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Economic slow down in India: A sectoral study

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Abstract
That the Indian economy is slipping into a recession is quiet apparent. The real GDP growth has gone down from a peak of 8.2% in 2016-17 to 6.8% in 2018-19, with the fourth quarter of 2018-19 dipping to 5.8%. The first quarter of 2019-20 is expected to dip further to 5.6%. Nor for that matter the fall in private consumption, which has gone down since the second quarter of 2018-19. Private consumption has been the main driver of India's growth, contributing about 60% to GDP, and its fall is dragging economic growth further down. The present article is an introspection into various aspects that led to the economic slowdown and sectoral impact of the same.

Keywords: economy, slipping, slipping, GDP

Introduction

According to global broking firm Goldman Sachs, as of June 2019, the current slowdown has lasted for 18 months, making it is the longest since 2006. More than half of the decline in economic activity has been driven by a consumption slowdown, which appears to be broad-based, with components other than auto contributing more than twice the effect of autos to the total consumption decline says the brokerage in a report.

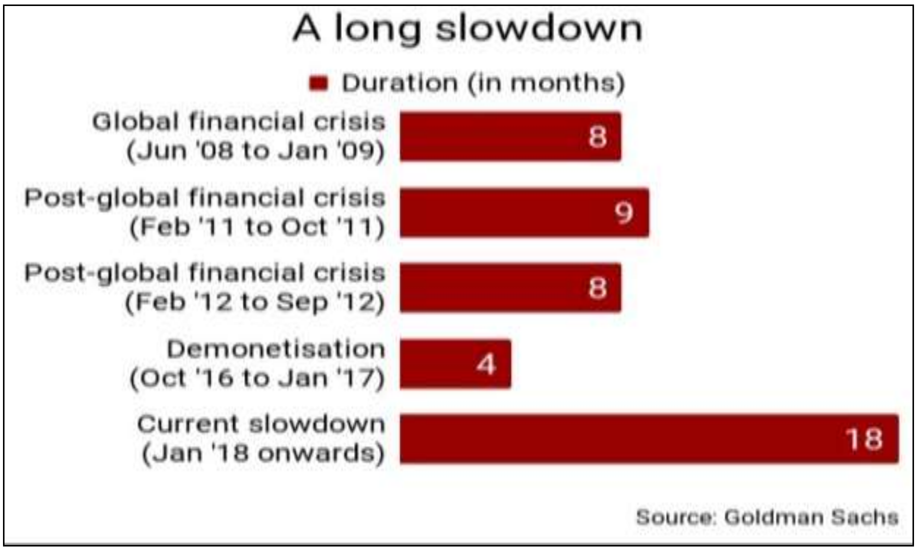

Fig 1

Since consumption expenditure is directly linked to income, especially for the lower and middle income working population forming the bulk of population of India, the imperative is to improve their wages to spur consumption demand. Wage growth is also linked to savings and investment. The Economic Survey of 2018-19 gives the example of China, where higher wages drove up savings rate, to argue for well-paying jobs in India and an effective minimum wage regime across the country. It notes that gross savings have fallen from 31.1% of GDP in 2015-16 to 30.5% in 2017-18 - entirely contributed by the household sector savings, which declined from 23.6% of GDP in 2011-12 to 17.2% of GDP in 2017-18. With this decline, investment rate has gone down.

Economy Slowdown- A Snapshot

- GDP is projected to grow 6 % in 2019 against back-calculated 8% in 2015-16
- GVA growth has shrunk from 8.03% to 6.79%
- IIP grew just 0.1% in February 2019- the lowest in 20 months
- In 2018-19, power generation grew 3.56%, the lowest in the past 5 years
- Passenger car industry grew just 3% in 18-19, the lowest in the past 5 years
- Car sales have tanked in urban markets in past 3 quarters: Maruti reported 8% drop in urban sales in Q4
- September and December 2018 quarters saw lowest growth in petroleum consumption in 7 quarters
- In 18-19, corporate India's sales and gross fixed assets

grew the second slowest in 5 years
- Finished steel production is the second lowest in 5 years
- RBI reported over Rs. 1 Lakh Crore fall in bank credit in the latest fortnight of April 12
- EPFO data shows 26% fall in average monthly job creation since Oct.

