## A] REVIEW OF THE GENERAL ECONOMIC ENVIRONMENT AND THE INVESTMENT CLIMATE

### General Economic Environment

The real GDP growth based on 1993-94 prices, was estimated at 6.4 per cent in 1999-2000. In 1998-99 it was 6.8 percent. Deterioration in the performance of agriculture sector largely accounted for the decline in the growth rate of the economy. However the industrial output emerged out the sluggish trend of the preceding year and recovery appeared to be underway. An important aspect of the industrial growth, which would have an impact on the capital market, was the increase in the output of manufacturing sector by 9.3 per cent which was more than double the growth achieved in the previous year (4.3 per cent). A further analysis shows that intermediate and consumer goods industries accelerated their growth to 15.2 per cent and 5.9 per cent, respectively, from that of 5.9 per cent and 2.4 per cent during 1998-99. The decline in growth of production of capital goods and lower increase in the imports of the capital goods indicate existence of investment pessimism in the real sector. A striking feature of growth of GDP is the continuous increase in the share of services sector which contributed nearly 52 per cent to it leading to recognition that India has been moving to a services based growth.

**Table 1.2 Saving Rates (as a percent of) GDP at Current Market Prices**

| | 1993-94 | 1994-95 | 1995-96 | 1996-97 | 1997-98 (P) | 1998-99 (Q) |
|---|---|---|---|---|---|---|
| **Gross Domestic Saving** | 22.5 | 25.0 | 25.5 | 23.3 | 24.7 | 22.3 |
| Public | 0.6 | 1.7 | 2.0 | 1.7 | 1.4 | 0.0 |
| Private | 21.9 | 23.3 | 23.4 | 21.6 | 23.3 | 22.3 |
| (i) Household sector | 18.4 | 19.8 | 18.5 | 17.1 | 19.0 | 18.5 |
| (a) Financial savings | 11.0 | 12.0 | 8.9 | 10.4 | 10.4 | 10.9 |
| (b)Physical savings | 7.4 | 7.8 | 9.6 | 6.7 | 8.6 | 7.6 |
| **Gross Domestic Investment*** | 23.1 | 26.1 | 27.2 | 24.6 | 26.2 | 23.4 |
| Public | 8.2 | 8.8 | 7.6 | 7.0 | 6.7 | 6.6 |
| Private | 13.0 | 14.8 | 18.9 | 14.9 | 16.7 | 15.2 |
| **Gross Domestic Investment*** | 23.1 | 26.1 | 27.2 | 24.6 | 26.2 | 23.4 |
| GFCF | 21.4 | 22.0 | 24.6 | 23.0 | 22.7 | 21.4 |
| Change in stocks | -0.2 | 1.6 | 1.9 | -1.2 | 0.7 | 0.4 |
| **Saving-Investment** | -0.6 | -1.2 | -1.8 | -1.3 | -1.5 | -1.0 |

| | | | | | | |
|---|---|---|---|---|---|---|
| **Gap @** | | | | | | |
| Public | -7.6 | -7.1 | -5.6 | -5.3 | -5.3 | -6.6 |
| Private | 8.9 | 8.5 | 4.5 | 6.7 | 6.6 | 7.1 |

Note: (i) Gross domestic investment denotes gross domestic capital formation (GDCF)

(ii) Figures may not add up due to rounding off

* : adjusted for errors and omissions;

@ : refers to the difference between the rates of savings and investment

GFCF: Gross fixed capital formation;

P : Provisional estimates; Q : Quick estimates

Source: Economic Survey, 1999-2000

In 1998-99 domestic savings deteriorated to 22.3 per cent from 24.7 per cent in the previous year. This raises concern about the availability of financial resources for maintaining the investment prospects in the economy. The decline in saving rate has been on account of deceleration in the saving rate of almost all the sectors viz. households, private corporate and government. The saving rate of government sector was almost zero. This has contributed to fall in gross domestic investment from 26.2 per cent in 1997-98 to 23.4 per cent in 1998-99 (Table 1.2).

