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# Economy strengthened by two domestic factors

## What is the issue?

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- India’s real GDP growth hit a road bump in FY17 as growth slowed to 7.2 % y-o-y in the first three quarters. Growth will pick up again to 7.6 % this year.
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- This will be strengthened by two domestic factors **(demographic dividends and higher productivity).**
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## What are the issues that need sorting?

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- India’s working age population will exceed overall population growth for at least two more decades. In turn, this will lead to a **sustained fall in its dependency ratio.**
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- This demographic dividend needs to be harnessed effectively, through higher labour absorption and job creation.
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- India’s labour force is presently highly fragmented and concentrated in the unorganised sector.
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- Hence labour issues need to be addressed on three counts:\n
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    - Growth needs to be inclusive and generate sufficient employment; the employment elasticity to growth has been receding in recent years;
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    - The workforce needs to be skilled; and
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    - A high proportion of casual/informal labour needs to be covered by

employment rules and regulations.
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- If tapped effectively, faster growth in India’s working age population will crucially to the overall GDP growth.
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## What are the productivity prospects?

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- Firstly, India’s **incremental capital output ratio (ICOR)** has eased to 4.0 in the first three quarters of FY16-17 from 6.3 in FY12-13. Part of this decline can be attributed to an easing investment-to-GDP ratio.
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- Secondly, **labour productivity has been softening.** Labour productivity per person employed eased from 10 % in 2010 to 4.8 % in 2016, according to the US Conference Board estimates.
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- Slower productivity and thereby slower output and incomes have kept per capita GDP at depressed levels for a long time.
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- Part of this dip was attributed to better efficiency brought about by technology and innovation.
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- Hence, there is sufficient headroom for productivity levels to improve and raise growth levels.
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## What were the reforms undertaken?

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These productivity gains are expected to get another shot in the arm from ongoing and upcoming reforms like.

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- The **execution of labour reforms** and land acquisition has been pushed to State governments, but changes here are expected to be gradual.
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- The operating architecture will be tightened by rationalising the number of documentation/clearances, simplifying the legal framework, lowering the number of institutions, etc.,
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- **FDI will be encouraged** by lifting sectoral caps, beefing up infrastructure capacity and improving the ease of doing business.
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- To improve the rollout of FDI, the Cabinet will phase out the Foreign Investment Promotion Board (FIPB) from April 2017.
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- In return for a strong consumption-driven market, foreign investments will bridge part of the funding gap for infrastructure projects and provide technological know-how to expand the domestic manufacturing base.
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- **Simplifying the taxation structure** is the next priority, with the rollout of GST in July 2017 under close watch.
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- The GST system's long-term benefits include better transparency, higher revenue generation, a wider tax base, collection efficiency, formalisation of the economy and limiting tax evasion/corruption.
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- Plans to increase use of technology and digitalisation across sectors including banking services, healthcare, education, start-ups etc.,
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- **Expanding the manufacturing base,** this will be positive for job creation given its better absorption levels.
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- Promoting social sector programmes like financial inclusion and direct benefit transfers which will help plug leakages.
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- Formalising the economy and encouraging the scaling-up of manufacturing activity (smaller unorganised sector).
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- **Addressing corruption/lower tax evasion** with closer scrutiny on deposits after the banknote ban, income declaration schemes, the Benami Property Act, plugging tax loopholes through changes to the double taxation agreements, amongst others.
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- On a positive note, these changes are taking place at a favourable time in India when inflation is benign amidst a narrower current account deficit, rising foreign reserves, credible fiscal consolidation efforts, and bullish domestic markets.
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**Source: Business Line**

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