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8.6 pc is the growth rate predicted by PMEAC in economic review

By **S.P.S. Pannu** in New Delhi

THE Prime Minister's Economic Advisory Council (PMEAC) on Monday projected an 8.6 per cent economic growth rate for India during the current financial year but came out in favour of tight monetary and fiscal policies to rein in the "uncomfortably high level" of inflation.

The 'Review of the Economy 2010-11' report sees the gross domestic product (GDP) growth rate bouncing back to nine per cent in 2011-12.

"Agriculture will do very well this year," said PMEAC chairman C. Rangarajan while releasing the report. The report expects the farm sector to grow at 5.4 per cent this fiscal, up from a measly 0.4 per cent in 2009-10 when the worst drought in recent years had caused crops to wither.

The services sector is expected to register a growth rate of 9.6 per cent against 9.1 per cent last year while industrial expansion is projected to moderate to 8.1 per cent from 8.8 per cent.

However, the PMEAC has raised its estimate for overall

Fiscal & revenue deficit beyond comfort zone

inflation to seven per cent by March-end from the 6.5 per cent anticipated earlier due to what it sees as "aberrant behaviour in the prices of vegetables".

The report points out that vegetable prices, which normally show a pronounced decline as winter sets in and the supply expands sharply, showed a contrary trend this year.

According to the report, the domestic economic conditions tend to suffer from supply bottlenecks as the robust demand growth tends to outstrip the pace of supply expansion.

It highlights the fact that controlling inflation has been made more difficult because the prices of internationally traded commodities, such as crude oil, sugar, urea, cotton, gold, copper and steel have surged past their pre-2008 levels.

However, at the same time the report strikes an optimistic note to state that although these factors make the task of maintaining price stability at home difficult, it is not impossible.

The PMEAC report states that monetary and fiscal policies have to be appropriately tight to protect the economy from inflation. Monetary policy has a role to play, even in situations where inflation is triggered by supply constraints.

However, this appears to be a hawkish line from the Indian industrialists' viewpoint as any increase in the interest rates by the Reserve Bank of India (RBI) as part of a tighter monetary policy could choke growth.

Car and two-wheeler manufacturers, who have been clocking robust growth rates this year, fear trouble ahead as high interest rates on vehicle loans could dampen buyers' enthusiasm.

Similarly, a tight fiscal policy would usher in a regime of higher excise duties, which in turn would lead to higher prices that would discourage buyers.

The report talks of reducing the fiscal deficit to tame inflation and proceed with the task of fiscal consolidation, which started with a two per cent rise in excise duties on all goods across-the-board in the last budget.

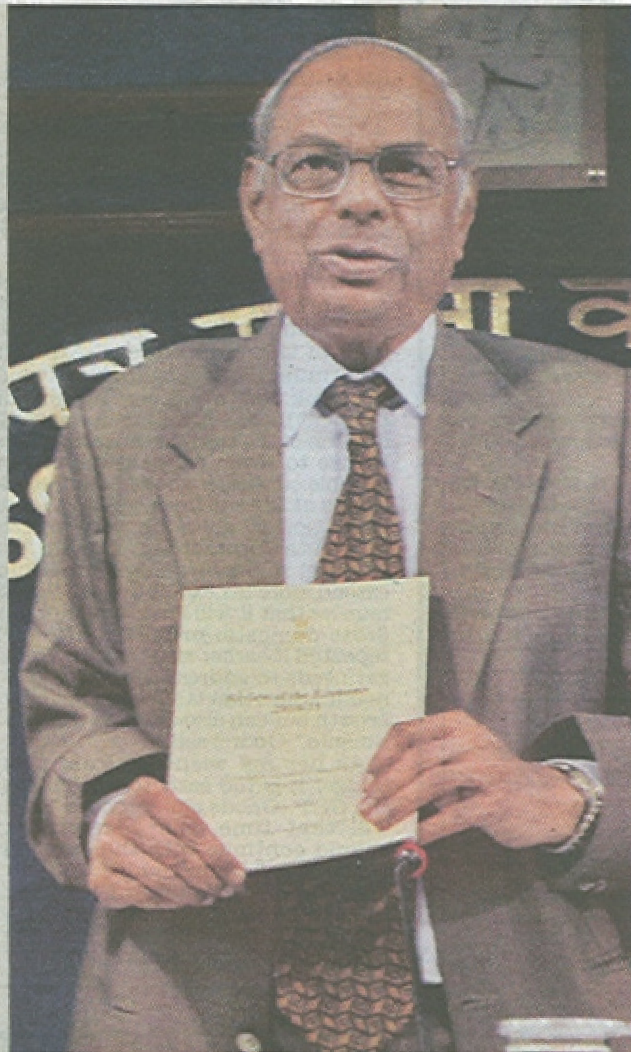
It states that the higher economic growth will help the government reduce the fiscal deficit to 5.2 per cent in 2010-11 from 5.5 per cent estimated earlier.

The report points out that while the government has to reduce the fiscal deficit, at the same time there will be increased expenditure on food security, right to education, healthcare and higher wages under the National Rural Employment Guarantee Act (NREGA). A significant portion of the fiscal adjustment to reduce the deficit will therefore have to come from additional tax revenues, it adds.

According to the report, the Centre needs to push ahead with the new Goods and Services Tax (GST) and the Direct Taxes Code (DTC). It also states that revenue productivity would have to be increased through reform in tax administration and measures to prevent the flight of income to tax havens.

THE LONG & SHORT OF IT

- **Agriculture expected to grow at 5.4% in 2010-11 and 3% next fiscal**
- Industry to grow at **8.1%** services likely to grow at **9.6%** in 2010-11
- **Slow recovery in global economic and financial situation**
- Rising domestic savings and investment chief engines of growth
- **Investment rate to be 37% in 2010-11 and 37.5% next fiscal**
- Current account deficit pegged at **3%** of GDP in 2010-11
- **Trade deficit pegged at $132 bn in 2010-11 and $151.5 bn next fiscal**
- Invisibles trade surplus projected at **$81.3 bn** in 2010-11 and **$95.7 bn** next fiscal
- **Inflation rate projected at 7% by March 2011**
- Need to ensure manufactured goods inflation remains below **5%**
- **Need to exit stimulus and look at fiscal tightening**
- Consolidated fiscal deficit is likely to be **7.5-8%** of GDP for 2010-11
- **Need to implement Goods and Services Tax (GST) soon**



C. Rangarajan, chairman of the PMEAC, releases the Review of Economy 2010-11 in New Delhi on Monday.