The distribution of households' financial savings among various financial instruments brings out the relative importance of securities market as an investment option for the households( Table 1.3). The instrument-wise distribution of households financial savings depicts that the share of households saving in the form of shares and debentures in their total financial savings, had increased from 2.1 per cent in 1997-98 to 2.4 per cent in 1998-99. On the other hand, the share of bank deposits decreased from 44.5 per cent to 36.9 per cent. Investment in the units of UTI did not show any improvement from 0.3 per cent in 1997-98. It is interesting to note that there has been a spurt in deposits of households with non-banking companies' from 4.4 per cent in 1997-98 to 7.4 per cent in 1998-99. The high growth of funds mobilised by the mutual funds has generated possibility of increase in investment in shares and debentures pushing up the their share in households financial savings in 1999-2000 (Table 1.3).

Developments on external front are very important as far as the capital market is concerned. According to provisional data, net FIIs inflows showed an increase of US$2.1 billion whereas FDIs inflows stood at US$2.17 billion during 1999-2000. The balance of payment data reflected an overall balance surplus of US$ 6.4 billion during 1999-2000.

**Table 1.3: Savings of the Households Sector in Financial Assets** ***(Rs. in crore)***

| Item | 1992-93 | 1993-94 | 1994-95 | 1995-96 | 1996-97 | 1997-98P | 1998-99$ |
|---|---|---|---|---|---|---|---|
| Savings(Gross) of the | 80,387 | 109,485 | 145,381 | 124,986 | 157,424 | 178,576 | 207,841 |

| | | | | | | | |
|---|---|---|---|---|---|---|---|
| Household Sector in Financial<br><br>Assets of which | | | | | | | |
| Currency | 6,562 | 13,367 | 15,916 | 16,525 | 13,643 | 12,780 | 22,131 |
| | (8.2) | (12.2) | (10.9) | (13.2) | (8.7) | (7.2) | (10.6) |
| Bank Deposits # | 29,550 | 36,200 | 55,834 | 39,995 | 57,367 | 79,514 | 76,590 |
| | (36.8) | (33.1) | (38.4) | (32.0) | (36.4) | (44.5) | (36.9) |
| Non-banking Deposits | 6,035 | 11,654 | 11,547 | 13,198 | 21,411 | 7,775 | 15,376 |
| | (7.5) | (10.6) | (7.9) | (10.6) | (13.6) | (4.4) | (7.4) |
| Life Insurance Fund** | 7,114 | 9,548 | 11,370 | 13,894 | 16,188 | 19,431 | 22,766 |
| | (8.8) | (8.7) | (7.8) | (11.1) | (10.3) | (10.9) | (11.0) |
| Provident and Pension Fund | 14,814 | 18,226 | 21,295 | 22,292 | 26,248 | 32,808 | 38,742 |
| | (18.4) | (16.6) | (14.6) | (17.8) | (16.7) | (18.4) | (18.6) |
| Claims on Government + | 3,885 | 6,908 | 13,186 | 9,588 | 11,701 | 22,164 | 27,004 |
| | (4.8) | (6.3) | (9.1) | (7.7) | (7.4) | (12.4) | (13.0) |
| Shares and Debentures ++ | 8,212 | 10,067 | 13,474 | 8,839 | 6,696 | 3,777 | 4,935 |
| | (10.2) | (9.2) | (9.3) | (7.1) | (4.3) | (2.1) | (2.4) |
| Units of Unit Trust of India | 5,612 | 4,705 | 3,908 | 262 | 3,776 | 595 | 565 |
| | (7.0) | (4.3) | (2.7) | (0.2) | (2.4) | (0.3) | (0.3) |

Due to Changes in Coverage of non-banking deposits, figures prior to 1998-99 are not strictly comparable with those of 1998-66

These data are compiled /revised in December 1999 and hence, do not tally with the Quick Estimates of CSO released in February 1999. Constituents may not add up to total due to rounding off.

Figures in brackets indicate percentages to total Financial Assets of households.

