Addressing the Investment Hesitancy

What is the issue?

- Over the past few years, the government has tried unsuccessfully to get the private sector to invest, even acceding to its demands and offering incentives.
- Yet, the Indian private sector has refused to increase investments in additional brownfield or greenfield capacity; here is why.

How is the current private sector investments?

- Private sector investment has not completely evaporated but has been dropping continuously over the past 5-6 years.
- The 2020-21 Economic Survey shows that gross fixed capital formation in the private sector never really recovered from its peak of 27.2% of GDP in 2011-12.
- Thereafter, it hovered at 21-22% every year from 2015-16 to 2018-19, the last year for which the survey has capital-formation data.
- During this period, though, GDP has more than doubled.

What has been the policy response?

- The government has gone to some lengths to meet India Inc's long-standing demands.
- **Interest rates** - For the longest time, industry has been demanding for lower interest rates.
- The government thus made its influence to work on RBI and push interest rates to a historic low.
- Even former RBI governor Urjit Patel was not spared when he raised interest rates or tightened insolvency laws to punish loan defaulters.
- His successor Shaktikanta Das cut RBI's benchmark repo rate of interest by 2.5 percentage points between February 2019 and May 2020.
- While this has failed to make large scale impact, it did help many large corporate debtors lower their interest outgo.
- **Corporate tax rate** - High corporate tax rates were cited as another impediment, though the reality is different.
- According to annual budget documents, the average statutory rate was 34.58% in 2018-19, against 34.6% in 2017-18.

- The average rate is based on the weighted average of corporate tax rates for a particular income bracket and the number of companies in that cohort.
- But, more importantly, the effective tax rate, after availing concessions and exemptions, works out to 27.81%, against 29.49% the previous year.
- These rates—both statutory and effective—are expected to drop further.
- This is because corporate tax rates were slashed twice thereafter, the last time in the budget for 2021-22.
- But falling tax rates have failed to enthuse corporate India.

What are the key reasons for India Inc's unresponsive attitude?

- One, corporate India has actually used the opportunity to compensate itself through higher salaries, dividends and share buybacks.
- Chief executive salaries in BSE500 companies grew by 72% during 2013-18, while profits grew by only 56%.
- The second reason is the government's sustained fondness for arbitrary decisions - demonetization, an unplanned lockdown, vaccine policy.
- Without stakeholder consensus or administrative feedback, these decisions have ended up hurting rather than helping.
- Third, as a direct consequence, these decisions have adversely affected jobs and income.
- It has left many companies nursing unutilized capacity.
- RBI survey data shows that corporate capacity utilization has crossed 75% in only one quarter since January 2014.
- So, unless demand picks up, companies are unlikely to resume investing.

What is the way forward?

- Budget 2021-22 made additional outlays for infrastructure, in the hope that this will induce private investment.
- But, the COVID second wave has wrecked chances of demand resumption in the short term.
- The infrastructure budget should thus be used to aggressively ramp up public health infrastructure.
- The Centre must not rely on the private sector to deliver the goods.
- As recent experience has shown, the private sector can be a component of the government's healthcare network. It cannot become the primary caregiver, given its inherent limitations.

Source: Livemint