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Decoding the problem with Indian economy

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ABSTRACT

On one hand, the Economy is worryingly slowing at a persistent pace and on the under that country is burning on issues based on religion, policy and culture. The Govt. for a large part of the year was in denial that there is an actual problem with the economy. But the signals have been quite overwhelming for anyone to deny that our country has entered a phase of economic slowdown and things have been looking quite gloomy do far. Now comes the question of why are we in a state that we find us in today. The World Bank has said that the Indian economy is facing a severe slowdown and has predicted GDP much slower than its earlier predictions. This paper presents a brief review of the factors that led us to this position along with trying to look for solutions.

Keywords— *Structural or Cyclical problem, GDP, Inflation, Yield Curve, Unemployment*

1. INTRODUCTION

1.1 INDICATORS

1.1.1 Yield Curve: A yield curve is a line that plots yields (interest rates) of bonds having equal credit quality but differing maturity dates. The slope of the yield curve gives an idea of future interest rate changes and economic activity. There are three main types of yield curve shapes: normal (upward sloping curve), inverted (downward sloping curve) and flat.

This yield curve is used as a benchmark for other debt in the market, such as mortgage rates or bank lending rates, and it is used to predict changes in economic output and growth. The yield curve is of three types Normal, Inverted or Flat. An inverted or down-sloped yield curve suggests yields on longer-term bonds may continue to fall, corresponding to periods of economic recession.

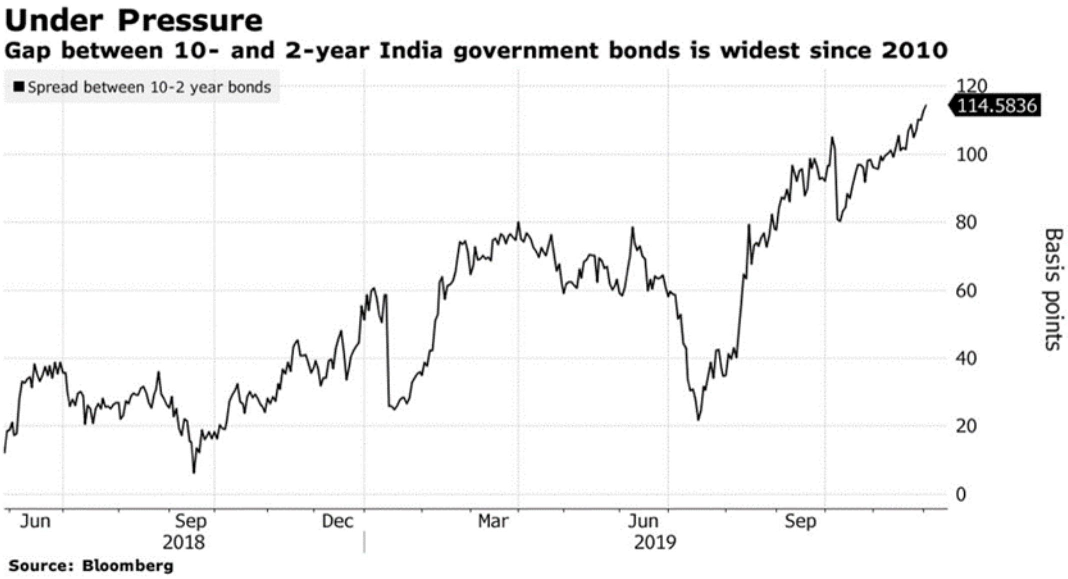

Fig. 1: Yield Curve

The gross domestic product grew 4.5% in the September quarter from a year earlier, the first time it's been below 5% since 2013. The weak GDP print will likely pave the way for a more interest-rate cut, helping to anchor yields on the short-end of the curve.

Mahendra Jajoo, head of fixed income at Mirae Asset Global Investments Co. in Mumbai said in Dec 2019 that "As long as there is a lack of clarity on how the fiscal deficit targets will be met and as long as the RBI maintains it's not bothered about market yields, the curve will continue to get steeper,"

1.1.2 Global Growth Is Slowing: Global economies are intertwined through trade. This means that slowing growth overseas can hurt the Indian economy. Recently the USA, China, Argentina, the U.K. and Germany have all seen deterioration in growth. Furthermore, there are no real areas of great strength to offset this. This global trade backdrop is becoming more of a drag. Also, issues such as Chinese trade tensions and Brexit continue to cause concern. In Simple context, the whole world is market for India but since they are not purchasing in the same quantity they used to hence our production is going south.

