January 31, 2017

Indian Economic Survey 2016-17

1. The Economic Survey 2015-16 had predicted the Indian economy to register the GDP growth rate in the range of 7% to 7.75%. The economy was indeed treading along that path and clocked 7.2 % in the H1- FY 2016-17. Post the demonetisation, expected slowdown in the rate of real GDP growth reduced by 0.25% to 0.5% points relative to the baseline of about 7% still makes India's growth substantial; given the weak and unsettled global economy registering 3% growth in 2016.
2. In FY2016-17, there were two major domestic policy developments: clearance on implementing the transformational Goods and Services Tax (GST) and demonetisation of the two highest denomination notes, Rs. 500 and Rs. 1,000. These moves seem to be costly in the short term but hold the potential for long term benefits. Follow-up actions to minimize the costs and maximise the benefits include: fast, demand-driven remonetisation; further tax reforms, including bringing land and real estate into the GST, reducing tax rates and stamp duties. These actions would allow growth to return to trend in FY 2017-18, post the temporary decline in FY 2016-17.
3. Over the last 30 years, India's growth performance has been robust, backed up by policy reforms that have made India more open to flow of goods and capital and have reduced the size of the public sector. The challenges faced includes ambivalence about property rights and the private sector, deficiencies in state capacity, especially in delivering essential services, and inefficient redistribution.
4. India's Twin Balance Sheet Problem - overleveraged companies and bad-loan-encumbered banks -- using a decentralised approach leading to rise in NPAs while credit and investment are declining. A need for different approach with a centralised Public Sector Asset Rehabilitation Agency that could take charge of the largest, most difficult cases, and make politically tough decisions to reduce debt.
5. India's experience of fiscal activism has been unsuccessful and highlighted the risk of relying on rapid growth rather than steady primary balance adjustment to reduce debt, a strategy that has failed to place the debt-GDP ratio firmly on a downward path.
6. Over the last few years, most states in India have achieved and maintained the target fiscal deficit level (3% of GSDP) and eliminated the revenue deficit soon after the introduction of their Fiscal Responsibility Legislation (FRL).
7. China has lost its dominant position in apparels and leather manufacturing due to rising labor costs, thus creating an opportunity for India. To retain its domination from competitors like Vietnam and Bangladesh, India will require easing restrictions on labor regulations, negotiating FTAs with major partners such as the EU and UK.
8. The investment to GDP ratio has not only been lower than the desirable levels but has been consistently declining over the last few years. An increase in international prices of crude oil & other commodities like coal, etc. could exert inflationary pressure and have the potential to adversely impact the trade and fiscal balances. The outlook for the next financial year suggests that growth is set to recover, as the currency in circulation returns to normal levels by considering the significant reform measures initiated by the government.

9. This survey also highlights Universal Basic Income (UBI) – a guaranteed minimum income to each individual. This scheme is expected to be an add-on to the current anti-poverty and social programs, which would make it fiscally unaffordable.
10. Despite rapid overall growth, there is striking evidence of divergence, or widening gaps in income and consumption across the Indian states. A striking feature is that the trade in goods and movement of people—are stronger within India than they are across countries. India’s internal trade-GDP ratio at about 54% is comparable to that of other large countries.
11. It is observed that there exists a high level of internal work related migration in India. Rising growth after the 1980s has led to an acceleration of labor migration flows as the rewards of better economic opportunities have overcome the costs of moving. Surprisingly, language does not seem to be a serious barrier to internal economic integration.

Watch out for KNAV’s exclusive coverage of the Union Budget 2017 to be unveiled on February 1, 2017 by India’s Finance Minister.