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Indian Economy Review

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Economy robust, but downside risks dominate upside potential

The Union finance ministry's Monthly Economic Review for March, released on April 25, has flagged a few areas of concern, even as it maintains that the Indian economy continues to be robust. The positive factors come from the potential for higher gross domestic product (GDP) growth in 2023-24 and a healthier mix of government expenditure with the ratio of revenue expenditure to capital expenditure being lower than in the past. The Reserve Bank of India has raised its growth forecast for India to 6.5 per cent and aligned it with the government's estimate of 6.5 per cent growth in 2023-24. The growth estimate upgrade comes even as the International Monetary Fund has cut its forecast for India to 5.9 per cent in the current year, compared to its earlier estimate of 6.1 per cent. The growth estimates for 2023-24 made by other agencies, however, confirm that India's growth would slow down from 7 per cent in 2022-23, but be higher than the estimates for China or any other large economy. The estimates for 2023-24 are: 6.3 per cent by the World Bank, 6.4 per cent by the Asian Development Bank, 5.9 per cent by the Organisation for Economic Cooperation and Development, 6 per cent by Standard & Poor's, 6 per cent by ICRA and 5.9 per cent by India Ratings. Significantly, the Monthly Economic Review notes that "downside risks to our official forecast of 6.5 per cent for real GDP growth in FY24 dominate upside risks." The report has outlined the downside risks in detail. It notes: "OPEC's surprise production cut has seen oil prices rise in April, off their lows of low-seventies per barrel in March. Further troubles in the financial sector in advanced nations can increase risk aversion in financial markets and impede capital flows. Forecasts of El Nino, at the margin, have elevated the risks to Indian monsoon rains." How the Indian economy fares in the coming months would have to be keenly watched by the government.

Positive monetary policy surprise, but inflation still a worry

The Monetary Policy Committee (MPC) of the Reserve Bank of India (RBI) sprang a positive surprise for the markets on April 6. Even as most market players, analysts and experts expected a 25-basis-point increase in the repo rate (at which scheduled commercial banks can borrow from the central bank against government securities), the MPC decided to keep the rate unchanged at 6.5 per cent. This was the first pause in the RBI's monetary policy stance since it began raising the rates from May 2022. In almost a year, the repo rate had been raised from 4 per cent to 6.5 per cent. The surprise over the pause was also caused by two sets of data that were available to the MPC members – on retail inflation and economic growth. Inflation based on the movement in the Consumer Price Index in January and February 2023 had stayed above 6 per cent, the upper end of the tolerance band of the RBI. The retail inflation target that the central bank must adhere to is 4 per cent. Economic growth projection for 2023-24 was revised upwards to 6.5 per cent, compared to the earlier number of 6.4 per cent. For 2022-23, the central bank believed that growth would be about 7 per cent, the same as indicated by the National Statistical Office of the government. What might have influenced the MPC to declare a pause on repo rate increases could be its assessment that retail inflation during 2023-24 would stay range-bound at around 5 per cent in each of the four quarters, but real economic growth might see a deceleration from 7.8 per cent in the first quarter of 2023-24 to 5.9 per cent in the final quarter of the current year. A view shared by a couple of the MPC members, which must have influenced the rate pause decision, was that the transmission of the impact of the 2.5 percentage points increase in interest rates in the last one year would be staggered and the next rate hike decision should depend on how well the past increases have impacted the liquidity situation. On the other hand, core inflation in February 2023 remaining sticky at 6.35 per cent was a cause for concern as far as the RBI's primary goal of ensuring price stability was concerned. The next monetary policy review due to be held in June 2023 should provide greater clarity on the central bank's approach to both managing inflation and nurturing growth.

