"A LEADING INDEX FOR INDIA'S EXPORTS"

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INTRODUCTION

With the recent increase in globalization of the Indian economy, policy makers, businesses, and financial analysts are closely tracking the external sector. A key driver in the external sector is the level of exports because it directly impacts the domestic economic performance. Since exports can affect fluctuations in the growth rate and the level of overall economic activity, it is essential to construct an accurate and reliable tool for forecasting the direction of change of the level and growth rate of exports. This study reports such a measure – the leading index for exports – that predicts movements in real exports, price of exports, and the value of exports respectively.

The leading indicator approach to business and economic forecasting is based on the premise that market-oriented economies experience business cycles that consist of "expansions occurring at about the same time in many economic activities, followed by similarly general recessions, contractions and revivals that merge into the expansion phase of the next cycle; this sequence of changes is recurrent but not periodic" (Burns and Mitchell, 1946). The leading indicator approach therefore predicts these repetitive sequences of the business cycle.

This study focuses on the external sector of the Indian economy. Since the external sector is expected to be driven largely by other countries' economic cycles, it will typically not be in synchronization with domestic business cycles. For this reason, a leading index for the aggregate domestic economy may not be a satisfactory predictor of the external sector. Hence, a separate, specialized leading index is required to forecast cycles in the external sector. This study constructs such an index to predict movements in exports.

Part I presents an overview of the external sector in the Indian economy. Part II describes the underlying rationale for constructing a leading index for exports. It also outlines the methodology for construction. Part III comments on the performance of the leading index for the three target variables – real exports, price of exports, and the value of exports over the past 25 years. It also evaluates the leading index with respect to lead profiles. The section that follows concludes the study and notes the limitations of the present study.