State of the economy : Temper the euphoria

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Context:

In its semiannual report, World Economic Outlook, 'Navigating Global Divergences' October 2023, the International Monetary Fund (IMF) has revised its projected GDP growth rate for India for 2023-24 to 6.3%, up from the earlier 6.1%. For India's policymakers, it is a vindication of their short term economic management. Official spokespersons have sought the IMF's endorsement to silence its critics.

Performance of Indian economy:

1. That the economies that were worst affected during the COVID19 pandemic were also the ones to record a steep recovery is widely acknowledged. India, which was one of the worst affected, has followed the pattern.
2. During the second quarter of 2020, India's GDP contracted by 25.6%, quarter on quarter, the worst among the world's major economies in 2020. Taking a slightly longer view, India's real (inflation adjusted) annual GDP growth rate slowed down from 6.8% in 2016-17 to 2.8% in 2019-20, immediately prior to the pandemic.
3. Real per capita income level in 2021-22, at ₹1.09 lakh, was higher than that in 2019-20 by about ₹600. In the following year, 2022-23, recovery gained momentum as domestic supplies were restored and global supply chains were straightened out.

Effects are cause for concern:

1. Surely, output recovery is welcome, yet its effects on employment, its quality and persistence of inflation of essential food items affecting the poor the most remain causes of concern — as many critics have highlighted. However, even focusing on output recovery, a sectoral view with trade dimension, would perhaps expose chinks on the armour.
2. Policymakers need to temper their optimism by taking a slightly longer view with a wider angle — appreciating the fast changing geopolitical underpinnings of economic policy making. It perhaps bears repetition that 2022-23 heralded the end of globalisation as we knew it (since the Berlin Wall's collapse in 1989) with tectonic shifts in the world geopolitical order, revealing India's persistent vulnerabilities of oil and food shocks.

Growing deficit with China:

1. However, the immediate concern is India's susceptibility to its soaring deficit with China. India's economic frailty has increased even as the net exports (exports minus imports) to GDP ratio has declined sharply.
2. India's dependence on Chinese imports of manufactures seems structural, and not easily corrected by changes in relative prices. In May 2020, the government initiated the

Atmanirbhar Bharat Abhiyan, amidst the Galwan crisis to curb Chinese imports of critical industrial products. China accounts for: 15%- 16% of India's imports and a third of India's trade deficit.

3. Willy nilly, India undid many import restrictions, as domestic production was getting throttled for lack of critical Chinese inputs. Industrial growth rates as per the Index of Industrial Production (IIP), despite its limitations, shows an alarming regression over a longer period. During the boom period (2004-05 to 2013-14), manufacturing grew at an annual average rate of 5.7%.
4. From 2011-12 to 2021-22, gross fixed capital formation (GFCF) to GDP ratio at current prices, declined steadily from 34.3% to 28.9% — an unprecedented fall in post independent India. And its public sector share has remained constant at 8% (National Accounts).
5. Net foreign direct investment (FDI excluding disinvestment and outward foreign direct investment), to current GDP ratio fell from 3.6% in 2008 to 2.4% in 2022 (World Development Indicators). The official optimistic picture of public investment growth since FY22, based on budgetary statistics, seems suspect.

Public investment has three parts:

1. Investment by government
2. Central public sector undertakings (PSUs)
3. State PSUs
4. Public investment by State governments, based on the Centre's loans and advances to States, is conditional upon policy reforms. The widely reported rise in the Centre's investment is apparently due to the merging of extrabudgetary borrowing by central PSUs with the Centre's own Budget. Hence, the projected boost in public investment seems illusory. Combining the three items, public investment seems around 6% of GDP — perhaps similar to its pre-COVID-19 levels.

Credibility of the HDI:

1. On social development, official spokespersons and critics have battled over the veracity of multidimensional poverty measure (MPI), and the unrepresentativeness of the Global Hunger Index (GHI). Instead, the UN Development Programme's Human Development Index (HDI) may be more credible and an acceptable measure.
2. The value of India's HDI index moderated from 0.645 in 2018 to 0.633 in 2021; and, its global rank went down by one rank during 2015 to 2021 — meaning that other countries have performed better than India.

Concerns:

To sum up, our economic recovery is weak with following concerns:

1. Strategic threat posed by an unrelenting rise in trade deficit with China, despite government's best efforts
2. Its mirror image is a decline in industrial output growth rates, especially capital goods' decimation
3. A decade long, unprecedented, decline in the economy's fixed investment rate; with an unchanging public sector's share in it,
4. India's HDI ranking slipping

Conclusion:

Official commentators would perhaps do well to engage with its critics in appreciating the gravity of economic setbacks in recent years than scoring brownie points over the IMF’s short term growth projections.