India after the Global Crisis

by

Shankar Acharya *

ICFAI Foundation for Higher Education (IFHE),
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• Honorary Professor, ICRIER (former Chief Economic Adviser to the Government of India, 1993-2001)
India's GDP growth since 1991/92

percent

## THE HALCYON YEARS, 2003 - 8

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<tbody>
<tr>
<td>Economic Growth (% per year)</td>
<td>8.9</td>
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<tr>
<td>Inflation (GDP deflator, % per year)</td>
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<td>Current Account Deficit (% of GDP)</td>
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<td>Gross Domestic Investment (% of GDP)</td>
<td>33.8</td>
<td>24.2</td>
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### Key Points/ Trends
- 5 Year growth at all-time high (compare previous 5 year high)
- Inflation moderate
- Current account deficit low
- Combined fiscal deficit down from 8.5% of GDP 2003/4 to 4% in 2007/8
- Gross Investment surges from 27% of GDP in 2003/4 to 38% in 2007/8
- Supported by strong domestic savings surge.
Major Causes of 2003–8 Growth / Investment Boom


4) Surge in domestic savings because of big drop in government dis-savings and strong rise in corporate savings. Gross investment rate surged from 25% of GDP to over 35%.

5) Caught the global boom in services (IT, Telecom, Finance etc.). India’s service exports increased @ 25% per year between 2001 and 2008.

## India’s Growth Resilient in Crisis

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<tbody>
<tr>
<td>World output(^a)</td>
<td>3.8</td>
<td>1.6</td>
<td>-2.1</td>
<td>4.2</td>
<td>2.8</td>
<td>2.7</td>
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<tr>
<td>Advanced economies</td>
<td>2.8</td>
<td>0.2</td>
<td>-3.4</td>
<td>3.2</td>
<td>1.6</td>
<td>1.4</td>
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<tr>
<td>United States</td>
<td>2.6</td>
<td>0.0</td>
<td>-2.6</td>
<td>3.0</td>
<td>1.7</td>
<td>2.0</td>
</tr>
<tr>
<td>Euro area</td>
<td>2.6</td>
<td>0.4</td>
<td>-4.1</td>
<td>1.9</td>
<td>1.5</td>
<td>-0.3</td>
</tr>
<tr>
<td>Japan</td>
<td>2.1</td>
<td>-1.2</td>
<td>-6.3</td>
<td>4.4</td>
<td>-0.7</td>
<td>2.4</td>
</tr>
<tr>
<td>Emerging-market and developing economies</td>
<td>8.1</td>
<td>6.1</td>
<td>2.8</td>
<td>7.5</td>
<td>6.2</td>
<td>5.6</td>
</tr>
<tr>
<td>Russia</td>
<td>7.7</td>
<td>5.2</td>
<td>-7.8</td>
<td>4.3</td>
<td>4.3</td>
<td>4.0</td>
</tr>
<tr>
<td>China</td>
<td>12.7</td>
<td>9.6</td>
<td>9.2</td>
<td>10.4</td>
<td>9.2</td>
<td>8.0</td>
</tr>
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<td>India(^b)</td>
<td>9.5</td>
<td>6.8</td>
<td>8.4</td>
<td>8.4</td>
<td>6.5</td>
<td>6.0</td>
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<td>4.4</td>
<td>5.2</td>
<td>-0.6</td>
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\(^a\) At market exchange rates.
\(^b\) For India, the years are April to March financial years, so 2008 refers to 2008–09 and so on for subsequent years.

**Sources:** International Monetary Fund, *World Economic Outlook* (WEO), April 2011, for data up to 2008; WEO Update (June 2011) for 2009; and WEO Update (July 2012) for 2010 onward. Data for India are from the Central Statistical Organization.
Factors Explaining Resilience

- Momentum of rapid growth and high investment in 2003 – 8.
- Transmission channels of global financial crisis blunted by conservative financial sector policies of RBI; strong regulation of banks; cautious approach to Capital Account Convertibility, etc.
- Extraordinary fiscal profligacy of Central Govt. in 2008 on wage increases (6th Pay Commission), huge subsidies (food, fuel, fertilizer), roll-out of entitlement programmes (NREGA) and farm loan waiver. Centre’s fiscal deficit soared from 2.5% of GDP (budgeted) to 8% of GDP!
- RBI quick to sharply reduce policy rates and boost domestic liquidity (Repo rates dropped from 9% in Sept. 2008 to 3.25% in April 2009). Also allowed exchange rate to depreciate.
- Initial promising recovery of global economy in late 2009 and 2010.
But Macro-Indicators weaken after 2008

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<td>Current account balance (percent of GDP)</td>
<td>−0.3</td>
<td>−1.3</td>
<td>−2.3</td>
<td>−2.8</td>
<td>−2.6</td>
<td>−4.2</td>
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<td>Gross domestic investment (percent of GDP)</td>
<td>33.8</td>
<td>38.1</td>
<td>34.3</td>
<td>36.6</td>
<td>35.8</td>
<td>35.5</td>
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<tr>
<td>Gross fixed investment (percent of GDP)</td>
<td>29.6</td>
<td>32.9</td>
<td>32.3</td>
<td>31.6</td>
<td>30.4</td>
<td>29.5</td>
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Source: Central Statistical Organization and Reserve Bank of India
Major Causes of Weakening Macro Performance

1) Little significant reforms since 2004.


3) Exit from fiscal spending/ deficit surge of 2008/9 proving difficult. Keeping inflation and medium-long interest rates high.

4) Drop in domestic savings because of high government dis-saving and decline in corporate savings.

5) Mismanagement of exchange rate in 2009 -10: excessive nominal and real appreciation fuelled rising trade and current account deficits and hurt industry.

6) Emergence of serious scams (spectrum, mining, big projects) and “coalition compulsions” distracted and stalled governmental decision-making.

7) Tightening regulatory and pricing bottlenecks in energy, mining and land allocation.
Crisis Building in 2012 Summer

1) External liquidity (BoP) crisis.
2) Financial sector Stresses.
3) Crisis in energy/ infrastructure sectors.
4) Prospect of slow (5 – 6%) growth for several years.
5) Bleak outlook on medium-term employment prospects for India’s “youth bulge”; OR “demographic dividend” could became a nightmare.
6) Weakening of India’s national security in a dangerous neighbourhood.
Policy Priorities: Near Term

A) Reduce growing fiscal deficit:
   • Increase POL and fertilizer prices
   • Slowdown on entitlement programmes

B) Resurrect Reform Thrust:
   • Implement FDI in Retail and other sectors.
   • Fast-track Goods and Services Tax (GST)
   • Push pending laws on insurance, banking and pensions.

C) Restore Investor Confidence:
   • Reverse bad tax measures of 2012 Budget.
   • Unblock logjam in major infrastructure sectors such as power, coal, roads, telecom, etc.
Policy Priorities : Medium Term

• Revamp of energy sector policies.

• Reform of Land, Water and Natural Resource allocation systems.

• More flexible labour laws and better skill development to realize demographic dividend.

• Meeting challenge of Urbanization.
Thank You