SLOWER GROWTH AND A TIGHTER FISCAL

India Slid Into The Pandemic Crisis In The Backdrop Of Economic Downslide; Fiscal Stimulus Has To Be Structured

The impact of COVID-19 will be debilitating for the global as well as the Indian economies. Various institutions have assessed India's growth prospects for 2020-21 ranging from 0.8% (Fitch) to 4.0% (Asian Development Bank). This wide range indicates the extent of uncertainty and tentative nature of these forecasts. The International Monetary Fund (IMF) has projected India's growth at 1.9%, China's at 1.2%, and the global growth at (-) 3.0%. The actual growth outcome for India would depend on: the speed at which the economy is opened up; the time it takes to contain the spread of virus, and, the government's policy support.

Growth prospects

India slid into the novel coronavirus crisis on the back of a persistent economic downslide. There was a sustained fall in the saving and investment rates with unutilised capacity in the industrial sector. In 2019-20, there was a contraction in the Centre's gross tax revenues in the first 11 months during April 2019 to February 2020, at (-) 0.8%. These trends continue to beset the Indian economy in this crisis.

We examine the growth prospects for 2020-21 from the output side, making reference to real gross value added (GVA). In 2019-20, which would serve as the base year, India may show GVA growth of about 4.4%, well below the Central Statistics Office's second advance estimate of 4.9%, as the fourth quarter number is likely to be revised downwards on account of the adverse impact of the virus on economic activities. The IMF's GDP growth estimate for 2019-20 is at 4.2%.

GVA is divided into eight broad sectors. Although all sectors have been disrupted, some may be affected less than the others. We divide the output sectors in four groups.

In group A, we consider two sectors that have suffered only limited disruption — namely agriculture and allied sectors, and public administration, defence and other services. In the case of agriculture, *rabi* crop is currently being harvested and a good monsoon is predicted later in the year. Despite some labour shortage issues, this sector may show near-normal performance. The public and defence services have been nearly fully active, with the health services at the forefront of the the COVID-19 fight. For the group A sectors, it may be possible to achieve 90% of the 2019-20 growth performance.

Sectoral growth prospects in 2020-21

Differential impact of the novel coranavirus on Gross Value Added in 2020-21

Group	Sector	Share 2019-20 (MAE)	Average growth (2017-18, 18-19, 19-20 MAE)	2019-20 MAE	Targeted growth (2020-21)	Contribution to growth (% points)
A	Agriculture, forestry & fishing	14.4	4.0	3.1	2.8	0.40
B	Mining & quarrying	2.6	0.6	2.2	1.1	0.03
C	Manufacturing	17.4	4.4	0.3	1.8	0.31
B	Electricity, gas, water supply & other utility services	2.3	8.0	4.1	2.1	0.05
B	Construction	7.8	4.7	2.4	1.2	0.09
D	Trade, hotels, transport, communication, etc.	19.6	7.0	5.1	1.5	0.30
B	Financial, real estate & professional services	22.3	6.3	6.8	3.4	0.76
A	Public Administration, defence and other services	13.6	9.3	8.2	7.4	1.00
	GVA at Basic Price	100.0	5.9	4.4	2.94	2.94

MAE refers to modified advance estimates that are derived by adjusting downwards, CSO advance estimates dated February 28, 2020

Next, we consider the group that is likely to suffer maximum disruption (Group D). This includes, trade, hotels, restaurants, travel and tourism under the broad group of “Trade, Hotels, Transport, Storage and Communications”. This sector may be able to show 30% of 2019-20 growth performance. Group B comprises four sectors which may suffer average disruption showing 50% of 2019-20 growth performance. These sectors are mining and quarrying, electricity, gas, water supply and other utility services, construction, and financial, real estate and professional services. In the last group (Group C), we place manufacturing which has suffered significant growth erosion in 2019-20. It is feasible to stimulate this sector by supporting demand.

In this case, we apply a 40% performance factor, not on the 2019-20 growth which is an outlier, but on the average growth of the preceding three years. Considering these four groups together, a GVA growth of 2.9% is estimated for 2020-21. Realising this requires strong policy support, particularly for the manufacturing sector which has a weight of 17.4%. It is also based on the assumption that the Indian economy may move on to positive growth after the first quarter. In the first quarter, GVA growth will be negative.

Calibrating policy support

Monetary policy initiatives undertaken so far include a reduction in the repo rate to 4.4%, the reverse repo rate to 3.75%, and cash reserve ratio to 3%. The Reserve Bank of India has also opened several special financing facilities. These actions will have a positive impact on output only after the lockdown is lifted. These measures need to be supplemented by an appropriate fiscal stimulus. Although industry has been clamouring for a large fiscal stimulus, cash-constrained central and State governments have taken expenditure reducing measures by announcing a freezing of enhancements of dearness allowance and dearness relief. This may result in savings of ₹37,000 crore for the Centre and about ₹82,000 crore for the States, together amounting to 0.6% of GDP.

There is also a talk of substantially reducing non-salary defence expenditure. With lower petroleum prices, fertilizer and petroleum subsidies may be reduced. These expenditure cuts are contemplated to keep the fiscal deficit under some control.

