The Suno India Show
Indian Economy Explained: Decoding India's GDP and Economic Slowdown

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The coronavirus pandemic and the sudden nationwide lockdown spiralled the economic downturn into a full-fledged economic crisis in the country. The Reserve Bank of India has projected the Indian economy to contract 9.5 per cent in the current fiscal, while the International Monetary Fund (IMF) and World Bank estimates the contraction at 10.3% and 9.6% respectively.

However, the Finance Minister, Nirmala Sitharaman was optimistic and said with the lockdown restrictions being eased in the country, the macroeconomic indicators have shown signs of a revival. And, that the government is expecting the festive season to boost the demand and an inflow of funds through the foreign direct investment route.

The Indian economy was already in bad shape before the COVID-19 pandemic struck. The former Reserve Bank of India's Governor, Raghuram Rajan also said that demonetisation and Goods and Services Tax (GST) were the two major headwinds that held back India's economic growth.

Hi, I'm Kunika Balhotra, Research and Communications Officer for Suno India and your host for this episode of our new mini series, "Indian Economy Explained" of The Suno India Show. This series will bring to you insightful discussions with economic experts, professors and researchers to keep you up to date with the latest economic developments in the country.

To know more about India's economic growth story, the impact of COVID19 pandemic on our country's Gross Domestic Product (GDP) and how the economy affects the GDP. I reached out to Dr Biswajit Nag, Professor and Head of Economics Division at the Indian Institute of Foreign Trade to understand why GDP figures and its sharp fall in recent times matters to every Indian.

Host: *So how is the country's GDP calculated? And especially in a country where the economy depends on retailers and service sectors rather than actual production?*

Prof. Biswajit Nag: Actually, you know, there are many methods in which GDP is calculated in case of India and it is generally done in two ways. One is basically through adding the class value added what we can see here, from different sectors, so, that's basically the income generated from different sectors and another method is what they call expenditure method. So, saying in a value added method, which is basically a factor cost. So, it's based on say, what is the income coming from agriculture from manufacturing from services. So, in general, there are a few common sectors that whenever you read any newspaper or any discussions on GDP, just after the budget, so we'll find out there are mostly eight sectors on which actually India is focusing one is agriculture, forestry and fishing together, then mining and quarrying, then manufacturing as a whole, electricity gas water supply, then constructions and then trade, hotels, transport and communications, and then financing insurance, real estate, business services, and then community. So the salaries and personal so, this is basically the collecting the income, as you know, the GDP is basically how much is the country as as generated in terms of value the value of the products in a particular year. So, these are the sectors from the income side, we didn't calculate. Another way of looking at it is basically from the expenditure side. So, it is basically the market price of how much actually being spent. So, it could be like, you know, consumption expenditure by individual. So, what we call private final consumption expenditure, there could be government expenditure and then gross fixed capital formation, that is how much assets has been built up in the country at that particular year. Then there are exports, imports , some small discrepancies and changes in stocks. So, these are the two ways basically we try to measure basically the GDP in a particular year.

Host: *Yeah, so now that you have talked about GDP. Could you tell me how a country's GDP affects the common citizens and the investors?*

