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VIF Brief - January 2018

The Indian Economy: Casting Away Structural Chains

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About the Author

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The Indian Economy: Casting Away Structural Chains

A Year of Profound Changes

On November 8, 2017, the world took note of the first anniversary of the 45th Presidency of the United States of America. India 'celebrated' or debated an anniversary of a different nature. On November 8, 2016, the Government of India had announced the withdrawal of two high-denomination notes – Rupees 500 and Rupees 1000. While there is some disagreement as to whether the withdrawal constitutes demonetisation in the strict sense, the fact is that the stock of these two denominations were demonetised. It was not an end for High Denomination Notes (HDN) in general because these two denominations were replaced with a new set of 500-Rupee and 2000-Rupee (yes!) denomination notes. These two denominations constituted more than 85 percent of the notes or currency in circulation by value.

Within a few months, the Government of India introduced a much-needed regulatory bill for the Real Estate sector. It notified a legislation for facilitating insolvency and bankruptcy for those who are either unable or unwilling to repay their debt obligations. Then, in July 2017, it introduced a Goods and Services Tax (GST) replacing indirect taxes both in States and in the Union Government with a single GST. Hence, it has been a year of profound and long-lasting changes for the Indian economy. What do they collectively mean for the outlook for the Indian economy?

See-sawing Growth in three Years

The withdrawal of the specified HDN constituted a huge liquidity shock to the economy, unsurprisingly, as they constituted a huge chunk of the currency in circulation by value. The economic growth rate predictably slowed in the first two quarters of the calendar year 2017. In the 12 months ending June 2017, growth rate

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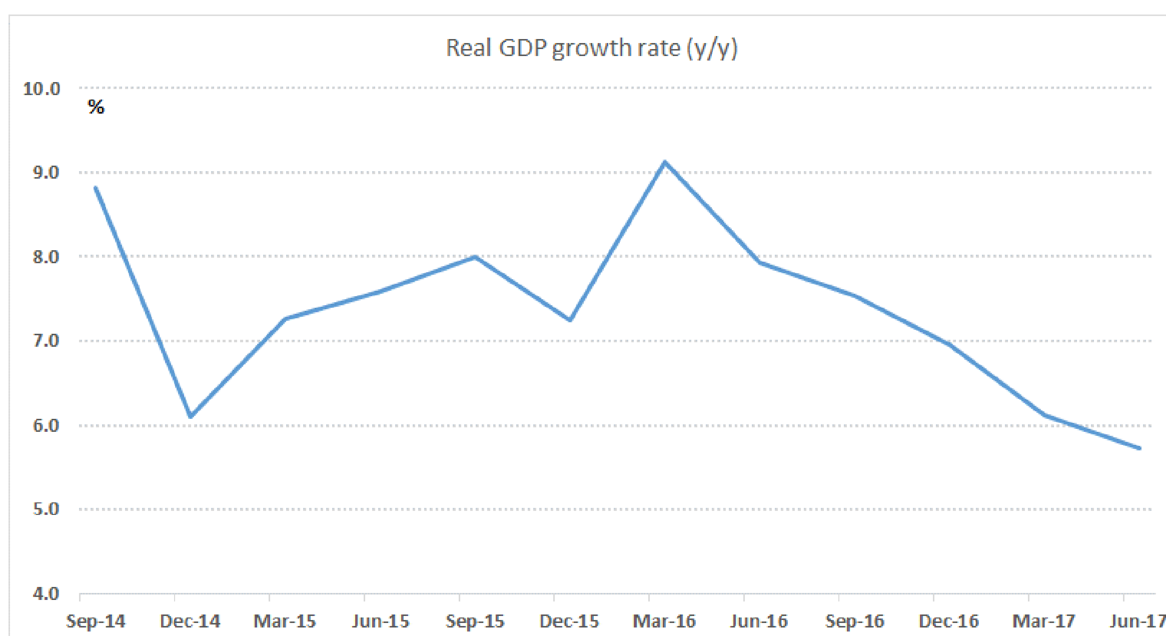
of the real Gross Domestic Product had slowed to 5.7 percent. Statistically, it is impossible to quantify the impact of the withdrawal of the HDN on economic growth. Economic growth had already begun to slow from the 9.1 percent rate attained in the first quarter of 2016. The gradual slowdown in the growth rate from that level was due to a multiplicity of factors.

