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## Growth Prospects

### What is the issue?

- Global growth prospects for 2020 have been projected by many multilateral institutions and rating agencies including that for India.
- India's growth in the first quarter of 2020-21 at (-) 23.9% showed one of the highest contractions globally.

### What are the forecasts for India?

- The 2020-21 real GDP growth is forecast in the range of (-) 5.8% (the RBI's Survey of Professional Forecasters) to (-) 14.8% (Goldman Sachs).
- The annual projections indicate a strong likelihood of the nominal GDP growth showing a contraction for 2020-21.

### What does the latest data reveal?

- The latest data of the Ministry of Statistics indicate a Consumer Price Index (CPI) inflation rate of 6.7% for August 2020.
- Average CPI inflation during the first 5 months of 2020-21 is estimated at 6.6%.
- Given the injection of periodic liquidity into the system and the inflation trends, the year as a whole may show 7% CPI inflation.
- The contraction in nominal GDP would be -5.0% for 2020-21.

### Why did some feel that the economy might not do too badly?

- There was a demand for health, relief and revival expenditures.
- Some thought that the key sectors such as agriculture and related sectors, public administration, defence services and others may have performed normally.
- Some had even expected that a small positive growth might be possible.
- The national income figures for Quarter I of 2020-21 hold no such hope.
- There was no fiscal stimulus.
- Independent estimates show that States' capital spending fell by 43.5%
- The worsening of the fiscal deficit appears to be because of **decline in**

**revenue** than increase in expenditure.

### Why would revenue contract?

- The policy challenge for the remaining part of the fiscal year is to **minimise the sharp contraction** in real and nominal growth.
- A sharp contraction in nominal GDP growth has adverse implications for the prospects of central and State tax revenues, which may both contract.
- The revenue calculations of the Budget were made on the assumption that the nominal income of the country would grow at 10%.
- With the prospect of a contraction in nominal growth, the Centre's tax revenues would show a huge shortfall as compared to the budgeted amounts.
- The combined fiscal deficit of the Centre and the States will have to make up for the shortfall in tax and non-tax revenues.

### Why fiscal deficit needs to be increased?

- The central government should maintain the level of budgeted expenditure and also provide for additional stimulus.
- For this, its fiscal deficit may have to be increased to close to an estimated 8.8% of GDP.
- If one adds the Centre's and States' fiscal deficit, the combined fiscal deficit amounts to 13.8% of GDP.
- If the nominal GDP actually contracts in 2020-21, the fiscal deficit as the percent of GDP would go up further.
- This does not take into account any additionality to borrowing because of the Goods and Services Tax (GST) compensation.
- The Centre's fiscal during the first four months of 2020-21 as a per cent of annual budgeted target was at 103.1%.

### How high can fiscal deficit go?

- The International Monetary Fund, in its 2020 World Economic Outlook, estimated the fiscal deficit of India and China at 12.1% of GDP.
- All the other countries except the United States and a few others have a deficit lower than this.
- There are not adequate resources to support India's fiscal deficit of nearly 14% of GDP.
- This will require support from the RBI which will have to take on itself, either directly or indirectly, a part of the central government debt.

### What could RBI do?

- **Direct mode** - The RBI can take on the debt directly from government at an

agreed rate.

- It took India long to move away from the automatic monetisation of debt. It happened in the early 1990s.
- Even if the RBI wants to support the borrowing programmes, it should not do so directly.
- **Indirect mode** - The indirect method, which is not new, is preferable as the market still sends out the signals on interest rate.
- The question ultimately relates to the extent of debt monetisation that may be undertaken.
- The country has also to guard against high inflation.

### What could be done?

- The economic situation warrants enhanced government expenditure.
- The fiscal deficit will go well beyond the mandated level. This has to be accepted.
- The best course of action would be to keep the **combined fiscal deficit** at around 14% of GDP in the current year and find ways to finance it.
- This will have to be brought down gradually.
- It may take several years of normalisation.

Source: The Hindu



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