ISAS Brief

No. 412 – 29 March 2016

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Outlook for India's Economy 2016

The paper outlines the positives and concerns on the macro-economic front in India in the light of the Central Government's recent Budget for 2016-2017.

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The excitement surrounding the Indian Budget has subsided. The summary of all the comments appears to be that, while the budget numbers appear achievable, there is not enough content in the programme announcements. In agriculture, irrigation, rural employment, health and education, the numbers do not support the announcements, and so it would be business as usual for these sectors.

Against this backdrop, it would be interesting to look at the expectations for the Indian economy for 2016.

First, the budget has made significant allocations for infrastructure, especially in roads and ports as well as railways. It is interesting that the three ministries/ministers that have shown some significant performance in the last two years have had their departments rewarded with adequate allocations. This is true for the power sector as well, where the programme to shift distribution companies' debts to an off-budget funding mechanism would revitalise these entities. Summer this year is expected to be particularly hot, and temperatures in March are

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reaching their all-time highs in many parts of the country. Demand for power is growing rapidly, and is improving the output from generating stations. Coal consumption has gone up by over 10% in March, and freight movement of coal is also on the rise. Several last-mile projects in the power sector, pending for demand-and-purchase agreements, are likely to see completion in the next few months. Iron ore prices have also firmed up, and there is movement in the steel industry. There have been some mergers and acquisitions, and some debt restructuring; production is on the rise. The combined effect of the increase in power generation, railway freight traffic and increased activity in the roads-sector is likely to impact the growth prospects positively in the coming months.

Second, the budget has wisely distanced itself from the debt burden of the banks, asking them to sort it out themselves. Actions for recovery, for write-down and for restructuring are going on at a frenetic pace in all the nationalised banks, and the balance-sheet problem would be under control by the end of June. Fresh credit expansion would then be possible, and there are a number of opportunities that have been provided by the budget. These include start-ups, and several new areas where Foreign Direct Investment has been liberalised. Interestingly, the focus is not on large corporate- and big-ticket-lending, but much more or medium-scale industries, Small and Medium Enterprises and new entrepreneurs.

Third, given even an average monsoon, the efforts to provide electronic-markets for agricultural produce, and the initiatives for providing roads in rural areas, is likely to improve trade and commerce in agriculture. The sugar sector has started showing signs of revival. Reduction of price volatility in horticulture and fruits and vegetables are likely to add to consumption-demand.

Fourth, there is definitely a movement in defence procurement and manufacturing. Some off-set production will start this year, and a number of manufacturing initiatives are starting up. This would add to materials demand, including steel and cement and special materials and engineering goods.

Finally, wholesale inflation and consumer price inflation appear to be within the Reserve Bank of India’s (RBI’s) target figures for the first time in several years.

The improved performance of corporate balance-sheets has been more due to lower input costs than higher top-lines. This is a cause for worry. Unless there is a strong consumption growth, especially in tier-two and tier-three cities, any increase in input costs will impact these balance-sheets. The future of oil prices is still unpredictable; but the expectations that below US$ 50 prices will hold for this year would help companies sustain their profitability. This is an exogenous variable, and a cause for concern. It remains to be seen whether the 'Make in India' initiatives will have any real impact in the coming year.

Against these positives, there are areas for worry. The first of these is commodity prices, including oil, coal and iron ore. Any sharp increases in commodity prices would affect this delicate balance of price stability. Another round of inflationary pressures is likely to affect growth negatively. The second is that growth is happening without adequate additions to employment opportunities. The recent agitations in different parts of the country for job reservations are an outlet for frustrations caused by lack of employment opportunities. There appear to be no policy signals to address this. Third, by giving away a substantial portion of revenues and programmes to the sub-national State governments, the Central Government has reduced its ability to leverage the economy and economic activity. With the revenues amounting to under 10% of GDP, and interest payments at 3% of GDP, the funds available for economic intervention are getting limited. The only solution is to improve the tax-GDP ratios by getting more people to pay tax, rather than increasing tax rates.

Exports are driven by expectations of the external environment. Growth in the United States is steady, and European Union region would clock a 2.6% growth this year, the same as last year. Brazil, Russia, Argentina, Nigeria and several of the emerging economies are facing difficulties. China's growth has faltered, but there are indications that things are stabilising there, and commodity traffic is gradually on the increase. Increased protectionism is being managed though exchange-rate controls – a tendency that the RBI Governor has warned against. He has repeatedly said that the tendency towards protectionism through exchange-rate manipulation would result in pushing weaker-currency countries into economic difficulty. Actions of the central banks of the US, EU and China would determine the growth path of the global economy.

In sum, there are sufficient opportunities for wholesome and steady growth of the Indian economy this year, and the next quarter would reveal whether India is firmly on this path.