Before explaining that, we have to acknowledge here that the growth rate climbed from 6.1 percent in the quarter ending December 2014 to a high of 9.1 percent in the quarter ending March 2016 on the back of lower price of crude oil that boosted government revenues and led to higher government spending. Part of the effect was, of course, statistical. In 2015, India's Central Statistical Organisation changed the methodology of calculating economic growth, citing the availability of more granular information on businesses and had shifted the base year from 2004-05 to 2011-12. Growth rates from 2011-12 onwards were revised higher. However, due to the non-availability of historical data – CSO is unable to revise historical GDP data for the new base year 2011-12 - it is hard to place these growth estimates in the historical context.



Source: Handbook of Statistics on the Indian Economy, Reserve Bank of India.

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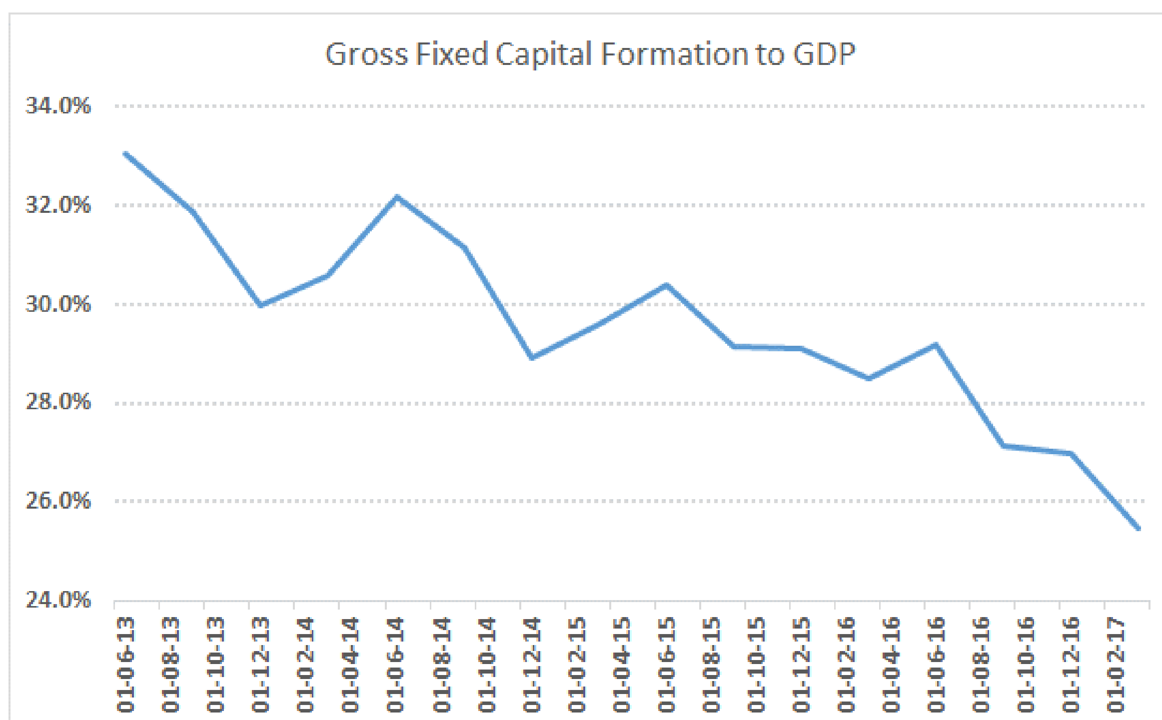
Now that we had explained the acceleration from 6.1 percent to 9.1 percent, how did the growth rate come down from 9.1 percent to 5.7 percent? As stated earlier, there is more than one explanation. Global growth had slowed in 2015 and it bottomed out only by mid-2016. Consequently, net exports was a drag on India's economic growth. The base effect of the crash in oil price had disappeared. More importantly, India was hobbled by the twin balance sheet problem. India's corporations were saddled with huge amounts of debt accumulated in the boom years preceding and following 2008, the year of the global financial crisis. Most of these companies were concentrated in the infrastructure sectors – steel, cement, power and lately, telecom. The slowdown in India's economic growth rate from 2011 onwards until 2014 had upended their plans and left them with debt that they could not service. Naturally, they had no appetite for taking on new loans to make green-field investments and create assets on the ground. India's fixed capital formation had slowed from 33.0 percent of GDP in June 2013 to around 25.5 percent of GDP in March 2017.



Source: Handbook of Statistics on the Indian Economy, Reserve Bank of India.