Prof. Biswajit Nag: Yeah, GDP number, which is just like a, you know, it's the tip of the iceberg, it says not a thing. At the same time, it doesn't say anything, because it's just a number. Most of the time, you know, what you see in the newspaper is the GDP growth rate, say, for example, currently, you know, India's GDP in the last quarter reduced by more than 10%. And we are expecting that the end of the whole year, you know, 23%, actually, and they end up the whole year, it could be maybe more than minus 10%, we'll get to do so. So, common people actually keep in mind the growth figures, but you know, how actually it affects the common people and how actually it affects the investors. So, let me just look at it from a different angle, if you look at the GDP figure, which is basically how much the income of a particular country is increased in a particular year. So, think of forget about a country. Think of it as an individual, one individual's income has increased by 5% or 10% in a year, that means that the individual has worked and worked hard to earn that money. So, that means, if you look at it from a country's perspective, so that means the country has really worked well, so that it's overall income has increased. So, GDP does not tell us the distribution expect how much has been earned by by farmers, how much has been earned by salaried persons or the business people, it basically tells you the overall , but if we just go one step ahead, GDP is calculated as a summation of different incomes generated from different sectors, which is value added what we call, so, in that case, what will happen if we just go one step ahead and try to find out kind of what are the incomes of different sectors then actually even you know, get a better picture. So, you can find out you know, how much is the growth in agriculture, how much is the growth in manufacturing, how much is the growth in trade depending on on their share in the GDP, for example, you know, maybe you know, agricultural share could be around say less than 20% manufacturing share could be around 17% okay industry as a whole maybe on 30% which includes mining, quarrying manufacturing, electricity, constructions, those are all part of industry. So, when we see which sectors are growing if we see the construction sector is growing, right. So, if we see the construction sector is growing, that means the people who are involved in construction sectors, their income has grown more than maybe the other sectors. So, the people who are actually working in the sector whose livelihood depends on the sectors directly indirectly, when construction sectors are actually growing, so their lives are actually getting, you know, some kind of positive benefit out of it. That's the way basically the common people like to get influenced by the GDP figures, you can understand a bit of overall improvement in the life, but as I just mentioned, this is a gross figure, you may not be able to understand the distributional aspects of it, coming back to the second part of the question, which is how actually investors actually getting influenced investors you can think of a domestic investor you can think of foreign investor. Now, for foreign investors, and definitely GDP growth rate is a positive number because they do not know the country much. So, there they will be very much influenced by some of the you know basic indicators of the economy, which are highlighted in international media or sometimes some research is done by some agencies, they will tell that this will be the projected growth and this growth will be coming from these these sectors, as I just mentioned about the construction sector or it could be from the trade sector. So, the foreign investors will then find out okay these are the sectors which are growing in that country and if the ease of doing business is relatively better and they find confidence in that country, so, they will be positively influenced they might take a decision to invest in that company for the domestic investors they are inside the country, many of them are already invested in different sectors, so, they have better information. So, it does GDP growth rate is it not that influential on their investment decisions, their investment decisions depends on much deep rooted understanding of the economy because sometimes what happens there could be a sudden rise in one sectors and then it tapers off because of certain you know reasons and and and that informations that they have been much domestic investors, but overall a positive GDP or higher GDP growth rate is having kind of a positive influence on investors.

Host: *All right, so you talked about how it affects the common citizens and the investors in the country. Now Could you tell me how it is linked with employment like the economy? How does the economic growth affect employment in the country?*

Prof. Biswajit Nag: If you recall some time back, I think the last decade we've had a situation what we called jobless growth, there is a high growth in India, but employments are actually not quite right and there could be a country's by relatively lower GDP growth, but higher employment could have been generated. So, as GDP is calculated from the contributions of different sectors, that means, the performance of different sectors are influencing the overall GDP figure. So, that means, if a particular sector is doing well, so, that means, there could be a possibility of employment generation. I'm saying that is a necessary condition but not sufficient, okay. For example, suppose there is a high productive sector due to high technology and sophisticated technology, more automation is there. So that sector perhaps, you know, generating a lot of growth, but employment is not growing significantly. Let me give you an example of two countries which generally I hear in the class that you know, mid 2000 this example came up two countries one is Malaysia and one is

Argentina, okay. So, Malaysia actually focused on labor intensive goods as they are in a production base to increase the exports. So, which includes electronics, actually electronics sectors can generate a lot of employment because at the end of the day, a lot of assembling activities are required for which not much skill is required. For example, a lot of office equipment requires fax machines, counting machines, mobile phones, telephones, okay? radios, televisions, cameras, okay. So, all these electronic goods recur at the end. And a lot of you know, bringing too many things together is just like, you know, the Lego toys you know, there are components, there are parts and you are putting them, feeding them and making the product. So, Malaysia has got a huge advantage of linking the growth with employment. Okay. On the other hand, Argentina, another country, which focused on high skilled and semi skilled sectors for their growth, which generate jobs for relatively skilled workers, okay. But it doesn't generate that much of a job towards the people who are the lowest strata okay. So, so that you can get a lot of good jobs. For, in India when this condition when this sort of jobless growth came up. So, there are a lot of jobs for IT sectors, but the other sectors are not growing much okay. So, GDP and employment sometimes people think that they are moving together in the same directions, but it may not be. So these two examples tell you that GDP could be a necessary thing, but it is not a sufficient cause for corresponding to this question. One debate which is very much there in many parts of the world and very much in our economy, that if you do Automation is to increase the productivity to increase the GDP, will there be job losses? Okay, so when that take out many people, I'd like to bring back to the memory that when typewriters are actually been taken out, and computers came in the same debate came out that it will actually, you know, reduce a lot of jobs, but it didn't happen, it created new kinds of jobs, okay. So it is just a matter of transition, that, you know, sometimes you require how fast you can get the skills to the new sector. So that particular thinking process is very important, so that we can address the job losses. The last point I'd like to highlight here, which is connected to COVID, or any kind of economic crisis, what we have noted in the world, that when GDP is growing, the employment growth is relatively slower. Okay, because GDP growth is mostly taking the advantage of productivity growth due to technology. But when GDP slides down, further it is in 97- 98, Southeast Asian crisis, whether it is Latin American prices whether it is the subprime crisis, or even during the covid crisis, when GDP goes down, employment goes down faster than that. So that's basically the thing you need to know the way the employment is rising and the way the employment goes down in different directions altogether. So, while there is a complex relationship between GDP and employment.

