seven years, indemnity level and minimum support price (MSP) of the current year; (ii) premium subsidy of 75 per cent to small and marginal farmers and 50 per cent for others; and (iii) withdrawal of MSP in select crops and districts in which the scheme is launched. The scheme is being implemented by the Agricultural Insurance Company of India Limited (AICL). In order to develop integrated agricultural markets nationwide, facilitate emergence of competitive agricultural markets in the private and the co-operative sectors and to create an environment conducive to massive investments in marketing-related infrastructure, a draft model Act, *viz.,* the State Agricultural Produce Marketing (Development and Regulation) Act, 2003 was framed in September 2003. It provides for establishment of private markets/yards, direct purchase centres, consumer/farmers' markets for direct sale and promotion of public-private partnership in the management and development of agricultural markets. Ten States have initiated legal or administrative action for 'direct marketing' and 'contract farming' arrangements in line with the Model Act. There is a need for all other States and Union Territories to bring the necessary amendments in their legislation on the lines of the Model Act. The establishment of *Kisan* Call Centres and Mass Media Support for Agriculture Extension were taken up in January 2004 with a view to overcoming information asymmetry through information technology. The Ministry of Agriculture is preparing a National Action Plan focusing on measures to be undertaken for increasing agricultural productivity and doubling food production by 2011-12.

Manufacturing and Infrastructure

1.9 Construction of quality infrastructure, initially in 20-25 functional clusters/industrial locations, was announced in January 2004. Implementation of the scheme would be through a Special Purpose Vehicle (SPV) formed by the cluster/industry association, which would carry out the business of developing, operating and maintaining the infrastructure facility created in industrial locations.

1.10 The Union Budget, 2004-05 proposed measures to encourage universal access to telecommunication facilities, facilitate research and development in bio-technology and promote investment in the industrial sector through setting up of an Investment Commission. The National Manufacturing Competitiveness Council proposed in the Union Budget, 2004-05 would help in energising and sustaining the growth of manufacturing industries. The reduction in the peak customs tariff on non-agricultural goods to 20 per cent in the *interim* Budget announced in February 2004 was maintained in the Union Budget 2004-05. Besides, the countervailing duty (CVD) exemption enjoyed by some imported goods where there is no corresponding exemption from excise duty on Indian made goods was removed. Specified raw materials for certain manufacturing items were exempted from excise duty. The customs duty on non-alloy steel was reduced from 15 per cent to 10 per cent, while the excise duty on steel was increased from eight per cent to 12 per cent so that the countervailing duty would also be applicable to imports. The peak customs duty on alloy steel, copper, lead, zinc and base metals was reduced to 15 per cent. The Central Value Added Tax (CENVAT) duty on textiles was abolished and there will be no mandatory excise duty on pure cotton, wool and silk, whether it is fibre, yarn, fabric or garment. There will be a mandatory excise duty on man-made staple fibre and other man-made filament yarn (16 per cent) and polyester filament yarn (24 per cent). The Union Budget, 2004-05 laid emphasis on technology upgradation of small scale industry (SSI) units to enable them to conduct business in a competitive environment and identified 85 items for de-listing from the reserved list of the SSI sector. An Inter-Institutional Group (IIG) will be formed to pool resources on a callable basis towards further development of infrastructure. A sum of Rs.40,000 crore will be made available to ensure speedy conclusion of loan agreements and implementation of infrastructure projects relating to airports, seaports and tourism.

1.11 Efforts were made to sustain the expansion of information technology and telecommunication sectors. The draft report of the Task Force on Power Sector Investments and Reforms (Chairman: Shri N.K. Singh) recommended liberalisation of generation, transmission and distribution. It also made recommendations to facilitate resource mobilisation by various measures such as according priority sector status to the power sector, SLR status to power sector bonds, access to the capital market for central utilities and also proposed wide-ranging fiscal incentives. The Information Technology Taskforce (Chairman: Shri Nandan Nilekani), set up by the Ministry of Power to develop a synergy between IT and the power sector, emphasised the need to adopt a holistic approach towards the standardisation of IT architecture, applications, network, hardware and management which could be customised to the specific requirements of individual utilities. In keeping with the objective of making telecommunication services available in the most efficient and affordable manner, it was decided by the Central Government that merger of licences would be restricted to the same service area.

EXTERNAL SECTOR POLICIES

1.12 External trade and payments policies were framed in the backdrop of the optimism generated by the strengthening of the balance of payments in 2003-04. The EXIM Policy 2002-07 was fine-tuned in January 2004 with a series of trade facilitation measures aimed at consolidation and acceleration of export growth so as to make India a manufacturing hub for producing quality goods and services. These measures focused on simplifying operational procedures and imparting greater transparency with the objective of reducing transaction costs for exporters. The Reserve Bank undertook a measured dismantling of restrictions on foreign exchange transactions with a view to providing an enabling environment for all entities engaged in external transactions. In conformity with this stance, the Exchange Control Department of the Reserve Bank was renamed as the Foreign Exchange Department.

1.13 Under the trade policy measures announced in January 2004, some of the restrictions for import of gold and silver, global positioning system receivers, electrical energy and air guns were removed. Under the Duty Free Replenishment Certificate (DFRC) Scheme, duty free import of fuel was allowed with actual user conditionality to offset the high power costs faced by the manufacturing industry. The procedure for fixation of the “nexus” between import of capital goods and export products under the Export Promotion Capital Goods (EPCG) Scheme was simplified. Imports are allowed on the basis of a Chartered Engineer’s certificate as against the earlier system of examination by an expert committee. Rupee payments received for port handling services were allowed to be reckoned for the discharge of export obligation under the EPCG Scheme. Deemed export benefits were granted for items attracting zero per cent basic customs duty as well as fertiliser and refinery projects spilling over from Eighth and Ninth Plan periods. Measures to boost project exports included (i) enhancement of the equity base of the

Export Credit Guarantee Corporation (ECGC) from Rs.500 crore to Rs.800 crore; (ii) creation of a National Export Insurance Account to enable the ECGC to underwrite high value projects being implemented by Indian companies abroad; and (iii) introduction of a Gold Card Scheme for creditworthy exporters with good track record to enable them to obtain export credit without difficulty. Import of all kinds of capital goods, including office and professional equipment, was allowed under the Duty Free Entitlement Scheme for the benefit of the services sector (including tourism).

1.14 India has played a crucial role in forming important alliances in the World Trade Organization (WTO) negotiations - G-20 on agriculture and G-16 on Singapore Issues (Box I.1). Suggestions made by India to address the developmental concerns of developing countries formed part of the revised framework for negotiations that was adopted by the General Council of the WTO on August 1, 2004.

Management of Foreign Exchange Transactions

1.15 The Reserve Bank continued to move away from micro management of foreign exchange transactions to macro management of flows. At the same time, greater emphasis was laid on transparency, data monitoring, information dissemination and stronger Know Your Customer (KYC) guidelines.

1.16 The Reserve Bank continued to liberalise foreign exchange transactions. Steps were also taken to strengthen risk management systems in banks. Firms engaged in export and import of commodities were allowed to hedge the price risk in international commodity exchanges/markets. Exporters were allowed greater flexibility in seeking regulatory compliance, self write-off and self extension of the due date for export realisation. The threshold limit for GR declaration was revised upwards and procedures for import remittances were simplified.

1.17 The process of liberalisation of the capital account was carried forward during 2003-04 with an accent on facilitating outflows by residents. Resident individuals were permitted to remit an amount of up to US $ 25,000 per calendar year for any current and capital account transaction or a combination of both and to borrow up to US $ 2,50,000 or equivalent from close relatives residing outside India free of interest with a minimum maturity period of one year. Authorised dealers were permitted to allow remittances up to US $ one million per calendar year,

Box I.1

Post-Cancun WTO Consultations

The Fifth Ministerial Meeting of the WTO held at Cancun, Mexico during September 11-14, 2003 was expected to take stock of the progress in ongoing negotiations under the work programme adopted in the Doha Declaration and provide necessary political guidance, including decisions on launching negotiations on the "Singapore Issues". The meeting, however, ended without reaching any agreement in view of sharp differences in the views and positions taken by members on the core agenda issues. The joint Ministerial Statement at the end of the conference noted that more work needed to be done in some key areas to proceed towards the conclusion of the negotiations in fulfillment of the Doha commitments. The post-Cancun consultations focused on four negotiating areas, *viz.*, agriculture, market access for non-agricultural products (NAMA), Singapore issues and cotton.

Agriculture holds the key to progress in future trade negotiations. Of the three "pillars" of agricultural negotiations (export subsidies, domestic support and market access), market access is viewed as the most important issue and a number of alternative formulae have been proposed. Under the "blended" formula jointly put forward by the US and the EU, tariffs would be divided into three groups: duty free, tariffs reduced by a simple average with a minimum reduction per product (the Uruguay Round approach) and tariffs reduced under the "Swiss formula" (a harmonising formula that reduces higher tariffs by greater amounts, simultaneously setting a maximum tariff rate). At the first "agriculture week" after Cancun held during March 22-26, 2004 delegates agreed on the need for allowing developing countries to accord special treatment but differences remained on the conditions that would apply. Subsequently, three negotiating papers from the G-20, G-10 and G-33 were put forward seeking to bridge the differences amongst members. Furthermore, the EU promised to phase out farm export subsidies on the condition that other forms of subsidised export competition were also eliminated. The Framework Agreement adopted by the WTO General Council on August 1, 2004 brought negotiations back on track. The major decisions taken by the General Council included: elimination of all forms of subsidies in agriculture by an "end date"; reduction of all trade-distorting domestic support according to a "tiered formula"; and continuation of the flexibility available to developing countries in providing certain subsidies for export of agricultural products for a reasonable period, after the phasing out of all forms of export subsidies and implementation of all disciplines is completed.

out of balances held in Non-Resident Ordinary (NRO) accounts/sale proceeds of assets, subject to the payment of applicable taxes. The limit of US $ one million per calendar year includes sale proceeds of assets. Sale proceeds of immovable properties which are not acquired through inheritance are eligible for remittances provided the same were held by non-resident Indians (NRIs)/persons of Indian origin (PIOs) for a period of not less than 10 years. In case a property is sold after being held for less than 10 years, remittances could be made if the sale proceeds were held in NRO accounts or eligible investment for the balance period.

1.18 Resident corporates and registered partnership firms were permitted to invest up to 100 per cent of their net worth in overseas Joint Ventures (JV)/Wholly Owned Subsidiaries (WOS) and undertake agricultural activities abroad. Resident entities with overseas direct investments were permitted to hedge the exchange risk.

1.19 Deposit schemes for NRIs underwent major policy-induced changes. Policy measures undertaken in the broader context of managing capital flows included raising of the minimum maturity to one year for Non-Resident External (NRE) rupee deposits, progressive rationalisation of interest rates to close differentials *vis-a-vis* the London Inter-Bank Offered Rate (LIBOR)/SWAP rates and disallowing of non-bank entities from accepting deposits by NRIs.

1.20 Norms for external commercial borrowings (ECBs) were further liberalised in respect of eligibility, end-use restrictions and spreads. The limit for the automatic route was raised to US $ 500 million and the approval process in respect of loans above US $ 500 million was shifted from the Government to the Reserve Bank. Resident corporates were allowed to raise ECBs for overseas direct investment in JV/WOS.

1.21 Foreign institutional investors (FIIs) and NRIs were permitted to trade in exchange traded derivative contracts. Multilateral development banks such as International Finance Corporation (IFC) and the Asian Development Bank, which are specifically permitted by the Government to float rupee bonds in India, were permitted to purchase dated Government securities.

1.22 In order to carry forward the process of liberalisation of the external sector, the Union Budget for 2004-05 proposed to i) raise the sectoral caps for FDI in telecommunications (from 49 per cent to 74 per cent), civil aviation (from 40 per cent to 49 per cent) and insurance (from 26 per cent to 49 per cent); ii) make the procedures for registration and operations simpler and quicker for FIIs; and iii) raise the investment ceiling for FIIs in debt funds from US $ one billion to US $ 1.75 billion. Other proposals included withdrawal of the exemptions on interest earned from a Non-Resident (External) Account and interest paid by banks to a Non-Resident or to a Not-Ordinarily Resident on deposits in foreign currency from tax. These exemptions would cease prospectively from September 1, 2004.

FISCAL POLICY

Central Government

1.23 The fiscal stance for 2003-04 was set by a firm commitment to prudence as reflected in the enactment of the Fiscal Responsibility and Budget Management (FRBM) Act in August 2003. A combination of measures to enhance revenue buoyancy, contain revenue expenditure, cut back capital expenditure and secure higher realisation of disinvestment proceeds resulted in all the key deficit indicators being lower than the budget estimates in 2003-04 for the first time since the initiation of structural reforms.

1.24 Tax reforms were reinforced by modifications to tax proposals announced in January 2004 covering reduction in customs duties and reduction in excise duties on computers and aviation fuel. Modifications in direct taxes included phasing out of filing of income-tax returns for employees drawing salary income up to Rs.1.5 lakh, exemption of pensioners from the purview of the ‘one-by-six’ scheme and expanding computerisation for tax administration.

1.25 The notification of the FRBM Act, 2003 and the FRBM Rules framed under it in July 2004 streamlined the process of the presentation of the Union Budget. The Union Budget, 2004-05 sought to achieve the following objectives, *viz.*, sustained growth rate of 7-8 per cent per annum; universal access to quality basic education and health; gainful employment and investment promotion; minimum assured employment; agriculture and infrastructure development; fiscal consolidation and reform; and higher and more efficient fiscal devolution.

1.26 The Union Budget, 2004-05 proposed to utilise the current favourable conditions to undertake tax reforms for widening the tax base and for reducing the revenue deficit from 3.6 per cent of GDP in 2003-04 to 2.5 per cent of GDP in 2004-05 - more than the annual minimum target of 0.5 per cent set in the FRBM Rules. It also proposed to assist the Reserve Bank in restraining the growth in money supply without damaging the medium/long-term prospects of savings in the economy and without hurting the interests of the poor, the senior citizens and other fixed-income earners. Plan expenditure priorities are proposed to be reoriented and subsidies restructured. An integrated development perspective is proposed to be adopted in areas that are vital to national well-being such as food, water, energy, transport and communication.

Tax Reform

1.27 The Union Budget 2004-05 seeks to expand tax reforms to encompass taxation of services and to facilitate the introduction of the Value Added Tax (VAT). The guiding principles of tax policy, as spelt out in the Fiscal Policy Strategy Statement 2004, aim at widening the tax base by reducing exemptions, incentives and concessions; reducing multiplicity of rates; lowering tax rates; shifting the incidence of tax burden from production to consumption; moving away from excessive reliance on taxes on manufacturing and taxing all value additions including from services; securing neutrality between present and future consumption; securing the neutrality of the tax system to forms of business organisations and sources of finance; and reengineering business processes of tax administration to reduce compliance cost and overcome the culture of tax avoidance and evasion.

1.28 Under direct taxes, measures proposed to provide relief to tax payers include tax rebate for individuals with total income up to Rs.1 lakh; tax exemption to certain sections of tax payers such as widows, children and nominated heirs of personnel of armed forces killed in the course of operational duties; and exemption of contributions to the new ‘defined contribution’ pension scheme. Measures aimed at rationalisation and simplification of the tax regime include tax exemption for all long-term capital gains arising from securities transactions and a flat tax rate of 10 per cent for short-term capital gains from securities transactions; enhancement of withholding tax from 12.5 per cent to 20 per cent for debt-oriented mutual funds on the income distributed to corporate unit holders; dematerialisation of Tax Deducted at Source (TDS) and Tax Collected at Source (TCS) certificates; mandatory filing of TDS/TCS returns in computer media for Government deductors; and subjecting infrastructure capital companies to the Minimum Alternate Tax (MAT). The Union Budget also seeks to plug revenue leakages through a series of measures which include not allowing set-off of business loss against salary income and preventing bonus and dividend stripping. Two new taxes are proposed to be introduced, *viz.*, a transaction tax in equities and a tonnage tax for shipping companies which would allow them to be taxed on notional income, based on the tonnage of the ship.

1.29 On the indirect tax front, the thrust of tax policy is on (i) moderation and stability in tax rates; (ii) increasing revenues from excise duties; (iii) aligning the tariff structure to that of the ASEAN countries; (iv) progressing towards a uniform rate of tax on goods and services; (v) progressing towards integration of tax on goods and services; and (vi) expanding the service tax net. The peak rate of customs duty is sought to be maintained at 20 per cent, while duties for specific industries are proposed to be reduced. Exemptions from excise duties are proposed to be granted for farm equipment, computers, telecom grade optical fibres and cables, raw materials for manufacture of parts of cathode ray tubes, specified capital goods for manufacture of mobile handsets and plasma display panels. Furthermore, measures are proposed to widen the tax base and rationalise rates towards the mean CENVAT rate. The service tax rate is proposed to be raised from eight per cent to 10 per cent along with the addition of 13 new services under the tax net as well as by expanding the scope of existing taxed services and removal of certain exemptions. The Union Budget proposed an education cess of 2 per cent on all taxes, *viz.*, income tax, corporation tax, excise duties, customs duties and service tax. Tax proposals on direct taxes are expected to yield a gain of Rs.2,000 crore. On the indirect taxes side, they are broadly revenue neutral. Tax deduction at source (TDS) and tax collection at source (TCS) are proposed to be extended to more activities. The Union Budget expects to recover arrears both in direct taxes and indirect taxes through a special multi-pronged drive.

Expenditure Policy

1.30 The public expenditure policy inherent in the Union Budget seeks to reorient expenditure allocation towards two major areas - defence and the thrust areas in governance relating to infrastructure and social development. An additional provision of Rs.11, 000 crore has been made for defence capital expenditure. The Union Budget has also made a lump sum provision of Rs.10,000 crore for programmes on Food for Work, *Sarva Shiksha Abhiyan*, mid-day meal scheme, basic health care, railway modernisation and safety, accelerated irrigation benefit programme, drinking water, public investment in agriculture, provision of urban amenities in rural areas (PURA), science and technology and road development. An intensive review of operational aspects of subsidies is proposed to be taken up so as to restructure and target them at the needy sections of the society. A blueprint on subsidies is proposed to be prepared for accomplishing these objectives.

State Governments

1.31 A number of States including Kerala, Punjab, Tamil Nadu and Uttar Pradesh enacted enabling legislation during the year to provide a statutory backing to fiscal reforms. A bill has also been introduced in Maharashtra. A Group comprising State Finance Secretaries of Kerala, Karnataka, Maharashtra, Punjab and Tamil Nadu and a representative from the Central Government was constituted in October 2003 to frame a model bill to facilitate faster adoption of the fiscal rule framework by the remaining State Governments.

1.32 The States have laid emphasis on fiscal rectitude and institutional reforms. On the revenue front, policy initiatives included strengthening of tax efforts and rationalisation of user charges relating to power, water and transport. On the expenditure side, the focus was on containment of revenue expenditure through restrictions on fresh recruitment/creation of new posts and cutbacks in administrative expenditure. Some States initiated measures to introduce a contributory pension scheme for their newly recruited staff. Public Sector Undertaking (PSU) reforms, particularly in the power sector, also assumed critical importance.

1.33 The Central Government supported the States' fiscal reforms by the States' Fiscal Reforms Facility (2000-01 to 2004-05) through which the States draw up a Medium-Term Fiscal Reforms Programme (MTFRP) by setting targets for broad fiscal indicators in the medium-term covering fiscal consolidation, PSU reforms, power sector reforms and budgetary reforms. The process of sub-national reform is, thus, being driven by a unique twin-track strategy blending a co-ordination approach (MTFRP) and an autonomous approach in the form of fiscal responsibility legislation.

1.34 The debt swap scheme (DSS) for the State Governments, put in place in the Union Budget 2003-04, would enable them to prepay their high cost debt to the Centre. All loans from the Centre to the State Governments bearing coupons in excess of 13 per cent are to be swapped with market borrowings and small saving proceeds at prevailing interest rates over a period of three years ending 2004-05. The debt swap scheme would, over a period of time, reduce the pressure on the States' revenue account by way of lower interest payments and thereby on their overall borrowing requirements.

1.35 The Union Budget, 2004-05 proposes to prepare for a partnership between the Centre and the States in moving towards a single national market through the introduction of VAT and dismantling of controls, especially in agriculture. The Centre-State partnership would also seek to reform and restructure the fiscal institutions, which will get a further boost on the basis of the recommendations of the Twelfth Finance Commission. The focus will also be on increasing fiscal discipline, curbing wasteful expenditure and enforcing tax compliance.

MONETARY POLICY FRAMEWORK

1.36 The conduct of monetary policy in 2003-04 was in conformity with the objectives of ensuring adequate liquidity to meet credit growth for investment demand and price stability. The policy stance was reinforced by a 25 basis point cut in the Bank Rate in end-April 2003 and in the cash reserve ratio (CRR) in mid-June, followed by a 50 basis point reduction in the LAF repo rate towards the end of August. Banks took advantage of easy liquidity conditions to cut deposit rates and lending rates. Responding to the Reserve Bank's initiative, banks switched over from tenor-linked prime lending rates (PLRs) to benchmark PLRs (BPLRs). As at end-March 2004, BPLRs were lower by 25-200 basis points than the PLRs which prevailed a year ago.

1.37 Monetary policy had to contend with challenges posed by large capital flows almost throughout the year. Beginning in the second quarter, massive sterilisation operations were conducted through open market sales and LAF repos. The large scale sterilisation necessitated by the relentless expansion in the net foreign assets of the Reserve Bank resulted in repos outstanding under the LAF soaring to over Rs.50,000 crore by March 2004 and large scale open market sales from the stock of Government securities in the Reserve Bank's portfolio. Accordingly, a Market Stabilisation Scheme (MSS) was introduced in April 2004 to strengthen the Reserve Bank's ability to conduct monetary and exchange rate management (Box I.2).

1.38 Against the backdrop of developments in 2003-04, the stance of monetary policy for 2004-05 reflects the priority attached to realising a structural

Box I.2

Market Stabilisation Scheme

In pursuance of the recommendations of the Reserve Bank's Working Group on the Instruments of Sterilisation, a Market Stabilisation Scheme (MSS) was introduced on April 1, 2004 under a Memorandum of Understanding (MoU) between the Government of India and the Reserve Bank. Under the MSS, Treasury Bills and dated securities of the Central Government are issued for conducting sterilisation operations.

The Reserve Bank notifies the amount, tenure and timing of issuances under the MSS under a calendar of issuances. The ceiling on the outstanding obligations of the Government for the year 2004-05 under the MSS has been fixed at Rs.60,000 crore, which is subject to revision through mutual consultation. Treasury Bills/dated securities issued under the MSS by way of auctions have the same features as the existing Treasury Bills/ dated securities. An indicative schedule for the issuance of Treasury Bills/ dated securities under the MSS is being announced on a quarterly basis.

Money raised under the MSS is held by the Government in a separate identifiable cash account maintained and operated by the Reserve Bank. The amount held in this account would be appropriated only for the purpose of redemption and/or buyback of the Treasury Bills and/or dated securities issued under the MSS.

Any increase in the Reserve Bank's net foreign assets (NFA) would, thus, be matched by an accretion in Government balances under the MSS driving down the net Reserve Bank credit to the Government. The consequent decline in reserve money nullifies the monetary impact of the increase in the Reserve Bank's NFA.

The impact on the revenue/fiscal balance of the Government would only be to the extent of the discount on Treasury Bills and coupons on dated securities (net of premium/discount and accrued interest) issued under the MSS. The receipts and payments towards interest and premium/discount under the Scheme would be shown separately in the Union Budget.

acceleration in the growth of the economy and to consolidating the recent gains from reining in inflationary expectations. Barring the emergence of any adverse and unexpected developments, the May 2004 Annual Policy Statement sets out the overall stance of monetary policy as:

- Provision of adequate liquidity to meet credit growth and support investment and export demand in the economy while keeping a very close watch on the movements in the price level.
- Consistent with the above, while continuing with the *status quo*, to pursue an interest rate environment that is conducive to maintaining the momentum of growth and macroeconomic and price stability.

Credit Delivery System

1.39 Several policy initiatives were undertaken to improve the process of credit delivery to agriculture and small and medium enterprises and strengthen the process of micro finance. Public sector banks were advised by the Government in July 2003 to charge interest rates not exceeding 9 per cent per annum on crop loans up to Rs.50,000 with a view to passing on the benefits of declining interest rates to the agricultural sector. Refinance from the National Bank for Agriculture and Rural Development (NABARD) to the district central co-operative banks directly was enabled by amending the NABARD Act, 1981 in September 2003 in order to reduce the transaction costs involved in extending credit facilities to the co-operative sector. Initiatives were also taken for franchising agricultural credit through post offices on a pilot basis in Tamil Nadu.

1.40 Steps were taken by the Government to liberalise the *Laghu Udyami* Credit Card scheme for providing small and medium enterprises easier access to bank credit. The Reserve Bank advised banks regarding enhancement of investment limits in plant and machinery for certain specified SSI units from Rs. one crore to Rs. five crore. Banks were allowed to increase the limit of dispensation of collateral requirement for loans to SSI units.

1.41 In order to increase the quantity and quality of credit flow to the agricultural sector, the Central Government announced a package of measures on June 18, 2004. Incremental agricultural credit by all financial institutions is slated to increase by 30 per cent to about Rs.1,05,000 crore in 2004-05. This would be reinforced by efforts to enhance coverage of institutional credit, with targets in terms of farmers, projects and agri-clinics in each rural and semi-urban branch.

FINANCIAL SECTOR POLICIES

1.42 The Reserve Bank intensified financial sector reforms during 2003-04 with an emphasis on deregulation, technological upgradation, strengthening of prudential standards and pro-active refinement of regulatory and supervisory oversight of the financial system.

1.43 Banks were sensitised to the need to put in place risk management systems and to draw up road maps by end-December 2004 for migration to Basel II. In recognition of the interest rate risks in a rising interest rate scenario, banks were advised to build up the minimum levels of the Investment Fluctuation Reserve (IFR) (5 per cent of investments in “Held for Trading” (HFT) and “Available for Sale” (AFS) categories) by March 2006 instead of the target date of March 2007 set earlier. Foreign currency exposure on account of foreign currency loans above US $ 10 million were required to be governed by a well laid down policy of their boards with regard to hedging of such currency loans. Guidelines on country risk management were expanded to include countries where a bank has an exposure of one per cent or more of its assets effective March 31, 2005.

1.44 The environment for non-performing assets (NPA) management through the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest (SARFAESI) Act of 2002 was considerably strengthened in April 2004 by the Supreme Court, which upheld the right of banks and financial institutions to attach and sell assets of the defaulting companies. The Court also upheld the borrowers’ right to appeal and struck down provisions requiring the defaulting borrower to pre-deposit 75 per cent of the liability.

1.45 Risk-based supervision (RBS) was introduced on a pilot basis for eight banks during 2003-04. The quality of compliance with the guidelines on Know Your Customer (KYC) was inspected in order to assess the adequacy of systems for anti-money laundering/ combating financing of terrorism. The Reserve Bank proposes to issue fresh licenses for urban co-operative banks after a comprehensive policy is put in place, including an appropriate legal and regulatory framework for the sector.

Policies for Financial Markets

1.46 The Reserve Bank persevered with the development of domestic financial markets through introduction of new instruments, tightening of prudential norms for market makers, improvements in payment systems and strengthening of corporate governance practices.

1.47 Prudential limits were stipulated on borrowing/ lending by banks and primary dealers in the call money market. The exposure limit of non-bank entities in the call money market was sharply curtailed with a view to converting the call money market into a pure inter-bank market and to foster the development of the repo market. In the Government securities market, there was a switch to the Delivery *versus* Payment (D*v*P) III mode in which transactions in Government securities could be settled on a net basis. An important development in 2003-04 was the operationalisation of real time gross settlement (RTGS) system which is expected to reduce the settlement risks and cost of financial intermediation significantly. Inter-bank transactions are being put through RTGS by 71 banks. A scheme of Special Electronic Funds Transfer (SEFT) was introduced for the electronic transfer of funds for retail transactions.

1.48 The Securities and Exchange Board of India (SEBI) initiated several policy measures to carry forward the process of development of the capital market and to ensure investor protection. The eligibility norms for unlisted companies to make initial public offers (IPOs) were revised to allow book building. A new clause on the Green Shoe Option (GSO) was added whereby any issuer company making an IPO of equity shares through the book building mechanism could avail of this facility for stabilising the post-listing price of its shares.

1.49 Guidelines prescribed by the SEBI for issue of debt securities on a private placement basis by listed companies require full disclosure, investment grade credit ratings and also issuance and trading in dematerialised form. Norms regarding issuances of derivative instruments such as participatory notes, equity-linked notes or similar instruments against the underlying securities by FIIs or sub-account holders were tightened. Interest rate futures were allowed to be traded on stock exchanges. The SEBI also specified risk containment measures and exposure limits in interest rate derivatives for FIIs and NRIs at US $ 100 million. In order to improve the liquidity in the market, the SEBI allowed corporate brokers with a net worth of at least Rs.3 crore to provide margin trading facility to their clients in the cash segment. A Central Listing Authority (CLA) was established in order to bring about uniformity in the due diligence process in scrutinising listing applications across the stock exchanges. The SEBI shortened the settlement cycle to T+2 with effect from April 1, 2003 with a view to reducing risks in the market and protecting the interest of investors. Straight Through Processing (STP) was made compulsory for all institutional trades with a view to making the trading system efficient and time saving.

1.50 The SEBI took several measures to strengthen corporate governance practices during 2003-04. All compensation paid to non-executive directors is now required to be fixed by the board of directors, subject to approval in a shareholders' general meeting. Company boards are required to lay down the code of conduct for all board members and senior management of a company. Audit committees would review, *inter alia*, the financial statement and draft audit report, with the company management required to justify departures from the accounting standards. The company's Chief Executive Officer (either Executive Chairman or Managing Director) and the Chief Finance Officer (whole-time Finance Director or other person discharging this function) would have to certify, *inter alia*, the balance sheet and profit and loss account and all its schedules and notes on accounts as well as the cash flow statements and the Directors' Report.

1.51 Various measures were initiated by the SEBI to improve the operations and governance of mutual funds. These included setting investment limits in respect of all debt securities, prescribing minimum number of investors in each mutual fund, issuing guidelines for the participation of mutual funds in derivatives trading, determining a uniform cut-off time for applying net asset values (NAVs) and permitting mutual funds to invest in foreign securities up to 10 per cent of the mutual fund's net assets as on January 31 of each year, subject to a maximum exposure of US$ 50 million by each mutual fund.

1.52 The Union Budget, 2004-05 made some important policy announcements relating to the capital market. A Securities Transaction Tax (STT) of 0.15 per cent was proposed on all transactions made on recognised stock exchanges. The short-term capital gains tax was proposed to be reduced to 10 per cent from 30 per cent earlier. The long-term capital gains tax was proposed to be abolished.

1.53 The proposal relating to the STT was revised by the Finance Minister through a statement made in the Parliament on July 21, 2004. The STT of 0.15 per cent was made applicable only to the delivery-based transactions to be shared equally between the buyer and the seller. While the STT on non-delivery based transactions by day traders and arbitrageurs was proposed to be reduced from 0.15 per cent to 0.015 per cent, the same for derivative transactions was reduced to 0.01 per cent. The debt market was fully exempted from the STT.

Changes in the Legal Framework

1.54 Several significant changes/modifications were effected in the legal infrastructure. In December 2003, the *Lok Sabha* passed the Industrial Development Bank (Transfer of Undertaking and Repeal) Bill, 2003 allowing IDBI to take up banking business. The Sick Industrial Companies (Special Provisions) Repeal Bill, 2001 enabling dissolution of (a) the Board for Industrial and Financial Reconstruction (BIFR) and (b) the Appellate Authority for Industrial and Financial Reconstruction (AAIFR) was also passed in December 2003 by the *Lok Sabha*. Some other legislations passed during the year were (i) the Fiscal Responsibility and Budget Management Act; (ii) NABARD (Amendment) Act, 2003 which allows NABARD to finance district central co-operative banks (DCCBs) directly; and (iii) the Electricity Act, 2003.

Outlook

1.55 The year 2003-04 was marked by an acceleration of growth and all round macroeconomic consolidation. Although a fuller assessment of the impact of the monsoon on the growth prospects for 2004-05 is difficult at the current juncture, the medium-term outlook remains favourable. With the deepening of the industrial recovery and sustained growth of the services sector, the Indian economy is set to build upon the robust performance recorded in 2003-04. Adequate stocks of foodgrains and foreign exchange reserves would provide a sufficient cushion to the economy against possible adverse developments.

II THE REAL ECONOMY

MACROECONOMIC SCENE

2.1 India recorded one of the highest growth rates in the world in 2003-04, second only to China among the emerging market economies. According to the *World Development Indicators 2004*, India became the fourth largest economy in terms of purchasing power parity, after the US, China and Japan. This robust economic performance was particularly noteworthy in an environment marked by hesitant global recovery, heightening of geo-political tensions during the year, volatility in international crude oil prices and large asset price movements in international financial markets engendered by abundant liquidity. Domestic developments – largely immune to the global business cycle – powered a surge in real GDP growth to 8.2 per cent – the highest in 15 years (Table 2.1). An agricultural rebound, typical of a post-drought supply response of the Indian economy, played a key role in the resurgence of growth. Activity also firmed up in a wide range of manufacturing and services sectors. Trade, hotels, restaurants, transport, storage and communication surpassed trend growth. Capital goods production also continued to surge. Merchandise exports weathered pressures of the rupee's appreciation against the US dollar, posting a growth of above 20 per cent in US dollar terms. Despite the widening trade deficit, symbiotic of the growth resurgence, buoyant software exports and remittances enabled a current account surplus in the balance of payments for the third consecutive year. This was accompanied by a surge in capital inflows. In spite of substantial policy-driven outflows, foreign exchange reserves rose to an unprecedented level.

2.2 A review of macroeconomic performance in 2003-04 reveals that weather conditions continue to remain a key influence on agricultural production. This was underscored by the role of the normal monsoon in aiding the sharp recovery in agricultural output in 2003-04. Agricultural performance will continue to determine the fluctuations of overall economic activity around its trend. In this regard, water conservation by alternative

Table 2.1: Growth Rates of Real GDP

(Per cent)

Sector	2003-04#	2002-03*	1992-93 to 2001-02 (Average)	2003-04 Q1	2003-04 Q2	2003-04 Q3	2003-04 Q4	2002-03 Q1	2002-03 Q2	2002-03 Q3	2002-03 Q4
1	2	3	4	5	6	7	8	9	10	11	12
1. Agriculture and Allied Activities	**9.1 (22.1)**	**-5.2 (22.0)**	**3.4 (27.5)**	**0.1**	**6.8**	**16.5**	**10.5**	**0.6**	**-2.9**	**-9.8**	**-6.3**
1.1 Agriculture	n.a.	-6.0	3.5								
2. Industry	**6.8 (21.7)**	**6.2 (22.0)**	**6.3 (22.0)**	**6.0**	**6.3**	**6.8**	**7.9**	**4.8**	**6.7**	**6.7**	**6.7**
2.1 Manufacturing	7.3	6.2	6.8	6.6	7.4	7.5	7.6	4.0	6.7	6.9	7.3
2.2 Mining and Quarrying	4.4	8.8	3.9	2.3	2.0	3.6	9.0	11.8	10.1	7.6	6.3
2.3 Electricity, Gas and Water Supply	5.5	3.8	5.6	4.8	2.9	4.8	9.5	4.3	3.9	4.8	2.2
3. Services	**8.5 (56.2)**	**7.2 (56.0)**	**7.5 (50.5)**	**7.2**	**10.0**	**9.1**	**7.6**	**7.2**	**7.9**	**6.8**	**6.8**
3.1 Trade, Hotels, Restaurants, Transport, Storage and Communication	11.2	7.0	8.4	7.3	9.9	13.3	13.8	6.4	7.4	6.5	7.7
3.2 Financing, Insurance, Real Estate and Business Services	6.8	8.8	7.8	5.7	6.4	6.5	8.5	9.6	9.8	8.6	7.5
3.3 Community, Social and Personal Services	6.0	5.8	7.1	9.4	15.2	5.3	-3.1	6.2	6.4	5.6	5.1
3.4 Construction	6.2	7.3	5.2	5.9	6.4	4.8	7.6	7.1	9.5	7.4	5.5
4. Real GDP at Factor Cost	**8.2 (100.0)**	**4.0 (100.0)**	**6.1 (100.0)**	**5.3**	**8.6**	**10.5**	**8.2**	**5.1**	**5.5**	**2.0**	**3.7**

: Revised Estimates. * : Quick Estimates. n.a.: Not available.

Notes : 1. Figures in parentheses denote shares in real GDP.
2. Q1: First Quarter (April - June); Q2: Second Quarter (July-September); Q3: Third Quarter (October-December); and Q4: Fourth Quarter (January-March).

Source: Central Statistical Organisation.

methods such as rainwater harvesting and watershed development, expansion in irrigated crop area, provision of adequate supply of quality farm power, arresting the stagnation in crop yields, initiating institutional reforms to energise the flow of rural credit and judicious management of foodstocks should be the immediate priorities in the weather-proofing of agriculture with a view to dampening the volatility of aggregate supply.

2.3 An assessment of industrial performance indicates an investment climate with growing business confidence. Generating this optimism is continued robust financial performance of the corporate sector. Manufacturing output recorded a steady improvement and was joined by a turnaround in electricity generation towards the close of the year. External demand embodied in export sales turned out to be a key driver of industrial activity; in certain industries such as steel, exports were an expression of rising international competitiveness. The industrial outlook was considerably strengthened by the expansion in capital goods production and in capacity utilisation. Another positive development which augurs well for the future is the framing of the National Electricity Policy. Diffusion of growth to basic and consumer goods industries as well as the infrastructure sector will lay the foundations of a solid and sustained acceleration in industrial growth.

2.4 New growth areas are emerging in the services sector which remained the principal engine of growth for the Indian economy in 2003-04. Alongside the new economy services, the robust growth recorded in activities such as trade, hotels, restaurants, transport and communication highlights the emerging avenues for the financial sector to ‘cash in’ on high growth opportunities.

AGGREGATE SUPPLY

2.5 The Indian economy broke out of a low real GDP growth trend of 3.5 per cent over the period 1950-1980 to average 5.8 per cent in the 1980s before being stalled by the external payments crisis in 1990-91. Structural reforms enabled the economy to achieve an average growth of 6.3 per cent during the period 1992-93 to 1999-2000 but the pace was uneven and dominated by cyclical influences. A combination of cyclical and structural factors slowed down real GDP growth to 5.6 per cent during the four-year period 2000-01 through 2003-04 in spite of the high growth in 2003-04 (Appendix Table II.1). Sectoral patterns show that real GDP originating in both ‘agriculture and allied activities’ and industry followed similar cycles. GDP in ‘agriculture and allied activities’ recovered from a low of 2.1 per cent during 1950-80 to 4.4 per cent in the 1980s but decelerated thereafter to 3.5 per cent during 1992-93 to 1999-2000 and further to 2.6 per cent during the four-year period from 2000-01 through 2003-04. GDP originating in industry accelerated from 5.5 per cent during 1950-80 to 7.4 per cent in the 1980s but fell to 6.7 per cent during the period from 1992-93 to 1999-2000 and further to 5.8 per cent during the four-year period from 2000-01 through 2003-04. Services, on the other hand, anchored the economy, exhibiting a steady acceleration of growth from 4.5 per cent during 1950-80 to 6.4 per cent in the 1980s and further to over 7.9 per cent in the 1990s before decelerating to 6.9 per cent during the four-year period from 2000-01 through 2003-04. A reappraisal of these trends warrants a pragmatic assessment of the growth path for the Indian economy over the medium term (Box II.1).

Agriculture

2.6 Real GDP originating in ‘agriculture and allied activities’ is estimated to have recorded a growth of 9.1 per cent in 2003-04 - the highest in seven years. This resurgence was distinctly similar to the post-drought rebound in 1988-89. With rainfall above the Long Period Average (LPA) in July 2003, the main sowing month of the *kharif* season, real GDP growth in ‘agriculture and allied activities’ surged in the second quarter and gathered further momentum over the rest of the year as *rabi* output also turned out to be satisfactory (Appendix Tables II.2 and II.3). The index of agricultural production rose by 19.6 per cent, a 14-year record. Foodgrains production recouped lost ground and returned closer to the pre-drought (2001-02) level. In the case of pulses, the production level reached an all-time high. Rice production rose by over 19 per cent, compensating for the loss of output in 2002-03 and supporting a vigorous export thrust, particularly in the non-basmati category. Oilseeds production scaled a new peak (over 25 million tonnes), led by groundnut and soyabean (Table 2.2).

2.7 The recent gains in agricultural performance have catalysed a metamorphosis from the conditions of food shortage in the 1960s and the 1970s to one of self sufficiency and beyond. There has been a radical transformation from a reliance on foodgrains aid to a position of comfortable foodstocks and exports. Today, India is a world leader in the production of a number of agricultural crops. It is the world’s largest producer of pulses and tea, and the second largest producer of rice, wheat, groundnut, sugarcane, onion, raw tobacco, jute and fruits and vegetables. India also ranks first in terms of livestock production (cattle and buffaloes) and is a leading producer of eggs and meat (Table 2.3).

Box II.1
What Does it Take to Sustain High Growth?

The impressive growth performance of 2003-04 has renewed the quest for a sustainable trajectory of high growth for India. Structural reforms undertaken since the early 1990s have imparted resilience to the Indian economy. Secular trends and studies thereof suggest that the step-up in the speed of growth over the last 25 years is associated with a reduction in the variability of output. Empirical studies in growth accounting frameworks project India's potential output growth at close to seven per cent between 2005-2025.

Risks to the achievement of this potential on a sustainable basis are the persistence of high levels of fiscal deficit, slowing down of saving and investment rates, the upward movement in the incremental capital output ratio (ICOR) and low labour participation rates despite rising levels of education. A recent study indicates that a 10 percentage point increase in the participation rate over the next 20 years could be expected to add another 0.3-0.4 percentage point to growth rates.

Capital accumulation and labour participation are only necessary conditions for growth. They have to be supported by stable macroeconomic policies, productivity improvements, development of human resources as well as the social and physical infrastructure. The key question in the Indian context is one of making appropriate choices, given limited resources and other constraints. In some sense, the issue of trade-off needs to be addressed. The kind of growth that would have a tangible impact on poverty reduction and environmental degradation would need policy action far beyond that of market liberalisation. Finally, the sustainability of high growth hinges on continuing systemic reforms, especially in agriculture, industry, external trade, labour market, bankruptcy and legal areas, and public administration.

References

1. Mohan, R. (2002), *Facets of the Indian Economy* : *The NCAER Golden Jubilee Lectures* (ed.), Oxford University Press, New Delhi.
2. Panagariya, A. (2004), "India in the 1980s and 1990s: A Triumph of Reforms", *IMF Working Paper No. 04/43*.
3. Rodrik, D. and A. Subramanian, (2004), "Why India Can Grow at 7 Per Cent a Year or More: Projections and Reflections", *Economic and Political Weekly*, April 17.
4. Virmani, A. (2004), "India's Economic Growth: From Socialist Rate of Growth to Bharatiya Rate of Growth", *ICRIER Working Paper No. 122*.

2.8 India has one of the largest livestock population in the world and has become the world's largest producer of milk. Several measures initiated by the Government to increase the productivity of livestock have resulted in a significant increase in the milk production to the level of around 86.4 million tonnes in 2002-03 as compared with 17 million tonnes in 1950-51. The contribution of livestock in the total employment is also gaining importance with its share in the total employment going up from around 3 per cent in 1993-94 to around 5 per cent in 1999-2000. The livestock and fishery sector contributed 5.4 per cent and 1.1 per cent to GDP, respectively, during 2002-03. India is the sixth largest producer of fish in the world (*Economic Suvey 2003-04*, Government of India). The production of fisheries increased sharply from 0.7 million tonnes in 1950-51 to 6.2 million tonnes in 2002-03. Besides being a source of nutritious food, fisheries contribute significantly to generation of income and employment.

Table 2.2: Agricultural Production

Crop	2003-04 #	2002-03	2001-02
1	2	3	4
1. Growth Rate (Per cent)##			
All Crops	**19.6**	**-15.2**	**7.6**
a. Foodgrains	21.8	-18.5	8.8
b. Non-foodgrains	16.3	-10.1	5.9
2. Production (Million Tonnes)			
a. Foodgrains	**212.1**	**174.2**	**212.9**
i. Rice	87.0	72.7	93.3
ii. Wheat	72.1	65.1	72.8
iii. Coarse Cereals	37.8	25.3	33.4
iv. Pulses	15.2	11.1	13.4
b. Non-foodgrains			
i. Oilseeds++	25.1	15.1	20.7
ii. Sugarcane	236.2	281.6	297.3
iii. Cotton@	13.8	8.7	10.0
iv. Jute and Mesta+	11.2	11.4	11.7
v. Tea*	857.1	826.2	853.9
vi. Coffee*	270.5	275.3	300.8

\# : Fourth Advance Estimate as on August 5, 2004.
\## : Based on Index of Agricultural Production with base triennium ending 1981-82 = 100.
+ + : For nine oilseeds out of eleven in all.
+ : Million bales of 180 kg. each.
@ : Million bales of 170 kg. each.
* : Million kilograms and data for tea on a calendar year basis.
Source : Ministry of Agriculture, Government of India.

2.9 Physical indicators of India's agricultural development present a mixed picture. India has the second largest share in global arable land, next only to the US. It holds the largest share in the world's total irrigated area. India ranks fourth in the world in tractor use, illustrating the synergies between agriculture and industry. Although there has been satisfactory progress in agricultural mechanisation in India, the availability of tractors in the country continues to be low (94 per 100 square kilometre of arable land) as compared with Malaysia (239 per 100 square kilometre of arable land) and Thailand (147 per 100 square kilometre of arable land) during 1999-2001. The consumption of chemical

Table 2.3: India's Position in World Agriculture

Item	India: Share in World (%)	India: Rank	Next to
1	2	3	4
Area			
Land Area	2.3	Seventh	Russian Federation, Canada, China, US, Brazil, Australia,
Arable Land	11.8	Second	US
Irrigated Area	21.5	First	
Crop Production			
Wheat	12.8	Second	China
Rice (Paddy)	22.4	Second	China
Total Pulses	23.6	First	
Oilseeds			
Groundnut	17.1	Second	China
Fruits & Vegetables			
Vegetables & Melons	9.2	Second	China
Onion (Dry)	10.4	Second	China
Commercial Crops			
Sugarcane	24.6	Second	Brazil
Tea	25.1	First	
Jute & Jute like Fibres	43.3	Second	Bangladesh
Tobacco Leaves	10.0	Second	China
Livestock			
Cattle	16.2	First	
Buffaloes	57.0	First	
Animal Products			
Eggs Total	n.a.	Fifth	US, Japan, Russian Federation, China
Total Meat	n.a.	Seventh	China, US, Brazil, France, Germany, Spain

n.a. : Not available.

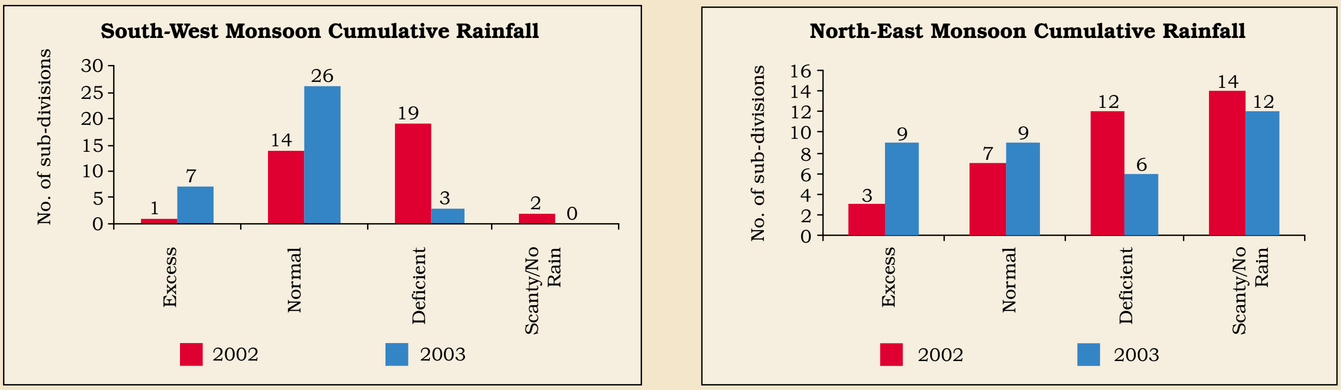
Source: *Agricultural Statistics at a Glance*, 2003, Ministry of Agriculture, Government of India.

fertilisers (nitrogenous, phosphatic and potassic) in Indian agriculture increased from 125.5 lakh tonnes in 1990-91 to 173.6 lakh tonnes in 2001-02. Electricity consumption in agriculture moved up by 68.4 per cent during the period 1990-91 to 2000-01. Although agricultural inputs like seeds, fertilisers and pesticides were available adequately during 2003-04, pest attacks were observed on sugarcane grown in Maharashtra, Karnataka and some pockets of Uttar Pradesh and Uttaranchal; rice in Orissa; pulses in Gujarat; soyabean in Madhya Pradesh; and coconut in Kerala.

2.10 Notwithstanding the progress made since the 1980s, Indian agriculture continues to depend significantly on the monsoon. This is evident, yet again, from the alternating experiences of poor monsoon and drought in 2002-03 and normal monsoon and strong recovery of production in 2003-04. Rainfall was also spatially well distributed during 2003-04. The cumulative rainfall during the South-West monsoon (June 1 to September 30, 2003) was two per cent above the Long Period Average (LPA) with 33 out of 36 meteorological sub-divisions receiving normal/excess rainfall (Chart II.1). Only north and south interior Karnataka and Kerala received deficient rains. Rainfall in the sowing months of June and July 2003 was eight per cent and six per cent above the LPA, respectively. The North-East monsoon was also normal with the cumulative rainfall at nine per cent above the LPA. The total live water storage in the major reservoirs at the end of the monsoon season (as on December 26, 2003) was about 47 per cent of the Full Reservoir Level (FRL) and 122 per cent of the preceding year's level.

2.11 An area of growing concern has been the continued incidence of localised droughts even in good monsoon years. Five out of 36 meteorological sub-divisions in North India suffered from severe drought

Chart II.1: Rainfall Conditions



consecutively for the last five years during the North-East monsoon season. Similarly, several sub-divisions in the Western and Southern regions were affected by localised droughts consecutively in at least two of the last five years (Table 2.4). Droughts in Maharashtra, Karnataka and Uttar Pradesh have adversely affected sugarcane production in recent years. These localised droughts have also affected the production of coarse cereals, pulses and cotton, although it is not fully manifested at the national level. Of the 267 meteorological districts affected by droughts during the South West Monsoon of 2003, 62 meteorological districts were mainly affected in the preceding year as well. These areas were spread across Karnataka (16 districts), Tamil Nadu (9 districts), Kerala (7 districts), Punjab (5 districts) and Maharashtra (4 districts). Another area of concern has been the growing exploitation of national forest resources. Intensified shifting cultivation, indiscriminate removal of timber, fuel wood, fodder and other forest produce, forest fire and encroachment have led to forest degradation and deforestation. According to the Tenth Five Year Plan, forests meet nearly 40 per cent of the country's energy needs and 30 per cent of the fodder needs. It is estimated that about 270 million tonnes of fuel wood and 280 million tonnes of fodder are removed from forests annually. Forests are consistently and

Table 2.4: Localised Droughts in India

(Percentage deviation from normal)

Sub-division with deficient/ scanty rainfall	2003		2002		2001		2000		1999		1998		1997	
	SW	NE	SW	NE	SW	NE	SW	NE	SW	NE	SW	NE	SW	NE
1	2	3	4	5	6	7	8	9	10	11	12	13	14	15
Andaman and Nicobar			-24		-25		-31	-21	-29	-24				-30
Arunachal Pradesh			-22	-46	-29			-24						-26
Assam and Meghalaya				-52	-21			-46						-54
Nagaland, Manipur				-55								-30		-57
Sub-Himalayan WB and Sikkim #				-75				-44						-49
Gangetic West Bengal				-23				-47						-38
Orissa				-44				-76			-25			
Jharkhand								-72						
Bihar				-53				-84						
East Uttar Pradesh		-21	-24	-65				-98						
West Uttar Pradesh		-55		-67		-56		-99						
Uttaranchal		-60		-67		-85		-92		-26				
Haryana, Chandigarh and Delhi		-48	-36	-52		-60		-97	-25	-78				
Punjab		-68	-36	-76		-70		-95		-93				
Himachal Pradesh		-66	-20	-83		-53		-88		-82				
Jammu and Kashmir				-75		-44		-68		-52		-60		
West Rajasthan		-94	-71	-41		-21	-25	-82	-24					
East Rajasthan		-93	-60	-81		-42	-30	-96						
West Madhya Pradesh		-90	-22	-64	-20		-35	-94						
East Madhya Pradesh		-55					-45	-96*			-25			
Gujarat Region, DDNH #		-91	-24	-99			-31	-76	-24					-52
Saurashtra and Kutch		-85	-25	-95		-44	-44	-91	-58					-93
Konkan and Goa		-71		-69	-21	-40		-20						
Madhya Maharashtra		-71		-70				-23						
Vidarbha		-57		-47				-89					-22	
Marathawada		-86		-66				-50					-32	
Chhattisgarh				-48										
Coastal Andhra Pradesh			-26	-31				-57		-25				
Telangana			-23					-73		-47			-27	
Rayalseema			-33							-25				
Tamil Nadu and Pondicherry			-45			-21		-28	-36					
Coastal Karnataka		-24	-30					-27						
North Interior Karnataka	-35	-23	-31											
South Interior Karnataka	-26		-44											
Kerala	-32		-35					-27	-25					
Lakshadweep			-45	-24		-33		-37						

* : including Chhattisgarh. SW : South West Monsoon. NE : North East Monsoon.
# : DDNH - Daman, Dadra and Nagar Haveli; WB - West Bengal.
Note : Normal : +19 per cent to -19 per cent; Deficient : - 20 per cent to - 59 per cent; Scanty: - 60 per cent or less; No Rain : less than - 99 per cent.
Source : India Meteorological Department.

seriously undervalued in economic and social terms. It is hoped that the future land-use policy would take into account these costs appropriately.

2.12 The crop yields have shown an unstable trend in recent years. Although the yield of foodgrains showed significant gains from 710 kg/hectare in 1960-61 to 1704 kg/ hectare in 1999-2000, it fluctuated mainly on account of changes in the yield of rice. The yield of pulses was low during the entire period from 1960-61 to 2002-03. In the case of commercial crops, the yield of oilseeds, which improved significantly during the 1980s and the 1990s, fluctuated in recent years. Sugarcane yields have also been declining in recent years, after consistently improving during the four decades since the 1960s. The yield of cotton, which more than doubled from 125 kg/ hectare in 1960-61 to 265 kg/hectare in 1996-97, has declined thereafter (Chart II.2).

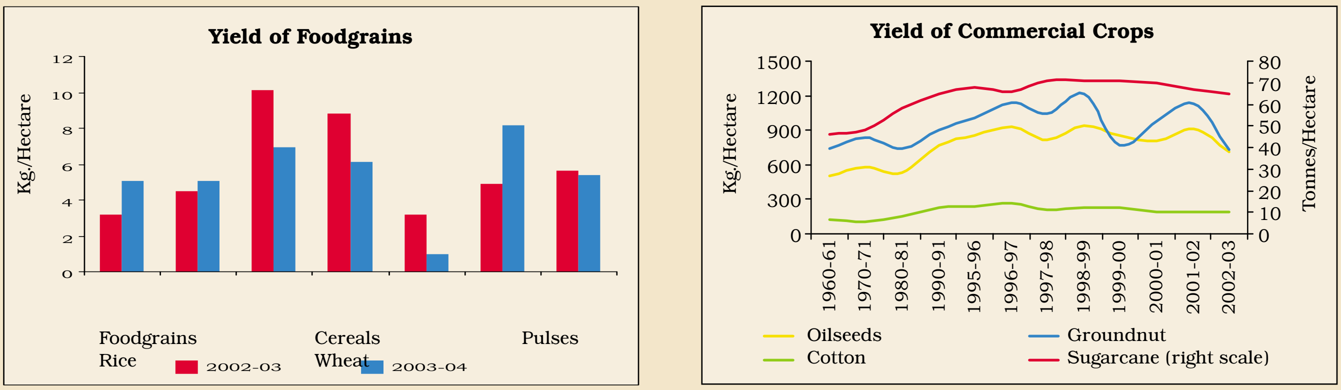
2.13 Stabilisation and augmentation of agricultural yield assume critical importance, given the limited scope for increasing area under cultivation of various crops. Furthermore, there has been a decline in land-holding size, increase in costs of production and depletion of ground water. Increase in production would, therefore, be possible mainly from improvements in productivity from the existing cultivated area through use of location-specific high-yielding varieties of seeds, balanced fertiliser doses along with bio-fertilisers/ organic manures. Upgradation of technology and timely supply of all inputs also assume equal importance. There is also an urgent need to increase the availability of farm power to boost productivity. Another thrust area should be the promotion of organic farming to tap the export potential of organic products.

2.14 Slowdown of investment in agriculture has impacted the pace and pattern of technological change. During the ten-year period spanning from 1993-94 to 2002-03, the ratio of gross capital formation in agriculture to real GDP originating in agriculture increased only by one percentage point from 6.1 per cent to 7.1 per cent. This was mainly on account of the share of the public sector in gross capital formation in agriculture which declined from 33 per cent in 1993-94 to 24.2 per cent in 2000-01. Decelerating public sector investment in agriculture, which goes primarily towards major irrigation projects, has also impeded adequate private sector investment in critical areas. The Committee on Capital Formation in Agriculture (2003) (Chairman: Prof. B.B. Bhattacharya) had noted that the lagging share of agriculture in aggregate capital formation relative to its share in real GDP raises a strong case for increasing the capital formation in agriculture commensurate with its share in GDP. The gross capital formation in allied activities such as fishing has improved in the recent past. The ratio of gross capital formation in fishing as a percentage of real GDP originating from it increased sharply from 14.4 per cent in 1993-94 to 22.3 per cent in 2002-03. The ratio in the case of forestry and logging, however, declined from 4.1 per cent to 2.8 per cent during the same period.

Agricultural Credit

2.15 The formal institutional structure for agricultural credit in India has evolved largely due to the Government intervention over the years (Box II.2). There has been some increase in both the outreach and flow of credit to the agricultural sector over the years. The share of agricultural bank credit in GDP originating in agriculture, which rose marginally from 10.3 per cent in 1993-94 to 10.8 per cent in 1999-2000, moved up sharply to 16.7 per cent in 2002-03. However, some problems continue to affect the flow of credit to agriculture. The credit-deposit (C-D) ratio of the rural branches of scheduled commercial banks declined from 49 per cent in 1995 to 42 per cent in 2002. Another disconcerting feature has been a decline in the proportion of medium/long-term

Chart II.2 : Yield of Foodgrains and Commercial Crops



Box II.2
Institutional Changes in Allocating Agricultural Credit

The evolution of the formal institutional structure for agricultural credit in India has been shaped largely by policy interventions over the years. A three-pronged strategy was adopted for developing institutional services for agricultural credit, *viz.*, expansion of institutional structure, directed lending and concessional credit. The institutional process of credit to agriculture goes back to the 1870s when Government provided credit to farmers during the drought years. The institutional disbursement of rural credit on a regular basis by the co-operative institutions commenced after the enactment of the Co-operative Societies Act in 1904. The Reserve Bank has been closely involved in rural credit and banking by virtue of the provisions of Section 54 of the RBI Act. A major initiative in pursuance of this mandate was taken when an All India Rural Credit Survey was initiated in 1951. The Committee set up for the purpose recommended one strong, integrated, state partnered commercial banking institution to stimulate banking development in general and rural credit in particular. Keeping this in view, the Imperial Bank was nationalised and renamed as the State Bank of India on July 1, 1955. The Reserve Bank played an active role in building the institutional network for agricultural credit by setting up the Agriculture Refinance Corporation (ARC) in 1963 and establishing the National Agricultural Credit (Long-Term Operations) Fund and the National Agricultural Credit (Stabilisation) Fund for the purpose of making long and medium term loans to the rural economy. Social control and the subsequent nationalisation of banks in 1969 and 1980 provided momentum to the efforts aimed at broad–basing the institutional arrangements for agriculture credit delivery. Regional Rural Banks (RRBs) set up in 1975 to usher in an institutional framework combined local feel and familiarity of rural problems (advantages of co-operatives) with professionalism and a large resource base (advantages of commercial banks). The ARC was renamed as Agriculture Refinance and Development Corporation (ARDC) in 1975 in order to re-orient this institution for striving for agricultural development. The National Bank for Agriculture and Rural Development (NABARD) was set up in 1982 from the erstwhile ARDC and Agricultural Credit Department of the Reserve Bank to pay focused attention to rural/agricultural credit.

Co-terminus with this multi-agency approach to rural credit, policy intervention in credit allocation to agriculture was considered necessary in the wake of several weaknesses, *viz.*, lack of collateral, high transaction cost and increased risk perception. The concept of priority sector evolved whereby it was made mandatory for banks to extend a certain portion of net bank credit (one-third from March 1979 and 40 per cent from March 1985) to preferred sections of society. Within the priority sector, a sub-target (15 per cent from March 1985 and 18 per cent from March 1990) was stipulated for agriculture and allied activities. The Lead Bank Scheme was introduced in 1969 and the main instrumentality used for the purpose of allocating credit to agriculture was directed lending at concessional rates of interest. The Differential Rate of Interest (DRI) Scheme was put in place in 1972 for providing small loans at a highly concessional rate of four per cent per annum. The Service Area Approach introduced in 1989 imparted development orientation to agricultural lending. To further supplement the institutional mechanism, a concept of local area bank was introduced in 1996-97.

In the 1990s, emphasis was laid on the process of consolidation with a view to improving profitability and viability of institutions. Two major innovations in the field of rural credit delivery in the 1990s were the successful introduction and wider implementation of *Kisan* Credit Cards (KCCs) and the extension of micro finance in the form of Self-Help Group (SHG)-Bank Linkage programmes. The establishment of the Rural Infrastructure Development Fund (RIDF) during 1995-96 with the NABARD marked another important step in the field of rural credit. Domestic scheduled commercial banks are required to contribute to the RIDF to the extent of shortfall in agricultural lending under priority sector target for on-lending for developing rural infrastructure.

References

1. Mohan, R. (2004), *Agricultural Credit in India: Status, Issues and Future Agenda*, Inaugural Address at the Annual Conference of Indian Society of Agricultural Marketing, Hyderabad, February (*mimeo*).
2. Rangarajan, C. (1996), *Rural India: the Role of Credit*, The First Ravi Matthai Memorial Lecture organised by the Academy of Human Resources Development at the Indian Institute of Management, Ahmedabad, March, *RBI Bulletin*, May.
3. Reddy, Y.V. (2000), "Future of Rural Banking", *Address at Prof. G. Rama Reddy's Third Endowment Lecture*, Hyderabad, *RBI Bulletin*, January.
4. _____ (2001), "Indian Agriculture and Reforms: Concerns, Issues and Agenda", Address at the Conference of the Indian Society of Agricultural Marketing at Vizag, *RBI Bulletin,* May.

loans in direct finance to agriculture and allied activities (from over 41 per cent in 1990-91 to about 31 per cent in 2000-01). The share of small and marginal farmers in direct finance fell from 54.5 per cent in 1990-91 to around 51 per cent in 2000-01, thereby enhancing their vulnerability. There have been wide disparities in the flow of credit across regions. Prevalence of cumbersome legal systems/tenancy laws continue to impede the flow of credit to agriculture. Several initiatives have been taken in recent years to address these concerns and to improve the agricultural credit delivery mechanism. These, *inter alia*, include simplifying procedures, encouraging decentralised decision-making and encouraging self-help groups under micro finance programmes.

Food Management: Procurement, Offtake and Stocks

2.16 The stock of foodgrains with the Food Corporation of India (FCI) and the State agencies declined sharply from the peak level of 64.8 million tonnes on June 1, 2002 to 39.8 million tonnes on June 1, 2003 partly due to drought relief measures and partly due to policy initiatives to liquidate the surplus food stocks. As 2002-03 was a drought year, procurement of foodgrains declined by 3.3 million tonnes, while offtake increased by 18.3 million tonnes. The Central Government allocated 8.3 million tonnes of foodgrains to drought affected States. Of this, 4.7 million tonnes were lifted during 2002-03. Lower procurement and continued offtake during 2003-04 brought down the stocks of foodgrains further by March 1, 2004 (Table 2.5 and Appendix Table II.4). The offtake during 2003-04, a normal monsoon year, remained closer to the offtake during the drought year of 2002-03, thereby reflecting continued policy initiatives to economise on wastage cost, storage cost and interest cost on food credit. Wheat procurement declined by 8 per cent during the *rabi* marketing season of 2002-03 and further by 17 per cent during the *rabi* marketing season of 2003-04. Paddy procurement declined by 26 per cent during the *kharif* marketing season of 2002-03. The offtake of foodgrains during 2003-04 was higher by 13 per cent in the Targeted Public Distribution System (TPDS) and 18 per cent in Other Welfare Schemes (OWS), while it was lower by 36 per cent under Open Market Sales (OMS). The procurement of paddy during the current *kharif* marketing season so far (October 1, 2003 to July 26, 2004) was higher by 39.8 per cent over 2002-03. The procurement of wheat during the *rabi* marketing season so far (April 1 to July 26, 2004) was also higher by more than 6 per cent over the corresponding period of the previous year. The offtake of foodgrains during the current year so far (April 1 to June 31, 2004) was, however, lower by around 40 per cent than the comparable period of the previous year. The foodgrains stocks at 30.6 million tonnes on July 1, 2004 are still above the stipulated quarterly norm of 24.3 million tonnes as on July 1.

Industry

2.17 Real GDP growth originating in industry gathered strength in every successive quarter of 2003-04. Industrial production steadily accelerated to reach a peak of 8.3 per cent in February 2004 (the highest since April 2000) before tapering off to 8.1 per cent in March 2004. The rise in the index of industrial production (IIP) in 2003-04 was the highest after 1995-96. The improvement in industrial performance was enabled by a rebound in rural demand, rising exports across a spectrum of industries, increased consumer durables demand fuelled by low interest rates and reduction in excise duties on a host of intermediate inputs. Continued buoyancy in capital goods production augurs well for the investment climate. Business

Table 2.5: Management of Food Stocks

(Million tonnes)

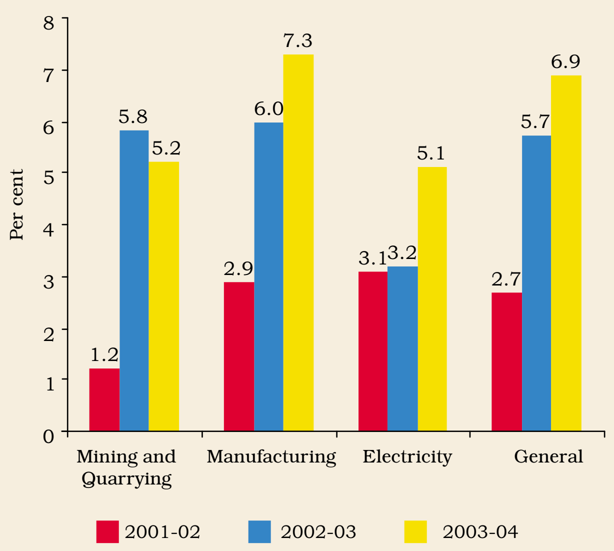
Month	Opening Stock of Foodgrains	Foodgrains Procurement	Foodgrains offtake				Closing Stock	Norm
			PDS	OWS	OMS – Domestic	Exports		
1	2	3	4	5	6	7	8	9
2003								
April	32.8	13.1	1.6	0.9	0.2	0.8	41.3	15.8
May	41.3	3.7	2.0	1.6	0.1	0.9	39.8	
June	39.8	1.0	1.5	2.5	0.2	1.3	35.2	
July	35.2	0.2	2.2	1.4	0.1	2.2	30.5	24.3
August	30.5	0.2	1.8	0.8	0.1	0.9	27.9	
September	27.9	0.2	2.2	1.0	0.1	0.9	23.7	
October	23.7	7.2	1.8	0.7	0.1	0.9	22.1	18.1
November	22.1	1.6	1.9	0.7	0.1	0.6	25.4	
December	25.4	2.9	1.7	0.7	0.2	0.5	25.0	
2004								
January	25.0	2.3	2.2	0.9	0.2	0.4	24.0	16.8
February	24.0	2.6	1.7	1.1	0.1	0.5	22.8	
March	22.8	2.1	2.2	1.2	0.1	0.4	20.7	
April	20.7	15.7	1.8	0.5	0.01	0.3	32.4	15.8
May	32.4	3.1	1.9	1.6	0.01	0.2	32.3	
June	32.3	1.3	1.9	1.6	0.01	0.2	30.6	
July	30.6	0.5	n.a.	n.a.	n.a.	n.a.	n.a.	24.3

n.a. : Not available. PDS: Public Distribution System. OWS: Other Welfare Schemes. OMS: Open Market Sales.

Note : The norm refers to the total minimum stocks to be maintained by Public Agencies under new buffer stocking policy.

Source : Ministry of Food, Consumer Affairs and Public Distribution, Government of India.

Chart II.3 : Sectoral Growth of IIP



confidence was upbeat on strong financial performance of the corporate sector.

2.18 The industrial revival became broad-based towards the latter part of 2003-04, driven primarily by manufacturing which contributed 86.5 per cent to overall growth in industrial production (Chart II.3 and Appendix Table II.5). This was supported by a strong expansion in electricity generation, especially in the last quarter of the year when plants, which had remained closed for repair and maintenance during the early part of the year, started functioning. The mining and quarrying sector also staged a recovery in the last quarter of 2003-04, which helped to maintain strong growth in the industrial sector.

Manufacturing Sector

2.19 The manufacturing sector (with a weight of 79.36 per cent in the IIP) sustained the industrial recovery. The improvement in manufacturing activity was spread across 12 industry groups. The production of paper and paper products, transport equipment and machinery and equipment rose by above 15 per cent. The paper industry benefited from improved market conditions and higher capacity utilisation on account of modernisation of some paper mills. The production of transport and machinery equipment was boosted by an upsurge in exports and domestic demand in the automobile segment. The transport segment responded well to the development of highways and improved rural road network. The demand for passenger vehicles was driven up by aggressive marketing, launching of new models and easy financing schemes. The passenger car segment expanded in the wake of rising external demand.

Table 2.6: Growth Performance of Manufacturing Industries

	2003-04		2002-03	
	No. of Groups	Weight (per cent)	No. of Groups	Weight (per cent)
1	2	3	4	5
Acceleration	7	37.7	10	45.5
Deceleration	5	22.8	4	24.5
Negative	5	18.9	3	9.4

Source: Central Statistical Organisation.

According to the Society of Indian Automobile Manufacturers, the share of exports in production of passenger cars rose from 9.8 per cent in 2001-02 to 16.0 per cent in 2003-04. Strong export demand for iron and steel and other metals provided a fillip to production in basic metals and alloy industries. Exports and higher domestic sales by pharmaceutical companies buoyed up the growth of basic chemicals and chemical products. On the other hand, textile products, 'leather and leather and fur products', cotton textiles, food products and 'jute and other vegetable fibre textiles' suffered decline in output (Table 2.6 and Appendix Tables II.6 and II.7). The textile industry received a series of setbacks from the decline in production of cotton and jute textiles, spun yarn and fabrics, a powerloom strike at the beginning of the year, poor external demand conditions and increase in cotton prices. The importance of external demand in strengthening the activity of manufacturing has increased over the years.

Use-based Classification

2.20 A heartening feature of the industrial recovery has been the sustained growth in the production of capital goods and intermediate goods with the former registering a double-digit growth during 2003-04 (Table 2.7 and Appendix Table II.8). The concomitant surge in imports of these items is indicative of capital

Table 2.7: Growth of IIP – Use-based Classification

(Per cent)

Sector	Growth Rate		Weighted Contribution in IIP Growth	
	2003-04	2002-03	2003-04	2002-03
1	2	3	4	5
Basic Goods	5.4	4.9	25.1	27.4
Capital Goods	13.1	10.5	17.6	16.2
Intermediate Goods	6.3	3.9	25.6	19.3
Consumer Goods	7.1	7.1	31.2	37.0
i) Consumer Durables	11.5	-6.3	12.0	-8.9
ii) Consumer Non-durables	5.7	12.0	19.3	45.9

Source: Central Statistical Organisation.

deepening associated with a more intensive utilisation of capacity.

2.21 Production in the basic goods sector increased marginally during the year due to slowdown in the growth of mining, cement and steel sectors. There was a sharp turnaround in the consumer durables production. Factors contributing to the revival of consumer durables are structural as well as cyclical. The structural factors pushing up the propensity to consume are low real rates of return on deposits and the penetration of consumer credit by financial intermediaries. Sustained increase in per capita income, on the other hand, enabled greater leverage by borrowers contributing to the consumer finance take-off. Increase in disposable income in rural areas as a result of the bumper agricultural harvest in 2003-04 also spurred sales of consumer durables. The non-durables segment of the consumer goods sector, however, slowed down. Payment and crop disease problems adversely affected sugar production. Lacklustre domestic and external demand held down the performance of the textile industry. The decline in the production of textiles and textile products is an area of concern, especially in the context of the phasing out of the Multi-Fibre Agreement (MFA) which would have implications for the Indian textile industry (Box II.3).

Box II.3

Phasing out of Multi Fibre Agreement – Implications

A series of bilateral and multilateral agreements on the imposition of tariff and non-tariff barriers by developed countries on textile imports from developing countries culminated in the Multi-Fibre Agreement (MFA) outside the ambit of the General Agreement on Tariffs and Trade (GATT) in 1974. Although MFA was devised as a temporary arrangement to enable the developed countries to restructure their textile industries for creating a level playing field in relation to the developing countries, it continued to be renewed several times. It was eventually replaced by the Agreement on Textiles and Clothing (ATC) of the World Trade Organisation (WTO) on January 1, 1995. The ATC mapped a three-stage phase out of quota restrictions by developed countries over a ten-year period ending 2004. Member countries are required to integrate 51 per cent of textiles products into the rules of the WTO during the *interim* phase before switching to complete integration by January l, 2005. The ATC provides for flexibility for members in deciding the products they would integrate at each stage to reach these thresholds.

A market-driven quota-free system would unleash a wave of relocation and restructuring of the textile industry in a number of countries and throw up opportunities and challenges. Developing countries with competitive textile industries could benefit in terms of increased textile exports which were earlier bound by quotas. At the same time, international competition would impose adjustment costs and undermine external sector balances in those countries which have overly protected and less competitive textile industries. Gains from abolition of the MFA are estimated at about US $2 billion per year for the South Asian region. Industrialised countries would reap substantial welfare gains from lower consumer prices and efficiency in the longer run. Adjustment costs in the short or medium-term may, however, push them to take greater recourse to other forms of protection (such as increased tariff rates) when the quotas are phased out.

Freedom from quantitative restrictions of the MFA would translate into significant gains for India's textile sector which accounts for nearly a quarter of India's merchandise exports. International competitiveness is based on inherent strengths such as relatively inexpensive and skilled labour force, abundant supply of quality raw material, design expertise and a competitive niche in outsourcing of textiles from India by global retail chain outlets. Freer international trade in textiles could also expose vulnerabilities embedded in the industry's excessively fragmented structure, application of inferior technology with low mechanisation, protection of the handloom industry and reservation of some textile segments for small sector industries. Rigidities in the existing labour laws and absence of good infrastructure have deterred large foreign direct investment in the textile sector. The Steering Group on Investment and Growth, 2002 (Chairman: Shri N.K Singh) had estimated that modernisation of the textile sector would cost Rs.98,500 crore.

Several initiatives have been undertaken to improve India's position in world textile trade in a quota-free environment . These include catch-up with state-of-the-art standards in terms of quality, design and marketing, access to international financial markets for purchasing project machinery under the Technology Upgradation Fund Scheme (TUFS), a uniform duty structure, a mechanism for restructuring the debt portfolios of viable and potentially viable textile units and setting up of Apparel Parks with special infrastructural facilities. The garments segment has been de-reserved and FDI is freely allowed in the textile sector.

References

1. Bhardwaj, A., S. Kathuria, and W. Martin (2001), "Implications for South Asian Countries of Abolishing the Multi Fibre Arrangement", World Bank.
2. Government of India (2002), Steering Group on Investment and Growth in Textile Industry.
3. Hertel, T., *et al* (1996), "Liberalising Manufactures Trade in a Changing World Economy", in Martin and Winters, L.A.,. *The Uruguay Round and Developing Countries* (ed.), Cambridge University Press, Cambridge.
4. Lankes, H. P. (2002), "Market Access for Developing Countries", *Finance and Development*, Volume No. 39, September.

Capacity Utilisation

2.22 Capacity utilisation recovered across all industries to 81.6 per cent during 2003-04 in the environment of industrial resurgence (Table 2.8). Out of 17 two-digit manufacturing groups, 9 manufacturing groups recorded an increase in capacity utilisation. These included 'food products', 'beverages, tobacco and related products', 'jute and other vegetable fibre textiles', 'paper and paper products', 'leather and leather products', 'non-metallic mineral products', 'basic metals and alloy industries', 'metal products and parts' and 'transport equipment and parts'. On the other hand, 'cotton textiles', 'wool, silk and man made fibre', 'textile products', 'wood and wood products', and machinery and equipment showed reduction in capacity utilisation. At the global level, data on capacity utilisation are available only in respect of few countries such as the US, Canada, Sweden, South Korea and Thailand. Methodologies followed by them also differ. While the capacity utilisation of South Korea and Thailand stood at 80.7 per cent and 77.5 per cent, respectively, the US recorded a lower capacity utilisation at 76.6 per cent in March 2004.

Infrastructure Industries

2.23 The composite index of six infrastructure industries recorded marginally lower growth during 2003-04 mainly on account of the subdued performance of crude petroleum, finished steel and cement sectors (Chart II.4 and Appendix Table II.9). The production of crude petroleum suffered on account of high water-oil ratio in some of the oil fields. The production of cement and steel decelerated from high growth during 2002-03 due to less than expected demand from the construction sector.

2.24 Many infrastructure industries were not able to achieve production targets (Table 2.9). Passenger traffic of domestic as well as international civil aviation sectors was below capacity. Electricity generation in both thermal and hydro segments was also below target. The production of crude petroleum fell short of target mainly due to lower production at some of the plants of the Oil and Natural Gas Corporation (ONGC). The fertiliser sector also remained below target on account of lacklustre performance by both public and private sector plants. The petroleum refinery sector could,

Table 2.8: Capacity Utilisation

(Per cent)

Industry	Weight	Capacity Utilisation P			
		2003-04	2002-03	2001-02	2000-01
1	2	3	4	5	6
Manufacturing Industry	**791.73**	**81.5**	**81.0**	**79.2**	**81.7**
Food products	90.83	76.0	71.2	64.4	59.9
Beverages, tobacco and related products	23.82	81.5	72.3	83.2	84.8
Cotton textiles	55.18	92.9	93.0	95.4	94.6
Wool, silk and man-made fibre textiles	18.70	89.3	91.6	88.3	91.1
Jute and other vegetable fibre textiles (except cotton)	5.90	76.9	75.2	74.8	79.0
Textile products (including wearing apparel)	25.37	88.9	91.5	85.7	92.5
Wood and wood products, furniture and fixtures	27.01	87.7	88.4	83.1	92.2
Paper and paper products and printing, publishing and allied activities	26.52	89.8	89.0	91.2	94.1
'Leather' and 'leather and fur products'	11.39	82.3	75.5	80.5	81.1
Chemicals and chemical products except products of petroleum and coal	140.52	83.9	84.1	81.2	86.5
Rubber, plastic, petroleum and coal products	57.28	82.0	83.1	80.1	84.6
Non-metallic mineral products	43.97	90.8	85.5	86.2	75.6
Basic metal and alloy industries	74.53	86.6	86.0	85.2	86.7
Metal products and parts (except machinery and equipment)	28.10	83.7	81.0	80.0	80.8
Machinery and equipment other than transport equipment	97.17	76.5	79.4	76.8	80.2
Transport equipment and parts	39.84	78.2	71.7	73.9	75.6
Other manufacturing industries	25.59	76.0	76.1	78.1	78.7
Mining and Quarrying	**104.74**	**88.9**	**87.8**	**90.4**	**91.0**
Electricity	**101.69**	**91.1**	**95.3**	**92.0**	**93.9**
All Industries	**998.15**	**81.6**	**81.0**	**79.3**	**81.7**

P : Provisional.

Note : Capacity utilisation has been estimated under the peak output approach from the production data for 303 industries supplied by the Ministry of Statistics and Programme Implementation.

Source : Ministry of Statistics and Programme Implementation, Government of India.

Chart II.4 : Growth of Six Infrastructure Industries

however, achieve its target on account of high capacity utilisation. Port traffic remained above target, mainly due to exports of iron ore cargo to China.

2.25 The power sector is affected by a widening gap between the cost of power supply and average realisation, on the one hand, and between availability and demand for power, on the other. Exacerbating the precarious situation are increasing annual losses of State Electricity Boards (SEBs) and rising outstanding dues to Central Power Sector Utilities (CPSUs). The recently passed Electricity Act, 2003 aims at consolidating the laws relating to generation, transmission, distribution, trading and use of electricity. Coordinated efforts by the Central and the State Governments have culminated in the framing of a National Electricity Policy in 2003-04 (Box II.4).

Performance of Central Sector Projects

2.26 The Central Government started several new projects in the power, railways and petroleum sectors during 2003-04. The implementation of these projects, however, suffered delays (Table 2.10). The number of delayed projects rose and cost overruns occurred, especially in surface transport and power sectors. Railways and surface transport sectors accounted for a major portion of the total Central Sector Projects. The large magnitude of cost overruns could be attributed to a variety of reasons, *viz.*, insufficient allocation of funds, disputes relating to land acquisition, law and order problems, delays in completing the procedures related to awarding the contracts, delays involved in completing feasibility study, project appraisal and planning, insufficient delegation of decision making process and inadequate monitoring of the projects.

Mergers and Acquisitions

2.27 The industrial restructuring process in terms of number of mergers and acquisitions slowed down in 2003-04 (Table 2.11). The value of total acquisitions announced, however, increased substantially during 2003-04. The significant increase in the value of acquisitions during January-March 2004 was due to

Table 2.9: Targets and Achievements of Infrastructure Industries

Sector	Unit	2003-04			2002-03		
		Target	Achievement	Gap (%)	Target	Achievement	Gap (%)
1	2	3	4	5	6	7	8
1. Power	Billion Units	573	558	-2.6	546	532	5.0
2. Coal	Million Tonnes	345	356	3.1	332	337	5.6
3. Finished Steel	Thousand Tonnes	37,319	36,925	-1.1	36,885	34,528	6.9
4. Railways	Million Tonnes	550	557	1.3	515	519	7.5
5. Shipping (Major Ports)	Million Tonnes	334	345	3.2	296	314	9.9
6. Fertilisers	Thousand Tonnes	15,821	14,200	-10.2	16,435	14,466	-1.8
7. Cement	Million Tonnes	126	123	-2.0	116	116	6.1
8. Crude Petroleum	Million Tonnes	34	33	-0.3	33	33	1.0
9. Petroleum Refinery Products	Million Tonnes	117	122	4.3	117	113	8.2
10. Civil Aviation (International)*	Lakh No.	175	131	-24.9	112	123	6.5
11. Civil Aviation (Domestic)*	Lakh No.	247	193	-21.9	215	170	13.1

* : Refers to capacity in the column for 'Target'.
Source : Ministry of Statistics and Programme Implementation, Government of India.

Box II.4

National Electricity Policy

Several emerging market economies have undertaken institutional reforms covering restructuring, introduction of competition and privatisation of ownership in the power sector. In India, the Electricity Act, 2003 empowered the Central Government to prepare a National Electricity Policy (NEP) in consultation with the State Governments and the Central Electricity Authority (CEA) to provide power for all by 2012, rural electrification for seeking electricity access to all households within the next five years, supply of reliable and quality power, increase in the per capita consumption of power and protection of consumer interests. In May 2004, the Government decided to undertake a review of the Electricity Act in view of the concerns expressed by a number of States. Subsequently, the draft NEP has been placed in the public domain for wider public debate. Some of the broad features of the draft NEP are indicated below.

Power Generation: The NEP outlines a strategy for meeting the target of addition in capacity of one lakh mega watts (MW). It proposes debt financing of longer tenure for hydro plant projects that have initiated an additional production capacity of 50,000 MW. In the case of thermal capacity, additional gas-based, liquid fuel-based and imported coal-based plants have been recommended subject to proper commercial viability and security of supply of materials. In the case of nuclear power, the objective is to achieve 20,000 MW installed capacity by 2020.

Transmission: The Central Government has indicated that it would facilitate the development of a national grid for inter-State transmission. Network expansion should be planned and a regulatory framework for non-discriminatory open access in transmission should be put in place to encourage trading in electricity.

Distribution: Robust competition in the electricity market depends on open access and multiple licenses in the same area of supply. The liabilities of State Electricity Boards (SEBs) need to be restructured for ensuring financial viability and sustainability. The other policy measures proposed to be undertaken include upgradation and augmentation of the distribution network, conduct of energy audit, time bound programme for reduction of technical and commercial losses, implementation of Information Technology (IT) system for billing of metered consumers, promotion of high voltage distribution system to reduce transmission and distribution losses and setting up of Special Courts for electricity theft.

The NEP assumes importance in the context of the priority attached to the power sector reforms. Rural electrification, creation of a Power Exchange for marketing electricity, energy conservation and regulation of quality of power to protect consumer interests are other priorities of the NEP.

References

1. Government of India (2004), *Report of the Task Force on Power Sector Investments and Reforms*, Ministry of Power, New Delhi.
2. _____(2003), *Annual Report* of the Ministry of Power, 2002-03, New Delhi.
3. _____(2003), Draft National Electricity Policy, Ministry of Power, New Delhi.

mega disinvestment of the Government's stake in ONGC amounting to Rs.10,536 crore. Mergers and acquisitions were higher in respect of food and beverages, textiles, chemicals, electronics and automobiles (including automobile ancillaries). In terms of value, however, acquisitions were led by

Table 2.10: Performance of Central Sector Projects

(No. of Projects)

	As at end-March		
	March 2004	March 2003	March 2002
1	2	3	4
Ahead	28	32	4
On Schedule	73	77	68
Delayed	112	95	49
Without O.D.C and D.O.C	73	60	69
Total	**286**	**264**	**190**
Cost Overruns of Delayed Projects (Rupees crore)	40,851	27,674	25,366
Cost Overruns of Delayed Projects (% of original cost)	79.3	53.6	80.7

O.D.C : Original Date of Commissioning.
D.O.C : Date of Commissioning.
Source : Ministry of Statistics and Programme Implementation, Government of India.

Table 2.11: Mergers and Acquisitions Announced

Period	Total Acquisitions				Mergers	
	2003-04		2002-03		2003-04	2002-03
	No.	Amount (Rupees Crore)	No.	Amount (Rupees Crore)	No.	No.
1	2	3	4	5	6	7
April-June	221	4,096	234	9,570	50	91
July- Sept.	194	4,427	253	6,528	132	119
Oct.-Dec.	218	7,105	180	3,945	54	92
Jan.-March	197	19,445	176	3,742	55	79
Total	**830**	**35,073**	**843**	**23,785**	**291**	**381**

Notes : 1. Data are provisional.
2. Deals include preferential allotments, buyback of shares and disinvestment proposals, among others.

Source : Centre for Monitoring Indian Economy (CMIE).

the mining industry, followed by chemicals, electronics, financial services, electricity and food and beverages.

2.28 Lead information suggests a perceptible improvement in the overall investment climate. The industrial investment intentions increased significantly during 2003-04, facilitated to a large extent by considerable procedural simplifications introduced during the year (Table 2.12). Industrial Entrepreneurs Memoranda (IEM) filed with the Government revealed that the proposed investment nearly doubled during the year. Industry-wise distribution of investment intentions continues to reflect a preference for textiles, metallurgical industries and chemicals other than fertilisers.

2.29 The financial performance of the private corporate sector improved markedly during 2003-04. Financial results of about 1200 companies during the year showed a pick-up in sales and a sustained decline in interest payments leading to a surge in post-tax profits (Table 2.13). Net profits continued to surge at a faster rate than sales for the second consecutive year mainly due to a decline in interest expenses which, in turn, was mainly due to substitution of high cost debt with low cost debt financing enabled by a soft interest rate regime. An internal study of a sample of companies during 2003-04 showed that although the sales growth of the services sector firms was distinctly higher than that of manufacturing sector firms, there was not much divergence between the net profit growth rates between the two groups of firms. This shows that manufacturing firms, which rely more on borrowed funds than services sector firms, tended to reap greater benefits of lower interest burden. This helped them to maintain their profitability comparable with the services sector firms despite registering relatively lower sales growth.

Table 2.12: Industrial Investment Proposals

Year	IEM		LOI/DILs	
	No. of Proposals	Proposed Investment (Rupees crore)	No. of Proposals	Proposed Investment (Rupees crore)
1	2	3	4	5
2001-02	3,094	70,994	102	1,361
2002-03	3,178	80,824	60	332
2003-04	4,130	1,54,954	145	3,454
Cumulative (up to March 2004)*	52,318	12,04,732	3,918	1,11,136

IEM : Industrial Entrepreneurs Memoranda.
LOI : Letter of Intent.
DILs : Direct Industrial Licences.
* : Since August 1991.
Source : Department of Industrial Policy and Promotion, Ministry of Commerce and Industry, Government of India.

Small Scale Sector Industries

2.30 Small scale industries continue to occupy a significant position in employment generation, output and exports. The SSI sector contributed about 34 per cent of the country's exports during 1999-2003. It created additional employment of more than a million persons every year during the same period. The value of output produced by the SSI sector during 2003-04 increased by 12.6 per cent to Rs.3,51,427 crore (Table 2.14).

2.31 The upsurge in industrial production has continued during the first quarter of 2004-05. IIP growth accelerated to 7.6 per cent as compared with 5.7 per cent during the comparable period of 2003-04 on the strength of manufacturing activity. It is encouraging to note that growth in intermediate goods production rose sharply to 10.4 per cent from 2.8 per cent in the first quarter last year. The growth of capital goods production also accelerated to 14.9 per cent from 8.4 per cent,

Table 2.13: Select Indicators of Financial Performance of Non-Government Non-financial Companies

(Growth rate in per cent)

Item	Quarter 1		Quarter 2		Quarter 3		Quarter 4	
	2003-04	2002-03	2003-04	2002-03	2003-04	2002-03	2003-04	2002-03
1	2	3	4	5	6	7	8	9
Number of Companies	**1,202**	**1,236**	**1,213**	**1,214**	**1,263**	**1,264**	**1,386**	**1,263**
Sales	11.1	7.6	14.6	9.6	20.5	10.8	19.6	14.6
Total Expenditure	11.6	7.6	14.8	9.2	20.7	9.9	17.5	13.9
Gross Profits	16.0	8.5	18.2	9.4	25.3	17.6	37.8	19.6
Interest	-15.5	-8.2	-15.9	-9.5	-16.6	-11.2	-17.1	-11.3
Profits after Tax	40.6	17.9	54.6	18.7	52.3	41.7	67.2	42.2

Table 2.14: Performance of Small Scale Industries

Item	2003-04	2002-03	2001-02	2000-01	1999-00
1	2	3	4	5	6
No. of Units (million)	11.40	10.95	10.52	10.11	9.72
Value of Output (Rs. Crore)	3,51,427	3,11,993	2,82,270	2,61,289	2,34,255
Employment (million)	27.14	26.01	24.91	23.91	22.91
Exports from SSI (Rs. Crore)	n.a.	86,013	71,244	69,797	54,200

SSI : Small Scale Industries. n.a. : Not available.
Source : Ministry of Small Scale Industries, Government of India.

reflecting higher demand from large scale construction activity and easy availability of finance. Growth in consumer durables also accelerated to 11.0 per cent from 4.0 per cent during 2003-04, reflecting higher demand for TV receivers, refrigerators, passenger cars, utensils and electric fans. The consumer non-durables segment, however, decelerated to 4.3 per cent from 11.0 per cent on account of decline in production of non-cotton cloth, sugar and edible oils. The performance of infrastructure improved in tandem with the overall industrial production, with the growth of six infrastructure industries increasing to 5.4 per cent during the first quarter of 2004-05 from 4.7 per cent during the first quarter of 2003-04. The higher growth was driven by increased production in petroleum, electricity and coal sectors. Petroleum production was boosted by increased refinery capacity as well as higher capacity utilisation. Higher coal production reflected a switch in domestic demand away from imports as a result of rising international prices.

2.32 According to the National Council of Applied Economic Research (NCAER), business confidence was at an eight-year high in April 2004. Private sector surveys also indicate that business optimism has touched an all-time high on three counts - volume of sales, net profits and new orders. The return to the high growth of the 1980s in industrial activity is contingent upon a revival of new investment in high growth sectors and intensification of the process of building up a world class physical infrastructure.

Services

2.33 The services sector continued to be the mainstay of the expansion during 2003-04, contributing 57.6 per cent to real GDP growth. Leading the upsurge was ‘trade, hotels, transport and communication’. This was in consonance with the improved performance of the commodity producing sectors. The strong expansion in cargo handled at major ports as well as the rise in freight and passenger traffic of the railways boosted the performance of the transport sector. According to the CSO, net tonne kilometres and passenger kilometres in respect of railways grew by 5.5 per cent and 3.7 per cent, respectively, during the first three quarters (April-December) of 2003-04. Production of commercial vehicles and cargo handled at major ports showed a growth of 35.7 per cent and 7.5 per cent, respectively during the same period. A record increase in tourist inflows and higher occupancy provided an impetus to the growth of the hotel industry during the year. Lower tariffs in the cellular phone segment due to intense competition among cellular operators and increased penetration into rural areas led to substantial growth of the telecommunication sector. Other categories of services registered somewhat lower growth than in the preceding year (Table 2.15).

Table 2.15: Sub-sectoral Performance of the Services Sector

(Per cent)

Sub-sector	Share in Services Sector GDP		Growth Rate		Relative Contribution to Growth in Services	
	2003-04#	2002-03*	2003-04#	2002-03*	2003-04#	2002-03*
1	2	3	4	5	6	7
Trade, Hotels, Transport and Communication	44.1	43.0	11.2	7.0	57.2	42.3
Financing, Insurance, Real Estate and Business Services	22.9	23.2	6.8	8.8	18.7	28.2
Community, Social and Personal Services	23.8	24.4	6.0	5.8	17.2	19.9
Construction	9.2	9.4	6.2	7.3	6.9	9.5
Services	**100.0**	**100.0**	**8.5**	**7.2**	**100.0**	**100.0**

: Revised Estimates. * : Quick Estimates.
Source : Central Statistical Organisation.

Box II.5

Financing Services – Cashing in on High Growth

The Indian economy is dominated by the services sector with communication services, financial services, business services (including IT) and community services being the main growth drivers. The financial sector does not seem to have exploited the tremendous opportunities for financing the growth of services. The services sector accounted for 35.6 per cent of total bank credit at the end of March 2002 as against 30.5 per cent at the end of March 1990. This level was much lower in comparison with the share of services in total bank credit in advanced countries such as the UK (47.9 per cent) and the US (where real estate sector alone accounted for 51.7 per cent of the total commercial bank credit), Thailand (63.8 per cent) and the Philippines (66.4 per cent). An analysis of distribution of bank credit among the various categories of services in India shows that the shares of transport operators and wholesale trade declined sharply between 1980 and 2002 due to increased credit allocation to other priority sector categories. This reflected some diversification in bank credit allocation which was essentially policy-driven as the coverage of the priority sector was widened.

The lagging of financing of services, to a large extent, reflects a legacy of nurturing the growth of basic and heavy industries as also directing credit to the priority sector (including agriculture). Lending to services has not been favoured by traditional banking practices followed in India such as collateral-based financing, emphasis on securitised instruments, particularly in the context of bill financing, limited appetite for risks inherent in financing services and lack of standardisation and customisation of financial products.

One feasible solution for providing credit to the services sector is to adopt a cash flow-based approach rather than a collateral-based approach. It is also possible to introduce innovative credit enhancement methods and securitisation in the financing of services. Venture capital funding by financial institutions needs to be encouraged to give a big push to the services sector. The Credit Information Bureau of India Limited (CIBIL) can help by addressing the problem of information asymmetry by providing information to banks about the credit history and repayment records of interested borrowers.

References

1. Gordon, J. and P. Gupta, (2003), “Understanding India’s Services Revolution”, A Paper prepared for the IMF – NCAER Conference.
2. Mohan, R. (2004), “Financing Services Sector Growth”, Lecture delivered at M.A. Master Memorial Lecture at Indian Merchants Chamber, March 26, Mumbai.
3. Reserve Bank of India (1999), *Report of the Working Group on Discounting of Bills by Banks* (Chairman: Shri K.R. Ramamoorthy).

Financing of the Services Sector

2.34 In India, services (including construction) accounted for 56.2 per cent of GDP in 2003-04, having steadily risen from 38.3 per cent in 1970-71. Services encompass a wide spectrum of heterogeneous activities ranging from the traditional trade and transport services to the knowledge-intensive new economy services. The buoyant expansion of the services sector in India offers significant financing opportunities. This calls for a strategy to improve credit delivery to the services sector commensurate with its large and growing presence in real activity in India (Box II.5).

Information Technology Enabled Services and Business Process Outsourcing

2.35 According to National Association of Software and Services Companies (NASSCOM), the Information Technology Enabled Services and Business Process Outsourcing (ITES-BPO) segment in India grew by 54 per cent during 2003-04, primarily on account of increased overseas demand. On the other hand, the domestic sales of software and services slowed down to around 15 per cent in 2003-04 as compared with 23 per cent in 2002-03. Software and services exports were estimated to have risen by 28 per cent to US$ 12.2 billion during 2003-04. According to the International Data Corporation (IDC), the global ITES-BPO market is expected to grow at a compound annual growth rate of 9.0 per cent during 2002-06. This augurs well for India where the software and services export segment contributed around 73 per cent to India’s overall invisible receipts in 2003-04 as against 59.0 per cent in 2002-03. North America continued to remain India’s largest software and services export destination, followed by the European and Asia Pacific regions. With the IT service exports rising, India continues to attract a large global share of the off-shore business from various countries like the US, the UK and Europe. This has generated a backlash against BPO, particularly in the US (Box II.6).

Box II.6
Business Process Outsourcing – Issues Involved

India is a leading destination for outsourcing of Information Technology Enabled Services (ITES) and other related Business Process Outsourcing (BPO) activities. Currently, India renders more than two-thirds of all offshored ITES worldwide. The BPO activities encompass not only ITES but also a wide range of areas comprising services relating to manufacturing, banking, insurance, sales, marketing, utilities and human resources. India's comparative advantage in the outsourcing business is on account of availability of well developed telecommunication network and advanced technological infrastructure, skilled yet low cost labour force, widespread use of English language, and India's location in a different time zone from the United States (US) enabling a 24-hour service. The BPO activities have benefited India by generating substantial job opportunities in the country and augmenting export earnings. India is expected to maintain its lead as the best offshore outsourcing destination, particularly for the US and European companies.

Several studies have indicated that offshoring of US business to India provides greater benefits to the US economy than to the Indian economy. The outsourcing has reduced the prices of IT hardware by 10-30 per cent due to the diffusion of IT throughout the US economy. It has also raised productivity and growth significantly. The US outsourcing from India reduces costs by 40-60 per cent, improves quality by 3-8 per cent and increases productivity by 20-150 per cent. Out of every $1.45-1.47 value created, $1.12-1.14 goes to the US and India receives only 33 cents. A number of US companies are in favour of outsourcing to India purely on economic grounds. More and more traditional industries like manufacturing, energy, transportation and retail sectors located in developed countries would be outsourced to developing countries in the near future.

Certain developed economies have, however, begun to view the outsourcing of ITES-BPO as a loss of domestic employment. Several States of the US have introduced legislations seeking a ban on outsourcing of various economic activities from India. There are, on the other hand, influential views in the US that feel that the fear of job losses due to outsourcing is exaggerated. Outsourcing abroad has proved profitable primarily for jobs that can be routinised. The European Union observes that BPO is good for India and good for the world economy. The UNCTAD has called upon developing countries to bring a legislation relating to BPO under the General Agreement on Trade in Services (GATS) in the wake of the legislative measures in the US. The UK is in favour of free, transparent and open market and would not put up barriers on the BPO. Globalisation and outsourcing work both ways. A study by Global Insight reveals that the majority of job losses to offshore outsourcing between 2000-03 occurred due to factors such as the slowdown in the US and the bursting of the telecom and dotcom bubbles. Raising of barriers by the US to worldwide outsourcing would not only slow down its economy but also reduce the number of new jobs available to American workers.

Indian entities should strive to diversify their markets to other countries rather than depending only on the US market. India would also have to continuously innovate and maintain its low-cost niche in order to compete with competitors like China, the Philippines, Malaysia, Australia, South Africa, and Singapore. India needs to set up more foreign affiliates in the IT segment to provide services offshore, besides attracting more FDI to undertake BPO activities in the country, which would pacify the protectionist reactions by developed countries. The Indian BPO market should also strive to attain maturity through consolidation to withstand the competitive threat, particularly from the emerging East Asian countries. This could be achieved through increased mergers and acquisitions, not only in India but also in developed countries, which would help to achieve cost efficiency and competitive price advantages. The BPO segment in India attracted US $1 billion worth of FDI during 1996-2002, which works out to 5 per cent of the total FDI inflows of US $20 billion during the period.

References

1. A. T. Kearny (2004), *Offshore Location Attractiveness Index - Making Offshore Decisions*, A.T.Kearny Consultancy Services, Illinois, USA.
2. Bernanke, B. S. (2004), Distinguished Speaker Series, Fuqua School of Business, Duke University, North Carolina, March.
3. Greenspan, A. (2004), Boston College Finance Conference 2004, Boston, March.
4. National Association of Software and Services Companies (2004), *The IT Industry in India: Strategic Review 2004*, NASSCOM, New Delhi.
5. OECD (2004), *Globalisation of the IT Sector*, OECD.
6. Ricupero, R. (2004), BPO a Legitimate Part of Liberalisation, UNCTAD, February.
7. UNCTAD (2003), *E-commerce and Development Report*, United Nations.
8. World Bank (2004), *Global Development Finance*, World Bank.

AGGREGATE DEMAND

2.36 The deceleration in economic growth in 2002-03 reflected the slowdown in real private consumption demand on account of a sharp decline in rural incomes. Investment demand, however, continued to accelerate even in the drought year. Increased Government demand - consumption as well as investment - acted as counter cyclical stabilisers in 2002-03 (Table 2.16).

Saving and Capital Formation

2.37 Information on saving and capital formation is available up to 2002-03. According to the CSO, the gross domestic saving (GDS) rate moved up to 24.2 per cent of GDP in 2002-03 from 23.5 per cent of GDP in the preceding year (Appendix Table II.10). The improved aggregate saving was entirely due to reduced public sector dis-saving, which contracted to 1.9 per cent of GDP in 2002-03 from 2.7 per cent in 2001-02, reflecting improved Government finances (Chart II.5). Saving by the household sector - the principal saver - declined marginally to 22.6 per cent of GDP from 22.7 per cent over the same period. There was a switch in household savings in favour of physical assets from financial assets. The buoyancy of private corporate savings noticed from 1999-2000 continued in 2002-03 on the back of increased profits. As a ratio to GDP, however, private corporate sector saving declined marginally from 3.5 per cent in 2001-02 to 3.4 per cent in 2002-03.

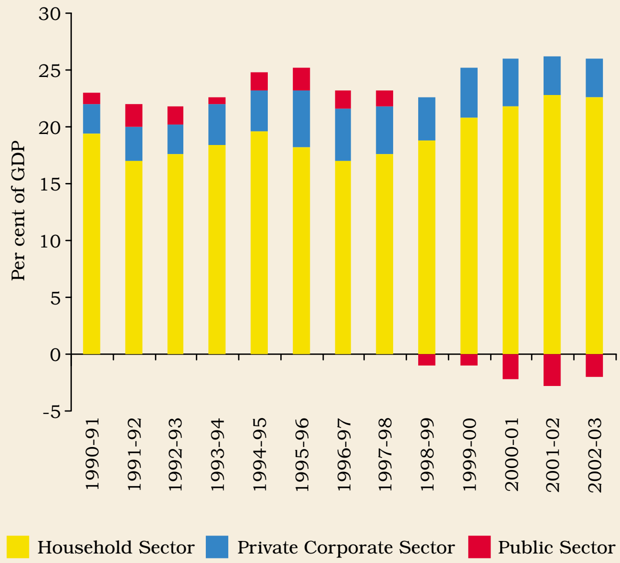
Table 2.16: Growth in Select Sources of Real Effective Demand #

(Per cent)

Item	2002-03*	2001-02@	2000-01	1999-00	1996-97 to 1998-99 (Average)
1	2	3	4	5	6
1. Total Final Consumption Expenditure	3.7	5.2	2.5	7.2	6.3
Of which :					
Private Final Consumption Expenditure	3.8	5.6	2.9	6.1	5.8
Government Final Consumption Expenditure	3.1	3.0	0.5	13.2	9.5
2. Total Investment +	7.6	-2.0	0.7	20.8	2.5
Private Investment ++	11.6	3.3	3.0	21.5	1.8
Public Investment ++	2.5	-5.8	-5.0	13.3	1.1
3. Total Fixed Investment	9.4	4.3	4.1	9.3	4.1
Of which :					
Private FixedInvestment	9.2	7.3	5.4	11.8	5.8
Public Fixed Investment	9.8	-4.9	0.4	2.7	0.2

: Based on select disposition of real GDP at market prices.
* : Quick Estimates. @: Provisional Estimates.
+ : Adjusted for errors and omissions.
++ : Unadjusted for errors and omissions.
Source : Central Statistical Organisation.

Chart II.5 : Sector-wise Saving Rates



2.38 In recent years, the investment rate has been lower than the saving rate. While the rate of gross domestic capital formation (GDCF) improved marginally in 2002-03, the improvement was sharper in the case of the GDS rate. As a result, the ratio of GDS-GDCF to GDP increased significantly to 0.9 per cent in 2002-03 from 0.3 per cent in the preceding year. The rate of capital formation of public and private corporate sectors declined marginally (Table 2.17).

2.39 Preliminary estimates, based on the latest available information, placed the rate of financial saving (net) of the household sector higher at 11.8 per cent of GDP at current market prices in 2003-04 as compared

Table 2.17: Sector-wise Rates of Gross Capital Formation @@

Item	2002-03*	2001-02@	2000-01	1999-2000
1	2	3	4	5
1. Household Sector	12.3	11.6	11.3	10.3
2. Public Sector	5.7	5.8	6.3	6.9
3. Private Corporate Sector	4.8	4.9	5.1	6.5
Gross Domestic Capital Formation (GDCF)#	**23.3**	**23.1**	**24.4**	**25.3**

@@ : As percentage of GDP at current market prices.
* : Quick Estimates. @ : Provisional.
# : As GDCF is adjusted for errors and omissions, the sector-wise capital formation figures may not add up to the GDCF.
Source : Central Statistical Organisation.

Table 2.18: Household Saving in Financial Assets

(Amount in Rupees crore)

Item	2003-04#	2002-03P	2001-02P	2000-01	1999-00
1	2	3	4	5	6
A. Financial assets (gross)	**4,17,675**	**3,36,609**	**2,89,953**	**2,48,774**	**2,36,351**
	15.1	13.6	12.7	11.9	12.2
1. Currency	42,200	28,447	28,156	15,632	20,845
a) As per cent of GDP at current market prices	1.5	1.2	1.2	0.7	1.1
b) As per cent of financial assets (gross)	10.1	8.5	9.7	6.3	8.8
2. Deposits@	1,79,388	1,39,701	1,14,233	1,02,017	85,850
a) As per cent of GDP at current market prices	6.5	5.7	5.0	4.9	4.4
b) As per cent of financial assets (gross)	42.9	41.5	39.4	41.0	36.3
3. Claims on Government	74,001	62,560	51,940	39,007	28,985
a) As per cent of GDP at current market prices	2.7	2.5	2.3	1.9	1.5
b) As per cent of financial assets (gross)	17.7	18.6	17.9	15.7	12.3
4. Investment in shares and debentures+	5,698	5,504	7,777	10,214	18,119
a) As per cent of GDP at current market prices	0.2	0.2	0.3	0.5	0.9
b) As per cent of financial assets (gross)	1.4	1.6	2.7	4.1	7.7
5. Contractual saving**	1,16,388	1,00,398	87,848	81,903	82,551
a) As per cent of GDP at current market prices	4.2	4.1	3.8	3.9	4.3
b) As per cent of financial assets (gross)	27.9	29.8	30.3	32.9	34.9
B. Financial liabilities	**89,865**	**72,576**	**42,082**	**31,769**	**35,275**
a) As per cent of GDP at current market prices	**3.2**	**2.9**	**1.8**	**1.5**	**1.8**
C. Saving in financial assets (net) (A-B)	**3,27,810**	**2,64,033**	**2,47,871**	**2,17,005**	**2,01,075**
a) As per cent of GDP at current market prices	**11.8**	**10.7**	**10.9**	**10.4**	**10.4**

: Preliminary. P : Provisional.
@ : Comprising bank deposits, non-bank deposits and trade debt (net).
+ : Including units of Unit Trust of India and other mutual funds.
** : Comprising Life Insurance, Provident and Pension Funds.

Notes : 1. These data are revised on the basis of information available up to July 2004 and hence may not tally with the data published in the Quick Estimates of CSO released in January 2004.
2. Components may not add up to the totals due to rounding off.

with the revised estimate of 10.7 per cent in 2002-03 (Table 2.18 and Appendix Table II.11). The increase in household financial saving (net) in 2003-04 reflected a greater propensity for saving in the form of deposits, claims on Government, currency and contractual schemes (life insurance, provident and pension funds).

Outlook

2.40 The India Meteorological Department (IMD) had made a forecast of normal South-West monsoon season at end-June, 2004, *i.e.*, 100 per cent of Long Period Average (LPA) with a model error of +/-4 per cent. The cumulative rainfall during June 1 to August 11, 2004 was, however, 7 per cent below normal (LPA) as compared with 3 per cent above LPA during the comparable period of 2003. The area sown as on July 30, 2004 indicates that production of major crops such as rice, coarse cereals, cotton, jute and mesta may be adversely affected, although a clearer assessment will depend on the progress of the South-West monsoon. The industrial recovery currently underway has been broad-based and qualitatively robust. Strong growth in key industries especially transport equipment and parts, paper and paper products, machinery and equipments and basic chemicals and chemical products has industrial growth in 2004-05. An encouraging feature of infrastructure performance has been a revival of the electricity sector. Various indicators suggest an improved investment climate. In particular, sustained expansion of the capital goods sector combined with increased capital goods imports augur well for investment climate. The services sector is also expected to gain further momentum from the commodity producing sectors, particularly in the trade, transport and communication segments and in the 'new economy' activities. Construction activity, in particular, is expected to pick up due to the impetus received from the growth in housing. Also, as the global economy picks up, export demand across a spectrum of industrial products and services is expected to increase. Uncertainties surrounding the progress of the monsoon, the impact on domestic real activity of elevated international crude price levels and the breadth of the global recovery contain some risks for the macroeconomic outlook for India.

III MONEY, CREDIT AND PRICES

3.1 Monetary conditions continued to remain easy during 2003-04, driven by persistent capital inflows. Despite sterilisation operations, the sheer volume of accumulation of the Reserve Bank's net foreign assets (NFA) expanded reserve money at the rate of 18.3 per cent – the highest since 1994-95. Broad money (M_3) expansion was also the highest since the late 1990s. As a consequence, financial markets operated in conditions of ample liquidity. Interest rates at the short end of the market continuum persistently ruled below the Reserve Bank's Liquidity Adjustment Facility (LAF) repo rate and generally softened across the maturity spectrum. Beginning in June 2002, the exchange rate appreciated through the year in nominal terms against the US dollar. Credit offtake remained weak in relation to initial expectations as bank finance was substituted by internally generated funds and cheaper funds raised overseas. The demand for bank credit picked up only in the latter half of the year. With the virtual absence of pressures from aggregate demand, inflation eased during the year, *albeit* haltingly in the second half of the year on account of transient supply pressures emanating from localised drought and the pass-through of hardening international crude prices into domestic prices of petroleum, oil and lubricant (POL) products.

3.2 The assessment of monetary and credit conditions in this Section highlights the rising cover of foreign assets for the monetary base and, thereby, the innate resilience being built against an unanticipated reversal of capital flows. An examination of the behaviour of reserve money shows that it was characterised by a large accumulation of cash balances by the Central Government and shifts in the Reserve Bank's portfolio on account of sterilisation operations. Money supply exceeded the indicative projections but was closely aligned with the surge in real activity. The analysis of domestic credit reflects a significant slowdown in net bank credit to the Government as well as a delayed pick-up in commercial credit. The commercial banking survey reveals a concentration of activity in the latter half of the year in terms of deposits, non-food credit, call/term borrowings and two-way movements in foreign assets/liabilities. A review of the price situation traces the uneven easing of inflation during 2003-04 and highlights the growing influence of international price movements on domestic inflation.

RESERVE MONEY

3.3 Reserve money growth nearly doubled during 2003-04, led by strong capital inflows. The ratio of NFA to reserve money consequently rose to 120.7 per cent by February 2004 – the highest level since the mid-1950s. The Reserve Bank's NFA/currency ratio reached 150.8 per cent in February 2004, and remained well above the benchmark of 70 per cent which was recommended by the Committee on Capital Account Convertibility (Chairman: Shri S. S. Tarapore) to ensure that the Reserve Bank possessed the wherewithal to meet reversals in the external sector. In response, the Reserve Bank's net domestic assets (NDA) registered an unprecedented contraction (Chart III.1).

3.4 Intra-year movements in primary liquidity highlight the sustained pressure from capital inflows (Chart III.2). Base money growth was strong in the first quarter, despite a 25 basis points (bps) cut in the cash reserve ratio (CRR) effective June 14, 2003. The reserve money expansion was driven by strong inflows on account of foreign institutional investors (FIIs) as well as ways and means advances from the Reserve Bank. Sizeable open market operations (OMO), along with the Centre's cash surplus with the Reserve Bank, were able to contract the

Chart III.1 : Sources of Reserve Money

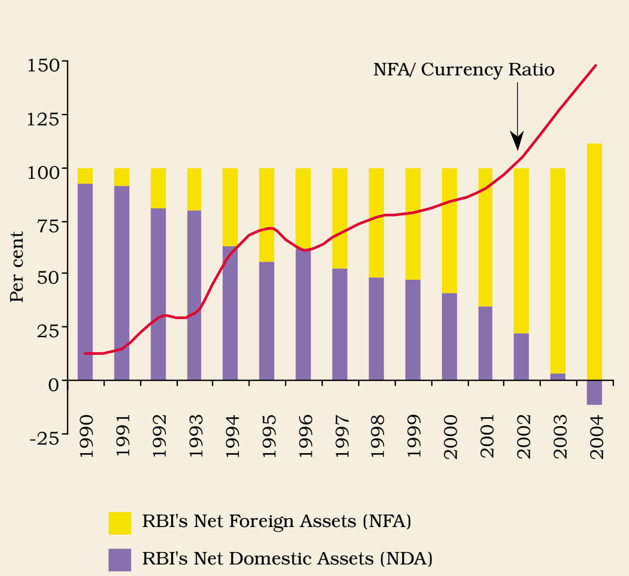
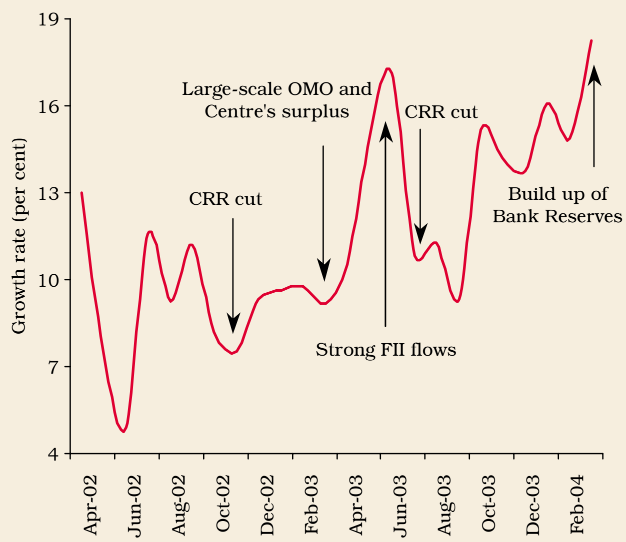


Chart III.2 : Reserve Money Growth



monetary base in the second quarter. A mix of redemption of Resurgent India Bonds (RIBs), prepayment of external debt and a step-up in sterilisation operations moderated the expansionary effect of the massive accretion to the Reserve Bank's NFA in the third quarter. Reserve money expansion continued in the fourth quarter with sustained FII inflows and external commercial borrowings (ECBs). This was exacerbated further by a build-up of bank reserves of Rs.19,662 crore during March 26-31, 2004 reflecting year-end considerations as well as uncertainty following a holiday on March 30, 2004 (Table 3.1 and Appendix Tables III.1 and 2).

3.5 The net Reserve Bank credit to the Central Government (Centre) contracted by 67.3 per cent during 2003-04, pulling its share in reserve money down to 8.5 per cent at end-March 2004 from over 90 per cent in the late 1980s (Table 3.2). Private placements with the Reserve Bank during 2003-04 were mainly to enable prepayment of US $ 3.8 billion

Table 3.1: Reserve Money

(Rupees crore)

Item	2003-04	2002-03	2003-04				2002-03			
			Q4	Q3	Q2	Q1	Q4	Q3	Q2	Q1
1	2	3	4	5	6	7	8	9	10	11
Reserve Money	**67,451** **(18.3)**	**31,091** **(9.2)**	**45,363**	**23,980**	**-18,235**	**16,342**	**25,233**	**7,917**	**6,791**	**-8,850**
Components										
1. Currency in Circulation	44,555	31,499	14,641	17,986	-5,955	17,882	11,561	11,205	-5,901	14,633
2. Bankers' Deposits with the RBI	21,019	-801	29,297	5,961	-12,633	-1,606	13,048	-2,427	12,451	-23,873
3. 'Other' Deposits with the RBI	1,877	393	1,426	33	352	65	625	-861	241	389
Sources										
1. RBI's Net Credit to the Government	-75,772	-31,499	-5,669	-12,506	-53,146	-4,451	9,919	-17,427	-19,779	-4,212
of which: to Central Government	-76,065 (-67.3)	-28,399 (-20.1)	-6,911	-15,844	-53,744	434	7,583	-17,882	-19,555	1,455
2. RBI's Credit to Banks and Commercial Sector	-2,728	-6,468	2,156	-796	-2,525	-1,564	844	8	-784	-6,537
3. Net Foreign Assets of the RBI	1,26,169 (35.2)	94,275 (35.7)	25,808	51,931	25,720	22,710	20,611	34,766	19,619	19,279
4. Government's Net Currency Liabilities to the Public	225	705	24	43	74	84	124	157	256	168
5. Net Non-Monetary Liabilities of the RBI	-19,557	25,922	-23,044	14,692	-11,642	437	6,265	9,587	-7,479	17,548
Memo:										
1. Net Domestic Assets	-58,719	-63,184	19,555	-27,951	-43,955	-6,368	4,622	-26,849	-12,828	-28,129
2. FCA, adjusted for revaluation	1,41,428	82,090	48,093	37,560	31,832	23,943	20,004	31,060	22,881	8,145
3. Net Purchases from Authorised Dealers	1,40,650	75,661	47,845	40,669	29,899	22,237	27,608	25,165	18,958	3,929
4. NFA/Reserve Money (end-period, in per cent)	111.0	97.1	111.0	117.2	110.8	98.8	97.1	98.2	90.2	86.1
5. NFA/Currency (end-period, in per cent)	148.1	126.8	148.1	146.8	138.1	126.8	126.8	124.6	116.6	106.6

NFA : Net Foreign Assets. FCA : Foreign Currency Assets.

Note : 1. Data are based on March 31 for Q4 and on last reporting Friday for all other quarters.
2. Figures in parentheses are percentage annual variations.

of multilateral and bilateral debt. This was counterbalanced by a large build-up of cash balances by the Centre on account of disinvestment proceeds, revenue buoyancy, proceeds under the State Debt Swap Scheme and the higher mobilisation on account of saving bonds. Sustained OMO, including repo operations under the LAF, reduced the stock of marketable Government paper with the Reserve Bank to Rs.40,750 crore at end-March 2004 from Rs.52,546 crore at end-March 2003. This was despite the conversion of the available stock of non-marketable special securities (of Rs.61,818 crore) created out of the past *ad hoc* and tap Treasury Bills into tradable securities during the year.

3.6 Changes in the relative significance of sources of reserve money have important implications. First, a higher ratio of foreign assets to domestic assets in the central bank's balance sheet strengthens its credibility in conducting monetary policy and exchange market operations, supporting investor confidence in the economy. Second, monetisation of capital inflows is more likely to amplify the process of credit creation over time. It directly adds to bank liquidity unlike money financing of public expenditure which often bypasses the banking system in the first round. Third, a higher share of foreign assets in the central bank's balance sheet exposes it to market risks in the event of a sharp appreciation of the domestic currency. Finally, the process of sterilising the monetary impact of the build-up of foreign exchange reserves carries quasi-fiscal costs which are cumulative in character and determine the span of time over which sterilisation operations can be sustained.

Developments during 2004-05

3.7 Reserve money expansion during 2004-05 (up to August 13, 2004) was broadly of the order recorded in the corresponding period of 2003-04 and was largely driven by the accretion to the Reserve Bank's NFA. Reflective of the Reserve Bank's sterilisation operations, the Reserve Bank's net credit to the Centre recorded a sharp decline. The Reserve Bank's net credit to the Centre, in fact, occasionally turned negative in the first quarter of 2004-05 due to the build-up in the Centre's cash balances, including proceeds under the Market Stabilisation Scheme (MSS) (Table 3.3).

Table 3.2: Net Reserve Bank Credit to the Centre

(Rupees crore)

Item	2003-04	2002-03	2003-04				2002-03			
			Q4	Q3	Q2	Q1	Q4	Q3	Q2	Q1
1	2	3	4	5	6	7	8	9	10	11
Net Reserve Bank Credit to the Centre (1+2+3+4-5)	**-76,065**	**-28,399**	**-6,911**	**-15,844**	**-53,744**	**434**	**7,583**	**-17,882**	**-19,555**	**1,455**
1. Loans and Advances	0	-5,176	0	0	-8,145	8,145	0	0	-7,648	2,472
2. Treasury Bills held by the Reserve Bank	-3	-15	0	0	0	-3	3	0	0	-18
3. Reserve Bank's holdings of Dated Securities	-72,227	-24,731	398	-15,795	-45,530	-11,300	11,116	-17,979	-11,761	-6,107
4. Reserve Bank's holdings of Rupee Coins	20	-92	-24	-51	-68	163	-106	97	-146	64
5. Central Government Deposits	3,856	-1,614	7,287	-1	0	-3,430	3,431	0	0	-5,044
Memo Items:*										
1. Market Borrowings through Dated Securities by the Centre #	1,21,500	1,25,000	26,500	15,000	36,000	44,000	18,000	23,000	35,000	49,000
2. Reserve Bank's Primary Subscription to Dated Securities	21,500	36,175	16,500	0	0	5,000	13,000	0	1,157	22,018
3. Repos (-) / Reverse Repos (+) (LAF), net position @	-32,230	1,940	-5,155	-3,580	1,557	-25,052	3,079	10,371	8,845	-20,355
4. Centre's Surplus Investment	17,764	8,905	4,629	-2,355	24,395	-8,905	-5,724	12,624	2,005	0
5. Net Open Market Sales #	41,849	53,781	5,333	14,225	16,671	5,620	11,150	15,693	19,918	7,020
6. Primary Operations +	-100	23,616	4,560	2,304	-32,608	25,643	15,187	-12,527	-8,642	29,598

* : At face value. # : Excluding Treasury Bills. @ : Including fortnightly repos. + : Adjusted for Centre's surplus investment.

Note : Quarterly variations are based on March 31 for Q4 and on last reporting Fridays for other quarters.

Table 3.3: Reserve Money – As on August 13, 2004

(Rupees crore)

Item	Year-on-year Variations			
	As on August 13, 2004		As on August 15, 2003	
	Absolute	Per cent	Absolute	Per cent
1	2	3	4	5
Reserve Money	**52,715**	**13.8**	**46,279**	**13.8**
Major Components				
1. Currency in Circulation	40,246	13.5	35,127	13.4
2. Bankers' Deposits with the RBI	11,627	14.3	11,106	15.8
Major Sources				
1. Net RBI credit to Government	-70,715	-81.2	-49,880	-36.4
of which: to Centre	-69,051	-83.0	-50,820	-37.9
Deposits of the Central Government	45,924		0	
of which: MSS Account	45,925		0	
2. Net Foreign Assets (NFA) of the RBI	1,53,837 (1,25,896)	39.2	97,642 (1,04,484)	33.1

Note : Figures in parentheses are foreign currency assets, net of revaluation.

MONETARY SURVEY

3.8 Broad money (M_3) growth was higher than projected in the Monetary and Credit Policy for 2003-04 (Table 3.4 and Appendix Table III.3). A distinctive feature of the intra-year development of monetary conditions during 2003-04 was the sharp acceleration in M_3 growth towards the end of the year. The large monetary expansion occurred in spite of a bullet redemption of the RIBs in October 2003. During the first half of the year, a revival in cash demand coupled with weak credit demand resulted in a slowdown of the annual M_3 growth rate to a 28-year trough of 11.5 per cent in May 2003. Monetary expansion resumed in September, driven by the abundant liquidity emanating from capital flows, the cut in CRR in June 2003 and the strengthening of the credit offtake.

3.9 The increase in the residency-based NM_3 aggregate during 2003-04 was higher than that of the conventional M_3 aggregate, as the latter directly reflected the contractionary impact of the redemption of the RIBs (Appendix Table III.4). The broader liquidity aggregates, *viz.*, L_1 (NM_3+ postal deposits), L_2 (L_1+ term deposits with financial institutions) and L_3 [L_2+ public deposits with non-banking financial companies (NBFCs)] also registered higher growth in 2003-04 (Appendix Table III.5). Postal deposits continued to grow in view of the attractive rates of return in

Table 3.4: Monetary Indicators

(Per cent)

Item	Outstanding as on March 31, 2004 (Rupees crore)	Variation			
		2003-04		2002-03	
		Point-to-point	Monthly average	Point-to-point	Monthly average
1	2	3	4	5	6
I. Reserve Money	4,36,512	18.3	13.9	9.2	9.3
II. Broad Money (M_3)	20,03,102	16.6	13.0	12.7	13.8
a) Currency with the Public	3,15,493	16.2	13.9	12.8	13.9
b) Aggregate Deposits	16,82,491	16.6	12.8	12.7	13.8
i) Demand Deposits	2,56,039	28.8	17.1	10.9	9.7
ii) Time Deposits	14,26,451	14.6	12.2	12.9	14.5
of which: Non-Resident Foreign Currency Deposits	75,336	-18.6@	-11.0@	1.8	4.4
III. NM_3	19,62,910	19.6	15.0	13.5	14.7
IV. a) L_1	20,34,297	19.9	15.4	13.9	15.0
of which: Postal Deposits	71,387	29.1	28.6	25.8	25.6
b) L_2	20,40,542	19.8	15.4	13.9	14.6
of which: FI Deposits	6,245	-0.8	7.5	22.5	-36.6
c) L_3	20,60,264	19.6	15.6	13.8	14.3
of which: NBFC Deposits	19,722	-0.9	3.6	2.5	6.5
V. Major Sources of Broad Money					
a) Net Bank Credit to the Government (i+ii)	7,45,499	10.2	12.3	14.7	13.6
i) Net Reserve Bank Credit to Government	44,907	-62.8	-43.0	-20.7	-17.4
Of which: to the Centre	36,920	-67.3	-44.9	-20.1	-17.9
ii) Other Banks' Credit to Government	7,00,591	26.0	25.9	27.1	25.5
b) Bank Credit to Commercial Sector	10,17,902	13.2	11.8	12.5	12.0
of which: Scheduled Commercial Banks' Non-food Credit	8,04,824	18.4	16.6	18.6	16.5
c) Net Foreign Assets of the Banking Sector	5,26,586	33.7	27.6	26.6	31.4

@ : Reflects the redemption effect of Resurgent India Bonds (RIBs).

Note : 1. Data are provisional.
2. Variations in deposits, M_3, NM_3, L_1, L_2, and L_3 are adjusted for the full impact of mergers during May 2002 - April 2003, while that in credit are adjusted for the initial impact of mergers.

Chart III.3 : Broad Money Growth – 2003-04

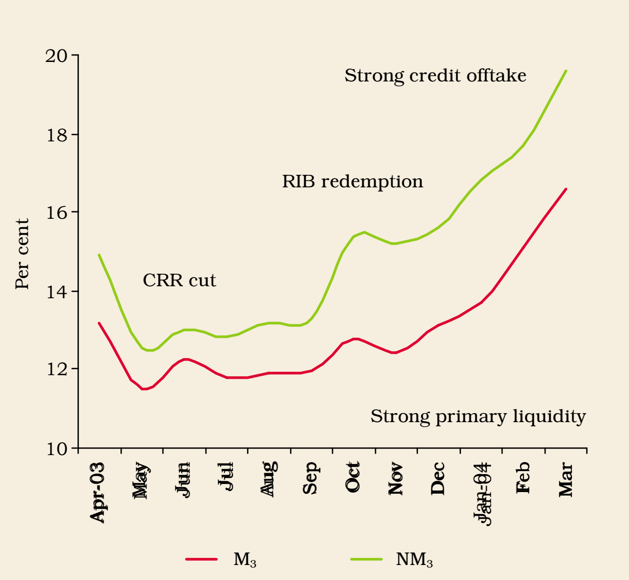
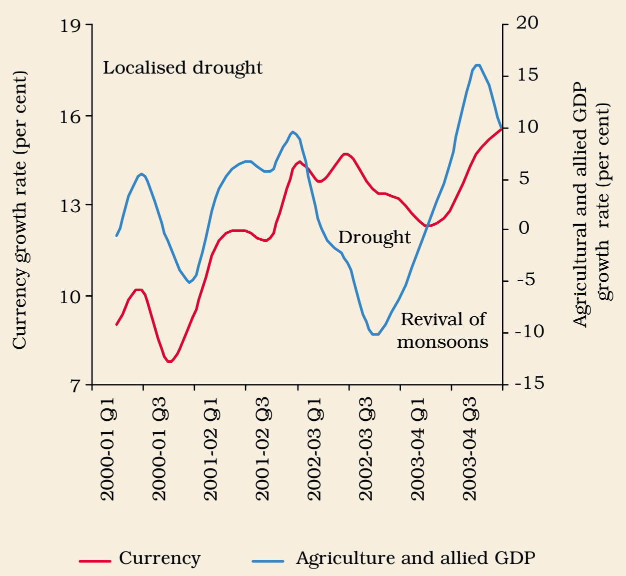


Chart III.4 : Rural Activity and Cash Demand



comparison with bank deposits. Deposits with financial institutions, however, stagnated with the gradual shrinkage of the sector. Some financial institutions were also barred from raising fresh borrowings because of their deteriorating financial situation. Public deposits with NBFCs declined partly because they preferred to rely more on cheaper bank loans (Chart III.3).

3.10 The strong recovery in agricultural activity during 2003-04 led to increased currency demand, especially because cash continues to dominate rural transactions (Chart III.4). Aggregate deposits picked up in the last quarter of the year. A sudden spurt in scheduled commercial banks' non-food credit during the latter half of the year was reflected in a sharp increase in demand deposits. Increased activity in the capital market, including disinvestment and increased FII funds, also contributed to the expansion in demand deposits. Time deposits grew at a marginally higher rate despite a continuing migration of household saving to postal deposits, a shift in household preferences towards mutual funds from banks' fixed deposits and a slowdown in non-resident deposit inflows emanating from the rationalisation of interest rates on NRE deposits (Chart III.5).

3.11 Commercial banks have increasingly turned to non-deposit sources of funds in recent years to take advantage of ample liquidity conditions in the system and easier access to low cost funds overseas. Borrowings by banks – mainly from non-bank entities from the term money market – increased from Rs.3,029 crore at end-March 2002 to Rs.12,638 crore at end-March 2003 and further to Rs.24,670 crore at end-March 2004. Borrowings from international markets by commercial banks rose from Rs.1,357 crore at end-March 2002 to Rs.7,208 crore at end-March 2003 and further to Rs.17,028 crore at end-March 2004.

3.12 The traditional distinction between demand and time deposits was blurred, to an extent, as fluctuations in stock market activity necessitated parking of temporarily idle funds in short-term fixed

Chart III.5: Time Deposits and Small Savings

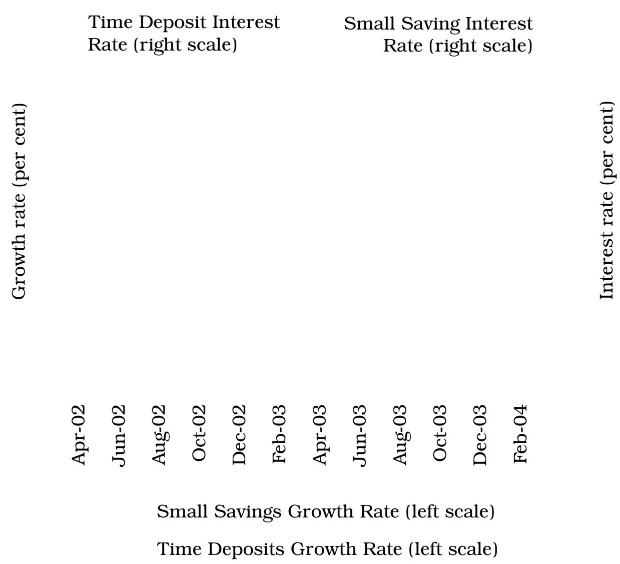


Chart III.6 : Scheduled Commercial Banks' Demand to Time Deposit Ratio

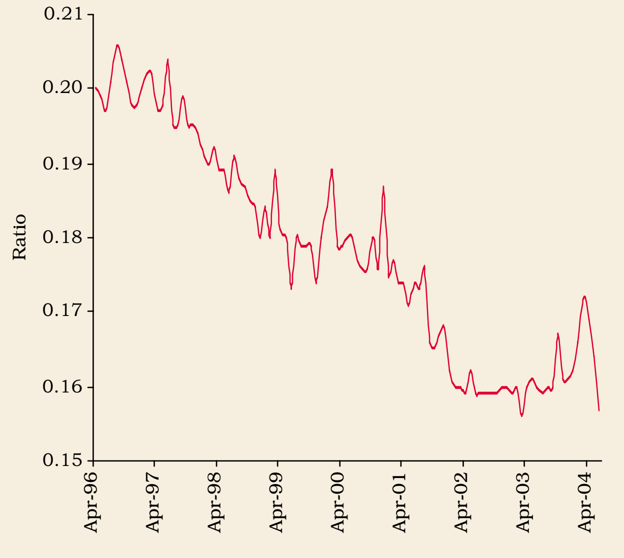
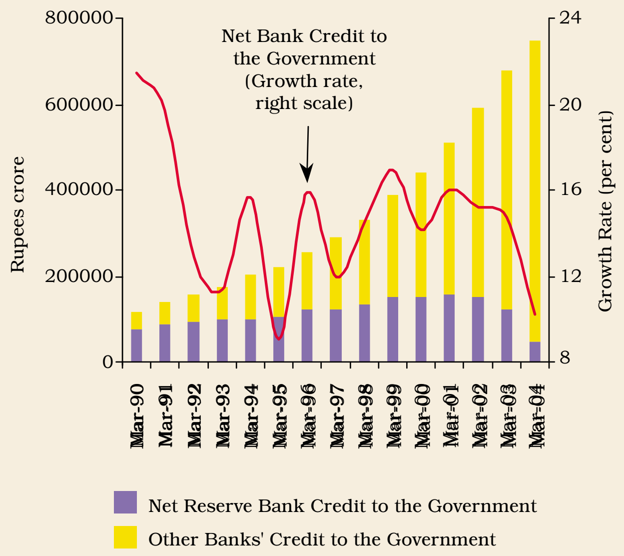


Chart III.7 : Net Bank Credit to the Government



deposits. The gradual shortening of the minimum maturity of fixed deposits in the latter half of the 1990s drove down the ratio (deseasonalised) of scheduled commercial banks' demand deposits to time deposits (adjusted for RIBs/IMDs and merger effects) (Chart III.6).

Sources of Money Supply

3.13 Changes in asset portfolios of commercial banks reflected the impact of rallies in the Government securities market, the appreciation of the exchange rate *vis-á-vis* the US dollar and the dynamics of credit demand. Domestic credit (including banks' non-SLR investments) decelerated to 11.0 per cent during 2003-04 from 13.5 per cent (adjusted for mergers) during the previous year.

3.14 Net bank credit to the Government grew at 10.2 per cent during 2003-04 – the lowest order of growth since 1994-95 – due mainly to a build-up of large cash balances by the Central Government with the Reserve Bank. Large sterilisation operations led to the share of the Reserve Bank in net bank credit to the Government dipping to a low of 5.1 per cent by February 2004 from 65.6 per cent at end-March 1990. Commercial banks continued to park surplus liquidity in gilts in response to attractive risk-free yields. This buoyed up their holdings of statutory liquidity ratio (SLR) securities to as much as 41.3 per cent of their net demand and time liabilities by end-March 2004, far in excess of the statutory requirement of 25 per cent (Chart III.7).

3.15 The growth of bank credit to the commercial sector during 2003-04 was comparable to that of the previous year. Food credit declined due to lower food stocks and sustained higher offtake. Commercial banks' non-food credit decelerated marginally for the year as a whole, although there was a significant pick-up in the latter half. Besides conventional credit, commercial banks' non-SLR investments recorded a marginal increase as higher exposures to mutual funds were largely offset by divestment of private sector corporate bonds (Table 3.5).

Table 3.5: Commercial Banks' Non-SLR Investments

(Rupees crore)

Instrument	Outstanding as at end-March	
	2004	2003
1	2	3
1. Commercial Paper	3,770	4,007
2. Units of UTI and other Mutual Funds	11,808	6,317
3. Shares issued by	9,696	10,206
3.1 Public Sector Undertakings	1,272	1,430
3.2 Private Corporate Sector	7,395	7,589
3.3 Public Financial Institutions	1,029	1,187
4. Bonds/debentures issued by	1,12,370	1,13,169
4.1 Public Sector Undertakings	48,646	46,854
4.2 Private Corporate Sector	27,903	32,973
4.3 Public Financial Institutions	30,704	28,771
4.4 Others	5,118	4,570
Total (1+2+3+4)	1,37,644	1,33,699
Memo:		
Conventional Bank Credit	8,15,728	7,07,856

Note : Excluding Regional Rural Banks.

Table 3.6: Flow of Resources from Non-banks to Corporates

(Rupees crore)

Item	2003-04	2002-03
1	2	3
1. Capital Issues* (i+ii)	2,059	642
i) Non-Government Public Ltd. Companies (a+b)	1,959	642
a) Bonds/Debentures	0	218
b) Shares	1,959	424
ii) PSUs and Government Companies	100	0
2. Euro Issues +	3,098	3,426
3. External Commercial Borrowings (ECBs) ##	15,136	-11,415
4. Issue of CPs #	2,304	2,063
5. Financial assistance extended by FIs (net) @	-1,435	-5,672
6. Total (1 to 5)	**21,162**	**-10,956**

* : Gross issuances excluding issues by banks and financial institutions. Figures are not adjusted for banks' investments in capital issues, which are not expected to be significant.

\+ : Including Global Depository Receipts (GDRs)/American Depository Receipts (ADRs) and Foreign Currency Convertible Bonds (FCCBs) other than those issues floated by banks and financial institutions.

\##: Excluding the impact of redemption of Resurgent India Bonds (RIBs).

\# : Excluding issuances by financial institutions and banks' investments in CPs.

@ : Excluding ICICI Ltd. and comprising loans and advances, equity, other investments and bills of exchange and promissory notes discounted/rediscounted. Financial institutions include IDBI, IFCI, IDFC, EXIM Bank, IIBI, SIDBI and TFCI.

Note : Data are provisional.

3.16 The flow of resources from non-banks to corporates recorded a jump during 2003-04 in sharp contrast to a decline in the previous year (Table 3.6). This was mainly due to large external commercial borrowings (ECBs) by corporates taking advantage of a favourable interest rate differential between domestic and international markets and an appreciating domestic currency.

3.17 In the deployment pattern of commercial bank credit, the priority sector continued to be the largest recipient, as in earlier years (Table 3.7 and Appendix Table III.8). This was essentially on account of substantially higher offtake by the 'other priority' segment, representing primarily small housing loans up to Rs.10 lakh. This segment benefited from low interest rates, fiscal incentives and an upsurge in housing demand. Large housing loans (above Rs.10 lakh) continued to record strong growth. Credit to medium and large industries, NBFCs and real estate recorded lower growth. This reflected greater recourse by corporates to ECBs and to internal generation of funds following significant improvement in profitability throughout 2002-03 and 2003-04. Bank credit to industry, however, recorded a pick-up since September 2003 with the jump in February and March 2004 accounting for about 75 per cent of the fiscal year offtake.

Table 3.7: Sectoral Deployment of Non-food Gross Bank Credit

(Rupees crore)

Sector	2003-04*		2002-03@	
	Absolute	Per cent	Absolute	Per cent
1	2	3	4	5
1. Priority sector	52,225	24.7	28,540	16.3
2. Industry (Medium and Large)	12,042	5.1	28,011	16.3
3. Housing	15,394	42.1	12,308	55.1
4. Non-banking financial companies	2,675	18.9	4,399	45.6
5. Wholesale trade	2,289	10.1	1,939	9.5
6. Export Credit	8,485	17.2	6,424	14.9

* : Includes the impact of the mergers since May 3, 2002.

@ : Excludes the impact of the mergers since May 3, 2002.

Note : Data are provisional and relate to select scheduled commercial banks which account for about 90 per cent of credit by all scheduled commercial banks.

3.18 An industry-wise distribution of credit shows that the lower expansion of credit was due to a decline in offtake by industries such as mining, iron and steel, other metal and metal products, chemicals, petroleum, fertilisers, cement, and rubber (Appendix Table III.9). This was reinforced by a deceleration in credit to cotton textiles, drugs and pharmaceuticals and computer software. On the other hand, credit to infrastructure industries, especially roads and ports, power and telecommunications, increased substantially. Some industries such as electricity, food processing, jute textiles, sugar, tea, tobacco, leather, gems and jewellery and construction also recorded higher bank credit offtake.