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Since the bulk of the debt had been taken from India's banks which are predominantly government-owned, the banking system had been groaning under the burden of non-performing assets (NPA). In some cases, the bank capital had been fully eroded and provisioning was on the lower side. Banks had also resorted to restructuring their loans so that they would be treated as current. Hence, problem-recognition was slow. The Reserve Bank of India ended the official sanction of forbearance and directed banks to account for all their NPA by March 2017. This had the effect of slowing down credit growth in the country. Both demand for and supply of credit were under stress. Private sector banks which were relatively less affected because they had not lent as much to corporations as government-owned banks had, continued to make personal loans for housing, automobile purchase and credit card debt too grew rapidly. Overall bank credit growth to businesses of all sizes had slowed to a crawl. In general, in recent quarters, government spending and private consumption expenditure had shouldered the task of maintaining economic growth. With export demand absent and with private sector investment spending held back by debt concerns, it was no surprise, therefore, that economic growth had decelerated for six quarters up to June 2017.

In the quarter ended September 2017, economic growth measured in constant 2011-12 prices has improved to around 6.3 percent (year to year). The biggest contributor to the improvement in GDP growth came from a rebound in manufacturing. Manufacturing growth rebounded to 7 percent from 1.2 percent in the second quarter. But, this is a puzzle considering that the index of industrial production went up only by 2.2 percent in the July-September quarter. Further, the rebound in manufacturing growth without an improvement in India's export performance is another source of anomaly. However, it is possible that India's economic growth is on an improving trajectory from here on. But, the firming trend in global crude oil prices remains a risk. Another source of risk is correction in asset

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prices globally. That would undermine confidence and halt global growth in its tracks, snuffing out the chances of recovery in India's exports. However, an end to initial compliance issues with GST and banking recapitalisation can improve the domestic growth impulse. It is possible that economic growth rebounds to between 6.5 percent and 7.0 percent in the coming quarters.

Demonetisation – upfront Costs and uncertain Future Benefits

Into this slowing growth dynamic, the government announced its unprecedented banning of HDN in November 2016. It is very difficult to pass a definitive judgement on the success or failure of the exercise because economic benefits, given sufficiently long time, might exceed the costs. However, near-term, the costs easily exceed the benefits. The government spelt out as its objectives the curbing of black money, corruption and terrorism. Subsequently, digitisation was added as a goal, more as an after-thought. If the exercise was about making it difficult to store ill-begotten wealth in cash or to use such cash for financing real estate transactions, the introduction and retention of currency note of the denomination of Rupees 2000.0 defeats the purpose.

It is often claimed that India has a low tax to GDP ratio and that there is a need to increase the tax ratio to meet development expenditure. But, a quick perusal of World Bank data on this ratio for many developing countries suggests that India is far from being an outlier on this matter. Further, there is plenty of statistics put out by the Government side on the number of high income tax payers being disproportionately few[1]. However, tax compliance is a two-player game. Tax rates and tax administration matter as much as the tax morality of taxpayers. Internationally, there is evidence that reasonable tax rates and a tax administration that is not coercive or vindictive lead to, over time, enhanced tax compliance and revenues for the government. India has a long way to go with respect to both.

[1] See, for example, Arun Jaitley, Union Budget Speech 2017-18, February 1, 2017 (http://indiabudget.nic.in/ub2017-18/bs/bs.pdf) .

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According to the 'Ease of Doing Business' survey, India's overall tax incidence at 55.3 percent is among the highest in the world. It used to be above 60 percent until last year but the introduction of GST has brought the tax incidence rate down. However, it is debatable if India's businesses see the benefits of the introduction of GST yet.

Long Way to Go for GST to become 'GST'

GST, dubbed the nation-wide single indirect tax, was introduced in July 2017. In theory, it should have facilitate the creation of a single market for goods and services in India by eliminating inter-state tax barriers. The initial months since the new tax had been introduced have witnessed considerable confusion, uncertainty and angst especially among small businesses. Not only have there been too many rates but the processes of filing returns and claiming input tax credits have proven to be daunting for many businesses, especially small and medium businesses. Further, given that a substantial chunk of daily consumption items have been exempted from GST, the Government has compensated by levying a GST rate of 28percent on several items. The Union Government has guaranteed a 14 percent compounded increase in annual revenues for five years to State governments, to make them give up their right to levy local sales tax, etc.

The design of the GST has featured an undue concern on ensuring revenue neutrality (that is, the expected revenue from the new tax should not be lower than the projected revenues from the taxes that were being withdrawn) rather than the tax being geared to facilitate enhanced economic activity, ushering in a genuine single market in the country. The consolation is that the government and the GST Council – the body that decides on GST rates comprising State Finance Ministers and the Union Finance Minister – have proven responsive to complaints and have simplified procedures, lowered the rates and have removed exemption limits. More work remains to be done to make it a genuinely 'Good and Simple' Tax and a

facilitator of a national market in India. But, the direction appears to be right. However, it is difficult to estimate is the growth impact of the original bad design of the tax and the duration of such impact. One can only hope that the damage is limited.