1.1.3 Unemployment Is Robust: A report on unemployment prepared by the National Sample Survey Office's (NSSO's) periodic labour force survey, has not been officially released by the government. According to Business Today, this report is the "first comprehensive survey on employment conducted by a government agency after Prime Minister Narendra Modi announced the demonetisation move in November 2016". According to this report, the 2017–2018 "usual status" unemployment rate in India at 6.1%, a four-decade high. The report states that male youth had an unemployment rate of 17.4% and 18.7% in rural and urban areas, while women youth had rates of 13.6 percent and 27.2 percent respectively in 2017-18.

The increasing unemployment rate is an indicator that production has reduced and also the fact that with an increase in unemployment the demand will further go down as this unemployed workforce is also a buyer, hence lesser money they have lesser will be the demand.

1.1.4 GDP: Gross Domestic Product (GDP) is the monetary value of all finished goods and services made within a country during a specific period. GDP provides an economic snapshot of a country, used to estimate the size of an economy and growth rate. GDP can be calculated in three ways, using expenditures, production, or incomes and in 2019 Indian GDP was 5th in the world at 3.6 trillion, however due to large population India is at 145th position in term of GDP (nominal) per capita. Per capita income of India is approx. 5 times lower than the world's average around $11,673. This figure is over 50 times lower than the richest country in the world and approx. 10 times greater than the poorest country in the world. India is at 33rd position in the list of Asian countries. In India, there has been lots of debate over GDP and people with very less knowledge of economics also debate over GDP and the fact that India's GDP is the second-fastest-growing next to China, however, these facts can be misleading also India's GDP growth rate has been lowest since 2013.

2. IS THE PROBLEM STRUCTURAL OR CYCLICAL

Many experts have debated whether this problem of the Indian economy is Structural or Functional

What is a cyclical slowdown?
A cyclical slowdown is a period of lean economic activity that occurs at regular intervals. Such slowdowns last over the short-to-medium term and are based on the changes in the business cycle. Generally, interim fiscal and monetary measures, temporary recapitalisation of credit markets, and need-based regulatory changes are required to revive the economy.

What is a structural slowdown?
A structural slowdown, on the other hand, is a more deep-rooted phenomenon that occurs due to a one-off shift from an existing paradigm. The changes, which last over a long-term, are driven by disruptive technologies, changing demographics, and/or change in consumer behaviour.

"A large part of the slowdown seems to be cyclical, but there are also structural components," said Axis Bank chief economist Saugata Bhattacharya. RBI's Annual report highlighted that there are still structural issues in land, labour, agricultural marketing and the like that need to be addressed.

What Lies Ahead.

By now it is widely accepted that the slump in demand for industrial and consumer goods that range from heavy equipment to automobile to soaps and biscuits have starkly reflected the reality of the slowdown. Regrettably, the govt. was working on the supply side by trying to inject inulin the producers in the form of a corporate tax cut. The curse of inflation is growing steadily and no one would like to enter the dangerous waters of stagflation ahead. The report of the expert committee on MSMe was set up by RBI and they have made recommendations like the support of venture capital funds and credit guarantee funds. The questions of unemployment and employment generation are fundamental in an economy and need to be addressed as soon as possible. Indian Govt needs to rejuvenate the MNREGA, PM-KISAN program to increase rural employment and increase the purchasing power of the people. A higher level of public spending for creating much-needed infrastructure in several sectors would not only generate employment but also create productive assets. India needs to work on the same model that the US used after WW1 to revive the economy, i.e. increase public spending, for instance, build roads, bridges, schools, hospitals etc. Ensuring lower borrowing cost, as well as adequate availability of credit, is crucial to helping create an enabling environment for consumer to consider taking out loans to fund their purchase. The taxes may also be cut but that comes with a risk of govt. losing it's financial goals also if the stimulus entails a large expenditure there could be second-order inflationary consequences. Govt. needs well-calibrated policy interventions and targeted incentives to select industries especially ones with high export potential would push MSMEs to a higher growth trajectory.