3.19 The pattern of credit behaviour in the Indian economy has been undergoing structural shifts as a result of newer avenues of resource mobilisation as well as new areas of deployment of assets. Demand for credit by corporates is becoming increasingly sensitive to cost considerations, availability of internal funds and international capital market developments (Box III.1). On the supply side, banks are beginning to optimise portfolios by arbitraging between the rates of return on advances in domestic currency and in foreign currency to residents as well as treasury operations in Government securities and in foreign assets. Thus, there is a growing substitution of domestic and foreign avenues of resource mobilisation and credit deployment.

Box III.1

Corporate Profitability and Non-food Credit Offtake

Indian industry has historically relied largely on external sources of funds comprising mainly borrowings from banks and finance institutions (FIs). With the decline in the importance of FIs in recent years, corporates were expected to increase their recourse to banks. During 2003-04, however, bank credit to industry decelerated to 5.9 per cent from 13.4 per cent in 2002-03 even as industrial growth picked up to 6.9 per cent from 5.7 per cent.

An analysis of data reveals that the decline in credit offtake by industry during 2003-04 was mainly due to the increased recourse to international capital markets by way of external commercial borrowings (ECBs), depository receipts and convertible bonds. Furthermore, since 2001-02, internal generation of funds has increasingly substituted funds from external sources. During 2001-02, the share of internal sources of funds of corporates (select large public limited companies) turned out to be 68.8 per cent of their total financing requirement. This took the form of provision for taxation and other current provisions reserves and surplus. Provision for taxation declined significantly in 2002-03, while reserves and surplus increased. Net corporate profits averaged at 53.7 per cent during 2003-04, reflecting the ongoing reduction in interest expenses. Industries which earned large profits such as petroleum, engineering, chemicals and iron and steel reduced their dependence on bank credit.

In India, the importance of bank finance to industry is significant at about 67.0 per cent of industrial GDP. As the industrial recovery gains momentum and project investment activity picks up, the potential demand for bank credit could rise along with an increasing resource mobilisation from international capital markets.

References

1. Calza, A., Gartner, C. and Sousa, J. (2001), “Modelling the Demand for Loans to the Private Sector in the Euro Area”, *European Central Bank Working Paper,* No.40.
2. Reserve Bank of India (2004), “Finance of Large Public Limited Companies, 2002-03”, *Reserve Bank of India Bulletin,* April.

Developments during 2004-05

3.20 The expansion of money supply during 2004-05 (up to August 6, 2004) continued to be driven by a sustained increase in the monetary base (Table 3.8). Currency expansion remained strong, reflecting a pick-up in activity across the economy. Demand deposits, in particular, recorded a strong growth, reflecting a sustained pick-up in scheduled commercial banks' non-food credit. Food credit expanded by Rs. 6,481 crore during 2004-05 (up to August 6, 2004) in sharp contrast to the decline of Rs. 6,228 crore in the corresponding period of the previous year. Net bank credit to the Government decelerated sharply following the significant slowdown in the Centre's market borrowing programme.

Table 3.8: Money Supply – As on August 6, 2004

(Rupees crore)

Item	Year-on-year Variation			
	As on August 6, 2004		As on August 8, 2003	
	Absolute	Per cent	Absolute	Per cent
1	2	3	4	5
Broad Money (M_3)	**2,84,440**	**15.7**	**1,89,622**	**11.7**
Major Components				
Currency with the Public	38,273	13.3	32,378	12.7
Aggregate Deposits	2,45,085	16.1	1,57,200	11.5
Major Sources				
Net Bank Credit to the Government	42,277	5.9	72,172	11.1
of which:				
By the Reserve Bank	-79,394	-92.6	-68,421	-44.4
Bank Credit to Commercial Sector	1,69,234	18.7	85,816	10.5
of which:				
Scheduled Commercial Banks' Non-food Credit	1,63,272	23.8	91,807	15.4
Net Foreign Assets (NFA) of the Banking Sector	1,62,349	37.9	84,592	24.6

Commercial Banking Survey

3.21 Liquidity in the banking system surged in the first quarter of 2003-04, essentially because of the build-up of deposits by banks to meet year-end targets for 2002-03 (Table 3.9 and Appendix Tables III.6 and 7). Time deposit growth began to slow down as funds moved from fixed deposits of households to mutual funds as the capital market revived. This, in turn, led to a sharp increase in current accounts maintained by mutual funds. Credit to the Government picked up with the launching of the market borrowing programme of the Centre. On the other hand, food credit slumped due to subdued procurement operations and lower carrying costs associated with diminishing food stocks. Non-food credit slowed down with corporates switching away from bank finance, as alluded to earlier. Contemporaneously, banks increased lending to primary dealers who are turning out to be the main borrowers in the call money market. Banks drew down their *nostro* balances and borrowed overseas to fund foreign currency loans to residents. Net outflows were recorded under the FCNR(B) scheme as the alignment

Table 3.9: Operations of Scheduled Commercial Banks

(Rupees crore)

Item	Outstanding as on March 19, 2004	2003-04 Q4	2003-04 Q3	2003-04 Q2	2003-04 Q1	2002-03 Q4	2002-03 Q3	2002-03 Q2	2002-03 Q1
1	2	3	4	5	6	7	8	9	10
Components									
Aggregate Deposits of Residents	**14,29,080**	**82,398**	**60,154**	**32,455**	**65,724**	**23,773**	**37,518**	**32,201**	**52,675**
Demand Deposits	2,25,022	30,822	18,496	-5,950	11,366	5,405	11,654	-4,535	4,717
Time Deposits	12,04,058	51,577	41,658	38,405	54,359	18,368	25,864	36,735	47,958
Call/Term Funding from Financial Institutions	**24,670**	**2,431**	**4,822**	**2,253**	**2,526**	**2,142**	**227**	**792**	**6,448**
Sources									
Credit to the Government	**6,54,758**	**32,133**	**18,342**	**45,333**	**35,534**	**23,798**	**22,680**	**18,716**	**47,047**
Credit to Commercial Sector	**1,002,479**	**54,800**	**40,606**	**5,635**	**10,400**	**27,881**	**39,481**	**20,342**	**22,806**
Food Credit	35,961	-391	-1,113	-12,601	586	-2,468	-1,415	-7,645	7,030
Non-food Credit	8,04,824	57,819	48,992	15,186	3,091	39,439	32,541	19,945	7,522
Credit to Primary Dealers	1,946	-2,276	-4,817	-610	5,557	-5,886	959	5,837	2,854
Investments in Other Approved Securities	22,830	-928	50	-407	-13	-306	-965	-459	-1,233
Other Investments (in non-SLR Securities)	1,36,918	577	-2,505	4,068	1,178	-2,898	8,361	2,664	6,633
Net Foreign Currency Assets of Commercial Banks	**-58,531**	**196**	**6,815**	**1,855**	**1,235**	**-9,120**	**-8,992**	**-15,136**	**2,748**
Foreign Currency Assets	33,833	3,931	-4,066	3,264	-377	-5,345	-7,955	-14,412	4,718
Non-resident Foreign Currency Repatriable Fixed Deposits	75,336	122	-13,916	-1,273	-2,103	-403	-265	669	1,655
Overseas Foreign Currency Borrowings	17,028	3,613	3,035	2,682	491	4,178	1,302	55	315
Net Bank Reserves	**76,895**	**-1,199**	**6,394**	**-14,272**	**20,149**	**-5,700**	**-1,619**	**11,055**	**-2,943**
Capital Account	**1,03,108**	**581**	**2,464**	**-1,826**	**15,349**	**1,625**	**-1,815**	**-742**	**15,152**
Other Items (net)	**1,18,743**	**520**	**4,718**	**5,669**	**-16,283**	**9,318**	**15,619**	**2,726**	**-4,617**
Memo Items:									
Foreign Currency Loans to Residents	43,485	2,970	2,007	2,125	1,167	-4,354	5,807	11,069	-179
Release of Resources through change in CRR	–	0	0	0	3,500	0	3,363	0	6,000
Net Open Market Sales to Commercial Banks	–	445	9,334	8,250	4,266 *	7,339	12,803	13,228	3,131 *

*** :** Variation over March 31.

Note : 1. Data relate to last reporting Friday for each quarter.
2. Deposits have been adjusted for the full impact of mergers, while credit has been adjusted for the initial impact of the same during May 2002 - April 2003.

of interest rates with international rates took effect. With subdued credit demand from the commercial sector and greater access to relatively cheaper overseas funds, surplus liquidity led to an expansion of bank reserves in the first quarter of 2003-04, despite the cut in CRR in mid-June 2003.

3.22 Deposit growth recorded a seasonal slowdown in the second quarter, with outflows from demand deposits. Banks' gilt portfolios rose sharply as the borrowing programme gathered momentum and the Reserve Bank engaged in sizeable open market sales. Repayments of food credit and relatively weak demand from industry kept credit to the commercial sector at moderate levels. Subdued credit offtake led to banks' expanding their exposure to the commercial sector through non-SLR investments. *Nostro* balances were built up by some banks in the second quarter in anticipation of RIB redemption on October 1, 2003. Banks' overseas borrowings picked up strongly in consonance with the growth of foreign currency loans to residents. The FCNR(B) scheme continued to record outflows. Net bank reserves declined as the surplus liquidity was absorbed by LAF auctions.

3.23 Deposit growth picked up in the third quarter in consonance with the recovery in real economic activity. The spurt in demand deposits was seasonal and associated with the parking of surplus liquidity by mutual funds resulting from divestment of non-SLR paper. Banks' investments in non-SLR securities also contracted in the third quarter, reflecting market uncertainty pertaining to non-SLR guidelines. Time deposits regained some momentum as the capital market underwent corrections. Credit to the Central Government ebbed due to scaling down of its borrowing programme. The upturn in non-food credit, which set in during August, firmed up in the third quarter. Primary dealers repaid bank credit leading to the accumulation of substantial cash balances with the Reserve Bank. Banks unwound *nostro* positions as most of the redemption proceeds of the RIBs were switched into domestic currency/non-resident deposit schemes. Overseas borrowings by banks rose in response to liberalisation in borrowing limits relating to Tier-I capital. Bank reserves rose significantly, driven by the surplus liquidity resulting from the slack in demand for funds by the Government.

3.24 There was a substantial rise in demand deposits during the fourth quarter due, *inter alia,* to higher growth in non-food credit due to year-end balance sheet considerations, inflows on account of disinvestment in ONGC, parking of funds by foreign institutional investors (FIIs) and substantial inflows under the exchange earners' foreign currency (EEFC) accounts which is also reflected in an accumulation of banks' foreign assets. The spurt in time deposits in the fourth quarter partly reflected a switch back of funds to bank deposits from mutual funds by households as well as a shift by mutual funds away from equity investments prompted by sell-offs in the stock market. The slowdown in call/term borrowing from financial institutions reflected a further scaling down of non-bank lendings in the call/notice money market. The rise in banks' investments in Government securities in the last quarter reflected repo operations conducted under the LAF. The growth of foreign currency loans to residents remained steady in all quarters. The large accretions in the capital account of banks reflected their building up of investment fluctuation reserves as well as adherence to prudential guidelines relating to the capital adequacy ratio.

3.25 Deposit mobilisation by commercial banks slowed down in the first quarter of 2004-05, reflecting the unwinding of demand deposits built up in the previous quarter following outflows on account of transfer of the proceeds of ONGC disinvestment to the Government account, drawdown of EEFC accounts and FII outflows. Food credit offtake rose sharply on account of higher procurement operations in contrast to the corresponding quarter of the previous year. Non-food credit, in particular, recorded a large increase. Although the net market borrowing programme of the Government was muted, banks invested heavily in auctions held under the MSS. In contrast to the corresponding quarter of the previous year, net foreign assets of the banking system recorded a decline mainly on account of a drawdown of *nostro* balances as well as an accretion to FCNR (B) deposits and higher overseas borrowings.

PRICE SITUATION

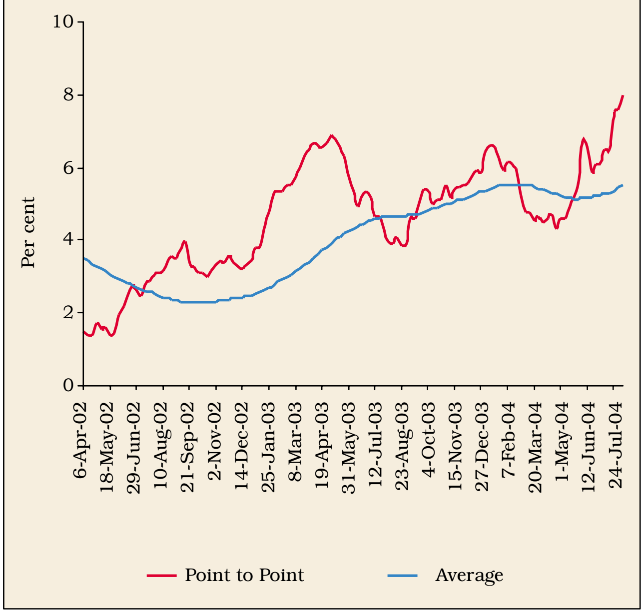
3.26 Inflation in India generally remained stable during 2003-04, although rising commodity prices led to episodes of pressures. Agricultural commodity prices were subdued due to favourable supply conditions in the market following the normal monsoon. The pick-up in domestic economic activity and exports led to an imbalance between domestic demand and supply of key commodities such as metals, cotton and fuel. This contributed to the hardening of their prices in line with international price movements. Owing to competitive pressures, however, a part of the higher input costs resulting from the rise in commodity prices seems to have been absorbed by corporates in their margins. Consequently, the rising commodity prices were not reflected fully in overall inflation. Accordingly, consumer price inflation remained benign in 2003-04, facilitated in addition, by stable housing and services prices.

Wholesale Price Inflation

3.27 Headline inflation, measured by year-on-year (y-o-y) changes in the wholesale price index (WPI), peaked at 6.9 per cent in the first week of May 2003, as transport disruptions and upward revisions in electricity prices offset the effect of cuts in petroleum product prices. Inflation receded thereafter to a trough of 3.8 per cent by August 23, 2003 due to declines in the prices of minerals oil, fruits, oilseeds, oil cakes and chemicals. Incipient inflationary pressures began to emerge when prices of iron and steel, cotton and fuel started firming up in line with international price movements. Prices of vegetables and sugar also rose during this period due to supply-side pressures from persistent localised drought conditions as well as upward revisions in the statutory minimum prices of sugarcane. By January 10, 2004 inflation had reached 6.6 per cent. About a fifth of this rise in inflation was caused by successive hikes in domestic petrol and diesel prices between December 16, 2003 and January 1, 2004. With the delayed seasonal fall in fruits and vegetable prices, a decline in prices of eggs and poultry chicken on fears of *avian influenza* and base effects of oil price hikes in February and March 2003, inflation retreated to 4.6 per cent by the end of the year.

3.28 Annual WPI inflation, excluding the administered and partially decontrolled items (electricity, coal mining, mineral oils and urea-N-content) was, at 5.4 per cent, above the headline rate in 2003-04. Inflation, measured by annual average WPI, was 5.4 per cent in 2003-04 as compared with 3.4 per cent a year ago (Chart III.8).

Chart III.8 : Wholesale Price Inflation



Components of Inflation

3.29 The key movers of headline inflation in 2003-04 were iron and steel, cotton textiles, fuel, sugar and milk. These items, which have a weight of 30 per cent in the overall WPI index, accounted for 65 per cent of the headline inflation.

3.30 Prices of manufactured products rose sharply during the second half of 2003-04 on account of iron and steel, cotton textiles and food products which responded to the spurt in global commodity prices. The contribution of the manufactured products group to inflation almost doubled over the year (Table 3.10 and Appendix Tables III.11 and 12).

Table 3.10: Annual WPI Inflation by Component

(Base: 1993-94=100)

(Per cent)

Major group / Item	Weight	Annual Inflation Rate (Year-on-year)			Weighted Contribution to Annual Inflation		
		2003-04	2002-03	2001-02	2003-04	2002-03	2001-02
1	2	3	4	5	6	7	8
All Commodities	**100.0**	**4.6**	**6.5**	**1.6**	**100.0**	**100.0**	**100.0**
1. Primary Articles	**22.0**	**1.6**	**6.1**	**3.9**	**8.0**	**21.6**	**53.4**
Food Articles	15.4	0.2	0.8	5.2	0.6	2.2	51.5
i. Cereals	4.4	-0.3	4.0	0.8	-0.3	2.9	2.4
ii. Pulses	0.6	-2.6	0.3	-3.3	-0.3	0.0	-1.4
iii. Vegetables	1.5	2.8	-15.7	23.4	0.6	-3.0	14.8
iv. Fruits	1.5	-8.6	7.6	9.5	-3.9	2.4	11.2
v. Milk	4.4	8.4	0.6	4.7	7.9	0.5	12.9
vi. Eggs, Fish and Meat	2.2	-6.5	-4.0	9.3	-3.4	-1.7	14.3
Non-food Articles	6.1	4.1	22.1	0.6	5.8	19.3	2.1
i. Raw Cotton	1.4	12.3	34.3	-21.3	3.4	5.4	-17.3
ii. Oilseeds	2.7	-1.2	30.0	6.8	-0.7	10.6	9.0
ii. Sugarcane	1.3	6.5	11.5	6.2	2.3	2.8	5.7
2. Fuel, Power, Light and Lubricants	**14.2**	**2.5**	**10.8**	**3.9**	**11.6**	**33.9**	**47.1**
i. Mineral oils	7.0	0.0	18.4	1.2	-0.1	29.7	7.8
ii. Electricity	5.5	4.9	3.4	9.2	8.1	4.2	41.3
iii. Coal Mining	1.8	9.2	0.0	-1.9	3.7	0.0	-2.4
3. Manufactured Products	**63.8**	**6.7**	**5.1**	**0.0**	**80.5**	**44.3**	**0.0**
i. Food Products	11.5	9.7	8.7	0.3	22.2	14.0	1.8
of which: Sugar	3.6	16.9	-15.0	-3.8	8.7	-7.0	-7.4
Edible Oils	2.8	6.6	27.4	12.5	3.4	8.5	14.0
Oil Cakes	1.4	5.0	40.3	15.0	2.0	8.8	11.5
ii. Cotton Textiles	4.2	15.6	8.3	-6.7	12.8	4.8	-16.7
iii. Man-made Fibre	4.4	-0.4	17.4	-5.0	-0.2	5.8	-7.1
iv. Chemicals and Chemical Products	11.9	0.1	4.2	2.5	0.3	8.2	19.3
of which: Fertilisers	3.7	-0.1	2.1	3.6	-0.1	1.2	8.1
v. Basic Metals, Alloys and Metal products	8.3	22.1	6.6	-0.9	34.4	7.3	-4.2
of which: Iron and Steel	3.6	34.6	9.2	0.0	23.6	4.4	0.0
vi. Non-Metallic Mineral Products	2.5	3.0	3.3	-2.8	1.4	1.1	-4.0
of which: Cement	1.7	1.3	1.1	-4.7	0.4	0.3	-4.7
vii. Machinery and Machine Tools	8.4	3.1	0.5	2.0	4.3	0.5	8.0
viii. Transport Equipment and Parts	4.3	1.4	-0.9	1.3	1.1	-0.6	3.1
Food Items (composite)	**26.9**	**4.0**	**3.9**	**3.3**	**22.8**	**16.2**	**53.3**
WPI excluding Food	**73.1**	**4.9**	**7.5**	**1.0**	**77.2**	**83.8**	**46.7**
WPI excluding Fuel	**85.8**	**5.2**	**5.4**	**1.1**	**88.4**	**66.1**	**52.9**
Memo Items:							
GDP Deflator		3.7	3.5	3.9			
Average WPI Inflation		5.4	3.4	3.6			
Average CPI Inflation (IW)		3.9	4.0	4.3			
Services in CPI-IW@ (year-on-year)	16.4	3.2	5.3	4.9	15.4	21.5	15.6
Housing in CPI-IW (year-on-year)	8.7	3.9	5.4	12.9	11.2	13.2	23.4

CPI-IW : Consumer Price Index for Industrial Workers (Base : 1982 = 100).

@ : Miscellaneous group in the Consumer Price Index for Industrial Workers.

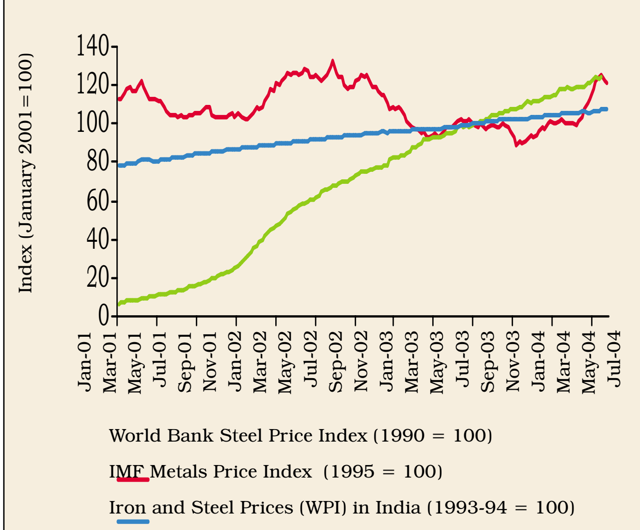


Chart III.9 : Iron and Steel Prices

Note: Domestic and international prices normalised to January 2001 = 100.

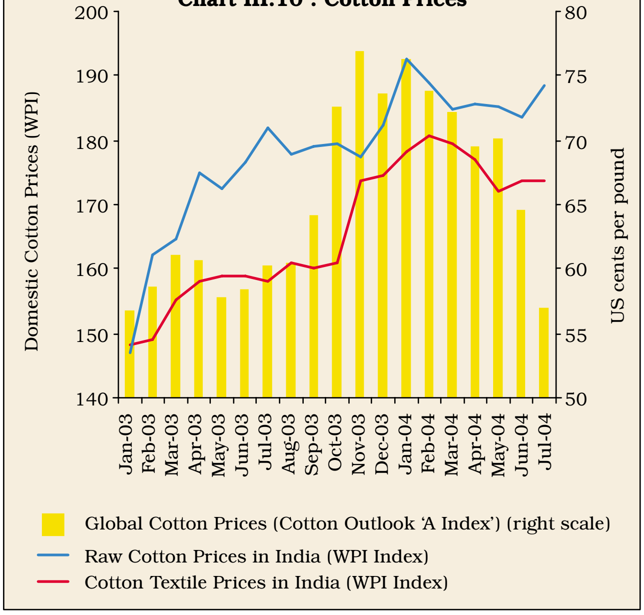


Chart III.10 : Cotton Prices

3.31 Domestic iron and steel prices increased by 34.6 per cent in 2003-04 and contributed 24 per cent of the headline inflation. Firming up of domestic iron and steel prices was associated with the improvement in domestic industrial activity and exports, rising input costs especially of scrap and cokes and international prices which were driven up by demand generated by heightened economic activity in China (Chart III.9). Fiscal measures comprising cuts in customs and excise duties on inputs as well as finished products, supported by freezing of benefits under the Duty Entitlement Pass Book and duty drawback schemes helped contain pressures from domestic iron and steel prices on overall inflation.

3.32 Cotton textile prices increased mainly on account of a rise in domestic raw cotton prices. Despite a satisfactory domestic cotton crop, raw cotton prices remained firm in consonance with international price movements (Chart III.10). Global cotton prices increased during 2003 mainly due to higher Chinese demand and low stocks. Global cotton stocks were projected at 33.5 per cent of global consumption, the lowest since 1993-94.

3.33 Domestic petroleum, oil and lubricants (POL) prices have, in general, become relatively more responsive to changes in international crude oil prices after dismantling of the administered pricing mechanism (APM) in April 2002 (Chart III.11). International crude oil prices increased by 5.6 per cent from US $ 27.6 per barrel in 2002-03 to US $ 29.1 per barrel in 2003-04, ruling well above the upper ceiling of the Organisation of Petroleum Exporting Countries (OPEC) band. Domestic mineral oils prices largely mirrored movements in international crude prices in the first three quarters of 2003-04, with some cushion provided by the appreciation of the rupee against the US dollar. In the last quarter of 2003-04, domestic diesel and petrol prices were not adjusted even as international crude prices hardened due to depleting inventories in advanced economies, geo-political uncertainties and concerns about production cut decisions by the OPEC. International crude prices soared to new peaks in

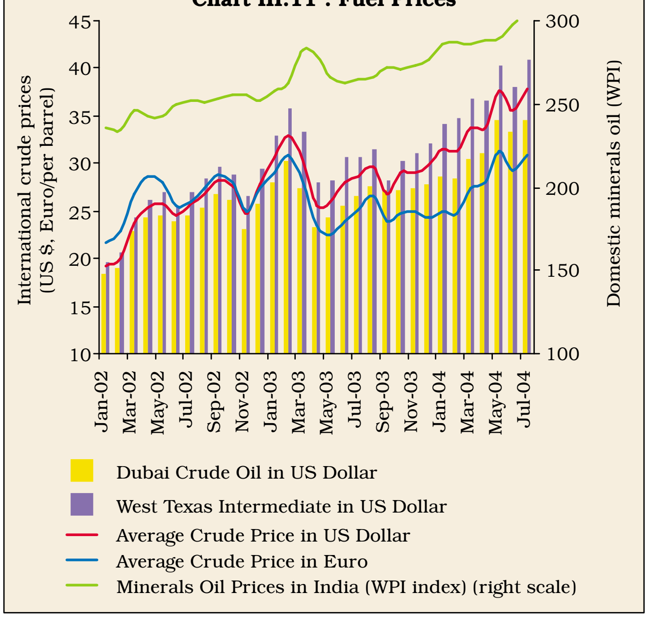


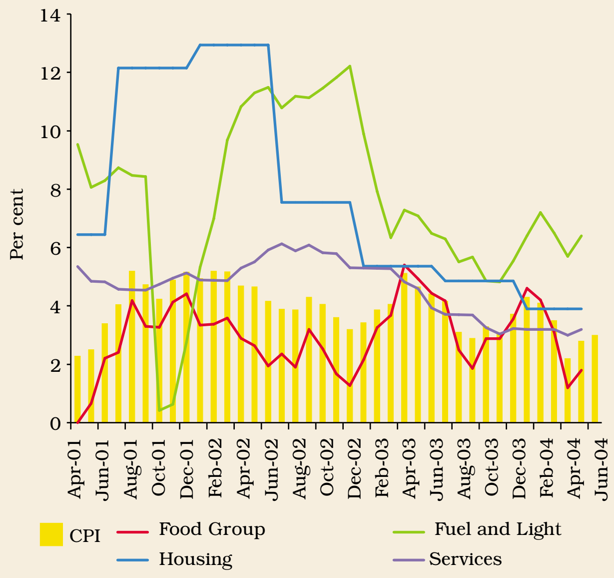
Chart III.11 : Fuel Prices

August 2004 due to robust growth in demand from the US and China, distribution bottlenecks in major consuming regions limiting gasoline supplies and heightened geo-political tensions in West Asia. This uptrend was temporarily arrested by the OPEC's decision on June 3, 2004 to raise its output target by 8.5 per cent, *i.e.*, 2 million barrels a day (mbd) to 25.5 mbd effective July 1 and by another 5 lakh barrels to 26 mbd effective August 1, 2004. Domestic POL prices were revised upwards on June 15 and August 1, 2004.

Consumer Price Inflation

3.34 Consumer price Inflation, measured by year-on-year variation in the consumer price index for industrial workers (CPI-IW), eased during the year to 3.5 per cent, reflecting the effects of the bumper agricultural production and negligible/lower weightage of the key movers of WPI inflation - iron and steel and fuel items - in the CPI basket (Appendix Table III.13). Disaggregated commodity price movements within the CPI-IW basket indicate that lower prices of oil and fats, housing and services (proxied by the broad miscellaneous group) led to the ebbing of inflation (Chart III.12). As against booming housing prices in developed countries, domestic housing prices remained moderate. Services prices remained flat. On an annual average basis, CPI inflation in 2003-04 remained below its level in the previous year.

Chart III.12 : Consumer Price Inflation (Year-on-Year)



Global Inflation Environment

3.35 Persisting output gaps and weak consumer demand enabled most central banks to continue supporting recovery through accommodative monetary policies in 2003. Deflationary concerns receded on the back of continued policy support to the sustenance of recovery, rebound in inter-regional trade and upturn in financial markets amidst easy liquidity. Inflationary expectations began to resurface with signs of global recovery gradually becoming stronger and widespread from the last quarter of 2003. In early 2004, many central banks began to sense risks to price stability emanating from rising commodity and fuel prices, booming asset prices especially housing, shrinking excess capacities and tightening labour market conditions as a result of strengthening of economic activity. Consequently, monetary authorities began sensitising the markets to exit strategies from the accommodative monetary policy stance as growth picks up (Table 3.11).

Table 3.11: Global Inflation Indicators

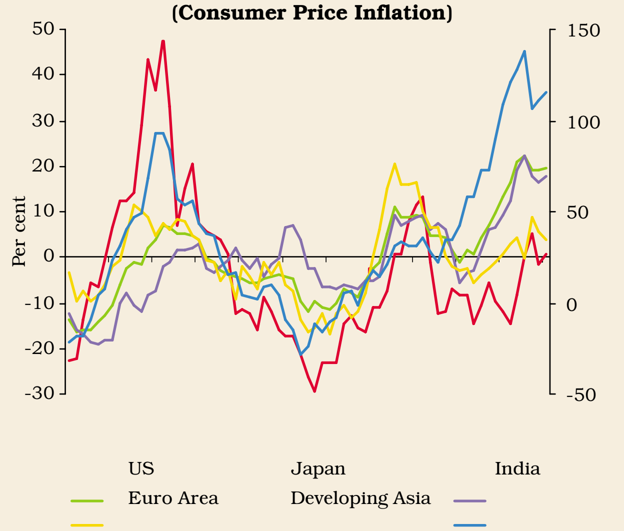
(Per cent)

Country/ Region	Key Policy Rate/ Bank Reserves Target	Changes	2003 GDP growth	2003 Inflation
1	2	3	4	5
US	Target Federal Funds Rate	From 1.25 to 1.0 (June 2003) to 1.25 (June 2004) to 1.5 (August 2004)	3.1	2.3
UK	Repo Rate	From 4.0 to 3.75 (February 2003) to 3.5 (July 2003) to 3.75 (November 2003) to 4.0 (February 2004) to 4.25 (May 2004) to 4.50 (June 2004) to 4.75 (August 2004)	2.3	1.4
Euro Area	Interest Rates on Deposit Facility Main Refinancing Operations Marginal Lending Facility	From 1.75, 2.75, 3.75 to 1.50, 2.50, 3.50 (March 2003) to 1.0, 2.0, 3.0 (June 2003)	0.4	2.1
Japan	Target Balance of Current Account (trillion Yen)	From 15-20 to 22-27 (April 2003) to 27-30 (May 2003) to 27-32 (October 2003) to 30-35 (January 2004)	2.7	-0.2

Source : IMF and official websites of respective central banks.

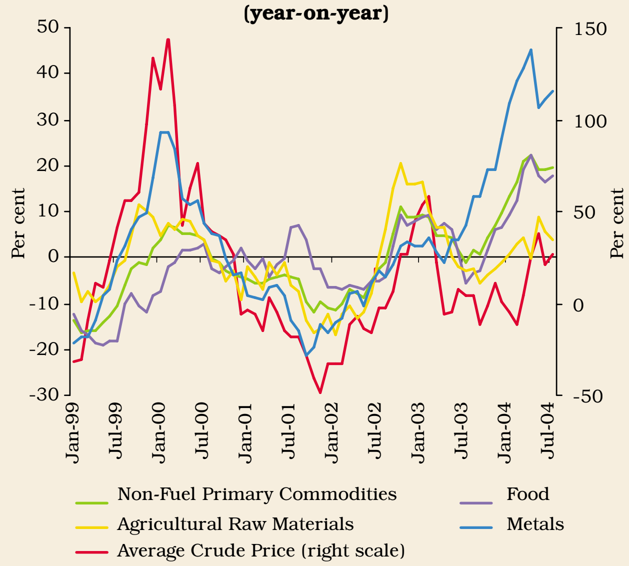
3.36 Consumer price inflation remained subdued in many parts of the world in 2003 and in the first quarter of 2004. In developed countries, inflation stayed below two per cent for the second year in succession, while it remained close to six per cent in developing economies. The downside risks of deflation receded with the strengthening of the global recovery during the year. In the US, a decline in consumer inflation started in the second half of 2003 driven by productivity gains. The growing wedge between consumer prices and producer prices in the US due to hardening of commodity prices was, to an extent, due to absorption of the rise in input costs, given the significant slack available in capacity utilisation. Monetary policy retained its accommodative stance in support of the recovery with short-term interest rates ruling at 30 year lows. In the United Kingdom, inflation remained well below the Bank of England's target of 2.0 per cent, although the sharp increase in house prices provoked pre-emptive tightening of monetary policy. In the euro area, inflation stayed close to the European Central Bank's target of 2.0 per cent as pressures emanating from higher oil and food prices were offset by the appreciation of the euro. Deflation continued to haunt Japan during 2003 despite stronger growth in the second half of the year and persistence by the Bank of Japan with quantitative easing. In developing Asia, consumer prices remained stable amidst congenial conditions

Chart III.13 : Global Inflation Environment (Consumer Price Inflation)



Note :Data for 2004 are IMF projections.
Source :World Economic Outlook, IMF, April 2004.

Chart III.14 : International Commodity Price Movements (year-on-year)



Source :International Monetary Fund.

created by a pick-up in domestic demand and export growth (Chart III.13). In China, consumer prices rose moderately on account of higher food and metal prices. Countries in Africa and the Western Hemisphere, on the other hand, continued to face relatively high inflation risks.

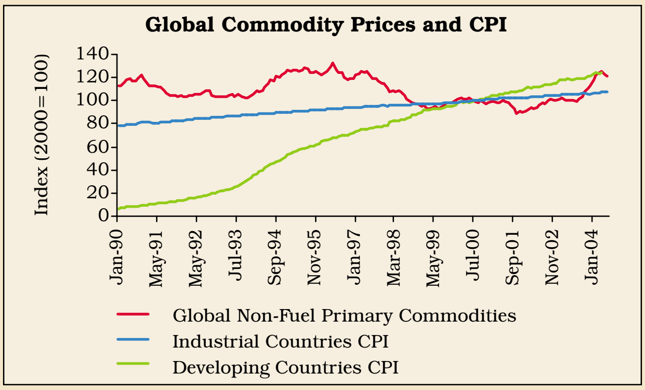
3.37 International commodity prices, especially of intermediate materials, surged in 2003 posing concerns about incipient inflationary pressures. International crude oil prices rose sharply due to slower than expected resumption of oil production in Iraq, increased demand associated with the rebound in economic activity, low levels of inventory in industrial countries especially in the US, production cuts by the OPEC and speculative pressures due to geo-political uncertainties. Global primary commodity prices increased by over 13 per cent in 2003. Non-fuel commodity prices surged, mainly reflecting increased Chinese demand for metals and cotton, crop failures in several parts as well as the depreciation of the US dollar - the currency in which commodity prices are generally invoiced (Chart III.14). The sharp increases in commodity prices were not transmitted into consumer prices in 2003-04 (Box III.2). The upward movement in consumer price inflation in 2004-05, however, appears to have been driven by commodity prices, especially fuel prices.

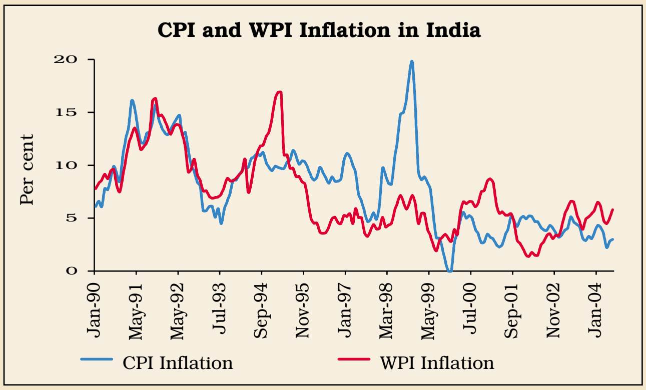
Box III.2
Consumer Price Inflation and Commodity Prices: What's Going On?

Up to the early 1980s, commodity prices were regarded as leading indicators of inflation. Since commodity prices are set in competitive market conditions, they tend to be more responsive than the general price level to both demand and supply shocks. In recent years, however, a divergence has been observed between commodity prices and consumer prices. In 2003, the wedge increased raising concerns about 'pipeline price pressures' gradually building up (Chart).

management; (iii) administered pricing of certain commodities in the WPI basket; and (iv) non-inclusion of services and housing in the WPI basket. The divergence between the CPI and WPI in India during 2003-04 was mainly due to the sharp rise in iron and steel and fuel prices which were key movers of WPI inflation, but had lower weightage in the CPI basket. Also, food prices in 2003-04 did not increase at the retail level as much as at the wholesale level, reflecting prudent supply management.

Chart : Commodity and Consumer Prices





The co-existence of high commodity prices and low inflation is attributed to a number of factors such as (a) the declining share of commodities in the overall cost of final goods and services; (b) the continuing slack in resource utilisation suggesting weakness in demand; and (c) producers' responses reflecting a preference for absorbing the costs on account of higher commodity prices under competitive pressures rather than passing on the burden to consumers. Producers benefited from productivity gains which resulted in lower unit labour costs. The wedge also reflects one-time shifts in product prices resulting from shocks to specific commodities since capacity utilisation in many industries remained slack indicating continuing output gaps. The growing role of prices of services and tradables in overall inflation is also at work.

In India, the wedge between CPI inflation and WPI inflation, in general, could be attributed to (i) the divergence in the composition of the two commodity baskets; (ii) supply

Incidentally, food prices in the CPI basket also have a higher weight of 57 per cent as against 27 per cent in the WPI basket. Besides, competitive pressures as well as the increasing role of imports have also been important factors in creating a divergence between wholesale and consumer price inflation in India. An examination of the structural relationship between WPI and CPI-IW shows that there are leads and lags during certain phases between inflation rates of CPI-IW and WPI, which get evened out over a long time span.

References

1. Furlong, Fred and Robert Ingenito (1996), "Commodity Prices and Inflation", *Federal Reserve Bank of San Francisco Economic Review*, No. 2.
2. International Monetary Fund (2004), *World Economic Outlook*, April.
3. Reserve Bank of India (1997), *Annual Report*, 1996 -97.

Asset Prices and Inflation

3.38 Rising asset prices, especially in housing, prompted pre-emptive tightening of monetary policy in the UK, Australia and New Zealand since the latter half of 2003. With the balance of risks shifting to the upside, monetary authorities have begun sensitising markets to the inevitability of some monetary tightening. In this context, the role of asset prices in the formulation of monetary policy has surfaced once again (Box III.3). During 2003-04, movements in equity and gold prices in India indicated a firming up of inflation expectations, partly offset by exchange rate appreciation and relatively stable housing prices.

Box III.3
Inflation and Asset Prices Revisited

The focus of central banks on asset market developments has increased in the aftermath of liberalisation of financial markets since the 1980s. Asset prices include the prices of financial assets, *viz.*, bonds, equities, derivatives and non-financial assets, including gold and real estate. The volatility associated with asset prices has led to concerns that large changes in asset prices might disrupt economic activity and endanger price stability as well as financial stability. Bursting of asset bubbles and consequent macro imbalances can turn a mild downturn into deflation, as was observed in Japan. It is argued that a correct measure of inflation should include asset prices because they reflect the current money prices of claims on future as well as current consumption.

The conventional wisdom is that central banks should ignore swings in asset prices. This is based on the belief that it is impossible to disentangle that portion of asset price movements which is related to fundamentals from that which is related to market idiosyncrasies. Asset prices would be of interest only to the extent that they provide useful information about the state of the economy. Adjustment of interest rates in response to asset price misalignments - even when inflation remains on track - enables central banks to reduce the long-term volatility of both inflation and output. A modest rise in interest rates above the level required to keep inflation on track would curb borrowing and over investment.

The empirical evidence indicates that the effects of asset price changes on monetary policy are transmitted through balance sheets of households, firms and financial intermediaries. Deteriorating balance sheets and reduced credit flows operate primarily on aggregate demand in the short-run, although in the long run they may also affect aggregate supply by inhibiting capital formation and reducing working capital. Asset prices could be used in monetary policy formulation in two ways, *viz.*, (i) they can be a part of the objectives of monetary policy (*i.e.*, built into the price index), and (ii) they can be treated as information variables (*i.e.*, form an element in the policy 'reaction function'). Adjusting monetary policy in the light of information on asset prices can improve macroeconomic outcomes even in countries where the central bank is following an inflation targeting strategy. Adjusting interest rates or other monetary policy instruments to asset price movements will not be appropriate in all circumstances, at least not in the context of movement in asset prices that reflect changes in the underlying fundamentals. Monetary policy could, however, make effective use of information from asset markets and offset adverse effects on the general economy flowing from asset price changes.

Recent empirical work in the Indian context provides weak evidence of asset prices affecting inflation. Among the asset prices, only stock prices appear to have information content about inflation expectations in the economy, while other asset prices, such as gold and exchange rates do not appear to contain lead information content on commodity price inflation.

References

1. Alchian, A. and Klein, L.R. (1973), "On Correct Measure of Inflation", *American Economic Review*.
2. Bernanke, Ben and Mark Gertler (1999), "Monetary Policy and Asset Price Volatility", *Economic Review*, Federal Reserve Bank of New York.
3. Cecchetti S., H. Genberg and S. Wadhwani (2002), "Asset Prices in a Flexible Inflation Targeting Framework", Federal Reserve Bank of Chicago.
4. Ray, Partha and S. Chatterjee (2002), "The Role of Asset Prices in Indian Inflation in Recent Years- Some Conjectures", *BIS Working Papers*, No.8.
5. Sahoo, Satyananda and S.C.Dhal (2002), "Financial Asset Price and its Implications for Monetary Policy: An Empirical Evaluation of Stock Price Movements in India", *Udyog Pragati*, Vol.26, No.1.
6. Vickers, John (1999), "Monetary Policy and Asset Prices", *Bank of England Quarterly Bulletin*.

Monitoring Inflation in India

3.39 The Reserve Bank continuously monitors the price situation by taking lead information from indicators for the conduct of monetary policy. Multiple indicators such as money, interest rates or rates of return in different markets (money, capital and government securities markets) along with such data as on currency, credit extended by banks and financial institutions, fiscal position, trade, capital flows, exchange rate, refinancing and transactions in foreign exchange available on high frequency are juxtaposed with output trends for drawing policy perspectives. Evolving global inflation and monetary policy responses elsewhere form an integral part of monitoring inflation conditions by the Reserve Bank. With increasing globalisation of the Indian economy, the pass-through of international prices to domestic inflation is becoming increasingly evident. Accordingly, international commodity price movements as well as the demand-supply situation in key commodities are constantly monitored to gauge their impact on the domestic inflation process.

Developments during 2004-05

3.40 Year-on-year WPI inflation firmed up to 8.0 per cent by August 7, 2004 reflecting lagged adjustment to changes in international metal prices, upward revision in the domestic prices of petroleum and coal as well as seasonal pressures from vegetables prices. Between end-March 2004 and August 7, 2004, prices of iron and steel increased by 20.1 per cent, coal by 15.8 per cent, mineral oils by 8.6 per cent and vegetables by 57.6 per cent. These commodities have a weight of 13.8 per cent in the WPI. Their weighted contribution to annual point-to-point inflation increased sharply from 27.8 per cent at end-March 2004 to 48.4 per cent by August 7, 2004. In order to contain inflationary pressures, customs and excise duties on certain petroleum products were revised downwards by five per cent and three per cent, respectively, with effect from August 18, 2004. Customs duty on non-alloy steel was also reduced from 10 per cent to five per cent with effect from August 20, 2004.

Outlook

3.41 Monetary conditions in 2004-05 are expected to remain stable. Non-food bank credit is likely to maintain its momentum, drawing from increased investment activity and improved business confidence. In this context, the Annual Policy Statement of May 2004 had projected money supply (M_3) expansion at 14.0 per cent during 2004-05. This order of monetary expansion should facilitate the financing of productive activity without placing undue pressure on aggregate demand.

3.42 The outlook on inflation during 2004-05 will, *inter alia*, depend on the progress of the South-West monsoon. The distribution of rainfall in various parts of the country up to July 2004 has raised some concern about the possible impact on primary agricultural commodity prices. The revival and spread of the monsoon since the beginning of August, however, could dampen the adverse impact on agricultural commodity prices to an extent. Food stocks and foreign exchange reserves should provide a cushion against any pressures on food prices. Fuel prices hold the key to the overall inflation outlook. Non-fuel commodity prices in the international market would have a critical bearing on the domestic inflationary situation during the year. Under the assumption of no significant supply shocks, and appropriate management of liquidity, the Annual Policy Statement had placed the inflation rate for 2004-05, on a point-to-point basis, at around 5.0 per cent. While the international non-fuel commodity prices could ease by the year end, further information, especially on the monsoon, would be needed to reassess the inflation scenario.

IV GOVERNMENT FINANCES

4.1 Government finances witnessed some improvement in 2003-04, reflecting the robust macroeconomic performance and the commitment towards sustainable fiscal consolidation. All the key deficit indicators, *viz.,* gross fiscal deficit (GFD), revenue deficit (RD) and primary deficit (PD) of the Centre in the revised estimates as well as in the provisional accounts for 2003-04 turned out to be lower than their budgeted levels, facilitated by higher revenue realisation and containment of non-Plan expenditure. In particular, the spectacular growth in corporation tax collections on the back of the rising profitability of the corporate sector enabled a rise in the tax-GDP ratio after seven years. Furthermore, proceeds from disinvestments exceeded the budgeted target after a gap of four years. On the other hand, there was an erosion in the health of State finances with all the key deficit indicators rising in the revised estimates for 2003-04 on account of the large increase in expenditure.

4.2 The review of Government finances in 2003-04 presented in this Section covers fiscal operations of the Centre, the States and the combined government (Centre and States) finances. The Section undertakes an assessment of the improvement in Central finances. It analyses the factors underlying deterioration in State finances - stagnancy in States' own revenue and a large increase in expenditure *albeit* accompanied by rising development expenditure. The debt position and contingent liabilities of the Centre and the States are also reviewed with details on debt management covered in Part Two of this Report.

4.3 An overview of the combined finances of the Centre and the States shows an improvement in 2003-04 on account of a lower growth in aggregate expenditure *vis-á-vis* non-debt receipts. The combined tax-GDP ratio increased by 0.5 percentage points over the previous year's level, with the improvement in direct taxes being more pronounced. On the expenditure front, there was a qualitative improvement in 2003-04 as reflected in a shift in favour of the developmental component. The softening of interest rates enabled by monetary policy, coupled with buoyant revenue receipts, resulted in a decline in the ratio of interest payments to revenue receipts (Table 4.1).

Table 4.1: Indicators of Fiscal Policy

Item	2003-04 RE	2002-03	1995-96	1990-91
1	2	3	4	5
(Per cent of GDP)				
Gross Fiscal Deficit	9.4	9.5	6.5	9.4
Revenue Deficit	6.2	6.6	3.2	4.2
Primary Deficit	2.9	3.1	1.6	5.0
Revenue Receipts	19.1	18.2	18.3	18.6
Tax Revenue	15.0	14.5	14.7	15.4
Direct Taxes	4.4	4.1	3.5	2.5
Indirect Taxes	10.6	10.4	11.2	12.9
Non-tax Revenue	4.1	3.7	3.6	3.2
Total Expenditure	31.9	29.4	25.6	28.8
Developmental Expenditure	15.9	14.5	13.9	17.4
Non-developmental Expenditure	14.4 *	14.4 *	11.6	11.4
Interest Payments	6.5	6.4	5.0	4.4
Debt	76.7	75.9	58.0	61.7
(Per cent)				
Capital Outlay/ Total Expenditure	11.0	9.0	10.7	13.1
Interest Payments/ Revenue Receipts	34.0	35.2	27.2	23.6
Revenue Deficit/GFD	66.1	69.4	48.8	44.6

RE : Revised Estimates.

* : Excluding repayments to NSSF.

Note: 1. All indicators are based on combined data of the Centre and the States with inter-Governmental transactions netted out.

2. Data in respect of the State Governments are provisional for the years 2002-03 and 2003-04 and relate to the Budgets of 27 State Governments, of which six are Vote on Account.

CENTRAL GOVERNMENT FINANCES – 2003-04

Revised Estimates

4.4 During 2003-04, finances of the Central Government revealed an improvement in the revised estimates *vis-á-vis* the budget estimates. This paved the way for the implementation of the Fiscal Responsibility and Budget Management (FRBM) Act, 2003. The key deficit indicators, *viz.,* gross fiscal deficit, revenue deficit and primary deficit in 2003-04 were lower in comparison with the budget estimates as well as their levels in 2002-03. In 2003-04, the GFD and the PD were at their lowest level since 1990-91 in relation to GDP. More than half of the reduction in the gross fiscal deficit was due to the improvement in the revenue account (Table 4.2).

4.5 The improved fiscal performance during 2003-04 was also attributable to a successful strategy

Table 4.2: Gross Fiscal Deficit – Budget *vis-á-vis* Revised Estimates

(Rupees crore)

Item	2003-04 (RE)	2003-04 (BE)	Variation RE over BE
1	2	3	4
Gross Fiscal Deficit (3+4+5+6-1-2)	**1,32,103**	**1,53,637**	**-21,534**
1. Revenue Receipts	2,63,027	2,53,935	9,092
2. Disinvestment	14,500	13,200	1,300
3. Revenue Expenditure	3,62,887	3,66,227	-3,340
4. Capital Outlay	36,273	42,283	-6,010
of which:			
Defence	16,906	20,953	-4,047
5. Public Debt Repayment#	46,602	–	46,602
6. Net Lending	-36,132	12,262	-48,394 @

RE : Revised Estimates. BE: Budget Estimates.
: Reflects expenditure on account of repayments to the NSSF met from recoveries under debt swap scheme.
@ : Net lending is negative on account of increase in recovery of loans from the States under the debt swap scheme.

for containing non-Plan expenditure. The decline in interest rates on fresh borrowings in recent years facilitated a reduction in the ratio of interest payments to revenue receipts. In addition, higher disinvestment proceeds also enabled fiscal consolidation. The Centre built up a cash surplus with the Reserve Bank from August 2003, which was generally invested in its own paper. The trend in cut back in capital outlay, however, persisted in 2003-04.

4.6 A sharp decline in net lending was on account of increased recovery of loans from the State Governments amounting to Rs.46,602 crore under the Debt Swap Scheme (DSS), which was utilised for discharge of liabilities to the National Small Savings Fund (NSSF). The utilisation of the debt swap receipts for discharging liabilities to the NSSF made the debt swap GFD neutral (Box IV.1).

Centre's Revenues

4.7 Buoyant economic activity led to an improvement in the ratio of revenue receipts to GDP. The increase in gross tax revenue was on account of

Box IV.1
Debt Swap Scheme

The Union Budget for 2003-04 announced a Debt Swap Scheme to enable the State Governments to substitute their high-cost loans from the Centre with fresh market borrowings and a portion of small saving transfers (100 per cent of the net small savings collections are being transferred to the States from 2002-03 onwards). Under the DSS, the States swapped high cost loans (bearing coupons in excess of 13 per cent) amounting to Rs.13,766 crore during 2002-03 with additional market borrowings of Rs.10,000 crore and the remaining through small saving transfers. During 2003-04, as per revised estimates the States swapped Rs.46,602 crore with additional market borrowings of Rs.26,623 crore (as per RBI records) and 30 per cent of the small saving transfers. Thus, of the total debt swapped amounting to Rs.60,400 crore, about 61 per cent was financed through additional market borrowings at interest rates below 6.5 per cent and the remaining through issue of special securities to the National Small Savings Fund (NSSF) with the interest rate fixed at 9.5 per cent. As per the Union Budget for 2004-05, recoveries from the States include a sum of Rs.11,000 crore under the DSS for the current fiscal year. The receipts under the DSS were used by the Central Government to partially redeem the special securities issued to the NSSF at the time of its inception in 1999. The NSSF, in turn, reinvested the funds in fresh Central Government special securities in 2003-04 at market-related interest rates.

According to the accounting arrangement in the Union Budget, recoveries of loans from the States under the DSS lead to an increase in non-debt capital receipts, while Centre's repayment to the NSSF results in an increase in the non-plan capital expenditure. Since both the receipts and expenditure increase by the same magnitude, the DSS is GFD neutral. However, the DSS results in a change in the composition of financing of Centre's GFD since the NSSF's reinvestment in the Central Government Special Securities reduces the financing need from other sources, including market borrowings.

For the States, the DSS is, *ipso facto*, debt neutral as it involves swapping one form of debt with another. In the States' Budgets, repayment of loans to the Centre reduces the debt of the States. However, as this repayment is made out of additional market borrowings and small saving transfers, it increases the debt from these sources by an equal magnitude. The DSS, however, does not have any effect on the magnitude of the fiscal deficit since by definition, borrowings for the purpose of repayment as well as repayments made out of such borrowings are not included in the calculation of the GFD. As in the case of the Centre, the DSS alters the composition of financing of States' GFD. While (net) market borrowings increase, (net) loans from the Centre register a decline. Over a period of time, savings in the form of lower interest payments would reduce the pressure on the revenue account of the States and thereby reduce their borrowing requirement.

References

1. Government of India (2004), *Economic Survey, 2003-04*.
2. Government of India (2004), *Union Budget, 2004-05*.
3. Reserve Bank of India (2004), *State Finances - A Study of Budgets of 2003-04*.

increased collections under corporation tax and service tax, which mitigated the shortfall in receipts under personal income tax and union excise duty. The considerable growth in service tax realisation resulted from measures aimed at bringing more services under the tax net (Box IV.2).

4.8 The rationalisation of direct taxes as a part of the ongoing reforms and the resultant improvement in tax compliance facilitated a rise in the share of direct taxes in total tax revenue. On the other hand, the share of indirect taxes came down from more than 80 per cent in 1990-91 to less than 60 per cent during 2003-04.

4.9 As per the revised estimates, non-tax revenue increased by 8.2 per cent over the budget estimates mainly due to higher dividends and profits (Table 4.3). Interest receipts were, however, lower in the revised estimates than the budgeted level, reflecting the impact of the DSS.

4.10 Capital receipts of the Central Government were also higher than the budget estimates on account of higher receipts under the DSS and proceeds from disinvestment (Table 4.4). Disinvestment proceeds exceeded the budgetary target after a gap of four years (Chart IV.1).

Centre's Expenditure

4.11 The total expenditure in the revised estimates for 2003-04 was higher than the budgeted level mainly due to the discharge of liabilities to the NSSF by the Centre (Table 4.5). Excluding the Centre's repayments to the NSSF, aggregate expenditure, however, was lower than the budgeted level. The reduction in expenditure was recorded both in the revenue account and in the capital account (net of NSSF repayments).

4.12 The lower revenue expenditure in the revised estimates was largely on account of a reduction in

Box IV.2

Taxation of Services

The objectives of levying a service tax are: (i) shrinking of the tax base as the share of industry in GDP decreases while that of services expands; (ii) failure to tax services distorts consumer choices and encourages spending on services at the expense of goods; (iii) untaxed service traders are unable to claim VAT on service inputs, which encourages businesses to develop in-house services, creating further distortions; and (iv) most of the services that are likely to become taxable are positively correlated with expenditure of high-income households and, therefore, service tax improves equity.

In the Indian context, taxation of services assumes importance in the wake of the need for improving the revenue system, ensuring a measure of neutrality in taxation between goods and services and eventually helping to evolve an efficient system of domestic trade taxes, both at the Central and the State levels. The service tax was levied in India on the basis of the recommendations made by the Tax Reforms Committee (Chairman: Dr. Raja Chelliah), the provisions of which were brought into force with effect from July 1, 1994. The coverage has progressively widened over the years. At present, service tax is levied on 58 items. The Union Budget, 2004-05 proposes to extend the service tax to 13 additional services. The service tax is applicable to all parts of India except the State of Jammu and Kashmir and is leviable on the gross amount charged by the service provider from the client. The rate of service tax has been increased from 5 per cent to 8 per cent on all the taxable services with effect from May 14, 2003. The Union Budget, 2004-05 proposes to increase the service tax rate to 10 per cent.

Collections from the service tax have shown a steady rise from Rs.410 crore in 1994-95 to Rs.8,300 crore in 2003-04 (RE); however, they accounted for only 4.4 per cent of the total tax receipts of the Centre (0.3 per cent of GDP) in 2003-04.

The service tax is envisaged as the tax of the future. The inclusion of all value added services in the tax net would yield a larger amount of revenue and make the existing tax structure more elastic. The increase in the share of the services sector in GDP holds the key to larger revenue generation.

References

1. Bagchi, Amaresh (2001), 'The Way to Tax Services', *Economic Times*, April 25.
2. Government of India website- http://www.servicetax.gov.in.
3. Govinda Rao M. (1993), 'Taxation of Services in the Asian and Pacific Region', *Asian Development Review*, Vol.11, No. 2. PP. 154-171.
4. ____ (2001), 'Taxing Services: Issues and Strategy', Paper presented at the National Institute of Public Finance and Policy (NIPFP) Conference on '*India: Fiscal Policies to Accelerate Economic Growth*', New Delhi, May.
5. Joshi, Vijay and I.M.D. Little (1996), '*India's Economic Reforms 1991-2001*', Oxford University Press, New Delhi.
6. NIPFP (1994), 'Reform of Domestic Trade Taxes in India: Issues and Options (Chairman: Amaresh Bagchi)', New Delhi.

Table 4.3 : Total Receipts of the Centre

(Rupees crore)

Item	2003-04 (RE)	2003-04 (BE)	2002-03	1995-96	1990-91	Variation RE over BE (2003-04)	
						Absolute	Per cent
1	2	3	4	5	6	7	8
Total Receipts (A+B)	4,74,255 (17.1)	4,38,795 (16.0)	4,14,162 (16.8)	1,68,468 (14.2)	93,951 (16.5)	35,460	8.1
A. Revenue Receipts (a+b)	2,63,027 (9.5)	2,53,935 (9.3)	2,31,748 (9.4)	1,10,130 (9.3)	54,954 (9.7)	9,092	3.6
a. Tax Revenue (Net)	1,87,539 (6.8)	1,84,169 (6.7)	1,59,425 (6.5)	81,939 (6.9)	42,978 (7.6)	3,370	1.8
b. Non-tax Revenue	75,488 (2.7)	69,766 (2.5)	72,323 (2.9)	28,191 (2.4)	11,976 (2.1)	5,722	8.2
B. Capital Receipts	2,11,228 (7.6)	1,84,860 (6.7)	1,82,414 (7.4)	58,338 (4.9)	38,997 (6.9)	26,368	14.3
Memo Items@:							
Gross Tax Revenue	2,54,923	2,51,527 (9.2)	2,16,266 (9.2)	1,11,224 (8.8)	57,576 (9.4)	3,396 (10.1)	1.4
Corporation Tax	62,986	51,499 (2.3)	46,172 (1.9)	16,487 (1.9)	5,335 (1.4)	11,487 (0.9)	22.3
Income Tax	40,269	44,070 (1.5)	36,858 (1.6)	15,592 (1.5)	5,371 (1.3)	-3,801 (0.9)	-8.6
Customs Duty	49,350	49,350 (1.8)	44,852 (1.8)	35,757 (1.8)	20,644 (3.0)	0 (3.6)	0.0
Union Excise Duty	92,379	96,791 (3.3)	82,310 (3.5)	40,187 (3.3)	24,514 (3.4)	-4,412 (4.3)	-4.6
Service Tax	8,300	8,000 (0.3)	4,122 (0.3)	862 (0.2)	– (0.1)	300	3.8

RE : Revised Estimates. BE : Budget Estimates.
@ : These items are on a gross basis, *i.e.*, including the States' share.
Notes : 1. Figures in parentheses are percentages to GDP.
2. Service tax was introduced from 1994-95.

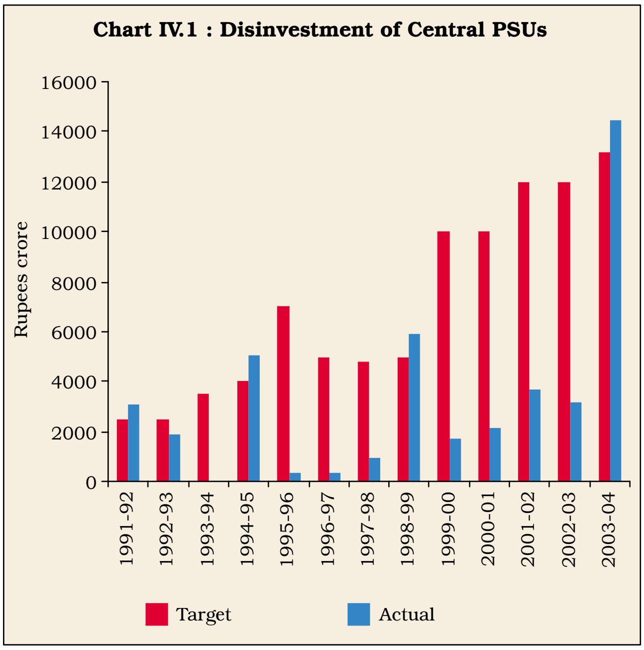
subsidies (Rs.5,198 crore) and non-Plan grants to the States and the Union Territories (Rs.2,700 crore) from the budgeted levels (Table 4.5). Interest payments (including prepayment premium of Rs.4,080 crore on internal and external debt) were higher than in the budget estimates. Excluding the premium amount,

Table 4.4: Capital Receipts of the Centre

(Rupees crore)

Item	2003-04 (RE)	2003-04 (BE)	2002-03	1995-96	1990-91	Variation RE over BE (2003-04)	
						Absolute	Per cent
1	2	3	4	5	6	7	8
Capital Receipts	2,11,228 (7.7)	1,84,860 (6.7)	1,82,414 (7.4)	58,338 (4.9)	38,997 (6.9)	26,368	14.3
Non-debt Capital Receipts	79,125 (2.9)	31,223 (1.1)	37,342 (1.5)	6,867 (0.6)	5,712 (1.0)	47,902	153.4
Debt Capital Receipts	1,32,103 (4.8)	1,53,637 (5.6)	1,45,072 (5.9)	51,471 (4.3)	33,285 (5.9)	-21,534	-14.0
Memo Items :							
Capital receipts excluding receipts on account of debt swap scheme							
Total Capital Receipts	1,64,626 (5.9)		1,68,648 (6.8)				
Non-debt Capital Receipts	32,523 (1.2)		23,576 (1.0)				

RE : Revised Estimates. BE : Budget Estimates.
Note : Figures in parentheses are percentages to GDP.



interest payments showed a decline of Rs.2,748 crore from the budgeted level.

4.13 Capital expenditure (net of NSSF repayments) was lower than in the budget estimates, with both the capital outlay and loans and advances declining over the budgeted levels (Table 4.6).

4.14 An analysis of aggregate expenditure (net of transactions relating to the debt swap scheme) shows that the reduction was effected exclusively in the non-Plan component. This comprised a reduction of Rs.4,583 crore in the revenue account and Rs.7,092 crore in the capital account on account of cutbacks in expenditure on subsidies and grants to the States and the Union Territories, as alluded to earlier, and reduction in defence expenditure (Table 4.7).

Financing Pattern of Gross Fiscal Deficit

4.15 The financing pattern of the GFD in the revised estimates *vis-á-vis* the budget estimates underwent a compositional shift on account of the DSS. The surplus cash balances emanating therefrom economised on the requirement of financing the GFD (Table 4.8). While the share of market borrowings was lower than the budget estimates, securities issued to the NSSF accounted for 45.7 per cent of the GFD.

Provisional Accounts

4.16 The financial position of the Central Government as revealed by the provisional accounts for 2003-04 showed an improvement in terms of all the key deficit indicators over the revised estimates (Table 4.9) .

Table 4.5: Aggregate Expenditure of the Centre

(Rupees crore)

Item	2003-04 (RE)	2003-04 (BE)	2002-03	1995-96	1990-91	Variation RE over BE (2003-04) Absolute	Per cent
1	2	3	4	5	6	7	8
1. Revenue Expenditure	3,62,887 (13.1)	3,66,227 (13.3)	3,39,627 (13.8)	1,39,861 (11.8)	73,516 (12.9)	-3,340	-0.9
2. Capital Expenditure	1,11,368 (4.0)	72,568 (2.6)	74,535 (3.0)	38,414 (3.2)	31,782 (5.6)	38,800	53.5
3.Total Expenditure (1+2)	4,74,255 (17.1)	4,38,795 (16.0)	4,14,162 (16.8)	1,78,275 (15.0)	105,298 (18.5)	35,460	8.1
Memo Items :							
Expenditure Net of Repayments to the NSSF							
Capital Expenditure	64,766 (2.3)		60,769 (2.5)				
Total Expenditure	4,27,653 (15.4)		4,00,396 (16.2)				

RE : Revised Estimates. BE : Budget Estimates.

Note : Figures in parentheses are percentages to GDP.

Table 4.6: Capital Expenditure of the Centre

(Rupees crore)

Item	2003-04 (RE)	2003-04 (BE)	2002-03	1995-96	1990-91	Variation RE over BE (2003-04)	
						Absolute	Per cent
1	2	3	4	5	6	7	8
Total Capital Expenditure (a+b=I+II)	64,766 * (2.3)	72,568 (2.6)	60,769 * (2.5)	38,414 (3.2)	31,782 (5.6)	-7,802	-10.8
a. Capital Outlay	36,273 (1.3)	42,283 (1.5)	29,101 (1.2)	14,099 (1.2)	12,130 (2.1)	-6,010	-14.2
b. Loans and Advances	28,493 (1.0)	30,285 (1.1)	31,668 (1.3)	24,316 (2.0)	19,652 (3.5)	-1,792	-5.9
I. Non-Plan Capital Expenditure	21,345 (0.8)	28,437 (1.0)	20,868 (0.8)	21,062 (1.8)	15,348 (2.7)	-7,092	-24.9
of which:							
Defence Capital	16,906 (0.6)	20,953 (0.8)	14,953 (0.6)	8,015 (0.7)	4,552 (0.8)	-4,047	-19.3
II. Plan Capital Expenditure	43,421 (1.6)	44,131 (1.6)	39,901 (1.6)	17,353 (1.5)	15,745 (2.8)	-710	-1.6
i) Central Plan Outlay	20,089 (0.7)	20,028 (0.7)	17,880 (0.7)	8,255 (0.7)	9,134 (1.6)	61	0.3
ii) Central Assistance for State and UT Plans	23,332 (0.8)	24,103 (0.9)	22,021 (0.9)	9,098 (0.8)	6,611 (1.2)	-771	-3.2

RE : Revised Estimates. BE : Budget Estimates. * : Net of repayments to the NSSF.

Note : Figures in parentheses are percentages to GDP.

4.17 In relation to GDP, the revenue deficit and the gross fiscal deficit were lower by 0.9 percentage points and 1.4 percentage points, respectively, than in 2002-03. The reduction in the revenue deficit was mainly on account of a decline in non-interest revenue expenditure, particularly in defence, subsidies and non-Plan grants to the States. The decline in the GFD was attributable to the lower revenue deficit and higher disinvestment proceeds. The gross primary deficit to GDP, which was 0.5 per cent in 2002-03, declined to 0.1 per cent in 2003-04, primarily on account of lower non-interest revenue expenditure.

Table 4.7: Non-Plan Expenditure of the Centre

(Rupees crore)

Item	2003-04 (RE)	2003-04 (BE)	2002-03	1995-96	1990-91	Variation RE over BE (2003-04)	
						Absolute	Per cent
1	2	3	4	5	6	7	8
Non-Plan Expenditure	3,06,146 * (11.0)	3,17,821 (11.6)	2,88,943 * (11.7)	1,31,901 (11.1)	76,933 (13.5)	-11,675	-3.7
Of which:							
Interest Payments	1,24,555 # (4.5)	1,23,223 (4.5)	1,17,804 (4.8)	50,045 (4.2)	21,498 (3.8)	1,332	1.1
Defence	60,300 (2.2)	65,300 (2.4)	55,662 (2.3)	26,856 (2.3)	15,426 (2.7)	-5,000	-7.7
Subsidies	44,709 (1.6)	49,907 (1.8)	43,515 (1.8)	12,666 (1.1)	12,158 (2.1)	-5,198	-10.4

RE : Revised Estimates. BE : Budget Estimates.

* : Net of repayments to the NSSF.

: Including prepayment premium of Rs.4,080 crore for reduction of debt.

Note : Figures in parentheses are percentages to GDP.

Table 4.8: Financing of Gross Fiscal Deficit of the Centre

(Rupees crore)

Item	2003-04 RE	2003-04 BE	2002-03	1995-96	1990-91
1	2	3	4	5	6
Gross Fiscal Deficit	1,32,103	1,53,637	1,45,072	60,243	44,632
Financed by:					
Market Borrowings*	85,671	1,07,194	1,04,126	34,001	8,001
	(64.9)	(69.8)	(71.8)	(55.6)	(17.9)
State Provident Funds	5,000	7,500	4,621	2,261	1,221
	(3.8)	(4.9)	(3.2)	(3.7)	(2.7)
NSSF Investment in Central Government Special Securities	60,400	0	0	12,761 +	9,104 +
	(45.7)	(0.0)	(0.0)	(20.9)	(20.4)
Special Deposits	-451 #	9,970	11,468	5,295	7,716
	-(0.3)	(6.5)	(7.9)	(8.7)	(17.3)
External Assistance	-11,705	3,582	-11,934	318	3,181
	-(8.9)	(2.3)	-(8.2)	(0.5)	(7.1)
Drawdown of Cash Balances	-10,232	0	1,883	9,807	11,347
	-(7.7)	(0.0)	(1.3)	(16.0)	(25.4)
Others@	3,420	25,391	34,908	-4,200	4,062
	(2.6)	(16.5)	(24.1)	-(7.0)	(9.1)

RE : Revised Estimates. BE : Budget Estimates.
* : Comprising dated securities and 364-day Treasury Bills.
+ : Represents small saving collections.
# : Reduction in receipts is on account of freezing of the corpus of special deposits as on June 30, 2003 and providing interest payment in cash on net balances.
@ : Includes saving bonds, reserve funds, deposits, postal insurance, life annuity funds and special securities issued to international financial institutions.
Note : Figures in parentheses are percentages to GFD

Table 4.9: Variations between the Budget Estimates, Revised Estimates and Provisional Accounts for 2003-04

(Per cent)

Deficit Indicators	RE over BE	ProA over RE	ProA over BE
1	2	3	4
Revenue Deficit	-11.1	-1.6	-12.5
Gross Fiscal Deficit	-14.0	-4.7	-18.0
Gross Primary Deficit	-75.2	-77.5	-94.4

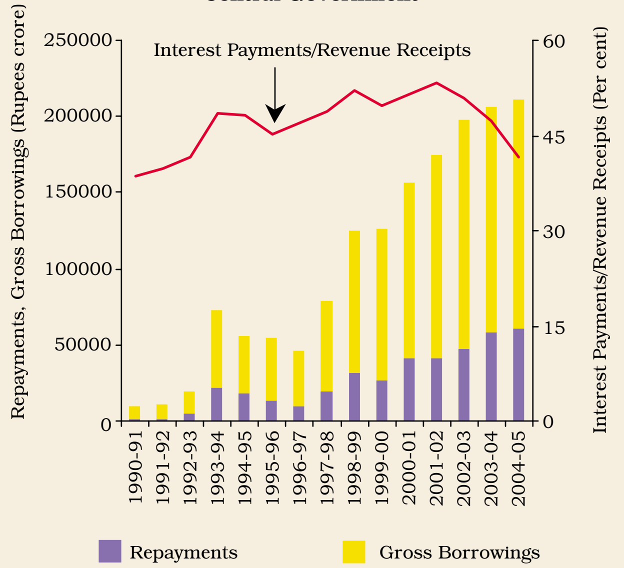
RE : Revised Estimates. BE : Budget Estimates.
ProA: Provisional Accounts (unaudited) as released by the Controller General of Accounts.

Debt Position of the Central Government

4.18 The outstanding domestic liabilities of the Central Government declined marginally to 60.5 per cent of GDP at end-March 2004 from 60.7 per cent at the end of the preceding fiscal year. Internal debt alone accounted for 65.8 per cent of the total outstanding debt of the Central Government, while 'other liabilities' which comprise, *inter alia*, small savings and provident funds accounted for 31.5 per cent.

4.19 The high debt-GDP ratio has resulted in a large debt service burden, both in terms of repayments and interest payments. Despite the elongation of the average maturity of dated securities in recent years, the proportion of repayments to gross market borrowings continued to be high at 39.8 per cent in 2003-04 as compared with the average of 31.5 per cent during the period 1998-99 to 2002-03. During 2004-05, repayments as a percentage of gross market borrowings are estimated at 40.1 per cent. Although the buoyancy in revenue receipts and the sharp decline in interest rates in the recent past enabled a decline in the proportion of interest payments to revenue receipts from 53.4 per cent in 2001-02 to 47.4 per cent in 2003-04, it continues to remain high at 41.9 per cent in 2004-05 (Chart IV.2).

Chart IV.2 : Debt Service Burden of the Central Government



Interest Rate Structure of Central Government Debt

4.20 The soft interest rate regime has facilitated the raising of resources at relatively low cost. In recent years, the weighted average interest rate on the Centre's market borrowings by way of dated securities has declined steadily (Table 4.10). The cost of resources mobilised through small savings and provident funds has also declined as a consequence of the efforts to align interest rates on various small saving instruments with the market interest rates. For instance, interest rates on Public Provident Funds and National Saving Certificates were reduced from 12.0 per cent in 1999 to eight per cent in 2003. The effective cost to the Government in respect of non-marketable borrowings such as small savings and provident funds would, however, be higher if various tax exemptions available on these instruments are taken into account.

Contingent Liabilities/Guarantees of the Government

4.21 The growing size of contingent liabilities has implications for the sustainability of Government finances. The rising trend in guarantees extended by the Central and the State Governments has, however, moderated since end-March 2001 (Table 4.11).

Table 4.10: Average Interest Rates on Outstanding Domestic Liabilities of the Centre#

(Per cent)

Year	Market Loans	Small Savings	Provident Funds	Special Deposits
1	3	4	5	6
1991-92	10.43	9.95	11.76	15.31
1992-93	10.44	9.48	11.80	14.79
1993-94	11.33	12.21	11.69	14.35
1994-95	11.94	13.20	11.34	14.86
1995-96	11.76	11.33	11.18	15.23
1996-97	11.70	13.03	10.74	15.59
1997-98	12.05	11.92	12.48	15.08
1998-99	13.09	10.34	11.93	14.05
1999-00	13.34	11.50	11.80	15.46
2000-01	12.99	11.60	10.54	13.01
2001-02	12.83	11.61	9.09	13.73
2002-03	10.69	11.61	8.27	9.00
2003-04 RE	9.86	10.88	7.66	8.22

#: The interest rate for each component is computed by dividing the interest payments in a year by the outstanding liabilities at the end of the preceding year.

RE: Revised Estimates.

Note : 1. Small savings represent small saving deposits, certificates and public provident fund.
2. Since 1999-2000, interest on small savings represents interest on Central Government Special Securities issued to the NSSF.
3. The Government has notified the freezing of the *corpus* of Special Deposit Scheme as on June 30, 2003.

Table 4.11: Outstanding Government Guarantees

(Amount in Rs. crore)

End-March	Centre		States		Total	
	Amount	Per cent of GDP	Amount	Per cent of GDP	Amount	Per cent of GDP
1	2	3	4	5	6	7
1993	58,088	7.8	42,515	5.7	1,00,603	13.4
1994	62,834	7.3	48,866	5.7	1,11,700	13.0
1995	62,468	6.2	48,479	4.8	1,10,947	11.0
1996	65,573	5.5	52,631	4.4	1,18,204	9.6
1997	69,748	5.1	63,409	4.6	1,33,157	9.7
1998	73,877	4.9	73,751	4.8	1,47,628	9.7
1999	74,606	4.3	97,454	5.6	1,72,060	9.9
2000	83,954	4.3	1,32,029	6.8	2,15,983	11.2
2001	86,862	4.1	1,68,719	8.1	2,55,581	12.2
2002	95,859	4.2	1,65,386	7.2	2,61,245	11.4
2003	90,617	3.7	1,84,294 P	7.5	2,74,911	11.2

P : Provisional.

Note : Ratios to GDP may not add up to the total due to rounding off.

Source : 1. Data on Centre's guarantees are from budget documents of the Central Government.
2. Data on States' guarantees are based on the information received from the State Governments and pertain to 17 States.

STATE GOVERNMENT FINANCES – 2003-04[1]

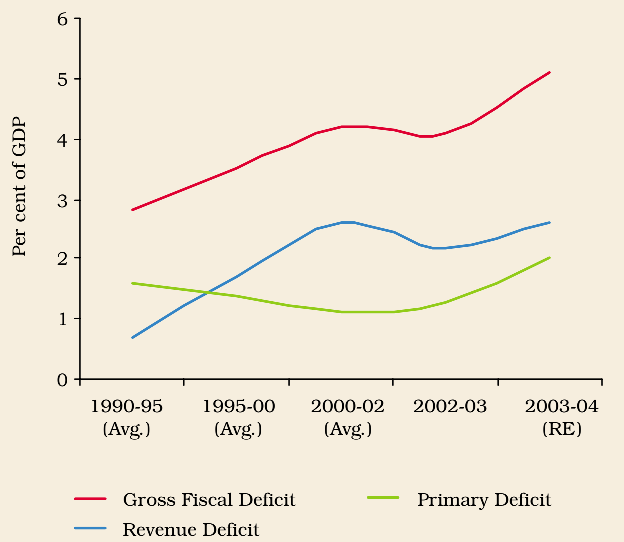
4.22 In recent years, the stress on the finances of the State Governments has intensified, as reflected in persistent and growing fiscal imbalances. The secular deterioration in State finances has impacted their current and prospective developmental and welfare-oriented functions. In this *milieu*, a positive development has been the growing recognition of the urgent need for fiscal consolidation. A number of State Governments initiated a wide spectrum of reforms in the late 1990s in order to arrest the deterioration in their financial position. These reforms have encompassed strengthening of tax efforts, rationalisation of user charges on public services, power sector reforms, expenditure management, ceilings on guarantees and, more recently, the enactment of fiscal responsibility legislation. The Central Government has also initiated measures to encourage and facilitate fiscal reforms at the State level.

4.23 Notwithstanding such initiatives, the emerging fiscal scenario as reflected in the revised estimates for 2003-04, indicates the persistence of structural infirmities in State finances, *albeit* with some improvement in the orientation of expenditure. This underscores the need to carry forward and reinvigorate the multi-pronged reform process at the State level.

4.24 All the major deficit indicators recorded substantial slippages from the budget estimates of 2003-04 and were placed higher than their respective levels in

[1] The analysis of State finances for 2004-05 is based on the budget documents of 27 State Governments of which 6 are Vote on Account. All data are provisional.

Chart IV. 3 : Trends in Major Deficit Indicators of the State Governments



the past (Chart IV.3). The widening of the revenue deficit in 2003-04 mainly reflected the increased outgo on economic services and interest payments, offset to some extent by a rise in shareable tax revenue from the Centre.

4.25 Higher provisions for capital outlay on economic services in conjunction with the increase in the revenue deficit translated into an upsurge in the net borrowing requirement (GFD). The GFD-GDP ratio was placed higher at 5.1 per cent during 2003-04. While the revenue deficit continued to pre-empt more than half of the net borrowings in 2003-04, the share of capital outlay in GFD increased sharply over the level of the previous year.

4.26 The financing pattern of the GFD shows that small savings continue to account for the predominant share. The share of market borrowings in GFD, however, shows a sharp increase reflecting, *inter alia*, additional allocations under the DSS. As a consequence, repayments of loans to the Centre exceeded gross loans from the Centre during 2003-04.

4.27 According to the Reserve Bank's records, net market borrowings allocated to the States for the fiscal year 2003-04 amounted to Rs.46,659 crore which included an additional allocation of Rs.29,000 crore under the DSS. Taking into account repayments of Rs.4,145 crore, the gross allocation amounted to Rs.50,805 crore. An amount of Rs.50,521 crore was actually raised during the year, of which Rs.26,623 crore was raised under the DSS for repayment to the Centre. Interest rates on States' market loans declined to 5.78-6.40 per cent during 2003-04 from 6.67-8.00 per cent in 2002-03.

4.28 The large and increasing GFD of the States has led to a steady accumulation of debt over the years. The debt-GDP ratio of the States increased further to 29.1 per cent at end-March 2004 from 27.8 per cent at end-March 2003.

4.29 The stress on State finances has emanated from a sluggish growth in States' own tax revenue, deterioration in States' own non-tax revenue and a persistent increase in revenue expenditure, particularly in respect of the non-developmental component which includes interest payments, pensions and administrative services. Current devolution and transfers from the Centre to the States (comprising shareable tax revenue and grants) declined in the 1990s as a ratio to GDP but increased thereafter up to 2003-04 (Chart IV. 4).

4.30 On the revenue side, States' own tax-GDP ratio has shown a slight improvement over the years indicating, *inter alia*, the potential to garner much needed revenues through taxation of services, implementation of VAT and improvement in tax administration.

4.31 The sluggish growth in States' own non-tax revenue is a major concern. It reflects, *inter alia,* the levy of inappropriate user charges in respect of public services provided by the State Governments. In fact, over the 1990s, cost recovery (measured by the ratio of non-tax revenue to non-Plan revenue expenditure) has remained nearly unchanged in respect of education and health services (Table 4.12). Cost recovery in respect of economic services such as irrigation, power and roads has been better than that of social services as highlighted by the Eleventh Finance Commission (EFC). There is, however, scope for further improvement which would

Chart IV.4 : Composition of Revenue Receipts of the State Governments

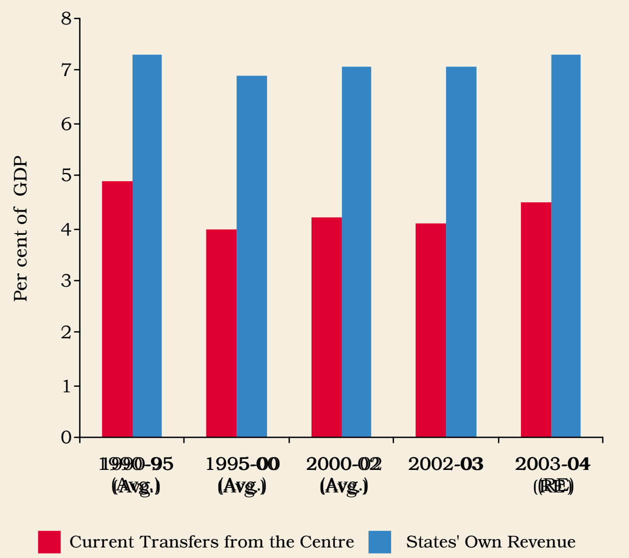


Table 4.12: Cost Recovery of Select Services of the State Governments*

(Per cent)

Item	2002-03P	2001-02	2000-01	1995-00	1990-95
1	2	3	4	5	6
Social Services					
Education	1.4	1.2	1.2	1.1	1.2
Health	6.6	6.1	4.6	5.0	5.8
Economic Services					
Irrigation	9.6	7.5	8.1	7.3	9.6
Power	10.9	6.4	6.5	10.8	16.1
Roads	13.3	19.4	16.1	15.0	15.0

P : Provisional.

* : Ratio of Non-tax Revenue to Non-plan Revenue Expenditure.

Source : Budget documents of the State Governments.

enable wider provision of qualitatively superior services. Mobilisation of non-tax revenue has also been affected by the lacklustre financial performance of many State Public Sector Undertakings (SPSUs). In this context, the EFC had also observed that the average rate of return on capital invested in the State Electricity Boards that account for the bulk of States' investment in SPSUs has been persistently negative.

4.32 In consonance with the ongoing reforms in the power sector, there is, thus, an urgent need to modernise and restructure sick SPSUs, keeping in view the national objectives that they are intended to serve, including the imperatives of a globally competitive economy (Box IV.3).

Box IV.3
Public Sector Restructuring at the State Level

The restructuring of Public Sector Undertakings (PSUs) is an important element of the process of structural reforms. The overall objective of restructuring of PSUs is to enhance economic efficiency and growth. Issues relating to restructuring and its implications are, however, complex and largely unsettled as corroborated by the international experience. Although restructuring and privatisation are often perceived to be complementary, it is important to note that restructuring, which involves industrial and organisational changes, can take place independent of privatisation. Unbundling of the generation, transmission and distribution of electricity as well as decentralising former State regional companies to the municipal level are notable examples in this regard.

Alternative methods of privatisation, *viz.,* public auctions, strategic sales, management/employee buyouts, management or lease contracts, mass privatisation or restitution could have differential social and financial impact. The fiscal implications of privatisation could also vary depending upon, *inter alia*, change in the budgetary support to PSUs following restructuring and the manner in which privatisation proceeds are utilised (say, for retiring public debt or for financing public expenditures). Thus, the decision to restructure or privatise PSUs would necessitate a comprehensive cost-benefit analysis.

In India, State Public Sector Undertakings (SPSUs) play a significant role in the achievement of developmental goals. There has, however, been a perceived need for restructuring some of the SPSUs in the context of a persistent deterioration in their financial performance over the years which has impacted their ability to meet the increasing demand for qualitatively superior public services. According to a Planning Commission Study (2002), in a sample of 747 SPSUs, 43 per cent belonged to manufacturing category, 22 per cent were promotional enterprises (which mainly focused on social activities), 12 per cent were utilities (mainly comprising State Road Transport Corporations and State Electricity Boards) and the balance belonged to trade and services, financial and welfare categories. These SPSUs recorded net losses during the 1990s, with a sharp increase in net losses evident since 1996-97. The financial performance, however, varied across categories. The manufacturing SPSUs - particularly the utility segments - made consistent losses, while the financial, trading and services and welfare segments almost invariably recorded profits. Promotional enterprises showed a mixed performance over the period.

Some of the recent State Government budgets reflect efforts to undertake a comprehensive review of the functioning of their PSUs. Some of these State Governments have also been considering the possibility of closing down non-viable SPSUs after providing for suitable safety nets to the employees. A notable development has been the initiation of power sector reforms which include the constitution of State Electricity Regulatory Commissions (SERCs) for determining the tariff structure, unbundling of electricity boards into separate entities for power generation, transmission and distribution, increasing power tariffs end measures for reducing transmission and distribution losses.

A number of issues would need to be addressed in this regard including the cost and timeframe of restructuring, an objective and transparent process of divestiture and the provision of social safety nets (say, in the form of State Renewal Funds) in order to fully protect the interests of retrenched workers. A holistic review of labour laws may also be necessary. The Planning Commission study has recommended that SPSUs may be adequately compensated for carrying out social obligations through explicit budgetary provisions. As indicated in the Economic Survey 2003-04, the National Common Minimum Programme pledges to devolve full managerial and commercial autonomy to successful, profit making companies operating in a competitive environment, while it is also committed to the *'Navratna'* companies remaining as PSUs. Furthermore, generally profit making companies will not be privatised and the process of privatisation would be transparent and on a consultative case-by-case basis.

References

1. Gupta S., C. Schiller and H. Ma (1999), 'Privatisation, Social Impact and Social Safety Nets', *IMF Working Paper No. 68.*
2. International Labour Organisation (1999), 'Report for Discussion at the Tripartite Meeting on Managing the Privatisation and Restructuring of Public Utilities (Water, Gas and Electricity)'.
3. Planning Commission (2002), '*Final Report of the* Study Group on Reforms in *State Public Sector* Undertakings', Government of India.
4. Government of India (2004), 'Economic Survey, 2003-04'.

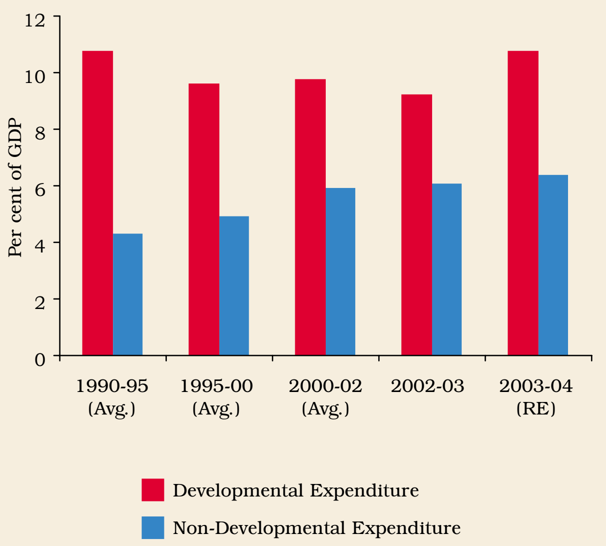
4.33 The revised estimates for 2003-04 also indicate a further increase in the revenue expenditure-GDP ratio and a sharp rise in the capital expenditure to GDP ratio. The increase in capital expenditure during the year, however, largely reflected higher repayments of loans to the Centre under the DSS. In fact, capital outlay, which represents physical and financial investment, showed a relatively smaller increase.

4.34 The distortions in the pattern of expenditure are compounded by the fact that while the ratio of non-developmental expenditure to GDP increased in 2003-04 from the first half of the 1990s, the ratio of developmental expenditure to GDP remained unchanged (Chart IV.5).

4.35 Within non-developmental expenditure, interest payments continue to remain one of the major stress factors absorbing more than 25 per cent of revenue receipts in 2003-04, substantially higher than that of 18 per cent recommended by the Eleventh Finance Commission (EFC) from the viewpoint of debt sustainability over the medium term. Notwithstanding the saving under the DSS as well as across-the-board reduction in interest rates, total interest payments increased in 2003-04.

4.36 Pensions liabilities have also been a heavy drag on the State budgets, being non-contributory in nature and unsupported by any funding arrangements. In fact, pension liabilities have pre-empted nearly 10 per cent of revenue receipts in recent years as compared with 3 per cent, on an average, during the early 1980s. Recognising the fiscal implications of increasing pension liabilities of the State Governments, some initiatives have been taken in this regard in the recent period (Box IV.4).

Chart IV.5 : Developmental and Non-Developmental Expenditure of the States



4.37 The observed weaknesses in State finances also have implications for the Local Governments in the context of fiscal decentralisation. Following the Seventy-third and Seventy-fourth Constitutional Amendment, there has been a renewed emphasis on the Local Governments. It is also increasingly recognised that the finances of the Local Governments are critical to the development of the socio-economic infrastructure and for the efficient delivery of public services (Box IV.5).

Contingent Liabilities

4.38 As alluded to earlier, outstanding guarantees of the State Governments have moderated since 2001-02. Although contingent liabilities do not directly form a part of the debt burden of the States, they will be required to meet debt service obligations in the event of default by the borrowing agency.

4.39 In view of fiscal implications of the rising level of guarantees, statutory ceilings on guarantees have been instituted by some States such as Goa, Gujarat, Karnataka, Sikkim and West Bengal, while some other States, *viz.,* Assam, Orissa and Rajasthan have imposed administrative ceilings on guarantees.

4.40 The Reserve Bank has continued its efforts to sensitise the State Governments about the problems posed by increasing volumes of guarantees. As a part of its ongoing initiatives, a Standing Committee has been constituted within the Reserve Bank to collect and monitor information on State Government guaranteed advances and bonds from the investors' side, on a periodic basis.

Ways and Means Advances (WMA) of the States

4.41 Effective March 3, 2003, the Reserve Bank revised the Scheme of WMA for the States based on the recommendations of the Advisory Committee on WMA to State Governments (Chairman : Shri C. Ramachandran) and after consultations with the State Governments. In terms of the revised scheme, the total normal WMA limits for the State Governments

Box IV.4

Managing Pension Liabilities of the State Governments – Recent Initiatives

Issues and concerns relating to social security schemes and civil service pension schemes, in particular, continue to engage the attention of academicians and policy makers. Even though civil service pensions started as a contributory system in many countries, Governments took over the liabilities of paying pensions out of public funds. In view of the growing pension liabilities, several countries subsequently initiated modifications in pension schemes which mainly focused on reducing the pension liabilities through parametric changes, gradually shifting towards some form of advance funding of benefit obligations and designing a system that allowed greater pension portability. In recent years, several countries have taken measures to reduce pension liabilities by, *inter alia*, introducing longer service periods, increasing the employee contribution rates and changing the post-retirement indexation policy.

In India, initiatives towards pension reforms are at a somewhat nascent stage. In August 2003, the Union Government approved the introduction of a restructured defined contributory pension system for new entrants to the Central Government services, except in the armed forces. An independent Pension Fund Regulatory and Development Authority was also set up to regulate and develop the pension market.

At the State Government level, the issue of increasing pension liabilities has also assumed critical importance since their unfunded and non-contributory nature has proved to be a mounting burden on the State budgets. So far, however, only a few State Governments (such as Rajasthan and Tamil Nadu) have initiated measures towards the introduction of a contributory pension scheme. Issues relating to State Government pensions came up for discussion during the Conference of State Finance Secretaries held in the Reserve Bank in January 2003. In accordance with the discussions, the Reserve Bank constituted a Group to Study the Pension Liabilities of the State Governments (Chairman: Shri B. K. Bhattacharya) in February 2003. The Group's Report was published in February 2004 and was placed on the Reserve Bank's website.

Some of the major recommendations of the Group are set out below:

Introduction of contributory pension scheme/s for all new employees of the State Governments in place of the existing non-contributory defined benefit pension scheme. The recommended alternative pension models are: (i) Pure Defined Contribution (DC) Scheme - the new employee and the Government each would contribute 10 per cent of the basic pay and dearness allowance to an individual account vested in a Fund which will be invested in accordance with the specified guidelines. At the time of retirement the employee will get an amount which will be the aggregate of the employee's contribution, Government's (employer's) contribution and the earnings (on investment made by the Fund) attributed to the employee's account; (ii) Defined Contribution -Defined Benefit (DC-DB) Scheme - a contributory scheme with guarantee of an appropriate level of pension fixed by individual State Governments; and (iii) A Two-Tier Scheme (*i.e.,* a DC-DB Scheme *plus* a second tier of DC Scheme) - the defined benefit in the first Tier of DC-DB scheme could be reduced from the present level of 50 per cent to an appropriate level of, say, 30 per cent and supplemented by a mandatory DC scheme, wherein both the employees and the State Governments make contributions.

A few parametric changes in the current pension scheme for both the existing employees and pensioners have become inevitable. These include immediate withdrawal of fixing of pensions on the basis of only last one month's pay, wherever applicable, eliminating wage indexation wherever applicable and reduction in the maximum permissible commutation amount from 40 per cent of Basic Pension to 33 1/3 per cent.

There is a need for setting up a "Dedicated Pension Fund" through levying a cess on/collecting contributions from all the existing employees, retaining a portion of increased salary and dearness allowance (DA) arising from the revisions in salary and DA in order to at least partially meet the pension burden of the existing employees and pensioners.

Reference

1. Reserve Bank of India (2003) , '*Report of the Group to Study Pension Liabilities of the State Governments*', October 2003.

were enhanced by 18.8 per cent to Rs.7,170 crore from the earlier limit of Rs.6,035 crore.

4.42 The utilisation of WMA and overdrafts by the States during 2003-04 was generally lower than that in the previous year. The number of States resorting to overdraft also declined from 21 in 2002-03 to 19 in 2003-04, indicating improved management of cash flows. A detailed analysis of State Government borrowings including WMA is provided in Section XI on Public Debt Management.

4.43 Effective April 1, 2004, the total WMA limit was further enhanced by 13.5 per cent to Rs.8,140 crore. The other features of the WMA/Overdraft scheme 2003 remain unchanged.

Box IV.5

Local Government Finances - Issues and Experience

The evolving role of local governments in the context of fiscal decentralisation has been the subject of intense debate. The international experience indicates that in a large number of countries, the powers of the local governments are drawn from the upper tiers of the government (such as in Australia, Korea and Canada). In some countries (such as Germany and Brazil), their role and functions are specified by law. The responsibilities of the local bodies are generally uniform across countries and mainly include provision of education, health and sanitation, welfare and water supply, although the priority attached to each of these sectors has varied across countries. Local governments in many countries are unable to meet their expenditure from their own resources and depend largely on transfers and borrowings, wherever possible.

In India, rural and urban local bodies are reported to have been in existence since ancient times, although they acquired a democratically elected character only during the nineteenth century. As indicated in the Report of the Eleventh Finance Commission (EFC), there are more than a quarter million local governments, of which around 3,700 are in urban areas and the remaining in rural areas. Apart from providing specific public services, local bodies implement a number of Centrally sponsored and State Plan schemes.

The Seventy-third and Seventy-fourth Constitutional Amendments in 1992 accorded statutory recognition to these local bodies as institutions of self-government. These Amendments assigned to the local bodies the task of preparing plans for economic development and social justice, apart from their traditional functions. Notwithstanding the Constitutional requirement on the part of the State Legislatures, the EFC observed that 'the pace of empowerment of these (local) bodies to function as institutions of self-government has, however, generally been slow'. Most of the State Governments have also constituted State Finance Commissions (SFCs), as required by the statute, to review the financial position of the local bodies and recommend the devolution of financial resources. It has, however, been observed that the principal recommendations of the SFCs are not accepted by the State Governments and even the accepted recommendations are not always implemented on the grounds of resource constraint. Furthermore, funds transferred for the implementation of development schemes remain unspent either on account of institutional/procedural constraints or are diverted to meet other committed expenditure.

The significance of local bodies has greatly enhanced over the years, given the urgent need to improve infrastructural facilities, and accentuated to a large extent with the rapid pace of urbanisation. Several studies have shown that the asymmetry in revenue and expenditure decentralisation is particularly stark at the local government level.

In recent years, a number of urban local bodies in India have accessed the capital market. It is important to note in this context that a number of countires (notably, Argenitina) have placed prudential controls on local government borrowing, given their implications for general government finances. Borrowing for current expenditure is usually avoided (Canada, the USA and the UK). Mexico allows for pledging federal revenue-sharing funds to borrow from banks. The Government of India had, in February 2001, specified guidelines for the issue of Municipal Bonds. The Government had permitted the issue of tax-free bonds to finance the development of urban infrastructure subject to, *inter alia*, compulsory credit rating of the debt instrument and creation of an escrow account for debt servicing with earmarked revenue. The magnitude of funds raised *via* municipal bonds, however, remains small. The factors that are reported to have been impeding the development of the municipal debt market include (i) weak financial position of local bodies, (ii) cash-based (instead of accrual-based) accounting systems which do not capture information about the asset-liability profile, (iii) relatively short tenure of bonds in relation to the gestation period of infrastructure projects that are being financed and (iv) absence of bond banks (as in the US) that access capital market and then on-lend to smaller local bodies.

As far as mobilisation of funds are concerned, an area of concern relates to the guarantees provided by State Governments to the borrowings of urban local bodies from public financial institutions to augment urban infrastructure facilities. These contingent liabilities of the State Governments are a potential source of instability in their finances. Another area of concern, as highlighted by the EFC, is the non-availability of data on the finances of local bodies. The absence of an institutionalised mechanism for collection of such data has greatly circumscribed in-depth analysis.

References

1. Ter-Minassian Teresa (1997), '*Fiscal Federalism in Theory and in Practice*', IMF, Washington.
2. Govinda Rao, M. (2000), '*Fiscal Decentralisation in Indian Federalism*', Institute for Social and Economic Change.
3. Rangarajan C., (2003), 'Inaugural Address in the National Seminar on Municipal Finance', Indian Institute of Public Administration, December 29-30.
4. 3i Network (2003), *'India Infrastructure Report - Public Expenditures Allocation and Accountability'*, Oxford University Press.

COMBINED BUDGETARY POSITION OF THE CENTRE AND THE STATES

4.44 The combined revenue receipts of the Centre and the States in 2003-04 (RE) exceeded their budgeted levels. While both the tax and non-tax revenues increased over the previous year, the rise was more pronounced in respect of non-tax revenue. The increase in combined revenue expenditure, however, outpaced the rise in revenue receipts, resulting in a higher revenue deficit. The combined aggregate expenditure exceeded the

Table 4.13: Indicators of Combined Finances of the Centre and the States*

(Rupees crore)

Item	2003-04 (RE)	2003-04 (BE)	2002-03	1995-96	1990-91	Variation RE over BE (2003-04) Absolute	Per cent
1	2	3	4	5	6	7	8
Gross Fiscal Deficit	2,60,217	2,59,200	2,34,923	77,671	53,580	1,017	0.4
	(9.4)	(9.4)	(9.5)	(6.5)	(9.4)		
Revenue Deficit	1,72,100	1,61,116	1,63,053	37,932	23,871	10,983	6.8
	(6.2)	(5.9)	(6.6)	(3.2)	(4.2)		
Primary Deficit	80,214	83,333	76,475	18,598	28,585	-3,119	-3.7
	(2.9)	(3.0)	(3.1)	(1.6)	(5.0)		
Total Receipts(A+B)	8,72,973	8,12,595	7,30,509	2,96,629	1,52,398	60,378	7.4
A. Revenue Receipts (1+2)	5,29,248	5,18,090	4,50,464	2,17,527	1,05,757	11,158	2.2
1. Tax Receipts (a+b)	4,15,283	4,13,057	3,57,889	1,74,852	87,564	2,226	0.5
a) Direct taxes	1,21,970	1,16,463	1,01,067	41,603	14,267	5,507	4.7
b) Indirect taxes	2,93,313	2,96,593	2,56,822	1,33,248	73,297	-3,280	-1.1
2. Non-tax Receipts	1,13,965	1,05,033	92,575	42,675	18,193	8,932	8.5
B. Capital Receipts (a+b)	3,43,725	2,94,506	2,80,045	79,102	46,641	49,219	16.7
a) Non-debt Capital Receipts	37,835	21,273	16,065	6,968	3,233	16,562	77.9
b) Debt Capital Receipts	3,05,890	2,73,233	2,63,980	72,134	43,408	32,658	12.0
Aggregate Expenditure (4+5)	8,85,293	8,19,833	7,26,139	3,03,586	1,63,673	65,460	8.0
1. Revenue Expenditure	7,01,348	6,79,205	6,13,517	2,55,457	1,29,628	22,144	3.3
2. Capital Outlay	97,023	97,343	65,310	32,594	21,370	-321	-0.3
3. Loans and Advances	28,927	22,013	22,625	14,115	11,589	6,914	31.4
4. Development Expenditure	4,39,465	4,05,720	3,57,948	1,65,361	98,686	33,745	8.3
5. Non-Development Expenditure (including others)@	4,45,827	4,14,113	3,68,191	1,38,225	64,987	31,714	7.7

RE : Revised Estimates. BE : Budget Estimates.

* : Data in respect of the State Governments are provisional from 2002-03 onwards.

@ : Others include compensation and assignments to local bodies and dischage of internal liabilities by the States and repayments to the National Small Savings Fund (NSSF) by the Centre.

Notes : 1. Inter-Governmental transactions have been netted out.
2. Figures in parentheses are percentages to GDP.
3. Combined GFD is the GFD of the Centre and the State Governments *minus* net lending from the Central Government to the States.
4. Revenue Deficit is the difference between revenue receipts and revenue expenditure adjusted for inter-Governmental transactions in the revenue account.
5. Gross primary deficit is defined as the combined GFD *minus* combined interest payments.

budget estimates on account of higher than anticipated revenue expenditure and loans and advances, while capital outlay was marginally lower than in the budget estimates. Relatively higher growth in aggregate expenditure *vis-á-vis* revenue receipts led to an increase in the GFD over the budgeted level. While in terms of GDP, the revenue deficit was higher by 0.3 percentage points over the budget estimates, the gross fiscal deficit remained unchanged at the budgeted level (Table 4.13).

Combined Debt

4.45 The combined outstanding liabilities of the Centre and the State Governments have risen steadily in recent years. During the period 1990-91 to 2003-04, outstanding liabilities of the Central Government increased by 6.9 percentage points of GDP, while those of the States showed an increase of 9.7 percentage points (Table 4.14).

Table 4.14: Combined Liabilities of the Centre and the States

Year (end-March)	Outstanding Liabilities (Rupees crore)			Debt - GDP Ratio (per cent)		
	Centre	States	Combined	Centre	States	Combined
1	2	3	4	5	6	7
1990-91	3,14,558	1,10,289	3,50,957	55.3	19.4	61.7
1995-96	6,06,232	2,12,225	6,89,545	51.0	17.9	58.0
2001-02	13,66,408	5,86,686	16,28,972	59.9	25.6	71.4
2002-03	15,59,201	6,86,142	18,70,519	63.1	27.8	75.7
2003-04 RE	17,24,499	8,05,667	21,25,151	62.2	29.1	76.7
2004-05 BE	19,86,167	9,10,902	24,20,091	63.6	29.2	77.5

RE: Revised Estimates. BE: Budget Estimates.

Note: 1. Data in respect of the States are provisional since 2002-03.
2. Under the head ‘combined’ inter-Governmental transactions are netted out.

FISCAL OUTLOOK FOR 2004-05[2]

Central Government

4.46 The Union Budget, 2004-05 was presented against the backdrop of sound macroeconomic fundamentals. The Fiscal Responsibility and Budget Management (FRBM) Act, 2003 has further streamlined the budget presentation process. The commitment to prudent financial policies has been demonstrated by notifying the FRBM Act, 2003 and FRBM Rules, 2004 with effect from July 5, 2004 (Box IV.6). More importantly, while presenting the

Box IV.6

The Fiscal Responsibility and Budget Management Act

Fiscal rules have become an imperative in the context of the need to restrain discretionary policies which have an inherent deficit bias. Fiscal rules could be defined as legislated or constitutional constraints on government deficits, taxes, expenditures or debt. The adoption of fiscal policy rules commits the Government to a deficit or debt reduction path into the future, thereby enhancing the credibility of the fiscal stance.

International experience shows that a number of countries facing widening fiscal imbalances have introduced medium-term fiscal adjustment plans through the adoption of rules: the medium-term Financial Strategy in the U.K., the Balanced Budget and Emergency Deficit Control Act [Gramm Rudman Hollings Act in the U.S of 1985], Fiscal responsibility legislations in New Zealand (1994), Argentina (1999), Peru (1999) and Brazil (2002).

In India, the Fiscal Responsibility and Budget Management Act, 2003 was enacted on August 26, 2003 and came into force from July 5, 2004. The Act embodies the spirit of inter-generational equity and provides for long-term macroeconomic stability by achieving sufficient revenue surplus and removing the fiscal constraints on the conduct of monetary policy and debt management. This is sought to be achieved through limits on deficits, borrowings and debt of the Central Government over the medium-term while increasing transparency of fiscal operations.

The Act also stipulates appropriate measures by the Central Government to reduce the fiscal deficit and eliminate revenue deficit by March 31, 2008 and thereafter build up adequate revenue surplus (The Union Budget for 2004-05 proposes to eliminate the revenue deficit by 2008-09). These deficits could, however, exceed the targets on grounds of national security, natural calamity or other exceptional circumstances. The Act prohibits direct borrowings by the Centre from the Reserve Bank from the fiscal year 2006-07 except by way of Ways and Means Advances to meet temporary mismatches in receipts and payments or under exceptional circumstances. The Reserve Bank may, however, buy or sell Central Government securities in the secondary market. The Act also contains provision to enhance transparency in the Central Government's fiscal operations by requiring the Government to place before the Parliament the outcome of a quarterly review of trends in receipts and expenditure in relation to the budget estimates.

In exercise of the powers conferred by the FRBM Act 2003, the Central Government framed the Fiscal Responsibility and Budget Management Rules, 2004, effective July 5, 2004. The Rules have set annual targets for the phased reduction in key deficit indicators over the period ending March 31, 2008. The rules also impose annual ceilings on Government guarantees and additional liabilities.

In accordance with the Rules framed under the FRBM Act, the Government presented the Medium-term Fiscal Policy Statement, the Fiscal Policy Strategy Statement and the Macroeconomic Framework Statement along with the Annual Financial Statement for 2004-05. The Medium-term Fiscal Policy Statement sets forth a three-year rolling target for certain fiscal indicators and elucidates the underlying assumptions. It also included an assessment of sustainability relating to the balance between revenue receipts and revenue expenditure and the use of capital receipts (including market borrowings) for generating productive assets. The Fiscal Policy Strategy Statement contains, *inter alia*, the key fiscal measures and rationale for any major deviation in these measures. The Macroeconomic Framework Statement provides an assessment of the growth prospects of the economy.

References

1. Government of India (2003), '*Fiscal Responsibility and Budget Management Act, 2003*', August.
2. Kennedy, Suzanne and Janine Robbins (2001), '*The Role of Fiscal Rules in Determining Fiscal Performance*,' Canadian Department of Finance, Working Paper No.16.
3. Kopits, George (2001), '*Fiscal Rules: Useful Policy Framework or Unnecessary Ornament?*', Fiscal Rules, Public Finance Workshop, Banca D'Italia.
4. Reserve Bank of India (2004), '*State Finances - A Study of Budgets of 2003-04*', April.
5. Government of India (2004), '*Union Budget, 2004-05*'.

[2] All comparisons in this section relating to 2004-05 are with respect to revised estimates for 2003-04, unless otherwise stated.

Table 4.15: Major Fiscal Indicators of the Centre

(Rupees crore)

Item	2004-05 (BE)	2003-04 (RE)	Variation (Col.3/Col.2)	
			Absolute	Per cent
1	2	3	4	5
Total Receipts	**4,77,829 (15.3)**	**4,74,255 (17.1)**	**3,574**	**0.8**
Revenue Receipts	3,09,322 (9.9)	2,63,027 (9.5)	46,295	17.6
Tax Revenue (Net)	2,33,906 (7.5)	1,87,539 (6.8)	46,367	24.7
Capital Receipts	1,68,507 (5.4)	2,11,228 (7.6)	-42,721	-20.2
Total Expenditure	**4,77,829 (15.3)**	**4,74,255 (17.1)**	**3,574**	**0.8**
Revenue Expenditure	3,85,493 (12.3)	3,62,887 (13.1)	22,606	6.2
Capital Expenditure	92,336 (3.0)	1,11,368 (4.0)	-19,032	-17.1
Expenditure Excluding Repayments to NSSF				
Total Expenditure	**4,77,829 (15.3)**	**4,27,653 (15.4)**	**50,176**	**11.7**
Capital Expenditure	92,336 (3.0)	64,766 (2.3)	27,570	42.6
Gross Fiscal Deficit	**1,37,407 (4.4)**	**1,32,103 (4.8)**	**5,304**	**4.0**
Revenue Deficit	76,171 (2.5)	99,860 (3.6)	-23,689	-23.7
Primary Deficit	7,907 (0.3)	7,548 (0.3)	359	4.8

BE: Budget Estimates. RE: Revised Estimates.

Note: Figures in parentheses are percentages to GDP.

Budget, the Government has also placed before the Parliament three important documents, *viz.,* (i) Macroeconomic Framework Statement, (ii) Medium-Term Fiscal Policy Statement, and (iii) Fiscal Policy Strategy Statement. These documents assume critical importance in the context of the commitment to fiscal prudence, transparency and budget integrity.

4.47 The Union Budget for 2004-05 has endeavoured to carry forward the process of fiscal consolidation, essentially based on a projected upsurge in revenue mobilisation coupled with some deceleration in expenditure. A notable feature of the budget estimates is the reduction of nearly 24 per cent in the revenue deficit in 2004-05 on top of the decline of about 7 per cent in the previous year. As a consequence, the revenue deficit is placed lower in 2004-05 than the revised estimates of the previous year and the average during the second half of the 1990s. The GFD-GDP ratio is also budgeted to decline in 2004-05 in comparison with recent trends (Table 4.15).

4.48 The Union Government constituted a Task Force on Implementation of the Fiscal Responsibility and Budget Management Act, 2003 (Chairman: Dr. Vijay L. Kelkar) to suggest ways of achieving the fiscal targets prescribed by the FRBM Act, 2003. The Task Force submitted its Report to the Government in July 2004, providing the road map for attaining the fiscal targets set in the FRBM Act (Box IV.7).

Box IV.7

Report of the Task Force on Implementation of the Fiscal Responsibility and Budget Management Act, 2003

The Government of India set up a Task Force (Chairman: Dr. Vijay Kelkar) to draw up the medium-term framework for fiscal policies to achieve the objectives set out in the Fiscal Responsibility and Budget Management Act (FRBM), 2003. The Report of the Task Force, which was submitted on July 16, 2004, attempted to address the issue of fiscal planning in two steps, *viz.,* (i) to provide baseline projections, with a forecast of broad contours of Central finances, and (ii) to devise policy proposals which close the gaps, if any, identified between the baseline projection and the requirements of the Act.

The Task Force advocated a fiscal strategy based on revenue augmentation and front-loaded efforts on revenue expenditure reforms in order to counter-balance the contractionary effects of the fiscal consolidation. The Task Force also made specific recommendations for tax reforms, tax administration and expenditure reforms. The tax-specific recommendations focused on widening the tax base; rationalising the tax system; enhancing vertical and horizontal equity of the tax system; shifting to a destination-based VAT on all goods and services; enhancing the neutrality of the tax system in respect of the timing of consumption, form of organisation and sources of finance; establishing an effective and efficient compliance system; and improving tax buoyancy rather than immediacy of tax revenue.

The Task Force made two major proposals regarding tax administration, *i.e.,* the implementation of the proposed Goods and Services Tax (GST) and measures to avoid tax evasion. Since the efficient implementation of GST system entails tax credits and refund of GST embedded in exports, the Task Force recommended that the existing Tax Information Network (TIN) and Online Tax Administration System (OLTAS) developed by the Central Board of Direct Taxes (CBDT) should be used for the implementation of the GST, both by the Centre and the States. The Task Force also proposed an IT-intensive system, *viz.,* Risk Intelligence Network (RIN) in order to identify tax evaders, while simultaneously having a taxpayer friendly system.

In the area of expenditure reforms, the broad strategy suggested by the Task Force related to greater allocation for legitimate public goods as opposed to transfers and subsidies; transfer production of local public goods like water, sanitation and primary education to *Panchayati Raj* institutions; greater focus on public goods outcomes rather than their expenditure; and extension of public-private partnership. The Task Force projected that under the reforms scenario, a small revenue surplus would be generated by 2008-09 and the fiscal deficit would dip below 3 per cent of GDP (Table).

The fiscal reforms proposed by the Task Force are expected to have a positive impact on investment, health, education, manufacturing, exports, financial sector, growth, employment and State finances.

Table : Fiscal Projections under Baseline/ Reforms Scenarios

(Per cent of GDP)

Item	2005-06		2006-07		2007-08		2008-09	
	Baseline Scenario	Reforms Scenario	Baseline Scenario	Reforms Scenario	Baseline Scenario	Reforms Scenario	Baseline Scenario	Reforms Scenario
1	2	3	4	5	6	7	8	9
1. Revenue Receipts	**9.36**	**10.27**	**9.31**	**10.78**	**9.32**	**10.99**	**9.42**	**11.18**
Tax revenue, net to Centre	7.20	8.14	7.41	8.91	7.55	9.34	7.91	9.73
Non-tax revenue	2.16	2.13	1.91	1.87	1.53	1.65	1.51	1.44
2. Non-debt Capital Receipts	**0.50**	**0.61**	**0.43**	**0.41**	**0.37**	**0.37**	**0.33**	**0.32**
Recoveries of loans	0.39	0.49	0.33	0.31	0.28	0.28	0.25	0.24
Other receipts	0.12	0.12	0.10	0.10	0.09	0.09	0.08	0.08
3. Total Expenditure	**14.76**	**14.90**	**14.42**	**14.75**	**14.01**	**14.48**	**13.74**	**14.30**
i. Revenue Expenditure	11.91	12.03	11.63	11.85	11.30	11.31	11.08	11.03
of which :								
a) Interest, debt servicing	4.14	4.07	4.08	3.92	4.00	3.74	3.91	3.54
b) Subsidies	1.28	1.28	1.13	1.13	0.92	0.91	0.82	0.80
ii. Capital Expenditure	2.85	2.87	2.79	2.90	2.71	3.17	2.65	3.27
4. Revenue Deficit	**2.61**	**1.76**	**2.35**	**1.07**	**1.98**	**0.33**	**1.66**	**(-)0.15**
5. Fiscal Deficit	**4.96**	**4.03**	**4.71**	**3.56**	**4.32**	**3.13**	**3.98**	**2.80**
Memo Item:								
Gross Tax Revenue	**9.72**	**11.05**	**10.00**	**12.07**	**10.33**	**12.64**	**10.70**	**13.17**

Reference

1. Government of India (2004), *'Report of the Task Force on Implementation of the Fiscal Responsibility and Budget Management Act, 2003',* July.

Table 4.16: Decomposition of GFD of the Centre

(Per cent)

Year	Revenue Deficit	Capital Outlay @	Net Lending
1	2	3	4
1990-91	41.6	27.2	31.2
1991-92	44.8	23.0	32.2
1992-93	46.2	29.0	24.7
1993-94	54.3	22.0	23.7
1994-95	53.8	17.0	29.2
1995-96	49.4	22.8	27.8
1996-97	48.9	20.7	30.4
1997-98	52.2	18.7	29.1
1998-99	59.1	11.4	29.5
1999-00	64.6	21.3	14.1
2000-01	71.7	19.0	9.2
2001-02	71.1	16.3	12.7
2002-03	74.4	27.4	-1.7
2003-04 (RE)	75.6	16.5	7.9
2004-05 (BE)	55.4	34.7	9.8

@ : Adjusted for disinvestment receipts from 1991-92.

4.49 The envisaged improvement in the revenue balance would facilitate the correction in the GFD. Although the share of the revenue deficit in the GFD is envisaged to be lower in 2004-05 as compared with the previous year, it continues to be high as compared with the first half of the 1990s (Table 4.16).

Pattern of Receipts

4.50 Gross tax revenue is budgeted to increase by about 25 per cent in 2004-05 as compared with 17.6 per cent in the previous year (Table 4.17). The gross tax to GDP ratio is accordingly estimated higher in 2004-05 than in the previous year and the average for the second half of the 1990s. Substantial increases are expected in respect of corporation tax (40.4 per cent), income tax (26.5 per cent), union excise duty (18.2 per cent) and service tax (70.5 per cent). In contrast, the growth in customs duty (9.9 per cent) is expected to be modest in line with the policy of rationalising customs duty, the ultimate objective being a transition to the uniform tax rate (Box IV.8).

4.51 Union excise duty and corporation tax are budgeted to account for over 60 per cent of the increase in gross tax revenue in 2004-05. The expected higher mobilisation of tax revenue reflects a variety of measures including the two per cent education cess, raising of the service tax rate coupled with the widening of coverage and the special drive

Table 4.17: Revenue Position of the Centre

(Rupees crore)

Item	2004-05 (BE)	2003-04 (RE)	Variation (Col. 2 / 3)	
			Absolute	Per cent
1	2	3	4	5
Total Receipts	**4,77,829**	**4,74,255**	**3,574**	**0.8**
	(15.3)	**(17.1)**		
Revenue Receipts	3,09,322	2,63,027	46,295	17.6
	(9.9)	(9.5)		
Tax Revenue (Net)	2,33,906	1,87,539	46,367	24.7
	(7.5)	(6.8)		
Non-tax Revenue	75,416	75,488	-72	-0.1
	(2.4)	(2.7)		
Capital Receipts	1,68,507	2,11,228	-42,721	-20.2
	(5.4)	(7.6)		
Memo Items :				
Gross Tax Revenue	**3,17,733**	**2,54,923**	**62,810**	**24.6**
	(10.2)	**(9.2)**		
Corporation Tax	88,436	62,986	25,450	40.4
	(2.8)	(2.3)		
Income Tax	50,929	40,269	10,660	26.5
	(1.6)	(1.5)		
Customs Duty	54,250	49,350	4,900	9.9
	(1.7)	(1.8)		
Union Excise Duty	1,09,199	92,379	16,820	18.2
	(3.5)	(3.3)		
Service Tax	14,150	8,300	5,850	70.5
	(0.5)	(0.3)		

BE : Budget Estimates. RE : Revised Estimates.
Note : Figures in parentheses are percentages to total.

to recover arrears in respect of both direct and indirect taxes (Chart IV.6).

4.52 Non-tax revenue is, however, budgeted to decline marginally in 2004-05, mainly reflecting the sharp reduction of over Rs.5,000 crore in dividends and profits transferred by the Reserve Bank, nationalised banks and financial institutions. Furthermore, interest receipts from the State Governments are budgeted to increase by only 4 per cent in 2004-05, reflecting saving by the States on interest costs on account of the DSS as well as the envisaged saving of Rs.375 crore from the reduction in the rate of interest on Central loans to 9.0 per cent with effect from April 1, 2004 as against 10.5 per cent in the previous year.

4.53 Capital receipts are budgeted to decline from the revised estimates for 2003-04. Non-debt capital receipts, both under recovery of loans (which includes Rs.11,000 crore under the debt swap scheme) and under disinvestment, are estimated to be lower than

Box IV.8
Uniform *versus* Multiple Tax Rate

In developing countries, taxes are levied with multiple objectives: mobilising revenue, protection of domestic industries and promotion of strategic industries. The tax rate structure in developing countries is complex due to high and multiple rates coupled with exemptions on several commodities. Multiple tax rates are often the source of high administrative cost and inconvenience to the taxpayers. Many countries have gradually rationalised multiple rates of taxes in the wake of globalisation and the need for ensuring greater tax efficiency. It has also been observed that de-escalating tariffs yield the highest welfare when the benefits of agglomeration are very high.

There are several arguments in the literature in favour of a uniform tax regime. Uniform tax rates facilitate tax smoothening and stabilise expectations among economic agents. Besides, a uniform rate is administratively convenient and enhances transparency of the tax system. Uniform tax rates also obviate moral hazard problems of lobbying and smuggling and other hidden actions that cannot be fully monitored. Among the indirect taxes, excise duties and customs duties are the major taxes which can be subjected to a uniform tax rate. Uniform taxation, however, may not be appropriate in the presence of externalities. Furthermore, considerations of equity and redistribution of wealth provide a strong case for a differentiated indirect tax structure.

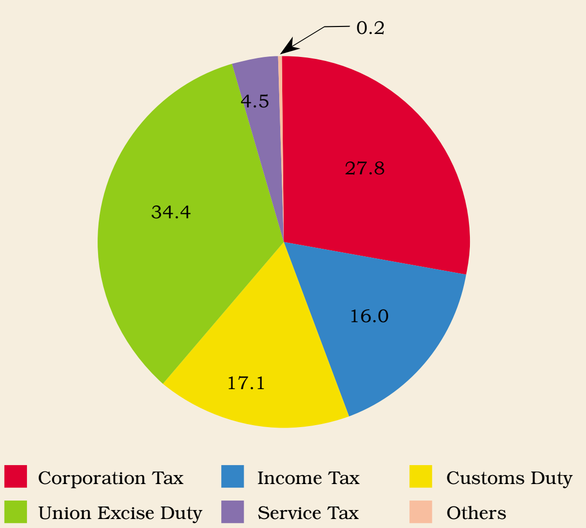
The Task Force on Indirect Taxes (Chairman: Dr Vijay L. Kelkar), 2002 was of the view that a simple tax law is not only cost effective and easy to administer but would also encourage compliance and have a positive impact on tax revenues. As a policy, it recommended that multiplicity of levies must be reduced. However, it did not favour a single duty regime. On import tariffs, the Tax Reforms Committee (Chairman: Dr. Raja Chelliah), 1992 ruled out a single duty rate regime and favoured a limited number of rates. It recommended that all commodities should be subjected to a minimum tariff. The Task Force recommended that there should be only three types of duties, *viz.,* Basic Customs Duty, Additional Duty of Customs (or Countervailing duty) and Anti-dumping/Safeguard duties. An Inter-Ministerial Group on Customs Tariff Structure constituted by the Ministry of Finance (Chairman: Dr. Arvind Virmani) in 2001 favoured uniformity of customs duty. The Group specifically recommended that no new end-use exemptions should be given and existing ones should be eliminated at the earliest. A recent study has recommended a uniform tariff rate of 15 per cent for all import items, including defence, which would not have any adverse revenue implications.

References

1. Amiti, M.(2004), ‘Are Uniform Tariffs Optimal?’, *IMF Working Paper, No.72*, International Monetary Fund.
2. Government of India, (2002), ‘Report of the Task Force on Indirect Taxes’.
3. Mirlees J. (1982), ‘The Theory of Optimum Taxation’, in Arrow K.J. and Intrilligator M.I. (eds.) Handbook of Mathematical Economics.
4. Roy J. and Pattnaik R.K. (2004), ‘Uniform Import Duty: India's Next Step in Tariff Reform’, *Economic and Political Weekly,* June.

in the revised estimates for 2003-04. Net market borrowings through dated securities and 364-day Treasury Bills [net of issuance under the Market Stabilisation Scheme (MSS)] are budgeted to increase by 5.5 per cent over the previous year (Table 4.18).

Chart IV.6 : Contribution of Major Taxes to Gross Tax Revenue - 2004-05



Pattern of Expenditure

4.54 As a proportion to GDP, total expenditure is estimated to be lower than in the previous year. Revenue expenditure would show a similar reduction. Capital expenditure, which increased sharply in 2003-04 mainly as a result of redemption of securities to the NSSF, would decline to 3.0 per cent of GDP in 2004-05.

4.55 Within revenue expenditure, the major non-Plan components, *viz.,* interest payments and subsidies, are budgeted to show a decline in relation to GDP. Total provision for subsidies is budgeted to decline even in nominal terms during 2004-05, notwithstanding the higher outgo on food and fertiliser subsidies (Table 4.19). This is essentially on account of a decline of over Rs.3,000 crore in petroleum subsidy (which includes subsidies for domestic LPG and PDS kerosene) in line with the decision to phase it out over a period of time. The ratio of interest payments to GDP would also show

Table 4.18: Capital Receipts of the Centre

(Amount in Rupees crore)

Item	2004-05 (BE)	2003-04 (RE)	Variation Col. 2 over Col. 3	
			Absolute	Per cent
1	2	3	4	5
Capital Receipts	**1,68,507**	**2,11,228**	**-42,721**	**-20.2**
Non-debt Capital Receipts	31,100	79,125	-48,025	-60.7
Debt Capital Receipts	1,37,407 *	1,32,103	5,304	4.0

BE : Budget Estimates. RE : Revised Estimates.
* : Net of issuances under the MSS.

a decline in 2004-05. Similarly, the absence of any provision for premium on prepayment of external debt (as compared with that of Rs.4,080 crore in the previous year) would contribute to the subdued growth in non-Plan revenue expenditure in 2004-05. Total establishment expenditure in the form of pay, allowances and travel expenses (excluding those in respect of defence personnel and Railways) is estimated to pre-empt 6.7 per cent (Rs.20,782 crore) of revenue receipts in 2004-05 as compared with 8.1 per cent in the previous year. Pensions would absorb 5.1 per cent (Rs.15,928 crore) of revenue receipts in 2004-05 as compared with 5.8 per cent in the previous year.

4.56 Plan revenue expenditure is budgeted to increase sharply by 17.6 per cent in 2004-05, mainly reflecting the renewed thrust on Central Plan schemes. As a ratio to GDP, however, Plan revenue expenditure would increase marginally by 0.1 percentage points to 2.9 per cent.

4.57 While there is a renewed thrust on developmental goals in the budget estimates for 2004-05, the allocation of expenditure on select heads indicates some elements of continuity (Table 4.20).

Financing of Gross Fiscal Deficit

4.58 Net market borrowings (excluding allocations budgeted under the MSS) would finance 65.8 per cent of the GFD in 2004-05 as compared with 64.9 per cent in the previous year. About 10 per cent of the GFD would be financed by drawing down surplus cash balances with the Reserve Bank. Contributions from other sources are budgeted to finance 14.4 per cent of the GFD as compared with 2.6 per cent in 2003-04, mainly on account of the budgeted increase in Savings Bonds. The securities against small savings are expected to finance only 1.0 per cent of the fiscal deficit (as against 45.7 per cent in the previous year) as there is no budgetary provision for repayment to the NSSF from the receipts under the DSS. The

Table 4.19: Expenditure Pattern of the Centre

(Rupees crore)

Item	2004-05 (BE)	2003-04 (RE)	Variation (Col.2 /Col. 3)	
			Absolute	Per cent
1	2	3	4	5
Total Expenditure	**4,77,829 (15.3)**	**4,27,653 * (15.4)**	**50,176**	**11.7**
Non-Plan Expenditure	**3,32,239 (10.6)**	**3,06,146 * (11.0)**	**26,093**	**8.5**
Interest Payments	1,29,500 (4.1)	1,24,555 (4.5)	4,945	4.0
Defence	77,000 (2.5)	60,300 (2.2)	16,700	27.7
Subsidies	43,516 (1.4)	44,709 (1.6)	-1,193	-2.7
Grants/loans to States	19,576 (0.6)	15,850 (0.6)	3,726	23.5
Other Non-Plan Expenditure	62,647 (2.0)	60,732 (2.2)	1,915	3.2
Plan Expenditure	**1,45,590 (4.7)**	**1,21,507 (4.4)**	**24,083**	**19.8**
Budgetary Support to Central Plan	87,886 (2.8)	72,847 (2.6)	15,039	20.6
Central Assistance for State and UT Plans	57,704 (1.8)	48,660 (1.8)	9,044	18.6

* : Net of repayments to the NSSF.
Note: Figures in parentheses are percentages to GDP.

Table 4.20: Expenditure on Select Developmental Heads of the Centre

(Rupees crore)

	2004-05(BE)	2003-04 (RE)	2002-03
1	2	3	4
Agriculture	36,349 (7.6)	33,126 (7.0)	31,185 (7.5)
Education	11,480 (2.4)	10,738 (2.3)	9,519 (2.3)
Health	5,956 (1.2)	4,632 (1.0)	4,007 (1.0)
Rural Development*	6,926 + (1.4)	11,466 (2.4)	11,703 (2.8)
Irrigation	361 (0.1)	372 (0.1)	366 (0.1)
Total Expenditure	477,829 (100.0)	474,255 (100.0)	414,162 (100.0)

BE : Budget Estimates. RE : Revised Estimates.

* : Comprising expenditure on special programmes for rural development, rural employment, land reforms and other rural development programmes.

+ : The fall in this allocation may be seen in conjunction with the lump sum provision of Rs.10,000 crore to the Planning Commission for reallocation to primary rural development activities.

Note: Figures in parentheses are percentages to total expenditure.

Table 4.21: Financing of Gross Fiscal Deficit of the Centre

(Rupees crore)

Year	2004-05 BE	2003-04 RE
1	2	3
Gross Fiscal Deficit	**1,37,407**	**1,32,103**
Financed by:		
Market Borrowings*	90,365 (65.8)	85,671 (64.9)
State Provident Funds	4,000 (2.9)	5,000 (3.8)
NSSF Investment in Central Government Special Securities	1,350 (1.0)	60,400 (45.7)
Special Deposits	200 (0.1)	-451 # -(0.3)
External Assistance	8,076 (5.9)	-11,705 -(8.9)
Drawdown of cash balances	13,597 (9.9)	-10,232 -(7.7)
Others@	19,819 (14.4)	3,420 (2.6)

BE : Budget Estimates. RE : Revised Estimates.

* : Includes dated securities and 364-day Treasury Bills.

: Reduction in receipts is on account of freezing of the corpus of special deposits as on June 30, 2003 and providing interest payment in cash on net balances.

@: Includes saving bonds, reserve funds, deposits, postal insurance and life annuity fund and special securities issued to international financial institutions.

securities against small savings during 2004-05 represent reinvestment by the NSSF out of funds to be received on redemption of State Government special securities (Table 4.21).

State Budgets - 2004-05

4.59 A significant correction of fiscal imbalances is to be effected in the finances of the States in 2004-05 through a compression of developmental and investment-oriented expenditures. All the major deficit indicators of the State Governments are expected to be placed substantially lower than their levels in the previous year (Table 4.22).

4.60 Total revenue receipts as well as States' own revenue constituents would, however, remain broadly unchanged in 2004-05 as ratios to GDP from their levels in the previous year (Table 4.23).

Table 4.22: Major Deficit Indicators of the State Governments

(Rupees crore)

Item	2004-05 (BE)	2003-04 (RE)	2003-04 (BE)	2002-03	2000-02 (Average)	1995-00 (Average)	1990-95 (Average)	Percentage variations	
								Col.2/3	Col.3/4
1	2	3	4	5	6	7	8	9	10
Gross Fiscal Deficit	1,12,251 (3.6)	1,40,407 (5.1)	1,16,110 (4.2)	1,02,058 (4.1)	(4.2)	(3.5)	(2.8)	-20.1	20.9
Revenue Deficit	48,259 (1.5)	72,240 (2.6)	48,824 (1.8)	55,173 (2.2)	(2.6)	(1.7)	(0.7)	-33.2	48.0
Primary Deficit	20,604 (0.7)	56,682 (2.0)	33,443 (1.2)	32,092 (1.3)	(1.1)	(1.4)	(1.6)	-63.6	69.5

RE: Revised Estimates. BE : Budget Estimates.

Note: The figures in parentheses are percentages to GDP.

Table 4.23: Total Receipts of the State Governments

(Rupees crore)

Item	2004-05 (BE)	2003-04 (RE)	2003-04 (BE)	2002-03	2000-02 (Average)	1995-00 (Average)	1990-95 (Average)	Percentage variations Col.2/3	Col.3/4
1	2	3	4	5	6	7	8	9	10
Total Receipts (1+2)	5,42,295	5,39,635	4,77,313	4,23,819				0.5	13.1
	(17.4)	(19.5)	(17.4)	(17.2)	(16.6)	(15.2)	(16.1)		
1. Total revenue receipts (a+b)	3,67,428	3,27,302	3,30,688	2,77,389				12.3	-1.0
	(11.8)	(11.8)	(12.1)	(11.2)	(11.3)	(10.9)	(12.1)		
(a) States own Revenue (i+ii)	2,30,991	2,03,114	2,04,804	1,76,479				13.7	-0.8
	(7.4)	(7.3)	(7.5)	(7.1)	(7.1)	(6.9)	(7.3)		
i) States own tax	1,82,982	1,62,700	1,64,838	1,42,006				12.5	-1.3
	(5.9)	(5.9)	(6.0)	(5.8)	(5.6)	(5.3)	(5.4)		
ii) States own non-tax	48,009	40,414	39,966	34,473				18.8	1.1
	(1.5)	(1.5)	(1.5)	(1.4)	(1.5)	(1.6)	(1.8)		
(b) Central Transfers (i+ii)	1,36,437	1,24,188	1,25,884	1,00,910				9.9	-1.3
	(4.4)	(4.5)	(4.6)	(4.1)	(4.2)	(4.0)	(4.9)		
i) Shareable taxes	77,343	65,044	64,049	56,457				18.9	1.6
	(2.5)	(2.3)	(2.3)	(2.3)	(2.4)	(2.4)	(2.6)		
ii) Central Grants	59,094	59,144	61,835	44,453				-0.1	-4.4
	(1.9)	(2.1)	(2.3)	(1.8)	(1.8)	(1.6)	(2.3)		
2. Capital Receipts (a+b)	1,74,867	2,12,333	1,46,625	1,46,430				-17.6	44.8
	(5.6)	(7.7)	(5.3)	(5.9)	(5.3)	(4.2)	(4.0)		
(a) Loans from Centre@	33,852	32,203	33,634	26,348				5.1	-4.3
	(1.1)	(1.2)	(1.2)	(1.1)	(1.0)	(1.0)	(1.2)		
(b) Other Capital Receipts	1,41,015	1,80,130	1,12,991	1,20,082				-21.7	59.4
	(4.5)	(6.5)	(4.1)	(4.9)	(4.3)	(3.2)	(2.9)		

BE : Budget Estimates. RE: Revised Estimates.

@ : With the change in the system of accounting with effect from 1999-2000, States' share in small savings, which was earlier included under loans from the Centre, is now included under internal debt and shown as special securities issued to the National Small Saving Fund (NSSF) of the Central Government. The data for the years prior to 1999-2000 as reported in this table, however, exclude loans against small savings for the purpose of comparison.

Note : Figures in parentheses are percentages to GDP.

4.61 Capital outlay would be compressed in 2004-05 but would remain higher as a ratio to GDP than the level in the 1990s. Developmental expenditure is budgeted to decline, while there would be no let-up in the increase in non-developmental expenditure. Consequently, while the ratio of developmental expenditure to GDP would decline in 2004-05, the non-developmental expenditure-GDP ratio would remain stable (Table 4.24).

Table 4.24: Expenditure Pattern of the State Governments

(Rupees Crore)

Item	2004-05 (BE)	2003-04 (RE)	2003-04 (BE)	2002-03	2000-02 (Average)	1995-00 (Average)	1990-95 (Average)	Percentage variations Col.2/3	Col.3/4
1	2	3	4	5	6	7	8	9	10
Total Expenditure (1+2 =3+4+5)	5,42,824	5,51,956	4,84,552	4,19,450				-1.7	13.9
	(17.4)	(19.9)	(17.7)	(17.0)	(16.6)	(15.3)	(16.0)		
1. Revenue Expenditure	4,15,687	3,99,541	3,79,513	3,32,563				4.0	5.3
of which :	(13.3)	(14.4)	(13.8)	(13.5)	(13.9)	(12.6)	(12.8)		
Interest payments	91,648	83,724	82,667	69,966				9.5	1.3
	(2.9)	(3.0)	(3.0)	(2.8)	(2.6)	(2.0)	(1.7)		
2. Capital Expenditure	1,27,137	1,52,415	1,05,039	86,887				-16.6	45.1
of which :	(4.1)	(5.5)	(3.8)	(3.5)	(2.7)	(2.7)	(3.2)		
Capital outlay	56629	60,751	55160	36209				-6.8	10.1
	(1.8)	(2.2)	(2.0)	(1.5)	(1.5)	(1.4)	(1.6)		
3. Development Expenditure	2,80,823	2,99,357	2,67,030	2,27,034				-6.2	12.1
	(9.0)	(10.8)	(9.7)	(9.2)	(9.8)	(9.6)	(10.8)		
4. Non-Development Expenditure	1,99,065	1,76,821	1,76,009	1,50,264				12.6	0.5
	(6.4)	(6.4)	(6.4)	(6.1)	(5.9)	(4.9)	(4.3)		
5. Others	62,936	75,778	41,513	42,152				-16.9	82.5
	(2.0)	(2.7)	(1.5)	(1.7)	(0.9)	(0.7)	(0.9)		

BE : Budget Estimates. RE : Revised Estimates.

Note : Figures in parentheses are percentages to GDP.

Table 4.25: Decomposition and Financing Pattern of Gross Fiscal Deficit of the States

(Per cent)

Item	2004-05 (BE)	2003-04 (RE)	2003-04 (BE)	2002-03	2000-02 (Average)	1995-00 (Average)	1990-95 (Average)
1	2	3	4	5	6	7	8
Decomposition (1+2+3)	100.0	100.0	100.0	100.0	100.0	100.0	100.0
1. Revenue Deficit	43.0	51.5	42.1	54.0	60.7	44.7	24.7
2. Capital Outlay	50.4	43.3	47.5	35.5	34.2	43.2	55.3
3. Net Lending	6.6	5.2	10.4	10.5	5.1	12.1	20.0
Financing (1+2+3+4+5)	100.0	100.0	100.0	100.0	100.0	100.0	100.0
1. Special Securities issued to the NSSF	53.5	41.6	43.2	49.7	36.8	5.8	–
2. Market Borrowings	23.0	32.1	14.5	27.9	16.0	16.1	16.0
3. State Provident Fund	10.9	8.2	9.3	9.6	10.2	13.4	14.3
4. Loans from the Centre	-6.5	-15.1	6.7	-1.8	13.5	40.6	49.0
5. Others	19.1	33.2	26.3	14.6	23.6	24.0	20.7

BE : Budget Estimates. RE : Revised Estimates. – : Not applicable.

4.62 Small savings are expected to continue to be the major source of financing of the States' GFD in 2004-05. The shares of market borrowings and 'others' including loans from banks and financial institutions are budgeted to decline in 2004-05 from the revised estimates of 2003-04 (Table 4.25).

4.63 To sum up, while the State budgets for 2004-05 seek to carry forward the reform process initiated in the recent past, it is evident that the structural weaknesses in their finances continue to circumscribe resource allocation towards developmental ends. A renewed emphasis on fiscal empowerment coupled with progressive adoption of fiscal responsibility legislation by all the State Governments could expedite the attainment of developmental goals.

Combined Budgets for 2004-05

4.64 The continued efforts towards fiscal consolidation were reflected in the lower projections for the combined gross fiscal deficit, the revenue deficit and the primary deficit in 2004-05 as compared with the revised estimates for 2003-04 (Table 4.26)[3]. This reduction is sought to be achieved through an acceleration in tax collections and a moderation in the growth of aggregate expenditure.

Table 4.26: Measures of Deficit - Central and the State Governments

Year	(Rupees crore)			(Per cent to GDP)		
	Gross Fiscal Deficit	Revenue Deficit	Primary Deficit	Gross Fiscal Deficit	Revenue Deficit	Primary Deficit
1	2	3	4	5	6	7
1990-91	53,580	23,871	28,585	9.4	4.2	5.0
1995-96	77,671	37,932	18,598	6.54	3.2	1.6
1996-97	87,244	48,768	17,156	6.38	3.6	1.3
1997-98	1,10,743	62,782	32,466	7.3	4.1	2.1
1998-99	1,57,053	1,10,618	63,956	9.0	6.4	3.7
1999-2000	1,84,826	1,21,393	74,375	9.5	6.3	3.8
2000-01	1,99,852	1,38,803	75,035	9.5	6.6	3.6
2001-02	2,26,418	1,59,395	84,048	9.9	7.0	3.7
2002-03	2,34,923	1,63,052	76,475	9.5	6.6	3.1
2003-04 BE	2,59,200	1,61,116	83,333	9.4	5.9	3.0
2003-04 RE	2,60,217	1,72,100	80,214	9.4	6.2	2.9
2004-05 BE	2,46,345	1,24,430	54,637	7.9	4.0	1.7

BE : Budget Estimates. RE: Revised Estimates.

[3] Data in respect of State Budgets are provisional.

Table 4.27: Combined Receipts and Disbursements of the Centre and the States

(Rupees crore)

Item	2004-05 (BE)	2003-04 (RE)	Variation (Col. 2/Col.3)	
			Absolute	Per cent
1	2	3	4	5
I. Total Receipts (A+B)	**8,98,290** **(28.8)**	**8,72,973** **(31.5)**	**25,317**	**2.9**
A. Revenue Receipts (1+2)	6,05,401	5,29,248	76,153	14.4
1. Tax Receipts	4,94,232	4,15,283	78,949	19.0
a) Direct Taxes	1,57,454	1,21,970	35,484	29.1
b) Indirect Taxes	3,36,777	2,93,313	43,464	14.8
2. Non-tax receipts	1,11,169	1,13,965	-2,796	-2.5
B. Capital Receipts	2,92,889	3,43,725	-50,836	-14.8
II. Total Disbursements (A+B)	**8,98,819** **(28.8)**	**8,85,293** **(31.9)**	**13,526**	**1.5**
A. Developmental Expenditure	4,28,266	4,39,465	-11,199	-2.5
B. Non-Developmental Expenditure (Including others)	4,70,553	4,45,827	24,726	5.5

BE : Budget Estimates. RE: Revised Estimates.

Note: Figures in parentheses are percentages to GDP.

