India after the Global Crisis

by

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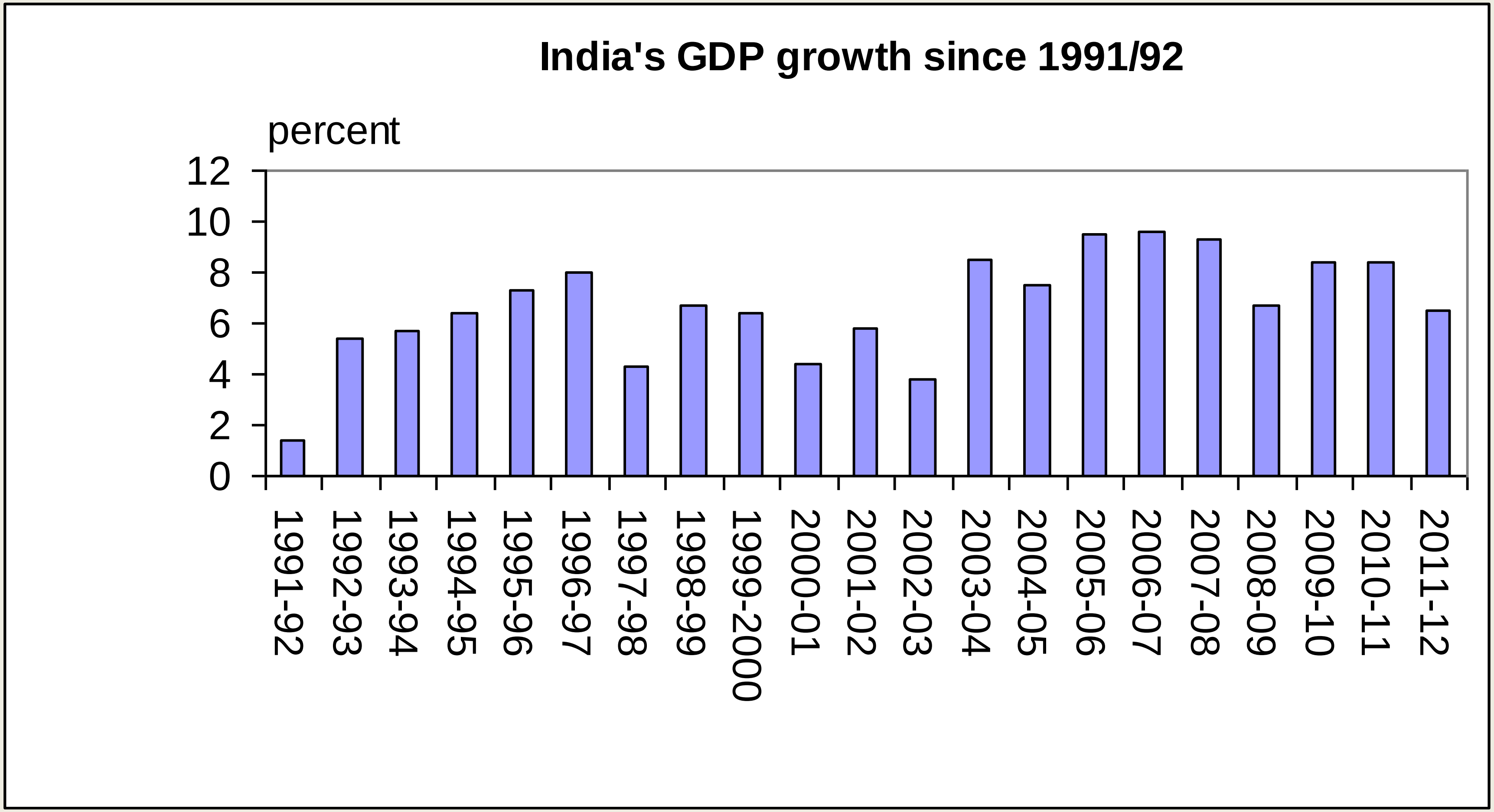
India's GDP growth since 1991/92
percent
12
10
8
6
4
2
0
1991-92
1992-93
1993-94
1994-95
1995-96
1996-97
1997-98
1998-99
1999-2000
2000-01
2001-02
2002-03
2003-04
2004-05
2005-06
2006-07
2007-08
2008-09
2009-10
2010-11
2011-12

THE HALCYON YEARS, 2003 - 8

	2003/4–2007/8	1992/3–1996/7
Economic Growth (% per year)	8.9	6.6
Inflation (GDP deflator, % per year)	5.6	9.1
Current Account Deficit (% of GDP)	0.3	1.1
Combined Fiscal Deficit (% of GDP)	6.3	7.1
Gross Domestic Investment (% of GDP)	33.8	24.2

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

1) Cumulative **reforms of 1991 – 2003.** Private sector boom in new globalized environment.

2) Liquidity-fuelled **Global boom of 2002 – 2007. Boosted international trade, capital flows and technology transfer.**

3) Strong fiscal consolidation of 2003 –2008 (FD down from 9.6% of GDP in 2002/3 to 4.1% in 2007/8) meant **lower interest rates** and **ample availability of funds**. Fuelled high investment.

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.

6) Deft **management of exchange** rate, till 2007. Prevented excessive appreciation of rupee despite surge in Capial inflows.

India’s Growth Resilient in Crisis

Country	2005–07	2008	2009	2010	2011	2012 (projected)
World output[a]	**3.8**	**1.6**	**–2.1**	**4.2**	**2.8**	**2.7**
Advanced economies	**2.8**	**0.2**	**–3.4**	**3.2**	**1.6**	**1.4**
United States	2.6	0.0	–2.6	3.0	1.7	2.0
Euro area	2.6	0.4	–4.1	1.9	1.5	–0.3
Japan	2.1	–1.2	–6.3	4.4	–0.7	2.4
Emerging-market and developing economies	**8.1**	**6.1**	**2.8**	**7.5**	**6.2**	**5.6**
Russia	7.7	5.2	–7.8	4.3	4.3	4.0
China	12.7	9.6	9.2	10.4	9.2	8.0
India[b]	**9.5**	**6.8**	**8.4**	**8.4**	**6.5**	**6.0**
Brazil	4.4	5.2	–0.6	7.5	2.7	2.5

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

Indicator	Average (2003–04 to 2007–08)	2007–08	2008–09	2009–10	2010–11	2011–12
Economic growth (GDP, percent per year)	8.9	9.3	6.7	8.4	8.4	6.5
Inflation (GDP deflator, percent per year)	5.6	6.6	8.5	8.1	10.6	8.8
Current account balance (percent of GDP)	–0.3	–1.3	–2.3	–2.8	–2.6	–4.2
Combined fiscal deficit (percent of GDP)	6.3	4.1	8.5	9.5	7.0	8.2
Gross domestic investment (percent of GDP)	33.8	38.1	34.3	36.6	35.8	35.5
Gross fixed investment (percent of GDP)	29.6	32.9	32.3	31.6	30.4	29.5

Source: Central Statistical Organization and Reserve Bank of India

Major Causes of Weakening Macro Performance

1) **Little significant reforms** since 2004.

2) **Global environment continues weak** post 2007-9 global crisis.

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.

Crises 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