

**PRESS INFORMATION BUREAU
GOVERNMENT OF INDIA**

**GOVERNMENT FIRMLY COMMITTED TO MEETING ITS FISCAL DEFICIT
TARGET FOR CURRENT YEAR: MID-YEAR ECONOMIC ANALYSIS (MYEA)
2014-15**

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Mid-Year Economic Analysis (MYEA) 2014-15 provides a technical perspective on several aspects of the Indian macro-economy. Following are the major highlights of the Mid Year Analysis:

Macro-economy and investor sentiment

There has been a striking turnaround in India's macro-economy and investor sentiment since the government took over, reflected in lower inflation, a lower current account deficit, surging capital inflows and stock market valuations, and the bottoming out of the growth deceleration seen for nearly three years. India is, and is perceived as, one of the sparks of the global economy. Underlying this change is the election of a new Government with a relatively unencumbered political mandate for decisive economic change.

Validating this mandate, the Government since coming into office has taken a number of policy actions, including (but not restricted to) deregulating diesel, raising the price of natural gas, moving toward direct transfers for cooking gas, moderating inflationary pressures in agriculture, increasing foreign direct investment caps in defence with planned increases in railways, expediting financial inclusion, and moving toward deregulating coal. These actions combined with favourable external developments in the form of declining oil and commodity prices have helped improve the macroeconomic situation, and business and investor sentiment.

Fiscal situation

The Government is firmly committed to meeting its fiscal deficit target for this year, and the MYEA highlights the unusually challenging circumstances facing the Government, which include:

- The economy growing slower than expected affecting revenue growth;
- The optimistic revenue projections in the budget not having materialized;
- The legacy of past expenditures weighing on the budget; and
- The ambitiousness of the target itself because of trying to achieve fiscal consolidation when the economy is growing slower than its potential. India is, somewhat unusually amongst the major economies, following such pro-cyclical fiscal policy.

Inflation

It has come down dramatically for four reasons: policy actions by the RBI and the Government, declining agricultural prices; declining oil prices; and the economy growing slower than its potential.

Going forward disinflationary impulses especially from agriculture, external and domestic, are strong, reflected for example in rapidly declining rural wage growth. The declining trend of inflation is likely to continue, with strong potential to surprise on the upside.

Exchange rate

From the headlines, it seems that the rupee is weakening. It is weakening against the dollar, which is strengthening against the other major currencies. Against a broader basket of currencies, the rupee has become stronger not weaker. The resulting deterioration in competitiveness of the Indian economy owes in part to India's higher inflation but also to strong capital inflows which have to be pragmatically and prudently managed.

Growth challenge

The growth deceleration witnessed for many years appears to have bottomed out. A durable recovery in investment and growth is a work-in-progress. Uncertainty about private investment stems from a relatively weak corporate sector (depressed or negative profits and high debt) and because the PPP model in infrastructure is in limbo. This condition might be characterized as a "balance sheet syndrome with Indian characteristics."

To revive growth going forward, public investment may have to play a greater role to complement and crowd-in private investment. Consideration should be given to pursuing counter-structural fiscal policy as a way of reviving growth, and to finding the fiscal space to finance such investment, while ensuring that projects are judiciously identified and effectively and expeditiously implemented.

Reforms ahead

Going forward, there is great reason for hope because in addition to liberalizing FDI in insurance, two game-changing reforms are on the horizon: (i) the Goods and Services Tax (GST) which will create a buoyant source of revenue and place the fiscal position on a permanently solid footing, help tax administration and reduce corruption in indirect tax collection, and serve to make India more of a common market by eliminating internal barriers to trade; and (ii) the increasing use of direct transfers, combining the Pradhan Mantri Jan Dhan Yojana with Aadhaar, that could replace over time extensive Government interventions to help producers and consumers.

Reforms at the centre will and should increasingly be complemented by reforms by the states. India can become a very distinctive model of a "cooperative and competitive federalism," deriving stability and strength from the former while harnessing the dynamism and energy afforded by the latter.

In sum, there is growing ground for hope and optimism but narrowing room for complacency.