Budget passed without debate; least sittings in 17th Lok Sabha

Such was the state of play in the Budget session of Parliament, which ended in the first week of April, that even Finance Minister Nirmala Sitharaman expressed her anguish over the way the Union Budget for 2023-24 had to be passed by Parliament without any meaningful debate. No proper discussion had preceded the passage of the Budget in the Lok Sabha on March 23. Four days later, the Rajya Sabha returned the Finance Bill to the Lok Sabha, again without any major discussion. What got passed without a proper discussion was a Budget that entailed a total expenditure of Rs 45 lakh crore during 2023-24. Worse, as many as 102 demands for grants for different central ministries were "guillotined" before being passed by Parliament. Enforcing a guillotine on demands for grants is a device used when no deliberation of the proposals put forward in a Budget takes place. Similarly, the Appropriation Bill, which empowers the government to withdraw money from the Consolidated Fund of India to spend under various schemes and projects, was passed quickly with hardly any debate. Also passed by a voice vote in the Lok Sabha were as many as 60 amendments to the Finance Bill, mooted by the government and many of them pertaining to significant changes in taxation rules. All these developments took place as India's parliamentarians were busy settling political scores and unfortunately found those issues more important than the annual financial statement of the government, the state of public finances, expenditure outlays of the Centre and new taxation proposals. A study by the PRS Legislative Research revealed a far more worrying trend. It noted that the 17^{th} Lok Sabha, which entered the final year of its term with the Budget session of 2023, had so far functioned for 230 sitting days. It also found that among all the Lok Sabhas which had completed a full five-year term, the 16^{th} Lok Sabha had recorded the lowest sitting days of 331. The study now notes that with just one year remaining in the term of the 17^{th} Lok Sabha and with only 58 average sitting days in a year, the ongoing Lok Sabha was unlikely to sit for more than 331 days. This could make the 17^{th} Lok Sabha flaunt the dubious record of having the lowest number of sitting days among all the lower houses of Parliament since 1952. That will be a sad commentary on the functioning of India's parliamentary democracy.

India's demographic challenge: Health care and education

A report, released by the United Nations Population Fund or UNPF, has shown that India would become the most populous country in the world with 1.429 billion people by the middle of 2023, surpassing China, whose population then would be 1.426 billion. While experts are debating over whether India would surpass China by the middle of 2023, comparisons between two of the world's most populous countries are instructive. On most socio-economic parameters, China is ahead of India. These parameters include life expectancy at birth (China: 82 years for women and 76 years for men; India: 74 years for women and 71 years for men) and per capita income at current $ prices (China: $13,721; India: $2601). But the big difference is in the demographic profile of the population in the two countries. The share of population in the age group of 10-24 years is 18 per cent in China, while it is much higher at 26 per cent in India. Similarly, the share of population in the age group of 65 years and above is 14 per cent in China and much lower at 7 per cent in India. Indeed, the share of population below the age of 25 years is almost 50 per cent in India. Population experts agree that India has a time-bound opportunity to take economic and social advantage from the demographic dividend that would be available for it to tap in the next couple of decades. The demographic transition as a youthful nation along with demographic diversity across states would be an opportunity for India. However, that would hugely depend on how well India strengthens its health care infrastructure and education facilities.