The Bright Side

Financial Inclusion

While the debate continues on the wisdom of demonetisation, its execution and on the design and implementation of GST, the government seems to have done a good job with two other equally important reforms. One is the Financial Inclusion scheme – banking the unbanked. The 'Pradhan Mantri Jan Dhan Yojana' (PMJDY) scheme undertaken in the initial months of the new government in 2014 was a massive success in enabling many millions of Indians to have a bank account in their names for the first time. With that, they will now be able to receive the cash transfers that they are entitled to, under various government schemes and subsidies. The success of PMJDY in bringing banking services to many Indians will greatly facilitate government's efforts to transfer cash benefits to citizens in lieu of persisting with price-distorting subsidies.

It is similar to the mobile phone connectivity that India achieved for its citizens in the first decade of the millennium. An empirical study ('Bank Accounts for the Unbanked: Evidence from a Big Bang Experiment', May 2017) has shown that PMJDY accounts are increasingly actively used over time - 70percent of the accounts migrate out of dormancy into active use. Second, activity levels in PMJDY accounts increase over time, a pattern not necessarily seen in non-PMJDY accounts. In many specifications, activity increases in PMJDY accounts relative to non-PMJDY accounts. These findings are especially stark given that non-PMJDY accountholders in our sample appear to be much poorer and have transaction sizes that are one order of magnitude smaller. Finally, we find that the active accounts experience significant

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increases in cash balances. Government direct benefits transfer aids but does not fully explain usage. Overall, the data indicate that the unbanked learn by doing, and increase usage of accounts for transactions, liquidity management, and increasingly, balance accumulation."

More good news is possible out of the successful financial inclusion initiative. Another paper ('Who wants to be an entrepreneur?', May 2016) suggests that "financial development facilitates economic growth by moving workers out of less productive, informal entrepreneurial activity into formal jobs in more productive firms." If this were to happen, India could reasonably aspire to resemble the prosperous high growth economies of the West. But it would take time and much more remains to be done to get from here to there. The important and underlying requirement is that productive firms create formal jobs. Unfortunately, it is not happening. It requires fixing two issues. One is the issue of NPA in the banking system and the other is the absence of dynamism in the formal business sector.

That a scheme like PMJDY was required after five decades of public sector banking is testimony to the fact that the poorer sections of society were not able to access financial services adequately from the organized financial system. Therefore, if the government were keen to take credit for the successful implementation of the PMJDY, and correctly so, it must be prepared to take the blame for allowing NPAs in public sector banks to fester for three years. May be, just maybe, there is some light at the end of the tunnel now.

Easing the Exit from Debt

The second success of the government is in putting in place a framework for Insolvency and Bankruptcy. That is working well. Cases are being referred to the National Company Law Tribunal which adjudicates on bankruptcy cases. Assets owned by defaulting debtors are quickly disposed of and creditors' claims are settled. Creditors too must take a haircut on their claims and move on, instead of

dragging the matter for years, keeping unviable and bad assets at inflated book values without providing for losses. All that is in the process of becoming history.

Stung by the growth slowdown to 5.7 percent (as discussed earlier), the government has moved to announce a massive bank recapitalisation scheme. It should take care of the substantial portion of the requirements of government-owned banks, provided there is no fresh accretion to their NPA. The government has also announced that it would use the opportunity to strengthen the banking system and banks where the government owns the majority stake. Little details are available on that, however. It would be a pity if the opportunity were missed to recast the Indian banking system owned by the government.

Government ownership plagues governance of these institutions. Prudent commercial considerations seldom inform their lending decisions. Either they lack the skills to assess credit risk correctly or other considerations dictate the creation of bank assets. This is India's third NPA crisis in three decades. Often, crises are the only opportunity to abandon the old and failed ways and usher in desirable changes that strengthen the institutional infrastructure. With bond market developments in the country stymied by both the government's first and large claim on national savings and due to the private sector's penchant for negotiating loans with bankers on favourable terms, it is imperative that the banking sector be reformed and decoupled from the government – both in terms of ownership and management.

Long-term Priorities

The short-term growth setbacks caused by the withdrawal of HDN and the needlessly complicate design and introduction of Goods and Services Tax may be ironed out over time. The bigger question is the long-run growth outlook. The chart below shows the compounded annual growth rate of Gross National Income per capita over a moving 5-year period. The growth momentum has slowed in recent years.