4.65 Combined revenue receipts are budgeted to register a substantial growth during 2004-05, solely on account of a rise in tax collections. The combined tax-GDP ratio of the Centre and the States is, accordingly, anticipated to register an improvement of 0.8 percentage points of GDP during 2004-05. The non-tax revenue, on the other hand, is budgeted to decline over the revised estimates for 2003-04. On the expenditure side, the share of non-developmental expenditure is budgeted to be higher than in the revised estimates for 2003-04 (Table 4.27).

4.66 Of the combined gross fiscal deficit, 47.2 per cent is budgeted to be financed through market borrowings. The share of small savings is budgeted to decline. The share of external financing will be relatively insignificant (Table 4.28).

Table 4.28: Financing of Gross Fiscal Deficit of the Centre and the States

(Rupees crore)

Year	Market Borrowings (Net)	State Provident Fund	Small Savings	External Borrowings	Others	Gross Fiscal Deficit
1	2	3	4	5	6	7
2002-03	1,32,587 (56.4)	11,654 (5.0)	52,261 (22.2)	-11,934 (-5.0)	50,355 (21.4)	2,34,923 (100.0)
2003-04 BE	1,24,034 (47.8)	14,696 (5.7)	60,000 (23.1)	3,582 (1.4)	56,888 (21.9)	2,59,200 (100.0)
2003-04 RE	1,30,745 (50.2)	13,977 (5.4)	124,900 (48.0)	-11,705 (-4.6)	2,300 (0.9)	2,60,217 (100.0)
2004-05 BE	1,16,170 (47.2)	12,991 (5.3)	71,800 (29.1)	8,076 (3.2)	37,308 (15.1)	2,46,345 (100.0)

RE : Revised Estimates. BE : Budget Estimates.

Note: Figures in parentheses are percentages to GFD.

Outlook

4.67 The policy objectives for 2004-05 are to build upon the fiscal consolidation, *albeit* modest, achieved in 2003-04. The deepening of tax reforms, reorienting expenditure towards thrust areas and enhancing investment should help in attaining the goals set under the FRBM Act, 2003. The commitment to eliminate the revenue deficit as stipulated by the FRBM Act, 2003 and generation of revenue surplus for further investment is consistent with the envisaged improvement in the tax-GDP ratio. In this context, the focus is on expanding scope of the services tax by bringing newer services within the purview of taxation. On the expenditure front, non-plan expenditure is sought to be pruned by plugging leakages and by targeting subsidies at the needy. Public investments in infrastructure, both economic and social, are to be stepped up with an improved mechanism for delivery of infrastructural services. The Centre may be able to continue with the policy of managing the debt prudently through the debt-swap scheme and refinancing to reduce the interest burden. The FRBM Rules, 2004 would facilitate the reduction of total liabilities of the Centre.

4.68 At the States' level, the emerging fiscal scenario, as reflected in the revised estimates for 2003-04, indicates the persistence of structural infirmities, *albeit* with some improvement in the orientation of expenditure. A renewed emphasis on fiscal empowerment is reflected in the major policy initiatives contained in the State Budgets for 2004-05. These include perseverance with fiscal reforms, revenue augmentation and expenditure containment, reforms in tax administration, improvement in recovery of user charges, restructuring of SPSUs, enhancing transparency in budgetary operations, emphasis on infrastructure development and reduction and management of States' debt. The debt swap scheme and availing of loans from external agencies on the same terms and conditions as the Centre would reduce the debt burden of the States.

V FINANCIAL MARKETS

5.1 A broad based rally in global financial markets in 2003-04 was characterised by rising equity prices, decline in bond spreads, a rebound in financial flows to emerging markets, improved corporate finances and increased appetite for risks by investors. The Morgan Stanley Capital International (MSCI) World index gained 23 per cent in 2003 and a further 3 per cent during the first two months of 2004. The pattern of investment flows generally implied an allocation of funds away from relatively low-yielding assets in favour of riskier investments. Equity and debt prices in emerging markets outperformed most other markets. A combination of abundant liquidity and improved fundamentals buoyed global asset prices. Net issuances in international debt securities markets were distinctly higher at US $ 1,467 billion in 2003, as compared with US $ 1,011 billion in 2002, and were made largely by emerging market economies.

5.2 Against this background, financial markets in India were also characterised by ample liquidity during 2003-04 mainly due to persistent external capital flows. A steady appreciation of the rupee against the US dollar in the spot segment of the foreign exchange market generated unidirectional upside expectations which dominated the forward segment. In the Government securities market, there was a persistent rally in prices, interrupted by open market operations (OMO) and a hardening of inflation expectations in the last quarter of the year. In the market for bank credit, falling deposit rates nudged the stickier lending rates down. Equity markets regained vibrancy with intermittent corrections.

5.3 This Section sets out developments in various segments of domestic financial markets in 2003-04. In respect of the money market, it highlights synchronous movement of key interest rates and their ruling at sub-repo levels. As regards the Government securities market, the review points to the softening of yields during the year with the yield curve steepening in the second half of the year in the wake of rising inflationary expectations, hardening of international interest rates and profit booking by investors. Yields on corporate bonds declined alongside a widening of spreads. In the credit market, the focus is on the pick-up in activity with banks cutting deposit and lending rates, the latter exhibiting downward inflexibility. Introduction of the benchmark prime lending rate (BPLR) system by banks in the fourth quarter of the year led to some rationalisation in prime lending rates. An overview of the foreign exchange market shows the impact of persistent excess supply conditions - the rupee faced upward pressure *vis-á-vis* the US dollar throughout the year and the forward premia turned into discounts in the third quarter before firming up marginally towards the close of the year. The profile of capital markets reflects a revival in the primary segment, particularly in the public issues market, significantly higher resource mobilisation by mutual funds and a turnaround in the financial assistance disbursed by financial institutions. The secondary segment of the capital market remained generally buoyant, attracting a record flow of foreign institutional investment (Table 5.1).

MONEY MARKET

Call/Notice Money Market

5.4 Activity in the call/notice money market ebbed during 2003-04 with call rates ruling persistently below the LAF repo rate, except in isolated episodes. The surplus liquidity at the beginning of the year drew heavy bidding at the LAF repo auctions (Appendix Table V.1). Call rates inched up in June 2003, with the outflows on account of the usual end-of-the-quarter advance tax payments by corporates and market borrowings by the Centre and the State Governments. Consequent upon a reduction in the cash reserve ratio (CRR) by 25 basis points in June 2003 and continuing external capital inflows, call rates eased and settled below the repo rate in July 2003 (Chart V.1).

5.5 Market participants built up surplus cash positions in anticipation of redemption of Resurgent India Bonds (RIBs) leading to the Reserve Bank trebling the notified amount of 91-day Treasury Bills in the auctions during August-September 2003. Call rates turned somewhat volatile for a brief period in August 2003. With the 50 basis points cut in the LAF repo rate on August 25, 2003 stability returned to the market, accompanied by a softening of call rates. Advance tax outflows, unsettled expectations surrounding the RIB redemptions and a build up of surplus cash balances of the Government with the Reserve Bank led to some edging up of call rates towards the last week of September 2003, prompting the Reserve Bank to

Table 5.1: Financial Markets at a Glance

Month	Call Money		Gilt	Foreign Exchange				Liquidity Management		Equity			
	Average Daily Turnover (Rs. crore)	Average Call Rates* (Per cent)	Turnover in Govt. Securities (Rs. crore)+	Average Daily Inter-bank Turnover (US $ million)	Average Exchange Rate (Rs. per US $)	RBI's net Foreign Currency Sales (-)/ Purchases(+) (US $ million)	Average Forward Premia 3-month (Per cent)	Net OMO Sales(-) Purchases (+) (Rs. crore)	Average Daily Repos (LAF)# (Rs. crore)	Average Daily BSE Turnover (Rs. crore)	Average Daily NSE Turnover (Rs. crore)	Average BSE Sensex**	Average S & P CNX Nifty**
1	2	3	4	5	6	7	8	9	10	11	12	13	14
2003-04													
April	17,338	4.87	2,26,803	5,585	47.38	1,432	2.08	-7	27,372	1,041	2,449	3037	965
May	18,725	4.87	2,99,933	5,960	47.08	2,342	1.10	-5,569	25,223	1,072	2,604	3033	963
June	20,544	4.91	3,00,504	5,837	46.71	897	2.76	-44	24,805	1,187	2,933	3387	1069
July	18,698	4.90	3,04,587	5,920	46.23	3,146	2.65	-57	42,690	1,434	3,429	3665	1150
August	19,556	4.83	4,09,539	5,983	45.93	2,352	2.25	-11,546	39,995	1,817	4,267	3978	1261
September	20,584	4.50	2,65,848	6,862	45.85	2,345	0.91	-5,107	31,373	2,032	4,698	4315	1369
October	23,998	4.64	3,89,968	7,672	45.39	1,593	0.02	-13,986	13,569	2,288	5,026	4742	1506
November	15,156	4.38	1,77,063	6,795	45.52	3,449	(-) 0.002	-69	21,182	2,251	4,644	4951	1580
December	15,276	4.40	1,81,991	6,207	45.59	2,888	(-) 0.30	-132	32,020	2,492	5,017	5425	1740
January	14,189	4.43	1,81,619	7,306	45.46	3,294	0.50	-5,228	38,539	3,125	6,394	5954	1906
February	9,809	4.33	1,39,130	7,171	45.27	3,357	0.51	-35	46,244	2,709	5,722	5827	1849
March	12,422	4.37	2,22,685	8,018	45.02	3,382	0.62	-69	54,915	2,308	4,767	5613	1780
2004-05													
April	12,916	4.29	3,00,864	10,118 P	43.93	7,427	-0.35	-253	75,218	2,243	5,048	5809	1848
May	10,987	4.30	1,92,264	8,521 P	45.25	-220	-1.33	-116	74,502	2,188	4,710	5205	1640
June	10,972	4.35	1,75,802	7,741 P	45.51	-413	0.93	-60	61,981	1,681	3,859	4824	1506
July	8,632	4.31	1,30,400	7,684 P	46.04	-1,180	2.25	-230	57,876	1,793	4,265	4973	1568

OMO : Open Market Operations. + : Outright turnover in Central Government dated securities. LAF : Liquidity Adjustment Facility.
BSE : The Stock Exchange, Mumbai. NSE : National Stock Exchange of India Ltd. P : Provisional.
* : Average of daily weighted average call money borrowing rates. ** : Average of daily closing indices. # : Outstanding

reduce the notified amount of 91-day Treasury Bills. Contrary to initial apprehensions, redemption of RIBs on October 1, 2003 did not strain the money market with liquidity conditions remaining comfortable. OMO sales and a series of 28-day repo auctions conducted by the Reserve Bank in the second half of October caused call rates to spike above 6.0 per cent towards the end of the month. Liquidity generated by large capital inflows brought down call rates to sub-repo levels for the remaining part of the year with some isolated dips in February 2004 due to unsterilised capital flows. Over the year, volatility in the call/notice money market declined and was accompanied by a reduction in turnover on account of abundant liquidity (Table 5.2). A part of call/notice money market activity migrated to the repo market (outside the LAF) and to the Collateralised Borrowing and Lending Obligations (CBLO) segment on account of cheaper availability of funds *vis-á-vis* the call/notice money market. Primary dealers (PDs), whose demand is related to the volume of the Government's market borrowing programme, emerged as the largest class of borrowers in the call/notice money market in 2003-04.

5.6 The year 2004-05 commenced with large volumes of liquidity in the system keeping the call rates below the repo rate during April 2004. Despite absorptions under the Market Stabilisation Scheme (MSS) and advance tax outflows in June, liquidity conditions continued to remain comfortable as reflected in large outstanding volumes under the LAF.

Chart V.1 : Call Rate and Repo Rate

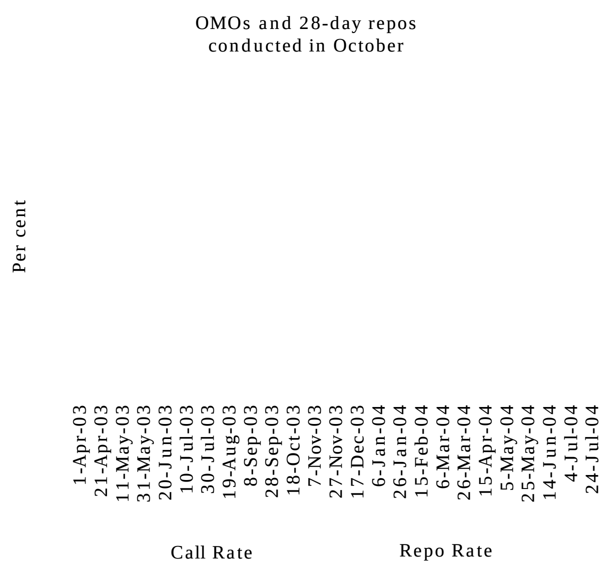


Table 5.2: Call/Notice Money Market Borrowing Rates – Summary Statistics

	Low				High				Weighted Average			
	Min. (per cent)	Max. (per cent)	Avg. (per cent)	CV	Min. (per cent)	Max. (per cent)	Avg. (per cent)	CV	Min. (per cent)	Max. (per cent)	Avg. (per cent)	CV
1	2	3	4	5	6	7	8	9	10	11	12	13
2002-03	**0.50**	**6.50**	**4.59**	**0.17**	**5.20**	**20.00**	**6.36**	**0.15**	**5.01**	**10.35**	**5.89**	**0.09**
2003-04	**1.00**	**5.25**	**3.39**	**0.18**	**4.50**	**12.00**	**4.89**	**0.13**	**3.99**	**6.21**	**4.62**	**0.06**
April	1.00	5.25	2.94	0.38	5.05	12.00	5.73	0.30	4.50	6.03	4.87	0.07
May	1.80	4.00	3.32	0.25	5.00	5.25	5.10	0.01	4.46	4.97	4.87	0.02
June	2.00	4.00	3.60	0.15	4.88	5.50	5.11	0.02	4.56	4.99	4.91	0.02
July	2.25	4.00	3.70	0.14	5.00	5.50	5.07	0.02	4.75	4.97	4.90	0.01
August	3.00	4.05	3.70	0.10	4.55	6.25	5.09	0.06	4.22	5.07	4.83	0.05
September	3.00	4.00	3.50	0.04	4.55	5.10	4.70	0.03	4.42	4.64	4.50	0.01
October	1.00	4.00	3.32	0.16	4.60	7.00	5.13	0.15	4.44	6.21	4.64	0.09
November	1.50	3.52	3.12	0.14	4.50	4.70	4.60	0.01	4.21	4.50	4.38	0.02
December	2.00	3.75	3.25	0.12	4.50	4.97	4.55	0.02	4.30	4.47	4.40	0.01
January	2.00	3.85	3.52	0.14	4.50	6.50	4.59	0.08	4.23	4.49	4.43	0.01
February	2.00	3.85	3.32	0.17	4.50	4.85	4.55	0.02	3.99	4.42	4.33	0.02
March	2.00	3.97	3.29	0.15	4.50	4.60	4.53	0.01	4.21	4.44	4.37	0.01
2004-05												
April	1.00	3.80	3.09	0.22	4.50	4.55	4.52	0.01	4.01	4.42	4.29	0.02
May	2.00	3.75	3.14	0.17	4.50	7.50	4.61	0.12	4.16	4.67	4.30	0.02
June	2.50	4.00	3.51	0.10	4.50	6.25	4.61	0.07	4.18	4.74	4.35	0.02
July	2.00	3.80	3.41	0.10	3.51	4.80	4.48	0.04	4.13	4.41	4.31	0.01

Min.: Minimum. Max: Maximum. Avg.: Average. CV: Coefficient of Variation.

Call rates remained generally easy, hovering in the range of 4.0-4.5 per cent during 2004-05 (up to July) except for some firming up during the late hours on May 28 and June 4 due to heavy outflow of funds on account of MSS operations. Turnover in the call money market declined during May, June and July 2004, reflecting the continued shifts in activity away from the uncollateralised segment. Call rates firmed up for a few days during the second week of August 2004 due to outflow of funds on accounts of surplus balances of Central Government with the Reserve Bank, auctions of Central Government dated securities and withdrawal of funds by mutual funds due to redemption pressure. Call rates returned to sub-repo levels by mid-August 2004.

Term Money Market

5.7 Recent money market reforms encompassing development of the repo market, introduction of exposure limits for banks in the call/notice money market segment and the calibrated phase out of non-banks from the call market have begun to infuse vibrancy into various money market segments. The average daily turnover in the term money market rose by 52 per cent to Rs.519 crore in 2003-04 from 341 crore in 2002-03, driven by the reform measures (Table 5.3). During the year 2004-05 (up to July 2004), the average daily turnover declined to Rs.288 crore.

Certificates of Deposit

5.8 The significant increase in the outstanding amount of certificates of deposit (CDs) in 2003-04 essentially reflected issuances by some banks with low deposit bases. Furthermore, the exemption of investments in CDs by banks from the restrictions on non-SLR investments below one year also supported the CD market. The reduction in stamp duty on CDs, effective March 1, 2004 and withdrawal of the facility of premature closure of deposits in respect of CDs were other factors that boosted activity in the market, providing greater opportunity for secondary market trading. Investment in CDs by mutual funds also increased on account of their improved funds position. An encouraging development was that some banks got their CDs rated for gaining better access to the market even when such rating was not mandatory under the extant guidelines. The typical discount rate (for 3-month maturity) on CDs softened from 7.20 per cent in mid-April 2003 to 5.50 per cent by end-August 2003 and further to 4.96 per cent by mid-March 2004 in

Table 5.3: Activity in Money Market Segments (other than Call/Notice Money)

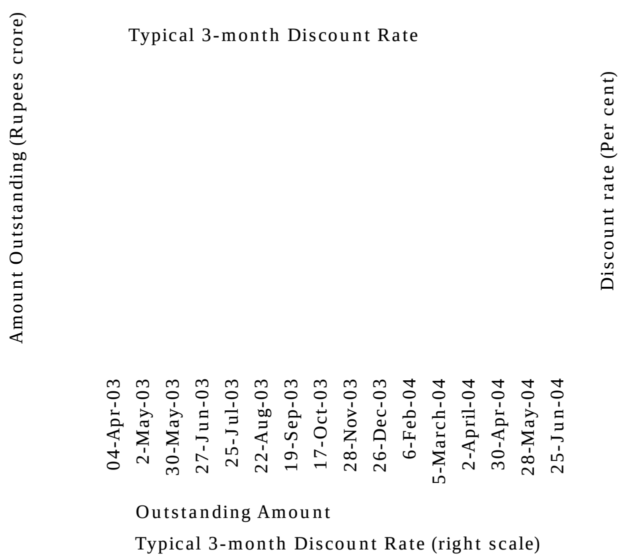
(Rupees crore)

Month	Average Daily Turnover in Term Money Market	Average Daily Turnover in Repo Market (Outside Reserve Bank)	Commercial Paper (Outstanding Amount)	Certificates of Deposit (Outstanding Amount)	Commercial Bills Rediscounted by Commercial Banks	Forward Rate Agreements/ Interest Rates Swaps (Notional Amount)	Average Daily Turnover in Collateralised Borrowing and Lending Obligation (CBLO)
1	2	3	4	5	6	7	8
2003-04							
April	604	5,575	5,994	1,485	164	2,49,449	47
May	455	5,591	6,820	1,996	334	2,84,048	41
June	610	6,481	7,108	2,183	393	2,93,127	37
July	573	9,669	7,557	2,466	364	3,05,409	126
August	644	9,528	7,646	2,961	693	3,14,708	16
September	772	9,525	7,258	3,098	644	3,33,736	234
October	543	11,542	6,845	3,321	354	3,83,866	156
November	428	12,910	7,956	3,666	429	4,05,102	248
December	403	12,939	8,762	3,830	469	4,31,597	363
January	482	15,426	9,562	4,419	791	4,86,571	708
February	343	12,660	9,379	4,656	1,234	4,89,701	1,693
March	376	13,378	9,131	4,461	305	5,18,260	2,506
2004-05							
April	325	15,195	9,706	4,725	330	5,13,760	2,496
May	372	15,932	10,328	4,860	370	6,11,595	3,872
June	274	17,517	10,910	5,438	n.a.	n.a.	4,015
July	182	19,226	10,898	n.a.	n.a.	n.a.	4,508

n.a. : Not available.

line with the general softening of interest rates (Chart V.2). During 2004-05 (up to June 25, 2004), the discount rate further softened to 4.5 per cent. The outstanding CDs continued to increase during the first quarter of 2004-05 (Appendix Table V.2).

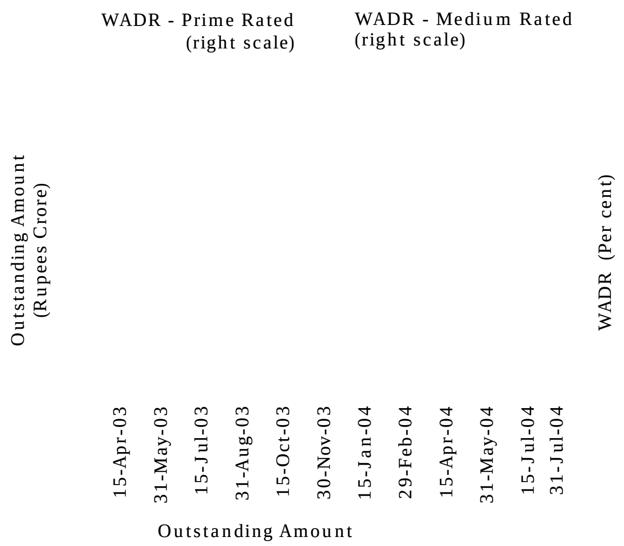
Chart V.2 : Certificates of Deposit Market



Commercial Paper

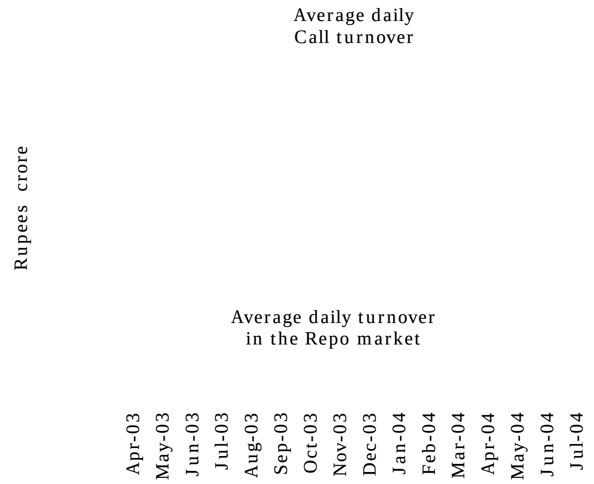
5.9 Easy liquidity conditions prompted companies to mobilise large volume of funds through commercial paper (CP). The outstanding amount of CP increased by about 59 per cent during 2003-04 (Appendix Table V.3). The issuance of CP picked up from mid-November 2003 on account of increased interest by mutual funds and banks in the wake of the guidelines by the SEBI and the Reserve Bank barring investments in non-SLR debt securities with original maturity up to one year except in CP and CDs (Chart V.3). Furthermore, reduction in stamp duty on CP also buoyed up the market. The discount rates on CP joined other short-term rates in easing through the year from a range of 5.25-8.15 per cent to 4.70-6.50 per cent. During 2004-05 (up to end-July 2004), the discount rates further declined to 4.60-5.60 per cent. The weighted average discount rate (WADR) also declined from 6.20 per cent at the beginning of April 2003 to 5.11 per cent as at end of March 2004 and further to 4.86 per cent as at end-July 2004. The spread of the WADR between the prime-rated and medium-rated companies narrowed from 162 basis points as at end-April 2003 to 73 basis points by end-March 2004 but increased marginally to 87 basis

Chart V.3 : Commercial Paper Market



WADR : Weighted Average Discount Rate.

Chart V.4 : Turnover in Call/Notice Market and Repo Market outside the Reserve Bank



points by end-June 2004. The spread, however, again narrowed to 29 basis points by end-July 2004. The most preferred maturities of CP were ‘up to 90 days’ and ‘181 days and above’. The share of manufacturing and other companies in the average outstanding amount of CP stood lower at 22 per cent in 2003-04 (35 per cent in 2002-03), while the shares of finance/ leasing companies and financial institutions rose to 49 per cent and 29 per cent, respectively, from 41 per cent and 24 per cent, a year ago.

5.10 The market for CP continued to remain buoyant during 2004-05 (up to end-July 2004) with issuances of CP aggregating Rs.8,052 crore as against Rs.7,293 crore during the corresponding period of the previous year. The share of ‘manufacturing and other companies’ and financial institutions in the outstanding amount of CP stood lower at 24 per cent and 15 per cent, respectively, while that of finance/leasing companies was higher at 61 per cent.

Repurchase Agreements (Outside the LAF)

5.11 Tightening of prudential norms relating to the call exposure of banks and gradual phasing out of non-bank participants from the call market led to increased activity in the repo market (outside the LAF) (Chart V.4). During 2003-04, the monthly average volume of repo transactions increased by 69.6 per cent to Rs.79,628 crore over the previous year. The share of repo in total transactions (outright and repos) increased to 36.8 per cent in 2003-04 from 30.6 per cent in 2002-03. Apart from banks, mutual funds and financial institutions were the main participants in the repo market (outside the LAF). The repo rates ranged between 3.00 per cent and 5.05 per cent during the year barring occasional spikes.

5.12 The volume of repo transactions increased by 43.7 per cent to Rs.1,49,000 crore in July 2004 over end-March 2004 as compared with 1.0 per cent in the corresponding period of the previous year due to sizable deployment by mutual funds, private banks and financial institutions. Interest rates in most of the transactions ranged from 3.0 per cent to 4.5 per cent. Average share of repo transactions in the total market volume during the year 2004-05 (up to July 2004) also improved to 51.9 per cent as compared with 25.5 per cent in the corresponding period of the previous year.

Forward Rate Agreements (FRAs)/Interest Rate Swaps (IRS)

5.13 There was a sharp increase in the volume in FRAs/IRS market during 2003-04, both in terms of number of contracts and outstanding notional principal amounts. The number of contracts rose from 9,363 to 19,867, while the outstanding amount rose from Rs.2,42,983 crore to Rs.5,18,260 crore during the period April 4, 2003 to March 19, 2004. The participation in the market was broad based and included public sector banks, PDs, foreign banks and private sector banks. In a majority of these contracts, the National Stock Exchange-Mumbai Inter-bank

Box V.1

Evolution of Money Market in India

The evolution of the money market in India could be traced to the late 1980s when the Working Group on Money Market (Chairman: N. Vaghul) made a series of recommendations for developing various segments of the money market. The administered interest rate system in the money market was dismantled. A series of measures were undertaken to build the institutional infrastructure for the money market. The Discount and Finance House of India (DFHI) was established in 1988 to promote secondary market activity in money market instruments, followed by a system of primary dealers in 1996 as a mechanism for developing the gilt market. The segment for Certificates of Deposit came into being in 1989. The money market expanded further to cover segments for Commercial Paper (1990), Repos with Reserve Bank (1992), Market Repos, Forward Rate Agreements/Interest Rate Swaps (1999) and Collateralised Borrowing and Lending Obligation (CBLO) (2003). The development of the payment system infrastructure was strengthened with the formation of the Clearing Corporation of India Ltd. (CCIL) in April 2002, introduction of the Negotiated Dealing System (NDS) in February 2002 and the implementation of real time gross settlement (RTGS) system from April 2004.

The profile of the money market has also been changing in the recent period. There have been indications of a more balanced development of the money market. Participants have been increasingly switching from the uncollateralised call/notice money market to the collateralised segments, driven by standardisation of accounting practices, broad basing of eligibility criteria, the gradual phasing out of non-banks from the call market and lower CRR requirements. In recent years, although the call money and the repo markets continued to be dominated by a few top lenders, they were not able to extract monopoly rents as call rates and market repo rates persistently ruled below the Reserve Bank's repo rate. While mutual funds have emerged as the largest supplier of funds in the repo and the CBLO markets, PDs are increasingly becoming the major borrowers in the call/notice money market.

The integration of various segments of the money market has improved after the introduction of the Liquidity Adjustment Facility (LAF). The correlation coefficient between interest rates of CDs, CPs, 91-day Treasury Bills and repo rate with the call money rate improved steadily from 0.32, 0.54, 0.61 and 0.36, respectively, during the period April 1993 to May 2000 to 0.93, 0.90, 0.95 and 0.87 during June 2000 to June 2004. Correlation coefficients turned out to be lower after netting out the repo rate reflecting the influence of the LAF in promoting money market integration. The integration of money market segments was further validated by confirmation of the existence of cointegrated relationships among money market rates. The degree of cointegration has strengthened in the recent period, *i.e.*, June 2000 to June 2004.

Reference

1. Reserve Bank of India (1987), *Report of the Working Group on the Money Market.*

Offered Rate (NSE-MIBOR) and Mumbai Inter-bank Forward Offered Rate (MIFOR) were used as the benchmarks. Other benchmark rates used were secondary market yields of the Government securities with residual maturity of one-year and primary cut-off yield on 364-day Treasury Bills. Activity in FRAs/IRS is expected to pick up after the regulatory and prudential norms for over-the-counter (OTC) and exchange traded derivatives are harmonised by the Reserve Bank. During 2004-05, the number of contracts rose further to 23,331 and the outstanding amount moved up to Rs.6,11,595 crore as on May 28, 2004.

Collateralised Borrowing and Lending Obligation

5.14 Collateralised Borrowing and Lending Obligation (CBLO) was operationalised as a money market instrument through the Clearing Corporation of India Limited (CCIL) on January 20, 2003. The CBLO can have an original maturity between one day and up to one year. Activity in this segment has gradually picked up in recent months with increasing supply of funds from mutual funds and demand for funds by banks and primary dealers. The daily average turnover in CBLO increased from Rs.47 crore in April 2003 to Rs.2,506 crore in March 2004. By March 2004, about 50 members were admitted to the CCIL's CBLO segment. To encourage activity in this segment, banks' borrowings through CBLO were exempted from CRR, subject to banks maintaining the minimum CRR of 3 per cent. During 2004-05 (up to July 2004), the daily average turnover increased substantially to Rs.4,508 crore with the weighted average rate working out to 3.96 per cent (Box V.1).

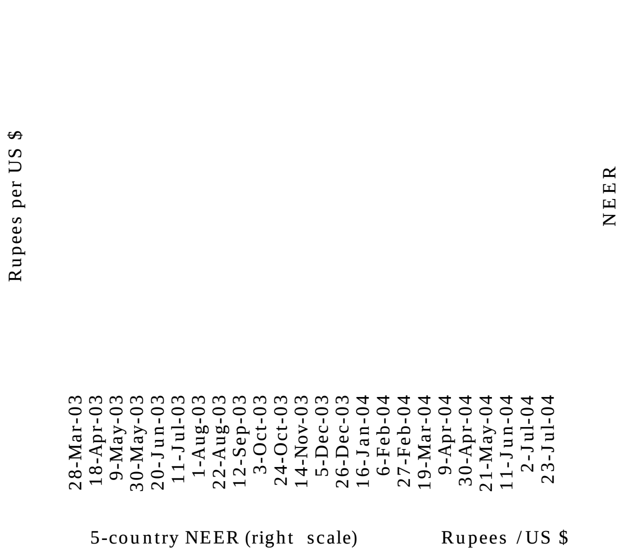
FOREIGN EXCHANGE MARKET

5.15 Excess supply conditions dominated the foreign exchange market during the major part of 2003-04, reflecting a sustained expansion of the current account surplus in the balance of payments and a surge in capital inflows. Large scale purchases by the Reserve Bank to absorb excess supplies in the foreign exchange market assuaged the strong upward pressures on the exchange rate. Despite these interventions, the Indian rupee appreciated by 9.3 per cent against the US dollar during 2003-04. This was counter balanced by the weakening of the rupee against other major currencies in tandem with the US dollar. Consequently, the depreciation of the rupee in terms of the nominal effective exchange rate was relatively muted (Chart V.5).

5.16 In cross-currency trade, the rupee weakened against both the Euro and the Pound sterling, reflecting the movements of the rupee against the US dollar and movement of the US dollar *vis-á-vis* other major international currencies. While the US dollar depreciated against the Euro, Pound sterling and Japanese yen by 11.4 per cent, 14.3 per cent and 11.7 per cent, respectively, the Indian rupee depreciated against these three currencies by 3.2 per cent, 6.0 per cent and 4.3 per cent, respectively, over the year (Chart V.6).

5.17 Market sentiment remained buoyant during the first quarter of 2003-04 against the backdrop of rising foreign exchange reserves, stable international crude oil prices and the US dollar's weakness against other major currencies. Strong supplies came from higher exports, remittances and foreign institutional investments. Despite robust imports, demand for credit was deflected from the domestic market by an increasing recourse to relatively low cost external commercial borrowings and trade credits. The rupee gained against the US dollar, appreciating by 2.2 per cent in spite of net purchases of US $ 4.7 billion by the Reserve Bank during the first quarter (Table 5.4 and Appendix Table V.4).

Chart V.5 : Exchange Rate of the Rupee



NEER : Nominal Effective Exchange Rate

5.18 The rupee ranged between Rs.45.71 and Rs.46.49 per US dollar and appreciated by 1.4 per cent against the US dollar during the second quarter of 2003-04. Although steady inflows from foreign funds and other sources continued, uncertainties in the foreign exchange market and the Reserve Bank's net market purchases of US $ 7.8 billion kept the rupee range-bound. An imposition of ceiling on interest rate on non-resident external rupee (NRE) deposits in July followed by a lowering of interest rate ceiling in September and banning of investment by overseas corporate bodies (OCBs) owned by non-resident Indians (NRIs)/persons of Indian origin (PIOs) in the Indian stock market fuelled speculative expectations

Chart V.6 : Movement of Currencies

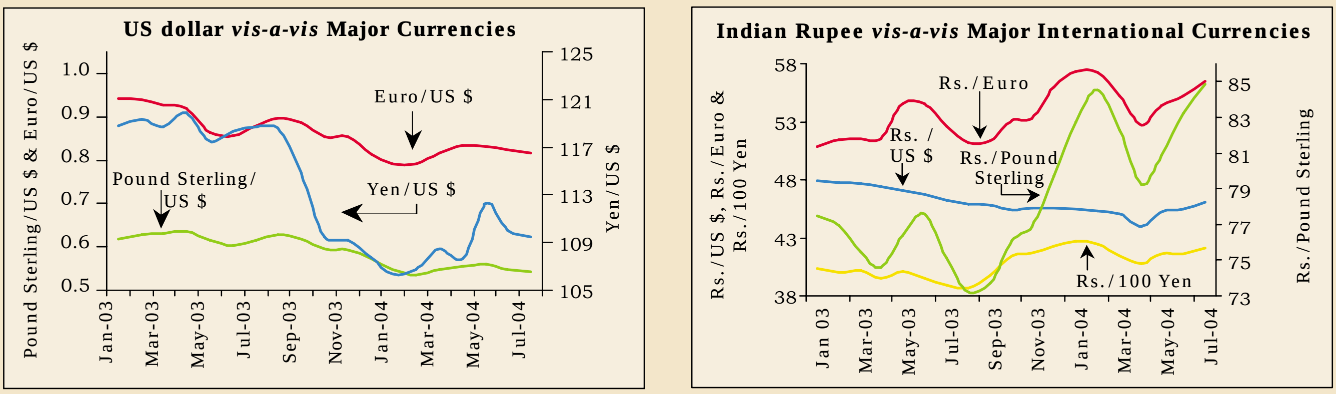


Table 5.4: Purchases and Sales of US dollars by the Reserve Bank

(US $ million)

Month	Purchases(+)	Sales (-)	Net@ (+/-)	Cumulative (over end-March)	Outstanding Net Forward Sales (-) / Purchases (+) (end of month)
1	2	3	4	5	6
2003-04					
April	2,943	1,511	1,432	(+)1,432	(+)3,281
May	3,978	1,636	2,342	(+)3,774	(+)4,186
June	1,879	982	897	(+)4,670	(+)3,866
July	6,096	2,950	3,146	(+)7,815	(+)4,549
August	3,712	1,360	2,352	(+)10,167	(+)4,803
September	6,574	4,229	2,345	(+)12,512	(+)1,412
October	6,821	5,228	1,593	(+)14,105	(+)981
November	4,029	580	3,449	(+)17,554	(+)518
December	3,373	484	2,888	(+)20,442	(+)740
January	4,322	1,028	3,294	(+)23,735	(+)1,101
February	5,520	2,163	3,357	(+)27,092	(+)763
March	6,171	2,789	3,382	(+)30,473	(+)1,392
2004-05					
April	10,759	3,332	7,427	(+) 7,427	(+) 311
May	3,220	3,440	(-) 220	(+) 7,207	(+)125
June	970	1,383	(-) 413	(+) 6,793	(+) 115
July	0	1,180	(-)1,180	(+) 5,614	(+) 115

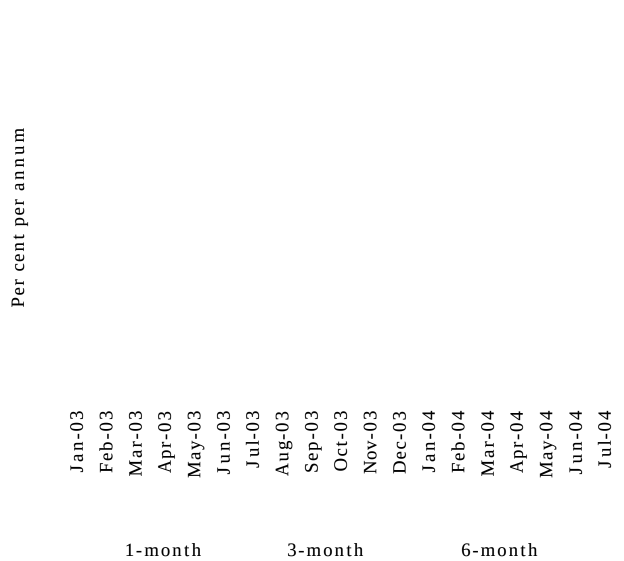
(+) : Implies purchases including purchase leg under swaps and outright forwards.
(-) : Implies sales including sale leg under swaps and outright forwards.
@ : Includes transactions under the Resurgent India Bonds (RIBs) and India Millennium Deposits (IMDs).
Note : This table is based on value dates.

of a slowdown in inflows. Furthermore, the building up of *nostro* balances in the run up to the redemption of the Resurgent India Bonds (RIBs) in early October 2003 exerted some pressure on the foreign exchange market. The Reserve Bank undertook forward purchases throughout the first half of 2003-04 in preparation of the RIB repayments. Strong export proceeds coupled with heavy inflows from FIIs helped to maintain easy liquidity conditions.

5.19 Forward premia fell as exporters continued to book forward sales in response to the strengthening of the rupee in the spot market. Easy liquidity conditions in the domestic money market also exerted downward pressure and the 3-month and the 6-month forward premia declined by 253 basis points and 184 basis points, respectively, during July-September 2003 (Chart V.7).

5.20 The smooth redemption of the RIBs, followed by the return flow of some part of the redemption proceeds, strengthened the rupee considerably in the first week of October 2003, aided by the continuing weakness of the US dollar against most major currencies. Sustained US dollar demand from corporates and importers amidst fears of slowdown in inflows on account of tightening of the external commercial borrowing (ECB) guidelines drove the

Chart V.7 : Forward Premia/Discount
(Monthly Averages)



rupee down by 59 paise or 1.3 per cent against the US dollar between November 14 and end-November 2003. It, however, bounced back against the US dollar in early December 2003 and the undertone in foreign exchange trading remained firm throughout the month on sustained investment flows from FIIs, steady inward remittances and a positive sovereign rating assigned by Standard & Poor's. The rupee moved in a narrow range of Rs.45.26-45.94 per US dollar and appreciated by 0.5 per cent during the third quarter of 2003-04, restrained by purchases of US $ 7.9 billion by the Reserve Bank.

5.21 In the forward segment, premia fell sharply across the maturity spectrum into discounts during November and December 2003 as exporters continued to offload forward positions. In January 2004, forward discounts turned into slender premia of less than 1.0 per cent for all maturities.

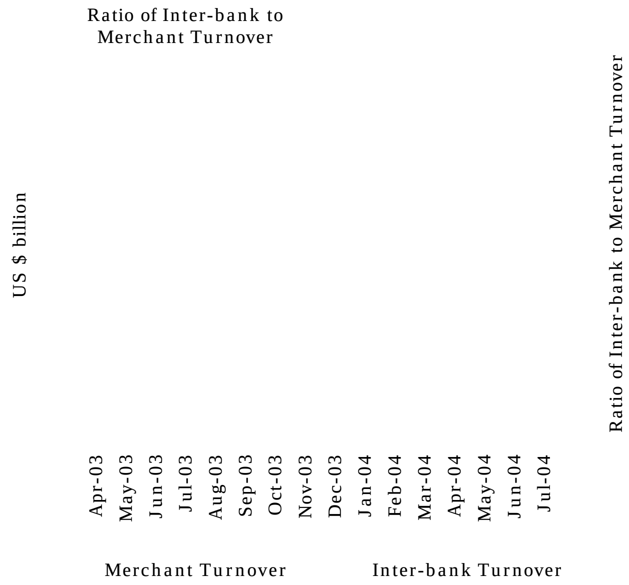
5.22 Liberalisation of the ECB regime, the impact of large export receivables, sustained FII inflows and upgrading of the country's long-term foreign currency rating by the Moody's Investor Services buoyed up the rupee in the last quarter of 2003-04 causing it to appreciate sharply by 5.0 per cent against the US dollar.

5.23 The Reserve Bank made net spot purchases of US $ 30.5 billion during the year. Outstanding net forward purchases, however, declined to US $ 1.4 billion at end-March 2004 from US $ 2.4 billion at end-March 2003, reflecting unwinding of forward purchases by the Reserve Bank built up to ensure smooth redemption of the RIBs.

5.24 Excess supply conditions ruled in the merchant segment. Net market purchases by authorised dealers (ADs) in the spot segment increased from US $ 512 million in April 2003 to US $ 2,692 million in March 2004 and from US $ 866 million in April 2003 to US $ 3,449 million in October 2003 in the forward segment before declining to US $ 1,695 million in March 2004. The average monthly turnover in the merchant segment of the foreign exchange market increased to US $ 40.5 billion in 2003-04 from US $ 27.0 billion in 2002-03. In the inter-bank segment, banks took positions in response to the merchant activity. The average monthly turnover in the inter-bank segment was high at US $ 134.2 billion as against US $ 103.0 billion in 2002-03. Consequently, the average monthly total turnover increased sharply to US $ 174.7 billion in 2003-04 from US $ 130.0 billion in the previous year. The inter-bank to merchant turnover ratio hovered in the range of 2.9-3.9 during the year, indicating orderly market conditions (Chart V.8).

5.25 The rupee came under pressure during May 2004 and reached Rs.45.96 per US dollar on May 17, 2004 on account of turbulence in the equity market, cash dollar shortage and rising global oil prices. FIIs sold heavily in the Indian equity market on that day. The Reserve Bank closely monitored

Chart V.8 : Foreign Exchange Market Turnover



developments across various financial market segments. A Task Force was constituted to keep a vigil on market developments. The Reserve Bank assured the market that it would continue to sell dollars through banks for augmenting supply in the foreign exchange market or would intervene directly to meet any demand-supply mismatches at the prevailing market rates. Furthermore, it was indicated that FIIs would remain free to reduce or increase their exposure in the Indian equity market at the prevailing market rates. The ADs, acting on behalf of these FIIs, were allowed to approach the Reserve Bank to buy foreign exchange at the prevailing market rates. The depreciation of the rupee continued in June-July 2004 on account of slowdown in capital inflows and higher demand for foreign exchange by corporates. As a result, the rupee depreciated by 6.5 per cent during April-July 2004 and traded in the range of Rs.43.57 – Rs.46.45 per US dollar.

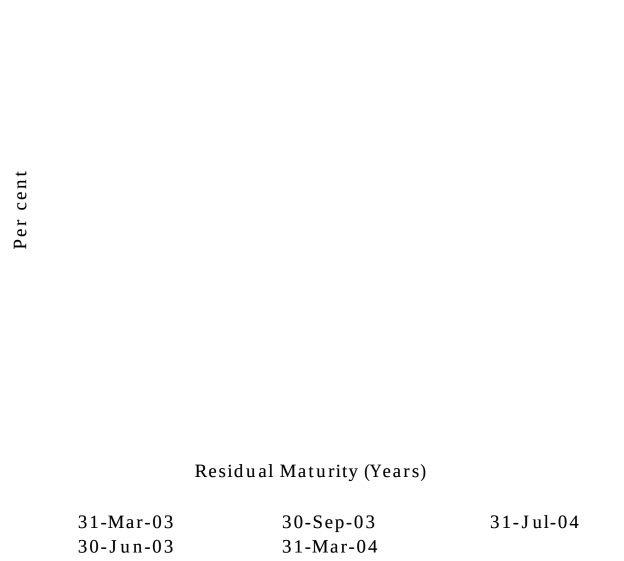
5.26 The forward market reflected the developments in the spot segment of the foreign exchange market during 2004-05 (up to August 13). The forward premia turned into discounts at the commencement of the year and the three-month forward premia dipped to 2.30 per cent by May 13, 2004, reflecting substantial forward sales by exporters. The forward rates, however, turned into premia thereafter as the exchange rate depreciated against the US dollar, import demand picked up and international oil prices steadily edged up. The three-month forward premia touched 2.98 per cent on August 13, 2004.

GOVERNMENT SECURITIES MARKET

5.27 Activity in the Government securities market was characterised by a sustained softening of yields during 2003-04. The benchmark 10-year yield declined by 106 basis points as compared with 115 basis points in 2002-03. The decline in yields was more pronounced for Government securities with maturity up to 14 years. During 2003-04, the aggregate volume of transactions in the Central and the State Government dated securities and Treasury Bills (outright as well as repos) increased by 36.0 per cent to Rs.26,39,897 crore, of which outright transactions constituted 63.8 per cent (Appendix Table V.6).

5.28 The yield curve flattened during the first half of 2003-04. Easy liquidity and benign inflationary expectations fuelled persistent rallies in prices of Government securities which was halted in August 2003 when the notified amount of 91-day Treasury Bills was raised to Rs.1,500 crore from Rs.500 crore and open market sales were conducted to absorb excess liquidity. The repo rate reduction on August 25, 2003 boosted market sentiment with the 10-year yield declining to 5.23 per cent on August 26 from 5.6 per cent on August 23, 2003. The yield spread between the securities of 10-year and 20-year tenors widened as shorter-term rates fell sharply in response to the repo rate cut (Box V.2). The announcement of a truncated calendar of issuance of the Government securities for the second half of 2003-04 (Rs.25,000 crore as against an expectation of Rs.60,000 crore) and expectations of a further repo rate cut in the wake of reduction in NRE deposit rates lifted market sentiment, bringing down short-term yields during the second quarter (Chart V.9).

Chart V.9 : Yield Curves for Central Government Dated Securities



5.29 In the second half of 2003-04, inflationary expectations hardened the yields at the long end of the maturity spectrum. The lowering of the cut-off yields in the auction of 364-day Treasury Bills drove down the 10-year yield of the Government securities to a low of 4.95 per cent on October 16, 2003. OMO sales and a series of 28-day repos under the LAF in the second fortnight of October checked possible rallies. Spreads widened and the yield curve

Box V.2
Dynamics of Yield Curve

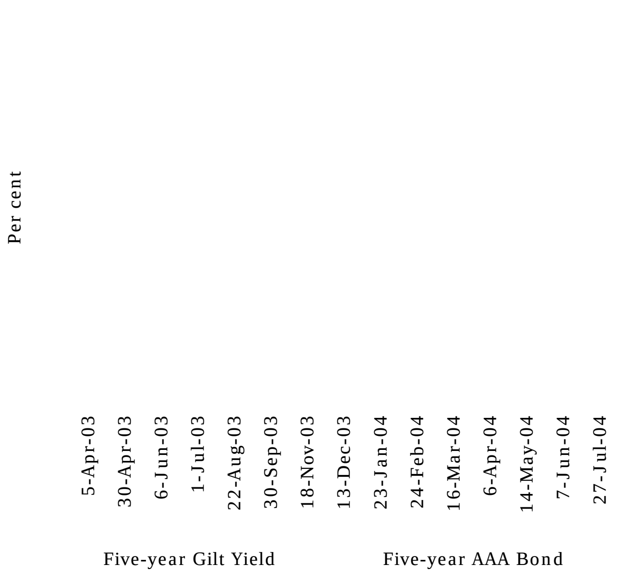
A yield curve, which is a graphical presentation of yields on securities of various maturities of a debt instrument with the 'same' default risk at a point of time, provides a snapshot of the term structure of interest rates in the market. Typically, yield curves slope upwards with interest rates rising as the tenor of the security increases. The yield curve shifts with a change in generalised perception about interest rates. The slope of the yield curve tends to be influenced by monetary policy action. Typically, when monetary policy is eased and short-term policy rates are reduced, the yield curve tends to get steeper. The curvature of the yield curve may change temporarily on account of specific demand-supply factors pertaining to particular tenors of a security.

An orderly evolution of the Government securities market in India has enabled a maturing of the yield curve into a smooth locus across one to 30-year tenors; however, a progressive flattening of the curve in recent years has engaged the attention of market participants, researchers and the policy makers alike. The narrowing of yield spreads in the 2-year to 10-year residual maturity segment (from 183 basis points to 63 basis points) and in the 10-year to 20-year segment (from 95 basis points to 77 basis points) during the period September 2001 to May 2004 made the yield curve in India one of the flattest internationally. The presence of a massive liquidity overhang accentuated the flattening of the yield curve, encouraging market participants to demand longer tenor securities so as to increase the duration of their portfolio and scale up potential capital gains amidst softening of interest rates. The Government's tendency to minimise the rollover risk by elongation of the maturity profile of the Government securities in falling interest rate conditions was in consonance with institutional participants' increasing demand for longer tenors. Some steepening of the yield curve was, however, witnessed at the time of easing of monetary measures such as the cut in the repo rate. The yield curve, however flattened as the long term yields fell in the wake of surplus liquidity conditions.

steepened by December 2003. Uncertainty about policy responses for managing capital flows and the edging up of inflation rates during January-February 2004 prompted a switch in portfolios. This, in turn, led to a decline in turnover and an upward shift of the yield curve. Turnover recovered in March 2004 as fuller information on the MSS became available to market participants.

5.30 During 2004-05 (up to August 16), yields at the longer end started edging up from May 2004, reflecting market uncertainty, expectation of raising of interest rate by the US, rising international crude oil prices and increase in the inflation rate. The yield curve steepened by end-June 2004 as market participants factored in the 25 basis points hike in the Federal Reserve's target rate. Turnover increased sharply in April, reflecting the MSS operations and auctions of dated Government securities by the Reserve Bank but declined subsequently. With the inching up of inflation and market apprehensions about possible measures to control inflation, the yield on the benchmark 10-year paper touched a peak of 6.73 per cent on August 11, 2004. However, the announcement of the reintroduction of one-day repo, effective August 16, 2004 calmed market sentiment, bringing down the yield of the 10-year security to 6.57 per cent. The yield spread between the Government securities and AAA-rated corporate bonds widened during 2003-04, reflecting market uncertainty about modification of norms relating to non-SLR investments (Chart V.10). The yield spread, which had narrowed in April 2004, widened further to about 91 basis points by July 2004.

Chart V.10: Yield Spreads (annualised)



CREDIT MARKET

5.31 Bank deposit rates were driven down across maturities during 2003-04 by easy liquidity conditions. Bank lending rates also declined but on a relatively muted scale, reflecting their inherent rigidity due to high cost of deposits contracted in the past and the overhang of non-performing assets (NPAs), along with some other structural factors. A sizeable portion of bank loans was extended at rates below the prime lending rates (PLRs). Sub-PLR lending (excluding exports, the bulk of which is at sub-PLR) constituted about half of the total outstanding advances above Rs.2 lakh by the banking system. Spreads around PLRs of public sector banks (PSBs) narrowed marginally by the last quarter of 2003-04. The benchmark prime lending rates (BPLRs), implemented through the operational guidelines issued by the Indian Banks' Association (IBA) in November 2003, is expected to improve transparency and to reduce complexity in pricing of loans. As on April 2004, almost all banks have adopted the new system of benchmark PLRs, which were significantly lower than earlier PLRs on cash credit or overdraft. During the period March 2003 and March 2004, the range of BPLR moderated by 25-200 basis points from the existing PLRs. Banks overwhelmingly adopted BPLRs by abandoning the system of tenor-linked PLR. The BPLRs of public sector banks moved in the range of 10.25-11.50 per cent in June 2004 (Table 5.5).

Non-Banking Financial Companies

5.32 Public deposits, as reported by 875 non-banking financial companies (NBFCs) [including residuary non-banking companies (RNBCs)] stood at Rs.20,100 crore as on March 31, 2003. Of the total public deposits, 23.3 per cent were contracted at interest rates of up to 10 per cent, followed by 41.7 per cent at interest rates between 10 per cent to 12 per cent and the remaining 35.0 per cent at interest rates between 12 per cent to 14 per cent. According to the quarterly information relating to large NBFCs (including RNBCs) with a public deposit base of Rs.20 crore and above, the aggregate public deposits of 24 reporting companies amounted to Rs.17,750 crore as at the end of March 2004, as against Rs.17,915 crore for 30 reporting companies as at end-March 2003. The information in respect of NBFCs/RNBCs having public deposits of Rs.500 crore and above shows that their number declined from four as at end-March 2002 to three as at end-March 2003. Although the number of companies

Table 5.5: Movements in Deposit and Lending Rates

(Per cent)

	June 2004	March 2004	December 2003	September 2003	June 2003	March 2003
1	2	3	4	5	6	7
1. Domestic Deposit Rate						
Public Sector Banks						
a. Up to 1 year	3.50-5.25	3.75-5.25	3.75-5.25	3.75-5.50	4.00-5.75	4.00-6.00
b. More than 1 year and up to 3 years	5.00-5.75	5.00-5.75	5.00-5.75	4.75-6.00	5.00-6.25	5.25-6.75
c. More than 3 years	5.25-5.75	5.25-6.00	5.25-6.00	5.25-6.25	5.25-6.50	5.50-7.00
Private Sector Banks						
a. Up to 1 year	3.00-6.00	3.00-6.00	3.00-6.25	3.00-7.00	3.00-7.00	3.50-7.50
b. More than 1 year and up to 3 years	5.00-6.50	5.00-6.50	5.00-7.00	5.50-7.50	5.50-7.75	6.00-8.00
c. More than 3 years	5.25-7.00	5.25-7.00	5.50-7.00	5.75-8.00	6.00-8.00	6.00-8.00
Foreign Banks						
a. Up to 1 year	2.75-7.50	2.75-7.75	2.75-7.75	3.00-7.75	3.00-7.75	3.00-7.75
b. More than 1 year and up to 3 years	3.25-8.00	3.25-8.00	3.35-8.00	3.50-8.00	3.50-8.00	4.15-8.00
c. More than 3 years	3.25-8.00	3.25.800	3.50-8.00	3.75-8.00	4.50-8.00	5.00-9.00
2. Prime Lending Rate#						
Public Sector Banks	10.25-11.50	10.25-11.50	9.00-12.25	9.00-12.25	9.00-12.25	9.00-12.25
Private Sector Banks	9.75-13.00	10.50-13.00	7.50-15.50	8.00-15.50	7.00-15.50	7.00-15.50
Foreign Banks	11.00-14.85	11.00-14.85	4.55-17.50	4.80-17.50	5.45-17.50	6.75-17.50
3. Actual Lending Rate*						
Public Sector Banks	n.a.	4.00-16.00	5.75-16.00	5.75-16.00	5.00-16.00	6.00-16.25
Private Sector Banks	n.a.	4.50-22.00	3.00-23.00	3.00-23.00	4.95-23.00	5.18-23.00
Foreign Banks	n.a.	3.75-23.00	3.00-22.00	5.00-22.00	5.00-23.00	5.40-20.00

\# : Prime Lending Rate for March and June 2004 are benchmark PLRs.
* : Interest rate on non-export demand and term loans above Rs.2 lakh excluding lending rates at the extreme 5 per cent on both sides.
n.a. : Not available.

remained the same in 2003-04, public deposits held by them declined by Rs.464 crore on account of repayment during the year (Table 5.6).

Table 5.6: NBFCs/RNBCs with Public Deposits Base of Rs.500 crore and above

As on March 31	No.of NBFCs/RNBCs	Public Deposits (Outstanding - Rs. crore)	Growth (Per cent)
1	2	3	4
2002	4	14,237	–
2003	3	15,707	10.32
2004	3	15,243	-2.95

EQUITY AND DEBT MARKETS

5.33 The capital market experienced generally buoyant conditions during 2003-04. Resource mobilisation from the public issues market increased, though this could not compensate for the decline in activity in the private placement market. Resource mobilisation by mutual funds witnessed a substantial increase. Assistance sanctioned and disbursed by financial institutions rose sharply after a gap of two years. The secondary market witnessed a strong rally led by a large institutional support, particularly from the FIIs due to attractive valuations *vis-á-vis* other emerging market economies. The stock market turned somewhat volatile during 2004-05 with turbulent conditions on May 17, 2004.

Primary Market

5.34 A long period of lacklustre activity and waning investor interest was dispelled in 2003-04 by signs of revival in the public issues segment (Table 5.7 and Chart V.11).

5.35 The bulk of resource mobilisation (71.4 per cent) from the public issues market in 2003-04 was

Chart V.11 : Resource Mobilisation in the Primary Market

Rupees crore

Public Issues (Private Sector)
Public Issues (Public Sector)
Private Placement (Private Sector)
Private Placement (Public Sector)

Table 5.7: Mobilisation of Resources from the Primary Market*

(Rupees crore)

Item	2003–04P		2002–03	
	No. of Issues	Amount	No. of Issues	Amount
1	2	3	4	5
A. Prospectus and Rights Issues				
1. Private Sector (a+b)	**27**	**3,210** (70.9)	**9**	**1,878** (-67.0)
a) Financial	3	1,251	4	1,236
b) Non–financial	24	1,959	5	642
2. Public Sector (a+b+c)	**8**	**3,980** (33.2)	**8**	**2,989** (110.5)
a) Public Sector Undertakings	–	–	–	–
b) Government Companies	1	100	–	–
c) Banks/Financial Institutions	7	3,880	8	2,989
3. Sub Total (1+2)	**35**	**7,190** (47.7)	**17**	**4,867** (-31.6)
B. Private Placement +				
1. Private Sector (a+b)	**578**	**14,866** (-40.7)	**877**	**25,077** (-12.4)
a) Financial	291	9,178	327	9,454
b) Non–financial	287	5,688	550	15,623
2. Public Sector (a+b)	**222**	**44,349** (5.9)	**267**	**41,871** (15.5)
a) Financial	123	25,879	157	20,407
b) Non–financial	99	18,470	110	21,464
3. Sub Total (1+2)	**800**	**59,215** (-11.5)	**1,144**	**66,948** (3.2)
C. Total (A+B)	**835**	**66,405** (-7.5)	**1,161**	**71,815** (-0.2)
Memo Item:				
Euro Issues	**18**	**3,098** (-9.6)	**11**	**3,426** (43.6)

* : Including both debt and equity. P : Provisional. – : Nil/Negligible.

+ : Estimates based on information gathered from arrangers, financial institutions and newspaper reports.

Note : Parenthetic figures represent percentage variations over the previous year.

by banks and financial institutions. Four public sector banks floated equity issues aggregating Rs.950 crore during 2003-04. In addition, there were six bond issues aggregating Rs.4,181 crore by the IDBI (Rs.2,930 crore from three issues) and the ICICI Bank (Rs.1,251 crore from three issues). The share of equity issues in total resource mobilisation increased sharply in 2003-04 in comparison with the previous year (Appendix Table V.9 and Chart V.12).

5.36 Initial public offerings (IPOs) picked up in 2003-04, accounting for about 26 per cent (Rs.1,854 crore) of total resources mobilised by way of prospectus and rights issues. The post-listing performance of recently issued IPOs is encouraging (Box V.3). A variant of a stabilisation scheme was introduced by the SEBI in August 2003 drawing from the experiences of the US, the UK and Canada.

5.37 Resource mobilisation from the private placement market declined during 2003-04. This decline needs to be placed in the context of stringent disclosure norms prescribed by the SEBI on September 30, 2003 for this segment, which had remained almost unregulated until then. Public sector entities (mainly financial intermediaries) continued to dominate the private placement market in 2003-04, accounting for

Chart V.12: Public Issues Market – Instrument Type

Box V.3

Post-listing Performance of IPOs

Initial public offering (IPO) refers to the first sale of stock by a private company to the public. Although both initial and subsequent public offerings result in expanding the equity base of a company, these issues are distinct in many ways. Investors participating in the equity offerings by listed companies take informed decisions based on details about the company that are already available in the market place. In the case of an IPO, however, the availability of information regarding the past performance of the company and its track record is generally inadequate and, therefore, lacks credibility. This information asymmetry may lead to the problems of moral hazard and adverse selection.

A large number of IPOs were floated in the Indian market in the mid-1990s following the introduction of free pricing. This boom in IPOs, however, faded mainly due to lower than expected performance of the issues. Prices of many issues, floated at high premia, declined significantly after listing. Investors also suffered heavy losses as several companies which made IPOs vanished. Investor confidence suffered a further setback in the late 1990s due to a sharp decline in the prices of technology stocks *albeit* in tandem with the world-wide 'tech' stock meltdown.

Preliminary empirical evidence regarding the variation of IPO share prices for the period 2001-02 to 2003-04 indicates that share prices of about 75 per cent of IPOs improved upon listing. The variation was measured as the percentage change between the offer price and the market price of the scrips after six months. Stringent entry and disclosure norms introduced by the SEBI have had a significant impact on the quality of issues entering the market as well as their post-listing performance.

References

1. Jain, B.A. and O. Kini (1994), "The Post Issue Operating Performance of IPO Firms", *Journal of Finance,* 49.
2. Loughran, Tim, and Jay R. Ritter (1995), "The New Issues Puzzle", *Journal of Finance,* 50(1), March.
3. Ritter Jay R. (1991), "The Long-Run Performance of Initial Public Offerings", *Journal of Finance*, 46.

75.0 per cent of the total resource mobilisation. Resource mobilisation by financial intermediaries (both public and private sector) increased by 17.4 per cent to Rs.35,057 crore, while that by non-financial companies declined sharply by 34.9 per cent to Rs.24,158 crore.

5.38 Resources raised by Indian corporates from the international capital market by way of Foreign Currency Convertible Bonds (FCCBs), Global Depository Receipts (GDRs) and American Depository Receipts (ADRs) declined marginally during 2003-04 (see Table 5.7). With a view to integrating the Indian capital market with the international capital markets and to enable Indian investors to diversify risk, foreign companies were allowed to access the Indian capital market by way of Indian Depository Receipts (IDR) (Box V.4).

Box V.4

Indian Depository Receipts

In terms of the Companies (Issue of Indian Depository Receipts-IDRs) Rules, 2004 notified by the Government on February 23, 2004 a company incorporated outside India can issue IDRs subject to the following: (i) the pre-issue paid-up capital and free reserves of the issuing company should be at least US $ 100 million with an average turnover of US $ 500 million during the preceding three financial years; (ii) the company has been making profits for at least five years preceding the issue and has been declaring dividend of not less than 10 per cent each year in this period; and (iii) the pre-issue debt-equity ratio is not more than 2:1. The issuing company may or may not have established any place of business in India. The issuing company would also have to fulfill the eligibility criteria stipulated by the SEBI and obtain necessary approvals from local authorities.

According to the IDR Rules, the issuing company shall appoint an overseas custodian bank, a domestic depository and a merchant banker for the purpose of issue of IDRs. The underlying shares will be delivered to an overseas custodian bank which will authorise the domestic depository to issue IDRs. IDRs will not be redeemable into the underlying equity shares for a period of one year from the date of issue. IDRs issued by any company in any financial year shall not exceed 15 per cent of its paid-up capital and free reserves. The IDRs will have to be denominated in Indian rupees, irrespective of the denomination of the underlying securities.

IDRs will be listed on one or more recognised stock exchanges having nation wide trading terminals in India and may be purchased, possessed and freely transferred by persons resident in India as defined under the Foreign Exchange Management Act, 1999 (FEMA). IDRs can be transferred and redeemed, subject to the provisions of the FEMA.

Mutual Funds

5.39 Resource mobilisation by mutual funds (net of redemptions) increased sharply to Rs.47,684 crore during 2003-04 from Rs.4,583 crore during 2002-03 due mainly to a sharp rise in resources mobilised by private sector mutual funds to Rs.42,873 crore from Rs.12,122 crore. The Unit Trust of India (UTI) also experienced net inflow of funds (Table 5.8).

Table 5.8: Net Resource Mobilisation by Mutual Funds

(Amount in Rupees crore)

Item	2003-04		2002-03	
	No. of Schemes	Amount	No. of Schemes	Amount
1	2	3	4	5
1. Unit Trust of India	41	1,050 *	59	-9,434
2. Public Sector Mutual Funds	64	3,761	70	1,895
3. Private Sector Mutual Funds	362	42,873	324	12,122
Total (1 to 3)	**467**	**47,684**	**453**	**4,583**

* : Data for 2003-04 relate to UTI Mutual Fund for the period February 01, 2003 to March 31, 2004 (also refer to footnote of Table 5.10)

Notes : 1. Data are provisional and compiled on the basis of information received from respective mutual funds.
2. For UTI, the data relate to net sales (with premium), including reinvestment sales. For other mutual funds, figures represent net sales under all schemes.
3. Data exclude amounts mobilised by off-shore funds and through rollover schemes.

Table 5.9: Scheme-wise Resource Mobilisation by Mutual Funds

(Rupees crore)

Year	Equity-Oriented	Debt-Oriented	Balanced	Total
1	2	3	4	5
2002-03	43	5,781	-1,628	4,196
2003-04	7,219	39,603	-13	46,809

Source: Securities and Exchange Board of India (SEBI).

5.40 The bulk of the resources mobilised by mutual funds have traditionally been in the form of debt-oriented schemes. This trend continued in 2003-04 (Table 5.9).

5.41 Debt-oriented schemes accounted for about 45 per cent of the total assets under management of mutual funds at end-March 2004 (Table 5.10).

All-India Financial Institutions

5.42 Select All-India Financial Institutions (AIFIs) have been permitted by the Reserve Bank to raise resources by way of term money borrowings, issue of CDs, CPs, acceptance of term deposits and inter-corporate deposits (ICDs) within the umbrella limit linked to their net owned funds. The outstanding aggregate amount of resources raised by financial institutions (IDBI, IFCI, EXIM Bank, SIDBI, IIBI, TFCI, NABARD, IDFC and NHB) by way of short-term money market instruments increased during 2003-04 (Table 5.11). It, however, declined marginally to Rs.6,207 crore by June 2004. Generally, CP was

Table 5.10: Assets under Management of Mutual Funds

(Amount in Rupees crore)

Instrument	End-March 2004	End-March 2003	End-March 2002	End-March 2001	End-March 2000
1	2	3	4	5	6
1. Debt	62,524	47,564	55,788	48,863	48,004
	(44.8)	(59.9)	(55.5)	(53.9)	(42.5)
2. Equity	23,613	9,887	13,852	13,483	30,611
	(16.9)	(12.4)	(13.8)	(14.9)	(27.1)
3. Money Market Instruments	41,704	13,734	8,069	4,128	2,227
	(29.9)	(17.3)	(8.0)	(4.6)	(2.0)
4. Government Securities	6,026	3,910	4,163	2,317	2,370
	(4.3)	(4.9)	(4.1)	(2.6)	(2.1)
5. Others	5,749	4,369	18,722	21,796	29,793
	(4.1)	(5.5)	(18.6)	(24.1)	(26.4)
6. Total	**1,39,616**	**79,464 ***	**1,00,594**	**90,587**	**1,13,005**
	(100.0)	**(100.0)**	**(100.0)**	**(100.0)**	**(100.0)**
		1,09,299 @			

* : Following the bifurcation of the UTI (into the UTI Mutual Fund and the Specified Undertaking of the Unit Trust of India), effective February 2003 data in respect of the Specified Undertaking of the Unit Trust of India have been excluded from the total assets under management of mutual funds from the year ended March 2003 onwards.

@ : Including the assets of Specified Undertaking of the Unit Trust of India.

Notes : 1. Others include balanced and equity linked saving schemes.
2. Figures in parentheses represent proportion to the total assets under management.

Source : Association of Mutual Funds in India (AMFI).

Table 5.11: Outstanding Amount Mobilised under Umbrella Limits by Select All-India Financial Institutions

(Rupees crore)

Instrument	March 2004	March 2003
1	2	3
Commercial Paper (CP)	2,740	1,425
Term Deposits	2,111	2,067
Inter-corporate Deposits	866	1,761
Certificates of Deposit (CD)	467	460
Term Money	300	245
Total	**6,483 (23,650)**	**5,958 (23,824)**

Note: Figures in parentheses denote 'Umbrella Limits.'

the preferred instrument followed by term deposits, term money and ICDs. Interest rates on all these instruments softened during the year, especially towards the end of the year.

5.43 Total resources mobilised by AIFIs by way of issue of rupee bonds/ debentures (including private placement and public issues - excluding erstwhile ICICI) rose sharply during 2003-04 as they took advantage of low interest rates. Some FIs such as IFCI and IIBI were not permitted to raise fresh borrowings from the market due to their deteriorating financial position. These FIs rolled over some of their existing bond liabilities. The weighted average maturity of the instruments issued by FIs was elongated, while the weighted average interest rate of resources raised across FIs eased during the year (Table 5.12).

5.44 Financial assistance sanctioned and disbursed by AIFIs increased sharply by 65.8 per cent and 24.5 per cent, respectively, during 2003-04. The increase in sanctions and disbursements by AIFIs points to an improvement in the investment climate (Appendix Table V.10).

Secondary Market

5.45 The stock market turned buoyant in 2003-04, ending a long subdued spell of over three years which began shortly after the BSE Sensex crossed the historical 6000-mark in intra-day trading in February 2000. The rally in equity prices, which began from end-May 2003, continued almost uninterrupted till January 2004 (Appendix Table V.11 and Chart V.13). It was sustained by large investments by FIIs against the background of improving fundamentals, strong corporate results and initiatives on the disinvestment front. The BSE Sensex crossed the 6000-mark again in January 2004. The uptrend was interspersed by several corrections from February 2004 in an environment of high uncertainty. Despite some downtrend in February 2004 and March 2004 due to political uncertainty, the BSE Sensex ended the year with net significant gains of over 83 per cent over the previous year.

5.46 The rally witnessed in 2003-04 was broad based and covered almost all the sectors, unlike the rally in 2000 which was largely confined to the technology sector. The broad based BSE 500 index (which includes several medium and small sized companies) increased by 109 per cent

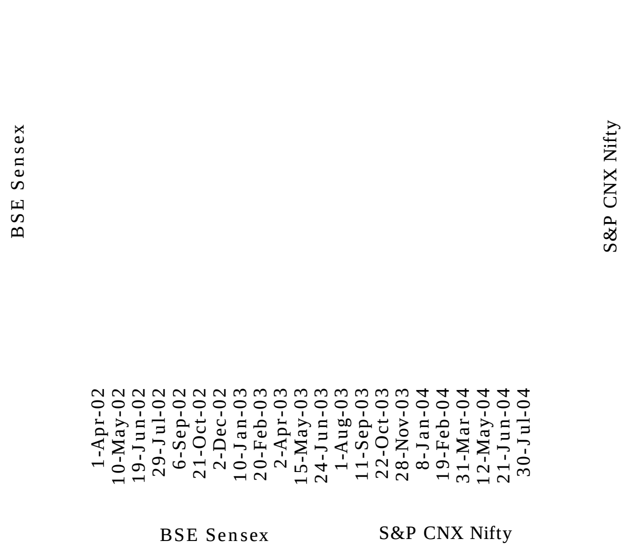
Table 5.12: Resources Raised by way of Bonds/Debentures* by Select All-India FIs

(Amount in Rupees crore)

Institution	Resources Raised		Total Borrowings Outstanding at end of		Weighted Average Cost of Funds (%)		Weighted Average Maturity (years)	
	2003-04	2002-03	March 2004	March 2003	2003-04	2002-03	2003-04	2002-03
1	2	3	4	5	6	7	8	9
IDBI	10,477	5,009	46,967	41,798	6.5	8.5	5.1	4.3
IFCI	–	267	17,564	20,203	8.2	9.6	3.2	2.2
IIBI	176	144	1,260	1,468	8.7	9.6	18.0	8.6
Exim Bank	2,025	2,505	11,920	5,424	5.9	8.9	6.7	6.1
NABARD	5,334	2,988	11,959	8,703	5.4	6.1	5.4	4.7
NHB	2,526	1,876	6,958	4,675	5.4	6.4	3.2	4.0
SIDBI	1,429	961	3,256	2,519	5.0	6.6	1.9	2.3
TFCI	102	93	546	632	8.6	10.1	10.0	8.5
IDFC	1,550	400	2,450	2,175	5.6	7.6	5.9	5.6
Total	**23,618**	**14,243**	**1,02,880**	**87,596**				

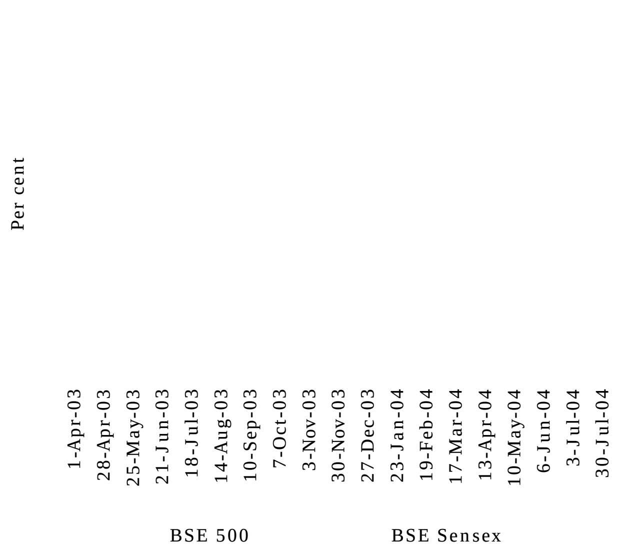
* : Relate to rupee resources only.
Note : Data are provisional.
Source : Various Financial Institutions (FIs).

Chart V.13 : Movements in Major Indian Stock Market Indices



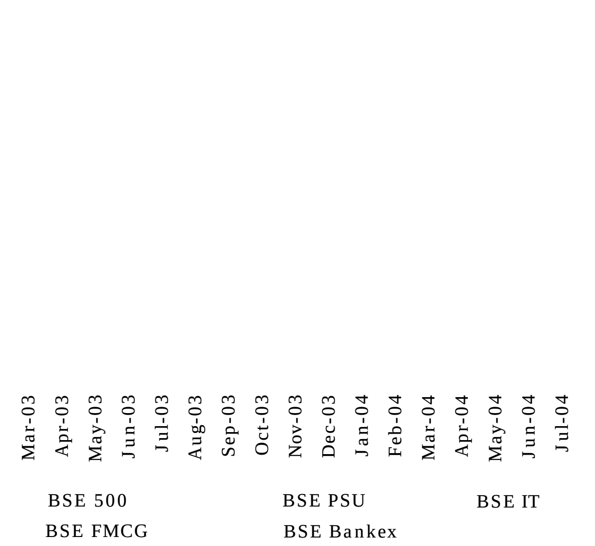
during the year as compared with the rise of 83 per cent in the BSE Sensex (which comprises 30 scrips) (Chart V.14).

Chart V.14 : Changes in BSE 500 Index and BSE Sensex (Year-on-year)



5.47 The rally encompassed almost all the sectors, *i.e.*, banking, PSU, fast moving consumer goods (FMCG) and IT (Chart V.15). The Indian stock market outperformed many other emerging market economies in Asia. In contrast to the Asian region, stock markets in many developed markets registered only modest gains (Table 5.13 and Chart V.16).

Chart V.15 : BSE 500 and Sectoral Indices*



* Normalised to March 2003 = 100

5.48 Movements in stock prices in India were accompanied by a rise in turnover. Market capitalisation of the BSE increased by 110 per cent during 2003-04 (Table 5.14). Despite sharp increase in share prices, the price-earning (P/E) ratio moved up only modestly, reflecting increased profitability of the corporate sector. Volatility in the stock markets, as measured by the coefficient of variation, however, increased during the year (Appendix Table V.12).

Table 5.13: Emerging Market Stock Indices

Country	Index	End-March 2004	End-March 2003	Percentage Variation
1	2	3	4	5
Indonesia	Jakarta Composite Index	735.68	398.0	84.8
India	BSE Sensex	5590.60	3048.72	83.4
Thailand	SET Composite Index	647.30	364.55	77.6
Taiwan	Taiwan Index	6522.19	4321.22	50.9
Malaysia	KLSE Composite Index	901.85	635.72	41.9
Philippines	PSE Composite Index	1424.33	1039.67	37.0

Source: Moneyline Telerate Information Services.

Chart V.16 : Movements in International Stock Indices

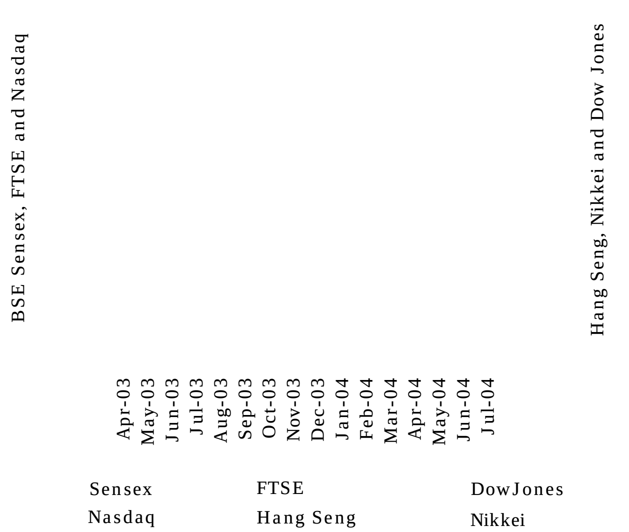
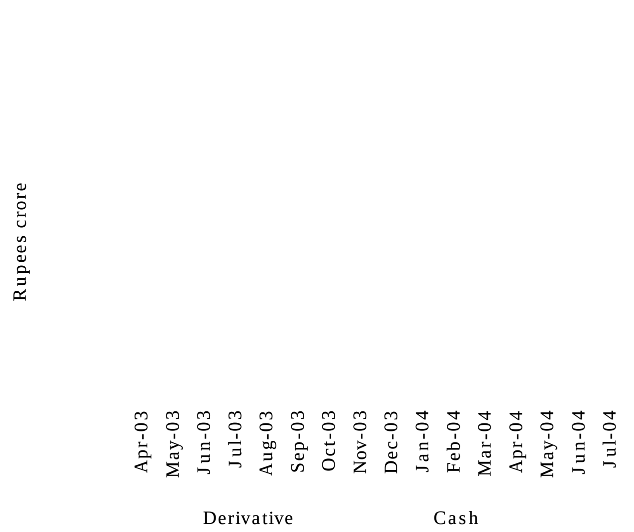


Chart V.17 : Turnover in Cash and Derivative Segments – NSE



5.49 A significant development during 2003-04 was an increased activity in the derivatives segment. With a five-fold increase in the turnover, the derivatives segment overtook the cash segment in NSE during the year (Appendix Table V.13 and Chart V.17).

Table 5.14: Indian Equity Markets

Indicator	BSE		NSE	
	2003-04	2002-03	2003-04	2002-03
1	2	3	4	5
1. BSE Sensex/ S&P CNX Nifty				
(i)Average	4492	3206	1428	1037
(ii)End-year	5591	3049	1772	978
2. Coefficient of Variation (per cent)	23.0	4.8	23.3	5.2
3. Price -Earning Ratio@	16.2	14.5	16.1	15.2
4. Price-Book Value Ratio@	2.9	2.2	3.1	2.6
5. Yield @ (per cent per annum)	2.0	2.2	2.1	2.1
6. Listed Companies #	5,528	5,650	909	673
7. Turnover (Rupees crore)	5,02,620	3,14,073	10,99,535	6,17,989
8. Market Capitalisation (Rupees crore) #	12,01,207	5,72,198	11,20,976	5,37,133

@ : Based on scrips included in the BSE Sensex and in the S&P CNX Nifty, respectively and are averages for the year.

\# : As at end-March.

Source : The Stock Exchange, Mumbai (BSE) and the National Stock Exchange of India Limited (NSE).

5.50 Net equity investments by FIIs increased by as much as 1480.7 per cent during 2003-04. FII investment in debt instruments also increased sharply. The bulk of the funds by mutual funds during 2003-04 were deployed in debt instruments in keeping with the objective of most of their schemes. Unlike 2002-03, however, mutual funds made net purchases in equities in 2003-04 (Table 5.15). FIIs continued to be strong buyers in equities. Their investments in equities in April 2004 were the highest ever in any single month. They, however, turned net sellers in equities in May 2004 for the first time in 18 months in line with their operations in several other emerging market economies. FIIs again turned net buyers in equity between June 2004 and August 2004.

5.51 The SEBI allowed brokers to extend margin trading facility to their clients in April 2004 with a view to improving liquidity in the secondary market and to facilitate the process of price discovery (Box V.5).

Table 5.15: Trends in Institutional Investments

(Rupees crore)

Year	FIIs		Mutual Funds	
	Net Investment in Equity	Net Investment in Debt	Net Investment in Equity	Net Investment in Debt
1	2	3	4	5
2001-02	8,067	685	-3,796	10,959
2002-03	2,528	162	-2,067	12,604
2003-04	39,959	5,805	1,308	22,701

Source: Securities and Exchange Board of India (SEBI).

Box V.5

Margin Trading

Margin trading is an arrangement whereby an investor purchases securities by borrowing a portion of the purchase value from the authorised brokers by using securities in his portfolio as collateral.

The Securities Exchange Board of India (SEBI) has allowed member brokers to provide margin trading facility to their clients in the cash segment since April 1, 2004. Securities with mean impact cost of less than or equal to one and traded at least 80 per cent (+/-5 per cent) of the days during the previous 18 months would be eligible for margin trading facility. Only corporate brokers with "net worth" of at least Rs.3 crore would be eligible to participate. Brokers wishing to extend the facility of margin trading to their clients are required to obtain prior permission from the exchange(s) where the facility is proposed to be provided. The broker may use his own funds or borrow from scheduled commercial banks and/or NBFCs regulated by the Reserve Bank. At any point of time, total indebtedness of a broker for the purpose of margin trading is not allowed to exceed 5 times of his net worth as defined by the SEBI. The "total exposure" of a broker towards the margin trading facility shall be within the self-imposed prudential limit and shall not, in any case, exceed the borrowed funds and 50 per cent of "net worth". The exposure to any single client at any point of time is restricted to 10 per cent of the "total exposure" of the broker.

The margin arrangement has to be agreed upon between the authorised broker and the client subject to the SEBI guidelines prescribed on March 19, 2004. Initial and maintenance margin for the client shall be a minimum of 50 per cent and 40 per cent, respectively, which has to be paid in cash. Initial margin is the minimum amount, calculated as a percentage of the transaction value, to be placed by the client with the broker before the actual purchase. The maintenance margin is the minimum amount, calculated as a percentage of the market value of securities with respect to the last trading day's closing price to be maintained by the client with the broker. When the balance deposit in the client's margin trading accounts falls below the required maintenance margin, the broker shall promptly make the margin call. According to the current arrangement, the broker may liquidate the securities if: (i) the client fails to meet the margin call made by the broker; (ii) fails to deposit the cheques after the marginal call has been made; (iii) where the cheque deposited by the client has been dishonored; and (iv) if the client's deposit in the margin account (after adjustment for mark to market losses) falls to 30 per cent or less of the latest market value of the securities. The broker shall maintain separate client-wise accounts of the securities purchased on the basis of margin trading with depositories. The SEBI and stock exchange(s) have the right to inspect the books of accounts maintained by brokers with respect to the margin trading facility.

Earlier in September 2001, the Reserve Bank had allowed scheduled commercial banks to extend finance to brokers for the purpose of margin trading, subject to certain terms and conditions.

5.52 The stock market remained somewhat volatile during April-June 2004. The downtrend witnessed in February 2004 continued during March and April 2004. On May 17, 2004 the stock market in India witnessed turbulent conditions. The market opened the day on an extremely weak note and plunged by 16.6 per cent during intra-day trading before recovering partly. The market ended the day with a net loss of 11.1 per cent as compared with the previous day's close. The trading was halted twice during the day due to the application of the index-based circuit filters.

5.53 The turbulence in the market on May 17, 2004 was caused mainly by uncertainty relating to the formation of the new Government after the general elections. External factors such as rising oil prices and apprehensions of rise in international interest rates also contributed to the sudden reversal of market sentiment. The sharp decline in the Indian stock market on May 17, 2004 was, however, a temporary phenomenon and not due to change in fundamentals which continued to be strong. On May 17, 2004 a sharp decline was also observed in several other emerging markets in Asia such as South Korea (-5.14 per cent), Taiwan (-5.10 per cent) and Thailand (-4.61 per cent).

5.54 Orderly conditions in the Indian stock market were quickly restored. Appropriate risk management systems were in place to tide over the period without any recourse to exceptional financing. Also, market participants were assured by the Reserve Bank of liquidity to meet payment obligations in stock exchanges (Box V.6).

5.55 The announcement in the Union Budget 2004-05 with regard to imposition of Securities Transaction Tax (STT) affected the market sentiment adversely. The Union Budget also proposed to reduce the short-term capital gains tax from 30 per cent to 10 per cent, abolish the long-term capital gains tax and increase the FDI limit for telecommunication, civil aviation and insurance sectors. Moreover, the ceiling for FII investment in debt funds was increased from

Box V.6

Role of the Reserve Bank in Stock Market Volatility

The Reserve Bank monitors developments in the money, the foreign exchange and the Government securities markets as the monetary authority and as debt manager to the Government. With the progressive integration of various segments of financial markets, the Reserve Bank keeps a close watch on activity in the equity market to guard against any possible spillover of disturbances to the money, the Government securities and the foreign exchange markets. Accordingly, when the stock market turned volatile on May 17, 2004 the Reserve Bank closely monitored major settlement banks and stock exchanges concerned to ensure that the payment obligations in the exchanges were met smoothly. The Reserve Bank publicly announced its readiness to provide sufficient liquidity to banks for meeting all their payment obligations and intra-day requirements so that the payment settlement was carried out smoothly. It announced measures to enable banks to provide liquidity to brokers and foreign exchange to foreign institutional investors (FIIs).

A Task Force was constituted under the Executive Director, Financial Market Committee for providing clarifications and liquidity assistance. On the recommendation made by the Task Force, it was decided to restore, with immediate effect, the *status quo ante* on margins that banks have to maintain for financing against shares/IPOs/issue of guarantees. The Financial Market Committee decided that as soon as there is a circuit breaker there should be a trigger within the Reserve Bank to monitor different market segments and ensure adequate liquidity.

US $ 1 billion to US $ 1.75 billion. Notwithstanding these initiatives in the Union Budget and encouraging corporate results, the market conditions remained sluggish up to mid-July 2004. The revision in the proposed STT on July 21, 2004 helped in improving the market sentiment. The stock market has been witnessing revival since end-July 2004.

Developments in Wholesale Debt Market Segment of NSE

5.56 In the Wholesale Debt Market (WDM) segment of the NSE, 2,621 securities were available for trading as on March 31, 2004 as compared with 1,990 securities as on March 31, 2003. The turnover in the WDM segment increased by 23.2 per cent to Rs.13,16,096 crore in 2003-04. Transactions in dated securities accounted for 92.6 per cent of the total traded value for the year 2003-04. Total market capitalisation of the securities available for trading in the WDM segment aggregated Rs.12,15,864 crore as on March 31, 2004.

Outlook

5.57 The financial markets are expected to remain stable and orderly, although they would evolve with the overall macroeconomic conditions. Developments in international financial markets as they prepare for the reversal in the interest rate cycle in major countries will have a strong bearing on the behaviour of domestic financial markets. Markets have experienced comfortable liquidity conditions during the first quarter of 2004-05, notwithstanding signs of a slow down in external inflows. With call rates generally remaining at sub-repo levels, the turnover in this segment is expected to decline as the participants increase their presence in the other money market segments. There has been a modest depreciation of the exchange rate against the US dollar in the first quarter but expectations relating to the near-term continue to be indicative of stable conditions in the foreign exchange market. The domestic price situation and global interest rate movements would have implications for yields in the Government securities market in 2004-05. The equity market, which remained subdued since February 2004, displayed signs of revival since end-July 2004. It is important to note, however, that with the return of inflation worldwide and the raising of policy rates by several central banks, reversal of the existing ample international liquidity conditions would impact domestic financial markets. As interest rates transit to a more neutral level, market participants could face the need for re-balancing of portfolios.

VI EXTERNAL SECTOR

6.1 The most significant feature of macroeconomic performance in 2003-04 was the developments in the external sector. Aided by a favourable external environment, India's balance of payments was characterised by robust exports of both merchandise and invisibles, a current account surplus of the order of 1.4 per cent of GDP, massive capital inflows brought in by sustained investor optimism about the resurgence of growth in India and an unprecedented accretion to the foreign exchange reserves which surpassed the level of external debt by the end of the year. This was also reflected in a marked improvement in India's international investment position. Under the circumstances, managing the surges in capital flows turned out to be an important objective of macroeconomic management during 2003-04. Strategic shifts in the policy stance were reflected in aggressive prepayment of external debt by official and private sectors to benefit from softer international interest rates, significant liberalisation of the exchange and payments system extended to freeing outward capital flows, fine tuning of interest rates on non-resident deposits to align them more closely with international interest rates and a tighter linkage between funds raised abroad and end-use domestically.

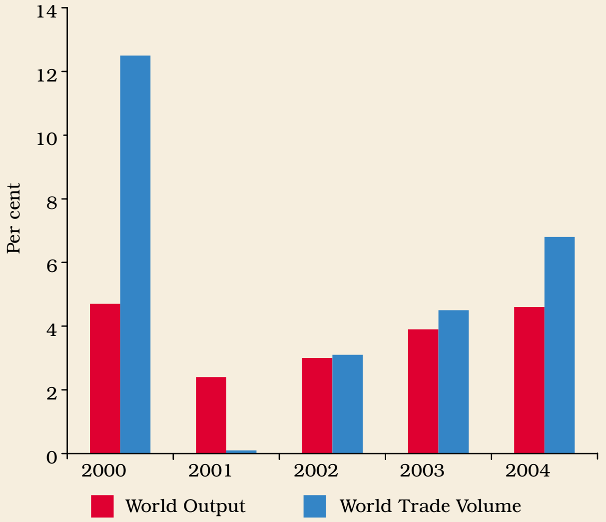
6.2 This Section reviews developments in India's external accounts in 2003-04. Beginning with a survey of international economic developments, the Section delineates the strong improvement in merchandise trade in terms of compositional and geographical shifts in exports and imports. The Section also highlights the crucial role played by invisibles in sustaining current account surpluses. The analysis underscores the growing significance of exports of software and IT enabled services and workers' remittances. A review of developments in the capital account reflects the return of non-debt creating flows to the top of the hierarchy of capital flows into India. The impact of these developments on the foreign exchange reserves and the international investment position are also set out in this Section.

INTERNATIONAL DEVELOPMENTS

6.3 World real GDP is estimated to have risen by 3.9 per cent in 2003 from 3.0 per cent in 2002 as the global recovery took root and extended its reach to all regions of the world, *albeit* with variations in the pace and spread (Appendix Table VI.1). The strength of the upturn was strongest in emerging Asia - led by China and India - and the US. Global growth surged to six per cent in the second half of 2003 on an annualised basis, regaining the momentum achieved before the onset of the synchronised downturn in 2000. More recent data indicate that the strong growth of 2003 has continued into early 2004. According to the IMF, the 'solid' improvement in global activity was associated with an acceleration in world trade, a sharp pick-up in industrial production and a resumption of business and consumer confidence. World trade shed the sluggishness characterising the first half of 2003 and expanded by 4.5 per cent during 2003, although it remained well below the average of 6.4 per cent recorded in the 1990s. Nominal trade flows were much more buoyant than real trade volumes with world exports in US dollar terms rising by 16.5 per cent due to weakening of the US dollar. China turned out to be the key driver of world trade, with imports rising by 41 per cent in US dollar terms. Accordingly, Asia recorded the strongest expansion in trade, followed by North America and Africa. Higher commodity prices, partly reflecting the depreciation of the US dollar, translated into gains in terms of trade for fuel and non-fuel exporters (Chart VI.1).

6.4 Exceptionally strong growth in the US in the second half of 2003 was led by private consumption buoyed up by the monetary-fiscal stimulus as well as an

Chart VI.1 : Growth in World Output and Trade



Note : Data for 2004 are IMF Projections.
Source : *World Economic Outlook*, IMF, April 2004

upturn in business investment on account of continuing productivity gains and improvement in corporate profitability on the back of balance sheet restructuring. Employment, however, remained weak by historical standards and, along with the massive trade and fiscal deficits, carried the most serious risks to recovery. Growth in the UK also remained strong and was supported by the cyclical upturn and expansionary fiscal policy. Housing price concerns prompted a counter-cyclical monetary policy response in the second half of 2003. In the Euro area, growth remained subdued due to weak domestic demand towards the close of 2003, although incipient recovery appears to have set in. In Japan, an exceptionally strong recovery was reflected in buoyant exports and a rebound in private investment. Deflationary pressures eased considerably with a modest improvement in the health of the financial system. Growth in emerging Asia shrugged off the SARS - related slowdown and bounded to seven per cent in 2003 led by strong domestic consumption and exports, despite appreciation of local currencies against the US dollar. A noteworthy development in 2003 was the emergence of China as a major export destination and the main driver of intra-regional trade. The economies in East Asia and the South-East Asia gained considerably from exports to China. Fears of overheating in China cast a shadow on macroeconomic performance in the region towards the close of 2003. Growth in the Latin America region strengthened with rising exports, supported modestly by domestic demand. In Africa, improvement in growth was mainly confined to oil exporting countries.

6.5 Despite large fiscal deficits, policy interest rates remained at historically low levels in most industrial countries - zero in Japan and Switzerland, one per cent in the US, two per cent in the Euro area, and at or near historic lows in the UK and Canada. Domestic bond markets rallied in most countries with some consolidation towards the end of the year tempering the heightened appetite for risk. Financial markets witnessed a broad based rally with rise in equity prices and decline in bond spreads, particularly emerging market bonds. Reflecting improved investment opportunities and receding systemic risks, capital flows to emerging market economies (EMEs) increased to US $ 131.2 billion in 2003 from US $ 47.0 billion in 2002 (Table 6.1).

6.6 Inflation remained generally subdued in 2003. Commodity prices surged in response to changing demand-supply balances, especially of intermediate commodities. Fuel prices soared, driven up by increased demand, production cuts by the OPEC and continuing geo-political uncertainties. Inflationary expectations in industrial countries remained low on account of continued excess capacity and weak labour markets. Owing to competitive pressures, corporates preferred to absorb rising input costs into their profits which also kept consumer prices low.

Table 6.1: Net Capital Flows to Emerging Markets and Developing Countries

(US $ billion)

Item	2003	2002	2001
1	2	3	4
Private capital flows	**131.2**	**47.0**	**20.6**
Private direct investment	119.3	139.3	189.1
Private portfolio investment	-87.5	-98.6	-95.7
Other private capital flows	99.3	6.3	-72.8
Official flows	**-7.2**	**3.3**	**25.8**

Source : *World Economic Outlook*, IMF, April 2004.

6.7 Although overall global growth prospects have improved markedly, some risks and uncertainties still remain. The major downside risks facing the global economy continue to emanate from global imbalances and the associated possibility of disruptive currency adjustments and lingering structural problems in the Euro area and Japan. Many developing countries are experiencing current account surpluses *vis-á-vis* the US. The fiscal deficit in the US, which was earlier being financed by domestic private sector, is now being financed by central banks of Asia. According to the IMF, net financial obligations of the US to the rest of the world could reach 40 per cent of its total economy within a few years which would be unprecedented. The twin deficits in the US economy is a challenge confronting the international community. Some of the other downside risks facing the global economy appear to be arising from (i) the rising global commodity prices, particularly oil prices, (ii) increasing probability of a global hardening of interest rates and the subsequent adjustments, and (iii) the timing and sequencing of the policy induced slowdown of the 'overheated' Chinese economy aimed at ensuring a 'soft landing'.

6.8 Inflation is slowly returning worldwide with the narrowing of output gaps, thus, restricting ability of producers to absorb input costs into profit margins. Higher fuel prices, largely reflecting the spurt in demand from the US and China, pose serious inflation and growth risks. The International Energy Agency (IEA), in a report released in 2004, has warned that a US $ 10 price increase per barrel of oil sustained over one year could trim about 0.8 per cent of Asia's overall economic growth. Some non-fuel commodity prices have flattened after reaching peaks in the first quarter with supply responding to increasing demand. Accordingly, central banks have been sensitising markets to exit strategies from the accommodative monetary policy stance that prevailed over the past two years. Leading central banks such as the US Federal

Reserve System and the Bank of England raised their key policy rates by 25 basis points each in June 2004 and again by 25 basis points each in August 2004.

BALANCE OF PAYMENTS

6.9 The evolution of India's balance of payments (BoP) during 2003-04 reflected robust improvements on several fronts. Merchandise exports surged ahead of the growth of world trade, drawing strength from a distinct firming up of activity in the domestic economy and sustained external demand. Software exports remained resilient and vigorous in the face of the IT slowdown worldwide and a protectionist reaction against outsourcing in some industrial countries. Remittances from expatriate Indians rose strongly, making India one of the largest recipients of such flows. Accordingly, even as burgeoning import demand expanded the merchandise trade deficit to about 2.8 per cent of GDP, the current account recorded a surplus for the third year in succession on a steadily expanding scale. A noteworthy aspect of the strength of the current account is that the rising degree of openness - merchandise and invisibles transactions taken together - estimated at close to 37 per cent of GDP in 2003-04 was driven by a robust export performance. This augurs well for the rising international competitiveness of the Indian economy and the sustainability of the external sector (Table 6.2 and Appendix Table VI.2).

6.10 Significant two-way movements in capital flows dominated the BoP outcome in 2003-04. The strong improvement in India's macroeconomic performance created a preferred habitat for private capital flows, led by unprecedented flows of portfolio investment. This was also reflected in an upgradation of the sovereign rating to investment grade during 2003-04 for the first time since 1997-98. Notwithstanding large outflows in the form of policy-induced prepayments of multilateral and bilateral loans as well as the one-shot redemption of Resurgent India Bonds (RIBs), the capital account recorded sustained inflows. Consequently, net capital inflows in 2003-04 were the highest ever. By March 2004, India had accumulated the sixth largest stock of international reserves in the world, sufficient to finance

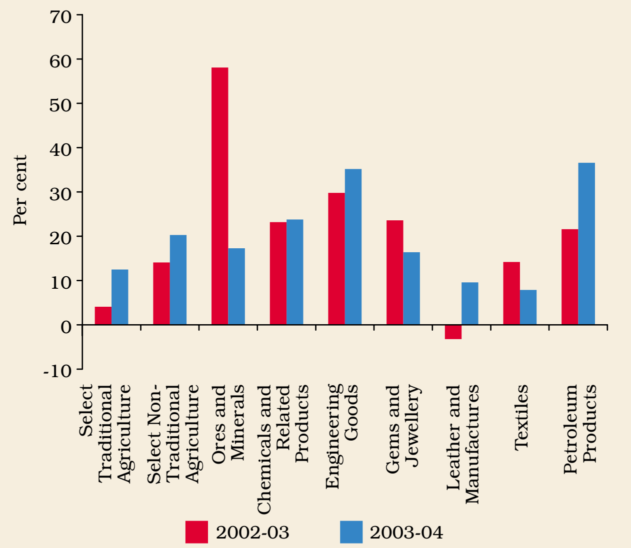
Table 6.2: Balance of Payments – Key Indicators

(US $ million)

Item/Indicator		2003-04(P)	2002-03	2001-02	2000-01	1999-2000	1990-91
1		2	3	4	5	6	7
i)	Trade Balance	-16,706	-12,910	-12,703	-14,370	-17,841	-9,437
ii)	Invisibles, net	25,425	17,047	13,485	10,780	13,143	-243
iii)	Current Account Balance	8,719	4,137	782	-3,590	-4,698	-9,680
iv)	Capital Account, net	22,122	12,113	10,573	10,018	10,444	7,056
v)	Overall Balance #	31,421	16,980	11,757	5,856	6,402	-2,492
vi)	Foreign Exchange Reserves* [Increase(-), Decrease (+)]	-31,421	-16,980	-11,757	-5,830	-6,142	1,278
Indicators (per cent)							
1.	**Trade**						
i)	Exports/GDP	10.4	10.3	9.4	9.8	8.4	5.8
ii)	Imports/GDP	13.2	12.8	12.0	13.0	12.4	8.8
iii)	Export Volume Growth	n.a.	21.8	3.9	23.9	15.5	11.0
2.	**Invisibles**						
i)	Invisible Receipts/GDP	8.6	8.5	7.7	7.6	6.8	2.4
ii)	Invisible Payments/GDP	4.4	5.2	4.9	5.3	3.8	2.4
iii)	Invisibles (Net)/GDP	4.2	3.3	2.8	2.3	2.9	-0.1
3.	**Current Account**						
i)	Current Receipts@/GDP	19.0	18.7	17.0	17.4	15.1	8.0
ii)	Current Receipts Growth@	19.8	17.6	2.4	17.6	12.9	6.6
iii)	Current Receipts@/ Current Payments	107.7	104.1	100.5	95.3	93.0	71.5
iv)	Current Account Balance/ GDP	1.4	0.8	0.2	-0.8	-1.0	-3.1
4.	**Capital Account**						
i)	Foreign Investment/GDP	3.0	1.1	1.7	1.5	1.2	0.0
ii)	Foreign Investment/Exports	25.5	10.7	18.1	15.1	13.8	0.6
5.	**Others**						
i)	Debt - GDP Ratio	17.6	20.2	21.0	22.6	22.1	28.7
ii)	Debt - Service Ratio	18.3	15.1	13.9	17.2	16.2	35.3
iii)	Liability - Service Ratio	19.1	16.1	14.9	18.4	17.0	35.6
iv)	Import Cover of Reserves (in months)	17.0	13.8	11.3	8.6	8.2	2.5

P : Preliminary. n.a. : Not available.
: Includes errors and omissions. * : Excluding valuation changes. @ : Excluding official transfers.

17 months of imports and over five years of debt servicing. The level of reserves exceeded the level of external debt for the first time in India's history. In 2003-04, India also turned creditor to the IMF.



Merchandise Trade

6.11 According to the Directorate General of Commercial Intelligence and Statistics (DGCI&S), merchandise exports grew by 20.4 per cent in US dollar terms during 2003-04 on top of 20.3 per cent recorded in the preceding year (Appendix Table VI.3). Export performance surpassed, by a significant measure, the target set for the year (*i.e.,* 12 per cent) and reflected the growing competitiveness of the Indian manufacturing sector. Certain traditional items in the primary products category did suffer erosion in competitiveness.

6.12 Commodity-wise data for 2003-04 indicate that manufactured products - mainly engineering goods, chemicals and gems and jewellery - were the main drivers of export growth (Appendix Table VI. 4). The rapid expansion in exports of engineering goods, propelled by technology-intensive items such as automobiles and iron and steel, is an indication of the increasing technological sophistication and the growing competitiveness of Indian manufacturing. Exports of gems and jewellery recorded a sharp increase, benefiting from the promotional measures announced in the EXIM Policy. Exports of petroleum products also rose sharply, reflecting the maturing of domestic refining capacity. In the textiles segment, while exports of items using domestic raw materials (*i.e.,* cotton yarn and fabrics) declined, those using synthetic/imported raw materials (man made yarn, fabrics and made-ups) registered a sharp increase. Exports of primary products declined mainly in respect of the traditional items such as cashew, rice and marine products. On the other hand, exports of non-traditional items such as wheat, other cereals, poultry products, fruits and vegetables, meat and meat preparations maintained the rising profile acquired in recent years (Chart VI.2). Over the years, the composition of primary products has shifted significantly in favour of non-traditional items.

6.13 The destination pattern of India's exports shows that exports to Asian countries increased sharply, indicative of the role of improvement in the macroeconomic performance in generating demand (Table 6.3). The pace of expansion in exports to the OECD countries moderated. Among the advanced economies, however, exports to France, Germany, Italy, the Netherlands and the UK increased sharply. Exports to the US also increased, *albeit* at a slower pace, while exports to Japan declined.

Table 6.3: Export Destinations

(Per cent)

Country	India's Export Growth		Partner Country's Real GDP Growth		Country	India's Export Growth		Partner Country's Real GDP Growth	
	2003-04	2002-03	2003	2002		2003-04	2002-03	2003	2002
1	2	3	4	5	1	2	3	4	5
1. UAE	52.7	33.5	7.0	1.9	12. France	20.1	13.7	0.2	1.2
2. People's Republic of China	49.8	107.5	9.1	8.0	13. Germany	19.7	17.8	-0.1	0.2
3. Singapore	48.9	46.2	1.1	2.2	14. Saudi Arabia	19.1	13.8	6.4	1.0
4. Sri Lanka	43.4	46.0	5.5	3.9	15. Malaysia	18.6	-3.1	5.2	4.1
5. Iran	40.1	158.8	5.9	7.2	16. South Korea	18.2	36.8	3.1	7.0
6. Bangladesh	40.0	17.3	5.4	4.9	17. Thailand	16.3	12.3	6.7	5.4
7. Indonesia	36.0	54.8	4.1	3.7	18. Canada	8.8	19.4	1.7	3.3
8. Italy	25.5	12.5	0.3	0.4	19. Belgium	8.7	19.5	1.1	0.7
9. Hong Kong	24.4	10.4	3.3	2.3	20. US	5.2	28.0	3.1	2.2
10. Netherlands	21.9	21.3	-0.8	0.2	21. Russia	0.7	-11.8	7.3	4.7
11. UK	21.5	15.5	2.3	1.7	22. Japan	-8.0	23.4	2.7	-0.3

Sources : DGCI&S and IMF, *World Economic Outlook*, April 2004.

6.14 India's exports to the SAARC countries and China grew sharply by 47.8 per cent and 49.8 per cent, respectively. China emerged as a major trading partner for India. Exports to other major Asian countries such as Hong Kong, Indonesia, Singapore and the UAE also increased sharply. India's participation in regional/bilateral trading arrangements with Asian countries is being increasingly reflected in the changing destination profile of exports in the favour of these countries (Box VI.1).

Box VI.1

Regional Trading Agreements in Asia

Preferential trade among and within a defined geographical trade region is perceived as a second best option in the context of current progress in trade negotiations under the aegis of the World Trade Organization (WTO). According to the WTO, 43 per cent of global merchandise trade is channelised through preferential trading arrangements and this is expected to cross 50 per cent by 2005.

The South Asian Preferential Trade Agreement (SAPTA) among the SAARC countries (Bangladesh, Bhutan, India, Maldives, Nepal, Pakistan and Sri Lanka), which was signed in April 1993, became operational in December 1995. The Governments of South Asian countries decided in May 1997 to move from preferential trading to free trade by 2001, thereby transforming SAPTA into the South Asian Free Trade Agreement (SAFTA) as a part of the larger cooperation plan of the SAARC. In January 2004, Bangladesh, Bhutan, India, Maldives, Nepal, Pakistan and Sri Lanka signed a free trade zone agreement under SAFTA whereby reduction in trade barriers among member countries would begin in 2006.

India has also been actively participating in the regional grouping of Bangladesh, India, Myanmar, Sri Lanka, Thailand Economic Cooperation (BIMST-EC) to promote regional cooperation in trade and investment among member countries. In the Joint Declaration issued after the BIMST-EC Summit held at Bangkok in July 2004, it was agreed that the grouping would henceforth be known as Bay of Bengal Initiative for Multi-Sectoral Technical and Economic Cooperation (BIMSTEC). Member countries, *inter alia*, agreed to focus on specific areas of cooperation, including but not limited to trade and investment, transport and communication, tourism, energy, human resource development, agriculture, fisheries, science and technology and people-to-people contact. Furthermore, the countries agreed to explore the expansion of BIMSTEC cooperation into areas of culture, education, public health, protection of bio-diversity and traditional knowledge, rural community development, small and medium scale enterprise, construction, environment, information and communication technology, biotechnology, weather and climatic research, natural disaster mitigation and management. Members also agreed to take all possible steps including timely completion of the Free Trade Area negotiations for realisation of the full potential of BIMSTEC trade and investment. India made a number of proposals, which, *inter alia*, included hosting a BIMSTEC Ministerial meeting on Energy Cooperation in 2005, setting up a BIMSTEC Centre on Weather and Climate Research and Information in New Delhi and sharing remote sensing data on agriculture.

Efforts have also been made to promote mutually beneficial bilateral trade. The Indo-Sri Lanka Free Trade Agreement signed in December 1998 became operational in March 2000. Under the agreement, tariff on a large number of items would be phased out within an agreed timeframe. While India would reduce the tariff to zero in three years, Sri Lanka would do so in eight years. Both sides would maintain negative lists of items where protection to local industry is considered necessary. For furthering bilateral economic co-operation, a Joint Study Group set up in 2003, recommended a Comprehensive Economic Partnership Agreement (CEPA) between India and Sri Lanka covering broader areas of services and investment in addition to trade in goods. India and Bangladesh have agreed to streamline customs and allied administrative procedures to facilitate unhindered flow of trade between the two countries. India agreed to provide duty free access to 40 tariff lines at a 6-digit level corresponding to 16 categories of Bangladesh products. India and Nepal have extended the validity of the bilateral trade treaty between the two countries for a further period of five years with modification to take care of some of the areas of mutual concern. The treaty would expire on March 5, 2007.

There are two major regional trading groups in Asia. A Preferential Trading Agreement (PTA) among the ASEAN members (Brunei Darussalam, Cambodia, Indonesia, Laos, Malaysia, Myanmar, the Philippines, Singapore, Thailand and Vietnam) signed in 1979, provides for preferential tariffs and non-tariff treatment. Realising the negligible impact of this effort on trade among members due to limited product coverage, the ASEAN countries agreed in January 1991 to establish an ASEAN Free Trade Area (AFTA) by the year 2008. A Framework Agreement setting out the transition towards the AFTA and a Common External Preferential Tariff (CEPT), which came into force in 1994, was accepted as the main formal tariff-cutting mechanism for achieving the free trade area.

India has a sizeable trade with the ASEAN. This group accounted for 9.1 per cent of India's total exports and 9.5 per cent of its imports in 2003-04. Efforts have been made during the last few years to strengthen India's ties with the ASEAN countries. A Framework Agreement on Comprehensive Economic Cooperation was signed between India and the ASEAN in October 2003 with the objective, *inter alia*, of strengthening and enhancing economic, trade and investment co-operation. The contemplated measures for economic co-operation include negotiations for establishing an India-ASEAN Regional Trade and Investment Area (RTIA).

Furthermore, for improving bilateral economic cooperation between India and Singapore, a Joint Study Group on India-Singapore Comprehensive Economic Cooperation Agreement (CECA) was constituted, which submitted its Report in April 2003.

References

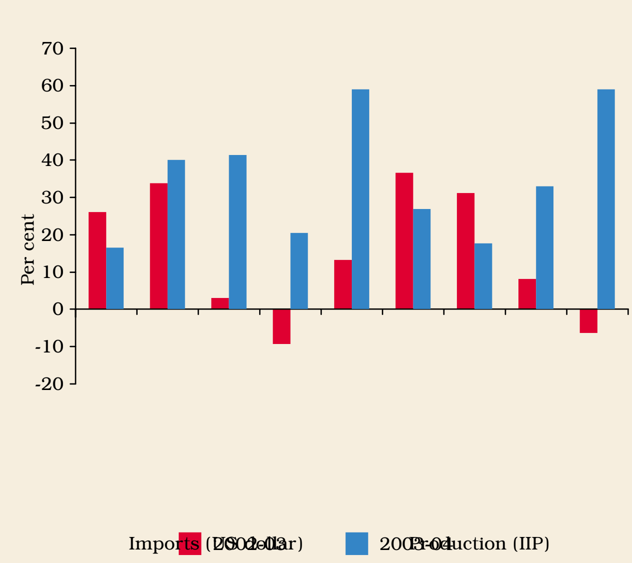
1. Asian Development Bank (2002), "Preferential Trade Agreements in Asia and the Pacific", *Asian Development Outlook*, 2002.
2. Joint Study Group Report on India-Singapore Comprehensive Economic Cooperation Agreement (CECA), April 2003.
3. Joint Study Group Report on India-Sri Lanka Comprehensive Economic Partnership Agreement (CEPA), October 2003.
4. World Trade Organization (2003), *World Trade Report*, 2003.
5. Zebregs, Harm (2004), "Intra-regional Trade in Emerging Asia", *IMF Policy Discussion Paper*, PDP/04/1, April.

6.15 India's imports increased by 25.4 per cent during 2003-04 reflecting a pick-up in domestic industrial activity (Appendix Table VI.3). Oil imports recorded a moderate growth of 16.6 per cent mainly on account of increased volumes driven by the growing demand (consumption *plus* exports) and the stagnant domestic production of crude oil (*viz.,* 33 million tonnes in 2002-03) (Chart VI.3).

6.16 Non-oil imports recorded an increase of nearly 29.0 per cent, led by a sharp increase of 26.9 per cent in the imports of capital goods during 2003-04 on top of the large increase in the preceding year. Non-oil imports excluding gold and silver increased by 25.7 per cent. The co-incident expansion of imports of capital goods and domestic production during 2003-04 is strengthening the environment for a revival of investment demand (Chart VI.4).

6.17 The pick-up in domestic industrial activity fuelled a surge in imports of several intermediate manufactures and raw materials such as iron and steel, non-ferrous metals, paper, paper board and manufactures (including newsprint), artificial resins and plastic materials, chemical materials and products and metalliferous ores and metal scraps. Imports of gold and silver, which had declined in 2002-03, increased by as much as 59.0 per cent during 2003-04, mainly due to revival in rural demand on the back of the rebound in agricultural output. Imports of edible oil increased mainly on account of refined palm oil and palmolein (Chart VI.5, Appendix Table VI.5).

Chart VI.4 : Capital Goods – Imports and Production (Growth Rates)



6.18 Country-wise data indicate an increase in imports from all the major regions. As in the case of exports, the sourcing pattern of imports also shows a distinct tilt in favour of Asian countries. Imports from the East Asian countries, *viz.,* China, Japan, Hong Kong, Malaysia, Singapore, South Korea and Thailand increased sharply during 2003-04. Among other major countries, imports from Australia, Germany, Indonesia, Switzerland, UAE and the US also increased significantly.

Chart VI.3 : Crude Oil – Imports, Production and International Prices

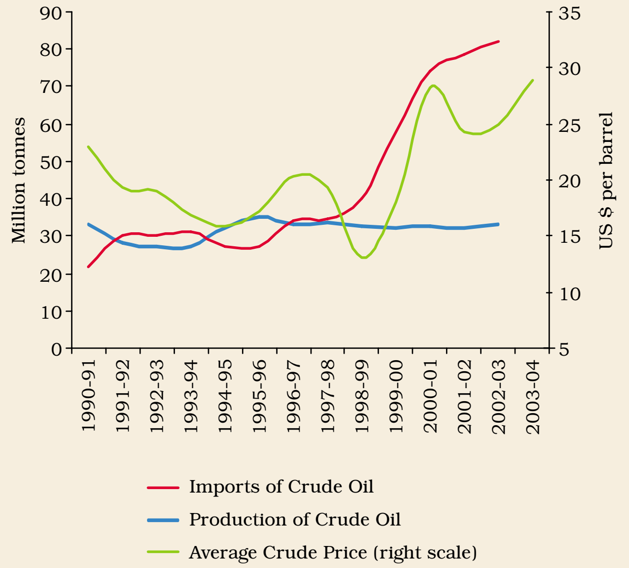
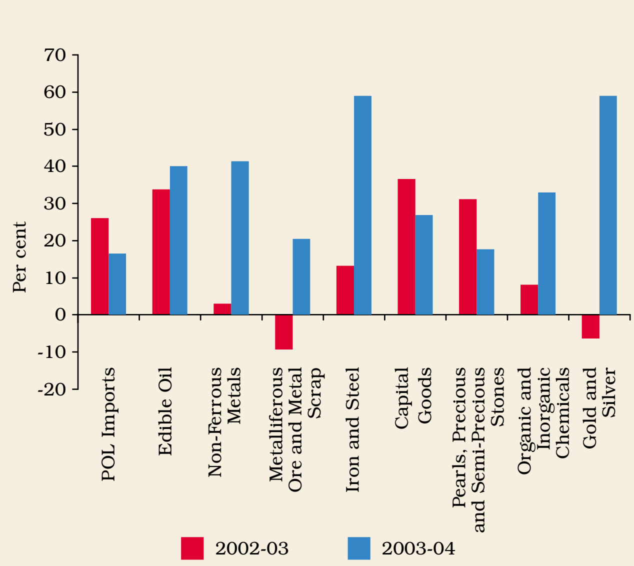


Chart VI.5 : Imports of Major Commodities (Growth Rates)



6.19 During the first quarter of 2004-05 (April-June), exports recorded a robust growth of 28.1 per cent as compared with 8.4 per cent in the corresponding period of the previous year. Imports during the same period posted an increase of 30.8 per cent as compared with 25.3 per cent during April-June 2003. The surge in imports was largely on account of non-oil imports, which increased by 25.8 per cent during April-June 2004 on top of an increase of 31.0 per cent in the corresponding period of the preceding year. The increase in non-oil imports was consistent with the sharp pick-up in domestic industrial production, especially in the capital goods and the intermediate goods sectors. Rising international oil prices contributed to the surge in POL imports.

Invisibles

6.20 The surplus in the invisibles account rose steadily throughout the year, peaking in the fourth quarter. It reached an all-time high at US $ 25.4 billion in 2003-04 (Appendix Table VI.6). Net invisible surpluses have traditionally been a source of support to India's BoP, offsetting merchandise trade deficits and economising on the reliance on external financing. Moreover, a distinct stability has characterised these flows which have shown a remarkable resilience in the face of financial crises and the synchronised global slowdown. The ratio of net invisibles to the trade balance, a measure of BoP support from invisibles, maintained a rising trend through the 1990s, reaching as high as 152.2 per cent in 2003-04 (Chart VI.6).

6.21 Spearheading the progressive improvement in the invisibles balance have been the heterogeneous category of professional and business services including software (which is recorded under 'services') and remittances from nationals employed overseas (recorded under 'transfers'). In recent years, and particularly in 2003-04, these receipts also displayed a growing co-movement. Both entail movement of natural persons. Moreover, with rising skill intensity in the temporary migration from India, the distinction between the two categories is getting increasingly blurred.

6.22 The income account under invisibles has traditionally been in deficit in India's BoP on account of interest payments on external debt, profit/dividend and other payments related to foreign investment in India. During 2003-04, the deficit on the income account worsened on account of a one-time outgo of accumulated interest payments on RIBs (Chart VI.7).

Services

6.23 Exports of services rose by 10.6 per cent in 2003-04. India ranked 20th in the world with a share of 1.4 per cent in global exports of services in 2003. An upward shift in the trend growth of services exports from 7.9 per cent in the first half of the 1990s to 15.3 per cent in the period from 2000-01 to 2003-04 reflected a distinct strengthening along with greater stability. The coefficient of variation of services exports, which increased from 12.0 per cent in the

Chart VI.6 : Invisibles and Trade Deficit

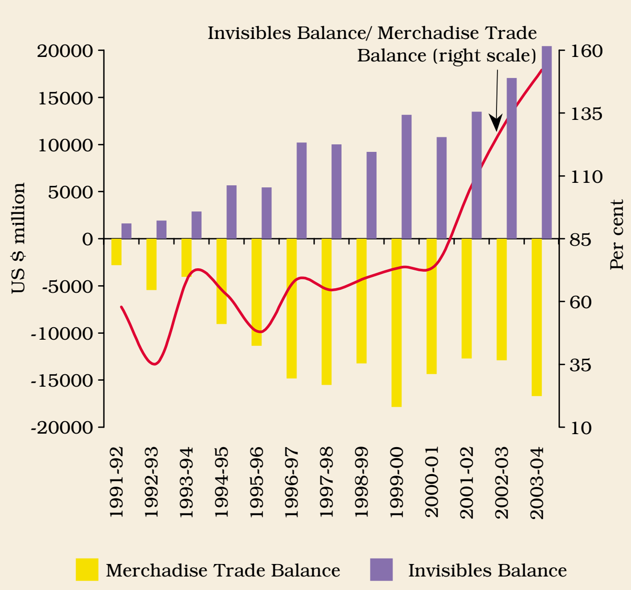
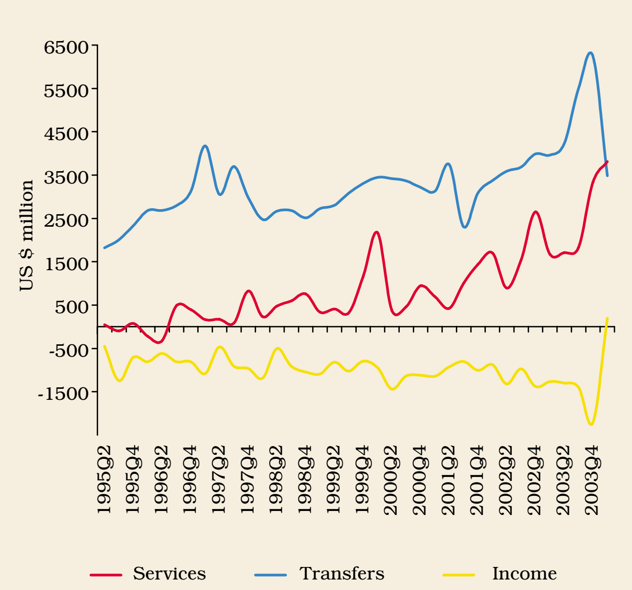


Chart VI.7 : Movement of Net Invisible Receipts



first half of the 1990s to 34.7 per cent in the second half, declined to 17.3 per cent during the period from 2000-01 to 2003-04.

6.24 Travel receipts, a traditional service export from India which had stagnated on account of global recessionary conditions and geo-political instability, also recovered. A strong revival of international tourist interest in India in 2003-04 was reflected in tourist arrivals increasing by 19.6 per cent in contrast to a marginal rise of 0.8 per cent in 2002-03. The US, the UK, Canada and the SAARC countries were the principal sources of tourist traffic into India in 2003-04. Typical of the usual seasonal pattern, earnings from travel peaked in the second half of 2003-04, coinciding with the tourist season in India.

6.25 Earnings on account of transportation and insurance moved in close alignment with merchandise exports. According to the Association of Shipping Corporation of India, about six per cent of India's exports and 23.0 per cent of imports (including 31 per cent of POL imports) were transported by the Indian shipping industry. With transportation and insurance earnings rising by an unprecedented 25.1 per cent, net receipts from transportation turned positive in 2003-04 after a prolonged gap of about 20 years.

6.26 In recent years, sectoral shifts within the spectrum of service exports have also imparted a measure of stability. The buoyant growth of professional, technical and business services has provided a cushion against the slowdown in traditional services such as travel and transportation (Table 6.4). These 'new economy' services witnessed an average annual growth of about 37 per cent during the period 1995-96 to 2003-04, contributing to over 70 per cent of total service exports in 2003-04. Studies have shown that India has a comparative advantage in exports of communication, software and other business services.

Table 6.4: Profile of India’s Services Exports

(Per cent of total services exports)

Year	Travel	Transportation	Insurance	G.N.I.E.	Software	Miscellaneous*
1	2	3	4	5	6	7
1990-91	32.0	21.6	2.4	0.3	0.0	43.7
1995-96	36.9	27.4	2.4	0.2	10.2	22.9
2000-01	16.8	10.1	1.4	3.5	33.6	34.6
2001-02	14.1	9.5	1.3	2.3	36.6	36.3
2002-03	12.1	10.1	1.5	1.2	38.5	36.6
2003-04	14.3	11.6	1.5	0.9	44.2	27.5

* : Miscellaneous services excluding software.
Note : G.N.I.E: Government Not Included Elsewhere.

6.27 Export of software and IT-enabled services rose by about 28 per cent in 2003-04 (Table 6.5). These exports have expanded at a steady rate of over 25 per cent, even though a global IT slowdown arrested the high growth run in the second half of the 1990s. Within this sector, IT enabled services (ITES) and the Business Process Outsourcing (BPO) segments emerged as the anchors of growth. India has remained a dominant exporter globally due to low cost, high quality of product and services and adequate supply of skilled labour. This has enabled it to expand its market share in global IT spending from around 1.5 per cent in 2000-01 to an estimated 3.4 per cent in 2003-04, despite a global slowdown in IT trade. Within ITES service lines, payment services, administration and finance were the fastest growing segments with impressive growth rates of 105 per cent, 74 per cent and 61 per cent, respectively, during 2003-04.

6.28 In terms of outsourcing of IT services, proficiency in the English language provides a comparative advantage to India's exports *vis-á-vis* those of competitors such as China and Mexico. Ireland, which was the biggest hub of ITES, was surpassed by India mainly on account of a relatively larger supply of IT professionals. In order to build upon the current dominant position in the global market, there is an increasing emphasis on diversifying overseas markets, improving cost competitiveness, moving up the IT value chain and focusing on new verticals such as healthcare, utilities and retailing to offset global reduction in IT spending in traditional verticals such as telecom and manufacturing. In the recent period, some downside risks have emerged due to restrictions on outsourcing of software services in certain parts of the world. It is estimated, however, that outsourcing has been resulting in cost saving in the range of 40-60 per cent for the trans-national corporations (see Box II.6, Section II). Exports of other

Table 6.5: Indian Services and Software Exports

(US $ million)

Year	IT Services Exports	ITES-BPO Exports	Total Software and Services Exports
1	2	3	4 (2+3)
1995-96	754	–	754
1996-97	1,100	–	1,100
1997-98	1,759	–	1,759
1998-99	2,600	–	2,600
1999-00	3,397	565	3,962
2000-01	5,287	930	6,217
2001-02	6,152	1,495	7,647
2002-03	7,045	2,500	9,545
2003-04 (Estimates)	8,600	3,600	12,200

ITES : IT enabled services. BPO : Business Process Outsourcing.
Source : NASSCOM.

Box VI.2

New Initiatives for Monitoring Trade in Services

Recent developments in negotiations under the General Agreement on Trade in Services (GATS), the ongoing liberalisation of current and capital account transactions and rationalisation of the reporting requirements have placed an increasing demand on comprehensive information relating to international trade in services. Timely and more disaggregated information on international transactions in services assumes vital importance for effective monitoring, especially because the cross border transactions in services are both on-site and off-site.

Under the common international initiative for strengthening information system on international trade in services, a comprehensive 'Manual on Statistics of International Trade in Services' has been designed by the United Nations to provide a coherent conceptual framework within which countries can structure the statistics collected and disseminated by them.

A Technical Group on Statistics of International Trade in Services appointed in the Reserve Bank submitted its report in March 2002. In pursuance of the recommendations of this Group, the purpose codes for capturing data on international trade in services were revised. This revision in purpose codes is designed to broadly comply with the requirements under the WTO in respect of the General Agreement on Trade in Services (GATS). Under the newly designed software for reporting, transaction-wise details of currency, amount, purpose and country are required to be entered. The package Foreign Exchange Transactions - Electronic Reporting System (FET-ERS) Version 6.2(R) effective April 1, 2004 provides for on-line validation to avoid data entry errors. With the new reporting system in place, the coverage and quality of data on India's international trade in services is likely to be strengthened which would, in turn, contribute to effective monitoring of cross-border transactions.

References

1. Reserve Bank of India (2002), *Statistics of International Trade in Services: Report of the Technical Group*, March.
2. United Nations (2002), *Manual on Statistics of International Trade in Services*.

professional and business services also rose during 2003-04, mainly under communication, financial, management, advertising and office maintenance.

6.29 The impact of the liberalisation of exchange restrictions on current payments was reflected in higher imports of transportation services, financial services, management related services and other business services. Travel payments rose under the segment 'business related travel' and basic travel quota, attributable to outward movement of workers and professionals and spurt in outbound tourist traffic from India. Higher interest payments occurred on account of bullet payment of interest on maturing RIBs. The spurt in investment income payments from 2000-01 onwards was due to the inclusion of reinvested earnings as payments following adoption of the revised definition of foreign direct investment (FDI). The Reserve Bank took initiatives to gather comprehensive information on India's trade in services in the context of the ongoing negotiation on international trade in services under the GATS framework (Box VI.2).

Workers' Remittances

6.30 Inward remittances from Indians working abroad continued to surge, reaching US $ 19.2 billion in 2003-04 and maintaining India's position as the leading recipient of remittances in the world. The sustained expansion in remittances since the 1990s was underpinned by structural reforms, including a market-based exchange rate, current account convertibility as well as a shift in the labour outflow pattern from semi-skilled to increasingly high skilled categories. A gradual shift has occurred in the sources of remittances from oil producing countries of Asia to Europe and America. During 2003-04, workers' remittances remained the mainstay of the current account (Table 6.6).

Table 6.6: Inward Workers' Remittances to India

Year	Flows (US $ million)	Share in Current Receipts (Per cent)	Flows (Per cent of GDP)
1	2	3	4
1990-91	2,083	8.0	0.7
1995-96	8,539	17.1	2.4
1999-00	12,290	18.1	2.8
2000-01	12,873	16.2	2.8
2001-02	12,192	14.9	2.5
2002-03	15,174	15.8	3.0
2003-04	19,235	16.7	3.2

Current Account

6.31 India's current account surplus rose to 1.4 per cent of GDP in 2003-04, extending a phase of surpluses which began in 2001-02. Current account surpluses were also being run across EMEs, the lone exception being Mexico. The counterpart has been the massive current account deficit of the US, indicative of the critical role of the US economy in global recovery (Table 6.7).

Table 6.7: Current Account Balances of Select Countries

(Per cent of GDP)

Country	2003	2002	2001	2000	1996
1	2	3	4	5	6
Argentina	5.7	10.5	-1.6	-3.1	-2.5
Brazil	0.8	-1.7	-4.6	-4.0	-3.0
China	2.1	2.8	1.5	1.9	0.9
Germany	2.4	2.8	0.2	-1.4	-0.6
India*	1.4	0.8	0.2	-0.8	-1.6
Indonesia	3.9	4.5	4.8	5.3	-3.2
Japan	3.2	2.8	2.1	2.5	1.4
Korea	2.0	1.0	1.7	2.4	-4.1
Malaysia	11.1	7.6	8.3	9.4	-4.4
Mexico	-1.5	-2.2	-2.9	-3.1	-0.8
Philippines	2.1	5.5	1.9	8.4	-4.6
Thailand	5.6	5.5	5.4	7.6	-7.9
US	-4.9	-4.6	-3.9	-4.2	-1.5

* : Data for India pertain to financial year (April-March).
Note : (-) indicates deficit.
Source : *World Economic Outlook*, IMF, April 2004.

6.32 India's current account surplus is structurally different from that of EMEs. For most EMEs, it is the merchandise trade account which is in surplus, reflecting high merchandise export growth. In contrast, India's current account surplus, in 2003-04 was on account of services, while the trade account recorded a deficit of the order of 2.8 per cent of GDP (Table 6.8).

6.33 India's current receipts grew at an average rate of 19 per cent during 2002-03 and 2003-04. Consequently, the ratio of current receipts to current payments rose to 107.7 per cent in 2003-04. The steady growth of current receipts has stabilised the 'interest payments to current receipts' ratio at a level of 5.6 per cent and the debt-service ratio at 18.3 per cent (see Table 6.2), which was one of the lowest among the EMEs. The robust pace of growth of current receipts underpinned the current account surplus in 2003-04.

Table 6.8: Current Account Balances of Developing Countries

(US $ billion)

Year	India*		Developing Asia		Western Hemisphere	
	Trade Balance	Services Balance	Trade Balance	Services Balance	Trade Balance	Services Balance
1	2	3	4	5	6	7
1996	-14.8	0.7	-29.4	-6.8	-1.3	-11.4
2000	-14.4	2.5	62.6	-10.2	-4.4	-11.8
2001	-12.7	4.6	56.1	-10.2	-12.0	-13.5
2002	-12.9	6.8	67.3	-5.1	16.3	-8.6
2003	-16.7	10.7	59.3	-12.3	34.3	-7.2

* : Data for India pertain to financial year (April-March).
Note : (-) indicates deficit.
Source : *World Economic Outlook*, IMF, April 2004.

Capital Account

6.34 Large shifts characterised the capital account which dominated the BoP in 2003-04. Massive movements of financial flows occurred in both directions. Debt creating flows ebbed in response to policy changes such as prepayment of high cost official debt and rationalisation of interest rates on NRI deposits. The bullet redemption of RIBs also dampened the net debt flows. Non-debt creating flows, particularly portfolio investments, surged ahead of the resumption of private financial flows to the EMEs. India attracted the highest portfolio investment inflows to Asia in 2003, second only to Korea. With this resurgence, total foreign investment inflows accounted for 65.5 per cent of net capital inflows in 2003-04 (Appendix Table VI.7).

Foreign Investment

6.35 A striking feature of the developments in the capital account in recent times has been the growing significance of non-debt creating flows in line with the policy preference for such flows. Foreign investment - both direct and portfolio - rose to an all-time high in 2003-04, amounting to 3.0 per cent of GDP and 25.5 per cent of merchandise exports (see Table 6.2). Net investment by foreign institutional investors (FIIs) rebounded from depressed levels in the preceding year to record an unprecedented surge during 2003-04. Portfolio flows were recycled to India following readjustments of global portfolios of institutional investors, triggered by the robust improvement in macroeconomic fundamentals, financial performance of the corporate sector and the buoyant and attractive valuations in the Indian equity markets relative to other EMEs in Asia (Table 6.9).

6.36 FDI flows remained subdued during 2003-04 in line with the slowing down of FDI flows to the developing countries in general (Chart VI.8).

6.37 Although Mauritius continues to be the single largest source of FDI into India, its relative significance has been declining. FDI from Mauritius declined sharply during the last two years, constituting 26.1 per cent of total FDI flow to India in 2003-04 as against 32.2 per cent in 2002-03 and as much as 62.3 per cent in 2001-02. The bulk of FDI was channelised into services, computers (hardware and software) and engineering industries (Table 6.10).

Table 6.9: Foreign Investment Flows to India

(US $ million)

	2003-04(P)	2002-03 (R)	2001-02(R)
1	2	3	4
A. Direct Investment (I+II+III)	**4,675**	**4,660**	**6,131**
I. Equity (a+b+c+d+e)	**2,387**	**2,700**	**4,095**
a) Government (SIA/ FIPB)	928	919	2,221
b) RBI	534	739	767
c) NRI	–	–	35
d) Acquisition of shares*	735	916	881
e) Equity capital of unincorporated bodies	190	126	191
II. Re-invested earnings	**1,800**	**1,498**	**1,646**
III. Other capital #	**488**	**462**	**390**
B. Portfolio Investment (a+b+c)	**11,377**	**979**	**2,021**
a) GDRs / ADRs	459	600	477
b) FIIs@	10,918	377	1,505
c) Off-shore funds and others	–	2	39
C. Total (A+B)	**16,052**	**5,639**	**8,152**

P : Provisional. R : Revised. – : Nil/Negligible.

* : Relates to acquisition of shares of Indian companies by non-residents under Section 5 of the FEMA, 1999.

: Data pertain to inter-company debt transactions of FDI entities.

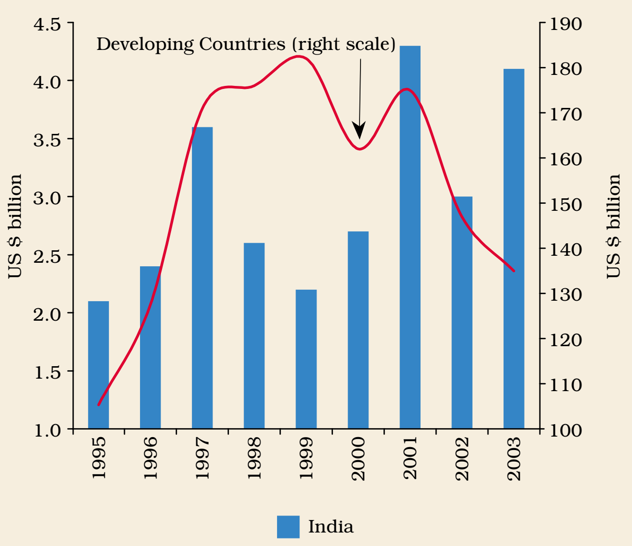
@ : Data represent net inflow of funds by FIIs.

Note : 1. Data on reinvested earnings for 2002-03 and 2003-04 are estimates.

2. Data on foreign investment presented in this table represent inflows into the country and may not tally with the data presented in other tables. They may also differ from data relating to net investment in stock exchanges by FIIs in Section V of this Report.

6.38 The sectoral pattern of FDI inflows to India shows that despite a slowdown in the overall level of FDI, flows into the engineering sector have remained stable, largely in consonance with buoyancy in export growth in that sector. Empirical studies in the Indian context suggest a lagged feedback effect from export growth to FDI. On the other hand, FDI inflows into the software sector continued to exhibit a downward trend despite the robust export performance of the software sector. This suggests that FDI is complementary rather than substitutive in sectors where domestic entrepreneurship and production have acquired an international competitiveness. FDI inflows into the services sector declined to US $ 431 million from a peak of US $ 1,128 million in 2001-02, in spite of high growth in services domestically and sustained exports of professional and commercial services (Table 6.10).

Chart VI.8 : FDI Flows in India *vis-á-vis* Developing Countries



6.39 There has been a growing international interest in the monitoring of portfolio investment flows, particularly in evolving international benchmarks for recording and evaluating information on these flows. The Coordinated Portfolio Investment Survey (CPIS), conducted under the auspices of the IMF, is guided by the objective of removing imbalances and gaps in statistics on global portfolio capital flows (Box VI.3).

Table 6.10: Foreign Direct Investment : Country-wise and Industry-wise Inflows*

(US $ million)

Country/Industry	2003-04(P)	2002-03	2001-02
1	2	3	4
Total FDI	**1,462**	**1,658**	**2,988**
Country-wise Inflows			
Mauritius	381	534	1,863
US	297	268	364
UK	157	224	45
Germany	69	103	74
Netherlands	197	94	68
Japan	67	66	143
France	34	53	88
Singapore	15	39	54
Switzerland	5	35	6
South Korea	22	15	3
Others	218	227	280
Industry-wise Inflows			
Chemical and allied products	46	53	67
Computers	151	297	368
Engineering	274	262	231
Electronics and electrical equipments	103	95	659
Finance	4	54	22
Food and dairy products	63	35	49
Pharmaceuticals	79	44	69
Services	431	509	1,128
Others	311	309	395

* : Data in this table exclude FDI inflows under the NRI direct investment route through the Reserve Bank and inflows due to acquisition of shares under Section 5 of the FEMA, 1999.

P : Provisional.

Box VI.3
Coordinated Portfolio Investment Survey

The Coordinated Portfolio Investment Survey (CPIS), which is conducted simultaneously by all the participating economies, uses standard definitions and encourages best practices in data collection. CPIS is a unique tool for capturing the world totals as well as geographical distribution of the holdings of portfolio investment assets in the form of both equity and debt, thereby leading to a better understanding of these flows. Specifically, the objectives of the Survey are to collect and bilaterally exchange among the participating as well as other countries comprehensive information on portfolio flows, including on the country of residence of the issuer of the stock of cross border instruments.

The progressive liberalisation of international flows has brought into focus measurement difficulties. These difficulties have been reflected in the imbalances at the global level between recorded financial assets and liabilities, with higher flows usually being recorded for liabilities than for assets. Concerned with these global imbalances and the associated discrepancies in income flows at the global level, the IMF Committee on Balance of Payments Statistics decided in 1993 to promote the idea of an internationally coordinated benchmark survey of long-term portfolio investment holdings to facilitate cross country comparisons, permit data exchanges and encourage standardisation and best practice. By undertaking a benchmark survey of holdings, countries would be in a position to obtain a reasonable estimate of the outstanding balances (at market price) of the level of portfolio investment held by their residents. By exchanging comparable data (subject to confidentiality constraints), participating countries can improve the statistics of non-resident holdings of their portfolio investment liabilities as well as associated financial flows and investment income data. Each participating country conducts its own national survey at a particular reference date. After the completion of the Survey, the national compilers supply them to the IMF, which facilitates exchange of data among countries. Along with the CPIS, the IMF also assesses the geographical breakdown of holdings of securities held as a part of reserve assets through its survey of Securities held as Foreign Exchange Reserves (SEFER). The Survey of Geographical Distribution of Securities held by International Organisations (SSIO) is also conducted by the IMF along with the SEFER.

Reference

1. International Monetary Fund (2002), *Coordinated Portfolio Investment Survey Guide*, Second Edition.

Debt flows

6.40 External assistance recorded a net outflow during 2003-04. Negative net resource transfers under external aid (disbursements net of principal repayments and interest payments) have occurred since 1995-96 (Appendix Table VI.8). During 2003-04, the Government prepaid high cost bilateral and multilateral loans of US $ 3.8 billion on the top of the prepayment of US $ 3.1 billion in 2002-03 (Table 6.11). About 68 per cent of the total prepayment in 2003-04 was to multilateral institutions, *i.e.,* the World Bank and the Asian Development Bank (ADB). Among bilateral donors, prepayments to Canada and the Netherlands were sizeable.

Table 6.11: Prepayment of External Assistance

(US $ million)

Year	Donor	Amount Prepaid	Premium Amount
1	2	3	4
2002-03	Multilateral	3,048	62
	IBRD	1,651	27
	ADB	1,397	35
	Bilateral	115	4
	Total	**3,163**	**66**
2003-04	Multilateral	2,584	24
	IBRD	1,398	14
	ADB	1,186	10
	Bilateral	1,230	1
	Total	**3,814**	**25**

6.41 Amortisation of external commercial borrowings (ECBs) rose during 2003-04 in comparison with that during 2002-03. The higher outflow in 2003-04 was on account of redemption of RIBs amounting to US $ 5.2 billion (including accrued interest) in October 2003. ECBs by corporates picked up during January-March 2004 in response to an improvement in the domestic investment climate and the relatively favourable interest rates available in the international financial markets.

6.42 Net inflows into deposit schemes for non-resident Indians (NRIs) were strong in the first half of 2003-04. These flows shared the overall investor optimism generated by the improvement in India's macroeconomic performance and responded to positive interest rate differentials in India *vis-à-vis* international interest rates, rendered attractive by a stable exchange rate. As a consequence of rationalisation of interest rates (see Section VIII in Part II), the inflows moderated in the second half of 2003-04, particularly in respect of the non-resident external rupee accounts [NR(E)RA] scheme. Average monthly inflows slowed down from US $ 365 million during April-September 2003 to US $ 59 million during the second half of 2003-04 except for a sharp increase in October 2003, following one-off effects created by redeployment of a sizeable portion of redemption

Table 6.12: Balances under NRI Deposit Schemes

(US $ million)

Scheme	Outstanding (At end-March)		Net Inflows@	
	2004	2003	2003-04	2002-03
1	2	3	4	5
1. FCNR(B)	10,961	10,199	762	526
2. NR(E)RA	20,559	14,923	4,695	6,195
3. NR(NR)RD	1,746	3,407	-1,816	-3,745
Total	**33,266**	**28,529**	**3,641**	**2,976**

@ : All figures are inclusive of accrued interest and valuation changes arising on account of fluctuations in non-dollar currencies against the US dollar.

