Understanding India’s GDP Fall

What is the issue?

- In the latest estimates of economic growth (for the financial year that ended in March 2021), India’s Gross Domestic Product (GDP) contracted by 7.3% in 2020-21.
- It is imperative, in this context, to understand the reasons for this contraction in GDP.

How could this be approached?

- There are two ways to view this contraction in GDP:

1. To look at this as an outlier - India, like most other countries, is facing a once-in-a-century pandemic
2. To look at what has been happening to the Indian economy over the last decade, and more precisely over the last 7 years

- Notably, between the early 1990s until the pandemic hit the country, India grew at an average of around 7% every year.
- So, the latest GDP data suggests that India’s economy had been steadily worsening during the current regime even before the Covid-19 pandemic.
- The “fundamentals of the economy” (a bunch of economy-wide variables showing an economy’s health) suggest this, as discussed below.

How has the GDP been?

- The GDP growth rate has been a point of growing weakness for the last 5 of these 7 years.
- After the decline in the wake of the Global Financial Crisis, the Indian economy started its recovery in March 2013.
- This recovery turned into a deceleration of growth since the third quarter (October to December) of 2016-17.
- While RBI does not state it, the demonetisation move and the hastily implemented GST impacted the economy (already struggling with bad loans in the banking system).
- Consequently, the GDP growth rate steadily fell from over 8% in FY17 to about 4% in FY20, just before Covid-19 hit the country.

- In January 2020, the GDP growth fell to a 42-year low (in terms of nominal GDP).

What is the GDP per capita level?

- GDP per capita is the total GDP divided by the total population.
- It is used to better understand how well-placed an average person is in an economy.
- From 2016-17, India's GDP per capita started decreasing.
- As a result, India has been losing out to other countries.
- Even Bangladesh has overtaken India in per-capita-GDP terms.

How has unemployment rate traversed?

- Between 2012 and 2018, the total number of employed people fell by 9 million.
- This is the first such instance of total employment declining in independent India's history.
- India started routinely witnessing unemployment rates close to 6%-7% in the years leading up to Covid-19.
- This is against the norm of an unemployment rate of 2%-3%.
- More worrying is the fact that unemployment rate is falling even when the labour force participation rate has been falling.
- With weak growth prospects, unemployment is likely to be the biggest challenge in the coming years.

How about inflation rate?

- In the first 3 years, the current government greatly benefited from very low crude oil prices.
- Oil prices (India basket) stayed close to the $110-a-barrel mark throughout 2011 to 2014.
- It then fell rapidly to just $85 in 2015, coming to below (or around) $50 in 2017 and 2018.
- The sudden, sharp fall in oil prices allowed the government to completely deal with the high retail inflation in the country.
- But since the last quarter of 2019, India has been facing persistently high retail inflation.
- Even the demand destruction due to lockdowns induced by Covid-19 in 2020 could not extinguish the inflationary surge.
- Going forward, inflation is a big worry for India.

What about fiscal deficit?

- Fiscal deficit too is a concern.
- In the Union Budget 2021, the government conceded that it had been underreporting the fiscal deficit by almost 2% of India's GDP.
- Even before Covid-19, it was an open secret that the fiscal deficit was far more than what the government publicly stated.

How strong is the Rupee as against the Dollar?

- A US dollar was worth Rs 59 in 2014. Seven years later, it is closer to Rs 73.
- The relative weakness of the rupee reflects the reduced purchasing power of the Indian currency.

What is the outlook on growth?

- The biggest engine for growth in India is the expenditure by common people in their private capacity.
- This "demand" for goods accounts for 55% of all GDP.
- The per capita level of private consumption expenditure has fallen to levels last seen in 2016-17.
- This means if the government does not help, India's GDP may not revert to the pre-Covid trajectory for several years to come.

Source: The Indian Express