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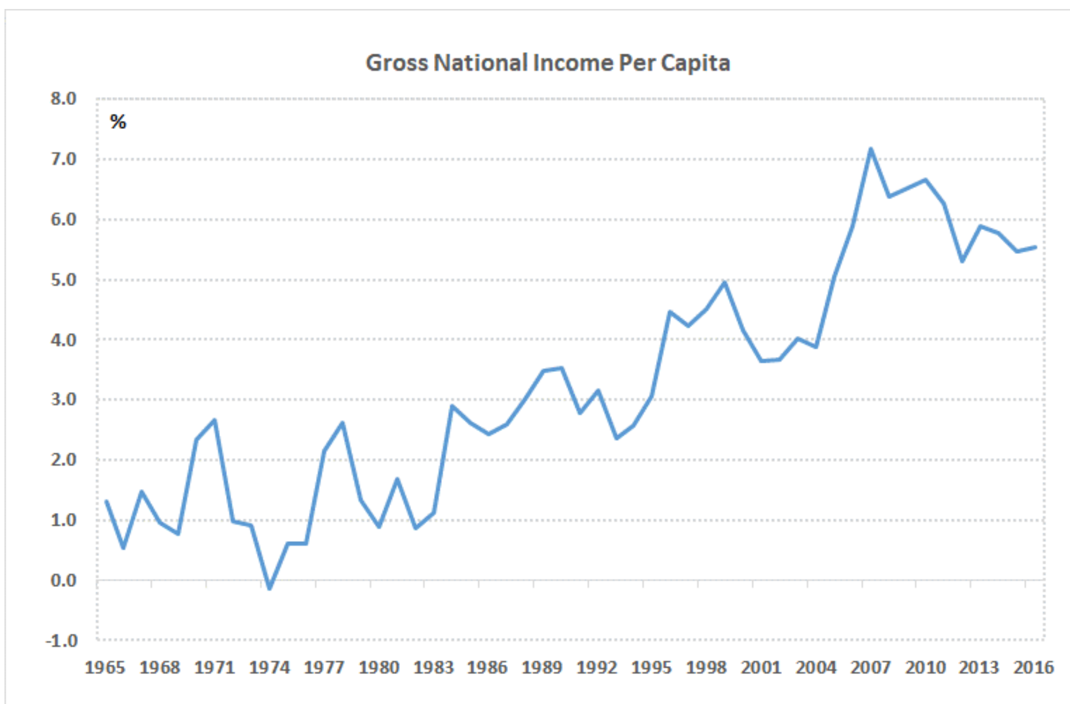

Source: World Bank

The challenge for the government is not only to restore growth but to sustain it. Among many things, it needs to address two things urgently. One is to eliminate the bias against bigness that has plagued Indian policymaking since Independence to the present day and, secondly, it has to ensure that its tax policies do not kill the economy in the process of extracting revenues for the government. The third issue is one of access to capital for small businesses. The government has a role in facilitating it but the responsibility lies with the private sector.

The 'Anti-Big' Bias

For that challenge to be met successfully, India needs to tackle the extreme fragmentation of its production – both in farms and factories. India's economic structure in farms and factories is fragmented, inefficient and primitive. The numbers are shocking and beyond belief. India cannot "make it" with such extremely nano and micro-sized farms and factories. There are an estimated 63.4 million non-agricultural unincorporated enterprises (excluding construction)

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contributing gross value added (GVA) of Rs 11.5 trillion only. In contrast, only 189,468 registered (with the Annual Survey of Industries) factories generate Rs 11.6 trillion of GVA. More startlingly, just 4.1 percent of them have 500 or more workers and they contribute 60 percent of the GVA of the registered factories. The fragmented production structure makes the economy prone to overheating and stagflation – lower growth combined with higher inflation. Too few large enterprises in the private sector capture the banking sector. Too many small and unproductive enterprises are unable to respond to demand surges resulting in higher inflation. Current account and trade deficits widen, consequently, bringing pressure on the currency to depreciate. The solution is not to favour the current big firms but to favour potential enterprises becoming big or to encourage firms to start big. But, the policymaking in India has an 'anti-big' bias.

The Economic Survey of India 2012-13 featured a rigorous discussion on India's demographic dividend and how it could be harnessed for the benefit of the country. That is feasible only if the youth have the right education and skills and can either be entrepreneurial or earn a living through employment. Typically, jobs are created when firms hire more as they grow in size. The shocking fact about India is that, in 35 years of existence, the productivity of a 35 year-old firm merely doubles, while its headcount actually falls by a fourth whereas a company in the United States grows ten times both in terms of operations and employment.[2]

This is neither normal nor healthy. Therefore, it is natural for economists and policymakers to examine causes. They are multiple. Labour laws, rules and regulations and the cost of hiring and employing permanent workers matter. That is a vast topic. We may not be able to do justice to it in this piece. Table I from the Survey examines policies that encourage or condemn firms to stay small.