Merchandise goods exports decelerate, but service exports boom

India's exports performance in 2022-23 gave policy makers reasons for some serious introspection on how to sustain the growth, particularly, in merchandise goods. With the prospects of global demand for goods already turning a little bleak, India's merchandise goods exports could grow by only 6 per cent to $447 billion in 2022-23. This growth was an indication of how exports of goods have begun facing headwinds. In 2021-22, merchandise goods exports had grown by a massive 44 per cent to $422 billion. But in 2022-23, the performance was a let-down. Of the 30 export sectors (accounting for over 93 per cent of total merchandise exports), only petroleum products (up 40 per cent at $94 billion), electronic goods (up 50 per cent at $24 billion) and rice (up 15 per cent at $11 billion) did quite well. Readymade garments exports at $16 billion grew by just 1 per cent, while exports of chemicals and drugs rose by 3 per cent each to $30 billion and $25 billion, respectively. In contrast, exports from as many as 13 sectors (including engineering goods, gems and jewellery, cotton and man-made fabrics, carpets, plastics, iron ore and cashew) declined in 2022-23. This did not augur well for merchandise exports prospects in 2023-24. Nor did it improve the feasibility of reaching the $1 trillion exports target for 2029-30, which would require a compound annual growth rate or CAGR of 12 per cent during the next seven years, against a 4 per cent CAGR in the last ten years. More importantly, poor performance of merchandise exports in sectors such as engineering goods, gems and jewellery and fabrics, in particular, was no good news for the job scene in India's manufacturing sector. But the good news came from India's services exports, which rose to $323 billion in 2022-23, an increase of 27 per cent over the previous year. The services exports in 2021-22 at $254 billion also recorded a healthy 23 per cent rise. The redeeming feature of India's growing services exports was that it was driven not just by the information technology services, but also by a host other business services. About 1600 global capability centres are now operating from India and these centres account for over a third of the total such capacity in the world. The potential for exports from these centres is huge, although the kind of jobs that these centres can create require a high level of skills and the need for boosting manufacturing exports to provide jobs for semi-skilled workers or those graduating from the farm sector would still remain critical. But booming services exports can be a big relief to address India's rising dependence on crude oil importance, eating up a good chunk of India's foreign exchange earnings.

Steady GST growth; direct taxes up, but buoyancy falls

The Centre's tax collections during 2022-23 have been a cause for cheer. Latest government data suggest that its direct tax collections exceeded the Revised Estimate of Rs 16.5 lakh crore. What's more, the final number of Rs 16.61 lakh crore represented an 18 per cent growth over the previous year's number of Rs 14 lakh crore. Interestingly, the growth in personal income-tax collections has been sharper than that in corporation tax collections. However, the share of direct tax collections in India's gross domestic product. (GDP) has inched up marginally from 6 per cent to 6.11 per cent in this period. More worrying is the decline in the direct tax collections' buoyancy, which was down from 2.67 in 2021-22 to 1.13 in 2022-23, underlining the need for policy fixes to maintain healthy tax buoyancy. Collections of goods and services tax (GST) during 2022-23 were encouraging. On top of a 31 per cent growth in GST collections of Rs 14.8 lakh crore in 2021-22, the performance in 2022-23 showed another healthy rise of 22 per cent to Rs 18.1 lakh crore. Thanks to the coverage of more enterprises under the tax net with the use of technology and a reasonably foolproof e-invoicing system, the share of GST collections in GDP maintained a healthy rising trend – from 5.7 per cent of GDP in 2020-21 to 6.31 per cent in 2022-23 and to 6.65 per cent of GDP in 2022-23. The good news is that the overall tax collections by the Centre, including direct and indirect taxes (GST, excise and customs), would help it adhere to the Revised Estimate of the fiscal deficit of 6.4 per cent of GDP in 2022-23. The challenge ahead would be to improve tax buoyancy in the coming years. Hopefully, the new exemptions-free personal income-tax regime should widen the tax base and encourage more collections over the next few years. The bigger challenge would be to plan for a major rate rationalization for the GST regime to not only give a boost to economic activities but also sustain the government's revenue collections.

Decline in fresh formal job creation poses new challenges

Developments on the employment front have not been encouraging. The government's data on fresh formal job creation, released in the third week of April, showed a sequential decline for the third consecutive month. The payroll data, released by the Employees Provident Fund Organisation or EPFO, revealed that the number of new monthly subscribers under the EPF declined by 10 per cent to 7.38 lakh persons in February from 8.2 lakh in January. This level of new monthly subscribers was the lowest since May 2021, when an estimated 6.5 lakh new subscribers had joined the Fund. The decline in fresh formal job creation in February is worrying because this number had remained above the 1-million mark for each of the months in the first half of 2022-23 but began declining in subsequent months. The data, released by the Centre for Monitoring the Indian Economy or CMIE, also showed that the unemployment rate climbed from 7.5 per cent in February to 7.8 per cent in March 2023. The labour participation rate and the employment rate declined from 39.9 per cent to 39.8 per cent and from 36.9 per cent to 36.7 per cent, respectively, during this period. For the whole of 2022-23, the unemployment rate remained elevated at over 7 per cent for each of the quarters during the year, with the average monthly unemployment rate estimated at 7.6 per cent. The labour participation rate also settled at below 40 per cent in 2022-23, down from 40.1 per cent in 2021-22. Worryingly, the unemployment rate in the first four weeks of April continued to rise and was estimated at 8.2 per cent as at the end of April 28.