Host: *So now that you mentioned about COVID, India's economic growth has been declining, so, what has gone wrong in these last years which has stopped India's growth story, before COVID?*

Prof. Biswajit Nag: India's case is a complex case, okay? Because India's GDP started going down before COVID and COVID is accentuated that particular crisis, okay. So that particular thing you need to keep in mind when we are comparing India with other countries. Now, if I go back to basic numbers, since 2016-17, the government was trying to make a lot of reform, but every reform has a kind of a friction it creates in the economy. So you need to take that friction into account before you actually try to understand what will be its long term impact, okay. So that is one aspect. But apart from that, more seriously, what happened, the government tried to focus on industry, under the programs like Make in India and now even in Atma Nirbhar India. But at the same time, India is much more open economy, as compared to 20 years back. So an open economy means there'll be a lot of components, parts, or even final goods will be imported. And what we expected is that, you know, after importing a lot of such companies, there'll be a lot of industrial activities, and India will be able to produce new kinds of goods and export to the rest of the world. So we'll import components from Thailand, Vietnam, or from China, and we will export to Middle East Africa, Europe, or the US. But, you know, that didn't happen. So, our industrial growth was actually quite, you know, less than what we expected what it should have been. And that's one particular thing. Agricultural sector was also not performing as per the expectations because agriculture sectors require a lot of reforms. And, and one of the things that there's a lot of wastage of agricultural products in India, productivity is less, mechanizations were not much there. Storage is not complete, properly handled, the agriculture market is not complete farmers are not getting the right signals about the pricing and agricultural financing and insurance around agriculture sectors also not very good. So, India as a country moving forward with having a baggage of low agricultural productivity. So agriculture, productivity are going down. industries are not performing well. And meanwhile, the service sector slowed down very much there because in case of IT and IT enabled services now what happens a lot of other countries have come up. So, they are competing with India and by this time of 20 years of good you know performance of IT sectors, the basic salary wages and cost of doing business in it sectors has also gone up. So, India has gradually become less competitive in IT sectors and has come at least in the lower part of the value chain. So, what is required for India to move to the higher part of the value chain of IT sectors, which also India is not able to move as part of expected growth. So, service sectors also slow this slowly you know becoming kind of a not stagnant but it is more or less stabilized to a particular growth. Lastly, the trade, our exports are also not growing. So, unfortunately before COVID we were already having a situation where our economy is not doing very well and the COVID part has been accentuated at this speed and that's why our growth rate has actually added nose dive significantly in the first two quarters.

Host: *Also, what do you think about measures like GST and demonetization? How these two measures impacted India's economic growth?*