Distinct Slowdown

Both nominal GDP (includes inflation) and real GDP grew at the slowest-ever pace since the NDA took charge in 2014. Nominal GDP is a proxy for income growth, especially that of corporates. A slowing nominal GDP will eventually lead to low tax collections. The government estimated a 11% nominal growth in the Union Budget and over 15% of tax revenue growth

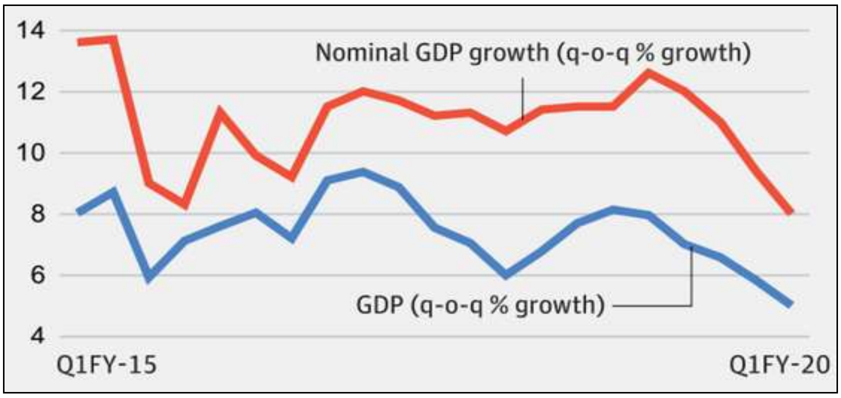

Fig 2

Declining Wage Growth: A Structural Issue

The SBI's study, Root Cause of the Current Demand Slowdown, says the reasons for the current slowdown are both structural and cyclical, apart from global uncertainties. Among the structural factors, it holds a substantial decline in both urban and rural wage growth as the "most crucial" one.

It is quite apparent that the Indian economy is slipping into a recession. The real GDP growth has gone down from a peak of 8.2% in 2016-17 to 6.8% in 2018-19, with the fourth quarter of 2018-19 dipping to 5.8%. The first quarter of 2019-20 dipped further to 5.6%. Nor for that matter the fall in private consumption, which has gone down since the second quarter of 2018-19. Private consumption has been the main driver of India's growth, contributing about 60% to GDP, and its fall is dragging economic growth further down.

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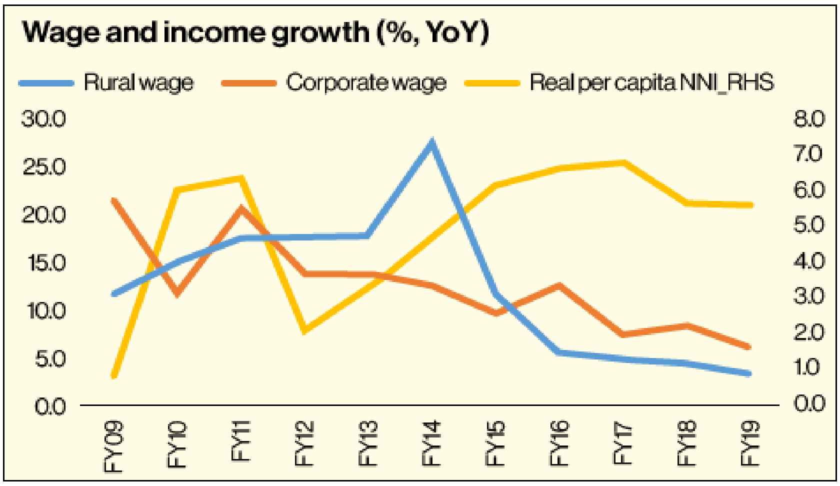
SBI's study says both urban and rural wages were growing in high double digits until a few years ago. Growth in urban wages (using corporate wages as a proxy) peaked at 20.5% in 2010-11 and then went down to single digit in 2018-19 (as companies went for cost cutting "in the midst of a massive deleveraging cycle"). Similarly, rural wages peaked at 27.7% in 2013-14 and went down to less than 5% in last three fiscals. It explains that this high growth phase was unsustainable (a deadly cocktail of wage-inflation nexus).



***Source*:** SBI Research

Fig 3

This decline in wages hit private consumption due to stagnation in income and household savings declined, it concludes.

A 2018 RBI's working paper, Rural Wage Dynamics in India: What Role does Inflation Play?, too had pointed out that rural wages decelerated significantly after a phase of high growth. The deceleration began after November 2014 and was marked by "low inflation occasionally surpassing growth in nominal wages, pushing real wage growth to the negative territory". This phase has been labelled as a period of "rural distress".

It further throws light on two major factors that drove high rural wage growth between 2007 and 2013, namely, implementation and quick progress of the MGNREGS and a healthy growth of the construction sector. The significance of both "weakened" later. It adds that subnormal monsoon years of 2014-15 and 2015-16 weakened agriculture growth negatively, impacting rural wages. Though rural economy saw some revival in 2016-17 due to normal monsoon, it did not provide a significant boost to the agriculture wages.