# Includes deposits with Co-operative non-credit societies.

** Includes State / Central Government and postal insurance fund. + Includes compulsory deposits.

++ Includes investment in shares and debentures of credit / non-credit societies, public sector bonds, and investment in mutual funds (other than UTI)

$ Tentative Estimates

Source : Report on Currency and Finance 1998-99, RBI

On the other hand inflows on account of FIIs showed positive increases of Rs.1,187 crore as against decline of Rs.390 crore during the entire year of 1998-99. The better performance on account of FIIs inflows was supported by the stability of exchange rate policy of country and improvement in prospects of capital appreciation in the investment in Indian stocks. FIIs investment in equity and debt amounted to more than $ 2 billion during April-March 1999-2000 compared to a negative inflow of $386.1 million during 1998-99. The healthy outlook for FIIs investment in the Indian stocks is expected to grow. Some improvement in stability and credibility of East Asian countries and other financial markets in Asia, relaxation by Government of India in the limit of FIIs investment to 40 per cent in the Union Budget 2000-01, has created more prospects for FIIs investment. The picking up of exports growth and rise in the level of foreign exchange reserve to US $ 33 billion as on alongwith higher GDP growth during 2000-2001 is expected to build up and improve the FIIs investment sentiments.

The decline in external Debt-GDP ratio and debt service ratio from 23.8 per cent and 19.1 per cent in 1998 respectively to 23.7 per cent and 18.1 per cent in 1999 augur well for prospective FIIs investments in India.

Investment activity in the primary market increased during 1999-2000. The total resource mobilisation by the primary market which stood at only Rs.5,586 crore during 1998-99 through 58 issues, sharply increased to Rs.7,817 crore through 93 issues during 1999-2000, thus recording a growth of 40 per cent. During the previous year, the growth was 22 per cent. This increased growth in 1999-2000 was contributed by the increases in public and rights issues, which recorded a growth of 25 per cent and 175 per cent, respectively. In absolute terms, the rights issues and public issues contributed an incremental amount of Rs.1,248 crore and Rs.933 crore respectively each during the year. It is important to note that there has been a decline in the share of financial institutions and banks in total resource mobilisation from the primary market, from 85 per cent during 1998-99 to about 52 per cent in 1999-2000 and an increase in participation by the manufacturing and other companies. This is an evidence of growing dis-intermediation in the capital market. Another important development was floatation of larger number of issues by new companies (IPOs) increasing their share to 35.0 per cent during 1999-2000 from a meagre share of 7.8 per cent during 1998-99. The issues by information technology and other knowledge-based companies were on the rise during the year, in keeping with the worldwide trend. Thus new economy companies mobilised close to 20 per cent of total resources raised during the financial year under review. Health and entertainment companies also raised resources offering the opportunity of diversification of investment for investors.

The bullish trend in the secondary market during the year under review was accompanied by a rise in the market capitalisation. As such, the market capitalisation at NSE increased from Rs.4,91,175 crore as at end March 1999 to Rs.10,20,426 crore as at end March 2000, a rise of 107.8 per cent. The market capitalisation at BSE increased from Rs.5,45,361 crore as at end-March 1999 to Rs.9,12,842 crore as at end- March 2000 recording a growth of 67.4 percent.

FII investments during the year remained positive with the net investment at US$ 2.4 billion compared to a net outflow of US$ 386.1 million during 1998-99. The cumulative net investment rose to US$11,253 million at end March 2000 from US$8897 million at end March 1999.

The performance of mutual funds significantly improved during the year. The aggregate net mobilisation increased to Rs.18,970 crore during 1999-2000 as against net outflow of the order of Rs.950 crore during 1998-99. While mutual funds under public sector continued to perform poorly with a net outflow of the order of Rs.745 crore in the current financial year, the private sector mutual funds added a net amount of Rs.15,166.48 crore and UTI another Rs.4548.3 crore. The spurt in mutual funds resources has been the result of tax incentives provided by the Union Budget 1999-2000. Efforts of RBI in lowering the interest rates structure is also resulting in shift of bank deposits to mutual funds. The regulatory framework of the mutual funds was also responsible for the improvement in the performance of this sector.