Prof. Biswajit Nag: Significantly what happened you know, demonetization has suddenly taken out a lot of money. So, what happened, the velocity of money the circular flow of the money has gone down and and that means, the cash flow in the economy has gone down substantially and large part of informal economy by the way, India is just at the lower middle income country, India has not even reached to a higher middle income country. So, the informal sector actually consists of a significant sector. So, the poor people do not use PayTM or credit card or they do not have any cashless basis as systems. So, of course, the cash shortage has not only reduced the cash flow in the economy, but also gave a kind of a signal which has a negative impact on the consumer sentiment, okay. So, consumers have become much more cautious on spending money. So, we need to understand that you know, consumer sentiment is the main driver of a capitalist economic sectors, because that drives the investment that basically help the investor to invest more money and then more goods may come. Just back to back the GST as is also kind of an issue because GST was very good approach because there are a lot of countries in the world has GST, but they were not having a legacy problem, but because in India is having a legacy problem, different kinds of Central State relationships, and we just overnight changed that. So, the ill I'm not saying that ill treatment either I said that, you know, slow and inexperienced rolling out of GST, now, the states are supposed to get the money back the tax revenues, but the center is earning out of GST because that's the contract all the time happens between Central and state and their shares. So, those shares are not reaching the states at the right moment. So, states are not able to, you know, spend as per their expenditure plan. And that's why you know, you must have noted that some sectors are outside GST okay, because of this particular concept, so that states can earn a lot of revenue out of it. And this has become very serious during the time of COVID because the states are running out of their budget, and they had there is a borrowing limit imposed on them though it has been relaxed a bit, but states are looking for their possible, you know, rights what what they call because that's the money should come from centers to the state, but at the same time center is also having a huge fiscal pressure. So the center is also not able to part with the revenue generated. So this basically creates a kind of a major hiccup for all the development expenditure. And in case of GDP. As you know, G what we call the government expenditure is a major component of GDP. And that part is getting affected both by the Central and State okay. So, those two issues definitely I think so, you need to look at the context. Our economy is not doing very well for our own fundamental reasons internationally, we are also not very able to perform properly because our exports are coming down at the same time GST as well as demonetisation also happened. So, all in timing happens and there is kind of a lack also is being you know, added to it because of COVID. So, this becomes a kind of a quite complicated situation for an economy like India.

Host: *Yeah, when COVID struck, the Finance Ministry announced a post pandemic financial package, which is Aatma Nirbhar Bharat package to help restore the Indian economic growth? So what do you think about this financial measure by the finance ministry?*

Prof. Biswajit Nag: See, Aatma Nirbhar Package, the details are not yet fully rolled out, that is one particular thing because we economists also need to understand how it is different from Make In India Okay. One and what are the changes you have done on Make In India because we need to understand the pros and cons of it because some sector must have done well and some sectors could not do and in case of Aatma Nirbhar Bharat we also need to understand strategically in which sectors we need to be you know, very good you know, are less dependent on the rest of the world for example, during the beginning of the year, when Coronavirus struck the US economy the US government came out clearly that they were very much dependent on China in case of pharmaceuticals, okay. So, they said that medicine should be considered as a strategy product and in this case the US should be more self dependent okay. So, in such cases our kind of an idea also needs to understand which are the strategic sectors. So far that information is not there. So, it is very difficult for us to comment on on in which direction Aatma Nirbhar Bharat will be going, but I can assume so, a lot of things that there could be a kind of an effort to reduce the input of some of the goods, but you need to understand that when you try to reduce the input this might give a negative signal to the international investor community, it should not be the case that because of this strategy, our foreign investment flow goes down. So, to make Aatma Nirbhar Bharat and then suddenly the foreign investment flow in the country goes down, we are already having no less money and if in part that there is a blow then there will be problems. So, we need to basically walk on a tightrope to bring out the balance to give the right signal to the world community. So that you know people consider India an open, fair country to do business and also at the same time India is very strong in terms of its economic policy, and there's a clear cut vision coming out of it.

Host: *So according to you what could be some of the potential interventions by the government to get that economy back on track?*

