Ease of Doing Business Index

What is the issue?

- There is news of continuing improvement in India's ranking according to the World Bank's 'Ease-of-doing-business' Index.
- This comes in handy for a government otherwise beleaguered by seemingly endless bad news on the economic front.

What was the government's reaction?

- The Finance Minister was quick to express both satisfaction and a determination to take India into the top 50 countries in the index.
- India is now pegged at the rank 63 among the 190 countries ranked according to this index.
- In a country where economic policy has for long remained impervious to the challenges faced by its smaller businessmen, any real attention their condition gets is to be welcomed.

Why the self-employed should be enabled?

- The scale of the problem is better understood if we recognise that by far the **largest number of working Indians is self-employed**.
- Among them are our carpenters and service providers, and neither the grand industrial policy statements of the Nehru era nor Modi's 'Make in India' programme have realised that they need to be enabled too.
- **Concerns** - There are concerns with the ease of doing business in India.
    1. The World Bank's perception is overly based on the regulatory regime without adequate attention to infrastructure.
    2. It has an embarrassingly narrow in its coverage, being confined to Delhi and Mumbai.
- **Dependence** - Having said the ease of doing business is important, it needs to be emphasised that a business cannot flourish on its own.
- Its fortunes are tied to the health of the economy within which it is embedded.

- Without the aggregate demand, neither the benignness of the regulatory environment nor the entrepreneurial capability of businessmen can make much of a difference to their fortunes.
- It would today be a mistake if our economic policymakers spend all their

energy on improving the ease of doing business while ignoring the state of aggregate demand in the economy.

Why ‘aggregate demand’ is important?

- **India’s rank improved** in the ease of doing business index from 142 in 2014 to 77 in the report for 2019, and 63 for 2020.
- However, this has **done little for private investment**, which, when measured as share of GDP, has remained unchanged since 2014.
- The recent surge in India’s ranking on the index has come at a time of a distinct slowing of growth.
- It appears that it would be unwise to judge the state of the economy by observing movements in the ease of doing business index.
- That the Indian economy is facing an aggregate demand slowdown is indicated by the fact that aggregate investment, as a share of GDP, peaked in 2011. Now, it is about 10% lower.
- There have been exhortations to the government to resort to deficit spending.
- This exhortation itself is a useful counter to the government’s self-righteous adherence to pre-set fiscal deficit targets.
- However, some familiarity with the experience of the last fiscal stimulus undertaken in India would be useful in the context.

What is the impact of fiscal stimulus?

- During 2008-09, in the wake of the global economic crisis, the fiscal deficit was hiked from 2.5% to 6% of GDP, rising further in the next year.
- Such high increases have been rare, if at all, in India.
- As a result, we didn’t encounter the steep decline in growth observed in parts of the western hemisphere.
- However, as soon as the deficit was taken back to levels dictated by the Fiscal Responsibility and Budget Management Act, 2003, the growth rate declined compared to what it had been before the fiscal stimulus.
- The composition of the public spending matters for growth; increases in the fiscal deficit that take the form of a rise in public consumption rather than public capital formation can have only a temporary effect.
- In the two years of an exploding fiscal deficit in 2008 and 2009, public capital formation increased little.
- Had the unusually high increase in the deficit gone entirely to capital formation, it would have both increased aggregate demand and raised the potential supply of the economy.
- Its growth impact would have lasted much longer.

What are the reasons for a slowdown?

- A slowing of aggregate demand growth can take more than one form.
- In the textbook view, it is part of the investment cycle, and deficit spending can take the economy out of it.
- But what we may be witnessing right now could be a demand slowing with Indian characteristics.
- This is so as the greater part of the population is located in a very slow-growing agricultural sector, putting a brake on consumption growth.
- The grimness of the situation is summed up by the dual feature that around 70% of the population is rural and in half the years of the decade since 2008, we have had zero or negative growth in agriculture.
- Now, as the income distribution shifts away from the overwhelming majority of the population, aggregate demand growth slows.
- There is a likelihood of an income-distributional shift having taken place.
- The recent corporate tax cut could feed a private investment surge but it could also add up to the ongoing shift in income distribution, further lowering aggregate demand.
- When faced with an aggregate-demand growth slowdown an active macroeconomic policy is needed.
- Of **monetary policy,** it seems we are **doomed** to see a change too little too late after years of the Reserve Bank of India having nursed a high-interest rate regime.
- **Fiscal policy** alone holds some **promise** but calibration would be necessary for its use.
- **Spending must focus on the rural sector** to raise agricultural yields and build the infrastructure needed to support non-farm livelihoods so that pressure on the land can be reduced.
- This will also expand aggregate demand. Now the government needs to be pro-active as a business cannot go it alone.

Source: The Hindu