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[2] Source: World Development Report 2013 (World Bank) cited in 'Comparison of Labour Laws: Select Countries', Occasional Paper No. 160, Export-Import Bank of India, August 2013.

The Survey has a Table on Government incentives dis-incentivising growth:

Figure 2.14: Government Incentives Dis-incentivizing Growth *(list not exhaustive)*

	SCHEME	DESCRIPTION	AVAILABLITY OF INCENTIVE BY SIZE OF ORGANIZATION			
			MICRO	SMALL	MEDIUM	LARGE
Non-Financial Incentives	National Manufact. Competitiveness Programme	• Assistance aimed at improving processes, designs, technology	✓	✓	✓	✗
Non-Financial Incentives	Government Purchase and Price Preference Policy for MSEs	• 358 items reserved for exclusive purchase from MSEs. 20% of annual value of goods and services purchased to be procured from MSEs.	✓	✓	✗	✗
Financial Incentives	Credit Linked Capital Subsidy Scheme for Technology Upgrade	• 15% capital subsidy for Tech. Upgrade on term loan from approved inst.	✓	✓	✗	✗
Financial Incentives	Credit Guarantee Fund Scheme for MSE	• Credit guarantee for collateral free loan for loans upto Rs. 1 Cr.	✓	✓	✗	✗
Financial Incentives	MSE-Cluster Development Programme	• Training, tech, etc.: grant of 75% of project cost • Tangible assets and infrastructure: grant of 80% of project cost	✓	✓	✗	✗
Financial Incentives	Quality upgradation in MSEs - incentives for certification	• Reimburse 75% of ISO certification expenses (max. Rs. 75K one time)	✓	✓	✗	✗
Financial Incentives	Micro Finance Programme	• SIDBI supporting NGOs/Micro Finance institution in providing loans	✓	✗	✗	✗

Source : Ministry of Micro, Small, and Medium Enterprises

The Survey notes, "Schemes and interventions based on tightly defined classifications create an incentive structure that might prevent firms from growing. Service tax exemptions for firms with less than Rupees 10 lakh revenue and exemption from central excise duty for firms with an annual turnover of less than Rupees 1.5 crore are examples of these schemes."

Fast forward four more years and the newly constituted NITI-Aayog picks up the theme in its latest Enterprise Survey of Indian States on the ease of doing business in India.[3] The survey found that firms with hundred or more employees took significantly longer to get the necessary approvals, faced more regulatory obstacle and higher costs of compliance than smaller firms. Tax regulations and environmental clearances were bigger obstacles for firms employing more than ten people. These things make it hard for firms to grow in size.

[3] See 'Executive Summary' and Chapter 9 of 'Ease of Doing Business – an enterprise survey of Indian States', NITI Aayog & IDFC Institute, August 2017.

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In fulfilling large export orders, India's smaller factory sizes are big deterrent. A typical textile factory in India had 150 people whereas a factory in Bangladesh had 600 people. The Textile Commissioner said recently that India's textile industry would grow to a size of USD 250 bn in two years from the present size of USD 150.0 bn.[4] It is pertinent to note here that only two textile firms, Alok Industries and Arvind are big. Alok Industries had a turnover of little under USD 2.0 bn in the year ending March 2016 whereas Arvind had a turnover of around USD 800 mn. This fragmentation can be contrasted with the IT industry where billion-dollar firms are numerous.

Importantly, the anti-big bias is in the minds. In a telling observation, an entrepreneur who runs an apparel sourcing company noted that, in China, "The volumes are so high they do not start out thinking you are a crook. Here, it is exactly the opposite. You can price yourself out or you can time yourself out."[5] The anti-big mindset not just among politicians and senior policymakers but also in the operational layers of bureaucracy must be one of the biggest causal factors behind a vast proportion of enterprises remaining pygmies in India.

On top of this, in recent years, the penchant of the political leadership to confer short-term (and long-term economically ruinous) fiscal benefits to the poorer segments of the population has meant that terrorism of the taxpayers that used to be the norm up to the Nineties has returned with a bang.

Tax Policies and Economic Activity

A 2015 World Bank paper on tax regimes in South Asia noted that generous corporate tax incentives require a higher tax rate compared to what would have been needed if all firms were subject to the same tax regulations. While tax

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[4] See 'Textile industry size to touch $250 billion in 2 years, says official', 4th July 2017 (http://economictimes.indiatimes.com/articleshow/59443523.cms).

