THE HINDU
OPINION » LEAD

May 1, 2015
Updated: May 1, 2015 03:35 IST

Growth: the next steps to be taken

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Strong economic growth is imperative as growth is the answer to many of our socio-economic problems. Prospects for a rise in growth rate appear to be bright, which depends critically on implementing, in a time-bound manner, the various initiatives announced in the Budget.

The Hindu
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TOPICS
economy, business and finance
economy (general)

The gloom over economic growth appears to have dissipated a bit after the new numbers on National Income were released at the end of January 2015. However, there is continued scepticism about the numbers as several analysts feel that they are not in accord with the ground realities. According to the advanced estimates for 2014-15, the growth rate is projected at 7.4 per cent. What are the prospects for 2015-16? We do not have the data for past years reworked on the new base and the new methodology, and without such a time series it becomes hard to forecast. Perhaps, 2015-16 will be a shade better than 2014-15, if all the positive factors mentioned later come together. However, it will fall short of the Budget expectations of eight per cent.

Favourable factors and uncertainty

What are the favourable factors that can contribute to a better performance of the economy in 2015-16? First and foremost, there is the advantage of low crude oil prices. This will not only reduce the oil import bill and impact favourably on the current account balance, but will also moderate the price increase in general because petroleum products are used in the production of almost every commodity and service. Second, the credit rating agency, Moody's decision to upgrade the outlook to "positive" may facilitate the inflow of capital. Though the recovery of the advanced economies is still tepid, the external environment as far as India is concerned may be benign. On the domestic front, there are signs of a gradual improvement in the investment "sentiment".

Still, there are several unfavourable or uncertain factors, chief among them being the uncertainty about the monsoon. We have not yet seen the full impact of the unseasonal rains of the last few months. The damage to crops has been extensive in several States and the natural consequence will be some pick up in food prices. Initial reports indicate that rainfall this time will be below normal. The impact on production will depend not only on the quantum of rainfall but also on its distribution over time and across States. Even though agriculture contributes only about 15 per cent to the GDP, any shortfall in agricultural production has serious implications. It fuels inflation and human distress is high as more than 50 per cent of the population depends on agriculture. Second, the several initiatives promised in the Budget will have the desired impact only if they are implemented speedily and effectively. For example, take the increased allocation of funds for railways and roads. Are these ministries adequately prepared to utilise these funds? Some of the initiatives such as the National Investment and Infrastructure Fund and Mudra Bank will take time to be set up and for their impact to be felt.

Role of public investment

The Economic Survey has persuasively argued for larger public investment at a time when private investment is yet to pick up. The same point was made by the Report of the Economic Advisory Council to the Prime Minister in September 2013, that said: "The focused attention that is being given to achieving the production and capacity creation targets in coal, power, road and railways should generate higher growth. In effect, the public sector would act as the driver of growth and crowd in private sector activities". It is to be noted that capital expenditures of the Central government in the Budget are not significant. Capital expenditures are also not synonymous with investment. While capital expenditures in 2015-16 show an increase over the revised estimates of 2014-15, as a proportion of GDP, they remain the same as in the Budget estimate of 2014-15, i.e. at 1.7 per cent of GDP. In fact, the bulk of the investment has to come from public sector institutions such as Coal India and the Indian Railways. What is needed is for the government to come out with a statement regarding the quantum of investment that will be made by the various public sector institutions. This should be monitored every quarter and the actual investments made should be made public. Apart from making the government accountable, this will inspire confidence in investors.

The new initiatives

For raising the growth rate, the government relies on many of the initiatives announced in the Budget. Several of them need clarification and refinement. For example, how will the National Investment in Infrastructure Fund operate? Will it take the form of a trust or a non-banking financial company (NBFC)? The word "trust" was used in the Budget speech. The sooner the details are spelled out, the better it will be. Take another idea, of the Mudra Bank. To call the institution a "bank" will be incorrect if it is only to be a refinancing institution. Which are the last mile finance institutions which will be refinanced by this institution? Apparently, this institution will have to rely totally on Budget allocation. The idea of a refinancing institution is good but, once again, the details need to be spelled out. In fact, in this context, perhaps the best way to promote investment in the large-, medium- and small-scale sector is to go back to the days when we had development banks which provided long-term finance to large, medium and small industries. At the national level, the IDBI (Industrial Development Bank of India of that time) played a major role. At the State level, State finance corporations operated to provide long-term finance to medium and small enterprises. The development banks became universal banks and in that process we have lost out on long-term finance. Even the new initiative of allowing commercial banks to raise infrastructure bonds may not be adequate. Very soon, they will reach the limits of exposure with respect to industries and groups. And, it is also difficult to have firewalls separating short term from long-term credit. While the new ideas promoted in the Budget are welcome, it is time to think in terms of creating long-term finance institutions to provide equity and long-term loans to large and medium industries.

'Stalled' projects and consensus

The easiest way to achieve higher growth in the short run is to ensure that the projects that are under way are completed in time so that output will flow out of them. India's investment rate as a proportion of GDP has come down from the peak it had reached in 2007-08. Nevertheless, it is still around 32 per cent. In normal circumstances, this should have given us a growth of 7.5 to 8 per cent. But the actual growth rate was below it. The decline in output growth is sharper than the decline in investment rate. This may be because of the delay in the completion of projects or a lack of complementary investments. In some cases, it can also be due to non-availability of critical inputs such as coal and power. The Economic Survey has examined in detail the causes behind "stalled" projects. The reasons include not only delay in clearances and permits but also decline in demand and lack of finance. The analysis also shows that clearing the top 100 projects by value will address 83 per cent of the problem of stalled projects. Focussed attention on removing the bottlenecks will give one an immediate pay off.

Strong economic growth is imperative as growth is the answer to many of our socio-economic problems. Prospects for a rise in growth rate in the immediate future appear to be bright. This depends critically on implementing, in a time-bound manner, the various initiatives announced in the Budget. Public investment is directly in the hands of the government. A continuous progress report regarding the performance in this area will go a long way in building up confidence. What is needed is a timetable of action. It is important that non-economic factors are not allowed to derail the process of economic growth. Contentious issues must be avoided and consensus building on key economic issues is very much the need of the hour.

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