Note : Net inflows in respect of NR(E)RA and NR(NR)RD deposits in columns 4 and 5 may not match with the differences between the outstanding stocks on account of exchange rate fluctuations during the year.

proceeds of RIBs. In spite of policy-driven deterrents, net inflows into total NRI deposits were higher in 2003-04 than in the previous year after accounting for shifts from non-resident non-repatriable rupee deposits [NR(NR)RD] to NR(E)RA (Table 6.12).

6.43 Net inflows under banking capital were lower during 2003-04 than in the previous year. Banking capital inflows took the form of drawdown from *nostro* balances and overseas borrowings in the first quarter of 2003-04 as banks compensated for outflows under the foreign currency non-resident (banks) [FCNR(B)] Scheme. Overseas borrowings continued to rise strongly through the rest of the year. On the other hand, *nostro* balances were built up in September 2003 in anticipation of the RIB redemption but were unwound in the subsequent period.

EXTERNAL DEBT

6.44 India's external debt stock amounted to US $ 112.6 billion at end-March 2004 (Table 6.13 and Appendix Table VI.10). During the year, all components of external debt recorded a decline except NRI deposits, bilateral debt and short-term debt. The increase in debt stock between end-March 2002 and end-March 2004 was contributed mostly by NRI deposits with their share increasing to 28.0 per cent of the debt stock from 18.3 per cent. This was due to the effect of increased inflows into the repatriable schemes reflecting discontinuation of the NR(NR)RD scheme (which was not part of external debt) with effect from April 1, 2002. The stock of external debt was also augmented by the redeployment of redemption proceeds of RIBs in NRI deposits.

6.45 Critical indicators of debt sustainability exhibited significant improvement during the year. The ratio of external debt to GDP showed a steady improvement, dropping to 17.6 per cent as at end-March 2004 from 30.8 per cent as at end-March 1995. The debt-service ratio increased during the year mainly on account of redemption of RIBs and prepayments (Table 6.14). Excluding these special transactions, the debt-service ratio would decline to 10.4 per cent. India improved its rank among the top 15 debtor countries from third in 1991 to eighth in 2002. Importantly, among the top 15 debtor countries, India's short-term debt to total debt ratio and short-term debt to foreign exchange reserve ratio are the lowest. India's foreign exchange

Table 6.13: India's External Debt

(US $ million)

Item	End-March	End-March	Variation during the Year	
	2004	2003	Absolute	Per cent
1	2	3	4	5
Multilateral	29,614	29,994	-380	-1.3
Bilateral	17,489	16,814	675	4.0
Trade Credit	4,588	4,974	-386	-7.8
ECB	22,286	22,540	-254	-1.1
NRI Deposit	31,171	23,160	8,011	34.6
Rupee Debt	2,709	2,818	-109	-3.9
Short Term	4,736	4,569	167	3.7
Total	**1,12,593**	**1,04,869**	**7,724**	**7.4**

Table 6.14: External Debt Service Payments

(US $ million)

Item	2003-04	2002-03
1	2	3
1. External Assistance@	7,302	6,308
2. External Commercial Borrowings*	10,446	6,357
3. IMF #	0	0
4. NRI Deposits (Interest Payments)	2,825	1,268
5. Rupee Debt Service	376	474
6. Total Debt Servicing	20,949	14,407
7. Total Current Receipts **	1,14,332	95,475
8. External Debt to GDP Ratio	17.6	20.2
9. Short Term Debt to Total Debt Ratio (%)	4.2	4.4
10. Short Term Debt to Foreign Exchange Reserves Ratio (%)	4.2	6.0
11. Foreign Exchange Reserves to External Debt Ratio (%)	100.3	72.6
12. Debt-Service Ratio (%) ##	18.3	15.1
13. Interest Payments to Current Receipts Ratio (%)	5.6	3.7
14. Debt to Current Receipts Ratio (%)	98.5	109.7
15. Liability-Service Ratio (%)	19.1	16.1

@ : Inclusive of non-Government loans.
* : Inclusive of interest on medium and long term credits.
# : Excluding charges on net cumulative allocation of SDRs.
** : Excluding official transfers.
: Ratio of total debt servicing (Item 6) to total current receipts (Item 7).

Note : 1. Debt service payments in this table follow the accrual method of accounting consistent with BoP compilation and may, therefore, vary from those recorded on a cash basis.
2. Liability-service ratio represents debt service payments and remittances of profits and dividends taken together as a ratio of total current receipts.

reserves provided a cover of a little over 100 per cent of total external debt outstanding as on March 31, 2004.

FOREIGN EXCHANGE RESERVES

6.46 India's foreign exchange reserves increased by US $ 36.9 billion (including valuation gains) during the year, the largest increase ever recorded in a single year. The large accumulation occurred despite the depletion of reserves on account of redemption of RIBs and prepayment of official debt.

6.47 At around US $ 113.0 billion on March 31, 2004 (Table 6.15 and Appendix Table VI.9), India held the fifth largest stock of international reserve assets among EMEs and ranked sixth in the world. As on August 13, 2004, the foreign exchange reserves amounted to US $ 119.3 billion.

6.48 In February 2003, the International Monetary Fund (IMF) designated India as a creditor country under its Financial Transaction Plan (FTP). India, therefore, participated in the IMF's financial support to Burundi in March-May 2003, to Brazil in June-September 2003 and to Indonesia in December 2003. The total lending under FTP to the IMF amounted to US $ 561.3 million during 2003-04.

Reserve Management and Operations

6.49 The significant accretions to the foreign exchange reserves in recent years, especially in 2003-04, have underscored the importance of appropriate reserve management strategies. Foreign currency assets (FCA) and gold holdings together account for about 90 per cent of the combined balance sheets of the Issue and the Banking Departments of the Reserve Bank. The structural shift in the composition of the Reserve Bank's balance sheet in favour of foreign assets has several implications, the most important of which is a change in its risk/return profile.

6.50 The broad objectives of management of foreign exchange reserves in India are similar to those of any other EME. The design of investment portfolios, however, varies widely across countries, reflecting essentially the exposure to liquidity, currency, interest rate and counterparty credit risks and the scope of active management thereof. Portfolio design takes into account a host of factors such as the exchange rate regime, the extent of openness of the economy, the size of the external sector relative to GDP, the state of development and integration of financial markets. In India, the primary objective of reserve management has been to preserve the long-term value of the reserves, in terms of purchasing power, by eschewing risks that may cause sharp volatility in returns. Considerations of safety, liquidity and return provide a hierarchy of preferences that permeates all strategic as well as tactical decisions on deployment of reserves.

6.51 The Reserve Bank of India (RBI) Act, 1934 provides the overarching legal framework for deployment of FCA and gold, defining the broad parameters in respect of currency, instruments, issuers and counterparties. The relevant provisions are contained in Section 17 of the Act. While major convertible currencies constitute the choice set for currency composition of FCA, the investment universe for FCA comprises deposits with other central banks, the Bank for International Settlements (BIS), top-rated foreign commercial banks, debt securities issued by sovereigns and supranational institutions with residual maturity not exceeding 10 years and any other instruments or

Table 6.15: Foreign Exchange Reserves

(US $ million)

As at end of March	Gold	SDR	Foreign Currency Assets	Reserve Position in the IMF	Total (2+3+4+5)	Use of IMF Credit
1	2	3	4	5	6	7
1993	3,380	18	6,434	296	10,128	4,799
1994	4,078	108	15,068	299	19,553	5,040
1995	4,370	7	20,809	331	25,517	4,300
1996	4,561	82	17,044	310	21,997	2,374
1997	4,054	2	22,367	291	26,714	1,313
1998	3,391	1	25,975	283	29,650	664
1999	2,960	8	29,522	663	33,153	287
2000	2,974	4	35,058	658	38,694	26
2001	2,725	2	39,554	616	42,897	0
2002	3,047	10	51,049	610	54,716	0
2003	3,534	4	71,890	672	76,100	0
2004	4,198	2	107,448	1,311	112,959	0

institutions as approved by the Central Board of the Reserve Bank.

Risk Management

6.52 Guidelines in pursuance of the provisions of the RBI Act, 1934 are in place for facilitating investment of FCA. Appropriate benchmarks have been established for the purpose of configuring currency allocation of FCA and maturity pattern (duration) of the investment portfolios in each currency segment. Benchmarks are constructed to reflect the strategic investment objectives after taking into account, *inter alia*, the longer-term prospects of the markets in which FCA are deployed. They also embody the risk tolerance and the expected return in respect of FCA. Tactical deviations from benchmarks are permitted to a limited extent for augmenting returns without, however, altering the risk profile in a significant manner. The benchmarks are reviewed periodically. One of the abiding features of investment benchmarks has been diversification with regard to currency, markets and instruments.

6.53 Accordingly, FCA are invested in multi-currency and multi-market portfolios. During the year 2003-04, there was a moderate shift in the deployment pattern of FCA, whereby, the share of deposits increased and that of securities fell correspondingly, reflecting interest rate uncertainties in major international markets (Table 6.16).

6.54 Movements in the FCA occur mainly out of purchases and sales of foreign exchange by the Reserve Bank in the foreign exchange market in India, including a small volume of transactions in the forward segment. In addition, income arising out of the deployment of foreign exchange reserves is held in the portfolio of the Reserve Bank. External aid receipts of the Central Government also flow into the reserves. In line with the international practices, the Reserve Bank expresses the foreign exchange reserves in US dollar terms for public dissemination, which implies that the movement of the US dollar against other currencies in which FCA are held would also influence its share in the FCA.

Table 6.16: Deployment Pattern of Foreign Exchange Reserves

(US $ million)

	As on March 31, 2004	As on March 31, 2003
1	2	3
1. Foreign Currency Assets	107,448	71,890
(a) Securities	35,024	26,929
(b) Deposits with other central banks and BIS	45,877	33,463
(c) Deposits with foreign commercial banks	26,547	11,498
2. Special Drawing Rights	2	4
3. Gold (including gold deposits)	4,198	3,534
4. Reserve Position in the IMF	1,311	672
5. Total Foreign Exchange Reserves (1+2+3+4)	**112,959**	**76,100**

6.55 Decisions involving the pattern of investments are driven by the broad parameters of portfolio management with a strong bias for capital preservation and liquidity. The entire stock of FCA is invested in assets of the highest quality with a significant proportion convertible into cash at short notice. The counterparties with whom deals are conducted are subject to a rigorous selection process, based on their international reputation and track record, apart from factors such as size, capital, rating, financial position and efficiency of operations. Counterparties could be banks, subsidiaries of banks or security houses.

6.56 The broad strategy for reserve management, including currency composition and investment policy, is decided in consultation with the Central Government. This decision-making procedure is supported by reviews of the strategy on a regular periodic basis within the Reserve Bank. In view of the significant accretion to reserves in 2003-04, this internal review mechanism was further strengthened by the inclusion of two in-house senior experts who are otherwise not involved in the foreign exchange management operations. There has been a renewed emphasis on managing and controlling the exposure to financial and operational risks attendant on deployment of reserves. The risk management functions are also being revamped to ensure development of sound governance structures in line with international best practices, improved accountability, a culture of risk awareness across all operations and efficient allocation of resources for development of in-house skills and expertise.

Audit and Monitoring

6.57 Considerable attention has been devoted to strengthening operational risk control arrangements. Concurrent audit, which is carried out on a real time basis in respect of transactions undertaken by the front office, has been one of the effective tools in this regard. The scope of concurrent audit has recently been expanded to include certain critical areas of the back office operations. A comprehensive external review of the scope of concurrent audit is on the cards. The incidence of exceptions, transgression of exposure limits and errors, being in the nature of operational risk events as revealed in concurrent audit and annual special audit of the front office transactions, have been minimal.

Infrastructure and Related Aspects

6.58 A new IT application for reserve management became operational in September 2003. This is an ORACLE 8i-based Relational Database Management System (RDBMS) application running on HP-UX 11i operating systems. The application is an advanced integrated system linking the front office, back office, middle office and accounting functions, facilitating, Straight Through Processing (STP) of transactions undertaken at the front office.

6.59 The Reserve Bank uses SWIFT as the messaging platform to settle its trades and to send financial messages to its counter parties, banks with whom *nostro* accounts are maintained, custodians of securities and other business partners. Major upgrades to SWIFT facilities, which took place in recent years globally, were successfully carried out by the Reserve Bank. SWIFT is moving towards a significantly improved communication protocol to replace the existing one by the end of 2004. The Reserve Bank achieved SwiftNet migration by end-June 2004, well ahead of the deadline set for the purpose.

External Asset Managers

6.60 A small portion of the reserves is assigned to external asset managers with the objectives of gaining access to and deriving benefit from their market research. This also makes it possible to take advantage of the technology available with asset managers and to provide training to the Reserve Bank's personnel. The asset managers are carefully selected from among internationally reputed asset management entities. They are given clear investment guidelines and benchmarks and their performance is evaluated at periodic intervals. External asset managers' views and outlook on international bond and currency markets are examined and taken as inputs for investment decisions.

Accounting Approach

6.61 Foreign currency assets are held as assets in the Issue Department (foreign securities) as well as in the Banking Department (balances held abroad and investment). Gold is also held in the Issue Department (under gold coin and bullion) and in the Banking Department. Although SDRs form part of India's official reserves, they are held by the Central Government and are not reflected in the Reserve Bank's balance sheet.

6.62 Key accounting practices in the management of reserves are: (i) all realised as well as accrued but unrealised interest/discount incomes are taken to the revenue account with the exception of penal interest and dividend which are accounted for on a receipt basis; (ii) all realised gains/losses on foreign exchange and securities transactions are also taken to the revenue account; (iii) unrealised gains/losses on currency and gold revaluation are taken to the Currency and Gold Revaluation Account (CGRA); (iv) unrealised losses on bonds revaluation are taken to the revenue account as direct deduction from interest income; and (v) outstanding forward exchange contracts are revalued and net losses, if any, are charged to the profit and loss account.

6.63 In the case of bonds/securities held as a part of the FCA, revaluation is undertaken every month on the basis of the month-end market prices. The principle of ‘lower of market or book value’ is followed, *i.e.*, if the market value is lower than the book value, the holdings are written down to the market value and valuation is not altered subsequently even if the market value increases. The income from the foreign exchange reserves is combined with other income of the Reserve Bank.

Disclosure and Transparency Issues

6.64 The Reserve Bank has been making available in the public domain data relating to foreign exchange reserves and its operations in the foreign exchange market. The movements in foreign exchange reserves of the Reserve Bank are published on a weekly basis in the Weekly Statistical Supplement (WSS) to the Reserve Bank's monthly Bulletin. As a part of the Special Data Dissemination Standards (SDDS), the IMF prescribed a data template for disclosure of the international reserves and foreign currency liquidity in respect of countries, subscribing to it. The Reserve Bank has already achieved full disclosure of information pertaining to international reserves and foreign currency liquidity position under the SDDS. The Reserve Bank's Annual Report, 2002-03 and the Report on Currency and Finance, 2002-03 extensively covered the subject of reserve management.

6.65 With the concurrence of the Central Government, the Reserve Bank decided to compile and make public half-yearly reports on management of foreign exchange reserves for enhancing transparency and also for expanding the level of disclosure in this regard. The first report with reference to September 30, 2003 was placed in the public domain through the websites of both the Central Government and the Reserve Bank in February 2004. The second report on foreign exchange reserves with reference to March 31, 2004 is available at the

Reserve Bank's website. This transparency in foreign exchange operations has been appreciated by market participants and also by the IMF.

Adequacy of Reserves

6.66 The Reserve Bank has been pursuing a policy of maintaining an adequate level of foreign exchange reserves to meet import requirements, unforeseen contingencies and liquidity risks associated with different types of capital flows. Adequacy of reserves has emerged as an important parameter in gauging its ability to cushion external shocks. This is viewed not only in relation to trade needs, but also in terms of the preparedness to meet short-term liabilities and to fulfill the need for maintaining orderly conditions in the foreign exchange market in the event of occasional mismatch between supply and demand. A long-term perspective on liquidity is also taken with a view to ensuring that reserves are also adequate in terms of short-term debt obligations and portfolio investments. At end-March 2004, the import cover of reserves was about 17 months. The ratio of short-term debt to foreign exchange reserves declined from 146.5 per cent at end-March 1991 to 4.2 per cent at end-March 2004. The ratio of volatile capital flows (defined to include cumulative portfolio inflows and short-term debt) to reserves declined from 146.6 per cent at end-March 1991 to 36.0 per cent at end-March 2004. In terms of overall external debt and total external liabilities, India's reserves were broadly adequate. Furthermore, India's net debt, *i.e.,* gross external debt minus foreign exchange reserves, was extinguished by end-March 2004. As regards the money-based indicators, there has been a marked improvement, indicative of reduced vulnerability of economic activity to any possibility of massive capital outflows. In terms of macro indicators, the ratio of India's reserves to GDP improved from 2.0 per cent at end-March 1991 to 17.7 per cent at end-March 2004.

6.67 In the recent period, assessment of reserve adequacy has also been influenced by the introduction of new measures that are particularly relevant for EMEs such as India. One such measure requires that the usable foreign exchange reserves should exceed scheduled amortisation of foreign currency debts (assuming no rollover) during the following year. Another adequacy measure is based on a 'Liquidity at Risk' rule that defines the 'worst-case' liquidity needs that a country could face. Under this approach, a country's foreign exchange liquidity need is estimated under different simulated scenarios, using a range of variables, including exchange rates, commodity prices and credit spreads.

INTERNATIONAL INVESTMENT POSITION

6.68 India's net international investment position (IIP) recorded a marked improvement during 2002-03 with net foreign liabilities declining by 12.7 per cent (Table 6.17).

6.69 India's international assets grew by 28.6 per cent, largely on account of reserve assets. Consequently, the share of reserve assets in total foreign assets improved significantly in March 2003. The share of 'other investments' comprising mainly deposits, currency holding and other international assets declined sharply (Table 6.18). This was attributable to the appreciation of the rupee *vis-à-vis* the US dollar as also a sharp decline in returns on investments in the form of bank deposits and fixed income securities in international markets. Indian banks liquidated a sizeable portion of their short-term investments in foreign assets and converted them into

Table 6.17: International Investment Position of India

(US $ million)

Item	End-March 2003P	End-March 2002PR	End-March 1997PR
1	2	3	4
A. Assets			
1. Direct investment abroad	5,054	4,006	617
2. Portfolio investment	721	670	282
2.1 Equity securities	386	356	172
2.2 Debt securities	335	314	110
3. Other investments	12,812	14,256	10,097
3.1 Trade credits	1,097	753	973
3.2 Loans	1,416	2,204	548
3.3 Currency and deposits	7,499	8,765	5,287
3.4 Other assets	2,800	2,534	3,288
4. Reserve assets	76,100	54,715	26,714
Total Foreign Assets	94,687	73,647	37,710
of which: Banks	9,138	11,093	7,271
B. Liabilities			
1. Direct investment in India	30,827	25,408	10,630
2. Portfolio investment	32,138	31,540	18,744
2.1 Equity securities	20,089	18,613	13,631
2.2 Debt securities	12,049	12,927	5,113
3. Other investments	91,788	85,521	89,388
3.1 Trade credits	4,745	3,819	5,698
3.2 Loans	60,993	62,724	67,743
3.3 Currency and deposits	25,569	18,509	15,300
3.4 Other liabilities	482	470	646
Total Foreign Liabilities	1,54,753	1,42,469	1,18,762
of which: Banks	37,169	30,154	18,383
Net Foreign Liabilities (B-A)	60,066	68,822	81,052
of which: Banks	28,031	19,061	11,112
Net Foreign Liabilities as per cent of GDP	11.8	14.4	21.0

P : Provisional. PR : Partially Revised.

Note : Data are partially revised based on extended coverage of FDI data and revised external debt information for 2002 and 2003.

Table 6.18: Distribution of International Assets and Liabilities of India

(Per cent)

Year (end-March)	Distribution of Assets: Direct Investment	Portfolio Investment	Other Investment	Reserve Assets
1	2	3	4	5
1997	1.6	0.7	26.8	70.8
1998	1.7	0.7	26.3	71.4
1999	3.6	0.3	25.3	70.8
2000	3.4	0.2	25.7	70.7
2001	4.2	0.8	26.3	68.7
2002	5.4	0.9	19.4	74.3
2003	5.3	0.8	13.5	80.4

Year (end-March)	Distribution of Liabilities: Direct Investment	Portfolio Investment	Other Investment
	6	7	8
1997	9.0	15.8	75.3
1998	11.5	16.7	71.8
1999	12.3	18.4	69.4
2000	13.3	19.0	67.7
2001	14.7	22.6	62.8
2002	17.8	22.1	60.0
2003	19.9	20.8	59.3

rupee assets. Reflecting the impact of the liberalisation of norms relating to Indian joint ventures/ wholly owned subsidiaries abroad and the growing international competitiveness of Indian corporates, direct investment abroad by the Indian entities turned out to be another high growth component of international assets during 2002-03.

6.70 India's total foreign liabilities increased by 8.6 per cent during 2002-03 due mainly to direct investment and 'other investments' comprising external borrowings,

Table 6.19: Composition of India's International Liabilities

(Per cent)

Year (end-March)	Debt Liabilities	Non-debt Liabilities
1	2	3
1997	79.0	21.0
1998	76.7	23.3
1999	77.1	23.0
2000	74.5	25.6
2001	72.5	27.5
2002	68.8	31.2
2003	66.8	33.2

non-resident deposits and trade credits. Of the total foreign liabilities outstanding at end-March 2003, loans constituted the largest component (39.4 per cent), followed closely by portfolio investment (20.8 per cent), direct investment in India (19.9 per cent) and currency and deposits (16.5 per cent).

6.71 The share of non-debt liabilities in total foreign liabilities increased, *albeit* moderately. Debt liabilities accounted for around two-thirds of total foreign liabilities at end-March 2003 (Table 6.19). The share of debt in India's total foreign liabilities was significantly higher than that of Hong Kong, Korea, Malaysia, Singapore and Thailand.

6.72 The net foreign liabilities of the Indian banking sector increased by 19.8 per cent, despite a rise in its foreign assets by 21.2 per cent between March 2003 and March 2004. Foreign currency denominated assets of local residents increased sharply *vis-à-vis* foreign currency liabilities to local residents (Table 6.20).

Table 6.20: International Liabilities and Assets of Banks in India

(US $ million)

Category/Item	Amount outstanding at end of: March 2004	December 2003	September 2003	June 2003	March 2003
1	2	3	4	5	6
Total International Liabilities	**50,871**	**46,105**	**47,023**	**44,285**	**42,209**
of which:					
FCNR(B) Deposits	10,460	9,690	9,478	9,331	9,261
NRE Rupee Deposits	17,501	15,496	14,370	13,017	11,184
Foreign Currency Borrowings	7,743	6,003	5,002	3,994	3,876
Bonds (including RIBs and IMDs)	6,389	6,128	9,557	9,464	9,281
NR(NR) Rupee Deposits	1,690	2,121	2,399	2,796	3,201
ADRs and GDRs	1,474	1,554	1,146	909	807
EEFC Accounts	1,045	1,015	965	975	1,028
Total International Assets	**26,680**	**23,704**	**23,513**	**22,993**	**22,015**
of which:					
Foreign Currency Loans to Residents	10,159	9,147	8,563	8,215	7,760
Outstanding Export Bills	4,750	4,376	4,317	4,226	4,051
NOSTRO Balances	9,053	7,587	8,079	8,147	7,728

RIBs : Resurgent India Bonds. IMDs : India Millennium Deposits. ADRs : American Depository Receipts.
GDRs : Global Depository Receipts. EEFC : Exchange Earners' Foreign Currency.
Note : All figures are inclusive of accrued interest. In view of the incompleteness of data coverage from all bank branches, data reported here are not strictly comparable with those from all branches.

Box VI.4
International Comparison of International Investment Position

In the aftermath of the financial crises during the 1990s, there has been a general consensus that, apart from the cross border financial flows, stocks of international assets and liabilities of the country as captured by the international investment position (IIP) are an essential component of the analysis of external sector vulnerability. While large build-up of foreign exchange reserves in many Asian EMEs including India, abundance of liquidity in the international financial system and narrowing of the yield spread for fixed-income securities issued by EMEs are often taken as indicators of strength and resilience of the external sector of these economies, it is important to take a closer look at the composition of international assets and liabilities.

Despite considerable consolidation in recent years, India's net international liabilities at US $ 60 billion at end-March 2003 remain significant. In absolute terms, India's net international liabilities were higher than those of other EMEs such as Malaysia, the Philippines and Thailand but lower than those of Korea and Indonesia. As a ratio of GDP, however, India's international assets as well as liabilities were the lowest among the select countries (Table).

Recent trends show that the share of reserve assets in the total international assets is generally much higher for East Asian EMEs as compared with the industrialised countries. Except for Hong Kong and Singapore, reserve assets accounted for close to or higher than 50 per cent of the total international assets for the East Asian EMEs. In the case of India, however, the ratio was the highest at 80 per cent. In terms of composition of international liabilities, FDI was an important source of external finance for countries such as Hong Kong, Malaysia, Singapore and Thailand, while for other EMEs including India, the stock of portfolio investment was higher than the stock of FDI. The net international liabilities to foreign exchange reserves ratio could be taken as an indicator of resilience of the economy in the event of external payments crisis. In terms of this indicator, India's resilience to withstand external sector crisis was higher than most of the Asian EMEs, but lower than that of Malaysia, Hong Kong and Singapore.

Table : Cross-Country IIP: Select Indicators (end-December 2002)

(Per cent)

Country	As a Ratio of GDP		Reserve Assets as a Ratio of Total International Assets	As a Ratio of Total International Liabilities		
	Foreign Assets	Foreign Liability		Direct Investment	Portfolio Investment	Other Investment
1	2	3	4	5	6	7
India	18.6	30.5	80.4	19.9	20.8	59.3
Hong Kong	606.9	404.6	10.9	49.0	13.6	37.4
Indonesia	31.7	100.0	66.2	7.6	9.4	83.0
Japan	73.1	38.1	15.3	4.9	38.4	56.7
Korea	43.6	58.8	58.5	22.4	41.6	36.0
Malaysia	76.3	85.8	47.8	29.3	13.9	56.9
Philippines	40.0	88.6	51.9	16.2	26.5	57.5
Singapore	428.4	378.2	21.4	44.3	13.4	42.4
Thailand	46.0	82.2	66.9	36.5	17.1	46.3
US	592.5	821.1	2.6	17.5	39.2	43.2

Note : Data for India relate to end-March 2003.

6.73 In the post East Asian crisis, central banks in the EMEs of Asia have exhibited strong preference for reserves as an insurance against external shocks. A comparison of the international investment position of India *vis-à-vis* other EMEs of Asia reveals that although other Asian countries, such as Indonesia, Korea, Malaysia, the Philippines and Thailand also maintain high levels of reserve assets, the ratio of reserves to total foreign assets in these countries stands lower than that of India (Box VI.4).

Outlook

6.74 Favourable global growth prospects are being signalled by the IMF, which revised its 2004 growth forecast upwards to 4.6 per cent in its *World Economic Outlook,* April 2004. Recent data show considerable uncertainty surrounding the strengthening of global economic recovery on account of the outlook on international crude oil prices. Global imbalances and possibility of disruptive currency movements, firming up of commodity prices, transition to high interest rates and the uncertain prospects of soft landing of the China's economy continue to be some of the major uncertainties and risks facing the global economy.

6.75 India's external sector would benefit from the prospects of strengthening of world output and trade in 2004. Merchandise exports have started the year on a high note, rising by 28 per cent during April-June 2004. The optimistic industrial outlook augurs well for consolidating and building upon the gains in international competitiveness. The key engines - software and remittances - are likely to be sustained, given the intensity of skill and specialised competency in labour outflows. By current reckoning, India has entered a phase of durable current account surpluses in the BoP, even after accounting for any acceleration in imports resulting from the positive macroeconomic outlook. The level of reserves is comfortable at present. Globalisation and the interface with new types of external transactions, particularly those impacting the overall international investment position, however, warrant a careful and continuous re-assessment of the adequacy of reserves.

VII ASSESSMENT AND PROSPECTS

ASSESSMENT OF 2003-04

7.1 The Indian economy recorded a strong performance during 2003-04. While the main driver of growth was the resurgence of agricultural production from the drought of the preceding year, the other factors included buoyant external demand and continued industrial recovery. The performance of agriculture in 2003-04 was typical of a normal monsoon year following a drought year as has been observed on previous occasions. The notable feature this time was the simultaneous and well distributed firming up of activity in industry and services. Exports contributed significantly to higher growth in a wide range of manufacturing industries – machinery and transport equipment, automobiles, iron and steel, chemicals and chemical products – attesting to the rising international competitiveness of Indian industry. Capacity utilisation improved in several manufacturing industries as well as in electricity generation and mining and quarrying. A robust expansion of activity in trade, hotels, transport and communication paved the way for strong growth of the services sector, well above the average for the period 1993-2003. Yet another heartening feature was the resilience of the information technology enabled services and business process outsourcing activities despite some evidence of increasing protectionist postures in major international markets.

7.2 The return to high growth in 2003-04 brought with it renewed business optimism and consumer confidence in the near-term outlook for the economy and a wider appreciation regarding India's potential for growth. It also underscored the need for consolidation of these gains and reorientation of the strategies for macroeconomic management so that a high growth trajectory is sustainable over the medium-term. At the same time, concerns have emerged about the need to ensure that all sections of society share in the gains from higher growth and participate in the realisation of India's potential in the years ahead. This reappraisal of the overall approach and strategy is leading to some rebalancing of macroeconomic priorities and tasks. Increasingly, the focus of ongoing structural reforms is turning to the quality of growth embodied in development, particularly of the rural economy.

7.3 Significant gains were posted in the external sector, indicative of a growing resilience of the economy to cushion domestic activity against external and internal shocks. The run of current account surpluses that began in 2001-02 was extended into 2003-04 – a steady rise from 0.2 per cent of GDP to 1.4 per cent. The foreign exchange reserves rose to US $ 113 billion by end-March 2004 and further to US$ 119.3 billion as on August 13, 2004. Reflecting the rising technology and knowledge content in the output of industry and services, the exports of manufactured goods as also travel-related and private business services grew robustly. The growth rate of merchandise export crossed 20 per cent in US dollar terms for the second consecutive year. With import growth at 25.4 per cent, the trade deficit increased from US $ 8.7 billion in 2002-03 to US $ 13.6 billion in 2003-04. Remittances from Indians abroad, which form a significant share of global remittance flows, continued to be a key component of India's balance of payments. The role of invisible earnings in underpinning the strength of the current account is perhaps the most noteworthy feature of balance of payments developments over 2001-04, especially since they enabled meeting a sizeable expansion in import demand without recourse to additional external liabilities. Rising international confidence in India's macroeconomic performance in an era of abundant international liquidity spurred large inflows of private capital in 2003-04 in the form of portfolio investments in domestic capital market. There was a reduction in debt owed to multilateral agencies by way of prepayments, besides the redemption of Resurgent India Bonds (RIBs). Consequently, indicators of external debt sustainability such as debt to GDP and debt service ratios continued to record a healthy improvement. These developments, coupled with the rising surplus in the current account, facilitated a step-up in the pace and spread of the liberalisation of the exchange regime.

7.4 The year 2003-04 witnessed a consolidation of gains achieved in respect of finances of the Central Government. The key indicators – revenue deficit, gross fiscal deficit and primary deficit – were better in the provisional accounts released by the Controller General of Accounts than those projected in the budget estimates as well as in the revised estimates. The improvement in Central finances was brought about by a reduction in the revenue deficit by 0.5 per cent of GDP in the revised estimates *vis-á-vis* the budget estimates. On the revenue side, there was an increase in tax receipts, mainly under corporate tax and service tax, as also in receipts from disinvestments, dividends and profits. On the expenditure side, there was a reduction in food and petroleum subsidies and non-Plan grants to States, along with some curtailment in capital outlay. These developments enabled an improvement in cash management by the Central Government. This progress in fiscal consolidation was accompanied by debt restructuring in the form of debt buybacks with the banking system, debt swaps with the States and prepayment of external debt. It also paved the way for the enactment of the Fiscal Responsibility and Budget Management Act, 2003. Although a fuller picture of the finances of the State Governments for 2004-05 is still emerging, the lower recourse to ways and means advance (WMA) - a leading indicator - reflects a slightly better financial discipline.

7.5 Another noteworthy feature of macroeconomic management in 2003-04 was the reining in of inflationary pressures. While in the early part of the year, global factors aided a benign inflationary situation, the latter part of the year was characterised by periodic episodes of hardening of international prices of metals, cotton, industrial intermediates and raw materials and a soaring of international crude oil prices in the closing months of the year. Transport disruptions in the beginning of the year, upward revisions in electricity prices and localised drought conditions in vegetable growing regions of the country also resulted in transient supply side pressures. Inflation receded in the first half of the year, reaching a trough in August 2003, before being driven up almost continuously up to January 2004 by a combination of international and domestic factors. By the end of the year, however, inflation had retreated to the levels anticipated by the Reserve Bank.

7.6 Monetary policy assigned priority to the revival of investment demand in the economy in 2003-04 in an environment of macroeconomic and financial stability. Cuts in key policy instruments – the CRR and the repo rate – were accompanied by active management of liquidity and refinements of the modes of delivery of bank credit, particularly to the priority sector, housing and infrastructure. The stance of monetary policy enabled a general reduction in the spectrum of market interest rates, although commercial bank lending rates did not decline commensurately. The expansionary effects of large capital inflows posed a challenge to monetary policy, especially since the absorption of liquidity through non-food credit remained lacklustre except in the last quarter of the year. This necessitated policy intervention almost continuously throughout the year to sterilise the capital flows and prevent undue monetary expansion. Open market operations, supplemented by repos, prepayment of external debt and liberalisation of outflows of foreign exchange were helpful in staving off the full impact of the capital inflows. Despite these actions, money supply expanded by 16.6 per cent – above the indicative rate of 14.0 per cent envisaged in the Monetary and Credit Policy Statement of April 2003. The institution of the Market Stabilisation Scheme in April 2004, which provides for issuance of Government securities exclusively for sterilisation operations, enhances the capacity of the Reserve Bank to deal with capital flows in future.

7.7 During 2003-04, domestic financial markets experienced orderly and stable activity in general, under conditions of ample liquidity. In the money market segments, interest rates displayed close co-movement and remained below the LAF repo rate over the year except for a few brief spikes. Turnover in the call money market declined in the second half of the year with activity shifting to other segments of the money market, particularly, the repo market outside the LAF, a segment which gained vibrancy and depth. The Government securities market was characterised by declining yields, reflecting the stance of monetary policy. The yield curve steepened in the latter part of the year, driven by market expectations relating to inflationary pressures and the raising of some major international interest rates. The foreign exchange market witnessed orderly conditions during the year. The exchange rate of the rupee appreciated against the US dollar, but depreciated against Euro, Pound Sterling and Japanese Yen during the period.

7.8 Efficient functioning of the financial system and an environment of financial stability were concurrent pursuits of the Reserve Bank. In 2003-04 heightened sensitivity to these objectives was reflected in the stance of financial policies. Issues relating to corporate governance and appropriate disclosures were the focus of the conduct of financial regulation. At the same time, prudential norms and supervision continued to be tightened and benchmarked to international best practices and the emphasis also continued to shift from micro regulation to risk-based supervision. A significant development during the year was a successful pilot run for risk-based supervision (RBS), aimed at allocating supervisory resources in accordance with the risk profile of banks. The initiatives taken in recent years were reflected in the significant improvement in profitability, asset quality and capital across the financial system.

7.9 The technological infrastructure for the smooth and secure functioning of the payment system was strengthened with the implementation of Real Time Gross Settlement (RTGS) system, the Special Electronic Funds Transfer system and the Online Tax Accounting System. The Negotiated Dealing System(NDS)-Clearing Corporation of India Ltd.(CCIL) system enabled an improvement in LAF auctions by providing in a timely fashion, all the parameters such as issue duration, type of auctions and opening and closing time. The CCIL, which also offers a multilateral netting mechanism for inter-bank spot and forward dollar-rupee transactions, has provided time and cost benefits to banks. Introduction of exchange traded interest rate derivatives in the National Stock Exchange and allowing sale of Government security against existing purchase contract provided depth to the Government securities market which switched to the Delivery *versus* Payment (D*v*P III) mode with effect from April 2, 2004.

7.10 International developments continued to have a bearing on domestic growth and inflation in 2003-04. The global economic recovery broadened and strengthened in 2003 led by the US and emerging Asia – most notably China and India. The recovery was underpinned by an acceleration in world trade, a pick-up in industrial activity, strong corporate performance and revival of consumer confidence. Economic activity in the UK and Japan strengthened although deflation haunted the stronger-than-expected growth in the latter. In the Euro area, recovery remained subdued and incipient. Inflation was benign in various parts of the world in spite of the rise in commodity prices, particularly oil prices. In recent months, while overall global growth prospects have improved markedly, monetary authorities all over the world are gearing up to contend with the return of inflation, the imminent reversal of the interest rate cycle, the persistence of large macro imbalances, and possible dangers of disruptive global currency adjustments.

OUTLOOK FOR 2004-05

7.11 Early developments in 2004-05 present several continuing strengths in the economy though accompanied by some uncertainties. The pre-monsoon assessment by the Meteorological Department was optimistic with the forecast of a normal monsoon. The monsoon set in almost ten days before time and the rainfall was normal in June 2004. The rainfall outlook became uncertain in July with the cumulative rainfall received till July 28, 2004 amounting to 15 per cent below the Long Period Average (LPA). In terms of spatial distribution, only 12 out of 36 meteorological sub-divisions had received excess/normal rainfall (as against 32 in the corresponding period of 2003). The monsoon, however, revived in August and the cumulative rainfall deficiency declined to seven per cent below the LPA by August 11, 2004. The spatial distribution of rainfall also improved significantly. Although the progress so far has not been as satisfactory as in the corresponding period of the South-West monsoon season of 2003, the earlier apprehensions of drought have distinctly receded. Indeed, 27 sub-divisions have received normal/excess rainfall in contrast to only 17 sub-divisions receiving normal/excess rainfall in the corresponding period of the drought year 2002. A clearer assessment of rainfall, as the monsoon progresses into central India and northern plains, will enable a firmer prognosis of the prospects for agriculture.

7.12 Industrial activity has gathered strength, rising by 7.6 per cent in April-June, 2004. All constituents – manufacturing, electricity and mining – have shared in this expansion *albeit* with some slowdown in electricity generation in the months of May and June. Seven manufacturing groups – wool, silk and man-made fibre textiles, basic chemicals and chemical products, machinery and equipment, leather and fur products, cotton textiles and textile products and metal products and parts – are leading the acceleration of activity. The industrial climate reflects a revival of investment demand and building up of capacity. In particular, the capital goods and the intermediate goods sectors have recorded robust growth signifying the quickening of investment activity. This has been supported by improved corporate profitability, expansion in non-food credit and continuing optimism regarding production and export growth. On the other hand, production of consumer goods has slowed down considerably with the sustained growth in consumer durables providing a silver lining.

7.13 The growth of the services sector is expected to build upon the momentum achieved in the preceding year and be sustained above trend levels. The principal drivers of service sector growth would be trade, hotels, transport and particularly communication which has registered robust expansion in the recent past. Community, social and personal services are also expected to record significantly higher growth. Overseas markets would increasingly provide the impetus for growth for a wide range of industrial products and services. In this context, the growing international competitiveness of India's business services augurs well for domestic producers. The prospects of certain categories of services such as trade and transport would depend significantly upon the performance of the agricultural sector. Similarly, the prospects for construction activity are linked to the production performance of electricity, coal and cement sectors.

7.14 In view of the above, on current indications, while the prospects for GDP growth continue to be bright, in particular, due to a possible acceleration in growth of world output and enhanced domestic investment activity, there are also downside risks emanating from uncertain monsoon as well as the possible persistence of high and uncertain oil prices. These risks impart an element of downward bias to the estimates of GDP growth made at the beginning of the year but evolving strengths during the rest of the year may restore the position and in any case India will continue to be among the top performers globally.

7.15 In the external sector, the robust performance characterising the preceding two years has extended into 2004-05. Merchandise export growth surged to 28 per cent in April-June, 2004 reflecting the sustained momentum of manufacturing activity and the conducive international environment. The firming up of aggregate demand in the economy is mirrored in import growth of 31 per cent in April-June 2004, with non-oil imports rising by 26 per cent and a trade deficit higher than in April-June last year. Capital flows have moderated with net outflows of US $ 0.8 billion under non-resident deposit schemes in the first quarter of 2004-05. Portfolio investment by FIIs recorded net outflows in May-July in tune with the observed pattern in other emerging markets as US interest rates are rising. On the other hand, net inflows in the form of FDI and ADRs/GDRs have gathered momentum. For the first quarter of 2004-05, the balance of payments recorded an overall surplus of US $ 7.5 billion. Reflecting these developments, the foreign exchange reserves crossed US $ 120 billion on July 2, 2004 before declining marginally to US $ 119.3 billion on August 13, 2004. Over the rest of the year, the outlook for the balance of payments appears reasonably strong and resilient. While the hardening of international crude prices is likely to increase the value of POL imports, sustenance of the robust growth of exports of merchandise and services recorded in the early months of the year would enable absorption of the additional import financing requirements. Accordingly, the current account is expected to remain in surplus *albeit* at a more moderate level than in 2003-04. Net capital flows are likely to remain positive, reflecting the underlying strength of the macroeconomic fundamentals and sustained international investor confidence in India. While the Indian economy may not have to deal with surges in capital inflows of the order of the preceding year, especially in the context of churning of portfolio investment flows in Asia, domestic financial markets must nonetheless be prepared for significant capital flows for the year as a whole.

7.16 Inflation, measured by year-on-year changes in the wholesale price index (WPI), has been edging up since May 15, 2004 driven up by prices of iron and steel, mineral oils, coal and vegetables. The CPI inflation, however, continues to be at moderate levels. The WPI inflation rate touched 8.0 per cent on August 7, 2004 following the increases in the prices of petroleum products, iron ore, iron and steel and coal. The hardening of inflation in 2004-05 has been mainly on account of the influence of international price movements in respect of crude oil and metals, particularly iron and steel. Over the rest of the year, pressures from international prices on domestic inflation are expected to moderate although considerable uncertainty surrounds the short-term movements in international crude oil prices, which would influence the domestic inflation outlook. Another important factor which would determine the inflation outlook in India is the progress of the monsoon, after taking into account the shortfalls and uneven spread of rainfall in July which is the sowing month of the *kharif* season. The overhang of liquidity would also need to be carefully monitored in view of its potential to pose demand pressures on prices. Domestic factors which could have a bearing on the inflation outcome include possible gaps in the availability of oilseeds, edible oil and cotton which have witnessed rising consumption levels relative to domestic production. Domestic iron and steel prices continue to remain at elevated levels even though international prices have plateaued. The outlook for headline inflation is, on current indications, less optimistic than what was envisaged at the beginning of the year. Price pressures could be a cause of some concern though it remains to be seen how the imported price shocks would evolve globally and be absorbed domestically. The comfortable level of foreign exchange reserves, however, provides the wherewithal for ensuring adequate supplies and for moderating inflationary pressures on the common man. It is relevant to note that inflation, as measured by the year-on-year changes in the consumer price index (for industrial workers), on a point-to-point basis, was 3.0 per cent in June 2004 and 3.4 per cent on an annual average basis. The consumer price index does not, to the same extent, reflect the price pressures from iron and steel and mineral oils because of the relatively low weight of these items in this index. In any case, the inflation environment needs to be monitored closely on a continuous basis for any unforeseen developments either in the global or in the domestic environment, with a view to considering prompt as well as measured responses, as appropriate.

7.17 Central Government finances were characterised by a higher growth in revenue receipts during April-June 2004 on account of higher growth in corporation tax, income tax and excise duties, partially offset by decline in customs duties and larger tax assignments to the States and the Union Territories. There was also a substantially higher growth in aggregate expenditure in comparison with the corresponding period of the previous year, primarily due to higher revenue expenditure. The growth in revenue deficit remained unchanged at 15.9 per cent as compared with the corresponding period of the previous year. The gross fiscal deficit, however, was higher by 8.0 per cent as against a decline of 2.4 per cent in the previous year.

7.18 Gross market borrowings [net of the Market Stabilisation Scheme (MSS)] of the Centre for 2004-05 are budgeted at Rs. 1,50,817 crore, while net market borrowings would amount to Rs. 90,365 crore. During 2004-05 (up to August 21, 2004), 36.5 per cent of the gross borrowing programme has been completed as compared with 59.8 per cent during the corresponding period of the previous year. An additional amount of Rs. 60,000 crore is expected to be absorbed under the MSS, of which, Rs. 52,231 crore has been raised so far. The gross allocation for the State Governments under their market borrowing programme during 2004-05 is kept at Rs. 42,020 crore, inclusive of Rs. 24,000 crore under the Debt Swap Scheme (DSS). During 2004-05 (up to August 21, 2004), the State Governments raised a gross amount of Rs. 22,259 crore. Going by the current indications, the borrowing of the States demonstrating better fiscal management could be completed comfortably as per the budgeted programme.

7.19 Money supply expanded faster in the first quarter of 2004-05 on a year-on-year basis, mainly on account of the large increase in net foreign assets of the Reserve Bank which drove up reserve money sharply in comparison with the preceding year. Broad money (M_3) grew at a higher rate of 15.7 per cent as on August 6, 2004 as compared with 11.7 per cent last year. Currency demand remained strong in consonance with the general improvement in economic activity, which was also reflected in the sharp increase in non-food credit. The revival of agricultural growth and the stepping up of procurement operations resulted in a turnaround in food credit from a decline of Rs. 6,228 crore in April-August 8, 2003 to an increase of Rs. 6,481 crore in the current year up to August 6, 2004. Financial markets experienced ample liquidity conditions with a liquidity overhang of about Rs. 1,00,000 crore or about 5 per cent of M_3 as compared with about 1.5 per cent of M_3 last year. With the institution of the MSS, there has been a shift of liquidity from the LAF to the MSS.

7.20 Financial market conditions have, by and large, remained stable during 2004-05. The weighted average call money rates have continued to hover close to the repo rate of 4.5 per cent during 2004-05 so far. Activity in the money market continued to shift to the collateralised segments such as the repo market. As regards the Government securities market, the market borrowing programme and pick-up in credit offtake have put some pressure on yields on Government securities, especially at the long end. The yield curve of Government securities has steepened with the yield of the 10-year benchmark security increasing by 139 basis points during April-August 10, 2004 to touch 6.54 per cent. Corporate bond yields also rose, with the spread of the five-year triple-A corporate bond over the Government security with similar maturity widening to 100 basis points by July 27, 2004 from 72 basis points on April 6, 2004. Stock markets recovered from a plunge on May 17, 2004 and currently display stable conditions. The foreign exchange market displayed orderly conditions. The rupee came under moderate pressure in May 2004 on account of turbulence in the equity market and the trends in global liquidity. Since April 1, 2004 the rupee depreciated against the dollar by 5.8 per cent (as on August 10, 2004). Reflecting the spot market conditions, the three and six month forwards have turned from discounts into premia in the recent period. As real activity is picking up globally and inflation is rising across the economies, several central banks have raised their key policy rates. The impact of the northward movement of international interest rates is likely to have some impact on domestic interest rates and financial markets would have to manage these challenges.

7.21 The pick-up in credit demand observed in the second half of 2003-04 continued to be in evidence in the current year, reflecting buoyant industrial activity and to an extent, a base effect as credit offtake in the comparable period of 2003-04 had slowed down significantly. After factoring in the base effect of higher growth in the latter half of 2003-04, the overall credit offtake during 2004-05 at 16-16.5 per cent, as projected in the May 2004 Annual Policy Statement, should be adequate to meet the credit needs of all the productive sectors of the economy.

7.22 The stance of monetary policy for 2004-05 continues to be guided by the objectives of provision of adequate liquidity for meeting credit growth and to support investment and export demand while keeping a very close watch on the movements in the price level. Consistent with the above, while continuing with the *status quo,* monetary policy would pursue an interest rate environment that is conducive to maintaining the momentum of growth as well as ensuring macroeconomic and price stability. The confluence of global factors - in particular, the rise in international interest rates - and domestic developments with respect to capital flows, liquidity management and the unforeseen impact of supply shocks have necessitated close and careful monitoring of price trends, keeping in view the policy preference for stability. In this background, the need, the extent and the timing of review of the policy stance would depend not only on these unfolding circumstances but also on the adjustments that take place in the financial markets, given their sensitivity to the global and domestic conditions.

7.23 Monetary policy would continue to enhance the integration of various segments of the financial market, upgrade credit delivery systems, nurture a conducive credit culture and improve the quality of financial services. There is also a need to consolidate the gains obtained in recent years from reining in inflationary expectations given the volatility in the inflation rate during 2003-04 and subsequent spikes in headline inflation during 2004-05 so far. It is important to appreciate that sustained efforts over time have helped to build up confidence in price stability. Inflationary expectations can turn adverse in a relatively short time if noticeable upward movements in prices continue to take place. While the economy has the resources and resilience to withstand supply shocks, the possible consequences of continued abundance of liquidity need to be monitored carefully. As such, the inflationary situation needs to be watched closely with a view to respond in a timely but measured manner and there is no room for complacency on this count. Maintaining confidence in price stability is a continuing policy objective.

REAL SECTOR

Agriculture

7.24 It is an imperative that the agricultural growth rate is enhanced to around 4 per cent per annum as the critical minimum in order to sustain an overall growth trajectory of the economy at 7 per cent and more. If agricultural growth were to continue at its long-term average of 2.5 to 3.5 per cent, it would be difficult for industry and services to grow in the range of 9-10 per cent that would be necessary to attain the overall growth rate of 7 to 8 per cent. To attain higher growth in agriculture, the major areas requiring attention in the financial sector are, *inter alia,* spread of insurance against crop losses, development of commodity-derivatives market to minimise the impact of price uncertainties and facilities for meeting the entire - not merely the credit - needs of the rural economy.

7.25 The recurring episodes of localised droughts in several meteorological sub-divisions raise concerns of crop failure even in a good monsoon year. Production of coarse cereals, pulses, cotton and sugarcane is most vulnerable to localised droughts. In this context, measures announced in the Union Budget for 2004-05 such as launching of a nation-wide water harvesting scheme, restoration of water bodies and restructured Accelerated Irrigation Benefit Programme (AIBP) are significant. If properly implemented, these measures would provide some relief to the drought-prone regions.

7.26 Sharp fluctuations in agricultural output in India over the past two decades have underscored the gaps in investment in agriculture. Gross capital formation in agriculture has undergone a sharp decline mainly on account of a steady erosion in the share of public investment. The increase in private sector capital formation has been concentrated in areas where water, power and other inputs are available uninterruptedly and with large subsidy. The inadequacy of private investment in fulfilling the capital requirements of agriculture has raised concerns about the state of the rural infrastructure which could turn into a binding constraint on growth. Irrigation coverage remains distinctly lower than the potential in terms of the gross cropped area. Insufficient village electrification has adversely affected the expansion of irrigation coverage, the growth of processing industries and cold storage facilities. The shortfall in capital formation relative to growth requirements in agriculture has also been reflected in poor road connectivity between farms and markets. Expanding investment in agriculture and in rural infrastructure would promote gains to the economy in terms of productivity, growth and poverty alleviation.

7.27 Dampening the fluctuations in output underscores the pressing need to promote the diversification of agriculture. Agricultural production has to be demand-driven with value addition. In recent years, the consumption basket is getting diversified towards value added food products such as meat, poultry, fish, vegetables and fruits. It is important for production to respond to these shifts in consumption. There is also a growing recognition that agriculture is becoming increasingly unsustainable from the point of view of environmental balance due to practices such as mono-cropping, over exploitation of natural resources, excessive irrigation and the intensive use of chemical fertilisers. The focus, therefore, needs to be on crop diversification and broad-based agricultural development that will not only cater to the changing consumption pattern and reduce imports, but also take advantage of India's global competitive strength in various agricultural products. The agro processing industry holds considerable potential in this context to emerge as the main driver of diversification of agriculture.

7.28 Efforts towards diversification must be complemented by a greater focus on recent gains from the impact of new advances in biotechnology and disease-resistance. Emerging areas like floriculture, horticulture, genetic engineering and organic farming hold high growth potential and have to be earmarked for prioritisation in investment. Furthermore, India has export potential in dairying, sericulture and horticulture which remains unexploited due to input heterogeneity and lack of marketing infrastructure.

7.29 The process of diversification calls for micro-level planning with emphasis on crop specific inputs, creating proper marketing infrastructure, cold storage, transportation facilities and supportive policies. There is a need for value addition in agricultural products through processing, packaging, and supply chain management so that farm incomes expand, employment is generated and rural poverty is alleviated. This cannot take place without directed policy actions, given the complexity inherent in diversified farming activity and the difficulties connected with the linking of farms to relevant markets. Policy action will itself have to be diversified keeping in view the needs of different agricultural and allied activities and the varied agro-climatic regions. Just as the spread of the Green Revolution was aided by a package approach across the country involving the coordinated supply of inputs, technology, seeds and extension of credit, there is clearly a need now for the creation of similar packages for diversification of agriculture in different regions. This also calls for vertical integration and public-private partnership in these activities, the modalities for which will have to be worked out. The thrust of diversification has to be on high value added products keeping in view the market demand both within and outside the country.

7.30 Efficient and well developed agricultural markets are necessary to enable farmers to deal with inherent risks associated with the perishability of their produce, to get remunerative prices and to secure smooth access to input supplies. Towards these objectives, the agricultural marketing system in the country needs to be integrated and strengthened. In this regard, speedy implementation of the Model Law on Agricultural Marketing and Contract Farming in all the States and the Union Territories would facilitate development of competitive agriculture markets in the private and the co-operative sectors and encourage contract farming.

7.31 Deceleration in the yields of many crops is an area of concern calling for research and development to evolve high-yielding and pest–resistant varieties of seeds, dry land farming and reclamation of waste lands. It is also recognised that adoption of new technology, especially new variety of seeds, entails higher risk than the use of traditional seeds. Measures to mitigate risks such as spread of irrigation facilities, better water management and adequate crop insurance must be emphasised.

Industry

7.32 The recovery of the industrial sector which began in the first quarter of 2002-03 has been steadily gaining momentum. Indian industry is engaged in a process of transformation due to competitive pressures, rapid technological progress, deregulation of product and financial markets and organisational change. Industrial restructuring has focused on niche strategies and core competencies while phasing out inefficient units. Enhanced quality consciousness through implementation of techniques like Total Quality Management (TQM) and Six Sigma have had a favourable impact on the quality of output of the manufacturing sector. Another significant development has been the changing composition of exports in favour of manufactures and technology-intensive products. There are also indications of improvement in the investment climate.

7.33 An issue of concern has been the fluctuations in industrial output in the second half of 1990s with adverse consequences for the competitiveness of manufactured products. While export demand imparts a competitive dynamism to industry, there is a need to broad-base competitiveness over a wider spectrum of products. Moreover, while strong export demand tends to support overall industrial demand, there is a need to generate domestic demand on a more enduring basis to sustain the growth momentum. In particular, concerted efforts need to be made to generate demand for those industries which are operating much below capacity levels such as ‘food products’, ‘machinery and equipment (other than transport)’, ‘transport equipment and parts’ and ‘other manufacturing industries’. In industries in which production is approaching existing potential, the focus must be on building new capacities.

7.34 India has the potential to be a major beneficiary of the phasing out of the Multi Fibre Agreement (MFA). The dismantling of MFA import quotas in 2005 offers the textile sector significant opportunities to capitalise on the expansion of overseas markets. At the same time, however, competitive pressures will intensify and continuous improvement in product quality will become an imperative to defend existing market shares. It is crucial, therefore, to develop appropriate skills and upgrade technology to fully exploit the available opportunities. Industrial growth should typically accelerate in India’s current stage of overall development. This acceleration has not taken place despite the wide-ranging industrial reforms in the 1990s. In a labour abundant country such as India, labour-intensive industries should be expected to grow faster. With the ongoing tariff reforms, some of the biases against labour-intensive industries have now been reduced. Further work needs to be done to identify policy actions that can help to induce high industrial growth that is particularly labour-intensive.

7.35 Small and medium enterprises (SMEs) occupy a unique position in the Indian economy due to their significant contribution to exports and value addition to domestic supply chains, employment generation, expansion of entrepreneurial base and diversification of the industrial sector. There is an urgent need for a comprehensive review of the policy framework for the small scale sector with a view to consolidating and carrying forward recent initiatives towards infrastructural support, technology upgradation, preferential access to credit, and preferential purchase policy. In particular, there is a need for a critical appraisal of the policy of reserving the items for production in the small scale sector. The Union Budget, 2004-05 has de-reserved 85 items for the small scale sector. While this is certainly a welcome policy change, there is a need for accelerated phasing out of the remaining reserved items. The focus should be on improving the competitive ability of SSI units through improvements in their efficiency and quality levels.

7.36 The persisting delay in execution of Central Sector Projects (CSPs) is another area which requires careful monitoring. While there has been some reduction in the cost overrun during 2003-04 as compared with the previous year, the proportion of delayed projects to total projects has increased. Many of the railway projects which are more than five years old are delayed due to inadequacy of funds and tardy progress in acquisition of land. The cost overrun of the delayed projects mainly relates to the projects in power and surface transport sectors. Issues regarding civil works, equipment supply, timely award of contract, feasibility studies and project appraisal continue to affect the speedy implementation of the CSPs. Adequate attention needs to be paid to ensure completion of projects in a time bound manner to avoid cost overruns.

Services

7.37 The services sector has emerged as the engine of growth of the Indian economy. The strength of the services sector needs to be leveraged in view of its enormous growth potential and positive externalities for the commodity producing sectors. While the rising share of services in the GDP is an encouraging sign of greater degree of diversification of the Indian economy, the corresponding decline in the shares of commodity producing sectors implies that overall productivity gains in the economy would depend increasingly on the degree of efficiency attained by the services sector.

7.38 The sustainability of high growth of services would hinge upon high quality of production and delivery, continuous improvement in productivity and pro-active supply responses in markets where tastes and patterns change rapidly. Customisation will be the hallmark of strategies for gaining market shares. The global market for the new drivers of service sector growth – Information Technology Enabled Services

(ITES) and Business Process Outsourcing (BPO) services – is becoming intensely competitive and is being compressed by protectionist pressures. Diversification of range of services offered as well as geographical markets, further innovations and ensuring customer satisfaction would remain crucial to maintaining India's competitive advantage in major international markets. Improvement in efficiency in the delivery of infrastructure services such as transportation, power, water supply and other urban services is critical to the enhancement of productivity in the commodity producing and services sectors alike. At this stage of development, construction activity holds the key for enhancing productivity and improving employment prospects across the economy. The modernisation of construction techniques would help in reducing overall costs in all infrastructure sectors and housing.

FISCAL POLICY

7.39 An important goal of fiscal consolidation through the implementation of FRBM Rules, 2004 is to eliminate the revenue deficit by 2008-09. This is sought to be achieved by raising the tax-GDP ratio through augmentation of tax receipts from sustained growth and better compliance. Moreover, emphasis needs to be on withdrawing exemptions and rationalising the tax structure so as to eliminate subjectivity in the tax system. In this context, it is also worthwhile to explore the applicability of a uniform tariff rate on imports. Given the downward rigidities characterising revenue expenditure, the attainment of the goals set out in the FRBM Rules would be contingent upon the realisation of the assumed revenue buoyancies. The Kelkar Task Force has made useful recommendations for boosting of revenues for the period 2004-05 through 2008-09 – a single goods and services tax (GST), removal of the plethora of exemptions granted to import and excise taxes, widening the net by expanding the service tax base and improving the tax compliance.

7.40 On the expenditure front, there is continued need for a review of the expenditure on subsidies and reorienting them so that the benefit accrues to the needy. It is also important to ensure that the quality of expenditure is enhanced by better targeting, elimination of waste in execution and emphasising value of output especially in delivery of services affecting the poor such as drinking water, sanitation, primary education and health. This, in turn, has wider ramifications for the productive capacity of the economy, given the paramount importance of public investment in critical areas of the Indian economy.

7.41 The emerging fiscal scenario of a number of State Governments underscores the need for concerted efforts towards achieving durable fiscal consolidation. This, in turn, entails appropriate user charges and cost recovery of social and economic services, apart from restructuring of state PSUs. The focus of adjustment, therefore, needs to be on fiscal empowerment and pro-active enactment of fiscal responsibility legislation by all the State Governments. In this regard, particular emphasis needs to be placed on strengthening the ability of the States to deliver efficiently the critical social services such as public health and primary education. The delivery of quality secondary education and medical services is also essential for further enhancement of the quality of life of all citizens.

EXTERNAL SECTOR

7.42 The growing strength of India's external sector has provided the enabling conditions to accelerate the pace of external liberalisation. This has considerably mitigated the inward-looking bias of past regimes and has brought forth a healthy response in terms of export earnings and the inflow of remittances. Liberalisation of foreign exchange transactions has to be backed up by price alignments in the form of reduction in tariff rates. The experience of most emerging markets suggests that internationally competitive tariff rates contribute towards export performance on a sustained basis.

7.43 The ongoing process of capital account liberalisation would deepen the foreign exchange market and make cross-border transactions increasingly sensitive to movements in interest rates and exchange rates. Capital account liberalisation is a process which has to be managed keeping in view the supply response of the economy and vulnerabilities or potential for shocks. Markets tend to react asymmetrically with a strong negative bias to reversals, unless there is already a crisis situation. The process of capital account liberalisation has to take into account the revealed preference for hierarchy in different types of capital flows. A key issue in managing the capital account is credibility and consistency in macroeconomic policies and the building up of safety nets to provide comfort to the markets. This also underscores the importance of prudential regulations over financial intermediaries in respect of their foreign exchange exposures and transactions, which are quite distinct from capital controls. It is the changing mix of controls that characterises the process of managing the liberalisation of the capital account. Furthermore, capital controls may be price based, including tax regimes, or may comprise administrative measures. Depending on the legal framework and governance structures, the mix between the two would vary. As liberalisation advances, the administrative measures would get reduced and price-based measures would be relied upon increasingly, but the freedom to change the mix should always be demonstrably available to assuage market sentiments in times of stress.

7.44 Outward FDI is receiving increased policy attention, not merely as a means of contending with capital inflows but also as a growing expression of competitiveness and entrepreneurial energy of Indian industry. FDI may be for resource-seeking, market-seeking, acquiring domain-knowledge or for business synergies. A greater integration with the global economy would be fostered and resilience imparted when India not only receives FDI but also promotes outward FDI.

FINANCIAL SECTOR

7.45 The Reserve Bank has been focusing on developing a competitive operating environment in the financial sector in terms of markets, institutions, products and practices. The increasing market orientation of the financial system helps in improving allocative efficiency of resources. At the same time, however, it exposes both public sector and private sector financial intermediaries to various risks, necessitating prudential regulation and supervision. The litmus test of regulatory design in a competitive environment is to strengthen financial stability while at the same time minimising the costs of financial regulation. This, in turn, implies that as the process of deregulation deepens, regulatory initiatives have to be reoriented towards more pro-active supervision of the financial system. It is in this context that the Reserve Bank's supervisory strategy has been to move away from micro-prescription oriented on-site supervision to risk-based supervision. A key element of a market-oriented risk-based supervisory strategy is to develop sound corporate governance practices, which would minimise the need for process-focussed supervision. The Reserve Bank, therefore, has been emphasising corporate governance and better risk assessment within banks and financial institutions, both public and private. The announcement in the Union Budget of a Task Force to examine the reforms required in the co-operative banking system, including the appropriate regulatory regime, is indeed welcome. The imperative of improving risk management systems must be seen as much from the angle of financial stability as from the process of economic development. Improved risk assessment systems are expected to enable banks to take greater exposures to sectors such as agriculture and small scale industries in which collateral valuations often pose difficulties. This is all the more important as the pattern of credit demand has been changing in recent years. Demand for bank credit from large corporates has been declining because of financial restructuring, improvements in productivity, optimisation of inventory cycles, better cash flow management, increased access to external commercial borrowings and improved internal generation of funds. With better risk assessment capabilities, banks should be able to shed their risk averse attitude and extend more finance to hitherto unbanked segments of agriculture, industry and services.

7.46 The critical challenge at this juncture is to improve the allocative efficiency of resources and at the same time guard against the risks of disruptive financial imbalances. The mandate of financial stability, in the Indian context, thus has to be seen in the broadest sense of the term, calling for a three-pronged strategy of ensuring uninterrupted financial transactions; maintaining a level of confidence in the financial system amongst all the participants and stakeholders; and ensuring orderly conditions in the financial markets to guard against potential adverse effects on real economic activity. The growing integration of financial markets, especially the increasing inter-linkages between domestic financial markets and the foreign exchange market, while desirable for economic efficiency, heightens the risk of contagion. As a result, special defence mechanisms need to be mounted for ensuring financial stability in the face of increasing uncertainties in the global financial scenario.

7.47 Management of the financial sector has been oriented towards gradual rebalancing between efficiency and stability and the changing shares of public and private ownership. Enhanced competition among diverse players has been encouraged. Regulation of urban co-operative banks is hampered by the system of dual control and speedy resolution of the issue is imperative to ensure the future health of the sector. Considerable improvements have taken place in prudential governance as also in moving away from administrative measures to market-orientation. Improvements in efficiency and stability are evident and there is merit in continuing with such rebalancing while refocusing on consolidation, governance and movement towards Basel II – *albeit* gradually, as in the past. Consolidation has started to encompass development finance institutions, public sector banks, private sector banks and non-bank financial companies. As the consolidation proceeds, it is necessary to design a road map so that over a period, there is a convergence between real sector reforms in India, a substantially liberalised capital account and an efficient but stable financial system, in particular the banking system, with an optimal diversity of players consistent with the growing size and complexity of the Indian economy.

7.48 The Reserve Bank favours a process of gradual convergence with international standards and best practices with suitable country-specific adaptations. This has also been the guiding principle in the approach to the New Basel Accord. Having decided, in principle, in April 2003 to adopt the Basel Accord, the Reserve Bank is overseeing a road map for migration to Basel II with reviews of the progress made at quarterly intervals. To begin with, all banks in India will adopt the Standardised Approach for credit risk and Basic Indicator Approach for operational risk. After adequate skills are developed, both in banks and at supervisory levels, some banks may be allowed to migrate to the Internal Ratings Based (IRB) Approach. The Reserve Bank is also putting in place supervisory policies to address the potential systemic risks arising due to operations of large and complex financial conglomerates.

7.49 There are, however, several areas which are likely to pose regulatory and supervisory challenges in the years ahead. First, the level of rating penetration is not yet adequate and it is restricted to issues (rather than issuers, as required by Basel II). Secondly, Basel II provides scope for the supervisor to prescribe higher than the minimum capital levels for banks for, *inter alia*, interest rate risk in the banking book and concentration of risks/ risk exposures. Thirdly, there are several issues in cross border supervision which have to be dealt with. Fourthly, although Basel II could actually imply a degree of pro-cyclicity of minimum capital requirements, there is a need to ensure that prudential norms are, in general, business cycle-neutral.

MONETARY POLICY

7.50 With the growing financial integration across borders, the conduct of monetary policy is becoming increasingly complex. It is not a coincidence that most of the uncertainties facing monetary policy at the present juncture are essentially international in character. The future evolution of international capital flows depends as much on the national fundamentals as on the stance of monetary policy followed by leading central banks in the world. The path of inflation is similarly governed not only by domestic economic activity, but also by the extent of liquidity emanating from capital flows and the movements in international commodity prices. Although the policy objectives remain rooted in the domestic macroeconomic circumstances, the process of monetary policy formulation has to factor in global macroeconomic developments, particularly, trends in world economic growth and trade, international price trends and movements in international interest rates and exchange rates.

7.51 The pursuit of price stability remains a key objective of monetary policy, especially in a country like India where a large majority of the population have no insurance against inflation. There is, thus, a need to consolidate the gains from reining in inflationary expectations especially as cross-country experiences suggest that public confidence can dissipate very quickly in the case of adverse movements in prices. An added dimension is the increasing sensitivity of domestic inflation to the movements in international commodity prices, with the opening up of the economy. The pursuit of price stability in future will call for a carefully crafted strategy in which monetary policy will not only need to address the demand side of the economy but also strike a fine balance in assessing the supply side of inflation, while enhancing prospects for growth.

7.52 Bank loans continue to be special in the Indian economy. This raises several issues in relation to credit culture, credit delivery and credit pricing. First, persistence of the large gap between lending rates and deposit rates remains a matter of concern. Policy-related barriers to reduction in the lending rate such as statutory pre-emptions and small saving interest rates have been eased considerably in recent years and asset quality has also improved. With almost all the structural rigidities having been reduced, bank-level efforts are now necessary to ensure that the benefits of low cost deposits are passed on to the customers. Secondly, there is the issue of stepping up loans to relatively disadvantaged sections of borrowers, including small and medium enterprises and the agricultural sector. To many of the borrowers in these sectors, it is, in fact, the availability of credit more than the price of credit which is of prime importance. This is especially so because interest rates in informal markets which serve as an alternative to bank finance, particularly in rural areas, are sometimes at usurious levels relative to the formal sector. The persistence of this large differential, *ipso facto*, implies that the formal credit mechanisms are not able to penetrate into the informal system. It is in this context that the recommendations of the Vyas and the Ganguly Committees assume significance. Whereas the Vyas Committee has recommended expansion of bank financing, especially direct lending, to agriculture, the focus of the Ganguly Committee has been on putting in place a strategy of lending to small scale industries in view of their potential for high growth.

7.53 To conclude, considerable progress has been made in preparing the ground for realising the full potential of the Indian economy. The drag imposed by high levels of unemployment, poverty and inequity has brought to the fore the urgency attached to actualising this potential. This is consistent with the renewed emphasis on equity in the reorientation of growth strategy that is underway. The process of structural reforms has imparted a resilience and a momentum to the economy even as the pursuit of macroeconomic and financial stability has produced gains in terms of low and stable inflation relative to several emerging economies and a vibrant and well-functioning financial system equipped with the wherewithal of intermediating the financing requirements of high and sustained growth. The regulatory and supervisory function is getting increasingly tuned to the fast changing financial environment. Issues in governance and transparency are at the forefront of this change even as efforts are being intensified to put in place the appropriate legislative framework for the smooth functioning of the financial sector.

PART TWO : THE WORKING AND OPERATIONS OF THE RESERVE BANK OF INDIA

VIII MONETARY AND CREDIT POLICY OPERATIONS

8.1 The conduct of monetary policy during 2003-04 was guided by the objective of provision of adequate liquidity to meet credit growth and support investment demand in the economy while continuing a vigil on movements in the price level. Ensuring macroeconomic stability was a concurrent objective with intensified monitoring of price movements, in view of the hardening of international commodity prices, especially crude oil, and the likely impact of the liquidity overhang in the system. Strong capital inflows posed a challenge for monetary management. The Reserve Bank responded with a policy mix of sterilisation, prepayment of external debt and liberalisation of foreign exchange transactions to maintain monetary conditions in line with the overall objectives. The need to fortify monetary management with additional instruments of sterilisation in the context of the large volume of capital inflows led to the institution of a Market Stabilisation Scheme (MSS). Interest rates on non-resident deposits were gradually aligned with those prevailing in the international markets in view of the rapid expansion in banks' external liabilities. These measures were reinforced by refinements in the Liquidity Adjustment Facility (LAF) scheme to strengthen the operating procedure of monetary policy. The Reserve Bank undertook parallel initiatives to improve the credit delivery system, especially in respect of agriculture and small and medium enterprises (SMEs).

8.2 This Section surveys the Reserve Bank's monetary and credit policy operations during 2003-04. A review of monetary policy operations sets out the dilemmas posed by the evolving monetary conditions. It also delineates the strategy adopted to balance the stance in support of growth against the need to ensure orderly conditions in financial markets and to contain potential inflationary pressures from persistent capital inflows and rising international oil and commodity prices. A review of interest rate policy profiles the measures undertaken to impart flexibility to the interest rate structure and to enhance transparency in the pricing of bank loans. The Section also presents the policy initiatives undertaken by the Reserve Bank during the year to strengthen the credit delivery system.

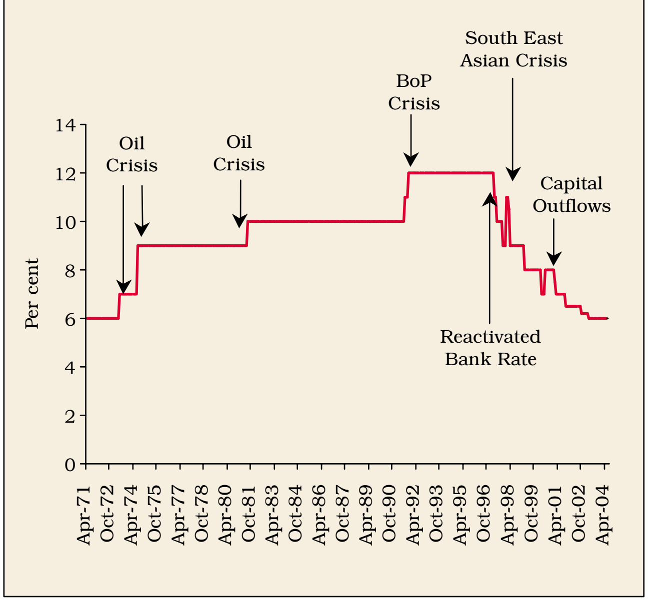
MONETARY POLICY OPERATIONS

Monetary Measures

Bank Rate

8.3 The Bank Rate was reduced by 25 basis points (bps) to 6.0 per cent effective April 30, 2003 – the lowest level since May 1973 (Chart VIII.1).

Chart VIII.1 : Bank Rate



Repo Rate

8.4 The repo/reverse repo rates in the auctions under the LAF signal the Reserve Bank's monetary policy stance. The Reserve Bank reduced the repo rate by 50 bps to 4.5 per cent effective August 25, 2003 (Table 8.1).

Table 8.1: Movement in LAF Rates

(Per cent)

Month	2003-04		2002-03		2001-02		2000-01	
	Repo	Reverse Repo	Repo	Reverse Repo	Repo	Reverse Repo	Repo	Reverse Repo
1	2	3	4	5	6	7	8	9
April	5.0	7.0	6.0	–	6.75-7.0	8.75-9.00		
May	5.0	7.0	6.0	8.0	6.5-6.75	8.75		
June	5.0	–	5.75 (June 27)	–	6.5	8.5	–	9.0-14.0
July	5.0	7.0	5.75	–	6.5	8.5	7.0-8.0	9.0-10.0
August	4.5 (August 25)	–	5.75	–	6.5	–	8.0-15.0	15.0-16.0
September	4.5	–	5.75	–	6.5	8.5	10.0-13.0	13.5
October	4.5	–	5.50 (Oct. 30)	–	6.5	8.5	8.0-9.75	10.25
November	4.5	–	5.50	7.5 (Nov. 12)	6.5	8.5	8.0	10.0
December	4.5	–	5.50	–	6.5	8.5	8.0	10.0
January	4.5	–	5.50	7.5	6.5	–	–	10.0
February	4.5	–	5.50	7.5	6.5	8.5	7.5-8.0	10.0
March	4.5	6.0 (March 29)	5.0 (March 3)	7.0	6.0 (March 5)	8.0	7.0-7.5	9.0

– : No repo/reverse repos.

8.5 The scope of the LAF was progressively enlarged to price primary liquidity at the reverse repo rate. Effective the fortnight beginning December 27, 2003 the ratio of the "normal" standing facility available at the Bank Rate and the "back-stop" standing facility linked to the reverse repo rate was modified to one-third and two-third (*i.e.*, ratio of 1:2) from one-half each (*i.e.*, ratio of 1:1). The entire quantum of export credit refinance and the liquidity support available for primary dealers was made available at a single rate, *i.e.*, the reverse repo rate, effective March 29, 2004.

8.6 Cross-country experience suggests that central banks influence short-term interest rates by directly fixing the interest rate on central bank accommodation and indirectly by open market operations (OMO) which, in turn, affect the price of primary liquidity. The Reserve Bank has adopted a balanced and flexible stance in this regard in recent years in response to the evolving situation. Fixed repo rate auctions, introduced in November 1997, were replaced in June 2000 with auctions under the LAF, in which interest rates emerged from the market bids. In effect, however, the LAF turned out to be a *de facto* fixed rate auction as market participants did not usually bid at a price different from the prevailing repo rate. In order to provide a clearer signal to the market, fixed rate repo auctions were reintroduced in March 2004. Also, the maturity period of repos was increased to 7 days, while for reverse repos it was retained on overnight basis. Furthermore, the spread between the repo rate and the reverse repo rate was reduced by 50 bps to 150 bps with effect from March 29, 2004. At the time of introduction of the revised LAF scheme, it was indicated that the Reserve Bank will continue to have the discretion to conduct overnight or longer-term repo auctions at fixed or variable rates depending on market conditions and other relevant factors. Accordingly, on an assessment of the prevailing situation, the Reserve Bank decided to reintroduce overnight fixed rate repos at 4.5 per cent under the LAF from August 16, 2004 while continuing with 7-day and 14-day repos and overnight fixed rate reverse repos.

Cash Reserve Ratio

8.7 The Reserve Bank continued to pursue its medium-term objective of reducing the cash reserve ratio (CRR) to the statutory minimum level of 3.0 per cent of banks' net demand and time liabilities (NDTL). In line with this policy stance, there was a cut in the CRR by 25 bps on June 14, 2003 (Table 8.2).

Table 8.2: Cash Reserve Ratio

(Amount in Rupees crore)

Month	2003-04		2002-03		2001-02		2000-01	
	CRR (Per cent)	Amount*	CRR (Per cent)	Amount*	CRR (Per cent)	Amount*	CRR (Per cent)	Amount*
1	2	3	4	5	6	7	8	9
April	4.75	0	5.5	0	8.0	0	8.0	7,200
May	4.75	0	5.5	0	7.5	4,500	8.0	0
June	4.5	3,500	5.0	6,500	7.5	0	8.0	0
July	4.5	0	5.0	0	7.5	0	8.25	-1,900
August	4.5	0	5.0	0	7.5	0	8.5	-1,900
September	4.5	0	5.0	0	7.5	0	8.5	0
October	4.5	0	5.0	0	7.5	0	8.5	0
November	4.5	0	4.75	3,500	5.75	6,000	8.5	0
December	4.5	0	4.75	0	5.5	2,000	8.5	0
January	4.5	0	4.75	0	5.5	0	8.5	0
February	4.5	0	4.75	0	5.5	0	8.25	2,050
March	4.5	0	4.75	0	5.5	0	8.0	2,050

* : Amount stands for first round release (+)/ impounding (-) of resources through changes in the cash reserve ratio.

Eligible CRR balances maintained by banks with the Reserve Bank are paid interest on a monthly basis starting from April 2003.

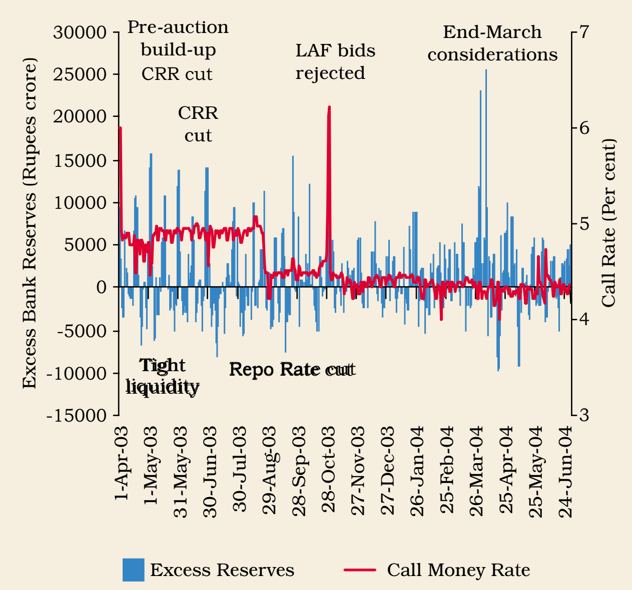
Liquidity Management

8.8 The Reserve Bank continued to modulate market liquidity through a mix of repo operations under the LAF and outright OMO. Barring fluctuations relating to primary auctions and the usual year-end switch to balances with the Reserve Bank, daily fluctuations in banks' excess reserves (defined as the excess balances over and above the CRR stipulation) with the Reserve Bank remained range-bound for the greater part of 2003-04 (Chart VIII.2). This imparted stability to the interest rate environment during the year.

8.9 During 2003-04, the Reserve Bank stepped up sterilisation operations through outright open market sales and LAF repo operations. As capital flows persisted, the Reserve Bank's stock of Government securities for OMO and the LAF was augmented by i) conversions of the available stock of non-marketable special securities into marketable paper; and ii) private placements of Government paper against the release of foreign exchange for the prepayment of the Government's external debt. Persistent and sizeable cash balances of the Government with the Reserve Bank in the second half of the year were invested in gilts, preventing their use in OMO. The reduction of Government paper in the Reserve Bank's portfolio necessitated a switch from outright OMO to repo operations thereby burdening the instrument of day-to-day liquidity management with the absorption of liquidity of an enduring nature.

8.10 The scope of sterilisation operations is circumscribed by the Reserve Bank of India Act, 1934 for three reasons. First, the Reserve Bank is not allowed to borrow beyond its paid-up capital of Rs.5 crore without collateral. This requires Government securities to be furnished as underlying collateral in repo operations under the LAF. Second, since the Government cannot statutorily receive interest on surplus balances with the Reserve Bank under the Act, it typically 'buys back' Government paper from the Reserve Bank and saves

Chart VIII.2 : Excess Bank Reserves and Call Rate



on interest payments. Third, the Reserve Bank cannot issue its own paper under the extant provisions of the Act. The stock of marketable Government paper with the Reserve Bank being finite can, thus, affect the extent of its monetary policy operations.

8.11 In this context, the Reserve Bank appointed two groups, *viz*., a Working Group on Instruments of Sterilisation and an Internal Group on Liquidity Adjustment Facility to search for alternative instruments of sterilisation (Box VIII.1). On the basis of the recommendations of the Working Group on the Instruments of Sterilisation, the MSS was instituted in April 2004 (refer to Box I.2 of Section I). In terms of the scheme, the Government issues securities to mop up the excess liquidity emanating from the Reserve Bank's operations in the foreign exchange market and parks the proceeds in an identifiable cash account, *viz*., the MSS account to be maintained and operated by the Reserve Bank. As a result, the primary liquidity generated by the accretion to the Reserve Bank's foreign currency assets is counter-balanced by a reduction in the Reserve Bank's net credit to the Centre.

8.12 The course of management of capital flows reflected the constraints within which the Reserve Bank had to operate. In this regard, sterilisation operations during 2003-04 and the first quarter of 2004-05 could be divided into three distinct phases in terms of the relative shifts in reliance on instruments used (Table 8.3).

Box VIII.1
Instruments of Sterilisation

The Reserve Bank's Working Group on the Instruments of Sterilisation (Chairperson: Smt. Usha Thorat) examined options that would augment the Reserve Bank's ability to sterilise capital inflows. Against the background of international experience and the existing financial and legal structure, the Working Group recommended a two-pronged approach for strengthening and refining the existing instruments and exploring new instruments appropriate in the Indian context to sterilise foreign exchange inflows. The appropriate mix of instruments would depend on the prevailing circumstances, the associated costs and benefits and the opportunity cost of not using sterilisation as a policy option. The major recommendations of the Group include:

Existing instruments

- The use of open market operations as an instrument of sterilisation.
- As outright transactions entail the permanent absorption of liquidity and transfer of market risk to participants, the alternative of using the existing stock of securities for longer-term repos (up to 3 to 6 months) could also be considered.
- It is not desirable to use the LAF as an instrument of sterilisation on an enduring basis, although it could supplement other instruments for limited periods.
- Surplus balances of the Government could be maintained with the Reserve Bank without any payment of interest. This would entail a review of the 1997 agreement between the Government and the Reserve Bank under which the Reserve Bank transfers securities to the Government account in *lieu* of interest payments.
- The use of CRR as an instrument of sterilisation should not be ruled out under extreme conditions of excess liquidity and when other options are exhausted.

New instruments requiring amendments to the Reserve Bank of India Act

- The Group favoured the institution of a standing deposit-type facility with flexibility in determination/remuneration of CRR balances so that interest can be paid on deposit balances actually maintained by scheduled banks with the Reserve Bank.
- Although many emerging market economies issue central bank paper to absorb liquidity, the Group did not find it desirable to pursue the option of such issuance. Central bank bills tend to concentrate the entire cost of sterilisation in the central bank's balance sheet. Cross-country experience suggests that the resultant financial impairment often erodes the ability of the monetary authority to conduct liquidity operations. Besides, the existence of two sets of risk-free paper - gilts and central bank bills - tends to fragment the market.

New instruments which do not require legislative amendments

- The Group recommended the institution of a Market Stabilisation Scheme (MSS). Proceeds of Government paper issued under the MSS to mop up liquidity generated on account of the accretion to the Reserve Bank's foreign assets would be parked with the Reserve Bank to neutralise the monetary impact of capital flows. Based on this recommendation, a Memorandum of Understanding was signed between the Government and the Reserve Bank on March 25, 2004 providing for the issuance of Treasury Bills and dated securities within an overall ceiling of Rs.60,000 crore, subject to review, if necessary.

Reference

Reserve Bank of India (2004), "Report of the Working Group on Instruments of Sterilisation", *Reserve Bank of India Bulletin,* April.

Table 8.3: Phases of Reserve Bank's Liquidity Management Operations

(Rs. crore)

Item	April 1-December 26, 2003	December 27, 2003-March 26, 2004	March 27-June 25, 2004
1	2	3	4
1. RBI's Foreign Currency Assets (adjusted for revaluation)	93,334	46,171	34,971
2. Repos (net) (under LAF)	27,075	31,910	-35
3. OMO sales (net)	36,517	5,332	429
4. MSS	–	–	37,812
5. Currency	29,914	14,896	14,042
6. Others (residual)	8,106	-15,601	-17,274
6.1 Surplus cash balances of the Centre with the Reserve Bank	13,135	-6,685	-18,577
Bank Reserves # (1-2-3-4-5-6)	**-8,278**	**9,634**	**-3**

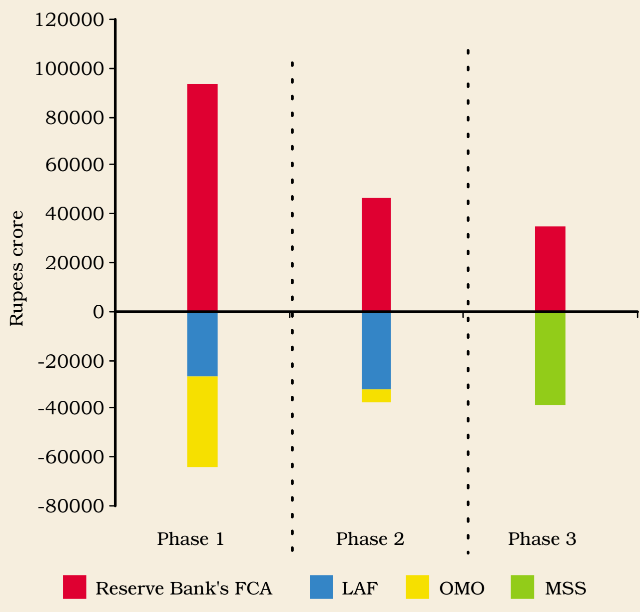
: Excludes vault cash with banks.

8.13 During the first phase, *i.e.,* April-December 2003, the Reserve Bank continued to absorb the liquidity emanating from capital inflows by deploying an almost even mix of open market outright sales (amounting to 39.1 per cent of the accretion of the Reserve Bank's foreign assets) and the LAF (29.0 per cent). In the second phase, *i.e.*, January-March 2004, the burden of sterilisation fell on the LAF, which offset almost 70 per cent of the accretion to the Reserve Bank's foreign currency assets. In the third phase, *i.e.*, during the first quarter of 2004-05, the MSS emerged as the primary mechanism of liquidity management (Chart VIII.3). Adding the balances parked in repos under the LAF and the paper issued under the MSS, the total liquidity overhang in the system exceeded Rs.1,00,000 crore or 5.0 per cent of broad money by end-June 2004.

Liquidity Adjustment Facility

8.14 The LAF is the Reserve Bank's primary instrument for modulating liquidity and transmitting interest rate signals to the market. Besides the usual function of day-to-day liquidity management, the LAF was increasingly used as an instrument of sterilisation during 2003-04. As a result, the average daily repos outstanding were consistently higher than those in 2002-03. Although the Reserve Bank adjusted the quantum of primary liquidity in the first half of the year by occasionally rejecting bids, all bids were, by and large, accepted in the second half of the year as the pressure from persistent capital inflows intensified (Table 8.4).

Chart VIII.3 : Sterilisation of Capital Flows



8.15 LAF repo operations were conducted to mop up the usual spurt in liquidity at the beginning of the year. Bids ebbed in May and June as the Centre's market borrowing programme gathered momentum. Repo bids soared – both in number and average size – in July with the easing of liquidity conditions, reinforced by the return flow of advance tax payments and the seasonal easing in cash demand. A 50 bps cut in the repo rate in August 2003 briefly closed the differential with the call rate and caused a temporary lull in repo biddings. A mix of open market sales and a series of 28-day repos to rationalise expectations were reflected in some reduction in LAF repos in October. Repo bids picked up again from November with the persistence of capital inflows as well as the gradual cessation of outright OMO. Accordingly, LAF repo operations had to not only provide an anchor to call rates but also act as the main sterilisation instrument. This pushed up the average daily repo outstanding to Rs.54,915 crore in March 2004, despite an outflow of over Rs.25,000 crore during March 26-31, 2004 on account of the build-up of bank reserves and transfer of the proceeds of ONGC disinvestment to the Government's account with the Reserve Bank (Chart VIII.4).

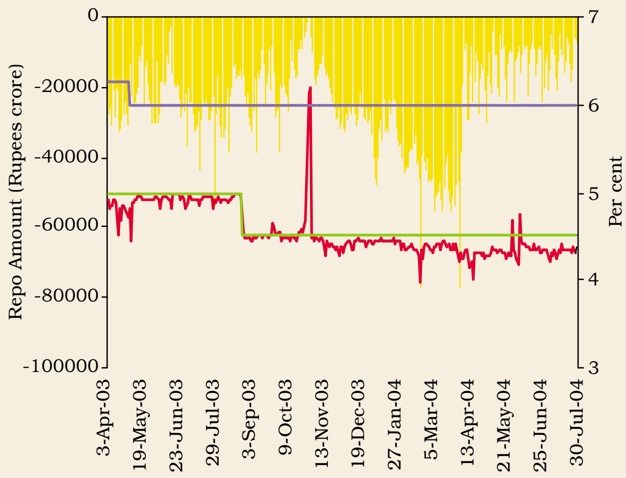
8.16 The pressure on the LAF began to build up in April 2004 due to strong capital inflows as well as

Table 8.4: Repo/Reverse Repo Bids under LAF

Month	Repo				Reverse Repo			
	No. of days bids were received	No. of days all bids were rejected	No. of days of full acceptance of bids	No. of days of partial acceptance of bids	No. of days bids were received	No. of days all bids were rejected	No. of days of full acceptance of bids	No. of days of partial acceptance of bids
1	2	3	4	5	6	7	8	9
2003-04								
April	17	0	15	2	1	0	1	0
May	19	0	18	1	1	0	1	0
June	20	0	18	2	0	0	0	0
July	23	0	22	1	1	0	1	0
August	20	0	19	1	0	0	0	0
September	21	0	19	2	0	0	0	0
October	22	2	19	1	1	1	0	0
November	19	0	19	0	0	0	0	0
December	22	0	22	0	0	0	0	0
January	21	0	21	0	1	1	0	0
February	18	0	17	1	0	0	0	0
March	21	0	21	0	1	0	1	0
2004-05								
April	19	0	19	0	0	0	0	0
May	20	0	20	0	0	0	0	0
June	21	0	21	0	1	0	1	0
July	23	0	23	0	0	0	0	0

the usual seasonal easing in credit demand. As a result, outstanding LAF repos jumped to an average of over Rs. 74,000 crore during April and May 2004. The pressure on the LAF window started abating by June due to a combination of factors such as seasonal currency demand, the beginning of the Government's borrowing programme, slowdown in capital inflows and the switch to the MSS.

Chart VIII.4 : Repo Auctions under LAF and Call Rate



8.17 The Reserve Bank introduced a revised LAF scheme on March 29, 2004 based on the recommendations of the Internal Group on LAF (Box VIII.2). Daily repo/reverse repo variable rate auctions were replaced by 7-day fixed rate repo auctions and daily fixed rate reverse repo auctions, with a spread of 150 bps. The 14-day variable rate multiple price repo auctions, however, would continue for some time, but would be phased out in due course.

Open Market Operations

8.18 The Reserve Bank continued to supplement LAF absorptions with outright open market sales. The Reserve Bank is required to have a sufficient stock of Government paper to modulate liquidity through OMO. The ratio of open market sales by the Reserve Bank to the addition to the gilt portfolio dropped to about 50 per cent during 2003-04 from an average of 90 per cent in the preceding five years following a switch to LAF operations (Table 8.5).

8.19 The Reserve Bank conducted five rounds of open market operations during 2003-04. OMO sales in May mopped up the surge in domestic liquidity emanating from capital inflows in the preceding two months. These operations resumed in August and early September after the Reserve Bank replenished its stock of marketable paper by converting non-

Box VIII.2
Internal Group on Liquidity Adjustment Facility

The Reserve Bank's Internal Group on Liquidity Adjustment Facility made a number of recommendations to enhance the efficacy of liquidity management.

- Daily LAF auctions could be replaced by weekly auctions conducted on a daily basis to enable balanced development of various segments of the money market with the flexibility to conduct overnight repo auctions if the situation so warrants.
- Fixed rate LAF auctions could replace variable rate auctions to enhance the ability of the Reserve Bank to transmit policy signals, *albeit* with the flexibility to use the variable price auction format, if necessary.
- The ambit of LAF operations could be enlarged by linking the entire liquidity support, including refinance, to the reverse repo rate.
- The timing of LAF auctions could be shifted to the middle of the day from 10.30 am to enable sufficient inter-play of market liquidity, especially with the provision of intra-day liquidity with the operationalisation of the real time gross settlement (RTGS) system.
- The LAF should primarily modulate liquidity of a somewhat "temporary" nature at the margin on a day-to-day basis.
- A standing deposit facility should be instituted with due amendments in the Reserve Bank of India Act, 1934 to accord the Reserve Bank greater flexibility in LAF operations as also to provide a floor to the interest rate corridor.
- Pending legislative amendments, the possibility of modifying the current CRR prescription to accommodate a standing deposit-type facility with placement of deposits at the discretion of banks could be explored; remuneration on the standing deposit-type facility would be below the repo rate.
- The Bank Rate should be aligned to the reverse repo rate under normal circumstances. In the event of introduction of a standing deposit facility, the interest rate corridor in the money market would be defined by the Bank Rate/reverse repo rate as the ceiling and the standing deposit facility rate as the floor.

Reference

Reserve Bank of India (2004), "Report of the Internal Group on Liquidity Adjustment Facility", *Reserve Bank of India Bulletin,* January.

marketable special securities in its portfolio into tradable paper. A fourth round took place in October, funded by drawals from repo operations following the conversion of the available stock of special securities in September. A final round of OMO sales took place in January 2004 to supplement the LAF operations in sterilising the large accretion to the Reserve Bank's NFA (Table 8.6).

Table 8.5: Reserve Bank's Holdings of Central Government Dated Securities

(Rupees crore)

Year	Devolvement on Reserve Bank	Private Placement taken by Reserve Bank	OMO Purchases by Reserve Bank	Conversion of Special Securities into Dated Securities	Total addition to stock of Reserve Bank 's Investments (2+3+4+5)	OMO Sales by Reserve Bank	Net Addition to Stock (6-7)	Outstanding Holding by Reserve Bank (end period)*	*Memo :* Net Repos Outstanding
1	2	3	4	5	6	7	8	9	10
1996-97	3,698	–	623	–	4,321	11,206	-6,885	6,666	2,300
1997-98	7,028	6,000	467	20,000	33,495	8,081	25,414	31,977	4,202
1998-99	8,205	30,000	–	–	38,205	26,348	11,857	42,212	400
1999-00	–	27,000	1,244	–	28,244	36,614	-8,370	35,190	–
2000-01	13,151	18,000	4,471	–	35,622	23,795	11,827	41,732	1,355
2001-02	6 79	28,213	5,084	–	33,976	35,419	-1,443	41,631	4,355
2002-03	5,175	31,000	–	40,000	76,175	53,780	22,395	63,866	2,415
2003-04	–	21,500	–	61,818	83,318	41,849	41,469	1,04,066	34,795
2004-05 (up to August 14)	217	–	–	–	217	716	-499	1,03,975	32,665

* : Inclusive of securities sold under the LAF and the investment of the Centre's surplus.

Table 8.6: Monthly Primary Liquidity Flows and Open Market Operations

(Rupees crore)

Month	RBI's Foreign Currency Assets#			Net RBI Credit to Centre			RBI's Initial Subscription			Net OMO Sales		
	2004-05	2003-04	2002-03	2004-05	2003-04	2002-03	2004-05	2003-04	2002-03	2004-05	2003-04	2002-03
1	2	3	4	5	6	7	8	9	10	11	12	13
April	32,608	3,817	3,076	-29,230	9,706	11,976	0	0	10,000	253	7	5,307
May	202	15,626	1,330	-7,038	-2,926	1,838	0	5,000	10,018	116	5,569	1,524
June	350	4,500	3,739	6,240	-6,346	-12,359	0	0	2,000	60	44	189
July	946	13,865	8,820	-8,530	-19,847	8,122	0	0	1,157	218	57	6,538
August		11,550	7,828		-24,023	-19,083		0	0		11,526	7,025
September		6,417	6,233		-9,874	-8,594		0	0		5,089	6,355
October		13,124	7,949		6,494	-8,074		0	0		14,024	71
November		10,775	11,887		-8,172	-1,192		0	0		69	11,073
December		13,661	11,223		-14,166	-8,616		0	0		132	4,549
January		11,723	9,375		4,420	-3,288		9,500	0		5,178	10,995
February		14,610	11,062		-17,738	-6,206		7,000	0		85	88
March		21,760	-434		6,407	17,077		0	13,000		69	66

: Adjusted for revaluation.
Note : Data based on March 31 for March and last reporting Friday for all other months.

Market Stabilisation Scheme

8.20 The Market Stabilisation Scheme (MSS), operationalised in April 2004, has emerged as a key instrument of liquidity management. The issuance under the MSS in April 2004 amounted to Rs. 23,000 crore reflecting the bunching of capital flows. An unscheduled auction amounting to Rs. 5,000 crore of dated securities under the MSS was held on April 8, 2004 to counter-balance the large accretion to the Reserve Bank's foreign currency assets (Rs.16,746 crore during April 1-9, 2004). The total stock of Treasury Bills and dated securities issued under the MSS amounted to Rs.39,730 crore by end-June 2004, in excess of the indicative allocation of Rs.35,500 crore for the quarter April-June 2004. With the abatement of capital inflows in May-June, funds invested in the MSS (Rs. 16,730 crore) essentially reflected a drawdown of the surplus parked in the LAF (Rs. 15,000 crore).

8.21 A schedule for issuances amounting to Rs.36,500 crore (including the rolling over of Rs.19,500 crore under 91-day Treasury Bills issued during the first quarter) for the second quarter ending September 2004 was issued on June 29, 2004. The total amount raised under the MSS amounted to Rs. 46,480 crore by August 14, 2004, inclusive of Rs.20,000 crore raised through dated securities with a residual maturity of up to 2.5 years.

Interest Rate Policy

Lending Rates

8.22 The Reserve Bank continued to take policy initiatives to impart a greater degree of flexibility to the interest rate structure. In order to enhance transparency in pricing of loan products by banks, the April 2003 Monetary and Credit Policy Statement advised banks to announce their benchmark prime lending rates (BPLRs), taking into account the actual cost of funds, operating expenses and a minimum margin to cover the regulatory requirement of provisioning/capital charge and a profit margin. Following a series of meetings with banks for expeditious implementation, the BPLR guidelines were modified into an operationally flexible framework. The November 2003 Mid-Term Review of Monetary and Credit Policy clarified that banks have the freedom to price their loan products based on time-varying term premia and relevant transaction costs using market benchmarks in a transparent manner. On November 25, 2003 the Indian Banks' Association (IBA) advised its member banks to announce BPLRs. By April 2004, almost all commercial banks had adopted the new system of BPLR.

8.23 Banks were permitted to determine rates of interest on loans and advances for purchase of consumer durables to individuals against shares and debentures/bonds and other non-priority sector personal loans without reference to prime lending rates (PLR) and regardless of the size of the loan.

Interest Rates on Export Credit

8.24 The reductions in the interest rate ceiling on pre-shipment rupee export credit up to 180 days and post-shipment credit up to 90 days to PLR *minus* 250 bps on September 24, 2001 were extended up to April 30, 2005. Interest rates on foreign currency export credit are linked to a ceiling related to the London Inter-Bank Offered Rate (LIBOR)/SWAP rates (*i.e.*, at LIBOR *plus* 75 bps). Banks are permitted to arrange lines of credit from overseas banks/financial institutions to augment foreign currency funds for onlending to exporters. Such borrowings by authorised dealers for financing export credit are kept outside the stipulated limit on their overseas foreign currency borrowings.

Interest Rates on Non-resident Deposits

8.25 With a view to providing consistency in interest rates offered on non-resident deposits, an interest rate ceiling linked to the LIBOR/SWAP rates was imposed on NRE deposits in stages during 2003-04. The ceiling on interest rate on fresh (and renewals of) term deposits for one to three years under the NRE scheme was placed at 250 bps above the LIBOR/SWAP rates for the US dollar of corresponding maturity, effective July 17, 2003. The differential was further reduced to 100 bps, effective September 15, 2003 and by 25 bps effective October 18, 2003 and was finally closed, effective April 17, 2004 in pursuance of the recommendations of the Internal Group on External Liabilities of Scheduled Commercial Banks (Box VIII.3). Furthermore, the NRE savings deposit rate was capped at a maximum of LIBOR/SWAP rates for six months' maturity on US dollar deposits effective April 17, 2004. No *lien* of any type, direct or indirect, is permitted against these deposits. The Foreign Currency Non-Resident (Banks) {FCNR(B)} deposit rate continues to be linked to LIBOR/SWAP rates (at LIBOR/SWAP rates of corresponding maturities *minus* 25 bps). The Union Budget for 2004-05 proposed the withdrawal of exemptions on interest income from NRI deposits, effective September 1, 2004.

Rationalisation of Interest Rates on Small Savings

8.26 The rationalisation of small saving schemes and the interest rates paid thereon remains an important policy priority in view of the high fiscal cost and in terms of the implications for the interest rate structure. In this context, the Union Government constituted an Advisory Committee to Advise on the Administered Interest Rates and Rationalisation of Saving Instruments (Chairman: Dr. Rakesh Mohan) on January 24, 2004. Recommendations of the Committee in respect of introduction of a Senior Citizens Savings Scheme and discontinuation of the Deposit Scheme for Retiring Employees and 6.5 per cent Saving Bonds 2003 (non-taxable) have been implemented with some modifications (Box VIII.4).

CREDIT DELIVERY

8.27 The Reserve Bank assigns the highest priority to nurturing a conducive credit culture among financial intermediaries, corporates and households. Credit delivery, in particular, to agriculture, SMEs and infrastructure is critical to sustain growth. In these sectors, the issue of availability of credit is often as

Box VIII.3
Internal Group on External Liabilities of Scheduled Commercial Banks

The Internal Group on External Liabilities of Scheduled Commercial Banks recommended that the current reserve and liquidity requirements on non-resident Indian (NRI) deposits may be left unaltered, as they are aligned to domestic deposits. Interest income from NRI deposits may be made taxable on the lines of domestic deposits, consistent with current account convertibility. The acceptance of NRI deposits should be restricted to authorised dealers only. Acceptance of NRI deposits by non-banking financial companies and non-financial corporates could be phased out.

The Group recommended an alignment of the pricing of non-resident external (NRE) deposits with rates of return in the international market. The NRE savings deposit rate could be delinked from the domestic savings deposit rate, with a ceiling of one-month LIBOR/SWAP rates on US dollar deposits. Furthermore, the Group recommended that the premium available on interest rates on NRE term deposits could be withdrawn to restrict the ceiling to the LIBOR of the corresponding maturity. The Resident Foreign Currency (RFC) deposit scheme could be made non-interest bearing as is the case with the Exchange Earners' Foreign Currency (EEFC) and RFC(D) accounts. Although the existing Non-Resident Ordinary (NRO) term/recurring deposits may be allowed to be maintained till maturity, fresh NRO deposits may have the nature of current/savings accounts only. For better availability of export credit in foreign currency, the ceiling on interest on such credit should be deregulated. If complete deregulation was not considered feasible, the interest rate ceiling should be raised by 50 basis points to LIBOR *plus* 125 basis points.

Reference

Reserve Bank of India (2004), "Report of the Internal Group on External Liabilities of Scheduled Commercial Banks", *Reserve Bank of India Bulletin,* July.

Box VIII.4
Advisory Committee to Advise on the Administered Interest Rates and Rationalisation of Saving Instruments

The Advisory Committee to Advise on the Administered Interest Rates and Rationalisation of Saving Instruments (Chairman: Dr. Rakesh Mohan), which submitted its report in May 2004, addressed three broad issues within its overall terms of reference, *viz.*, (i) suggesting appropriate benchmarking and spread rules for administered interest rate, (ii) rationalising existing saving schemes particularly in respect of tax treatment in the light of the recommendations made by the Expert Committee to Review the System of Administered Interest Rates and Other Related Issues (Chairman: Dr. Y. V. Reddy) in 2001, and (iii) designing a structure of the proposed *Dada-Dadi* (Senior Citizens) Scheme as announced by the Finance Minister on January 9, 2004.

After considering alternative benchmarks like the inflation rate, bank deposit rate, Bank Rate, and yields on Government securities, the Committee decided to continue with Government securities (G-sec) yields as the most suitable benchmark in line with the suggestion made by the Reddy Committee as they are mostly market determined, signal a measure of expected (rather than past) inflation and would facilitate rationalisation of interest rates on various schemes. However, in order to impart stability to the benchmark, the Committee recommended that the benchmark could be calculated on a weighted average basis, with weights of 0.67 to G-sec yields for the previous year and 0.33 to yields for the year before that. Furthermore, a fixed illiquidity premium of 50 basis points over the average benchmark yields was also retained on similar lines as suggested by the Reddy Committee. The Committee expressed concern over the sharply falling yields over the past few years due to excess liquidity in the financial market and suggested an inter-year movement of interest rate fluctuations within a band of 100 basis points to address the immediate concern of savers.

The Committee was in favour of continuing most of the small saving schemes as these are popular in rural and semi-urban areas due to convenience, habitual preference and ease of transactions as well as more intensive penetration of post offices as compared with the branch network of commercial banks. However, in the interest of rationalising existing saving schemes, the Committee recommended discontinuance of a few saving instruments offered by the Government where investments are primarily motivated by tax benefits available under Section 88 and Section 10 of the Income Tax Act. Accordingly, it recommended discontinuance of National Savings Certificates (VIII Issue), Deposit Scheme for Retiring Employees and 6.5 per cent GoI (Tax Free) Savings Bond (2003). The Committee also recommended the discontinuance of the *Kisan Vikas Patra* in which tax is not deducted at source and therefore, could lead to potential difficulties from the viewpoint of tax management. In this respect, the Committee also emphasised the need to explore ways and means of making tax deductible at source (TDS) provisions effectively applicable to taxable bonds. The Committee, however, observed that the Public Provident Fund (PPF), which also enjoys similar tax benefits, could be retained in its present form for sometime as it provides income security, especially in the unorganised sector. Similarly, other post office schemes catering to the needs of small savers, particularly in rural and semi-urban areas, were recommended to continue in their present form.

The Committee recommended a structure for the *Dada-Dadi* Scheme designed to improve the welfare of senior citizens. The interest rate on the Scheme could be 100 basis points higher than the average benchmark for other small saving instruments. The tenor could be shorter at three years to ensure liquidity. The Scheme would be taxable in terms of Section 80L of the Income Tax Act so that senior citizens at the lower end of the tax bracket, *ipso facto*, obtain higher returns. An individual ceiling of Rs. 20 lakh was proposed on investment.

Reference

Government of India (2004), “Report of the Advisory Committee to Advise on the Administered Interest Rates and Rationalisation of Savings Instruments”, *Reserve Bank of India Bulletin,* August.

important as the cost of credit, especially as the rates of interest on alternative sources of finance from the informal sector are prohibitively high. It is in this context that the Reserve Bank continued to pursue initiatives to ensure flow of adequate bank credit at reasonable rates of interest.

8.28 The monetary and credit policy has taken several initiatives to improve the credit delivery mechanism and credit flows to different sectors. Pursuant to the announcements in the November 2003 Mid-Term Review of the Monetary and Credit Policy, the Reserve Bank constituted an Advisory Committee on Flow of Credit to Agriculture and Related Activities from the Banking System (Chairman: Prof. V.S. Vyas) and a Working Group on Flow of Credit to SSI Sector (Chairman: Dr. A.S. Ganguly) to recommend measures to improve the credit delivery mechanisms for agriculture and SMEs, respectively.

8.29 A package of measures including withdrawal of limits on unsecured exposures of banks and improvement in the credit information system available with the Credit Information Bureau (India) Limited (CIBIL) was introduced to complement the process of refinements in the credit delivery mechanism from the supply side. Banks were encouraged to align the pricing of credit with the assessment of credit risk in order to improve credit delivery and pass on the benefit of lower rates to borrowers with good track records.

Priority Sector Lending

8.30 Several measures were taken to improve the credit delivery mechanism in the priority sector through raising of loan limits and expanding the definition of the priority sector. Investment limits in plant and machinery for 13 items of the stationery sector and 10 items of the drugs and pharmaceuticals sector in addition to hosiery and hand tools (which figure in the list of items reserved for manufacture in the small scale industries sector) were enhanced from Rs. one crore to Rs. five crore for the purpose of classification under priority sector advances. Furthermore, the limit for uncollateralised loans to SSI units with good financial positions and track record was increased from Rs.15 lakh to Rs.25 lakh (with the approval of the appropriate authority in the banks). All new loans granted by banks to non-banking financial companies (NBFCs) for the purpose of on-lending to the SSI sector were reckoned as priority sector loans. Banks are allowed to extend direct finance to the housing sector up to Rs.10 lakh in rural and semi-urban areas as a part of priority sector lending. Moreover, educational loans up to the ceiling of Rs.7.5 lakh for studies in India and Rs.15 lakh for studies abroad were treated as priority sector advances. As indicated in the Union Budget, 2004-05 commercial banks have agreed to waive the need for collateral for educational loans up to Rs. 7.5 lakh in place of Rs. four lakh earlier, subject to satisfactory guarantee on behalf of the student. A Gold Card Scheme was introduced for easy availability of export credit on the best terms to creditworthy exporters with good track record to step up export credit offtake.

8.31 Foreign banks are required to make good the shortfall in priority sector targets and sub-targets by depositing an equivalent amount with the Small Industries Development Bank of India (SIDBI) for a period of one year. The interest rate on deposits of foreign banks placed with the SIDBI was reduced to the Bank Rate, *i.e.*, 6.0 per cent from 6.75 per cent, with effect from November 3, 2003.

8.32 Commercial banks achieved the overall target for priority sector lending (Table 8.7). This was facilitated by (i) higher lending by banks to individuals directly for housing and indirectly for investment in bonds issued by the National Housing Bank (NHB)/ Housing and Urban Development Corporation (HUDCO) for housing (*i.e.*, indirect lending); (ii) retail trade by public sector banks; and (iii) lending to direct housing in the case of private sector banks. Nine private sector banks and two public sector banks did not achieve the overall priority sector lending target of 40 per cent as on the last reporting Friday of March 2004.

Table 8.7: Priority Sector Advances

(Rupees crore)

As on last reporting Friday of	Public Sector Banks	Private Sector Banks	Foreign Banks
1	2	3	4
March 1999	1,04,094	13,947	8,268
	(39.2)	(41.3)	(36.5)
March 2000	1,27,478	18,368	9,934
	(40.3)	(38.0)	(35.2)
March 2001	1,49,116	21,567	11,572
	(43.7)	(36.7)	(33.5)
March 2002 P	1,71,185	25,709	13,414
	(43.1)	(40.9)	(34.0)
March 2003 P	2,03,095	36,705	14,848
	(42.5)	(44.4)	(33.9)
March 2004 P	2,45,501	52,629	17,651
	(43.9)	(47.3)	(34.2)

P : Provisional.

Notes : 1. Figures in parentheses are percentages to net bank credit in the respective group.

2. The target for aggregate advances to the priority sector is 40 per cent of net bank credit for domestic banks and 32 per cent of net bank credit for foreign banks.

8.33 Several recommendations of the *interim* report of the Advisory Committee on Flow of Credit to Agriculture and Related Activities from the Banking System were implemented by the Reserve Bank in its Annual Policy Statement for 2004-05. Loans for storage units (including cold storage) for storing agricultural produce/products, irrespective of their location, are to be reckoned as indirect agricultural advances under the priority sector. Investment by banks in securitised assets representing direct or indirect advances to agriculture would be treated as direct/indirect lending to agriculture under the priority sector, provided that securitised loans are originated by banks and financial institutions. Banks were advised to waive margin/security requirements for agricultural loans up to Rs.50,000 and in the case of agri-business and agri-clinics, for loans up to Rs.five lakh. Non-performing asset (NPA) norms for agricultural finance, including agricultural term loans, were modified with a view to aligning the repayment dates with the harvesting of crops (Box VIII.5). According to the modified norms, a loan will be treated

Box VIII.5

Advisory Committee on Flow of Credit to Agriculture and Related Activities from the Banking System

The Reserve Bank's Advisory Committee on Flow of Credit to Agriculture and Related Activities from the Banking System (Chairman: Prof. V.S. Vyas) submitted its report in June 2004. The major recommendations of the Committee are:

- A comprehensive review of mandatory lending to agriculture by commercial banks to enlarge direct lending programmes for greater integration of investment credit and production credit.
- A road map for public sector and private sector banks to reach a level of direct lending at 13.5 per cent of net bank credit - within the overall limit of 18.0 per cent of total agricultural lending - within a period of four years with an *interim* target of 12 per cent in two years.
- Special Agricultural Credit Plan (SACP) to be restricted to direct lending and extended to private sector banks.
- The share of small and marginal farmers in agricultural credit to be raised to 40 per cent of disbursements under the Special Agricultural Credit Plan (SACP) by the end of the Tenth Plan period.
- Expanding the outreach of banks in rural areas by enlarging retail lending to agriculture, externalising retailing through corporate dealer networks, organisational innovations, offering hedging mechanisms to the farmers, providing legal backing to tenancy to facilitate access to credit, capacity building of borrowers, greater use of information technology, procedural simplifications and modifications in the service area approach.
- Reduction in cost of agricultural credit through enhancing the cost effectiveness of agricultural loans, especially in terms of cost of raising funds, transaction cost and risk cost.
- Non-performing asset (NPA) norms in agricultural credit to be attuned to the cash flow of the farmer, coinciding with the harvesting/marketing of the crop.
- Impediments to the flow of credit to disadvantaged borrowers to be mitigated through reduction in cost of borrowing, revolving credit packages, procedural simplifications, involvement of *Panchayati Raj* institutions and extension of micro finance.

Reference

Reserve Bank of India (2004), "Report of the Advisory Committee on Flow of Credit to Agriculture and Related Activities from the Banking System", *Reserve Bank of India Bulletin,* August.

as an NPA if the instalment of principal or interest remains unpaid for two crop seasons beyond the due date in the case of loans for short duration crops and one crop season beyond the due date in the case of loans for long duration crops.

Micro Finance

8.34 Self-help Groups (SHGs) contribute to development of human and social capital. The number of SHGs linked to banks under the SHG-bank linkage programme aggregated 10,79,091 as on March 31, 2004 of which 90 per cent were exclusively women groups (Table 8.8). The cumulative disbursement of bank loans to SHGs amounted to Rs. 3,904 crore as on March 31, 2004 to around 16 million families. This translates to an average loan per SHG at Rs. 36,179 and the average loan per family at Rs. 2,412.

8.35 The Reserve Bank stepped up efforts to nurture micro finance initiatives. Based on the recommendations of the four Groups on issues relating to structure and sustainability, funding, regulation and capacity building of micro finance institutions, banks were advised to provide adequate incentives to their branches for financing SHGs, establishing linkages and adopting simple and easy procedures to suit local conditions. The ambit of micro finance was extended to include consumption expenditure. Banks were also advised that the group dynamics of the SHGs need not be regulated. There was also no need to impose or insist upon formal structures. Micro finance institutions are not allowed to accept public deposits unless they comply with the extant regulatory framework of the Reserve Bank.

Credit to Agricultural Sector

8.36 The share of agricultural advances of public sector banks in outstanding bank credit has remained stable in recent years (Table 8.9). Disbursements by public sector banks under the Special Agricultural Credit Plan were Rs. 42,211 crore against the projection of Rs. 42,576 crore during 2003-04.

8.37 Some new private sector banks also stepped up agricultural advances. The recovery of direct agricultural advances of public sector banks continued to remain stable (Table 8.10).

8.38 Several initiatives have been taken in pursuance of the objective set in the Union Budget for 2004-05 to achieve a doubling of the flow of credit to agriculture in three years. Banks were advised to reschedule/restructure debts as on March 31, 2004,

Table 8.8: Self-Help Groups and Bank Linkages

(Amount in Rs. crore)

Region/ State	Commercial Banks		Regional Rural Banks		Co-operative Banks		Total	
	No. of SHGs	Bank Loans	No. of SHGs	Bank Loans	No. of SHGs	Bank Loans	No. of SHGs	Bank Loans@
1	2	3	4	5	6	7	8	9
Northern Region								
Haryana	744	7.9	1,563	6.7	37	0.1	2,344	14.6
Himachal Pradesh	5,156	10.0	2,281	4.5	5,791	17.0	13,228	31.5
Punjab	724	3.6	216	1.6	708	3.0	1,648	8.3
Jammu and Kashmir	606	1.6	371	0.6	263	1.4	1,240	3.6
Rajasthan	12,476	25.4	16,996	38.1	4,374	9.8	33,846	73.4
New Delhi	90	0.9		0.0		0.0	90	0.9
Sub-total	**19,796**	**49.4**	**21,427**	**51.6**	**11,173**	**31.4**	**52,396**	**132.4**
North Eastern Region								
Assam	1,809	6.1	8,529	10.2	368	0.5	10,706	16.9
Manipur	162	0.5	63	0.1		0.0	225	0.6
Meghalaya	67	0.6	117	0.0	10	0.0	194	0.6
Sikkim	27	0.1	0	0.0	5	0.0	32	0.1
Tripura	63	0.0	714	0.5	73	0.0	850	0.5
Nagaland	0	0.0	24	0.3	0	0.0	24	0.3
Arunachal Pradesh	150	0.5	53	0.4	22	0.1	225	1.0
Mizoram	1	0.0	21	0.2	0	0.0	22	0.2
Sub-total	**2,279**	**7.8**	**9,521**	**11.7**	**478**	**0.7**	**12,278**	**20.2**
Eastern Region								
Bihar	5,197	13.7	10,916	16.6	133	0.4	16,246	30.8
Jharkhand	7,841	30.3	4,806	11.2		0.0	12,647	41.5
Orissa	25,959	41.4	43,506	72.3	8,123	13.8	77,588	127.5
West Bengal	10,676	11.1	13,946	20.8	27,063	28.5	51,685	60.5
Andaman and Nicobar Islands	5	0.1		0.0	66	0.3	71	0.3
Sub-total	**49,678**	**96.5**	**73,174**	**121.0**	**35,385**	**43.0**	**1,58,237**	**260.5**
Central Region								
Madhya Pradesh	11,087	30.4	13,486	24.1	2,522	5.6	27,095	60.0
Chattisgarh	1,283	1.0	5,879	5.1	2,634	1.8	9,796	7.9
Uttar Pradesh	25,860	51.5	51,005	115.0	2,345	5.1	79,210	171.6
Uttaranchal	7,067	25.9	1,581	6.2	2,260	4.7	10,908	36.8
Sub-total	**45,297**	**108.8**	**71,951**	**150.5**	**9,761**	**17.1**	**1,27,009**	**276.3**
Western Region								
Goa	208	1.1		0.0	98	0.7	306	1.8
Gujarat	9,826	14.6	4,595	8.0	1,553	2.8	15,974	25.5
Maharashtra	18,769	65.5	12,514	32.0	7,252	16.1	38,535	113.6
Sub-total	**28,803**	**81.3**	**17,109**	**40.0**	**8,903**	**19.6**	**54,815**	**140.9**
Southern Region								
Andhra Pradesh	2,46,123	1,142.6	1,30,470	554.7	8,983	31.1	3,85,576	1,728.4
Karnataka	38,605	100.7	37,087	109.5	28,174	73.5	1,03,866	283.6
Kerala	21,378	78.6	5,365	13.6	6,985	30.7	33,728	122.9
Tamil Nadu and Pondicherry	86,463	589.2	39,894	225.7	24,829	124.1	1,51,186	939.0
Sub-total	**3,92,569**	**1,911.1**	**2,12,816**	**903.4**	**68,971**	**259.4**	**6,74,356**	**3,073.9**
Grand Total	**5,38,422**	**2,254.8**	**4,05,998**	**1,278.3**	**1,34,671**	**371.1**	**10,79,091**	**3,904.2**

@ : Includes an amount of Rs.69.8 crore provided to 1,71,669 existing SHGs.

Source : National Bank for Agriculture and Rural Development (NABARD).

of farmers who have suffered production and income losses on account of successive natural calamities during the past five years, provided the State Government concerned declared such districts as calamity affected. Banks were also advised to formulate guidelines on one-time settlement of debt of small and marginal farmers who have been declared defaulters by June 24, 2004 and have become ineligible for fresh credit. Banks are required to review all cases of small and marginal farmers

Table 8.9: Outstanding Agricultural Advances

(Rupees crore)

End-March	Public Sector Banks		Private Sector Banks	
	Amount Outstanding	% of Net Bank Credit	Amount Outstanding	% of Net Bank Credit
1	2	3	4	5
1999	37,632	14.2	3,467	9.1
2000	45,296	14.3	4,023	8.3
2001	53,571	15.7	5,634	9.6
2002 P	63,082	15.9	8,022	8.5
2003 P	73,507	15.3	11,873	10.8
2004 P	86,127	15.4	17,594	12.3

P : Provisional.

Note : The target for advances to agriculture is 18 per cent for the domestic banks.

where credit has been denied on the sole ground that a loan account was earlier settled through compromise or write-offs by September 30, 2004. In order to mitigate the acute distress that farmers might be facing due to the heavy burden of debt from non-institutional lenders (such as money lenders) and to provide them relief from such indebtedness, banks were advised to advance loans to such farmers against appropriate collateral or group security.

Rural Infrastructure Development Fund (RIDF)

8.39 Domestic scheduled commercial banks are required to deposit shortfalls in lending to the priority sector/agricultural lending targets in the Rural Infrastructure Development Fund (RIDF) established with the National Bank for Agriculture and Rural Development (NABARD). The lending and deposit rates in respect of undisbursed amounts of RIDF IV to IX were restructured with effect from November 1, 2003 in order to provide a disincentive to banks for not achieving the agricultural lending target. Banks will be paid interest at 6 per cent per annum in respect of the undisbursed amounts of RIDF IV to VII uniformly and at varying rates of interest between the Bank Rate and Bank Rate *minus* 3 percentage points in respect of RIDF VIII and RIDF IX. The State Governments are required to pay interest at 7 per cent per annum in respect of RIDF IV to VII uniformly and at the Bank Rate *plus* 0.5 percentage points in respect of RIDF VIII and IX. In the case of RIDF VIII and IX, rates of interest on deposits will continue to be inversely linked to the shortfall in lending to agriculture. In pursuance of the announcement made in the Union Budget, 2004-05 the RIDF X has been operationalised with a *corpus* of Rs.8,000 crore for the year 2004-05. The lending and deposit rates in respect of RIDF X will be as applicable to RIDF IX.

Table 8.10: Recovery of Direct Agricultural Advances by Public Sector Banks

(Rupees crore)

Year ended June	Demand	Recovery	Overdues	Percentage of Recovery to Demand
1	2	3	4	5
2000	20,215	14,058	6,158	69.5
2001	22,429	15,540	6,889	69.3
2002	24,561	17,758	6,803	72.3
2003	28,940	21,011	7,929	72.6

Kisan Credit Cards

8.40 Banks were advised to intensify plans for issuing *Kisan* Credit Cards (KCCs) to all eligible borrowers by March 2004 to enable them to purchase agricultural inputs and draw cash for production needs. During 2003-04, public sector banks issued 30.9 lakh cards, exceeding the target of 30 lakh. Banks can provide a personal insurance package to KCC holders – as with other credit cards – to cover against accidental death or permanent disability up to a maximum amount of Rs.50,000 and Rs.25,000, respectively, with the premium burden to be shared by the card holder and issuing institution. Scheduled commercial banks (excluding RRBs) have begun implementing the Personal Accident Insurance Scheme formulated by the NABARD.

8.41 The Reserve Bank commissioned the National Council for Applied Economic Research (NCAER) for conducting a National Impact Assessment Survey to assess the weaknesses of the KCC Scheme and to offer suggestions to make it more effective in providing adequate and timely credit to agriculture (Box VIII.6). The Survey was carried out in 11 representative States, covering a sample of 4,337 KCC holders, 865 non-holders of KCC and 433 bank branches.

Credit to Women

8.42 Public sector banks were advised to lend up to at least 5 per cent of their net bank credit to women by end-March 2004. The credit extended by all public sector banks stood at 4.7 per cent of overall net bank credit. At end-March 2004, 19 banks achieved the annual target.

Credit to SSIs

8.43 The Reserve Bank continued to take steps to enlarge the flow of credit to small scale industries (SSIs). Total credit provided by public sector banks to SSIs worked out to 10.4 per cent of net bank credit

Box VIII.6
Kisan Credit Card (KCC) Scheme - National Impact Assessment Survey (NIAS)

Advantages derived from the Scheme

- Augmentation in flow of credit to the agriculture sector.
- About 6 per cent decrease in cost of borrowings for farmers after they were given KCCs.
- Cost of borrowings for KCC holders from formal sources about 3 per cent lower than those for non-KCC holders.
- Significant drop in the number of borrowers depending exclusively on informal sources for their short-term credit needs.
- Reduction in cost of borrowings from informal sources by about 3 per cent.
- Significant saving in time spent in taking short-term agricultural loans.
- Decline in cost of delivering credit due to simplification in procedures.

Scope for fine tuning

- Banks still impose too many undue restrictions on the issuance of KCCs.
- Cardholders are unable to use KCCs in branches other than the ones issuing them due to the restrictions imposed by banks.
- Generally, there are no incentives/rewards for timely payments.
- Credit limits sanctioned by banks are largely inadequate.
- Awareness/implementation level in respect of the Personal Accident Insurance Scheme is quite low.

and 23.7 per cent of the total priority sector advances as at end-March 2004. 497 specialised SSI branches were operationalised by banks to implement the policy directive of having at least one such branch in every district and centre having a cluster of SSI units.

8.44 Credit extended by scheduled commercial banks to 1,67,980 sick SSI units stood at Rs.5,706 crore as at end-March 2003. Of these, 3,626 units were found to be viable, with their outstanding bank credit at Rs.625 crore (11.0 per cent). Banks placed 993 units involving outstanding credit of Rs.382 crore (6.7 per cent) under nursing programmes.

8.45 The Working Group on Flow of Credit to SSI Sector (Chairman: Dr. A.S. Ganguly) submitted its report to the Reserve Bank in May 2004 (Box VIII.7).

Credit to Khadi and Village Industries Commission

8.46 A consortium of select public sector banks led by the State Bank of India was formed to provide credit to the *Khadi* and Village Industries Commission (KVIC) at an interest rate of 1.5 per cent below the average prime lending rates of five major banks in the consortium. Out of Rs.738 crore disbursed, an amount of Rs.342.4 crore was outstanding at end-March 2004.

Government Sponsored Schemes

8.47 A total number of 8,75,690 *Swarozgari*s received bank loans amounting to Rs.1,275 crore (and Government subsidy amounting to Rs. 698 crore) under the *Swarnajayanti Gram Swarozgar Yojana* (SGSY) during 2003-04. Of the *Swarozgari*s assisted, 4,01,142 (45.8 per cent) belonged to scheduled castes and scheduled tribes, 4,62,230 (52.8 per cent) were women and 8,316 (1.0 per cent) were physically handicapped. Under the *Swarna Jayanti Shahari Rozgar Yojana* (SJSRY), disbursements amounting to Rs. 173.4 crore were made in 58,800 cases (out of 73,877 applications sanctioned) during the year. Besides, Rs. 12.8 crore were disbursed in 7,429 cases out of 9,140 applications sanctioned under the Scheme of Liberation and Rehabilitation of Scavengers (SLRS) during 2003-04.

8.48 SHGs are considered eligible for financing under the Prime Minister's *Rozgar Yojana* (PMRY), effective December 8, 2003, provided all members individually satisfy the eligibility criteria laid down and total membership does not exceed twenty. There is also no ceiling on the loan amount. Assistance under the Scheme amounted to Rs. 629 crore for 1,04,733 beneficiaries during 2003-04. Of these, 16,340 (15.6 per cent of total) belonged to the scheduled castes and scheduled tribes, 15,054 (14.4 per cent) were women and 609 (0.6 per cent) were physically handicapped.

Differential Rate of Interest (DRI) Scheme

8.49 The outstanding advances of public sector banks under the DRI Scheme amounted to Rs. 315 crore in respect of 3.7 lakh borrowal accounts at end-March 2004, forming 0.1 per cent of the total outstanding advances as at the end of the previous year which were substantially lower than the stipulated target of 1.0 per cent of advances. Banks were advised to increase their lending under the Scheme.

Box VIII.7

Recommendations of the Ganguly Working Group

- Definition of the small and medium enterprises (SMEs) sector to be based on turnover. Tiny, small and medium enterprises could be redefined in terms of limits as under:

  Tiny : Turnover up to Rs. 2 crore;

  Small : Turnover of above Rs. 2 crore and up to Rs. 10 crore; and

  Medium : Turnover of above Rs.10 crore and up to Rs. 50 crore.
- Lending to SMEs in identified clusters.
- Rating mechanism for designated industrial clusters, designed jointly by CRISIL, IBA, SIDBI and SSI Associations.
- Measures to promote corporate-linked SME cluster models by banks and FIs.
- Proactive role by CIBIL to serve as an effective mechanism for exchange of information between banks and financial institutions for curbing growth of non-performing assets in the SME sector.
- Setting up of a dedicated national level SME Development Fund by the SIDBI for exclusively undertaking venture and other development financing activities for SMEs. Banks could also contribute to the *corpus* created by the SIDBI (on risk-sharing basis) or alternatively, set up their own venture financing instruments.
- Setting up of an independent Technology Bank for the SMEs by the SIDBI to facilitate technology transfer and provide services such as project evaluation, risk assessment and mitigation to SMEs adopting new technologies. Besides the SIDBI, banks may also contribute to the *corpus* of the proposed Technology Bank to ensure its commercial viability and play an active role in enhancing the capabilities and credit worthiness of the SME sector.
- Promoting and financing special purpose vehicles (SPVs) by banks in the form of micro credit agencies dedicated to servicing SME clusters. Such micro credit intermediaries in the form of NBFCs (funded by individual or a group of banks but not permitted to accept public deposits) could credit rate and assess risk and serve as instruments for extending quick credit to SME clusters accredited to them.
- Special dispensation for the North-East region and other backward areas such as adoption of model of mutual credit guarantee to address the problem of collateral, where village council guarantee is available. Coverage of all SSI units without any ceiling (of Rs.25 lakh) under the Credit Guarantee Fund Trust for Small Industries (CGTSI) scheme.
- Revival of State Financial Corporations.

In pursuance of these recommendations, the Reserve Bank instructed the CIBIL to work out a mechanism, in consultation with the Reserve Bank, the SIDBI, and the IBA, to develop a system of proper credit records to facilitate appropriate pricing of loans to SMEs. A special group is formulating a mechanism for debt restructuring for medium enterprises on the lines of the Corporate Debt Restructuring (CDR) scheme.

Reference

Reserve Bank of India (2004), “Report of the Working Group on Flow of Credit to Small Scale Industries Sector”, *Reserve Bank of India Bulletin,* August.

Amendment of the NABARD Act, 1981

8.50 The NABARD Act, 1981 was amended in September 2003 enabling the NABARD to directly refinance district central co-operative banks (DCCBs). This is proposed to be implemented selectively in respect of DCCBs which comply with Section 11(1) of the Banking Regulation Act, 1949 (As Applicable to Co-operative Societies) and certain other conditions.

Relief for Drought Affected Farmers

8.51 Repayment of loans by farmers in drought-affected districts was deferred during 2002-03. In order to further mitigate the hardship of farmers in drought-affected States, it was decided to waive the first year’s deferred interest liability - amounting to 20 per cent of the deferred interest - on *kharif* loans completely. This instalment of deferred interest which is to be waived by banks would be reimbursed by the Government. No interest would be charged on the deferred interest and the balance of the deferred interest would be recovered in reasonable instalments.

Infrastructure Lending

8.52 The Reserve Bank extended several regulatory relaxations for infrastructure financing during the year. These measures, *inter alia*, included (i) enhancing the scope of definition of infrastructure lending to include construction activities involving agro-processing, supply of inputs to agriculture, preservation and storage of processed agro-products and perishable goods including testing facilities for quality and construction of educational institutions and hospitals; (ii) relaxing the prudential single borrower exposure limit from 15 per cent to 20 per cent of capital funds in respect of infrastructure companies; (iii) assigning a concessional risk weight of 50 per cent on investment in securitised paper satisfying conditions pertaining to an infrastructure facility; (iv) permitting lending to private sector special purpose vehicles (SPVs) registered under the Companies Act for directly undertaking viable infrastructure projects; and (v) lending to promoters, with certain safeguards and where appropriate, for acquiring a controlling stake in existing infrastructure companies. A Working Group on credit enhancement by the State Governments for financing infrastructure at the State level was also constituted.

8.53 A critical limitation in extending long-term financing for infrastructure by banks is that their deposit liabilities are largely short-term. The Reserve Bank, therefore, allowed banks to raise long-term bonds with a minimum maturity of five years to the extent of their exposure of residual maturity of more than five years to the infrastructure sector.

Credit Package to Trade and Industry in the State of Jammu and Kashmir

8.54 A comprehensive package was framed during the year to ensure a large flow of credit to trade and industry in the State of Jammu and Kashmir with appropriate changes in the monitor mechanism. The package would be operative till end-March 2005. It covers, *inter alia*, (i) sanction of increased working capital facilities; (ii) review of all borrowal accounts within a period of 3 months; (iii) encouraging finance against accepted *hundies* (usance bills); (iv) extending concessional service tariffs for remittances; (v) honouring small fixed deposit receipts (up to Rs.10,000) of Kashmiri migrants at the designated branches without verifying details from the branch of origin against indemnity bonds, where necessary; (vi) allowing reschedulement of the repayment programme in deserving cases; and (vii) extension of liberal acceptance of credit/line of credit facilities.

Monetary Policy Stance for 2004-05

8.55 The Reserve Bank's Annual Policy Statement announced in May 2004 was framed against the backdrop of a macroeconomic assessment that provided grounds for optimism. Considering the India Meteorological Department's initial forecast of a normal monsoon and under the assumption of a sustained growth in the industrial sector and good performance of exports, real GDP growth for 2004-05 was placed in the range of 6.5 to 7.0 per cent. Taking into account the inflation trends and assuming no significant supply shocks and appropriate management of liquidity, the inflation rate in 2004-05, on a point-to-point basis, was placed at around 5.0 per cent. Given the 'pass through' of international price trends to domestic inflation, it was stated that the inflation rate during 2004-05 is likely to be influenced to a significant extent by international oil prices and trends in commodity prices. Consistent with the projected real GDP growth and inflation, expansion of money supply (M_3) for 2004-05 is placed at 14.0 per cent. Non-food bank credit adjusted for investment in CPs, shares/debentures/bonds of PSUs and private corporate sector is projected to increase by 16.0 – 16.5 per cent. The Mid-term Review of the Annual Policy would review the macroeconomic developments since the announcement of the Annual Policy and, if necessary, revise the projections.

8.56 Taking into account the assessment of the macroeconomy and assuming no unexpected exogenous shocks or adverse inflationary developments occur, the overall stance of monetary policy for 2004-05 is: (i) provision of adequate liquidity to meet credit growth and support investment and export demand in the economy while keeping a very close watch on the movements in the price level, and (ii) consistent with the above, while continuing with the *status quo*, to pursue an interest rate environment that is conducive to maintaining the momentum of growth and macroeconomic and price stability.

IX DEVELOPMENT AND REGULATION OF FINANCIAL MARKETS

9.1 The maintenance of stable and orderly conditions in financial markets assumed priority for the Reserve Bank in 2003-04. Taking advantage of the headroom provided by the comfortable liquidity conditions, the marked improvement in Central Government's finances and somewhat muted demand for banks' non-food credit in the first half of the year, the Reserve Bank carried forward the development of the money, debt and foreign exchange markets over which it has direct regulatory jurisdiction. Satisfactory operation of paperless and straight through settlement of transactions through the Negotiated Dealing System (NDS)/Clearing Corporation of India Limited (CCIL) brought with it significant gains for the functioning of markets. It facilitated speeding up the process of phasing out non-banks from the call/notice money market and simultaneous growth of a buoyant repo market outside the LAF. New modules in the NDS-CCIL system were introduced leading to a switch to the Delivery *versus* Payment (D*v*P) III mode in the Government securities market from April 2, 2004. Measured liberalisation of external transactions was undertaken with a view to adding depth to the foreign exchange market and freeing outflows by resident corporates and individuals. Sensitising market participants to the risks embedded in sudden shifts in market conditions in accordance with global developments remained a concurrent priority.

9.2 Against this backdrop, this Section presents regulatory and developmental aspects of the functioning of the money, debt and foreign exchange markets in 2003-04. In the money market, the focus of the review is on upgradation of the technological infrastructure and various initiatives taken to improve activity including in the emerging segments. The major initiatives in the Government securities market relate to introduction of new instruments and the functional autonomy accorded to market participants. The review of the foreign exchange market underscores the significant liberalisation granted to all classes of participants with a view to deepening the market, while simultaneously improving transparency in an overall move away from micro management of transactions to macro management of flows. Building and upgrading the technological wherewithal for markets is a recurring theme through this Section.

MONEY MARKET

9.3 The Reserve Bank continued to foster balanced development of different segments of the money market. The strategy for market development was characterised by initiatives to introduce new instruments, reduce dependence of participants on uncollateralised exposures, facilitate price discovery in the short-end and upgrade the payment system infrastructure.

Call/Notice Money Market

9.4 The smooth operation of NDS/CCIL enabled progression in the endeavour to develop the call segment as a pure inter-bank market. Exposures of non-banks in the call/notice money market were brought down from 85 per cent of their average daily lendings during 2000-01 to 75 per cent in June 2003, to 60 per cent in December 2003 and further to 45 per cent in June 2004 (Table 9.1). This process was smoothened by the assurance of temporary reprieve from the phase-out in case any non-bank institution faces any genuine difficulty in deploying excess liquidity.

9.5 With effect from February 7, 2004, primary dealers (PDs) were permitted to borrow up to 200 per cent of their net owned funds (NOFs), as at end-March of the preceding financial year, on average, in a reporting fortnight. Any PD facing genuine difficulty in adhering to the limit was permitted to approach the Reserve Bank for extension of period of compliance.

9.6 An endeavour of the Reserve Bank has been to improve transparency in the call/notice money market. Effective the fortnight beginning May 3, 2003, reporting of call/notice money market transactions on the NDS was made mandatory, irrespective of whether executed on the NDS or outside and whether the counterparty is a member of the NDS or not. Necessary changes in the software and dissemination of data to NDS members was executed in July 2003.

9.7 The Reserve Bank had instituted prudential limits of exposure to the call/notice money market for banks from October 2002 keeping in view the potential risk of systemic instability arising out of defaults due to large recourse to the uncollateralised money market segment. Rupee funds raised under the Reciprocal

Table 9.1: Phasing out of Non-banks from the Call/Notice Money Market

Stages	Time Table Announced
1	2
Stage I	Effective May 5, 2001 non-bank institutions (*i.e.*, financial institutions, mutual funds and insurance companies) were allowed to lend up to 85 per cent of average daily call lendings during 2000-01; corporates were allowed to route call transactions through primary dealers up to June 30, 2001.
Stage II	Effective June 14, 2003 the limit of non-bank lendings in the call/notice money market was scaled down to 75 per cent of average daily call lendings during 2000-01.
Stage III	Access of non-banks to the call/notice money market was lowered to 60 per cent of average daily call lendings during 2000-01 effective December 27, 2003 and to 45 per cent with effect from June 26, 2004.

Line Facility were exempted from these limits. This exemption was phased out from the fortnight beginning February 7, 2004.

Certificates of Deposit

9.8 Activity in the Certificates of Deposit (CDs) segment picked up considerably after the issuance of guidelines by the Reserve Bank and the SEBI on investments by banks and mutual funds in non-SLR debt securities, the reduction in stamp duty on CDs effective March 1, 2004 and disallowance of premature closure of CDs *vis-à-vis* alternative competing instruments such as fixed deposits. These developments stimulated demand for investment in CDs by mutual funds, particularly on account of improved funds positions. An encouraging development in this area was rating of CDs by some banks even when such rating is not mandatory under the existing guidelines.

Commercial Paper

9.9 Non-bank entities, including corporates, were allowed during 2003-04 to offer unconditional and irrevocable guarantees for credit enhancement to CP issuances so as to provide flexibility to both issuers and investors. The issuer is required to fulfil the eligibility criteria prescribed for issuance of CP with the guarantor requiring a credit rating of at least one notch higher than that of the issuer from an approved credit rating agency. The offer document for CP needs to disclose the net worth of the guarantor names of the companies to which the guarantor has issued similar guarantees, the extent of the guarantees offered and the conditions under which the guarantee will be invoked. Banks were allowed to invest in CP guaranteed by non-bank entities, provided their exposure remains within the regulatory ceiling for unsecured exposures. Along with the reduction in stamp duty on CP, the recent guidelines by the Reserve Bank on investments in non-SLR securities evinced keen interest from mutual funds for investment in CPs *vis-à-vis* bonds and fixed deposits.