Prof. Biswajit Nag: I personally think that immediately in the short run when the medium term in the long run in the short run, the consumer sentiment is very important. So India is a large country and it has a very good investor community inside the country. Okay, so consumer sentiment needs to go up. So if you just tape out, you just ask even the vegetable seller, even the local grocery, even the tea shops like chai ki dukaan you find out everybody will say that the sales have gone down substantially. Okay. And in some cases the prices have gone up. Right. This is maybe maybe not going to the grocery stores or to buy dresses, they may be doing online business but it is not 100% replacement, because everybody is scared of coronavirus and as a result consumer sentiment has gone down. So you need to, you need to find a way out how to actually give more money in the hands of the people. Now what is happening, suppose if you want to give more money to the states from the center wants to give more money to the States, and if you consider this is an opportunity to do some hard reform, then states may be maybe thinking twice, and they may not be very much interest to take that second one, in many cases, it's a loan. And, in case of the financial packages, which are coming out, for example, and I can tell you, I know, one person who told me that he was trying to get that additional loan at a cheaper rate. He said that I have two questions. He said that his business is already down. He doesn't know after taking the loan whether the business will improve. He's not having that confidence. So he's saying that, you know, that it's a good effort from the government side, but the demand for loan off take is not there. Second thing he said that there are procedural problems, for example, he has already taken a loan from the bank. Okay. And the bank says first you repay those loans, and then we'll give you the loan. So, it doesn't help. So, the government is you know, is ready to give the money, but one is not reaching to the people and one is not reaching to the people the consumer sentiment is that going up and as the consumer sentiment is going up, then definitely you know, in the short run the revival of the economy, which is not this is the point number one, point number two, I think the government this is the right time and think of giving huge focus on education as a whole. Historically, what we have noted especially in the United States that when there are boom times the people do not go to the colleges and universities because it is very easy to get jobs, when there is a recession actually the kids will go to the college and universities they try to take one more diploma because that they are not getting jobs. So they do not want to get that time wasted. So they try to improve their skills okay. So, we need to understand in this country at this moment, because there is a major technological change happening due to COVID and it is now written on the wall that not all jobs will come back initially there is a job losses in the informal sector. Now people in the formal sectors are losing jobs, which is more dangerous, because informal sector people losing jobs, they can get the jobs very easily some other sectors because they do not require a skill for example, the migrant workers who are working in a construction side, they go back home, they can they can open up they can work in some other sectors may be in a rice mill sector may be in it in a shop, okay. So, because that doesn't make that much of a transition in terms of transition along with the skills, but the skilled workers when they are losing jobs, they will not get back the job. so easily, which is basically a kind of a serious, you know, issue in which India is getting into. So, what is important at this moment, that skill development should be encouraged. So, India has a lot of public and private sector level institutions, even at the diploma and certificate levels, but what happens for skill development, there is no loan educational loan available. For example, if you want to become an engineer or if you want to study an MBA in a good reputed school bank, say all the time interested to give you a loan, but suppose there is a plumber or electricians, okay. New technology has come up or and you know, AC mechanic, okay. So, he or she wants to improve his skills, okay, little bit, maybe a two months three months program for we suppose 20,000 or 30,000 rupees his loan is required, okay, so if he goes to the bank bank will not give, right, because there is no collateral and kind of things. So the government must push actually money through the banking systems for people skill development, there should be certified skill development from the public private partnerships, kind of things, you know, maybe an extension of a vocational school and kind of things could be there all over the country. And it doesn't take much time to do that in two, three months time, you can actually easily set up that particular structure, so that you know, this becomes a sustainable thing for the long run. And as I said, that the New technology will come. So, new job opportunities will come up and people will easily then actually seamlessly go from one sector to the other sector. So, that is in the medium run which is a very important skill development for the country because that helps the manufacturing sector also.

Prof. Biswajit Nag: What I like to add here is India has a peculiar problem, what we call a middle income trap, okay. So, most of the countries who are in the middle income like Brazil is a country, Russia is a country middle income the problem of the middle income country they cannot become a rich country easily because they they they are suffering from a two obstacles, one middle income countries productivity is not as high as the developed country, but at the same time, the cost of production is not as low as the lower income countries because their wages are quite high Okay, if you look if you go to Brazil or Russia, their wage rate is much higher than India okay, but their productivity is not as high as Japan or US or Sweden. So, they are suffering from two particular problems. China is entering into this problem okay, because in China the wage rate is going up and China's productivity is not as high as that. So, China is trying to make a balance between these two. Unfortunately, India has is or rather moving into a middle income trap quite early because India is right now at the lower middle income level right. But India's wage rate is rising significantly because a lot of public services and other things are not available, which it should have been. So, the cost of living is going up, which is also pushing the wages, urban lives are you know, quite you know, fast and costly. So, companies need to pay higher wages. So, it is going up, but because of a lot of, not much skill set there with the people. So, those people are not able to work so effectively. So, the wages are rising, but the productivity is not rising. And that is India's most critical challenge. So, if the government thinks that next ten years, our mission should be to improve the skills of the youth. So that you know not everybody has to become an engineer. So there should be a whole lot of subjects or areas where actually the country needs people and actually there is a huge shortage, okay. And so, every area there should be, you know, skill centers in every town and every city. If there are then definitely there will be no new jobs will be coming up. And that is the way actually India can move forward.

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