On fiscal deficit

Fiscal stimulus can be of three types: relief expenditure for protecting the poor and the marginalised; (b) demand-supporting expenditure for increasing personal disposable incomes or government’s purchases of goods and services, including expanded health-care expenditure imposed by the novel coronavirus, and, bailouts for industry and financial institutions. The Centre had earlier announced a relief package of ₹1.7-lakh crore of which the additionality was only ₹65,000 crore, since it included a frontloading of the budgeted expenditures. The Centre’s budgeted fiscal deficit of 3.5% of GDP may have to be enhanced substantially to make up for the shortfall in budgeted revenues; account for a lower than projected nominal GDP for 2020-21, and provide for a stimulus. Thus, the Centre’s fiscal deficit may increase to 6.0% of GDP. Expenditure on construction of hospitals, roads and other infrastructure and purchase of health-related equipment and medicines require prioritisation. These expenditures will have high multiplier effects. Similar initiatives may be undertaken by the State governments which may also enhance their combined fiscal deficit to about 4.0% of GDP to account for 3.0% of GDP under their respective Fiscal Responsibility Legislation/Law and to provide for the shortfall in their revenues and some stimulus.

Financing of the fiscal deficit poses a major challenge this year. On the demand side, the Central (6.0%) and State governments (4.0%) and Central and State public sector undertakings (3.5%) together present a total public sector borrowing requirement (PSBR) of 13.5% of GDP.

Against this, the total available resources may at best be 9.5% of GDP consisting of excess saving of the private sector at 7.0%, public sector saving of 1.5%, and net capital inflow of 1.0% of GDP3. The gap of 4.0% points of GDP may result in increased cost of borrowing for the Central and State governments. This gap may be bridged by enhancing net capital inflows including borrowing from abroad and by monetising some part of the Centre's deficit. Monetisation of debt can at best be a one-time effort. This cannot become a general practice.

Meanings of Difficult Words:

1. **fiscal (year)** (noun) – financial year.
2. **slid past and past participle of slide** (verb) – fall, drop, plunge/descend (to a lower level).
3. **pandemic** (noun) – the worldwide spread of a new disease; The illness spreads around the world and typically affects a large number of people across a wide area.
4. **backdrop** (noun) – situation, scenario, context.
5. **downslide** (noun) – decline, downward movement/ trend, downgrade.
6. **fiscal stimulus** (noun) – an attempt by a government by measures normally involving increased public spending and lower taxation, aimed at giving a positive jolt to economic activity.
7. **debilitating** (adjective) – weakening, disabling, paralyzing, undermining, impairing.
8. **prospects** (noun) – outlook, expectations, potential, possibilities.
9. **extent** (noun) – range, level; magnitude.
10. **forecast** (noun) – prediction, indication, projection, speculation, calculation (of future events or trends).
11. **depend on** (verb) – be based on, rely on, be conditional on.
12. **open up** (phrasal verb) – begin/start doing business again and make it available for the customers to get involved in it; restart/reopen (economic activity).
13. **on the back of** (phrase) – as a result of, after, subsequent to (something already exists).
14. **persistent** (adjective) – continuing, unrelenting, unceasing, never-ending.
15. **sustained** (adjective) – continuous, constant, steady, uninterrupted, unceasing.
16. **unutilized** (adjective) – not used completely.
17. **contraction** (noun) – decline, decrease, reduction.
18. **beset** (verb) – trouble, bother, embarrass (persistently).
19. **make reference to** (phrase) – to refer to; to mention.
20. **gross value added (GVA)** (noun) – it is a measure of total output and income in the economy. It provides the rupee value for the amount of goods and services produced in an economy after deducting the cost of inputs and raw materials that have gone into the production of those goods and services. It also gives sector-specific picture like what is the growth in an area, industry or sector of an economy. On the other hand, GDP or gross domestic product is a measure of economic activity in a country. It is the total value of a country's annual output of goods and service.
21. **base year** (noun) – a starting or benchmark (year) with reference to which the national account figures such as gross domestic product (GDP), gross domestic saving, gross capital formation are calculated in the subsequent years. The base year is the year in which an index is set to 100. While computing macroeconomic numbers such as inflation or economic growth rates, indices are used.
22. **advance** (adjective) – early, previous, prior, beforehand.
23. **on account of** (phrase) – because of, owing to/due to, by virtue of.
24. **adverse** (adjective) – unfavourable, disadvantageous, bad.
25. **Gross domestic product** (GDP) (noun) – a measure of economic activity in a country. It is the total value of a country's annual output of goods and service.
26. **rabi crops/sowing** (noun) – winter crops; seeds sowing in the beginning (Nov) of the winter and harvesting at the end of the season (Apr) in the South Asia.
27. **kharif crops/sowing** (noun) – monsoon crops; seeds sowing in the beginning (Jun) of the monsoon and harvesting at the end of the season (Oct) in the South Asia.
28. **harvest** (verb) – gather a ripe crop from the fields.
29. **near-normal** (adjective) – almost normal.
30. **at/in the forefront of** (phrase) – be in a leading/front/important position in an important activity.
31. **erosion** (noun) – destruction, deterioration, decline, weakening.