Derivatives

9.10 The Reserve Bank allowed banks and primary dealers to transact in exchange traded interest rate futures in June 2003 in order to make available a wide array of products for banks to hedge their interest rate risk effectively. While PDs were allowed to hold trading as well as hedging positions in Interest Rate Futures (IRFs), banks were allowed only to hedge their underlying Government securities in 'available for sale' (AFS) /'held for trading' (HFT) category portfolio through IRFs. The National Stock Exchange (NSE) introduced futures on a notional 10-year Government security, a 3-month Treasury Bill rate and a 10-year Government zero coupon in June 2003. Activity in the IRF market has not, however, picked up as yet because of valuation problems. Furthermore, the activity in the IRF market was subdued as banks have been allowed only to hedge but not to trade. The Reserve Bank set up an Internal Working Group on Derivatives in September 2003 which recommended, *inter alia*, (i) a harmonisation of regulations between over-the-counter (OTC) interest rate derivatives and exchange traded interest rate derivatives; and (ii) permission to those banks to hold trading positions in IRF market which have adequate internal risk management and control systems and a robust operational framework. The SEBI revisited issues pertaining to introduction of new futures contracts in consultation with the Fixed Income Money Market and Derivatives Association of India (FIMMDA). On January 5, 2004 it permitted trading of interest rate futures contract on an underlying 10-year coupon-bearing notional bond which would be priced on the basis of the yield-to-maturity (YTM) of a basket comprising bonds with maturity ranging from 9 to 11 years.

Collateralised Borrowing and Lending Obligation (CBLO)

9.11 Collateralised Borrowing and Lending Obligation (CBLO) was operationalised as a money market instrument through the CCIL on January 20, 2003. With a view to developing the market for the CBLO, it was exempted from CRR. Furthermore, securities lodged in the gilt accounts of the bank maintained with the CCIL under the Constituents' Subsidiary General Ledger (CSGL) facility and remaining unencumbered at the end of any day can be reckoned for SLR purposes. The wider usage of the instrument is expected to receive impetus from the establishment of real time connectivity between the Public Debt Office (PDO) of the Reserve Bank and the CCIL and value-free transfer of securities between market participants and the CCIL.

Repo Market

9.12 The Reserve Bank has been making efforts to develop the repo market, so as to provide a stable collateralised funding alternative with a view to promoting smooth transformation of the call/notice money market into a pure inter-bank market and for deepening the underlying Government securities market. To broaden the repo market, the Reserve Bank enabled non-banking financial companies, mutual funds, housing finance companies and insurance companies not holding SGL accounts to undertake repo transactions with effect from March 3, 2003. These entities were permitted to access the repo market through their 'gilt accounts' maintained with the custodians. Necessary precautions were built into the system to ensure 'delivery *versus* payment' (D*v*P) and transparency, while restricting the repos to Government securities only. Rollover of repo transactions in Government securities was facilitated with the enabling of D*v*P III mode of settlement in Government securities which involves settlement of securities and funds on a net basis, effective April 2, 2004. This provided significant flexibility to market participants in managing their collateral.

GOVERNMENT SECURITIES MARKET

9.13 The Reserve Bank stepped up efforts to broaden and deepen the Government securities market during 2003-04. Initiatives to promote liquidity in the Government securities market took the form of relaxation of restrictions relating to transactions in the Government securities, introduction of new instruments such as interest rate derivatives to enable participants to hedge market risk and initiation of stricter prudential regulation and surveillance.

Diversification of Instruments

9.14 During 2003-04, the Reserve Bank continued to issue Floating Rate Bonds (FRBs) as an instrument for hedging interest rate risk by investors in the context of elongation of the maturity profile of Government debt in the recent period. During 2003-04, FRBs were issued in three tranches (May 20, August 8 and November 10, 2003) accounting for 16 per cent of the total issuances of dated securities, excluding those issued by way of private placements with the Reserve Bank. The interest rate on these bonds was calculated by adding a fixed spread (determined in the auction) over a variable base rate. With a view to simplifying the price discovery process in the secondary segment of the Government securities market, the design of determining the variable base rate of FRBs was modified with effect from the auction held on May 19, 2003. In terms of the modified design, the base rate was set equal to the average cut-off yield in the preceding three auctions (instead of six) of 364-day Treasury Bills with annual resetting instead of semi-annual. During 2004-05 (up to August 10, 2004), FRBs were issued in three tranches (May 7, July 2, and August 10, 2004) of Rs. 6,000 crore each accounting for 14.4 per cent of budgeted issuances of dated securities.

9.15 Development of the Separate Trading for Registered Interest and Principal of Securities (STRIPS) market received impetus from the steps taken to realign the coupon payment dates with four identified dates so as to create a critical mass for issue of coupon STRIPS. Accordingly, a new security, *viz.*, 6.01 per cent Government Stock 2028 was issued on August 8, 2003 with coupon dates of the new security aligned with the set of coupon payment dates, *viz.*, March 25 and September 25 as identified by the Working Group on STRIPS. The enabling legal provisions for STRIPS will come into effect with the passage of the Government Securities Bill.

9.16 Banks and PDs were permitted to undertake transactions in exchange traded IRFs in June 2003. Operational guidelines were formulated to enable participation of the entities regulated by the Reserve Bank (see Para 9.10 for details).

Trading in Stock Exchanges

9.17 The country wide anonymous, screen-based and order-driven trading in Government securities, which was introduced in stock exchanges (NSE, BSE and OTCEI) in January 2003, continued to register low trading volumes during 2003-04. A Working Group on Screen Based Trading in Government Securities (Chairman: Shri R. H. Patil) was constituted to examine the successful operationalisation of screen-based trading in the NDS as well as the issue of improving liquidity in Government securities trading in the exchanges. Following its recommendations, an anonymous, screen-based, order matching trading system is being incorporated in the NDS. The introductory demonstration was held on August 11, 2004.

Public Debt Office – Negotiated Dealing System

9.18 The LAF module was operationalised on January 13, 2004 in the Reserve Bank's PDO-NDS. LAF auctions were announced by providing all parameters such as issue, duration, type of auctions, opening and closing time. Market participants submit bids within the cut-off time on the system. Members facing genuine systems problems are permitted to submit physical bids. The Treasury Bill auction module was operationalised on October 22, 2003 on the PDO-NDS. The auction is announced and processed on-line in a straight through process (STP) on the system. These two modules are being further fine tuned, encompassing new features and feedback received from market participants.

Sale of Government Securities – New Dispensations

9.19 The Reserve Bank permitted market participants to sell Government securities from April 2, 2004 against confirmed purchase contracts, provided the previous purchase contracts were either guaranteed by the CCIL or have the Reserve Bank as the counterparty. A sale transaction would be settled either in the same settlement cycle as the preceding purchase contract or in a subsequent settlement cycle so that the delivery obligation under the sale contract is met from the securities acquired under the purchase contract. This dispensation would not only reduce the market risk of participants but also facilitate rollover of repos. It was operationalised by switching over to the D*v*P III mode of settlement of Government securities transactions under which securities are settled on a net basis (as against gross basis under the D*v*P II mode).

Primary Dealers

9.20 The primary dealer system has been introduced in a number of countries with the objective of strengthening the securities market infrastructure and bringing about improvement in the secondary market trading, liquidity and turnover in Government securities as also for encouraging voluntary holding amongst a wider investor base. The primary dealer system has been in operation in India for the last eight years (Box IX.1).

9.21 There were 18 primary dealers (PDs) in operation in India at the end of March 2004 (Table 9.2). Bidding commitments in Treasury Bill auctions for all PDs taken together were fixed at 121.8 per cent of the issue amount indicated to be raised in 2003-04. Total bids received at Rs. 99,279 crore amounted to 157.78 per cent of the total Treasury Bill issues of Rs. 62,921 crore. For dated securities auctions, the bidding commitments for all PDs taken together were originally fixed at Rs.1,31,000 crore. Subsequently, the bidding commitments were reduced to Rs. 98,200 crore due to the reduction in the market borrowing programme of the Government. Actual bids tendered by PDs at Rs.1,10,953 crore were 110.95 per cent of the amounts notified. The success ratio was 66.6 per cent for Treasury Bills and 45.1 per cent for dated securities in 2003-04 as against 62.6 per cent and 45.3 per cent, respectively, in the previous year. PDs offered Rs.1,00,000 crore for underwriting primary issues during the year, out of which bids for Rs.49,150 crore were accepted by the Reserve Bank. The share of total primary purchases by the PDs was higher in 2003-04 at 67 per cent (for Treasury Bills) as against 65 per cent during 2002-03. For dated securities, PDs' share was lower at 50.1 per cent as against 63.0 per cent in 2002-03, reflecting a more aggressive interest in the primary market by other investors. The share of turnover of PDs in outright market for Government securities has declined in recent years, reflecting increased participation by banks. The total bidding commitment (for auctions other than those under the MSS) for the year 2004-05 for dated securities for all PDs has been fixed at Rs. 1,20,300 crore (96.5 per cent of the borrowing programme), while the same for Treasury Bills amounted to 122.6 per cent of the issue amount to be raised. The liquidity support limit under the Standing Liquidity Facilities to all PDs was fixed at Rs. 3,000 crore, *i.e.*, at a lower level than for 2003-04.

Box IX.1
Primary Dealer System - A Cross-country Experience

Primary dealers are financial intermediaries that agree to perform specific obligations or functions in the market for Government securities in exchange for specific privileges. The objectives of the PD system are to ensure that the Government's financing needs and its obligations are met at the lowest possible cost consistent with a prudent degree of rollover risk. The obligations of PDs include (i) participating in the primary market in a substantial and consistent manner; (ii) serving as a market maker in the secondary market by providing two-way quotes; and (iii) providing market related information to the public debt manager.

The system of PD was first established in the US in 1960. In India, it was introduced in 1996. Some advanced countries such as Australia, Germany and New Zealand have not yet established the PD system. According to the IMF's cross country survey in 2003, important prerequisites for establishing a PD system include (i) a debt issuance strategy which provides a medium term horizon of the investment; (ii) interest rate liberalisation in the Government securities market to ensure efficient price discovery; (iii) an adequate number of end investors; (iv) a diversified maturity spectrum in Government securities; (v) policy impetus for developing the secondary market for the Government securities without direct intervention; and (vi) a competitive market environment (Table).

The IMF survey also brings out the crucial role played by the supporting market segments (such as inter-bank and local capital markets) and the infrastructure (such as book-entry system, D*v*P and bidding technology). This supporting system is, however, still under-developed in many countries. With electronic trading of securities and auctions, which effectively expand investor base, the role of PDs in developed economies is losing importance. PDs, however, continue to play a critical role where the fiscal deficits and financing needs of the Government are large.

In India, the PD system has contributed to the development of a deep and vibrant market for the Government securities. Several issues such as granting the PDs limited exclusivity in the Treasury Bills auctions and permitting them to invest in overseas sovereign bonds and setting of joint ventures (JVs)/wholly owned subsidiaries (WOSs) abroad to enable them to diversify their balance sheets are under examination.

Reference

1. Armone, M. and G. R. Iden (2003), "Primary Dealers in Government Securities: Policy Issues and Selected Countries' Experience", *IMF Working Paper No. 45.*

Table : Features of PD System in Various Countries

Country	Starting Date	No. of PDs	Open Market Operations	Availability of Liquidity of Stock Facilities with the Central Bank	Debt/GDP ratio (Per cent)	Periodicity of Review
1	2	3	4	5	6	7
Argentina	1996	12	Yes		30	Annually
Brazil	1974	22	Yes		40	Semi-annually
Canada	1998	12	Yes	Yes	70	Bi-annually
France	1987	18			30	Every 2 years
Hungary	1996	13			70	Semi-annually
India	1996	17	Yes	Yes	50	Annually
Italy	1994	16			120	Every 2 years
Korea	1997	26			10	Annually
Mexico	2000	5		Yes	20	Semi-annually
Singapore	1987	11	Yes	Yes	90	Semi-annually
Thailand	2000	9	Yes		60	Annually
UK	1986	17			40	Semi-annually
US	1960	25	Yes	Yes	50	Semi-annually

Source: Armone and Iden (2003).

9.22 The Reserve Bank issued operational guidelines to PDs to undertake portfolio management service (PMS) for entities other than those regulated by the Reserve Bank subject to (a) prior approval of the Reserve Bank, (b) receipt of certificate of registration from the SEBI and (c) compliance with the operational guidelines issued by the Reserve Bank. PDs were allowed to deal in IRFs on notional bonds and Treasury Bills both for hedging and for holding trading positions. The prudential guidelines

Table 9.2: Select Indicators of Primary Dealers

(Rs. crore)

Item	March 2004	March 2003	March 2002	March 2001
1	2	3	4	5
Number of PDs	18	18	18	15
Total capital (NOF)	5,972 @	5,055	4,371	3,184
Total assets	18,360 @	17,378	15,305	14,772
of which: Government securities (G-Secs)	16,108 @	14,573	12,217	10,401
G-Secs as percentage of total assets	88 @	84	80	70
PD system turnover (outright)	8,10,250	7,32,143	6,52,127	3,16,915
Market turnover (outright)	32,30,790	27,55,482	24,23,933	11,44,291
PD turnover as percentage of outright market turnover	25.1	26.7	26.9	27.7
Liquidity Support Limits	4,500	4,500	6,000	6,000
Normal #		3,000	4,000	
Backstop #		1,500	2,000	
CRAR (per cent)	41.6	29.7	38.4	40.9

NOF : Net Owned Fund.
@ : Unaudited.
\# : Normal and backstop facilities, which were introduced on May 5, 2001, were combined effective March 29, 2004.
Note : Turnover data pertain to the financial year.

on investments by PDs in non-Government securities in both primary and secondary segments were also prescribed in March 2004. Investments in unrated non-Government securities were prohibited, while investment in unlisted non-Government securities was allowed up to 10 per cent of their total non-Government securities portfolio. Prudential guidelines on dividend payout were issued in June 2004. The dividend payout ratio was linked to CRAR and a ceiling on individual payout ratio was fixed.

9.23 The periodical supervisory returns being submitted by PDs were rationalised and simplified. A new quarterly return (PDR-IV) on certain balance sheet and profit and loss (P&L) indicators was introduced from the quarter ended March 31, 2004. Revised 'capital adequacy standards and risk management guidelines' for PDs were issued in January 2004. In terms of the guidelines, the minimum holding period for Value at Risk (VaR) was reduced from 30 days to 15 days. This is expected to reduce capital charge for market risk and enable PDs to hold higher portfolios. The reporting of capital adequacy was standardised. Some off-balance sheet items (such as underwriting commitments), which were not included earlier, were reckoned for risk weighted assets. Besides off-site supervision through structured returns, the Reserve Bank also conducts on-site inspection of PDs. During the year, the inspection of 15 PDs was undertaken.

9.24 The CCIL, which offers clearing and settlement facilities for inter-institutional Government securities transactions and inter-bank foreign exchange transactions, has been recognised as a Systemically Important Payment System (SIPS). The CCIL's turnover in the Government securities segment increased by 63.0 per cent to Rs. 25,18,323 crore in 2003-04. The caps placed by the Reserve Bank on call money borrowings by banks and PDs, the increased activity in the repo market segment and the general upswing in the securities market boosted the CCIL's turnover.

FOREIGN EXCHANGE MARKET

9.25 A number of measures were undertaken during the year to deepen the foreign exchange market and impart flexibility to market participants. The focus was on providing an enabling environment for all entities to engage in foreign exchange transactions. A host of new measures were introduced to further deepen the foreign exchange market (Box IX.2). Liberalisation of foreign exchange transactions was extended to residents, non-residents and corporates. The thrust of liberalisation was on greater transparency, data monitoring and information dissemination and a regulatory shift from micro management of foreign exchange transactions to macro management of foreign exchange flows. Reflecting this, the Exchange Control Department (ECD) of the Reserve Bank was renamed as the Foreign Exchange Department (FED) effective January 31, 2004. Simultaneously, procedural formalities are being minimised to avoid paper work and to reduce compliance burden, while ensuring that Know-Your-Customer (KYC) guidelines are in place.

Box IX.2

Initiatives for Developing the Foreign Exchange Market in 2003-04

Forward Contracts - Residents

- Residents were allowed to book forward contracts and participate in hedging instruments for managing risk in the foreign exchange market. Authorised Dealers (ADs) were allowed to offer foreign currency-rupee options on a back-to-back basis or run an option book as per specified terms and conditions.
- Residents were permitted to book forward contracts for hedging transactions denominated in foreign currency but settled in rupees.
- Resident entities were also allowed to hedge their overseas direct investment exposure against exchange risk.
- The eligible limit for booking of forward contracts by exporters/importers was increased to 50 per cent (from 25 per cent earlier) of the average of the previous three financial years' actual import/export turnover or the previous year's turnover, whichever is higher, (from only average of past three years' turnover earlier) without any limit (US $ 100 million, earlier). Importers/exporters desirous of availing limits higher than the overall ceiling of 50 per cent were allowed to approach the Reserve Bank for permission.
- ADs were permitted to enter into forward/option contracts with residents who wish to hedge their overseas direct investment in equity and debt. These contracts could be completed by delivery or rollover up to the extent of market value on the due date.

Forward Contracts -Non-residents

- Non-residents were permitted to enter into forward sale contracts with ADs in India to hedge the currency risk arising out of their proposed FDI in India.
- Holders of FCNR(B) accounts were permitted to book cross-currency forward contracts to convert the balances in one currency into another currency in which FCNR(B) deposits are permitted.
- FIIs were permitted to trade in exchange traded derivative contracts approved by the SEBI subject to the limits prescribed by it.
- NRIs were allowed to invest in exchange traded derivative contracts approved by the SEBI out of rupee funds held in India on a non-repatriable basis.

9.26 A significant policy change in 2003-04 was derecognition of the overseas corporate bodies (OCBs) in India as an eligible class of investor under various routes/schemes available under the Foreign Exchange Management Act (FEMA). OCBs were not allowed to undertake (i) fresh investments under FDI schemes; (ii) purchase of shares/convertible debentures; (iii) purchase of Government dated securities or Treasury Bills or units of domestic mutual funds; (iv) lending in foreign currency to residents; and (v) to open and maintain non-resident deposit accounts.

Capital Account Liberalisation

9.27 Capital account transactions were further liberalised during 2003-04. Relaxations were allowed for overseas investments and remittances abroad by banks, corporates, resident and non-resident individuals. Policy initiatives to improve the inflows of foreign direct investment, foreign portfolio investment and external commercial borrowings were also carried forward during the year.

Facilities for Resident Individuals

9.28 Resident individuals were allowed to remit up to US $ 25,000 freely per calendar year for any permitted purposes under the current and the capital account. Under this scheme, resident individuals were permitted to acquire and hold immovable property or shares/portfolio investment or any other asset outside India without prior approval of the Reserve Bank. They were also allowed to open, maintain and hold foreign currency accounts with a bank outside India for making remittances without prior approval of the Reserve Bank. Resident beneficiaries were permitted to open and credit the proceeds of insurance claims/ maturity/surrender value settled in foreign currency to their resident foreign currency (RFC) domestic accounts.

9.29 Indian students studying abroad were made eligible for all facilities available to non-resident Indians (NRIs) under the Foreign Exchange Management Act (FEMA). They would, however, continue to avail of educational and other loans as residents in India. The limit for foreign exchange remittance by resident individuals for current account purposes other than import without documentation formalities was raised to US $ 5,000 from US $ 500.

9.30 ADs were permitted to allow remittances for (i) securing insurance for personal health from a company abroad; (ii) covering expenses by artists while touring abroad; (iii) commission to agents abroad towards sale of residential flats/commercial plots in India up to US $ 25,000 or five per cent of the inward remittance per transaction, whichever is higher; (iv) short term credit to overseas offices of the Indian companies; (v) advertisements on foreign television channels; (vi) royalty up to five per cent of local sale and eight per cent of exports and lump sum payment not exceeding US $ 2 million; and (vii) use and/or purchase of trademark/franchise in India.

9.31 The limit for release of foreign exchange for employment abroad, emigration, maintenance of close relatives abroad and education abroad was increased to US $ 1,00,000 on the basis of self declaration. The limit for release of foreign exchange for medical treatment abroad without estimate from a hospital/doctor was increased to US $ 1,00,000 from US $ 50,000. The limit for remittance towards consultancy services from outside India was raised to US $ one million per project from US $ 1,00,000. Resident individuals were permitted to take interest free loans from close relatives residing outside India up to US $ 250,000 with a minimum maturity period of one year.

9.32 Resident individuals maintaining foreign currency accounts with ADs in India or banks abroad were allowed to obtain International Credit Cards (ICCs) issued by overseas banks and other reputed agencies. While no monetary ceiling was fixed by the Reserve Bank for remittance under ICCs, the applicable limit is the credit limit fixed by the card issuing banks. Diplomatic missions, diplomatic personnel and non-diplomatic staff of foreign embassies were allowed to maintain foreign currency deposit accounts in India.

9.33 Remittance of the net salary of a citizen of India on deputation to the office or branch of an overseas company in India was allowed for the maintenance of close relatives residing abroad.

9.34 Balances in the exchange earners' foreign currency (EEFC) and resident foreign currency (domestic) [RFC(D)] accounts were allowed to be credited to non-resident (external) (NRE) rupee/ foreign currency non-resident (banks) [FCNR(B)] accounts at the option of the account holders consequent upon change of residential status (to non-resident).

Facilities for Corporates

9.35 Steps were taken to encourage outflows that would enhance the strategic presence of Indian corporates overseas. They were allowed to invest in overseas joint ventures (JVs)/wholly owned subsidiaries (WOSs) up to 100 per cent of their net worth. This facility was also extended to partnership firms. Resident corporates and registered partnership firms were allowed to undertake agricultural activities overseas, including purchase of land incidental to this activity, either directly or through their overseas offices, *i.e.*, other than through JVs/ WOSs, within the overall limit available for investment overseas under the automatic route. This would enable Indian companies to take advantage of global opportunities and also to acquire technological and other skills for adaptation in India. The automatic route for overseas investment was widened to cover investment overseas through special purpose vehicles (SPVs) and by way of share swaps with requisite approval processes.

9.36 Foreign banks operating in India were permitted to remit net profits/surplus (net of tax) arising out of their Indian operations to their head offices on a quarterly basis without prior approval of the Reserve Bank. Corporates were permitted to issue equity shares against lump sum fees, royalty and outstanding external commercial borrowings (ECBs) in convertible foreign currency. General permission was granted to foreign entities for setting up project offices in India. These project offices were permitted to open foreign currency accounts with the Reserve Bank's approval. Permission was also granted to foreign companies to establish branch offices/units in special economic zones (SEZs) to undertake manufacturing and service activities subject to certain conditions.

9.37 Keeping in view the comfortable foreign exchange reserves and the prevailing strength of India's external sector, a comprehensive review of the guidelines for ECBs led to significant liberalisation. The revised ECB guidelines allowed (i) corporates to access ECBs for undertaking investment activity in India and for overseas direct investment in JVs/WOSs, and (ii) borrowings under the approval route by financial institutions dealing exclusively with infrastructure or export finance and also by banks and financial institutions which had participated in the textile or steel sector restructuring package. The maximum amount of ECB that can be raised by Indian corporates under the automatic route was enhanced to US $ 500 million in a financial year with minimum average maturity of three years for loans up to US $ 20 million and minimum average maturity of five years for loans above US $ 20 million. Initiatives were taken for bringing about transparency in policy implementation and data dissemination with respect to ECBs.

9.38 Indian companies were permitted to grant rupee loans to their employees who are NRIs or persons of Indian origin (PIO) for personal purposes, including purchase of housing property in India.

Facilities for Exporters and Importers

9.39 The remittance of premium made by exporters for overseas insurance of exports of sea-food and other perishable food/food products against rejection by importers was permitted. ADs were allowed to grant permission to exporters for opening/hiring of warehouses abroad initially for one year and renewal thereof. Units in domestic tariff areas (DTAs) were allowed to make payment in foreign currency towards goods supplied to them by units in SEZs. Project/ service exporters were allowed to pay their Indian suppliers/ service providers in foreign currency from their foreign currency accounts maintained in India for execution of such projects. Realisation of export proceeds up to 360 days from the date of shipment was allowed for export of books on a consignment basis.

9.40 The limit on export of goods by way of gifts was increased from Rs. 1 lakh to Rs. 5 lakh per annum. With effect from April 1, 2004 submission of declaration in form GR/SDF/ PP/SOFTEX in respect of export of goods and software of value not exceeding US $ 25,000 or its equivalent was waived.

9.41 The limit for submission of documentary evidence of all imports made into India was enhanced from US $ 25,000 to US $ 1,00,000. For select importers, the limit for accepting exchange control (EC) copy of bill of entry for import remittances was enhanced from US $ 1,00,000 to US $ one million, subject to certain conditions.

9.42 Credits for imports up to US $ 20 million per transaction with a maturity period beyond one year and up to three years were permitted only for import of capital goods. Limits for direct receipt of import bills/documents by non-corporate importers were raised to US $ 100,000 or its equivalent.

9.43 Exporters with good track record, including those in small and medium sectors, have been made eligible for issue of Gold Card to ensure easy availability of export credit. The salient features of the Gold Card scheme include better terms of credit than those extended to other exporters by banks, faster and simpler processing of applications for credit, sanction of 'in principle' limits for a period of three years with the provision of timely renewal and preference for grant of packing credit in foreign currency. The Gold Card holders will also be considered for issuance of foreign currency credit cards for meeting urgent payment obligations on the basis of their track record of timely realisation of export bills.

Facilities for Overseas Investments

9.44 Listed Indian companies were permitted to disinvest their investment in JVs/WOSs abroad even in cases where such disinvestment may result in a write-off of the capital invested to the extent of 10 per cent of the previous year's export realisation. Firms in India registered under the Indian Partnership Act, 1932 and with a good track record were permitted to make direct investments outside India in an entity engaged in any *bona fide business* activity under the automatic route up to 100 per cent of their net worth.

9.45 Multilateral institutions such as International Finance Corporation (IFC) and Asian Development Bank (ADB), which can float rupee bonds in India, were permitted to purchase Government dated securities.

Facilities for Non-resident Indians (NRIs) and Persons of Indian Origin (PIO)

9.46 Non-resident shareholders were allowed to apply for issue of additional equity shares or preference shares or convertible debentures over and above their rights entitlements. Allotment is subject to the condition that the overall issue of shares to non-residents in the total paid-up capital of the company does not exceed the sectoral cap.

9.47 NRIs were permitted to invest in exchange traded derivative contracts approved by the SEBI out of rupee funds held in India on a non-repatriable basis, subject to the limits prescribed by the SEBI. Foreign Embassies /Diplomats/Consulate Generals were allowed to purchase/sell immovable property in India other than agriculture land/plantation property/farm houses.

9.48 ADs were permitted to grant rupee loans to NRIs. Earlier, housing loans availed by NRIs/PIO could be repaid by borrowers either by way of inward remittances through normal banking channels or by debit to NRE/FCNR(B)/NRO/NRNR/ NRSR accounts or out of rental incomes derived from the property. In May 2004, borrowers' close relatives in India were allowed to repay the instalment of such loans, interest and other charges directly to the concerned ADs/ housing finance institutions through their bank accounts.

Foreign Exchange Clearing

9.49 An important element in the infrastructure for the efficient functioning of the foreign exchange market has been the clearing and settlement of inter-bank US dollar-rupee transactions. The CCIL offers a multilateral netting mechanism through a process of novation for inter-bank spot and forward US dollar-rupee transactions. The live operations of foreign exchange clearing, which commenced from November 12, 2002 have been satisfactory. Effective February 2004, the CCIL began to settle cash and T+1 settlement trades in addition to spot and forward trades. The CCIL also launched its foreign exchange trading platform, *i.e.,* FX-CLEAR on August 7, 2003. During the period between April 2003 and June 2004, 8,97,352 trades amounting to over US $ 727 billion were settled by the CCIL.

Outlook

9.50 The Reserve Bank would continue to calibrate the process of building various segments of the financial market with overall macroeconomic developments with a view to improving allocative efficiency and ensuring financial stability. In the near term, the reintroduction of Capital Indexed Bonds (CIBs) with modified features would improve the width of the Government securities market. Harmonisation of the regulatory prescriptions for OTC and exchange traded interest rate derivatives with clearing arrangements through the CCIL is under consideration. Enhancements in hardware and software systems and functionalities including introduction of anonymous, screen-based and order matching in the NDS are also underway. The operationalisation of the RTGS would bring speed and efficiency to financial transactions. The ongoing upgradation of the CCIL-NDS and the other elements of technological infrastructure, introduction of new instruments, the sequenced process of developing the call/notice money market into a pure inter-bank market, the concurrent development of other market segments and the gathering pace of exchange and payments liberalisation are all expected to deepen financial markets and ensure stability and vibrancy.

X FINANCIAL REGULATION AND SUPERVISION

10.1 The blurring of the distinction between financial intermediaries under the combined effect of domestic and cross-border integration, innovations in instruments and processes, advances in technology and the massive volumes of capital intermediated by the financial system has necessitated a pro-active strengthening of the regulatory and supervisory framework. Recent international experience has highlighted the critical role played by the regulatory and supervisory system in ensuring the stability of the financial system. This has made the upgradation and refinement of the regulatory and supervisory function of the Reserve Bank a concurrent priority. The approach of the Reserve Bank in this context has been to pursue a progressive upgrading of prudential norms and benchmarking of these norms against international best practices, although there has been a strong emphasis on adapting these standards to the country-specific situation.

10.2 This Section presents an overview of the regulatory and supervisory policy initiatives undertaken in 2003-04 to intensify and broaden the ongoing process of financial sector reforms. It reviews the measures initiated during the year to strengthen the financial sector with a view to calibrating the approach to a new supervisory regime compatible with the Basel II process. An overview of various measures initiated to enhance the co-ordination with other regulatory agencies, to strengthen the transparency and corporate governance practices and to improve customer service is also presented. The performance of various intermediaries - commercial banks, co-operative banks, financial institutions and non-bank financial companies - is evaluated in terms of key financial and prudential indicators.

REGULATORY FRAMEWORK FOR THE INDIAN FINANCIAL SYSTEM

10.3 The Reserve Bank regulates commercial and urban co-operative banks, development finance institutions (DFIs) and non-banking financial companies (NBFCs). There are 293 commercial banks (289 scheduled and 4 non-scheduled), 1,926 urban co-operative banks (UCBs), 9 DFIs and 13,671 NBFCs (of which 584 NBFCs are permitted to accept/hold public deposits). In addition, the Reserve Bank is also the regulator in respect of State and district central co-operative banks [(the supervision is vested with the National Bank for Agriculture and Rural Development (NABARD)]. Life insurance companies and mutual funds are regulated by the Insurance Regulatory and Development Authority (IRDA) and the Securities and Exchange Board of India (SEBI), respectively.

10.4 The main objective of regulation and supervision has been to maintain confidence in the financial system by enhancing its soundness and efficiency. For this purpose, the Reserve Bank evaluates system-wide risks and promotes sound business and financial practices. It also conducts analyses of institution-wise risks to detect deficiencies in their operations, if any, in a timely manner and ensures that institution-specific problems do not spread to the system as a whole. The Board for Financial Supervision (BFS), constituted as a Committee of the Central Board of the Reserve Bank in November 1994 and headed by the Governor with a Deputy Governor as Vice Chairperson and other Deputy Governors and four Directors of the Central Board as members, held 12 meetings during the period July 2003 to June 2004. During this period, it examined 105 inspection reports. While State and district co-operative banks are supervised by the NABARD, certain problem cases are reviewed by the BFS. The Reserve Bank closely monitors these banks to enforce regulatory provisions and takes corrective action in respect of problem banks.

REGULATORY AND SUPERVISORY INITIATIVES

10.5 As the financial sector matures and becomes more complex, the process of deregulation must continue, but in such a manner that all types of financial institutions are strengthened and financial stability of the overall system is safeguarded. As deregulation gathers momentum, the emphasis of regulatory practice has to shift towards effective monitoring and implementation of regulations. To ensure this shift in regulatory practice, corporate governance within financial institutions must be strengthened and internal systems must be developed. Furthermore, as financial institutions expand and grow more complex, it is also necessary to ensure that the quality of service to customers is focused upon and improved.

10.6 Various issues which received regulatory attention during the year included ownership and governance in banks, further progress towards international best practices in prudential norms with country-specific adaptation, greater deregulation and rationalisation of banking policies, compliance with Know Your Customer (KYC) norms, strengthening the financial system for global integration in the light of the ongoing liberalisation of the capital account, greater inter-regulatory co-ordination and the drive for improving the quality of public services rendered by banks. In the evolution and implementation of policy, a consultative approach continues to be followed through formal institutional structures such as the BFS, the newly-formed Standing Committee on Financial Regulation, the Technical Committee on Money and Government Securities Markets and also through specific working groups and committees as well as formal and informal consultations with the regulated entities, external experts and professionals.

Scheduled Commercial Banks

Ownership and Governance of Banks

10.7 Corporate governance has assumed crucial significance for ensuring the stability and soundness of the financial system in recent years. The ongoing debate is focused on shareholders' rights and shareholder influence on corporate behaviour in respect of banks. Furthermore, in order to protect the interests of depositors and integrity of the financial system, it is necessary that owners and managers of banks are persons of sound integrity. Keeping these considerations in view, the Reserve Bank initiated several measures to enhance transparency and strengthen corporate governance practices in the financial sector in India.

10.8 The Reserve Bank provided guidelines for acknowledgment for transfer of shares of private sector banks in February 2004. The guidelines set out the factors that would be taken into account by the Reserve Bank for permitting acquisition of 5 per cent or more of the paid-up capital of banks. Due diligence would be intensified at higher threshold levels, keeping in view the desirability of diversified ownership and public interest. It was also decided that an independent advisory committee will make appropriate recommendations to the Reserve Bank for dealing with such applications.

10.9 In pursuance of the discussions held at the BFS for ensuring that suitable persons are appointed as directors in private sector banks, the Reserve Bank advised banks in June 2004 that they should undertake due diligence to ensure that persons appointed as directors satisfy 'fit and proper' criteria upfront. Also, such persons should be required to sign a deed of covenant undertaking to follow good governance principles.

10.10 The BFS formulated a draft comprehensive policy framework with regard to ownership of and governance in private sector banks and placed it in the public domain on July 2, 2004 for wider consultation and feedback before it is finalised. The draft policy framework envisages diversified ownership and restrictions on cross holding by banks (Box X.1).

10.11 In terms of the existing legal framework, mergers between banking companies and non-banking companies do not require specific approval by the Reserve Bank. As such mergers could involve significant changes in ownership and control of banks with implications for depositor interest, the Reserve Bank advised banks in June 2004 that banks should obtain prior approval of the Reserve Bank for any merger with a non-banking financial company.

10.12 In order to minimise cross holding of equity and other instruments eligible for capital status within the financial system, banks/DFIs were advised in July 2004 to restrict their investments in these instruments issued by other entities in the financial system to 10 per cent of the investing bank's capital funds. Furthermore, the equity holding in any other bank/ DFI is required to be restricted to 5 per cent of the capital of the investee bank. Banks/DFIs are required to indicate to the Reserve Bank the time frame for reducing the equity holding where such holding exceeds 5 per cent.

Strengthening Prudential Norms

10.13 Banks were advised to ensure that the building up of the Investment Fluctuation Reserve (IFR) to 5 per cent of their investments in 'Held for Trading' (HFT) and 'Available for Sale' (AFS) categories is achieved earlier, though they have time up to March 2006. In order to ensure that the internationally accepted norms for capital charge for market risk under Basel I are adopted, banks were also advised in June 2004 to maintain an explicit capital charge for market risks on the lines of the standardised duration method prescribed under the 1996 Amendment to the Capital Accord issued by the Basel Committee on Banking Supervision (BCBS). This would apply to the trading portfolio by March 2005 and to the AFS category by March 2006.

Box X.1

Ownership and Governance in Private Sector Banks - Draft Guidelines

The objective of the draft guidelines issued by the Reserve Bank in July 2004 is to have a regulatory road map for ownership and governance in private sector banks in the interests of the depositors and financial stability. The underlying thread of the draft guidelines is to ensure that the ultimate ownership and control of banks is well diversified, banks are owned and managed by 'fit and proper' persons/entities and well capitalised and that the processes are transparent and fair. Several countries, both developed and developing, have regulatory stipulations and clearance for significant shareholding and control. The threshold level may vary from country to country and can also involve more stringent conditions for higher thresholds.

The draft guidelines allow for a level of shareholding of a single entity or a group of related entities beyond 10 per cent with the prior approval of the Reserve Bank. Such approval will be governed by the principles enunciated in the February 2004 guidelines. Apart from more intensive due diligence at higher levels of shareholding, the February 2004 guidelines require public interest objectives to be served for shareholding beyond 30 per cent. Where the ownership of a bank is by a corporate entity, diversified ownership of that corporate entity will be considered among other factors. The draft guidelines do not cover foreign bank investment in Indian banks, which will be released separately, consistent with the policy in the Government press note of March 2004 to allow only one form of operational presence for foreign banks in India.

In order to minimise vulnerability due to small size, the guidelines provide for increasing the net owned funds to Rs.300 crore for all private sector banks within a reasonable period. Cross holding beyond 5 per cent is sought to be discouraged and where such holding exceeds five per cent, the objective is to reduce it to 5 per cent. Promoters with existing shareholding beyond 10 per cent will be required to indicate the time table for reduction - the requests would be considered on the basis of the underlying principles of 'fit and proper' governance and public interest. As a matter of desirable practice, not more than one member of a family or close relative or associate should be on the board. Based on the feedback received, a second draft of the guidelines would be prepared and put in the public domain.

10.14 Banks were advised to examine the soundness of their risk management systems and draw up a road map by end-December 2004 for migration to Basel II. They were also advised to review the progress made thereunder at quarterly intervals. The Reserve Bank is closely monitoring the progress made by banks in this direction.

10.15 In terms of the earlier guidelines, all eligible direct agricultural advances would become NPA when interest and/or instalment of principal remains unpaid, after it has become due for two harvest seasons, not exceeding two half years. In the case of long duration crops, the prescription of “not exceeding two half-years” was considered to be inadequate. In order to align the repayment dates with crop seasons, with effect from September 30, 2004 a loan granted for a short duration crop (*i.e.,* with a crop season less than one year) would be treated as a non-performing asset (NPA), if the instalment of principal or interest thereon remains overdue for two crop seasons. A loan granted for a long duration crop (*i.e.*, with a crop season beyond one year) would be treated as NPA, if the instalment of principal or interest thereon remains overdue for one crop season.

10.16 Banks were advised to increase the provisioning on the secured portion of doubtful assets which have remained in that category for over three years from 50 to 100 per cent. In the case of existing assets in this category, a time period of three years is allowed. It is expected that this will facilitate speedy resolution of doubtful assets including through transfer to asset reconstruction companies (ARCs).

10.17 The Reserve Bank’s guidelines on country risk management issued in February 2003 require banks to maintain provisions on a graded scale relating to the level of risk in respect of countries to which they have net funded exposure of two per cent or more of total assets. With effect from the year ending March 31, 2005 the coverage would be enlarged to include countries to which a bank has net funded exposure of one per cent or more of its total assets.

10.18 As banks have been putting in place risk management systems and considering the requirement of banks to cater to the evolving requirements of their clientele, the Reserve Bank permitted banks to consider enhancement of the exposure up to a further 5 per cent of capital funds to 20 per cent of capital funds for a single borrower and 45 per cent of capital funds for group borrowers. The additional limits to be sanctioned are subject to approval by banks’ boards and the borrower consenting to the banks making appropriate disclosures in their annual reports.

10.19 The reporting mechanism for cases of wilful default by banks/DFIs was strengthened in July 2003. Decisions to classify borrowers as wilful defaulters were entrusted to a committee of senior functionaries headed by an Executive Director. The decision to declare a borrower as a wilful defaulter should be supported by sufficient evidence *vis-á-vis* the Reserve Bank's guidelines. Banks/DFIs should create a grievance redressal mechanism, headed by the Chairman and Managing Director, for allowing representation by borrowers who have been wrongly classified as wilful defaulters.

Resolution of NPAs

10.20 During the year, the Reserve Bank strengthened the existing mechanisms for NPA management and initiated some new measures to strengthen the efforts of banks to recover their dues.

10.21 A recent addition to the menu of options available to banks for resolving NPAs is the establishment of ARCs. In terms of the provisions of the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest (SARFAESI) Act, 2002 the Reserve Bank prescribed guidelines for the formation and functioning of securitisation companies (SC) and reconstruction companies (RC). Guidelines were also provided to banks/DFIs to facilitate sale of NPAs to SCs/RCs. One ARC, *viz.*, Asset Reconstruction Company of India Ltd. (ARCIL) was set up during 2003-04. Banks and financial institutions sold assets aggregating Rs.7,099 crore to ARCIL.

10.22 Corporate debt restructuring offers an avenue for reorganising the indebtedness of viable entities without reference to the Board for Industrial and Financial Reconstruction (BIFR), debt recovery tribunals (DRTs) and other legal proceedings. The process of corporate debt restructuring gained momentum during 2003-04 after revised guidelines were provided by the Reserve Bank in June 2004 (Table 10.1). The major beneficiaries were iron and steel, refinery, fertilisers and telecommunication sectors which accounted for more than two-thirds of the total value of assets restructured.

10.23 In pursuance of the recommendations of the Working Group to review the existing provisions of the Recovery of Debts Due to Banks and Financial Institutions Act, 1993 (Chairman: Shri S. N. Aggarwal), the Central Government amended substantially the Debt Recovery Tribunal (Procedure) Rules in 2003, especially Rules 7 and 10 relating to application fee and plural remedies, respectively. A Working Group was also set up for reviewing and streamlining the functioning of DRTs. Out of 61,301 cases (involving Rs.88,876 crore) filed with DRTs by banks as on December 31, 2003, 25,510 cases (involving Rs.23,273 crore) were adjudicated with recovery amounting to Rs.6,874 crore.

Table 10.1: Progress under Corporate Debt Restructuring Scheme

(Amount in Rupees crore)

Item	No. of cases	Amount involved
1	2	3
Cases referred to CDR forum	135	72,139
Final schemes approved	94	64,017
Rejected	30	5,445
Pending	11	2,677

10.24 A scheme for settlement of chronic NPAs up to Rs.10 crore in public sector banks was introduced in January 2003 to give one more opportunity to borrowers for settlement of their outstanding dues. As on March 31, 2004, 2,12,370 cases amounting to Rs.1,977 crore were decided by banks and recovery was effected in 1,80,117 cases aggregating Rs.1,095 crore.

10.25 The SARFAESI Act, 2002, *inter alia*, provides for enforcement of security interest for realisation of dues without the intervention of courts or tribunals. In April 2004, the Supreme Court upheld the right of banks and financial institutions to attach and sell assets of the defaulting companies and the borrower's right to appeal. It struck down the provisions contained in Section 17 (2) of the SARFAESI Act requiring the defaulting borrower to pre-deposit 75 per cent of the liability in case the borrower wants to appeal against the order of the attachment of the assets. The Union Budget, 2004-05 has proposed to amend the relevant provisions of the Act to appropriately address the Supreme Court's concerns regarding a fair deal to borrowers while ensuring that the recovery process is not delayed or hampered. Up to December 31, 2003 27 public sector banks issued 49,169 notices involving an amount of Rs.16,318 crore. An amount of Rs.1,037 crore from 16,490 cases was recovered.

Inter-Regulatory Co-ordination and Co-operation

10.26 The Reserve Bank announced in November 2003 that it would set up a monitoring system in respect of systemically important financial intermediaries (SIFIs), including (i) a reporting system for SIFIs on financial matters of common interest to the Reserve Bank, the SEBI and the IRDA; (ii) the reporting of intra-group transactions of SIFIs; and (iii) the exchange of relevant information among the Reserve Bank, the SEBI and the IRDA. A Working Group (Chairperson : Smt. Shyamala Gopinath) was set up by the Reserve Bank in December 2003 with representation from the SEBI and the IRDA to recommend a framework for monitoring financial conglomerates. The Working Group, which submitted its report in June 2004, recommended the introduction of a framework for the complementary supervision of financial conglomerates (Box X.2).

10.27 The High Level Co-ordination Committee on Financial and Capital Markets (HLCCFCM), set up in 1992 with the Governor of the Reserve Bank as its Chairman and Finance Secretary, Government of India and the Chairman, SEBI as its members (subsequently, the Chairman, IRDA was also made a member), constituted three Standing Technical Committees in order to provide a more focused inter-agency forum for sharing of information and intelligence. These Committees meet at regular intervals. Reports detailing the outcome of the meetings are presented before the HLCCFCM for its information and any further directions.

10.28 The responsibilities of the Technical Committee on RBI Regulated Entities include reviewing exposure of the Reserve Bank regulated entities to the capital market on an ongoing basis in the light of market developments. In case a policy issue of wider interest requires inter-agency co-ordination, it also decides whether the case should be referred to the RBI-SEBI Technical Committee of the HLCCFCM.

Opening up of the Financial Sector

10.29 In terms of the agreement arrived at under the *aegis* of the World Trade Organization (WTO), India is committed to permitting the opening of 12 new branches by foreign banks per year in the country. Thirty two foreign banks now operate 217 branches in India. During 2003-04, permission was granted to 5 foreign banks to open 18 branches. Three foreign banks, *viz*., Toronto Dominion Bank, Overseas Chinese Banking Corporation Ltd. and Bank Muscat (SAOG) shut down their branches in India. There was a worldwide merger of Credit Lyonnais and Credit Agricole Indosuez into CALYON Bank, which resulted in the merger of their operations in India as well. In addition to opening of branches, foreign banks can open representative offices which cannot do any banking business. During the year, Everest Bank Ltd., Nepal was permitted to open a representative office in New Delhi and with West LB AG, Germany closing down its representative office, the number of operating representative offices stands at 26.

10.30 Indian banks continued to expand their presence overseas. During the year, ICICI Bank opened representative offices in Dubai (UAE) and Shanghai (China), while IndusInd Bank set up offices in Dubai (UAE) and London (UK) and Punjab National Bank opened an office in London (UK). The number of Indian banks with overseas operations increased by one to 10, although the number of branches remained at 93. The number of representative offices increased by four to 22. The total number of subsidiaries set up by Indian banks stood at 16.

10.31 During 2003-04, ten banks were given 'in principle' approval to open 14 overseas banking units (OBUs) in Special Economic Zones (SEZs). Of these, six banks, *viz*., State Bank of India, Bank of Baroda, Union Bank of India, ICICI Bank and Punjab National Bank have begun operations in the Santa Cruz Electronics Export Processing Zone, Mumbai and Canara Bank in NOIDA, Uttar Pradesh.

Box X.2

Working Group on Monitoring of Financial Conglomerates

The major recommendations of the Working Group on Financial Conglomerates comprise:

- Identifying financial conglomerates for focused regulatory oversight; capturing intra-group transactions and exposures amongst 'group entities' within the identified financial conglomerates and large exposures of the group to outside counter parties; identifying a designated entity within each group to furnish group data to the principal regulator for the group; and formalising a mechanism for inter-regulatory exchange of information.
- Segments under the jurisdiction of the Reserve Bank, the SEBI, the IRDA, and the NHB should be subjected to complementary regulation. The framework could later be extended to the segment covered by the Pension Fund Regulatory and Development Authority.
- The new reporting framework should track: (i) any unusual movement in respect of intra-group transactions manifested in major markets; (ii) build-up of any disproportionate exposure (both fund based and non-fund based) of any entity to other group entities; (iii) any group-level concentration of exposure to various financial market segments and outside counter parties; and (iv) direct/ indirect cross-linkages amongst group entities.
- Individual intra-group transactions beyond threshold levels (Rs.1 crore for fund based transactions and Rs.10 crore for others) should be included in the reporting format, supplemented by exposure ceilings in respect of intra-group exposures.

Reference

Reserve Bank of India (2004), *Report on Monitoring of Financial Conglomerates,* June.

Towards More Deregulation

10.32 As a part of the move towards greater deregulation, banks fulfilling certain minimum criteria regarding CRAR and net NPAs have been given the discretion to pay dividend without the prior approval of the Reserve Bank, provided the dividend payout ratio does not exceed 33.3 per cent. Banks which do not meet the minimum criteria or which seek a higher payout ratio are required to obtain the prior approval of the Reserve Bank. Foreign banks operating in India were advised that they may remit net profits/surplus (net of tax) arising out of their Indian operations on a quarterly basis, without the prior approval of the Reserve Bank. This is conditional on (i) audit of the accounts on a quarterly basis, (ii) appropriate transfers to statutory reserves as per Section 11(2)(b)(ii) and other relevant provisions of the Banking Regulation (BR) Act, 1949, and (iii) compliance with the directions issued by the Reserve Bank.

10.33 Banks were not allowed to assume unsecured exposures by way of guarantees and advances beyond a prescribed ceiling in terms of the Reserve Bank's guidelines prescribed in 1967. In view of the ongoing shift towards financing borrowers based on estimated cash flows rather than on collateral and in recognition of the availability of financial assistance through credit substitutes, *viz.*, commercial paper, bonds and debentures, the restriction on unsecured exposures was withdrawn. Banks' boards are allowed to formulate their own policies on unsecured exposures. The unsecured exposures would, however, attract a higher provisioning of 20 per cent when they become sub-standard.

10.34 Effective September 22, 2003 banks are not required to obtain prior approval of the Reserve Bank for engaging in insurance agency business or referral arrangement without any risk participation, subject to their complying with the prescribed conditions. Banks intending to set up insurance joint ventures with equity contribution on a risk participation basis or making investments in insurance companies for providing infrastructure and services support would still require prior approval of the Reserve Bank.

Towards Greater Transparency

10.35 In recent years, banks have turned out to be the major investors in bonds issued on a private placement basis. In view of the fact that issuance of such bonds lacked transparency, banks were advised in November 2003 to restrict their fresh investments in unlisted securities to 10 per cent of their overall non-SLR portfolio. A time period was also prescribed for getting the existing outstanding bonds listed. Simultaneously, the SEBI also prescribed guidelines requiring all debt issuances, including private placements, to be rated and listed within a specified time period.

10.36 With a view to aligning standards adopted by the Indian banking system with global standards, the Reserve Bank issued detailed guidelines relating to several Accounting Standards (AS) in March 2003. In April 2004, guidelines for compliance with three more standards, *viz.*, AS 24 (discontinuing operations), AS 26 (intangible assets) and AS 28 (impairment of assets) were issued. Banks are required to ensure that there are no qualifications by the auditors in their financial statements for non-compliance with any of the accounting standards.

10.37 The Credit Information Bureau (India) Ltd. (CIBIL) took over from the Reserve Bank the responsibility of disseminating the information on suit-filed accounts at banks/FIs in India in respect of defaulters and wilful defaulters with effect from March 31, 2003. The Reserve Bank issued instructions to banks/DFIs to obtain the consent of all their borrowers - not only defaulters - for dissemination of credit information to enable CIBIL to compile and disseminate comprehensive credit information.

Preserving the Integrity of the Banking System

10.38 Preventing misuse of the financial system and preserving its integrity is vital for orderly development of the financial system. Prevention of frauds and implementation of anti money laundering (AML) measures are two important aspects of the efforts being made by the Reserve Bank to prevent misuse of the financial system by criminals whose transactions threaten the stability of financial transactions worldwide.

10.39 In 2002, banks were advised to follow certain KYC norms while opening accounts, with specific focus on verification and identity. These norms were also required to be applied to the existing accounts in a given time frame. With a view to adopting a risk-based approach and to mitigate the inconvenience to the common man, banks were advised to apply the new KYC norms only to those accounts where the annual credit or debit summation were Rs.10 lakh or more or where the transactions in the account was of a suspicious nature.

Improving Customer Service

10.40 The Reserve Bank set up a Committee on Procedures and Performance Audit on Public Services (Chairman : Shri S.S.Tarapore) to advise it on improving the quality of such services. Banks were asked to constitute similar a*d hoc* committees to undertake procedures and performance audit on public services rendered by them and co-ordinate with the Tarapore Committee. Based on the reports of the Committee on personal transactions of individuals in foreign exchange, government transactions, banking operations and currency management, a number of guidelines have been issued with a view to improving the customer service rendered by banks and the Reserve Bank.

10.41 The Reserve Bank provided detailed operational guidelines for banks for the process of takeover of bank branches in rural and semi-urban centres. Due publicity is required to be given to the constituents of the branch concerned by the existing bank as well as of the bank taking over. In cases where the rural branch being taken over is the only one functioning in the village/town, the bank taking over would not be permitted to merge it with any of its existing branches in rural/semi-urban areas (with service area obligation).

Technology Upgradation/ Training

10.42 The Reserve Bank has been emphasising the need to harness the developments in information technology in the business of banking (Box X.3).

Strengthening the Consultative Process

10.43 The relationship between the Reserve Bank and market participants has continued to evolve over a period through the expansion and reinforcement of the consultative processes. A Standing Technical Advisory Committee on Financial Regulation was set up during the year on the lines of the Reserve Bank's Technical Advisory Committee on Money and Government Securities Market. The Committee would advise the Reserve Bank on regulations covering banks, non-bank financial institutions and other market participants on an ongoing basis, in addition to the existing channels of consultation. The Committee, constituted with Smt K.J.Udeshi, Deputy Governor as the Chairperson, comprises experts drawn from academia, financial markets, banks, non-bank financial institutions and credit rating agencies. During the year, the Committee's views were sought on a wide range of topical regulatory issues, including (i) issuance of long-term bonds by banks; (ii) adequacy of present prudential credit exposure ceilings; (iii) review of prudential norms in respect of unsecured exposures; (iv) norms for declaration of dividend by public and private sector banks; and (v) review of the calendar of reviews placed before the boards of banks.

10.44 With a view to reinforcing this consultative process further and making the regulatory guidelines more user-friendly, a Users' Consultative Panel was constituted comprising representatives of the Indian Banks' Association (IBA), public sector, private sector and foreign banks and market participants. The panel provides feedback on regulatory instructions at the formulation stage to avoid ambiguities and operational glitches.

Supervisory Initiatives

10.45 Keeping in view the emerging scenario under the Basel II accord and the need to use supervisory resources more productively, a beginning towards risk-based supervision (RBS) of banks was made. The Risk-Based Supervision Manual (RBS Manual), customising the international best practices to Indian conditions, was finalised during the year. A pilot study of eight banks was taken up during the year, which was later extended to 15 additional banks. Extensive training was imparted to the Reserve Bank's supervision staff as also to the risk managers of various banks across the country. The review of the current methodology, based on the first pilot study, is under examination.

10.46 The scheme of Prompt Corrective Action (PCA), indicating 'structured' and 'discretionary' actions to be initiated by the Reserve Bank against banks

Box X.3

Computerisation of Banks - Aligning Technology Plan with Business Strategy

The Reserve Bank sponsored a study by the National Institute of Bank Management (NIBM), Pune to assess the computerisation in the banking system with a view to suggesting a broad methodology with which banks could smoothly integrate their technology plan with their business objectives. The report suggested a business-technology model termed as 'Enterprise Maturity Model' (EMM). It has five layers with defined business objectives at each layer starting with 'increasing operational efficiency' and leading up to higher strategic objectives such as 'maximising wealth and stakeholder value'. While every individual bank will need to chart its own course in integrating its business and technology plans, the NIBM report serves as a benchmark for banks to review the direction of their progress. The Reserve Bank advised banks which have not adopted core banking solutions to identify the level at which they are in the Enterprise Maturity Model and accordingly chart their future course of action with the approval of their boards.

which had hit the trigger points under the PCA framework, was introduced in 2002-03. Since the scheme was introduced on an experimental basis, banks that could potentially attract the provisions of the PCA framework were informed of the possible corrective action required to be taken in case the same were made applicable to them.

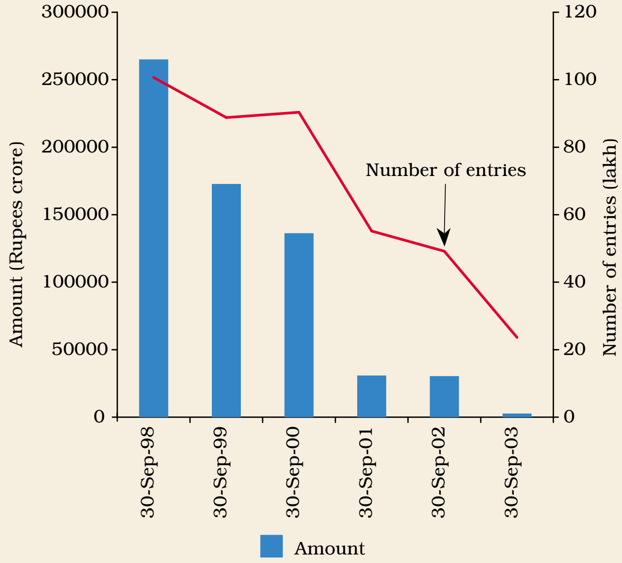
10.47 Frauds in banks reflect in most cases failure of well laid down systems and procedures, and the boards and the top management in banks need to view frauds with utmost seriousness. With a view to ensuring prompt reporting of frauds, a software package for fraud reporting and monitoring system was developed and supplied to all commercial banks. They were also advised to constitute a special board-level committee for monitoring and follow-up of cases of frauds involving Rs. one crore and above exclusively, while the audit committee of the board may continue to monitor all the cases of frauds in general.

10.48 A separate Fraud Monitoring Cell has been set up at the Reserve Bank to pay focused attention to the monitoring and follow-up of frauds in commercial banks, co-operative banks, financial institutions, NBFCs, local area banks and regional rural banks.

10.49 On an application by the Reserve Bank, the Central Government issued an Order of Moratorium in respect of Global Trust Bank (GTB) on July 24, 2004 in public interest, in the interest of depositors and the banking system. Keeping in view the need to minimise the period of moratorium, the available options and the synergies of strategic advantages in merging with Oriental Bank of Commerce (OBC), the Reserve Bank prepared a draft scheme of amalgamation of GTB with OBC and announced it on July 26, 2004 soon after both the banks, which are listed, had notified the information to the stock exchanges. After due sanction from the Central Government, the scheme came into force with effect from August 14, 2004 from which date customers, including depositors of GTB, were able to operate their accounts as customers of OBC.

10.50 The BFS took several steps to streamline the long outstanding entries under inter-branch accounts, balancing of books, reconciliation of inter-bank accounts (including *nostro* accounts) and clearing differences, especially in respect of public sector banks. While institution-specific action, as advised by the BFS, was taken, the time period allowed for reconciliation of accounts was also reduced from one year to six months with effect from March 31, 2004. On account of the initiatives taken by the BFS, the amount of outstanding entries under inter-branch accounts declined steadily (Chart X.1).

Chart X.1: Position of Reconciliation of Inter-branch Accounts



Co-operative Banks

10.51 Membership of co-operative credit institutions comprises largely lower and middle-income sections of society. UCBs are supervised by the Reserve Bank, while district central co-operative banks (DCCBs) and state co-operative banks are supervised by the NABARD. Both are regulated by the State Governments in respect of certain types of functions. In addition, multi-State UCBs are regulated by the Central Government. UCBs are concentrated in five states, *viz.*, Maharashtra, Gujarat, Karnataka, Andhra Pradesh and Tamil Nadu which account for 79 per cent of the urban co-operative banking sector and 90 per cent of deposit resources. The focus of supervision of urban co-operative banks by the Reserve Bank has been on strengthening the prudential norms, resolving the issue of dual control, addressing the lack of professionalism, use of unscientific loan policy and increasing incidence of financial weakness.

10.52 A system of gradation of UCBs, based on critical financial parameters, *viz.*, capital adequacy, net non-performing advances and profitability was introduced as a framework for initiating prompt corrective action. The gradation is communicated to problem banks to enable them to formulate action plans for corrective action. The content and structure of off-site surveillance returns were modified and the revised returns came into effect from the quarter ended March 2004 (Box X.4).

10.53 The period for recognition of loan impairment was reduced from 180 days to 90 days with effect from March 31, 2004 in line with the international best practice and to ensure greater transparency. Gold

Box X.4
Off-site Surveillance System for UCBs

The system of off-site surveillance, introduced in April 2001 under Section 27 (2) of the Banking Regulation Act, 1949 (As Applicable to Co-operative Societies), requires scheduled urban co-operative banks to submit returns to the Reserve Bank on a quarterly basis. The content and structure of OSS returns was modified to enlarge the breadth and depth of information obtained while reducing the volume of data submission. Seven quarterly returns (submitted from April 2004) and one annual return have been prescribed to obtain information on areas of supervisory concern, and at the same time, to strengthen MIS systems within the scheduled UCBs and sensitise their managements about the prudential concerns of the supervisory authority. The OSS is proposed to be extended to non-scheduled UCBs with a deposit base of Rs.100 crore and above and thereafter to other UCBs. A project is underway for development of software for UCBs that would assist them in preparation and submission of all the regulatory and supervisory returns including OSS returns in an electronic format.

loans and small loans up to Rs. one lakh, however, continue to be governed by the 180-day impairment norm. The Registrars of Co-operative Societies of all States were advised to issue suitable instructions enabling UCBs to take recourse to the SARFAESI Act for recovery of NPAs. UCBs were also advised to build up Investment Fluctuation Reserves (IFR) out of realised gains on sale of investments of a minimum of 5 per cent of the investment portfolio within a period of 5 years, subject to available net profit, in order to mitigate interest rate risk.

10.54 It was observed by the BFS that some of the large UCBs are facing serious problems with regard to solvency and liquidity. The State Governments concerned were advised to infuse capital funds to ensure that the banks attain the minimum CRAR level.

10.55 In pursuance of the recommendations of the Joint Parliamentary Committee (JPC) on Stock Market Scam and Matters relating thereto, a complete ban was imposed on granting of loans and advances to the directors and their relatives or the concerns in which they are interested, with effect from October 1, 2003. Only UCBs with strong financials are allowed to declare dividend.

10.56 The Reserve Bank is concerned with the existence of a large number of financially weak UCBs, some of which are unlicensed. As some UCBs have faced problems of liquidity and solvency in recent years, a scheme of reconstruction was approved by the Reserve Bank in respect of two scheduled UCBs in exceptional circumstances which, *inter alia*, require payment of insured deposits by the DICGC. However, the Reconstruction Scheme has not yielded the desired results. Therefore, in the light of experience gained, the Reserve Bank decided that it would only consider a scheme of reconstruction which envisages recapitalisation by the stakeholders, *viz*., the shareholders/co-operative institutions/Government to the extent of achieving the prescribed capital adequacy norms, without infusion of liquidity through settlement of insurance claims by the Deposit Insurance and Credit Guarantee Corporation (DICGC). Furthermore, the scheme should lay a clear road map for reducing the NPA level to a tolerable limit within the stipulated time frame.

10.57 In order to examine new applications for licence by proposed UCBs, the Reserve Bank constituted a Screening Committee consisting of eminent experts. In the light of experience gained, the policy of licensing co-operative banks was revised and it was decided to consider applications for licence of UCBs only after a comprehensive policy, including an appropriate legal and regulatory framework for the sector, is put in place and a policy for improving the financial health of the urban co-operative banking sector is formulated.

10.58 Scheduled UCBs with a minimum net worth of Rs.100 crore and complying with the exposure norms and connected lending were allowed to act as corporate agents for undertaking insurance business without risk participation, after obtaining the approval of the Reserve Bank.

10.59 The Central Government had enacted a Multi-State Co-operative Societies (MSCS) Act, 2002 by repealing the MSCS Act, 1984. The MSCS Act, 2002 does not contain provisions empowering the Reserve Bank on matters relating to supercession of boards of UCBs, which is one of the pre-requisites for banks to have deposit insurance cover of the DICGC in terms of Section 2(gg) of the DICGC Act, 1961. Therefore, deposits of UCBs registered under the MSCS Act, 2002 lose insurance cover of the DICGC.

10.60 The Supreme Court, in its judgement in a case relating to the Apex Urban Co-operative Bank of Maharashtra and Goa Limited, Mumbai in October 2003 ruled that the UCBs registered under the MSCS Act, 2002 do not fall within the meaning of 'primary co-operative bank' as defined under the Banking Regulation Act, 1949. In order to rectify the deficiencies, the Reserve Bank has suggested to the Government amendments in the BR Act, 1949 and the DICGC Act, 1961 with the objective of bringing all UCBs registered under the MSCS Act, 2002 under the BR Act, 1949 and extend deposit insurance cover of the DICGC.

10.61 In 2003-04, licence applications of two DCCBs were rejected by the Reserve Bank in view of their precarious financial position. Besides, show cause notices were issued to 3 DCCBs as to why their licence applications should not be rejected. As on June 30, 2004 seven DCCBs were placed under the Reserve Bank's directions prohibiting them from granting any loans and advances and/or accepting fresh deposits.

Development Finance Institutions (DFIs)

10.62 With the change in the operating environment, DFIs have been facing difficulties in sustaining their operations. Several policy initiatives have been taken to facilitate the process of transition of DFIs opting for conversion into banks through a series of measures aimed at financial restructuring, provision of regulatory relaxation for restructured investments of creditor banks or providing Government support, transfer of stressed assets of DFIs to asset reconstruction companies/asset management trusts for managing the NPA level and harmonisation of prudential norms between banks and DFIs.

10.63 A Working Group on DFIs (Chairman : Shri N. Sadasivan) was set up by the Reserve Bank. The Working Group, which submitted its Report in May 2004, has suggested a road map for development financing and the future role of DFIs (Box X.5).

Strengthening of Prudential Norms

10.64 DFIs were advised that, with effect from end-March 2006, an asset should be classified as non-performing if the interest and/or instalment of principal remain overdue for more than 90 days. DFIs would have the option to phase out the additional provisioning required for moving over to the 90-day income recognition norm over a period of three years beginning from the year ending March 31, 2006, subject to at least one fourth of the additional provisioning being made in each year. Guidelines provided to banks to prevent the slippage of accounts in the 'sub-standard' category to the 'doubtful' category were extended to DFIs as well. They were advised to place the guidelines before their boards of directors and take appropriate actions for implementing the recommended measures. As in the case of banks, "special mention" accounts,

Box X.5
Report of the Working Group on Development Financial Institutions

The major recommendations of the Group are set out below:

- Banks may be encouraged to extend high risk project finance with suitable Government support.
- As a market-driven business model of any DFI is inherently unsustainable, a detailed social cost benefit analysis should identify activities which require development financing. The rest of the DFIs must convert to either a bank or a NBFC, as recommended by the Narasimham Committee.
- Concessions in the form of according "approved investment" status to paper issued and a lower risk weight of 20 per cent allowed for exposure by banks, DFIs, NBFCs and RNBCs should be withdrawn for public financial institutions, as many of them have become financially weak and act without any assurance of Government support.
- DFIs which convert into banks could be accorded certain exemptions/relaxations for a period of 3-5 years after conversion.
- Regulation of DFIs should ensure that overall systemic stability is not endangered.
- The Reserve Bank should continue to regulate the Exim Bank, NABARD, SIDBI and NHB which would continue to function as DFIs. As there is a scope for conflict of interest, the Reserve Bank may divest its ownership in NABARD and NHB.
- The Reserve Bank may ensure that the standards of regulation and/or supervision exercised by NHB (in case of Housing Finance Companies), SIDBI (SFCs and SIDCs) and NABARD (state co-operative banks, district central co-operative banks and RRBs) are broadly at par with those maintained by the Reserve Bank.
- DFIs which have been constituted as companies and are performing developmental roles should be classified as a new category of NBFCs called 'Development Financial Companies' (DFCs) and subjected to uniform regulation. Considering the nature of business of development financing, DFCs may be permitted to maintain 9 per cent CRAR as against 15 per cent prescribed for NBFCs in general.
- Public deposit mobilisation by RNBCs should be capped at 16 times the net owned fund (NOF) as an initial measure and finally to the level for other NBFCs in five years. This should be accompanied by deregulation in the quantitative restrictions (alongside more stringent quality criteria) on the asset side.

Reference

Reserve Bank of India (2004), *Report of the Working Group on Development Financial Institutions*, May.

which would track potentially weak accounts, would only be for internal control and follow-up purposes and would not constitute an additional category under the extant asset classification norms.

10.65 In December 1998, DFIs were advised that their investments in the bonds/debentures of certain Public Financial Institutions (PFIs) would attract a uniform risk weight of 20 per cent. In the Annual Policy Statement for the year 2004-05, it was announced that with effect from April 1, 2005 exposures to all PFIs will attract a risk weight of 100 per cent. In terms of the guidelines provided in January 2004, FIs must not, *inter alia*, invest in unrated debt securities or in debt securities of original maturity of less than one year other than CP and CDs, effective April 1, 2004. All fresh investments in debt securities are required to be made only in listed debt securities.

Transformation into Banks

10.66 During 2003-04, the Industrial Development Bank (Transfer of Undertaking and Repeal) Act, 2003 was passed by the Parliament and received assent of the President of India on December 30, 2003. In terms of the provisions of the Act, the undertaking of Industrial Development Bank of India (IDBI) would vest in the company named Industrial Development Bank of India Limited, which has to be incorporated as a Company under the Companies Act, 1956. On the 'Appointed Date', the new company would assume all assets and liabilities of IDBI. In this regard, the Government of India has already approved the IDBI's proposal to set up a Stressed Asset Stabilisation Fund (SASF) wherein stressed assets of IDBI amounting to Rs.9,000 crore would be transferred to the SASF against transfer of an equivalent amount of 20-year maturity bonds issued by the Central Government in favour of the SASF on cash/fisc neutral basis.

10.67 The Board of Directors of the IFCI Limited approved, in principle, a merger with a bank. The Central Government has already decided to take over certain liabilities of the IFCI and correspondingly the Reserve Bank has provided certain regulatory relaxations for restructured liabilities of the IFCI.

10.68 While sending the inspection reports of the IDBI, the IFCI and Industrial Investment Bank of India (IIBI) Limited, action was taken on the various directives given by the BFS that included conveying the concerns on IIBI to the Government.

Consolidated Accounting and Consolidated Supervision

10.69 Guidelines on consolidated accounting and consolidated supervision, which were prescribed for banks, were extended to DFIs as well, effective April 1, 2003 (July 1, 2003 in the case of the NHB). They comprise three components in the supervisory framework, *viz.*, (i) consolidated financial statements (CFS); (ii) consolidated prudential returns (CPR); and (iii) application of prudential regulations such as capital adequacy, large exposures and liquidity gaps on group-wide basis in addition to the solo prudential norms applicable to the parent DFIs/subsidiaries. The publication of the CFS as per the Accounting Standard (AS) 21 of the Institute of Chartered Accountants of India (ICAI) is mandatory for the listed FIs in terms of the Listing Agreement with the Stock Exchanges. The Reserve Bank's guidelines sought to make such publication mandatory even for the non-listed DFIs from the financial year beginning April 1, 2003.

Non-Banking Financial Companies (NBFCs)

10.70 The policy initiatives in respect of NBFCs related to measures for protecting depositors, aligning interest rates offered by NBFCs with those of banks in respect of NRI deposits on a repatriable basis, issuance of KYC guidelines and allowing diversification into insurance business.

10.71 The maximum rate of interest that NBFCs (including *Nidhi* companies and Chit Fund companies) could pay on their public deposits was reduced from 12.5 per cent per annum to 11.0 per cent per annum with effect from March 4, 2003 in line with the general softening of interest rates. Similarly, the minimum rate of interest payable by the Residuary Non-Banking Companies (RNBCs) was reduced from 4 per cent per annum to 3.5 per cent per annum on daily deposit schemes and from 6 per cent per annum to 5 per cent per annum on other types of deposits. The rate of interest which NBFCs and Miscellaneous Non-Banking Companies (MNBCs) could pay on NRI deposits was also aligned with that payable by scheduled commercial banks on such deposits. It was clarified that NBFCs were not allowed to accept such deposits for a period less than one year (with a maximum period of three years).

10.72 NBFCs were allowed to take up insurance agency business for a fee on a non-risk participation basis without the approval of the Reserve Bank, subject to certain conditions. NBFCs intending to set up joint ventures in insurance with equity contribution on a risk participation basis or making investments in the insurance companies would continue to obtain prior approval as envisaged in the guidelines issued on June 9, 2000.

10.73 The KYC guidelines, akin to those issued for commercial banks, were prescribed for NBFCs, including MNBCs (Chit Fund Companies) and RNBCs in January 2004.

10.74 The inspection policy of NBFCs was revised in July 2003 to increase the frequency. Inspections of 460 deposit taking companies and 385 non-deposit taking companies as also scrutiny and *ad hoc* scrutiny of books of accounts of 568 companies were carried out. Important findings of inspection and scrutiny reports were placed before the BFS.

10.75 An Internal Group in the Reserve Bank examined the scope of providing insurance cover to depositors of NBFCs on a suggestion made by the Joint Parliamentary Committee (JPC) on Stock Market Scam and Matters Relating Thereto. The Group did not favour extending deposit insurance to NBFCs in view of high risks and inadequate compliance with the regulatory and supervisory framework. These recommendations were endorsed by an external group.

10.76 The Reserve Bank issued final guidelines and directions to Securitisation Companies and Reconstruction Companies on April 23, 2003 relating to registration, owned funds, permissible business, operational structure for giving effect to the business of securitisation and asset reconstruction, deployment of surplus funds, internal control system, prudential norms and disclosure requirements. In order to ensure that the size of capital has some relationship to the value of assets acquired by the securitisation company or reconstruction company, the Reserve Bank in March 2004 issued a notification whereby the minimum owned funds for commencing the business of securitisation or asset reconstruction has been stipulated at an amount not less than 15 per cent of the total financial assets acquired or to be acquired by the securitisation company or reconstruction company on an aggregate basis or Rs.100 crore, whichever is lower. This stipulation is irrespective of whether the assets are transferred to a trust set up for the purpose of securitisation or not. However, the provisions relating to maintaining a capital adequacy ratio which shall not be less than 15 per cent of the total risk weighted assets of the securitisation company or reconstruction company on an ongoing basis, shall continue to be applicable.

10.77 In June 2004, the Reserve Bank rationalised the investment pattern of RNBCs for imparting greater liquidity and safety to their investments, enhancing the protection available to the depositors and reducing the overall systemic risk (Box X.6).

Box X.6

Residuary Non-Banking Companies (RNBCs)

A Residuary Non-Banking Company (RNBC) is a non-banking financial company which, as its principal business, is engaged in collecting deposits under any scheme or arrangement and cannot be placed in any one of the defined categories of NBFC, *i.e.,* leasing company, hire purchase finance company, loan company or investment company. At present, there are four companies registered under Section 45 IA of the RBI Act, 1934 which operate as RNBCs. Aggregate deposits of these companies stood at Rs.15,062 crore as on March 31, 2003, constituting 74.9 per cent of aggregate deposits of all NBFCs. Two large RNBCs account for deposits aggregating Rs.15,058 crore, constituting 99.9 per cent of the deposits with all RNBCs and 77.3 per cent of public deposits of all NBFCs.

RNBCs are required to invest not less than 80 per cent of the aggregate liabilities to the depositors (ALD) in the manner prescribed by the Reserve Bank which include Government securities, Government guaranteed bonds, fixed deposits with scheduled commercial banks, debentures of public financial institutions, commercial paper (CP) issued by companies and units of mutual funds, within certain limits.

The Reserve Bank recently reviewed the current regulations relating to investments by RNBCs. Modifications include stipulation of minimum rating, exposure norms and an increase in investment in government securities as set out below:

- RNBCs should invest only in (i) the fixed deposits and CDs of scheduled commercial banks; and (ii) CDs of specified financial institutions provided such CDs are rated not less than AA+ or its equivalent by an approved credit rating agency, with exposure to a scheduled commercial bank not exceeding 1 per cent of the aggregate deposit liabilities of the bank as on March 31 of the previous accounting year and exposure to any one specified DFI not exceeding 1 per cent of the ALD.
- RNBCs should invest in the Central and State Government securities issued by the Governments in the course of their market borrowing programme an amount which shall not be less than 15 per cent of the outstanding ALD.
- Investment in debt securities should be confined to those having minimum AA+ or equivalent grade rating and listed in any one of the stock exchanges.
- The investment in units of mutual funds should be in only debt-oriented mutual funds, subject to the aggregate investment in mutual funds not exceeding 10 per cent and in any one mutual fund not exceeding 2 per cent of ALD.
- Effective April 1, 2005, RNBCs will be permitted to invest, as per their discretion, only 10 per cent of the ALD as at the second preceding quarter or up to their net owned funds (NOF), whichever is lower. Effective April 1, 2006 the discretionary investment limit would stand abolished.

10.78 The Reserve Bank directed that the NBFCs which were granted Certificates of Registration (CoR) in the non-public deposit taking category should meet the minimum capital requirements of Rs.200 lakh to be eligible to apply to the Reserve Bank for accepting public deposits. Accordingly, NBFCs registered in the non-deposit taking category were advised to ensure compliance with this requirement before applying to the Reserve Bank for approval to accept public deposits.

10.79 During the year under review, the Reserve Bank cancelled CoR of twenty NBFCs for reasons other than conversion from category ‘A’ (deposit accepting NBFCs) to category ‘B’(non-deposit accepting NBFCs). The Reserve Bank launched prosecution proceedings against 63 companies so far and winding up petitions have been filed with the courts in respect of 71 companies.

MACRO-PRUDENTIAL INDICATORS REVIEW

10.80 Macro-prudential indicators (MPIs), which comprise both aggregated micro-prudential indicators of the health of individual financial institutions (FIs) and macroeconomic variables associated with financial system soundness, are a useful tool to assess the health and stability of the financial system. The Reserve Bank has been compiling MPIs from March 2000 onwards. Over the last few years, the compilation exercise has been refined in consonance with the methodology given by the International Monetary Fund (IMF). In the Annual Policy Statement for 2004-05, it was indicated that the salient features of the MPI review would be published on an annual basis. Accordingly, the MPI review for the year 2003-04 is set out below.

Capital Adequacy

10.81 The capital position of financial intermediaries was generally above the minimum requirement (Table 10.2). The core capital ratio of banks showed some decline during 2003-04. The Capital to Risk-weighted Assets Ratio (CRAR) of the majority of banks as also major bank groups was well above the regulatory stipulation, except for two banks (Tables 10.3 and 10.4). This should enable the meeting of requirements relating to the capital charge for market risk and provisioning for doubtful assets as announced in the Policy Statement. Tier I capital of scheduled UCBs also recorded an improvement, in absolute terms, partly because of the liquidation of two banks with negative net worth, inclusion of one bank in the scheduled category and the attainment of 9 per cent CRAR level by some banks (Table 10.5).

10.82 In the case of DFIs, although the aggregated CRAR was high, the erosion of capital of two large Government-owned DFIs due to the high level of NPAs resulted in negative CRAR in respect of these institutions (Table 10.6). The average aggregate

Table 10.2: Select Financial Indicators

(per cent)

Item	Year	Scheduled Commercial Banks	DFIs	PDs	NBFCs
1	2	3	4	5	6
CRAR	2003	12.7	22.4	29.8	21.9
	2004	13.0	22.0	42.7	19.2
Gross NPAs to Gross Advances	2003	8.8	14.3	n.a.	8.8
	2004	7.3	16.4	n.a.	8.6
Net NPAs to Net Advances	2003	4.5	9.7	n.a.	2.7
	2004	3.0	10.5	n.a.	2.6
Return on Total Assets	2003	1.0	0.9	6.6	1.4
	2004	1.2	-0.2	5.9	n.a.
Return on Equity	2003	17.5	4.1	24.1	10.4
	2004	19.8	-1.2	19.9	n.a.
Cost/Income Ratio	2003	48.3	11.8	13.6	67.1
	2004	45.7	26.1	16.9	n.a.

n.a. : Not available.

Note : 1. Data for March 2004 are provisional.
2. Data for 2004 in respect of NBFCs pertain to the period ended September 2003.
3. Data for scheduled commercial banks pertain to domestic operations only and may not tally with the balance sheet data.

Table 10.3: Scheduled Commercial Banks – Performance Indicators

(Per cent)

Item / Bank Group	2004-05	2003-04				2002-03			
	Q1	Q4	Q3	Q2	Q1	Q4	Q3	Q2	Q1
1	2	3	4	5	6	7	8	9	10
Operating Expenses/Total Assets*									
Scheduled Commercial Banks	2.3	2.1	2.3	2.3	2.2	2.3	2.2	2.3	2.2
Public Sector Banks	2.2	2.2	2.2	2.3	2.2	2.4	2.2	2.3	2.3
Old Private Sector Banks	2.1	1.6	2.1	2.2	2.0	1.9	2.1	2.1	2.0
New Private Sector Banks	2.3	1.7	2.0	2.3	2.2	1.8	2.1	2.0	1.9
Foreign Banks	2.9	2.4	3.3	2.7	2.6	2.7	2.9	2.9	2.7
Net Interest Income/Total Assets*									
Scheduled Commercial Banks	3.1	2.5	3.1	2.9	3.1	2.6	2.8	2.9	2.9
Public Sector Banks	3.1	2.8	3.2	3.0	3.2	2.8	2.9	3.1	3.0
Old Private Sector Banks	2.9	1.9	2.8	2.7	2.7	2.0	2.8	2.4	2.6
New Private Sector Banks	2.4	1.5	2.1	2.1	2.0	1.6	1.7	1.5	1.7
Foreign Banks	3.7	3.0	3.8	3.0	4.0	2.7	3.6	3.6	3.5
Net Profit/Total Assets*									
Scheduled Commercial Banks	1.2	1.0	1.2	1.3	1.3	0.9	1.2	1.0	1.0
Public Sector Banks	1.2	1.1	1.2	1.2	1.2	0.9	1.1	0.9	0.9
Old Private Sector Banks	0.9	0.2	1.5	1.5	1.6	0.7	1.6	1.1	1.2
New Private Sector Banks	1.2	0.6	1.3	1.4	1.2	0.3	1.2	1.0	1.0
Foreign Banks	1.8	1.4	0.9	1.8	2.5	2.0	1.5	1.3	1.5
Gross NPAs to Gross Advances**									
Scheduled Commercial Banks	7.3	7.3	9.3	9.7	9.8	8.8	10.9	11.1	11.2
Public Sector Banks	8.1	8.1	9.6	10.0	10.2	9.4	11.2	11.6	11.6
Old Private Sector Banks	7.9	7.7	10.1	10.1	9.8	8.9	12.5	12.8	12.3
New Private Sector Banks	3.9	4.8	9.6	10.4	10.4	7.6	11.4	11.3	11.3
Foreign Banks	4.7	4.9	5.2	5.3	5.4	5.2	5.6	5.5	5.6
Net NPAs to Net Advances**									
Scheduled Commercial Banks	2.8	3.0	3.7	4.0	4.6	4.5	5.1	5.5	5.7
Public Sector Banks	3.0	3.1	3.6	4.0	4.7	4.7	5.2	5.8	6.0
Old Private Sector Banks	3.8	3.9	5.7	6.1	6.2	5.8	7.8	8.3	8.1
New Private Sector Banks	1.8	2.4	4.0	4.4	4.6	4.5	5.1	5.0	5.2
Foreign Banks	1.4	1.5	1.3	1.5	1.7	1.7	2.0	1.9	1.9
CRAR**									
Scheduled Commercial Banks	13.7	13.0	13.5	13.2	13.0	12.7	12.8	12.5	12.3
Public Sector Banks	13.5	13.2	13.8	13.3	13.0	12.6	12.6	12.3	11.9
Old Private Sector Banks	14.3	13.7	15.0	14.4	13.5	12.8	13.4	13.1	13.3
New Private Sector Banks	13.7	10.6	11.2	11.3	11.3	11.3	12.8	12.6	12.9
Foreign Banks	14.7	15.0	14.8	14.9	14.7	15.2	13.5	13.0	13.2

* : Annualised to ensure comparability between quarters. ** : Position as at the end of the quarter.

Note : Data for March and June 2004 are provisional.

Source : DSB returns submitted by banks covering domestic operations.

capital ratio in respect of NBFCs remained well above the regulatory minimum of 12 per cent (Chart X.2). The number of NBFCs not complying with the regulatory stipulation has shown a declining trend. The CRAR of primary dealers (PDs) also recorded a significant improvement.

Asset Quality

10.83 A sharp decline in the gross and net NPAs of scheduled commercial banks, in spite of the change over to 90-day delinquency norm, reflects the impact of various initiatives undertaken for resolution of NPAs (Table 10.7). Similarly, the net NPA to capital

Table 10.4: Frequency Distribution of CRAR (end-March 2004 P)

Bank Group	Negative	Between 0 and 9 per cent	Between 9 and 10 per cent	Between 10 and 15 per cent	15 per cent and above	Total
1	2	3	4	5	6	7
Public Sector Banks						
SBI Group	0	0	0	8	0	8
	(0)	(0)	(0)	(8)	(0)	(8)
Nationalised Banks	0	0	1	16	2	19
	(0)	(0)	(1)	(16)	(2)	(19)
Private Sector Banks						
Old Private Sector Banks	0	0	0	12	8	20
	(0)	(0)	(3)	(13)	(5)	(21)
New Private Sector Banks	1	1	0	7	1	10
	(1)	(1)	(1)	(5)	(1)	(9)
Foreign Banks	0	0	0	8	25	33
	(0)	(0)	(0)	(8)	(28)	(36)
All Banks	1	1	1	51	36	90
	(1)	(1)	(5)	(50)	(36)	(93)

P : Provisional.
Note: Figures in parentheses relate to March 2003.

ratio, which is a worst-case scenario measure, steadily declined between end-March 2003 and end-March 2004.

Table 10.5: Key Financial Indicators of Scheduled UCBs

(Amount in Rupees crore)

Indicator	March 2004	March 2003	Percentage variation
1	2	3	4
Number of Scheduled UCBs	55	56	
Paid up capital	707	608	16.1
Reserves (excluding loan loss provisions)	2,488	2,195	13.4
Tier I capital	297	-10	
Tier II capital	529	434	21.7
Deposits	39,305	36,024	9.1
Investment in Government and other approved securities	13,954	10,806	29.1
Loans and Advances	23,962	22,941	4.5
Gross NPAs	6,892	6,927	-0.5
Net NPAs	3,509	3,827	-8.3
Net Profit#	497	354	40.4
Net Loss*	101	326	-69.1
Accumulated Losses	2,320	2,276	2.0
Memo items : Ratios (in per cent)			
Gross NPAs as percentage of gross advances	28.8	30.2	
Net NPAs as percentage of net advances	17.1	19.3	

: Relates to 47 banks in March 2003 and 50 banks in March 2004.
* : Relates to 9 banks in March 2003 and 5 banks in March 2004.
Note : Data as on March 31, 2004 are unaudited and provisional.

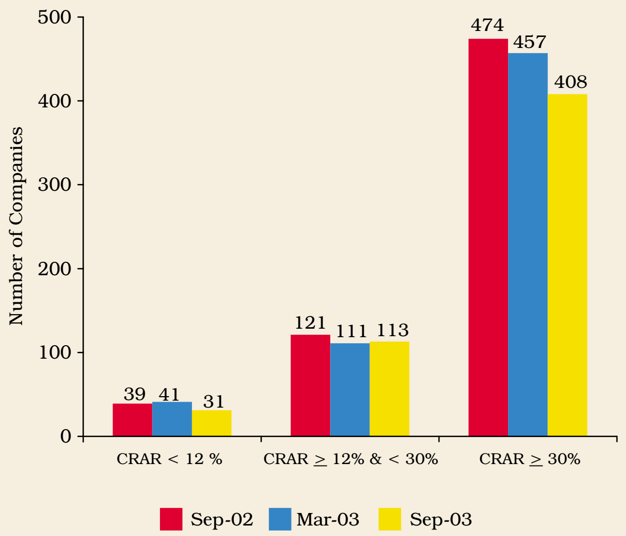
10.84 A large concentration of credit in a few sectors is an indicator of vulnerability since the lending institutions are exposed to the heightened credit risk, especially in the downturn phase of the business cycle. Data on sector-wise deployment of gross bank credit by 48 major banks showed that the share of food credit declined. The share of credit to the priority sector remained more or less unchanged up to September 2002 before increasing gradually,

Table 10.6: CRAR and Net NPAs of Select FIs (end-March 2004)

Financial Institution	CRAR (Per cent)	Net NPAs (Rupees crore)	Net NPAs to net loans (Per cent)
1	2	3	4
Term-Lending Institutions (TLIs)			
IDBI	18.3	8,693	21.1
IFCI	-12.8	4,177	34.1
EXIM Bank	23.5	129	1.3
IIBI	-18.1	703	52.1
TFCI	23.1	145	21.2
IDFC	37.0	0	0.0
All TLIs	**14.2**	**13,847**	**19.8**
Refinancing Institutions (RFIs)			
NABARD	39.1	1	0.0
NHB	29.4	63	1.0
SIDBI	53.8	226	2.4
All RFIs	41.8	290	0.5
All FIs	22.0	14,137	10.5

Source : Off-site returns submitted by FIs.

Chart X.2: Frequency Distribution of CRAR - Number of Reporting NBFCs



reflecting the broadening of the definition of the priority sector over the period. The share of 'other sectors' recorded a steady increase, mainly due to

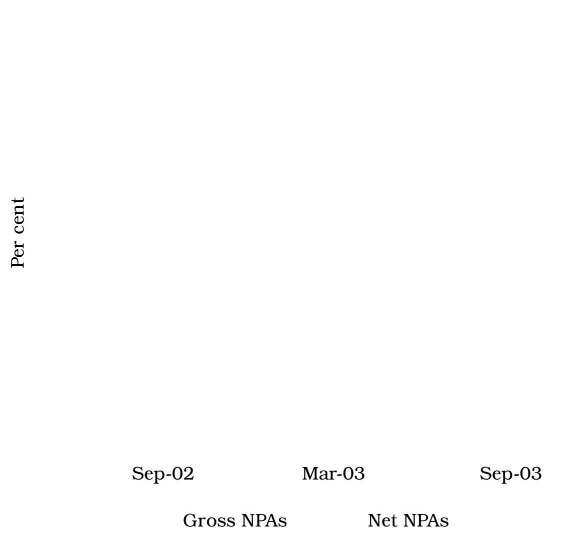
Table 10.7: Net NPAs to Net Advances of Scheduled Commercial Banks

(Frequency Distribution)

Year	Public Sector Banks		Private Sector Banks		
	SBI Group	Nationalised Banks	Old	New	Foreign Banks
1	2	3	4	5	6
1996-97					
Up to 10 per cent	5	12	22	9	36
Above 10 per cent and up to 20 per cent	3	6	3	–	1
Above 20 per cent	–	1	–	–	2
2000-01					
Up to 10 per cent	8	14	16	8	31
Above 10 per cent and up to 20 per cent	–	5	4	–	6
Above 20 per cent	–	–	3	–	5
2001-02					
Up to 10 per cent	8	16	17	8	25
Above 10 per cent and up to 20 per cent	–	3	3	–	5
Above 20 per cent	–	–	3	–	9
2002-03					
Up to 10 per cent	8	17	19	8	28
Above 10 per cent and up to 20 per cent	–	2	1	1	4
Above 20 per cent	–	–	1	0	4
2003-04 P					
Up to 10 per cent	8	18	18	9	27
Above 10 per cent and up to 20 per cent	0	1	2	0	2
Above 20 per cent	0	0	0	1	4

P : Provisional.

Chart X.3 : Ratio of Non-Performing Assets to Credit Exposure - NBFCs



the growth in the housing and retail sectors. Industry-wise data showed a steady increase in share of credit to infrastructure industries. The share of engineering industries, however, declined steadily.

10.85 The asset quality of DFIs as a group has been deteriorating due to very high NPA ratios in respect of two DFIs. NPA ratios were low in respect of NBFCs (Chart X.3).

Earnings and Profitability Indicators

10.86 The earnings and profitability indicators for the financial system as a whole were positive, except in the case of DFIs. The return on total assets (ROA) in respect of DFIs was negative, reflecting persistent losses combined with limited recourse to low cost funds. Although the ROA of the PDs declined marginally due to increased volatility in securities market, it was still high. The ROA of scheduled commercial banks has been improving steadily even after making substantial provisions. Continued higher income from securities trading, profits from foreign exchange operations and decline in interest expenses are some of the reasons for the buoyancy in banks' profitability. The return on equity (ROE) of the commercial banking system remained high which augurs well for their efforts towards raising capital from the market.

10.87 The operating costs of banks witnessed an increase during April-September 2003, due to increases in staff costs and other operating expenses as a percentage to income. However, the cost income

Table 10.8: Operational Results of Scheduled Commercial Banks - Key Ratios

(Per cent)

Ratio to Total Assets	2003-04	2002-03
1	2	3
Earnings before Provisions and Taxes (EBPT)	2.70	2.43
Profit after Tax	1.18	1.01
Total Income	9.48	10.29
Interest Income	7.41	8.39
Non-Interest Income	2.07	1.91
Total Expenditure	6.76	7.86
Interest Expenses	4.52	5.59
Operating Expenses	2.24	2.27
Provisions and Contingencies	1.53	1.42

Note : Data are provisional and relate to domestic operations only.

ratio (ratio of operating expenses to total income net of interest expended) declined, reflecting improved efficiency. While containment of such costs is imperative to sustaining improved profitability, the impending wage revision in the financial sector may put pressure on its operating costs in the near future.

10.88 A sharp improvement in the commercial banks' bottomline was due, in large part, to the treasury profits which were fuelled by the decline in interest rates and profit-booking on sale of Government securities. These sources of profits may not be sustained in the future. Banks' earning capacity would increasingly depend on other sources such as interest earned from lending operations and fee-based business (Tables 10.8 and 10.9).

Sensitivity to Market Risk

Interest Rate Risk

10.89 Given the significant share of investments in Government securities in the assets of commercial banks, the interest rate sensitivity of their balance sheets is critical. The Reserve Bank, therefore, conducts periodic sensitivity analyses of banks' balance sheets.

Currency Risk

10.90 An appreciation in the rupee *vis-à-vis* the US dollar, combined with soft global interest rates during 2003-04, led to increased recourse to external commercial borrowings as also increased borrowings in foreign currency from the domestic banks. The foreign currency positions of importers and other corporates going in for such borrowings have, however, remained largely unhedged. Banks have, therefore, been sensitised to the need to assess the foreign currency risk of their borrowers spilling over to the credit risk.

Commodity Risk

10.91 Banks in India generally do not trade in commodities. Certain banks have, however, been allowed to trade in precious metals and in gold derivatives subject to fulfilment of certain prudential norms. The exposure of the banking system to precious metals is insignificant and is not a cause of systemic concern.

Table 10.9: Operational Results of Scheduled Commercial Banks – 2003-04

(Number of banks showing increase in ratios during the year)

Ratio to Total Assets	Public Sector Banks		Private Sector Banks		Foreign Banks	All Banks
	SBI Group	Nationalised Banks	Old	New		
1	2	3	4	5	6	7
Earnings before Provisions and Taxes (EBPT)	7	16	8	3	19	53
Profit after Tax	7	15	11	6	22	61
Total Income	1	0	3	0	5	9
Interest Income	0	0	1	0	5	6
Non-Interest Income	7	15	6	1	15	44
Total Expenditure	0	1	1	0	4	6
Interest Expenses	0	0	0	0	3	3
Operating Expenses	3	5	9	6	12	35
Provisions and Contingencies	7	14	7	5	17	50

Note : Data are provisional and relate to domestic operations only.

Equity Risk

10.92 Banks' exposure to the capital market at 1.8 per cent of total advances at end-March 2004 was well below the stipulated ceiling of 5 per cent. Some new private sector banks have exposures close to the limit prescribed.

Liquidity

10.93 The ratio of liquid assets to total assets of banks declined to 42.6 per cent at end-March 2004 from 44.2 per cent at end-September 2003. This was indicative of the increased credit offtake from the banking system during the last half year.

10.94 MPIs also include key indicators of the global economic outlook, prospects for the domestic economy, financial markets, corporate profitability and credit offtake. These have been covered extensively elsewhere in the Report. Besides, exposure of banks to retail credit has also assumed considerable significance as an MPI, which is covered in Section III.

10.95 To sum up, the response of the financial sector to the Reserve Bank's initiatives has been encouraging. This has resulted in improvement in key banking parameters, especially in increased capital adequacy and reduced net NPA ratios. The improved macroeconomic outlook and the pick-up in industrial activity have also resulted in an improved credit offtake. The financial sector has acquired greater strength, efficiency and stability. The performance of the banking sector is noteworthy considering the legacy of past NPAs and progressive tightening of prudential norms. Overall rigidity in lending rates as well as inadequacy in quality of service to some sections continue to be matters of concern.

Outlook

10.96 The process of financial liberalisation has exposed financial institutions to a wide range of market risks than before. This has necessitated an ongoing restructuring of the regulatory framework, adaptation to the changing landscape of the financial system and a continuous sharpening of the focus of monitoring. Furthermore, recent events have brought issues relating to corporate governance and internal control systems to the centre-stage of the responsibility for financial stability. It also calls for watchfulness among all stakeholders.

10.97 The Reserve Bank would continue to strengthen its supervisory initiatives. Risk-based supervision and the PCA framework would be strengthened further. Consolidated supervision would be complemented by a supervisory framework for financial conglomerates. Regulators and regulated entities would have to enhance their risk detection and management systems in order to prepare themselves for the eventual adoption of the new capital adequacy norms under the Basel II process. The improvement in the asset quality in spite of the adoption of the 90-day delinquency norm is indeed a noteworthy development. The Reserve Bank would continue to ensure a sustained reduction in the non-performing assets to levels comparable with those of industrial countries and even below.

XI PUBLIC DEBT MANAGEMENT

11.1 The conduct of public debt management by the Reserve Bank in 2003-04 was marked by significant gains in terms of its objectives of minimisation of cost and elongation of maturity profile for limiting the rollover risk. Lower net market borrowings by the Central Government considerably strengthened debt management operations in an environment characterised by large capital inflows, easy liquidity and generally stable inflation expectations. Innovative efforts were directed towards restructuring and consolidating States' debt and lowering the debt servicing burden. The borrowing programme of the Central Government was completed successfully in 2003-04 without any devolvement on the Reserve Bank for the first time since the introduction of auctions in primary issuances in 1992-93. Market borrowings by the States also elicited good response.

11.2 The review of debt management operations in 2003-04 presented in this Section indicates distinct progress in ensuring the sustainability of public debt. At the level of the Centre, the review underscores a noteworthy turnaround from Ways and Means Advances (WMA)/overdrafts to surplus cash balances and investments, a strong appetite for Treasury Bills which became an effective instrument for absorbing excess liquidity in the system, a softening of yields on dated securities and elongation of maturities, including that of States' debt. Strategies for debt consolidation, which included debt buyback from the banking system and prepayment of external debt, were aimed at replacing high cost debt. As regards State finances, debt swaps with the Centre have provided headroom to the States in terms of lower debt service. Structural reforms of State finances, however, continue to hold the key to a sustainable level of indebtedness.

CENTRAL GOVERNMENT

Ways and Means Advances

11.3 The Ways and Means Advance (WMA) limits of the Centre were kept unchanged at Rs.10,000 crore for the first half (April-September) and Rs.6,000 crore for the second half (October-March) of 2003-04. The Central Government was in overdraft for only 43 days and on 10 occasions during the year (Table 11.1). A noteworthy development was the absence of recourse to WMA in the second half of the year, which was unprecedented.

11.4 Beginning August 8, 2003 (and up to April 29, 2004), the Central Government continuously maintained surplus cash balances in its current account with the Reserve Bank mainly due to substantial inflows on account of the debt swap scheme and increased issuance of 91-day Treasury Bills. The Central Government had an investment balance of Rs.26,669 crore at end-March 2004 (Chart XI.1). In view of the

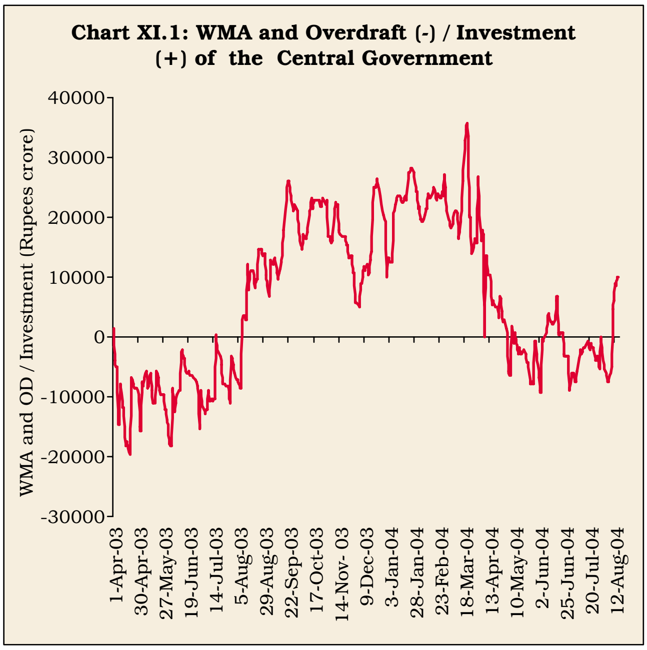
Table 11.1: Overdraft Position of the Central Government

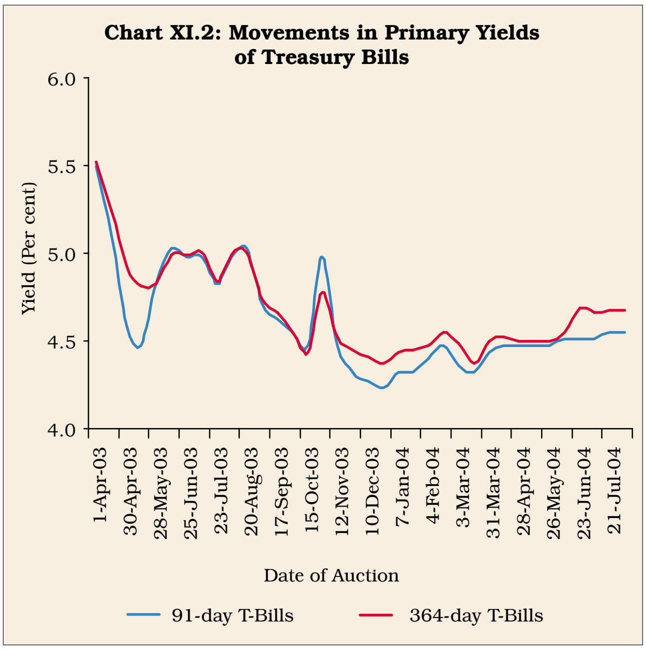
(Rupees crore)

Month	2003-04			2002-03		
	Range of Overdraft	No. of Days	No. of Occasions	Range of Overdraft	No. of Days	No. of Occasions
1	2	3	4	5	6	7
April	1,642 - 9,656	15	2	144 - 6,300	13	2
May	900 - 5,867	9	3	734 - 7,773	12	2
June	875 - 8,349	5	1	359 - 5,154	9	3
July	383 - 5,288	14	4	85 - 3,893	13	4
August	–	–	–	25 - 3,863	10	2
September	–	–	–	–	–	–
October	–	–	–	–	–	–
November	–	–	–	–	–	–
December	–	–	–	39 - 1,711	2	2
January	–	–	–	–	–	–
February	–	–	–	–	–	–
March	–	–	–	–	–	–
Total	0 - 9,656	**43**	**10**	**0 - 7,773**	**59**	**15**

– : No overdraft.

Note : The Central Government did not resort to overdraft during 2004-05 (up to August 14, 2004).





need by the Reserve Bank to preserve its existing stock of securities for the conduct of monetary policy operations, investment of the Central Government's surplus cash balances in dated securities was discontinued temporarily from April 8, 2004. From June 12, 2004 the arrangement of investment of surplus balances was partially restored for investment up to Rs.10,000 crore due to reduction in outstandings under the Liquidity Adjustment Facility (LAF), partly facilitated by absorption under the Market Stabilisation Scheme. After maintaining surplus cash balances for a brief period in June 2004, the Centre took recourse to WMA to the tune of Rs.2,632 crore at end-July 2004.

Treasury Bills

11.5 The notified amount of 364-day Treasury Bills was maintained at Rs.1,000 crore in 2003-04, while that of 91-day Treasury Bills was refixed at Rs.500 crore from February 2003. The notified amount of 91-day Treasury Bills was raised temporarily to Rs.1,500 crore for eight auctions conducted between August 6, 2003 and September 24, 2003 with a view to absorbing the abundant liquidity in the system. The weighted average primary market yields of 91-day and 364-day Treasury Bills declined by 110 basis points and 125 basis points, respectively (Table 11.2 and Appendix Table V.8).

11.6 The reduction in the repo rate in August 2003 led to softening of yields in respect of both 91-day and 364-day Treasury Bills. Between May and mid-October 2003, the spread between cut-off yields on 91-day and 364-day Treasury Bills narrowed to near convergence. Frequent OMOs absorbed Rs.13,986 crore from the system during October 2003, which led to a rise in the cut-off yield on 91-day Treasury Bills to the extent of 22 basis points higher than the cut-off yield on 364-day Treasury Bills. Beginning November 2003, the cut-off yields on 91-day and 364-day Treasury Bills remained lower than the repo rate, resulting in an inverted yield curve at the short end (Chart XI.2).

11.7 The positive response to Treasury Bill auctions in the primary market led to improved bid-cover ratio during the year (Table 11.3). Consequently, there was no devolvement on the Reserve Bank in any of the auctions during the year.

Table 11.2: A Profile of Treasury Bills

(Rupees crore)

Type of T-Bill	Weighted Average Cut-off Yield (per cent)		Gross Amount		Net Amount		Outstanding Amount	
	2003-04	2002-03	2003-04	2002-03	2003-04	2002-03	2003-04	2002-03
1	2	3	4	5	6	7	8	9
91-day	4.63	5.73	36,786	26,402	(-) 2,488	4,626	7,139	9,627
364-day	4.67	5.92	26,136	26,126	9	6,538	26,136	26,126

Table 11.3: Treasury Bills - Primary Market@

Month	Average Implict Yield at Minimum Cut-off Price (Per cent)		Bid-Cover Ratio*	
	91-day	364-day	91-day	364-day
1	2	3	4	5
2003				
April	5.04	5.19	4.13	2.56
May	4.56	4.77	1.94	1.88
June	4.95	4.95	1.91	2.51
July	4.87	4.88	3.06	2.15
August	4.90	4.96	1.73	2.01
September	4.60	4.65	2.91	3.32
October	4.61	4.53	2.24	2.38
November	4.37	4.42	3.23	2.32
December	4.19	4.32	2.76	1.80
2004				
January	4.25	4.37	2.01	1.98
February	4.38	4.44	3.07	1.72
March	4.27	4.39	3.42	2.28
April	4.39	4.45	2.16	2.68
May	4.40	4.43	2.93	2.46
June	4.46	4.56	2.49	1.29
July	4.48	4.61	2.54	2.07

@: As per dates of auction.
* : Ratio of competitive Bids Received (BR) to Notified Amount (NA).

11.8 During 2004-05 (up to August 4, 2004), the primary market cut-off yields on 91-day and 364-day Treasury Bills moved up to 4.49 per cent and 4.62 per cent, respectively, from 4.24 per cent and 4.31 per cent, respectively, at end-March 2004.

Dated Securities

11.9 The Central Government raised a gross amount of Rs.1,21,500 crore (a net amount of Rs.88,807 crore) through issuances of dated securities during the year (Appendix Table V.5). Of this, Rs.1,00,000 crore was raised through auctions (28 auctions comprising 19 reissues and 9 new issues) and Rs.21,500 crore by way of private placements (mainly for the prepayment of external debt). Taking into account the four dated securities issued on July 22, 2003 under the debt buy-back scheme amounting to Rs.14,434 crore, issuances of dated securities aggregated Rs.1,35,934 crore (Appendix Table V.7). The conversion of Government of India Treasury Bills (Conversion) Special Securities amounting to Rs.61,818 crore into dated securities added to the stock of marketable securities of the Reserve Bank. Of the 124 outstanding marketable securities amounting to Rs.8,24,314 crore as on March 31, 2004, 41 securities with outstanding amount of Rs.10,000 crore or more accounted for 63 per cent.

11.10 Private placements of the Centre's dated securities with the Reserve Bank were restricted mainly to the prepayment of external debt. Out of Rs.21,500 crore (17.7 per cent of the gross borrowings through dated securities) placed privately with the Reserve Bank, Rs.16,500 crore was for the purpose of prepayment of external debt. Although this arrangement was reserve money neutral, it added to the stock of marketable securities with the Reserve Bank. Securities amounting to Rs.5,000 crore were placed privately with the Reserve Bank on April 23, 2003 outside the calendar for market borrowing and these, together with Rs.7,000 crore raised through auctions as per the borrowing calendar on the same day, wiped out the Central Government's overdraft, which had peaked at Rs.9,656 crore on April 22, 2003.

11.11 The calendar of dated securities issuance for the first half (April-September) of 2003-04 covering 50.6 per cent (*i.e.*, Rs.71,000 crore) of the budgeted amount was mostly adhered to even as the actual mobilisation by the Government was somewhat higher at Rs.80,000 crore (excluding Rs.14,434 crore issued under the debt buyback scheme). After adjusting for the amounts received from the State Governments towards prepayment of high cost loans and keeping in view trends in other receipts, the calendar for the second half of 2003-04 (October-March) was announced for an aggregate borrowing of Rs.25,000 crore. This had a softening impact on the market yields as market participants had anticipated an amount of Rs.60,000 crore. The weighted average yield of dated securities issued during the year and of the total outstanding stock declined by 163 and 114 basis points, respectively (Chart XI.3).

Chart XI.3: Yield and Maturity of Centre's Primary Issuances

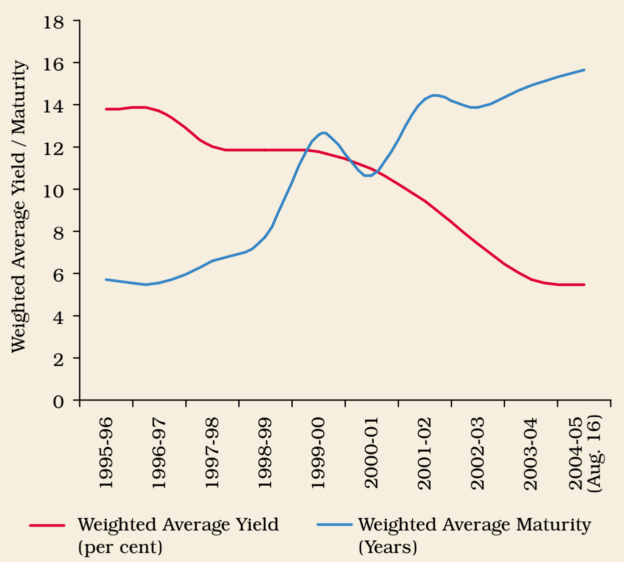


Table 11.4: A Profile of Central Government's Market Loans

(Yield in per cent/Maturity in years)

Year	YTMs at Primary Issues (per cent)			Weighted Average Yield	Maturity of New Loans	Weighted Average Maturity	Weighted Average Maturity of outstanding stock	Weighted Average Yield of outstanding stock
	Under 5 years	5-10 years	Over 10 years					
1	2	3	4	5	6	7	8	9
1997-98	10.85-12.14	11.15-13.05	–	12.01	3-10	6.6	6.5	n.a.
1998-99	11.40-11.68	11.10-12.25	12.25-12.60	11.86	2-20	7.7	6.3	n.a.
1999-00	–	10.73-11.99	10.77-12.45	11.77	5-19	12.6	7.1	n.a.
2000-01	9.47-10.95	9.88-11.69	10.47-11.70	10.95	2-20	10.6	7.5	n.a.
2001-02	–	6.98-9.81	7.18-11.00	9.44	5-25	14.3	8.2	10.84
2002-03	–	6.65-8.14	6.84-8.62	7.34	7-30	13.8	8.9	10.44
2003-04	4.69	4.62-5.73	5.18-6.35	5.71	4-30	14.94	9.78	9.30
2004-05 (up to August 16, 2004)	–	–	4.49-7.50	5.52	11-30	15.68	9.84	8.95

n. a.: Not available. – : No issues. YTM : Yeild to Maturity.

11.12 The response at primary auctions was generally favourable with the average bid-cover ratio working out to 1.7 in 2003-04 as against 2.1 in 2002-03. For the first time, there was no devolvement on the Reserve Bank or on primary dealers in any auction during the year.

11.13 The policy of elongation of maturity of dated securities continued during the year with the multiple objectives of developing a yield curve for the long end of the maturity spectrum, managing rollover risk and locking in borrowings at low costs. The weighted average maturity of the securities issued during the year and outstanding dated securities increased to 14.94 years and 9.78 years, respectively (Table 11.4).

11.14 The weighted average yield of the dated securities issued during 2004-05 (up to August 16, 2004) worked out to 5.52 per cent as against 5.89 per cent during the corresponding period of the previous year. The weighted average maturity of the dated securities issued during 2004-05 (up to August 16, 2004) was 15.68 years as compared with 15.84 years during the corresponding period of 2003-04.

Table 11.5: Maturity Profile of Central Government Securities

(Per cent)

Year	Outstanding Stock			Issued During the Year		
	Under 5 Years	5-10 Years	Over 10 Years	Under 5 Years	5-10 Years	Over 10 Years
1	2	3	4	5	6	7
1997-98	41	41	18	18	82	–
1998-99	42	42	16	18	68	14
1999-00	37	39	24	–	35	65
2000-01	27	47	26	6	41	53
2001-02	31	36	33	2	24	74
2002-03	26	35	39	–	36	64
2003-04	24	32	44	5	15	80

11.15 Securities over 10-year maturity constituted the largest share in the outstanding stock of securities as well as in new issuances (Table 11.5).

11.16 The Central Government converted the balance stock of 4.6 per cent Government of India Treasury Bills (Conversion) Special Securities held by the Reserve Bank into marketable lots on a private placement basis. This considerably enhanced the stock of marketable securities in the portfolio of the Reserve Bank, strengthening the conduct of sterilisation operations (Table 11.6).

Table 11.6: Reserve Bank's Stock of Central Government Securities@

(Rupees crore)

Year (end-March)	Outstanding Dated Securities*	Special Securities Issued to RBI in Conversion of *Ad-hoc* Treasury Bills	Total Out-standing*
1	2	3	4
1996-97	6,666	1,21,818	1,28,484
1997-98	31,977	1,01,818	1,33,795
1998-99	42,212	1,01,818	1,44,030
1999-00	35,190	1,01,818	1,37,008
2000-01	41,732	1,01,818	1,43,550
2001-02	40,927	1,01,818	1,42,745
2002-03	55,438	61,818	1,17,256
2003-04	77,397	0	77,397
2004-05 (As on August 9, 2004)	1,02,402	0	1,02,402

@ : Does not include other special securities.
* : Inclusive of securities sold under the LAF.

Table 11.7: Repayment Schedule for Centre's Market Loans Outstanding
(As on March 31, 2004)

Year	(Amount in Rs. crore)
1	2
2004-05	34,316
2005-06	35,631
2006-07	39,079
2007-08	45,876
2008-09	44,028
2009-10	49,589
2010-11	50,586
2011-12	50,581
2012-13	57,074
2013-14	55,009
2014-15	42,018
2015-16	41,244
2016-17	36,130
2017-18	50,774
2018-19	37,478
2019-20	28,000
2020-21	11,000
2021-22	13,213
2022-23	24,000
2023-24	21,000
2025-26	16,688
2026-27	15,000
2027-28	8,000
2028-29	6,000
2032-33	12,000
Total	**8,24,314**

11.17 The profile of repayments of outstanding market loans of the Central Government indicates some bunching between 2006-07 and 2013-14 in nominal terms (Table 11.7).

Table 11.8: Interest Rate Profile of Outstanding Central Government Securities
(As on March 31, 2004)

Interest Rate (Per cent)	Outstanding (Amount in Rs. crore)	Share in Total
1	2	3
4.50-4.99	27,500	3.34
5.00-5.99	78,818	9.56
6.00-6.99	1,16,835	14.17
7.00-7.99	1,10,541	13.41
8.00-8.99	29,638	3.60
9.00-9.99	51,744	6.28
10.00-10.99	83,537	10.13
11.00-11.99	1,86,344	22.61
12.00-12.99	1,07,135	13.00
13.00-14.00	32,222	3.91
Total	**8,24,314**	**100.0**

11.18 Securities with coupon at 10 per cent and above declined to 49.6 per cent of the total stock outstanding as on March 31, 2004 from 67.6 per cent as on March 31, 2003 (Table 11.8).

11.19 With a view to enabling institutional and retail investors to plan their investment better and for imparting transparency and stability to the Government securities market, it was decided in consultation with the Government to continue with the system of releasing an indicative calendar for the period April to September 2004, specifying the amounts and maturity of loans to be issued. The calendar is subject to variations depending on market conditions and other factors. In addition to the borrowing schedule as per the calendar, the Reserve Bank has the option of additional issuances as warranted by the Government's requirement and market conditions (Table 11.9).

Table 11.9: Issuance Calendar and Actual Borrowings (April 1, 2004 to September 30, 2004)

Borrowings as per Issuance Auction Calendar			Actual Borrowings		
Period of auction	Amount (Rs. crore)	Maturity Period of the Security	Date of Auction / Date of issue	Amount (Rs. crore)	Tenor of the Security (Years)
1	2	3	4	5	6
April 12-20,2004	5,000	15 to 19 year	No Issue		
May 3-10,2004	6,000	i) 10 to 14 year	May 6/7, 2004	6,000	12.00
	3,000	ii) 20- year and above	May 6/7, 2004	3,000	23.88
June 1-8,2004	6,000	i) 10 to 14 year	June 3/4, 2004	6,000	12.00
	4,000	i) 20- year and above	June 3/4, 2004	4,000	23.81
June 17-24,2004	6,000	i) 10 to 14 year	June 17/18, 2004	6,000	11.21
	3,000	ii) 20- year and above	June 17/18, 2004	3,000	23.96
July 1-8, 2004	6,000	i) 10-14 year	July 1/2, 2004	6,000	11.00
	2,000	ii) 20-year and above	July 1/2, 2004	2,000	23.92
August 2-9, 2004	6,000	i) 10-14 year	August 9/10, 2004	6,000	11.00
	2,000	ii) 20-year and above	August 9/10, 2004	2,000	30.00
September 2-9, 2004	6,000	i) 5-9 year			
	4,000	ii) 15-19 year			

Box XI.1

Debt Buyback Scheme

The first ever buyback auction was conducted for 19 high coupon but relatively illiquid Government of India dated securities at a price range of Rs.122.75-148.87 on a voluntary basis through a live interactive platform where participants were allowed to revise their bids. In all, 131 offers amounting to Rs.14,434 crore (face value) were received. The entire amount was accepted as the offers were at or above the minimum discount of 7.5 per cent (to the market value) expected by the Government. The market value of the securities bought back amounted to Rs.19,394 crore. The difference between the market value and the face value (*i.e.*, Rs.4,960 crore) was shared between the Government and market participants. While the premium paid to market participants amounted to Rs.3,472 crore, the Government saved Rs.1,488 crore or 7.67 per cent of the market value or the discount. In exchange of the securities bought back, the Government reissued four existing liquid securities of equal face value (Rs.14,434 crore). The prices at which the securities were reissued were the weighted average prices during the period July 14-18, 2003. Banks were allowed additional deduction for tax purposes to the extent such income was used for provisioning of non-performing assets (NPAs).

11.20 Net market borrowing of the Central Government for the year 2004-05 was placed at Rs.90,365 crore in the Union Budget. Including repayments of Rs.60,451 crore, gross market borrowings are expected to be of the order of Rs.1,50,817 crore (Rs.1,24,817 crore through dated securities and Rs.26,000 crore through 364-day Treasury Bills), as against Rs.1,47,636 crore raised in 2003-04. The issuance calendar for dated securities of the Central Government for the first half of 2004-05 was drawn up on the assumption that Rs.24,000 crore would be prepaid by the States during the first half. This amount was to be raised by way of market borrowings (Rs.12,000 crore) and by utilising small saving receipts (Rs.12,000 crore). Accordingly, it was announced on March 25, 2004 that Rs.59,000 crore would be raised by way of dated securities during the first half of 2004-05.

11.21 Excluding the amount raised under the Market Stabilisation Scheme, the gross market borrowings raised by the Central Government during 2004-05 (up to August 14, 2004) amounted to Rs.54,035 crore (Rs.44,000 through dated securities and Rs.10,035 crore by way of 364-day Treasury Bills) as compared with Rs.98,464 crore (Rs.88,434 crore through dated securities and Rs.10,030 crore through 364-day Treasury Bills) during the corresponding period of the previous year. The net market borrowing amounted to Rs.18,229 crore as against Rs.50,875 crore during the corresponding period of the previous year.

Debt Restructuring - Central Government

11.22 The Union Budget, 2003-04 envisaged measures for debt restructuring as a part of the process of fiscal consolidation - the buyback of loans by the Central Government from banks on a voluntary basis, prepayment of external debt and the States' debt swap scheme. The Reserve Bank conducted a buyback auction of high coupon but relatively illiquid securities for the first time on July 19, 2003 (Box XI.1).

11.23 Taking into account the comfortable foreign exchange reserves and soft domestic interest rates, the Central Government prepaid high cost external debt amounting to US $ 3.8 billion. Private placement did not have a monetary impact and was neutral to public debt as it involved substitution of external debt with domestic debt.

STATE GOVERNMENTS

Ways and Means Advances

11.24 A majority of States reduced their recourse to normal WMA and overdrafts (OD) during 2003-04 (Table 11.10). The use of special WMA by the States increased by 52.7 per cent during 2003-04, mainly due to the change in provision that special WMA should be availed first before availing the normal WMA as recommended by the Ramachandran Committee (2003). The interest rate charged on Special WMA is one percentage point less than the rate on normal WMA (Chart XI.4). The buoyant proceeds from small savings and higher market borrowings (other than under the debt swap scheme) also contributed to the substantially lower recourse to the normal WMA *vis-à-vis* the aggregate limit of Rs.7,170 crore available for the year 2003-04.

11.25 During 2003-04, some States, especially Tamil Nadu, Haryana, Nagaland and Uttaranchal considerably reduced their recourse to WMA (in terms of number of days) and overdraft (both in terms of number of days and number of occasions) (Table 11.11).

Table 11.10: WMA/Overdrafts and Investment of the State Governments*

(Rupees crore)

Month	Normal WMA		Special WMA		Overdraft		Investment in 14-day Intermediate Treasury Bills	
	2003-04	2002-03	2003-04	2002-03	2003-04	2002-03	2003-04	2002-03
1	2	3	4	5	6	7	8	9
April	2,145	2,924	989	835	1,088	2,987	3,894	1,652
May	1,816	2,961	941	480	445	1,428	4,987	2,404
June	1,179	3,007	937	559	204	1,022	6,232	3,670
July	2,160	3,295	1,138	658	612	1,252	4,095	2,727
August	2.183	2,058	968	507	658	817	5,193	4,367
September	1,681	2,875	959	610	532	924	5,190	4,389
October	2,464	3,238	1,150	709	946	1,860	3,690	3,156
November	3,829	3,673	1,246	704	1,053	1,575	3,497	2,396
December	4,513	4,454	1,216	833	1,185	1,407	2,820	2,440
January	3,417	3,982	1,055	922	1,203	1,431	3,716	3,299
February	3,274	3,352	1,023	493	698	1,351	4,208	3,371
March	2,068	2,806	811	832	703	715	4,234	3,301
Average	**2,379**	**3,219**	**1,036**	**679**	**777**	**1,397**	**4,313**	**3,098**

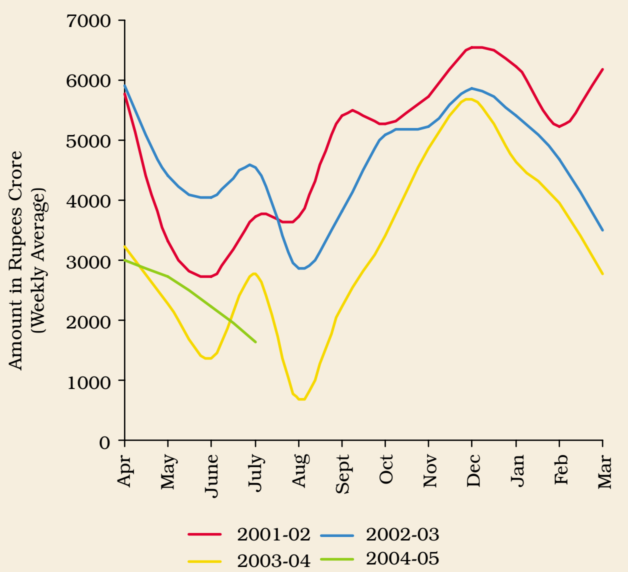
* : Average of Friday outstandings.

11.26 Effective April 1, 2004 the formula-based aggregate normal WMA limit of the State Governments was revised upwards by 13.5 per cent to Rs.8,140 crore on the basis of higher average revenue receipts of the States in the preceding three years (Table 11.12).

Market Borrowings

11.27 Gross market borrowings raised by the State Governments increased by 63.7 per cent during 2003-04 (Table 11.13). Of the total amount of Rs.29,000 crore allocated under the debt swap scheme (DSS), Rs.26,623 crore was utilised towards repayment of debt under the DSS. A part of market borrowings under the DSS was allowed to be retained by a few States for other purposes, while a small portion of the DSS remained unsubscribed.

Chart XI.4 : WMA and Overdraft of the States



11.28 Of the total borrowings by the States during 2003-04, 94.3 per cent was through sale of securities on a tap basis. Interest rates on States' market borrowings softened during 2003-04 even as the maturity profile of select tap tranches was extended up to 13 years to minimise the rollover risk and bunching of repayments arising from the higher market borrowings under the DSS (Table 11.14).

11.29 Borrowings raised by way of auctions aggregated Rs.2,895 crore, accounting for 5.7 per cent of total borrowings. The spread *vis-à-vis* Central Government dated security of similar maturity ranged at 48-88 basis points (Table 11.15).

11.30 The weighted average yield of the State Government loans declined in 2003-04 (Table 11.16). The spread in the case of tap issues was fixed at a mark-up of about 50 basis points over the secondary market yield on the Central Government dated securities of similar maturity.

Table 11.11: State-wise Availment of WMA/Overdraft

(Rupees crore)

State	WMA		Overdraft			
	2003-04	2002-03	2003-04		2002-03	
	No. of days	No. of days	No. of Occasions	No. of days	No. of Occasions	No. of days
1	2	3	4	5	6	7
Non-Special Category States						
1. Andhra Pradesh	173	72	6	30	6	33
2. Bihar	92	1	5	44	0	0
3. Goa	270	266	8	48	9	66
4. Gujarat	203	219	4	21	13	47
5. Haryana	24	64	0	0	4	21
6. Karnataka	196	157	6	33	1	1
7. Kerala	328	330	27	178	28	196
8. Madhya Pradesh	261	251	10	59	22	176
9. Maharashtra	207	301	5	39	17	154
10. Orissa	315	329	19	168	21	189
11. Punjab	291	214	14	131	11	53
12. Rajasthan	303	329	16	94	21	151
13. Tamil Nadu	38	326	1	2	13	73
14. Uttar Pradesh	321	229	10	100	14	79
15. West Bengal	362	318	21	140	28	260
16. Chhattisgarh	0	0	0	0	0	0
17. Jharkhand	31	0	0	0	0	0
Special Category States						
1. Arunachal Pradesh	0	27	0	0	0	0
2. Assam	337	121	20	235	24	315
3. Himachal Pradesh	327	252	14	109	27	181
4. Manipur	268	333	14	201	19	350
5. Meghalaya	31	78	0	0	1	1
6. Mizoram	131	184	3	5	4	24
7. Nagaland	12	297	0	0	19	143
8. Tripura	25	28	0	0	0	0
9. Uttaranchal	78	180	3	13	9	41

11.31 The weighted average maturity of the State Government securities issued during the year increased to 11.05 years in 2003-04 from 10 years in 2002-03. Of the outstanding loans of the State Governments, securities in the maturity range of 6-10 years constituted the largest share (53.9 per cent), followed by 0-5 years (32.1 per cent) and above 10 years (14.0 per cent) (Table 11.17). The weighted average maturity of the outstanding stock of the State Government securities stood at 9.32 years at end-March 2004.

11.32 The annual repayment schedule of the State Government market loans (including power bonds) indicates some amount of bunching of repayments during the three year period from 2011-12 to 2013-14 (Table 11.18), reflecting large amount of market borrowings in recent years inclusive of borrowings under the DSS.

11.33 The interest rate profile of the outstanding stock of State Governments indicates that 53.1 per cent was contracted at interest rates ranging from 5.00 to 9.99 per cent and the remaining at 10 per cent and above (Table 11.19).

11.34 The net initial allocations under the market borrowing programme for the State Governments for 2004-05 were placed at Rs.12,947 crore, including additional allocations of Rs.230 crore, Rs.50 crore and Rs.0.8 crore to Tamil Nadu, Himachal Pradesh and Nagaland, respectively. Taking into account the repayments of Rs.5,123 crore, the gross allocation amounted to Rs.18,070 crore excluding Rs.24,000 crore allocated under the debt swap scheme (DSS).

Table 11.12: Normal WMA Limits of the States

(Rupees crore)

	State	WMA Limits 2004 (effective April 1, 2004)	WMA Limits 2003 (effective March 3, 2003)	WMA Limits 2002 (effective April 1, 2002)	WMA Limits 2000 (effective Febuary 1, 2001)	WMA Limits 1999 (effective March 1, 1999)
	1	2	3	4	5	6
Non-Special Category States						
1.	Andhra Pradesh	700	620	520	463	288
2.	Bihar	340	305	245	220	195
3.	Chhattisgarh	155	130	100	91	82
4.	Goa	65	50	50	25	24
5.	Gujarat	520	485	445	393	243
6.	Jharkhand	175	105	75	57	51
7.	Haryana	245	205	180	167	99
8.	Karnataka	505	460	375	331	228
9.	Kerala	315	270	225	215	144
10.	Madhya Pradesh	395	345	275	244	221
11.	Maharashtra	1,000	905	760	685	483
12.	Orissa	250	215	185	159	141
13.	Punjab	325	240	235	200	141
14.	Rajasthan	405	365	310	288	202
15.	Tamil Nadu	615	570	415	402	281
16.	Uttar Pradesh	835	755	630	559	531
17.	West Bengal	480	420	360	295	235
	Sub Total	**7,325**	**6,445**	**5,385**	**4,794**	**3,589**
Special Category States						
1.	Arunachal Pradesh	50	50	50	35	28
2.	Assam	250	210	180	161	114
3.	Himachal Pradesh	140	135	115	92	59
4.	Manipur	50	50	50	38	25
5.	Meghalaya	50	50	50	30	25
6.	Mizoram	50	50	50	28	25
7.	Nagaland	60	55	50	40	26
8.	Tripura	70	60	55	46	31
9.	Uttaranchal	95	65	50	19	19
	Sub Total	**815**	**725**	**650**	**489**	**352**
	Total	**8,140**	**7,170**	**6,035**	**5,283**	**3,941**

11.35 During 2004-05 (up to August 14, 2004), the State Governments raised gross amount of Rs.22,259 crore under the market borrowing programme (inclusive of Rs.13,782 crore under the DSS). On April 21, 2004 all the 28 States raised Rs.7,500 crore through tap issuances of 5.60 per cent 10-year State Development Loans 2014 under the market borrowing programme. On May 26-27, 2004, 19 States raised an amount of Rs.8,471 crore at a coupon of 5.70 per cent for a tenure of 10 years through tap sale, of which Rs.8,091 crore went towards the debt swap scheme. On July 28-29, 2004 19 States raised an amount of Rs.6,288 crore at a coupon rate of 6.35 per cent for a tenure of nine years through a tap sale, of which Rs.5,691 crore went towards the debt swap scheme.

States' Debt Swap Scheme

11.36 Under the DSS, the Central Government permitted State Governments to prepay high cost debt from the Centre aggregating over Rs.1,00,000 crore (contracted at interest rates of 13 per cent or more) over a three-year period ending 2004-05. During

Table 11.13: Market Borrowings of the State Governments - 2003-04

(Rupees crore)

	State	Gross Allocation	Repayment	Net Allocation (Col. 2 - Col.3)	Gross Amount raised by Auction	Gross Amount raised by Tap	Gross Borrowings (Co.l 5+ Col.6)
	1	2	3	4	5	6	7
1.	Andhra Pradesh	3,226	393	2,833	500	2,726	3,226
2.	Arunachal Pradesh	131	5	126	–	131	131
3.	Assam	943	124	819	–	943	943
4.	Bihar	2,131	309	1,822	–	2,131	2,131
5.	Chhattisgarh	742	48	693	–	642	642
6.	Goa	240	10	230	–	240	240
7.	Gujarat	3,333	138	3,195	250	3,083	3,333
8.	Haryana	1,165	79	1,086	–	1,165	1,165
9.	Himachal Pradesh	882	26	856	–	882	882
10.	Jammu and Kashmir	522	45	478	–	522	522
11.	Jharkhand	575	105	470	–	575	575
12.	Karnataka	2,779	181	2,598	–	2,779	2,779
13.	Kerala	1,931	220	1,711	450	1,481	1,931
14.	Madhya Pradesh	2,405	133	2,272	220	2,185	2,405
15.	Maharashtra	6,449	226	6,223	700	5,749	6,449
16.	Manipur	192	15	177	–	192	192
17.	Meghalaya	166	17	149	–	166	166
18.	Mizoram	101	5	96	–	101	101
19.	Nagaland	227	20	207	–	227	227
20.	Orissa	2,119	300	1,819	–	2,101	2,101
21.	Punjab	2,056	51	2,006	190	1,867	2,056
22.	Rajasthan	2,714	249	2,465	–	2,714	2,714
23.	Sikkim	62	7	55	–	62	62
24.	Tamil Nadu	2,851	313	2,538	250	2,601	2,851
25.	Tripura	229	20	209	–	229	229
26.	Uttar Pradesh	5,540	766	4,774	–	5,375	5,375
27.	Uttaranchal	1,366	41	1,325	–	1,366	1,366
28.	West Bengal	5,729	300	5,429	335	5,394	5,729
	Total	**50,805**	**4,145**	**46,659**	**2,895**	**47,626**	**50,521**

2003-04, the States repaid Rs.46,211 crore under the DSS. This included Rs.26,623 crore prepaid to the Centre out of fresh market borrowings. For the year 2004-05, the States would raise an additional Rs.24,000 crore from the market under the DSS.

Working Group on Model Fiscal Responsibility Legislation at the State Level

11.37 A Working Group comprising Finance Secretaries of States that have already enacted the Fiscal Responsibility legislation (or placed the bill before the Legislature), a representative each from the Central Government and the Reserve Bank was constituted in October 2003 to draft a model fiscal responsibility legislation at the State level in recognition of the importance of a rule-based fiscal policy to achieve fiscal sustainability (Box XI.2). The draft report was discussed in the 14th Conference of the State Finance Secretaries held on August 13, 2004. The report would be finalised after taking into account the comments of the State Finance Secretaries.

Guarantees Issued by the State Governments

11.38 State Governments have been issuing a large number of guarantees and letters of comfort to the State-level institutions, both in the public and private sectors, to enable them to mobilise resources for investment in infrastructure and for promotion of rural development (Table 11.20).

Table 11.14: Market Borrowings Raised Through Tap Issuances - 2003-04

(Amount in Rs. crore)

State	Period of Tap Issue/Coupon						
	Feb. 19-20, 2004, 5.85 per cent***	Jan. 19-20, 2004, 5.90 per cent **	Oct. 13-15, 2003, 5.85 per cent *	Aug. 25, 2003, 6.20 per cent *	Jul. 30, 2003, 6.20 per cent	Jun.12, 2003, 6.35 per cent	May 12-13, 2003, 6.40 per cent
1	2	3	4	5	6	7	8
1. Andhra Pradesh	0	306	264	462	462	404	828
2. Arunachal Pradesh	23	58	12	10	10	9	9
3. Assam	0	205	158	130	130	113	207
4. Bihar	22	569	202	337	337	295	369
5. Chhattisgarh	0	302	100	83	83	73	0
6. Goa	0	49	57	25	25	22	62
7. Gujarat	0	629	300	630	630	551	343
8. Haryana	0	141	199	212	212	186	216
9. Himachal Pradesh	0	110	176	141	141	124	190
10. Jammu and Kashmir	0	75	17	109	109	96	116
11. Jharkhand	0	28	147	83	83	72	162
12. Karnataka	500	221	519	340	340	297	562
13. Kerala	300	119	115	192	192	168	395
14. Madhya Pradesh	800	129	220	228	228	200	379
15. Maharashtra	50	884	567	1254	1254	1097	644
16. Manipur	28	50	58	10	10	9	27
17. Meghalaya	11	39	52	10	10	9	35
18. Mizoram	12	33	18	7	7	6	17
19. Nagaland	21	42	82	8	8	7	58
20. Orissa	481	464	183	220	220	193	339
21. Punjab	250	256	0	402	402	351	206
22. Rajasthan	300	230	571	381	381	334	517
23. Sikkim	0	30	10	5	5	5	7
24. Tamil Nadu	250	443	150	383	383	335	657
25. Tripura	13	56	62	20	20	18	39
26. Uttar Pradesh	474	865	795	808	808	708	916
27. Uttaranchal	0	0	263	339	339	297	128
28. West Bengal	500	899	164	1,171	1,171	1,024	466
Total	**4,036**	**7,233**	**5,460**	**8,002**	**8,001**	**7,002**	**7,893**

* : Tenure 12 years. ** : Tenure 13 years. *** : Tenure 11 years.

11.39 The devolvement of guarantees on a State Government has implications for its debt sustainability and overall financial stability. The development of a comprehensive database and an appropriate reporting system would help promote market discipline and effective supervision of financial intermediaries

Table 11.15: Market Borrowings Raised in Auctions - 2003-04

(Amount in Rupees crore/rate in per cent)

State	Date of Auction	Notified Amount (per cent)	Market Rate*	No. of Bids Received	Amount Offered (per cent)	Weighted Average (per cent)	Cut-off Rate	Spread (Col. 8-Col. 4)
1	2	3	4	5	6	7	8	9
1. Andhra Pradesh	13.08.03	500	5.52	79	2,362	5.98	6.03	0.51
2. Gujarat	13.08.03	250	5.52	56	1,630	5.98	6.00	0.48
3. Kerala	13.08.03	250	5.52	57	1,397	5.99	6.02	0.50
	25.03.04	200	5.17	38	430	5.76	5.80	0.63
4. Madhya Pradesh	08.09.03	220	5.28	19	408	5.99	6.00	0.72
5. Maharashtra	08.09.03	400	5.28	55	1,116	5.78	5.78	0.50
	12.01.04	300	5.12	31	303	5.81	6.00	0.88
6. Punjab	20.09.03	190	5.31	21	357	5.88	5.90	0.59
7. Tamil Nadu	13.08.03	250	5.52	64	1,799	5.97	6.00	0.48
8. West Bengal	08.09.03	335	5.28	27	962	5.78	5.78	0.50

* : Yield on Central Government dated security of similar maturity.

Table 11.16: Weighted Average Yield of State Government Market Loans

(per cent per annum)

Year	Range	Weighted Average
1	2	3
1995-96	14.00	14.00
1996-97	13.75-13.85	13.83
1997-98	12.30-13.05	12.82
1998-99	12.15-12.50	12.35
1999-00	11.00-12.25	11.89
2000-01	10.50-12.00	10.99
2001-02	7.80-10.53	9.20
2002-03	6.60-8.00	7.49
2003-04	5.78-6.40	6.13

subscribing to bonds and providing advances. A Working Group on Information on State Government Guaranteed Advances and Bonds (Chairman: Shri G. Padmanabhan) was set up to evaluate the status of the reporting system from the perspective of the intermediaries with exposure to the State Government guaranteed loans and bonds. It was also required to develop a reporting framework that would provide comprehensive data coverage and a transparent reporting system on State Government guarantees (Box XI.3).

Table 11.17: Maturity Profile of Outstanding State Government Market Loans (At end-March 2004)

	Percentage to total amount outstanding			
State	0-5 years	6-10 years	Above 10 years	Total Amount Outstanding (Rs. Crore)
1	2	3	4	5
1. Andhra Pradesh	34.7	59.3	6.0	17,090
2. Arunachal Pradesh	16.0	44.7	39.3	262
3. Assam	35.0	54.1	11.0	4,496
4. Bihar	37.1	51.9	11.0	10,243
5 Chhattisgarh	0.0	66.4	33.6	1,445
6. Goa	31.0	53.5	15.5	843
7. Gujarat	26.1	59.5	14.4	10,846
8. Himachal Pradesh	19.8	65.2	15.0	2,839
9. Harayana	32.7	52.9	14.4	3,825
10. Jammu and Kashmir	25.3	65.9	8.9	2,277
11. Jharkhand	0.0	83.1	16.9	1,523
12. Karnataka	29.0	54.6	16.4	9,645
13. Kerala	38.5	52.7	8.8	8,221
14. Maharashtra	27.4	52.4	20.2	13,655
15. Madhya Pradesh	37.7	46.8	15.5	8,867
16. Manipur	31.4	41.0	27.6	529
17. Meghalaya	39.3	44.6	16.1	700
18. Mizoram	29.6	53.8	16.6	422
19. Nagaland	36.6	49.4	14.0	1,098
20. Orissa	37.5	47.0	15.5	8,681
21. Punjab	29.8	55.3	15.0	6,059
22. Rajasthan	33.9	54.0	12.1	12,282
23. Sikkim	56.1	28.7	15.2	296
24. Tripura	34.8	46.1	19.2	792
25. Tamil Nadu	32.0	57.4	10.6	11,537
26. Uttaranchal	0.0	76.3	23.7	2,543
27. Uttar Pradesh	39.8	46.2	14.0	23,739
28. West Bengal	27.4	54.0	18.6	14,711
Total	**32.1**	**53.9**	**14.0**	**1,79,465**

Table 11.18: Maturity Profile of Outstanding State Market Loans and Power Bonds (As at end-March 2004)

(Rupees crore)

Year	State Loans	Power Bonds	Total Outstanding
1	2	3	4
2004-05	5,123		5,123
2005-06	6,274		6,274
2006-07	6,551	1,480	8,031
2007-08	11,555	2,961	14,515
2008-09	14,400	2,961	17,361
2009-10	16,511	2,961	19,472
2010-11	15,870	2,961	18,830
2011-12	22,032	2,961	24,993
2012-13	30,628	2,961	33,589
2013-14	25,790	2,961	28,751
2014-15	4,036	2,961	6,997
2015-16	13,462	2,961	16,423
2016-17	7,233	1,480	8,713
Total	**1,79,465**	**29,606**	**2,09,071**

Scheme for Settlement of Dues of State Electricity Boards

11.40 Under the One-Time Settlement Scheme for dues of the State Electricity Boards (SEBs), Power Bonds amounting to Rs.28,984 crore in respect of 26 States were issued to the Central Public Sector

Table 11.19: Interest Rate Profile of the Outstanding Stock of State Government Market Loans (As at end-March 2004)

Range of Interest Rate (per cent)	Outstanding Amount (Rupees crore)	Percentage to Total
1	2	3
5.00-5.99	18,641	10.39
6.00-6.99	52,274	29.13
7.00-7.99	11,029	6.15
8.00-8.99	8,004	4.46
9.00-9.99	5,412	3.02
10.00-10.99	14,563	8.11
11.00-11.99	17,062	9.51
12.00-12.99	30,485	16.99
13.00-13.99	15,720	8.76
14.00 and above	6,274	3.50
Total	**1,79,465**	**100.00**

Box XI.2

State Government Debt – Sustainability Issues

The fiscal health of the State Governments has deteriorated steadily from the early 1980s as reflected in the sharp rise in the debt/GDP ratio from 16.7 per cent in 1980-81 to 29.4 per cent in 2003-04. The persistent increase in non development expenditure - debt service payments, subsidies, wage and pension outgo - the erosion in the tax/GDP ratio, inadequate returns from public investment and insufficient growth in central transfers have led to a hard budget constraint facing States. This has eased somewhat in the recent period on account of buoyant small savings, including securities issued to the National Small Savings Fund (NSSF), borrowings through State level PSUs and Special Purpose Vehicles (SPVs), funding of large arrears of State Electricity Boards through power sector bonds and provision of guarantees.