[5] 'Rahul Jacob: Will garment factories move to Vietnam?', Business Standard, 2nd March 2016 (http://www.business-standard.com/article/opinion/rahul-jacob-will-garment-factories-move-to-vietnam-116030201031_1.html) .

incentives may benefit the privileged firms, they worsen the overall investment climate and put disproportionate pressure on a narrow range of taxpayers. Often, such tax incentives are offered to less productive firms or activities, dragging overall economic productivity down even as it introduces distortions and sends the wrong message to productive and efficient firms.[6]

The policy implications are clear. India needs lower tax rates, higher tax thresholds, and a drastic and rapid elimination of ad-hoc tax exemptions and concessions. The government made a beginning in this direction in the budget for 2016-2017. It announced a gradual reduction in corporate income tax and phase-out of exemptions. The budget of 2017-2018 did not follow through on them. The basic corporate tax rate had been brought down only for firms that have a gross income of less than 500 million rupees. That is a pity.

The fact that GST had to be amended comprehensively within four months of introduction is an implicit admission that, in its initial design, it represented the triumph of the moral police and that of the bean counter. On November 9, 2016 – the day after the Prime Minister had announced the withdrawal of HDN, we had noted, "short-term liquidity squeeze could be severe and hence economic activity could suffer. Further, with the eventual design of the GST looking more complicated than originally envisaged and with the timelines getting shorter, uncertainty could be compounded. That risk is non-trivial. That is why GST should have been more concerned with simplicity, ease of use and implementation rather than revenue considerations. Bold thinking was always needed and more so, in the light of this announcement."

Successful policymaking is as much about entrepreneurship and risk-taking as commercial businesses are. Crucially, it is also about finding the right balance

[6] Anna Reva, "Toward a More Business Friendly Tax Regime: Key Challenges in South Asia," Policy Research Working Paper 7513, Equitable Growth, Finance and Institutions Global Practice Group, December 2015. The World Bank Group.

between enabling and policing. The government must bet on economic activity and not on economic policing. A reasonable tax regime that is non-vindictive and non-usurious in its administration is the need of the hour in India.

Access to Working Capital

We should bear in mind that the problem of unproductive micro and small enterprises is not merely on account of government policies and attitudes in the government against size but it is also because the private corporate sector denies working capital to their small suppliers. The unequal balance of power between corporate buyers and small suppliers ensures that the latter are at the mercy of the former for payments against supplies. That often does not come on time and even palms have to be greased to get payments released.

If the buyer is monopsony, then the supplier's bargaining position is even weaker. Nor can they afford to pursue legal remedies against recalcitrant corporate customers. Such remedies will be costly, protracted and may ruin the business too. 'Factoring' is the answer. Small and medium-sized enterprises (SME) suppliers discount their receivables and bills of exchange with banks who buy them (with or without recourse to the SME, in the event of non-payment) at a discount and then collect the proceeds from the corporate buyer. The idea was included in the report of the Raghuram Rajan Committee on Financial Sector Reforms in 2008. Then, Reserve Bank of India (RBI) appointed a working group which submitted its report in November 2009. RBI then issued a concept paper in 2014. Then, the draft guidelines were issued followed by final guidelines. Receivables Exchange of India (RXIL), India's first Trade Receivables Discounting System (TReDS) started operating only in January 2017. The time taken underscores the glacial pace at which crucial reforms that would lift the economy on to a higher growth path are pursued. The world over, on providing working capital to small suppliers, things are

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moving much faster.[7]

Six months after its commencement in January 2017, hurdles to the smooth of functioning of RXIL are emerging. Companies are wary of uploading invoices lest competitors come to know about their suppliers. Second, this is important, "since TReDS is a transparent system, they (companies) necessarily would have to settle the suppliers' invoices within 45 days of acceptance of goods/services rendered". The Government deserves credit for insisting that public sector enterprises should mandatorily register themselves in the TReDS platform. It has done so as part of its recent policy package on recapitalisation of banks and on infrastructure investment. The Government and RBI must find ways to drag the private sector to be part of the platform such that one of the biggest hurdles that prevent small firms from growing is removed.

Concluding remarks

Converting Potential into sustained Performance

On 16th November, Moody's Investor Services upgraded India's sovereign credit rating from 'Baa3' to 'Baa2'. It is the first rating upgrade for India in fourteen years.[8] In doing so, Moody's recognised the importance of bank credit growth for India's growth story and the significance of the government's decision to recapitalise banks. Importantly, Moody's said that India's public debt profile was unlikely to deteriorate. That is a statement of confidence on India's future growth trajectory. That reinforces what the International Monetary Fund had noted too. As part of its annual consultations and assessment of its member countries, the Fund publishes the 'Article IV' report. It projects the public debt and deficits of member countries as part of the exercise. India's public debt and deficit profile over the next several years

[7] See https://www.economist.com/news/finance-and-economics/21730150-squeezed-suppliers-and-big-corporate-buyers-stand-benefit-technology .