32. **feasible** (adjective) – practicable, viable, realistic.
33. **stimulate** (verb) – encourage, motivate, prompt/activate, galvanize.
34. **outlier** (noun) – (in statistics) outlier is an observation of data that does not fit the rest of the data. It is sometimes called an extreme value (it can be too high/too low value). When you graph an outlier, it will appear not to fit the pattern of the graph.
35. **preceding** (adjective) – previous, prior, earlier.
36. **weight** (noun) – importance, significance, value/power.
37. **assumption** (noun) – belief, notion, impression, premise.
38. **move on** (phrasal verb) – develop, improve, make progress, advance, get better.
39. **calibrate** (verb) – carefully assess, regulate, adjust.
40. **monetary policy** (noun) – the macroeconomic policy laid down by the central bank. It involves management of money supply and interest rate and is the demand side economic policy used by the government of a country to achieve macroeconomic objectives like inflation, consumption, growth and liquidity.
41. **undertake** (verb) – begin, start, embark on, launch into.
42. **repo rate** (noun) – it is the rate at which the central bank of a country (RBI in case of India) lends money to commercial banks in the event of any shortfall of funds.
43. **reverse repo rate** (noun) – it is the rate at which the central bank of a country (RBI in case of India) borrows money from commercial banks within the country.
44. **cash reserve ratio** (CRR) (noun) – a certain minimum amount of deposit that the commercial banks have to hold as reserves with the central bank. The proportion of liabilities which a bank has to set aside as cash.
45. **supplement** (verb) – augment, increase, add to, boost.
46. **clamour** (verb) – protest, complain, demand, push/press.
47. **cash-constrained** (adjective) – restricted (due to lack of cash-liquidity) from doing something.
48. **freeze** (noun) – hold something at a fixed state for a period of time.
49. **dearness allowance (DA)** (noun) – DA is an allowance that every government employee gets and it is calculated as a proportion of the basic salary. This DA is paid to compensate the rise in inflation (cost of living).
50. **dearness relief (DR)** (noun) – DR is an allowance that every government pensioner gets and it is calculated as a proportion of the basic pension. This DR is paid to compensate the rise in inflation (cost of living).
51. **contemplate** (verb) – consider, think about, reflect on.
52. **fiscal deficit** (noun) – the difference between total expenditure and total income of the government.
53. **the marginalised** (noun) – the people who are treated as insignificant, treated as unimportant, neglected.
54. **personal disposable income/disposable personal income** (DPI) (noun) – it is the amount of money an individual has to spend or save after subtracting/paying taxes from his/her total income.
55. **bailout** (noun) – an act of providing financial help/support by the outside investors to a bank/institution/organisation which faces serious financial difficulty.
56. **Comprehensive Relief Package** (noun) – a comprehensive package should have simultaneous reliefs across different realms (area of activity) (for instance, tax compliance, relief for poor, RBI monetary policy interventions, and relief for middle class in terms of EMI, internet rate subvention and most importantly an increase in investment in health infrastructure).
57. **additionality** (noun) – the property/fact of being additional.
58. **frontload** (verb) – allocate major portion of (costs, effort, expenditures etc.) at the beginning of the enterprise/activity/project (during budget).
59. **make up for** (phrase) – offset, counterbalance, compensate for; balance, neutralize.

60. **shortfall** (noun) – deficit, inadequacy/deficiency; shortcoming/defect.
61. **account for** (phrasal verb) – constitute, make up, comprise, form.
62. **stimulus** (noun) – impetus, boost, incentive, fillip.
63. **prioritisation** (noun) – the activity that arranges items or activities in order of importance relative to each other.
64. **multiplier effect** (noun) – the proportional amount of increase in final income (particularly of the government) that results from an injection of spending; it occurs when an initial injection (investment/spending) into the economy causes a bigger final increase in national income.
65. **fiscal responsibility** (noun) – the act of creating, optimizing and maintaining a balanced budget.
66. **pose** (verb) – raise, ask, put (a question/matter for consideration).
67. **public sector borrowing requirement** (PSBR) (noun) – it is the old name for the budget/fiscal deficit; (a fiscal deficit is a shortfall in a government's income compared with its spending/expenditure and this deficit has to be financed by the public sector borrowing requirement (PSBR) (amount a government needs to borrow to cover its expenditure).
68. **at best** (phrase) – simply, merely, only.
69. **capital inflow** (noun) – a steady movement of capital (amount) into a place, economy, activity etc.
70. **capital outflow** (noun) – money/assets flowing out of (or leaving) a particular country's economy.
71. **bridge** (verb) – join, link, connect, unite.
72. **monetise** (verb) – earn money, generate revenue.
73. **deficit** (noun) – shortfall, deficiency, shortage.
74. **monetisation** (noun) – in general, it is the process of converting something (e.g. an asset) into money.
75. **debt** (noun) – liability, financial obligation, borrowed capital.
76. **one-time** (adjective) – done only once.