Debt sustainability assumes an inter-temporal dimension in the context of the States, *i.e.*, movements in the debt/GDP ratio, the primary deficit and the interest rate on the debt stock have to be monitored in terms of a sustainable path. Sustainability also depends on the extent of the development of the financial markets, which determines the absorptive capacity of the markets. Forward-looking financial markets can demand a higher risk premium leading to a higher cost of borrowing for the Government. Thus, even without any increase in the primary deficit, high debt ratios can become unstable. The assessment of public debt should relate to combined finances of the Centre and the States, which exclude the impact of inter-governmental transfers emerging from the financial intermediary role of the Central Government. Among the positive developments during 2003-04, the States had a lower recourse to WMA/OD and there was a perceptible decline in interest rates on their market borrowings, although they witnessed a rise in the debt-GDP ratio. The States would need to accelerate the fiscal consolidation process through revenue augmentation and reduction of non-Plan expenditure. Additional measures are also desirable in the form of setting up consolidated sinking funds, establishing guarantee redemption funds, imposing ceiling on guarantees and introducing guarantee fees, fostering transparency with regard to budgeting, accounting and auditing, levying appropriate user charges and promoting private-public partnerships for infrastructure projects and public utilities. Five States have already enacted fiscal responsibility legislations to safeguard fiscal discipline and impose a statutory limit on the size of States' debt and/or borrowings (including guarantees). The Act is being enacted by one more State. The remaining States would need to enact similar legislation.

References

1. Acharya, S. (2002), 'India's Macroeconomic Management in the 1990s', *Economic and Political Weekly*, April 20-27, Volume 37, No.16. pp. 1515-38.
2. Feldstein, M. (2004), 'Budget Deficit and Public Debt', L.K. Jha Memorial Lecture, Reserve Bank of India, Mumbai, January.
3. Mohan,R. (2000),'Fiscal Correction for Economic Growth: Data Analysis and Suggestions', *Economic and Political Weekly*, June 10-16, Volume 35, No.24. pp. 2027-36.
4. Prasad, A., R. Goyal and A. Prakash (2004), 'States' Debt and Debt Relief', *Economic and Political Weekly*, June 26 - July 2, Volume 39, No. 26, pp. 2726-36.
5. Govinda Rao, M.(2002), 'State Finances in India: Issues and Challenges', *Economic and Political Weekly*, August 3-9, Volume 37, No.32, pp. 3261-71.
6. Goyal R., J.K. Khundrakpam and P., Ray (2004), 'Is India's Public Finance Unsustainable? Or, Are the Claims Exaggerated', *Journal of Policy Modeling*, Volume 26, pp. 401-20.
7. Rangarajan, C. and D.K.Srivastava, (2003), 'Dynamics of Debt Accumulation in India: Impact of Primary Deficit, Growth and Interest Rate', *Economic and Political Weekly*, November 15, Volume 38, pp. 4851-58.

Undertakings (CPSUs) in September 2003 (with retrospective date of October 1, 2001). Power Bonds in respect of Jharkhand were issued for Rs.622 crore in May 2004. Goa does not have any outstanding dues in respect of its SEB. Thus, the total loans issued amounted to Rs.29,606 crore. Ten per cent of the bonds could be taken to the market each year for trading for imparting liquidity to the bonds, once the overdue interest (for the period beginning from October 1, 2001 to September 30, 2003) is paid by the States to the CPSUs by September 2004.

Conference of State Finance Secretaries

11.41 The Reserve Bank has been organising the Conferences of the State Finance Secretaries in a structured manner since 1997, wherein a consensual approach among the Central Government, State Governments and the Reserve Bank has evolved on issues relating to State finances. During 2003-04, the 12th and 13th conferences were held on August 1, 2003 and January 23, 2004, respectively. In the 12th Conference, the major issues deliberated upon were

Table 11.20: Outstanding Guarantees of the State Governments

End-March	Amount (Rs. Crore)	Proportion to GDP (per cent)
1	2	3
1992	40,159	6.1
1993	42,515	5.7
1994	48,866	5.7
1995	48,479	4.8
1996	52,631	4.4
1997	63,409	4.6
1998	73,751	4.8
1999	97,454	5.6
2000	1,32,029	6.8
2001	1,68,719	8.1
2002	1,65,386	7.2
2003 (P)	1,84,294	7.5

P : Provisional.
Note : Data on State Governments guarantees are based on information received from 17 State Governments.

(i) defaults in servicing of guaranteed bonds; (ii) market borrowings of the State Governments; (iii) infrastructure financing; (iv) restructuring of State level PSUs; and (v) one-time settlement of SEB dues. A one-day interactive workshop on cash management was also organised by the Reserve Bank on August 2, 2003 for the benefit of officials of the State Government. In the 13th conference held on January 23, 2004 the major issues discussed were (i) the Report of the Group to Study the Pension Liabilities of the State Governments; (ii) default on loans/bonds of State Governments, including guaranteed bonds issued by State Finance Corporations (SFCs); and (iii) market borrowings of the State Governments. Two Working Groups were constituted to examine issues relating to credit enhancement in infrastructure projects and uniform application of software for treasury operations. A workshop on "Restructuring and Disinvestment of State Public Sector Undertakings" was also organised on January 24, 2004 for the benefit of officials of the State Governments. In the 14th Conference held on August 13, 2004, important issues discussed related to (i) implications of higher market borrowings and other borrowings of the State Governments; (ii) enhancing the liquidity of the State Government

Box XI.3

Monitoring State Government Guaranteed Advances and Bonds

The Working Group on Information on State Government Guaranteed Advances and Bonds (Chairman: Shri G. Padmanabhan) underscored the need for consolidation and sharing of data with a view to ensuring its regular dissemination and recommended a central point or 'data warehouse' on all State government guaranteed loans and bonds. There are several gaps in the present reporting system in respect of State Government guaranteed bonds/ advances from the side of investors/ creditors. The only source of data is the off-site surveillance returns furnished by commercial banks, large non-banking financial companies (NBFCs) and select All India Financial Institutions (AIFIs) that are under the supervisory purview of the Reserve Bank. Data covering all NBFCs, co-operative banks, public financial institutions (excluding those supervised by the Reserve Bank) and provident funds that have a considerable exposure to State Government guaranteed bonds and advances are not available. Some information is available on a disaggregated basis across various financial sector regulators such as NABARD, NHB, SIDBI, IRDA, Ministry of Labour (in respect of Provident Fund Trusts) and the Ministry of Power (in respect of REC and PFC) though not in a structured form.

A centralised database is to be located in the Reserve Bank to meet the needs of various regulators as also to serve as a useful input for policy formulation. Data requirements in respect of guaranteed loans and advances cover State-wise, borrower-wise and sector-wise information and details of formal guarantees and letters of comfort (LCs) issued by the State Governments. The sum of formal guarantees and LCs give the aggregate amount of explicit as well as implicit guarantees. A distinction is made between 'amount overdue and guarantee not invoked' and 'amount where guarantees have been invoked but not honoured'. In respect of guaranteed bonds, information requirements of the central database would cover issuer-wise and nomenclature-wise (*i.e.*, ISN identification number) total investments in guaranteed bonds, amount of overdue bonds (principal and interest) and amount of invoked guarantees not honoured. Inter-temporal changes in the default position would also be reported. The periodicity of reporting would be half-yearly with a lag of one month.

Transparency in information disclosure is crucial for enhancing market discipline. While the availability of information on defaults at a State-wise aggregated level (rather than at the level of the borrower) could sometimes go against the guarantor than would be the case if information was available on a more disaggregated (*i.e.*, project/borrower) basis, legal aspects relating to the publication of borrower-wise data on defaults would have to be taken into account. Subject to this limitation, (i) individual lender/investor-wise data (broken up into sectors) and (ii) State-wise data on guaranteed advances and investments (including defaults) could be disseminated through the Reserve Bank's publications and its website.

Reference

1. Reserve Bank of India (2003), 'Working Group on Information on State Government Guaranteed Advances and Bonds', October.

securities; (iii) dimensions of debt sustainability of the States; and (iv) credit enhancement for infrastructure financing at the State level. The draft report of the Working Group on the model fiscal responsibility legislation at the State level was also discussed. Two Working Groups were constituted on (i) improving secondary market liquidity of the State Development Loans and (ii) methodology of compilation of data on various types of debt liabilities of the States.

Technical Advisory Committee

11.42 During 2003-04 and 2004-05 (up to August 14, 2004), the Technical Advisory Committee (TAC) held four meetings in June 2003, October 2003, March 2004 and May 2004. Issues discussed in the meeting in June 2003 related to (i) introduction of 'when issued market'; (ii) interest rate derivatives; (iii) report of the Internal Group on forward sale of securities acquired under OMO; (iv) capital indexed bonds; (v) introduction of 28-day Treasury Bills; and (vi) retailing of Government securities. Issues discussed in the October 2003 meeting included (i) relaxation of the existing norms on sale of Government securities/ introduction of D*v*P-III mode of settlement and rollover of repos; (ii) exclusive access to primary dealers in Treasury Bill auctions; and (iii) settlement of Government securities transactions on a T+1 basis. The TAC was reconstituted and named as Technical Advisory Committee on Money, Government Securities and Forex Markets. In its first meeting held in March 2004, the newly constituted Committee discussed issues relating to (i) permitting PDs to invest in overseas markets; (ii) development of the repo market by allowing entry to corporates; and (iii) permission to banks to trade in exchange traded derivatives. As a follow-up of decisions taken in the TAC meeting held on March 29, 2004 a sub-group (Chairman: Dr. R.H. Patil) of the TAC was constituted to examine issues relating to diversification of business by primary dealers, including overseas investments. The report of the sub-group is expected to be submitted shortly. In the meeting of the TAC held in May 2004, various issues such as over-the-counter (OTC) derivatives, permission to banks to trade in exchange traded derivatives, development of the term money market, improving secondary market liquidity of State Development Loans and extension of repo eligibility to corporates were deliberated.

Outlook

11.43 The lower market borrowings of the Central Government have provided some room for manoeuvre to the Reserve Bank and undertake innovative debt rescheduling /restructuring measures. These initiatives would be carried forward with a view to ensuring the sustainability of public debt. The Reserve Bank would also persevere with efforts towards development of financial markets, including new instruments and new participants, with an ongoing priority attached to modernising the technological infrastructure. These efforts, in turn, would help minimise debt servicing costs, transaction costs and volatility. The relaxation of regulations relating to sale of Government securities facilitating repo rollover, institution of delivery *versus* payment (D*v*P) III and the launching of screen based trading in Government securities would help in deepening the Government securities market and would facilitate the process of debt management. The reintroduction of capital indexed bonds (CIBs) would lower the cost of borrowings to the Government, while minimising the inflation risk to the investors. The lower cost of borrowing by way of CIBs would hinge on effective fiscal-monetary coordination. The enactment of Fiscal Responsibility and Budget Management Act, 2003 and the Fiscal Rules, 2004 effective July 5, 2004 would prohibit borrowings through subscription to primary issues of the Government by the Reserve Bank from April 1, 2006. This would impart greater flexibility and manoeuverability in the conduct of monetary policy. The Reserve Bank would pursue the debt management policy consistent with objectives of minimisation of cost and rollover risk taking into account market conditions. The liquidity in State Government securities is an issue that would need to be addressed. Besides, the States would need to adopt a prudent fiscal policy, with enabling fiscal responsibility legislations for fiscal consolidation.

XII CURRENCY MANAGEMENT

12.1 The note issue and currency management function vested in the Reserve Bank in terms of Section 22 of the Reserve Bank of India Act, 1934 was guided during 2003-04 by the objectives of ensuring adequate availability of notes and coins and improving the quality of notes in circulation. Initiatives were taken to improve customer service and enhance security features in currency notes with a strong drive towards computerisation of currency management information system.

12.2 This Section reviews currency operations during 2003-04 covering currency chest activity and efforts undertaken to satisfy the buoyant demand for notes and coins in the face of constraints on fresh supply. An update of efforts under the Clean Note Policy shows progress in improving the quality of currency by efficient withdrawal of soiled and mutilated notes from circulation and mechanisation of processing and destruction. This Section also highlights the priority attached to enhancing the security of the currency through stepped-up detection of counterfeit notes and improved security features in currency notes. The heightened emphasis accorded to customer service in 2003-04, the setting up of a Monetary Museum and a review of the activities of the Bharatiya Reserve Bank Note Mudran Pvt. Ltd. are other aspects covered in this Section.

CURRENCY OPERATIONS

12.3 Currency operations are performed by the Reserve Bank through its 19 regional offices/sub-offices and a wide network of currency chests and small coin depots spread across the country.

12.4 The total number of currency chests declined during the year consequent to implementation of the policy to progressively convert and/or close currency chests held with the State Treasuries. Commercial banks expanded their currency chest operations. Foreign banks were permitted for the first time to operate currency chests. The State Bank Group dominates the currency chest system by maintaining about 72.0 per cent of total currency chests (Table 12.1).

Notes in Circulation

12.5 During the year, the total value of notes in circulation registered a growth of 15.8 per cent, reflecting the buoyancy in economic activity. The ratio of currency to broad money (M_3) remained unchanged at 15.8 per cent at end-March 2004 (Chart XII.1).

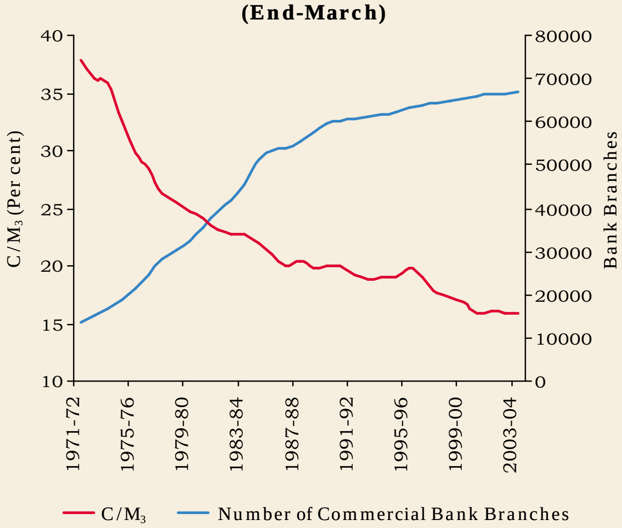
Table 12.1: Currency Chests

Category	No. of Currency Chests		
	June 30, 2004	June 30, 2003	March 31, 2003
1	2	3	4
Treasuries	214	405	417
State Bank of India	2,173	2,116	2,117
SBI Associate Banks	1,004	1,002	1,002
Nationalised banks	943	903	897
Private sector banks	58	36	32
Co-operative banks	1	1	1
Foreign banks	4	–	–
Reserve Bank of India	20	20	20
Total	**4,417**	**4,483**	**4,486**

12.6 The supply of notes was lower than the 'indent' made by the Reserve Bank. The supply of coins was also less than the indent but the indent itself was found to be slightly higher than the actual requirement due to decline in demand for coins (Table 12.2).

12.7 Accordingly, efforts to keep pace with the rising volume of currency demand took the form of judicious distribution of available supplies, increase in the percentage of higher denomination notes along with coinisation of lower denomination notes and ensuring the recirculation of notes by use of machines for processing, verification and sorting.

Chart XII.1 : Share of Currency in Broad Money (End-March)



C - Currency
M_3 - Broad Money

Table 12.2: Fresh Notes and Coins – 2003-04

Item	Notes		Coins	
	Pieces (in Million)	Value (Rupees crore)	Pieces (in Million)	Value (Rupees crore)
1	2	3	4	5
Indent	15,800	1,76,250	3,460	720
Supply	13,166	1,37,278	2,828	509

12.8 A gradual compositional shift is underway in the form of a gradual replacement of lower denomination notes by higher denomination notes. The demand for Rs.500 denomination notes increased sharply due to the growing network of Automated Teller Machines (ATMs). In terms of value, the largest share in circulation was of Rs.500 denomination. Notes of Rs.100 denomination had the largest share in terms of volume. Notes of Rs.100 denomination and Rs.500 denomination together accounted for 76.5 per cent of the total circulation in terms of value (Table 12.3). Both Rs.500 and Rs.1000 denomination notes taken together have a significant share in the value of notes issued over the last four years, although there was a marginal rise in the volume of these notes (Chart XII.2).

12.9 Notes of one rupee denomination have been withdrawn from issuance; however, 2,500 million pieces continued to be in circulation as on March 31, 2004. Value of Rs.5 coins in circulation increased at an average rate of 12.0 per cent over the last two years. The total value of coins including small coins in circulation showed an average growth of 7.0 per cent during the same period (Chart XII.3).

12.10 With adequate availability of coins from the mints, the Reserve Bank undertook intensive efforts to ensure that the shortage of coins in the country in the recent past was mitigated and that the supply of coins to the interior parts of the country was sustained (Box XII.1).

Table 12.3: Circulation of Notes and Coins

(End-March 2004)

Denomination	Value		Volume	
	Rupees crore	Share (per cent)	Million Pieces	Share (per cent)
1	2	3	4	5
Notes				
Rs.2 and Rs.5	2,748	0.9	6,911	18.1
Rs.10	7,750	2.4	7,750	20.2
Rs.20	4,383	1.4	2,192	5.7
Rs.50	33,027	10.3	6,605	17.2
Rs.100	1,21,442	38.0	12,144	31.7
Rs.500	1,22,938	38.4	2,459	6.4
Rs.1,000	27,473	8.6	275	0.7
Total	**3,19,761**	**100.0**	**38,336**	**100.0**
Coins				
Small Coins	1,353	18.8	54,102	62.9
Rupee coins	2,057	28.6	20,565	23.9
Rs. 2	1,255	17.4	6,275	7.3
Rs.5	2,536	35.2	5,071	5.9
Total	**7,201**	**100.0**	**86,013**	**100.0**

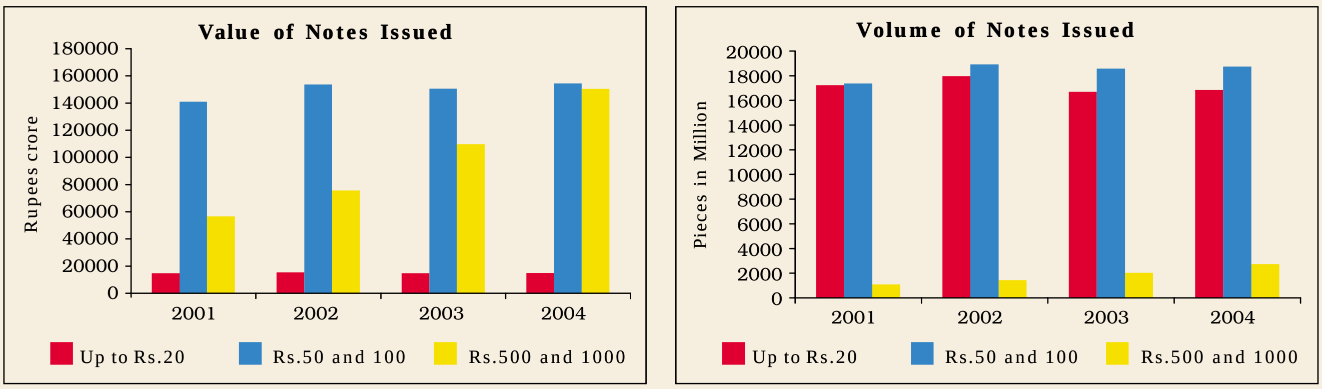
CLEAN NOTE POLICY

12.11 The Reserve Bank took various measures to improve the quality of notes in circulation. These measures included discontinuance of the practice of stapling of note packets, supply of adequate quantity of fresh notes to banks and mopping up of soiled and mutilated notes, particularly notes of lower denominations from circulation and acceleration in mechanised processing of notes at the offices of the Reserve Bank.

Disposal of Soiled Notes

12.12 During 2003-04 (April-March), 12,445 million pieces of soiled notes were processed and disposed off. The denomination-wise disposal of soiled notes indicates that Rs.10 constituted the largest share (40.2 per cent), followed by Rs.100 notes (31.8 per cent) and Rs.50 notes (21.0 per cent) (Table 12.4).

Chart XII.2 : Denomination-wise Notes Issued



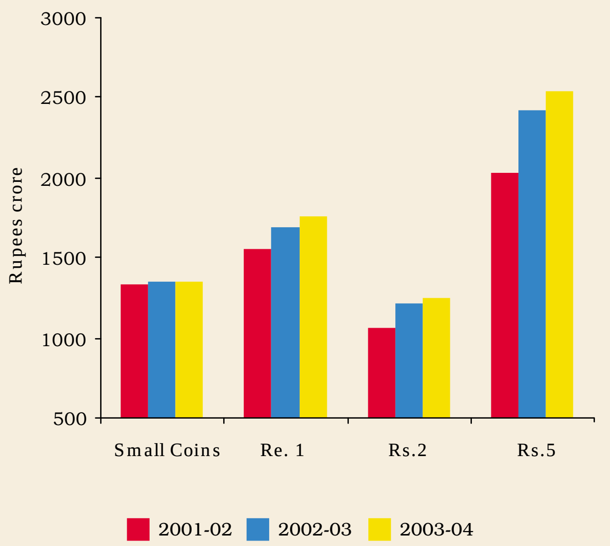
Box XII.1
Coins – Shortage to Surplus

The Reserve Bank allowed its offices to engage private transport operators for remittances of coins to the interior parts of the country. Coins were distributed through mobile vans. Banks were persuaded to distribute coins in marketplaces and to keep their branches at select places open on Sundays. Services of postal authorities, Regional Rural Banks (RRBs), co-operative banks and State Transport Undertakings were utilised for distribution of coins. A survey conducted by the Administrative Staff College of India (ASCI), Hyderabad, revealed that the availability of coins was 97 per cent of the demand even in rural areas. This was achieved by overcoming the bottlenecks in the distribution system such as non-availability of railway wagons/police security and the reluctance of banks to handle the distribution work.

The demand for coins, particularly of lower denominations, has declined considerably. There has also been a reverse flow of coins of 5 paise, 10 paise and 20 paise denominations. The parallel issue of notes and coins of Rs.5 denomination has reduced the demand for Rs.5 coins. Increasing stocks of coins with the public and reluctance to accept coins by shops and banks have led to surplus of coins, especially in temple towns, large cities as well as with agencies such as transport authorities and large organisations. The Reserve Bank directed banks maintaining currency chests to accept coins freely from the public either for exchange or for deposit. It also decided to phase out from circulation all lower denomination coins such as 5 paise, 10 paise and 20 paise and cupro-nickel coins of 25 paise, 50 paise and one rupee. Banks have been directed to accept and remit these coins to the Government mints.

Offices of the Reserve Bank have been accepting coins in bulk quantity by weight for the sake of convenience of the public and bank branches. Banks have been directed to implement this measure. Polythene pouches are being made available at some of the bank branches to pack 100 coins for quick and smooth service.

Chart XII.3 : Value of Coins in Circulation



12.13 During 2003-04 (April-March), the Issue Offices of the Reserve Bank received 21,933,212 mutilated notes. 21,908,135 notes, including the backlog from 2002-03, were adjudicated under the Reserve Bank (Note Refund) Rules.

Mechanisation

12.14 Mechanisation of processing and destruction of currency notes has been one of the major thrust areas of the Reserve Bank in currency management.

Table 12.4: Denomination-wise Disposal of Soiled Notes – 2003-04

(Million pieces)

Denomination	2003-04	As percentage to total
	2	3
Rs. 1,000	13	0.1
Rs. 500	247	2.0
Rs. 100	3,954	31.8
Rs. 50	2.617	21.0
Rs. 20	306	2.5
Rs. 10	5,004	40.2
Up to Rs. 5	304	2.4
Total	**12,445**	**100.0**

The Reserve Bank has installed 48 Currency Verification and Processing Systems (CVPS) at 18 offices. The notes processed on these machines during 2003-04 aggregated 3,290 million pieces. Twenty-seven Shredding and Briquetting Systems (SBSs) were installed at 18 Issue Offices of the Reserve Bank. These environment-friendly machines provide shredding, granulation and briquetting of soiled currency notes in a secure and eco-friendly manner. These machines have replaced the conventional furnaces. As a result of mechanisation and certain special measures, 12.4 billion pieces of bank notes were disposed off during 2003-04 as compared with 15.6 billion pieces during the previous year.

Counterfeit Notes

12.15 The Reserve Bank's regional offices and branches of various banks detected counterfeit notes valued at Rs. 2.76 crore during 2003-04 as against

Rs. 3.50 crore during 2002-03. While there was a decline in the number of counterfeit notes detected in Rs.500 denominations, there was increase in the number of notes detected in Rs. 100 and Rs.1000 denominations (Table 12.5). Sustained public awareness campaigns on security features of notes were conducted during the year through print and electronic media. Necessary training for detection of counterfeit notes was also imparted to the staff from banks as well as large public sector undertakings and government departments such as Railways.

12.16 The Reserve Bank and the Central Bureau of Investigation (CBI) jointly conducted a workshop on counterfeiting, security features of notes and detection of counterfeit notes with participants from senior level police officers from States/Union Territories, National Crime Record Bureau (NCRB), Ministry of Home Affairs and Ministry of Finance.

Table 12.5: Counterfeit Notes Detected

(No. of pieces)

Denomination	2003-04	2002-03
1	2	3
Rs. 1,000	248	39
Rs. 500	17,783	35,398
Rs. 100	1,82,361	1,72,597
Rs. 50	4,701	3,488
Rs. 20	56	34
Rs. 10	77	198
Total	**2,05,226**	**2,11,754**

Mahatma Gandhi Series Notes

12.17 The Mahatma Gandhi series of notes with enhanced security features were introduced from 1996. With the advancement in reprographic techniques, earlier security features were no longer considered sufficient to deter forgeries. Accordingly, new security features have been progressively built into these notes over the period since their introduction (Box XII.2).

Box XII.2
Security Features of Mahatma Gandhi Note Series

Security features of bank notes of the Mahatma Gandhi Note Series are set out below:

Watermark: The Mahatma Gandhi Series of bank notes contain the Mahatma Gandhi watermark with a light and shade effect and multi-directional lines in the watermark window.

Security Thread: Rs. 1000 notes contain a readable, windowed security thread alternately visible on the obverse with the inscriptions 'Bharat' (in Hindi), '1000' and 'RBI', totally embedded on the reverse. The Rs.500 and Rs.100 notes have a security thread with similar visible features and inscription 'Bharat' (in Hindi), and 'RBI'. When held against the light, the security thread on Rs.1000, Rs.500 and Rs.100 notes can be seen as one continuous line. The Rs.5, Rs.10, Rs.20 and Rs.50 notes contain a readable, fully embedded windowed security thread with the inscription 'Bharat' (in Hindi) and 'RBI'. The security thread appears to the left of Mahatma Gandhi's portrait.

Latent Image: On the obverse side of Rs.1000, Rs.500, Rs.100, Rs.50 and Rs.20 notes, a vertical band on the right side of Mahatma Gandhi's portrait contains a latent image showing the respective denominational value in numeral. The latent image is visible only when the note is held horizontally at eye level.

Micro lettering: This feature appears between the vertical band and Mahatma Gandhi's portrait. It contains the word 'RBI' in notes of Rs.5 and Rs.10. Notes of Rs.20 and above also contain the denominational value in micro letters. This feature can be seen better under a magnifying glass.

Intaglio Printing: The portrait of Mahatma Gandhi, the Reserve Bank's seal, the guarantee and promise clause, the Ashoka Pillar Emblem on the left and the Governor's signature are printed in intaglio, *i.e.,* in raised prints, which can be felt by touch in Rs.20, Rs.50, Rs.100, Rs.500 and Rs.1000 notes.

Identification Mark: A special feature in intaglio introduced on the left of the watermark window on all notes except the Rs.10/- note assigns different shapes for various denominations (Rs. 20-Vertical Rectangle, Rs.50-Square, Rs.100-Triangle, Rs.500-Circle and Rs.1000-Diamond) to help the visually impaired to identify the denomination.

Fluorescence: Number panels of the notes are printed in fluorescent ink. The notes also have optical fibres. Both can be seen when the notes are exposed to ultra-violet lamp.

Optically Variable Ink: A new security feature was incorporated in the Rs.1000 and Rs.500 notes with revised colour scheme introduced in November 2000. The numerals 1000 and 500 on the obverse of Rs.1000 and Rs.500 notes, respectively, are printed in optically variable ink, *viz.*, a colour-shifting ink. The colour of the numeral 1000/500 appears green when the note is held flat but would change to blue when the note is tilted.

See Through Register: The small floral design printed both on the front (hollow) and back (filled up) of the note in the middle of the vertical band next to the watermark has an accurate back to back registration. The design will appear as one floral design when seen against the light.

References

1. Balachandran, G. (1998), '*The Reserve Bank of India, 1951-67*', Oxford University Press.
2. Bazil Shaik and Sandhya Srinivasan, (2001), '*The Paper and the Promise: A Brief History of Currency and Bank Notes in India*', Reserve Bank of India.
3. Reserve Bank of India (2001), '*Functions and Working of the Reserve Bank of India*'.

Computerisation of Currency Management

12.18 The Reserve Bank is putting in place an Integrated Computerised Currency Operations and Management System (ICCOMS) in the Issue Departments of the regional offices of the Reserve Bank and in the Department of Currency Management at the Central Office. The project includes computerisation and networking of the currency chests with the Reserve Bank's offices to facilitate prompt, efficient, error-free reporting and accounting of currency chest transactions in a secure manner. The system will provide a uniform computing platform across all the regional offices for transaction processing, accounting and management information system relating to currency.

Customer Service

12.19 The Reserve Bank stepped up efforts to improve customer services in the issue of coins, acceptance of coins from public and exchange of soiled and mutilated notes. The Reserve Bank introduced a single window customer service at its Issue Offices under which coins and notes of all denominations are either issued or accepted at one counter. Similarly, mutilated notes are accepted in a Drop Box (even beyond normal banking hours) without any limit. A noteworthy development in this regard in 2003-04 was the constitution of a Committee on Procedures and Performance Audit on Public Services (Chairman: Shri S.S. Tarapore) to study, *inter alia*, services relating to individuals (non-business) on currency management (Box XII.3).

Reserve Bank Monetary Museum

12.20 The Reserve Bank is setting up a Monetary Museum in Mumbai to preserve the country's monetary heritage. The Museum is the first of its kind in the country and aims to depict the history of currency and the evolution of money in India. The Museum would exhibit representative collection of coinage, paper currency, financial instruments and curiosities across the Indian history. The main exhibit sections of the Museum relate to concepts, ideas and curiosities; coinage – from coins to bank notes – and advent of banking in India.

12.21 The entire display has been divided into self-contained thematic modules. The coinage section spans a period going back from the early issues of punched marked coins in the sixth century B.C. to the contemporary Republic of India coins. The notes on display date from the early nineteenth century and consist of notes issued by private and semi-government banks, the Government of India and the Reserve Bank. The section on Financial Instruments depicts hundies, cheques and promissory notes, used in India. The Museum also houses portraits of Governors of the Reserve Bank.

The Bharatiya Reserve Bank Note Mudran Pvt. Ltd

12.22 The total production of notes by the two presses of the Bharatiya Reserve Bank Note Mudran Pvt. Ltd. (BRBNMPL) at Mysore and Salboni increased by 34 per cent to 8,100 million pieces during the year 2003-04 as compared with 6,049 million pieces in the previous

Box XII.3

Committee on Procedures and Performance Audit on Public Services

The major recommendations of the Committee, which have been accepted by the Reserve Bank, are:

- Transparency in currency management;
- Early introduction of Rs.10 coin;
- Phasing out of Rs.5 note totally;
- Currency Chest Agreement to be revised to incorporate a provision for monetary penalty for non-compliance with the Reserve Bank's instructions;
- A Systems Study of Banking Hall arrangements in the Mumbai Office of the Reserve Bank to be commissioned with the help of a specialised agency to resolve the bottlenecks in the smooth flow of transactions;
- Suitable measures to separate location/time for services to money changers and other individuals;
- Citizens' Charter for Currency Exchange Facilities be made available to customers visiting the Banking Halls of the Reserve Bank offices and bank branches;
- Authorised bank branches to exhibit prominently a notice that soiled/mutilated currency notes are freely exchanged at the bank branch;
- The Reserve Bank Note Refund Rules to be written in easily understandable language;
- The practice of pasting of mutilated notes at the time of tendering for exchange should be reviewed by the Reserve Bank; and
- Stringent action to be taken against violation of instructions by banks on exchanging soiled/mutilated notes.

Reference

1. Reserve Bank of India (2004), 'Committee on Procedures and Performance Audit on Public Services', May.

year. The sales turnover increased by 22.0 per cent to Rs. 813 crore during 2003-04 from Rs. 667 crore in the previous year. The company achieved a net profit of Rs.135 crore during 2003-04 as compared with Rs.274 crore during the previous year. The decline in profit was due to reduction in the sale price and certain adjustments in booking of interest income in respect of loans extended to the Government of India presses. The company repaid the outstanding balance of long-term loans of Rs.1,300 crore and working capital of Rs.175 crore to the Reserve Bank by switching over credit facilities to the State Bank of India (SBI). The company was certified as "ISO 14001-1996 Company" during the year.

Outlook

12.23 The Reserve Bank would continue to pursue the objective of meeting the currency demand of the economy and improving the quality of notes. Installation of additional Currency Verification and Processing Systems would be undertaken to ease the pressure of accumulation of soiled notes. Customer service would be upgraded further. A sustained campaign against counterfeiting is being devised along with greater emphasis on enhanced security features. The Reserve Bank would continue to facilitate the circulation of clean notes in the economy. It intends to implement the Integrated Computerised Currency Operations and Management System (ICCOMS) in all its offices and major currency chests during 2004. The process of design and development of software for the system is in progress. This will be followed by testing on a pilot basis at currency chests and select offices of the Reserve Bank. In view of the magnitude and spread, a process of dialogue with banks has been initiated to work out the modalities for testing, training, trial run and implementation. The Information Technology (IT) initiatives taken by banks for computerisation of branch operations, coupled with advances in the communication facilities in the country, would provide the necessary platform for successful implementation of the ICCOMS across all banks throughout the country. These measures would provide an enabling environment for smooth currency management.

XIII PAYMENT AND SETTLEMENT SYSTEMS AND INFORMATION TECHNOLOGY

13.1 The development of payment and settlement systems conforming to the best international standards has been a key objective of the Reserve Bank. A milestone was crossed during 2003-04 with the commencement of the Real Time Gross Settlement (RTGS) as a facility available for quick, safe and secure electronic mode of funds transfer. Preparation of the draft legislation relating to payment and settlement systems was another important development. The legislation aims at providing a sound legal basis to various payment and settlement systems operating in India and empowers the Reserve Bank to regulate and supervise such systems.

13.2 This Section profiles the significant expansion of activity in the payment systems in India and the key drivers – retail payments and the rising popularity of card-based transactions, large value payments propelled by rising turnover in the inter-bank clearing, Negotiated Dealing System (NDS) and foreign exchange clearing segments. Noteworthy landmarks in the evolution of payment systems highlighted in this Section are the implementation of Real Time Gross Settlement (RTGS) system, the Special Electronic Funds Transfer (SEFT) system and the foundation being laid for the constitution of a Board for Payment and Settlement Systems as an apex regulatory authority. Reviewing developments in the settlement systems in India in 2003-04, the Section highlights the continuing preponderance of paper-based (cheque) clearing and the preparatory steps being taken to introduce cheque truncation to improve the speed and efficiency of paper-based settlement systems. The implementation of Online Tax Accounting System (OLTAS) to IT-enable tax payment as well as tax administration is brought out in this Section along with developments relating to the Indian Financial Network (INFINET) and Structured Financial Messaging Solution (SFMS). The role of central counter parties (CCPs) in minimising settlement risks is underscored. The Section concludes with a review of the growing role of information technology (IT) within the Reserve Bank and the special emphasis being laid on information security and disaster recovery management.

PAYMENT SYSTEMS

13.3 The overall turnover through the various payment and settlement systems rose by 1.4 per cent during 2003-04 to Rs.1,60,15,716 crore. This was mainly in the form of retail payment such as Electronic Clearing Services (ECS), Magnetic Ink Character Recognition (MICR) and Non-MICR clearing (Table 13.1). The substantial increase in repo transactions (outside the Reserve Bank's LAF) and the onset of foreign exchange clearing resulted in a sizeable increase in the value of turnover under the Negotiated Dealing System (NDS) and the foreign exchange clearing.

Retail Payment Systems

13.4 Retail payment systems constitute the bulk of the volume of payment transactions of the country. The settlement of the retail systems is typically

Table 13.1: Payment System Indicators – 2003-04

Component	Volume (000s)	Value (Rupees crore)	
1	2	3	4
Systemically Important Payment Systems (SIPS)			
1. Inter-bank Clearing	1,142 (1,039)	30,46,666 (60,65,825)	
2. High Value Clearing	13,172 (7,207)	30,23,290 (28,86,263)	Cheques of Rs. 1 lakh and above
3. NDS	265 (203)	25,18,323 (15,45,673)	Settlement through CCIL
4. Forex Clearing	331 (200)	23,18,530 (6,58,035)	Settlement through CCIL
5. RTGS @	76@	2,031	
Total-SIPS (1 to 5)	**14,910 (8,649)**	**109,08,840 (111,55,796)**	
Others			
6. MICR Clearing	6,24,360 (4,79,189)	20,35,934 (18,43,726)	At 39 centres
7. Non-MICR Clearing	3,34,039 (3,61,400)	30,05,139 (27,45,307)	Includes all other paper based clearing
8. Electronic Clearing	29,046 (23,660)	29,933 (10,222)	Comprising ECS, EFT and SEFT
9. Cards	1,85,501	35,870	Including credit, debit and smart cards
Total-Others (6 to 9)	**11,72,946 (8,64,249)**	**51,06,876 (45,99,255)**	
Grand Total	**11,87,856** (8,72,898)	**1,60,15,716** (1,57,55,051)	

@ : RTGS became operational on March 26, 2004; 76 transactions took place by end-March, 2004.

Note : Figures in parentheses represent data for 2002-03.

accomplished in the form of Deferred Net Settlement (DNS) Systems. The predominant mode of retail payments comprises the cheque clearing system (constituting the MICR and Non-MICR clearings). Other systems, which include electronic systems such as the Electronic Clearing Service (ECS – Debit and Credit), Electronic Funds Transfer (EFT), the Special EFT (SEFT) and card based systems (credit, debit, ATM and smart cards), are gaining acceptance. While ECS-Credit and ECS-Debit systems are for bulk payments akin to the automated clearing houses (ACH) elsewhere, the EFT and SEFT systems are for individual transactions. The ECS-Credit, EFT and SEFT systems are credit transfer based modes of payments, whereas the ECS-Debit system is based on direct debits. All the retail electronic payment modes have grown considerably during the year, reflecting their growing popularity (Table 13.2).

Smart Cards

13.5 The Reserve Bank partnered a pilot project on smart cards in 1999 in order to provide for large scale usage of smart cards for financial transactions. With the spread of rapid technological developments and the potential of the usage of smart cards for many purposes, the Reserve Bank teamed up with the Government of India, the academia, banks and the card industry to conduct another pilot project for the use of smart cards for multiple purposes. The Multi-Application Smart Card Project is in the nature of a commercial pilot conducted jointly by the Indian Institute of Technology (IIT), Mumbai and the Institute for Development and Research in Banking Technology (IDRBT), Hyderabad. It has participation from banks and industry stakeholders such as card manufacturers, terminal providers and network service providers. The pilot project is expected to address various issues relating to technology, security, regulatory and supervisory concerns and legal implications. It would enable the identification of common, inter-operable and open standards for use on a large scale. The project is aimed at including applications relating to banking, insurance, postal services, citizen identification and health, apart from financial applications such as credit, debit and e-purse all on a single card.

Table 13.2: Retail Electronic Payment Transactions – 2003-04

Type	Volume of transactions (000s)	Growth in volume (per cent)	Value of transactions (Rs. crore)	Growth in value (per cent)
1	2	3	4	5
ECS-Credit	20,315 (18,753)	8.33	9,676 (6,862)	40.99
ECS-Debit	7,874 (4,538)	73.51	2,241 (1,033)	116.95
EFT	775 (370)	109.46	15,711 (2,327)	575.16
SEFT	82		2,304.99	
Credit Cards	97,405		17,268	
Debit Cards	86,379		18,513	
Smart Cards	1,717		89	

Note: Figures in parentheses represent data for 2002-03.

13.6 With a view to providing for transfer of funds electronically across a large number of bank branches in the country as a forerunner to the nationwide funds transfer system (NEFT), the Special Electronic Funds Transfer (SEFT) System was introduced from April 1, 2003. It has succeeded in ensuring faster credit transfers to branches that are computerised and networked even though they are situated at locations where the Reserve Bank does not have a presence. The settlement is centralised at Mumbai and the system provides for same day funds settlement with multiple settlements during the day. SEFT covers 2,312 branches of 29 banks situated in 127 cities across the country. This system has facilitated the introduction of the T+2 rolling settlement system by stock exchanges in the country.

13.7 Card based transactions have emerged as the most preferred among all the retail electronic modes of payments due to proliferation and increasing usage of debit cards.

Large Value Payment Systems

13.8 Large value payment systems in India comprise the Inter-Bank Cheque Clearing and the High Value Clearing for paper based systems; the Negotiated Dealing System (NDS), the Inter-Bank Foreign Exchange Transactions Clearing and Settlement System (Forex Clearing) and the Real Time Gross Settlement System (RTGS) for the electronic mode based systems. During the year, RTGS was introduced parallel with the existing Inter-Bank Cheques Clearing system with the ultimate objective of migrating to the RTGS completely (Box XIII.1). RTGS would be extended throughout the country covering around 3,000 bank branches in about 275 centres.

13.9 The RTGS system requires continuous funding for settling transactions. Internal funding by participants may, therefore, prove costly on account of opportunity costs, leading to delay in outgoing payment instructions. The provision of intra-day credit facilities extended either by the market or by the central bank is regarded as a circuit-breaker. Liquidity

Box XIII.1

RTGS Implementation in India

With the commencement of the operations of the Real Time Gross Settlement (RTGS) system from March 26, 2004 India crossed a major milestone in the development of systemically important payment systems (SIPS) and complied with the Core Principles framed by the Bank for International Settlements (BIS). It was a 'soft' launch with four banks, besides the Reserve Bank, as participants. In addition to the service provider, the Reserve Bank is also a participant in the RTGS System. Currently, there are 71 direct participants in the RTGS system. Scheduled banks, primary dealers and clearing houses numbering around 125 are the targeted members.

The RTGS system started with pure inter-bank transactions. Customer based inter-bank transactions were permitted to be settled through the system, effective April 29, 2004. The RTGS system will be fully integrated with the accounting system of the Reserve Bank and other payment systems and services.

Salient features of the RTGS system are:

- Payments are settled transaction by transaction for high value and retail payments;
- Settlement of funds is final and irrevocable;
- Settlement is done on a real time basis and the funds settled can be further used immediately;
- It is a fully secure system which uses digital signatures, and Public Key Infrastructure (PKI) based encryption for safe and secure message transmission;
- There is a provision for intra-day collateralised liquidity support for member banks to smoothen the temporary mismatch of fund flows.
- RTGS provides for transfer of funds relating to inter- bank settlements as also for customer related fund transfers.

  More than 75 per cent of the value of inter-bank transactions, which was earlier being settled through the deferred net settlement systems (DNSS) based Inter-bank clearing, is now being settled under the RTGS.

requirements for settlement of transactions under the RTGS system are met through intra-day liquidity support to the members by the Reserve Bank on a collateralised repo basis (Box XIII.2).

Box XIII.2

Intra-day Liquidity under RTGS System

Payment systems based on discrete time are known as deferred net settlement systems (DNSS), while continuous-time settlement systems are referred to as real time gross settlement (RTGS) systems. Under DNSS, each participant pays/receives only the net amount. Typically, the central bank acts as the settlement agency by debiting/crediting current accounts maintained by the participants with it. The RTGS system, on the other hand, embodies settlement of transactions instantaneously, *i.e.*, on a gross basis, thereby completely obviating the need for any clearing arrangement in the transaction. The advantage of DNSS is a lower level of collateral/settlement balance requirement for effecting payment transactions as against higher level of collateral/settlement balance under RTGS system. Settlement risk in the event of default is, however, higher under DNSS.

The Reserve Bank would provide the intra-day liquidity (IDL) to RTGS participants. This may eliminate liquidity risk but the credit risk is transferred from the participants to the central bank. Cross-country experiences in dealing with credit risk show that central banks may (i) adopt strict membership standards for participants; (ii) require full collateralisation with suitable margin; and (iii) enforce participant-wise caps for granting intra-day credit.

The underlying principle in a intra-day credit facility is that participants must extinguish it by the close of the day by *fiat* money to the central bank. Thus, the stock of reserve money which expands during the course of the day returns to its initial level. The Reserve Bank would charge Rs.25 per transaction following the recommendations of the Working Group on Intra-day Credit Facility (Chairman: Shri A. B. Telang). In order to minimise credit risk, IDL would be provided against Central Government marketable securities with appropriate haircut up to a limit of three times of net owned funds (NOF) (Tier-I capital) as per the latest audited balance sheet. It is imperative to ensure that there exists a firewall between the intra-day and inter-day markets so that users would not have any incentive to use such funds for speculative purposes. Accordingly, if a participant is unable to extinguish its intra-day repo position during the course of the day, the outstanding amount would attract a penal rate pegged at twice the Bank Rate or twice the corresponding day's maximum call money rate, whichever is higher. If this breach *(i.e.,* spillover to the overnight loan) occurs once, the participant would have to pay the penalty, besides being cautioned by the Reserve Bank. The account would also be placed under surveillance. If it happens for a second time in a six-month period, the intra-day facility would be suspended by the Reserve Bank and supervisory surveillance would be triggered. For restoration of the intra-day facility, reasonable evidence has to be provided to the Reserve Bank that prudential treasury management is in place. If after restoration, it recurs for the third time during the six-month period, the intra-day facility would be withdrawn permanently. For this purpose, the six-month period would cover April-September and October-March and intra-day maturity would be defined as the length of the official working hours in a day.

Reference

1. Reserve Bank of India (1999), ‘Report of the Working Group on Intra-day Credit Facility’.

13.10 The RTGS has the capability to settle retail payments also. Along with the RTGS and the SEFT, banks in almost all the commercially important centres of the country have the capability to offer their customers country-wide electronic modes of fund transfer services.

13.11 The apex-level National Payments Council (NPC) has overseen the reforms in the payment and settlement systems since 1999. In order to create the appropriate regulatory and supervisory infrastructure for the payment and settlement systems in the country, a Board for Payment and Settlement Systems is proposed to be constituted (Box. XIII.3). The Board, which would comprise members of the Central Board of Directors of the Reserve Bank, would oversee the overall functioning of the payment and settlement systems of the country. A Department of Payment and Settlement Systems within the Reserve Bank would assist the Board in carrying out its functions

SETTLEMENT SYSTEMS

Paper Based Clearing

13.12 Cheque clearing continued to be the most important retail settlement system in terms of volume, with its share being 81 per cent in total transactions recorded during 2003-04. MICR-based clearing operations, which commenced in 1986 at the four major metropolitan centres, is emerging as an efficient method for processing paper based funds movement. Expansion of the coverage of MICR technology is being pursued in a phased manner. During the year, 12 more centres (Rajkot, Allahabad, Gwalior, Jodhpur, Varanasi, Kozhikode, Thrissur, Bhubaneshwar, Nashik, Raipur, Jabalpur and Vishakapatnam) commenced MICR based clearing using state-of-the-art reader sorter-based processing capabilities, taking the total number of MICR Centres to 39. These centres account for about 70 per cent of the cheque volumes of the country.

13.13 The Reserve Bank initiated arrangements with the State Bank of India to set up back-up MICR Cheque Processing Centres. While the back-up centres at Chennai and Mumbai were set up in 1998 and 1999 respectively, the centres at Delhi and Kolkata were made operational during 2003-04. Testing of the back-up centres with full volumes is conducted periodically to take care of any contingency. Centres situated nearby can operate as back-up centres for one another.

Box XIII.3
Board for Payment and Settlement Systems

Cross-country experience indicates that there are special administrative arrangements for regulation and oversight on payment and settlement systems. These arrangements are in the form of a board, council or a committee, constituted either within the ambit of central banks or under specific statutory provisions. In Australia, the Reserve Bank Act (1959) gives the Payments System Board the responsibility for determining the Reserve Bank of Australia payments system policy. The European Central Bank (ECB) has set up the Payment and Settlement Systems Committee (PSSC) to deal with issues of oversight and development of payment systems. In contrast, the South African Reserve Bank regulates and oversees the activities of the payment system management body, called the Payments Association of South Africa (PASA) and of its members. In Canada, the regulatory responsibility for payments system is shared between the Bank of Canada and the Ministry of Finance.

Efforts are also underway in India to build the infrastructure for effective regulation and supervision of payment and settlement systems in anticipation of the statutory changes envisaged under the draft 'Payment and Settlement Systems Bill'. A Board for Payment and Settlement Systems (BPSS) is proposed to be constituted under the Reserve Bank of India Act, 1934, which will be in the form of a Committee of the Central Board of Directors of the Reserve Bank. The mandate of the BPSS would cover:

- Laying down policies for regulation and supervision of the payment and settlement systems, both electronic and non-electronic systems as well as domestic and cross-border systems;
- Laying down the standards for both existing and future payment and settlement systems;
- Determining the criteria for access to membership, continuance of membership, removal from membership as well as denial of membership of entities to the various payment and settlement systems;
- Fixing and administering penalties for violation of rules/guidelines/directions.
- Pending the enactment of the Payment and Settlement Systems Act, the BPSS will create the necessary administrative structure within the existing rules and regulations for ensuring the effective regulation and supervision of the payment and settlement systems.

13.14 Reduction of the time taken for processing of paper-based instruments has been engaging the attention of the Reserve Bank. To the extent that the physical instrument needs to be transported from the collecting bank branch to the drawee bank branch, delay is in-built into the paper based instrument clearing mechanism. Cheque truncation is one of the measures adopted in several countries to remove this systemic handicap. Payment instruments do not get transported all the way, but get stopped or truncated at a point in the cycle and thereafter, only information about the instrument and/or its image flows electronically to the drawee bank branch for payment. A Working Group on Cheque Truncation and E-cheques (Chairman: Dr. R.B. Barman) was constituted to recommend a suitable model of cheque truncation for India. The Group submitted its report in July 2003 (Box XIII.4). Preparatory steps for implementation of cheque truncation on a pilot basis were initiated in the National Capital Region of Delhi during the year.

13.15 The use of Automated Teller Machines (ATM) has been growing rapidly and this has helped in optimising the investments made by banks on infrastructure. Encouraged by the Reserve Bank, banks joined together in small clusters to share their ATM networks during the year. There are five such ATM network clusters functioning in India. In order to facilitate inter-operability among these clusters at the national level, the IDRBT has initiated the process of setting up a National Financial Switch to facilitate apex level connectivity of other switches established by banks. The total number of ATMs installed by the public sector banks stood at 8,219 at end-March 2004 as compared with 5,963 ATMs at end-March 2003.

13.16 Guaranteed settlements minimise risks in net settlement systems. The role of central counter parties (CCPs) is very crucial in this regard. The risk management policies, procedures and practices of the CCPs have been receiving international attention. The BIS Task Force on Risk Management for the CCPs - a joint Group of the Committee on Payment and Settlement Systems (CPSS) and the International Organisation of Securities Commission (IOSCO) - released its recommendations on CCP in January 2004 (Box XIII.5).

Online Tax Accounting System (OLTAS)

13.17 Implementation of OLTAS was initiated during the year on a pilot basis. Jointly developed by the Government and the Reserve Bank, the OLTAS has several benefits in terms of streamlining tax payment procedures, improving tax administration and building up an information base as an input for policy formulation (Box XIII.6).

13.18 The implementation of OLTAS has been undertaken in a phased manner. It was introduced on a pilot basis in June 2003 covering 48 branches of 16 banks in four cities. Currently, OLTAS Pilot Project – IV, which spans all the designated banks, branches

Box XIII.4

Cheque Truncation Model for India

The Working Group on Cheque Truncation and E-cheques recommended an image based cheque truncation at the presenting bank for all cheques, irrespective of value, beginning with the four metro centres. The physical cheques will be truncated within the presenting bank to derive maximum efficiency and settlement will be generated on the basis of the current structure of the MICR fields. Electronic images will be used for payment processing. Grey Scale technology for image capture will be used for imaging. The preservation period of paper instruments will be one year and that of the electronic images will be eight years. A centralised agency per clearing location will act as an image warehouse for banks. Minimum entry norms for the warehouse agency such as technical competency, efficiency orientation and size of resources have been recommended.

Deployment of Public Key Infrastructure (PKI) to protect data and image flow over the network and to establish authenticity, non-repudiation and integrity and use of digital signatures is another recommendation of the Group. Certification process based on Information Security Audit guidelines of the Reserve Bank for participants has been recommended. Countermanding payments and recording stops will be allowed till the time of payment, as is the existing practice. The implementation of cheque truncation will result in accelerated cheque clearing and settlement process, especially for the outstation cheques.

A pilot cheque truncation project is to be undertaken in the National Capital Region of Delhi and nearby areas. Tenders for the procurement of the central system for the Clearing House at Delhi were floated and the process of evaluation of the technical bids received from vendors is currently under progress. Banks have been advised to take initial steps for procuring the requisite systems at their end.

Reference

1. Reserve Bank of India (2003), ‘Working Group on Cheque Truncation and E-cheques’, July.

Box XIII.5

Central Counter Parties

A Central Counter Party (CCP) is an entity which interposes itself between counterparties to financial contracts in one or more markets, becoming the buyer to every seller and the seller to every buyer. By doing so, the CCP assumes the counterparty risk associated with each buyer and seller. Central counterparties play an important role in ensuring smooth clearing and settlement of financial transactions through containment of settlement risk. CCPs have long been used by derivatives exchanges and a few securities exchanges and trading systems. In recent years, they have begun to provide their services to Over-The-Counter (OTC) markets also, including the markets for fixed income securities for outright as well as repo transactions like the Clearing Corporation of India Limited (CCIL).

The effectiveness of a CCP's risk controls and the adequacy of its financial resources are critical aspects of the infrastructure of the markets it serves. A risk management failure by a CCP has the potential to disrupt the markets. Therefore, securities regulators and central banks have a strong interest in risk management systems of the CCP. In November 2001 the Committee on Payment and Settlement Systems (CPSS) of the central banks of the Group of Ten countries and the Technical Committee of the International Organisation of Securities Commissions (IOSCO) issued a report entitled Recommendations for Securities Settlement Systems (RSSS). Under Recommendation 4, each CCP is to rigorously control the risks that it assumes. The Task Force on Securities Settlement Systems, with representatives from central banks and security regulators from 19 countries and other international organisation like the IMF, the World Bank and the BIS, was mandated to develop standards for risk control by CCPs. The report of the Task Force, released for public comments, recommends:

- A well-founded, transparent and enforceable legal framework for each aspect of CCP activity in all relevant jurisdictions;
- Sufficient financial resources and robust operational capacity to meet obligations arising from participation in the CCP;
- Calculation of the CCP's credit exposures to participants on a daily basis and holding collateral which, in normal market conditions, covers its potential losses from closing out positions held by a defaulting participant;
- Maintenance of sufficient financial resources to withstand a default by the participant to which it has the largest exposure in extreme but plausible market conditions that produce losses not fully covered by collateral requirements;
- Clear and transparent default procedures to ensure that the CCP can take timely action to contain losses and liquidity pressures.
- Holding assets in instruments with minimal credit, market and liquidity risks.
- Identification of sources of operational risk and minimising them through the development of appropriate systems, controls, procedures and business continuity plans;
- Money settlement arrangements that eliminate or strictly limit settlement risks - funds transfers to the CCP should be final when effected;
- Clear statement of obligations with respect to physical deliveries, with risks from these obligations identified and managed;
- CCPs that establish links either cross-border or domestically to clear trades should design and operate such links in ways that observe the other recommendations contained in the report.
- Cost-effectiveness in meeting the requirements of users while maintaining safe and secure operations;
- Effective, clear, and transparent governance arrangements for a CCP ; and
- Provision of sufficient information to market participants to identify and evaluate accurately the risks and costs associated with using its services.
- A CCP should be subject to transparent and effective regulation and oversight.

Reference

1. Bank for International Settlements (2004), *'Recommendations for Central Counterparties, Consultative Report of Committee on Payment and Settlement Systems',* January.

and centres, is in progress on a live mode. Of the 11,000 bank branches connected, more than 5,150 branches collected 8.58 lakh challans that were transmitted under the OLTAS project during the quarter January-March 2004.

Payment System Infrastructure and Utilities

13.19 The Indian Financial Network (INFINET), established by the IDRBT as the secure, exclusive communication backbone for the banking and financial sectors, registered further growth during the year with the membership going up to 163. The bandwidth of the network was considerably enhanced to meet the growing demand and for improving performance and availability. The terrestrial links of the network between the metropolitan centres were upgraded to 4 mega bytes per second (mbps) from 2 mbps, while the links connecting other centres were upgraded to 2 mbps

Box XIII.6

Online Tax Accounting System

The Income Tax Department has set up a National Tax Information Network (TIN) to act as a repository of all taxpayer related information, including payment and refund of taxes. It would enable assessees to pay taxes and get refunds electronically, besides providing the Income Tax Department with information for accounting in a scientific and accurate manner. As a part of TIN, an Online Tax Accounting System (OLTAS) has been conceived. Under the OLTAS, a network of about 11,000 branches of various banks authorised for collection of tax receipts has been established. The Reserve Bank and the Tax Information Repository at the National Securities Depository Ltd. (NSDL) are also part of the OLTAS. Data are captured from the challans submitted by tax payers tendered at the designated bank branches and transmitted electronically to the repository. The collection and transmission of data on tax collections is on a T+1 cycle basis. The OLTAS works in a fully secured environment, with data being transmitted using encryption facilities and digital signatures for enhanced security.

from 64 kilo bytes per second. The link between Mumbai and Hyderabad was quadrupled to 8 mbps. Furthermore, connectivity to INFINET was enabled through Integrated Services Digital Network (ISDN) channels to provide redundancy so that additional mode of access is available. The INFINET has become a hybrid network with satellite, terrestrial and ISDN connectivities. Wireless connectivity in the form of radio frequency links is also being tested to enhance its robustness.

13.20 The INFINET's Structured Financial Messaging Solution (SFMS), which is a domestic messaging system similar to the system of the Society for Worldwide Interbank Financial Telecommunication (SWIFT), was upgraded during the year to allow transmission of files in a secure manner. Initiatives are being contemplated for providing access to SFMS through the Internet. This would facilitate the usage of SFMS by a larger section of the financial community and provide for seamless integration of messages with members of the INFINET as also with other financial sector participants.

13.21 As part of measures aimed at enhancing the facilities available through INFINET, the IDRBT is constantly providing upgrades to the network. Some of the activities planned for the near future include the provision of increased bandwidth in the form of increasing the capacity of the leased lines between the major metropolitan centres to 8 mbps and across other cities to 2 mbps. The Network Management System (NMS) at the IDRBT would closely monitor availability of the network so that the high levels of availability (which is in excess of 99.9 per cent) are maintained.

INFORMATION TECHNOLOGY IN THE RESERVE BANK

13.22 The primary role of information technology (IT) within the Reserve Bank is to support its business objectives and to provide efficient customer services. A Strategic Information Technology Plan (SITP) is being prepared to provide the framework for effective management of information technology resources in the Reserve Bank. The plan is built on an IT management model based on both centralised and decentralised IT management, decision making and support.

13.23 Information security is a key requirement in a technology intensive environment. A comprehensive Information Security Policy (ISP) covering the various information assets of the Reserve Bank was prepared following international best practices and codes, including the ISO 17799 code on Information Security (Box XIII.7).

Box XIII.7

Information Security Policy

The objective of the Information Security Policy is "to provide the Reserve Bank with a critical minimum information security framework to address and manage various security risks to information assets and quality maintenance". These assets include information processing facilities, information system functions, information shared electronically, information transmitted by mail or through other communication media, information transmitted through computer network or other electronic means and information stored or reprinted on paper.

The IS Policy categorises information based on its nature of sensitivity. The Policy will apply to all the units of the Reserve Bank, subsidiaries and managed affiliates which share IT resources. It will also apply to all service providers who perform any function of relevance. The policy will be supplemented by the best practices, procedures and guidelines for IT / Information Security.

Box XIII.8
Disaster Recovery Management and Business Continuity Plan

The Disaster Recovery Management and Business Continuity Plans (BCP) have gained significance after the events of September 11, 2001. Considerable emphasis is placed on regular review, updating and testing of disaster recovery and business continuity plans.

The Reserve Bank has adopted a dual strategy for its DRS/BCP - one for mission critical applications and the other for other applications. The approach towards Business Continuity is to ensure that in case of any contingency, operations are resumed within a minimal time gap of two hours in the case of mission critical applications and within a day in the case of others. While both the applications will have off-city recovery and business continuity site/s, the mission critical applications will have on-city recovery and continuity site as well. The IT resources and assets will be consolidated in the form of Data Centres both at the Primary Site and at the Recovery and Continuity site/s. Data processing requirements of the Central Office Departments (CODs) would be provided by the systems at the Data Centre. Normal day-to-day operations of the regional office (RO) applications and other locations would work independently, *i.e.*, independent of the Data Centres but would provide means to upload daily transactions to these Data Centres. In case of an emergency, the affected COD/RO would operate the computer systems from the Data Centre/s either remotely from the affected location or from its application from any of the two Data Centres.

IT Efforts in the Reserve Bank

13.24 One of the key objectives for IT implementation within the Reserve Bank is to ensure desktop computing capability for every employee, which would result in a 1:1 ratio in respect of computers and employees. An Intranet of the Urban Banks Department (UBD), which acts as a common platform for communication between its regional offices and the central office, was made operational. The Centralised Public Debt Office Module under the integrated PDO-NDS-SSS system was implemented in all 14 Public Debt Offices (PDOs) of the Reserve Bank. Live operations on the Primary Market Operations (PMO) Module commenced from October 20, 2003. The second phase of the Centralised Funds Management System consisting of the Funds Transfer module with latest Public Key Infrastructure (PKI) - based security is ready for implementation. It will provide Straight Through Processing (STP) capability for banks. The Integrated Establishment System (IES) - a platform for establishment related payments/recoveries apart from payroll processing - is scheduled to be operational by July 2004.

13.25 In order to provide internet banking services to the customers of the Reserve Bank, a secured Internet Website was established and is currently under testing. This system will facilitate two-way electronic access to those constituents who are not members of the INFINET. A blue print for an Enterprise Knowledge Management System (EKMS) will be implemented in stages.

Disaster Recovery Management

13.26 Critical importance was attached to the back-up and disaster recovery management systems in 2003-04. Two geographically dispersed sites were identified as back-up/disaster recovery and data centres are being set up at these locations. The back-up site established for mission critical applications was tested for live operations during the year (Box XIII.8).

Outlook

13.27 The Reserve Bank is committed to providing a safe, secure, efficient and integrated payment and settlement system for the country. The operationalisation of the RTGS would greatly facilitate the optimum utilisation of funds. The draft bill on the constitution of the Board for Payment and Settlement Systems under the Reserve Bank of India Act, 1934 would provide an explicit legal sanction to the Reserve Bank's oversight of payment and settlement systems. The INFINET is emerging as the communication backbone for the banking and the financial sector. Cheque truncation is expected to reduce the delay in payment system considerably. Continuous efforts towards upgradation of technology within the Reserve Bank would help in improving its customer services. Initiatives for setting up disaster recovery management would gather momentum with comprehensive business continuity plans to anticipate disasters and cope with them.

XIV HUMAN RESOURCES DEVELOPMENT AND ORGANISATIONAL MATTERS

14.1 The focus of human resources development in the Reserve Bank has been changing in tune with the rapidly evolving external environment. A growing emphasis is being placed on facilitating performance improvement and personal growth within the overall institutional goals whereby personnel policies and practices are being increasingly integrated into the corporate strategy. A major challenge has been the building up of appropriate skills in an environment that fosters creativity, learning and efficiency. During 2003-04, the Reserve Bank continued with its efforts to upgrade its human resources to face the challenges arising out of globalisation and advances in technology. Concomitant measures were initiated to ensure transparency in operations and to improve customer service.

14.2 The goal of human resource (HR) initiatives in the Reserve Bank is to put in place robust human resource management systems that enhance efficiency and create an enabling work environment, which encourages individual responsibility. The endeavour is to foster an atmosphere of trust and integrity so as to keep the staff motivated and committed by adopting transparent personnel policies and keeping communication channels open by providing redressal windows.

14.3 These initiatives have assumed a new significance in the context of the Optional Early Retirement Scheme (OERS), whereby about 29 per cent of officers opted for voluntary retirement. In the post-OERS scenario, personnel policies are being reviewed and the existing initiatives are being reoriented, keeping in view the need for job realignment and consolidation. The new focus of HR policy in the Reserve Bank is essentially to create an environment which enhances efficiency and empowers the staff to draw out their latent potential. The emphasis of HR policies is on motivation, job involvement and commitment to the institution.

14.4 This Section reviews the efforts of the Reserve Bank directed towards upgrading human resources by imparting training within and outside India. It presents the employee profile within the ambit of overall industrial relations. The Section also reviews the various measures initiated to improve the quality of customer service and the interface with the general public, including information dissemination and data base management. The Section also presents an overview of the meetings of the Central Board and its Committee, appointment/retirement of executives and visits of important Committees and foreign dignitaries to the Reserve Bank.

TRAINING AND SKILLS ENHANCEMENT

14.5 Three training colleges of the Reserve Bank, *viz*., the Bankers' Training College (BTC), Mumbai, the Reserve Bank Staff College (RBSC), Chennai and the College of Agricultural Banking (CAB), Pune cater to the training needs of the officers of the Reserve Bank and the banking industry. The Bankers' Training College was established with a view to training the personnel of commercial banks and other financial institutions in India. The College caters mainly to the training requirements of middle and senior level officers. The RBSC was established to impart training to the Reserve Bank's own officers in junior and middle management cadre and occasionally to officers in the senior management cadre. The College of Agricultural Banking was originally set up with a focus on rural and co-operative credit. It provides training to senior and middle level officers from the financial sector as well as Government institutions. In recent years, the CAB has diversified into areas relating to non-banking financial companies, human resource management and information technology. Zonal Training Centres (ZTCs) focus exclusively on Class III and IV staff of the Reserve Bank (Table 14.1).

Bankers Training College, Mumbai

14.6 The BTC is a premier training institution in the field of banking. It has imparted high quality training to a large pool of professionals from the financial sector. The important programmes conducted by the College during the year included integrated risk management, money laundering, market risk, foreign exchange transactions for concurrent internal auditors and risk based internal audit. The endeavour of the BTC is to position itself as a training institute for senior bankers and to provide a forum for top executives of the financial sector to exchange views and ideas. The College extended faculty support to several other training institutions such as Syndicate Bank Training College, Manipal; Jawaharlal Nehru Institute of Development Banking (JNIDB), Hyderabad; Council of Scientific and

Table 14.1: Reserve Bank Training Establishments - Programmes Conducted

Establishment	2003-04		2002-03		2001-02		2000-01		1999-2000	
	No. of Programmes	No. of Participants	No. of Programmes	No. of Participants	No. of Programmes	No. of Participants	No. of Programmes	No. of Participants	No. of Programmes	No. of Participants
1	2	3	4	5	6	7	8	9	10	11
RBSC, Chennai	144	2,874	139	3,013	125	2,795	140	2,949	109	2,489
BTC, Mumbai	171	3,204	160	3,735	115	2,532	113	2,436	95	2,137
CAB, Pune	147 *	3,138 *	173	3,461	179	3,777	153	3,179	124	2,596
ZTCs (Class III)	187	3,652	153	2,991	131	2,576	100	2,013	86	1,660
ZTCs (Class IV)	56	958	31	535	26	470	17	313	16	312
Establishment	**1998-99**		**1997-98**		**1996-97**		**1995-96**		**1994-95**	
	No. of Programmes	No. of Participants	No. of Programmes	No. of Participants	No. of Programmes	No. of Participants	No. of Programmes	No. of Participants	No. of Programmes	No. of Participants
	12	13	14	15	16	17	18	19	20	21
RBSC, Chennai	131	3,055	132	3,030	119	2,542	108	2,061	111	2,207
BTC, Mumbai	77	1,818	91	2,102	91	1,957	101	1,987	118	2,429
CAB, Pune	126	2,940	109	1,982	124	2,231	97	2,013	113	2,429
ZTCs (Class III)	95	1,711	119	1,824	114	2,113	131	2,358	137	2,465
ZTCs (Class IV)	12	224	16	319	9	164	–	148	–	190

RBSC : Reserve Bank Staff College. BTC : Bankers Training College. CAB: College of Agricultural Banking. ZTCs: Zonal Training Centres.
* : Including 10 outstation programmes conducted at the initiative of Regional Offices involving 384 participants.

Industrial Research (CSIR), Hyderabad; NABARD Staff Training College, Lucknow; Punjab National Bank, Regional Staff College and the Stock Exchange, Mumbai. The College also conducted exclusive programmes for officers of the Indian Foreign Service, the National Institute for Finance Management, Foreign Exchange Dealers Association of India (FEDAI), Kotak Mahindra Bank and certain public sector banks. The BTC conducted eight programmes in collaboration with the Indian Institute of Bank Management, Guwahati at their campus. The College also brought out an interactive e-learning module on Internal Debt Management in the form of CD-Rom. Seventy-six foreign participants from Bhutan, Sri Lanka, Bangladesh, Nepal, Uganda and Tanzania attended 18 training programmes at the College. The College would be celebrating its Golden Jubilee in September 2004.

Reserve Bank Staff College, Chennai

14.7 The Reserve Bank Staff College (RBSC) caters primarily to the training and developmental needs of officers of the Reserve Bank. The College is expected to play a crucial role in upgrading the skills of officers to face the challenges of new tasks and introduction of new technologies. This has assumed an added significance in the context of the large retirements under the OERS. The thrust of the RBSC would continue to be on probationers and middle level management officers. Important activities of the RBSC during the year included introduction of specialised programme on derivatives, econometrics and programme on integrated treasury management. The college extended faculty support to the training establishments of the Indian Bank, the Union Bank of India, the Anna Institute of Management, Chennai, University of Madras, the Indian Institute of Technology (IIT), Chennai and the Bharat Overseas Bank.

College of Agricultural Banking, Pune

14.8 The College of Agricultural Banking (CAB) was originally set up to impart training in agriculture and rural banking. As alluded to earlier, the College has diversified into other areas such as the non-banking financial sector, human resource management and information technology. In the near future, the college proposes to consolidate these activities. The College conducted off-site programmes for State level financial institutions and extended faculty support to the workshops conducted by the Reserve Bank for Directors of urban co-operative banks. The College also extended faculty support to the National Institute of Bank Management (NIBM), Pune; Vaikunth Mehta National Institute of Co-operative Management (VAMNICOM), Pune; and Cosmos Co-operative Bank Ltd., Pune. Under the funded project of the Department for International Development (DFID), UK "Towards Ensuring Sustainable Financial Services for the Poor through Improved Capacity Building" taken up in collaboration with the University of Reading, UK, the College designed and conducted a training programme for impacting the attitudes of branch managers towards lending to the poor. The College organised five training programmes for participants from Bhutan, Nepal, Maldives and Sri Lanka.

Zonal Training Centres

14.9 The Zonal Training Centres (ZTCs) at the four metropolitan centres, (*i.e.,* Mumbai, New Delhi, Kolkata and Chennai) cater exclusively to the training needs of the Reserve Bank's employees covering Class III and Class IV cadres. The programmes conducted by the ZTCs covered the functions and working of the Reserve Bank, computer applications and behavioural aspects. The programmes for Class III related to functional areas such as issue, banking and other specialised departments, besides behavioural training. The Class IV staff were generally exposed to the behavioural programmes. The ZTCs also conducted new programmes such as foreign exchange reserve management and integrated development for redeployed Class III staff. Apart from conducting regular retirement programmes for the Class III and IV staff, the ZTCs also extended faculty support to the retirement programmes organised by Regional Offices for employees who had opted for the Optional Early Retirement Scheme (OERS).

Deputation of officers for training in India and abroad

14.10 During 2003-04, 433 officers were deputed by the Reserve Bank to participate in training programmes, seminars and conferences organised by external management/banking institutions in India. The areas of training included human resources management, risk management, international banking and foreign trade, labour laws and micro finance.

14.11 The Reserve Bank deputed 242 officers to attend training courses, seminars, conferences and workshops conducted by banking and financial institutions and multilateral institutions in 24 countries abroad (Table 14.2). The areas of training covered, *inter alia*, banking supervision, derivatives, risk management, financial programming and policies, central bank accounting, monetary policy and operations, finance for agriculture, rural development, and macroeconomic management.

14.12 Four officers were selected in 2003-04 under the Golden Jubilee Scholarship Scheme for higher studies abroad. Three of them are pursuing post-doctoral research work in areas such as option pricing from Carnegie Mellon University, US, modelling financial risks in India at the University of California, US and determination of interest and exchange rates at the Harvard University, US. One officer has enrolled at the University of Birmingham, UK for Master of Business Administration in banking and finance. Seventy-one officers have been deputed under the Scheme so far.

Table 14.2: Number of Officers Trained in External Training Institutes in India and Abroad

Year	No. of Officers trained in India	No. of Officers trained abroad
1	2	3
1999 - 2000	399	164
2000 - 01	444	122
2001 - 02	355	137
2002 - 03	452	208
2003 - 04	433	242

14.13 Seven officers availed of the Reserve Bank's higher studies scheme. One officer was deputed to the Bank for International Settlements (BIS), Basel under the Visiting Fellowship Scheme.

Training in Computer Technology

14.14 The Reserve Bank continued to provide incentives to staff members to acquire qualifications in the field of computers. The IT Training Plan implemented under the guidance of the Interactive Coordination Group (ICG) resulted in 98 per cent computer literacy in the Reserve Bank. In order to improve the skills of officers in the use of computers, 90 officers from Regional Offices and Central Office Departments were imparted training at institutions such as the National Institute of Bank Management (NIBM), Pune; the Management Development Institute (MDI), Gurgaon; the Xavier Labour Relations Institute (XLRI), Jamshedpur and the Institute for Development and Research in Banking Technology (IDRBT), Hyderabad.

Training Attachments and Interface Sessions

14.15 During 2003-04, 31 officials from four countries, *viz.*, Uganda, Indonesia, Tanzania and Bhutan were provided study attachments at the Reserve Bank's training establishments and Central Office Departments. The Training Division of the Reserve Bank arranged interface sessions with senior officers of the Central Office Departments for officers from the Naval Warfare College of Defence Management, MBA students from Mercer University, Georgia; students from McCombs School of Business, University of Texas, Afghan diplomats, officials from the Ministry of External Affairs, Government of India and participants from Iraq.

HUMAN RESOURCE INITIATIVES

14.16 The Reserve Bank has been nominating its officers on deputation/secondment/tour of duty to other organisations. The purpose of such deputations has been to widen the officers' perspective, provide them with alternative job experience and career opportunities and lend temporarily manpower support to other organisations. The Scheme was streamlined and widened in scope in March 2000 and certain amendments were made with regard to recognition of service on deputation towards superannuation benefits.

Summer Placement

14.17 A total of 44 students were selected for summer placements in the Reserve Bank during the year. These summer interns were drawn from diverse disciplines such as commerce, management, science, engineering and IT. The interns were placed predominantly in the Reserve Bank's Central Office at Mumbai, while some were assigned to select Regional Offices, *viz*., Ahmedabad, Bangalore, Chennai, Kolkata and New Delhi. A number of students in specialised areas were also accommodated in different Departments of the Reserve Bank outside the Scheme.

Organisational Climate Survey

14.18 The Reserve Bank conducted an organisational climate survey in mid-2003 amongst the staff in Classes I and III to gauge the impact of the policy initiatives and welfare measures undertaken in the last few years on the satisfaction level of the employees. The Bank had conducted similar satisfaction surveys in 1996 and 1998. The survey received a response level of approximately 40 per cent which was more than twice the response level in the previous surveys. The analysis of the responses showed a general improvement in the satisfaction levels, especially in areas such as job satisfaction, infrastructure support and personnel welfare. As compared with previous surveys, there was an improvement in the overall satisfaction levels as measured in terms of Net Satisfaction Factor (NSF which represents the overall difference between those replying to the questions as satisfied and dissatisfied) which went up from (-) 0.63 per cent in 1996 to 3.93 per cent in 1998 and further to 16.36 per cent in 2003. It implied that approximately 58 per cent of the respondents were generally satisfied (Table 14.3). Certain areas of concern were also brought out by the survey such as performance appraisal and recognition of merit, organisational culture and internal communication.

Table 14.3: Results of Organisational Climate Survey (NSF in per cent)

Section	2003	1998	1996
1	2	3	4
I. Job Satisfaction	38.02	20.95	17.54
II. Organisation Culture	7.82	14.67	11.71
III. Infrastructure Support	49.30	6.70	2.61
IV. Training	18.31	-0.30	-5.90
V. PAS and Merit	-10.60	-26.13	-31.76
VI. Personnel Welfare	18.49	-11.38	-19.17

PAS : Performance Appraisal System.
NSF : Net Satisfaction Factor

Optional Early Retirement Scheme

14.19 The Reserve Bank introduced an Optional Early Retirement Scheme (OERS) on August 16, 2003 (Box XIV.1). The OERS was closed on December 31, 2003 and the last group of employees who opted for the scheme was relieved on March 31, 2004. A total

Box XIV.1

Optional Early Retirement Scheme

The Optional Early Retirement Scheme (OERS) was introduced in the Reserve Bank for a brief period, broadly on the framework of the voluntary retirement scheme (VRS) implemented by public sector undertakings. There were, however, some marked differences. VRS is typically an offer to a section of employees of an organisation to retire voluntarily from service by accepting monetary benefits before their normal date of superannuation. The compensation, in addition to the normal superannuation benefits, would depend on the years of service put in by the employee or the remaining period of service. In commercial organisations, voluntary retirement schemes were implemented for maintaining the cost effectiveness in a competitive environment. In India, VRS was introduced as a strategy to reduce the surplus/ redundant workforce in some of the central public sector undertakings in the early 1980s. The banking industry introduced VRS for its employees in 2000.

Technological upgradation undertaken by the Reserve Bank towards streamlining the work in general and its core function, *i.e.*, currency management led to re-engineering of processes in some areas. Therefore, a scheme analogous to-but not exactly identical to-a VRS model was deemed necessary. Accordingly, an Optional Early Retirement Scheme (OERS) was introduced on August 16, 2003 which closed on December 31, 2003.The scheme was opened to all full-time regular employees who had completed 25 years of service and attained 50 years of age as on August 1, 2003. Though the scheme was purely voluntary, the Reserve Bank reserved the right to accept or reject any application in keeping with administrative exigencies. The outgo of employees was also staggered in order to keep the flow of work smooth. Employees opting for the scheme were granted *ex gratia* amount equal to pay *plus* dearness allowance of two months for each year of service rendered or pay *plus* dearness allowance for the remaining months of service, whichever was less. In addition, they were entitled to all other normal retirement benefits. The scheme evoked a good response from the employees and 4,468 applications were accepted under the scheme. All of them were relieved from service.

Table 14.4: Employees who Opted for OERS

Centre	Class I		Class III		Class IV		Total	
	OERS	AS	OERS	AS	OERS	AS	OERS	AS
1	2	3	4	5	6	7	8	9
Ahmedabad	124	292	63	566	43	376	230	1,234
Bangalore	137	340	84	671	40	376	261	1,387
Bhopal	26	142	5	107	3	113	34	362
Bhubaneswar	18	142	14	238	12	238	44	618
Chandigarh	30	171	4	115	1	122	35	408
Chennai	230	559	180	937	64	698	474	2,194
Guwahati	25	169	17	343	22	262	64	774
Hyderabad	135	317	61	461	32	355	228	1,133
Jaipur	44	195	41	413	23	316	108	924
Jammu	9	62	0	35	3	51	12	148
Kanpur	73	239	49	618	64	523	186	1,380
Kolkata	105	511	218	1,602	144	1,030	467	3,143
Lucknow	32	146	20	245	6	139	58	530
Mumbai (including Central Office)	685	2,611	457	3,323	255	2,585	1,397	8,519
Nagpur	105	228	87	622	20	375	212	1,225
New Delhi	155	476	112	1,038	51	598	318	2,112
Pune	7	43	18	53	6	91	31	187
Patna	54	220	86	526	75	389	215	1,135
Thiruvananthapuram	64	225	23	357	7	259	94	841
Total	**2,058**	**7,088**	**1,539**	**12,270**	**871**	**8,896**	**4,468**	**28,254**
Memo Item:								
Percentage of Employees who opted for OERS	29.0		12.5		9.8		15.8	

AS : Actual Staff strength as on June 30, 2003.
OERS : Optional Early Retirement Scheme.

of 4,468 employees representing 15.8 per cent of the workforce as on June 30, 2003 availed of the Scheme (Table 14.4). The age profile of officers who opted for OERS indicates a concentration in the age group of 54 to 57 (Chart XIV.1).

14.20 An exit survey conducted among the officers who opted for OERS indicated that the predominant reasons for opting for OERS by officers were personal reasons and poor health conditions (Chart XIV.2).

Chart XIV.1 : Age Profile of Officers Opting for OERS

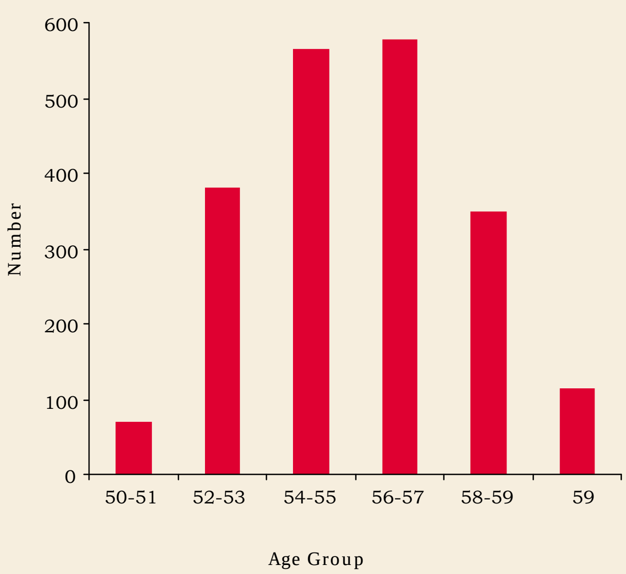
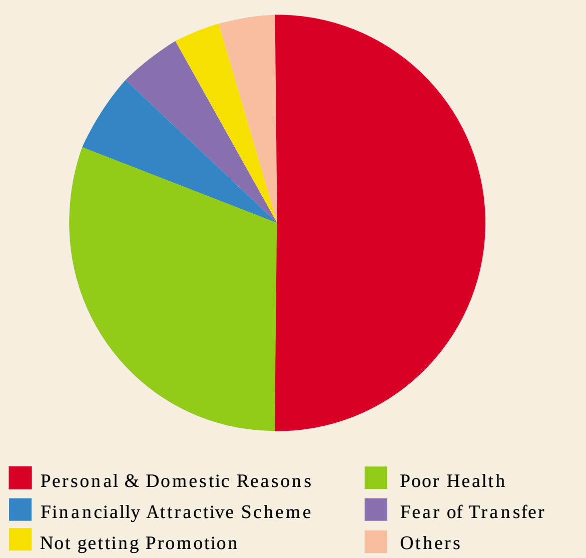


Chart XIV.2 : Reasons for Opting OERS by Officers



14.21 In order to overcome the challenges posed by the OERS in managing the work of the Reserve Bank, a Committee on Job Realignment/Job Consolidation was constituted under the Chairmanship of Shri A. V. Sardesai, Executive Director to conduct a quick study of the systems and procedures in various Departments. The recommendations of the Committee mainly related to simplification of existing work procedures in the Reserve Bank such as rationalisation of returns/statements, level jumping for quicker decision making. Other recommendations dealt with reorganisation/consolidation between departments. The Committee has submitted its report and its recommendations are under implementation.

Promotion of Hindi

14.22 The Reserve Bank continued to create awareness of Hindi among employees by way of intensifying training programmes in various fields under the Official Language Policy. Annual Programme on use of Hindi formulated by the Government of India was implemented successfully. The Committee of Parliament on Official Languages visited the Reserve Bank's Panaji office. Their observations were forwarded to all offices of the Reserve Bank for implementation. The recommendations of Hindi *Salahkar Samiti* of the Ministry of Finance, Government of India were implemented. Workshops were organised for senior officers in various Regional Offices. The Reserve Bank organised an all-India seminar for reorientation of Rajbhasha officers of the banks. The use of Hindi on computers has increased in the Reserve Bank and public sector banks.

14.23 The Reserve Bank continued to publish its major publications bilingually. The Bankers' Training College improved the quality of its quarterly magazine called *"Banking Chintan Anuchintan".* With a view to increasing the correspondence in Hindi, a collection of specimens, *i.e.*, 'Bank Patrachar ke Namoone' was published during the year. The fifth edition of '*Banking Glossary (English-Hindi)'*, published by the Reserve Bank was widely welcomed by the banking sector. The Hindi version of the publication entitled 'Functions and Working of Reserve Bank of India' was prepared and published by the Reserve Bank Staff Training College.

14.24 The Reserve Bank continued with its efforts for increasing the use of Hindi in public sector banks and all-India financial institutions. Their progress was reviewed in the quarterly meetings of the Official Language Implementation Committee. The Reserve Bank organised Bilingual and Hindi Griha Patrika Competitions for public sector banks and financial institutions during the year. The Reserve Bank provided secretarial assistance to the Government of India, Ministry of Home Affairs in preparing results for the Indira Gandhi Official Language Award Scheme for the public sector banks and financial institutions.

Industrial Relations

14.25 Industrial relations in the Reserve Bank remained, by and large, peaceful during 2003-04. Meetings were held with the recognised Associations/ Federation of employees and officers on wage revision and on various other matters.

Recruitment

14.26 During the year 2003, the Reserve Bank recruited 127 employees, of which 19 were from Scheduled Castes (SCs) and Scheduled Tribes (STs) categories, constituting 15.0 per cent of total recruitment (Table 14.5).

14.27 The total staff strength as on December 31, 2003 was 24,994 as compared with 28,884 a year ago. Of the total staff, 20.1 per cent belonged to Scheduled Castes and 8.1 belonged to Scheduled Tribes (Table 14.6).

14.28 During the calendar year 2003, the Reserve Bank's Liaison Officer for Scheduled Caste/Scheduled Tribe employees conducted inspection of reservation rosters maintained at three offices, *viz*., Patna, Guwahati and Central Office. Meetings between the Management and the representatives of the All India Reserve Bank Scheduled Castes/Scheduled Tribes and the Buddhist Federation were held on four occasions during the year to discuss issues relating to the implementation of reservation policy in the Reserve Bank. In accordance with the Central Government's policy, effective September 8, 1993 the Reserve Bank provided reservation to Other

Table 14.5: Recruitment – 2003 (January to December)

Category	Total Recruited	*Of which*		Percentage	
		SC	ST	SC	ST
1	2	3	4	5	6
Class I	68	5	2	7.35	2.94
Class III	22	3	2	13.63	9.09
Class IV					
(a) Sweepers	9	2	–	22.22	–
(b) Others	28	4	1	14.28	3.57
Total	**127**	**14**	**5**	**11.02**	**3.93**

Table 14.6: Total Staff Strength

Category	Category- wise Strength						Per cent to Total Strength	
	Total Strength		SC		ST		SC	ST
	December 31, 2003	December 31, 2002	December 31, 2003	December 31, 2002	December 31, 2003	December 31, 2002	December 31, 2003	
1	2	3	4	5	6	7	8	9
Class I	6,128	7,261	862	835	305	249	14.07	4.98
Class III	10,644	12,570	1,572	1,894	960	1,058	14.77	9.02
Class IV	8,222	9,053	2,594	2,618	761	778	31.55	9.26
Total	**24,994**	**28,884**	**5,028**	**5,347**	**2,026**	**2,085**	**20.12**	**8.11**

Backward Classes (OBCs). The representation of OBCs in the Reserve Bank as on December 31, 2003 stood at 660, constituting 2.6 per cent of total staff strength. Of these, 133 (2.2 per cent) were in Class I, 107(1.0 per cent) in Class III and 420(5.2 per cent) in Class IV.

14.29 The total strength of ex-servicemen in the Reserve Bank as at the end of December 2003 stood at 137 in Class I, 485 in Class III and 1,023 in Class IV. The total number of physically handicapped employees in Class I, Class III and IV cadres in the Reserve Bank stood at 60,273 and 151, respectively, as at the end of 2003.

14.30 Of the total staff strength of the Reserve Bank 24.5 per cent of the staff were in Class I, 42.6 per cent in Class III and the remaining 32.9 per cent in Class IV (Table 14.7).

14.31 The department-wise deployment of the staff in the Reserve Bank has remained broadly stable (Table 14.8) with adequate staff strength at various centres (Table 14.9).

Table 14.7: Category-wise Staff Strength - Actual (As on December 31, 2003)

	Class	Actual Strength
	1	2
	Class I	
1.	Senior Officers in Grade F	80
2.	Senior Officers in Grade E	209
3.	Senior Officers in Grade D	366
4.	Officers in Grade C	850
5.	Officers in Grade B	1,354
6.	Officers in Grade A	2,684
7.	Treasurer	17
8.	Deputy Treasurer	75
9.	Assistant Treasurer	493
	Total Strength - Class I	**6,128**
	Class III	
1.	Clerk Gr. I	2, 905
2.	Clerk Gr.II	5, 803
3.	Stenographer	302
4.	Typist	618
5.	Teller	343
6.	Class III (Others)	673
	Total Strength - Class III	**10, 644**
	Class IV	
1.	Peon	1, 705
2.	Mazdoor	2, 172
3.	Class IV (Others)	4, 345
	Total Strength - Class IV	**8, 222**
	Total Strength in the Reserve Bank	**24, 994**

Premises Department

14.32 The Premises Department has taken up the task of improving the ambience in work places and residential colonies, mechanisation and computerisation as well as upgradation and modernisation of the existing infrastructural facilities. The state-of-the-art systems, *viz.*, modern communication systems (EPABXs) and backbone/structured cabling systems for Local Area Networks (LANs) have been provided as standard building service systems at all offices of the Reserve Bank. Closed Circuit TV (CCTV) systems have also been provided in all the offices of the Reserve Bank as a part of the security system. In addition, access control systems comprising proximity/biometric readers, smart cards, walkthroughs, turnstiles and X-Ray Baggage scanner at entry points to office buildings are being provided at all the offices. Micro processor based addressable fire/smoke alarm systems to act as an early warning system in case of fire/emergencies have been provided in the Bhopal, Chandigarh, Kolkata, two office buildings in Mumbai, Main Office Building, Nagpur and New Delhi. It would be extended to remaining offices shortly. Construction of officers' flats at Dadar/Parel, Mumbai has been completed. The office building at Lucknow and staff quarters for Class IV staff at Patna are under advanced stages of construction.

Table 14.8: Department-Wise Staff Strength (As on December 31, 2003)

Sr. No.	Department	Class I			Class III			Class IV			Grand Total (5+8+11)
		CO	RO	Total	CO	RO	Total	CO	RO	Total	
1	2	3	4	5	6	7	8	9	10	11	12
1.	Department of Administration and Personnel Management (DAPM)	116	301	417	136	614	750	70	1,051	1,121	2,288
2.	Department of Banking Operations and Development (DBOD)	108	70	178	109	164	273	78	128	206	657
3.	Department of Banking Supervision (DBS)	122	527	649	36	186	222	21	83	104	975
4.	Department of Currency Management (DCM)	42	1,073	1,115	35	3,305	3,340	19	2,812	2,831	7,286
5.	Department of Economic Analysis and Policy (DEAP)	192	31	223	218	37	255	89	19	108	586
6.	Department of Expenditure and Budgetary Control (DEBC)	49	167	216	105	582	687	38	89	127	1,030
7.	Department of External Investment and Operations (DEIO)	53	–	53	35	–	35	15	–	15	103
8.	Department of Statistical Analysis and Computer Services (DESACS)	136	15	151	167	58	225	86	12	98	474
9.	Department of Government and Bank Accounts (DGBA)	51	1,042	1,093	69	2,693	2,762	25	1,974	1,999	5,854
10.	Department of Information Technology (DIT)	61	12	73	21	3	24	16	1	17	114
11.	Department of Non-Banking Supervision (DNBS)	47	242	289	12	132	144	9	64	73	506
12.	Foreign Exchange Department (FED)	80	208	288	149	587	736	63	172	235	1,259
13.	Human Resources Development Department (HRDD)	21	7	28	24	8	32	9	3	12	72
	A. Bankers Training College, Mumbai	–	32	32	–	38	38	–	92	92	162
	B. Reserve Bank Staff College, Chennai	–	32	32	–	31	31	–	33	33	96
	C. Zonal Training Centers.	–	17	17	–	9	9	–	5	5	31
	D. College of Agricultural Banking, Pune	–	45	45	–	35	35	–	85	85	165
14.	Internal Debt Management Department (IDMD)	20	–	20	11	–	11	7	–	7	38
15.	Industrial and Export Credit Department (IECD)	32	–	32	26	–	26	11	–	11	69
16.	Inspection Department (ID)	45	66	111	20	21	41	8	5	13	165
17.	Legal Department (LD)	30	5	35	24	6	30	11	2	13	78
18.	Press Relations Division (PRD)	5	–	5	5	–	5	3	–	3	13
19	Premises Department (PD)	49	179	228	53	358	411	50	704	754	1,393
20.	Rural Planning and Credit Department (RPCD)	68	234	302	44	150	194	40	56	96	592
21.	Secretary's Department	32	–	32	20	–	20	35	–	35	87
22.	Urban Banks Department (UBD)	50	343	393	25	158	183	40	47	87	663
23.	Rajbhasha Cells	–	26	26	–	48	48	–	7	7	81
24.	Deposit Insurance and Credit Guarantee Corporation	–	31	31	–	62	62	–	28	28	121
25.	Reserve Bank Services Board	14	–	14	15	–	15	7	–	7	36
	Total	**1,423**	**4,705**	**6,128**	**1,359**	**9,285**	**10,644**	**750**	**7,472**	**8,222**	**24,994**

Note:
1. The staff in the Monetary Policy Department (MPD) are not shown separately since they are drawn from five Departments, *viz.*, DEAP, DESACS, DBOD, RPCD and DAPM. The staff strengths of MPD in different categories as on December 31, 2003 was 42 in Class I, 35 in Class III and 21 in Class IV.
2. CO - Central Office. RO - Regional Office.
3. The staff shown against DCM is inclusive of staff employed in Issue Departments. The staff shown against DGBA is inclusive of staff employed in Banking Departments.
4. The staff strength of Rajbhasha Department, Central Office is included in DAPM-Central Office.

Table 14.9: Regional Office-wise Staff Strength (As on December 31, 2003)

	Department/Office	Class I	Class III	Class IV
	1	2	3	4
1.	Ahmedabad	284	484	347
2.	Bangalore	315	536	349
3.	Belapur	94	234	280
4.	Bhopal	130	94	110
5.	Bhubaneswar	136	211	227
6.	Chandigarh	168	99	122
7.	Chennai	383	765	633
8.	Guwahati	163	320	243
9.	Hyderabad	220	383	350
10.	Jaipur	192	361	293
11.	Jammu	67	32	47
12.	Kanpur	193	564	484
13.	Kochi	25	85	49
14.	Kolkata	508	1,376	957
15.	Lucknow	134	232	133
16.	Mumbai	686	1,296	1,340
17.	Nagpur	185	566	348
18.	New Delhi	386	897	542
19.	Panaji, Goa	06	08	02
20.	Patna	224	465	331
21.	Pune(CAB and CRDC)	45	35	85
22.	Thiruvananthapuram	161	242	200
	Total	**4,705**	**9,285**	**7,472**

CAB : College of Agricultural Banking
CRDC : Central Records and Documentation Centre.

Inspection of Offices/Departments in the Reserve Bank

14.33 The Management Audit and Systems Inspection (MA&SI) within the Reserve Bank focuses on compliance with the prescribed systems and procedures and evaluates efficiency and economy in operations. Within this process, a risk-based strategy was evolved whereby high risk-prone areas in the functioning of offices were identified for intensive deployment of inspection resources. The performance of internal inspections and compliance is monitored by a Committee of Executive Directors under the overall supervision and guidance of the Inspection and Audit Sub-Committee (IASC) of the Central Board of the Reserve Bank. Information Systems Audits (IS Audits) have been conducted on a regular basis. During the period July 2003-June 2004, the Management Audit and Systems Inspection of 14 Regional Offices (ROs), 9 Central Office Departments (CODs), 3 Training Colleges and the Bharatiya Reserve Bank Note Mudran (Pvt.) Ltd. was conducted. The Information Systems Audit of 5 CODs and 6 ROs was conducted during the period from July 2003 to December 2003. In January 2004, the Information Systems Audit was integrated with the Management Audit and Systems Inspection. Rating of Regional Offices/Regional Directors (RDs), which was introduced with effect from January 1, 2003 stabilised during the year. Accordingly, ratings of 16 ROs/RDs were finalised. The Inspection Guidelines (for inspecting officers), framed originally in 1992, were revised and put into effect in February 2004.

Library

14.34 The Central Library of the Reserve Bank, attached to the Department of Economic Analysis and Policy (DEAP), plays an important role in the storage, retrieval and dissemination of information. The Library has a comprehensive collection of books, journals, working papers, reports, CD-ROMs and other documents. The Library maintains electronic databases of all these documents (OPAC – Online Public Access Catalogue), which can be accessed through Intranet from the Central Office building and from all other offices of the Reserve Bank. Through its home page, the Library offers access to various online databases such as ECONLIT Online, Proquest Business Periodicals Database (covering 2,359 journals), India Business Insight Database and Elsevier Science Direct.

14.35 The Library database has 98,009 records which covers books and other documents. The Library receives 534 technical journals. The Library provides Current Awareness Services for all new documents including books as well as select articles from professional journals through Intranet on a regular basis. In addition, the Library also provides information services and support to training colleges and libraries in other offices of the Reserve Bank.

Dissemination Policy

14.36 During the year under review, the Reserve Bank continued to disseminate information through media, press releases, publications, notifications, frequently asked questions (FAQs) and advertisements. It organised meetings, workshops and seminars for interacting with special audiences. Information kiosks and intranet sites were also used for communicating with the general public visiting the Reserve Bank's premises.

14.37 The Reserve Bank's website continued to remain a major source of information. Over 7,963 users registered themselves for receiving information through e-mail. As many as 19,954 visitors used the personalised service to access information available on the Reserve Bank's website in the form they want.

During the year under review, the Reserve Bank issued 1,522 press releases and added 7.5 giga-bytes (GBs) of material to its website, taking the volume of information available on the website to 13 GBs. The e-mail helpdesks continued to furnish replies to the queries raised by the general public. For seeking clarifications relating to the policies of the Reserve Bank, members of the public also send their queries through e-mail/telephone/fax to the helpdesks set up in various operational departments/Regional Offices. The queries primarily relate to foreign exchange, banking, complaints against banks and Government securities.

14.38 The Reserve Bank introduced running serial numbering of the circulars issued by all its operational departments from January 2004 based on the recommendation of the Advisory Group on Financial Regulations (Chairperson: Smt. K.J. Udeshi). The continuous serial number was introduced in addition to the number given by the respective departments. It is expected to help recipients of the Reserve Bank circulars to track the circulars and approach one single point for replacement of the missing ones. In order to facilitate the tracking of the circulars, the Reserve Bank website (www.rbi.org.in) publishes an index of all the circulars issued during the year. The index is maintained serial number-wise and is regularly updated.

Customer Service Measures

14.39 Efforts were made to further improving customer service, especially in the areas of currency management, foreign exchange and banking matters. Publicity was given to the Customer Redressal Mechanism, which provides a forum to the public to seek redressal of their complaints against any department of the Reserve Bank. Advertisements were issued in newspapers informing members of the public that they could seek redressal of their grievances by contacting a designated officer in each regional office. Tele-banking was introduced with a view to providing better customer service to the Government departments. In addition, a new facility called the Easy Term Remote Terminal Facility was also introduced in most offices.

14.40 Coin dispenser and note counting machines were installed in Banking Halls in most offices for the benefit of customers. Various initiatives undertaken by the Reserve Bank based on the recommendations of the Committee on Procedures and Performance Audit on Public Services (Chairman: Shri S.S. Tarapore) to improve the customer service in currency distribution have been detailed in Chapter XII. Some offices set up ATMs in collaboration with commercial banks within the Reserve Bank premises. Other customer-friendly measures introduced included installation of electronic moving display boards and notice boards at strategic points to display information of interest/ relevance to customers. Complaint boxes were also placed in various premises of the Reserve Bank to receive customer complaints. The Citizens' Charters were displayed in front of the operational departments for information of the public.

14.41 The Kolkata office of the Reserve Bank conducted an on-the-spot customer survey to gauge the quality of service being rendered by its cash counter staff. The survey revealed a marked improvement in the quality of service. The Bhubaneswar office of the Reserve Bank declared 'customer delight' as its mission. To achieve this, the office established performance benchmarks for each department with a focus on reducing the response time and increasing the quality of service rendered to customers. It also arranged a two-day workshop on 'Communication and Creativity to Improve Productivity and Customer Service' for a batch of 20 officers. The regional office at Hyderabad provided a computer in the Banking Hall to enable members of the public to offer suggestions on improving customer service and for ensuring quick redressal of their grievances.

14.42 The Reserve Bank prepared two pamphlets containing information about foreign exchange facilities available to residents and non-residents for the benefit of the general public. Pamphlets were distributed to all authorised distributors for display at their branches. The copies of the pamphlets were also sent to institutions like Airport Authority of India, Indian Railways, Department of Tourism and several five star hotels. These were updated from time to time to incorporate the latest policy announcements affecting resident and non-resident Indians. Similar pamphlets were also prepared for 8 per cent Savings Bonds for distribution through regional offices.

Department of Economic Analysis and Policy

14.43 The Reserve Bank continued with its efforts of providing analytical inputs on various facets of the Indian economy for the purpose of policy formulation. In order to accomplish this objective, the Department of Economic Analysis and Policy (DEAP) plays a major role in providing inputs to the policy formulation as well as in bringing out various analytical and research publications of the Reserve Bank for the public. Some of the important publications prepared in the Department and released during the year included the *Reserve Bank's Annual Report*, 2002-03, the *Report on Trend and Progress of Banking in India*, 2002-03 and a *Study on Finances of State Governments*. *The Report on Currency and Finance*, 2002-03 chose "*Management of India's External Sector in an Open Economy*" as its theme. A document entitled '*Macroeconomic and Monetary Developments in 2003-04*' was released along with the Governor's Annual Policy Statement issued on May 18, 2004. The Department also disseminated information on key parameters of the Indian economy in the Reserve Bank's *Monthly Bulletin* and its Weekly Statistical Supplement. The *Reserve Bank of India Occasional Papers* continued to publish analytical studies in the areas concerning the Indian economy. The *Reserve Bank Staff Studies*, an in-house journal intended to provide an important outlet for the research efforts made by officers of the Reserve Bank, carried six studies during 2003-04. The Department also provided technical inputs to other Departments and participated in several Inter-Departmental Groups. The Department coordinated the work relating to Article IV consultations with the staff of the IMF. The Department also conducted the 8th L.K. Jha Memorial Lecture which was delivered by Prof. Martin Feldstein on January 12, 2004. The Department organised a series of seminars/lectures by foreign dignitaries and experts from India.

14.44 The Development Research Group (DRG), which was constituted in the Reserve Bank in November 1991, continued to serve as a forum for collaborative research between professional economists and officers of the Bank. The DRG has published 24 studies since its inception. The studies cover a wide range of subjects relating to monetary, fiscal, banking and external areas, besides real and social sector. During the year, a study on 'Interest Rate Modelling and Forecasting in India' was completed. The studies initiated during the year under the DRG included i) Bank Soundness and Macroeconomic Policy, ii) Supply Response in Indian Agriculture, iii) Targeting Efficiency in PDS: A Comparison of the Revamped and Targeted PDS, iv) Effect of Private Remittances on the Indian Economy and v) Regional Inequality in India: A Fresh Look. Constant efforts are being made to make the DRG mechanism more transparent and broad-based.

Department of Statistical Analysis and Computer Services

14.45 The Department of Statistical Analysis and Computer Services (DESACS) completed the 'Survey of Small Borrowal Accounts, March 2001', covering small borrowal accounts with a credit limit of Rs.2,00,000 or less. The salient features of the survey results were published in the May 2004 issue of the Reserve Bank's Bulletin. The Reserve Bank has been collecting detailed information on deposits and credit of scheduled commercial banks through Basic Statistical Returns 1 and 2 and publishing them in the form of BSR Volumes since 1972. These data were brought out in a CD-ROM entitled 'Banking Statistics: Basic Statistical Returns, 1 and 2, Volume 1 to 31', covering the period from 1972 to 2002. A publication entitled "*Basic Statistical Returns of Scheduled Commercial Banks in India*" Volume 32, March 2003, relating to the distributional aspects of deposits and gross bank credit of scheduled commercial banks was brought out during the year.

14.46 As a part of the implementation of the Bank for International Settlements (BIS) methodology of International Banking Statistics (IBS) in India, the quarterly data on international assets/liabilities of banks were compiled in the form of locational banking statistics (LBS) and consolidated banking statistics (CBS). The BIS incorporated CBS and LBS data of India for the first time in its publications for the quarter ended December 31, 2001. Data for subsequent quarters were also released by them. Accordingly, the Reserve Bank became the third central bank among developing countries to comply with the BIS requirement. Besides, the articles presenting the summary results of IBS of India for each of the quarters were published in the Reesrve Bank Bulletin.

14.47 The "Directory of Commercial Bank Offices in India-Vol.2- September 2003" was brought out in December 2003 in CD-ROM and was posted on the Reserve Bank's website. The Directory contains information on various functional and locational details of 68,723 branches/offices of 295 commercial banks as on September 30, 2003.

14.48 Software for the timely compilation of balance of payments and international trade in services, was revised and implemented with effect from April 1, 2004. A comprehensive survey on software and IT exporting companies was taken up covering the period April 2002 to March 2003, based on the recommendations of the 'Technical Group on Re-examination of Data Reporting System on Software

Exports' set up in pursuance of the recommendations of the National Statistical Commission.

Banking Ombudsman Scheme

14.49 Fifteen offices of the Banking Ombudsmen administer the Banking Ombudsman Scheme, 2002. During the year 2003-04 8,246 complaints were received. The number of complaints dealt with pertained, *inter alia*, to deficiency in servicing of loans and advances, deposit accounts and delay in collection of cheques/bills. During the period 1999-2000 to 2003-04, 98 per cent of the complaints disposed off were by mutual settlement and awards were passed in respect of the remaining two per cent. As provided in the Scheme, the amount spent by the Ombudsmen is being recovered from the participating banks in proportion to the working funds of these banks as at the end of the preceding financial year.

CENTRAL BOARD AND ITS COMMITTEES

14.50 Six meetings of the Central Board were held during the year ended June 30, 2004 of which two meetings were held at traditional centres, *viz*., Chennai and Mumbai and four were held at non-traditional centres, *viz*., Chandigarh, Bangalore, Patna and Thiruvananthapuram. Forty-seven weekly meetings of the Committee of the Central Board were held during the year at Mumbai. During the year, the Committee of the Central Board attended to the current business of the Reserve Bank, including approval of its weekly accounts pertaining to the Issue and the Banking Departments. Discussions at the meetings of the Central Board broadly covered matters pertaining to general superintendence and direction of the Reserve Bank's affairs in which Directors, with their vast experience in diverse fields, actively contributed to important decisions. Some important policy matters discussed at these meetings related to currency management, information technology, human resource development, banking supervision, monetary and credit policy, accounting policy and internal debt management policy. The Central Board and its Committee also reviewed the functioning of Local Boards with a view to enabling them to perform their advisory role better.

14.51 One meeting of the Staff Sub-Committee, six meetings of the Inspection and Audit Sub-Committee (IASC) and three meetings of the Building Sub-Committee were held during the year. These Sub-Committees of the Central Board have been constituted to assist the Central Board in direction of the affairs of the Reserve Bank. During the year, the Building Sub-Committee advised the Reserve Bank on various matters including construction of staff quarters, renovation of office space, rehabilitation of officers quarters, replacement of air conditioning plants and lifts in office buildings. It also reviewed the utilisation of the capital budget for the year 2003-04. The Staff Sub-Committee addressed proposals for sanction of additional posts in all categories of staff in various Departments and Regional Offices of the Reserve Bank during the year. It also considered matters concerning manpower planning in the Reserve Bank. The Inspection and Audit Sub-Committee examined 'Critical Areas' emanating from Management Audit and Systems Inspection of Central Office Departments/Regional Offices of the Reserve Bank. Besides, it went into various accounting issues like outstanding entries in sundry/suspense account, reconciliation of internal accounts, outstanding entries in transit accounts and advised the course of action to be adopted to cleanse the accounts before migration to new technologies.

Directors/Members of the Central Board/Local Boards

14.52 Dr. Bimal Jalan, Governor demitted office on September 6, 2003 consequent upon his nomination as a member of the Rajya Sabha.

14.53 Dr. Y. V. Reddy took over as Governor of the Reserve Bank on September 6, 2003 for a period of five years.

14.54 Shri Vepa Kamesam, Deputy Governor retired from the Reserve Bank's service from the close of business on December 23, 2003.

14.55 Smt. Devaki Jain was nominated as a member of the Local Board (Southern Area) with effect from February 12, 2004.

14.56 Prof. A. M. Khusro, former Director on the Central Board of the Bank (from February 28, 1970 to April 1, 1979) passed away on August 24, 2003.

14.57 Smt. Kiran Ghai ceased to be a Member of the Local Board (Eastern Area) consequent upon her election as Member of the State Legislative Council of Bihar on June 14, 2004.

Appointment/Retirement of Executives

14.58 Shri Y. S. P. Thorat, Executive Director retired from the Reserve Bank's service on March 17, 2004 consequent upon his appointment as the Managing Director of the National Bank for Agriculture and Rural Development.

14.59 Shri P.V. Subba Rao was appointed as Executive Director with effect from March 19, 2004.

Parliamentary Committees

14.60 Shri Arjun Singh, Chairman, Parliamentary Committee on Empowerment of Women visited the Reserve Bank on September 28, 2003 and had discussions with Shri A.V. Sardesai, Executive Director and other senior officials of the Rural Planning and Credit Department (RPCD). Senior officials of the RPCD from the Central Office and the Regional Offices at Bhubaneswar, Bangalore, Ahmedabad, Bhopal, Lucknow, and Patna appeared before the Standing Committee of Parliament on Finance, the Standing Committee of Parliament on Industry and the Estimate Committee of Parliament during the year on several occasions.

Foreign Dignitaries

14.61 Mr. Kenneth S. Rogoff, Director (Research) IMF, visited the Reserve Bank on July 18, 2003 and met Governor and Deputy Governors. He also addressed senior officials of the Reserve Bank and later held a press conference.

14.63 Mr. Malcolm Knight, General Manager, Bank for International Settlements, Basel visited the Reserve Bank on September 24, 2003 and met Governor and Deputy Governors.

14.63 Prof. Richard Portes of the London Business School and President of the Centre for Economic Policy Research (CEPR) visited the Reserve Bank on January 5, 2004. He also delivered a lecture on ‘Monetary Policy of the European Central Bank’.

14.64 Prof. Ricardo Hausmann of Harvard University visited the Reserve Bank on January 7, 2004 and delivered a lecture on ‘Good Credit Ratios but Bad Credit Ratings: The Role of Debt Denomination’.

14.65 Prof. Martin Feldstein, Professor of Economics, Harvard University and President, National Bureau of Economic Research, Cambridge, US visited the Reserve Bank from January 11 to 13, 2004. He delivered the 8th L.K. Jha Memorial Lecture on January 12, 2004.

14.66 Dr. (Ms.) Anne Krueger, First Deputy Managing Director, IMF visited the Reserve Bank on January 22, 2004. She had a meeting with Governor and Deputy Governors. She also held discussions with Executive Directors.

14.67 Mr. Vittorio Corbo, President of the Central Bank of Chile visited the Reserve Bank on January 27, 2004 and held a seminar.

14.68 Ms. Sheryl Kennedy, Deputy Governor for Financial Markets, Bank of Canada, visited the Reserve Bank on June 18, 2004 and met Deputy Governor and Executive Director.

Auditors

14.69 The accounts of the Reserve Bank were audited by M/s. J. L. Sengupta & Co., Kolkata; M/s. S. N. Nanda & Co., New Delhi; M/s. Khimji Kunverji & Co., Mumbai; M/s. P. B. Vijayaraghavan & Co., Chennai; M/s. Ford Rhodes Parks & Co, Mumbai; and M/s. Rajendra K. Goel & Co., New Delhi. While the first four audit firms were reappointed, the latter two were appointed for the first time by the Central Government.

XV THE RESERVE BANK'S ACCOUNTS FOR 2003-04

15.1 The key financial results of the Reserve Bank's operations during the year are presented in this Section.

INCOME AND EXPENDITURE

15.2 The gross income, expenditure, appropriations and net disposable income of the Reserve Bank have been evolving over the last five years (Table 15.1).

Table 15.1: Trends in Gross Income, Expenditure and Net Disposable Income

(Rupees crore)

Item	2003-04	2002-03	2001-02	2000-01	1999-00
1	2	3	4	5	6
Total Income (Gross)	14,323.70	23,185.64	24,690.34	21,848.87	21,960.97
Less transfer to:					
(i) Contingency Reserve	969.47	6,733.92	6,996.04	6,202.57	6,554.50
(ii) Asset Development Reserve	188.09	890.31	827.91	704.78	711.55
Total (i + ii)	1,157.56	7,624.23	7,823.95	6,907.35	7,266.05
Total Income (Net)	13,166.14	15,561.41	16,866.39	14,941.52	14,694.92
Total Expenditure	7,762.14	6,723.41	6,542.39	5,587.52	5,340.92
Net Disposable Income	5,404.00	8,838.00	10,324.00	9,354.00	9,354.00
Less : Transfer to Funds *	4.00	4.00	4.00	4.00	4.00
Surplus transfer to the Government	5,400.00	8,834.00	10,320.00	9,350.00	9,350.00
of which :					
i) Normal Transfer	3,069.00	7,117.00	8,841.00	7,871.00	7,871.00
ii) Interest differential on account of conversion of special securities into marketable securities	2,331.00	1,717.00	1,479.00	1,479.00	1,479.00

* : An amount of Rupees one crore each transferred to the National Industrial Credit (Long Term Operations) Fund, National Rural Credit (Long Term Operations) Fund, National Rural Credit (Stabilisation) Fund and National Housing Credit (Long Term Operations) Fund during each of the five years.

Surplus Transferable to the Government of India

15.3 The surplus transferable to the Central Government for the year 2003-04 amounted to Rs.5,400.00 crore, inclusive of Rs.2,331.00 crore towards interest differential on special securities converted into marketable securities. The transfer on account of interest differential is intended to compensate the Government for the difference in interest expenditure, which the Government had to bear consequent on the conversion.

Income

15.4 The gross income of the Reserve Bank for the year 2003-04 was Rs.14,323.70 crore which was lower by Rs.8,861.94 crore (38.2 per cent) as compared with the previous year's total income of Rs.23,185.64 crore. There was a decline in income from both domestic and foreign sources (Table 15.2 and Chart XV.1).

Table 15.2: Gross Income

(Rupees crore)

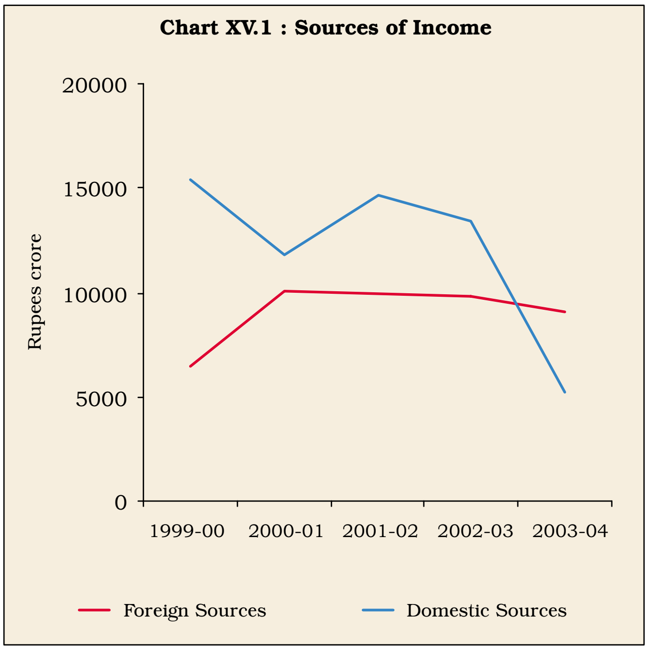
Item	2003-04	2002-03	2001-02	2000-01	1999-2000
1	2	3	4	5	6
A. Foreign Sources					
Interest, Discount, Exchange	9,103.50	9,826.65	9,986.46	10,086.08	6,514.73
B. Domestic Sources					
Interest	4,872.41	13,064.77	14,492.14	11,314.12	14,928.38
Discount	0.01	0.08	10.92	211.59	323.11
Exchange	0.07	0.09	0.08	0.85	0.14
Commission	335.05	279.42	189.51	210.37	185.62
Rent realised and others	12.66	14.63	11.23	25.86	8.99
Total: Domestic	5,220.20	13,358.99	14,703.88	11,762.79	15,446.24
C. Total Income (Gross) (A+B)	**14,323.70**	**23,185.64**	**24,690.34**	**21,848.87**	**21,960.97**

Table 15.3: Contingency and Asset Development Reserves and Surplus Transfer to the Government

(Rupees crore)

Item	2003-04	2002-03	2001-02	2000-01	1999-2000
1	2	3	4	5	6
Total Income (Gross)	14,323.70	23,185.64	24,690.34	21,848.87	21,960.97
Transfer to Contingency Reserve	969.47	6,733.92	6,996.04	6,202.57	6,554.50
	(6.8)	(29.0)	(28.3)	(28.4)	(29.9)
Asset Development Reserve	188.09	890.31	827.91	704.78	711.55
	(1.3)	(3.8)	(3.4)	(3.2)	(3.2)
Surplus transfer to the Government	5,400.00	8,834.00	10,320.00	9,350.00	9,350.00
	(37.7)	(38.1)	(41.8)	(42.8)	(42.6)

Note: Figures in parentheses indicate proportion to total income.



15.5 Transfer to Contingency Reserve, Asset Development Reserve and surplus transfer to the Central Government witnessed some decline in 2003-04 as a proportion to total income (Table 15.3).

Earnings from Foreign Sources

15.6 The Reserve Bank's earnings from the deployment of foreign currency assets and gold decreased by Rs.723.15 crore from Rs.9,826.65 crore in 2002-03 to Rs.9,103.50 crore in 2003-04 (Table 15.4). This was mainly on account of lower money market interest rates in major countries, on the one hand, and a fall in prices of securities due to rise in longer term yields, on the other. Before accounting for mark-to-market depreciation in securities, the rate of earnings on foreign currency assets and gold was 2.8 per cent in 2003-04 as against 3.2 per cent in 2002-03. The rate of earnings on foreign currency assets and gold, after accounting for depreciation, decreased from 3.1 per cent in 2002-03 to 2.1 per cent in 2003-04.

Table 15.4: Earnings from Foreign Sources

(Rupees crore)

Item	As on		Variation	
	June 30, 2004	June 30, 2003	Absolute	Per cent
1	2	3	4	5
Foreign Currency Assets (FCA)	5,24,865.01	3,65,000.98	1,59,864.03	43.8
Gold	18,655.48	17,182.40	1,473.08	8.6
Special Drawing Rights (SDR)	8.42	6.09	2.33	38.3
Reserve Position in the IMF	5,980.47 **	4,534.03	1,446.44	31.9
Total Foreign Exchange Reserves (FER)	5,49,509.38	3,86,723.50	1,62,785.88	42.1
Average FCA	4,38,958.40	3,17,297.00	1,21,661.40	38.3
Earnings (Interest, Discount, Exchange gain/loss, Capital gain / loss on Securities)	12,415.99	10,219.47	2,196.52	21.5
Depreciation on Securities	(-) 3,312.49	(-) 392.82	2,919.67	743.3
Earnings Net of Depreciation	9,103.50	9,826.65	(-) 723.15	(-) 7.4
Memo Items:				
Unrealised appreciation on Securities	330.31	1,888.12	(-) 1,557.81	(-) 82.5
Earnings as percentage of Average FCA	2.8	3.2		
Earnings (net of depreciation) as percentage of Average FCA	2.1	3.1		

** : Reserve Position in the International Monetary Fund (IMF), which was shown as a memo item from May 23, 2003 to March 26, 2004 has been included in the reserves from the week ended April 2, 2004.

Table 15.5: Earnings from Domestic Sources

(Rupees crore)

Item	As on		Variation	
	June 30, 2004	June 30, 2003	Absolute	Per cent
1	2	3	4	5
Domestic Assets	84,872.74	1,54,812.91	(-) 69,940.17	(-) 45.2
Weekly average of Domestic Assets	88,288.77	1,56,365.36	(-) 68,076.59	(-) 43.5
Earnings	5,220.20	13,358.99	(-) 8,138.79	(-) 60.9
	(2,744.69)	(642.81)		
of which:				
(i) Profit on Sale of Securities	2,322.62	4,798.03	(-) 2,475.41	(-) 51.6
(ii) Interest on Securities	1,938.28	7,100.29	(-) 5,162.01	(-) 72.7
(iii) Interest on Loans and Advances	376.64	1,013.63	(-) 636.99	(-) 62.8
(iv) Other Earnings	582.66	447.04	135.62	30.3
Memo Items:				
Earnings in percentage terms (on average domestic assets)	5.9	8.5		
Earnings in percentage terms (excluding profit on sale of securities)	3.3	5.5		

Note : Figures in parentheses are depreciation on securities.

Income from Domestic Sources

15.7 Domestic income decreased by Rs.8,138.79 crore (60.9 per cent) from Rs.13,358.99 crore in 2002-03 to Rs.5,220.20 crore in 2003-04. This decline in income was mainly due to (a) reduction in profit from sale of rupee securities under open market operations and booking of substantially higher depreciation in the value of rupee securities, (b) substantial rise in cost of monetary operations under the Liquidity Adjustment Facility (LAF), (c) reduction in interest income due to decline in the size of the portfolio and (d) investment of Government of India surplus balances in rupee securities held by the Reserve Bank (Table 15.5).

15.8 Profits booked on sale of securities amounted to Rs.2,322.62 crore in 2003-04, representing a decrease of Rs.2,475.41 crore over the previous year. The interest income on ways and means advances declined by Rs.241.98 crore from Rs.612.50 crore in 2002-03 to Rs.370.52 crore in 2003-04, reflecting decreased recourse by the Central Government to this facility and also the lower Bank Rate. Interest earnings from loans and advances to banks/financial institutions declined by Rs.395.01 crore from Rs.401.13 crore in 2002-03 to Rs.6.12 crore in 2003-04 due to lower utilisation of the refinance facility by primary dealers/scheduled commercial banks combined with lower interest rates applicable on these advances.

Expenditure

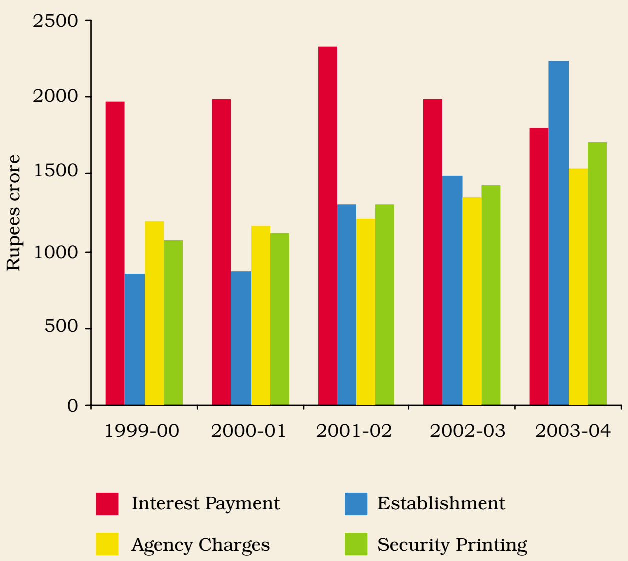
15.9 Total expenditure of the Reserve Bank increased by Rs.1,038.73 crore (15.5 per cent) from Rs.6,723.41 crore in 2002-03 to Rs.7,762.14 crore in 2003-04 (Table 15.6 and Chart XV.2).

Table 15.6: Expenditure

(Rupees crore)

Item	2003-04	2002-03	2001-02	2000-01	1999-2000
1	2	3	4	5	6
I. Interest Payment	**1,808.48**	**1,990.09**	**2,334.99**	**1,994.80**	**1,971.88**
of which:					
a) Scheduled Banks	1,323.23	1,483.02	1,838.57	1,660.83	1,656.18
b) Payment in *lieu* of service charges on borrowings from IMF payable to Government of India	–	–	–	–	7.82
II. Establishment	**2,232.99**	**1,488.86**	**1,304.36**	**870.85**	**846.75**
III Non-Establishment	**3,720.67**	**3,244.46**	**2,903.04**	**2,721.87**	**2,522.29**
of which:					
a) Agency charges	1,539.12	1,352.41	1,207.84	1,160.70	1,193.62
b) Security printing	1,709.56	1,433.09	1,304.49	1,122.78	1,068.44
Total [I+II+III]	**7,762.14**	**6,723.41**	**6,542.39**	**5,587.52**	**5,340.92**

Chart XV.2 : Major Expenditure Items



Interest Payment

15.10 Interest payment decreased by Rs.181.61 crore (9.1 per cent) from Rs.1,990.09 crore in 2002-03 to Rs.1,808.48 crore in 2003-04 due to a reduction in the cash reserve ratio and lower interest rates payable on eligible CRR balances.

Establishment Expenditure

15.11 Establishment expenditure increased by Rs.744.13 crore (49.9 per cent) from Rs.1,488.86 crore in 2002-03 to Rs.2,232.99 crore in 2003-04 as a result of increased provisioning in respect of gratuity and superannuation funds and payment of *ex-gratia* of Rs.408.00 crore to staff who opted for Optional Early Retirement Scheme (OERS). As per the actuarial valuation, the appropriation to the Gratuity and Superannuation Fund was to the extent of Rs.1,010.00 crore during 2003-04 as against Rs.616.67 crore during the previous year. The establishment expenditure during 2003-04 comprised of salary (14.5 per cent), allowances (25.7 per cent), funds (47.2 per cent) and miscellaneous expenditures (12.6 per cent).

Non-Establishment Expenditure

15.12 Expenditure on security printing comprising, *inter alia*, cost of printing currency notes and cheque forms, increased by Rs.276.47 crore (19.3 per cent) from Rs.1,433.09 crore in 2002-03 to Rs.1,709.56 crore in 2003-04 mainly due to higher indent and supply of notes by more than 150 crore pieces.

BALANCE SHEET

Liabilities

National Industrial Credit (Long Term Operations) Fund

15.13 There were no operations in the National Industrial Credit (Long Term Operations) Fund (established under Section 46C of the Reserve Bank of India Act, 1934) during 2003-04 except the credit of Rs.1.00 crore to the Fund out of the Reserve Bank's income.

National Housing Credit (Long Term Operations) Fund

15.14 The National Housing Credit (Long Term Operations) Fund was established by the Reserve Bank in terms of Section 46 D(I) of the Reserve Bank of India Act, 1934 in January 1989. A token contribution of Rs.1.00 crore was made to the Fund out of the Reserve Bank's income during 2003-04.

Deposits - Banks

15.15 'Deposits - Banks' represent balances maintained by banks in current accounts with the Reserve Bank mainly for maintaining Cash Reserve Ratio (CRR) and as working funds for clearing adjustments.

Deposits - Others

15.16 'Deposits - Others' include deposits from financial institutions, employees' provident fund deposits, surplus earmarked pending transfer to the Government and sundry deposits.

Other Liabilities

15.17 'Other Liabilities' include the internal reserves and provisions of the Reserve Bank and net credit balance in the RBI General Account. These liabilities have increased by Rs.11,573.48 crore (9.8 per cent) from Rs.1,18,356.01 crore as on June 30, 2003 to Rs.1,29,929.49 crore as on June 30, 2004 mainly on account of increase in the levels of the Currency and Gold Revaluation Account (CGRA).

15.18 The reserves, *viz.* Contingency Reserve, Asset Development Reserve, Currency and Gold Revaluation Account and Exchange Equalisation Account reflected in 'Other Liabilities' are in addition to the 'Reserve Fund' of Rs.6,500.00 crore held by the Reserve Bank as a distinct balance sheet head.

Currency and Gold Revaluation Account (CGRA) and Exchange Equalisation Account

15.19 Gains/losses on valuation of foreign currency assets and gold due to movements in the exchange rates and/or prices of gold are not taken to the Profit and Loss Account but instead booked under a balance sheet head named as CGRA. The balance represents accumulated net gain on valuation of foreign currency assets and gold. During 2003-04, there was an accretion of Rs 11,006.63 crore to the CGRA, thus increasing its balance from Rs.51,276.41 crore as on June 30, 2003 to Rs.62,283.04 crore as on June 30, 2004. The balance in the CGRA at the end of June 2004 was equivalent to 11.5 per cent of foreign currency assets and gold holdings of the Reserve Bank, as compared with 13.4 per cent at the end of June 2003. The decline was mainly on account of increase in the level of foreign currency assets on the one hand, and appreciation of the rupee against the US dollar during 2003-04, on the other. The balance in the Exchange Equalisation Account (EEA) represents provision made for exchange losses arising out of forward commitments. The balance in the EEA as on June 30, 2004 stood at Rs 5.65 crore. The balances in the CGRA and the EEA are grouped under 'Other Liabilities' in the balance sheet (Table 15.7).

Contingency Reserve and Asset Development Reserve

15.20 The Reserve Bank maintains a Contingency Reserve (CR) to enable it to absorb unexpected and unforeseen contingencies. The Reserve Bank has set an indicative target for the CR at 12 per cent of the Reserve Bank's total assets to be achieved in phases by the year 2005, subject to review if considered necessary. The balance in the CR has increased from Rs.55,249.29 crore as on June 30, 2003 to Rs.56,218.76 crore as on June 30, 2004. A transfer of Rs.969.47 crore was made to the CR during 2003-04 from the Reserve Bank's income. The balance in the CR is sufficient to meet contingent liabilities.

Table 15.7: Balances in Currency and Gold Revaluation Account and Exchange Equalisation Account

(Rupees crore)

As on June 30	Currency and Gold Revaluation Account	Exchange Equalisation Account
1	2	3
2000	27,608.43	791.27
2001	29,124.44	49.46
2002	51,010.77	51.50
2003	51,276.41	567.25
2004	62,283.04	5.65

15.21 In order to meet the internal capital expenditure and make investments in its subsidiaries and associate institutions, the Reserve Bank had created a separate Asset Development Reserve (ADR) in 1997-98, with the aim of reaching one per cent of the Reserve Bank's total assets within the overall target of 12 per cent set for the CR. In the year 2003-04, an amount of Rs.188.09 crore was transferred from income to the ADR raising its level from Rs.5,590.85 crore as on June 30, 2003 to Rs.5,778.94 crore as on June 30, 2004. The CR and ADR together constituted 10.2 per cent of total assets of the Reserve Bank as on June 30, 2004 (Table 15.8).

Table 15.8: Balances in Contingency Reserve and Asset Development Reserve

(Rupees crore)

As on June 30	Balance in CR	Balance in ADR	Total	Percentage to total assets
1	2	3	4	5
2000	29,911.56	3,167.85	33,079.41	9.2
2001	36,514.13	3,872.63	40,386.76	9.9
2002	48,434.17	4,700.54	53,134.71	11.7
2003	55,249.29	5,590.85	60,840.14	11.7
2004	56,218.76	5,778.94	61,997.70	10.2

CR : Contingency Reserve. ADR : Asset Development Reserve.

Assets

Foreign Currency Assets

15.22 The foreign currency assets comprise foreign securities held in the Issue Department and balances held abroad and investments in foreign securities held in the Banking Department. Such assets rose from Rs.3,65,000.98 crore as on June 30, 2003 to Rs.5,24,865.01 crore as on June 30, 2004. The increase in the level of foreign currency assets was mainly on account of net purchases of US dollars from the market, interest and discount received and revaluation gains.

Investment in Government of India Rupee Securities

15.23 Investment in Government of India Rupee Securities which stood at Rs.1,05,144.04 crore as on June 30, 2003 decreased by Rs.64,964.30 crore (61.8 per cent) to Rs.40,179.74 crore as on June 30, 2004 (Table 15.9 and Chart XV.3).

Table 15.9: Outstanding Foreign Currency and Domestic Assets

(Rupees crore)

As on June 30	Foreign Currency Assets	Domestic Assets
1	2	3
2000	1,50,901.13	2,09,065.64
2001	1,91,226.06	2,16,246.37
2002	2,67,333.18	1,86,226.62
2003	3,65,000.98	1,54,812.91
2004	5,24,865.01	84,872.74

Investments in Shares of Subsidiaries and Associate Institutions

15.24 There was no change in the Reserve Bank's investments in the shares of its subsidiaries and associate institutions during 2003-04 (Table 15.10).

Other Assets

15.25 'Other Assets' comprise mainly fixed assets, gold holdings in the Banking Department, amounts spent on projects pending completion and staff advances. The level of 'Other Assets' increased by Rs.2,035.21 crore (16.4 per cent) from Rs.12,424.56 crore as on June 30, 2003 to Rs.14,459.77 crore as on June 30, 2004.

Chart XV.3: Trends in Foreign Currency and Domestic Assets

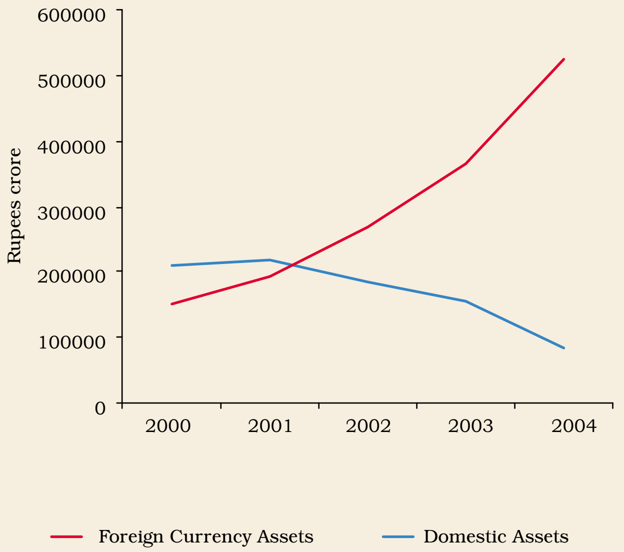


Table 15.10: Investments in Shares of Subsidiaries/Associate Institutions

(Rupees crore)

Institution	Book value of shares held as on June 30, 2004	Book value of shares held as on June 30, 2003
1	2	3
1. Deposit Insurance and Credit Guarantee Corporation	50.00	50.00
2. National Bank for Agriculture and Rural Development	1,450.00	1,450.00
3. State Bank of India	1,222.73	1,222.73
4. National Housing Bank	450.00	450.00
5. Bharatiya Reserve Bank Note Mudran (Pvt.) Ltd.	800.00	800.00
6. Infrastructure Development Finance Co. Ltd.	150.00	150.00
Total	**4,122.73**	**4,122.73**

Financial Sector Reforms and the Reserve Bank's Balance Sheet

15.26 The process of financial sector reforms has impacted the Reserve Bank's balance sheet in terms of size, composition and sources of income (Box XV.1).

Auditors

15.27 The accounts of the Reserve Bank for the year 2003-04 were audited by M/s. P.B.Vijayaraghavan & Co., Chennai, M/s. Khimji Kunverji & Co., Mumbai, M/s. J.L. Sengupta & Co., Kolkata, M/s. S.N. Nanda & Co., New Delhi, M/s Rajendra K. Goel & Co., New Delhi and M/s. Ford, Rhodes, Parks & Co., Mumbai appointed by the Central Government.

Box XV. 1
Financial Sector Reforms and the Reserve Bank's Balance Sheet

The financial sector reforms initiated in the early 1990s have influenced the Reserve Bank's Annual Financial Statements and accounting policies in terms of size and composition of assets and sources of income and expenditure. The last 14 years have also witnessed a shift in the Reserve Bank's policy towards transparency and disclosure in accounting. The Committee on Financial Sector Reforms (Chairman : Shri M. Narasimham) gave a further impetus to the reform process. Liberalisation in trade and foreign investment policies, exchange control liberalisation and other reforms have strengthened the country's balance of payments. Foreign exchange reserves have accordingly increased substantially over this period, which have had a significant impact on the nature of the Reserve Bank's balance sheet.

The salient features of financial sector reforms and their impact on the Reserve Bank's Balance Sheet are as under:

- Since 1990 'Interest Income' and 'Interest Expenditure' are being furnished in the Profit and Loss Account as against 'Net Income' reported earlier. The break-up of 'Income' into 'Income from Domestic Sources' and 'Income from Foreign Sources' is being provided since 1994. Allocation to statutory funds is being disclosed as an item of appropriation of surplus funds. A detailed break-up of major items of Annual Financial Statements is now available in the Annual Report.

- The 'Significant Accounting Policies' and 'Notes to the Accounts' are disclosed every year from 1992 onwards.

- Several Accounting Standards, both Indian and international, were adopted with suitable modifications during the last decade. The RBI General Regulation 23 was amended in 1996 to carry out the valuation of rupee securities and foreign securities at monthly intervals and foreign currency assets at weekly intervals. Section 33(4) of the RBI Act, 1934 was amended in 1991 to provide for valuation of gold at rates not exceeding international market rates at the end of every month.

- A substantial part of income was earmarked every year to meet exchange losses / exchange guarantee on account of schemes such as the FCNRA scheme and India Development Bonds. It was decided that the exchange risk liability on account of these schemes would be met by the Central Government which resulted in easing of pressure on the Exchange Equalisation Account.

- The practice of transferring large sums to the Statutory Developmental Funds out of surplus income was discontinued from 1993; instead a token amount of Rupees one crore each is being contributed to the funds.

- It was decided that no further loans and advances would be made from the Development Funds to development finance institutions and the repayments made by them will not be redeployed for fresh lending to them. The balance in statutory funds consequently increased substantially and it was decided in 1998 to transfer these unutilised balances to the Contingency Reserve, resulting in the strengthening of the Reserve Bank's internal reserves.

- The outstanding loan balances of development finance institutions with the Reserve Bank were transferred to the Central Government in March 2002 in exchange for Government securities of an equal amount. While the loans and advances on the asset side of the balance sheet were, thus, replaced by Government securities, the balances in the Statutory Funds on the liability side were transferred to the Contingency Reserve.

- In the recent past, the composition of assets of the Reserve Bank has undergone a major change. Foreign currency assets and gold which stood at 41.9 per cent of total assets as on June 1997 increased to 89.1 per cent as on June 30, 2004. Over the same period, the share of domestic assets in total assets declined from 58.1 per cent as on June 30, 1997 to 10.9 per cent as on June 30, 2004. The substantial change in the asset composition was mainly on account of the absorption of external inflows into foreign exchange reserves and sterilisation of the incremental liquidity through sale of domestic securities.

- Corresponding to the changes in the asset composition of the balance sheet, the Reserve Bank's income profile has also undergone changes. The gross income increased from Rs.11,931.7 crore during the year 1995-96 to Rs. 24,690.3 crore during 2001-02, mainly due to factors such as reduced interest expense on CRR balances of banks, discontinuance of issuance of exchange guarantees, shifting of exchange loss of FCNRA deposits to the Government and increase in the domestic interest rates during the period. The gross income, however, has been showing a decline since 2001-02, which could be attributed to high-yielding Government securities getting replaced by low-yielding foreign currency assets, fall in both domestic and international interest rates, lower demand for refinance from the Reserve Bank due to adequate liquidity in the market and reduction in the Bank Rate.