[8] See https://www.moodys.com/research/Moodys-upgrades-Indias-government-bond-rating-to-Baa2-from-Baa3--PR_374998

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is in sharp contrast to China's profile. See the tables below. They tell their own story.

The table for China:

Memorandum Items	2012	2013	2014	2015	2016	2017*	2018*	2019*	2020*	2021*	2022*
Nominal GDP (bn RMB) 7/	54,099	59,696	64,718	69,911	74,631	81,344	88,364	95,919	104,067	112,608	121,482
Augmented debt (% GDP) 8/	44.1	48.1	52.3	58.2	62.2	68.1	73.2	78.1	83.1	87.6	91.5
Augmented net lending/borrowing (% GDP) 8/	-5.1	-7.6	-7.2	-8.4	-10.4	-10.6	-10.8	-11.1	-11.2	-11	-10.7
Augmented fiscal balance (% GDP) 9/	-7.8	-10.3	-9.8	-10.2	-12.4	-12.6	-12.6	-12.6	-12.6	-12.3	-11.9

* Projected figures.

Source: People's Republic of China 2017 Article IV consultation—press release; staff report; and statement by the executive director for the People's Republic of China, International Monetary Fund, August 2017 (Table 1, page 43).

The table for India:

Fiscal position (% GDP)	2012/13	2013/14	2014/15	2015/16	2016/17*	2017/18*	2018/19*	2019/20*	2020/21*	2021/22*
Central government balance 4/	-5.1	-4.6	-4.2	-4.1	-3.8	-3.7	-3.5	-3.3	-3.0	-2.8
General government balance 4/	-7.5	-7.6	-7.3	-7.0	-6.8	-6.6	-6.2	-5.8	-5.5	-5.2
General government debt 5/	69.1	68.0	68.3	69.8	69.7	68.6	66.9	64.8	62.7	60.5

* Projected figures.

Source: India 2017 Article IV consultation—press release; staff report; and statement by the executive director for India, International Monetary Fund, February 2017 (Table 7, page 62).

As for the growth outlook, given India's demographic advantage and the substantial scope for productivity improvement in India's fragmented farm and factory sectors ,

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it should be possible to grow the economy at a nominal rate of around 12 percent annually for over a decade or more. However, it won't come easily. The government can facilitate that by focusing on liberalising higher education, on reducing corporate taxes as promised and by actually recapitalising banks. Of course, addressing some of the issues identified earlier such as continued simplification of GST would help. Notwithstanding these, India faces more challenges than East Asian nations faced in their development phase.

In the twentieth century, success stories of economic development were to be found in East Asia and they rode the manufacturing wave, producing for the advanced world. Whether India can hope to repeat it is a question that is not answered easily. Trade protectionism is on the rise and global growth, on average, has slowed. With aging populations, productivity in the western world is on the decline. Information technology industry, India's growth engine in the first decade of the new millennium, is undergoing profound transformation. Further the advent of robotics and artificial intelligence has unpredictable consequences for reviving the manufacturing sector. Among other things, it raises a different set of skill demands on the population. Education has to be re-thought. Then, there are health and environment concerns. Recent pollution levels in the national capital underscores the enormity of the challenges that India faces on both the fronts.

Therefore, successful economic development and the achievement of middle-income status in the twenty-first century is arguably considerably more difficult than it has been in the previous two centuries. Hence, the burden on the political leadership today is immeasurably greater than it has ever been. Not only should they sustain their focus and energies but also keep themselves open to honest and competent advice. That is what would increase the chances of the government prioritising and addressing the right issues which have been discussed in this note.

Tamil sage Thiruvalluvar had dedicated one chapter (10 couplets or 'Kural', from

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441 to 450) to the idea of surrounding oneself with wise men who would keep kings grounded and ensure that they rule the kingdom well, in the interests of all the subjects. I share the translation of four of them here:

> *A king wise enough to have men of greater wisdom than he to advise him shall be a powerful ruler. (Kural No. 444);*
>
> *Where the king's counsellors possess the courage to reprove him when necessary, nothing on earth can bring about such a king's ruin. (Kural No. 447);*
>
> *Without courageous counsellors to point out his faults and so protect him, a king will ruin himself, even without foes. (Kural No. 448);*
>
> *It is foolish surely to incur enmity of many foes, but 10 times worse to lose righteous friends. (Kural No. 450).*

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The Vivekananda International Foundation is an independent non-partisan institution that conducts research and analysis on domestic and international issues, and offers a platform for dialogue and conflict resolution. Some of India's leading practitioners from the fields of security, military, diplomacy, government, academia and media have come together to generate ideas and stimulate action on national security issues.

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