Factors That Triggered the Slowdown in the Economy

Demonetisation

Demonetization was a bad vibe. It disrupted and disturbed India's production and business networks that were conducted mainly in informal ways (downplay this in exams; just mention mild shock from it).

Banking sector and the prolonged NPA problems

Banks can't lend significantly, as far as their balance sheets are weak. The prolonged NPA problem tempted them to stay back from credit expansion. The next uptrend will happen only with credit expansion.

Farmer's income fall

Farmers are facing income fall due to adverse terms of trade. Agricultural prices are not increasing but the prices of other materials are increasing. Similarly, farmers living expenses to spend on industrial and service items going up.

Global factors

Trump's trade war created trust deficit in international trade. Another factor is the rising crude prices. Similarly, foreign capital is showing outflow trends.

Quick implementation of GST

GST implementation slowed down business activities as its procedural complexities discouraged big traders to procure materials from small unorganized players (downplay the point in exams).

Formalization driven away the informal sector from the value chain

Formalization of economic activities is always desirable. But its sudden implementation without preparing the small businesses slowed down economic activities. Meeting traders, experts, entrepreneurs to gauge the pulse of the nation, Sitharaman has become a reformer, pulling all stops to get the economy out of a six-year-low growth rate.

Sectoral Crises

From 12.1% growth in April-June 2018 to 0.6% in April-June 2019, the manufacturing sector experienced the biggest slowdown. This is the lowest growth in the last 6 years (barring q1 FY2018, when it shrunk because of destocking before GST implementation). For the fourth straight quarter both "mining and quarrying" and "agriculture, forestry and fishing" have grown at less than 5%.

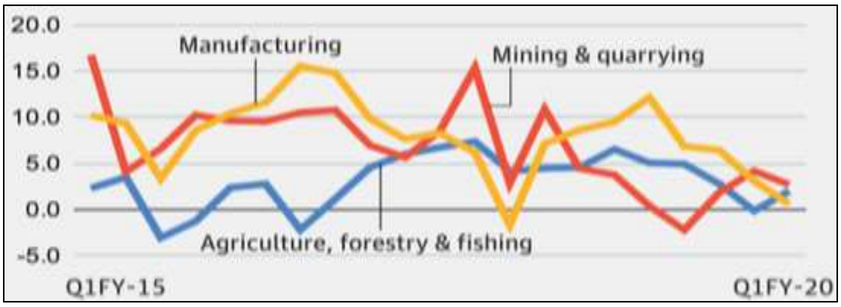
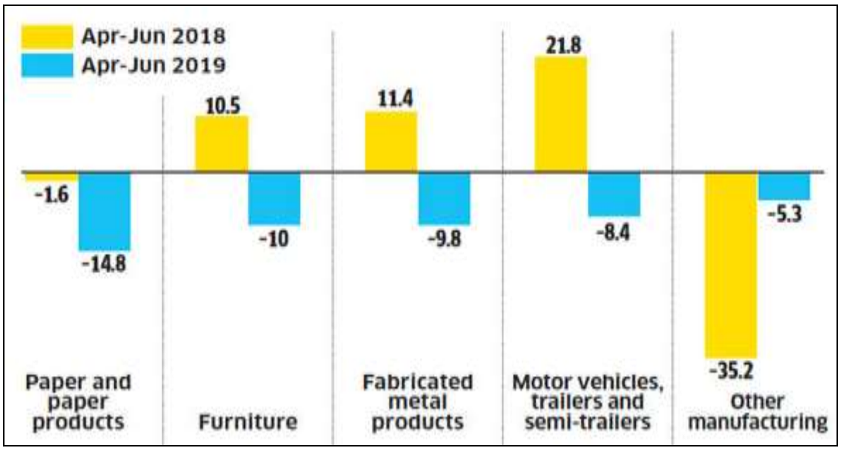


Fig 4: Sectoral Crises



***Source*:** CSO

Fig 5: Worst-hit Sectors in Manufacturing Y-o-Y IIP Change (%)

This is a clear sign that the slowdown narrative is not uniform across the manufacturing spectrum. Manufacturing accounts for over 16% of the India economy and employs 13% of the country's workforce. The pockets of growth in manufacturing may disappear if some of the struggling sectors, which are also big employers, do not recover in the next few months.

Laggardly pace

For a while now, the rest of the sectors have had growth rates within the 5% to 10% band. In Q1FY19, construction sector, an employment-intensive sector apart from Manufacturing, slowed down to a seven-quarter low (5.7%).