APPENDIX TABLE I.1 : SELECT MACROECONOMIC AND FINANCIAL INDICATORS

Item	2003-04	2002-03	2001-02	2000-01	1999-00	Average	
						1994-95 to 2003-04 (10 years)	1980-81 to 1989-90 (10 years)
1	2	3	4	5	6	7	8
1. Real GDP (% change)	8.2 RE	4.0 QE	5.8 P	4.4	6.1	6.2	5.8
2. Industrial Production (% change)#	6.9 P	5.7	2.7	5.0	6.7	6.6	7.4
3. Agricultural Production (% change)*	19.6	-15.2	7.6	-6.4	-1.3	1.8	5.2
4. Foodgrains Production (Million tonnes)*	212.1	174.2	212.9	196.8	209.8	197.3	146.5
5. Gross Domestic Saving Rate (% of GDP)	n.a.	24.2 QE	23.5 P	23.7	24.2	23.7 +	19.4
6. Gross Domestic Investment Rate (% of GDP)	n.a.	23.3 QE	23.1 P	24.4	25.3	24.5 +	21.2
7. Central Government Finances (% of GDP)							
a) Total Revenue Receipts	9.5 RE	9.4	8.8	9.2	9.4	9.1	9.8
b) Total Expenditure	17.1 RE	16.8	15.9	15.6	15.4	15.7	17.7
c) Revenue Deficit	3.6 RE	4.4	4.4	4.1	3.5	3.5	1.7
d) Fiscal Deficit	4.8 RE	5.9	6.2	5.7	5.4	5.5	6.8
e) Net RBI Credit to Centre	-2.8	-1.1	-0.2	0.3	-0.3	-0.1	2.1
f) Interest Payments	4.5 RE	4.8	4.7	4.8	4.7	4.5	2.6
g) Domestic Debt	60.5 RE	60.7	56.7	52.8	49.7	51.7	41.7
8. Monetary Aggregates (% change)							
a) Broad Money (M_3)	16.6 P	12.7 @	14.1	16.8	14.6	16.8	17.2
b) Narrow Money (M_1)	21.8 P	12.0	11.4	11.0	10.6	14.5	15.1
c) Reserve Money	18.3	9.2	11.4	8.1	8.2	12.3	16.8
9. Scheduled Commercial Banks (% change)							
a) Aggregate Deposits	17.5	13.4 @	14.6	18.4	13.9	17.0	18.1
b) Bank Credit	15.3	16.1 @	15.3	17.3	18.2	17.8	16.8
c) Non-Food Credit	18.4	18.6 @	13.6	14.9	16.5	18.2	17.8
d) Investments in Government Securities	25.1	27.3	20.9	22.1	24.7	20.6	19.4
10. Wholesale Price Index (% change)							
a) Point-to-Point	4.6	6.5	1.6	4.9	6.5	6.1	7.5
b) Average	5.4	3.4	3.6	7.2	3.3	5.8	8.0
11. Consumer Price Index - Industrial Workers (% change)							
a) Point-to-Point	3.5	4.1	5.2	2.5	4.8	6.6	8.9
b) Average	3.9	4.0	4.3	3.8	3.4	6.9	9.1
12. BSE Sensitive Index (% change)	40.1	-3.8	-22.0	-8.4	41.4	6.9	22.3
13. Trade and Balance of Payments							
a) Exports in US $ (% change)	20.4 P	20.3	-1.6	21.0	10.8	11.5	8.1
b) Imports in US $ (% change)	25.4 P	19.4	1.7	1.7	17.2	13.1	7.2
c) Current Account (% of GDP)	1.4	0.8	0.2	-0.8	-1.0	-0.6	-1.8
d) Capital Account (% of GDP)	3.7	2.4	2.2	2.2	2.3	2.4	1.6
14. Foreign Exchange Reserves** (US $ million)	1,12,959	76,100	54,716	42,897	38,694	–	–
15. External Debt** (US $ million)	1,12,593	1,04,869	98,757	1,01,132	98,263	–	–
a) Debt-GDP Ratio	17.6	20.2	21.1	22.6	22.1	23.4	n.a.
b) Debt-Service Ratio	18.3	15.1	13.9	17.2	16.2	18.9	n.a.
16. Exchange Rate (Rupee / US$)							
a) High	43.45	47.51	46.56	43.61	42.44	31.32	7.73
b) Low	47.46	49.06	48.85	46.89	43.64	49.06	17.13

P : Provisional. n.a. : Not available. @ : Adjusted for mergers in the banking system since May 3, 2002.

* : Figures for 2003-04 as per the Fourth Advance Estimate (as on August 5, 2004). ** : As at the end of the period.

: Base : 1993-94 =100 for columns 2 to 7 and 1980-81=100 for column 8. – : Not applicable.

RE : Revised Estimates. QE : Quick Estimates. + : Average of 9 years starting from 1994-95 to 2002-03.

APPENDIX TABLE I.2 INTEREST RATE STRUCTURE OF SCHEDULED COMMERCIAL BANKS

(Per cent per annum)

Item	Rates as on												
	Jan. 16, 2004	Jan. 9, 2004	Jan. 2, 2004	Dec. 5, 2003	Nov. 7, 2003	Oct. 3, 2003	Sept.12, 2003	July 11, 2003	June 20, 2003	May 16, 2003	May 9, 2003	May 2, 2003	April 11, 2003
1	2	3	4	5	6	7	8	9	10	11	12	13	14
A. Lending Rates													
Size of Credit Limit													
1. Up to Rs. 2 lakh	≤ PLR	≤ PLR	≤ PLR	≤ PLR	≤ PLR	≤ PLR	≤ PLR	≤ PLR	≤ PLR	≤ PLR	≤ PLR	≤ PLR	≤ PLR
2. Over Rs. 2 lakh (Prime Lending Rate*)	10.25-11.00	10.25-11.00	10.25-11.00	10.50-11.00	10.50-11.50	10.50-11.50	10.50-11.50	10.50-11.50	10.50-11.50	10.50-11.50	10.50-11.50	10.75-11.50	10.75-11.50
B. Deposit Rates													
Category of Account													
1. Current	Nil	Nil	Nil	Nil	Nil	Nil	Nil	Nil	Nil	Nil	Nil	Nil	Nil
2. Savings	3.50	3.50	3.50	3.50	3.50	3.50	3.50	3.50	3.50	3.50	3.50	3.50	3.50
3. Term Deposits @													
a) Up to and including one year	4.00-4.75	4.00-4.75	4.00-4.75	4.00-5.00	4.00-5.00	4.00-5.25	4.00-5.25	4.00-5.25	4.00-5.50	4.25-5.50	4.25-5.50	4.00-5.50	4.00-5.50
b) 1-2 years	5.00	5.00	5.00	5.00-5.25	5.00-5.25	5.00-5.50	4.75-5.25	5.00-5.75	5.00-5.75	5.25-5.75	5.25-5.75	5.25-5.75	5.25-5.75
c) 2-3 years	5.00-5.25	5.00-5.25	5.00-5.25	5.00-5.50	5.00-5.50	5.00-5.75	5.00-5.75	5.00-5.75	5.00-5.75	5.50-5.75	5.25-5.75	5.25-6.00	5.25-6.00
d) > 3 years	5.25-5.50	5.25-6.00	5.25-5.75	5.25-5.75	5.25-6.00	5.25-6.00	5.25-6.00	5.25-6.00	5.25-6.00	5.75-6.00	5.50-6.00	5.50-6.25	5.50-6.25
Memo Item :													
Bank Rate #	6.00	6.00	6.00	6.00	6.00	6.00	6.00	6.00	6.00	6.00	6.00	6.00 (April 29, 2003)	6.25

* : Data relate to major public sector banks.

≤ : Not exceeding.

\# : The change in the Bank Rate was made effective from the close of business of the date indicated in the parenthesis.

@ : The minimum maturity period of term deposits is 15 days, effective April 29, 1998. Data relate to major public sector banks.

APPENDIX TABLE I.3 : INTEREST RATES ON EXPORT CREDIT

(Per cent per annum)

Export Credit	Rates Effective									
	May 1, 2003	September 26, 2001#	May 5, 2001#	January 6, 2001	May 26, 2000	October 29, 1999	April 1, 1999	August 6, 1998	April 30, 1998	January 1, 1998
1	2	3	4	5	6	7	8	9	10	11
1. Pre-shipment Credit										
i) Up to 180 days	≤ PLR-2.5 PP	≤ PLR-2.5 PP	≤ PLR-1.5 PP	10.00	10.00	10.00	10.00	9.00	11.00	12.00
ii) Beyond 180 days and up to 270 days	Free	≤ PLR+0.5 PP	≤ PLR+1.5 PP	13.00	13.00	13.00	13.00	12.00	14.00	14.00
iii) Against incentives receivable from Government covered by ECGC Guarantee up to 90 days	≤ PLR-2.5 PP	≤ PLR-2.5 PP	≤ PLR-1.5 PP	10.00	10.00	10.00	10.00	9.00	11.00	12.00
2. Post-shipment Credit										
i) Demand Bills for transit period (as specified by FEDAI)	≤ PLR-2.5 PP	≤ PLR-2.5 PP	≤ PLR-1.5 PP	≤ 10.00	≤ 10.00	≤ 10.00	≤ 10.00	9.00	≤ 11.00	≤ 11.00
ii) Usance Bills										
(for total period comprising usance period of export bills, transit period as specified by FEDAI and grace period wherever applicable)										
a) Up to 90 days	≤ PLR-2.5 PP	≤ PLR-2.5 PP	≤ PLR-1.5 PP	≤ 10.00	≤ 10.00	≤ 10.00	≤ 10.00	9.00	≤ 11.00	≤ 11.00
b) Beyond 90 days and up to six months from the date of shipment	Free	≤ PLR+0.5 PP	≤ PLR+1.5 PP	12.00	12.00	12.00	12.00	11.00	13.00	13.00
c) Beyond six months from the date of shipment	–	–	–	–	–	–	–	–	–	20.00 ## (Min.)
iii) Against incentives receivable from Government covered by ECGC Guarantee (up to 90 days)	≤ PLR-2.5 PP	≤ PLR-2.5 PP	≤ PLR-1.5 PP	≤ 10.00	≤ 10.00	≤ 10.00	≤ 10.00	9.00	≤ 11.00	≤ 11.00
iv) Against undrawn balance (up to 90 days)	≤ PLR-2.5 PP	≤ PLR-2.5 PP	≤ PLR-1.5 PP	≤ 10.00	≤ 10.00	≤ 10.00	≤ 10.00	9.00	≤ 11.00	≤ 11.00
v) Against retention money (for supplies portion only) payable within one year from the date of shipment (up to 90 days)	≤ PLR-2.5 PP	≤ PLR-2.5 PP	≤ PLR-1.5 PP	≤ 10.00	≤ 10.00	≤ 10.00	≤ 10.00	9.00	≤ 11.00	≤ 11.00
3. Deferred Credit										
Deferred credit for the period beyond 180 days	Free	Free	Free	Free	Free	Free	Free	Free	Free (FDA)	Free (FDA)
4. Export Credit, not otherwise specified										
a) Pre-shipment credit	Free	Free	Free	Free	Free	Free	Free	Free	Free	
b) Post-shipment credit	Free	Free	Free	Free	25.00 (Min.)	Free	20.00 (Min.)	20.00 (Min.)	20.00 (Min.)	20.00 (Min.)

FDA : From the date of advance. ≤ : Not Exceeding Min. : Minimum. – : Not Applicable. PP : Percentage points.

\# : These are ceiling rates, banks would be free to charge any rate below the ceiliing rate.

\## : Chronic cases, *i.e.* , overdues as on July 1, 1997 are exempted.

Note : 'Free' means banks are free to charge interest rates keeping in view the PLR and spread guidelines.

APPENDIX TABLE II.1 : GROWTH RATES AND SECTORAL COMPOSITION OF REAL GROSS DOMESTIC PRODUCT (At 1993-94 Prices)

(Per cent)

Sector	Growth Rate					Share in real GDP			
	2003-04#	2002-03*	2001-02@	2000-01	1997-98 to 2002-03**	2003-04#	2002-03*	2001-02@	2000-2001
1	2	3	4	5	6	7	8	9	10
1. Agriculture and Allied Activities	**9.1**	**-5.2**	**6.5**	**-0.1**	**0.9**	**22.1 (24.2)**	**22.0 (-31.4)**	**24.1 (26.9)**	**23.9 (-0.6)**
of which :									
Agriculture	n.a.	-6.0	6.7	-0.4	0.7	n.a.	20.0	22.1	21.9
2. Industry	**6.8**	**6.2**	**3.5**	**6.5**	**4.4**	**21.7 (18.2)**	**22.0 (33.7)**	**21.5 (13.3)**	**22.0 (32.1)**
of which :									
a) Mining and quarrying	4.4	8.8	2.2	2.4	4.9	2.3	2.4	2.3	2.3
b) Manufacturing	7.3	6.2	3.6	7.4	4.3	17.1	17.2	16.9	17.2
c) Electricity, gas and water supply	5.5	3.8	3.6	4.3	5.3	2.4	2.4	2.5	2.5
3. Services	**8.5**	**7.2**	**6.4**	**5.6**	**7.8**	**56.2 (57.6)**	**56.1 (97.7)**	**54.4 (59.9)**	**54.1 (68.5)**
of which :									
a) Construction	6.2	7.3	3.1	6.7	6.9	5.2	5.3	5.1	5.2
b) Trade, hotels and restaurants	11.2 ##	4.5	8.7	4.0	6.6	24.8 ##	15.1	15.0	14.6
c) Transport, storage and communications	n.a.	11.6	8.6	12.2	10.0	n.a.	9.0	8.4	8.2
d) Financing, insurance, real estate and business services	6.8	8.8	4.5	3.5	7.7	12.8	13.0	12.4	12.6
e) Community, social and personal services	6.0	5.8	5.6	5.2	8.5	13.4	13.7	13.4	13.5
4. Gross Domestic Product at Factor Cost	**8.2**	**4.0**	**5.8**	**4.4**	**5.2**	**100.0**	**100.0**	**100.0**	**100.0**

: Revised Estimates. * : Quick Estimates. @ : Provisional Estimates. ** : Average during the period n.a. : Not available.

: Corresponds to 'trade, hotels and restaurants' and 'transport, storage and communications'.

Note : Figures in parentheses indicate relative contribution of the sectors to the real GDP growth.

Source : Central Statistical Organisation.

APPENDIX TABLE II.2 : QUARTERLY GROWTH RATES AND SECTORAL COMPOSITION OF REAL GROSS DOMESTIC PRODUCT (At 1993-94 Prices)

(Per cent)

Sector	2003-04				2002-03				2001-02				2000-01			
	Q_1	Q_2	Q_3	Q_4	Q_1	Q_2	Q_3	Q_4	Q_1	Q_2	Q_3	Q_4	Q_1	Q_2	Q_3	Q_4
1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	16	17
1. Agriculture and Allied Activities	**0.1**	**6.8**	**16.5**	**10.5**	**0.6**	**-2.9**	**-9.8**	**-6.3**	**4.3**	**7.0**	**6.2**	**9.7**	**-0.2**	**5.8**	**-0.5**	**-4.5**
	(22.0)	**(17.8)**	**(26.8)**	**(21.2)**	**(23.2)**	**(18.1)**	**(25.4)**	**(20.8)**	**(24.2)**	**(19.6)**	**(28.7)**	**(23.0)**	**(24.3)**	**(19.3)**	**(28.7)**	**(22.4)**
2. Industry	**6.0**	**6.3**	**6.8**	**7.9**	**4.8**	**6.7**	**6.7**	**6.7**	**2.6**	**3.2**	**3.7**	**4.3**	**7.9**	**6.7**	**7.3**	**4.4**
	(22.2)	**(23.1)**	**(20.3)**	**(21.6)**	**(22.1)**	**(23.5)**	**(21.0)**	**(21.6)**	**(22.1)**	**(23.3)**	**(20.1)**	**(21.0)**	**(22.5)**	**(23.8)**	**(20.6)**	**(21.5)**
of which :																
a) Manufacturing	6.6	7.4	7.5	7.6	4.0	6.7	6.9	7.3	3.2	3.4	3.7	4.4	8.7	7.7	7.8	5.3
	(17.4)	(18.2)	(15.9)	(16.9)	(17.2)	(18.4)	(16.4)	(17.0)	(17.4)	(18.2)	(15.6)	(16.5)	(17.6)	(18.6)	(16.0)	(16.8)
b) Mining and quarrying	2.3	2.0	3.6	9.0	11.8	10.1	7.6	6.3	-1.4	1.0	4.8	3.9	4.0	2.7	3.3	0.0
	(2.3)	(2.3)	(2.2)	(2.4)	(2.3)	(2.5)	(2.3)	(2.3)	(2.2)	(2.3)	(2.2)	(2.3)	(2.3)	(2.5)	(2.2)	(2.3)
c) Electricity, gas and water supply	4.8	2.9	4.8	9.5	4.3	3.9	4.8	2.2	2.2	3.7	2.1	3.8	5.9	3.2	8.1	2.8
	(2.5)	(2.5)	(2.2)	(2.3)	(2.5)	(2.6)	(2.3)	(2.2)	(2.5)	(2.7)	(2.3)	(2.3)	(2.6)	(2.7)	(2.3)	(2.3)
3. Services	**7.2**	**10.0**	**9.1**	**7.6**	**7.2**	**7.9**	**6.8**	**6.8**	**5.7**	**5.7**	**7.2**	**6.3**	**6.5**	**6.9**	**6.2**	**3.7**
	(55.8)	**(59.2)**	**(52.9)**	**(57.2)**	**(54.8)**	**(58.4)**	**(53.6)**	**(57.6)**	**(53.7)**	**(57.1)**	**(51.2)**	**(56.0)**	**(53.2)**	**(56.9)**	**(50.7)**	**(56.1)**
of which :																
a) Construction	5.9	6.4	4.8	7.6	7.1	9.5	7.4	5.5	-1.2	0.1	4.2	7.7	12.7	10.0	7.2	-0.9
	(5.4)	(5.4)	(4.7)	(5.1)	(5.4)	(5.6)	(5.0)	(5.1)	(5.3)	(5.4)	(4.8)	(5.0)	(5.6)	(5.6)	(4.8)	(5.0)
b) Trade, hotels, restaurants, transport, storage and communication	7.3	9.9	13.3	13.8	6.4	7.4	6.5	7.7	7.7	9.0	8.1	9.6	9.1	7.0	6.7	5.0
	(24.2)	(25.0)	(24.2)	(25.7)	(23.7)	(24.7)	(23.6)	(24.4)	(23.4)	(24.3)	(22.6)	(23.5)	(22.8)	(23.5)	(22.2)	(22.9)
c) Financing, insurance, real estate and business services	5.7	6.4	6.5	8.5	9.6	9.8	8.6	7.5	4.4	5.0	4.8	3.9	4.6	3.3	2.5	3.5
	(13.4)	(13.7)	(11.9)	(12.6)	(13.3)	(14.0)	(12.4)	(12.6)	(12.8)	(13.5)	(11.6)	(12.1)	(12.8)	(13.5)	(11.8)	(12.5)
d) Community, social and personal services	9.4	15.2	5.3	-3.1	6.2	6.4	5.6	5.1	6.5	3.4	9.2	2.9	1.5	9.0	8.8	3.5
	(12.8)	(15.0)	(12.1)	(13.8)	(12.3)	(14.1)	(12.7)	(15.5)	(12.2)	(14.0)	(12.2)	(15.3)	(12.0)	(14.3)	(11.9)	(15.8)
4. Gross Domestic Product at Factor Cost	**5.3**	**8.6**	**10.5**	**8.2**	**5.1**	**5.5**	**2.0**	**3.7**	**4.7**	**5.4**	**6.2**	**6.6**	**5.1**	**6.6**	**4.4**	**1.9**
	(100.0)	**(100.0)**	**(100.0)**	**(100.0)**	**(100.0)**	**(100.0)**	**(100.0)**	**(100.0)**	**(100.0)**	**(100.0)**	**(100.0)**	**(100.0)**	**(100.0)**	**(100.0)**	**(100.0)**	**(100.0)**

Note : 1. Figures in parentheses are percentage shares to GDP.
2. Quarters Q_1, Q_2 , Q_3 and Q_4 denote April-June, July-September, October-December and January-March, respectively.
3. Data are provisional.

Source : Central Statistical Organisation.

APPENDIX TABLE II.3 : AGRICULTURAL PRODUCTION

(Million tonnes)

Crop	2003-04*	2002-03	2001-02	2000-01	1999-2000
1	2	3	4	5	6
1. All Crops: Annual Growth Rate (Per cent) #	**19.6**	**-15.2**	**7.6**	**-6.4**	**-1.3**
i) Foodgrains	21.8	-18.5	8.8	-6.7	2.7
ii) Non-foodgrains	16.3	-10.1	5.9	-6.0	-6.8
2. Foodgrains (a+b)	**212.1**	**174.2**	**212.9**	**196.8**	**209.8**
i) Rice	87.0	72.7	93.3	85.0	89.7
ii) Wheat	72.1	65.1	72.8	69.7	76.4
iii) Coarse cereals	37.8	25.3	33.4	31.1	30.3
iv) Pulses	15.2	11.1	13.4	11.1	13.4
a) Kharif	**112.0**	**87.8**	**112.1**	**102.1**	**105.5**
i) Rice	73.9	63.7	80.5	72.8	77.5
ii) Coarse cereals	31.8	20.0	26.7	24.9	23.2
iii) Pulses	6.3	4.1	4.8	4.5	4.8
b) Rabi	**100.0**	**86.4**	**100.8**	**94.7**	**104.3**
i) Rice	13.1	9.0	12.8	12.2	12.2
ii) Wheat	72.1	65.1	72.8	69.7	76.4
iii) Coarse cereals	6.0	5.3	6.7	6.2	7.1
iv) Pulses	8.9	7.0	8.5	6.6	8.6
3. Non-foodgrains					
i) Oilseeds +	25.1	15.1	20.7	18.4	20.7
ii) Sugarcane	236.2	281.6	297.2	296.0	299.3
iii) Cotton@	13.8	8.7	10.0	9.5	11.5
iv) Jute and Mesta ++	11.2	11.4	11.7	10.6	10.6
v) Tea**	857.1	826.2	853.9	847.0	826.0
vi) Coffee**	270.5	275.3	300.8	301.2	292.0

* : Fourth Advance Estimate as on August 5, 2004.
# : Based on Index of Agricultural Production with base triennium ending 1981-82 = 100.
+ : For nine oilseeds out of eleven in all.
@ : Million bales of 170 kg. each.
++ : Million bales of 180 kg. each.
** : Million kilograms; data for tea are on a calendar year basis.
Source : Ministry of Agriculture, Government of India; Tea Board, and Coffee Board.

APPENDIX TABLE II.4 : PROCUREMENT, OFFTAKE AND STOCKS OF FOODGRAINS

(Million tonnes)

Fiscal year	Procurement			Offtake			Stocks *		
	Rice	Wheat	Total	Rice	Wheat	Total	Rice	Wheat	Total @
1	2	3	4	5	6	7	8	9	10
1996-97	11.87	8.16	20.04	12.31	13.32	25.63	13.17	3.24	16.41
1997-98	14.51	9.30	23.82	11.20	7.76	18.96	13.05	5.08	18.12
1998-99	11.56	12.65	24.21	11.83	8.90	20.73	12.16	9.66	21.82
1999-2000	17.28	14.14	31.43	12.42	10.63	23.05	15.72	13.19	28.91
2000-01	20.10	16.35	36.46	10.42	7.79	18.21	23.19	21.50	44.98
2001-02	20.88	20.63	41.51	15.32	15.99	31.30	24.91	26.04	51.02
2002-03	19.16	19.02	38.18	24.64	24.99	49.63	17.16	15.65	32.81
2003-04	21.02	15.80	36.83	23.74	24.19	47.93	13.07	6.93	20.65
First Quarter (April-June)									
2003-04	1.96	15.75	17.71	6.93	6.64	13.57	10.97	24.19	35.17
2004-05 #	3.41	16.68	20.09	4.69	3.60	8.29	10.76	19.15	30.56

* : Stocks are as at end-March.

@ : Including coarse grains.

\# : Procurement and offtake up to June 30, 2004; and stocks as on July 1, 2004.

Source : Ministry of Food, Consumer Affairs and Public Distribution, Government of India.

APPENDIX TABLE II.5 : TRENDS IN INDEX OF INDUSTRIAL PRODUCTION (BASE : 1993-94=100)

Sector	Mining & Quarrying		Manufacturing		Electricity		General	
Weight	10.47		79.36		10.17		100.00	
Period	Index	Growth Rate (per cent)	Index	Growth Rate (per cent)	Index	Growth Rate (per cent)	Index	Growth Rate (per cent)
1	2	3	4	5	6	7	8	9
1999-2000	126.7	1.0 (1.4)	159.4	7.1 (87.5)	148.5	7.3 (10.7)	154.9	6.7 (100.0)
2000-01	130.3	2.8 (4.9)	167.9	5.3 (87.0)	154.4	4.0 (7.7)	162.6	5.0 (100.0)
2001-02	131.9	1.2 (3.8)	172.7	2.9 (86.6)	159.2	3.1 (11.1)	167.0	2.7 (100.0)
2002-03	139.6	5.8 (8.4)	183.1	6.0 (86.0)	164.3	3.2 (5.4)	176.6	5.7 (100.0)
2003-04P	146.9	5.2 (6.3)	196.4	7.3 (86.5)	172.6	5.1 (6.9)	188.8	6.9 (100.0)
2002-03								
April-June	131.4	6.8	173.1	3.7	160.6	3.7	167.5	4.3
July-September	134.2	6.2	178.0	6.9	163.5	3.3	171.9	6.5
October-December	143.6	4.7	184.5	6.1	167.8	4.5	178.5	5.8
January-March	149.1	5.7	196.8	6.9	165.5	1.5	188.7	6.5
April-September	132.8	6.5	175.6	5.5	162.0	3.5	169.7	5.4
October-March	146.3	5.2	190.7	6.5	166.7	3.0	183.6	6.1
2003-04P								
April-June	138.7	5.6	183.4	6.0	167.3	4.2	177.1	5.7
July-September	138.1	2.9	191.5	7.6	166.5	1.9	183.3	6.6
October-December	149.9	4.4	199.2	7.9	174.9	4.3	191.5	7.3
January-March	160.9	8	211.9	7.7	181.7	9.8	203.5	7.9
April-September	138.4	4.2	187.4	6.8	166.9	3.0	180.2	6.2
October-March	155.4	6.2	205.5	7.8	178.3	7.0	197.5	7.6
2004-05P								
April-June	147.2	6.1	197.9	7.9	177.0	5.8	190.5	7.6

P : Provisional.

Note : Figures in parentheses are relative contributions, computed as the ratios (in percentage terms) of the change in the index of the respective industry group to the change in the overall index adjusted for the weight of the relative industry group.

Source : Central Statistical Organisation.

APPENDIX TABLE II.6 : GROWTH IN INDEX OF SEVENTEEN MAJOR INDUSTRY GROUPS OF MANUFACTURING SECTOR (Base : 1993-94=100)

Industry Group	Weight	Index		Percentage Variation		Relative Contribution (Per cent)	
		2003-04P	2002-03	2003-04	2002-03	2003-04	2002-03
1	2	3	4	5	6	7	8
I. Acceleration	**37.72**						
1. Transport equipment and parts	3.984	272.6	232.9	17.0	14.6	14.8	14.3
2. Paper & paper products and printing, publishing & allied industries	2.652	208.7	180.5	15.6	6.8	7.0	3.7
3. Machinery and equipment other than transport equipment	9.565	233.3	201.4	15.8	1.6	28.5	3.6
4. Basic chemicals & chemical products (except products of petroleum & coal)	14.002	208.4	191.8	8.6	3.7	21.7	11.6
5. Wood and wood products, furniture & fixtures	2.701	81.7	76.5	6.9	-17.6	1.3	-5.4
6. Other manufacturing industries	2.559	186.6	173.3	7.7	0.0	3.2	0.0
7. Wool, silk and man-made fibre textiles	2.258	240.5	225.1	6.8	3.0	3.2	1.8
II. Deceleration	**22.77**						
8. Beverages, tobacco and related products	2.382	312.1	287.6	8.5	27.9	5.5	18.1
9. Basic metal and alloy industries	7.453	186.0	170.4	9.1	9.3	10.8	13.1
10. Rubber, plastic, petroleum and coal products	5.728	187.7	179.7	4.4	5.5	4.3	6.5
11. Non-metallic mineral products	4.397	240.6	232.0	3.7	5.1	3.5	6.0
12. Metal products and parts (except machinery and equipment)	2.810	157.3	151.7	3.7	6.4	1.5	3.1
III. Negative	**18.87**						
13. Food products	9.083	167.9	168.7	-0.5	11.0	-0.7	18.4
14. Cotton textiles	5.518	117.4	121.2	-3.1	-2.7	-1.9	-2.2
15. Textile products (including wearing apparel)	2.537	184.3	190.3	-3.2	14.4	-1.4	7.4
16. Jute and other vegetable fibre textiles(except cotton)	0.590	103.4	107.9	-4.2	8.3	-0.2	0.6
17. Leather and leather & fur products	1.139	147.0	152.9	-3.9	-3.2	-0.6	-0.7
MANUFACTURING (Total)	**79.36**	**196.6**	**183.1**	**7.4**	**6.0**	**100.0**	**100.0**

P : Provisional.

Note : 1. The industry groups of manufacturing sector have been categorised according to their performance during 2003-04.

2. The relative contribution is computed as the ratio (in percentage terms) of the change in the index of the respective industry group to the change in the overall index adjusted for the weight of the relative industry group.

Source : Central Statistical Organisation.

APPENDIX TABLE II.7 : FREQUENCY DISTRIBUTION OF GROWTH RATES OF SEVENTEEN MAJOR INDUSTRY GROUPS OF MANUFACTURING SECTOR - 1999-2000 to 2003-04

(Number of years)

Industry Group	Weight	Negative	0-5 %	5-10 %	10-15 %	15+ %	5% and above (Col. 5+6+7)
1	2	3	4	5	6	7	8
1. Food products	9.08	2	1	0	2	0	2
2. Beverages, tobaco and related products	2.38	0	1	2	1	1	4
3. Cotton textiles	5.52	3	1	1	0	0	1
4. Wool, silk and man-made fibre textiles	2.26	0	2	2	1	0	3
5. Jute and other vegetables fibre textiles (except cotton)	0.59	3	1	1	0	0	1
6. Textile products (including wearing apparel)	2.54	1	3	0	1	0	1
7. Wood and wood products, furniture and fixtures	2.70	3	1	1	0	0	1
8. Paper and paper products and printing, publishing and allied activities	2.65	1	1	2	0	1	3
9. Leather, leather & fur products	1.14	2	0	1	2	0	3
10. Chemicals and chemical products except products of petroleum and coal	14.00	0	2	3	0	0	3
11. Rubber, plastic, petroleum and coal products	5.73	1	1	1	2	0	3
12. Non-metallic mineral products	4.40	1	2	1	0	1	2
13. Basic metal and alloy industries	7.45	0	2	3	0	0	3
14. Metal products and parts (except machinery and equipment)	2.81	2	1	1	0	1	2
15. Machinery and equipment other than transport equipment	9.57	0	2	1	0	2	3
16. Transport equipment and parts	3.98	1	0	2	1	1	4
17. Other manufacturing industries	2.56	1	1	2	1	0	3

Source : Central Statistical Organisation.

APPENDIX TABLE II.8 : USE-BASED CLASSIFICATION OF INDUSTRIAL PRODUCTION (BASE : 1993-94=100)

Industry Group	Weight	Index			Growth Rate (Per cent)					
		2003-04P	2002-03	2001-02	2003-04P	2002-03	2001-02	2000-01	1999-00	1998-99
1	2	3	4	5	6	7	8	9	10	11
1. Basic Goods	35.57	168.5	159.9	152.5	5.4 (25.1)	4.9 (27.4)	2.6 (32.3)	3.7 (24.0)	5.5 (27.7)	1.6 (13.9)
2. Capital Goods	9.26	200.6	177.4	160.6	13.1 (17.6)	10.5 (16.2)	-3.4 (-11.8)	1.8 (3.5)	6.9 (10.2)	12.6 (28.1)
3. Intermediate Goods	26.51	198.9	187.1	180.1	6.3 (25.6)	3.9 (19.3)	1.5 (16.3)	4.7 (27.2)	8.8 (37.7)	6.1 (42.3)
4. Consumer Goods (a+b)	28.66	200.8	187.5	175.1	7.1 (31.2)	7.1 (37.0)	6.0 (64.5)	8.0 (45.4)	5.7 (24.4)	2.2 (15.8)
a) Consumer Durables	5.36	265.1	237.8	253.7	11.5 (12.0)	-6.3 (-8.9)	11.5 (31.8)	14.5 (20.1)	14.1 (13.7)	5.6 (8.7)
b) Consumer Non-durables	23.30	186.0	175.9	157.0	5.7 (19.3)	12.0 (45.9)	4.1 (32.8)	5.8 (25.1)	3.2 (10.6)	1.2 (6.6)
IIP - General	**100.00**	**188.8**	**176.6**	**167.0**	**6.9** **(100.0)**	**5.7** **(100.0)**	**2.7** **(100.0)**	**5.0** **(100.0)**	**6.7** **(100.0)**	**4.1** **(100.0)**

P : Provisional.

Note : Figures in parentheses are relative contributions, computed as the ratios (in percentage terms) of the change in the index of the respective industry group to the change in the overall index adjusted for the weight of the relative industry group.

Source : Central Statistical Organisation.

APPENDIX TABLE II.9 : GROWTH OF SIX INFRASTRUCTURE INDUSTRIES (BASE : 1993-94=100)

Industry	Weight	Index		Growth Rate (Per cent)				
		2003-04P	2002-03	2003-04P	2002-03	2001-02	2000-01	1999-2000
1	2	3	4	5	6	7	8	9
1. Electricity	10.17	172.5	164.3	5.1 (33.3)	3.2 (20.7)	3.1 (36.6)	3.9 (28.9)	7.2 (30.3)
2. Coal	3.22	144.1	137.1	5.1 (9.0)	4.5 (7.7)	4.2 (12.5)	3.5 (6.8)	3.1 (3.6)
3. Steel	5.13	242.9	227.2	6.9 (32.1)	10.1 (43.5)	3.6 (26.8)	6.4 (30.1)	15.0 (37.4)
4. Cement	1.99	215.3	203.0	6.1 (9.8)	8.8 (13.4)	7.4 (18.9)	-0.9 (-1.6)	14.2 (12.9)
5. Crude Petroleum	4.17	123.5	122.3	1.0 (2.0)	3.2 (6.5)	-1.2 (-4.6)	1.5 (3.7)	-2.4 (-3.6)
6. Petroleum Refinery Products	2.00	228.1	210.9	8.2 (13.7)	4.9 (8.1)	3.7 (10.6)	20.3 (32.1)	25.4 (19.4)
Composite Index of Infrastructure Industries #	**26.68**	**182.3**	**172.9**	**5.4** **(100.0)**	**5.6** **(100.0)**	**3.2** **(100.0)**	**5.1** **(100.0)**	**9.1** **(100.0)**

P : Provisional. # : Estimate based on weighted industry-wise index.

Note : Figures in parentheses are relative contributions, computed as the ratios (in percentage terms) of the change in the index of the respective industry group to the change in the overall index adjusted for the weight of the relative industry group.

Source : Office of the Economic Adviser, Ministry of Industry, Government of India.

APPENDIX TABLE II.10 : GROSS DOMESTIC SAVING AND INVESTMENT

Item	Per cent of GDP (at current market prices)				Amount in Rupees crore		
	2002-03*	2001-02@	2000-01	1996-97 to 1999-00 (Average)	2002-03*	2001-02@	2000-01
1	2	3	4	5	6	7	8
1. Household Saving	22.6	22.7	21.9	18.6	5,59,258	5,19,040	4,58,215
of which :							
a) Financial Assets	10.3	11.1	10.7	10.2	2,54,407	2,54,304	2,22,721
b) Physical Assets	12.3	11.6	11.3	8.3	3,04,851	2,64,736	2,35,494
2. Private Corporate Sector	3.4	3.5	4.1	4.2	84,169	78,849	86,142
3. Public Sector	-1.9	-2.7	-2.3	0.2	-45,730	-62,704	-48,371
4. Gross Domestic Saving	**24.2**	**23.5**	**23.7**	**23.0**	**5,97,697**	**5,35,185**	**4,95,986**
5. Net Capital Inflow	-0.9	-0.3	0.6	1.2	-22,664	-7,268	12,847
6. Gross Domestic Capital Formation	**23.3**	**23.1**	**24.4**	**24.2**	**5,75,033**	**5,27,917**	**5,08,833**
7. Errors and Omissions	0.5	0.8	1.7	1.9	11,217	18,857	36,125
8. Gross Capital Formation	**22.8**	**22.3**	**22.6**	**22.3**	**5,63,816**	**5,09,060**	**4,72,708**
of which :							
a) Public Sector	5.7	5.8	6.3	6.8	1,40,386	1,33,003	1,31,505
b) Private Corporate Sector	4.8	4.9	5.1	7.2	1,18,579	1,11,321	1,05,709
c) Household Sector	12.3	11.6	11.3	8.3	3,04,851	2,64,736	2,35,494

* : Quick Estimates.
@ : Provisional Estimates.
Source : Central Statistical Organisation.

APPENDIX TABLE II.11 : FINANCIAL SAVING OF THE HOUSEHOLD SECTOR (GROSS)

(Per cent)

Item	2003-04#	2002-03P	2001-02P	2000-01	1999-00
1	2	3	4	5	6
Financial Saving (Gross)	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**
	(15.1)	**(13.6)**	**(12.7)**	**(11.9)**	**(12.2)**
a) Currency	10.1	8.5	9.7	6.3	8.8
	(1.5)	(1.2)	(1.2)	(0.7)	(1.1)
b) Deposits	42.9	41.5	39.4	41.0	36.3
	(6.5)	(5.7)	(5.0)	(4.9)	(4.4)
i) with banks	40.5	36.3	35.3	32.5	30.8
ii) with non-banking companies	0.2	1.6	2.6	2.9	1.7
iii) with co-operative banks and societies	2.3	3.7	3.6	5.6	4.3
iv) trade debt (net)	-0.1	-0.1	-2.1	0.1	-0.4
c) Shares and debentures	1.4	1.6	2.7	4.1	7.7
	(0.2)	(0.2)	(0.3)	(0.5)	(0.9)
i) private corporate business	0.7	0.8	1.5	3.1	3.4
ii) co-operative banks and societies	0.0	0.0	0.1	0.0	0.0
iii) units of UTI	-0.4	-0.5	-0.6	-0.4	0.8
iv) bonds of PSUs	0.0	0.0	0.0	0.1	0.1
v) mutual funds (other than UTI)	1.1	1.3	1.8	1.3	3.4
d) Claims on government	17.7	18.6	17.9	15.7	12.3
	(2.7)	(2.5)	(2.3)	(1.9)	(1.5)
i) investment in government securities	4.0	4.3	5.8	1.7	0.9
ii) investment in small savings, *etc.*	13.7	14.3	12.1	14.0	11.3
e) Insurance funds	14.9	15.5	14.2	13.6	12.1
	(2.2)	(2.1)	(1.8)	(1.6)	(1.5)
i) life insurance funds	14.5	14.8	13.5	12.9	11.2
ii) postal insurance	0.1	0.2	0.3	0.2	0.3
iii) state insurance	0.3	0.5	0.4	0.5	0.6
f) Provident and pension funds	13.0	14.3	16.1	19.3	22.8
	(2.0)	(2.0)	(2.0)	(2.3)	(2.8)

: Preliminary. P : Provisional.

Note : 1. Figures in parentheses are percentages to GDP at current market prices.

2. Components may not add up to the totals due to rounding off.

APPENDIX TABLE III.1 : VARIATIONS IN RESERVE MONEY

(Amount in Rupees crore)

Item	Outstanding as on March 31, 2004	Variations							
		Financial year				April-June			
		2003-04		2002-03		2004-05		2003-04	
		Absolute	Per cent	Absolute	Per cent	Absolute	Per cent	Absolute	Per cent
1	2	3	4	5	6	7	8	9	10
Reserve Money (C.1+C.2+C.3 = S.1+S.2+S.3+S.4+S.5-S.6)	**4,36,512**	**67,451**	**18.3**	**31,091**	**9.2**	**-6,832**	**-1.6**	**16,342**	**4.4**
Components									
C.1. Currency in Circulation	3,27,028	44,555	15.8	31,499	12.6	14,297	4.4	17,882	6.3
C.2. Bankers' Deposits with the RBI	1,04,365	21,019	25.2	-801	-1.0	-19,665	-18.8	-1,606	-1.9
of which: Scheduled Commercial Banks	97,316	20,273	26.3	-1,964	-2.5	-18,927	-19.4	-1,078	-1.4
C.3. 'Other' Deposits with the RBI	5,119	1,877	57.9	393	13.8	-1,463	-28.6	65	2.0
Sources									
S.1. Net RBI Credit to Government (a+b)	44,907	-75,772	-62.8	-31,499	-20.7	-34,143	-76.0	-4,451	-3.7
a) Net RBI credit to Central Government (i-ii)	**36,920**	**-76,065**	**-67.3**	**-28,399**	**-20.1**	**-30,029**	**-81.3**	**434**	**0.4**
i) Claims on Central Government	44,307	-72,209	-62.0	-30,013	-20.5	496	1.1	-2,996	-2.6
ii) Deposits of Central Government	7,387	3,856	109.2	-1,614	-31.4	30,525	413.2	-3,430	-97.1
b) Net RBI Credit to State Governments (i-ii)	7,988	293	3.8	-3,100	-28.7	-4,114	-51.5	-4,885	-63.5
i) Claims on State Governments	7,988	293	3.8	-3,100	-28.7	-4,073	-51.0	-4,844	-62.9
ii) Deposits of State Governments	0	0	–	0	–	41	–	41	–
S.2. RBI's Claims on Commercial and Co-operative Banks	5,419	-1,741	-24.3	-3,588	-33.4	-2,813	-51.9	-1,491	-20.8
of which: Loans and Advances to Scheduled Commercial Banks	0	-102	-100.0	-2,821	-96.5	0	–	-101	-99.0
S.3. RBI's Credit to Commercial Sector	2,061	-987	-32.4	-2,880	-48.6	-172	-8.3	-73	-2.4
S.4. Net Foreign Exchange Assets of the RBI	**4,84,413**	**1,26,169**	**35.2**	**94,275**	**35.7**	**57,525**	**11.9**	**22,710**	**6.3**
S.5. Government's Currency Liabilities to the Public	7,296	225	3.2	705	11.1	17	0.2	84	1.2
S.6. Net Non-Monetary Liabilities of the RBI	1,07,585	-19,557	-15.4	25,922	25.6	27,245	25.3	437	0.3
S.7. Net Domestic Assets of the RBI (S.1+S.2+S.3+S.5-S.6)	**-47,901**	**-58,719**	**-542.8**	**-63,184**	**-85.4**	**-64,357**	**134.4**	**-6,368**	**-58.9**

– : Not applicable.

Note : Data are provisional.

APPENDIX TABLE III.2 : RESERVE BANK OF INDIA SURVEY

(Amount in Rupees crore)

Item		Outstanding as on March 31, 2004	Variations							
			Financial year				April-June			
			2003-04		2002-03		2004-05		2003-04	
			Absolute	Per cent	Absolute	Per cent	Absolute	Per cent	Absolute	Per cent
1		2	3	4	5	6	7	8	9	10
Components										
C.I	Currency in Circulation	3,27,028	44,555	15.8	31,499	12.6	14,297	4.4	17,882	6.3
C.II	Bankers' Deposits with the RBI	1,04,365	21,019	25.2	-801	-1.0	-19,665	-18.8	-1,606	-1.9
C.II.1	Scheduled Commercial Banks	97,316	20,273	26.3	-1,964	-2.5	-18,927	-19.4	-1,078	-1.4
C.III	'Other' Deposits with the RBI	5,119	1,877	57.9	393	13.8	-1,463	-28.6	65	2.0
Reserve Money (C.I+C.II+C.III = S.I + S.II + S.III - S.IV - S.V)		**4,36,512**	**67,451**	**18.3**	**31,091**	**9.2**	**-6,832**	**-1.6**	**16,342**	**4.4**
Sources										
S.I	**RBI's Domestic Credit (S.I.1+S.I.2+S.I.3)**	**52,388**	**-78,500**	**-60.0**	**-37,967**	**-22.5**	**-37,129**	**-70.9**	**-6,015**	**-4.6**
S.I.1	Net RBI Credit to the Government (S.I.1.1+S.I.1.2)	44,907	-75,772	-62.8	-31,499	-20.7	-34,143	-76.0	-4,451	-3.7
S.I.1.1	Net RBI Credit to the Central Government (S.I.1.1.1 + S.I.1.1.2 + S.I.1.1.3 + S.I.1.1.4 - S.I.1.1.5)	36,920	-76,065	-67.3	-28,399	-20.1	-30,029	-81.3	434	0.4
S.I.1.1.1	Loans and Advances to the Central Government	0	0	–	-5,176	-100.0	3,222	–	8,145	–
S.I.1.1.2	Investments in Treasury Bills	0	-3	-100.0	-15	-83.6	0	–	-3	-100.0
S.I.1.1.3	Investments in Dated Government Securities	44,217	-72,227	-62.0	-24,731	-17.5	-2,901	-6.6	-11,300	-9.7
S.I.1.1.3.1	Central Government Securities	40,750	-11,796	-22.4	15,269	41.0	-2,900	-7.1	8,700	16.6
S.I.1.1.4	Rupee Coins	90	22	31.6	-91	-57.2	175	194.8	162	237.4
S.I.1.1.5	Deposits of the Central Government	7,387	3,856	109.2	-1,614	-31.4	30,525	413.2	-3,430	-97.1
S.I.1.2	Net RBI Credit to State Governments	7,988	293	3.8	-3,100	-28.7	-4,114	-51.5	-4,885	-63.5
S.I.2	RBI's Claims on Banks	1,226	-143	-10.4	-2,880	-67.8	14	1.1	-137	-10.0
S.I.2.1	Loans and Advances to Scheduled Commercial Banks	0	-102	-100.0	-2,821	-96.5	0	–	-101	-99.0
S.I.3	RBI's Credit to Commercial Sector	6,255	-2,585	-29.2	-3,588	-28.9	-2,999	-47.9	-1,427	-16.1
S.I.3.1	Loans and Advances to Primary Dealers	0	-34	-100.0	-2,849	-98.8	0	–	-34	-100.0
S.I.3.2	Loans and Advances to NABARD	4,194	-1,598	-27.6	-708	-10.9	-2,827	-67.4	-1,354	-23.4
S.II	**Government's Currency Liabilities to the Public**	**7,296**	**225**	**3.2**	**705**	**11.1**	**17**	**0.2**	**84**	**1.2**
S.III	**Net Foreign Exchange Assets of the RBI**	**4,84,413**	**1,26,169**	**35.2**	**94,275**	**35.7**	**57,525**	**11.9**	**22,710**	**6.3**
S.III.1	Gold	18,216	1,431	8.5	1,917	12.9	-112	-0.6	491	2.9
S.III.2	Foreign Currency Assets	4,66,215	1,24,739	36.5	92,358	37.1	57,636	12.4	22,219	6.5
S.IV	**Capital Account**	**1,04,056**	**-7,588**	**-6.8**	**20,002**	**21.8**	**20,246**	**19.5**	**-1,086**	**-1.0**
S.V	**Other Items (net)**	**3,528**	**-11,969**	**-77.2**	**5,919**	**61.8**	**6,999**	**198.4**	**1,523**	**9.8**

– : Not applicable.

Note : Data are provisional.

APPENDIX TABLE III.3 : VARIATIONS IN MONEY STOCK

(Amount in Rupees crore)

Item	Outstanding as on March 31, 2004	Variations							
		2003-04		2002-03		April-June			
						2004-05		2003-04	
		Absolute	Per cent	Absolute	Per cent	Absolute	Per cent	Absolute	Per cent
1	2	3	4	5	6	7	8	9	10
Broad Money (M_3) (C.1+C.2+C.3 = S.1+S.2+S.3+S.4-S.5)	**20,03,102**	**2,85,143**	**16.6**	**2,19,605** (1,89,934)	**14.7** (12.7)	**73,913**	**3.7**	**88,939**	**5.2**
Components									
C.1. Currency with the Public	3,15,493	43,912	16.2	30,787	12.8	13,545	4.3	15,354	5.7
C.2. Aggregate Deposits with Banks (a+b)	16,82,491	2,39,355	16.6	1,88,425 (1,58,754)	15.0 (12.7)	61,831	3.7	73,519	5.1
a) Demand Deposits	2,56,039	57,282	28.8	19,558	10.9	-11,421	-4.5	11,353	5.7
b) Time Deposits	14,26,451	1,82,073	14.6	1,68,867 (1,39,196)	15.7 (12.9)	73,252	5.1	62,166	5.0
C.3. 'Other' Deposits with the RBI	5,119	1,877	57.9	393	13.8	-1,463	-28.6	65	2.0
Narrow Money (M_1)[C.1+C.2(a)+C.3]	**5,76,651**	**1,03,070**	**21.8**	**50,738**	**12.0**	**661**	**0.1**	**26,773**	**5.7**
Sources									
S.1. Net Bank Credit to Government (A+B)	7,45,499	68,976	10.2	86,958	14.7	9,349	1.3	36,894	5.5
A. Net RBI Credit to Government (a+b)	44,907	-75,772	-62.8	-31,499	-20.7	-34,143	-76.0	-4,451	-3.7
a. Net RBI Credit to Central Government	36,920	-76,065	-67.3	-28,399	-20.1	-30,029	-81.3	434	0.4
b. Net RBI Credit to State Governments	7,988	293	3.8	-3,100	-28.7	-4,114	-51.5	-4,885	-63.5
B. Other Banks' Credit to Government	7,00,591	1,44,748	26.0	1,18,457	27.1	43,492	6.2	41,345	7.4
S.2. Bank Credit to Commercial Sector (a+b)	10,17,902	1,18,922	13.2	1,39,334	18.3	40,595	4.0	11,327	1.3
a) RBI's Credit to Commercial Sector	2,061	-987	-32.4	-2,880	-48.6	-172	-8.3	-73	-2.4
b) Other Banks' Credit to Commercial Sector	10,15,841	1,19,908	13.4	1,42,214	18.9	40,767	4.0	11,400	1.3
S.3. Net Foreign Exchange Assets of Banking Sector (a+b)	5,26,586	1,32,872	33.7	82,680	26.6	57,525	10.9	23,876	6.1
a) RBI's Net Foreign Exchange Assets	4,84,413	1,26,169	35.2	94,275	35.7	57,525	11.9	22,710	6.3
b) Other Banks' Net Foreign Exchange Assets	42,173	6,702	18.9	-11,595	-24.6	0	0.0	1,166	3.3
S.4. Government's Currency Liabilities to the Public	7,296	225	3.2	705	11.1	17	0.2	84	1.2
S.5. Banking Sector's Net Non-Monetary Liabilities (a+b)	2,94,181	35,851	13.9	90,072	53.5	33,572	11.4	-16,758	-6.5
a) Net Non-Monetary Liabilities of RBI	1,07,585	-19,557	-15.4	25,922	25.6	27,245	25.3	437	0.3
b) Net Non-Monetary Liabilities of Other Banks (residual)	1,86,596	55,408	42.2	64,150	95.7	6,327	3.4	-17,195	-13.1
Memo Items : Select Monetary Ratios									
1. M_3 Multiplier	4.6								
2. Bank Reserves to Aggregate Deposits Ratio	6.9								
3. Currency to Aggregate Deposits Ratio	18.8								

Note : 1. Data are provisional.
2. Revised in line with the new accounting standards and consistent with the methodology suggested by the Working Group on Money Supply : Analytics and Methodology of Compilation (June 1998).
3. Time deposits and broad money include India Millennium Deposits (IMDs) worth Rs.25,662 crore since November 17, 2000 and the impact of redemption of Resurgent India Bonds (RIBs) of Rs. 22,693 crore since October 1, 2003.
4. Figures in parentheses exclude the impact of mergers since May 3, 2002.

APPENDIX TABLE III.4 : NEW MONETARY AGGREGATES

(Amount in Rupees crore)

Item		Outstanding as on March 31, 2004	Variations							
			Financial year				April-June			
			2003-04		2002-03		2004-05		2003-04	
			Absolute	Per cent	Absolute	Per cent	Absolute	Per cent	Absolute	Per cent
1		2	3	4	5	6	7	8	9	10
Monetary Aggregates										
M_1 (C.I+C.II.1+C.III)		5,77,304	1,03,835	21.9	48,573	11.4	-261	0.0	26,338	5.6
NM_2 (M_1+C.II.2.1)		11,89,725	1,96,310	19.8	1,22,157	14.0	29,964	2.5	51,946	5.2
NM_3 (NM_2+C.II.2.2+C.IV = S.I+S.II+S.III-S.IV-S.V)		**19,62,910**	**3,21,368**	**19.6**	**2,21,702** (1,92,031)	**15.6** (13.5)	**72,298**	**3.7**	**85,771**	**5.2**
Components										
C.I	**Currency with the Public**	**3,15,203**	**43,692**	**16.1**	**30,857**	**12.8**	**13,678**	**4.3**	**15,249**	**5.6**
C.II	**Aggregate Deposits of Residents (C.II.1+C.II.2)**	**16,17,918**	**2,63,767**	**19.5**	**1,80,842** (1,51,171)	**15.4** (12.9)	**54,691**	**3.4**	**67,931**	**5.0**
C.II.1	Demand Deposits	2,56,982	58,267	29.3	17,322	9.5	-12,475	-4.9	11,024	5.5
C.II.2	Time Deposits of Residents (C.II.2.1+C.II.2.2)	13,60,936	2,05,501	17.8	1,63,520 (1,33,849)	16.5 (13.5)	67,166	4.9	56,907	4.9
C.II.2.1	Short-term Time Deposits	6,12,421	92,475	17.8	73,584	16.5	30,225	4.9	25,608	4.9
C.II.2.1.1	Certificates of Deposits (CDs)	6,911	6,177	840.9	-1,499	-67.1	-1,472	-21.3	574	78.2
C.II.2.2	Long-term Time Deposits	7,48,515	1,13,025	17.8	89,936	16.5	36,941	4.9	31,299	4.9
C.III	**'Other' Deposits with the RBI**	**5,119**	**1,877**	**57.9**	**393**	**13.8**	**-1,463**	**-28.6**	**65**	**2.0**
C.IV	**Call/Term Funding from Financial Institutions**	**24,670**	**12,032**	**95.2**	**9,609**	**317.3**	**5,393**	**21.9**	**2,526**	**20.0**
Sources										
S.I	**Domestic Credit (S.I.1+S.I.2)**	**19,19,248**	**1,86,747**	**10.8**	**2,43,195**	**16.3**	**37,458**	**2.0**	**47,797**	**2.8**
S.I.1	Net Bank Credit to the Government (S.I.1.1+S.I.1.2)	7,45,518	68,565	10.1	87,051	14.8	6,271	0.8	36,447	5.4
S.I.1.1	Net RBI Credit to the Government	44,907	-75,772	-62.8	-31,499	-20.7	-34,143	-76.0	-4,451	-3.7
S.I.1.2	Credit to the Government by the Banking System	7,00,610	1,44,337	25.9	1,18,550	27.1	40,414	5.8	40,898	7.4
S.I.2	Bank Credit to the Commercial Sector (S.I.2.1+S.I.2.2)	11,73,730	1,18,182	11.2	1,56,143	17.4	31,187	2.7	11,350	1.1
S.I.2.1	RBI Credit to the Commercial Sector	6,255	-2,585	-29.2	-3,588	-28.9	-2,999	-47.9	-1,427	-16.1
S.I.2.2	Credit to the Commercial Sector by the Banking System	11,67,475	1,20,768	11.5	1,59,732	18.0	34,186	2.9	12,776	1.2
S.I.2.2.1	Other Investments (Non-SLR Securities)	1,46,196	2,994	2.1	14,299	11.1	-2,148	-1.5	1,253	0.9
S.II	**Government's Currency Liabilities to the Public**	**7,296**	**225**	**3.2**	**705**	**11.1**	**17**	**0.2**	**84**	**1.2**
S.III	**Net Foreign Exchange Assets of the Banking Sector (S.III.1+S.III.2)**	**4,25,882**	**1,36,270**	**47.1**	**63,774**	**28.2**	**49,718**	**11.7**	**23,945**	**8.3**
S.III.1	Net Foreign Exchange Assets of the RBI	4,84,413	1,26,169	35.2	94,275	35.7	57,525	11.9	22,710	6.3
S.III.2	Net Foreign Currency Assets of the Banking System	-58,531	10,101	-14.7	-30,501	80.0	-7,807	13.3	1,235	-1.8
S.IV	**Capital Account**	**2,31,440**	**9,855**	**4.4**	**37,259**	**20.2**	**36,445**	**15.7**	**14,845**	**6.7**
S.V	**Other Items (net)**	**1,58,075**	**-7,980**	**-4.8**	**48,713**	**41.5**	**-21,552**	**-13.6**	**-28,790**	**-17.3**

Note :1. Data are provisional.

2. Data are revised in line with the new accounting standards and consistent with the methodology suggested by the Working Group on Money Supply : Analytics and Methodology of Compilation (June 1998).
3. Time deposits and broad money include India Millennium Deposits (IMDs) aggregating Rs.25,662 crore since November 17, 2000 and the impact of redemption of the Resurgent India Bonds (RIBs) of Rs. 22,693 crore since October 1, 2003.
4. Figures in parentheses exclude the impact of mergers since May 3, 2002.

APPENDIX TABLE III.5 : LIQUIDITY AGGREGATES (OUTSTANDING AMOUNTS)

(Rupees crore)

Month	NM_3	Postal Deposits	**L_1 (2+3)**	Liabilities of Financial Institutions				**L_2 (4+8)**	Public Deposits with NBFCs	**L_3 (9+10)**
				Term Money Borrowings	CDs	Term Deposits	Total (5+6+7)			
1	2	3	**4**	5	6	7	8	**9**	10	**11**
2002-03										
April	14,50,542	44,332	**14,94,874**	3,083	602	1,701	5,386	**15,00,260**		
May	15,24,013	45,061	**15,69,074**	2,668	579	2,391	5,638	**15,74,712**		
June	15,29,150	45,868	**15,75,018**	2,470	531	2,536	5,537	**15,80,556**	19,764	**16,00,320**
July	15,36,978	46,893	**15,83,871**	2,920	460	2,628	6,008	**15,89,879**		
August	15,44,285	47,658	**15,91,943**	2,950	404	2,780	6,134	**15,98,077**		
September	15,55,029	48,453	**16,03,482**	3,139	409	3,375	6,923	**16,10,405**	18,662	**16,29,067**
October	15,73,152	49,230	**16,22,382**	2,221	403	3,374	5,998	**16,28,380**		
November	15,93,978	50,073	**16,44,051**	1,583	406	3,664	5,653	**16,49,704**		
December	16,00,871	51,105	**16,51,976**	1,594	448	3,754	5,796	**16,57,772**	19,264	**16,77,036**
January	16,12,135	51,899	**16,64,034**	1,581	449	3,758	5,788	**16,69,822**		
February	16,26,290	53,609	**16,79,899**	1,563	405	3,732	5,700	**16,85,598**		
March	16,41,542	55,275	**16,96,817**	2,128	355	3,813	6,296	**17,03,113**	19,906	**17,23,019**
2003-04										
April	16,95,927	55,841	**17,51,768**	2,228	189	3,845	6,262	**17,58,030**		
May	17,15,021	56,913	**17,71,934**	2,179	189	3,722	6,090	**17,78,024**		
June	17,27,313	58,336	**17,85,649**	2,351	374	3,898	6,623	**17,92,272**	19,954	**18,12,226**
July	17,35,700	60,026	**17,95,726**	1,752	368	4,205	6,325	**18,02,051**		
August	17,48,764	61,181	**18,09,945**	1,769	366	4,184	6,319	**18,16,264**		
September	17,61,591	62,264	**18,23,855**	1,347	363	4,320	6,030	**18,29,885**	20,368	**18,50,253**
October	18,14,946	63,648	**18,78,594**	1,269	361	4,150	5,780	**18,84,374**		
November	18,36,664	64,945	**19,01,609**	1,364	356	4,408	6,128	**19,07,737**		
December	18,49,886	66,511	**19,16,397**	1,675	449	4,388	6,512	**19,22,909**	20,301	**19,43,209**
January	18,82,565	68,122	**19,50,687**	1,792	446	4,379	6,617	**19,57,304**		
February	19,14,762	69,193	**19,83,955**	2,131	445	4,286	6,862	**19,90,817**		
March	19,62,910	71,387	**20,34,297**	1,696	560	3,989	6,245	**20,40,542**	19,722	**20,60,264**

CDs : Certificates of Deposit. L_1, L_2 and L_3 : Liquidity Aggregates. NBFCs: Non-Banking Financial Companies.

Note :
1. Data are provisional.
2. The methodology of compilation of the liquidity aggregates is available in the "New Monetary and Liquidity Aggregates", RBI Bulletin, November 2000, which also presented the Liquidity series from April 1993 onwards. The acronym NM_3 is used to distinguish the new monetary aggregate as proposed by the Working Group from the existing monetary aggregates.
3. Postal deposits comprise post office saving bank deposits, post office time deposits, post office recurring deposits, other deposits and post office cumulative time deposits.
4. Financial Institutions (FIs) comprise IDBI, IFCI, EXIM Bank, IIBI, SIDBI, NABARD, NHB, TFCI and IDFC.
5. Since July 2001, term money borrowings of FIs comprise borrowings from corporates and others.
6. Since August 2002, Term Deposits include CP and Others.
7. Estimates of public deposits are generated on the basis of returns received from all NBFCs with public deposits of Rs. 20 crore and more as recommended by the Working Group.
8. While L_1 and L_2 are compiled on a monthly basis, L_3 is compiled on a quarterly basis.

APPENDIX TABLE III.6 : IMPORTANT BANKING INDICATORS - SCHEDULED COMMERCIAL BANKS

(Amount in Rupees crore)

Item	Outstanding as on March 19, 2004	Variations							
		Financial year				April-June			
		2003-04		2002-03		2004-05 P		2003-04	
		Absolute	Per cent	Absolute	Per cent	Absolute	Per cent	Absolute	Per cent
1	2	3	4	5	6	7	8	9	10
1. Gross Demand and Time Liabilites (2+3+4+6)	**17,31,657**	**2,46,013**	**16.6**	**2,13,470**	**16.8**	**59,113**	**3.4**	**64,899**	**4.4**
2. Aggregate Deposits (a+b)	**15,04,416**	**2,23,563**	**17.5**	**1,77,493 (1,47,822)**	**16.1 (13.4)**	**55,517**	**3.7**	**63,622**	**5.0**
a. Demand deposits	2,25,022	54,733	32.1	17,241	11.3	-12,469	-5.5	11,366	6.7
b. Time deposits	12,79,394	1,68,830	15.2	1,60,252 (1,30,581)	16.9 (13.7)	67,986	5.3	52,256	4.7
3. Other Borrowings #	24,670	12,032	95.2	9,609	317.3	5,393	21.9	2,526	20.0
4. Other Demand and Time Liabilities	1,48,084	18,278	14.1	17,923	16.0	-5,045	-3.4	810	0.6
5. Borrowings from the RBI	0	-79	-100.0	-3,537	-97.8	0	–	-78	-98.7
6. Inter-bank Liabilities	54,487	-7,859	-12.6	8,444	15.7	3,249	6.0	-2,058	-3.3
7. Bank Credit (a+b)	**8,40,785**	**1,11,570**	**15.3**	**1,39,493**	**23.7**	**36,623**	**4.4**	**3,678**	**0.5**
a. Food Credit	35,961	-13,518	-27.3	-4,499	-8.3	7,100	19.7	586	1.2
b. Non-food Credit	8,04,824	1,25,088	18.4	1,43,992	26.9	29,523	3.7	3,091	0.5
8. Investments (a+b)	**6,77,588**	**1,30,042**	**23.8**	**1,09,276**	**24.9**	**39,821**	**5.9**	**35,521**	**6.5**
a. Government Securities	6,54,758	1,31,341	25.1	1,12,241	27.3	39,276	6.0	35,534	6.8
b. Other Approved Securities	22,830	-1,299	-5.4	-2,964	-10.9	545	2.4	-13	-0.1
9. Cash in hand	7,898	331	4.4	1,322	21.2	625	7.9	2,441	32.3
10. Balances with the RBI	68,997	10,662	18.3	-4,068	-6.5	9,391	13.6	17,630	30.2
11. Inter-Bank Assets	48,179	-10,840	-18.4	6,156	11.6	2,137	4.4	-7,254	-12.3
12. Credit-Deposit Ratio (per cent)	55.89	_	49.9	_	78.6		66.0	_	5.8
13. Non-food Credit-Deposit Ratio (per cent)	53.50	_	56.0	_	81.1		53.2	_	4.9
14. Investment-Deposit Ratio (per cent)	45.04	_	58.2	_	61.6		71.7	_	55.8

P : Provisional. – : Not applicable.

: Other than from the Reserve Bank/IDBI/NABARD/EXIM Bank.

Note : 1. Figures in parentheses exclude the impact of mergers since May 3, 2002.

2. Data are revised in line with the new accounting standards and consistent with the methodology suggested by the Working Group on Money Supply : Analytics and Methodology of Compilation (June 1998). The revision is in respect of pension and provident funds with commercial banks which are classified as other demand and time liabilities and includes those banks which have reported such changes so far.

APPENDIX TABLE III.7 : COMMERCIAL BANK SURVEY

(Amount in Rupees crore)

	Item	Outstanding as on March 19, 2004	Variations							
			Financial year				April-June			
			2003-04		2002-03		2004-05		2003-04	
			Absolute	Per cent	Absolute	Per cent	Absolute	Per cent	Absolute	Per cent
	1	2	3	4	5	6	7	8	9	10
Components										
C.I	**Aggregate Deposits of Residents (C.I.1+C.I.2)**	**14,29,080**	**2,40,732**	**20.3**	**1,75,838 (1,46,167)**	**17.4 (14.4)**	**54,282**	**3.8**	**65,724**	**5.5**
C.I.1	Demand Deposits	2,25,022	54,733	32.1	17,241	11.3	-12,469	-5.5	11,366	6.7
C.I.2	Time Deposits of Residents (C.I.2.1+C.I.2.2)	12,04,058	1,86,000	18.3	1,58,596 (1,28,925)	18.5 (15.0)	66,751	5.5	54,359	5.3
C.I.2.1	Short-term Time Deposits	5,41,826	83,700	18.3	71,368	18.5	30,038	5.5	24,461	5.3
C.I.2.1.1	Certificates of Deposits (CDs)	6,911	6,177	840.9	-1,499	-67.1	-1,472	-21.3	574	78.2
C.I.2.2	Long-term Time Deposits	6,62,232	1,02,300	18.3	87,228	18.5	36,713	5.5	29,897	5.3
C.II	**Call/Term Funding from Financial Institutions**	**24,670**	**12,032**	**95.2**	**9,609**	**317.3**	**5,393**	**21.9**	**2,526**	**20.0**
Sources										
S.I	**Domestic Credit (S.I.1+S.I.2)**	**16,57,237**	**2,42,782**	**17.2**	**2,67,294**	**23.3**	**73,618**	**4.4**	**45,933**	**3.2**
S.I.1	Credit to the Government	6,54,758	1,31,341	25.1	1,12,241	27.3	39,276	6.0	35,534	6.8
S.I.2	Credit to the Commercial Sector (S.I.2.1+S.I.2.2+S.I.2.3+S.I.2.4)	10,02,479	1,11,441	12.5	1,55,053	21.1	34,342	3.4	10,400	1.2
S.I.2.1	Bank Credit	8,40,785	1,11,570	15.3	1,39,493	23.7	36,623	4.4	3,678	0.5
S.I.2.1.1	Non-food Credit	8,04,824	1,25,088	18.4	1,43,992	26.9	29,523	3.7	3,091	0.5
S.I.2.2	Net Credit to Primary Dealers	1,946	-2,147	-52.5	3,765	1,148.9	-678	-34.8	5,557	135.8
S.I.2.3	Investments in Other Approved Securities	22,830	-1,299	-5.4	-2,964	-10.9	545	2.4	-13	-0.1
S.I.2.4	Other Investments (in non-SLR Securities)	1,36,918	3,317	2.5	14,759	12.4	-2,148	-1.6	1,178	0.9
S.II	**Net Foreign Currency Assets of Commercial Banks (S.II.1-S.II.2-S.II.3)**	**-58,531**	**10,101**	**-14.7**	**-30,501**	**80.0**	**-7,807**	**13.3**	**1,235**	**-1.8**
S.II.1	Foreign Currency Assets	33,833	2,752	8.9	-22,994	-42.5	-3,507	-10.4	-377	-1.2
S.II.2	Non-resident Foreign Currency Repatriable Fixed Deposits	75,336	-17,170	-18.6	1,656	1.8	1,235	1.6	-2,103	-2.3
S.II.3	Overseas Foreign Currency Borrowings	17,028	9,820	136.2	5,851	431.0	3,065	18.0	491	6.8
S.III	**Net Bank Reserves (S.III.1+S.III.2-S.III.3)**	**76,895**	**11,072**	**16.8**	**792**	**1.2**	**10,016**	**13.0**	**20,149**	**30.6**
S.III.1	Balances with the RBI	68,997	10,662	18.3	-4,068	-6.5	9,391	13.6	17,630	30.2
S.III.2	Cash in Hand	7,898	331	4.4	1,322	21.2	625	7.9	2,441	32.3
S.III.3	Loans and Advances from the RBI	0	-79	-100.0	-3,537	-97.8	0	–	-78	-98.7
S.IV	**Capital Account**	**1,03,108**	**16,568**	**19.1**	**14,221**	**19.7**	**16,199**	**15.7**	**15,349**	**17.7**
S.V.	**Other items (net) (S.I+S.II+S.III-S.IV-C.I-C.II)**	**1,18,743**	**-5,377**	**-4.3**	**37,917**	**44.0**	**-47**	**0.0**	**-16,283**	**-13.1**
S.V.1	Other Demand and Time Liabilities (net of S.II.3)	1,31,056	8,458	6.9	12,072	10.9	-8,111	-6.2	319	0.3
S.V.2	Net Inter-Bank Liabilities (other than to PDs)	8,254	834	11.2	6,054	443.2	435	5.3	10,753	144.9

Note : 1. Data are provisional.
2. Figures in parentheses exclude the impact of mergers since May 3, 2002.
3. Time deposits and broad money include India Millennium Deposits (IMDs) aggregating Rs.25,662 crore since November 17, 2000 and the impact of redemption of the Resurgent India Bonds (RIBs) of Rs. 22,693 crore since October 1, 2003.

APPENDIX TABLE III.8 : SECTORAL DEPLOYMENT OF GROSS BANK CREDIT

(Amount in Rupees crore)

Sector	Outstanding as on				Variations	
	March 19, 2004 *	March 21, 2003 *	March 21, 2003 @	March 22, 2002 @	2003-04*	2002-03@
1	2	3	4	5	6	7
I. Gross Bank Credit (1+2)	**7,64,383**	**6,69,534**	**6,16,906**	**5,36,727**	**94,849**	**80,179**
1. Public Food Procurement Credit	35,961	49,479	49,479	53,978	-13,518	-4,499
2. Non-food Gross Bank Credit	7,28,422	6,20,055	5,67,427	4,82,749	1,08,367 (100)	84,678 (100)
A. Priority Sectors #	2,63,834	2,11,609	2,03,799	1,75,259	52,225 (48.2)	28,540 (33.7)
i) Agriculture	90,541	73,518	71,609	60,761	17,023 (15.7)	10,848 (12.8)
ii) Small Scale Industries	65,855	60,394	60,486	57,199	5,461 (5.0)	3,287 (3.9)
iii) Other Priority Sectors	1,07,438	77,697	71,704	57,299	29,741 (27.4)	14,405 (17.0)
B. Industry (Medium and Large)	2,47,210	2,35,168	2,00,335	1,72,324	12,042 (11.1)	28,011 (33.1)
C. Wholesale Trade (other than food procurement)	24,867	22,578	22,398	20,459	2,289 (2.1)	1,939 (2.3)
D. Other Sectors	1,92,511	1,50,700	1,40,895	1,14,707	41,811 (38.6)	26,188 (30.9)
of which :						
i) Housing	51,981	36,587	34,654	22,346	15,394	12,308
ii) Consumer Durables	8,274	7,219	6,904	7,015	1,055	-111
iii) Non-Banking Financial Companies	16,802	14,127	14,052	9,653	2,675	4,399
iv) Loans to Individuals against Shares and Debentures/Bonds	2,020	2,001	1,762	1,520	19	242
v) Real Estate Loans	5,577	5,894	3,098	2,596	-317	502
vi) Other Non-Priority Sector Personal Loans	35,165	27,905	26,089	23,402	7,260	2,687
vii) Advances against Fixed Deposits	26,346	22,708	22,701	21,243	3,638	1,458
viii) Tourism and Tourism Related Hotels	3,269	2,428	1,806	1,540	841	266
II. Export Credit [included under item I(2)]	**57,687**	**49,202**	**49,402**	**42,978**	**8,485 (7.8)**	**6,424 (7.6)**
III. Net Bank Credit (including inter-bank participations)	**7,63,855**	**6,68,576**	**6,16,085**	**5,35,063**	**95,279**	**81,022**

\# : Data in this statement may not match with those stated elsewhere in the Report due to differences in the data source.

* : Including the impact of mergers since May 3, 2002.

@ : Excluding the impact of mergers since May 3, 2002.

Note :
1. Data are provisional and relate to select scheduled commercial banks which account for about 90 per cent of bank credit of all scheduled commercial banks.
2. Gross bank credit data include bills rediscounted with the Reserve Bank, IDBI, EXIM Bank, other approved financial institutions and inter-bank participations.
3. Net bank credit data are exclusive of bills rediscounted with the Reserve Bank, IDBI, EXIM Bank and other approved financial institutions.
4. Figures in parentheses are proportions to incremental non-food gross bank credit.

APPENDIX TABLE III.9 : INDUSTRY-WISE DEPLOYMENT OF GROSS BANK CREDIT

(Amount in Rupees crore)

Industry	Outstanding as on				Variations	
	March 19, 2004 *	March 21, 2003 *	March 21, 2003 @	March 22, 2002 @	2003-04*	2002-03@
1	2	3	4	5	6	7
Industry (Small, Medium and Large)	**3,13,065**	**2,95,562**	**2,60,821**	**2,29,523**	**17,503**	**31,298**
1 . Coal	1,165	1,334	1,325	1,409	-169	-84
2 . Mining	1,635	1,769	1,776	1,593	-134	183
3 . Iron and Steel	26,295	28,065	21,425	20,042	-1,770	1,383
4 . Other Metals and Metal Products	8,168	8,556	7,513	6,496	-388	1,017
5 . All Engineering	26,348	26,272	23,414	24,199	76	-785
of which: Electronics	8,421	7,831	6,237	5,941	590	296
6 . Electricity	14,090	11,173	11,300	9,343	2,917	1,957
7 . Cotton Textiles	17,166	15,762	13,863	11,744	1,404	2,119
8 . Jute Textiles	1,051	860	786	737	191	49
9 . Other Textiles	15,941	15,075	14,058	13,455	866	603
10. Sugar	6,363	5,726	5,024	5,028	637	-4
11. Tea	1,222	1,052	1,053	986	170	67
12. Food Processing	9,872	8,577	8,360	7,285	1,295	1,075
13. Vegetable Oils (including *vanaspati*)	3,219	2,919	2,853	2,729	300	124
14. Tobacco and Tobacco Products	891	756	756	861	135	-105
15. Paper and Paper Products	5,990	5,049	4,326	3,741	941	585
16. Rubber and Rubber Products	2,593	2,662	2,498	2,246	-69	252
17. Chemicals, Dyes, Paints, *etc.*	30,629	31,805	27,831	25,988	-1,176	1,843
of which:						
i) Fertilisers	6,249	6,923	6,293	5,463	-674	830
ii) Petro-Chemicals	7,221	7,735	7,007	6,663	-514	344
iii) Drugs and Pharmaceuticals	8,667	7,892	7,492	6,393	775	1,099
18. Cement	5,689	6,431	5,180	4,224	-742	956
19. Leather and Leather Products	3,167	2,940	2,927	2,852	227	75
20. Gems and Jewellery	9,178	7,533	7,542	6,456	1,645	1,086
21. Construction	5,978	4,891	4,551	4,000	1,087	551
22. Petroleum	12,266	14,743	12,021	11,320	-2,477	701
23. Automobiles including Trucks	5,302	5,629	4,707	4,454	-327	253
24. Computer Software	3,029	2,611	2,531	1,665	418	866
25. Infrastructure	37,224	26,297	20,033	14,809	10,927	5,224
i) Power	19,655	15,042	10,752	7,373	4,613	3,379
ii) Telecommunications	8,408	5,779	4,110	3,972	2,629	138
iii) Roads and Ports	9,161	5,476	5,171	3,464	3,685	1,707
26. Other Industries	58,594	57,075	53,168	41,861	1,519	11,307

* : Including the impact of mergers since May 3, 2002.

@ : Excluding the impact of mergers since May 3, 2002.

Note : Data are provisional and relate to select scheduled commercial banks which account for about 90 per cent of bank credit of all scheduled commercial banks.

APPENDIX TABLE III.10 : RESERVE BANK'S ACCOMMODATION TO SCHEDULED COMMERCIAL BANKS

(Amount in Rupees crore)

Item	2004-05	2003-04				2002-03
	June +	March	December	September	June	March
1	2	3	4	5	6	7
1. Export Credit Refinance						
A) Limit	4,519	4,664	4,707	4,632	4,866	5,048
a) Normal	–	1,553	2,354	2,316	2,433	2,524
b) Backstop	–	3,111	2,354	2,316	2,433	2,524
B) Outstanding	–	0	1	2	3	85
a) Normal	–	0	1	2	3	62
b) Backstop	–	0	0	0	0	23
Memo Items :						
1. Aggregate Export Credit *	62,898	59,744	56,710	52,339	51,443	50,248
2. Export Credit eligible for Refinance	30,178	31,101	31,402	30,883	32,440	33,655
3. Aggregate Export Credit as percentage of Net Bank Credit	7.2	7.1	7.2	7.0	6.9	6.8

+ : As on June 11, 2004.

* : Inclusive of Rupee export credit, pre-shipment credit in foreign currency (PCFC), rediscounting of export bills abroad (EBR) and overdue export credit.

Note : 1. Data pertain to the last reporting Friday of the month.

2. Effective April 1, 2002, ECR facility is being provided to banks to the extent of 15 per cent of the outstanding export credit eligible for refinance as at the end of second preceding fortnight. Apportionment of normal and back-stop under the ECR facility which was changed from the initial ratio of two-third to one-third (i.e., 67:33) to one half (50:50) each effective November 16, 2002 was further changed to one-third to two-third (33:67) from December 27, 2003. Effective March 29, 2004, normal and backstop facilities were merged into a single facility.

APPENDIX TABLE III.11 : VARIATIONS IN INDEX NUMBERS OF WHOLESALE PRICES (BASE : 1993-94 = 100)

(Per cent)

Major Group/Sub-group/Commodity	Weight	Variations				End-June	
		Point-to-point basis		Average basis		Point-to-point basis	
		2003-04	2002-03	2003-04	2002-03	2004-05 P	2003-04
1	2	3	4	5	6	7	8
All Commodities	**100.000**	**4.6**	**6.5**	**5.4**	**3.4**	**6.1**	**5.3**
I. Primary Articles	**22.025**	**1.6**	**6.1**	**4.3**	**3.4**	**0.1**	**7.7**
1. Food articles	15.402	0.2	0.8	1.2	1.7	-1.5	4.3
a) Cereals	4.406	-0.3	4.0	1.6	2.0	-1.9	4.5
i) Rice	2.449	-2.0	4.1	1.7	-0.6	-2.7	4.1
ii) Wheat	1.384	6.1	0.1	3.2	0.2	1.5	3.1
b) Pulses	0.603	-2.6	0.3	-2.2	-4.5	-3.6	-2.2
c) Fruits and vegetables	2.917	-4.9	-1.2	2.6	0.7	-11.2	12.0
d) Milk	4.367	8.4	0.6	2.5	3.4	6.7	1.8
e) Eggs, fish and meat	2.208	-6.5	-4.0	-3.6	1.5	0.5	-1.1
f) Condiments and spices	0.662	0.2	7.4	5.6	3.1	-6.4	8.1
g) Other food articles	0.239	-5.9	17.9	-4.2	-2.7	12.7	-3.4
i) Tea	0.157	-2.5	14.2	-8.0	0.5	18.8	-10.4
ii) Coffee	0.082	-12.5	25.9	5.0	-9.7	-0.7	16.6
2. Non-food articles	6.138	4.1	22.1	12.4	8.3	2.7	18.0
a) Fibres	1.523	12.3	26.5	23.3	-4.7	4.0	26.3
i) Raw cotton	1.357	12.3	34.3	26.8	-4.2	3.8	31.2
b) Oilseeds	2.666	-1.2	30.0	10.8	16.3	-1.6	20.9
3. Minerals	0.485	25.3	-1.3	2.1	-0.4	23.9	0.0
II. Fuel, Power, Light and Lubricants	**14.226**	**2.5**	**10.8**	**6.3**	**5.6**	**11.8**	**4.8**
1. Coking coal	0.241	8.8	0.0	6.6	0.0	34.3	0.0
2. Mineral oils	6.990	0.0	18.4	7.5	6.4	15.8	4.3
3. Electricity	5.484	4.9	3.4	4.5	5.8	2.8	6.6
III. Manufactured Products	**63.749**	**6.7**	**5.1**	**5.6**	**2.8**	**6.6**	**4.6**
1. Sugar, *Khandsari and Gur*	3.929	14.5	-10.5	3.5	-7.9	18.8	-5.3
i) Sugar	3.619	16.9	-15.0	0.7	-8.8	21.0	-9.1
ii) *Khandsari*	0.173	14.0	-11.9	-2.2	-8.3	26.1	-9.7
iii) *Gur*	0.060	15.5	-9.5	-5.0	-6.9	45.1	-14.9
2. Edible oils	2.755	6.6	27.4	14.3	22.3	-0.3	16.9
3. Cotton textiles	4.215	15.6	8.3	12.1	-1.1	9.3	8.2
4. Chemicals and chemical products	11.931	0.1	4.2	1.9	2.9	1.5	2.0
5. Cement	1.731	1.3	1.1	1.2	-2.2	3.9	1.8
6. Iron and steel	3.637	34.6	9.2	26.2	5.1	43.8	18.8
7. Machinery and tools	8.363	3.1	0.5	1.8	0.9	1.9	1.2
8. Transport equipments and parts	4.295	1.4	-0.9	-0.1	0.5	2.6	-1.7

P : Provisional.

APPENDIX TABLE III.12 : VARIATIONS IN WHOLESALE PRICES - WEIGHTED CONTRIBUTIONS (BASE : 1993-94 = 100)

(Per cent)

Major Group/Sub-group/Commodity	Weight	Point-to-point basis		Average basis		End-June Point-to-point basis	
		2003-04	2002-03	2003-04	2002-03	2004-05 P	2003-04
1	2	3	4	5	6	7	8
All Commodities	**100.000**	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**
I. Primary Articles	**22.025**	**8.0**	**21.6**	**18.1**	**22.8**	**0.2**	**33.3**
1. Food articles	15.402	0.6	2.2	3.6	8.4	-4.1	13.7
a) Cereals	4.406	-0.3	2.9	1.4	2.7	-1.4	3.9
i) Rice	2.449	-1.0	1.6	0.8	-0.4	-1.1	1.9
ii) Wheat	1.384	1.9	0.0	0.9	0.1	0.4	0.8
b) Pulses	0.603	-0.3	0.0	-0.3	-0.9	-0.4	-0.3
c) Fruits and vegetables	2.917	-3.3	-0.6	1.6	0.7	-7.0	8.0
d) Milk	4.367	7.9	0.5	2.1	4.4	4.8	1.5
e) Eggs, fish and meat	2.208	-3.4	-1.7	-1.7	1.2	0.2	-0.6
f) Condiments and spices	0.662	0.0	0.9	0.8	0.7	-0.8	1.2
g) Other food articles	0.239	-0.2	0.4	-0.1	-0.1	0.3	-0.1
i) Tea	0.157	-0.1	0.2	-0.2	0.0	0.3	-0.2
ii) Coffee	0.082	-0.1	0.2	0.0	-0.1	0.0	0.1
2. Non-food articles	6.138	5.8	19.3	14.0	14.2	3.0	19.8
a) Fibres	1.523	3.8	4.9	5.7	-2.0	1.0	6.3
i) Raw cotton	1.357	3.4	5.4	5.8	-1.5	0.9	6.5
b) Oilseeds	2.666	-0.7	10.6	5.2	10.9	-0.7	9.6
3. Minerals	0.485	1.8	-0.1	0.1	0.0	1.3	0.0
II. Fuel, Power, Light and Lubricants	**14.226**	**11.6**	**33.9**	**23.7**	**32.6**	**39.1**	**18.1**
1. Coking coal	0.241	0.5	0.0	0.3	0.0	1.4	0.0
2. Mineral oils	6.990	-0.1	29.7	14.9	19.6	27.4	8.6
3. Electricity	5.484	8.1	4.2	6.6	13.1	3.6	9.5
III. Manufactured Products	**63.749**	**80.5**	**44.3**	**58.8**	**46.4**	**60.7**	**48.5**
1. Sugar, *Khandsari and Gur*	3.929	9.2	-5.7	2.1	-8.2	9.2	-3.3
i) Sugar	3.619	8.7	-7.0	0.4	-7.8	8.4	-4.8
ii) *Khandsari*	0.173	0.4	-0.3	-0.1	-0.4	0.5	-0.3
iii) *Gur*	0.060	0.1	-0.1	0.0	-0.1	0.3	-0.1
2. Edible oils	2.755	3.4	8.5	6.0	12.6	-0.1	7.1
3. Cotton textiles	4.215	12.8	4.8	8.4	-1.2	5.9	5.8
4. Chemicals and chemical products	11.931	0.3	8.2	4.4	10.6	2.9	4.7
5. Cement	1.731	0.4	0.3	0.3	-1.0	0.9	0.5
6. Iron and steel	3.637	23.6	4.4	15.2	4.6	24.6	10.7
7. Machinery and tools	8.363	4.3	0.5	2.2	1.8	2.0	1.5
8. Transport equipments and parts	4.295	1.1	-0.6	0.0	0.5	1.5	-1.3

P : Provisional.

APPENDIX TABLE III.13 : ANNUALISED VARIATIONS IN PRICE INDICES
(Point-to-Point Basis)

(Per cent)

Year/ Month	Wholesale Price Index@	CPI for Industrial Workers #	CPI for Urban Non-manual Employees+	CPI for Agricultural Labourers*
1	2	3	4	5
1998-99	5.3	8.9	9.0	8.8
	(5.9)	(13.1)	(11.3)	(11.0)
1999-00	6.5	4.8	5.0	3.4
	(3.3)	(3.4)	(4.5)	(4.4)
2000-01	4.9	2.5	5.6	-2.0
	(7.2)	(3.8)	(5.6)	(-0.3)
2001-02	1.6	5.2	4.8	3.0
	(3.6)	(4.3)	(5.1)	(1.1)
2002-03	6.5	4.1	3.8	4.9
	(3.4)	(4.0)	(3.8)	(3.2)
2003-04	4.6	3.5	3.4	2.5
	(5.4)	(3.9)	(3.7)	(3.9)
2002-03				
April	1.8	4.7	4.5	2.7
May	1.4	4.7	4.2	2.6
June	2.7	4.2	4.1	2.6
July	3.0	3.9	3.8	2.3
August	3.5	3.9	3.6	2.2
September	3.3	4.3	4.1	3.2
October	3.1	4.1	3.8	2.9
November	3.4	3.6	3.3	3.2
December	3.5	3.2	2.8	2.9
January	4.8	3.4	3.3	3.9
February	5.5	3.9	4.1	4.5
March	6.5	4.1	3.8	4.9
2003-04				
April	6.7	5.1	4.3	5.5
May	5.7	4.7	4.3	5.1
June	5.3	4.4	3.7	5.1
July	4.3	4.2	3.7	4.7
August	3.9	3.1	3.2	3.8
September	5.4	2.9	2.9	3.4
October	5.1	3.3	3.7	3.4
November	5.5	3.1	3.4	3.1
December	5.9	3.7	4.0	3.4
January	5.9	4.3	4.4	3.8
February	5.2	4.1	3.9	3.1
March	4.6	3.5	3.4	2.5
2004-05				
April	4.3	2.2	2.9	1.5
May	5.6	2.8	2.9	1.8
June	6.1 P	3.0	3.4	1.8

P : Provisional. @ : Base : 1993-94=100. # : Base : 1982=100.
+ : Base : 1984-85=100. * : Base : 1986-87=100. CPI : Consumer Price Index.

Note : Figures in parentheses are on an average basis.

APPENDIX TABLE IV.1 : MEASURES OF DEFICIT OF THE CENTRAL GOVERNMENT

(Rupees crore)

Year	Fiscal Deficit		Primary Deficit		Variation in Net RBI Credit to the centre+	Revenue Deficit
	Gross	Net	Gross	Net		
1	2	3	4	5	6	7
1995-96	60,243 (50,253)	42,432	10,198 (208)	10,806	19,855	29,731
2000-01	1,18,816	1,07,854	19,502	41,351	6,705	85,234
2001-02	1,40,955	1,23,074	33,495	51,152	-5,150	1,00,162
2002-03	1,45,072	1,33,830	27,268	53,628	-28,399	1,07,880
2003-04 (RE)	1,32,103	1,21,633	7,548	33,077	-76,065	99,860
2004-05 (BE)	1,37,407	1,23,889	7,907	31,339	n.a.	76,171
As Percentage to GDP at Current Market Prices						
1995-96	5.07 (4.23)	3.57	0.86 (0.02)	0.91	1.67	2.50
2000-01	5.69	5.16	0.93	1.98	0.32	4.08
2001-02	6.18	5.39	1.47	2.24	-0.23	4.39
2002-03	5.90 #	5.42	1.10 #	2.17	-1.15	4.40 #
2003-04 (RE)	4.80 #	4.39	0.30 #	1.19	-2.74	3.60 #
2004-05 (BE)	4.40 #	3.97 @	0.30 #	1.00 @	n.a.	2.50 #
Average 1993-94 to 2002-03	5.26 *	4.56	0.77 *	1.71	0.22	3.50

RE : Revised Estimates. BE : Budget Estimates. n.a. : Not available.
(-) : Indicates Surplus.
+ : As per RBI records after closure of Government accounts.
# : As per Budget at a Glance for 2004-05.
@ : Worked out on the basis of implicit nominal GDP underlying the Budget Estimates of GFD/GDP ratio of 4.4 per cent for 2004-05.
* : Net of States' share in small savings.

Note : 1. The revenue deficit denotes the difference between revenue receipts and revenue expenditure. The net RBI credit to the Central Government is the sum of the RBI's holdings of i) Treasury Bills, ii) Government of India dated securities, iii) rupee coins, and iv) loans and advances from the Reserve Bank to the Centre since April 1, 1997 adjusted for Centre's cash balances with the Reserve Bank. The gross fiscal deficit is the excess of total expenditure including loans net of recoveries over revenue receipts (including external grants) and non-debt capital receipts. The net fiscal deficit is the difference between gross fiscal deficit and net lending. The gross primary deficit is the difference btetween the gross fiscal deficit and interest payments. The net primary deficit denotes net fiscal deficit *minus* net interest payments.

2. Figures in parentheses exclude States' share in small savings as per the new system of accounting followed since 1999-2000.

Source : Central Government's Budget Documents and the Reserve Bank records.

APPENDIX TABLE IV.2 : MAJOR ITEMS OF RECEIPTS AND EXPENDITURES OF THE CENTRAL GOVERNMENT

Item	2004-05 (BE)	2003-04 (RE)	2003-04 (BE)	2002-03	2001-02	2000-01	1995-96	Average (1993-94 to 2002-03)
1	2	3	4	5	6	7	8	9
1. Total Receipts (2+5)	4,77,829	4,74,255	4,38,795	4,14,162	3,63,806	3,26,789	1,68,468	
	(15.30)	(17.11)	(15.99)	(16.77)	(15.94)	(15.64)	(14.18)	(15.40)
2. Revenue Receipts (3+4)	3,09,322	2,63,027	2,53,935	2,31,748	2,01,306	1,92,605	1,10,130	
	(9.91)	(9.49)	(9.26)	(9.38)	(8.82)	(9.22)	(9.27)	(9.05)
3. Tax Revenue (Net to Centre)	2,33,906	1,87,539	1,84,169	1,59,425	1,33,532	1,36,658	81,939	
	(7.49)	(6.77)	(6.71)	(6.46)	(5.85)	(6.54)	(6.90)	(6.44)
4. Non-tax Revenue	75,416	75,488	69,766	72,323	67,774	55,947	28,191	
	(2.41)	(2.72)	(2.54)	(2.93)	(2.97)	(2.68)	(2.37)	(2.61)
of which :								
i) Interest Receipts	36,950	35,999	39,160	37,602	35,538	32,811	18,419	
	(1.18)	(1.30)	(1.43)	(1.52)	(1.56)	(1.57)	(1.55)	(1.63)
ii) Dividend and Profits	18,875	22,081	17,861	21,230	17,289	13,575	3,248	
	(0.60)	(0.80)	(0.65)	(0.86)	(0.76)	(0.64)	(0.27)	(0.46)
5. Capital Receipts	1,68,507	2,11,228	1,84,860	1,82,414	1,62,500	1,34,184	58,338	
	(5.40)	(7.62)	(6.74)	(7.39)	(7.12)	(6.42)	(4.91)	(6.35)
6. Total Expenditure (7 + 8)	4,77,829	4,74,255	4,38,795	4,14,162	3,62,310	3,25,592	1,78,275	
	(15.30)	(17.11)	(15.99)	(16.77)	(15.88)	(15.58)	(15.01)	(15.70)
7. Revenue Expenditure	3,85,493	3,62,887	3,66,227	3,39,628	3,01,468	2,77,839	139,861	
	(12.34)	(13.09)	(13.35)	(13.75)	(13.21)	(13.30)	(11.77)	(12.54)
of which :								
i) Interest Payments	1,29,500	1,24,555	1,23,223	1,17,804	1,07,460	99,314	50,045	
	(4.15)	(4.49)	(4.49)	(4.77)	(4.71)	(4.75)	(4.21)	(4.49)
ii) Subsidies	43,516	44,709	49,907	43,515	31,210	26,838	12,666	
	(1.39)	(1.61)	(1.82)	(1.76)	(1.37)	(1.28)	(1.07)	(1.30)
iii) Defence	43,517	43,394	44,347	40,709	38,059	37,238	18,841	
	(1.39)	(1.57)	(1.62)	(1.65)	(1.67)	(1.78)	(1.59)	(1.68)
8. Capital Disbursements	92,336	1,11,368	72,568	74,535	60,842	47,753	38,414	
	(2.96)	(4.02)	(2.65)	(3.02)	(2.67)	(2.29)	(3.23)	(3.15)
of which :								
Capital Outlay	60,718	36,273	42,283	29,101	26,558	24,745	14,099	
	(1.94)	(1.31)	(1.54)	(1.18)	(1.16)	(1.18)	(1.19)	(1.22)
9 Developmental Expenditure*	2,14,108	1,97,025	1,96,915	1,84,197	1,59,364	1,39,386	84,427	
	(6.86)	(7.11)	(7.18)	(7.46)	(6.98)	(6.67)	(7.11)	(7.36)
of which :								
Social Sector	59,811	61,428	60,019	58,606	44,538	34,467	18,701	
	(1.92)	(2.22)	(2.19)	(2.37)	(1.94)	(1.64)	(1.57)	(1.68)
10 Non-Developmental Expenditure*	2,78,212	2,91,196	2,55,485	2,42,749	2,15,456	1,97,470	98,632	
	(8.91)	(10.50)	(9.31)	(9.83)	(9.44)	(9.45)	(8.30)	(8.81)
Memo Items:								
1. Interest Payments as per cent of Revenue Receipts	41.87	47.35	48.53	50.83	53.38	51.56	45.44	49.62
2. Revenue Deficit as per cent of Gross Fiscal Deficit	55.43	75.59	73.09	74.36	71.06	71.74	49.35	59.94
3. Net RBI Credit to Centre as per cent of Gross Fiscal Deficit	n.a.	-57.58	n.a.	-19.58	-3.65	5.64	32.96	4.20

BE : Budget Estimates. RE : Revised Estimates. n.a. : Not available.

* : Data on developmental and non-developmental expenditures are inclusive of commercial departments.

Note : Figures in parentheses are percentages to GDP.

Source: Central Government Budget Documents and the Reserve Bank records.

APPENDIX TABLE IV.3 : DIRECT AND INDIRECT TAX REVENUES OF THE CENTRAL AND THE STATE GOVERNMENTS

(Rupees crore)

Year		Centre (Gross)			States@			Centre and States Combined		
		Direct	Indirect	Total	Direct	Indirect	Total	Direct	Indirect	Total
1		2	3	4	5	6	7	8	9	10
1995-96		33,563	77,661	1,11,224	8,040	55,587	63,627	41,603	1,33,248	1,74,851
	(a)	30.2	69.8	100.0	12.6	87.4	100.0	23.8	76.2	100.0
	(b)	2.8	6.5	9.4	0.7	4.7	5.4	3.5	11.2	14.7
2000-01		68,305	1,20,299	1,88,604	12,204	1,04,823	1,17,027	80,509	2,25,122	3,05,631
	(a)	36.2	63.8	100.0	10.4	89.6	100.0	26.3	73.7	100.0
	(b)	3.2	5.7	9.0	0.6	5.0	5.6	3.9	10.8	14.6
2001-02		69,197	1,17,863	1,87,060	14,269	1,13,164	1,27,433	83,466	2,31,027	3,14,493
	(a)	37.0	63.0	100.0	11.2	88.8	100.0	26.5	73.5	100.0
	(b)	3.0	5.2	8.2	0.6	5.0	5.6	3.7	10.1	13.8
2002-03 *		83,080	1,33,186	2,16,266	17,987	1,24,355	1,42,342	1,01,067	2,57,541	3,58,608
	(a)	38.4	61.6	100.0	12.6	87.4	100.0	28.2	71.8	100.0
	(b)	3.4	5.4	8.8	0.7	5.0	5.8	4.1	10.4	14.5
2003-04*		95,714	1,55,813	2,51,527	20,749	1,44,380	1,65,129	1,16,463	3,00,193	4,16,656
BE	(a)	38.1	61.9	100.0	12.6	87.4	100.0	28.0	72.0	100.0
	(b)	3.5	5.7	9.2	0.8	5.3	6.0	4.2	10.9	15.2
2003-04*		1,03,400	1,51,523	2,54,923	18,570	1,43,390	1,61,960	1,21,970	2,94,913	4,16,883
RE	(a)	40.6	59.4	100.0	11.5	88.5	100.0	29.3	70.7	100.0
	(b)	3.7	5.5	9.2	0.7	5.2	5.8	4.4	10.6	15.0
2004-05*		1,39,510	1,78,223	3,17,733	17,944	1,60,154	1,78,098	1,57,454	3,38,377	4,95,831
BE	(a)	43.9	56.1	100.0	10.1	89.9	100.0	31.8	68.2	100.0
	(b)	4.5	5.7	10.2	0.6	5.1	5.7	5.0	10.8	15.9
Memo Items :										
(Average)										
1993-94 to	(a)	32.9	67.1	100.0	11.4	88.6	100.0	24.7	75.3	100.0
2002-03	(b)	2.9	6.0	8.9	0.6	4.8	5.4	3.5	10.8	14.3

RE : Revised Estimates. BE : Budget Estimates.

@ : Excluding States' share in Central Taxes as reported in Central Government Budget Documents.

* : Data relating to State Governments are provisional (see Notes to Appendix Table IV.5 for details).

(a) : Represents percentages to total tax revenue.

(b) : Represents percentages to GDP.

Source : Budget Documents of the Central and the State Governments.

APPENDIX TABLE IV.4 : FINANCING OF GROSS FISCAL DEFICIT OF THE CENTRAL GOVERNMENT

(Rupees crore)

Year	Internal Finance				External Finance	Total Finance/ Gross Fiscal Deficit (5+6)
	Market Borrowings #	Other Liabilities @	91-day Treasury Bills /drawdown of cash balances +	Total (2+3+4)		
1	2	3	4	5	6	7
1990-91	8,001	22,103	11,347	41,451	3,181	44,632
	(17.9)	(49.5)	(25.4)	(92.9)	(7.1)	(100.0)
1995-96	34,001	16,117	9,807	59,925	318	60,243
	(56.4)	(26.8)	(16.3)	(99.5)	(0.5)	(100.0)
2000-2001	73,431	39,077	-1,197	1,11,311	7,505	1,18,816
	(61.8)	(32.9)	(-1.0)	(93.7)	(6.3)	(100.0)
2001-2002	90,812	46,038	-1,496	1,35,354	5,601	1,40,955
	(64.4)	(32.7)	(-1.1)	(96.0)	(4.0)	(100.0)
2002-2003	1,04,126	50,997	1,883	1,57,006	-11,934	1,45,072
	(71.8)	(35.2)	(1.3)	(108.2)	(-8.2)	(100.0)
2003-04 (BE)	1,07,194	42,861	–	1,50,055	3,582	1,53,637
	(69.8)	(27.9)	–	(97.7)	(2.3)	(100.0)
2003-04 (RE)	85,671	68,369	-10,232	1,43,808	-11,705	1,32,103
	(64.9)	(51.8)	(-7.7)	(108.9)	(-8.9)	(100.0)
2004-05 (BE)	90,365 *	25,369	13,597	1,29,331	8,076	1,37,407
	(65.8)	(18.5)	(9.9)	(94.1)	(5.9)	(100.0)

RE : Revised Estimates. BE : Budget Estimates. – : Nil / Negligible.

: Including dated securities and 364-day Treasury Bills; also includes Zero Coupon Bonds and Loans in conversion of maturing Treasury Bills.

@ : Other liabilities comprise small savings, state provident funds, special deposits, reserve funds, Treasury Bills other than 364-day Treasury Bill, *etc.* For the years 1999-00 to 2001-02, small savings and public provident funds are represented by NSSF's investment in the Central government special securities and hence form part of Centre's public debt. Reinvestment of debt-swap proceeds by the NSSF in Central Government special securities is included in 2003-04.

+ : Variations in 91-day Treasury Bills issued net of changes in cash balances with the Reserve Bank up to March 31, 1997. Since April 1, 1997, these figures represent drawdown of cash balances.

* : Exclusive of amount to be raised under the Market Stabilisation Scheme.

Note : 1. Figures in parentheses represent percentages to total finance (gross fiscal deficit).
2. Since 1999-00, gross fiscal deficit excludes the States' share in small savings.

Source : Central Government Budget Documents and the Reserve Bank records.

APPENDIX TABLE IV.5 : BUDGETARY OPERATIONS OF THE STATE GOVERNMENTS

A : Measures of Deficit of State Governments

(Rupees crore)

Year	Fiscal Deficit		Primary Deficit		Net RBI Credit*	Conventional Deficit	Revenue Deficit
	Gross	Net	Gross	Net			
1	2	3	4	5	6	7	8
1990-91	18,787	14,532	10,132	8,280	420	-72	5,309
1995-96	31,426	26,695	9,494	10,556	16	-2,849	8,201
2002-03 P	1,02,058	91,382	32,092	30,904	-3100	-4,369	55,173
2003-04 (RE) P	1,40,407	1,32,991	56,682	59,479	293	12,321	72,240
2004-05 (BE) P	1,12,251	1,04,888	20,604	26,213	n.a.	529	48,259
As Percentage to GDP at Current Market Prices (Base : 1993-94)							
1990-91	3.3	2.6	1.8	1.5	0.1	–	0.9
1995-96	2.6	2.2	0.8	0.9	–	-0.2	0.7
2002-03 P	4.1	3.7	1.3	1.3	-0.1	-0.2	2.2
2003-04 (RE) P	5.1	4.8	2.0	2.1	–	0.4	2.6
2004-05 (BE) P	3.6	3.4	0.7	0.8	n.a.	–	1.5

B : Select Budgetary Variables of State Governments

	Item	2004-05 P (BE)	2003-04 P (RE)	2002-03 P	1990-00 (Average)
	1	2	3	4	5
1.	GFD / Total Expenditure (excluding recoveries)	23.4	30.0	26.9	21.4
2.	Revenue Deficit / Revenue Expenditure	11.6	18.1	16.6	9.3
3.	Conventional Deficit / Aggregate Disbursements	0.1	2.2	-1.0	-0.1
4.	Revenue Deficit / GFD	43.0	51.5	54.1	34.8
5.	Non-Developmental Revenue Expenditure / Revenue Receipts	53.0	52.9	53.0	39.6
6.	Interest Payments/Revenue Receipts	24.9	25.6	25.2	16.5
7.	Developmental Expenditure / GDP	9.0	10.8	9.2	10.2
	of which :				
	Social Sector Expenditure / GDP	5.3	5.9	5.5	5.7
8.	Non-Developmental Expenditure / GDP	6.4	6.4	6.1	4.6
9.	States' Tax Revenue/GDP	5.9	5.9	5.8	5.3
10.	States' Non-Tax Revenue / GDP	1.5	1.5	1.4	1.7

RE : Revised Estimates. BE : Budget Estimates. – : Negligible. n.a. : Not available.
GFD : Gross Fiscal Deficit.
(-) : Indicates surplus.
* : Data pertain to State Governments having accounts with the Reserve Bank.
P : Provisional; data relate to the Budgets of 27 State Governments of which 6 are Vote-on-Account.
Note : Variations in net RBI credit to State Governments refer to variations in loans and advances given to them by the Reserve Bank net of their deposits with it.
Source : Budget Documents of the State Governments and the Reserve Bank Records.

APPENDIX TABLE IV.6 : COMBINED RECEIPTS AND DISBURSEMENTS – CENTRE AND STATES

(Rupees crore)

Item	2004-05 (BE)	2003-04 (RE)	2003-04 (BE)	2002-03 (Accounts)	2001-02 (Accounts)	Percentage Variation	
						Col.2 over Col.3	Col.3 over Col.5
1	2	3	4	5	6	7	8
I. Total Disbursements (A+B+C)	**8,98,819**	**8,85,293**	**8,19,833**	**7,26,139**	**6,52,968**	**1.5**	**21.9**
of which :							
A. Developmental Expenditure (i+ii +iii)	**4,28,266**	**4,39,465**	**4,05,720**	**3,57,948**	**3,29,074**	**-2.5**	**22.8**
i) Revenue	3,34,480	3,35,558	3,12,902	2,87,319	2,62,702	-0.3	16.8
ii) Capital	76,559	77,005	72,600	50,293	40,709	-0.6	53.1
iii) Loans	17,228	26,902	20,218	20,335	25,663	-36.0	32.3
B. Non-Developmental Expenditure (i+ii+iii)	**4,31,203**	**3,80,520**	**3,85,817**	**3,37,452**	**3,11,157**	**13.3**	**12.8**
i) Revenue	3,88,522	3,58,478	3,59,278	3,20,146	2,92,294	8.4	12.0
of which :							
Interest Payments	1,91,709	1,80,002	1,75,867	1,58,448	1,42,387	6.5	13.6
ii) Capital	40,788	20,017	24,744	15,017	18,118	103.8	33.3
iii) Loans	1,893	2,025	1,795	2,290	745	-6.5	-11.6
C. Others (i+ii)	**39,350**	**65,307**	**28,296**	**30,739**	**12,737**	**-39.7**	**112.5**
i) Revenue	6,830	7,313	7,025	6,052	4,515	-6.6	20.8
ii) Capital +	32,520	57,994	21,271	24,687	8,222	-43.9	134.9
II. Total Receipts	**8,98,290**	**8,72,973**	**8,12,595**	**7,30,509**	**6,51,039**	**2.9**	**19.5**
of which :							
A. Revenue Receipts	**6,05,401**	**5,29,248**	**5,18,090**	**4,50,464**	**4,00,162**	**14.4**	**17.5**
i) Tax Receipts (a + b + c)	4,94,232	4,15,283	4,13,057	3,57,889	3,13,844	19.0	16.0
a) Taxes on commodities and services	3,36,153	2,92,719	2,96,036	2,56,249	2,30,753	14.8	14.2
b) Taxes on Income and Property	1,57,454	1,21,970	1,16,463	1,01,067	82,546	29.1	20.7
c) Taxes of Union Territories (Without Legislature)	624	594	557	573	545	5.1	3.7
ii) Non-tax Receipts	1,11,169	1,13,965	1,05,033	92,575	86,318	-2.5	23.1
of which :							
Interest Receipts	20,484	17,934	18,416	17,768	17,141	14.2	0.9
B. Non-debt Capital Receipts (i+ii)	**14,552**	**37,835**	**21,273**	**16,065**	**18,160**	**-61.5**	**135.5**
i) Recovery of Loans and Advances	10,552	23,335	8,073	12,914	14,514	-54.8	80.7
ii) Disinvestment proceeds	4,000	14,500	13,200	3,151	3,646	-72.4	360.2
III. Gross Fiscal Deficit [I - ICii - (IIA + IIB)]	**2,46,345**	**2,60,217**	**2,59,200**	**2,34,923**	**2,26,425**	**-5.3**	**10.8**
Financed by :							
A. Institution-wise (i+ii)	**2,46,345**	**2,60,217**	**2,59,200**	**2,34,923**	**2,26,425**	**-5.3**	**10.8**
i) Domestic Financing (a+b)	2,38,269	2,71,922	2,55,618	2,46,857	2,20,824	-12.4	10.2
a) Net Bank Credit to Government#	n.a.	68,976	n.a.	86,958	77,610	–	-20.7
of which :							
Net RBI Credit to Government	n.a.	-75,772	n.a.	-31,499	-1,699	–	–
b) Non-Bank Credit to Government	n.a.	2,02,946	n.a.	1,59,899	1,43,214	–	26.9
ii) External Financing	8,076	-11,705	3,582	-11,934	5,601	-169.0	-1.9
B. Instrument-wise (i+ii)	**2,46,345**	**2,60,217**	**2,59,200**	**2,34,923**	**2,26,425**	**-5.3**	**10.8**
i) Domestic Financing (a+b+c+d+e)	2,38,269	2,71,922	2,55,618	2,46,857	2,20,824	-12.4	10.2
a) Market Borrowings (net)@	1,16,170	1,30,745	1,24,034	1,32,587	1,04,741	-11.1	-1.4
b) Small Savings (net)##	71,800	1,24,900	60,000	52,261	43,773	-42.5	139.0
c) State Provident Funds (net)	12,991	13,977	14,696	11,654	14,096	-7.1	19.9
d) Budget Deficit ++	13,068	-22,552	-7,238	2,486	1,929	–	–
e) Others**	24,240	24,852	46,126	47,869	47,869	-2.5	-48.1
ii) External Financing	8,076	-11,705	3,582	-11,934	5,601	–	–
IV. I as per cent of GDP	**28.8**	**31.9**	**29.9**	**29.4**	**28.6**	**–**	**–**
V. II as per cent of GDP	**28.8**	**31.5**	**29.6**	**29.6**	**28.5**	**–**	**–**
VI. IIA as per cent of GDP	**19.4**	**19.1**	**19.9**	**18.2**	**17.5**	**–**	**–**
VII. IIA (i) as per cent of GDP	**15.8**	**15.0**	**15.1**	**14.5**	**13.8**	**–**	**–**
VIII. IIII as per cent of GDP	**7.9**	**9.4**	**9.4**	**9.5**	**9.9**	**–**	**–**

BE : Budget Estimates. RE : Revised Estimate.

* : Data pertaining to State Governments from 2002-03 onwards are provisional and relate to Budgets of 27 State Governments, of which 6 are vote-on-account.

\+ : Including discharge of internal liabilities by the States and repayments to the NSSF by the Centre.

\# : As per Reserve Bank records.

@ : Borrowing through dated securities and 364-day Treasury Bills.

n.a. : Not available.

++ : Including drawdown of cash balance pertaining to Centre since 1997-98.

\## : Represents National Small Savings Fund's investment in the Central and State Government Special Securities.

** : Including reserve funds, deposits and advances, Treasury Bills excluding 364-day Treasury Bills, loan from international financial institutions, etc.

Source : Budget Documents of the Central and State Governments.

APPENDIX TABLE IV.7 : OUTSTANDING INTERNAL LIABILITIES OF THE CENTRAL GOVERNMENT

(Rupees crore)

Year	Internal Debt	Small Savings, Deposits, Provident Funds and Other Accounts	Reserve Funds and Deposits	Total Internal Liabilities (2+3+4)	External Liabilities	Total Liabilities
1	2	3	4	5	6	7
1990-91	1,54,004	1,07,107	21,922	2,83,033	31,525	3,14,558
	(27.1)	(18.8)	(3.9)	(49.8)	(5.5)	(55.3)
1995-96	3,07,869	2,13,436	33,680	5,54,985	51,247	6,06,232
	(25.9)	(18.0)	(2.8)	(46.7)	(4.3)	(51.0)
2000-01	8,03,698	2,40,364	58,535	11,02,597	65,945	11,68,542
	(38.5)	(11.5)	(2.8)	(52.8)	(3.2)	(55.9)
2001-02	9,13,061	3,08,668	73,133	12,94,862	71,546	13,66,408
	(40.0)	(13.5)	(3.2)	(56.7)	(3.1)	(59.9)
2002-03	10,20,689	3,98,774	80,126	14,99,589	59,612	15,59,201
	(41.3)	(16.1)	(3.2)	(60.7)	(2.4)	(63.1)
2003-04 (RE)	11,34,020	4,55,918	87,153	16,77,091	47,407	17,24,498
	(40.9)	(16.4)	(3.1)	(60.5)	(1.7)	(62.2)
2004-05 (BE)	12,91,628	5,46,056	93,399	19,31,083	55,084	19,86,167
	(41.4)	(17.5)	(3.0)	(61.8)	(1.8)	(63.6)

RE : Revised Estimates. BE : Budget Estimates.

Note : 1. Figures in parentheses represent percentages to GDP.

2. Beginning 1999-2000 Centre's share in small saving collection has been converted into Central Government special securities and are part of internal debt.

Source : Budget Documents of the Government of India.

APPENDIX TABLE IV.8 : FINANCING OF STATE GOVERNMENTS' GROSS FISCAL DEFICIT

(Rupees crore)

Year	Loans from the Central Government (net)	Market Borrowings (net)	Others#	Gross Fiscal Deficit (2+3+4)	States' Outstanding Liabilities (end-March)			States' Outstanding Liabilities as percentage to GDP at current market prices
					Total+	Loans and Advances from the Centre	Market Loans	
1	2	3	4	5	6	7	8	9
1990-91	9,978 (53.1)	2,556 (13.6)	6,253 (33.3)	18,787 (100.0)	1,10,289	74,117	15,618	19.4
1995-96	14,801 (47.1)	5,888 (18.7)	10,737 (34.2)	31,426 (100.0)	2,12,225	1,31,505	36,021	17.9
2002-03 P	-1,805 (-1.8)	28,461 (27.9)	75,402 (73.9)	1,02,058 (100.0)	6,86,142	2,33,759	1,31,176	27.8
2003-04 (RE) P	-21,238 (-15.1)	45,074 (32.1)	1,16,571 (83.0)	1,40,407 (100.0)	8,05,667	2,12,521	1,76,250	29.1
2004-05 (BE) P	-7,341 (-6.5)	25,805 (23.0)	93,787 (83.6)	1,12,251 (100.0)	9,10,902	2,05,180	2,02,055	29.2

RE : Revised Estimates. BE : Budget Estimates.

: Including loans from financial institutions, provident funds, reserve funds, deposits and advances, special securities issued to the NSSF, *etc.* With the change in the system of accounting with effect from 1999-2000, States' share in small savings which was hitherto included under loans from the Centre is included under others.

\+ : Including internal debt (including Special Securities issued to the NSSF), loans and advances from the Central Government and Provident Funds.

P : Provisional; data relate to the Budgets of 27 State Governments, of which 6 are Vote -on-Account.

Note : 1. Figures in parentheses are percentages to the Gross Fiscal Deficit.

2. Data on outstanding liabilities of the State Governments have been revised taking into account the latest available information.

Source : Budget Documents of the State governments and Combined Finance and Revenue Accounts of the Union and State Governments.

APPENDIX TABLE IV.9 : MARKET BORROWINGS – CENTRE, STATES AND SPONSORED INSTITUTIONS

(Rupees crore)

Government/Authority	Gross			Repayments			Net		
	2004-05 BE	2003-04+	2002-03+	2004-05 BE	2003-04+	2002-03+	2004-05 BE	2003-04+	2002-03+
1	2	3	4	5	6	7	8	9	10
1. Central Government (a+b)	1,50,817	1,47,636	1,51,126	60,452	58,819	47,008	90,365	88,816	1,04,118
a) Dated Securities	1,24,817	1,21,500	1,25,000	34,316	32,693	27,420	90,501	88,807	97,580
b) 364-day Treasury Bills	26,000	26,136	26,126	26,136	26,126	19,588	-136	9	6,538
2. State Governments	42,071 #	50,521 *	30,853	5,123	4,145	1,789	36,948	46,376	29,064
3. Institutions Sponsored by State Governments (relating to SFCs and SLDBs / SCARDBs)	–	–	319	–	–	271	–	–	48
Grand Total (1+2+3)	**1,92,888**	**1,98,157**	**1,82,298**	**65,575**	**62,964**	**49,068**	**1,27,313**	**1,35,192**	**1,33,230**

– : Not applicable. BE : Budget Estimates. + : Actuals as per the Reserve Bank Records.

* : Including additional borrowings of Rs. 26,623 crore for the Debt Swap Scheme.

\# : Including additional borrowings of R. 24,000 crore under the Debt Swap Scheme.

Source : Central Government Budget Documents and the Reserve Bank records.

APPENDIX TABLE V.1 : REPO / REVERSE REPO AUCTIONS UNDER LIQUIDITY ADJUSTMENT FACILITY

(Amount in Rupees crore)

LAF Date*	Repo/ Reverse Repo period (Day (s))	Repo					Reverse Repo					Net injections (+)/ absorption(–) of liquidity [(11) – (6)]	Outstanding Amount @
		Bids received		Bids Accepted		Cut-off Rate (per cent)	Bids Received		Bids Accepted		Cut-off Rate (per cent)		
		Number	Amount	Number	Amount		Number	Amount	Number	Amount			
1	2	3	4	5	6	7	8	9	10	11	12	13	14
2003-04													
1-Apr-03	2	23	14,010	23	14,010	5.00	6	1,635	6	1,635	7.00	-12,375	12,375
3-Apr-03	1	30	17,690	30	17,690	5.00	–	–	–	–	–	-17,690	17,690
4-Apr-03	3	34	27,880	34	27,880	5.00	–	–	–	–	–	-27,880	27,880
7-Apr-03	1	29	25,040	29	25,040	5.00	–	–	–	–	–	-25,040	#
	14	3	1,200	3	1,200	5.00	–	–	–	–	–	-1,200	26,240
8-Apr-03	1	35	31,185	35	31,185	5.00	–	–	–	–	–	-31,185	32,385
9-Apr-03	1	36	26,655	36	21,324	5.00	–	–	–	–	–	-21,324	22,524
10-Apr-03	6	36	28,645	36	28,645	5.00	–	–	–	–	–	-28,645	29,845
16-Apr-03	1	32	25,285	32	20,228	5.00	–	–	–	–	–	-20,228	21,428
17-Apr-03	4	46	21,115	46	21,115	5.00	–	–	–	–	–	-21,115	22,315
21-Apr-03	1	35	25,365	35	25,365	5.00	–	–	–	–	–	-25,365	#
	14	8	7,255	8	7,255	5.00	–	–	–	–	–	-7,255	32,620
22-Apr-03	1	37	31,995	37	31,995	5.00	–	–	–	–	–	-31,995	39,250
23-Apr-03	1	40	29,355	40	29,355	5.00	–	–	–	–	–	-29,355	36,610
24-Apr-03	1	37	27,525	37	27,525	5.00	–	–	–	–	–	-27,525	34,780
25-Apr-03	3	39	24,610	39	24,610	5.00	–	–	–	–	–	-24,610	31,865
28-Apr-03	1	44	27,660	44	27,660	5.00	–	–	–	–	–	-27,660	34,915
29-Apr-03	1	42	30,770	42	30,770	5.00	–	–	–	–	–	-30,770	38,025
30-Apr-03	2	45	22,960	45	22,960	5.00	–	–	–	–	–	-22,960	30,215
2-May-03	3	43	13,710	43	13,710	5.00	1	100	1	100	7.00	-13,610	20,865
5-May-03	1	40	16,115	40	16,115	5.00	–	–	–	–	–	-16,115	#
	14	8	12,520	8	6,260	5.00	–	–	–	–	–	-6,260	22,375
6-May-03	1	43	25,250	43	25,250	5.00	–	–	–	–	–	-25,250	31,510
7-May-03	1	40	24,400	40	24,400	5.00	–	–	–	–	–	-24,400	30,660
8-May-03	1	33	21,735	33	21,735	5.00	–	–	–	–	–	-21,735	27,995
9-May-03	3	37	20,020	37	20,020	5.00	–	–	–	–	–	-20,020	26,280
12-May-03	1	28	10,595	28	10,595	5.00	–	–	–	–	–	-10,595	16,855
13-May-03	1	34	12,540	34	12,540	5.00	–	–	–	–	–	-12,540	18,800
14-May-03	5	28	8,750	28	8,750	5.00	–	–	–	–	–	-8,750	15,010
19-May-03	1	36	16,155	36	16,155	5.00	–	–	–	–	–	-16,155	#
	14	7	8,835	7	8,835	5.00	–	–	–	–	–	-8,835	24,990
20-May-03	1	35	17,945	35	14,356	5.00	–	–	–	–	–	-14,356	23,191
21-May-03	1	29	12,495	29	12,495	5.00	–	–	–	–	–	-12,495	21,330
22-May-03	1	37	19,270	37	19,270	5.00	–	–	–	–	–	-19,270	28,105
23-May-03	3	41	23,125	41	23,125	5.00	–	–	–	–	–	-23,125	31,960
26-May-03	1	45	25,415	45	25,415	5.00	–	–	–	–	–	-25,415	34,250
27-May-03	1	43	30,015	43	30,015	5.00	–	–	–	–	–	-30,015	38,850
28-May-03	1	45	30,085	45	30,085	5.00	–	–	–	–	–	-30,085	38,920
29-May-03	1	44	30,230	44	30,230	5.00	–	–	–	–	–	-30,230	39,065
30-May-03	3	28	12,240	28	12,240	5.00	–	–	–	–	–	-12,240	21,075
2-Jun-03	1	33	20,865	33	20,865	5.00	–	–	–	–	–	-20,865	#
	14	9	13,945	9	9,762	5.00	–	–	–	–	–	-9,762	30,627
3-Jun-03	1	37	27,375	37	27,375	5.00	–	–	–	–	–	-27,375	37,137
4-Jun-03	1	32	18,235	32	18,235	5.00	–	–	–	–	–	-18,235	27,997
5-Jun-03	1	33	18,335	33	18,335	5.00	–	–	–	–	–	-18,335	28,097
6-Jun-03	3	33	19,275	33	19,275	5.00	–	–	–	–	–	-19,275	29,037
9-Jun-03	1	33	18,105	33	18,105	5.00	–	–	–	–	–	-18,105	27,867
10-Jun-03	1	29	15,270	29	10,693	5.00	–	–	–	–	–	-10,693	20,455
11-Jun-03	1	29	16,500	29	13,200	5.00	–	–	–	–	–	-13,200	22,962
12-Jun-03	1	19	4,315	19	4,315	5.00	–	–	–	–	–	-4,315	14,077
13-Jun-03	3	11	2,695	11	2,695	5.00	–	–	–	–	–	-2,695	12,457
16-Jun-03	1	26	10,350	26	10,350	5.00	–	–	–	–	–	-10,350	#
	11	3	10,020	3	6,012	5.00	–	–	–	–	–	-6,012	16,362
17-Jun-03	1	31	19,270	31	19,270	5.00	–	–	–	–	–	-19,270	25,282
18-Jun-03	1	30	19,935	30	19,935	5.00	–	–	–	–	–	-19,935	25,947
19-Jun-03	1	31	19,385	31	19,385	5.00	–	–	–	–	–	-19,385	25,397
20-Jun-03	3	27	19,270	27	19,270	5.00	–	–	–	–	–	-19,270	25,282
23-Jun-03	1	34	23,750	34	23,750	5.00	–	–	–	–	–	-23,750	29,762
24-Jun-03	1	40	28,305	40	28,305	5.00	–	–	–	–	–	-28,305	34,317
25-Jun-03	1	39	26,115	39	26,115	5.00	–	–	–	–	–	-26,115	32,127
26-Jun-03	1	42	26,490	42	26,490	5.00	–	–	–	–	–	-26,490	32,502
27-Jun-03	4	36	21,455	36	21,455	5.00	–	–	–	–	–	-21,455	21,455
1-Jul-03	1	33	21,970	32	21,945	5.00	–	–	–	–	–	-21,945	#
	13	4	14,750	4	14,750	5.00	–	–	–	–	–	-14,750	36,695
2-Jul-03	1	38	20,375	38	20,375	5.00	–	–	–	–	–	-20,375	35,125
3-Jul-03	1	40	24,155	40	24,155	5.00	–	–	–	–	–	-24,155	38,905
4-Jul-03	3	43	24,060	43	24,060	5.00	–	–	–	–	–	-24,060	38,810
7-Jul-03	1	40	27,470	40	27,470	5.00	–	–	–	–	–	-27,470	42,220
8-Jul-03	1	52	32,795	52	32,795	5.00	–	–	–	–	–	-32,795	47,545
9-Jul-03	1	49	32,005	49	32,005	5.00	–	–	–	–	–	-32,005	46,755
10-Jul-03	1	42	31,100	42	31,100	5.00	–	–	–	–	–	-31,100	45,850
11-Jul-03	3	41	26,960	41	26,960	5.00	–	–	–	–	–	-26,960	41,710
14-Jul-03	1	40	26,360	40	26,360	5.00	–	–	–	–	–	-26,360	#
	14	9	17,625	9	17,625	5.00	–	–	–	–	–	-17,625	43,985
15-Jul-03	1	46	29,030	46	29,030	5.00	–	–	–	–	–	-29,030	46,655
16-Jul-03	1	43	24,735	43	24,735	5.00	–	–	–	–	–	-24,735	42,360
17-Jul-03	1	48	25,280	48	25,280	5.00	–	–	–	–	–	-25,280	42,905
18-Jul-03	3	46	23,255	46	23,255	5.00	–	–	–	–	–	-23,255	40,880

APPENDIX TABLE V.1 : REPO / REVERSE REPO AUCTIONS UNDER LIQUIDITY ADJUSTMENT FACILITY *(Contd...)*

(Amount in Rupees crore)

LAF Date*	Repo/ Reverse Repo period (Day (s))	Repo					Reverse Repo					Net injections (+)/ absorption(–) of liquidity [(11) – (6)]	Outstanding Amount @
		Bids Received		Bids Accepted		Cut-off Rate (per cent)	Bids Received		Bids Accepted		Cut-off Rate (per cent)		
		Number	Amount	Number	Amount		Number	Amount	Number	Amount			
1	2	3	4	5	6	7	8	9	10	11	12	13	14
21-Jul-03	1	41	25,400	41	25,400	5.00	–	–	–	–	–	-25,400	43,025
22-Jul-03	1	50	29,425	50	29,425	5.00	–	–	–	–	–	-29,425	47,050
23-Jul-03	1	47	29,150	47	29,150	5.00	–	–	–	–	–	-29,150	46,775
24-Jul-03	1	50	27,050	50	27,050	5.00	–	–	–	–	–	-27,050	44,675
25-Jul-03	3	48	22,855	48	22,855	5.00	–	–	–	–	–	-22,855	40,480
28-Jul-03	1	48	33,590	48	33,590	5.00	–	–	–	–	–	-33,590	#
	14	11	20,530	11	20,530	5.00	–	–	–	–	–	-20,530	54,120
29-Jul-03	1	46	27,905	46	27,905	5.00	–	–	–	–	–	-27,905	48,435
30-Jul-03	1	37	17,780	37	17,780	5.00	2	1,220	2	1,220	7.00	-16,560	37,090
31-Jul-03	1	44	25,845	44	25,845	5.00	–	–	–	–	–	-25,845	46,375
1-Aug-03	3	48	31,130	48	31,130	5.00	–	–	–	–	–	-31,130	51,660
4-Aug-03	1	51	34,305	51	34,305	5.00	–	–	–	–	–	-34,305	54,835
5-Aug-03	1	49	34,570	49	34,570	5.00	–	–	–	–	–	-34,570	55,100
6-Aug-03	1	49	31,890	49	31,890	5.00	–	–	–	–	–	-31,890	52,420
7-Aug-03	1	53	25,460	53	25,460	5.00	–	–	–	–	–	-25,460	45,990
8-Aug-03	3	47	19,860	47	19,860	5.00	–	–	–	–	–	-19,860	40,390
11-Aug-03	1	43	17,795	43	17,795	5.00	–	–	–	–	–	-17,795	#
	14	15	20,830	15	20,830	5.00	–	–	–	–	–	-20,830	38,625
12-Aug-03	1	43	22,985	43	22,985	5.00	–	–	–	–	–	-22,985	43,815
13-Aug-03	1	41	20,035	41	20,035	5.00	–	–	–	–	–	-20,035	40,865
14-Aug-03	4	35	14,065	35	14,065	5.00	–	–	–	–	–	-14,065	34,895
18-Aug-03	1	31	13,825	31	13,825	5.00	–	–	–	–	–	-13,825	34,655
19-Aug-03	1	33	17,800	32	17,750	5.00	–	–	–	–	–	-17,750	38,580
20-Aug-03	1	31	17,165	31	17,165	5.00	–	–	–	–	–	-17,165	37,995
21-Aug-03	1	30	16,940	30	16,940	5.00	–	–	–	–	–	-16,940	37,770
22-Aug-03	3	38	14,810	38	14,810	5.00	–	–	–	–	–	-14,810	35,640
25-Aug-03	1	17	2,675	16	2,585	4.50	–	–	–	–	–	-2,585	#
	14	6	14,790	6	14,790	4.50	–	–	–	–	–	-14,790	17,375
26-Aug-03	1	36	16,805	36	16,805	4.50	–	–	–	–	–	-16,805	31,595
27-Aug-03	1	35	23,015	35	23,015	4.50	–	–	–	–	–	-23,015	37,805
28-Aug-03	1	36	24,850	36	24,850	4.50	–	–	–	–	–	-24,850	39,640
29-Aug-03	3	37	21,925	37	21,925	4.50	–	–	–	–	–	-21,925	36,715
01-Sep-03	1	42	28,430	41	28,230	4.50	–	–	–	–	–	-28,230	43,020
02-Sep-03	1	43	30,940	43	30,940	4.50	–	–	–	–	–	-30,940	45,730
03-Sep-03	1	45	32,900	45	32,900	4.50	–	–	–	–	–	-32,900	47,690
04-Sep-03	1	45	26,970	45	26,970	4.50	–	–	–	–	–	-26,970	41,760
05-Sep-03	3	42	17,645	42	17,645	4.50	–	–	–	–	–	-17,645	32,435
08-Sep-03	1	36	21,740	36	21,740	4.50	–	–	–	–	–	-21,740	#
	14	7	16,870	7	16,870	4.50	–	–	–	–	–	-16,870	38,610
09-Sep-03	1	34	16,265	34	16,265	4.50	–	–	–	–	–	-16,265	33,135
10-Sep-03	1	29	18,040	29	18,040	4.50	–	–	–	–	–	-18,040	34,910
11-Sep-03	1	28	14,940	28	14,940	4.50	–	–	–	–	–	-14,940	31,810
12-Sep-03	3	32	9,105	32	9,105	4.50	–	–	–	–	–	-9,105	25,975
15-Sep-03	1	36	13,855	36	13,855	4.50	–	–	–	–	–	-13,855	30,725
16-Sep-03	1	38	24,815	38	24,815	4.50	–	–	–	–	–	-24,815	41,685
17-Sep-03	1	31	19,050	31	19,050	4.50	–	–	–	–	–	-19,050	35,920
18-Sep-03	1	26	16,185	26	16,185	4.50	–	–	–	–	–	-16,185	33,055
19-Sep-03	3	25	9,040	25	9,040	4.50	–	–	–	–	–	-9,040	25,910
22-Sep-03	1	24	20,005	24	20,005	4.50	–	–	–	–	–	-20,005	#
	14	4	1,195	4	1,195	4.50	–	–	–	–	–	-1,195	21,200
23-Sep-03	1	15	16,330	15	8,167	4.50	–	–	–	–	–	-8,167	9,362
24-Sep-03	1	22	21,825	22	16,372	4.50	–	–	–	–	–	-16,372	17,567
25-Sep-03	1	30	28,250	30	28,250	4.50	–	–	–	–	–	-28,250	29,445
26-Sep-03	3	31	27,205	31	27,205	4.50	–	–	–	–	–	-27,205	28,400
29-Sep-03	1	29	26,270	29	26,270	4.50	–	–	–	–	–	-26,270	27,465
30-Sep-03	1	40	38,750	40	38,750	4.50	–	–	–	–	–	-38,750	39,945
1-Oct-03	2	43	19,165	43	19,165	4.50	–	–	–	–	–	-19,165	20,360
3-Oct-03	3	40	19,825	40	19,825	4.50	–	–	–	–	–	-19,825	21,020
6-Oct-03	1	27	19,145	27	19,145	4.50	–	–	–	–	–	-19,145	#
	14	4	100	4	100	4.50	–	–	–	–	–	-100	19,245
7-Oct-03	1	35	21,715	35	21,715	4.50	–	–	–	–	–	-21,715	21,815
8-Oct-03	1	37	22,490	37	22,490	4.50	–	–	–	–	–	-22,490	22,590
9-Oct-03	1	40	27,160	40	27,160	4.50	–	–	–	–	–	-27,160	27,260
10-Oct-03	3	37	17,805	37	17,805	4.50	–	–	–	–	–	-17,805	17,905
13-Oct-03	1	21	7,090	21	7,090	4.50	–	–	–	–	–	-7,090	7,190
14-Oct-03	1	30	12,960	30	12,960	4.50	–	–	–	–	–	-12,960	13,060
15-Oct-03	1	37	15,140	37	15,140	4.50	–	–	–	–	–	-15,140	15,240
16-Oct-03	1	40	17,835	40	17,835	4.50	–	–	–	–	–	-17,835	17,935
17-Oct-03	3	42	16,745	42	16,745	4.50	–	–	–	–	–	-16,745	16,845
20-Oct-03	1	25	8,310	25	8,310	4.50	–	–	–	–	–	-8,310	#
	14	1	25	1	25	4.50	–	–	–	–	–	-25	#
	28	3	1,275	3	1,275	4.50	–	–	–	–	–	-1,275	9,610
21-Oct-03	1	26	8,785	26	8,785	4.50	–	–	–	–	–	-8,785	#
	28	4	655	4	655	4.50	–	–	–	–	–	-655	10,740
22-Oct-03	1	21	8,580	21	6,436	4.50	–	–	–	–	–	-6,436	#
	28	0	0	0	0	4.50	–	–	–	–	–	0	8,391
23-Oct-03	1	21	8,350	21	8,350	4.50	–	–	–	–	–	-8,350	#
	28	3	640	3	640	4.50	–	–	–	–	–	-640	10,945
24-Oct-03	3	18	5,880	18	5,880	4.50	–	–	–	–	–	-5,880	#
	28	2	245	2	245	4.50	–	–	–	–	–	-245	8,720

APPENDIX TABLE V.1 : REPO / REVERSE REPO AUCTIONS UNDER LIQUIDITY ADJUSTMENT FACILITY *(Contd...)*

(Amount in Rupees crore)

LAF Date*	Repo/ Reverse Repo period (Day (s))	Repo					Reverse Repo					Net injections (+)/ absorption(–) of liquidity [(11) – (6)]	Outstanding Amount @
		Bids Received		Bids Accepted		Cut-off Rate (per cent)	Bids Received		Bids Accepted		Cut-off Rate (per cent)		
		Number	Amount	Number	Amount		Number	Amount	Number	Amount			
1	2	3	4	5	6	7	8	9	10	11	12	13	14
27-Oct-03	1	13	4,020	13	4,020	4.50	–	–	–	–	–	-4,020	6,860
28-Oct-03	1	3	2,080	3	2,080	4.50	–	–	–	–	–	-2,080	4,920
29-Oct-03	1	4	1,685	0	0	4.50	3	1,900	–	–	–	–	2,840
30-Oct-03	1	2	140	0	0	4.50	–	–	–	–	–	–	2,840
31-Oct-03	3	19	5,500	19	5,500	4.50	–	–	–	–	–	-5,500	8,340
03-Nov-03	1	26	9,610	26	9,610	4.50	–	–	–	–	–	-9,610	#
	14	3	535	3	535	4.50	–	–	–	–	–	-535	12,960
04-Nov-03	1	35	17,340	35	17,340	4.50	–	–	–	–	–	-17,340	20,690
05-Nov-03	1	41	19,125	41	19,125	4.50	–	–	–	–	–	-19,125	22,475
06-Nov-03	1	37	16,945	37	16,945	4.50	–	–	–	–	–	-16,945	20,295
07-Nov-03	3	37	15,535	37	15,535	4.50	–	–	–	–	–	-15,535	18,885
10-Nov-03	1	37	13,420	37	13,420	4.50	–	–	–	–	–	-13,420	16,770
11-Nov-03	1	33	13,625	33	13,625	4.50	–	–	–	–	–	-13,625	16,975
12-Nov-03	1	37	11,025	37	11,025	4.50	–	–	–	–	–	-11,025	14,375
13-Nov-03	1	43	14,170	43	14,170	4.50	–	–	–	–	–	-14,170	17,520
14-Nov-03	3	48	16,815	48	16,815	4.50	–	–	–	–	–	-16,815	20,165
17-Nov-03	1	37	14,370	37	14,370	4.50	–	–	–	–	–	-14,370	#
	14	6	1,425	6	1,425	4.50	–	–	–	–	–	-1,425	17,335
18-Nov-03	1	45	17,465	45	17,465	4.50	–	–	–	–	–	-17,465	19,775
19-Nov-03	1	52	20,125	52	20,125	4.50	–	–	–	–	–	-20,125	22,435
20-Nov-03	1	52	21,450	52	21,450	4.50	–	–	–	–	–	-21,450	23,120
21-Nov-03	3	57	24,355	57	24,355	4.50	–	–	–	–	–	-24,355	25,780
24-Nov-03	1	61	26,150	61	26,150	4.50	–	–	–	–	–	-26,150	27,575
25-Nov-03	2	61	29,115	61	29,115	4.50	–	–	–	–	–	-29,115	30,540
27-Nov-03	1	58	28,320	58	28,320	4.50	–	–	–	–	–	-28,320	29,745
28-Nov-03	3	58	25,635	58	25,635	4.50	–	–	–	–	–	-25,635	27,060
1-Dec-03	1	52	25,745	52	25,745	4.50	–	–	–	–	–	-25,745	#
	14	11	6,345	11	6,345	4.50	–	–	–	–	–	-6,345	32,090
2-Dec-03	1	57	29,910	57	29,910	4.50	–	–	–	–	–	-29,910	36,255
3-Dec-03	1	59	31,620	59	31,620	4.50	–	–	–	–	–	-31,620	37,965
4-Dec-03	1	58	32,930	58	32,930	4.50	–	–	–	–	–	-32,930	39,275
5-Dec-03	3	53	28,035	53	28,035	4.50	–	–	–	–	–	-28,035	34,380
8-Dec-03	1	58	29,325	58	29,325	4.50	–	–	–	–	–	-29,325	35,670
9-Dec-03	1	61	25,030	61	25,030	4.50	–	–	–	–	–	-25,030	31,375
10-Dec-03	1	59	27,170	59	27,170	4.50	–	–	–	–	–	-27,170	33,515
11-Dec-03	1	63	27,775	63	27,775	4.50	–	–	–	–	–	-27,775	34,120
12-Dec-03	3	54	25,540	54	25,540	4.50	–	–	–	–	–	-25,540	31,885
15-Dec-03	1	53	24,775	53	24,775	4.50	–	–	–	–	–	-24,775	#
	14	9	3,135	9	3,135	4.50	–	–	–	–	–	-3,135	27,910
16-Dec-03	1	55	31,110	55	31,110	4.50	–	–	–	–	–	-31,110	34,245
17-Dec-03	1	50	29,475	50	29,475	4.50	–	–	–	–	–	-29,475	32,610
18-Dec-03	1	48	25,245	48	25,245	4.50	–	–	–	–	–	-25,245	28,380
19-Dec-03	3	46	21,925	46	21,925	4.50	–	–	–	–	–	-21,925	25,060
22-Dec-03	1	54	26,245	54	26,245	4.50	–	–	–	–	–	-26,245	29,380
23-Dec-03	1	52	28,505	52	28,505	4.50	–	–	–	–	–	-28,505	31,640
24-Dec-03	2	52	29,315	52	29,315	4.50	–	–	–	–	–	-29,315	32,450
26-Dec-03	3	56	26,355	56	26,355	4.50	–	–	–	–	–	-26,355	29,490
29-Dec-03	1	50	23,370	50	23,370	4.50	–	–	–	–	–	-23,370	#
	14	9	6,965	9	6,965	4.50	–	–	–	–	–	-6,965	30,335
30-Dec-03	1	51	29,595	51	29,595	4.50	–	–	–	–	–	-29,595	36,560
31-Dec-03	1	46	26,995	46	26,995	4.50	–	–	–	–	–	-26,995	33,960
1-Jan-04	1	47	33,735	47	33,735	4.50	–	–	–	–	–	-33,735	40,700
2-Jan-04	3	58	40,055	58	40,055	4.50	–	–	–	–	–	-40,055	47,020
5-Jan-04	1	60	46,085	60	46,085	4.50	–	–	–	–	–	-46,085	53,050
6-Jan-04	1	57	47,720	57	47,720	4.50	–	–	–	–	–	-47,720	54,685
7-Jan-04	1	54	40,080	54	40,080	4.50	–	–	–	–	–	-40,080	47,045
8-Jan-04	1	51	32,330	51	32,330	4.50	–	–	–	–	–	-32,330	39,295
9-Jan-04	3	50	29,640	50	29,640	4.50	–	–	–	–	–	-29,640	36,605
12-Jan-04	1	42	27,960	42	27,960	4.50	–	–	–	–	–	-27,960	#
	11	11	7,145	11	7,145	4.50	–	–	–	–	–	-7,145	35,105
13-Jan-04	1	35	23,300	35	23,300	4.50	1	1,800	–	–	–	-23,300	30,445
14-Jan-04	1	48	33,090	48	33,090	4.50	–	–	–	–	–	-33,090	40,235
15-Jan-04	1	49	32,120	49	32,120	4.50	–	–	–	–	–	-32,120	39,265
16-Jan-04	3	46	32,630	46	32,630	4.50	–	–	–	–	–	-32,630	39,775
19-Jan-04	1	41	23,715	41	23,715	4.50	–	–	–	–	–	-23,715	30,860
20-Jan-04	1	42	27,445	42	27,445	4.50	–	–	–	–	–	-27,445	34,590
21-Jan-04	1	43	24,655	43	24,655	4.50	–	–	–	–	–	-24,655	31,800
22-Jan-04	1	43	23,130	43	23,130	4.50	–	–	–	–	–	-23,130	30,275
23-Jan-04	4	45	23,975	45	23,975	4.50	–	–	–	–	–	-23,975	31,120
27-Jan-04	1	50	27,600	50	27,600	4.50	–	–	–	–	–	-27,600	#
	13	12	4,455	12	4,455	4.50	–	–	–	–	–	-4,455	32,055
28-Jan-04	1	53	35,280	53	35,280	4.50	–	–	–	–	–	-35,280	39,735
29-Jan-04	1	53	37,260	53	37,260	4.50	–	–	–	–	–	-37,260	41,715
30-Jan-04	4	55	36,470	55	36,470	4.50	–	–	–	–	–	-36,470	40,925
3-Feb-04	1	60	40,735	60	40,735	4.50	–	–	–	–	–	-40,735	45,190
4-Feb-04	1	59	44,920	59	44,920	4.50	–	–	–	–	–	-44,920	49,375
5-Feb-04	1	59	43,425	59	43,425	4.50	–	–	–	–	–	-43,425	47,880
6-Feb-04	3	61	42,620	61	42,620	4.50	–	–	–	–	–	-42,620	47,075
9-Feb-04	1	56	37,305	56	37,305	4.50	–	–	–	–	–	-37,305	#
	14	15	5,925	15	5,925	4.50	–	–	–	–	–	-5,925	43,230

APPENDIX TABLE V.1 : REPO / REVERSE REPO AUCTIONS UNDER LIQUIDITY ADJUSTMENT FACILITY *(Contd...)*

(Amount in Rupees crore)

LAF Date *	Repo/ Reverse Repo period (Day (s))	Repo					Reverse Repo					Net injections (+)/ absorption(–) of liquidity [(11) – (6)]	Outstanding Amount @
		Bids Received		Bids Accepted		Cut-off Rate (per cent)	Bids Received		Bids accepted		Cut-off Rate (per cent)		
		Number	Amount	Number	Amount		Number	Amount	Number	Amount			
1	2	3	4	5	6	7	8	9	10	11	12	13	14
10-Feb-04	1	58	38,800	58	38,800	4.50	–	–	–	–	–	-38,800	44,725
11-Feb-04	1	57	37,440	57	37,440	4.50	–	–	–	–	–	-37,440	43,365
12-Feb-04	1	57	37,700	57	37,700	4.50	–	–	–	–	–	-37,700	43,625
13-Feb-04	3	60	36,185	60	36,185	4.50	–	–	–	–	–	-36,185	42,110
16-Feb-04	1	55	33,790	55	33,790	4.50	–	–	–	–	–	-33,790	39,715
17-Feb-04	2	63	41,855	63	41,855	4.50	–	–	–	–	–	-41,855	47,780
19-Feb-04	1	66	41,580	65	41,075	4.50	–	–	–	–	–	-41,075	47,000
20-Feb-04	3	72	46,055	72	46,055	4.50	–	–	–	–	–	-46,055	51,980
23-Feb-04	1	58	37,505	58	37,505	4.50	–	–	–	–	–	-37,505	#
	14	17	7,495	17	7,495	4.50	–	–	–	–	–	-7,495	45,000
24-Feb-04	1	53	39,465	53	39,465	4.50	–	–	–	–	–	-39,465	46,960
25-Feb-04	1	59	41,475	59	41,475	4.50	–	–	–	–	–	-41,475	48,970
26-Feb-04	1	59	44,050	59	44,050	4.50	–	–	–	–	–	-44,050	51,545
27-Feb-04	3	60	40,370	60	40,370	4.50	–	–	–	–	–	-40,370	47,865
1-Mar-04	2	66	46,975	66	46,975	4.50	–	–	–	–	–	-46,975	54,470
3-Mar-04	1	59	46,175	59	46,175	4.50	–	–	–	–	–	-46,175	53,670
4-Mar-04	1	66	47,065	66	47,065	4.50	–	–	–	–	–	-47,065	54,560
5-Mar-04	3	68	46,595	68	46,595	4.50	–	–	–	–	–	-46,595	54,090
8-Mar-04	1	63	48,370	63	48,370	4.50	–	–	–	–	–	-48,370	#
	14	15	7,250	15	7,250	4.50	–	–	–	–	–	-7,250	55,620
9-Mar-04	1	63	50,980	63	50,980	4.50	–	–	–	–	–	-50,980	58,230
10-Mar-04	1	59	50,765	59	50,765	4.50	–	–	–	–	–	-50,765	58,015
11-Mar-04	1	59	49,345	59	49,345	4.50	–	–	–	–	–	-49,345	56,595
12-Mar-04	3	57	47,380	57	47,380	4.50	–	–	–	–	–	-47,380	54,630
15-Mar-04	1	49	51,925	49	51,925	4.50	–	–	–	–	–	-51,925	59,175
16-Mar-04	1	51	55,045	51	55,045	4.50	–	–	–	–	–	-55,045	62,295
17-Mar-04	1	49	48,415	49	48,415	4.50	–	–	–	–	–	-48,415	55,665
18-Mar-04	1	49	42,395	49	42,395	4.50	–	–	–	–	–	-42,395	49,645
19-Mar-04	3	47	39,745	47	39,745	4.50	–	–	–	–	–	-39,745	46,995
22-Mar-04	1	50	42,225	50	42,225	4.50	–	–	–	–	–	-42,225	#
	14	18	7,520	18	7,520	4.50	–	–	–	–	–	-7,520	49,745
23-Mar-04	1	56	53,090	56	53,090	4.50	–	–	–	–	–	-53,090	60,610
24-Mar-04	1	55	55,475	55	55,475	4.50	–	–	–	–	–	-55,475	62,995
25-Mar-04	1	52	51,645	52	51,645	4.50	–	–	–	–	–	-51,645	59,165
26-Mar-04	3	55	53,880	55	53,880	4.50	–	–	–	–	–	-53,880	61,400
29-Mar-04	2	56	45,660	56	45,660	4.50	–	–	–	–	–	-45,660	#
29-Mar-04	7	13	2,475	13	2,475	4.50	–	–	–	–	–	-2,475	55,655
31-Mar-04	1	36	22,780	36	22,780	4.50	–	–	–	–	–	-22,780	#
31-Mar-04	7	10	2,020	10	2,020	4.50	–	–	–	–	–	-2,020	#
31-Mar-04	1	–	–	–	–	–	1	150	1	150	6.00	150	34,645
2004-05													
1-Apr-04	1	51	44,800	51	44,800	4.50	–	–	–	–	–	-44,800	#
1-Apr-04	7	12	2,390	12	2,390	4.50	–	–	–	–	–	-2,390	59,205
2-Apr-04	3	51	44,830	51	44,830	4.50	–	–	–	–	–	-44,830	#
2-Apr-04	6	18	5,925	18	5,925	4.50	–	–	–	–	–	-5,925	65,160
5-Apr-04	7	55	32,350	55	32,350	4.50	–	–	–	–	–	-32,350	#
	14	11	6,150	11	6,150	4.50	–	–	–	–	–	-6,150	48,835
6-Apr-04	7	37	19,455	37	19,455	4.50	–	–	–	–	–	-19,455	68,290
7-Apr-04	6	36	9,075	36	9,075	4.50	–	–	–	–	–	-9,075	75,345
8-Apr-04	7	23	7,380	23	7,380	4.50	–	–	–	–	–	-7,380	74,410
12-Apr-04	7	51	29,800	51	29,800	4.50	–	–	–	–	–	-29,800	71,860
13-Apr-04	7	48	29,310	48	29,310	4.50	–	–	–	–	–	-29,310	72,640
15-Apr-04	7	45	15,580	45	15,580	4.50	–	–	–	–	–	-15,580	80,840
16-Apr-04	7	31	8,595	31	8,595	4.50	–	–	–	–	–	-8,595	89,435
19-Apr-04	4	44	27,065	44	27,065	4.50	–	–	–	–	–	-27,065	#
	14	14	6,335	14	6,335	4.50	–	–	–	–	–	-6,335	86,885
20-Apr-04	7	37	18,275	37	18,275	4.50	–	–	–	–	–	-18,275	75,850
21-Apr-04	7	31	10,215	31	10,215	4.50	–	–	–	–	–	-10,215	86,065
22-Apr-04	7	41	12,580	41	12,580	4.50	–	–	–	–	–	-12,580	83,065
23-Apr-04	7	53	27,950	53	27,950	4.50	–	–	–	–	–	-27,950	75,355
27-Apr-04	6	42	17,825	42	17,825	4.50	–	–	–	–	–	-17,825	74,905
28-Apr-04	7	40	13,135	40	13,135	4.50	–	–	–	–	–	-13,135	77,825
29-Apr-04	7	35	14,775	35	14,775	4.50	–	–	–	–	–	-14,775	80,020
30-Apr-04	7	48	21,005	48	21,005	4.50	–	–	–	–	–	-21,005	73,075
3-May-04	7	48	24,840	48	24,840	4.50	–	–	–	–	–	-24,840	#
	14	10	5,515	10	5,515	4.50	–	–	–	–	–	-5,515	79,270
5-May-04	7	40	16,490	40	16,490	4.50	–	–	–	–	–	-16,490	82,625
6-May-04	7	39	9,915	39	9,915	4.50	–	–	–	–	–	-9,915	77,765
7-May-04	7	39	19,340	39	19,340	4.50	–	–	–	–	–	-19,340	76,100
10-May-04	7	44	21,680	44	21,680	4.50	–	–	–	–	–	-21,680	72,940
11-May-04	7	23	3,915	23	3,915	4.50	–	–	–	–	–	-3,915	76,855
12-May-04	7	39	11,340	39	11,340	4.50	–	–	–	–	–	-11,340	71,705
13-May-04	7	32	10,995	32	10,995	4.50	–	–	–	–	–	-10,995	72,785
14-May-04	7	41	20,050	41	20,050	4.50	–	–	–	–	–	-20,050	73,495
17-May-04	7	44	22,410	44	22,410	4.50	–	–	–	–	–	-22,410	#
	14	10	6,060	10	6,060	4.50	–	–	–	–	–	-6,060	74,770
18-May-04	7	26	5,395	26	5,395	4.50	–	–	–	–	–	-5,395	76,250
19-May-04	7	38	9,385	38	9,385	4.50	–	–	–	–	–	-9,385	74,295
20-May-04	7	32	8,420	32	8,420	4.50	–	–	–	–	–	-8,420	71,720

APPENDIX TABLE V.1 : REPO / REVERSE REPO AUCTIONS UNDER LIQUIDITY ADJUSTMENT FACILITY *(Concld.)*

(Amount in Rupees crore)

LAF Date*	Repo/ Reverse Repo period (Day (s))	Repo					Reverse Repo					Net injections (+)/ absorption(–) of liquidity [(11) – (6)]	Outstanding Amount @
		Bids Received		Bids Accepted		Cut-off Rate (per cent)	Bids Received		Bids Accepted		Cut-off Rate (per cent)		
		Number	Amount	Number	Amount		Number	Amount	Number	Amount			
1	2	3	4	5	6	7	8	9	10	11	12	13	14
21-May-04	7	45	17,645	45	17,645	4.50	–	–	–	–	–	-17,645	69,315
24-May-04	7	49	24,030	49	24,030	4.50	–	–	–	–	–	-24,030	70,935
25-May-04	7	37	13,560	37	13,560	4.50	–	–	–	–	–	-13,560	79,100
26-May-04	7	38	10,195	38	10,195	4.50	–	–	–	–	–	-10,195	79,910
27-May-04	7	32	8,945	32	8,945	4.50	–	–	–	–	–	-8,945	80,435
28-May-04	7	40	10,055	40	10,055	4.50	–	–	–	–	–	-10,055	72,845
31-May-04	7	45	21,205	45	21,205	4.50	–	–	–	–	–	-21,205	#
	14	7	3,555	7	3,555	4.50	–	–	–	–	–	-3,555	67,515
1-Jun-04	7	42	13,000	42	13,000	4.50	–	–	–	–	–	-13,000	66,955
2-Jun-04	7	37	11,420	37	11,420	4.50	–	–	–	–	–	-11,420	68,180
3-Jun-04	7	31	9,815	31	9,815	4.50	–	–	–	–	–	-9,815	69,050
4-Jun-04	7	29	8,450	29	8,450	4.50	1	800	1	800	6.00	-7,650	66,645
7-Jun-04	7	41	16,330	41	16,330	4.50	–	–	–	–	–	-16,330	62,570
8-Jun-04	7	41	11,250	41	11,250	4.50	–	–	–	–	–	-11,250	60,820
9-Jun-04	7	33	9,200	33	9,200	4.50	–	–	–	–	–	-9,200	58,600
10-Jun-04	7	34	8,125	34	8,125	4.50	–	–	–	–	–	-8,125	56,910
11-Jun-04	7	33	8,560	33	8,560	4.50	–	–	–	–	–	-8,560	57,020
14-Jun-04	7	44	17,735	44	17,735	4.50	–	–	–	–	–	-17,735	#
	14	8	4,550	8	4,550	4.50	–	–	–	–	–	-4,550	59,420
15-Jun-04	7	45	13,335	45	13,335	4.50	–	–	–	–	–	-13,335	61,505
16-Jun-04	7	49	9,150	49	9,150	4.50	–	–	–	–	–	-9,150	61,455
17-Jun-04	7	33	7,395	33	7,395	4.50	–	–	–	–	–	-7,395	60,725
18-Jun-04	7	34	9,630	34	9,630	4.50	–	–	–	–	–	-9,630	61,795
21-Jun-04	7	47	16,650	47	16,650	4.50	–	–	–	–	–	-16,650	60,710
22-Jun-04	7	48	13,565	48	13,565	4.50	–	–	–	–	–	-13,565	60,940
23-Jun-04	6	35	9,185	35	9,185	4.50	–	–	–	–	–	-9,185	60,975
24-Jun-04	7	40	8,510	40	8,510	4.50	–	–	–	–	–	-8,510	62,090
25-Jun-04	7	38	8,905	38	8,905	4.50	–	–	–	–	–	-8,905	61,365
28-Jun-04	7	44	20,825	44	20,825	4.50	–	–	–	–	–	-20,825	#
	14	7	3,295	7	3,295	4.50	–	–	–	–	–	-3,295	64,285
29-Jun-04	7	45	20,350	45	20,350	4.50	–	–	–	–	–	-20,350	61,885
1-Jul-04	7	38	12,360	38	12,360	4.50	–	–	–	–	–	-12,360	65,735
2-Jul-04	7	38	10,735	38	10,735	4.50	–	–	–	–	–	-10,735	67,565
5-Jul-04	7	41	20,990	41	20,990	4.50	–	–	–	–	–	-20,990	67,730
6-Jul-04	7	39	15,015	39	15,015	4.50	–	–	–	–	–	-15,015	62,395
7-Jul-04	7	28	4,660	28	4,660	4.50	–	–	–	–	–	-4,660	67,055
8-Jul-04	7	35	9,360	35	9,360	4.50	–	–	–	–	–	-9,360	64,055
9-Jul-04	7	42	11,235	42	11,235	4.50	–	–	–	–	–	-11,235	64,555
12-Jul-04	7	37	17,700	37	17,700	4.50	–	–	–	–	–	-17,700	57,970
12-Jul-04	14	8	2,965	8	2,965	4.50	–	–	–	–	–	-2,965	60,935
13-Jul-04	7	43	12,680	43	12,680	4.50	–	–	–	–	–	-12,680	58,600
14-Jul-04	7	29	4,850	29	4,850	4.50	–	–	–	–	–	-4,850	58,790
15-Jul-04	7	25	9,360	25	9,360	4.50	–	–	–	–	–	-9,360	54,450
16-Jul-04	7	37	11,235	37	11,235	4.50	–	–	–	–	–	-11,235	53,630
19-Jul,-04	7	38	15,950	38	15,950	4.50	–	–	–	–	–	-15,950	51,880
20-Jul-04	7	41	12,505	41	12,505	4.50	–	–	–	–	–	-12,505	51,705
21-Jul-04	7	30	5,950	30	5,950	4.50	–	–	–	–	–	-5,950	52,805
22-Jul-04	7	43	7,275	43	7,275	4.50	–	–	–	–	–	-7,275	55,060
23-Jul-04	7	45	13,430	45	13,430	4.50	–	–	–	–	–	-13,430	58,075
26-Jul-04	7	40	16765	40	16765	4.50	–	–	–	–	–	-16765	55925
26-Jul-04	14	8	2085	8	2085	4.50	–	–	–	–	–	-2085	58010
27-Jul-04	7	48	15030	48	15030	4.50	–	–	–	–	–	-15030	60535
28-Jul-04	7	27	5650	27	5650	4.50	–	–	–	–	–	-5650	60235
29-Jul-04	7	38	6455	38	6455	4.50	–	–	–	–	–	-6455	59415
30-Jul-04	7	32	7295	32	7295	4.50	–	–	–	–	–	-7295	53280
02-Aug-04	7	41	17,315	41	17,315	4.50	–	–	–	–	–	-17,315	53,830
03-Aug-04	7	42	14,365	42	14,365	4.50	–	–	–	–	–	-14,365	53,165
04-Aug-04	7	35	8,395	35	8,395	4.50	–	–	–	–	–	-8,395	55,910
05-Aug-04	7	29	5,735	29	5,735	4.50	–	–	–	–	–	-5,735	55,190
06-Aug-04	7	33	7,760	33	7,760	4.50	–	–	–	–	–	-7,760	55,655
09-Aug-04	7	40	16,980	40	16,980	4.50	–	–	–	–	–	-16,980	53,235
09-Aug-04	14	8	2,580	8	2,580	4.50	–	–	–	–	–	-2,580	55,815
10-Aug-04	7	20	6,085	20	6,085	4.50	–	–	–	–	–	-6,085	47,535
11-Aug-04	7	14	2,210	14	2,210	4.50	–	–	–	–	–	-2210	41,350
12-Aug-04	7	7	1,490	7	1,490	4.50	1	5000	1	5000	6.00	3510	32,105
13-Aug-04	7	11	3,320	11	3,320	4.50	–	–	–	–	–	-3320	32,665
16-Aug-04	7	15	6,740	15	6,740	4.50	–	–	–	–	–	-6740	#
16-Aug-04	1	38	17,855	38	17,855	4.50	–	–	–	–	–	-17,855	40,280

* : Working days, on which no bid was received under LAF auction, have been excluded. @ : Net of reverse repo. – : No repo/reverse repo.

