Economy awaits big policy push

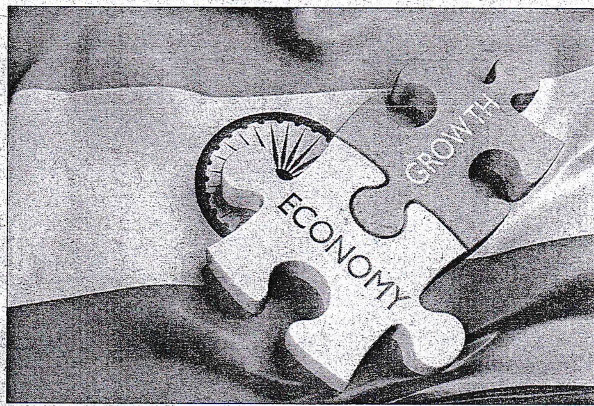
LAND, LABOUR AND capital must be put to more efficient use for higher value creation, while India integrates more seamlessly with the global value chains.

All this may well be on the agenda of any government taking office after the polls, since exigency would demand it. But growth impulses would also come from a reversal of the centralisation of polices and governance, for which the outcome of the elections will be a key determinant.

It is a safe bet for Prime Minister Narendra Modi to "guarantee" that his "third term" would make India the third-largest economy in the world in current dollar terms. This will likely happen latest by FY28 (and probably earlier), even with a further slowing of growth, and by then, India would have moved seven notches up in the global economic pecking order in less than one-and-a-half decades.

Such climb up the standings, however, is thanks to the unique period, when India found a number of economies in striking distance in the economic race, all growing at anaemic rates. However, to move further and become the second-largest economy, it would have to wait at least another half a century, even in the best-case scenario (with per capita income still much lower than most high-income countries).

To be sure, more than four years since the economy bore the brunt of the pandemic (and shrank by nearly a quarter in Q1FY21), statistical data is yet to be shorn of the distortion caused by the tragedy. Growth in the quarter ended September 2023 may well be less than the impressive headline figure of 7.6% by one percent point or more. If such an expansion rate is causing concerns of overheating, it signifies a considerable undermining of the growth capacity, which may have dropped to around 6%.



That is subdued growth for a country anxious to traverse the high-growth path in the coming decades. And even this is produced with a relentless overuse of fiscal firepower over the years. The mismatch between the economy's capacity to churn out revenues for the government, and latter's ability for pump-priming has widened.

To the government's credit, it has made commendable strides in tax collections, aided by the drive to "formalise" the economy, and a greater connect between the direct and indirect tax wings. But the statistical practice of a larger de facto weight being accorded to wholesale price index in the GDP deflator too is behind the instant high tax buoyancy (tax-GDP ratios in FY23 and H1FY24 were somewhat identical, but buoyancy jumped 2.4 times from the last fiscal).

In 2024 and onward, support to the economy from government investments and consumption will inevitably wane. An effort to rein in "general government debt" to somewhere close to the recommended level of 60% will require economical spending.

Since Q2FY20, which represents the pre-pandemic phase, gross fixed capital formation has grown nearly twice as private final consumption expenditure. The fixed investment creation was predominantly due to public-sector capex. But the recent years' large spikes in public capex are partly optical, as it masks a deliberate shift of public investment mandate to the Centre (Union Budget) from states and CPSEs, which had conventionally played bigger comparative roles. The limitations of the strategy of creating a virtuous cycle of investments by using government funds to crowd in the private sector are apparent.

For sure, many sectors of Corporate India are reportedly witnessing capacity utilisation of over 75%. If this doesn't yet boost the confidence of companies to invest afresh, it is because they perceive the domestic consumption demand is weak and transient, and fear the external sector won't see a quick turnaround.

Though sales of high-end consumer goods have been buoyant in the past year, the broader consumption market is rather sluggish, and the rural sector is languishing. The recent spurt in corporate profits has much to do with an incidental fall in input costs, rather than a broad-based uptick in demand. Such corporate profitability would easily vacillate, being excessively prone to global commodity market trends, capital flows and exchange rates.

Any monetary easing by RBI is unlikely at least before the third quarter of the next fiscal, given the persisting inflationary risks. RBI's latest monthly bulletin rightly notes that, unless inflation is "brought back to the 4% target and tethered there, there is a strong likelihood that growth may falter".