Economic Activity in the Indian Economy during the Economic Slowdown

The GDP of an economy is the sum of private consumption expenditure, investment, government expenditure and net exports (exports minus imports). There are many high-frequency economic indicators which tell us about the state of each of these four inputs that form the GDP. Following are some of the economic indicators to see how the economic activity during the period April to June 2019 has slowed down.

The consumption matrix

Consumption is the most important part of the Indian economy, given that it forms around three-fifths of the Indian economy. And any slowdown here is bound to affect the overall economy. Except for perhaps retail loans given by banks, there is a contraction in all other parameters which measure consumption in different ways.

Domestic car sales

During April to June 2019, car sales fell by 23.3% in comparison to the same period in 2018. This is the biggest contraction in quarterly sales since 2004 (that's how far back the quarterly data in the Centre for Monitoring Indian Economy database goes). A slowdown in car sales negatively impacts everyone from tyre manufacturers to steel manufacturers to steering manufacturers etc., when it comes to the backward linkages that car manufacturers have. As far as forward linkages are concerned, many auto dealerships are shutting down or shrinking. At the same time, the vehicle loans growth has slowed down to 5.1%, the slowest it has been in five years.

Two-wheeler sales

These have not been as badly hit as car sales. Between April and June 2019, two-wheeler sales contracted by 11.7%. This is the biggest fall since October to December 2008, when two-wheeler sales had contracted by 14.8%, in the aftermath of the start of the financial crisis. In fact, even mopeds are not selling, with their sales down 19.9% between April and June 2019 (In 2018-2019, a total of 880,000 mopeds were sold, suggesting there is still good demand for them).

Tractor sales

A good indicator of rural demand, tractor sales during April to June 2019, fell by 14.1%, the highest fall in nearly four years.

Housing sales

As per Liases Foras, a real estate research company, India's top 30 cities had 1.28 million unsold housing units as of March 2019, a jump of 7% from March 2018, when the number was at 1.2 million. This means that builders are building new houses at a faster pace than people are buying them. The real estate sector has forward and backward linkages with 250 ancillary industries. So, when the real estate sector does well, many other sectors, right from steel and cement to furnishings, paints, etc., do well too. This is something which isn't happening currently. The fact that real estate prices haven't gone up in years makes people feel less wealthy and as a result spend less.

Non-oil non-gold non-silver imports

This is a good indicator of consumer demand as it indicates when people buy more imported goods. During April to June 2019, these imports fell by 5.3%, the biggest contraction in three years. They had risen by 6.3% during the same period last year.

Firing up Economy

In the backdrop of economic slowdown the Central Government has taken following measures to revive the economy.

- Corporate tax slashed to 22%
- Rs 1.45 trillion revenue forgone
- New manufacturing firms can pay 15% tax

First Tranche: The Booster Dose

- Rolling back the surcharge on income of FPIs
- Rs 1,400 crore forgone by government
- Took back the prison sentence for CSR norms violation

Auto sector push

- Deferment of one-time registration fees for vehicles till June 2020
- Additional 15% depreciation on all vehicles acquired till 31 March 2020

Angel for start-up

No angel tax for start-ups under Income Tax Act

GST refunds

- Pending GST refund requests of the MSMEs will be addressed within a month
- In future, all GST refunds will be paid within two months of their application

Second tranche: Big Bank Reforms

- 10 PSBs merged into four
- Strengthened bank boards
- Improved appraisal mechanism for top executives
- Rs 11,550 crore capital infused into weak banks

Third tranche: Expanding Exports

- Rs 70,000-crore package for exports and real estate
- Setting up a stress asset fund four housing
- New scheme for reimbursement of taxes paid on exports
- Higher insurance cover to banks' lending working capital for export

Fourth tranche: Improving Credit

- "Loan melas" in 400 districts
- No stressed asset of MSMEs to be declared NPAs till

March 2020

Conclusion

The economic slowdown in India has resulted from multitude of factors. GDP slashed below 6% alarming for the economy. The overall Private consumption as measured with the domestic sales of car, two-wheeler, tractors and homes has seen a major decline in 2019 in comparison with 2018. Investment as measured in domestic commercial vehicle sales, bank lending to industry, Revenue-earning rail freight, final consumption of finished steel and the like have not been very encouraging. The decline in the net exports on negative continuum is witnessed in the economy reducing the foreign exchange earnings. The reformative measures proved little costly for the Modi Government leading to cascading effect leading to decline in the growth of the economy. The aftermath measures to check the same is not so rewarding. There is a long way to go in this direction to revive back the Indian Economy.

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