\# : Outstanding amount is shown along with 1-day/7-day/14-day/28-day repo.

Note : 1. The revised LAF scheme was operationalised with effect from March 29, 2004, through (i) 7-day fixed rate repo conducted daily and (ii) overnight fixed rate reverse repo conducted daily on weekdays.

2. Overnight fixed rate repo at 4.50 per cent was reintroduced under LAF effective August 16, 2004.

APPENDIX TABLE V.2 : ISSUE OF CERTIFICATES OF DEPOSIT BY SCHEDULED COMMERCIAL BANKS

(Amount in Rupees crore)

Fortnight ended	Total Outstanding	Rate of Discount @ (Per cent)	Fortnight ended	Total Outstanding	Rate of Discount @ (Per cent)	Fortnight ended	Total Outstanding	Rate of Discount @ (Per cent)	Fortnight ended	Total Outstanding	Rate of Discount @ (Per cent)
1	2	3	4	5	6	7	8	9	10	11	12
2001			**2002**			**2003**			**2004**		
January 12	1,180	7.25-11.00	January 11	775	6.20-9.50	January 10	1,199	4.37-6.61	January 9	4,457	3.87-6.00
26	1,197	7.25-10.75	25	1,008	5.99-9.60	24	1,226	4.60-7.00	23	4,419	3.57-6.11
February 9	1,153	7.25-11.00	February 8	1,196	6.00-9.50	February 7	1,214	4.75-6.50	February 6	4,826	3.92-5.06
23	1,187	6.75-12.0	22	1,292	5.95-10.15	21	1,125	3.00-7.50	20	4,656	3.75-6.00
March 9	1,060	7.25-11.00	March 8	1,503	5.95-10.00	March 7	928	5.25-7.10	March 5	4,831	3.59-5.75
23	771	5.50-11.00	22	1,576	5.00-10.03	21	908	5.00-7.10	19	4,461	3.87-5.16
April 6	1,061	6.50-11.00	April 5	1,474	5.00-10.88	April 4	891	5.25-7.40	April 2	4,626	3.75-5.16
20	905	7.00-11.00	19	1,393	5.00-10.28	18	1,485	5.25-7.40	16	4,813	4.64-6.00
May 4	1,011	5.00-10.80	May 3	1,247	5.00-10.28	May 2	1,660	5.00-6.26	30	4,725	3.50-4.45
18	935	6.30-11.50	17	1,362	5.00-9.50	16	1,946	5.25-6.25	May 14	4,703	4.08-4.61
June 1	960	6.80-10.50	31	1,360	6.00-8.90	30	1,996	3.94-7.00	28	4,860	1.09-4.73
15	979	5.00-10.00	June 14	1,357	5.00-10.00	June 13	2,227	3.99-7.00	June 11	5,065	4.70-5.00
29	921	6.80-10.25	28	1,359	5.40-9.20	27	2,183	3.74-6.50	25	5,438	3.96-6.75
July 13	782	5.00-10.50	July 12	1,312	5.21-9.10	July 11	2,242	4.45-6.25			
27	751	6.00-10.00	26	1,303	5.10-8.50	25	2,466	5.25-6.75			
August 10	786	6.00-10.50	August 9	1,161	4.99-8.50	August 8	2,741	4.25-6.75			
24	757	5.00-10.00	23	1,007	5.03-8.50	22	2,961	4.75-5.68			
September 7	729	6.00-10.00	September 6	1,249	5.00-8.50	September 5	3,024	4.50-5.61			
21	736	6.33-9.50	20	1,236	5.50-8.75	19	3,098	4.25-6.00			
October 5	825	6.00-9.50	October 4	1,270	5.20-8.25	October 3	3,154	3.75-6.75			
19	786	6.20-9.75	18	1,394	4.94-8.00	17	3,243	4.50-7.00			
November 2	766	6.44-9.40	November 1	1,310	6.00-7.50	31	3,321	4.25-6.50			
16	791	6.40-9.40	15	1,309	4.69-8.50	November 14	3,511	4.50-7.00			
30	876	6.33-9.30	29	1,219	4.46-7.05	28	3,666	3.75-6.10			
December 14	798	5.00-9.50	December 13	1,204	4.69-8.50	December 12	3,643	4.00-6.00			
28	839	5.00-9.20	27	1,163	4.71-6.50	26	3,830	3.75-6.00			

@ : Effective discount rate range per annum.

APPENDIX TABLE V.3 : COMMERCIAL PAPER*

(Amount in Rupees crore)

Fortnight ended		Total Outstanding	Typical Effective Rates of Discount (Per cent)	Fortnight ended		Total Outstanding	Typical Effective Rates of Discount (Per cent)
1		2	3	4		5	6
2002							
January	15	8,644	7.40 - 9.75	May	15	6,396	5.05 - 8.50
	31	8,822	7.35 - 9.80		31	6,820	5.00 - 9.88
February	15	8,494	7.10 - 9.81	June	15	6,854	5.00 - 8.00
	28	8,402	7.20 - 10.00		30	7,108	5.20 - 7.40
March	15	8,273	7.15 - 10.35	July	15	7,069	5.15 - 6.80
	31	7,224	7.41 - 10.25		31	7,557	4.99 - 8.25
April	15	7,783	7.60 - 11.10	August	15	7,488	5.10 - 8.25
	30	8,046	7.60 - 9.60		31	7,646	5.00 - 6.65
May	15	8,080	7.54 - 10.10	September	15	7,212	4.69 - 6.60
	31	8,111	7.70 - 10.00		30	7,258	4.74 - 6.50
June	15	8,293	7.65 - 10.25	October	15	6,974	4.75 - 7.75
	30	8,447	7.67 - 9.75		31	6,845	4.89 - 8.00
July	15	7,709	6.90 - 9.50	November	15	7,230	4.81 - 6.00
	31	8,520	6.55 - 9.30		30	7,956	4.70 - 6.04
August	15	9,148	6.30 - 8.75	December	15	8,444	4.66 - 6.50
	31	9,125	5.72 - 8.50		31	8,762	4.64 - 6.75
September	15	9,374	6.05 - 9.71	**2004**			
	30	9,549	6.05 - 8.10	January	15	9,525	4.63 - 6.00
October	15	8,589	6.13 - 8.25		31	9,562	4.70 - 5.75
	31	8,426	6.07 - 8.35	February	15	9,355	4.73 - 6.75
November	15	8,606	5.79 - 8.00		29	9,379	4.60 - 7.50
	30	8,599	5.70 - 8.50	March	15	9,342	4.81 - 5.90
December	15	9,006	5.50 - 8.45		31	9,131	4.70 - 6.50
	31	9,025	5.50 - 8.25	April	15	9,590	4.66 - 6.20
2003					30	9,706	4.50 - 6.50
January	15	8,645	5.70 - 7.50	May	15	10,322	4.47 - 5.95
	31	8,554	5.60 - 8.05		31	10,328	4.56 - 7.00
February	15	8,173	5.58 - 9.86	June	15	10,354	4.50 - 6.05
	28	7,070	5.82 - 9.50		30	10,910	4.60 - 6.20
March	15	6,573	5.60 - 8.20	July	15	10,688	4.63 - 7.00
	31	5,749	6.00 - 7.75		31	10,848	4.61 - 5.60
April	15	5,839	5.25 - 8.15				
	30	5,994	5.05 - 9.85				

***** : Issued at face value by companies.

APPENDIX TABLE V.4 : INTER-BANK AND MERCHANT TRANSACTIONS IN THE FOREIGN EXCHANGE MARKET

(US $ million)

Month	Inter-bank							Merchant						
	Spot			Forward/Swap				Spot			Forward			
	Purchases	Sales	Net	Purchases	Sales	Net	Turnover	Purchases	Sales	Net	Purchases	Sales	Net	Turnover
1	2	3	4	5	6	7	8	9	10	11	12	13	14	15
2003														
April	11,993	13,001	-1,008	22,073	21,602	471	89,363	6,896	6,384	512	3,402	2,536	866	24,992
May	15,834	17,688	-1,854	29,125	28,621	504	113,246	7,574	6,752	822	5,187	3,364	1,823	29,067
June	19,528	19,773	-245	26,227	26,405	-178	122,571	9,012	8,269	743	4,943	3,647	1,296	35,697
July	22,213	24,793	-2,580	29,145	28,156	989	136,155	9,517	8,221	1,296	6,053	2,923	3,130	37,358
August	18,992	20,733	-1,741	24,666	25,845	-1,179	119,662	9,316	7,727	1,589	4,876	2,870	2,006	32,982
September	21,436	21,397	39	34,140	33,383	757	144,095	10,153	9,396	757	6,009	3,761	2,248	40,601
October	25,927	29,149	-3,222	38,681	35,795	2,886	168,790	11,936	9,902	2,034	7,646	4,197	3,449	46,407
November	20,667	21,919	-1,252	28,582	27,098	1,484	129,098	9,952	7,969	1,983	6,784	4,407	2,377	41,487
December	20,482	22,249	-1,767	28,969	27,449	1,520	136,554	12,792	10,686	2,106	5,550	4,260	1,290	46,525
2004														
January	21,737	23,779	-2,042	33,458	32,444	1,014	153,424	12,716	11,208	1,508	6,468	4,406	2,062	49,797
February	17,147	18,398	-1,251	28,776	26,061	2,715	129,069	11,145	9,634	1,511	5,139	3,711	1,428	43,837
March	29,099	31,327	-2,228	32,916	31,788	1,128	168,370	15,865	13,173	2,692	7,628	5,933	1,695	56,574
April P	29,964	33,828	-3,864	45,245	42,479	2,766	192,240	12,224	10,588	1,636	10,609	6,281	4,328	52,431
May P	29,808	28,600	1,208	43,655	42,263	1,392	178,934	11,111	10,957	154	8,428	6,669	1,759	49,994
June P	28,651	27,414	1,237	37,320	38,051	-731	170,307	12,612	12,258	354	5,900	6,722	-822	51,768
July P	29,276	27,796	-1,749	34,537	36,154	-1,617	169,052	12,051	11,937	114	5,851	6,201	-350	50,404

P : Provisional.

Note : 1. Merchant turnover includes cross-currency (*i.e.,* foreign currency to foreign currency, both spot and forward) transactions and cancellation of forward contracts.
2. Inter-bank turnover includes cross-currency (*i.e.,* foreign currency to foreign currency, both spot and forward) transactions .

APPENDIX TABLE V.5 : A PROFILE OF CENTRAL GOVERNMENT DATED SECURITIES

(Amount in Rupees crore)

Item	2003-04	2002-03	2001-02
1	2	3	4
1. Gross Borrowing	1,21,500	1,25,000	1,14,213
2. Repayment	32,693	27,420	26,499
3. Net Borrowing	88,807	97,580	87,714
4. Weighted Average Maturity (in years)	14.94	13.83	14.26
5. Weighted Average Yield (per cent)	5.71	7.34	9.44
6. A. Maturity Distribution - Amount			
(a) Up to 5 Years	6,500	–	2,000
(b) Above 5 and up to 10 Years	22,000	45,500	16,000
(c) Above 10 Years	93,000	79,500	96,213
Total	1,21,500	125,000	114,213
B. Maturity Distribution (per cent)			
(a) Up to 5 Years	5	–	2
(b) Above 5 and up to 10 Years	18	36	14
(c) Above 10 Years	77	64	84
Total	100	100	100
7. Price Based Auctions - Amount	74,000	56,000	53,000
8. Yield - Per cent			
(a) Minimum	4.69 (4 years)	6.05 (12 years, 8 months)	6.98 (FRB, 8 years)
(b) Maximum	6.35 (18 years, 11 months)	8.62 (24 years, 3 months)	11.00 (19 years, 8 months)
9. Yield (per cent) - Maturity Distribution - wise			
(a) Less than 10 Years			
Minimum	4.62 (9 years)	6.57 (8 years)	6.98 (8 years)
Maximum	5.76 (8 years, 10 months)	7.72 (9 years,11 months)	9.81 (7 years, 4 months)
(b) 10 Years			
Minimum	5.32	6.72	9.39
Maximum	5.32	8.14	9.39
(c) Above 10 Years			
Minimum	5.09 (FRB, 11 years)	6.05 (12 years, 8 months)	7.18 (14 years, 11 months)
Maximum	6.33 (29 years, 4 months)	8.62 (24 years, 3 months)	11.00 (19 years, 8 months)
Memo Item :			
1. Initial Subscription by the Reserve Bank*	21,500	36,175	28,892
2. Open Market Operations by the Reserve Bank - Net Sales*	41,849	53,780	30,335
3. Monetised Deficit*	-76,065	-28,399	-5,150
4. Ways and Means Advances to the Centre (Outstanding on March 31)	Nil	Nil	5,176

* : Financial year variation. FRB : Floating Rate Bond.

Note : Figures in parentheses represent residual maturity in years.

APPENDIX TABLE V.6 : SECONDARY MARKET TRANSACTIONS IN GOVERNMENT SECURITIES

(Amount in Rupees crore)

Item	Transaction in Government Securities															
	2003-04												2004-05			
	April	May	June	July	August	September	October	November	December	January	February	March	April	May	June	July
1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	16	17
I. OUTRIGHT TRANSACTIONS																
1. Central Government Securities	1,13,401 (90.50)	1,49,966 (95.13)	1,50,252 (94.52)	1,52,294 (92.65)	2,04,769 (94.04)	1,32,924 (90.40)	1,94,984 (94.52)	88,531 (90.61)	90,996 (89.96)	90,810 (90.88)	69,565 (87.86)	1,11,343 (87.77)	1,50,432 (90.62)	96,132 (82.85)	87,901 (80.00)	65,200 (74.77)
2. State Government Securities	555 (0.44)	919 (0.58)	1,535 (0.97)	943 (0.57)	1,921 (0.88)	1,435 (0.98)	1,521 (0.73)	620 (0.63)	1,385 (1.37)	1,077 (1.08)	1,319 (1.67)	2,870 (2.27)	1,216 (0.73)	1,649 (1.42)	3,033 (2.76)	2,526 (2.90)
3. Treasury Bills (a+b)	11,354 (9.06)	9,756 (4.29)	7,182 (4.52)	11,146 (6.78)	11,059 (5.08)	12,685 (8.63)	9,782 (4.74)	8,549 (8.75)	8,772 (8.67)	8,032 (8.04)	8,295 (10.48)	12,639 (9.96)	14,350 (8.64)	18,251 (15.73)	18,937 (17.24)	19,471 (22.33)
(a) 91-days	3,667 (2.93)	5,012 (1.28)	2,861 (1.80)	5,322 (3.24)	6,220 (2.86)	7,068 (4.81)	4,297 (2.08)	3,915 (4.01)	3,662 (3.62)	3,274 (3.28)	3,390 (4.28)	3,652 (2.88)	7,533 (4.54)	11,146 (9.61)	10,092 (9.19)	12,973 (14.88)
(b) 364-days	7,687 (6.13)	4,744 (3.01)	4,321 (2.72)	5,824 (3.54)	4,839 (2.22)	5,617 (3.82)	5,485 (2.66)	4,635 (4.74)	5,110 (5.05)	4,758 (4.76)	4,905 (6.19)	8,987 (7.08)	6,817 (4.11)	7,105 (6.12)	8,845 (8.05)	6,498 (7.45)
Total (1+2+3)	1,25,310 (100.00)	1,60,641 (100.00)	1,58,969 (100.00)	1,64,383 (100.00)	2,17,750 (100.00)	1,47,044 (100.00)	2,06,287 (100.00)	97,701 (100.00)	1,01,153 (100.00)	99,918 (100.00)	79,179 (100.00)	1,26,852 (100.00)	1,65,998 (100.00)	1,16,032 (100.00)	1,09,870 (100.00)	87,196 (100.00)
II. REPO TRANSACTIONS																
1. Central Government Securities	35,101 (83.94)	37,624 (86.84)	40,807 (83.96)	67,383 (89.92)	65,604 (88.84)	62,476 (89.88)	82,463 (92.19)	92,426 (95.46)	94,770 (94.51)	1,14,135 (95.47)	89,515 (97.42)	1,01,273 (97.68)	1,05,184 (92.30)	1,03,794 (84.06)	1,10,165 (83.85)	1,11,987 (75.16)
2. State Government Securities	0 (0.00)	99 (0.23)	0 (0.00)	0 (0.00)	597 (0.81)	1,521 (2.19)	2,107 (2.36)	1,405 (1.45)	1,370 (1.37)	877 (0.73)	1,186 (1.29)	601 (0.58)	1,028 (0.90)	1,638 (1.33)	1,063 (0.81)	1,637 (1.10)
3. Treasury Bills (a+b)	6,714 (16.06)	5,605 (12.94)	7,798 (16.04)	7,553 (10.08)	7,643 (10.35)	5,516 (7.93)	4,882 (5.46)	2,993 (3.09)	5,135 (4.12)	4,542 (3.80)	1,188 (1.29)	1,803 (1.74)	7,753 (6.80)	18,041 (14.61)	20,152 (15.34)	35,377 (23.74)
(a) 91-days	214 (0.51)	520 (1.20)	744 (1.53)	1,219 (1.63)	3,566 (4.83)	2,639 (3.80)	1,876 (2.10)	819 (0.85)	1,434 (1.43)	382 (0.32)	254 (0.28)	586 (0.57)	1,774 (1.56)	8,405 (6.81)	11,892 (9.05)	20,483 (13.75)
(b) 364-days	6,500 (15.54)	5,085 (11.74)	7,054 (14.51)	6,334 (8.42)	4,078 (5.52)	2,877 (4.14)	3,005 (3.36)	2,174 (2.25)	2,700 (2.69)	4,160 (3.48)	934 (1.02)	1,217 (1.17)	5,980 (5.25)	9,636 (7.80)	8,260 (6.29)	14,894 (10.00)
Total (1+2+3)	41,815 (100.00)	43,328 (100.00)	48,605 (100.00)	74,936 (100.00)	73,844 (100.00)	69,512 (100.00)	89,452 (100.00)	96,824 (100.00)	1,01,275 (100.00)	1,19,553 (100.00)	91,889 (100.00)	1,03,677 (100.00)	1,13,966 (100.00)	1,23,472 (100.00)	1,31,380 (100.00)	1,49,000 (100.00)
III. GRAND TOTAL (I+II)	167,125	2,03,969	2,07,574	2,39,319	2,91,594	2,16,556	2,95,739	1,94,525	2,02,428	2,19,472	1,71,068	2,30,528	2,79,964	2,39,504	2,41,250	2,36,196
I as percentage of III	74.98	78.76	76.58	68.69	74.68	67.90	69.75	50.23	49.97	45.53	46.29	55.03	59.29	48.45	45.54	36.92
II as percentage of III	25.02	21.24	23.42	31.31	25.32	32.10	30.25	49.77	50.03	54.47	53.71	44.97	40.71	51.55	54.46	63.08

Note : 1. Figures in parentheses indicate percentages to total outright / repo transactions.
2. Repo transactions exclude second leg of transactions.

APPENDIX TABLE V.7 : ISSUES OF CENTRAL GOVERNMENT DATED SECURITIES

(Amount in Rupees crore)

Issue / Auction Particulars						Bids/Application Received				Bids / Application Accepted							Gross Amount Raised (15+16+17)	Cut-off Price (Rs.) / Yield (%)
Nomenclature of loan	Date of Auction	Date of Issue	Tenor (Years)	Re-sidual Matu-rity (Years)	Notified Amount	Competitive		Non-Competitive		Competitive		Non-Competitive		Allocation to				
						Num-ber	Face Value	Number ++	Face Value	Number	Face Value	Number ++	Face Value	Others (12+14)	PDs @@	RBI @@/P		
1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	16	17	18	19
2003-04																		
7.37% GS 2014 + **	08-Apr-03	09-Apr-03	12	11.02	5000.00	236	7926.00	24	60.20	201	4939.81	24	60.20	5000.00	–	–	5000.00	111.11/5.9787
6.30% GS 2023 # **	08-Apr-03	09-Apr-03	20	20.00	4000.00	245	10413.00	25	147.31	65	3852.69	25	147.31	4000.00	–	–	4000.00	6.30
6.25% GS 2018 + **	22-Apr-03	23-Apr-03	15	14.69	5000.00	319	9655.25	26	101.93	134	4898.07	26	101.93	5000.00	–	–	5000.00	101.40/6.1032
7.95% GS 2032 + **	22-Apr-03	23-Apr-03	30	29.35	2000.00	131	4472.75	19	60.65	9	1939.35	19	60.65	2000.00	–	–	2000.00	121.51/6.3274
6.25% GS 2018 + P	–	23-Apr-03	15	14.69	3000.00	–	–	–	–	–	–	–	–	–	–	3000	3000.00	101.40/6.1032
7.95% GS 2032 + P	–	23-Apr-03	30	29.35	2000.00	–	–	–	–	–	–	–	–	–	–	2000	2000.00	121.51/6.3274
7.27% GS 2013 + **	03-May-03	05-May-03	11	10.33	6000.00	314	12468.70	14	30.90	98	5969.10	14	30.90	6000.00	–	–	6000.00	109.92/5.9679
6.30% GS 2023 + **	03-May-03	05-May-03	20	18.93	3000.00	143	4158.75	14	41.55	118	2958.45	14	41.55	3000.00	–	–	3000.00	99.45/6.3485
GOI FRB 2014	19-May-03	20-May-03	11	11.00	5000.00	110	8710.00	2	0.80	55	4999.20	2	0.80	5000.00	–	–	5000.00	0.14 @
																		100/5.09% for first 1 yr
6.85% GS 2012 + **	03-Jun-03	04-Jun-03	10	8.84	6000.00	378	13026.00	21	91.30	151	5908.70	21	91.30	6000.00	–	–	6000.00	107.48/5.7566
6.13% GS 2028 # **	03-Jun-03	04-Jun-03	25	25.00	3000.00	187	7886.00	19	214.32	15	2850.00	19	150.00	3000.00	–	–	3000.00	6.13
7.37% GS 2014 + **	01-Jul-03	02-Jul-03	12	10.79	5000.00	298	12800.00	20	95.42	116	4904.58	20	95.42	5000.00	–	–	5000.00	112.80/5.7590
6.05% GS 2019 + **	01-Jul-03	02-Jul-03	16	15.94	4000.00	279	9055.80	22	178.09	94	3821.91	22	178.09	4000.00	–	–	4000.00	100.90/5.9613
6.13% GS 2028 + **	01-Jul-03	02-Jul-03	25	24.92	3000.00	114	5379.75	20	136.14	45	2863.86	20	136.14	3000.00	–	–	3000.00	100.39/6.0989
6.35% GS 2020 + **	15-Jul-03	16-Jul-03	17	16.46	6000.00	371	15722.50	29	309.94	115	5700.00	29	300.00	6000.00	–	–	6000.00	103.92/5.9723
7.95% GS 2032 + **	15-Jul-03	16-Jul-03	30	29.12	3000.00	134	5234.75	22	68.19	12	2931.81	22	68.19	3000.00	–	–	3000.00	123.38/6.2041
6.65% GS 2009 *	–	22-Jul-03	7	5.70	–	–	–	–	–	–	–	–	–	–	–	–	2886.80	106.25
6.72% GS 2014 *	–	22-Jul-03	11	10.59	–	–	–	–	–	–	–	–	–	–	–	–	5773.60	107.64
7.46% GS 2017 *	–	22-Jul-03	15	14.10	–	–	–	–	–	–	–	–	–	–	–	–	2886.80	114.13
6.25% GS 2018 *	–	22-Jul-03	15	14.44	–	–	–	–	–	–	–	–	–	–	–	–	2886.80	103.14
GOI FRB 2011	07-Aug-03	8-Aug-03	8	8.00	6000.00	115	13145.00	10	19.40	54	5980.60	10	19.40	6000.00	–	–	6000.00	0.13 @
																		100/5.03% for first 1 yr
6.01% GS 2028 # **	07-Aug-03	8-Aug-03 ##	25	24.64	3000.00	176	7476.26	27	243.32	79	2850.00	27	150.00	3000.00	–	–	3000.00	6.01
6.17% GS 2023 + **	03-Sep-03	04-Sep-03	20	19.77	6000.00	317	10651.50	25	215.88	149	5784.12	25	215.88	6000.00	–	–	6000.00	101.92/6.0019
5.69% GS 2018 + **	21-Oct-03	22-Oct-03	15	14.93	5000.00	335	11448.42	24	350.94	85	4750.00	24	250.00	5000.00	–	–	5000.00	103.51/5.3452
GOI FRB 2012	07-Nov-03	10-Nov-03	9	9.00	5000.00	85	10930.00	4	9.00	29	4991.00	4	9.00	5000.00	–	–	5000.00	0.09 @
																		100/4.62% for first 1 yr
6.01% GS 2028 + **	04-Dec-03	05-Dec-03	25	24.31	5000.00	169	8233.50	16	58.28	118	4941.73	16	58.28	5000.00	–	–	5000.00	96.90/6.2590
4.69% GS 2008 P	–	02-Jan-04	4	4.00	6500.00	–	–	–	–	–	–	–	–	–	–	6500	6500.00	100.00/4.69
5.64% GS 2019 P	–	02-Jan-04	15	15.00	3000.00	–	–	–	–	–	–	–	–	–	–	3000	3000.00	100.00/5.64
7.38% GS 2015 + **	06-Jan-04	07-Jan-04	13	11.66	5000.00	288	14009.00	16	68.22	77	4931.78	16	68.22	5000.00	–	–	5000.00	119.15/5.1708
5.64% GS 2019 + P	–	30-Jan-04	15	14.92	2000.00	–	–	–	–	–	–	–	–	–	–	2000	2000.00	98.69/5.7716
5.32% GS 2014 P	–	16-Feb-04	10	10.00	5000.00	–	–	–	–	–	–	–	–	–	–	5000	5000.00	100.00/5.32
5.64% GS 2019 + **	26-Feb-04	27-Feb-04	15	14.85	5000.00	276	8487.00	12	40.20	149	4959.80	12	40.20	5000.00	–	–	5000.00	98.32/5.8096
2004-05																		
6.01% GS 2028 + **	06-May-04	07-May-04	25	23.88	3000.00	173	6791.00	14	55.08	16	2944.92	14	55.08	3000.00	–	–	3000.00	102.78/5.7930
GOI FRB 2016	06-May-04	07-May-04	12	12.00	6000.00	127	17140.00	3	10.40	18	5989.60	3	10.40	6000.00	–	–	6000.00	0.04 @
																		100/4.49% for first 1 yr
5.59% GS 2016 # **	03-June-04	04-June-04	12	12.00	6000.00	243	11834.00	10	33.49	87	5966.51	10	33.49	6000.00	–	–	6000.00	5.59
6.01% GS 2028 + **	03-June-04	04-June-04	25	23.81	4000.00	178	7344.00	14	47.54	41	3952.46	14	47.54	4000.00	–	–	4000.00	97.22/6.2348
7.38% GS 2015 + **	17-June-04	18-June-04	13	11.21	6000.00	261	10785.00	10	15.19	145	5984.81	10	15.19	6000.00	–	–	6000.00	114.80/5.5842
6.13% GS 2028 + **	17-June-04	18-June-04	25	23.96	3000.00	180	5982.50	13	51.00	134	2949.00	13	51.00	3000.00	–	–	3000.00	98.03/6.2900
GOI FRB 2015	01-July-04	02-July-04	11	11.00	6000.00	94	8730.00	3	3.20	76	5996.80	3	3.20	6000.00	–	–	6000.00	0.19 @100/4.71% for first 1 yr
6.13% GS 2028 + **	01-July-04	02-July-04	25	23.92	2000.00	62	3033.00	9	15.72	35	1984.28	9	15.72	2000.00	–	–	2000.00	93.20/6.7039
7.50% GS 2034 # U	09-Aug-04	10-Aug-04	30	30.00	2000.00	24	2463.00	6	8.97	16	1991.03	6	8.97	2000.00	–	–	2000.00	7.50
GOI FRB 2015 (II)	09-Aug-04	10-Aug-04	11	11.00	6000.00	106	7205.00	4	7.71	93	5405.00	4	7.71	5412.71	370.00	217.29	6000.00	0.50@100/5.12% for first 1 yr

@ : Mark-up (spread) over the base rate.
* : Securities reissued under the debt buy-back scheme.
\+ : Reissues.
** : Allotment to Non-Competitive bidders at weighted average yield/price of competitive bids.
P : Private Placement with the Reserve Bank.
: Notional commencement date of tenure of the stock is March 25, 2003.
\# : Yield Based Auction.
U : Uniform Price Auction.
++ : Number of applicants.
@@: Devolvement.

Note : Excluding issuances under the Market Stabilisation Scheme (MSS) introduced since April 2004.

APPENDIX TABLE V.8 : PROFILE OF TREASURY BILLS

(Amount in Rupees crore)

Item		2003-04	2002-03	2001-02	2000-01
1		2	3	4	5
1. Implicit Yield at Cut-off Price (per cent)					
14-day Treasury Bills					
	Minimum	–	–	6.78	6.26
	Maximum	–	–	7.56	10.97
	Average	–	–	7.13	8.23
91-day Treasury Bills					
	Minimum	4.16	5.10	6.05	7.91
	Maximum	5.47	7.00	8.50	10.47
	Average	4.59	5.73	6.88	8.98
182-day Treasury Bills					
	Minimum	–	–	8.33	8.42
	Maximum	–	–	8.57	10.42
	Average	–	–	8.44	9.43
364-day Treasury Bills					
	Minimum	4.31	5.35	6.16	8.66
	Maximum	5.50	6.98	8.85	10.91
	Average	4.67	5.93	7.30	9.76
2. Gross Issues					
14-day Treasury Bills		–	–	1,100	10,480
91-day Treasury Bills		36,786	26,402	20,216	7,255
182-day Treasury Bills		–	–	300	2,600
364-day Treasury Bills		26,136	26,126	19,588	15,000
3. Net Issues					
14-day Treasury Bills		–	–	-300	-25
91-day Treasury Bills		2,488	4,626	3,171	310
182-day Treasury Bills		–	–	-1,300	–
364-day Treasury Bills		9	6,538	4,588	2,000
4. Outstanding at Period End					
14-day Treasury Bills		–	–	–	300
91-day Treasury Bills		7,139	9,627	5,001	1,830
182-day Treasury Bills		–	–	–	1,300
364-day Treasury Bills		26,136	26,126	19,588	15,000

– : Not applicable.

Note : 1. Auction of 14-day and 182-day Treasury Bills were discontinued from the week beginning May 14, 2001.

2. Non-competitive bids allowed to certain entities such as State Governments result in the difference between notified amount and actual amounts issued and outstanding.

APPENDIX TABLE V.9 : NEW CAPITAL ISSUES BY NON-GOVERNMENT PUBLIC LIMITED COMPANIES

(Amount in Rupees crore)

Security and Type of Issue	2003-04P		2002-03P		2001-02	
	No. of Issues	Amount	No. of Issues	Amount	No. of Issues	Amount
1	2	3	4	5	6	7
1) Equity Shares (a+b)	**24**	**1,958.7**	**5**	**460.2**	**6**	**860.2**
	(17)	**(1,240.3)**	**(5)**	**(391.3)**	**(3)**	**(654.3)**
a) Prospectus	13	1,464.3	3	206.7	4	852.5
	(9)	(1,087.4)	(3)	(201.0)	(2)	(653.7)
b) Rights	11	494.4	2	253.5	2	7.7
	(8)	(152.9)	(2)	(190.3)	(1)	(0.6)
2) Preference Shares (a+b)	**–**	**–**	**–**	**–**	**–**	**–**
a) Prospectus	–	–	–	–	–	–
b) Rights	–	–	–	–	–	–
3) Debentures (a+b)	**–**	**–**	**1**	**217.5**	**4**	**774.0**
a) Prospectus	–	–	–	–	1	69.5
b) Rights	–	–	1	217.5	3	704.5
of which:						
i) Convertible (a+b)	–	–	1	217.5	3	518.1
a) Prospectus	–	–	–	–	1	69.5
b) Rights	–	–	1	217.5	2	448.6
ii) Non-Convertible (a+b)	–	–	–	–	1	255.9
a) Prospectus	–	–	–	–	–	–
b) Rights	–	–	–	–	1	255.9
4) Bonds (a+b)	**3**	**1,250.9**	**3**	**1,200.0**	**9**	**4,058.0**
a) Prospectus	3	1,250.9	3	1,200.0	9	4,058.0
b) Rights	–	–	–	–	–	–
5) Total (1+2+3+4)	**27**	**3,209.6**	**9**	**1,877.7**	**19**	**5,692.2**
a) Prospectus	16	2,715.2	6	1,406.7	14	4,980.0
b) Rights	11	494.4	3	471.0	5	712.2

– : Nil/Negligible. P : Provisional.

Note :
1. Data exclude bonus shares, offers for sale and private placement.
2. Figures in parentheses refer to premium amount on capital issues. These are included in respective totals.
3. Preference shares include cumulative convertible preference shares and equi-preference shares.
4. Convertible debentures include partly convertible debentures.
5. Non-convertible debentures include secured premium notes and secured deep discount bonds.
6. Data are compiled from prospectus /circulars/advertisements issued by companies, replies given by the companies to the Reserve Bank's questionnaires, information received from stock exchanges, press reports, *etc.*

APPENDIX TABLE V.10 : ASSISTANCE SANCTIONED AND DISBURSED BY FINANCIAL INSTITUTIONS

(Rupees crore)

Institution	2003-04 P		2002-03 P		2001-02	
	Sanctions	Disbursements	Sanctions	Disbursements	Sanctions	Disbursements
1	2	3	4	5	6	7
A. All India Development Banks (1 to 6)	**23,408 (756)**	**14,057 (527)**	**22,272 (878)**	**17,225 (668)**	**63,848 (461)**	**46,556 (451)**
1. IDBI	5,631 (–)	4,409 (–)	5,898 (–)	6,615 (–)	13,505 (285)	11,151 (302)
2. IFCI	1,392	278	1,960	1,780	760	1,079
3. IDFC	5,727	2,704	2,304	949	3,008	1,506
4 ICICI *	–	–	–	–	36,229	25,831
5. SIDBI	8,246 (756)	4,414 (527)	10,904 (878)	6,789 (668)	9,026 (177)	5,919 (149)
6. IIBI	2,412	2,252	1,207	1,092	1,321	1,070
B. Specialised Financial Institutions (7 to 9)	**485**	**441**	**476**	**491**	**873**	**869**
7. IVCF	–	–	2	2	3	4
8. ICICI Venture	380	361	390	394	774	778
9. TFCI	105	80	84	95	96	87
C. Investment Institutions (10 to 12)	**23,705**	**17,402**	**5,965**	**7,903**	**9,364**	**11,668**
10. LIC	21,974	15,782	4,333	6,206	6,742	8,914
11. UTI #	–	–	307	415	991	1,270
12. GIC @	1,731	1,620	1,325	1,282	1,631	1,484
D. Total Assistance by All-India Financial Institutions (AIFIs) [A+B+C]	**47,598**	**31,900**	**28,713**	**25,619**	**74,085**	**59,093**
E. State-level Institutions (13 and 14)	**1,134**	**857**	**2,780**	**2,704**	**3,804**	**3,468**
13. SFCs	1,134	857	1,856	1,454	2,210	1,750
14. SIDCs	n.a.	n.a.	924	1,250	1,594	1,718
F. Total Assistance by All Financial Institutions (AFIs) [D+E]	**48,732**	**32,757**	**31,493**	**28,323**	**77,889**	**62,561**

P : Provisional. n.a. : Not available. – : Nil/Negligible.

* : Since ICICI Ltd. was merged with ICICI Bank Ltd. effective March 30, 2002 ICICI Ltd. has ceased to exist. Data for ICICI Ltd. are, therefore, available only for the year 2001-02.

: Data for 2002-03 relate to the period April-October 2002 only.

@ : Data include GIC and its former subsidiaries.

Note : Data in parentheses for IDBI and SIDBI pertain to refinance to State Financial Corporations (SFCs)/State Industrial Development Corporations (SIDCs), seed capital as also loans to and subscription to shares and bonds of financial institutions and are excluded from the total.

Source : 1) Respective financial institutions.
2) IDBI for GIC and its former subsidiaries and SIDCs.
3) SIDBI for SFCs.

APPENDIX TABLE V.11: TRENDS IN DOMESTIC STOCK INDICES

Month/Year	BSE Sensex (Base: 1978-79=100)				S&P CNX Nifty (Base: 03.11.1995 = 1000)			
	Average	High	Low	End of the Year/Month	Average	High	Low	End of the Year/Month
1	2	3	4	5	6	7	8	9
Financial Year								
2001-02	**3332 (-22.0)**	**3742**	**2600**	**3469**	**1077 (-19.3)**	**1198**	**854**	**1130**
2002-03	**3206 (-3.8)**	**3513**	**2834**	**3049**	**1037 (-3.7)**	**1147**	**923**	**978**
2003-04	**4492 (40.1)**	**6194**	**2924**	**5591**	**1428 (37.6)**	**1982**	**924**	**1772**
2003								
April	3037	3215	2924	2960	965	1032	924	934
May	3033	3181	2943	3181	963	1007	936	1007
June	3387	3607	3182	3607	1069	1134	1011	1134
July	3665	3793	3554	3793	1150	1186	1109	1186
August	3978	4245	3742	4245	1261	1357	1171	1357
September	4315	4453	4134	4453	1369	1417	1302	1417
October	4742	4931	4455	4907	1506	1569	1421	1556
November	4951	5098	4771	5045	1580	1619	1522	1615
December	5425	5839	5132	5839	1740	1880	1646	1880
2004								
January	5954	6194	5594	5696	1906	1982	1771	1810
February	5827	6036	5567	5668	1849	1920	1766	1800
March	5613	5935	5365	5591	1780	1885	1685	1772
April	5809	5926	5655	5655	1848	1892	1796	1796
May	5205	5757	4505	4760	1640	1833	1389	1484
June	4824	4964	4644	4795	1506	1551	1446	1506
July	4973	5170	4844	5170	1568	1632	1518	1632

Note : Figures in parentheses are percentage variations over the previous year.

Source : The Stock Exchange, Mumbai (BSE) and the National Stock Exchange of India Ltd. (NSE).

APPENDIX TABLE V.12 : MAJOR INDICATORS OF DOMESTIC EQUITY MARKETS

Year/Month	The Stock Exchange, Mumbai (BSE)					National Stock Exchange of India Ltd. (NSE)				
	Coefficient of Variation @	Dispersion (Range) @	Price/ Earning Ratio #	Market Capitalisation (Rupees crore)	Turnover (Rupees crore)	Coefficient of Variation@	Dispersion (Range) @	Price/ Earning Ratio #	Market Capitalisation (Rupees crore)	Turnover (Rupees crore)
1	2	3	4	5	6	7	8	9	10	11
Financial Year										
2001-02	**7.2**	**1141.95**	**16.55**	**6,12,224**	**3,07,292**	**6.80**	**344.25**	**15.72**	**6,36,861**	**5,13,167**
2002-03	**4.8**	**679.14**	**14.51**	**5,72,198**	**3,14,073**	**5.20**	**223.80**	**15.24**	**5,37,133**	**6,17,989**
2003-04	**23.0**	**3270.08**	**16.19**	**12,01,207**	**5,02,620**	**23.30**	**1057.85**	**16.11**	**11,20,976**	**10,99,535**
2003										
April	3.0	291.21	13.21	5,72,526	20,823	3.6	107.20	13.20	5,30,630	48,971
May	2.2	237.97	13.21	6,60,982	22,510	2.1	70.80	11.15	6,12,030	54,690
June	3.6	425.16	14.61	7,34,389	24,933	3.3	123.50	12.20	6,78,550	61,586
July	1.8	238.48	14.73	7,75,996	32,976	1.8	76.65	12.50	7,19,145	78,878
August	3.8	503.07	15.33	9,05,193	36,334	4.3	185.50	13.89	8,36,651	85,347
September	2.1	319.09	15.76	9,33,087	44,698	2.5	115.00	15.08	8,63,481	1,03,345
October	2.4	475.45	17.07	10,00,494	52,631	2.4	148.60	16.64	9,26,748	1,15,595
November	1.9	326.61	16.28	10,65,853	45,029	1.8	96.40	17.42	9,79,541	92,886
December	4.1	707.42	17.30	12,73,361	54,816	4.4	233.95	19.19	11,67,029	1,10,373
2004										
January	2.5	600.37	19.39	12,06,854	65,620	3.0	211.65	21.02	11,16,150	1,34,269
February	2.6	468.68	18.71	11,96,221	51,464	2.7	154.30	20.32	11,10,954	1,08,718
March	3.2	569.79	18.55	12,01,207	50,786	3.6	200.25	20.78	11,20,976	1,04,877
April	1.3	270.49	19.31	12,55,347	44,864	1.4	96.35	19.92	11,71,828	1,00,951
May	6.6	1252.14	17.28	10,23,129	45,938	7.5	444.05	14.86	9,50,494	98,920
June	1.8	319.75	14.76	10,47,258	36,990	1.8	104.45	12.18	9,79,700	84,898
July	1.9	326.55	14.82 P	11,35,589 P	39,449 P	2.1	114.15	13.08	10,66,087	93,836

@ : Based on BSE Sensex and S&P CNX Nifty, respectively.
\# : Based on scrips included in the BSE Sensex and the S&P CNX Nifty, respectively.
P : Provisional.
Source : The Stock Exchange, Mumbai (BSE) and the National Stock Exchange of India Ltd. (NSE).

APPENDIX TABLE V.13 : TURNOVER IN THE EQUITY DERIVATIVES MARKET

(Rupees crore)

Month/Year	The Stock Exchange, Mumbai (BSE)				National Stock Exchange of India Ltd. (NSE)				
	Index Futures	Index Options #	Stock Futures	Stock Options #	Index Futures	Index Options #	Stock Futures	Stock Options #	Interest Rate Futures
1	2	3	4	5	6	7	8	9	10
2001-02	**1,276.30**	**78.30**	**451.60**	**115.51**	**21,482**	**3,766**	**51,516**	**25,163**	**–**
2002-03	**1,810.99**	**1.98**	**644.30**	**21.17**	**43,952**	**9,247**	**2,86,532**	**1,00,133**	**–**
2003-04	**6,571.52**	**0.03**	**5,171.05**	**331.61**	**5,54,446**	**52,816**	**13,05,939**	**2,17,207**	**202**
2002									
April	1.11	0.61	21.49	0.55	1,656	382	15,065	4,570	–
May	9.90	0.03	104.70	0.32	2,022	463	15,981	5,133	–
June	12.31	0.00	90.36	0.43	2,123	389	16,178	4,642	–
July	0.89	0.00	77.38	0.40	2,513	511	21,205	6,178	–
August	0.02	0.00	43.93	0.46	2,978	518	17,881	5,562	–
September	0.09	0.00	18.10	1.99	2,836	583	17,501	6,221	–
October	0.00	0.00	13.85	0.15	3,145	727	21,213	8,357	–
November	0.00	0.00	13.15	0.10	3,500	845	25,463	10,028	–
December	0.00	0.00	15.51	0.45	5,958	1,088	35,532	13,043	–
2003									
January	546.57	0.00	100.26	0.27	5,557	940	38,299	14,353	–
February	589.42	0.03	89.70	5.68	5,040	946	32,445	10,964	–
March	650.68	1.31	55.87	10.37	6,624	1,856	29,770	11,082	–
April	64.77	0.00	20.77	1.80	6,993	1,707	29,749	11,569	–
May	8.13	0.03	10.46	4.33	6,283	1,617	32,752	12,772	–
June	0.59	0.00	6.08	2.54	9,348	1,941	46,505	15,041	182
July	50.80	0.00	48.90	3.40	14,743	3,204	70,515	21,370	19
August	302.50	0.00	206.30	0.10	24,989	3,839	91,288	20,247	1
September	407.90	0.00	441.50	1.50	45,861	5,012	1,13,874	20,402	0
October	419.60	0.00	435.10	2.70	56,433	4,570	1,46,378	22,977	0
November	449.60	0.00	477.60	1.50	49,486	3,847	1,22,463	16,375	0
December	1,785.00	0.00	1,844.00	54.90	65,376	5,454	1,50,930	17,139	0
2004									
January	2,213.19	0.00	1,498.44	75.32	99,872	6,913	1,95,784	21,485	0
February	555.06	0.00	78.65	96.19	86,356	6,543	1,61,461	18,472	0
March	314.38	0.00	103.25	87.33	88,706	8,169	1,44,240	19,358	0
April	76.01	0.00	8.78	0.00	79,555	7,315	1,21,044	12,376	0
May	0.00	0.00	38.77	0.00	82,149	10,292	92,629	9,690	0
June	0.00	0.00	0.00	0.00	64,018	8,473	78,392	7,423	0
July	n.a.	n.a.	n.a.	n.a.	61,124	9,912	94,009	10,293	0

: Notional turnover including call and put options.
– : Not applicable. n.a. : Not available.
Source : The Stock Exchange, Mumbai (BSE) and the National Stock Exchange of India Ltd. (NSE).

APPENDIX TABLE VI.1 : SELECT ECONOMIC INDICATORS - WORLD

Item	2005 +	2004 +	2003	2002	2001	2000	1999	1998
1	2	3	4	5	6	7	8	9
I. World Output (Per cent Change)	4.4	4.6	3.9	3.0	2.4	4.7	3.7	2.8
i) Advanced economies	3.1	3.5	2.1	1.7	1.1	3.8	3.5	2.7
ii) Emerging market and developing countries**	5.9	6.0	6.1	4.6	4.1	5.9	4.0	3.0
a) Developing Asia	7.0	7.4	7.8	6.4	5.6	6.7	6.2	4.1
b) Africa	5.4	4.2	4.1	3.5	3.8	3.0	2.7	3.2
c) Middle East	5.0	4.1	5.4	4.2	4.3	5.9	2.1	4.0
d) Western Hemisphere	3.7	3.9	1.7	-0.1	0.4	3.9	0.4	2.3
II. Inflation-CPI (Per cent Change)								
i) Advanced economies	1.7	1.7	1.8	1.5	2.1	2.1	1.4	1.5
ii) Emerging market and developing countries	5.0	5.7	6.1	6.0	6.8	7.3	10.4	11.4
of which : Developing Asia	3.6	4.0	2.7	2.0	2.7	1.9	2.5	7.8
III. Fiscal Balance #								
i) Advanced economies	-2.6	-3.2	-3.3	-2.5	-1.0	0.2	-1.1	-1.0
ii) Other emerging market and developing countries (weighted average)	-2.5	-2.7	-3.0	-3.5	-3.2	-3.0	-3.8	-3.8
IV. Net Capital Flows* (US $ billion)								
Emerging market and developing countries								
i) Net private capital flows (a+b+c)	100.9	162.9	131.2	47.0	20.6	42.2	86.6	77.4
a) Net private direct investment	143.3	135.5	119.3	139.3	189.1	175.0	171.2	153.0
b) Net private portfolio investment	-36.9	-43.9	-87.5	-98.6	-95.7	6.1	66.0	38.4
c) Net other private capital flows	-5.5	71.2	99.3	6.3	-72.8	-139.0	-150.6	-114.0
ii) Net official flows	-18.0	-20.0	-7.2	3.3	25.8	-14.5	6.4	47.3
V. World Trade @								
Imports								
i) Advanced economies	5.4	5.7	3.5	2.3	-0.8	11.6	8.2	5.9
ii) Newly industrialised Asian economies	7.9	9.4	8.9	7.9	-6.5	17.2	8.5	-8.6
Exports								
i) Advanced economies	6.1	6.3	2.7	1.9	-0.8	11.7	5.6	4.2
ii) Newly industrialised Asian economies	7.4	10.8	12.1	9.5	-4.4	16.9	9.4	1.1
Terms of Trade								
i) Advanced economies	-0.4	0.1	0.7	0.9	0.3	-2.4	-0.3	1.3
ii) Newly industrialised Asian economies	-0.4	-2.6	-1.4	0.1	-0.7	-3.2	-2.3	0.1
VI. Current Account Balance (US $ billion)								
i) Advanced economies	-191.7	-184.1	-241.9	-193.3	-206.7	-246.3	-102.2	38.1
ii) Emerging market and developing countries	39.6	85.4	121.0	83.6	37.9	88.1	-18.1	-115.0
of which : Developing Asia	53.1	51.1	61.8	68.1	38.1	45.4	48.1	48.9

+ : Projections.
# : Central Government fiscal balance as percentage of GDP.
* : Net capital flows comprise net direct investment, net portfolio investment and other long-term and short-term net investment flows, including official and private borrowings.
** : Excluding Hongkong SAR, Korea, Singapore, Taiwan province of China and Israel.
@ : Annual percentage change in world trade in volume of goods and services.

Source : World Economic Outlook, IMF, April 2004.

APPENDIX TABLE VI.2 : INDIA'S OVERALL BALANCE OF PAYMENTS

Item	Rupees Crore			US $ Million		
	2003-04	2002-03	2001-02	2003-04	2002-03	2001-02
1	2	3	4	5	6	7
A. Current Account						
1. Exports, f.o.b.	2,88,769	2,54,022	2,14,351	62,952	52,512	44,915
2. Imports, c.i.f.	3,65,641	3,16,450	2,74,778	79,658	65,422	57,618
3. Trade Balance	-76,872	-62,428	-60,427	-16,706	-12,910	-12,703
4. Invisibles, Net	1,16,510	82,415	64,161	25,425	17,047	13,485
a) 'Non-Factor' Services	48,878	32,671	21,960	10,684	6,765	4,577
of which: Software Services Exports	55,986	46,427	36,036	12,200	9,600	7,556
b) Income	-21,676	-23,871	-17,467	-4,703	-4,935	-3,601
c) Private Transfers	86,764	71,642	57,821	18,885	14,807	12,125
d) Official Transfers	2,544	1,973	1,847	559	410	384
5. Current Account Balance	39,638	19,987	3,734	8,719	4,137	782
B. Capital Account						
1. Foreign Investment, Net (a+b)	66,299	21,918	31,877	14,492	4,555	6,692
a. Direct Investment *of which :*	14,404	17,412	22,588	3,137	3,611	4,741
i. In India	21,463	22,575	29,192	4,675	4,660	6,131
Equity	*10,949*	*13,091*	*18,658*	*2,387*	*2,700*	*4,095*
Re-invested earnings	*8,271*	*7,250*	*8,710*	*1,800*	*1,498*	*1,646*
Other Capital	*2,243*	*2,234*	*1,824*	*488*	*462*	*390*
ii. Abroad	-7,059	-5,163	-6,604	-1,538	-1,049	-1,390
Equity	*-1,289*	*-2,051*	*-2,701*	*-282*	*-424*	*-570*
Re-invested earnings	*-5,403*	*-2,600*	*-3,329*	*-1,176*	*-519*	*-699*
Other Capital	*-367*	*-512*	*-574*	*-80*	*-106*	*-121*
b. Portfolio Investment	51,895	4,506	9,289	11,355	944	1,951
In India	51,998	4,679	9,617	11,377	979	2,020
Abroad	-103	-173	-328	-22	-35	-69
2. External Assistance, Net	-12,179	-11,745	5,418	-2,661	-2,460	1,117
Disbursements	15,375	13,392	16,073	3,374	2,773	3,352
Amortisation	-27,554	-25,137	-10,655	-6,035	-5,233	-2,235
3. Commercial Borrowings	-8,439	-11,370	-7,476	-1,853	-2,344	-1,576
Disbursements	28,577	13,678	12,896	6,253	2,833	2,696
Amortisation	-37,016	-25,048	-20,372	-8,106	-5,177	-4,272
4. Short Term Credit, Net	7,318	4,715	-4,236	1,560	979	-891
5. Banking Capital	28,491	40,612	26,671	6,197	8,412	5,592
of which : NRI Deposits, Net	16,800	14,414	13,127	3,628	2,976	2,754
6. Rupee Debt Service	-1,758	-2,303	-2,458	-376	-474	-519
7. Other Capital, Net @	21,881	16,679	793	4,763	3,445	158
8. Total Capital Account	1,01,613	58,506	50,589	22,122	12,113	10,573
C. Errors & Omissions	2,674	3,523	2,269	580	730	402
D. Overall Balance [A(5)+B(8)+C]	**1,43,925**	**82,016**	**56,592**	**31,421**	**16,980**	**11,757**
E. Monetary Movements (F+G)	-1,43,925	-82,016	-56,592	-31,421	-16,980	-11,757
F. IMF, Net	0	0	0	0	0	0
G. Reserves and Monetary Gold [Increase (-), Decrease (+)]	**-1,43,925**	**-82,016**	**-56,592**	**-31,421**	**-16,980**	**-11,757**

@ : Includes delayed export receipts and advance payments against imports.

Note : 1. Gold and silver brought by the Indians returning from abroad have been included under imports, with a *contra* entry in private transfer receipts.

2. Data on exports and imports differ from those given by DGCI&S on account of differences in coverage, valuation and timing.

APPENDIX TABLE VI.3 : INDIA'S FOREIGN TRADE

	Item	Rupees crore			US $ million			SDR million		
		April-March			April-March			April-March		
		2003-04P	2002-03	2001-02	2003-04P	2002-03	2001-02	2003-04P	2002-03	2001-02
	1	2	3	4	5	6	7	8	9	10
I.	**Exports (a+b)**	**2,91,582**	**2,55,137**	**2,09,018**	**63,454**	**52,719**	**43,827**	**44391**	**39,785**	**34,712**
		(14.3)	(22.1)	(2.7)	(20.4)	(20.3)	(-1.6)	(11.6)	(14.6)	(1.5)
	a. Petroleum, oil and lubricants (POL)	16,168	12,469	10,107	3,518	2,577	2,119	2,461	1,944	1,678
		(29.7)	(23.4)	(16.9)	(36.6)	(21.6)	(12.0)	(26.6)	(15.8)	(15.6)
	b. Non-oil	2,75,414	2,42,668	1,98,911	59,936	50,143	41,708	41,930	37,841	33,034
		(13.5)	(22.0)	(2.0)	(19.5)	(20.2)	(-2.3)	(10.8)	(14.6)	(0.9)
II.	**Imports (a+b)**	**3,53,976**	**2,97,206**	**2,45,200**	**77,032**	**61,412**	**51,413**	**53,890**	**46,345**	**40,721**
		(19.1)	(21.2)	(6.2)	(25.4)	(19.4)	(1.7)	(16.3)	(13.8)	(5.0)
	a. Oil and POL	94,520	85,367	66,770	20,569	17,640	14,000	14,390	13,312	11,089
		(10.7)	(27.9)	(-6.6)	(16.6)	(26.0)	(-10.5)	(8.1)	(20.0)	(-7.6)
	b. Non-oil	2,59,456	2,11,839	1,78,430	56,463	43,773	37,413	39,500	33,033	29,632
		(22.5)	(18.7)	(12.0)	(29.0)	(17.0)	(7.2)	(19.6)	(11.5)	(10.7)
III.	**Trade Balance (I-II)**	**-62,394**	**-42,069**	**-36,182**	**-13,578**	**-8,693**	**-7,587**	**-9,499**	**-6,560**	**-6,009**
	a. Oil Balance (I.a – II.a)	-78,352	-72,898	-56,663	-17,051	-15,063	-11,881	-11,929	-11,367	-9,410
	b. Non-oil Balance (I.b – II.b)	15,958	30,829	20,482	3,473	6,370	4,295	-2,430	4,807	3,401

P : Provisional.

Note : Figures in parentheses are percentage variations over the previous year.

Source : DGCI & S.

APPENDIX TABLE VI.4 : INDIA'S EXPORTS OF PRINCIPAL COMMODITIES

Commodity Group	Rupees crore					US $ million				
				Percentage Variation					Percentage Variation	
	2003-04P	2002-03	2001-02	2003-04P over 2002-03	2002-03 over 2001-02	2003-04P	2002-03	2001-02	2003-04P over 2002-03	2002-03 over 2001-02
1	2	3	4	5	6	7	8	9	10	11
I. Primary Products	**44,786**	**42,133**	**34,165**	**6.3**	**23.3**	**9,746**	**8,706**	**7,164**	**11.9**	**21.5**
	(15.4)	**(16.5)**	**(16.3)**			**(15.4)**	**(16.5)**	**(16.3)**		
A. Agricultural and Allied Products	**34,030**	**32,473**	**28,144**	**4.8**	**15.4**	**7,406**	**6,710**	**5,901**	**10.4**	**13.7**
	(11.7)	**(12.7)**	**(13.5)**			**(11.7)**	**(12.7)**	**(13.5)**		
of which :										
1. Tea	1,595	1,652	1,719	-3.5	-3.9	347	341	360	1.7	-5.3
2. Coffee	1,082	994	1,095	8.9	-9.2	236	205	230	14.7	-10.5
3. Rice	4,133	5,831	3,174	-29.1	83.7	899	1,205	666	-25.4	81.0
4. Oil Meal	3,272	1,487	2,263	120.0	-34.3	712	307	474	131.7	-35.2
5. Marine Products	6,068	6,928	5,898	-12.4	17.5	1,320	1,432	1,237	-7.8	15.8
B. Ores and Minerals	**10,756**	**9,660**	**6,021**	**11.3**	**60.4**	**2,341**	**1,996**	**1,262**	**17.3**	**58.1**
	(3.7)	(3.8)	(2.9)			(3.7)	(3.8)	(2.9)		
II. Manufactured Goods	**2,18,802**	**1,94,765**	**1,59,146**	**12.3**	**22.4**	**47,616**	**40,245**	**33,370**	**18.3**	**20.6**
	(75.0)	(76.3)	(76.1)			(75.0)	(76.3)	(76.1)		
of which :										
A. Leather and Manufactures	**9,307**	**8,945**	**9,110**	**4.0**	**-1.8**	**2,025**	**1,848**	**1,910**	**9.6**	**-3.2**
	(3.2)	(3.5)	(4.4)			(3.2)	(3.5)	(4.4)		
B. Chemicals and Related Products	**42,405**	**36,080**	**28,862**	**17.5**	**25.0**	**9,228**	**7,455**	**6,052**	**23.8**	**23.2**
	(14.5)	(14.1)	(13.8)			(14.5)	(14.1)	(13.8)		
1. Basic Chemicals, Pharmaceuticals and Cosmetics	25,792	22,545	17,632	14.4	27.9	5,613	4,658	3,697	20.5	26.0
2. Plastic and Linoleum	7,992	5,912	4,709	35.2	25.6	1,739	1,222	987	42.4	23.7
3. Rubber, Glass, Paints and Enamels, *etc.*	6,817	5,799	4,695	17.6	23.5	1,483	1,198	984	23.8	21.7
4. Residual Chemicals and Allied Products	1,805	1,824	1,826	-1.1	-0.1	393	377	383	4.2	-1.6
C. Engineering Goods	**56,121**	**43,715**	**33,183**	**28.4**	**31.7**	**12,213**	**9,033**	**6,958**	**35.2**	**29.8**
	(19.2)	(17.1)	(15.9)			(19.2)	(17.1)	(15.9)		
D. Textiles	**54,727**	**53,407**	**46,094**	**2.5**	**15.9**	**11,910**	**11,036**	**9,665**	**7.9**	**14.2**
	(18.8)	(20.9)	(22.1)			(18.8)	(20.9)	(22.1)		
of which :										
1. Cotton Yarn, Fabrics, Made-ups, *etc.*	15,276	16,217	14,655	-5.8	10.7	3,324	3,351	3,073	-0.8	9.1
2. Readymade garments	27,977	27,536	23,878	1.6	15.3	6,088	5,690	5,007	7.0	13.6
3. Manmade yarn, fabrics, made-ups, *etc.*	8,075	6,639	5,079	21.6	30.7	1,757	1,372	1,065	28.1	28.8
E. Gems and Jewellery	**48,294**	**43,701**	**34,845**	**10.5**	**25.4**	**10,510**	**9,030**	**7,306**	**16.4**	**23.6**
	(16.6)	(17.1)	(16.7)			(16.6)	(17.1)	(16.7)		
F. Handicrafts	**2,032**	**3,801**	**2,618**	**-46.5**	**45.2**	**442**	**785**	**549**	**-43.7**	**43.1**
	(0.7)	(1.5)	(1.3)			(0.7)	(1.5)	(1.3)		
G. Carpets	**2,617**	**2,578**	**2,433**	**1.5**	**5.9**	**569**	**533**	**510**	**6.9**	**4.4**
	(0.9)	(1.0)	(1.2)			(0.9)	(1.0)	(1.2)		
1. Handmade	2,495	1,941	1,788	28.6	8.6	543	401	375	35.4	7.0
2. Millmade	–	541	473	–	14.2	–	112	99	–	12.5
3. Silk	122	96	172	26.5	-44.2	26	20	36	33.3	-45.0
III. Petroleum, Crude and Products	**16,168**	**12,469**	**10,107**	**29.7**	**23.4**	**3,518**	**2,577**	**2,119**	**36.6**	**21.6**
	(5.5)	(4.9)	(4.8)			(5.5)	(4.9)	(4.8)		
IV. Others	**11,826**	**5,770**	**5,600**	**105.0**	**3.0**	**2,574**	**1,191**	**1,174**	**115.9**	**1.5**
	(4.1)	(2.3)	(2.7)			(4.1)	(2.3)	(2.7)		
V. Total Exports (I+II+III+IV)	**2,91,582**	**2,55,137**	**2,09,018**	**14.3**	**22.1**	**63,454**	**52,719**	**43,827**	**20.4**	**20.3**

P : Provisional.

Note : 1. Figures in parentheses represent percentages to total exports.

2. Leather and manufactures include finished leather, leather goods, leather garments, footwear of leather and its components and saddlery and harness.

3. Engineering goods comprise ferro alloys, aluminium other than products, non-ferrous metal, manufactures of metals, machine tools, machinery and equipments, transport equipments, residual engineering items, iron and steel bar/rod *etc.*, primary and semi-finished iron and steel, electronic goods, computer software and project goods.

4. Textiles include readymade garments, cotton yarn, fabric made-ups *etc.,* man-made textiles made-ups *etc.*, natural silk textiles, wool and woolen manufactures, coir and coir manufactures and jute manufactures.

Source : DGCI & S.

APPENDIX TABLE VI.5 : INDIA'S IMPORTS OF PRINCIPAL COMMODITIES

Commodity Group	Rupees crore					US $ million				
				Percentage Variation					Percentage Variation	
	2003-04P	2002-03	2001-02	2003-04P over 2002-03	2002-03 over 2001-02	2003-04P	2002-03	2001-02	2003-04P over 2002-03	2002-03 over 2001-02
1	2	3	4	5	6	7	8	9	10	11
I. Bulk Imports	**1,34,964 (38.1)**	**1,17,598 (39.6)**	**96,638 (39.4)**	**14.8**	**21.7**	**29,371 (38.1)**	**24,300 (39.6)**	**20,263 (39.4)**	**20.9**	**19.9**
A. Petroleum, Petroleum Products and Related Material	**94,520 (26.7)**	**85,367 (28.7)**	**66,770 (27.2)**	**10.7**	**27.9**	**20,569 (26.7)**	**17,640 (28.7)**	**14,000 (27.2)**	**16.6**	**26.0**
B. Bulk Consumption Goods	**14,057 (4.0)**	**11,668 (3.9)**	**9,745 (4.0)**	**20.5**	**19.7**	**3,059 (4.0)**	**2,411 (3.9)**	**2,043 (4.0)**	**26.9**	**18.0**
1. Cereals and Cereal Preparations	88	119	87	-25.7	36.6	19	24	18	-21.7	34.6
2. Edible Oil	11,674	8,780	6,465	33.0	35.8	2,541	1,814	1,356	40.0	33.8
3. Pulses	2,251	2,737	3,160	-17.8	-13.4	490	566	663	-13.4	-14.6
4. Sugar	43	33	33	31.0	0.3	9	7	7	37.9	-1.2
C. Other Bulk Items	**26,387 (7.5)**	**20,563 (6.9)**	**20,124 (8.2)**	**28.3**	**2.2**	**5,742 (7.5)**	**4,249 (6.9)**	**4,220 (8.2)**	**35.1**	**0.7**
1. Fertilisers	3,303	3,028	3,238	9.1	-6.5	719	626	679	14.9	-7.8
a) Crude	615	894	796	-31.2	12.4	134	185	167	-27.6	10.8
b) Sulphur and unroasted iron pyrites	396	403	274	-1.8	47.1	86	83	57	3.5	46.2
c) Manufactured	2,292	1,731	2,169	32.4	-20.2	499	358	455	39.5	-21.4
2. Non-ferrous Metals	4,331	3,226	3,087	34.3	4.5	942	667	647	41.4	3.0
3. Paper, Paper board and manufactured including Newsprint	2,950	2,175	2,131	35.6	2.1	642	449	447	42.8	0.6
4. Crude Rubber, including Synthetic and Reclaimed	1,287	883	831	45.7	6.2	280	182	174	53.5	4.7
5. Pulp and Waste Paper	1,877	1,662	1,405	12.9	18.3	408	343	295	18.9	16.5
6. Metalliferrous Ores and Metal Scrap	5,746	5,022	5,455	14.4	-7.9	1,251	1,038	1,144	20.5	-9.3
7. Iron and Steel	6,893	4,567	3,976	50.9	14.9	1,500	944	834	59.0	13.2
II. Non-Bulk Imports	**2,19,012 (61.9)**	**1,79,608 (60.4)**	**1,48,561 (60.6)**	**21.9**	**20.9**	**47,661 (61.9)**	**37,113 (60.4)**	**31,150 (60.6)**	**28.4**	**19.1**
A. Capital Goods	**78,722 (22.2)**	**65,325 (22.0)**	**47,130 (19.2)**	**20.5**	**38.6**	**17,132 (22.2)**	**13,498 (22.0)**	**9,882 (19.2)**	**26.9**	**36.6**
1. Manufactures of Metals	3,158	2,363	1,941	33.6	21.7	687	488	407	40.7	20.0
2. Machine Tools	2,112	1,195	921	76.7	29.8	460	247	193	86.1	27.9
3. Machinery except Electrical and Electronics	21,701	17,256	14,169	25.8	21.8	4,723	3,566	2,971	32.4	20.0
4. Electrical Machinery except Electronics	3,970	3,214	2,835	23.5	13.4	864	664	594	30.1	11.7
5. Electronic Goods incl. Computer Software	36,192	29,488	19,070	22.7	54.6	7,876	6,093	3,999	29.3	52.4
6. Transport Equipments	9,845	9,183	5,482	7.2	67.5	2,142	1,897	1,149	12.9	65.1
7. Project Goods	1,745	2,626	2,714	-33.6	-3.2	380	543	569	-30.0	-4.6
B. Mainly Export Related Items	**58,352 (16.5)**	**49,914 (16.8)**	**39,394 (16.1)**	**16.9**	**26.7**	**12,699 (16.5)**	**10,314 (16.8)**	**8,260 (16.1)**	**23.1**	**24.9**
1. Pearls, Precious and Semi-precious Stones	32,756	29,341	22,046	11.6	33.1	7,128	6,063	4,623	17.6	31.2
2. Chemicals, Organic and Inorganic	18,483	14,640	13,352	26.2	9.7	4,022	3,025	2,800	33.0	8.1
3. Textile Yarn, Fabrics, *etc.*	5,741	4,696	3,565	22.3	31.7	1,249	970	747	28.8	29.8
4. Cashew Nuts, Raw	1,372	1,236	431	11.0	186.8	299	255	90	16.9	182.6
C. Others	**81,938 (23.2)**	**64,369 (21.7)**	**62,037 (25.3)**	**27.3**	**3.8**	**17,831 (23.1)**	**13,301 (21.7)**	**13,008 (25.3)**	**34.1**	**2.3**
of which :										
1. Gold and Silver	31,327	20,753	21,854	50.9	-5.0	6,817	4,288	4,582	59.0	-6.4
2. Artificial Resins and Plastic Materials	4,963	3,784	3,215	31.2	17.7	1,080	782	674	38.1	16.0
3. Professional, Scientific and Optical Goods	5,636	5,484	4,965	2.8	10.5	1,226	1,133	1,041	8.2	8.8
4. Coal, Coke and Briquittes *etc.*	6,479	5,999	5,453	8.0	10.0	1,410	1,240	1,143	13.7	8.4
5. Medicinal and Pharmaceutical Products	2,956	2,865	2,027	3.2	41.4	643	592	425	8.6	39.3
6. Chemical Materials and Products	2,899	2,187	2,120	32.5	3.2	631	452	444	39.6	1.7
7. Non-Metallic Mineral Manufactures	1,500	1,136	1,049	32.1	8.3	326	235	220	39.1	6.7
III. Total Imports (I+II)	**3,53,976**	**2,97,206**	**2,45,200**	**19.1**	**21.2**	**77,032**	**61,412**	**51,413**	**25.4**	**19.4**

P : Provisional.

Note : Figures in parentheses represent percentages to total imports.

Source : DGCI & S.

APPENDIX TABLE VI.6 : INVISIBLES BY CATEGORY OF TRANSACTIONS

Item	Rupees Crore			US $ Million		
	2003-04	2002-03	2001-02	2003-04	2002-03	2001-02
1	2	3	4	5	6	7
I. Non Factor Services, Net	**48,878**	**32,671**	**21,960**	**10,684**	**6,765**	**4,577**
Receipts	1,26,297	1,20,736	98,559	27,616	24,963	20,665
Payments	77,419	88,065	76,599	16,932	18,198	16,088
Travel, Net	1,948	-2,120	3,011	434	-438	628
Receipts	18,058	14,641	13,880	3,945	3,029	2,910
Payments	16,110	16,761	10,869	3,511	3,467	2,282
Transportation, Net	3,988	-120	-1,936	869	-23	-413
Receipts	14,474	12,216	9,410	3,200	2,524	1,969
Payments	10,486	12,336	11,346	2,331	2,547	2,382
Insurance, Net	250	266	71	56	54	13
Receipts	1,921	1,777	1,279	419	368	267
Payments	1,671	1,511	1,208	363	314	254
G.N.I.E., Net	137	378	942	31	79	197
Receipts	1,110	1,486	2,235	243	307	469
Payments	973	1,108	1,293	212	228	272
Miscellaneous, Net	42,555	34,267	19,872	9,294	7,093	4,152
Receipts	90,734	90,616	71,755	19,809	18,735	15,050
Payments	48,179	56,349	51,883	10,515	11,642	10,898
of which:						
Software Services, Net	53,458	42,855	32,834	11,650	8,863	6,884
Receipts	55,986	46,427	36,036	12,200	9,600	7,556
Payments	2,528	3,572	3,202	550	737	672
II. Income, Net	**-21,676**	**-23,871**	**-17,467**	**-4,703**	**-4,935**	**-3,601**
Receipts	20,782	13,685	17,316	4,529	2,826	3,448
Payments	42,458	37,556	34,783	9,232	7,761	7,049
III. Private Transfers, Net	**86,764**	**71,642**	**57,821**	**18,885**	**14,807**	**12,125**
Receipts	88,367	73,415	58,136	19,235	15,174	12,192
Payments	1,603	1,773	315	350	367	67
IV. Official Transfers, Net	**2,544**	**1,973**	**1,847**	**559**	**410**	**384**
Receipts	2,548	1,977	1,851	559	410	385
Payments	4	4	4	0	0	1
V. Invisibles, Net (I to IV)	**1,16,510**	**82,415**	**64,161**	**25,425**	**17,047**	**13,485**
Receipts	2,37,994	2,09,813	1,75,862	51,939	43,373	36,690
Payments	1,21,484	1,27,398	1,11,701	26,514	26,326	23,205

GNIE : Government, Not Included Elsewhere.

APPENDIX TABLE VI.7 : COMPOSITION OF CAPITAL INFLOWS

Item	2003-04	2002-03	2001-02	2000-01	1999-00	1998-99	1997-98	1996-97	1995-96	1990-91
1	2	3	4	5	6	7	8	9	10	11
Total Capital Inflows(Net)	**22,122**	**12,113**	**10,573**	**10,018**	**10,444**	**8,435**	**9,844**	**12,006**	**4,089**	**7,056**
(in US $ Million)										
Of which :	(in per cent)									
1. Non- Debt Creating Inflows	**72.5**	**46.6**	**77.1**	**67.8**	**49.7**	**28.6**	**54.8**	**51.3**	**117.5**	**1.5**
a) Foreign Direct Investment*	21.1	38.5	58.0	40.2	20.7	29.4	36.2	23.7	52.4	1.4
b) Portfolio Investment	51.4	8.1	19.1	27.6	29.0	-0.8	18.6	27.6	65.1	0.1
2. Debt Creating Inflows	**1.4**	**-10.7**	**9.2**	**59.4**	**23.1**	**54.4**	**52.4**	**61.7**	**57.7**	**83.3**
a) External Assistance	-12.0	-20.0	11.4	4.3	8.6	9.7	9.2	9.2	21.6	31.3
b) External Commercial Borrowings #	-8.4	-19.4	-14.9	37.2	3.0	51.7	40.6	23.7	31.2	31.9
c) Short-term Credits	7.1	8.1	-8.4	1.0	3.6	-8.9	-1.0	7.0	1.2	15.2
d) NRI Deposits **	16.4	24.6	26.0	23.1	14.7	11.4	11.4	27.9	27.0	21.8
e) Rupee Debt Service	-1.7	-3.9	-4.9	-6.2	-6.8	-9.5	-7.8	-6.1	-23.3	-16.9
3. Other Capital @	**26.1**	**64.1**	**13.7**	**-27.2**	**27.2**	**17.0**	**-7.2**	**-13.0**	**-75.2**	**15.2**
4. Total (1 to 3)	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**

* : Data on FDI have been revised since 2000-01 with expanded coverage to approach international best practices. As such data from 2000-01 onwards are not comparable with those of earlier years.
\# : Refers to medium and long-term borrowings.
** : Including NR (NR) Rupee Deposits.
@ : Including leads and lags in exports (difference between the custom and the banking channel data), Banking Capital (assets and liabilities of banks excluding NRI deposits), loans to Non-residents by residents, Indian investment abroad, India's subscription to International Institutions and quota payments to the IMF.

APPENDIX TABLE VI.8 : EXTERNAL ASSISTANCE

Item	Rupees crore			US $ million		
	2003-04P	2002-03R	2001-02R	2003-04P	2002-03R	2001-02R
1	2	3	4	5	6	7
1 Loans	15,241	13,871	16,112	3,409	2,866	3,306
2. Grants	2,072	1,839	1,448	464	380	297
3. Gross Utilisation (1+2)	17,313	15,710	17,560	3,873	3,246	3,603
4. Repayments	27,752	28,976	10,705	6,200	6,091	2,194
5. Interest Payments	3,560	4,606	5,256	795	968	1,077
6. Net (3-4-5)	-13,999	-17,872	1,599	-3,122	-3,813	332

P : Provisional. R : Revised.

Note : 1. Loans are inclusive of non-government loans but exclusive of suppliers' credits and commercial borrowings.
2. Grants are exclusive of PL 480-II grants including non-government technical grants.
3. Repayments include amortisation of civilian debt owed to Russia and hence do not tally with the data given in Appendix Table VI.2

Source : Controller of Aid, Accounts and Audit, Government of India.

APPENDIX TABLE VI.9 : INDIA'S FOREIGN EXCHANGE RESERVES

End of Month	Foreign Exchange Reserves (Rupees crore)					Foreign Exchange Reserves (US $ million)					Total Foreign Exchange Reserves (in SDR million)	Movement in Foreign Exchange Reserves (in SDR million)@
	SDRs	Gold *	Foreign Currency Assets	Reserve Tranche Position in IMF	Total (2+3+ 4+5)	SDRs	Gold*	Foreign Currency Assets	Reserve Tranche Position in IMF	Total (7+8+ 9+10)		
1	2	3	4	5	6	7	8	9	10	11	12	13
March 1994	339	12,794	47,287	938	61,358	108	4,078	15,068	299	19,553	13,841 (11,367)	6,595 (6,140)
March 1995	23	13,752	66,005	1,050	80,830	7	4,370	20,809	331	25,517	16,352 (13,998)	2,511 (2,631)
March 1996	280	15,658	58,446	1,063	75,447	82	4,561	17,044	310	21,997	15,054 (12,379)	-1,298 -(1,619)
March 1997	7	14,557	80,368	1,046	95,978	2	4,054	22,367	291	26,714	19,272 (16,796)	4,218 (4,416)
March 1998	4	13,394	1,02,507	1,117	1,17,022	1	3,391	25,975	283	29,650	22,200 (20,108)	2,929 (3,312)
March 1999	34	12,559	1,25,412	2,816	1,40,821	8	2,960	29,522	663	33,153	24,413 (22,635)	2,213 (2,527)
March 2000	16	12,973	1,52,924	2,870	1,68,783	4	2,974	35,058	658	38,694	28,728 (26,923)	4,315 (4,288)
March 2001	11	12,711	1,84,482	2,873	2,00,077	2	2,725	39,554	616	42,897	34,034 (32,276)	5,306 (5,353)
March 2002	50	14,868	2,49,118	2,977	2,67,013	10	3,047	51,049	610	54,716	43,876 (41,836)	9,842 (9,561)
June 2002	47	16,272	2,67,333	3,177	2,86,829	10	3,330	54,703	650	58,693	44,114 (42,014)	238 (178)
September 2002	48	15,964	2,88,648	3,130	3,07,790	10	3,300	59,663	647	63,620	48,098 (46,006)	4,222 (4,170)
December 2002	33	16,542	3,21,774	3,194	3,41,543	7	3,444	66,994	665	71,110	52,496 (50,356)	8,620 (8,520)
March 2003	19	16,785	3,41,476	3,192	3,61,472	4	3,534	71,890	672	76,100	55,394 (53,225)	11,518 (11,389)
June 2003	6	17,182	3,65,001	4,535	3,86,724	1	3,698	78,546	976	83,221	59,407 (57,171)	4,013 (3,946)
September 2003	17	17,967	3,99,870	5,516	4,23,370	4	3,919	87,213	1,203	92,339	64,582 (62,244)	9,188 (9,019)
December 2003	13	19,225	4,45,232	6,002	4,70,472	3	4,215	97,617	1,316	1,03,151	69,417 (66,983)	14,022 (13,758)
March 2004	10	18,216	4,66,215	5,688	4,90,129	2	4,198	1,07,448	1,311	1,12,959	76,298 (73,866)	20,904 (20,641)
June 2004	8	18,655	5,24,865	5,980	5,49,508	2	4,057	1,14,151	1,301	1,19,511	81,509 (79,145)	5,211 (5,280)

* : Gold has been valued close to international market price.

@ : Variations over the previous March.

Note : 1. Gold holdings include acquisition of gold amounting to US $ 191 million from the Government during 1991-92, US $ 29.4 million during 1992-93, US $ 139.3 million during 1993-94, US $ 315.0 million during 1994-95 and US $ 17.9 million during 1995-96. On the other hand, 1.27 tonnes of gold amounting to Rs.43.55 crore (US $11.97 million), 38.9 tonnes of gold amounting to Rs.1485.22 crore (US $ 376.0 million) and 0.06 tonnes of gold amounting to Rs.2.13 crore (US $ 0.5 million) were repurchased by the Central Government on November 13, 1997, April 1, 1998 and October 5, 1998, respectively, for meeting its redemption obligation under the Gold Bond Scheme.

2. Conversion of foreign currency assets into US dollar was done at exchange rates supplied by the IMF up to March 1999. Effective April 1, 1999, the conversion is at New York closing exchange rate.

3. Figures in parentheses represent reserves adjusted for gold revaluation, pursuant to the practice of valuing gold reserves close to international market price, effective October 17, 1990.

APPENDIX TABLE VI.10 : INDIA'S EXTERNAL DEBT
(As at end-March)

Item	Rupees crore			US $ million		
	2004P	2003R	2002	2004P	2003R	2002
1	2	3	4	5	6	7
I. Multilateral	**1,28,662**	**1,42,680**	**1,55,633**	**29,614**	**29,994**	**31,899**
A. Government borrowing	1,16,493	1,29,727	1,38,023	26,814	27,271	28,290
i) Concessional	98,524	1,02,559	96,177	22,678	21,559	19,713
a) IDA	97,141	1,01,122	94,848	22,360	21,257	19,440
b) Others #	1,383	1,437	1,329	318	302	273
ii) Non-concessional	17,969	27,168	41,846	4,136	5,712	8,577
a) IBRD	13,634	19,069	28,012	3,138	4,009	5,742
b) Others ##	4,335	8,099	13,834	998	1,703	2,835
B. Non-Government borrowing	12,169	12,953	17,610	2,800	2,723	3,609
i) Concessional	0	0	0	0	0	0
ii) Non-concessional	12,169	12,953	17,610	2,800	2,723	3,609
a) Public sector	8,897	9,255	12,729	2,048	1,945	2,609
IBRD	5,482	4,378	7,298	1,262	920	1,496
Others ##	3,415	4,877	5,431	786	1,025	1,113
b) Financial institutions	2,814	3,177	3,736	647	668	766
IBRD	427	525	1,049	98	110	215
Others ##	2,387	2,652	2,687	549	558	551
c) Private sector	458	521	1,145	105	110	234
IBRD	258	298	929	59	63	190
Others	200	223	216	46	47	44
II. Bilateral	**75,981**	**79,983**	**74,762**	**17,489**	**16,814**	**15,323**
A. Government borrowing	56,423	60,243	56,302	12,987	12,664	11,540
i) Concessional	56,045	59,688	55,418	12,900	12,547	11,359
ii) Non-concessional	378	555	884	87	117	181
B. Non-Government borrowing	19,558	19,740	18,460	4,502	4,150	3,783
i) Concessional	8,750	8,013	6,885	2,014	1,684	1,411
a) Public sector	5,711	5,152	4,278	1,315	1,083	877
b) Financial institutions	3,039	2,861	2,607	699	601	534
c) Private sector	0	0	0	0	0	0
ii) Non-concessional	10,808	11,727	11,575	2,488	2,466	2,372
a) Public sector	5,273	5,183	4,822	1,214	1,090	988
b) Financial institutions	2,954	3,572	3,708	680	751	760
c) Private sector	2,581	2,972	3,045	594	625	624
III. International Monetary Fund	**0**	**0**	**0**	**0**	**0**	**0**
IV. Trade Credit	**19,933**	**23,649**	**26,110**	**4,588**	**4,974**	**5,368**
a) Buyers' credit	10,961	13,408	16,147	2,523	2,820	3,311
b) Suppliers' credit	4,097	5,051	5,144	943	1,063	1,069
c) Export credit component of bilateral credit	4,875	5,190	4,819	1,122	1,091	988
d) Export credit for defence purposes	0	0	0	0	0	0

APPENDIX TABLE VI.10 : INDIA'S EXTERNAL DEBT *(Concld.)*

(As at end-March)

Item	Rupees crore			US $ million		
	2004P	2003R	2002	2004P	2003R	2002
1	2	3	4	5	6	7
V. Commercial Borrowing	**96,823**	**1,07,165**	**1,13,451**	**22,286**	**22,540**	**23,226**
a) Commercial bank loans	50,705	47,062	48,682	11,671	9,898	9,962
b) Securitised borrowings* (including FCCBs)	42,191	57,696	62,258	9,711	12,136	12,757
c) Loans/securitised borrowings, etc. with multilateral/bilateral guarantee and IFC(W)	3,927	2,407	2,511	904	506	507
d) Self Liquidating Loans	0	0	0	0	0	0
VI. NRI and FC (B and O) Deposits (above one year maturity)	**1,35,422**	**1,10,021**	**83,712**	**31,171**	**23,160**	**17,154**
VII. Rupee Debt **	**11,770**	**13,390**	**14,844**	**2,709**	**2,818**	**3,042**
a) Defence	10,492	11,931	13,235	2,415	2,511	2,712
b) Civilian +	1,278	1,459	1,609	294	307	330
VIII. Total Long-term Debt (I to VII)	**4,68,591**	**4,76,888**	**4,68,512**	**1,07,857**	**1,00,300**	**96,012**
IX. Short-term Debt	**20,577**	**21,705**	**13,396**	**4,736**	**4,569**	**2,745**
a) NRI deposits (less than 1 year maturity)	1,321	9,320	4,724	304	1,962	968
b) Others (trade related) @	19,256	12,385	8,672	4,432	2,607	1,777
X. GRAND TOTAL	**4,89,168**	**4,98,593**	**4,81,908**	**1,12,593**	**1,04,869**	**98,757**
Concessional Debt						
As percentage of Total Debt	35.8	36.8	36.0	35.8	36.8	36.0
Short Term Debt						
As percentage of Total Debt	4.2	4.4	2.8	4.2	4.4	2.8
Memo Items:						
Debt Indicators:						
1. Debt Stock - GDP Ratio (in per cent)	17.6	20.2	21.1	17.6	20.2	21.1
2. Debt Service Ratio(per cent) (for fiscal year) (Including debt-servicing on non-civilian credits)	18.3	15.1	13.9	18.3	15.1	13.9

P : Provisional. R : Revised.
: Refers to debt outstanding to Institutions such as IFAD, OPEC and EEC (SAC).
: Refers to debt outstanding against loans from ADB.
* : Including net investment by 100 per cent FII debt funds, Resurgent India Bonds (RIBs) and India Millennium Deposits (IMDs).
** : Debt owed to Russia denominated in Rupees and converted at current exchange rates, payable in exports.
+ : Including Rupee suppliers' credit from end-March 1990 onwards.
@ : Excluding suppliers' credit of up to 180 days for which estimates are not available.

Note : Multilateral loans do not include revaluation of IBRD pooled loans and exchange rate adjustment under IDA loans for pre-1971 credits.

APPENDIX TABLE VI.11: INDICES OF REAL EFFECTIVE EXCHANGE RATE (REER) AND NOMINAL EFFECTIVE EXCHANGE RATE (NEER) OF THE INDIAN RUPEE

Year/Month	36 - country bilateral trade weights (Base : 1985 = 100)		5 - country bilateral trade weights (Base : 1993-94 = 100)	
	REER	NEER	REER	NEER
1	2	3	4	5
1993-94	61.59	44.69	100.00	100.00
1994-95	66.04	43.37	105.81	96.09
1995-96	63.62	39.73	102.29	87.69
1996-97	63.81	38.97	103.43	86.38
1997-98	67.02	40.01	105.84	86.43
1998-99	63.44	36.34	97.79	76.45
1999-00	63.29	35.46	96.74	74.22
2000-01	66.53	35.52	100.76	73.77
2001-02	68.43	35.75	102.09	73.18
2002-03	72.76	37.05	97.88	68.78
2003-04 (P)	74.14	36.25	99.60	67.36
2003-04				
April	74.14	36.72	99.55	68.18
May	72.67	35.88	97.91	66.88
June (P)	73.07	36.03	98.30	67.12
July (P)	74.55	36.83	100.27	68.56
August (P)	75.71	37.42	101.77	69.61
September (P)	75.75	37.09	101.86	69.08
October (P)	75.04	36.65	100.48	67.94
November (P)	74.72	36.34	100.72	67.63
December (P)	73.11	35.58	98.31	66.14
January (P)	72.88	35.18	97.99	65.30
February (P)	73.32	35.26	98.16	65.25
March (P)	74.72	36.03	99.85	66.64
2004-05 (P)				
April	77.01	36.97	103.12	68.61
May	74.78	35.72	101.30	67.27
June	75.98	35.86	100.80	66.14

P **:** Provisional.

Note :
1. The 36-country and 5-country REER indices have been recalculated from April 1994 and April 1993 onwards, respectively, using the new Wholesale Price Index (WPI) series (Base : 1993-94=100).
2. The 36-country REER and NEER have been estimated using the common price index and the exchange rate for the Euro, thus, representing 31 countries and the Euro area effective March 1, 2002.

RESERVE BANK OF INDIA
BALANCE SHEET AS AT 30TH JUNE 2004

ISSUE DEPARTMENT

(Rupees Thousands)

2002 - 03	LIABILITIES		2003 - 04	2002 - 03	ASSETS		2003 - 04
	Notes held in the				**Gold Coin and Bullion:**		
28,16,95	**Banking Department**	**23,89,70**		14036,76,55	(a) Held in India	**15240,39,42**	
292509,85,82	**Notes in circulation**	**332654,21,56**		–	(b) Held outside India	**–**	
				255000,00,00	**Foreign Securities**	**313709,35,44**	
292538,02,77	**Total Notes issued**		**332678,11,26**	269036,76,55	**Total**		**328949,74,86**
				228,78,36	**Rupee Coin**		**261,59,80**
				23272,47,86	**Government of India Rupee Securities**		**3466,76,60**
				–	**Internal Bills of Exchange and other Commercial Paper**		**–**
292538,02,77	**Total Liabilities**		**332678,11,26**	292538,02,77	**Total Assets**		**332678,11,26**

BANKING DEPARTMENT

2002- 03	LIABILITIES	2003- 04	2002- 03	ASSETS	2003- 04
5,00,00	**Capital paid-up**	**5,00,00**	28,16,95	**Notes**	**23,89,70**
6500,00,00	**Reserve Fund**	**6500,00,00**	29,02	**Rupee Coin**	**6,94**
	National Industrial Credit		25,25	**Small Coin**	**2,21,73**
12,00,00	**(Long Term Operations) Fund**	**13,00,00**			
	National Housing Credit			**Bills Purchased and Discounted :**	
186,00,00	**(Long Term Operations) Fund**	**187,00,00**	–	(a) Internal	–
			–	(b) External	–
			–	(c) Government Treasury Bills	–
	Deposits		109831,26,17	**Balances Held Abroad**	**194673,18,21**
	(a) Government				
100,16,22	(i) Central Government	**37912,22,37**			
41,15,13	(ii) State Governments	**41,15,30**			
	(b) Banks		86514,01,14	**Investments**	**57668,22,25**
78614,08,82	(i) Scheduled Commercial Banks	**80069,04,70**			
1643,02,50	(ii) Scheduled State Co-operative Banks	**2034,54,55**			
1548,21,00	(iii) Other Scheduled Co-operative Banks	**1667,74,11**			
47,07,61	(iv) Non-Scheduled State Co-operative Banks	**81,83,91**			
2748,21,23	(v) Other Banks	**3043,39,61**			
17454,27,45	**(c) Others**	**15521,74,89**		**Loans and Advances to :**	
			9783,00,00	(i) Central Government	**3272,00,00**
			3058,92,35	(ii) State Governments	**4159,80,49**
48,81,69	**Bills Payable**	**77,34,78**		**Loans and Advances to:**	
			1,05,48	(i) Scheduled Commercial Banks	**–**
			7,06,97	(ii) Scheduled State Co-operative Banks	**2,78,00**
			–	(iii) Other Scheduled Co-operative Banks	**–**
			–	(iv) Non-Scheduled State Co-operative Banks	**–**
			4475,64,84	(v) NABARD	**2732,09,05**
			1004,78,34	(vi) Others	**39,50,00**
118356,01,11	**Other Liabilities**	**129929,49,45**		**Loans, Advances and Investments from National Industrial Credit (Long Term Operations) Fund:**	
				(a) Loans and Advances to:	
			–	(i) Industrial Development Bank of India	**–**
			–	(ii) Export Import Bank of India	**–**
			–	(iii) Industrial Investment Bank of India Ltd.	**–**
			–	(iv) Others	**–**
				(b) Investments in bonds/debentures issued by:	
			–	(i) Industrial Development Bank of India	**–**
			–	(ii) Export Import Bank of India	**–**
			–	(iii) Industrial Investment Bank of India Ltd.	**–**
			–	(iv) Others	**–**
				Loans, Advances and Investments from National Housing Credit (Long Term Operations) Fund:	
			175,00,00	(a) Loans and Advances to National Housing Bank	**50,00,00**
			–	(b) Investments in bonds/ debentures issued by National Housing Bank	–
			12424,56,25	**Other Assets**	**14459,77,30**
227304,02,76	**Total Liabilities**	**277083,53,67**	227304,02,76	**Total Assets**	**277083,53,67**

Significant Accounting Policies and Notes to the Accounts as per Annex.

PROFIT AND LOSS ACCOUNT FOR THE YEAR ENDED 30TH JUNE 2004

(Rupees Thousands)

2002- 03	INCOME		2003- 04
15561,40,98	**Interest, Discount, Exchange, Commission *etc.* [1]**		**13166,13,55**
15561,40,98	**Total**		**13166,13,55**
	EXPENDITURE		
1990,08,87	**Interest**		**1808,48,34**
1488,85,85	**Establishment**		**2232,99,22**
55,14	**Directors' and Local Board Members' Fees and Expenses**		**93,14**
28,09,43	**Remittance of Treasure**		**21,09,23**
1352,40,66	**Agency Charges**		**1539,12,19**
1433,08,53	**Security Printing (Cheque, Note forms etc.)**		**1709,56,01**
26,15,85	**Printing and Stationery**		**51,81,29**
17,86,79	**Postage and Telecommunication Charges**		**23,01,90**
59,88,44	**Rent, Taxes, Insurance, Lighting etc.**		**58,80,81**
1,00,39	**Auditors' Fees and Expenses**		**1,28,87**
1,63,67	**Law Charges**		**1,90,60**
125,52,79	**Depreciation and Repairs to Bank's Property**		**154,34,33**
198,24,57	**Miscellaneous Expenses**		**158,77,62**
6723,40,98	**Total**		**7762,13,55**
8838,00,00	**Available Balance**		**5404,00,00**
	Less: Contribution To:		
	National Industrial Credit (Long Term Operations) Fund	1,00,00	
	National Rural Credit (Long Term Operations) Fund [2]	1,00,00	
	National Rural Credit (Stabilisation) Fund [2]	1,00,00	
	National Housing Credit (Long Term Operations) Fund	1,00,00	
4,00,00			**4,00,00**
8834,00,00	**Surplus Payable to Central Government**		**5400,00,00**

1. After making the usual or necessary provisions in terms of Section 47 of the Reserve Bank of India Act, 1934.
2. These funds are maintained by National Bank for Agriculture and Rural Development (NABARD).

V. S. Das	**K. J. Udeshi**	**Rakesh Mohan**	**Y.V. Reddy**
Chief General Manager	Deputy Governor	Deputy Governor	Governor

REPORT OF THE AUDITIORS

TO THE PRESIDENT OF INDIA

We, the undersigned auditors of the Reserve Bank of India, do hereby report to the Central Government upon the Balance Sheet of the Bank as at 30th June, 2004 and the Profit and Loss Account for the year ended on that date.

We have examined the above Balance Sheet of the Reserve Bank of India as at 30th June, 2004 and the Profit and Loss Account of the Bank for the year ended on that date and report that where we have called for information and explanations from the Bank, such information and explanations have been given and have been satisfactory.

These financial statements are the responsibility of the Bank's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in India. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion and according to the best of our information and explanations given to us and as shown by the books of account of the Bank, the Balance Sheet read with Significant Accounting Policies and Notes to the Accounts is a full and fair Balance Sheet containing all necessary particulars and is properly drawn up in accordance with the Reserve Bank of India Act, 1934 and Regulations framed thereunder so as to exhibit a true and correct view of the state of the Bank's affairs, in conformity with the accounting principles generally accepted in India.

P. B. Santhanakrishnan (M. No. 20309) **M/s. P.B.Vijayaraghavan & Co.,** Auditors	S. N. Nanda (M. No. 5909) **M/s. S.N. Nanda & Co.,** Auditors	P. Parthasarathy (M. No. 19410) **M/s. J.L.Sengupta & Co.,** Auditors	Shivji K. Vikamsey (M. No. 2242) **M/s. Khimji Kunverji & Co.,** Auditors	R. K. Goel (M. No. 6154) **M/s.Rajendra K.Goel & Co.,** Auditors	A. D. Shenoy (M. No. 11549) **M/s. Ford, Rhodes, Parks & Co.,** Auditors

ANNEX

RESERVE BANK OF INDIA

SIGNIFICANT ACCOUNTING POLICIES AND NOTES TO THE ACCOUNTS FOR 2003-04

SIGNIFICANT ACCOUNTING POLICIES

1. CONVENTION

The financial statements are prepared in accordance with the Reserve Bank of India Act, 1934 and the notifications issued thereunder and in the form prescribed by the Reserve Bank of India General Regulations, 1949.

Historical cost basis of accounting is used except where it is modified to reflect revaluation.

The accounting practices and policies followed in the statements, unless otherwise stated, are consistent with those followed in the previous year.

2. REVENUE RECOGNITION

Income and expenditure are recognised on accrual basis except penal interest and dividend which are accounted for on receipt basis. Only realised gains are recognised. Provision for outstanding expenditure is made for unpaid bills in each case of Rs. 1 lakh and above.

Balances unclaimed and outstanding for more than three consecutive years in certain transitory accounts including Drafts Payable Account, Payment Orders Account, Sundry Deposits Account, Remittance Clearance Account and Earnest Money Deposit Account are reviewed and written back to the Reserve Bank's income. Claims in this respect are considered and charged against the Reserve Bank's income as and when paid.

Income and expenditure in foreign currency are translated on the basis of exchange rates prevailing on the last business day of the preceding week.

3. GOLD AND FOREIGN CURRENCY ASSETS AND LIABILITIES

(a) Gold

Gold is valued at the end of the month at 90 per cent of the daily average price quoted at London for the month. The rupee equivalent is determined on the basis of the exchange rate prevailing on the last business day of the month. Unrealised gains/losses are adjusted to the Currency and Gold Revaluation Account.

(b) Foreign Currency Assets and Liabilities

All foreign currency assets and liabilities are translated at the exchange rates prevailing on the last business day of the week and also on the last business day of the month.

At the year-end, assets and liabilities in foreign currencies are translated at the exchange rates prevailing on the last business day except in cases where rates are contractually fixed. Foreign securities other than Treasury Bills are valued at lower of book value or market price prevailing on the last business day of each month. The depreciation is adjusted against current income. Foreign Treasury Bills are valued at cost. Forward exchange contracts are evaluated half-yearly and net loss, if any, is provided for.

Profit/loss on sale of foreign currency assets is recognised with respect to the book value. Exchange gains and losses arising from translation of foreign currency assets and liabilities are accounted for in Currency and Gold Revaluation Account and remain adjusted therein.

4. RUPEE SECURITIES

Rupee securities, other than Treasury Bills, held in the Issue and Banking Departments, are valued at lower of book value or market price or rates based on the yield curve prevailing on the last business day of the month where the market price for such securities is not available. The depreciation in the value is adjusted against current income. Treasury Bills are valued at cost.

5. SHARES

Investments in shares are valued at cost.

6. FIXED ASSETS

Fixed Assets are stated at cost less depreciation.

Depreciation on computers, motor vehicles, office equipments, furniture and electrical fittings, *etc.*, is charged on a straight-line basis. Depreciation on other assets including premises and fixtures is charged on written-down value basis.

Depreciation on fixed assets is charged only if held for a period of more than six months as at the year-end.

7. RETIREMENT BENEFITS

The liability on account of retirement benefits and leave encashment to employees is estimated based on an actuarial valuation.

8. CONTINGENCY RESERVE AND ASSET DEVELOPMENT RESERVE

Contingency Reserve represents the amount provided on a year-to-year basis for meeting unexpected and unforeseen contingencies including depreciation in value of securities, exchange guarantees and risks arising out of monetary/exchange rate policy compulsions.

In order to meet the internal capital expenditure and make investments in subsidiaries and associate institutions, a further specified sum is provided and credited to the Asset Development Reserve.

NOTES TO THE ACCOUNTS

1. SURPLUS TRANSFER TO THE GOVERNMENT OF INDIA

Surplus transferable to the Government includes an amount of Rs.2,331 crore representing interest differential pertaining to the period April 1, 2003 – March 31, 2004 on account of conversion of Special Securities into marketable securities.

2. RESERVE FUND

The Reserve Fund comprises initial contribution of Rs. 5 crore made by the Government of India and appreciation of Rs. 6,495 crore on account of revaluation of gold up to October 1990. Subsequent gains/losses on monthly revaluation of gold are taken to Currency and Gold Revaluation Account.

3. DEPOSITS

a. Deposits of the Central Government include an amount of Rs. 37,812.01 crore on account of operations under the Market Stablisation Scheme.

b. Deposits - Others :

(Rupees crore)

Particulars	As at June 30	
	2004	2003
1	2	3
I. Rupee Deposits from Foreign Central Banks and Foreign Financial Institutions	4,087.35	3,311.34
II. Deposits from Indian Financial Institutions	453.50	538.73
III. Accumulated Retirement Benefits	5,152.38	4,447.63
IV. Surplus transferable to Government of India	5,400.00	8,834.00
V. Miscellaneous	428.52	322.57
Total	**15,521.75**	**17,454.27**

4. OTHER LIABILITIES

(Rupees crore)

Particulars	As at June 30	
	2004	2003
1	2	3
I. Contingency Reserve		
Balance at the beginning of the year	55,249.29	48,434.17
Add : Accretion during the year	969.47	6,733.92
Add : Transfer from unresolved items of credit	–	81.20
Balance at the end of the year	**56,218.76**	**55,249.29**
II. Asset Development Reserve		
Balance at the beginning of the year	5,590.85	4,700.54
Add : Accretion during the year	188.09	890.31
Balance at the end of the year	**5,778.94**	**5,590.85**
III. Currency and Gold Revaluation Account		
Balance at the beginning of the year	51,276.41	51,010.77
Add : Net Accretion during the year	11,006.63	265.64
Balance at the end of the year	**62,283.04**	**51,276.41**
IV. Exchange Equalisation Account		
Balance at the beginning of the year	567.25	51.50
Transfer from Exchange Account	763.65	1,123.92
Add : Net Accretion(+)/ Net Utilisation(-) during the year	(-)1,325.25	(-)608.17
Balance at the end of the year	**5.65**	**567.25**
V. Provision for net debit entries in RBI General Account	**63.15**	**63.15**
VI. Provision for Outstanding Expenses	**1,153.86**	**1,239.12**
VII. Miscellaneous	**4,426.09**	**4,369.94**
Total (I to VII)	**1,29,929.49**	**1,18,356.01**

5. RBI GENERAL ACCOUNT

Miscellaneous under "Other Liabilities" includes Rs.517.39 crore in respect of inter-office transactions and balances under reconciliation. Reconciliation of entries is in progress and necessary adjustments are being effected as and when ascertained.

6. RUPEE INVESTMENTS

Securities sold under LAF repos have been reduced from *'Investments'*. Accordingly, the Reserve Bank has absorbed the liquidity in the market to the tune of Rs.61,885.00 crore as on June 30, 2004 for which securities amounting to Rs.64,979.25 crore were provided as collateral. These securities were repurchased in July 2004. Depreciation on these securities is parked in a separate account called Depreciation Adjustment Account and reversed in the month of July at the time of repurchase.

7. FOREIGN CURRENCY ASSETS

(Rupees crore)

Particulars	As at June 30	
	2004	2003
1	2	3
I. Held in Issue Department	3,13,709.35	2,55,000.00
II. Held in Banking Department -		
a) Included in Investments	16,482.48	169.72
b) Balances Held Abroad	1,94,673.18	1,09,831.26
Total	**5,24,865.01**	**3,65,000.98**

Note: (i) As on June 30, 2004, there were outstanding US$/Rupee forward exchange purchase contracts to the tune of Rs. 524.66 crore as against Rs. 18,634.03 crore outstanding as at June 30, 2003. There were no outstanding forward sale contracts as at June 30, 2004.

(ii) Uncalled amount on partly paid shares of the Bank for International Settlement as at June 30, 2004 was Rs 75.80 crore.

8. OTHER ASSETS

(Rupees crore)

Particulars	As at June 30	
	2004	2003
1	2	3
I. Fixed Assets (net of accumulated depreciation)	520.17	550.74
II. Gold	3,415.09	3,145.63
III. Income accrued but not received	6,339.20	6,621.92
IV. Miscellaneous	4,185.31	2,106.27
Total	**14,459.77**	**12,424.56**

9. INTEREST, DISCOUNT, EXCHANGE, COMMISSION, *ETC.*

Interest, Discount, Exchange, Commission, *etc.* include the following items.

(Rupees crore)

Particulars	Year ended	
	June 30, 2004	June 30, 2003
1	2	3
i. Profit on sale of Foreign and Rupee Securities	3,022.85	6,127.32
ii. Rent realised	9.17	11.98
iii. Net profit on sale of Bank's property	0.73	2.65

10. RETIREMENT BENEFITS

The Bank has made a provision of Rs. 1,010.00 crore (including additional provision on account of Optional Early Retirement Scheme) towards Gratuity and Superannuation Fund during the year based on actuarial valuation.

11. ESTABLISHMENT EXPENDITURE

Establishment expenditure includes payment of Ex-gratia of Rs. 408.00 crore to staff who opted for Optional Early Retirement Scheme.

LIST OF ABBREVIATIONS

AAIFR	-	Appellate Authority for Industrial and Financial Reconstruction
ACE	-	Asset Care Enterprise Ltd.
ACH	-	Automated Clearing Houses
ACU	-	Asian Clearing Union
AD	-	Authorised Dealer
ADB	-	Asian Development Bank
ADR	-	American Depository Receipt
AFS	-	Available for Sale
AFTA	-	ASEAN Free Trade Area
AIBP	-	Accelerated Irrigation Benefit Programme
AICL	-	Agricultural Insurance Company of India Ltd.
AIFI	-	All India Financial Institutions
ALD	-	Aggregate Liabilities to the Depositors
ALM	-	Asset Liability Management
AMFI	-	Association of Mutual Funds in India
AML	-	Anti Money Laundering
AMS	-	Aggregate Measures of Support
AoA	-	Agreement on Agriculture
APDRP	-	Accelerated Power Development and Reform Programme
APL	-	Above Poverty Line
APM	-	Administered Price Mechanism
ARC	-	Asset Reconstruction Company
ARCIL	-	Asset Reconstruction Company of India Ltd.
ARDC	-	Agriculture Refinance and Development Corporation
AS	-	Accounting Standard
ASCI	-	Administrative Staff College of India
ASEAN	-	Association of South East Asian Nations
ATC	-	Agreement on Textile and Clothing
ATM	-	Automated Teller Machine
BCBS	-	Basel Committee on Banking Supervision
BCP	-	Business Continuity Plan
BFS	-	Board for Financial Supervision
BFSI	-	Banking, Financial Services and Insurance
BIFR	-	Board for Industrial and Financial Reconstruction
BIMST-EC	-	Bangladesh, India, Myanmar, Sri Lanka, Thailand Economic Cooperation
BIMSTEC	-	Bay of Bengal Initiative for Multi-Sectoral Technical and Economic Cooperation
BIS	-	Bank for International Settlements
BoP	-	Balance of Payments
BPL	-	Below Poverty Line
BPLR	-	Benchmark Prime Lending Rate
BPO	-	Business Process Outsourcing
BPSS	-	Board for Payment and Settlement Systems
BRBNMPL	-	Bharatiya Reserve Bank Note Mudran Private Limited
BSE	-	The Stock Exchange, Mumbai
BSR	-	Basic Statistical Returns
BTC	-	Bankers Training College
CA	-	Certification Authority
CAB	-	College of Agricultural Banking
CAC	-	Collective Action Clause
CAG	-	Comptroller and Auditor General
CBI	-	Central Bureau of Investigation
CBDT	-	Central Board of Direct Taxes
CBLO	-	Collateralised Borrowing and Lending Obligation
CBoT	-	Chicago Board of Trade
CBSL	-	Central Bank of Sri Lanka
CBS	-	Consolidated Banking Statistics
CCA	-	Controller of Certifying Authorities
CCIL	-	Clearing Corporation of India Limited
CCP	-	Central Counter Party
CD	-	Certificate of Deposit
CDBMS	-	Central Database Management System
CDR	-	Corporate Debt Restructuring

LIST OF ABBREVIATIONS

CD-ROM	-	Compact Disk Read Only Memory
CEA	-	Central Electricity Authority
CECA	-	Comprehensive Economic Cooperation Agreement
CENVAT	-	Central Value Added Tax
CEO	-	Chief Executive Officer
CEPA	-	Comprehensive Economic Partnership Agreement
CEPR	-	Centre for Economic Policy Research
CEPT	-	Common External Preferential Tariff
CFMS	-	Centralised Funds Management System
CFS	-	Consolidated Financial Statement
CFTS	-	Centralised Funds Transfer System
CGRA	-	Currency and Gold Revaluation Account
CGTSI	-	Credit Guarantee Fund Trust for Small Industries
CIB	-	Capital Indexed Bond
CIBIL	-	Credit Information Bureau of India Limited
CIS	-	Commonwealth of Independent States
CLA	-	Central Listing Authority
CLF	-	Collateralised Lending Facility
COD	-	Central Office Department
CoR	-	Certificate of Registration
CPIS	-	Coordinated Portfolio Investment Survey
CPI	-	Consumer Price Index
CPI-IW	-	Consumer Price Index for Industrial Workers
CPR	-	Consolidated Prudential Report
CP	-	Commercial Paper
CPSS	-	Committee on Payment and Settlement Systems
CPSU	-	Central Power Sector Utility
CRAR	-	Capital to Risk Weighted Assets Ratio
CRM	-	Country Risk Management
CRR	-	Cash Reserve Ratio
CSGL	-	Constituents' Subsidiary General Ledger Account
CSIR	-	Council of Scientific and Industrial Research
CSO	-	Central Statistical Organisation
CSP	-	Central Sector Project
CVPS	-	Currency Verification and Processing System
DAD	-	Deposit Accounts Department
DAPM	-	Department of Administration and Personnel Management
DBOD	-	Department of Banking Operations and Development
DBS	-	Department of Banking Supervision
DC-DB	-	Defined Contribution- Defined Benefit
DCA	-	Debtor-Creditor Agreement
DCCB	-	District Central Co-operative Bank
DCM	-	Department of Currency Management
DEAP	-	Department of Economic Analysis and Policy
DEBC	-	Department of Expenditure and Budgetary Control
DEIO	-	Department of External Investments and Operations
DESACS	-	Department of Statistical Analysis and Computer Services
DFHI	-	Discount and Finance House of India
DFI	-	Development Finance Institution
DFID	-	Department For International Development
DFRC	-	Duty Free Replenishment Certificate
DGBA	-	Department of Government and Bank Accounts
DGCI&S	-	Directorate General of Commercial Intelligence and Statistics
DICGC	-	Deposit Insurance and Credit Guarantee Corporation
DIT	-	Department of Information Technology
DNBS	-	Department of Non-Banking Supervision
DNSS	-	Deferred Net Settlement System
DP	-	Depository Participant
DRDA	-	District Rural Development Agency
DRG	-	Development Research Group

LIST OF ABBREVIATIONS

DRI	-	Differential Rate of Interest
DRS	-	Disaster Recovery System
DSS	-	Debt Swap Scheme
DRT	-	Debt Recovery Tribunal
DTA	-	Domestic Tariff Area
DTL	-	Demand and Time Liabilities
D*v*P	-	Delivery *versus* Payment
DWCRA	-	Development of Women and Children in Rural Areas
EC	-	Exchange Control
ECB	-	External Commercial Borrowing
ECD	-	Exchange Control Department
ECGC	-	Export Credit Guarantee Corporation
ECN	-	Electronic Communication Network
ECR	-	Export Credit Refinance
ECS	-	Electronic Clearing Services
EDI	-	Electronic Data Interchange
EDIFAR	-	Electronic Data Information Filing and Retrieval
EEA	-	Exchange Equalisation Account
EEFC	-	Exchange Earners' Foreign Currency Account
EFC	-	Eleventh Finance Commission
EFT	-	Electronic Funds Transfer
EKMS	-	Enterprise Knowledge Management System
EME	-	Emerging Market Economy
EMM	-	Enterprise Maturity Model
EMU	-	European Monetary Union
EOU	-	Export Oriented Unit
EPCG	-	Export Promotion Capital Goods
ESCAP	-	Economic and Social Commission for Asia and the Pacific
ESOP	-	Employees Stock Option Plan
EU	-	European Union
EXIM	-	Export Import
FAQ	-	Frequently Asked Question
FCA	-	Foreign Currency Assets
FCI	-	Food Corporation of India
FCNRA	-	Foreign Currency Non-Resident Account
FCNR(B)	-	Foreign Currency Non-Resident (Banks)
FCRA	-	Forward Contract Regulation Act
FCCB	-	Foreign Currency Convertible Bond
FDI	-	Foreign Direct investment
FEDAI	-	Foreign Exchange Dealers' Association of India
FED	-	Foreign Exchange Department
FEMA	-	Foreign Exchange Management Act
FER	-	Foreign Exchange Reserves
FET-ERS	-	Foreign Exchange Transactions - Electronic Reporting System
FI	-	Financial Institution
FII	-	Foreign Institutional Investor
FIIS	-	Farm Insurance Income Scheme
FIMMDA	-	Fixed Income Money Market and Derivatives Association of India
FMCG	-	Fast Moving Consumer Goods
FRA	-	Forward Rate Agreement
FRB	-	Floating Rate Bond
FRBM	-	Fiscal Responsibility and Budget Management
FRL	-	Full Reservoir Level
FSSA	-	Financial System Stability Assessments
FTP	-	Financial Transaction Plan
FTT	-	Foreign Travel Tax
G-20	-	Group of Twenty
GAAP	-	Generally Accepted Accounting Principles
GATS	-	General Agreement on Trade in Services
GATT	-	General Agreement on Tariffs and Trade
GB	-	Giga-bytes
GCF	-	Gross Capital Formation
GDCF	-	Gross Domestic Capital Formation
GDP	-	Gross Domestic Product
GDS	-	Gross Domestic Saving

LIST OF ABBREVIATIONS

GDR - Global Depository Receipt
GFCF - Gross Fixed Capital Formation
GFD - Gross Fiscal Deficit
GIC - General Insurance Corporation of India
GoI - Government of India
GRF - Guarantee Redemption Fund
GSO - Green Shoe Option
GST - Goods and Services Tax
GTB - Global Trust Bank
HACCP - Hazard Analysis and Critical Control Points
HFC - Housing Finance Company
HFT - Held for Trading
HLCCFCM - High Level Co-ordination Committee on Financial and Capital Market
HR - Human Resources
HRDD - Human Resources Development Department
HTM - Held to Maturity
HUDCO - Housing and Urban Development Corporation
IAS - Integrated Accounting System
IASC - Inspection and Audit Sub-Committee
IATT - Inland Air Travel Tax
IBA - Indian Banks' Association
IBS - International Banking Statistics
ICA - Inter-creditor Agreement
ICAI - Institute of Chartered Accountants of India
ICC - International Credit Card
ICCOMS - Integrated Computerised Currency Operation and Management System
ICDs - Inter-corporate Deposits
ICG - Interactive Co-ordination Group
ICOR - Incremental Capital Output Ratio
ID - Inspection Department
IDC - International Data Corporation
IDBI - Industrial Development Bank of India
IDFC - Infrastructure Development Finance Company
IDL - Intra-day Liquidity
IDMD - Internal Debt Management Department
IDR - Indian Depository Receipt
IDRBT - Institute for Development and Research in Banking Technology
IEA - International Energy Agency
IECD - Industrial and Export Credit Department
IEM - Industrial Entrepreneurs Memoranda
IFC - International Finance Corporation
IFCI - Industrial Finance Corporation of India
IFI - International Financial Institution
IFR - Investment Fluctuation Reserve
IIBI - Industrial Investment Bank of India
IIP - Index of Industrial Production
IIP - International Investment Position
IIT - Indian Institute of Technology
IMD - India Meteorological Department
IMF - International Monetary Fund
IMFC - International Monetary and Financial Committee
INFINET - Indian Financial Network
IOSCO - International Organisation of Securities Commissions
IPO - Initial Public Offering
IRB - Internal Rating Based
IRDA - Insurance Regulatory and Development Authority
IRF - Interest Rate Future
IRS - Interest Rate Swap
ISA - Information System Audits
ISP - Information Security Policy
ISN - International System of Nomenclature
IT - Information Technology
ITES-BPO - Information Technology Enabled Services and Business Process Outsourcing

LIST OF ABBREVIATIONS

JCI	-	Jute Corporation of India
JNIDB	-	Jawaharlal Nehru Institute of Development Banking
JPC	-	Joint Parliamentary Committee
JV	-	Joint Venture
KCC	-	*Kisan* Credit Card
KVIC	-	*Khadi* and Village Industries Commission
KYC	-	Know Your Customer
LAB	-	Local Area Bank
LAF	-	Liquidity Adjustment Facility
LAN	-	Local Area Network
LaR	-	Liquidity at Risk
LBS	-	Locational Banking Statistics
LC	-	Letter of Credit
LD	-	Legal Department
LIC	-	Life Insurance Corporation of India
LIBOR	-	London Inter-Bank Offered Rate
LIFFE	-	London Inter-Bank Financial Futures Exchange
LPA	-	Long Period Average
LPG	-	Liquefied Petroleum Gas
LTO	-	Long Term Operations
LVPS	-	Large Value Payment Systems
M&A	-	Merger and Acquisition
M_3	-	Broad Money
MASI	-	Management Audit Systems Inspection
MAT	-	Minimum Alternate Tax
MB	-	Mega-byte
MBS	-	Mortgage-Backed Securities
MFA	-	Multi Fibre Agreement
MG	-	Mahatma Gandhi
MICR	-	Magnetic Ink Character Recognition
MIFOR	-	Mumbai Inter-Bank Forward Offered Rate
MIS	-	Management Information System
MNBC	-	Miscellaneous Non-Banking Company
MoU	-	Memorandum of Understanding
MPBF	-	Maximum Permissible Bank Finance
MPI	-	Macro-Prudential Indicator
MRTP	-	Monopolies and Restrictive Trade Practices
MSCS	-	Multi-State Co-operative Societies
MSS	-	Market Stabilisation Scheme
MSP	-	Minimum Support Price
MTFRP	-	Medium-Term Fiscal Reforms Programme
MW	-	Mega Watts
NABARD	-	National Bank for Agriculture and Rural Development
NASSCOM	-	National Association of Software and Services Companies
NAFED	-	National Agricultural Co-operative Marketing Federation
NAV	-	Net Asset Value
NFA	-	Net Foreign Assets
NHB	-	National Housing Bank
NBFC	-	Non-Banking Financial Company
NCAER	-	National Council of Applied Economic Research
NCD	-	Non-Convertible Debenture
NDA	-	Net Domestic Assets
NDS	-	Negotiated Dealing System
NDTL	-	Net Demand and Time Liabilities
NEP	-	National Electricity Policy
NEER	-	Nominal Effective Exchange Rate
NEFT	-	National Electronic Funds Transfer
NFBS	-	National Family Benefit Scheme
NGO	-	Non-Government Organisation
NHAI	-	National Highway Authority of India
NHB	-	National Housing Bank
NIAS	-	National Impact Assessment Survey
NIBM	-	National Institute of Bank Management
NIC	-	National Industrial Credit
NMBS	-	National Maternity Benefit Scheme
NMS	-	Network Management System
NOAPS	-	National Old Age Pension Scheme
NOF	-	Net Owned Fund
NPA	-	Non-Performing Asset

LIST OF ABBREVIATIONS

NPC	-	National Payments Council
NRB	-	Nepal Rastra Bank
NRE	-	Non-Resident External
NRI	-	Non-Resident Indian
NR(NR)RD	-	Non-Resident (Non-Repatriable) Rupee Deposits
NRO	-	Non-Resident Ordinary Accounts
NRSR	-	Non-Resident Special Rupee Deposits
NSAP	-	National Social Assistance Programme
NSC	-	National Statistical Commission
NSE	-	National Stock Exchange
NSSF	-	National Small Saving Fund
NSE-MIBOR	-	National Stock Exchange-Mumbai Inter-Bank Offered Rate
NSDL	-	National Securities Depository Ltd.
NSF	-	Net Satisfaction Factor
NSS	-	National Settlement System
NIC	-	National Industrial Credit
O&M	-	Operation and Maintenance
OBC	-	Oriental Bank of Commerce
OBCs	-	Other Backward Classes
OBU	-	Offshore Banking Unit
OCB	-	Overseas Corporate Body
OD	-	Overdraft
OECD	-	Organisation for Economic Cooperation and Development
OERS	-	Optional Early Retirement Scheme
OLTAS	-	Online Tax Accounting Systems
OMO	-	Open Market Operation
ONGC	-	Oil and Natural Gas Commission
OPAC	-	Online Public Access Catalogue
OPEC	-	Organisation of Petroleum Exporting Countries
OSMOS	-	Off-site Monitoring and Surveillance
OTCEI	-	Over-the-Counter Exchange of India
OTS	-	One-Time Settlement
OWS	-	Other Welfare Schemes
PAS	-	Performance Appraisal System
PAT	-	Profit After Tax
PBT	-	Profit Before Tax
PCA	-	Prompt Corrective Action
PCD	-	Partially Convertible Debenture
PD	-	Premises Department
PD	-	Primary Dealer
PDO	-	Public Debt Office
PDS	-	Public Distribution System
PFC	-	Power Finance Corporation
PFI	-	Public Financial Institution
PIO	-	Person of Indian Origin
PKI	-	Public Key Infrastructure
PLR	-	Prime Lending Rate
P&L	-	Profit and Loss
PMGSY	-	*Pradhan Mantri Gram Sadak Yojana*
PMGY	-	*Pradhan Mantri Gramodaya Yojana*
PMO	-	Primary Market Operations
PMRY	-	Prime Minister's *Rozgar Yojana*
PMS	-	Portfolio Management Services
POL	-	Petroleum, Oil and Lubricants
PRD	-	Press Relations Division
PSB	-	Public Sector Bank
PSRS	-	Prudential Supervisory Reporting System
PSSC	-	Payment and Settlement Systems Committee
PSU	-	Public Sector Undertaking
PTA	-	Preferential Trading Agreement
QIS	-	Quantitative Impact Study
RBS	-	Risk-Based Supervision
RBSB	-	Reserve Bank Services Board
RBSC	-	Reserve Bank Staff College
RC	-	Reconstruction Companies
RD	-	Revenue Deficit
RDBMS	-	Relational Data Base Management System
REC	-	Rural Electrification Corporation
REER	-	Real Effective Exchange Rate

LIST OF ABBREVIATIONS

RFC(D)	-	Resident Foreign Currency (Domestic)
Repo	-	Ready Forward/Repurchase Agreement
RIB	-	Resurgent India Bond
RIDF	-	Rural Infrastructure Development Fund
RIN	-	Risk Intelligence Network
RNBC	-	Residuary Non-Banking Company
RO	-	Regional Office
ROA	-	Return on Total Assets
ROE	-	Return on Equity
RPCD	-	Rural Planning and Credit Department
RPT	-	Risk Profile Template
RRB	-	Regional Rural Bank
RSSS	-	Recommendations for Securities Settlement System
RTGS	-	Real Time Gross Settlement
RTIA	-	Regional Trade and Investment Area
RTP	-	Reserve Tranche Position
SAARC	-	South Asian Association for Regional Cooperation
SACP	-	Special Agricultural Credit Plan
SAD	-	Special Additional Duty
SAFE	-	South Asian Federation of Stock Exchanges
SAFTA	-	South Asian Free Trade Agreement
SAPTA	-	South Asian Preferential Trade Agreement
SARFAESI Act	-	Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002
SARB	-	South African Reserve Bank
SARS	-	Severe Acute Respiratory Syndrome
SASF	-	Stressed Assets Stabilisation Fund
SBI	-	State Bank of India
SBS	-	Shredding and Briquetting System
SC	-	Securitisation Companies
SCB	-	Scheduled Commercial Bank
SC	-	Scheduled Caste
SCRA	-	Securities Contracts (Regulation) Act, 1956
SDDS	-	Special Data Dissemination Standards
SDF	-	Submission of Declaration Form
SDRM	-	Sovereign Debt Restructuring Mechanism
SDR	-	Special Drawing Right
SEBI	-	Securities and Exchange Board of India
SEB	-	State Electricity Board
SEFER	-	Securities held as Foreign Exchange Reserves
SEFT	-	Special Electronic Funds Transfer
SERC	-	State Electricity Regulatory Commission
SEZ	-	Special Economic Zone
SFC	-	State Financial Corporation
SFMS	-	Structured Financial Messaging Solution
SGL	-	Subsidiary General Ledger
SGSY	-	*Swarnajayanti Gram Swarozgar Yojana*
SHG	-	Self-Help Group
SHPI	-	Self-Help Promoting Institutions
SIDBI	-	Small Industrial Development Bank of India
SIDC	-	Small Industries Development Corporation
SIFI	-	Systemically Important Financial Intermediary
SIPS	-	Systemically Important Payment System
SITP	-	Strategic Information Technology Plan
SJSRY	-	*Swarna Jayanthi Shahari Rozgar Yojana*
SLR	-	Statutory Liquidity Ratio
SLRS	-	Scheme of Liberation and Rehabilitation of Scavengers
SME	-	Small and Medium Enterprise
SMP	-	Statutory Minimum Price
SOR	-	States' Own Revenue
SPSU	-	State Public Sector Undertaking
SPV	-	Special Purpose Vehicle
SSI	-	Small Scale Industry
SSS	-	Securities Settlement System

LIST OF ABBREVIATIONS

STP	-	Straight Through Processing
STRIPS	-	Separate Trading for Registered Interest and Principal of Securities
ST	-	Scheduled Tribe
SIFI	-	Systemically Important Financial Intermediaries
SWIFT	-	Society for Worldwide Inter-bank Financial Telecommunications
TAC	-	Technical Advisory Committee
TBT	-	Technical Barriers to Trade
TFCI	-	Tourism Finance Corporation of India
TFPG	-	Total Factor Productivity Growth
TIN	-	Tax Information Network
ToR	-	Terms of Reference
TPA	-	Tri-Partite Agreement
TPDS	-	Targeted Public Distribution System
TQM	-	Total Quality Management
TUFS	-	Technology Upgradation Fund Scheme
UBD	-	Urban Banks Department
UCB	-	Urban Co-operative Bank
UIP	-	Uncovered Interest Parity
UNCTAD	-	United Nations Conference for Trade and Development
UR	-	Uruguay Round
URIF	-	Urban Reforms Incentive Fund
VAMNICOM	-	Vaikunth Mehta National Institute of Co-operative Management
VaR	-	Value at Risk
VAR	-	Vector Auto Regression
VAT	-	Value Added Tax
VRS	-	Voluntary Retirement Scheme
WADR	-	Weighted Average Discount Rate
WAN	-	Wide Area Network
WCDL	-	Working Capital Demand Loan
WDM	-	Wholesale Debt Market
WHO	-	World Health Organization
WMA	-	Ways and Means Advance
WOS	-	Wholly Owned Subsidiaries
WPI	-	Wholesale Price Index
WSS	-	Weekly Statistical Supplement
WTO	-	World Trade Organization
XLRI	-	Xavier Labour Relations Institute
Y-on-Y	-	Year-on-Year
YTM	-	Yield-to-Maturity
ZTC	-	Zonal Training Centres

This Report can also be accessed on Internet
URL : www.rbi.org.in