Monsoon forecasts create uncertainties for agriculture output

India's monsoon outlook for the current year appears a little clouded. On April 11, the India Meteorological Department (IMD), the state-run official weather agency, released its assessment of the monsoon prospects this year, which contradicted the forecast made by Skymet, a private agency, just a day earlier. The IMD predicted normal rains during the four months of June to September in 2023, estimated at 96 per cent of the Long Period Average (LPA). And this forecast was despite the onset of El Nino conditions that are expected to affect the smooth spread of the monsoons. El Nino conditions are created due to the warming of waters in the Pacific Ocean near South America, thereby weakening the monsoon winds. A day earlier, Skymet had predicted that the monsoons this year would be “below normal” due to El Nino. Note that good monsoons are crucial for India’s agriculture output, as almost 52 per cent of its net cultivated land depends on good rainfall during the June-September season. Four factors will be relevant to assess how such monsoon forecasts will play out for agricultural crops. One, the IMD’s forecast is based on a model that has an error of 5 per cent over or less than the LPA of monsoons during the period of 1971 to 20220. The LPA for this period suggests a rainfall of 87 centimetres. Two, the start, the progress and the departure of the monsoons are as important as the extent of rainfall during this season. Three, the spread of the rainfall holds the key to making the monsoon work positively for agriculture. And four, in the past several years, the first forecasts made by the IMD and Skymet have been at variance from the actual rainfall. In other words, even though El Nino conditions cannot be ruled out, the first forecasts made by the weather agencies can provide only an indication, but no firm conclusions can be made from what kind of impact the actual rainfall will make on crop output and, therefore, the state of the rural economy.

Mudra loans disbursement grow at a rapid pace; NPAs at 3.2%

After eight years of its launch, the Prime Minister Mudra Yojana or the Mudra scheme continues to see healthy growth in the number and value of collateral-free loans of up to Rs 10 lakh each to non-corporate, non-farm small and micro-entrepreneurs. The Mudra Yojana was launched in April 2015 and the collateral-free loans are given under three broad categories – Shishu loans of up to Rs 50,000, Kishore loans of above Rs 50,000 and up to Rs 5 lakh and Tarun loans of above Rs 5 lakh and up to Rs 10 lakh. In 2022-23, the total value of Mudra loans granted under these categories amounted to Rs 4.32 lakh crore, an increase of 27 per cent over the previous year. The number of loans in this period also increased by 9 per cent from 53.7 million to 58.8 million, indicating that the amount of loans per applicant has increased significantly or there are more applicants under the Tarun category. An analysis of Mudra loans shows that almost three-fourths of the accounts under this scheme belonged to women entrepreneurs and almost half of the loan recipients were entrepreneurs from under-privileged sections of society like scheduled caste, scheduled tribe and other backward castes. The total cumulative value of Mudra loans sanctioned in the last eight years is estimated at Rs 23.2 lakh crore to over 408 million applicants or an average loan of about Rs 57,000 to each recipient. There are, however, worries over many of these collateral-free loans turning into non-performing assets for the banking sector. According to data for the period ended March 2022, 3.17 per cent of the Mudra loans had turned sticky or non-performing assets. The incidence of NPAs among Mudra loans in Maharashtra is a little higher as over 16 per cent of the Rs 30,019 crore of Mudra loans issued to 5.2 million eligible entrepreneurs in the state had turned into non-performing assets. The need for a closer monitoring of these loans can hardly be ignored, even as the gains of financial inclusion are beyond doubt.

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(The views expressed are personal)

COMMENTS