Guess paper MAINS 2019

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SESSION - 23

DATE- 7 September 2019

WHY 5% GDP GROWTH IN INDIA

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India's gross domestic product (GDP) growth rate slowed to a six year low of 5% in the first quarter of the 2019-20 financial year. The last time the GDP grew slower was in the fourth quarter (January to March) of the financial year 2012-13, according to data with the Ministry of Statistics.

Apart from slowdown in manufacturing and construction, the steep decline in consumption is a big cause for worry. The slowdown has been across most segments — **mining, manufacturing, and construction** — as indicated by the index of industrial production (IIP) data too. The sharp slowdown in **financial, real estate and professional services and private final consumption** on the expenditure side, is particularly worrisome.

Automobile sales, a barometer of the economy, have declined sharply in recent months, forcing production cuts and jobs losses. The government has offered incentives on auto purchases to help revive demand. Weak global economy and trade tensions have kept export growth muted.

While the real GDP growth has fallen from 8 per cent last year to 5 per cent this fiscal in the Apr-June quarter, the **sharp fall in nominal GDP growth from 12.6 per cent to 8 per cent** during this period, is worrisome.

The **GDP deflator** (growth in ratio of nominal to real GDP) — another measure of inflation — has **fallen from 4.3 per cent last year to 2.8 per cent currently**. If high inflation hurts consumers, low inflation also has an impact on India Inc. and consumers. While falling food prices hurt agriculture income and spending, overall inflation also has a bearing on the wage growth and income levels across industries. Nominal GDP, also decides the credit requirement of a corporate, and hence impacts the growth in bank credit. CPI inflation has fallen from 7.4 per cent levels five years ago to 3.per cent recently.

Also, the Centre has managed to retain a comforting **3.3 per cent on fiscal deficit**, by assuming 11 per cent growth in nominal GDP growth for FY20 (from CSO's FY19 estimates). Given the current sharp slowdown in growth and the underlying trend in inflation, such growth appears a tall task. The subdued growth is already **impacting tax revenues** for the government.

This is the second consecutive quarter that India has fallen behind China. **India's "fastest growing economy" tag is in danger.**

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REASONS

- Domestic consumption slowdown in India.
- Exports have not risen substantially to compensate for the same.
- Economic disturbances like demonetization, GST and changes in the banking system have led to uncertainty and thus economic slowdown.
- Global activities like trade war and protectionism have a role to play too.
- Very high unemployment rates (45-year high) have taken a toll on private consumption and investment.
- Government funds are pressed between cleaning the banking sector through recapitalization and controlling the fiscal deficit.
- Agriculture, manufacturing, construction, etc – all sectors are facing a slowdown, creating a vicious cycle.
- Banking crisis, including the NBFCs, has severe impact on credit availability and market liquidity.
- The private sector, including startups, also complaints of oppressive tax laws.

WAY FORWARD

- Increase rural income through various measures, especially by making agriculture remunerative.
- Tax reforms, including lower tax rates and easier payment systems, are important to increase the tax revenue, so that, government can compensate for declining private investment.
- Employment creation by upskilling the youth and filling government vacancies.
- Move towards an export-oriented economy, from an import-oriented one.
- Move to alternative fuels from fossil fuels, to reduce India's dependence on imports and hence, global disturbances.
- Proper planning before implementation of any major reforms like demonetization.
- Cleaning up the banking sector at the earliest, without wasteful use of taxpayers' money, by undertaking governance reforms and holding the culprits accountable.

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CONCLUSION

In the past week, the government has **announced a package of measures** such as liberalising FDI for select sectors, ensuring flow of credit to non-banks, rollback of a controversial tax surcharge on foreign portfolio investors, more capital for banks and a big-bang bank consolidation.

Independent experts (including RBI), however, expect the slowdown to persist for a while and see **another rate cut by the central bank** in October after the 110 percentage points slashed in this round of monetary easing. Even, **RBI**, in its recent report, said that the slowdown is a **cyclical one, rather than structural**. If it were structural, it would have required more reforms.

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